

Asia

Weekly Watch

Hong Kong, June 14, 2010

Economic Analysis

Asia

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Markets

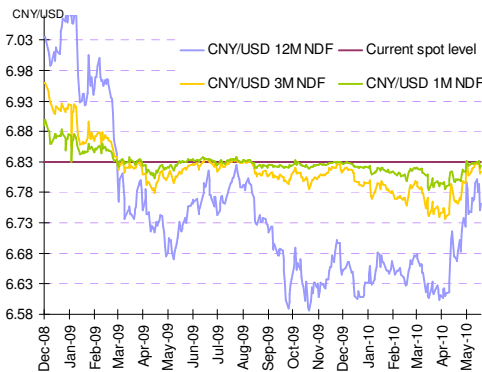
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Sentiment rises on strong regional economic data

A strong set of May economic indicators from China has helped to alleviate concerns of an abrupt slowdown. And while market concerns about spillovers from the European debt crisis persist, sentiment has rebounded for the time being. In particular, strong exports, industrial production, and fixed asset figures helped allay concerns of a hard landing for the Chinese economy. In addition, a rise in China's trade surplus for May has helped to increase expectations once again of a resumption of currency appreciation later this year, in line with our expectations.

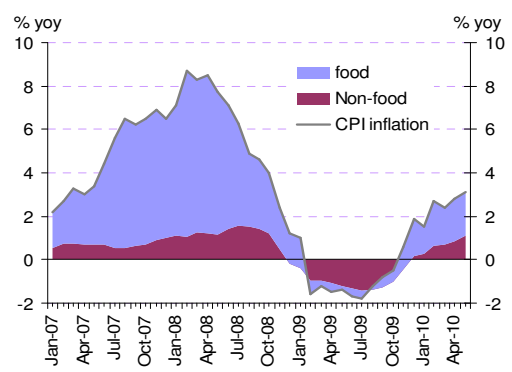
Elsewhere in the region data continues to be strong. In both Australia and Korea, unemployment levels fell significantly in May (to 5.2% in the former, and 3.2% in the latter). Nevertheless, the Bank of Korea again left its policy rate unchanged at its monthly monetary meeting, given low inflation and uncertainties about the global environment; markets, however, anticipate a rate hike may be forthcoming in the next few months. Outside of India and Vietnam, inflation remains subdued (May inflation figures for India will be released in the coming week). In China, CPI inflation for May increased to just above the government's 3% comfort level, but this was widely expected given base effects and the evolution of food prices.

Chart 1
NDFs: Expectations of CNY appreciation have diminished



Source: BBVA Research and Bloomberg

Chart 2
Inflation is rising on higher food prices, but remains under control



Source: BBVA Research and Bloomberg

Highlights

Markets

Highlights

Calendar

Markets Data

China's strong growth continues, with signs of moderation

Korea government remains conservative despite of the improving labor data

Japan expansion continues triggered by overseas demand

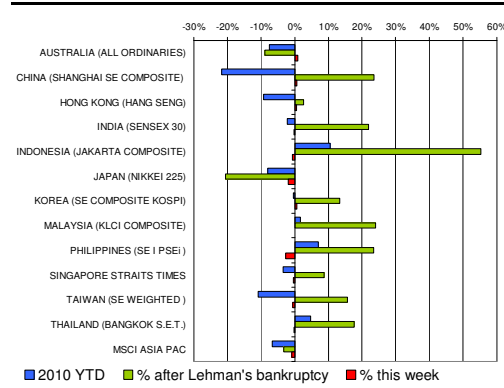
Volatility remains

Asian financial markets remained volatile over the past week, reflecting swings in market sentiment. On Monday (June 7), concerns over Hungary’s sovereign risk and signs of slowing growth in China weighed on market sentiment. Asian currencies and equities tumbled. Since then, sentiment has improved, especially after China’s May data was released, showing strong export and growth figures. Asian currencies rebounded by Friday, erasing losses of earlier in the week. The Australian Dollar surged the most, due to new gains in commodity prices and lower risk aversion. While market sentiment still remains fragile, our positive view on Asian economies and currencies remains intact.

