

Good MornING Asia - 18 February 2020

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EM Space: Real economic impact from Covid-19 starting to surface

- **General Asia:** Consumer electronics makers warn that the Covid-19 outbreak is set to hurt both production and demand for their products. Emerging markets will likely pullback on Tuesday given their exposure to the electronics sector and with ASEAN export sectors all supporting China's vast supply chain. Reports of an anti-viral drug may help ease some concerns although caution is still likely to dominate given the Covid-19 episode.
- **Singapore:** The [2020 Budget](#) headlines will start hitting the terminals once finance minister Heng Swee Keat begins his budget speech at 3 pm local time. An adverse impact of Covid-19 on key sectors of trade and tourism could push the economy into recession this year, a possibility we also highlighted yesterday for some other Asia economies (see our notes on [Japan](#) and [Thailand](#)). Hopes are being pinned on a significant fiscal stimulus to avert this crisis, and the authorities seem likely to deliver. This will likely make this the most market-friendly budget for years.
- **Thailand:** GDP growth slipped to a five-year low of 1.6% YoY in the final quarter of 2019. With the coronavirus threatening trade and tourism, it looks as if Thailand is in for a prolonged downturn. Unlike Singapore, the lack of timely, adequate, and effective policy support makes a recession more likely than not. We are cutting our 2020 growth forecast to

- 1.5%, keeping our view of another central bank rate cut in March on track.
- **Malaysia:** The government is considering a stimulus package to soften the impact of Covid-19 on the economy. The announcement is scheduled for the next Thursday (27 February). Speaking to local media, finance minister Lim Guan Eng has urged companies to upgrade existing facilities to prepare themselves for a post-Covid-19 bounce back in business. We recently cut our 2020 growth forecast to 3.5% from 4.5% and expect an additional 50 basis points of central bank rate cuts by mid-year.
 - **Indonesia:** Indonesian President Jokowi urged his cabinet to rollout spending “as early as possible” to help cushion the economy from the fallout from the Covid-19 spread with exports and manufacturing expected to take a hit. The Finance minister indicated that the impact will be “substantial” and we expect the government to front-load spending while waiting for the passage of the so-called “omnibus bill” which should help bolster investment activity in the latter half of the year. Until then, we may expect lackluster growth numbers with both fiscal and monetary stimulus attempting to keep growth close to the government target of 5.3%.
 - **Philippines:** The Bureau of the Treasury (BTr) announced it was mulling the issuance of Dollar-denominated debt which we expect will be rolled out within the next two weeks given the depressed yield on US Treasuries. The BTr generally issues fresh Republic of the Philippines (ROP) bonds in January, which could have taken a backseat as the treasury issued a round of Peso retail bonds. The fresh supply could affect longer-dated ROPs such as ROP42 and ROP29 given that BTr will likely issue at the long end of the curve.

What to look out for: FOMC minutes

- US empire manufacturing (18 February)
- US housing starts and PPI (19 February)
- Bank Indonesia policy (20 February)
- FOMC minutes (20 February)
- Malaysia inflation (21 February)
- US existing home sales (21 February)

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Japan heads towards recession

Even before the economy was hit by Covid-19, Japan was contracting sharply. A recession now looks all but inevitable



-6.3% 4Q19 GDP
QoQ annualised

Worse than expected

4Q19 contraction was man-made

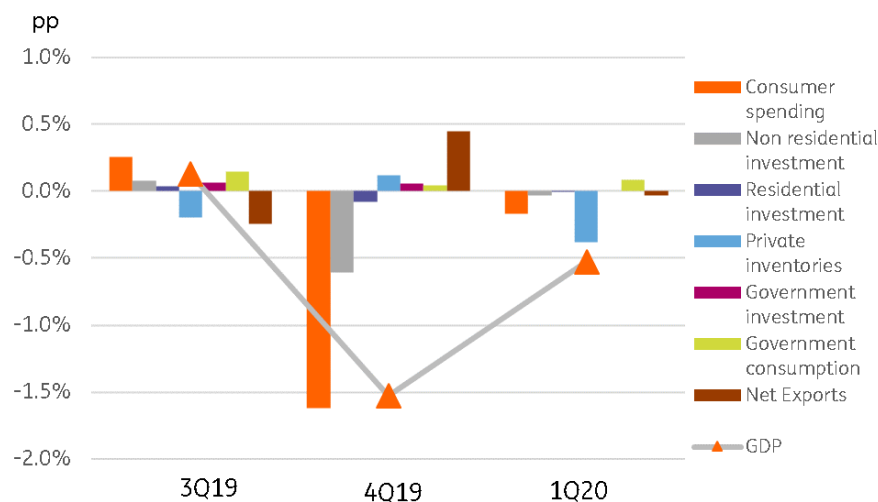
The 1.6%QoQ contraction in GDP in 4Q19 (-6.3%QoQ annualised) was a surprise only in its magnitude. The decline was not much in doubt. Following on from Japan's 2 percentage point October consumption tax hike, there was a wholly expected decline in expenditure, which was only unusual in that the pre-hike front-loading of spending was very muted. So the October consumption tax hike was all about "bust" and not about "boom", though the full-year GDP result of 0.8% is probably not all that far off potential and on a historical basis, isn't really a problem.

