Trade rhetoric still roiling markets

From "not this side of the election", a December trade deal complete with tariff rollbacks is the talk of markets this morning - this is not all in the price

President Donald Trump, left, meets with Chinese Vice Premier Liu He, front right, at the White House in Washington

Source: Shutterstock

USDCNH provides some insight into the trade war

I frequently choose the 10Y US Treasury yield as the benchmark for global market risk sentiment. However, in this part of the world, and especially when considering market expectations on the trade war, USDCNH is probably as convenient a place to start, and also provides more of an Asian-flavour to my note.

The question is, not just whether we will get a deal before December 15, which in my view remains a coin-toss. Rather, it is, whether the market has fully priced in any deal or not.

My guess, and it is no more than that, is that this is at best only partially priced in. Consider the last few days. Today, reports suggest a trade deal with tariff rollbacks is now looking probable before December 15. But then only a day previously, President Trump had suggested that we may not get a deal until after the Presidential Election. Prior to that, we are back to hearing that a deal was "very close".

USDCNH was trading at a little over 7.04 before the downbeat Trump announcement sent it to just under 7.09. The more optimistic commentary this morning has taken it back down to 7.05, though still above where it was a couple of days ago.

Being whipped around like this does not encourage markets to take strong positions. Neither those who might believe a trade deal is likely, nor trade pessimists, will be prepared to go "all-in" when the environment and rhetoric change so abruptly. So were we in fact to get a substantive deal, then I would think we should be eyeing USDCNH moving closer to 7.0 again. But if tariffs get imposed, then a spike above 7.10 also seems plausible.

In US Treasury terms, the comparable peaks and troughs on the volatile newsflow in the past three days have been a peak of 1.82% and a trough of 1.715%. So pick your own numbers, but I could imagine a good news scenario sending US Treasuries back towards their November high of 1.95% or even eyeing 2.0%, but a bad news outcome taking them towards the 1.55% October low.

It is perhaps not all that surprising that today's 1.77% figure is practically in the middle of that range, maybe slightly tilted toward good news. But it suggests that whether you are looking at USDCNH, USDKRW, US Treasuries, or equity markets, there is still plenty to play for over the coming days as we near a deal/no deal on the Trade war.

Asia Day ahead

The main Asia interest today comes from the Reserve Bank of India (RBI). There is a widespread expectation that the RBI will cut rates again following the disappointing 4.5% GDP growth in 3Q19. And this is in spite of rising inflation. Most market forecasters are pencilling in a 25bp rate cut taking the repo rate to 4.90%.

One or two forecasters, including ourselves, are forecasting a bigger cut. In our case, 40bp. This would take the repo rate down to 4.75%. There is a precedent for non-25bp cuts. The 7 August cut was 35bp. So 40bp is certainly not ridiculous and takes the repo rate to a more satisfying 4.75% level.

For a longer more considered view, read this by Prakash Sakpal published recently.

Otherwise, Philippine inflation data for November out this morning could come in above the consensus 1.2% forecast, causing Governor Diokno to pause from cutting rates further this month. We still believe there is more to come from the Philippine Central Bank (BSP) next year, probably in February. Here is a link to what Nicholas Mapa has to say on the subject.

Iris Pang in Hong Kong SAR writes this about efforts to offset the local macro impacts of the protests there. "The Financial Secretary released another batch of relief measures, which included tax payments by instalment upon request and some waivers for electricity and water usage for firms, including catering businesses. We think that the impact of these measures will be small, as tax payments by instalment have long been allowed if tax-payers are in difficulty. And the waivers for utility charges have a low upper limit. These relief measures will only likely have a significant positive impact if violent protests cease".

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