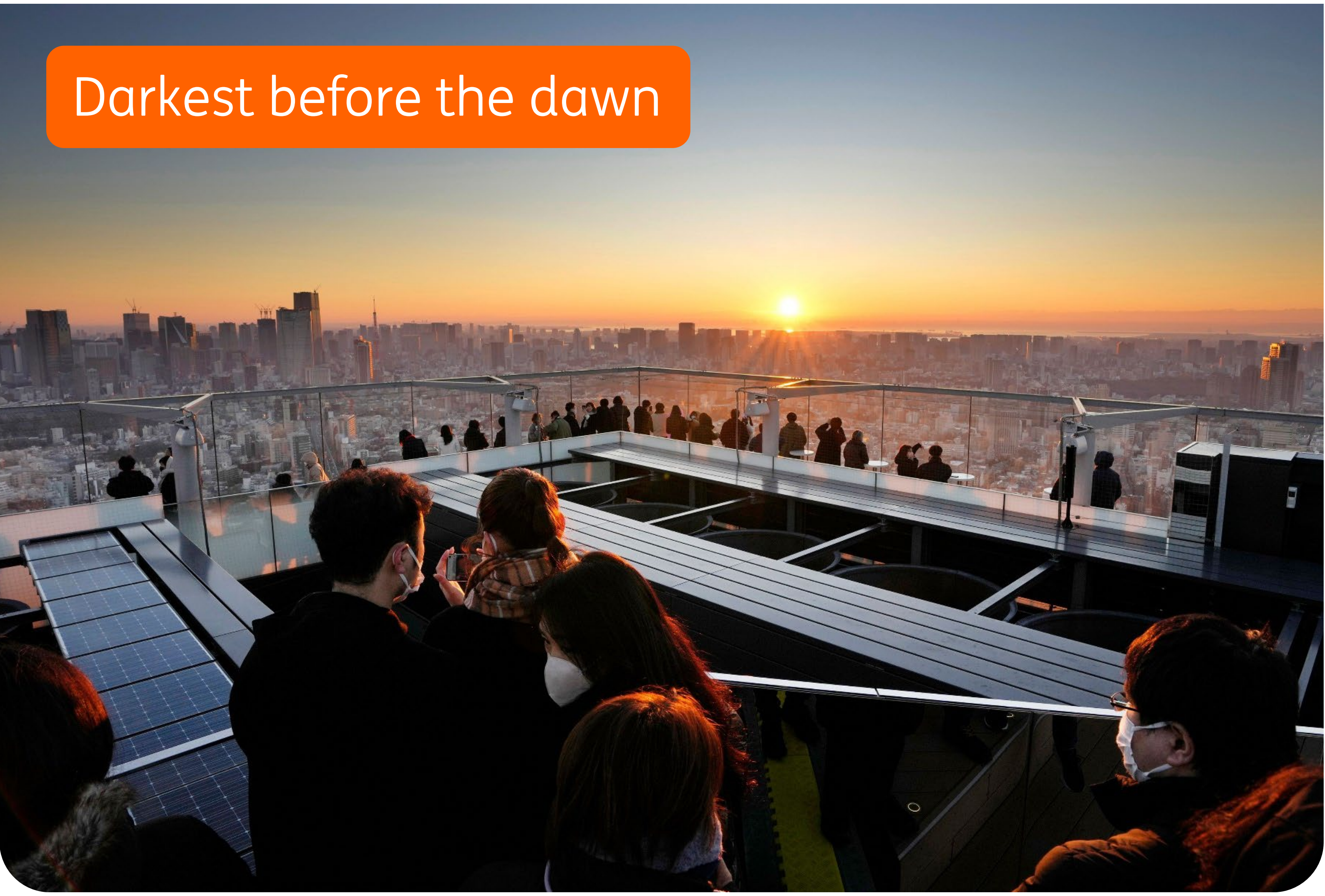
The year ahead for Asian economies

January 2023



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Asia 2023: Darkest before the dawn

2023 is not going to be a great year for growth – the region's main external trade partners are all already in, or going into recession, and the region's largest economy, China, is struggling right now. But China's Covid-19 waves will pass, inflation is already coming down in many economies, and rate policy, currency and other market strains should ease

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What does the Year of the Rabbit hold?

As we move out of the Year of the Tiger towards the Year of the (Water) Rabbit, it's a good time to look ahead and consider what the New Year will hold for the macro economy and markets of the Asia Pacific region. Given the limitations of the economist professions' own forecasting abilities, it seems churlish to ignore the horoscope's message, which for this sign of the Chinese Zodiac, appears to be one of longevity, peace and prosperity.

Is there any hope for this? It seems an overly optimistic leap of faith. Still, if there were a breakout of peace in Ukraine, this would undoubtedly be welcomed in Asia (as well as the rest of the world), taking pressure off commodity energy and agricultural import prices. Arguably, the idea of longevity may also be tied in with some improvement in China's Covid situation, although this is currently extremely tricky. One can imagine markets rallying hard and delivering prosperity if either of these events transpires.

Macro outlook starts badly, but should improve

But despite the zodiac's suggestions for a brighter future, the facts on the ground remain that 2023 is shaping up to be a poor one for Asia's macroeconomy. Major external markets are either already in recession (Europe) and going deeper, or slowing and probably headed for recession (US). Regional demand is also being rocked by China's Covid transition, from "zero-Covid" to "living with Covid". Official data on this cannot be taken remotely seriously, but it doesn't sound like it is going well at the moment, and it may be some months before the situation calms. When it does, though, it could deliver a more optimistic trade environment than exists currently. Double-digit declines in export growth across the region, which reflect external (and China's) weakness, may get slightly worse first, but it should begin stabilising later in 2023.

The downturn in the semiconductor cycle, which is important for much of the region, may also benefit from improving local and regional demand as China re-emerges. But as new chip fabrication plants come online in 2023 and 2024, we may see these depressing unit prices and profits. And the trend of restrictions on US trade with China in technology is unlikely to reverse or be circumvented any time soon, though high-level talks between the US and China in the New Year may lessen tensions.

Markets may do better than macro

Even with some pickup later on in 2023, our expectations for 2023 economic activity are cautious. But there is room for some market confidence. Not only will the global rate cycle likely hit its peak in early 2023, but it is also entirely conceivable that we see some decline in global rates before the end of 2023, taking pressure off local Asian policy rates, bond yields and currencies. All of which should also be a catalyst for some pick up in equity prices, helped also by declining inflation rates, which have peaked in most of the region (there are a few exceptions).

