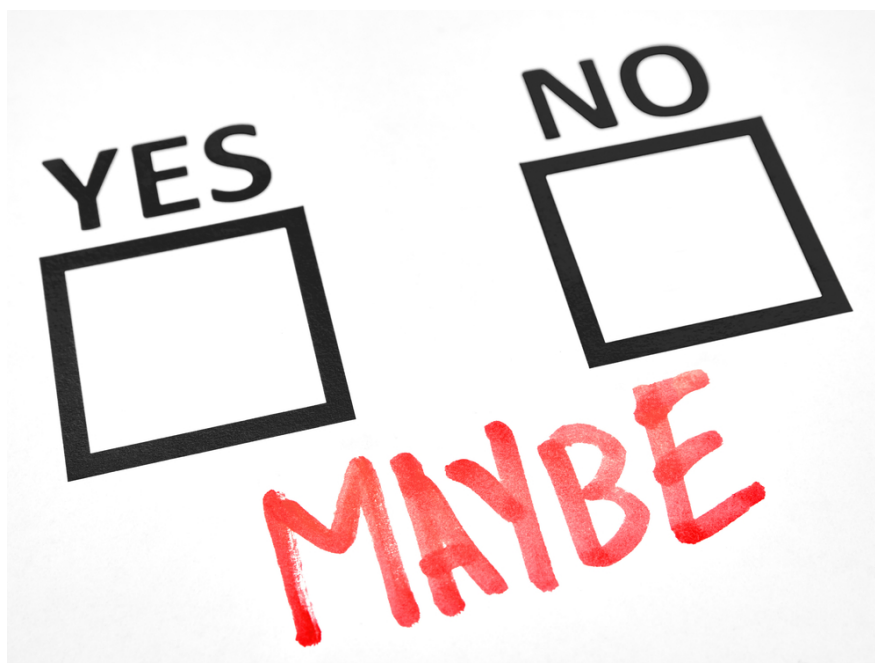


Trade or no trade?

Trump professed to being a "Free-trader" in Davos, but then he pulled out of TPP on Day 1 of his Presidency. Mnuchin says he wants a weak dollar. Trump says he wants a strong one, then so does Mnuchin - what's going on?



undecided

More is less

There comes a point where more information leads to less understanding, and this is where I am today with the Trump administration. The weak / strong dollar and free-trade / no-trade gyrations of Treasury Secretary Mnuchin and President Trump leave us no wiser. The same may be true of this week's State of the Union Address. I anticipate this to feature long on the policy achievements of last year (fiscal reform) and paint a rosy picture of the future based on those successes. Add in some wishful thinking about infrastructure spending, and a dollop of immigration control, and it will provide an optimistic vision of an America that is thriving under Trump's "America First" policies.

And at face value, he is not wrong. Yes, the 4Q17 GDP data last week were a little shy of consensus, but this was still a figure close to 3% growth, with more on offer in 2018. And yes, payrolls growth may start to come in a little softer from now on, as Friday's figures may attest, but

employment cannot grow at a 200K per month rate forever (at least without more immigration). Further, with corporate America feeling a little cash-rich thanks to tax reforms, we may even see a little of this spill over into wages growth - providing some further momentum for the economy, and some additional food for thought for the Federal Reserve (Fed).

If its all good in the US, why is the USD tanking?

But the apparently rosy story is not reflected so well by markets. Stocks are holding up well and earnings provide further grounds for optimism. But in fixed income markets, rising bond yields suggest anxiety about 1) future inflation (breakeven inflation rates now >2.0%) 2) concern about the path of the USD (higher yields needed to compensate for expected dollar weakness) and 3) anxiety about fiscal and external balances (at least relative to the Eurozone).

The FOMC meets again this week for what will be Janet Yellen's last meeting as FOMC chair. We don't think we are in for any rate hike surprises at this meeting. In my view, Yellen has been a steady and reliable Fed chair - exactly what the market needed at a particularly difficult transition in the economy and financial markets. She leaves the chair with the economy in a better place than it was when she took it over. Looking back over her time at the helm, I doubt she will particularly miss the semi-annual testimonies to Congress. Robust questioning is not the same as rudeness. Jerome Powell takes over at a potentially tricky time, though, After so long without inflation or wages growth, this could be exactly the moment that the Fed's resolve is tested if both metrics start to tick up. There is a very good chance they will. But having been in cautious tightening mode for a long time, I think the Fed has lessened the risks of this running away from them. I am relaxed about the US. And in turn, this means I am relaxed about the global economy.

Author

Robert Carnell

Regional Head of Research, Asia-Pacific

robert.carnell@asia.ing.com

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