The Outlook for Asian & Australian Economies

Asian economies accelerate growth backed by strong exports, maintain stable growth led by domestic demand

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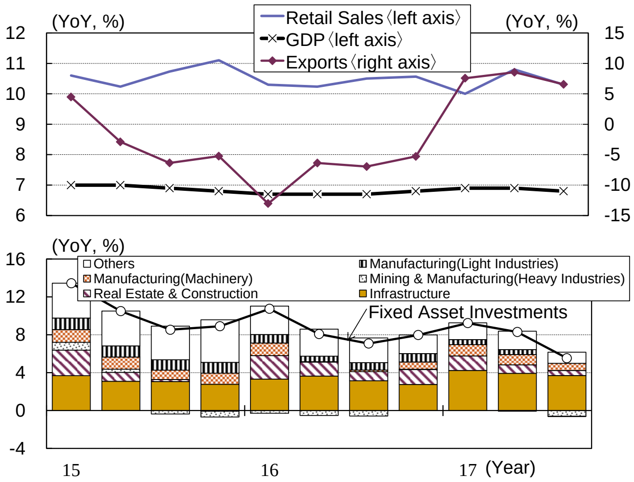
1. Summary of Current Conditions and Outlook for Asian and Australian Economies

(1) CURRENT CONDITIONS

Real GDP growth of China, the largest economy in Asia, was +6.8% YoY in Jul-Sep 2017, slightly decelerated from the previous quarter (+6.9% YoY). Private consumption remains firm and is supporting the economy while tightening environmental regulation, in addition to the adjustment in excess production capacity, weigh on production and investments especially in mining and heavy industry sectors, and a trend of economic slowdown has been slightly intensifying (see chart 1, table 1).

Chart 1：China's GDP-related Indicators



Source: China National Bureau of Statistics, BTMU Economic Research Office

Table 1：Main Economic Indicators (China)

	2017				
	Jun	Jul	Aug	Sep	Oct
Exports (YoY, %)	10.8	6.5	5.1	8.1	6.9
Imports (YoY, %)	17.1	11.0	13.4	18.6	17.2
Fixed Assets Investment (YTD, YoY, %)	8.6	8.3	7.8	7.5	7.3
Retail Sales (YoY, %)	11.0	10.4	10.1	10.3	10.0
Industrial Production (YoY, %)	7.6	6.4	6.0	6.6	6.2
Manufacturing PMI	51.7	51.4	51.7	52.4	51.6
Non-manufacturing PMI	54.9	54.5	53.4	55.4	54.3
CPI (YoY, %)	1.5	1.4	1.8	1.6	1.9
PPI (YoY, %)	5.5	5.5	6.3	6.9	6.9

Note: 1) Manufacturing PMI and Non-manufacturing PMI are from China National Bureau of Statistics.
2) Shadowed portion indicates lower growth rates or decline in indicators from previous months.

Source: China National Bureau of Statistics, BTMU Economic Research Office

In other Asian economies excluding China, in addition to the solid domestic demand, driven by private consumption amid ongoing price stability at lower levels, strong exports are boosting growth pace. Real GDP growth in Jul-Sep showed acceleration of pace in countries/regions such as NIEs, Thailand and Malaysia which are highly dependent on exports (see table 2). In India, the impact of Goods and Services Tax (GST) which was introduced in July has been fading while real GDP growth in Jul-Sep accelerated for the first time in six quarters. The Australian economy is continuing moderate expansion on the back of a recovery in corporate sector due to a rebound in resource prices.

Table 2: Real GDP Growth Rates, Major Asian Economies

(YoY, %)

