

Taper tedium - Evergrande still rumbling

It seems like no one in Asia will be all that bothered if the US Fed announces a taper in November, which now looks all but certain. But there is still some residual interest in the Evergrande story with some sort of solution apparently in place for a domestic coupon payment due today. Questions remain over offshore payments...



Fed Chair, Jerome Powell

Fed first

We will start today with a quick look at the Fed decision and move to look at the Evergrande and Asia backdrop a little later. And we begin with [this note by our macro, rates and FX guys](#). The abridged version of the note is:

- No change in rates or asset purchases announced at the latest meeting
- But the strongest possible hint that "taper" will happen in November
- A split dot-plot around the 2022/2023 date
- And a new 2024 plot sitting around 1.75% - on the high side.

So what did markets do in the end? The bond market was not particularly fazed by all this, indicating that this outcome was more or less expected. 2Y yields nosed 2.2bp higher to 0.236%. But the yield on 10Y US Treasury bonds eased lower by the same amount though still just managed to cling on above 1.30%.

It was the FX markets where I think there was a more interesting story. Despite markets generally reacting positively to the FOMC meeting, and both the S&P 500 and Nasdaq equity indices finishing up around 1% on the day, the USD also put in some decent gains. Today's EURUSD rate is about 1.1689, a notable fall from about 1.1730-1.1740 around this same time yesterday - as well as breaching the 1.17 level. We're getting very close to previous lows, and could be setting up a base to test 1.16 if the USD remains bid. And that's where we might need a bit more interest returning to the Evergrande story and a shift towards risk-off again.

Where next for Evergrande?

Markets yesterday took some comfort from an announcement that Evergrande had resolved a domestic coupon payment due today. It's not entirely clear what "resolved" means in this context. And the wording used implies that the domestic coupon will not be fully paid today, whilst giving no indication that it will ultimately be paid in full at some later date. As far as the offshore coupon, USD83.5m is also due on a five-year dollar note today. Missing that payment today would still leave a 30-day grace period before this is registered as a default, and our guess is that Evergrande will make full use of that window to buy time.

What seems to be emerging from all of this is a playbook for the resolution of this episode with re-payments focussed on the domestic investor base. Foreign bonds are already pricing in default with low recovery rates, and although that sounds bad, it is now in the price so perhaps the market has done most of its adjustment already.

Today remains an important day to test market attitudes. It looks at this stage as if the narrative has moved away from Evergrande being a systemic issue, to one where Evergrande is eventually restructured, but where collateral damage will be localised. In this context, the CNH, which was one of the better-performing currencies yesterday in the Asia pack, could show some further resilience today. That said, the Western media continues to chunter on about Lehman's and subprime in a nervy manner, and it feels as if some markets are looking for an excuse to take profits at these levels. So it's not clear that we are out of the woods just yet.

Asia today

We've already had the September 20-day trade figures from South Korea, and they don't look too bad. Export growth is showing a rise of 22.9%YoY, while imports are holding up even better at 38.8%. That does, however, imply some shrinking of the trade surplus if these trends hold for the full month (they probably will), and could put the KRW under some further depreciation pressure (it's already up to 1185 today).

And From Nicky Mapa, "Singapore's August inflation is set for release today. Market participants expect a slight moderation in the headline number to 2.4% (from 2.5%) while core inflation will likely remain steady at 1.0%. Core inflation accelerated to pre-pandemic levels last month due largely to base effects and pricier energy costs reaching the fastest pace recorded during the pandemic. We expect this trend to persist for the August inflation reading. Cost-related price pressures will likely fade towards the end of the year as base effects wane while demand pressures stay soft due to the ongoing pandemic.

Bangko Sentral ng Pilipinas (BSP) meets today. The central bank is widely expected to keep policy settings untouched despite resurgent inflation. Price pressure flared up once more in August as supply chain disruptions caused by Covid and inclement weather pushed food inflation to 6.5%.

BSP Governor, Diokno, is expected to look past the inflation breach as he hopes to provide monetary support for the fledgling economic recovery. We forecast Diokno keeping rates unchanged “for as long as the Philippines is in recovery mode” with the first policy adjustment coming not earlier than mid-2022”.

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