

Weekly Watch

Asia

23 December 2011
Economic Analysis

Asia

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Tensions ease over North Korea

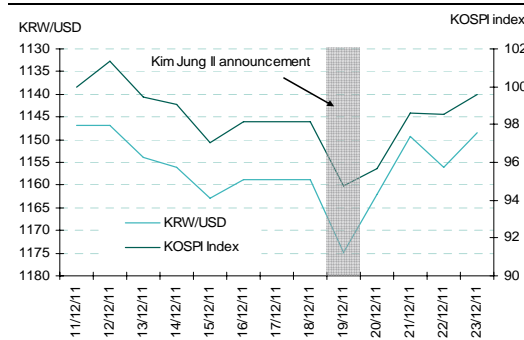
Markets in Korea have more than regained their losses from earlier in the week on news of the death of Kim Jong Il in the North (Chart 1). After sliding by 3.4% on Monday, the KOSPI ended up by 1.5% for the week as immediate fears of instability receded and as positive news flow from Europe and the US boosted regional markets in general. While it is anyone's guess of how developments will play out with the succession process in North Korea (at the time of this writing, prospects for a transition without military incidents appeared good), we continue to hold a positive view of South Korea's economic resilience, as explained in our [Korea Economic Watch](#). Strong fundamentals should help to weather market nerves over the North, while improving external debt and banking indicators reduce, though do not eliminate, vulnerability to the crisis in Europe.

Inflation is easing as growth slows

Inflation continues to ease across much of the region, with Hong Kong (5.7% y/y vs. 5.8% prior), Malaysia, (3.3% y/y vs. 3.4% prior), and Vietnam (18.1% vs. 19.8% prior) all reporting lower inflation for the month of November, although it ticked up in Singapore (5.7% y/y vs. 5.4% prior) (Chart 2). (For more on Hong Kong, see our [Economic Watch](#)). This should set the stage for some monetary easing in the months ahead if external demand continues to weaken. Meanwhile, Taiwan export orders moderated in line with expectations (2.55 y/y; consensus: 2.8%), underscoring the strength of global headwinds that are expected to slow overall growth momentum in 2012 (see Highlights for more on Taiwan). Export outturns for November were released in Thailand (-12.4% y/y) and Japan (-4.5% y/y) (see Highlights), with each showing disappointing results due to weakening external demand and disruptions to electronics and auto part supply chains from the floods in Thailand. Singapore's industrial production also fell unexpectedly (-9.6% y/y; consensus: 12.2%).

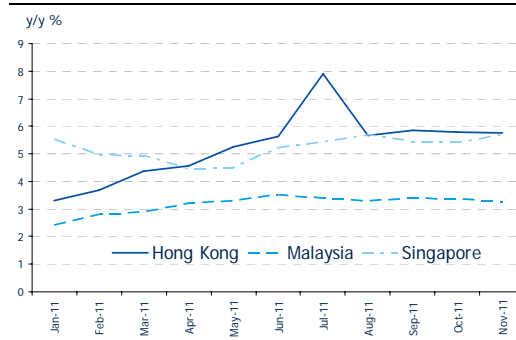
As markets take a break in the coming weeks, the data flow will be relatively light. A key focus will be on China's official PMI outturn on January 1 (see Weekly Indicator). December inflation will be published in Korea, Thailand, and Taiwan, while Singapore will issue its advance GDP estimate for the fourth quarter. In Taiwan, the central bank will hold its quarterly policy meeting on December 29, and we expect the discount rate (1.875%) to remain unchanged.

Chart 1
Korean markets rebound as nerves ease



Source: Bloomberg and BBVA Research

Chart 2
Inflation has begun to decline



Source: Bloomberg and BBVA Research

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Highlights

Bank of Japan downgrades its outlook due to global headwinds

After a soft patch in Q4, the recovery should resume in 2012 on post-quake reconstruction

Cross-strait ties are the focus in Taiwan's Presidential elections

Taiwan's January elections will be watched for continued warming relations with China

