This Time, is Different(iated)?

Why Asia FX may be Compromised

"In a dark place we find ourselves, and a little more knowledge lights our way disturbing"

- Master Yoda, Star Wars

"I find your lack of faith disturbing"

- Darth Vader,

Star Wars (Ep IV): The Empire Strikes Back

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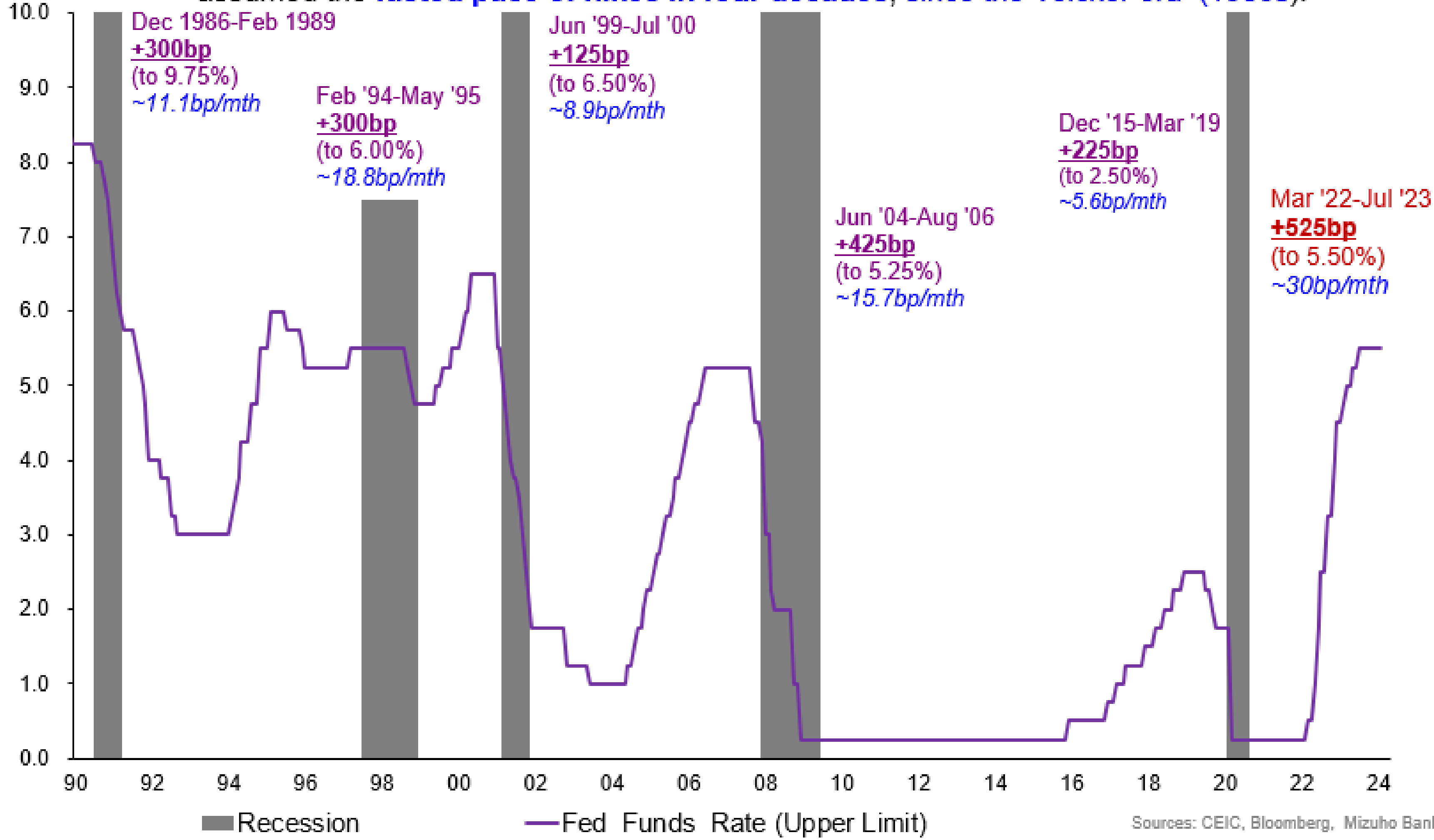
June 2024

This Time It is Different? Euphoria

1. **Will the Fed Manage a Soft Landing or Muddle through Miscalculations?**
    a. Historical Precedents are not Encouraging
    b. The Plot Has Thickened: More Hawkish 'Dot Plot'!
    c. Policy is Exceptionally Tight vis-à-vis Economic Conditions
    d. Consumer Exceptionalism May be Overstated
    e. Cash-flow Constriction a Risk to Consumer Demand
    f. Jobs Not as Hot & Wage-Price Risks are Overstated
    g. Risk View to Stoic Fed: Deeper Cuts in 2025!
2. **Challenging Received Wisdom on Bearish Pivot USD**
    a. Bearish USD on Peak Fed is Common, But Not Without Exception
    b. Prolonged Peak Introduces "Fear" & "Fed" Boost for USD
    c. USD Retains Policy Advantage … at least in terms of Direction Bias
    d. Not to Confuse Peak USD for Bearish USD
3. **The (Geo-)Politics of USD Trump**
4. **Why AXJ Reversion is Not Guaranteed?**
    a. Relative Under-performance Reveal Eroding Advantages
    b. Adverse Policy-FX Loop May Amplify Downside4 Volatility
    c. Carry Unwind Risks on JPY Upside Volatility Flare
5. **Especially in the Context of CNH Risks**
    a. China & Attendant CNH Risks Loom Large
    b. Exceptional CNY Pressures Amplifies Policy Conundrum ...
    c. … Including Devaluation Risks

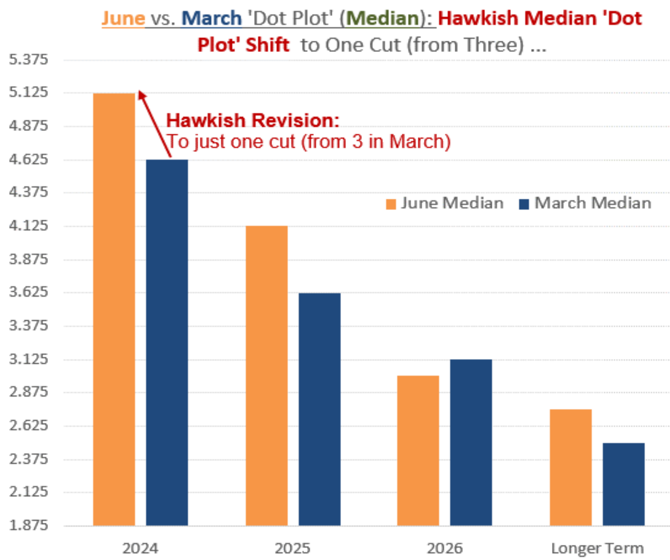
1a. Historically, Aggressive Rate Hikes Have Seldom Been Without Economic Pain

Fed Tightening Cycles & Global Recessions: **Few Tightening Cycles** by the Fed Have Resulted in "Goldilocks" Outcomes that **Avert a Recession**. And this time, the Fed has assumed the **fasted pace of hikes in four decades**; since the Volcker era (1980s).



Sources: CEIC, Bloomberg, Mizuho Bank

1b. Fed Has Gotten More Hawkish at the Margin



Sources: Bloomberg, Mizuho Bank

Summary of Economic Projections (SEP)

Percent

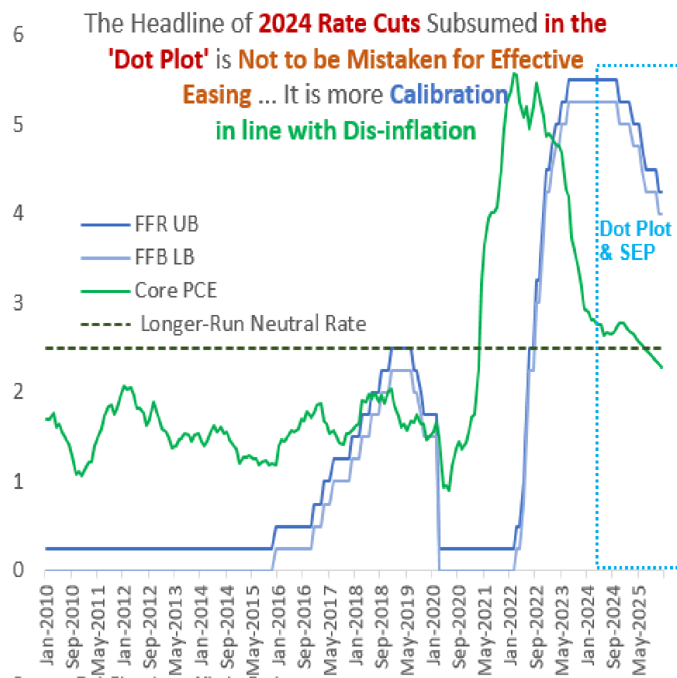
Variable	Median[1] 2024	2025	2026	Longer run
Change in real GDP	2.1	2.0	2.0	1.8
March projection	2.1	2.0	2.0	1.8
Unemployment rate	4.0	4.2	4.1	4.2
March projection	4.0	4.1	4.0	4.1
PCE inflation	2.6	2.3	2.0	2.0
March projection	2.4	2.2	2.0	2.0
Core PCE inflation[4]	2.8	2.3	2.0	
March projection	2.6	2.2	2.0	
Memo: Projected appropriate policy path				
Federal funds rate	5.1	4.1	3.1	2.8
March projection	4.6	3.9	3.1	2.6

PCE +0.2%-pt

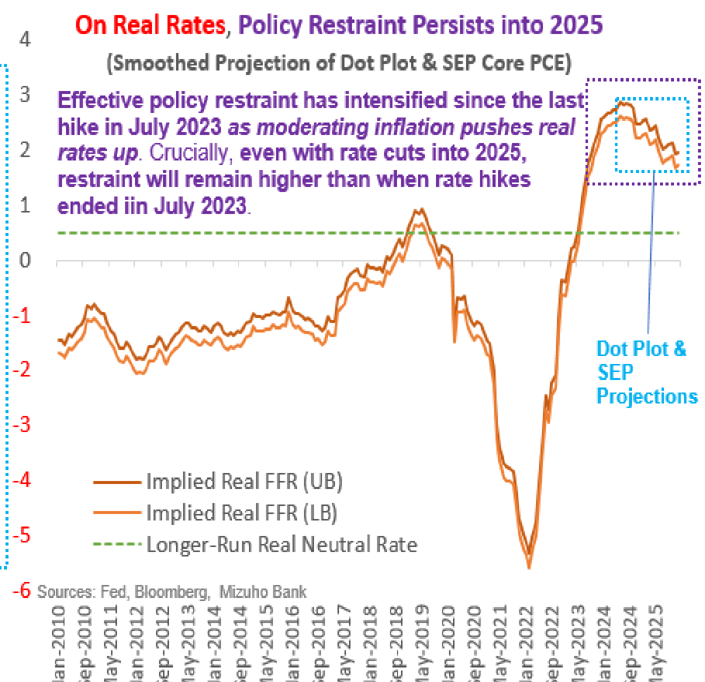
Core PCE +0.2%-pt

FFR +50bp

Real Rates +30bp



Sources: Fed, Bloomberg, Mizuho Bank



Sources: Fed, Bloomberg, Mizuho Bank

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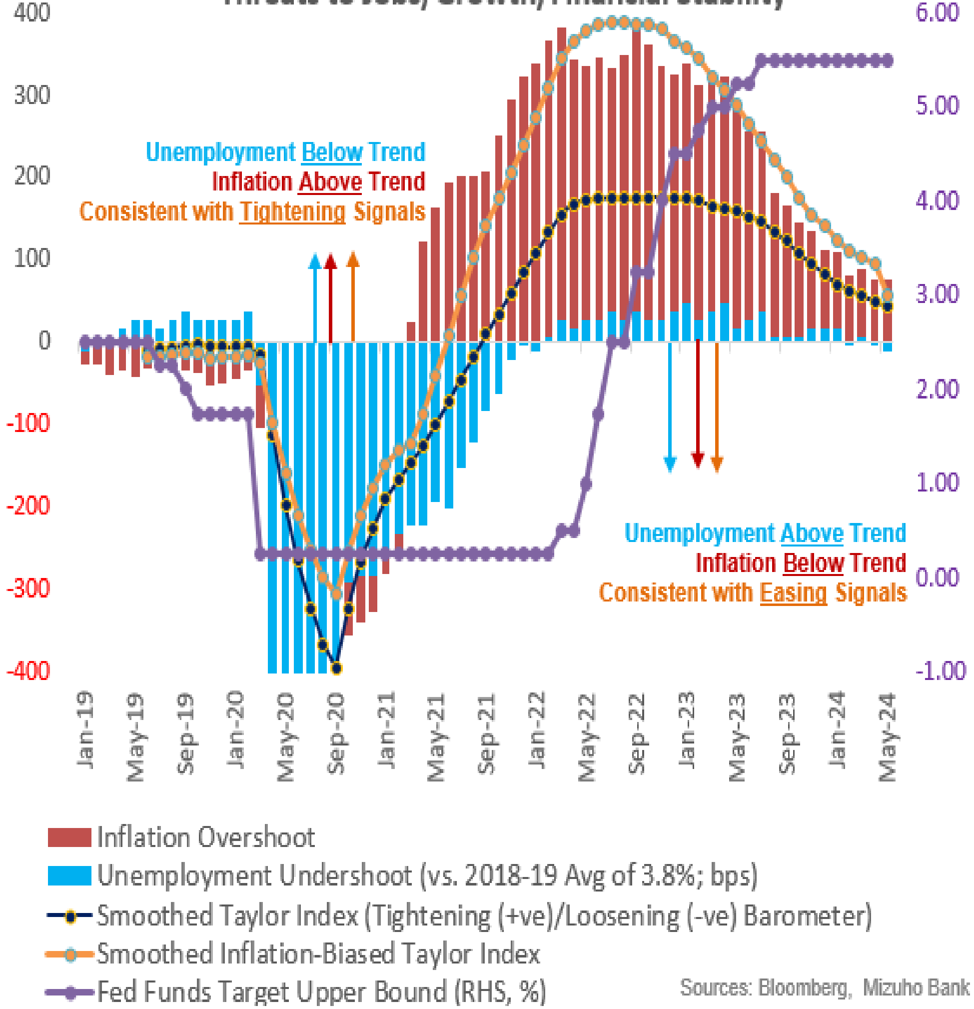
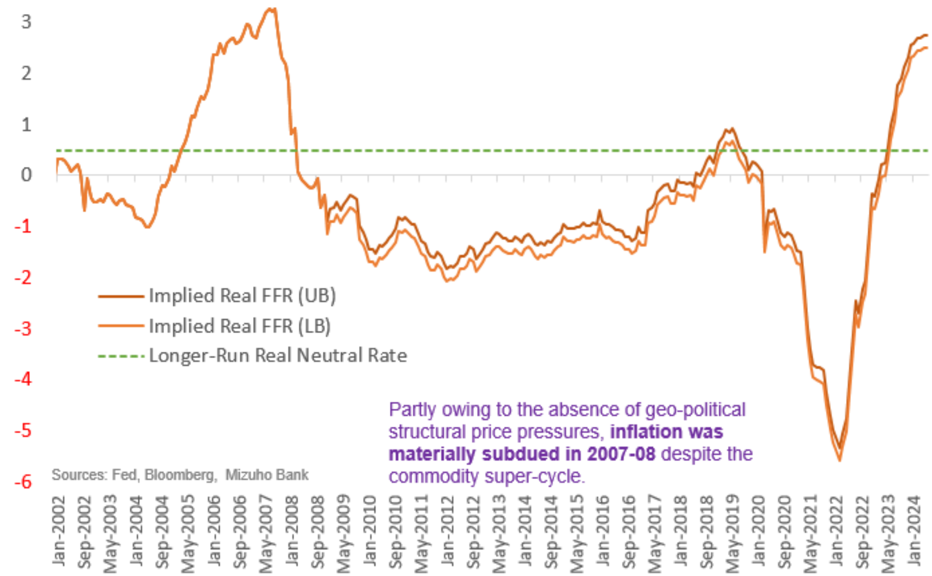
1c. Conditions are Exceptionally Tight! Taylor Rule Does Not Require This Much Restriction

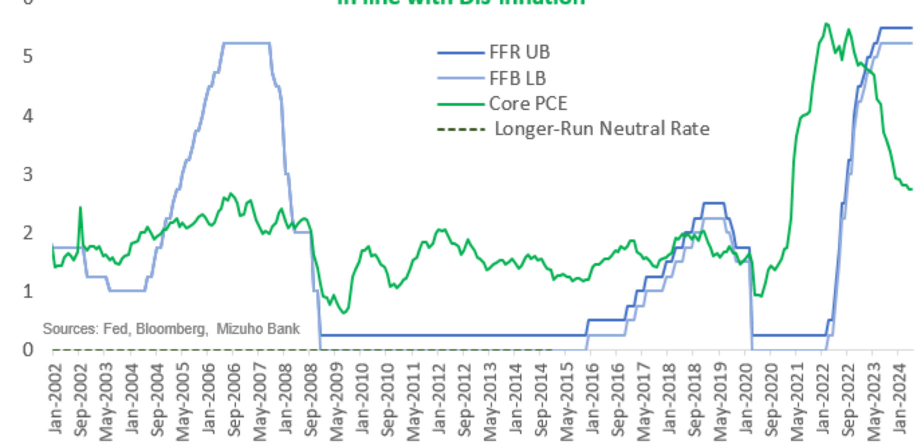
Taylor Rule: Current Setting are Deliberately More Restrictive amid perceptions of inflation risks … but *Response Function could change Fairly Quickly* on Threats to Jobs/Growth/Financial Stability



Compared to the Longer-term (assumed) Real Neutral Rate of 0.5%, Policy Now is About the Most Restrictive in 20 Years*



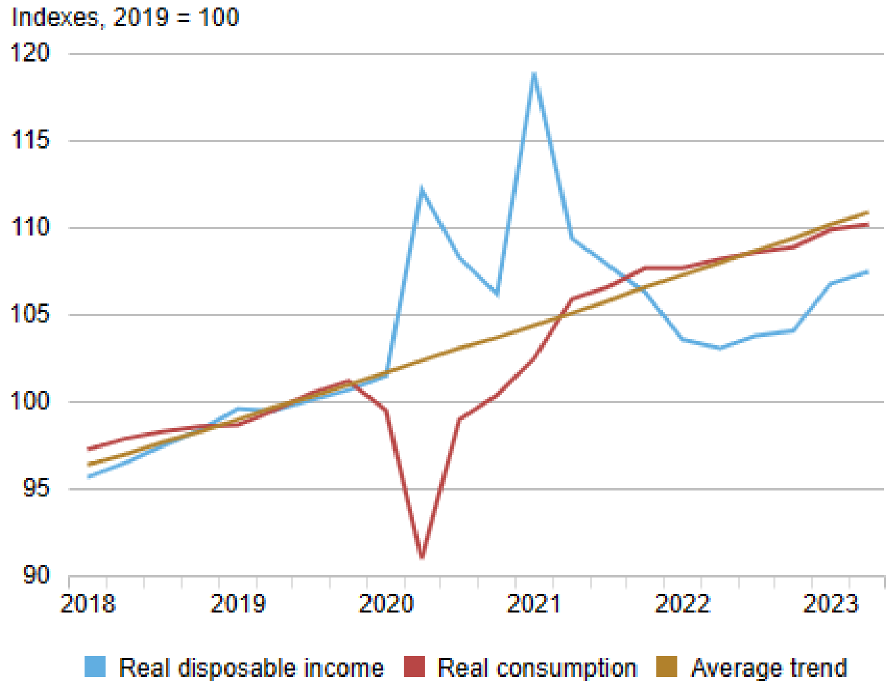
Headline of **2024 Rate Cuts** Subsumed **in the 'Dot Plot'** is **Not to be Mistaken for Effective Easing** … It is more **Calibraton in line with Dis-inflation**



1d. US Consumer Exceptionalism Requires Exceptional Conditions

U.S. Consumption Back to Trend but Income Lags

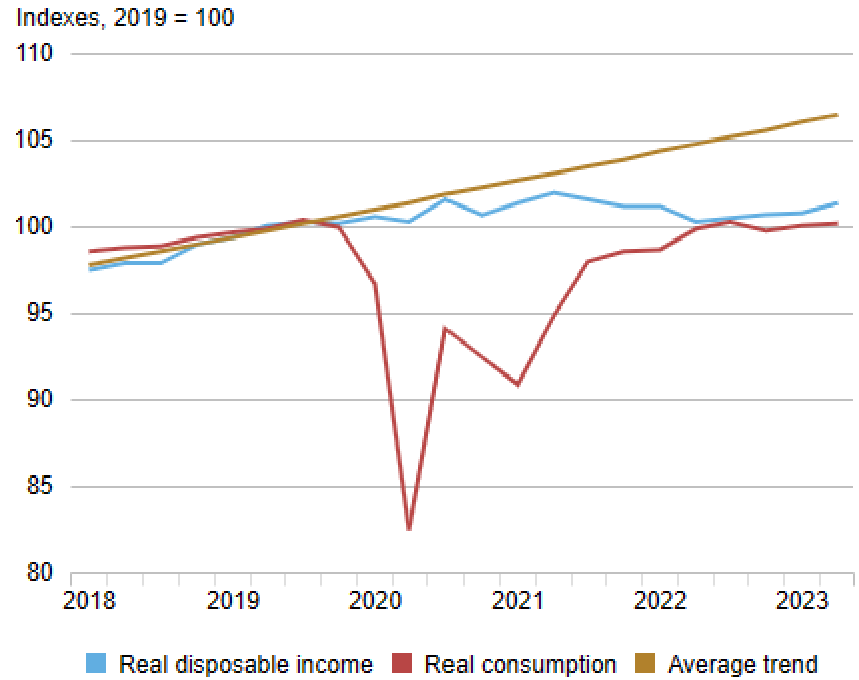
United States: Real Income and Consumption Indexes



Sources: Bureau of Economic Analysis, Integrated Macroeconomic Accounts; authors' calculations.
Note: The average trend for consumption and income is based on growth from the fourth quarter of 2014 to the fourth quarter of 2019.

Foreign Income and Consumption Tracking Below Trend

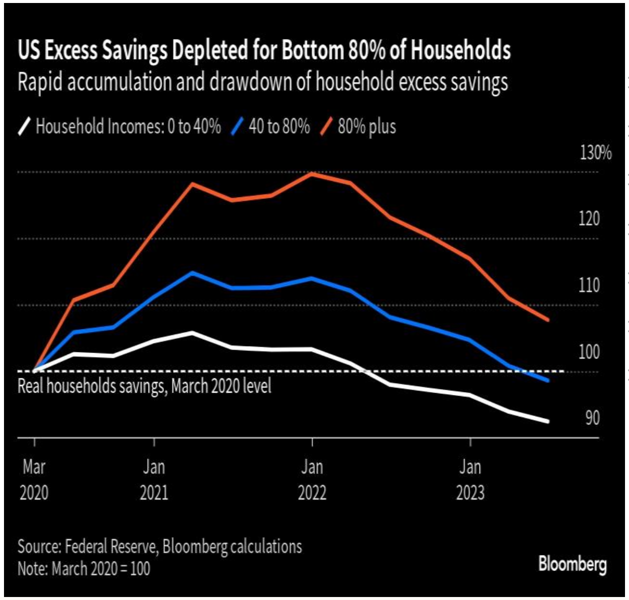
Foreign Economies: Real Income and Consumption Indexes

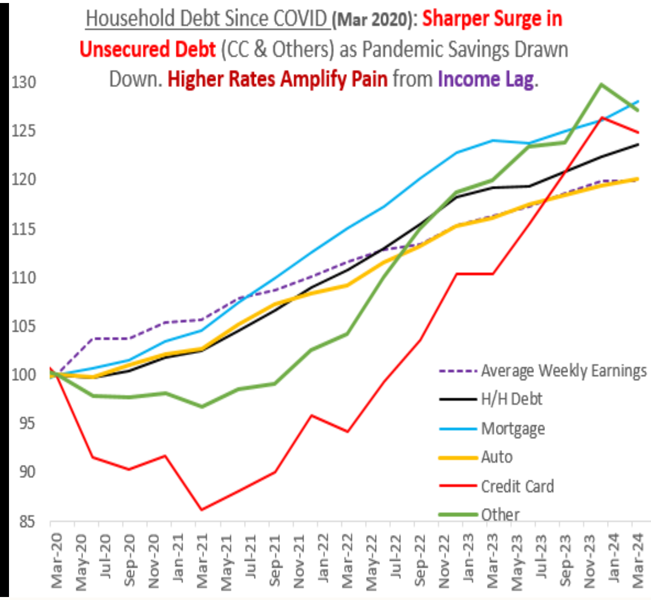


Sources: Eurostat; UK National Statistical Office; Japanese Cabinet Office; Statistics Canada; authors' calculations.
Notes: The foreign high-income series is a GDP-weighted average of the euro area, Japan, the United Kingdom, and Canada. Disposable income data for the second quarter of 2023 in Japan have not yet been released. Income for that quarter is extrapolated from the first quarter of 2023 at the average growth since the first quarter of 2022. Japan represents about 15 percent of the foreign index.

Source: Federal Reserve Bank of New York

1e. Consumer Tea Leaves Suggest Intensifying Cash-flow Constraints on Demand Growth





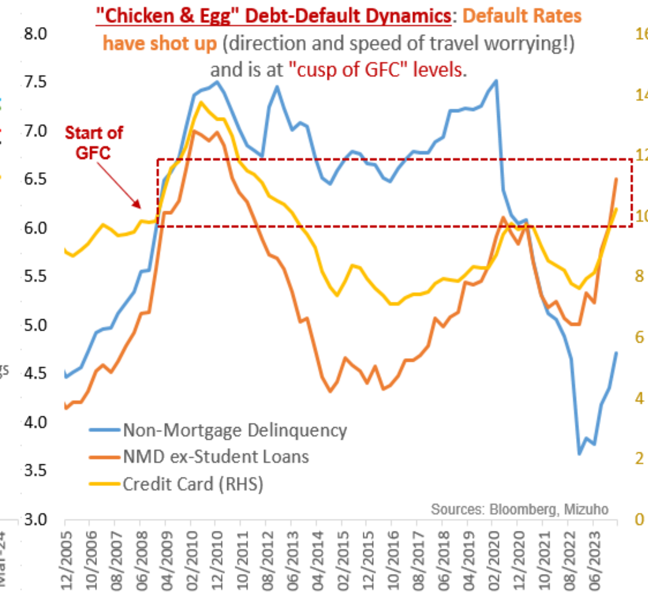
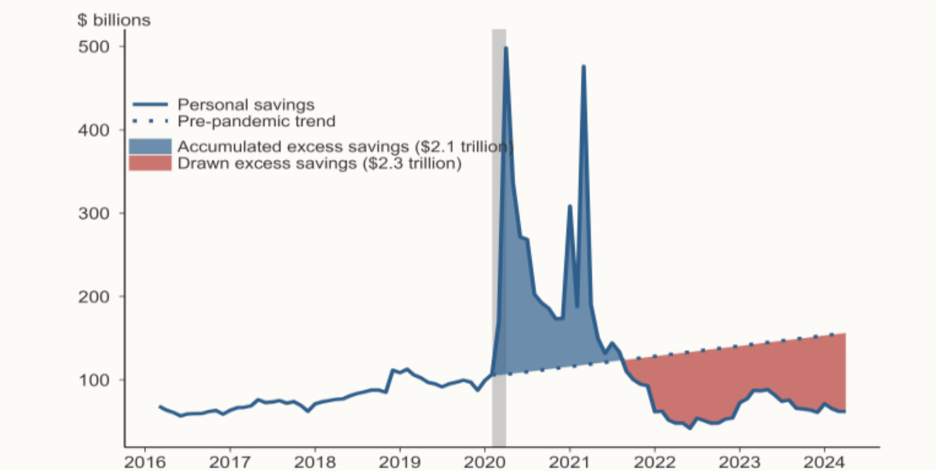


Chart 1: Aggregate personal savings compared with the pre-pandemic trend



Note: Gray shaded area represents NBER recession dates. Source: Bureau of Economic Analysis and author: calculations.

