

Monthly Update of the ASEAN+3 Regional Economic Outlook (AREO)

ASEAN+3 Macroeconomic Research Office (AMRO)

Singapore

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This Monthly Update of the AREO was prepared by the Regional Surveillance team and approved by Dr Khor Hoe Ee (Chief Economist).

Unless otherwise indicated, the analysis in this report is based on information available up to 6 August 2018. For the sake of brevity, “Hong Kong, China” will be referred to as “Hong Kong” in the text and figures.

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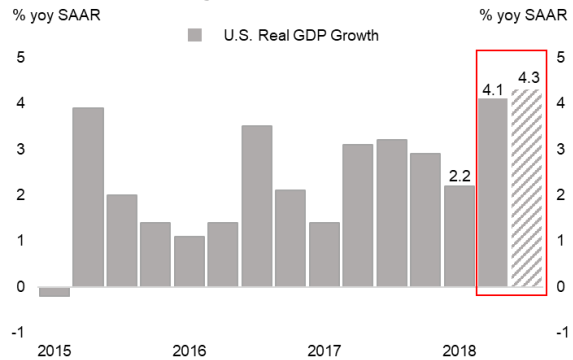
Economic Developments in the U.S. & Europe

The U.S. economy grew strongly in Q2 2018, with generally favorable fundamentals supporting continued expansion. Preliminary growth data suggest that the U.S. economy grew by 4.1 percent (qoq SAAR), the fastest pace in nearly four years (Figure 1). Growth was driven by sustained consumer spending, higher government expenditures and some frontloading of exports.¹ The growth outlook for Q3 is expected to remain robust, maintaining the trajectory of slightly above-trend growth. This is expected to support wage increases and underlying prices, while further tightening the labor market. Core inflation has been trending upwards since early this year, reaching 2.4 percent in July 2018, while the latest jobs report in July 2018 show that unemployment rate fell to 3.9 percent, with steady increase in wages (Figure 2).

Economic growth slowed further in the Eurozone while the U.K. saw a slight rebound in Q2 2018. The Eurozone reported a slower annualized growth of 2.1 percent in Q2 2018, as trade uncertainties weighed on business sentiment. Going into July and Q3, economic sentiment appears to have improved (Figure 3), suggesting that economic activities could potentially rebound in the months ahead.² In the U.K., after temporary setbacks due to weather-related disruptions in early 2018, recent data point to some stabilization of economic activities in Q2, with preliminary business surveys suggesting similar pace of growth in Q3 2018.

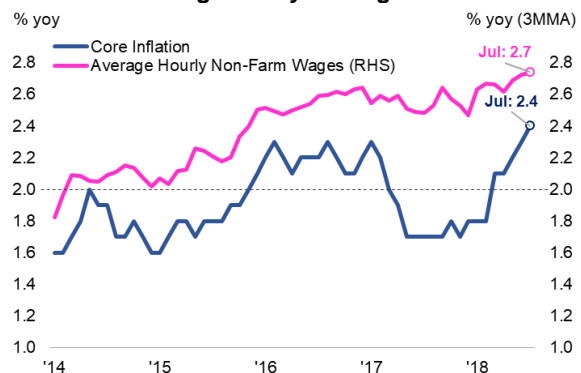
Turning to central bank policy, both the Fed and the ECB kept policy unchanged (in July 2018), while the BOE delivered a 25 bps rate hike (in August) as anticipated by markets.

Figure 1
U.S. economic growth picked up in Q2 2018...



