Good MornING Asia - 23 July 2019

Reports of the US and China resuming trade negotiations next week are positive for risk sentiment, but escalating tension in the Middle East pushing oil higher are negative. We anticipate wait and watch sentiment taking hold of the markets ahead of the ECB meeting this week and the Fed meeting next week.

In this bundle

ASEAN Morning Bytes

General market tone: Wait and see. Investors will likely refrain from making substantial bets ahead of key central bank meetings in the week.

EM Space: Hopes for a trade deal and rebounding energy sector will clash with caution ahead of ECB

- **General Asia:** Reports of the US and China resuming trade negotiations next week are positive for risk sentiment, but escalating tension in the Middle East pushing oil higher are negative. We anticipate wait and watch sentiment taking hold of the markets ahead of the ECB meeting this week and the Fed meeting next week.
- **Thailand:** Yesterday's June trade data showing an unexpectedly large trade surplus comes as a further boost to the THB. $3.2 billion trade surplus in the last month was the fourth-highest monthly surplus on record as exports improved for a smaller drop of 2.2% YoY while imports crashed by 9.4%. Weak domestic demand and lower oil price seem to be depressing imports and this is sustaining large external surpluses. We believe the economy needs lower interest rates to revive domestic spending, which will also help in curbing the THB strength. We forecast two 25 basis point cuts by year-end.
- **Malaysia:** Finance Minister Lim Guan Eng is worried about public finances staying on track to meet the 3% of GDP deficit target in 2020. He pointed to weak growth amid the US-China trade war and need to reduce public debt, estimated at over MYR 1 trillion, as main 'challenges', though minister also sees opportunities from trade diversion from the trade

war. In the ongoing global slowdown, Malaysia's economy is performing relatively well. The central bank (BNM) eased the policy with a 25bp rate cut in May and has enough policy space to stimulate the economy further if needed.

- **Singapore:** June CPI is due with consensus looking for a slowdown in headline inflation to 0.8% YoY and in the core to 1.2% from 0.9% and 1.3% respectively in the previous month. We see lower transport costs from falling COE prices and fuel prices to more than offset the holiday season surge in recreational costs. With subdued inflation and deteriorating growth prospects, the central bank (MAS) is expected to ease the policy before the next scheduled semi-annual policy review in October.
- **Indonesia:** Bank Indonesia (BI) Governor Warjiyo stepped up the dovish rhetoric in testimony before lawmakers yesterday, signaling further monetary policy easing ahead via cuts in both policy interest rates and banks' reserve requirement ratio. He sees this helping the growth momentum in 2H19.
- **Philippines:** The government budget posted a deficit of PHP 41.8 billion in June. This puts the deficit for the first half of 2019 at PHP 42.6 billion. Delayed passage of the budget for 2019 kept government spending lackluster while revenue collection picked up. Weak government spending was a drag on GDP growth in 1Q19. We believe it persisted in 2Q19, leaving GDP growth below 6%.

What to look out for: Regional inflation data and geopolitical tension

- Singapore inflation (23 July)
- Taiwan industrial production (23 July)
- Malaysia inflation (24 July)
- US durable goods (25 July)
- South Korea GDP (25 July)
- Hong Kong trade (25 July)
- ECB meeting (25 July)
- Japan inflation (26 July)
- US GDP (26 July)

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Snap | 22 July 2019 Taiwan

Taiwan: Export orders fall and will keep on falling

Despite flattering base effects given weakness last year, Taiwan continues to disappoint. We wonder whether policies to attract manufacturers to set up in Taiwan will deliver and whether the central bank will follow its Asian peers and cut rates

A woman checks her mobile phone while waiting to cross the street in Taipei, Taiwan

Taiwan export orders keep falling

Taiwanese export orders fall for the eighth month in a row, decreasing by $1.82 billion from June 2018, a reduction of 4.5%YoY. In the second quarter of 2019, they fell 4.7% YoY. For 1H19 export orders fell 6.5%YoY, and that's all with a very low base effect.

The speed of reduction may be slowing slightly from the start of the year, but it's falling nonetheless. And that means production activities will also continue to weaken and we'll be able to confirm that from Tuesday's industrial production data.

Promoting Taiwan's production line investments

With global smart devices entering a late product cycle, there's a negative environment for manufacturers, especially for technology-focused Taiwanese producers.

