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Global

FX Flash

Understanding the Trump Trade

It is not all about the RMB

Donald Trump just accepted the nomination as the Republican's candidate for the Presidential Election on 5 Nov. In order to understand what the "Trump trade" entails, we need to know the key policies that he has been advocating. We also rely on past and recent market reactions as clues. To be clear, we are still rather early in the run-up to the US elections in Nov. The outcomes of the elections could still be fluid, Trump's priorities could change, Biden just dropped out of the race and endorsed his Vice President Kamala Harris. However the Democrat's candidate remains fluid until probably the Democrat convention in Aug. We suspect the characteristics of the "Trump trade" that we pencilled in here could evolve further later.

Biden's move to drop out is not unexpected but the events that led to this illuminated the Trump Trade. There are a few salient policies that form the characteristics of "the Trump Trade"

- **Tariff Hikes -** 60-100% (or 50%?) tariff on Chinese imports and 10% on imports from the rest of the world.
- **Extension of corporate tax rate cuts** from his 2017 Tax Cuts and Jobs Act (TCJA) and **potentially further cuts** from current 21% to 15% as mentioned in his recent interview with Bloomberg Newsweek. He had floated the idea of **removing personal income tax** and replacing the tax revenue with the revenue from tariffs
- The Republicans accused Biden of not doing enough to **stem the flow of migrants** flowing across the borders. Trump's running mate pledge to deport undocumented immigrants.
- **Lower USD** to lift export competitiveness of American goods.
- **Lower interest rates.**

We found the Trump trade to manifest more strongly after his attempted assassination at his rally on 13th Jul. We saw USD strengthening against most Asian currencies, gold and bitcoin rose and all US bourses posted gains. There was also a noted bear steepening of the UST curve amid some concerns on the impact of Trump's policies on the US' fiscal health, negative for Asian currencies.

The Trump Trade - FX View

Balance of risks could be on net, skewed to the upside for the USD as Trump's trade policies could have inflationary effects on the US and also produce a deflationary shock to the rest of the world as China's excess supply gets diverted away (as highlighted by our economists). Most of his policies could drive a divergence in inflation trajectories between the US and the rest of the world and that could bring back US rate exceptionalism again. These policies. (i.e. tariff hikes, tax cuts, anti-immigrants drive) are likely to be prioritized over their desires for a weaker USD and lower interest rates given that Trump had enacted those policies in his first term with grand effects. Despite his last election loss in 2020, his persistent popularity had likely emboldened him to implement those policies at more extreme levels. Yuan would be under pressure once again but even with might higher tariffs in store, pressure on the yuan may not be proportionately larger as the Fed is in an easing cycle compared to a hiking cycle in 2018. In addition, Trump had recently called out yen and yuan weakness last week. He could do that again and that could dampen the rise of the USDJPY and USDCNY, albeit with diminishing effects.

In terms of relative value plays, we look for PHP, IDR and THB to remain more resilient compared to CNH, CNY, MYR, SGD, KRW and TWD.

MYR, SGD, KRW and TWD are likely to remain sensitive to impact on the yuan. SGD could fall this time as a Trump-triggered deflationary shock could increase the risk of MAS easing. PHP, IDR may be more insulated as what was observed before in 2019 when the Fed is about to cut rates. THB should get its usual boost from the gold.

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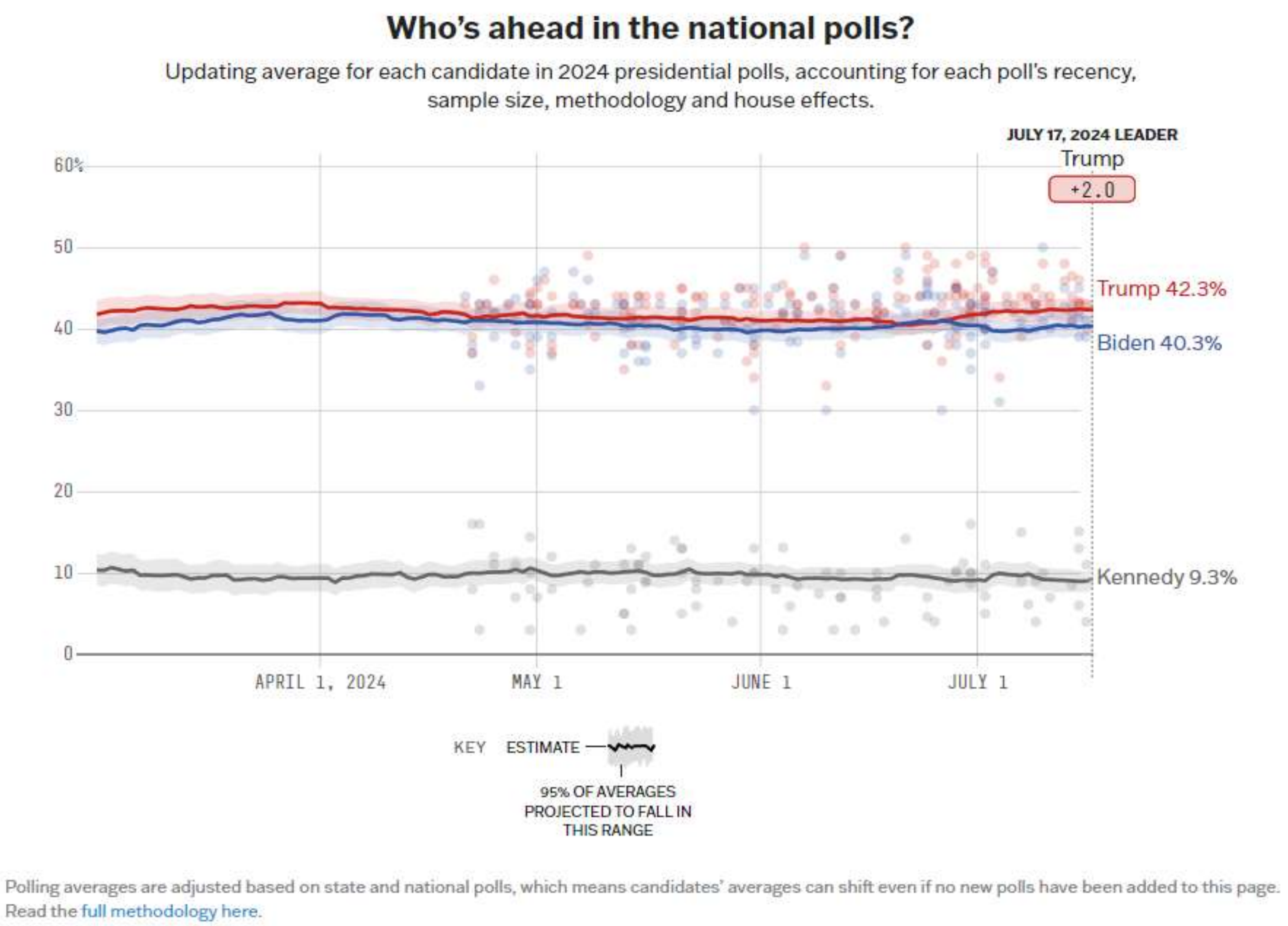
What is the Trump Trade?

