Economist Letter

The Emerging Asian Economic Outlook

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Summary

- Overall, the growth rate of emerging Asian economies[1] has slowed down since last year. It seems to have reached a certain level, but we cannot discern a recovery yet. Economic diversity continues in individual countries. The economies of South Korea and Taiwan are sluggish because their export oriented economies have been impacted by the global slump. India, which suffered from high inflation, has also seen a reduction in the growth rate. On the other hand, ASEAN countries have achieved higher growth because of strong domestic demand.
- Financial markets haven't gone through rapid ups and downs, except the Indian market. Nonetheless, strengthening currency is a new concern in South Korea and the Philippines. This is an incentive for their central bank to cut their policy rates. The Indian rupee has been volatile in part due to foreign investor sentiment.
- The Inflation rates in emerging Asian economies are stable except in India. Some central banks have room to cut their policy rate and a few have done so. On the other hand, supply restrictions keep India's inflation rate high.
- South Korea, Taiwan and India, whose economies are sluggish, are expected to recover in the future. However, the pace is very slow and their growth rate is still below their potential growth rate in 2013. Their central banks see this as a chance to adopt a rate-cutting policy.
- Potential crises in foreign economies are a downside risk factor of emerging Asian economies, especially the EU debt problem and the prolonged fiscal cliff in the U.S. However, the possibility of this problem being actualized seems low.

Emerging Asian Economic Outlook

(YoY, %)

GDP Growth rate	2011	2012			2013					2014
		7-9	10-12		1-3	4-6	7-9	10-12		
	A	A	A/F	A/F	F	F	F	F	F	F
South Korea	3.6	1.5	1.5	2.0	2.2	2.6	3.1	3.4	2.8	3.4
Taiwan	4.1	1.0	3.4	1.2	2.9	2.9	2.9	3.2	3.0	3.4
Malaysia	5.1	5.2	6.4	5.6	5.1	5.2	5.3	5.2	5.2	5.5
Thailand	0.1	3.0	18.9	6.4	5.7	3.0	3.5	3.9	4.0	4.5
Indonesia	6.5	6.2	6.1	6.2	6.3	6.3	6.2	6.2	6.3	6.4
Philippines	3.9	7.1	6.8	6.6	5.5	5.4	5.1	5.1	5.3	5.0
India <Fiscal Year>	7.5 <6.5>	5.3	5.6	5.4 <5.6>	5.9	6.1	6.4	6.5	6.2 <6.4>	6.8 <6.9>

Inflation rate	2011	2012			2013					2014
		7-9	10-12		1-3	4-6	7-9	10-12		
	A	A	A	A	F	F	F	F	F	F
South Korea	4.0	1.6	1.7	2.2	1.8	2.2	2.6	2.9	2.4	3.2
Taiwan	1.4	2.9	1.8	1.9	1.4	1.3	0.8	2.1	1.4	2.3
Malaysia	3.2	1.4	1.3	1.7	1.8	2.1	2.5	2.7	2.3	2.7
Thailand	3.8	2.9	3.2	3.0	3.1	3.4	3.6	3.6	3.4	3.2
Indonesia	5.4	4.5	4.4	4.3	4.9	5.2	5.4	5.6	5.3	5.6
Philippines	4.7	3.5	3.0	3.1	3.5	3.8	4.4	4.6	4.1	4.5
India <Fiscal Year>	9.5 <8.8>	7.9	7.3	7.5 <7.3>	6.7	6.7	6.3	6.6	6.6 <6.6>	6.6 <6.4>

* Year on year. Indian GDP is at factor cost. Indian inflation rate is WPI growth rate and others are CPI growth rate.
Sources: CEIC, NLI Research Institute

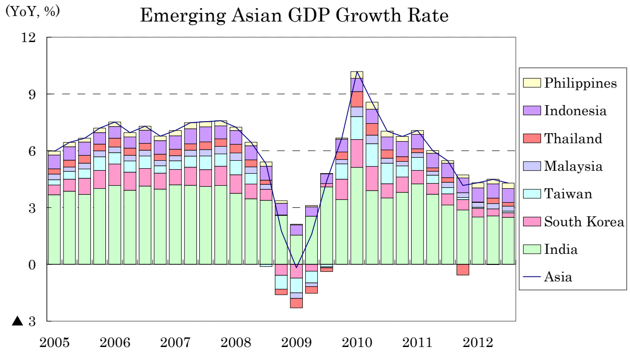
[1] Emerging Asia includes South Korea, Taiwan, Malaysia, Thailand, Indonesia, Philippines and India. China is not covered in this report.

1. Emerging Asia's General Situation

The economies of both the U.S. and the EU are sluggish, and emerging Asian exports to them have shrunk. As a result, the growth rate of emerging Asian economies has been below or near 4.5% since the last half of 2011. It hasn't fallen any further, but remains at a low level (Chart 1).

Roughly speaking, the situation has not changed. Furthermore, South Korea and Taiwan seem to have finally bottomed out.

(Chart 1)



*Potential GDP is estimated by NLI Research Institute.
Sources: CEIC, NLI Research Institute (Quarterly)

Next, we'll comment on the present situation of the overall emerging Asian economy and the short-term outlook.

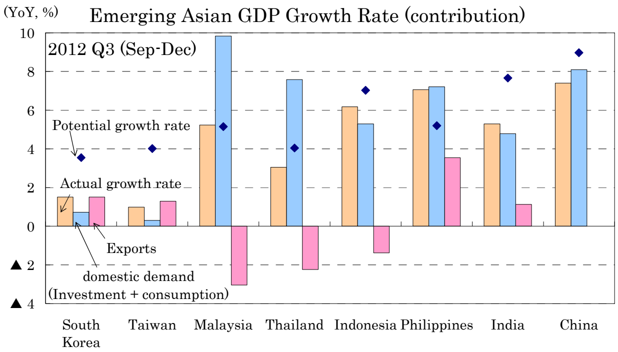
1-1. The Present Situation: Exports Have Bottomed Out, Domestic Demand Diversity Continues

(Real Economy)

First, we examine the growth rate in Q3 (Sep–Dec) 2012 (Chart 2). Weak exports is a feature that stands out among all countries. On the other hand, domestic demand diversity continues. In contrast to ASEAN's high growth rate, South Korea, Taiwan and India have slowed. As a result the latter three countries have growth rates that are much lower than their potential growth rates.

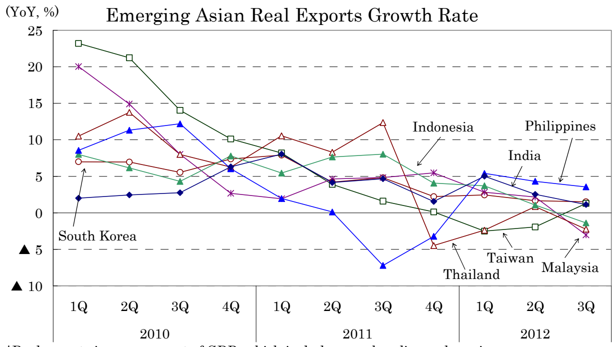
However, there is a sign of a transition. World demand for electronic devices, the main export market of South Korea and Taiwan, is recovering. As a result, their export outlook is improving[2] (Chart 3).

