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Highlights

- Maersk's CEO says despite trade wars, the effect on trade flows so far seems to be nil
- But he agrees with prior expectations of shifting bilateral trade balances and a boost to US inflation
- The US and Mexico are reportedly close to a bilateral NAFTA deal but US President Trump may still want Section 232 auto tariffs
- We're also not sure how Canada will respond to any such deal
- A very nice explanation of US Trade Representative Lighthizer's views
- Increasingly in our view, what Chinese de-leverage there was is over
- And there is a newly unveiled problem of hidden local government debt
- US midterm projections and prospects of even *more* polarization

INDICATIVE RATES 23 Aug 2018 Data snapped ~11:36 HK TIME

Foreign Exchange					Equity Indices			Interest Rates		
	Asia	% Chng	New York	London		Close	% Chg	3M FIXING	%	bp Chng
USD/JPY	110.80	0.24	110.54	108.79	DJIA	25733.60	-0.34	USD LIBOR	2.31175	0.15
EUR/JPY	127.99	-0.16	128.22	127.82	N225	22403.90	0.18	JPY TIBOR	0.08625	0.00
EUR/USD	1.1550	-0.40	1.1597	1.1749	DAX	12385.70	0.01	EURIBOR	-0.31900	0.00
GBP/USD	1.2865	-0.34	1.2913	1.2857	FTSE	7574.24	0.11	GBP LIBOR	0.80588	0.15
USD/SGD	1.3708	0.32			STI	0.00	-100.00	SGD SIBOR	1.63432	0.11
USD/THB	32.810	0.43			SET	1707.11	0.52	THB BIBOR	1.58677	0.00
USD/MYR	4.1030	0.17	Commodities		KLCI	1806.62	0.47	MYR KLIBOR	3.69000	0.00
USD/IDR	14628	0.36	CRB	191.12	JCI	5979.57	0.59	IDR JIBOR	7.13278	-1.39
USD/PHP	53.490	0.24	Brent Crude*	74.65	PSEi	7713.71	1.07	PHP REF	3.96600	-7.60
USD/INR	70.040	0.26	Gold (USD/oz)	1195.11	SENSEX	38285.75	-100.00	INR MIBOR	7.40000	1.00
USD/KRW	1122.42	0.51			KOSPI	2269.33	-0.18			
USD/TWD	30.773	0.38	Market Gauges		TAIEX	10821.52	0.16			
AUD/USD	0.7288	-0.79	VIX	12.25	ASX	6253.70	-0.20			
USD/HKD	7.8497	0.00	Dollar Index	95.429	HANG SENG	27732.61	-0.70	*If prior trading day is a holiday,*		
USD/CNY	6.8724	0.47	UST 2Y	2.595	SHCOMP	2711.25	-0.12	*comparison with preceding day.*		
USD/VND	23276	0.01	UST 10Y	2.824	VNI	986.91	0.48	** ICE Brent Crude (USD/bbl)*		

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

[We're back. This is about 3½ days' worth of interactive chat posts.]

GLOBAL/Trade. Earlier this week, Maersk's CEO made a number of interesting observations/conjectures about the future impact of global trade wars.

https://www.bloomberg.com/news/articles/2018-08-19/tariffs-will-hurt-u-s-much-more-than-rest-of-world-maersk-says?cmpid=BBD082018_MKT&utm_medium=email&utm_source=newsletter&utm_term=180820&utm_campaign=marketsasia

First, in terms of real economic impacts, to the start of 3Q18, Maersk - which transports about 20% of the world's seaborne consumer goods - basically said **so far there was none.** In fact, to dodge future tariffs, importers may be accelerating purchases. [The FOMC minutes for the 31 July – 1 August 2018 meeting also noted a surge in US exports in May.] In 3Q18, traditionally the season of Christmas-related shipping demand, Asian (read: China) shipments to Europe and the US appear strong, which suggests support for upcoming export/import #s over the next couple of months.

Other Dutch data we had followed had previously suggested to us momentum in global real trade may be decelerating. This data is updated tomorrow.

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Then Skou talked about a **substitution effect:**

"The first thing the American importers would do if tariffs are put on Chinese consumer goods would be to buy in Vietnam, in Indonesia or elsewhere in Asia," Skou said. "Big U.S. consumer brands like Nike produce in all of Asia, not just in one country, so there will be a substitution effect."

This is consistent with our discussion on shifting bilateral trade balances in *Asia Cross Current: USD/Asia - Some Unpleasant Macroeconomics for Trump Trade Policy, 27 June 2018*.

Finally, from Maersk's point of view the key threat is if Trump tariffs move to consumer goods (as it appears at risk of doing), in which case US trade growth could be crimped by 3-4ppts (implying very big absolute #s). Right now this would appear to crucially depend upon whether US tariffs extends to the USD200bn of additional imports from China. [We note in recent days AAPL Ceo Tim Cook had dinner with Trump at the White House.]

