Global Market Wrap-up

Don’t get greedy

KEY MESSAGE

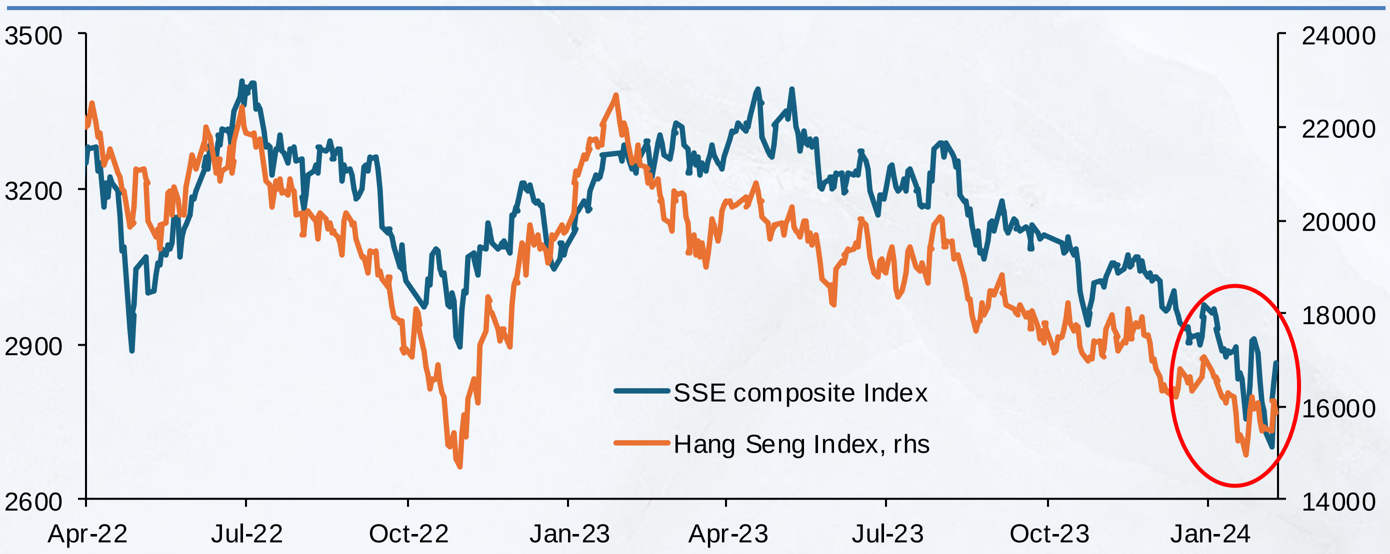
The resilient US economy again re-adjusts market expectations. Strong Non-Farm payroll & ISM service PMI prove Powell’s stance that the last mile of disinflation will be more difficult, while the SLOOS suggests that US economy is now heading to soft landing smoothly. However, the US equities market become more volatile as the elevated price makes investors anxious about the outlook. There could be a significant correction if any result undershoots the expectation.

Soft Eurozone economy makes the hawk retreat. Both BoE and ECB turn more cautious in their statement about the easing cycle. We acknowledged the stickiness for pressuring inflation from 3% to 2%, but weak economy should allow the ECB to throw the first stone, while the BoE followed by conducting the first cut in summer.

China needs more consistent stimulus to regain confidence. Although the PBoC introduced 50bps RRR cuts along with the “national team” to boost the market sentiment, tragic performance suggests that old methods are already not enough to satisfy investors these days. The continuous contraction in CPI & PPI should persist till H2.

YCC & NIRP exit are around the corner. BoJ Governor Ueda present a hawkish stance in the Jan MPM press conference by introducing the thought of continuous rates hike, albeit at a very gradual pace. However, monetary policy should remain accommodative even after the NIRP exit. Moreover, there’s room for USDJPY to go lower as monetary divergence between Fed and BoJ appears, we argued.

Chart of the week: A/H shares finally get rid of the gloomy sentiment?



Source: CEIC, CUIRS Investment Research

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Market Overview

Foreign Exchange	Spot	1w Change	1m change	3m change	6m change	YTD change
G10						
DXY	104.08	-0.01%	1.51%	-1.68%	1.52%	1.84%
EURUSD	1.079	0.05%	-1.34%	0.72%	-1.74%	-2.43%
GBPUSD	1.263	0.06%	-0.67%	2.78%	-0.73%	-0.81%
AUDUSD	0.653	0.32%	-2.42%	1.88%	-0.17%	-4.31%
NZDUSD	0.615	1.45%	-1.39%	4.03%	1.45%	-2.69%
USDJPY	149.26	0.54%	3.27%	-1.07%	3.85%	5.89%
USDCAD	1.346	-0.09%	0.53%	-2.43%	0.29%	1.65%
USDCHF	0.874	0.83%	2.59%	-2.74%	-0.25%	4.01%
USDNOK	10.54	-0.74%	1.77%	-5.70%	3.35%	3.68%
USDSEK	10.45	-0.60%	1.90%	-4.05%	-2.08%	3.73%
EM Asia						
USDCNH	7.22	0.16%	0.49%	-1.08%	-0.07%	1.03%
USDHKD	7.82	-0.03%	0.05%	0.06%	0.07%	0.15%
USDTWD	31.40	0.10%	1.12%	-2.52%	-1.23%	2.36%
USDKRW	1332.91	-0.33%	1.09%	1.92%	1.25%	3.07%
USDTHB	35.93	0.96%	2.86%	1.10%	2.66%	4.39%
USDPHP	55.89	-0.20%	-0.25%	0.25%	-0.70%	1.16%
USDMYR	4.76	0.95%	2.54%	1.68%	3.93%	3.65%
USDSGD	1.347	0.20%	1.21%	-0.70%	-0.10%	2.08%
USDIDR	15629	-0.45%	0.74%	0.08%	2.77%	1.60%
USDINR	82.98	-0.01%	-0.12%	-0.29%	0.16%	-0.33%
USDVND	24398	0.27%	0.16%	0.11%	2.82%	0.57%

Equities	Current Level	1w Change	1m change	3m change	6m change	YTD change
Americas						
Dow Jones	38671.69	0.41%	2.82%	11.35%	9.04%	2.47%
S&P 500	5026.61	1.51%	5.22%	12.16%	11.10%	5.65%
SOX	4567.30	4.00%	11.62%	21.36%	21.24%	11.92%
S&P/TSX Comp	3856.96	0.04%	-2.96%	8.24%	0.54%	-3.59%
IBOVESPA	128580	0.66%	-2.19%	0.77%	7.53%	-3.63%
EMEA						
Euro Stoxx 50	4715.87	1.34%	5.20%	10.32%	8.45%	5.68%
FTSE 100	7572.58	-0.71%	-1.30%	1.54%	-0.19%	-1.97%
CAC 40	7647.52	0.72%	2.79%	6.98%	4.26%	1.53%
DAX	16926.50	0.05%	1.36%	9.30%	6.35%	0.93%
Asia Pacific						
NIKKEI	36897.42	1.30%	7.40%	11.52%	12.72%	9.78%
SSE	2865.90	3.04%	-1.04%	-6.51%	-13.77%	-3.36%
HSI	15746.58	2.38%	-2.73%	-11.21%	-22.22%	-6.62%
HSCEI	5306.79	2.59%	-2.77%	-13.63%	-24.61%	-6.89%
ASX 200	7644.80	-0.24%	1.95%	8.24%	4.01%	0.22%
KOSPI	2620.32	1.95%	1.17%	7.58%	1.77%	-1.89%
TAIEX	18096.07	0.01%	2.60%	8.00%	6.08%	1.34%
SPCNX NIFTY	21782.50	-0.27%	1.10%	10.96%	9.87%	0.54%
JAKARTA COMP	7235.15	0.49%	-1.82%	5.41%	4.82%	-1.22%
FTSE/ BM KLCI	1512.28	-0.18%	1.40%	3.97%	3.32%	3.91%
FTSE/ ST	3138.30	-0.21%	-1.08%	0.09%	-5.88%	-2.92%

Source: Refinitiv, CUIRS Investment Research. As of 10 Feb 2024

United States: Smooth process toward soft landing

In its first meeting of 2024, the Federal Open Market Committee (FOMC) again unanimously voted to keep the federal funds target range at 5.25-5.50%. We view Fed Chair Jerome Powell's press conference as suggesting that each monthly inflation reading going forward is likely to be important in terms of determining the outlook for policy rate cuts. Powell noted that any decision to "start the process of dialing" back on monetary restriction would be "highly consequential." The next release of core PCE inflation data is scheduled for 29 February; this will be preceded by CPI data on 13 February and PPI data on 16 February. (See more in our *Global Macro Commentary | US FOMC: Rising expectation, stay away from politics*, 1 February 2024).

January Non-Farm Payroll: The January jobs report was impressively strong: nonfarm payrolls handily topped expectations, revisions showed stronger hiring momentum into year-end and average hourly earnings far overshot the upper bound of consensus forecasts. Headline nonfarm payrolls increased by 353k on the back of an upwardly revised 333k gain prior. We noted the nascent broadening in job growth beyond just three sectors (state/local government, healthcare, leisure/hospitality) at the end of 2023. The beginning of a new year confirmed acceleration of this trend. For the first time since June 2022, the "big three" sectors accounted for less than half of job gains in January, as breadth improved sharply compared to the prior months (**Fig. 1**). Job gains outside of the "big three" accelerated to 217k in January from 34k in November. In line with that, the diffusion index increased in January to 65.6 after a significant increase in December to 64.0 (**Fig. 2**).

Average hourly earnings growth was exaggerated, but cannot be wholly discounted: The 0.6% m/m jump in average hourly earnings overstates underlying momentum, as hours worked fell across a range of industries in January. To illustrate that point, average weekly earnings were unchanged in the month. Though exaggerated on account of excess weather-related curtailments, in our view, the latest figure extends a string of accelerating monthly readings over the last six months, having averaged 0.3% in Q3 2023 and 0.4% in Q4.

Total average pay accelerated to 4.5% y/y, from 4.3% the prior month (upwardly revised from 4.1%), shown in green in the chart at left below. On a shorter horizon, the chart at right below shows 3m annualized run rates and y/y rates still running hotter than pre-pandemic norms across a wide range of industries. The Q4 ECI, released earlier this week, showed wage rates are running closer to levels that would be comfortable for the Fed on a shorter-term 6m-annualized basis. Yet amid signs of improved economic momentum and elevated job openings, officials may see the latest results as reason to slow-walk an initial rate cut.

