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Asia Pacific Executive Brief

March 2016

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CONTENTS

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This report summarises the current business environment analysis and short-term forecasts of country directors running executive briefing programs across Asia. The Asia Pacific Executive Brief is owned and produced by International Market Assessment Asia Pty Ltd (IMA Asia).

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Global outlook

The US and China are OK

… so a global recession is unlikely

There are a number of occasions every decade or so when financial indicators signal an impending recession yet growth continues. That financial indicators can be misleading was famously captured by Paul Samuelson's 1966 comment that Wall Street indexes had predicted nine out of the last five recessions. While risk indicators jumped on Wall Street in February, the latest US demand data points to steady growth in a 2-3% range for 2016 and 2017. Sitting in Shanghai after a day of debating China's outlook with clients, the overall impression is also one of firm growth in China, backed by plenty of stimulus and good consumer spending. Steady growth in both these critical global markets should be sufficient to stop another global recession.

But stimulus levers no longer work in much of the OECD

… so we face a 5th year of weak growth

Yet we live in unusual times, with many advanced economies operating under central banks with negative interest rates. Worryingly, the negative rates, which are meant to jump start growth, appear to have failed. The outlook for fiscal policy (the second big stimulus lever) in the advanced markets is equally poor. Public debt levels are over 100% of GDP and few governments in the West or Japan have the stomach to act on the OECD's call in February for a wave of stimulus spending. As the type of ground breaking reforms that can also trigger growth are off the table, there seems little prospect of lifting growth in the advanced markets, even if we can avoid a global recession. As a result, we are in for our fifth straight year of sub-par global growth, with 3% expected this year and 3.3% next year from an average 3.9% for the 2000 decade (which included 0% growth in 2009).

Steady US consumer & capex growth

… and not too much pain on the trade account

US GDP for Q4'15 has just been revised up, lifting full year growth to 2.4% thanks to a big upward revision in consumer demand growth to 3.1% from an earlier US government estimate of 2.8%. Private fixed investment growth was also good at 4%, and although down from 5.3% growth in 2014, it was helped by an 8.7% surge in residential investment, which offset a 1.6% fall in non-residential structures (this is where the cut to fracking hit; growth was 8.1% in this sub-sector in 2014). So the US consumer is being buoyed by lower oil prices and is out shopping, buying cars (a 5.7% rise to 17.5m cars and light trucks breaking a 15-year old record), and ordering new homes (the seasonally adjusted annual rate for private housing approvals jumped 13.5%yoy to 1.1m units in January). While big Q1 snow storms mean that 2016 will get off to a slow start, another year of steady growth in consumer and fixed investment seems likely. The missing bit is exports, with the GDP measure of volume growth slowing to 1.1% last year from 3.4% in 2014 due to weak offshore demand and a rising US$. Meanwhile, growth in the US trade deficit was marginal, as cheap oil meant that a 3.1% fall in the value of imports mostly offset a 4.8% fall in the value of exports.

Mild inflation returns by mid-2016

… and the US$ climb continues

While global oil prices look like staying in a US$30-40 band for the next few years, the more important point is that they are unlikely to fall further. That should see low or falling headline inflation numbers fade by the middle of 2016 in the year-on-year calculation. As the US has good employment and wages growth alongside strong housing and car markets, we expect the US Fed to make at least one 25 basis point rate hike this year. That will keep the US$ on an upward trend, rising by 5% for the year average on its trade weighted index in 2016 and 1-3% in 2017 after jumping 16.2% in 2015. Its rise on the Euro will be about the same (as the ECB continues with quantitative easing), putting the greenback close to parity with the Euro by the end of 2017. China's Yuan, which since last August is pegged to a basket of currencies rather than the greenback, will no longer follow the US$ up, dropping by 6% this year and 3-5% next year.

IMA Asia's forecasts	2013	2014	2015	2016	2017
World – Real GDP growth, %	3.3	3.4	3.1	3.0	3.3
- US	1.5	2.4	2.4	2.3	2.5
- Euro area	-0.3	0.9	1.5	1.7	1.7
- Asia/Pacific (14)	4.5	4.3	4.2	4.1	4.1
- NICs (4)	2.7	3.4	2.1	1.7	2.3
- Developing or "EM" Asia (7)	7.0	6.8	6.6	6.0	5.8
- ASEAN (6)	5.0	4.4	4.4	4.4	4.8
World goods & services trade volume, % growth	3.5	3.3	2.6	3.4	4.1
Interest rates, US Fed target rate, year end, %	0.10	0.10	0.25	0.50	1.00
Inflation, CPI, US, year avg., %	1.5	1.6	0.1	1.2	2.0
Inflation, CPI, Euro area, %	1.3	0.4	0.1	1.0	1.2
Crude oil, avg of 3 spot crudes, US$	105	103	50	40	50
US$ / Euro 1, year average rate	1.33	1.33	1.11	1.05	1.02
Yen / US$1, year average rate	98	106	121	112	117

The Asia/Pacific 14 = the countries on the forecast summary page. NICs are the newly industrialised countries = Korea, Taiwan, HK, Singapore. The ASEAN 6 = Indonesia, Thailand, Malaysia, Philippines, Vietnam, + Singapore. Dev Asia = ASEAN 5 + China and India. IMA Asia forecasts.

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Regional outlook

Summary of forecasts in this month's Asia Brief

GDP (Expenditure), real growth, %	2013	2014	2015	2016	2017
Japan	1.4	0.0	0.4	0.3	0.2
China	7.7	7.3	6.9	6.2	5.7
Hong Kong	3.1	2.6	2.4	1.6	2.3
Taiwan	2.2	3.9	0.7	0.9	2.4
South Korea	2.9	3.3	2.6	2.0	2.3
Indonesia	5.6	5.0	4.8	5.0	5.8
Malaysia	4.7	6.0	5.0	3.4	3.4
Philippines	7.1	6.1	5.8	6.3	5.8
Singapore	4.4	3.3	2.0	1.8	2.8
Thailand	2.8	0.8	2.8	3.4	3.6
Vietnam	5.4	6.0	6.7	6.5	6.3
India (CY)	6.4	7.0	7.3	6.6	6.8
Australia	2.0	2.6	2.2	1.9	2.2
New Zealand	1.7	3.0	2.9	2.3	2.7

Inflation, CPI year average, %	2013	2014	2015	2016	2017
Japan	0.3	2.8	0.8	-0.2	-0.2
China	2.6	2.0	1.4	1.0	1.0
Hong Kong (composite CPI)	4.4	4.4	3.0	1.8	2.2
Taiwan	0.8	1.2	-0.3	0.6	1.3
South Korea	1.3	1.3	0.7	0.9	0.7
Indonesia	6.4	6.4	6.4	4.1	5.2
Malaysia	2.1	3.2	2.1	1.6	1.9
Philippines	3.0	4.1	1.4	1.6	2.6
Singapore	2.4	1.0	-0.5	-0.3	0.5
Thailand	2.2	1.9	-0.9	0.1	1.3
Vietnam	6.6	4.1	0.6	1.0	1.9
India (CY CPI urban non-manual workers)	10.1	6.7	4.9	7.4	6.7
Australia	2.4	2.5	1.5	1.6	2.2
New Zealand	1.1	1.2	0.3	1.1	2.0

Exchange rate to US$1, year avg.	2013	2014	2015	2016	2017
Japan	98	106	121	112	117
China	6.20	6.14	6.23	6.61	6.85
Hong Kong	7.76	7.75	7.75	7.77	7.75
Taiwan	29.8	30.4	31.9	33.6	33.5
South Korea	1,095	1,052	1,133	1,246	1,285
Indonesia	10,460	11,868	13,389	13,725	14,250
Malaysia	3.15	3.27	3.90	4.43	4.36
Philippines	42.4	44.4	45.5	48.1	48.4
Singapore	1.25	1.27	1.37	1.45	1.48
Thailand	30.7	32.5	34.2	37.3	39.3
Vietnam	20,933	21,148	21,677	22,639	23,428
India (FY)	58.5	61.0	64.1	69.3	69.5
Australia	1.03	1.11	1.33	1.45	1.45
New Zealand	1.22	1.20	1.41	1.50	1.52

Sources: CEIC, central banks, and national statistics offices. Forecasts are by IMA Asia.

Regional outlook

Political & policy issues to watch

Stimulus still works in Asia

… and plenty is underway

While monetary and fiscal stimulus have lost traction in many of the advanced economies, that is not the case across much of the Asia Pacific. This is important, as Asia faces its fifth straight year without its traditional export engine to lift growth. Critically, China has a large monetary, fiscal, and policy (for housing and cars) stimulus underway, while it is avoiding the mistakes of the 2009 splurge. Meanwhile, governments in the Philippines and Indonesia both find themselves with underspent budgets in 2015, and a catch-up surge in spending either underway (in the Philippines) or expected (in Indonesia). Monetary easing is also underway with China again in the lead. In Southeast Asia, a sharp fall in inflation for countries like Indonesia and Vietnam opens the way for substantial interest rate cuts from quite high rates to support growth.

