Mizuho Asia Quarterly – Q4 2021

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MIZUHO

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— Q4 2021: More Heat than Light —

It's one thing that *"variant risks"* could pose as a **damp squib to hopes of emerging encumbered from the figurative COVID tunnel**; as "start-stop" activity resumption remains a reality. But the ***wider point*** is that regardless of how "variant risks" are expressed and managed, the process of ***emerging from the COVID tunnel will be fraught with more heat than light***; and in more than one sense of that phrase.

For starters, **impediments to unfettered global travel will delay and hobble recovery**. Not just in tourism-dependent industries but more widely as elusive tourism-related multipliers subdue aggregate demand. Moreover, **supply chain kinks** may be **exacerbated by asynchronous global growth recovery**; amid lagged/phased vaccine administration.

Crucially, **inflation running hot will turn the heat up on central banks to exit from policy accommodation far sooner** than they otherwise might have been comfortable with; given the lamentable **dearth of "light" to clearly spot** a path of **sustained growth** with confidence.

What's more, impending **fiscal fade** amid a **shift in psyche** *(from pulling all stops for economic survival to pulling fiscal punches),* as fiscal sustainability priorities and inflation risks overtake, means ***fiscal authorities may have to take some heat***. Especially in EM economies hit by mounting deficits and debt. *If caught wrong-footed,* this **may trigger credit risk warning lights**.

Above all, with a hawkish Fed set to lead rate hikes, **higher global yields and a stronger USD** means ***hot money could leave EM economies out in the cold;*** exposed to the chills of macro-stability risks at the nascent/fragile stage of recovery. Finally, **geo-political risks involving Russia and US-China unearth diplomatic heat** *rather than light the way for global cooperation* on COVID and climate.

27th December 2021

Mizuho Bank, Ltd.

Asia & Oceania Treasury Department

Executive Summary

• **US: Solid economic momentum** heading into 2022 and **chronic inflation overshoot underpins the Fed's hawkish turn**; retiring "transitory" inflation concession, concluding taper by Q1 2022 and three rate hikes penciled in by the Dec FOMC 'Dot Plot'. And even if fiscal shortfall on "build back better" is a risk, this will probably not dampen the Fed's hawkish intent in H1 2022.

• **EZ:** With **Omicron setbacks harsher in Europe**, the **ECB is validated in lagging the Fed's "exit"** despite elevated inflation. While sharper policy inflection in H2 2022 is a non-negligible risk that could heighten volatility. **Japan:** ***Despite growing discomfort with inflation,*** the **BoJ will to maintain the most dovish stance**; as cost push ultimately suppress demand.

• **China:** The CEWC, China's top economic policy-setting body, **unambiguously pivoting to policy stimulus** ***is diametrically opposed to a hawkish Fed***. **But** on-going efforts to rein in tighten **property sector risks**/excesses **alongside "common prosperity" objectives entail sharp trade-offs** in relation **to** quantitative economic (**growth**) outcomes.

• That said, **PBoC's credit re-channeling to priority sectors** in cutting edge tech, new energy and material/Bio-med should **provide some offset from property sector** (~30% of GDP) **drag**. Overall **social and economic** *(growth, currency, leverage)* **stability will guide policies**.

• **India:** The *good news* is that a **more entrenched recovery** (from "delta devastation) has been underway since H2. The *reality* is that the recovery is from a **soft base** and lamentably **uneven**. And the *challenge* is that **resurgent inflation intensifies RBI policy dilemma and growth risks**.

• **Indonesia's growth may fall short of potential** as *rising global rates* and *lingering COVID risks* hamper; but **commodity tailwinds provide welcome policy space and IDR backstop**.

• Export tailwinds accentuated by chip demand, aid South Korea's recovery. But BoK hikes pose a latent headwind. Vietnam's labour supply setback from COVID may take a while to dissipate completely, deferring a full and even recovery; US Treasury-related VND risks watched too**.**

• **Singapore:** *High vaccination* rates, *boost from chips/Pharma* and *wealth effects* lend **cyclical resonance to recovery**, **validating further MAS tightening**; though China/wider risks lurk. **Malaysia** is better positioned for a more emphatic recovery with rising vaccination and buoyant Oil providing fiscal cushion. But *supply-chain kinks* and *variant risks* suggest a **bumpy recovery**.

• **Thailand** remains **hobbled by tourism** resumption being impeded. Between Omicron and China's Zero COVID policy (of closed border), *unfettered tourism re-boot will have to wait till late-2022*. This **buys the BoT time**, but (less than deserved) to H2 only. **Philippines growth may be flattered by Q1-Q2 campaign spending** for the Presidential elections in May; but **underlying recovery may yet be subpar** as tourism snags and higher inflation dampen demand recovery**.**

• **Australia: RBA's QE may terminate** as early as Fed, although rate hikes may be pushed out to H1 2023 given a highly uneven recovery led by volatile commodities.

• **AXJ:** The backdrop of a "**Kokomo USD**", characterized by **front-end USD strength in 2022 before mellowing in the latter half**, sets AXJ up for "two-halves" (weaker/more volatile earlier, regaining traction/ stability later). A **hawkish Fed** and **higher oil/inflation** means *"twin deficit" currencies may underperform,* while a stable **CNY backstops proxy currencies**.

AT A GLANCE

Yearly Economic Forecasts

Country	2020			2021			2022		
	GDP YoY	CPI	C/A (% GDP)	GDP YoY	CPI	C/A (% GDP)	GDP YoY	CPI	C/A (% GDP)
United States	**-3.4**	**1.2**	**-2.9**	**5.7**	**4.8**	**-3.5**	**4.1**	**4.0**	**-3.5**
Japan	**-4.6**	**0.0**	**3.2**	**1.9**	**-0.2**	**3.0**	**2.8**	**0.6**	**2.8**
Eurozone	**-6.4**	**0.3**	**2.0**	**5.0**	**2.6**	**2.6**	**4.3**	**2.4**	**2.8**
ASIA (ex-Japan)	**-0.8**	**2.8**	**2.4**	**7.2**	**2.2**	**2.6**	**6.0**	**2.1**	**1.5**
ASEAN-6	**-3.5**	**1.3**	**3.0**	**3.2**	**1.9**	**1.7**	**5.7**	**2.1**	**1.6**
China	2.3	2.4	1.5	8.0	1.3	2.0	5.8	2.3	1.5
India	-7.1 (-7.5)	6.6 (6.2)	0.9	8.0 (9.0)	5.2 (5.6)	-1.0	7.9 (7.9)	5.9 (5.7)	-1.4
Korea	-0.9	0.5	4.6	3.7	2.4	4.5	3.3	2.4	4.2
Singapore	-5.4	-0.2	17.6	6.9	2.0	18.5	4.1	2.2	17.2
Malaysia	-5.6	-1.1	4.2	3.1	2.3	3.8	6.0	1.7	3.7
Indonesia	-2.1	2.0	-0.4	3.5	1.5	-0.3	5.0	2.3	-1.0
Thailand	-6.1	-0.8	3.5	1.2	1.2	-0.5	3.5	1.6	2.1
Philippines	-9.6	2.6	3.6	5.0	4.3	0.4	7.2	3.0	-1.8
Vietnam	2.9	3.2	3.7	2.4	1.9	1.8	6.0	3.2	3.2
Australia	-2.4	0.9	2.2	4.3	2.6	3.6	3.7	1.8	1.8

Note: Asia (ex Japan) includes China, India, South Korea, Singapore, Hong Kong, Taiwan, Malaysia, Indonesia, Thailand, Philippines, Vietnam
The current account forecasts for Asia, the GDP, CPI and CA foreasts for G3 are from the IMF (October 2021 WEO edition)

Quarterly Outlook – Growth and Consumer Inflation

Growth Forecasts

GDP Growth Forecasts (% YoY)

Country	2020				2021				2022				2017-19	2020	2021	2022	2023
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Average	(FY20/21)	(FY21/22)	(FY22/23)	(FY23/24)
Australia	1.4	-6.2	-3.7	-1.0	1.4	9.5	3.9	1.9	3.8	1.9	4.8	4.2	2.4	-2.4	4.3	3.7	2.8
China	-6.8	3.2	4.9	6.5	18.3	7.9	4.9	4.1	4.4	5.1	7.0	6.2	6.5	2.3	8.0	5.8	5.5
India	3	-24.4	-7.4	0.5	1.6	20.1	8.4	5.2	5.2	14.0	6.8	6.4	5.8	-7.1 (-7.5)	8.0 (9.0)	7.9 (7.9)	6.5 (6.4)
Indonesia	3.0	-5.3	-3.5	-2.2	-0.7	7.1	3.5	4.4	5.7	3.9	5.0	5.4	5.1	-2.1	3.5	5.0	5.5
Malaysia	0.7	-17.1	-2.6	-3.4	-0.5	16.1	-4.5	3.4	6.5	2.8	8.6	6.3	5.0	-5.6	3.1	6.0	4.8
Philippines	-0.7	-17.0	-11.6	-8.3	-3.9	11.8	7.1	5.4	10.0	4.3	7.4	7.5	6.5	-9.5	5.0	7.2	6.5
Singapore	0.0	-13.3	-5.8	-2.4	1.5	15.2	7.1	4.6	2.9	4.5	4.8	4.2	3.1	-5.4	6.9	4.1	3.3
Korea	1.4	-2.7	-1.1	-1.4	1.9	6.0	4.0	3.1	2.4	2.2	3.6	4.8	2.8	-1.0	3.7	3.3	2.7
Thailand	-2.0	-12.1	-6.4	-4.2	-2.6	7.5	-0.3	0.6	1.7	2.1	5.2	5.0	3.5	-6.1	1.2	3.5	3.4
Vietnam	3.7	0.4	2.6	3.8	4.7	6.6	-6.2	4.5	4.8	5.5	9.0	5.0	7.1	2.9	2.4	6.0	6.5

Consumer Inflation forecasts

Inflation Forecast (%YoY)

Country	2020				2021				2022				2017-19	2020	2021	2022	2023
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Average	(FY20/21)	(FY21/22)	(FY22/23)	(FY23/24)
Australia	2.2	-0.3	0.7	0.9	1.1	3.8	3.0	2.4	2.1	1.9	1.6	1.8	1.8	0.9	2.6	1.8	2.1
China	5.0	2.7	2.3	0.1	0.0	1.1	0.8	1.8	2.1	2.2	2.4	2.3	2.2	2.5	1.3	2.3	2.4
India	6.7	6.6	6.9	6.4	4.9	5.6	5.1	5.1	6.2	6.0	5.9	5.7	3.9	6.6 (6.2)	5.2 (5.6)	5.9 (5.7)	5.1 (5.2)
Indonesia	2.9	2.3	1.4	1.6	1.4	1.5	1.6	1.7	1.9	2.5	2.5	2.4	3.3	2.0	1.5	2.3	2.5
Malaysia	0.9	-2.6	-1.4	-1.5	0.5	4.2	2.1	2.4	1.9	1.7	1.7	1.3	1.8	-1.1	2.3	1.7	1.5
Philippines	2.7	2.3	2.5	3.1	4.5	4.4	4.6	4.0	3.1	3.2	2.9	2.7	3.5	2.6	4.3	3.0	3.2
Singapore	0.4	-0.7	-0.3	-0.1	0.8	2.3	2.5	3.1	2.6	2.1	2.3	1.4	0.5	-0.2	2.0	2.2	1.6
Korea	1.2	-0.1	0.6	0.4	1.1	2.5	2.6	3.5	2.8	2.5	2.0	1.5	1.3	0.5	2.4	2.4	1.2
Thailand	0.4	-2.7	-0.7	-0.4	-0.5	2.4	0.7	2.5	2.2	1.3	2.0	1.0	0.8	-0.8	1.2	1.6	1.0
Vietnam	5.6	2.8	3.2	1.4	0.3	2.7	2.5	2.3	3.5	3.3	3.2	3.0	3.3	3.2	1.9	3.2	3.5

Central Bank Policy Outlook

Central Bank Policy Outlook

Country	Central Bank	2020				2021				2022				2023	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
US	**Fed**	**0.00-0.25%**	**0.00-0.25%**	**0.00-0.25%**	**0.00-0.25%**	**0.00-0.25%**	**0.00-0.25%**	**0.00-0.25%**	**0.00-0.25%**	**0.00-0.25%**	**0.25-0.50%**	**0.50-0.75%**	**0.75-1.00%**	**1.00-1.25%**	**1.00-1.25%**
Australia	**RBA**	0.25%	0.25%	0.25%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.25%	0.50%	0.50%
China	**PBoC**	4.35%													
		4.05%	3.85%	3.85%	3.85%	3.85%	3.85%	3.85%	3.80%	3.75%	3.75%	3.75%	3.75%	3.75%	3.75%
India	**RBI**	4.40%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.25%	4.50%	4.75%	4.75%	4.75%	4.75%
Indonesia	**BI^**	4.50%	4.00%	4.00%	3.75%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.75%	4.00%	4.25%	4.50%
Malaysia	**BNM**	2.50%	2.00%	1.75%	1.75%	1.75%	1.75%	1.75%	1.75%	1.75%	2.00%	2.25%	2.50%	2.50%	2.50%
Philippines	**BSP**	3.25%	2.50%	2.25%	2.00%	2.00%	2.00%	2.00%	2.00%	2.25%	2.25%	2.50%	2.75%	3.00%	3.00%
Singapore	**MAS***	Flatten S$NEER & Re-Centre to Prevailing S$NEER (~40-70bps lower)		Status Quo		Status Quo		Restore a "Slight" S$NEER Slope (0.5% per annum)		"Slight" Increase to S$NEER Slope (1.0% per annum)		Maintain S$NEER Slope (1.0% per annum)		"Slight" Increase to S$NEER Slope (1.5% per annum)	
Korea	**BoK**	0.75%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.50%	1.50%	1.50%	1.50%
Thailand	**BoT**	0.75%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.00%	1.00%
Vietnam	**SBV**	5.00%	4.50%	4.50%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.25%	4.50%	4.50%	4.50%

* The MAS conducts monetary policy via FX. Specifically it adopts a trade-weighted SGD appreciation at "modest and gradual" (estimated to be 2% per annum) pace as default.

^ BI shifted to the 7 Day repurchase rate as the benchmark rate in August 2016. This by default constituted 125 bps reduction from the last policy rate

^^ PBoC instituted the loan prime rate (LPR), which sets a floor on commercial interest rates. This replaces the 1-yr Lending rate

FX Outlook

FX Forecasts	Dec 21	Mar 22	Jun 22	Sep 22	Dec 22	Mar 23
USD/JPY	112 - 116 (114)	113 - 117 (115)	114 - 120 (116)	114 - 120 (117)	114 - 121 (118)	114 - 121 (118)
EUR/USD	1.11 - 1.16 (1.13)	1.10 - 1.15 (1.12)	1.11 - 1.16 (1.13)	1.11 - 1.16 (1.14)	1.12 - 1.16 (1.14)	1.12 - 1.16 (1.14)
USD/CNY	6.17 - 6.62 (6.43)	6.35 - 6.80 (6.60)	6.37 - 6.87 (6.53)	6.12 - 6.57 (6.32)	6.13 - 6.58 (6.33)	6.18 - 6.55 (6.38)
USD/INR	73.1 - 78.1 (75.8)	73.3 - 79.0 (76.5)	73.5 - 78.3 (76.0)	71.4 - 77.2 (74.8)	70.9 - 76.6 (74.2)	69.7 - 76.0 (73.0)
USD/KRW	1160 - 1250 (1200)	1170 - 1300 (1250)	1200 - 1310 (1250)	1150 - 1250 (1200)	1100 - 1210 (1150)	1080 - 1170 (1120)
USD/SGD	1.33 - 1.40 (1.37)	1.35 - 1.42 (1.38)	1.33 - 1.44 (1.37)	1.31 - 1.40 (1.35)	1.29 - 1.38 (1.33)	1.29 - 1.37 (1.33)
USD/IDR	13840 - 14920 (14200)	14120 - 15290 (14550)	14310 - 15620 (14750)	13940 - 15140 (14400)	13790 - 14990 (14250)	13650 - 14960 (14100)
USD/MYR	3.96 - 4.40 (4.21)	4.07 - 4.45 (4.23)	3.97 - 4.36 (4.22)	4.00 - 4.33 (4.19)	4.00 - 4.32 (4.17)	3.97 - 4.30 (4.14)
USD/PHP	49.3 - 53.2 (51.0)	49.8 - 53.5 (51.8)	49.2 - 53.0 (51.4)	48.7 - 52.5 (50.9)	47.9 - 51.6 (50.0)	48.0 - 52.2 (50.1)
USD/THB	33.2 - 35.3 (33.9)	32.8 - 35.5 (34.0)	32.0 - 35.0 (33.8)	31.1 - 34.1 (33.0)	31.1 - 33.3 (32.0)	30.7 - 32.9 (31.6)
USD/VND	22700 - 23400 (23000)	22900 - 23500 (23250)	22900 - 23600 (23150)	22700 - 23300 (22800)	22500 - 22900 (22600)	22400 - 23000 (22650)
USD/MMK	2030 - 2170 (2076)	2080 - 2230 (2138)	2140 - 2250 (2181)	2180 - 2310 (2246)	2250 - 2380 (2314)	2320 - 2480 (2383)
AUD/USD	0.673 - 0.756 (0.710)	0.667 - 0.757 (0.700)	0.661 - 0.745 (0.713)	0.697 - 0.777 (0.735)	0.727 - 0.801 (0.765)	0.757 - 0.827 (0.788)

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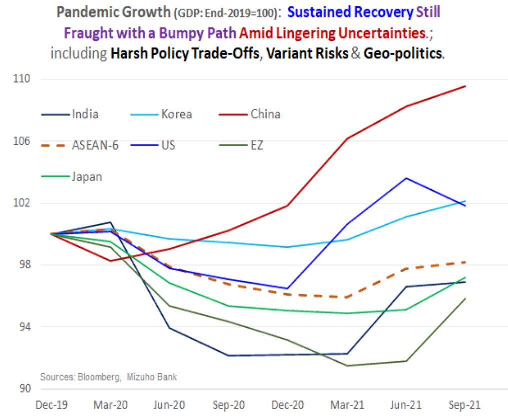
Global Overview: More Heat than Light?

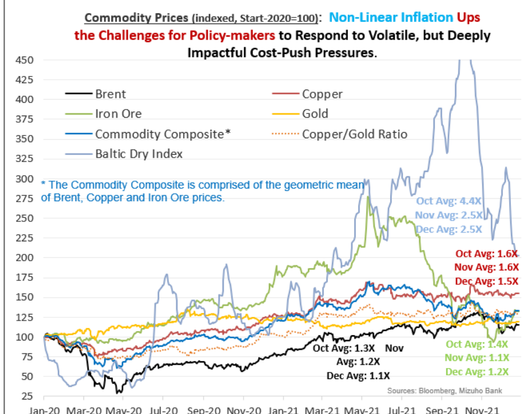
Growth: Clarity remains in short supply; as **emerging from the COVID tunnel** emphatically in 2022 (flagged in the last edition), while valid, **reveals *more heat than light***. To be sure, the **good news** is that the **global economy is on track to extend and entrench recovery**; as **re-opening of borders** fire up tourism-related multipliers and scope for **de-congestion of supply-chains** greases industrial activity. ***But*** the **recovery path** is **likely to be bumpy**; characterized by uneven, not unfettered, acceleration. Moreover, between policy response (albeit from exceptional accommodation) **to** *inflation worries*, *fiscal fade* (both planned and unintended) *literally* **evolving** *"variant risks"*, not only is the **uncertainty** around amplitude and timing of sustained pick-up **elevated**, but **synchronization of global recovery remains fraught**.

