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EXCEL WORKBOOK: IMA Asia clients can also access a 14-page excel workbook with data and charts that can be used for reports and presentations.

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

A soft but broad global upturn in 2017

… forecasts are lifted for China, Japan & the Euro area

The IMF has just released its semi-annual World Economic Outlook (WEO), and for the first time in four years it has lifted—marginally—its forecast for the year ahead, in this case raising global growth for 2017 to 3.5% from a forecast of 3.4% last October. The biggest gains are in advanced economies, up 0.2 percentage points (pp) to 2%, led by a 0.9pp lift for the UK (to 2%), a 0.6pp rise for Japan (to 1.2%), and 0.2pp rise for the Euro area (to 1.7%). The US forecast is up just 0.1pp to 2.3% for 2017, but gets a big lift in 2018 of 0.4pp to 2.5%. For the rest of Asia, China is up 0.4pp to 6.6% in 2017, India is down 0.4pp to 7.2%, and the five biggest ASEAN economies are slightly down 0.1pp to 5.0%. That's mostly how our own forecasts have moved, with notable increases for Japan and China, and a cut to the India forecast. The gains are widely spread around the world, and reflect the gradual repair of balance sheets some eight years after the global financial crisis, the ensuing lift in demand for manufactured goods, services, and commodities, and strong stimulus in China.

Plus firm growth in the US in 2017

… provided policy doesn't stall

… with faster growth in 2018 as capex lifts

The US enters Q2'17 with an unusually large gap between strong consumer and business sentiment and surprisingly weak hard indicators, which suggest that real growth slumped in Q1'17 (the advanced estimate is due out on April 28). For growth to reach our 2.4% forecast for 2017 and 2.8% in 2018, two things are required. First, the Trump administration needs to deliver on some of its policies that should lift demand, particularly extra infrastructure spending and tax cuts. That should lift growth in 2018 (reflected in the IMF's forecast above). Second, business and consumer sentiment needs to remain firm. That's critical to 2017, and it hinges on signs of legislative progress on Trump's policies this year. US firms are sitting on record cash piles. If they are confident in future tax rates and the regulatory environment, they'll lift their investment to match firm demand. If not, then investment growth will stall, and US growth will slip to 1.5%pa for the next two years. Our forecast is a bit stronger than the IMF's, and is based on real growth in consumer spending lifting above 3% in 2017 and 2018 from 2.7% last year, while private fixed investment this year matches last year's weak 0.7% rise before lifting to 2.5% for 2018 and the next few years.

At last, a stronger Euro zone

The 18-country Euro zone enters 2017 with the best data seen since 2007. Inflation in the first three months stayed in a firm 1.5-2.0%yoy band, reflecting a lift in demand and better pricing power as some firms passed through higher energy and commodity costs or rebuilt margins. The 12-month total for new car sales was up 6.1%yoy at February, and new orders in manufacturing were up 5.5%yoy. Consumers are responding to a stronger employment market, with the unemployment rate for the EU27 dropping to 9.5% in February, a rate last seen in May 2009. Along with a sustained rally in home prices for the Euro area and a 19%yoy rise in Euro equity markets, that's led to a steady rise in consumer sentiment.

Moving out of the QE shadow

The lift in demand is firm enough that most of the world's advanced economies can edge policy interest rates up from historical lows and phase out quantitative easing. While the US stock market likely faces a modest correction, that's mostly because expectations are too far ahead of growth. The next US rate hike is expected in June, with a third hike before year end. That should keep the US$ on a mild appreciation path. The ECB should end its QE program at the end of 2017, and may make 1-2 rate hikes next year. Such steps shouldn't sink stock markets or undermine real economies.

IMA Asia's forecasts	**2014**	**2015**	**2016**	**2017**	**2018**
World – Real GDP growth, %	3.4	3.1	3.1	3.8	4.0
- US	2.4	2.6	1.6	2.4	2.8
- Euro area	0.9	1.6	1.7	1.7	1.6
- Asia/Pacific (14)	4.3	4.4	4.6	4.8	4.6
- NICs (4)	3.5	2.1	2.3	2.7	2.6
- Developing or "EM" Asia (7)	6.7	6.6	6.5	6.4	6.2
- ASEAN (6)	4.5	4.4	4.5	4.8	5.2
World goods & services trade volume, % growth	3.5	2.8	2.3	3.8	4.2
Interest rates, US Fed target rate, year end, %	0.25	0.50	0.75	1.50	3.00
Inflation, CPI, US, year avg., %	1.6	0.1	1.3	2.5	3.5
Inflation, CPI, Euro area, %	0.4	0.0	0.3	1.1	1.3
Crude oil, avg of 3 spot crudes, US$	96	51	43	50	52
US$ / Euro 1, year average rate	1.33	1.11	1.11	1.07	1.05
Yen / US$1, year average rate	106	121	109	114	119

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, %	2014	2015	2016	2017	2018
Japan	0.3	1.2	1.0	1.5	1.0
China	7.3	6.9	6.7	6.6	6.2
Hong Kong	2.8	2.4	1.9	2.4	2.4
Taiwan	4.0	0.7	1.5	2.7	2.6
South Korea	3.3	2.6	2.7	2.8	2.5
Indonesia	5.0	4.9	5.0	5.4	6.1
Malaysia	6.0	5.0	4.2	4.3	4.0
Philippines	6.2	5.9	6.8	6.5	6.4
Singapore	3.6	1.9	2.0	2.7	3.2
Thailand	0.9	2.9	3.2	3.7	4.1
Vietnam	6.0	6.7	6.2	6.1	6.3
India (CY)	6.8	7.4	7.4	6.8	7.2
Australia	2.8	2.4	2.5	3.0	2.8
New Zealand	2.9	3.1	4.0	3.5	3.4

Inflation, CPI year average, %	2014	2015	2016	2017	2018
Japan	2.8	0.8	-0.2	0.4	0.6
China	2.0	1.4	2.0	2.0	2.5
Hong Kong (composite CPI)	4.4	3.0	2.6	2.5	2.2
Taiwan	1.2	-0.3	1.4	1.6	1.5
South Korea	1.3	0.7	1.0	2.3	2.6
Indonesia	6.4	6.4	3.5	4.0	4.9
Malaysia	3.2	2.1	2.1	3.8	3.5
Philippines	4.1	1.4	1.8	4.0	4.2
Singapore	1.0	-0.5	-0.5	1.0	1.5
Thailand	1.9	-0.9	0.2	2.0	3.2
Vietnam	4.1	0.6	2.7	4.4	3.9
India (CY CPI urban non-manual workers)	6.7	4.9	5.0	4.0	5.1
Australia	2.5	1.5	1.3	2.3	2.6
New Zealand	1.2	0.3	0.6	2.4	3.1

Exchange rate to US$1, year avg.	2014	2015	2016	2017	2018
Japan	106	121	109	114	119
China	6.16	6.28	6.64	6.92	7.04
Hong Kong	7.75	7.75	7.76	7.75	7.75
Taiwan	30.3	31.8	32.2	30.3	28.6
South Korea	1,053	1,131	1,160	1,124	1,083
Indonesia	11,868	13,389	13,308	13,536	13,825
Malaysia	3.27	3.90	4.14	4.47	4.48
Philippines	44.4	45.5	47.5	50.5	51.7
Singapore	1.27	1.37	1.38	1.39	1.40
Thailand	32.5	34.2	35.3	34.4	34.9
Vietnam	21,148	21,677	21,932	22,499	23,203
India (FY)	61.0	64.1	67.2	69.5	72.0
Australia	1.11	1.33	1.35	1.32	1.30
New Zealand	1.20	1.43	1.43	1.44	1.38

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

Regional outlook

Political & policy issues to watch

Geopolitics

… the threat from N Korea

North Korea risk ranges from mild (some commerce is hurt in North Asia, as China, South Korea, and the US manoeuvre for leverage) through major (a China-US stand-off that halts bilateral commerce), to extreme (the shelling of Seoul). Despite bombast from N Korea, it is only mild risk that is on the table in 2017. Beijing is the central player, and US pressure may see it take mildly tougher action against Pyongyang. The Beijing-Seoul spat over the US THAAD system is a side game, as Beijing attempts to exert greater control over Seoul, and Washington looks for ways to pressure Beijing to take a tougher line on N Korea. Pyongyang can't attack, as that would mean its obliteration. If Pyongyang does look like attacking, Beijing would have to arrange for a new leadership. So, at most, firms with Korea exposure might assess mild risk events that could hurt sales or supplies, as Beijing continues to target individual S Korean firms or specific flows, like tourists.

… & responding to US populism

The loss of the Trans-Pacific Partnership trade deal (TPP, signed by all 12 members in February 2016) after the US withdrew in January is a major blow to better business across Asia, and to US firms, who would have been major beneficiaries. Japan and China have also been threatened with US retaliation for running surpluses with the US, while Washington has said that it aims to renegotiate the Korea-US FTA (KORUS). President Xi of China and PM Abe of Japan have shown how to defuse this risk, by quickly bringing President Trump on side. Korea, with a new leader from May 10, is most exposed.

