Weekly Watch

Asia

16 September 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

Zhigang Li
zhigang.li@bbva.com.hk

Sumedh Deorukhkar
sumedh.deorukhkar@grupobbva.com

Jeffrey Cantwell
jeffrey.cantwell@bbva.com.hk

George Xu
george.xu@bbva.com.hk

Markets

FX Strategy
Richard Li
richard.li@bbva.com.hk

Economic analysis
Jeffrey Cantwell
jeffrey.cantwell@bbva.com.hk

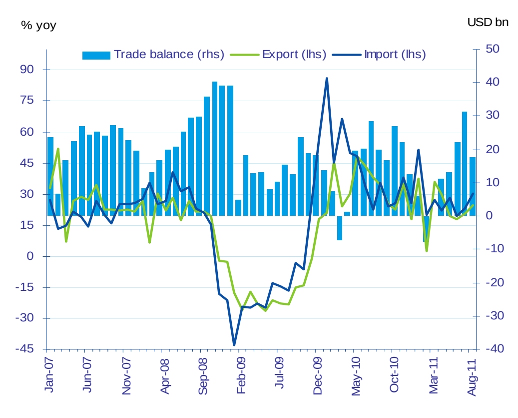
Asian economies show their resilience

As policymakers in Europe seek solutions to ongoing growth, debt and banking woes, Asian economies continue to show signs of resilience. While the region is already feeling the slowing effects from weaker external demand, much of the recent activity data, at least for now, has been surprisingly robust. The latest signs of this came from China (Chart 1) and Singapore (see Highlights) where August exports surprised to the upside. The outturns follow similarly upbeat export figures from Korea, as reported earlier this month. Despite still high inflation, most, but not all, central banks have shifted to pause mode. In fact, India today hiked interest rates for a 12th time in 18 months (see Highlights) to help anchor inflation expectations, following the Bank of Thailand's hike last month. Given global uncertainties and slowing growth, however, we do not expect further rate hikes for the region during the remainder of the year. At the same time, strong underlying domestic demand and still high inflation is likely to prevent central banks from easing policy anytime soon.

Robust exports and activity indicators

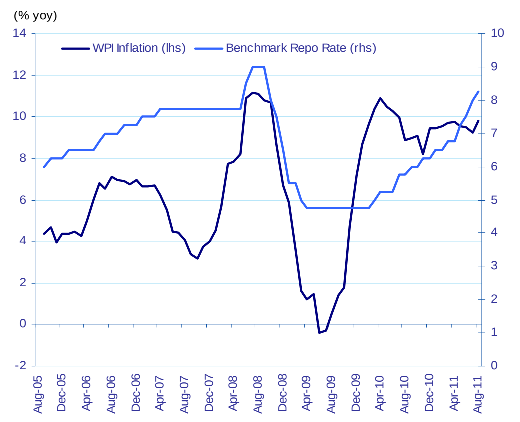
China's August trade outturns were better than expected (see Highlights), providing strong support to demand in the region. Singapore's August exports also surprised to the upside (5.1% y/y vs. consensus -6.5%) ahead of the MAS' bi-annual policy meeting in mid-October. India's rate hike was a response to elevated inflation, which is nearing 10% (Chart 1). For next week, the focus will turn to CPI as Hong Kong, Singapore and Malaysia are set to report August outturns. Also exports in Japan and export orders in Taiwan (see Weekly Indicator) will provide an important gauge of external demand.

Chart 1
China: strong import demand



Source: CEIC and BBVA Research

Chart 2
India: RBI hikes rates again to stem inflation



Source: CEIC and BBVA Research

Highlights

China's encouraging August trade data round out a picture of robust demand
China's activity data continues to point to a soft landing for the economy

India: RBI stays firm on inflation with a rate hike despite risks to growth
India's central bank hikes interest rates despite global uncertainty and signs of slowing growth

Singapore's better-than-expected exports are the latest sign of Asia's resilience
As Singapore's exports surprise to the upside, a slowdown looms on weak external demand

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Economic Analysis
Jeffrey Cantwell
jeffrey.cantwell@bbva.com.hk
FX Strategy
Richard Li
richard.li@bbva.com.hk

Markets

Asian markets continue to feel the ripple effects from Europe

Asian equities, credit and currencies continue to experience elevated volatility in the near-term as concerns over the European fiscal situation and banking system deepen. On Wednesday, the combined effect of a Moody's downgrade of two French banks and an ADB report forecasting lower growth and higher inflation for Asia was enough to send the MSCI Asia Index to its lowest level since August 2010. Asian currencies were sharply weaker, and central banks such as Bank Indonesia intervened to smooth volatility. However, after Germany and France reemphasized their commitment to assisting Greece, and central banks made a concerted pledge to offer US dollar funding to Eurozone banks, a cautious return to risk-taking ensued, but overall sentiment still remains tenuous in the near-term.

