Economics & Strategy Research

Macro Insights Weekly

Recession watch resumes

Economics/Strategy/Rates/FX/Credit

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Taimur Baig
Chief Economist
taimurbaig@dbs.com

Radhika Rao
Economist
radhikarao@dbs.com

Please direct distribution queries to
Violet Lee +65 68785281 violetleeyh@dbs.com

- *COVID-19 related disruptions to production (supply side) and travel and transportation (demand side) are pushing up recessionary risks worldwide*
- *Supply side disruptions could be temporary and somewhat compensated by extra shifts of production when pandemic fears ebb*
- *But weaker demand and lower margins (as services like travel decline, pushing down energy use and price) could cause prolonged impact on earnings and employment*
- *Many DM and EM economies could report zero or negative growth in 1H20. With limited monetary and fiscal room left in many economies, policy may not be able respond decisively to such slowdown.*
- *With debt at record levels, and much of it dependent on non-bank financing, policy rates at their floor may not be sufficient to prevent a credit crunch and corporate distress.*
- ***We expect Fed fund rates to go to zero by the middle of this year; ECB and BoJ would ease further as well.***

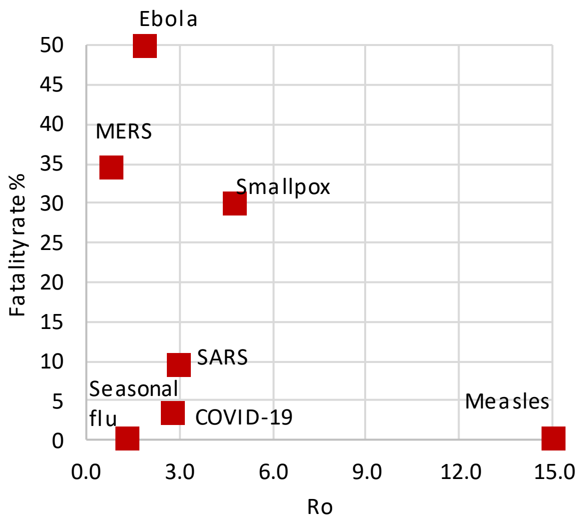
Key data release and events this week:

- *We expect China's inflation to stay elevated, but India's to decelerate from the January's peak*
- *ECB is likely to lower the deposit facility rate, on the heels of US Fed's surprise cut last week*
- *Malaysia IP is expected to slip into red*

Chart of the Week: Fatality rate vs Ro

Epidemiologists look at fatality rate and R_0 (reproduction rate of a virus) when gauging the dimensions of an epidemic. As per data from WHO, COVID-19 is more infectious than MERS or Ebola, but much less fatal. The key public health challenge going forward is to reduce Ro by a mix of treatment and quarantine of patients, improving sanitation, and in some cases, lockdown of population.

Two dimensions of contagious diseases



Commentary: Recession watch resumes

A torrid week for the global economy and markets, starting with a G-7 communique and 50bps rate cut by the US Federal Reserve, ending with wider spread of COVID-19 worldwide, even as infections fell in China and activity began to resume there. Auto, airline, hotel, and commodity-related outlook has continued to darken, while it is still not clear the extent to which supply-side disruptions would hit product shelves in the months ahead.

Surging gold, plunging oil and USD, and the entire US yield curve below 1%, the markets have started this week with an extent of nervousness not seen since the 2008/09 global financial crisis. Unlike then, there is no question of bank liquidity drying up; there have also been no systemic risk manifestation yet. But another differentiating factor is that there is perhaps less clarity now. During the GFC, it was clear that central bank intervention was needed to stem financial sector distress and fiscal policy was needed to offset the ensuing recession. Today, there is considerably more uncertainty about the extent of damage to activities and sentiments.

As policy makers and public health officials continue to grapple with the outbreak, the uncertainty is palpable in market pricing. US yield curve remains inverted despite the 50bps cut in the Fed funds rate, with the 10-year yield hitting historic lows day after day. The fixed income market appears to be pricing in a return to the zero bound by June.

COVID-19 related disruptions to production (supply side) and travel and transportation (demand side) are pushing up recessionary risks worldwide, in our view. Granted, supply side disruptions could be temporary and somewhat compensated by extra shifts of production when pandemic fears ebb. But weaker demand and lower margins (as services like travel decline, pushing down energy use and price) could cause prolonged impact on earnings and employment worldwide.

