Good MornING Asia - 30 August 2019

An olive branch from China, but this trade war is far from over. We don't think China is about to acquiesce without the US removing a lot of existing tariffs and holding off from new ones, and the US needs a big concession from China on IP and openness, or it too will appear weak.

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Take the good news while it lasts

Markets opened with a positive hue this morning in response to China's offering to delay the introduction of new tariffs on the US in retaliation to the US' latest round of tariffs. President Trump told Fox News yesterday that talks with China on trade will occur today, though there are no more details.

Amidst signs that the US may be slowing faster than expected in 2Q19, could it be that US President Trump is about to look for a way to restore calm to markets by finding some sort of deal or truce with China?

Personally, I doubt it. For a number of reasons. Here are a few off the top of my head:

1. President Trump most likely believes that the US is weathering the trade war better than China - that is a moot point, but it doesn't matter what I think.
2. US public opinion would not welcome a weak trade deal with China as much as they would not welcome a slowing economy. This is a trade-off.
3. The decision to call off a trade war is as much a decision for China as it is for the US, and the sort of deal that China needs to get - reversal of existing tariffs, curtailment of new tariffs, better treatment for Huawei and other tech companies, is exactly the sort of deal that the US cannot deliver without appearing to cave in.

I won't go on.

So yes, markets are happy today as a goldfish is with a new rock in the tank to swim around, and around, and around.

I'd be gearing up for the next down-leg personally.

And Iris agrees..

Don't just take my word for it, here's what our Greater China Economist, Iris Pang thinks on the subject: "China's Ministry of Commerce said that to continue to have trade talks there must be necessary conditions for both sides. For China, this means the US would need to cancel the planned tariff increases.

I believe the market has interpreted recent developments too positively. It will be very difficult for President Trump to back down so quickly. It is also completely uncertain if there will be meaningful trade talks in September. Even if there are, both sides may just reaffirm to the other side their pre-conditions for further talks. And for both, this is likely to be that the other side first needs to make concessions. This implies no progress".

India GDP to buck weakening trend

India's GDP figure for the April-June quarter (1Q FY2019-20) today should testify to the elevated concern over growth evident from the massive stimulus the authorities have unleashed this year. However, the consensus of just a tenth of a percent dip in growth (5.7% from 5.8% in 4Q FY2018-19) doesn't quite come across as really worrisome. Nor do firmer exports and manufacturing growth suggest any real growth slowdown. Yes, there have been some pockets of weakness evident from slowing car sales and bank lending, though this largely reflects policy lags (pointed out by an RBI policymaker in the latest policy minutes) with less than 40% of the rate cuts so far being transmitted to the banking system.

We believe growth, in fact, improved in the reporting period to 6.0% making the additional RBI easing by 35bp rate cut earlier this month unnecessary. If so, we would reconsider our view of an additional 50bp of RBI rate cuts in the rest of the year, which isn't really a conviction call, but merely reflects the fact that the central bank is under pressure from the government to do more. (From Prakash Sakpal)

BoK - to hold today

We don't expect the BoK to follow up their July rate cut decision with another at today's meeting.

1. The KRW at 1209 is already very weak

2. The BoK will not want to front-run the US Fed
3. Following yesterday's budget there is less need to use monetary policy
4. Production data today hint that the electronics cycle is troughing - better news for growth.

The final point is good news not just for Korea. We also see evidence of an electronics cycle trough in data from Singapore, which may just side-step a feared recession as a result. So there is some genuine good news out there. I just don't think you should over-do it.

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Source: Shutterstock

Are we at the end of it? Not yet...

First of all, let's hope for no more escalation of the US-China trade rhetoric over the coming weekend even as a portion of new US tariffs on Chinese products takes effect on Sunday, 1 September. On a positive note, China's Commerce Ministry has just ruled out an immediate retaliation to last weekend's US tariff increase.

China has ample means for retaliation but thinks the question that should be discussed now is about removing the new tariffs to *prevent escalation. - Ministry of Commerce spokesman Gao Feng*

Absent additional trade bashing, the focus should return to where we are in terms of the real impact so far. China's purchasing managers index (PMI) and Korea's export growth, the first August releases from the region due over the coming weekend, may provide some insight. While we anticipate no departure from the recent trend of weak exports depressing manufacturing, at least the trend doesn't seem to have got any worse either. Nor has it bottomed.

The recent escalation of the tariff war provides no hopes of a near-term trade deal. As such, we are in for a long stretch of slow growth and increasingly challenging policy environment, as some central bankers have warned.

RBA policy meeting – a non-event

The Reserve Bank of Australia's Governor Philip Lowe has recently pointed to policy challenges as "political shocks are turning into economic shocks" and argued about government stimulus as more impactful than cutting interest rates, which risks pushing up asset prices.

This suggests the RBA meeting next week will likely pass as a non-event, while Australia's GDP growth has continued to slow (2Q GDP data is due next week). We, in line with consensus, expect no change to the 1.0% RBA policy rate, and a slowdown in GDP growth to 1.5% year-on-year from 1.8% in 1Q. However, continued negative capex growth in 2Q imparts a downside risk to our growth view. That said, we expect the RBA policy pause to continue until the end of the year.

More good news for BSP's easing, not for BI's

Meanwhile, the August inflation releases in Indonesia and the Philippines will inform on central bank policy paths in these countries. The consensus view of a sharp fall in inflation below 2% (to 1.8% from 2.4% in July – the lowest in three years) would delight the Bangko Sentral ng Pilipinas (Philippines central bank) looking to cut rates further.

