BBVA | RESEARCH

Weekly Watch

Asia

27 May 2011
Economic Analysis

Asia
Stephen Schwartz
stephen.schwartz@bbva.com.hk

Mario Nevares
mario.nevares@bbva.com.hk

Fielding Chen
fielding.chen@bbva.com.hk

Le Xia
xia.le@bbva.com.hk

Jenny Zheng
jenny.zheng@bbva.com.hk

Serena Wang
serena.wang@bbva.com.hk

Zhigang Li
zhigang.li@bbva.com.hk

Sumedh Deorukhkar
sumedh.deorukhkar@grupobbva.com

Markets
Richard Li
richard.li@bbva.com.hk

Mario Nevares
mario.nevares@bbva.com.hk

Markets →
Highlights →
Calendar →
Markets Data →
Charts →

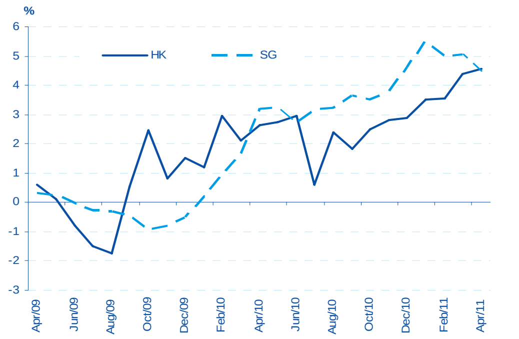
Is growth slowing?

As flagged in our recent *Asia Economic Outlook*, second quarter regional activity indicators are expected to slow due to headwinds from high oil prices, supply disruptions in Japan, and financial market tensions in Europe. The data are now bearing this out. Recent indicators in Japan, China, Taiwan, Hong Kong, and Thailand point to slowdowns in production and/or exports, albeit from very high growth rates. That said, we continue to expect a resumption of strong growth trends during the second half of the year, with the soft patch in Q2 helping to alleviate overheating pressures. Meanwhile, with the exception of Vietnam, headline inflation is showing signs of having peaked in a number of economies.

Easing production and inflation

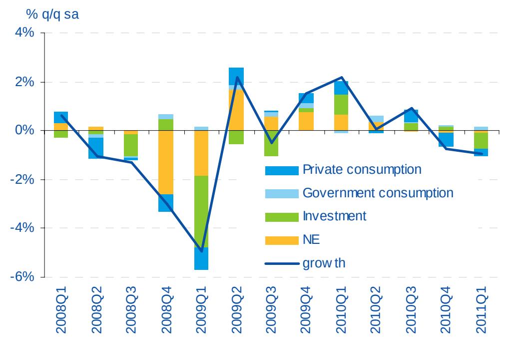
Industrial production and exports eased for April in a number of economies. In particular, Taiwan saw weaker-than-expected outturns for industrial production (6.9% y/y vs. consensus: 13.4% y/y) and export orders (10.1% y/y vs. consensus: 14.7%), and Hong Kong also saw much weaker-than-expected exports (4.1% y/y vs. consensus: 16.8%). In Thailand (Highlights), industrial production contracted by -7.8% y/y (consensus: -4.8%). The weaker industrial production figures, especially in Taiwan and Thailand likely reflect the temporary impact of supply disruptions in Japan. Meanwhile, inflation data in some countries show signs of having peaked, with the CPI in Hong Kong staying flat at 4.6% y/y, in line with expectations, and in Singapore easing to 4.5% y/y (Chart 1). The outliers are Japan, which has seen a welcome end to deflation from the supply chain disruptions, with April inflation of 0.3% y/y, and Vietnam, where inflation has surged to a staggering 19.8% y/y. Next week we will feature Q1 GDP outturns for India, Australia and the Philippines.

