

Reforms and Resilience in Asia: 20 Years after the Asian Financial Crisis

12 June 2017, Bangkok, Thailand

Mandate

- Conduct macroeconomic and financial surveillance of global and regional economies
- Contributes to early detection of risks, policy recommendations for remedial actions and effective decision-making of the CMIM

Core Functions

Surveillance

- Conducting macroeconomic surveillance (regional, member countries, functional/sectoral) and conducting thematic studies/research

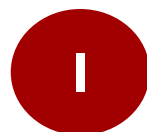
CMIM Support

- Providing support to the members to ensure that the CMIM is operationally ready

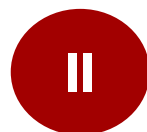
Technical Assistance (TA)

- Providing TA to the members to enhance their human and institutional capacities for macroeconomic surveillance and implementation of CMIM

Contents



ASEAN+3 Macroeconomic Prospects and Challenges



Thematic Chapter: ASEAN+3 Region 20 Years after the Asian Financial Crisis



ASEAN+3
REGIONAL
ECONOMIC
OUTLOOK 2017

ASEAN+3 Region:
20 Years after the
Asian Financial Crisis



Chapters

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ASEAN+3 Macroeconomic Prospects and Challenges

II

Thematic Chapter: ASEAN+3 Region 20 Years after the Asian Financial Crisis

Chapters

I

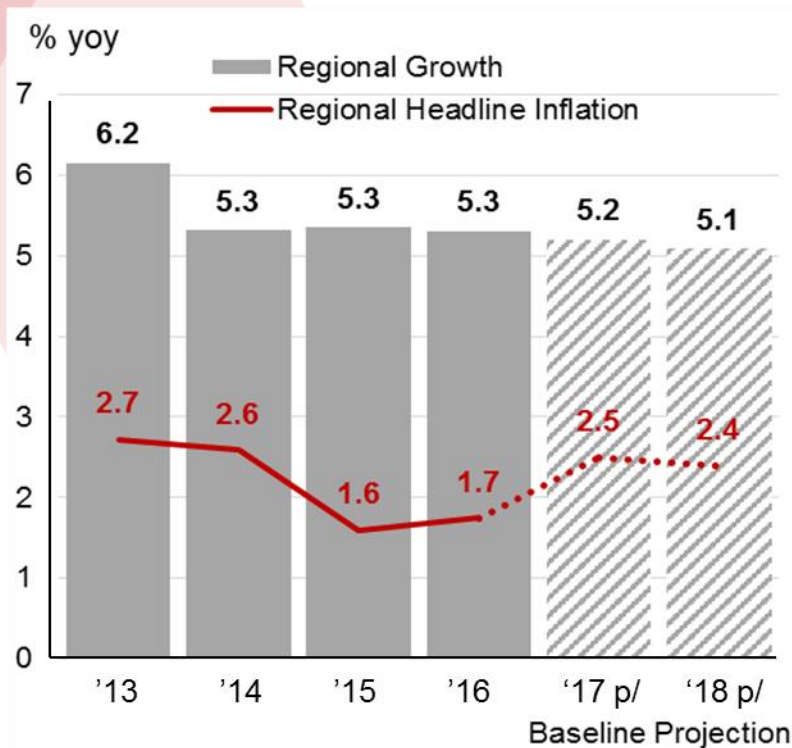
ASEAN+3 Macroeconomic Prospects and Challenges

II

Thematic Chapter: ASEAN+3 Region 20 Years after the Asian Financial Crisis

Amid the external uncertainties, regional growth will continue to be driven by domestic demand. Growth is anticipated to moderate slightly, but sustained around 5 percent in 2017-18

ASEAN+3: Baseline Growth and Inflation Projections



	'16	'17 p/	'18 p/
China	6.7	6.5	6.3
Japan (FY)	1.4	1.3	1.1
Korea	2.8	2.5	2.6
ASEAN-4 & VN	5.0	5.1	5.2
BCLM	5.6	6.5	6.8
HK & SG	2.0	2.1	2.3
ASEAN+3	5.3	5.2	5.1

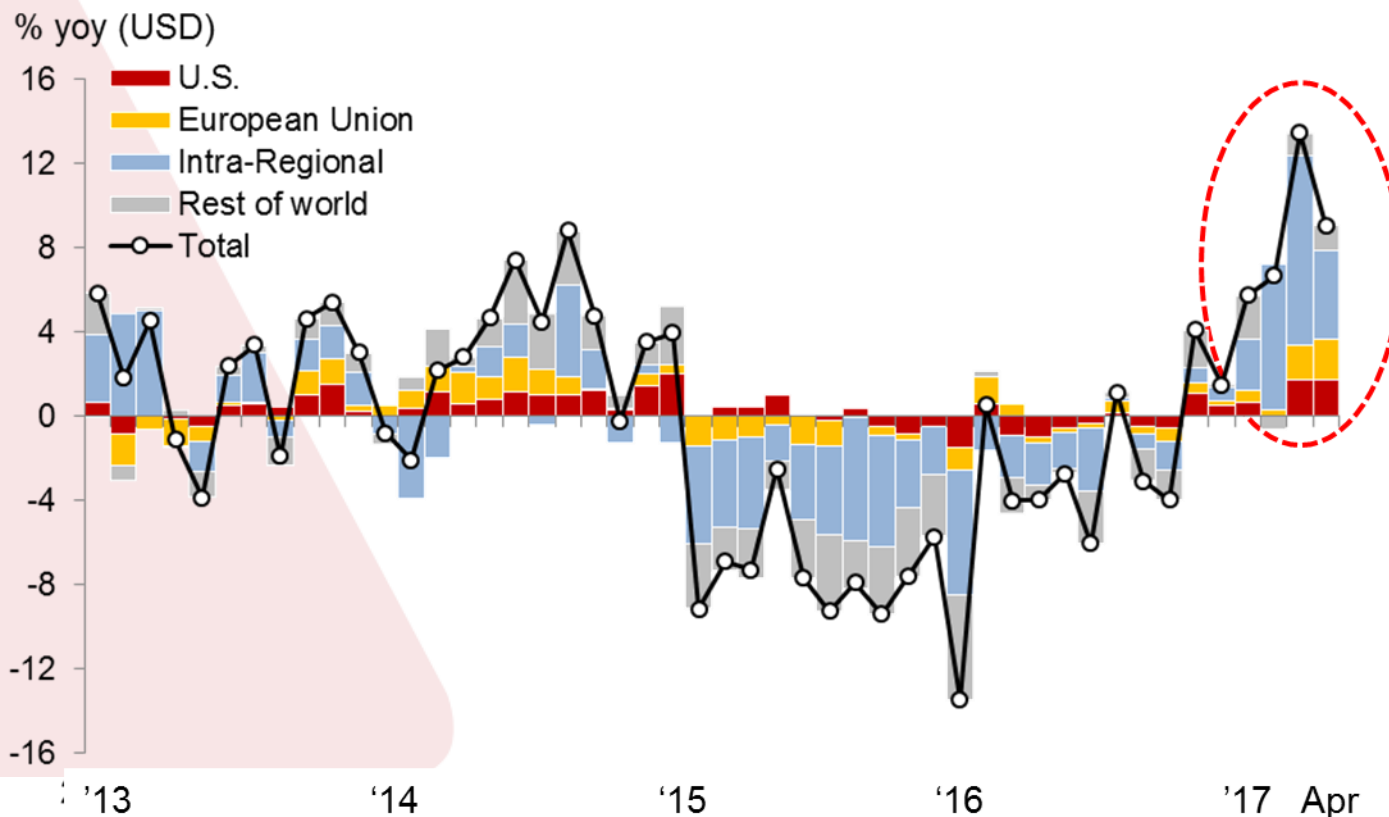
In ASEAN, growth is expected to be sustained around 5 percent in 2017-18, while inflation is expected to be manageable

ASEAN: Baseline Growth Projections

	'16	'17 p/	'18 p/
Brunei	-2.1	1.6	2.9
Cambodia	6.9	6.8	6.8
Indonesia	5.0	5.1	5.2
Lao PDR	6.9	7.0	7.0
Malaysia	4.2	4.5	4.6
Myanmar	6.0	7.0	7.2
Philippines	6.8	6.8	7.0
Singapore	2.0	2.0	2.2
Thailand	3.2	3.4	3.5
Vietnam	6.2	6.4	6.4
ASEAN	4.8	4.9	5.1

