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

**ASEAN+3 Macroeconomic Research Office (AMRO)**

Singapore

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This Monthly Update of the AREO was prepared by the Regional Surveillance team and approved by Dr Khor Hoe Ee (Chief Economist).

The analysis in this report is based on information available up to 5 June 2018. For the sake of brevity, “Hong Kong, China” will be referred to as “Hong Kong” in the text and figures.

## Global Economic Developments

**In the ASEAN+3 Regional Economic Outlook (AREO) 2018 published in May, we assess that the risks faced by the region are mostly external, as summarized in AMRO's Global Risk Map (Annex 1).** The main near-term risks are:

(i) A faster-than-expected tightening in global financial conditions; and

(ii) An escalation of global trade tensions from the imposition of tariffs by the U.S.

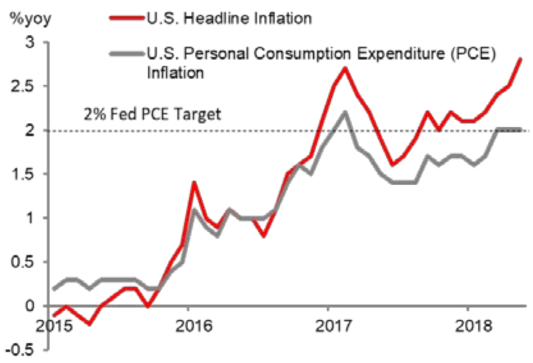
Tail risks of low likelihood include geopolitical risks in the near term and a sharper-than-expected slowdown in China's economy in the medium term.

With PCE inflation in the U.S. reaching the Fed's 2 percent target in March 2018 (Figure 1), the Fed has continued its path of rate hikes, with markets widely expecting the second Fed rate hike this year in the FOMC meeting on 12-13 June. Inflation has increased further to 2.8 percent in May reflecting the robust U.S. economy, with job gains in the labor market and the unemployment rate staying low at 3.8 percent in April.

10-year U.S. Treasury yields broke the 3 percent level in late April, on the back of the robust economy, boosted by the fiscal tax stimulus from the beginning of this year. Rising yields have also pulled up the U.S. dollar (Figure 2). Global financial conditions are set to tighten further.

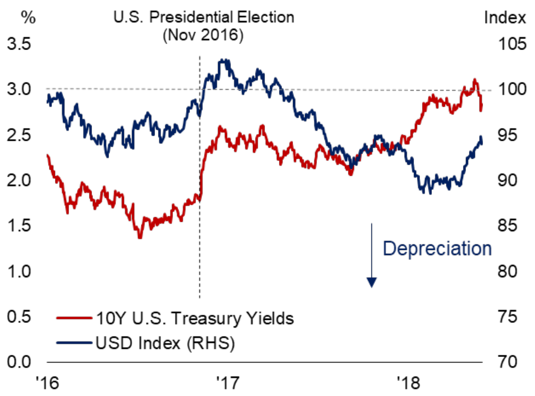
**Rising U.S. yields and an appreciating U.S dollar have prompted capital outflows from some emerging market economies that are seen by investors as vulnerable, including Turkey and Argentina, which increased policy rates to defend their currencies.** Turkey hiked interest rates by 300 basis points on 23 May in response to its currency losing 12 percent of its value since mid-April. On 4 May, Argentina raised its benchmark interest

**Figure 1 U.S. inflation has picked up to reach the Fed's 2% target**




Source: Bloomberg

**Figure 2 Global financial conditions are tightening with rising U.S. yields and an appreciating dollar**




Source: CEIC

rates three times in a span of one week, from 27.25 percent to 40 percent, in order to defend the peso. In early June, Argentina and the IMF reached an agreement on a 36-month Stand-By Arrangement (SBA) amounting to USD50 billion.

