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Highlights

- It seems to us the US shutdown could drag on a bit; which would hit the economy; which could hit the stock market; and kick the USD when it's already down
- Just watch polls and see which side is losing popularity the fastest
- A US Navy destroyer sails within 12 nautical miles of the Scarborough Shoal; it doesn't look like a freedom of navigation issue anymore
- One commentator says the PLA Navy must build out the Scarboroughs to protect its second-strike submarines stationed at the Yulin Naval Base
- The Counter-Cyclical Factor is now neutral, which means zero, right? Right?
- It'll take more than pretty pictures to prove robots are boosting Chinese productivity
- More pollution controls in China after March
- Former Bo Xilai aide released more than a year early

INDICATIVE RATES 22 Jan 2018 Data snapped ~11:35 HK TIME

Foreign Exchange			Equity Indices				Interest Rates			
	Asia	% Chng	New York	London		Close	% Chg	3M FIXING		% bp Chng
USD/JPY	110.79	0.03	110.84	108.79	DJIA	26071.72	0.21	USD LIBOR	1.74447	-0.02
EUR/JPY	135.46	0.04	135.51	127.82	N225	23772.02	-0.15	JPY TIBOR	0.06375	0.00
EUR/USD	1.2227	0.06	1.2224	1.1749	DAX	13434.45	1.15	EURIBOR	-0.32800	0.00
GBP/USD	1.3869	0.14	1.3853	1.2857	FTSE	7730.79	0.39	GBP LIBOR	0.52350	0.16
USD/SGD	1.3212	0.04			STI	3550.36	0.82	SGD SIBOR	1.18779	0.00
USD/THB	31.870	0.06			SET	1824.43	0.17	THB BIBOR	1.57400	0.20
USD/MYR	3.9400	0.10	Commodities		KLCI	1827.30	-0.08	MYR KLIBOR	3.44000	0.00
USD/IDR	13338	0.20	CRB	195.50	JCI	6515.75	0.38	IDR JIBOR	5.31278	0.56
USD/PHP	50.925	0.50	Brent Crude*	68.83	PSEI	8967.89	0.58	PHP REF	3.28500	-0.40
USD/INR	63.913	0.14	Gold (USD/oz)	1331.41	SENSEX	35511.58	0.71	INR MIBOR	6.88000	6.00
USD/KRW	1069.10	0.19			KOSPI	2489.56	-1.22			
USD/TWD	29.179	-0.55	Market Gauges		TAIEX	11182.05	0.28			
AUD/USD	0.7990	0.00	VIX	11.27	ASX	6008.60	0.05			
USD/HKD	7.8195	0.04	Dollar Index	90.627	HANG SENG	32260.62	0.02	If prior trading day is a holiday,		
USD/CNY	6.4050	0.09	UST 2Y	2.061	SHCOMP	3490.30	0.07	comparison with preceding day.		
USD/VND	22710	0.04	UST 10Y	2.639	VNI	1074.60	1.18	* ICE Brent Crude (USD/bbl)		

Source: BTMU & Reuters. FX daily % changes from 2100 GMT prior Reuters closes; London and New York show BTMU closes.

Up Front/USD/Shutdown. Latest is there's a procedural vote in the US Congress scheduled for 0100 HKG time tomorrow after an earlier effort to end the US shutdown before federal workers started the workweek failed; we hadn't counted on the earlier effort to work.

"If it doesn't happen tonight [US time], it's going to get a lot harder tomorrow," said Sen. Lindsey O. Graham (R-S.C.), who has pressed for action on immigration legislation and met with the moderates' group Sunday.

Because:

- The main issue remains **immigration**.
- This subject, it seems fair to say, is EXTREMELY DIVISIVE in the United States of America.
- So even if somehow Congress had managed to get government to re-open again, it didn't/doesn't mean we won't all be back here again before too long.
- Due to the **immigration** issue not being resolved.

As the shutdown prolongs, it will become more and more unpopular. At the start of the shutdown, polling seemed to indicate the Democrats were "ahead" with more than a 20ppt gap between them and the Republicans, in terms of who surveyed voters "blame" for the shutdown. The politics now is to watch the evolution of polling as the weeks drag on. **Whatever party is seen as losing the popularity race will be the party that is going to fold.** That's what both Democrats and Republicans are counting on.

