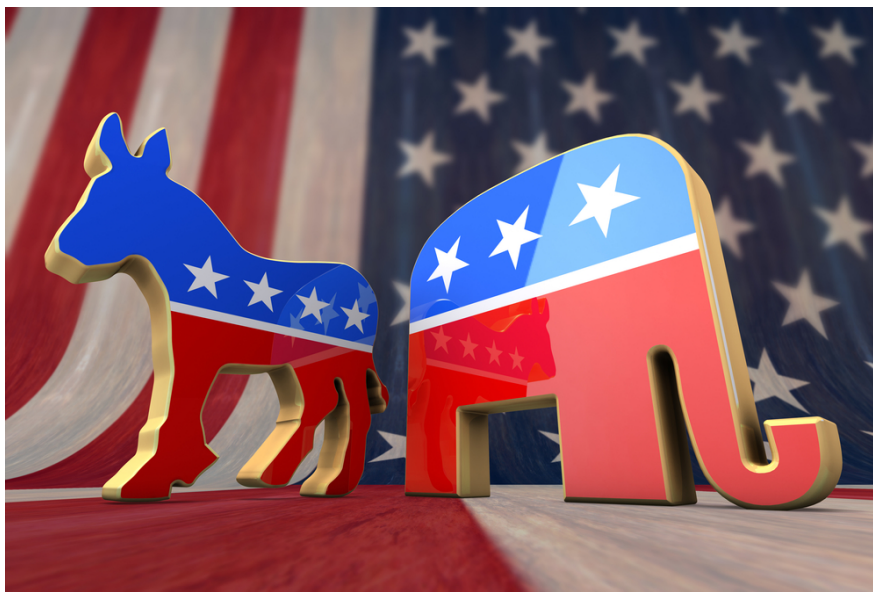


And the winner is....

While we wait for the outcome of the US mid-term elections, everything else is on hold - but what difference could it make to Asia?



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The most watched mid-term I can remember

For the longest time, mid-terms were something that simply happened. Sometimes there was a notable shift in control of Congress. But I don't remember a mid-term being contested as avidly as this one, which probably goes to show the strength of feeling on both sides of the political divide about how this administration is faring.

As of writing, the polls on the East coast are closing, but it will be about early lunchtime in Asia before we get some sense of what has happened and can try to draw some conclusions.

For the views of our US economists and FX strategists on how this may all pan out, the note, ["Feeling Blue?"](#) is well worth a read. We are looking forward to the on-the-spot reaction of James Knightley writing from Texas later today, where he will be in the heart of the exciting Beto O'Rourke vs Ted Cruz Senate race.

But while this is good TV and fills the papers (and this note), what, if anything does it mean for us here in Asia?

What it all means for Asia...

I think there are a number of things to consider:

1. Market reaction. If Donald Trump secures both the House and Senate, then we can look towards a big middle-income tax cut next year and possibly increased infrastructure spending that will stave off any Wile. E. Coyote fiscal crash. This pushes back the likelihood of any US economic slowdown or technical recession. As a result, although this is good news for equity markets short term, it also suggests the Fed will be in hiking mode for longer, and the dollar will consequently be stronger - Asian currencies weaker. Conversely, a Democrat-controlled House would make any further fiscal expansion less likely, the dollar would weaken on softer growth and earnings expectations and bond yields and the dollar would be lower (weaker). Equity volatility - difficult to say, could fall as this is the market consensus, but it isn't clear-cut.
2. Economic policy: When we say economic policy, we are really talking about trade policy, since this is about all the President has left if he loses control of the revenue-raising House of Representatives. In my view, and I think in the view of a growing consensus, a loss of the House by the Republicans would likely encourage more aggressive trade policy, notably against China - probably not against the EU or close neighbours ([see also this point in the earlier referenced note](#)). Forget the recent olive-branch offered to China of talks at the G-20. A bad mid-term for Trump would, in my view, harden the US President's attitude towards any deal. Now at this point, there is not much else from China that could be tariffed, but the existing tariffs could be raised.
3. As well as China, don't forget Japan. PM Abe has been trying to cultivate good relations with the US president, but with Japan's economy doing better than for some time, and the trade balance trending around \$300bn per month, Japan could also come into the cross-hairs of the US. Other countries that could suffer the ire of a renewed trade push include almost any Asian trade surplus country - Thailand is on this list, and despite the re-worked Korus trade deal, South Korea might come back into the spotlight - the Korus deal was not particularly onerous, and the US trade deficit with most of its bilateral trading creditors has not got any better. Now a more aggressive US on trade policy is likely to spell a stronger USD. That seems in some contradiction to the earlier comment that a successful mid-term was likely to be good for the dollar. It isn't, but whereas a mid-term victory for Trump is generally a strong dollar outcome, a mid-term defeat could spell a stronger dollar against specific Asian currencies.

One way or another, we should have a better idea of how the land lies by the end of the day.

New Zealand - great labour market report, strong NZD

The Reserve Bank of New Zealand (RBNZ) Governor, Adrian Orr, has for some time painted a fairly mediocre picture of the NZ economy and prospects for any policy change, with risks of rate cuts, flagged as a future possibility just as much as rate hikes. As of today, the rate cut scenario for New Zealand looks extremely unlikely, and the odds of a nearer term hike have improved substantially, pushing the NZD up against the USD, and also, the AUD. In Australia, in contrast, although the labour market is also doing well, the rest of the economy looks distinctly patchier, and the Reserve Bank of Australia, although still leaning towards eventual tightening, seems in no mood to do anything this side of Christmas, that's Christmas 2019 incidentally.

The unemployment rate in New Zealand has dropped to a 10-year low of 3.9% (from 4.4%). Despite the unemployment rate fall, the participation rate has risen, and there is now a surge in hourly wages growth, which at 1.4%YoY, is the fastest they have grown since 2014. The RBNZ meet tomorrow to discuss rates incidentally... I still think wages growth is too low for them to hike at this meeting, even if the direction and improvement in wages is very positive. But I also think the RBNZ will have to ditch the potential rate cut talk and acknowledge the possibility that if wages growth puts on another spurt next quarter, rates could be going up a whole lot quicker than anyone has imagined.

With the Australian economic data remaining mixed, and the RBA in benign neglect-mode the likelihood of AUDNZD testing (at least) the April 2018 low in the coming weeks and months is looking very strong.

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