

# NRI: looking from December to the new year

## External demand looks tenuous

East Asia's economies held up better than expected into the close of the past year. External demand provided much of that support, particularly in the economies most leveraged to growth in China: Taiwan, Hong Kong and South Korea. All tapped still-booming demand on the mainland. Our view on the Philippines is largely unchanged. Elsewhere, the picture was more mixed. Malaysia's growth was a bit off what we'd expected, though still quite solid. Thailand's stable and steady recovery remains on pace. Singapore increasingly looks in the doldrums, hurt by negative consumer sentiment that flows from rising unemployment. Indonesia's troubles are well known and aggravated by the attack in Bali. As we enter the new year, the lack of growth drivers stands out. Fiscal policy may lose steam while uncertainty remains in external demand.

- **South Korea.** We see a stable monetary policy in the new year and the possibility of the won gaining ground against the yen, which we think will weaken. Overall, we look for a GDP rise of 5.6% y-y in 2003. Key risks are a deterioration in external demand hurting private consumption.
- **Taiwan.** The island also went into the end of the year on strong growth figures, though we think this is largely base effect. For 2003, we expect GDP growth of 2.9% y-y. Any substantial recovery here looks difficult, however, with the island hostage to external demand and amid a tough restructuring of its financial sector.
- **Hong Kong.** The SAR saw a bit of a rise in 3Q02, boosted by stronger economic activity from China. But local malaise means we don't see much recovery in the new year, where we expect GDP will rise 1.9% y-y.
- **China.** We expect 2003 GDP will post a rise of 7.5% y-y, following estimated growth of 8.0% in 2002. Exports should slow over the 2003, a key risk for the year. We also expect to see the local currency trade in a wider band, though the renminbi should continue to be supported by a strong current-account surplus.
- **Singapore.** We see lacklustre prospects in a city-state hemmed in by a demanding external environment and domestic sentiment that is being hurt by rising unemployment. We project 2003 GDP growth at 3.9% y-y and a largely flat currency.
- **Malaysia.** The economy remains sound, backed by solid domestic demand. We see 4.9% y-y GDP growth in 2003 and little pressure on the peg at RM3.8:US\$1.
- **Indonesia.** The key risk to this economy should be the aftermath of Bali and its effect on tourist revenues. Moreover, presidential and general elections run the risk of hotting up local affairs. We see 2003 GDP rising 3.7% y-y and chances that the rupiah will weaken over the year.
- **The Philippines.** Our view here is largely unchanged. We expect GDP to rise 3.8% y-y and the currency to trade around current levels.
- **Thailand.** The country is showing stable, strong growth. Private demand is holding up. We expect the baht will appreciate over the year and see 2003 GDP growth at 4.3% y-y.

## Economic Insight

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## A modest slowdown expected

### Mixed signals

*We do not expect a “double-dip” US recession, a mild positive for East Asia’s economies*

In terms of the external environment since November 2002, the Asian economies, particularly the financial markets, have breathed a sigh of relief. In the US, various economic indices showed signs of advancing, and then retreated. However, the financial markets regained a measure of stability, reflected easing fears over recession. This has had a ripple effect on Asian markets. Pre-Christmas demand for electronic products was unexpectedly strong and there was no seeming impact from the October strike at US ports. While the pace of recovery in the US is slow, NRI maintains its view a “double-dip” recession is unlikely and that the appointment of a new economic team there will shore up the economy.

*External demand has held up better than expected...*

In East Asia’s economies, strong and weak data emerged. GDP across Asia showed a stronger 3Q02 performance, supported by an increase in exports. South Korea’s exports to China were driven by demand there for mobile phones and other consumer electronics having been strong. Hong Kong also showed a GDP growth rate of 3.3% y-y in 3Q02, backed by an increase in re-exports and re-imports to and from China. From the viewpoint of external demand, the trend in East Asia’s economies did not look weak going into the end of the year.

*...though we expect support to ebb going into 2003*

But despite strong short-term demand, weak trends continue to crop up. These look to be on concerns over the broader picture going into the new year. Some sectors of the electronic industry voiced concerns over the consequences of the strong pre-Christmas demand. Taking into consideration the slow recovery in factory operation rates, any recovery in private-sector capital investment will likely be muted.

### Private consumption tapering off

*With scope for fiscal easing limited, private consumption may be at risk*

A concern being raised is this: if an easing of monetary policy across Asia does not lead to a recovery of capital investment, the other category of demand, private consumption (bolstered by an easing policy), may begin to wane.

*Lending to households has run its course, if not over-shot*

This, perhaps, is most evident in South Korea. Lending to households is still relatively strong. At end-September, lending to households stood at W424.3tn, equivalent to almost 75% of GDP. The delinquency rate in credit-card payment has risen to about 10%. The Financial Supervisory Service is trying to rein in lending to households while maintaining low interest rates. A possibility we cannot rule out is that a deterioration in the economy would lead to rising bad debts in household loans. In turn, this might depress consumer sentiment — which might cause a further deterioration in the economy. Concerns over household lending are also prevalent in Malaysia and Thailand. In Hong Kong, the slump in real estate is hampering recovery in private consumption.