Chart 2: Cumulative aggregate pandemic-era excess savings

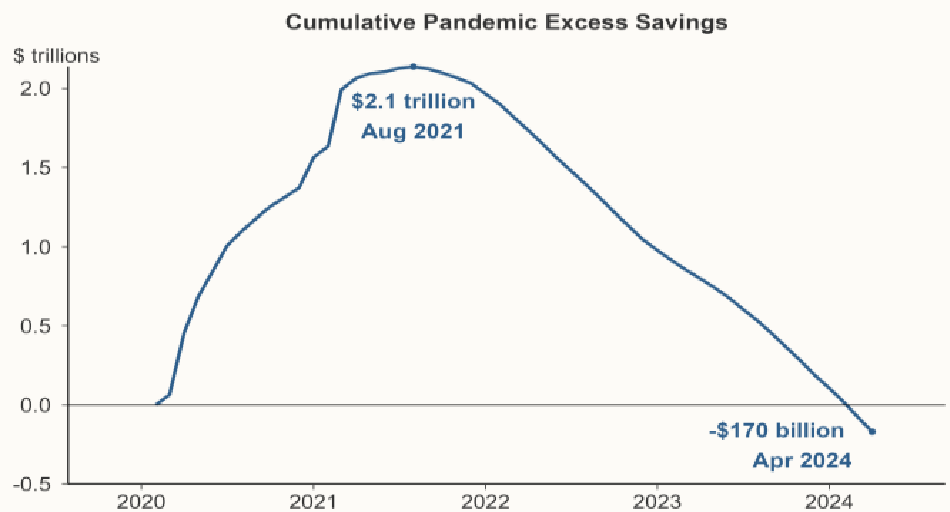


Chart from Bloomberg, San Francisco Fed,

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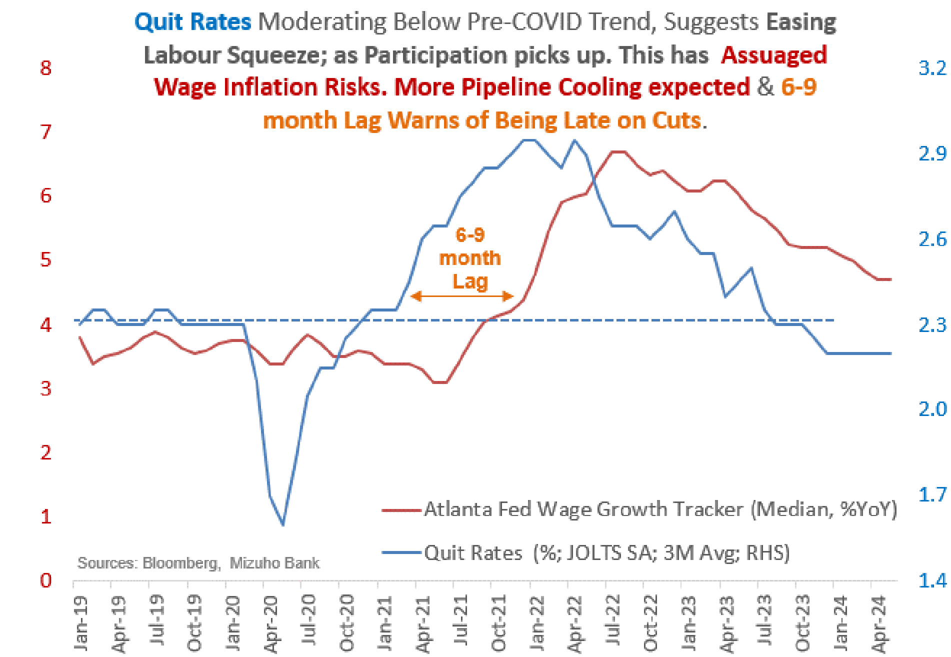
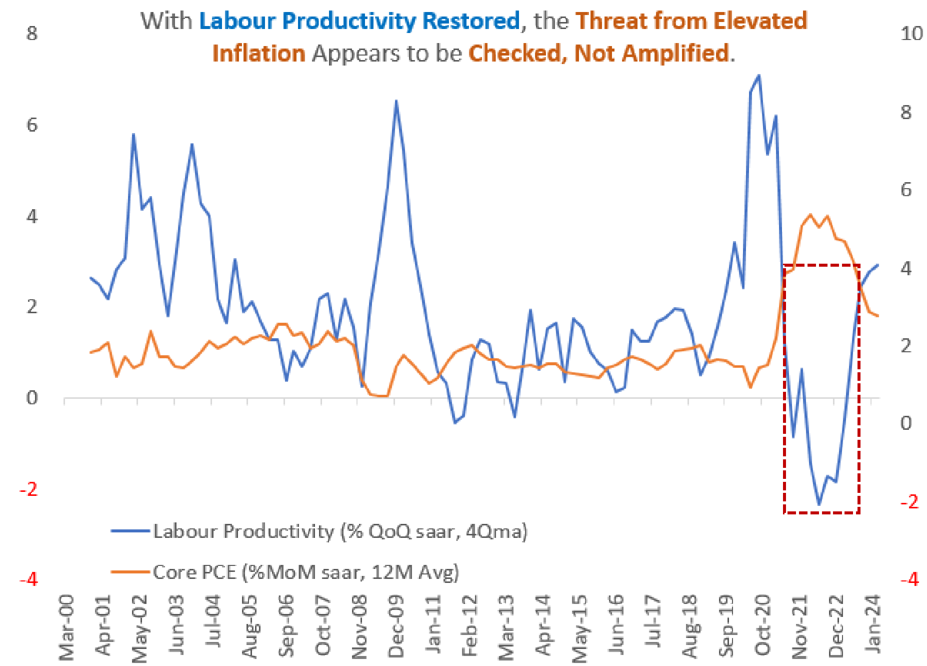
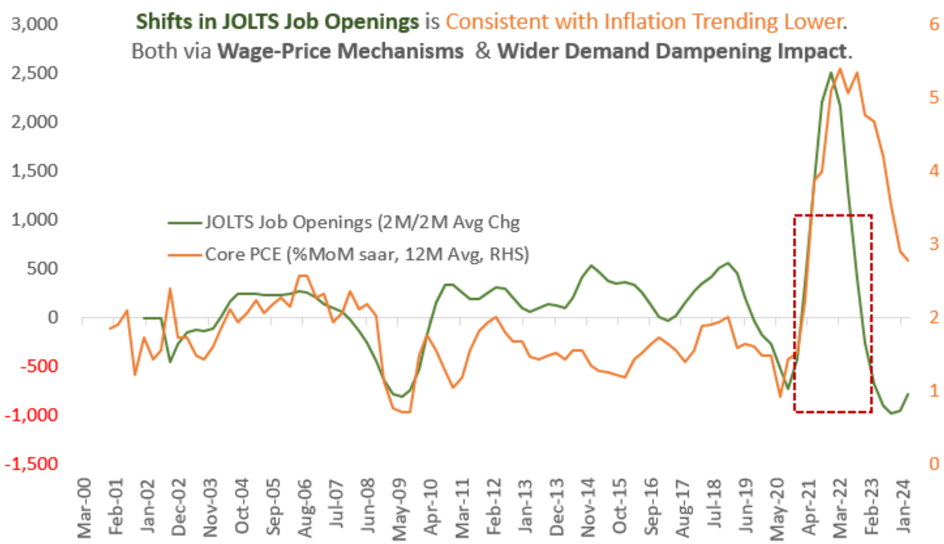
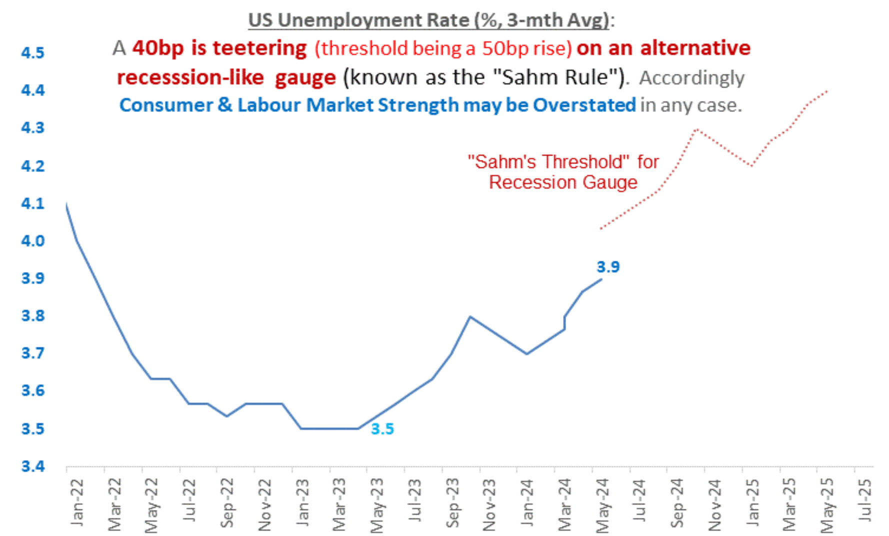
1f. Significantly Diminished Wage-Price Risks May Augment Fed Response Function









1g. The Fed's "Type-2" Error Risks – *Baggage from "Transitory" Risks "Too High for too Long"*

	End-2021	End-2022	End-2023	2024				2025				2026		2027	
			Q4 23	Q1 24	Q2 24	Q3 24	Q4 24	Q1 25	Q2 25	Q3 25	Q4 25	H1 26	H2 26	H1 27	H2 27
Fed Funds Target Rate Ceiling	0.25	4.50	5.50	5.50	5.50	5.25	5.00	4.25	3.50	3.00	2.75	2.50	2.50	2.50	2.50
Fed Funds Target Rate floor	0.00	4.25	5.25	5.25	5.25	5.00	4.75	4.00	3.25	2.75	2.50	2.25	2.25	2.25	2.25
UST 2Y Yields	0.73	4.43	4.25	4.62	4.59	3.93	3.50	2.70	2.69	2.80	2.53	2.50	2.30	3.33	3.18
UST 10Y Yields	1.51	3.87	3.88	4.25	4.35	4.16	3.88	3.22	3.35	3.42	3.28	3.33	3.18	3.33	3.18

Sources: Bloomberg, Mizuho Forecasts

"Too High for Too Long" Risks Defer but Don't Diminish Fed Rate Cuts

- The quirks of post-pandemic durability in demand defer Fed rate cuts vis-à-vis past Fed cycles.
- But 'Type-2' error (from overcompensating for "transitory") of "too high, for too long" are accentuated now
- Which accentuates the risks of having to catch-down more hurriedly with belated rate cuts.

"2024 Runway Curtailed, but 2 Cuts Likely …

- Barring a crisis (not our base case), rate cut run-way for 2024 is constrained by data-watching and elections.
- July FOMC virtually ruled out. September, November and December are "live".
- 50-75 bps of rate cuts still on the table, with 50bp being most likely.

Rate Cuts to Gather Pace in H1 2025

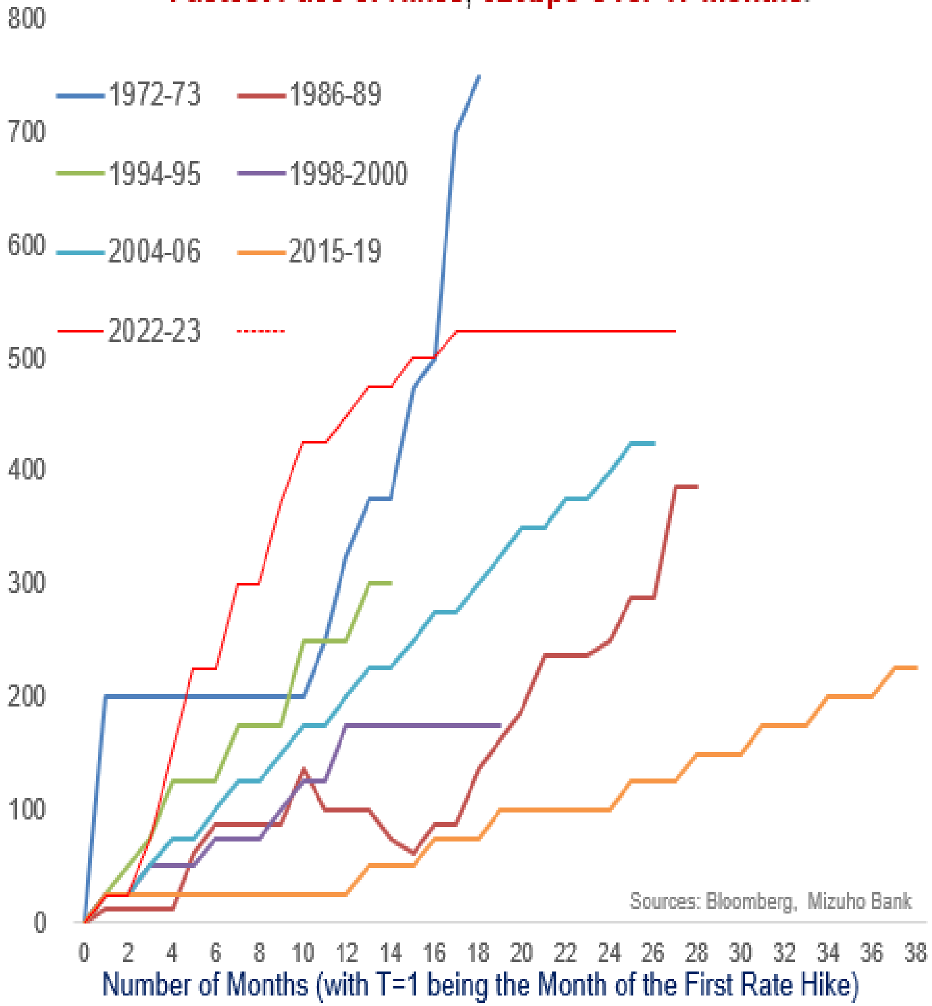
- Sharper demand softening alongside rapid slowdown set to diminish wage-price spiral risks.
- Consequently, Fed rate cuts will gather pace in H1 2025 so as to alleviate acute policy restriction.
- Up to 200bp of rate cuts by mid-2025 is not as outlandish. Fact is, 3.25-3.50% is likely still restrictive.

Consumer Slowdown, Not Crisis

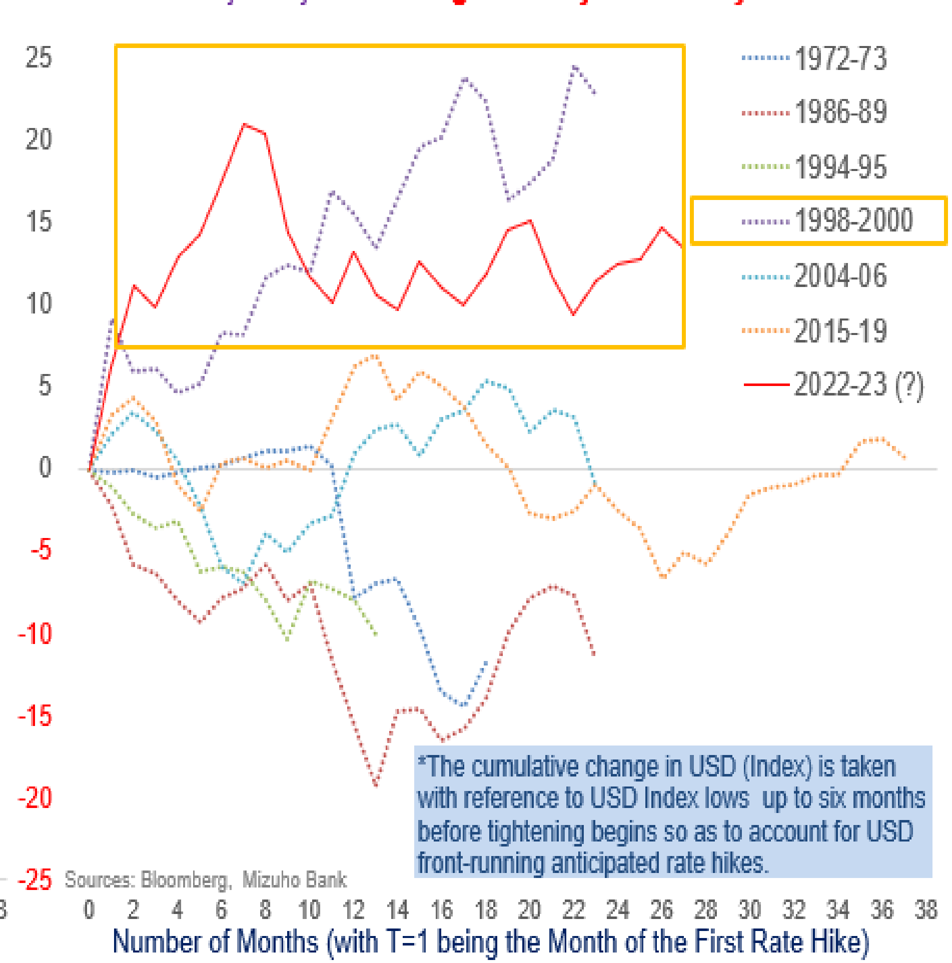
- Brisker cuts are premised on sharper consumption slowdown amid tightening cash-flows ➔ Not so soft landing
- And not a crisis from a balance sheet shock – for which far deeper and larger rate slashing will be required.

2a. Policy Nuance: Not All Pivots are Created Equal! "Competitive Pivot"/US Exceptionalism

Fed Hiking Cycle (Cumulative Rate Hikes; bp): **Although not the Greatest Amplitude of Rate Hikes** (1970s More Brutal, with >700bp of Hikes), **this Cycle Marks the Fastest Pace of Hikes**; **525bps Over 17 Months**.



Corresponding USD Performance (Cumulative % Chg*): **Notably, the Current Rate Hike Cycle Has Resulted in the Sharpest Phase of USD Strength in the First 8-9 months**; moderating below corresponidng 1998-2000 Trajectory but **still significantly more buoyed**.



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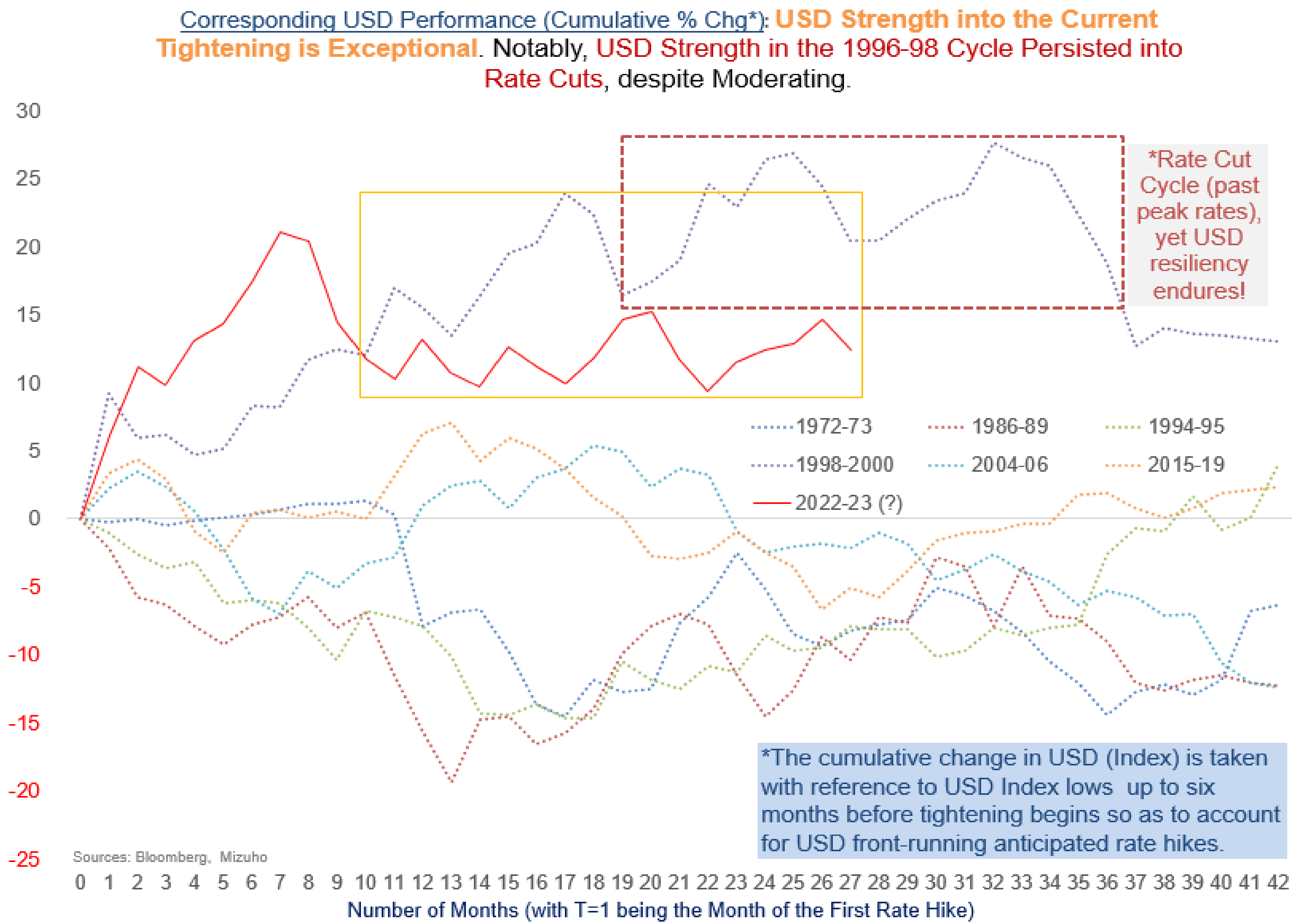
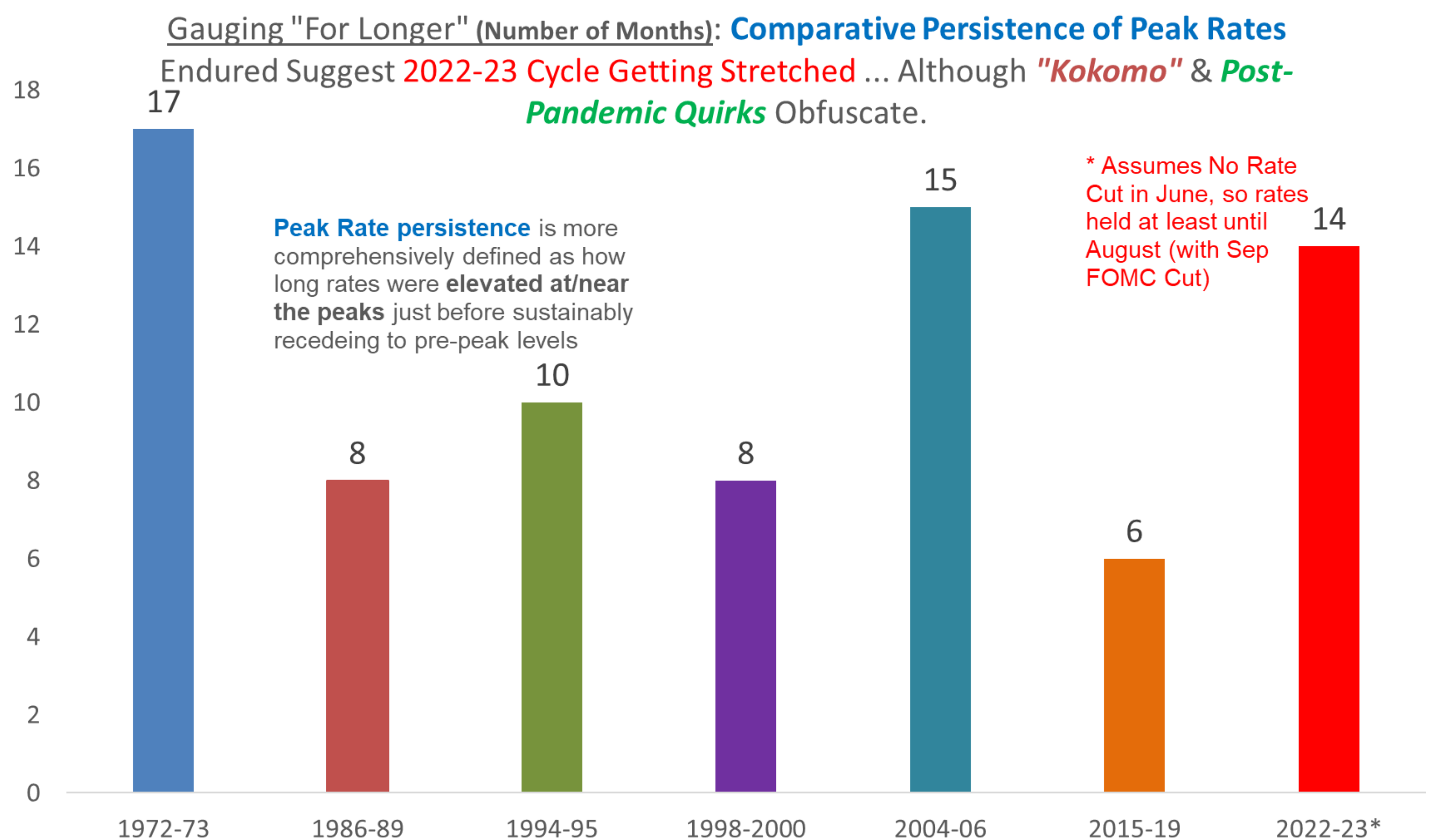
2a: Corresponding USD Response is Not the Usual "Peak USD ahead of Peak Fed"