We think many DM and EM economies could report zero or negative growth in 1H20. With limited monetary and fiscal room left in many economies, policy may not be able respond decisively to such slowdown. With debt at record levels, and much of it dependent on non-bank financing, policy rates at their floor may not be sufficient to prevent a credit crunch and corporate distress.

Back to the US, Credit spreads in the high yield sector are widening, especially in the sectors related to transportation, hospitality, and energy. We think the incipient risk to credit markets was the key deciding factor in driving the Fed into cutting rates last Monday. With market pricing so decisively in favour of further cuts, and considerable risk of further outbreak in the horizon, **we are inclined to go along with calling for another 50bps of rates cuts later this month and zero bound being reached during the first half of the year.**

China's markets may have held up rather well due to the improving data on infections, the world's second largest economy is not remotely close to being out of the woods. A resurgence of infection as workers go back to work could unravel the ongoing narrative of gradual normalisation. Moreover, as the outbreak disrupts activities overseas, intermediate goods that Chinese manufacturers depend upon may not come in desired quantity and pace. Expectations of a V-shaped recovery will have to be tempered, in our view. Our risk scenario of growth going down to 4.5% is swiftly in danger of becoming the baseline.

Taimur Baig

This Week in key data releases and events

Event	DBS	Previous
Mar 9 (Mon)		
Taiwan: exports (Feb)	2.4% y/y	-7.6% y/y
- imports	10.4% y/y	-17.7% y/y
- balance	USD3.96bn	USD3.5bn
Mar 10 (Tue)		
Philipp: exports (Jan)		21.4% y/y
- imports		-7.6% y/y
- balance		-USD2.5bn
China: CPI (Feb)	5% y/y	5.4% y/y
Eurozone: GDP (4QF)	0.9% y/y	0.9% y/y
China: new yuan loans (Feb)	CNY1500bn	CNY3340bn
China: M2 (Feb)	8.5% y/y	8.4% y/y
Mar 11 (Wed)		
US: CPI (Feb)	2.3% y/y	2.5% y/y
Mar 12 (Thurs)		
India: CPI (Feb)	6.6% y/y	7.6% y/y
India: industrial prod (Jan)	0.8% y/y	-0.3% y/y
Eurozone: ECB main refi rate	0%	0%
ECB d.f.rate	-0.60%	-0.50%
Mar 13 (Fri)		
India: exports (Feb)	-3.2% y/y	-1.7%y/y
- imports	8% y/y	-0.8% y/y
- balance	-USD14bn	-USD15.2bn
Malaysia: industrial prod (Jan)	-5.8% y/y	1.3% y/y

China: Partly due to the usual Lunar New Year effect, where corporates hoards for cash before the festival, the new yuan loan is expected to have fallen from CNY3340bn in January to CNY1500bn in February. More importantly, the widespread of COVID-2019 should have also dragged loan demand. On the supply side, M2 growth is expected to increase from 8.4% to 8.5% amid aggressive monetary easing. For instance, the PBOC cut has cut the 1 Year LPR from 4.15% to 4.05%. As such, CPI should stay elevated at 5.0%. This is also partly a result of the short-term shortage of necessities during the early stage of COVID-2019 outbreak. Consumer price levels should return to a more stable level in the months ahead.

India: February CPI inflation is expected to decelerate to 6.6% y/y from a peak of 7.6% last month. High-frequency food staples and proteins have softened on MoM basis, along with lower fuel prices. Core inflation should also pullback from 4% levels last month. Industrial production is expected to return to small black on better utilities and manufacturing output (on restocking demand). Outlook for 1Q20 is, however, clouded by COVID-19 related supply chain disruptions. Hopes are that supplies will resume as China returns to work gradually.

Malaysia: Industrial production figure for Jan20 is likely to show the first monthly contraction in seven years. A decline of 5.8% has been penciled into our forecast and risk is on the downside. While some producers may opt to front-load their production ahead of the Lunar Year New at the end of the month, which will provide some respite, output level is usually down during the festive season, plus this coincides with a high base in the same period last year. Yet, this risk is that this could be a protracted contraction that could last for months, as extended plant closures within China due to the Covid-19 outbreak will indirectly weigh down on output in Malaysia. China accounts for about 14.2% of Malaysia's total exports. This impact from Covid-19 will be more pronounced in the next 1-2 months.

