

Daily Breakfast Spread

DBS Group Research

30 July 2010

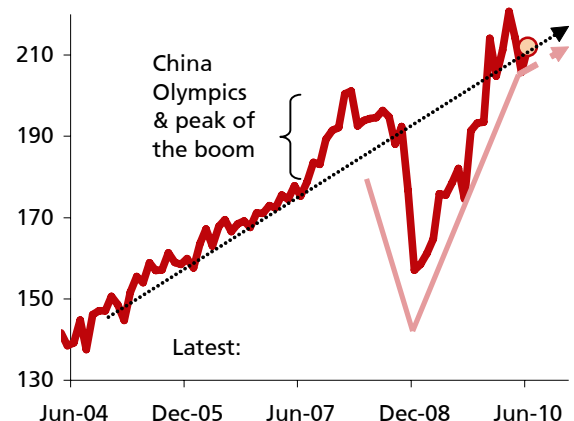
Economics

Southeast Asia, India

- TH:** June economic and balance of payments data are out today. As usual, the customs trade data out a week earlier has provided guidance not just for the balance of payments data but also for the general economy including the manufacturing sector. Trade numbers should be similar to the customs data with export and import growth likely to print 47% (YoY) and 37% (YoY). We expect the current account balance to record a surplus of over USD 2bn, not too far from the trade surplus of USD 2.5bn registered in the customs data. In sequential terms, the customs exports imply a rise of 7% (MoM, sa) in exports. We think this suggests a 3% (MoM, sa) rise in manufacturing production which works to 19% (YoY) growth, similar to consensus forecasts (Chart). The central bank last Friday upgraded its GDP forecasts for 2010 and 2011 to 7% from 5% forecasted in April. This upgrade continues to underestimate GDP growth prospects. We think the June customs data clearly points to upside risk to our GDP forecast of 7%. The central bank's core inflation forecasts for 2011 – the relevant variable for monetary policy decisions – has been maintained at 2%. The GDP upgrade by itself doesn't alter the interest rate policy outlook (since it is in line with our current GDP forecast). However, the strong June customs trade data certainly increase upside risk to the growth and interest rate outlook.

TH: Manufacturing production - square root

2000=100, SA



US Fed expectations

Implied fed funds rate

	Sep-10	Dec-10	Mar-11
Market			
Current	0.19	0.19	0.27
1wk ago	0.19	0.19	0.23
DBS	0.25	0.25	0.50

Source: Bloomberg fed fund futures

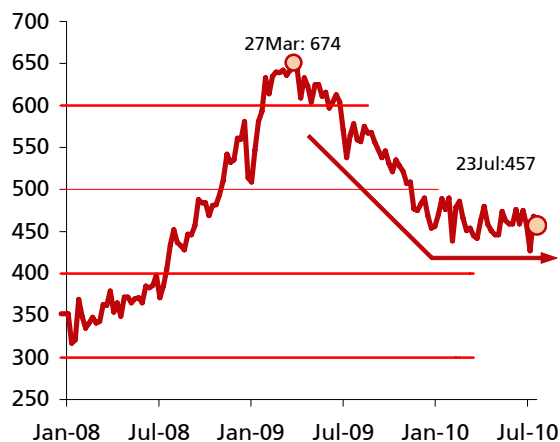
Notes: Given a FF target rate of 0.25%, an implied FF rate of 0.30 is interpreted roughly as the market pricing in a 20% chance of a Fed hike to 0.50% from 0.25% (30 is 1/5th of the distance to 50 from 25). DBS expectations are presented in discrete blocks of 25bps, i.e., the Fed moves or it does not. See also "Policy rate forecasts" below.

G3

- US:** We have altered our Fed forecast owing mainly to a labor force that seems to be stuck permanently in neutral. After solid improvement through the 12 months of 2009 (chart below left), initial jobless claims hit a roadblock in January 2010 and have remained stuck at about 460k per week ever since. Yesterday's outcome of 457k for the week of July 24 is but another rock chiseled from the same clogged data pipe. Nonfarm payrolls fell by 125k last month and consensus expects another 70k loss in next week's July reading. Much of that loss is census-related (thus offsetting the artificial positive readings back in April/May). But even the expected 100k rise in private sector payrolls is less than the 115k-125k new jobs needed just to 'break even' with growth in the labor force and keep the unemployment rate from rising. As one can see from the chart below right, we need to see weekly jobless claims down around 300k-350k (100k below current levels) before appreciable improvement in payrolls can be expected. Against this backdrop, and with core inflation still running at about 1% YoY (juxtaposed against an unofficial Fed target of 1.5% to 2%), we have pushed our forecast of Fed funds approximately one quarter further into the future. We now anticipate a first