And Maersk hinted **there could be a more pronounced boost to measured inflation if we get to the more dangerous stage:**

"The other factor is that there's a lot of stuff that's now imported into the U.S. that just isn't produced anywhere within the U.S.," Skou said. "You can't get Nike sneakers or iPhones that are produced in the U.S. So it will end up being pushed on to the consumer." **[Back to Highlights]**

USD/MXN/Trump/Trade/NAFTA. *Even as the U.S. and Mexico have largely finalized a deal on the new auto rules of origin, the U.S. has been pushing for cars that don't meet the threshold to be subject to a 20-to-25 percent tariff, according to the people familiar with the talks. That would represent a major jump from the 2.5 percent tariff the U.S. charges currently under World Trade Organization rules.*

https://www.bloombergquint.com/onweb/2018/08/23/trump-auto-tariff-threats-are-said-to-hinder-push-for-nafta-deal#gs.2Pd69Rg

Mexico has made clear to the U.S. that if the nations reach a deal to update the content rules for cars produced in the region and traded duty-free, those vehicles would need to be excluded from potential 232 tariffs, *according to a person familiar with the talks, who asked not to be named discussing private negotiations. Mexico would not be satisfied living with the threat of 232 tariffs over its head, the person said.*

"We're going to put a 25 percent tax on every car that comes into the United States from the European Union," *the president told supporters at a campaign rally in West Virginia on Tuesday, complaining that there were no Chevrolets to be seen on the streets in Berlin.*

So, we reiterate: A breakdown in NAFTA as an, uh, engine of global trade and economic growth could be as destructive as anything that occurs on the US-China trade front.

Officials on both sides have insisted that talks in Washington this week between the U.S. and Mexico have been going well with the White House eager to make an announcement of a bilateral deal as soon as this week. Such a move would clear the way for Canada to be brought back into the discussions for a final push toward a new Nafta that could be signed by the three countries' leaders by the end of the year. [But privately, we are hearing from knowledgeable Canadian sources that even if a US-Mexico deal is struck, **Canada does not intend to be a pushover in crafting a final NAFTA deal.**]

All of the above followed by a few hours other wire stories saying a handshake deal on NAFTA between Trump and Mexico might be with us as early as today.

http://thehill.com/policy/finance/403044-mexican-trade-official-says-nafta-deal-with-us-may-be-hours-away

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USD/MXN/CAD/NAFTA. If Team Trump wants a deal within calendar 2018, here are some of the deadlines.

http://thehill.com/policy/finance/402428-time-running-out-for-trumps-nafta-talks

... the trade promotion authority law governing the deal back in the U.S. requires the White House to notify Congress 90 days before he intends to sign a trade deal. That means that if Trump wants to sign a deal with Peña Nieto and not López Obrador, he has to notify Congress by Sept. 1 at the very latest.

Newly elected Mexican president Andrés Manuel López Obrador, a populist, is set to take office on Dec. 1. Outgoing President Enrique Peña Nieto, who is a more vocal advocate for free trade, is eager to wrap up the deal and get it signed into law before he leaves office. For his part, López Obrador would be happy to keep his fingerprints off the deal altogether for now. Once he's in office, experts say, negotiators would have to go back to the drawing board.

A notification to the US Congress 1 September should mean the earliest Trump can sign a new NAFTA deal would be 30 November, a day before AMLO comes into office. [Back to Highlights]

USD/Trump/Trade. We attach for your edification the most coherent expression we have read to date of Trump Trade Policy, as embodied in US Trade Representative Robert Lighthizer.

https://foreignpolicy.com/2018/08/06/you-live-in-robert-lighthizers-world-now-trump-trade/

Where Lighthizerism departs from standard free trade philosophy isn't in its desired goals of open markets but in its commitment to using an openly politicized arsenal of weapons for achieving them. Since the formation of the General Agreement on Tariffs and Trade—the precursor to the World Trade Organization—in 1947, the dominant school of thought on international trade has favored multilateralism, or agreements between many nations where trade barriers sink collectively on the "most favored nation" principle. ***Lighthizerism scorns the multilateral approach in favor of bilateralism,*** *or deals between two nations to lower barriers. Against the collective approach exemplified by the WTO agreement, which over 100 countries signed in Marrakech in 1994, he promotes a transactional one instead, proceeding deal by deal and case by case. "We're not talking about a level playing field," he said to Congress,* ***"What we're saying to the country is, 'We'll give you better access than the rest of the world, and you give us approximately an equal amount of better access.'"***