	2016				2017		
	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep
China	6.7	6.7	6.7	6.8	6.9	6.9	6.8
India	9.1	7.9	7.5	7.0	6.1	5.7	6.3
South Korea	2.9	3.4	2.6	2.4	2.9	2.7	3.8
Taiwan	-0.3	1.0	2.0	2.8	2.6	2.3	3.1
Hong Kong	1.0	1.8	2.0	3.2	4.3	3.9	3.6
Singapore	1.9	1.9	1.2	2.9	2.5	2.9	5.2
NIEs	**1.9**	**2.6**	**2.3**	**2.6**	**3.0**	**2.8**	**3.8**
Indonesia	4.9	5.2	5.0	4.9	5.0	5.0	5.1
Malaysia	4.1	4.0	4.3	4.5	5.6	5.8	6.2
Thailand	3.1	3.6	3.2	3.0	3.3	3.8	4.3
Philippines	6.9	7.1	7.1	6.6	6.4	6.7	6.9
Vietnam	5.5	5.8	6.6	6.7	5.2	6.3	7.5
ASEAN5	**4.8**	**5.1**	**5.0**	**4.9**	**5.0**	**5.3**	**5.6**
Asia 11 economies	**6.1**	**6.1**	**6.0**	**6.0**	**6.0**	**6.0**	**6.2**

(QoQ, %)

Australia	**1.0**	**0.8**	**-0.3**	**0.9**	**0.4**	**0.9**	**0.6**

Note: Shadowed portion indicates lower growth rates from previous quarters.
Source: Individual country statistics, BTMU

(2) OUTLOOK

Looking ahead, Asian economies as a whole will continue stable growth towards 2018 buoyed by ongoing solid domestic demand led by private consumption as well as the expected export expansion.

China's economy is expected to maintain real GDP growth of mid +6% YoY range throughout the year although the growth pace will slow down towards 2018 (see table 3). The government will continue to push for sustaining the growth to ensure social stability even after the twice-a-decade Communist Party congress is closed, exports will maintain its increasing trend backed by solid economic growth in overseas, and private consumption will expand due to favorable employment and income environment.

In other Asian economies, domestic demand mainly driven by private consumption will remain firm on the back of stable employment and income environment and ongoing growth-friendly fiscal and monetary policy. The exports are expected to decelerate its growth pace towards next year yet are likely to maintain its gradual increasing trend driven by solid demand in advanced countries. Based on this, we forecast real GDP growth to show between upper +2% YoY and +3% YoY range towards 2018 in NIEs, which is highly dependent on external demand, and slightly more than +5% YoY in ASEAN-5 countries. The Indian economy will return to a stable growth path led by domestic demand on the back of the economic stimulus packaged by the government, while the impact of GST introduction will fade away gradually.

The Australian economy will stay on a gradual recovery trend as the mining sector's downward pressure on the economy is expected to weaken in response to recovering resource prices.

The foreseeable risk could be the external environmental changes such as destabilization of financial markets due to US rate hikes and the increasing geopolitical risks. The major Asian currencies overall remain stable backed by increasing capital inflows from overseas due to their favorable fundamentals. Though many countries maintain an accommodative monetary policy amid ongoing price stability at lower levels, US interest rate hikes at a moderate pace is expected hence the risks of significant capital outflows and sharp currency depreciation remain.

It is advisable to take note of these risks as the currency depreciation often leads to an increase in inflation, makes it difficult to maintain an accommodative monetary policy, and could hinder private consumption and business activities.

Table 3: Outlook for Asian and Australian Economies

	Nominal GDP (2016)		Real GDP growth (YoY %)			Consumer price inflation (YoY %)			Current account (USD billion)		
	USD trillion	Share %	2016 Results	2017 Outlook	2018 Outlook	2016 Results	2017 Outlook	2018 Outlook	2016 Results	2017 Outlook	2018 Outlook
Asian countries/regions	18.17	100.0	5.9	6.1	5.9	2.2	2.0	2.3	469	370	374
China	11.22	61.7	6.7	6.8	6.4	2.0	1.6	1.8	196	124	136
India*	2.26	12.4	7.1	6.6	7.6	4.5	3.2	4.5	-15	-33	-37
NIEs	2.56	14.1	2.3	3.0	2.6	1.1	1.5	1.5	242	236	240
South Korea	1.41	7.8	2.8	3.0	2.8	1.0	2.0	1.6	99	87	85
Taiwan	0.53	2.9	1.4	2.5	2.3	1.4	0.8	1.3	72	78	76
Hong Kong	0.32	1.8	2.0	3.5	2.5	2.4	1.5	2.0	15	9	13
Singapore	0.30	1.6	2.0	3.3	2.5	-0.5	0.8	1.4	57	62	66
ASEAN5	2.14	11.8	4.9	5.2	5.1	2.4	3.2	3.3	46	43	36
Indonesia	0.93	5.1	5.0	5.1	5.2	3.5	3.9	4.2	-17	-17	-18
Malaysia	0.30	1.6	4.2	5.5	5.1	2.1	3.7	2.5	7	8	8
Thailand	0.41	2.2	3.2	3.6	3.5	0.2	0.7	1.4	48	48	42
Philippine	0.30	1.7	6.9	6.6	6.3	1.8	3.2	3.6	-1	0	0
Vietnam	0.20	1.1	6.2	6.7	6.4	2.7	3.9	4.2	8	5	4
Australia	1.22	-	2.5	2.3	2.7	1.3	2.0	2.1	-33	-33	-34

