EAST ASIA UPDATES

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# Southeast Asia recorded 4.7% growth in Q1 2017

Major Association of Southeast Asian Nations (ASEAN) countries (Indonesia, Malaysia, Philippines, Singapore, Thailand, and Viet Nam) recorded an average growth of 4.7% in Q1-2017 (Table 1).

In Q1 2017 growth of the ASEAN countries is generally driven by improvements in the external sector, as manifested through higher exports, robust manufacturing activity, and healthy private consumption. Furthermore, the increasing exports of Southeast Asian countries are also having a positive effect on their current account balances and international reserve levels (Table 1). These positive developments provide greater optimism regarding the structural reforms that are being undertaken in these countries and provide their governments with greater legitimacy to continue the reforms.

**Table 1. Selected East Asian Countries' GDP Growth, Ratio of Current Account to GDP, and Foreign Reserves**

| | Country | Q4 2016 | Q1 2017 | 2017e |
|---|---|---|---|---|
| **Australia** | GDP Growth (%, YoY) | 2.4 | 1.7 | 2.7 |
| | CA/GDP (%) | -0.9 | -0.8 | -2.3 |
| | International Reserves (import cover, months) | 2.6 | 2.9 | 2.4 |
| **China** | GDP Growth (%, YoY) | 6.8 | 6.9 | 6.6 |
| | CA/GDP (%) | 0.4 | 0.7 | 1.5 |
| | International Reserves (import cover, months) | 19.1 | 19.1 | 16.7 |
| **India** | GDP Growth (%, YoY) | 7.0 | 6.1 | 7.2 |
| | CA/GDP (%) | -1.4 | | -1.1 |
| | International Reserves (import cover, months) | 9.1 | 9.4 | 8.5 |
| **Indonesia** | GDP Growth (%, YoY) | 4.9 | 5.0 | 5.2 |
| | CA/GDP (%) | -0.9 | -1.0 | -1.6 |
| | International Reserves (import cover, months) | 8.8 | 9.2 | 8.8 |
| **Japan** | GDP Growth (%, YoY) | 1.7 | 1.6 | 1.1 |
| | CA/GDP (%) | 2.9 | 4.3 | 4.0 |
| | International Reserves (import cover, months) | 19.1 | 19.8 | |
| **Malaysia** | GDP Growth (%, YoY) | 4.6 | 5.6 | 4.3 |
| | CA/GDP (%) | 3.8 | 1.6 | 3.0 |
| | International Reserves (import cover, months) | 6.3 | 6.4 | 5.9 |
| **New Zealand** | GDP Growth (%, YoY) | 3.5 | | 3.1 |
| | CA/GDP (%) | -3.3 | | -3.1 |
| | International Reserves (import cover, months) | 4.5 | 4.7 | 4.3 |
| **Philippines** | GDP Growth (%, YoY) | 6.6 | 6.4 | 6.5 |
| | CA/GDP (%) | -1.2 | | 0.4 |
| | International Reserves (import cover, months) | 9.5 | 9.5 | 9.0 |
| **Republic of Korea** | GDP Growth (%, YoY) | 2.4 | 2.9 | 2.9 |
| | CA/GDP (%) | 7.1 | 5.3 | 6.0 |
| | International Reserves (import cover, months) | 8.9 | 9.0 | 7.9 |
| **Singapore** | GDP Growth (%, YoY) | 2.9 | 2.5 | 2.3 |
| | CA/GDP (%) | 16.9 | 18.4 | 19.8 |
| | International Reserves (import cover, months) | 6.8 | 7.2 | 6.8 |
| **Thailand** | GDP Growth (%, YoY) | 3.0 | 3.3 | 3.8 |
| | CA/GDP (%) | 9.3 | 12.3 | 11.0 |
| | International Reserves (import cover, months) | 9.4 | 9.8 | 9.3 |
| **Viet Nam** | GDP Growth (%, YoY) | 6.7 | 5.1 | 6.3 |
| | CA/GDP (%) | | | -0.6 |
| | International Reserves (import cover, months) | 2.5 | | 2.3 |

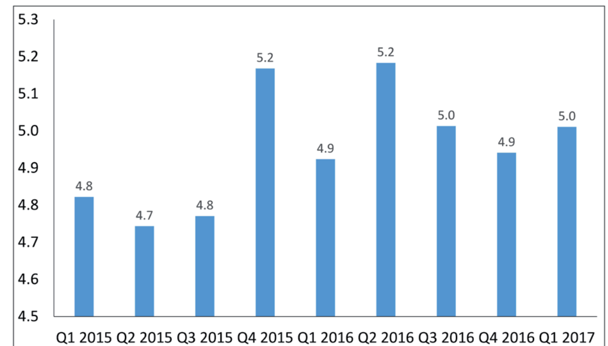
Source: Each Country Statistics Office and Central Bank, via CEIC.
Note: Estimated 2017 and international reserves data are taken from Economist Intelligence Unit, 2017.

