

ASEAN Macro View

Chartbook: Between the Good, Bad and Ugly

- **Negative surprises in “bad” CA economies and vice versa** — Growth in ASEAN-5 surprised negatively in 2Q13 at 5.0% (1Q13: 5.2%), led by ID, TH and MY – which have all seen sizeable CA deterioration. Conversely, we saw upside surprises in the “good” CA surplus economies of SG and PH. Despite uneven sequential growth, we see a modest YoY growth pick-up for ASEAN-5 in 2H13, led by net export improvement in SG, MY and TH even as rising household debt constrains consumption. Investment should remain a growth driver across ASEAN – led by diversion of FDI from CN – including PH from a low base. The exception is ID, where a slowdown is inevitable given liquidity constraints from CA imbalances and possible policy tightening.
- **ID looks the “ugliest” among the “bad”, followed by MY and TH (see [note](#))** — With ID's net external debt status, the IDR adjustment desired by policymakers has been smaller but declining reserve positions will also lead to significantly lower economic growth due to liquidity constraints (even though dramatic rate hikes have been avoided). MY and TH can still afford more FX weakness. Compared to TH, MY's higher speed of CA deterioration argues for greater urgency in bolstering savings via fiscal and macroprudential tightening. Although CA dynamics in TH seem benign, caution against populist fiscal programmes and a debt-fuelled consumption binge is warranted.
- **Spillovers from ID slowdown larger in SG and MY/ TH, but offset by G3 pick-up** — From a trade perspective, SG appears most vulnerable to a slowdown in ID, followed by MY (both in refined oil exports), and TH (transport equipment). On balance, provided the slowdown in ID and CN is modest, the impact via the trade channel on GDP growth should be more than offset by a pick-up in direct and indirect exports to G3, which are 3-12 times larger than exports to CN and ID. SG is also more vulnerable to a slowdown in demand for tourism services from ID, followed by MY and TH.
- **Disinflation has ended but uptick not sufficient to trigger rate hikes (ex ID)** — Inflation should edge up in 2H13 (except in TH on base effects), reflecting [1] lagged impact and second round effects of fuel subsidy cuts in ID and possibly in MY (year end); [2] lagged impact of FX weakness on imported inflation; and [3] lingering wage pressures. Inflation should stay within CB tolerance thresholds, however, implying no urgency to hike, except in ID, where we think 50bps in hikes are warranted.
- **More near term pressure on IDR, MYR and THB; PHP relative weakness overdone** — While this is not 1997, new risks from rising private leverage, portfolio flow volatility, and Fed tapering will continue to dominate broad FX trends (see [note](#)), though intra-ASEAN differentiation identifies where relative value lies. A more hawkish stance by BI is needed to alleviate pressure on IDR on weak external liquidity, CA and growth dynamics. Heavy foreign positioning, weaker CA and external liquidity suggest near term vulnerability for MYR vs THB, while growth vulnerability to a slowdown in ID and CN could potentially chip away SGD's safe haven status. Strong external position and limited growth vulnerability suggest relative weakness in PHP may be overdone.

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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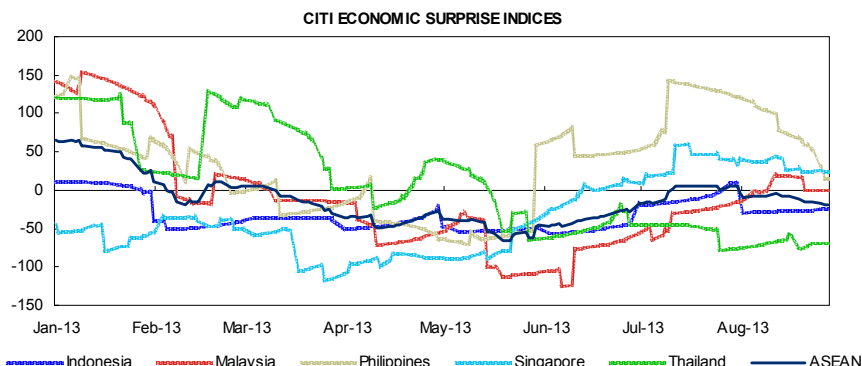
Chartbook: Between the Good, Bad and Ugly

After recent improvements, ASEAN-5 economic surprises are beginning to turn negative again in Aug. However, within ASEAN, recent downside surprises have been dominated by TH and ID. Elsewhere, economic surprises have been positive, led by PH, and to a lesser extent SG, though these are now beginning to narrow as expectations catch up with reality. Monthly MY data has surprised on the upside relative to downcast expectations, though the recent downside surprise in 2Q GDP has brought the ESI back to neutral levels.

Domestic demand led the 2Q growth slowdown in ID and TH, with net export drag providing the tipping point into technical recession in TH. While domestic demand also slowed modestly in MY, this was more than offset by a slightly smaller drag in net exports. For SG, a turnaround in net exports was the key driver behind the 2Q GDP upside surprise. For PH, 2Q YoY growth was kept steady by a smaller net export drag, even as private consumption and investments moderated (the latter from elevated levels)

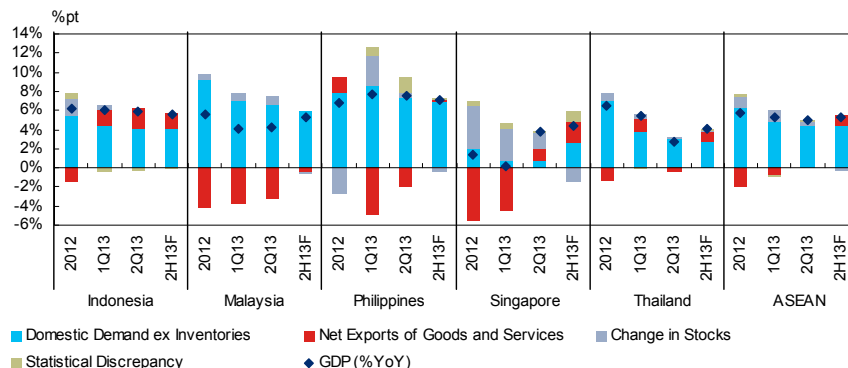
In sequential terms, except for ID and PH almost all ASEAN economies saw better sequential growth in 2Q13, with SG outperforming. Even TH, which slipped into technical recession, saw a smaller rate of contraction – a first sign of a growth bottom. Sequential growth profiles will remain uneven across ASEAN in 2H13. An anticipated 2H13 pick up in TH and MY hinges partly on a bottoming of exports and some pick up in fixed investment spending. In PH, SG and ID, some pullback is expected in 3Q, before a rebound in 4Q. For ID, the slowdown reflects tighter financial conditions and drag from IDR weakness on import dependent sectors, before pre-election spending takes up some of the slack in 4Q.

Figure 1. Citi Economic Surprise Indices



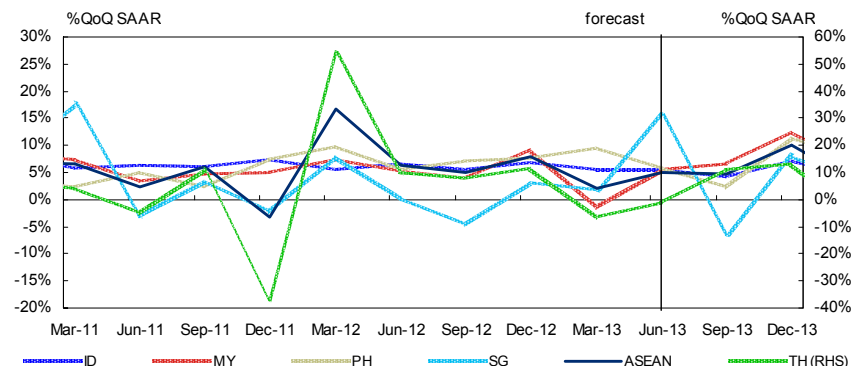
Source: Bloomberg, Citi Research

Figure 2. Contributions to YoY GDP growth



Source: CEIC, Haver, Citi Research Estimates

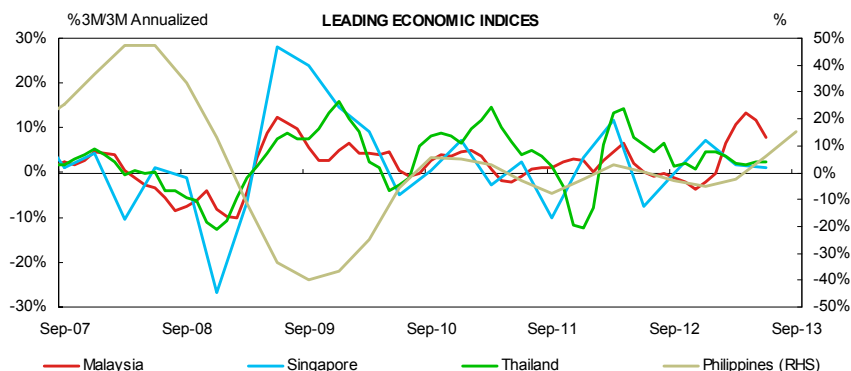
Figure 3. Sequential GDP growth %QoQ SAAR



Source: CEIC, Haver, Citi Research Estimates

Available national leading indicators, suggest stronger near term pick-ups in MY and PH, while momentum is likely to stay lackluster in SG and TH near term.