Note: *Fiscal year (from April to March)

Source: Individual country statistics, BTMU Economic Research Office

2. Key points

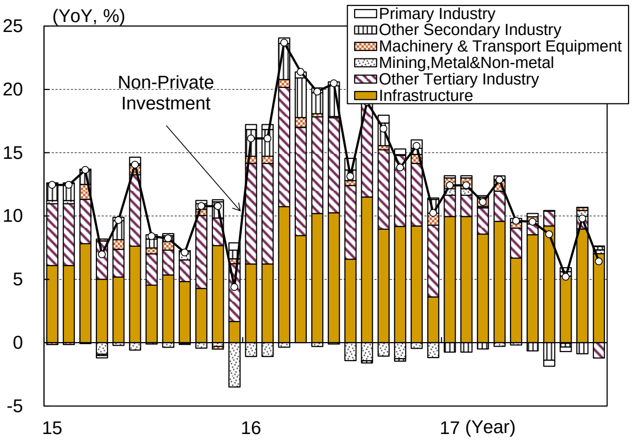
(1) Chinese Economy

General Secretary Xi Jinping incorporated the political thought bearing his name in the party constitution at the 19th Communist Party Congress held in October, and enhanced the power base in the second term of his administration. The government is expected to shift its focus to structural adjustment however it will continue to pay close attention to maintain growth to ensure social stability. Considering that the government has enough room to introduce policies to sustain economic growth, and private consumption has a trend of stable expansion, the economy is expected to maintain real GDP growth of mid +6% YoY range throughout the year although the growth pace will slow down towards 2018.

We will look at the details below. The reduction of production capacity seems to be steadily progressing in steel and coal sectors in 2017, following the previous year, and it was announced that the annual targets have been achieved. Inspections by the government detected some cases where reduction in excess production capacity was not fully enforced which leaves room for doubt about the achievement of annual targets. However it is a fact that, under improving market conditions and circumstances of less excessive competitions, there has been an increase in profits in both steel and coal industries (net profits in Jan-Oct 2017 recorded 2.3-fold YoY in steel industry and 4.4-fold YoY in coal industry).

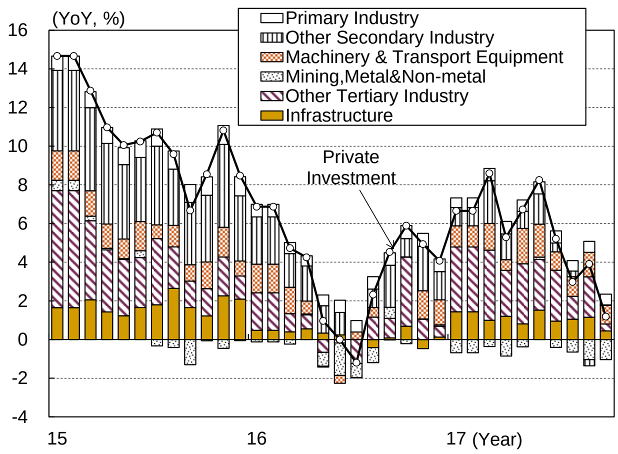
Under such situation, investments will continue its decelerating trend both in state-owned enterprises (SOEs) and private enterprises. SOEs have been driving the investments since last year. Infrastructure and tertiary industry (excluding infrastructure, mainly real estate) were the main industries SOEs invested heavily last year. However, since the beginning of this year, the growth of investment in tertiary industry has slowed, and infrastructure investment also showed slowdown subsequently (see chart 2). Furthermore, the central government instructed local governments to monitor and review public-private partnership (PPP) projects which have been boosting infrastructure investment, and the number of PPPs which have been interrupted already started to increase. Meanwhile, private investment, which was sluggish last year, showed some recovery since the beginning of this year backed by tax cuts and other factors. However, it started to slow the pace again since the second half of this year (see chart 3), which indicates the difficulty of obtaining loans under the gradual tightening policy towards deleverage.

