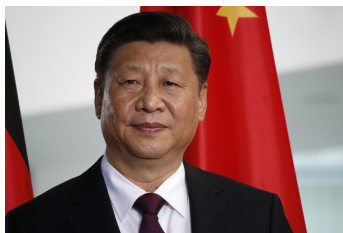


Good MornING Asia - 1 November 2018

Markets are reasonably calm, a little Brexit optimism is in the air, and no one seems too flustered as USDCNY approaches 7.0. But a week could change all that. Friday's US wages numbers may spur thoughts of faster Fed tightening, the passing of the mid-terms may drive up market volatility again and Chinese politicians are worrying about growth

In this bundle



China | India...

All is well - apparently

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By Robert Carnell



Taiwan: Slower growth from trade war could get worse

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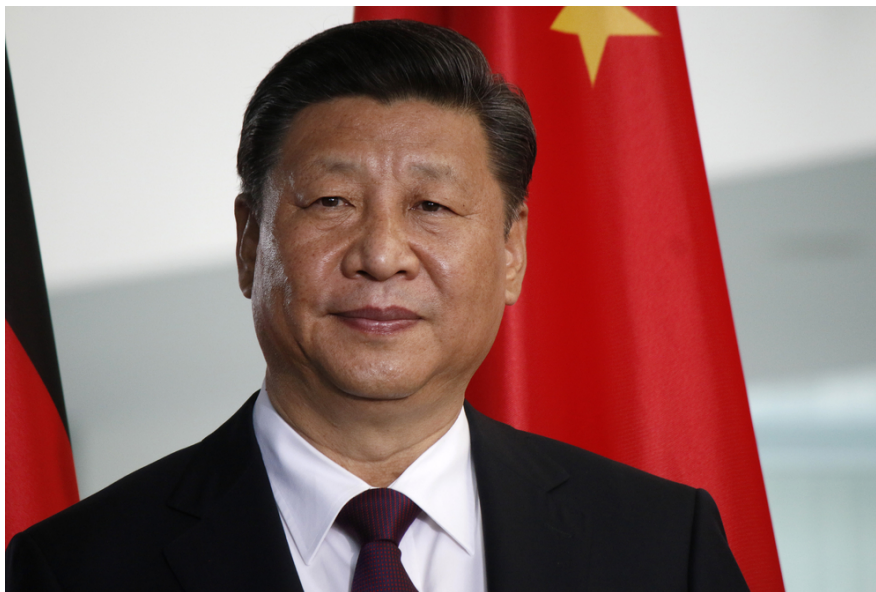
Thailand

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Source: Shutterstock

Asian PMIs - Caixin is the key figure

Amidst a welter of purchasing manager indices (PMI) today, one, in particular, will stand out - the China Caixin PMI. This index is more skewed to smaller private firms with greater international trading exposure. The risk is that it slips into contraction territory (a figure below 50). The consensus view is that it will be exactly 50, completely unchanged from last month's figure. Judging by the official PMI weakness shown yesterday, that seems very optimistic, and if it happens, will not look particularly credible. Our Greater China economist, Iris Pang, thinks it will come in at only 49.5 - that seems more plausible. Though more worrying.

Overnight, China's Politburo, Chaired by President Xi, has said it will take timely steps to counter the slowdown, so it is clearly taking things seriously. Further weakness in today's figures is likely to elicit further comments of support, though the market will likely need to see some hard cash being flashed before it starts to calm down. Chinese media reports that President Xi has stated the importance of developing artificial intelligence (AI) and becoming self-reliant in key technologies. It should also promote industrial upgrades and productivity. Iris Pang is now expecting a very big support package for China's economy and suspects that the absence of any hard numbers just yet may be to avoid giving the impression of an emergency support package - though that is what it will be.