*Some grim signs are out: private consumption and external demand may falter and the monetary taps have already been run*

While external and private sector demand are increasingly uncertain, monetary policy has reached a deadlock. The accommodative monetary situation in the US should be a long-term affair. At the same time, the trend of monetary easing should continue in Asia. But there is a limit to how far rates can fall and room to stimulate the economy through further interest-rate cuts is minimal. Looking back, the expansionary fiscal policy adopted in 2002 (in hindsight, not such a bad year) means economic stimulus through fiscal measures will not be particularly effective in most economies in this survey — the scope is not there.

## Mild deceleration seen in 2003

*We start the new year amid a lack of growth drivers*

All this leads us to our view there will be a mild deceleration across East Asia's economies in 2003. Under our base-case scenario, where a double-dip recession in the US will be avoided, the possibility of a sudden drop in external demand does not look on the cards. This means the possibility of a severe deterioration in employment and incomes is low in East Asia. So, while private consumption is far from dynamic, present levels look well enough supported. Indeed, risks may arise from a reverse scenario — a drop in external demand which might lead to a deterioration in employment and household income, which, in turn, depresses private consumption. Were this to be topped by a credit crunch to households, further pressure would hit the affected economies.

*The overhangs are political: terrorism and the threat of war*

On the political front, the impact of the Bali bombing and fear of Islamic terrorism is eroding consumer sentiment across Asean. We see it as unlikely China will be thrown into confusion by the change in political power, but the wait-and-see situation on economic policy is expected to continue until the next National People's Conference (NPC) conference, set for spring 2003. For South Korea, uncertainties stirred by the presidential election are easing, though increasing concerns over North Korea remain a persistent drag on sentiment.

Hiroyuki NAKAI

### Outlook for Asian economies by NRI

(%)	2002E		2003F	
	Previous	Current	Previous	Current
Asia NIEs	4.2	<b>4.2</b>	4.2	<b>4.1</b>
Korea	6.1	<b>6.1</b>	5.8	<b>5.6</b>
Taiwan	3.1	<b>3.3</b>	3.0	<b>2.9</b>
Hong Kong	0.9	<b>1.9</b>	1.7	<b>2.5</b>
Singapore	4.7	<b>2.4</b>	5.5	<b>3.9</b>
Asean4	4.4	<b>4.0</b>	4.6	<b>4.1</b>
Indonesia	4.0	<b>3.3</b>	4.4	<b>3.7</b>
Malaysia	4.8	<b>4.1</b>	5.6	<b>4.9</b>
Philippines	3.9	<b>3.9</b>	4.0	<b>3.6</b>
Thailand	4.8	<b>4.8</b>	4.7	<b>4.3</b>
China	7.7	<b>8.0</b>	7.4	<b>7.5</b>
Total	5.7	<b>5.8</b>	5.6	<b>5.5</b>
(Ref.)				
NIEs+Asean4	4.2	<b>4.1</b>	4.4	<b>4.1</b>

Source: Nomura Research Institute

### Short-term economic outlook for Asian NIEs and Asean4 economies

	Real economic growth (%)					Inflation rate (CPI) (%)					Current account balance (US\$bn)				
	1999	2000	2001	2002E	2003F	1999	2000	2001	2002E	2003F	1999	2000	2001	2002F	2003F
Asian NIEs	7.6	8.5	0.6	4.2	4.1	(0.2)	0.9	1.6	0.6	1.5	61.4	46.2	56.1	61.8	59.2
South Korea	10.9	9.3	3.0	6.1	5.6	0.8	2.3	4.1	2.8	3.7	24.5	12.2	8.6	4.4	(1.4)
Taiwan	5.4	5.9	(2.2)	3.3	2.9	0.2	1.3	(0.0)	(0.2)	0.0	8.4	8.9	17.9	25.2	26.0
Hong Kong	3.4	10.2	0.6	1.9	2.5	(4.0)	(3.8)	(1.6)	(3.0)	(1.0)	12.0	9.1	11.7	14.0	15.2
Singapore	6.9	10.3	(2.0)	2.4	3.9	0.5	1.3	1.0	(0.3)	1.0	16.5	15.9	17.9	18.2	19.4
Asean4	3.3	5.4	2.3	4.0	4.1	8.8	2.8	5.7	5.2	4.4	38.2	34.9	24.6	23.2	22.1
Indonesia	0.8	4.9	3.3	3.3	3.7	20.7	3.8	11.5	11.9	7.7	5.8	8.0	6.5	6.7	6.0
Malaysia	6.1	8.3	0.5	4.1	4.9	2.8	1.6	1.4	1.8	2.3	12.6	8.5	7.3	6.5	6.9
Philippines	3.4	4.4	3.2	3.9	3.6	6.7	4.3	6.1	3.1	3.9	7.4	9.1	4.6	4.9	5.9
Thailand	4.4	4.6	1.8	4.8	4.3	0.3	1.6	1.6	0.8	2.1	12.5	9.3	6.2	5.0	3.3
China	7.1	8.0	7.3	8.0	7.5	(1.4)	0.4	0.7	(0.8)	(0.2)	15.7	20.5	17.4	31.6	29.8
<b>Total</b>	<b>6.6</b>	<b>7.7</b>	<b>3.7</b>	<b>5.8</b>	<b>5.5</b>	<b>0.9</b>	<b>1.0</b>	<b>2.0</b>	<b>0.8</b>	<b>1.3</b>	<b>115.3</b>	<b>101.5</b>	<b>98.1</b>	<b>116.6</b>	<b>111.1</b>
Asian NIEs + Asean4	6.3	7.5	1.1	4.1	4.1	2.6	1.5	2.9	2.0	2.4	99.6	81.0	80.7	85.0	81.3
Japan	0.7	2.8	0.3	(0.3)	(0.1)	(0.3)	(0.7)	(0.7)	(1.0)	(0.6)	114.6	119.7	87.8	112.6	111.2
United States	4.1	3.8	0.3	2.4	2.0	2.2	3.4	2.8	1.6	1.9	(292.9)	(410.3)	(393.4)	(481.9)	(478.4)

