Economic commentary

07/12/2018

Week Ahead Asia-Pacific Economic Preview

- **Release of flash PMI surveys give early clues to full Q4 economic performance and price trends of major economies**
- **China data updates**
- **ECB, Philippines and Brazil set monetary policy**
- **Key UK Brexit vote**
- **Special focus on US-China trade war**

Release of Flash December PMI surveys in the coming week will offer early signals into the economic performance at the end of the fourth quarter. China's clutch of data updates will also receive strong attention, while the Philippines' central bank Monetary Board will meet to make their monetary policy decision.

Other data highlights for Asia include updated estimates to Japan's GDP, South Korea's unemployment data as well as industrial production figures for Malaysia and India. Elsewhere, Brexit developments in the US and the ECB's policy meeting will be especially keenly watched.

Our special focus this week looks at recent development in the US-China trade war.

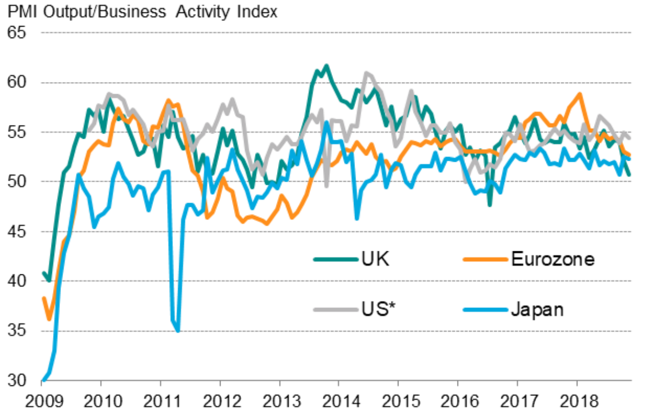
Flash PMI surveys

Flash December PMI data for the US, Eurozone, Japan and Australia will provide the first signals of economic performance and price trends for the whole final quarter of the year. The forward-looking sub-indices will be especially closely eyed for insights into growth trends at the start of 2019.

The flash data come on the heels of November's PMI surveys, which showed global PMI holding at a two-year low as worldwide exports fell for a third month running. While the US economy continued to show encouraging resilience and Japan showed signs of recovering from natural disasters, European growth continued to slow.

In addition to the flash PMI for Japan, GDP data will also be updated for the third quarter, which are widely expected to indicate a steeper than previously estimated drop in economic activity, caused mainly by and earthquake and typhoons. Encouragingly, Nikkei PMI data have since rebounded.

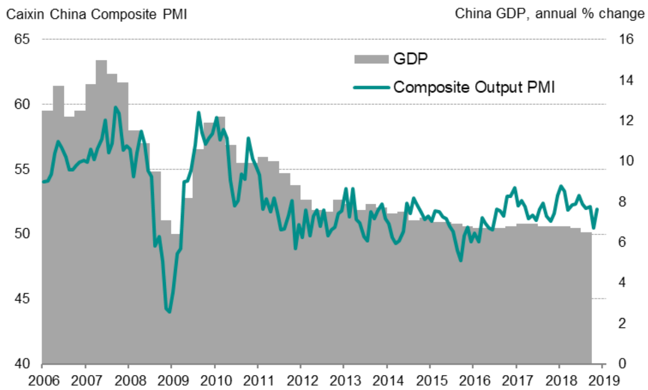
PMI surveys (manufacturing and services output)



* US uses November flash PMI.

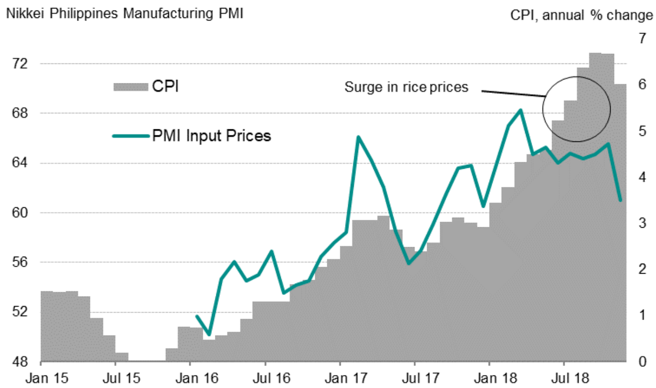
Sources: IHS Markit, Nikkei, CIPS.

China PMI and economic growth



Sources: IHS Markit, Caixin, NBS

Philippines PMI and consumer inflation



Sources: IHS Markit, Nikkei, PSA

Continued…

China data update

With Caixin China PMI surveys hinting that the pace of economic growth has cooled further in the fourth quarter as trade tensions continued to curb exports, analysts will keenly monitor the clutch of official statistics released in the coming week, including fixed asset and foreign direct investment, credit growth, retail sales and factory output.