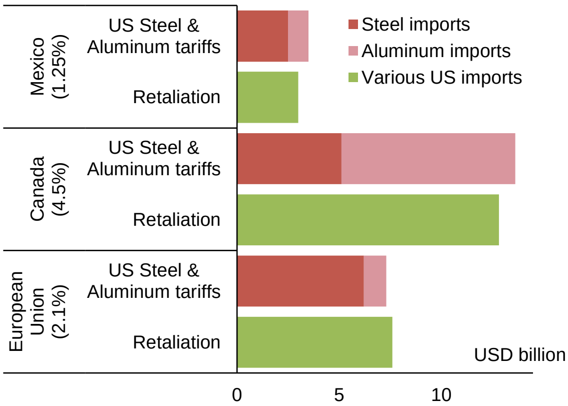
**An escalation of global trade tensions continues to be a risk weighing on global growth performance, affecting business sentiment in targeted countries including in Europe and in NAFTA.** The U.S. imposition of tariffs on steel and aluminium imports from Canada, Mexico and the E.U., with the exemption expiring on 1 June, has attracted retaliatory tariffs from these countries on their U.S. imports (see Figure 3, and Annex 2 for a chronology of U.S. trade actions since January). While the tariffs are still imposed only on a small proportion of U.S. and its trading partners' exports (less than 5 percent), the risk of successive rounds of retaliation weighs on global trade and economic prospects.

## Regional Economic Developments

**Emerging markets in the region, while experiencing capital outflows similar to other regions, remain relatively resilient (Figure 4).** After the global market sell-off in February this year, the region is still receiving bond inflows but are experiencing net outflows from the equity markets. Regional currencies, due to the appreciation of the U.S. dollar, have depreciated in past weeks but by less than those in Latin America (Figure 5).

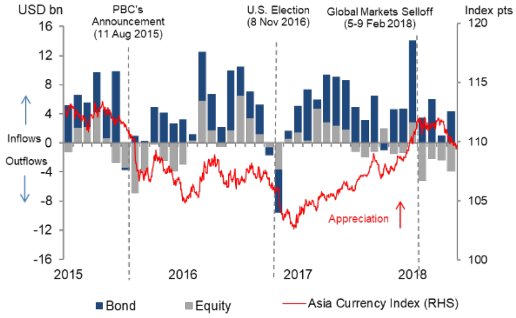
**So far, markets have continued to differentiate between other emerging markets and those in our region, based on better economic fundamentals in our region.** Overall growth in the region remains strong in Q1 2018 (Annex 3), generally supported by domestic demand and exports. The Philippines, Thailand and Singapore reported faster growth in Q1 2018, while growth in China was 6.8 percent year on year in Q1 2018,

**Figure 3 U.S. tariffs have attracted retaliation from its trading partners**



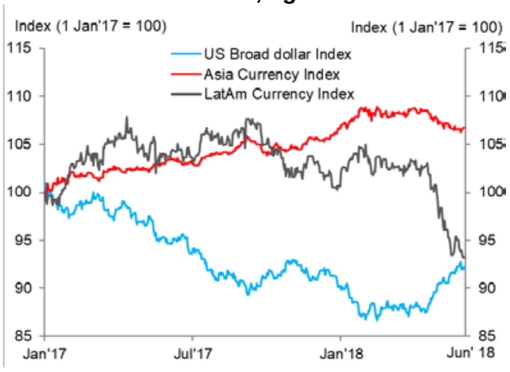

Note: Percentages in parentheses denote the country's steel and aluminum exports to the U.S. as a percentage share of country's total exports to the U.S.
Source: USITC

**Figure 4 Emerging markets are starting to feel the pressure with capital outflows prompted by tightening global financial conditions**




Note: Data, as of May 2018. refer to Indonesia, Malaysia, the Philippines, Thailand and Korea. The Bloomberg Asia currency index consists of currencies from China, Hong Kong, China, India, Indonesia, Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand against USD.
Source: National Authorities, Bloomberg

**Figure 5 In the past weeks, Asian currencies have depreciated less than those in Latin America, against the USD**




Source: Bloomberg, JP Morgan

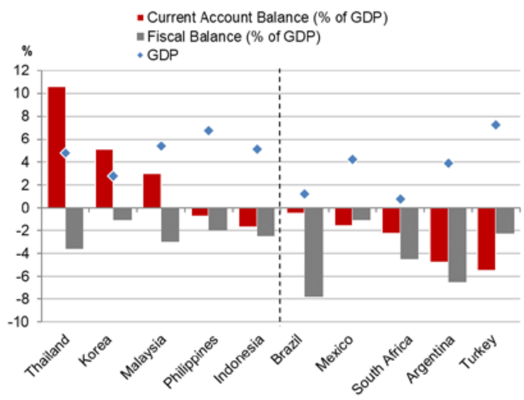
unchanged from the previous quarter. The region is also seen to be in a better position in terms of its current account and fiscal balances (Figure 6).

