BBVA Research

Asia

Weekly Watch

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Economic Analysis

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Positive start for Asian economies in 2011

Asia started the New Year with a set of positive economic data reaffirming strong growth momentum. China's PMI for December registered a strong reading, while indicating a healthy moderation following several months of strengthening momentum that had been generating worries about overheating (see Highlights). The main concern for the region now has shifted to the inflation outlook, with demand pressures adding to existing inflationary trends from food and commodity prices.

Singapore regains growth momentum, while regional inflation ticks up

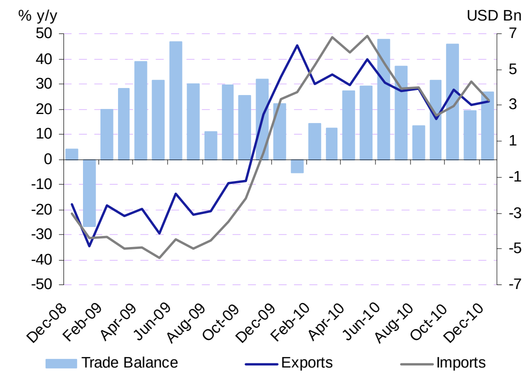
Singapore's advanced Q4 GDP showed renewed growth momentum (see Highlights), which is likely to be reflected in trends elsewhere in the region. For example, Korean exports in December (23.1% y/y) beat expectations (19.4%) (Chart 1). Meanwhile, Indonesia posted higher-than-expected inflation for December (7.0%, consensus: 6.7%), but Bank Indonesia kept interest rates unchanged given stable core inflation (Chart 2). Thai core inflation also increased (1.4% y/y vs. consensus 1.1%), as did Korean headline inflation, to 3.5% y/y (consensus: 3.2%), with the Bank of Korea emphasizing its commitment to containing inflation to within the target range of 2-4% in 2011. Meanwhile, the Philippines became the latest country to receive an outlook upgrade from Moody's, from stable to positive (within Ba3).

In the coming week…

A new batch of monthly data for China, including new loans, trade, FDI, property prices, money growth, and foreign exchange reserves (see What to Watch). Moreover, markets will be watching WPI inflation in India, trade balances in Japan and Australia, and industrial production in Japan, India, Malaysia, and Singapore. On the monetary front, it's a close call whether the Bank of Korea will raise rates (January 13), but on balance we think they will wait until February; we expect Thailand to hike rates by 25bps on January 12.

Chart1

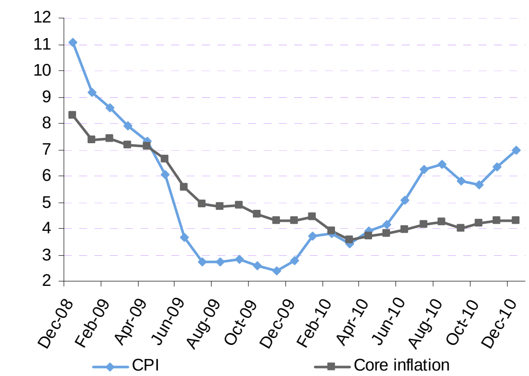
Korean export growth remains strong



Source: BBVA Research and Bloomberg

Chart2

Indonesia's inflation heats up



Source: BBVA Research and Bloomberg

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Highlights

China's PMI suggests a welcome moderation

A moderation in December PMI helps to alleviate overheating concerns

More moves to curb capital inflows

Policymakers implement further macro-prudential measures to stem inflows

Singapore's GDP outperforms in 2010

Q4 advanced GDP estimates showed renewed growth momentum

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Markets

European debt concerns resurface

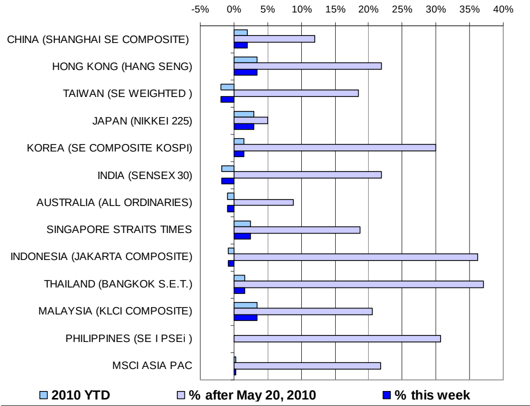
Despite China's pledges to buy Spanish debt, European peripheral yields spiked again under heavy financing needs for next week (Portugal on January 12; Spain and Italy on January 13). The USD strengthened against major currencies as positive statistics on the US labor market exceeded expectations. Asian fx fell against the USD.