India inflation and production

Updated industrial production for India are expected to show an improved annual rate of growth, corresponding with more upbeat survey data in recent months. Consumer prices inflation is expected to have cooled, however, vindicating the Reserve Bank's recent decision to keep rates on hold.

Philippines monetary policy

Even though the headline inflation rate in the Philippines eased to 6% in November, it remained well above the upper bound of the central bank's 2–4% target range, which could add to pressure for tighter monetary policy. The Bangko Sentral ng Pilipinas (BSP) meets next week to set monetary policy, with the decision likely to be a close call. The latest PMI survey showed robust manufacturing activity in November, buoyed by strong order inflows. However, there were also signs of cooling inflationary pressures.

ECB asset purchases in spotlight

In Europe, December's flash PMI surveys are preceded by the European Central Bank's policy meeting, at which the central bank has already stated it expects to announce the halting of asset purchases. More attention will therefore likely be placed on the bank's new growth and inflation projections, with especially interest on whether policymakers see the recent softening of growth as temporary.

Not forgetting Brexit…

Other key releases elsewhere include fresh GDP data for the UK, as well as updated official labour market data, which will help provide guidance as to how the economy is faring as Brexit uncertainties intensify. The week starts with a key parliamentary vote on the UK's withdrawal agreement from the EU, which the government is currently widely expected to lose, casting doubt on the Brexit process.

Other key events include the release of US inflation and producer prices, Japan's Tankan survey and machinery orders, Russian GDP plus Brazil's monetary policy meeting.

Monday 10 December

Japan GDP (final, Q3)

Australia home loans (Oct)

Germany trade (Oct)

UK GDP and trade balance (Oct)

UK industrial production and construction output (Oct)

US JOLTs job opening (Oct)

Tuesday 11 December

Australia business confidence (Nov) and house price index (Q3)

Philippines trade (Oct)

UK jobless rate and earnings (Oct)

UK employment change (Oct) and claimant count change (Nov)

Euro area and Germany ZEW surveys (Dec)

US producer prices (Nov)

Wednesday 12 December

South Korea unemployment rate (Nov)

Australia consumer confidence (Dec)

Japan machinery orders (Oct)

Malaysia industrial production (Oct)

China FDI (Nov)

Euro area industrial production (Oct)

India current account (Q3) industrial production (Oct) and inflation (Nov)

US inflation (Nov)

Russia GDP (final, Q3)

Thursday 13 December

Brazil interest rate

RBA bulletin and Australia new home sales (Nov)

Germany and France inflation (final, Nov)

Philippines interest rate decision

ECB monetary policy meeting

Friday 14 December

IHS Markit flash PMI surveys for Australia, Japan, US, Eurozone, Germany and France (Dec)

Japan Tankan surveys (Q4)

Australia jobless rate (Nov)

China FAI, industrial production, retail sales, new yuan loans, M2, total social financing (Nov)

India WPI (Nov)

Special Focus

A Christmas Truce in US-China Trade War: Assessing the Economic Impact

By Rajiv Biswas, Asia-Pacific Chief Economist, IHS Markit

The 90-day truce agreed by President Trump and President Xi at the G-20 Summit is a positive outcome for the near-term Asia-Pacific trade outlook. The deal temporarily suspends the US plan to hike tariffs on USD200 billion of Chinese exports to the US from 10% to 25% on 1st January 2019.

US-China Truce at the G-20 Summit

At their bilateral meeting held at the G-20 Summit in Buenos Aires, US President Donald Trump and Chinese President Xi Jinping agreed a truce in the US-China trade war for a period of 90 days starting from the date of the US-China meeting at the Summit.

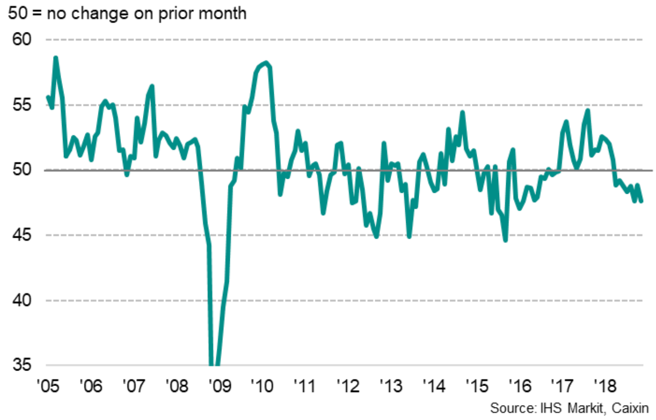
During this period, both leaders agreed that no further trade war escalation measures will be implemented. Meanwhile, efforts to find a compromise trade deal will continue. With another US-North Korea summit being planned for early 2019, the US will be seeking China's cooperation to facilitate a successful summit between President Trump and North Korean leader Kim Jong Un, in order to make progress towards a durable agreement for denuclearization of the Korean peninsula.