In summary, we are perhaps a bit less optimistic than our zodiacal competitors in the forecasting world, but we can at least see some light at the end of the tunnel. 2024 should be better…

China: Timing of recovery is a big question mark

China has drastically eased its Covid-19 measures. Both domestic mobility and international traffic should increase in 2023. But the question is in which quarter? The current Covid wave could last at least a few months. By then, the US and EU will likely be in recession, hurting China's exports. We also worry about the fiscal deficit getting bigger

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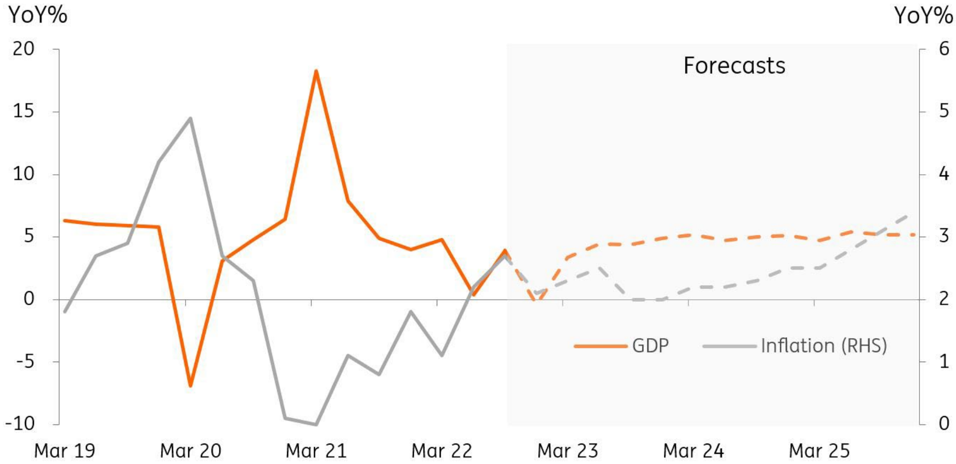
China is set to lift its quarantine requirement for inbound travellers

China: At a glance

The Chinese economy has slowed since the second quarter of 2022, mainly due to strict Covid measures that disrupted port and land logistics, retail sales and catering, and caused temporary shutdowns of factories in some key manufacturing locations. Even when restrictions were eased, a mixture of a weak domestic economy and high external inflation hit manufacturing in the fourth quarter of 2022. In addition, real estate developers have struggled to get enough cash to complete residential projects. This triggered a slew of easing measures for real estate developers to get financing via banks, stock and debt markets in the fourth quarter. The fragile economy means there has been no inflation pressure at all, and luckily no deflation. The People's Bank of China (PBoC) has used re-lending programmes to inject liquidity into specific areas, such as small and medium-sized enterprises and real estate. Conventional interest rates and required reserve ratios were not used frequently as those tools were not effective when there were Covid restrictions. The strong dollar combined with the weak Chinese economy resulted in a weak Chinese yuan (CNY) in 2022.

GDP and inflation outlooks



Source: CEIC, ING estimates

3 calls for 2023

1 **It is really about timing when it comes to the question of economic recovery**

Most Covid-19 measures were removed in December 2022. The removal of mandatory quarantine when entering Mainland China suggests that business travel will resume soon, even with the current spike in Covid cases as people in most locations outside China have become used to living with the virus. Residents could start to visit Hong Kong to get medicines and healthcare services, and then later in the year they could begin to travel to foreign countries for leisure activities. We believe that leisure travel into Mainland China could resume from the Easter holidays. Retail sales should recover, and the current Covid wave should ease after a few months (although it's difficult to gauge the timing), which should minimise the risk of supply chain disruptions.

2 **External demand to be weaker in 2023**

The US and Europe have been China's second and third top export destinations respectively. According to our house forecasts, the timing of recession in the US and Europe should be around the first half of 2023, and therefore should not overlap with the peak export season of the fourth quarter. But whether export demand can recover after the recession is still in question. China's trade with ASEAN – the number one export destination for China – and the rest of Asia also depend on the consumer market in the US and Europe. Both exports and imports could enter yearly contraction in the first half of 2023. Trade could recover towards the second half when domestic and external economies recover.

3 **Fiscal deficit could become an issue, and unconventional monetary policy could become a norm**

The fiscal deficit has not previously been an issue for China. But Covid and the real estate crisis have changed this. The fiscal deficit-to-GDP will be around 8% by the end of 2022, which is higher than the historical high (data goes back to December 1995) of 6.2% in the fourth quarter of 2020. The fiscal deficit-to-GDP should remain at 8% in 2023 even if there is much less spending on Covid tests and quarantines. Fiscal spending on high-tech development will increase. As for monetary policy, the PBoC may choose to stay on hold next year as the central bank has hesitated to lower the 7D interest rate any further to avoid falling into a liquidity trap. We do not expect the PBoC to cut the required reserve ratio or interest rates in 2023. That said, the re-lending programme for specific targets should continue at least into the first half of 2023. Further liquidity injections via the re-lending programme in the second half will depend on the speed of recovery of real estate developers and external markets. We expect the CNY to strengthen against the dollar as the economy picks up and the US enters a recession.

China summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	-0.4	3.4	4.4	4.4	4.9	2.1	4.3	5.0	5.1
Inflation (YoY%)	2.1	2.3	2.5	2.0	2.0	2.0	2.2	2.3	3.0
New home price (YoY%)	-2.3	-0.5	2.2	3.5	4.7	-1.3	2.5	7.5	6.8
Surveyed jobless (%)	5.7	5.4	5.0	4.9	4.8	5.6	5.1	4.8	4.7
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
7D reverse repo (%)	2.0	1.9	1.8	1.8	1.8	1.8	1.8	2.0	2.4
10Y bond yields (%)	2.95	2.95	3.10	3.20	3.35	3.45	3.55	3.8	4.3
USD/CNY	6.98	6.9	6.77	6.75	6.72	6.75	6.80	7.00	7.00

Source: CEIC, ING estimates

Taiwan's economy under pressure as trade woes continue

Weak global semiconductor demand, limited benefits from China's re-opening, and further rate hikes mean it'll be a tough year ahead for Taiwan

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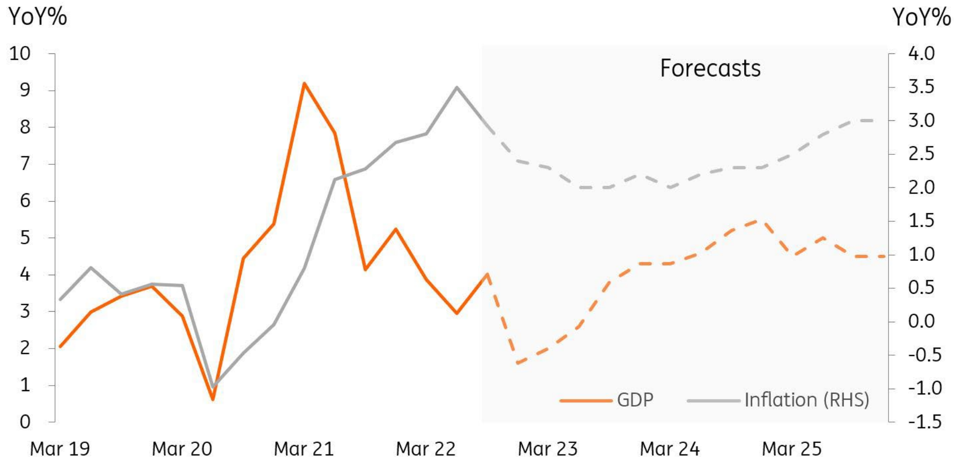
Taiwan accounts for around two-thirds of semiconductor production

Taiwan: At a glance

Taiwan's economy has been showing signs of weakness since September 2022, when global semiconductor demand slumped. That was mostly due to high inflation and therefore weaker demand for electronic goods in the US and Europe. Demand from China, which is also a big consumer market, also suffered due to Covid-19 measures. Average growth in the first three quarters averaged above 3% year-on-year. This is low compared to 7% for the same period in the previous year. Inflation picked up but didn't exceed 3.6% in 2022. The central bank still raised the discount rate to 1.75% from 1.125%. The Taiwan dollar weakened against the US dollar by around 10% in 2022.