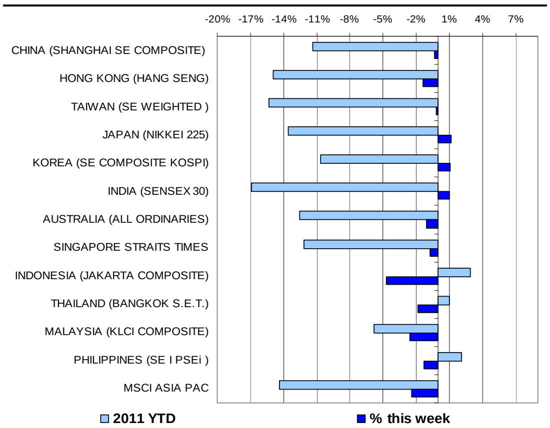
Asian FX: broad-based weakening as slowdown fears continue

Regional currencies traded lower early this week in a broadly risk-off mode before recovering somewhat on Friday. On Wednesday, Bank Indonesia intervened after selling pressures caused its currency to depreciate by 2.6% for the day. In India, the rupee weakened close to 2% for the week over concerns of a potential hard-landing, triggered by equities outflows. Markets are concerned with a hard landing in India as inflation remains elevated even after aggressive tightening this year and industrial output growth has shown signs of marked deceleration. In the near term, Asian FX will continue to be driven by external factors. Investors will listen for signs of stabilization from European policymakers this weekend, and also wait for Federal Reserve Chairman Ben Bernanke (the two-day Fed meeting is scheduled for September 20-21), to elaborate on what 'a fuller discussion of monetary tools' means for the US economy.

Markets: News on Asia's resilience is challenged

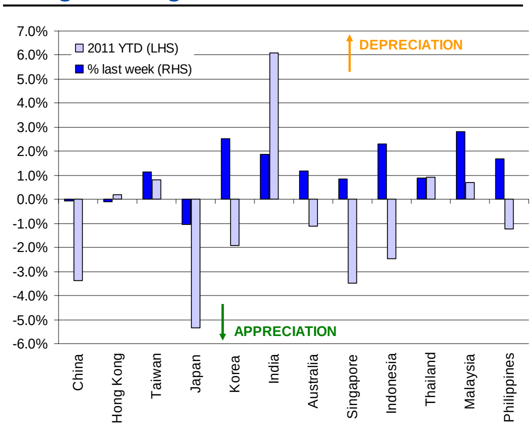
Well aware that significant risks remain to the downside, and that macro headwinds are driving regional performance, our view remains that Asian economies are well positioned in a lukewarm global environment, where the US continues to grow modestly, and there is no disorderly default on Greek debt. The price action this week in Asian FX seems to price in a more downbeat scenario, where Asian financial conditions could tighten as the European debt crisis may be spreading to core countries. This is still not our base case scenario, but timely action by European leaders is required to contain these risks.