Chart 1
High inflation in Hong Kong and Singapore show signs of leveling off for the time being



Source: BBVA Research and Bloomberg

Chart 2
Japan's GDP and activity indicators plunge after the earthquake



Source: BBVA Research and Bloomberg

Highlights

Japan: despite disappointing post-quake data, a strong rebound is underway

A quick resumption of supply chains is expected to result in a strong rebound

The Thai economy remains resilient with the election just around the corner

First quarter GDP data were strong, although supply disruptions from Japan are now evident

Electricity shortage is unlikely to dent China's growth

A looming shortage of electricity this summer should have only small output effects

Economic Analysis

Richard Li
richard.li@bbva.com.hk

Mario Nevares
mario.nevares@bbva.com.hk

Markets

Asian FX and equity markets ended broadly lower for the week (Chart 4), on European debt anxieties, USD weakness and prospects of Asian monetary tightening dominated sentiment. Equities, especially in China, were down (Chart 3), due to the usual concerns about tightening measures. However, they rallied slightly in the last two days on improved risk sentiment.

Sharp rise in Chinese short-term rates causes jitters

Short-term interbank rates surged in China following a new regulation to become effective in June requiring banks to provide monthly average loan-to-deposit ratios instead of merely end-quarter ratios. Market players expect the new prudential requirement to increase liquidity demand by banks, with the 7-day repo rates jumping to 5.0%, up from 3.6% at the end of last week. Higher market interest rates coupled with signs of a worsening of the European debt crisis agitated China's local stock markets. But in our view, every cloud has a silver lining, as recent spikes in interbank rates may defer further tightening at least in the near term. Signs of growth moderation amidst power shortage further increase the likelihood of a deferral, and markets will closely monitor the PMI due next week in this regard.

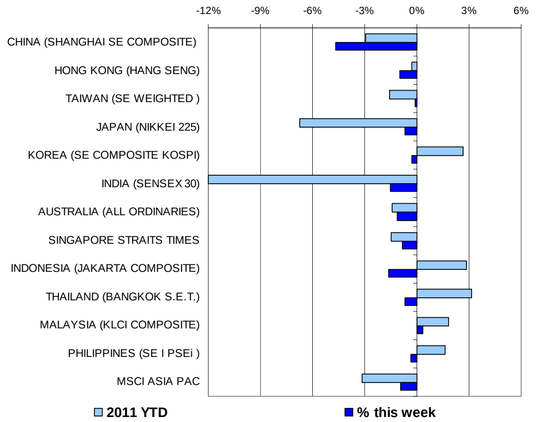
SGD NEER trade closer to centre as inflation already peaks

Singapore's CPI slowed to 4.5% y/y in April, down from 5.0% y/y in March and its peak of 5.5% in January. As inflation moderated, market players also started to price in the possibility of a less aggressive MAS in October's meeting, with USDSGD trading closer towards the band. The outturn reinforces our view that the worst of price fears may be behind us, although we believe inflation will stay above 4.0% for quite a while.

Japan's data show little signs of repatriation post-quake

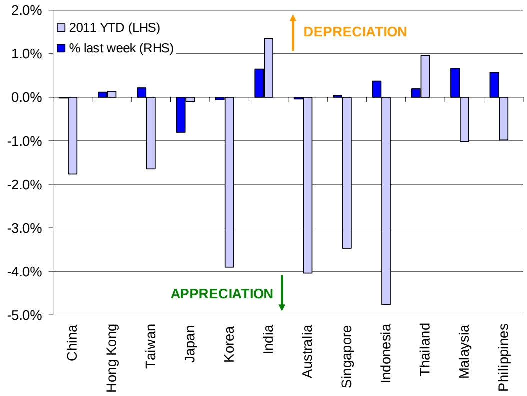
The release of monthly portfolio data by investor type offered few signs of large-scale repatriation by Japanese life insurance and investment trust companies following the earthquake. Capital outflows remained in April on a net basis for these investors, although the amounts were smaller than seen in previous four years, reflecting the general caution in investing abroad following the catastrophe. We continue to see USDJPY largely a play on US rates given little chance for the BoJ to alter its monetary policy in the near term. As such, JPY remained adamantly irresponsive to domestic macro data such as the trade deficits in April. Instead, it strengthened markedly on Friday ensuing lower-than-expected US GDP estimates for Q1.

