The Outlook for Asian & Australian Economies

Asian economies maintain stable growth led by domestic demand although growth pace slows down

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1. Overview of Asian and Australian Economies

Real GDP growth of China, the largest economy in Asia, was +6.8% YoY in Jan-March, recording the same growth rate for the third consecutive quarter and made a good start towards achieving the government's 2018 goal (+6.5% YoY) (see table 1). Negative contribution of net exports (exports less imports) was offset by reacceleration of investments, particularly those in real estate. In other Asian economies excluding China, solid domestic demand driven by private consumption and ongoing increasing trend in exports have enabled stable economic expansion. Real GDP growth in Jan-Mar showed acceleration in Hong Kong, Singapore, Thailand and Philippines. Some economies showed deceleration of growth though such deceleration remained modest (see table 1). The Australian economy, as monthly economic indicators indicate, is continuing its gradual recovery mainly supported by private consumption.

Table 1: Real GDP Growth Rates, Major Asian Economies

(YoY, %)

	2016		2017				2018
	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
China	6.7	6.8	6.9	6.9	6.8	6.8	6.8
India	7.6	6.8	6.1	5.6	6.3	7.0	7.7
South Korea	2.7	2.6	2.9	2.8	3.8	2.8	2.8
Taiwan	2.0	2.8	2.6	2.3	3.2	3.4	3.0
Hong Kong	2.2	3.4	4.4	3.9	3.6	3.4	4.7
Singapore	1.2	3.7	2.5	2.8	5.5	3.6	4.4
NIEs	2.3	2.8	3.0	2.8	3.8	3.1	3.3
Indonesia	5.0	4.9	5.0	5.0	5.1	5.2	5.1
Malaysia	4.3	4.5	5.6	5.8	6.2	5.9	5.4
Thailand	3.1	3.0	3.4	3.9	4.3	4.0	4.8
Philippines	7.1	6.7	6.5	6.6	7.2	6.5	6.8
Vietnam	6.6	6.7	5.2	6.3	7.5	7.7	7.4
ASEAN5	5.0	4.9	5.0	5.3	5.6	5.5	5.5
Asia 11 economies	6.0	6.0	6.0	6.0	6.2	6.1	6.3
Australia	2.0	2.4	1.8	2.0	2.8	2.4	n.a.

Note: Shadowed portion indicates lower growth rates from previous quarters.
Source: Individual country statistics, MUFG Bank Economic Research Office

Looking ahead, Asian economies as a whole will maintain its stable growth, although the pace of growth is expected to slow down slightly towards 2019, buoyed by ongoing solid domestic demand led by private consumption as well as gradual expansion of exports.

Looking at China, downward pressure on the economy is expected to mount as Xi Jinping administration in its second term has been promoting structural adjustments. At the same time, however, the government is determined to avoid a substantial slowdown in economic growth under the uncertainties of an intensifying trade dispute with US, and it has room to avoid it using flexible and expeditious economic and monetary policies. Taking this into account, real GDP growth is expected to maintain +6% YoY range although it will gradually slow down towards 2019.

In other Asian economies, domestic demand mainly driven by private consumption will remain solid on the back of stable employment and income environment and ongoing growth-friendly fiscal and monetary policies. Although the pace of export expansion is expected to decelerate, it is likely to maintain its gradual increasing trend driven by growing demand in advanced countries. Based on this, we forecast real GDP growth towards 2019 to show upper +2% YoY in NIEs and lower +5% YoY in ASEAN-5 countries. Indian economy, led by domestic demand, is expected to sustain stable growth at mid +7% YoY range due to settlement of the impact of Goods and Services Tax (GST) which was introduced in July 2017 and the government's economic stimulus package. Australian economy will maintain gradual growth supported by a recovery in capital investment and an expansion of infrastructure investments amid ongoing accommodative monetary policy.

2. Outlook of each country and region

(1) China

The National People's Congress (NPC) in March voted to abolish term limits for the presidency (2 terms, 10 years), paving the way for a long-term rule by Xi administration. President Xi Jinping has clearly indicated the administration's focus on structural reforms such as supply-side structural reform and market-oriented reform with his vision of turning China into a strong power in mid-to-long term. However, considering that this year's target of real GDP growth rate is set around +6.5% YoY which is the same as last year, the administration will not allow deflationary pressure associated with structural reforms and the adverse effects of the intensifying US-China trade dispute to weigh on the economic growth rate and intends to avoid a substantial slowdown in economic growth with flexible policy management. With such stance of the administration in mind, economic growth rate is expected to maintain +6% YoY range although it will gradually slow down towards 2019.