**While low inflation has generally afforded economies in the region some monetary policy space (Figure 7), some economies have already begun tightening** in May in response to external developments. Indonesia raised interest rates by 25 basis points twice in May to maintain stability, while the Philippines increased its policy rate by 25 basis points in order to contain inflationary pressures (Annex 5). The Malaysian stock market saw some capital outflows and the ringgit depreciated because of the unexpected result of the general elections in early May, but this was short-lived. With tightening global financial conditions, however, further bouts of volatility can be expected and the region should remain vigilant.

**U.S. trade protectionist actions continue to weigh on the region's trade outlook.** Trade tensions remain elevated as China's imports continue to be targeted by the Trump administration. With global supply chain networks linking the region to China, the impact on the region would depend on specific sectors that are targeted. For China's major exports of electronics, machineries and autos to the U.S., the degree of value-add sourced from Japan, Korea and the ASEAN differs, ranging from 8 percent of total value-added in machineries to 23 percent in electronics (Figure 8).

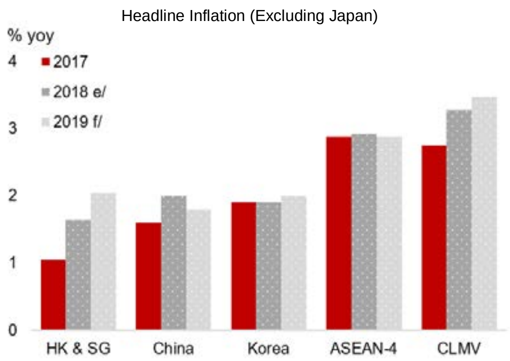
China's response to the U.S. trade actions has been measured, and trade discussions between the U.S. and Chinese authorities have attenuated the immediate risk of escalating trade tensions thus far. However, this remains a risk for the region to watch closely. Annex 2 summarises U.S. trade actions from January onwards towards its major trading partners.

**Figure 6 The region's resilience stems from its stronger economic fundamentals**



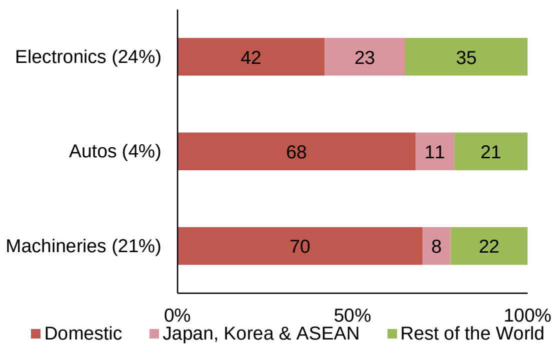

Note: Data as of 2017 for comparison purposes.
Source: National Authorities, IMF

**Figure 7 While external developments have prompted monetary tightening, low inflation continues to afford some monetary policy space**