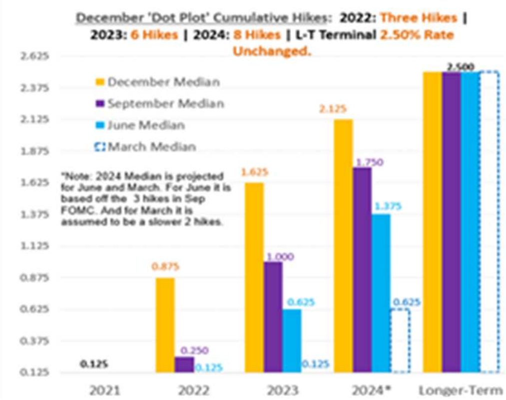
Risks: Adverse pandemic evolution, **policy mis-steps** and **geo-political friction** are **three glaring risks**. Admittedly, with significantly higher global vaccination rates, severity of economic pain from COVID variants diminishes disproportionally. That said, **vaccine-evading**, **virulent variants** interrupt and undermine; given *reliance on border re-opening* to *revive tourism multipliers* to even out the recovery and *dis-entangle supply kinks* (consumption shifts and labour flow). In addition, ***excessive/inadequate policy response to non-linear but potentially sticky inflation*** (amid *asynchronous global policy normalization*) pose *dangers from overwhelming headwinds/macro-instability*. Finally, **geo-political risks** remain the *known unknown*.

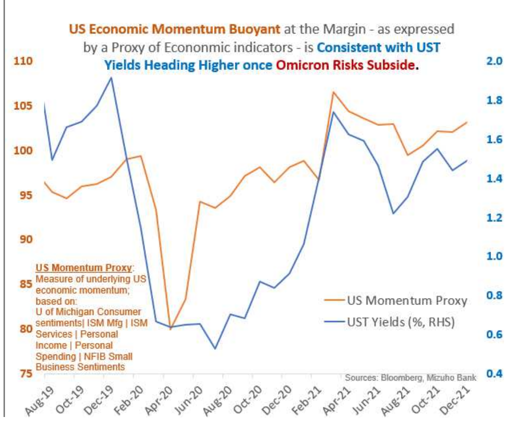
Policy: **"Kokomo"** – *"get here fast, then take it slow"* – **exit** (Box 1) from exceptionally easy policy is the policy "sweet spot" to **minimize policy risks** associated with trade-offs in taming inflation risks at a nascent/fragile stage of recovery.
While **preventing inflation expectations from becoming untethered**, it mitigates risks of ***over-tightening*** into fiscal fade and over-reacting to fading cost-push as; i) *pent-up pandemic demand is re-channeled* (re-allocation to services); ii) capacities restored, and; iii) *jobs filled* amid re-opening borders/pandemic fade. Apart from **hastened 'taper' to wind down QE in Q1 2022**, the **Fed** may **initiate hikes no later than mid-2022**. The **BoJ** and, to a lesser extent, the **ECB** are **expected to lag the Fed appreciably** in terms of tightening.

Asset Markets: **Higher UST yields** (curve flattening bias on rate hikes) *square with a "Kokomo" Fed*. Correspondingly, **a stronger USD** may assert in H1 2022, amid hawkish; although **as policy divergence flips to convergence,** a ***mellower USD*** is likely in H2. Nevertheless, ***USD strength and higher yields* may conspire to trigger risk re-pricing in H1**. In particular, if rising rates (on cost-push inflation worries) are not offset by cheer from rising demand; and equities begin to slip back as "taper" collides with historically rich valuations. But the silver lining is, **flush global liquidity** despite taper – and partly owed to extended ECB bond buying (with APP offset to PEPP expiry) – **means an implosion is not the base case either**.

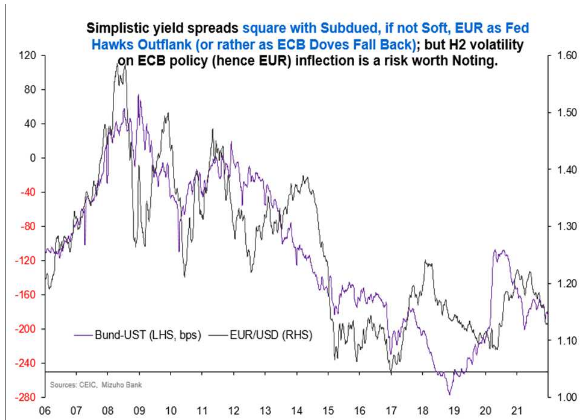




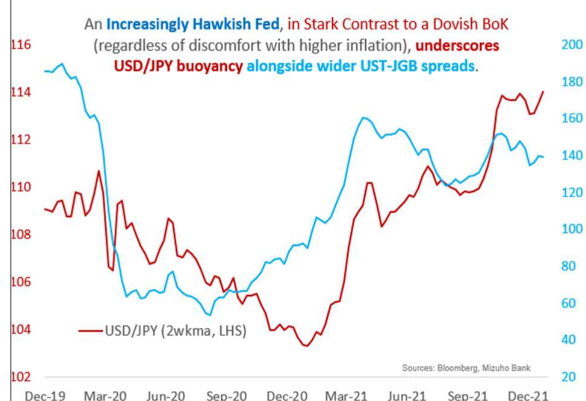




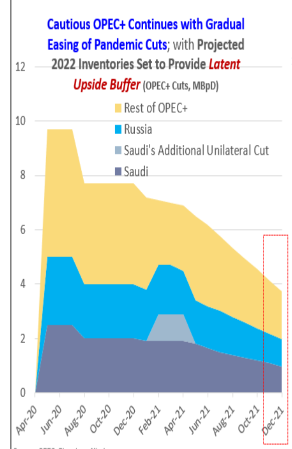
EUR/USD Outlook: A **conflict of policy divergence with Fed driving the EUR lower** on one hand **and persistent and solid C/A surplus** of 2.3-2.8% of GDP backstopping the EUR on the other, ***underpin inherent tensions and resultant volatility*** in EUR. Nonetheless, **early-2022 EUR tendencies will be to the downside** as the ***ECB is set to entrench dovish insurance*** *– with rate hold commitment and APP bump-up to partly offset the wind down of PEPP end-Q1*. What's more, spiraling gas prices and resultant p**ower crunch eroding profits and purchasing power may undermine early-2022 EUR tone**; entailing sub-1.10 risks. But **H2 ECB-Fed convergence on "exit", ought to revive EUR traction**.

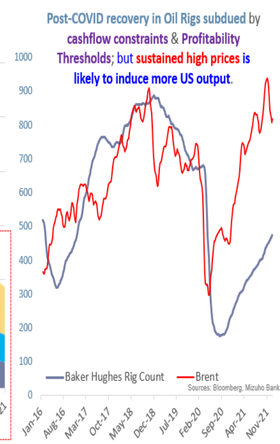


USD/JPY Outlook: Trenchant BoJ doves (underscoring that escalating cost-push pressures are ultimately deflationary for consumer demand), in sharp contrast to a hawkish Fed, **set the stage for JPY under-performance** amongst Major currencies. But 2022 is not set to be a one-dimensional JPY story; not by a long shot. For one, the JPY's safe-haven status means **pockets of JPY surge on bouts of "risk off"** – amid elevated uncertainty around "variant risks" and the confluence of nascent global recovery and asynchronous policy normalization. So, barring worst-case outcomes on US growth/policy mistake risks, USD/JPY may be mostly buoyed; albeit with considerable volatility.



Oil (Brent): Even with recovering demand, there are three reasons **why Oil may settle predominantly amid $65-$90 in 2022**, ***not accelerate uncontrollably to $100-130***. First, for all the restraint in supply restoration by OPEC+, the big picture is for **supply response catch-up** (incremental OPEC+ restoration, potential Iran supply, lagged US response). Second, sharp drawdown in **inventories** have been **at least partly replenished**, thereby mitigating sharp surges in price from softer supply may be mitigated. Finally, **policy tightening** led by the Fed **alongside global fiscal fade may temper demand-supply mismatch**. Moreover, give the usual *negative correlation, Oil is more likely to be tempered by a strong USD.*



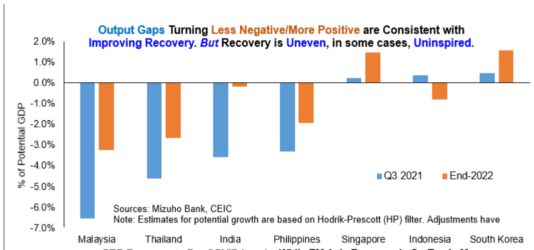


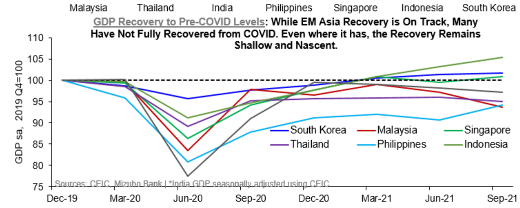
	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
Fed Rate^ (%)	0.00-0.25	0.00-0.25	0.00-0.25	0.00-0.25	0.50-0.75	0.75-1.00
ECB Rate^ (%)	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
BoJ Rate (%)	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
EUR/USD*	1.158	1.14	1.13	1.12	1.13	1.15
	1.15 - 1.20	1.11 - 1.17	1.11 – 1.16	1.09 – 1.15	1.10 – 1.16	1.11 – 1.17
USD/JPY*	111.3	114	116	117	118	119
	108 - 113	110 - 116	113 - 118	114 -120	115 -121	116 -122
Brent Crude (US$/bbl)	78.5	77.5	82.2	76.5	83.5	78.8
	64.6-80.8	65.7-86.7	66.5-88.0	72.5-88.5	70.8-93.0	70.8-84.0

Note: Values in black are historical whereas those in blue represent forecasts.
* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.
^ Fed rates refer to the Fed Funds Target rate; ECB rates refer to the Deposit facility rate.

Asia Outlook: Improving, But Uneven & Uninspired

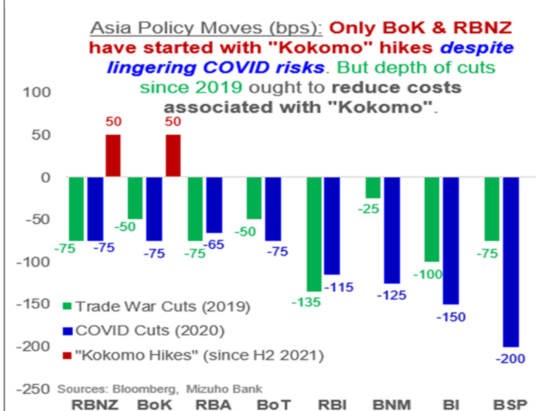
Output: **Continued improvement** in demand recovery will accompany **easing supply chain snarls** amid **rising global vaccination rates**. In particular, as re-opening of borders revives tourism multipliers. **But restoration of activity may be uneven and uninspired**. Not only do *"variant" risks* amid **lags in vaccinations** booster threaten with start-stop setbacks, but **China's Zero-COVID policy** alongside cautious/phased resumption of international travel **stifles aspirations for "escape velocity"** from tourism. What's more, a **hawkish Fed** amid pockets of **lingering supply-side impediments** and **fiscal fade** render H1 2022 recovery a tad tenuous. Finally, ***China's loosening bias*** to avert hard landing, while welcome, may have ***limited wider spillover to the rest of Asia.***



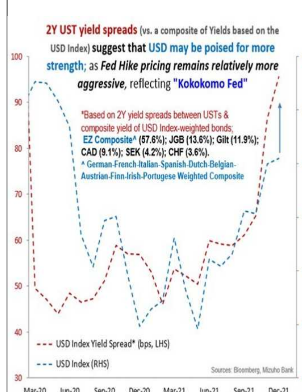


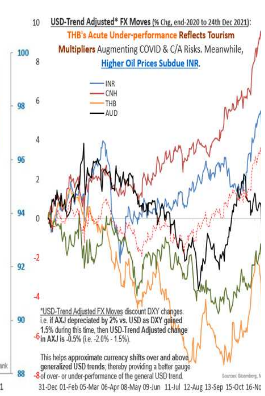
Inflation: Whilst **EM Asia** appears to be **spared the worst of inflation**ary pressures, this is **more a subordination to overarching growth risks and fiscal buffers** subduing cost-push rather **than a get-out-of-jail-free card**. *In fact,* rising food inflation risks in the context of dominant, food (and fuel) weights in CPI baskets means that **inflation will at least persist, if not grow in prominence, as a key risk**. **Not just due to policy ramifications**. But crucially for bread and butter issues such as *erosion of disposable income* compromising consumption multipliers (and boost) and *thinning profit margins* curtailing investment recovery.

Policy: Needless to say, the **policy pressures are also remarkable**. Fiscal policy may inadvertently add to rising cost pressures, but perhaps also be diminished in impact as higher prices hijack quantum of demand. Moreover, **monetary policy tensions are set to mount**. The **trade-off** between ***boosting growth*** and ***risking inflation overtaking incomes*** to depress demand and stability outcomes cannot be shrugged off. This may **require policy makers to tighten sooner** and ***more*** than they might otherwise be inclined to ***at an early stage of the recovery***. With most of **EM Asia policy at record levels of accommodation** also **leaves little wiggle room**. *BSP and RBI* (BNM, BI & BoT to follow later in 2022) may be *at the sharp end of pressures to initiate tightening*; as BoK and MAS tighten further.



FX: **EM Asia FX are set for a year of two halves**, with *front-end (H1) weakness* before scope to regain *traction later in 2022* **as dictated by "Kokomo USD"** – *strong USD giving way to mellower USD in H2 as by hawkish Fed divergence flips to global policy convergence.* Caveat though is that the *juxtaposition of variant risks* and *asynchronous normalization* **accentuating economic uncertainty** and **policy trade-offs** will **heighten volatility and sharpen differentiation** amongst **EM Asia FX**. High inflation, re-emergence of "twin deficits" and tourism dependence may be bugbears undermining currencies. A fairly stable CNY though may offer some degree of backstop.





Box 1: The "Kokomo" Conjecture

"Physics is not about how the world is. It is about what we can say about (it)" – **Niels Bohr**

Kokomo Conjecture: The What

"Aruba, Jamaica, oh I want to take you to/
Bermuda, Bahama, come on pretty mama/
Key Largo Montego, baby why don't we go/
Oh I want take you down to Kokomo/
We'll get there fast and then we'll take it slow/
That's where we want to go/
Way down in Kokomo"
- **Kokomo, Beach Boys, 1988**

Our so-called **"Kokomo" conjecture about central banks** is inspired by the Beach Boys song of that same title: "Kokomo". Specifically, our allusion to the "Kokomo" conjecture is inspired by arguably the most inspirational line, "*get there fast and then … take it slow*". Admittedly, Beach Boys' genius taken out of context. But oh so deliciously apt. For clarity, the "Kokomo" conjecture **proposes *two key postulates*** on policy approach.

1. First, "*we get there fast*"; **in reference to initiating calibrated normalization** from exceptionally accommodative settings.
2. Second and crucially, "*and then we take it slow*"; whereby **by virtue of "getting there fast"**, central banks **may able to stop sooner and at lower terminal rates**, exploiting the policy space from earlier calibrations.

Kokomo Conjecture: The Why

Why "Kokomo"? Because "*getting there fast, and then … taking it slow*", despite the initial appearance of aggressive normalization, eventually results in the **highest likelihood of minimizing economic costs** (both from current tightening in the context of future liability to tighten) whilst **insuring against** the dangers of **run-away inflation** and **mitigating policy credibility risks** associated with reluctance to respond to inflation.

Minimizing Policy Costs: The most compelling reason **"Kokomo" presents the most optimal solution** to an unenviable policy predicament is because this minimizes economic costs from tightening over a longer horizon. Specifically, by way of;

i) **fairly muted economic cost of earlier calibrations** *from exceptionally accommodative policy settings* (e.g. **initial hikes from record low rates** unlikely to derail economic recovery) and;
ii) **diminished risk of compensatory over-tightening** thanks to **moving** earlier, possibly **"ahead of the curve"**.

Put differently, "Kokomo" **offers "a stitch in time" mitigation of far greater costs later**. In "*getting there fast, and then taking it slow*" not only are *costs associated with initial calibrations likely to be measured (helped by an exceptionally low base),* but higher chances of a lower terminal rate *check potential economic pain from having to (over-)tighten later to compensate for delayed policy response.*

The Inflation Quagmire: Crucially, **rising inflation that has proliferated more widely poses a quagmire demanding *urgent* policy response despite lingering pandemic risks**. What began as inconvenient but innocuous supply-side cost push, and mostly dismissed as "transitory", is justifiably fuelling worries of enduring, self-reinforcing inflationary risks.

Especially as the **conspiracy of cost-push and demand-revival factors obfuscate just how persistent and profound inflationary pressures may end up**. Hence, **growing inflation risks amid de-sensitized policy response underscores need to** "*get there fast*". Although, "*then take it slow*" checks over-tightening risks as wage-price spirals are arrested; allowing for cost-push driver o fade off alongside COVID distortions.

Curbing Affronts to Policy Credibility: Consequently, restraint premised on "transitory" cost-push amid nascent recovery must concede to **growing risks of inflation expectations becoming unhinged**. Worryingly, the **real danger may be to the credibility of central banks**. In turn, this requires some urgency of policy response, even if there is genuine belief of fading price pressures in the longer horizon. Inevitably, **policy makers need to,** "*get there fast*" **in spite of "variant risks"** (currently manifesting as "Omicron") and only "*then take it slow*" **once self-fulfilling inflation spiral risks are snapped**; allowing for cost-push to fade.

Kokomo Conjecture: The How

To be fair, between tolerating some inflation as a by-product of recovery and repudiating worrying dimensions of inflationary risks, policy makers are caught between a rock and a hard place. Precisely why **"Kokomo", done right, will help engineer a policy transition that both anchors inflation expectations** (with rapid and decisive early "exit") **and insures recovery** (by refraining from pre-ordained, overdone tightening cycles; especially as inflation fades further out, once wage-price spiral risks are snapped).

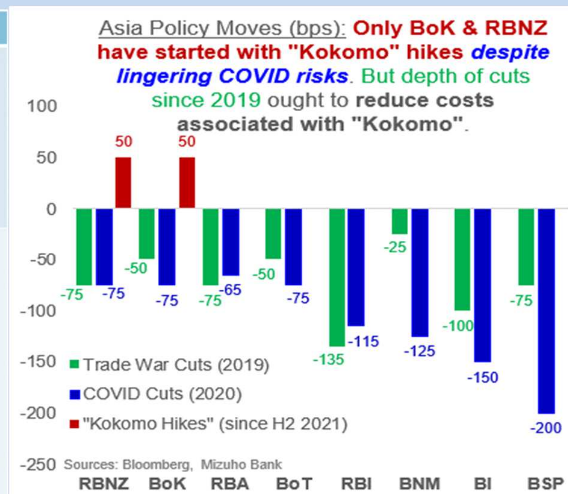
The idea being, **"Kokomo" helps avert an inadvertent lurch from over-confidence** (about "transitory)" **to over-reactions** (to exaggerated inflation fear-mongering); thereby mitigating policy mistake risks with an optimal, "low-cost" approach of **early policy response to inflation upside surprise**.

Kokomo Conjecture: The Who

In Asia, the notable **early-adopter "Kokomo" central banks are** the **BoK** (having hiked twice in 25bps increments, first in August then again in November, to 1.00%), the **MAS** (restoring a calibrated appreciation bias for the S$NEER policy October) and the **RBNZ** (hiking twice in 25bps increments in August and November; to 0.75%).

The **common thread** running through is the **caveat that the "calibrations" do not entail hiking cycles**. The BoK is careful *to qualify calibrations to align with economic conditions as is the MAS.* So the **message of** "*and then … take it slow*", especially **contingent on fluid economic risks** is expressly alluded to. As for the RBNZ, despite the aggressive start to "exit" policy accommodation, it has hinted that a cooling property market may be reason to slow the pace of tightening.

