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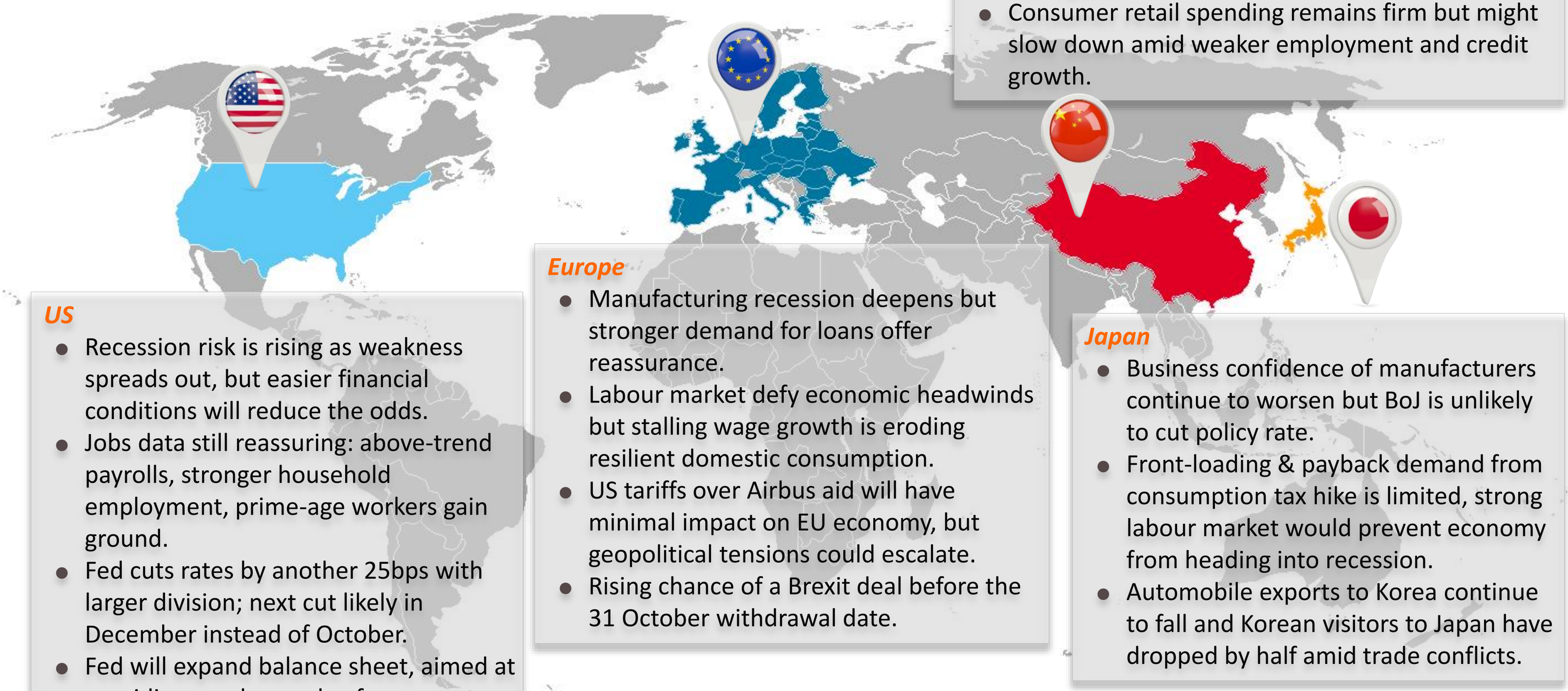
MONTHLY ECONOMIC BULLETIN

October 2019

Krungsri Research

Global: Weakness starts to fan out



China

- Activity has been resilient recently; manufacturing sector has stopped contracting, services starting to rise again.
- Consumer retail spending remains firm but might slow down amid weaker employment and credit growth.

US

- Recession risk is rising as weakness spreads out, but easier financial conditions will reduce the odds.
- Jobs data still reassuring: above-trend payrolls, stronger household employment, prime-age workers gain ground.
- Fed cuts rates by another 25bps with larger division; next cut likely in December instead of October.
- Fed will expand balance sheet, aimed at providing ample supply of reserves to curb money market fluctuations.

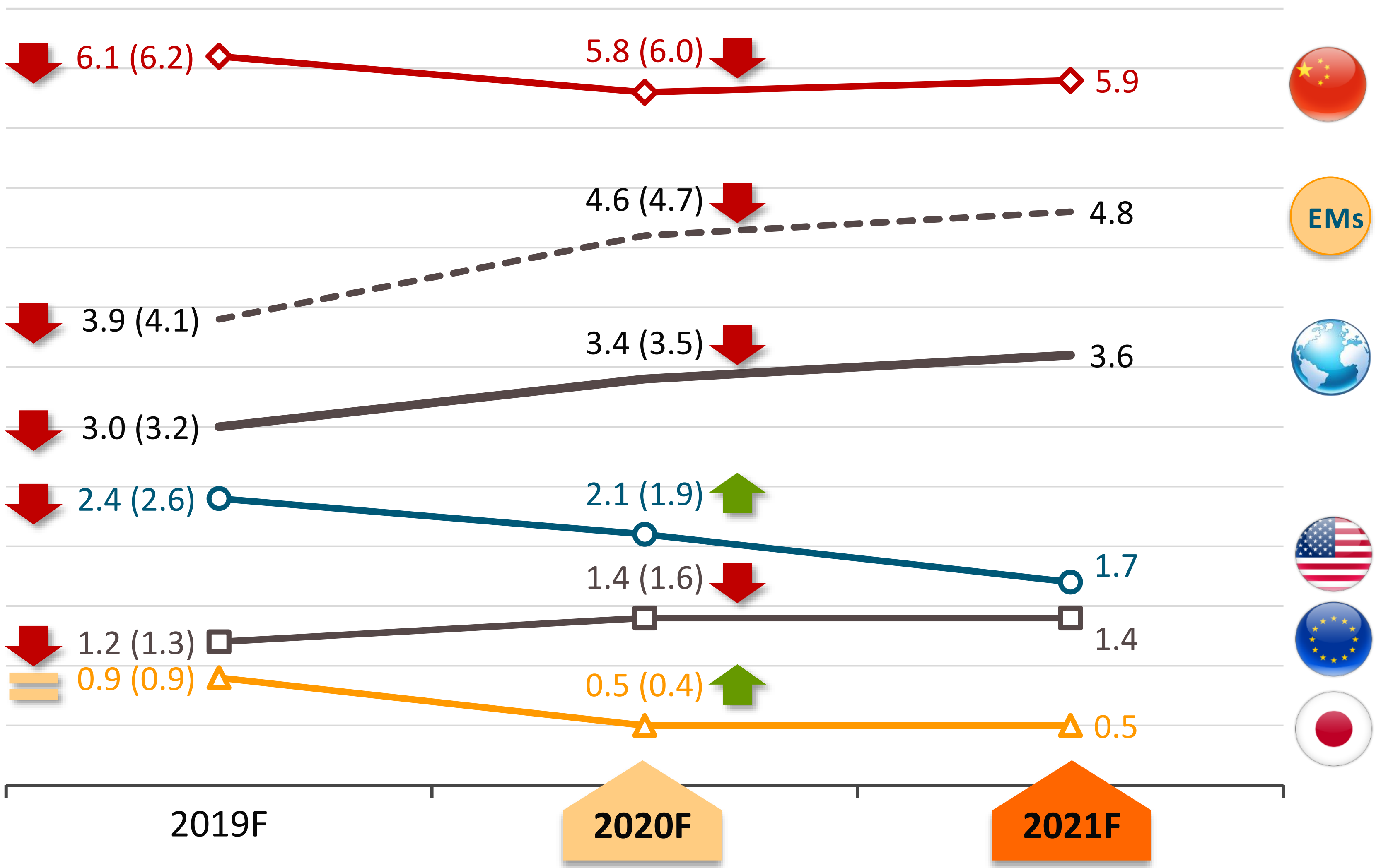
Europe

- Manufacturing recession deepens but stronger demand for loans offer reassurance.
- Labour market defy economic headwinds but stalling wage growth is eroding resilient domestic consumption.
- US tariffs over Airbus aid will have minimal impact on EU economy, but geopolitical tensions could escalate.
- Rising chance of a Brexit deal before the 31 October withdrawal date.

Japan

- Business confidence of manufacturers continue to worsen but BoJ is unlikely to cut policy rate.
- Front-loading & payback demand from consumption tax hike is limited, strong labour market would prevent economy from heading into recession.
- Automobile exports to Korea continue to fall and Korean visitors to Japan have dropped by half amid trade conflicts.

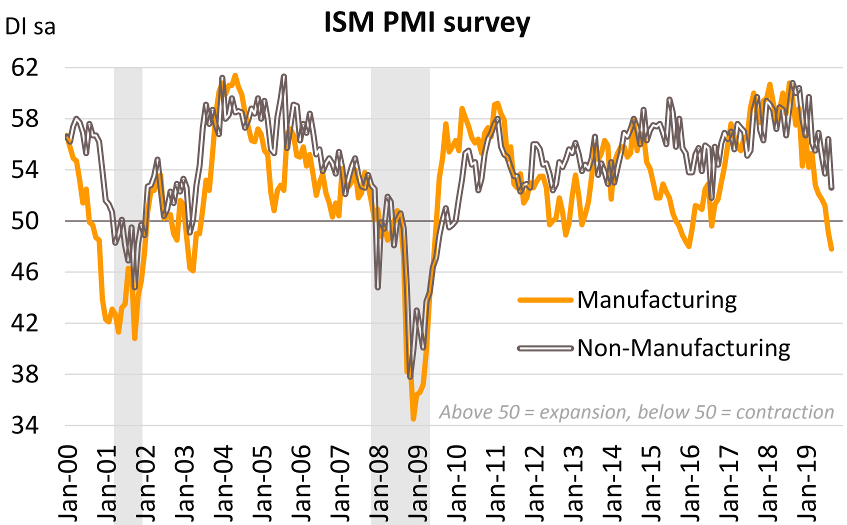
IMF cuts global growth forecasts to the slowest since the global financial crisis, the fifth downgrade in a row

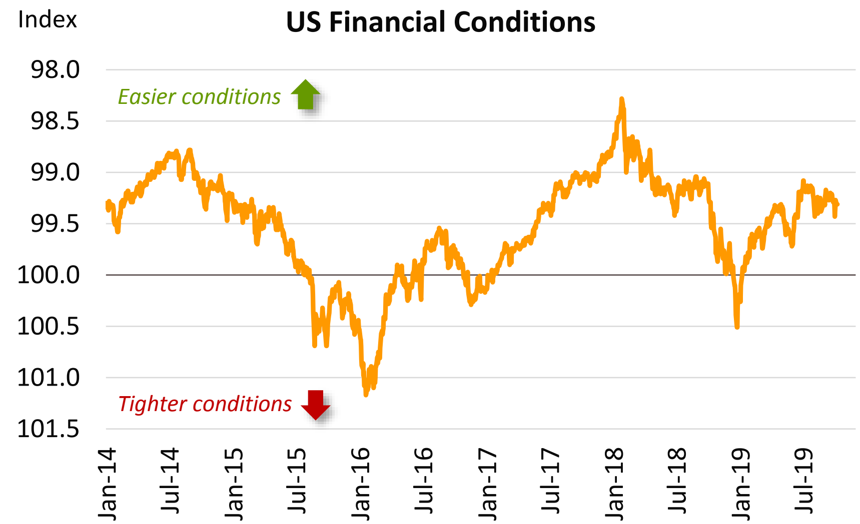


Note: ( ) July 2019 forecast Unit: %

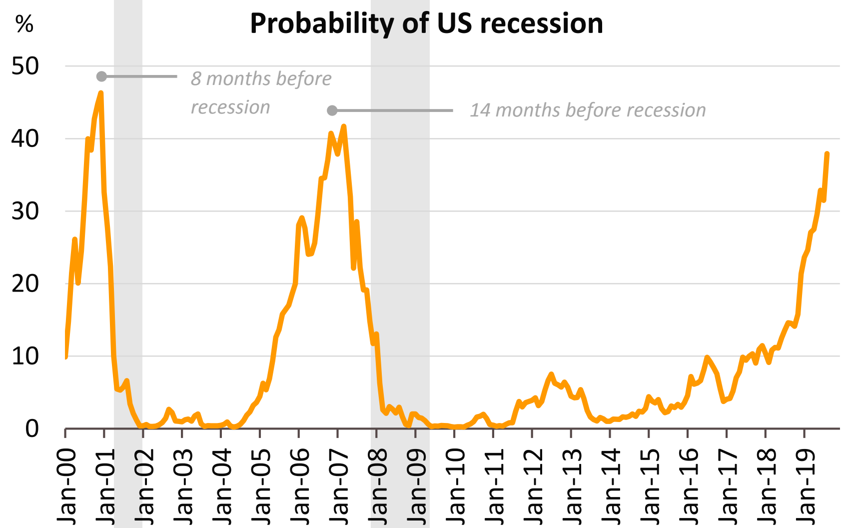
Source: IMF World Economic Outlook (October 2019), Krungsri Research

US: Recession risk is rising as weakness spreads out, but easier financial conditions will reduce the odds





Shaded areas indicate recessions

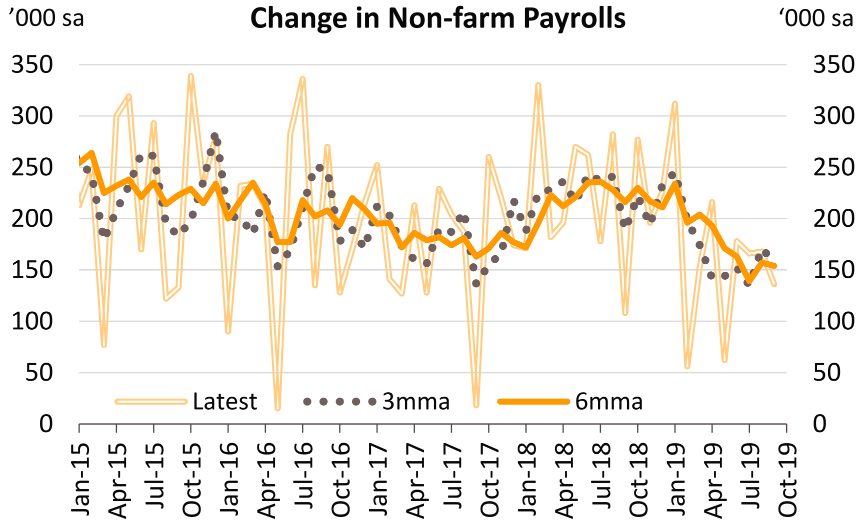


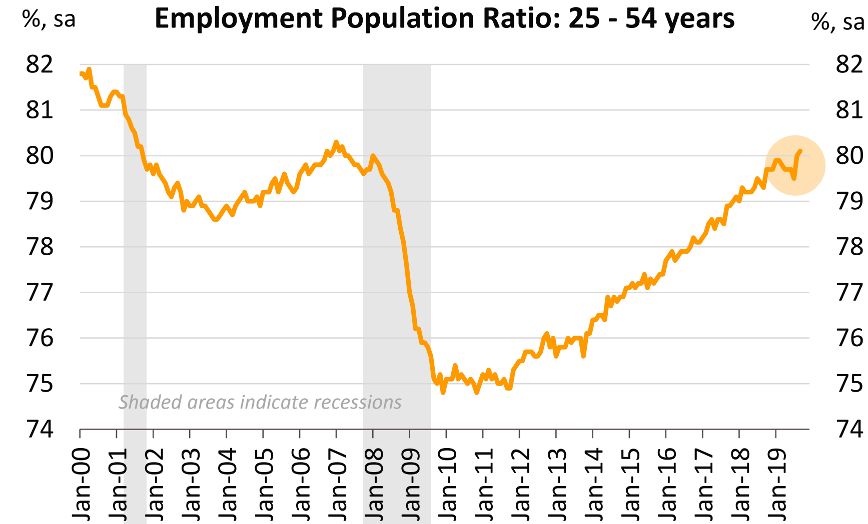
Krungsri Research's view

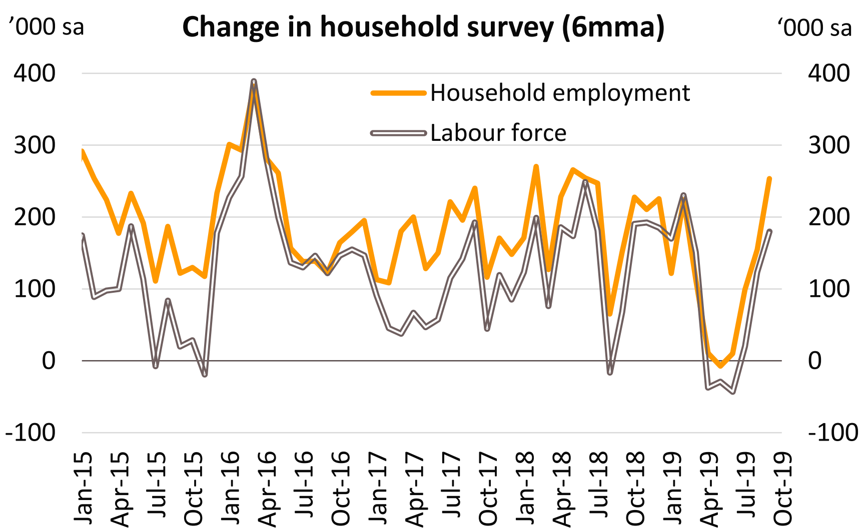
- The US economy has reached a critical juncture where weakness in the manufacturing sector is spreading to the much larger services sector, reflected by weaker-than-expected Non-Manufacturing ISM data. The economic weakness might start to feed on itself and potentially trigger a recession. The probability of a recession has risen to close to 40% – suggesting there could be a recession within the next 8-14 months.
- But, the deceleration in the services sector has been limited so far. This is the key difference with the 2001-02 and 2008-09 periods, when the services sector collapsed in lockstep with manufacturing activity. And US financial conditions have eased significantly in the last two months, thanks to the dovish pivot by the Fed. Looser financial conditions usually bode well for growth outlook, and would support the continued recovery in rate-sensitive sectors like durables consumption and housing.

Source: Institute for Supply Management (ISM), Federal Reserve Bank of New York, Bloomberg, Krungsri Research

Jobs data still reassuring: above-trend payrolls, stronger household employment, prime-age workers gain ground





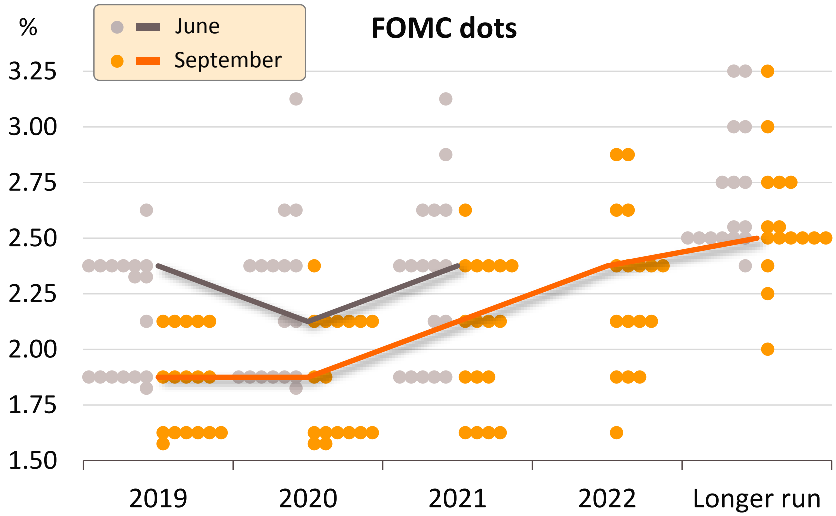


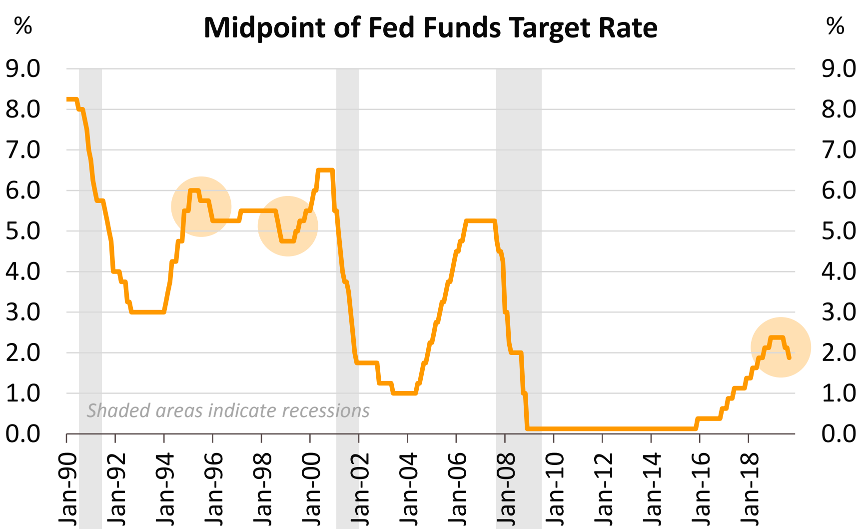
Source: Bureau of Labor Statistics (BLS), Bloomberg, Krungsri Research

Krungsri Research's view

- Non-farm payrolls rose by 136k in September, below consensus estimate of +145k. But upward revisions in the previous two months (45k sum) took the underlying trend (both 3- and 6-month moving average) to above 150k.
- Household survey data was much stronger, with U3 unemployment rate and U6 underemployment rate falling to new cycle-lows of 3.5% and 6.9%. This was for good reasons: (i) household employment gained by 391k, outpacing the 117k rise in the labour force, which caused 6-month moving average for these indicators to continue to rise; (ii) the share of population aged 25 -54 who were working inched up by one-tenth to 80.1% in September, the highest since March 2007.
- Even though jobs data are lagging indicators, it does not hurt to think recession fears are excessive premised on the following: (i) slower pace of job gains is still sufficient to accommodate new workers entering the labor force; and (ii) despite the economic slowdown becoming more prominent, businesses are still hiring (net hiring).