Donald Trump just accepted the nomination as the Republican's candidate for the Presidential Election on 5 Nov. In order to understand what the "Trump trade" entails, we need to know the key policies that he has been advocating. We also rely on past and recent market reactions as clues. To be clear, we are still rather early in the run-up to the US elections. The outcomes of the elections could still be fluid, Trump's priorities could change, another Democrat candidate may take over Biden as candidate, and so, even the characteristics of the "Trump trade" that we pencilled in here could evolve. Some of the Republicans are even worried of overconfidence - Republican pollster Frank Luntz said Trump is mistaken if he thinks he's winning. He added that "the truth is, Joe Biden is losing".

We had two instances of Trump trade surfacing thus far recently – 1) Post Biden-Trump Debate, 2) Post Trump Shooting Incident. Both incidents portrayed Trump as the stronger candidate and polls swung in the favour of him succeeding Biden as the 47th US President.

Chart 1: Trump's Lead over Biden Widens After the Biden-Trump Debate on 27 Jun 2024, giving rise to Trump Trade.



Note: Polling averages are adjusted on state and national polls, which means candidates' averages can shift even if no new polls have been added to this page. Polls are as of 17 Jul.

Source: Fivethirtyeight.com

Since Biden dropped out of the race for Nov, he endorsed his Vice President Kamala Harris. While approval polls for both candidates are similar, Kamala Harris scored better on the disapproval polls at 50.4% vs. Biden's 56.2%. She is seen as a stronger contender than Biden, against Trump. However, it could still be challenging for her to form a compelling narrative to unite the Democrats against Trump at this stage.