Highlights

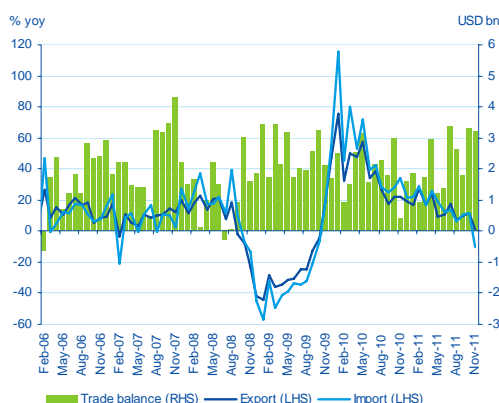
Taiwan's Presidential election centers on cross-strait ties with the Mainland

Taiwan will hold its next Presidential election on January 14. The winner will begin a 4-year term on May 20. The election pits the incumbent President Ma Ying-jeou and his ruling Kuomintang Party (KMT) against Ms. Tsai Ying-wen of the Democratic Progress Party. According to the latest surveys, which vary greatly and may not be very reliable, President Ma appears to be leading by a slim margin of around 4 percentage points. Some 16% of voters are reported to still be undecided.

Among the factors for the significance of the election are differences with respect to cross-strait ties with Mainland China. The KMT took office in 2008 on a platform of warming ties with the Mainland. Delivering on these promises, President Ma has forged a closer relationship with the Mainland. During Ma's term, direct commercial flights between Taiwan and the Mainland have been launched, tourism has been opened to Mainland visitors, and most significant of all, an Economic Cooperation Framework Agreement (ECFA) has been signed to boost bilateral trades and economic integration. The DPP, on the other hand, holds a more "pro-independence" position and a more cautious approach to cross-strait relations. The DPP held the Presidency during 2000-2008, a period marked by rising political tensions between the Mainland and Taiwan. The election also comes at a crucial time for the Taiwanese economy, which is slowing from weakening external demand (Charts 5 & 6). But whichever side wins, there are unlikely to be differences in the approach to domestic economic policies. Both parties, for example, plan to increase government spending on social welfare and strengthen support for the export sector.

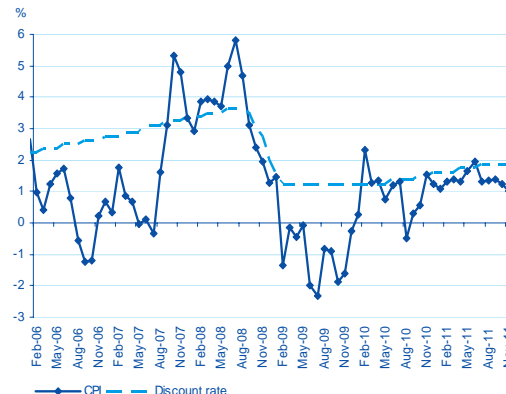
A DPP victory would probably not result in a sudden change in cross-strait policies, as the process has advanced and cannot be turned back quickly, if at all. Indeed, sensing public support for such ties, the DPP has recently warmed up to the idea of continuing closer cross-strait economic ties. In addition, the likelihood of the KMT maintaining a majority of Legislative seats would also make any significant policy changes unlikely in such a scenario. Nevertheless, a DPP victory could slow down the pace and tone of steps toward further integration.

Chart 5
Taiwan's export growth is weakening



Source: BBVA Research and Bloomberg

Chart 6
Inflation remains very low



Source: BBVA Research and Bloomberg

Bank of Japan downgrades its outlook due to global headwinds

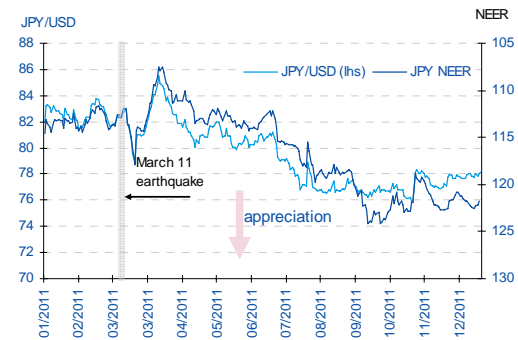
For the second straight month, the Bank of Japan (BoJ) has downgraded its assessment of the domestic economic outlook, saying in its monthly policy statement this week that the recovery has “paused” due to global headwinds and the strong yen. As expected, the BoJ left the policy rate unchanged at 0-0.1%, and also left the size of its asset purchasing program unchanged at ¥55trillion—with interest rates at zero, the asset purchase program is the main policy instrument available to affect credit conditions. In addition to declining external demand, the BoJ also noted that the recent floods in Thailand have put downward pressure on the auto and electronic sectors. Japanese exports, the main growth driver, fell for a second consecutive month, by -4.5% y/y in November. Meanwhile, the BoJ's quarterly Tankan survey of business sentiment showed disappointing results when it was released earlier this week. Also, on Wednesday the Tokyo-based Rating and Investment Information agency lowered its AAA rating for the first time, a reminder that Japan's high public debt burden (over 200% of GDP), while currently overshadowed by the crisis in Europe, could become a problem in the future.