The Korean won was one of the worst performing currencies against the dollar in the past week. In addition to ongoing concerns about relations with the North and uncertainties about the global economic outlook, the won was weighed down by concerns over a plan to limit onshore forward trades by domestic and foreign banks. USD-KRW closed at 1246, down 3.6% from last week. In our view, the impact of the upcoming rules is unlikely to be dramatic as outlines of the plan were floated in advance, and as the authorities are providing time for banks to comply. USD-KRW should continue to strengthen based on fundamentals, i.e., the stronger recovery and the mature conditions for raising rates.

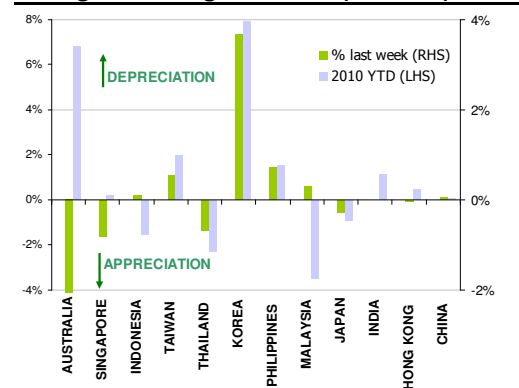
Stock markets remained volatile over the last week. Fears of a spreading European debt crisis and weak US jobs figures added to concerns of an abrupt slowdown in China, dragging down markets across the region on Monday. However, most markets recorded gains the rest of the week on reassurances by the US Fed Chairman that the US economy is on a solid track to recovery. Moreover, China’s monthly data release suggesting that economic growth remains strong and moderating to a more sustainable pace (see the Highlights, below) boosted stock markets late in the week. Despite the late gains, some of the stock markets closed the week in the red.

Chart 3
Stock Markets



Source: BBVA Research

Chart 4
Foreign Exchange Markets (vs. USD)



Source: BBVA Research

Economics Analysis

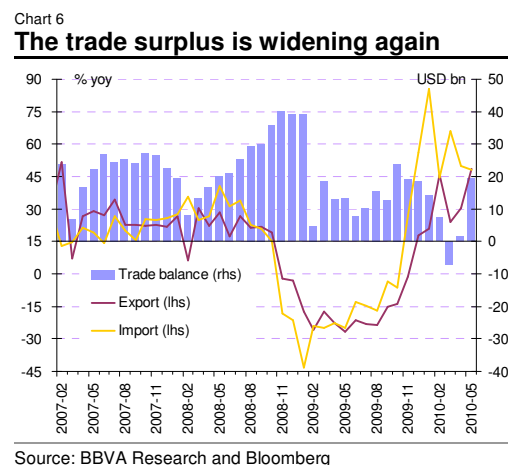
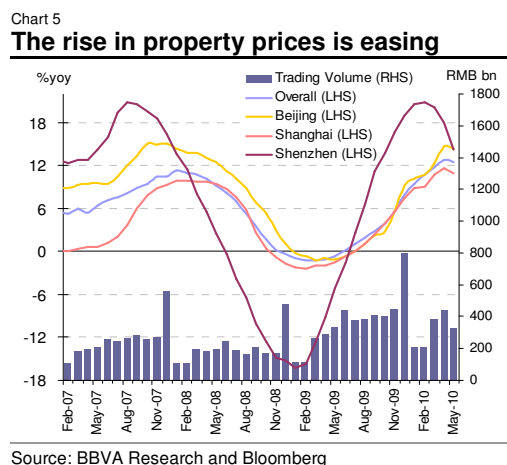
Highlights

China's strong growth continues, with signs of moderation

China's monthly release of economic data for May suggests the economy's strong growth is moderating toward a more sustainable pace, in line with our expectations. The data nevertheless remain strong (in particular exports which were much higher than expected) and should help alleviate concerns of an abrupt slowdown. New loan growth was also somewhat higher than expected (RMB639 billion down from RMB774 billion last month). The former is leading to renewed calls by trading partners for currency appreciation, while the latter highlights the challenges the authorities still face in reining in rapid credit growth to prevent overheating. Slowing M2 and credit growth are in line with the authorities' efforts to tighten policies to prevent overheating.

