

# Asian Development Outlook 2011

## Comments

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Hong Kong, 7 April 2011

# Roadmap to comments

- General thoughts
- A quick look at recent developments
- The outlook for 2011-12
- Key upside risks and policy recommendations
- Downside risks should not be forgotten

# General thoughts

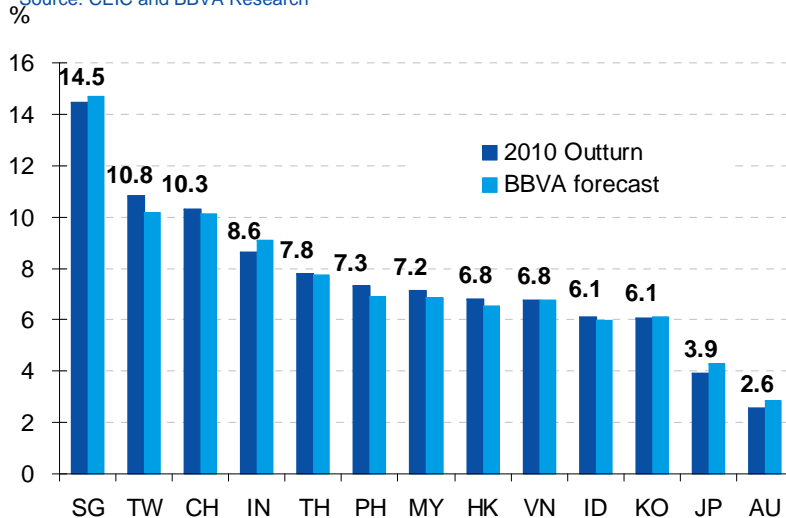
- Great report
- Outlook for the region very similar to that of BBVA Research, even for most countries individually
- Agree with thrust of recommendations
  - Risk on the upside
    - Can Asia die of success/excess?
  - However some risks on the downside also

## Recent developments

- Forecast errors: GDP and CPI
- GDP outturns in 2010 outpaced forecasts in a number of cases, due to a strong Q4
- Inflation outturns in 2010 were broadly in line with forecasts, and inflation continues to trend higher
- High frequency indicators in Q1 have so far surprised to the upside

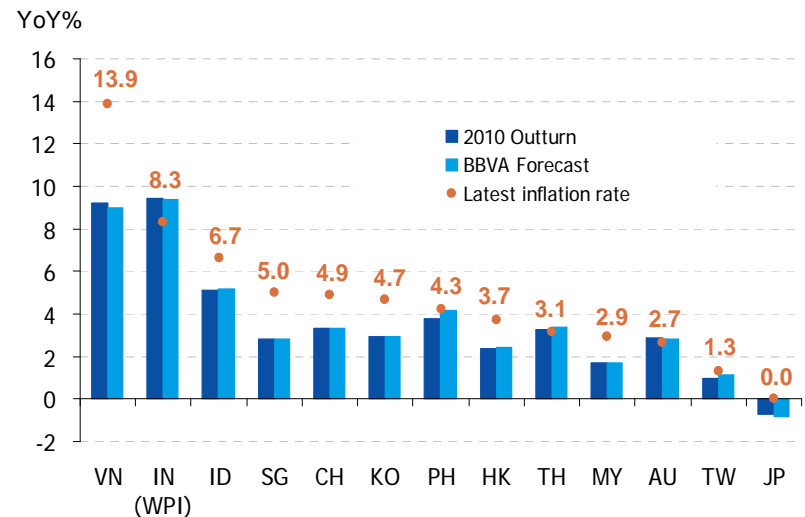
### BBVA 2010 GDP growth forecast vs. Outturn

Source: CEIC and BBVA Research



### BBVA 2010 CPI growth forecast vs. Outturn

Source: CEIC and BBVA Research



### Key economic indicators: outcome versus bloomberg consensus

2011Q1\*

Asia	Retail sales	CPI	PPI	Industrial production	Exports	Unemployment rate
	Above Consensus	Above Consensus	Above Consensus	In line	Above Consensus	Below Consensus

