

ASIA WEIGHS A TRUMP PRESIDENCY



With Mr. Trump officially inaugurated as the 45th President of the United States, the world is now shifting its focus to the implementation of his policies during his first 100 days.

From an Asian investor's point of view, the only significant threat likely to manifest itself within the first 100 days is the potential introduction of tariffs, which the President could theoretically introduce of up to 15%, for up to 150 days from day one¹.

Nevertheless, Asian investors, focusing on the longer term, remain unnerved by Mr. Trump's stance on China's trade and currency policies. Asian concerns have been further fueled by the aggressive tone adopted by both the Secretary of State² and Commerce Secretary³ nominees during their Senate confirmation hearings.

While markets globally are digesting the ramifications of a Trump presidency (apart from US equities which have enthusiastically rallied), Asia has been less impressed. Asia's policy fall-out fears, however, may have been over discounted.

At the legislative level, for example, Mr. Trump may not get all he wants. Although the Republicans swept all three branches of government, control of the Senate is slim (52R-48D)⁴. This means issues on trade, international relations and the budget will need to be approved by a combination of drifting Democrats and stoic Republicans... and the Democrats know that. Moreover, the differing opinions of key individuals within Mr. Trump's proposed cabinet may result in a more moderate outcome⁵.

Paramount to Asia is a potential US-China trade stand-off. Many Asian investors fear that Mr. Trump's "America First" policies

appear too protectionist. In contrast, China's leader, Mr. Xi Jinping, positioned China as a champion of free trade at last week's Davos forum⁶. Complicating the picture, at the same forum, Anthony Scaramucci, Mr. Trump's newly appointed public liaison official, took great pains to explain that Mr. Trump was not against free trade per se, but against "asymmetrical" trade⁷ (i.e. trade agreements that disadvantage the US).

At the time of writing, the Trump administration is already starting the process of withdrawing from the Trans-Pacific Partnership. There are also plans to renegotiate the North Atlantic Free Trade Agreement.

THERE ARE CLEARLY MANY MOVING PARTS. UNTIL BRINKSMANSHIP AND RHETORIC FIND A MIDDLE GROUND, EVERYTHING IS UP FOR NEGOTIATION.

The outcome may be less severe than Asian investors fear particularly given the evolving nature of Asian growth, which has been increasingly driven by rising domestic demand over the past decade.

ASEAN exports to the US, for example, have fallen as a percentage of GDP since 2000⁸. In addition, China's policy switch from investment and export led expansion towards domestically generated growth has already resulted in exports falling as a percentage of GDP^{9,10}. On balance, the trade-war bark could be worse than its bite.

Interwoven with trade is uncertainty surrounding the US' strong dollar policy of the last two decades, which Mr. Trump's election rhetoric suggests he will abandon¹¹.

This possibility was further amplified last week as Mr. Scaramucci concurred at Davos¹². But, in another "clarification", nominee for Treasury Secretary, Steven Mnuchin, maintained that a strong currency is strategically important if the US is to remain a favoured investment destination¹³. A further instance of "everything up for negotiation", it seems.

Missing in the discussion so far, is the "real" impact of "real" capital flows that could result from Mr. Trump's policies. The US' Twin Deficits¹⁴ (Fig.1.), for example, suggest that the dollar is already peaking, particularly if Mr. Trump implements his spending plans in full. In this instance, the impact of the resulting rise of liquidity may outstrip the impact of rising interest rates.

From "Corporate Asia's" point of view, US dollar fears could also prove unfounded. Locally denominated debt, for example, comprises the larger portion of Asia's non-bank company debt¹⁵. In addition, the moderate rise in the net debt to equity ratio signals that rising debt reflects improving business conditions rather than leverage trouble¹⁶. The composition of Asian listed company sales to their domestic markets (Fig.2.) also highlights that "Corporate Asia's" exposure to the greenback varies widely.

One can easily conclude that Asian investors have built an excessive buffer of fear. This situation could change quickly; a political gridlock, recognition of Asia's changing growth drivers and a weaker than expected dollar could conspire to alleviate the current fears restraining Asian markets.

If these fears do indeed prove to be exaggerated during Mr. Trump's first 100 days, Asia's low valuations¹⁷ have plenty of head-room to make up.

Fig.1. US' Twin Deficits suggest the USD is peaking

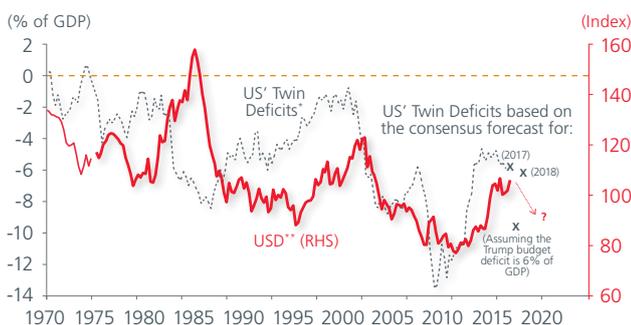
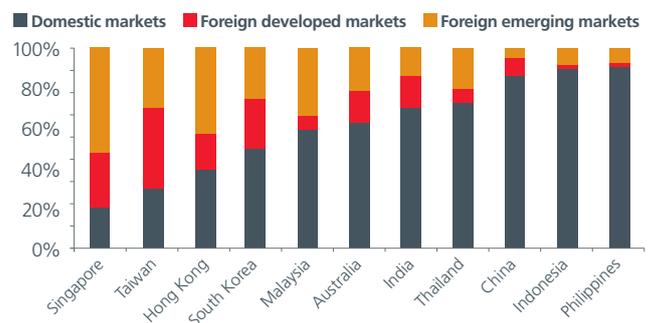