We will look at the details below. In regards to reduction of production capacity, a main task of supply-side structural reforms, the NPC set the annual target of 30 million ton on steel (50 million ton in the previous year), 150 million ton on coal (same as the previous year) and 4 million kW on substandard, small-scale coal-fueled generation (50 million kW in the previous year), leaving some downward pressure on the investments though it may not be as much as the previous year. Furthermore, infrastructure investments, which have underpinned investments, have been unable to maintain growth of around +20% YoY that lasted for about five years (see chart 1). The number of pullout from or review of public-private partnership (PPP) projects has been increasing, reaching RMB 5 trillion in total amount by April under strict supervision by the central government who is concerned with growing debts held by local governments.

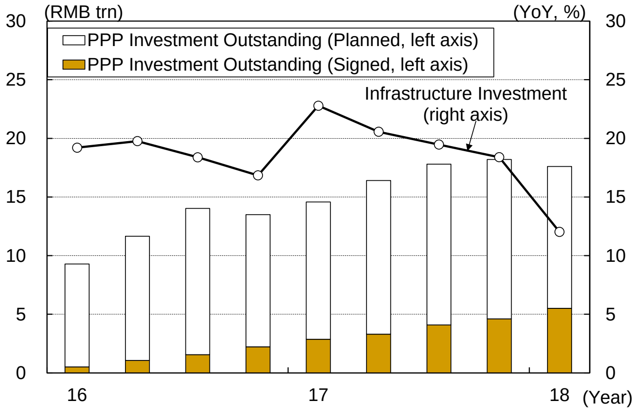
Nevertheless, slowdown in investments will be limited as the authorities give full consideration to achieve growth targets. First of all, the People's Bank of China (PBOC) said in April that reserve requirement ratios (RRRs) would be cut, for the first time in almost two years, by 100 basis points (bps). PBOC instructed financial institutions to use the newly-released funds from the reserve cut to pay back the central bank's medium-term lending facility (MLF) (900 billion yuan) first, then to enhance loans to small businesses (400 billion yuan). PBOC raised the interest rate on MLF itself (by 5 bps) and emphasized that monetary policy stance has been unchanged, however monetary easing effect to a certain extent can be expected. Secondly, as part of the supply side reform, the authorities have been trying to reduce corporate cost since 2016 to ease downward pressure on growth which is associated with reduction of excessive production capacity and debts. Furthermore, a new tax cut and reduction in utilities prices were introduced this year and those effects will be expected as well.

Real estate investment is expected to remain firm on the back of low level of housing inventory (39% below its peak level) and strong actual demand, although the current pace of double-digit increase is unlikely to sustain. In fact, although sales are sluggish in China as a whole, looking at the breakdown by areas, many, particularly in inland areas, are showing solid sales in major cities where supply has been restrained because strict guidance was imposed to set new home prices lower than market trend, some say demand itself is strong.

Private consumption will remain solid. Favorable employment and income environment with stable expansion of income and rise in jobs-to-applicants ratio has been unchanged. Corporates, particularly internet companies, have been implementing changes towards enhancing efficiencies and convenience in business dealings, including the use of artificial intelligence (AI) and big data. Furthermore, the government is preparing policy measures to expand consumption, mainly the one of IT equipment, according to media reports.

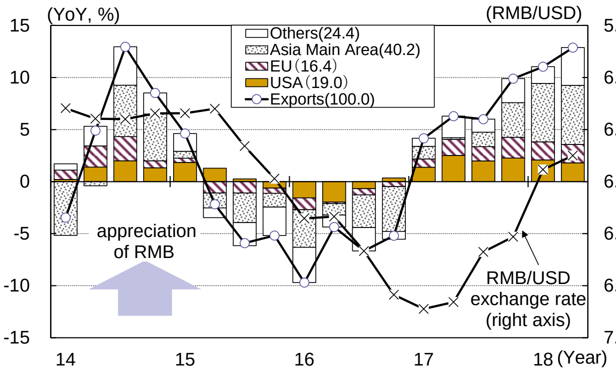
Exports will continue to increase steadily, assuming global economy continues to expand. Exports have been increasing recently at a faster pace than previous year, and positive effects of a rise in overseas demand surpassed adverse effects of an appreciation in yuan (see chart 2). Trade dispute with US, however, remains as a huge uncertainty. The government is using carrot-and-stick policy, emphasizing market opening measures such as easing restrictions on foreign investments into financial and auto sectors and import expansion including lowering tariffs while countering US tariff hike with equal scale of retaliatory tariff. US and China agreed,