Two critical leadership changes loom in KL

Malaysia is likely to change its political leader this year and is due to change its central bank head in April. Despite his tight grip on the ruling UMNO party and his suppression of local investigations into 1MDB, PM Najib Razak faces a rising wave of revelations from foreign anti-corruption agencies that will force his party to jettison him. While another UMNO stalwart will replace him, it is far from clear who that will be. Fortunately, 1MDB has been substantially deleveraged over the last few months with Chinese state owned enterprises buying its energy assets and one of its largest property projects. That should help revive banking and property deals in KL. Almost as important will be the selection of a replacement for highly regarded Bank Negara head Zeti Aziz. She undoubtedly angered Najib when the central bank tried investigating breaches of foreign exchange rules by 1MDB. If Najib or his successor puts a pliable placeman in charge, the M$ will fall.

Disappointment in Indonesia and India

Asia would be a very different region today if PM Modi in India and President Joko Widodo (Jokowi) in Indonesia had delivered on what they had promised when they won office in 2014. Within months of taking office both lost political momentum to obstructive parliaments, dashing reform hopes and allowing operating environments to get worse rather than better. Both still promise reform, and Jokowi enters 2016 in a stronger position as the opposition in the Indonesian legislature fragments. While there are hopeful signs, we are not pencilling in a reform-driven lift to growth for either country in the next few years. Indeed, India's growth will be cut unless Modi can reboot his political program.

Outlook for the market

Resilience in Asia yet again

Despite better stimulus prospects in Asia, the region's growth is not immune to the slashing of global growth forecasts in the last six weeks by the IMF, the World Bank, and the OECD. Since last month's Asia Brief, the 2016 growth forecast for the 14 Asia Pacific markets has been trimmed to 4.1% from 4.4%, while the trade-driven NICs were cut to 1.7% from 2.2%, and the seven emerging markets were cut to 6.0% from last month's 6.2%. For Asia's emerging markets to collectively hold onto 6% real growth is a surprisingly good result, and reflects the region's ability to contain risks and rely on domestic sources of growth when its export sector runs flat. This proved to the case when Asia rebounded strongly from the 2008 global financial crisis and the 2001 global tech wreck.

Foreign exchange and balance of payments risks are limited

Asia has been a major beneficiary of falling oil prices as despite a 7.3% fall in regional exports in 2015, the region's trade surplus actually rose by some US$400bn. That stopped a blow-out in current account deficits, reducing macro risk. The region did suffer capital outflows, with combined foreign exchange reserves dropping $570bn or by 8% for the year to January. China's official drop of $583bn was actually bigger, but offset by rising foreign exchange reserves elsewhere. While financial markets are panicking over China's fall in forex reserves it should be noted that it ran a current account surplus of $293bn last year, which will helps offset the impact of capital account outflows on foreign exchange reserves. Indonesia and India, Asia's two emerging markets with the most worrying current account deficits, have largely fixed their challenges; Indonesia by greatly reducing fuel subsidies (it is a net oil importer) and India by limiting gold imports.

Asia starts following the Yuan

China's move to pegging its Yuan against a basket of currencies rather than the US$ last August transforms Asia's foreign exchange outlook. China is the largest buyer from the rest of Asia and also the biggest competitor to the rest of Asia. While its Yuan is no match to the US$ in international trade, where it heads is vitally important to every other country in Asia. Most currency movements in Asia will now start to shadow the Yuan.

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Japan

Political & policy issues to watch

Falling support for PM Abe

… watch for a snap election

A big slide in opinion poll support for PM Abe's cabinet has made the 2016 political outlook uncertain. Until January, it looked straightforward, with the government expected to easily maintain its majority in July's upper house elections. But with support for the cabinet dropping seven percentage points since January to 46.7%, PM Abe may go for an early lower house election, either in April, July (alongside the upper house poll) or December with the aim of taking advantage of current low opinion poll support for the opposition (just 9.3% for the DPJ).

A loss of confidence in policy

Support has swung against the government as "Abenomics", the growth revival strategy promoted by PM Abe, is seen to have failed. It isn't just a sharp fall in growth in Q4'15 or a return to deflation in January (-0.1%yoy) that hurt Abe's poll numbers. Voters appear to have been dismayed by the Bank of Japan's move to negative interest rates in January, which is frightening for an older population that relies on its savings.

Weakening the reform push

… on tax & market opening

A number of big reforms lie ahead that include a second hike in the sales tax (to 10% from 8%) in April 2017, and market opening measures in agriculture and other sectors. The latter are required under the Trans Pacific Partnership, which Japan signed with 11 other countries at the start of February (ratification by all parliaments may take a year or more). With monetary and fiscal stimulus exhausted, reform is the one area that has the potential to revitalise Japan. Yet PM Abe, a cautious reformer at best, will likely run cold on reform given the shift in the political winds. Critically, this means that the April 2017 sales tax hike is likely to be delayed or shelved, which will have a big impact on demand (see below). Although legislated, the hike was conditional on demand being strong enough to weather the tax hike, and that is no longer the case.

Outlook for the market

Slipping back into recession

… as exports fall & local demand slows

Growth fell 0.4% in Q4'15 on the prior quarter, and with a similar fall expected in Q1'16, Japan is likely back in a recession right now (two consecutive quarter-on-quarter declines). Using our normal year-on-year measure, which puts GDP growth at a weak but still positive 0.5% in Q4'15, two problems stand out. First, consumer demand growth fell 1.1%yoy in Q4'15 after a reasonably good 0.4%yoy lift in Q3'15. Second, export volume (which counts in the real GDP measure) fell 0.8%yoy after good growth of 4%ytd through the first three quarters of 2015. As a result, Japan enters 2016 with the two engines capable of supporting GDP growth both contracting. Moreover, most of this year's growth was expected to come in 2H'16, as households and firms purchased capital goods before the April 2017 sales tax hike (essentially pulling demand forward by 2-3 quarters, and leaving little if any growth in 2017). That tax hike now looks unlikely, so we've slashed our 2016 growth forecast to 0.3% from 1.2% last month. Our 2017 forecast, which was about zero, edges up to 0.2%. These forecasts aren't much different from the 0.5% trend growth that the Bank of Japan (BOJ) thinks Japan is capable of.

Wage growth is stuck at 1% as deflation returns

At the core of Abenomics is the goal of reviving domestic demand, by putting pressure on companies to lift wage growth above 1% and by pushing inflation to 2% or more so that consumers have an incentive to buy now before the price rises. Spring wage talks are now underway with the main union groups seeking a 2% lift in the basic wage, but with January core inflation (ex-food and fuel) at 0.7%yoy and dropping, employers will likely hold the line at 1% on the argument that real wages will grow by 1%+ as Japan slides back into deflation. Consumer demand fell 1.2% in 2015 and will likely be flat this year (we had expected close to 1% growth to beat the April 2017 sales tax hike).

The Yen rises and then falls

Core inflation is likely to turn negative in Q2'16 and stay there, pulling headline inflation into negative territory for the next two years. The abnormal Yen surge in 2016, driven by safe-haven forces, isn't helping, as a stronger Yen removes one source of inflation. A rebound in oil prices to $50+ would help, but seems unlikely. Assuming the world moves into calmer waters by 2017, the Yen will swing to a fall as the BOJ maintains QE.

	2013	2014	2015	2016	2017
GDP, real growth (2005p), %	1.4	0.0	0.4	0.3	0.2
CPI, year average, %	0.3	2.8	0.8	-0.2	-0.2
Overnight call rate, year end, %	0.07	0.07	0.01	0.01	0.01
Yen to US$1, year average	98	106	121	112	117

Sources: 2012-2014 data from the BOJ and government sources; 2015-2016 estimates by IMA Asia

China

Political & policy issues to watch

Who's in charge?

… a modern economy needs a government that governs

By the end of the 2015, stumbles over a new exchange rate policy and an inflated stock market had led to a loss of confidence in Beijing. Moreover, Premier Li Keqiang and his top ministry officials appeared to have been sidelined. Control over policy has moved to study groups run by the Communist Party, which have blossomed under the all-powerful party general secretary, Xi Jinping. China has a chance to sort out the confusion at the National People's Congress (NPC), which starts on March 5, as that should be Premier Li's show. The NPC will provide details on the 13th Five Year Plan (2016-20) and, as China is a policy-driven market, those details will be critical for growth in many industries.

Lots of monetary & fiscal stimulus to support growth & curb risk

China's stimulus is strong enough to underpin growth of 6.5% this year and to control risk in housing, the finance sector, and industry. Loan growth has continued at a steady 15%yoy, despite a fall in current GDP growth to 8%. Interest rates and the bank reserve requirement ratio are also being steadily cut. Meanwhile, fiscal stimulus has jumped, with spending growth up 16% last year while revenue growth slowed to 8% on our estimates. Finally, restrictions on the property market have been eased and incentives introduced for car purchases, with both triggering a jump in sales in recent months.

