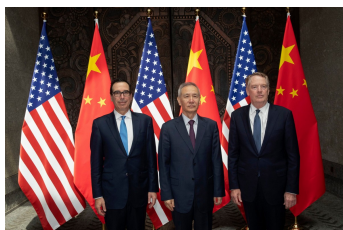# Good MornING Asia - 15 November 2019

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Trade tensions trip Treasuries

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Chinese Vice Premier Liu He, centre, with U.S. Trade Representative Robert Lighthizer, right, and Treasury Secretary Steve Mnuchin before talks in Shanghai

Trade - the dynamics are changing

In recent days, if it wasn't already crystal clear, the over-riding importance of the US-China Trade War for financial markets and the global macroeconomy has become even starker. I had a very enjoyable chat with local officials and other economists at the Ministry of Trade and Industry here yesterday, which highlighted the degree to which this is dominating thinking.

In order to provide further backing for this thesis, I did a quick search for "Trade War indices" online today. By quick, I mean about 30 seconds. Bear in mind that this note is usually put together in about 40 mins from conception to publication - so don't judge me too harshly.

I found this one. It is an ETF based on US stocks that are supposed to outperform the index in the event of a trade war, based on their patronage by the US government. It has the advantage of being quoted daily, though the history of the series is not that long. Given an extra ten minutes, I could de-trend the series (as Treasury yields are stationary over this sort of time frame) and make it even better - I'll update you if I ever get round to that.

Imagine my lack of surprise when it tracked the 10Y US Treasury yield closely. Yes, there is other stuff going on. But if you want to explain the recent journey down to 1.5% and then back almost all the way to 2.0% and the subsequent drift back to 1.8%, then the trade war and a phone with twitter enabled is about all you need.

Recent trade chatter relates to difficulties in agreeing to monthly targets for Chinese agricultural purchases. I think this may demonstrate that China's recent agricultural purchases were mainly an expedient way of dealing with the impacts of African Swine Fever, not really a trade concession at all. The ongoing difficulties about new targets support this. China won't want to be boxed in if it doesn't suit them. But then maybe the US is getting wise to China's tactics in these negotiations. A further story cites White House Adviser, Larry Kudlow, saying that a deal is "close". But we have heard that many times before and without further detail, the market seems to be largely ignoring that.

Where markets previously were prepared to view delay as an inevitable process leading to a deal and trade in a positive fashion, they may now be more inclined to see delay as raising the chances of no deal. The dynamics of this are slowly changing.

Trade War and Treasuries

Source: Bloomberg, ING

Trade ETF and Treasury yields

China economic pressure mounting

Yesterday we got the monthly China data dump, with figures on everything from fixed asset investment to retail sales. Most of the data was very poor and highlight the pressure on China to secure some tariff rollbacks from the first phase of the trade deal, not just some way down the track and with a bunch of contingencies to meet first.

Iris Pang's note details yesterday's data and also concludes that the outcome of these negotiations will be of paramount importance for China's economy Iris' note also raises the role of 5G in 2020. China seems to be forging ahead on this despite the trade war while the rest of the world seems content to blame global uncertainty for doing very little. If the trade war was partly an attempt to keep China from reaching pre-eminence in the tech sector, it doesn't seem to be working.

Day ahead

It's relatively quiet in Asia today. Trade balance data for India and Indonesia today - two of the regions biggest deficit countries, could be important for the performance of the INR and IDR

respectively.