For its part, the Japanese government, has just approved a fourth extra budget (¥2.5 trillion 0.5% of GDP) to support post quake reconstruction, on top of three extra budgets of ¥18 trillion in total for the fiscal year ending March 31. The fourth extra budget aims to help finance relief programs for those suffering from the March 11 disasters, and to support auto manufacturers and farmers.

In view of the above, we expect Japan's growth to have stalled in the fourth quarter, following a sharp rebound of 5.6% (annualized, seasonally adjusted) in the third quarter, which would put annual growth at an estimated -4% for the year. Looking ahead, we still expect the recovery to resume in 2012 as the ongoing post-quake reconstruction helps to bolster consumer spending and business investment.

Chart 7

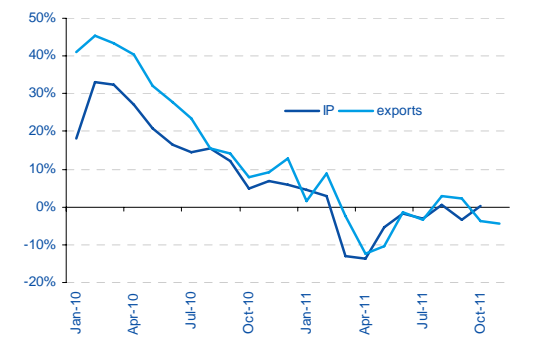
Japanese yen has been stable under the threat of more fx intervention to stem appreciation



Source: BBVA Research and Bloomberg

Chart 8

Japan's recovery has stalled in Q4



Source: BBVA Research and Bloomberg

Calendar Indicators

China	Date	Period	Prior	Cons.
Industrial Profits YTD YoY	27-Dec	NOV	25.30%	--
HSBC Manufacturing PMI	30-Dec	DEC	47.7	--
PMI Manufacturing	1-Jan	DEC	49	49.1
China Non-manufacturing PMI	3-Jan	DEC	49.7	--
China HSBC Services PMI	5-Jan	DEC	52.5	--
Hong Kong	Date	Period	Prior	Cons.
Exports (YoY)	29-Dec	NOV	11.50%	--
Imports (YoY)	29-Dec	NOV	10.90%	--
Retail Sales - Value (YoY)	3-Jan	NOV	23.10%	--
Japan	Date	Period	Prior	Cons.
Vehicle Production (YoY)	27-Dec	NOV	20.30%	--
Housing Starts (YoY)	27-Dec	NOV	-5.80%	-4.90%
Overall Hhold Spending (YoY)	28-Dec	NOV	-0.40%	-1.20%
CPI Inflation (YoY)	28-Dec	NOV	-0.20%	-0.40%
Retail Trade YoY	28-Dec	NOV	1.90%	0.00%
Industrial Production YOY%	28-Dec	NOV P	0.10%	-2.00%
Singapore	Date	Period	Prior	Cons.
GDP (QoQ)	03-13 JAN	4Q A	1.90%	--
GDP (YoY)	03-13 JAN	4Q A	6.10%	--
Korea	Date	Period	Prior	Cons.
Industrial Production (YoY)	29-Dec	NOV	6.20%	6.10%
CPI Inflation (YoY)	30-Dec	DEC	4.20%	4.00%
Exports (YoY)	1-Jan	DEC	13.80%	6.70%
Imports (YoY)	1-Jan	DEC	11.30%	11.50%
Taiwan	Date	Period	Prior	Cons.
CPI Inflation (YoY)	5-Jan	DEC	1.01%	--
WPI YoY%	5-Jan	DEC	5.29%	--
Thailand	Date	Period	Prior	Cons.
Exports (YoY)	30-Dec	NOV	-0.10%	--
Imports (YoY)	30-Dec	NOV	20.60%	--
CPI Inflation (YoY)	4-Jan	DEC	4.19%	--
Vietnam	Date	Period	Prior	Cons.
CPI Inflation (YoY)	24-Dec	DEC	19.80%	--
GDP Constant Prices YTD (YoY)	24-30 DEC	4Q	5.80%	--
Industrial Production YoY	24-29 DEC	DEC	8.10%	--