China is still a zombie movie, unfortunately

China's outlook would be great this year if it wasn't for a massive oversupply of housing and industrial capacity, along with a mountain of bad loans, mostly hidden, that contributed to both. The question is how fast Beijing clears up the mess. The process started in 2015, with some chemical and steel firms being closed. A string of recent statements initially suggested a faster pace for SOE restructuring in 2016. Yet the details point to a gradualist approach, which means that zombie firms will continue to thrive across China in 2016.

Outlook for the market

Learning to read China's GDP

… its growth Jim, but not as we know it

… the rise of China's services economy

Arguments over how much China has overstated its growth rate have faded as observers have come to understand the dramatic and painful realignment portrayed in the data. On the real growth measure (i.e. volume), China's secondary sector (85% of which is manufacturing and construction) grew 6% in 2015. Yet in current prices (volume + inflation or price rises) growth was just 0.9%. In other words, prices crashed, which reflects the intense competition created by excess capacity. By contrast, the "tertiary" or services sector saw real growth of 8.3% and current growth of 11.7%, a more normal pattern reflecting growing business volumes and rising prices. China's hunger for services – financial, entertainment, travel, logistics, ecommerce – still exceeds the delivery of those services. On the real price measure services reached 45% of the economy in 2015 from 40.5% in 2000, largely at the expense of a rapid fall in agriculture's share. On the current price measure services exceeded 50.5% of GDP for the first time in 2015. Either way, services are now the driving engine of China.

Real growth eases while oversupply hurts factories & construction

The same real/current growth pattern will continue for the next 3-5 years, as the secondary sector continues to struggle with excess capacity, while the services sector faces unmet demand that allows price increases. For the three years from 2015, we put real growth for manufacturing at 5.9%, 5%, and 4.5% (current at 0.4%, 0%, 0%). For construction, we expect real growth of 6.8%, 6%, and 5% (current 3.7%, 3%, 2.5%). For services, we expect real growth of 8.3%, 7.8%, and 7.3% (current at 11.7%, 10.8%, and 10.3%).

Good consumer growth despite slower wage rises

The driver for demand growth will be consumers and cooling but still critical fixed investment. Wage growth has slowed from 12% under the 12th five-year plan (the goal was 13%) to 7-8% for 2016-2020 (with 5% for this year). That's 3-4 percentage points above expected inflation, which supports good consumer demand growth.

A falling Yuan on a rising US$

Last August's decision to unhitch the Yuan from the US$ and peg instead to a basket of currencies was of global consequence. The Yuan need no longer be dragged up with the US$'s surge, so we expect year average declines on the greenback of 6% this year and 3-4% next year after a 1.4% fall in 2015. That still leaves the Yuan as one of the world's stronger currencies, and it may regain ground on the US$ once its surge fades from 2018.

	2013	2014	2015	2016	2017
GDP, real growth, %	7.7	7.3	6.9	6.2	5.7
CPI, year average, %	2.6	2.0	1.4	1.0	1.0
PBOC 1-year loan, at Dec., %	6.00	5.60	4.35	3.85	3.35
Yuan to US$1, year average	6.20	6.14	6.23	6.61	6.85

Sources: 2013-15 data from CEIC and government agencies; 2016-17 forecasts by IMA Asia

Hong Kong

Political & policy issues to watch

A good Budget

… helps HK and Tsang

Financial Secretary John Tsang unveiled the 2016/17 budget in this month, aiming to provide support for HK's ailing economy. Tsang announced an increase in households' tax allowances, a SME tax cut, plus a one-off cut in salary tax and rates. While these moves will reduce public revenue, the budget is forecast to remain in surplus in 2016-17 (HK$11bn), albeit a reduced one from 2015-16 (HK$30bn). Overall, Tsang's budget has been well received and may help add to his appeal as a potential candidate in the 2017 Chief Executive election.

LegCo will be unresponsive to economic challenges

The Legislative Council (LegCo) is expected to approve the Budget by the end of its current term in July. However, members are unlikely to pass many more bills in the run-up to the September elections. Only bills related to funding for the high-speed rail and HK-Macau bridge, and the Eastern Tunnel takeover may get through. The disparate pro-Democracy opposition are expected to continue to disrupt sessions, as part of their multi-faceted dispute over increasing mainland presence and authority in the SAR. This could adversely impact HK's response to future economic volatility.

Little financial risk

HK's economic and housing downturn should not place the financial sector under risk. A large number of cash purchases of houses means that property loans made up only 11.3% of banks' assets in mid-2015, well below Singapore's rate (28.2%). This will enable banks to absorb the likely 20-30% fall in housing prices.

Outlook for the market

Lowered 2016 GDP forecast

We have lowered our 2016 HK GDP forecast by 0.7pp to 1.6%, as the region faces sizable challenges. The China slowdown is expected to affect both trade and tourism in 1H'16, while the housing decline will weaken construction. Modest job and wage growth is expected to limit consumer spending. The economy should firm in 2017 - but will face an ageing population, modest Chinese demand, and the gradual offshoring of its ports trade. This should limit GDP growth to below 3%pa for the rest of the decade.

Real estate boom has ended

… housing will ease

HK's staggering real estate boom has come to an end. Housing prices, which had tripled in the seven years to September 2015, have fallen 7% in the following four months. Land sales and housing transactions have both eased. This will likely slow private construction investment growth from 4.7% in 2015 to -2.0% in 2016. Strong underlying demand and government policies to support construction will prevent a deeper downturn, and likely lead to a solid 4-5% rise in 2017. Funding for infrastructure projects would stabilise public construction.

Export hub in trouble

HK's position as a world-leading import-export hub is under threat. Goods export growth has eased from 8%cagr in 2001-11 to 3%cagr in 2012-14. Exports fell 2% in 2015 and will likely do the same in 2016. Weak Chinese demand is key to this slowdown, but it also relates to decisions by shipping agencies to gradually move from HK to cheaper mainland ports. This will limit the 2017-20 export recovery to 2%pa growth.

Mainlanders impact HK tourism

HK's tourism sector faces a tough 2016. Protests, visitor restrictions, overseas competition, and the weak Chinese economy helped mainland tourist growth to ease from 5%yoy in 1H'15 to a 10% fall in 2H'15 – a situation likely to persist this year. European and American visitors did rise 3%yoy in 2H'15 from a 2%yoy fall, but they make up just 5% of overall arrivals. Lower tourism numbers will soften hotel and restaurant revenues, and cut spending on electronic and luxury items.

Low inflation, but interest rates rise

Reduced housing costs are expected to ease inflation from 3.0% in 2015 to 1.8% in 2016. Rising commodity prices will likely lift the CPI in 2017. Despite weak prices, the HK$-US$ link will force local authorities to match any US interest rate rises.

	2013	2014	2015	2016	2017
GDP, real growth, %	3.1	2.6	2.4	1.6	2.3
Composite CPI (04/05), year average, %	4.4	4.4	3.0	1.8	2.2
Discount window base rate, % year end	0.50	0.50	0.75	1.00	1.50
HK$ to US$1, year average	7.76	7.75	7.75	7.77	7.75

Sources: 2013-2015 from Censtat, HKMA, and CEIC; 2016-2017 estimates by IMA Asia.

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Taiwan

Political & policy issues to watch

A 4-month pause in government

In the wake of January's elections, the newly-elected legislature has met and for the first time is under the control of long-time opposition party, the DPP. Out-going President Ma Ying-jeou will hand over power to the DPP's Ms Tsai Ying-wen in May. The 4-month handover period under a caretaker administration leaves Taiwan more or less rudderless in policy terms, which will constrain its ability to respond to a collapse in global demand.

DPP policy goals

… start new industries & avoid annoying China

As the outlook for Taiwan's traditional core industries has weakened, the DPP aims to promote new industries, such as aerospace and biotechnology. Taiwan excelled at promoting its world-leading high-tech sector three decades ago, but whether the DPP has the skills to repeat that success with new industries remains to be seen. A more immediate challenge will be handling cross-strait relations, as Beijing has made clear its unease at the DPP's sweeping election victory. Ms Tsai is expected to moderate her party's traditional call for independence, aware that many Taiwanese industries (recently including tourism) are massively dependent on the mainland.

Tough policy decisions needed on ageing

Taiwan is facing dramatic population ageing, so one of Ms Tsai's biggest challenges will be reforming pensions alongside policies to boost female and mature worker participation in the workforce. Such reforms won't be popular, and that will test whether the DPP, which is more accustomed to protesting than ruling, can maintain its unity in the legislature.

Outlook for the market

A broad fall in growth

Taiwan ended 2015 with two successive quarters of negative year-on-year GDP growth. It will likely start 2016 with two more. Weak Chinese demand and an electronics slowdown will see manufacturing's 4%yoy fall in 2H'15 extend into 1H'16. This will depress labour markets, which also means weaker consumer spending. Provided global growth lifts in late 2016, manufacturing should enter a mild recovery in 2017, lifting GDP growth to above 2%, as exports recover and IT firms boost capex on a new round of products for 2018.