Notes: 1 Each economy's weight in the aggregate figures for real economic growth was calculated on the basis of its Nominal GDP for 1999 in US dollars;

2 "Asian NIEs" refers to South Korea, Hong Kong, Taiwan, and Singapore; "Asean4" refers to Malaysia, Indonesia, Thailand, and the Philippines;

3 As of this publication, composite index is used for inflation rate for Hong Kong; (4) data as of 10 December, 2002

Source: Nomura Research Institute, from International Financial Statistics, International Monetary Fund, and official statistics of the economies concerned. Forecasts are by Nomura Research Institute.

## Foreign exchange rates (against US\$1)

	12 Sep	3Q02	4Q02	1Q03	2Q03	3Q03
Japanese yen (¥)	123.4	123.4	(115.0 - 130.0)	(115.0 - 130.0)	(117.5 - 132.5)	(117.5 - 132.5)
Euro (€)	1.01	0.981	0.925 - 1.050	0.925 - 1.050	0.925 - 1.050	0.925 - 1.050
South Korean won (W)	1,213	1,223	(1,125 - 1,300)	(1,125 - 1,300)	(1,150 - 1,325)	(1,150 - 1,325)
Taiwan dollar (NT\$)	34.8	34.86	32.50 - 37.50	33.00 - 38.00	33.50 - 38.50	33.50 - 38.50
Hong Kong dollar (HK\$)	7.80	7.80	7.80	7.80	7.80	7.80
			(7.77 - 7.90)	(7.77 - 7.90)	(7.77 - 7.90)	(7.77 - 7.90)
Singapore dollar (S\$)	1.76	1.78	1.78	1.79	1.79	1.79
		0.00	(1.72 - 1.84)	(1.73 - 1.84)	(1.73 - 1.84)	(1.73 - 1.84)
Indonesian rupiah (Rp)	8,978	9,000	9,100	9,100	9,300	9,300
		0	(8,100 - 10,600)	(8,100 - 10,400)	(8,300 - 10,600)	(8,300 - 10,600)
Malaysian ringgit (RM)	3.8	3.8	3.8	3.8	3.8	3.8
Philippine peso (P)	53.3	52.4	53.0	52.7	52.5	52.5
		0.0	(52.0 - 54.5)	(51.2 - 54.2)	(51.0 - 54.0)	(51.0 - 54.0)
Thai baht (THB)	43.4	43.3	43.7	43.0	43.0	43.0
		0.0	(41.7 - 45.7)	(41.5 - 44.5)	(41.5 - 44.5)	(41.5 - 44.5)
Chinese renminbi (RMB)	8.28	8.28	8.28	8.28	8.28	8.28
NICQ		0.00		(8.20 - 8.35)	(8.20 - 8.35)	(8.20 - 8.35)

Note: Real figures are expected value at the end-period; figures in brackets are expected range at end-period.

