Good MornING Asia - 19 November 2018

The risk to global economies and markets from the Sino-US trade war is elevated after an impasse between two countries at the APEC summit

In this bundle

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ASEAN morning bytes

General market tone: Wait and see. US stocks posted marginal gains on Friday but still posted weekly losses with tech and energy shares dragging. Comments from a Fed official, on the other hand, sparked a rally in bonds.

International theme: US-China trade comments boost sentiment but APEC tone suggests otherwise

- US shares managed to post gains on Friday on hopes of improvements in the US-China trade spat, however, comments from both China and the US at the APEC meeting showed relations remained icy. Meanwhile, Fed Vice Chair Clarida, erstwhile quiet on his policy stance, indicated that the current Fed funds rate was approaching “neutral”, sending bond yields lower.

EM Space: Focus remains on Sino-US relations

- **General Asia:** Asian equity will likely take their cue from reports regarding the US-China trade spat with commentary from the APEC meeting showing the tenuous relationship as world powers jockey for positioning in the region.
- **Malaysia:** 3Q18 GDP growth of 4.4% YoY was only a slight slowdown from 4.5% in 2Q. As expected, household consumption remained the key growth driver. Data remains supportive our view of an on-hold BNM policy for in the rest of this year and through 2019.

- **Thailand:** 3Q18 GDP is due today. The consensus is looking for a slowdown in growth to 4.2% YoY from 4.6%. We are more bearish with our 3.7% growth forecast derived from a sharp slowdown in manufacturing growth and weakening tourism sector.
- **Indonesia:** Bank Indonesia forecasts inflation to remain benign with November inflation seen at 3.13%, well-within their target for the year. Meanwhile, the government looked to attract more foreign investors by including more sectors open for the foreign players as well as extending tax holidays to entice entrants to the country. With the current account threatened anew by widening trade deficits, Indonesia is looking to shore up its foreign flows via the financial account.
- **Philippines:** The Bangko Sentral ng Pilipinas (BSP) has leeway "to digest the rate hikes" with Deputy Governor Guinigundo expecting inflation expectations to come down significantly in the next 2-3 weeks. BSP flagged this as the key reason for hiking rates another 25 bps at its 15 November meeting. Guinigundo is not a voting member of the Monetary Board but it may signal the willingness of the BSP to hold off on rates after raising rates a total of 175 bps year to date.

What to look out for:

- TH 3Q GDP (19 November)
- PH BOP (19 November)
- HK CPI inflation (20 November)
- US housing starts (20 November)
- TH trade (21 November)
- US durable goods (21 November)
- US existing home sales (21 November)
- JP CPI inflation (22 November)
- SI 3Q GDP (22 November)
- MY CPI inflation (23 November)
- SI CPI inflation (23 November)
- TH GIR (23 November)

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Hong Kong: Downgrading GDP forecasts

Hong Kong GDP growth was surprisingly slow in 3Q, at 2.9% year-on-year. Consumer spending has been growing at a slower pace and there are risks ahead, as the trade dispute looks set to hurt the economy through logistics, exports and eventually, wage growth in export-related industries. As such, we're cutting out forecasts

Source: Shutterstock

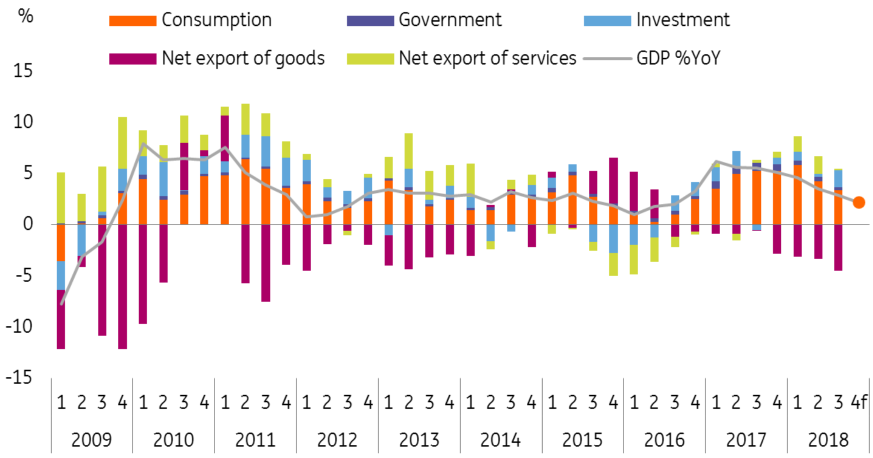
Hong Kong GDP growth slowed more than expected

GDP slowed to 2.9% year-on-year in 3Q18 from 3.5% previously. It was the slowest rate since 3Q16.

The main factor behind the slowdown was consumption. While this still grew 5.2% YoY in 3Q18, it was the slowest growth rate since 1Q17. We believe this is a result of consumers making large down payments on residential properties, which reduced the pool of money available for other purchases.

The other unexpected effect is that front-loading export activities in China have distorted export and import growth data. We believe that this distortion will continue in 4Q18 as tariffs on $200 billion of Chinese imported goods into the US will increase to 25% on 1 January 2019.

Consumption contribution slowed substantially



Source: ING, Bloomberg

Rising interest rate during economic downturn

The exchange rate system is not helping the economy. As the Federal Reserve is going to raise the Fed Funds Rate into 2019, Hong Kong interest rates should follow suit in theory under Hong Kong's linked exchange rate system. That is, the economy faces a downturn at the same time interest rates are rising.