Big trade deals in Asia are dead for now

APEC trade officials will meet on May 20 and 21 in Hanoi with a key topic being whether any form of multilateral trade deal is worth pursuing without the US. An 11-member TPP is a non-starter, despite interest from Japan. That leaves China's Regional Comprehensive Economic Partnership (RCEP includes India and 14 others). ASEAN is interested, but there is so little of value in RCEP (as it pitches to the lowest common denominator while the TPP pitched to the highest) that we doubt it will go ahead.

Korea heads to the left

Complicating plans to corral N Korea and to move forward on trade deals (or renegotiate them) is an expected swing to the left in the Korean government that will take office on May 10 (see our Korean page).

India may delay GST from July 1

India has done a massive amount of work to prepare for the GST's introduction on July 1, but that is unlikely to be enough, as it is unusually complicated, and key details are only just being released. Since last November, we've flagged this as a risk for India's operating environment, but avoided flagging it as a risk to the economy. Yet, with many now worried about poor implementation, it may undermine growth if it is not delayed.

Outlook for the market

Asia's export engine is back in gear

After five years in neutral (i.e. no growth in exports measured in US$), Asia's export engine is back in gear. By February, exports for the A/P 14 were up 10.2%yoy (see the Asia Brief Excel workbook) and our forecast for 2017 is about 8% growth followed by around 5% in 2018 (see the Asia Forecast Book Excel). While it's not a return to the 11% average annual rate for the two decades to 2011, it is lifting commodity exporters like Australia and Indonesia, and high-tech exporters like Japan and Taiwan.

Will capex and wages also lift?

The $64,000 question is whether the export recovery will prompt a lift in wages and spending on plant and equipment. In many sectors, clients report a catch-up surge in orders by customers who have run with very low inventories over the last five years. In some cases, there are shortages and a scramble for components. That's now extending to labour shortages, at least in Japan (see this month's Japan page). In Q2'17, it should lead to higher spending on plant and equipment, particularly in North Asia. But while a handful of clients have decided to expand production, most are still worried by excess global capacity. There's also little sign yet of wage growth lifting from last year's tepid levels.

Uncomfortably firm Asian currencies

… particularly on a falling Yuan

Some Asian currencies are being pushed higher on the US$ in a pattern that is typical of an Asian export-led recovery. That is, a sharp lift in exports some six to 12 months before a similar lift in imports. The result is a surging trade surplus, and more buying than selling of local currencies, at least on the trade account. Affected currencies belong to Taiwan (up 6%yoy on the US$ in March), South Korea (up 3.4%), Thailand (up 1%), Australia (up 1.9%) and NZ (up 4%). While these are small moves on the US$, they've occurred at the same time as China's Yuan has dropped 5.6%yoy, which is painful for most.

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Japan

Political & policy issues to watch

PM Abe is firmly in the saddle

… talking about reform

… and pitching a stronger Japan

Japan has had 26 prime ministers in the post-war period (an average of 2.8 years each), so with four and a quarter years in office, PM Shinzo Abe counts as one of Japan's longest serving PMs. What's surprising in this world of disgruntled voters is his opinion poll support, which remains firmly above 50%, even though he has done relatively little to deliver the economic gains he has promised voters. Voters stick with him for two reasons. First, there is growing awareness that Japan needs to break with decades on inertia, and PM Abe is the only politician who promises bold action, even if his delivery is poor. Second, north Asia looks a more threatening neighbourhood, and Abe's assertive nationalism may be a safe bet. Many would grant that he has also done well in getting alongside US President Trump, thus curbing the threat from American populism. These strengths have allowed Abe's cabinet to weather the forced resignation in April of a gaffe-prone reconstruction minister without damage. The LDP has changed its rules to allow Abe a third three-year term as party president, so he may well be in power through the next election (due on or before Dec. 2018) and the 2020 Tokyo Olympics.

A focus on non-economic bills

… PM Abe needs to rethink nuclear power

Abe's government is pushing an array of law-and-order bills through the Diet, and preparing for the introduction of equally contentious bills in late 2017 to allow integrated resorts (i.e. casinos). High level discussions are also underway with the Trump administration to identify any changes needed to the US-Japan relationship; we don't expect much change here. Much less successful has been the government's plan to restart Japan's nuclear reactors. Of the 54 nuclear reactors Japan had prior to the 2011 Fukushima disaster, only three are currently running, while 15 are unlikely to ever restart, including the six at Fukushima and another five just approved for decommissioning, which looks like becoming the single biggest growth industry in Japan.

Outlook for the market

An improving outlook

We've lifted our 2017 growth forecast to 1.5% (from 1.3%) and 2018 to 1% (from 0.9%), due to stronger exports and a related and smaller lift in local demand. The spread of growth from the export sector into the local economy is apparent in the Nikkei March services PMI, which reached a 19-month high of 52.9 in March from February's 51.3.

9 months of stronger exports

… lifting import demand

… & industrial production

Japan's export recovery emerged ahead of the rest of the region, with a 7.1%yoy lift in Q3'16 (US$ basis), followed by 8.9%yoy in Q4, and 10.1%yoy in Q1'17. That is the best growth since the 2008 global financial crisis, if the big 2010 rebound after the equally big 2009 crash is excluded. Strong exports will likely push industrial production up 3-4% this year, with 2-3% possible in 2018, after a 4.6% average fall over the last five years. Import growth (excluding mineral fuels) lifted to 4.4%yoy in Q1'17 after an average annual fall of 3% over the last five years. The Nikkei manufacturing PMI for April rose to 52.8 from 52.4 in March, its eight-straight month of expansion. We expect export growth (US$ basis) of 7-9% this year and 3-5% next year after five years with an average fall of 4.6%.

A tighter labour market should lift consumer sentiment

… but no lift yet in equipment capex

A key question is how the export lift feeds into the local economy via demand for labour and capital goods. The March Tankan (business sentiment) survey by the Bank of Japan reports a -25 reading on labour availability, which is the tightest labour market since 1992. That reflects both rising job offers and a 500,000-person annual fall in the labour pool due to ageing. In labour-intensive areas that's led to a scramble for workers, with some firms moving staff from a temporary basis to fulltime. However, it's too early to get excited about this, as national wage data continues to show barely any wage growth. Nevertheless, consumer sentiment should improve and underpin real growth in consumer demand of 1.2% this year and 0.8% next year from 0.4% in 2016. While there's no sign yet of a sustained lift in core machinery orders, that should emerge by Q2'17.

Little inflation and a weaker Yen

Despite the demand recovery, Japan may briefly return to deflation after core inflation slowed to 0.1%yoy in February. There's little reason for interest rates to rise in the next few years, and that should mean a weaker Yen on a rising US$.

	2014	2015	2016	2017	2018
GDP, real growth (2005p), %	0.3	1.2	1.0	1.5	1.0
CPI, year average, %	2.8	0.8	-0.2	0.4	0.6
Overnight call rate, year end, %	0.07	0.04	-0.06	-0.06	-0.06
Yen to US$1, year average	106	121	109	114	119

Sources: 2013-2015 data from the BOJ and government sources; 2017-2018 estimates by IMA Asia

China

Political & policy issues to watch

Xi Jinping is set for a second 5-year term

… with even more power

President Xi Jinping is on track for a smooth entry into his second five-year term as leader of China's communist party at the 19th party congress later this year. All power in China flows from this central position, and Xi has used his first five-year term to become surprisingly dominant over the party, the military, and all levels of government. Risks that may have disturbed his nomination for a second term—such as factional party squabbles, weak growth, a financial crisis, and geopolitical threats—have been comprehensively contained. That should ensure that Xi's supporters will dominate in promotion to key party posts, particularly the powerful Politburo Standing Committee. With his supporters dominating in key positions, Xi will be considerably more powerful in his second five-year term. A key question, with few good answers, is what he'll do with that power.

A crack down on risky lending is underway

Beijing relaxed efforts to curb financial risk as it strove to lift growth last year. With that goal achieved, the first quarter has seen a sharp tightening of control over the financial system with the aim of clarifying and then limiting high-risk lending between different types of financial institutions. That's seen a spike in bond yields and a drop in share prices, but it hasn't yet translated into monetary tightening for the real economy.

Progress on reforms, except for SOEs

Xi has pressed ahead with reforms that cover new economic zones, tax, energy, healthcare, and rural land. By contrast, reform of state-owned enterprises (SOEs) has stalled. While that could reflect a desire to avoid a spike in unemployment as well as some latent opposition to reform, it underscores a major policy swing that has placed a high priority on party control over the market. SOEs help ensure that control.