\* based on available Q1 data by April 06, 2011

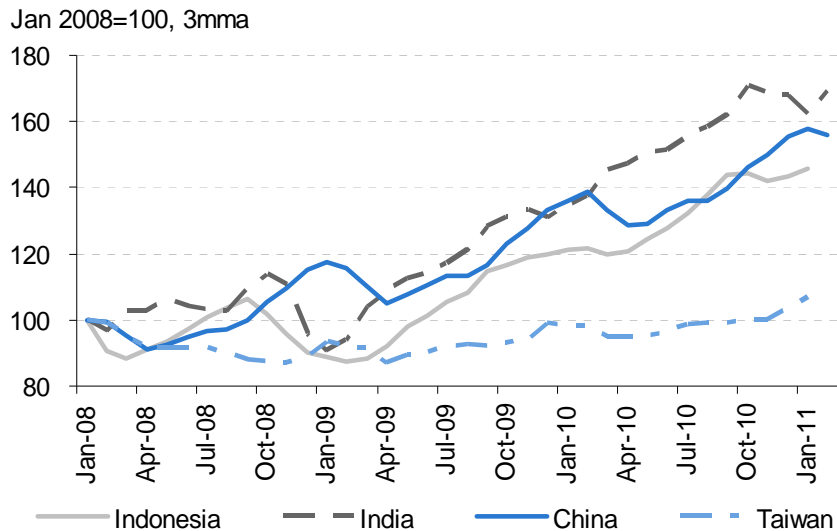
## Recent developments

### Growth has become more self-sustaining

- Private consumption has been picking up
- A revival of credit growth is leading to investment spending and rising production

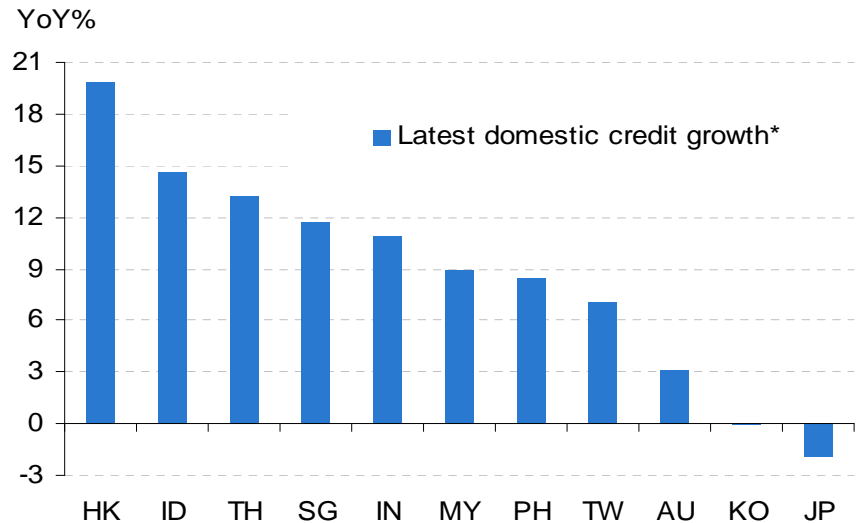
### Retail sales have been rising on improved labor markets and consumer confidence

Source: CEIC and BBVA Research



### Rapid credit growth is supporting domestic demand

Source: CEIC and BBVA Research



\* In real terms. 2011 February data for HK, SG, MY, TW, and JP, 2011 January data for IN, ID, KO, PH, and TH, and 2010 December data for AU.

## Recent developments

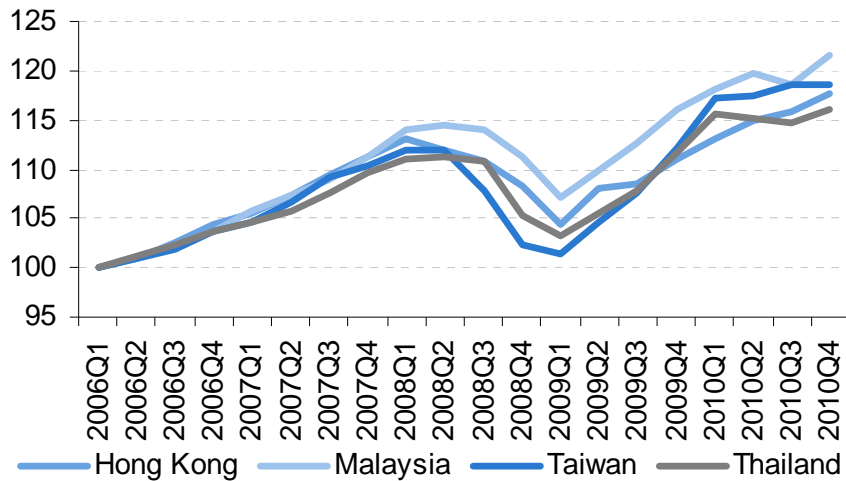
### Overheating pressures are present

- GDP levels are well above pre-crisis, and output gaps are closed
- Capacity utilization rates are back to normal