Two-Part "Kokomo" Effect	Drivers
Part 1: "*get there fast*" - Fed to **end QE in Q1-2022** | **At least 2 hikes in 2022** | Starting mid-2022 - BoE to hike ~3 times in 2022	1) **Exceptionally accommodative settings** 2) Inflation **sticker shock** 3) Surge in **Energy Prices** (stagflation worries) 4) **Conspiracy of other cost-push** factors 5) **Sticky Inflation** till mid-/late-2022 6) **Sustained**, if not strong, growth **recovery**
Part 2: "*then … take it slow*" - Fed to not rush QT | pace of hikes to decline by mid-2023 - BoE to slow the pace of hikes by mid-2023	**1) Cost Push factors to subside** into late-2022; albeit unevenly **2) Oil** turns dramatically **dis-inflationary** **3) China** to resume absorbing global inflationary pressures 4) Post-COVID **reversion to services consumption** (even if with a lag) to ease supply-chain/shipping kinks **5) Fiscal fade** from COVID largesse **6) Labour supply catch-up** on lagged re-entry of workers (enhanced by border re-opening)



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Amongst the G4, the **BoE and Fed are leading the way in getting ready to belt out "Kokomo"**. But not all G4 central banks have signed up for "Kokomo". Interestingly, and in a parallel to the RBA-RBNZ contrast, the ECB has pushed back on urgency near-term policy normalization despite appreciable upside surprise in inflation. In doing so, the ECB points to lingering COVID risks to growth that come unfortunately come bundled with transitory COVID-induced price pressures. So the **ECB will necessarily lag the "Kokomo Fed"**. Regardless, the **title of the most steadfast dove**– that for good reasons *cannot appreciate "Kokomo", and hence will not dance to that tune* – **unambiguously belongs to the BoJ**.

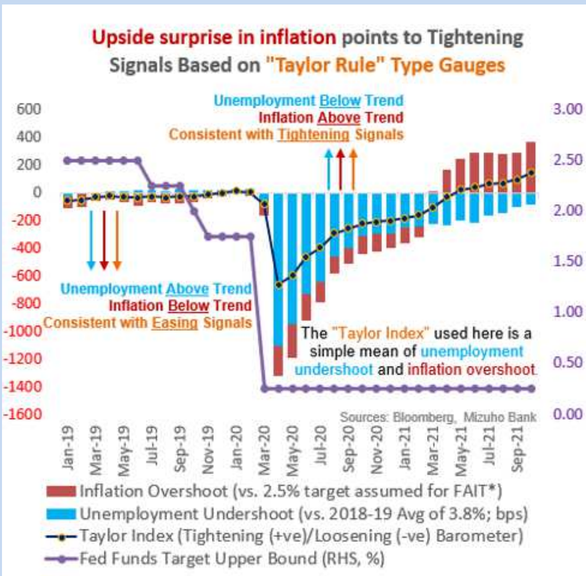
The "Kokomo Fed" …

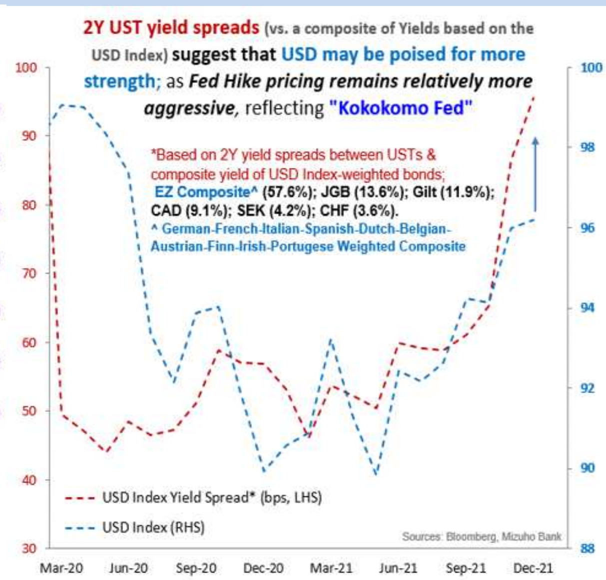
"Kokomo" is a Necessary Reset for the Fed: With the onslaught of upside surprises to US inflation (that hit a 30-year high for October, and still upwardly biased), coupled with broadening price pressures, the **Fed has been caught out overly-dovish** on its pronouncements of "transitory" inflation. This is a threat to, if not **to the detriment of, the Fed's policy credibility**.

And the **"Kokomo"** approach is the Fed's **best shot at reclaiming credibility**, ***without snuffing out the recovery***.

Faster Taper & Rate Hikes for 2022: Accordingly, in deference to inflation dynamics and policy credibility calculus in the US, we have now shifted up our **first Fed rate hike to mid-2022**, with **at least one more hike later in H2**; with a cumulative 100-125bps of hikes by end-2023. And setting the stage for this will be **hastened "taper" so that QE is wound down by late-Q1/early-Q2 2022**; such that there may be a **distinct break between end of taper and the first hike to de-couple** the latter from the former so as to temper overly-hawkish interpretations.

"First Mover" Effect: The point worth noting though is that while "Kokomo" policy approach may be gaining broad appeal, **a "Kokomo Fed", by virtue of its relative "fist mover"** position that is amplified by its economic/financial heft, **inadvertently ends up being the benchmark for laggards and catch-up** amongst other global central banks. This ***sets the stage for Fed policy divergence to dominate the policy and market narrative***.





… Making Landfall as "Kokomo Dollar"?

Consequently, the **Fed policy divergence theme asserted by** the **"Kokomo Fed",** via **significant sway on interest rates/yields**, will **result in the "Kokomo USD"** setting the main backdrop for currency markets. To be clear, the "Kokomo USD" is ***not to be mistaken for a bullish USD***.

Instead, the "Kokomo USD" in its true form will evolve roughly in tandem with the two phases of "Kokomo". The earlier "*get there fast"* phase will mostly **correspond to USD strength**. As a corollary, **transition to** "*and then … take it slow*" could result in **a mellower, *albeit not collapsing,* USD**. Moves will be nuanced by Fed policy convergence and other factors leading to policy shocks.

The "*get there fast*" phase: Specifically, in the initial stage (mostly *H1 2022*) of **the "Kokomo Fed"**, where markets are actively pricing in more hawkish outcomes, **UST yields (led by the front-end)** are not only likely to be **upwardly biased**, but set to outpace; resulting in **widening UST spreads**. As a result of which, the **bias may be for a stronger USD supported by interest rate differentials in favour of demand for the Greenback**.

The "*and then … take it slow*" phase: Whereas, transition to the "*take it slow*" phase (*H2 2022*) may align with policy convergence. Which in turn could **at least partly reverse earlier USD strength**; **in tandem with erosion from wider yield spreads** from earlier. And relative equilibrium rates amongst other factors could determine currency catch-up trades against the USD.

Borrowing illumination from the famous Quantum Physicist Niels Bohr, it appears that "**Kokomo" is an expression of *what we can say about policy risks;*** and **not necessarily how policy risks stack up and will play out in reality**.

China: Constrained Cushion

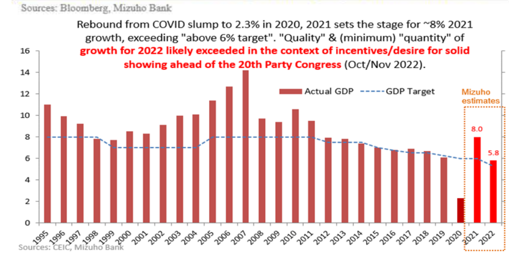
Growth: The **recently concluded CEWC***, which sets the economic policies for 2022, **unequivocally shifted gears to economic stimulus** citing unprecedented **trifecta of growth headwinds** of; i) *demand contraction*; ii) *supply constraints* and; iii) *confidence deficit*. But this is **not** an **unbridled pivot to boost growth at any cost.** ***Instead***, it's best understood as a "*hand-brake turn*" **to avert a hard landing** *but* **whilst adhering to the constraints of financial stability risks** and **"common prosperity"** objectives. A **constrained cushion** that ***falls short of an all-out growth propulsion***; reined in by lingering credit restraint and redistribution. The gravitational pull of structurally lower 4-5% trend growth is a matter of time even if GDP is lifted to ~5.8% in 2022 (possibly above 6%) ahead of the National Party Congress in Oct/Nov; especially **as Beijing may only temper, not trash, regulatory tightening**.

(*Central Economic Work Conference: See Box 2 for details).

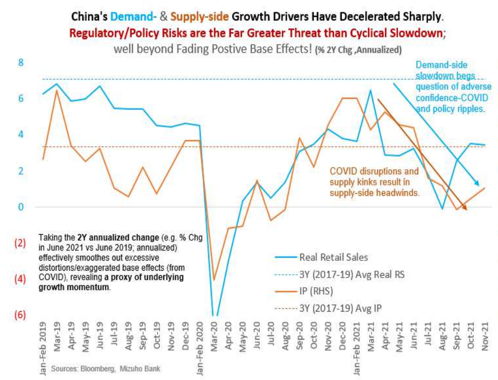
Main Take-Away of CEWC is a Shift to Stimulus

Headwinds to Growth	"Regularity"	Implication
Demand Contraction	Last mentioned in 2015 before the "China crisis". Suggests some severity of downturn.	Policy stimulus to ensure that negative property multipliers are countered via liquidity and offsetting fiscal stimulus to bolster activity and jobs.
Supply Constraints	Not unexpected amid current global supply kinks.	Resolution underway (for the case of the power crunch). On-going efforts to ensure supply-side shocks are buffered.
Confidence Deficit	Never before cited. Likely signals acute policy cognisance of adverse feedback loops (demand-confidence).	Urgent policy stimulus to buttress household and wider corporate balance sheets critical for absorbing potential property sector triggered financial shocks alongside and employment support are par for the course.
Prioritizing "stabilization" in this context suggests ***unequivocal policy inflection to front-loaded stimulus***; but measured in a way not to completely unravel structural reforms.		

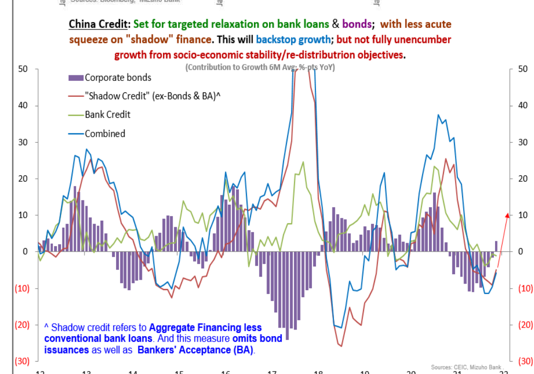
Sources: Bloomberg, Mizuho Bank



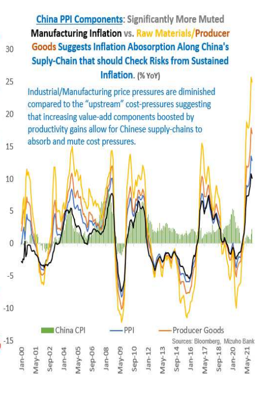
Industry: Despite *"first in, first out"* supply-side activity *revival* since Q2 2020, *amplified by nimble industry adaptations* to cater for global "pandemic demand" – unequivocally boosting China's exports and goods surplus – China's **industrial recovery has faltered**; and remains incomplete vis-à-vis pre-COVID trends. This, mainly as ***exports-led boost to industry is hobbled by negative ripples from property sector shake-down.*** A conspiracy of construction goods/activity setback and a knock back in durable goods demand are likely to hamper unfettered rebound in industrial activity; although **policy focus to boost "priority" industries should backstop**.



Growth dynamics: Accordingly, **credit is likely to be re-channelled to priority industries*** to facilitate consolidation/acquisition of resources and know-how required to make the transition to a high-tech, high value-add economy. But this is ***not an abandonment of financial stability objectives*** that are non-negotiable. Instead, it's a ***re-prioritization of socio-economic objectives*** and attendant ***re-direction of resources that will necessarily entail growth-stability trade-offs***. Case in point being, **property sector stress**, differentiated by developer quality, **may subside but will not vanish**. Whereas ***new industrial capacity*** building and ***public infrastructure*** (with support for LGFVs) will **provide some offset, not a panacea**.

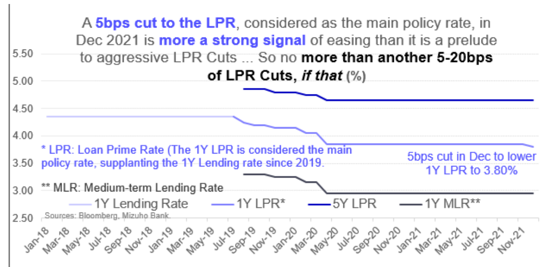


Inflation: **Elevated, but peaking**, will **provide the requisite policy latitude for** outright **easing**. But inflation is not monolithic; with **fairly restrained CPI** (~2% from below 1% for Q1-Q3 2021) **in stark contrast to surging producer inflation** (at 26-year highs ~13% Oct-Nov 2021). Two key reasons why inflation is more likely to subside than flare. First, **energy-led surge in producer inflation is set to subside** as China tackles coal shortage by flexibly adjusting mining and import policies. Second, and crucially, China's **production/supply-chains are primed to absorb cost-push** alongside a stable, if not strong CNY. So, while inflation may be elevated (2022 CPI at 2-3% vs 2021: 1.9%), underlying price pressures would have peaked; allowing growth focus.

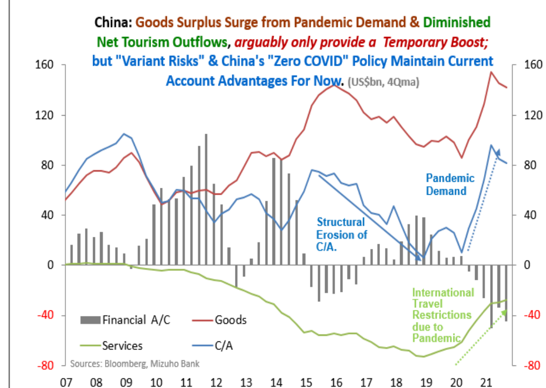


* e.g. AI, Robotics, Materials, New Energy/NEVs, semiconductors, Aerospace, Bio-medical

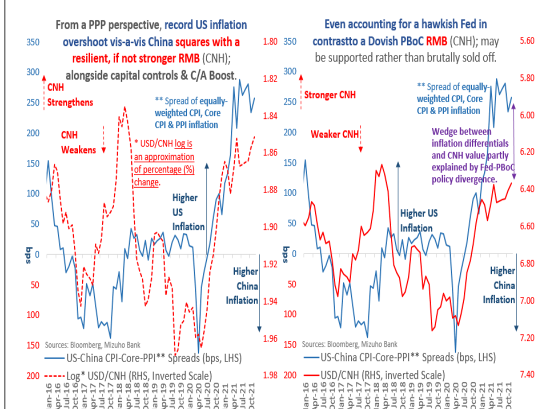
Policy: To be sure, the CEWC had quite unambiguously flagged an ***unequivocal dovish shift***. Which is **precisely why the token 5bps cut in 1-yr LPR** – deemed to be the headline policy rate – to 3.80% **constitutes a tectonic policy signal**. But the critical nuance here is that while **Beijing is pulling *almost* all stops to avert a hard-landing**, it does not desire a rebound built on credit excesses that could come back to haunt with "Minsky" risks. So, aggressive LPR cuts are not the game-plan although modest trims in LPR may be a strategic signal. **Deeper (50-100bps) RRR cuts** instead is a complement to ***re-channeling credit to favoured industries*** **alongside SMEs** (which account for a disproportional share of employment), **SOEs**, LGFVs (for infrastructure) and **"higher quality" private enterprises**, which have stronger balance sheets and better practices generally.



External Position: The **ability to cater for "pandemic demand"** has **boosted** the **Goods surplus** while the **services deficit** – mainly driven tourism outflows – has **significantly diminished with Beijing's Zero COVID border policy crimping outbound Chinese tourists**; resulting in a **strong surge in the Current Account (C/A) surplus through COVID**. This however is **not a permanent reversal of the structural erosion** that had been **underway prior to COVID**. As such, a **gradual reversion to declining C/A surplus is likely** beyond 2022, led by **higher commodity and energy prices** (cutting into net goods balance), followed by **resumption of outbound tourism**. ***US-China tensions re-emerging may also cut into the external balance***.



FX: Admittedly, the **big picture for a strong USD** given an increasingly hawkish Fed, in stark contrast to a dovish PBoC (*especially in H1 2022*) **ought to dampen CNY**. *But without undermining a broadly stable CNY NEER*. Crucially as the **PBoC's *overarching policy of stability encompasses CNY stability***. This is in turn **backed by persistent Current Account surplus** – boosted by exceptional "pandemic demand" goods surfeit and significantly diminished Services deficit as net tourism outflows arrested by the Zero COVID policy – which is **unlikely to reverse abruptly in 2022 amid persistent** "variant risk". Moreover re-shuffling at the Fall 2022 Party Congress will favour a "stable" and slightly buoyed currency. Interestingly, **PPP-dynamics also square with CNY resilience** despite a "Kokomo USD strength" as US inflation persistently exceeds China's.



	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	4.9%	4.1%	4.4%	5.1%	7.0%	6.2%
CPI (% y/y)	0.8%	1.8%	2.1%	2.2%	2.4%	2.3%
Policy Rate^ (%)	3.85%	3.80%	3.75%	3.75%	3.75%	3.75%
USD/CNY*	6.45	6.43	6.60	6.53	6.32	6.33
	6.35-6.58	6.17 - 6.62	6.35 - 6.80	6.37 - 6.87	6.12 - 6.57	6.13 - 6.58

Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

Box 2: China's "Stabilization" is Pseudonym for Stimulus

"Oft hope is born, when all is forlorn" **– Legolas, Lord of the Rings**

China's Central Economic Work Conference (**CEWC**), which was concluded on Friday (10th Dec), **validates** our view of **policy stimulus to pump prime the economy ahead of the 20th National Party Congress** - *where impending key leadership changes under President Xi will benefit from political capital and economic legitimacy.* Accordingly, **front-loaded policy stimulus** by way of ***further liquidity cushion*** and ***positive credit impulse up-front;*** led by local supportive government bond. To be clear this is **neither an abandonment of financial stability** objectives **nor** a frantic **capitulation from structural reforms (property and tech)**. Instead, it is **critical counter-cyclical responses to avert a hard-landing**; underpinning the reality that "*growing the pie*" **cannot be forsaken** as it is imperative to a **more equitable** "*distribution of the pie*". As such, despite structural headwinds pressuring China's potential growth below 5%, **"stabilization" policies in 2022** may ***square with above-trend outcomes that exceed 5.0-5.5%*** (likely to be the official target to be revealed in Q1 2022).
allowing for cost-push to fade.

Main Take-Away of CEWC is a Shift to Stimulus

Headwinds to Growth	"Regularity"	Implication
Demand Contraction	Last mentioned in 2015 before the "China crisis". Suggests some severity of downturn.	Policy stimulus to ensure that negative property multipliers are countered via liquidity and offsetting fiscal stimulus to bolster activity and jobs.
Supply Constraints	Not unexpected amid current global supply kinks.	Resolution underway (for the case of the power crunch). On-going efforts to ensure supply-side shocks are buffered.
Confidence Deficit	Never before cited. Likely signals acute policy cognisance of adverse feedback loops (demand-confidence).	Urgent policy stimulus to buttress household and wider corporate balance sheets critical for absorbing potential property sector triggered financial shocks alongside and employment support are par for the course.
Prioritizing "stabilization" in this context suggests ***unequivocal policy inflection to front-loaded stimulus***; but measured in a way not to completely unravel structural reforms.		

Sources: Bloomberg, Mizuho Bank

Not Throwing Caution to the Wind Altogether

To be clear, the precise wording of headlines from China's CEWC (Central Economic Work Conference), which concluded 10th December, **unequivocally prioritized "stabilization"** rather alluding to unbridled stimulus to ignite headline growth. Moreover, **policy speak has continued to express restraint**, alluding to the characteristic refrain of "common prosperity" that **housing** is "*for living, not speculation*".