Fig. 1: Payrolls trend

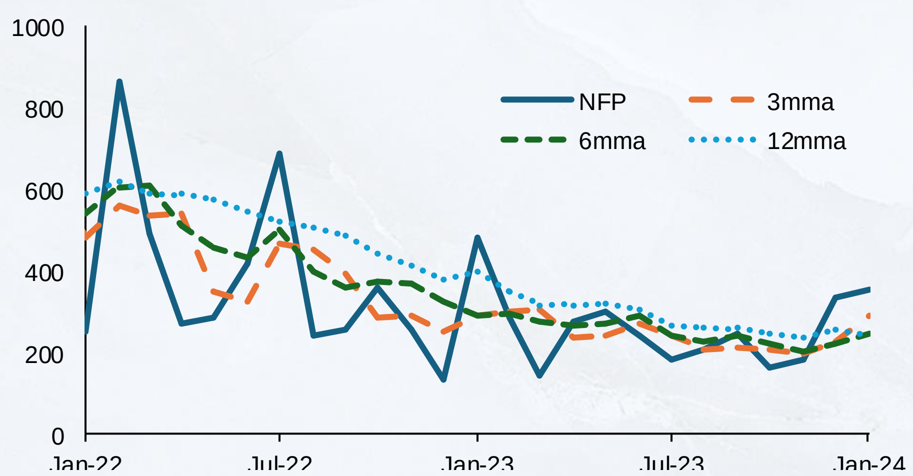
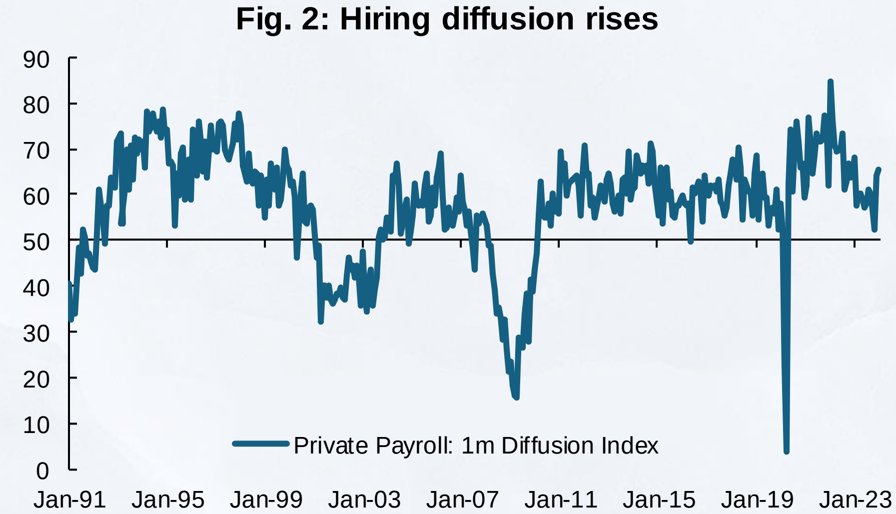


Fig. 2: Hiring diffusion rises



Jan SLOOS: January's Senior Loan Officer Opinion Survey on Bank Lending Practices (SLOOS) shows that most banks tightened lending standards, on net, for most business and household loans in the fourth quarter. However, the net share of banks tightening has fallen considerably after peaking in the aftermath of last spring's regional bank failures, suggesting that the current tightening episode will likely have a happier ending than prior ones.

Banks continue to report weakening demand for most types of loans, though the pace of contraction appears to be slowing across all borrower types. Overall, January's SLOOS report corroborates other indicators showing a significant easing of financial conditions relative to earlier in 2023, consistent with fading concerns about the solvency of regional banks since last spring.

Fig. 3: In Q4, smaller percentage of banks tightened lending standards for C&I loans...

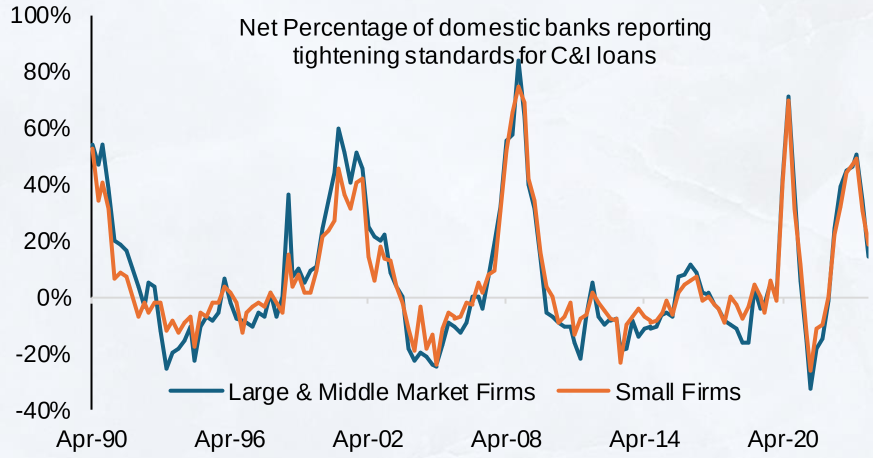
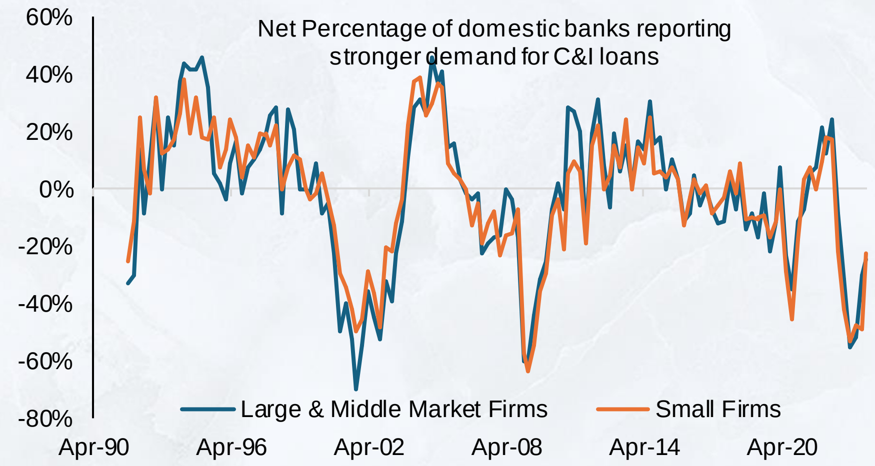


Fig. 4: ...amid loan demand that remained quite weak



January ISM Service PMI: The ISM services index returned to a range consistent with solid expansion after having slowed abruptly in December, led mainly by a rebound in employment. January's 2.9pt jump, to 53.4, was somewhat stronger than the rebound anticipated in forecasts. January's firmer reading mainly reflects a 6.7pt increase in the employment component, which returned to its prior range after having plunged in December, and by more modest rises in the new orders (+2.2pts) and supplier delivery times (+2.9pts) components.

We regard January's pickup in the composite as consistent with what we are seeing in hard data on activity and other indicators, suggesting another strong quarter of GDP growth in Q1 24. An increase in the prices paid component to its highest reading since February further intensifies risks that the Fed will deliver fewer rate cuts this year than markets expect.

Fig. 5: Service sector business activity measures have strengthened

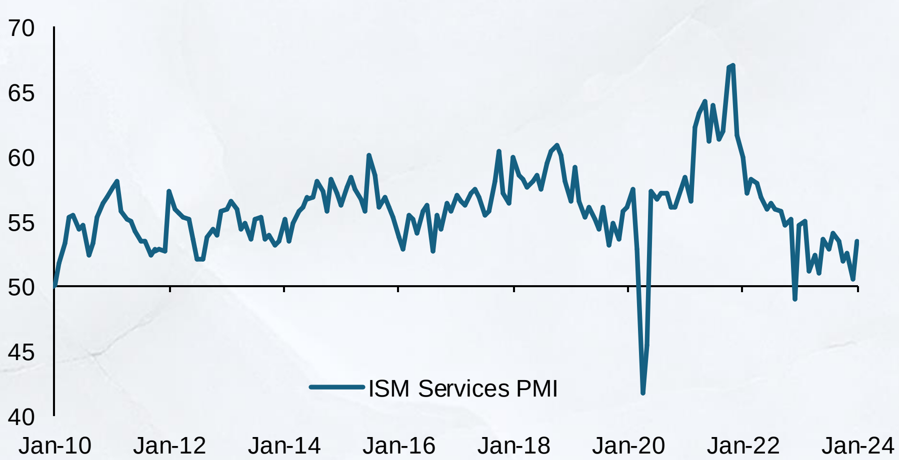
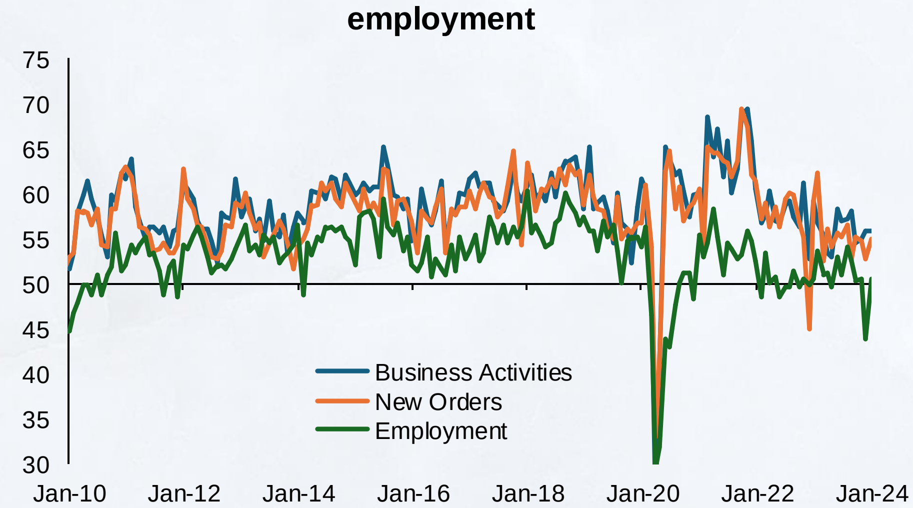


Fig. 6: Major components firmed in January, led by employment



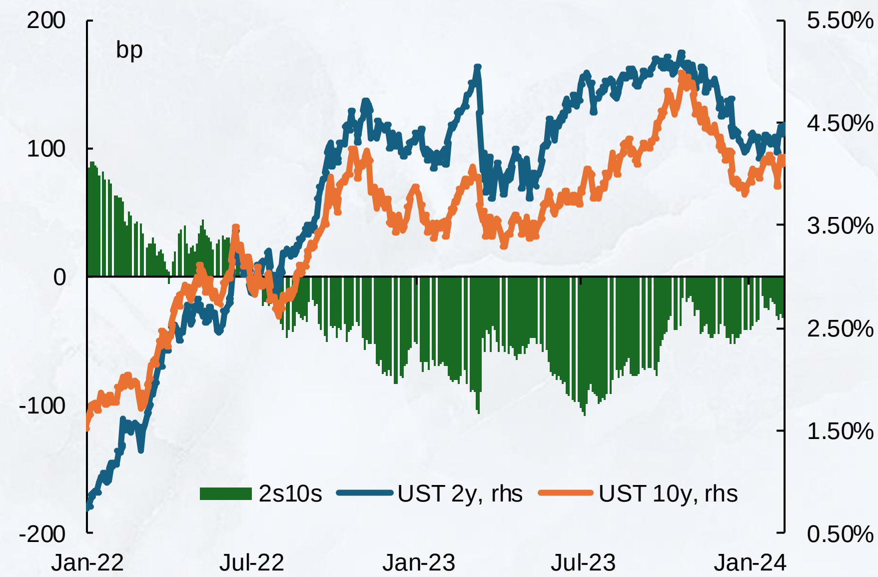
FX & Rates: The USD rallied after yet another set of strong data. After a much higher-than-expected non-farm payrolls print, ISM services survey overshooted expectations as well, with stronger data across almost all subcomponents. There was a particularly notable jump in the Prices component, which hit its highest level since February 2023. This chimes with the stronger-than-expected ISM manufacturing data released last week, which saw the highest Prices sub-index since April last year.