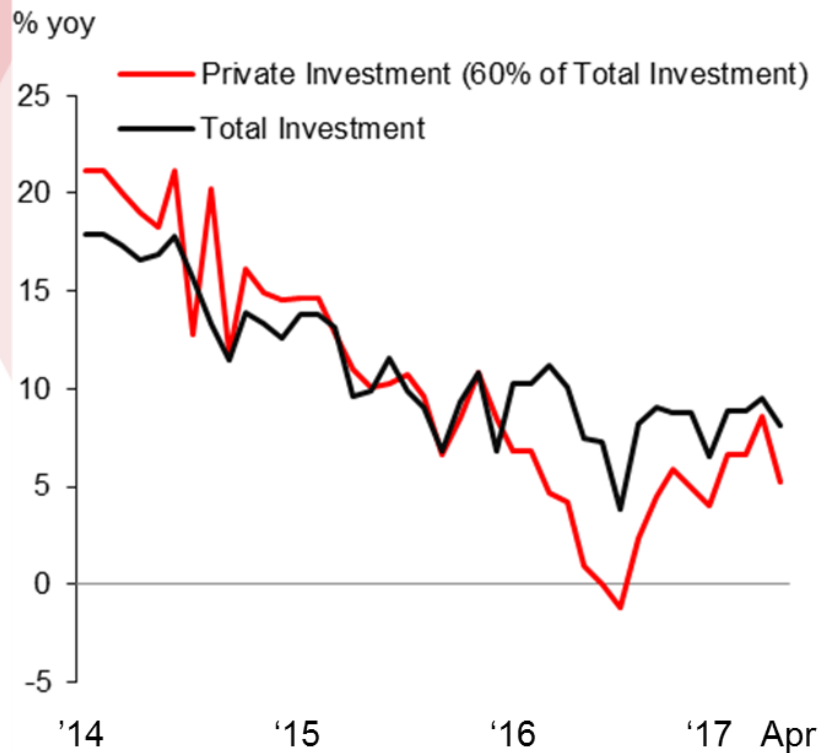
The recent recovery in global trade, if sustained, could provide some upsides to regional exports and growth

Regional Exports by Major Destinations

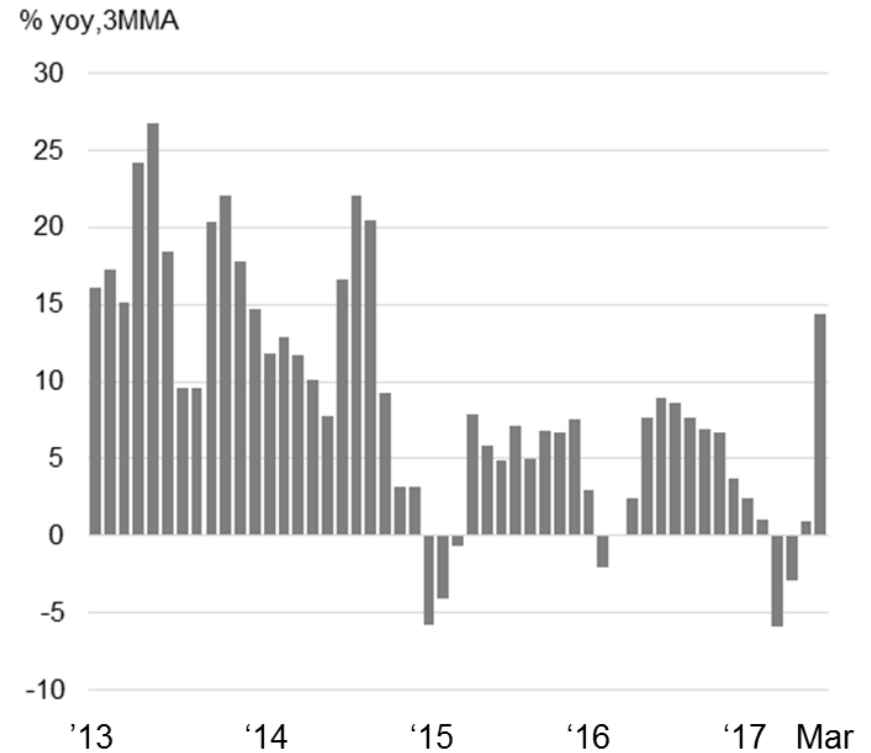


In China, the economy posted a relatively high growth in Q1 2017. Private investment is also firming, reflecting the pick-up in domestic economic activities, alongside an improvement in corporate profits

China: Private Sector Investment

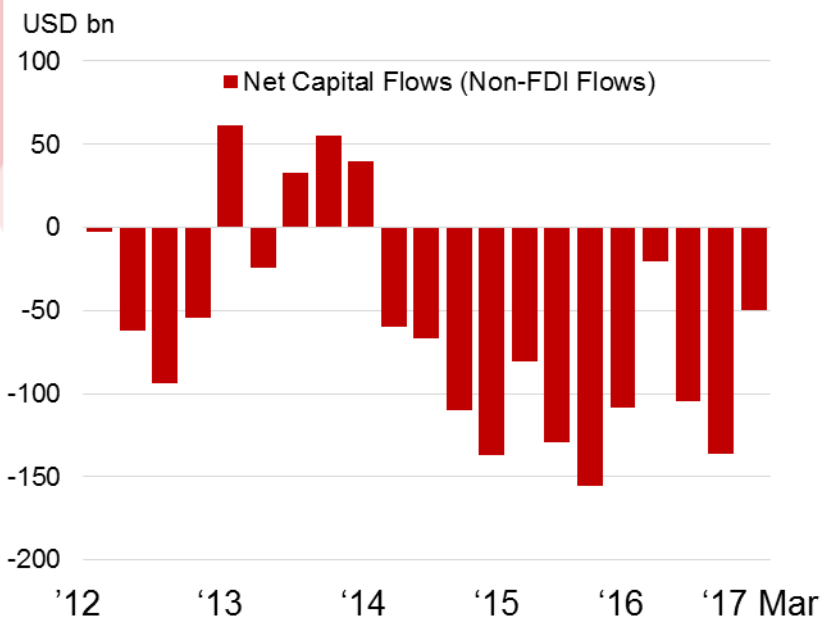


China: Private Sector Profitability

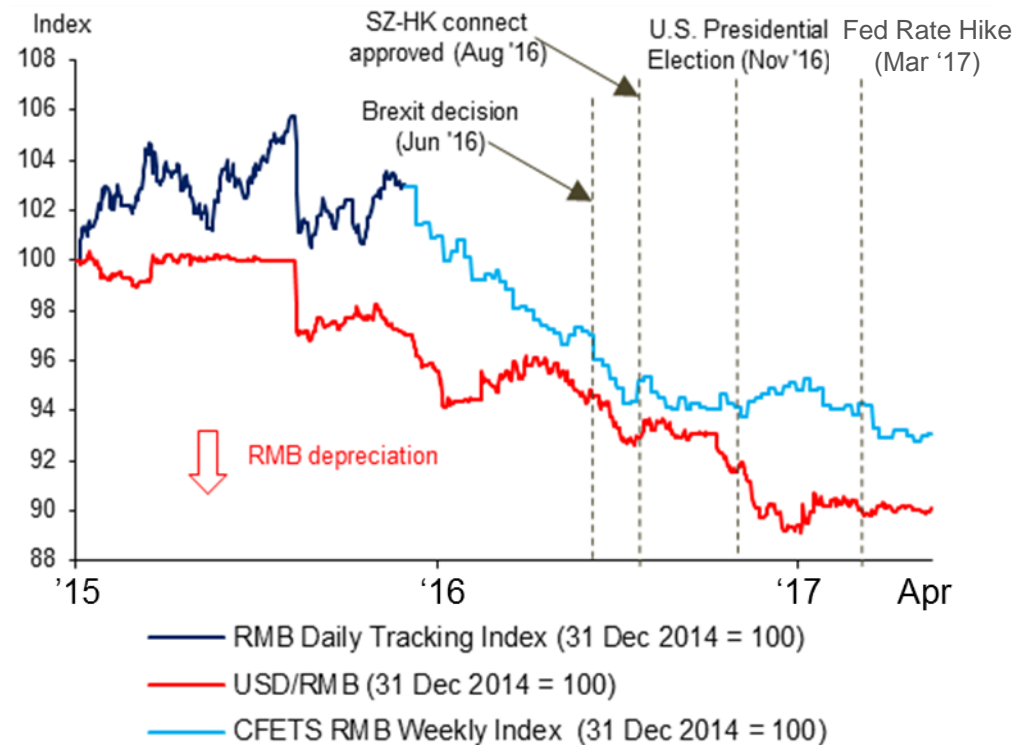


Concerns about China's capital outflows have eased recently, partly reflecting the strengthened capital flows management which helped in containing RMB exchange rate volatility