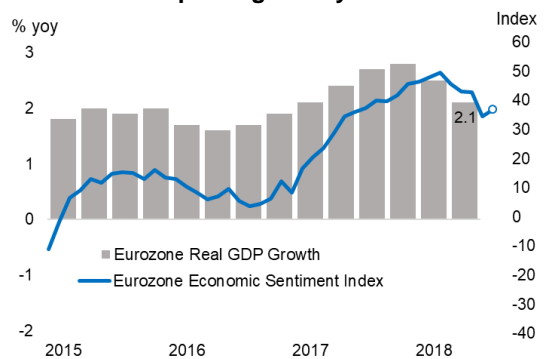
Notes: Preliminary estimates for Q2 2018, with revised Q1 2018 estimates for Q1 2018 (+0.2 pts). Q3 2018 figure refers to the Atlanta Fed's GDPNow (latest estimate as of 9 Aug 2018).
Source: BEA

Figure 2
...while wages and underlying inflation are gradually firming



Source: BEA

Figure 3
Eurozone economic sentiment appears to be improving in July 2018



Notes: The Eurozone economic sentiment index refers to the Sentix Economic Index on current situation. A reading above zero indicates optimism; below indicates pessimism.
Source: EuroStats, Haver

¹ Farmers rushed the shipments of soybeans to China, ahead of threat of import curbs by China following the planned implementation of tariffs by the U.S. on USD50 billion worth of Chinese imports on 6 July 2018.

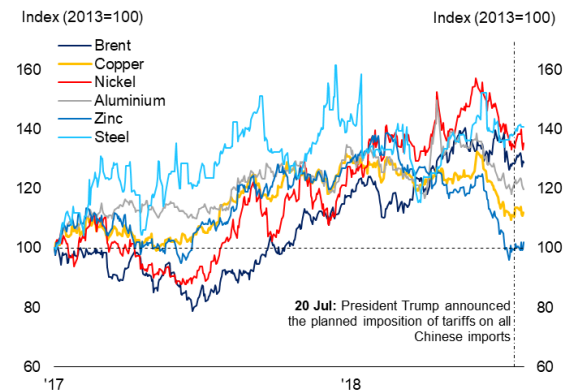
² The positive outcome following the meeting between U.S. President Trump and European Commission President Jean-Claude Juncker in July is also reassuring, helping to support confidence in the Eurozone economy.

In commodity markets, key base metal prices continue to face headwinds from the ongoing global trade tensions, while crude oil prices dropped on renewed worries about oversupply. Escalating global trade tensions are depressing key base metal prices, after U.S. President Trump threatens to impose tariffs on all Chinese imports on 20 July. Key base metal prices notably copper (widely used in consumer goods, e.g. air-conditioning and refrigerators) and nickel (used in car batteries) declined further, as these are among the goods targeted by tariffs (Figure 4). Brent spot dropped to the lowest level in six weeks, after an unexpected increase in U.S. inventories of crude in early August. To some extent, lower prices reflect activities by hedge funds/money managers slashing their net long positions in U.S. crude, reducing their bets that oil prices would rise.

Regional Economic Developments

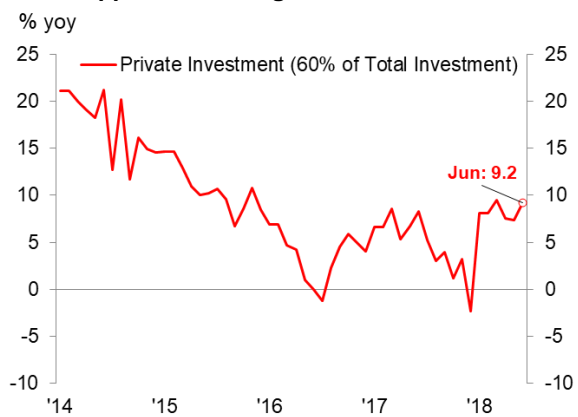
China's growth remains robust in H1 2018, notwithstanding the external uncertainties from trade tensions, and ongoing financial deleveraging domestically. The Chinese economy posted a moderate growth of 6.7 percent in Q2 2018. The expansion in Q2 was underpinned by strong private consumption as well as a rebound in private investment (Figure 5). Looking ahead in Q3, PMI indicators in July points to softer factory output, with lower new export orders (Figure 6). On the financial side, domestic liquidity conditions have tightened, reflecting the deleveraging process in the financial markets.³ The equity and FX markets continue to be weighed down by external uncertainties, with the benchmark Shanghai Composite Index falling by 5 percent from June 15 to Aug 6, 2018 while the RMB depreciating by 6 percent during the same period⁴. This development was largely in line with the trend observed in other regional emerging markets.