Source: Nomura Research Institute

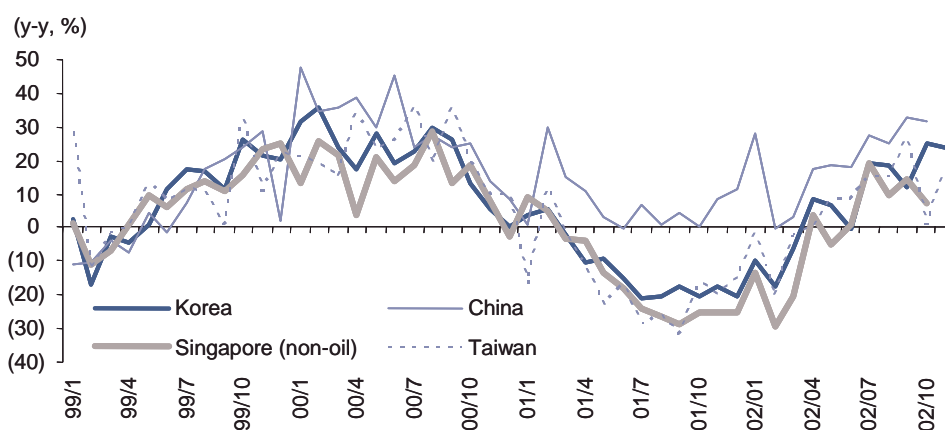
## Interest rates

	12 Sep	3Q02	4Q02	1Q03	2Q03	3Q03
USFF rate	1.25	1.75	1.00 - 1.25	1.00 - 1.25	1.00 - 1.25	1.00 - 1.50
South Korea overnight call rate	4.30	4.30	4.00 - 4.50	4.00 - 4.75	4.00 - 4.75	4.00 - 5.00
Taiwan (overnight call rate)	1.59	1.96	1.50 - 1.75	1.25 - 1.75	1.00 - 1.75	1.00 - 2.00
Hong Kong (3M Hibor)	1.54	1.89	1.25 - 1.50	1.25 - 1.50	1.25 - 1.50	1.25 - 1.75
Singapore (3M Sibor)	0.88	1.38	0.5 - 1.00	0.5 - 1.25	0.5 - 1.25	0.5 - 1.25
Indonesia (overnight Jibor)	12.6	12.92	11.5 - 13.5	11.0 - 14.5	11.0 - 14.5	11.0 - 14.5
Malaysia M Klibor	3.2	3.190	2.5 - 3.5	2.5 - 3.5	2.5 - 3.5	2.5 - 3.5
Philippines (91D T-bill rate)	5.1	5.221	5.00 - 6.00	5.50 - 7.00	5.50 - 7.00	5.50 - 7.25
Thailand (14D repo)	1.75	2.00	1.50 - 1.75	1.25 - 1.75	1.25 - 1.75	1.25 - 2.00
China 1Y lending rate for working capital	5.31	5.31	5.31	4.77 - 5.31	4.77 - 5.31	4.77 - 5.31