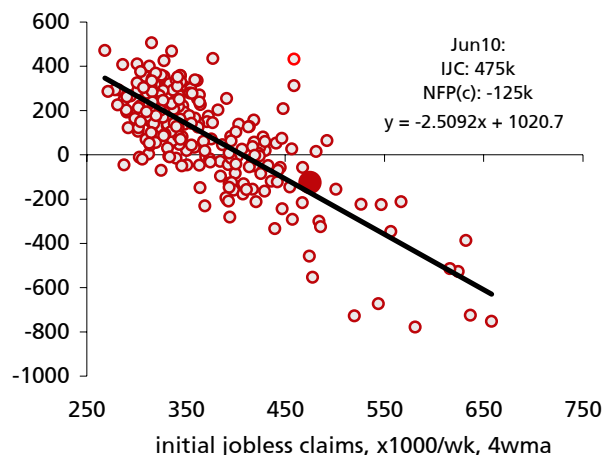
US - initial jobless claims

thousand claims/week, seas adj



US - initial jobless claims and nonfarm payrolls

NFP, x1000/mth, Jan90-present



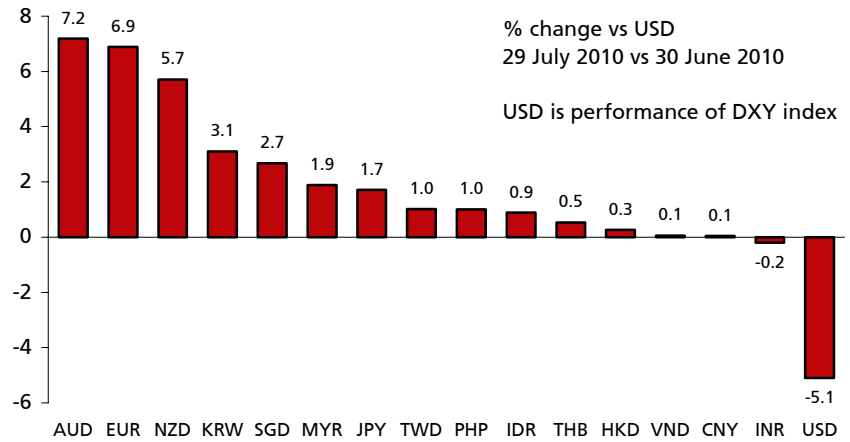
Fed hike in 2Q11 (rather than 1Q11) and expect Fed funds to end the year (2011) at 1.50% rather than 2.00%. With respect to the expected timing of the first hike, this change puts us on the same page as markets (as proxied by Fed fund futures) where a first hike is fully priced in about June. We remain more aggressive than markets, however, with respect to Fed funds at year-end. Markets expect Fed funds to end the year at about 0.75%, some 125bps lower than the 2% rate that was priced in just 3 months ago in April before the EU / Greek debt crisis took center stage. But markets have calmed considerably in the past month as investors reassess the likely impact from Europe and identified more clearly the banks most exposed to weak credits. Libor and Libor-OIS spreads are falling back toward April levels and it seems likely that, as this proceeds, market expectations as regards the Fed will turn tail as well.

On the data front, 2Q GDP is on tap today. Growth of 2.6% (QoQ, saar) is expected, as discussed in more detail here through the week. For the record, we expect consumption growth of 2.8% (nearly the long-run average of 3%), business investment growth of 7%-8% and zero contribution from inventories. A volatile housing sector will be responsible for cutting overall GDP growth to 2.6% when 3% would otherwise have been expected.

Currencies

- Euro bears were badly bruised when broad-based USD weakness returned in July. The DXY (USD) index fell 5.1% when focus shifted to US's sluggish recovery after the Eurozone sovereign debt crisis stabilized. The commodity currencies – AUD and NZD – were the main beneficiaries with 7.2% and 5.7% gains respectively. Worries over a double-dip recession receded after central banks in Malaysia (+25bps to 2.75% on July 8), South Korea (+25bps to 2.25% on July 9), Thailand (+25bps to 1.50% on July 14), Canada (+25bps to 0.75% on July 20), New Zealand (+25bps to 3.00% on July 29) and India (+25bps to 5.75% on July 27) hiked interest rates. Currencies in these countries that hiked rates generally performed better except for India where inflation became a problem. As it becomes more evident that the worst was over, speculators were further forced to cover their record net short EUR and GBP positions, just as others began to accumulate net long AUD positions again. Looking ahead, the US dollar is expected to remain under pressure as risk appetite returns. Policy-wise, the US will want to prevent a widening US trade deficit from subtracting headline GDP growth, especially when consumer spending is constrained by renewed weakness in the housing sector and slow job creation. With American voters concerned about the still-wide budget deficit, and the Fed keeping rates ultra-low to nurture the recovery, policymakers will not mind a weaker USD to lift exports. Hence, US lawmakers are also likely to pressure China once more to allow more appreciation in the Chinese yuan ahead of the US mid-term elections in November.