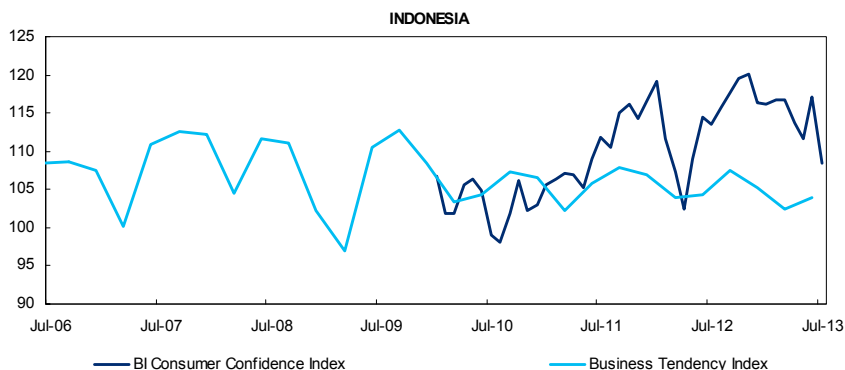
Figure 4. Leading Economic Indices and Indicators



Source: CEIC, Citi Research

Both consumer and business confidence remain weak in ID, reflecting the hit to discretionary incomes from the fuel price hike in late Jun and the tightening of liquidity and financial conditions as a result of worsening external imbalances.

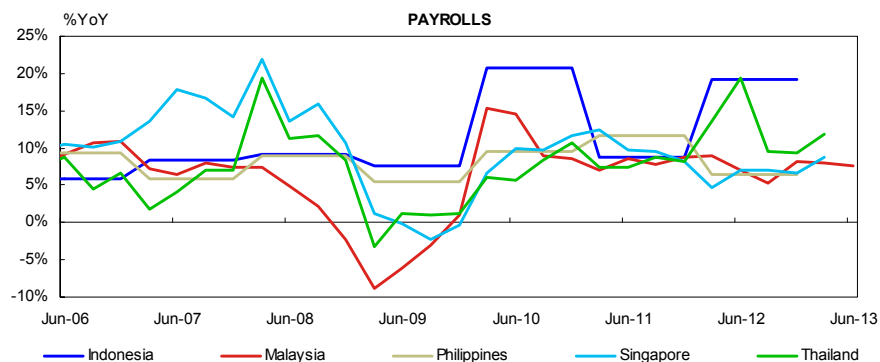
Figure 5. Indonesia Consumer and Business Tendency Indices



Source: CEIC, Citi Research

For now, still buoyant employment and wages underpinning robust growth in overall labour incomes should place a floor on consumption growth...

Figure 6. Labour Incomes

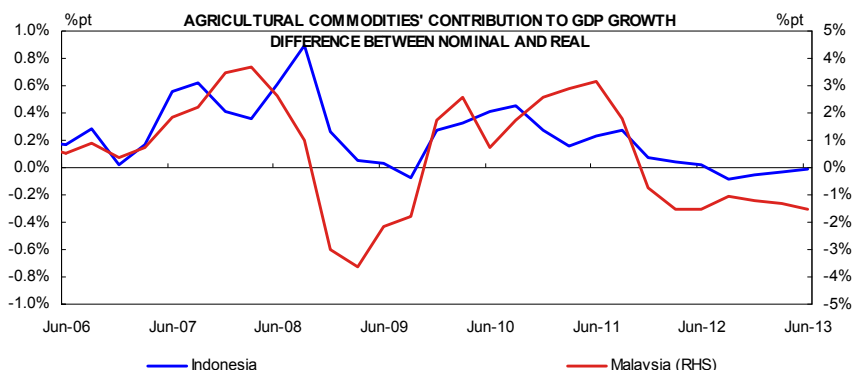


Note: Indonesia and Philippines on annual basis. We estimate payrolls as the product of average wages and employment.

Source: CEIC, Haver, Citi Research

...but softening agricultural commodity prices have hurt rural incomes and nominal GDP growth in MY and ID. In MY for example, nominal GDP growth – a proxy for overall income growth in the economy – would have been 1.5%-pts stronger in 2Q13 were it not for the fall in palm oil and rubber prices.

Figure 7. Agricultural Commodities' Contribution to GDP Growth – Difference between Nominal and Real

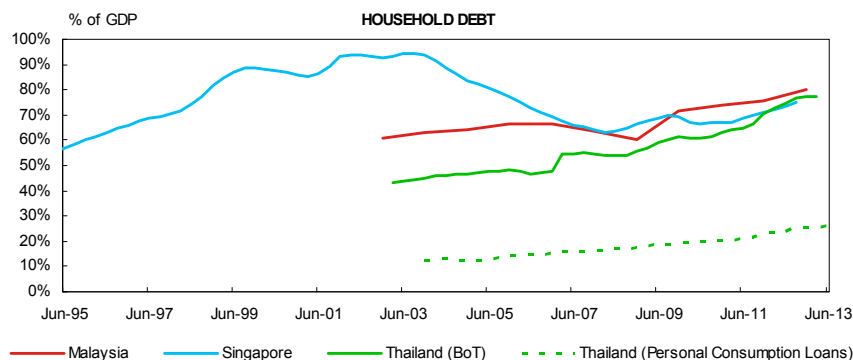


Note: We use non-food crops for Indonesia and rubber and oil palm for Malaysia. We first calculate the contribution to YoY headline GDP growth in both nominal and real terms and then take the difference between the two. A more negative gap indicates that GDP growth would have been higher were it not for lower prices.

Source: CEIC, Citi Research

Rising household debt to GDP ratios in MY, SG and TH could be a potential constraint on consumption growth going forward, given the likely rise in debt service ratios. Broader estimates of HH leverage in TH based on BOT's broader definition (which includes 'business loans' to individuals and lending from non-bank lenders) could yield a figure as high as 77% of GDP, up from 55% of GDP in 2007.

Figure 8. Household Debt

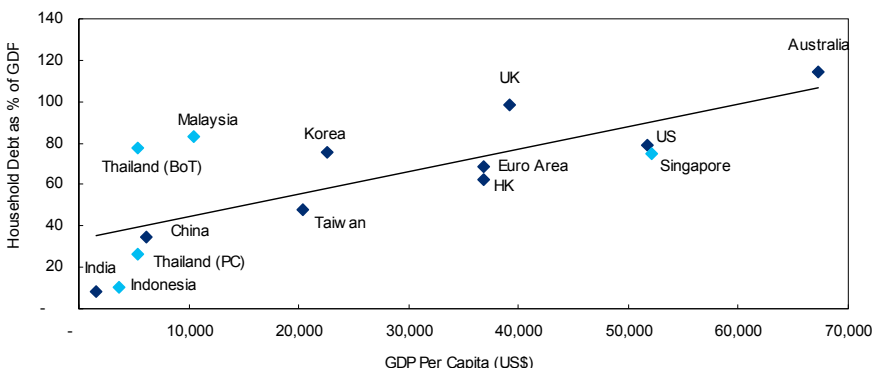


Source: CEIC, Haver, BoT, Citi Research

HH debt issue is more acute in MY and TH, where the stock of HH debt is large relative to per capita incomes, in turn suggesting higher debt service burdens relative to household incomes, especially if interest rates rise. Debt service ratios in MY for example are as high as 43% of gross income. In mitigation, our TH banks analyst Kritapas Siripassorn argues that TH HH debt would be 20-30% lower if only looking at purely consumption related HH debt, i.e. excluding business loans (see [Thailand Banks – Household Debt: Not as Bad as Feared](#)). We see two way constraints on policy rate action – while rate cuts could spur a further increase in the *flow* of new borrowers, the large *stock* of existing borrowers places limits on rate hikes, which could slow growth excessively.

Except for SG, fixed investment growth continued to soften noticeably through 2Q in most of ASEAN, largely reflecting a slowdown in machinery and equipment investments in most countries even as construction activities held relatively steady. We think the continued slowdown in equipment investment is more a function of weak external demand dampening manufacturing FDI, though a substantial portion of construction investments may also be related to manufacturing activity, e.g. in MY where investments in “structures” is partly related to O&G. Only in TH have we seen equipment investment dominate the investment figures, reflecting the lagged impact of particularly buoyant FDI approvals in 2012.

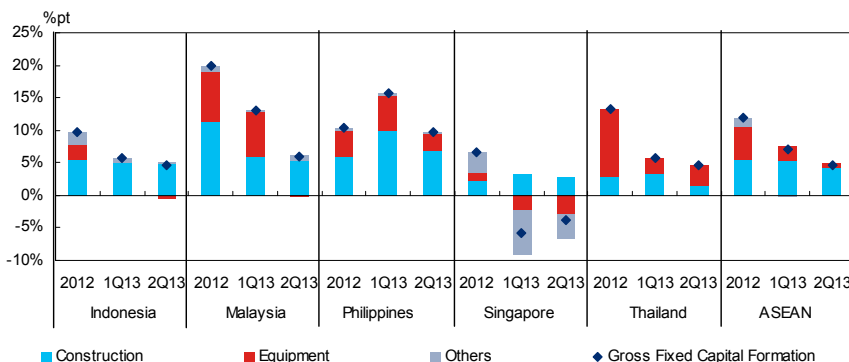
Figure 9. Citi Household Debt Estimates vs GDP per Capita



Note: Thailand (BoT) uses BoT's definition of household debt while Thailand (PC) uses personal consumption loans in Thailand. We proxy household debt with Financial Institutions' Loans to Households for China, Loans to Professional and Private Individuals for HK, Scheduled Commercial Banks' Personal Loans for India, Credit to Households for Korea, and Consumer Loans for Taiwan.

Source: CEIC, Haver, MAS, Citi Research

Figure 10. ASEAN Gross Fixed Capital Formation



Note: As far as possible we try to exclude Transport Equipment from the Equipment category. Included in the Equipment category are Machine and Equipment (excludes Transport) for Indonesia; Machinery and Equipment (includes Transport) for Malaysia; Durable Equipment (includes Transport) for Philippines; Machinery, Equipment and Software (excludes Transport) for Singapore; and Equipment (includes Transport) for Thailand.