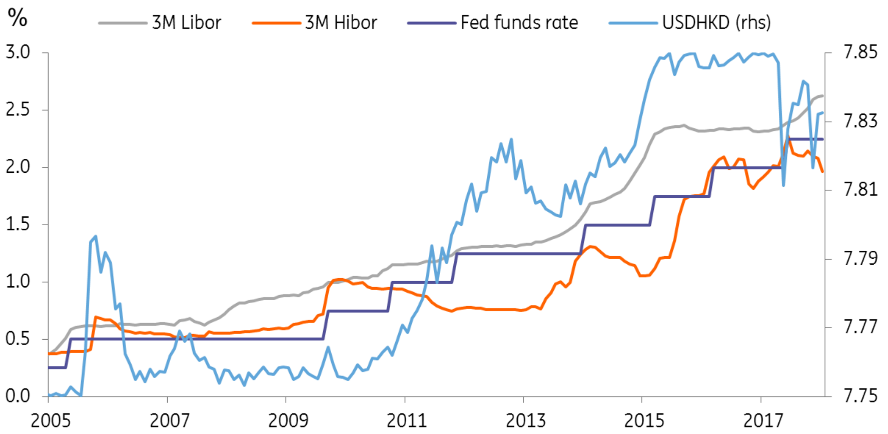
On the Hong Kong dollar, after sticking to HKD7.85 per dollar, the upper bound of the linked exchange rate system, the HKD is heading towards 7.80, the mid-level of the range of 7.75 and 7.85 (spot rate: 7.83).

There are opposing forces that are driving the HKD:

- On the one hand, falling interbank interest rates (HIBOR) attract activities that buy US dollars and sell HK dollars in the market.
- On the other hand, banks in Hong Kong have raised lending and deposit interest rates to close the gap of USD and HKD, and should strengthen HKD against USD.

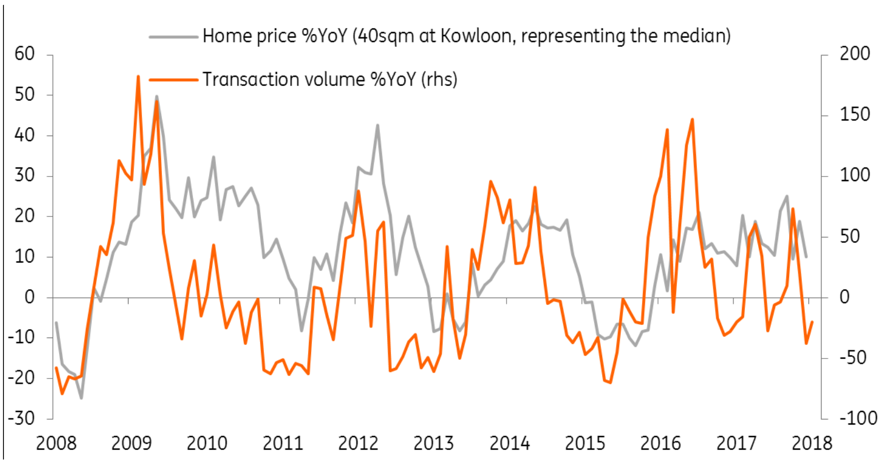
Whether the HKD will continue to strengthen to 7.80 depends on whether banks in Hong Kong continue to raise interest rates when the next Fed rate hike arrives, possibly in December.

Fed funds rate is affecting HIBOR and hence HKD



Source: ING, Bloomberg

Hong Kong housing transactions fall after prices reach high



Source: ING, Bloomberg

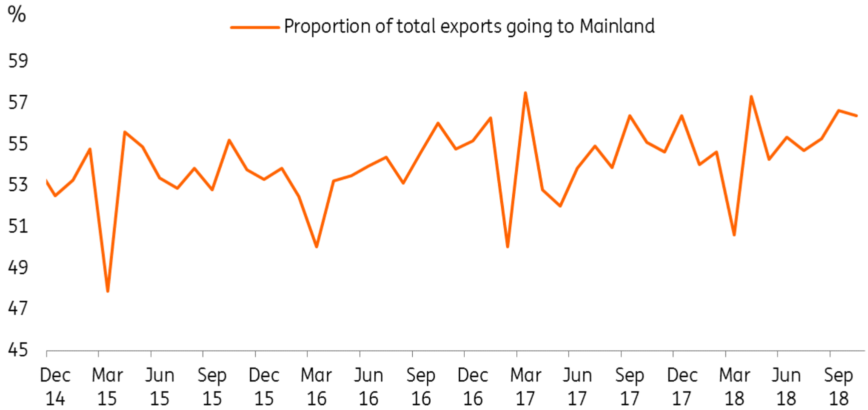
Growth will be even slower in coming quarters

The trade dispute between China and the US will continue to hurt import and export activities as more than half of exports go to Mainland China. And consumption activities will still be constrained by the money that has been spent on down payments. These individuals will need to rebuild their savings pool and therefore are likely to spend less in coming quarters. In addition, a falling stock market and housing market could fuel a negative wealth effect, and hurt consumer sentiment.

To cushion the economy, we expect that the government will speed up the construction of public housing to cushion some of the negative impact.

Considering all these factors, we revise our GDP growth forecast downward to 2.2% YoY for 4Q18 from 2.8% YoY and to 3.3% for 2018 from 3.6%. For 2019, we predict growth of 2.2% compared to a previous forecast of 2.6%.

Hong Kong exports rely on Mainland China



Source: ING, Bloomberg

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