Chart 2: Approval/Disapproval Polls of Kamala Harris

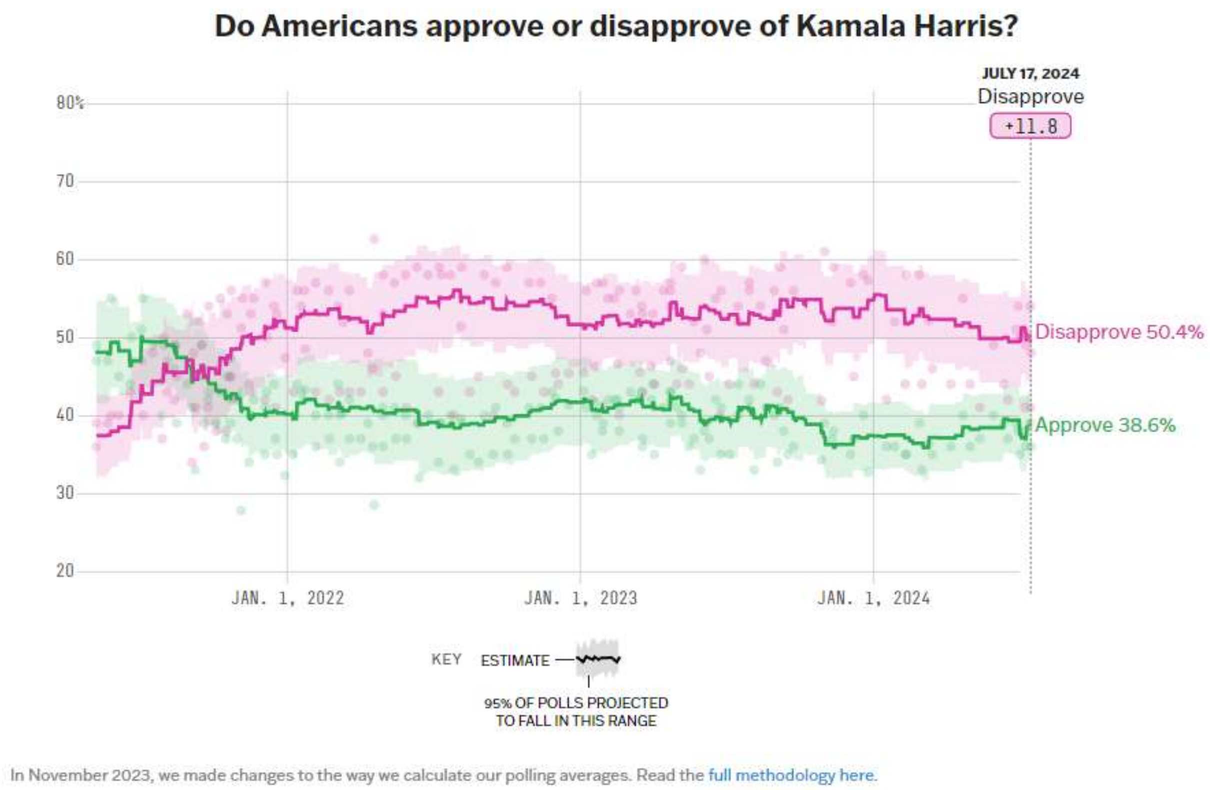
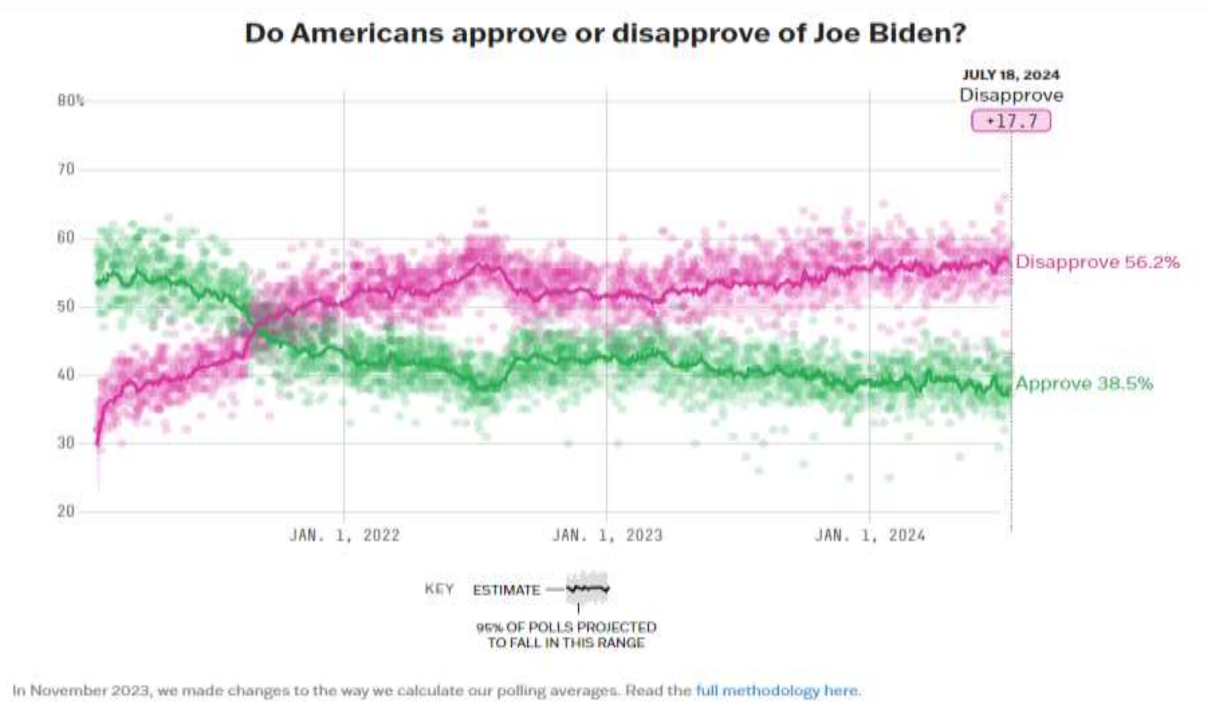


Chart 3: Approval/Disapproval Polls of Joe Biden



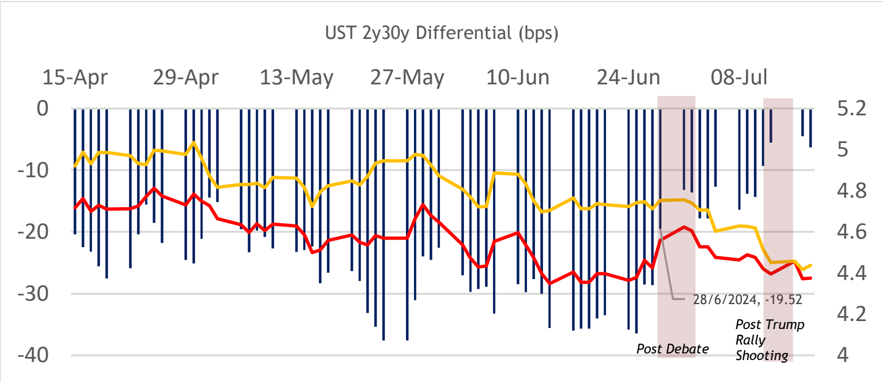
Source: Fivethirtyeight.com

Biden's move to drop out is not unexpected but the events that led to this illuminated the Trump Trade.

1) **Bear-Steepening of the UST Curve:**

One common observation after both events is the steepening of the UST curve. UST2y30y differential even turned slightly positive (not shown in Chart 4) for the first time on 15 Jul since Jan (right after the shooting) but that was reversed within the day. The bear steepening of UST has significant implications for EM currencies.