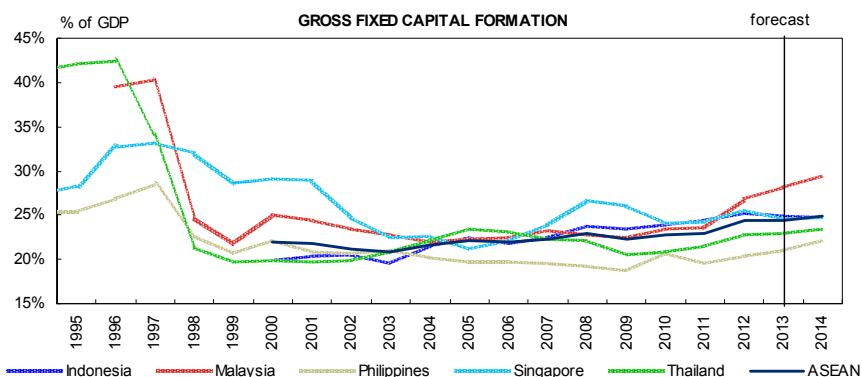
Source: CEIC, Citi Research

Notwithstanding cyclical gyrations, we still expect the investment share of GDP in ASEAN to rise through 2014 in MY, TH and PH, with the sharpest increases in MY and PH – the latter largely a catch up story from a low base facilitated by the “crowding in” from public infrastructure investments, while the former two a mixture of government infrastructure projects and manufacturing/commodities related FDI. In contrast, investment share of GDP is likely to fall in ID, constrained by weaker investments in commodity-related sectors and, more broadly, external imbalances

ASEAN continued to close the FDI gap with China in 2012, as FDI into China saw the first decline in a non-recession year. The gap between China and ASEAN's FDI at US\$9.8bn is now the smallest post GFC and was only smaller in 2006 (US\$8.8bn) and 2007 (-US\$2.1bn when ASEAN FDI temporarily outpaced China's).

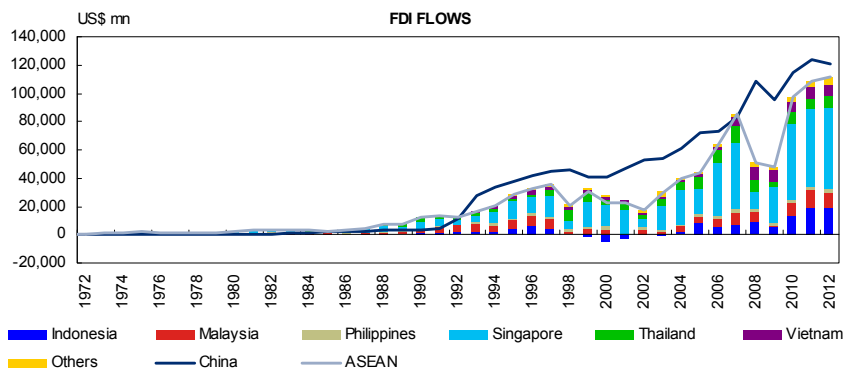
Ex SG, ID remains the largest recipient of FDI in ASEAN, followed by MY. Reflecting infrastructure weaknesses and relative lack of a capital-intensive manufacturing base, PH remains the regional FDI laggard (US\$2.8bn) but interestingly saw the sharpest the YoY rise in ASEAN (US\$981bn or 54%YoY).

Figure 11. Gross Fixed Capital Formation as % of GDP



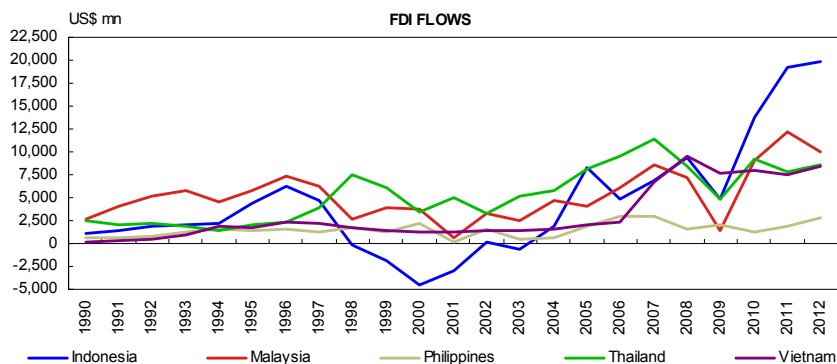
Source: CEIC, Haver, Citi Research Estimates

Figure 12. Foreign Direct Investments



Source: UNCTAD, Citi Research

Figure 13. Foreign Direct Investments – Ex Singapore



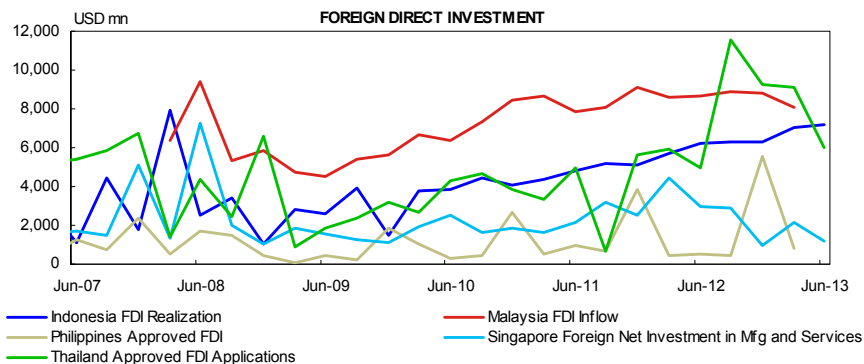
Source: UNCTAD, Citi Research

Into 1H13, FDI realization remained robust particularly in ID (but not sufficient to finance the CA deficit), whilst FDI approvals are coming off a high base in TH as flood-related construction comes to an end. FDI approvals have been relatively choppy in PH, but have been picking up from a low base. In SG, FDI appears slowed as cost competitiveness has been eroded by restructuring measures.

A major factor driving FDI inflows into ASEAN has been Japan. Japan's ODI to ASEAN-4 (ex SG) has overtaken that into China since 2Q13, reflecting ODI diversification away from China in the wake of bilateral tensions and ASEAN's improving cost competitiveness. Interestingly, even FDI into SG, which had previously slowed on cost competitiveness concerns, has now converged with that into China.

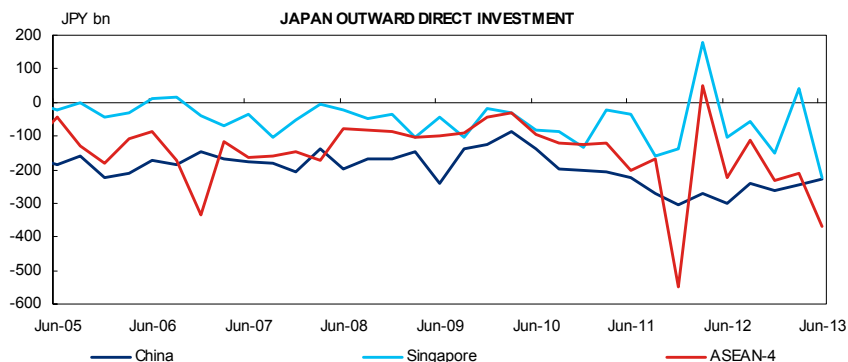
Whilst ASEAN as a whole should still benefit from FDI diversion from China, we see scope for greater intra-ASEAN diversification away from current favorites ID and TH. Surveys by the Japan External Trade Organization suggest that after CN, TH and ID were also seen as having the biggest risks in terms of labour costs, which could portend some ODI diversification into MY and PH.

Figure 14. Foreign Direct Investments Approvals and Realization



Source: CEIC, Haver, Citi Research

Figure 15. Japan Outward Direct Investment by Destination



Note: A larger negative figure indicates a larger flow of direct investments out of Japan

Source: CEIC, Citi Research

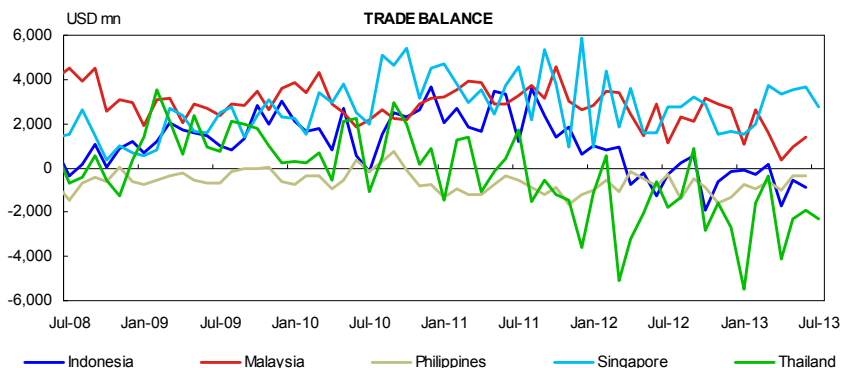
Figure 16. Risks and problems that concern Japanese companies – high or rising labour costs (% of firms currently doing business or considering starting business in country)

	FY2012	FY2010	FY2008
China	49.5	46.2	42
Thailand	30.1	19.8	19
Indonesia	21	4.5	9
Vietnam	18.1	10.5	17
Malaysia	15.9	11.9	14
India	7.9	6.7	11
Philippines	7.3	3.3	4

Source: JETRO

Trade balances in TH, ID and MY have seen particularly sharp deterioration in recent months, but have improved in SG and PH. Even so, we note that trade balances are seeing some sequential improvements in MY and could improve slightly further in 2H13 if exports bottom as we expect.

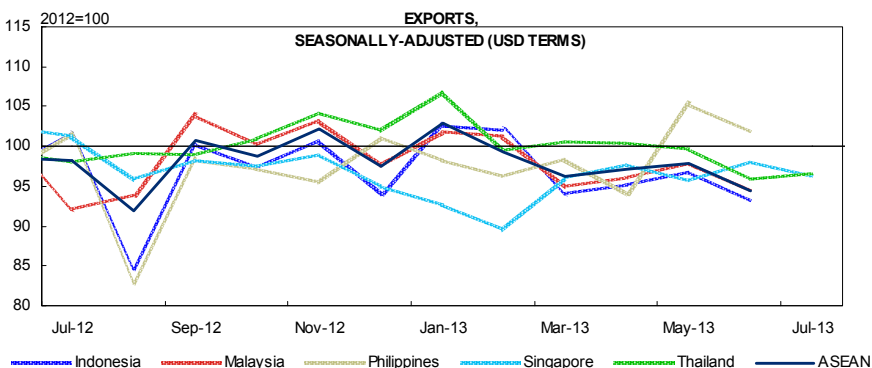
Figure 17. Merchandise Trade Balance



Source: CEIC, Citi Research

Except for PH, export levels in the rest of ASEAN have stabilized into Jun at low levels in sequential terms. Jul data for SG and TH point to a broadly flattish export profile into early 3Q.

