

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

ASEAN+3 Macroeconomic Research Office (AMRO)

Singapore

October 2018

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 28 September 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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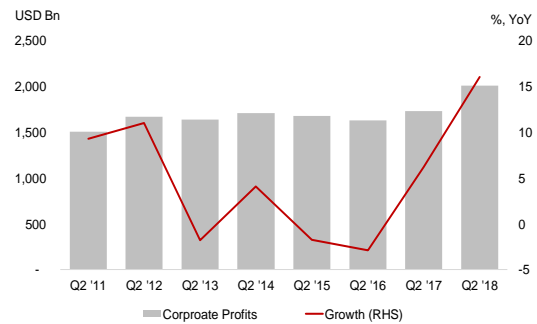
Global Economic Developments

The U.S. economy remains robust, as favorable fundamentals continue to support near term expansion. The U.S. economy continues to expand at above trend growth, which is tightening the labor market and gradually boosting wage growth. Coupled with sustained improvement in consumer confidence and steady rise in consumer spending in August 2018, the near term consumption outlook remains robust. On the corporate side, Q2 earnings report surpassed market expectations (+16.1 percent), notching the fastest pace in 6 years, largely reflecting the boost from tax cuts (Figure 1). Market expectations for H2 2018 continue to hold up.

As widely anticipated, the U.S. Fed raised the Fed Funds rate by 25 bps in the 26 September FOMC meeting, and signaled another rate hike by end of this year. Global financial conditions is expected to tighten with the additional rate hike by end of this year while the Fed has maintained its projection for three rate hikes in 2019, as per its latest Summary of Economic Projections (SEP) (Figure 2). The FOMC Dots Median (2.375 percent in 2018) suggests that market consensus has converged to Fed's signaled pace of rate hikes (Figure 2).

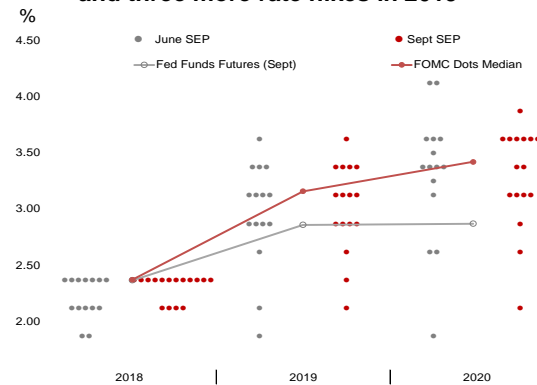
In Europe, economic sentiment and confidence indicators in both Eurozone and the U.K. dip in September, signaling less buoyant economic activities ahead. Eurozone's economic sentiment indicator edged lower in September after the slight uptick in August, along with the decline in consumer confidence (Figure 3). The Eurozone's manufacturing PMI readings also saw a decline although still remaining expansionary in September, partly in line with a more moderate pace of global demand. The downward trend of these indicators is also observed in the U.K. economy¹, mainly reflecting the uncertainty

Figure 1 The U.S. corporate profits surpassed market expectations in Q2 2018, with the outlook for H2 2018 holding up



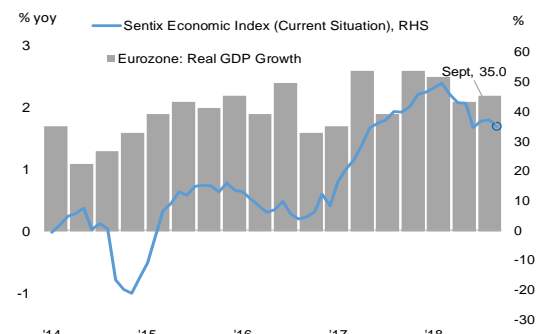
Source: Bureau of Economic Analysis, Federal Reserve Bank of St. Louis, AMRO staff calculation

Figure 2 Based on the September SEP, the U.S. Fed signaled one more rate hike in 2018 and three more rate hikes in 2019



Source: FOMC

Figure 3 Eurozone economic sentiment and confidence indicators show a slight dip in confidence



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

¹ U.K. manufacturing PMI came in at 52.8 in August, down from 53.8 in July 2018.