A weak labour market will hurt consumers

Job growth fell from 27,000 per quarter for Q1-Q3 2015 to just 13,000 in Q4'15. Wage growth also slowed from 3%yoy to 1%yoy. Waning consumer optimism saw retail sales swing from 1.9%yoy growth in 1H'5 to a 0.5%yoy fall in 2H'15. We expect real consumer growth to slow from 2.3% in 2015 to 1.3% this year, with a mild lift to 1.7% in 2017.

Industry is waiting for the next chip

The semiconductor sector has been key to Taiwan's electronic slowdown. The industry operates on a multi-year, boom-bust cycle driven by the release of new chip technology. The most recent chip designs lifted revenue by 16%yoy in 2013 and 2014 and 20%yoy in Q1'15. However, growth fell 2%yoy for the final three quarters of 2015. The next wave of chip technology (7nm) is not due to go into production until 1H'18, which suggests weak growth through to 2017, apart from capex on new equipment.

Weak capex

Fixed investment growth is expected to be a mild 1.2% in 2016, down from 1.5% in 2015. Falling housing and commercial starts will cause construction investment to decline. A mild construction recovery in 1H'17 and investment in the next round of chip technology will likely lift investment to 2.7% in 2017. A key issue is whether Taiwanese firms are allowed to partner with Chinese firms in the next technology round.

Little inflation and a weak NT$

Taiwan escaped a year of deflation in January, with the headline CPI rising to 0.6%yoy. Inflation will likely stay in a 0-1% range, as the big oil price fall of 2015 moves out of the calculation. The central bank has room to cut its policy rate if needed. The NT$ has been one of Asia's strongest currencies in 2015, falling just 5.8% on a surging US$. A similar fall is expected this year, before a return to mild appreciation in 2017.

	2013	2014	2015	2016	2017
GDP, real growth, %	2.2	3.9	0.7	0.9	2.4
CPI, year average, %	0.8	1.2	-0.3	0.6	1.3
Official discount rate, year-end, %	1.88	1.88	1.63	1.63	1.88
NT$ to US$1, year average	29.8	30.4	31.9	33.6	33.5

Sources: 2012-2014 government data and CEIC; 2015-2016 forecasts by IMA Asia.

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South Korea

Political & policy issues to watch

President Park & her party are well placed in polls

President Park Geun-hye and her Saenuri party are well positioned for national assembly elections in April and the presidential race in December 2017 (Park faces a single term limit). The latest opinion polls give Saenuri a 15-point lead over the main left-wing opposition, which has splintered into two parties. That should help the ruling party lift its share of legislative seats from a current 52%, while allowing them to seek greater control over the committees that play a critical role in the progress of bills. Park has backed key supporters within her party for the April contest, so her hold over the ruling party should tighten just as it improves its position in the assembly.

Labour reform is this year's big policy battle

One of Park's top policy objectives this year is deregulating the labour market. Unions strongly oppose this, so several nationwide strikes are likely. Apart from making it easier for firms to do business, Park is motivated by a rise in non-regular workers to 32% of the workforce. Such workers are paid less and received limited benefits, which, in turn, makes them weak consumers.

Less stimulus in 2016

… as policies to boost housing are dropped

One of 2015's surprises was the effectiveness of stimulus measures to boost the property and residential construction market. Starting in 2014, mortgage regulations were eased and the central bank cut its policy rate four times to a record low of 1.5%. That saw house and apartment sales soar to an annual rate of 3.0m units by last November, well above the 2.1m unit average for the prior seven years. Meanwhile, housing approvals jumped 49% to 765,328 units and starts rose 22% to 111,926 units. While house prices gains have been modest, the government (and IMF) are now worried by soaring household debt, so the housing stimulus will be wound down in 2016 and real growth for the construction sector will likely drop from 2.9% last year to 1.9% this year, with a fall of some 2% in 2017.

Outlook for the market

Growth slows to 2% as stimulus fades

We've cut our 2016 forecast to 2.0% (from 2.4% last month) as Korea confronts a continued fall in exports and a weaker consumer sector. Moreover, the housing stimulus that helped deliver 2.6% growth in 2015 is fading and no similar stimulus boost is likely this year. 2017 should see a lift to 2.3% growth, provided export demand recovers.

An late 2015 jump in consumer demand will fade over 1H'16

The 2015 property boom helped consumers, with retail sales accelerating to 4.5%yoy growth in Q4 from a 1%ytd for the first three quarters and car sales surging 19%yoy from 6%ytd for the first three quarters. This also reflected an absence of national crises, such as MERS, which hurt sales in 1H'15. Employment conditions were steady (unemployment of 3.5% and 3%+ wage growth) while home prices gained 4.4%yoy. Yet with the property and construction sectors expected to ease, and no sign of a lift in export manufacturing, unemployment will rise and wage growth will slow. Real growth in consumer demand in 2016 and 2017 is unlikely to better than the 2.1% reported in 2015.

No lift for exports or capex on plant & equipment until 2017

Exports fell 8% last year (US$ terms) but an 18.8%yoy plunge in January exports has rattled the government, which has decided to accelerate, but not yet increase, its spending in 2016. Industrial production fell 0.7% last year with a smaller fall likely this year, and about 2% growth in 2017. The local purchasing managers' index has been below the 50 for most of the past year, encouraging firms to cut their capex plans.

Little inflation & a weaker Won

Weak demand and low inflation leave room for one more 25 basis point cut to the policy rate of the Bank of Korea (BOK). While inflation might edge up in 2017, it is unlikely to trigger a rate rise. The currency has fallen below the 1,200 to the US$ level for the first time in five years, and the authorities will likely keep it weak to help exporters.

	2013	2014	2015	2016	2017
GDP growth, %	2.9	3.3	2.6	2.0	2.3
CPI, year average, %	1.3	1.3	0.7	0.9	0.7
BOK Base rate, year-end, %	2.50	2.00	1.50	1.25	1.25
Won to US$1, year average	1,095	1,052	1,133	1,246	1,285

Sources: 2013-2015 government data (NSO, BOK) and CEIC; 2016-2017 forecasts by IMA Asia.

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Indonesia

Political & policy issues to watch

President Jokowi gains a majority in the legislature

Some 16 months into his first 5-year term, President Joko Widodo (Jokowi) is gaining political momentum as the opposition Red & White Coalition (KMP) in the legislature collapses. Deft manoeuvring led by senior minister and trusted Jokowi confidant Luhut Panjaitan have pulled Golkar and PPP out of KMP, although they have yet to join Jokowi's government. The main opposition party is now Prabowo Subianto's Gerindra, which is differentiating itself from the administration on key policy issues ahead of the 2017 local elections (including the prized Jakarta governorship) and the 2019 national contest.

The challenges of a bigger coalition

Jokowi is treading carefully with his expanded coalition, recognising the pitfalls of the "grand coalition" model adopted by his predecessor, President Yudhoyono, which had so many factions that leadership was weak and policymaking stalled. Still, a cabinet reshuffle may be required to find seats to lock in support from Golkar and PPP. That will also give Jokowi a chance to jettison some ministers with a penchant for independent policy.

Rolling back nationalist laws

… in mining and business

Jokowi is pushing back a wave of nationalist legislation over the last decade. The government will review a 2014 export ban on partially processed metal ores, as the smelters that miners were required to build have stalled. February also saw openings for foreign investors announced in a new negative investment list (DNI), which is the 10th reform package since last September aimed at cutting red tape. A presidential decree enacting the DNI has yet to be issued, but its modest gains are moving in the right direction. Foreign direct investment (FDI) inflows fell 15% last year to US$15bn, with Ford saying it would exit Indonesia while Panasonic and Toshiba will reduce their operations.

Outlook for the market

Stuck with modest growth

… although capex edges up

Indonesia wrapped up 2015 with a 5.1% lift in fixed investment led by a 6.2% rise in capex for building. That helped offset flat capex (-0.3%) for plant and equipment, the third straight year that this critical engine for long-term growth failed to rise above 1% growth. With Jokowi's reforms, we expect growth in plant and equipment capex to rise to 3-5%pa for the next two years, lifting overall capex growth to 6-7%pa. Elsewhere, growth will be flat on last year's modest gain. Consumer growth is likely to be a bit weaker than last year's 5% and closer to the 10-year cagr of 4.7%, before a rise above 5% in 2017. Exports are likely to fall 2-4% in volume terms and by 6-8% in US$ terms in 2016, before recovering to weak growth in 2017 of 2-3% by volume and 6-8% by value.