The outlook for 1Q20 though is still terrible

At the beginning of the year, even this awful 4Q19 GDP figures could have been written off as a bygone, with 2020 shaping up to be buoyed by a less bellicose trade environment and a possible

pick up in technology demand and production . The outlook was fair, rather than good, but that was before Covid-19 hit and now the story has changed substantially.

Contribution to GDP QoQ% 3Q and 4Q19 and 1Q20 forecast



Source: ING
Contributions to GDP

1Q20 will also contract

Looking at what caused the 4Q19 contraction, there are few encouraging signs for 1Q20. Consumer spending, which slumped following the tax hike in 4Q19, will now struggle to do anything except contract further in 1Q20 as the impact of Covid-19 weighs on consumer sentiment, weighing in particular on the consumer services sector.

Right now, there are few reasons to assume that this will not also be a factor weighing on consumer spending in 2Q20.

The net export sector was actually a positive contributor to GDP growth in 1Q19, despite weak exports, as imports fell even more sharply (2.6%QoQ), and any recovery in 1Q or 2Q20 will only work to drag down again on those GDP figures.

The other side of weak imports is often inventory reduction. But not here. Private inventory building was supportive for growth in 4Q19 to the tune of about 0.1pp. This increase was almost certainly unplanned and undesired and will need working down before inventories can begin to be rebuilt in a way that might help lift GDP. That might happen in 2Q20, but probably not in 1Q20.

In short, recession looks unavoidable

Without labouring the point too much further, other aspects of GDP, such as private investment offer no rays of hope for near term GDP either. The current fiscal stimulus programme, although substantial, basically only offsets the negative impact of last year's consumption tax hike, and without any further stimulus, will do nothing to change the overall growth picture. Some further government spending may help to curb any further contraction in GDP beyond 1Q20. But that will not stop what started off as a technical downturn, from evolving into a full-blown recession.

We now see full-year GDP growth for 2020 at -1.1%. The BoJ may try to talk up its resolve to tackle this abysmal outlook, but in our view, they were out of viable options years ago, and we don't anticipate any meaningful policy responses from them.

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Thai economy on a downward path

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Source: Shutterstock

1.6% 4Q19 GDP growth

Five-year low

Lower than expected

Downside miss in 4Q19 growth

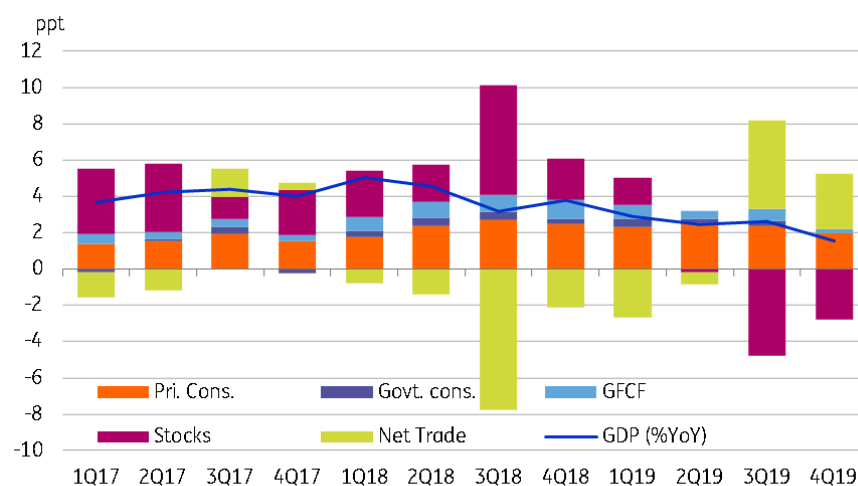
Growth in Thailand slumped to a five-year low in the fourth quarter of 2019. This was weaker than the consensus median estimate of 1.9% (we were a bit more bearish at 1.8%) and also down sharply from 2.6% growth in 3Q19.

Across-the-board weakness in spending, both domestic, as well as exports, caused the slowdown. The contributions of all main domestic demand components – private consumption, government consumption, and gross fixed capital formation shrank, while de-stocking remained a key drag on headline growth. The export decline accelerated but imports declined more than exports, leaving net trade in the driving seat of GDP growth, albeit with a smaller contribution to GDP growth.

Agriculture and manufacturing were the industry-side drags on GDP.

This brings full-year growth down to 2.4%, almost half of what it was in 2018. This makes 2019 growth numbers the lowest since the 1% growth seen in 2014.