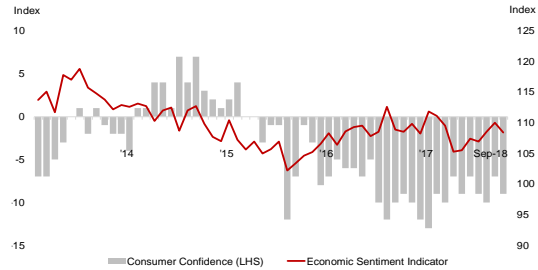
surrounding the outcome of Brexit, weighing on consumer sentiments (Figure 4). Moving forward, while the Eurozone's economy is proceeding at a relatively lower gear compared to 2017, the positive trend remains intact.² In its meeting on 13 September, the ECB decided to keep its policy rate on hold at least through summer 2019, while halving bond purchases from October 2018. In contrast, uncertainty over the terms governing Brexit, plus slow money and lending growth, suggest that U.K. economy will likely continue to underperform both the U.S. and the Eurozone in the near term. As widely expected, the Bank of England kept its policy interest rate on hold in its September meeting, with the base interest rate remaining at 0.75 percent.

In commodities markets, global oil prices continue to rally, while agriculture and base metal prices remain sluggish. Global oil prices reached around USD82 per barrel as of late September, on concerns about supply cuts as the second round of sanctions on Iran will come into force on 4 November 2018. Market estimates suggest that the sanctions against Iran's oil exports would cause a cut in world supply of at least 1.5 million barrels a day or 1.5 percent of the total global oil supply³. Agriculture and base metal prices remain sluggish, diverging from oil prices. For metal prices, the divergence reflects muted demand from consuming industries as sentiments continued to be bearish on the back of persistent concerns over the escalation in global trade tensions.

Regional Economic Developments

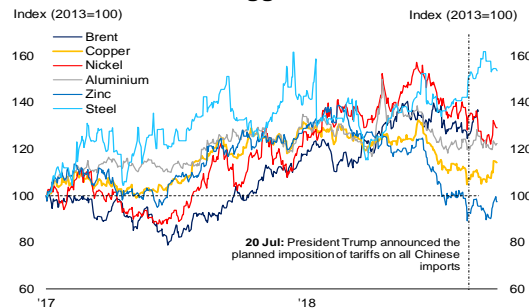
While baseline regional economic growth in 2018 of 5.4 percent remains unchanged, the uncertainty about the baseline growth trajectory in 2019 has increased. Even as common global factors (Fed policy and trade tensions) weigh on regional economic outlook,

Figure 4 Brexit continues to weaken economic sentiment and consumer confidence in the UK



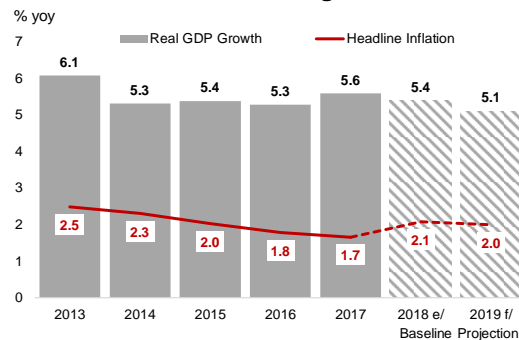
Source: European Commission, GfK NOP (UK)

Figure 5 Global oil prices have been on the uptrend, while base metal prices remained sluggish



Source: Haver Analytics

Figure 6 Baseline regional growth and inflation remain unchanged, but the uncertainty over baseline growth in 2019 is mounting



Source: AMRO

² The still-accommodative monetary policy stance in the Eurozone will continue to underpin domestic demand, with firming employment and wage growth. Given the improved inflation outlook in the Eurozone, the ECB remains on track to phase out its bond-buying program by the year end.
³ According to OPEC, global oil supply increased by 0.49 mb/d to average 98.9 mb/d in August.

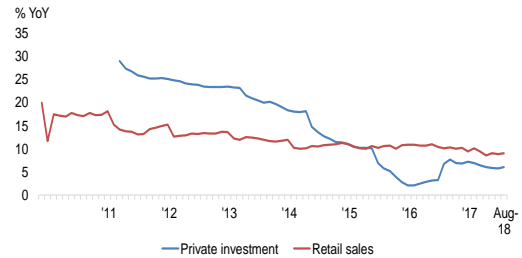
the region has also been hit by large volatility shocks from the turmoil in other EM regions, dampening the short term outlook. For 2018, AMRO has maintained the baseline growth estimates for the region at 5.4 percent, with inflation remaining benign (at 2.1 percent), but shaved our forecast for next year to 5.1 percent (Figure 6, Annex 1 and 2).