In the region, the flooding in Australia has caused massive damage. Our economists think that modest near term inflation trends, combined with the fallout of the catastrophe, is likely to keep the RBA on hold for the next 2-3 months. Regional economic data are positive – Singapore's GDP growth turned positive again in Q4 and Taiwan's and Korea's exports in December also beat expectations. Moody's raised the outlook for the Philippines' credit rating to positive, hinting at an upgrade later this year. On the other hand, food and commodities prices, driven by bad weather and strong emerging market demand, rose further and are pushing Asian inflation rates higher. The rising trend will likely prompt central banks to tighten further in 1H 2011. But the pace will be slowed by perennial concerns of hot money inflows and accompanying appreciation pressure.

Among Asian fx, the AUD was among worst performing currencies this week. Serious flooding in Queensland as well as signs of a cooling housing market reduced expectations of an RBA's rate hike in 1H2011. Meanwhile, the USD rebound triggered a sell-off in commodities, putting more pressure on the AUD. The JPY also depreciated markedly this week on rising US yields. USDJPY stopped below 84 awaiting US non-farm payrolls data tonight. Stronger USD also prompted the Chinese authorities to set the daily USDCNY fixing higher. But the market is still hopeful of a near-term CNY rise ahead of President Hu's visit to the US on Jan 19. The 12-month NDF is relatively stable at 6.46, implying around 2.5% appreciation. In Taiwan, the strength of the TWD remains amidst strong domestic growth and export recoveries. To resist appreciation, the CBC raised the reserve requirement on fx deposits and continued to intervene in the currency market at market open/ close. Its close scrutiny of onshore branch of foreign banks has so far been effective in preventing TWD to appreciate further.

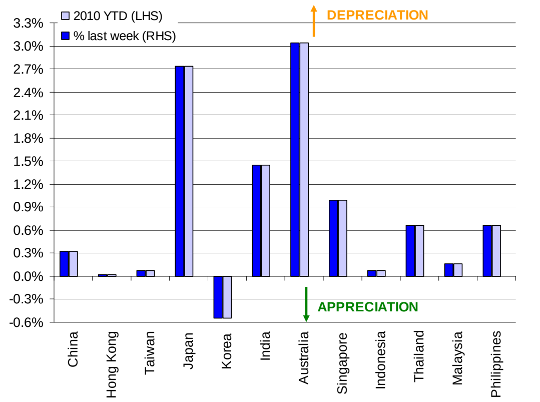
This past week the Asia Pacific Index (MXAP) reached its highest level since June 2008, mainly due to an improvement on the US outlook. However, in the middle of the week some profit-taking movements dragged most of the indicators after a sharp rise over the last two weeks. The Nikkei index was among the best performers, as the USD strengthened against the JPY, bolstering export companies' outlook. Meanwhile, Chinese equities rose after PMI's slowdown suggested that inflation eased last month, and also due to solid corporate reports.

Chart 3
Stock markets



Source: BBVA Research and Bloomberg

Chart 4
Foreign exchange markets



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Highlights

China's PMI outturn suggests a welcome moderation in momentum

Recently released data on China's December Purchasing Managers' Index (PMI) eased, to 53.9% from 55.2% (consensus: 55.0%), following four consecutive months of stronger-than-expected outturns and five straight months of increases. As such, this marked the first key indicator in many months showing that growth trends could be moderating, a welcome relief for concerns about economic overheating. The main contributors to the decline in the official index were the "new orders index" (30% weight) and the "production index" (25% weight), providing some indication that increasingly aggressive tightening measures during the course of 2010—which included 3 reserve requirement and two interest rate hikes since October—may have begun to show up in the forward-looking data components. On the inflation front, the input price index dropped to 66.7% in December (from 73.5% in November), which should help to alleviate rising inflationary pressures on the Producer Price Index. We view the outturn—which remains firmly in the 50+ expansion zone—as a welcome sign of moderation, reinforcing our expectations that further tightening measures should be gradual, and in line with our soft landing scenario. The coming week will bring a further batch of closely-watched monthly data for December, including new loans, trade, FDI, property prices, money growth, and foreign exchange reserves (see *What to Watch*).