Fed cuts rates by 25bps again with greater division; next cut is likely in December instead of October



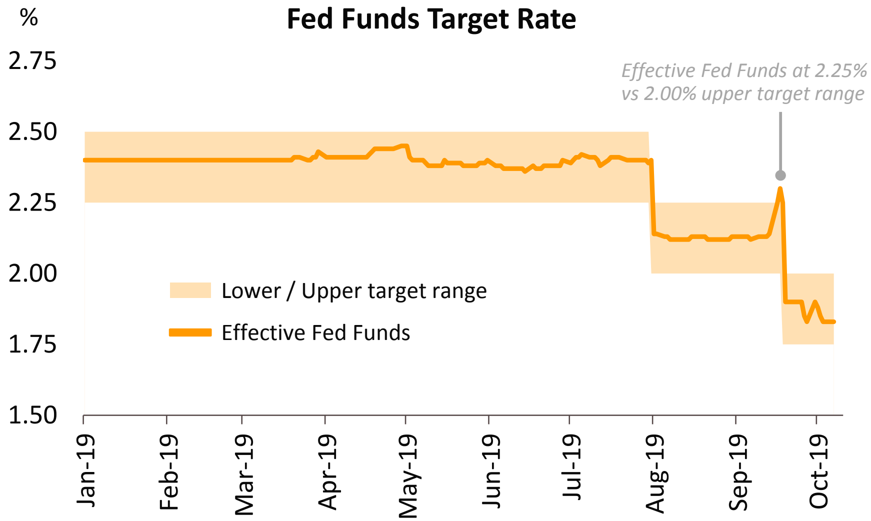


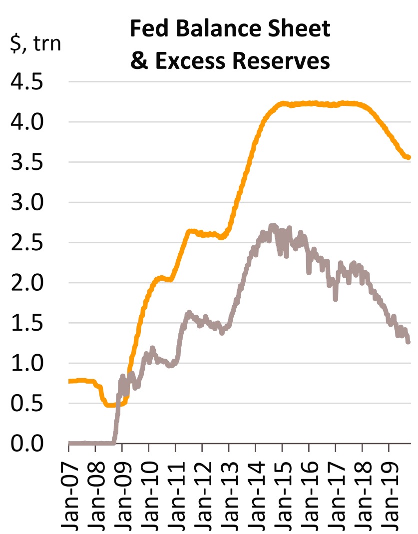
Source: Board of Governors of the Federal Reserve System, Bloomberg, Krungsri Research

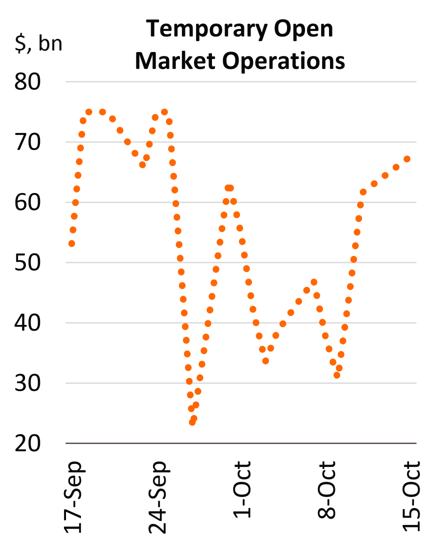
Key notes from FOMC Meeting on 17-18 September

- The FOMC voted 7-3 to lower target fed funds rate by 25bps to 1.75-2.00%, as widely expected. Among the three dissenters, Boston Fed President Eric Rosengren and Kansas City Fed President Esther George voted to keep the target range unchanged, while St. Louis Fed President James Bullard voted for a 50bps rate cut.
- The accompanying statement continued to note that the Fed will *"act as appropriate to sustain the expansion"*. And the economic assessment is largely unchanged. Household spending *"has been rising at a strong pace"* – an upgrade from *"has picked up"* in the previous meeting. On a weaker tone than previously, the statement indicated business fixed investment and exports *"have weakened"*.
- The median dots suggest no more cuts this year, with greater division among Fed officials. Seven participants project another 25bps cut before year-end, while five members expect no further cuts and five officials disagreed with the 25bps cut at this meeting. Beyond 2019, the dots show no change in 2020, and a 25bps rate hike each in 2021 and 2022.
- At the press conference, Fed Chair Powell hinted he would support another 25bps cut this year, saying *"it's better to be proactive in adjusting policy if you can"* and *"it can be a mistake to try to hold onto your firepower until a downturn gains momentum"*. To address recent pressures in money markets, Powell noted the Fed would use temporary open market operations *"for the foreseeable future"*, and it *"will need to resume the organic growth of the balance sheet earlier than we thought"*.
- The less-dovish dots along with greater division in the FOMC strengthen the case for no rate change in October. Beyond this, we remain convinced the Fed would provide additional insurance against trade policy uncertainty, and we continue to expect another 25bps cut in December, close to the final round of tariffs on imports from China scheduled for 15 December.
- In total, we expect 75bps in cuts, equivalent to the amount of easing orchestrated during both the 1995-96 and 1998 mid-cycle slowdown episodes. The Fed appears to be using these two episodes as a base for its current decisions. The Fed might also start to expand its balance sheet in November.

Fed will soon expand balance sheet to provide ample supply of reserves to curb money market volatility







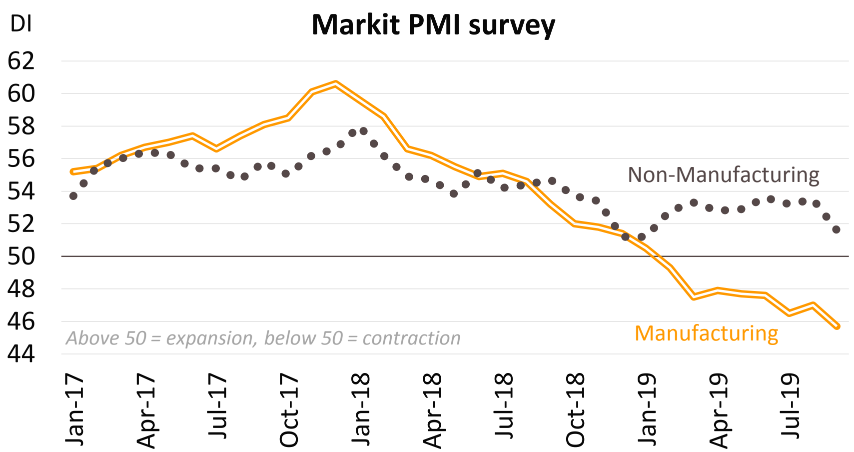
Source: Board of Governors of the Federal Reserve System, Bloomberg, Krungsri Research

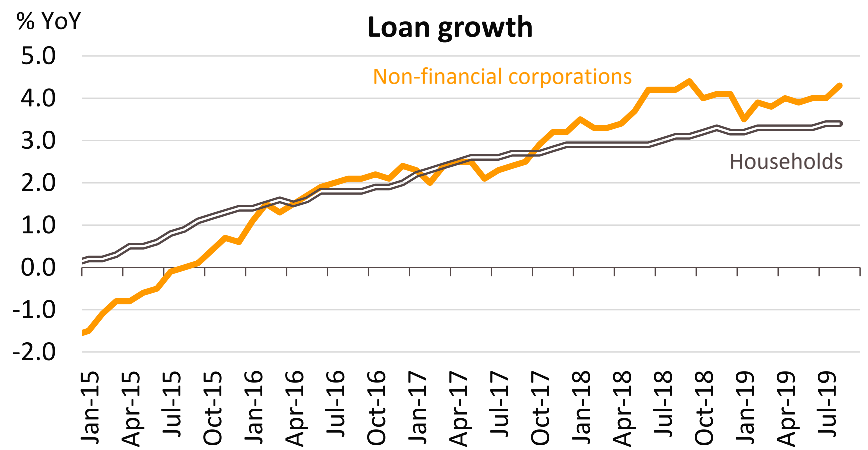
Krungsri Research's view

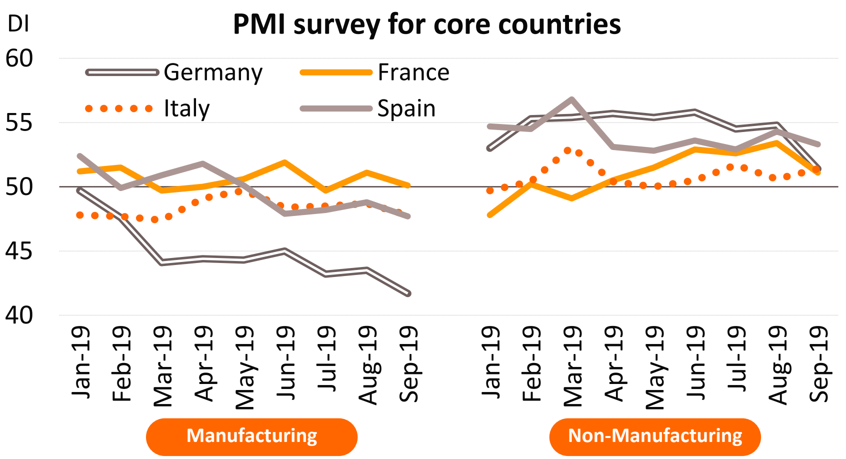
- In mid-September, money market interest rates surged unexpectedly, raising the possibility of a funding crunch and catching traders off guard. Repo rates briefly spiked (intra-day levels soared as high as 10%), and the effective fed funds rate exceeded the FOMC's target range.
- These developments were contributed by both idiosyncratic and structural factors, including (i) payments to meet corporate tax obligations and to purchase Treasury securities, which drained about USD100bn from money-market funds; and (ii) shrinking reserves in the banking system driven by the unwinding of the Fed's balance sheet.
- Reserves – bank deposits held at the Fed – have tumbled from USD2.72trn in 2014 (when the Fed stopped buying assets) to USD1.26trn at end-September, apparently closer to the appropriate level of reserves (with a precautionary buffer) of USD1.2tn (according to the Fed's February Senior Financial Officer Survey).
- To counter these pressures, the Fed began conducting temporary open market operations, which have generally reduced money market volatility. However, the Fed has to decide how to prevent these strains from recurring and impeding the effective implementation of monetary policy and hurt market confidence.
- At the NABE conference, Fed Chairman Jerome Powell hinted the Fed will soon increase purchases of short-term Treasury securities. He said these purchases should not be construed as quantitative easing, noting that a portfolio weighted towards shorter-term securities is aimed at maintaining an appropriate level of reserves – the move simply reduces volatility in the funding market and provides little or no economic stimulus.
- We expect asset purchases for reserve management purposes to be formally announced at the October 29-30 FOMC meeting, and implemented shortly thereafter. It is critical that it be implemented soon as funding and liquidity pressures tend to creep up towards year-end.

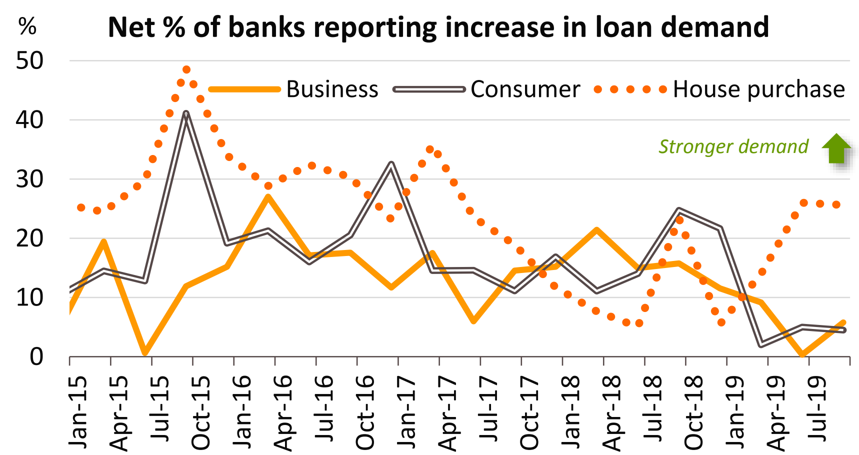
Europe: Manufacturing recession deepens but stronger demand for loans offer reassurance

Manufacturing PMI data suggest industrial production would contract more sharply in the following months. Germany's industrial slump is likely to get worse due to a larger knock-on effect from the auto sector. Activity slid deeper into contraction territory in Italy and Spain, but held up well in France. Services PMI data has been more stable recently but is a lot weaker than in 2017. Meanwhile, bank lending growth has accelerated to 3.8% in August, the highest in over 10 years. Lending to households is rising at a decent pace. Lending to firms rose 4.3%, only 0.1ppt lower than its cyclical high in September 2018. And, the net percentage of banks reporting an increase in demand for business loans picked up in September. Coupled with the ECB's comprehensive easing package in September, that could further support bank lending and rein in mounting downside risk.





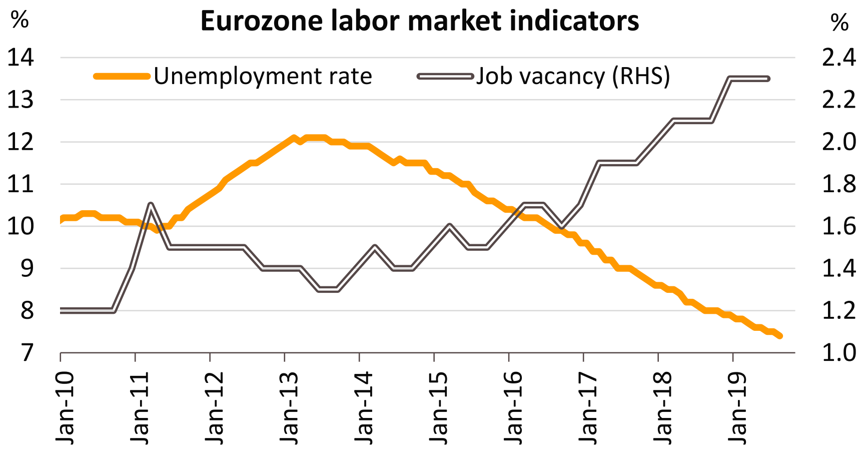


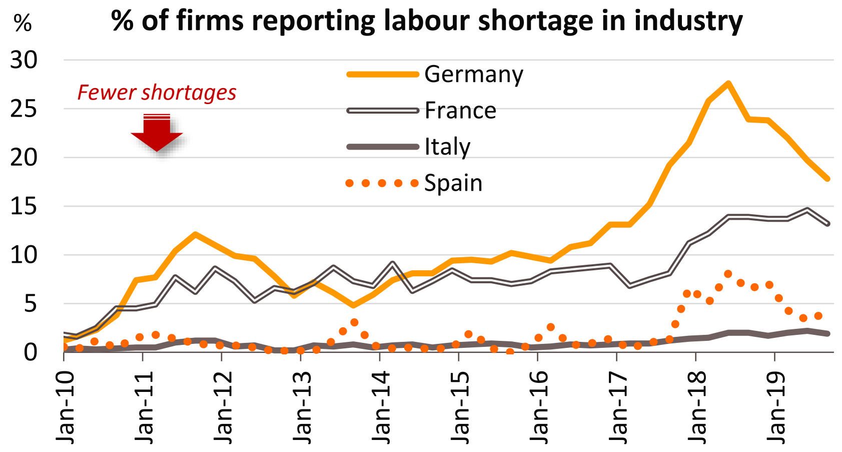


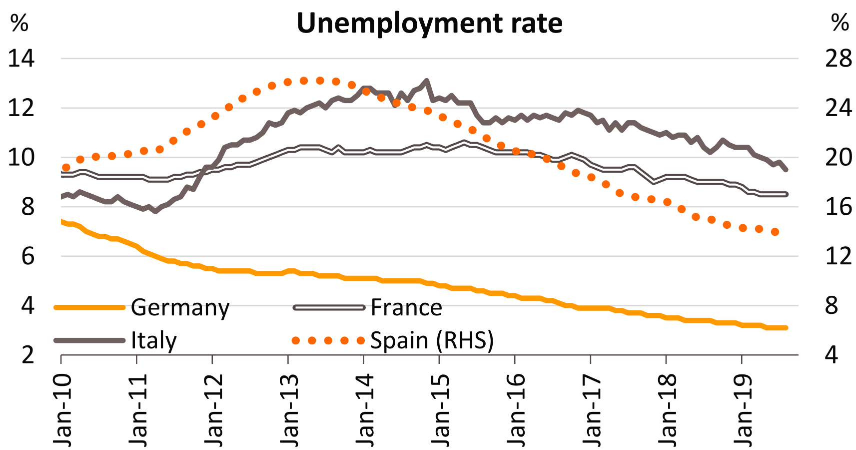
Source: Eurostat, European Commission (EC), Markit, Bloomberg, Krungsri Research

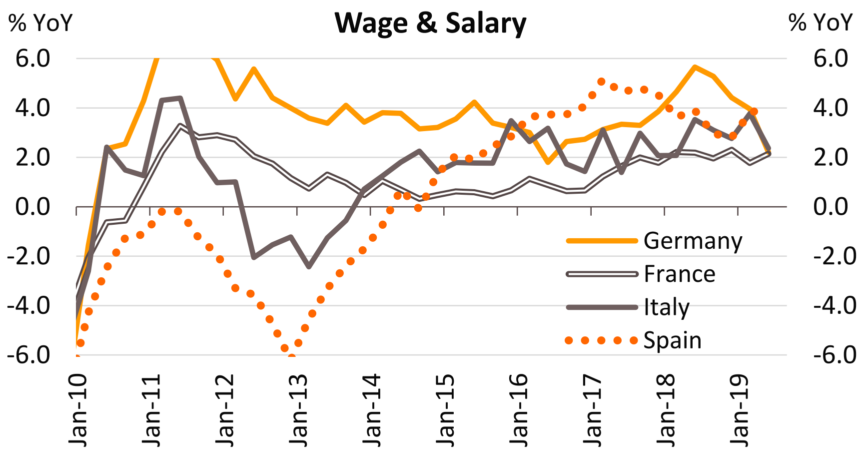
Labour market defy economic headwinds but stalling wage growth is eroding resilient domestic consumption

Eurozone unemployment rate continued to drop to a cyclical low of 7.4% in August. Jobless rate fell markedly in Italy (-0.3ppt to 9.5%) and mildly in Spain (-0.1ppt to 13.8%), and was unchanged in Germany (3.1%) and France (8.5%). In addition, job vacancy rate is at the highest since the survey began in 2004. However, surveys of firms' hiring intentions point to employment growth losing momentum in the periods ahead. The share of firms reporting labour shortage continued to fall in all core countries, most sharply in Germany. Given this, wage growth is likely to have passed its peak, and could start to erode resilient domestic consumption.