Note: Rates at end-period

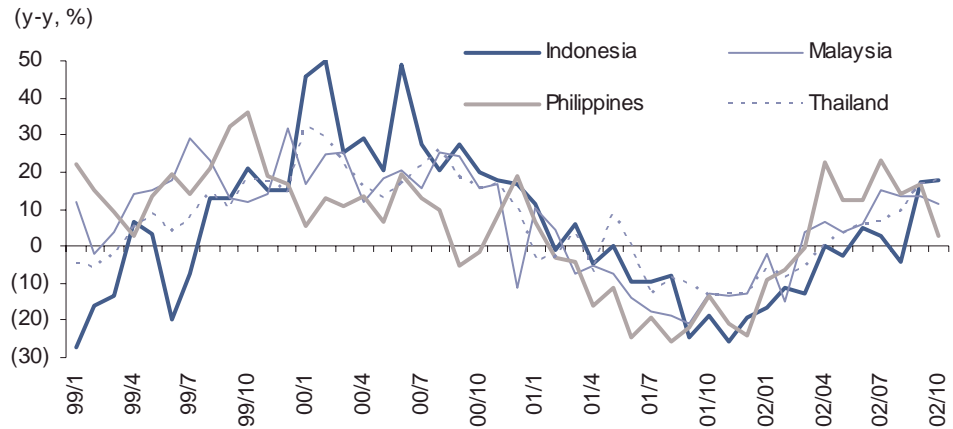
Source: Nomura Research Institute

## Exports in East Asia (Korea, China, Singapore, Taiwan)



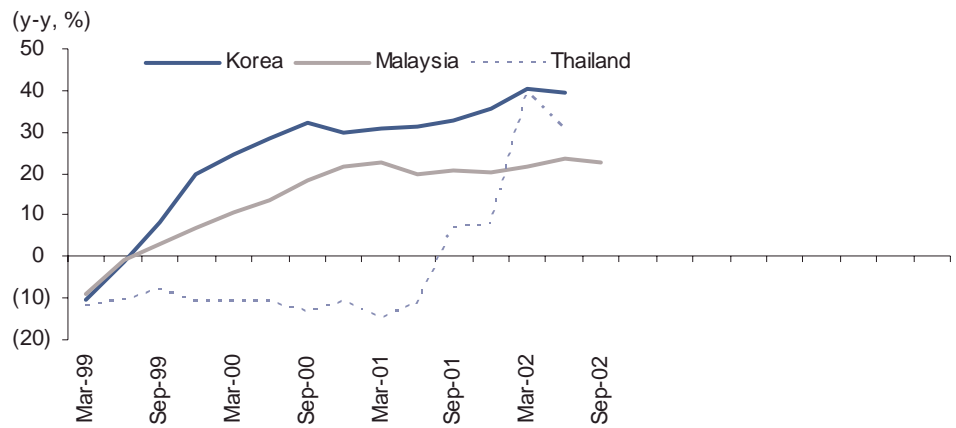
Source: Official statistics

**Exports in East Asia (Indonesia, Malaysia, the Philippines, Thailand)**



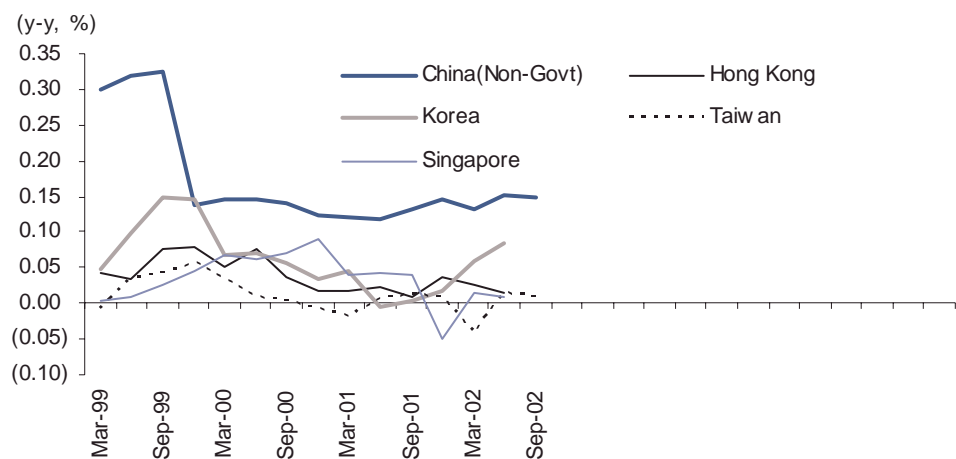
Source: Official statistics

**Household lending (Korea, Malaysia, Thailand)**



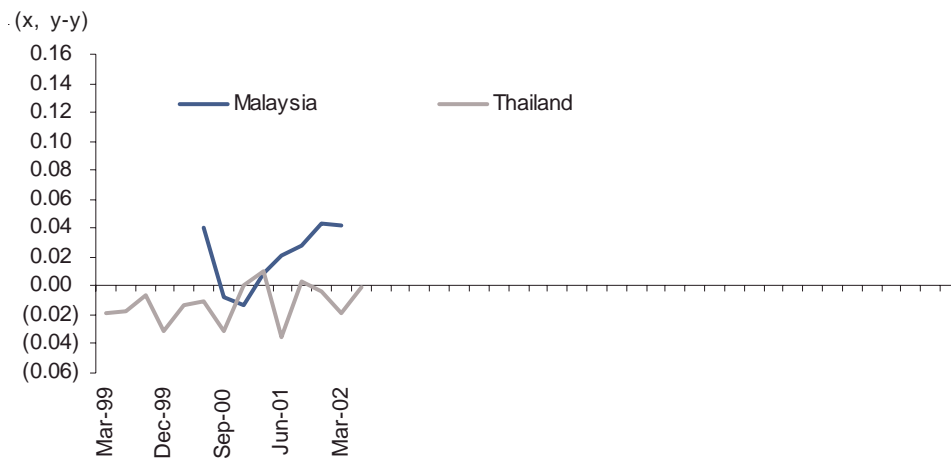
Source: Official statistics

**Income in East Asian countries and territories, real terms**



Source: Official statistics

Income in Asian countries and territories, real terms



Source: Official statistics

## South Korea's economy: stable

The South Korean economy grew by 5.8% y-y in 3Q02, up from 1.3% y-y growth in 2Q02. While private consumption moderated, growing 6.1% y-y, the quarter-on-quarter comparison showed a fall of 0.2%, on account of the expiry of tax breaks (especially for autos). Exports rose by 18.3% y-y and 6.3% q-q.

### *Exports and industrial output remained strong in 3Q03*

Since October, exports and industrial output for exports have been brisk. Exports in October and November combined (nominal basis, US dollars) grew by 24.5% y-y and industrial production in October rose by 12.3% y-y. By sector, electronic and non-electronic products have been doing well. By destination, a notable increase in exports to China was seen. Particularly since the beginning of 2002, the increase in the exports of mobile phones, computer-related products and household appliances has been quite solid. In 3Q02, exports to China rose 35.8% y-y, out of which the above three items accounted for 21.1%. While this may be a spike, it is also a sign South Korean companies have been active in setting up shop in China since 2H01.

### *Private consumption looks set to decline from a strong base*

But recovery in capital investment was slack, reflecting the weak corporate sentiment that flows from concerns over the US economy and excessive capacity at home. We expect private consumption to decline slowly, a likely consequence of the high base set in 1H02 and tighter lending policies to households.

### *We expect GDP growth of 5.6% y-y in 2003*

All told, we have revised our forecast GDP growth to 6.1% (unchanged from our previous forecast) for 2002 and 5.6% in 2003 (also unchanged). Changes to underlying assumptions include slightly higher expected external demand and slightly lower expected domestic demand. We see risks as to the downside, given the possibility of a deterioration in the external environment, which would, in turn, worsen unemployment and hurt household income.

### *Monetary policy limited: some scope for an appreciation in the won*

In monetary policy, economic growth is stable and if the economy takes the path forecast by NRI, a small rise in interest rates in early 2003 may be a precaution taken against an overheating economy. But with domestic demand weak amid mild inflationary pressure, a substantial hike looks unlikely. As for the currency, it is possible the won may appreciate a bit against the yen, backed by a stronger local economy.