Korean data a bit stronger

After very disappointing Korean production data yesterday, today's higher inflation figures aren't terribly alarming. The headline October rate of inflation is now 2.0%, up from 1.9% in September, but it is all temporary effects from weather-affected food and crude-affected energy prices. Base effects may prevent inflation falling substantially ahead of the New Year, but any further rises from here should be modest and short-lived. No need then for the Bank of Korea to do anything hasty, like hiking rates, though they seem to have an itchy trigger finger, so this risk is never completely absent.

The October export figures were stronger than expected, coming at 22.7%YoY, but the net effect on GDP will still be negative, as imports surged even more (27.9%YoY) and the trade balance narrowed from \$9.565bn in September to only \$6.552bn in October. However, the trade balance is in line with the trend prevailing before September, so it was last month's spike in the surplus that was the aberration, not this month's dip

India - RBI-Government truce, but subject to caveats

In India, the ongoing rift between the government and the central bank (RBI) has reignited weakening pressure on the currency. The USD/INR pushed above the 74 level once again yesterday; the previous breach of this level was after the RBI's rate decision in early October. The rift is caused by pressure on the RBI from the government to ease current tight liquidity conditions and relax regulations governing public sector banks in a bid to stimulate lending and boost the economy in the run-up to national elections in early 2019.

This has set the markets guessing about Governor Patel's resignation. Such an event will indeed undermine the RBI's autonomy as well as raise policy uncertainty, which is going to be even more detrimental for sentiment toward the INR. The government has sought to ease the tension with a statement respecting the central bank's autonomy 'within the framework of the RBI Act', though also noting that 'both the government and the central bank, in their functioning, have to be guided by public interest and the requirement of the Indian economy'. We are skeptical that this will do any good to the INR. We maintain our end-2018 USD/INR forecast of 76.5.

Christmas comes early for UK economists working abroad

If you live and work in a high-cost dynamic Asian country but are still essentially paid in sterling and subject to UK taxation, then Brexit Minister, Dominic Raab's optimism overnight about a November 21 Brexit deal is welcome. Admittedly so far, the GBP bounce is extremely modest. But the alternative is far worse. A positive end to this debacle will avoid seeing your converted salary crumble as your home currency becomes worthless, whilst at the same time, UK consumer prices surge, closing the cost of living gap with your host country. Maybe it will also avoid seeing your home government replaced with one that will tax you even more heavily.

Still, if a deal is in sight, it means that one or other side has probably blinked on the Irish border sticking point, and that is more likely to have been the UK than the EU, which leaves open the question about whether any deal struck can possibly pass the UK parliament. Until that vote is passed, the local currency contract will remain an appealing alternative.

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Taiwan: Slower growth from trade war could get worse

The bilateral trade conflict between Mainland China and the US is hurting Taiwan's exports and as a result, GDP growth. We think the worst is yet to come



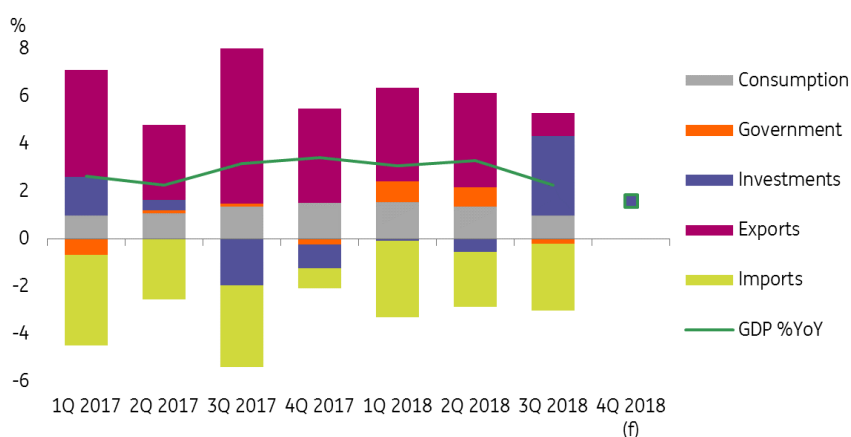
Source: Shutterstock

GDP slows

GDP in 3Q grew at 2.28% year-on-year, close to our forecast of 2.0% but below the 3.3% pace in 2Q and the 3.1% rate in the first quarter. Consumption contributed only 0.998 percentage points, which is a downward surprise to us as we expected spending to prop up the economy during the trade dispute.