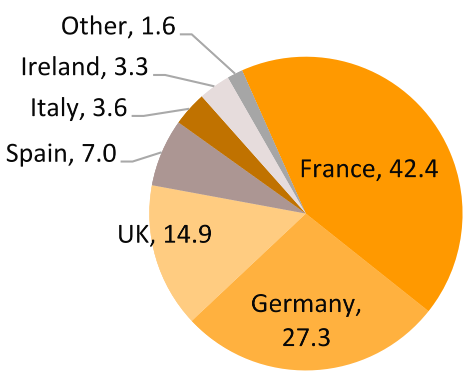




Source: Eurostat, EC, Bloomberg, Krungsri Research

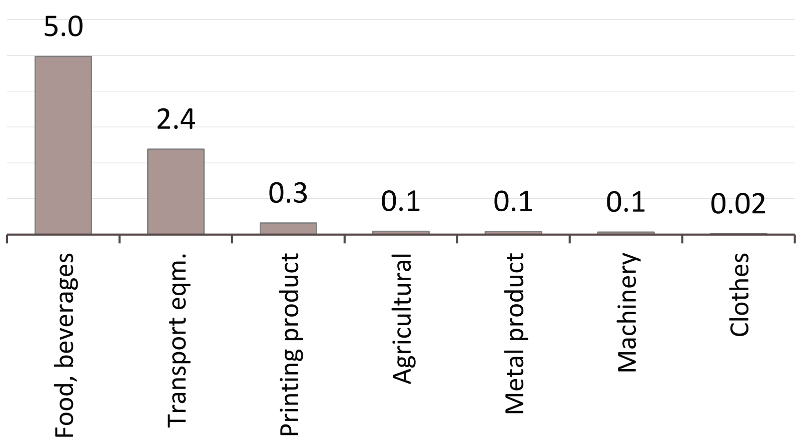
US tariffs over Airbus aid have minimal impact on EU economy but geopolitical tensions could escalate

Share of tariffed EU products worth USD7.5bn by country (%)



Tariff impact on EU economy (% change from baseline)

Higher effective tariff by sector (% change)



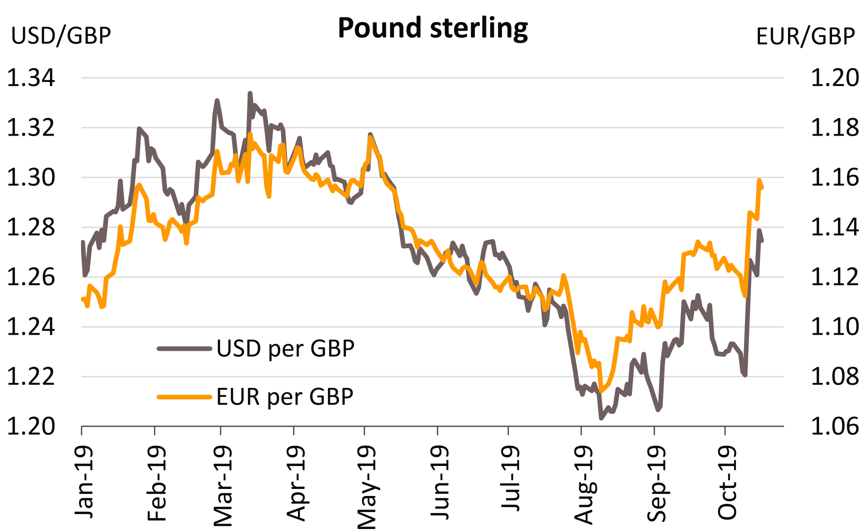
Krungsri Research's view

- The WTO has allowed the US to impose tariffs on EU goods worth USD7.5bn annually over unfair EU subsidies for Airbus since 2004. The tariffs include 10% on EU aircraft and 25% on other goods such as dairy products and liqueurs. The tariffs are effective 18 October.
- The highest tariffs will be on products from France, Germany, UK and Spain, which account for a combined 90% of tariffed products worth USD7.5bn. The largest impact would be on the Aircraft industry in these four countries. There is also widespread impact on the Food & Beverage sector in several EU countries.
- The EU is pursuing a similar retaliation by asking the WTO to grant tariffs on US goods. Although this could worsen the trade tensions, the tariff hikes would have minimal impact on their overall economies.

Source: Global Trade Analysis Project (GTAP), World Trade Organization (WTO), United States Trade Representative (USTR), Trade Map, Bloomberg, Krungsri Research

Rising chance of a *Brexit* deal before 31 Oct

	May's deal	Johnson's proposal
North Ireland (NI) customs/tariffs	• NI in EU customs union	• All UK (including NI) in own customs jurisdiction
Great Britain (GB) customs/tariffs	• GB in EU 'customs territory'	• UK in own customs jurisdiction
Agriculture and manufactured goods	• NI follows EU • UK maintains comparable standards	• NI follows EU • UK flexibility
Labor/environmental standards	• No digression/level playing field	• UK gets more flexibility
Implications for third country free trade agreements	• Services only	• UK gets more flexibility
Likely EU-UK free trade agreement	• Full free trade agreements • Customs jurisdiction • Some regulatory alignment ('Turkey+')	• Goods only ('Canada minus') • Minimal coverage of services • Significant non-tariff barriers
Irish border	• No checks	• Checks away from the border



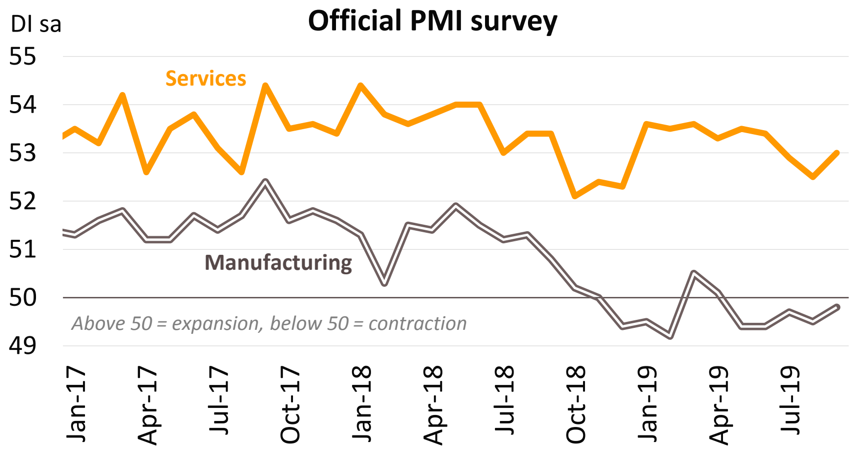
Source: The UK in a Changing Europe, Bloomberg, Krungsri Research

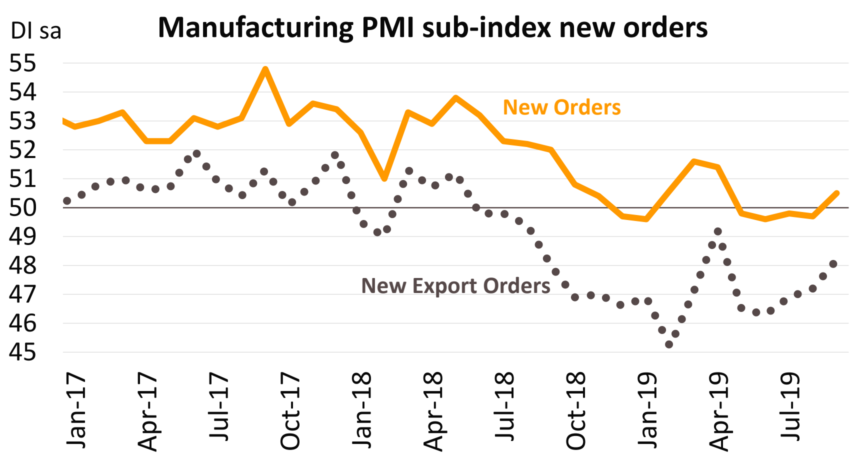
Krungsri Research's view

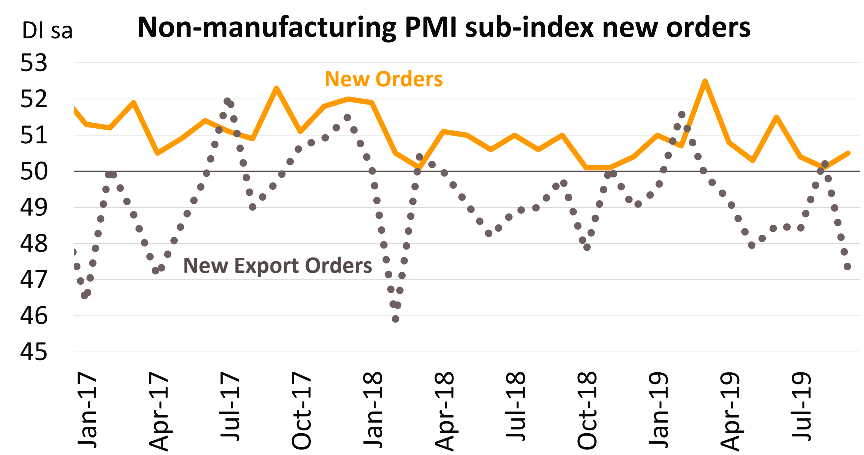
- The UK pound sterling has appreciated in recent days to a 5-month high after reports the UK and EU negotiators are close to a Brexit deal before the 31 October withdrawal date.
- Although there are substantial differences between the key elements in the Withdrawal Agreement (negotiated by Theresa May and agreed by the EU) and Boris Johnson's proposal (recently submitted to the EU), there is optimism of a Brexit deal, signalled by the EU's chief Brexit negotiator. He indicated it was *"time to turn good intentions into legal text"* and *"it [a deal] is still possible this week"*. At the 17-18 October EU Summit, negotiators from both sides will discuss the legal and technical implications of the proposal. Even if they agree on a deal, it would require ratification by the UK parliament.
- Under PM Johnson's proposal, Northern Ireland (NI) and Great Britain (GB) would both leave the EU's customs union, but NI would remain aligned with EU regulations for all goods (subject to approval by NI every 4 years) while GB would have an independent trade policy. All in, the plan would necessitate customs checks on NI-Ireland trade and regulatory checks on NI-GB trade.

China: Activity has been resilient recently; manufacturing data has stopped contracting, services data is rising again

The official Manufacturing PMI data inched up to 49.8 in September (from 49.5 in August). The sub-index new orders, which indicate domestic demand, rebounded to above-50 for the first time in five months. While the new export orders component remained in contraction territory, it is clearly on an upward trend. The rise in industrial inventories continued to slow and the level is now low by historical standards, offering reassurance there would not be massive destocking ahead. Despite uncertainty in US-China trade negotiation, there is limited downside risk to manufacturing sector activity. The official Services PMI data inched up from 52.5 in August to 53.0 in September led by strong growth in the new orders component.



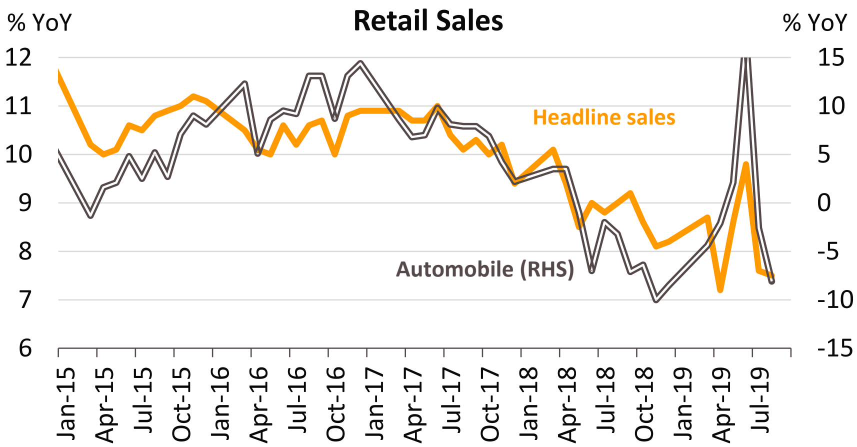


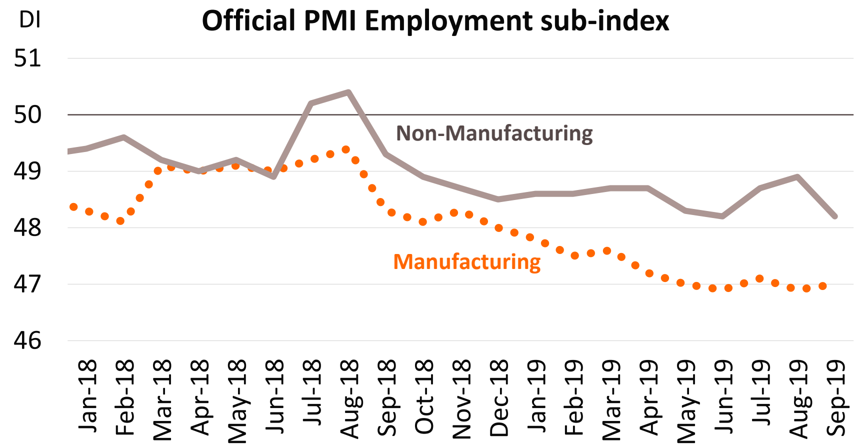


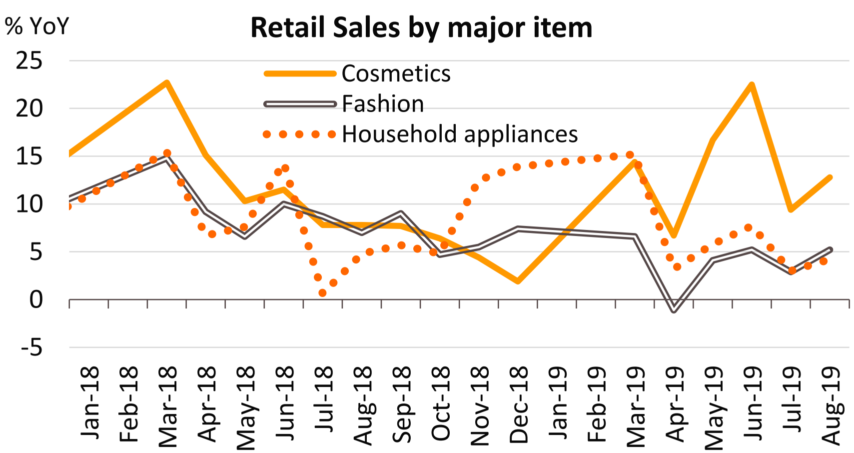
Source: China Federation of Logistics and Purchasing, National Bureau of Statistics (NBS), Bloomberg, Krungsri Research

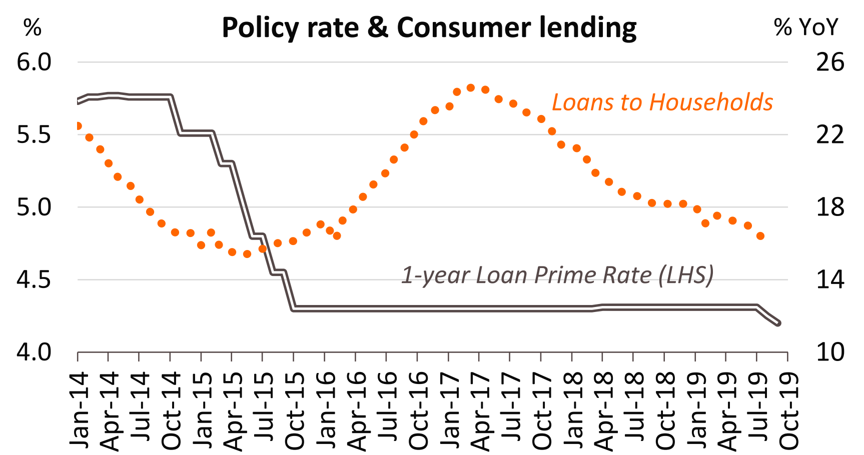
Consumer retail spending remains firm but looks ripe for a slowdown amid weaker employment and credit growth

Headline retail sales was firm in August, rising 7.5% YoY (vs +7.6% in July). This was despite automobile sales tumbling 8.1% YoY after sliding 2.6% in July. There was a pick-up in other categories. Sales of cosmetics, fashion products and household appliances surged 12.8% YoY, 5.2% and 4.2% respectively. However, there are lingering fears this uptick might not be sustainable due to slower employment growth. The Employment PMI sub-index, which is below-50, suggests weaker new hires in the manufacturing and services sectors. In addition, PBOC's efforts to use the Loan Prime Rate (LPR) to reduce banks' lending rates have had limited impact and failed to boost consumer lending.





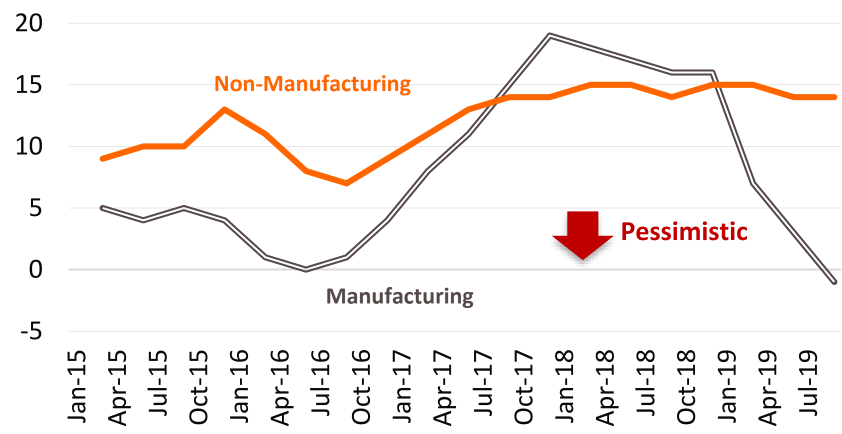




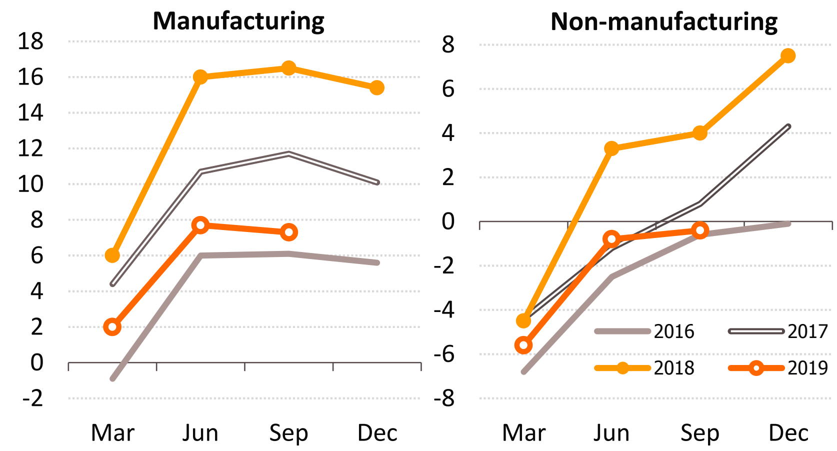
Source: China Federation of Logistics and Purchasing, NBS, People's Bank of China (PBOC), Bloomberg, Krungsri Research

Japan: Business confidence of manufacturers continue to worsen but policy rate cut unlikely to happen

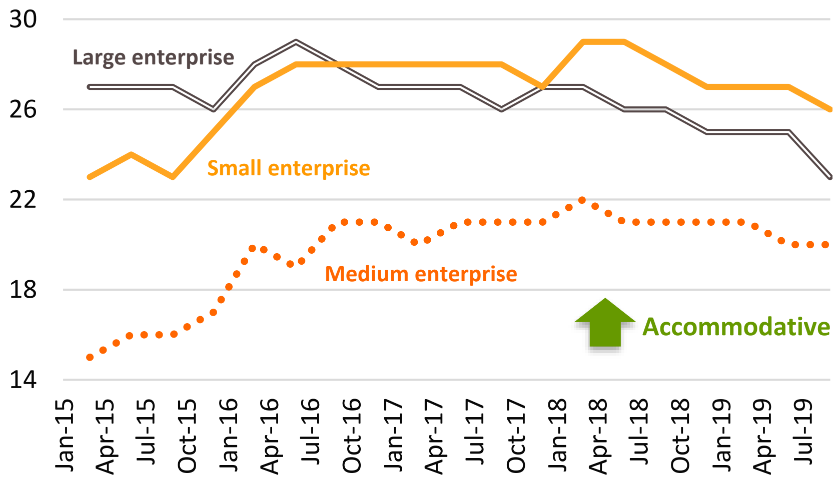
Business Confidence (Diffusion Index)



Capex plan for FY2019 (full spending: % YoY)



Lending attitude of financial institution index (Diffusion Index)



Source: Bank of Japan (BOJ), Bloomberg, Krungsri Research

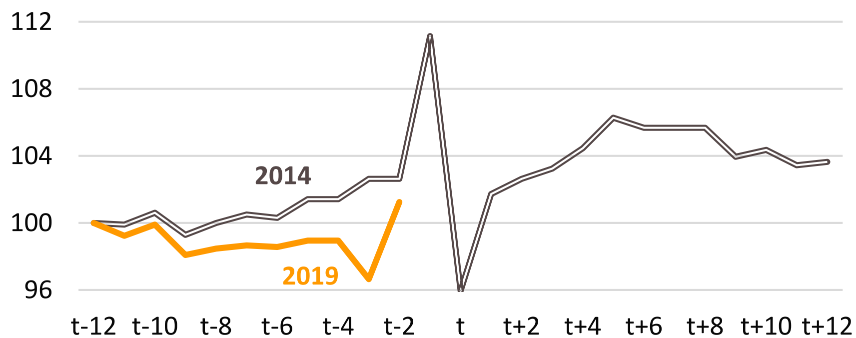
Krungsri Research's view

- Tankan survey data show big manufacturers' business confidence had dropped to a six-year low in 3Q19 due to the global slowdown and escalating trade wars. However, confidence remained robust in non-manufacturing sectors. This resilient services sector could drive stronger domestic consumption to offset the impact of slower external demand.
- Capex plans are stable despite heightened uncertainty in external demand. FY2019 capex plans of manufacturers were revised down slightly to +7.3% YoY in September, but that still beat economists' estimates. Meanwhile, capex plans by non-manufacturers inched up to -0.4 % YoY.
- We expect the BOJ to maintain policy interest rates to avoid an adverse effect on bank profits. Data suggests financial institutions are focusing on lending to small firms because they can get margins than lending to larger firms. However, to ease market concerns over a global slowdown, the BOJ could extend its forward guidance for ultra-low interest rates at least to the end of 2020 at the October 30-31 meeting (vs at least spring at the previous meeting).