Impact of the Trade Truce

The 90-day truce is a positive outcome for the near-term Asia-Pacific trade outlook, as it averts the previous US plan to hike tariffs on USD 200 billion of Chinese exports to the US from 10% to 25% on 1st January 2019. This large US tariff hike would have hit Chinese exporters hard, so it provides substantial relief for China's export sector, at least temporarily. Such a large tariff hike would also have had significant transmission shocks for other Asian economies, due to the integrated Asian manufacturing supply chain providing raw materials and intermediate goods for China's manufacturing sector.

There are clear signs that the existing tariffs are already having a noticeable impact on China's exports. The Caixin China General Manufacturing Purchasing Managers' Index™ (PMI™) for November showed that weaker external demand continued to weigh on overall manufacturing sales, as export orders declined further midway through the final quarter of 2018. The survey showed that Chinese new export orders have been contracting in each of the past eight months. According to survey responses, a key factor contributing to the slowdown in Chinese manufacturing export orders has been the impact of US tariff measures that have been implemented during 2018.

Caixin manufacturing PMI new export orders



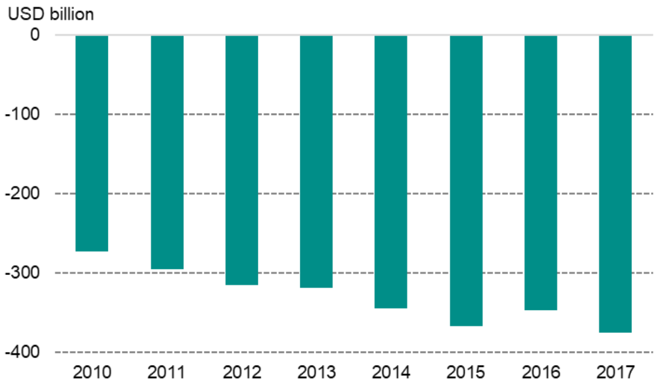
The postponement of the further tariff hike from 10% to 25% on USD 200 billion of Chinese products which had been originally scheduled for 1st January 2019 will create an additional window for US purchasers to continue ordering Chinese imports at the 10% tariff rate, which may temporarily boost US orders for Chinese exports. As part of the trade truce agreement, China will be ramping up orders of US products, notably for agricultural and energy products, which may also create a near-term boost for Chinese orders for US exports.

The US-China trade truce also signals that renewed bilateral trade dialogue will intensify in early 2019 to try to find a compromise bilateral trade deal. However, China would need to agree to very substantial measures within 90 days in order to negotiate a compromise trade deal. Key areas where China will need to make substantial offers to the US will be to significantly narrow the bilateral trade deficit, as well as to substantially strengthen Chinese regulatory protection for the intellectual property rights of US firms.

China's Ministry of Commerce has stated that China and the US will move ahead with trade negotiations during the next 90 days and that China is confident that an agreement can be implemented. The Chinese Ministry of Commerce also stated that China will work to implement specific issues agreed upon as quickly as possible. The US Administration has indicated after the bilateral talks at the G-20 Summit that China had made substantial commitments to ramp up imports of US agricultural and industrial products, in order to take imminent action to narrow the US bilateral trade deficit.

President Trump and President Xi have also agreed that during the next 90 days, bilateral negotiations on structural changes will be conducted with respect to technology transfer, intellectual property protection, non-tariff barriers, cyber intrusions and cyber theft.

US merchandise trade deficit with China



Source: US Census Bureau.

Auto Sector

A key issue for the bilateral trade negotiations is also tariffs on autos. US Trade Representative Robert Lighthizer stated on 28th November that China currently imposes a tariff of 40% on US automobiles, much higher than the 27.5% tariff rate that the US imposes on imports of autos produced in China, and that he would be examining available methods to equalize the tariffs on autos. The US Department of Commerce is currently conducting an investigation of imports of autos and auto parts under Section 232 of the US Trade Expansion Act of 1962, which could result in potential remedies in the form of increased US tariffs on auto imports from some nations.

President Trump has indicated that China has offered to remove its tariffs on its imports of US autos during the bilateral talks held at the G-20 Summit. "China has agreed to reduce and remove tariffs on cars coming into China from the US. Currently the tariff is 40%," President Trump tweeted on 2nd December 2018.

Outlook

The China-US trade war truce is positive as it has re-established a framework and roadmap for intensive bilateral negotiations over the next three months to try to find a compromise trade deal. The US decision to delay increasing the 10% tariff rate on USD 200 billion of Chinese products to 25% also provides some near-term relief for Chinese exporters, who had faced a considerable loss of US new orders due to the steep increase in tariff rates that had been scheduled for 1st January 2019.

However, if a US-China trade deal cannot be reached within 90 days, the US administration has signalled that it would then proceed with its plan to ramp up the tariff rate on USD 200 billion of Chinese imports from 10% to 25%. Furthermore, President Trump has said that he may also consider imposing additional tariffs on all remaining Chinese exports, which amount to an additional USD 267 billion of Chinese products.

For further information:

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