In Indonesia, we see inflation ticking up in August (to 3.5% from 3.2%), supporting our view of no more rate cuts from Bank Indonesia for the rest of the year.

Asia Economic Calendar

Country	Time	Data/event	ING	Survey	Prev.
		Saturday 31 August			
China	0200	Aug Manufacturing PMI	49.5	49.6	49.7
	0200	Aug Non-manufacturing PMI	53.1	53.7	53.7
		Sunday 1 September			
South Korea	0100	Aug Trade balance (US$mn)	-	2420	2403
	0100	Aug Exports (YoY%)	-	-12.5	-11.0
	0100	Aug Imports (YoY%)	-	-4.5	-2.7
		Monday 2 September			
China	0245	Aug Caixin Manufacturing PMI	49.7	49.8	49.9
India	0600	Aug Nikkei Manufacturing PMI	-	-	52.5
Indonesia	-	Aug CPI (YoY%)	3.5	3.47	3.32
	-	Aug CPI core (YoY%)	-	3.17	3.18
Taiwan	0130	Aug Nikkei Manufacturing PMI	48.5	-	48.1
Thailand	0500	Aug CPI (YoY%)	0.8	-	1.0
	0500	Aug Core-CPI (YoY%)	0.4	-	0.4
South Korea	0130	Aug Nikkei Manufacturing PMI	-	-	47.3
		Tuesday 3 September			
Singapore	1400	Aug Purchasing Managers Index	-	-	49.8
South Korea	0000	2Q F GDP (QoQ/YoY%)	-/-	-/2.1	1.1/2.1
	0000	Aug CPI (MoM/YoY%)	-/-	-/-	-0.3/0.6
		Wednesday 4 September			
India	0600	Aug Nikkei Services PMI	-	-	53.8
Hong Kong	0130	Aug Nikkei PMI	-	-	43.8
Malaysia	0500	Jul Exports (YoY%)	-5.0	-	-3.1
	0500	Jul Imports (YoY%)	-4.0	-	-9.2
	0500	Jul Trade balance (RM bn)	7.1	-	10.3
		Thursday 5 September			
India	-	2Q Current account balance (Q) (US$bn)	-	-	-4.6
Philippines	0200	Aug CPI (YoY%)	-	-	2.4
		Friday 6 September			
Hong Kong	-	Aug Forex Reserves (US$bn)	-	-	448.5
Malaysia	0800	Aug Forex reserves- Month end (US$bn)	-	-	103.1
Philippines	-	Aug Forex reserves (US$bn)	-	-	85175.76
Taiwan	0900	Aug CPI (YoY%)	0.9	-	0.4
	0900	Aug WPI (YoY%)	0.5	-	-3.4

Source: ING, Bloomberg, *GMT

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Korean 2020 budget

South Korea's budget for 2020 includes an increase in government spending of 9.3%.

Source: Shutterstock

9.3% Increase in government spending

A net boost of about 2.2% GDP

"As expansionary as possible"

Finance Minister, Hong Nam-ki, has described the 2020 budget as being "as expansionary as possible". Perhaps a more literal translation would be "as expansionary as feasible", since clearly, more could have been done.

But the 9.3% increase in government spending is impressive, and even though this is whittled down in its effectiveness by some revenue increases form tax measures, that still leaves a net expansion of government spending of some KRW42tr, or about 2.2% of GDP.

As far as fiscal thrust goes, I'd have to say that this is pretty good, though critics point to Korea's debt-to-GDP ratio, which is now forecast to rise to 39.8% and argue that with such an enviably low debt ratio, the government should have done more.

This is probably not the final story

Such criticisms are somewhat harsh, in our view. Korea is facing what is undoubtedly one of the most negative cyclical backdrops for some time - a combination of a global technology slump in demand (volumes) and prices, exacerbated by the global downturn in trade, amplified regionally by the US-China trade and technology war.

The local spat between Japan and South Korea over war-time events doesn't help and is ill-timed, and the lingering economic weakness in both economies is no doubt a catalyst fueling this argument. It is hard to see a circuit-breaker to this barring outside intervention (the US?).

In any case, some more positive signs of a bottoming in the electronics cycle are becoming evident, and if so, further fiscal stimulus may not be necessary. If, however, this turns out to be a false dawn, then indeed, more will be needed. Today's budget does not preclude a further stimulus package later, and a supplementary budget can be forthcoming if necessary once the situation is more clear.

Budget detail

From what we can gather from newswire headlines, until a more detailed breakdown appears on the Finance Ministry website, the current budget aims to increase South Korean self-reliance in materials/parts, which sounds like a response to the loss of Japanese "whitelisting", and could be viewed as a deadweight loss of the ongoing argument.

But spending on automated "smart factories" sounds like a positive supply-side measure, though begs the side-question of how it helps to boost employment and wages..?

As for the debt-to-GDP ratio, such a low ratio is a rare asset these days, and should not be rashly traded away for a few years of debt-fuelled and unsustainable growth. South Korea is wise to tread with some caution. This won't be the only year when the Finance Ministry is asked to pull a rabbit out of a hat, so it makes sense to tread carefully with this finite resource.

Bank of Korea probably on hold

The Bank of Korea decides whether to follow up the July 25bp rate cut tomorrow with a further cut. We don't think they will. For one thing, this budget measure does some of their stimulus work for them. But mainly, we suspect they will want to see which way the Fed moves in September before committing to a further cut. We expect one further 25bp rate cut from the BoK in 4Q19.

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