

Good Morning Asia - 21 October 2019

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Clarity may emerge on Brexit this week

For those who wish this will all end, this week may finally see some more clarity on Brexit.



Source: Shutterstock
UK prime minister, Boris Johnson

Is this the real thing? Is it just fantasy?

I was in India all of last week, hence the hiatus in these daily opinion pieces. There will be a break at the end of this week as I go to Hong Kong to chair EMTA meetings there on Thursday. Then back to near-normal the following week. Thanks to those who asked where the note was.

Anyway, I had to give a lot of presentations in India, many of which touched on Brexit. This usually had me reaching for my phone, to check in case something had happened in the hours since the previous presentation. On a couple of occasions, it had.

Brexit has not been kind to analysts. [James Smith's excellent note about Saturday's votes](#) had a short-shelf life, given the Letwin amendment, that meant no vote took place on Johnson's deal this Saturday and the PM had to send letters asking for a Brexit extension. That letter was left unsigned and was accompanied by other letters stressing that Johnson had no intention of seeking an extension beyond October 31.

Now, we either get a "meaningful vote" today, or more probably, a vote on the "programme motion", which sets out the timetable for legislation votes over the days ahead. That, if it goes

ahead, will still try to meet the October 31st deadline. On paper, at least, it also has the votes to get through, though only by a whisker. 5 votes according to what I have been reading this morning. Sterling has given back a bit of ground, but with the prospects of a no-deal outcome seeming to dim, that weakness may prove short-lived. I have some modest euro-denominated bills to pay, so I may wait a couple of days.

Trade deal also seeming to come together

It also looks as if trade tensions should continue to diminish in the weeks ahead. Vice-Premier, Liu He is quoted on Bloomberg today as saying that trade talks have made "substantial progress", for a "phase one" agreement. So a partial deal does look possible. That could see the CNY make further small moves back in the direction of 7.0 (7.08 today and Iris Pang thinks that 7.05 is possible, lower if we got some removal of existing tariffs). That could also drag some of the region's currencies, (INR in particular) with it.

Iris also notes "PBoC Governor, Yi Gang, commented that the current yuan level (which has been around 7.07-7.20) has been driven by market forces, and this level of the yuan is appropriate. We believe that the yuan will stay at the range of 7.05-7.50 depending on the progress of the trade talks. Though China made a positive statement that the two sides are drafting a partial agreement, China did emphasise that US has to respect China to achieve a deal. As such we still see uncertainties for a deal to be reached".

Risk sentiment more broadly is improving on growing hopes for a partial trade deal, and perhaps also a bit on looming Brexit relief. Yields on US Treasuries have risen. The 10Y is now offering a respectable 1.75%, with a decent 21bp over the corresponding 2Y yield, so perhaps thoughts of recession should be scaled back a bit? The NY Fed's probability of a recession in 12 months indicator has indeed dropped back a bit to 34.8 from its recent high of 37.93%. My own unrestricted model based on the NY Fed's approach shows only about 15% probability, down from a recent 18% high, but still elevated from "normal" readings closer to zero.

Perhaps what this is telling us is that we are not about to lurch into some sharp slowdown, but that a continued slow grind lower is in prospect. For those for whom the semantics of a global recession matter, it is worth noting that there are no widely accepted definitions of this. The IMF has a methodology that is the nearest thing in my view, but, as [the linked wikipedia article shows](#), requires consideration of up to seven indicators, so by the time you've crunched the numbers, it is probably either too late, or you would have emerged on the other side already.

A more workable definition might be that a rate of global growth of 3% or less would constitute a global recession. Any guesses what the latest IMF forecast for global growth in 2019? It's 3%, down from their earlier estimate of 3.2%. In other words, recession, already.

They do forecast a pick up to 3.4% in 2020 incidentally. But I think that will be contingent on the trade war.

3.0% Global GDP
IMF 2019 forecast

Asia today

It's relatively quiet in Asia today. China might trim its loan prime rate (LPR) by 5bp - a small but creeping incremental monetary easing. That would take the 1 year LPR down to 4.15% from 4.20%.

