

President Donald Trump – A New World Order

What happened

Donald Trump won the US presidential election and will be inaugurated on 20 January 2017. Since then, he has stated that the key priorities are to withdraw from the Trans-Pacific Partnership and negotiate fair bilateral deals, remove restrictions in the energy sector, reduce government regulations, improve national security and protect national infrastructure, investigate abuses of visa programmes that disadvantage American workers. Nonetheless, uncertainties will remain until more details are revealed as he enters his first term of office. In this commentary, we discuss our preliminary views on the possible impact of his presidency.

Implications on the US

Short-term boost for US economy

The US economic growth will be Trump's top agenda to ensure a second term in the office. His plans to significantly increase infrastructure investments, tighten border control and increase defence spending will lead to job creation and boost the economy through multiplier effects. Trump will also push for lower corporate taxes and introduce an attractive repatriation tax to encourage US companies to repatriate cash held overseas back, leading to some increase in capital expenditures and domestic hiring. Financial deregulation and fewer restrictions in the energy sector will also have short-term benefits to the economy, although the longer-term impact would depend on the level of risk-taking by banks from deregulation and whether increased US oil supply would lead to lower-for-longer oil prices.

Higher inflation, higher interest rates

Trump's "America first" expansionary policies are stoking inflation expectations, given that the economy is already improving and the labour market showing signs of tightening. If he imposes trade barriers on countries like China and Mexico, imported goods will cost more, further fuelling inflation.

The Fed may have to accelerate its interest rate normalisation path, potentially hiking rates once in December 2016 and 2 times in 2017. Concerns that Trump's fiscal spending will lead to wider budget deficits and increase the national debt burden over time have also translated to higher long-dated bond yields, sparking a global bond selloff and causing the US dollar (USD) to rally as a result.

Implications on Asia-Pacific

Trade impact

Among Asia-Pacific (APAC) countries, China, Japan, South Korea and Taiwan are on the US Treasury Department's monitoring list of potential currency manipulators, but none meet all the necessary criteria. Labelling a country as a currency manipulator will trigger a 1-year negotiation process with the country to take remedial action, failing which, could attract penalties from the US, including higher tariffs.

China: The main target in Trump's campaign, he regularly threatened to impose tariffs of up to 45% on Chinese goods, up from the current estimated 4.2%. If tariffs are raised to 45%, the following could happen:

- Exports to the US will drop significantly. The direct impact may be small as exports to the US are just 4% of China's GDP, but this excludes spillover effects on export-oriented jobs and domestic consumption. Given that China is managing an economic slowdown, every bit of contribution from trade would help ease the moderation.
- China will retaliate with tariffs on US goods, resulting in a trade war. While exports to China are <1% of US' GDP, corporate profits, ~1 million American jobs and domestic consumption could be at risk. China could hit back at US corporations, such as cutting business dealings, restricting sales of American-branded goods and limiting investments to and from the US.

- China will step up efforts to lobby for its own free-trade agreements (FTAs), such as the Regional Comprehensive Economic Partnership (RCEP) and the Free Trade Area of the Asia Pacific (FTAAP) to boost regional trade and actively promote the One Belt, One Road initiative as a means to export its industrial capacity.

Rest of APAC: Due to China's integration within the global value chain, trade friction between the US and China will affect the other Asian countries to various degrees.

- Hong Kong appears most vulnerable, with exports to China at 78% of its GDP, out of which intermediate goods is estimated at 18% of GDP. Singapore, Taiwan and South Korea will also be affected from their exports of intermediate goods to China, but the direct impact is estimated at <5% of their GDPs.
- If only China is hit by higher tariffs, it could benefit alternative production bases in Asia and increase their exports to the US. For instance, Vietnam and Indonesia could be beneficiaries if more of the low-end goods production is moved out of China.
- Economic growth in the US and a stronger USD will also benefit the other Asian exporters, especially if wages grow and American consumers increase import spending.
- Trump could clamp down on the H-1B visa programme, which allows US employers to employ foreign workers in selected industries. Tech companies in Silicon Valley could see a brain drain to places like China, Singapore, Hong Kong, South Korea and Japan, where the governments are pushing for innovation and entrepreneurship in fields such as fintech. This will drive demand for office and business park space in these markets.
- Being on the monitoring list, Taiwan, South Korea and Japan could see their exports to the US reduced if Trump also brands them as currency manipulators. Taiwan and South Korea will be more affected than Japan from reduced exports to both the US and China, which together account for 20% and 15% of their respective GDPs. Given its large bilateral trade deficit

with the US, South Korea's FTA with the US may also come under Trump's scrutiny, further jeopardising bilateral trade volumes.