Chart 4: The UST 2Y30Y Differential Substantially Narrowed (aka steepened) After Debate



Source: Bloomberg, Maybank FX Research & Strategy

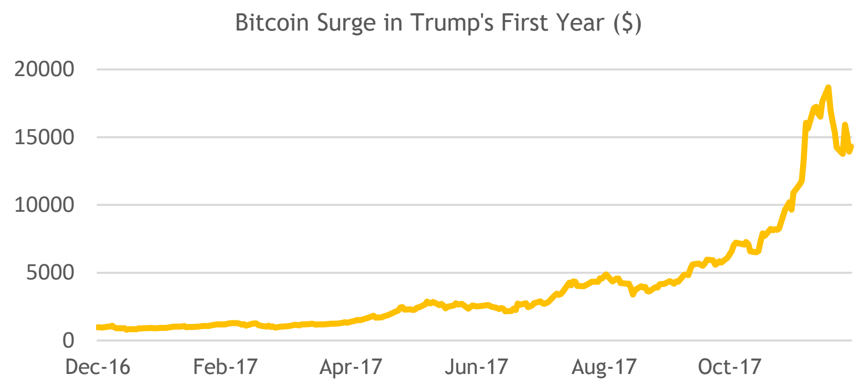
The reason for these sporadic bear steepening episodes after each event could be linked to Trump's idea of eliminating US income tax and replacing it with tariffs on imports. Such a radical tax reform could risk jeopardizing the fiscal health of the country. As we have mentioned in the past notes, bear-steepening is one of the more negative yield regimes for EM Asian currencies vis-à-vis USD.

Meanwhile, the "Fed easing" trade anchors the front end of the UST curve. Data releases of late as well as Fed speaks suggest increasing focus on the employment conditions at home, paving the way for rate cuts to start within the year.

2) **The Rise of Bitcoin**

Another common observation after both events was the rise in bitcoin. Trump had declared support for cryptocurrency in late May, pledging to ease regulation on cryptocurrencies. He also accepts campaign donations in bitcoin and some other cryptocurrencies. We recall that bitcoin had indeed rallied around 20x from $967 as of 28 Dec 2016 to a high of $19,511 on 18 Dec 2017, within the first year of Trump's first term as the US President. Biden has also recently ramped up crypto industry outreach, seeking guidance on "crypto community and policy". However, Trump's recent commitment successfully marketed a Trump Presidency as a more favourable one for crypto compared to Biden.

Chart 5: Bitcoin After Trump got Elected as 45th President of the US

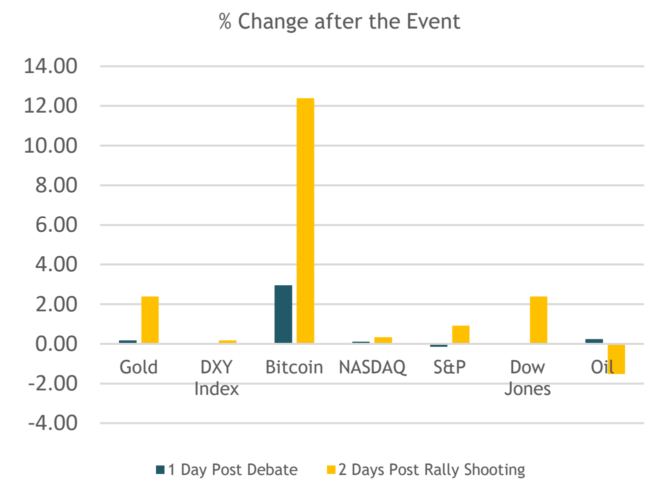


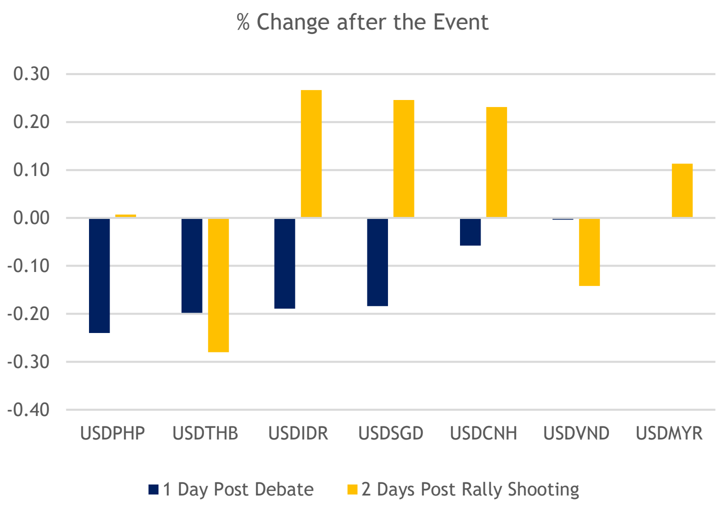
Source: Bloomberg, Maybank FX Research & Strategy

3) Markets Perceive Trump to be Positive for Equities for now

Trump's penchant to use the stock markets as a gauge of his success in his first term likely prompted to US bourses to rise along with his polls recently.

Chart 6: The Impact of the Biden-Trump Debate and Trump Shooting





Source: Bloomberg, Maybank FX Research & Strategy

4) Impact on Currencies Could Be More Nuanced

The impact on currencies after the Biden-Trump Debate was not clear as the focus was also on the US data. Core PCE price index for May (28 Jun) and Jun ISM Mfg (1 Jul) printed softer, bringing the USD lower against most currencies.

By mid-Jul, markets are almost fully priced in for a Fed cut in Sep, the Trump trade began to manifest more clearly after the failed assassination of Trump and even lasted longer. Gold rose more discernibly as the risks of further geopolitical escalations are seen rising with the prospect of a Trump presidency. Some of the Asian currencies (SGD, MYR, IDR) have started to give up recent gains against the USD over the two-days. VND, on the contrary, strengthened but we suspect this is due to news that President To Lam has taken over some of the duties from the Party Leader in a sign that the fight for party leadership is near an end. The rise in gold likely also lifted the THB.

The impact on the DXY index (which takes into account USD move against the EUR, JPY, GBP, CAD, SEK and CHF) was relatively muted as indicated on Chart 6.

