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Viewpoint | China

A Trump win is not good for China's economy

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- **The election of Donald Trump as the next president of the US means significantly more uncertainty for China, spill-over from likely lower growth in the US and a shift in US policy on globalization and free trade, with repercussions for China's exports and, perhaps, the CNY.**

- **In all, we expect more downward pressures on China's growth in 2017 because of the Trump win, probably leading to some more stimulus. But we do not change our forecast for the CNY in the coming quarters and continue to look for gradual depreciation.**

A changed outlook for the US

More uncertainty...

First and foremost, a Trump presidency will mean more uncertainty. More uncertainty about politics, policies, the economy and financial markets. In the coming months, some of the uncertainty will fade away as it becomes clear who the key personalities in the administration will be and on what kind of initiatives can Trump and the Republicans in Congress (they will have a majority in both houses) find common ground relatively quickly. But even then uncertainty would remain as to the new President's approach on key economic and foreign policy issues and the chances of getting changes through Congress.

...and likely slower growth in the US

A Trump presidency is likely to be negative for economic growth in the US and globally, although it is unclear to what extent and so far financial market impact has been muted, reflecting a 'wait and see' approach. In any case, business confidence is likely to be hit by the heightened uncertainty. Also, policies such as more deportation of illegal immigrants are bad for growth. Markets are now increasingly pricing in more expansionary fiscal policy with tax cuts and/or infrastructure spending, but its effect is unlikely to be large enough to fully offset the negative impact on GDP growth of Trump's other policies. Since the election outcome we have revised down our US GDP growth forecast for 2017 slightly to 1.9% (from 2.1%). However, we maintain our forecast that the Fed will raise its policy rate in December.

Trade restrictions or renewed currency bashing?

Imposing tariffs is actually not straightforward

In addition, under President Trump the US will become more averse to globalization and free trade, and that will be particularly unfavourable to China and Asia. One of the headline grabbing policies that Trump campaigned on was the imposition of high tariffs on imports from China and Mexico. However, in the US' political system this is not straightforward. For many types of trade restrictions he would need backing from the Republicans in Congress, and it may not be easy to get this given the Republican party's traditional stance in favour of free trade. Moreover, most types of tariff would break WTO rules and China is highly likely to retaliate.

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In principle, the US President can impose (temporary) tariffs under the WTO safeguard agreement. This is what President Obama did in 2010, in the case of Chinese tires. For such tariffs to be implemented, the non-partisan United States International Trade Commission would have to determine that the exports have caused material harm to the affected industry in the US.

Tariffs imposed outside of the WTO safeguards agreement would be illegal under WTO rules, giving China the right to retaliate. But historical experience suggests China is likely to retaliate even to tariffs under the WTO safeguard agreement (it imposed tariffs on chicken meat in retaliation to the tariffs on tires). This retaliation does not always have to take the form of outright tariffs. There are various measures China could take that are unfavourable to the sizeable operations of US companies in China (the stock of US FDI in China was US$ 80 bn in August 2016). Also, agricultural products constitute a large share of US exports to China and such products are particularly vulnerable to the imposition of food safety-related inspections or bans.

Given such complications, we think that the Republican leadership of the House and the Senate will probably urge Trump to first focus on issues that all Republicans can agree on – tax cuts and deregulation for businesses – rather than major trade restrictions on Chinese exports. Since the President needs to have many parts of his agenda passed by Congress, this gives the Republican leadership some leverage over him.

Other initiatives unfavorable to China may be easier to push through

The need for Trump to deliver something anti-China in the face of these constraints makes it possible that he will – as he promised to do – push the US Treasury to name China a currency manipulator. As such this will be awkward, as the PBoC has recently spent sizeable amounts of reserves preventing the currency from depreciating more. Also, it would not have major repercussions (other than Chinese companies loosing access to US government procurement). But it is relatively easy to do and would receive a lot of attention. Another area in which it is likely that a Trump administration will move in a direction unfavourable for China is the attitude to Chinese FDI in the US and the ongoing negotiations of a Bilateral Investment Treaty.

In any case, the new US administration is a negative for China's exports

In all, imposing high tariffs on China is not so straightforward. Nonetheless, the new administration's policies towards international trade and currencies is a negative for China, the world's largest exporter and the most important beneficiary of globalization. China is likely to face a more hostile environment for exports to the US, which is the destination for 20% of its exports, and we have reflected this in our new China forecast.

Impact on China's growth and macro policy

Downward pressures on China's growth have risen due to the US election

Weaker exports and an unfavourable impact on corporate investment because of greater uncertainty will make it more challenging for the government to meet its GDP growth targets of 6.5% through 2020. Given the concerns about excessive credit growth, and the fact that Trump-induced weakness is clearly an external development may make it easier for policymakers to accept some of the impact and to reduce growth ambitions. However, we think that the leadership will remain keen to preserve stability on all fronts in the run up

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to the 19th Party Congress in H2 2017. Hence, the government is likely to offset some of the impact in 2017 via macro stimulus, largely via additional fiscal expansion.

We recently nudged up our forecast for GDP growth in 2016 to 6.7% because of stronger than expected real estate sector developments. However, we now expect that the positive carry-over of this into next year will be offset by the impact of the more challenging environment post US-election, even with some additional stimulus. Therefore we have kept our forecast for GDP growth for next year unchanged at 6.3%.

The CNY

US trade restrictions on Chinese products will put negative pressure on the CNY. More generally, weaker growth of exports and GDP in China will be bad for the CNY. Also, China's policymakers may allow the currency to depreciate more in response to the imposition of US trade restrictions. However, a more hawkish US stance on the CNY, which, as we noted above, we find likely, may by itself lead to some appreciation. Also, if the US Fed rate hike in December does not materialize, the pressure on the CNY should diminish. In all, we have kept our forecast for the CNY unchanged. We expect it to reach 6.84 against the US$ by end-2016 with some further depreciation to 6.9 through mid-2017.

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