The government offers a preferential interest rate policy to manufacturers to encourage them to move production lines from mainland China. But, even if the government attracts investment funds into Taiwan, those production lines may not be running in any meaningful capacity if export orders keep falling.

We believe this will only change to a positive picture once 5G is widely used. Then smartphones will have new product cycles. Until then, we don't think there can be a significant upturn in Taiwan's production and, subsequently, its exports.

The central bank says it won't cut rates

Other Asian central banks have cut interest rates, Taiwan's has responded by indicating its rate, currently at 1.375%, won't be changing any time soon.

Taiwan CPI inflation is low at 0.86%YoY. GDP has avoided falling into negative territory, with the economy growing at 1.71% in 1Q19, and we expect 1.8% for the whole of 2019. Given that rates are already low, it's difficult for the bank to cut them further in a pre-emptive strike to boost growth.

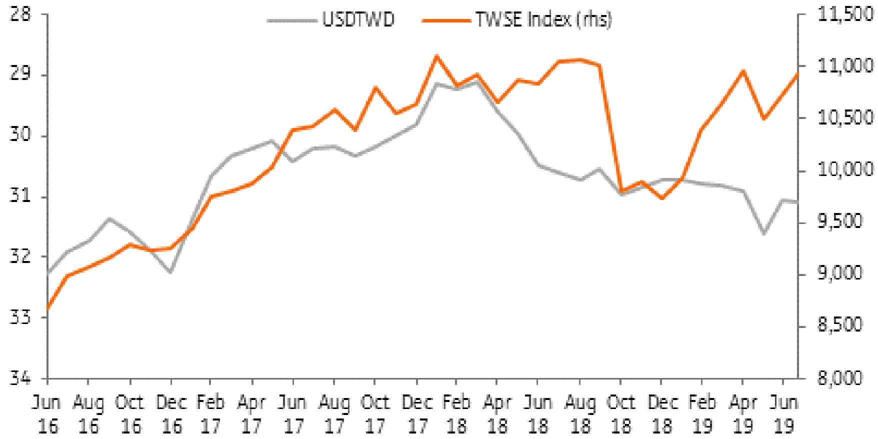
USD/TWD still weak because of the yuan

Usually, when the Taiwan stock indices rise, there will be inflows of foreign capital into the market, and that should support the Taiwan dollar against the USD. But the stock index (TWSE) have been moving in opposite directions with the currency. The stock market has increased by 13%YTD but the currency has depreciated 1% in the same period.

It could be that the smartphone production cycle has suppressed both Mainland China and Taiwan's economies. The TWD, therefore, has shared the same pressure as the CNY, the yuan. CNY has depreciated slightly at 0.03%YTD.

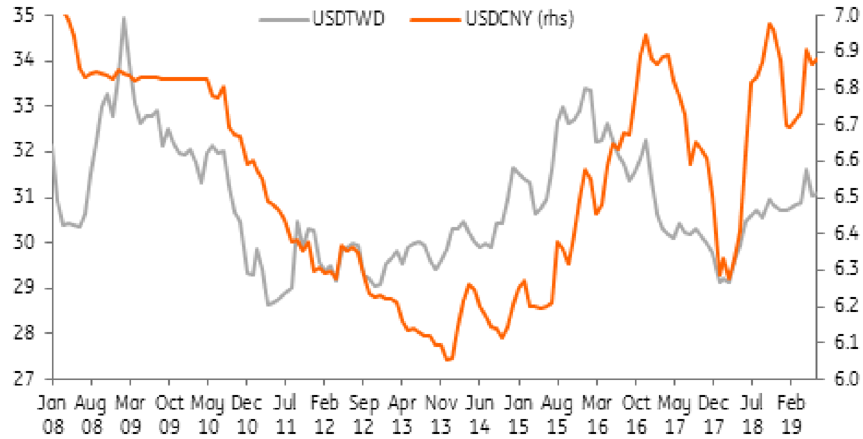
As the two economies are even more interlinked, building up production lines in Taiwan doesn't seem to be the best way to boost growth as the economic weakness lies in the smartphone product life cycle. This will continue until there is a new demand for phone upgrades, which most likely will come from 5G.

