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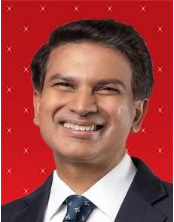
Macro Insights Weekly

A year without rate cuts?

Group Research | **May 6, 2024**



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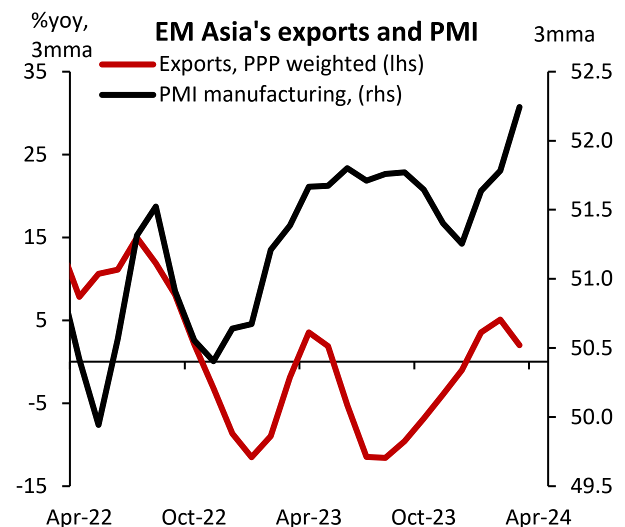
- *Over three trading days last week, global fixed income markets swung from despair to hope. This type of volatility is a marker of things to come as the 2024 rate cut scenario is priced in and out.*
- *We think there is room for rate cut as inflation and jobs momentum is on track to fade.*
- *Stickiness of inflation in recent months could fade on the back of easing energy and rental costs.*
- *Parts of the jobs market are showing early signs of cooling, but overall trend is still positive.*
- *There is a 25% chance, in our view, that inflation and jobs momentum doesn't ease.*
- *Then expect considerable bond and currency volatility as pricing would shift toward no rate cuts.*

Key data release and events this week:

- *Indonesia's 1Q24 growth to print at a steady 5.1% YoY, vs 5.05% average rise in 2023.*
- *We expect BNM to maintain its overnight policy rate (OPR) at 3.00%.*
- *CPI inflation is set to pick up in China and the Philippines, and remain steady in Taiwan.*

Chart of the Week: Asia's trade bifurcation

At first glance, it appears that Asia's nascent exports recovery is in danger of fizzling out. From commodity exporters like Indonesia and Malaysia to tech powerhouses like China and Singapore, March was a disappointing month. But April data releases are off to an encouraging start, with Korea and Vietnam reporting sizeable jumps in exports. Also, PMI readings have perked up across the region. Trade will follow, we're sure.



Source: CEIC, DBS.

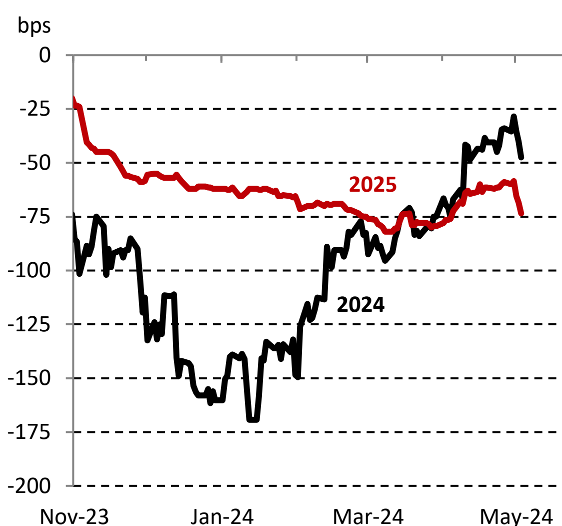
Refer to important disclosures at the end of this report.

Commentary: A year without rate cuts?

Global fixed income markets swung from despair to hope in the span of three days last week. At the middle of the week, following the April 30-May 1 meetings of the Federal Open Market Committee, the markets were chastened. Comments from Chair Powell that there has lately been "a lack of further progress" towards the 2% inflation target, pushed fixed income markets to pricing in no more than one rate cut this year. By the end of the week though, a weaker than expected nonfarm payrolls release for April and an uptick in the unemployment rate brought back two rate cuts to the price.

Like the US Federal Reserve, markets are set for several months of wait and see. The key issue is the noise associated with inflation. Goods inflation has eased substantially, but some aspects of core inflation have become a source of concern. If energy and food prices remain steady, as we expect they would, a path toward additional, sustainable disinflation is there for 2Q24, but to paraphrase Chair Powell, confidence in that path has waned somewhat.