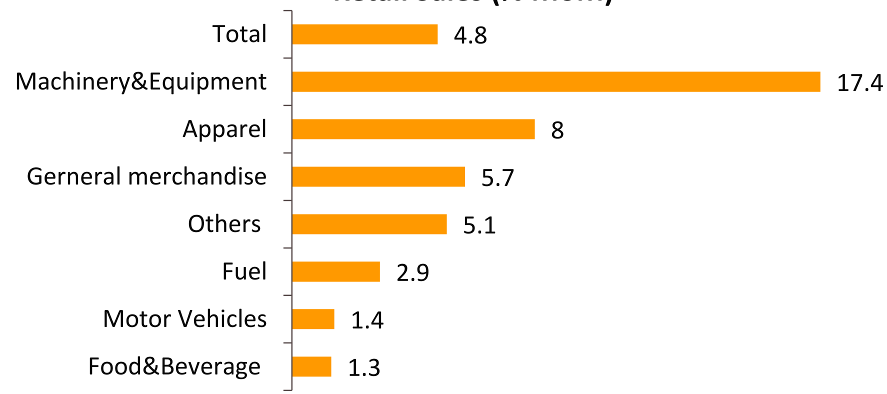
Front-loading & payback demand from tax hike is limited, strong labor market would prevent a recession

After retail sales shrank in July partly because of bad weather, it surprisingly jumped 4.8% MoM in August with broad-base growth in goods. This should eased fears consumption is too weak to weather the consumption tax hike in October. We still expect frontloading and payback demand from the tax hike this year to be moderate and less than during the 2014 tax hike, due to the smaller increment (8% to 10% in 2019 vs 5% to 8% in 2014). However, consumption could weaken in 4Q19 due to payback effect and worsening consumer confidence amid the global slowdown. The job market remains strong with labor shortage reported in the non-manufacturing sectors. Demand for labor in the manufacturing sector has dropped by remains strong. The record-low unemployment rate and high jobs-to-applicant ratio suggest the labor market remains strong and could prevent an economic recession.

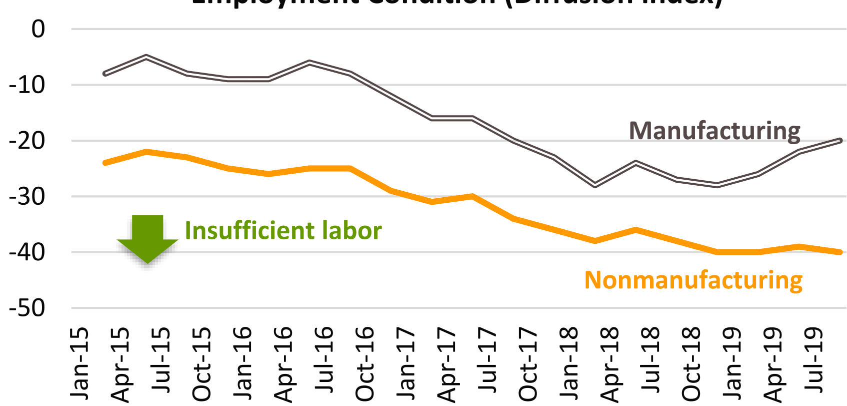
Retail Sales Index (12 month before tax hike = 100)



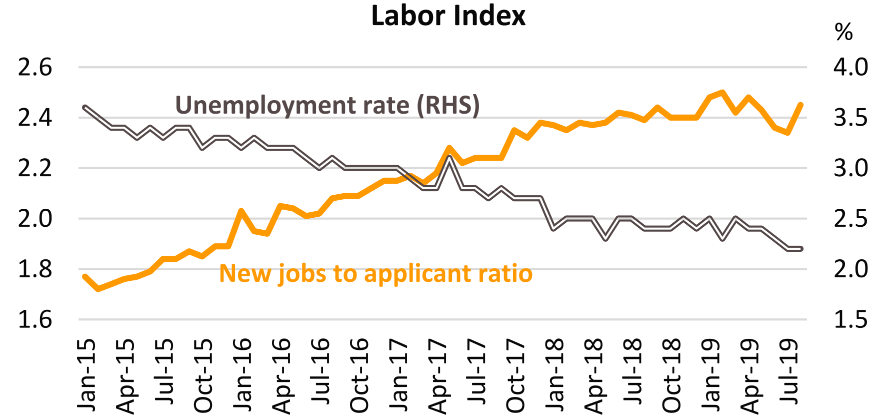
Retail Sales (% MoM)



Employment Condition (Diffusion index)



Labor Index

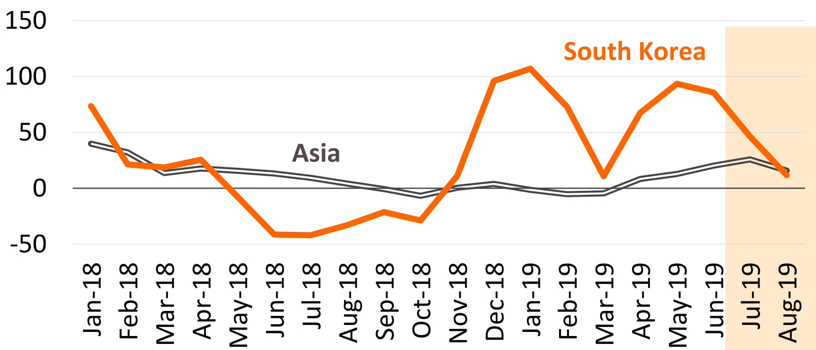


Source: BOJ, Statistical Bureau, Bloomberg, Krungsri Research

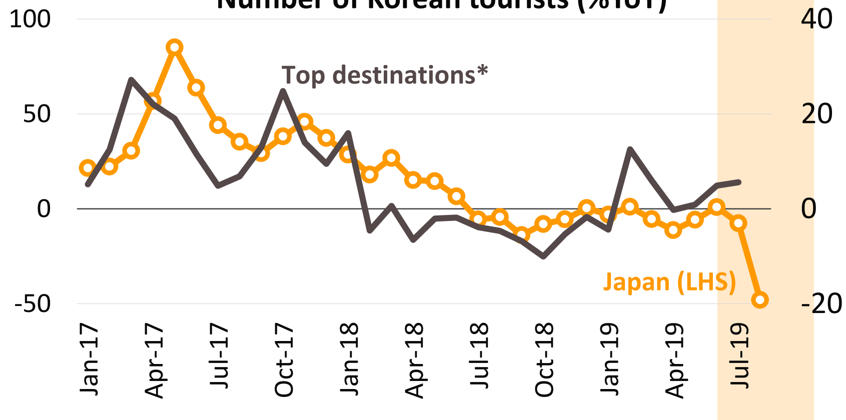
Automobile exports to Korea continue to fall, Korean visitors to Japan drop by half amid trade conflict

Japanese automobile exports to South Korea continued to decline after Korean consumers started to boycott Japanese goods since July amid escalating trade conflict. However, the impact is moderate because automobile exports to Kores account for only 0.9% of Japan's total automobile exports. Nevertheless, we will monitor to see if the boycott could extend to other export items as South Korea is the third largest export market for Japan at 7% of total Japanese exports. And, anti-Japanese sentiment has spread to the services sector. Korean visitors to Japan had dropped by 48% YoY in August, but the effect on the services sector could be limited because although Korean tourists are the second-largest share of arrivals at 24.2%, their spending is only 12.7% of total foreign tourist spending in Japan. This is much less than spending by Chinese tourists which account for 40.6% of arrivals in Japan.

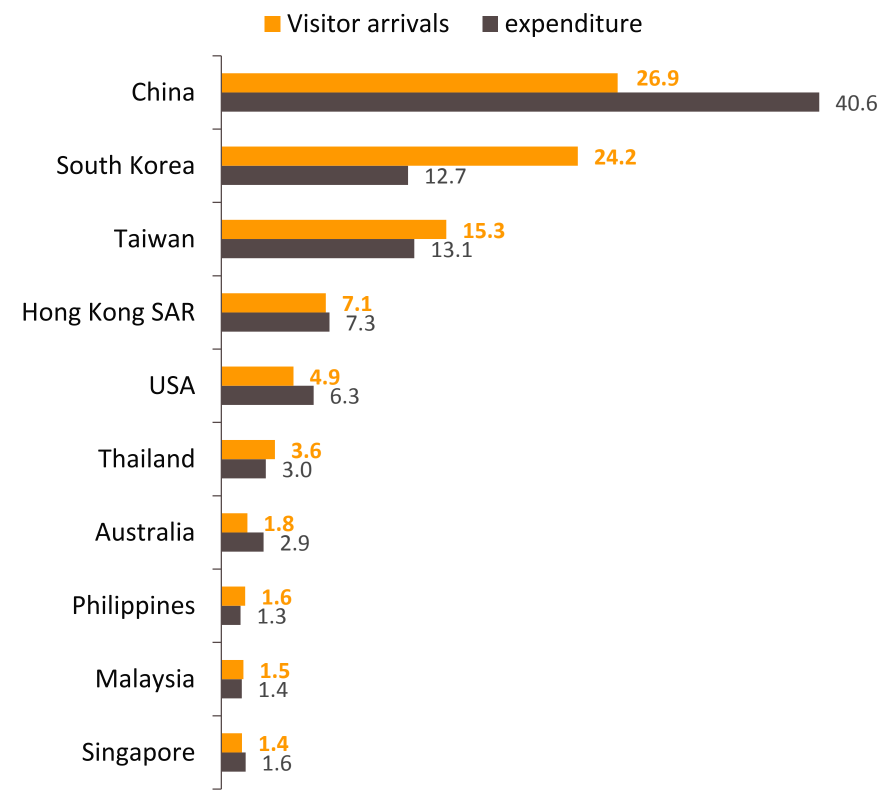
Japanese automobile exports (3mma,% YoY)



Number of Korean tourists (%YoY)



Share of visitor arrivals and expenditure in Japan in 2018 (%)



Note: Top destinations include Japan, USA, Thailand, Philippines, Hong Kong, Singapore, Australia, Taiwan, Germany and Canada

Source: Cabinet Office, CEIC, Statistical Bureau, Bloomberg, Krungsri Research

Thailand: Further weakness in economic and inflation data suggests another rate cut is imminent

Domestic spending weakened in August, dampening economic growth further in 3Q19

- Private consumption growth slowed again in August following a contraction in spending on durable and semi-durable goods. Private investment plunged, with all investment categories slipping for the first time since February 2017. Household income indicators were mixed in August: farm income slowed for the sixth month, and non-farm wage growth eased. Sentiment survey data were weak in September: business sentiment slipped deeper below 50, and consumer confidence marked a 3-year low.

Exports weakened again in August after surprise growth in July; we keep 2019 export growth forecast at -1.6%

- Merchandise exports slipped back to negative growth in August after the surprise surge in July. Excluding gold, exports saw a steeper decline, marking the sixth consecutive month of contraction. Exports tumbled for almost all products and destinations, except for processed foods and shipments to the US and the Middle East. Looking ahead, even if lingering trade tensions and a global downturn continue to dim the export outlook, there is more visible positive impact from trade diversion which has been gathering momentum, as suggested by the continued strength in exports of processed foods and rubber products, as well as shipments to the US. Coupled with a favorable low base, we continue to expect smaller negative growth the rest of the year, and maintain 2019 export growth forecast at -1.6% (or -2.8% FOB basis).

Disinflation continued in September because of Non-Food deflation, taking annual inflation deeper below target

- Headline inflation inched down to 0.32% in September, taking 12-month moving average deeper below target range for the third month. Prices for Non-Food & Beverage categories continued to slip for the fourth month, marking the slowest rate since June 2016. This was primarily due to Energy deflation, which led to a steeper decline in the price of Transportation & Communication. A slower rise in Food & Beverage inflation added to the downside. Core inflation eased further to 0.44%, suggesting demand-pull price pressure remained subdued.

BOT keeps rates; weaker growth outlook, stronger forward guidance support another 25bps cut before year-end

- After a surprise 25bps cut at the previous meeting, the Bank of Thailand maintained policy rate at 1.50%. The BOT sounded more bearish in its outlook for the economy and has strengthened its forward guidance even as it kept rates steady, suggesting another rate cut is possible before year-end. As such, we continue to expect the next 25bps rate cut in November. This is premised on the following: (i) 3Q19 GDP data is likely to remain sluggish; (ii) fiscal impetus could have only a marginal impact, which could prompt the BOT to introduce additional insurance; (iii) strong peer pressure as several other central banks – notably the Bank of Korea – continue to pursue monetary easing towards the end of the year.

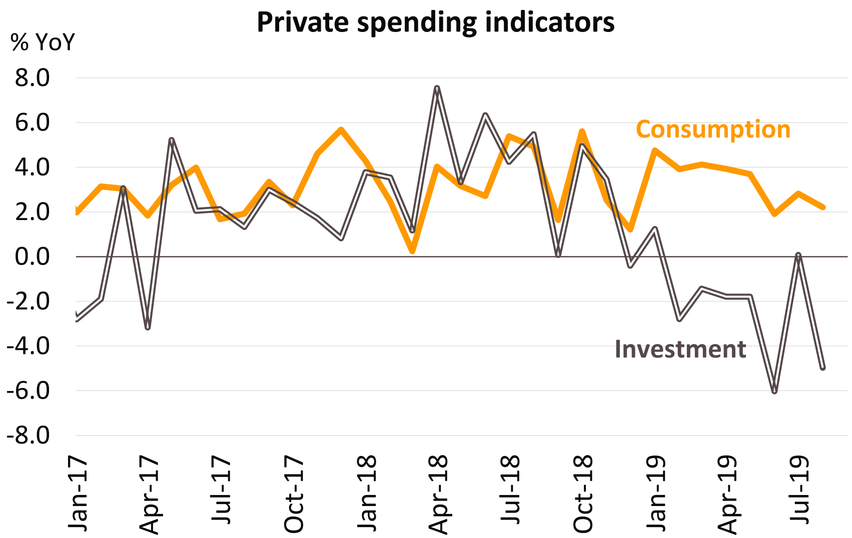
Thailand Economic Outlook 2019-2020

Krungsri Research Forecast		2017	2018	2019F	2020F
GDP growth	YoY (%)	4.0	4.1	2.9	3.5
Private Consumption Expenditure	YoY (%)	3.0	4.6	3.9	3.8
Government Consumption Expenditure	YoY (%)	0.1	1.8	2.2	2.8
Private Investment	YoY (%)	2.9	3.9	3.4	4.5
Public Investment	YoY (%)	-1.2	3.3	2.5	4.2
Nominal Exports in USD (f.o.b.) *	YoY (%)	9.5	7.5	-2.8	2.0
Nominal Imports in USD (f.o.b.)	YoY (%)	13.2	13.7	-3.5	4.0
Current Account Balance	USD, bn	44.0	28.5	31.9	27.4
Tourist Arrivals	Mn, persons	35.6	38.3	39.6	42.0
Headline Inflation	YoY (%)	0.7	1.1	0.9	1.1
Core Inflation	YoY (%)	0.6	0.7	0.6	0.7
Exchange rate (end of period)	THB/USD	32.66	32.42	30.63	30.00
Policy Interest rate (end of period)	(%)	1.50	1.75	1.25	1.25
Dubai crude price (period average)	USD/bbl	53.0	69.3	66.5	74.0

** Customs-based export growth forecast: -1.6% in 2019, +1.3% in 2020*

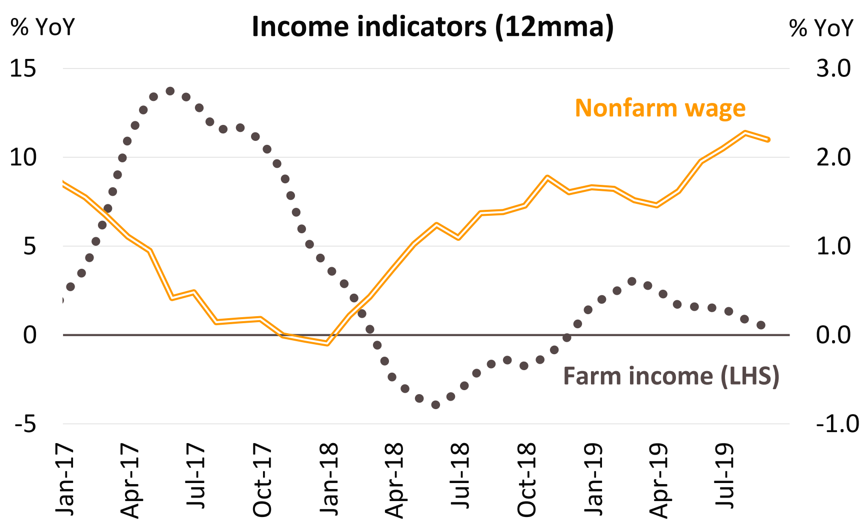
Source: Office of the National Economic and Social Development Council (NESDC), Bank of Thailand (BOT), Ministry of Commerce (MOC), Ministry of Tourism and Sports (MOTS), Krungsri Research

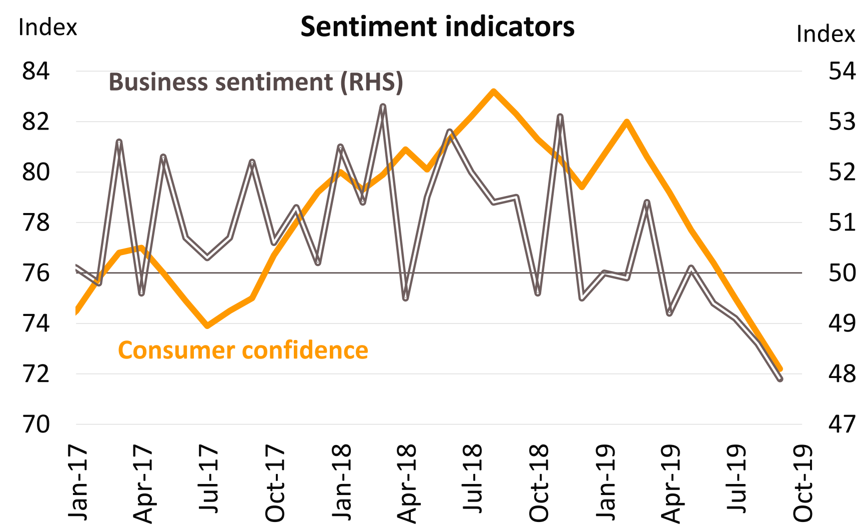
Domestic spending weakened in August, dampening economic growth further in 3Q19



Krungsri Research's view

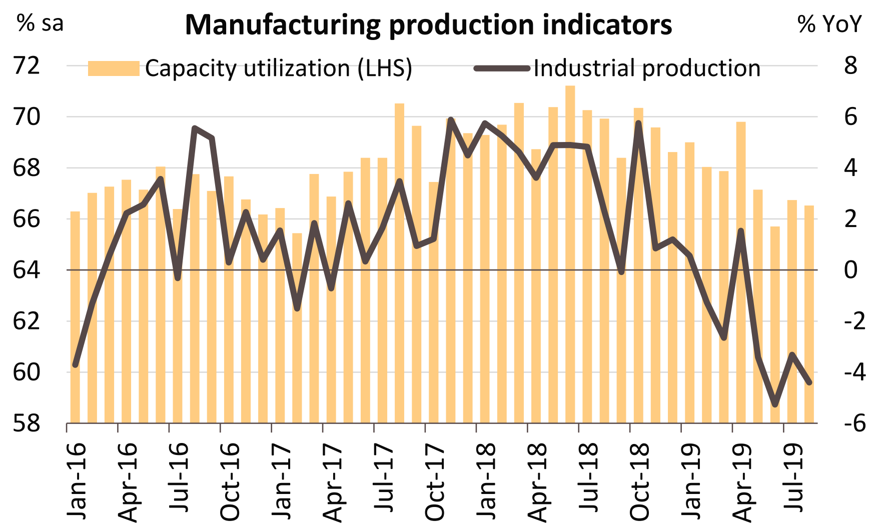
- Private consumption growth slowed to +2.21% YoY in August (vs +2.82% in July), taking QTD average growth to +2.51% (vs +3.20% average in Q2). There was contraction in spending on durable goods (-4.02% YoY) and semi-durable goods (-0.11%). Spending growth for non-durable goods eased to +1.55% YoY, the slowest in eleven months. On a positive note, services spending rose 2.32% YoY, the strongest in four months.
- Private investment plunged 4.97% YoY (vs +0.08% in July). This took QTD growth to -2.51% YoY, although that is an improvement from -3.26% in 2Q19. All investment categories fell for the first time since February 2017. The sub-categories which reversed from positive to negative growth were imports of capital goods (-8.78% August vs +8.07% July) and new motor vehicle registrations (-8.23% vs +5.23%). Machinery purchases and the construction permit index continued to decline.
- Household income indicators were mixed in August: farm income slowed for the sixth month to +0.4% YoY; non-farm wage growth eased to +2.2% YoY (from 2.3%). Sentiment survey data were weak in September: business sentiment slipped deeper below the threshold of 50 that separates improvement from deterioration; consumer confidence marked a 3-year low.

