The AMRO Inaugural Flagship Report: ASEAN+3 Regional Economic Outlook 2017

4 May 2017, Yokohama, Japan
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
Chapters

I. ASEAN+3 Macroeconomic Prospects and Challenges

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

AMRO’s Baseline Growth and Inflation Projections

<table>
<thead>
<tr>
<th></th>
<th>‘16</th>
<th>‘17 p/</th>
<th>‘18 p/</th>
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<tbody>
<tr>
<td>China</td>
<td>6.7</td>
<td>6.5</td>
<td>6.3</td>
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<tr>
<td>Japan (FY)</td>
<td>1.4</td>
<td>1.3</td>
<td>1.1</td>
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<td>Korea</td>
<td>2.8</td>
<td>2.5</td>
<td>2.6</td>
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<td>ASEAN-4 &amp; VN</td>
<td>5.0</td>
<td>5.1</td>
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<tr>
<td>BCLM</td>
<td>5.6</td>
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<td>HK &amp; SG</td>
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<tr>
<td>ASEAN+3</td>
<td>5.3</td>
<td>5.2</td>
<td>5.1</td>
</tr>
</tbody>
</table>

Source: National authorities, AMRO

p/ Projections
The recent recovery in global trade, if sustained, could provide some upsides to regional exports and growth.
In China, growth continues along a moderating trend, while the rebound in producer prices supported the recent improvement in private sector profits and investment.

China: Real GDP Growth

China: Private Sector Profits and Investment

% yoy, 3mma

Source: NBS, AMRO

p/ Projections
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

p/ Projections
Source: Cabinet Office, JMOF, BOJ, 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.
So far, talks about U.S. fiscal stimulus and concerns about foreign capital flowing back to the U.S. have not translated into sustained increase in local currency sovereign bond yields.

Selected Regional 10Y Sovereign Bond Yields vs. 10Y U.S. Treasury Yields

Source: Reuters
Potential escalation of global uncertainties could amplify the financial stability risks of regional economies with large external financing needs, and where vulnerabilities have built up from sustained high private sector credit growth.

**Risks: Financing and Turning of the Credit Cycle**

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

The region’s FX buffer remains adequate by conventional metrics, policy room has generally narrowed across the region.

FX Reserves (in Months of Imports)

FX Reserves / Short-Term External Debt Ratio

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 staff calculations.

Source: National Authorities, AMRO ERPD Matrix
Leveraging Regional Integration

On a positive note, the region has become an important source of final demand, benefiting from the growing regional integration, as well as the 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

Source: COMTRADE, OECD, AMRO
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.

Source: ASEAN Investment Report 2016
Despite better fundamentals, some regional policymakers will face a sharper trade-off between growth and financial stability objectives, at a time when policy space is narrowing, or constrained.

**Monetary Policy / Macroprudential Policy**

- Tightening global monetary conditions in 2017 and rising inflation will constrain regional economies’ use of monetary policy to support growth.
- Constraints most apparent in economies where financial vulnerabilities have built up.
- Targeted macroprudential policy measures can help to safeguard financial stability.

**Fiscal Policy**

- Fiscal policy may have to play a greater role to support the economy, although policy space has generally narrowed, and in some economies, is constrained by fiscal rules.
- In economies with weaker fiscal position, reprioritizing and rebalancing existing expenditure programs should be the first steps pursued.
Chapters

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

Real GDP: ASEAN-4 and Korea

Source: National Authorities, AMRO
<table>
<thead>
<tr>
<th>Feature</th>
<th>After AFC</th>
<th>After GFC</th>
</tr>
</thead>
<tbody>
<tr>
<td>What led the recovery?</td>
<td>Exports</td>
<td>Domestic demand</td>
</tr>
<tr>
<td>Level of Investment</td>
<td>Fell and remained below trend</td>
<td>Remained largely unchanged</td>
</tr>
<tr>
<td>Capital flows</td>
<td>Did not return immediately</td>
<td>Returned immediately</td>
</tr>
<tr>
<td>China</td>
<td>Led the surge in intra-regional exports</td>
<td>Rebalancing towards more domestic consumption</td>
</tr>
<tr>
<td>Japan</td>
<td>Retrenchment of Japanese banking flows from Asia</td>
<td>Increase in Japanese bank flows to Asia</td>
</tr>
<tr>
<td>Share of China, Korea and Japan in ASEAN’s</td>
<td>Accounts for around 18% of ASEAN trade in 1999</td>
<td>Share increased to 31%</td>
</tr>
<tr>
<td>total trade</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Productivity growth</td>
<td>Healthy growth via technology</td>
<td>Moderated</td>
</tr>
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</table>
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

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<th>Source</th>
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<th>2014</th>
<th>2015</th>
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<td>4.9</td>
<td>3.1</td>
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<td>Korea</td>
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<td>4.2</td>
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<td>ASEAN-4 &amp; SG</td>
<td>19.1</td>
<td>11.2</td>
<td>14.9</td>
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<td>Lao PDR</td>
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<td>7.0</td>
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<tr>
<td>Myanmar</td>
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<td>30.2</td>
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<td>16.4</td>
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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
Theme: 20 Years after the Asian Financial Crisis (AFC)

Lessons from the AFC

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.

• In the current uncertain global environment, the AFC continues to offer valuable lessons to policymakers.
Theme: 20 Years after the Asian Financial Crisis (AFC)

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)

Note: Data for Myanmar are not available
Source: World Bank
Recap: Key Messages

1. Growth to be sustained in 2017-18 (about 5%), with upside from exports.

2. Outlook clouded by tightening global financial conditions, trade protectionism and policy uncertainties.

3. Policy priorities – Maintaining short term macroeconomic stability, while supporting longer term reforms.

4. AFC shaped policymakers’ perspectives on crisis management and resolution – AMRO and CMIM established.

5. Post-AFC, policy attention shifted to capital flows and contagion risks – the need for flexible policy framework.

6. Openness to trade and FDI enabled the region the reap the benefits from the growing regional trade integration, and the rise of China.

7. 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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