Pricing for Fed Hikes(+)/Cuts(-)



Source: Bloomberg, DBS

The other issue is the labour market, but we don't see a great deal of noise there. The red-hot jobs market of 2022/23 may be behind, and some weakness has crept up in some segments (construction and retail), but overall market dynamics are still positive. The April payrolls figures that pleased the markets on Friday largely reflect a slowdown in government hiring, which in our view does not reflect a dawning of a new trend. With no fiscal tightening measure in the pipeline and outlays from recent years' large infrastructure bills still percolating through the economy, public sector hiring is not about the fade.

How do the inflation and labour market developments align with two rate cuts in 2H24? So far, quite well, in our view. A little bit of disinflation in oil (already underway) and rentals (downtrend has emerged) will help restore the Fed's confidence about inflation heading toward 2%, which could be further supported by marginal softening of jobs demand in the coming months.

But there is an emerging scenario under which energy and rental costs don't ease much, and neither does the labour market. Between Middle-East tensions and Washington's sustained fiscal support for the US economy, the idea of very little disinflation and no further weakening of the jobs market is hardly outlandish. We will assign this scenario a probability of 25%. Under this scenario, the Fed will remain on wait-and-watch for the rest of the year, eager but incapable of implementing rate cuts. We see considerable bond and currency market volatility in this scenario, a preview of which was amply visible in the last week of April. Could be a bumpy ride.

Taimur Baig

Key forecasts for the week

Event	DBS	Previous
May 6 (Mon)		
Indonesia: GDP (1Q)	5.1% y/y	5.0% y/y
May 7 (Tue)		
Philippines: CPI (Apr)	4.1% y/y	3.7% y/y
Taiwan: CPI (Apr)	2.2% y/y	2.1% y/y
May 8 (Wed)		
Philippines: exports (Mar)	-2.4% y/y	15.7% y/y
- imports	-9.7% y/y	6.3% y/y
- trade balance	-USD4.1bn	-USD3.6bn
Taiwan: exports (Apr)	6.5% y/y	18.9% y/y
- imports	3.8% y/y	7.1% y/y
- trade balance	USD8.0bn	USD8.7bn
May 9 (Thu)		
China: exports (Apr)	0.8% y/y	-7.5% y/y
- imports	4.3% y/y	-1.9% y/y
- trade balance	USD81.7bn	USD58.6bn
China: M2 (Apr)	8.3% y/y	8.3% y/y
Malaysia: BNM overnight policy rate	3.00%	3.00%
Philippines: GDP (1Q)	6.0% y/y	5.5% y/y
May 10 (Fri)		
India: Industrial production (Mar)	5.4% y/y	5.7% y/y
Malaysia: Industrial production (Mar)	2.8% y/y	3.1% y/y
May 11 (Sat)		
China: CPI (Apr)	0.7% y/y	0.1% y/y
China: PPI (Apr)	-2.6% y/y	-2.8% y/y

Central bank meetings

Reserve Bank of Australia (RBA) (May 7): This week's monetary policy meeting matters. CPI inflation increased to 3.5% YoY in March after three months of steady 3.4% prints. While this latest rise will unlikely lead to a surprise hike at this meeting, the market did price in an 81% chance of a 25bps rate hike at the September 24 meeting. Conversely, economists polled by Bloomberg still see the RBA lowering rates by the end of 2024. However, they could change their minds if the RBA asserts that rates must stay restrictive for longer to bring inflation back to the 2-3% target. More so if the accompanying Statement of Monetary Policy delivers new forecasts depicting price pressures from a tight labour market, keeping wage growth high and above that of headline inflation. Since the last RBA meeting on March 19, the 10Y bond yield has risen from 4.08% to 4.42%, above the 4.35% policy rate for the first time since early December.

Bank of England (BOE) (May 9): We expect the BOE to keep the bank rate unchanged at 5.25%. Although CPI inflation fell to 3.2% YoY in March from 3.4% in February, monthly inflation was high and unchanged at 0.6% MoM for a second month. At the last monetary policy meeting on March 21, the BOE's two hawks – Jonathan Haskel and Catherine Mann – stopped voting for a hike. Swati Dhingra will likely remain the lone dove calling for a cut. After the meeting, BOE Governor Andrew Bailey and Deputy Governor Dave Ramsden became more confident about falling inflation. Bailey has opened the door for a rate cut this year, but Chief Economist Huw Pill cautioned that the first cut might be months away. The market has priced in two rate cuts for this year starting as early as September.