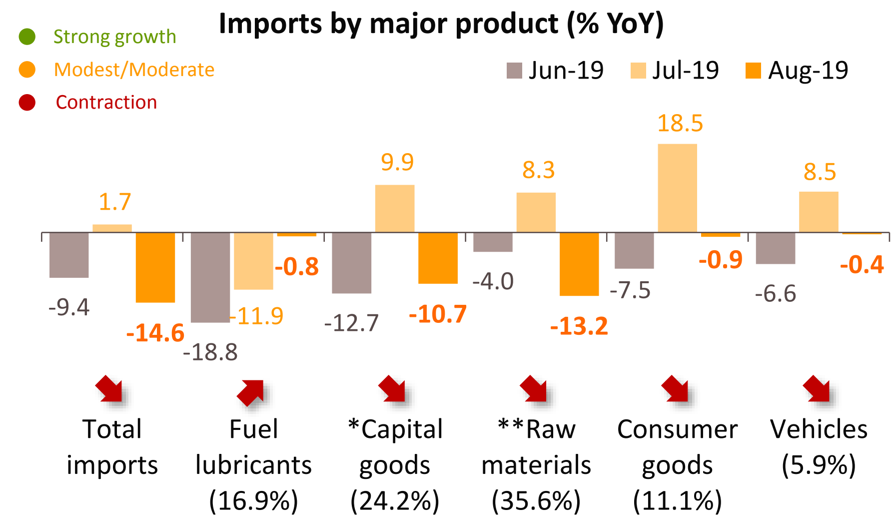




Source: BOT, National Statistical Office (NSO), Office of Agricultural Economics (OAE), University of the Thai Chamber of Commerce (UTCC), Krungsri Research

Industrial recession is deepening; imports saw broad-based contraction





Note: ( ) share in 2018 * Capital goods exclude aircraft, ship ** Raw materials exclude gold

Manufacturing Production: Top 10 industries

Manufacturing Production (% YoY) *	Weight	2018												2019							
		J	F	M	A	M	J	J	A	S	O	N	D	J	F	M	A	M	J	J	A
All industry	100.0%																				
Food & Beverages	19.9%																				
Automotive	13.9%																				
Petroleum	9.6%																				
Chemicals	9.2%																				
Rubbers & Plastics	8.9%																				
Cement & Construction	5.5%																				
IC & Semiconductors	5.5%																				
Electrical Appliances	3.8%																				
Textiles & Apparels	3.5%																				
HDD	3.4%																				

** Green > 0%, Red < 0% / Darker green (red) indicates stronger (weaker) momentum*

Source: Office of Industrial Economics (OIE), MOC, Krungsri Research

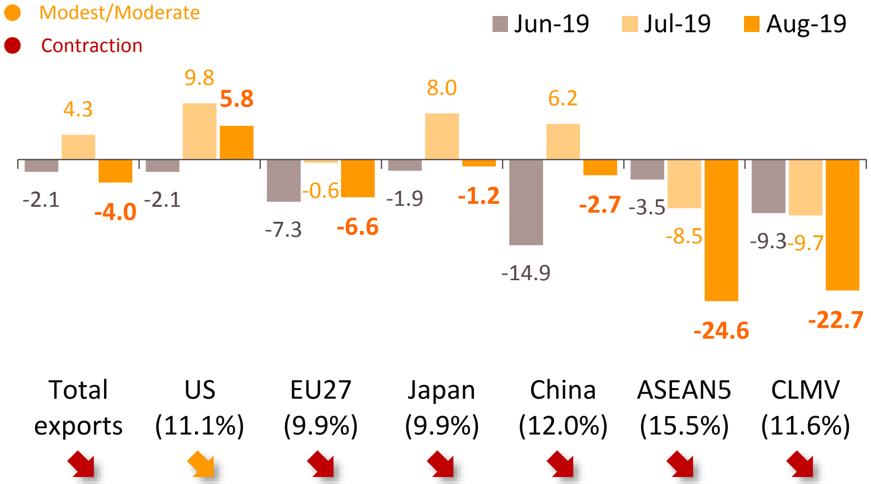
Krungsri Research's view

- The Manufacturing Production Index slid for the fourth month, by 4.4% YoY, after slipping 3.3% in July. Out of 10 major sectors, only three industries avoided an output recession in the month. HDD industry was surprisingly strong with output rising 12.7% YoY, snapping an 11-month streak of recession. However, that might have been because of restocking activity after a long period of contraction, instead of a fundamental recovery. Two sectors exhibited mild growth – Food & Beverage and Chemicals. Production in other major industries contracted. Seasonally-adjusted Capacity Utilization edged down to 66.52% from 66.74% in July.
- August imports slumped 14.6% YoY, the largest drop since April 2016. It is below the weakest Bloomberg survey data (-13.7%), and caused trade surplus to widen markedly to USD2,053m from USD110m in July.

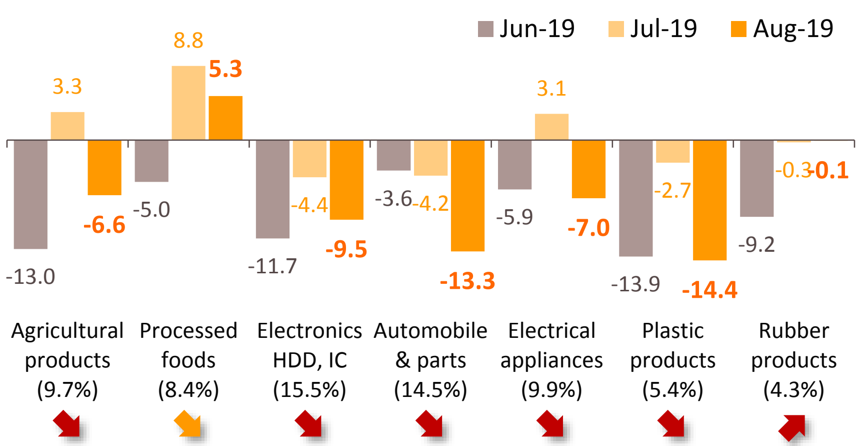
Exports weakened again in August after surprise growth in July; we keep 2019 export growth forecast at -1.6%

Strong growth
Modest/Moderate
Contraction

Exports by major destination (% YoY)



Exports by major product (% YoY)



Note: ( ) share in 2018

Source: MOC, Krungsri Research

Krungsri Research's view

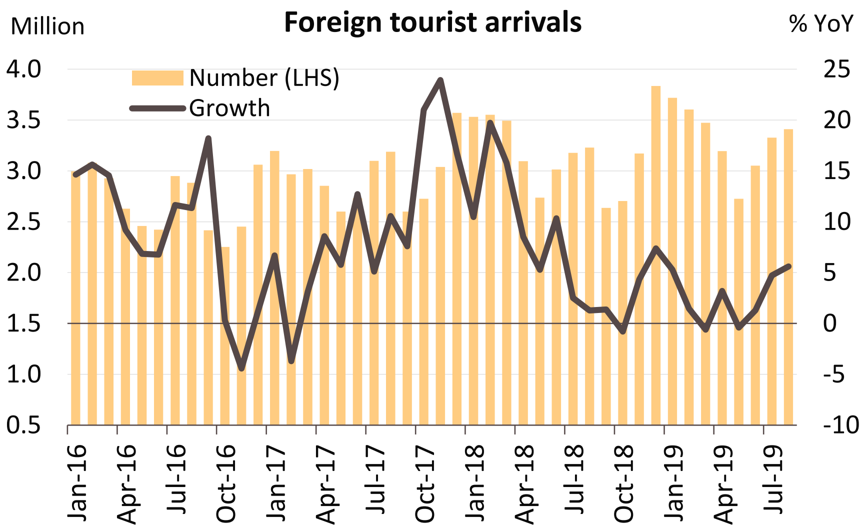
Exports plunged in August for almost all products and destinations

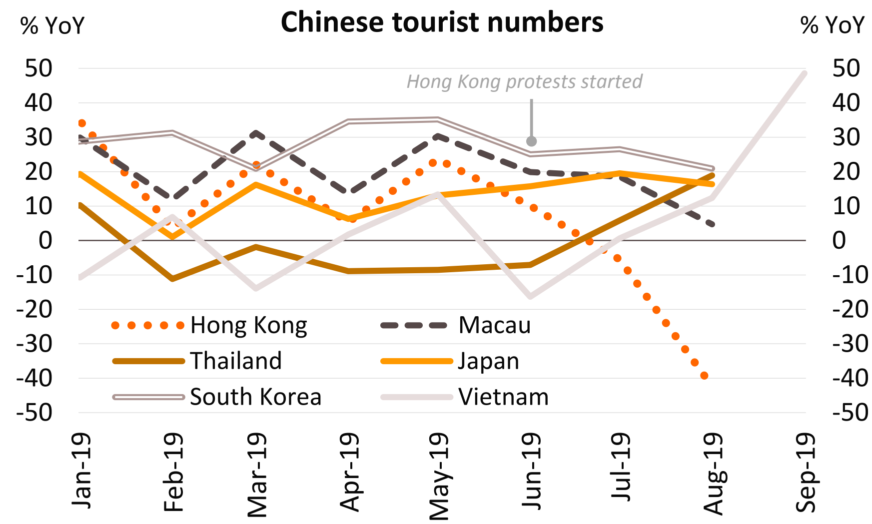
- Merchandise exports slipped back to negative growth again at -4.0% YoY in August, after the surprise surge in July (+4.3%). August reading was weaker than our and market expectations (-2.2% and -2.0%, respectively). Excluding gold, exports saw a steeper decline, at -9.8% YoY vs -0.4% in July, marking the sixth consecutive month of contraction. Exports tumbled for almost all products and destinations, except for processed foods (+5.3% YoY) and shipments to the US (+5.8%) and the Middle East (+5.3%).
- By product, oil-related products (-40% YoY) led the drop, followed by chemical products (-22.3%). Exports of other major manufacturing products shrank considerably but rubber products remained resilient with flat growth. By destination, there was a substantial drop in shipments to ASEAN5 (-23.9%), CLMV (-22.7%) and India (-18%), which accounted for 31.5% of total export value in 2018. The common export products that registered contraction in the three regions is vehicles and auto parts. Exports to China (-2.6% YoY) and shipments to some countries linked to China's supply chains fared better than the headline data: Japan (-1.2% YoY), and Taiwan (+4.7%).

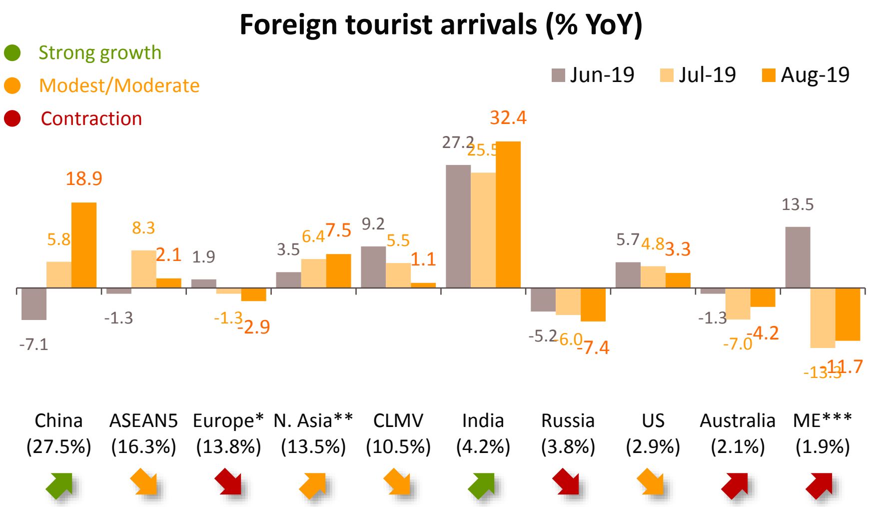
Positive impact of trade diversion is gaining momentum; we keep 2019 export growth forecast at -1.6%

- Strong July trade data and subsequent weak August reading support our view that domestic demand and exports will not recover so soon. Looking ahead, even if lingering trade tensions and a global downturn continue to dim the export outlook, there is more visible positive impact from trade diversion which has been gathering momentum, as suggested by the continued strength in exports of processed foods and rubber products, as well as shipments to the US. Coupled with a favorable low base, we continue to expect smaller negative growth the rest of the year and maintain 2019 export growth forecast at -1.6%.

Thailand is reaping windfall from Hong Kong protests as tourist arrivals from China rise







Note: ( ) share in 2018 * Europe excludes Russia ** North Asia excludes China *** Middle East

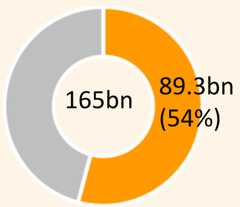
Source: Ministry of Tourism and Sports (MOTS), Krungsri Research

Krungsri Research's view

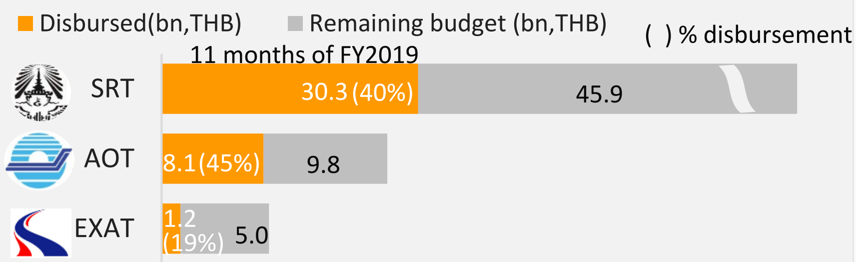
- Foreign tourist arrivals continued to rise by 7.4% YoY, the strongest in eight months, to 3.466 million in August. There was a strong recovery in arrivals from China, which surged 18.9% YoY to surpass 1 million for the first time in historical August data. Thailand is benefitting from the extended protests in Hong Kong, which suffered a sharp drop in Chinese arrivals (-42.3% YoY in August). This trend is likely to continue as turmoil continues to escalate.
- Inbound tourist numbers from India jumped 32.4% YoY, taking YTD growth to +25.4%. Strong growth in arrivals from these markets offset the continued drop in tourist numbers from Russia, Australia, the Middle East, and Europe.

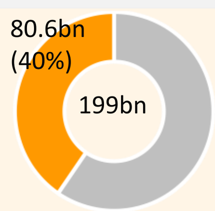
State enterprises' investments in key projects have been delayed, dashing hopes of a boost to economic growth

State enterprises' investment budget and disbursement rate (as of August 2019)

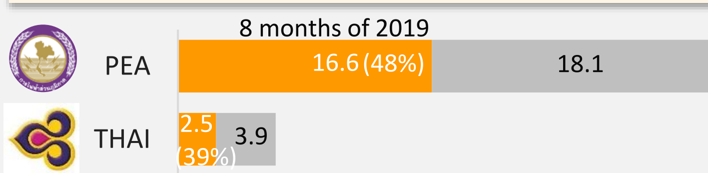


In **the first 11 months of FY2019** (October 2018-August 2019), investments by 34 state enterprises which accounting period is based on the fiscal year totaled THB89.3bn, accounting for **only 54% of total capital budget for the whole fiscal year.**





For the remaining 11 state enterprises which accounting period is based on calendar year, investments in **the first 8 months of 2019** (January-August 2019) totaled THB80.6bn, accounting for **40% of total capital budget for the whole calendar year.**



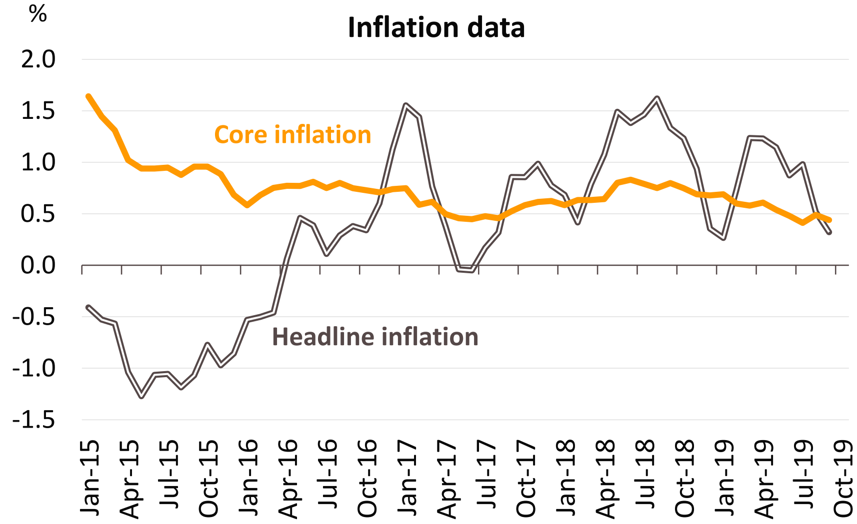
Source: State Enterprise Policy Office (SEPO), Local Press, Krungsri Research

Krungsri Research's view

- State enterprises' mega investments – the main catalyst to boost the economy -- have been delayed with budget disbursements at less than 50% (as of August 2019) by many state enterprises, led by State Railway of Thailand (SRT), Airports of Thailand (AOT), Expressway Authority of Thailand (EXAT), Provincial Electricity Authority (PEA) and Thai Airways (THAI).
- Main reasons for the postponed investments include resignation and reshuffle of board members in several state enterprises, delays in land expropriation, and new public procurement regulations. These obstacles will take time to be resolved, suggesting state enterprises' investments might not be strong enough in the near future to create crowding-in effect or support overall economic growth.

