

## Good MornING Asia - 28 January 2019

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By Robert Carnell



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#### Singapore

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Opinion | 27 January 2019

## This week could matter, but then again...

Two uncertainties that underlie some of our key assumptions may get greater clarity this week - US-China trade relations and Brexit, but then we've been hoping for clarity for some time, without getting any.



### First Trade

If you accept the basic proposition that being hostile on trade and imposing tariffs on other countries will tend to lead to an offsetting market balancing act and a stronger currency, then there is some latent strength in the USD right now that could dissipate rapidly if the trade background were to improve. So with key Chinese trade negotiators en-route to Washington this week to try to thrash out a deal before the March 1 deadline, some USD weakness might hint at optimism for such talks.

The end of last week did see EURUSD surge from 1.13 to more than 1.14. This comes against a backdrop for this currency pair of a trading range centered very tightly on 1.14 since October last year. The Asia dollar index (ADXY) also reflects this dollar weakness, with the index pushing up through the 200-day moving average.

Failure to achieve a deal and renewed threats of higher tariffs could see the USD power stronger (lower) against currencies like the EUR, reversing these moves.

Our best guess...this week will probably not deliver any game-changers for the currency...we probably need to be much closer to the end of the deadline for that, and all that we are likely to

achieve this week are some optimistic sounding platitudes that merely postpone any eventual decision. That could leave currencies floundering close to their current levels, with optimism remaining, but the absence of anything more to drive them further.

Further down the track, we do anticipate there being a very upbeat sounding "Deal struck!" announcement closer to March 1, which will generate a softer USD, and see the ADXY power higher. But we also think this will be shortlived, as the announcement proves to have little substance, and may require unrealistic monitoring and progress on the Chinese-side to fully unlock any promised benefits. Unwinding this could be quite nasty, as we think a lot of good news has been priced in.

But it looks like we're still going to be stuck in the current ranges this week.

## If not plan B, then what?

This week might also see UK parliamentarians taking further steps to rule out a no-deal Brexit, and also ruling out Theresa May's bill - where there seems to be no possibility of a compromise on the Northern Ireland Backstop (no time limiting, and no appetite for a permanent customs union with the EU). If hardline Brexiters and the DUP cannot be brought on board, then the arithmetic for May's plan seems ever more insoluble. Time for a real plan B (or plan's C, D, E etc), could be this week, where an amendment to the government's bill would see MPs debate various alternatives, including a second referendum, or some form of much milder Brexit, such as a Norway-style membership of the single market but from outside the EU.

Sterling has already been showing signs of strength on thoughts of a less-Brexit future, trading up to 1.32 against the USD, and heading towards 0.86 on EURGBP, a level we last saw in May 2017. EURGBP traded at about 0.70 in 2015, weakening to 0.75-0.80 in the year ahead of the Brexit vote.

## Data to spew out of the US this week

This week, we might get rather more US data than we will know what to do with, as pent up numbers built up during the government shutdown come spewing out. We could get final factory orders, durable goods, trade balance (all for November), and December retail sales, housing starts, building permits as well as GDP (4Q advance), Non-farm payrolls (January), and the FOMC meeting.

At least the FOMC meeting should deliver no surprises. No change expected this quarter after the committee seemed to give in to pressure to ease back the pace of tightening - another reason for the USD to remain range-bound. Don't expect them to stay on hold forever though - this could coincide with a review of the trade situation to push the USD stronger in time.

## Asia data - lots

When asked what to look at if Chinese GDP data are unreliable, I quite often suggest industrial profits as a good directional indicator. I would stick by that assessment. The current series is running at a -1.8% YoY rate. The low for this series (since 2011) is -8.8%. Data for December should be released today...PMI data for the region, including for China are released later this week - which are also decent alternatives to GDP.

The rest of the week sees Australian 4Q CPI, which are unlikely to cause any concern to the Reserve

Bank of Australia. Korean industrial production for December will help us to see what progress Korea is making towards emerging from its current industrial malaise - our best guess, not much, and this should also be evident in its January inflation data, also released this week.

*And this from Prakash Sakpal on India:*

India's interim finance minister Piyush Goyal unveils the budget for FY2019-20 (April-March) on Friday, 1 February (Finance Minister Arun Jaitley is reportedly on medical leave). Growth will outweigh fiscal discipline as the Modi administration pushes its way for a second term in the general elections scheduled for May this year. As such, with an overshoot of the fiscal deficit in the last financial year and more likely again in the current year, hopes of fiscal consolidation receiving any prominence in evolving macro policy are largely misplaced. We see the revised budget for current FY2018-19 producing a deficit equivalent to 3.6% of GDP, well above the government's initial projection of 3.3% (consensus 3.5%). Our deficit forecast for FY2019-20 deficit is 3.4%. In either event of the incumbent government staying in power or the Congress-led coalition taking over the fiscal policy will likely remain overly be loose and deficit well above the 3% comfort level, the mark it never ever reached. Meanwhile, re-pricing for weaker public finances and rising political risk will keep the government bond yields and the USD/INR rate under upward pressure.