A weak consumer market at the top end

… while basic FMCG does OK

Consumer real growth dipped to 4.9%yoy in Q4'15, its slowest pace in four and a half years. Falling vehicle sales in January suggest a further easing in 1H'16, with motorcycles down 17% (in line with the full 2015 fall), the big multi-purpose vehicle sector flat after a 20% fall in 2015, and the small passenger sedan sector down 39% (above the 2015 fall of 19%). Commercial truck sales plunged 28% in January after a 16% fall in 2015. After stripping out inflation, retail sales growth of 7.6% in January was slightly better than last year's 6.8% as basic FMCG demand tends to be steadier. An above average 6.6% lift in rice production last year would have helped rural consumers. Urban consumers should also benefit from a 13% rise in the average monthly minimum wage for 2016.

Mining contracts & manufacturing is weak

On the GDP volume measure mining fell 5.1% last year (after 0.7% growth in 2014) while manufacturing slowed to 4.2% growth (from 4.6%). Despite promised reforms (see above), mining will likely contract for several more years while manufacturing stays in a 4-5% band.

Scope for rate cuts & a mild Rupiah fall

With annual inflation of 4.2%yoy in January (and 3.6% on the core measure), Bank Indonesia has cut rates already this year and has scope for several more cuts without unduly weakening the Rupiah. After breaching 14,000 in December the currency has recovered to around 13,500 to US$1, but has downside risk of 3-5%pa on the US$.

	2013	2014	2015	2016	2017
GDP, real growth, %	5.6	5.0	4.8	5.0	5.8
CPI, year average, (2007=100), %	6.4	6.4	6.4	4.1	5.2
Central bank policy rate (O/N rate) at Dec %	7.50	7.75	7.50	6.50	7.00
Rupiah to US$1, year average	10,460	11,868	13,389	13,725	14,250

Sources: 2012-2014 government data (BPS, BI) and CEIC; 2015-2016 forecasts by IMA Asia

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Malaysia

Political & policy issues to watch

PM Najib fends off corruption charges

… but could step down in 2016

PM Najib Razak retains the upper hand in his battle to stay in office despite growing evidence that he used 1MDB, a sovereign wealth fund under the finance ministry, which he also heads, to steal millions of dollars. He has tightened his grip over UMNO, the party that has run government since independence, and closed down domestic investigations into 1MDB. His problem is that other investigations by regulators in the US, Singapore, and Switzerland continue to unearth incriminating details. Rumours suggest that some top UMNO leaders are negotiating with Najib for his exit. A key test of UMNO's support for Najib is the crucial Sarawak state election due in September 2016.

1MDB's fire sale to China

… a plus for sentiment & deals

… watch for who takes over at Bank Negara in April

Apart from the political theatre, two developments bear watching. First, a 1MDB fire sale has reduced the US$11bn in debt run up under Najib. As many local banks and developers where caught up in 1MDB's schemes, its travails have stymied new projects, undermined investor sentiment, and delayed bank sector consolidation. China has stepped in with a US$2.3bn purchase of 1MDB's power assets (via China General Nuclear Power Corporation) and $1.3bn for 60% of the Bandar Malaysia real estate project (via China Railway Group Ltd, which is keen to build a high speed rail link to Singapore). Deleveraging 1MDB should ease commercial stress and uncertainty in Malaysia. A second development to watch is Najib's choice of a new central bank head to replace Dr Zeti Aziz, a highly regarded governor who brought stability in her 15-year term. Najib, who was angered by Bank Negara's investigation of 1MDB's breaches of foreign exchange rules, may chose a puppet, which would undermine the currency and investor sentiment.

Tighter fiscal policy as oil falls

… which limits macro risk

As Malaysia has the highest exposure in Asia to falling oil prices (40% of budget revenue comes from oil and gas), the government has had to revise its budget. Development spending has been trimmed, more aggressive tax collection is planned, the foreign workers' levy is to be hiked (infuriating business, which has won a temporary halt), and offshore investments by state-owned funds are being sold. Prompt fiscal action has reassured bond rating agencies, who assess macro risk as low.

Outlook for the market

Headwinds cut growth to 3.4%

Apart from bad politics and falling oil prices, Malaysia also faces a deleveraging consumer cycle, and an oversupplied housing market. We expect the combined headwinds to cut GDP growth to around 3.4% over 2016 and 2017 from 5.0% in 2015 and 6.0% in 2014. As there's no room for fiscal and monetary stimulus, Malaysia will have to wait for a revival in commodity prices and export demand. China's purchase of 1MDB assets is a plus, as it reduces 1MDB-driven risk, and will help revive a number of big projects.

Consumers pull back

Consumer growth eased to 4.5%yoy in 2H'15 from 7.6%yoy in 1H'15, and is heading to 3.3%pa in 2016-17 after a decade long surge at 7.5%. Sentiment fell to a record low in Q4'15, as households reacted to a weaker jobs market. Falling home loan applications reflect a reluctance by consumers to add to their record high debt (88% of GDP).

Capex relies on big projects

Key projects, such as the Light Rail Transit project and Mass Rapid Transit, survived the January budget cuts, and with 1MDB-related risk easing infrastructure should do well in the next few years. That will cushion weak residential and manufacturing capex. Structures (mainly housing and infrastructure) finished 2015 with 6.9% real growth even as housing completions fell 25%. Meanwhile, plant and equipment capex slipped 0.3% last year.

More rate cuts, but watch for a M$ recovery by 2017

With growth slowing, inflation should fall from December's 2.7%yoy to sub-2% to the end of 2017, leaving room for several interest rate cuts. The M$'s fall looks excessive, and a rebound is possible in 2H'16 or 2017 provided the next head of Bank Negara is sound.

	2013	2014	2015	2016	2017
GDP, real growth, %	4.7	6.0	5.0	3.4	3.4
CPI, year average (2010=100), %	2.1	3.2	2.1	1.6	1.9
Central bank overnight policy rate, Dec, %	3.00	3.25	3.25	2.75	2.75
Ringgit to US$1, year average	3.15	3.27	3.90	4.43	4.36

Sources: 2012-2014 government, Bank Negara, & CEIC; 2015-2016 forecasts by IMA Asia.

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Philippines

Political & policy issues to watch

The May 2016 elections

… remain wide open

Uncertainty over the outcome of the May 2016 presidential election has not diminished investors' appetite for Philippine sovereign debt. In February, President Aquino's outgoing administration raised US$2bn from the sale of 25-year bonds at a record low yield of 3.7%. Bond buyers seem to believe that Aquino's growth-oriented reforms (mostly anti-corruption, fiscal improvement, and private sector involvement in infrastructure development) are sufficiently entrenched to survive a less reformist president. Aquino's preferred candidate, based on his commitment to continuing Aquino's policies, is Interior Secretary Manuel Roxas. A February opinion poll gives him just 18% support, behind independent senator Grace Poe and Davao City Mayor Rodrigo Duterte (both with 24%), and the frontrunner, VP Jejomar Binay with 29%. These rankings are likely to change by May, as Binay faces a new round of senate investigation into corruption allegations, while Poe and Duterte face eligibility challenges. The son of former dictator Marcos, who plundered the country for two decades, is also running for VP and bizarrely championing his father's legacy.

Fiscal stimulus jumps

… as earlier underspending is reversed

A 17.4%yoy jump in real growth for public consumption and a 30%yoy surge in plant & equipment investment in 2H'15 indicate that Aquino has managed to reverse earlier underspending, which had resulted in unintentional fiscal tightening from 2014 into early 2015. Aquino has also been trying to maintain reform momentum by removing restrictions on foreign direct investment (FDI) and pushing for implementation of a peace deal with Muslim rebels in Mindanao. In February, the authorities also lifted a 17-year ban on the issuing of new banking licensees, which should see foreign banks (most likely from neighbouring ASEAN states) challenge a few family-owned local banks.

Outlook for the market

Strong domestic demand sustains fast GDP growth

Falling exports (-5.6% in 2015 on a US$ basis) and a fast-expanding trade deficit did not stop GDP from growing at an enviable 5.8% in 2015 on the back of an 8.2% rise in domestic spending. The Philippines' relatively low exposure to international trade and investment cycles turns out to be useful in times of global economic turbulence. We expect rising investment and consumption momentum to lift GDP growth to 6.3% in 2016, before capacity constraints pull growth down to 5.8% in 2017.

Infrastructure has at last taken off

A 20.3% surge in plant & equipment lifted real growth in investment to 14% in 2015 from 6.8% in 2014. Capex will continue to outpace GDP with projected growth of 8-10% in 2016 and 6-8% in 2017. Most of the activity will be centred on building transport infrastructure under the government's extensive public-private partnership (PPP) program. The latter has been gaining momentum with the participation of some of the country's largest companies. The surge in activity has attracted foreign firms, with foreign direct investment (FDI) approvals up 27% to US$5.3bn in 2015, after falling 35% in 2014 and 8% in 2013.