Chart 3
Stock markets



Source: BBVA Research and Bloomberg

Chart 4
Foreign exchange markets



Source: BBVA Research and Bloomberg

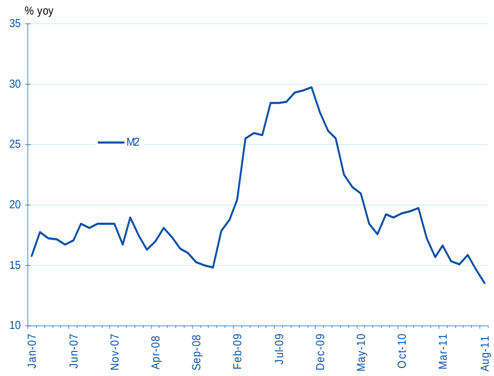
Economic Analysis

Highlights

China's encouraging August trade data round out a picture of robust demand

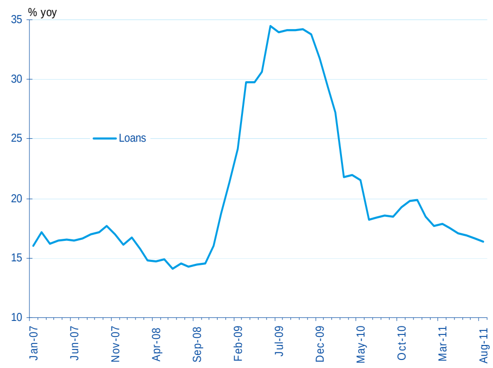
A set of positive trade figures released this week helped to round out a picture of robust demand and growth in China. Taken together and following last week's set of encouraging activity indicators, the data helped lift regional market sentiment, which has been weighed down by China's tightening measures and weak global growth prospects. Both exports and imports registered stronger-than-expected growth for August (exports: 24.5% y/y; imports: 30.2% y/y), well above consensus expectations (exports: 21.9%; imports: 21.0%), resulting in a narrower trade surplus of USD 17.8 billion (July: USD 31.5 billion). The detailed breakdown of exports showed increased trade with other emerging markets, along with strong demand from Japan as its economy continues to rebound, post-earthquake. On the other hand, exports to Europe declined and those to US remained flat. The fast growth of imports is a sign of robust domestic demand, particularly for energy-intensive commodities such as oil and iron ore. On the monetary front, data released this past week on money supply (Chart 5) and credit growth (Chart 6) also showed further strong domestic demand, in line with our projected soft landing. New loans came in at RMB 548.5 billion in August (consensus: RMB 500 billion), indicating that liquidity conditions are somewhat better than expected. Overall credit growth registered 14.8% y/y (July: 15.0% y/y) and money supply growth (M2) came to 13.5% y/y (July: 14.7% y/y), on the effects of recent tightening measures. We believe the tightening cycle is near an end, as the growth outlook is increasingly becoming the authorities' focus given the uncertain external outlook, despite still high inflation (6.1% y/y in August). As such, monetary policy has entered a wait-and-see phase in which our previous expectation of one more rate hike before the end of the year appears unlikely. While some market participants now anticipate monetary easing, we think this is also unlikely given high inflation and still strong domestic demand.

Chart 5
China: M2 growth being curtailed...



Source: BBVA Research and Bloomberg

Chart 6
...while loan growth is also reigned in



Source: BBVA Research and Bloomberg

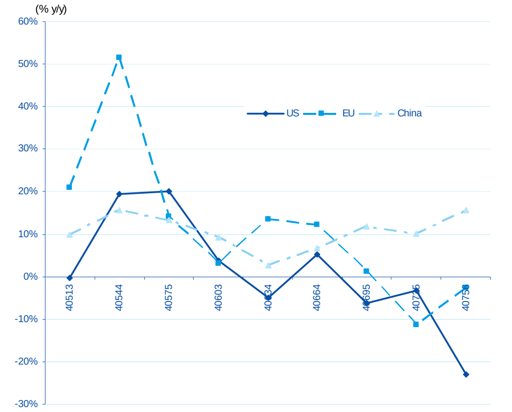
India: RBI stays firm on inflation with a rate hike despite risks to growth

The past week was an eventful one for India on the economic data and policy fronts, as rising downside risks to growth, persistent inflationary pressures and a sharply weaker currency clouded the economic outlook in the run up to today's central bank policy meeting. In an effort to tame inflation expectations – WPI inflation surged to a 12-month high of 9.8% y/y in August from 9.2% in July – and reinforce previous policy actions, the RBI raised the benchmark repo rate by another 25 bps to 8.25%, the 12th successive rate hike in the current cycle (350bps cumulatively). The move was in contrast to our out-of-consensus expectations of a pause, based on rapidly increasing downside risks to domestic growth. In recent months policy settings have become increasingly complex as the authorities contend with a combination of persistently high inflation and a rapidly worsening global environment that is exacerbating an ongoing slowdown in India's economic activity. Meanwhile, a sharp decline in the rupee this month, to a 16-month low driven by fears of a global hard landing, has added further to inflationary woes. The RBI has maintained its hawkish stance in today's policy meeting, leaving the door open for further policy action if inflation trajectory continues. However, looking ahead, we expect interest rates to have peaked as price trends are to slow, albeit gradually, amidst policies to alleviate food supply bottlenecks, favorable monsoon, and demand compression due to high interest rates and worsening prospects on the global front. Following a sub 8.0% y/y real GDP growth in 1H 2011, the slowing trend on the domestic growth front, namely IP, PMI, motor vehicle sales, and cement dispatches suggests further softening in economic activity, in turn raising downside risk to our growth outlook.