China: Capital Flows Developments

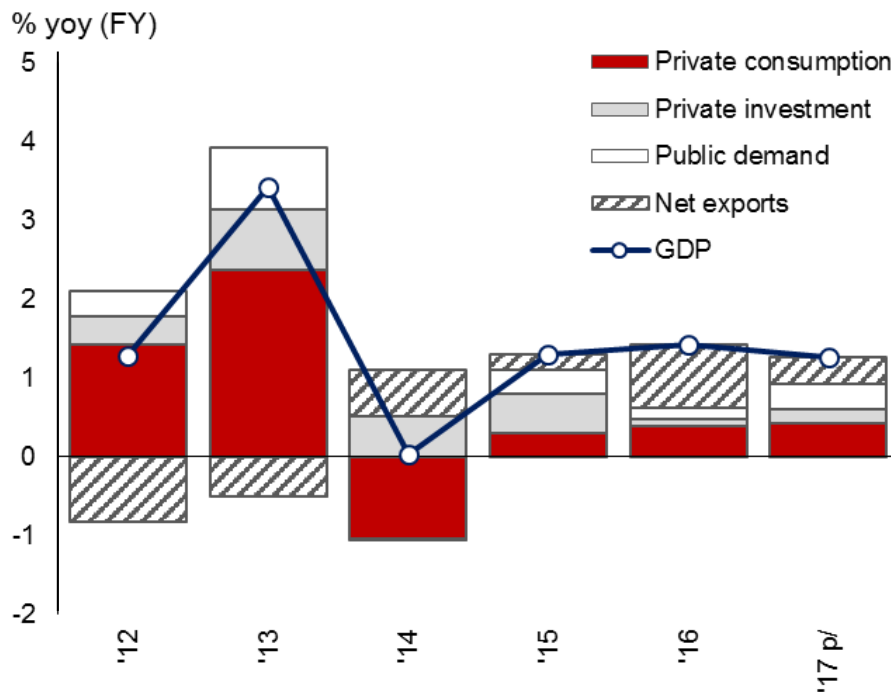


China: Exchange Rate Developments

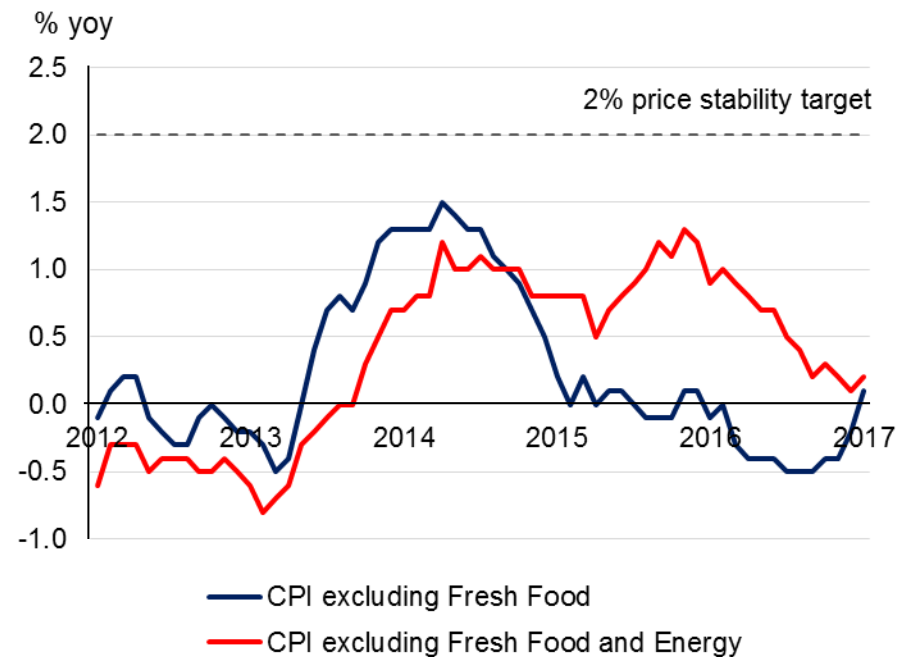


In Japan, growth is expected to remain strong in 2017, higher than the potential growth rate, while achieving the price stability target of 2.0 percent remains challenging

Japan: Real GDP Growth



Japan: Inflation and Price Stability Target



Spillover Analysis (Shocks from 1% sustained decrease (or increase) in U.S.' & China's real & financial variables), Preliminary

1. Real Sector Shocks

1% Sustained Decline in Real GDP Growth	Mean Impact on Regional EMs (Cumulative, 36 months)
<ul style="list-style-type: none"> 1% sustained decline in U.S.' real GDP growth 	Impact on growth → -0.11 pts
<ul style="list-style-type: none"> 1% sustained decline in China's real GDP growth 	Impact on growth → -0.75 pts Impact on nominal export growth (in local currency) → -1.35 pts

2. Financial Sector Shocks

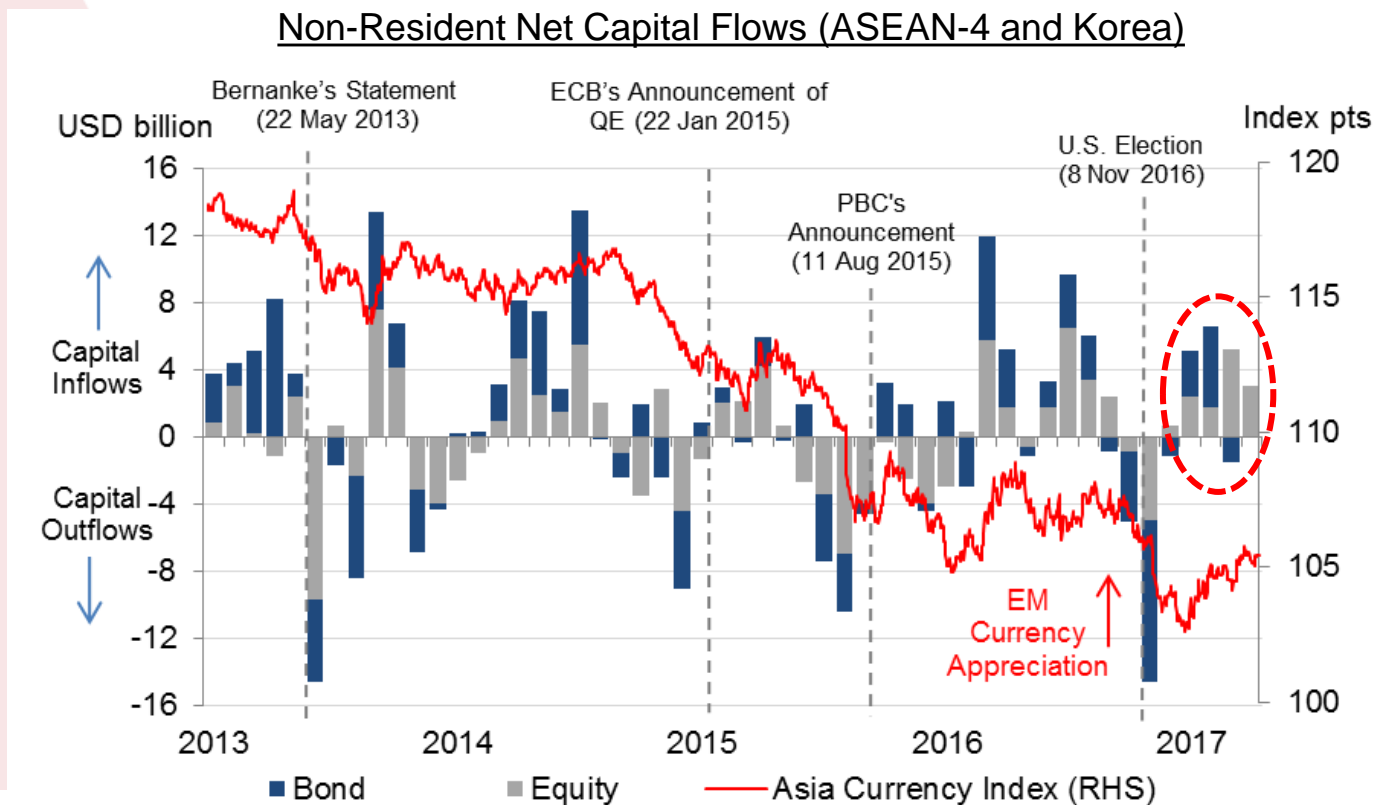
	1% Sustained Increase in Expected Default Frequency (EDF)	Mean Impact on Regional EMs (Cumulative, 12 months)
Banking Sector Shocks	<ul style="list-style-type: none"> U.S.' banking sector soundness China's banking sector soundness 	→ +0.11 pts (Impact on Regional Banks' EDF) → +0.25 pts (Impact on Regional Banks' EDF)
Corporate Sector Shocks	<ul style="list-style-type: none"> China's corporate sector soundness 	→ +0.11 pts (Impact on Regional Banks' EDF) → +0.12 pts (Impact on Regional Corporates' EDF)

Note: Expected Default Frequency (EDF) is a measure of the probability that a firm will default over a specified period of time (typically one year). "Default" is defined as failure to make scheduled principal or interest payments. According to the Moody's EDF model, a firm defaults when the market value of its assets (the value of the ongoing business) falls below its liabilities payable (the default point). The firm level EDFs are aggregated to form EDFs at the sectoral and country level