# INDONESIA

Indonesia's credit rating has just been upgraded by S&P Global Ratings from BB+ since April 2011 to BBB- in May 2017 with stable outlook. The improvement is due to positive achievements manifested by more effective expenditure and revenue management that stabilizes Indonesia's public finance conditions. Robust growth of 5.0% in Q1 2017 (Figure 1), and a strong export performance of 21% year-on-year growth in Q1 2017 provide the Indonesian economy with a further boost.

The improvement of Indonesia's credit rating (Fitch's rating has been BBB since December 2011 and Moody's Baa3 since January 2012) will have a positive impact on the Indonesian economy as it will mean lower risk premiums, which will reduce the government bond coupon rate. In the longer run, Indonesian companies are expected to benefit from easier access to funding due to lower risk. Not only corporations will benefit directly from the improvement of the nation's credit rating through the debt market; the stock market also has been bullish, achieving a record high of 5,791 on 19 May 2017 just after the announcement was made.

**Figure 1. Indonesia GDP Growth (%, YoY)**



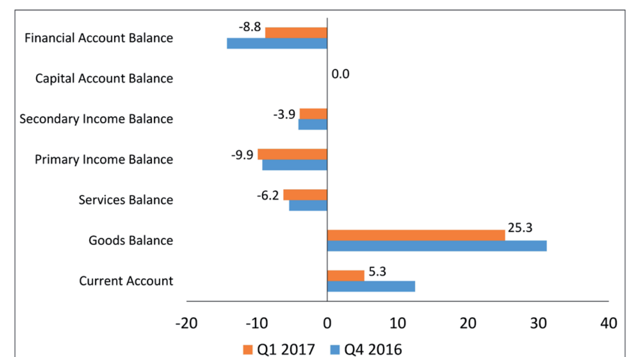

Source: Statistics Indonesia, 2017.

# MALAYSIA

The Malaysian economy grew by 5.6% in Q1 2017, the fastest quarterly year-on-year growth in the past 2 years, driven by robust export growth of 21% and strong private consumption growth of 6.6%. The strong growth in Q1 2017 was driven by the services sector growth, which grew by 5.8%, and manufacturing, which rose by 5.6%, while the agriculture, forestry, and fishery sectors saw the strongest growth at 8.3%.

Looking at Malaysia's external sector, its current account surplus narrowed in Q1 2017 compared with Q1 2016, due to robust import growth and a widening deficit in the services trade balance (Figure 2). Malaysia's current account surplus is expected to expand again as the increase in commodity prices is expected to be prolonged.

**Figure 2. Malaysia Balance of Payment by Source (in bn MYR)**

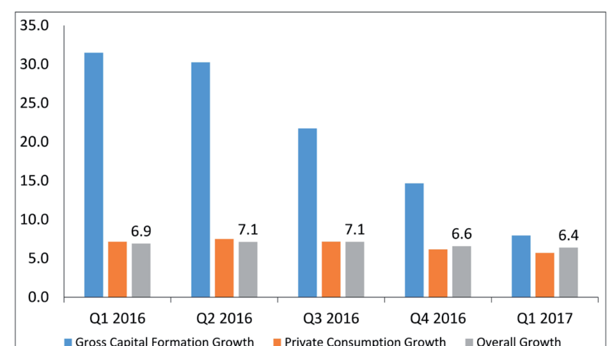



Source: Department of Statistics Malaysia, 2017

# PHILIPPINES

The Philippines grew by 6.4% in Q1 2017, its slowest growth since Q4 2015, though it maintained the highest growth amongst the ASEAN 6. In terms of sectors, growth in Q1 2017 was driven by the manufacturing sector (up 7.5%, yoy) and trade and repair of personal motor vehicles and household goods (up 7.1%, yoy). In terms of expenditure, growth continued to be driven by gross capital formation (up 7.9%, yoy) and consumption (up 5.7%, yoy) (Figure 3).