The ongoing strength of the US economy relative to most of its G10 peers continues to support a bullish view on the USD since September 2023. The strength of activity data will, in our view, make it harder for the Fed to have confidence that inflation is fully tamed. As such, we see rate pricing in the US being more prone to upside than downside for now. The USD has already broken free from its recent ranges and is at its highest since November last year using the DXY measure. If current economic momentum persists, there is little reason to think we will see a reversal to the weak side any time soon.

We also believe the remaining March cut risk should decay with time: some premium has to remain for the tail risk that "something breaks," but each day that passes uneventfully should see the remaining 4-5bp squeezed out. Risks around May and beyond should be a bit more dynamic. Re-emergence of inflation risk and any attending concerns that the Fed may have to re-engage with rate hikes would be a stronger driver of resumed flattening.

Fig. 7: It's hard to bearish USD with robust economy…

Fig. 8: …while rates market could face dynamic correction



Equities: US stock market showed strong momentum last week, with the S&P 500 index surging 1.4%, achieving a remarkable record by closing above 5,000 for the first time. Meanwhile, the Dow Jones was relatively stable throughout the week, while the Nasdaq Composite Index saw a significant 2.3% increase, and the Russell 2000 small-cap index jumped 2.4% (**See *Page.3* for detailed performance**).

While the overall market appears calm, individual stock volatility has exposed market anxiety. According to released financial reports of U.S. companies, overall earnings exceeded Wall Street expectations by 6.8%, and were 5.7% higher than the four-quarter average, indicating a potential 9% growth in fourth-quarter earnings.

However, the current calmness in the U.S. stock market seems superficial, evident from the unusually strong market reaction to fourth-quarter earnings. Dow Jones market data reveals that, as of last Thursday, the median price change of S&P 500 component stocks after earnings announcements was 3.6%, a more intense fluctuation compared to the 2.7% median over the past decade.

The significant price swings result from the uncertainty in corporate earnings outlook, which is more chaotic than the overall stock market prospects. It also reflects investors' concerns about the high valuation of the broader market. The current price-to-earnings ratio of the S&P 500 has risen to 20.4x, signaling an elevated valuation. Despite this, stock prices continue to rise seemingly indifferent to potential economic growth slowdown, disinflation, or the risk of persistently high interest rates. Tom Essaye, founder of Sevens Report, states, "Investors are uneasy, hence the more intense reaction to earnings."

The VIX, which is considered the "fear gauge" of the U.S. stock market, is currently around 12.8, significantly below the 20-year average of 17.7. However, considering the S&P 500 has risen 21% since October, the VIX below 13 indicates a market that is overly complacent and not fully considering potential risks. Reuters highlights four looming risks, including elevated valuations, persistent inflation, a cautious Fed outlook on interest rate cuts, and the possibility of a mild recession. It also suggested that the S&P 500 index may face a 10% downside risk, as increased volatility is seen as a more likely scenario than an extreme one.

Fig. 9: US equities continue to rally with bullish sentiment

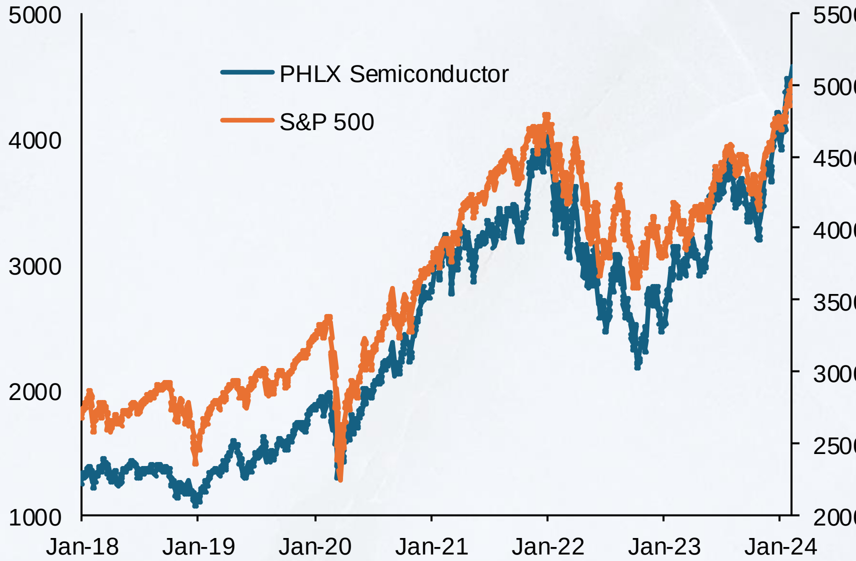


Fig. 10: but VIX is still at the depressed level

Eurozone: ECB chooses to be data-dependent

While Jan's rate cut discussion was seen as 'premature' by the Governing Council, overall, the communications strongly support the view that the April meeting is a 'live' one for rate cuts. If inflation materially undershoots the ECB's current projections over the coming months, this should lead to a significant re-assessment of the outlook in the March projections, paving the way for policy rate normalization to begin in April.

The meeting struck a more dovish tone than some of the communication from Governing Council members in recent weeks. The emphasis was firmly on the ECB's data dependence, which increases the importance of upcoming data releases such as inflation prints. Importantly, President Lagarde noted that the ECB does not need to wait until wage growth starts to slow in the data, as it believes it is already happening, consistent with the picture painted by more timely measures. The ECB also appears more confident that so-called 'greedflation' has ended and that above-trend wage increases are now being absorbed by unit profits.

Disinflation still on track: The fall in headline from 2.9% in December to 2.8% in January was a bit stronger than market consensus expectation but does not change the overall trend of disinflation, in our view. Headline inflation continued to be flattered by a benign picture for energy inflation, which remained in negative territory for the ninth month in a row. Core continues on a downward trend: Although falling by 0.1pp to 3.3%, the decline in the core was less than the 3.2% expected by market consensus, owing to unchanged services inflation of 4.0%.

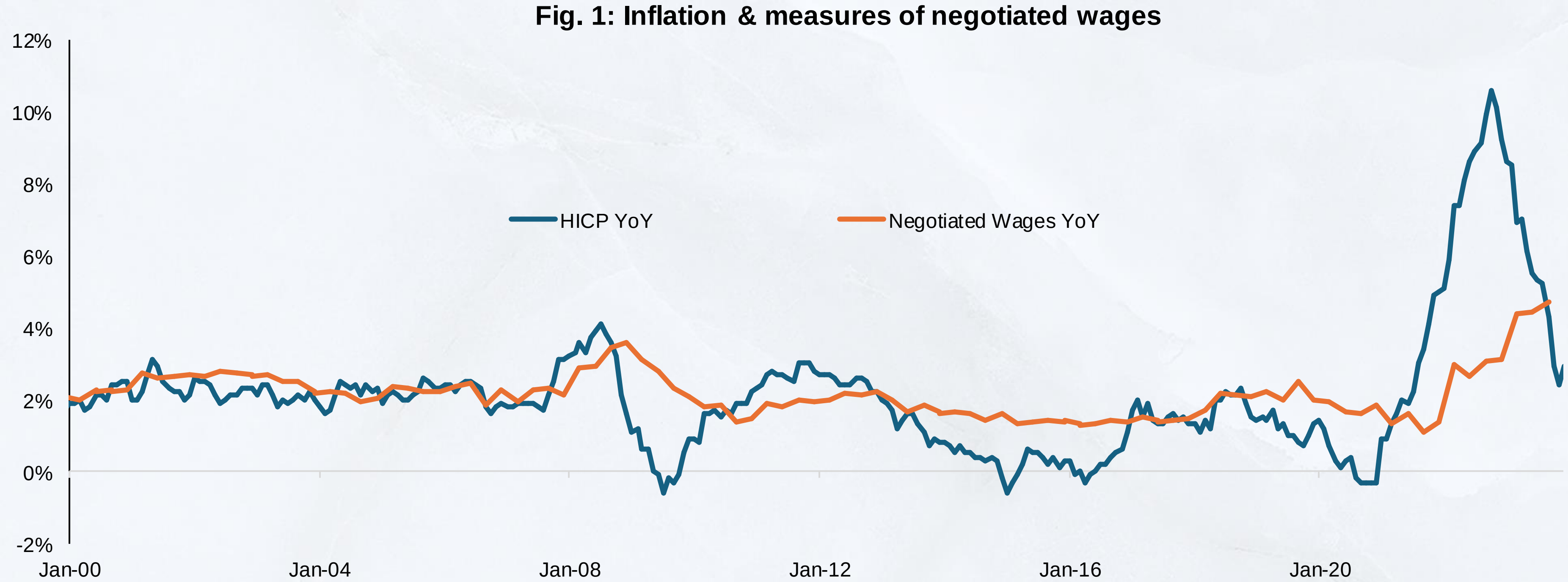
Given the annual re-weighting, the end of government support measures, and the typical January 'reset' of some prices, there is undoubtedly some 'noise' in the figures. But in broad-brush terms, energy inflation came in a bit weaker than we expected while core inflation was a touch stronger than we forecast.

Growth glass half full: Lagarde also struck a cautiously optimistic tone on the economic outlook too. For example, when asked about the January PMI data, she chose to focus on the positive elements, such as the directional increase, rather than the weak level in absolute terms. We share some of this optimism and think that the worst has likely now passed for the eurozone economy and continue to see a modest recovery over 2024.

While the ECB was able to kick the can a bit further down the road at Jan's meeting, we think the March meeting will be the moment of reckoning. As Lagarde noted: "We will have our projections in March and assess whether we are on track; we will have two more inflation prints by then, and then we will continue to get wage data."

