

Good MornING Asia - 26 July 2019

Investors continue to digest green shoots of upcoming US-China trade talks amid persisting anxiety about the likely turn economic policies in the developed world take. The ECB failed to deliver any easing yesterday and the focus now shifts to the Fed policy for which hopes are pinned on a 25bp rate cut next week.

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By Nicholas Mapa



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-8.5%

Consensus on Singapore's June manufacturing growth

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- **General Asia:** Investors continue to digest green shoots of upcoming US-China trade talks amid persisting anxiety about the likely turn economic policies in the developed world take. The ECB failed to deliver any easing yesterday and the focus now shifts to the Fed policy for which hopes are pinned on a 25bp rate cut next week.
- **Malaysia:** East Coast Rail Link (ECRL) project is back on track in a significant sentiment booster for foreign investors in Malaysia. After suspension for a year, China and Malaysia have reportedly resumed construction for the 640 km rail line forming a part of China's Belt-and-Road initiative. Meanwhile, Malaysia managed to get the project cost cut by a third to

about \$44 billion and aims for completion by end-2026. Hopefully, this spins the wheels for another key rail project, the Kuala Lumpur-Singapore High-Speed Rail (HSR), that's been on hold currently.

- **Singapore:** June industrial production figures today will inform about the likely direction of revision to the 0.1% YoY (-3.4% QoQ SAAR) advance 2Q GDP growth estimate. Underlying the consensus of -8.5% YoY IP growth is worst NODX performance with over 17% fall. While electronics continued to be the weak link in both NODX and IP, we don't rule out highly volatile pharmaceutical production producing surprises. But anything bad than consensus would intensify calls for MAS easing before the October policy review.
- **Thailand:** Moody's affirmed Thailand's Baa1 sovereign rating but upgraded outlook of the same Positive from Stable. It cited strong public and external finances providing for a significant room to counter shocks, and a large and diverse economy allowing shock absorption capacity. It identified lingering political risks and long-term structural challenges of aging society and labor skills shortages as key constraints on potential growth (and rating). Judging from the last rating changed in 2000 and 2003, Moody's acted within months after putting the rating on an upgrade watch. The circumstances are different now as the economy remains plagued by sustained anaemic growth for the last several years, which keeps us from anticipating a quick upgrade this time.
- **Indonesia:** Bank Indonesia (BI) Governor Warjiyo maintains his dovish rhetoric, indicating that subdued inflation and the need to boost growth underscore the need further reduction in policy rates. Meanwhile, his newly appointed Deputy Governor Destry Damayanti expressed her opinion that the global monetary easing cycle may be drawn out, affording BI room to ease further. Damayanti shared that further BI easing could trigger an influx of foreign funds into Indonesia, thus offsetting the current account deficit and supporting the IDR in the process.
- **Philippines:** The BSP's Monetary Board member Bruce Tolentino downplayed the need to ease policy in the near term, indicating he did not see the need to "rush" into cutting rates. Preaching data-dependence, Tolentino wants to see more data and the effects of recent easing before considering future policy adjustments. This dampens the chances to some extent for a BSP rate cut in August with investors looking to economic data reports in coming weeks.

What to look out for: US GDP

- Japan inflation (26 July)
- US GDP (26 July)

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Asia week ahead: Some shoots on second-half outlook

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Source: Shutterstock

➔ PMI data dominates

Around this time of the month, markets typically focus on purchasing managers index for the manufacturing and service sectors. Within these, China's PMI always steals the limelight but has been doing even more so since the onset of the trade war. However, we don't think the upcoming Chinese PMI data will be telling us anything different from recent releases.

