

Good MornING Asia - 10 September 2018

The risk aversion continues to be a key theme for the markets as President Trump doubles down tariffs threat to \$267bn of Chinese products, on top of \$50bn already implemented and \$200bn in the pipeline

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Asian MornING Bytes

General market tone: Risk off International theme: US jobs point to Fed Hike, Trump doubles down Emerging markets: Investors await word on the trade front



International theme: NFP points to Fed hike, Trump doubles down

- US labour data continues to point to a tightening path for the Fed as NFP beat the market consensus and wage growth cemented a rate hike in September.
- On the trade front, Canada and the US remain in limbo on discussions, with the Canadian dairy tariff the stumbling block to an agreement. China's trade surplus reported over the weekend hit a nerve with President Trump who pledged tariffs on an additional \$200 billion of goods on top of the negotiated \$200 billion.

EM Space: Market awaits word on the trade front

- **General Asia:** Asian markets will likely remain on the backfoot and await any developments related to the dual trade issues with the US in talks with both Canada and China.
- **Malaysia:** Strong July exports and industrial production data last week suggested that the economy was off to a good start in the third quarter. But weak investment will weigh down GDP growth amid growing anti-foreign investment policy. The government reportedly cancelled three China-backed oil and gas pipeline projects. Markets are on holiday today for

the King's birthday.

- **Philippines:** Governor Espenilla reversed his initial stance to take a more forceful tone, indicating a strong monetary policy response to the inflation surge and reviving Asian financial crisis-era measures to curb speculative trading in the Peso spot market. Trade data will be released on Tuesday with expectations for another \$3 billion trade deficit seen to pressure the spot market higher anew.

What to look out for?

- China CPI inflation 09/10/2018
- EZ ECB meeting 9/13/2018
- PHL trade data 9/11/2018
- US CPI inflation 9/13/2018
- US Retail sales 9/14/2018
- US-China trade negotiations (on-going)
- Argentina-IMF credit line request 09/04/2018 (on-going)

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Report | 7 September 2018

Asian FX Talking: Gauging the fallout

While Asian markets have seen some contagion from the troubles in Turkey and Argentina, the selling has not been indiscriminate. Indeed, some countries in the region have shown signs of resilience. Read our report to find out which currencies we think may be able to withstand the pressure and which are more vulnerable



Source: iStockphoto

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China: Ready to strike back

China is gearing up to respond to an expected escalation in US trade aggression. Counter-measures against US exports and US business interests look likely, while fiscal and monetary stimulus aims to support the Chinese economy



The first train linking China and Kazakhstan is a boost to the Belt and Road initiative

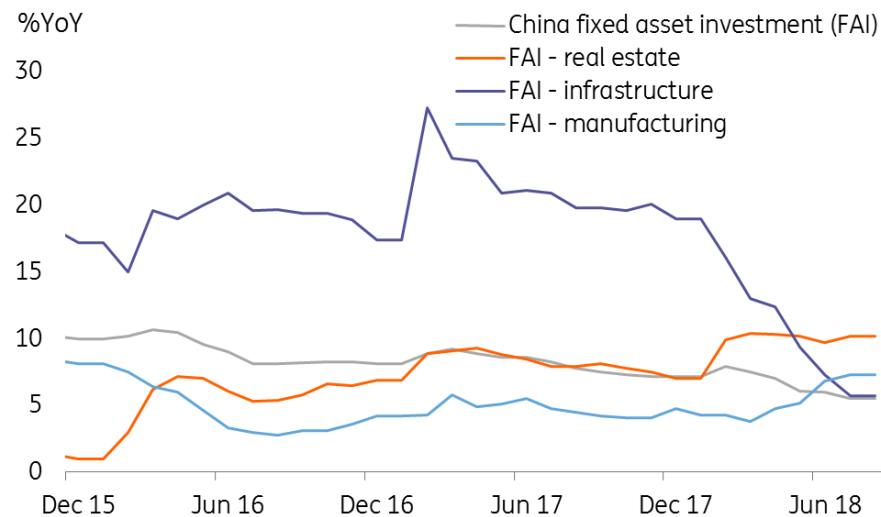
Trade war with the US likely to escalate

On 3 August China's Ministry of Commerce announced a \$60 billion list of goods on which to impose tariffs ranging from 5% to 25%. This came after US President Trump said he would increase the tariff rate on the next \$200 billion of goods to be hit from 10% to 25%. Together with the US's previous tariffs on \$50 billion of Chinese exports, this would mean nearly half of China's exports to the US are covered by tariffs. This will have a major impact on China's export, manufacturing and logistics sectors, and therefore the economy as a whole.