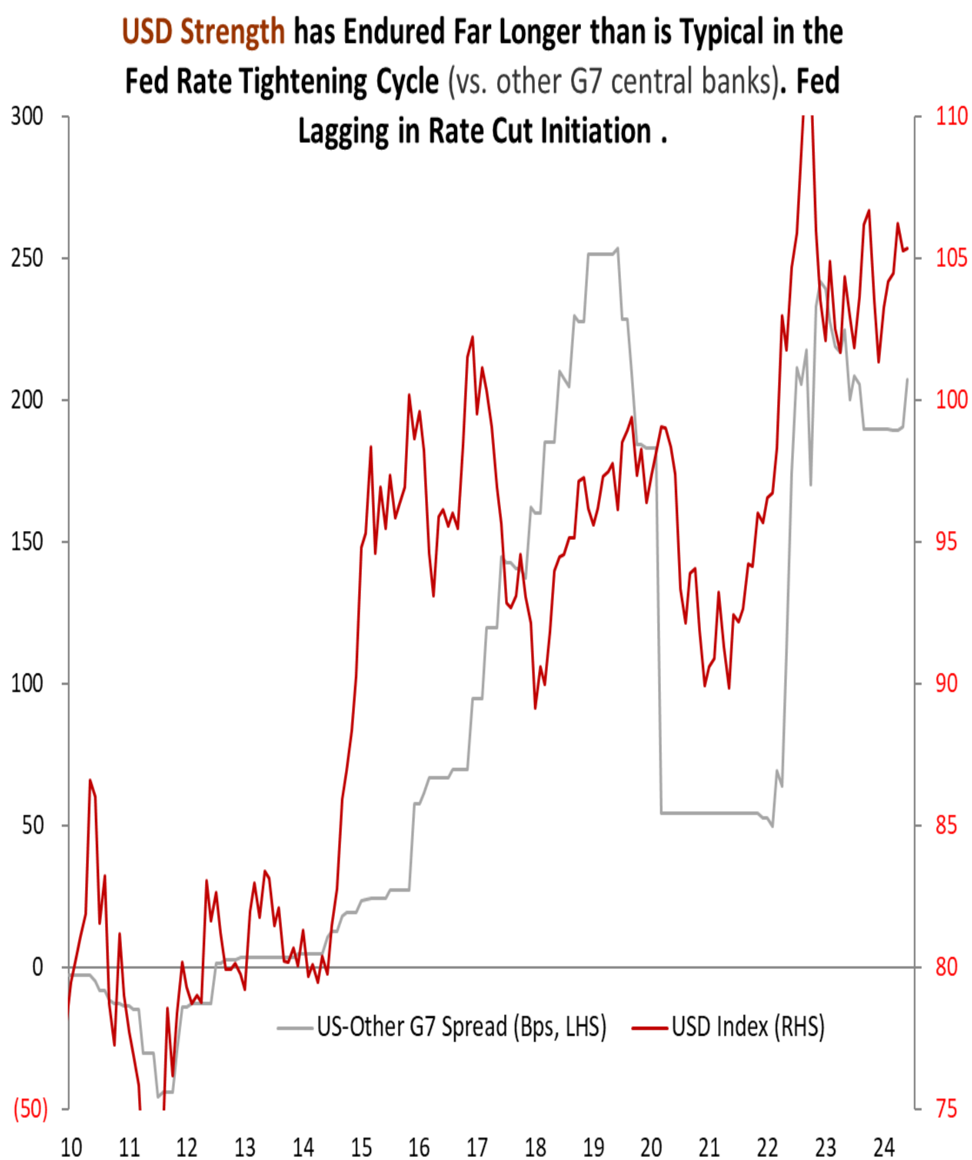


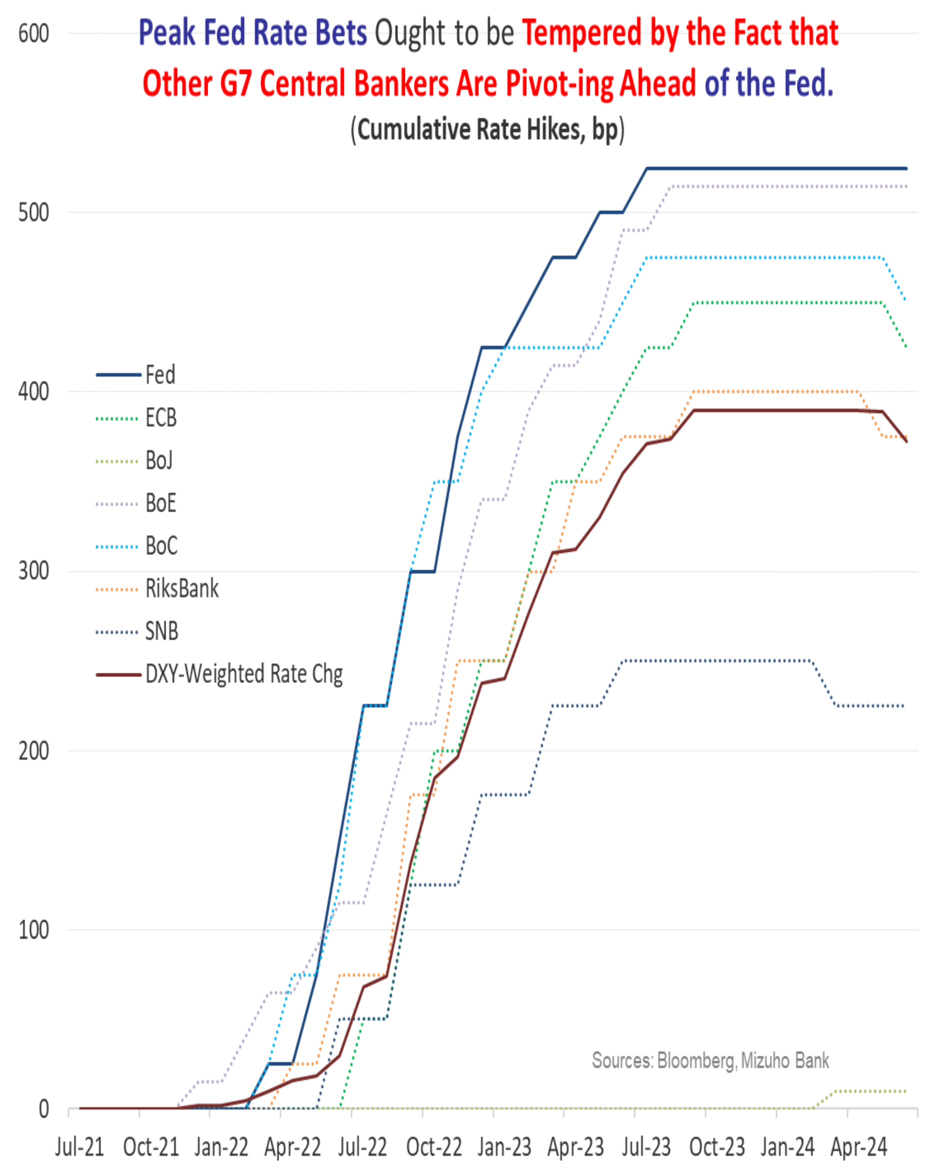
2b: Peak Persistence Increases Tail Risks on Both Ends – Fear & Fed Involved!



Sources: Bloomberg, Mizuho Bank

2c: Relative Rate Strength Understate "Competitive Pivot" Inclination Shifts





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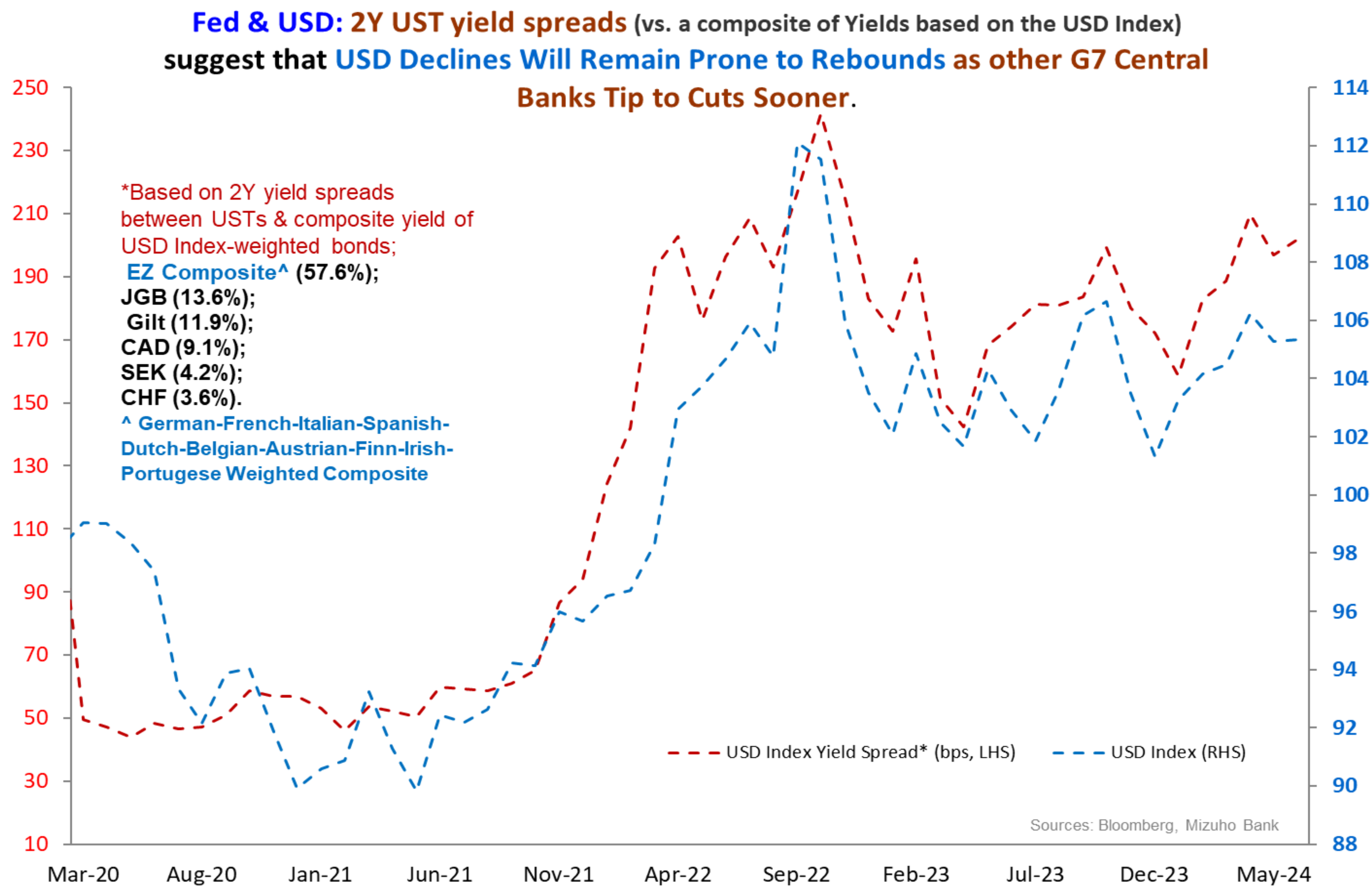
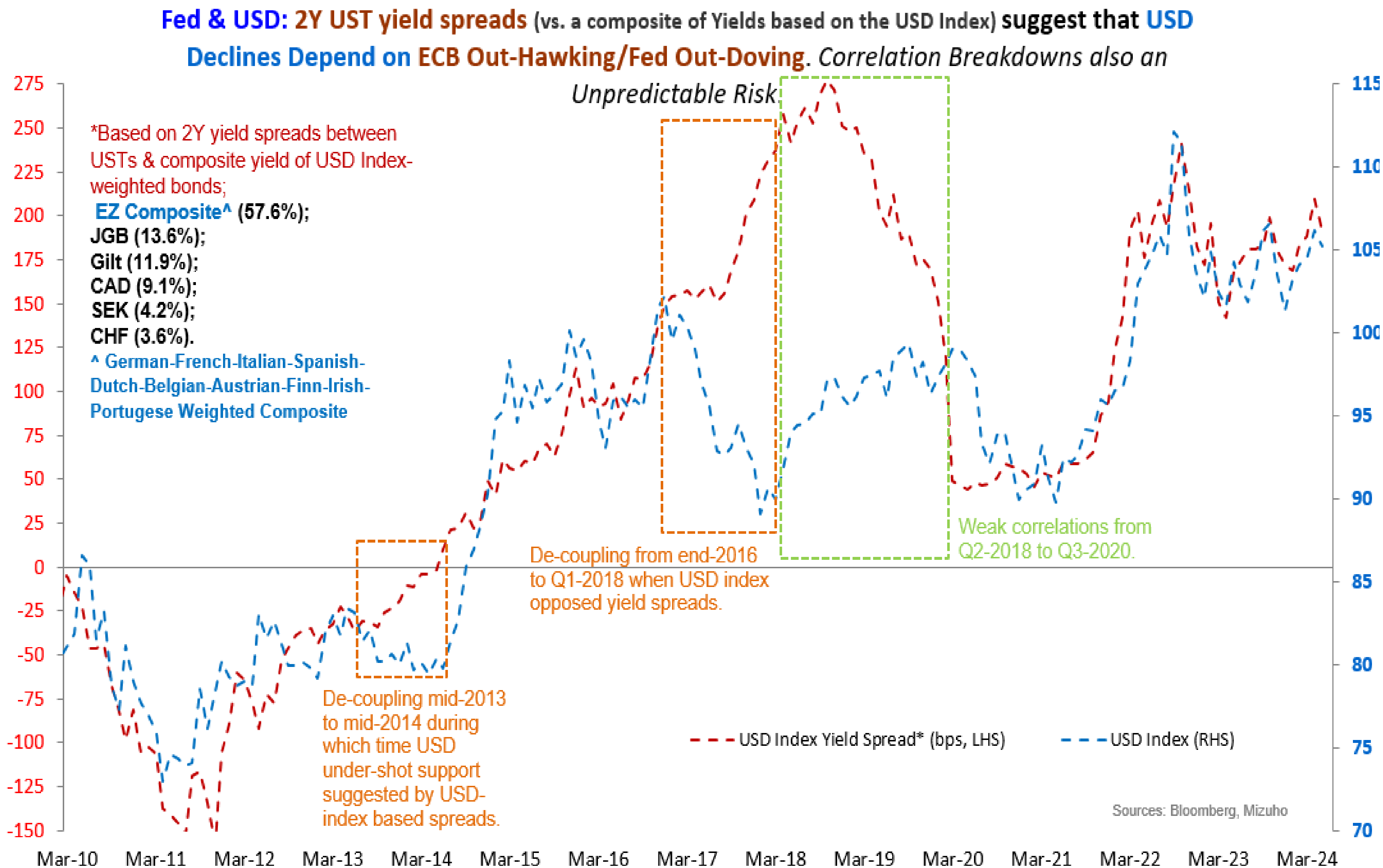
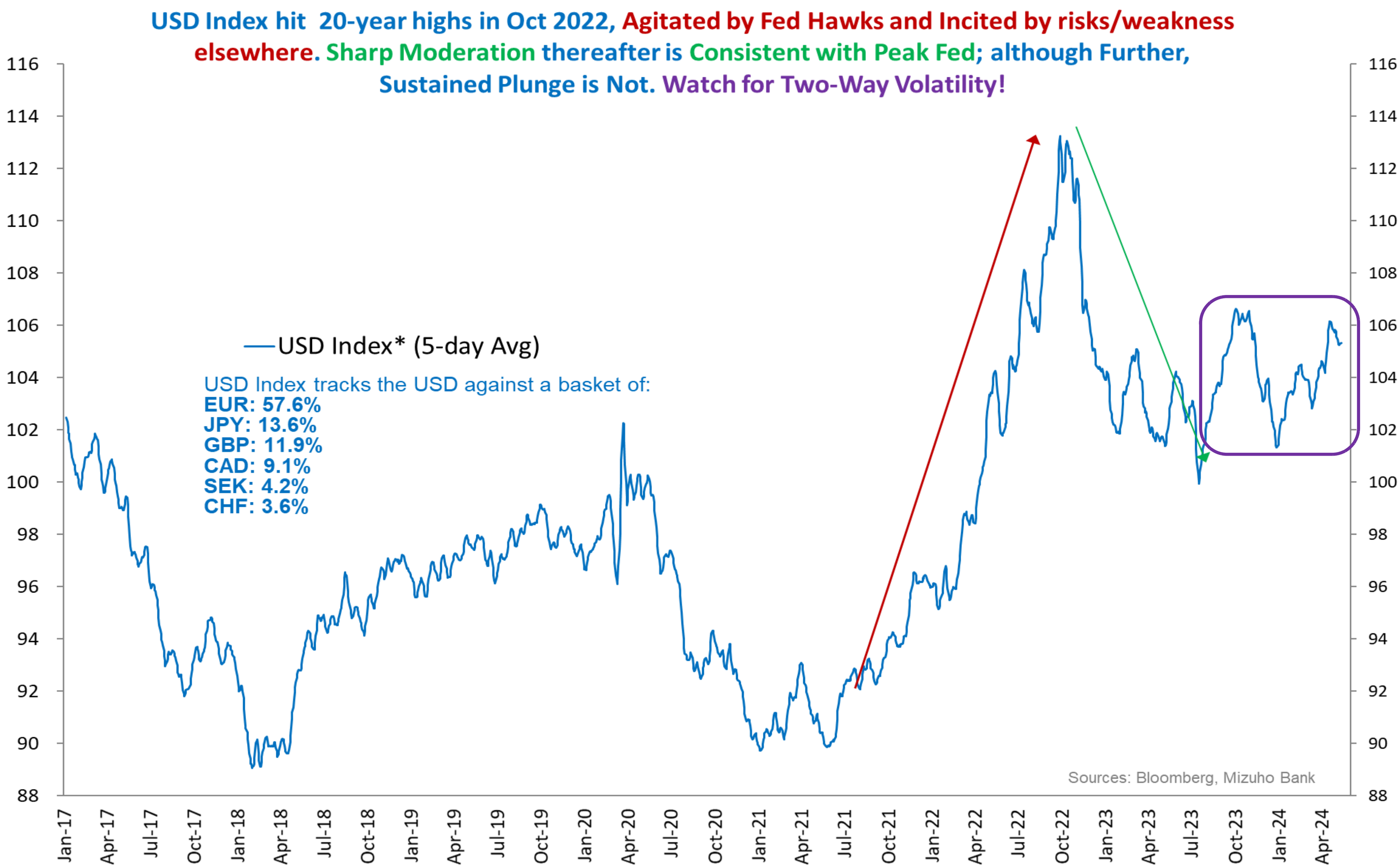
2c: Yield Spreads Better Capture the Tendency for USD Bounce .. At Least USD Resiliency



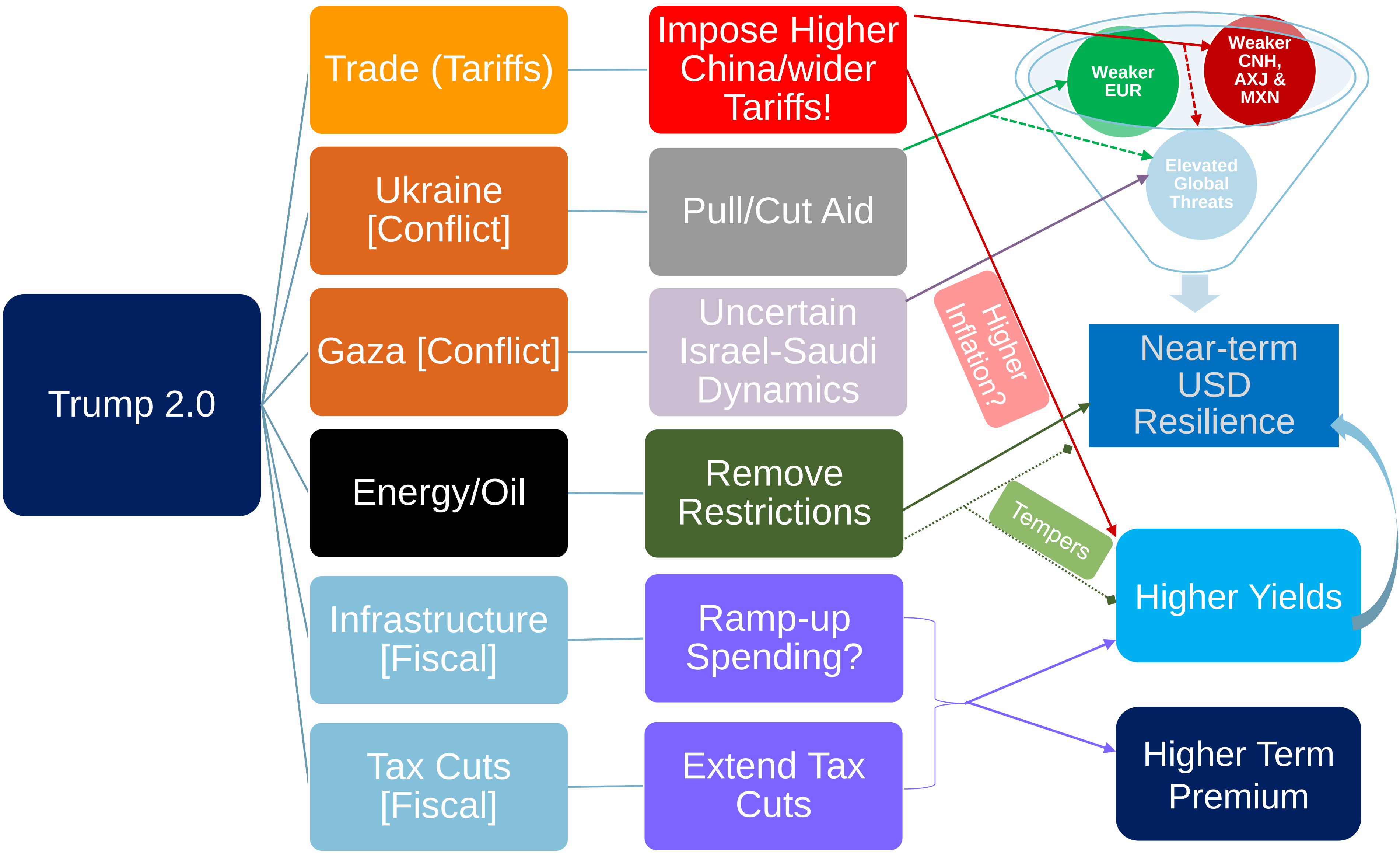
2c Caveat: Correlation Shifts & De-Coupling Cloud the Outlook!



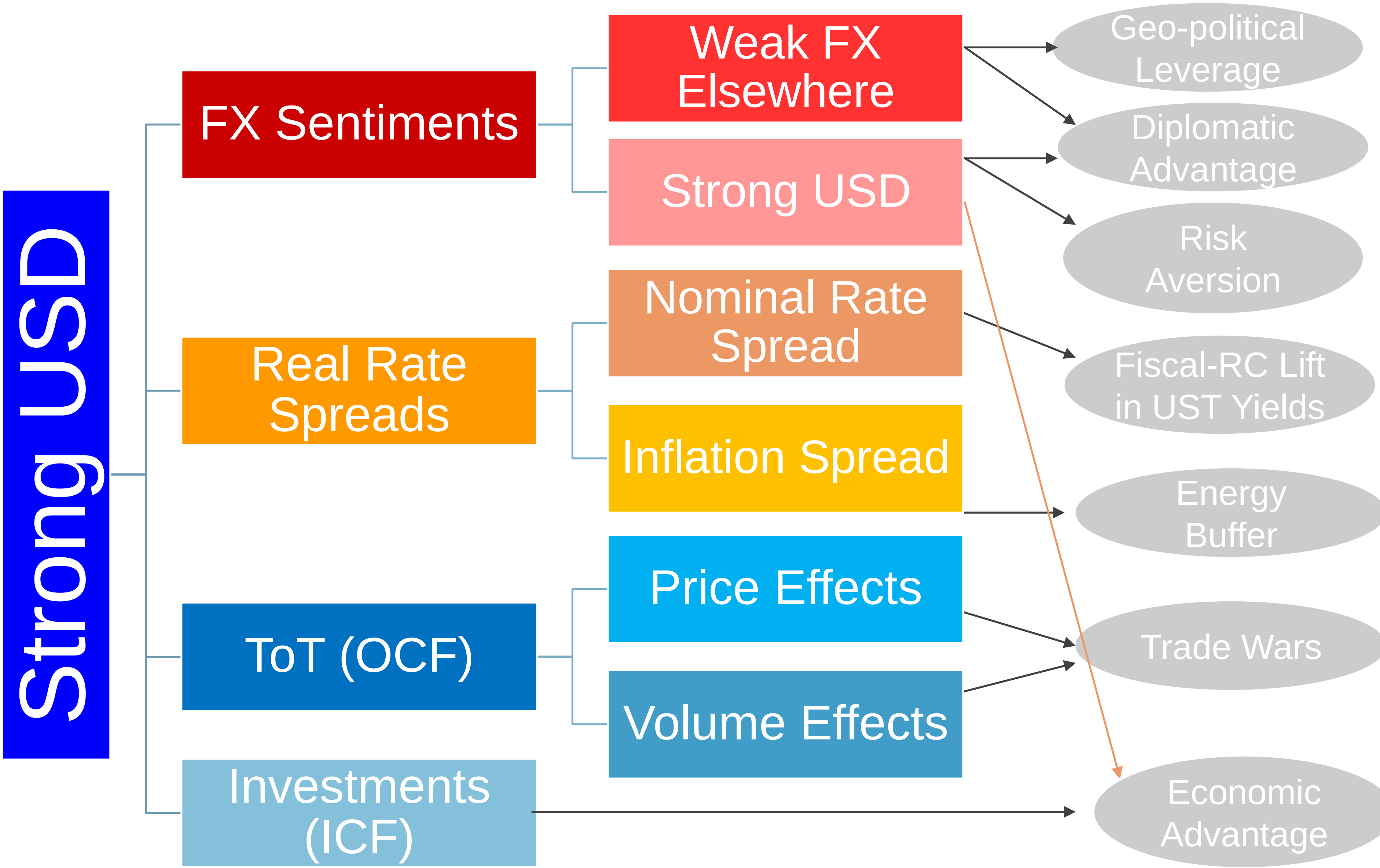
2d: Peak USD is Not the Same as a Bearish USD