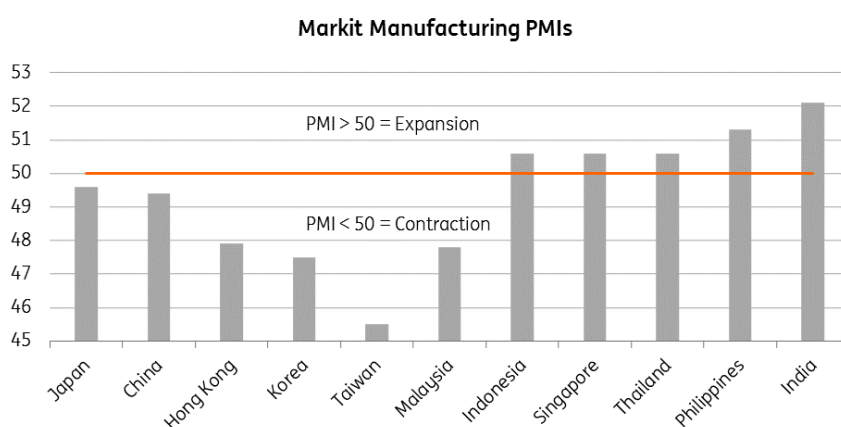
While the trade war continues to hurt exports and manufacturing, services activity is holding up well. Even if this gulf widens further, it will be increasingly difficult for the services sectors to remain

afloat without eventually being dragged lower without support from exports and manufacturing.

On the other spectrum is India, where manufacturing activity is firmly on the growth trajectory reflected by the recent PMI well above the 50 threshold, however, service activity has been in the contracting territory with the PMI in June coming in at 49.6. This isn't a good mix for the economy with services accounting for over 50% of GDP.

And there is this north-south divide as well – manufacturing PMIs for the majority of the south still in the expansionary zone, while in the north it seems to be contracting. But not all is bad in sub-50 countries. Malaysia stands out here. Despite weak PMI, Malaysia's manufacturing sector is holding up relatively well on the back of the electronics-led export outperformance as is expected to be reinforced by June trade figures out next week.

Asian manufacturing PMI - Not everything gray is bad



Source: Bloomberg, ING

➔ But hard data matters more

Having said all of the above, PMIs are still sentiment-driven soft economic indicators. Hard activity data matters more. Korea's trade figures for July will be setting up expectations for trade and manufacturing performance for the rest of the region.

Despite the deep export slump, [Korea dodged recession](#) with a pick-up in second-quarter GDP growth. Yet, we don't see July trade figures calming nerves, especially with trade tensions with Japan clouding the prospects further. We expect a continued double-digit export decline in July, while weak domestic demand depresses imports and sustains wide trade surplus.

Hong Kong and Taiwan are next in line to report GDP data for 2Q19. Like Korea, the electronics slump has been hurting Taiwan quite a bit. Even if [Taiwan's exports posted positive growth in June](#), our Chinese economist warns against celebrating just yet. Indeed, she was right because subsequent export orders data for the month was still bad. As such, the consensus of 1.8% growth in Taiwan's GDP is at risk of a downside surprise (ING forecast 1.4%).

Undoubtedly, Hong Kong's economy has been hit hard by anti-government protests since late March, which could dent growth further below the 0.6% rate in 1Q19, which in itself was the slowest in a decade since the 2009 global financial crisis.

[South Korean economy dodges recession](#)

[Taiwan: Export growth positive but too soon to celebrate](#)

