

# Weekly Watch

## Asia

15 April 2011  
Economic Analysis

**Asia**

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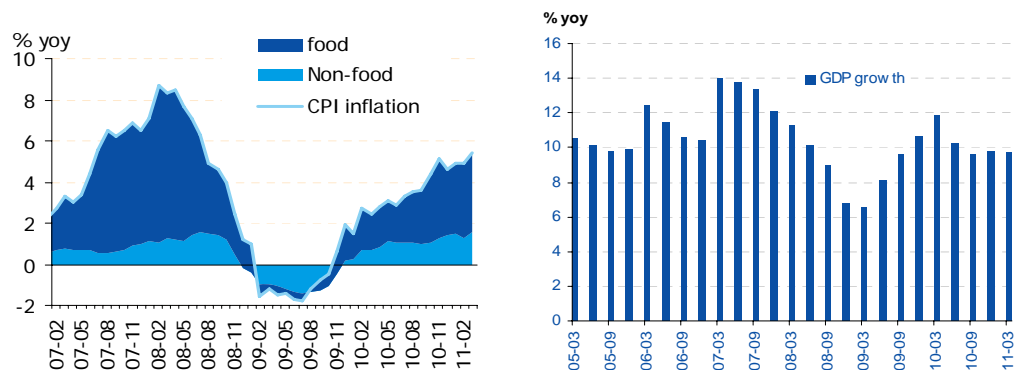
## Growth reinforces tightening bias

Despite headwinds from rising oil prices and Japan’s nuclear risks, growth momentum around the region not only remains intact, but continues surprising to the upside. First quarter GDP in China and Singapore were stronger-than-expected (see Highlights) which, together with rising inflation, has raised expectations of further tightening. Singapore re-centered its exchange rate band to a more appreciated level, setting the tone for further appreciation trends across the region.

### Inflationary pressures keep central banks in the spotlight

March inflation data released this past week for China and India were both higher than expected. In China, headline inflation picked up to 5.4% y/y (prior: 4.9%; consensus: 5.2%) on higher food and energy prices. In India, WPI inflation rose to 9.0% y/y (consensus: 8.4%) from 8.3% in February. The outturns are likely to raise expectations of more monetary tightening. For its part, as noted above, the Monetary Authority of Singapore (MAS) again tightened policy at its 6-monthly policy meeting. Korea and Indonesia stayed on hold as expected, but we anticipate further rate hikes during the year (see Highlights).

Chart 1  
Stronger than expected growth and inflation reinforce expectations of more monetary tightening



Source: Bloomberg and BBVA Research

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### China’s first quarter GDP and inflation surprise to the upside

Stronger than expected growth and inflation reinforce expectations of more tightening

### Singapore tightens monetary policy

The MAS re-centers its exchange rate band leading to more appreciation

### Central banks in the spotlight: Korea and Indonesia

Korea and Indonesia’s central banks stay on hold in April, but more hikes are expected

## Economic Analysis

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## Markets

Japan's raising of the alert level on its nuclear crisis worsened risk aversion in the region, triggering a general sell-off of major FX against JPY. Given the possibility of G7 intervention if the JPY were to strengthen significantly, we see USDJPY to be able to find support above 80 and will most likely range-bound in the near term. China's growth and inflation data exceed expectations (see Highlights), pointing to the risk of more aggressive tightening ahead. But as the possibility of abrupt growth slowdown in China is low in our view, the monthly data do not justify sharply higher risk premium yet. Meanwhile, the MAS re-centered its policy band and allowed a stronger SGD to combat inflation amidst strong growth (see Highlights). Its move may have some demonstration effects for other small open economies in Asia (especially Malaysia), which are also facing the challenge of rising imported inflation and healthy growth.

### Renewed tensions in Japan's nuclear crisis reverse JPY sell-off

Japanese authorities raised the severity rating of the nuclear crisis to 7 out of 7. While the contamination in Japan is still broadly under control, the hike marked the crisis in Japan comparable to the event of Chernobyl in 1986. Worries about more serious radiation leakage and damages from more aftershocks ahead renewed expectations of repatriation of capital by Japan's insurers. Coupled with IMF's downgrade of US growth on oil concerns, markets sought safety and unwound the carry trades. The short-covering caused JPY to appreciate broadly against liquid FX.