(From Iris Pang): Final data on HK SAR GDP will also be released today. Usually, this data doesn't catch any market attention but given the recent escalating violence level the market will see if there is any revision. Preliminary GDP growth was -3.2%QoQ and -2.9%YoY in 3Q19. We don't expect revision on this data. However, the market may be more forward-looking towards 4Q19 GDP data. After the loss of tourism and consumption activity, Hong Kong may begin to lose exports of education services. For the past few days, foreign students have left Hong Kong presumably due to safety concerns"

(And From Prakash Sakpal): Malaysia's increasingly weak activity data in recent months followed by the central bank's (BNM) surprise easing (50 basis point reserve requirement cut a week ago) -- have all prepared markets for a bad third-quarter GDP report today. We have recently revised our 3Q GDP forecast from 4.8% to 4.4%, which is also the consensus median. We expect a further drift lower to 4.1% in the last quarter of the year, which we hope to be the low point in this cycle. We believe the BNM easing cycle has further to go with at least 50bp more policy rate cuts, which we have pencilled in for the first quarter of 2020"

Out in the G-7, US October retail sales will be an interesting read. The US economy is being kept going thanks to the resilience of the US household sector and their continued spending. Business investment is in contrast, in decline. So any sign of retail spending weakness (consensus is for a 0.2% MoM headline and 0.3% "control group" - strips out a lot of the volatile bits) would be unexpected, and therefore alarming.

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ASEAN Morning Bytes

With investors increasingly wary over the fate of the US-China "phase one" trade deal the week might end with a more volatile trading session...

4.4% Consensus on Malaysia's 3Q GDP growth

Down from 4.9% in 2Q

EM Space: Elevated trade anxiety

- **General Asia:** Much weaker than expected Chinese economic data yesterday adds to increasing anxiety about the ongoing trade negotiations between the US and China. Investors will be looking to US retail sales later in the evening and regional growth numbers for further direction.
- **Malaysia:** An increasing weak activity data in recent months followed by central bank's (BNM) surprise easing via a 50 basis point reserve requirement cut a week ago -- all of this has prepared the markets for a bad third-quarter GDP report today. We have recently revised our 3Q GDP forecast from 4.8% to 4.4%, which is also the consensus median now, and a expect further drift lower to 4.1% in the last quarter of the year, which we hope to be low in this cycle. We believe the BNM easing cycle has further to go with at least 50bp more

policy rate cuts as what we have pencilled in for the first quarter of 2020.

- **Singapore:** October non-oil domestic exports figures coming out early morning on Monday will be a key indicator of where the economy is headed in the final quarter of the year. The consensus of accelerated NODX decline (-10.1% YoY vs. -8.1% in September) doesn't sound good. Judging from persistently big declines in semiconductor exports from other Asian countries in October, electronics likely remained a drag on NODX. As such, any recovery in Singapore's GDP growth in the last quarter of 2019 looks to be far-fetched.
- **Indonesia:** October trade data are expected to show continued contraction in both exports and imports contracted in the last month. While the trade war has been depressing exports, the government's drive to cut back on trade and current deficits is weighing on imports. That said, the consensus is still looking for a near-doubling of the trade deficit to $300 million in October from the previous month.

What to look out for: US retail sales

- Malaysia GDP (15 November)
- Indonesia trade (15 November)
- Thailand GIR (15 November)
- Hong Kong GDP (15 November)
- US retail sales (15 November)
- Philippines OF remittances (15 November)

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Asia week ahead: Export slump continues in final quarter

Trade data stands out in an otherwise light economic calendar in Asia, while the US-China trade noise will remain a key driver for markets in the week ahead

Source: Shutterstock

➡ No export recovery in sight

Next week in Asia kicks off with the release of Singapore's trade figures, in which the focus typically is on non-oil domestic exports. We will also get trade data from Japan, Taiwan and Thailand over the course of the week. All of these being October figures, they will be probed for signs of an export-led recovery in the reporting countries.

Against frequent negative and positive swings in rhetoric, the US-China Phase One trade deal remains far from becoming a reality. So too is the recovery in Asian exports, which is being held

back by weak electronics demand globally. This is why we aren't expecting any positive news in the forthcoming trade data aside from some signs of bottoming.

Also making headlines on Monday morning will be Thailand's GDP report for 3Q. We think recent events – the Bank of Thailand policy rate cut last week followed by signals this week from a top central bank official about a further downgrade of the growth outlook and further room for easing – could be a prelude to a bad GDP report. So markets may be in for a disappointment if they go by the current consensus view of 2.8% 3Q GDP growth, up from 2.3% in 2Q. We, on the other hand, are looking for a slowdown to 2%. Even so, we don't think the BoT will cut rates again in December.