Inflation rose by 3.1% y/y in May (in line with expectations) due to base effects and food prices. We expect inflation to peak in June and to recede thereafter as monetary and credit growth are reined in (we project end-year inflation of around 3%). We expect further tightening measures during the second half of the year, including currency appreciation, although the timing has been delayed relative to our previous expectations because of uncertainties to the global outlook. Meanwhile, property prices rose by 12.4% y/y in May, down from a record 12.8% y/y April (NDRC data, covering 70 large cities) as the government's recent measures to cool the property sector take effect.

Growth of urban fixed asset investment (25.4% y/y, consensus: 25.7%) and industrial production (16.5%, consensus: 17.0%) remained strong, but moderated from the growth rates of the previous month. Overall, these indicators suggest a gradual slowdown, consistent with our full-year GDP growth projection of 9.8%. The surge in exports (48.5% y/y, consensus: 32.0%) resulted in a wider trade surplus, and renewed calls from the U.S. administration for RMB appreciation.



Korean government remains cautious on withdrawing stimulus, despite strong GDP growth and improving labor data

Korea's economic bounce-back from the global financial crisis has been one of the fastest in the region. After a faster-than-expected Q1 GDP outturn (2.1% QoQ sa) in Q1, the unemployment rate fell sharply in May, to a seasonally adjusted 3.2%. In addition to the contribution of government jobs programs, hiring by the private sector played a role, suggesting that, despite uncertainties to the global outlook, Korea's rebound has become increasingly self-sustaining.

However, European debt woes and volatile financial markets have caused the government and Bank of Korea to stay cautious in withdrawing policy stimulus. In this regard, the BoK again left its benchmark rate unchanged at 2% for a 16th month in a row at its policy meeting last week. Nevertheless, market participants are expecting the BOK to hike rates soon, perhaps within the next few months.

The Korean won came under pressure, meanwhile, on the government's reported plans to introduce restrictions on onshore currency swaps and forwards, designed to reduce currency volatility. Specifics of the plans were announced today, limiting foreign and domestic banks' currency derivatives to 250% of equity capital and to 50% the latter, respectively. In addition, the limit on derivatives to cover corporate settlements will be cut to 100% of the total, from the current 125%.

Japan expansion continues, triggered by overseas demand

Machinery orders, a leading indicator of business investment three to six months ahead, climbed on a seasonally adjusted basis by 4.0% mom (consensus: 1.7%) in April as Japan's export-driven rebound is leading companies to increase investment spending. Meanwhile, the current account surplus rose to USD13.2 billion in April, albeit lower than market expectations of USD14.2 billion, on strong demand from China's and increasing demand from the US. We expect Japan's economic recovery to advance during the rest of the year, with GDP projected to expand by 1.6% yoy in 2010 mainly led by exports, with private consumption remaining weak.