Source: AMRO

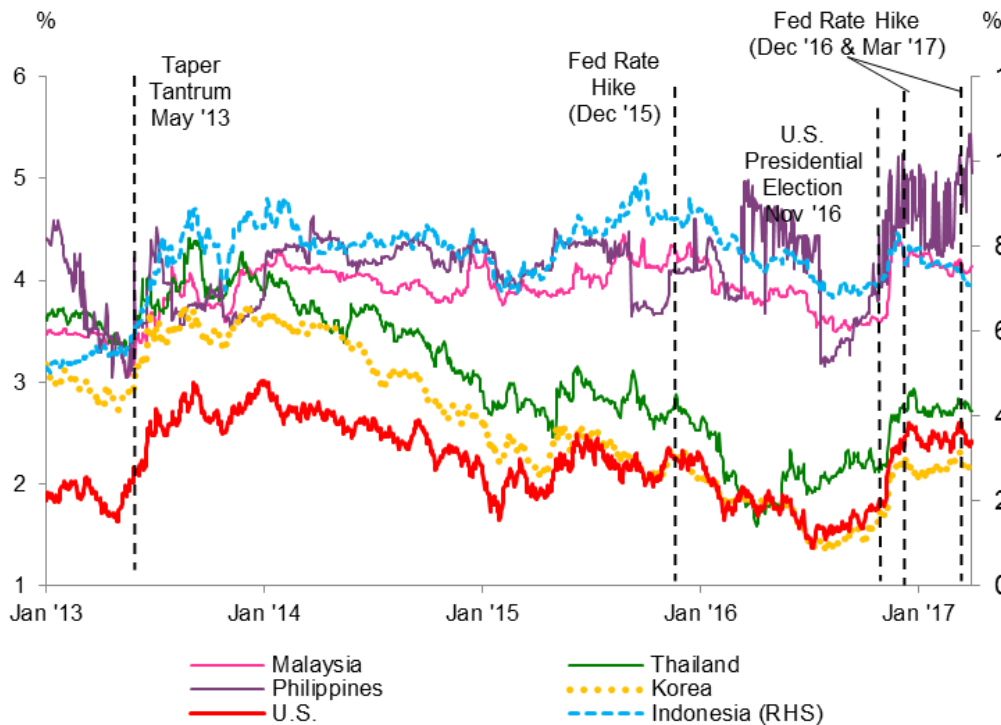
Risks Spotlight: Capital Flows Volatility and Reversal Risks

Financial markets have been largely stable, with the resumption of capital inflows, although risks remain tilted to the downside, mainly from global policy uncertainties

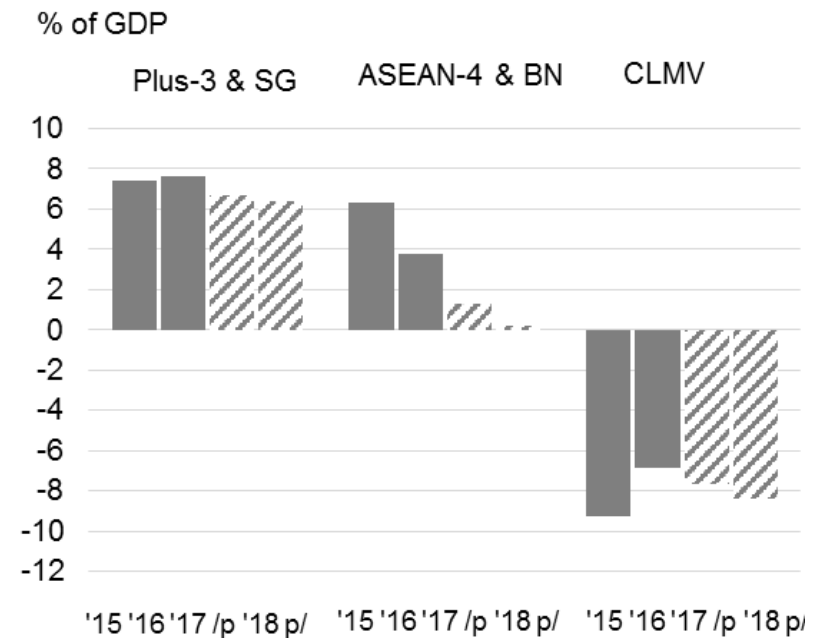


Potential escalation of global uncertainties could amplify the financial stability risks of regional economies with large external financing needs

Selected Regional 10Y Sovereign Bond Yields vs. 10Y U.S. Treasury Yields



Baseline Current Account Projections



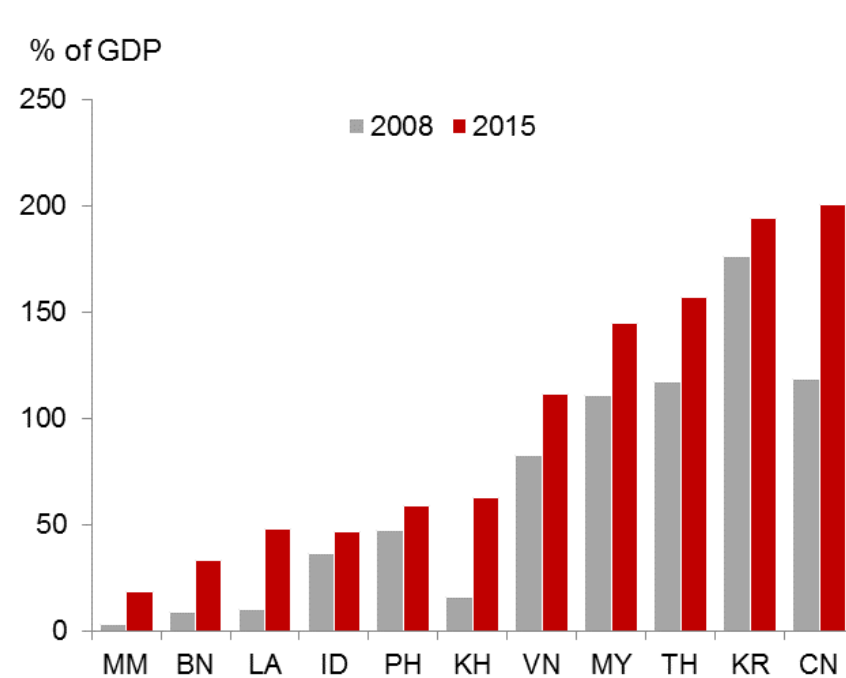
Risks Spotlight: Turning of the Credit Cycle

Rising cost of borrowing could pose vulnerabilities to some regional economies where private sector credit to GDP ratio has increased significantly since 2008

U.S.: Average Daily Fed Funds Effective Rate
(Implicit for December 2017)

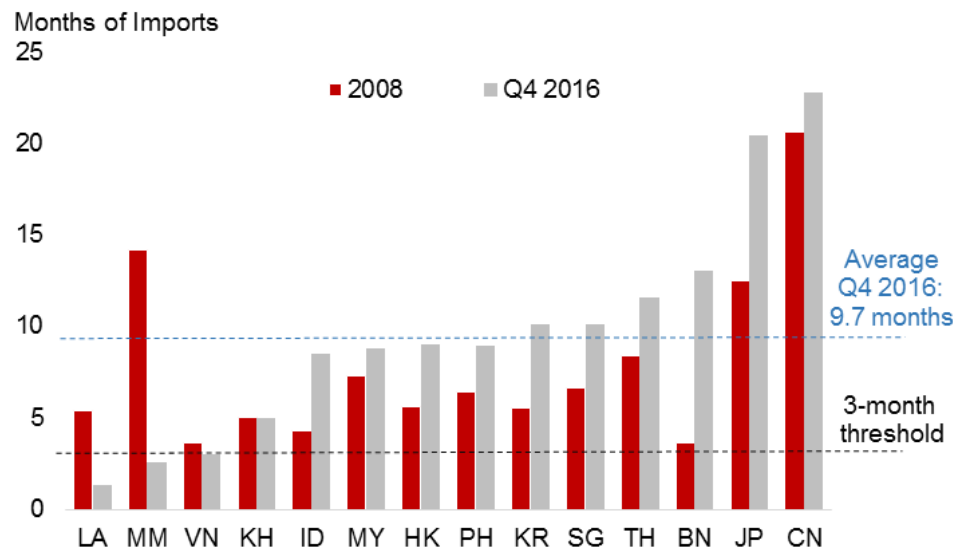


Private Sector Credit-to-GDP Ratio
(Selected Economies)