Tariff Hikes – Potential Inflation Divergence between the US and RoW that could Strengthen the USD

One of the earliest headlines that grabbed market's attention was Trump's threat to raise tariffs on Chinese goods to 60% back in early Feb this year. In addition, Trump also mentioned a 10% blanket tariff for the rest of the world. Taken together with the China-targeted tariff hikes in store, such a trade policy could trigger a deflationary shock to the rest of the world (according to our economists) as shipments from China would be diverted to other parts of the world whilst also, increasing costs for US businesses. Our economists also warned on the use of rules of origin on third party countries to crack down on trade evasion and diversion.

We opine that risks could be arguably tilted to the upside for the US inflation in the medium term should Trump come into power and such a drastic policy could drive a divergence between the inflation trajectories of the US and the rest of the world, bringing back the possibility of US rate exceptionalism and USD strength emerging again in 2025 and beyond.

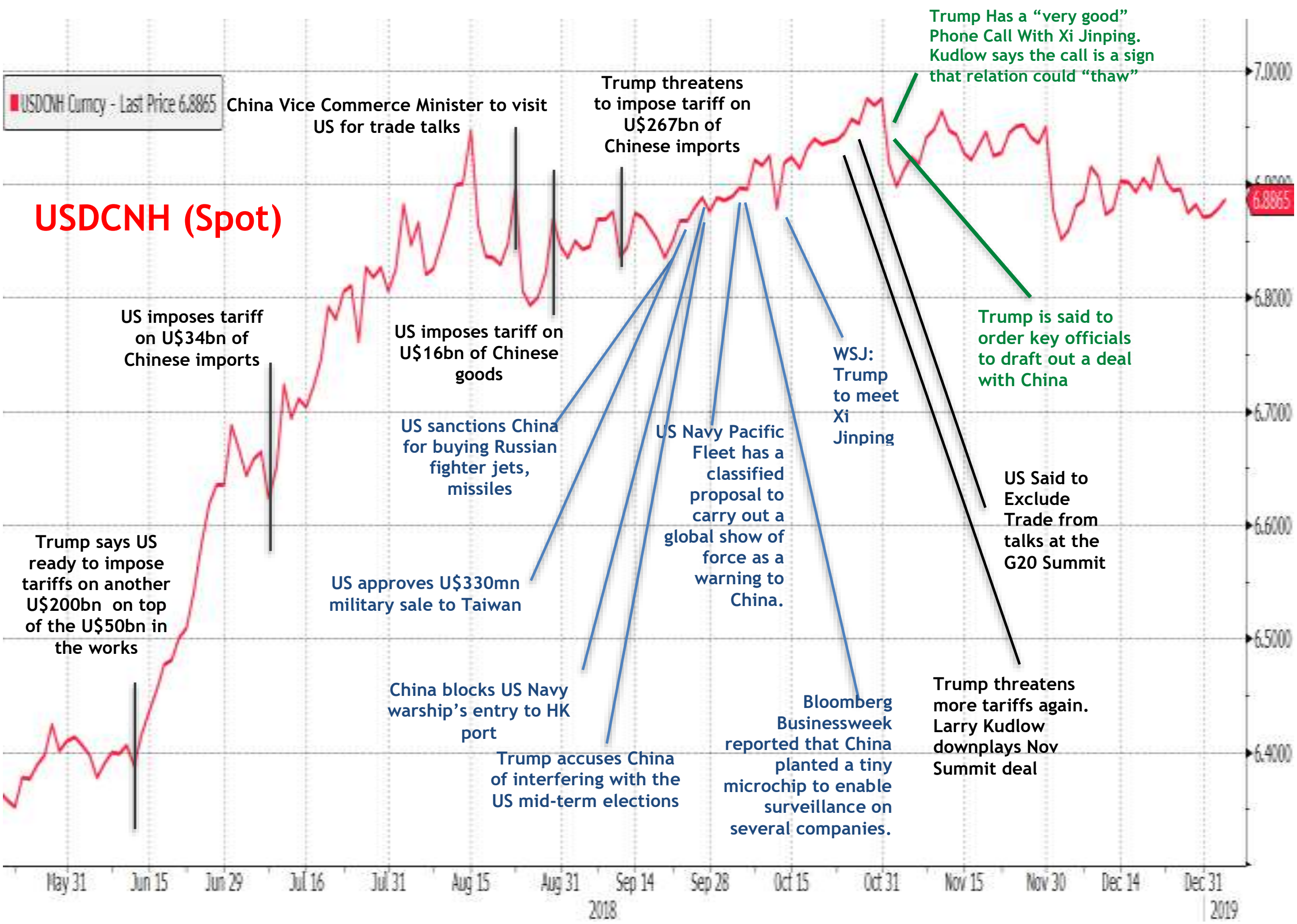
Significant Tariffs on China to Severely Undermine US-China Bilateral Relations Once Again

Revoking the Most Favoured Nation (MFN) Status for Chinese imports had been gaining traction amongst policymakers for a while. It was a recommendation from the US Congressional Select Committee on the Strategic Competition between the United States and the Chinese Communist Party (source hinrich foundation).

This status is granted to all WTO members and it is now called the Permanent Normal Trade Relations (PNTR) in the US. Removing this status for China allows the US to impose any level of tariff rates it desires. That would bring the world back to the days of his signature trade war with China. The CNY had weakened 15% against the USD between 2018-2019. That however, happened in the middle of a hiking cycle in the US and the shock of the first trade war along with the uncertainties of the global economic outlook added pressure on the yuan as well as many other EM currencies then.

As one can tell from chart 7 below, USDCNH rose with every additional tranche of tariff imposed on China by the US in 2018. However, the magnitude of each rise of USDCNH was discernibly smaller for the last two tranches/threats in 2018. Markets were increasingly less sensitive to news of more tariffs. The tail end of the Fed's rate hike cycle might also have played a part in mitigating the impact on CNH.

