

CAMRI Global Perspectives

Monthly digest of market research & views

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Currency Conflict – A Hazy Outlook?

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The Cusp of Conflict: The Yen in Motion

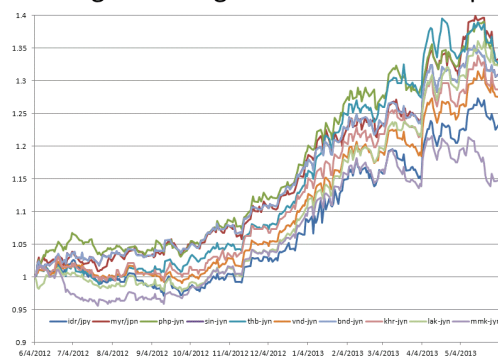
The noble effort to revive the moribund Japanese economy has caused tension among Japan’s Asian trading counterparts. The yen depreciated 28% against the dollar in the span of 9 months, propelling the Nikkei up by 66% over the same period. It has attracted international attention to the aggressive Japanese monetary strategy, and awakened domestic interest in their moribund equity market and economy. One early sign of success has been the improved demand for homes and mortgages. Fear struck Japanese home buyers that policy might become successful and send home prices and mortgage rates upwards. It is too early to judge whether the Prime Minister’s three-pronged strategy will succeed, but it has caused reactions among Japan’s Asian trading partners.

Reactions from the region

ASEAN currencies have appreciated by 20% to 30% against the yen in less than a year, as shown in chart 1. Moreover, ASEAN countries’ exports growth is decelerating rapidly. For example, Malaysia experienced a 3.3% decline in exports in April from a

year ago; exports from the Philippines plunged 12.8% in April; April exports contracted for the 13th straight month in Indonesia; and in Thailand exports slowed leaving Thailand with a record trade deficit. In May, Singapore reported that their exports dropped 4.6% from last year. For an export-led economy, plunging demand for its exports in Q2 2013, following a contraction of GDP in Q1, sends a serious signal of economic problems.

Foreign Exchange Rates ASEAN vs Japan



Decreased demand from everywhere

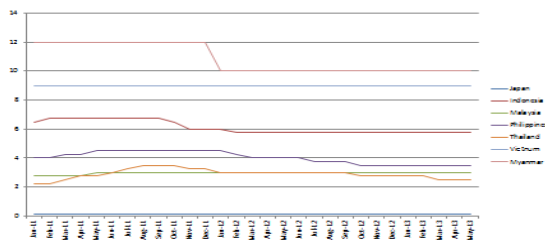
While some of the deceleration in export activity is attributable to the prolonged slowdown in external demand from the sagging western economies, some is also due to the recent more-than-expected deceleration in economic growth in China.

China’s industrial production growth slowed to 9% YOY in May, and their export growth declined to just 1% over the past year. Such deceleration in China’s production activity caused them to drastically reduce their demand for commodities, hence damaging commodity exporters throughout the region. A final factor contributing to ASEAN’s declining exports is the altered dynamics in trade with Japan.

ASEAN governments’ reaction

ASEAN governments are worried over the loss in export activity since exports have been so important to regional growth. They have averaged 77% of GDP for the group. Consequently governments are beginning to react to this loss first by lowering interest rates (see chart below) to alter the price competitiveness with Japan, to reduce the relative attractiveness of short-term investment in their money markets, and to curtail the flow of capital coming into the region. A second action being considered is to tighten their entry criteria to block products made in Japan.

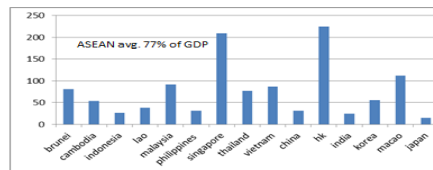
ASEAN Central Banks Reducing Rates



Japan has become the major external trade counterparty with many of the ASEAN

economies, and Asian countries have become Japan’s largest export market, especially China and the Newly Industrialized Economies (NIEs). South Korea, a very close competitor to Japan, is already reacting in a manner similar to the ASEAN governments with respect to the competitive threat from the devaluing yen.

