Wong Kok Hoi
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US-China Trade War?

I invited former Singapore Cabinet Minister Raymond Lim and China expert Professor Tan Kong Yam to a roundtable discussion with our investment teams across Asia recently to discuss rising US-China trade tensions. Here are the salient points of the discussion -

We believe the real issue goes beyond tariffs on goods. What is of greater importance is a developing hawkish stance designed to slow China's advancement on the global stage.

The tariffs to be placed on steel and aluminium, for example, is noise compared to what the US would like to redress in areas such as technology. China has accumulated vast amounts of intellectual property through its joint ventures and acquisitions over many years. There is growing interest to slow this trend as this has threatened US supremacy in an area they have dominated in the past.

Trade is important to Trump as this has been a central concern within his voter base. This negative sentiment against China had been brewing even before this last US election, therefore we don't believe this is an issue that will go away soon. Many investors are concerned that measures will be rolled out quickly by the Trump administration in this trade tussle, without much discussion within the US, and little negotiation with China. The good personal rapport Trump perceives he has with President Xi Jinping is at odds with the hawkish position of some within his own administration, possibly complicating things further. We believe Trump will focus on the short term as he believes he can "win in China".

To China, this is a game of Go, not chess. The Chinese administration will in all likelihood be more strategic and play the long game. What is of more concern to China would be the growing hawkish sentiment among the American and European corporate as well as political elites. China's priority is to avoid having the trade issue become the catalyst for the US unifying allies such as Japan, South Korea, Australia, and some European nations into an anti-China alliance.

Because China understands that the issue is much bigger than trade, it will methodically choose its next move. Its initial reaction will likely be calibrated and proportional to prevent escalation. They may impose tariffs on categories such as American fruit, wine, and pork as retaliation for US tariffs on aluminium and steel. China has likely compiled a longer list of targets aimed at Trump's voter base, such as agricultural exports, as a potential response to Washington's Section 301 list when it is revealed. In order to pacify Trump, China may increase imports in the areas of oil and gas, aircraft, and industrial equipment to help narrow the trade deficit.

In the medium term, the recent episode will further propel China to reduce its export dependence on the US market and accelerate the structural shift of the Chinese economy to become more domestic consumption driven. Artificial intelligence and cyber security will likely be some of the other key areas that will see supportive policy from Beijing. While some technology hardware names may face short term headwinds, we believe the Chinese government will offer more support to further develop this sector. These companies may benefit in the long run, especially if they generate more of their revenue domestically.

In the long run, China will likely relocate some manufacturing to ASEAN nations to reduce its US trade surplus, which is positive for growth in Southeast Asia. We expect to see some relocation of manufacturing to the US as well, especially in states of political significance. We witnessed this scenario following the Japan-US trade friction in the 1980s.

We expect to see elevated levels of volatility in the medium term. If the market's knee-jerk reaction stretches out into a more sustained sell-down, it may create buying opportunities as many Asian markets and companies are supported by strong fundamentals. However, we are cognizant of the strong run in stock prices across Asia prior to the recent sell-off, so we remain patient and will stay disciplined in terms of valuations. At APS, we tend to not react to short term noise, and instead we will be looking carefully at the long-term implications of this trade tussle, in particular on what it portends for the existing liberal rules-based economic order.

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The Founder and CIO, Wong Kok Hoi, has over 35 years of investment experience, including CIO at Cititrust Japan, Senior PM at Citibank HK, and Senior Investment Officer of GIC. He was the recipient of the prestigious Mombusho Scholarship in Japan, and graduated with a Bachelor of Commerce (Honors) degree from the Hitotsubashi University (1981). Mr. Wong also graduated from the Investment Appraisal and Management Program at Harvard University (1990).

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