Chart 3
Stock markets



Source: BBVA Research and Bloomberg

Chart 4
Foreign exchange markets



Source: BBVA Research and Bloomberg

Economic Analysis

Highlights

Japan: despite disappointing post-quake data, a strong rebound is underway

The Japanese economy continues to adjust in the aftermath of the March 11 earthquake. The extent of the post-quake disruption has become increasingly evident, following the release of Q1 GDP earlier this month (Chart 2, above) and April activity indicators this week. April exports were down by -12.7% y/y (consensus: -12.5%) and retails sales declined by -4.8% y/y (consensus: -6.2%). The data follow similar plunges in March, as supply disruptions—especially in the auto sector—and weak consumer and business confidence take their toll. Q1 GDP growth surprised to the downside (-3.7%, q/q saar vs. consensus: -2.0%), confirming a technical recession (two consecutive quarters of negative growth). However, the impact of the earthquake on full-quarter GDP was probably small since the earthquake occurred toward the very end of the quarter, meaning that underlying growth momentum may have been weaker than previously anticipated. Nevertheless, there is good reason to expect a rapid rebound during the second half of the year, as incorporated in our 2011 full-year growth projection of 0.5%. Anecdotal evidence suggests that a resumption of supply chains may occur faster than previously expected, and consumers may already be returning to more normal spending patterns after an initial period of caution. It is also noteworthy that the weak Q1 GDP outturn was due to a drawdown of inventories. As supply chains are restored, a rebuilding of inventories would likely contribute to a rebound in activity, over and above the boost from reconstruction spending. On the monetary policy front, the Bank of Japan (BoJ) kept its monetary stance unchanged at its most recent meeting on May 20, after unveiling an initial round of stimulus policies just after the quake. We expect the BoJ to implement additional schemes to facilitate recovery. These may well include an expansion of the asset-purchase program from the current ¥10 trillion (doubled in March) and boosting the ¥3 trillion special lending facility. We also expect the government to approve further spending, although room for maneuver is limited due to the very high public debt, with Fitch the latest to downgrade the outlook.

The Thai economy remains resilient with the election just around the corner

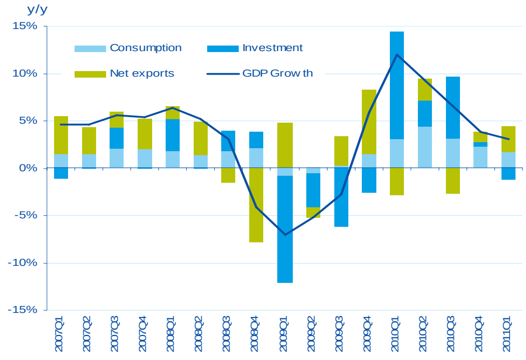
Over the past year, Thailand's economy has proven to be remarkably resilient to ongoing domestic political tensions, the uncertain external environment, and high commodity prices. Despite deadly protests last April, the economy grew by an impressive 7.8% in 2010 on strong exports and domestic demand. The latest evidence of this resilience is the first quarter GDP outturn, which registered the fastest pace in a year to a 2.0% q/q (seasonally adjusted) from a previous 1.3% q/q (consensus: 2.2%). The solid growth, similar to outturns in most Asian countries in Q1, was supported by both domestic and external demand. Growth may have been even stronger were it not for supply disruptions from Japan's earthquake: Thailand is particularly susceptible given its large auto industry and reliance on imported components from Japan, as seen by a plunge in April manufacturing production by -7.8% y/y. The Q1 GDP release has come just over a month ahead of general elections scheduled for July 3. The long-anticipated election will pit Prime Minister Abhisit Vejjejiva's Democrat party against "Red Shirt" allies of ex-Premier Thaksin Shinawatra, who was ousted in a 2006 coup. Political instability has predominated ever since, and it remains to be seen whether the July elections will lead to stability or to a renewed bout of turbulence. We still expect Thailand's resilient economy to register growth of at least 3.8% in 2011.