ASEAN Exports as % of GDP vs Other Economies (2011)



Stepping back from the cusp

Recently market participants have become less sanguine over the prospects for the success of Abenomics. The third prong of his strategy, structural reforms, has provided scant new ideas to previous proposals, and many of them would be very difficult to legislate. Consequently, the depreciation of the yen stalled and the Nikkei slid backwards in the past few weeks. The market’s dissatisfaction brought the FX tension back from the brink of conflict. But with exports diminished and prospects for improvement in the near future negligible, the depreciated yen may still be the ASEAN governments’ common enemy. Therefore, they may still use it as an excuse to shield their monetary actions.

For more information, please contact camri@nus.edu.sg

KEY INDICATORS TABLE (AS OF 31 May 2013)								
INDEX	LEVEL LC	%1MO (LC)	%1MO (USD)	%1YR	%1YR (USD)	INDEX	LEVEL	%1YR
S&P500	1630.74	2.34	2.34	27.28	27.28	3MO LIBOR	0.27525	-41.04
FTSE	6583.09	2.87	0.45	29.02	26.99	10YR UST	2.1282	36.62
NIKKEI	13774.54	-0.62	-3.91	64.50	27.86	10YR BUND	1.505	25.37
HANG SENG	22392.16	-0.87	-0.90	24.10	24.08	10YR SPG	4.44	-32.33
STI	3311.37	-1.09	-3.60	23.01	25.28	10YR SGS	1.81	23.30
EUR	1.2999	-1.28		5.13		US ISM	49	-6.70
YEN	100.45	3.08		28.26		EU PMI	48.3	7.10
CMCI	1467.755	-0.82		2.03		JP TANKAN	-8	-33.33
Oil	91.97	-1.59		6.29		CHINA IP	9.2	-4.20

Source: Bloomberg

APPENDIX

GLOSSARY OF KEY TERMS (Source: Bloomberg, with tickers in parenthesis. In US\$ where applicable)

S&P500: capitalization-weighted index of the prices of 500 US large-cap stocks (SPX)

FTSE: capitalization-weighted index of the prices of the 100 largest LSE-listed stocks (UKX)

NIKKEI: capitalization-weighted index of the largest 225 stocks of the Tokyo Stock Exchange (NKY)

HANG SENG: capitalization-weighted index of companies from the Hong Kong Stock Exchange (HSI)

STI: cap-weighted index of the top 30 companies listed on the Singapore Exchange (FSSTI)

EUR: USD/EUR exchange rate: 1 EUR = xx USD (EUR)

YEN: YEN/USD exchange rate: 1 USD = xx YEN (JPY)

CMCI: Constant Maturity Commodity Index (CMCIPI)

Oil: West Texas Intermediate prices, \$ per barrel (CLK1)

3MO LIBOR: interbank lending rate for 3-month US dollar loans (US0003M)

10YR UST: 10-year US Treasury yield (IYC8 – Sovereigns)

10YR BUND: 10-year German government bond yield (IYC8 – Sovereigns)

10YR SPG: 10-year Spanish government bond yield, proxy for EU funding problems (IYC8 – Sovereigns)

10YR SGS: 10-year Singapore government bond yield (IYC8 – Sovereigns)

US ISM: US business survey of more than 300 manufacturing firms by the Institute of Supply Management that monitors employment, production inventories, new orders, etc. (NAPMPMI)

EU PMI: Purchasing Managers' index for the 17 country EU region (PMITMEZ)

JP TANKAN: Bank of Japan business survey on the outlook of Japanese capital expenditures, employment and the overall economy, quarterly index (JNTGALLI)

CHINA IP: China's Industrial Production index, with 1-month lag (CHVAIOY)

LC: Local Currency

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