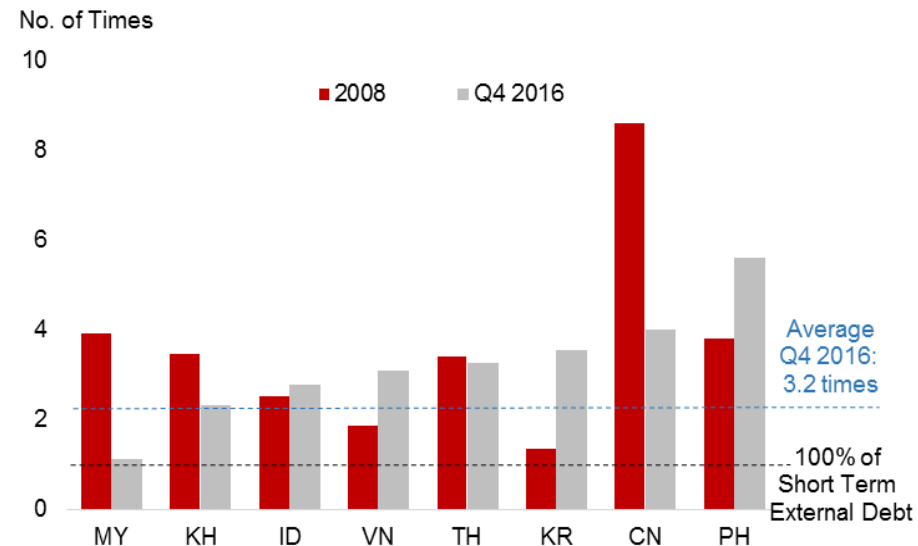


The region's reserve buffers remain adequate by conventional metrics, although policy room has generally narrowed/constrained across the region

FX Reserves (in Months of Imports)



FX Reserves / Short-Term External Debt Ratio (Selected Economies)



Note: Latest data refers to 2012 (for Vietnam), 2014 (for Cambodia), 2015 (for Brunei), Q3 2016 (for Myanmar). For Myanmar and Lao PDR, data reflect imports of both goods and services based on AMRO's calculations.

Note: Latest data refers to 2012 (for Cambodia), Q3 2016 (for China), and 2014 and 2016, respectively (for Vietnam). Some member economies have adopted the latest BPM6 (such as Malaysia), which includes local currency-denominated debt held by non-residents in their short term external debt data.

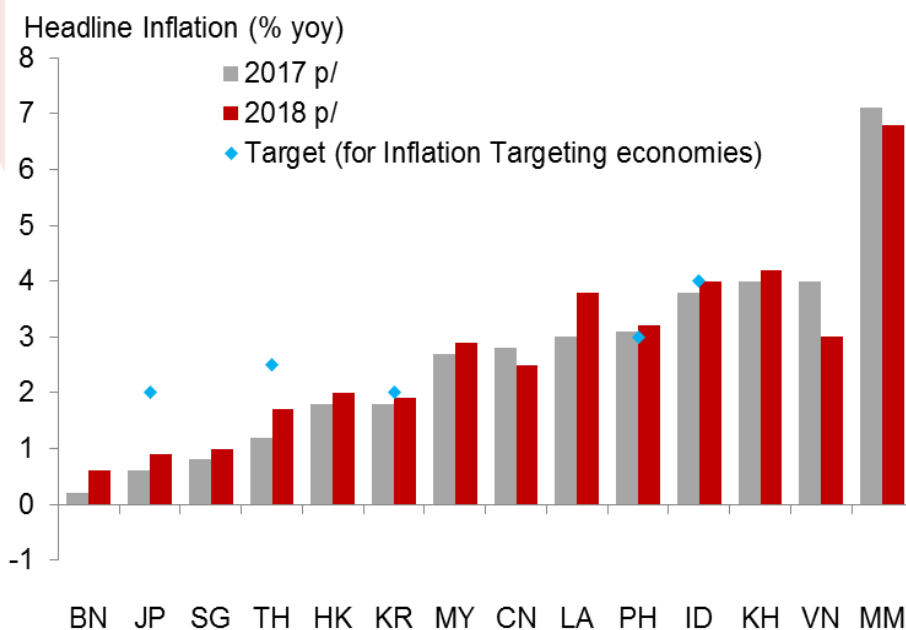
Suggested Policy Consideration

Some policymakers will face a sharper trade-off between growth and financial stability objectives, at a time when policy space has narrowed/constrained

Monetary Policy / Macroprudential Policy

- Tightening global monetary conditions in 2017 and rising inflation will constrain regional economies' use of monetary policy to support growth.

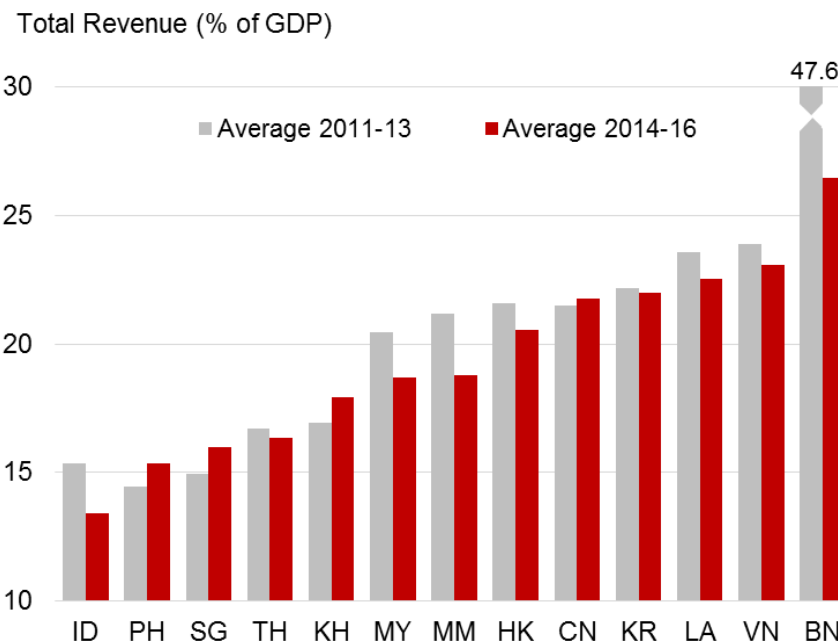
Headline Inflation



Fiscal Policy

- Fiscal conditions are expected to remain generally tight due to revenue shortfalls in some economies

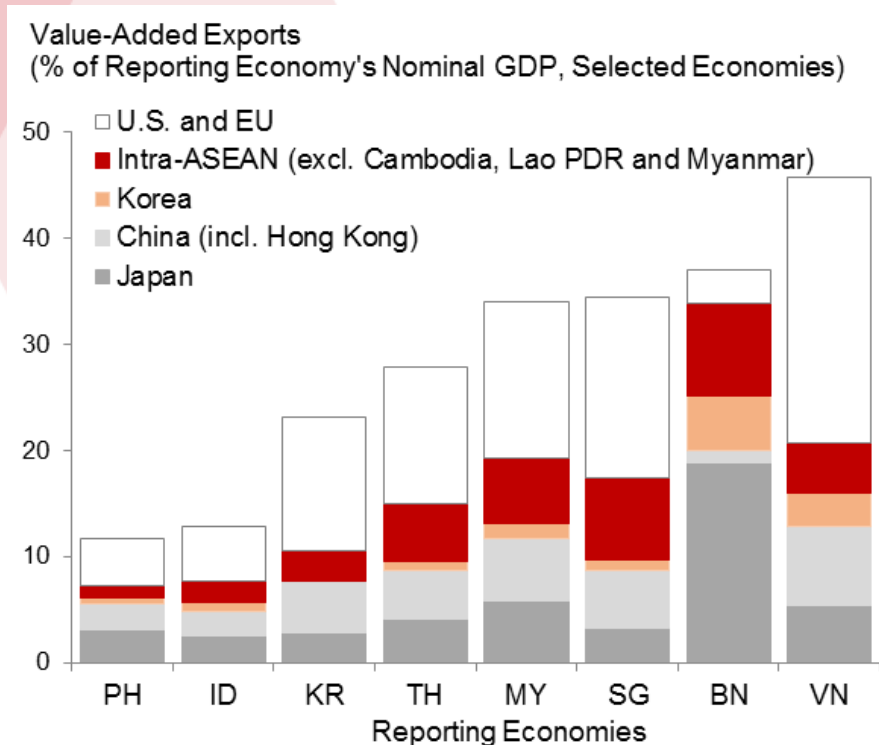
Central Government Fiscal Revenue Performance