Calendar

AUSTRALIA	Date	Period	Prior	Cons.
Dwelling Starts	18-Jun	1Q	15.10%	--
HONG KONG	Date	Period	Prior	Cons.
Industrial Production (YoY)	14-Jun	1Q	-4.90%	--
Unemployment Rate SA	17-Jun	MAY	4.40%	--
INDIA	Date	Period	Prior	Cons.
Monthly Wholesale Prices YoY%	14-Jun	MAY	9.59%	9.60%
JAPAN	Date	Period	Prior	Cons.
Industrial Production (MoM)	14-Jun	APR F	1.30%	--
Industrial Production YOY%	14-Jun	APR F	31.80%	--
Capacity Utilization (MoM)	14-Jun	APR F	0.60%	--
Tertiary Industry Index (MoM)	16-Jun	APR	-3.00%	2.60%
Machine Tool Orders (YoY)	16-Jun	MAY F	191.80%	--
KOREA	Date	Period	Prior	Cons.
Department Store Sales YoY	18 Jun	MAY	8.80%	--
Discount Store Sales YoY	18 Jun	MAY	0.30%	--
MALAYSIA	Date	Period	Prior	Cons.
CPI YoY	18-Jun	MAY	1.50%	1.60%
PHILIPPINES	Date	Period	Prior	Cons.
Unemployment Rate	15-Jun	APR	7.30%	--
Overseas Remittances (YoY)	16-Jun	APR	5.60%	--
Balance of Payments	17-Jun	MAY	\$982M	--
SINGAPORE	Date	Period	Prior	Cons.
Retail Sales (YoY)	15-Jun	APR	-2.40%	1.00%
Retail Sales (MoM) sa	15-Jun	APR	-1.40%	0.70%
Electronic Exports (YoY)	17-Jun	MAY	19.30%	20.60%
Non-oil Domestic Exports (YoY)	17-Jun	MAY	29.40%	25.10%
Non-oil Domestic Exp SA (MoM)	17-Jun	MAY	2.10%	-1.00%

What to watch

India: Wholesale Price Index for May (June 14th)

Forecast: 9.58

Consensus: 9.60

Previous: 9.59

India is one of Asia's few economies struggling to combat high inflation (Vietnam is another). While probably having peaked, we expect WPI inflation to remain high in May on account of rising food and electricity prices. The authorities have so far responded through two 25bp interest rate hikes last March and April and increases in the required reserve ratios. We expect inflation to moderate to 8.5% by the end of the calendar year as the harvest season leads to lower food prices. A higher than expected WPI outturn, together with recent robust GDP growth (8.6% y/y in January-March) could raise expectations of further interest rate increases at or before the RBI's next policy meeting on July 27.

Japan – BOJ Target Rate (17th June)

We expect interest rate will remain unchanged

Actual **Survey**

0.10% 0.10%

Hong Kong – Composite Interest Rate (21st June)

We expect interest rate will remain unchanged

Actual **Survey**

0.11 % 0.11%

Global Market Data

Table 1

Market data

		Close	Weekly change	Monthly change	Annual change		
Interest rates (changes in bps)	US	3-month Libor rate	0.54	0	10	-9	
		2-yr yield	0.74	2	-8	-52	
		10-yr yield	3.25	5	-28	-54	
	EMU	3-month Euribor rate	0.72	1	4	-55	
		2-yr yield	0.47	-1	-14	-122	
		10-yr yield	2.57	-1	-37	-106	
Exchange rates (changes in %)	Europe	Dollar-Euro	1.208	0.5	-4.0	-13.9	
		Pound-Euro	0.83	0.3	-3.0	-2.2	
		Swiss Franc-Euro	1.39	-0.4	-0.8	-8.0	
	America	Argentina (peso-dollar)	3.92	-0.1	0.6	4.1	
		Brazil (real-dollar)	1.81	-2.0	2.1	-5.6	
		Colombia (peso-dollar)	1926	-2.0	-1.7	-4.5	
		Chile (peso-dollar)	538	-0.3	1.5	-4.3	
		Mexico (peso-dollar)	12.69	-1.6	2.7	-5.4	
		Peru (Nuevo sol-dollar)	2.84	-0.1	0.3	-4.4	
	Asia	Japan (Yen-Dollar)	91.62	-0.2	-1.3	-6.8	
		Korea (KRW-Dollar)	1247.35	1.9	10.3	-0.7	
		Australia (AUD-Dollar)	0.848	2.6	-5.7	4.3	
	Comm. (chg %)	Brent oil (\$/b)	74.8	3.7	-6.7	5.4	
		Gold (\$/ounce)	1226.9	0.6	-0.5	30.6	
		Base metals	473.7	0.9	-3.7	16.1	
Stock markets (changes in %)	Euro	Ibex 35	9559	7.1	-4.2	-1.6	
		EuroStoxx 50	2642	3.4	-4.4	5.3	
		USA (S&P 500)	1082	1.6	-6.5	14.4	
	America	Argentina (Merval)	2260	3.6	-0.9	36.6	
		Brazil (Bovespa)	62964	2.1	-2.8	17.6	
		Colombia (IGBC)	12301	0.6	-0.4	27.2	
		Chile (IGPA)	18374	1.8	1.6	18.9	
		Mexico (CPI)	32149	3.7	-0.6	26.3	
		Peru (General Lima)	14197	2.7	-8.3	2.6	
		Venezuela (IBC)	64321	1.6	3.9	48.3	
		Asia	Nikkei225	9705	-2.0	-8.6	-4.2
	HSI		19872	0.5	-2.7	5.2	
	Credit (changes in bps)	Ind.	Itraxx Main	133	6	35	26
			Itraxx Xover	604	14	142	-76
		Sovereign risk	CDS Germany	39	-10	-6	4
CDS Portugal			290	-62	91	213	
CDS Spain			206	-51	54	110	
CDS USA			38	-3	0	—	
CDS Emerging			286	-8	49	-91	
CDS Argentina			1110	-62	214	-754	
CDS Brazil			141	-5	20	-28	
CDS Colombia			162	-7	17	-45	
CDS Chile			103	-2	15	-21	
CDS Mexico			139	-6	20	-69	
CDS Peru	139	-7	20	-43			