The region is increasingly being tested with a sharper trade off between financial stability and growth objective. As global financial conditions tighten and the pull factors, (particularly in the U.S.) become stronger, EM assets, including in the region are likely to become less attractive, particular as risk appetite wanes. Some economies in the region have pro-actively tightened monetary policy in response. Indonesia and the Philippines, for instance, raised their benchmark policy rates by 25 basis points to 5.75 percent and 50 basis points to 4.5 percent on 27 September, respectively (Annex 4).⁴

In China, economic activities are largely sustained for the rest of 2018, with some uncertainty over the 2019 outlook. Retail sales and private investment data suggest that the trend is largely stable this year (Figure 7). However, China’s industrial profit growth nearly halved to 9.2 percent in August, from 16.2 percent in July 2018, the lowest performance in 5 months suggesting that the deleveraging campaign to contain corporate debt and risky borrowings has weighed on business activities (Figure 8).

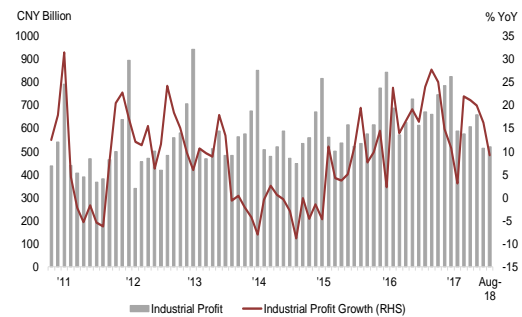
In Japan, the favorable Q3 outlook is likely to be sustained, as several major indicators have recorded further improvement. August data indicate an improvement in both factory output and retail trade. Japan’s industrial production increased for the first time in 4 months to 0.7 percent at the end of August and is expected to continue rising in the next

Figure 7 Retail sales and private investment data suggest that the trend is largely stable this year



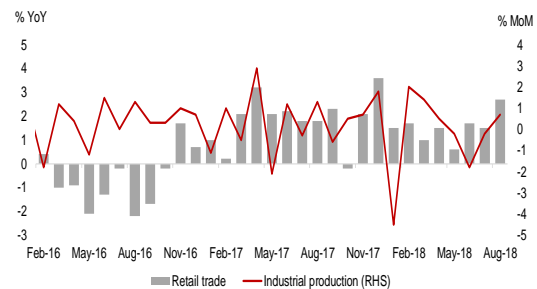
Source: China’s National Bureau of Statistics

Figure 8 China’s industrial profit growth hits 5-month low



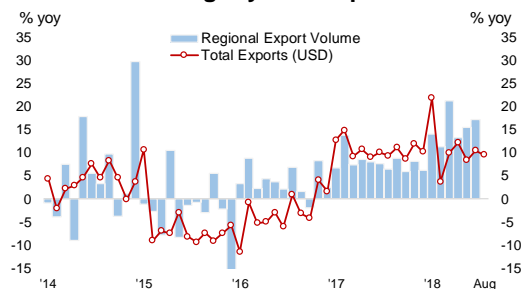
Source: China’s National Bureau of Statistics

Figure 9 Japan’s industrial production and retail trade improved, reflecting better Q3 growth



Source: National Authorities

Figure 10 Regional export performance grew at a slightly slower pace



Source: National Authorities

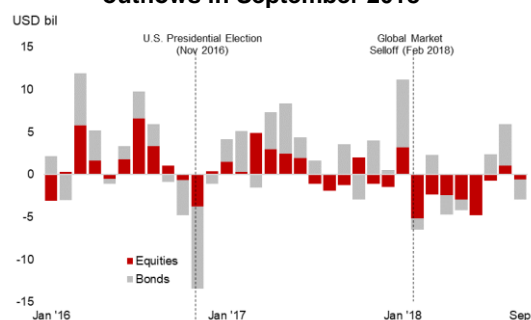
⁴ On a year-to-date basis, Indonesia has raised its policy interest rate five times by a cumulative 150 bps, and the Philippines 4 times by a cumulative 150 bps, as of September 2018.

few months as trade frictions between Japan and the U.S eased after the kick-start of bilateral trade negotiations between the two economies. Retail trade growth, meanwhile, surged at the fastest pace in eight months (+2.7 percent yoy), while the unemployment rate slipped slightly to 2.4 percent in August (Jul '18: 2.5 percent).

Other economies in the region reported a moderation in PMI readings for September in line with the softer outlook for Q3 2018 (Annex 3). In tandem with the softer global manufacturing PMI readings, the region saw a moderate pace of expansion in factory output, with new export orders suggesting some weakness ahead (notably in China, Indonesia, Singapore and Vietnam). Vietnam, however, still bucked the trend, with stronger-than-expected growth data for Q3 2018 (+7 percent yoy). On exports, regional exports slowed slightly in August, as compared to July, in tandem with the softer expansion in factory output (Figure 10).