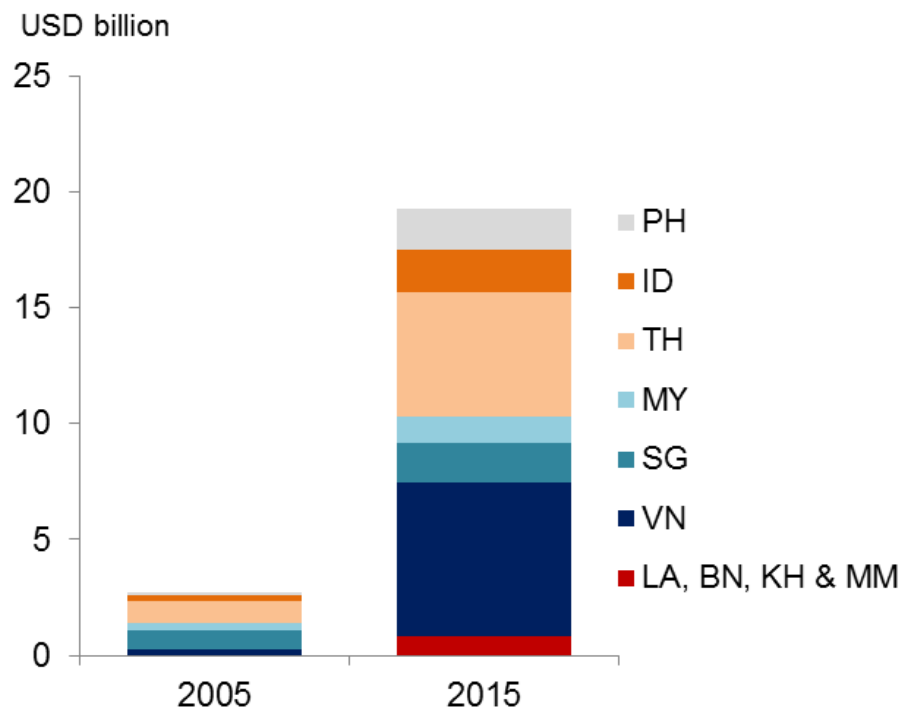
Structural Developments – Leveraging Regional Integration

On structural developments, the region has become an important source of final demand, benefiting from the growing regional integration, and rising middle class in China, which can cushion the impact of potential protectionist threats

Share of Exports Destined for Final Demand in the Region
(2015 Estimates)

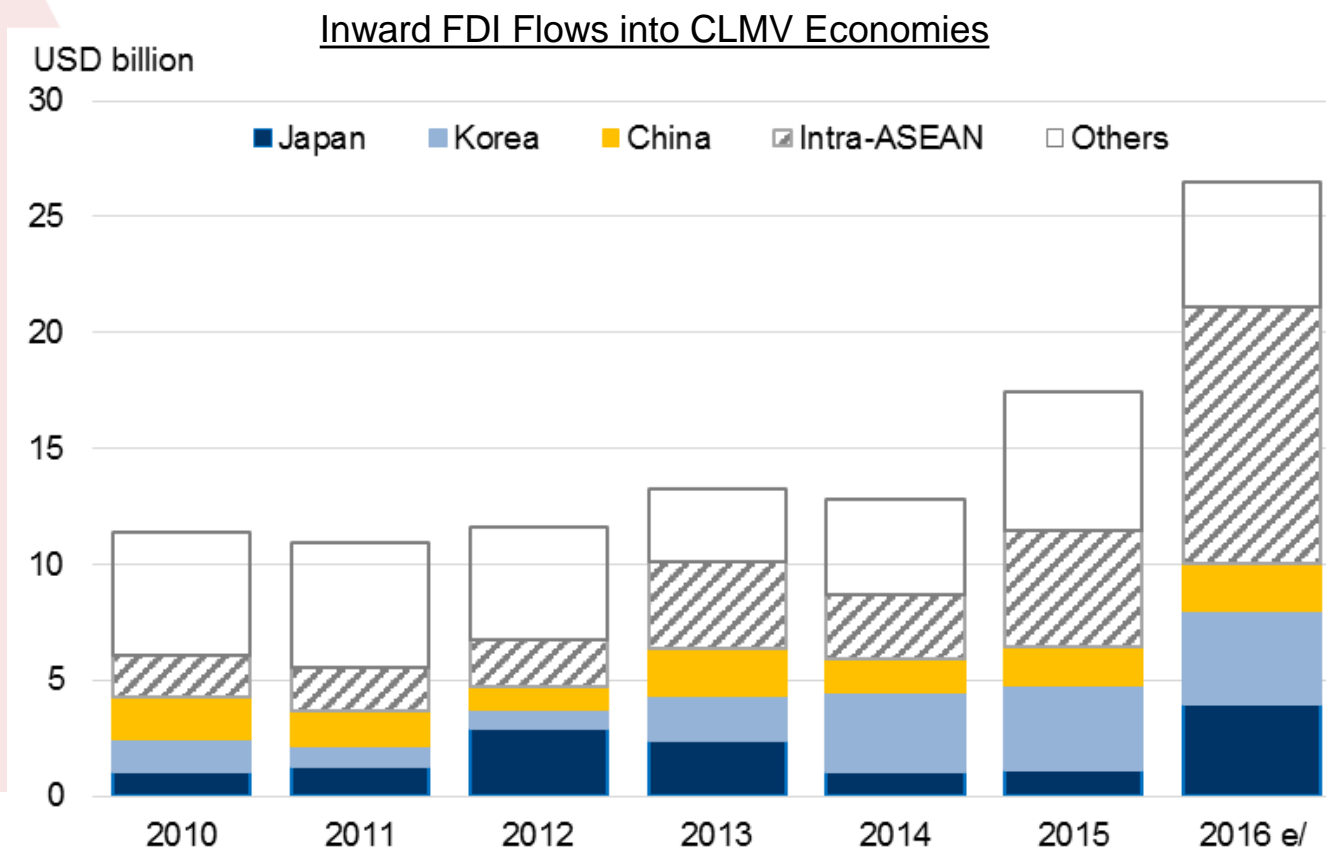


China's Imports of Consumption Goods from ASEAN



Structural Developments – Leveraging Regional Integration

Developing ASEAN economies have also benefited from the deepening of intra-regional investment, reflecting the recycling of domestic savings to productive investment in the region



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Thematic Chapter: ASEAN+3 Region 20 Years after the Asian Financial Crisis

2017 marks twenty years after the Asian Financial Crisis (AFC), a landmark event in the ASEAN+3 region.

20 Years post-AFC

Shaped the subsequent foundations and trajectory of economic growth and regional integration

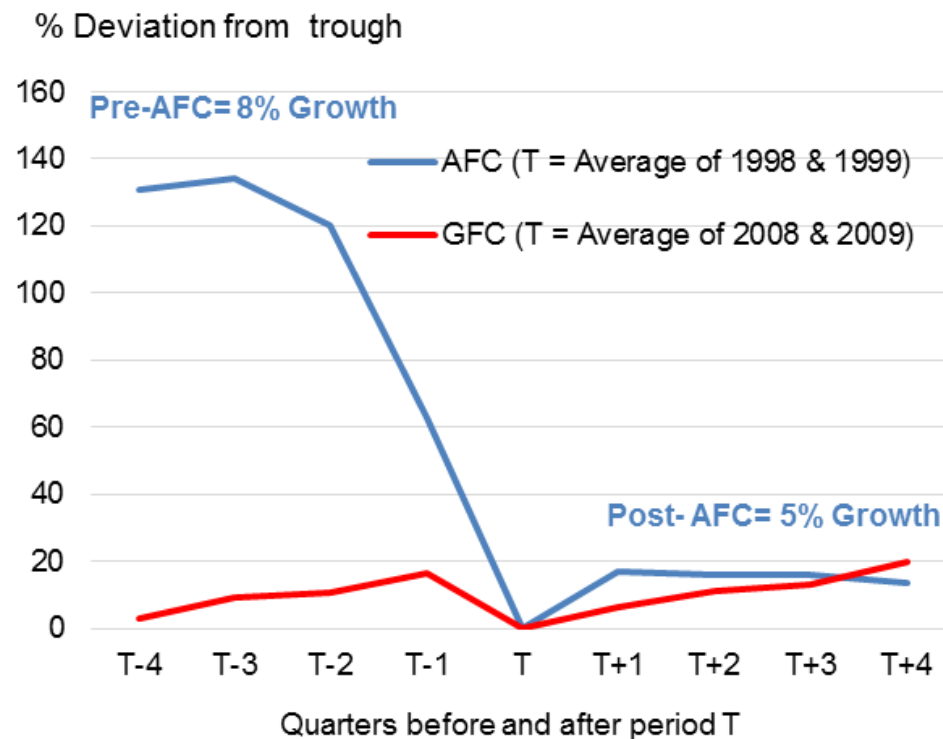
Shaped policymakers' perspectives on crisis management and resolution

- Highlighted the urgent need for regional financial cooperation
 - ➔ CMI (2000-09), CMIM (2010 onwards)
 - ➔ Establishment of AMRO as independent macroeconomic surveillance unit supporting the CMIM (2011)

1 First Decade Post-AFC: Rebuilding Foundations

- Period of economic consolidation after a sharp negative shock
- Painful policy adjustments in exchange rate regimes, corporate and financial sector reforms, fiscal consolidation, and reforms in prudential regulation
- Policy adjustments enabled the affected economies to rebuild the foundations for economic growth, with exports leading the recovery

Real GDP: ASEAN-4 and Korea



2 2007 – 2016: Rebalancing and Leveraging Regional Integration

- Openness to trade, FDI and capital flows post-AFC enabled the region (esp. CLMV economies) to reap the benefits from growing regional integration and the emergence of China
- Increased intra-regional financial flows have eased the ASEAN+3 region's rebalancing from export-led to domestic-led demand.