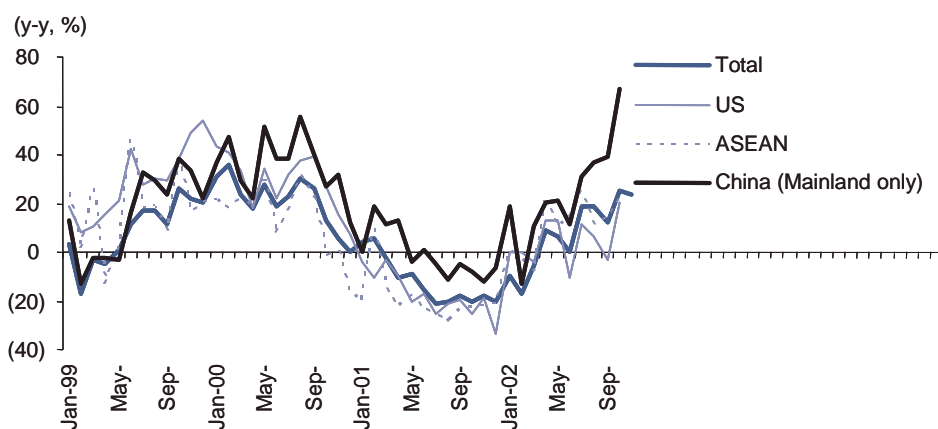
**Hiroyuki NAKAI**

**Short-term economic outlook**

(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	10.9	9.3	3.0	6.1	5.6
Private consumption	10.7	7.8	4.3	7.0	4.5
Govt. consumption	1.3	0.1	0.1	3.8	1.5
Fixed capital formation	4.2	10.3	(1.6)	3.9	2.3
(Facilities investment)	38.6	33.4	(9.8)	6.7	7.8
Change in stock (contribution)	5.4	(0.2)	0.0	(0.3)	0.0
Exports	17.0	20.3	1.0	12.7	10.9
Imports	29.7	19.9	(2.9)	15.7	8.8
CPI (y-y, %)	0.8	2.3	4.1	2.8	3.7
Current A/C balance (US\$bn)	24.5	12.2	8.6	4.4	(1.4)
(Weight to GDP, %)	602.6	2.7	2.0	0.9	(0.3)
Unemployment rate (%)	4.8	3.9	3.6	3.0	3.1
Overnight call rate (%)	5.0	5.1	4.8	4.2	4.6
W:US\$1 (average)	1,188	1,130	1,291	1,250	1,223

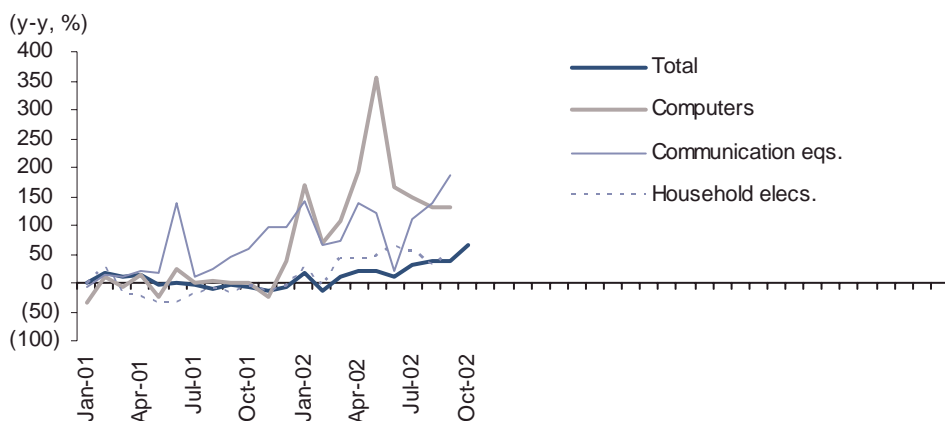
Source: Nomura Research Institute

**Exports by country**



Source: Official statistics

**Imports to China by item**



Source: Official statistics

## Taiwan's economy: a slower recovery seen

*Much of the rise in GDP through the end of the past year was a function of base effect*

On government figures, real GDP growth for 3Q02 was 4.77% y-y. But the strong showing was mainly on the low base set in the year-on-year comparison. We note: 3Q02 saw a bigger contribution from domestic demand and significantly lower contributions from external demand, though the latter remained positive. By sector, industrial including manufacturing rose by 7.5% and the service sector rose just 3.4%; finance/insurance was a standout, up 9.2%.

*Significant drags face the economy*

On the back of the stronger-than-expected external demand, the government revised its forecast for GDP growth from 3.1% y-y to 3.3% for 2002, but cut its 2003 figure from 3.5% to 3.4%. NRI revised its forecasts for 2002 and 2003 to 3.3% and 2.9%. We expect a slow turnaround from an external-demand-led to a domestic-demand-led economy. In 2003, however, we expect external demand will pick up only in 2H03. Overall, private consumption should be the main pillar of the economy, though nagging (and increasingly structural) unemployment will likely remain a drag on an economy that remains under pressure.