Outlook for the market

Better than expected growth

… on strong exports & firm local demand

China surprised us with strong 6.9%yoy growth in Q1'17 as exports recovered. Domestic demand (consumption + investment) was up a firm 6.6%yoy, slightly above Beijing's full-year target of around 6.5%. Given the recovery in global demand, sustained local demand, and a rise in infrastructure capex, we've lifted our 2017 forecast up to 6.6% (previously 6.3%) and 2018 to 6.2% (previously 5.8%). The problem with faster growth is that it slows a long-planned rebalancing from capex to consumer driven growth, and adds to a mountain of debt. While a debt crisis isn't imminent, bad-debt challenges will become increasingly apparent in 2017 and 2018.

Consumption remains resilient

Retail sales growth was steady at 10%yoy in Q1'17, with faster growth in premium goods, on-line sales, and services, while food, consumer staples, and clothing lagged (a well-established pattern). As wage growth slowed to 8% last year, consumers are saving a bit less and borrowing a bit more to maintain spending. With a high savings rate and low consumer debt, there's plenty of room for that dynamic to continue for many years, provided consumer confidence remains good. Real growth in consumer spending this year is likely to be close to last year's 7.4% with around 7% possible in 2018.

A surge in capex for infrastructure

Fixed investment growth accelerated to 9.2%yoy in Q1'17 thanks to a 24%yoy surge in infrastructure capex. Capex growth elsewhere remains in the single digits but has been edging up, according to China's fixed asset investment data. That shows residential investment up 8.5%ytd by March after 5.4% growth in 2016 and zero growth in 2015. FAI for equipment lifted to 9.9%ytd by March from 2.1% for 2016 and 10.2% in 2015. Total fixed investment growth this year will be close to last year's 6.3% with 5-6% likely in 2018.

Low inflation and a mildly weak Yuan

Inflation slipped to 0.9%yoy in March on lower food prices from a recent high of 2.5%yoy in January. Inflation should stay within a 2-3% range, in line with moderate demand growth. The Yuan has risen about 1% on the US$ this year, as capital outflows have eased (forex reserves fell just $1m from end 2016 to end March 2017). From a current 6.88, we expect a mild Yuan depreciation to 6.98 by the end of 2017 against the greenback.

	2014	2015	2016	2017	2018
GDP, real growth, %	7.3	6.9	6.7	6.6	6.2
CPI, year average, %	2.0	1.4	2.0	2.0	2.5
PBOC 1-year loan, at Dec., %	5.60	4.35	4.35	4.35	4.35
Yuan to US$1, year average	6.16	6.28	6.64	6.92	7.04

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

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Hong Kong

Political & policy issues to watch

Carrie Lam faces a growing gap between HK & Beijing

Strong support from Beijing ensured that Carrie Lam won selection in March as HK's next Chief Executive (CE). But she'll start her first five-year term on July 1 with little popular support, and almost no rapport with the pan-democrat or localist camp in the Legislative Council (Legco), which remains able to slow or block bills. That suggests she'll do little to ease a widening gap between Beijing's demand for political obedience, and rising demands for more independence. CY Leung, the current CE and her boss, was both unpopular and ineffective, and so failed to win Beijing's support for a second term.

Her first challenge is constructing a cabinet

Lam's immediate challenge is putting together a cabinet. Many potential candidates will be worried about being caught between Beijing's demands and rising local distrust of China. There's also little chance of attracting supporters from the localist camp into a "unity" cabinet. Several candidates have already turned down cabinet posts.

Then she must tackle housing

Lam aims to improve on Leung's housing policy, as soaring home prices threaten stability. She's suggested land reclamation, cutting into parks, faster brownfield rezoning, a "starter home" scheme, and public-private partnerships for public housing construction. Last year, Leung initiated a 40% lift in housing supply, and Lam's policies will build on that. The challenge is considerable. Some new flats on sale are just 284sq feet (26sqm), and it would take 26 years of every dollar in the median HK salary to pay them off. 2017 started with mainland developers pushing aside HK firms, who are sitting on large land banks, with record bids for sites. The politics of land is, in many ways, the politics of HK.

Outlook for the market

A weak 2017 recovery

A mild recovery in global trade, firmer growth in China, and strong housing should lift real growth in GDP to 2.4% for the next two years from 1.9% in 2016. By the standards of the last 30 years, this will be a weak recovery, with growth well below the 3.4% annual average for the two decades to 2016. That reflects the challenges of policy gridlock, a structural loss of transhipment work, and an end to the surge of PRC shoppers.

… as port business hollows out

HK's trade and logistics sector (20% of GDP) lost out in last year's consolidation of world shipping into three new alliances, which saw some transhipment move to Singapore. That comes after years of losing out to cheaper nearby ports and airports in China. The government hopes this will be offset by growing integration with China's vibrant Guangdong Province, backed by the 50km HK-Macau-Zhuhai bridge. Yet, the bridge has been delayed for years, and its unclear whether HK's services sector will get a boost.

More home building will help

An 80% surge in home starts in 2016 points to a strong construction market in 2017, although companies are struggling with high costs and labour shortages. Plans for strong infrastructure spending also face approval delays by Legco. The net outcome should be a mild lift in capex growth to 2-4%pa over 2017-21 from 1.3%pa in the last three years.

Hope that a fall in PRC visitors ends

… weak income growth limits local consumers

HK retail sales fell 6.7% in 2016, and will likely fall 5-10% in 2017 and 2018, as the US$ peg makes HK uncompetitive and mainland shoppers purchase more at home (a prominent Beijing policy). PRC visitors (75% of total) fell 6.7% last year after a 3% fall in 2015. The first two months of 2017 saw a 1.1% rise and given our firm China consumer outlook, growth of 1-2% is likely for the full year. Local household spending in 2016 was constrained by a slip in median income growth to 2.6% from 5.7% in 2015. We expect real growth in consumer spending to edge up to 2.5% this year and next from 1.6% in 2016. That's still well below the 3.2% average for the 20 years to 2016.

Little inflation & following US rates up

Given a strong HK$ and a weak recovery, inflation of 2.0-2.5% is likely over 2017-18. The 34-year old peg to the US$ will be retained, and that means the local policy interest rate will stay 50 basis points above the US Fed's rate.

	2014	2015	2016	2017	2018
GDP, real growth, %	2.8	2.4	1.9	2.4	2.4
Composite CPI (04/05), year average, %	4.4	3.0	2.6	2.5	2.2
Discount window base rate, % year end	0.50	0.75	1.00	1.75	3.75
HK$ to US$1, year average	7.75	7.75	7.76	7.75	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

Fractious politics slow tough policy decisions

Taiwan's outlook is limited by fractious politics and, as a result, a weak capacity for reforms needed to underpin long-term growth. The problem is apparent in President Tsai Ing-Wen's poll support, which has plunged below 50% from 76% a year ago when she took office, as she battles to reform labour laws and a public pension system that is about to go bust. That has cost her left-of-centre government union support. Meanwhile, Taiwanese firms are worried about deteriorating relations with China due to the ruling DPP's independence inclinations. That saw mainland tourist arrivals fall 34%yoy in 2H'16 with another 41%yoy fall for the first two months of 2017.

… a promise to lift infrastructure spending

Fortunately for President Tsai, an export recovery is underway, and a lift in sentiment and growth may help her poll numbers and legislation. Last month, the government also proposed an eight-year, US$29bn stimulus package covering transportation, water management, green energy (notably offshore wind and solar), digital infrastructure and urban-rural amenities. That should have a mildly positive impact on fixed investment, provided enabling bills make it through the legislature in the next few months.

Outlook for the market

Electronics lead a lift in exports & GDP

A general recovery in global trade and a lift in the production cycle for new smartphones should provide Taiwan with an export-led recovery in 2017. Strong import growth over the last six months was mostly driven by a rise in capex spending by manufacturers in the export sector. Meanwhile, proposed infrastructure projects, including a third LNG terminal, should help lift GDP growth to 2.7% in 2017 from 1.5% in 2016.

However, growth will fade from 2018

Exports grew 15.1%yoy in Q1'17 (US$ basis) following 11.7%yoy growth in Q4'17, marking a dramatic and sustained lift in growth after a 12% slide in export earnings between 2011 and 2016. Taiwan's massive electronics sector is well positioned to benefit from a cyclical rebound in consumer electronics, which is expected to run through 2017. The medium-term outlook is less certain, as there is growing global competition in high-end electronics. After 10% growth in 2017, export growth is likely to cool to 4-6% in 2018.

Firm capex for plant & equipment

… construction capex bottoms

Real growth for fixed investment in plant and equipment jumped 9.1% last year as industry prepared for the next chip cycle and new mobile phones. That should result in 5-7% growth this year and about 4% in 2018. Construction capex fell 2.8% last year, as housing starts fell 17.5%. While housing remains weak, construction capex should edge into positive territory this year and rise by 3-6% next year on stronger civil works.

