Good MornING Asia - 15 May 2019

Risk sentiment looks set to improve as President Trump downplays trade spat with China

In this bundle

ASEAN Morning Bytes

General market tone: Wait and see. Risk sentiment looks set to improve as President Trump downplays trade spat with China.

-$509m

Consensus on Indonesia's April trade balance

Swing to deficit from $540m surplus in March

EM Space: Trump indicates trade talks would resume and could still succeed

- **General Asia:** Donald Trump downplayed the recent escalation in trade tensions after the two countries traded tariffs, helping lift some sentiment overnight. This positive sentiment may feed into Asia with trade numbers out from Indonesia and India while China reports retail sales and industrial production.
- **Indonesia:** April trade data is due today with the market expecting sustained import compression as the government looks to help limit the current account deficit. Exports are still seen to struggle given the ongoing trade tensions between the US and China despite the recent efforts to bolster the export sector via incentives. A likely swing in trade balance to a deficit in April from a surplus in March may exert additional pressure on the IDR although the central bank has pledged to support the currency.

- **Philippines:** April road vehicle sales continued to struggle with the month seeing only a 0.8% growth as passenger car sales contraction was slightly offset by strong growth of commercial vehicles. Car sales figured in the weaker GDP growth in the first quarter of 2019.

What to look out for: Lots of trade data from Asia

- China's April economic data (15 May)
- EU revised 1Q19 GDP (15 May)
- India April trade (15 May)
- Indonesia April trade (15 May)
- Philippines March OCW remittances (15 May)
- US April retail sales and industrial production (15 May)
- Bank Indonesia policy decision (16 May)
- Malaysia 1Q19 GDP and balance of payments (16 May)
- Singapore April NODX (17 May)

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US-China trade war: What happens now?

China has retaliated against the US tariffs, but only mildly. We believe China could take a more aggressive stance towards the US if it wanted. Meanwhile,...

Source: Shutterstock

Donald Trump, Xi Jinping. President Donald Trump, right, with China's President Xi Jinping, left

Gentle retaliation

As mentioned in our trade research, China's response to US tariff hikes has been relatively mild. The increase in tariffs on $60 billion goods varies from 25% to 5%, which is less than half of the 15% (25% - 10%) increase in tariffs on $200 billion goods imposed by the US.

Why did China respond in this way?

We believe that China wants to refrain from escalating the trade tensions and its response implies that it is willing to continue the negotiations.

What will China's reaction be if the US imposes 25% tariffs on all remaining goods

If the US retaliates by imposing 25% tariffs on all remaining Chinese goods ($339.5 billion, using data of US imports from China in 2018) China might react more aggressively.

For example, as a first step, China could stop businesses from investing in the US. The hot topic of whether China will stop buying US Treasuries depends on whether the US escalates the trade war, but we believe China will reserve this option as the last salvo.

China will step up tax cuts and targeted liquidity easing

As mentioned by Premier Li last Friday (10 May), the government is prepared to cut taxes and fees to further support the economy. We think these fiscal measures will be combined with more targeted monetary easing. The increase in liquidity will put downward pressure on interbank interest rates.

Will China allow yuan to depreciate further?

We think that yuan depreciation is not the answer to boost exports. If export orders fall as a result of tariffs, a small depreciation of the yuan will not help.

In fact, if the yuan depreciates further (USD/CNY spot 6.8817) in a short period of time, it will fuel concerns of capital flight. The central bank wants to prevent this from happening, mainly through stabilising the daily fixing of the exchange rate, so as to send a signal to both onshore and offshore markets that the yuan is stable.

By the time President Xi and President Trump meet at the G20 summit in June, the yuan should stabilise further. We maintain our USD/CNY forecast 6.75 by the end of 2Q19, though we don't rule out increased volatility in the pair in the run up to the G20 meeting.

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