The EUR has been on the back foot in the aftermath of the ECB's decision and press conference – deservedly so, in our opinion. A continuation of the soft recent sequential momentum – especially on core inflation – will likely see the market coalesce more firmly around a cut happening in March or April. We have argued EUR-USD will fall this year on policy divergence from the US.

Fig. 1: Inflation & measures of negotiated wages



United Kingdom: Market optimism retreats as hawkish bias remained

The Bank of England's Monetary Policy Committee (MPC) left Bank Rate unchanged at 5.25% at February meeting, with six members voting for a hold, two for a 25bps hike and one for a 25bps cut. While the new wording is technically a shift to a more neutral outlook, the current direction of travel is clear, so it feels as though the majority of the MPC is implying that the next move will be down. In fact, given that two members were still voting for a hike, it perhaps goes a little further in a dovish direction than it might have done.

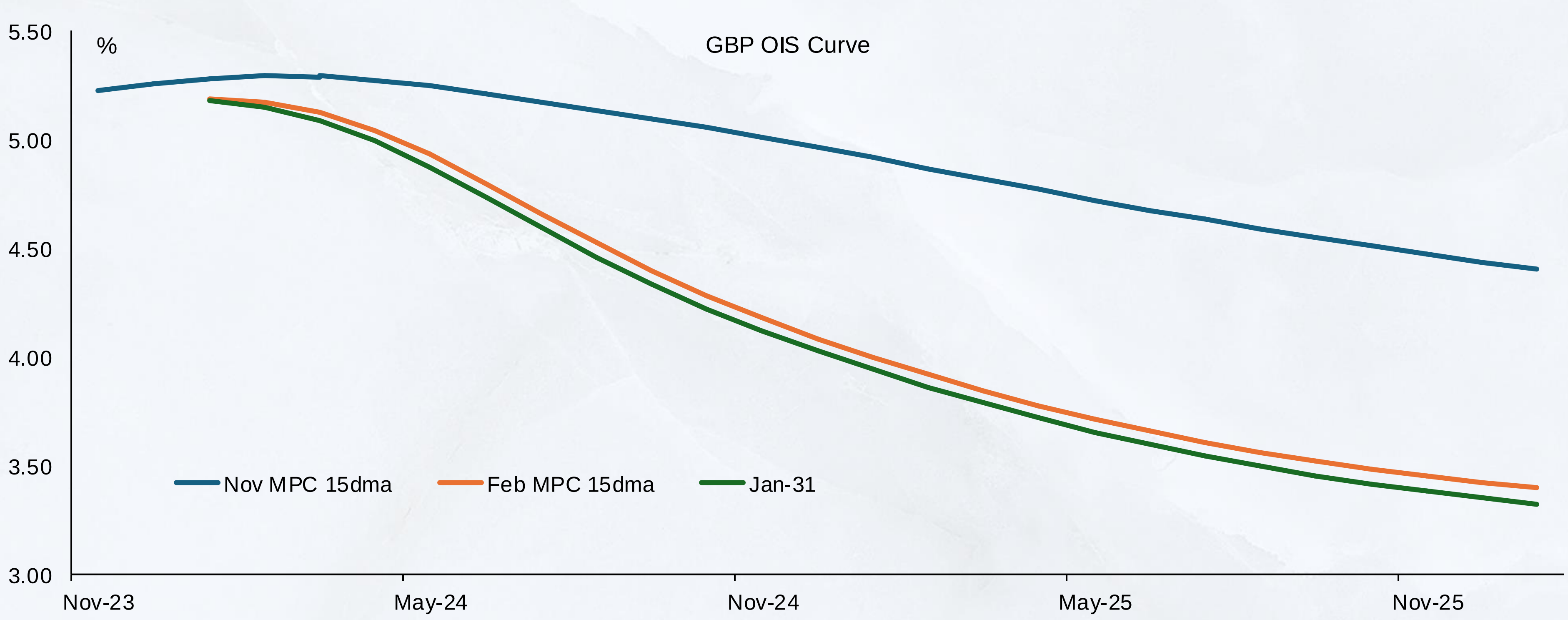
The statement also added that while external inflation risks emanating from Red Sea disruption had increased in the near term, "risks from domestic price and wage pressures were now more evenly balanced". Previously, the Committee had seen these domestic risks as skewed to the upside. Deputy Governor Ben Broadbent said in the press conference that the BoE did not need to see downside surprises to its inflation forecasts to allow cuts to happen (as illustrated by the fact that inflation on a constant market rate path would be too low), but that the Committee did need to be more confident about those forecasts.

On the other hand, the BoE has not turned dovish. The two votes for a hike alone tell the story with the statement that the fall in inflation thus far was "not necessarily informative about inflation persistence". But even leaving those two votes aside, the six members who wanted to keep Bank Rate unchanged still recognised that key indicators of inflation persistence remained elevated. Moreover, Governor Andrew was quoted by Bloomberg as saying that more evidence was needed before rates could be lowered. In our view, we see the BoE adopted similar language to both the Fed yesterday and the ECB last week.

The initial market reaction suggests that investors took the hint. Despite a mixed bag of news in terms of voting and messaging, the market takeaway is a little hawkish: going into the meeting, the market had priced about a 50% chance of a 25bps cut in May, which has now fallen to about 47%. For June, the market had 34bps, which has now dropped to about 31bps.

On the market front, The GBP is the best performing G10 FX in YTD. Sentiment with regards to UK fundamentals has improved but we would caution against getting carried away on the currency as we see little scope for a sustained rise in the GBP. MPC's dovish pivot has only just begun and there is scope for it to accelerate. Barclays stress-test a rapid repricing of Bank Rate expectations by c.75bp, as required to align it with their estimates of the UK's neutral rate. However, spill-overs to the pound should be limited to up to c.2% depreciation vs the EUR according to their estimation. Finally, UK's current account deficit and negative broad basic balance of payments leave the currency vulnerable to weakness.

Fig. 1: A lower market-implied path for policy rates help explain the upward revision to the growth outlook



Switzerland: SNB back to rebuild its FX reserve

The CHF's strong performance from Q4 2023 has started to reverse, raising the question whether a more meaningful move lower is due. Little has changed cyclically or structurally, but the FX policy preference for a stronger CHF is evolving, which could have a meaningful impact. Admittedly, there have been signs of a shift in FX policy. SNB language around the currency has become more balanced, and some data points might be signalling a return to FX reserves accumulation. But a shift away from a "strong franc" policy does not automatically mean a preference for a "weak franc". However, we are cautious of extrapolating modest signals.

Confirmation of Intervention. The SNB intervened in January as the CHF REER hit a new record high. The SNB has placed great store in the value of the REER as it becomes increasingly concerned by the impact on Swiss corporates. Whilst the SNB has so far stopped short in characterising the CHF as "significantly overvalued", further CHF strength may trigger such a response and we think the March meeting is "live" as the SNB has one eye on developments in ECB policy as well.

Looking at the numbers. January Swiss FX reserves rose CHF8bn from December. This is the largest %m/m increase in FX reserves since January 2022. On a y/y basis, FX reserves are still lower, but we suspect the pace of declines will slow dramatically against the backdrop of this enhanced FX policy. As ever, valuation adjustments are important with the SNB portfolio composed of both bond and equities. Whilst the MSCI rose 1%, bond returns fell by 1.3% and SNB reserves were approximately CHF660bn. This suggests some attrition on the headline number, but the message is clear. The SNB has been intervening and comparing this to the valuation adjusted December reading, we estimate, that January interventions could be as large as CHF20bn.

From an economic perspective, we do not think the recent data justify a shift towards a weak currency policy. Inflation has been relatively low through the recent cycle, but there has been a distinct lack of downward momentum in recent months. Real policy rates over a shorter-term window are much lower than in the Eurozone, suggesting less room for monetary and FX policy looseness in Switzerland. Meanwhile, export strength and soft import growth do not suggest an excessively overvalued CHF.

A further kicker for the CHF could come in the form of "hot money" inflows if the global, and particularly European, backdrop were to turn more averse. Foreign investors withdrew a significant number of deposits through 2023, so there is potential for this to reverse to inflows on any increase in negative sentiment, especially regarding European growth dynamics or peripheral debt concerns. **However, We are bearish on Swiss Franc as the huge rates differentials stay, while the shift of FX policy further strengthen our view.**

Fig. 1: SNB start building FX reserve since Jan 2022…

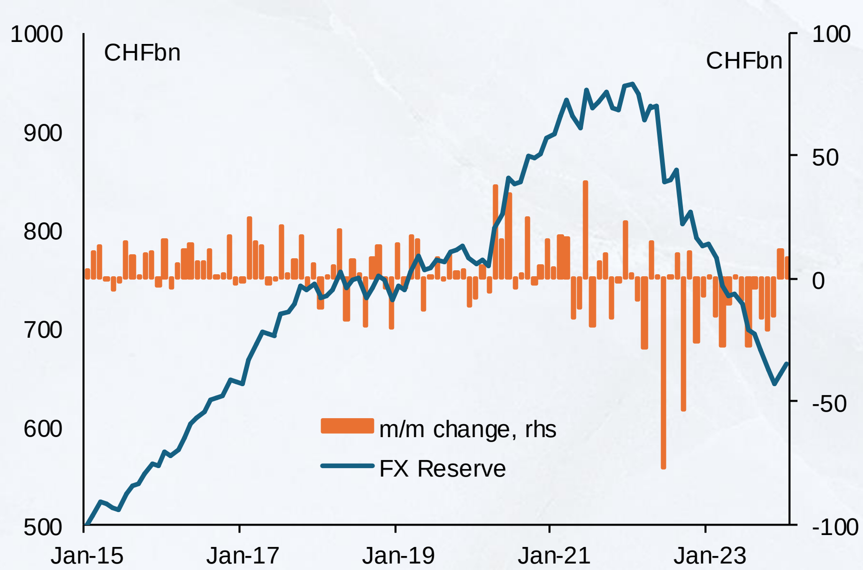


Fig. 2: …as the CHF over-strength continues

Australia: Stubbornly Hawkish

The RBA left its cash rate unchanged at 4.35% in line with market expectations and OIS market pricing had an 5% chance of a 25bp cut priced in just prior to the announcement.

High inflation remains the key challenge, and as the RBA noted, 'while recent data indicate that inflation is easing, it remains high'. The RBA specifically noted that although goods price inflation had declined, 'services inflation remains high, supported by continued excess demand ... and strong domestic cost pressures, both for labour and non-labour inputs.

The central bank's inflation forecasts were revised a little lower in the short-run, driven by the downside surprise they got on the Q4 2023 print. However, the longer-term forecasts still show that they expect inflation will be above the top end of the 2-3% target band until mid-2025. The forecasts were extended out to mid-2026, at which point they expect inflation to have fallen to 2.6% y-o-y. So, as the market had expected, over the entire forecast horizon the RBA expects that inflation is still above its 2.5% target midpoint.