Watch for a lift in consumer demand

As growth in average monthly earnings slipped to 0.6% last year from 2.5% in 2015 and 3.6% in 2014, real growth in consumer spending slowed to 2.1% after averaging 2.8%pa over the prior three years. Taiwanese households are big savers (20-22% of income) and make little use of debt (45% of GDP), so spending drops quickly as the economic outlook deteriorates. With an export recovery underway, consumer spending growth could lift by 3% this year and next. Passenger car sales have already recovered, rising 8%yoy in Q4'16 and Q1'17, after falling 5.7%ytd in the first three quarters of 2016.

Little inflation

… and a strong NT$

Flat food prices pulled headline inflation down to 0.8%yoy in Q1'17 from 1.8%yoy in Q4'16. Even with a lift in export manufacturing and infrastructure work, inflation is unlikely to rise above 1.5% for the next two years, allowing current low interest rates to stay in place. That should help slow the NT$'s recent rise, which reflects a large trade surplus and strong foreign fund inflows into high-tech stocks. From a recent low of 33 to US$1 in March 2016, the NT$ has climbed to 30.3 in mid-April and could break through 30 in 2H'17, particularly if the US$ weakens following a loss of confidence in the Trump administration.

	2014	2015	2016	2017	2018
GDP, real growth, %	4.0	0.7	1.5	2.7	2.6
CPI, year average, %	1.2	-0.3	1.4	1.6	1.5
Official discount rate, year-end, %	1.88	1.63	1.38	1.38	1.38
NT$ to US$1, year average	30.3	31.8	32.2	30.3	28.6

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

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South Korea

Political & policy issues to watch

Korean politics will swing to the left from May 9

Korea is heading to the polls on May 9 to elect a new president, following the impeachment of president Park Geun-hye. She has since been charged with bribery, while leaders of Samsung and Lotte, two of Korea's biggest conglomerates (or chaebol), have been caught up in the case, and have also been charged. Ordinary Koreans are tiring of the family-run chaebol and their cosy relationship with politicians. Centre-left candidates, who promise to reduce their power, are leading the presidential race, with Moon Jae-in of the Democratic party polling at 40%, followed by Ahn Cheol-soo of the People's party at 37%. Combined support for conservative candidates is only 14% in a mid-April poll.

Bringing cooler US ties

… and a bit of fiscal stimulus

US President Trump is likely to find the next Korean government difficult to deal with. First, it is likely to be warmer towards North Korea and China, constraining US policy on North Korea. It will also be harder to deal with if the US tries to renegotiate the Korea-US FTA. If Moon wins (and takes office on May 10), he'll unleash a US$8.9bn spending package on top of the US$356bn budgeted by Park's administration for 2017, aiming to create 810,000 extra public sector jobs over five years and lift the minimum wage next year.

Outlook for the market

Exports lead a mild 2017 upturn

… with local demand helping

The economy started 2017 on a firm note, with Q1'17 exports surging 14.9%yoy, after five straight years with an average 2.2% annual fall in exports (US$ basis). That non-energy imports rose 15.1%yoy in Q1'17 (after an average annual fall of 1.5% over the last five years) suggests a scramble by companies to buy materials and capital goods, even though the March manufacturing PMI was below the breakeven 50 level on falling new orders. Factory output growth quickened to 4.3%yoy in January-February from average annual growth of 0.5% over the prior five years, and consumer sentiment has started recovering from the drama of Park's impeachment. We've lifted our 2017 GDP growth forecast to 2.8% from 2% and that for 2018 to 2.5% from 2.4% due to better exports, firmer consumer demand, a mild lift in plant and equipment capex, and increased public spending.

A mild lift for consumer demand despite constraints

Consumer demand is constrained by record-high household debt (91.6% of GDP in 2016 from 62% in 2005), high youth unemployment (9.8% for 20-29 year olds versus 3.7% for the average of working-age population), and a cooling housing market. Nevertheless, consumer sentiment is improving, as households look forward to a new government while employment growth has risen to 1.4%yoy in Q1'17 from a 1.1%yoy pace over the previous four quarters. Q1'17 car sales, up 1.2%yoy, were in line with 1.3% growth for 2016 with faster growth expected for full 2017. Real growth in consumer spending is expect to lift to 2.6% in 2017 and 2.5% in 2018 from 2.4% growth last year.

Rising capex in plant & equipment

… as construction cools

An 11% rise in construction activity helped lift total capex real growth to 5.3% in 2016, despite a 2.4% fall in plant and equipment (P&E) capex. This year the trends should reverse, as residential starts slowed to 2.9% last year after surging 21.9% in 2015. Extra public spending under a likely Moon administration should cushion a slowdown in construction capex growth, with around 7% real growth likely this year and 4% possible in 2018. Meanwhile, P&E capex is likely to swing to 5-7% growth, with the upside limited by continued offshoring of production.

Low interest rates

… watch out for a continued Won rise

The BOK is in no hurry to lift its policy interest rate (currently at a record low of 1.25%), despite a rise in CPI inflation to 2.1%yoy in Q1'17, as it sees plenty of spare capacity in the economy. Meanwhile, the Won has risen 5.6% on the US$ since early January on a surging current account surplus and near record foreign exchange reserves. While narrowing interest rate differentials should mean a weaker Won on a rising US$, we expect it to continue edging higher into 2018 on a mild Korean growth recovery story.

	2014	2015	2016	2017	2018
GDP growth, %	3.3	2.6	2.7	2.8	2.5
CPI, year average, %	1.3	0.7	1.0	2.3	2.6
BOK Base rate, year-end, %	2.00	1.50	1.25	1.50	2.00
Won to US$1, year average	1,053	1,131	1,160	1,124	1,083

Sources: 2013-2015 government data (NSO, BOK) and CEIC; 2017-2018 forecasts by IMA Asia.

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Indonesia

Political & policy issues to watch

The wash-up from the Jakarta race

…the rise of a more aggressive political Islam

… and a boost for Prabowo as the next president

Jakarta's hotly contested gubernatorial election in April produced a clear win for Anies Baswedan, with 58% of the vote to 42% for incumbent governor, Basuki Tjahaja Purnama (a.k.a. Ahok). The race unexpectedly became the central political contest midway through the first five-year term of President Joko Widodo (a.k.a. Jokowi). A year ago, the election looked like an easy win for Ahok, despite being a Christian of Chinese descent in a mainly Muslim country, thanks to his reputation for good government. Yet six months ago, an unknown radical Islamic group, the Indonesian Defenders Front (FPI) launched a hard-hitting attack on Ahok as a non-Muslim. The use of fake news, large public protests, and an aggressively political Islam has shifted the country's political debate. It has also vaulted Prabowo Subianto, who lost the 2014 presidential race, into a strong position for the 2019 race. Prabowo backed Anies and is close to FPI.

Jakarta still ends up with a good governor

Jakarta should see a smooth transition to its new governor in October, when Ahok steps down. Anies and his running mate, Sandiaga Uno, have reputations as reformists and moderates, largely promising to continue the "good" policies of the Ahok administration. Both have good track records and no corruption scandals in their background.

FDI lifts despite bad press over Freeport's mine

Despite speculation, President Jokowi is unlikely to announce a cabinet reshuffle in the wake of the Jakarta election. Meanwhile, the government is pressing ahead with its demand for a bigger stake in Freeport's Grasberg mine, and has granted a six-month export permit for copper concentrate, which will help export earnings and tax revenues. FDI inflows rose 5.5%yoy in Q1'17 to US$7.3bn after three years of virtually no growth.

Outlook for the market

A mild lift in growth

… due to better exports and a slow rise in local demand

We retain last month's forecast of 5.4% growth for 2017, with a rise to 6.1% in 2018 thanks to better export demand and a gradual lift in domestic demand. Combined, they'll produce a mild upturn, which is apparent in vehicle sales, with 5.8%yoy growth in Q1'17 after falling some 14% over 2013-16. Local demand has been undercut by a host of factors, ranging from a two-year drought (El Nino related and ending in late 2016) and a collapse in commodity prices, to painful cuts to fuel subsidies and little if any growth in capex on plant and equipment for four years. Each of those problems has ended or is fading. Meanwhile, ahead lie stronger exports and a possible return to investment grade by S&P.

Good exports should help GDP & the Rupiah

The value of Indonesia's non-oil and gas exports surged 18%yoy in Q4'16 and then 22%yoy in Q1'17 (US$ terms). As local demand has been weak, that pushed up the trade surplus and supported the Rupiah. Export volumes on the GDP real growth measure were also up a firm 4.2%yoy for Q4'16, adding to GDP real growth, after eight quarterly falls. We expect export growth of 8-10% this year and 4-6% in 2018 (US$ values).