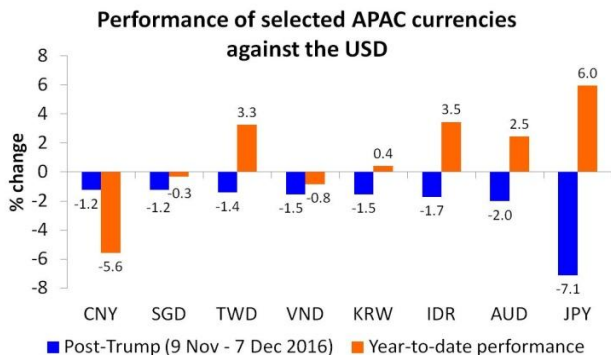
- APAC countries are expected to close ranks and increase regional trade and deepen integration with China, including participation in regional trade pacts and the One Belt, One Road initiative.

Interest rate and currency shocks

Given the rising bond yields in the US and the resultant rally in the USD since Trump's victory, there are financial implications on many APAC countries.

- Faster interest rate hikes in the US will filter down to Singapore and Hong Kong interest rates, given that their monetary policies manage exchange rates rather than interest rates. Borrowing costs will rise, albeit from a low base, which could affect sentiment and real estate demand given the uncertain and weak global environment. In Japan and Australia where policy rates remain at all-time lows and are likely less affected by Trump's policies, the relatively higher yield spreads from property investments will keep investment interest high.
- Currency-wise, Hong Kong's USD-peg will make its exports less competitive as the USD strengthens. Singapore on the other hand, could allow the SGD to depreciate in a broader band to maintain its export competitiveness. The CNY, TWD and KRW could continue to see mild depreciation bias in the near-term (Figure 1) largely due to the strengthening USD, which will also help their exports. Real estate investments will also look more attractive.
- Assuming no significant changes in commodity demand, commodity prices and the strength of commodity currencies tend to correlate negatively with USD strength. The AUD, being a commodity currency, will remain under depreciation pressure in the medium-term if the USD rally persists. The lower AUD will be a boost to Australia's services sector, since tourism and higher education will be more affordable for foreigners. This will be a boon for Australia's hospitality, retail, office and student accommodation sectors.

Figure 1: JPY depreciation sharpest after Trump’s victory



Source: Bloomberg

- The JPY has been one of the worst-hit currencies since Trump’s victory, but it is largely a reversal of the strong appreciation since early 2016 and the widening yield differential. The weaker JPY will be positive for Japanese corporate profits, tourism and the economy, which in turn bode well for Japan’s hospitality, retail and office sectors.

Foreign relations

In APAC, the US has strategic military alliances with Japan, South Korea, Taiwan, Philippines and Australia. Trump affirmed his commitment to his allies and the need to maintain a deterrent force to counter the threats of North Korea and provide balance against the rise of China.

As for US-China bilateral relations, much will depend on whether Trump provokes a trade war and how he handles relations with Taiwan. Trump is likely to adopt a softer, more pragmatic approach in negotiating new deals rather than to risk greater enmity, having agreed on the need for mutual respect and cooperation in his first telephone conversation with Xi Jinping.

Conclusion

The outcome of the US presidential election has introduced greater uncertainty and market volatility. The best-case scenario is that Trump adopts a pragmatic and business approach, which is also our base case. However, uncertainties will remain until he announces and rolls out his policies, both domestic and foreign, with more clarity in 1H2017. Until then, many major business, investment and leasing decisions will be put on hold.

Pending further clarity in 1H2017, it will be prudent to be cautious in the short-term and stay focused on markets with better fundamentals such as large domestic market, diversified economy, single-minded government intent on reform to restructure economy for sustainable future growth, and healthy financial position.

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