#### GDP levels\* are well above pre-crisis

Source: CEIC and BBVA Research

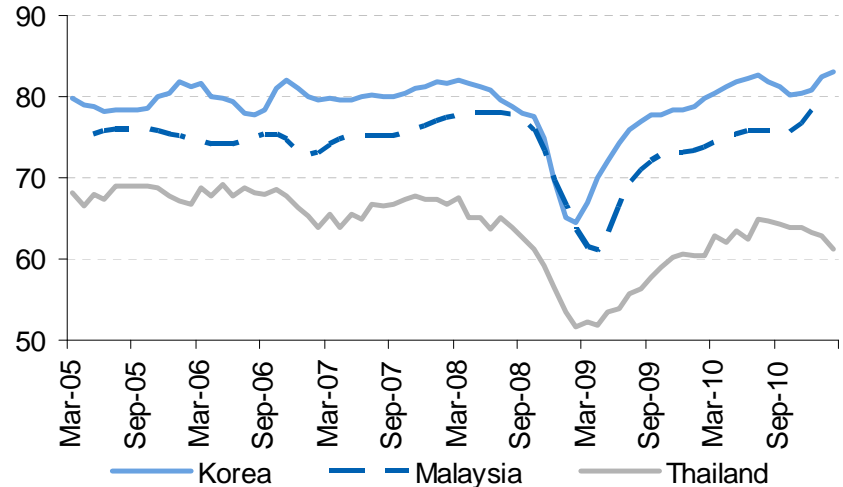
2006Q1=100



#### Capacity utilization ratios are high

Source: CEIC and BBVA Research

%, 3mma



\* Real GDP in level terms, seasonally adjusted

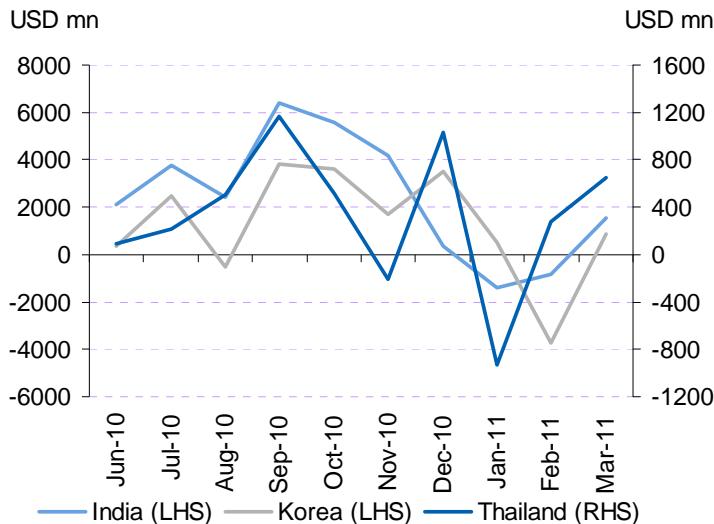
## Recent developments

### Capital inflows show signs of resuming after a brief lull

- Inflows diminished for a time earlier in the year due to risk aversion
- More recently there is evidence a resumption of inflows, which is creating more currency appreciation pressure

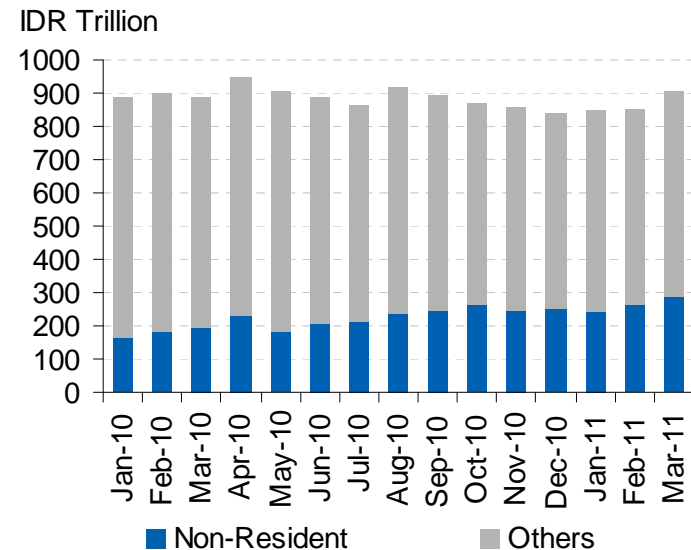
### Net foreign purchases of equities have resumed...