China's retaliatory tariffs will not be enough to match the US like-for-like because China imports much less from the US than it exports. For this reason, China is very likely to impose qualitative retaliation (behind the border obstacles than make it more difficult for US companies to compete in Chinese markets) when the US imposes the next tariffs in order to fully match. The form that qualitative retaliation will take is uncertain, and how harsh these measures will be is also not known. Qualitative retaliation is open-ended in nature, and could create much more uncertainty in the market than simple tariffs.

The Chinese response will depend on how far the US goes with its next round of tariffs. Negative feedback from US companies could pressure the US government to trim the list of goods hit by tariffs, and lower the rate imposed. In that case, China would not retaliate as harshly and the dynamic between the two sides might change for the better. This may lead to risks subsiding gradually.

Chinese fixed asset investment



Source: Bloomberg

Support measures to help the domestic economy

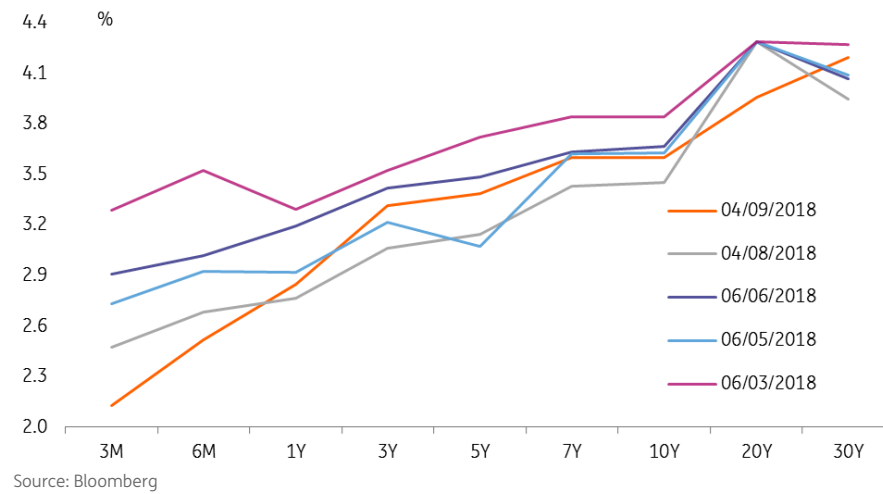
China has put fiscal stimulus and monetary easing in place in order to offset the damage from trade war as much as possible. The front end of the sovereign curve has fallen, suggesting that risks in the Chinese economy are rising.

The State Council announced a CNY2.6 trillion fiscal stimulus package in August, and has also requested that local governments prepare a pool of backup infrastructure investment projects. Fiscal stimulus could increase to CNY5 trillion in 2H18 with another CNY5 trillion in 1H19, particularly if this has to offset the negative impact from the full \$200 billion in added tariffs should the US carry out its threats in full. For China's leaders, keeping manufacturing activities stable so that jobs are secured is a key priority.

In addition, the Chinese central bank (PBOC) has eased liquidity and guided interest rates lower. Liquidity is ample, with a net injection of CNY195.5 billion from the Medium Lending Facilities in August. 3M SHIBOR has fallen from 4.155% at the end of June to 2.878% on 4 September. We expect a targeted required reserve ratio (RRR) cut of 50 bps in October in order to direct liquidity to smaller enterprises and so avoid a liquidity crunch as the export environment deteriorates.

The central bank has also restarted the counter-cyclical factor in the USDCNY daily fixing mechanism which, together with the 20% reserves on short yuan forwards, has slowed the yuan's depreciation.

Chinese sovereign yield curve



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Article | 7 September 2018

Taiwan: Another month of weak exports

It's been another month of weak Taiwan exports. There should be temporary support from handset sales in September but Taiwan's dependence on this industry means the economy is vulnerable to external risks



Source: Shutterstock

Another month of weak export growth

Exports grew 1.9% year on year in August, down from 4.7% in July, while imports grew moderately at 7.9% YoY in August, down from 26.12% YoY in July.

Exports of electric parts grew only 1.3% YoY, which is very slow growth, and integrated circuit exports grew at a mere 0.4% YoY in August from 7.0% YoY in July.

We expect September to be a better month for Taiwan exports because of the scheduled handset sales in the month.

Taiwan's export and manufacturing sector depends too much on handsets

Taiwan's export growth depends too much on the handset industry, and there won't be new handset releases every month, which means the sector is vulnerable to external risks. This underlines our worry on the Taiwan economy that if the US imposes tariffs on \$200 billion worth of

goods and China retaliates, Taiwan's manufacturers would be hurt via the supply chain, although handsets are still excluded from the tariff lists so far.