In a way, in the US, resort to shutdown is like turning over an intractable issue to a popular referendum, only citizens don't vote but pollsters conduct daily polls. Not the most efficient way to govern, but on **immigration** the US system right now seems to have hit its limits.

https://www.washingtonpost.com/powerpost/trump-launches-new-round-of-partisan-attacks-as-government-shutdown-hits-day-2/2018/01/21/0560aece-fe35-11e7-a46b-a3614530bd87_story.html?hpid=hp_hp-banner-main_shutdown0122-822am%3Ahomepage%2Fstory&utm_term=.de82e200fbe8

A *Slate* commentary saying similar political things as us:

<https://slate.com/news-and-politics/2018/01/how-the-shutdown-ends.html>

A pretty clear guide to the shutdown:

https://www.washingtonpost.com/graphics/2018/politics/government-shutdown-faq/?utm_term=.310d52977104

As to where future unpopularity will lurk, we noted the FEMA bullet above: The idea that ongoing reconstruction work in Texas, Florida, Puerto Rico and California, in response to the natural disasters of last year, may stall. Texas and Florida were Trump states.

Bottom Line: The most straightforward market implications would seem to go straight through the economy, with the simple thought that a longer shutdown will drag down the economy just when the Trump Team was counting on lesser withholdings cheering up the paychecks of workers. As we go to press, fair-value calculations are indicating an opening decline on US stock indices tonight. The USD hardly needs any more encouragement to decline. [\[Back to Highlights\]](#)

USD/CNY/PHP/ISLANDS. China warned off a US Navy destroyer that apparently sailed within 12 nautical miles of the Scarborough Shoals over the weekend. This is the Shoal upon which, if the Chinese were to build military installations as they have in the Paracels and Spratlys, the *Washington Post* editorial board last Summer recommended a US military response (which caught our eye in an earlier *call note*).

<http://www.scmp.com/news/china/diplomacy-defence/article/2129805/china-warns-us-destroyer-near-south-china-seas>

Zhang said the shoal was the Philippines' unspoken bottom line in its quiet diplomacy with China on the South China Sea. "The current diplomatic approach of the Philippines is to make the sovereignty [over the shoal] ambiguous," she said. "It has asked China not to build on the shoal, which China has not. The mutual preference of both the Philippines and China over this particular [shoal] is stability."

*Zhang said she expected to see more frequent confrontations between the US and Chinese militaries in the South China Sea, with Washington putting China and Russia at the centre of its new national defence strategy. "The South China Sea will be the ground on which the two powers will wrestle for military power. **It has become a long-term conflict,**" she said. [Our emphasis.]*

We found one reader comment for this article interesting (HT higherbatson@*****):

Manila lost control of the Scarborough Shoal in 2012 following a standoff with the Chinese Coast Guard. The Philippines had held the Scarborough Shoal for a century. During the Spanish colonial era, it was marked as Philippines territory. Following the Second World War U.S., forces in the Philippines used it for gunnery training. The shoal lies nine hundred kilometers from the closest Chinese landfall.

China will build a large airfield and port facilities on the Scarborough Shoal as soon as it is able to do so without inciting a too costly international reaction.

*The planned facility will dwarf those on Woody Island in the Paracels [sic] or the facilities in the Spratly Islands completed in 2016. Like these, it will be primarily military and host a permanent presence. PLA sources are clear the addition of the airfield is primarily driven by the PLAN's need to protect the approaches to naval facilities on Hainan Island. Foremost among these is the Yulin naval base, the homeport of the Chinese ballistic submarine fleet. The PLAAN's reach over the contested waters will be complete once coverage by maritime and air facilities on the Scarborough Shoal is operational. Notwithstanding any delays cause by political considerations, military sources make it clear **this is a non-negotiable objective if the PLA is to be in a position to assure the second strike capability of China's ballistic missile submarines.** [Our emphasis.] [\[Back to Highlights\]](#)*

CNY/Counter-Cyclical Factor. The counter-cyclical factor is now *neutral* (中性), with the USD/CNY fixing formula the same (in terms of parameters); ie, *USD/CNY close price + CFETS RMB index's change + counter-cyclical factor* (收盘价 + 一篮子货币汇率变化 + 逆周期因子). (Source: CEFTS)

<http://www.chinamoney.com.cn/fe/Info/43479495> (simplified Chinese)

This is the same as our previous analytical result in which, in the depreciation regime, the counter-cyclical factor is statistically insignificant and very small.

Logically, *neutral* might mean zero, in which case why discuss the CCF at all? Maybe authorities meant by this statement, which came out after the onshore market close last Friday evening, that CCF is not dead so maybe daily movements can be expected to still contain a little voodoo.