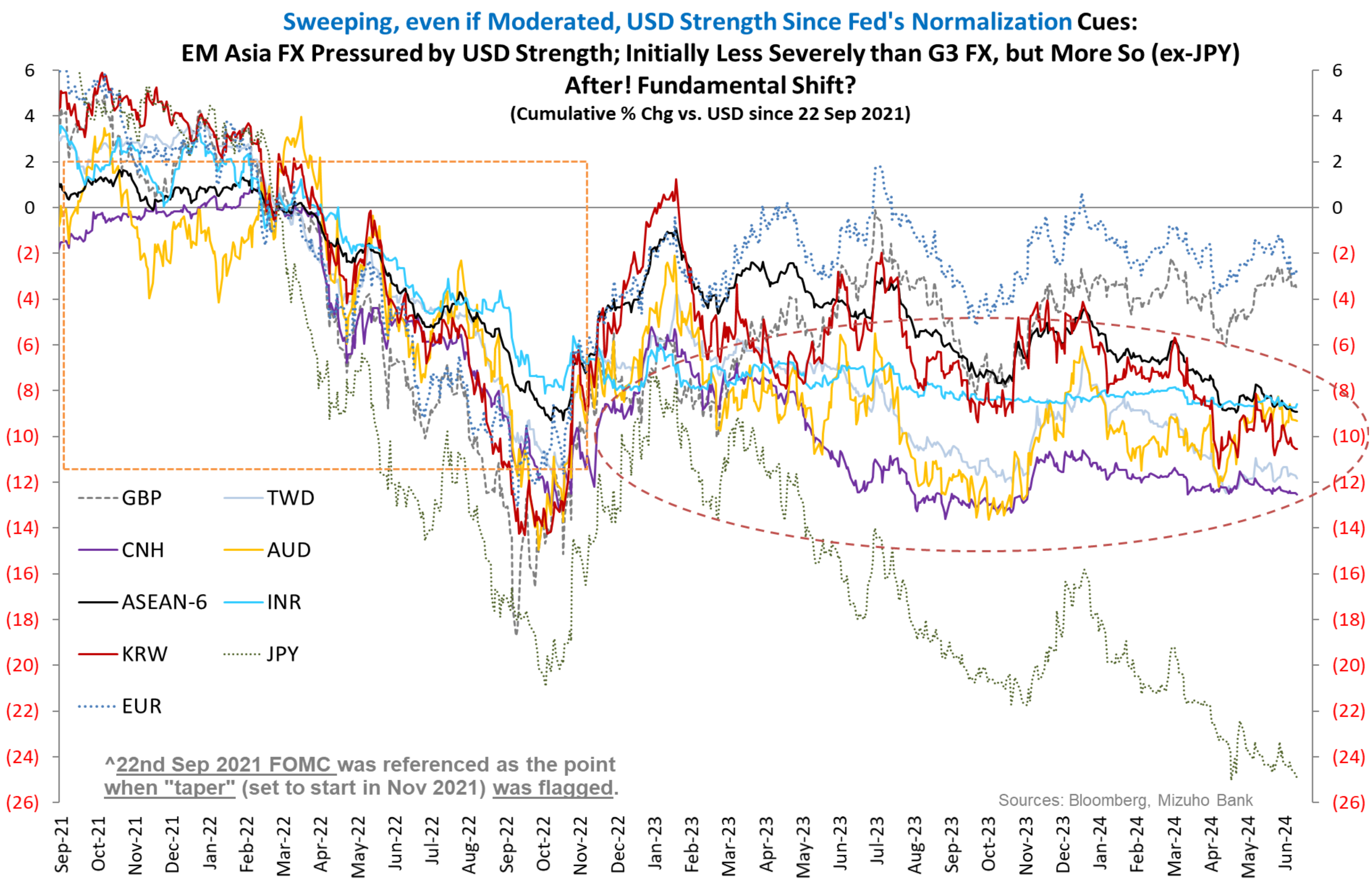
3. Politics: Trump 2.0 (US Elections): Bracing for Geo-economic Blows



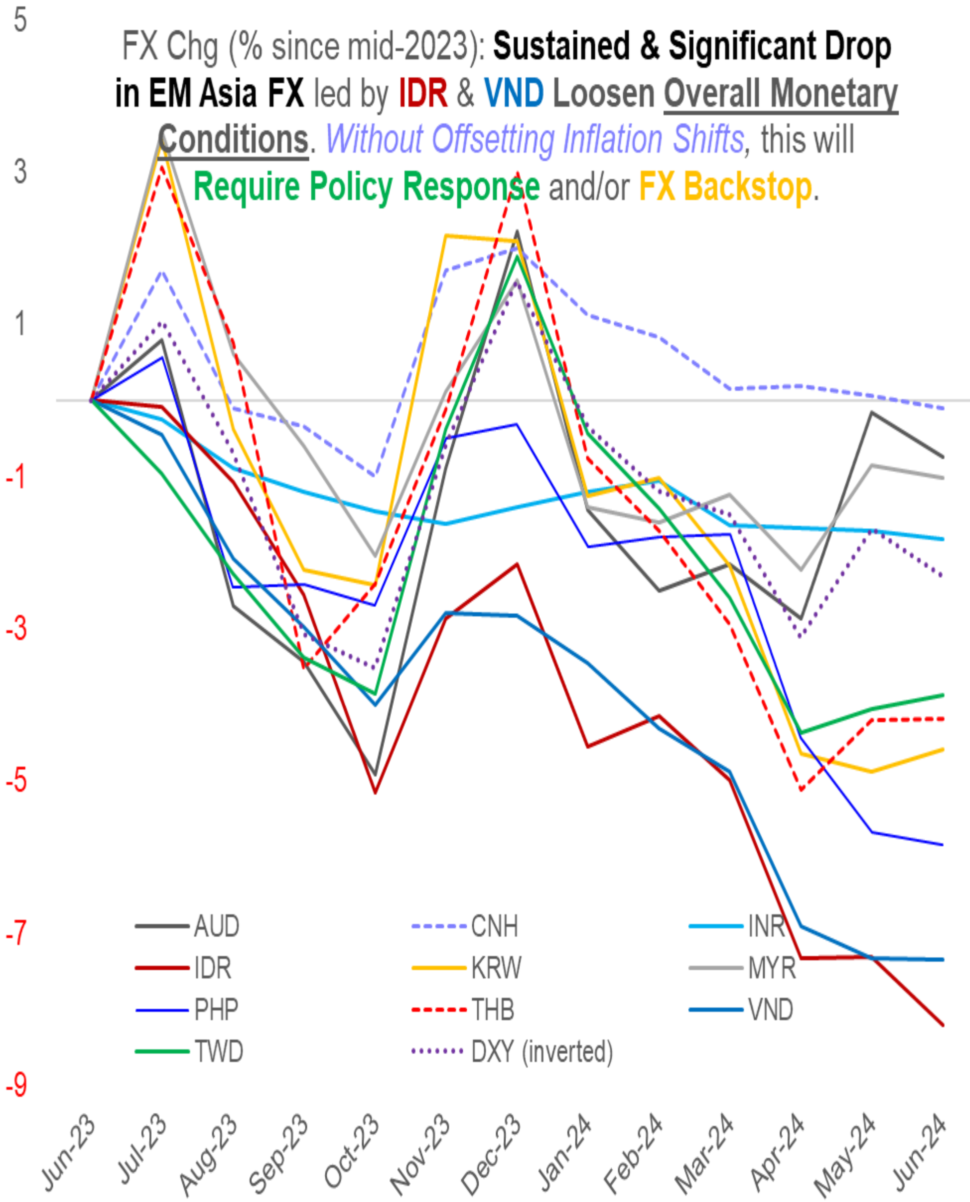
Channels of "Dollar Trump"

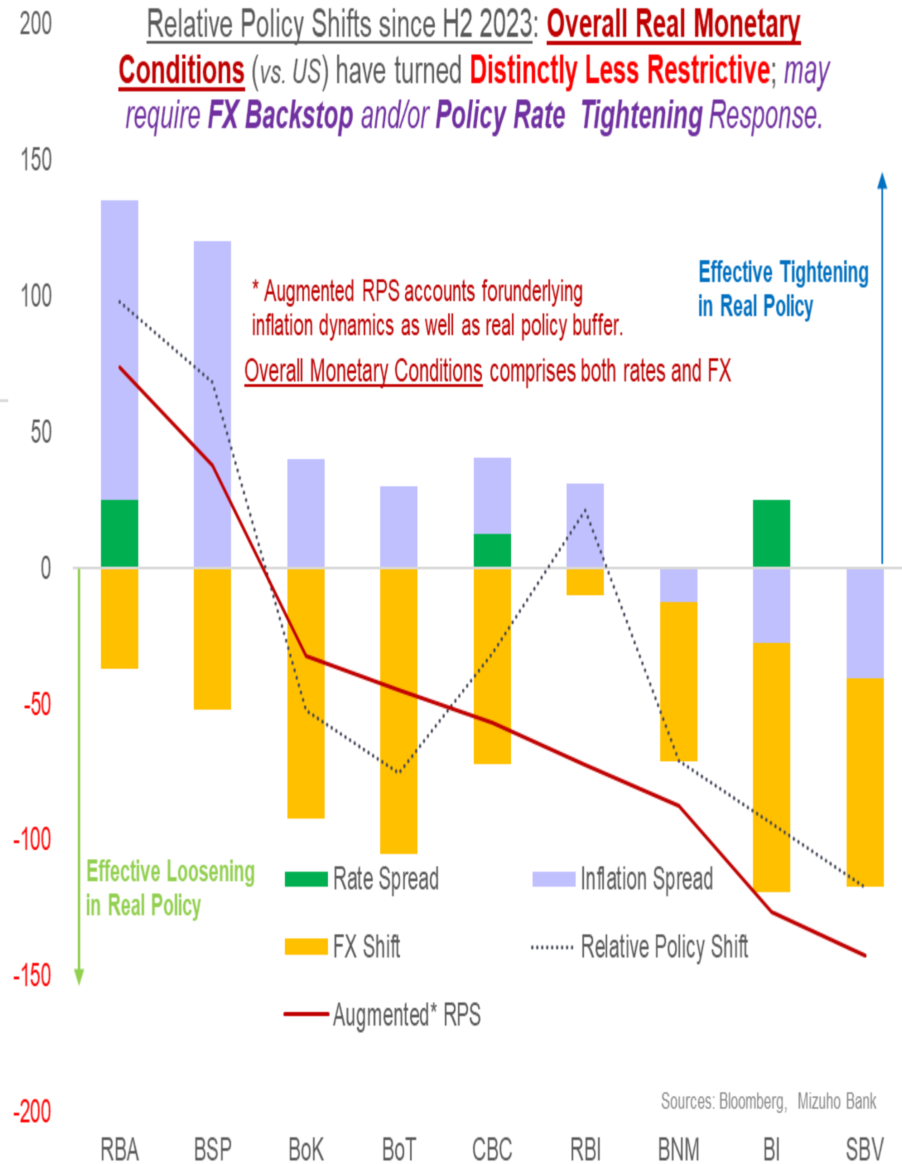


4a. Relative AXJ Under-performance is Worth Analyzing … Apart from Hysteresis Risks



4b. EM Asia Erosion: … With FX Amplifying Circular/Reflexive Policy-FX Risks ➔ Reflexivity!





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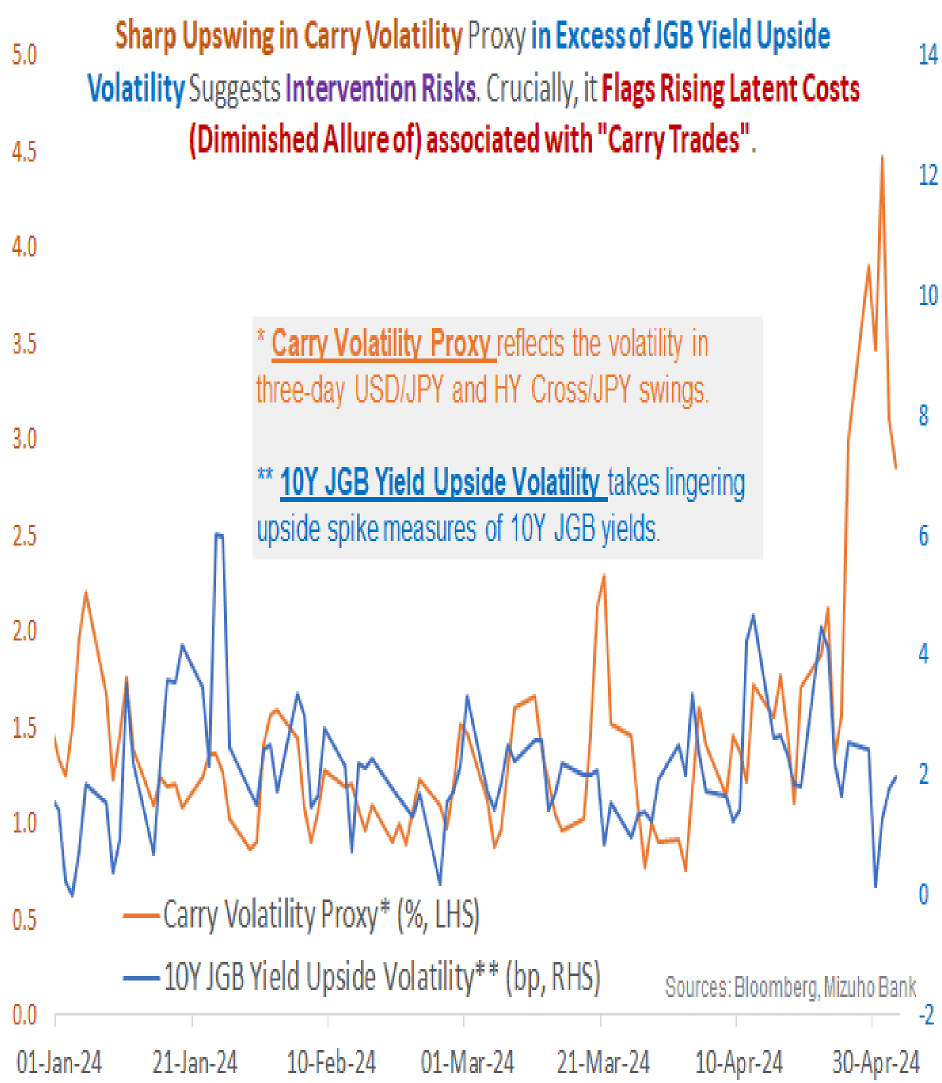
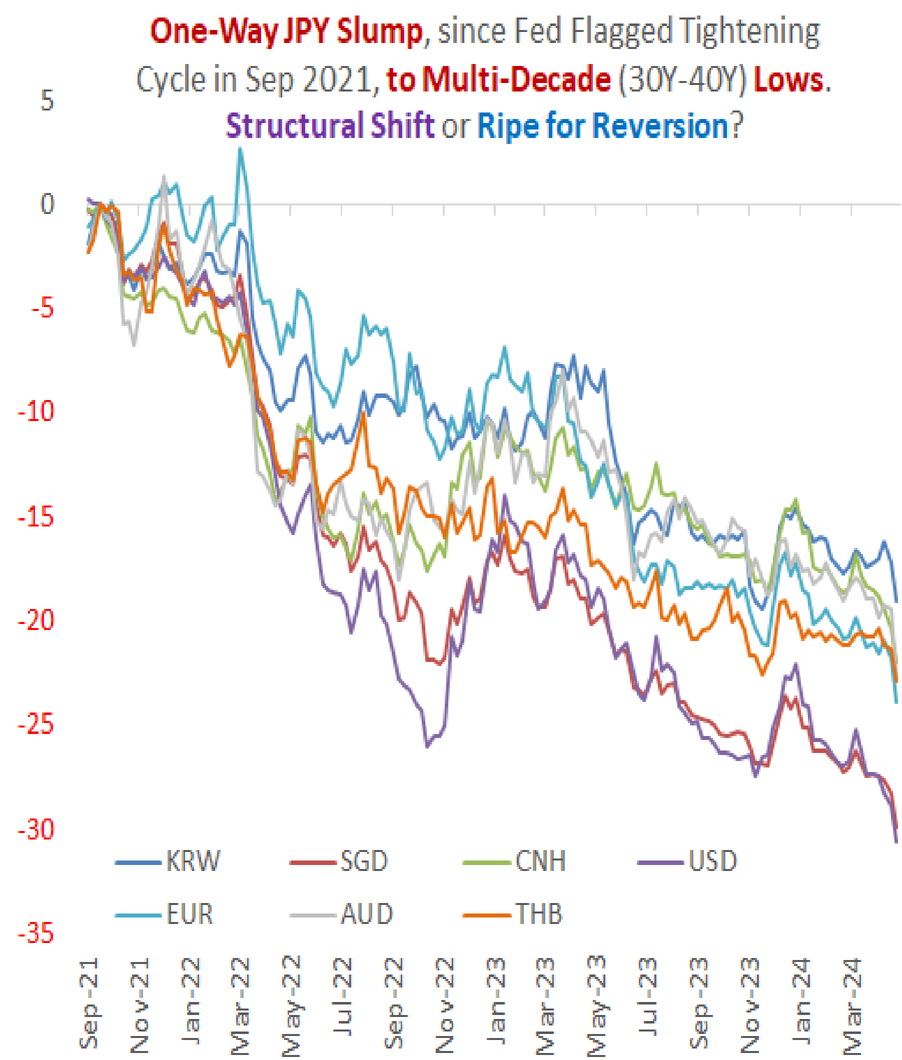
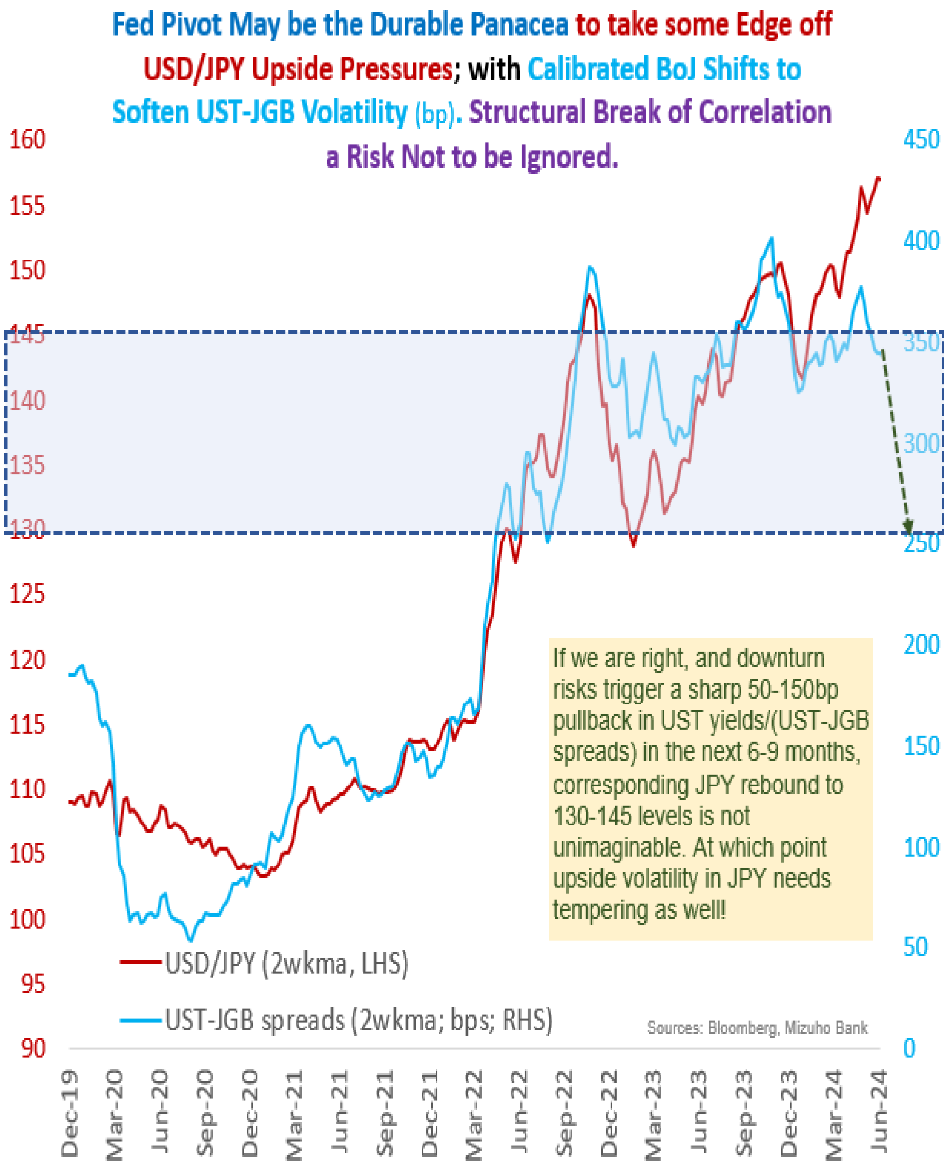
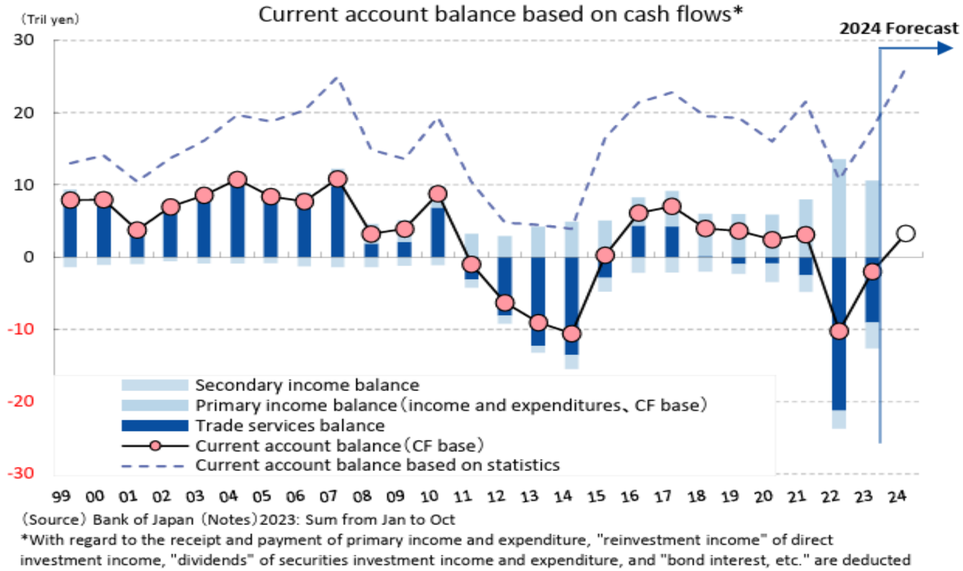
4c. Latent JPY (Upside) Volatility with "Carry (Unwind) Impact!

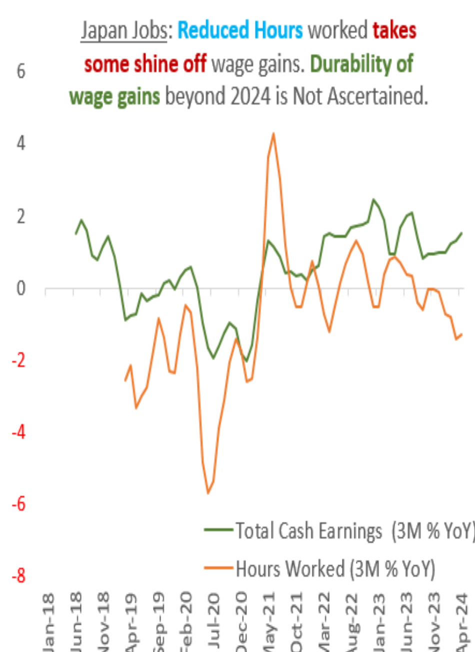


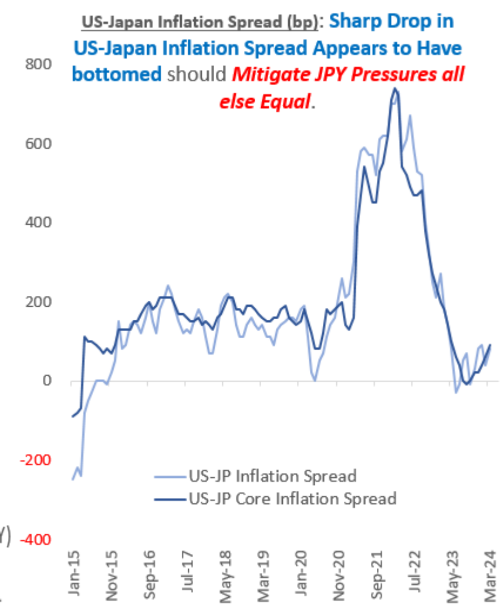


4c: Despite JPY Pressures (*"BoJ Problem"*), Sharp JPY Upside Introduces *"Fed Solution" Risks*



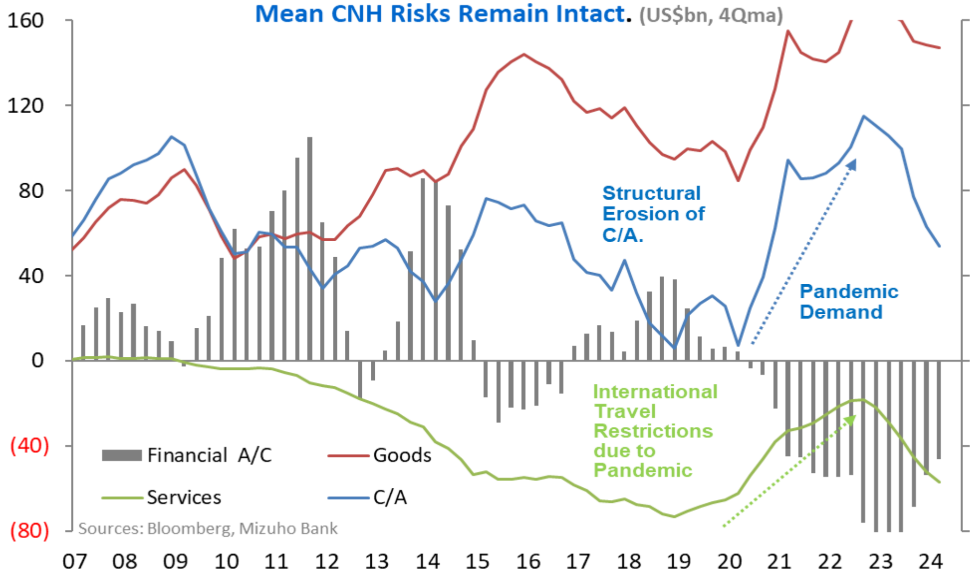






5a. China Factor: CNH is Still Not Out of the Woods & A Drag Factor!