**Figure 3. Philippines GDP Quarterly Growth Based on Expenditure (%, YoY)**

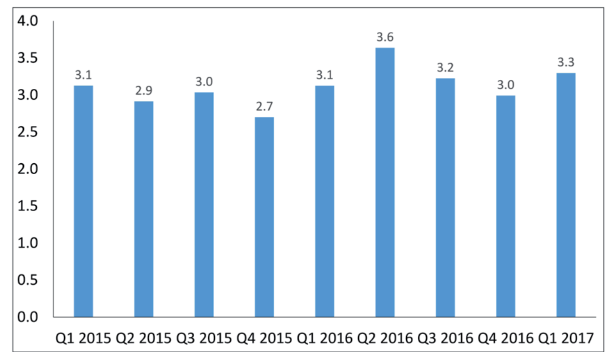



Source: Philippine Statistics Authority, 2017.

# THAILAND

Thailand grew by 3.3% in Q1 2017 (Figure 4), driven by robust export growth (up 6.6%, year-on-year), rising private consumption (3.2%), a growing agricultural sector (7.7%), and an expanding tourism sector (5.3%). However, the manufacturing sector grew at just 1.2% in Q1 2017 compared with 2.2% in Q4 2016, due to a contraction in vehicle production. The growth of the Thai economy is expected to continue being supported by a recovery of exports – fuelled by a pickup of demand from key trading partners and a recovery of global commodity prices – continued expansion of the tourism sector, and an acceleration of agricultural production due to favourable agricultural product prices.

**Figure 4. Thailand GDP Growth (%, YoY)**



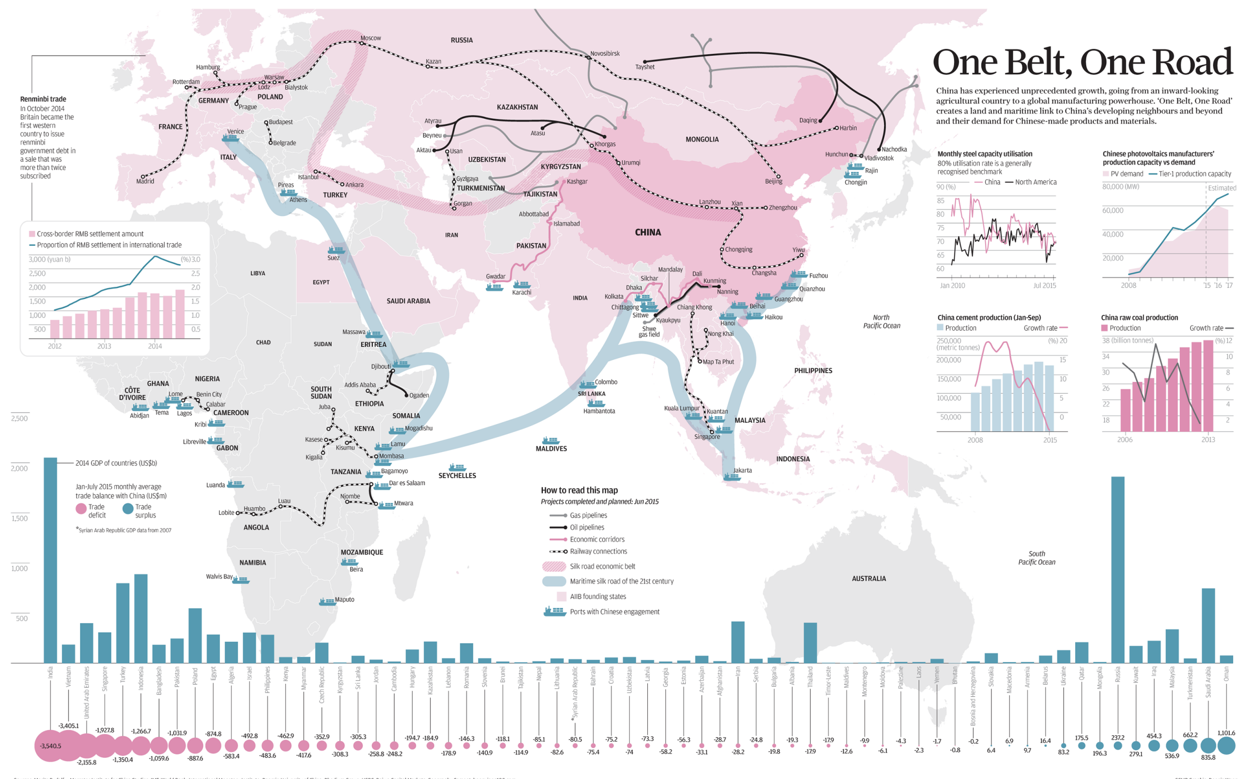

Source: National Economic and Social Development Board Thailand, 2017.