This not only confirms our suspicion that cheer about the earlier omission of this line (at the Politburo statements that accompanies the RRR was cut on 3rd Dec) was misplaced, but emphasizes that this is **not a myopic abandonment of structural reforms** (trained at the property sector and the wider economy) and **financial safe-guards**. Rather, this is **policy optimization**; recognizing that "*growing the pie*" cannot be forsaken as it is **a critical pre-condition for equitable** "*distribution of the pie*" fixated on by "common prosperity".

The corollary is that while **property cooling measures may be granted some cyclical reprieve** *skewed to public sector and higher quality private sector developers,* the **structural framework set in place to contain the property sector** (with regards to over-reliance for growth, risks from over-leveraging, unhealthy industry practices as well as self-reinforcing household balance sheet exposure/obsession and price spiral) are **not about to be thrown into an aggressive or alarmed reversal** either.

The tech parallel being, even as funding priority for cutting edge tech (AI, new/alternative energy initiatives, materials technology, high-tech chips, etc.) are promoted, there will be no back-pedalling on oversight initiatives aimed at monopolistic aspects (spanning data, labour practices, and wider anti-competitive impulses) of the tech sector; especially in the "social tech" space.

Distinct Policy Inflection to Stimulus Mode

But that said, the **unequivocal elevation of growth "stabilization" as the policy priority** is in this case policy speak for a **distinct policy inflection from "common prosperity" inspired regulatory and property market crackdown** that knocked growth to sub-5% growth trajectory *tinged with hard-landing risks* (amid brutal self-fulfilling liquidity-turned-solvency crisis for developers) **to reviving growth not just back to trend, but potentially for a marked out-performance**.

Particularly as the **CEWC statements have warned of a worryingly rare trifecta of economic headwinds** from; demand contraction; ii) supply disruptions and; iii) confidence deficit; as the backdrop for warranting "stabilization". Reading between the lines, the assessment of economic gloom is fairly dire. Fact is, the **CEWC has not flagged demand contraction since 2015 and never before fretted about confidence deficit**. It ***therefore follows that the attendant policy response deemed necessary must be emphatic.***

Political Capital From Economic Growth

Especially in the context of the once-in-half a decade key political appointment changes that are expected at the **20th National Party Congress in the Fall of 2022** (likely October). Fact is, for President Xi Jinping, the *desire and political incentive to boost growth is not just conceivable, but in fact compelling*, in the context of the sheer political and economic leverage required to manoeuvre political horse-trading in a machinery as sprawling and complex as the CCP (Chinese Communist Party). The upshot is that **political legitimacy will require a solid enough economic report card** that gives no cause for doubting the direction of the leadership.

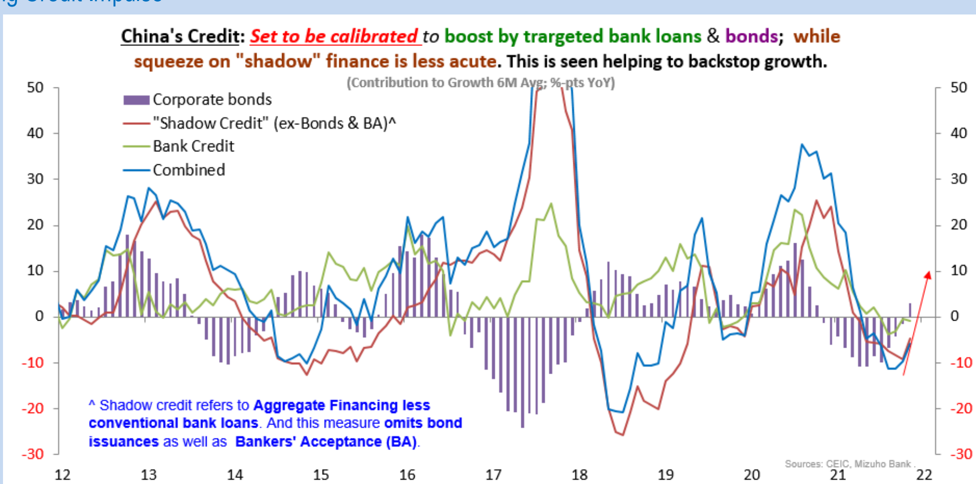
Front-Loaded, but Not Self-Defeating, Stimulus …

Accordingly, **front-loaded policy stimulus** by way of ***further liquidity cushion*** (another broad-based 50bps RRR cut in Q1 alongside 50-100bps of targeted RRR cuts in H1) and ***positive credit impulse up-front*** (boost to local government funding) to complement a ***slower withdrawal of fiscal stimulus*** (led by local government infrastructure and building efforts) are par for the course. But this will be a **controlled and targeted credit impulse**, **not a self-defeating credit bonanza** that results in excesses, mis-allocations and ultimately more acute financial stability risks.

… Targetting (Not Just Targeted) Liquidity …

Apart from **another 50-100bps of targeted RRR** cuts in favour of SMEs/priority industries **in H1**, this will imaginably entail some degree or broad-based liquidity easing as a "catch all" insurance to absorb financial tremors. Thus**, *separate to targeted RRR cuts,* a broad-based 50bps RRR cuts in Q1 2022** (separate from targeted RRR cuts) is also being baked in.

… & Priming Credit Impulse



The necessity to lift the economy off its soft landing may require a **fairly strong, front-loaded positive credit impulse** over and above a **slower withdrawal of emphatic fiscal stimulus**. This features ***local government bond issuances and debt rollover high up on the priority*** list; given the importance of infrastructure and public construction programs to pick up the slack in the property sector. The case for broader, headline credit easing also emerges in the context of existing property sector risks. **While** headline **LPR cuts** have **not** been (and are not as yet) in **our baseline**, the **odds** of this **continue to climb** (~20-25%) alongside the case for MLR cuts (~30%).

Need for Which is Accentuated by Lingering Property Sector Restraints

Especially if Beijing continues to take a sharply differentiated approach to loosening the noose on the property sector, allowing more comfortable refinancing only for SOE and much higher quality POE developers. Point being, with the **overwhelming heft as well as reach (~30% of GDP) of the property sector** means financial ripples from housing related credit shocks may resonate much farther; thereby **requiring Beijing to err on the side of caution in providing liquidity and credit cushion**.

Cushion that will be necessary **given hard-to-predict/quantify balance sheet shocks** across the economy ***if "controlled collapse" of developers*** – given Beijing's conviction to repudiate "too big to fail" complacency by weeding out chronically overleveraged POE developers – ***is deliberately allowed/engineered***.

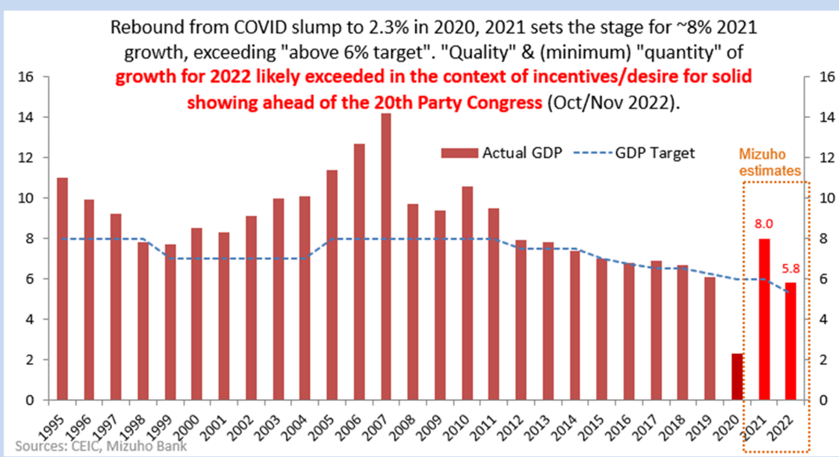
"Constructing" Stability

As undesirable as Beijing may deem the property sector's overwhelming (~30%) share of China's GDP (on a wider measure of indirect contributions), it knows that **going "cold turkey" on "unproductive" property investments is not an option**; simply because it will be impossible to immediately substitute loss of economic support from the property sector. At least **not until offsetting investments elsewhere** are available. And so, **public sector construction**, ***led by resumption of infrastructure programs and affordable housing by SOE developers,*** will **feature prominently as a key backstop for growth.**

Growth Primed for Above-Trend Boost

At, or just ahead of, the People's Congress in March 2022, when the CEWC growth targets are likely to be made known, the revealed **growth target** is set to aspire for ***"quality" as well as a minimum "quantity"***. And so, **in the context of counter-cyclical and front-loaded policy stimulus**, **2022 growth target may be indicated by Beijing to be in the ballpark of 5.0-5.5%**; defying longer-term structural headwinds to growth pressuring potential and current downturn both pointing to growth below 5%.

In fact, **actual outcomes for 2022 likely to exceed with a print around sub-6%**, *consistent with economic outperformance during past Party Congress years (2012: actual of 7.9% vs. 7.5% floor; 2017: actual 6.9% outrun f 6.5% floor).* What's more, Beijing's emphasis on "*investment before de-investment*" **with regards to renewable energy** not only **quells fears of intended activity disruptions and unwelcome "green-flation"**, but also ***reflects the wider wisdom of ensuring a smooth, tried and tested transition*** rather than a rash leap/mis-step that inflicts unnecessary economic pain. Hence, **underpinning considered alignment of economic stabilization**.

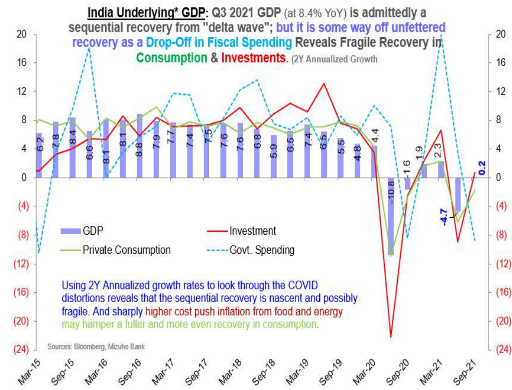


Relief, Not Blank Cheque Rescue

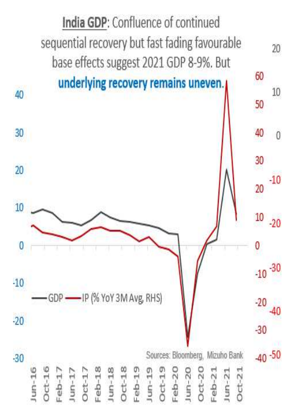
All said, the **CEWC's unequivocal allusion to policy stimulus sooner rather than later**, while not a complete surprise given the predictable need to shore up the economy ahead of the Party Congress in Fall (Oct/Nov) 2022, is nevertheless **a welcome *"Logolas moment"***; revealing *hope born when all was (ostensibly) forlorn* amid brutal regulatory and property tightening into 2021. The **relief is that tail risks of a hard-landing** for the economy have been **nipped**. But the ***reality check though is that this is not a blank cheque rescue for all and sundry*** in the property sector; and as such some wobbles, if not upheavals, are not decisively rued out either.

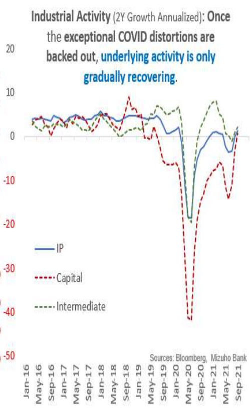
India: Invasive Inflation

Growth: Despite a devastating **"delta wave" in Q2,** the **recovery narrative for 2021 remains intact**; and **sequential momentum** appears **sufficient for** sustained pick-up in activity for 2022. ***But*** 8-9% growth for 2021 is flattered by base effects and overstate underlying 2022 growth momentum. Crucially, **persistent "variant risks"** and **invasive inflation** may **inevitably dampen** nascent and possibly fragile **recovery**; which may remain ***uneven and K-shaped*** (entrenching inequalities). Inflation may undermine lower income consumption most acutely while COVID disruption threatens to displace the most vulnerable grey market jobs. Moreover, **investment slowdown may impede growth multipliers. *Especially as inflation*** *threatens macro/rupee stability and* ***invades policy space***, resulting in subpar recovery outcomes.

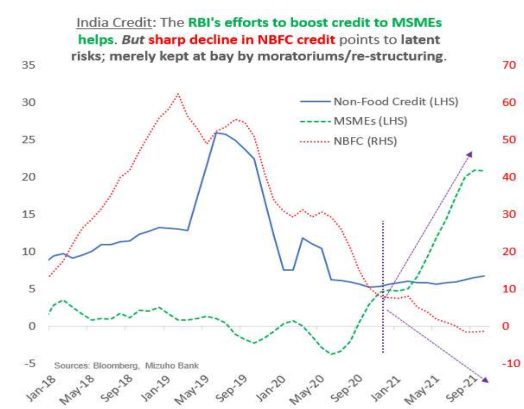


Industry: To be sure, *sharp deceleration in Q3 industrial output is a statistical quirk that misrepresents* what is in fact a ***continued recovery* in underlying momentum**. Which is corroborated by **re-opening factories and resultant improvement in jobs** as well as **capacity utilization**. ***But*** that said, this **recovery is from a soft place**, **subject to an uneven path**. Fact is, stretched corporate balance sheets, exacerbated by global supply constraints, dampen growth multipliers. Especially as **higher inflation**, which invariably erodes profit margins, compromises consumption and crimps scope for stimulus, dampens of industrial activity recovery.

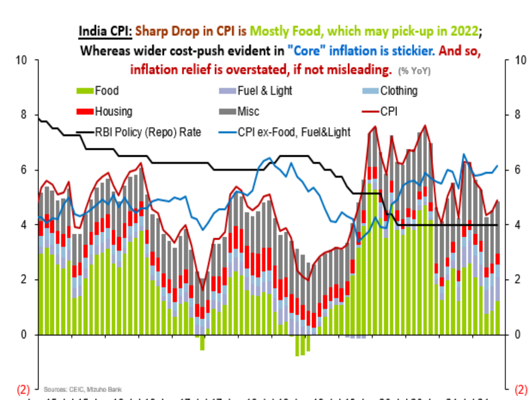




Growth dynamics: **Moderation** in late-2021/early-2022 may be **unavoidable** as **fiscal fade** coincides with, and is compounded by, **elevated inflation**. Fact is, emerging from the worst of the COVID devastation, gentle fiscal consolidation (to ~6.8% of GDP) is not just desirable, but arguably optimal to avert monetary policy over-steer. Especially as **macro-stability risks are accentuated by re-emerging twin deficits**. The silver lining is that credit growth to MSMEs continue to improve encouragingly. But **legacy issues haunting NBFCs** is stark reminder that **recovery is stuck in 'K' mode** segregated along the lines of access (to credit) and exposure to inflation.

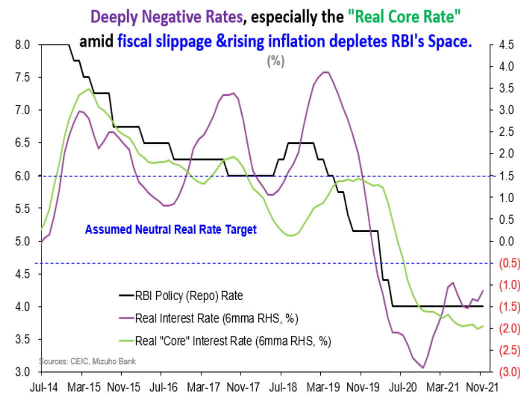


Inflation: Technically, **inflation** remains within RBI's **4-6% target**; well off recent (mid-2021) highs above 6%. But consolation is hollow as **closer examination reveals worry, not relief**. For one, **sharp drop in food** inflation – more an artefact of base effects than softer sequential pressures – **overstates** headline **inflation relief**. In addition, fleeting food inflation points to the **risk of inflation rising sharply in early-2022** as distortions from food fade. A danger already *reflected in core inflation nudging above 6%*. What's more, **energy inflation may be sticky just as food inflation rebounds** (in line with sharply higher global food costs). Upshot being, **inflation will be invasive, cutting into growth**.

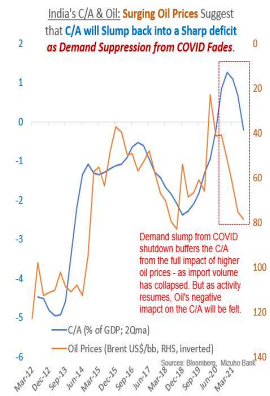


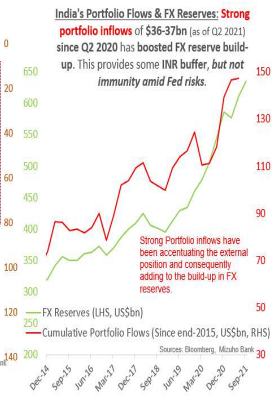
MSMEs: Micro, small and medium-sized enterprises
NBFC: Non-banking financial companies in India, the source of credit surge in the recent past.

Policy: While the **RBI has engineered policy space** by *resorting non-rate policy tweaks* (e.g. liquidity mop up) *in lieu of headline normalization*, it is ***not unaware of growing inflation risks.*** In fact, precisely because of the delicate balance of growth-inflation risks, the **RBI is** attempting policy manoeuvers to buy time. But upside inflation risks and a *hawkish Fed primed for hikes by or before mid-2022,* means the RBI is **on borrowed time**. Especially given that **exceptionally low** (real headline rate), ***if not near-record lows*** (real core rate) **real rates** mean that ***rate hikes delayed translate into macro-stability risks amplified***. Knowing that these risks are best addressed a priori, the **RBI is set to initiate rate hikes in Q1** with more follow-up tightening.

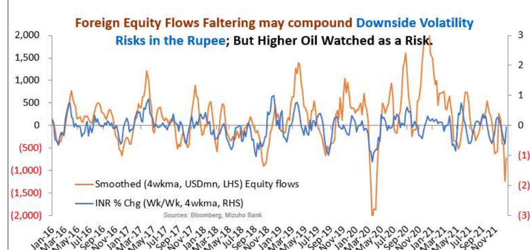


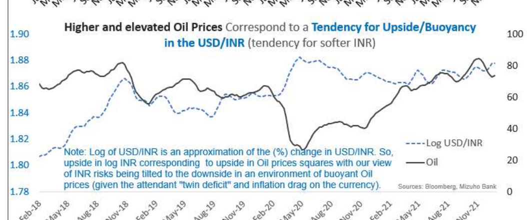
External Position: Although the current account stayed in a **small surplus of 0.9% of GDP in Q1 FY22** (i.e. Q2 CY21), it is **unlikely to sustain** given the **sharp rise in commodity import prices** (led by Oil) of which India is a net importer exacerbated by a domestic power crunch. Indeed, the trade deficit in Q3 CY22 more than doubled versus Q2. Furthermore, **demand pressures will see that import compression wear off,** especially for cap goods, and play catch-up with exports. Even though FDI inflows have stabilized since the lows of 2020, **portfolio flows remain volatile**; and is vulnerable to be exacerbated by a normalization of monetary policy by the Fed and other DM central banks. As such, **balance of payments funding concerns may increase**. The RBI's solid ***FX reserve build-up will offer some buffer, but not immunity***.





FX: With **higher oil prices compounding invasive inflation** alongside a **slip back into "twin deficits"**, the threat of a hawkish **Fed on a rate hike path will accentuate rupee's vulnerability**. Especially **in the context of capital outflow risks associated with negative real rates** in India amid a tolerant, if not dovish-leaning, RBI in contrast to the Fed. That said, brutal, risk-aversion induced **rupee sell off reminiscent of 2013-14 "taper tantrums", is not the base case**. Partly because of a sturdier FX reserve buffer. But this is only a partial cover. More importantly, due to continued recovery helping to underpin risk-adjusted carry returns premised on inflation being subdued into H2. All said, **downside volatility in H1 2022 is par for the course for the rupee, with 76-79 levels in sight**. Late-2022 will however allow for some ground to be recouped back below 75.