Singapore's better-than-expected exports are the latest sign of Asia's resilience

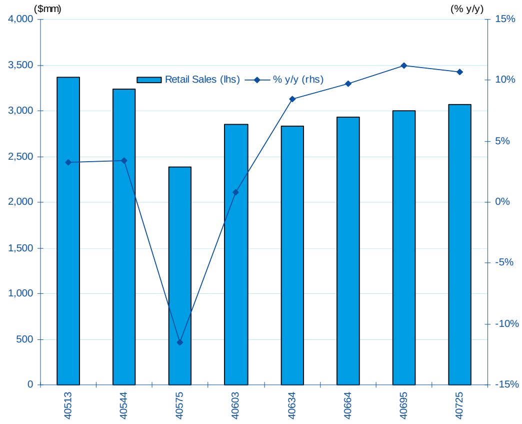
While the Asian economies are vulnerable to a global slowdown, much of the activity data so far continues to point to a surprising degree of resiliance (as we reported last week for China). The latest signs of this come from data released this week for one of the region's smallest and most open economies, Singapore. July retail sales (Chart 8) surprised to the upside (10.7% y/y, consensus 8.7% y/y), and export data released today were stronger-than-expected, with non-oil exports (Chart 7) growing in August by 5.1% y/y, well ahead of consensus estimates which were expecting a -6.5% y/y contraction. Seasonally adjusted, exports rose 8.3% m/m, also well ahead of expectations of 0.5%. Such data for Singapore are notoriously volatile, and the strength may prove to be temporary, as the upswing was due to strong sales of ships, boats and optical equipment. Electronics exports continued to slump, however, posting a -19.4% y/y decline due to weakening demand from the EU (-2.5% y/y) and the US (-23.1% y/y). Demand for PC's and computer chips was weak, a possibly ominous sign as the holiday season approaches in developed countries. It was a different story for exports to China, as strong demand (15.7% y/y) from the second largest buyer of Singapore's electronics buoyed Singapore's economy. For Singapore's policymakers, who remain wary of a looming recession, these results were a temporary reprieve from what had become a steady stream of troublesome data (2Q GDP, July CPI). The focus now will turn to next week's CPI release, which will help shape expectations before the Monetary Authority of Singapore's bi-annual policy meeting in mid-October, in which we currently expect no change to the policy stance.

Chart 7
Singapore: Exports remain strong....



Source: CEIC and BBVA Research

Chart 8
...while retail sales surprise to the upside



Source: CEIC and BBVA Research

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Calendar Indicators

China	Date	Period	Prior	Cons.
HSBC Flash China Manufacturing PMI	22-25 SEP	SEP	49.9	- -
Hong Kong	**Date**	**Period**	**Prior**	**Cons.**
Unemployment Rate SA	20-Sep	AUG	3.4%	- -
Bal of Paymts - Current A/C	22-Sep	2Q	$40.64B	- -
Bal of Paymts - Overall	22-Sep	2Q	$18.69B	- -
CPI - Composite Index (YoY)	22-Sep	AUG	7.9%	5.8%
Japan	**Date**	**Period**	**Prior**	**Cons.**
Convenience Store Sales YoY	20-Sep	AUG	9.5%	- -
Merchnds Trade Balance Total	21-Sep	AUG	¥72.5B	-¥300B
Adjusted Merchnds Trade Bal.	21-Sep	AUG	-¥130.5B	-¥22.1B
Merchnds Trade Exports YoY	21-Sep	AUG	-3.3	8.0
Merchnds Trade Imports YoY	21-Sep	AUG	9.9	14.3
All Industry Activity Index (MoM)	21-Sep	JUL	2.30%	0.5%
Supermarket Sales (YoY)	22-Sep	AUG	2.10%	- -
Malaysia	**Date**	**Period**	**Prior**	**Cons.**
CPI YoY	21-Sep	AUG	3.4%	3.3%
Philippines	**Date**	**Period**	**Prior**	**Cons.**
Balance of Payments	19-Sep	AUG	$1270M	- -
Budget Deficit/Surplus	19-25 SEP	AUG	-26.5B	- -
Singapore	**Date**	**Period**	**Prior**	**Cons.**
CPI (MOM) - NSA	23-Sep	AUG	1.5%	- -
CPI (YoY)	23-Sep	AUG	5.4%	- -
Korea	**Date**	**Period**	**Prior**	**Cons.**
Department Store Sales YoY	18-20 SEP	AUG	8.5%	- -
Discount Store Sales YoY	18-20 SEP	AUG	4.9%	- -
Unemployment Rate (SA)	21-Sep	AUG	3.3%	- -
Taiwan	**Date**	**Period**	**Prior**	**Cons.**
Export Orders (YoY)	20-Sep	AUG	11.1%	7.6%
Unemployment Rate - sa	22-Sep	AUG	4.4%	4.4%
Commercial Sales (YoY)	23-Sep	AUG	4.61%	5.1%
Industrial Production (YoY)	23-Sep	AUG	3.93%	4.0%
Thailand	**Date**	**Period**	**Prior**	**Cons.**
Customs Exports (YoY)	20-23 SEP	AUG	38.30%	- -
Customs Imports (YoY)	20-23 SEP	AUG	0.135	- -
Customs Trade Balance	20-23 SEP	AUG	$2798M	- -