Instead, most of the GDP growth came from investment, which we believe is from an increase in inventories (this will be clearer when the data is updated in November). If that is the case, it means that Taiwan growth is worse than the official statistics suggest.

Taiwan GDP by contributors

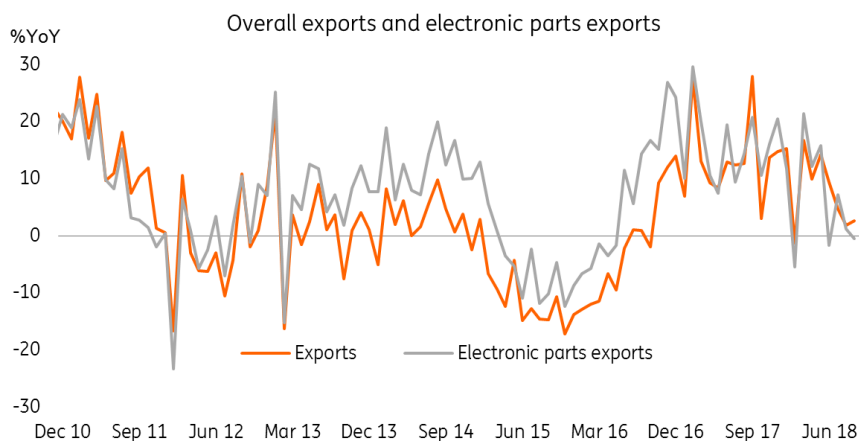


Source: ING, Bloomberg

Trade war hurts exports

Slowing economic growth, especially in exports, we believe is a result of the bilateral trade war between Mainland China and the US. In the past 12 months, Mainland China, together with Hong Kong, accounted for 32% of Taiwan's exports. When China's exports slow down, imports from Taiwan, including electronic materials, slow at the same time.

Exports suffer from near no growth



Source: ING, Bloomberg

Even slower growth in 2019

And we think the worst is yet to come. GDP growth in 4Q18 could slow to 1.6% YoY, suggesting that GDP will grow 2.57% in 2018 overall.

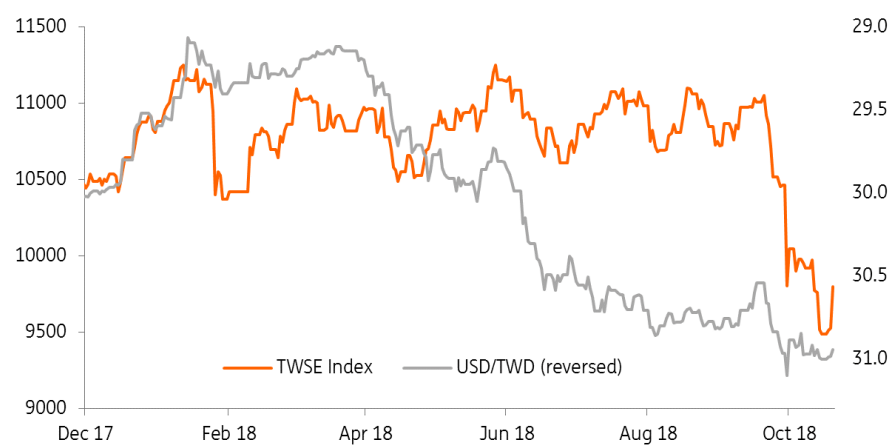
If the trade dispute continues into 2019, we expect Taiwan's exports will be hurt further and GDP growth could slow to 2.0% next year.