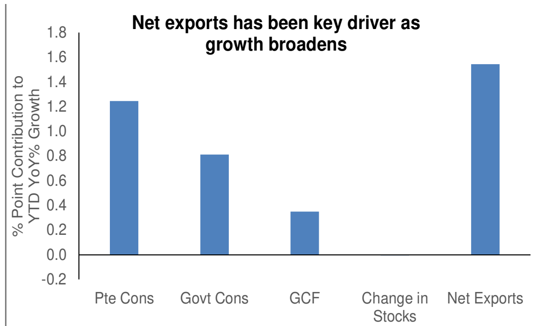
	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	8.4%	5.2 %	5.2%	14.0%	6.8%	6.4%
CPI (% y/y)	5.1%	5.1%	6.2%	6.0%	5.9%	5.7%
Policy Rate (%)	4.00%	4.00%	4.25%	4.50%	4.75%	4.75%
USD/INR*	74.2	75.8	76.5	76.0	74.8	74.2
	72.9 – 74.9	73.1 - 78.1	73.3 – 79.0	73.5 – 78.3	71.4 – 77.2	70.9 – 76.6

Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

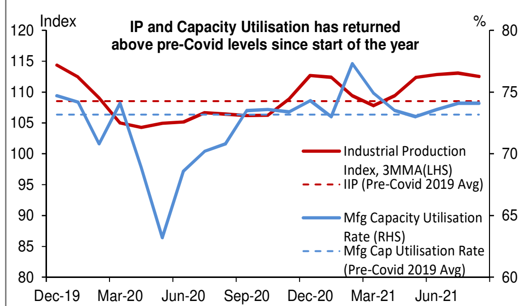
South Korea: Trend Reversion

Growth: GDP growth is estimated at 3.7% in 2021 and will slow closer to 3.3% in 2022, nearer to pre-pandemic trend growth. Exports growth is expected to continue to hold up next year with robust demand forecast for electronics/semiconductors. Consumption recovery which took a step back in Q3 due to social distancing measures, but improve gradually in Q4 and into 2022 with the phased reopening from early November. Downside risks stems from disruptions in supplies of intermediate goods for the manufacturing sector and a gradual slowdown amid China structural shifts.



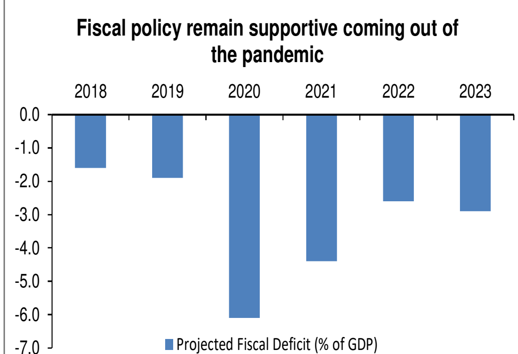
Source: CEIC, Mizuho Bank

Industry: Industrial production has been nursed back to health; **underlying components show both manufacturing and services which constitute more than two-thirds of the index returning above pre-COVID levels.** Likewise, manufacturing capacity utilization stay above pre-pandemic since the start of the year pointing to less slack available in the economy. Cumulative FDI investment pledges and arrivals both displayed healthy YoY growth (>40%) as of Q3 2021. This combined with Korean New Deal 2.0 efforts (8.3% of GDP over 2020-25) bodes well for 2022 investments.



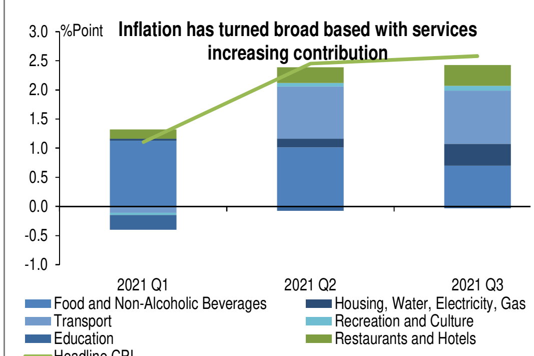
Source: CEIC, Mizuho Bank

Growth dynamics: GDP levels YTD is now 3.2% above the corresponding period in pre-pandemic 2019. Their negative output gap has narrowed considerably since the depths of the pandemic. The upcoming trajectory will hinge on three phase re-opening plan which has a two-week grace period for each phase. While **early fits and starts are likely** as global **re-opening interactions** present uncertain threats, **Korea's above 80% vaccination rate and domestic production of vaccines which ensures booster sufficiency will help keep plans on track, delayed but not derailed**. Fiscal deficit in 2022 is expected to close to -2.6% from -4.4% due to higher revenues from economic recovery; planned expenditure at close to 2021 allocations (which included the supplementary budgets) supports growth.



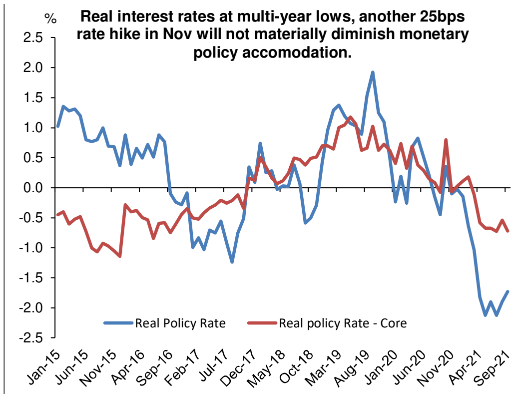
Source: CEIC, Mizuho Bank

Inflation: Headline inflation averaged 2.6%YoY in Q3 given high food and energy inflation, though this may be restrained in Q4 by a 20% fuel tax cut from November to April 2022. Core inflation averaged 1.7% underscoring broadening inflationary pressures as services-related components such as recreation picked up. For 2022, with unresolved supply chain kinks and energy cost passing though, headline inflation will remain elevated in H1 and ease slightly **below 2% in H2 2022 as wage pressures from both higher minimum wage legislated and labor shortages, may prevent inflation from slipping further when energy cost pressures ease.**



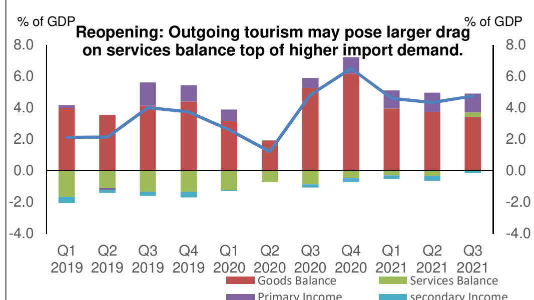
Source: CEIC, Mizuho

Policy: **Monetary policy settings imply exceedingly negative real interest rates of at least -150bps in Q4 even if inflation steadies at September levels**; the two 25bps calibrated increase thus far should be viewed as raising real rates to appropriately align to the current economic conditions. **Into 2022, we penciled in 2 rate hikes in each quarter of H1,** contingent on sticky inflation above BoK's 2% target which necessitates real rate calibrations. Subsequent policy moves leans towards structural considerations of longer term potential growth amid a silvering population and productivity issues. Even as the economy reopens, fiscal policy has also remained agile with measures announced in Q4 to repair impaired balance sheets of small firms and workers in hard hit sectors — important in underpinning recovery though not a huge boost at 0.5% of GDP.



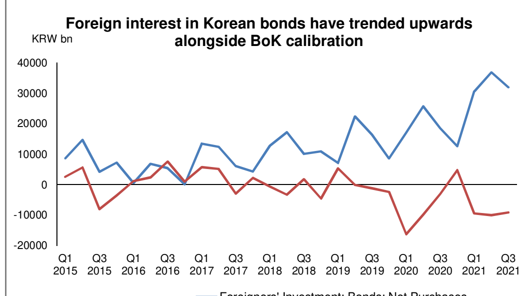
Source: CEIC, Mizuho Bank

External Position: The current account surplus improved from 2020, showing resilience as it stayed above 4% of GDP in 2021 backed by dissipating drag from services balance as freight services improved and technology exports buoyed. The **reopening will improve consumer sentiments boosting goods imports and outgoing tourism and in turn pose drags on the surplus to narrow in 2022.** Continued **FDI investments could support the capital account** amid initiatives such as the Korean New Deal 2.0 and tax incentives to encourage re-shoring and promote investment in strategic technologies (e.g. batteries, semiconductors and vaccines).



Source:CEIC, Mizuho Bank

FX: Further weakness in the Korean Won in Q4 is likely but extent of weakness likely to be capped. The prospects of an early Fed tapering will continue to pose headwinds. **The BoK's rate calibration ahead of most regional peers has boosted interest in Korean bonds and combined with a fundamentally strong current account in 2022 will lean against excessive weakness in the KRW and likely China risks.** We expect USD/KRW will move higher into H1 2022 before easing back lower towards the end of the year, mainly reflecting our USD direction.



Source: CEIC, Mizuho Bank

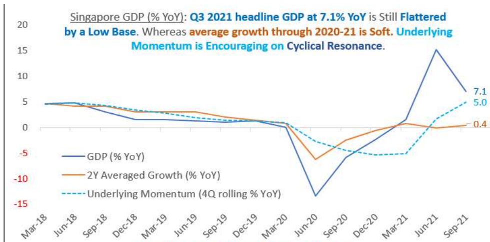
	Q3 2021	Q4 2021	Q1 2021	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	4.0%	3.1%	2.4%	2.2%	3.6%	4.8%
CPI (% y/y)	2.6%	3.5%	2.8%	2.5%	2.0%	1.5%
Policy Rate (%)	0.75%	1.00%	1.25%	1.50%	1.50%	1.50%
USD/KRW*	1184	1200	1250	1250	1200	1150
	1129-1189	1160 - 1250	1170 - 1300	1200 - 1310	1150 - 1250	1100 - 1210

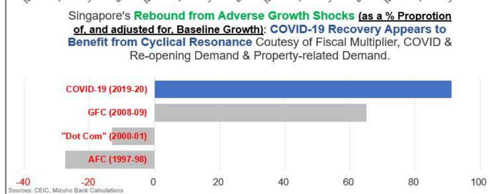
Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

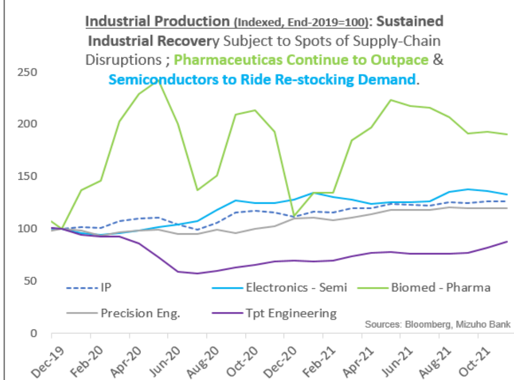
Singapore: Cyclical Resonance?

Growth: A confluence of **exports outrun**, **re-opening demand bump-up**, **fiscal multipliers** and **property-related demand spill-over** have resulted in a **cyclical resonance** of sorts. The resultant activity boost does not merely set the stage for 2021 outperformance with near-7% growth, but also provides tailwinds for fairly robust economic momentum for 2022 growth to land in the vicinity of 4%; convincingly at the high-end of, if not above, Singapore's estimated potential growth in the 2.5-3.5% range. ***But*** that said, **cross-winds from "variant risks", Fed tightening** (to the downside) **and China stimulus** (to the upside) suggest a ***bumpy brand of measured buoyancy rather than unbridled economic boom*** - and so requiring policy to be appropriately tempered.

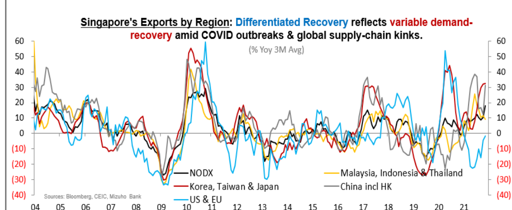


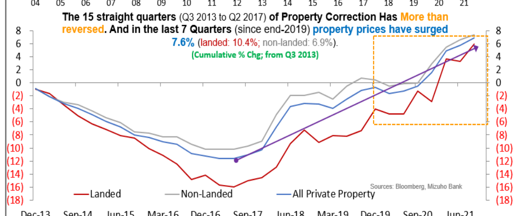


Industry: Continued recovery in global aggregate demand amid lingering chip shortages suggest **manufacturing activity may be fairly buoyed** ***even with fading base effect boost.*** Re-stocking of processor chips and solid biomed demand set these sectors up for continued outperformance. Further pick-up in Petro-chemicals may square with widening resumption in activity/demand alongside more even recovery. **But convergence across sectors** may elude yet, as travel-related/tourism dependent industries remain sluggish and global supply-chain disruptions give rise to intermittent soft spots. More even pick-up may only begin later in 2022.



Growth dynamics: **Despite cyclical resonance** boosting aggregate GDP, **unevenness will not be abolished** as **growth multipliers will not be firing on all cylinders**, as lingering COVID risks, inflation and stability risks conspire. While pent-up demand may be more inclined to ignore a good part of *"variant risks"*, **China's Zero COVID policies may invariably hobble growth boost** - both from *tourism revenues forgone* in Singapore, and crucially, from indirect demand shortfall in regional economies with which Singapore has tight economic links. **Inflation may also dampen consumption multipliers** insofar that disposable budgets are compromised and **macro prudential tightening in response to property bubble risks** could inadvertently result in *credit restraints and caution,* **impairing growth multipliers**.

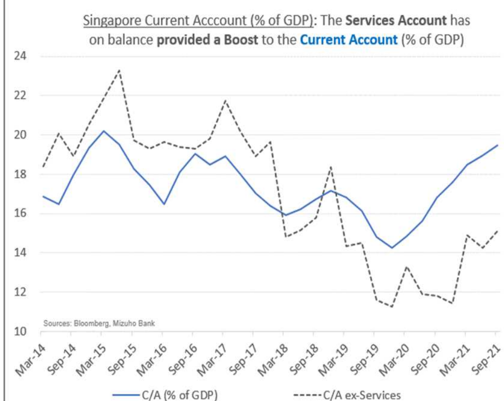




Inflation: Both **headline and core inflation are expected to head higher**, in the **2-3% vicinity for 2022**; with ***tail risks of headline inflation slightly exceeding***. This could especially bear *out if unexpectedly high food inflation compounds higher transport* as well as *energy costs*. The most worrying risk could be if this confluence of cost-push factors conspires with a far more rapid escalation in wages than had been expected earlier. A **particular** risk is sharply higher wages **if COVID** ***wreaks havoc with reinstating cross-border flow of labour*** amid obvious labour supply disruptions. While these are non-negligible risks amid somewhat chaotic manifestation of cost-push factors, the **base case of for inflation to normalize to 1.5-2.0% heading into 2023**.

Policy: But that d**oes not absolve the need for further policy tightening ahead of 2023**. Especially given the backdrop of reasonable outrun in growth, which in and of itself argues for a gradual but sustained removal of policy accommodation. **To be fair**, the **MAS had already gotten ahead of the proverbial curve** in *reinstating a "slight" S$NEER slope* (estimated appreciation bias if 0.5% per annum) *at the Oct 2021 meeting*. With **inflation picking up pace more briskly than expected in Q4 2021**, we now think that despite the pre-emptive move, the **MAS is more likely to have to follow up with an increment to the S$NEER slope** (to ~1% per annum appreciation) **in Apr 2022** (before pausing at the Oct 2022 meeting) *instead of pausing in April and increasing the slope in October.*

External: **Persistent Current Account surplus** continues to be **a feature, rather than a quirk, of the post-COVID recovery**. For one, the chip demand means **both volume and price effects boost the goods account**. What's more, as a re-exporter of refined petroleum, the ability to pass on higher crude prices is a sizeable advantage for maintaining the solid Current Account surfeit. The Services surplus has also picked up amid offshore spending diverted onshore. Meanwhile, **capital reallocation within EM Asia may still benefit Singapore's amid political/diplomatic uncertainties**. Although the Fed's impending tightening remains the key known unknown for capital flows. On the whole though, the **balance of payments position ought to be a backstop for, if not accretive to, the trade-weighted SGD**.



FX: **Although**, that (accretive C/A position) is **not to be conflated with sustained and unchallenged SGD strength** (vis-à-vis USD). ***Not even on account of further S$NEER tightening*** (appreciation bias) being baked in sooner rather than later in 2022. For one, **a strong ("Kokomo") USD will probably set the defining backdrop**, whereby *SGD will defer to, not defy, USD strength*; albeit having scope to out-perform (depreciate less than) most other EM Asia currencies. More importantly, *the S$NEER at the upper half of the MAS trading band* means that *scope for intra-band correction (lower) is significant.* We **expect a softer SGD in H1**, with 1.40 as the initial barrier above, **but USD/SGD poised for a good recovery to 1.32-1.33 in late-2022** as the Greenback mellows.

	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	7.1%	4.6%	2.9%	4.5%	4.8%	4.2%
CPI (% y/y)	2.5%	3.1%	2.6%	2.1%	2.3%	1.4%
FX Policy	Restore a "Slight" S$NEER Slope (0.5% per annum)		"Slight" Increase of S$NEER Slope (1.0% per annum)		Maintain S$NEER Slope (1.0% per annum)	
USD/SGD*	1.36	1.37	1.38	1.37	1.35	1.33
	1.34-1.37	1.33 - 1.40	1.35 - 1.42	1.33 - 1.44	1.31 - 1.40	1.29 - 1.38

Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

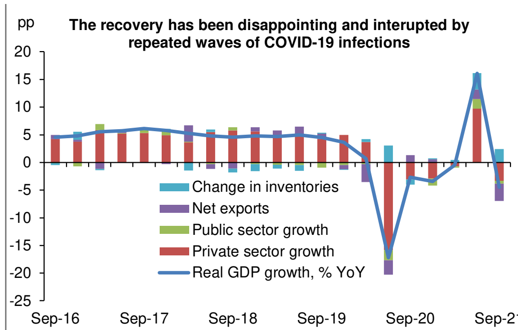
Malaysia: Bumpy Pick-Up

Growth: **The elevated number of COVID-19 cases in Q2 and Q3 which forced the country into differing degrees of lockdown clearly weighed on growth.** Q3 GDP contracted by 4.5% YoY after increasing by (a base effect distorted) 16.1% in Q2. The weakness was broad-based with private and public sector contributions to growth shrinking in Q3, worsened by a drop in net exports despite the tailwinds from commodity prices. On the supply-side, GDP contracted in the manufacturing, services and agriculture sectors. The data for Q4 suggests only modest improvements.

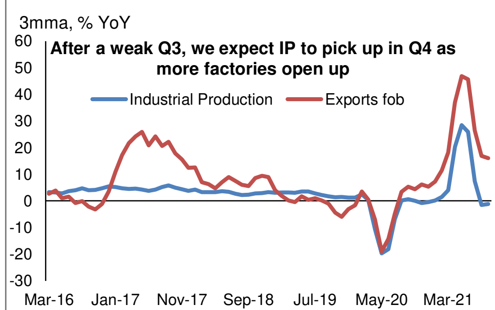
Industry: Industrial production started Q4 on better footing as the restrictions imposed on factory capacity have been eased, after a fairly dismal Q3. **The government is also gradually allowing migrant workers to return to the country.** Although the initial focus was on easing shortages at palm oil plantations, rubber manufacturers have appealed for a quota increase. Furthermore, the tailwinds from commodity prices will likely catch-up as exports look set to gain from these improved price-effects. **However, the recent floods impacting KL and Selangor impact ~40% of GDP,** with the manufacturing sector hardest hit.

Growth dynamics: GDP growth has averaged 3% in Q1-Q3 2021, at the low end of the authorities' 3-4% range for the year, **resulting in us lowering our lowering our 2021 GDP growth forecast to 3.1% from 4.3%.** At the same time, flooding in KL and Selangor threatens to worsen supply chain constraints, raise COVID infection rates and hence pose significant downside risks to Q4 growth. **For 2022, we expect GDP growth to pick-up to 6.0% as higher vaccination rates usher in more tourists, a lesser reliance on social restrictions and ease labour shortages following opening up of inter-state movement.** Fiscal support, following the increase of the debt ceiling to 65% until end-2022, will also play a crucial role in supporting growth. Although the state elections of Melaka and Sarawak were smooth, lingering political uncertainties cannot be ignored given the tight rope the central government is threading.