(Chart 2)



*Potential GDP is estimated by NLI Research, China doesn't release exports component.
Sources: CEIC, NLI Research Institute

(Chart 3)



*Real exports is a component of GDP, which includes merchandise and services.
Sources: CEIC (Quarterly)

(Financial Market)

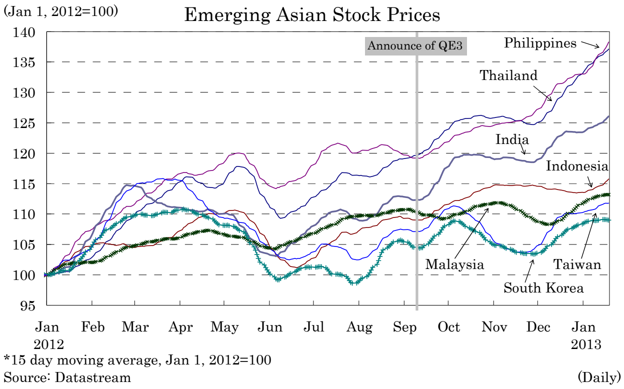
Second, we examine the financial market. The characteristic movement occured after the announcement of QE3 in the U.S. The stock price of emerging Asian economies went up, except for South Korea and Taiwan (Chart 4).

[2] Exports of resource-rich countries such as Malaysia and Indonesia have slowed down. We think the reason is that resource prices have become weak.

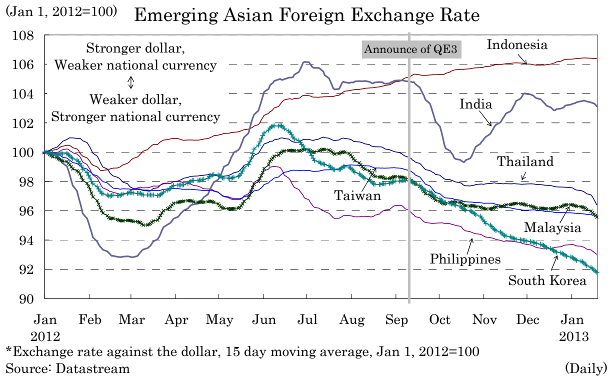
In the foreign exchange market, all currencies except the Indonesian rupiah were strong (Chart 5). In reaction to this, central banks intervened in their own exchange market in order to restrain a strong currency, meaning they bought dollars and increased foreign reserves. During this time, the Indonesian rupiah depreciated consistently where the current account balance is in a deficit. The Indian rupee has been volatile and affected by foreign investor sentiment.

We didn't observe rapid swings in the financial markets except in India; however, strong currencies are a new concern in South Korea and the Philippines. This is an incentive for their central banks to cut their policy rates.

(Chart 4)



(Chart 5)

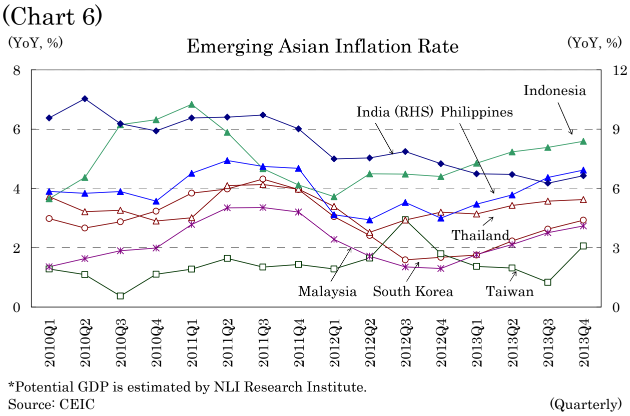


(Inflation)

Inflation rates in emerging Asian economies are stable except in India (Chart 6). Some central banks have room to cut their policy rates. Actually, central banks in South Korea, Thailand, and the Philippines, cut their policy rates (Chart 7). Despite strong growth, BSP (the central bank of the Philippines) cut its policy rate in order to reduce the effect of the sluggish external economic situation and control the appreciation of the Philippine peso.

On the other hand, supply restrictions such as undeveloped infrastructure are causing inflationary pressures in India. Therefore, the RBI (the central bank of India) cannot decide to cut its policy rate aggressively, although the Indian economy slowed down and people expected that the RBI would cut the rate to support the Indian economy.

(Chart 6)



(Chart 7)

Policy Rates in Asian Countries

	2009年	2010年 1-3月	2010年 4-6月	2010年 7-9月	2010年 10-12月	2011年 1-3月	2011年 4-6月	2011年 7-9月	2011年 10-12月	2012年 1-3月	2012年 4-6月	2012年 7-9月	2012年 10-12月	現在 (09年対比)
South Korea (7 days repo rate)	2.00			↑	↑	↑ ↑	↑					↓	↓	2.75 (+0.75)
Taiwan (discount rate)	1.250		↑		↑ ↑		↑	↑						1.88 (+0.625)
Malaysia (ovenight interbank rate)	2.00	↑	↑	↑			↑							3.00 (+1.00)
Thailand (overnight repo rate)	1.25			↑ ↑	↑	↑ ↑	↑ ↑	↑ ↑	↓	↓			↓	2.75 (+1.50)
Indonesia (overnight borrowing rate)	6.50					↑			↓ ↓ ↓	↓				5.75 (▲ 0.75)
Philippines (overnight lending rate)	6.00					↑	↑			↓ ↓		↓	↓	5.50 (▲ 0.50)
India (overnight repo rate)	4.75	↑	↑	↑ ↑ ↑	↑	↑ ↑	↑ ↑ ↑	↑ ↑ ↑	↑		↓ ↓			8.00 (+3.25)
China (1 year base lending rate)	5.31				↑ ↑	↑	↑				↓	↓		6.00 (+0.69)

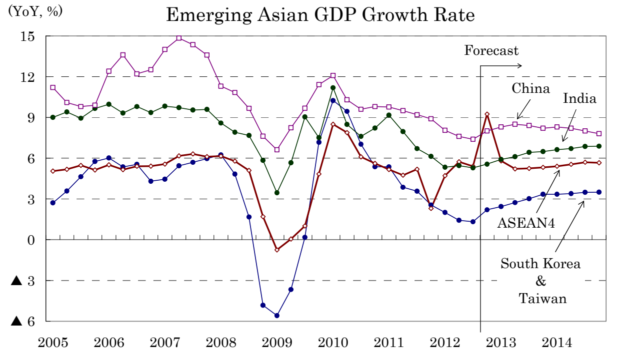
* policy rate or target rate name is in blanket. ↑:raise the policy rate ↓:cut the policy rate.
Resource: CEIC

1-2. Forecast: Improvement

The recently sluggish economies of South Korea and Taiwan are expected to improve, and the RBI will be able to cut its policy rate and support growth, thereby supporting emerging Asian economies as a whole (Chart 8–9). However, the pace of recovery is expected to slow down and be less than its potential growth rate.

Although ASEAN countries will be able to sustain strong growth, Thailand may face downward pressure. This is due to the ending of the surge in consumption and exports which resulted from the restoration of flood damaged areas in 2011.