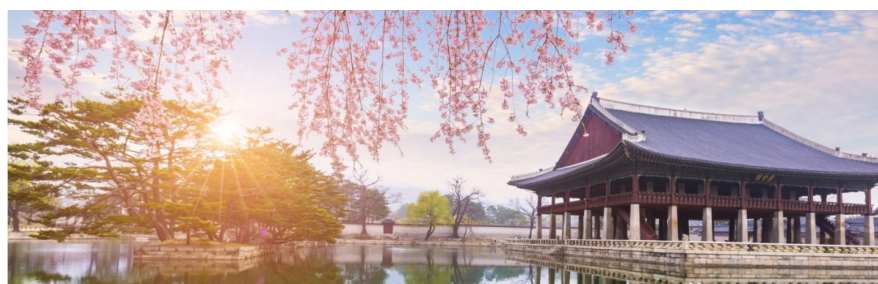
Asia Economic Calendar

Country	Time	Data/event	ING	Survey	Prev.
Saturday 27 July					
China	0230	Jun Industrial profits (YTD, YoY%)	-1.9	-	1.1
Monday 29 July					
South Korea	2200	Aug BOK Business Survey Index, mfg	73.8	-	75.0
	2200	Aug BOK Business Survey Index, non-mfg	73.0	-	74.0
Tuesday 30 July					
Thailand	-	Jun Manufacturing index (YoY%)	-3.5	-	-4.0
Wednesday 31 July					
China	0200	Jul Manufacturing PMI	49.5	49.7	49.4
	0200	Jul Non-manufacturing PMI	53.7	54	54.2
India	-	Jun Fiscal deficit (INR crore)	-	-	209109
Taiwan	0900	2Q P GDP (YoY%)	1.4	-	1.7
South Korea	0000	Jun Industrial production (MoM/YoY%)	1.0/-1.4	-/-	-1.7/-0.2
Hong Kong	0915	2Q GDP (% YoY)	1.4		0.6
Thailand	0830	Jun Current account balance (US\$bn)	4.9		-0.4
Thursday 1 August					
China	0245	Jul Caixin Manufacturing PMI	49.5	49.8	49.4
India	0600	Jul Nikkei Manufacturing PMI	50.9	-	52.1
Indonesia	-	Jul CPI (YoY%)	3.3	-	3.3
	-	Jul Core CPI (YoY%)	-	-	3.3
Taiwan	0130	Jul Nikkei Manufacturing PMI	45	-	45.5
Thailand	0500	Jul CPI (YoY%)	0.8	-	0.9
	0500	Jul Core CPI (YoY%)	0.5	-	0.5
South Korea	0000	Jul CPI (YoY%)	0.8	-/-	0.7
	0100	Jul Exports (YoY%)	-12.0	-	-13.5
	0100	Jul Imports (YoY%)	-8.0	-	-11.1
	0100	Jul Trade balance (US\$m)	4249	-	3995
	0130	Jul Nikkei Manufacturing PMI	-	-	47.5
Hong Kong	0930	Jun Retail sales value (%YoY)	-1.6		-1.3
	0930	Jun Retail sales volume (%YoY)	-2.0		-1.7
Malaysia	0130	Jul Markit manufacturing PMI	48.5		47.8
Thailand	0130	Jul Markit manufacturing PMI	50.1		50.6
Friday 2 August					
Malaysia	0500	Jun Exports (YoY%)	0.0	-	2.5
	0500	Jun Imports (YoY%)	-3.0	-	1.4
	0500	Jun Trade balance (RM bn)	8.2	-	9.1
Singapore	1400	Jul Purchasing Managers Index	49.5	-	49.6

Source: ING, Bloomberg, *GMT

South Korean economy dodges recession

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2.1% 2Q19 GDP growth

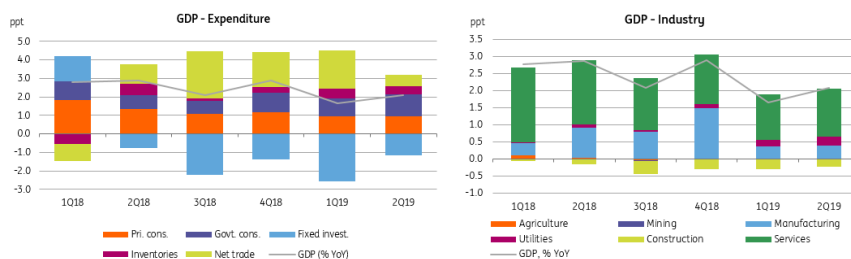
Better than expected

Growth picks up in 2Q19

South Korea's second quarter GDP grew by 2.1% from a year ago and by 1.1% (seasonally adjusted) from the preceding quarter. Growth was not only firmer than the Bloomberg consensus estimates of 1.9% year-on-year and 0.9% quarter-on-quarter, but also marked an acceleration from the 1.7% YoY and -0.4% QoQ SA rates recorded in 1Q19. More importantly, the economy avoided a recession with QoQ growth back in positive territory.

Private and public consumption persisted as the key expenditure-side drivers of GDP growth. The contribution of private consumption to GDP growth rose to 1.0 percentage point (ppt) from 0.9ppt in 1Q and that of government consumption was up to 1.2ppt from 1.0ppt. Investments remained a drag albeit smaller than in 1Q (-1.2ppt vs. -2.6ppt in 1Q). And all this more than offset a significant narrowing in the net trade contribution. On the industry-side, services retained their spot as the main driver of GDP growth, while an improvement in manufacturing and utilities also helped.

