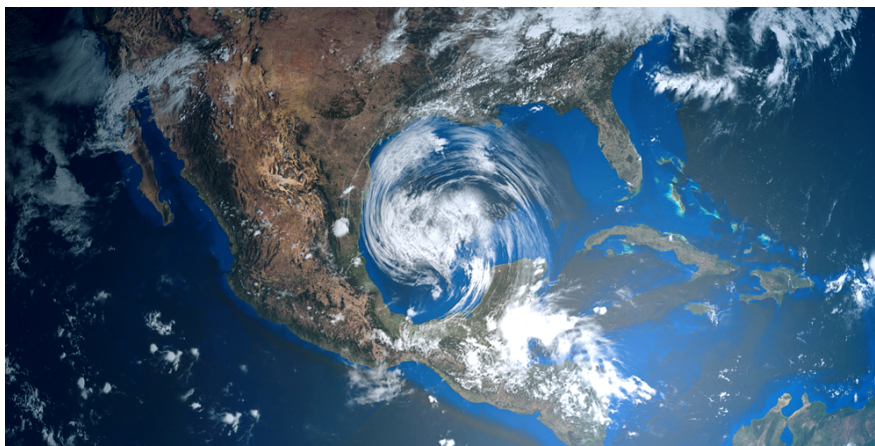


Storm chasing - what does Dorian mean for markets?

Ignoring the ongoing trade war saga, Brexit debacle and the weekend's clashes in HK SAR, today I turn my focus to the natural world, and what it can mean for financial markets.



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Nervous traveller

Just five days before I board a plane for the US, I'm anxiously watching news about Hurricane Dorian, currently battering the Bahamas. This category 5 hurricane, with its estimated 180mph winds, could affect much of the Eastern Seaboard. I'm expecting a bumpy flight, even on Friday. One of the features of this hurricane is that it is very slow-moving. That enables it to straddle land and sea for longer, doing a lot more damage than it might do otherwise if it quickly moved inland and lost its power source of warm seas.

The Hurricane will inevitably be totted up by the bean-counters at some stage. Wikipedia very helpfully has a list of the most costly Atlantic Hurricane's, with Hurricane Katrina in top place (\$125bn), along with a more recent Hurricane Harvey (2017 and only a category 4 Hurricane - also \$125bn, though I have to say I don't remember that one). Investopedia has a similar list, though the numbers differ. The orders of magnitude are roughly the same though - in excess of a hundred billion dollars.

The Three R's

What if any economic consequences does this have? The answer to this is tricky, and not at all intuitive. Hurricanes are hugely disruptive whilst they endure, and for some time after, given the damage to infrastructure and dislocation of workforce who flee to safer areas. But in the months that follow, the received wisdom is that the three R's of repair, replacement and rebuilding, can provide a boost to activity and GDP growth that can outweigh the initial disruption.

[This report by the New York Fed is interesting though](#), as it cites longer-term negative consequences of such disasters, which it shows can last decades after an event such as Katrina.

But the traditional theory of such events runs along lines like this: If an economy's capital stock is its balance sheet, then a Hurricane causes a big loss, but its GDP is more like its profit and loss, and that can take a boost. In any event, the net effect on financial markets is not clear.

Financial Market response

[I found this quite interesting study by Cambridge University online this morning](#) in a quick search. It is probably worth a longer read. That said, it concentrates more on the sort of "Super-catastrophe" scenarios that this hurricane hopefully won't be.

Most of the studies I found online this morning in a five-minute search tended to focus on the stock market, which typically responds negatively to the cash-flow disruption of such events. Commodity markets often are positively affected - supply channels, especially of oil from the Mexican Gulf can lead to shortages and price spikes. But the bond market, which is rarely if ever mentioned, will in my opinion, most likely rally (the Cambridge paper talks about rating downgrades, but it is looking at entirely a different league of disaster).

As for the currency, Fed and short term rates...using Katrina as a benchmark, the Fed tends not to react to events like this, at least not through monetary policy, though it does provide liquidity assistance to regional banks affected by the disaster.

Back in 2005, the Fed was in hiking mode and had already hiked rates twice that year, hiking on a quarterly schedule to coincide with its press briefing meetings. Katrina formed on August 23 and dissipated by August 31, the Fed hiked rates again in September at their next meeting, though there was a longer than usual pause before their next hike in January the following year. There is some evidence that the USD lost some ground in the period during the hurricane and immediately afterward, though it rapidly made it back.

This may not be an appropriate yardstick for a Fed in easing mode, though. I imagine that markets will view this as an excuse to take an already dovish Fed over the line at this month's meeting.

Day ahead:

After that refreshing break from commenting on the trade war, Brexit or the HK SAR unrest, what does today bring?

Well before we look at that, let's start with a quick look at events breaking late last week and over the weekend: Starting with India's GDP. [Check out Think for a more considered piece by Prakash](#). But the short story here is that the 5.0%YoY release was substantially at the low end of expectations and very disappointing given the degree of stimulus the economy has already had.

We have a further 50bp of easing penciled in for the RBU for the rest of the year. We should maybe ink it in now.