GDP and inflation outlooks



Source: CEIC, ING estimates

3 calls for 2023

1 **Weak semiconductor demand leading to slower growth**

Taiwan's economy will continue to come under pressure from shrinking sales of semiconductors as external demand wanes. Semiconductors contribute around 40% of Taiwan's exports. As high inflation continues to lower purchasing power in the US and Europe, and with Mainland China's economy yet to recover fully, the challenging time for semiconductors and therefore trade for Taiwan could continue until at least the first half of 2023. If external demand improves in the second half of the year, Taiwan's economic growth should accelerate.

2 **Mainland China's reopening of borders may not benefit Taiwan**

Mainland China's elimination of most Covid restrictions and the reopening of borders may not benefit Taiwan, at least in the first half of 2023. Taiwan has banned Mainland Chinese tourists since the Covid outbreak, and only allows Chinese citizens to visit for business or family reasons. This means retail sales in Taiwan may not recover to pre-Covid levels in 2023.

3 **Monetary policy will weigh on the economy**

Taiwan's central bank may continue to shadow the US Fed's rate hike path, at least in the first quarter of 2023. That means the monetary policy will exacerbate the weak growth of the economy. This is a risky policy, which could bring further financial pressure to companies and households that will face higher interest costs. On the fiscal side, the government may need to extend preferential policies to small and medium-sized enterprises and it is likely to spend more on military expenses. The New Taiwan dollar (TWD) could be volatile when the central bank changes its interest rate path from hikes to cuts. Taking more time to move from hikes to easing than the Fed in the US could help support the TWD against the US dollar from the second quarter to the fourth quarter of 2023.

Taiwan summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	1.6	2.0	2.6	3.8	4.3	3.1	3.2	4.9	4.6
Inflation (YoY%)	2.4	2.3	2.0	2.0	2.2	2.9	2.1	2.2	2.8
Unemployment rate (%)	3.7	4.0	4.2	4.4	4.1	3.7	4.2	3.8	3.5
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
Discount rate (%)	1.750	1.875	1.875	1.750	1.625	1.500	1.375	1.375	1.500
10Y bond yields (%)	1.35	1.35	1.35	1.23	1.10	0.98	0.98	1.11	1.23
USD/TWD	30.6	30.2	29.6	29.5	29.4	31.5	30.0	32.0	32.0

Source: CEIC, ING estimates

Japan: A modest recovery will continue to be supported by accommodative macro policies

We expect Japan's GDP growth to slow in 2023 but to remain above its potential rate, supported by an accommodative macro policy environment. The near-term outlook is bleak due to high inflation and weak global demand conditions

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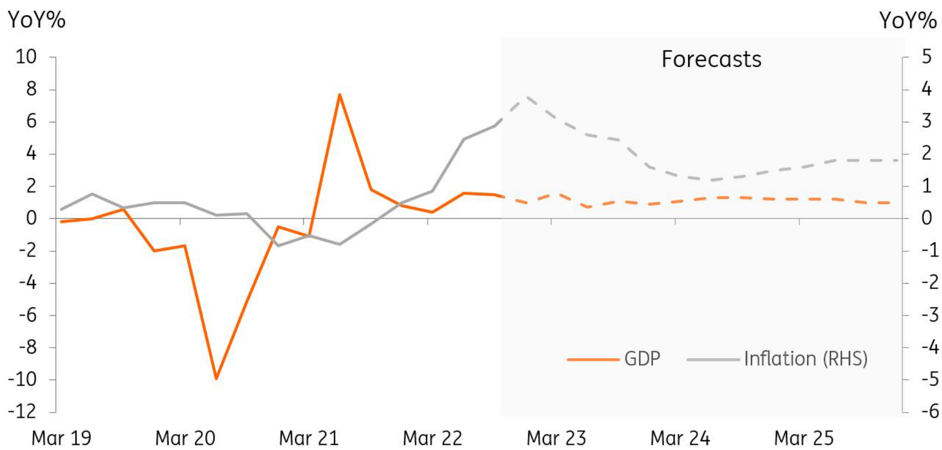
Inflation hasn't peaked yet in Japan and is likely to hit 4.0% in early 2023

Japan: At a glance

After a slight contraction (-0.2% quarter-on-quarter seasonally adjusted) in the third quarter of 2022, we expect GDP to rebound (0.6%) in the fourth quarter. A stronger yen and more relaxed border controls are likely to improve trade conditions, plus the fiscal stimulus programme will support a fourth-quarter recovery. However, the rebound should be limited as cost-push inflation puts pressure on corporate margins and household spending. We expect GDP to grow by 1.0% year-on-year in 2023, slightly lower than the 1.2% growth we expect for 2022. Weakening demand from the US, EU, and China will hurt exports and manufacturing, while limited wage growth will slow private consumption in the first quarter. Inflation hasn't peaked yet in Japan and is likely to hit 4.0% in early 2023, but it will soon decelerate back to the 2% range in the second quarter. Fiscal policy will continue to support the recovery while monetary policy will reduce the extent of accommodation, but at a slower pace than the market currently expects.

GDP and inflation outlooks



Source: CEIC, ING estimates

3 calls for 2023

1 Normalisation of Bank of Japan policy – a long and tough road ahead

The Bank of Japan's (BoJ's) unexpected decision to broaden its yield curve control band in December has paved the way for policy normalisation. But the path forward will face many challenges. A cloudy growth outlook early in the year could prevent the new central bank governor from taking immediate action, while cost-push inflation is likely to begin to subside in the second quarter. In our view, wage growth will rise more slowly than the 3% sought by the BoJ. Considering these factors, we believe the new governor will first adjust the BoJ's forward guidance in the second quarter and then call for a policy review in the third quarter. We also believe that revisiting inflation targets could be a consideration. Eventually, we expect the BoJ to lift the mid-point target for the 10Y Japanese government bond (JGB) from 0% to 0.25% in early 2024. If GDP recovers to pre-pandemic levels sooner than we expect, the timing could be moved up to the end of 2023. We also expect the BoJ to raise its short-term policy interest rate from -0.1% to 0.0% in the second quarter of 2024. That supports our view that the JGB yield curve will flatten by about 15 basis points and thus the 10Y JGB yield will come down to the 0.25-0.30% range by the year-end.