Bank Indonesia meets on Thursday to decide policy. Bloomberg consensus indicates a 25bp rate cut to 5.0%.

Later in the week, we have some preliminary 3Q19 GDP figures out of Korea, which likely won't make great reading. Singapore CPI also out later in the week may also highlight the limited nature of the recent Monetary Authority of Singapore (MAS) easing.

Thai trade data for September out today will likely show weak export growth, but contracting imports, for a net increase in the trade surplus. This adds pressure on the BoT to respond with some easing, but their reticence to act means the more likely result is further THB strength.

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ASEAN Morning Bytes

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EM Space: World leaders hint at more fiscal stimulus

- **General Asia:** The joint IMF-World Bank meetings over the weekend highlighted the ill effects of the ongoing trade spat between the US and China on the global growth outlook. With monetary policy stretched, global leaders have turned their eye to fiscal stimulus for additional support. The ECB President Draghi will chair his last policy meeting this week. In Asia, Bank Indonesia is likely to keep the powder dry for another possible cut before the end of the year.
- **Indonesia:** President Jokowi formally took his oath for a second term over the weekend, vowing to push for reforms to bolster Indonesia to a \$7 trillion economy in 25 years. In the further announcement today, Jokowi aims to revamp his cabinet with technocrats, industrialists and even former political rivals expected to be named to his new team. Bank Indonesia Governor Warjiyo has been mentioned as a possible candidate to be moved. Jokowi's directive is to spur growth via the investment route, which will be beneficial for the IDR.
- **Malaysia:** A huge surge in vehicle demand and production in September – sales up 43% YoY and production 22% -- is a reflection of the low statistical base rather than a sharp turnaround in the sector a slew of sharp declines in recent months. We maintain our view of

one more 25 basis point rate cut by Bank Negara Malaysia in the current quarter, while the fiscal policy continues to be restrictive.

- **Philippines:** Bangko Sentral ng Pilipinas (BSP) Governor Diokno reiterated his leaning for policy in the next few months, indicating that the 2019 rate cut cycle may be closed although he did keep open the possibility for a reduction for reserve requirements. In further positive for the Peso, the balance of payments remained in surplus in September, albeit a sharp narrowing to \$38 million from \$493 million in August. This brings the year-to-date surplus to \$5.57 billion, a sharp turnaround from a deficit of \$2.7 billion in the same period of 2018.
- **Thailand:** Trade figures for September are due today. We consider the consensus of 2.7% YoY export growth optimistic (ING forecast -2.0%). Electronics and autos and parts, the key export drivers with a combined 30% weight, continue to be weak. But import growth has been in deeper negative than exports this year, reflecting weak domestic demand and low oil prices. As such, 2019 is shaping to be the turning point in the trend of narrowing current account surplus since it peaked over 10% of GDP in 2016. We see annual surplus this year at about 7% of GDP (6.4% in 2018), which together with hawkish central bank policy should sustain the Thai baht at the top emerging market currencies in the rest of the year.

What to look out for: ECB meeting and US home sales

- Thailand trade (21 October)
- Malaysia GIR (22 October)
- US existing home sales (22 October)
- Malaysia inflation (23 October)
- Singapore inflation (23 October)
- Hong Kong trade (24 October)
- Bank Indonesia meeting (24 October)
- ECB meeting (24 October)
- US durable goods and new home sales (24 October)
- Singapore industrial production (25 October)
- Thailand GIR (25 October)

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Asia week ahead: Bank Indonesia to keep its powder dry

Given the recent wobbles experienced by the Indonesia rupiah, we expect the central bank to stay put next week, but China's central bank might cut its revamped loan prime rate



People's Bank of China could go more accomodative

The People's Bank of China will announce the revamped loan prime rate (LPR) on Sunday, 20 October. Though the medium-term lending facility interest rate remains unchanged, there is still a chance that the central bank will cut the one-year lending facility by 5 basis points to 4.15% to support the flagging economy.