Figure 18. Export Levels, Seasonally-Adjusted



Note: We use NODX for Singapore.

Source: CEIC, Citi Research

Tech leading indicators remain mixed, with 4 out of 9 indicators in Jul rising sequentially, vs 5-6 in the preceding 3 months

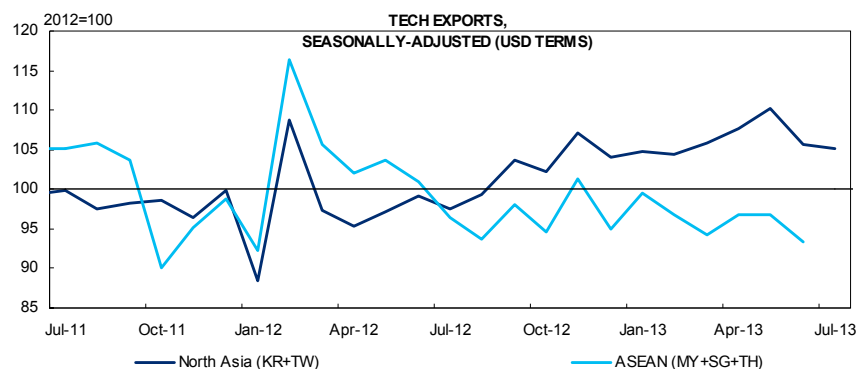
Figure 19. Indicators of Electronics Demand

	US New Orders for Computers and Electronic Products	PPI for Semicon & Related Device Mfg	US Shipment to Inventories Ratio for Computers and Electronic Products	US ISM Mfg PMI	US NASDAQ	US Semicon Book-to-Bill Ratio	Taiwan Electronics Products Export Orders	Taiwan Information and Communication Products Export Orders	Singapore Electronics New Export Orders PMI	Number of Categories Rising Sequentially
	USD mn, SA	Dec-98=100			2/5/71=100		2006=100, SA	2006=100, SA		
Jan-13	20,910	39.2	0.604	53.1	3,142.13	1.11	106.9	109.4	50.4	5
Feb-13	20,716	39.1	0.598	54.2	3,160.19	1.10	100.1	103.1	53.2	3
Mar-13	20,595	38.8	0.620	51.3	3,267.52	1.11	100.1	95.7	52.5	3
Apr-13	21,541	40.2	0.598	50.7	3,328.79	1.08	101.7	102.8	53.1	6
May-13	22,236	40.5	0.585	49.0	3,455.91	1.08	101.5	103.1	53.3	5
Jun-13	22,063	40.5	0.588	50.9	3,403.25	1.10	103.8	103.3	51.7	5
Jul-13	21,262	39.6	0.571	55.4	3,626.37	1.00	104.2	103.7	51.3	4

Source: Haver, CEIC, Citi Research

Tech exports in ASEAN continue to underperform North Asia...

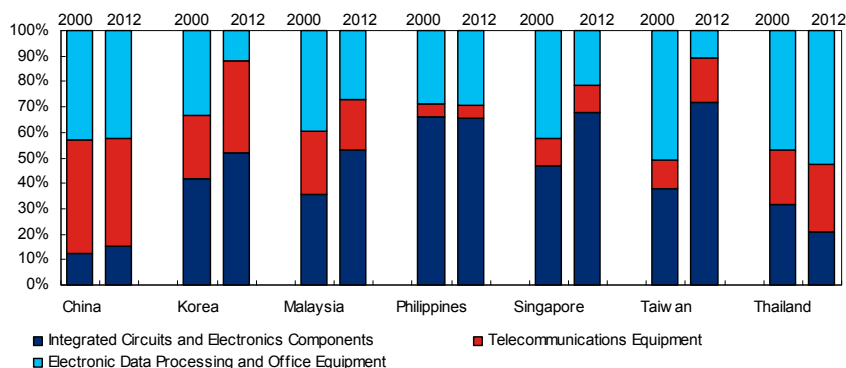
Figure 20. Tech Export Levels, Seasonally-Adjusted



Source: CEIC, Citi Research

...partly reflecting exposure to PC-related final demand in ASEAN tech exports vs KR and TW.

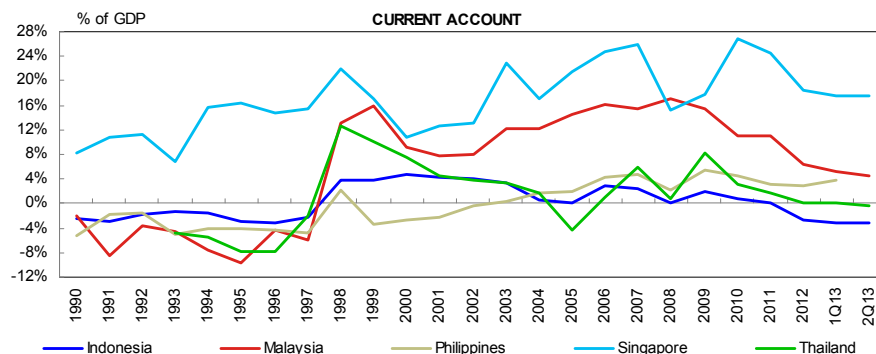
Figure 21. Composition of Tech Exports



Source: WTO, Citi Research

While current account balances have been deteriorating amongst the ASEAN-5, only ID's has reached 1997 levels. Even so, the 1997 Asian Financial Crisis was preceded by years of persistent CA deficits in the ASEAN-4 (ex SG) – which is far from the case at present. For example, MY and TH saw CA deficits averaging around 6.4% and 5.6% of GDP in respectively from 1993-1997 vs surpluses of 7.3% and 0.5% from 2011-1H13. In other words, while recent trends are valid source of concern, imbalances can still be corrected if policy remedies are undertaken early.

Figure 22. Current Account



Note: Data is annual except for 1Q13 and 2Q13 where we use 4-quarter rolling sums.

Source: CEIC, Haver, Citi Research

Liquidity buffers are generally stronger relative to pre-1997 levels. Ex ID, ASEAN-4 reserves remain several times above external financing requirements (ST external debt + amortizations). Even in ID, FX reserve coverage ratios remain above 1997 levels, even after taking into account the wider CA deficit.

Unlike the rest, MY's official definition of short term external debt does not include foreign holdings of short term bills or non-resident deposits of <1 yr maturity. Including these would result in significantly lower FX coverage ratios, though direct comparisons with 1995-97 are difficult given data limitations.

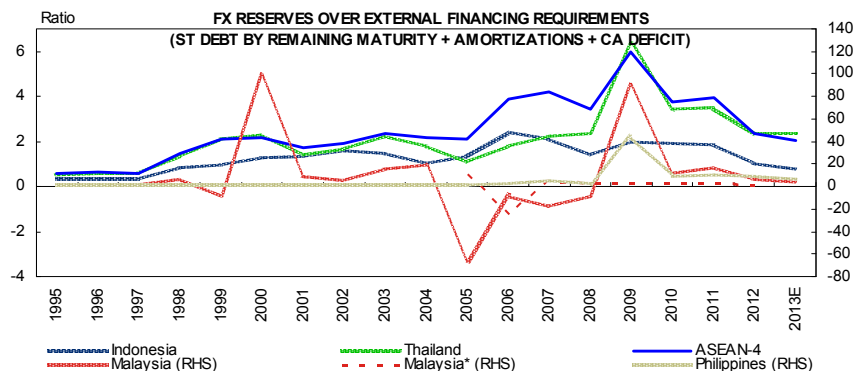
A CA deterioration is less worrying if it finances new investments that generates future earnings rather than consumption, which reduces savings.

In addition to a rise in investments, a sizeable fall in the national savings rate since 2011 has also played an important role in ID and especially MY. This reflects both the fall in commodity prices (especially for ID), sustained larger public sector deficits (especially in MY) and a likely fall off in private savings from debt driven consumption binge (in MY).

A CA deficit would be less worrying if driven by investments in tradables sectors that would ultimately generate export earnings in the future. Tradables sectors appear to play a more important role in MY and especially TH, but investments in ID have been concentrated in non-tradable building/construction activity.

That said, 70% of "building" investments in ID comprises civil infrastructure, including roads, ports and "special construction", e.g. telecom towers and power plans, which could indirectly lift the productivity of the tradables sectors.

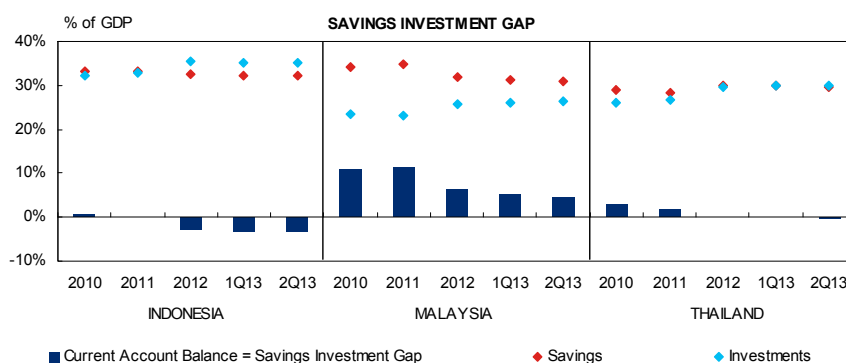
Figure 23. Reserves over Financing Requirements (ST Debt + Amortization + CA Deficit)



Note: We adjust the Malaysia* series by including foreign holdings of short term bills and non-resident deposits of <1 year maturity.