### Strong data in China raise expectations of more tightening

China's Q1 GDP and March CPI revealed a strong growth momentum accompanied by rising inflationary pressure. The outcomes were higher than what the market had anticipated, exacerbating concerns that the PBoC may have to initiate more aggressive tightening. But the price action has thus far been modest, with Asian equities down by less than 1.0% by mid-day Friday after the releases and risk sensitive currencies such as AUD and KRW falling less than 0.3%.

### A re-centering of the exchange rate band in Singapore and strong Q1 growth adds to SGD appreciation

The MAS re-centered its exchange rate policy band upwards to combat inflation, while leaving the slope and the band width unchanged. While the move was largely expected, strong GDP growth released at the same time raised hope that SGD will be trade closer to the new upper band before long. SGD appreciated by 0.85% in the past week, making it the best performing FX in the region. Stronger growth and currency in Singapore should also Malaysia in our view, whose currency tends to track closely to SGD.

### Equities end the week down on expectations of further monetary tightening

Asian stock markets were mixed during the week, ahead of today's release of GDP and inflation data in China. They were volatile at end-week due to the stronger-than-expected outturns in China. The Shanghai Composite Index was down sharply in early trading on Friday, but reversed course during the day. For the week, Korea, Thailand and the Philippines saw gains. India's market traded to the upside for much of the week, but showed signs of reversing on Friday on the high inflation outturn for March. The strongest losses for the week were in Malaysia (-2.5%), Taiwan (-2.0%), Japan (-1.8%), Hong Kong (-1.6%) and Singapore (-1.1%) (Chart 2).

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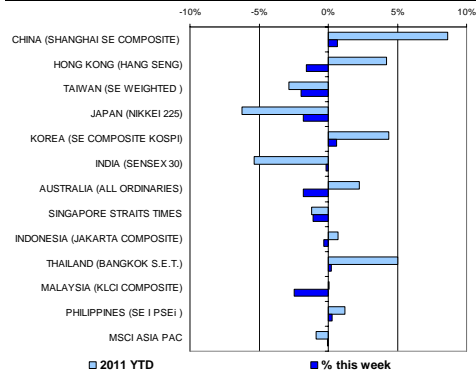
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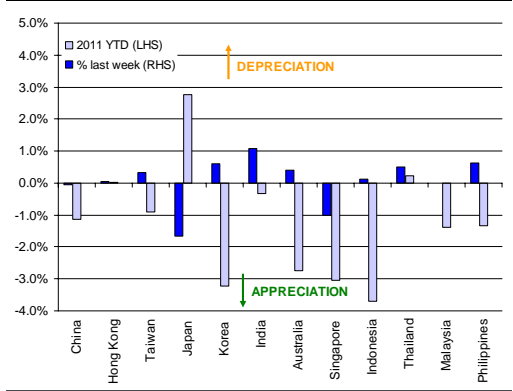
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Chart 2  
Stock markets



Source: BBVA Research and Bloomberg

Chart 3  
Foreign exchange markets



Source: BBVA Research and Bloomberg

## Highlights

### China's first quarter GDP and inflation surprise to the upside

First quarter GDP and inflation data point to continued strong growth in the Chinese economy with underlying price pressures. In particular, Q1 GDP growth registered 9.7% y/y (BBVA: 9.3%), down slightly from the previous quarter (9.8% y/y). Headline inflation rose to 5.4% y/y in March (BBVA: 5.0%) from 4.9% in February, due to both rising food and non-food prices. Producer price inflation (PPI) in March also edged up to 7.3% y/y from 7.2% y/y in February on rising commodity prices, marking a fourth straight month of increases in the reading. The outturns explain why the authorities have been so aggressive in tightening monetary policy in the past months and weeks, and expectations of further tightening measures may intensify, which could weigh on market sentiment. There are upside risks to our expectations of one more 25bp rate hike and at least 100 bps hikes in the required reserve ratio in the coming quarters. A positive interpretation of today's data, however, is that growth remains robust, even as the authorities implement measures to tame inflation. Recent credit growth data are showing an encouraging slowdown--new loans for all of Q1 were RMB 2.2 trillion, broadly in line with what we believe to be the authorities' (unannounced) full-year target of RMB 7.0-7.5 trillion.