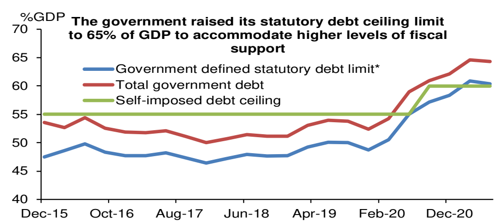
Inflation: Headline inflation averaged 2.2% until September 2021, at the low end of the authorities 2-3% estimate for the full year. With fuel subsidies in place and limited signs of pass-through from elevated producer prices, inflationary pressures may not be as much of a concern for Malaysian authorities despite rising global inflationary pressures. **This, however, cannot be taken for granted if persistently higher PPI inflation is passed through onto the consumers by manufacturers protecting their bottom-line.**



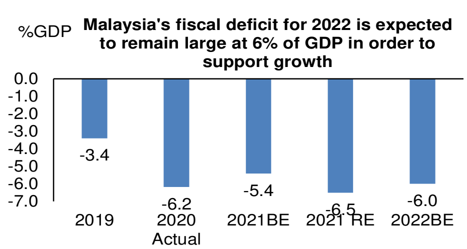
Source: CEIC; Mizuho Bank



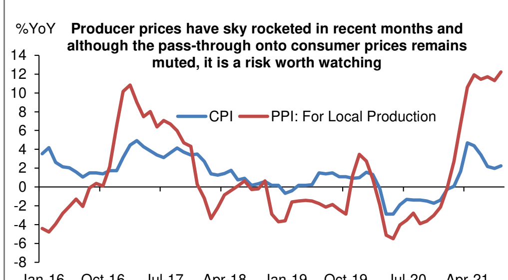
Source: CEIC; Mizuho Bank



Note: *The governments' definition includes MGS, MGII and Islamic T-bills.For the latter, we do not the exact breakdown and proxy it with total T-bills. Data is quarterly; % GDP is a 4 quarter rolling sum figure. Source: CEIC; Mizuho Bank

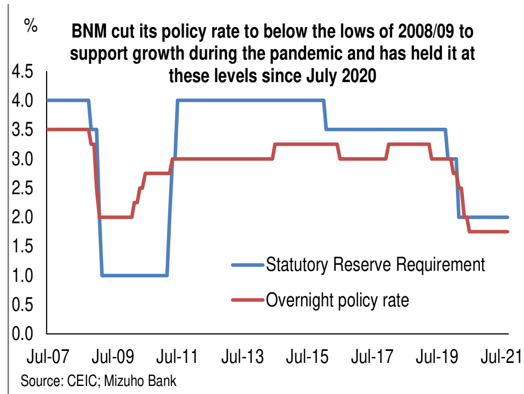


Source: CEIC; MOF; Mizuho Bank

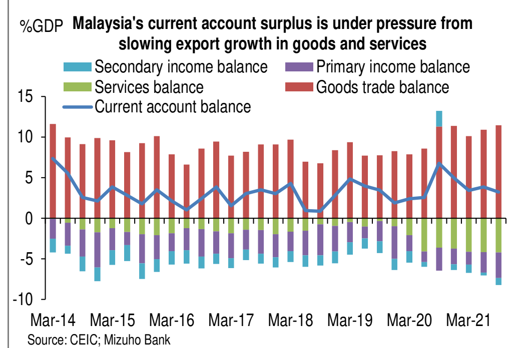


Source: CEIC; Mizuho Bank

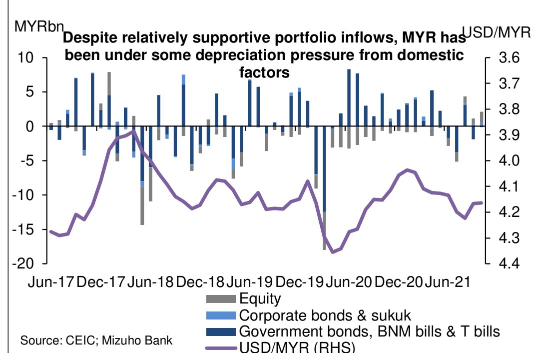
Policy: The unevenness of the economic recovery so far in 2021 has completely justified BNM's accommodative stance, which has complemented the expansionary fiscal policy stance. **Budget 2022 in fact continues to underscore fiscal support for growth while re-balancing expenditures towards capex and allowing for higher government revenue from tax rate adjustments as well as better nominal GDP growth.** **As the recovery becomes more entrenched, we expect BNM will be ready to start normalizing monetary policy settings by Q2 2022.** The risk is that the process could be pushed into H2 if the recovery is threatened by another wave of severe COVID-19 infections.



External Position: **The current account surplus narrowed to 3.5% of GDP in Q1-Q3 2021 from 4.2% in 2020 as the services deficit widened, given the absence of international tourists, more than offsetting the continued surplus in the goods trade balance.** The latter which has also benefited from higher commodity price effects. As the country re-opens to international tourism, albeit gradually, the services deficit should narrow. **But with it, the goods surplus will also narrow as the improvement in domestic demand leads to higher imports.**



FX: MYR has been in weaker position than we had anticipated recently as risks to the growth outlook have taken precedence over tailwinds from commodity prices. Moreover, it seems that oil prices have come off their peak with the US releasing strategic oil reserves. Furthermore, even though the COVID-19 situation has improved significantly since a peak of over 20,000 cases/day in Q3, there are concerns around renewed waves of infections following the floods in KL and Selangor. **These, along with Fed rate hike pressures, will keep USD/MYR on the back foot for most of H1 2022; consistent with a 'Kokomo' Fed outcome.**



	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	-4.5%	3.4%	6.5%	2.8%	8.6%	6.3%
CPI (% y/y)	2.1%	2.4%	1.9%	1.7%	1.7%	1.3%
Policy Rate (%)	1.75%	1.75%	1.75%	2.00%	2.25%	2.50%
USD/MYR*	4.18	4.21	4.23	4.22	4.19	4.17
	4.13-4.25	3.96 - 4.40	4.07 - 4.45	3.97 - 4.36	4.00 - 4.33	4.00 - 4.32

Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

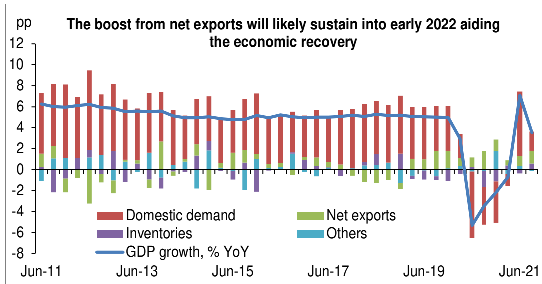
Indonesia: Commodity Tailwinds for Recovery

Growth: Q3 GDP growth slowed to 3.5% YoY from 7.1% in Q2 mainly on account of base effect distortions from 2020. Domestic final demand contributed a much lower 1.8pp to headline GDP growth from 6.1pp in Q2 while the net exports added 1.2pp from 0.9pp in Q2, supported by strong commodity exports. **Abstracting from base effects, we deem that underlying economic momentum is actually looking up with the stringent social restrictions imposed in June/July easing.** Mobility measures have also showed marked improvements supporting the growth recovery.

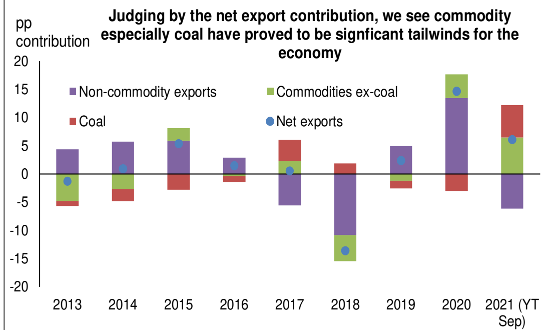
Industry: The run up in commodity prices boosted coal, palm oil and mineral ore exports. By our estimates, the net export contribution from commodities until September 2021 added 12.2 percentage points to the total, more than offsetting the negative 6.1pp net export contribution from non-commodities. **Coal exports, in particular, have got a boost from geopolitical tensions between China and Australia, which have implicitly pushed China to substitute out Australian coal.** This implies that some part of the increase in coal demand could be more structural and last beyond this year; a positive for growth in 2021 and potentially 2022.

Growth dynamics: With year-to-date GDP growth at 3.3%, **we have revised down our 2021 and 2022 GDP growth forecasts to 3.5% and 5.0% from 3.9% and 6.6%, respectively.** Even with an easing of social restrictions following a decline in daily cases in Q3, the recovery in consumer demand may take some time to find solid footing. **Labour market conditions remain weak and household balance-sheets, hit by the pandemic, will take some time to recover.** Moreover, even with the pace of vaccinations improving and air travel gradually resuming, we do not expect tourism to return in a big way until late 2022, weighing on the services sector recovery. **On the bright side, the introduction of the Tax Harmonisation Law, which amongst other things, will raise the VAT rate in 2022 and by 2025 will increase tax revenues and creating fiscal space.**

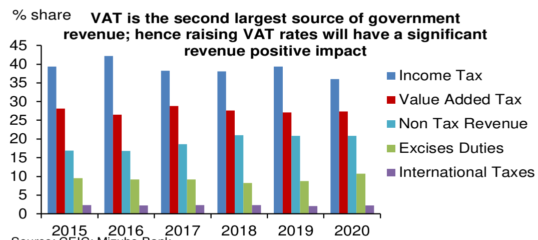
Inflation: Headline inflation was below Bank Indonesia's (BI) 2-4% range for Q1-Q3 2021 and will likely so in Q4. Fuel subsidies controlling retail fuel prices allows for a benign inflation backdrop even as global oil prices rise. ***The quasi-fiscal burden of these subsidies will likely be borne by Pertamina.*** For 2022, we do not expect a big change to the picture; **but the VAT increase will cause a pick-up in headline inflation to average 2.3% from 1.5% this year.**



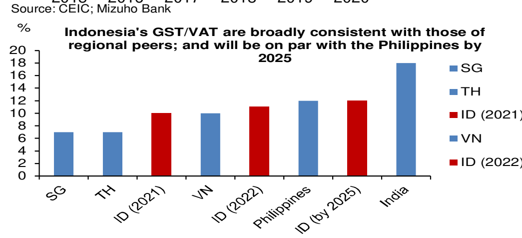
Source: CEIC; Mizuho Bank



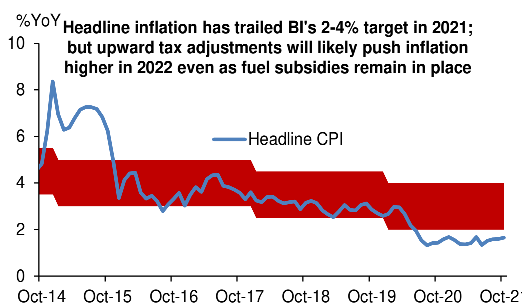
Note: We use SITC 3 digits. Commodites include coal, petroleum, natural gas, palm oil, rubber, mineral ores (inc. manuf. ores). Non-commodites is the residue from the total.
Source: CEIC; Mizuho Bank



Source: CEIC; Mizuho Bank

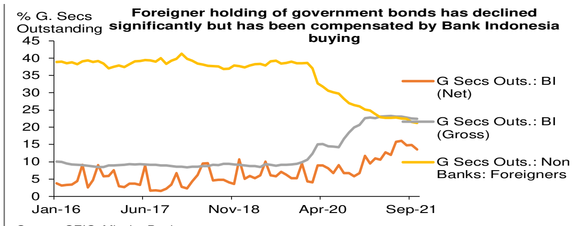


Note: For all other countries apart from Indonesia, GST/VAT rates are as of 2020.
Source: PwC; Mizuho Bank

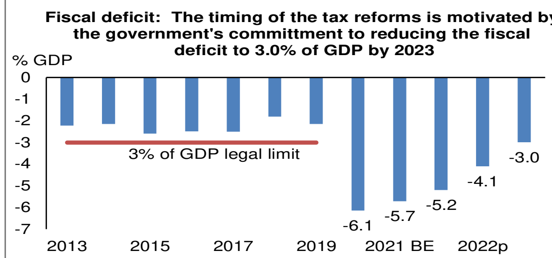


Source: CEIC; Mizuho Bank

Policy: **Government revenues have also got a boost from higher commodity prices.** Even though there is some offset with fuel subsidies firmly in place, the government has narrowed it expected 2021 fiscal deficit to 5.2% of GDP from a budgeted 5.7% of GDP. **Beyond the commodity boost, the Harmonised Tax Law approved in October 2021 will also help structurally improve tax revenue collections.** According to FM, the boost could be up to 1% of GDP allowing for the fiscal deficit to narrow to 4.1% of GDP in 2022. This will ease the pressure on BI to directly finance the fiscal deficit; although the plan will continue through next year. **From BI's stand point, the improved growth profile, fiscal consolidation and a benign inflation allow it the flexibility to raise interest rates only in H2 2022.** IDR stability risks will the biggest risk in terms of bringing forward the timings of these hikes.

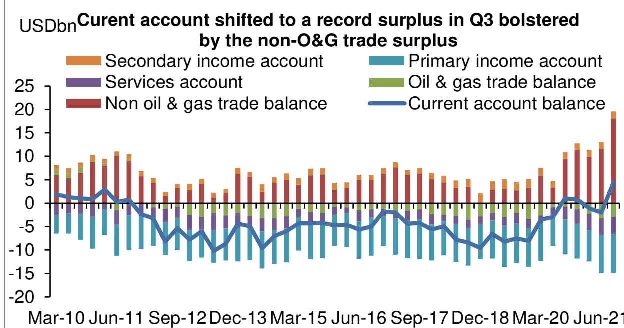


Source: CEIC; Mizuho Bank



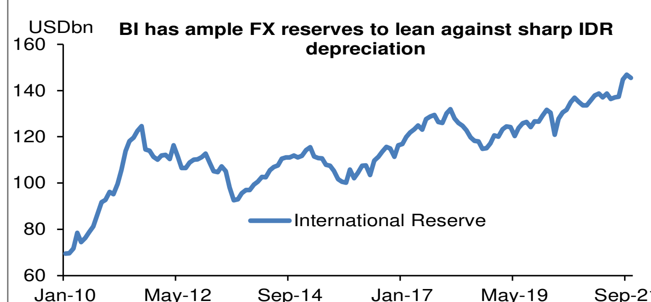
Source: CEIC; Mizuho Bank

External Position: **The solid current account surplus of USD4.5bn in Q3 helped boost the basic balance,** even as net FDI came down. In general, FDI inflows have improved since 2020 but remain subdued nonetheless. Deferring the corporate tax cut that was planned for 2022 may come as disappointment but a general ease of doing business with the introduction of **the 'Omnibus Bill' as well as comprehensive tax package to raise revenues should bolster investor confidence.** Even if FDI is slow to return, Indonesia's focus on boosting upstream manufacturing and pivot away from exporting mineral ores will help raise manufacturing value-add and support durable exports.



Source: CEIC; Mizuho Bank

FX: **IDR stability will be paramount for BI as the US Federal Reserve unwinds its ultra-easy monetary policy stance.** A reduced proportion of foreigners holding government bonds, BI raising its own lines of defense from building on FX reserves to instituting bi-lateral swaps has helped raise confidence that IDR will unlikely depreciate as sharply as it did in 2013 during the 'taper tantrum' episode. But it will be subject to depreciation pressures nonetheless especially during episode of USD strength. **This will be most obvious, in our view, in H1 2022 with USD/IDR popping higher and pushing BI into hiking its policy rate starting H2.**



Source: CEIC; Mizuho Bank

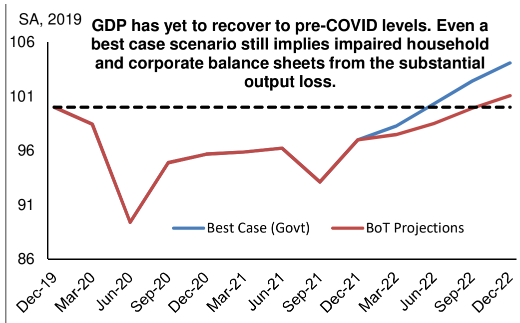
	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	**3.5%**	4.4%	5.7%	3.9%	5.0%	5.4%
CPI (% y/y)	**1.6%**	1.7%	1.9%	2.5%	2.5%	2.4%
Policy Rate (%)	**3.50%**	3.50%	3.50%	3.50%	3.75%	4.00%
USD/IDR*	**14313**	14200	14550	14750	14400	14250
	14182-14568	13840 - 14920	14120 - 15290	14310 - 15620	13940 - 15140	13790 - 14990

Note: Values in black are historical whereas those in blue represent forecasts.

Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

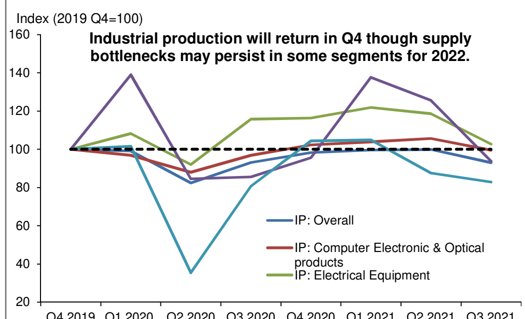
Thailand: Nascent Recovery

Growth: **GDP is expected to come in at 1.2% for 2021 as the economic recovery was severely hampered by renewed Covid-19 outbreaks and the November re-opening output uptick likely to be a restrained one.** A large part of private consumption had been supported by fiscal packages enabled by the passing of two 'Emergency Decrees'. **For 2022, GDP growth is projected to come in at 3.5%, lower end of the Bank of Thailand's (BoT) estimate,** on account of H1 recovery hamstrung by missing Chinese tourists who are more likely to return in H2, in addition to household balance sheets under repair mode and unable to rejuvenate the economy.



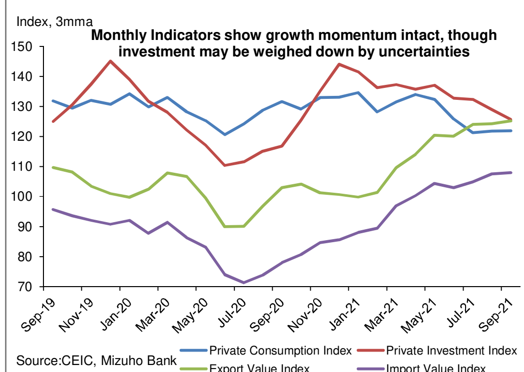
Source: CEIC, Mizuho

Industry: Industrial production took a step back in Q3 as the delta outbreak hit factories, despite the government's sandbox attempts. Notably, automobile production had already slow prior in Q2 as the semiconductor shortage weighed. **This portends a likely divergence into early 2022 as automobile and to a lesser degree electronics lags the rest of manufacturing sub-sectors such as agricultural products.** Recovery in investments may be weighed down with political uncertainties in H2 2022.



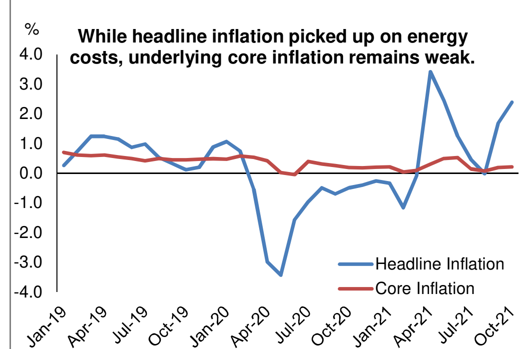
Source: CEIC. Mizuho Bank

Growth dynamics: While a Q4 sequential expansion is likely place, a high degree of uncertainty surrounds the pace of recovery going forward. On the pandemic front, the less than 60% vaccination rate lags behind regional peers. This will **weigh on the travelers' minds hindering the speed of reopening** and heighten the risk of starts and stops. The **resumption of mobility will be set to stress test the healthcare system as foretold by elevated loads on the medical front** in Europe where vaccination rates are higher and in Thailand's case, issues of booster shots and vaccine efficacy may add further complications. **Recovery will be incomplete without the return of Chinese tourists likely only in H2 2022**.