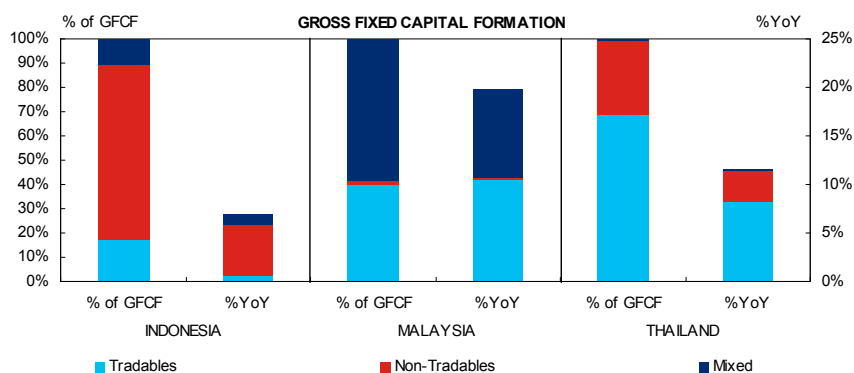
Source: CEIC, Haver, Citi Research Estimates

Figure 24. Savings-Investment Gap: Indonesia, Malaysia and Thailand



Note: We calculate the savings rate implied by investments and current account balances. Data is quarterly on a 4-quarter rolling sum basis. Source: Source: CEIC, Citi Research Estimates

Figure 25. % of Overall GFCF levels and Growth from Tradables



Note: For Indonesia, we classify GFCF in Machinery and Equipment as Tradables, Building as Non-Tradables, and Transportation and Others as Mixed. For Malaysia, we classify Mining and Manufacturing as Tradables, Construction as Non-Tradables, and Agriculture and Services as Mixed. For Thailand, we classify Manufacturing as Tradables; Construction as Non-Tradables; and Business Services, Agriculture, and Mining as Mixed.

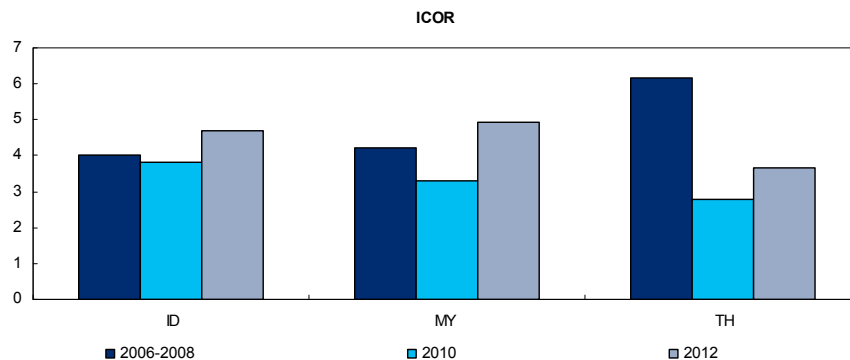
Source: CEIC, Citi Research Estimates

ICOR gives an indication of broad investment efficiency at the macro level, though data limitations mean that this can be a tricky concept to measure or interpret.

Our proxy for ICOR would suggest an increase across all three countries since 2010, but perhaps more so in MY and ID rather than TH. We note some caveats in interpreting the data however. For MY, the rise in ICOR may simply reflect the significant time needed to translate sizeable investments in MRT projects and oil and gas into actual output. In ID, ICOR may be distorted upwards by the shrinking output of the oil industry which has actually seen limited investments.

An alternative measure of investment efficiency is the Return on Invested Capital (ROIC) measure for listed companies. ID has seen the highest ROIC, though this has been declining since 2011 – corroborating the rise in ICOR. However, ROIC in MY has been rising, while TH has been steady. An important caveat with regard to our ROIC measure is that it only includes large listed companies for which investments may not necessarily be in the home country, e.g. MY listed corporates investing in ID for example.

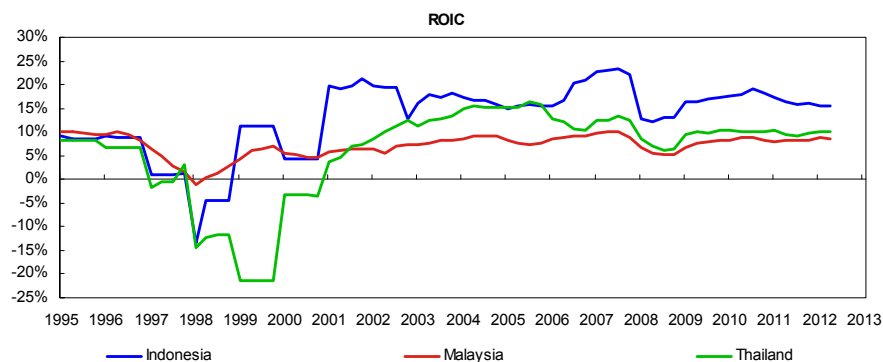
Figure 26. Proxy for ICOR



Note: Given the lack of net capital stock data in ID, we use the real gross (as opposed to net) capital formation as a proxy for the change in capital stock (i.e. ignoring the impact of capital depreciation) for consistency across countries.

Source: CEIC, Citi Research Estimates

Figure 27. Return On Invested Capital



Source: Citi Research Estimates

With its net external debtor status limiting the extent to which it can adjust via a weaker IDR, the brunt of ID's external adjustment will have to be via significantly slower growth. Because MY and TH are both net external creditors, they can afford to let their currencies weaken. MY's larger speed of CA deterioration vs TH – driven to a larger extent by a running down of public and private savings – and higher concentration in the non-tradables sectors would argue for relatively greater urgency in tackling the issue via somewhat slower growth, primarily via measured fiscal tightening in the upcoming Budget on Oct 25th.

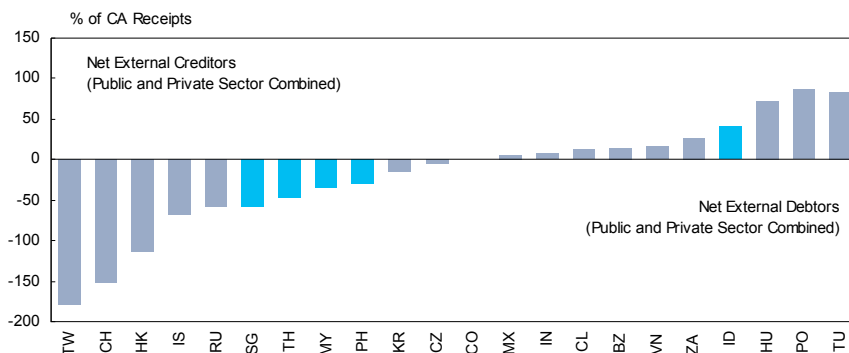
The drain on domestic liquidity from widening current account deficits have been most evident in ID, where the slowdown in the broad money has been most acute since mid 2012. Liquidity drain from the overall BOP deficit in ID are evident in the net foreign asset drag on broad money growth and liquidity constraints have become more binding given that LDR ratios are already near 100%.

These same factors also suggest liquidity constraints are becoming more binding in TH and to a lesser extent MY (where LDR ratios are lower and the slowdown in loan growth may reflect weaker demand rather than liquidity constraints).

While overall LDR ratios in SG are approaching 100%, this is dominated by non-SGD lending to foreign entities (including in ASEAN), with SGD LDR ratios still below 80%. We thus do not see liquidity constraints on domestic SGD loan growth, but the implied currency mismatch on bank balance sheets raises risks to short term interest rates and liquidity should there be a USD liquidity crunch.

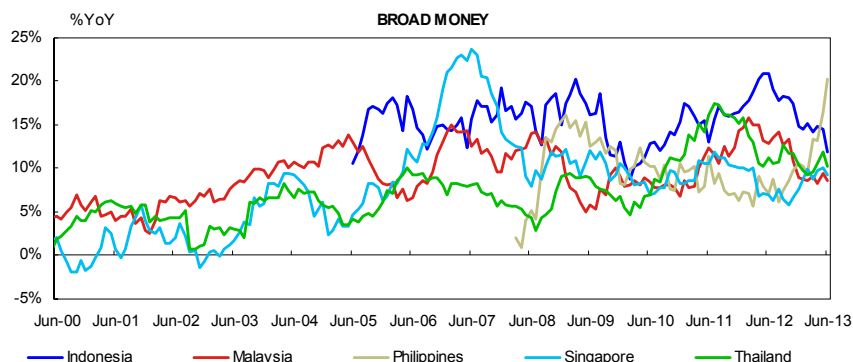
At the other end of the spectrum, buoyant liquidity from CA surpluses (driven by resilient remittances) continue to support broad money growth in PH.