(Chart 8)

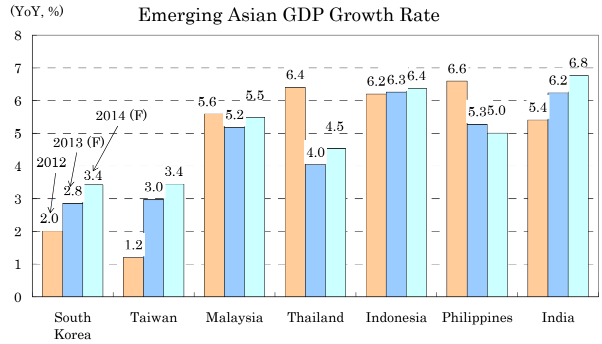


*ASEAN4 is Malaysia, Thailand, Indonesia and Philippines

Sources: CEIC, NLI Research Institute

(Quarterly)

(Chart 9)



*Indian GDP is at factor cost.

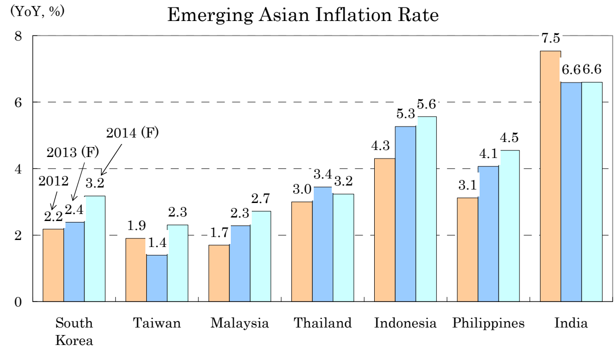
Sources: CEIC, NLI Research Institute

One risk factor is the slowdown of outside economies, for example due to the EU debt problem, the slowdown of the Chinese economy, and the prolonged fiscal cliff in the U.S. If these problems materialize, the exports of emerging Asian economies will shrink and a healthy growth rate will be impeded.

However, to date, there is some progress in the EU, Chinese economic indicators are improving, and some agreement has been reached in the U.S. to avoid the fiscal cliff. Taking these points into account, the possibility of this problem being actualized seems low. Still, we are cautious about repatriation from the emerging Asian market. The above risk factors highlight why foreign investor sentiment holds a risk of repatriation.

Inflationary pressure will not be strong in either South Korea or Taiwan because their recovery pace is slow. Their central banks see this as a justification for cutting their policy rates. On the other hand, inflationary pressure will be strong in ASEAN countries because their economic conditions will get better and wages are going up (Chart 10). Hence, ASEAN central banks, except the BOT (the central bank of Thailand) are taking a wait-and-see approach, or are considering raising their policy rates. Because Thailand's growth will slow after the restoration activity of flood damage subsides, the BOT will take another cut of its policy rate. In India, although the inflation rate will stay at a high

(Chart 10)



*Indian inflation rate is WPI growth rate and others are CPI growth rate.

Sources: CEIC, NLI Research Institute

level, inflationary pressure will weaken slightly. Therefore, the RBI will cut its policy rate just after 2013. Actually, the RBI cut its policy rate by 0.25% in January 2013 and they will cut it in steps during 2013.

The above is an overview of the situation of emerging Asian economies, and of course individual countries have their own problems. Next, we'll examine the present and future situation of each country.

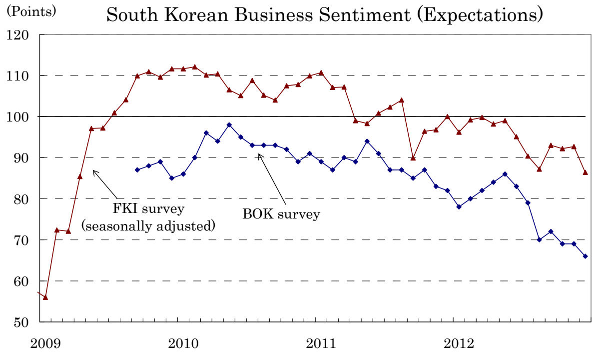
1. Country by Country Analysis

2-1. South Korea

South Korea, which is an export oriented economy, has seen slow economic growth since last year because of slowdowns in major advanced economies, including China. The growth rate in Q3 2012 is lower than the quarter before on a year-on-year basis.[3] Taiwan, which is also an export oriented economy, already began a recovery in Q2 2012, so South Korea's recovery seems to be lagging.

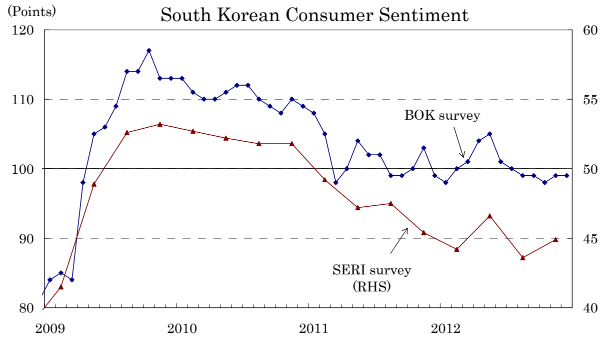
One of the biggest factors of restrained growth seems to be a stronger won. The won has appreciated since May 2012, and exporters expect to sustain serious loses.[4] In fact, South Korea's Business Sentiment Index is moving in a downward direction (Chart 11). Exports improved[5] but a stronger won could bring the pace down.

(Chart 11)



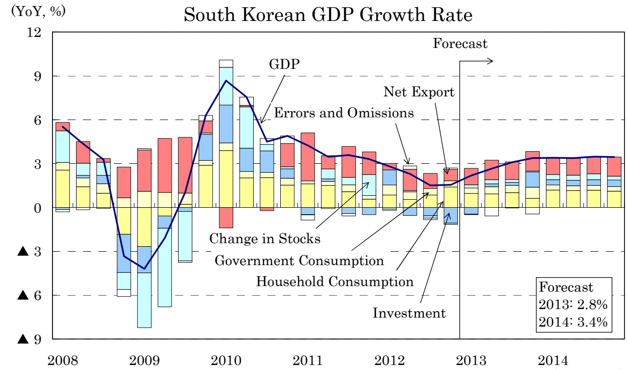
*Above 100 represents optimism. BOK survey started after September 2009.
Source: CEIC (Monthly)

(Chart 12)



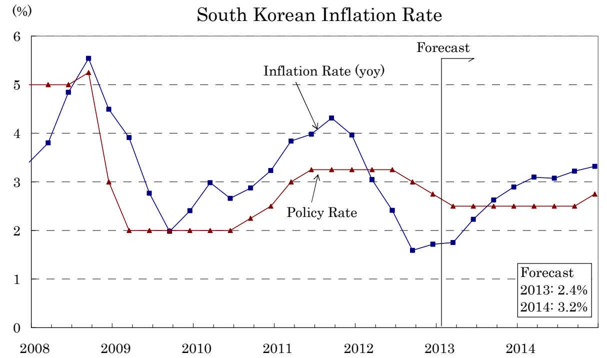
*Above 100 represents optimism in BOK survey and above 50 represents optimism in SERI
Sources: CEIC, SERI (BOK: Monthly, SERI: Quarterly)

(Chart 13)



Sources: CEIC, NLI Research Institute (Quarterly)

(Chart 14)



Sources: CEIC, NLI Research Institute (Quarterly)

In addition, South Korea has some domestic problems, such as a high level of household debt and a new risk of falling housing prices.[6] The government introduced several stimulus measures, such as support for housing loans, easing of loan debts for lower income people in

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[3] The real GDP growth rate of South Korea was 1.5% in 2013 Q3, 2.3% in Q2, and 2.8% in Q1 on a year-on-year basis (0.1%, 0.3%, and 0.9% respectively quarter-on-quarter on a seasonally adjusted basis). This means that the growth rate slowed down as time passed.