Taiwan: Exports are expected to rise 2.4% YoY in February, but average only -2.6% in the entire Jan-Feb period. As inferred from the moderate decline in February manufacturing PMI (49.9), the supply-side disruptions caused by China's COVID-19 outbreak are not very severe for Taiwan for the time being. That said, the adverse impact on Taiwan's exports demand remains a warranted concern. This will be showed by February's trade figures.

Economics Team

Macro Strategy

Rates: Pandemic crisis

Heightened uncertainties on COVID would probably prompt more policy support across the globe in the coming few months. The Fed's emergency 50bps will probably not be the last and **we expect the Fed to cut to 0-0.25% range by mid-2020. Odds another inter-meeting cut and / or QE are elevated.** This would take the Fed funds range to 0.25-0.50% range, just a notch above the all-time low registered when the Fed had to deal with the Global financial crisis. With the Fed giving the green light for easing, G10 central banks will follow suit. The Reserve Bank of Australia (RBA) acted before the Fed while the Reserve Bank of Canada followed immediately after. There are also speculation of imminent cuts from the Bank of England (BOE) and **a token move from the European Central Bank (ECB).** Meanwhile, the Bank of Japan (BOJ) may be the most reluctant to ease further. **We doubt the BOJ would cut rates** and would instead opt to buy selected assets if needed.

Peak fear of COVID in the US and Europe will soon be upon us. In Asia, worries about the Chinese economy appears to have dissipated as firm measures led to a sharp drop in infections. Moreover, there are signs that the economy is normalizing, albeit slowly. We suspect that a bottom in longer-term developed market rates may be found within the next few weeks. All eyes will be on how Europe and the US contain the virus outbreak. News flow is likely to be interpreted negatively and this could nudge USD rates even lower. We are particularly **worried that the COVID-19 episode could lead to persistent credit stresses in global markets.** During the Global Financial Crisis, it took coordination between the Fed and the government to unfreeze credit markets. Accordingly, it would be less damaging for the markets and the real economy if the authorities (central banks and governments) act quickly to ease these conditions. **Our sense is that things could get worse before getting better.** Events could eventually play out similarly to China, with virus fatigue and / or containment occurs, allowing sentiment to stabilize.

We think steepening trades will no longer work with sentiment getting worse. TINA (there is no alternative) is already kicking in and we might see **bull flattening if sentiment worsens as we expect.**

Selected Asian economies have already embarked on fiscal and monetary stimulus to cushion the ongoing slowdown. The Fed's willingness to cut rates will allow economies with mid-to-high interest rates (China, India, Indonesia, Malaysia and the Philippines) room to ease. In the short term, with sentiment dicey, we reiterate that **China and Singapore govvies offer significant yield premium and will likely be viewed as safe haven plays.** Once market volatility settles, the lower for longer narrative will prompt a search for carry. Demand for yield coupled with likely easing from Indonesia and India in the coming months suggests that govvies will perform well beyond the current bout of volatility. **We have revised our interest rates forecasts lower across the board (see table below).**

Eugene Leow & Duncan Tan

FX: USD remains under pressure but watch the rearview mirror

The US dollar index (DXY) has given up its uptrend this month. The Fed's emergency rate cut on March 3 to cushion the US economy against COVID-19 has arrested the DXY's attempt to push above 100. This morning's 30% plunge in crude oil price has extended the slide in the US 10Y bond yield to below 0.50% amidst expectations for the Dow Jones Industrial Average to shed more than 5% when US markets open tonight.

The knee-jerk reaction has been to push the DXY lower towards 95 this morning. USDJPY has broken below its 105 level to its lowest level since November 2016. EURUSD has risen close to 1.14. It, however, remains to be seen if the Japanese and European policymakers will stay on the side line and allow their exchange rates to appreciate past pivotal levels (100 for USDJPY and 1.15 for EURUSD) at a time when their economies are considered weaker than the US and more vulnerable to COVID-19. Lest we forget, they did pledge in last week's G7 statement to join the Fed in delivering targeted action to address the impact from the epidemic.