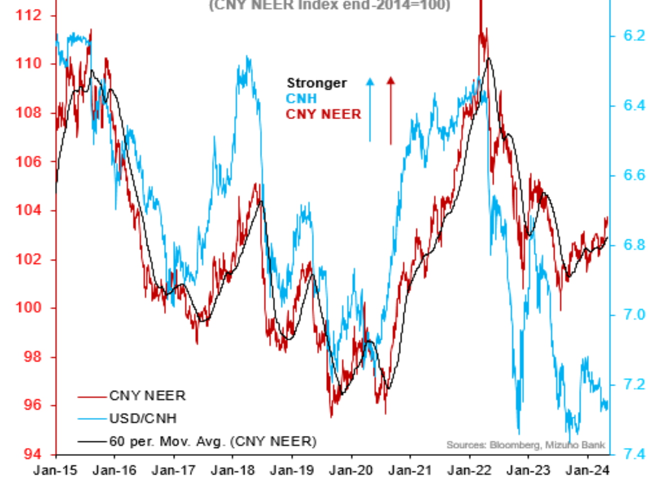
China: Goods Surplus Surge from Pandemic Demand & Diminished Net Tourism Outflows Are Fading Quickly; & Capital Outflows Mean CNH Risks Remain Intact. (US$bn, 4Qma)



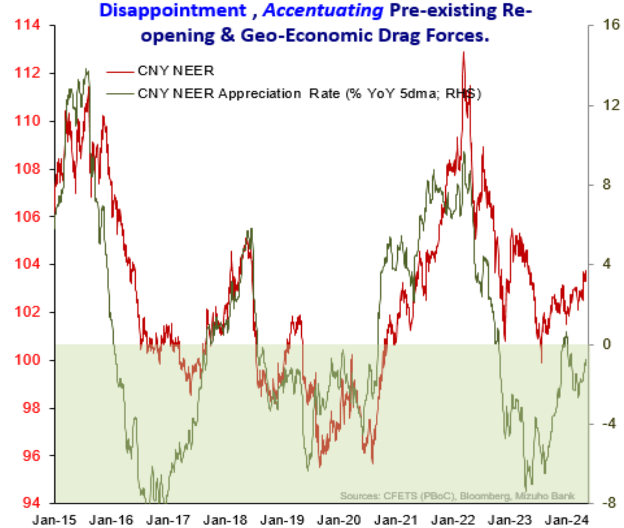
CNY NEER Traction is Undermined by Lingering US-China Risks amid "Unforced" Policy Stumbles. USD trend is instead dictating relative CNY shifts! (Index end-2014=100)

Drop in CNY NEER (& Sharper collapse in CNH) reflects Macro, Re-opening & Geo-Economic Vunerabilities Accentuated via China's Financial Conduits

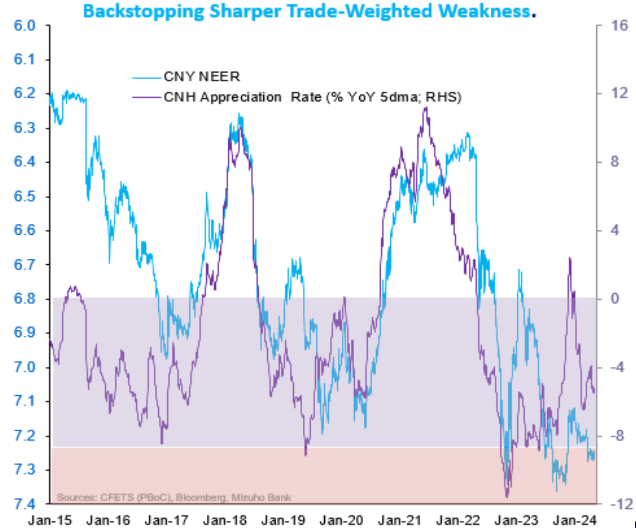
(CNY NEER Index end-2014=100)



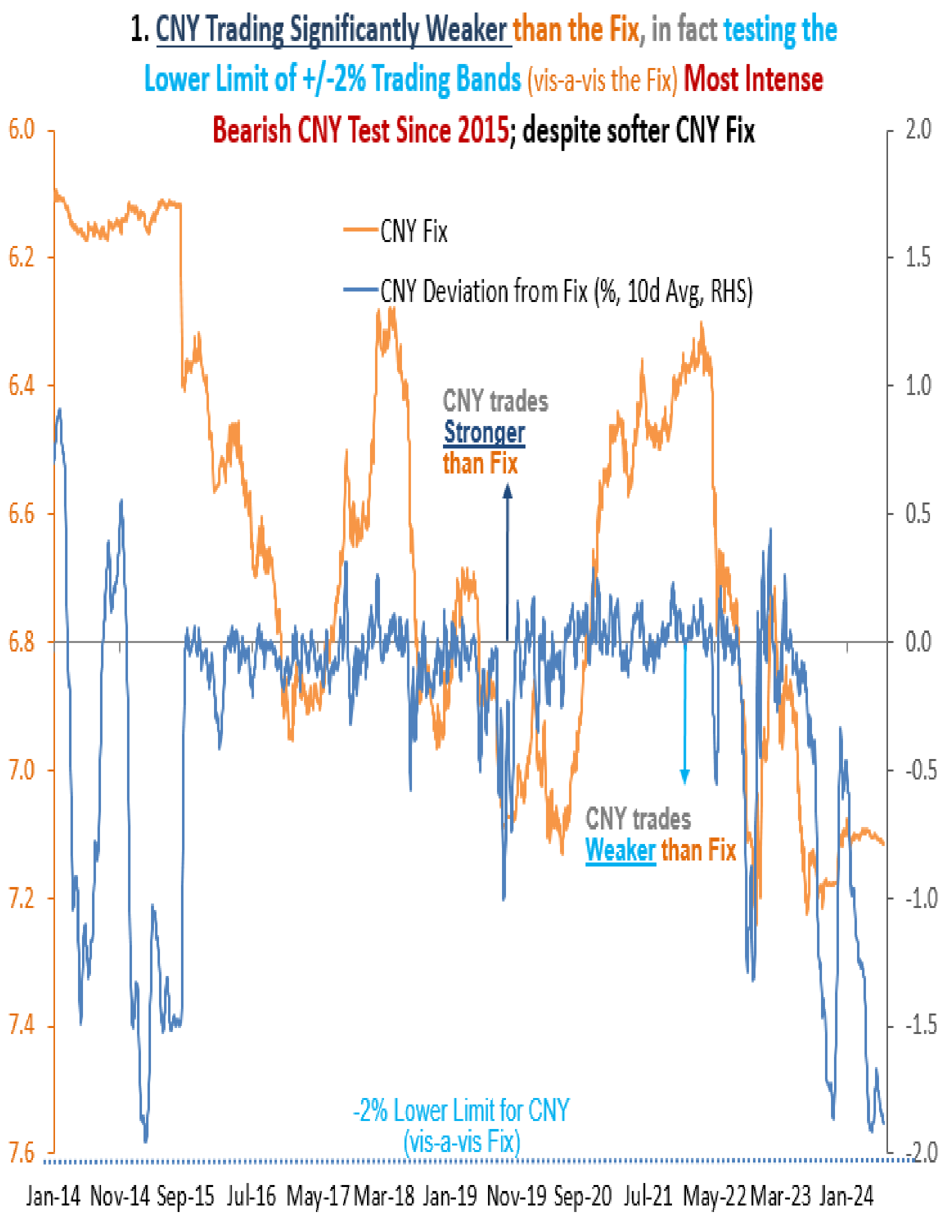
Sharp CNY NEER Depreciation Reflects Economic Disappointment , *Accentuating* Pre-existing Re-opening & Geo-Economic Drag Forces.

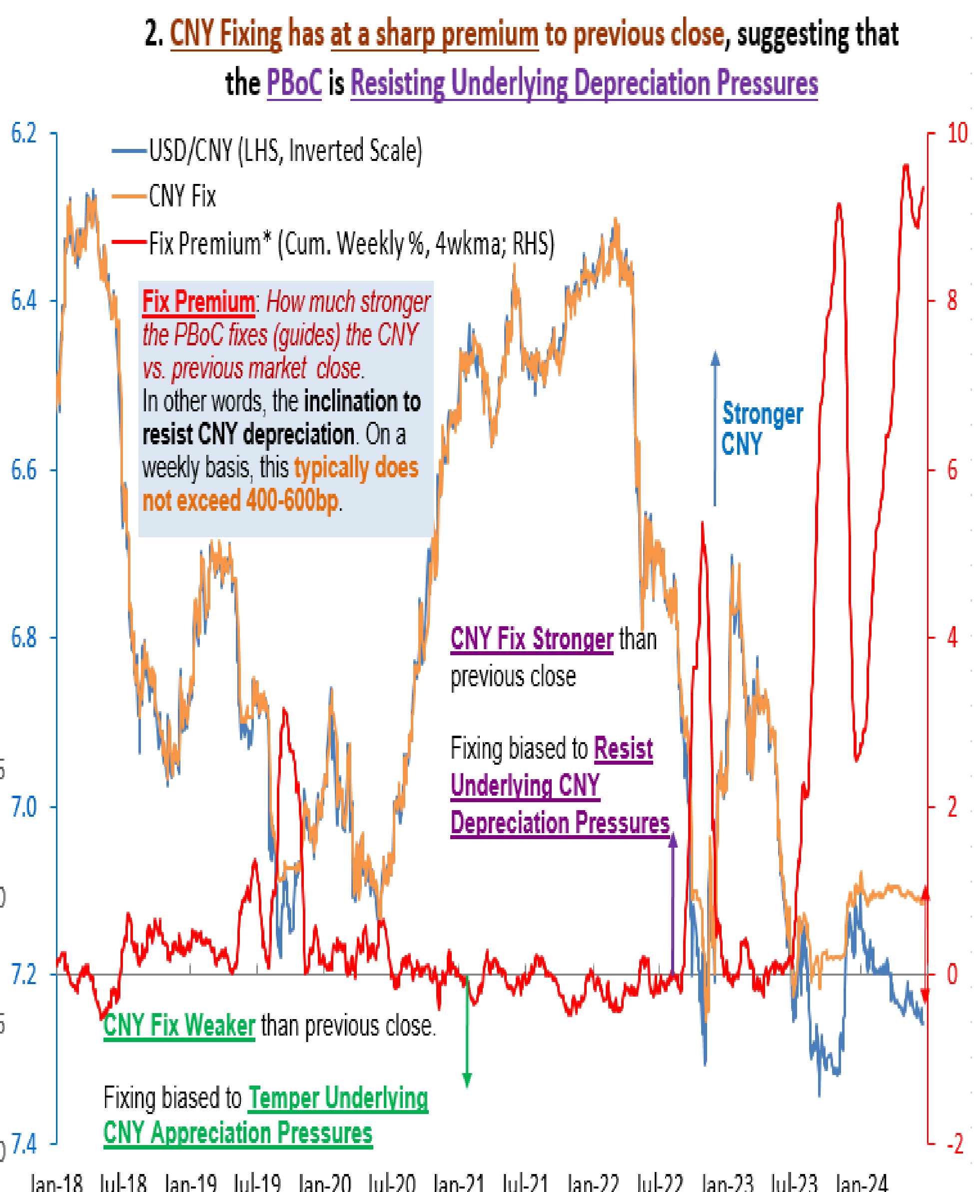


CNH Depreciation Validates PBoC Intervention; Backstopping Sharper Trade-Weighted Weakness.

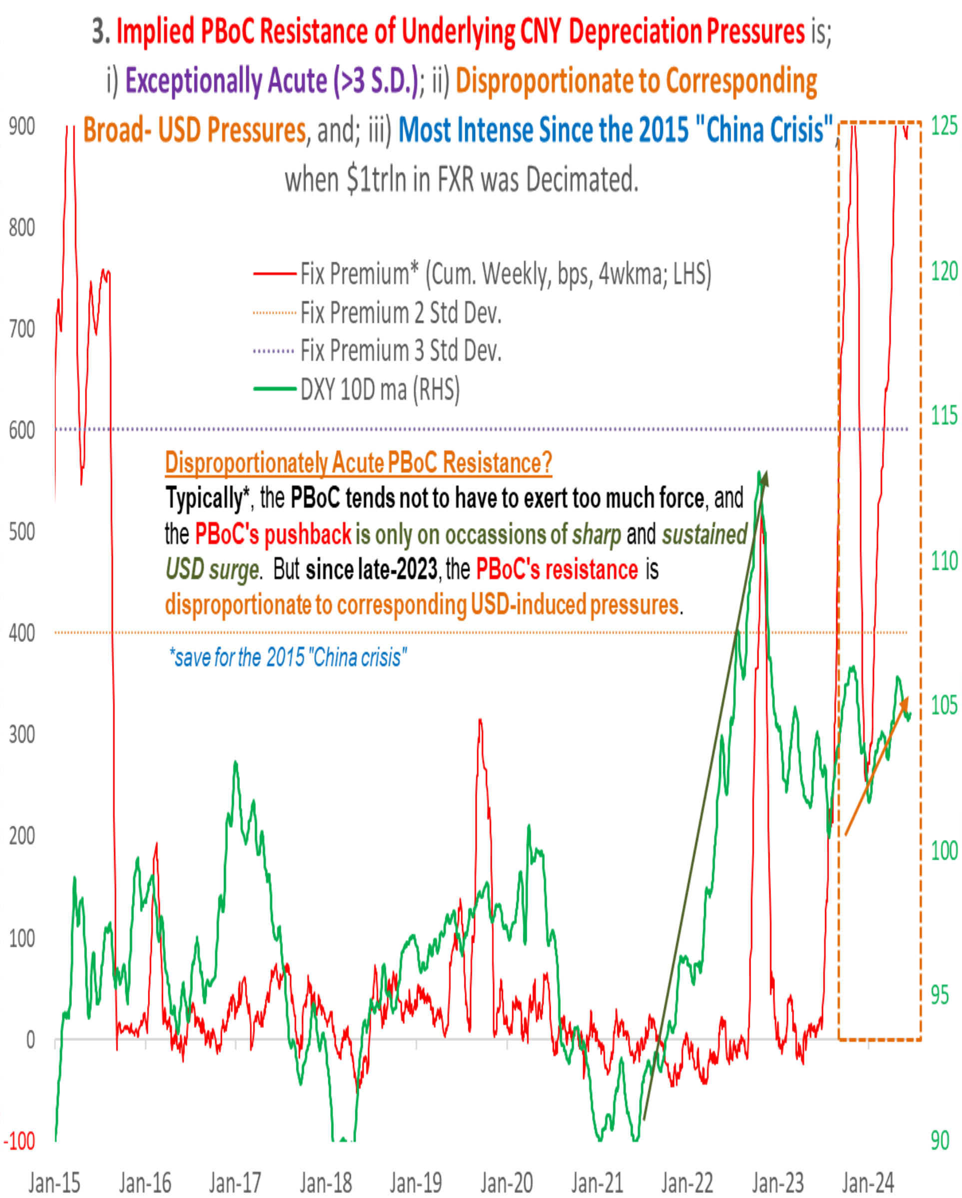


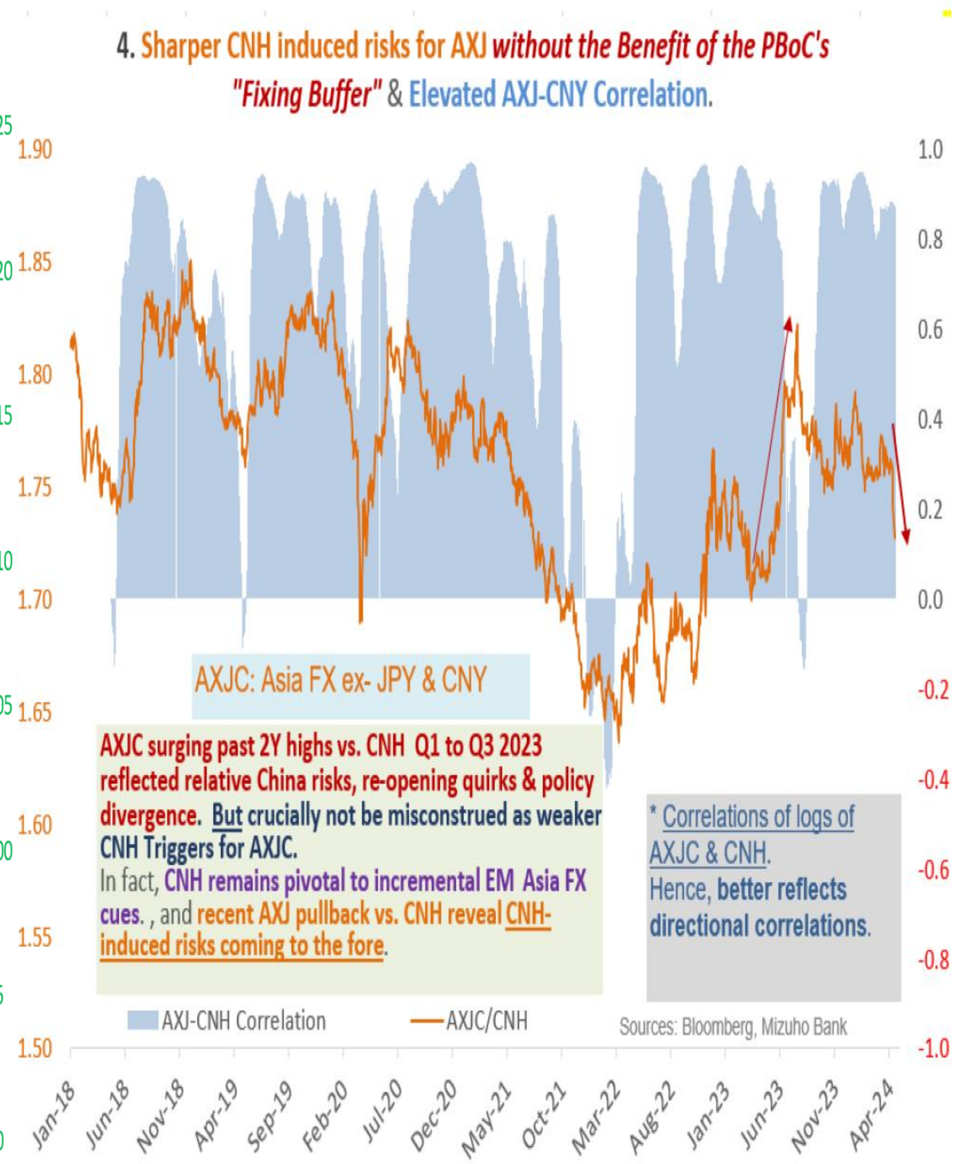
5b China Factor: PBoC Pressures – *Respect, Not Trust*





5b. China Factor: Disproportionate Pressures a Reflection of China-specific Risk (Spill-over)





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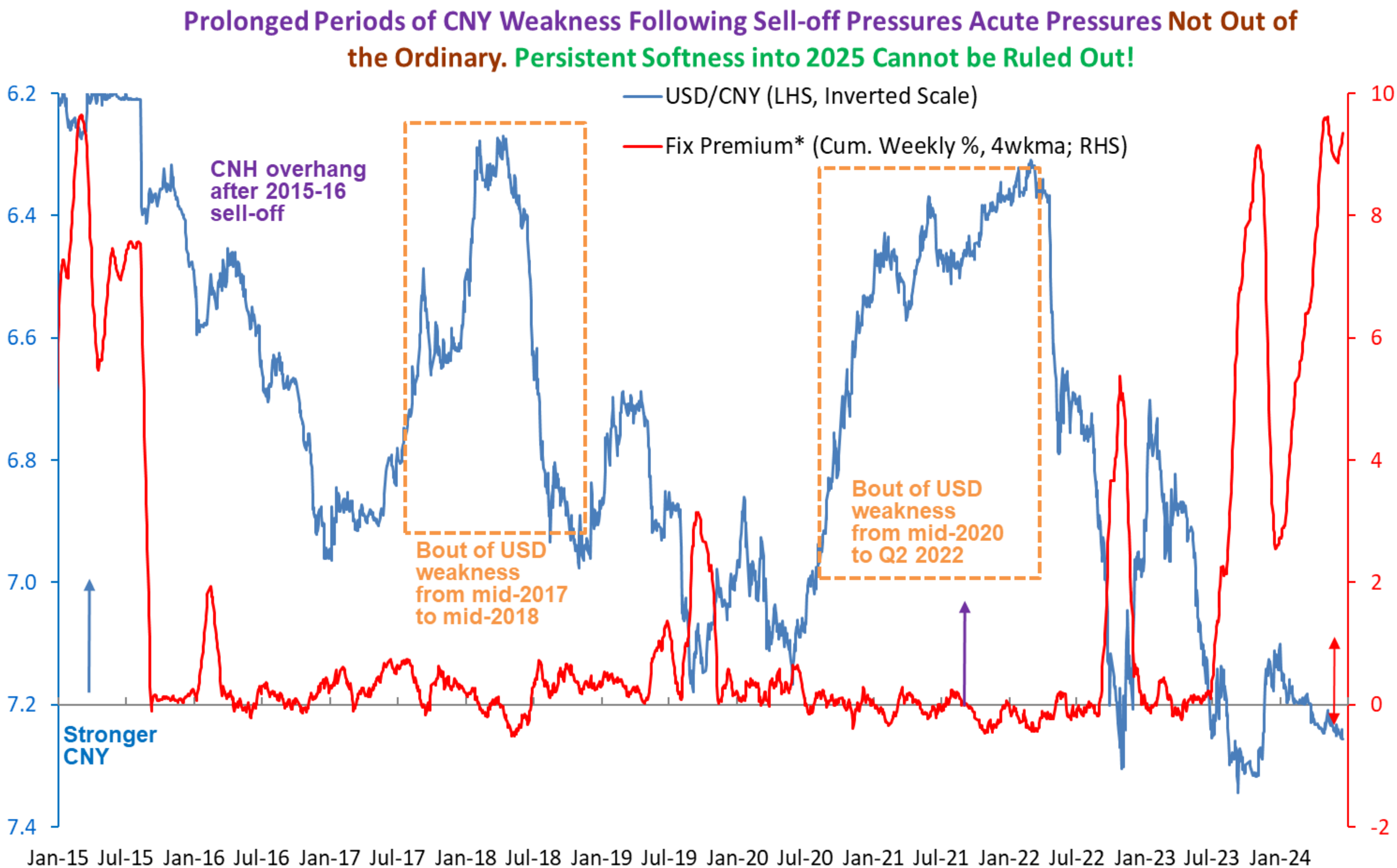
5c. China Factor: Disproportionate Pressures a Reflection of China-specific Risk (Spill-over)



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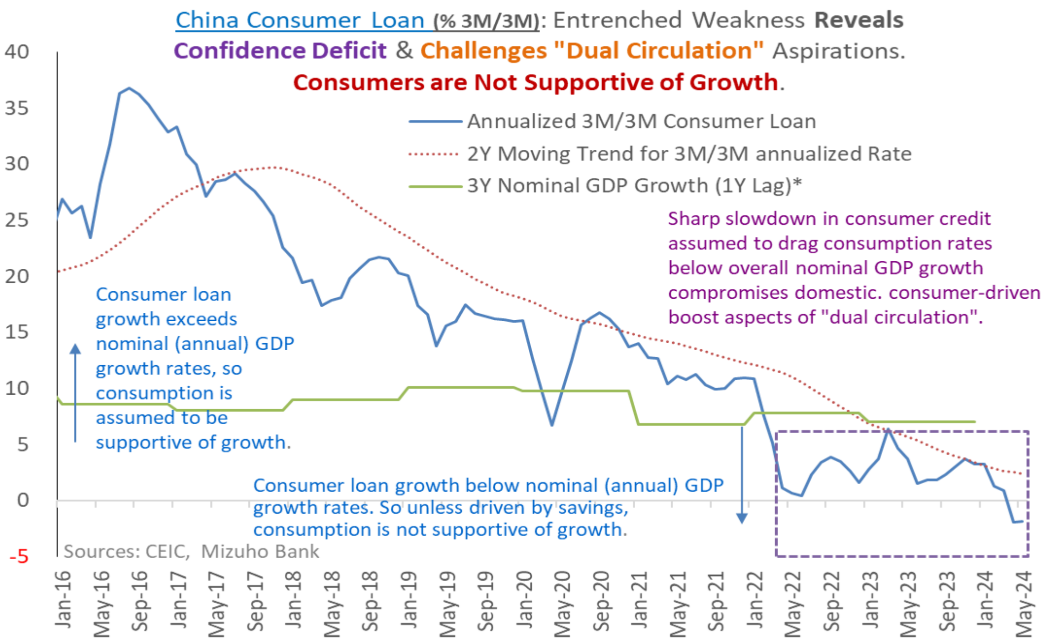
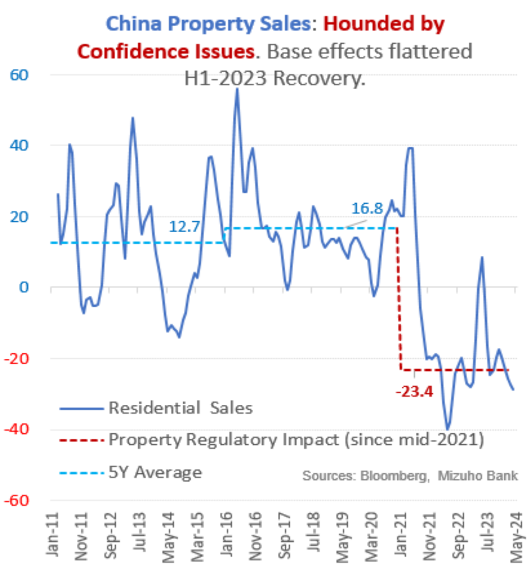
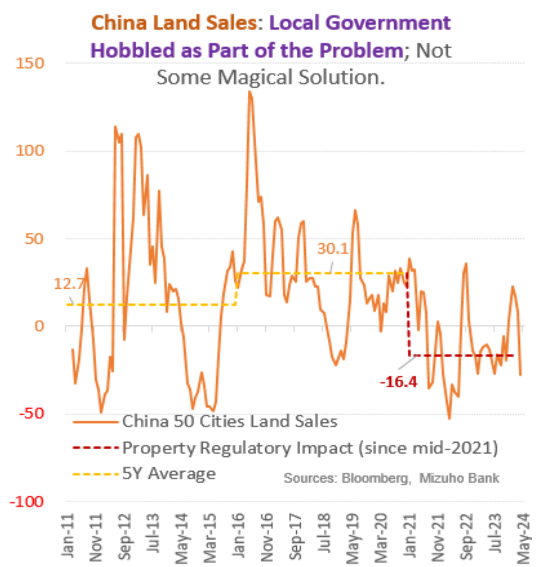
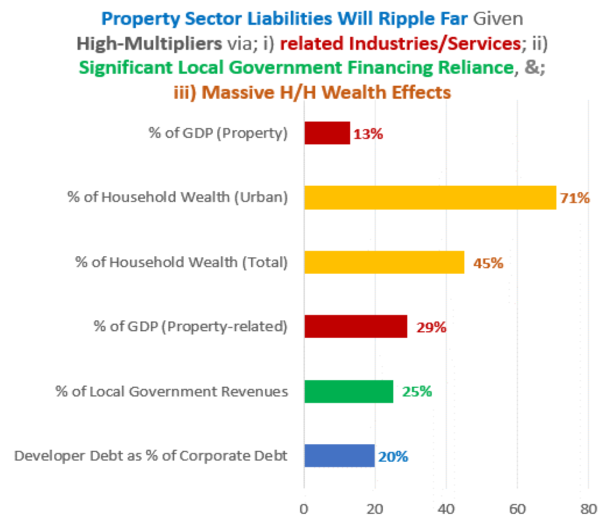
Appendix: China Consumer Confidence Impaired