Chart 2：China's Non-Private investment



Source: China National Bureau of Statistics, BTMU Economic Research Office

Chart 3：China's Private investment



Source: China National Bureau of Statistics, BTMU Economic Research Office

Real estate investment is also expected to show a slowing trend. Since the autumn of 2016, inventory reduction made progress nationwide as demand has shifted to small and medium cities due to the introduction of regulations in major cities where the housing prices soared. According to the housing policy announced in April this year, there should be many areas subject to supply expansion as per inventory level. However more and more selling restrictions have been applied in small and medium cities as the housing prices increase. As a result the housing sales are sluggish, and its impact is inevitable.

Exports will continue to increase, but high growth is difficult to be expected. Exports will be supported by stable growth of overseas economy however it is unlikely that the government will tolerate a substantial depreciation of yuan which would provoke capital outflow. Trade conflicts with US seem to recede after $253.5 billion package of deals signed between China and US and China's decision to open up its financial sector to foreign investment by easing foreign ownership restrictions on its financial institutions during US President Donald Trump's visit to China in November. However, take note that most of commercial deals were signed in memorandum or letter of intent with no firm commitments, and financial deregulation is also depend on how it will be implemented in the future.

Private consumption is expected to remain firm. Tax break for small-sized vehicles which was introduced in 2016 will expire next year after the tax break reduction this year. Considering that motor vehicle sales have remained stable after it had a rush demand in the second half of 2016 and its sluggishness in early 2017, the expiration of tax break will have a limited effect. The growth of housing-related materials such as furniture and building materials is showing a slowdown as the growth of housing sales decelerated. Meanwhile, there are favorable factors. Both urban and rural areas have the favorable employment and income environment where income growth rate gradually accelerates, and online shopping, which has been growing with high pace and leading private consumption, is spurring its activities even more through the integration with real offline shops.

If the government rush to promote structural adjustment, especially deleverage, the possibilities cannot be ruled out that it could lead to financial and capital market turmoil and/or slowdown of real economy which has been supported by increasing debts. In fact, reform of SOEs have been implemented through more gentle way such as debt-equity swaps and corporate merger rather than liquidation, therefore such reform should not become strong downward pressure to the economy. Furthermore, the authorities seem to try and balance structural adjustment and stable growth lately. The People's Bank of China, the central bank, announced on September 30 that it would reduce the reserve requirement ratio (RRR) depending on the volume of banks' lending to smaller firms in early 2018, and this is expected to create room to expand lending of at least RMB 600 billion. Meanwhile, the State Council Financial Stability and Development Committee, whose establishment was announced at National Financial Work Conference (a twice-a-decade conference to decide a financial policy) in July, held the first meeting in November 8. The Committee aims to enhance efficiency by linking banking, securities, and insurance-divided regulatory bodies. It indicates Xi administration's emphasis on the progress of structural adjustment and avoidance of systemic risk, and its success or failure is to be watched as it will greatly affect the mid-to-long term development of Chinese economy.

(2) Other Asian Economies

For Asian economies excluding China, stable growth will continue as domestic demand remains solid and exports expand and its favorable effect spreads. Private consumption is expected to show solid expansion backed by stable employment and income environment. In addition, the ongoing fiscal policies responding to the economic conditions will continue to support domestic demand expansion. Looking at the each country's next fiscal year's budget, it indicates the continuation of the government's growth-friendly policy which focus on lower income group, employment and infrastructure investment while it emphasis on the maintenance of fiscal discipline. The Malaysian government announced FY2018 budget in October which concentrates funding in major infrastructure investments such as high-speed railway, and includes income tax exemption for lower income group and bonus payment to public servants in the run up to the upcoming election. Indian government also announced the economic stimulus package worth 9 trillion rupees (7% of GDP) in October which funds infrastructure development such as highway construction and injects capital into public sector banks.

