Foreword

Building on our achievements so far, AMRO has continued to enhance its outreach and publication of our surveillance work and research activities. Following the inaugural publication of *AREO 2017* in May 2017 and the publication of the Annual Country Consultation Reports of several countries during that year, we have continued to publish country reports in 2018 with the support of AMRO's members. AMRO staff have also increased their thematic and other research activities with the aim of providing relevant and timely analysis to our stakeholders, as well as to inform the public. It is encouraging to note that the publication of the Monthly Updates of the AREO and staff blogs on selected topics on AMRO's website has been well-received.

We are continuing to improve our analytical frameworks and toolkits, to fulfill our mandate of contributing to the financial stability of the region through conducting regional economic surveillance and supporting the implementation of the Chiang Mai Initiative Multilateralization Agreement. In this issue, *AREO 2019*, we introduce the property market valuation cycle, as well as estimate the Taylor Rule model for selected ASEAN+3 regional economies, building upon AMRO's surveillance framework, which has been strengthened with the development and implementation of the Economic Review and Policy Dialogue Matrix framework. These new analytical tools enhance our assessment of risks to respective member economies, while enabling richer cross-country analyses. More importantly, they aid staff's assessment of the current policy stance and inform policy recommendations to member authorities.

Regional economic growth should remain resilient, although fundamental global growth drivers are slowing relative to 2018, and are expected to deliver less of a boost to the region in 2019–2020. With dissipating tailwinds from global trade, the drag from weaker external demand on regional growth could become more evident. However, recent monetary pivots in the advanced economies could mitigate this risk. Global markets experienced bouts of sharp volatility last year, reflecting the uncertainties in international trade, but monetary conditions have eased recently in the wake of the more dovish tone adopted by the U.S. Federal Reserve and the European Central Bank. Regional policymakers need to stand ready to mitigate the downside risks by using the available policy tools flexibly, and calibrating them in accordance with country-specific conditions and circumstances. Encouragingly, while the near-term prospects for the region are expected to be a shade softer, the longer-term economic fundamentals remain intact.

This year's thematic study is on "Building Capacity and Connectivity for the New Economy." It follows from the thematic chapter in *AREO 2017*, which assesses the economic consolidation and rebalancing in the region after the Asian Financial Crisis (AFC), and the one in *AREO 2018*, which focuses on the drivers of growth and the strategy that the region uses to maintain resilience and sustain growth. The region as a whole has prospered in the past two decades, with the "manufacturing for export" strategy as the main pillar in most countries. This AREO issue explores how ASEAN+3 members could embrace the New Economy and embark on their next phase of economic development by enhancing capacity and connectivity, the three major challenges in these areas and how to address them.

While the move up the technological frontier has been, and will continue to be, uneven, the transformation to services is inevitable, and will require a rethink of what capacity means and what connectivity is needed. The investments needed to generate and sustain growth will include: new technology; human capital to work with the new technology; and networks and connectivity for new value chains that are becoming more complex and international. At the same time, developing economies face three major challenges to building the infrastructure: funding gap arising from low saving rates; foreign exchange constraints from the need to build buffers against capital flow volatility; and factors gap reflecting the need to improve governance, human capital and connectivity. Finally we argue that the solution to many of the challenges can be met from within the region by leveraging on the rich and diverse resources of the region, and by enhancing capacity and connectivity through greater regional integration.

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