[4] The dollar against won rate got close to 1200 won in May 2012, but it is currently over 1060 won. The BOK (the central bank of Korea) seems to have intervened in the foreign exchange market to control their currency. But if the measures are too extreme, criticism to its stance will increase, so it is problematic. Actually, the "Semiannual Report on International Economic and Exchange Rate Policies" which was submitted to the U.S. congress in November 2012, said that the U.S. will "continue to press the Korean authorities to limit their foreign exchange interventions to the exceptional circumstances of disorderly market conditions."

[5] Exports decreased until September 2012, but increased from October 2012 on a year-on-year basis.

[6] In addition to the government policy which forced banks to restrain lending to households from two years ago, the government started to force non-bank and insurance companies to do it as well from February 2012. The growth rate of household debt slowed, but the outstanding level breaks the record. And in a BOK systemic risk survey conducted in July 2012, respondents considered the greatest key risk to be the "deepening of the sovereign debt crisis in Europe (91.9%)," followed by the "household debt problem (89.2%)," the "recession in the real estate market (73.0%)," and the "hard landing of the Chinese economy (64.9%)." The number of respondents of "recession in the real estate market" largely increased from the previous survey conducted in January 2012 (from 24.3% to 73%).

July 2012, deregulation of real estate loans and reduction of taxes in September 2012. However, consumer sentiment is still low and it makes the stimulus seem to be insufficient (Chart 12).

In the political arena, the presidential election was held on December 19, 2012 and the ruling Saenuri party candidate, Park Geun-hye, was elected. Her policy is to move South Korea from a "cheabol" (family-controlled conglomerate) oriented economy to one of greater equality for small and medium sized firms. However, it is difficult to achieve this in the short-term.

In conclusion, the South Korean economy will recover quickly while the outside situation improves, but a stronger won keeps South Korea from a strong recovery. The real growth rate of South Korea will be 2.8 % in 2013 (Chart 13).

The inflation rate has been decreasing since last year and it is below the BOK's target range (2.5–3.5%[7]). This supports the BOK's decision to cut its policy rate in July and October 2012 in order to boost the economy. The inflation rate will remain at a low level and a stronger won is a concern for its economy, so the BOK will cut its policy rate early in 2013 again. The Inflation rate will be 2.4 % in 2013 (Chart 14).

2-2. Taiwan

Taiwan is similar to South Korea in terms of being an export oriented economy, and Taiwan has also experienced an economic slowdown. However, Taiwan's economy has already begun to recover and the growth rate in Q3 2012 is better than in Q2 2012. Specifically, the market conditions of Taiwan's main industry, semiconductors, are a significant factor for its recovery. In fact, the shipment-to-inventory ratio is improving with the support of the release of Apple's iPhone5 and Microsoft's Windows 8 (Chart 15). Although the export value was still decreasing, export orders are now increasing[8] and exports will continue to improve. However, not all electronics industries are in good condition. Restructuring is widespread, especially in bad DRAM companies, and leave without pay is increasing (Chart 16). The Taiwanese economy as a whole will recover based on exports, but recovery of the job market is slow. Weak domestic demand will continue for the next three quarters.

The government established special economic zones, targeted new export markets as an economic policy, and reinforced its relations with China.[9] However, they are mid- or long-term policies, and short-term stimulus is lacking. Only passive policies, such as prolonging the plan to raise electricity rates[10] in December 2013, have been implemented.

In conclusion, Taiwan's real growth rate in 2013 will recover to 3% while its export situation is improving (Chart 17).

The inflation rate rose suddenly in Q3 2012 because of high food prices caused by heavy rain. The central bank has little room to cut its interest rate, and they didn't cut it during this setback phase. However, the inflation rate is becoming stable and the central bank will cut its

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[7] In 2012, the target range was 2–4%.

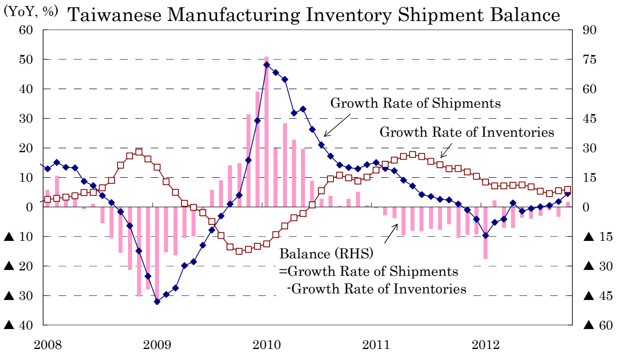
[8] Export value decreased 2.2% in November 2012 from a year ago in Taiwan dollar bases, but export orders increased 11.1% in November 2012.

[9] The Economic Cooperation Framework Agreement (ECFA), which is a preferential trade agreement between the governments of the People's Republic of China (mainland China) and the Republic of China (Taiwan), came into effect on January 2010. It aims to strengthen four areas: free trade of products, deregulation of the service trade, promoting two-way investment, and promoting economic cooperation. Free trade makes progress mainly in "early harvest" items, but the extension of tax reduction items and the deregulation of the service trade are now in conference. Taiwan president Ma Ying-jeou disclosed his intentions to sign all related consultation and China expressed receiving agreement.

[10] Higher oil prices have resulted in a lower profit margin for Taiwan Power Company. To ameliorate this situation, the government planned an increase in electricity rates in March 2012, but it was amended to an incremental increase in June. The first increase was implemented then, but the second planned increase, which was planned for December, has been put off.

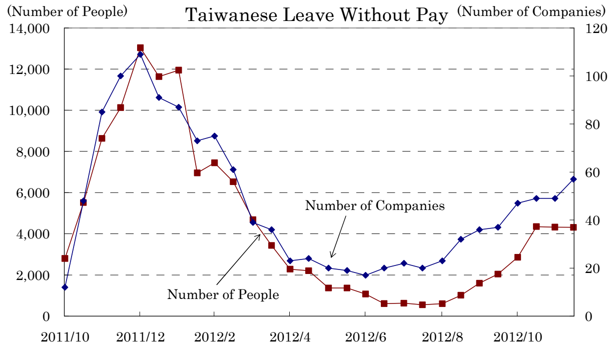
policy rate in order to boost its economy this year. The inflation rate will be 1.4 % in 2013.