Chart 1：China's Infrastructure & PPP Investment



Note: "Infrastructure Investment" shows year-to-date figures
Source: China Ministry of Finance, National Bureau of Statistics of China, MUFG Bank Economic Research Office

Chart 2: Exports by destinations in China (in USD)



Note: 1. ( ) next to countries/regions represents percentage of total (as of 2017).
2. "Asia Main Area" includes Japan, Hong Kong, Taiwan, South Korea, ASEAN and India.
3. Quarterly basis except for the latest (April) figure.
Source: China's General Administration of Customs, IMF, MUFG Bank Economic Research Office

through negotiations held twice in May, to buy more US agricultural and energy products to help narrow US trade deficit with China. Meanwhile US reiterated with an introduction of tariffs within the same month. Mounting pressure against China from US eyeing November’s midterm elections will bear close watching.

(2) Other Asian Economies

In Asian economies excluding China, stable growth will continue amid ongoing growth-friendly fiscal policy and accommodative monetary policy as domestic demand remains solid, in addition to export expansion and the positive effects arising from it. The pace of increase in exports will slow down towards 2019 as growth rate of advanced economies will gradually return to the level close to the potential growth rate as macro demand-supply balance tightens. However, moderate increasing trend will be maintained. An increase in exports will contribute to growth directly, and also boost growth rate through spillover effects to other expenditures. Specifically, high level of corporate earnings as a result of export increase will lead to an expansion of private investment and an increase in household income, then to an expansion of private consumption.

Governments in the region have already been implementing fiscal management which focuses on low-income groups, employment and infrastructure investments. In Malaysia, where the opposition coalition won the the lower house election in May which brought the first change of government ever, the abolishment of the Goods and Services tax (GST): zero-rated from June which was announced by Mahathir administration is expected to boost private consumption in the near term. In regards to monetary policy, more central banks in Asia have raised interest rates due to an improvement of economic outlook, a rise in inflation and greater pressure on decline in currency value. However, this will not be a huge obstructive factor to economic expansion as policy rates in those countries/regions are still historically accommodative level.

Although there has been a growing concern over massive capital outflow from and currency depreciation in emerging countries as a result of US interest rate hike and appreciation in the dollars, if you look at Asian countries/regions only, currency depreciation is limited and no sign of movements which could lead to currency crisis (see table 2). This is because fundamentals such as current account balance and foreign debts have been improved than in the past, and appropriate responses have been taken with regards to monetary and fiscal policies. Meanwhile, in Latin American countries, such as Argentina whose currency has been sold off relatively heavily, and Turkey, an improvement in fundamentals has been delayed and political uncertainties are high prior to presidential elections ahead. Going forward, monetary policies in Asia will head to gradual tightening stance in accordance with the movement towards monetary policy normalization in US. However, owing to such appropriate responses, massive capital outflow or sharp currency depreciation is likely to be averted.

Table 2 : Fundamentals and Currency Performance of Major Emerging Economies

	Current Account (% of GDP)		External Debt (% of GDP)		Foreign Reserve to shot-term debt (times)		Change in exchange rates (from 18 April to 29 May, %)
	1997	2017	1997	2017	1997	2017	
China	3.8	1.3	13.7	14.0	4.5	3.1	-2.3
South Korea	-1.8	5.1	29.1	27.4	0.3	3.3	-0.8
Indonesia	-2.3	-1.7	60.6	34.7	0.5	2.6	-1.6
Malaysia	-5.3	3.0	46.7	65.3	1.4	1.2	-2.4
Thailand	-2.9	10.6	72.1	32.7	0.7	3.1	-2.9
Philippines	-4.8	-0.8	47.3	23.3	0.6	5.1	-1.1
Vietnam	-5.7	2.9	81.0	42.4	0.8	2.6	-0.2
India	-0.7	-1.5	25.1	20.4	4.9	4.0	-3.4
Argentina	-3.9	-4.8	39.6	36.5	0.7	0.9	-23.5
Brazil	-3.5	-0.5	22.6	15.4	1.5	7.2	-10.3
Mexico	-1.6	-1.6	31.0	36.5	1.0	3.3	-9.7
Turkey	-1.0	-5.6	33.3	53.2	1.0	0.7	-13.4
Russia	-0.2	2.6	42.0	33.0	2.1	6.9	-3.3
【cf.】USD Nominal Effective Exchange Rate Index (from 18 April to 29 May, %)							4.3