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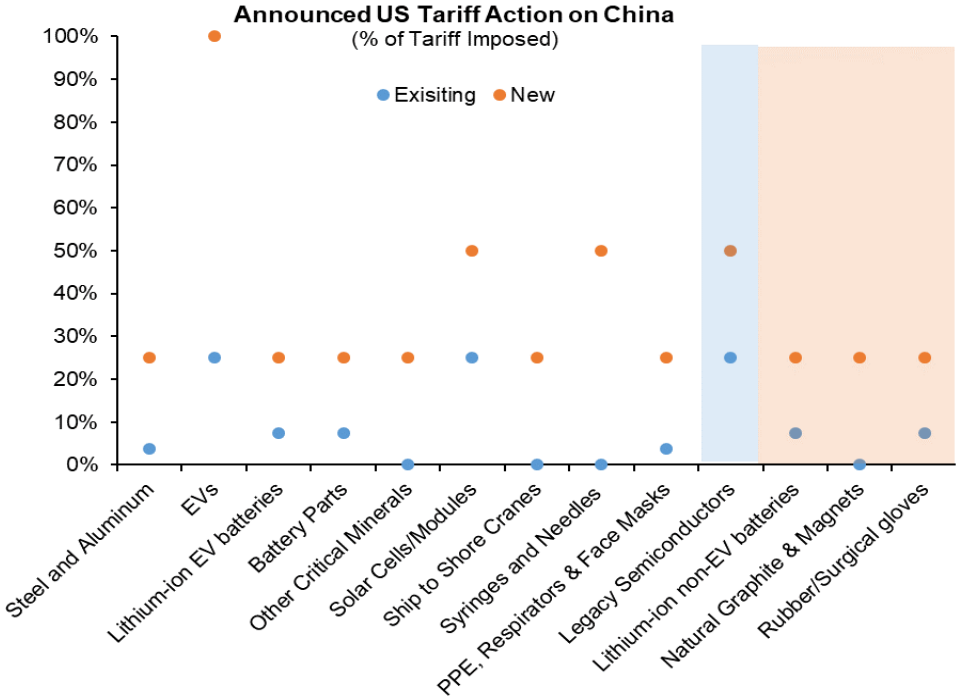
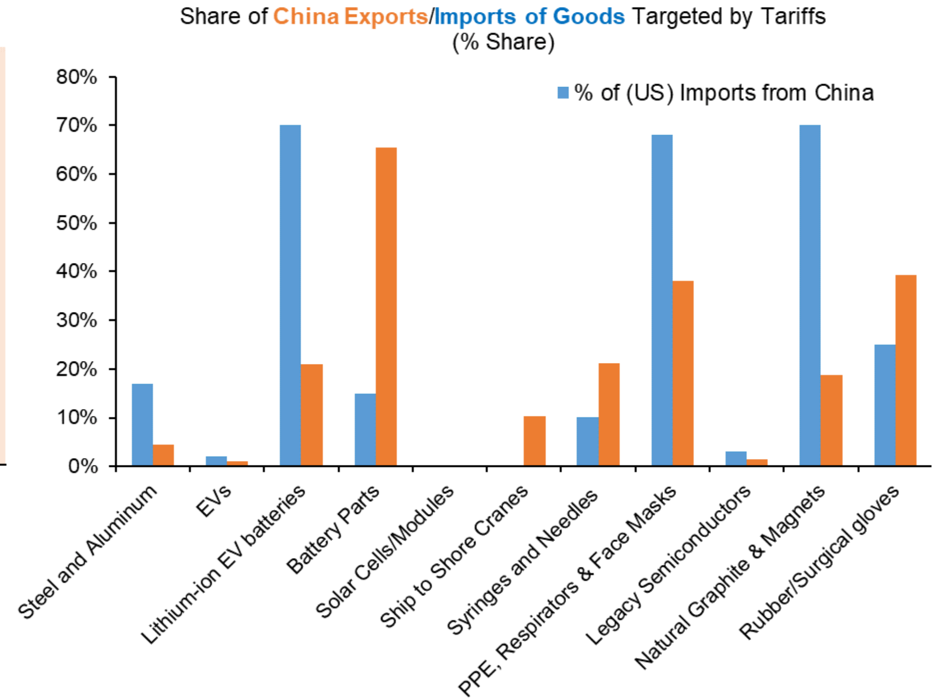
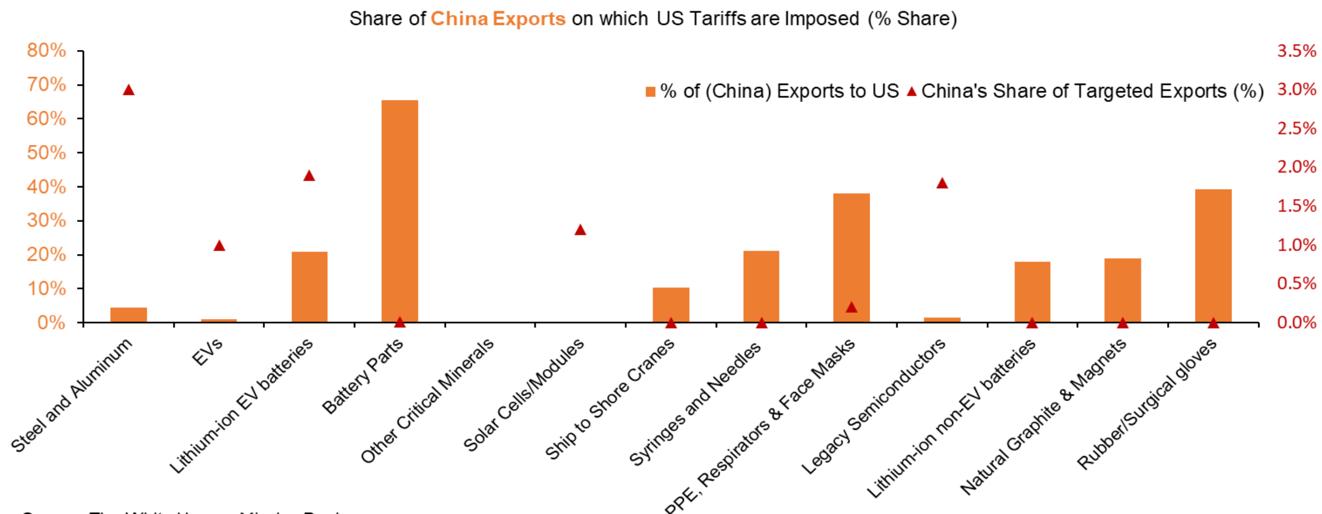
Appendix: Geo-Political Flares to Watch



Source: The White House; Mizuho Bank



Source: The White House; Mizuho Bank



Source: The White House; Mizuho Bank

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Appendix-Geo-Politics: Conflict, Production & Passage

Straits of Hormuz:

Conflict risks

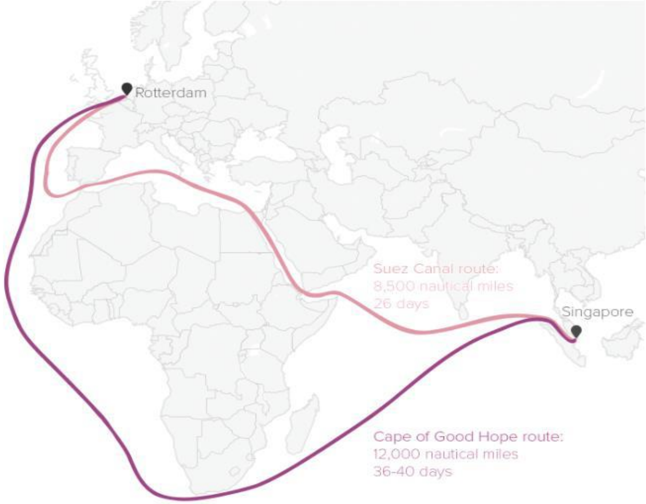
Most critical Oil choke point – Iran risk

20-22MBpD of Oil (~$1.2b worth)

Most of Saudi's Oil passage

~20-25% od seaborne Oil Passage

➔ as Large as a Doubling in Prices!



Red Sea:

Conflict risks - Houthi Rebels

Could disrupt passage of Oil

~12% of global shipping (~$1trln)

CoGH detour adds 3-4 weeks to Asia routes

➔ approximated to be 20% of shipping capacity impact

Panama Canal:

Water Crisis

(Non Conflict Risk)

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Mizuho Asia Treasury Seminar

Private and confidential

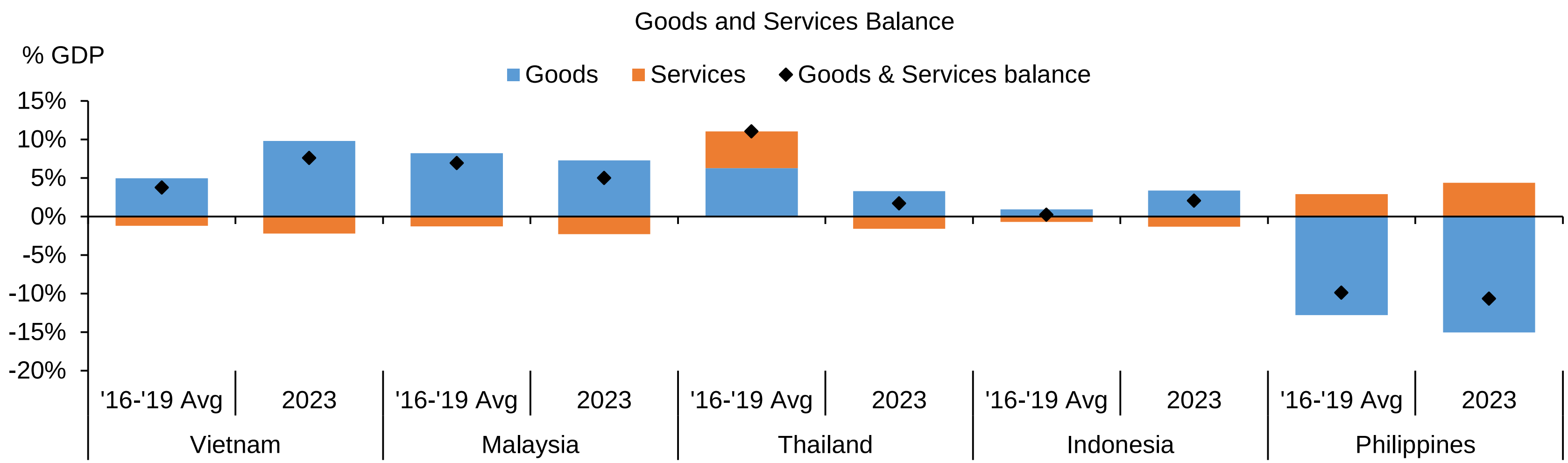
Photo Credits: Vector Stock

June 2024

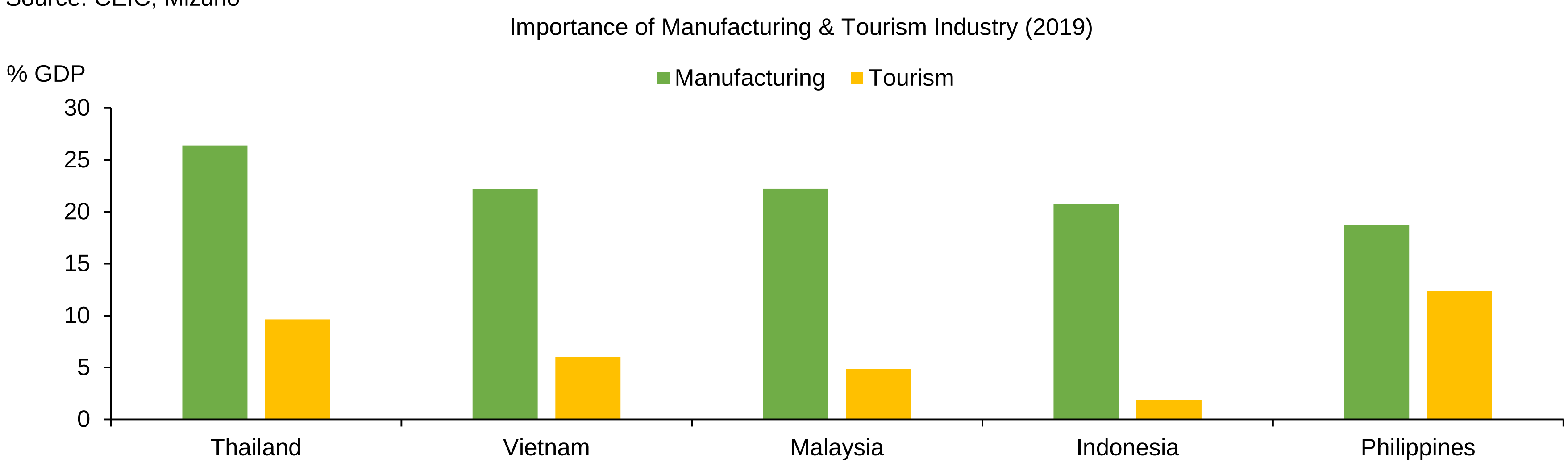
Outline

- ASEAN Focus: Re-examining How ASEAN Stocks Up Goods-Services Cycle – Between Exhaustion & Exploitation
  - The Goods Upturn: Semi-Conductors the Bellwether for Exploiting a More Distinct and Defined Upturn?
  - The Tourism Boost: Hitting Exhaustion with the Low-Hanging Big Gains?
  - How ASEAN's Fiscal Shifts Impact

Goods & Services Balance: Past vs Present

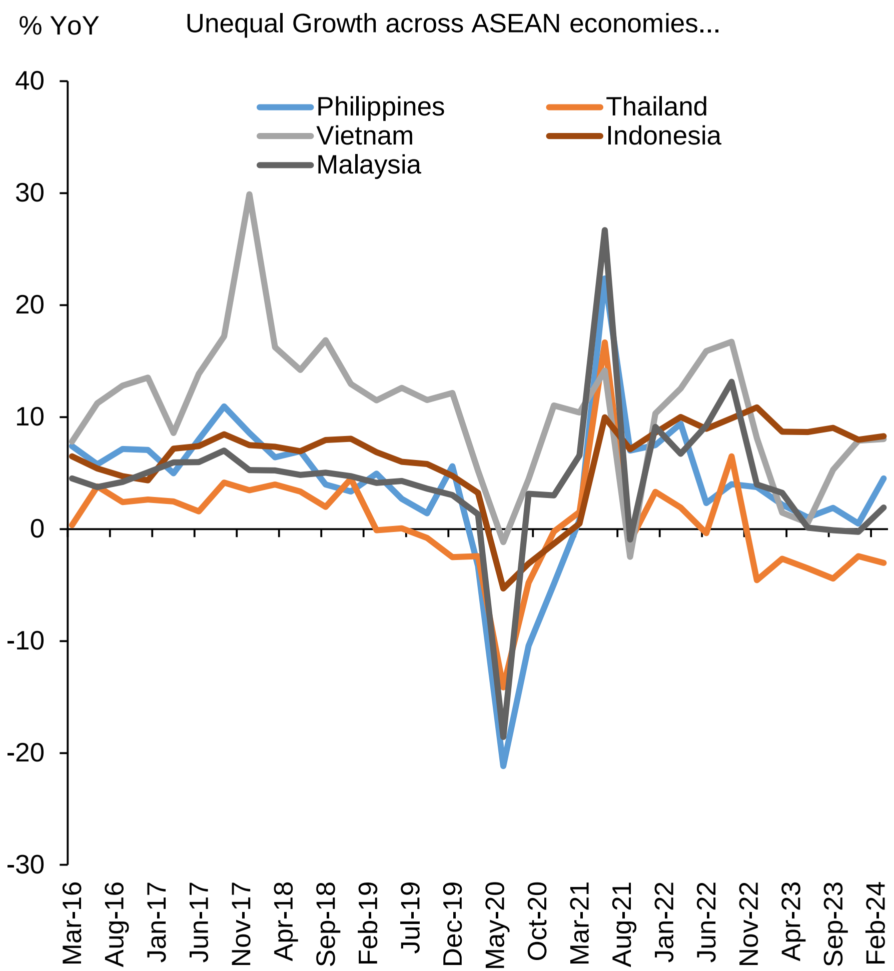


Source: CEIC; Mizuho

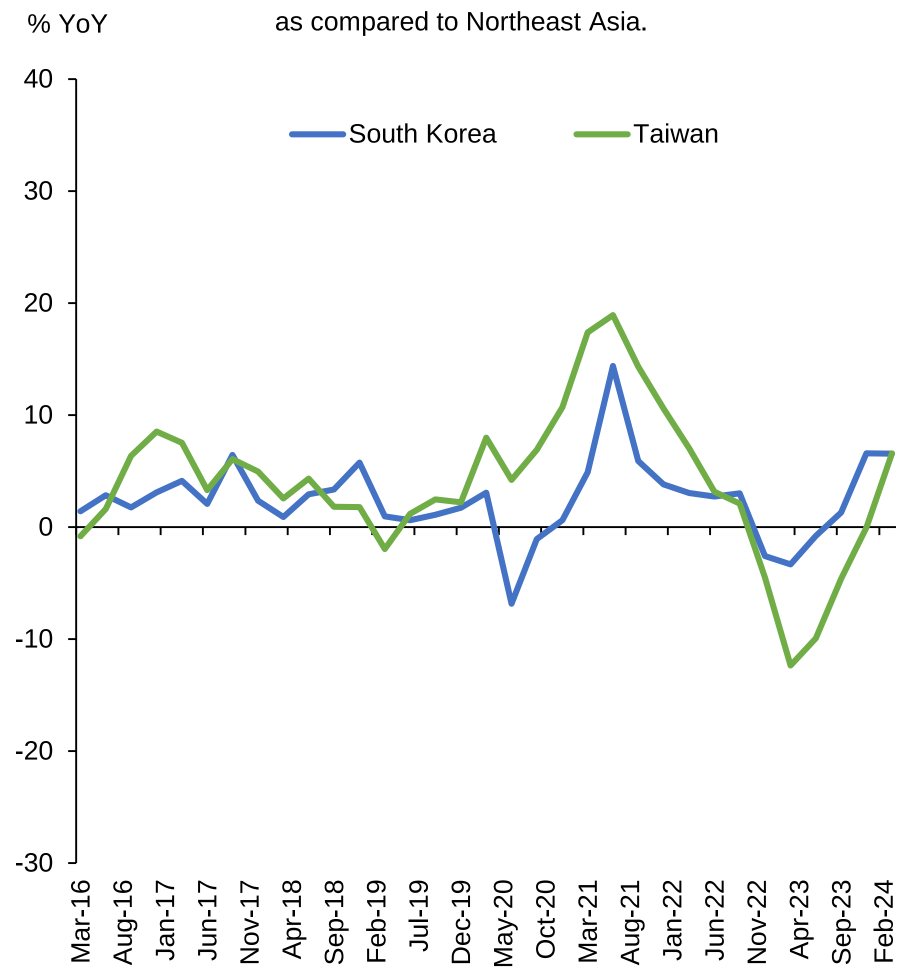


Source: CEIC; World Bank; Mizuho

Goods – Broadbased or Peculiar Drivers?



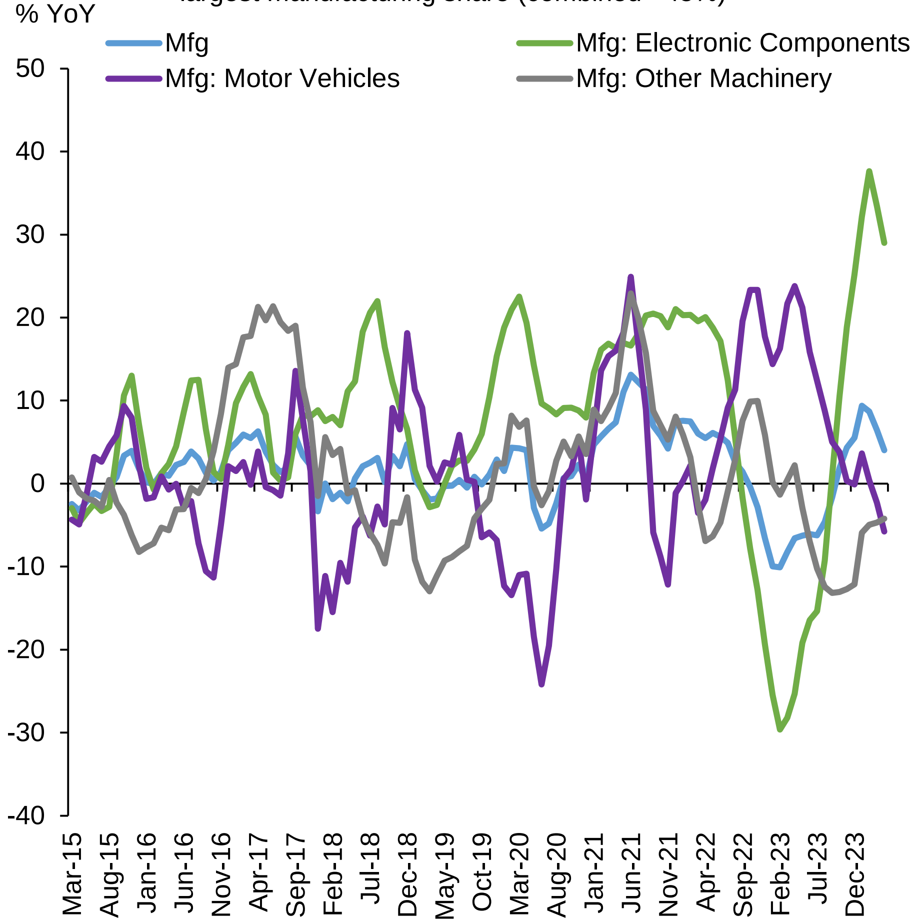
Source: CEIC; Mizuho



Source: CEIC; Mizuho

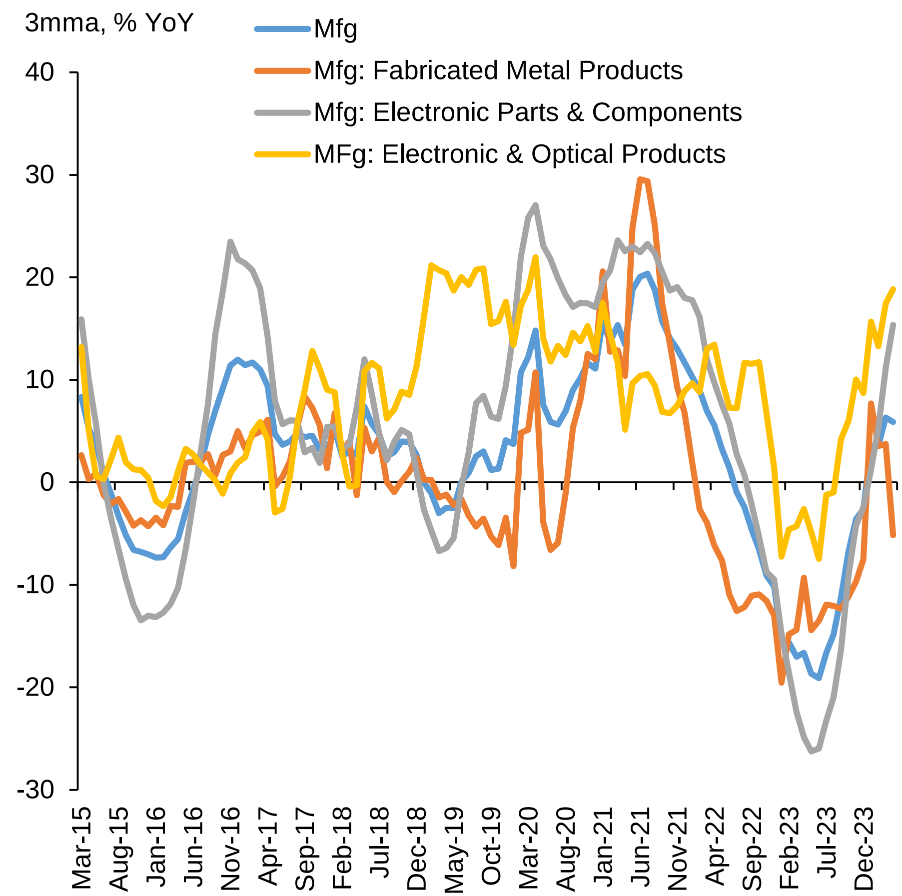
Goods – Composition of South Korea and Taiwan's Manufacturing Industry

South Korea: Industrial Production of top 3 products with largest manufacturing share (combined ~45%)



Source: CEIC; Mizuho

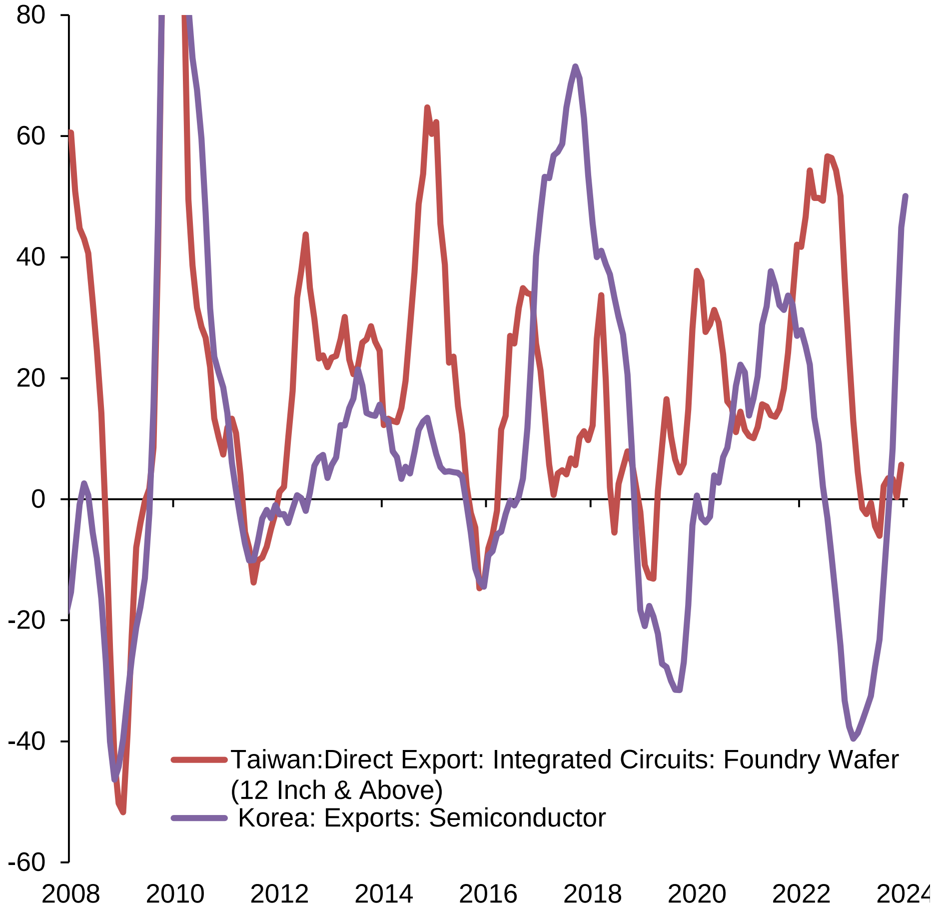
Taiwan: Industrial Production of top 3 product groups with largest manufacturing share (combined ~62%)



Source: CEIC; Mizuho

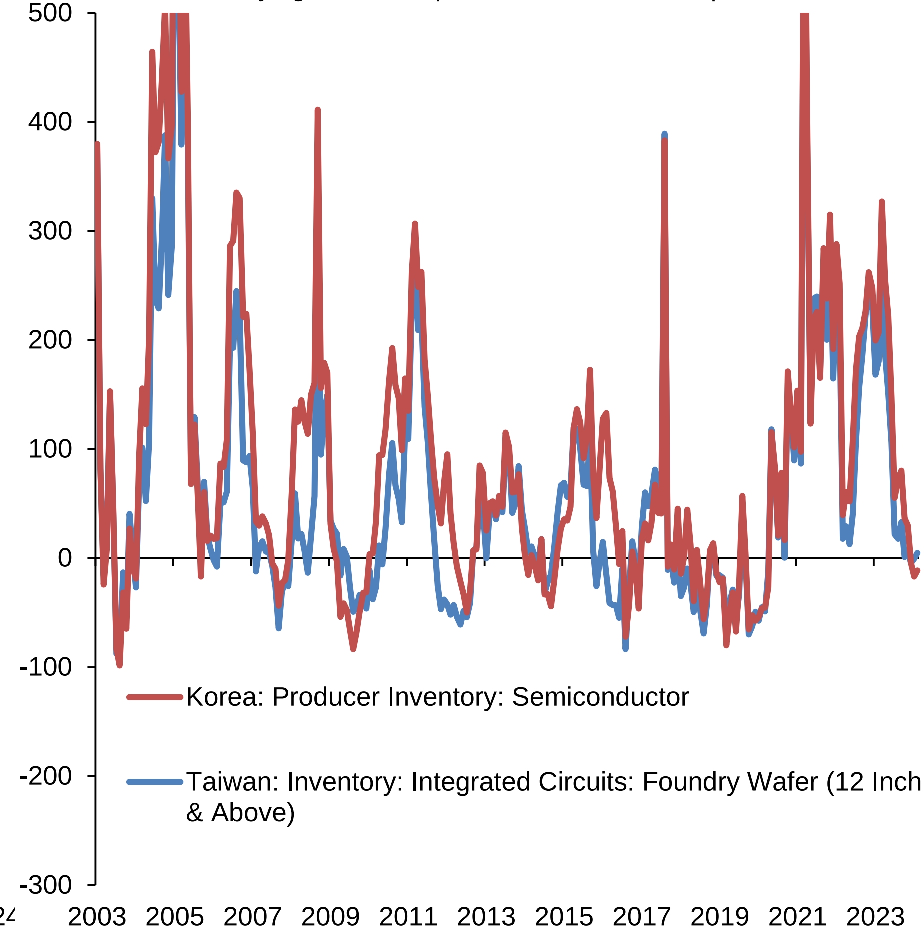
Goods – Drivers of Semiconductor Growth

Semiconductor Exports (% YoY 3mma): Taiwan and Korea trade data point to semiconductor led recovery.