(Chart 15)



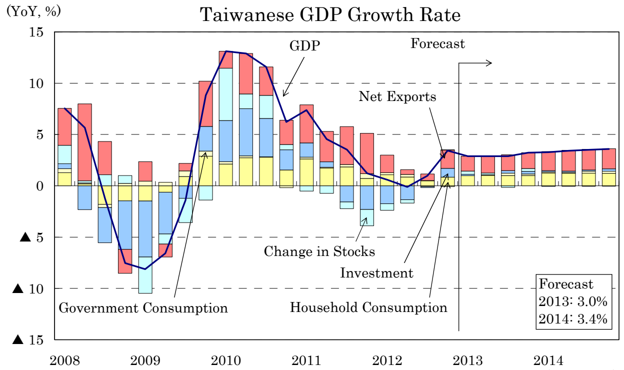
*Growth rate is calcurated 3 month average of year on year growth rate.
Source: CEIC (Monthly)

(Chart 16)



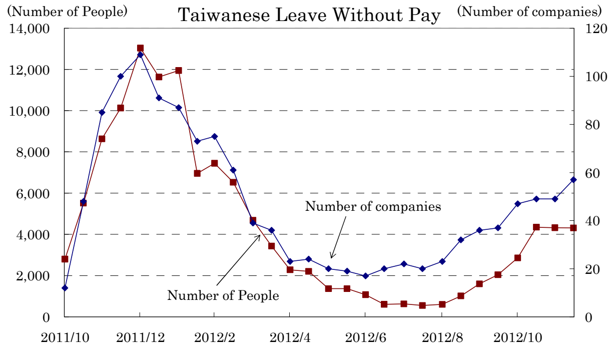
Source: Countil of Labor Affairs (Twice a month)

(Chart 17)



Sources: CEIC, NLI Research Institute (Quarterly)

(Chart 18)



Source: Countil of Labor Affairs (Twice a month)

2-3. Malaysia

Malaysia is also an export oriented economy. Furthermore, export dependence is stronger than in South Korea or Taiwan. However, Malaysia's consumption and investment is strong, and its domestic demand makes up for weak exports. As a result, Malaysia has achieved strong growth.

Regarding consumption, the term of the lower house expired this April, and they engaged in excessive spending before the election. In addition, the inflation rate is stable. As a result, consumer sentiment is good, which is welcomed by the Malaysian economy. This year, government spending and the introduction of a minimum wage system supported household consumption in the short term.[11] In terms of investment, a satisfactory ETP (Economic Transformation Programme)[12] and the welcoming of FDI (foreign direct investment) helped boost the Malaysian economy.

However, the prospects regarding exports are unclear. So far, exports of resources such as LNG and palm oil make up for the decreasing exports of industrial products such as electronic equipment. However, this may not be sustainable. If resource prices decrease too much, palm oil prices will also decrease, and exports could slow down considerably (Chart 20). The most likely scenario is that exports will recover while external demand recovers, but the resource price is a risk factor.

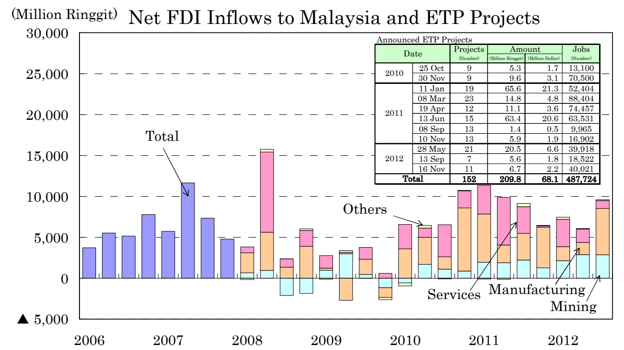
[11] The government gave cash benefits for low-income people and an increased salary for public service workers last year because the election will be held this year. The budget for this year includes a cash benefit for low-income people and reduction of income tax. On the other hand, structural reforms to reduce the budget deficit, such as introducing VAT and a reduction of the subsidy for energy have been shelved. However, they are pursuing an aggressive course of deregulation for trade policy. They relaxed regulations of the service sector, concluded the FTA with Australia (effective this January), started to negotiate about the FTA with the EFTA (European Free Trade Association), negotiated about the FTA with the EU and Turkey, and proceeded on the TPP (Trans-Pacific Strategic Economic Partnership).

[12] The government said that the ETP wrapped up its second year announcing approximately RM20.6 billion in realized investments as of Q3 2012. This constituted 71% of some RM29 billion investments committed for the first two years of implementation. The total investment amount is planned to be RM212 billion.

Generally speaking, domestic demand is so strong that in spite of the risk, Malaysia could achieve 5.2 % growth in 2013.

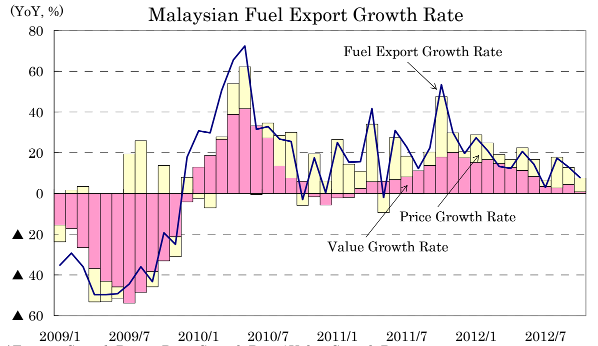
The inflation rate is decreasing, but inflationary pressure will be strong because of the growing economy. As a result, the inflation rate will increase by 2.3% in 2013. Currently, the central bank has room to cut its policy rate, but it will remain at the current rate because the economy seems to be strengthening rather than weakening.

(Chart 19)



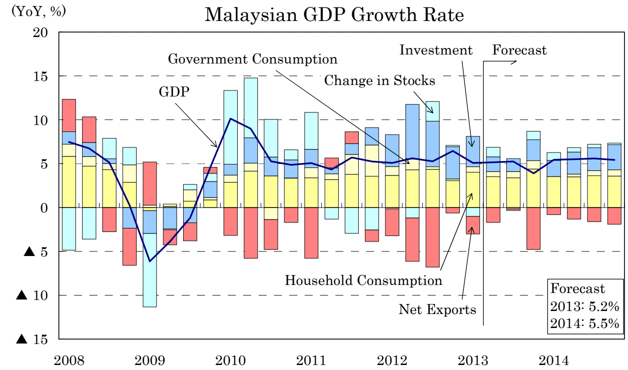
*Components shown from 2008. Amount is calculated 1 Dollar = 3.08 Ringgit
Sources: CEIC, ETP Website (http://etp.pemandu.gov.my/) (Quarterly)

(Chart 20)



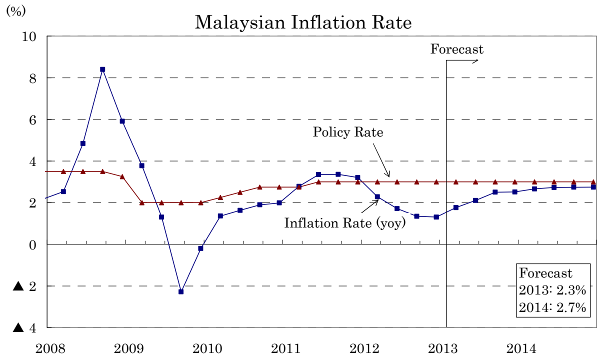
*Exports Growth Rate = Price Growth Rate / Value Growth Rate
Source: CEIC (Monthly)

(Chart 21)



Sources: CEIC, NLI Research Institute (Quarterly)

(Chart 22)



Sources: CEIC, NLI Research Institute (Quarterly)

2-4. Thailand

Thailand suffered serious floods in late 2011, but recovered strongly last year. Restoration in the beginning of the year proceeded quickly, and the government policy to control inflation and boost the economy went well and pushed up the growth rate.