Asian central banks in general continued to hold the interest rates steady. While the Bank of Korea raised interest rates to adjust the degree of monetary easing on the back of an improvement in growth outlook etc., most central banks are expected to maintain accommodative monetary policies for a time as the pace of US rate hikes is likely to be moderate compared to the past and currency value and price remain stable.

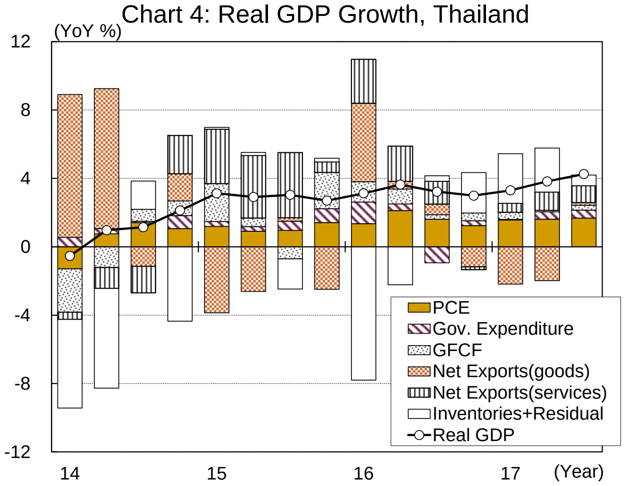
The pace of export expansion will gradually slow down towards next year as the cycle of semiconductor demand pass a peak and Chinese economy slows down, however an increasing trend on the back of expanding demand from advanced countries will be maintained. Export expansion is likely to boost growth rate through an improvement in contribution of external demand to GDP and spillover effects to other demand items. For example, an improvement in corporate earnings associated with export expansion will support private investment, reinforce an increase in household income which enables an expansion of private consumption, and boost growth rate of export-driven economies such as NIEs and Malaysia.

[Thailand]

Thai economy remains solid. Real GDP growth came in at + 4.3% YoY in Jul-Sep (compared to + 3.8% YoY in Apr-Jun), accelerated to the highest level in four and a half years (see chart 4). While private consumption remains firm, export expansion boosted the growth rate. Export of passenger vehicles has been sluggish due to conservative purchase in Vietnam prior to tariff elimination towards imported cars from ASEAN region at the beginning of 2018, while exports of agriculture, fisheries and processed food products such as rice, cassava, and natural rubber, petrochemical products, and electronic equipment and components all maintained high growth.

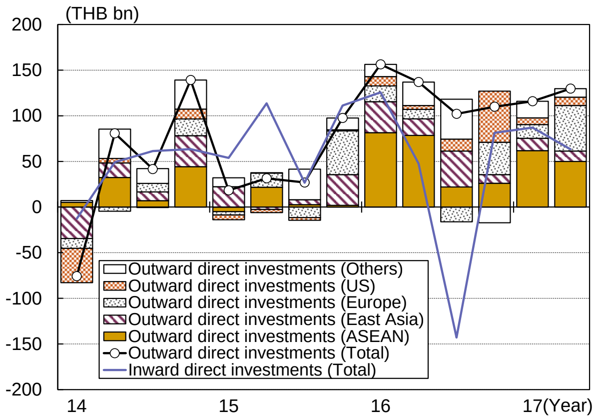
Going forward, with firm private consumption and export expansion together with acceleration of infrastructure investment, the economy will continue to grow gradually. For infrastructure investment, around THB 340 billion (2.3% of GDP) project, which invests in transportation such as expansion work of urban railways, highways and international airports, is in progress and another THB 350 billion-project is about to commence next year. Meanwhile, private investment will see an ongoing and gradual recovery on the back of improved corporate earnings associated with export expansion and rise in capacity utilization however a strong recovery will not be expected. One of the reasons why domestic private investment lack strength is that local major companies, who aim to tap into overseas markets and gain access to cheap labor, are increasing foreign direct investment while domestic market is expected to

Chart 4: Real GDP Growth, Thailand



Source: NESDB, BTMU Economic Research Office

Chart 5：Inward/Outward direct investments in Thailand



Note: “East Asia” represents the total figures of Japan, China, Hong Kong, Korea and Taiwan.
Source: The Bank of Thailand, BTMU Economic Research Office