2 Wage growth is key to watch

We expect the job market to tighten in the short term as hospitality and tourism-related employment continues to rise, benefiting from the government's travel subsidy programme and the return of inbound travel. However, manufacturing jobs will likely decrease, mainly due to sluggish exports. Although the government offered incentives for wage increases this year, we anticipate that actual wage growth will be less than 3%. Base salaries may pick up, reflecting high inflation, but most of it is expected to be offset by a reduction in bonuses and other incentives as corporate earnings are likely to be squeezed. It is also questionable whether wage growth of 3% can be sustained in the upcoming years.

3 Fiscal policy is supporting growth

The second FY22 supplementary budget of 29 trillion yen (5.5% of GDP) will boost near-term growth, providing energy subsidies, maternity and childcare-related support, and vocational training support. In addition, the Cabinet approved a draft budget of 114.4 trillion yen for FY23, which is a 6.3% year-on-year rise from FY22's original budget. However, most of the positive impact of fiscal policy will be concentrated at the end of 2022 and early 2023. The budget rise in FY23 is mainly due to a large increase in defence spending (26.3% YoY), thus its policy impact on the real economy should be limited. In addition, if the government raises taxes and cuts other programmes to finance defence spending, it could hurt private consumption and result in a sudden drop in approval ratings.

Japan summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	1.0	1.6	0.6	1.1	0.9	1.2	1.0	1.2	1.2
Inflation (YoY%)	5.2	4.5	3.2	2.5	2.5	5.1	3.1	1.8	2.1
Unemployment rate (%)	2.5	2.2	2.3	2.4	2.6	2.6	2.3	2.4	2.4
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
Policy rate (%)	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	0.0	0.0	0.10
10Y bond yields (%)	0.45	0.40	0.35	0.30	0.35	0.50	0.50	0.50	0.75
USD/JPY	134	128	127	125	125	123	122	120	120

Source: CEIC, ING estimates

South Korea: A recession in the first half of 2023, followed by a mild recovery

Despite an anaemic start to 2023, we expect conditions to improve in the second half of the year as global demand begins to pick up while the deleveraging cycle comes to an end

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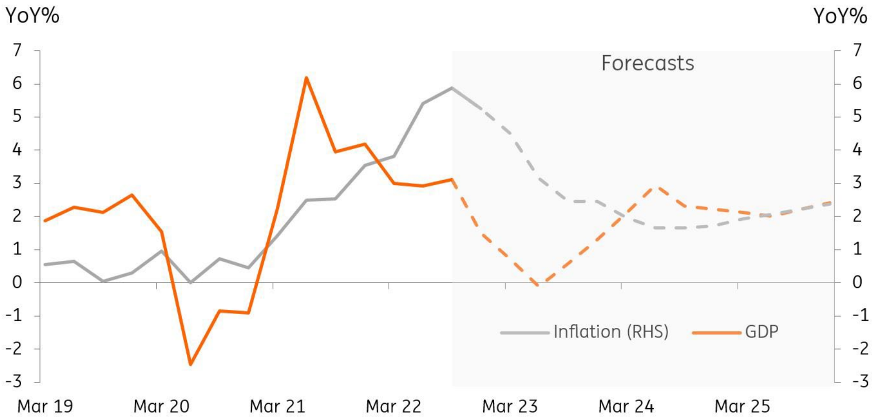
Korea's housing market is cooling as mortgage rates rise

South Korea: At a glance

South Korea's economy has deteriorated considerably since the start of the fourth quarter of 2022, with exports, manufacturing and service activity tumbling sharply. Consequently, we believe that fourth-quarter GDP will contract. With such an anaemic start to 2023, we expect the annual growth rate for Korea to decelerate to only 0.6% year-on-year in 2023 from 2.6% in 2022. Both external and domestic demand is likely to weaken further, especially in the first half of 2023, and painful deleveraging is expected to hurt short-term growth given high levels of private sector debt. Inflation has clearly peaked and inflation expectations have fallen to around 3% and are expected to decelerate further. The accumulated pressure to raise utility and public service fees will add upward inflationary pressures, but most of these are expected to be offset by falling housing prices, global oil prices, and a stronger Korean won. Due to asset price adjustment and the higher debt service burden, the Bank of Korea (BoK) is likely to respond with a rate cut in the second half of 2023.

GDP and inflation outlooks



Source: CEIC, ING estimates

3 calls for 2023

1 Deleveraging will be painful

House prices have already declined significantly in 2022, but we expect prices to fall by another 10% in 2023 and remain stagnant throughout the year. Given the sharp rise in unsold units in major cities, it may take a while for the recovery to take hold in the residential housing market. The government will continue to soften real estate measures and lending conditions, but higher interest rates will not enable home buyers to return to the housing market quickly. Historically it usually takes two to three years to complete a downcycle. Deleveraging for corporates is also likely, and construction and real estate developers will suffer the most. The financial crunch in the corporate debt market has now subsided due to the government's response, but it is expected to come back to the surface as corporate bond issuance increases at the beginning of the year and high interest rates continue.

2 Exports to lead a recovery in the second half of the year

Despite the poor export performance in the fourth quarter of 2022, annual exports grew 6.1% year-on-year in 2022. However, in 2023 we expect exports to decline by about -7.0%, given the weakness of global demand and unfavourable price effects. We believe the downcycle for semiconductors will continue until the third quarter of 2023 and China's reopening could add a negative impact on Korea's exports in the first half of 2023, with a surge of Covid-19 patients, the risk of new variants, and supply chain disruptions. However, we expect exports to rebound quite meaningfully in the latter part of the year with the US and EU's economy bottoming out and China's situation normalising, which should lead the overall GDP growth in the second half of 2023.

3 The Bank of Korea to turn dovish as inflation subsides

We expect the terminal interest rate to peak at 3.50% and the Bank of Korea to enter an easing cycle in the third quarter of 2023. Given that the current policy rate is at 3.25%, our call for an additional 25bp hike in February will be the final destination for the current tightening cycle. Despite a reduction in gasoline tax subsidies and higher public service charges, base effects will anchor headline CPI to around 4% in the first quarter of 2023. We expect the Bank of Korea to maintain its hawkish stance throughout the first half of 2023 as inflation is still likely to far exceed its 2% target, and uncertainties over utility bill hikes and the resulting secondary effects from these are still high. But, as the real economic activity contracts and deleveraging continues, the BoK's policy priority is expected to shift toward supporting growth.