Bank Indonesia to stay put... for now

Indonesia's central bank will meet on 24 October against a backdrop of slowing growth. The central bank governor forecasts growth to dip to 5.1%, citing the headwinds from the trade war for this expectation.

With inflation within target and decelerating, the central bank has some room to trim borrowing

costs further. Governor Warjiyo has slashed borrowing costs for three straight meetings in a bid to provide a boost to sagging GDP growth momentum, but the central bank may opt to keep its powder dry given the recent wobble experienced by the IDR. That being said, we expect BI to stay on hold with the possibility for a rate cut at the November meeting if inflation resumes its downward trend and growth numbers warrant further stimulus.

Barrage of data

China's industrial profit growth should shrink less than previous months as infrastructure projects have created businesses to manufacturers.

Orders and deliveries of smartphones will provide some support to Taiwan export orders and industrial production as well as Hong Kong exports and imports, but the support should not be enough to change a yearly negative growth trend to positive growth.

The Philippines will report the budget balance for the month of September with spending figures and the budget balance now increasingly of importance given the recent slowdown in GDP growth due to the budget delay. Government officials have vowed a swift catch-up in spending with a substantial budget deficit seen to rekindle hopes for a rebound in growth for the 3Q.

Asia Economic Calendar

Country	Time	Data/event	ING	Survey	Prev.
Sunday 20 October					
China	03300	Loan prime rate		4.15	4.20
Monday 21 October					
Taiwan	0900	Sep Export orders (YoY%)	-	-10.1	-8.3
Thailand	0430	Sep Exports (Cust est, YoY%)	-	-	-4.0
	0430	Sep Imports (Cust est, YoY%)	-	-	-14.6
	0430	Sep Trade balance (Cust est, US\$m)	1903	-	2053
South Korea	2200	Sep PPI (YoY%)	-	-	-0.6
China	0230	Sep 70-cities New home prices (MoM/YoY%)	-/-	-/-	0.6/9.1
Japan	0050	Sep Exports (YoY%)	-7.6		-8.2
	0050	Sep Imports (YoY%)	-0.1		-12.0
	0050	Sep Adjusted trade balance (¥ bn)	-271.0		-130.8
	0530	Aug All industry activity index (MoM%)	0.7		0.2
Tuesday 22 October					
Malaysia	0800	Oct 15 Forex reserves- Month end (US\$bn)	-	-	103
Philippines	-	Sep Budget balance (PHP bn)	-86.4	-	-2.5
Hong Kong	0915	Sep Composite (YoY%)	-	-	3.5
Japan	-	Imperial Enthronement Day Holiday			
Korea	0000	Sep PPI (YoY%)	-0.7	-	-0.6
Wednesday 23 October					
Malaysia	0500	Sep CPI (YoY%)	1.3	-	1.5
Singapore	0600	Sep CPI (YoY%)	-	-	0.5
	0600	Sep CPI core (YoY%)	-	-	0.8
Taiwan	0900	Sep Industrial production (YoY%)	5.1	-	2.3
Thursday 24 October					
Hong Kong	0930	Sep Exports (YoY%)	-3.8	-	-6.3
	0930	Sep Imports (YoY%)	-8.7	-	-11.1
	0930	Sep Trade balance (HK\$ bn)	-25.5	-	-28.0
Indonesia	-	BI policy decision (7-day reverse repo, %)	5.25	-	5.25
Taiwan	0920	Sep Money supply (M2) (YoY%)	-	-	3.4
South Korea	0000	3Q P GDP (SA QoQ/YoY%)	0.6/2.2	-/-	1.0/2.0
	2200	Oct BOK Consumer Sentiment Index	-	-	96.9
Friday 25 October					
Singapore	0330	3Q Jobless rate (Q) (% , SA)	-	-	2.2
	0600	Sep Industrial production (MoM/YoY%)	-/-	-/-	-7.5/-8

Source: ING, Bloomberg, *GMT+1

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China: After 6% GDP growth in 3Q, we raise our 4Q forecast

China's economy grew at the target rate of 6% in the third quarter, and despite uncertainty over the trade war, we are raising our forecast for fourth quarter growth



Source: Shutterstock

The perfect 6

GDP grew by 6% in the third quarter, down from 6.2% year-on-year in the second quarter.