More moves to curb capital inflows

Despite spillovers from Europe's debt problems, the Asia region faces the prospect of further strong capital inflows due to its strong economic prospects and comparatively high (and rising) yields. This has policy makers continuing to express concerns about the risk of asset price bubbles and currency appreciation, with some countries unveiling additional macro-prudential measures. To date, the most active Asian countries in this regard have been Korea, Indonesia, and Taiwan. Last June Indonesia and Korea announced various measures to reduce currency volatility—consisting mainly of an intensification of existing regulations on hedging positions--and in October-November Thailand (15%) and Korea (14%) reintroduced withholding taxes on foreign investors' interest earnings from government bonds, while Taiwan (which had previously disallowed foreign time deposits) restricted off-shore funds from investing more than 30% of their portfolios in government bonds and money-market products. More recently, Indonesia raised reserve requirements on foreign currency deposits and imposed limits on banks' short-term borrowing, Korea announced that its cap on banks' outstanding foreign-exchange derivatives would be lowered, and Taiwan reduced the limit on banks' foreign exchange derivatives transactions, and also increased reserve requirements on local-currency deposits held by non-residents. Moreover, Korea has announced a bank levy on foreign borrowing (to be implemented later in 2011), but this appears to be part of its efforts to reduce external vulnerability, rather than to stem capital inflows per se.

Singapore's GDP outperforms in 2010

As a sign of strengthening regional momentum, Singapore's advanced Q4 GDP estimate expanded by 6.9% (quarter-on-quarter, seasonally adjusted annualized basis; consensus: 9.4%), bringing full-year growth for 2010 to a record-breaking 14.7%. Fourth quarter GDP was mainly driven by a strong expansion in the manufacturing sector and, to a lesser extent, an expansion in the financial services sector. The strength of Singapore's economic rebound, however, has led to rising inflationary pressures, as is increasingly the case in much of the region. In response, the Monetary Authority of Singapore (MAS) tightened policy last October at its six-monthly monetary meeting, by steepening the currency appreciation path and widening the nominal effective exchange rate band (Singapore uses an exchange-rate based monetary framework, rather than adjustments in interest rates). The currency appreciated by almost 10% against the USD in 2010, in line with many other regional currencies. Further inflationary pressures could result in another round of tightening (faster currency appreciation) in April. We expect the economy to grow by 5% in 2011, driven by growth in the services sector. While inflationary pressures are expected to persist, given its small size and high degree of openness, the economy also faces downside risks from deterioration in external demand.

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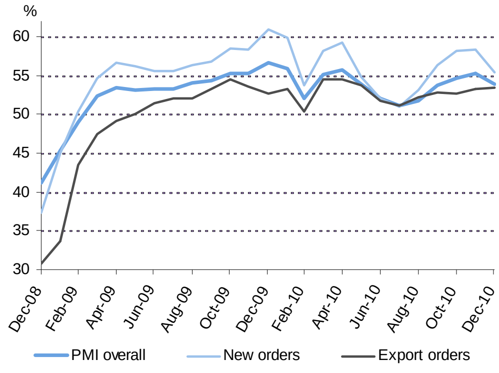
Chart 5

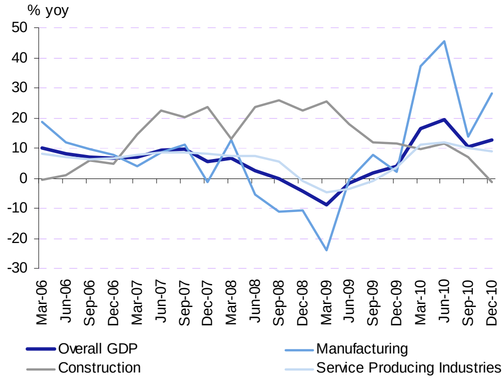
China's PMI moderates in December



Source: BBVA Research and Bloomberg

Chart 6

Singapore posts strong Q4 GDP growth



Source: BBVA Research and Bloomberg

What to watch

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China: New RMB loans for December (January 12)

Forecast: RMB 420 bn **Consensus:** RMB 360 bn **Previous:** RMB 564 bn

Along with the other indicators, new loan growth will be watched closely given the authorities' increasingly aggressive efforts to rein in credit growth to tame inflation and achieve a soft landing for the economy. The authorities' annual target ceiling (RMB 7.5 trillion) for full-year 2010 was essentially reached in November, meaning that the December outturn will likely breach the target (we project overall credit growth of 19.7% y/y for December). A higher-than-expected reading could increase expectations of further monetary tightening measures.