Plus-3 and ASEAN shares of FDI inflows to CLMV

Host	Source	2013	2014	2015
Cambodia	China	22.5	32.1	31.6
	Japan	3.0	4.9	3.1
	Korea	14.0	6.2	4.2
	ASEAN-4 & SG	19.1	11.2	14.9
Lao PDR	China	35.1	67.3	61.6
	Japan	0.4	0.2	7.0
	Korea	2.5	1.4	4.2
	ASEAN-4 & SG	4.7	11.8	7.6
Myanmar	China	30.2	7.5	1.9
	Japan	1.4	4.0	3.4
	Korea	0.0	1.2	1.3
	ASEAN-4 & SG	44.6	69.8	74.5
Vietnam	China	10.7	2.3	3.2
	Japan	26.6	10.5	8.1
	Korea	19.9	35.3	29.6
	ASEAN-4 & SG	23.0	16.4	17.6

Capital Inflows Post-GFC

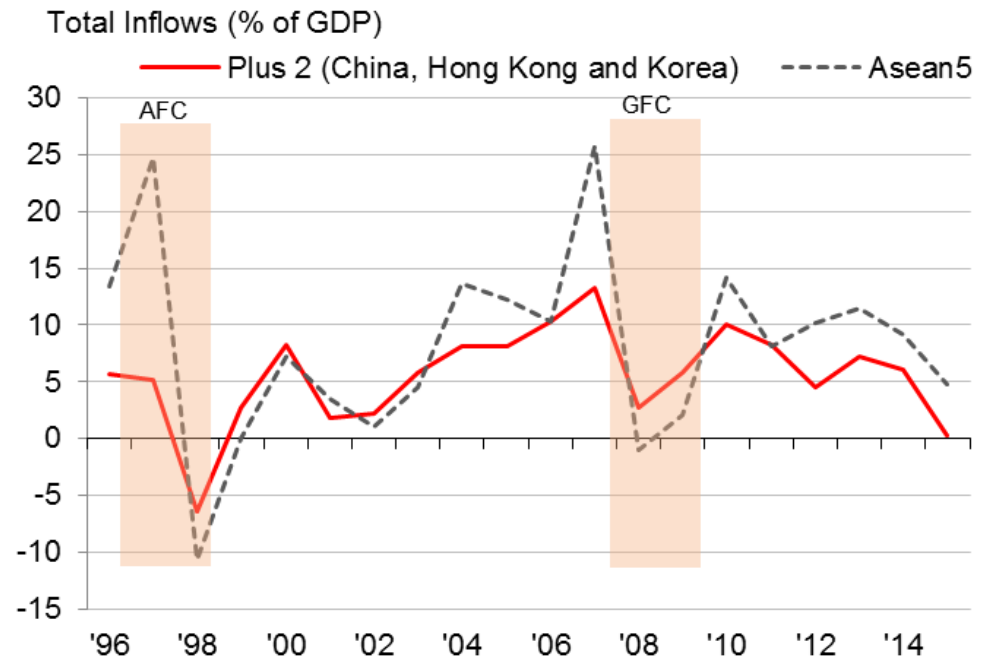
Eased rebalancing towards domestic demand, but posed risks to financial stability

- ➔ Financial vulnerabilities: credit growth, asset price inflation, leverage
- ➔ Amplifies pro-cyclicality of financial cycle and volatility, especially with lack of depth in financial markets in EMs

Policy response

- Pragmatic and robust use of policy tools, including macroprudential measures
 - ➔ Macroprudential policies
 - ➔ Capital flow management measures
 - ➔ FX interventions + greater flexibility in exchange rates

Capital Inflows (Net)
(ASEAN-4, Singapore, China and Korea)



Lessons from the AFC

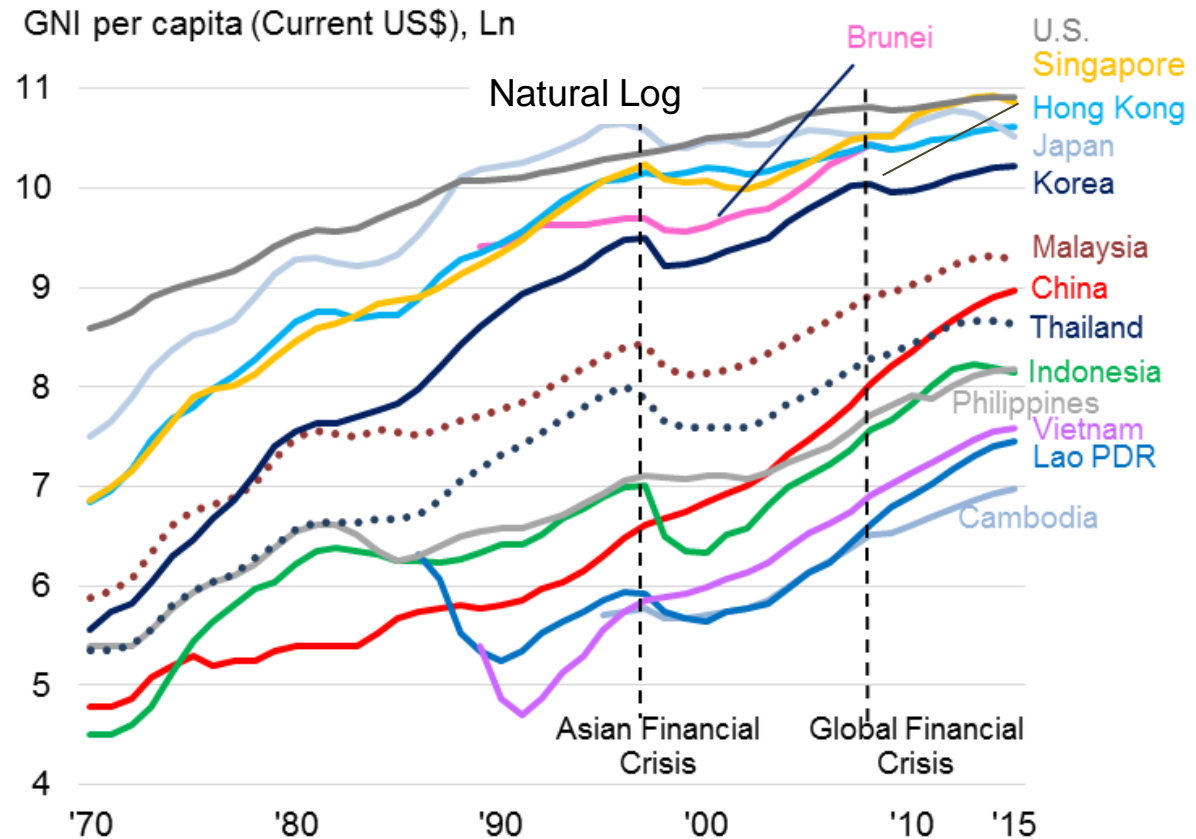
In the current uncertain global environment, the AFC continues to offer valuable lessons to policymakers

- I Focus on risks arising from financial markets and capital outflows (inter-connectedness and contagion risks)
- II Flexible and responsive policy framework, and strengthening of buffers
- III Greater financial cooperation within the region to deal with external shocks.

3 Looking Ahead: Challenges

- Short term macroeconomic & risks management
- Strengthening regional financial safety net
- Accelerating structural reforms (e.g. raising TFP to avoid growth from reaching stalling speeds)

Income Convergence and Catch-up

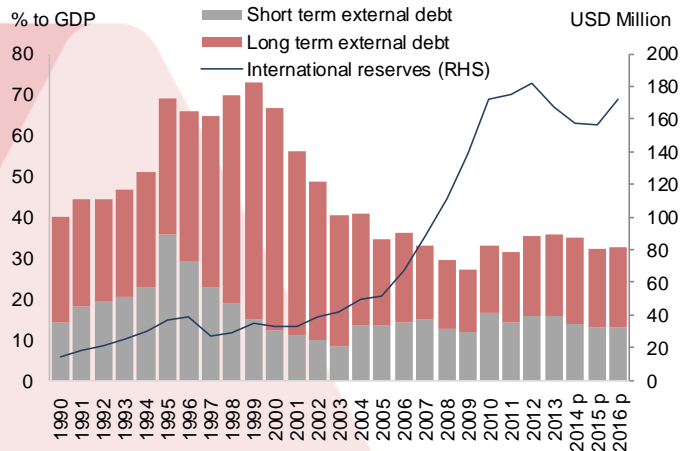


Macroeconomic and financial stability has been strengthened.