Note: 1) Shadowed portion indicates an improvement from 1997.
2) Figures for Vietnam's External Debt is as of the end of 2016.
Source: IMF, World Bank, MUFG Bank Economic Research Office

[Thailand]

Thai economy remains solid. Real GDP growth accelerated to + 4.8% YoY in Jan-Mar (previous quarter: + 4.0% YoY), recording the highest level in five years (see chart 3). Private consumption remained firm, and capital investments by state-owned enterprises (such as purchasing aircrafts) as well as an expansion of housing and infrastructure investments also contributed to boost growth rate.

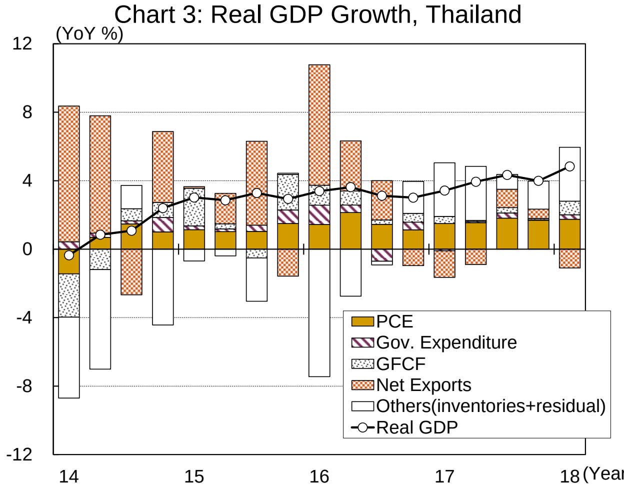
Looking ahead, an improvement of corporate earnings as a result of export expansion will boost capital investment and make a positive contribution to private consumption through an increase in household income, and the economy will continue to grow at a moderate pace. Acceleration of investments by implementing the infrastructure investment project (of total THB 1 trillion) on expansion of international airports, construction of high-speed railways between major airports, and port maintenance in Eastern Economic Corridor (EEC) in the three Eastern provinces will also support the economic expansion.

(3) Australia

Australian economy is continuing its gradual recovery. Private consumption remains solid backed by an improvement in employment and income environment and ongoing low-interest rates (see chart 4). Investments have been supported by a recovery in private non-mining sector while housing sector is showing a sluggish growth.

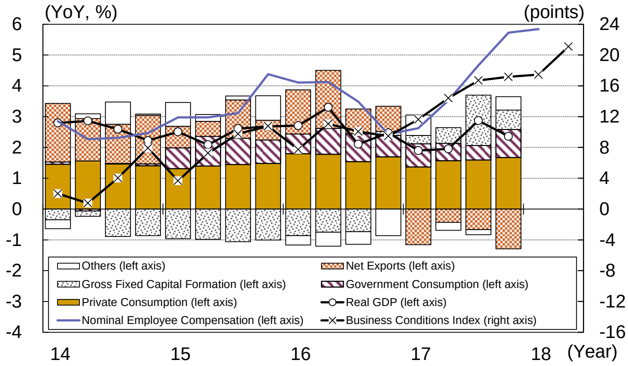
Looking ahead, private consumption is likely to continue its gradual recovery on the back of ongoing low-interest rates and income tax reduction (AUD 13.4 billion in four years). Considering that exports will maintain increasing trend due to global economic expansion and new liquefied natural gas (LNG) projects and an expected recovery in capital investments in private non-mining sector on the back of an improvement in corporate earnings and business conditions, the economy is likely to continue to expand at a moderate pace. In addition, the AUD 75 billion infrastructure projects to invest in building roads and railways over the next 10 years will support the economy.

Chart 3: Real GDP Growth, Thailand



Source: NESDB, MUFG Bank Economic Research Office

Chart 4: Real GDP Growth, Employee Compensation and Business Conditions in Australia



Note: "Nominal Employee Compensation" is multiplication of number of employees by wage per week.

Source: Australian Bureau of Statistics, National Australia Bank, MUFG Bank Economic Research Office

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