Indicator of the Week: Taiwan August Export Orders (September 20)

Forecast: 7.8% y/y	Consensus: 7.6% y/y	Prior: 11.1% y/y

Comment: As a leading indicator of actual exports for the ensuing 1 to 3 months, Taiwan's export orders are a good gauge of global demand. Weakness in US and European growth are already having an impact on Taiwan's export performance, which is closely watched given the economy's position in the global supply chain. Nevertheless, robust demand from mainland China is proving to be a support to export demand, especially for information and communication products. Market Impact: A worse than expected outturn could undermine confidence in Asia's growth outlook, and solidify expectations that the rate hike cycle has ended.

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Calendar Events

Australia – Reserve Bank's Board September Minutes, September 20

Markets Data

STOCK MARKETS

INDEX	Last price	% change over a week	Year to date	% Change over 1 Y
China – Shanghai Comp.	2489.4	-0.3	-11.3	-4.3
Hong Kong – Hang Seng	19591.9	-1.4	-14.9	-9.7
Taiwan – Weighted	7594.9	-0.2	-15.4	-6.2
Japan – Nikkei 225	8840.5	1.2	-13.6	-7.0
Korea – Kospi	1832.1	1.1	-10.7	1.1
India – Sensex 30	17045.3	1.1	-16.9	-12.2
Australia – SPX/ASX 200	4150.3	-1.1	-12.5	-9.9
Singapore – Strait Times	2804.1	-0.7	-12.1	-8.6
Indonesia – Jakarta Comp	3808.1	-4.8	2.8	14.0
Thailand – SET	1043.0	-1.8	1.0	12.8
Malaysia – KLCI	1430.9	-2.6	-5.8	-2.9
Philippines – Manila Comp.	4290.2	-1.3	2.1	7.1

Last update: Friday, 12.20 Hong Kong time.

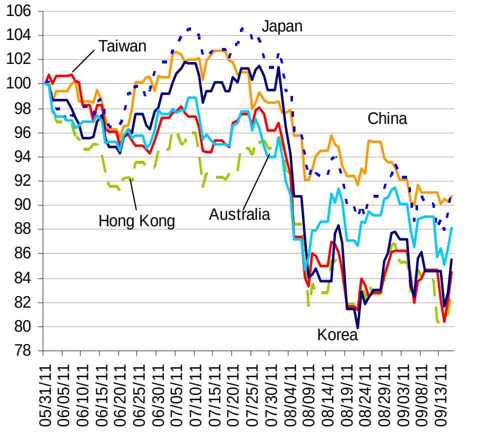
FOREIGN EXCHANGE MARKETS

CURRENCY	Spot	% change over a week	Forward 3-month	Forward 12-month
China (CNY/USD)	6.38	0.08	6.36	6.32
Hong Kong (HKD/USD)	7.79	0.10	7.78	7.75
Taiwan (TWD/USD)	29.5	-1.12	29.36	28.87
Japan (JPY/USD)	76.8	1.07	76.70	76.32
Korea (KRW/USD)	1104	-2.44	1110	1113
India (INR/USD)	47.4	-1.82	48.10	49.05
Australia (USD/AUD)	1.04	-1.15	0.98	n.a.
Singapore (SGD/USD)	1.24	-0.84	1.24	1.23
Indonesia (IDR/USD)	8774	-2.23	8922	9268
Thailand (THB/USD)	30.3	-0.89	30.56	31.06
Malaysia (MYR/USD)	3.09	-2.75	3.10	3.12
Philippines (PHP/USD)	43.3	-1.66	43.33	43.46

Last update: Friday, 12.20 Hong Kong time.