Chart 7: Throwback to US-China Trade-War 1 in 2018 and How USDCNH Reacted



Source: Bloomberg, Maybank FX Research & Strategy

The above chart shows the behaviour of USDCNH along with significant events in 2018. It does not tell the full trade war story.

Let us look at the trade war that started in 2018

6 Jul 2018 - US imposed 25% tariff on $34bn worth of Chinese imports

23 Aug 2018 – US imposed 25% tariff on another $16bn worth of Chinese goods.

24 Sep 2018 – US imposed 10% tariff on $200bn of Chinese imports.

1 Dec 2018 – Truce

So within 2018, USDCNH rose around 12%.

Let us look at the 2019 trade war development.

10 May 2019 - Trade negotiations broke down and the **US increases tariffs on $200bn worth of Chinese goods from 10% to 25%.**

15 May 2019 – Huawei is on US Department of Commerce's "entity list"

29 Jun 2019 – Truce is declared again at G20 summit in Japan

1 Aug 2019 – US declares **10% tariffs on another $300bn of Chinese goods starting 1 Sep**

5 Aug 2019 – US Designates China as a "currency manipulator"

1 Sep 2019 – US tariffs on more than $125bn worth of Chinese imports take effect. With some delayed to Dec.

13 Dec 2019 – Phase 1 of Trade Deal Agreed

13 Jan 2020 – US officially drops China's currency manipulator label before the signing of the phase 1 deal on 15 Jan 2020.

Source: SCMP, China Briefing

USDCNH's Behaviour in Trade War 1 and what we can Expect from Trade War 2.0

The trough to peak USDCNH move was measured to be 7.0% for 2019. This takes into account the impact of the US repo crisis in Sep 2019 that added to USD strength then. Arguably, the tariffs threatened and imposed in 2019 were targeting a lot more Chinese goods ($250bn in 2018 vs. $350bn in 2019). However, the impact on the USDCNH in 2019 was comparatively smaller. This could be due to frequent, albeit rocky trade negotiations in 2019 which might have provided some periods of calm and restrain in yuan bears. In addition, the Fed had started to cut policy rates in Jul 2019.

Should Trump come into power in 2025 and follow through with his pledge to declare trade war 2.0, it is no surprise that the impact on yuan will be negative. However, the Fed would then be in the middle of an easing cycle. That is one less negative factor on yuan compared to trade war 1.0. Nonetheless, the shock of a second trade war would be significant. Market estimates of damage on China's GDP are around 2-2.5ppt damage should the US levy 60% tariff on China and 10% on the RoW. Just like what we saw in the first trade war, the amount of Chinese goods targeted and the tariff rate hikes in 2019 have to be bigger and higher in order to elicit the shock and awe that the tariffs evoked in 2018.

We see similar strategies already in the campaign promises of eye-popping tariff rates of 60-100% on Chinese goods promised to the American people. He recently mentioned 50%. Regardless, the tariffs for China would be high. Given the rising polls in favour of a Trump victory, some of that fear and concern, along with China's fragile economic outlook, should have lifted the USDCNH more. However, that did not happen so far. USDCNY is up a mere 2.5%ytd (as of 19 Jul), likely capped also by the local authorities. Perhaps, we could be too early in the race for the 47th Presidency to tell but markets would know by now to take Trump literally on his words.

Potential Impact on ASEAN FX

Our economists identified *Vietnam* as a potential third country target given its *widening bilateral trade surplus with the US, growing intermediate imports and FDI from China. Malaysia, Singapore and Thailand are at risk of collateral damage given their export dependence. Indonesia and the Philippines are less at risk because of their low trade dependence and not being major beneficiaries of the supply chain shifts.*

We looked back at how currencies fared in 2018-2019. Given that the trade war was largely targeted on China, it is no surprise that the yuan was one of the worst hit. While the rest of the currencies actually recovered into 2019, the yuan remained comparatively under pressure as shown in the chart 7b aside from a slight rebound. Bearing in mind that the Fed had hiked 100bps in 2018, we can imagine why the worst hit ASEAN FX was actually the IDR. IDR was hurt by both negative sentiments/confidence effects from the trade war as well as the effects of the Fed rate hikes. THB was one of the least affected, cushioned by the gold rise during this period of geopolitical conflict, which Thailand exports and given its gold hub status.

Chart 7a: % Change of ASEAN+China FX from 1 Jan 2018 to their respective trough between 2018-2019