TWD and stock index has lost the link



Source: ING, Bloomberg

TWD and CNY has increased correlation



Source: ING, Bloomberg

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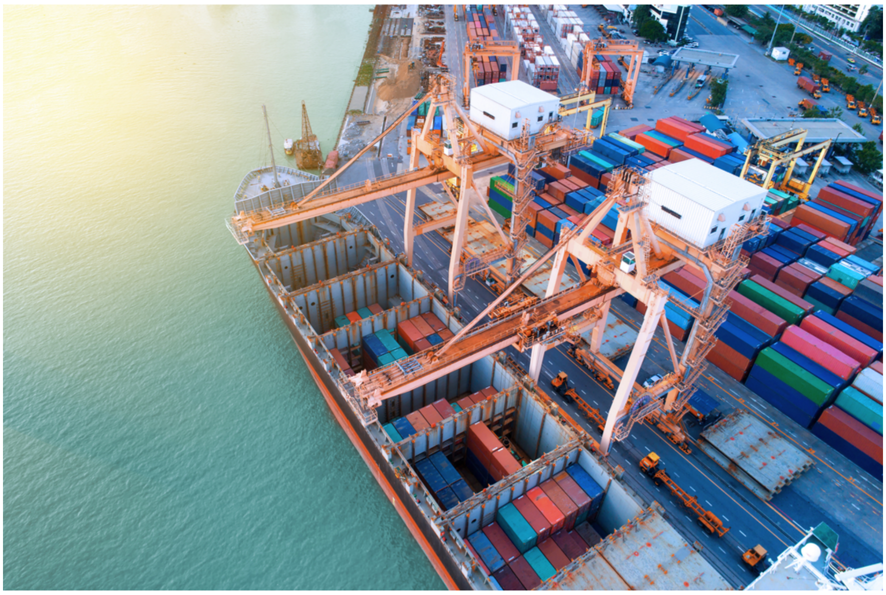
Article | 22 July 2019 Thailand

Thailand: Wide external surplus dents drive to curb baht strength

The Bank of Thailand's latest efforts to curb appreciation in the Thai baht are proving ineffective and aggressive interest rate cuts are needed to revive beleaguered domestic demand. We forecast two 25 basis point cuts before year-end



Source: Shutterstock

$3.2 billion June trade surplus

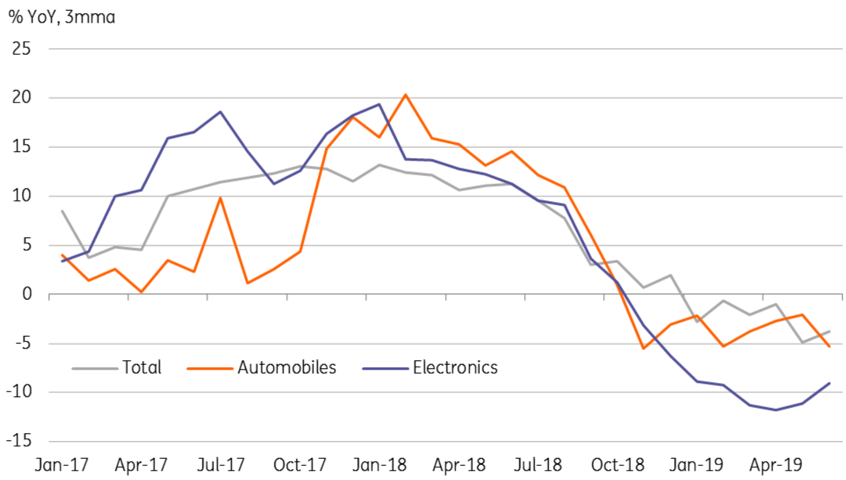
Higher than expected

Fourth highest trade surplus in June

Thailand's trade balance posted an unexpectedly large $3.2 billion surplus in June, the fourth largest monthly surplus on record. This happened as year-on-year (YoY) exports contracted by 2.2% while imports tumbled by 9.4% YoY compared to consensus estimates of -5.0% YoY and -2.5%, respectively. The corresponding growth rates for May were -6.2% and -0.7%.

Electronics and automobiles, with a combined 30% weight in total exports, remained the key drags; the global tech slump is depressing electronics exports and rising tariff barriers by the US are hurting automobiles and parts. Persistently weak domestic demand weighed on imports, while lower global crude prices likely kept a lid on fuel imports. Fuel makes up 17% of total imports.