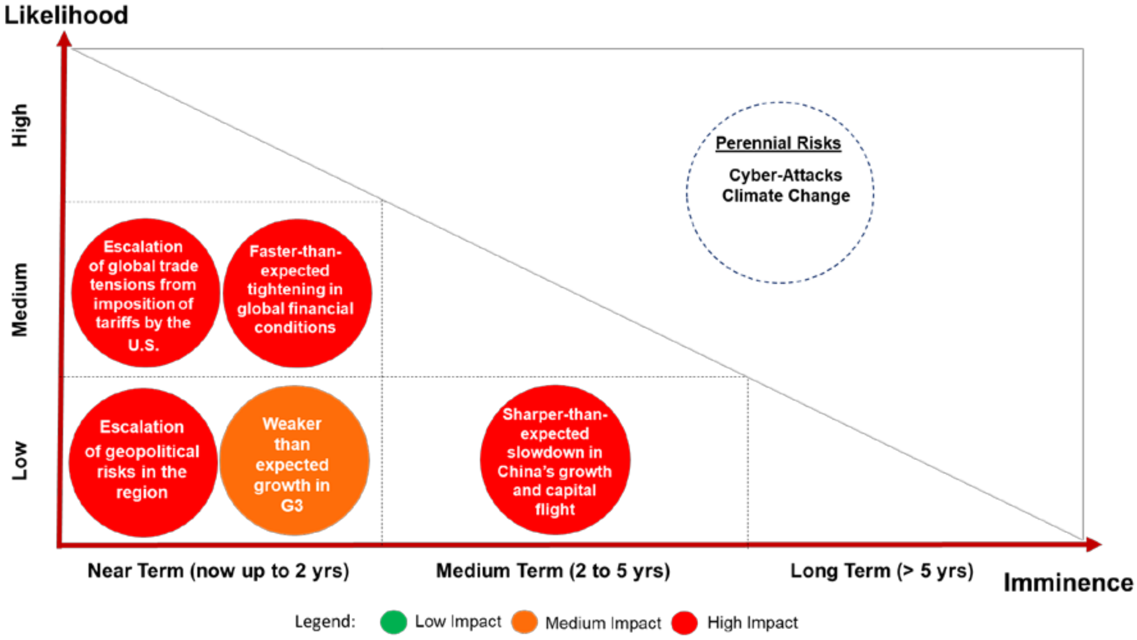

Source: National Authorities, AMRO estimates

**Figure 8 The impact on the region from U.S. tariffs on China would depend on specific sectors that are targeted**




Note: Figure in the bar refers to the proportion of value-added by origin into China's exports in those sectors, with "domestic" referring to value-added from China. The percentage in parenthesis refer to share of China's exports to the U.S.
Source: OECD, AMRO staff estimates

## Annex 1: AMRO Global Risk Map



## Annex 2: Chronology of U.S. Trade Actions in 2018

**Section 201: Trade Investigation into Washing Machines and Solar Panels Imports**

| Date | Details |
|---|---|
| 22 January | Announcement of global safeguard tariffs on imported washing machines (20 percent) and solar panels (30 percent) on USD 8.5 billion and USD 1.8 billion worth of washing machines and solar panels respectively. |
| 5 February | China initiates antidumping duty investigations on U.S. sorghum imports worth USD 1 billion. |
| 17 April | China announces tariffs of 178.56 percent on U.S. sorghum imports. |
| 18 May | China's tariffs on sorghum officially ended. |

**Section 232: Trade Investigation into Steel and Aluminium Imports**

| Date | Details |
|---|---|
| 1 March | Announcement of Section 232 tariffs on steel and aluminium based on national security considerations. Tariffs imposed on imported steel (25 percent) and aluminium (10 percent) on all trading partners, covering an estimated USD 48 billion of imports. |
| 22 March | Temporary exemptions granted to the EU, Canada, Mexico, Brazil, Argentina and Australia. |
| 23 March | China imposes tariffs on 128 U.S. products including steel pipes, fruit, wine, pork and aluminium worth USD 2.4 billion, in response to tariffs on Chinese steel and aluminium worth USD 2.8 billion. |
| 25 March | Korea receives permanent exemption, in return for self-imposing a steel quota of 2.68 million tons, cutting its shipment by 21.2 percent from 2017. |
| 1 June | The U.S. ends temporary steel and aluminium exemptions for the E.U., Canada and Mexico. Canada's exports will be most affected by these tariffs (USD 13.4 billion), followed by the European Union (USD 7.3 billion) and Mexico (USD 3.6 billion). All 3 countries announced planned retaliatory responses:<br>− Canada and Mexico also imposed tariffs on U.S. steel, aluminium and a range of consumer goods worth USD 12.8 billion and USD 3 billion, respectively<br>− European authorities are weighing plans to impose tariffs on U.S. imports worth approximately USD 3.3 billion, and a second batch worth USD 4.3 billion after 3 years. |