The central bank also published its updated Statement of Monetary Policy (SoMP), including its latest set of forecasts (**Fig. 1**), and Governor Bullock gave a press conference. The latest business liaison also suggests wages growth ran around 4% y-o-y in 4Q23, and the businesses expect wages growth to slow to around 3.5% y-o-y over the next 12 months. Firms are also reportedly moderating employment intentions, which have now declined to around longer-term levels.

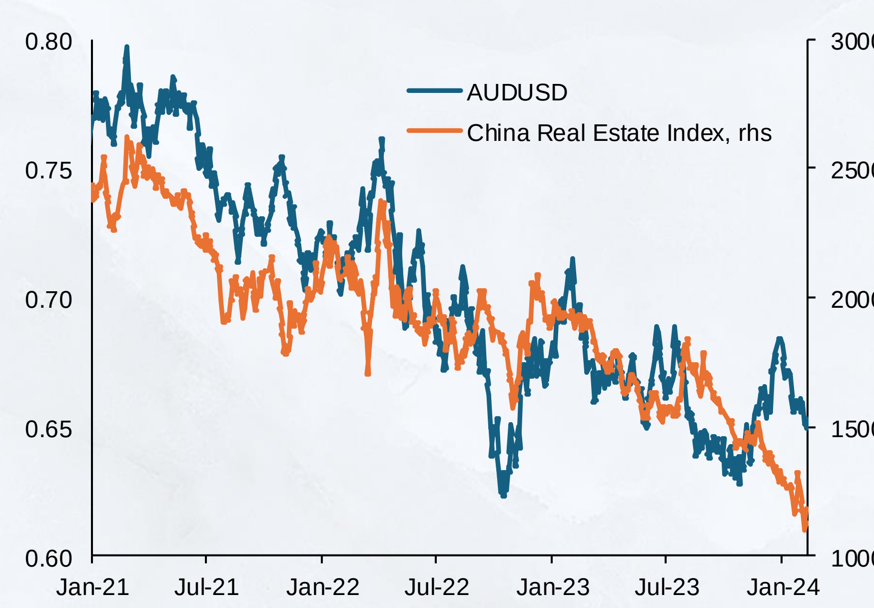
The new Statement also contained information on the RBA's assessment of the output gap and full employment. The Statement noted "a range of model-based estimates of potential output also suggest the level of economic demand is above its supply capacity" and that while the output gap has narrowed, it is "consistent with excess demand in the economy contributing to elevated domestic inflationary pressures". The Statement also noted that "model-based estimates suggest labour market conditions are still tighter than full employment, consistent with elevated domestic inflationary pressure and robust wages growth".

From FX perspective, the key determinant for AUDUSD remains global risk sentiment and financial conditions. Risks are skewed towards markets dialing back easing expectations for the Fed, which will weigh on AUDUSD via both risk sentiment and relative yield channels. Meanwhile, the RBA may lag G10 peers in cutting rates, those prospects may be overpriced versus the Fed, based on relative growth and inflation metrics. A higher household debt-to-disposable income ratio and a faster transmission of policy tightening have seen the household saving ratio in Australia remain on a declining trend, while it has stabilized in the US. Lastly, we doubt that the muted recovery in China and continued policy support for the property sector will become a bullish factor for AUDUSD anytime soon, let alone that the pair has already overshot its relationship with China equities and USDRMB (**Fig. 2**).

Fig. 1: RBA's latest set of forecast

		Dec-23	Jun-24	Dec-24	Jun-25	Dec-25	Jun-26
Real GDP Growth (y/y %)	Nov-23	1.60	1.80	2.00	2.20	2.40	
	Now	1.50	1.30	1.80	2.10	2.30	2.60
Headline CPI (y/y %)	Nov-23	4.50	3.90	3.50	3.30	2.90	
	Now	4.10	3.30	3.20	3.10	2.80	2.60
Trimmed mean inflation	Nov-23	4.50	3.90	3.30	3.00	2.90	
	Now	4.20	3.60	3.10	3.00	2.80	2.60
Unemployment Rates (%)	Nov-23	3.80	4.00	4.20	4.30	4.30	
	Now	3.80	4.20	4.30	4.40	4.40	4.40
Oil Price (USD/Barrel)	Nov-23	84.0	84.0	84.0	84.0	84.0	
	Now	83.2	80.4	80.4	80.4	80.4	80.4
Exchange rate (EOP TWI)	Nov-23	61.0	61.0	61.0	61.0	61.0	
	Now	60.9	61.6	61.6	61.6	61.6	61.6

Fig. 2: AUD has overshooted the relation with China



China: More needs to be done to save the market, consumptions and confidence

We have witnessed tragic performances of the A-share market in January. It seems like all the stimulating policies including increasing national debt, lowering reserve ratio and supplying PSL fail to add confidence to the economy and the investors. In the first month of 2024, despite the fact that the "national teams" have brought billions of capitals into the market, SSE Composite Index (000001.SH) still dropped for 6%, Shenzhen Index (399001.SZ) retreated for 13% and the Growth Enterprise Index (399006.SZ) took a nosedive for about 16%.

Regarding the economic data, China's consumer prices fell 0.8% y/y in January, which has been the largest decline since September 2009 and, the 4th consecutive months for China to be trapped in deflation. According to the National Bureau of Statistics of China, the unexpectedly weak data is mainly due to the base effects last year, when general consumptions soared after the official announcement of giving up the quarantine policies. However, the silver lining of this set of data is the precious reversal of price levels on a monthly basis as CPI finally comes back to 0.3% m/m. Economists are speculating that the Lunar New Year is the reason behind this tiny rebound as consumption profoundly recovers during this most important festival in Chinese community.

Combing through the whole year of 2023, China economy was deeply trapped in deflation. The price levels remained positive for the first three months (2.1% y/y in January, 1.0% y/y in February, 0.7% y/y in March) but quickly plummeted to the break-even point in April. The data turned negative in July (-0.3% y/y) and that was the first time for China to have deflation since February 2021. Throughout the whole year, it seems like Chinese people's sentiment have fluctuated with the price levels and eventually been illustrated by the performances in A-share market. To cope with these undesirable economic conditions, the central government has spent quite a lot of efforts to boost the economy and rebuild people's confidence in the economic growth. For instance, the PBC has lowered the reserve requirement for commercial banks twice in 2023 and once in 2024, to bring more capitals into the markets. Also, China has approved slightly more than 1 trillion yuan in additional sovereign debt issuance in October 2023, to support development projects and utility expenditures such as renovating urban villages. Since we have not yet seen strong positive responses from the capital markets, it is of utmost importance for the authority to re-consider the direction and the strengths of their policies.

Generally speaking, price level is usually considered the barometer of one country's consumption and confidence level. We estimate that the price data will still be fragile in the first half of 2024 and China economy definitely requires more support from the central government.

Fig. 3: Stock markets in China perform tragically since 2021

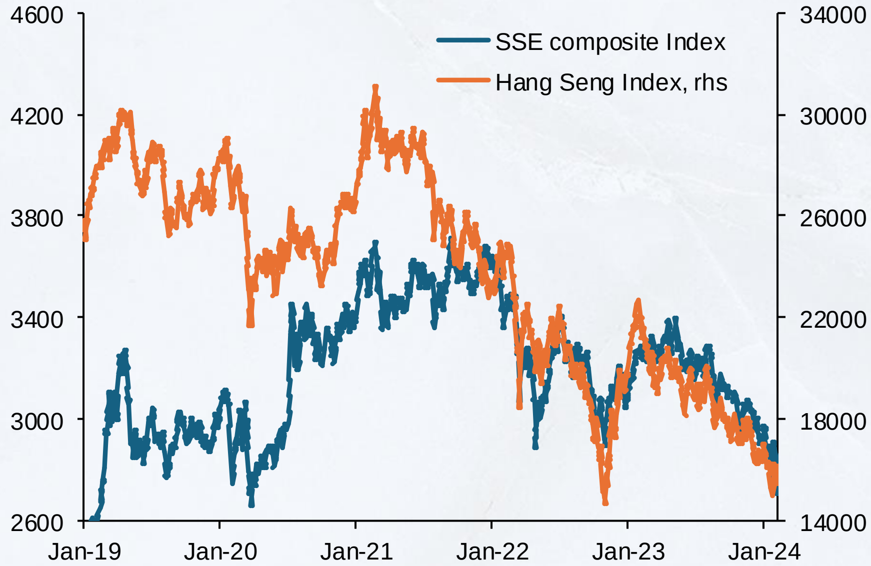
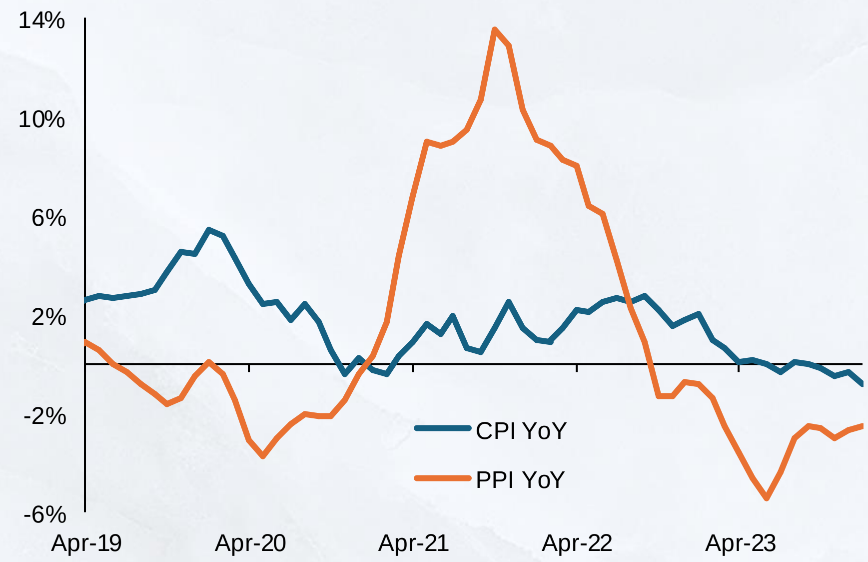


Fig. 4: January is the 4th straight month for deflation in China



Japan: BoJ's cautious tactics raise concern; Rates differentials cap JPY upside

By unanimous vote, the Bank of Japan (BoJ) maintained the rate on the Policy- Rate Balance at -0.1% and kept the existing YCC framework at its January meeting. Committed to further promoting both lending and demand, the board also unanimously voted to extend the deadlines for its Loan Support Program by a year.