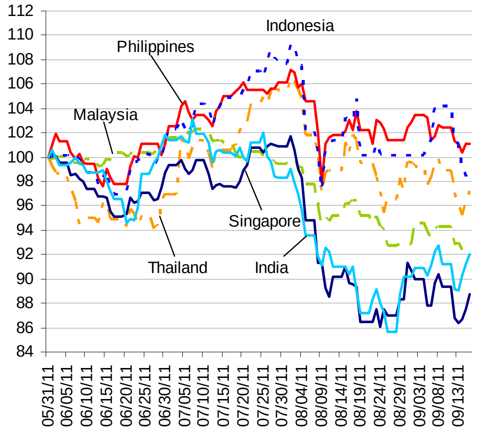
Charts

Chart 9
Stock Markets



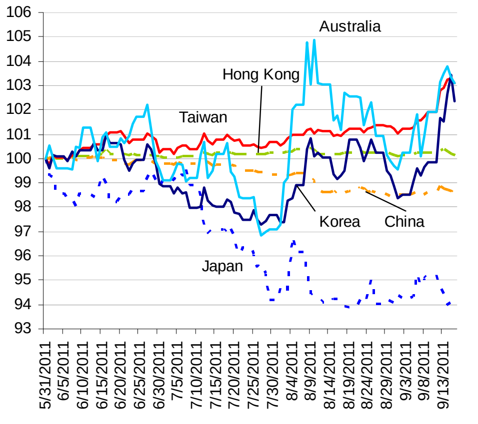
Source: BBVA Research and Bloomberg

Chart 10
Stock Markets



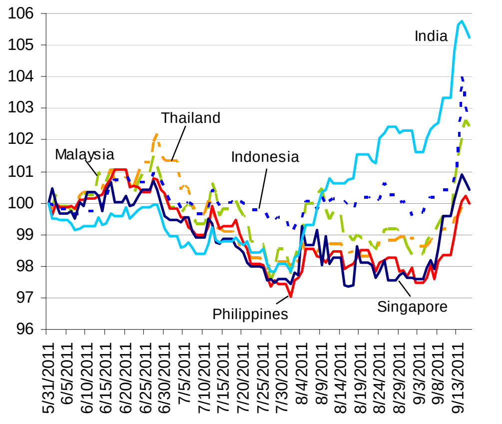
Source: BBVA Research and Bloomberg

Chart 11
Foreign Exchange Markets



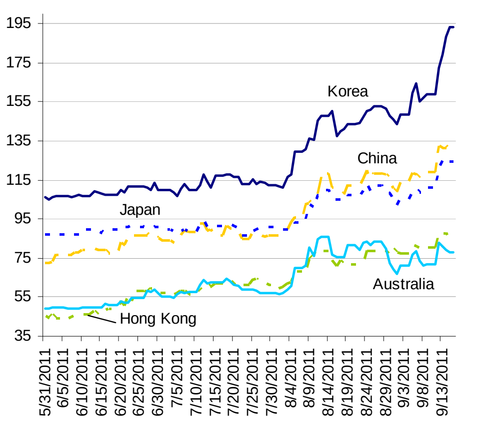
Source: BBVA Research and Bloomberg

Chart 12
Foreign Exchange Markets



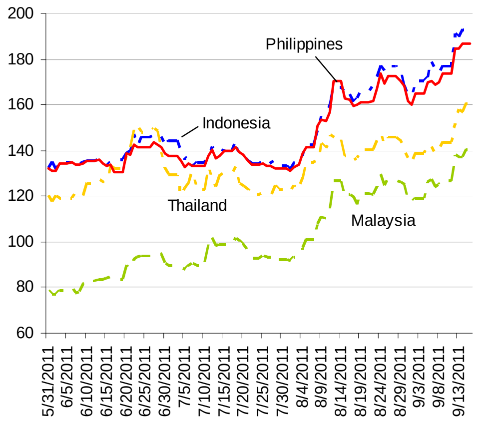
Source: BBVA Research and Bloomberg

Chart 13
Credit Default Swaps



Source: BBVA Research and Bloomberg

Chart 14
Credit Default Swaps



Source: BBVA Research and Bloomberg

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