However, Thailand's export dependence is strong and the recovery has slowed down due to weak external demand.[13] The foreign economic situation is improving slowly, but external demand is still weaker than last year. The reopening of factories which were flooded seems to be delayed and the industrial production index has not showed much growth.[14] Business sentiment recovered in the beginning of last year, but fell again among most industries except automobiles and biotechnology (Chart 23).

Moreover, consumption, which is currently strong, remains a concern for the future. The government's budget for this year is economically stimulative and will support Thailand's

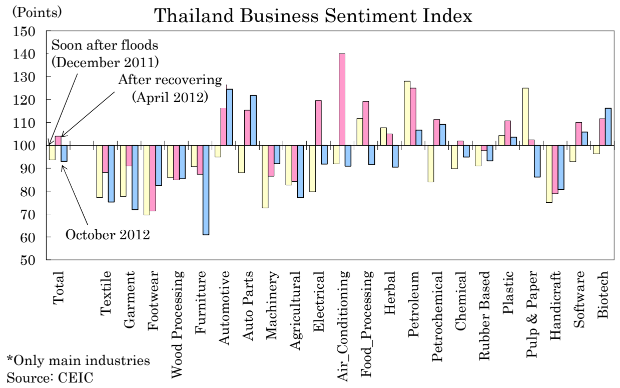
[13] Thailand is more vulnerable to large swings in demand for manufactured goods than Malaysia is to the relatively small changes in natural resource demand. The production HDD (Hard Disk Drive) and communication products are dull.

[14] The production index is under the average of 2011 which is before the flood except May. One possible reason for the delay in the reopening of damaged factories is that weak demand means there is not a strong incentive to quickly restart production.

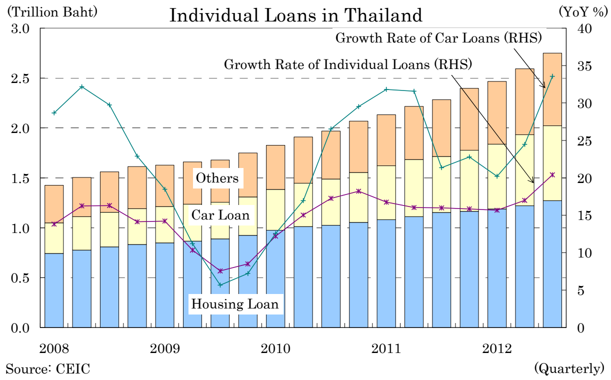
growth in the short term.[15] However, some fiscal policies have had a harmful influence. For example, a government incentive for buying new cars caused an increase in individual loans (Chart 24). It is possible that household consumption will slow after the fiscal policy expires.

In conclusion, the growth rate in 2012 is strong, but it will decrease by 4.0 % in 2013 (Chart 25).

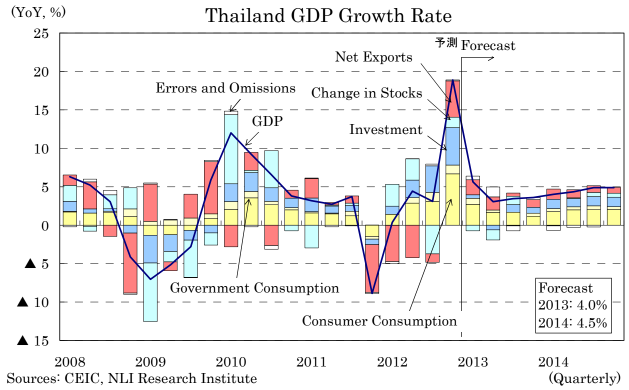
(Chart 23)



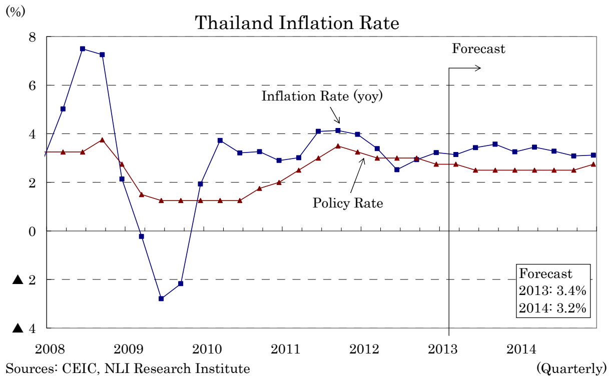
(Chart 24)



(Chart 25)



(Chart 26)



The inflation rate is stable in relation to the BOT's target (which is between 0.5%-3% in terms of core inflation rate[16]). However, strong upward pressure on wages will increase the inflation rate by 3.4% in 2013.

The BOT cut its policy rate in November 2011, February 2012, and again in October 2012 as a relief of measure from the world economic slowdown under these circumstances, which means BOT seems to change its policy stance against inflation from being hard-liners to moderates. Inflationary pressure will make the room for another easing narrow, but the growth rate will be under the expectation of BOT[17] and they will cut their policy rate again this year.

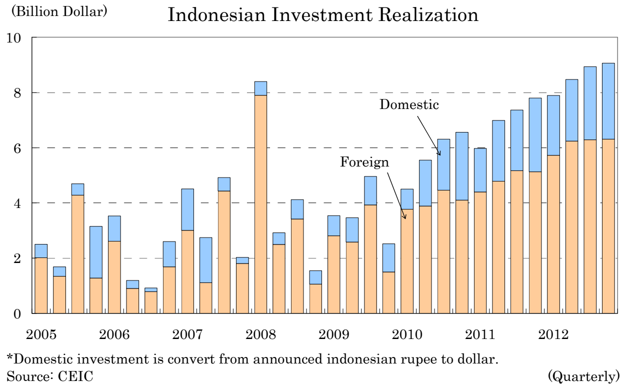
2-5. Indonesia

In spite of a slowdown in exports from weak foreign demand, Indonesia has experienced high growth due to domestic demand. Both domestic and foreign direct investment is growing (Chart 27) and MP3EI (Master Plan for the Acceleration and Expansion of Indonesian

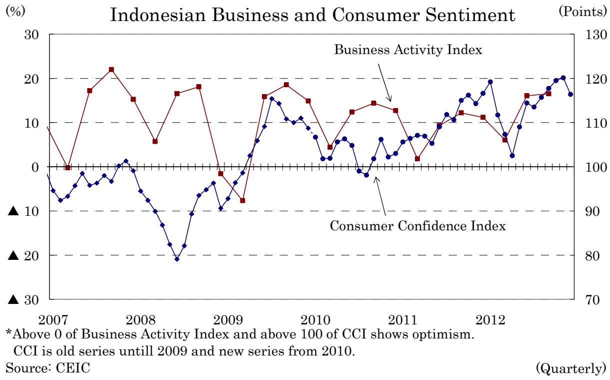
[15] The minimum wage increased by 300 baht and corporate tax and income tax were reduced. In addition, a paddy-pledging program which is essentially a paddy buying program by the government was decided to be continued.
[16] The growth rate of headline CPI is about 3%, but core CPI is about 2% and on target.
[17] The BOT's forecast of GDP growth rate is 4.9% in 2013, which is written in the inflation report by BOT released in January 2013.