Foreign portfolio capital flows in regional EMs turned to net outflows in September 2018, as uncertainties in other EM regions heightened. After two months of net capital inflows, portfolio capital flows reversed to net outflows across regional EMs (excluding China), as risk aversion towards EM assets took hold following the turmoil in Turkey. Regional EMs saw an outflow of USD0.6 billion for equities and USD2.3 billion for bonds. Korea, however, still received large cumulative capital inflows of around USD12 billion into its bond market during Jan-Sep 2018, given its strong economic fundamentals and resilience to external shocks. On 13 September this year, Moody's maintained Korea's global bond offering rating at "Aa2", citing the country's resilience to external shocks, sound public finances due to the continued implementation of structural reforms, as well as the easing geopolitical tension.

Figure 11 The region saw net capital outflows in September 2018



Note: September data for bonds refer to Indonesia and Korea only.
Source: National Authorities

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 | 3Q'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 | 3.5 | - |
| 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 | 4.5 | - |
| 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 | 3.9 | - |
| Thailand | 3.3 | 3.9 | 3.4 | 3.9 | 4.3 | 4.0 | 4.8 | 4.6 | - |
| Vietnam | 6.2 | 6.8 | 5.2 | 6.3 | 7.5 | 7.7 | 7.5 | 6.8 | 7.0 |

Source: National Authorities, Bloomberg, CEIC

*Table shows economies with latest GDP data releases since the last edition of the Monthly Update of the AREO. Data released as of 28 September 2018.

Annex 2: AMRO's Growth and Inflation Projections for ASEAN+3

| % year-on-year | 2016 | 2017 | 2018 e/ | 2019 f/ |
|-------------------------------|------|------|---------|---------|
| ASEAN+3 | | | | |
| Real GDP Growth | 5.3 | 5.6 | 5.4 | 5.1 |
| Inflation | 1.8 | 1.7 | 2.1 | 2.0 |
| Brunei Darussalam | | | | |
| Real GDP Growth | -2.5 | 0.5 | 1.6 | 3.4 |
| Inflation | -0.7 | -0.1 | 0.2 | 0.4 |
| Cambodia | | | | |
| Real GDP Growth | 7.0 | 6.9 | 7.2 | 7.0 |
| Inflation | 3.0 | 2.9 | 3.1 | 3.2 |
| China | | | | |
| Real GDP Growth | 6.7 | 6.9 | 6.6 | 6.2 |
| Inflation | 2.0 | 1.6 | 2.0 | 1.8 |
| Hong Kong, China | | | | |
| Real GDP Growth | 2.1 | 3.8 | 3.8 | 2.7 |
| Inflation | 2.4 | 1.5 | 2.6 | 2.7 |
| Indonesia | | | | |
| Real GDP Growth | 5.0 | 5.1 | 5.2 | 5.3 |
| Inflation | 3.5 | 3.8 | 4.0 | 4.0 |
| Japan | | | | |
| Real GDP Growth (Fiscal Year) | 1.2 | 1.6 | 1.2 | 0.7 |
| Inflation (Fiscal Year) | 0.2 | 0.0 | 0.9 | 1.0 |
| Korea | | | | |
| Real GDP Growth | 2.8 | 3.1 | 2.8 | 2.6 |
| Inflation | 1.0 | 1.9 | 1.5 | 1.9 |
| Lao PDR | | | | |
| Real GDP Growth (Fiscal Year) | 7.0 | 6.8 | 6.7 | 6.9 |
| Inflation | 1.6 | 0.8 | 2.5 | 2.5 |
| Malaysia | | | | |
| Real GDP Growth | 4.2 | 5.9 | 4.9 | 4.7 |
| Inflation | 2.1 | 3.8 | 1.2 | 2.3 |
| Myanmar | | | | |
| Real GDP Growth (Fiscal Year) | 5.9 | 6.8 | 7.4 | 7.6 |
| Inflation | 6.8 | 5.1 | 5.0 | 4.5 |
| The Philippines | | | | |
| Real GDP Growth (Fiscal Year) | 6.9 | 6.7 | 6.5 | 6.4 |
| Inflation | 1.8 | 3.2 | 5.2 | 4.3 |
| Singapore | | | | |
| Real GDP Growth | 2.4 | 3.6 | 3.2 | 2.4 |
| Inflation | -0.5 | 0.6 | 0.6 | 1.3 |
| Thailand | | | | |
| Real GDP Growth | 3.3 | 3.9 | 4.4 | 4.0 |
| Inflation | 0.2 | 0.7 | 1.3 | 1.5 |
| Vietnam | | | | |
| Real GDP Growth | 6.2 | 6.8 | 6.9 | 6.7 |
| Inflation | 2.7 | 3.5 | 3.9 | 3.7 |