South Korea summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	1.5	0.7	-0.1	0.6	1.3	2.6	0.6	2.4	2.2
Inflation (YoY%)	5.2	4.5	3.2	2.5	2.5	5.1	3.1	1.8	2.1
Unemployment rate (%)	2.9	3.2	3.5	3.5	3.8	2.8	3.5	3.6	3.3
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
7-day repo rate (%)	3.25	3.50	3.50	3.25	3.00	2.75	2.50	2.50	2.75
10Y bond yields (%)	3.75	4.00	3.75	3.50	3.50	3.25	3.00	3.00	3.25
USD/KRW	1260	1300	1270	1250	1225	1225	1200	1200	1250

Source: CEIC, ING estimates

Indonesia to miss boost from commodity boom as Jokowi's term winds down

Indonesia benefited from the commodity boom in 2022 but may not be able to bank on this next year

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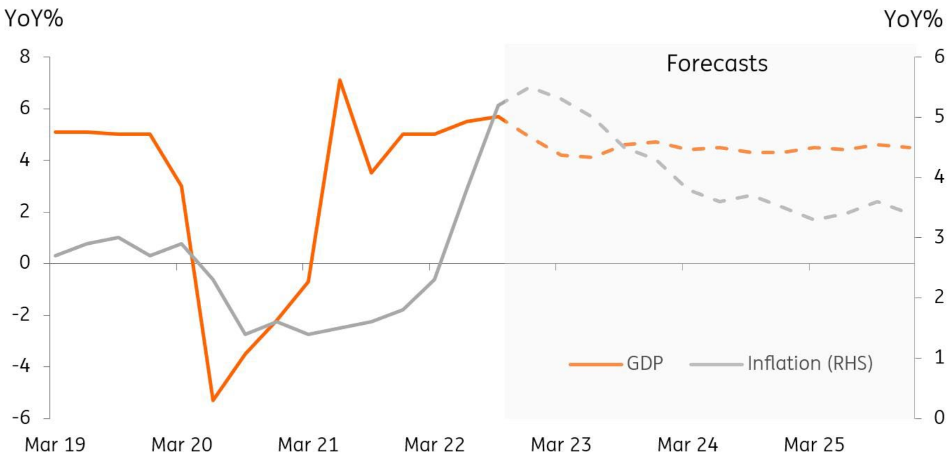
Indonesia: At a glance

Growth in 2022 will likely average 5.3% year-on-year but momentum is slowing as the commodity boom fades and inflation accelerates. Forecasts by Bank Indonesia (BI) indicate GDP growth should settle between 4.7-5.5% YoY next year.

Household spending was one solid factor behind the growth engine due in part to relatively well-behaved domestic inflation in the first half of the year. Relatively less pronounced price pressures allowed BI the space to delay rate adjustments until the second half of 2022, which also supported growth. By the second half of the year, price pressures finally caught up with Indonesia as headline inflation breached the central bank's upper bound target of 4%.

Indonesia's trade sector has also seen momentum fade as commodity prices have normalised after surging due to the war in Ukraine. This development will also be worth watching in the coming months.

GDP and inflation outlooks



Source: Badan Pusat Statistik and ING estimates

3 Calls for 2023

1 Slowing trade momentum to keep FX pressured

Indonesia was one of the few countries that benefited from the commodity price boom in 2022, translating to record trade surpluses. This resulted in the current account also reverting to positive territory, which in turn provided robust support to the Indonesian rupiah (IDR). The relative stability of the IDR helped limit price pressures early in 2022 which in turn allowed the central bank to postpone rate hikes to the latter half of 2022. With commodity prices moderating and expected to slide further, we could see Indonesia's trade surplus diminish or even move into deficit territory in 2023. The loss of this previous support suggests that the IDR will likely remain pressured for much of next year, especially if financial outflows continue. A weaker IDR in 2023 could also translate to additional rate hikes by the central bank early next year.

2 Tinkering with central bank charter a positive or a negative?

The Covid-19 pandemic's impact on fiscal balances led to some central banks resorting to quasi-budget financing in addition to quantitative easing. Bank Indonesia (BI) was one of the more active central banks in terms of providing support to fiscal counterparts with BI purchasing government bonds in the primary market. This temporary scheme was termed a "burden-sharing arrangement" and was permitted via Presidential decree. BI Governor Perry Warjiyo promised to wind down such operations after the pandemic, but Indonesia's lawmakers passed fresh legislation to make the quasi-central bank financing a permanent fixture for BI.

The use of "burden sharing" during Covid-19 raised eyebrows when first implemented but was justified given the fallout from the pandemic. The passage into law could call into question central bank independence, which in turn could cause some anxiety in the bond markets and the currency.

3 Jokowi's last full year in office ahead of early 2024 election

President Joko Widodo enters his last full year in office next year as he is not eligible to take up a third term as President. Indonesia holds presidential elections in February 2024. Jokowi appears to have made a veiled endorsement for his successor by suggesting that Indonesians vote for a candidate with "white hair" and "wrinkles". Opinion polls currently have three front runners: Central Java Governor Ganjar Pranowo, former Jakarta governor Anies Baswedan and former defence minister Prabowo Subianto.

It will be interesting to see how Jokowi spends the last 14 months of his term as he could still pass key legislation given his control over the house of representatives. Key legislative bills include the New Capital City (NCC) law and a new penal code. In particular, the NCC could positively impact growth potential as amendments could bring in a fresh round of investment given the capital-intensive requirements to move the capital from Jakarta to East Kalimantan.

Jokowi, on the other hand, may become more involved in the campaign by explicitly endorsing one of the three front runners - a move which could distract him from passing amendments to existing laws or drafting fresh legislation.

Indonesia summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	4.9	4.2	4.1	4.6	4.7	5.2	4.4	4.4	4.5
Inflation (YoY%)	5.4	5.3	5.0	4.5	4.3	4.2	4.8	3.7	3.4
Trade balance (bn$ EOP)	4.5	4.2	4.3	3.8	3.6	4.5	3.6	3.5	3.8
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
BI policy rate (%)	5.5	5.75	6.0	5.75	5.5	5.5	5.25	5.0	4.5
10Y bond yields (%)	7.2	7.3	7.2	7.1	7.0	7.2	7.3	7.1	6.8
USD/IDR	15,650	15,200	15,000	14,800	14,750	14,600	14,800	14,500	15,000

Source: Badan Pusat Statistik and ING estimates

Philippines: 'Revenge' spending to fade as new central bank governor takes over

Philippine growth received a nice boost from 'revenge' spending but we don't think that will continue in 2023