Also, (from Iris Pang) "As the new US tariffs kick in (came in yesterday on September 1), we expect that China's Caixin manufacturing PMI will stay below 50 for another month in September even though there will be more infrastructure projects in place. The official manufacturing PMI fell to 49.5 in August from 49.7 a month earlier, showing that contraction in manufacturing activities continued. The details showed that both export orders and domestic orders continued to stay below 50. The sub-index of production was 51.9, which is likely the result of infrastructure projects entering their production phase.

This should continue to give some support to the overall manufacturing PMI in the coming months. But we have to keep in mind that this growth came from fiscal stimulus. It is not the result of regular manufacturing activity, which will be hit by another wave of tariffs starting from 1st September".

Today sees plenty more PMIs across the region, most of which look to dip a little further into the red, though there is an increase in the Korean PMI, possibly reflecting what we believe might be an emerging trough in the semiconductor industry. Though this economy still has substantial problems.

Thai CPI today is of no particular market interest, as they don't really have any inflation. Indonesian inflation is more relevant given the recent swing of Governor Warjiyo from talking the dovish talk to walking the dovish walk with their recent rate cut (August 22 25bp cut of 7-Day reverse repo rate to 5.5%).

Author

Alissa Lefebre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Sector Economist, TMT & Healthcare

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist
samuel.abettan@ing.com

Franziska Biehl
Senior Economist, Germany
Franziska.Marie.Biehl@ing.de

Rebecca Byrne
Senior Editor and Supervisory Analyst
rebecca.byrne@ing.com

Mirjam Bani
Sector Economist, Commercial Real Estate & Public Sector (Netherlands)
mirjam.bani@ing.com

Timothy Rahill
Credit Strategist
timothy.rahill@ing.com

Leszek Kasek
Senior Economist, Poland
leszek.kasek@ing.pl

Oleksiy Soroka, CFA
Senior High Yield Credit Strategist
oleksiy.soroka@ing.com

Antoine Bouvet
Head of European Rates Strategy
antoine.bouvet@ing.com

Jeroen van den Broek
Global Head of Sector Research
jeroen.van.den.broek@ing.com

Edse Dantuma
Senior Sector Economist, Industry and Healthcare
edse.dantuma@ing.com

Francesco Pesole
FX Strategist
francesco.pesole@ing.com

Rico Luman
Senior Sector Economist, Transport and Logistics
Rico.Luman@ing.com

Jurjen Witteveen

Sector Economist
jurjen.witteveen@ing.com

Dmitry Dolgin
Chief Economist, CIS
dmitry.dolgin@ing.de

Nicholas Mapa
Senior Economist, Philippines
nicholas.antonio.mapa@asia.ing.com

Egor Fedorov
Senior Credit Analyst
egor.fedorov@ing.com

Sebastian Franke
Consumer Economist
sebastian.franke@ing.de

Gerben Hieminga
Senior Sector Economist, Energy
gerben.hieminga@ing.com

Nadège Tillier
Head of Corporates Sector Strategy
nadege.tillier@ing.com

Charlotte de Montpellier
Senior Economist, France and Switzerland
charlotte.de.montpellier@ing.com

Laura Straeter
Behavioural Scientist
+31(0)611172684
laura.Straeter@ing.com

Valentin Tataru
Chief Economist, Romania
valentin.tataru@ing.com

James Smith
Developed Markets Economist, UK
james.smith@ing.com

Suvi Platerink Kosonen
Senior Sector Strategist, Financials
suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios

maarten.leen@ing.com

Maureen Schuller

Head of Financials Sector Strategy

Maureen.Schuller@ing.com

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Philippe Ledent

Senior Economist, Belgium, Luxembourg

philippe.ledent@ing.com

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

Inga Fechner

Senior Economist, Germany, Global Trade

inga.fechner@ing.de

Dimitry Fleming

Senior Data Analyst, Netherlands

Dimitry.Fleming@ing.com

Ciprian Dascalu

Chief Economist, Romania

+40 31 406 8990

ciprian.dascalu@ing.com

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland
Karol.Pogorzelski@ing.pl

Carsten Brzeski
Global Head of Macro
carsten.brzeski@ing.de

Viraj Patel
Foreign Exchange Strategist
+44 20 7767 6405
viraj.patel@ing.com

Owen Thomas
Global Head of Editorial Content
+44 (0) 207 767 5331
owen.thomas@ing.com

Bert Colijn
Chief Economist, Netherlands
bert.colijn@ing.com

Peter Vanden Houte
Chief Economist, Belgium, Luxembourg, Eurozone
peter.vandenhoute@ing.com

Benjamin Schroeder
Senior Rates Strategist
benjamin.schroeder@ing.com

Chris Turner
Global Head of Markets and Regional Head of Research for UK & CEE
chris.turner@ing.com

Gustavo Rangel
Chief Economist, LATAM
+1 646 424 6464
gustavo.rangel@ing.com

Carlo Cocuzzo
Economist, Digital Finance
+44 20 7767 5306
carlo.cocuzzo@ing.com