State enterprises	Big-ticket projects that missed budget disbursement plans
• State Railway of Thailand (SRT)	Thai-Chinese high-speed railway: Bangkok–Nakhon Ratchasima
• Airports of Thailand (AOT)	Suvarnabhumi Airport development project
• Expressway Authority of Thailand (EXAT)	Rama III-Dao Khanong- Western Outer Ring Road expressway project
• Provincial Electricity Authority (PEA)	Transmission and distribution system development project (Phase I)
• Thai Airways (THAI)	Aircraft Maintenance Plan (D-Check)

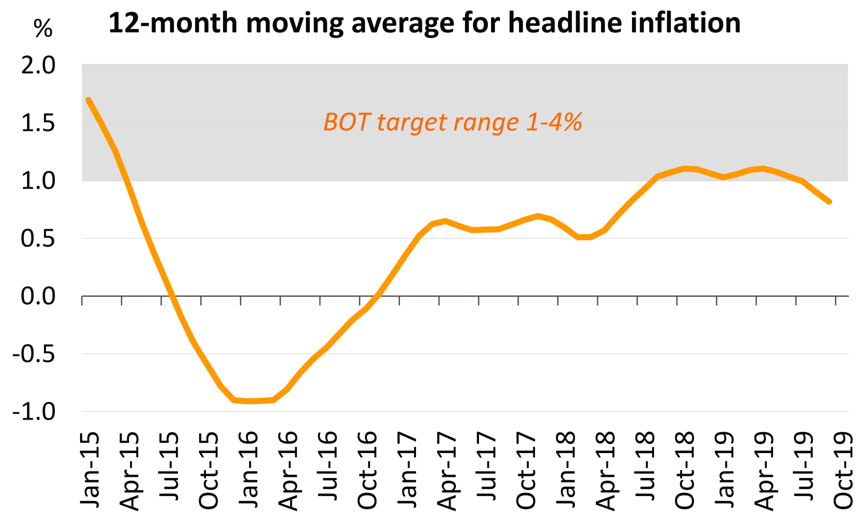
Disinflation continued in September because of Non-Food deflation, taking annual inflation deeper below target



Consumer Price Index: major categories

Consumer Price Index (% YoY)*	Weight	2018												2019								
		J	F	M	A	M	J	J	A	S	O	N	D	J	F	M	A	M	J	J	A	S
Headline CPI	**100.00%**																					
Food & Beverages	36.13%																					
Apparel & Footwear	2.88%																					
Housing & Furnishing	23.25%																					
Medical & Personal care	6.22%																					
Transportation & Communication	24.02%																					
Recreation & Education	6.13%																					
Tobacco & Alcoholic beverages	1.38%																					
Prepared food	17.02%																					
Raw food	15.69%																					
Energy	11.75%																					
Core CPI	**72.56%**																					

** Green > 0%, Red < 0% / Darker green (red) indicates stronger (weaker) momentum*



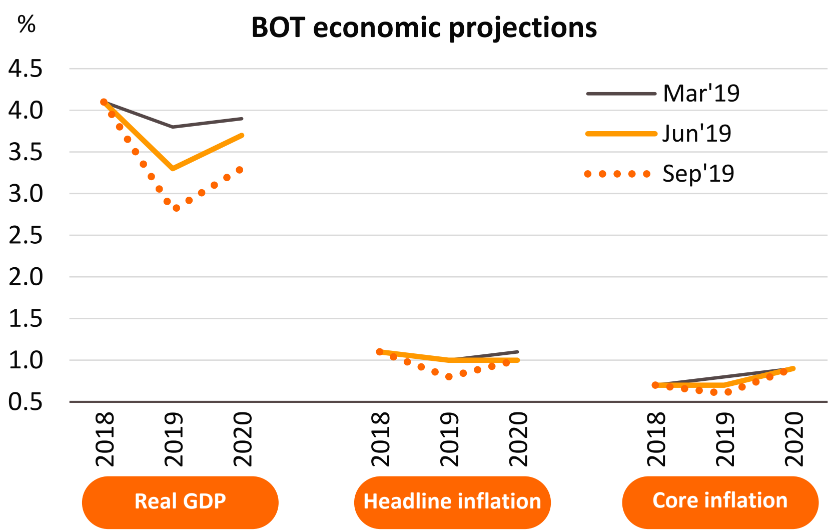
Source: MOC, Krungsri Research

Krungsri Research's view

- Headline inflation inched down to +0.32% in September (vs +0.52% in August), taking 12-month moving average deeper below target range for the third month. September reading missed our expectation (+0.42%) and median consensus estimate (+0.41%).
- Prices for Non-Food & Beverage categories continued to slip for the fourth month, by 0.90% YoY, the slowest rate since June 2016. This was primarily due to Energy deflation (-6.39% YoY vs -5.16% in August), which led to a steeper decline in the price of Transportation & Communication (-2.86% YoY vs -2.22% in August). A slower rise in Food & Beverage inflation (+2.47% YoY vs +2.63% in August) added to the downside.
- Despite the upside surprise, core inflation eased further to +0.44% (+0.49% in August), compared to our and market expectations of +0.41%. This was largely driven by lower price for Prepared Food (+0.59% YoY vs +0.97% in August), which shaved 0.09ppt off core inflation (September reading compared to August data). But after adjusting for seasonal effect, core CPI rose for the second month, by 0.04% MoM (vs +0.09% in August).

Third consecutive downgrade by the BOT

BOT Forecasts		2019F			2020F		
		Previous	Latest		Previous	Latest	
GDP growth	YoY (%)	3.3	2.8	▼	3.7	3.3	▼
Private Consumption Expenditure	YoY (%)	3.8	3.8	=	3.4	3.1	▼
Government Consumption Expenditure	YoY (%)	2.2	2.3	▲	2.6	3.4	▲
Private Investment	YoY (%)	3.8	3.0	▼	5.5	4.8	▼
Public Investment	YoY (%)	3.8	2.5	▼	7.2	6.3	▼
Nominal Exports in USD (f.o.b.)	YoY (%)	0.0	-1.0	▼	4.3	1.7	▼
Nominal Imports in USD (f.o.b.)	YoY (%)	-0.3	-3.6	▼	4.8	3.5	▼
Current Account Balance	USD, bn	29.1	34.2	▲	26.3	30.4	▲
Tourist Arrivals	persons, m	39.9	39.7	▼	41.3	41.2	▼
Headline Inflation	YoY (%)	1.0	0.8	▼	1.0	1.0	=
Core Inflation	YoY (%)	0.7	0.6	▼	0.9	0.9	=
Dubai crude price - period average	USD/bbl	65.9	64.0	▼	65.0	63.0	▼



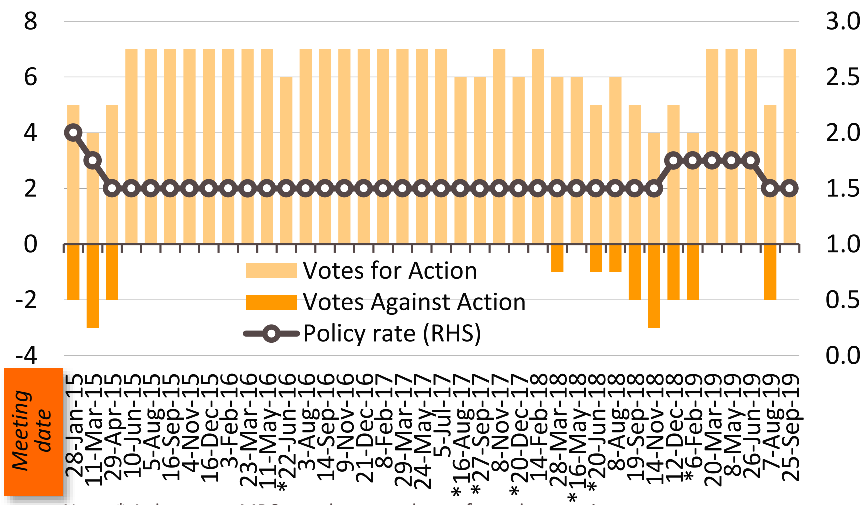
Source: BOT, Krungsri Research

Krungsri Research's view

- The BOT slashed growth outlook again, reducing 2019 GDP growth from +3.3% to +2.8% and 2020 growth from +3.7% to +3.3%. The downgrade was broad-based with all economic activity variables noting a weaker footing.
- The statement also included a reference to weaker exports and slower consumption growth, noting *"a prolonged downturn in the electronic cycle"* as the source of weakness in the former, and *"impacts from natural disasters"* added to downside for the latter. The inflation assessment was unchanged, with annual headline inflation projected to slip below target range and expectations of subdued core inflation in the absence of demand-pull pressure.

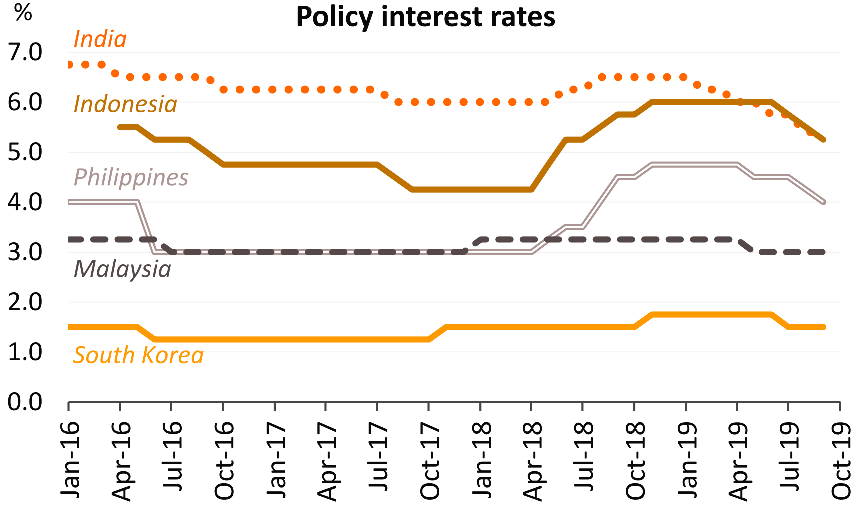
BOT keeps rates; weaker growth outlook, stronger forward guidance support another 25bps cut before year-end

MPC policy rate decisions



Note: * At least one MPC member was absent from the meeting

Policy interest rates



Source: BOT, National Central Banks, Bloomberg, Krungsri Research

Krungsri Research's view

MPC unanimous in keeping rates

- After a surprise 25bps cut at the previous meeting, the Bank of Thailand's Monetary Policy Committee (MPC) voted unanimously to keep policy rate at 1.50%. While the decision is in line with Bloomberg consensus survey (21 out of 29 forecast MPC would hold rate, including Krungsri Research), the voting result was more hawkish than we expected.

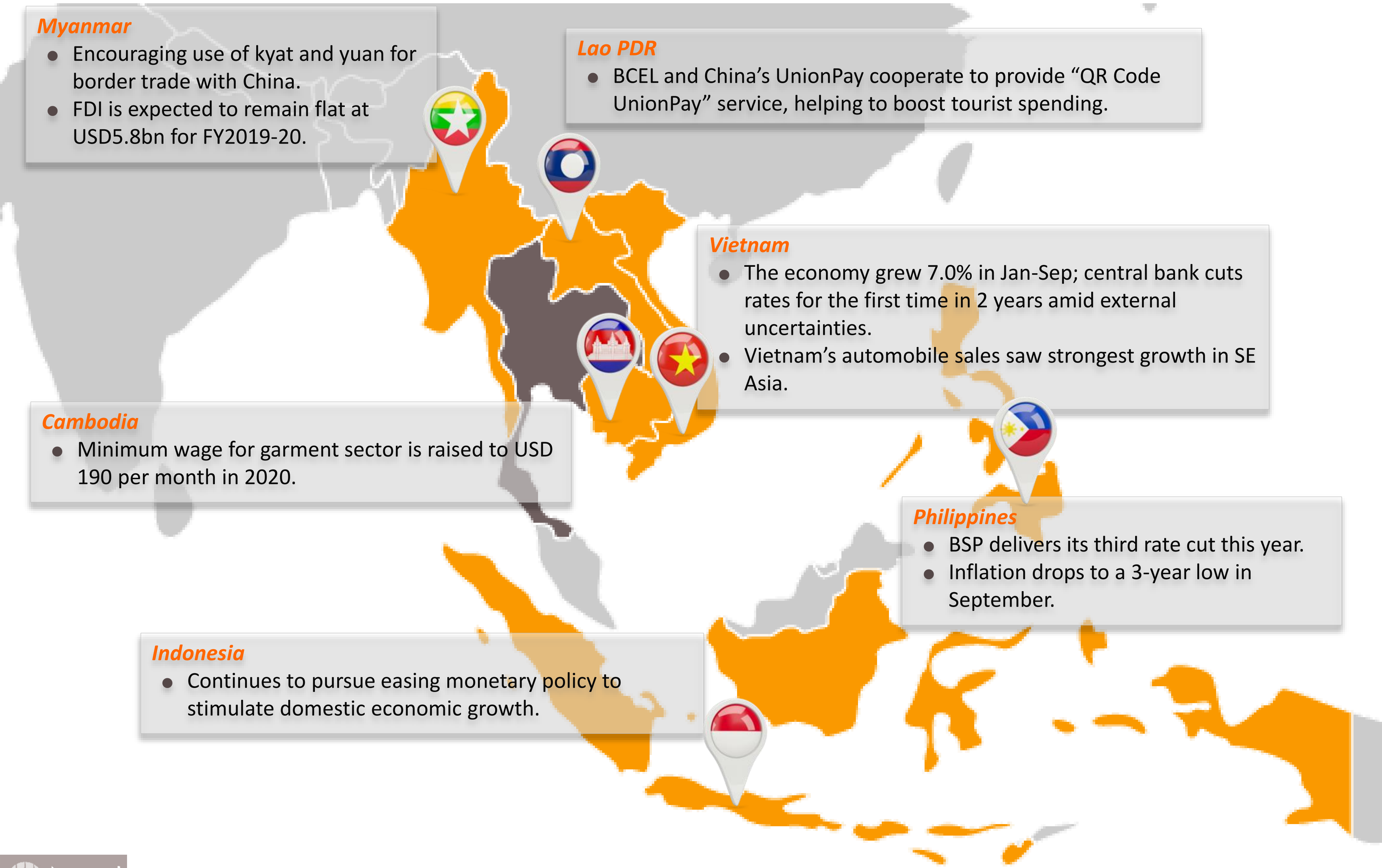
MPC pledges to stand ready to use policy tools if needed

- In the forward guidance, the accompanying statement keeps the following narrative: (i) the committee would continue to *"closely monitor"* developments in all economic variables and risks when deliberating future monetary policy; and (ii) the economy would continue to *"face structural problems"* that cannot only be addressed by monetary policy. The only addition to the guidance was that the MPC would *"stand ready to use policy tools as appropriate"*, that is a step up from the previous meeting's statement.

Weaker economic tone along with stronger forward guidance support our view of another 25bps cut before year-end

- The BOT sounded more bearish in its outlook for the economy and has strengthened forward guidance even as it kept rates steady, suggesting another rate cut is possible before year-end. As such, we continue to expect the next 25bps rate cut in November. This is premised on the following: (i) 3Q19 GDP data is likely to remain sluggish; (ii) fiscal impetus could have only a marginal impact, which could prompt the BOT to introduce additional insurance; (iii) strong peer pressure as several other central banks – notably the Bank of Korea – continue to pursue monetary easing towards the end of the year.

Regional Economic and Policy Developments in October 2019



Myanmar
- Encouraging use of kyat and yuan for border trade with China.
- FDI is expected to remain flat at USD5.8bn for FY2019-20.

Lao PDR
- BCEL and China's UnionPay cooperate to provide "QR Code UnionPay" service, helping to boost tourist spending.

Vietnam
- The economy grew 7.0% in Jan-Sep; central bank cuts rates for the first time in 2 years amid external uncertainties.
- Vietnam's automobile sales saw strongest growth in SE Asia.

Cambodia
- Minimum wage for garment sector is raised to USD 190 per month in 2020.

Philippines
- BSP delivers its third rate cut this year.
- Inflation drops to a 3-year low in September.

Indonesia
- Continues to pursue easing monetary policy to stimulate domestic economic growth.

ADB cuts GDP growth forecasts for SE Asia to 4.5% (2019) and 4.7% (2020) amid escalating US-China trade tensions

The ADB cut economic growth forecasts for Southeast Asia by 0.4ppt to +4.5% for 2019 and by 0.3ppt to +4.7% for 2020. Forecasts were downgraded for Indonesia, Laos, Philippines, Singapore and Thailand, citing (i) an escalation in US-China trade tensions, (ii) weakening global trade, and (iii) a downturn in global electronic cycle, all of which could drag exports of those countries, which largely rely on external demand. Inflation forecasts are also revised down, except for Laos and Myanmar which face upward pressure in domestic food prices. We expect SE Asian countries to implement accommodative policies to boost their domestic economies, which account for 45%-85% of GDP, to cushion the impact of external headwinds. This year, Indonesia, Malaysia, Philippines, Thailand, and Vietnam have cut policy interest rates to support economic growth.

ADB: GDP Growth Forecast for SE Asian Countries

ADB outlook update	2018	2019F (Old)	*2019F (New)*	2020F (Old)	*2020F (New)*
SE Asia	**5.1**	**4.9**	***4.5***	**5.0**	***4.7***
Brunei	0.1	1.0	*1.0*	1.5	*1.5*
Cambodia	7.5	7.0	*7.0*	6.8	*6.8*
Indonesia	**5.2**	**5.2**	***5.1*** ↓	**5.3**	***5.2*** ↓
Lao PDR	**6.3**	**6.5**	***6.2*** ↓	**6.5**	***6.2*** ↓
Malaysia	4.7	4.5	*4.5*	4.7	*4.7*
Myanmar	6.8	6.6	*6.6*	6.8	*6.8*
Philippines	**6.2**	**6.4**	***6.0*** ↓	**6.4**	***6.2*** ↓
Singapore	**3.1**	**2.6**	***0.7*** ↓	**2.6**	***1.4*** ↓
Thailand	**4.1**	**3.9**	***3.0*** ↓	**3.7**	***3.2*** ↓
Vietnam	7.1	6.8	*6.8*	6.7	*6.7*

ADB: Inflation Forecast for SE Asian Countries

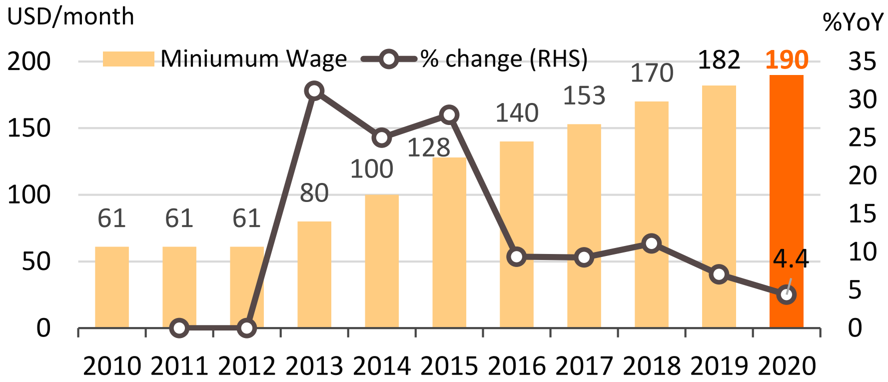
ADB outlook update	2018	2019F (Old)	*2019F (New)*	2020F (Old)	*2020F (New)*
SE Asia	2.7	2.6	*2.3*	2.7	*2.6*
Brunei	0.1	0.2	*0.1*	0.2	*0.2*
Cambodia	2.5	2.5	*2.2*	2.5	*2.5*
Indonesia	3.2	3.2	*3.2*	3.3	*3.3*
Lao PDR	2.0	2.0	*2.3*	2.0	*2.3*
Malaysia	1.0	2.0	*1.0*	2.7	*2.0*
Myanmar	5.9	6.8	*8.0*	7.5	*7.5*
Philippines	5.2	3.8	*2.6*	3.5	*3.0*
Singapore	0.4	0.7	*0.7*	0.9	*0.9*
Thailand	1.1	1.0	*1.0*	1.0	*1.0*
Vietnam	3.5	3.5	*2.0*	3.8	*3.5*

Source: ADB Outlook 2019 Update, Krungsri Research

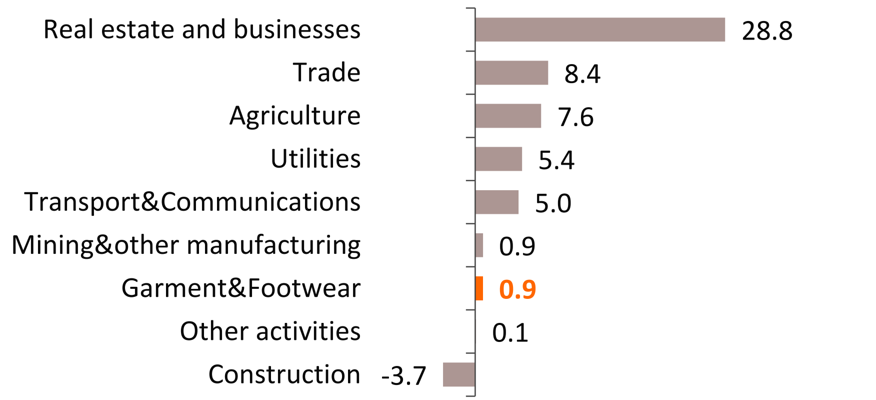
Cambodia: Minimum wage for garment sector is raised to USD190 per month in 2020

The minimum wage for the garment, footwear, and textile (GTF) sector in Cambodia is raised by 4.4% to USD190 per month starting January 2020, from USD182 currently, according to the Ministry of Labor and Vocational Training. There is no change to other allowances, including USD7 for transportation, USD10 for accommodation, KHR2,000 (USD0.50) for meals, and a seniority bonus of USD2 to USD11. These would take the average salary for GTF workers to between USD207 and USD218 per month next year.