Infrastructure projects are the pillar of growth

The main growth driver was still infrastructure projects. These projects have moved from the investment stage to the production stage. Fixed asset investment growth stabilised at 5.4% from 5.5% in August. The transition from investments to production has supported industrial production, which grew by 5.8% in September from 4.4% in August. Transportation grew 10.5% YoY, which also boosted mining investments by 26.2%YoY YTD.

Private sector manufacturing activities continued to shrink, e.g. smartphone production contracted by 3.6% YoY in September. This highlights that some production lines in the private sector could have been scaled down in China and moved to other locations in Asia due to the US tariffs.

Retail sales grew on essential items

Consumption made up 60.5% of the GDP growth in the third quarter, higher than the 60.1% recorded in the first half. Overall retail sales grew 7.8% YoY in September from 7.5% in the previous month.

It seems to have been a good month for consumption but the details paint a slightly different picture. Only essential items saw strong growth. For example, food, household items and drugs grew more than 10% YoY in September. The only non-essential item that grew more than 10% was cosmetics. In contrast, automobile spending fell 0.7%. This tells us that, when it comes to non-essential purchases, consumers prefer small-ticket items to bigger, more expensive items.

Looking forward in 4Q19

We expect infrastructure projects to continue to be the central pillar of growth in the fourth quarter.

There is another CNY1 trillion yuan from the local government special bond quota, borrowed from next year, to be used until the end of 2019. These bonds are the source of financing for infrastructure projects. As such, both investment and industrial production will continue to rely on infrastructure.

This will mark even bigger differences between private and public sector growth. The private sector will continue to suffer from the scaling down of factory activity due to the US tariffs. This will add even more uncertainty in terms of job security and salary growth which, in turn, will put pressure on consumption, even if substantial public sector growth acts to counter these negative pressures.

The good news is that we expect 5G infrastructure, production and services to start to make a visible contribution to the economy from the fourth quarter. Although it is still uncertain how much 5G can help China's exports, domestic usage of 5G alone should offer good support to the economy.

Trade war is still an uncertainty

While both China and the US say they are drafting the texts of a "phase one" trade deal, it's still unclear what exactly will be in the agreement. China has asked for a rollback of all tariffs imposed by the US before it commits to increasing annual purchases of US agricultural products.

Meanwhile, the technology war rages on. Just before the last round of trade talks, the US added eight Chinese technology companies to its Entity List, effectively blocking US companies from doing any business with these companies. China could retaliate with its own unreliable entity list.

All of this is negative for the future growth of the Chinese economy.

If the US decides to roll back some of its tariffs, the picture will change. Manufacturers may think twice before moving factories to another location, which is very costly. Unfortunately, this is not our base case.

Monetary policy will loosen in 4Q19

To facilitate a lower interest cost for local government special bonds-which will support infrastructure investments- we expect a five basis point cut in the Loan Prime Rate on 20 October, and a 0.5 percentage point cut in the required reserve ratio (RRR) in the fourth quarter.

Without a lower interest rate, the economy may not be able to sustain growth of 6% in the fourth quarter.

Forecasts

We are raising our forecast for 4Q19 GDP growth from 5.8% to 6.0%. As such, our GDP growth forecast for the whole of 2019 will be 6.15%.

If the trade agreement in November is drafted in line with market expectations, i.e., China purchases \$50 billion of US agricultural produce annually without the US rolling back its current tariffs, the USD/CNY could trade around the 7.0-7.1 level. If the US does roll back some of the tariffs, we may see USD/CNY strengthen below 7.0. But again, this is not our base case.

Then there are the planned US tariffs in December. If the US does not defer those tariffs, the USD/CNY will weaken to around 7.20 or even higher.

In short, volatility should remain high, and the progress of trade talks will be key.

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