What's behind firmer GDP growth in the last quarter?



Source: Bloomberg, CEIC, ING

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

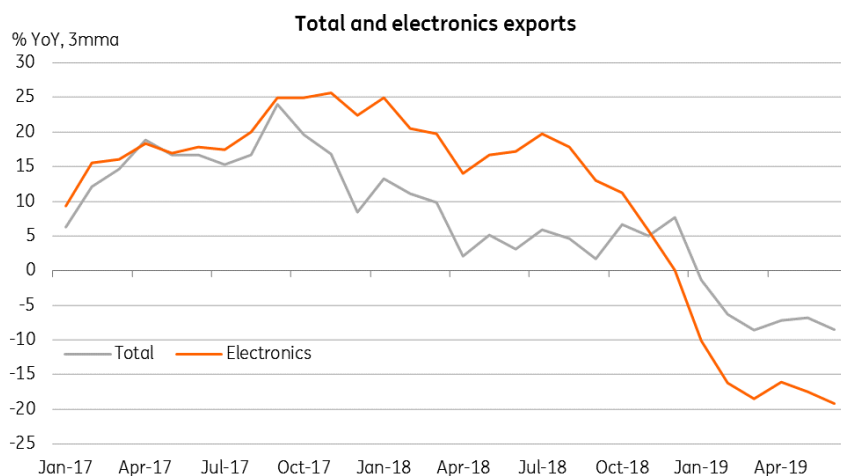
Economy dodges a recession

While YoY growth of 2.1% matched our forecast exactly, we overestimated the QoQ weakness in forecasting no growth for the period. With a 0.4% QoQ 1Q19 contraction and further weakness displayed by activity data in 2Q19, we feared the economy could have fallen into a technical recession. Even the tiniest negative reading (rounding up to our forecast of zero growth) would have resulted in a technical recession defined as two straight quarters of negative QoQ growth.

This would not have been too surprising given that the economy is heavily reliant on exports, which have been beaten up by the US-China trade and tech wars as well as a global tech slump. Electronics exports, a bellwether for the economy which account for a third of total exports, have suffered from a contraction of as much as 20% YoY in recent months, and within that, semiconductors have fared even worse, with a more than 30% fall.

Could it be that the wonky seasonal adjustment for QoQ growth helped the economy to avert a recession?

Electronics dampening export performance



Source: Bloomberg, CEIC, ING

Outlook isn't promising though

Even if the economy has averted a recession for now, the outlook for the rest of the year remains clouded by a worsening external environment, including an ongoing trade spat with Japan.

Just a week ago, the Bank of Korea (BoK) scaled back its growth forecast for 2019 to 2.2% from 2.5%. Average 1.9% GDP growth in the first half of the year precisely matched the BoK's revised forecast for the period. But its 2.4% growth view for the second half of the year appears optimistic. Aside from some favourable base effects (growth slowed sharply in 3Q18), there's no reason for year-on-year growth to recover in the second half. That, too, assumes that things don't become any worse than they currently are, which is a risky proposition absent any let-up in the export slump.

More easier policy is the order of the day

Better late than never, the BoK's 25 basis point policy interest rate cut no more than a week ago was a step in the right direction. However, [as we argued at the time](#), this was a mere reversal of the tightening late last year, not a stimulus in any real sense.

The key questions that today's data pose are whether the BoK will be complacent after an acceleration in GDP growth and stay on hold for the rest of the year, or, will it see through the GDP figure that's masking underlying weakness in the trade and electronics sectors, and ease policy further with more rate cuts?

Judging from the shift in global central bank policies, increased policy support for growth is the order of the day. We expect the BoK to go with the flow and ease again by 25bp in the final quarter of the year as its 2.2% full year GDP forecast looks increasingly unattainable. ING's forecast for Korea's full-year 2019 GDP growth is 1.4% (consensus 2.0%).

[Korea: Central bank starts easing cycle with 25bp rate cut](#)

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