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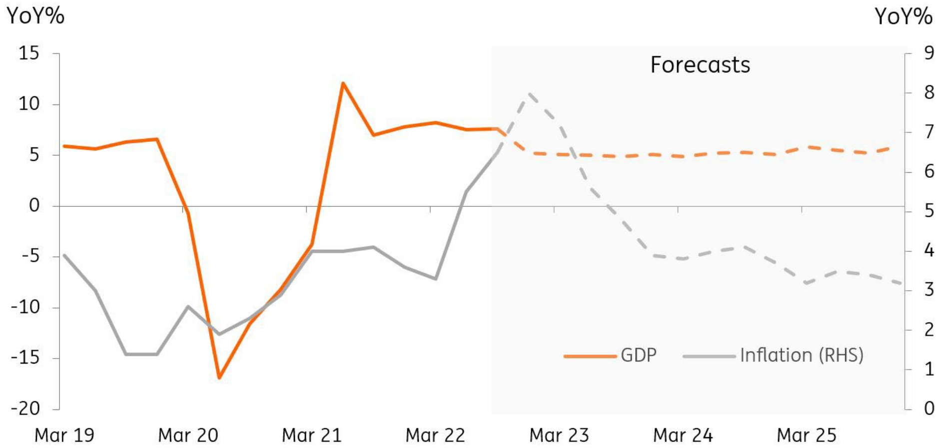
Philippines: At a glance

The Philippine economy benefited from election-related spending in the first half of 2022 on top of pent-up demand after mobility restrictions were finally relaxed. Lockdowns in the country were particularly long (almost two years) which may be contributing to 'revenge' spending, which appeared to be quite robust at the end of 2022. Household consumption remained solid despite surging prices and rising borrowing costs. In particular, spending on items such as air travel, restaurants and hotels and recreation has now registered at least four quarters of double-digit growth giving more credence to the reopening story.

Meanwhile, the potent mix of resurgent demand, currency depreciation and elevated commodity prices have all contributed to a pickup in price pressures. As a result, Bangko Sentral ng Pilipinas (BSP) has been busy, hiking rates by 350bp in 2022. BSP Governor Felipe Medalla has been particularly worried about the peso's weakness given its impact on inflation but we could see an eventual reversal in policy stance as early as the first quarter of 2023.

GDP and inflation outlooks



Source: Philippine Statistics Authority and ING estimates

3 Calls for 2023

1 **Revenge spending to fade by 2Q 2023 after savings depletion**

Pent-up demand explained the better-than-expected growth numbers from the Philippines recently, but we need to ask the following questions: how much longer will this last? And more importantly, how are households funding these purchases amidst multi-year high inflation? In the past, surging prices resulted in a sharp cutback in spending, however, the reopening story appears to be more compelling, at least for now.

Robust spending is likely supported by improving labour market conditions. However, we believe that the recent run of spending may also be funded by a drawdown in savings. The most recent BSP consumer expectations survey showed a decline in the number of households able to set aside savings. This could explain why consumption remains strong despite the twin headwinds of surging prices and rising borrowing costs.

With savings likely depleted to fund an extended run of spending, we expect households to eventually move to rebuild savings by the second quarter of 2023. As households shift a portion of their income back to savings, household spending should fade, resulting in the much-anticipated pullback in consumption, with GDP growth potentially slowing to below 5.0 YoY%.

2 **BSP policy stance up in the air but high inflation to persist**

Although the current BSP governor has expressed his preference to match any Federal Reserve policy adjustment from here on, Governor Medalla is set to retire by July 2023. Thus, we can expect the BSP to maintain a 100bp differential with the Fed but only until mid-2023. After that, we believe that the policy direction and the pace of any adjustment by the BSP next year will be largely dependent on who President Marcos appoints to head the central bank. And his choice for this post will be a key point to watch next year.

Regardless of who will sit as the BSP governor, inflation will likely stay stubbornly high in 2023. Inflation is expected to peak by the end of 2022 at around 8.2% YoY and then only grind lower throughout 2023. Price pressures are spread across the CPI basket with nearly 60% of the items experiencing inflation above 4% YoY suggesting price pressures are well entrenched. Thus, we forecast 2023 full-year inflation to settle at 5.4%.

3 **Debt to GDP ratio still an issue. Wealth fund pushed by new administration**

The current government debt-to-GDP ratio remains elevated (62.5%) and should remain above 60% for the next four years. The government expects this ratio to slip below 60% by 2026 suggesting that tight fiscal space will be the norm in the medium term. This would mean that government outlays will only have a limited ability to support growth should the economy face headwinds and this could in turn cap growth prospects for the Philippines.

Given the tight fiscal space, the new administration is pushing for the creation of a sovereign wealth fund (SWF) to help attract foreign investors and generate fresh revenues. The proposed SWF hopes to attract foreign investors for big-ticket infrastructure projects. If successful, the SWF would help bring in foreign currency to help stabilise the currency and boost capital formation although we need to wait for more details on how the fund would operate.

Philippines summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	7.8	4.2	4.7	5.0	4.9	7.8	5.0	5.1	5.6
Inflation (YoY%)	7.9	7.2	5.6	4.9	4.0	5.8	5.4	3.9	3.3
Remittance (YoY%)	3.0	2.5	3.6	4.2	3.5	3.0	3.5	4.1	2.8
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
BSP policy rate (%)	5.5	5.75	6.0	5.75	5.50	5.0	4.75	4.5	3.5
10Y bond yields (%)	7.60	7.45	7.2	7.1	6.75	6.8	6.75	6.5	6.0
USD/PHP	57.5	57.0	56.25	55.8	55.75	55.5	55.8	55.0	53.0

Source: Philippine Statistics Authority and ING estimates

Singapore to feel impact from slowing trade

The projected global downturn will impact Singapore. Will the return of tourists cushion the blow?

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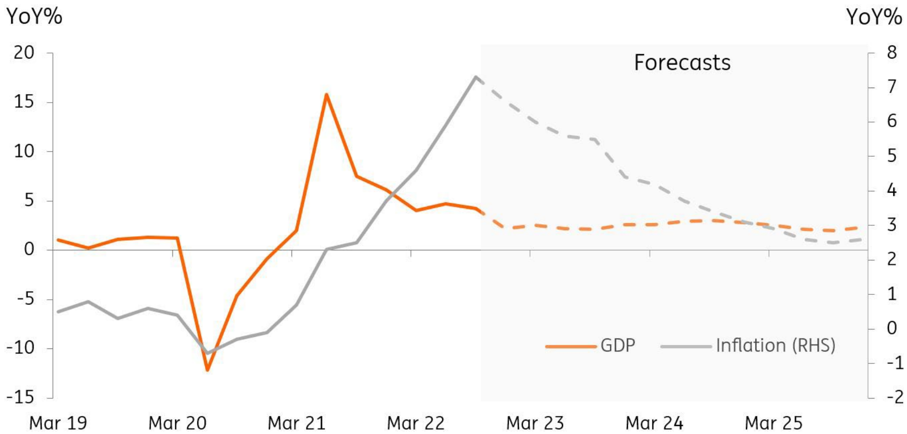
Singapore: At a glance

Singapore managed to record respectable growth in 2022, supported by an improvement in global trade and robust domestic consumption, but momentum is now fading. The sharp uptick in inflation and supply disruptions caused by China's repeated lockdowns due to Covid have been key factors for the moderation in growth momentum.

Surging inflation and rapid tightening from global central banks worked against the economy, which in turn forced aggressive action from the Monetary Authority of Singapore (MAS). The rise in price pressures was so pronounced it warranted tightening from the MAS at two non-policy meetings, on top of action during both scheduled meetings.