So, pay attention to the European Central Bank meeting on March 12. Apart from a 10bps cut in the deposit facility rate, the ECB may tweak its TLTROs to alleviate liquidity squeezes arising from the epidemic. Falling oil prices help to lower EU inflation and facilitate more asset purchases. We have noted that EU 10Y bond yields may soon join the US in posting new record lows. Meanwhile, the next Bank of Japan meeting is scheduled on March 18-19. With the Japanese economy headed for a technical recession, the BOJ may favour deeper negative rates and tweak its yield curve control policy.

Philip Wee

Credit: No overt tightening in China

Chinese corporate stresses are surfacing amidst extended COVID-19 disruptions. We have previously warned that Chinese consumer cyclical firms are vulnerable given the expected fall-off in consumption. An indebted auto maker in Western China has now declared that it faces risks to raising funds for a bond repayment due in March. We maintain our view that specific risks to disproportionately hit industries are set to linger.

The good news is that overall credit conditions are unlikely to tighten overtly. In the securities markets, regulators have allowed a fast-track for the issuance of "anti-epidemic" corporate bonds, while state-linked investors have also been mobilized to support the bond market. Issuance volume has thus risen from previous Jan-Feb levels, even as real activity is still struggling to recover. Regulators have also streamlined processes for bond issuance.

Policy support for bank lending is still of prime importance, which includes RMB300bn of targeted PBoC funding for banks to lend to firms "combating" the epidemic, as well as increased regulatory forbearance. Loan repayments by Chinese SMEs scheduled between 25 January and 30 June can now be delayed without being recognized as problem loans. The waiver will also apply for all firms in Hubei, with the province being the worst hit in China. **With the support of regulators and encouragement from authorities, credit should continue to flow to Chinese firms despite current economic stresses.**

Chang Wei Liang

Reports in the past week

- India: Assessing prospects of bond index inclusion
- Coronavirus & supply chain: Electronics sector in focus
- Aftermath of the Fed rate cut; what will ECB do?
- G20, not G7, to follow Asia in easing
- MYR Rates: Navigating monetary, fiscal and politics
- China chartbook – How much the country has returned to work
- Oil price outlook: China and OPEC dimensions
- India's soft growth underscores need for easy policy
- Macro Insights Weekly: COVID-19 goes global

Growth, Inflation, Policy Rates & FX forecasts

	GDP growth, % YoY				CPI inflation, % YoY, ave			
	2018	2019f	2020f	2021f	2018	2019f	2020f	2021f
China	6.6	6.1	5.3	5.6	2.1	2.6	2.3	2.5
Hong Kong	3.0	-1.7	-0.9	1.5	2.4	2.7	2.5	2.5
India	6.8	5.3	5.1	6.0	4.0	3.7	5.1	4.2
*India (FY basis)**	*7.3*	*6.2*	*5.0*	*5.6*	*3.6*	*3.4*	*4.8*	*4.2*
Indonesia	5.2	5.0	5.0	5.1	3.2	3.1	3.4	3.2
Malaysia	4.7	4.3	4.6	4.6	1.0	0.7	1.6	1.8
Philippines**	6.2	5.9	6.0	6.3	5.2	2.8	3.5	3.3
Singapore	3.1	0.7	0.9	1.8	0.4	0.6	1.1	1.5
South Korea	2.7	2.0	2.2	2.3	1.5	0.4	1.5	1.3
Taiwan	2.7	2.7	2.3	2.2	1.3	0.6	1.0	1.1
Thailand	4.2	2.4	2.0	2.1	1.1	0.8	1.2	1.3
Vietnam	7.1	7.0	6.8	6.7	3.5	2.8	2.9	3.0
Eurozone	1.9	1.2	1.1	1.2	1.8	1.2	1.0	1.2
Japan	0.3	0.7	0.2	1.1	1.0	0.5	0.7	0.6
United States***	2.9	2.3	2.0	1.9	1.9	2.3	1.8	2.1

* refers to year ending March i.e. 2020 represents FY20 - year ending March 2020 ** new CPI series *** eop for CPI inflation