Trade war has weakened the Taiwan dollar

The Taiwan dollar (TWD) is weakening against the dollar and hit our 4Q18 forecast of 31.00 earlier this month. We believe that the currency could get some support from foreigners holding more Taiwan equities, which could slow down the depreciation but this won't prevent the currency from weakening. As the Chinese yuan continues to weaken due to the escalating trade war, we expect that the TWD will follow suit.

We maintain our forecast of USD/TWD at 31.00 by the end of this year. And we expect the currency pair to go to 32.00 in 2019.

Recent increase of foreign holdings of equities could slow down depreciation



Source: ING, Bloomberg

Thailand: Current account surplus bounces back into billions

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Source: Shutterstock

\$2.4bn

Thai current account surplus

September

Higher than expected

A huge upside miss led by strong trade surplus

We expected the Thai current account surplus to widen, but not by this much. The \$2.4bn figure was double the consensus estimate. The figures come from the Bank of Thailand balance of payments and we'd gleaned from the earlier release of the customs-basis trade balance, which returned to surplus in September after two consecutive months of deficits, that the current account surplus was rising.

Clearly, the boost came from the goods trade, with the surplus here jumping to close to \$2bn in

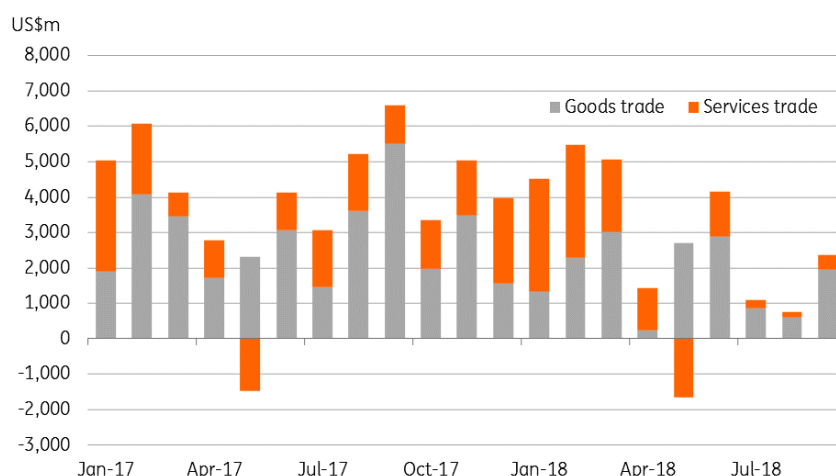
September from \$604m in August. This came off a -5.5% year-on-year export growth, consistent with the customs data, and 14.3% import growth, much stronger than the 9.9% in the customs data.

Slowing tourism weighed down services surplus

The inflows from services, income, and current transfers combined also improved to \$406m from \$149bn. However, inflows on this side have been anaemic compared with a year ago, as you can see in the chart below. Slowing visitor arrivals have most likely weighed down the tourism receipts. The overall payments balance posted a surplus of little over \$1bn in September, more than five-fold increase over the August level.

The cumulative current surplus in the first nine months of 2018 was \$25.9bn, about \$12bn below the year-ago level. Our forecast of the annual surplus narrowing to the equivalent of 7% of GDP this year from over 11% in the last two years remains on track.

Current account balance



Source: Bloomberg, ING

THB has lost its lustre as Asia's outperformer

Although the current account surplus is still large enough to support the currency outperformance, the THB seems to have lost its lustre and has ended the month of October among Asia's worst performers with 2.4% depreciation against the USD, the second-worst monthly performance of the currency this year after a 3.4% depreciation during the June emerging-market selloff. The USD/THB has already traded through our 33.0 end-year forecast. Beyond a transitory relief, we don't think the FX market is likely to take much comfort from today's strong data.

We revise our end-year USD/THB forecast to 33.6 (spot 33.2).

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