Source: Bloomberg and BBVA Research



### ...as seen by foreign holdings of Indonesian bonds also slightly increased

Source: Bank Indonesia and BBVA Research



## Recent developments

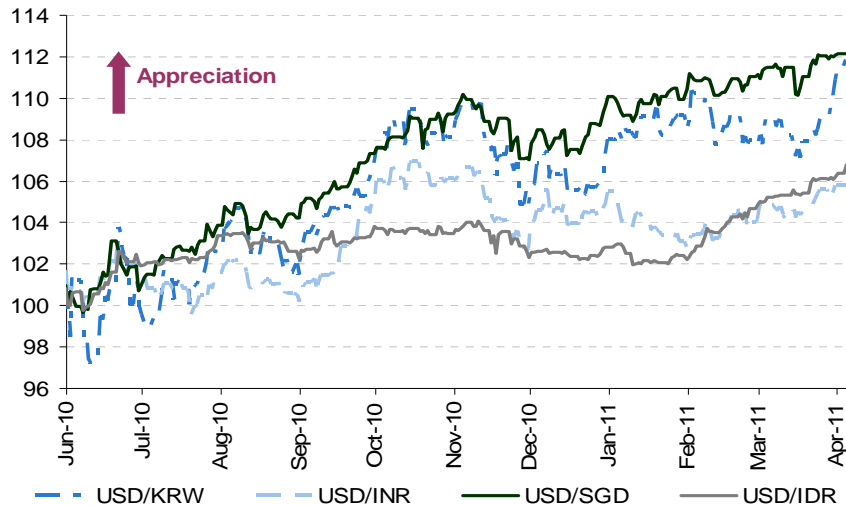
### Currency appreciation is resuming

- A resurgence of capital inflows
- Some countries are allowing faster appreciation to help tame inflation (e.g., Indonesia and Singapore)

