

Good MornING Asia - 31 August 2018

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By Robert Carnell



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Not contagion, but negative backdrop returns

When you increase interest rates to 60%, and your currency just keeps falling, you know you have problems. This is Argentina and the peso, which has the dubious honour of performing worse against the USD this year than the Turkish Lira. Turkey is also back in the spotlight as the deputy central bank governor has resigned to take up a job at a development bank. The phrase, "rats off a sinking ship" does spring to mind. The Brazilian real and South African rand are also under weakening pressure.

Here in Asia, the usual suspects are feeling some heat, though not as intensely. But the backdrop does reinforce the need for Bank Indonesia and the Philippine central bank to follow through with the additional rate hikes we are forecasting this year. As for the RBI, they are already behind the curve and some catch-up hiking will be necessary. A 25bp hike in October will not be considered sufficient by markets who will likely sell the INR on the day if that is all they do.

CNY a little weaker - weighing on Asian FX

China has not abandoned its countercyclical policy, but in response to the announcement by Donald Trump yesterday that he is looking to introduce the new wave of China tariffs next week, as soon as the public consultation is over, the PBoC seems to be responding by allowing a modest depreciation of the yuan (CNY). This, rather than the Argentine / Turkish issues is most likely why the region's currencies are looking a little soft today. There is still room for a little more of this in the days ahead, without threatening a renewed run on USD/CNY 7.0.

Unfair trade

Donald Trump's latest response to the offer of zero tariffs on US cars coming into the EU in exchange for reciprocation on EU car exports to the US, has been met with a very telling response. President Trump has replied that this is, like China's offers, "not good enough", and then (bizarrely) citing EU consumer habits as favouring EU cars over US cars as the problem.

So...what you are really saying President Trump, is that...because the people of the EU prefer their cars to American ones, a level playing field on tariffs is not good enough? That the playing field actually needs to be tipped in favour of the US, to overcome these EU household's innate preference for their local product? For China, facing a new slew of tariffs as early as next week, this is a very important revelation as to the US game-plan for trade. The question is, does China view a substantial trade tilt in favour of the US a price worth paying for an end to this tariff war? We'll find out soon enough.

In short, the current US policy could easily be described as "Unfair Trade" policy. If anyone can see this any differently, please let me know.

Blessed are the cheese-makers?

Is it parmesan (hard cheese) or mozzarella (soft) for the Canadian trade negotiators today (yesterday's cheese-themed note is still working its way out)? There's more than just dairy at stake here, with NAFTA anti-dumping procedures one of Canada's red-lines. If no deal is achieved, the CAD will likely sell off. Though to be fair, this Friday deadline is somewhat artificial. This is more of a deadline of convenience.

Asia day ahead

The Bank of Korea (BoK) meet today with an almost universal expectation for no change in rates today (or in our view, any time soon). Though industrial production did bounce a bit in July, a 0.9%YoY growth rate is not good enough to merit increasing rates, not when inflation is also subdued, and further production weakness looms ahead, as suggested by inventory ratios.

The BoK Governor will make a press conference later, which we shall keep tabs on for any clues as to policy direction changes.

Japan's July industrial production was worse than last month (falling 0.1%), though it is maintaining a better annual growth rate than Korea (YoY 2.3% vs 0.9%YoY). In both economies, it is likely the consumer that will have to do the heavy lifting for GDP, with industry and net exports no longer reliable engines for growth.

China's manufacturing and non-manufacturing PMIs are also due today. The market is anticipating

a small decline in both. We are more inclined towards no change for the manufacturing sector to reflect offsetting supportive measures during the recent trade disputes.

And from my colleague, Prakash Sakpal:

Indian data on GDP for 1Q FY2018-19 (April-June quarter) and the government budget for July are also due. The consensus of just a tick down in GDP growth to 7.6% in 1Q from 7.7% looks optimistic to us, judging by the performance of other Asian economies over the same period. Underlying our 7% projection is a slowdown in manufacturing, even as export growth accelerated in the last quarter (exports account for a small share of GDP, average just 13% in the last five years). And with an oil-led import surge pushing the trade deficit higher, net exports will likely be a deeper drag on GDP growth. A sharp GDP slowdown isn't a good start to the year, the rest of which remains at risk of greater external uncertainty and rising domestic political risk.

As for the budget, the deficit in July should be close to June's INR 835bn; July typically is a weak month for both government revenue and expenditure. This will take the cumulative deficit in the first four months of the financial year to over 80% of the full-year budget target. Moody's was right in its warning recently about another overshoot of the deficit this year above the 3.3% of GDP target. While EM contagion is driving the USD/INR higher, domestic economic fundamentals aren't helping. We now see more upside than downside risk to our USD/INR 71.5 end-year forecast.

Thailand reports its balance of payments data for July. We know from a large swing in the customs trade balance to a deficit in July, that the current surplus narrowed sharply. Our forecast is for a \$2.6bn current account surplus, down from \$4.1bn in June. Still, the large surplus is supporting the currency (THB) outperformance relative to some Asian peers, obviating any need for central bank action to offset EM market contagion.

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Source: Shutterstock

➔ Get ready for an exciting September

The trade war will persist as a major overhang on global and Asian markets. The consultation period for further US tariffs on China ends next week (5 September) after which Washington could impose duties on another \$200 billion worth of Chinese goods. China has pledged \$60 billion of retaliatory tariffs on US products.