*The local economy needs to look abroad for support, not an easy prospect...*

Given the weak recovery in domestic demand, Taiwan will have to look abroad to lift the economy. But the lacklustre global outlook, and the risk of weaker PC/semiconductors orders, should mean any success here will be limited. Despite what look like bright figures, any economic recovery will likely be brittle.

*...nor is restructuring the finance sector proving an easy task*

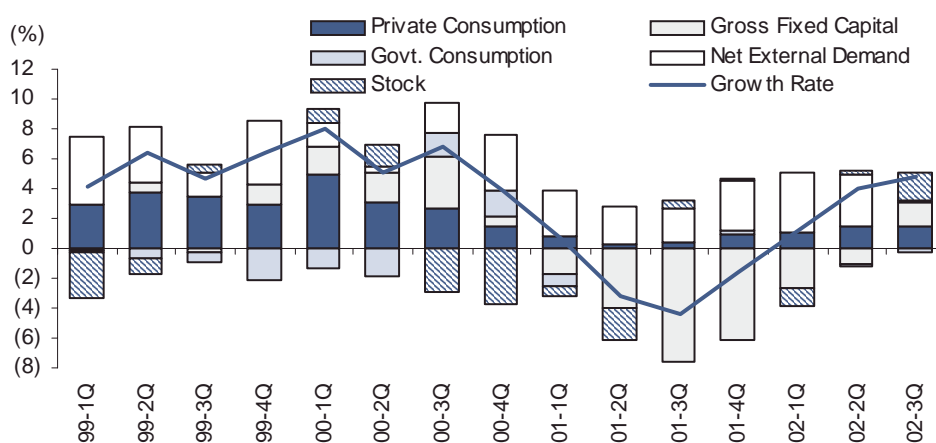
In more local affairs, the action by farmers and fishermen seeking to scotch the plan to liquidate the credit departments of the farmers' and fishermen's associations (part of larger plans to reform the financial system) led to the island's largest-ever demonstration, one involving more than 100,000 people. This prompted the resignation of the ministers of finance and agriculture — a clear demonstration of the difficulties in reforming the financial system, even in measured stages. With some parts of the plan having been shelved, concerns over the government's determination and capacity to reform the financial system, particularly the commercial banks, are spreading — both at home and abroad.

**Masaki KOBAYASHI**

**Short-term economic outlook**

(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	5.4	5.9	(2.2)	3.3	2.9
Private consumption	5.4	4.9	1.0	2.2	2.4
Govt. consumption	(6.5)	0.6	(1.0)	(1.4)	(0.7)
Fixed capital formation	1.8	8.6	(20.6)	(2.0)	5.9
(Private investment)	(0.7)	15.7	(29.2)	(0.2)	9.9
Stock (contribution)	(0.9)	(1.2)	(0.5)	0.8	0.3
Export	11.9	17.6	(7.8)	10.2	9.2
Import	4.4	14.5	(13.9)	8.2	10.7
CPI (y-y, %)	0.2	1.3	(0.0)	(0.2)	0.0
Current account balance (US\$bn)	8.4	8.9	17.9	25.2	26.0
(To GDP, %)	2.9	2.9	6.4	9.0	9.4
Unemployment (%)	2.9	3.0	4.6	5.1	5.2
Overnight call rate (%)	4.8	4.7	3.6	2.1	1.8
NT\$:US\$1	32.3	31.2	33.8	34.6	36.0

Source: Nomura Research Institute

**Contribution to GDP growth**

Source: Nomura Research Institute, from official statistics

**Banking sector: balance overdue**

(As at 30 Sept, 2002, NT\$bn)	Lending		Overdue loans	
	Amount	Weight (%)	Amount	Ratio to Total (%)
Domestic banks	12,176	89.6	901	7.4
Foreign banks	404	3.0	10	2.5
Community financial institutions	1,010	7.4	165	16.4
<b>Total</b>	<b>13,590</b>	<b>100.0</b>	<b>1,076</b>	<b>7.8</b>

Source: Nomura Research Institute, from official statistics

## Hong Kong's economy: an upward revision

*The SAR's economy approached the close of the year with strong support from the mainland's economy...*

In Hong Kong, real GDP in 3Q02 rose by 3.3% from 0.8% in 2Q02 (an upward revision to the previously announced 0.5% rise). The major factor was a surge in exports of goods and services. Exports of goods in 3Q02 rose by 11.4%, the first double-digit increase since 4Q00. This was mainly on strong re-exports to/from China. Owing to strong tourist arrivals and offshore trade and transportation, exports of services rose 14.1%.

*...but the outlook at home remains weak*

Meanwhile, domestic demand remains sluggish, though a slight improvement was seen. Private consumption in 3Q02 fell 1.5%, against the 2.4% fall in 2Q02. This is mostly base effect: a year-on-year rise in 3Q02 figures had been expected since private consumption started to decline in 3Q01 (in quarter-on-quarter terms). Moreover, employment (three-month moving average) bottomed out in June, posting slight improvements thereafter. However, fixed capital formation fell by 5.0% y-y. While real estate investment held steady, investment in machines, equipment and software fell. Composite CPI in 3Q02 fell by 3.5% — the fourth consecutive year of deflation.