Figure 4
Base metal prices continue to be under downward pressure, reflecting the escalation of trade tensions towards end-July 2018



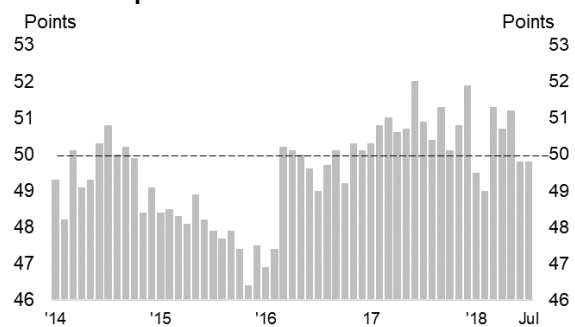
Note: Data as of 6 Aug 2018.
Source: Commodity Exchanges

Figure 5
A rebound in China's private investment is supportive of the growth outlook ahead



Source: China National Bureau of Statistics

Figure 6
China's new export orders dipped below 50-point threshold since June 2018



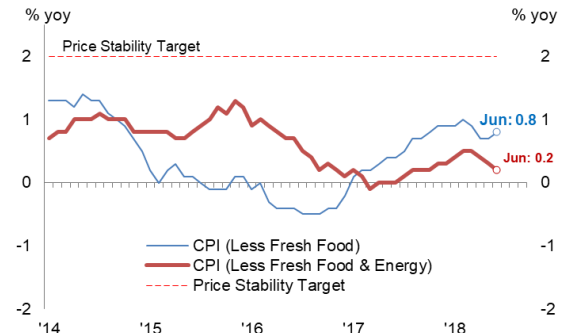
Source: China National Bureau of Statistics

³ Earlier in June 2018, the authorities lowered the reserves requirement of banks to inject liquidity into the financial markets, allowing interest rates to remain relatively stable. Amid increasing external uncertainties, the authorities has recently pledged to keep the economy on a stable track, supported by proactive fiscal policy and prudent monetary policy in the second half of the year (see Annex 3).

⁴ The FX rates refer to the the RMB/USD spot. Against a basket of currencies, the RMB has depreciated by 5 percent during the same period.

In Japan, the economy grew strongly in Q2 2018, although underlying price pressures continued to be relatively subdued. After a contraction in Q1, real GDP grew by 1.9 percent (qoq SAAR) in Q2 2018, helped by a strong rebound in private consumption and business spending. Going into July, growth momentum appears to have eased, judging from the reduced pace at which new orders increased. Inflation continued to show sluggish developments in June 2018, notwithstanding the gradual tightening of the labor market (Figure 7).

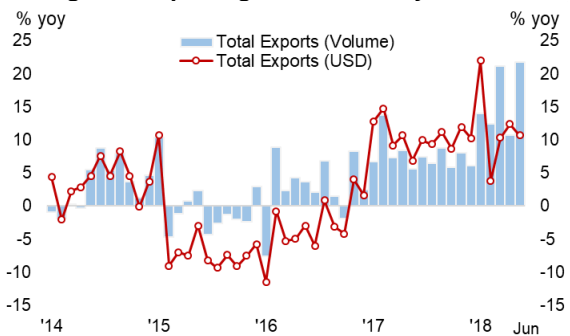
Figure 7 Underlying inflationary pressures continued to be relatively subdued



Source: Ministry of Internal Affairs and Communications

In other regional economies, monthly manufacturing PMI readings suggest slight softening of economic activities in July, potentially signaling a moderate growth outlook in Q3 2018. Despite the uncertainties in global trade, so far, it has not affected the region materially. Regional exports in Q2 2018 grew moderately, after a 13 percent surge in Q1. Volume wise, the expansion remains relatively robust (Figure 8 and Annex 2).