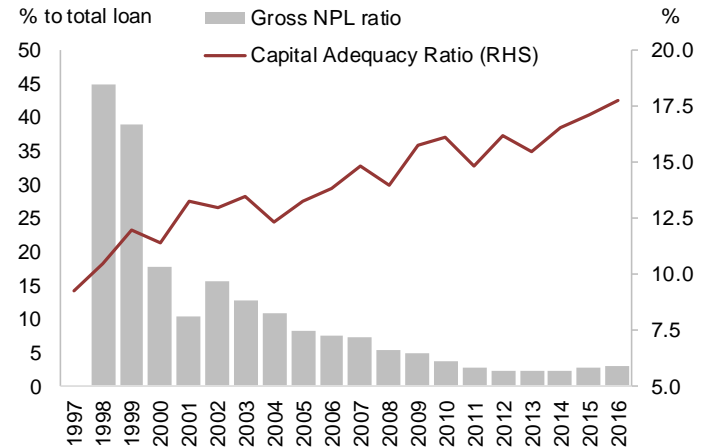
Policy	Pre-AFC Period	Post-AFC Period
Monetary Policy	Pegged exchange rate regime	<ul style="list-style-type: none"> • Inflation Targeting with a managed-float exchange rate regime • Capital Account Liberalization Plan
Fiscal Policy		<ul style="list-style-type: none"> • Fiscal Sustainability Framework • Tax Reforms
Financial Regulations	<ul style="list-style-type: none"> • Commercial Banking Act 1962 • Finance Companies and Credit Fonciers Act 1962 • Compliance-based supervision 	<ul style="list-style-type: none"> • Financial Institution Act 2008 • Risk-based supervision (Basel standards, consolidated supervision for financial conglomerate, IAS 39 accounting standard) • Macroprudential measures on some categories of consumer loans • Regulatory reforms for non-bank financial institutions • Financial Sector Master Plan Phase I, II and III
Financial infrastructure		<ul style="list-style-type: none"> • Credit Bureau • Deposit Protection Agency • National e-Payment system

From 'Dual Crisis' to 'Multiple Stability'

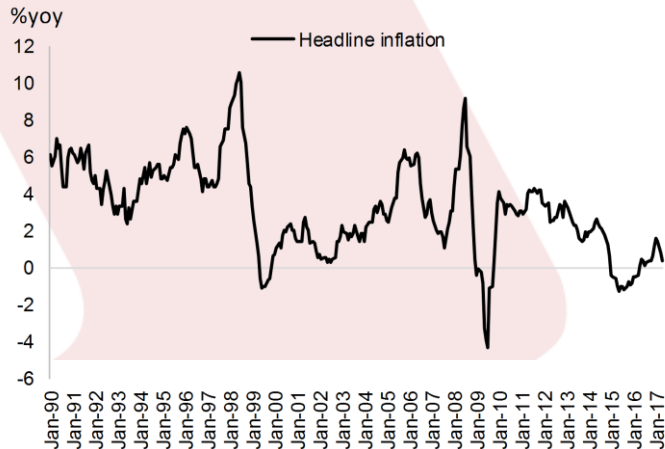
External Stability



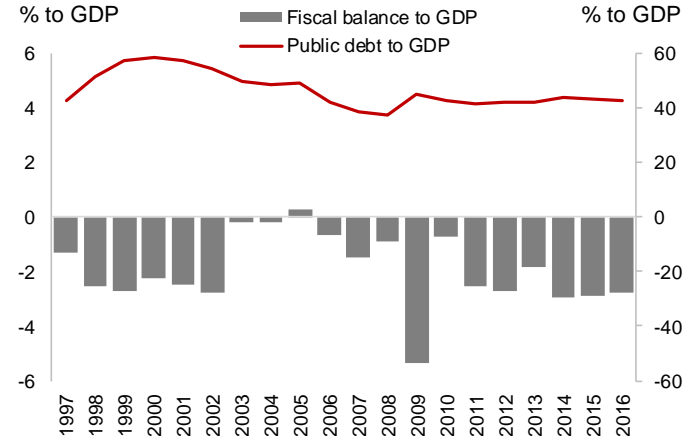
Financial Stability



Price Stability



Fiscal Stability

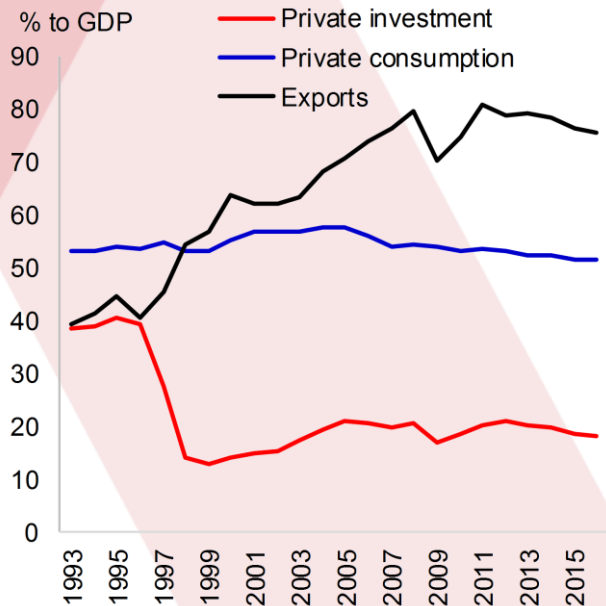


Note: Capital Adequacy Ratio consists of locally incorporated commercial banks only.

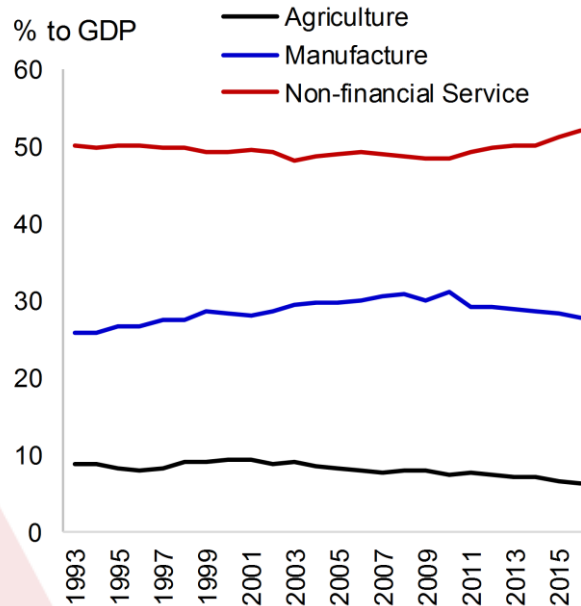
Source: Bank of Thailand, AMRO staff calculations

Structural change in the economy and financial landscape is underway.

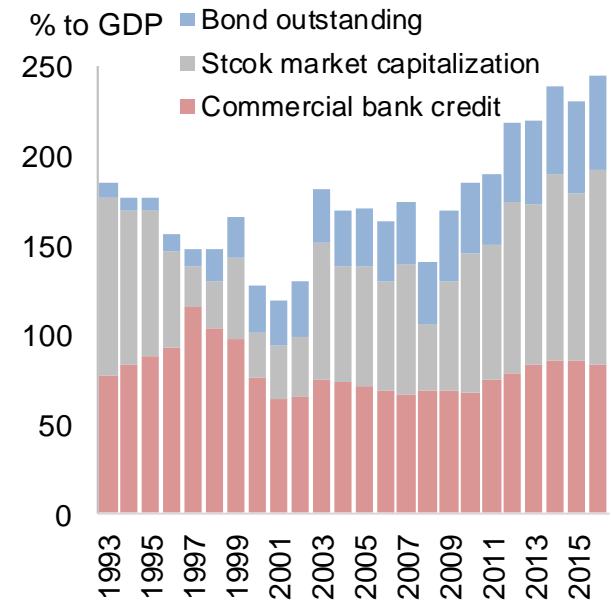
Demand structure



Production structure



Financial System Structure



Recap: Key Messages

1. Regional growth to be sustained about 5% in 2017-18.
2. Near term outlook for the region turned somewhat brighter, although risks are tilted to the downside, from tightening global financial conditions, trade protectionism and global policy uncertainties.
3. In China, growth is expected to moderate in 2017-18, projected at 6.5% and 6.3%, respectively. Private investment activities have notably picked up recently, alongside improvement in corporate profits.
4. Some policymakers will face a sharper trade-off between growth and financial stability objectives, at a time when policy space has narrowed/constrained.
5. AFC shaped policymakers' perspectives on crisis management and resolution – AMRO and CMIM established. Post-AFC, policy attention shifted to capital flows and contagion risks – the need for flexible policy framework.
6. Enhanced financial cooperation in ASEAN+3 will improve the resilience against shocks, allowing the region to sustain relatively strong growth. ³⁰

Thank You

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