A weaker currency won't make exports shine

With this backdrop, a weaker Taiwan dollar won't particularly help Taiwan's exports.

The spot price is now at 30.77, and we expect USD/TWD to reach 31.00 by the end of 2018, which is largely a result of a strong dollar due to risk-off sentiment from the escalation of trade tensions.

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Malaysia: Economy off to a good start in third quarter

The balanced economic risks underpin our view of the Malaysian ringgit (MYR) regaining its status as an Asian outperformer once the external uncertainty lifts. Our end-year forecast for the USD/MYR rate is 4.25



Source: Shutterstock

First strong July trade figures and then strong industrial production, both suggesting that the Malaysian economy is off to a strong start in the third quarter. The country's GDP growth is slowing but the economy isn't falling off a cliff. The balanced economic risks underpin our view of the Malaysian ringgit (MYR) regaining its status as an Asian outperformer once the external uncertainty lifts. Our end-year forecast for the USD/MYR rate is 4.25, revised recently from 4.35 (spot 4.14).

2.6% July industrial production growth

Higher than expected

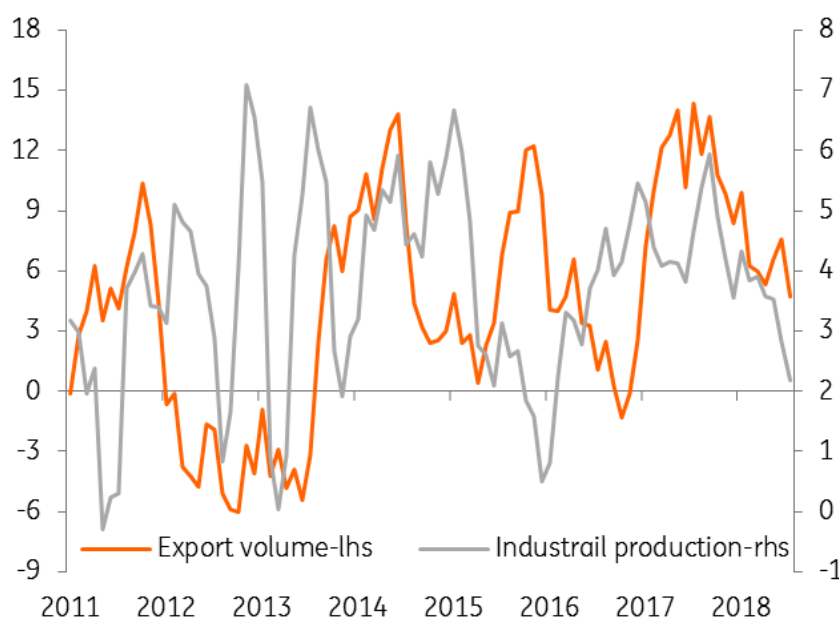
Manufacturing activity firmed up in July

Following on from a surprisingly strong export performance in July, industrial production grew by 2.6% year-on-year in that month, surpassing the consensus estimate of 1.4%. The acceleration from 1.1% growth rate in June comes as faster export growth boosted manufacturing, while utility growth also quickened and mining posted the smallest decline in three months.

Among other manufacturing indicators including sales, employment in the sector and wages, all were firm. The manufacturing sales growth of 9.6% was the fastest since January. So was the productivity growth as implied by growth in sales per employee of 7.6%.

Both exports and production growth are slowing on a trend basis (see figure), which will be associated with the slowdown in GDP growth. However, a sharp GDP slowdown in 2Q18 to 4.5% from 5.4% in the previous quarter was partly a function of the high base-year effect. With the base effect continuing in play in the remainder of the year, we expect GDP growth to settle around 4% in the second half of the year, for a full-year average growth of 4.5%.

Exports and industrial production growth (year-on-year, 3-month moving average)



Source: Bloomberg, CEIC, ING

Balanced economic risks

The commodity currencies have started to feel the heat in the recent emerging market currency sell-off. The MYR isn't spared with a 1.3% depreciation since mid-August, shifting it from being an Asian outperformer to one of the underperformers. Besides emerging market contagion, PM Mahathir's rhetoric against foreign investors should have added to the currency weakness. The central bank (BNM) seems to be accommodating the MYR weakening pressure as long as it's from external factors, while the currency enjoys decent support from the trade and current account surpluses.

We view economic risks as balanced and see no need for any central bank policy support, either for the economy or for the currency.

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