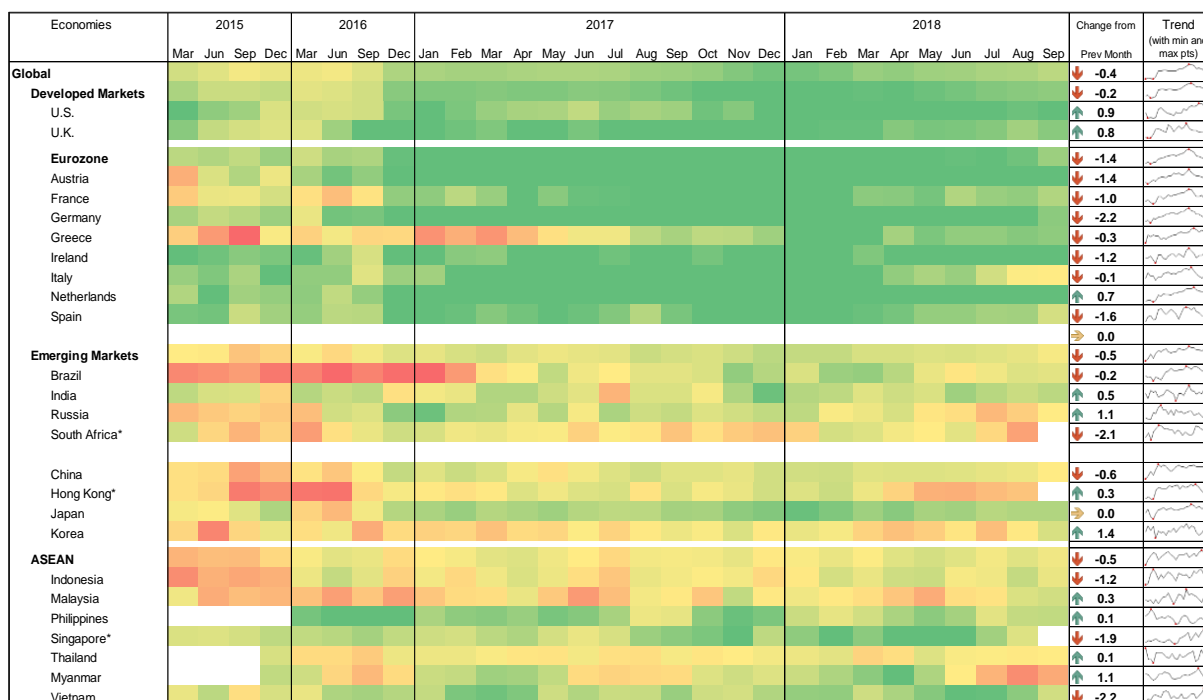
Notes: e/ refers to estimates, f/ refers to forecasts

GDP Growth: refers to calendar year, unless otherwise stated.

Inflation: refers to period average headline inflation; in calendar year unless otherwise indicated

Source: National authorities, AMRO staff estimates and projections

Annex 3: Global Manufacturing PMI Heatmap



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 4: Major Policy Developments (7 – 28 September 2018)

| | |
|--------------|---|
| China | <p>[25 September] In order to promote the opening-up of the bond market and regulate the bond issuance by overseas institutions, with the approval of the State Council, the People's Bank of China (PBC) and the Ministry of Finance (MOF) have jointly issued the Interim Measures for Administration of the Bond Issuance by Overseas Institutions in the National Inter-bank Bond Market.</p> <p>[30 September] According to the Ministry of Finance, starting from November 1 this year, China will slash most-favored-nation tariffs on a total of 1,585 taxable items as the country moves to further open its market. The average tariff rate will be reduced from 10.5 percent to 7.8 percent for these items.</p> |
| Japan | <p>[19 September 2018] The Policy Board of the Bank of Japan decided to maintain the policy rates and the guidelines for asset purchases unchanged.</p> |
| Korea | <p>[13 September] The government announced additional measures to curb the overheating housing market in Seoul. The measures comprise of tighter mortgage conditions for multiple homeowners, higher property taxes for multiple homeowners, and more housing supply in Seoul.</p> |

| | |
|--------------------|--|
| Indonesia | [27 September 2018] Bank Indonesia raised the seven-day reverse repo rate by 25 basis points to 5.75 percent. |
| Philippines | [27 September 2018] The Monetary Board of the Bangko Sentral ng Pilipinas (BSP) raised the interest rate on the overnight reverse repurchase (RRP) facility by 50 basis points to 4.5 percent. |
| Thailand | [19 September 2018] Bank of Thailand's Monetary Policy Committee kept the policy rate unchanged at 1.50 percent. |