Indicator of the Week: China's PMI for December (January 1)

Forecast: 50.2

Consensus: 49.1

Prior: 49.0

A rapidly declining monthly Purchaser Manufacturers' Index (PMI) in China has been one of the clearest signs of a slowdown in growth momentum. The official index slipped below the critical 50-threshold last month, indicating a contraction in economic activity, particularly in the export sector due to weakening external demand. The authorities have recently signaled a subtle shift in their policy stance toward greater support to growth, away from taming inflation, which has been declining in any event (to 4.2% y/y in November). At the end of November, the PBoC cut the RRR, the first sign of monetary easing. We expect the December PMI to rebound back into the expansion zone, based on an improved HSBC flash estimate and seasonality.

Calendar Events

Taiwan - Central Bank's Quarterly Policy Meeting, December 29

The benchmark rate is expected to be unchanged, with risks to the downside.

Current Consensus

1.875% 1.875%

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Markets Data

STOCK MARKETS	INDEX	Last price	% change over a week	Year to date	% Change over 1 Y
	China - Shanghai Comp.	2207.2	-0.8	-21.4	-22.7
	Hong Kong - Hang Seng	18569.2	1.6	-19.4	-18.9
	Taiwan - Weighted	7101.1	4.7	-20.9	-20.2
	Japan - Nikkei 225	8395.2	-0.1	-17.9	-18.9
	Korea - Kospi	1867.3	1.5	-9.0	-8.4
	India - Sensex 30	15813.4	2.1	-22.9	-20.9
	Australia - SPX/ASX 200	4140.4	-0.5	-12.7	-13.7
	Singapore - Strait Times	2673.1	0.5	-16.2	-14.8
	Indonesia - Jakarta Comp	3804.3	1.0	2.7	5.3
	Thailand - SET	1042.5	0.8	0.9	2.1
	Malaysia - KLCI	1493.7	1.9	-1.7	-1.4
	Philippines - Manila Comp.	4384.7	1.9	4.4	5.2

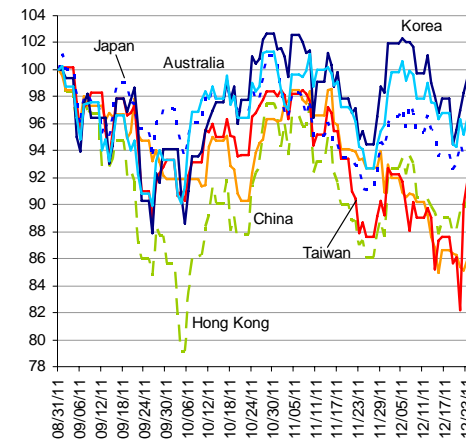
Last update: Friday, 11.45 Hong Kong time.

FOREIGN EXCHANGE MARKETS	CURRENCY	Spot	% change over a week	Forward 3-month	Forward 12-month
	China (CNY/USD)	6.34	0.18	6.36	6.39
	Hong Kong (HKD/USD)	7.78	0.06	7.78	7.77
	Taiwan (TWD/USD)	30.3	0.23	30.19	29.89
	Japan (JPY/USD)	78.1	-0.40	77.92	77.31
	Korea (KRW/USD)	1148	0.89	1155	1162
	India (INR/USD)	52.7	1.74	53.94	56.09
	Australia (USD/AUD)	1.02	1.95	0.99	n.a.
	Singapore (SGD/USD)	1.29	1.15	1.29	1.29
	Indonesia (IDR/USD)	9044	-0.10	9266	9664
	Thailand (THB/USD)	31.3	0.00	31.50	31.88
	Malaysia (MYR/USD)	3.16	0.72	3.17	3.20
	Philippines (PHP/USD)	43.5	0.94	43.62	43.74

Last update: Friday, 11.45 Hong Kong time.