Electricity shortage is unlikely to dent China's growth

China is reportedly about to face this summer its most severe electricity shortage since 2004. In anticipation, some provinces (such as Zhejiang, Jiangsu, Hunan, Hubei, Chongqing and Shanghai) have already started to ration electricity. The severity of this year's seasonal power shortage is attributable to several factors: (i) exceptionally strong demand, especially in energy-intensity industries such as cement, iron and steel, and other metals; (ii) an ongoing drought in the southern region, which has affected water flow in the Yangtze river and disrupted the supply of hydroelectric power; and (iii) perhaps most important of all, soaring coal prices. The latter development has led to a cut in production of thermally-generated power (which accounts for almost 80% of total electricity production), as producers are restricted from passing on higher costs to end-users under China's regulated electricity price regime. That said, dire predictions of shortages leading to steep drops in economic activity are not warranted, in our view, as the looming electricity shortages are unlikely to be widespread. Moreover, if history is any guide, solutions will be found. In 2004, a prolonged power shortage struck, but GDP growth still managed to remain at a rapid 10.1%. Solutions to the current shortage could include allowing producers to pass on higher coal prices and other administrative measures.

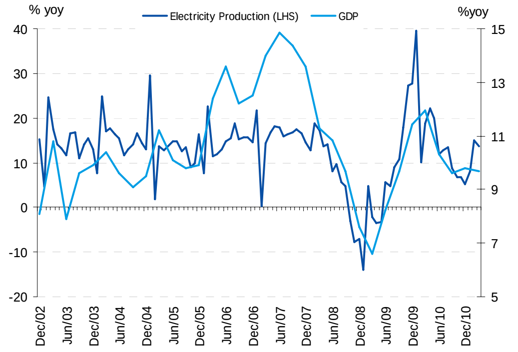
Home
Markets
Calendar
Markets Data
Chart

Chart 5
Thailand's GDP remains resilient



Source: BBVA Research and Bloomberg

Chart 6
China's strong demand for electricity is contributing to a looming power shortage



Source: BBVA Research and Bloomberg

Calendar Indicators

Australia	Date	Period	Prior	Cons.
Gross Domestic Product (YoY)	01-Jun	1Q	2.70%	1.80%
Trade Balance	02-Jun	APR	1740M	2100M
Retail Sales s.a. (MoM)	02-Jun	APR	-0.50%	0.40%
China	**Date**	**Period**	**Prior**	**Cons.**
PMI Manufacturing	01-Jun	MAY	52.9	51.6
Hong Kong	**Date**	**Period**	**Prior**	**Cons.**
Retail Sales - Value (YoY)	31-May	APR	26.00%	24.30%
Indonesia	**Date**	**Period**	**Prior**	**Cons.**
Total Trade Balance	01-Jun	APR	$1813M	$1460M
Inflation (YoY)	01-Jun	MAY	6.16%	6.00%
Exports (YoY)	01-Jun	APR	27.50%	29.00%
Total Imports (YoY)	01-Jun	APR	32.00%	26.90%
India	**Date**	**Period**	**Prior**	**Cons.**
Qtrly GDP YoY%	31-May	1Q	8.20%	8.10%
Exports YoY%	01-Jun	APR	43.90%	- -
Imports YoY%	01-Jun	APR	17.30%	- -
Japan	**Date**	**Period**	**Prior**	**Cons.**
Industrial Production YOY%	31-May	APR P	-13.10%	-12.20%
Vehicle Production (YoY)	31-May	APR	-57.30%	- -
Vehicle Sales (YoY)	01-Jun	MAY	-51.00%	- -
Malaysia	**Date**	**Period**	**Prior**	**Cons.**
Exports YoY%	03-Jun	APR	7.80%	10.70%
Imports YoY%	03-Jun	APR	12.10%	11.50%
Trade Balance	03-Jun	APR	13.52B	10.30B
Philippines	**Date**	**Period**	**Prior**	**Cons.**
GDP (YoY)	30-May	1Q	7.10%	5.40%
Korea	**Date**	**Period**	**Prior**	**Cons.**
Industrial Production (YoY)	31-May	APR	8.70%	9.40%
Consumer Price Index (YoY)	01-Jun	MAY	4.20%	4.30%
Ext Trade - Export (YoY)	01-Jun	MAY	26.60%	28.30%
Ext Trade - Imports (YoY)	01-Jun	MAY	23.70%	28.10%
Ext Trade - Balance in US$ Mln	01-Jun	MAY	5823	4579
Thailand	**Date**	**Period**	**Prior**	**Cons.**
Total Exports YOY%	31-May	APR	31.00%	- -
Total Imports YOY%	31-May	APR	27.20%	- -
Total Trade Balance	31-May	APR	$1892M	- -
Consumer Price Index (YoY)	01-Jun	MAY	4.04%	4.20%