Source: CEIC; Mizuho

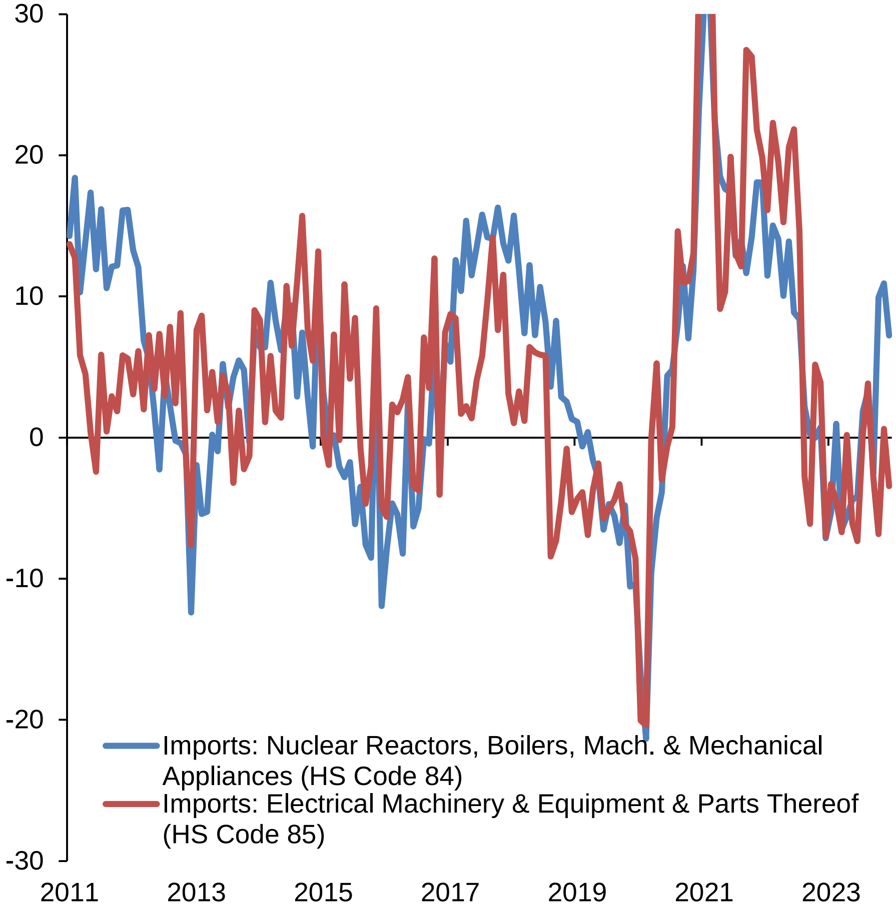
Inventory Growth (%YoY): Inventory rundown also aids underlying need to replenish amid demand uptick.



Source: CEIC; Mizuho

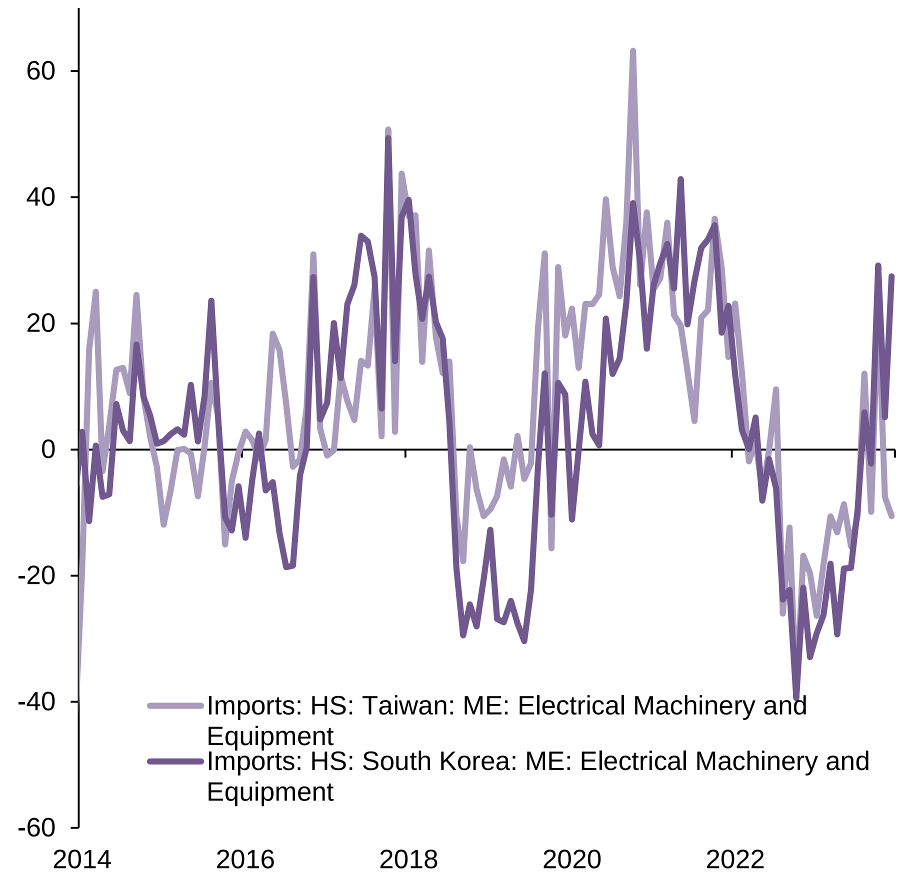
Goods – External Drivers

US Imports (% YoY): US imports of computers have surged while imports of semiconductors remain weak.



Source: CEIC; Mizuho

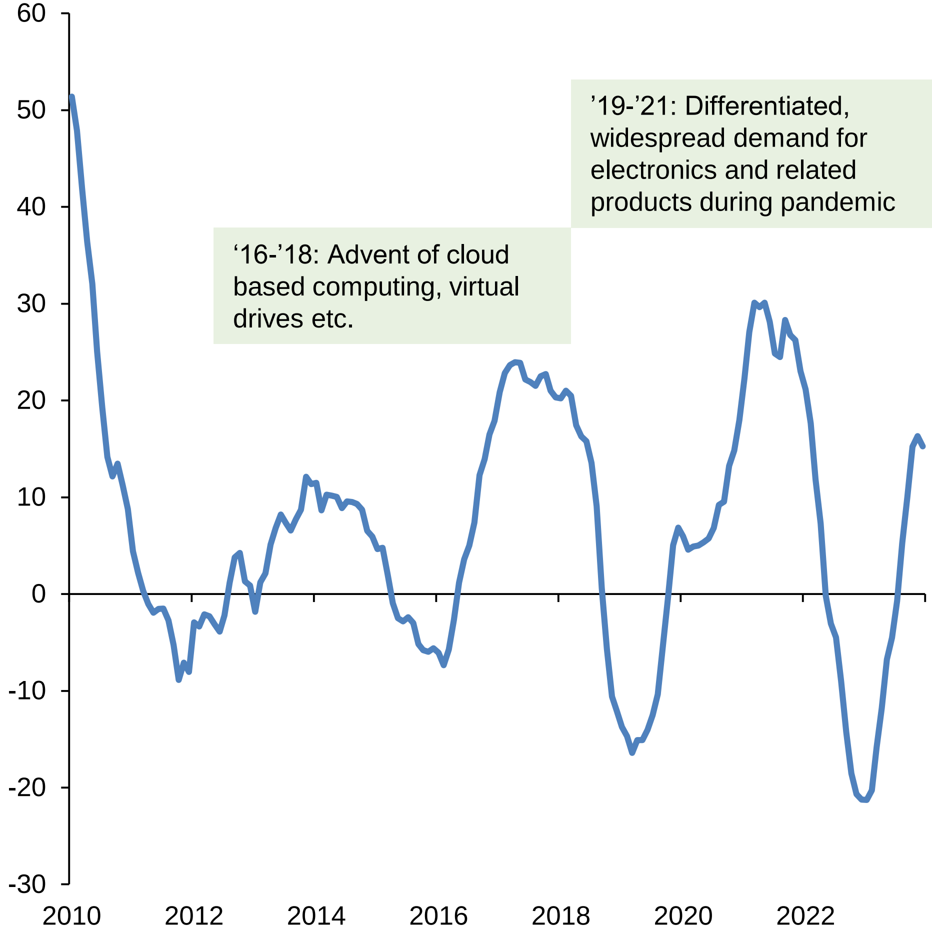
China's Imports Growth (% YoY): China's semiconductor imports from Taiwan and South Korea have often in tandem. and likely drove the recent turnaround.



Source: CEIC; Mizuho

Goods – Strength of Recovery

Semiconductor Shipments Worldwide (3mma, % YoY):



Source: CEIC; Mizuho

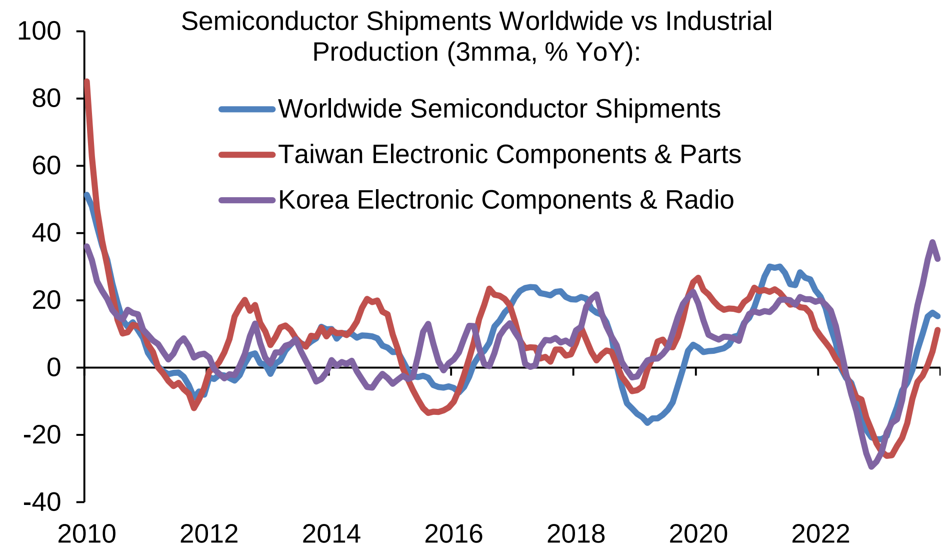
Net Exports of Electrical Machinery & Equipment (as % of Exports)

Source: UNComtrade (2021); Mizuho

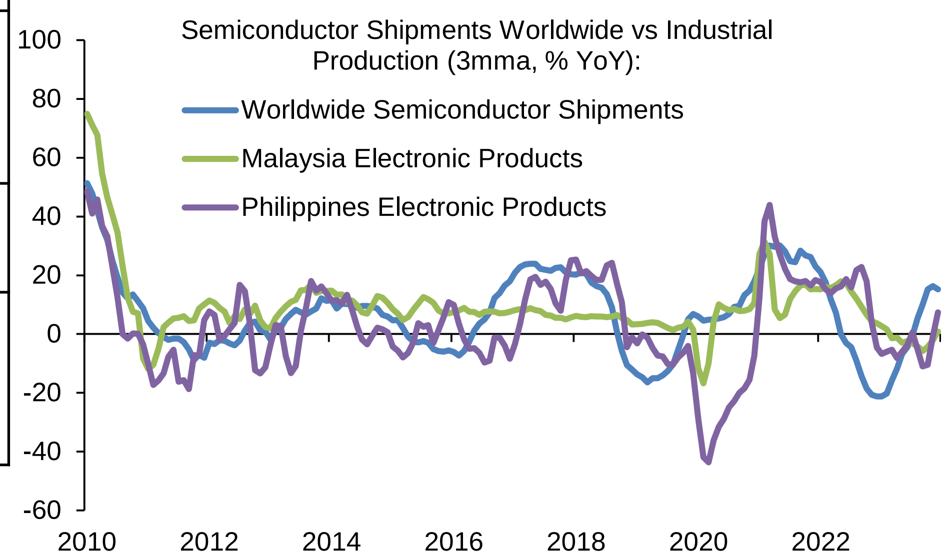
Goods –Spillovers to ASEAN

	Top Electrical machinery and Equipment Exports
Malaysia	• Electronic integrated circuits (5.6%) • Disc, tapes, solid-state devices (1.8%) • Diodes, transistors, similar semiconductor devices (1.4%)
Philippines	• Electronic integrated circuits (11.6%) • Insulated wire, cable etc. (1.7%) • Electric transformers, static converters (1.1%)
Vietnam	• Telephone sets (14.4%) • Monitors and projectors (1.3%) • Transmission apparatus (1.1%)
Thailand	• Transmission apparatus (0.4%) • Electric transformers, static converts (0.3%)
	<u>Others</u> • Vehicles, other than rail (8.0%) • Rubber and articles thereof (6.1%) • Nuclear reactors, boilers etc. (5.5%)
Indonesia	• Monitors and projectors (0.6%) • Insulated wire, cable (0.2%)
	<u>Others</u> • Animal or vegetable fats (14.0%) • Mineral fuels, mineral oils (7.0%) • Iron and steel (3.9%)

Source: UNComtrade (2021), Mizuho

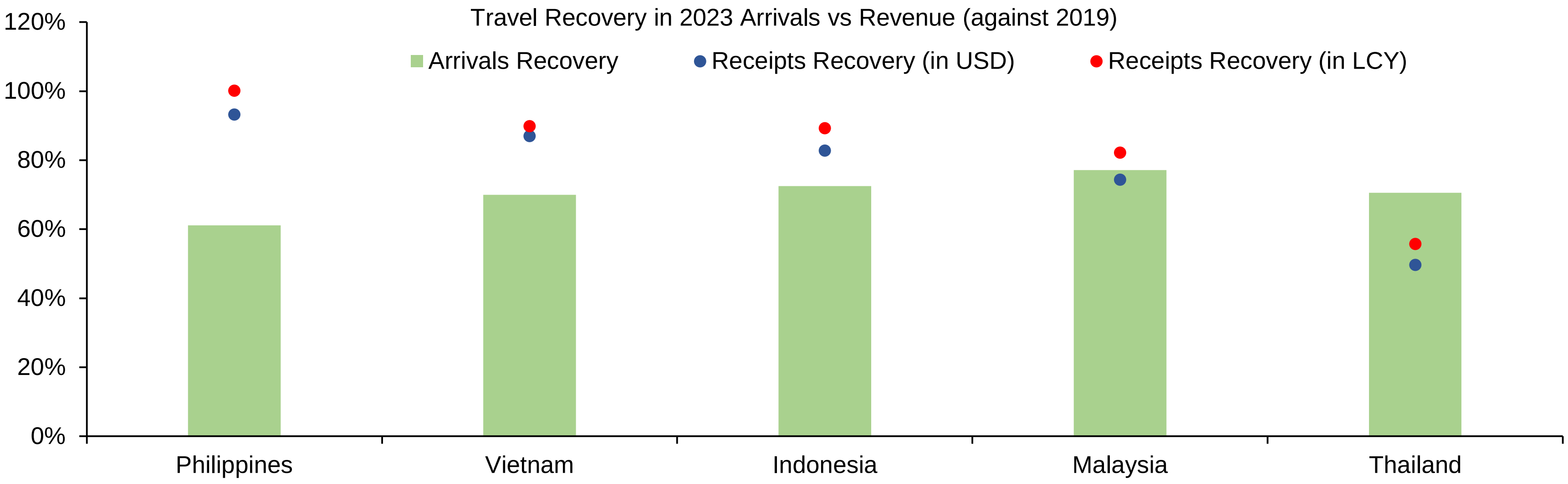


Source: CEIC; Mizuho

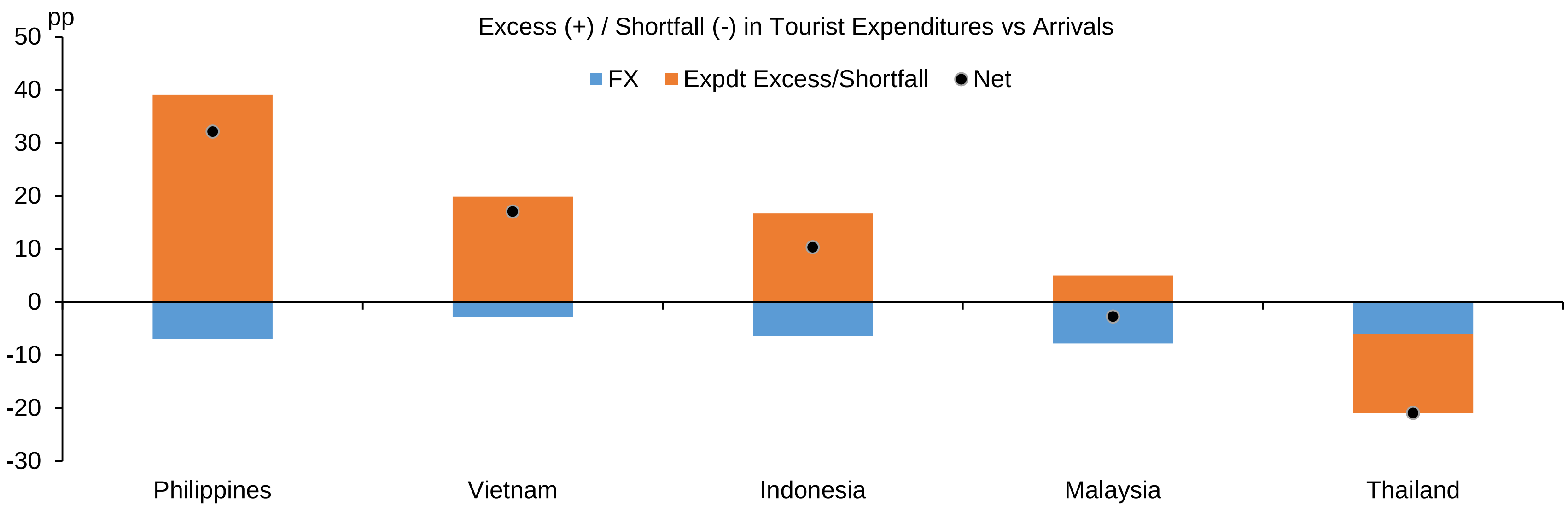


Source: CEIC; Mizuho

The Tourism Boost: People vs Dollars



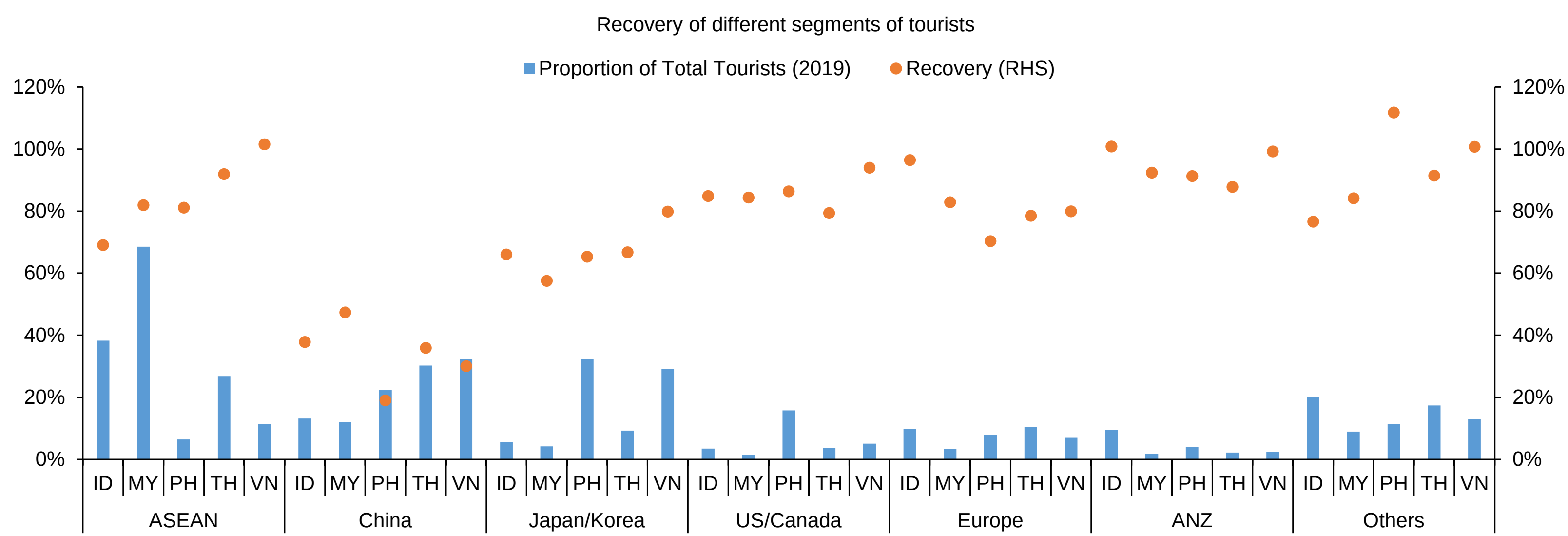
Source: CEIC; Mizuho



Source: CEIC; Mizuho

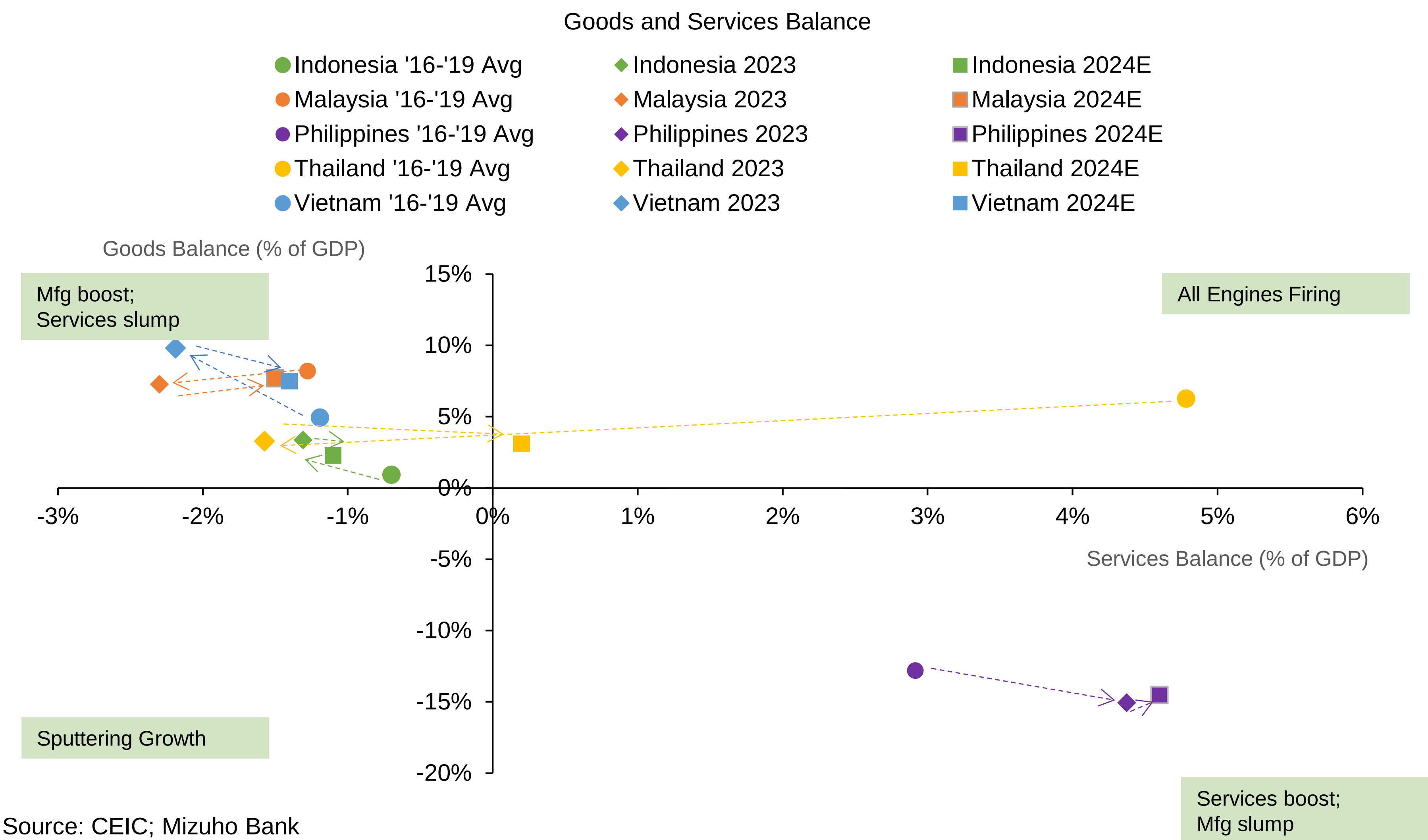
Tourism: The Last-Mile Tourist Dollar

	Where are the Tourists?
Thailand	• Lagging in recovery of higher spending **Chinese tourists** could mean more catch-up in coming quarters amid a permanent visa-free travel from March 2024. Visa free travel from India starting June.
Malaysia	• Surge in day tourists from neighboring countries on weaker MYR could have inflate arrivals recovery but less impact on revenue recovery could mean more scope for further recovery. • Scope for outperformance on recovery in **Chinese tourists** is much more limited.
Philippines	• Indications that efforts to attract **Middle East tourists** are paying off. Albeit constituting a small proportion, could boost tourism dollars. • But stringent visa requirements could mean **Chinese tourists** recovery will be lackluster.
Indonesia	• Tourism recovery still supportive, but no notable indications for outperformance.
Vietnam	• Stellar performance in 2023 on the back of early launch of visa exemption program in August 2023 • Better performance in 2023 could mean moderating growth in 2024.