Sources: Bloomberg, Datastream and JP Morgan

Asia Market Data

Table 2

INDEX	Last price	% change over		% Change over 1 Y
		a week	Year to date	
China – Shanghai Comp.	2569.9	0.6	-21.6	-8.1
Hong Kong – Hang Seng	19872.4	0.5	-9.1	5.8
Taiwan – Weighted	7299.5	-0.6	-10.9	11.1
Japan – Nikkei 225	9705.3	-2.0	-8.0	-2.8
Korea – Kospi	1675.3	0.7	-0.4	18.0
India – Sensex 30	17042.3	-0.4	-2.4	10.6
Australia – SPX/ASX 200	4505.5	1.3	-7.5	11.3
Singapore – Strait Times	2796.3	-0.4	-3.5	17.4
Indonesia – Jakarta Comp	2801.9	-0.8	10.6	34.1
Thailand – SET	769.6	-0.3	4.8	22.7
Malaysia – KLCI	1294.7	0.0	1.7	18.9
Philippines – Manila Comp.	3265.4	-2.7	7.0	25.7

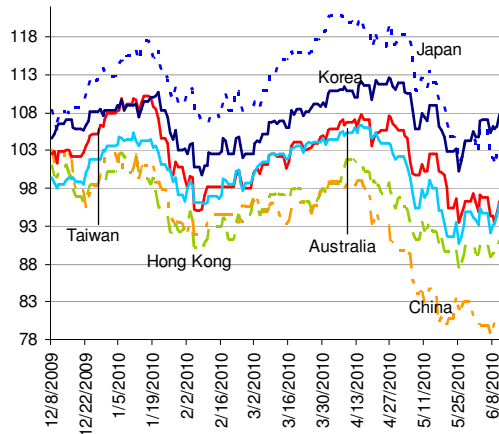
Source: BBVA Research and Bloomberg

Table 3

CURRENCY	Spot	% change over		Forward 3-month	Forward 12-month
		a week	Forward 3-month		
China (CNY/USD)	6.83	-0.06	-0.02	-0.08	
Hong Kong (HKD/USD)	7.79	0.02	-85.7	-312.5	
Taiwan (TWD/USD)	32.4	-0.56	-0.27	-0.88	
Japan (JPY/USD)	91.79	0.23	-13.5	-73.1	
Korea (KRW/USD)	1246	-3.6	3.4	2.85	
India (INR/USD)	46.85	-0.01	41.7	116.6	
Australia (USD/AUD)	0.84	2.9	128.5	n.a.	
Singapore (SGD/USD)	1.40	0.69	-4.9	-21.5	
Indonesia (IDR/USD)	9200	-0.10	137.5	499.2	
Thailand (THB/USD)	32.47	0.62	4.5	15	
Malaysia (MYR/USD)	3.28	-0.29	135	470	
Philippines (PHP/USD)	46.64	-0.73	0.34	1.46	