# CHINA

China's GDP rose by 6.9% in the first 3 months of 2017, driven mainly by strong investment and manufacturing output. On the investment side, fixed-asset investment expanded by 9.2% year-on-year as a result of strong performances of the agriculture and industrial sectors. On the manufacturing side, industrial production rose by 7.6% in March compared to the same month in 2016. Retail sales growth was 10.9% in March 2017, maintaining the average growth rate registered in Q4 2016.

Against the backdrop of high debt levels, Moody's downgraded China's credit rating from Aa3 to A1 because of concern over its financial strength over the coming years due to its continued rise of credit growth as potential growth slows. The downgrade is generally ignored by domestic investors, which account for 96% of total outstanding debt, limiting the effect of the downgrade on the bond yield. However, the rating downgrade is a warning of the risks posed by the rapidly increasing leverage that may adversely affect a country's economy.

The pace of growth in the remainder of 2017 is widely expected to be lower than in Q1 2017, as the government continues with its efforts to move from investment- and export-led growth to a more consumer-driven model through various reforms in the financial sector that aim to lower credit growth in the market.



# More integrated Asia: Is ‘Belt and Road Initiative’ an answer?

First introduced in September 2013 by China’s President Xi Jinping, the China Belt and Road Initiative (BRI), previously called the One Belt One Road initiative, is a programme promoted by the Chinese government to increase connectivity throughout the Asian region that aims to increase trade and boost economic growth in the region. There are 65 countries involved in the initiative, which spreads across Asia, Africa, and Europe. The BRI covers around 62% of the world’s population, around 30% of global GDP, and around 34% of the world’s merchandise trade. The total amount of investment to be poured into this initiative is expected to reach at least US$1 trillion, mainly to be financed by the China Development Bank (US$900 billion), the Asian Infrastructure Investment Bank (US$100 billion), and the New Silk Road Fund (US$40 billion) over the next 10 years. While many countries have been responding to the initiative quite warmly, there are also countries that are cautious about joining the BRI.

There are three potential benefits China might gain from the BRI. First, the BRI is believed to be one way the government can promote equality between the poor western parts of China and its more prosperous eastern parts. The rationale behind this is quite straightforward. By integrating the western parts with the eastern parts and also with countries outside the BRI, it is believed that the economic welfare of the western parts may increase due to an improvement of connectivity in the region.

Second, the BRI is seen as a way for China to upgrade its industry and export its high-end manufactured product standards to the less developed countries in the region. The BRI will facilitate the export of higher-end manufactured products to developing countries – those products that would not be accepted by developed countries’ standards, such as high-speed railways and energy generators. By being able to set standards in railway building and oil and gas projects, China will be able to create markets for its products among the developing nations involved in the BRI.

Third, the BRI will utilise China’s industrial capacity. The BRI is less about increasing export products such as steel and more about moving excess production capacity out of China, thereby lowering pressure of excess capacity in the domestic market. Ultimately, the success of Beijing to maintain and create employment will give legitimacy to the Chinese Communist Party, if thereby it manages to maintain economic growth and improve people’s standard of living.

At the same time, BRI will be one of the ways Asian countries can address their infrastructure gaps and let this new economic activity become the new driver of growth amidst slow growth in the United States and the European Union. Improved infrastructure is believed to be key to higher growth among exporting countries in Asia, as it facilitates the movement of goods between countries both within the BRI’s reach and outside the BRI. Other than that, better connectivity within the countries inside the BRI will also improve their economic condition, as the building of new infrastructure itself creates employment and better connectivity and will increase economic efficiency within each nation.

Despite its potential benefits to the Chinese economy and the region, there are three main challenges regarding implementation of the BRI. First, there is a lack of political trust between China and important countries located inside the BRI. This is evident, for example, from India’s reservations about joining the initiative, arguing that there needs to be proper consultation before it is executed. Second, only 23 out of 65 countries involved in the BRI have investment grade issuer credit ratings from agencies such as Standard and Poor’s, Fitch, and Moody’s. This is an indication that most of the countries involved might not have sufficient institutional capacity to handle such a programme, which entails risks for investors – mainly Chinese banks. Third, China itself is currently facing a financial problem of its own as its debt to GDP ratio was an alarming 277% of GDP at the end of 2016.

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