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

12 June 2017, Bangkok, Thailand
Introduction: About AMRO

**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
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I. ASEAN+3 Macroeconomic Prospects and Challenges

II. Thematic Chapter: ASEAN+3 Region 20 Years after the Asian Financial Crisis
Regional Growth Outlook

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

<table>
<thead>
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<th>‘16</th>
<th>‘17 p/</th>
<th>‘18 p/</th>
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<tr>
<td>Japan (FY)</td>
<td>1.4</td>
<td>1.3</td>
<td>1.1</td>
</tr>
<tr>
<td>Korea</td>
<td>2.8</td>
<td>2.5</td>
<td>2.6</td>
</tr>
<tr>
<td>ASEAN-4 &amp; VN</td>
<td>5.0</td>
<td>5.1</td>
<td>5.2</td>
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<td>BCLM</td>
<td>5.6</td>
<td>6.5</td>
<td>6.8</td>
</tr>
<tr>
<td>HK &amp; SG</td>
<td>2.0</td>
<td>2.1</td>
<td>2.3</td>
</tr>
<tr>
<td>ASEAN+3</td>
<td>5.3</td>
<td>5.2</td>
<td>5.1</td>
</tr>
</tbody>
</table>

p/ Projections
Source: National authorities, AMRO
Regional Growth Outlook

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

<table>
<thead>
<tr>
<th>Country</th>
<th>‘16</th>
<th>‘17 p/</th>
<th>‘18 p/</th>
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</thead>
<tbody>
<tr>
<td>Brunei</td>
<td>-2.1</td>
<td>1.6</td>
<td>2.9</td>
</tr>
<tr>
<td>Cambodia</td>
<td>6.9</td>
<td>6.8</td>
<td>6.8</td>
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<tr>
<td>Indonesia</td>
<td>5.0</td>
<td>5.1</td>
<td>5.2</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>6.9</td>
<td>7.0</td>
<td>7.0</td>
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<tr>
<td>Malaysia</td>
<td>4.2</td>
<td>4.5</td>
<td>4.6</td>
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<tr>
<td>Myanmar</td>
<td>6.0</td>
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<td>7.2</td>
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<tr>
<td>Philippines</td>
<td>6.8</td>
<td>6.8</td>
<td>7.0</td>
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<tr>
<td>Singapore</td>
<td>2.0</td>
<td>2.0</td>
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<tr>
<td>Thailand</td>
<td>3.2</td>
<td>3.4</td>
<td>3.5</td>
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<tr>
<td>Vietnam</td>
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<td>6.4</td>
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<tr>
<td>ASEAN</td>
<td>4.8</td>
<td>4.9</td>
<td>5.1</td>
</tr>
</tbody>
</table>

Source: National authorities, AMRO
The recent recovery in global trade, if sustained, could provide some upsides to regional exports and growth.
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**

- **Private Investment (60% of Total Investment)**
- **Total Investment**

**China: Private Sector Profitability**

- % yoy, 3MMA

Source: NBS, AMRO
Concerns about China’s capital outflows have eased recently, partly reflecting the strengthened capital flows management which helped in containing RMB exchange rate volatility.

Source: PBC, SAFE, AMRO
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

Source: Cabinet Office, JMOF, BOJ, AMRO
Spillover Analysis (Shocks from 1% sustained decrease (or increase) in U.S.’ & China’s real & financial variables), Preliminary

1. Real Sector Shocks

<table>
<thead>
<tr>
<th>1% Sustained Decline in Real GDP Growth</th>
<th>Mean Impact on Regional EMs (Cumulative, 36 months)</th>
</tr>
</thead>
<tbody>
<tr>
<td>• 1% sustained decline in U.S.’ real GDP growth</td>
<td>Impact on growth ➔ -0.11 ppts</td>
</tr>
</tbody>
</table>
| • 1% sustained decline in China’s real GDP growth | Impact on growth ➔ -0.75 ppts  
Impact on nominal export growth (in local currency) ➔ -1.35 ppts |

2. Financial Sector Shocks

<table>
<thead>
<tr>
<th>1% Sustained Increase in Expected Default Frequency (EDF)</th>
<th>Mean Impact on Regional EMs (Cumulative, 12 months)</th>
</tr>
</thead>
</table>
| Banking Sector Shocks | ➔ +0.11 ppts (Impact on Regional Banks’ EDF)  
• U.S.’ banking sector soundness  
• China’s banking sector soundness ➔ +0.25 ppts (Impact on Regional Banks’ EDF) |
| Corporate Sector Shocks | ➔ +0.11 ppts (Impact on Regional Banks’ EDF)  
• China’s corporate sector soundness ➔ +0.12 ppts (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
Financial markets have been largely stable, with the resumption of capital inflows, although risks remain tilted to the downside, mainly from global policy uncertainties.