Calendar

Australia	**Date**	**Period**	**Prior**	**Cons.**
Retail Sales s.a. (MoM)	10-Jan	NOV	-1.10%	- -
Trade Balance	11-Jan	NOV	2625M	- -
Unemployment Rate	13-Jan	DEC	5.20%	- -
China	**Date**	**Period**	**Prior**	**Cons.**
Trade Balance (USD)	10-Jan	DEC	$22.89B	20.25B
Exports YoY%	10-Jan	DEC	34.90%	24.0
Imports YoY%	10-Jan	DEC	37.70%	25.3
M2	10-15 Jan	DEC	19.1	19.5
New Yuan Loans (RMB)	10-15 Jan	DEC	350b	564b
Property Prices	10-15 Jan	DEC	7.1	7.7
India	**Date**	**Period**	**Prior**	**Cons.**
Industrial Production YoY	12-Jan	NOV	10.80%	- -
Monthly Wholesale Prices YoY%	14-Jan	DEC	7.48%	- -
Japan	**Date**	**Period**	**Prior**	**Cons.**
Current Account Total	12-Jan	NOV	¥1436.2B	971.4
Adjusted Current Account Total	12-Jan	NOV	¥1462.6B	1190.0
Trade Balance - BOP Basis	12-Jan	NOV	¥912.9B	281.7
Machine Orders (MoM)	13-Jan	NOV	-1.40%	1.6
Machine Tool Orders (YoY)	13-Jan	DEC P	104.20%	--
Korea	**Date**	**Period**	**Prior**	**Cons.**
Unemployment Rate (SA)	12-Jan	DEC	3.20%	3.2
Malaysia	**Date**	**Period**	**Prior**	**Cons.**
Industrial Production YoY	10-Jan	NOV	3.00%	5.9
Singapore	**Date**	**Period**	**Prior**	**Cons.**
Retail Sales (MoM) sa	14-Jan	NOV	0.90%	- -
Thailand	**Date**	**Period**	**Prior**	**Cons.**
Consumer Confidence Economic	13-Jan	DEC	70.3	- -

	Current	**Expected**
Thailand – Benchmark Interest Rate, January 12 We expect an interest rates hike by 25 bps	2.00	2.25
Korea – 7-Day Repo Rate, January 13 The BOK will likely stay on hold	2.50	2.50

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STOCK MARKETS

INDEX	Last price	% change over a week	Year to date	% Change over 1 Y
China – Shanghai Comp.	2838.8	1.1	1.1	-11.1
Hong Kong – Hang Seng	23666.0	2.7	2.7	6.3
Taiwan – Weighted	8782.7	-2.1	-2.1	6.6
Japan – Nikkei 225	10541.0	3.1	3.1	-1.3
Korea – Kospi	2086.2	1.7	1.7	23.9
India – Sensex 30	19982.5	-2.6	-2.6	13.4
Australia – SPX/ASX 200	4705.0	-0.8	-0.8	-4.0
Singapore – Strait Times	3258.5	2.1	2.1	11.8
Indonesia – Jakarta Comp	3622.7	-2.2	-2.2	40.0
Thailand – SET	1046.8	1.4	1.4	42.5
Malaysia – KLCI	1570.3	3.4	3.4	21.6
Philippines – Manila Comp.	4202.5	0.0	0.0	36.5

Last update: Friday, 15.42 Hong Kong time.

FOREIGN EXCHANGE MARKETS

CURRENCY	Spot	% change over a week	Forward 3-month	Forward 12-month
China (CNY/USD)	6.63	-0.36	6.58	6.47
Hong Kong (HKD/USD)	7.77	-0.02	7.8	8
Taiwan (TWD/USD)	29.4	-0.23	29.09	28.58
Japan (JPY/USD)	83.5	-2.84	83.4	83.0
Korea (KRW/USD)	1122	0.33	1129.93	1138.98
India (INR/USD)	45.3	-1.40	46.1	48
Australia (USD/AUD)	0.99	-2.98	1	n.a.
Singapore (SGD/USD)	1.30	-1.02	1.30	1.3
Indonesia (IDR/USD)	9013	-0.19	9076	9365
Thailand (THB/USD)	30.3	-0.86	30.35	30.5
Malaysia (MYR/USD)	3.07	-0.23	3.1	3
Philippines (PHP/USD)	44.1	-0.74	44.12	44.15

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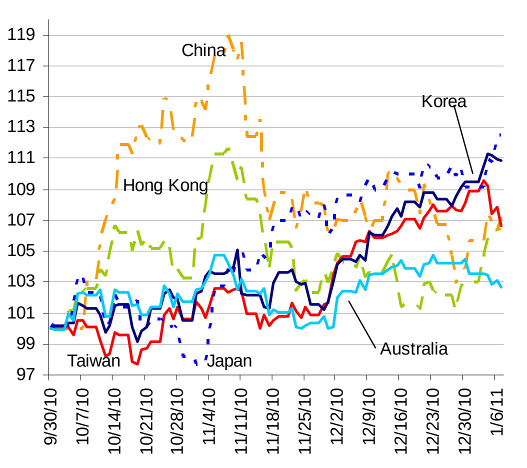