Better demand from consumers as drought fades & sentiment lifts

While vehicle sales have perked up, retail sales growth slumped to 4.2%yoy in Q1'17 from 11-14% for each of the prior five years. Notably, food and drink sales growth slowed to 5.8%yoy in Q1 while appliance sales slipped to 2.3%yoy after both categories grew 9.9% in 2016. We expect real growth in consumer spending to lift to around 5.7% this year and next from around 5% for each of the last three years, as drought conditions ease across rural Indonesia and consumer sentiment lifts.

Low inflation and a slower slide for the Rupiah

Inflation of 3.7%yoy in Q1'17 was in line with the prior five quarters with a mild rise ahead, as local demand lifts. The Rupiah has edged up from a recent low of 13,417 to US$1 in last December to 13,351 in late April thanks to a rising trade surplus and mild capital inflows in expectation of an S&P upgrade. After decades of falling at an average annual 3%, we expect a modest 1-2% fall in 2017 and 2018 thanks to better macro policies.

	2014	2015	2016	2017	2018
GDP, real growth, %	5.0	4.9	5.0	5.4	6.1
CPI, year average, (2012=100), %	6.4	6.4	3.5	4.0	4.9
Central bank rate (7-day RR) at Dec %	-	6.25	4.75	5.25	6.50
Rupiah to US$1, year average	11,868	13,389	13,308	13,536	13,825

Sources: 2013-2015 government data (BPS, BI) and CEIC; 2017-2018 forecasts by IMA Asia

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Malaysia

Political & policy issues to watch

The political risk outlook improves

… as PM Najib shrugs off 1MDB

… & plans an early election

PM Najib Razak has until August 2018 to call Malaysia's next election, although he is likely to bring it forward to later this year to take advantage of an improved political position. He has shrugged off the 1MDB scandal, despite a steady stream of negative news from investigations in the US, Switzerland, and Singapore. 1MDB has also slashed its debt by selling core assets to Chinese SOEs. That eases concern that 1MDB risks might harm local banks and major projects. As such problems fade, Najib's UMNO-led coalition should improve on its poor showing in the 2013 election, when it lost the popular vote but retained power. UMNO will be helped by a fragmented opposition and cash handouts in the latest budget (FY2017) to farmers, public servants, and low-income earners.

A rebound in oil prices helps the government

Since 2013, the government has been under pressure from falling revenues in the oil & gas sector, with total public revenues dropping 7.5% in the year to June 2016. Since then, however, oil prices and government revenues have lifted. Moreover, PM Najib also secured US$34bn worth of Chinese business deals last November, and Saudi oil giant Aramco has announced it will invest US$7bn for a 50% stake in the Refinery and Petrochemical Intergraded Development (RAPID) project developed by Petronas, the national oil company, in the southern state of Johore. Such developments point to a revival in fixed investment growth over the next few years.

Outlook for the market

A better growth outlook

… as exports and capex lift

In addition to the oil price, Malaysia's outlook depends on what happens to other exports and private fixed investment, both of which have been very weak in recent years, and how households continue their adjustment to less generous support from the government. We've also factored in a lift in government spending as late 2017 elections approach. In aggregate, the outlook is improving, so we've lifted our 2017 GDP growth forecast to 4.3% from 4% last month, while our 2018 growth forecast remains unchanged at 4%. That puts real annual growth in line with the two-decade average to 2016 of 4.6%.

Oil & gas lead the export rebound

… a milder lift for manufactured goods

Malaysia's exports collapsed over the five years to 2016, with an average fall of 3.4%pa (US$ basis). Energy exports led the five-year slump (-6.3%pa) and the latest four-month recovery (up 15.5%yoy). Manufactured exports, which dominate at 63% of total exports, fell 1.6%pa over 2012-16, with a recovery to 6.6%yoy growth for the four months to February. For 2017, we expect export growth of about 8%, easing to 5% in 2018. The lift for manufacturing has been modest, with the March PMI stuck below the 50 expansion/ contraction level, due to falling new orders and rising inventories. But with help from local demand, industrial production in 2017 and 2018 should grow close to last year's 4.3%.

Big projects should lift capex growth

Fixed investment real growth should lift to around 3.6% in 2017 and 2018 from 2.7% in 2016 thanks to big projects (the RAPID project, rail projects in peninsula Malaysia, including a high speed link to Singapore, and a highway between Sabah and Sarawak in East Malaysia). That should offset cooler growth in an overbuilt residential market.

While consumers trim spending

Real growth in the consumer sector is expected to slow to 4.7% in 2017 and 3.7% in 2018 after a strong 7.3%pa expansion over 2003-16. High household debt (88.4% of GDP), a cooling jobs market, and softer house prices will slow spending growth.

Inflation briefly lifts with a firmer M$

A steep M$ fall from mid-2016 contributed to a 4.3%yoy jump in inflation in Q1'17. However, Bank Negara is unlikely to lift its policy interest rate this year, as spare capacity in the economy should contain prices. In addition, the M$ has stabilised against the US$ since late 2016, and should continue to find support from firm crude oil prices.

	2014	2015	2016	2017	2018
GDP, real growth, %	6.0	5.0	4.2	4.3	4.0
CPI, year average (2010=100), %	3.2	2.1	2.1	3.8	3.5
Central bank overnight policy rate, Dec, %	3.25	3.25	3.00	3.00	3.50
Ringgit to US$1, year average	3.27	3.90	4.14	4.47	4.48

Sources: 2013-2015 government, Bank Negara, & CEIC; 2017-2018 forecasts by IMA Asia.

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Philippines

Political & policy issues to watch

Pres. Duterte's ugly but astute local politics

Less than a year into his single six-year term, President Duterte continues to polarise opinion. Foreigners are appalled by his support for vigilante killings in his war on drugs, and are worried by abrupt policy swings and the undermining of democratic institutions. By contrast, his opinion poll support stands at 78%, as voters back his campaign to tackle drugs and deliver more equitable growth. Critically, Duterte has strong support in Congress, in part because he has wound up the "pork barrel" corruption case, in which around 100 lawmakers were implicated in the theft of over US$200m in public funds.

Plus, some big development goals

Duterte's goal is to lift GDP/capita above US$11,000 by 2040 from $2,976 in 2016 by pushing development programs into the provinces. To achieve that goal, infrastructure spending will have to lift from 4.3% of GDP in 2015, to 5.4% this year, and 7.4% in 2022, the last year of his term. A foreign policy swing towards China in 2016 has helped, with China committing US$3.4bn to infrastructure projects and Chinese firms promising another $10.3bn in investments. Meanwhile, Japan has promised $8.6bn over five years.

… which require major tax reforms

However, if Duterte is to fund a promised US$160bn in infrastructure works to 2022, he'll have to lift tax revenue from just 14% of GDP (compared with 16% for Thailand and over 20% for advanced economies). Four tax reform bills aim to cut the top personal tax rate to 25% from 32%, raise the tax-free threshold, lower inheritance tax, cut the corporate tax rate to 25% from 30%, lower tax exemptions, lift fuel and vehicle taxes, broaden VAT, and lift taxes on cigarettes, alcohol, and (possibly) sugary drinks.

… & possibly a tax amnesty

Following Indonesia's successful tax amnesty, the Philippines is considering a tax amnesty to lift revenues. Like Indonesia's, it would aim to encourage the return of overseas funds with very low penalty rates and immunity from prosecution. Preparation will likely take a year or more, as bills will need to be drafted and passed by Congress.

Outlook for the market

Scope to sustain 6%+ growth

… if inflation is contained & bills are passed

The Philippines should remain one of Asia's fastest growing economies thanks to favourable demographics, steady growth in offshore income from business process outsourcing (BPO) and offshore Filipino workers (OFWs), and Duterte's infrastructure plan. Key challenges will be containing inflation, as growth is bumping up against capacity constraints, and maintaining Congressional support for Duterte's reforms. We are cautiously optimistic on both issues, suggesting GDP should expand by 6.0-6.5% in 2017 and 2018, well above its two-decade average pace of 4.8%.

Surging capex drives local demand

… but also leads to a big trade deficit

Central to the outlook is a jump in domestic demand growth to 10.8% in 2016, with a firm 7-8% rise likely in 2017 and 2018. Last year's 23.5% surge in fixed investment should moderate to a more sustainable 10-13% pace, which is well above a two-decade average rate of 5.7%. The challenge will be skilled labour shortages and surging imports of capital goods (up 40% to a record US$27bn in 2016). Fortunately, strong BPO and OFW income kept the current account in a narrow surplus in 2016, despite a doubling in the trade deficit to US$24bn. Meanwhile, motor vehicle sales surged by some 25% in each of the last three years, with a record 359,572 units sold in 2016. Buoyant consumer confidence and steady OFW remittances should help consumer spending grow 6.5-7.0%pa in the next two years, with some upside in 2018 if income tax cuts are delivered.