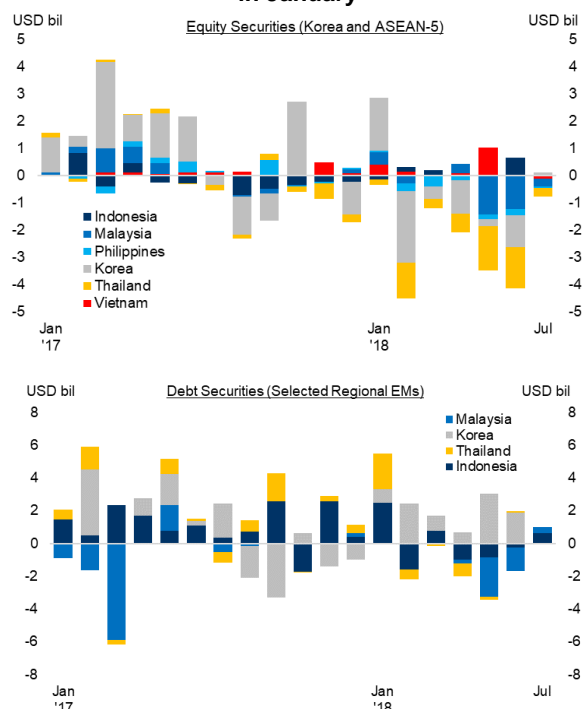
Figure 8 Regional exports grew moderately in Q2 2018



Note: Excludes Brunei, Cambodia, Lao PDR and Myanmar.
Source: Haver, AMRO staff estimates

Foreign capital flows in regional emerging markets have become more volatile relative to 2017, reflecting the frequent shifts in investor risk appetite. Figure 9 shows that regional stock markets continued to record net outflows of foreign funds in July 2018. Foreign capital flows in the bond market noticeably slowed in June 2018, after peaking in January.

Figure 9 Foreign equity capital outflows persist in July, while bond flows generally slowed, after peaking in January



Note: Data for July refer to Indonesia and Malaysia only.
Source: National Authorities

The uncertainties over global trade outlook and the renewed USD strength will continue to pose strong headwinds, with downward pressure on asset prices and capital flows. While policy settings in the region continues to be supportive of growth, the near term risks continued to be characterized by potential upside surprises in U.S. wage growth/inflation triggering a faster-than-expected Fed rate hike, and a sharp re-pricing of U.S. Treasury yields. The downside risks to emerging markets' asset prices and capital flows could interact with further escalation of global trade tensions, which can be mutually reinforcing.

Annex 1: GDP Growth for Selected ASEAN+3 Economies

Economy	Annual GDP Growth, % y-o-y							
	2016	2017	1Q'17	2Q'17	3Q'17	4Q'17	1Q'18	2Q'18
China	6.7	6.9	6.9	6.9	6.8	6.8	6.8	6.7
Hong Kong	2.0	3.8	4.4	3.9	3.6	3.4	4.7	-
Japan ⁽¹⁾	1.2	1.6	1.5	1.6	2.0	2.0	1.0	1.0
Korea	2.8	3.0	2.9	2.8	3.8	2.8	2.8	2.9
Brunei	-2.5	1.3	-1.3	0.2	1.3	5.2	2.5	-
Indonesia	5.0	5.1	5.0	5.0	5.1	5.2	5.1	5.3
Malaysia	4.2	5.9	5.6	5.8	6.2	5.9	5.4	-
Philippines	6.9	6.7	6.5	6.6	7.2	6.5	6.6	6.0
Singapore	2.0	3.6	2.5	2.8	5.5	3.6	4.3	3.8
Thailand	3.3	3.9	3.4	3.9	4.3	4.0	4.8	-
Vietnam	6.2	6.8	5.2	6.3	7.5	7.7	7.5	6.8

Notes:

⁽¹⁾ For Japan, annual figures are based on the fiscal year ending March.