No major changes in BoJ's forecasts. In the BoJ's first outlook report in 2024, officials tweaked their forecasts for inflation on the back of recent developments in oil prices. The median estimate for core (excluding fresh food) inflation in FY2024, which ends in March 2025, was revised down to 2.4% (2.8% previously). Meanwhile, median core inflation for FY2025 remained below 2%, with core now expected to come in at 1.8% (1.7% previously). Median forecasts for core-core (excluding fresh food and energy) were unchanged. On growth, the BoJ remained optimistic, with officials continuing to expect above potential growth through the forecast horizon.

Meanwhile, communication from the outlook report and from Governor Ueda in the accompanying press conference reiterated the message of patience, with the outlook report continuing to highlight "high uncertainties" in activity and price developments. Nonetheless, the BoJ continued to note that progress is being made towards bringing inflation towards target on a sustained basis. More and more firms were noted to have continued to announce constructive wage hikes ahead of Shunto, of which the first set of results are expected mid-March.

Consistent with the increased optimism in the Outlook Report, Governor Ueda confirmed that the data—including early signals from the spring wage negotiations—were moving in the right direction, and that the BoJ is getting closer to declaring its 2% price stability "in sight". He also stated clearly that when the BoJ reaches this point when it can project the achievement of underlying 2% inflation on a forward-looking basis, "it would need to consider whether to continue the various large-scale monetary easing measures that it currently has in place, including negative interest rate policy."

Most importantly, Governor Ueda stressed that, based on the BoJ's current assessment for the outlook for Japan's economy and prices, monetary policy will likely remain accommodative even after the BoJ declares 2% inflation "in sight" and exits NIRP. We think governor's remarks are consistent with view that NIRP exit will be followed by additional hikes, albeit at gradual pace and to levels well below estimates of Japan's nominal neutral rate.

Looking ahead, we expect the BoJ to declare its 2% price stability target "in sight" and exit NIRP+YCC in April-July '24. In our view, the more optimistic tone in the January Outlook Report and Governor Ueda's press conference remarks strengthen the probability that the BoJ will make the move at the 25-26 April MPM.

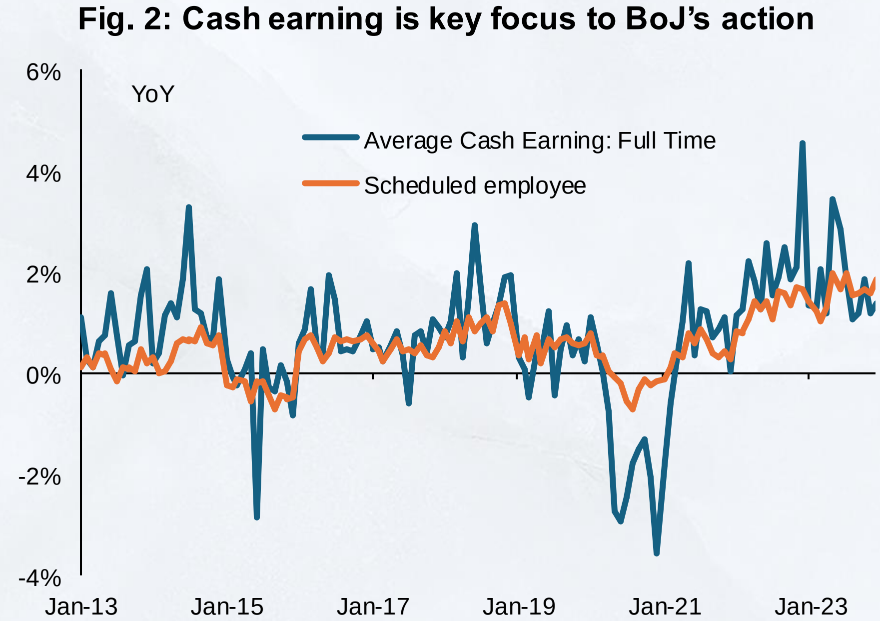
While the hike in March cannot be ruled out, we think probability that the BoJ actually delivers at the March MPM is relatively low. Though Japan's largest umbrella union (Rengo) is scheduled to publish the results of the first response round of the FY24 Shunto on 15 March, waiting until April will allow the BoJ to confirm the results of the 1Q BoJ Tankan (due 1 April), as well as reports from the April BoJ branch managers' meeting.

The BoJ's next Outlook Report, in April, will also see the policy board extending its growth and inflation forecasts to FY26. Having already penciled in 1.9% ex-energy core inflation in FY24 and FY25, FY 26 projection is likely to see inflation sustained at around 2%, supporting the case for a move off emergency policy settings.

Fig. 1: BoJ's latest set of economy projection

		FY2023	FY2024	FY2025
Real GDP	Oct-23	1.8 to 2.0 [2.0]	0.9 to 1.4 [1.0]	0.8 to 1.2 [1.0]
	Now	1.6 to 1.9 [1.8]	1.0 to 1.2 [1.2]	1.0 to 1.2 [1.0]
CPI Ex-Fresh Food (FF)	Oct-23	2.7 to 3.0 [2.8]	2.7 to 3.1 [2.8]	1.6 to 2.0 [1.7]
	Now	2.8 to 2.9 [2.8]	2.2 to 2.5 [2.4]	1.6 to 1.9 [1.8]
CPI Ex-FF & Energy	Oct-23	3.5 to 3.9 [3.8]	1.6 to 2.1 [1.9]	1.8 to 2.2 [1.9]
	Now	3.7 to 3.9 [3.8]	1.6 to 2.1 [1.9]	1.8 to 2.0 [1.9]

Fig. 2: Cash earning is key focus to BoJ's action



USD-JPY has rebounded strongly since the end of last year. The 5.9% rise YTD looks strong compared with the change in US-JP yield differentials over the same period. For example, 10y differential has re-widened by 20bp (35% retracement of the earlier fall in Nov-Dec) and 2y differential has re-widened by only 5bp (5% retracement).

There is probably some short covering happening in the FX market. CFTC data suggests that short JPY positions were cut by 60% from mid-November levels (Figure 4), when USD-JPY averaged 134. Apart from spot losses and negative carry, some positions are probably abandoned due to low conviction for January BoJ MPM.

The correlation of USD-JPY with the Nikkei index has strengthened recently. Due to a widening of tax exemption benefits in the NISA (Nippon Individual Savings Account) programme that came into effect on 1 January 2024. There could be common driver (retail flows) behind the recent rise in both the Nikkei index and USD-JPY (outflows to overseas markets).

Over the past 10 years, investment trusts (which capture a lot of the retail investors' flows) have bought USD30bn of foreign stocks per year on average. The risk is that this may increase sharply this year due to the higher NISA investment limits (2-3 times higher), and undermine the JPY. The weekly portfolio flow data for Japan suggests that this risk is worth following, but it not a game-changer at this juncture. In the first two week of 2024, there were USD6.7bn equity outflows by all residents, which is a turnaround after the USD11bn repatriation inflows in Nov-Dec 2023. However, as market become more volatile, the "hot money" actions turns more dynamic. There were foreign inflows to Japanese equities – USD17bn – in January too. Overall, the weekly portfolio flows actually become supportive to Yen (**Fig. 3)**.

Our base case is that the JPY will recover modestly this year, after depreciating by some 30% since the Fed started its rate hike cycle. The catalysts would be (i) the Fed cutting rates (**Fig. 5**); (ii) the BoJ removing YCC and exiting NIRP; and (iii) Japanese lifers rebuilding FX hedge ratios from extremely low levels. In our view, the rationale remains intact, but the timing is being debated now.

Overall, we believe the crux for the JPY's outlook still comes down to the Fed and the BoJ. The anticipated policy divergence to the JPY's advantage should trigger a change in positions by the speculative community and by Japanese lifers. But while the timing for pivoting by the respective central banks is being debated now, short-covering has caused this temporary squeeze higher in USD-JPY.

