

Good Morning Asia - 18 September 2018

The next round of the US-China trade war kicks off as early as next Monday with 10% tariffs on \$200bn of US imports from China. The announcement dashes hopes of any trade negotiations between two rivals. Be prepared for a prolonged period of risk-off

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International theme: You're Tarrified! China to counter?

- Donald Trump announced a 10% tariff on a substantial amount of goods although he steered clear of hitting important consumer electronic items from Apple as well as other select consumer goods.

EM Space: Asian markets likely to be on the defensive

- **General Asia:** Asian markets will open to reports that Trump pushed through with a 10% tariff on up to \$200Bn worth of imports from China. Although the levy saw a lower rate, it could foment a response from China who had previously threatened to walk away from the negotiating table.
- **Indonesia:** Indonesia's trade gap swelled to \$1.02 billion, running well past market expectations as exports grew by 4.15% as opposed to hopes for a 10.0% gain. Indications point to a current account deficit for the 3Q of the year. The widening trade gap will likely compound the IDR's woes with the government looking to curb imports and keep the current account deficit under control.
- **Philippines:** Remittances from overseas Filipinos grew by 5.2% in July, with flows reaching

\$2.4 billion for the month to bring the year to date haul to \$16.5 billion. The rebound in remittances was the first bit of good news out from the Philippines but these flows from migrant workers remain inadequate to cover external obligations related to trade.

What to look out for: Fall-out from Trump tariff

- Fall-out from Trump's 10% tariff on \$200 billion of Chinese imports
- Japan BoJ meeting 9/19/2018
- Thailand BoT meeting 9/19/2018
- Euro zone consumer confidence 9/20/2018
- US existing home sales 9/20/2018
- US-China trade negotiations (deadline: end of September)
- Argentina-IMF credit line request (on-going)

Why China could rebuff Trump's trade talks

Investment data shows that real estate activity has held up well, suggesting that China has support from a key sector even as the trade war escalates....



Source: Shutterstock

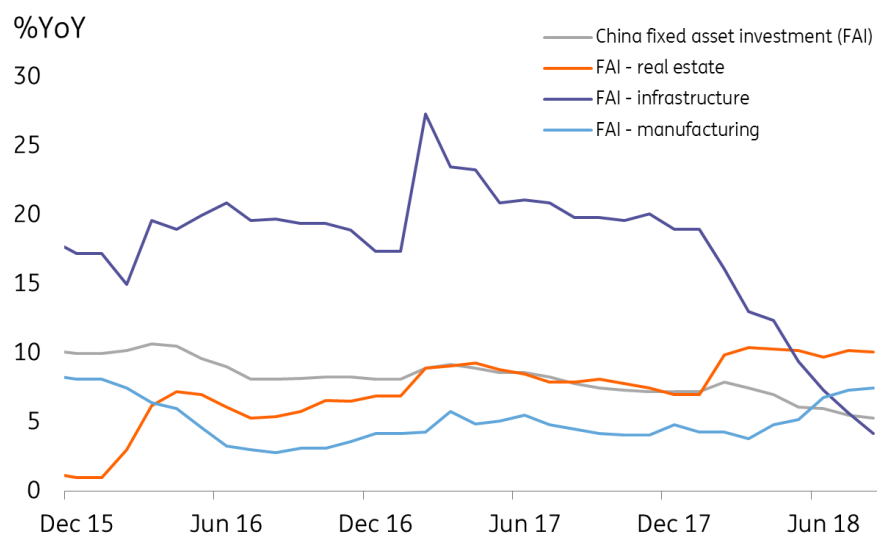
Trade talks rebuffed?

Real estate activity in China has continued to support overall investment, suggesting that sentiment in the real estate asset market is still positive, even amidst the trade war. This could buy China some time and suggests there's no rush for them to enter trade talks again, as reported in Chinese media.

With tariffs on \$200 billion of goods yet to be imposed, the offer of talks from the US - led by Treasury Secretary Steven Mnuchin - could signal that the administration is interested in some sort of compromise, possibly lowering the tariff rate to 10% from 25%. Though it is reported that President Trump also wants to impose further tariffs on \$267bn of goods.

China could delay talks until after the US mid-term elections, as discussions before then are unlikely to yield any solid result. [President Trump's tweets](#) also suggest he is in no hurry to strike a deal with China.

Where was infrastructure investment?



Source: ING, Bloomberg

Fixed asset investment grew at a slower-than-expected pace in August

Investment was slower than expected in August because we misjudged the timing of fiscal stimulus.

We did not expect railway investment to deteriorate from the previous month's -8.7% year-on-year YTD rate. Instead, it was down 10.6% YoY YTD. Still, we believe that transportation infrastructure will rise in the coming months to reflect the results of fiscal stimulus.

We still expect to see fiscal stimulus come into effect in September.

If not, we may need to gauge the situation in China again. It could be that the government is looking ahead and wants to avoid too much overcapacity in the future, even if the economy is currently facing the negative impact of a trade war. It could also be that the government has estimated a smaller impact from the trade war compared to our own estimates. In this case, China may not need a lot of pro-growth programmes.