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## ASEAN morning bytes

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### EM Space: Investors await the Fed, China data and US-China trade talks for direction

- **General Asia:** Despite the temporary reopening of the US government traders will likely refrain from taking aggressive bets. The focus will be on the Fed meeting and China's manufacturing data out later in the week for direction.
- **Indonesia:** Indonesia is looking for more ways to narrow their current account deficit with the government unveiling a scheme to entice export growth. The plan will allow exporters of oil, minerals, and coal to apply for tax exemption for as long as they keep their foreign exchange earnings in the country. The measure is seen to boost the export sector and help narrow the trade deficit in 2019.
- **Philippines:** The Bangko Sentral ng Pilipinas (BSP) is looking to slash reserve requirements (RRR) with Governor Espenilla indicating that they "now see scope for further reductions in the RRR as we see inflation returning firmly to within target". Espenilla has vowed to slash the RRR to single digits by the end of his term and the first of two cuts may be in the offing as soon as the 1Q of 2019.

## What to look out for: Fed decision, US-China trade talks

- China industrial profits (28 January)
- Hong Kong trade data (28 January)
- US wholesale inventories (29 January)
- Hong Kong retail sales (30 January)
- China PMI manufacturing and non-manufacturing (31 January)
- US Fed meeting (31 January)
- India FY2020 budget (1 February)
- US non-farm payroll (1 February)

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# Singapore: Manufacturing misses the mark

Based on December manufacturing data, we estimate a downward revision to 4Q18 GDP growth from 2.2% to 2.1%



Source: Shutterstock

# 2.7%

December industrial production growth

Year-on-year

Lower than expected

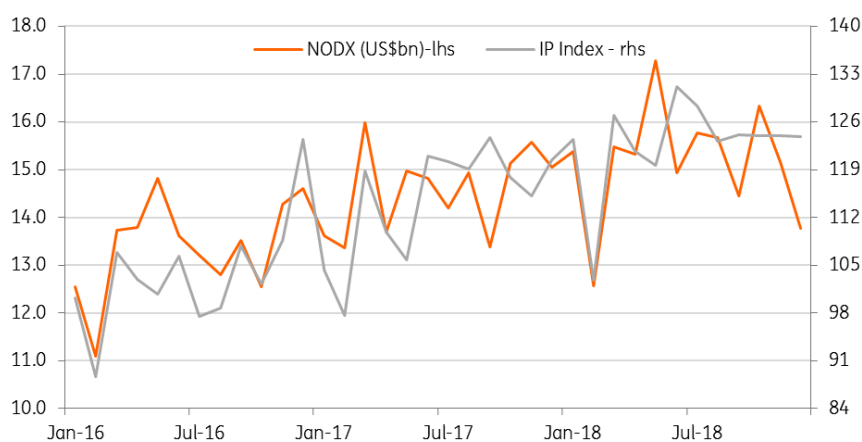
## Electronics depresses manufacturing

Industrial production rose by 2.7% year-on-year in December, slower than the 4.0% consensus estimate and down from November's 7.6% growth. The seasonally-adjusted 5.6% month-on-month fall was the steepest monthly fall in two years and this nearly wiped out monthly gains in the previous two months.

Electronics remained the weak spot; a 6.8% year-on-year and 10.9% month-on-month (unadjusted) fall wasn't a surprise though given a crash in semiconductor exports in December. Chemicals was another one. Pharmaceuticals held up steady, while transport and marine and

offshore engineering outperformed.

## Non-oil domestic exports and manufacturing growth



Source: Bloomberg, ING

## Possible downgrade of 4Q18 GDP growth

IP growth is tightly correlated with manufacturing GDP growth. The consensus estimate of IP growth in the last month of the quarter is typically derived from the manufacturing growth in the advance GDP for the quarter. It wasn't any different this time; the 5.5% YoY manufacturing GDP growth in 4Q18 implied a 3.8% December IP growth.

However, the below-consensus outcome for December suggests a downgrade to manufacturing GDP growth to 5.1%, which on its own should push the headline GDP growth for 4Q18 from 2.2% to 2.1% (revised data is due mid-February). This doesn't affect the 3.3% estimate of the full-year 2018 growth though.

### Policy implications

Singapore's small open economy is exposed more than most other Asian economies to the widely anticipated global growth slowdown. Even as GDP growth should remain within the official 2.5-3.5%, more likely closer to the lower end of the range, the risk of it falling short cannot be ruled out.

Against such a backdrop and having tightened policy twice in 2018, we believe the central bank (MAS) will choose the course of stable policy, by which we mean no change to the prevailing pace of appreciation, or the width or the level of the S\$-NEER policy band, at the next semi-annual meeting in April. Nor do we expect growth or inflation to deteriorate sufficiently to require a reversal of last year's tightening this year.

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