One of Asia's best consumer stories

34% average annual growth for car sales from 2013 to 2015 reflects an increasingly confident household sector. This is despite growth in remittances from some 10 million Filipinos working abroad slowing to 6.4% in 2015 from 26% in 2001. More and better paying jobs at home, led by the booming business process outsourcing (BPO) sector, are offsetting the impact of slower remittances. We expected consumption growth to edge up to 6.3% in 2016 and 6.4% in 2017 from 6.2% in 2015 and 5.4% in 2014.

Room for rate cuts & a mild fall for the Peso

At 1.4%yoy in January, headline inflation is well below the central banks 2-4% target range with plenty of room for at least 50 basis points to be cut from a current 4% policy rate. If global growth heads sharply lower, even more could be cut. That leaves room for a lower Peso against a strong US$.

	2013	2014	2015	2016	2017
GDP growth, %	7.1	6.1	5.8	6.3	5.8
CPI, annual average, %	3.0	4.1	1.4	1.6	2.6
Central bank reverse rep. rate, year end	3.50	4.00	4.00	3.50	3.75
Peso to US$1, annual average	42.4	44.4	45.5	48.1	48.4

Sources: 2012-2014 BSP data and CEIC; 2015-2016 forecasts by IMA Asia.

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Singapore

Political & policy issues to watch

Dancing to the tune of the global growth cycle

A drop in Singapore's growth to 2% in 2015 from a post-GFC high of 15.2% in 2010 highlights the city-state's extreme sensitivity to the global business cycle. No other country's exports and imports come close to Singapore's oversized 198% and 169% share of GDP respectively. This partly explains the central bank's reluctance to adopt expansionary monetary policies to lift local demand. However, the government has become more active on the fiscal front in recent months. Public investment grew 6.6%yoy in 2H'15 from 1.2% in 1H'15, partly offsetting a 2.9%yoy drop in private investment. Public consumption growth also lifted to 10.7%yoy in 2H'15 from 2.6%yoy in 2H'15 and -0.1% in full 2014. While the government has lifted fiscal stimulus the central bank has been cautious on monetary stimulus, as the resident unemployment rate has been hovering around 2.5-3.0% in 2015. The unusual mix of weak growth and a tight labour market can be traced to a major policy switch towards more restrictive immigration following public anger over high foreign worker inflows from 2005 to 2012. While the new immigration policy has been popular with the public, it has forced companies to restructure work arrangements and move some operations to cheaper foreign locations.

…with evidence of a mild fiscal stimulus from 2H'15

Keeping the brake on housing

While the government has lifted its fiscal stimulus it has kept curbs on the housing market in place, even though private home prices have fallen 8.4% from their Q3'13 peak, following a 62% surge from Q2'09 to Q3'13. Local developers have been lobbying for the property curbs to be lifted, but with the world still awash with cheap cash, and many global investors seeking a safe bolt hole, the government is not inclined to move.

Outlook for the market

Good local demand in Q4'15

… but stocks were slashed

GDP grew just 1.8%yoy in Q4'15 as a big fall in stocks offset a 3.7%yoy lift in domestic spending and a positive contribution from net exports. Domestic demand was boosted by rising private and public consumption (5.5%yoy and 9.4%yoy respectively), helping to offset a 0.7%yoy drop in fixed investment. While the big decline in inventories is a potentially healthy sign for 2016 growth, weak exports and oversupply in the residential, commercial and industrial property markets are set to limit the pace of GDP growth to 1.8% in 2016 and 2.8% in 2017.

Construction & fixed investment to slow

On-going work on public infrastructure projects, such as extensions of the MRT network, the Singapore sea port and Changi airport, will provide some support for construction in 2016. However, with a 30% fall in the value of contracts awarded last year, the sector faces a fall in growth to 1-2% in 2016 from 2.5% in 2015 and an 11% average for the 10 years to 2015. Overall investment growth, which fell for the last two years, will be flat at best in 2016 and 2017 unless the government lifts its fiscal stimulus.

… so will consumer demand

The 4.5% rise of private consumption in 2015, amid the housing downturn, was surprising and out of step with the 1.2% fall of ex-car retail sales. We expect consumer growth to ease to 3%pa in 2016-17 due to less supportive labour and asset markets.

A steady slide for the S$ on the US$

… which could accelerate

With headline CPI falling since November 2014 (and -0.6%yoy in January) there is scope for easier monetary policy. However, the tight labour market has prevented the MAS from switching to expansionary monetary settings, which are managed by the S$'s exchange rate. It has kept the S$ on a mildly appreciating slope against a basket of currencies, although that hasn't stopped the local dollar falling 7.8% on the US$ in 2015. We expect a fall of about 5% on the US$ this year, but a bigger fall is possible if the MAS sees the need for monetary easing to offset a fall in global growth.

	2013	2014	2015	2016	2017
GDP, real growth, %	4.7	3.3	2.0	1.8	2.8
CPI, year average, %	2.4	1.0	-0.5	-0.3	0.5
3 month interbank interest rate, Dec, %	0.40	0.46	1.19	1.42	1.66
S$ to US$1, year average	1.25	1.27	1.37	1.45	1.48

Sources: 2013-2015 government data and CEIC; forecasts for 2016-2017 by IMA Asia

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Thailand

Political & policy issues to watch

Several more years ahead under military rule

Thailand has been ruled by an autocratic military regime since General Prayut Chan-o-cha seized power in May 2014. Prayut, who serves as PM of the governing military council, has vaguely committed to returning Thailand to democracy, but shows no sign of doing so. Most observers assume his goal is ensuring a peaceful transition in the elite, while also blocking a return to power by the populist Shinawatra clan (the party of PM Thaksin and his sister, PM Yingluck, which easily won elections in 2001, 2005, 2007, and 2011). While discontent simmers, there's no hint of a popular uprising or a military split. Companies interested in Thailand will need to deal with the current government for several more years, beyond which the outlook is uncertain and may include rising political instability.

Kick-starting growth

… infrastructure

… & subsidies

Prayut is keen to revive growth as the country is suffering from a collapse in commodity prices and severe drought, a sharp lift in debt for rural and urban households, and weak consumer and business confidence. Prayut has responded on three fronts. First, he has prioritised major infrastructure projects and embraced China's "One Belt One Road" plan to extend rail lines from Kunming to Bangkok. Second, he has tried to slash red tape, pushing the bureaucracy for faster approvals and spending. Finally, he has reversed course on rural subsidies in the face of a growing rural crisis, and announced US$1bn in rice subsidies and $365m for rubber growers.

China's growing role

China looms large in Prayut's Thailand, and not just via infrastructure. Chinese tourist arrivals, jumped 71% last year to 8m, which helped revive the tourism sector and saw the GDP measure of services exports climb 15% (helping offset a 0.5% fall in the volume measure for goods exports in GDP). Thailand also held its first joint military exercise with China in 2015, while the Thai navy may buy three Chinese submarines for US$1bn.

Outlook for the market

Local demand leads a mild recovery

Thailand staged a weak recovery in 2015 to 2.8% growth after political strife slashed 2014 growth to just 0.8%. A 34% surge in public capex for construction led the upturn, with milder recoveries for consumer demand (to 2.1% from 0.6%) and manufacturing (to 0.9% from -0.2% on the GDP measure). Trade was in surplus (US$12bn), as imports fell 11% on weak local demand while the export fall was 6%. That saw the current account surplus surge to 8.9% of GDP, which supported the Baht. Our forecast of about 3.5% growth for the next two years is mostly based on a mild but steady recovery in local demand. Exports may recover to about 2% growth this year, with 4-6% possible in 2017, which leaves the large manufacturing sector (28% of GDP) with about 2% growth this year and 4% in 2017.

Public works drives capex and GDP growth

The government's US$50bn infrastructure program should lift total construction capex by around 9% this year and 6% next year after a 16% jump in 2015. By contrast, private sector construction capex, which edged back to 0.7% growth in 2015 from a 3.3% fall in 2014, is expected to grow by just 2-3% this year and 3-4% in 2017. Urban construction permits issued last year fell 12%, the third straight year of decline, led by a 17% fall in residential and an 8% drop in industrial, while commercial rose 8%.

Restrained consumer demand

Real growth for consumer demand is expected to edge up to 2.3% this year and 3% in 2017 as high debt levels, drought, historically low rice and rubber prices, and weak wage growth (1.8% in 2015 from 11.9% in 2012) limit spending. Fortunately, the rice and rubber price subsidies announced in November saw farm gate prices jump in December.

A weaker Baht on a rising US$

By January, Thailand's CPI had fallen for 13 straight months, leaving room for the central bank to cut its policy rate from a current 1.50%. The Baht's 9.4%yoy fall on the US$ in January was roughly in line with the ASEAN-6 average (- 8.9%yoy) and not particularly helpful to Thai exports. Falls of 5-8% on a rising US$ are likely in 2016 and 2017.