USD weakness was the theme in July



Looking Back

- US mkts:** US stocks fell overnight on disappointing earnings reports from Kellogg and Colgate-Palmolive. The Dow Jones Industrial Average fell 0.29% to 10467.16 and the Nasdaq closed 0.57% lower at 22511.69. Treasury yields fell 2bps to 0.6% in the 2Y sector and were little changed around 3% in the 10Y sector.

Economic calendar

Event	Consensus	Actual	Previous
July 26 (Mon)			
US: Chicago fed NAI (Jun)		-0.63	0.21
US: new home sales (Jun)	311K	330K	300K
KR: GDP (2Q, A)	1.3% q/q sa	1.5% q/q sa	2.1% q/q sa
SG: industrial production (Jun)	38.4% y/y	26.1% y/y	58.6% y/y
July 27 (Tue)			
US: consumer confidence (Jun)	51.0	50.4	54.3
US: S&P/CS home prices (May)	0.20% m/m sa	0.47% m/m sa	0.61% m/m sa
PH: trade balance (May)		-USD 513 m	-USD 937 m
PH: imports (May)		31.4% y/y	48.2% y/y
HK: trade balance (May)	HKD -25.6 bn	HKD -30.6 bn	HKD -25.1 bn
-- exports	22.8% y/y	26.7% y/y	24.4% y/y
GDP CQOQ Index	25.2% y/y	31.0% y/y	29.7% y/y
July 28 (Wed)			
US: durable goods order (Jun)	1.0% m/m sa	1.0% m/m sa	-0.8% m/m sa
KR: current account (Jun)		\$5037.5mn	\$3818.4mn
July 29 (Thur)			
US: continuing jobless claims	4500K	4565K	4487K
July 30 (Fri)			
US: Chicago PMI (Jul)	56		59.1
US: GDP (2Q, A)	2.6% q/q saar		2.7% q/q saar
KR: industrial production (Jun)	16.5% y/y	16.9% y/y	21.5% y/y
MY: M3			9.5% y/y
TH: manufacturing production (Jun)	18.5% y/y		17.2% y/y
TH: capacity utilization (Jun)			67.3%
TH: current account (Jun)	\$2000mn		\$1039mn
TH: exports (Jun)			42.5% y/y
imports (Jun)			53.5% y/y
trade balance (Jun)			USD 2299mn
SG: bank loans & advances (Jun)			8% y/y
SG: money supply M2 (Jun)	18.0% y/y		9% y/y
SG: unemployment rate (2Q)	2.1% sa		2.2% sa
JN: industrial production (Jun)	18.9% y/y	17.0% y/y	20.4% y/y
JN: natl CPI	-0.7% y/y	-0.7% y/y	-0.9% y/y
JN: jobless rate	5.20%	5.30%	5.20%

Central bank policy calendar

Date	Country	Policy Rate	Current	Consensus	DBS	Actual
This week						
27-Jul	IN	O/N repo	5.50%	5.75%	5.75%	5.75%
27-Jul	IN	O/N reverse repo	4.00%	4.25%	4.25%	4.50%
27-Jul	IN	cash reserve ratio	6.00%	6.00%	6.00%	6.00%
Next week						
4-Aug	ID	o/n reference rate	6.50%	6.50%	6.50%	
5-Aug	EZ	refi rate	1.00%	1.00%	1.00%	
Last week						
no meetings						