Watch for interest rate hikes and a softer Peso

Inflation hit a 28-month high of 3.4% in March, and will likely breach the central bank's 4% ceiling soon, prompting a mild rate hike cycle. A falling current account surplus has made the Peso one the region's weakest currencies recently. However, capital inflows, a mild rate rise, and OFW and BPO income should keep the Peso in a 49-52 range in 2017-18.

	2014	2015	2016	2017	2018
GDP growth, %	6.2	5.9	6.8	6.5	6.4
CPI, annual average, %	4.1	1.4	1.8	4.0	4.2
Central bank reverse rep. rate, year end	4.00	4.00	3.00	4.00	4.50
Peso to US$1, annual average	44.4	45.5	47.5	50.5	51.7

Sources: 2013-2015 BSP data and CEIC; 2017-2018 forecasts by IMA Asia.

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Singapore

Political & policy issues to watch

The challenge of much weaker trend growth

The PAP, which has ruled Singapore since independence in 1965, is firmly entrenched, receiving 70% of the votes in the 2015 election. Yet, despite a tradition of strong long-term planning, the city faces major policy challenges, which reflect painful transitions in the global economy, and a popular rejection of using migrant labour to sustain growth. Growth for the 20 years to 2012 averaged 6.4%pa, but halved to 3.1%pa for the last four years. Our 2.8%pa forecast for 2017-21 reflects a difficult realignment facing the city.

Reflects big cuts to migrant labour inflows

… and falling productivity

Two central challenges for the economy are weaning itself off a high reliance on migrant workers and reversing a fall in productivity growth. Reliance on migrant workers saw the non-citizens portion of the population grow from 9.6% in 1969/70 to 39.2% in 2015/16. For the two decades to 2011/16 that meant average growth of 7.1%pa for non-citizens. After a sharp drop in support at the 2011 election, the government was forced to slow growth in the non-citizen population to 1.8% for 2015/16. Apart from slowing GDP growth, that challenges the future of labour-intensive manufacturing and parts of the SME sector, with rising pressure on both to relocate. At the same time, productivity growth has fallen by 0.7%pa over the four years to 2016, after average growth of 1.2%pa for the 20 years to 2012. Rapid growth in new industries, like aerospace and healthcare, has failed to halt the productivity slide. We can see no easy fix, thus our muted five-year forecast to 2021.

… and a cooler property market

Weak growth also reflects the successful cooling of an overheated property market. After home prices surged 62% from 2009 to 2013, a series of curbs produced a 12% fall in prices. Some curbs are now being eased, which could lift real estate transaction volumes. However, a rebound in prices seems unlikely, as mortgage rates have crept up to 3.4% on a rising US Fed rate from a record low of 2.9% in early 2015.

Outlook for the market

A mild recovery for 2017-18

After four quarters of sub 2% growth, GDP lifted by 2.9%yoy in Q4’16 and 2.5%yoy in Q1’17 thanks to stronger exports. That suggests a mild recovery to 2.7% growth in 2017, based on export growth of 9-11% this year (US$ basis) after a 4% average annual fall in exports for the five years to 2016. Local demand growth, which hit a 13-year low of 0.2% in 2016, should also lift, as growth picks up in the services and construction sectors. A continuation of those trends should push GDP growth above 3% in 2018.

… as exports recover after 5 bad years

Non-oil domestic exports surged 15.2%yoy in Q1’17, after falling 2%pa in the last five years. That drove an 8%yoy lift in industrial output in Jan-Feb, as semiconductor production jumped 48%yoy in the same period. The current export surge should continue for several more months, as export orders rose to a 28-month high in March. However, the pace should cool by mid-year as global inventory rebuilding eases.

… capex should also lift

Fixed investment growth fell to a 13-year low last year, as weak construction and manufacturing sectors, and low business confidence saw firms scale back capex. However, growth in loans for construction, transportation, business services, and retail & wholesale trade has picked up in recent months, suggesting capex growth could recover by a mild 1-3% in both 2017 and 2018.

… & consumers should spend more

Despite good wage growth of 3.7% across all industries last year, real growth in consumer spending slipped to 0.6% in 2016 from an average pace of 4.5% for the prior 20 years, as consumers reacted to a weak property market (85%+ of households own their homes) and a weak economy. However, retail sales (ex-vehicles) have stabilised in recent months, suggesting a return to 2.0-2.5%pa consumer growth for the next two years.

Little inflation & a steady S$

Better demand lifted inflation to 0.6%yoy in Q1’17 from zero in Q4’16, with around 1% expected in 2017 and 1.5% in 2018. Monetary policy, which in Singapore guides the currency against a basket of currencies, should remain in a neutral stance. That is likely to keep the S$ trading in a 1.38-1.41 range against the greenback in 2017 and 2018.

	2014	2015	2016	2017	2018
GDP, real growth, %	3.6	1.9	2.0	2.7	3.2
CPI, year average, %	1.0	-0.5	-0.5	1.0	1.5
3-month interbank interest rate, Dec, %	0.46	1.19	0.97	1.10	1.20
S$ to US$1, year average	1.27	1.37	1.38	1.39	1.40

Sources: 2013-2015 government data and CEIC; forecasts for 2017-2018 by IMA Asia

Thailand

Political & policy issues to watch

Gains in short-term political stability

Almost three years after a military coup, PM Prayut's government has achieved short-term political stability. With political debate suppressed, opinion poll support for his government has climbed to 83%, as civic order has been restored, corruption has been reduced, and rural development programs have been launched. The stable accession of King Maha Vajiralongkorn last December, after the death of his father, King Bhumibol Adulyadej, also helped. In late October, King Bhumibol will be cremated. Firms should be careful of social sensitives then, but it should bring an end to a year of mourning.

… longer-term gains are possible

While the long-term political outlook is less clear, it is gradually improving. A new constitution, which ensures military control over the next elected governments and affirms the King's power as final arbiter, has been approved. That opens the way to new elections in 2018, in which two issues will be critical: the level of popular support for a military-guided government; and whether the pro-Thaksin forces that have dominated and roiled Thai politics for 15 years have been neutralised. Progress is being made in both areas.

The EEC plan to revitalise export manufacturing

Prayut's government has also come up with a better development plan after its early efforts faltered. Central to that is an industrial revitalisation strategy, which hinges on the success of the Eastern Economic Corridor (EEC). The EEC promises an attractive investment regime, and it could become the industrial hub for ASEAN with focus industries including automotive, electronics, biotechnology, robotics, aviation, chemicals, and healthcare.

Outlook for the market

A mild recovery builds through 2017

Thailand's weak recovery from 2015 should build in 2017, with exports, manufacturing, and tourism all expected to lift. The key issues to watch include the longevity of the export recovery, whether the EEC project can trigger a recovery in private capex, and whether political stability can be maintained. We think the signs are positive, suggesting GDP growth should improve towards 3.7% this year and 4.1% next year (unchanged from last month's forecast). That's above the two-decade average to 2016 of 3.1% growth.

… as capex recovers after four weak years

Fixed investment growth has averaged just 1% for the four years to 2016, as a surge in public construction capex over 2015 and 2016 (an average 23%pa) failed to ignite private construction capex (stuck at 0.7%pa) or plant and equipment capex (-0.4%pa). We think conditions now favour a recovery in private construction capex (4.5%pa growth for 2017 and 2018) and plant and equipment capex (4.8%pa). With public construction capex likely to sit around 8%pa growth, that should see total fixed investment grow around 5% this year and next year, which is above the 3.6%pa pace for the two decades to 2016. Much depends on a good start for the government's Bt1.8trn (US$51bn or 13% of GDP) infrastructure program to 2022, with some 20 projects set to start in 2017.

Steady growth in consumer demand

Real growth in consumer demand rose to 3.1% in 2016 from 2.2% in 2015, and should stay at about that pace in 2017 and 2018, with higher farmer incomes, lower income taxes, and a 3.3% rise in the minimum wage for Bangkok and environs helping. Underscoring better sentiment, vehicle sales rose 15.4%yoy for the first two months of 2017, after falling 3.9% in 2016 and 9.3% in 2015.

A modest export recovery

Export growth should lift to 5-6% (US$ basis) in 2017 and 2018 after an average fall of 0.6%pa over the prior five years. The mild export recovery should support a modest 4% rebound for manufacturing in 2017 and 2018 after four years of average growth at 1.2%pa.

A firm Baht helps to cap inflation

Some US$3.4bn in foreign capital has poured into Thailand this year, helping to push the Baht up 4%ytd and making it one of Asia's strongest currencies. While that will help cap inflation this year, the Baht should start softening by 2018 on a rising US$.

	2014	2015	2016	2017	2018
GDP, real growth, %	0.9	2.9	3.2	3.7	4.1
CPI (2002 index), year average, %	1.9	-0.9	0.2	2.0	3.2
Central bank, policy rate, year end, %	2.00	1.50	1.50	2.00	3.00
Baht to US$1, year average	32.5	34.2	35.3	34.4	34.9

Source: 2013-2015 data from the IMF and CEIC; 2016-2018 forecasts by IMA Asia.