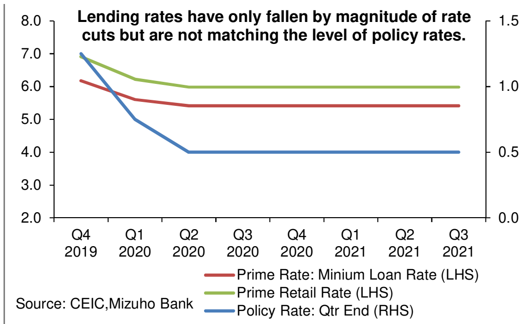
Source:CEIC, Mizuho Bank

Inflation: Headline inflation averaged 1% YoY for the first 10 months of 2021 accompanied by a recent pickup in energy cost as utilities subsidies expired, masking the weak core inflation of 0.2%. **Nonetheless, a cap on diesel prices could serve to cap the headline inflation surge**. Notably, the BoT has managed to achieve their target range of 1-3% as inflation in the two remaining months is unlikely to deter. **In 2022, we expect core inflation to remain contained given large negative output gap absorbing these pressures while headline inflation should comfortably fall within the BoT's range in the absence of energy subsidies.**

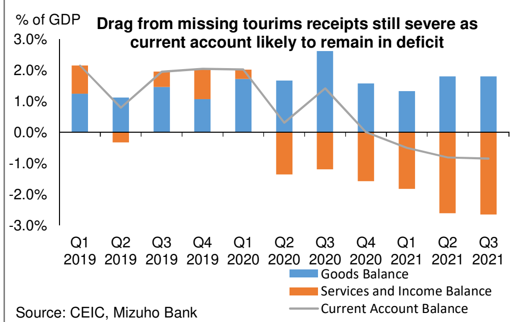


Source: CEIC, Mizuho Bank

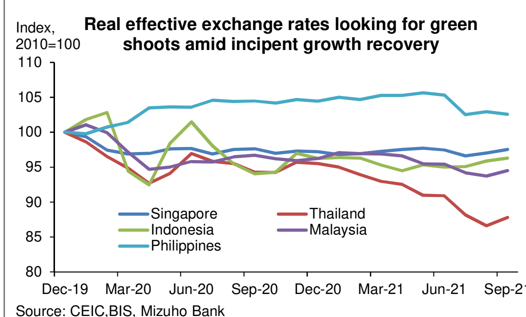
Policy: **With BoT's policy rate at historical low of 0.5% supporting the ongoing recovery, rate cuts are likely off the table** while the bar for any upswing in inflation to trigger a policy response is far higher than regional peers, given that the nascent recovery indicators illustrated above. Against an accommodating monetary background, **fiscal policy armed with the remaining 70% of the THB 500 billion emergency borrowing yet to be disbursed**, will continue to share the stage with the implementation of reopening plans**.** Under assumptions of smooth reopening and Q4 2022 GDP exceeding pre-Covid levels, **incremental policy rate calibration could take place in H2** given lagged effects of monetary policy and leaning against any Fed headwinds.



External Position: **The current account has remained in deficit since the start of 2021 and will likely remain as such till H2 2022,** with the major swing factor being the timing of relaxation of outbound travel for Chinese tourism being after the Winter Olympics in Q1 or the National Party Congress (NPC) in Q4. We expect some easing of travel before the NPC which should see flows of tourism revenue to supplement Thailand's weak current account position. **The weakened THB may provide a slide edge to support goods exports.**



FX: Following the worsening current account, the THB lost more than 9% against the USD since the turn of the year and **the twin deficit position will continue to put the THB under pressure for early 2022** stemming from **Fed's tapering and hike** headwinds. Given the extent of THB depreciation thus far, further slippage from Fed-BoT divergence may be viewed as excessive and "against fundamentals" which leans towards FX intervention rather than an accompanying rate hike. On balance, 2022 will show features of an incipient recovery of the real effective exchange rate as both the nominal THB and domestic inflation embarks on a **gradual** catch up with regional peers as economic activity resumes. H2 2022 recovery will be premised on tourism kick-started and BoT moves.



	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	**-0.3%**	0.6%	1.7%	2.1%	5.2%	5.0%
CPI (% y/y)	**0.7%**	2.5%	2.2%	1.3%	2.0%	1.5%
Policy Rate (%)	**0.50%**	0.50%	0.50%	0.50%	0.75%	1.00%
USD/THB*	**32.8**	33.9	34.0	33.8	33.0	32.0
	32.0-34.0	33.2-35.3	32.8 - 35.5	32.0 - 35.0	31.1 - 34.1	31.1 - 33.0

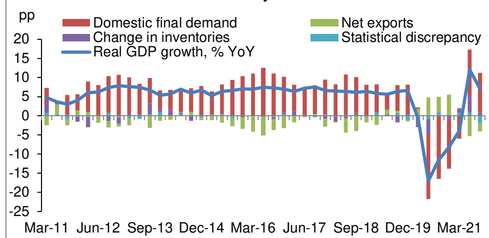
Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

Philippines: Lingering Pains, Growing Dilemmas

Growth: GDP growth averaged 4.9% YoY in Q1-Q3 2021 after sharp drop of 9.5% YoY in 2020, implying that **the economy still has some way to go for real output to reach pre-COVID levels.** The reliance on tighter social restrictions amidst a generally slower vaccination drive has led to a 'stop-start' activity cycle, which is weighing on the economic recovery. **The bright spot was that private consumption, looking at the Q3 print, proved to be resilient even under conditions of tight social restrictions.** However, the mainstay for growth remained government spending.

GDP growth picked up in Q3 with private consumption being relatively resilient



Source: CEIC; Mizuho Bank

Industry: Although the annual rate of increase in IP (by value and volume) has been exponential since April 2021, **the levels suggest that the improvements are modest compared to pre-Covid levels.** Moreover, as of September, less than one-fourth of (responding) establishments were operating at above 80% capacity utilization suggesting **spare capacity remains elevated within the manufacturing sector. This is reflecting as slower goods export growth, which has trailed import growth, and lead to a widening of the trade deficit since the start of 2021.**

Table B. Distribution of Responding Establishments by Capacity Utilization for Total Manufacturing: September 2021[p]

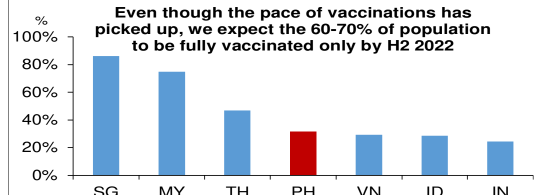
Capacity Utilization	Number of Responding Establishments	Percent Share to Responding Establishments
TOTAL	476	100.0
Below 50%	74	15.5
50% - 59%	65	13.7
60% - 69%	44	9.2
70% - 79%	85	17.9
80% - 89%	98	20.6
90% - 100%	110	23.1

p – preliminary
Notes:
1) Details may not sum to totals due to rounding.
2) Results are based on the responses of establishments which were in operation during the reference month.
3) There were 28 establishments which responded but were not included in the tabulation as they temporarily or permanently ceased their business operations.

Source: Philippine Statistics Authority

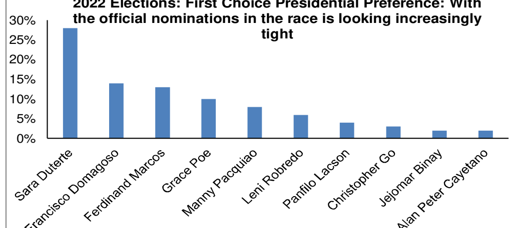
Growth dynamics: **We have raised our 2021 GDP growth forecast to 5% and as a result adjusted the recovery downward for next year to 7.2%.** Pre-election spending boost ahead of the May 2022 Presidential elections, gradual improvements in consumer demand consistent with higher vaccination rates as well as political continuity after the elections (which allows for a sustained focus on infrastructure spending) will bolster the economic recovery next year. Tourism activities will likely resume only in Q4 2022. **The risks, however, are apparent especially since the Presidential race is shaping up to be a closely contested race implying that political uncertainty could persist longer than in our base case.** In addition, **the damage from Typhoon Rai threatens to dampen Q4 GDP growth, especially in the agriculture sector.**

Even though the pace of vaccinations has picked up, we expect the 60-70% of population to be fully vaccinated only by H2 2022



Source: Our World in Data, Philippines Ministry of Health, Bloomberg, Mizuho Bank

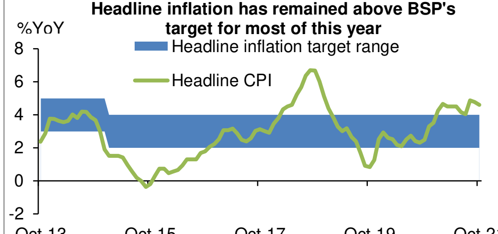
2022 Elections: First Choice Presidential Preference: With the official nominations in the race is looking increasingly tight



Source: Pulse Asia; Survey conducted from June 7-16 2021

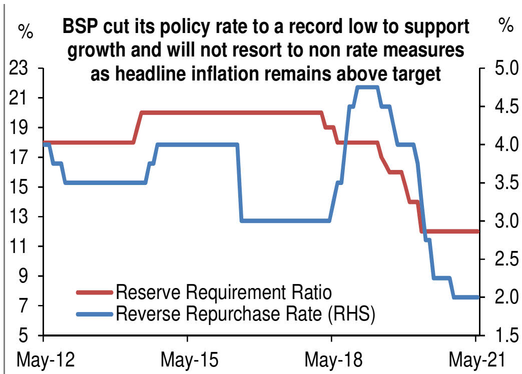
Inflation: Much to Bangko Sentral ng Pilipinas's (BSP) disdain, headline inflation has remained above the target of 2-4% throughout this year. While supply-side constraints from higher food and fuel prices have been the main culprits, we think demand-side pressures and second round effects will play catch-up soon enough. **This will put the BSP in an uncomfortable situation, prompting it to reconsider its accommodative stance sooner than it would have liked.**

Headline inflation has remained above BSP's target for most of this year



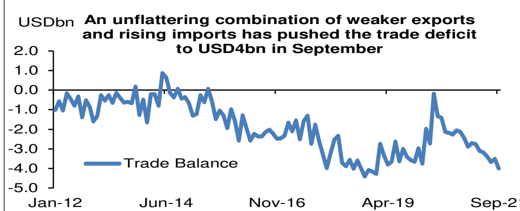
Source: CEIC; Mizuho Bank

Policy: **We expect BSP's unwanted dilemma of improving growth and elevated inflation will push it to hike rates in late Q1 2022.** ***However, the pace of further rate increases will be calibrated and dependent on the data mix.*** Meanwhile, fiscal policy accommodation will likely continue through next year. **Apart from pre-election spending, the government is also working towards gaining authorization to use funds earmarked in the 2021 budget in 2022.** The fiscal deficit for 2021 looks to be undershooting the 9.3% of GDP target for the year, implying that **the government has more room to raise its official target from 7.5% of GDP next year.**

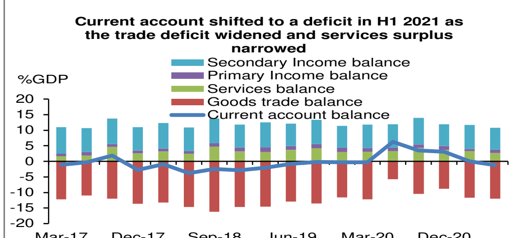


Source: CEIC; Mizuho Bank

External Position: **The current account (CA) position turned to a deficit of 0.7% of GDP in H1 2021** from a surplus of 3.1% in 2020. The worsening of the trade deficit in Q3 will only weigh on the CA deficit further and without any contribution from tourism, we expect a CA deficit for 2021. **This CA deficit will persist into next year as improvements in domestic demand bolster import growth;** this will more than offset any pickup in exports from higher capacity utilization. **With the recovery in tourism only expected to take hold in Q4 2022, concomitant with higher rates of vaccination, we expect the contribution of services exports will remain minimal** (beyond the traditional IT services). Support from overseas remittances will gradually improve and travel restrictions ease.

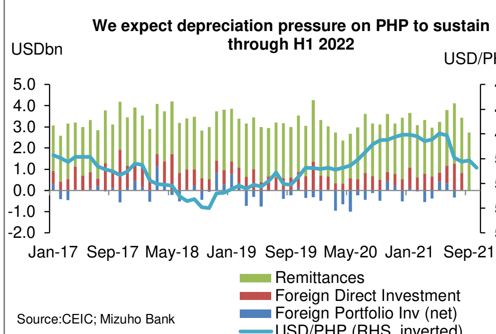


Source: CEIC; Mizuho Bank



Source: CEIC; Mizuho Bank

FX: Although USD/PHP gained some traction in the early part of Q4 2021, **we expect PHP depreciation pressures to persist into the year end and in H1 2022.** A recalibration of US Fed rate hike expectations as well as ECB and other global central banks eventually jumping on the normalization bandwagon will keep PHP on the back foot, albeit with some pressures easing into H2. Moreover, persistently high domestic inflationary pressures and the growing unwanted dilemma that BSP will be faced along with election driven political uncertainty will worsen the situation. **We expect these pressures to be recouped only by BSP rate hikes and H2 recovery.**



Source:CEIC; Mizuho Bank

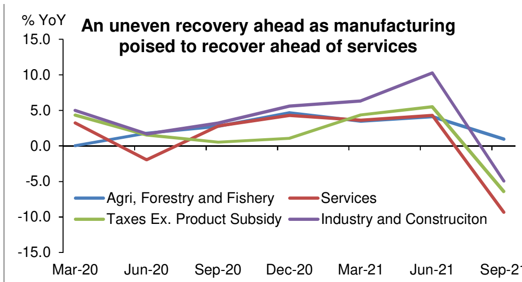
	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	**7.1%**	5.4%	10.0%	4.3%	7.4%	7.5%
CPI (% y/y)	**4.6%**	4.0%	3.1%	3.2%	2.9%	2.7%
Policy Rate (%)	**2.00%**	2.00%	2.25%	2.25%	2.50%	2.75%
USD/PHP*	**50.99**	51.0	51.8	51.4	50.9	50.0
	48.89-51.04	49.3 - 53.2	49.8 - 53.5	49.2 - 53.0	48.7 - 52.5	47.9 - 51.6

Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

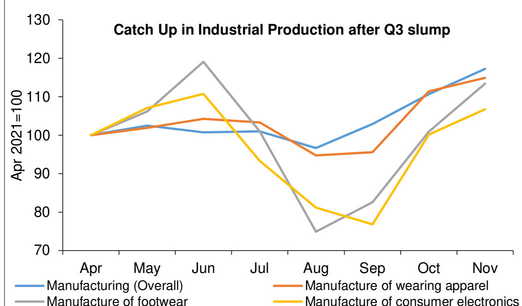
Vietnam: Lagged Divergence

Growth: The Q3 contraction of 6.2% prompted the need for an easing of COVID-19 restrictions which will serve to resurrect the manufacturing and services sectors and support 2021 growth at 2.4%. Although labour shortages restrain the manufacturing rebound, **industrial resiliency with fiscal support (through lower VAT and income taxes which helps to repair balance sheets),** will enable a healthy recovery in this last quarter. On the contrary, low vaccination rates (<50%) will hold back both domestic and foreign spending on services. With **6.0%-6.5% targeted in 2022, its boldness is highlighted by considerations of raising the public debt ceiling.**



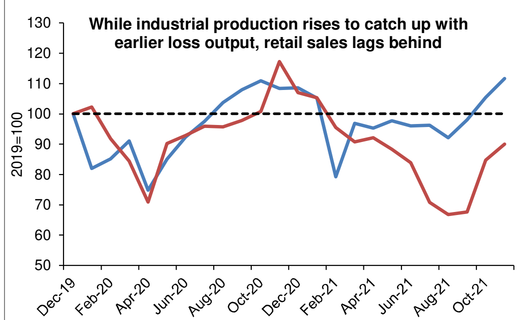
Source: CEIC, Mizuho Bank

Industry: Continued recovery of industrial production will require incentives of higher wages and health assurances to resolve labour shortages. The unevenness theme and asymmetry of the recovery will continue to play out as consumer electronics will face added pressures on semiconductor front. Like the **case for many countries in 2020, we expect the resiliency of businesses together with the government** (vaccination priorities) to maneuver this bump and give support in Q4, though recovery pace in 2022 may slow as **services may continue to lag behind.**



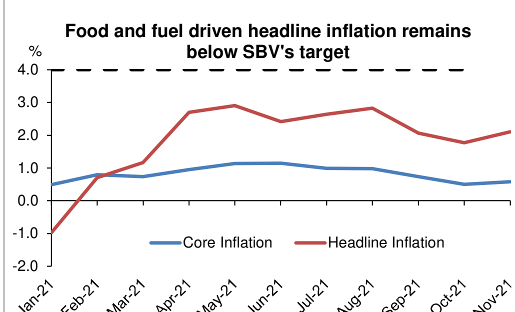
Source: GSO; Mizuho Bank

Growth dynamics: We now expect GDP growth in 2022 at 6%. Despite supply chain woes, the base scenario assumes the **manufacturing sector to continue performing alongside continued FDI inflows as global recovery holds up**. The extent of retail spending contraction in 2021 (measured by cumulative output loss below end-2019 level) stands at 156%; **an approximate loss on 1.5 months of expenditure. This scarring reveals** that even with retail sales back at pre-pandemic levels domestic corporates and household balance sheets may **need assistance** to repair the damage done; aligning with **recent fiscal stimulus** to reduce VAT by 30% and exempting both corporate and personal income taxes for H2 2021.



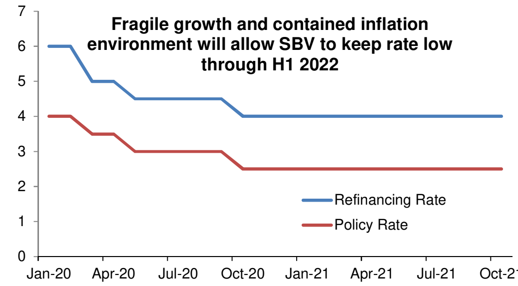
Source: CEIC; Mizuho Bank

Inflation: **Headline inflation remain elevated in Q3 as transport cost rose on the back of higher fuel prices** which were adjusted upward in view of rising crude oil prices. Inflation in Q4 should ease as weak rentals reflect movement out of cities, electricity prices adjust with the season and are kept low via subsidies, though high fuel costs will ensure headline inflation stays above 1% as petrol stabilization fund starts to feel strains (See Box 3). **Into 2022, inflation recovery hinges on tourism return to support entertainment inflation and subsequent multiplier effects on domestic household consumption.**



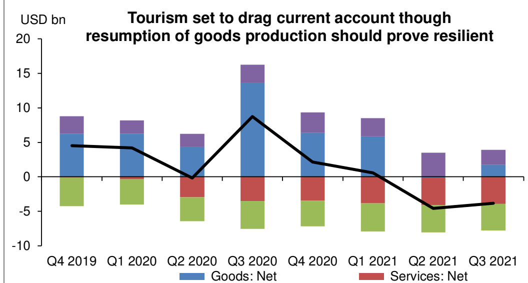
Source: CEIC; Mizuho Bank

Policy: SBV cut its policy rate by 150bp in 2020, taking it to a record low of 2.5%. With **headline inflation remaining well-contained** with a VAT cut offsetting higher energy prices, focus turns to growth recovery after the sharp Q3 contraction, we **expect SBV to keep the current monetary accommodation till H2 2022**, barring any snapback of output in Q4 2021. The SBV will also continue non-policy rate measures such as rescheduling of payments, exempting and reducing interest on existing debt and extending new loans. The magnitude of fiscal deficit will bear watching as the National Assembly contemplates a higher debt ceiling.