Notes: All data are up to end-April 2017, except for bond (up to end-Apr 2017). The Bloomberg Asia Currency Index refers to ADXY.

Source: National Authorities, Bloomberg
Risks Spotlight: Financing Risks

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

Note: Private sector credit refers to loans and advances extended by the banking system to non-financial companies and households. Source: National Authorities, World Bank, Bloomberg.
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.

Source: National Authorities, AMRO ERPD Matrix
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 / Macropudential Policy**

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

**Fiscal Policy**

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

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**Headline Inflation**

<table>
<thead>
<tr>
<th>Country</th>
<th>2017 p/</th>
<th>2018 p/</th>
<th>Target (Inflation Targeting Economies)</th>
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<tr>
<td>MM</td>
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</tbody>
</table>

**Central Government Fiscal Revenue Performance**

- Total Revenue (% of GDP)
  - Average 2011-13
  - Average 2014-16

Notes: Fiscal data for China and Vietnam refers to general government only.
Source: National Authorities, AMRO
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**
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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I. ASEAN+3 Macroeconomic Prospects and Challenges

II. 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)

Source: AMRO
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
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

<table>
<thead>
<tr>
<th>Host</th>
<th>Source</th>
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<td>23.0</td>
<td>16.4</td>
<td>17.6</td>
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</table>

Source: ASEANstats
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

Source: AMRO, IMF
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**

Note: Data for Myanmar are not available
Source: World Bank
Macroeconomic and financial stability has been strengthened.

<table>
<thead>
<tr>
<th>Policy</th>
<th>Pre-AFC Period</th>
<th>Post-AFC Period</th>
</tr>
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<tbody>
<tr>
<td>Monetary Policy</td>
<td>Pegged exchange rate regime</td>
<td>• Inflation Targeting with a managed-float exchange rate regime</td>
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<tr>
<td></td>
<td></td>
<td>• Capital Account Liberalization Plan</td>
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<tr>
<td>Fiscal Policy</td>
<td></td>
<td>• Fiscal Sustainability Framework</td>
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<td></td>
<td></td>
<td>• Tax Reforms</td>
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<tr>
<td>Financial Regulations</td>
<td>• Commercial Banking Act 1962</td>
<td>• Financial Institution Act 2008</td>
</tr>
<tr>
<td></td>
<td>• Finance Companies and Credit Fonciers Act 1962</td>
<td>• Risk-based supervision (Basel standards, consolidated supervision for financial conglomerate, IAS 39 accounting standard)</td>
</tr>
<tr>
<td></td>
<td>• Compliance-based supervision</td>
<td>• Macroprudential measures on some categories of consumer loans</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Regulatory reforms for non-bank financial institutions</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Financial Sector Master Plan Phase I, II and III</td>
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<tr>
<td>Financial infrastructure</td>
<td></td>
<td>• Credit Bureau</td>
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<tr>
<td></td>
<td></td>
<td>• Deposit Protection Agency</td>
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<td></td>
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<td>• National e-Payment system</td>
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</table>
From ‘Dual Crisis’ to ‘Multiple Stability’

**External Stability**
- Short term external debt
- Long term external debt
- International reserves (RHS)

**Financial Stability**
- Gross NPL ratio
- Capital Adequacy Ratio (RHS)

**Price Stability**
- Headline inflation

**Fiscal Stability**
- Fiscal balance to GDP
- Public debt to GDP

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**

- Private investment
- Private consumption
- Exports

**Production structure**

- Agriculture
- Manufacture
- Non-financial Service

**Financial System Structure**

- Bond outstanding
- Stock market capitalization
- Commercial bank credit

Source: Office of National Economic and Social Development Board, Bank of Thailand, AMRO staff calculations
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.
Thank You

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