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Vietnam

Political & policy issues to watch

Stable politics and good policies

A stable leadership reshuffle last year and pro-growth policies under a government led by PM Nguyen Xuan Phuc suggest that trade and investment-friendly policies will continue. Policing of environmental rules has been tightened after last year's coastal pollution disaster, which triggered mass protests. Increased efforts to curb corruption are also apparent. Such changes not only help political stability, but also help the operating environment, with Vietnam's ranking in the World Bank's annual ease of doing business survey climbing to 82nd last year from 91st in 2016.

A 7% growth target

… as modern Vietnam replaces rural Vietnam

The government aims to deliver 6.5-7.0% growth in 2016-20, up from 5.9%pa in 2011-15. Getting there requires the continued transformation of the economy, with services and the broad industry sector (manufacturing, mining, and utilities) rising to 85% of GDP by 2020 from 67% in 2016. That requires agriculture, fishing and forestry (the primary sector) to fall from 15% of GDP in 2016 to 10% by 2020, with construction stable around 5-6%. The continued transfer of workers from the primary sector (44% in all workers in 2014/15, down from 55% in 2004/05), will support urbanisation and consumer growth.

Three risks to watch

… the Dong, public debt, & poor lending

Three risks need watching. First, foreign reserves, although rising, remain below the three months of imports typically required for exchange rate stability. Given surging imports of capital and consumer goods, that leaves the currency exposed to an abrupt fall if export growth cools (see our Dong comments below). Second, public debt has risen to its mandated cap of 65% of GDP, which limits the government's ability to support much-needed infrastructure investment. Attracting private funding will be essential. Third, rapid credit growth, which is targeted at 18% for 2017, could weaken the banking sector, which continues to struggle with bad debts and poor lending practices.

Outlook for the market

A weak start to 2017

… with growth to lift from Q2

Vietnam is unlikely to meet the government's 6.7% GDP growth target for 2017, after growth slowed to 5.1%yoy in Q1'17 from 6.2% in full 2016. Activity weakened across the major sectors, with agriculture struggling from the lingering effects of last year's severe drought, and manufacturing easing due to a slowdown in Samsung smartphone production. However, the growth outlook remains positive. GDP growth typically firms from Q2, as public capex normally picks up through the year and manufacturing tends to lift by Q4. That should see full-year growth reach 6.1% in 2017 (down from a previous forecast of 6.5%), with about 6.3% likely for 2018, well above the 5.9%pa pace of 2011-15.

… as exports firm on better global demand

A big 32% drop in electronic components production in March coincided with weaker phones & spare parts exports in Q1'17, which fell 6%yoy from growth of 13.5% in full 2016. Still, exports increased by 15.2%yoy in Q1'17, thanks to a lift in textiles, footwear, and computer & electronic component exports. Firmer export demand on the back of a synchronised global upturn and the start of Vietnam's EU free trade agreement in 2018 should see exports lift some 10-12%pa in the next two years from 9% growth (US$ basis) in 2016. Along with continued investment in new factories, that should see manufacturing grow around 11% in 2017 and 2018, about its average pace in 2015-16.

… amid a steady rise in capex and consumer demand

Average FDI inflows of US$15.5bn in each of the last three years has stoked growth in construction and manufacturing, and helped lift capex to 30% of GDP in 2016 from 27% in 2012. The consumer market should continue to benefit from favourable demographics, low unemployment, rising disposable incomes, and upbeat consumer confidence. Passenger vehicle sales almost doubled to 159,000 units in 2016 from 79,000 in 2014. Consumer demand should grow 7-8%pa in 2017 and 2018, a bit above its average pace in 2005-15.

Watch out for a weaker Dong

March's 4.7%yoy inflation rate is above the central bank's 4% ceiling, suggesting higher interest rates are needed. With the trade balance likely to slip into deficit and the current account set to weaken, we now expect the Dong to slide around 2-3% this year and next year, up from a 1.2% fall in 2016 (and prior forecasts of 1-2% falls in 2017 and 2018).

	2014	2015	2016	2017	2018
GDP, real growth, %	6.0	6.7	6.2	6.1	6.3
CPI, yoy, % (2005=100 from 2007)	4.1	0.6	2.7	4.4	3.9
Central bank refinancing rate, year-end, %	6.50	6.50	6.50	7.00	7.00
Dong to US$1, year average	21,148	21,677	21,932	22,499	23,203

Source: 2013-2015 data from the IMF and CEIC; 2017-2018 forecasts by IMA Asia

India

Political & policy issues to watch

A big win for PM Modi in UP

… will help him push reforms

… and win a 2nd term in 2019

Despite last November's controversial demonetisation, which hurt many poor Indians, the ruling BJP did well in state elections in March, notably winning in Uttar Pradesh (UP, India's largest and one of its poorest states). That will help shift the balance of power at the national level, where PM Modi's reform program has been frustrated by opponents in the upper house. The March results also underscore the decline of Congress—the major opposition party—and suggests that PM Modi should win a second five-year term in 2019. It may also contribute to firmer national growth by bringing better government to UP. Last month, we characterised Yogi Adityanath, UP's new Chief Minister, as a Hindu firebrand who would aggravate communal tensions. Our colleagues at IMA India note that this is not the case, and that the new chief minister should improve administration in what has been one of India's worst governed states. Better state administrations, in which Modi played a part when he was Chief Minister of Gujarat, is critical to lifting India's growth.

The GST start on July 1 should be delayed

… a high risk of confusion that will hurt growth

All attention is now focused on the introduction of a Goods & Services Tax (GST), which is scheduled for July 1, although there are growing calls for a delay due to the complexity of four rates (from 5% to 28%) and the absence of information about which rate will apply to specific goods and services. Under current legislation, the GST introduction can take place at any time before September. A delay beyond that would require a series of votes in parliament, which PM Modi should manage, as the GST has opposition support. Since last November, our operating risk rating for India has been Moderate with a Negative outlook because of risks associated with poor GST implementation.

Outlook for the market

The impact of demonetisation through to Q1'17

… small, cash-only businesses & poorer consumers hit hard

… milder impact on middle income households & big businesses

Last November, we picked vehicle sales as the best guide to the impact of demonetisation. Total vehicle sales (including 2 and 3-wheeler) fell 4%yoy in Q4'16 and 0.8%yoy in Q1'17, after growth of 13.8%ytd for Q1-Q3 2016 – so a sharp slowdown. Note that the first three quarters of 2016 saw a strong recovery from a drought-affected 2015 (just 1.8% growth). The passenger vehicle segment (cars and light vehicles) was least affected, with growth of 8.9%ytd by Q3'16 slowing to 1.8%yoy for Q4'16 and rebounding to 11.1%yoy growth in Q1'17. A big public sector pay hike (done once every 10 years) helped. 3-wheeler sales (for tuk-tuks, a classic small cash-only business) were hardest hit. After growth of 15.7%ytd by Q3'16, they fell 18.3%yoy in Q4'16 with a bigger 24.4%yoy fall in Q1'17. Reports of continued cash shortages at bank ATMs also suggest that India's cash-only economy remained constricted in Q1'17. Two-wheeler sales, a guide to low-income households, fell 4.6%yoy in Q4'16 and another 2.3%yoy in Q1'17, after growth of 14.6%ytd by Q3'16. By contrast, commercial vehicle sales suggest that most businesses weathered demonetisation, with a sales fall of 1.1%yoy in Q4'16, roughly in line with a 2%ytd fall by Q3'16, followed by a rebound to 5.7%yoy growth in Q1'17.

Modern India is doing OK

… rural India is hurting

Bizarrely, India's new GDP series says that demonetisation triggered an acceleration in real growth for consumer spending to 10.1%yoy in Q4'16 from 7.7%ytd for the first three quarters. Our own clients split into three groups on what happened. Those dealing B2B (excluding the tuk-tuk end of the market) mostly report stable or improving business through demonetisation. Those serving the urban middle class saw a slight dip. Those serving rural India report major falls and a very slow recovery.

Bad debt limits India's outlook

… & threatens the Rupee

We doubt India got the 7.4% growth officially reported for 2016. In Q4, we estimate growth slipped to 4-5%yoy (not the official 7.5%) from 7.7%ytd by Q3'16. Full year 2016 growth would have been around 6.7% and that guides our forecast of 6.8% for 2017. The main challenge this year is a widening balance sheet crisis for industrial India, which is reflected in a jump in bank non-performing loans and weak bank lending. Those problems will keep the Rupee under pressure, with 3-4% annual falls in 2017 and 2018.

Calendar year starting January	2014	2015	2016	2017	2018
GDP (MP, 2011-12), real growth, %	6.8	7.4	7.4	6.8	7.2
Inflation - CPI, %	6.7	4.9	5.0	4.0	5.1
RBI repo rate, December, %	8.00	6.75	6.25	6.50	7.25
Rupee to US$1, year average	61.0	64.1	67.2	69.5	72.0

Sources: 2013-2015 data from the government (NCI, RBI) and CEIC. 2016-2018 forecasts by IMA Asia with guidance from IMA India.