Not enough policy room either

A slew of price data – producer prices from Korea and consumer prices from Japan, Malaysia and Singapore – will be read in light of central bank policies in the region. Inflation hasn't been an issue in the majority of Asian countries. And unless we see a severe food price shock (for example, much worse spread of swine fever, or disruptive weather conditions, etc.) or a fuel price shock (geopolitical risk in the Gulf region), we don't see inflation becoming a problem through 2020 and perhaps beyond.

But with the central bank policy rates in most regional countries close to their record lows, the room for additional easing is limited. Bank Indonesia, which meets next week, still enjoys some policy space and may be inclined to ease after a surprising dip in inflation in October while growth has been stuck at the 5% level for the last several years. However, BI may follow its Philippines counterpart (BSP) by leaving policy on hold and preserving that leftover policy space for the future.

Asian Economic Calendar

Country	Time	Data/event	ING	Survey	Prev.
Monday 18 November					
Singapore	0030	Oct Non-oil domestic exports (MoM SA/YoY%)	-3.0/-14.0	-/-	-3.3/-8.1
	-	3Q F GDP (Q) (QoQ Ann/YoY%)	2.1/0.5	-/0.2	0.6/0.1
Thailand	0230	3Q GDP (QoQ/YoY%)	-0.6/2.0	0.1/2.7	0.6/2.3
Tuesday 19 November					
South Korea	2100	Oct PPI (YoY%)	0.4	-	-0.7
Wednesday 20 November					
Malaysia	0400	Oct CPI (YoY%)	1.0	-	1.1
Taiwan	0800	Oct Export orders (YoY%)	-4.6	-	-4.9
	0820	3Q Current account balance (US$bn)	18.4	-	17.6
Thailand	0200	Bank of Thailand's MPC Minutes			
China	0130	1Y Loan Prime Rate	-	4.20	4.20
	0130	5Y Loan Prime Rate	-	4.85	4.85
Thursday 21 November					
Indonesia	-	Policy decision (7-day reverse repo, %)	5.0	-	5.0
Hong Kong	0800	Oct CPI (YoY%)	3.0	-	3.2
Thailand	0330	Oct Exports (Cust est, YoY%)	-5	-	-1.4
	0330	Oct Imports (Cust est, YoY%)	-6.5	-	-4.2
	0330	Oct Trade balance (cust est, $m)	163	-	1275.0
Friday 22 November					
Malaysia	0700	Nov 15 Forex reserves- Month end (US$bn)	-	-	103.2
Singapore	-	Oct CPI (YoY%)	0.5	-	0.5
	-	Oct CPI - Core (YoY%)	0.6	-	0.7

Source: ING, Bloomberg, *GMT

Article | 14 November 2019

China: Trade war, cyclical demand and 5G seen in data

The trade war has accelerated the deterioration of a downward economic cycle in China, especially on consumption. 5G should be the new growth engine in 2020

Source: Shutterstock

Investment data shows trade war damage

Fixed asset investment grew only 5.2% year-on-year, year-to-date in October, the slowest growth rate since the data started in 1998. The weakness here shows that Chinese business investment has been highly affected by the trade war.

Investment in the textile industry (-8.5%YoY YTD) and electric equipment (-7.5%YoY YTD) actually contracted. Investment in these areas is only likely to recover when there is substantial progress in the trade negotiations.

For most of 2019, investment has been supported by transportation infrastructure investment via the issuance of local government special bonds. As the end of the year approaches, investment in these projects has slowed, shrinking 5.9%YoY YTD though we expect a pick up from 1Q20.

Industrial production shows cyclical pressure from trade war and local consumption

Headline industrial production growth slowed to 4.7%YoY in October from 5.8% in the previous month.