Fig. 3: Japanese weekly portfolio flows

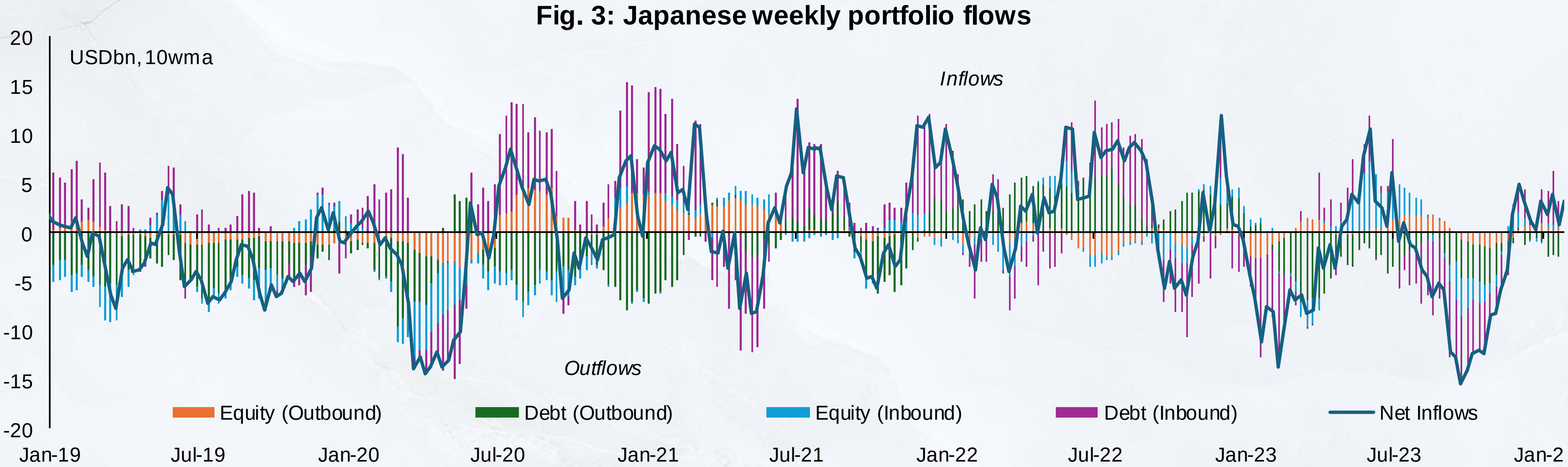


Fig. 4: Short JPY positions re-bulid after Jan MPM

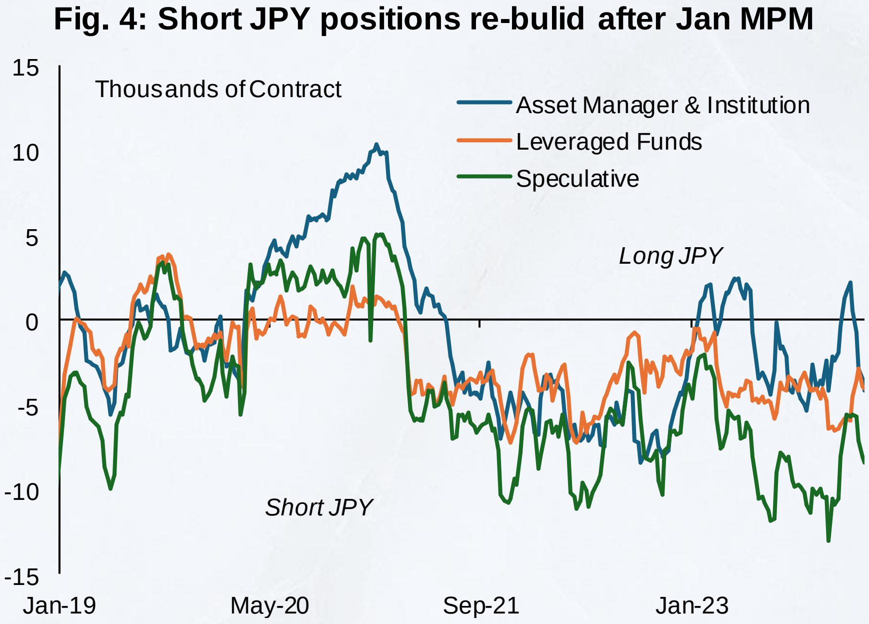
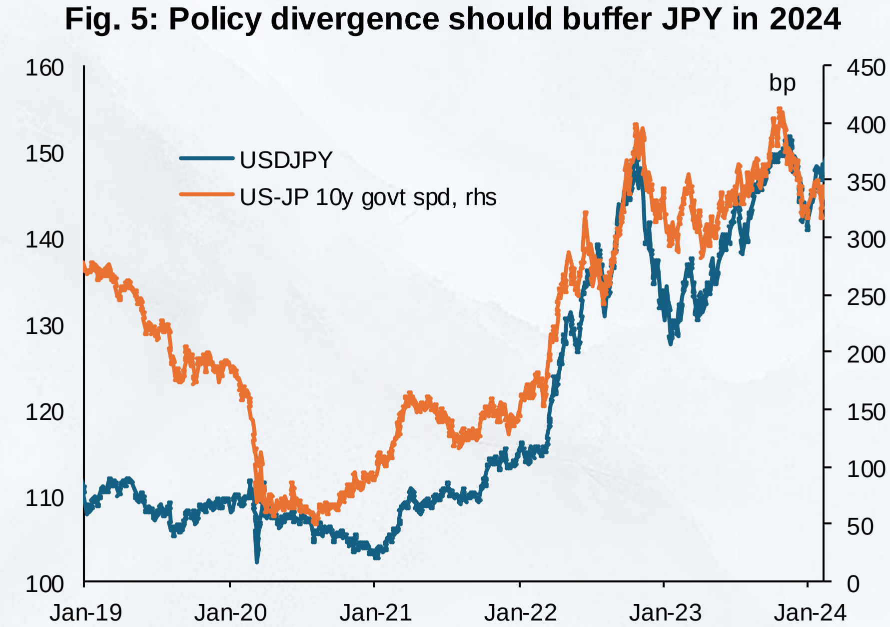


Fig. 5: Policy divergence should buffer JPY in 2024



Korea: Export momentum remains intact; C/A surplus stays steady

Exports continued to post a steady recovery despite the weakness seen mid-month. Exports increased by 18.0% y/y in January, accelerating from 5.1% in December, partly boosted by 2.5 more working days from different timing of the Lunar New Year in 2024. That said, the outcome was better than Bloomberg's consensus of a 17.6% increase. While the recovery momentum continued, we think it was dented in January due to: 1) logistics disruptions that deterred non-tech exports; and 2) softer seasonality of tech in H1.

Red Sea disruption likely weighed on non-tech exports. A Korea International Trade Association survey found 7.5 out of 10 companies experienced disruption due to prolonged Red Sea risk (Figure 2). Most member companies noted the increase in freight costs as the biggest factor, but some also noted delays in shipments, and difficulty in securing both freight space and containers. We believe the latter concerns are reflected in the data and disrupted some non-tech exports that are typically shipped by sea.

Despite the sharp increase in y/y growth, we believe the sequential momentum slowed modestly. However, We expect the semiconductor export recovery cycle to continue. Semiconductor exports rose 2.0% m/m sa, following a 6.0% increase in December, which translated into 56.2% y/y increase. That said, sequential momentum softened as exports growth eased to 15.6% from 17.8% in November on 3m/3m basis.

That said, we expect strong pricing momentum to continue to keep growth strong in y/y terms. Currently, spot DRAM prices trade at a 20% premium to contract prices. We believe this translates into a 15-20% pricing increase for DRAM contract prices for Q1. As producers are keen to keep the supplies tight, we think the pricing momentum is likely to last at least until late H1.

Given the improvement in the semiconductor exports cycle, we expect improvement in trade balance to continue along with improvements in the terms of trade. Imports rose 2.8% m/m sa in January, with increases in some energy imports, likely due to the heating demand. The trade surplus narrowed to USD0.3bn from USD4.5bn in December. Adjusting for the seasonality, however, we think it continued to improve.

Fig. 1: Export recovery momentum remain intact

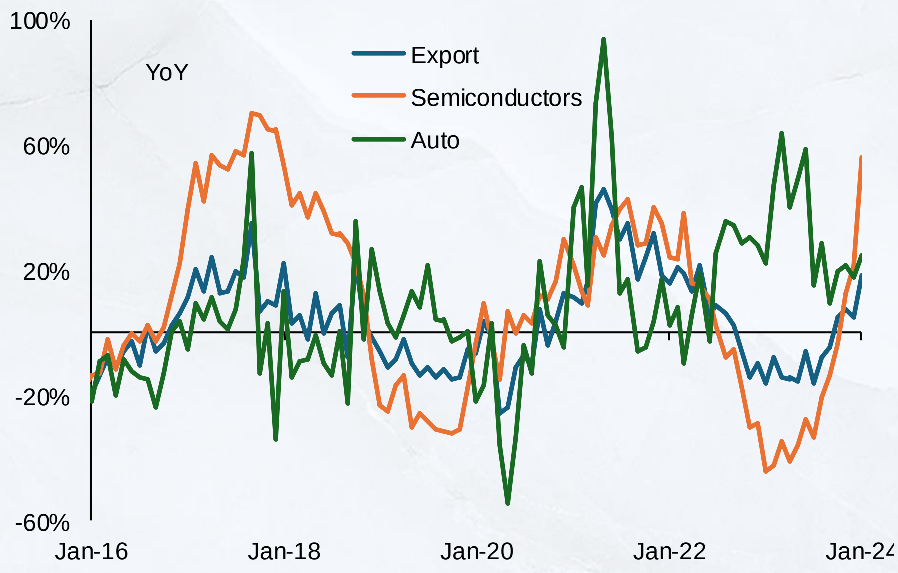
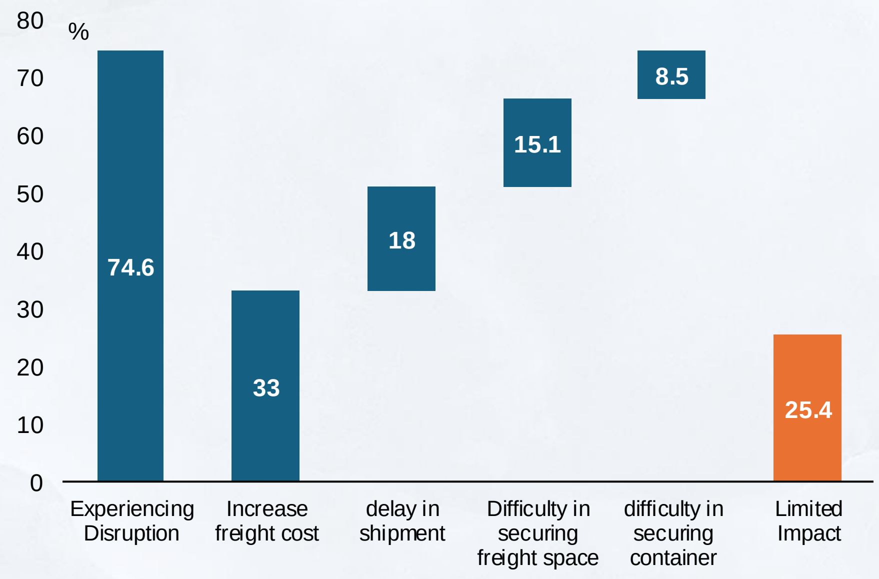


Fig. 2: while 7.5 out of 10 Korean company see impact from Red Sea



January headline CPI inflation eased to 2.8% y/y from 3.2% in December, softer than the Bloomberg consensus for 2.9%. While agricultural prices turned out to be higher than expected, declines in processed food and tourism-related services prices led to 2.8% inflation, in our view.

Meanwhile, core inflation fell slightly more than our forecast, declining to 2.5% y/y from 2.8% in December (excluding food and oil). As we note above, we believe softening in processed food and tourism-related services prices likely have been major part. Catering services prices started to rise sequentially, but the pace remained slower than last year's.

We continue to believe "sufficient signs of inflation converging to the target" is the key MPC discussion topic in 2024, as the BoK contemplates the timing of its first rate cut. Our baseline continues to assume the headline inflation will fall below target around September-October, but we believe the BoK will pay more attention to underlying measures of inflation in y/y terms (Figure 3) to gauge price pressures.

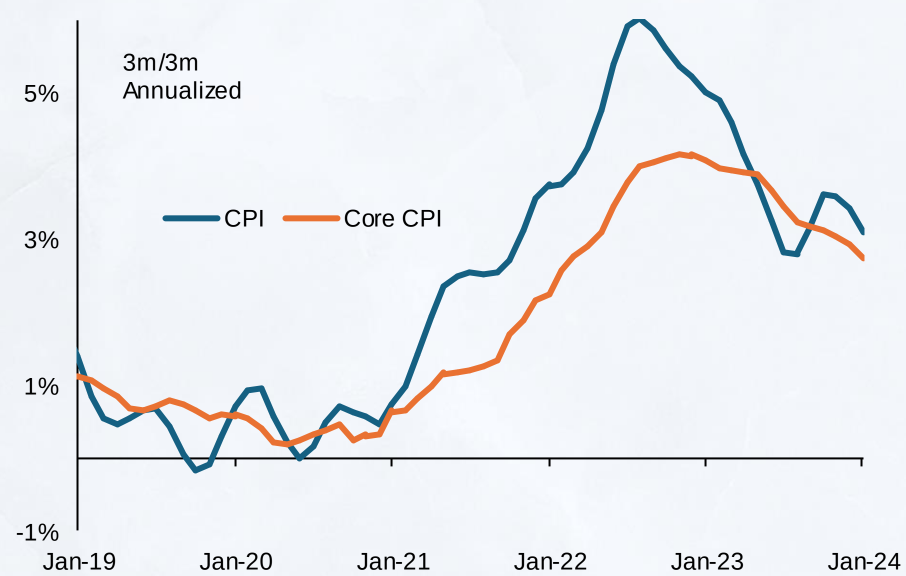
Even with relatively benign disinflation progress from January CPI print, we believe the BoK is likely to push back against expectations for an early pivot. Even as inflation broadly tracks the forecast trajectory, we believe the BoK to remain cautious and careful in declaring victory on price stability.