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Australia

Political & policy issues to watch

Frequent leadership changes & policy gridlock

… as politics fragments and fringe parties rise

Despite 25 years of uninterrupted growth, Australians have become disillusioned with mainstream politicians and their parties. They are unhappy about slow wage growth and rising inequality, as well as the demise of long-established companies if not industries (like car building), soaring home prices in the main cities, and the casualisation of the workforce (part-time jobs grew 4.1% in 2016 while full-time jobs rose just 0.5%). Voters have been deserting the mainstream for fringe parties who oppose imports, foreign investment, and migrants. This makes life difficult for the Coalition government led by PM Malcolm Turnbull, as it has a one-seat majority in the lower house and must rely on fringe parties to pass bills in the upper house. His fragile hold on office also exposes Turnbull to the demands of right-wing conservatives in his own Liberal Party. More generally, it means frequent changes in leadership and gridlock on almost all major policies, which hinders major investment.

The 2017/18 budget may tackle housing

… but not the deficit

In his May 9 budget speech, Treasurer Scott Morrison is likely to focus on housing affordability, as the average home price has doubled in Sydney and Melbourne since 2006. The key question is whether he'll tackle negative gearing, which allows investors to buy homes and offset any loss against their income tax obligations. Despite nine straight budget deficits, he's unlikely to tighten fiscal policy. Net public debt is under 20% of GDP, interest rates remain low, and rising commodity prices should help revenues.

Outlook for the market

Firm GDP growth thanks to exports

… masks weak local demand growth

Treasurer Morrison is likely to forecast continued growth in a 2.5-3.5% band in his budget, in part thanks to a recovery in commodity prices over the last year. That saw export earnings jump 44% (US$ basis) for the first two months of 2017. Even though the value of commodity exports fell sharply over most of 2013-16, real GDP growth (a quantity measure) stayed at 2.4%pa as export volumes for coal and iron ore rose quickly. The challenge for many firms is that once that is stripped out, domestic demand growth (mainly consumer demand, public spending and fixed investment) was just 1.2%pa. With some minor adjustments, that pattern is set to continue, with 3% GDP growth in 2017 and 2.8% in 2018.

Challenges for capex growth

… in mining, manufacturing, and housing

The biggest challenge for domestic demand has been falling fixed investment for the last four years. Central to that is a 35% fall in mining-related capex over the last three years. After a 19.5% drop last year, the fall will likely halve this year and halve again in 2018. Capex for plant and equipment (a mix of manufacturing, mining and other sectors) has also fallen for four years. On the manufacturing side, a big part of that has been the winding down of production and now the closure of Australia's three remaining car builders (Ford last year and GM and Toyota this October). Capex for housing helped cushion the downturn, with dwelling starts up 11% in 2013, 19% in 2014, and 12% in 2015. But growth in commencements slowed to 3% last year and it's unclear if Treasurer Morrison can fix that with his May budget. Overall, the fall in capex should slow if not halt in 2016 and 2017, but it remains the weakest part of domestic demand.

Firm consumer demand relies on rising debt

Consumers have been the strongest component of domestic demand, although that's been achieved with a big run-up in household debt (now 125% of GDP from 100% in 2005). That enabled steady consumer real growth of around 2.7% over the last three years. While the soaring debt is mostly mortgage related, FMCG firms report consumers swinging to cheaper brands as their budgets come under pressure. In the absence of a sharp correction in the housing market, we expect consumer demand to grow 2.6% in 2017 and 2.7% in 2018.

A bit more inflation

… and a steady A$

With inflation edging up to 2.1%yoy in Q1'17 from a 1%yoy low on Q2'16, the RBA's interest rate cutting cycle has come to an end. The central bank is increasingly concerned about low interest rates fuelling Australia's housing bubble and is likely to start a gradual monetary tightening cycle later this year. Rising commodity prices helped the A$ resist downward pressure from a narrowing interest rate differential with the US. These two opposing forces are likely to keep the A$ within a 0.74-0.78 range against the US$ over 2017-18.

Year ending December 31	2014	2015	2016	2017	2018
GDP, real growth, %	2.8	2.4	2.5	3.0	2.8
CPI, year average, %	2.5	1.5	1.3	2.3	2.6
RBA cash rate, year-end, %	2.50	2.00	1.50	1.75	2.50
A$1 = US$, year average	1.11	1.33	1.35	1.32	1.30
US$1 = A$, year average	0.90	0.75	0.74	0.76	0.77

Source: 2013-2015 data from the ABS; 2016-2018 forecasts by IMA Asia

New Zealand

Political & policy issues to watch

Government could change at the Sept 2017 elections

A year ago, the National Party looked set to cruise to a 4th straight victory in elections scheduled for September 23. Since then, its lead over a Labour/Green alliance has fallen, with some polls putting the opposition ahead. The main challenge for the Nationals is that John Key, their popular leader who won the last three elections, stepped down as PM last December, and Bill English, who took over, lacks Key's touch. English has been trying to soften his technocratic image, acquired during his time as a reforming finance minister in successive Key governments. He has increased social spending and refined immigration policy by raising the salary threshold for accepting skilled migrants. Moreover, he'll be able to announce personal tax cuts soon, thanks to repairs to public finances he championed as finance minister. PM Key brought political stability along with a steady reform agenda, and that helped sustain growth and lower risk. While the election is now too close to call, we don't expect a significant loss of political stability or policy making capacity.

Surging inward migration leads the policy debate

With net inward migration reaching a record-high 71,932 in the year to March, migration policy and the related impact on housing and public services has moved to the centre of the policy debate this year. It's also central to the economic outlook, as migration boosted total population growth to 2.1%yoy at December 2016, and that has added a percentage point to GDP growth. English's modest changes to immigration policy (see above) won't change the current 70,000 annual net inflow in 2017. By contrast, Labour has said it would slash inward migration in 2018 without giving details.

Outlook for the market

GDP continues growing above 3%

… supported by fast population growth

Strong net inward migration helped lift GDP growth to 4% in 2016 from 3.1% in 2015 and 2.3%pa over 2010-14. Record net inward migration reflects strong inflows and a sharp fall in outbound migration. Apart from boosting GDP growth, it has also helped curb inflation by ensuring a strong supply of new workers, particularly in the booming construction sector. Without that, wage-push inflation would have emerged over a year ago, which would have forced much higher interest rates to cool the economy. With no real change to migration policy this year under the Nationals, GDP should grow 3.5% this year. We've forecast 3.4% growth for 2018 on the assumption that PM English manages to hold onto power in September with the help of tax cuts.

A boom in housing is set to cool

Fixed investment grew 5.7% in 2016 thanks to an 11% surge in housing investment. Non-residential capex grew at a much slower 3.8%. Fuelled by record-low interest rates and an immigration boom, NZ's housing market is in bubble territory. The median home price hit a new record high in March, but recent declines in residential transactions and housing approvals point to cooler conditions ahead. Unless non-residential activity picks up, we expect fixed investment growth to slow to around 3.7% in 2017 and 3.3% in 2018.

Strong consumer growth continues

Private consumption growth accelerated to a multi-year high of 4.2% in 2016 from 2.9% in 2015 and 3.0%pa in 2010-14. Consumer demand was boosted by an immigrant-led lift in population, strong jobs growth (4.6% in 2016 from 2.2% in 2015), and the positive wealth effect of a booming housing market. We expect consumption to keep growing faster than GDP at 3.9% in 2017 and 3.7%yoy in 2018.

Rising inflation and interest rates to support NZ$

The RBNZ is likely to start lifting its policy interest rate later this year from the current all-time low of 1.75%, as the CPI edged up to 2.2%yoy in Q1'17 from 1.3%yoy in Q4'16 and an average of 0.4%yoy in Q1'15-Q3'16. Inflation is heading above 3% by 2H'18, as the economy is running at capacity. This should provide some support to the NZ$, which has climbed 14% to 0.70 against the US$ from an August 2015 low.

Calendar years	2014	2015	2016	2017	2018
GDP(Expenditure), real growth, %	2.9	3.1	4.0	3.5	3.4
GDP(Production), real growth, %	3.8	2.4	3.1	3.5	3.4
CPI, year average, %	1.2	0.3	0.6	2.4	3.1
Official cash rate, year end, %	3.50	2.50	1.75	2.00	2.75
NZ$1 = US$, year average	0.83	0.70	0.70	0.70	0.72
US$1 = NZ$, year average	1.20	1.43	1.43	1.44	1.38
NZ$1 = A$, year average	1.09	1.07	1.07	1.09	1.06

Source: 2013-2015 data from Statistics NZ; 2016-2018 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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