Economic Development), which is the public-private investment plan, will boost the growth rate.[18] An increase in minimum wage this year will keep consumption strong.[19] As a result, both consumer sentiment and business sentiment are good (Chart 28).

(Chart 27)



(Chart 28)



(Chart 29)

(Chart 30)

On the other hand, some risks have appeared on the horizon. The October 2012 trade deficit, the largest yet, and falling natural resource prices have produced a decrease in exports. Though the dependence on exports is not so great and domestic demand will make up for it, this decrease is a downward pressure. There is also a chance that demonstrations and strikes over wages and cuts to fuel subsidies[20] will take place. In addition, the government stance tends to be protectionist[21] making it more difficult for foreign investors to do their business. The regulation for individual loans that the government introduced has had little effect so far, but the worry is that the government will expand the range of application this year.[22]

In conclusion, the real GDP growth rate will be 6.3% in 2013 (Chart 29).

The inflation rate stands in the middle of the target of the BI (the central bank of Indonesia), whose range is 3.5%-5.5% in 2013. The BI has maintained a moderate stance after cutting its

[18] The master plan intends to develop industry and infrastructure in the six economic corridors of Indonesia. The total investment amount is 4,000 trillion rupiahs (1,700 trillion of these are for infrastructure). Some pointed out the delay of the progress, but some projects have made progress and the government has tried to proceed with investment positively; for example, they set 15 priority projects.

[19] Wages will increase all over the Indonesia; for example, wage will increase by 44% in Jakarta.

[20] To improve the government deficit, fuel subsidies were planned to be cut last year, but many people objected to it, so the congress rejected it. As a result, any solution has been postponed. Because of the election in 2014, it is difficult to cut subsidies before the election. Only electric rates are being considered.

[21] To promote local refineries, exporting unprocessed metal will be banned. Additionally, regulations on the export of unprocessed metal before 2014 have been imposed. However, the Supreme Court invalidated the decision and the prospect of the government policy is unclear.

[22] The government set the minimum rate of an initial payment for a vehicle except shariah financial institutes in June 2012, but from April 2013 shariah banks will have the same regulations imposed.

policy rate in response to the financial crisis in 2008.[23] However, good economic conditions and rising wages will push the inflation rate higher this year (Chart 30). The BI will keep this moderate stance for the moment and raise its interest rate to control inflation, as well as strengthen currency during the last half of this year.

2-6. The Philippines

Like Indonesia, the Philippines' domestic demand is strong, especially in car and bicycle sales, which achieved strong growth because of the Thai floods. Philippine exports also continue to grow well because the total exports of 2011 were relatively weak, and the production index is increasing (Chart 31). As a result, the Philippines maintained over 6% growth, 7.9% in 3Q 2012.

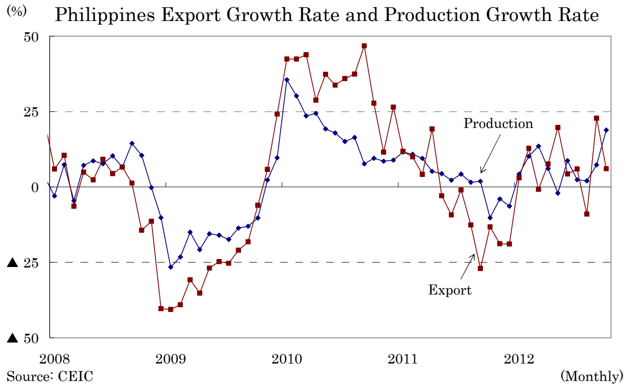
Consumption is likely to remain bullish. The large number of remittance from OFW (Overseas Filipino Workers) will support household consumption[24] and government consumption will also be strong because of the election held in May this year.

Investment will be supported by the PPP (Public Private Partnership), which plans for large infrastructure investments, though investment is not the driver at this time.[25] Investment approval is not so strong compared to 2012. The Philippines need more investment to maintain this strong growth[26] (Chart 32). Exports will grow, as mentioned above, but will not be robust due to the slow economic recovery abroad.

We conclude that the real GDP growth rate will be 5.3% in 2013 (Chart 33).

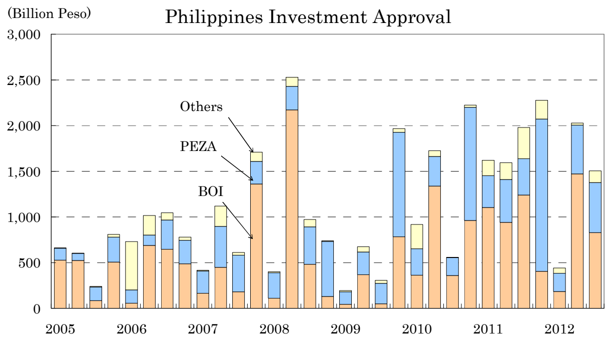
The inflation rate achieved moderate growth. Floods in the Philippines caused inflationary pressure, but the inflation rate is below the target of the BSP (the central bank of Philippines), whose range is 3%-5%. However, the inflation rate will increase by 4.1% in 2013 because domestic business conditions are good (Chart 34). Under the moderate inflation, the BSP has cut its policy rate four times in 2012, in spite of good economic conditions. They seem to be concerned about a slowdown caused by sluggish foreign conditions and a strong currency. Looking ahead, the inflation rate will strengthen and the BSP will keep its policy rate in 2013.

(Chart 31)



Source: CEIC

(Chart 32)



Source: CEIC

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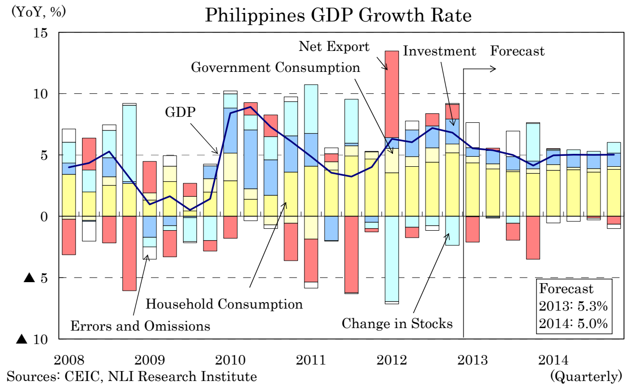
[23] The BI has maintained their policy rate but they raised the interest rate of the central bank's deposit facility (FASBI, which decides the lower limit of the BI's target rate, overnight interbank rate, in essence) in order to reduce liquidity.