### Singapore posts a strong Q1 GDP outturn, and tightens monetary policy

Singapore's advanced GDP estimate for Q1 beat expectations at 23.5% q/q (saar, consensus: 11.4%). Manufacturing rose 13.9% y/y, while the service sector grew surprisingly by 7.2% yoy, boosted by tourist arrivals. The higher-than-expected growth outturn, together with rising inflation, prompted the Monetary Authority of Singapore (MAS) to announce a tightening of policy through a re-centering (appreciation) of the exchange rate band with no change to the slope or width, broadly in line with our expectations. The announcement was made at the conclusion of the MAS' six-monthly policy meeting and marks the third consecutive tightening since April 2010. The Singapore dollar (SGD) has been on a strong appreciating trend in recent months (Chart 4) and appreciated on the announcement to a new record high of 1.24 per USD from around 1.26 in the preceding days. It is noteworthy that the re-centering was "below the prevailing exchange rate level", probably reflecting the authorities' awareness of headwinds to growth from rising oil prices. Headline inflation accelerated to 5.0% in March, but the rise has been driven by volatile components (such as car license premiums and energy prices), and core inflation remains considerably lower at 2.0% y/y. We expect GDP to set back temporarily in Q2 on (in part from developments in Japan), but full year GDP growth should still advance within the government's 4-6% forecast range.

### Central banks in the spotlight: Korea and Indonesia

Trends in inflation and interest rates in Korea and Indonesia are watched closely by international portfolio investors. Both economies have performed well since the 2008-09 crisis, with growth reaching 6.1% and 6.2% respectively in Indonesia and Korea last year. At the same time, they are both struggling to tame inflation, which has risen well above their respective inflation targets. The Bank of Korea moved first, beginning a series of interest rate hikes last July, while Bank Indonesia hiked rates for the first time in February. This past week, however, both of them stayed on hold (at 3.00% in Korea and 6.75% in Indonesia), as expected given their tendency to raise rates gradually (in the past, for example, the Bank of Korea has rarely raised rates in consecutive months). Nevertheless, we expect additional rate hikes in the months ahead—100bps in Korea and 75bps in Indonesia for the year—given solid growth prospects and ongoing inflationary pressures.

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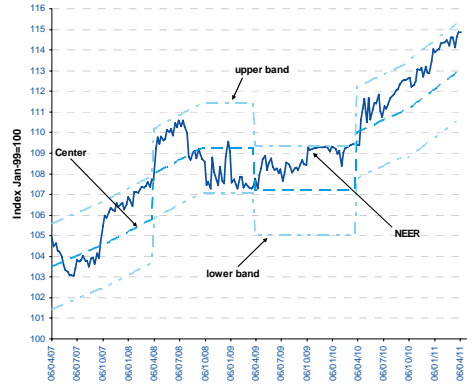
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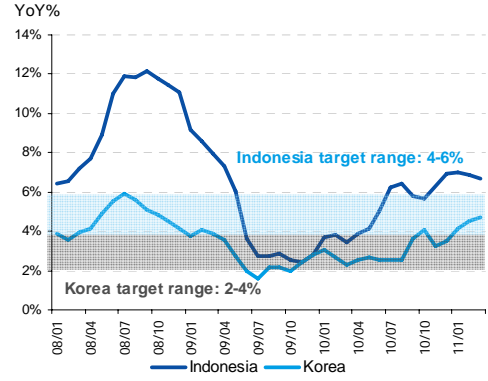
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Chart 4  
Singapore tightens monetary policy again by re-centering the NEER band for the SGD