Cambodia: Official minimum wage for the garment sector

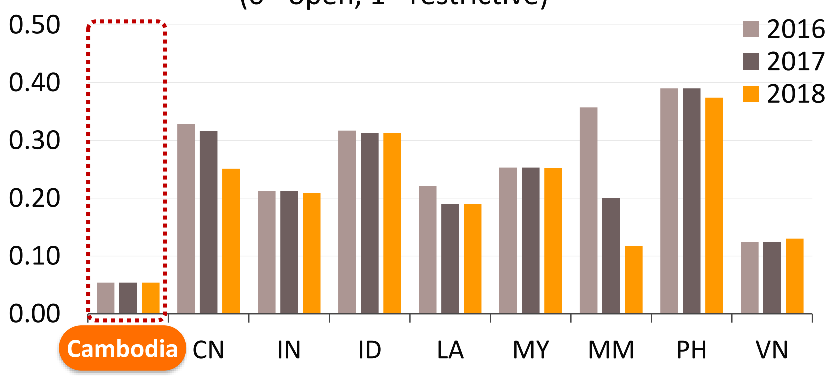


Cambodia: Annual productivity growth (2007-14) in key sectors (%)



OECD: FDI Regulatory Restrictiveness Index

(0= open, 1= restrictive)



Note: KH =Cambodia, CH = China, IN = India, ID = Indonesia, LA = Lao PDR, MY = Malaysia, MM = Myanmar, PH = Philippines, VN = Vietnam

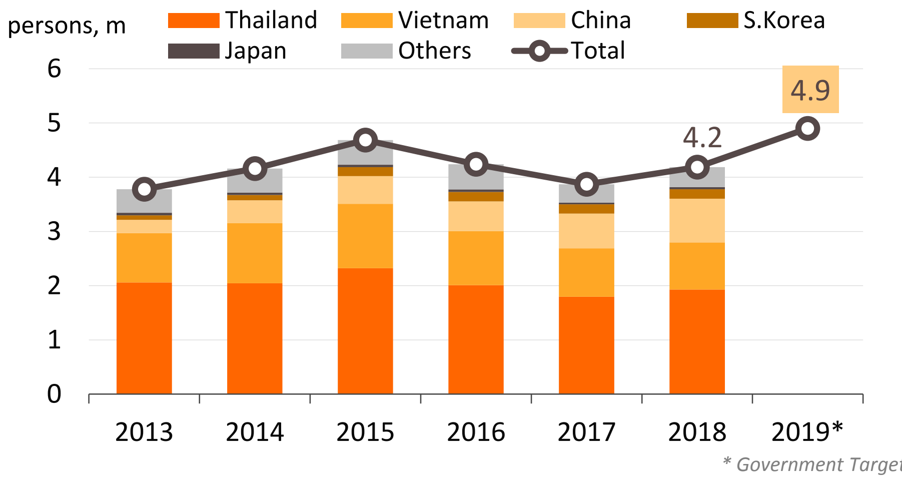
Source: OECD, World Bank's Cambodia Economic Updates, Krungsri Research

Krungsri Research's view

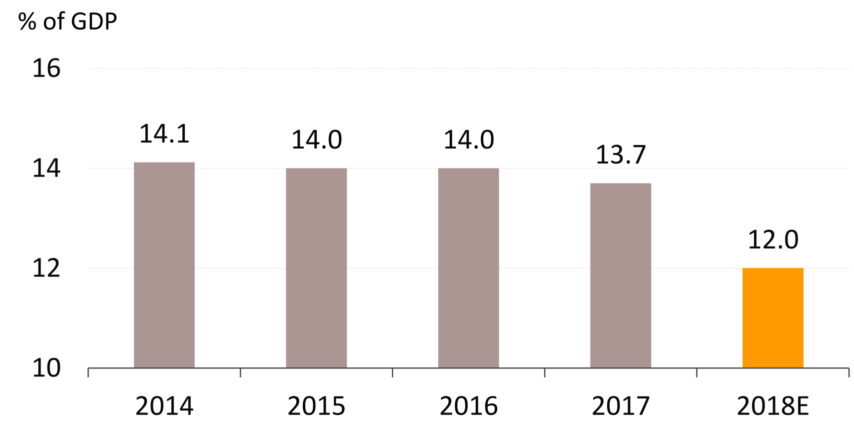
- Rising wages in the GFT sector- the only manufacturing sector with minimum wage regulation and the largest manufacturing sector in the country - would reduce the sector's competitiveness and make it less attractive for foreign investors. This is because the raise is not in line with productivity growth, and measures announced by the authorities in March are insufficient to weather headwinds in the sector, including potential loss of tariff-free access to the EU market. While minimum wage will continue to rise going forward, it is a part of the political agenda. Cambodia needs structural reforms to improve its competitiveness and diversify its economic structure.
- However, we believe Cambodia's openness and relatively mild restrictions for foreign investment and cross-border fund flows, coupled with generous tax incentives, should offset the effects of higher minimum wages and keep Cambodia attractive to foreign investors.

Lao PDR: BCEL and China's UnionPay cooperate to provide "QR Code UnionPay" service, will boost tourist spending

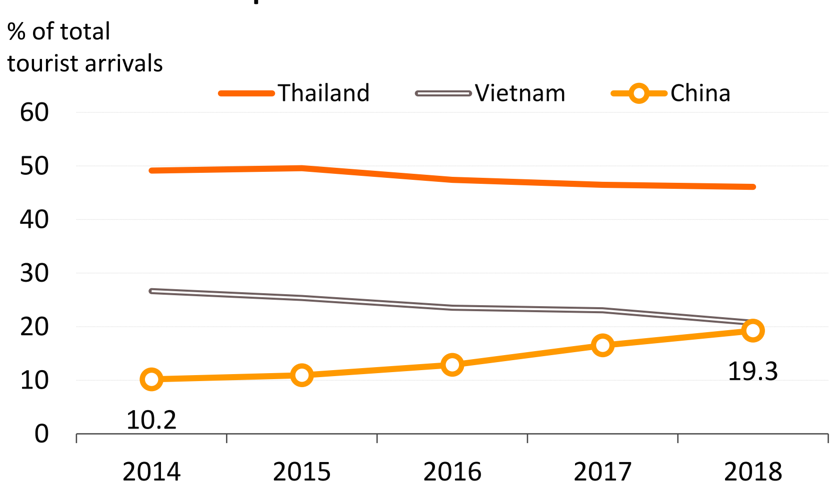
Tourist arrivals in Laos



Laos: Tourism Revenue



Top 3 tourist sources in Laos



Krungsri Research's view

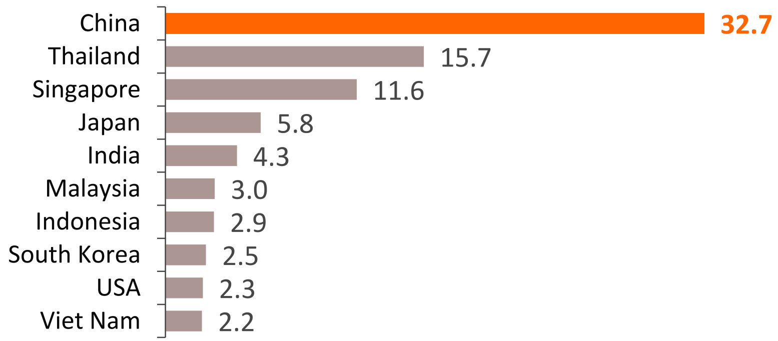
- In September 2019, Banque pour le Commerce Lao Public (BCEL) in cooperation with UnionPay International (UPI), started to provide digital payment service through "QR Code UnionPay". This is likely another step by Laos to develop its financial technology (Fintech) industry. The new payment service will enable instant financial transactions between Laos and China, with easier, faster, safer, and low-cost transactions.
- The payment service is expected to help boost spending in Laos, mainly tourist spending in the future. This payment service would complement other policies promoting "Visit Laos-China Year 2019" to attract more Chinese tourists – the third largest source of tourist arrivals which accounts for about 20% of total tourist arrivals in Laos. Currently, BCEL has more than 10,000 member shops across the country and UnionPay is one of the most popular mobile payment applications in China with about 150 million users. The service is expected to boost tourist spending in Laos.

Source: Laos Tourism Statistics, Ministry of Information, Culture and Tourism, World Travel & Tourism Council, CEIC, Krungsri Research

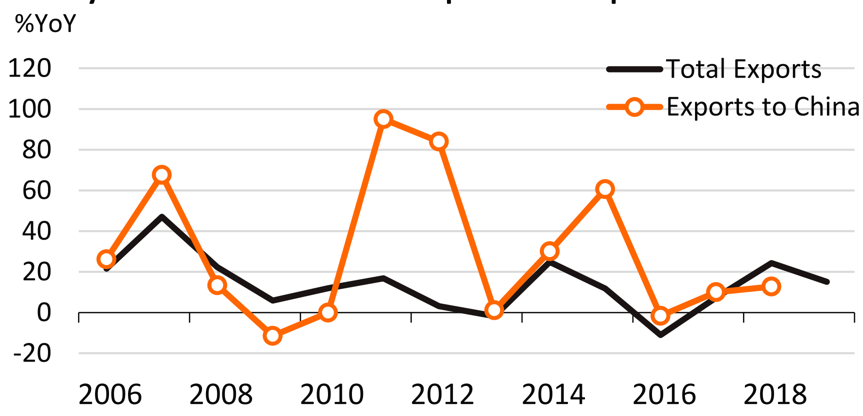
Myanmar: Encouraging kyat and yuan usage for border trade with China

Myanmar wants to promote the use of kyat and yuan for Myanmar-China border trade to help eliminate foreign exchange risks, reduce transaction costs, and facilitate bilateral trade as China is currently Myanmar's main border trade partner. In addition, it would be more efficient and economical to use local currencies for trade settlements instead of a third currency such as the USD, according to U Ye Min Aung, Vice Chair of the Union of Myanmar Federation of Chambers of Commerce and Industry (UMFCCI). The promotion of local currency usage is supported by the Industrial and Commercial Bank of China Limited (ICBC). The Central Bank of Myanmar (CBM) officially allowed Japanese yen and Chinese yuan as settlement options for cross-border payments and settlements in January 2019, in addition to USD, EUR, SGD.

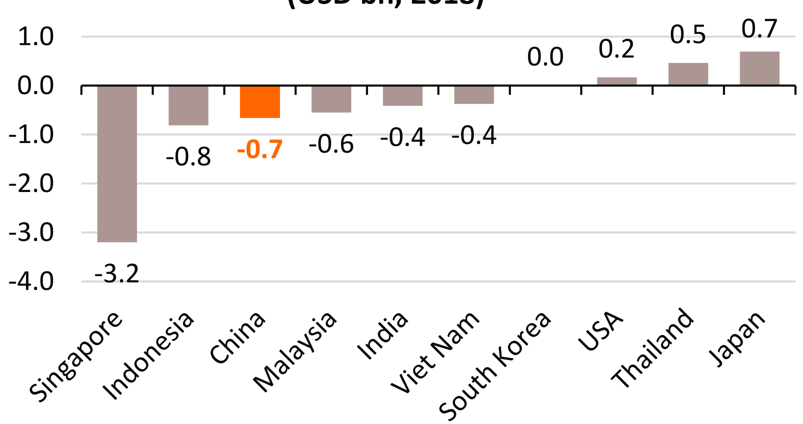
Myanmar: Major trading partners by share of total trade value (%, as of 2018)



Myanmar: Growth of total exports and exports to China



Myanmar: Trade balance with major trading partners (USD bn, 2018)



Source: Trade map, CEIC, Krungsri Research

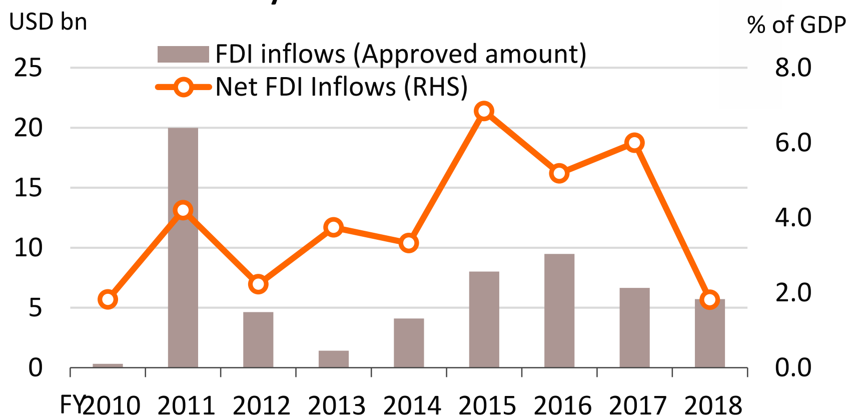
Krungsri Research's view

- While the use of kyat and yuan for cross-border trade settlements has potential to facilitate bilateral trade and make it more cost-efficient for exporters and importers, those advantages might not be realized so soon because the soft and hard infrastructure for cross-border payments is not fully in place. Currently, only banks are allowed to conduct yuan-denominated transactions against a backdrop of an illiquid yuan market in Myanmar as individuals and businesses have not been allowed to open yuan-denominated accounts. In addition, there are currently no bilateral liquidity backstop agreements through swap agreements between the two countries, while Myanmar running a trade deficit with China is preventing Myanmar from accumulating yuan supply.

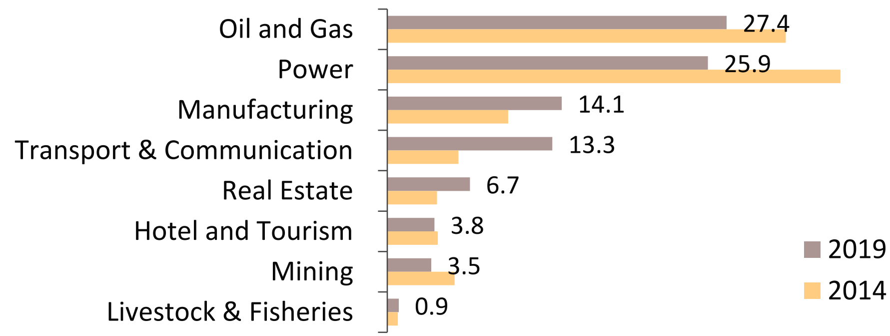
FDI is expected to remain flat at USD5.8bn for FY2019-20

The Directorate of Investment and Company Administration (DICA) expects Foreign Direct Investments (FDI) to reach USD5.8bn in 2019-20 fiscal year (FY), the same forecast for the last FY. Myanmar received only USD4.5bn in FDI for 285 projects in FY2018-19, which was below the official target, according to U Thant Sin Lwin, Director General of DICA. However, for the current FY, the authorities expect more investments to flow into the manufacturing sector because of attractive investment incentives and ongoing structural reforms.

Myanmar: FDI inflows



Share of Total Cumulative FDI by sector (% of Approved Amount as of September 2019)



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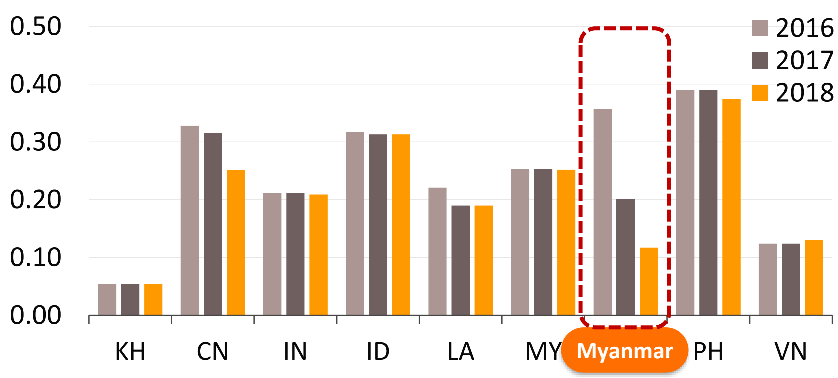


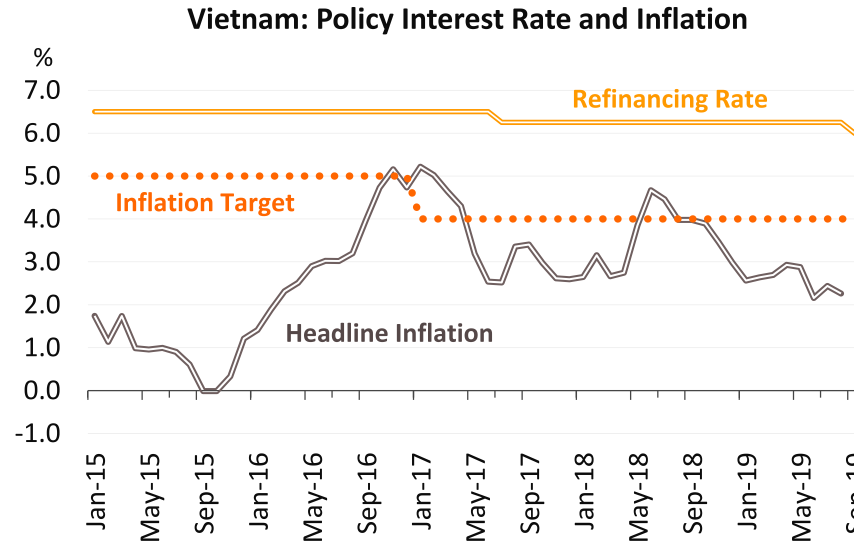
Note: KH =Cambodia, CH = China, IN = India, ID = Indonesia, LA = Lao PDR, MY = Malaysia, MM = Myanmar, PH = Philippines, VN = Vietnam

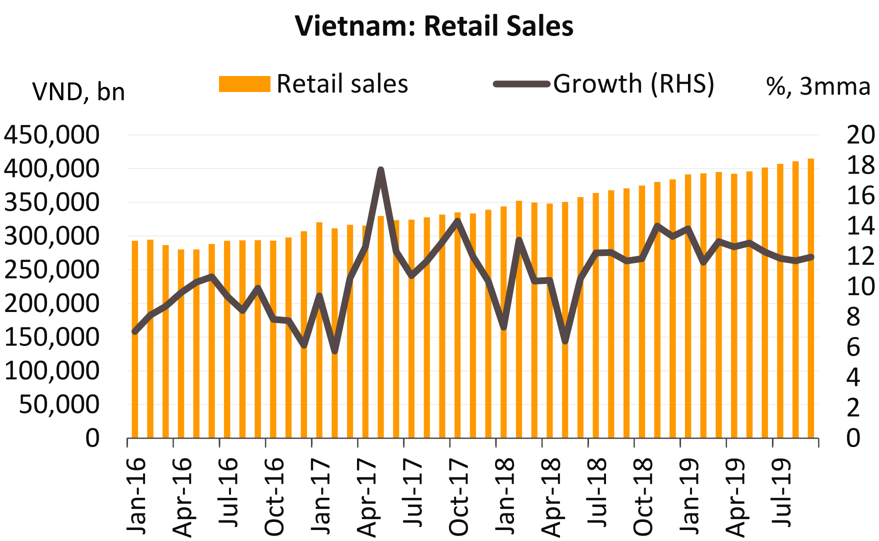
Source: Trade map, OECD, CEIC, Krungsri Research

Krungsri Research's view

- There are positive developments to attract more FDI in FY2019-20. These are (1) ongoing structural reforms, (2) streamlining of foreign investment approval processes, (3) relocation of labour-intensive production out of China, due in part to the re-escalation of global trade tensions. In addition, Myanmar has been successful in facilitating FDI inflows, and there are untapped investment opportunities in several sectors such as manufacturing, tourism, and agriculture.
- However, we view it would be challenging to meet the FDI target because of lingering downside risks, especially the upcoming 2020 general election and unrest in some parts of the country. Although we expect the National League for Democracy (NLD) led by State Counsellor Aung San Suu Kyi to be re-elected, there is still a degree of political uncertainty because of the ongoing constitution amendment efforts. This might delay foreign investment. In addition, there is fear unrest in some regions could disrupt construction of investment projects under the Belt and Road Initiative (BRI).