[24] OWF remittances tend to increase during the Christmas season, so the rate could slow after that.

[25] Only two projects have had bids made for (one was in 2011 and the other was in 2012). It was originally planned that the bids for eight projects would be made, but their progress was delayed.

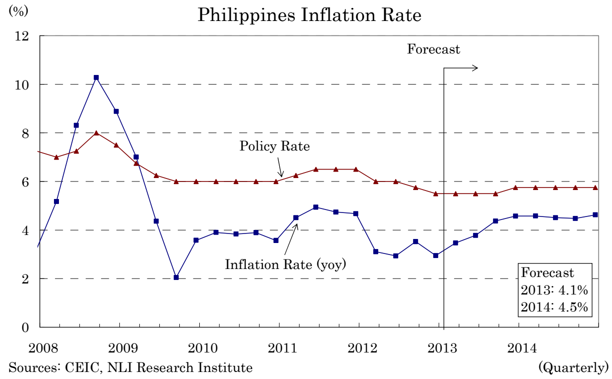
[26] The government is attempting to combine the strategies and policies of the various institutions and organizations who promote foreign investment. The aims include simplifying the complicated incentive systems, prevention of unfair use and increasing tax revenues. However, some are concerned about uncertainties with this process.

(Chart 33)



Sources: CEIC, NLI Research Institute

(Chart 34)



Sources: CEIC, NLI Research Institute

2-7. India

The Indian economy has been sluggish recently. The growth rate[27] has been under 6% since last year and is about 5.5%. The main reason why the Indian economy is sluggish is the fairly high inflation rate. In order to stabilize prices the RBI raised its policy rate. This had a clearly negative effect on economic growth (Chart 35).

Underdeveloped infrastructure continues to cause high inflation, which seems to take much time to solve. Investor sentiment was disappointing, not only because of disappearing growth expectations, but also because of events such as political confusion in congress, large blackouts and riots in automobile firms. However, in September 2012, the government announced a series of structural reforms[28] and impressed investors favorably. As a result, investor sentiment is improving. This caused not only capital inflow in financial markets but also improvements in the real economy, such as a recovery in production (Chart 36).

However, for the present, the progress of the reforms is a topic of concern[29] and whether the reforms will actually be put into practice is unclear. If the progress is delayed, capital inflows will slow down again and could hinder growth in India.[30]

The inflation rate is another point of concern. If the RBI cuts its policy rate, growth expectations will rise. The RBI has cut its policy rate only once, in April 2012. Since then they have left the policy rate unchanged until January 2013 because of high inflation. However, the RBI has assessed the government's reform favorably, and they are changing its stance from restraining inflationary pressure to promoting growth. The RBI has started to cut its interest rate in January 2013 and will cut it more in steps. However, the total rate to cut is limited because structural problems are difficult to solve.

In conclusion, a strong recovery is unlikely to occur, and the growth rate will be 6.4% in 2013 (Chart 37). The inflation rate will slowdown, but will still be at a high level of 7% in 2013 (Chart 38).

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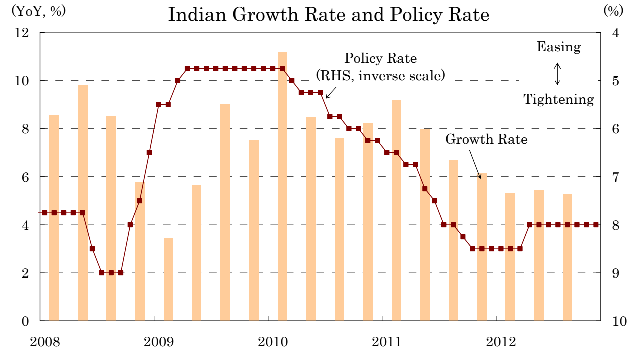
[27] GDP at factor cost.

[28] These are reforms of the restriction on foreign investment (such as opening up its supermarket sector to foreign chains and allowing more foreign investment in airlines and broadcasters), cutting subsidies for diesel and so on. Opening the pension sector to foreign investment and raising the FDI cap in insurance were proposed after that. It was decided to set up the Cabinet Committee on Investment (CCI) to fast-track infrastructure projects.

[29] Discussion about insurance and pension reforms, as well as land expropriation, which is an obstacle to investing infrastructure, was not started during the winter session of Parliament. Discussion will start from February this year.

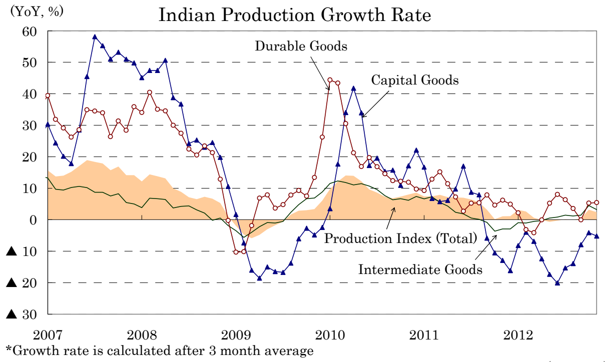
[30] The government decided to allow the opening of general retail sores with some requirements in December 2011, but they withdrew the decision because of objection from opposition parties. The parliament remained idle in August 2012 because of suspicion of corruption of Prime Minister Singh.

(Chart 35)



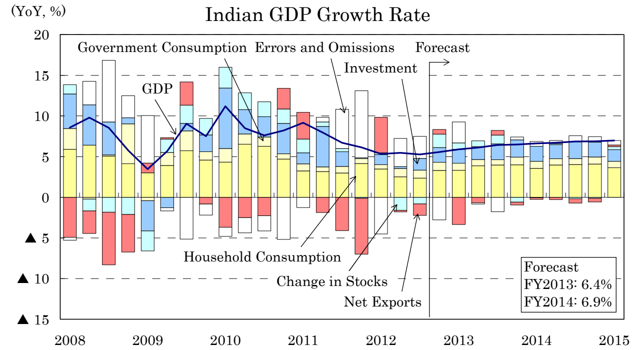
Source: CEIC (Growth Rate: Quarterly, Policy Rate: Monthly)

(Chart 36)



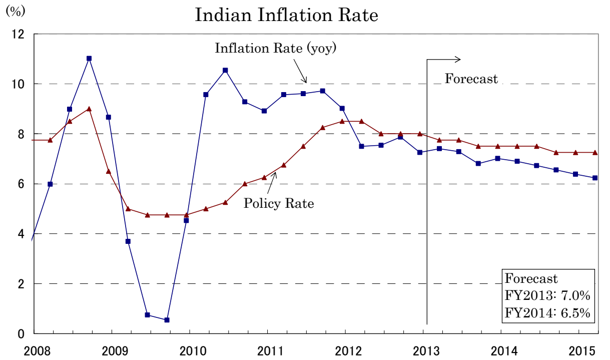
*Growth rate is calculated after 3 month average
Source: CEIC (Monthly)

(Chart 37)



*GDP is at factor cost
Sources: CEIC, NLI Research Institute (Quarterly)

(Chart 38)



Sources: CEIC, NLI Research Institute (Quarterly)