Source: BBVA Research and Bloomberg Index=100

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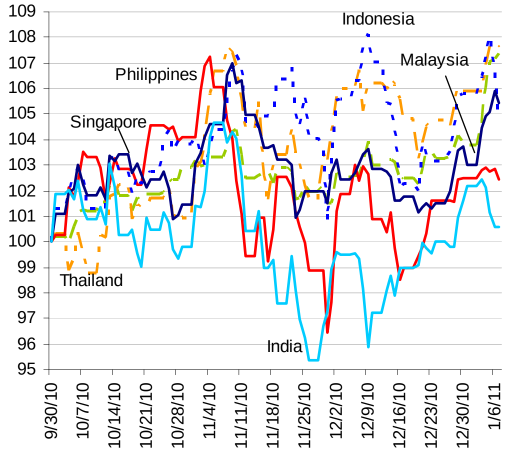
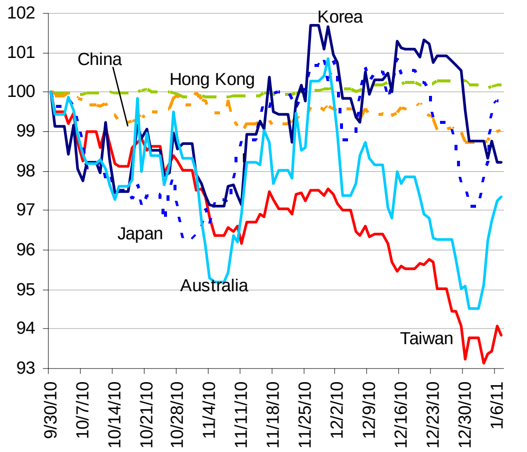


Source: BBVA Research and Bloomberg Index=100

FOREIGN EXCHANGE MARKETS



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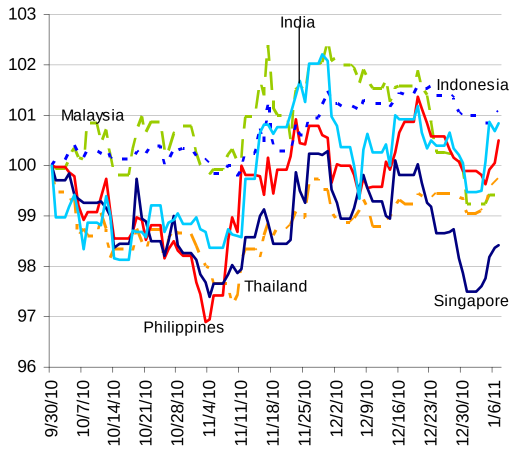

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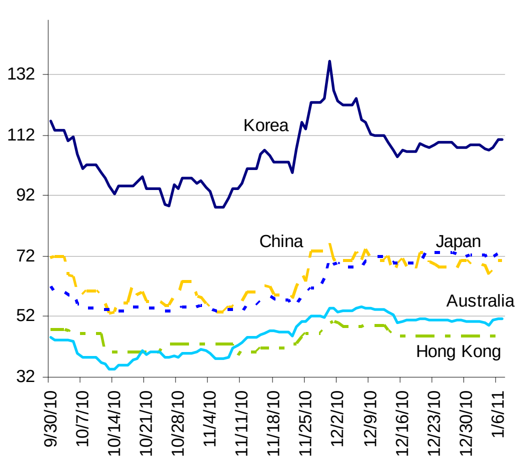

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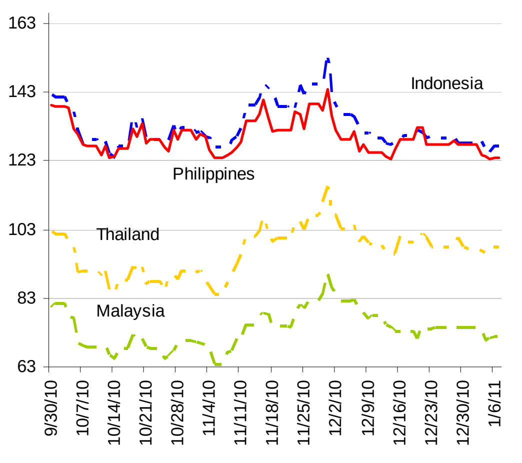

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