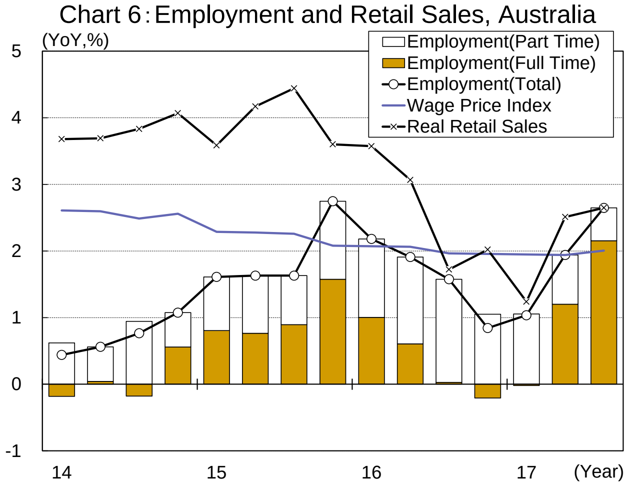
mature (see chart 5). While such move by Thai companies is expected to continuously curtail domestic investments, tapping into overseas markets and strengthening industrial competitiveness by establishing supply chain at local level could accelerate corporate activities and eventually support the economy in the mid-to-long term.

(3) Australian Economy

Australian economy continues its gradual recovery trend supported by the expansion of government expenditure while downward pressure from mining sector is receding on the back of a recovery in resource prices. Private consumption remains solid owing to an increase in employment and the ongoing low-interest rates while retail sales have been showing lower growth compared to the past (see chart 6). Looking at the recent increase in employment, it is mainly owing to an increase in “Health Care and Social Assistance” sector due to National Disability Insurance Scheme (NDIS) which was rolled out nationally on July 2016, and the growth of average wage has lost momentum. The fact that the ratio of household debt to disposal income stays as high as around 190% could be one of the factors weighing on the pace of recovery in consumption.

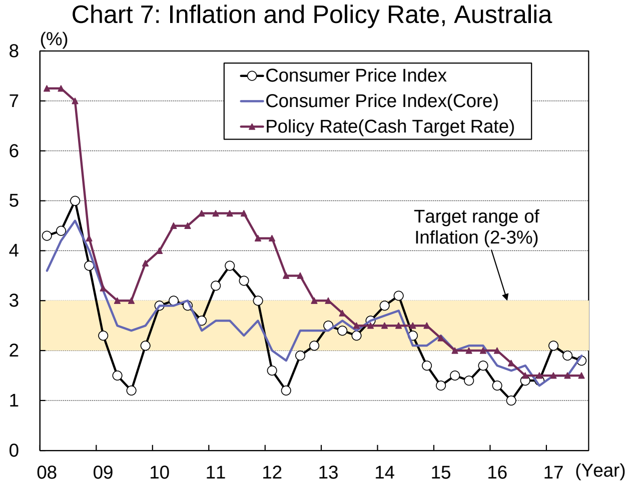
Going forward, a gradual economic recovery trend will continue on the back of a pickup in mining sector supported by a rebound in resource prices and the ongoing growth-friendly monetary policy. However, it will not be as strong as the growth pace of pre-2008 financial crisis (average +3.5% YoY) due to weaker private consumption and a slowdown in investments in China which is a major export destination. For price and monetary policies, the Reserve Bank of Australia (RBA) has been keeping official cash rates at record low of 1.5% since August 2016 as the rate of increase in Consumer Price Index (CPI) has stayed below the level of the targeted range of inflation (+2-3% YoY) (see chart 7). CPI recorded +1.8% YoY in Jul-Sep, stayed below the targeted range of inflation, as inflationary pressure from the demand in general is weak and growth of fuel price is slow, and considering that wage growth is moderate, RBA is expected to maintain its current monetary policy for a time.

Chart 6：Employment and Retail Sales, Australia



Source: Australian Bureau of Statistics, BTMU Economic Research Office

Chart 7: Inflation and Policy Rate, Australia



Source: ABS, RBA, BTMU Economic Research Office

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