	2013	2014	2015	2016	2017
GDP, real growth, %	2.7	0.8	2.8	3.4	3.6
CPI (2002 index), year average, %	2.2	1.9	-0.9	0.1	1.3
Central bank, policy rate, year end, %	2.25	2.00	1.50	1.25	1.25
Baht to US$1, year average	30.7	32.5	34.2	37.3	39.3

Source: 2013-2015 data from the IMF and CEIC; 2016-2017 forecasts by IMA Asia.

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Vietnam

Political & policy issues to watch

Trung retains Vietnam's top job

… and commits to continued reform

The failure of reformist PM Nguyen Tan Dung to be named general secretary at the Communist Party's 12th congress in January is unlikely to derail Vietnam's pro-market reforms or to reverse its tilt to the West. Dung's political rival, Nguyen Phu Trong, retained the top post and, although more conservative, has pledged to continue with market-friendly reforms. Since 2011, Trong has presided over trade deals with Korea, the EU, and the US-led Trans-Pacific Partnership (TPP). TPP implementation will require major reforms to labour markets, government procurement, and state-owned enterprises (SOEs) in 2016. Meanwhile, ongoing territorial disputes with China will ensure good diplomatic ties with the US, with President Obama due to visit in May. Dung is expected to remain PM until the legislature approves a replacement in late 2016.

Rising M&A deals

… as SOEs privatise

M&A deals were up 40% to a record high of US$4.3bn in 2015, reflecting growing foreign interest in SOE privatisations and the attractions of a fast growing consumer market. More liberal foreign investment rules from last June contributed to a surge in cross-border deals, including a US$108m stake in state-owned Vietnam Airlines by Japan's ANA Holdings, and a US$1.1bn stake in beer maker Masan Group by Thailand's Singha Corp. 2016 is likely to be another busy M&A year, with SOEs lining up for partial or full privatisation. These include airport operator Airports Corp of Vietnam, dairy producer Vinamilk, mobile network provider Mobiphone, and oil refiner Bihn Son Refining and Petrochemical Company.

Outlook for the market

Growth stays above 6%

… on strong local demand

… & fast growth in export factories

We expect GDP growth to stay above 6.0% in 2016-17, after posting a 6.7% increase in 2015 on the back of the strong growth in manufacturing and construction (up 10.6% and 10.8% respectively). The emergence of a US$4.1bn trade deficit in 2015 from a small US$0.8bn surplus in 2014 reflects a rebound in domestic demand after the 2011-12 slump, which was triggered by a collapse in real estate. The deficit isn't worrying, as the more important current account balance was a $6.6bn surplus for the year to Q3'15, and we expect it to remain in surplus for the next few years. Vietnam led Asia with export growth of 8% last year as new factories came on stream with production relocated from north Asia. Since 2010, Vietnam's exports have risen from 37% of Thailand's to 76% in a dramatic realignment of southeast Asian manufacturing capacity.

Construction does well from housing & infrastructure

Improved availability of credit for both home buyers and developers lifted residential construction and house prices in 2015 (even though the latter are still 15-20% below their 2008 peak). The construction sector is set to benefit from increased private participation in transport infrastructure development, as the government faces budgetary constraints. Official estimates put the cost of infrastructure development at US$48bn during 2016-20. We expect construction output to grow 10.3% in 2016 and 9.2% in 2017.

Strong FDI helps transform the economy

We estimate that brisk construction activity, along with strong inflows of foreign direct investment (FDI) in mostly "greenfield" export manufacturing lifted investment growth to 11% in 2015 from 9.3% in 2014. US$15.6bn worth of FDI projects were approved in 2015. In January, approved FDI soared 101%yoy to US$1.3bn, with realised FDI rising 23%yoy to US$0.8bn. These should translate into solid capex growth of 9.6%pa in 2016-17.

Strong growth for consumers

Some of the incoming FDI is targeting Vietnam's consumer sector. Its growth prospects are brightened by favourable demographics (60% of the population are under 35), low household debt and rising income partly supported by sizeable remittances from relatives working abroad (5.2% of GDP). Consumer spending growth has been rising steadily from 4.1% in 2011 to an estimated 6.3% in 2015 and is expected to edge up to 6.6% in 2017.

A faster slide for the Dong on the US$

With inflation under 1% there is room for the central bank to cut interest rates to weaken the Dong, which has risen sharply against its ASEAN counterparts due to its much slower fall on a rising US$. We expect the Dong slide on a rising US$ to accelerate to 4-5% in 2016-17 from 2.4% in 2015 and 1.0% in 2014.

	2013	2014	2015	2016	2017
GDP, real growth, %	5.4	6.0	6.7	6.5	6.3
CPI, yoy, % (2005=100 from 2007)	6.6	4.1	0.6	1.0	1.9
Central bank refinancing rate, year end, %	7.00	6.50	6.50	5.50	5.50
Dong to US$1, year average	20,933	21,148	21,677	22,639	23,428

Source: 2013-2015 data from the IMF and CEIC; 2016-2017 forecasts by IMA Asia

India

Political & policy issues to watch

PM Modi needs a change in strategy

PM Modi needs to reboot his political strategy in 2016 or he'll fail to win a second term in 2019 and achieve little in his first term. 2015 finished with a big loss for Modi's BJP-led coalition in the Bihar state election, which made clear that Modi's championing of reform-driven growth and his presidential-style campaigning can't beat local politics and local issues. The swelling local issue across India this year is a devastating drought, which comes a year after Modi downgraded the prior Congress government's rural employment program, which had provided a social security backstop in rural India. That miscalculation leaves the BJP exposed to walloping defeats in a string of state polls, and no matter how badly run the opposition Congress Party are, it will lift them in the 2019 national polls.

More support for rural India and infrastructure

Modi has quickly reversed his stand on the rural employment program, pumping more cash into it since late 2015. Rural spending was also prioritised in the 2016/17 budget announced on February 29 by Finance Minister Jaitley. While the budget targets a reduction in the deficit to 3.5% of GDP from this year's 3.9% room has also been found to lift infrastructure spending by 22.5%.

Still pushing ahead on reforms

… & the GST

Modi hasn't abandoned his push to reform India's chronically mismanaged economy. Debt restructuring for state owned power distribution utilities is underway, which is essential to ending power shortages. Ironically, Bihar is the latest of six states to sign up. Direct subsidy payments for LPG to low-income households have also worked and the system will be extended to kerosene, helping end rampant theft and fuel adulteration. There's still talk of big reforms, particularly introducing a GST, which is all but ready to start if the opposition Congress Party approves it in India's upper house, which it controls.

Outlook for the market

Growth will slip

… as rural India slides

… while urban India lifts

India is suffering from its first back-to-back drought in 30 years, which is creating two quite different markets. Rural India (850m or 66% of the population) is suffering, which contributed to a 3.6% fall in food and beverage production last year while 2-wheeler sales grew just 0.7% from 12.7% in 2014. By contrast, urban India (428m) is on an upswing, with passenger vehicle sales up 6.5% last year from 1.6% in 2014, while domestic air travel rose 22% from 10% in 2014. With the urban recovery partly offsetting the rural downturn, overall consumer growth eased to 6.2% last year from 6.8% in 2014. That was sufficient to encourage firms to lift capex growth to a modest 5.2% in 2015 from 2.8% in 2014 (commercial vehicle sales grew 8% last year after a 9% fall in 2014). But even with extra fiscal stimulus, growth will slow to around 6.6% this year from 7.3% in 2014.

A growing gap between low and middle income households

A big part of the slowdown will be weaker consumer spending, which we expect to ease to 5.8% this year from 6.2% last year. Cutting back the rural employment program saw the flow of cheap rural workers into cities accelerate, pulling down wage growth for low-income urban households. That will be partly offset by a 23% pay hike for 23m federal employees and pensioners in early 2016. While that will boost car sales and similar spending by better off households, it will accentuate the gap to the lower-income households.

A jump in public salaries & a mild lift in capex

Government consumption grew just 1.9% last year as Jaitley attempted to rein in the deficit, but will likely jump to 12-15% this year as the public pay hike goes through. Fixed investment growth, which should be 10%+ if India was healthy, will be about the same as last year's 5.2%, with a lift to 7-8% in 2017. There is scope for stronger capex growth if Modi and Jaitley can accelerate some big projects, particularly in infrastructure.

Inflation & rates to rise while the Rupee slips

Rising food prices are expected to push inflation up to 7-8% this year and alongside a bigger budget deficit that will force the RBI to lift its rates by 100 basis points or more. The Rupee slid 5% last year and will likely slide by 5-10% this year before stabilising in 2017.

Calendar year starting January	2013	2014	2015	2016	2017
GDP (MP, 2011-12), real growth, %	6.3	7.0	7.3	6.6	6.8
Inflation - CPI, %	10.1	6.7	4.9	7.4	6.7
RBI repo rate, December, %	7.75	8.00	6.75	7.75	7.50
Rupee to US$1, year average	58.5	61.0	64.1	69.3	69.5

Sources: 2013-2015 data from the government (NCI, RBI) and CEIC. 2016-2017 forecasts by IMA Asia with guidance from IMA India.