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Indonesia: August trade gap bodes ill for 3Q current account

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Source: Shutterstock

-\$1.02bn

August trade balance

July-August trade deficit amounts to -\$3.03bn

Worse than expected

Current account deficit of \$8bn seen in 3Q

Indonesia's strong domestic demand continues to power imports. Oil and gas imports posted a 51.4% year-on-year increase in August accelerating from July's 50% increase and June's 32% pace. Higher energy prices have contributed to the high oil and gas import bill. Benchmark oil prices were almost 60% higher YoY while the Indonesian rupiah (IDR) depreciated by an annualised rate of 9% for the month. IDR's weakness of almost 8% year-to-August has not restrained demand. Higher energy subsidies have insulated energy demand from IDR's weakness and higher oil prices.

- Non-oil and gas imports remain strong with a YoY increase of 20%.
- Meanwhile, exports moderated to a 4.2% YoY increase in August.
- Non-oil and gas exports slowed drastically to only a 3.4% annual increase from July's pace of growth of almost 20%.

As a result, the economy posted a second straight deficit in August. The July-August deficit now amounts to \$3.03 billion, a reversal of the surplus of \$1.9 billion for the same period last year. This means that the 3Q current account will likely incur another \$8 billion deficit which would be as bad as the 2Q deficit. Such an outcome would keep the current account deficit at close to -3% of GDP. We reiterate our current account deficit forecast of -2.6% of GDP or a deficit of almost \$28 billion in 2018 from 2017's -1.4% of GDP or -\$14.5 billion. We believe that such a weak external balance would keep the IDR on a weakening path. However, the central bank's hawkish stance together with government efforts toward import substitution for fuel, export enhancing rules and modest fiscal deficit spending could deliver some relief for the currency.

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Philippines: Overseas remittances rebound in July

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Source: Jun Acullador

5.2%

July Overseas Worker remittance growth

Rebound still does not cover the wider trade deficit

As expected

Weak PHP trend hasn't changed despite remittance rebound

Overseas Filipino worker (OFW) remittances recovered with 5.2% YoY growth in August from a drop of 4.5% in June. The 7-month 2018 average growth of 3% is below our 4-4.5% 2018 growth forecast.

- Remittances from the US, Asia and Europe continue to fuel the growth.
- Remittances from the US- accounting for 35% of total remittances in July- were 5.9% higher YoY and averaged a monthly growth rate of 6.3% for the first seven months of the year.
- Asian remittances were up 15.9% YoY and account for 21% of total remittances for the

- month. The 7-month growth of remittances from Asia was 15% on average.
- Remittances from Europe, including the UK (which account for 15% of the total in July), increased by 12.5% YoY and by 10% for the seven month period.
 - Middle-East remittances continued to disappoint with an almost 14% YoY drop and 12.6% decline for the period.

Monthly remittances remain inadequate to finance the monthly trade deficit. This shortfall in July amounted to \$1.1 billion. For the seven months, it was \$5.9 billion, a reversal of the \$3 billion excess in 2017. This shortfall will continue and should keep the peso on a defensive bias.

India: Rupee takes no comfort in stabilisation measures

Investors may start pricing in more aggressive tightening in India after recent measures failed to stem the currency weakness. But we're in no rush to...



Markets fail to cheer stabilisation measures

After a brief hiatus, India's currency slide resumed today despite new measures to stem the rupee (INR) depreciation. At the start of trading today, the INR reversed almost all its gains against the US dollar, which had been eked out in the last two trading sessions in anticipation of some significant action from the government and the RBI to stabilise the currency market.

Late Friday, the finance ministry announced measures including the relaxation of regulation of foreign borrowing up to \$50 million by manufacturing companies for a year compared to the current minimum of three years, the scrapping of withholding tax on masala (INR-denominated) bonds, and a possible easing in the current 20% limit on foreign ownership of corporate bonds. Nothing more.

It's hard to imagine these measures being immediately effective in curbing the currency depreciation, as the external payments situation remains on a deteriorating path. Today's market reaction testifies to this. As such, more measures are expected. Some potential steps have been widely-discussed, including:

- A central bank policy rate hike
- Exchange market intervention
- Tapping funds from overseas Indians
- Raising import tariffs
- Swap window for oil companies

All eyes on the Reserve Bank of India policy

The markets may start pricing in an aggressive Reserve Bank of India policy rate hike, as also implied by two-thirds of odds of the 50 basis point hike at the next meeting in early October. It wouldn't come as a complete surprise to us. However, we remain sceptical that the RBI will follow that path, now that inflation is running in the lower half of the 2-6% inflation target.

The current currency weakness will eventually push inflation higher at some point in the future. A pre-emptive aggressive move would be a welcome support for the currency. But this could also depress economic activity, while external risks from the trade war now loom large.

We aren't rushing to change our forecast of two more 25 basis point hikes at the October and December meetings, and a USD/INR rate of 73.5 by end-2018.

USD/INR: Trading on Monday kicks off with INR sell-off



Source: Bloomberg

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