**Section 301: Trade Investigation into China's Trade Practices**

| Date | Details |
|---|---|
| 22 March | Announcement of trade investigations findings based on the Section 301 China's trade practices related to technology transfer, innovation and intellectual property, which proposes tariffs on more than 1,300 China technology imports worth USD 50 billion. |
| 4 April | Release of USTR 301 proposed list of products under consideration, which proposes 25 percent tariffs on 1,300 China products worth USD 50 billion. |
| 4 April | China responds with its own list of U.S. imports that is potentially subject to 25 percent tariffs. 106 U.S. products are listed, including U.S. soybeans, cars, chemicals and planes worth USD 50 billion. |
| 6 April | President Trump instructs USTR to consider tariffs on an additional USD 100 billion imports. |
| 20 May | U.S. Secretary Steven Mnuchin announces that the tariffs on China's imports were "on hold". |
| 29 May | U.S.announces plan of resuming tariffs on USD 50 billion worth of imports from China. |

| | |
|---|---|
| 5 June | China intends to purchase nearly USD 70 billion worth of U.S. agricultural and energy goods if the U.S. rolls back tariffs, based on unofficial sources. |
| 15 June (tentative) | Conclusion of 60 day public consultation on tariff list and potential implementation of tariffs. |

**Section 232: Trade Investigation into Auto Imports**

| Date | Details |
|---|---|
| 23 May | Launch of Section 232 trade investigations into auto imports based on national security considerations. President Trump is considering implementing 25 percent tariffs on auto-related imports such as automobiles, SUVs, vans, trucks and auto-parts worth USD 290 billion. |

## Annex 3: Annual GDP Growth Figures for ASEAN+3 Economies

| Economy | Annual GDP Growth, % y-o-y | | | | | | |
|---|---|---|---|---|---|---|---|
| | 2016 | 2017 | 1Q'17 | 2Q'17 | 3Q'17 | 4Q'17 | 1Q'18 |
| China | 6.7 | 6.9 | 6.9 | 6.9 | 6.8 | 6.8 | 6.8 |
| Hong Kong | 2.0 | 3.8 | 4.4 | 3.9 | 3.6 | 3.4 | 4.7 |
| Japan | 0.9 | 1.6 | 1.4 | 1.6 | 2.0 | 1.9 | 1.1 |
| Korea | 2.8 | 3.0 | 2.9 | 2.8 | 3.8 | 2.8 | 2.8 |
| Brunei | -2.5 | 1.3 | -1.3 | 0.2 | 1.3 | 5.2 | - |
| Indonesia | 5.0 | 5.1 | 5.0 | 5.0 | 5.1 | 5.2 | 5.1 |
| Malaysia | 4.2 | 5.9 | 5.6 | 5.8 | 6.2 | 5.9 | 5.4 |
| Philippines | 6.9 | 6.7 | 6.5 | 6.6 | 7.2 | 6.5 | 6.8 |
| Singapore | 2.0 | 3.6 | 2.5 | 2.8 | 5.5 | 3.6 | 4.4 |
| Thailand | 3.3 | 3.9 | 3.4 | 3.9 | 4.3 | 4.0 | 4.8 |
| Vietnam | 6.2 | 6.8 | 5.2 | 6.3 | 7.5 | 7.7 | 7.4 |

Source: National Authorities, Bloomberg, CEIC
* Data released as of 5 June 2018

## Annex 4: Global Manufacturing PMI Heatmap

| Economies | Change from Prev Month |
|---|---|
| **Global** | -0.4 |
| **Developed Markets** | -0.4 |
| U.S. | -0.1 |
| U.K. | 0.5 |
| **Eurozone** | -0.7 |
| Austria | -0.7 |
| France | 0.6 |
| Germany | -1.2 |
| Greece | 1.3 |
| Ireland | 0.1 |
| Italy | -0.8 |
| Netherlands | -0.4 |
| Spain | -1.0 |
| **Emerging Markets** | -0.2 |
| Brazil | -1.6 |
| India | -0.4 |
| Russia | -1.5 |
| South Africa* | -0.7 |
| China | 0.0 |
| Hong Kong* | -1.3 |
| Japan | -1.0 |
| Korea | 0.5 |
| **ASEAN** | 0.5 |
| Indonesia | 0.1 |
| Malaysia | -1.0 |
| Philippines | 1.0 |
| Singapore* | 1.2 |
| Thailand | 1.6 |
| Myanmar | -2.9 |
| Vietnam | 1.2 |