Indicator of the Week: China PMI for May (June 1)

Forecast: 51.9	Consensus: 51.6	Prior: 52.9

Comment: We expect the Purchasing Managers' Index (PMI) to ease further in May following a number of recent activity indicators pointing to moderation in growth. A moderating trend in the PMI would be welcome news for the authorities who have been seeking to contain inflation and prevent overheating through monetary tightening. While some market participants have expressed fear of a hard landing, the PMI should remain well within the 50+ expansion zone, indicating a soft landing. Market impact: A reading in line with or below consensus is likely to exacerbate market fears of a hard landing in China.

Home →
Markets →
Highlights →
Markets Data →
Charts →

Calendar Events

Thailand – Benchmark Interest Rate, June 1	Current	Expected
We expect a hike of 25 bp in the Benchmark Interest Rate	2.75%	3.00%

Markets Data

STOCK MARKETS

INDEX	Last price	% change over a week	Year to date	% Change over 1 Y
China – Shanghai Comp.	2725.3	-4.7	-2.9	2.6
Hong Kong – Hang Seng	22971.9	-1.0	-0.3	18.2
Taiwan – Weighted	8831.3	-0.1	-1.6	21.9
Japan – Nikkei 225	9538.6	-0.7	-6.7	-1.0
Korea – Kospi	2104.7	-0.3	2.6	30.9
India – Sensex 30	18044.6	-1.5	-12.0	8.3
Australia – SPX/ASX 200	4678.3	-1.1	-1.4	6.8
Singapore – Strait Times	3142.4	-0.8	-1.5	14.7
Indonesia – Jakarta Comp	3807.8	-1.7	2.8	40.3
Thailand – SET	1065.5	-0.7	3.2	44.5
Malaysia – KLCI	1546.4	0.3	1.8	21.8
Philippines – Manila Comp.	4269.4	-0.4	1.6	35.3

Last update: Friday, 11.15 Hong Kong time.

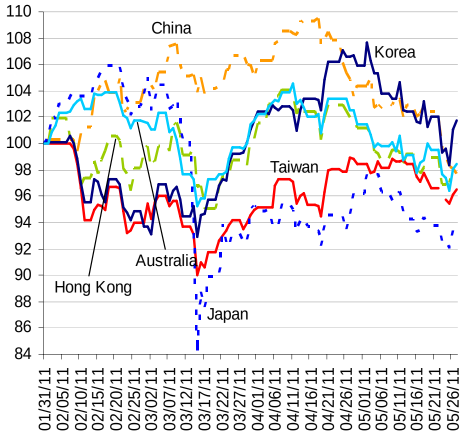
FOREIGN EXCHANGE MARKETS

CURRENCY	Spot	% change over a week	Forward 3-month	Forward 12-month
China (CNY/USD)	6.49	0.02	6.47	6.37
Hong Kong (HKD/USD)	7.78	-0.13	7.8	8
Taiwan (TWD/USD)	28.8	-0.21	28.62	28.00
Japan (JPY/USD)	81.0	0.81	81.0	80.7
Korea (KRW/USD)	1082	0.06	1088.54	1103.48
India (INR/USD)	45.3	-0.73	45.9	48
Australia (USD/AUD)	1.07	0.04	1	n.a.
Singapore (SGD/USD)	1.24	-0.05	1.24	1.2
Indonesia (IDR/USD)	8568	-0.37	8661	8983
Thailand (THB/USD)	30.4	-0.20	30.50	30.8
Malaysia (MYR/USD)	3.03	-0.66	3.0	3
Philippines (PHP/USD)	43.4	-0.56	43.44	43.60

Last update: Friday, 11.15 Hong Kong time.