We believe the markets are pretty much priced for this oncoming trade risk and are unlikely to be jolted by it. Hopefully, a stable start to the new month will also bring more clarity on a host of

other important economic issues in developed markets; the Fed's tightening cycle, the ECB tapering timeframe, and the Brexit deal. And if that's not enough, the contagion risks from emerging economies continue to linger with Argentina and Turkey remaining on edge, so we'll be in for a month full of excitement and elevated market volatility.

On the data front, next week in Asia is packed with trade, manufacturing and inflation releases from across the region. There is little on the policy front except for a Malaysian central bank (BNM) meeting which will likely be a non-event, though ugly inflation data from the Philippines will keep the central bank there (BSP) on its toes.

➔ Export performance still not too bad

August trade releases from Korea and Taiwan, the first for the month from the region, will be closely watched for the trade war impact. The focus will also be on the manufacturing purchasing manager indexes (PMIs) from around the region, particularly the new export orders component.

Our house forecasts for export growth - 11% year-on-year for Korea and 5% for Taiwan - imply positive month-on-month gains for two consecutive months, indicating there has been no impact yet from escalating trade tensions. Already-released data showing a 15% year-on-year surge in Korean exports in the first 20 days of August confirms this point.

Semiconductors continue to be the main driver of Korean exports but tariff-hit steel exports are also holding up. It looks like the shift in trade away from the US to other countries has already started, judging by the recent surge in Korea's and Japan's steel exports to India.

➔ Philippines inflation monster rears its head higher

There's a slew of August inflation data from the region next week but figures from the Philippines' will be the most important. We see inflation surging past the 6% mark for the first time in over a decade from 5.7% in July, consistent with the consensus centred on 6%. Bad inflation data will keep the central bank (BSP) on its toes, even as the currency (PHP) has stabilised from a Turkish-led downturn in early August.

High inflation and twin-deficits (trade and government) have kept the PHP under intense weakening pressure this year, with a 6.6% year-to-date depreciation. The question is, will the BSP overlook the inflation data and wait for the recent 100 basis point rate hike to take effect. The current economic backdrop suggests the BSP policy tightening has further room to run. The next BSP meeting is on 28 September. We expect the BSP to pause at this meeting but hike again in the final quarter of the year.

Asia Economic Calendar

Country	Time	Data/event	ING	Survey	Prev.
Saturday 1 September					
South Korea	0000	Aug Exports (YoY%)	11.2	-	6.2
	0000	Aug Imports (YoY%)	12.3	-	16.2
	0000	Aug Trade balance (US\$m)	6826	-	6912
Monday 3 September					
China	0245	Aug Caixin Manufacturing PMI	50.7	50.6	50.8
India	0600	Aug Nikkei Manufacturing PMI	52.8	-	52.3
Indonesia	0500	Aug CPI Core (YoY%)	-	-	2.87
	0500	Aug CPI (YoY%)	3.3	-	3.18
Singapore	1400	Aug Purchasing Managers Index	52.5	-	52.3
Taiwan	0130	Aug Nikkei Manufacturing PMI	53	-	53.1
Thailand	0400	Aug CPI (YoY%)	1.3	-	1.46
	0400	Aug CPI Core (YoY%)	0.8	-	0.79
Thailand	0030	Aug Nikkei Manufacturing PMI	50.2	-	50.1
South Korea	0130	Aug Nikkei Manufacturing PMI	48.8	-	48.3
Malaysia	30	Aug Nikkei Manufacturing PMI	48.5	-	49.7
Tuesday 4 September					
South Korea	0000	2Q F GDP (QoQ/YoY%)	0.7/2.9	-/-	0.7/2.9
	0000	Aug CPI (MoM/YoY%)	-1.1	-/-	0.2/1.5
	0700	Aug CPI core (YoY%)	0.9	-	1.1
Wednesday 5 September					
India	0600	Aug Nikkei Services PMI	53.2	-	54.2
	-	2Q Current Account Balance (Q) (US\$bn)	-	-17	-13.047
Hong Kong	0130	Aug Nikkei PMI	-	-	48.2
Malaysia	0500	Jul Trade Balance (RM bn)	4.1	-	6.05
	0500	Jul Imports (YoY%)	0	-	14.91
	0500	Jul Exports (YoY%)	-5	-	7.63
	0800	Overnight Policy Rate	3.25	-	3.25
Philippines	0200	Aug CPI (YoY%)	6.1	-	5.7
Taiwan	0800	Aug Forex Reserves (US\$bn)	458	-	458.5
	0900	Aug CPI (YoY%)	1.5	-	1.75
	0900	Aug WPI (YoY%)	2.5	-	7.02
Thursday 6 September					
Malaysia	0800	Aug 30 Forex Reserves - Month End (US\$bn)	-	-	104.2
South Korea	0700	Jul Current A/c Balance (US\$m)	7150	-	7377
Friday 7 September					
China	-	Aug Forex Reserves (US\$bn)	3121	-	3117.95
Hong Kong	-	Aug Forex Reserves (US\$bn)	-	-	431.9
Malaysia	0500	Jul Industrial Production (YoY%)	0.5	-	1.1
Philippines	-	Aug Forex Reserves (US\$bn)	-	-	76721.7
Taiwan	0900	Aug Exports (YoY%)	5.1	-	4.7
	0900	Aug Imports (YoY%)	22.2	-	20.5
	0900	Aug Trade balance (US\$bn)	2.25	-	2.24

Source: ING, Bloomberg

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