Automobiles and electronics led export downturn



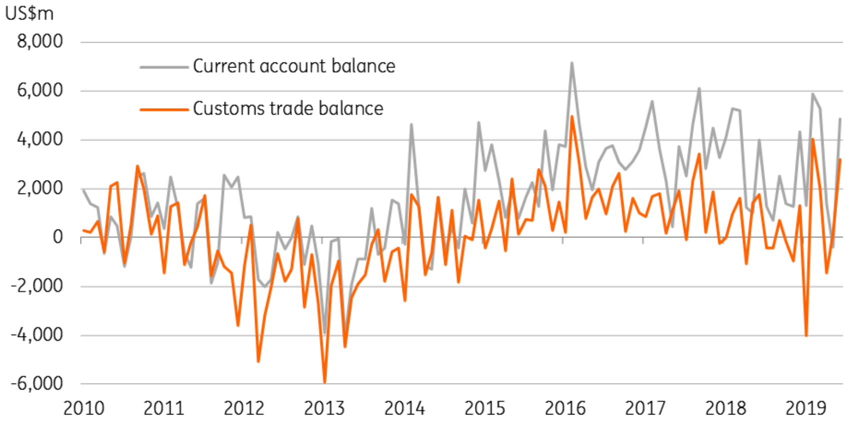
Source: Bloomberg, CEIC, ING

Persistent large current surplus

This puts cumulative export and import growth in the first half of the year (1H19) at -2.9% and -2.4%, respectively, both down sharply from +11.7% and +10.2% in 1H18. The 1H19 trade surplus of $3.9 billion, however, was little changed on the year.

The trade surplus is driving the current account surplus. Based on today's data, we estimate a close to $5bn current surplus in June (data due on 31 July), leading to a more than $18bn cumulative surplus in 1H19. A small narrowing from $20.8bn in 1H18 would far from satisfy the US Treasury, which currently has Thailand on its radar for currency manipulation. Having run at a rate of around 10% of GDP in 2016 and 2017, the current surplus dropped to 6.4% of GDP in 2018. We are considering an upward revision to our view of a further narrowing in the surplus to 4.8% of GDP in 2019 (consensus 6.6%).

Trade balance drives current account balance



Source: Bloomberg, CEIC, ING

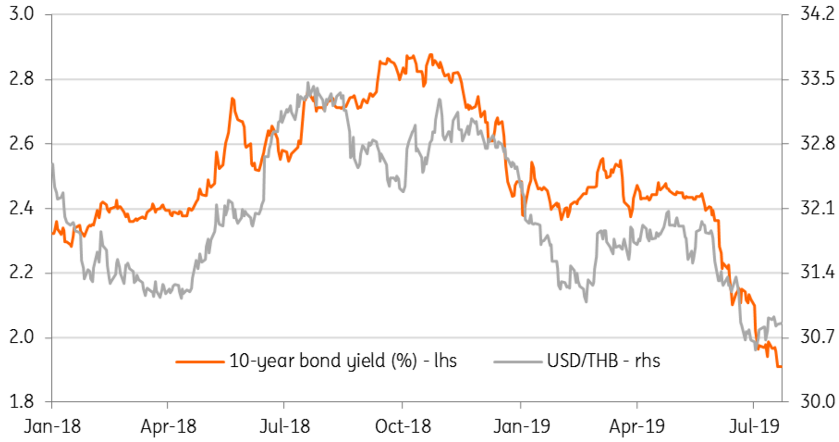
Efforts to curb THB strength in vain

A large trade surplus dampens the Bank of Thailand's recent efforts to rein in runaway currency (THB) appreciation this year. With a 5.5% year-to-date appreciation, the baht is the best performing Asian currency (second-best emerging market currency performer after the Russian rouble) this year.

Recently, the BoT has cut the limit on outstanding balances in non-resident THB accounts, including those for securities, to 200 million from 300 million. It has also tightened reporting requirement for non-residents' holding of debt securities issued in Thailand, making mandatory the disclosure of end beneficiaries of such holdings. While these measures have proven to be insufficient to arrest the currency appreciation, the authorities are considering more measures like reduction of bond supply and easing of rules on capital outflows.

Besides the persistently large external surplus, any efforts to curb THB appreciation pressure are currently being countered by USD weakness, as Fed rate cuts loom. A BoT rate cut may help to some extent, though it will take more aggressive central bank easing to revive beleaguered domestic demand. We forecast two 25 basis point BoT policy rate cuts in August and in the fourth quarter of the year.

Rallying Thai government bonds and the THB



Source: Bloomberg, ING

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