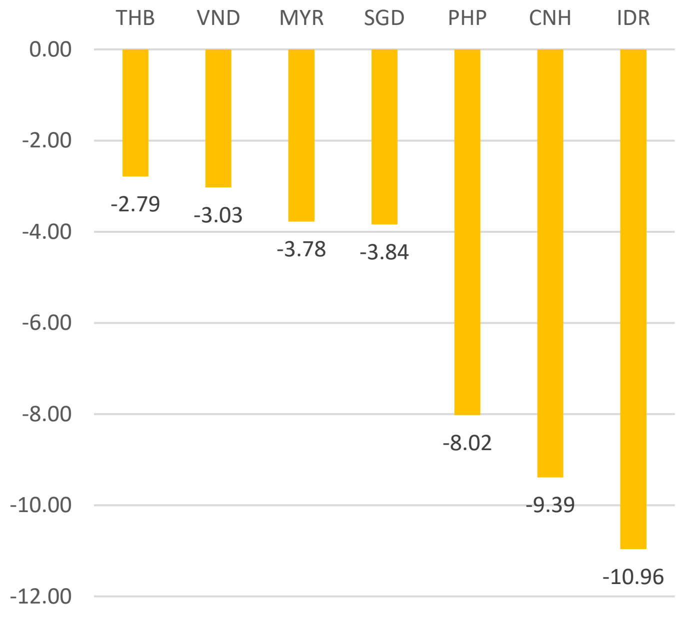
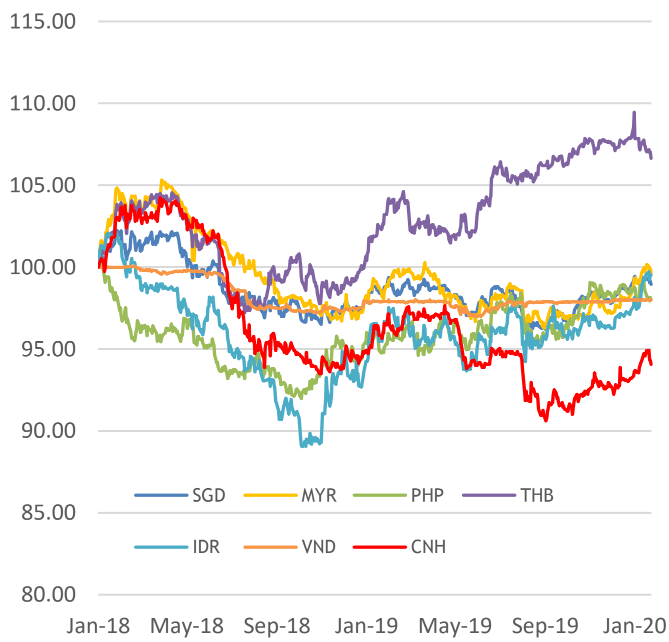


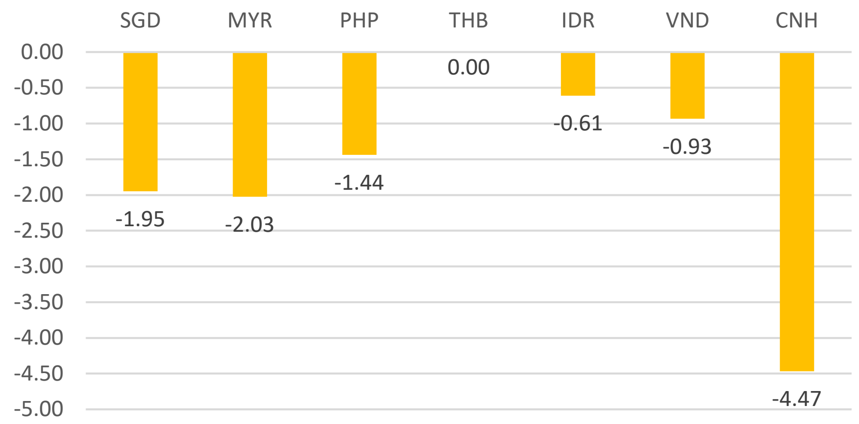
Chart 7b: Currency Movements Against the USD with respective prices on 1 Jan 2018 taken to be 100



Source: Bloomberg, Maybank FX Research & Strategy

Singapore, Malaysia and Vietnam were added to the US Currency Watchlist in **May 2019.** Along with that, there was also an escalation of trade war with China as negotiations broke down and the **US increases tariffs on $200bn worth of Chinese goods from 10% to 25% on the 10th.**

Chart 8: %Change of ASEAN+China FX vis-à-vis USD from 1 Jan 2019 to their respective trough in 2019

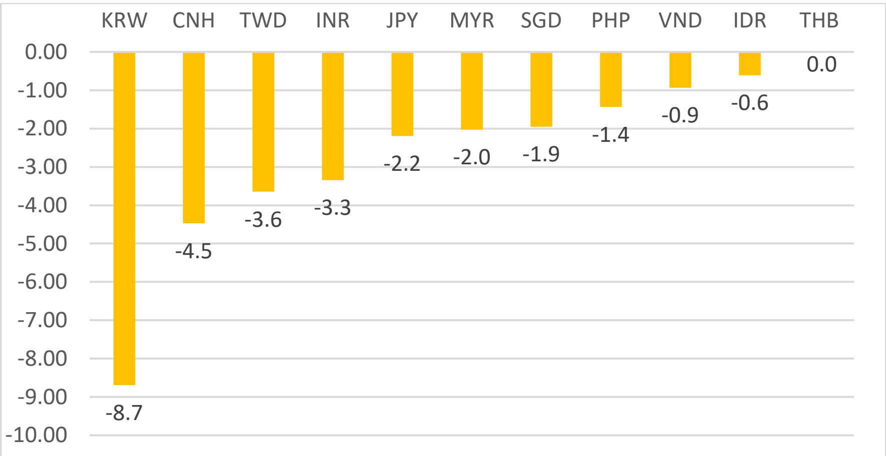


Source: Bloomberg, Maybank FX Research & Strategy

SGD and MYR slid a further 2%, reaching a trough for the year in Jun 2019 after being added to the US currency Watchlist, clocking a steeper decline than VND, PHP, IDR and THB. Their sensitivity to the CNY also likely amplified their weakness. We can imagine that in an environment of no further rate hikes, SGD and MYR's sensitivity to CNY as well as the concerns on being added to the US currency watchlist in May 2019 have led to their underperformance among ASEAN peers.

However, if we expand the list of currencies to other Asian peers, SGD and MYR's underperformance seemed almost muted compared to KRW and TWD. These currencies were much more sensitive to yuan and their dependency on exports and the deglobalization trend likely hurt these risk-sensitive currencies the most as shown in Chart 9.