Figure 28. Net External Debt



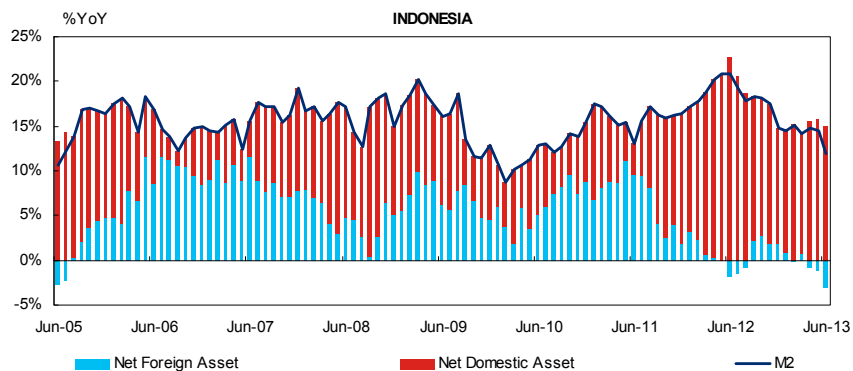
Source: Fitch Data Comparator (March 2013)

Figure 29. Broad Money



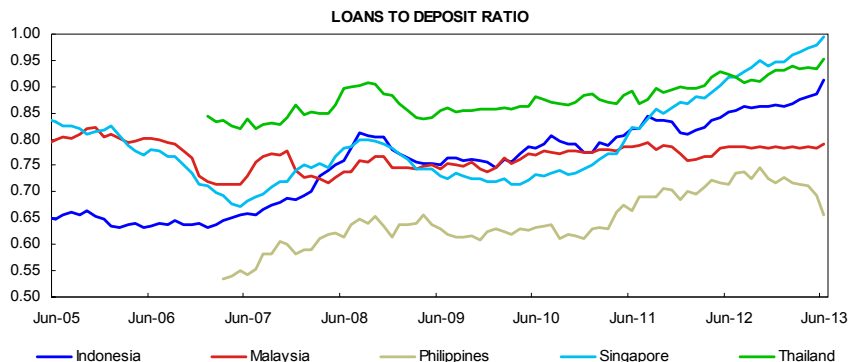
Note: We use M2 for Indonesia; M3 for Malaysia, Philippines, and Singapore; and Broad Money for Thailand.
Source: CEIC, Citi Research

Figure 30. Indonesia Broad Money



Source: CEIC, Citi Research

Figure 31. Loan-to-Deposit Ratio



Source: CEIC, Citi Research

An external imbalance-induced growth slowdown in ID could have second round spillover effects on other ASEAN countries, including those not facing CA pressures.

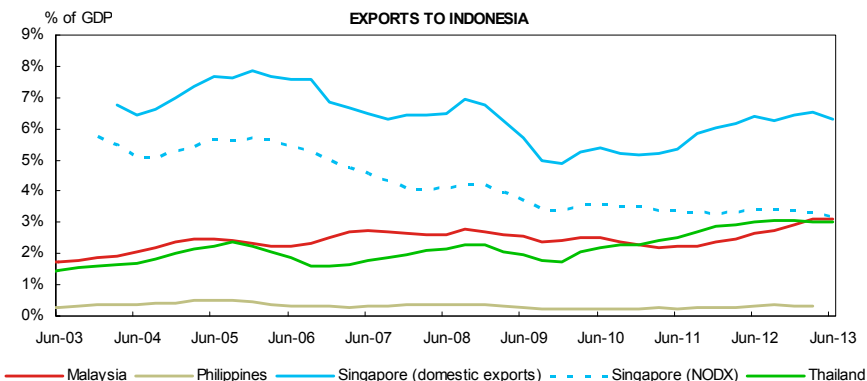
From a trade perspective, SG appears the most vulnerable to a growth slowdown in ID, especially if refined oil exports to ID shrink as a result of subsidy cuts and/or import substitution with biodiesel. This reflects both a large share of exports to ID (7.8% of domestic exports) and a more open economy.

TH's export exposure is almost as large as MY's, while PH appears the most insulated to a trade shock from ID.

TH appears comparatively more exposed to an investment slowdown in ID, as almost half of its exports to ID are in capital goods (largely transport equipment, other machinery and electrical goods).

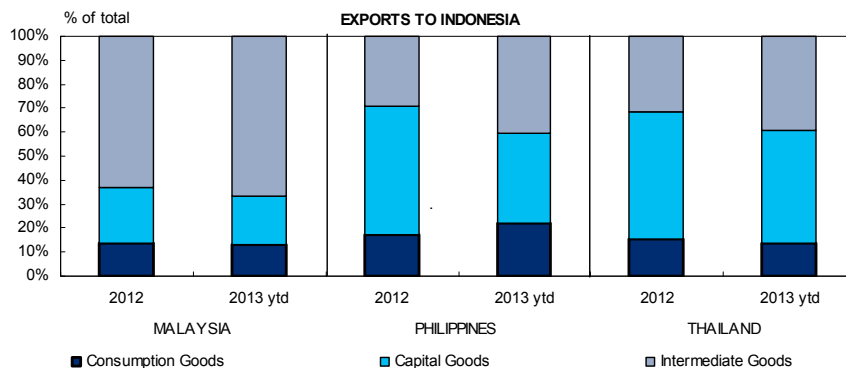
For MY, the impact would be felt largely via a slowdown in intermediate imports used for domestic demand, especially refined petroleum products to ID, particularly as the impact of lower fuel subsidies starts to bite.

Figure 32. Exports to Indonesia



Source: CEIC, Citi Research

Figure 33. Estimated Decomposition of Exports to Indonesia by End Use



Source: CEIC, Citi Research Estimates

Besides via the merchandise trade channel, a slowdown in ID would adversely impact ASEAN economies via the services trade channel, including financial services, transport and tourism flows. Of these, the impact via the tourism channel is easiest to quantify. With ID its largest source of tourists (19% of visitor arrivals), SG appears most vulnerable from this channel (though small at just 0.8% of GDP), followed by MY and TH.

Our prognosis remains that a modest China slowdown should have relatively limited impact on ASEAN exports. The exception is ID, whose commodity exports are heavily exposed to Chinese domestic demand.

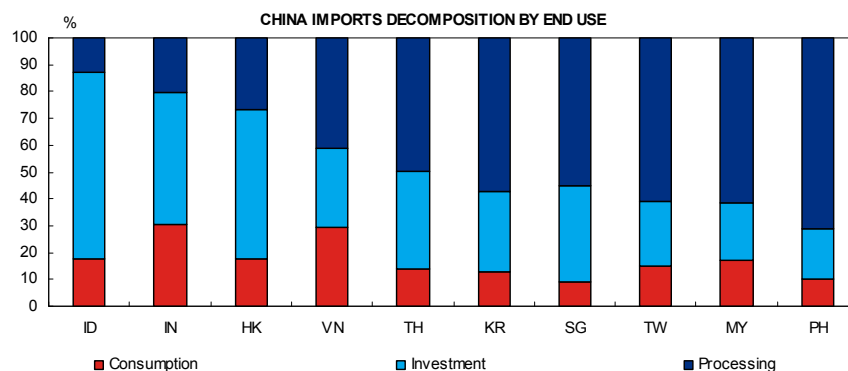
A more recent and granular analysis data from the Japan-based RIETI suggests an even heavier emphasis on intermediate goods exports to CN, especially for SG and MY, where the intermediate goods share is around 70-80% of total exports. Our estimates based on the RIETI estimates suggest that only 31% of ASEAN exports to China are for its domestic demand.

Figure 34. Estimated Real GDP Exposure to Indonesian Tourist Spending



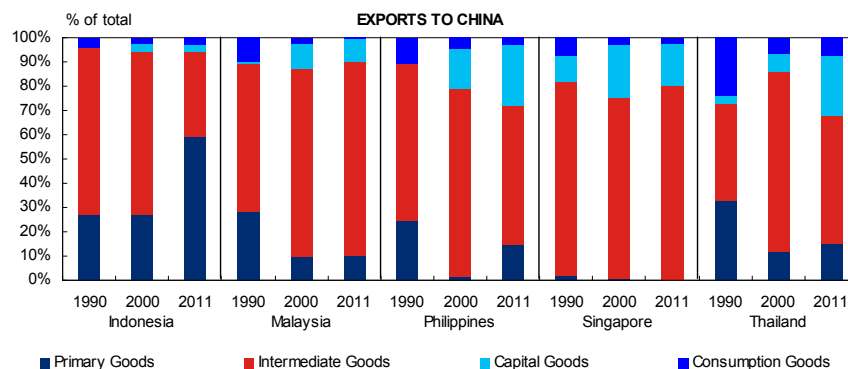
Note: We estimate nominal Indonesian tourist spending and deflate to constant prices to obtain real GDP exposure.
Source: CEIC, Citi Research Estimates

Figure 35. CN's Imports from Asia by End Use (Citi Estimates)



Source: CEIC, Citi Research Estimates

Figure 36. Exports to CN by end use (RIETI Estimates)



Source: RIETI (<http://www.rieti.go.jp>), Citi Research

Provided the slowdown in ID and CN is modest, the impact via the trade channel on GDP growth should be more than offset by a pick up in demand from G3, as exports to the G3 (taking into account indirect exports via CN, proxy using intermediate goods exports to CN) are between 2-7 times larger than exports to CN and ID.

Note that SG's large headline exposure to EU final demand as % of GDP masks the fact that around half of NODX to EU is in pharmaceuticals not closely tied to the economic cycle. Stripping out pharma exports to EU, final demand exposure to G3 would be still be twice that of CN and ID combined.

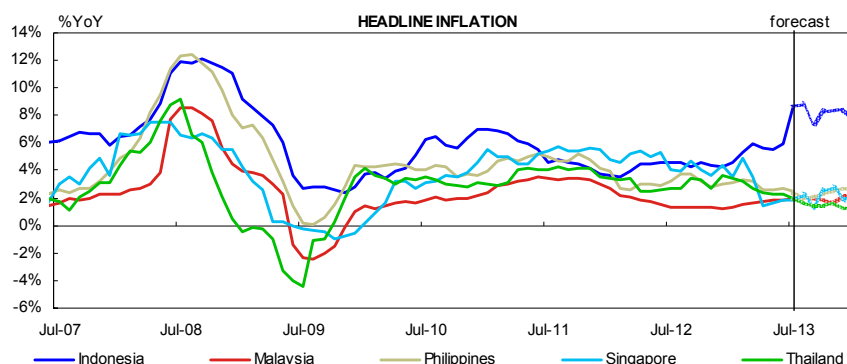
Both headline and core inflation have been on an upward trajectory in ID, MY and SG. Inflation should generally stabilize or edge up in 2H13, except in TH where base effects will continue to dominate. This reflects [1] lagged impact and second round effects of fuel subsidy cuts in ID and possibly MY (at year end); [2] lagged impact of FX weakness on imported inflation; and [3] lingering wage pressures amid structurally tight labour markets, which could be passed on to consumers as stronger growth/closing output gaps in 2H13 raise pricing power.