Table shows economies with latest GDP data releases since the last edition of the Monthly Update of the AREO. Data released as of 10 August 2018.

Source: National Authorities

Annex 2: Global Manufacturing PMI Heatmap

Economies	2015				2016				2017												2018							Change from Prev Month	
	Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul		
Global																													↓ -0.3
Developed Markets																													↓ -0.3
U.S.																													↓ -0.1
U.K.																													↓ -0.3
Eurozone																													↑ 0.2
Austria																													↑ 0.2
France																													↑ 0.8
Germany																													↑ 1.0
Greece																													↔ 0.0
Ireland																													↓ -0.3
Italy																													↓ -1.8
Netherlands																													↓ -2.1
Spain																													↓ -0.5
Emerging Markets																													↓ -0.2
Brazil																													↑ 0.7
India																													↓ -0.8
Russia																													↓ -1.4
South Africa*																													↑ 0.9
China																													↓ -0.2
Hong Kong*																													↑ 0.5
Japan																													↓ -0.7
Korea																													↓ -1.5
ASEAN																													↓ -0.6
Indonesia																													↑ 0.2
Malaysia																													↑ 0.2
Philippines																													↓ -2.0
Singapore*																													↓ -3.0
Thailand																													↓ -0.1
Myanmar																													↓ -2.1
Vietnam																													↓ -0.8

Note: These seasonally adjusted PMI readings are coded by colors:

- Darker shades of red in the reading denote readings further below (< 45) the diffusion level of 50; conversely, greener shades in the readings denote readings further above (> 55) the diffusion level of 50.
- The trend lines shown in the right-most column represent the PMI readings since January 2015, the red dots denote minimum and maximum points in that period.
- Global PMI is as aggregated by JP Morgan. China's PMI refers to Caixin/ Markit PMI.
- (*) denotes whole economy PMI

Source: Markit, JP Morgan

Annex 3: Major Policy Developments (7 July – 6 August 2018)

<p>China</p>	<p>[31 July 2018] China will keep its economy on a stable and healthy development track with proactive fiscal policies and prudent monetary policies in the second half, according to a meeting of the Political Bureau of the Communist Party of China (CPC) Central Committee. (Link to Announcement)</p> <p>[3 August 2018] The People's Bank of China decided to adjust the foreign exchange risk reserve ratio of forward sales from 0 to 20 percent amid signs of pro-cyclical fluctuations in the foreign exchange market. This move will help prevent macro-financial risks, promote the stable operation of financial institutions, and strengthen macro-prudential management. (Link to Press Release)</p>
<p>Japan</p>	<p>[31 July 2018] The Policy Board of the Bank of Japan decided to strengthen its commitment to achieving the price stability target by introducing forward guidance for policy rates, and to enhance the sustainability of "Quantitative and Qualitative Monetary Easing (QQE) with Yield Curve Control." (Link to Monetary Policy Statement)</p>
<p>Korea</p>	<p>[13 July 2018] The Monetary Policy Board of the Bank of Korea decided to leave the Base Rate unchanged at 1.50 percent for the intermeeting period. (Link to Press Release)</p> <p>[18 July 2018] The Ministry of Economy and Finance announced the Economic Policy Direction for H2 2018, focusing on creating jobs and strengthening social safety nets, accelerating 'growth through innovation', sharing the outcomes of growth, and maintaining expansionary fiscal management. (Link to Press Release)</p>
<p>Indonesia</p>	<p>[19 July 2018] The Bank Indonesia (BI) Board of Governors agreed to hold the BI 7-day Reverse Repo Rate at 5.25 percent, while maintaining the Deposit Facility and Lending Facility rates at 4.50 percent and 6.00 percent respectively. (Link to Press Release)</p>
<p>Malaysia</p>	<p>[11 July 2018] The Monetary Policy Committee of Bank Negara Malaysia decided to maintain the Overnight Policy Rate at 3.25 percent. (Link to Press Release)</p>