Meanwhile, industrial production and exports have been weighed down by softer demand from China and the rest of the world. While multi-year high inflation likely capped household spending, resurgent visitor arrivals may have provided a lift to department store sales.

GDP and inflation outlooks



Source: CEIC, ING estimates

3 Calls for 2023

1 Singapore GST implementation to keep inflation elevated, slow growth

The planned increase in Singapore's goods and services tax (GST) was pushed through on 1 January 2023. Previously delayed due to the pandemic, the GST rises from 7% to 8% in 2023 and should impact both the inflation outlook and growth momentum next year. The latest inflation forecasts from the MAS incorporate the scheduled GST increase, with core inflation expected to settle between 3.5% to 4.5% for the year. Relatively high inflation should cap household consumption next year as overall economic activity is set to slow due to global factors.

Furthermore, given that core inflation will likely stay well above the MAS's core inflation target of 2%, we also believe that the central bank will be forced to retain tight financial conditions to help bring inflation back to target. The backdrop of tight financial conditions coupled with high inflation should weigh on growth, and we expect full-year growth to settle at 2.5% year-on-year in 2023.

2 Slowing global trade to dent growth momentum further

Expectations for a recession in the US and Europe have sparked concern about slowing global trade for the past few months. Rapid fire rate hikes from major central banks and stubbornly high inflation all point to a sharp slowdown in growth around the world which should reduce overall demand for goods and services.

Early signs that this development may be impacting Singapore surfaced late in 2022 with non-oil domestic exports (NODX) falling sharply, by more than 14% YoY last November. Some were pinning their hopes on the much-anticipated economic reopening by China, however, with China's recent surge in cases, we remain sceptical that we will see any benefits from this anytime soon, or on the scale that was previously expected.

What we can be sure of is the projected recession in the US and most of Europe which will definitely send ripples through the ASEAN export supply chain. Singapore will likely feel the impact of the slowdown in global trade and this factors into our modest growth projection for 2023.

3 Return of tourist arrivals to provide counterbalance to global headwinds

Singapore's growth momentum appears challenging given the projected slowdown in global trade. But one brighter spot for the economy is the return of foreign visitor arrivals.

In November, Singapore recorded 816,758 visitor arrivals, a little more than half the number it used to receive prior to Covid-19 but still more than the 330,059 visitors received for all of 2021. The influx of tourists boosted the services sector with hotels, restaurants and department stores benefiting from their return.

With most countries having fully relaxed border controls by now and with more people now more open to travel, we can expect a sustained increase in visitor arrivals for Singapore next year. The recovery in visitor arrivals will be even more pronounced if China can overcome its current Covid surges and its population resumes international travel again in large numbers. The projected global slowdown could blunt the impact of tourism to some extent, but if Singapore were to receive more visitors in 2023 than it did in 2022, we could expect a decent boost from the resurgent services sector to act as a counterweight to softer domestic demand and slowing global trade.

Singapore summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	2.2	2.7	2.2	2.2	2.8	3.8	2.4	2.8	2.2
Inflation (YoY%)	6.6	6.0	5.6	5.5	4.4	6.1	5.4	3.6	2.7
NODX (YoY%)	-10.0	-3.5	-4.0	2.1	4.5	-10.0	4.5	8.5	5.5
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
3M bond yields (%)	4.2	4.05	3.8	3.6	3.0	2.5	2.25	2.0	2.0
USD/SGD	1.35	1.35	1.34	1.33	1.33	1.31	1.32	1.3	1.3

Source: Singapore Department of Statistics and ING estimates

India will do better than most of its Asian peers in 2023

Proactive policy in 2022 leaves India in a good position to benefit from easier conditions in 2023. India's lesser reliance on trade with China also provides a buffer, while a rethink on global bond market inclusion for government securities could see substantial capital inflows

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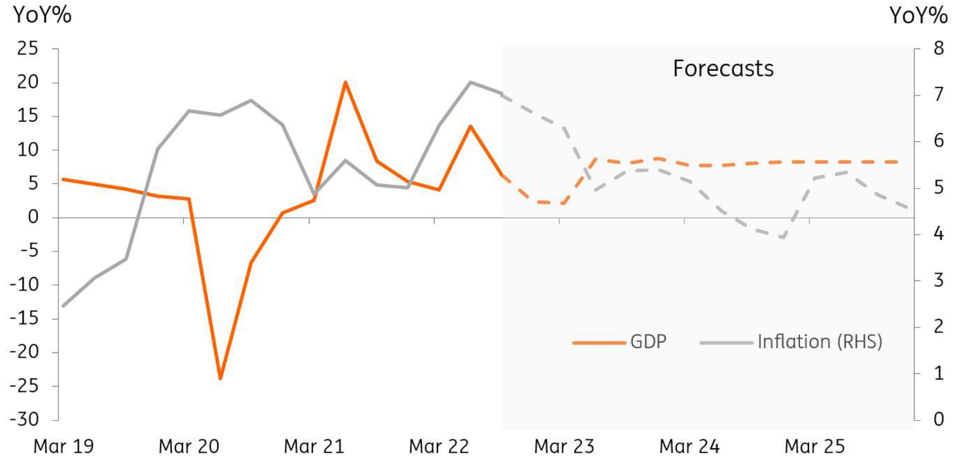
India: At a glance

India’s economy is bucking the global trend, showing signs of strength in the third quarter of 2022 as the annual growth rate slightly beat expectations to grow at 6.3%YoY. That leaves GDP on track to grow by 6.3% for the full calendar year of 2022 and a bit less than 6% for the fiscal year 2022/23.

While GDP remains relatively robust, inflation has shown clear signs of peaking out. The latest inflation print for November came in at just 5.88%YoY below the Reserve Bank of India’s target and materially lower than the policy repo rate (currently at 6.25%) following a 35bp rate hike in December. The INR remains one of the region's weaker currencies and has not held on to earlier gains in November and December.

GDP and inflation outlooks



Source: CEIC, ING estimates

3 calls for 2023

1 Nearing peak rates

Rates are close to a peak and will come down before the end of the year. Now that policy rates are positive in real terms (which will continue as the high inflation tide recedes), we're confident that the peak will be close even without further hikes from the RBI. There also remains a chance that we may already have seen it.

The next rate decision doesn't take place until 8 February and could still be influenced by an additional inflation release on 12 January. With inflation in India likely closing in on 4-5% by the middle of the year, we believe the central bank could start to tentatively take back some of its tightening before the end of 3Q23.

2 Global bond market inclusion

Indian bonds will be included in global indices in 2023. Both JP Morgan and FTSE Russell kept Indian bonds on their watch list for inclusion in 2022 and are expected to make a decision on inclusion early this year. Key reasons for excluding Indian government bonds from their indices in 2022 include tax treatment for foreign investors, which the government has not seemed in any hurry to change its stance on.