Exchange rates, eop

	Q1 20	Q2 20	Q3 20	Q4 20	Q1 21	Q2 21	Q3 21	Q4 21
USD/CNY	7.10	7.15	7.05	7.00	6.95	6.90	6.85	6.80
USD/HKD	7.78	7.80	7.78	7.77	7.76	7.76	7.75	7.75
USD/INR	72.5	73.5	73.0	72.0	71.5	71.0	70.5	70.0
USD/IDR	13900	14000	13800	13600	13500	13400	13300	13200
USD/MYR	4.25	4.30	4.25	4.20	4.18	4.16	4.14	4.12
USD/PHP	51.0	51.8	51.4	51.0	50.8	50.6	50.4	50.2
USD/SGD	1.41	1.43	1.42	1.41	1.40	1.39	1.38	1.37
USD/KRW	1210	1220	1200	1180	1160	1140	1120	1100
USD/THB	31.8	32.3	31.8	31.2	31.0	30.8	30.6	30.4
USD/VND	23300	23360	23330	23300	23270	23240	23210	23180
AUD/USD	0.66	0.64	0.65	0.66	0.67	0.67	0.68	0.68
EUR/USD	1.07	1.06	1.08	1.10	1.11	1.12	1.13	1.14
USD/JPY	113	115	113	111	110	109	108	107
GBP/USD	1.27	1.25	1.26	1.27	1.28	1.29	1.30	1.31

Australia, Eurozone and United Kingdom are direct quotes

Policy interest rates, eop

	1Q20	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	4Q21
China*	4.00	3.85	3.70	3.55	3.55	3.55	3.55	3.55
India	5.15	4.90	4.65	4.65	4.65	4.65	4.65	4.65
Indonesia	4.50	4.25	4.25	4.25	4.25	4.25	4.25	4.25
Malaysia	2.50	2.25	2.00	2.00	2.00	2.00	2.25	2.50
Philippines	3.50	3.25	3.25	3.25	3.25	3.25	3.25	3.25
Singapore**	0.85	0.40	0.40	0.40	0.40	0.40	0.40	0.40
South Korea	1.25	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Taiwan	1.38	1.38	1.38	1.38	1.38	1.38	1.38	1.38
Thailand	0.75	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Vietnam***	6.00	5.50	5.00	5.00	5.00	5.00	5.50	6.00
Eurozone	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Japan	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20
United States	0.75	0.25	0.25	0.25	0.25	0.25	0.25	0.25