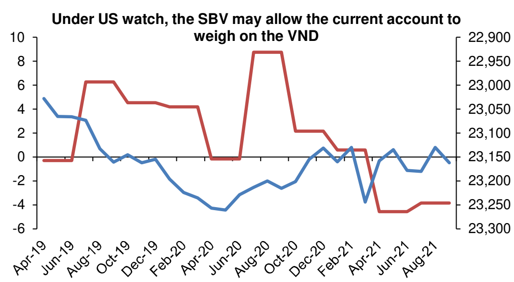
Source: CEIC; Mizuho Bank

External Position: Q3 current account deficit is likely to widen with the lockdown imposed while Q4 should see a narrowing of this deficit. A turnaround of the current account position may be seen in early 2022 when production capacities are restored. Nonetheless, the surplus is likely to be small as **the drag from services will weigh as tourism which contributed 40% of 2019's current account surplus has dissipated**. However, FDI inflows will be set to continue its structural trend amid on-going supply chain reconfigurations. The slight weakness in the current account position may in turn restrain the upside VND in the context of twin deficits.



Source:CEIC; Mizuho Bank

FX: On a more optimistic note, **structural factors will underpin the VND for 2022 as Vietnam is poised to benefit from recent multilateral FTAs**: RCEP, CPTPP and bilateral ones such as the EU-Vietnam FTA. SBV and US Treasury joint statement in July highlighted the need to ensure "an improvement in exchange rate flexibility over time" which may see the current account weakness to come through on the VND. **On balance, the VND is likely to defer to the USD trend,** leaning toward a weakening of the VND as structural factors do not yet present a unanimous upside for the VND.



Source: CEIC, Mizuho Bank

	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	**-6.2%**	4.5%	4.8%	5.5%	9.0%	5.0%
CPI (% y/y)	**2.5%**	2.3%	3.5%	3.3%	3.2%	3.0%
Policy Rate (%)	**4.00%**	4.00%	4.00%	4.00%	4.25%	4.50%
USD/VND*	**22761**	23000	23250	23150	22800	22600
	22734-23073	22700 - 23400	22900 - 23500	22900 - 23600	22700 - 23300	22500 - 22900

Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q3 2021 ranges are from Bloomberg and only indicative.

Box 3: Vietnam's Inflation: Weak Transmission by Design

Global crude oil price have risen significantly in 2021 and in turn result in headline inflation pressures in the US and also in Asia such as Korea and Singapore. This box examines two key features of the price transmission mechanism in Vietnam to understand the subdue pass-through of energy prices to headline inflation.

Vietnam Electricity - Distribution and Coordination

For electricity distribution and sales, Vietnam Electricity (EVN) is the sole state-owned enterprise in charge of transmission. Tariffs are set by the Ministry of Industry and Trade with calibration allowed for EVN to adjust for cost changes. In the event that input cost increase by 3%, automatic adjustments are limited to 5% and any adjustment beyond will require different layers of government approval. This mechanism implies a weakened pass through to consumers.

On inflationary effects of adjustments, it has been telegraphed during electricity price adjustments that the Ministry of Industry and Trade (MoIT) cooperated with the General Statistics office to obtain the impact on CPI and ensure that projections remain below their target. Though at times, estimates might be cut too close to the target as the case in 2019 where the estimated inflation rate was at 3.9%, just below the 4% bound and left less tolerance for changes beyond their estimates in other components such as food, leading to overshooting at times.

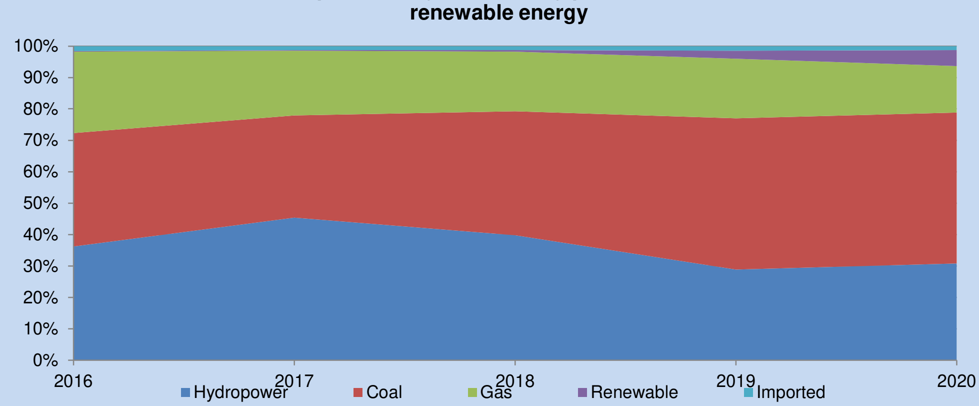
As a state owned company, policy responses via the EVN can be relatively easily coordinated. Over 2020 to 2021, a total of 5 resolutions were passed to reduce electricity prices in response to the pandemic. In 2020, two resolutions for these subsidies cost VND 12300bn (0.2% of GDP). While in 2021, a total of three resolutions with more targeted approach were passed, which cost an estimated of around VND 5000bn (0.1% of GDP). These subsides help to keep housing-related cost low and contain inflationary pressures.

Summary Table: Covid Responses

	Resolution	Discount/ Duration	Target Group
1	Resolution No. 41/NQ-CP dated 9 April 2020	10%/3 months (April to July)	86% of households and manufacturing customers, tourist facilities
2	Resolution No. 180/NQ-CP dated 17 February 2020	20%/3 months (Oct to Dec)	Business related to tourism and health industries
3	Resolution No. 55/NQ-CP dated 02 June 2021	20-100%/7 months (Jun to Dec)	Touris accomodation, Covid medical facilities
4	Resolution No. 83/NQ-CP dated 31 July	10%-15%/2 months (Aug to Sep)	Households living in areas under lockdown
5	Resolution No. 97/NQ-CP dated 28 August 2021	10%/3 months (Sep to Nov)	Selected industries in cities under lockdown (e.g. vegetables and fruits, export entrprises with US$1bn turnover)

Vietnam Electricity – Risks

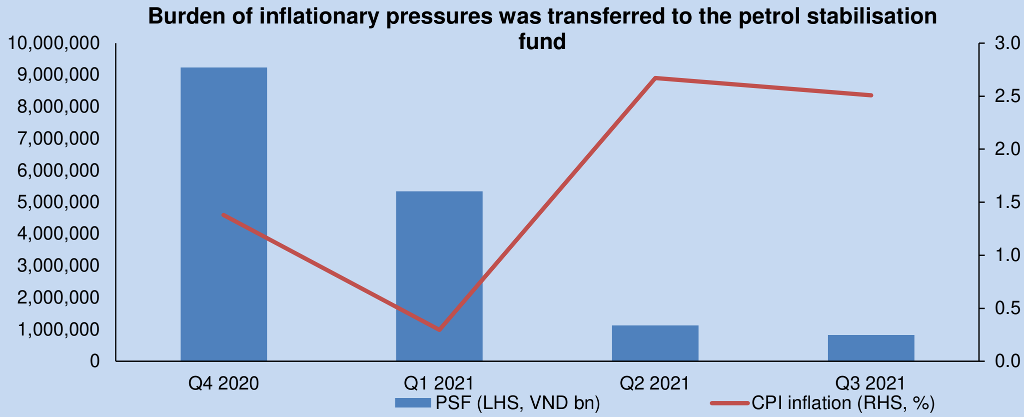
Coal still feature prominently in electricity production with slow rise in renewable energy



Source: EVN; Mizuho Bank

While hydropower remains significant source of electricity generation, lower water levels has resulted in its share declining over recent years. While renewable energy such as wind and solar power gains traction, grid issues prevent appropriate utilization of these renewable sources as solar and wind generation projects take place and are completed at a faster pace than grid expansion projects. This in turn implies a continued dependence on coal amid increasing energy consumption needs as the economy continues to attract substantial manufacturing investments. Greater coal reliance increases their susceptibility to higher coal prices as Vietnam has turned a net coal importer leading to inflationary pressures.

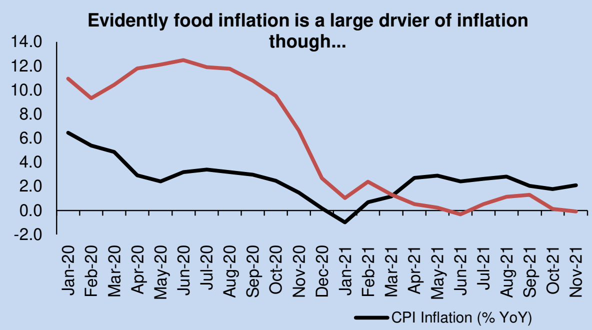
Petrovietnam – Petrol Price Stabilisation Fund



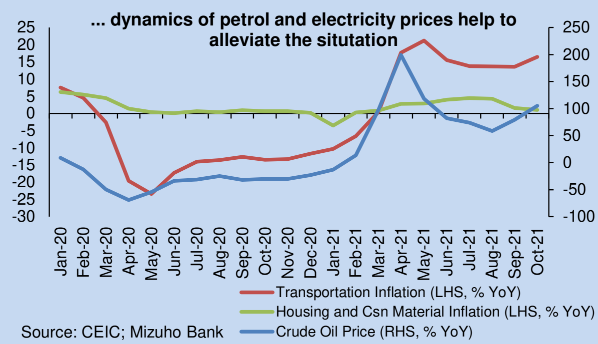
Source: Vietnam MOF; CEIC; Mizuho Bank

In Vietnam, petrol prices are set by the MOF and MoIT are subject to a review every 15 days at the earliest. The petrol price stabilization fund like its name suggest serves the purposes of managing domestic fuel prices. In times when price of oil imports are rising, petrol traders are allowed to draw from the fund to offset the increase in cost to keep prices at level stipulated by the MOF and MoIT. In other times of lower oil prices, consumers and businesses would pay a premium depending on the type of petrol, which then contributes to the fund as the government does not price in the full extent of decline onto retail prices.

This mechanism serves to ensure separation with the state's fiscal budgeting and prevent the escalating crude prices from fully passing through to petrol prices. Nonetheless, escalating global oil prices may see the fund dwindle as in the case for 2021 with the fund shrinking to just VND 800bn (see chart above) as the government tried to keep a lid on inflation with crude oil price averaging 100% YoY over Q2-Q3 while retail petrol price growth averaged 16%.



Source: CEIC; Mizuho Bank



Source: CEIC; Mizuho Bank

With food prices stabilising in 2021, the SBV managed to avert the exceeding the target inflation range, though are already mounting on the petrol stabilisation fund as oil prices remain elevated. Strains were revealed on 25 November when the government established a separate fund for traders to tap on as the authorities adjusted prices lower and allowed only one type of petrol to be subsidized from the existing PSF. The attendant impact on fiscal deficit will be felt through higher expenditures the continued need for sustaining these subsidies or via lower collections as tax cuts via import and excise taxes are being proposed.

That said, EVN continues to record high net profits of VND 14.5 trillion in 2020 and should be able to tide over the periods of elevated oil prices, though declining proportion of low cost hydropower may weigh on margins. Thus, for now, EVN should be able to hold electricity cost low and keep inflation below the SBV's 4% target, barring any escalation of food prices.

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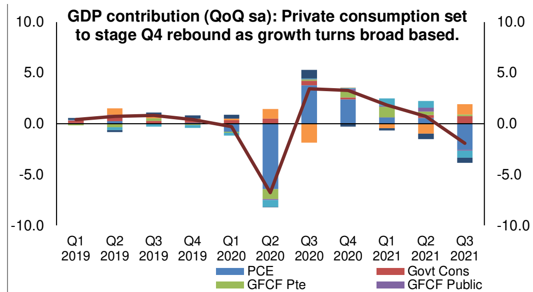
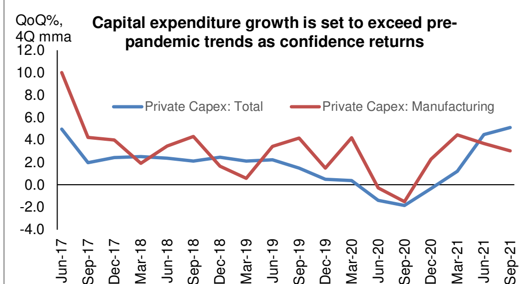
Australia: Of Commodities & Consumption

Growth: Despite the Q3 lockdown induced contraction, Australia's recovery will continue to be supported by commodity exports and reopening consumption boost in Q4, with 2021 growth expected at 4.2% and moderating to 3.7% in 2022. With accommodative monetary policy, this trajectory represents **continued above trend growth, underpinned by US infrastructure push and global recovery supporting more structural (rather than seasonal) commodities demand interacting with favourable terms of trade**. Possible downsides could stem from **China's pivot away from real estate** which could induce a slowdown which **may structurally reduce reliance on Australian exports**.



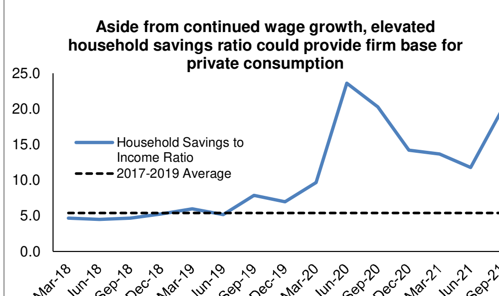
Source: CEIC; Mizuho Bank

Industry: Aside from the global recovery demand benefiting exports, industrial production is set to benefit from the **improved clarity** and certainty on domestic and global re-opening as seen with the fall in Economic Policy Uncertainty Index in turn supporting capital expenditures and corporate confidence. The **still elevated levels** of building approvals in Q3, despite the lockdown induced contraction, bodes well for upcoming construction sector recovery. While industrial and investment recovery translate to "multiplier" effects, recovery on the services front will depend on re-opening to revive tourism and education for critical boost



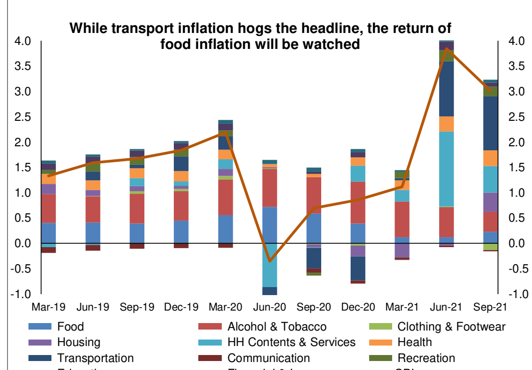
Source: CEIC; Mizuho Bank

Growth dynamics: The potential for drawdown of excess savings continues to be a potential boost for consumption. A silver lining of the **Q3 2020 lockdown** is that in curtailing wider consumption, it imaginably resulted in a significant **accumulation of savings; which now present a strategic backstop for private consumption in coming quarters, even as expiring JobKeeper fiscal support potentially dampens**. That said, the confluence of high vaccinations, and attendant re-opening/resumption of activity being sustained are critical to ensure that underlying jobs recovery supports the consumption backstop from savings.



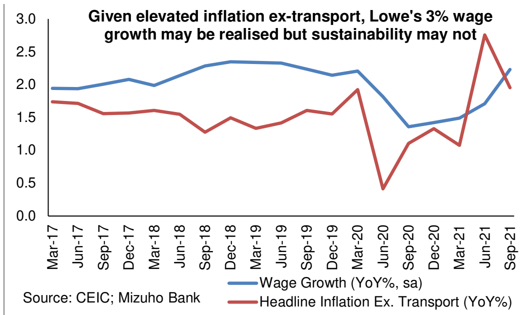
Source: CEIC; Mizuho Bank

Inflation: While energy-related transport component drove a third of Q3's 3% headline inflation (with some base effects), the question is on the **durability** of pickup in **food, alcohol & tobacco inflation which contributed a fifth of Q3 inflation, way below its more than 50% contribution in 2019**. In 2022, as slack in the economy dissipates, wage pressures which are still contained in Q4 may accumulate and 2022 wage growth hinges on two-way feedback from **improved price setting abilities upon reopening**. While our central case at 1.8% represents a return to trend inflation with stable energy prices, an **unfortunate collision of demand pressures with delayed supply easing** may put RBA in a bind.

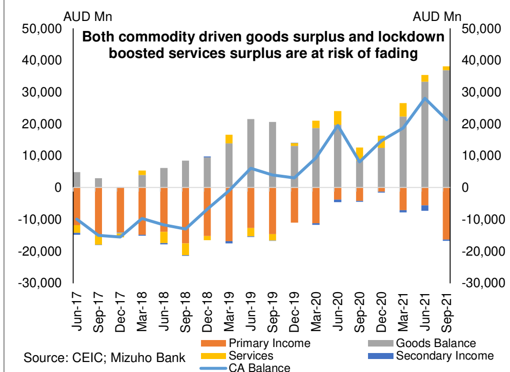


Source: CEIC; Mizuho Bank

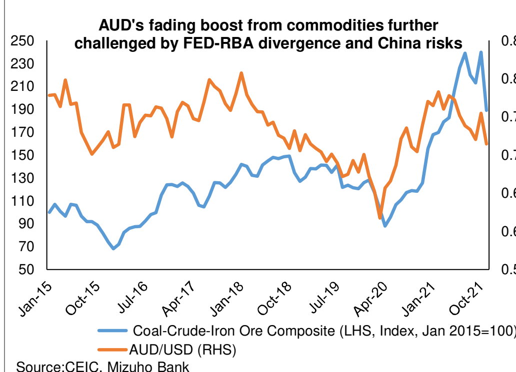
Policy: With "earlier than expected progress towards the inflation target", RBA discontinued the YCC and guides towards **state dependence of** "until actual inflation is sustainably within 2 to 3% target range" and Governor Lowe's hope of 3% wage growth**.** However, RBA stance continues to be dovish and pushed back against rate hikes in 2022, though markets are pricing in hikes from mid-2022. Given underlying mechanisms of wage settings may be tightened by **labour shortages amid reopening demand/disruptions, wage growth sustaining ~3% may give reasons for markets to challenge dovish RBA guidance. But it is not sufficient to force the RBA in a hike for most of 2022. We expect a calibrated 15bps hike to 0.25% in late-2022 before another 25bps lift in H1 2023.**



External Position: Commodities such as coal boosted the goods balance in H2 2021 with improved positive terms of trade from buoyant coal prices. As lockdowns kept Australians within the country, the current account was further boosted by a persistent services surplus. **Into 2022, tailwinds from commodity prices may fade as government supply side interventions curb these undesirable effects.** The reopening of borders will also see a reversion of services balance to a deficit likely in late Q1-early Q2, depending on the pace of bilateral negotiations of travel arrangements and inflow of education services demand. **Overall current account surplus will likely narrow into 2022.**



FX: AUD tailwinds from positive terms of trade, commodity boost (as China unloaded Australian coal on its ports) and RBA rate hike bets which allowed testing of 0.76 were quickly reversed as coal interventions and RBA's YCC drop and dovish push back coincide with Fed's impending taper to push the AUD down below 73 cents. Looking ahead, **while the fading current account surplus adds to FED-RBA divergence, underperformance in early 2022 will be the likely case though global reopening alongside US infrastructure push may underpin and backstop the AUD.** Structural diversification of trade via means such as the delayed EU-AU FTA will be important but hard to achieve due to diplomatic frictions. ***H2 2022 may see potential for AUD catch up as RBA primes for likely end-2022 shifts.***



	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022
GDP (% y/y)	**3.9%**	1.9%	3.8%	1.9%	4.8%	4.2%
CPI (% y/y)	**3.0%**	2.4%	2.1%	1.9%	1.6%	1.8%
Policy Rate (%)	**0.10%**	0.10%	0.10%	0.10%	0.10%	0.25%
AUD/USD*	**0.723**	0.710	0.700	0.713	0.735	0.765
	0.711-0.760	0.673 - 0.756	0.667-0.757	0.661-0.745	0.697-0.777	0.727-0.801

Note: Values in black are historical whereas those in blue represent forecasts.

* Point forecast is for end-period. Q2 2021 ranges are from Bloomberg and only indicative.