GDP & inflation forecasts

	GDP growth, % YoY					CPI inflation, % YoY				
	2007	2008	2009	2010f	2011f	2007	2008	2009	2010f	2011f
US	2.1	0.4	-2.4	3.2	2.9	2.9	3.8	-0.3	2.0	2.1
Japan	2.4	-1.2	-5.1	2.8	1.8	0.1	1.4	-1.4	-0.4	0.5
Eurozone	2.7	0.5	-4.0	0.6	1.0	2.1	3.3	0.3	0.8	1.0
Indonesia	6.3	6.0	4.5	5.5	5.5	6.4	9.8	4.9	4.7	6.3
Malaysia	6.2	4.6	-1.7	8.0	5.5	2.0	5.4	0.6	1.8	2.4
Philippines	7.1	3.8	0.9	6.2	4.9	2.8	9.3	3.3	4.0	4.4
Singapore	8.2	1.4	-1.3	15.0	4.5	2.1	6.5	0.6	3.0	2.7
Thailand	4.9	2.5	-2.2	7.0	4.0	2.2	5.5	-0.8	3.5	2.2
Vietnam	8.4	6.2	5.3	6.5	6.9	8.3	23.1	7.0	9.0	8.0
China	13.0	9.6	8.7	11.0	10.0	4.8	5.9	-0.7	4.0	3.0
Hong Kong	6.4	2.1	-2.7	5.5	4.5	2.0	4.3	0.5	3.0	3.0
Taiwan	6.0	0.7	-1.9	7.5	3.8	1.8	3.5	-0.9	0.9	1.4
Korea	5.1	2.3	0.2	6.2	3.9	2.5	4.7	2.8	2.9	3.1
India*	9.2	6.7	7.4	8.8	8.5	4.7	8.4	3.7	8.0	5.3

* India data & forecasts refer to fiscal years beginning April; inflation is WPI
Source: CEIC and DBS Research

Policy & exchange rate forecasts

	Policy interest rates, eop					Exchange rates, eop				
	current	3Q10	4Q10	1Q11	2Q11	current	3Q10	4Q10	1Q11	2Q11
US	0.25	0.25	0.25	0.25	0.50	...	...	...	...	...
Japan	0.10	0.10	0.10	0.10	0.20	86.8	94	95	96	94
Eurozone	1.00	1.00	1.00	1.00	1.25	1.306	1.26	1.28	1.30	1.32
Indonesia	6.50	6.75	7.25	7.75	8.00	8,943	9,200	9,100	9,000	8,900
Malaysia	2.75	2.75	3.00	3.25	3.25	3.19	3.22	3.20	3.18	3.16
Philippines	4.00	4.25	4.50	4.75	5.00	45.7	45.7	45.5	45.3	45.1
Singapore	n.a.	n.a.	n.a.	n.a.	n.a.	1.36	1.38	1.37	1.36	1.35
Thailand	1.50	1.75	2.00	2.50	2.75	32.3	32.4	32.2	31.9	31.7
Vietnam [^]	8.00	8.00	8.00	8.00	8.00	19,075	19,310	19,420	19,450	19,450
China*	5.31	5.58	5.85	6.12	6.39	6.78	6.74	6.69	6.64	6.60
Hong Kong	n.a.	n.a.	n.a.	n.a.	n.a.	7.77	7.75	7.75	7.75	7.75
Taiwan	1.38	1.50	1.75	2.00	2.25	32.0	31.9	31.7	31.5	31.3
Korea	2.25	2.50	3.00	3.50	3.75	1188	1160	1150	1140	1130
India	5.75	5.75	6.25	6.50	6.50	46.5	45.8	45.6	45.4	45.2

[^] prime rate; * 1-yr lending rate

Market prices

	Policy rate	10Y bond yield		FX		Equities		
	Current (%)	Current (%)	1wk chg (bps)	Current	1wk chg (%)	Index	Current	1wk chg (%)
US	0.25	2.97	-2	81.6	-1.0	S&P 500	1,102	0.7
Japan	0.10	1.09	1	86.8	0.6	Topix	861	4.3
Eurozone	1.00	2.72	5	1.306	1.7	Eurostoxx	2,487	1.0
Indonesia	6.50	8.10	-16	8943	1.2	JCI	3,097	2.9
Malaysia	2.75	3.91	1	3.19	0.2	KLCI	1,358	1.7
Philippines	4.00	7.63	-2	45.7	1.5	PCI	3,429	0.4
Singapore	Ccy policy	2.05	-15	1.364	0.6	FSSTI	2,998	1.4
Thailand	1.50	3.44	0	32.3	-0.1	SET	855	2.8
China	5.31	...	...	6.78	0.1	S'hai Comp	2,648	3.3
Hong Kong	Ccy policy	2.24	2	7.77	0.0	HSI	21,094	2.4
Taiwan	1.38	1.38	-2	32.0	0.4	TWSE	7,799	1.7
Korea	2.25	4.84	-5	1187	1.0	Kospi	1,771	2.0
India	5.75	7.79	12	46.5	0.9	Sensex	17,992	-0.7

Source: Bloomberg

* 1yr lending rate

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