Industrial production of two items in particular, vehicles (-11.1%YoY) and smartphones (-7.3%YoY), show how the trade war has affected exports as well as local demand. Vehicles and smartphones share two similar features; they are both expensive and demand for new models from consumers is low without an obvious reason to upgrade. As demand is weak, production shrinks as inventory must be sold.

It's not all bad though. Production of integrated circuits grew 23.5%YoY in October and we expect this to remain strong due to the production of 5G parts and products.

Retail sales hit by big ticket items

Headline retail sales grew at 7.2%YoY, lower than the market expectation of 7.8%YoY, and the lowest this year. The growth was supported by spending on necessities (12%).

Uncertainty about job security is a key reason why consumers are cautious about spending on big-ticket items. Data shows that spending on vehicles fell 3.3%YoY and jewellery was down 4.5%YoY even though there was a long holiday in October.

People did spend on smartphones (22.9%) as some Chinese brands began selling 5G phones in October. This confirms that 5G is the new growth engine of the economy.

Growth prospects rest on trade and 5G

We expected that the process of getting a Phase One trade deal would be full of uncertainty. It is unfortunate that we are correct. Chinese companies will continue to defer investments if they are in the export business. However, if Chinese companies are involved in building and producing 5G infrastructure, equipment, parts, and final goods and services, they are highly likely to enjoy decent growth, even though they may not be able to export their products to some parts of the world.

Unless these factors change, we won't be revising our GDP forecast of 6.2% for 2019 and 5.9% for 2020.

Yuan outlook

For the market, all of this means that USD/CNY will be very volatile.

The yuan will weaken a lot if there is no Phase One deal and we can't rule this out even if the chance is small. On the other hand, the currency will strengthen if tariffs on $112 billion worth of goods, imposed in September, are lifted.

Volatility will continue even after a Phase One deal is agreed because the market will then start to question the likelihood of a more comprehensive follow-up agreement.

We are forecasting USD/CNY at 7.0 by the end of 2019 and 6.85 for the end of 2020, which mostly

depends on the progress of the trade talks.

The market will soon realise that a simple Phase One deal is by no means the end of the trade war.

Philippines central bank holds fire as expected

After aggressively rolling back policy rates and conducting operational adjustments, Philippines' central bank opted to gauge the impact of its latest...

Source: Shutterstock

4.0% Reverse repurchase rate

policy rate

As expected

Waiting for the dust to settle

The Bangko Sentral ng Pilipinas (BSP) opted to keep policy rates unchanged with the overnight reverse repurchase rate (RRP) kept at 4.0%. After quite a busy 2019, the "pro-growth" governor decided it was time to weigh the impact of his recent accommodative moves to close out the year. Governor Benjamin Diokno, who had previously vowed to "normalise" rates, has kept the mantra of "data dependency" in guiding his policy decisions and we expect him to monitor inflation forecasts and the economy's overall growth momentum going forward. Inflation is forecast to bounce from its recent reading of 0.8% (in October) as base effects wash out quickly

and as meat, fish and chicken prices tick higher as consumers substitute away from pork. BSP lowered its inflation forecast for 2019 to 2.4% (from 2.5%) and retained the 2.9% inflation forecast for 2020 and 2021. Meanwhile, growth is expected accelerate but most analysts expect it to fall short of the government's growth target of 6.0-7.0%.

Appropriate for now but likely to ease further

Given a possible miss on the growth objective, we expect Governor Diokno to come out swinging in 2020 with up to 50 basis points of policy rate cuts to help bolster growth momentum. Next year, the government will be chasing a higher growth target of 6.5-7.5% and BSP may likely need to shore up fiscal stimulus while inflation dynamics allow them to do so. We also expect BSP to carry out its phased and pre-announced reductions to the reserve requirement ratio (RRR) in 2020 as Diokno looks to align the Philippines' RRR with regional peers. Although the exact timing may still be in question, we are confident that any form of adjustment, both policy and operational, will be guided by data and will be effectively communicated to the markets.

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