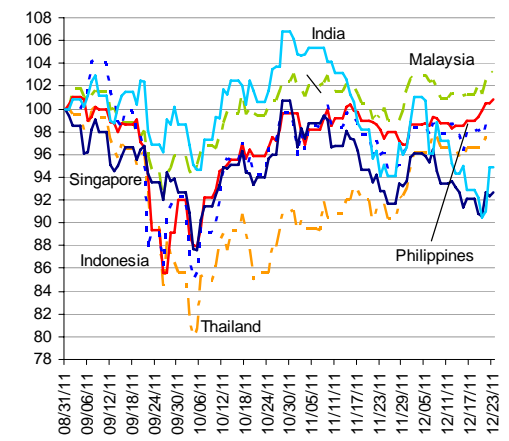
Charts

Chart 9
Stock Markets



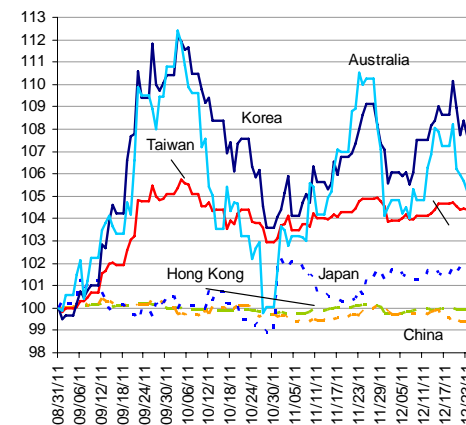
Source: BBVA Research and Bloomberg

Chart 10
Stock Markets



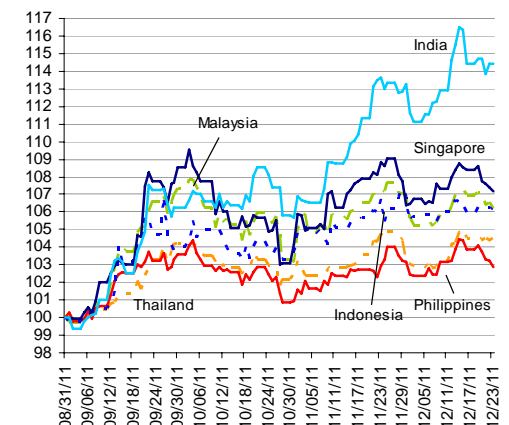
Source: BBVA Research and Bloomberg

Chart 11
Foreign Exchange Markets



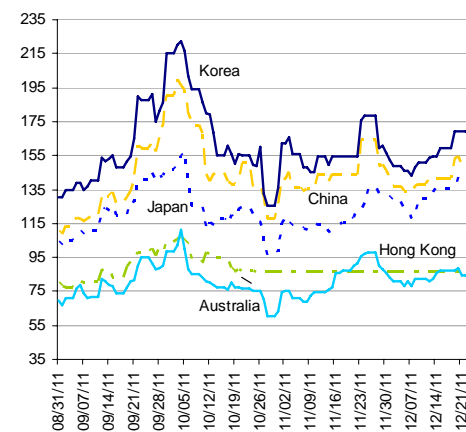
Source: BBVA Research and Bloomberg

Chart 12
Foreign Exchange Markets



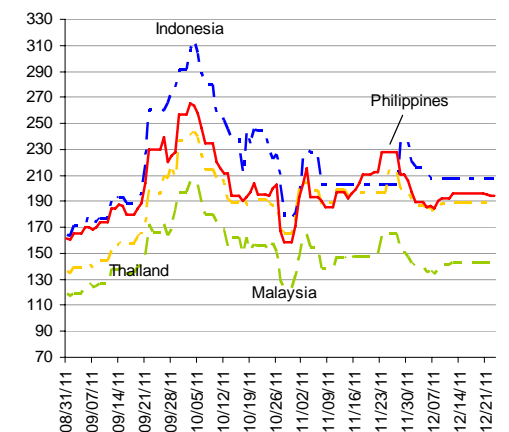
Source: BBVA Research and Bloomberg

Chart 13
Credit Default Swaps



Source: BBVA Research and Bloomberg

Chart 14
Credit Default Swaps



Source: BBVA Research and Bloomberg

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