### Asian currencies continue to gain ground against the USD...

Source: Bloomberg and BBVA Research

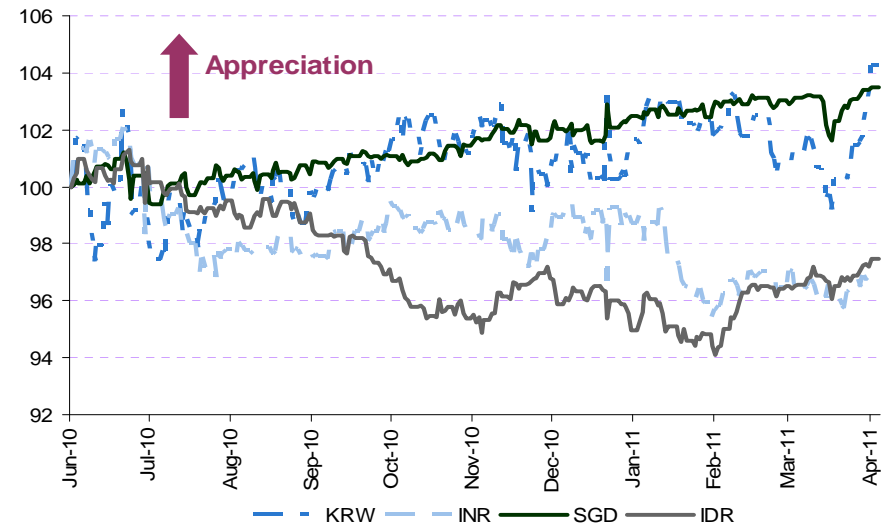
June 1, 2010=100



### ...although appreciation has been less in nominal effective terms

Source: Bloomberg and BBVA Research

June 1, 2010=100





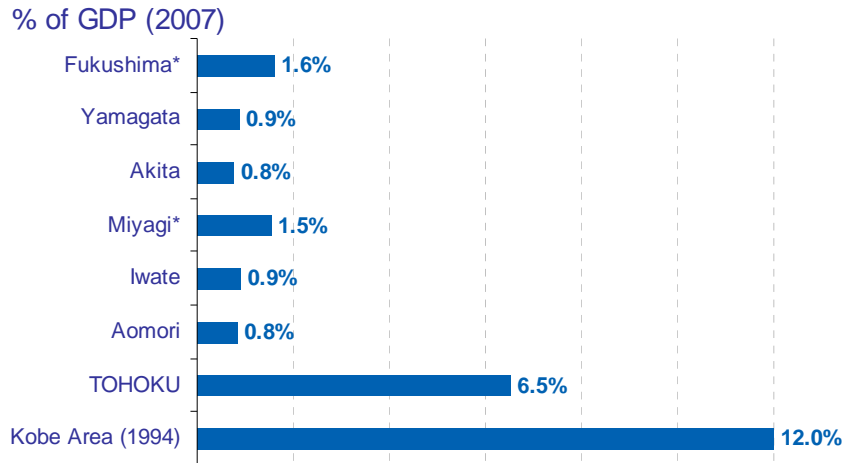
## Outlook for 2011-12

### Assessing the impact of Japan's earthquake

- The economic impact is estimated to be temporary and modest—policy responses and rebuilding are usually offsets following natural disasters—although uncertainty is still high.
- Nevertheless, we propose to raise our estimate of the impact in 2011 to -0.5% from previously (-0.2%) given the ongoing nuclear threat, and the severe impact on consumer and business confidence.

### Tohoku area has a smaller economic size relative to Kobe area...

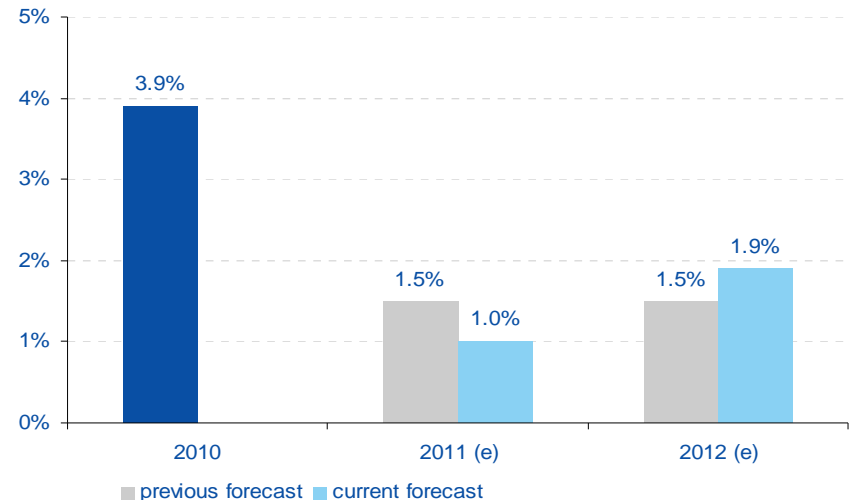
Source: CEIC and BBVA Research



\*Areas most affected by the earthquake and the nuclear leak

### The quake's impact on Japan is estimated to be temporary and moderate

Source: BBVA Research and IMF



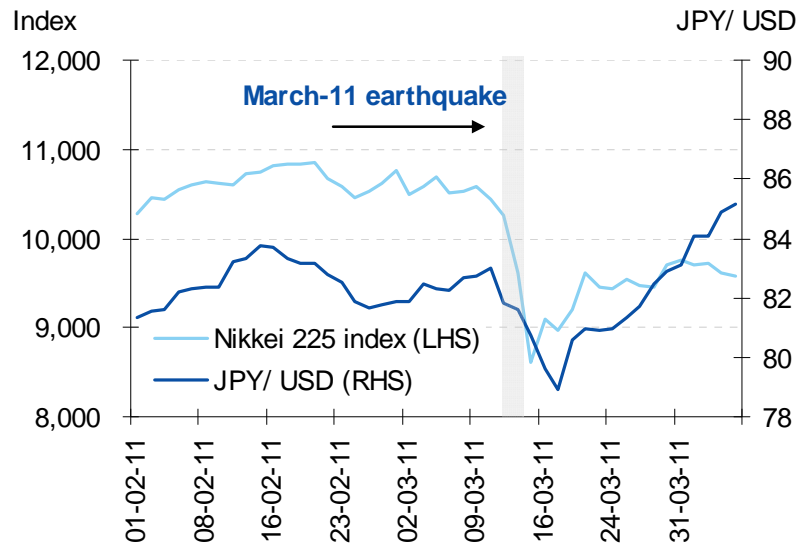
# Outlook for 2011-12

## Assessing the impact of Japan's earthquake

- The impact on other Asian economies should be modest, although concern lingers about disruptions to supply chains, especially for Taiwan and Thailand which import heavily from Japan