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 5: Major Policy Developments (7 May – 5 June 2018)

| | |
|---|---|
| **China** | [22 May 2018] China will cut import tariffs on cars and auto parts. Import tariffs will be cut to 15 percent from 25 percent for most vehicles from July 1. Lowering auto import tariffs is a major step for China to further expand its reform and opening-up.<br><br>[24 May 2018] The currency swap arrangement between State Bank of Pakistan (SBP) and People's Bank of China (PBOC) has been extended for a period of 3 years in respective local currencies.<br><br>[1 June 2018] In order to further support SMEs and the "green economy", and to develop the credit bond market, the People's Bank of China decided to increase eligible collaterals pool appropriately for medium-term loan facility (MLF). The additional collateral pool includes: AA-class SME, green and "agricultural" financial bonds, and AA+ and AA corporate credit bonds (priority for bonds involving SMEs and the green economy, high-quality SME loans and green loans. |
| **Korea** | [24 May 2018] The Monetary Policy Board of the Bank of Korea decided to maintain the Base Rate unchanged at 1.5 percent. |
| **Indonesia** | [18 May 2018] Bank Indonesia (BI) decided today to increase its policy rate – BI 7 day reverse repurchase rate or BI7DRR rate – by 25 basis points to 4.50 percent. BI mentioned that monetary policy would be prioritized toward maintaining stability amid growing global challenges.<br><br>[30 May 2018] Bank Indonesia raised the BI 7-day reverse repo rate by another 25 basis points to 4.75 percent. According to BI statement, the rate hike is "pre-emptive, front-loading and ahead-of-the-curve" in response to expectations of higher US interest rates. |
| **Malaysia** | [10 May 2018] The Bank Negara Malaysia (BNM) decided to maintain the overnight policy rate (OPR) at 3.25 percent. The decision to maintain the OPR came amid headline inflation and core inflation decelerating to 1.3 percent and 1.7 percent, respectively, in March.<br><br>[1 June 2018] The 6 percent Goods and Services Tax (GST) was reduced to 0 percent and would be replaced by a Sales and Services Tax (SST) in September. |
| **Philippines** | [10 May 2018] Bangko Sentral ng Pilipinas (BSP) announced a 25 bps hike in the policy rate to 3.25 percent. The rate hike was deemed necessary by BSP since latest forecasts for inflation have shifted higher, with inflation being broad-based for the policy horizon. |
| **Singapore** | [12 May 2018] The Autoriti Monetari Brunei Darussalam (AMBD) and the Monetary Authority of Singapore (MAS) signed a FinTech Cooperation Agreement (CA) to |

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|---|---|
| | foster innovation in financial services between Brunei Darussalam and Singapore. The FinTech CA will facilitate the sharing of information on emerging FinTech trends and developments, and promote joint innovation projects between both countries. It will also establish a framework for both authorities to provide support for FinTech companies to better understand the regulatory regime and opportunities in each jurisdiction.<br><br>[21 May 2018] The Bank of Japan (BOJ) and the Monetary Authority of Singapore (MAS) renewed the existing Bilateral Swap Arrangement (BSA). Under the terms of the Arrangement, Singapore can swap Singapore dollars for up to USD 3 billion or its equivalent in Japanese yen from Japan. Japan can swap Japanese yen for up to USD 1 billion from Singapore. |
| **Thailand** | [16 May 2018] The Bank of Thailand (BOT) decided to maintain the policy rate of 1.5 percent. The decision to maintain the policy rate came amid economic growth gaining traction and inflation inching up at a gradual pace. |