To get to the endpoint of better access and lower barriers, Lighthizer sees little shame in the use of unilateral action. Executive orders, diplomatic pressure, and legal measures like the above-mentioned Section 232 are legitimate tools for unsettling existing arrangements and pushing partners to the negotiating table. *Lighthizerism is no roadmap for retrenchment but a blueprint for recapturing what is seen as a lost edge for U.S. manufacturing on the world stage. It does not herald "the end of globalization" but a more aggressive phase of it. And far from shielding producers from the discipline of competition, Lighthizerism aims to deepen it.*

Reciprocal access might provide some clues as to how the US and China might ultimately find some areas for agreement. Here, though, the key question is to what extent China is willing to provide such access? As had been mentioned quite often in the press, the relatively lower ranked officials taking part in this week's US-China trade talks do not appear to possess the power to promise access. And obviously since this article focuses on Lighthizer and Lighthizer is not involved in this week's talks (he's busy with NAFTA), it wouldn't stand to reason much on market access can be accomplished this week.

One more thought while reading through this essay: Yes, it's true Lighthizer is reprising tactics from the 1980s (Back to the Future). But the relative heft of the United States within the world economy is not what it was once. [Back to Highlights]

CNY/CNH/Monetary Policy. **What deleveraging there was, is over.**

China's banking and insurance regulator has asked financial institutions to give more support to infrastructure investment, importers and exporters, and creditworthy companies experiencing temporary problems. It ... *said financial institutions should not "blindly" withdraw funding from companies that have a good credit record but that are experiencing "temporary operational difficulties."*

https://www.reuters.com/article/us-china-banking-policy/china-regulator-asks-financial-institutions-to-support-infrastructure-investment-idUSKBN1L401L

China almost quadrupled the value of fixed-asset investment projects approved in July *from the previous month as it looks to accelerate infrastructure spending.* [Back to Highlights]

CNY/CNH/Monetary Policy. A total of 22 provincial-level areas and cities sold local government bonds worth a combined 696.3 billion yuan ($101.3 billion) in the 25 days after the State Council meeting on July 23, according to Caixin's calculations. The figure was **nearly half** of the 1.4 trillion yuan in total local government bonds issued across the country in the first six months of the year.

https://www.caixinglobal.com/2018-08-20/local-governments-set-timetable-to-eliminate-off-balance-sheet-debt-101316936.html?rkey=4jojc%2BU9Dvs0eyjTyPSDXfFL%2FE7ci4pK%2B%2FtXHFfE3Gb4jLClDZyvAw%3D%3D&cxg=web&Sfrom=twitter

In figures rarely published by authorities, the documents released in recent months by the local governments about reducing their off-balance-sheet borrowings showed that the size of the debt was **many times higher than that of their liabilities on the books. Often dubbed "hidden government debt,"** the borrowings were mainly accumulated through spending in projects such as renovation of run-down urban residential areas, construction of low-income housing, and government payment in public-private partnership deals.

For example, Guyuan city in Northwest China's Ningxia Hui autonomous region logged in 4.34 billion yuan in outstanding standard government debt by the end of last year. However, its off-balance-sheet liabilities were worth 15.35 billion yuan, according to the city's plan for lowering government debt. The city government has set a target to cut off-balance-sheet debt by over 5 billion yuan by 2022 to bring down the ratio of those liabilities to its GDP to 44.69% from the 96.91% at the end of 2017. To achieve the goals, it will carry out auditing of the debts and repay some of them using fiscal revenues or proceeds from sales *of land or government housing. For those classified by auditors as non-government liabilities, it will order the companies that own the projects to pay for them.*

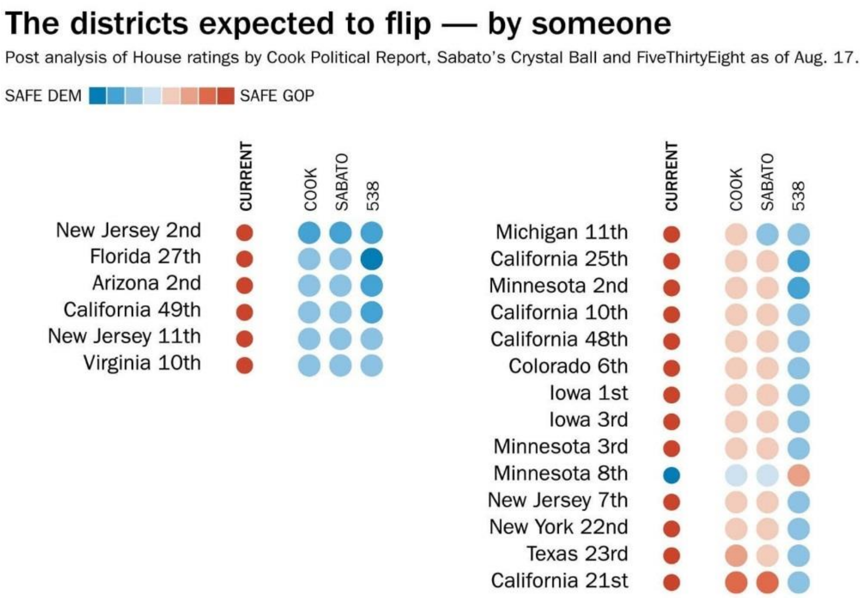
This article reported that last Thursday (16 August), Guangdong issued CNY60.9bn of bonds on just that day alone (including CNY34.2bn for land acquisition for the Greater Bay Area initiative, which Hongkongers might note). The day before (Wednesday 15 August) apparently Inner Mongolia issued CNY52.5BN. **[Back to Highlights]**