For a recent view, see [Asia Cross Current: CNY – R.I.P. Countercyclical Factor \(10 January 2018\)](#). [\[Back to Highlights\]](#)

CNY/#Overcapacity. There was an item in last week's *Global Times* (maybe the official unofficial tabloid) with this headline:

Robots help boost productivity in E China's Zhejiang

Except that it had no supporting evidence, only a few pictures of Rui'an (a large area near Wenzhou in Zhejiang) factories, which apparently bought 500 robots last year.

<http://www.globaltimes.cn/content/1085207.shtml>

ROBOTS IN RUI'AN



Source: *Global Times*

Robots boosting productivity near the traditional center of China entrepreneurialism (Shenzhen should be counted, too) would be a top story. If they hadn't boosted productivity that would be interesting as well. But as geeks we'd probably prefer a few more numbers and a few fewer pictures next time.

Because another article pointed out that KUKA, 95% owned by China's Midea Group (acquired in Spring 2016, two years ago), has the LOWEST profit margins among the world's four leading robot groups, which are (along with their profit margins):

- FANUC 24.4%
- Yaskawa 7.8%
- ABB 6.6%
- KUKA 2.5%

http://host.madison.com/business/investment/markets-and-stocks/robotic-stocks-that-could-profit-from-tesla-s-model-ramp/article_e056bb7d-0807-55a6-808e-3a242cf60167.html

Nonetheless both KUKA and FANUC stocks have returned approximately the same over the past year: 54.2% vs. 58.7%, respectively. [\[Back to Highlights\]](#)

CNY. ... amid concerns that enterprises and local governments could lower their guard once short-term campaigns to meet air quality targets have been completed, China has been trying to "normalize compliance" and put firms under more permanent

scrutiny and pressure. In a notice published on its website late on Friday, China's Ministry of Environmental Protection said all new industrial projects in 28 key northern Chinese cities would now have to comply with even tougher emission curbs when undergoing environmental impact assessments from March 1. [\[Back to Highlights\]](#)

<https://www.reuters.com/article/us-china-pollution/china-draws-up-new-special-emission-curbs-on-industries-idUSKBN1F903W>

CNY. A former aide to Bo Xilai, fresh-faced at trial and convicted of bringing the cyanide to his former boss's wife with which she then murdered Briton Neil Heywood in 2011, appears to have been released more than a year ahead of prior expectations; appearing last week at the 11th anniversary death commemoration for Bo Yibo, Bo Xilai's father. [\[Back to Highlights\]](#)

<http://www.scmp.com/news/china/policies-politics/article/2129724/former-bo-xilai-family-aide-jailed-over-murder-uk>

TWO DAYS HENCE

BOJ monetary policy decision: consensus no change to 10-year yield target at 0.00% and policy balance rate at -0.10%. **US Senate Banking Committee to hold a hearing to consider the nomination of Marvin Goodfriend to be a Fed Board governor.** Goodfriend, a prominent economist, is known for defending the rules-based approach to conducting monetary policy, and he prefers negative interest rates over QE. **Germany January ZEW survey current situation:** consensus 89.6 > last 89.3, with an expected higher expectations: consensus 17.7 > last 17.4. The impact of political uncertainties and the euro's appreciation might have weighed somewhat on investor's confidence, posing downside risks to consensus forecasts. **Eurozone January Consumer confidence:** consensus 0.6 > last 0.5. The expected improvement would probably largely reflect households' more optimistic assessment of future unemployment.

Philippines 4Q GDP: consensus 6.7%YoY < last 6.9%, while on a seasonally QoQ basis, an improvement is likely seen: consensus 1.5% > last 1.3%, probably supported by an uptick in both private and public consumption. **Taiwan December Industrial production:** consensus 1.20%YoY > last 0.85%. MOEA manufacturing trend index (in terms of number of manufacturers) remained below 50 in December (48.0 < last 48.9), but on a positive note, the trend index (in terms of production value) increased to 51.8 in December from 49.8 in November, probably signaling mild growth in production in December which means a rather balanced risk to consensus forecast. **Hong Kong December CPI:** consensus 1.7%YoY < last 1.6%. Although inflation is expected to quicken slightly in December, quickening for four months in a row (if realized), the overall inflation risks should remain limited in the near term, amid the slow increases in import prices and moderate local cost pressure,

Bonds: Philippines to sell PHP20bn 3-year bonds (last coupon rate 3.375% and amount accepted PHP15bn), while **Indonesia** to sell 2, 4, 7 and 15-year Sukuk. [\[Back to Highlights\]](#)

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