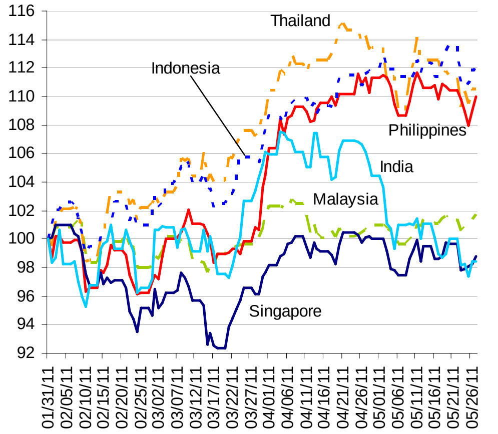
Charts

Chart 6
Stock Markets



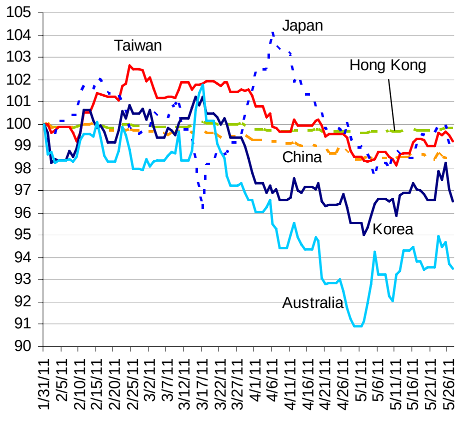
Source: BBVA Research and Bloomberg

Chart 7
Stock Markets



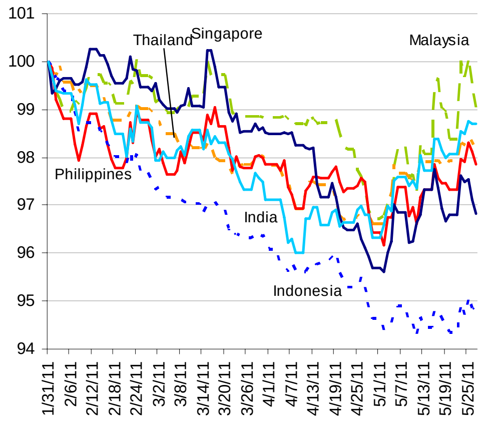
Source: BBVA Research and Bloomberg

Chart 8
Foreign Exchange Markets



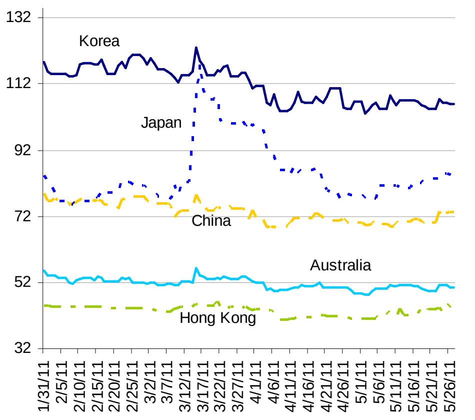
Source: BBVA Research and Bloomberg

Chart 9
Foreign Exchange Markets



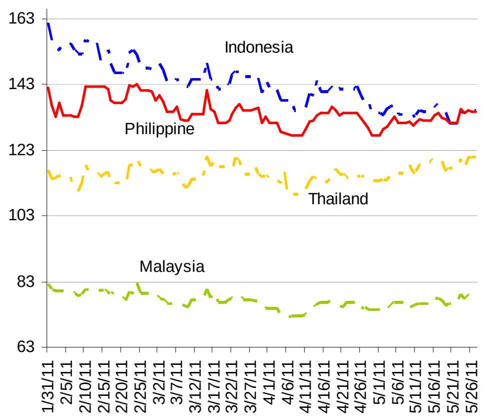
Source: BBVA Research and Bloomberg

Chart 10
Credit Default Swaps



Source: BBVA Research and Bloomberg

Chart 11
Credit Default Swaps



Source: BBVA Research and Bloomberg

DISCLAIMER