Source: BBVA Research and Bloomberg

Chart 5  
Korea and Indonesia are seeking to tame inflation



Source: BBVA Research and Bloomberg

## Calendar Indicators

Australia	Date	Period	Prior	Cons.
Import price index (QoQ)	20-Apr	1Q	-3.80%	--
Export price index (QoQ)	20-Apr	1Q	-8.10%	--
Producer Price Index (QoQ)	21-Apr	1Q	0.10%	--
China	Date	Period	Prior	Cons.
Actual FDI (YoY)	15-22 APR	MAR	32.20%	--
China March Property Prices	18-Apr			
HSBC Flash China Manufacturing	19-Apr	APR	51.8	--
Hong Kong	Date	Period	Prior	Cons.
Unemployment Rate SA	19-Apr	MAR	3.60%	3.50%
Composite Interest Rate	19-Apr	MAR	0.20%	--
CPI - Composite Index (YoY)	21-Apr	MAR	3.70%	4.20%
Japan	Date	Period	Prior	Cons.
Adjusted Merchnds Trade Bal.	20-Apr	MAR	¥556.0B	¥278.6B
Merchnds Trade Exports YoY	20-Apr	MAR	9	-0.7
Merchnds Trade Imports YoY	20-Apr	MAR	9.9	7.6
Malaysia	Date	Period	Prior	Cons.
CPI YoY	20-Apr	MAR	2.90%	3.00%
Philippines	Date	Period	Prior	Cons.
Balance of Payments	19-Apr	MAR	-\$133M	--
Budget Deficit/Surplus	21-25 APR	MAR	-21.5B	--
Singapore	Date	Period	Prior	Cons.
Electronic Exports (YoY)	18-Apr	MAR	-12.80%	-9.00%
Non-oil Domestic Exports (YoY)	18-Apr	MAR	7.80%	4.00%
Non-oil Domestic Exp SA (MoM)	18-Apr	MAR	2.90%	-1.30%
Taiwan	Date	Period	Prior	Cons.
Export Orders (YoY)	20-Apr	MAR	5.33%	3.90%
Unemployment Rate - sa	22-Apr	MAR	4.59%	4.50%
Thailand	Date	Period	Prior	Cons.
Customs Exports (YoY)	20-25 APR	MAR	31.00%	18.00%
Customs Imports (YoY)	20-25 APR	MAR	22.50%	20.60%
Customs Trade Balance	20-25 APR	MAR	\$1768M	\$864M

### Thailand – Benchmark Interest Rate, April 20

We expect no change in the interest rates

**Current Expected**

2.50% 2.50%

### Australia – Reserve Bank's Board April Minutes, April 19

## Calendar Events

### Japan: Export growth in March (April 20)

Forecast: 5.3% y/y

Consensus: -0.7% y/y

Prior: 9.0% y/y

**Comment:** Japan's exports and imports are likely to have been disrupted in the aftermath of the earthquake. Exports for March, although only partially reflecting the full-month impact, will offer a first glimpse of the magnitude of the supply shock. So far trade data from Japan's most significant trading partners in Asia (such as Taiwan) show a strong impact. Japan's exports in March are expected to have fallen from the levels of previous months. **Market impact:** A better-than-expected outcome might lift market sentiment, while a lower-than-expected outcome could exacerbate concerns about the impact not only on Japan, but for the region.

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## Markets Data

STOCK MARKETS	INDEX	Last price	% change over a week	Year to date	% Change over 1 Y
	China – Shanghai Comp.	3050.5	0.7	8.6	-3.6
	Hong Kong – Hang Seng	24008.1	-1.6	4.2	8.4
	Taiwan – Weighted	8718.1	-2.0	-2.8	6.7
	Japan – Nikkei 225	9591.5	-1.8	-6.2	-14.9
	Korea – Kospi	2140.5	0.6	4.4	22.7
	India – Sensex 30	19415.4	-0.2	-5.3	8.9
	Australia – SPX/ASX 200	4852.1	-1.8	2.3	-3.0
	Singapore – Strait Times	3151.8	-1.1	-1.2	4.5
	Indonesia – Jakarta Comp	3729.2	-0.3	0.7	28.6
	Thailand – SET	1084.9	0.2	5.0	42.6
	Malaysia – KLCI	1519.3	-2.5	0.0	13.5
	Philippines – Manila Comp.	4251.6	0.3	1.2	29.7

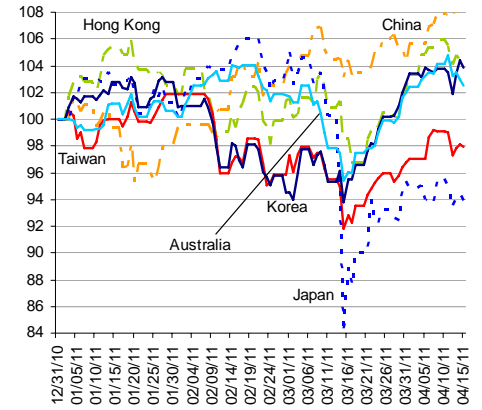
Last update: Friday, 16.15 Hong Kong time.