Source: CEIC; Mizuho

Goods & Services Balance: Past vs Present



Source: CEIC; Mizuho Bank

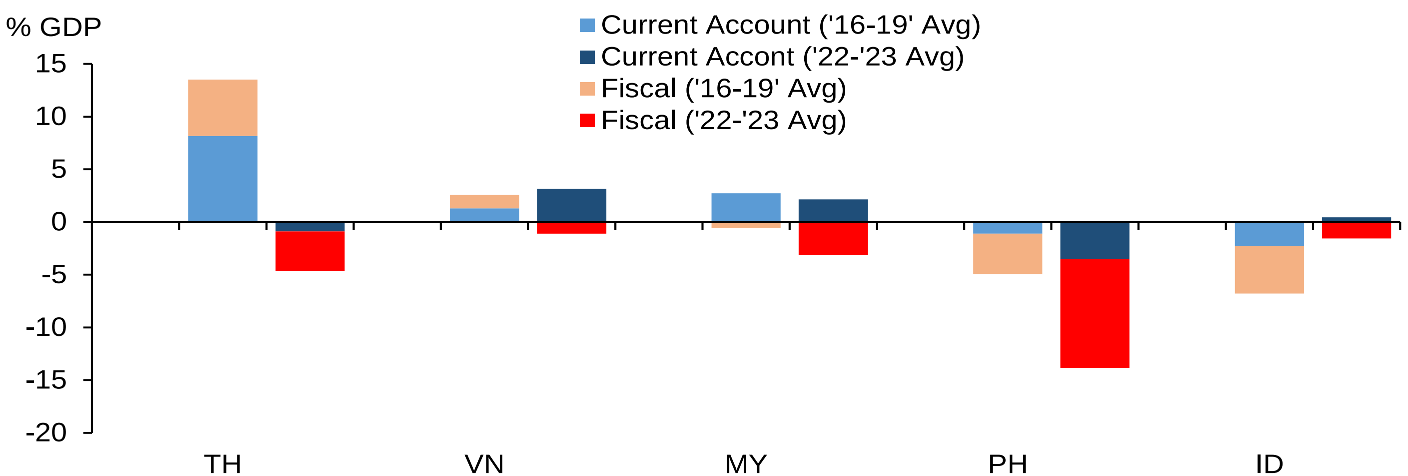
The Fiscal Situation

Historical Budget Deficits (as % of GDP) and Fiscal Trajectory

	'16-'19 Avg	2022	2023	2024E	Fiscal Trajectory
ID	2.3%	2.4%	1.7%	2.8%	Expected to be maintained within 3% of GDP ceiling.
MY	3.3%	5.6%	5.0%	4.3%	Target at 3.5% of GDP for 2024-2026 under Medium Term Fiscal Framework
PH	2.7%	7.3%	6.2%	5.6%	Target to reach 3.7% of GDP by 2028.
TH	2.8%	3.5%	3.3%	3.6%	2025 budget deficit widen to 4.4% on digital wallet plans.
VN	2.9%	4.4%	4.1%	3.6%	2021-2025 National Financial Plan targets fiscal deficit at 3.7% of GDP.

Source: CEIC: National Authorities: Mizuho

Current Account and Fiscal Positions

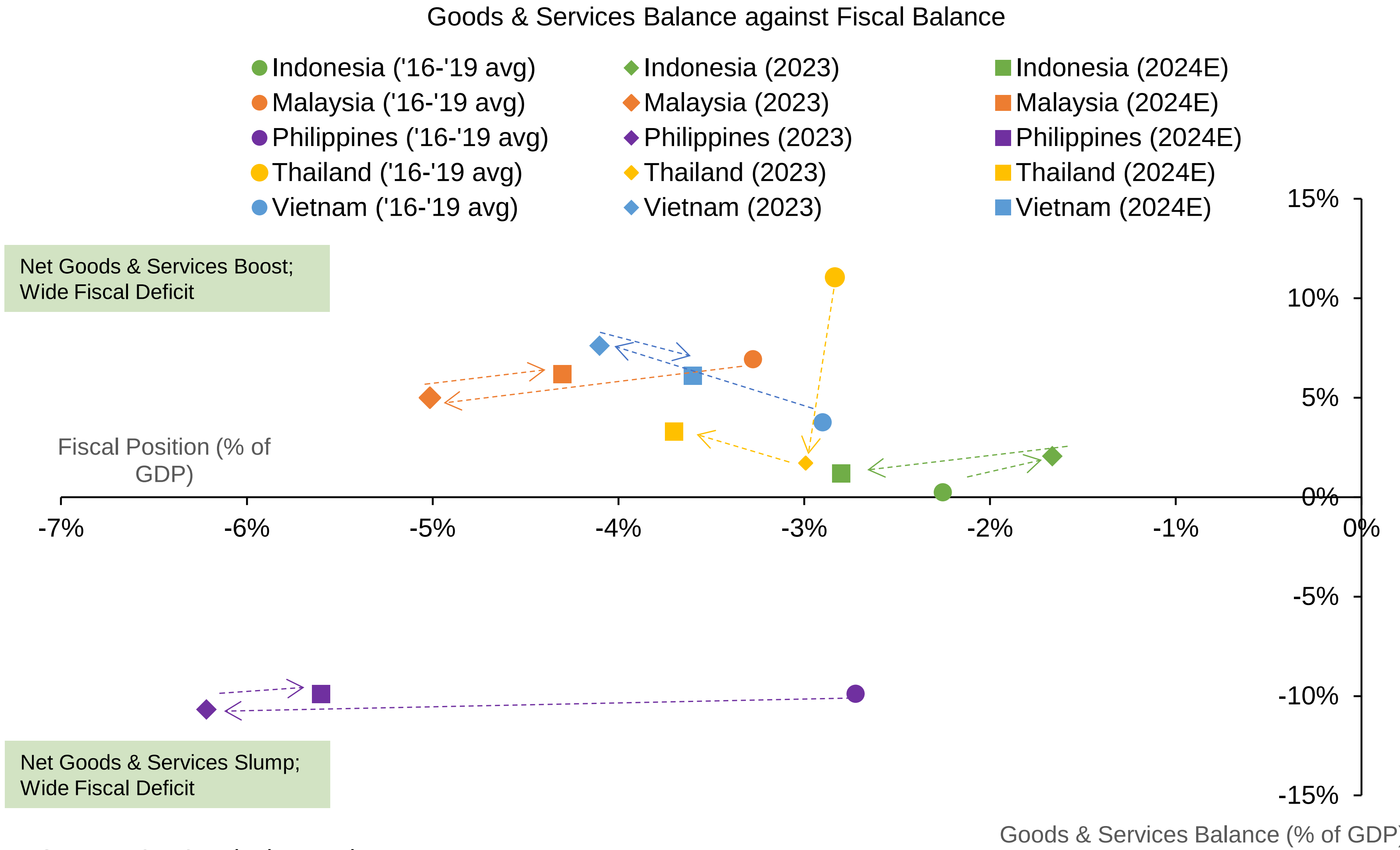


Source: CEIC; Mizuho

Fiscal Standing Assessment

	Notable Revenue Measures	Notable Expenditure Measures	Assessment
Malaysia	• Introduction of capital gains tax • Increase in services tax (eff 1 Mar 2024)	• Reduction in diesel subsidies (eff 10 Jun 2024)	• Concrete actions undertaken thus far provide confidence on government's commitment towards fiscal sustainability.
Vietnam	• Extended VAT rate cut ((from 10% to 8% introduced in early 2022) from Jul 2023 to Jun 2024, after a brief rate reversal in early 2023.	• Public investments likely to continue to struggle to hit targets, though land law reforms should aid better disbursements	• Continued VAT rate cut extension likely but no imminent fiscal worries. Risks remain on ensuring financial sector stability.
Philippines	• Many tax reforms pending, including Digital Services Tax Bill, Mining Fiscal Regime	• Continuation of current programmes, target 5-6% of GDP yearly on infrastructure. • National government's spending performance for 2023 surpassed target by 2.1%.	• Slow-to-consolidate fiscal deficits amid slow progress on revenue measures.
Indonesia	• Scrap VAT of 11% on home purchases worth less than IDR2bn until Jun 2024, after which it will be halved for an unspecified time.	• Free lunch programs and other welfare measures (likely rolled out end 2024/2025) expected to cost IDR460tn, more than the entire 2023 budget deficit.	• Albeit still within 3% GDP ceiling, higher fiscal expenditures on campaign pledges cast an overhang; uncertainty over debt outlook incites worries.
Thailand	• VAT reduction from 10% to 7% (from Covid) extended till Sep 2024.	• Digital wallet plans expected to cost THB500bn (~3% of GDP).	• 2025 budget deficit widen to 4.4% on digital wallet plans. • Public debt path may come dangerously close to legal ceiling in the next 2-3 years.

External and Fiscal



Source: CEIC; Mizuho Bank

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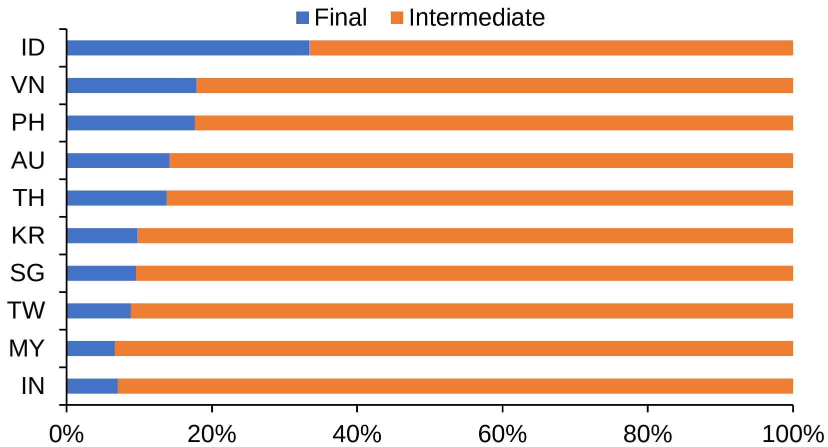
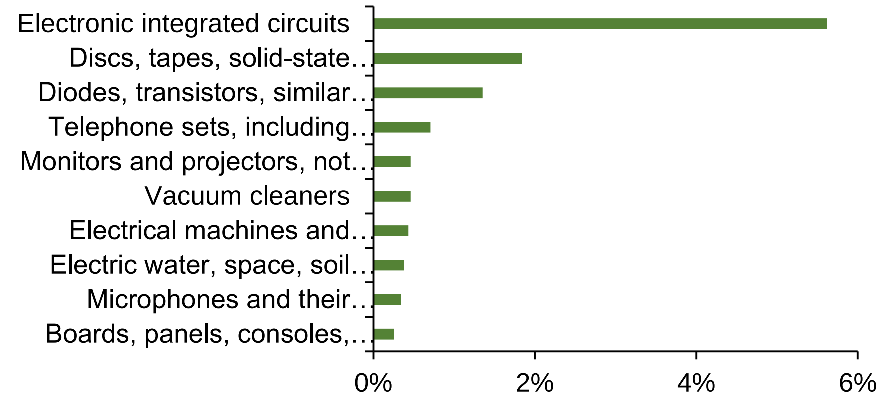
Appendix: Ascertaining Spillovers from Value-Chain positioning

Share of intermediate vs final electrical and optical production



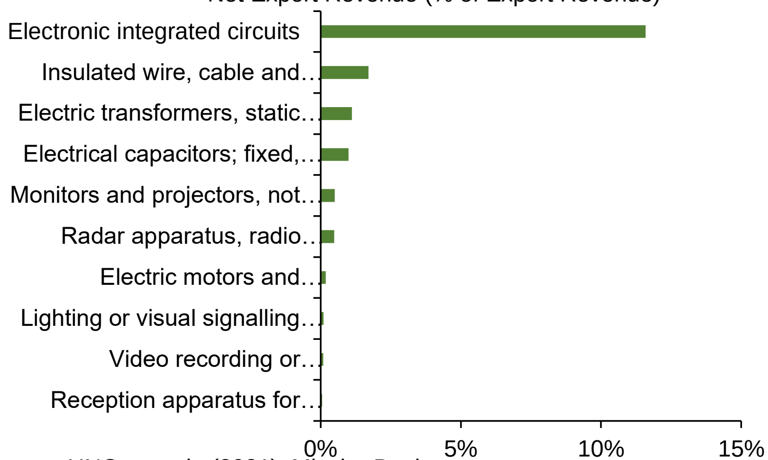
Source: Input-Output Table; Mizuho Bank

Malaysia: Electrical machinery and Equipment Breakdown: Net exports (% of Export Revenue)



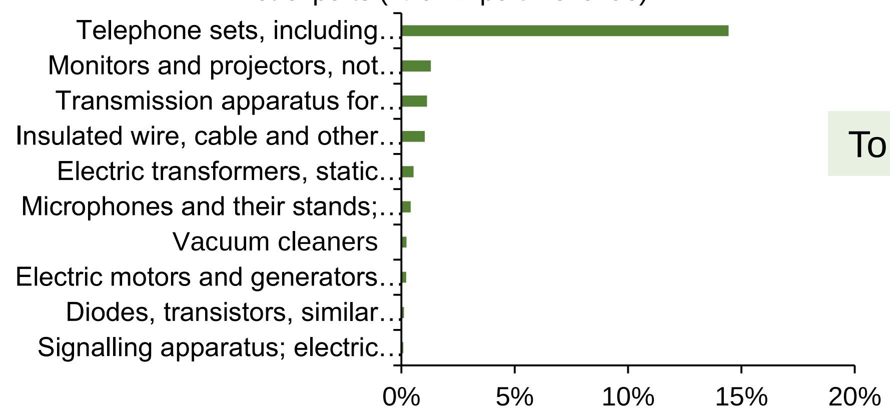
Source: UNComtrade (2021); Mizuho Bank

Philippines: Electrical machinery and equipment Breakdown: Net Export Revenue (% of Export Revenue)



Source: UNComtrade (2021); Mizuho Bank

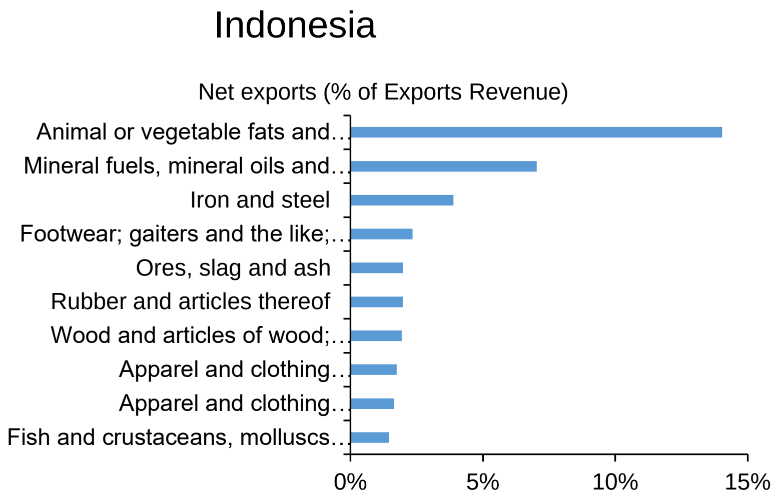
Vietnam: Electrical Machinery and Equipment Breakdown: Net exports (% of Export Revenue)



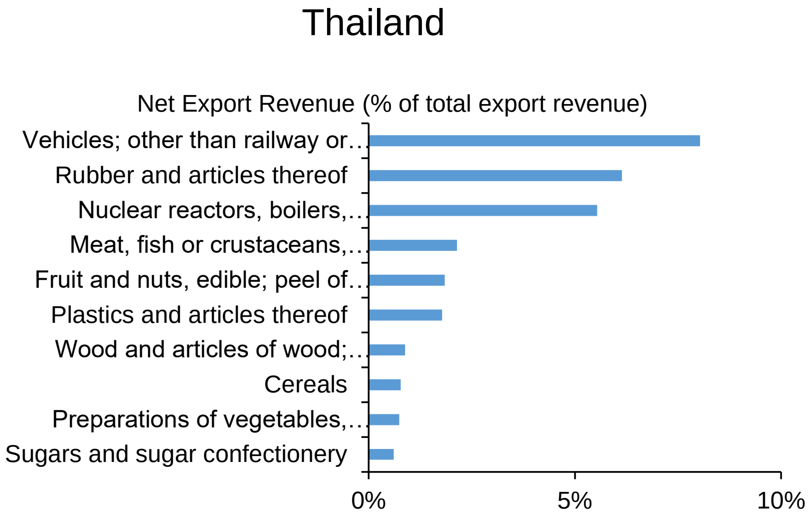
Source: UNComtrade (2021); Mizuho Bank

To work

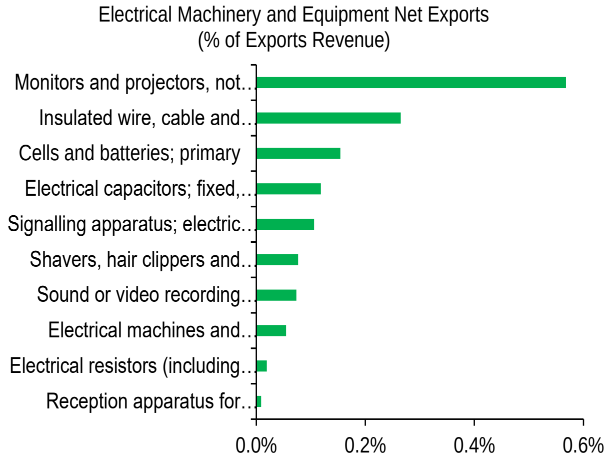
Appendix: Goods – Limited Tailwinds for Others



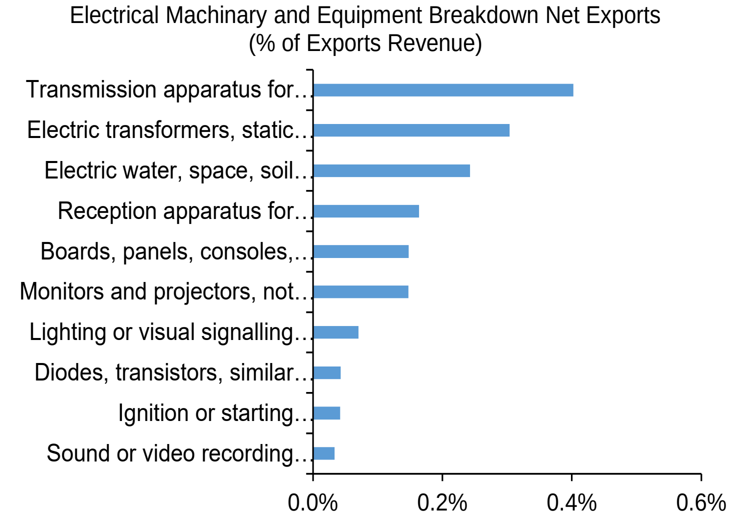
Source: UNComtrade (2021); Mizuho Bank



Source: UNComtrade (2021); Mizuho Bank



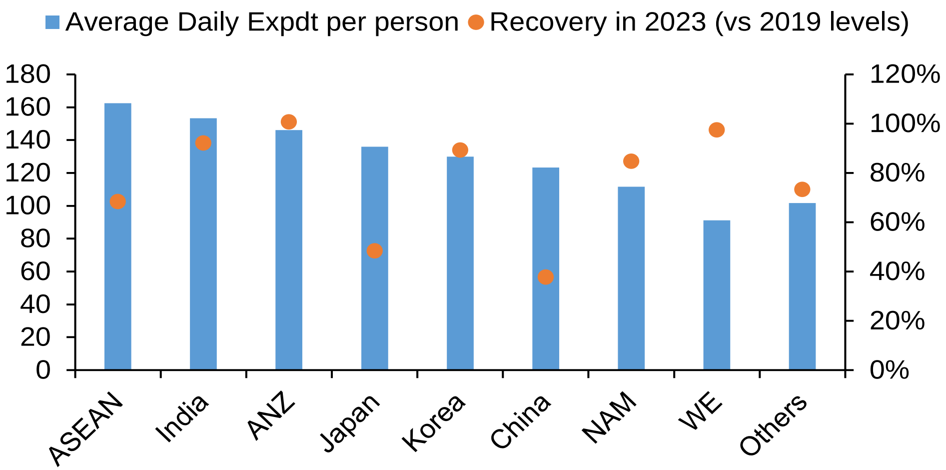
Source: UNComtrade 2021: ; Mizuho Bank



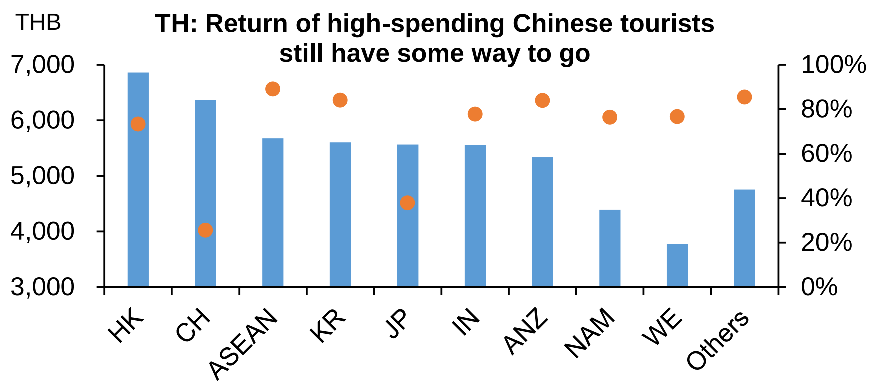
Source: UNComtrade (2021); Mizuho Bank

Appdendix: Tourism: Hitting Exhaustion with the Low-Hanging Big Gains?

Indonesia: Daily Expdt per person vs Recovery



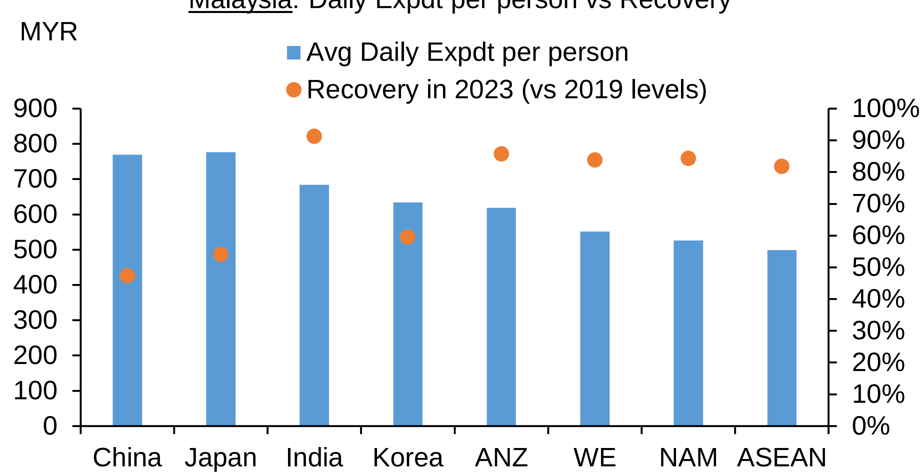
Source: CEIC; Mizuho Bank



Note: Western Europe (WE) comprises Austria, Belgium, France, Germany, Netherlands, Spain, Switzerland and UK; North America (NAM) comprises Canada and USA.

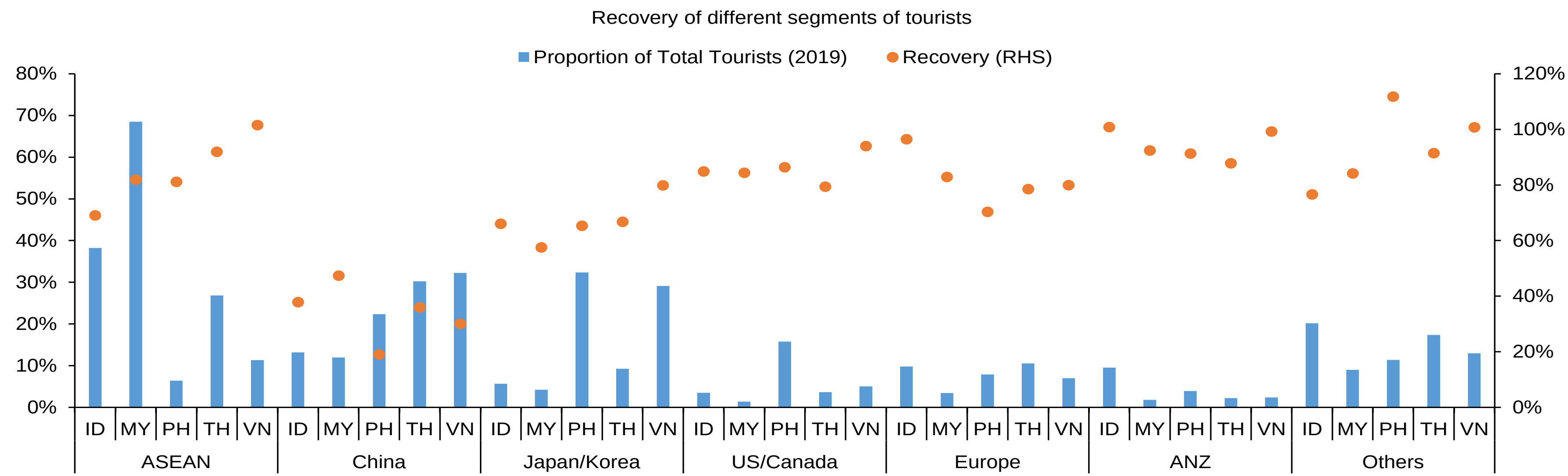
Source: CEIC; Mizuho Bank

Malaysia: Daily Expdt per person vs Recovery



Source: CEIC; Mizuho Bank

Appendix: Tourism: The Chinese Tourists



Source: CEIC; Mizuho

Visa Requirements for Chinese Tourists

Destination	Visa Requirements
Thailand	Visa-Free (eff 25 Sep 2023)
Malaysia	Visa-Free (eff 1 Dec 2023)
Singapore	Visa-Free (eff 9 Feb 2024)
South Korea	Visa-free to Jeju or if transitting to certain destinations only.
Vietnam	eVisa; Visa-free for Phu Quoc only
Philippines	Apply Visa at consulate following suspension of eVisa on 30 Nov 2023
Japan	eVisa

Source: Government agencies; various news outlets; Mizuho