Figure 37. Overall export exposure of ASEAN countries to ID, CN and G3

% of GDP	ID	MY	PH	SG NODX	SG Exports	TH	ASEAN
Direct Exports to US	1.7	6.3	2.8	4.3	7.6	5.9	3.6
Direct Exports to EU	1.7	6.4	2.2	6.5	11.8	5.1	3.8
Direct Exports to Japan	3.3	8.4	3.8	3.0	6.2	6.0	4.6
Direct Exports to Indonesia	3.1	0.3	3.2	14.5	3.0		
Direct Exports to China	2.5	9.1	2.2	6.1	15.8	6.8	4.8
Exports to China used for Intermediate goods (% of exports to China)	34.6	80.0	57.3	80.0	80.0	52.2	68.8
Exports to China used for Domestic Demand (% of exports to China)	65.4	20.0	42.7	20.0	20.0	49.9	31.2
Exports to China used for Domestic Demand	1.6	1.8	0.9	1.2	3.1	3.4	1.5
China's Exports to US (% of China's exports)	16.5	16.5	16.5	16.5	16.5	16.5	16.5
Indirect Exports to US via China	0.1	1.2	0.2	0.8	2.1	0.6	0.5
Total Direct and Indirect Exports to US	1.8	7.5	3.0	5.1	9.6	6.4	4.2
China's Exports to EU (% of China's exports)	15.3	15.3	15.3	15.3	15.3	15.3	15.3
Indirect Exports to EU via China	0.1	1.1	0.2	0.7	1.9	0.5	0.5
Total Direct and Indirect Exports to EU	1.8	7.5	2.4	7.2	13.7	5.6	4.3
China's Exports to Japan (% of China's exports)	6.9	6.9	6.9	6.9	6.9	6.9	6.9
Indirect Exports to Japan via China	0.1	0.5	0.1	0.3	0.9	0.2	0.2
Total Direct and Indirect Exports to Japan	3.3	8.9	3.9	3.3	7.1	6.2	4.8
Total Direct and Indirect Exports to G3	6.9	23.8	9.3	15.7	30.4	18.3	13.3
Exports to ID and China for Domestic Dd	4.9	1.3	4.4	17.6	6.4		

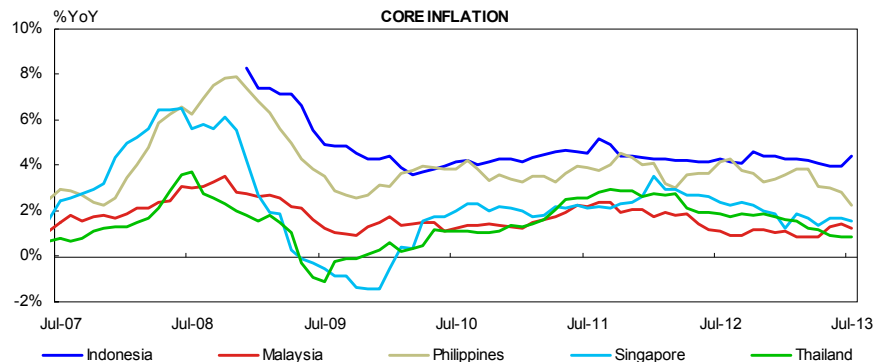
Source: RIETI, CEIC, Citi Research

Figure 38. Headline Inflation and Citi Forecasts



Source: CEIC, Haver, Citi Research estimates

Figure 39. Core Inflation

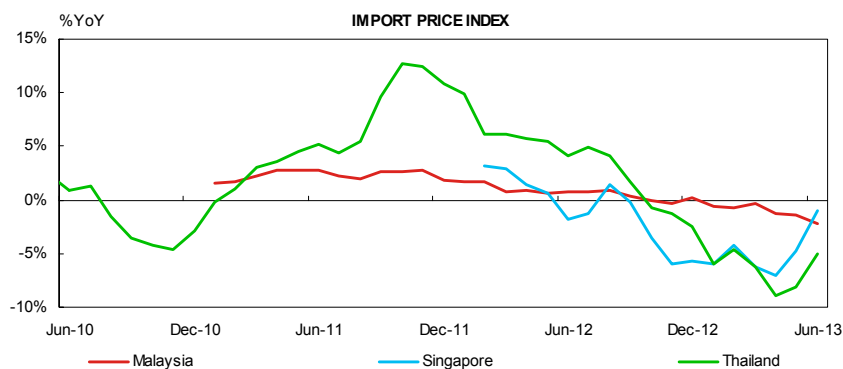


Note: We use CPI ex food and transport for Malaysia

Source: CEIC, Haver, Citi Research

FX weakness since Jun has limited disinflationary impact of lower commodity prices on import prices. Indeed, import prices in SG and TH appear to have bottomed, though being a commodity exporter, import prices in MY have yet to feel the impact of MYR weakness. In ID, our regression estimates suggest that every 1ppt IDR/USD depreciation raises headline inflation by 0.1ppt.

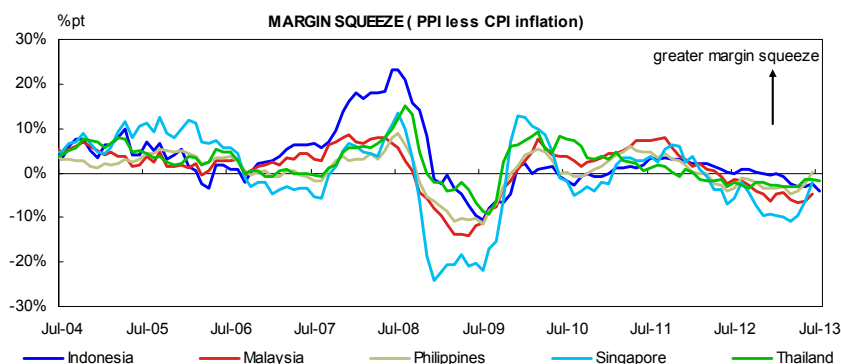
Figure 40. Import Price Inflation



Source: CEIC, Citi Research

While cost pressures corporate profit margins have been benign so far, evident by the widening negative spread between PPI and CPI inflation, they appear to be intensifying, especially in SG and to a lesser extent TH and PH.

Figure 41. Margin Squeeze

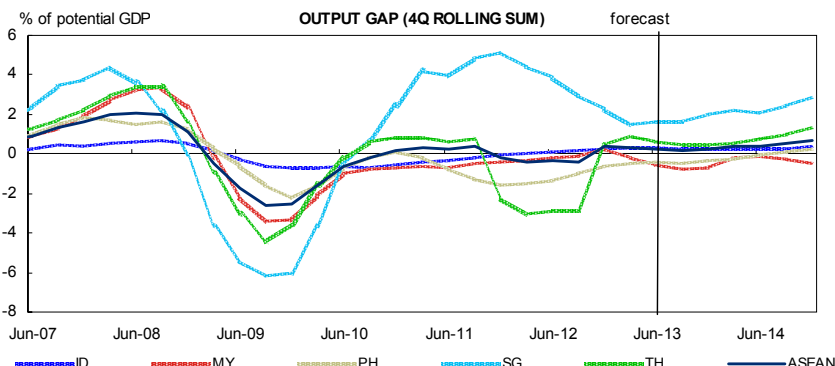


Note: We estimate margin squeeze by taking the differential between producer and consumer price inflation (YoY terms). We use the wholesale price indices for Indonesia and Philippines and the domestic supply price index for Singapore in lieu of producer price indices.

Source: Haver, Citi Research

The trajectory of output gaps – with stable and positive output gaps in SG and TH, narrowing positive output gaps in ID and negative output gaps in MY and PH – are not expected to intensify demand pull pressures soon, though such pressures will likely intensify into 2014 as negative output gaps turn positive and positive output gaps widen.

Figure 42. Output Gap



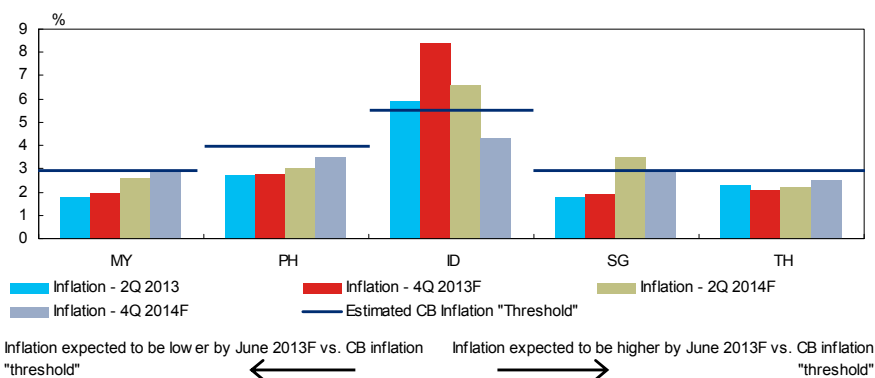
Note: We assume potential growth of 5.5% for Malaysia and 6.5% for Philippines starting 2013 and 3.5% for Singapore starting 2011.

Source: CEIC, Citi Research

Overall, inflation should stay within central bank tolerance thresholds, implying less urgency to tighten. The exception is ID, where the fuel price hike is expected to bring headline inflation >8% by year end, significantly above BI's target of 4.5-5.5%. Thus we think BI needs to hike 50bps and signal a more hawkish stance to restore confidence in the currency.

SG's headline inflation could breach the MAS's implicit tolerance threshold of around 3% in early 2014 on base effects, but unless accompanied by a concurrent pick up in core inflation, we don't see MAS tightening on its FX policy for now.