FOREIGN EXCHANGE MARKETS	CURRENCY	Spot	% change over a week	Forward 3-month	Forward 12-month
	China (CNY/USD)	6.53	0.06	6.48	6.39
	Hong Kong (HKD/USD)	7.78	-0.05	7.8	8
	Taiwan (TWD/USD)	29.0	-0.33	28.81	28.06
	Japan (JPY/USD)	83.4	1.67	83.3	83.0
	Korea (KRW/USD)	1090	-0.61	1095.98	1109.90
	India (INR/USD)	44.6	-1.08	45.2	47
	Australia (USD/AUD)	1.05	-0.41	1	n.a.
	Singapore (SGD/USD)	1.24	1.02	1.24	1.2
	Indonesia (IDR/USD)	8663	-0.12	8737	9054
	Thailand (THB/USD)	30.1	-0.50	30.19	30.5
	Malaysia (MYR/USD)	3.02	0.01	3.0	3
	Philippines (PHP/USD)	43.2	-0.61	43.25	43.41

Last update: Friday, 11.15 Hong Kong time.

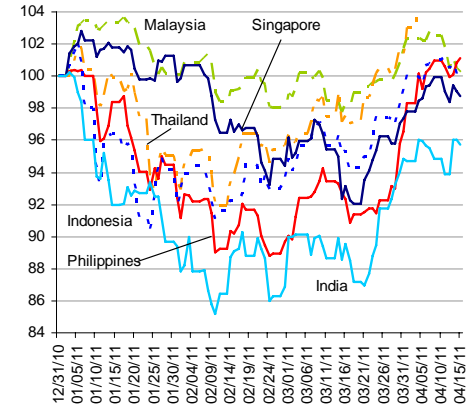
# Charts

Chart 6  
Stock Markets



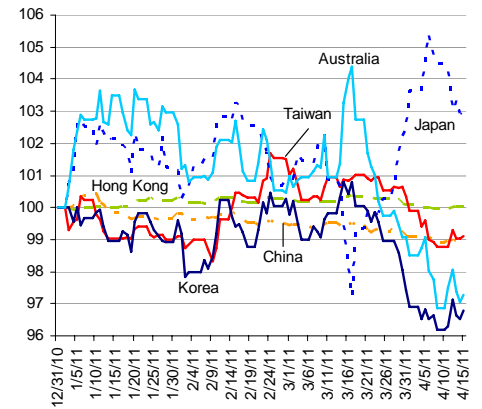
Source: BBVA Research and Bloomberg

Chart 7  
Stock Markets



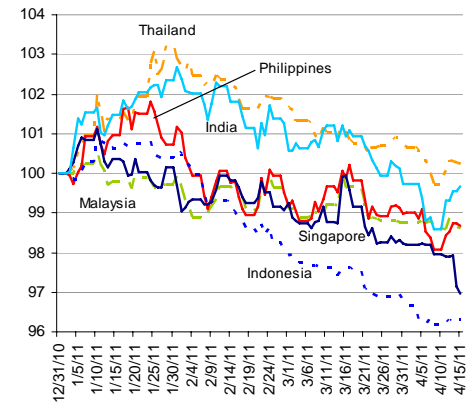
Source: BBVA Research and Bloomberg

Chart 8  
Foreign Exchange Markets



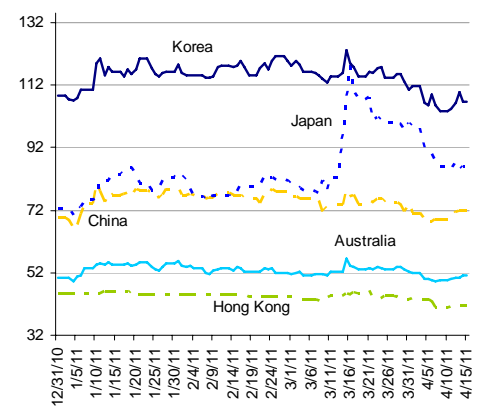
Source: BBVA Research and Bloomberg

Chart 9  
Foreign Exchange Markets



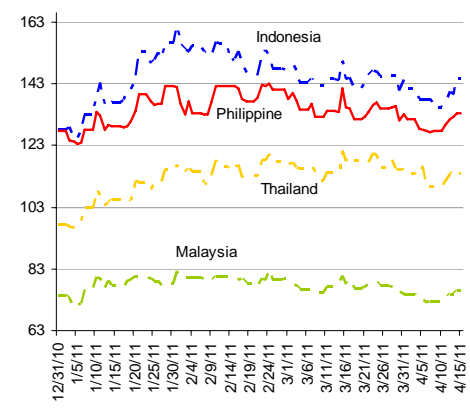
Source: BBVA Research and Bloomberg

Chart 10  
Credit Default Swaps



Source: BBVA Research and Bloomberg

Chart 11  
Credit Default Swaps



Source: BBVA Research and Bloomberg



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