USD/#midterms. Well-known US Big Data and political blogger Nate Silver gives Democrats a 75% chance of retaking control of the House of Representatives in the #midterm elections. (But, then, and not to be snarky, he gave Hillary Clinton a 70% chance of winning, too.)

https://www.washingtonpost.com/news/politics/wp/2018/08/17/here-are-the-house-seats-most-likely-to-flip-according-to-election-rating-systems/?utm_term=.ac0ca1f0a8b1

Our view remains cautious: We lean towards the Democrats retaking the House (but not the Senate) and think the race will be very close. **[Back to Highlights]**

US HOUSE DISTRICTS PROJECTED TO FLIP



Source: Washington Post

USD/Trump/#midterms. An editor from one of the other political consultancies highlighted above - the longstanding Cook Political Report - sees **more** polarization after the midterms.

https://www.nytimes.com/2018/08/20/opinion/midterms-democrats-republicans-blue-wave.html

Much as 2016 produced an anomalous split between the popular vote and the Electoral College, 2018 could produce a split decision between the House and Senate. That would allow both parties to claim a midterm mandate — and reinforce their stubbornness.

In my time covering races professionally, I've never observed this little overlap between the battlegrounds of high-stakes Senate and House races. Of the 64 most competitive House races, only 14 are in states with highly competitive Senate races.

It seems to us what this analyst is saying boils down to: In this election, relatively poorer and less educated rural areas will keep the Senate in Republican hands; and defense of Trump, which hitherto has largely been a House affair, will increasingly be a Senate undertaking in the next two years (if it is going to continue).

US: THE MEDIAN MIDTERM VOTER, HOUSE VS. SENATE

Two Midterm Voter 'Baskets'

Compared with House districts, voters in competitive Senate races are more pro-Trump, less urban, less college educated, whiter and poorer. Below is a profile of the strikingly different "baskets" of voters in the most competitive Senate and House races — using the median (middle) of the 11 most competitive Senate races and the 64 most competitive House races, as designated by the nonpartisan newsletters The Cook Political Report and Inside Elections.

	U.S. OVERALL	MEDIAN HOUSE SEAT	MEDIAN SENATE SEAT
2016 Trump vote share	46%	49% Percentage point difference from U.S.: +3	56% +10
Trump vote margin vs. Clinton	−2%	+4% +6	+19% +21
White share (non-hispanic)	62%	74% +12	80% +18
Percent with bachelor's degree (age 25+)	30%	32% +2	28% -2
Population density (people per square mile)	90	407	88
Median house-hold income	$55,322	$60,003	$50,433

By The New York Times | Sources: The Cook Political Report; Inside Elections; 2016 American Community Survey 5-Year Estimates. Figures rounded to nearest whole number.

Source: The New York Times

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TWO DAYS HENCE

US Annual Jackson Hole Central Banking Symposium (24-25 Aug). This year's topic is "*Changing Market Structure and Implications for Monetary Policy*". Discussion could be on the structure of the Fed's balance sheet, e.g., how much reserves should the Fed keep in the long run? **US July Durable goods orders**: Consensus -1.0%SAMM < last 0.8%, in part due to fewer Boeing orders in July (30 vs. Last 233). So, ex-transport, an improvement is expected: Consensus 0.5%SAMM > last 0.2%. **Japan July Nationwide CPI/ex-food/ex-food & energy**: Consensus 1.0%YoY/0.9%YoY/0.3% > last 0.7%/0.8%/0.2%. An expected slight pick-up in inflation, thanks to a weaker yen, still far from BOJ's 2% target.

Singapore July Industrial production: Consensus 6.0%YoY/-1.0%SAMM < last 7.4%/3.9%. Electronic shipments shrank for the eighth straight month in July, but non-oil domestic exports rebounded (11.8%YoY > last 0.8%, revised from 1.1%), probably rendering support to manufacturing. **Bonds**: **China Chongqing** will sell CNY30bn 5/7-year bonds, and **Gansu** will sell CNY10.58bn 3/5/7-year bonds. [Back to Highlights]

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