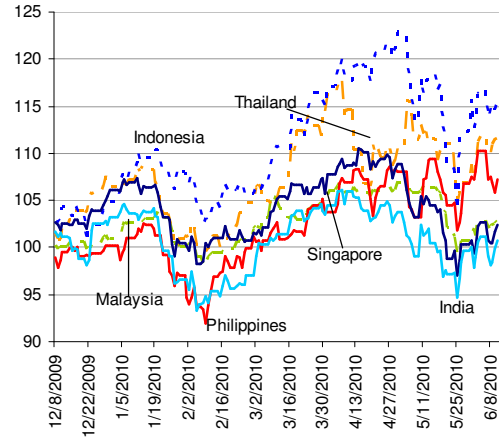
Source: BBVA Research and Bloomberg

STOCK MARKETS



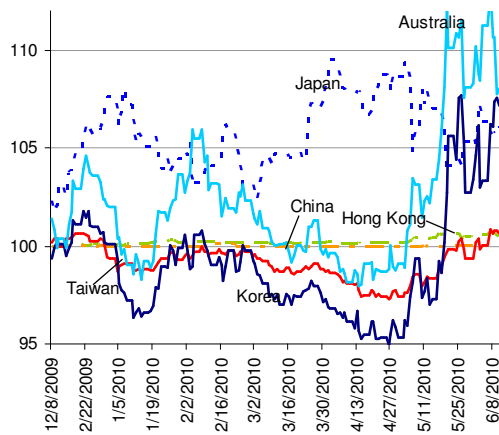
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STOCK MARKETS



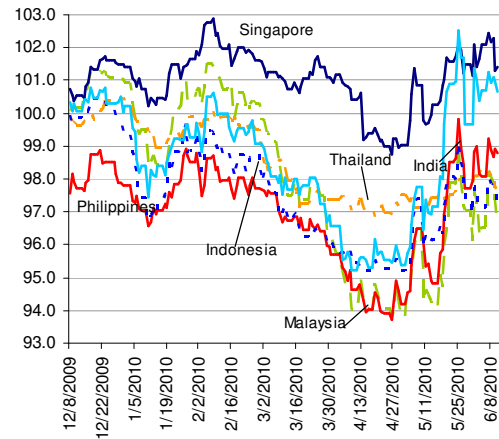
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FOREIGN EXCHANGE MARKETS



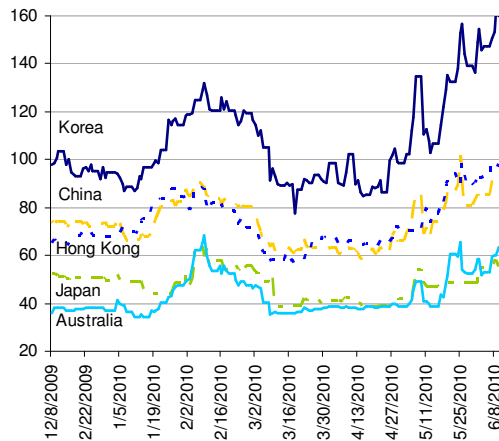
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FOREIGN EXCHANGE MARKETS



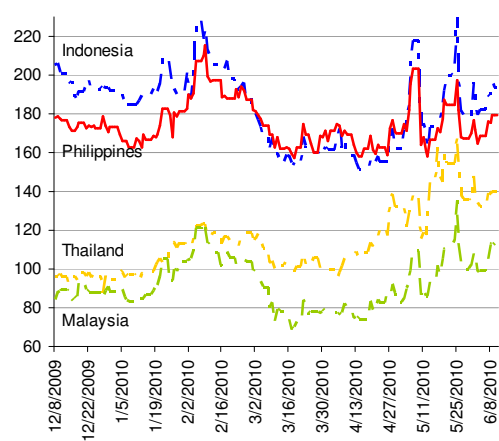
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