Sources of GDP growth



Note: Bars may not stack up to GDP growth due to statistical discrepancy

Source: CEIC, ING

Downgrade of 2020 growth outlook

With perennial weak domestic spending and heavy dependence on tourism, we believe the economy is heading for a prolonged slump this year as coronavirus keeps tourists at bay. Or, probably even a recession as quarter-on-quarter (seasonally adjusted) GDP, which barely grew in the last few quarters, could well move into contraction territory over the next couple of quarters.

The last time the economy plunged into recession was during the military coup in 2014 when annual growth dipped to 1%. We could see something similar this year, or even worse if the virus continues to spread rapidly. But that's not our baseline scenario for now.

The National Economic and Social Development Council now sees GDP growth in 2020 in the 1.5% to 2.5% range, slower than its earlier forecast of 2.7% to 3.7%. We think growth at the low-end of the NESDC's revised range appears to be a more probable view for the year. We are cutting our forecast to 1.5% from 2.3%.

Will economic policy do any good?

The Bank of Thailand resumed its easing cycle with a 25 basis point rate cut earlier this month. And we are still of the view that they will cut rates again by another 25bp in March.

We believe worsening growth prospects keeps doors open for more monetary easing ahead, while inflation continues to be non-existent and the economy needs a weaker Thai baht to help the recovery. However, we are sceptical that in an environment of weak confidence, more rate cuts will do much for the economy.

Meanwhile, parliament finally passed the FY20 budget bill, clearing the way for THB 3.2

trillion of planned government spending for the year, which has already been delayed by four months now. It would be fair to expect that most of it would be front-loaded to avert a deeper economic downturn.

We think the economy will need extra fiscal support to stay afloat, but gauging from the delay in passing the regular budget, we think it is unlikely we will see such support.

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Philippines: Remittance growth jumps but the coronavirus could be a game changer

Remittances sent home by Overseas Filipino (OF) workers grew 4.1% in 2019, helping to prop up consumption and stabilise external reserves



Source: Shutterstock

Remittance growth hit 4.1%

December remittance flows grew 1.9%, bringing full year growth to 4.1% with roughly \$30.1 billion worth of flows reaching the Philippines. Remittances provide a steady stream of foreign exchange to help offset the widening trade gap and limit the current account deficit. Together with business process outsourcing receipts, OF remittance flows augment domestic wages, translating into potent purchasing power to fund household consumption, and even capital formation.

Is the coronavirus a game changer?

In the past, OF remittance flows managed to defy sceptics, posting strong growth even in times of global recession or geopolitical events which caused substantial upheaval of Filipinos in their host countries. OFs are deployed across the globe in several jurisdictions and in several diversified services professions, making them more able to sidestep economic downturns. Case in point, remittances from the Middle East, a mainstay source of OF remittances, have remained in contraction for the last year and yet overall remittance flows have remained largely positive. However, given the reach and nature of the coronavirus, this stable source of FX flows and peso purchasing power now faces a real threat. The virus has spread across the globe and will likely

affect both deployment and actual work of Filipinos based abroad. The outbreak also forces people to go into quarantine or affects consumption patterns which could have an adverse impact on the services industry, where most OFs are employed. The recent plight of cruise ships around the world will likely put pressure on cruise liners and the hospitality industry as a whole, making it difficult for Filipinos to send home remittances should their salaries be curtailed or they lose their jobs altogether.

OFs to find a way again?

Filipinos found a way to send home remittances throughout the global financial crisis and every other economic downturn experienced around the globe. While the coronavirus presents a new challenging landscape for these flows, we expect OF remittances to post modest growth from the average 3-4% growth clip per year, given the altruistic nature of the flows. A less vigorous pace of OF remittance flows at a time of projected widening in the trade deficit could translate to renewed pressure on the peso in the near term.

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Indonesia: Trade gap widens by more than expected as exports unexpectedly contract

Trade gap expected to widen further in 2020, on global trade slump from COVID-19.



Exports unexpectedly contract in January

Indonesia's trade deficit hit \$870m, much wider than expected and compared to the previous month as exports slipped unexpectedly into contraction. Exports fell 3.7%, counter to the expected modest 1.2% gain. Exports to China were in the red for a second straight month and exports to ASEAN were also negative. Imports on the other hand contracted by more than expected, with iron and steel shipments, machinery and vehicle parts down by 16.6%, 11.7% and 36.7%, respectively. The sustained import compression may be tied to a directive from the government to limit the current account deficit but, given the likely resumption of investment activity sponsored by Jokowi, we expect import compression to be a thing of the past.

BI looking to provide boost but awaiting IDR stability

Bank Indonesia (BI) had previously signaled policy easing in the near term with Governor Warjiyo indicating that he was merely gauging the proper timing for such a move. We believe that BI will cut policy rates on Thursday, with additional policy rate cuts contingent on IDR stability. With the trade gap expected to widen throughout 2020 as import growth resumes at a time of export sector

struggles, we expect IDR to come under pressure and limit the ability of the BI to cut further after Thursday.

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