Recent official communication from the BoK continued to highlight: 1) the "last mile" challenges in bringing inflation down toward the target level; and 2) the importance of weighing the cost of premature easing against the cost of keeping policy too tight, even as underlying inflation is declining. Against this backdrop, e continue to expect the BoK's first cut from Q3 as this gives the BoK more room to focus on the underlying inflation trajectory as external pressures likely soften.

We believe sequential and instantaneous measures of inflation offer important value on price momentum in Q1 as the seasonal price-adjustment cycle kicks in (Figure 4). In our baseline view, underlying inflation gauges and inflation expectations will start falling to around pre-COVID averages by late Q3 to Q4.

Fig. 3: Disinflation process remain smooth..

Fig. 4: ..while momentum also remain moderating



The current account surplus widened in December, bouncing back from the one-off primary income deficit in November. The current account surplus increased to USD7.4bn, from USD3.9bn in November, better than our forecast for USD4.8bn. With today's print, we estimate the current account surplus in 2023 was 2.1% of GDP. Goods exports increased by 5.8% y/y, slightly softer than the 6.7% gain in November. Lower commodity prices and slower capital goods imports led to reduced imports, widening the goods balance.

We continue to expect a relatively large size current account surplus into 2024 and will support the KRW. In particular, the basic balance maintained a relatively large surplus of around USD3bn in the three months through December, while the balance of payments also increased in December. While we continue to expect dividend repatriation flows from overseas subsidiaries to slow in 2024, we think the current account surplus will be anchored by increased exports, driven by semiconductors.

Overall, we expect the turnaround in the current account position to contain volatility in the KRW and provide a buffer against risks of any sharp depreciation in the currency. We now see short USDKRW as an attractive trade in Asia, while we acknowledge the persistent USD strength poses a huge risk.

Fig. 5: CA surplus registered USD35.5bn in 2023

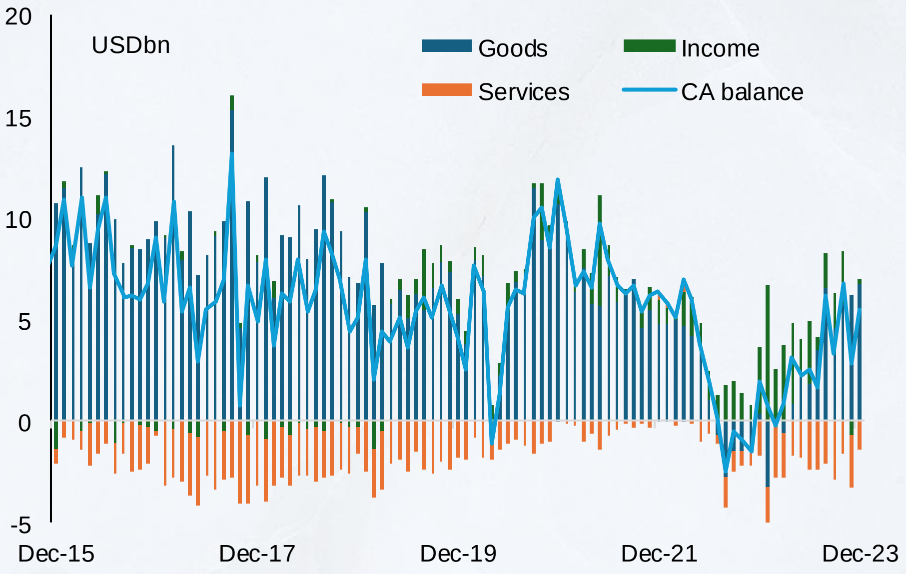
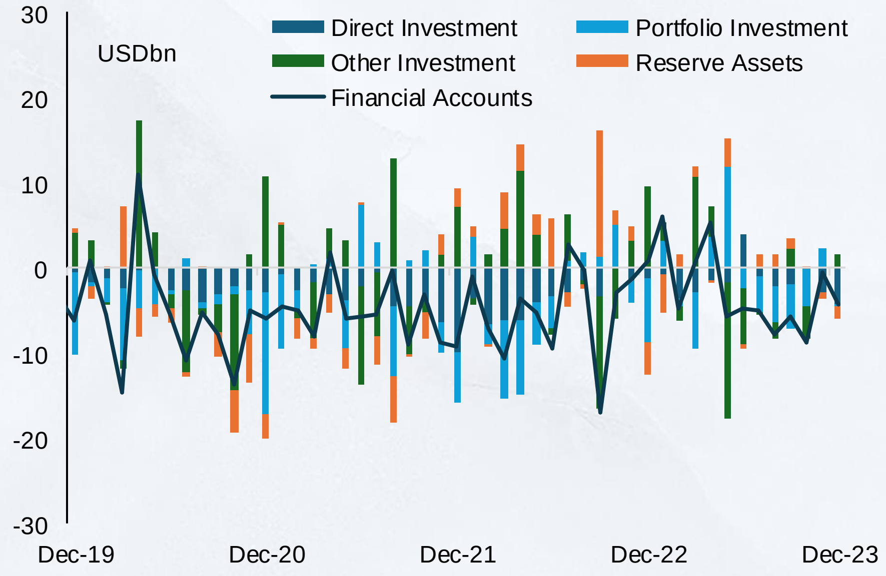


Fig. 6: Outflows pick up by direct investment



Taiwan: Surprises in imports imply for greater growth in 2024

Exports rose by 18.1% y/y in January (Dec: +11.8% y/y), slightly below the Bloomberg consensus estimate of 19.5% y/y. In sequential terms, we estimate January exports fell by 2.1% m/m sa, after gaining 5.9% in December. Tech exports declined 2.0% m/m sa in January, after increasing 5.5% m/m sa in December, while Non-tech exports fell 2.1% m/m sa in January (Dec: +6.6% m/m). Taiwan authorities expect February exports to fall by between -1% and -5% y/y, and Q1 exports to increase by mid to high single digits.

Imports surged by 19.0% y/y, from -6.5% in December, much higher than the Bloomberg consensus estimate of a -4.8% drop. This was due to 1) increased electronics imports from China and Korea; 2) potential arms imports from the US; and 3) increased commodity imports, both in price and volume terms. Despite these areas of strength, relatively muted capital goods imports still suggest domestic demand, especially around investment, is subdued. We think 1) increased electronics and equipment imports for inputs, 2) arms imports, and 3) higher commodity prices were behind the higher imports.

Meanwhile, January CPI inflation surprised on the downside as it eased notably to 1.79% y/y from 2.70% in December, lower than the Bloomberg consensus of 2.2% and our forecast of 2.3%. Along with the headline rate, core inflation – excluding fruit, vegetables, and energy – also eased to 1.64% y/y from 2.43% y/y in December. In sequential terms, we estimate the headline was flat in seasonally adjusted terms (Dec: +0.3% m/m sa), while core CPI rose by 0.25% m/m sa versus 0.20% in December. While CPI inflation eased notably in January, we believe this is likely to be due to base effects and subsidies around entertainment and nursing services. We believe the CBC will keep rates on hold in the near term and only look to pivot towards more neutral in H2 24.

According to the December meeting note, one of the CBC members mentioned an aggressive tightening action may be needed if inflation stays above 2% in 2024. Taiwan inflation is currently sticky with the core and headline both above the CBC inflation target of 2% at 2.43% and 2.71%. The scheduled minimum wage increases slated for 1 Jan pose upside risks to the inflation outlook. Therefore, a near-term policy rate cut looks unlikely and we expect CBC to remain on an extended pause at 1.875% through 2024.

Meanwhile, the TWD is currently at the regime of carry disadvantage dominant. The US-TW rate differential floors USDTWD from the downside. The currency may still underperform the basket due to the carry disadvantage and China concerns even though the electronic cycle has seemingly bottomed out. Since FX plays an important role in the overall monetary condition, the not-to-strong currency and the robust fundamentals indicate little room for rates to go down further.

Taiwan rates went up due to the market paying interest following CBC members' hawkish statement in the December meeting note published on 25 January. This is generally in line with our view that near near-term rate cut is unlikely given the still sticky inflation and the carry-constraint currency. Given the reasons above, we think there is room for a bear steepen front-end curve as 1s5s NDIRS is trading below par.

Fig. 1: Big jump on Import should further boost the recovery

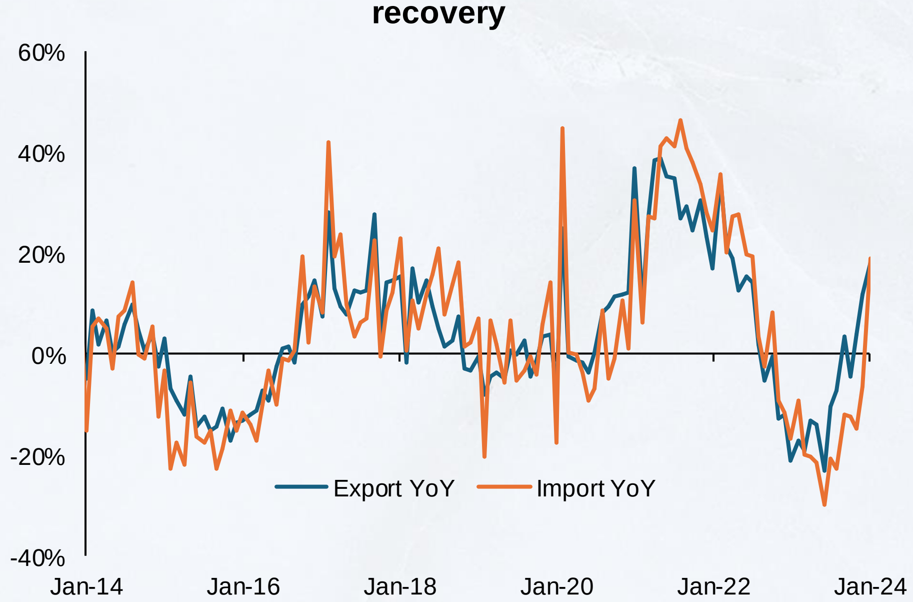


Fig. 2: Inflation should keep CBC away from easing

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