Lengthy settlement of INR bond transactions which takes place onshore is not helping, although moving settlement to Euroclear is not a deal-breaker given that neither Chinese nor Indonesian bonds are settled there. Adding Indian government bonds to these indices will fill a gap left by the exclusion of Russian bonds. At stake for India is an estimated $40bn of capital inflows that will help pay for the current account deficit and support the INR.

3 India to benefit from FDI inflows

India will continue to climb the rankings of foreign direct investment destinations in 2023, even as the external economic outlook darkens and China re-opens. India is increasingly being seen as an alternative destination for investment following policy measures designed to ease FDI inflows and promote the manufacturing industry, as well as investment issues in China (trade wars, tech wars, zero-Covid etc). India is the only economy in Asia to offer the potential for scalability, which was one of the main attractions of China. Its younger population and growing middle class also make it a sizable end-market for sales, in addition to being a site for export production.

India summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	2.4	2.2	8.6	8.1	8.8	6.3	6.8	8.0	7.8
Inflation (YoY%)	6.6	6.3	5.0	5.4	5.1	6.8	5.5	4.4	5.0
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
Repo rate (%)	6.25	6.25	5.90	5.40	5.15	4.90	4.90	4.90	4.90
10Y bond yields (%)	7.20	7.10	6.80	6.50	6.30	6.30	6.50	6.60	6.80
USD/INR	82.0	81.0	80.0	80.0	82.0	83.0	84.0	84.0	84.0

Source: CEIC, ING estimates

Australia: GDP growth to remain below 2% this year

While parts of the Australian economy, in particular the labour market, remain robust, there are already clear signs that the economy is slowing, and it should slow further in 2023. That at least will provide some scope for a relaxation of monetary policy as inflation is also showing signs of peaking out

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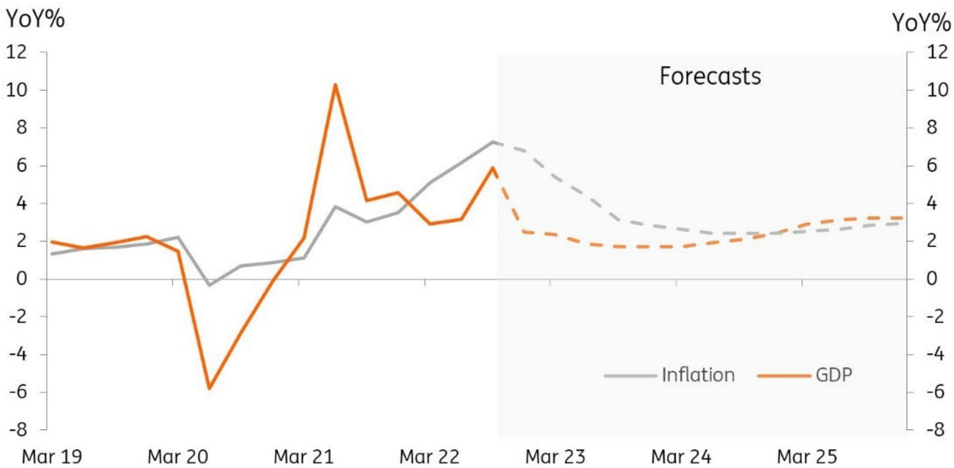
Source: iStock

Australia: At a glance

The Australian economy is slowing down. In the third quarter of 2022, the GDP growth rate dropped to 0.6% quarter-on-quarter. And even though that still leaves the year-on-year growth rate looking very robust at 5.9%, most of that is due to base effects, and that growth rate will drop sharply in the fourth quarter of 2022. Inflation also appears to have peaked, with the new monthly CPI series showing inflation dropping below 7%. House prices too have been falling rapidly in the last quarter as the Reserve Bank of Australia has increased the cash rate to squeeze out inflation. Business investment remains depressed thanks to the higher rate environment and weak external backdrop, and while the trade surplus remains impressive, it is no longer adding to growth. The Australian dollar (AUD) has been moving in line with broader US dollar (USD) trends and is showing signs of strengthening again.

GDP and inflation outlooks



Source: CEIC, ING estimates

3 calls for 2023

1 GDP growth to be less than 2% in 2023

GDP growth should fall below 2% for the full year. After projected growth of around 3.6% for 2022, GDP growth is expected to slow to a sub-2% pace in 2023. The household sector is running out of room to keep spending growing in the face of higher inflation and much more subdued nominal wage growth. Households are also running out of room to smooth spending by reducing savings, as savings rates have already fallen sharply from their pandemic peaks and the falling values of real assets (property) will also weigh on their balance sheets. Large discrete mortgage re-sets will probably not do too much damage, as many households are already making overpayments, but this will cause problems for some.

2 House prices will fall from their 2022 peaks

House price growth should drop to nearly -10% YoY. In year-on-year terms, median Australian house price growth has already fallen from its pandemic stimulus-induced peak rate of 25.0% YoY, to just 1.1% YoY in 3Q22. Further small quarterly declines in the first and second quarters of 2023 will all but ensure that the annual rate of house price growth falls to close to -10% YoY at its most negative, delivering a full-year decline of just over 7%. Prices should stabilise by the end of 2023, but it may be closer to the end of 2024 before house prices are recording positive year-over-year growth rates again.

3 Cash rates close to peak and could fall

Cash rates will peak at only 3.6% and will start to be reduced before the end of the year, in our view. The cash rate target was raised a further 25bp in December and now stands at 3.1%. We are calling for a peak rate of only 3.6%, in other words, after only another two rate hikes of 25bp each. This forecast derives from our assumptions of more slowdowns in GDP growth, further declines in consumer price inflation, worsening negative house price growth, and the discrete impacts of rate hikes on mortgage payments. Rates ending the year lower than their forecast peak will lessen the subsequent re-set impact in early 2024 and sow the seeds for a broader recovery.

Australia summary forecast table

	4Q22	1Q23	2Q23	3Q23	4Q23	FY2022	FY2023	FY2024	FY2025
GDP (YoY%)	2.5	2.3	1.9	1.7	1.7	3.6	1.9	2.0	3.1
Inflation (YoY%)	6.8	5.4	4.4	3.1	2.8	6.3	3.9	2.5	2.7
House prices (YoY%)	-5.8	-9.5	-9.2	-5.9	-4.4	6.3	-7.3	0.8	3.4
Unemployment rate (%)	3.5	3.6	4.1	4.7	4.8	3.5	4.8	3.9	3.6
	4Q22	**1Q23**	**2Q23**	**3Q23**	**4Q23**	**1Q24**	**2Q24**	**4Q24**	**4Q25**
Cash rate target (%)	3.1	3.6	3.6	3.1	2.6	2.35	2.35	2.35	2.6
10Y bond yields (%)	3.4	3.3	3	2.9	2.7	2.7	2.7	2.7	3.2
USD/AUD	0.68	0.69	0.7	0.72	0.72	0.72	0.7	0.7	0.68

CEIC, ING estimates

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