Bank Negara Malaysia (BNM) (May 9): We expect BNM to maintain its overnight policy rate (OPR) at 3.00% during its May meeting. Like the previous decision in March, we reckon that BNM is likely to assess its policy stance as remaining supportive of the economy, with exports recovering, domestic spending resilient, and inflation contained. The Malaysian ringgit's volatility will continue to garner BNM's attention during its May decision. We note the MYR's outperformance vs regional currencies over the past month, which reflects some effectiveness of ongoing initiatives to encourage inflows, and therefore reduces the impetus of an OPR increase. Yet, there is also limited room for easier BNM monetary policy, given Malaysia's negative interest rate differentials with the US, and a still-firm US dollar due to the uncertainty regarding the timing and extent of potential US interest rate cuts over the coming months.

Forthcoming data releases

China: Consumer price growth is expected to accelerate from 0.1% YoY in March to 0.7% in April. This acceleration is primarily attributed to a softening drag from food prices, buoyed by stabilised average pork prices. Furthermore, an improvement in consumer sentiment is evident through robust domestic tourist traffic and revenue during the Qingming holiday.

The decline in producer prices is anticipated to ease from 2.8% YoY in March to 2.6% in April, aligning with the improvement in the sub-PMI Producer Price Index from 47.4 in March to 49.1 in April. Commodity prices, particularly metals and industrial products, witnessed an uptick during the month.

On trade, exports are projected to rebound from a decline of 7.5% year-on-year in March to a moderated growth of 0.8% in April. This rebound is largely attributed to the fading of high base effect from the previous month. However, the new export order in the PMI sub-index slightly declined from 51.3 in March to 50.6 in April, indicating a possible weakening in overall external demand, particularly from major trade partners such as the US, ASEAN, and the Eurozone, which recorded a slowdown in manufacturing PMI in April. Import is expected to improve from decline of 1.9% YoY in March to 4.3% growth in April, mainly driven by base effect.

Indonesia: The economy is likely to kickstart the year on a positive note, with growth to rise 5.1% YoY, largely steady from 5.05% average rise in 2023. Our GDP Nowcast model that captures high frequency indicators, points towards a stabilisation in the momentum on higher consumption (helped also by pre-festive demand) and campaign spending in early part of the quarter. Imports had also picked pace, suggesting investments and demand fared better in 1Q. Export growth on the other hand was subdued, as the trade surplus in 1Q narrowed by 40% compared to the same time year before. Firm growth allows for the BI to focus on price and FX stability.

Taiwan: April trade and inflation data will be released this week. Exports are expected to exhibit high single-digit growth, driven by increasing demand for electronic goods amidst the global tech sector upturn, and temporary supply-side disruptions caused by the Hualien earthquake. Further growth into double digits is forecasted from May onwards, as the impact of the earthquake dissipates. Meanwhile, CPI inflation is forecasted to remain steady at 2.2% YoY in April, with a notable MoM increase of 0.4%, primarily attributed to the government's recent electricity price hike. A further uptick to 2.5% is expected in May, driven by the pass-through effects of the electricity price adjustment, alongside rising global oil prices.

Economics Team

Taiwan: Accelerating to 4% Growth

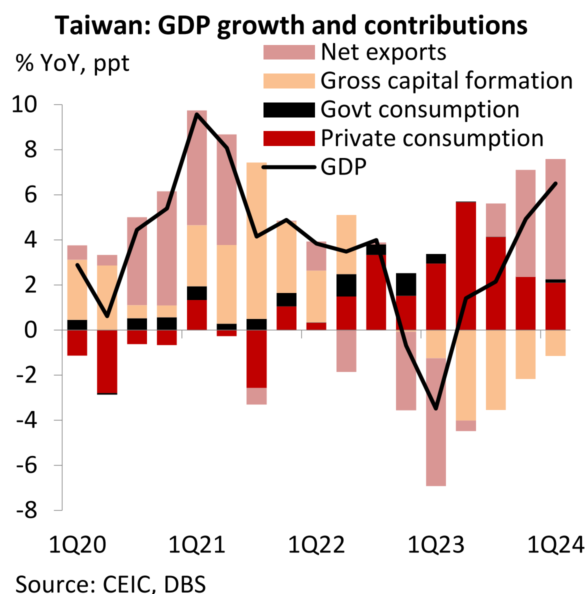
We are revising our full-year 2024 GDP growth forecast upward to 4.2% from 3.5%, buoyed by the robust growth performance observed in 1Q.

Preliminary estimates indicate that real GDP expanded by 6.5% YoY in 1Q, surpassing both consensus expectations of 6.0% and our forecast of 5.7%. Net exports emerged as the primary driver of this positive surprise, contributing a substantial 5.5 ppt to headline growth. This surge was fuelled by a 10.2% YoY increase in exports of goods and services, significantly outpacing a modest 2.2% growth in imports. Conversely, domestic demand made a modest contribution of 1.0 ppt to 1Q growth. Private consumption expenditures sustained a robust expansion of 4.1% YoY, albeit slightly lower than the 5.1% growth recorded in 4Q23. The decline in gross capital formation moderated to -4.5% from -9.1%, owing to inventory restocking.