Fig.2. Most corporate sales are to the home market





References ¹US Trade Act of 1974, Section 122. Authorization trigger: Large and serious US balance of payments deficit. Presidential powers: Impose tariffs up to 15 percent, or quantitative restrictions, or both for up to 150 days against one or more countries with large balance of payments surpluses. ²Recap of Rex Tillerson's Senate confirmation hearing for secretary of state, Politifact, 12 January 2017. ³Ross escalates Trump trade criticism against Beijing, Financial Times, 19 January 2017. ⁴The Democratic Party gained two seats in 2016 US Elections, resulting in a 52-48 majority for Republicans. The two independent members of the Senate are included in the Democratic totals, as they caucus with Democrats. ⁵Clash of views in Trump cabinet sets stage for policy confusion, Financial Times, 19 January 2017. ⁶Xi Jinping signals China will champion free trade if Trump builds barriers, The Guardian, 18 January 2017 ⁷Donald Trump is committed to globalisation, Davos told, Financial Times, 17 January 2017 ⁸ASEAN Secretariat, Table 21: Top ten export markets and import origins, % of total exports. 2000 @ 20.1%, 2015 @ 10.9%, 2020est @ 8.5%, November 2016. Note: While exports as percentage of GDP of Singapore and Thailand, (and Hong Kong for that matter) have remained broadly stable, the dependency has fallen in other ASEAN economies. ⁹A truer picture of China's export machine, McKinsey Quarterly, September 2010. ¹⁰Thomson Reuters Datastream, 30 September 2016. ¹¹Dollar retreats on Trump's concern over currency's strength, Financial Times, 17 January 2017. ¹²Davos 2017: Trump's Scaramucci warns over dollar strength, Financial Times, 17 January 2017. ¹³Mnuchin reasserts support for strong dollar, Financial Times, 20 January 2017. ¹⁴FRBSF Economic Letter, Understanding the Twin Deficits: New Approaches, New Results, Cavallo, Number 2005-16, July 2005. ¹⁵Institute of International Finance, EM Debt Monitor March 2016. US dollar debt accounts for only 28% of total debt. In 2015, emerging market non-financial debt rose 6½ percentage points to circa 100% of GDP, (which compares with 87% for developed economies). Within Asia, China and Malaysia comprised most of the rise. The bulk of the rise was in local currencies with foreign debt, particularly US debt being repaid. This US debt reduction was pronounced in China (where debt fell by USD70bn in H2, 2015). ¹⁶Asia leverage – After the boom, Standard Chartered, March 2016. ¹⁷Price to book of MSCI Asia Pacific ex Japan @ 1.5x, MSCI World @ 2.2x, MSCI US @ 2.9x. Bloomberg, 31 December 2016.

Fig.1. US Bureau of Statistics and the US Federal Reserve Board from Datastream as at 20 January, 2017 and Consensus Economics Inc. as at 9 January, 2017. *The US budget and current account deficits as a percentage of forecast nominal GDP. **The nominal effective exchange rate. Fig.2. Global Exposure Guide, Morgan Stanley Research, 22 May 2016. Around 28% of Asian corporate sales are in US dollars.

Disclaimer

This document is produced by Eastspring Investments (Singapore) Limited and issued in:

Singapore and Australia (for wholesale clients only) by Eastspring Investments (Singapore) Limited (UEN: 199407631H), which is incorporated in Singapore, is exempt from the requirement to hold an Australian financial services licence and is licensed and regulated by the Monetary Authority of Singapore under Singapore laws which differ from Australian laws.

Hong Kong by Eastspring Investments (Hong Kong) Limited and has not been reviewed by the Securities and Futures Commission of Hong Kong.

United States of America (for institutional clients only) by Eastspring Investments (Singapore) Limited (UEN: 199407631H), which is incorporated in Singapore and is registered with the U.S Securities and Exchange Commission as a registered investment adviser.

European Economic Area (for professional clients only) and Switzerland (for qualified investors only) by Eastspring Investments (Luxembourg) S.A., 26, Boulevard Royal, 2449 Luxembourg, Grand-Duchy of Luxembourg, registered with the Registre de Commerce et des Sociétés (Luxembourg), Register No B 173737.

United Kingdom (for professional clients only) by Eastspring Investments (Luxembourg) S.A. - UK Branch, 125 Old Broad Street, London EC2N 1AR.

Chile (for institutional clients only) by Eastspring Investments (Singapore) Limited (UEN: 199407631H), which is incorporated in Singapore and is licensed and regulated by the Monetary Authority of Singapore under Singapore laws which differ from Chilean laws.

The afore-mentioned entities are hereinafter collectively referred to as **Eastspring Investments**.

This document is solely for information purposes and does not have any regard to the specific investment objective, financial situation and/or particular needs of any specific persons who may receive this document. This document is not intended as an offer, a solicitation of offer or a recommendation, to deal in shares of securities or any financial instruments. It may not be published, circulated, reproduced or distributed without the prior written consent of Eastspring Investments.

Investment involves risk. Past performance and the predictions, projections, or forecasts on the economy, securities markets or the economic trends of the markets are not necessarily indicative of the future or likely performance of Eastspring Investments or any of the funds managed by Eastspring Investments.

Information herein is believed to be reliable at time of publication. Where lawfully permitted, Eastspring Investments does not warrant its completeness or accuracy and is not responsible for error of facts or opinion nor shall be liable for damages arising out of any person's reliance upon this information. Any opinion or estimate contained in this document may subject to change without notice.

Eastspring Investments (excluding JV companies) companies are ultimately wholly-owned/indirect subsidiaries/associate of Prudential plc of the United Kingdom. Eastspring Investments companies (including JV's) and Prudential plc are not affiliated in any manner with Prudential Financial, Inc., a company whose principal place of business is in the United States of America.



A member of Prudential plc (UK) 