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Australia

Political & policy issues to watch

An uncertain election year

… as PM Turnbull focuses on senate reform

The upcoming 2016 election should have been an easy victory on a reformist agenda for PM Malcolm Turnbull, but the outlook has become less clear in the last month. Turnbull, who took office last September after beating PM Abbott in a Liberal Party leadership contest, has shifted his focus from reforming policy to reforming the senate, where fringe parties with little popular support have won seats (by trading preferences) and hold the balance of power. To unseat them, Turnbull may opt for a double dissolution (i.e. a whole senate election instead of a half senate election in a normal general election). That would bring the election forward to July from a likely September date.

Sidelining a GST hike

… & considering a fiscal stimulus

As Turnbull shifts his focus to senate reform, he is ditching big policy reforms, such as raising the GST (possibly to 15% from the current 10%). The one reform still on the table is a bill to amend election rules to stop fringe parties, like the Motoring Enthusiasts, gaming the electoral system to win seats. Fiscal policy will also be critical, with the May budget revealing if Turnbull will opt for a fiscal stimulus as global growth stalls. Ditching plans to return to a surplus would put Australia's AAA credit rating at risk.

Australia's big & risky gamble on commodities

Credit rating agencies are also nervous about Australia's trade exposure in a weak global economy. Commodities dominate exports, with unprocessed metals (29%), fuels (25%), and food (14%) prominent. Moreover, 32% of goods exports go to China's slowing economy. Long-term, Australia should do well, as it is one of the world's lowest cost commodity producers, and the current collapse in commodity prices should drive smaller players out of business. Even as prices have tumbled, Australia has lifted export volumes.

Outlook for the market

Near 2% growth as the east coast lifts

… & mining volumes rise

Despite a collapse in commodity prices and massive cuts to mining capex, the economy did well in 2015. GDP growth is estimated at 2.2%, with 304,000 jobs created (the most in four years), and a lift real wages. Housing construction and the services sector helped sustain growth, although both will cool in 2016, lowering GDP growth under 2%. While export earnings fell last year (by 6% in A$ or 21% in US$), volume rose by an estimated 5%, which contributed to real (i.e. volume) GDP growth. That dynamic is set to continue through the end of the decade.

A two-speed economy flips over

Australia's two-speed economy, which in the 2000 decade boomed in the mining states and stalled in the densely populated southeast, has flipped over in 2015. Western Australia is slowing, with a 13% fall in house approvals and 2.6% retail sales growth compared to a national rate of 4.2%. Meanwhile, lower interest rates and a construction boom saw NSW record a 5.2% rise in retail sales lift and a 28% jump in housing approvals.

A housing boom should ease

Housing investment is expected to ease from 8% growth in 2015 to 6%yoy in 1H'16 to 2-3% in 2H'16 and 2017. Sydney housing prices reportedly fell in Q4'15, while the Melbourne market eased. This will likely cause developers to cut back on projects. However, a large amount of construction work is underway. The government may use this period of weaker home building to boost civil works in the 2016/17 budget.

Tourism doing well

A plunge in the A$ helped overseas tourist arrivals climb from 6%yoy in 1H'15 to 9%yoy in 2H'15. China led the way (+24%), followed by Korea (+13%) and the United States (+11%). Despite the global downturn, the tourism sector is expecting another year of strong growth in 2016.

Downside risk for the A$

Inflation is tracking well below the Reserve Bank's 2-3%yoy target band, which suggests the policy interest rate will stay at a record low 2.0% well into 2017 when a small lift may be needed as the economy recovers. That means a big reduction in the interest rate differential to the US (assuming one more US Fed rate hike in 2016), which will keep the $A weak with downside risk for the next two years.

Year ending December 31	2013	2014	2015	2016	2017
GDP, real growth, %	2.0	2.6	2.2	1.9	2.2
CPI, year average, %	2.4	2.5	1.5	1.6	2.2
RBA cash rate, year end, %	2.50	2.50	2.00	2.00	2.25
A$1 = US$, year average	1.03	1.11	1.33	1.45	1.45
US$1 = A$, year average	0.97	0.90	0.75	0.69	0.69

Source: 2013-2015 data from the ABS; 2016-2017 forecasts by IMA Asia

New Zealand

Political & policy issues to watch

Political stability & steady reform under PM Key

… but rising voter unease may shape the 2017 elections

NZ's next election is due by November 2017 and may be called earlier. PM John Key, who has led his National Party to victory in the last three elections, will need to decide this year if he'll run for a fourth term. Steady leadership on a pro-market reform agenda and a strong economy saw the first opinion poll for 2016 (by Roy Morgan) put Nationals at 47%, well ahead of the opposition Labour/Green alliance at 41.5%. While the main parties would like to run on economic issues in 2017, there is an uneasy groundswell in white middle-class New Zealand over surging Asian migration and a Maori political renaissance. A minor party has already called for curbs on the recent migration boom, which has created housing shortages and driven up prices. If acted on, the outlook for consumer demand and construction would need to be trimmed.

The risks to watch

… housing & a current account deficit

The IMF's latest country review backs the government's decision to ease fiscal policy and a similar modest easing of monetary policy by the central bank. The IMF's main concerns are an Auckland housing bubble, a low savings rate, and weak productivity. A big current account deficit, estimated at 4.8% of GDP in 2015 from 3.1% in 2014, will likely grow to 6-7% this year before falling back to a more normal 5-6% of GDP from 2017. While it's a risk to watch, markets understand that the risk is offset by conservative fiscal policy (a very small budget deficit and gross public debt of around 31% of GDP) and higher interest rates. The IMF notes that while farm exports are struggling this year, they'll recover on strong long-term Asian demand for high quality foods from NZ.

Outlook for the market

A mild slowdown in 2016 as export volumes drop

… with a recovery in 2017

NZ is riding out a collapse in export earnings thanks to strong domestic demand and strong export volumes. Central to local demand growth is a strong migration inflow, which has boosted housing demand and consumer spending, while also ensuring a plentiful labour supply. A fall in the value of exports – by 2.2% in NZ$ and a larger 16.5% in US$ terms - wasn't matched by the volume measure on GDP, which likely rose 6-7% in 2015, well above 2014's 3% growth. The net outcome was surprisingly strong growth estimated at 2.9% in 2015 on the expenditure measure (growth on the production GDP measure was likely slower at 2.3%). With domestic demand easing and growth in export volumes expected to slow this year, overall GDP growth will likely drop to 2.3%. Rising export volumes in 2017 should nudge GDP growth back to 2.7% in 2017.

Migrant inflow boosts consumer demand

Inward migration has lifted labour force growth from 19,000pa in 2008-13 to 63,000pa in 2014 and 2015. That allowed employment growth to accelerate from 8,000pa to 65,000pa without a tightening in the labour market. While keeping inflation and interest rates low it also meant that average wage growth stayed in a 2-3%yoy band. So it is the increase in the number of consumers, rather than rising spending power, that will keep real consumer growth at 2.5% in 2016 and 2017, close to the 2.7% average set for 2010-15.

Construction boom rolls on

… but will soften

New building consents surged 17%yoy in 2H'15 from a 6%yoy rise in 1H'15. Strong population growth boosted the North Island by 30%yoy, with Auckland (36% of total consents) up 27%yoy. Canterbury's earthquake housing re-construction boom is past its peak, with consents down 10%yoy. While consents growth will ease, the large amount of work underway should lift construction by 4-5% in 2016 and about 2% in 2017.

Dairy volume is stable

Weak dairy prices have seen banks announce a rise in non-performing loans to the sector. The good news is that this season's milk production is down just 3%yoy despite the El Nino weather cycle. Recent rains suggest solid production should continue.

Little inflation and a weak NZ$

Inflation is likely to remain below the midpoint of the Reserve Bank's 1-3% band to 2017. This will provide room for one 25bp cut mid-year, taking the official cash rate to a record low 2.25%. The NZ$ will remain below 70 US cents until commodity prices improve.

Calendar years	2013	2014	2015	2016	2017
GDP(Expenditure), real growth, %	1.7	3.0	2.9	2.3	2.7
GDP(Production), real growth, %	2.4	3.7	2.3	2.0	2.6
CPI, year average, %	1.1	1.2	0.3	1.1	2.0
Official cash rate, year end, %	2.50	3.50	2.50	2.25	2.25
NZ$1 = US$, year average	0.82	0.83	0.71	0.67	0.66
US$1 = NZ$, year average	1.22	1.20	1.41	1.50	1.52
NZ$1 = A$, year average	1.18	1.09	1.06	1.04	1.05

Source: 2013-2015 data from Statistics NZ; 2016-2017 forecasts by IMA Asia

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The Asia Pacific Executive Brief is produced by a unique network of in-country experts who run briefing and advisory programs that are designed to help senior executives monitor and anticipate critical business developments through timely insights and analysis. Further information on the markets and the peer group briefing programs is available from the Country Directors listed below.

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