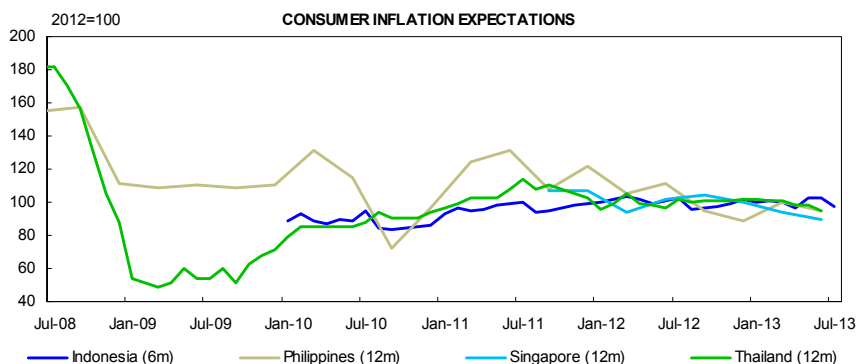
Figure 43. Inflation Forecasts vs Central Bank Thresholds



Source: Citi Research

Inflation expectations have been relatively well behaved, with notable declines observed in SG and PH. Despite the fuel price hike, inflation expectations in ID appear to be stabilizing.

Figure 44. Consumer Price Inflation Expectations



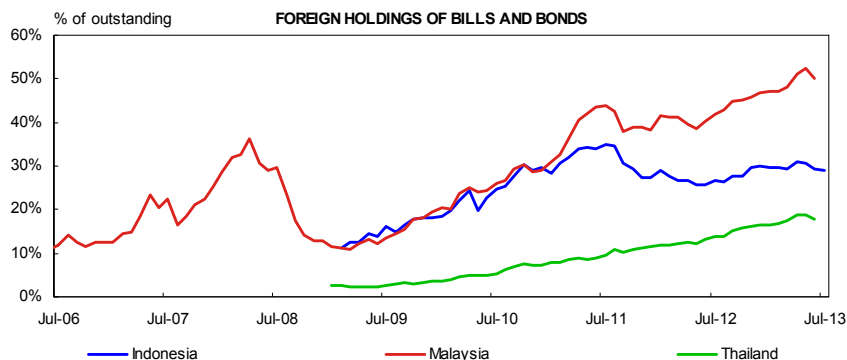
Source: CEIC, BSP, SMU-Mastercard, Citi Research

Despite sell-offs since late May, Jun/Jul data indicates foreign ownership of bills and bonds remains high in ASEAN, especially in ID and MY (MY: 50.2% in Jun, 52.4% in May; ID: 29.1% in Jul, 29.3% in Jun; TH: 17.9% in Jun, 18.9% in May). During the last major sell-off in 2011, most of the unwinding in MY came from short-term central bank and government bills – for bonds, only ID saw a large decline from around Jul/Aug 2011 till mid 2012, while MY never actually saw a decline in foreign ownership of MGS.

In 2011, total unwinding of foreign ownership of bonds and bills in the ASEAN 3 countries amounted to US\$19.8bn between Sep-2011 and Dec-2011, of which around US\$10.9bn came from ID, and the balance largely from MY. Looking at bonds alone, foreign ownership in ASEAN-3 fell by \$7.7bn between Sep 11 and Dec 11, of which two thirds came from ID. The bulk of the unwinding in ASEAN-3 therefore came from bills, which actually peaked earlier in May 2011 at \$34.4bn, and more than halved to \$15.5bn by Nov 2011 – \$18.9bn of unwinds in total in six months.

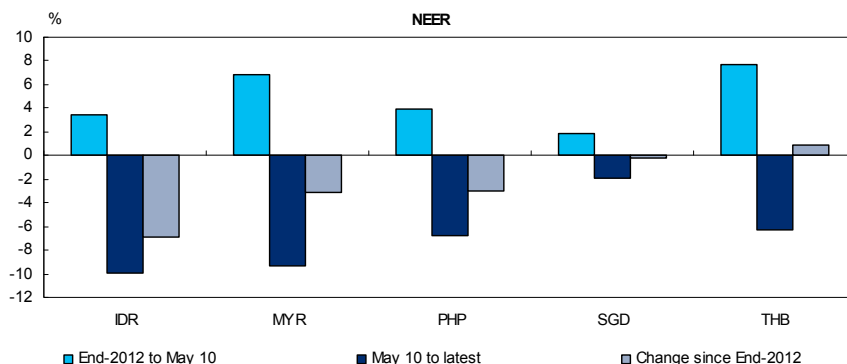
ASEAN-5 currencies have depreciated by between 2.0-9.9% on a NEER basis since 10 May. Except for THB, ASEAN currencies have more than given up all of their gains earlier in the year. IDR and MYR have not surprisingly been the worst performers given positioning and CA dynamics, though these have yet to fully run their course. The sell-off in PHP has been severe relative to fundamentals and conversely THB seems unusually resilient.

Figure 45. Foreign Holdings of Bills and Bonds



Source: CEIC, Citi Research

Figure 46. NEER Performance



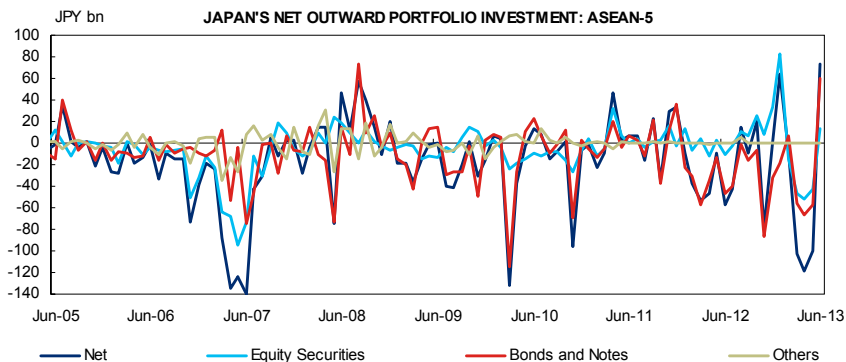
Source: Haver, Citi Research

Surge in both bond and equity portfolio outflows from Japan to the ASEAN-5 post BOJ Bazooka in late Mar/Apr had reversed by Jun, with an unprecedented magnitude of sell off in bonds.

On the equity front, TH and ID saw the greatest selling by Japanese portfolio investors in Jun, although MY has hardly seen outflows and SG continued to receive inflows even through Jun, reflecting its safe haven status

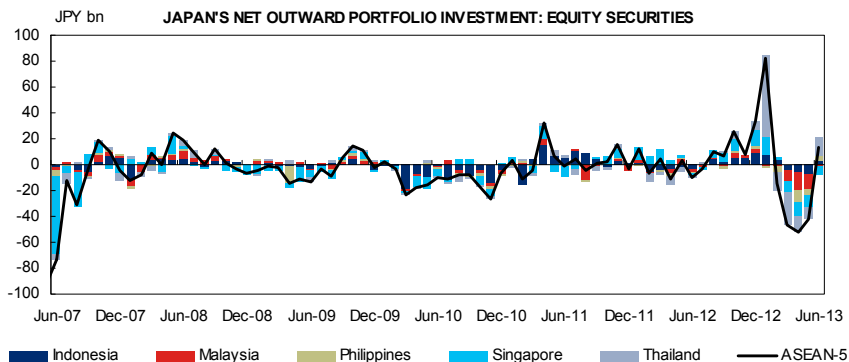
On the bond side, the largest sell-off was seen in MY, which also received the largest inflows in preceding months (at unfavourable levels). SG, another low yielder, also saw large sell-offs, though interestingly ID continued to receive net inflows through Jun – which may suggest further vulnerability to selling pressure going forward.

Figure 47. Japan's Net Outward Portfolio Investment: ASEAN-5



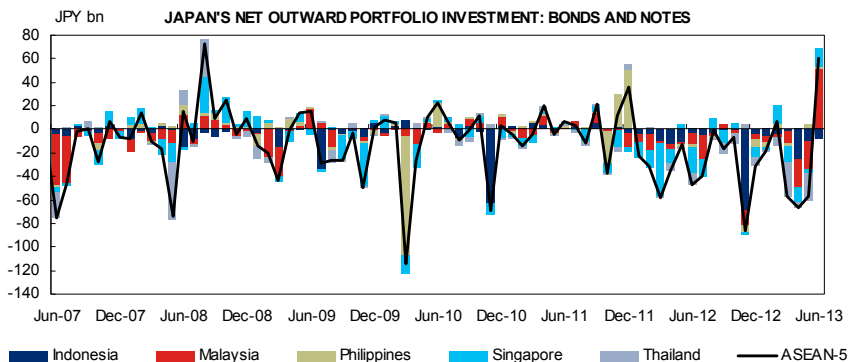
Source: CEIC, Citi Research

Figure 48. Japan's Net Outward Portfolio Investment: Equity Securities



Source: CEIC, Citi Research

Figure 49. Japan's Net Outward Portfolio Investment: Bonds and Notes



Source: CEIC, Citi Research

Ranking ASEAN currencies according to various vulnerability criteria, a more hawkish BI stance may be necessary to arrest pressure on IDR on weak external liquidity, CA and growth dynamics. Heavy foreign positioning, weaker CA dynamics and external liquidity should imply more near term vulnerability for MYR vs THB, while growth vulnerability to a slowdown in ID and CN could potentially weigh on SGD's safe haven status. Limited foreign positioning, a healthy CA surplus and limited growth vulnerability to ID or CN, the sell-off in PHP looks overdone in our view.

Figure 50. FX Vulnerability Ranking

Vulnerability Ranking (higher = more vulnerable)	IDR	MYR	PHP	SGD	THB
Relative gains/losses	2	1	3	4	5
Foreign positioning	4	5	1	3	2
Policy (mis)alignment	5	4	2	1	3
Willingness/ability to adjust via weaker FX	3	5	1	2	4
Growth vulnerability	5	3	1	4	2
FX reserve adequacy	5	4	2	1	3
Total	24	22	10	15	19

Note: We rank the ASEAN currencies by our estimates of vulnerability – the higher the ranking, the more vulnerable the currency on that dimension.

Source: Citi Research Estimates

Appendix A-1

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