Looking ahead, we expect that the export-driven growth momentum will persist throughout the remainder of the year. Exports are poised to accelerate further, driven by increased global demand for high-performance chips and high-capacity servers/storage, as businesses scale up AI infrastructure to meet growing computational needs. Despite a projected temporary slowdown in April due to the Hualien earthquake disaster, the overall trajectory remains positive. The uptick in S&P manufacturing PMI to 50.2 in April, the first positive reading in two years, indicates that the earthquake's impact on the manufacturing sector is minimum.

Conversely, while consumption is expected to remain robust, it is likely to experience a deceleration. Favourable labour market conditions and positive wealth effects will continue to support consumption. However, the escalation of energy price inflation, attributed to government electricity price hikes and rising global oil prices, is expected to restrain consumers' real incomes and purchasing power. The latest survey indicates a 10-point drop in the consumer confidence index for April, lowest level in over 12 months.

Note that the recovery in exports exhibits variance across different sectors. The electronics sector has witnessed a notable rebound, whereas demand for non-electronic goods such as chemicals, metals, plastics, and rubbers remains sluggish. Moreover, recovery is primarily driven by the G3 and ASEAN markets, with demand from China remaining tepid. This trend is expected to persist, given factors such as overcapacity and import substitution in China's manufacturing industry, alongside escalating trade tensions between China and Taiwan in the ECFA-covered sectors.



Source: CEIC, DBS

Ma Tieying

FX: USD has become less exceptional

The factors that kept the USD strong this year have weakened. The DXY Index retreated to 105 last week after failing to break above 106.50 in the past three weeks. Other signs of the USD's possible reversal included the quickened recoveries in the JPY and CNY, two of Asia's weakest currencies. For example, the offshore USD/CNH is now below and not above the onshore USD/CNY. After touching 160 on April 29 for the first time since 1990, USD/JPY plunged to 153 on alleged interventions by Japan's policymakers and the Fed maintaining its dovish stance last week.

The US economy has become less exceptional. Advanced GDP growth slowed to 1.6% QoQ saar in 1Q24, its worst performance since the technical recession in 1H22. The ISM PMIs for services and manufacturing were below the breakeven 50 levels in April, heralding a slower start to the economy in 2Q24. The Conference Board's consumer confidence index faltered a third month to 97 in April, its lowest since July 2022. Only 11.7% of the respondents expected more jobs in the next six months, the fewest since late 2011.

The US labour market has become less tight. Nonfarm payrolls slowed to 175k in April from 315k in March, its first sub-200k print in five months. Average hourly earnings growth slowed a third month to 3.9% YoY in April, below 4% for the first time since June 2021. The ISM services employment index fell to 45.9 in April, below 50 for a third month. Last Friday's monthly jobs data finally brought the US Treasury 10Y yield below 4.60% to 4.51%, its lowest since April 9, with interest rate futures contemplating a September rate cut again.

The stall in US disinflation was insufficient for the Fed to abandon its dovish pivot. At the post-FOMC press conference on May 1, Chair Jerome Powell said the Fed's next policy rate move was unlikely a hike. The PCE core deflator was 2.8% YoY in March, down significantly from its 5.6% peak in February 2022, near the Fed's 2.6% projection for 4Q24, a major assumption underlining the three rate cuts in March's dot plot. Hence, **two inflation data could send the DXY below its 50-day moving average (104.56) next week**. On May 13, the New York Fed's 1-year inflation expectations could drop in April to below 3% for the first month since November 2022. On May 15, the Bloomberg consensus sees CPI inflation slowing again to 3.7% YoY in April, a three-year low.

The DXY's downside will need its largest component, the EUR, to recover. The EU Commission will likely upgrade its forecasts this week. Real GDP expanded by 0.3% QoQ sa expansion in 1Q24 vs. the 0% consensus, exiting the technical recession seen in 2H23. The European Central Bank has been unwilling to pre-commit to more rate cuts beyond the one in June. GBP might also take its cue from the UK GDP on May 10, confirming the UK economy's exit from technical recession. At its meeting on May 9, the Bank of England will likely be more confident about falling inflation but remain too divided on a rate cut anytime soon. AUD can appreciate above 0.6650, or the past two months' resistance, if the Reserve Bank of Australia keeps the door open for another hike, supported by more optimistic forecasts in its Statement of Monetary Policy on May 7.

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