Good MornING Asia - 28 August 2018

Regional currencies look bid today, helped by a slightly weaker USD (on the Mexico trade deal) and stronger risk appetite, providing some support for EM assets. But it is really the about-face by the CNY that is providing the greater lifting power, thanks to the recently introduced countercyclical policy amendments

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Nafta is dead: Long live the US / Mexico Trade Agreement

The Canadian dollar is looking more supported after Mexico struck a deal with the US on trade. But this is not going to be a pushover. Nafta is dead. Will Canada be willing to sign up to a deal on Mexican terms?

The Mexico deal replaces, rather than amends Nafta

With Mexico signing on the dotted line of the new trade deal, the big question now is, will Canada follow? Trump is at this stage sounding quite downbeat about Canada's prospects. But then this gruff approach could simply be a way to get Canada to bend a little more to US will to make a deal possible. Certainly, there is no great love lost between President Trump and the Canadian Prime Minister Justin Trudeau. And there are still some issues for Canada, including dispute resolution and dairy protection to overcome. These may remain dealbreakers. We don't see the US softening its stance, so it is all for Canada to do. The US would like a deal done as soon as possible. But if this proves elusive, it appears that Canada has the right to sign the deal at a later stage. If they don't sign quickly, this deal will move through Congress for a simple Yes / No vote as a bilateral deal.

If that happened, then Nafta would indeed be dead. Even if Canada does come on board, Trump is jettisoning the name Nafta, which he feels has negative connotations, for the US / Mexico Trade Agreement (snappy, huh?). Presumably, it would then become the United States / Mexico / Canada Trade Agreement...

What Mexico has agreed to in order to get this deal done is:

- Increased regional automotive content to 75% from 62.5%

- 40-45% of workers in automotive earning $16 per hour
- Deal to be reviewed after six years (from an initial suggestion of five)
- Greater protection for copyright holders aimed at protecting internet and pharmaceutical companies where intellectual property is key
- Duty-free access for agricultural products to remain
- Mexico to take legislative action to recognise collective action by workers
- Recognition of Tequila and Mezcal as distinctive Mexican products and Bourbon and Tennessee whiskey as specifically American
- No restriction on market access for US named cheeses

The Mexico deal offers no hope for China

Far from ushering in a more reasonable attitude to free trade generally, it is safer to view this latest deal as one that the US has managed to bash into shape by sheer negotiating muscle. But there seems to be no appetite now for pushing forward with a deal for China. There is, right now, no visible interest from the US administration in pursuing talks with China over trade, and there will likely not be either unless China proposes some far-reaching changes to issues such as intellectual property protection and forced technology transfer. Meanwhile, the public consultation on the rate of tariffs to set on an additional $200 billion of Chinese imports is ticking away and will likely see new tariffs imposed by the end of September. So as far as China and Asia are concerned, this new Mexico deal solves nothing. Indeed, it strengthens the US position to play hard-ball with China. This doesn't look good for the region.

Regional currencies look bid today, helped by a slightly weaker US dollar (on the Mexico trade deal) and stronger risk appetite, providing some support for emerging market assets. But it is really the about-face by the Chinese yuan that is providing the greater lifting power, thanks to the recently introduced countercyclical policy amendments.

Asia Day Ahead

Thailand reports manufacturing data for July later today, with the consensus forecasting a slight slowdown in growth to 4.3% year-on-year from 4.7% in June. We are below consensus at 3.6%, as high base-year effects and tapering export strength in recent months are likely to slow manufacturing and thereby GDP growth in the current quarter. However, the recent step-up in hawkish rhetoric by Bank of Thailand officials, especially Governor Veerathai Santiprabhob about the need for monetary policy normalisation, will put all activity data under intense scrutiny. Creating some policy space for the future is one thing, but the economy isn’t screaming out for a policy tightening and higher rates could also threaten the fragile recovery reflected by still anaemic domestic demand. That said, our call for the BoT keeping policy unchanged this year remains at risk at the next policy meeting on 19 September.

South Korean consumer confidence data for August doesn't make happy reading. The index dipped further to 99.2 from 101.0 and shows few signs of abating the decline that has been going on since the end of last year. Policy initiatives to boost household incomes and increase worker leisure time seem to have backfired by limiting weekly hours and causing some loss of retail jobs. Recent policies to address some of these concerns such as the impact of higher minimum wages on small firms have yet to be felt and certainly aren't evident in this data. The BoK meets to set rates later this week (31 August). We see no chance of them hiking policy rates. The consensus is almost unanimous in supporting this view.

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