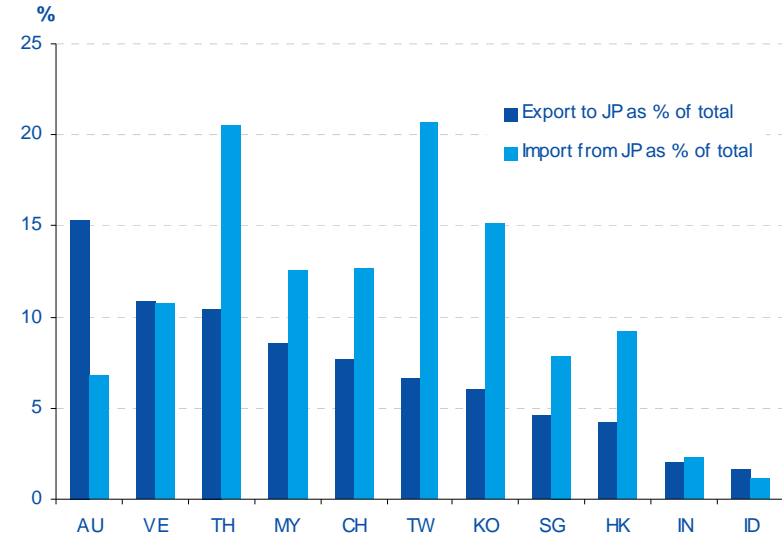
### Stock market has rebounded fast, and yen is back to the pre-quake level

Source: CEIC and BBVA Research



### Supply chains could be disrupted as Asian economies rely on Japan for components

Source: BBVA Research and IMF



# Where are the upside risks

- **Food inflation** extremely important the more the poorer the countries
  - Policies to ease imports should be introduced when domestic supply is a bottle neck
- Even more problematic if not accompanied by **wage inflation**
  - **China** is moving away from previous restrain policies
  - Helping rebalancing towards more consumption
  - Also leading to more real exchange rate appreciation

# Where are the upside risks

- **The extent of capital inflows** is another way to measure the upside risks
  - More moderate than what people have in mind
  - Even some reversals
- **Nominal exchange rate appreciation** continues but at a slow pace
  - Generally less than in Latin America, another region with overheating and inflation risks
- **Nominal appreciation should be seen more as a risk moderation tool** than a risk
  - As long as such appreciation is not too sudden and too large but we are clearly far from that situation
- **More generally, Asia should not fear some loss of competitiveness**
  - Still extremely competitive compared with international average
  - Higher inflation than trading partners is probably a more costly way to reduce competitiveness than nominal appreciation
  - More so if inflation is concentrated on food and other first priority products

# Risks are now broadly balanced

- Downside risks have increased recently Downside risks have increased recently :
  - Higher oil prices
  - Risks of lingering nuclear contamination in Japan and disruptions to supply chains
  - Ongoing risks of a hard-landing in China from monetary tightening (unlikely)
- On the domestic side, inflation and asset price bubbles continue to pose the largest risks
- Country-specific risks:
  - Japan is coping with its “triple disaster”
  - Thailand faces election uncertainties (July)
  - Vietnam has been struggling to maintain macroeconomic stability in the face of large fiscal and current account deficits
  - India is tightening monetary policy to prevent overheating
  - Inflation pressures for Hong Kong, Korea and Indonesia bear watch

# Downside risks have increased recently

- Higher oil prices due to supply concerns from the North Africa and Middle East revolts
  - Risks of lingering nuclear contamination in Japan and disruptions to supply chains
  - Europe is a key trading partner for several Asian countries, including China
  - Ongoing risks of a hard-landing in China from monetary tightening (very unlikely)
- 
- Country-specific risks:
    - Japan is coping with its “triple disaster”
    - Thailand faces election uncertainties (July)
    - Vietnam has been struggling to maintain macroeconomic stability in the face of large fiscal and current account deficits
    - India is tightening monetary policy to prevent overheating
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## All in all

- Asia is doing fine but it cannot be complacent
- It needs to be proactive in implementing the right policies not to die of success/excess without being trapped in any of the downside risks
- Those downside risks, though, should not be used as an excuse not to take action
- The region needs to acknowledge its new role in the world:
  - More as a growth engine than a follower benefitting from the rest of the world's demand

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