* 1-yr Loan Prime Rate; ** 3M SOR ; *** prime rate

Interest rate forecasts

		2020				2021			
		Q1	Q2	Q3	**Q4**	Q1	Q2	Q3	**Q4**
US	3m Libor	0.75	0.35	0.35	**0.35**	0.35	0.35	0.35	**0.35**
	2Y	0.30	0.35	0.35	**0.40**	0.50	0.50	0.60	**0.70**
	10Y	0.40	0.50	0.50	**0.70**	0.90	1.00	1.10	**1.20**
	10Y-2Y	10	15	15	**30**	40	50	50	**50**
Japan	3m Tibor	0.05	0.05	0.05	**0.05**	0.05	0.05	0.05	**0.05**
	2Y	-0.30	-0.30	-0.25	**-0.20**	-0.15	-0.13	-0.13	**-0.10**
	10Y	-0.20	-0.20	-0.10	**-0.10**	-0.10	-0.10	-0.05	**-0.05**
	10Y-2Y	10	10	15	**10**	5	3	8	**5**
Eurozone	3m Euribor	-0.50	-0.60	-0.60	**-0.60**	-0.60	-0.60	-0.60	**-0.60**
	2Y	-0.90	-0.90	-0.85	**-0.80**	-0.75	-0.65	-0.60	**-0.50**
	10Y	-0.80	-0.80	-0.70	**-0.60**	-0.50	-0.40	-0.30	**-0.20**
	10Y-2Y	10	10	15	**20**	25	25	30	**30**
Indonesia	3m Jibor	5.10	4.90	4.90	**4.90**	4.90	4.90	4.90	**4.90**
	2Y	5.20	5.20	5.20	**5.20**	5.30	5.40	5.50	**5.50**
	10Y	6.60	6.30	6.40	**6.50**	6.50	6.50	6.50	**6.50**
	10Y-2Y	140	110	120	**130**	120	110	100	**100**
Malaysia	3m Klibor	2.90	2.65	2.65	**2.65**	2.65	2.65	2.65	**2.65**
	3Y	2.50	2.40	2.40	**2.40**	2.40	2.40	2.40	**2.40**
	10Y	2.75	2.85	2.90	**2.95**	3.00	3.05	3.10	**3.10**
	10Y-3Y	25	45	50	**55**	60	65	70	**70**
Philippines	3m PHP ref rate	3.00	3.25	3.10	**3.05**	3.00	2.95	2.90	**2.90**
	2Y	3.60	3.85	3.85	**3.85**	3.80	3.80	3.80	**3.85**
	10Y	4.00	4.00	4.10	**4.20**	4.25	4.35	4.40	**4.50**
	10Y-2Y	40	15	25	**35**	45	55	60	**65**
Singapore	3m Sibor	0.85	0.40	0.40	**0.40**	0.40	0.40	0.40	**0.40**
	2Y	0.70	0.55	0.50	**0.50**	0.55	0.55	0.55	**0.60**
	10Y	0.90	0.80	0.70	**0.70**	0.85	0.95	1.00	**1.10**
	10Y-2Y	20	25	20	**20**	30	40	45	**50**
Thailand	3m Bibor	1.12	1.12	1.12	**1.12**	1.12	1.12	1.12	**1.12**
	2Y	0.65	0.75	0.75	**0.80**	0.85	0.85	0.90	**0.95**
	10Y	0.90	0.95	0.95	**1.00**	1.00	1.00	1.10	**1.20**
	10Y-2Y	25	20	20	**20**	15	15	20	**25**
China	1 yr LPR	4.00	3.85	3.70	**3.55**	3.55	3.55	3.55	**3.55**
	2Y	2.10	2.20	2.25	**2.30**	2.35	2.40	2.40	**2.40**
	10Y	2.30	2.40	2.50	**2.50**	2.60	2.70	2.80	**2.80**
	10Y-2Y	20	20	25	**20**	25	30	40	**40**
Hong Kong	3m Hibor	0.95	0.55	0.55	**0.55**	0.55	0.55	0.55	**0.55**
	2Y	0.60	0.55	0.55	**0.60**	0.70	0.70	0.80	**0.90**
	10Y	0.70	0.70	0.70	**0.90**	1.10	1.20	1.30	**1.40**
	10Y-2Y	10	15	15	**30**	40	50	50	**50**
Korea	3m CD	1.40	1.15	1.15	**1.15**	1.15	1.15	1.15	**1.15**
	3Y	1.00	1.00	1.05	**1.05**	1.05	1.05	1.10	**1.10**
	10Y	1.25	1.25	1.35	**1.35**	1.45	1.45	1.55	**1.55**
	10Y-3Y	25	25	30	**30**	40	40	45	**45**
India	3m Mibor	5.80	5.55	5.30	**5.30**	5.30	5.30	5.30	**5.30**
	2Y	5.20	5.20	5.30	**5.40**	5.40	5.40	5.40	**5.40**
	10Y	6.00	6.00	6.15	**6.30**	6.40	6.40	6.40	**6.40**
	10Y-2Y	80	80	85	**90**	100	100	100	**100**

%, eop, govt bond yield for 2Y and 10Y, spread bps

Group Research

Economics & Macro Strategy

Taimur Baig, Ph.D.
Chief Economist - G3 & Asia
+65 6878-9548 taimurbaig@dbs.com

Chang Wei Liang
Strategist
+65 6878-2072 weiliangchang@dbs.com

Nathan Chow
Strategist - China & Hong Kong
+852 3668-5693 nathanchow@dbs.com

Eugene Leow
Rates Strategist - G3 & Asia
+65 6878-2842 eugeneleow@dbs.com

Chris Leung
Economist - China & Hong Kong
+852 3668-5694 chrisleung@dbs.com

Ma Tieying, CFA
Economist - Japan, South Korea, & Taiwan
+65 6878-2408 matieying@dbs.com

Radhika Rao
Economist – Eurozone, India, & Thailand
+65 6878-5282 radhikarao@dbs.com

Irvin Seah
Economist - Singapore, Malaysia, & Vietna
+65 6878-6727 irvinseah@dbs.com

Samuel Tse
Economist - China & Hong Kong
+852 3668-5694 samueltse@dbs.com

Duncan Tan
FX and Rates Strategist - Asean
+65 6878-2140 duncantan@dbs.com

Philip Wee
FX Strategist - G3 & Asia
+65 6878-4033 philipwee@dbs.com

Sources: Data for all charts and tables are from CEIC, Bloomberg and DBS Group Research (forecasts and transformations)