Vietnam: Economy grew 7.0% in Jan-Sep; central bank cuts rates for first time in 2 years amid external uncertainties



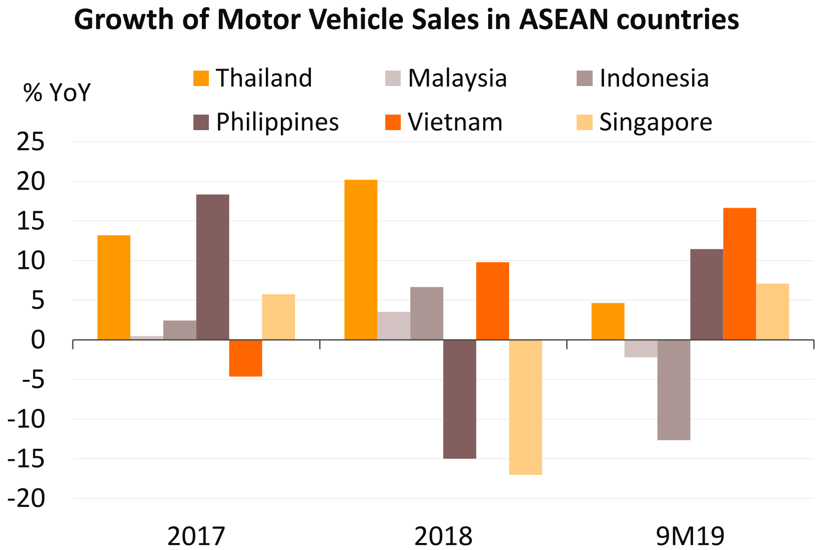


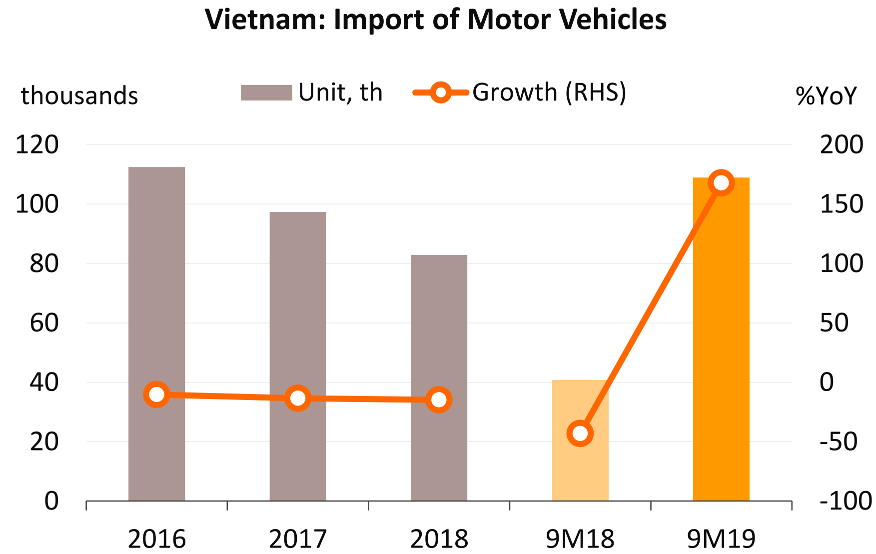
Source: The General Statistics Office, CEIC, Krungsri Research

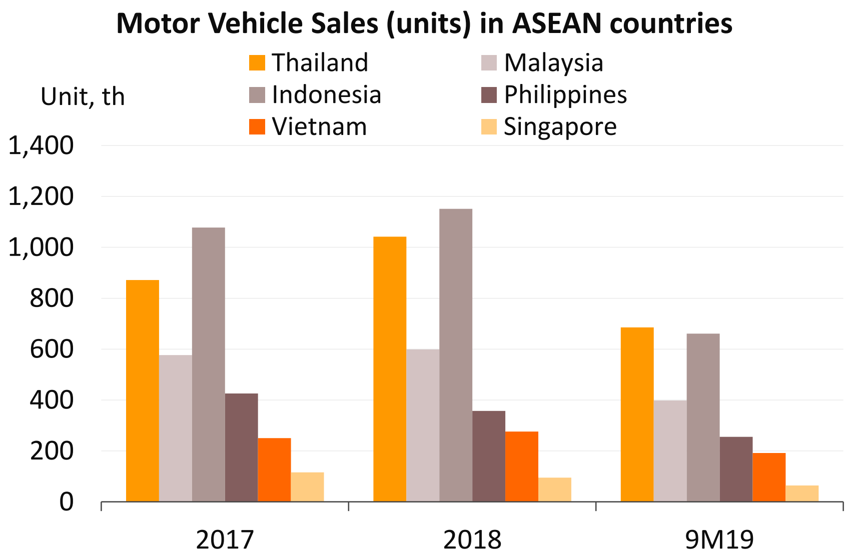
Krungsri Research's view

- Vietnam's economy expanded 7.3% YoY in 3Q19, the strongest growth in three quarters. In the nine months to September 2019, the economy expanded 7.0%.
- In addition, the central bank recently cut policy interest rate by 25bps to 6.0%, the first cut since October 2017. This would reduce cost of funds, increase liquidity, and support growth in consumption and investment—which together account for around 100% of GDP.
- For the rest of the year, the economy will face challenges from a high-base GDP growth rate and rising external pressures from slowing global trade and the US-China trade war. However, Vietnam has resilient domestic demand and authorities have helped to support demand by cutting key interest rates. Hence, we forecast Vietnam's economic growth at 6.6-6.8% for this year.

Vietnam's auto sales saw strongest growth in SE Asia







Source: CEIC, Krungsri Research

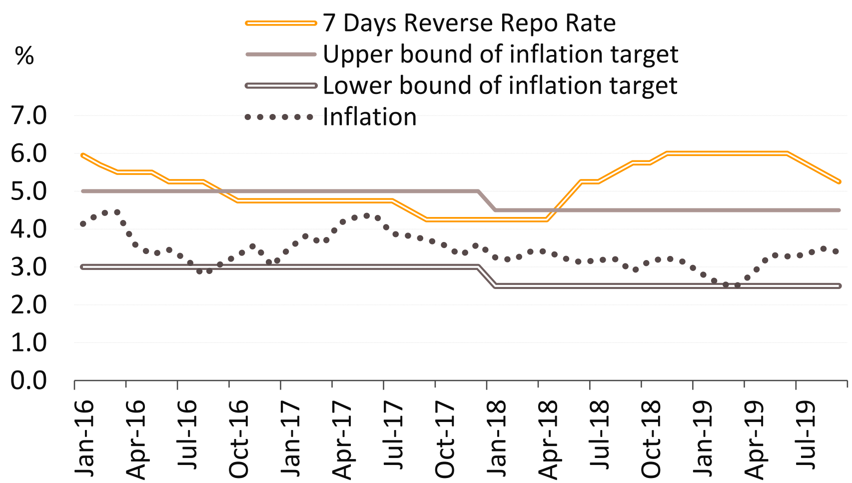
Krungsri Research's view

- Vietnam's automobile sales continued to register solid growth, and is the strongest among ASEAN countries in the first 9 months of 2019. This is supported by the supply side with the exemption in import tariff for motor vehicles from ASEAN, as well as demand side on the back rising demand in Vietnam.
- The number of imported motor vehicles surged 168% YoY in the first 9 months of 2019, after contracting 14.8% last year following import restrictions for vehicles effective January 2018. The robust imports of vehicles this year is simply because importers and distributors have adjusted to comply with those rules.
- Looking ahead, Vietnam's demand for automobiles should remain strong, supported by encouraging economic growth, a growing middle-income population (currently 13% of population), as well as rising investments in the country, which will need more capital goods including transportation equipment to facilitate business activities.

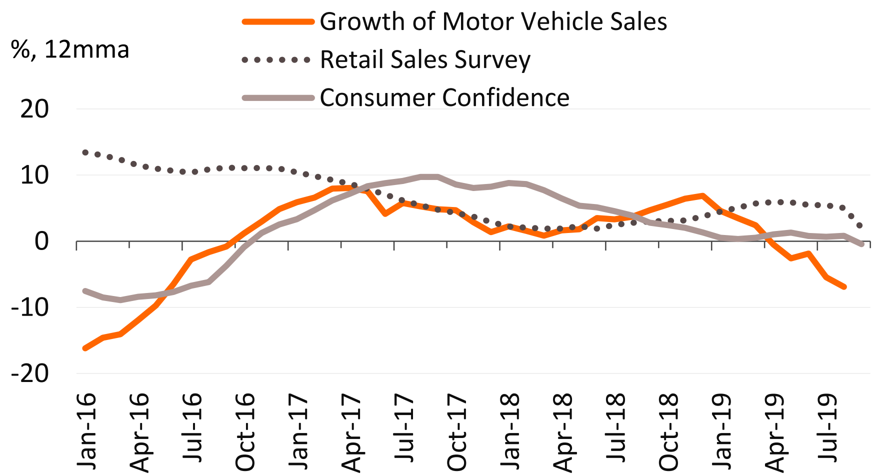
Indonesia: Continued easing monetary policy to stimulate domestic economic growth

Bank Indonesia (BI) has cut key interest rate in September 2019 by 0.25bps to 5.25%, after two 0.25bps rate cuts in July and August. The central bank also relaxed financing rules, including (i) decreasing loan-to-value (LTV) and financing-to-value (FTV) ratios for property loans/financing by 5%; and (ii) reducing down payments for motor vehicle loans to 5-10% of purchase price. In addition, it also provide additional LTV/FTV relief for green property loans/financing and reduced down payments for loans for environmental-friendly motor vehicles by 5%. The new rules will be effective 2 December 2019.

Indonesia: 7-Day Reverse Repo Rate and Inflation



Indonesia: Growth of Motor Vehicle Sales, Retail Sales and Consumer Confidence



Krungsri Research's view

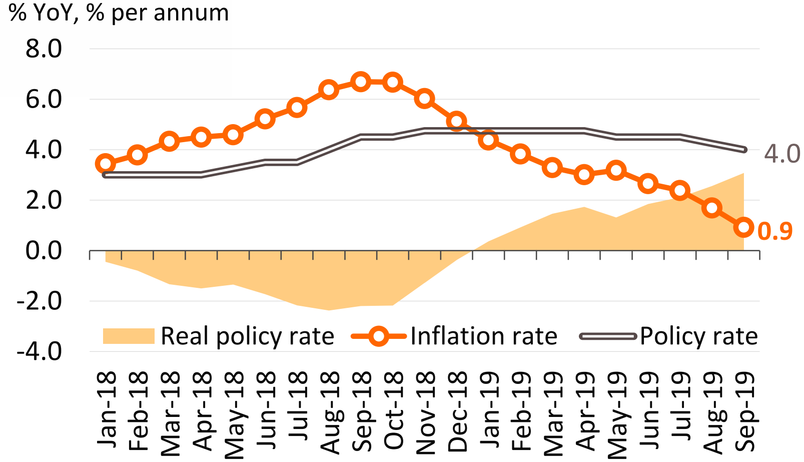
- Bank Indonesia has moved to support economic growth for domestic and external reasons. Domestic demand has weakened, and inflation is low. In addition, there is intensifying external uncertainties, including the global economic slowdown and an escalation in US-China trade war.
- Indonesia's domestic demand has weakened in recent months, reflected by a drop in motor vehicle and retail sales. BI's consumer confidence survey also indicates a declining trend. This suggests it would be more challenging for the authorities to boost the economy, given lackluster domestic consumption, in which private consumption accounts for 57% of GDP. Also, the Ministry of Finance and economists project Indonesia's economy would grow by 5-5.1% this year, which is the lower range of BI's previous target of 5-5.4%.
- Given low projected inflation, sustained external stability, and continued accommodative monetary policies in the US and EU, we expect the BI to cut key interest rates again.

Source: Bank Indonesia (BI), CEIC, Krungsri Research

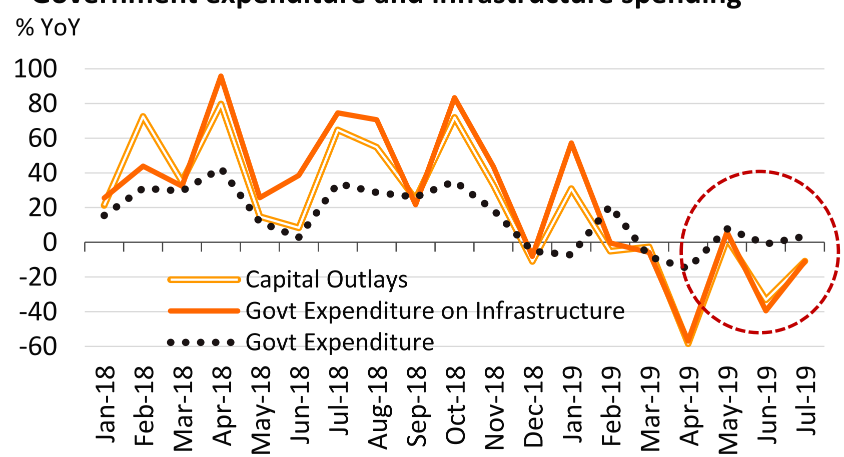
Philippines: BSP delivers its third rate cut this year

On 26 September, the Monetary Board (MB) of the Bangko Sentral ng Pilipinas (BSP) cut policy rate by 25 bps, the third cut this year, to 4.0% amid easing inflationary pressure and a subdued growth outlook. This cut was widely expected because it had been signalled by Governor Benjamin E. Diokno. According to Bloomberg, at the upcoming policy meeting, the BSP will consider policy actions of other central banks as well as domestic economic developments, and Governor Dioko had commented "monetary policy works with lag" and the BSP would remain data-dependent in making its policy decision.

Philippines: Real policy rate and inflation rate



Government expenditure and infrastructure spending



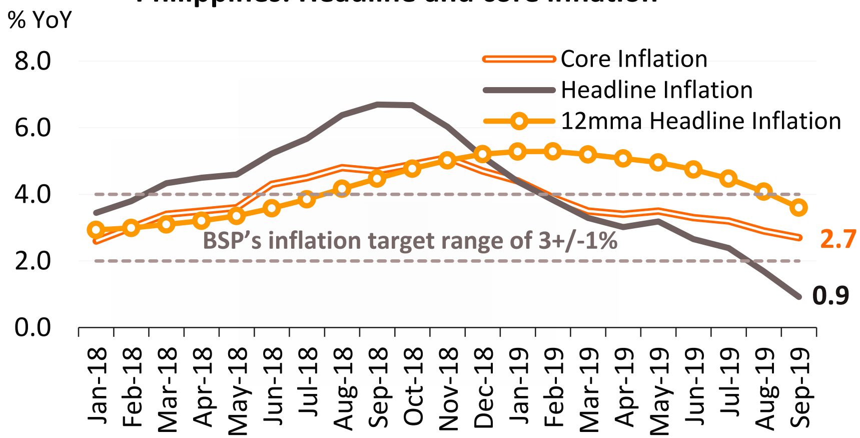
Source: Bangko Sentral ng Pilipinas (BSP), CEIC, Bloomberg, Krungsri Research

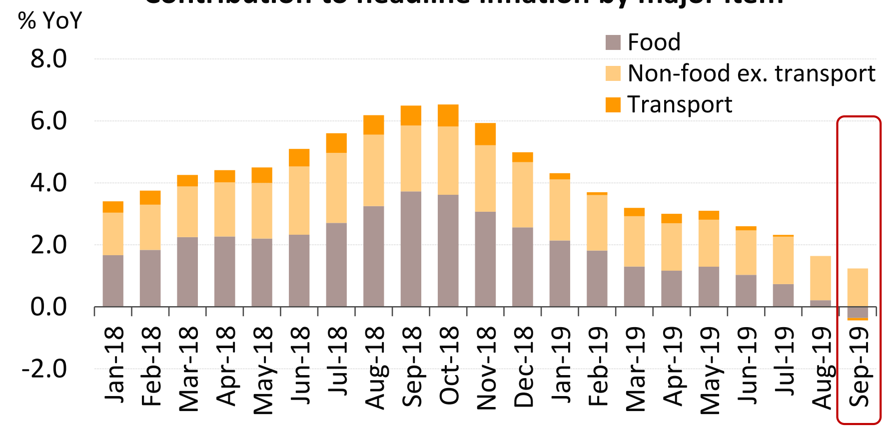
Krungsri Research's view

- The Press Release from the Monetary Board (MB)'s on 26 September wrote "*...the Monetary Board also noted that the balance of risks to the inflation outlook have shifted toward the upside for 2020, while it is seen to tilt to the downside for 2021...the Monetary Board believes that the benign inflation outlook provides room for a further reduction in the policy rate to support economic growth and reinforce market confidence. Going forward, the BSP will continue to monitor emerging price and output developments to ensure that monetary policy settings remain consistent with price stability while being supportive of sustained non-inflationary economic growth over the medium term...".* Premised on this, the BSP is likely to pause its easing cycle the rest of this year to assess the impact of lower rates on the economy prior to resuming the cycle in 1Q20. Note that there are two more meetings this year, on 14 November and 12 December.
- The BSP had previously assessed the economy would pick up considerably in 2H19 as government spending, especially infrastructure investment, is showing signs of recovery. This should support the economy to grow by at least 6% in 2019, the lower end of the official target of 6.0-7.0%. However, there is room for another rate cut in 4Q19 if the GDP reading for 3Q19 – due out on 7 November – reports below-6% growth.

Inflation drops to 3-year low in September

Headline inflation tumbled to +0.9% YoY in September from +1.7% YoY in August, the lowest since September 2016. Core inflation fell to +2.7% YoY from +2.9% a month ago, according to the Philippine Statistics Authority (PSA). September inflation data is lower than Bloomberg consensus estimate of +1.1% but is within the BSP's target range of 0.6%-1.4% YoY. This takes YTD inflation (Jan-Sep) to +2.8% YoY. The continued drop in headline and core inflation was due to lower prices of major items including Food and Transportation.





Bangko Sentral ng Pilipinas (BSP): Baseline Inflation forecasts
(as of 10 October)

	9 May Meeting	20 Jun Meeting	8 August Meeting	26 September Meeting
2019	2.9%	2.7%	2.6%	2.5%
2020	3.1%	3.0%	2.9%	2.9%
2021	n.a.	n.a.	2.9%	2.9%

Krungsri Research's view

- September inflation reading reflects weakness in the demand and supply side. While inflation should pick up from November onwards due to fading high-base effect, we expect full-year inflation to remain just below 3%, the mid-point of BSP's target range. And, inflation should stay within the target range of 2-4% in 2020 in the absence of major upside risks.
- Following the BSP's move to downgrade inflation for 2019 to +2.5% from +2.6% previously, which suggests an easing inflation outlook, there is room for the BSP to normalize its monetary policy and provide a boost to the economy if growth is anticipated to miss the official target.

Source: Philippine Statistics Authority (PSA), BSP, CEIC, Krungsri Research

KRUNGSRI RESEARCH

Somprawin Manprasert, Ph.D.	**Head of Research Division and Chief Economist**

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Macroeconomic Team

Sarun Sunansathaporn	Senior Economist (Global Economy)
Sujit Chaivichayachat	Senior Economist (Thai Economy)
Churailuk Pholsri	Senior Economist (Forecasting)
Soison Lohsuwannakul	Senior Economist (Lao PDR, Vietnam, Indonesia)
Sathit Talaengsatya	Senior Economist (Cambodia, Myanmar, The Philippines)
Lookhin Varachotisate	Economist
Tanaporn Sriklay	Economist

Industry Team

Phornphan Phoksuphat	Head of Industry Research
Taned Mahattanalai	Senior Analyst (Manufacturing, Steel)
Chamadanai Marknual, Ph.D.	Senior Analyst (Construction, S-Curve)
Poonsuk Ninkitsaranont	Senior Analyst (Healthcare, Modern Trade , ICT)
Piyanuch Sathapongpakdee	Senior Analyst (Transportation & Logistics, Construction Materials)
Narin Tunpaiboon	Senior Analyst (Power Generation, Biofuel, Chemical & Plastic Products)
Puttachard Lunkam	Analyst (Tourism Sectors, Industrial Estate)
Wanna Yongpisanphob	Analyst (Automobile, Electronics & Electrical Appliances, Food & Beverages)
Patchara Klinchuanchun	Analyst (Real Estate)
Chaiwat Sowcharoensuk	Analyst (Agricultural Products)

Intelligence Team

Talublugkhana Thanadhidhasuwanna	Senior Analyst (Financial Sectors)
Rachot Leingchan	Analyst (Oil & Gas, Petrochemicals)
Arpakorn Nopparattayaporn	Analyst
Chutipha Klungjaturavet	Analyst

MIS and Reporting Team

Suratchanee Somprasong	Administrator
Thamon Sernsuksakul	Administrator
Chirdsak Srichaiton	MIS Officer
Wongsagon Keawuttung	MIS Officer

For research subscription, contact

krungsri.research@krungsri.com