Chart 9: % Change of Asian FX from 1 Jan 2019 to their respective trough in 2019



Source: Bloomberg, Maybank FX Research & Strategy

This trend of de-globalisation could come back more strongly should Trump return to the oval office and follow through with his pledged trade policies, potentially sinking KRW and TWD along with the CNY once again. SGD could soften as well, faced with a scenario of a Trump-triggered deflationary shock that may potentially allow room for MAS to ease its policy. We prefer relative value plays and we expect KRW, TWD, CNY, SGD to underperform the IDR, PHP and THB.

The USD may be anchored to some extent as the world anticipates the start of the Fed's easing cycle, compared to the 2018 trade war which took place in the middle of a Fed hiking cycle. However, should Trump policies come into play, the balance of risks is skewed to the upside for the greenback against most currencies but not without two-way swings.

We also see opportunities for long G10 short Asia trade such as long EUR short CNH. This has been playing out for a good part of this year. A revisit of 8.12 cannot be ruled out if Trump stops aid to Ukraine and end the war in Ukraine whilst starting another trade war with China

Trump Calls Out Yen and Yuan Weakness

Another item on Trump-Vance's wishlist surfaced more prominently recently and this complicates the nature of Trump trade. According to the Bloomberg Businessweek interview on 17 Jul, he highlighted the weakness of the yen and yuan, insinuating that he may try to weaken the USD if he were to come into power, in order to boost the competitiveness of the US exports. USDJPY dropped 1.4% while USDCNH fell 0.2% on that day. We cannot be sure that this move was due entirely to Trump's comments. Rumours of JPY intervention floated in markets. His blatant desire for softer USD suggests that he may attempt at exerting some influence on the greenback. Such soundbites also trigger USD swings. As to whether he can actually do it, we think it is less probable as it largely contradicts the rest of his agenda which are mostly inflationary (tariff hikes, tax cuts, anti-immigrants).

The effects of these soundbites may either diminish over time if there are no concrete plans to follow through with it, or simply add to the two-volatility. Given that a weak USD is still a prominent part of the Trump-Vance agenda, more sound-bites are likely to come along. That could actually dampen the uptrend of the USDCNY.

Further Corporate Tax Cuts, Anti-Immigrant Drive

Trump's promise of extending corporate tax cuts (currently at 21%) from his 2017 Tax Cuts and Jobs Act (TCJA) and to lower it even more to 15% (based on his latest interview with Bloomberg Businessweek 17 Jul) could add to demand pressures. He also wants to set more limits on legal immigration and guest-worker visas in order to lower the immigration levels. That could potentially lower the supply of labour and risk reigniting inflation.

Taken together with the impact of tariffs, the Fed may not be able to cut as much as it would have without the said policies in place. As such, the desire for weaker USD may not come to fruition. It is hard to see how Trump can eat his cake (hike tariffs, cut tax rates, restrict immigration) and still have it (weaker USD, lower interest rates). The latter of which could have less political mileage than the former in his political base. He would likely prioritize tariff hikes, tax cuts and anti-immigrant policies as he has attempted these policies before with significant effects.

In Conclusion

Gold, bitcoin and US bourses in general are beneficiaries of Trump Trade. The Trump trade also brings about bear-steepening of the UST curve.

In terms of equities, Trump has a penchant to use the stock market as a gauge of his success. Hence, equities tend to rise alongside Trump's approval ratings. His advocate for the oil industry, less regulations are seen as positive for the petroleum and banking. However, Biden had the CHIPS Act and so he is seen as more positive for technology stocks. Trump on the other hand, criticized Taiwan for taking away the US microchips business and he wants them to pay for defence. Regardless, it will be challenging for Trump to undo the CHIPS Act given that it has been approved by Congress. As such, on net, US bourses could still potentially get a health boost from corporate tax cuts.

When it comes to the FX aspect of the Trump trade, balance of risks on **net is skewed to the upside for the USD** based on the potentially inflationary effects of Trump's proposed policies on the US economy which could also produce also a deflationary shock to the rest of the world as China's excess supply gets diverted to the rest of the world. We see potential for a divergence of inflation trajectories between the US and the rest of the world and that could bring back US rate exceptionalism again. These policies (tariff hikes, tax cuts, anti-immigrants drive) are likely to be prioritized over their desires for a weaker USD and lower interest rates given that Trump had enacted those policies in his first term with grand effects. Despite the last election loss in 2020, his persistent popularity could likely embolden him to do more. Yuan would be under pressure once again but even with greater tariffs in store, pressure on yuan would not be proportionately larger as the Fed is in an easing cycle compared to a hiking cycle in 2018. In addition, Trump had recently called out yen and yuan weakness last week. He could do that again and that would dampen the rise of the USDJPY and USDCNY, albeit with diminishing effects.

In terms of relative value plays, we look for PHP, IDR and THB to remain more resilient compared to CNH, CNY, SGD, MYR, KRW and TWD. SGD, MYR, KRW and TWD could remain sensitive to impact on the yuan. SGD this time could see potential for MAS easing should Trump's trade produce a deflationary shock. PHP, IDR could be as insulated as what was observed before in 2019 when the Fed is about to cut rates. THB would get its usual boost from the gold.

EURCNH could rise.

This is not the base case scenario for 2025. This piece is all about illuminating the Trump Trade that can emerge and fade for the next few months depending on the US election developments. Thus far, Trump has secured a solid nomination from the Republicans and achieved a wide margin of lead over Biden before the latter dropped out. That is why the Trump trade had been the focus. Should Trump win the electoral votes on 5 Nov, we can expect this characteristics of the Trump Trade to manifest more strongly thereafter.

Due to the election uncertainties however, we can expect the USD decline to remain bumpy. USDAsians could continue to see some upside risks especially with yuan under increasing pressure in 3Q. In addition, Aug and Sep are seasonally strong for the USD as well. In addition, a Sep rate cut is already well priced which leaves room for USD and US rates upside should the next few data releases come in firmer.

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