Real GDP will likely post solid growth for 4Q02, since China's imports and exports remain strong and the base in 4Q01 was low, showing the after-effects of 11 September. At NRI, we have revised up our 2002 forecast for real GDP growth to 1.9% from 0.9%.

*A modest upward revision to our GDP forecast for 2003, though our view falls short of calling for a full-on recovery*

Our GDP forecast for 2003 is also revised up, to 2.5% y-y from 1.7%. Again, the revision is mostly on base effects. Furthermore, external demand is looking uncertain. It is not clear how the developed economies will do in the new year and China's imports and exports are forecast to slow. On the fiscal side, significant stimulus measures are not expected, given a spiralling deficit. The deficit in the first seven months of this fiscal year (April to October 2002) reached HK\$72.4bn, against an initial budget of HK\$45.2bn (subsequently revised to HK\$60bn). All the above inform our view a full-scale recovery is not in the offing for the coming year.

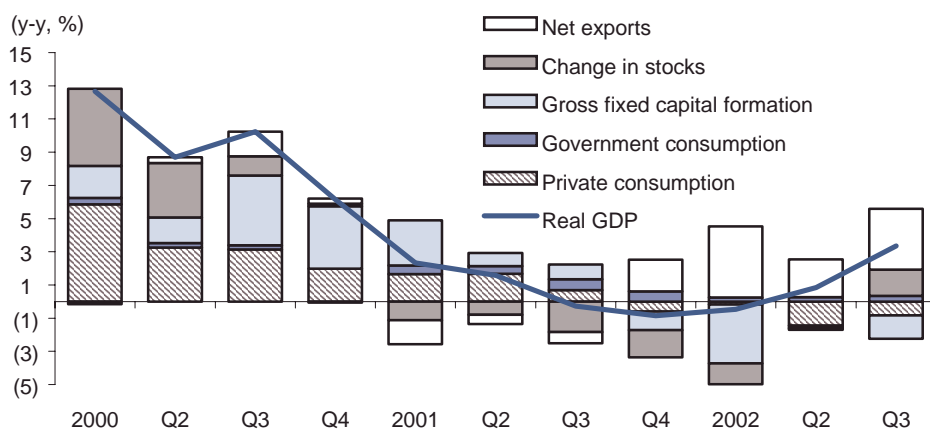
**Suiyo LI**

**Short-term economic outlook**

(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	3.4	10.2	0.6	1.9	2.5
Private consumption	1.3	5.9	1.4	(1.4)	(1.1)
Government consumption	3.1	2.0	6.0	2.9	2.7
Gross domestic fixed capital formation	(16.6)	11.0	2.9	(5.3)	(1.3)
Changes in inventories (contr to GDP)	1.1	2.2	(1.4)	0.5	0.1
Exports of goods	3.7	17.1	(3.3)	6.5	5.9
Exports of services	6.4	12.9	5.9	10.5	8.2
Imports of goods	0.0	18.2	(1.9)	5.7	4.9
Imports of services	(4.1)	4.2	(0.2)	(0.8)	0.8
Composite CPI	(4.0)	(3.8)	(1.6)	(3.0)	(1.0)
Current account balance (US\$bn)	12.0	9.1	11.7	14.0	15.2
(as of GDP, %)	7.5	5.5	7.2	11.1	11.9
3-month interbank int rate (period-avg, %)	5.84	6.12	3.58	1.69	1.34
Best lending rate (period-average, %)	8.50	9.22	7.01	4.38	4.50
HK\$:US\$1	7.60	7.79	7.80	7.80	7.80

Source: Nomura Research Institute, from Hong Kong Census and Statistics Department

**Contribution to GDP by demand composition**



Source: Nomura Research Institute, from Hong Kong Census and Statistics Department

## China's economy: a slowdown expected in 2003

*On our projections, China's GDP will rise 7.5% y-y in 2003...*

For 2002, China's economy should see real GDP growth of 8.0% y-y, driven by the expansion of investment (a result of a stimulatory fiscal policy), an increase in foreign direct investment (FDI) and exports. For 2003, assuming the government's fiscal policy becomes more mediatory, we expect real GDP growth to fall to 7.5%.

*...a year where exports should provide less support*

First, all indications are exports will slow, constrained by: 1) unclear economic prospects in the developed economies; 2) the export tax rebate, the main factor contributing to 2002's increased exports, being delayed owing to financial difficulties; and 3) since exports by private enterprises have increased so rapidly, base effects will likely come into play in 2003.

*Strong investment inflows should continue*

The second factor is slowing in-coming investment. We expect state-owned enterprises' (SOEs) investments in new plant and equipment, infrastructure and property will slow. This should be driven by: 1) with the change of regime expected in March 2003, government projects in progress should have been wrapped up in 2002 and new projects put off; and 2) investment in property, which grew by nearly 30% in 2002, will have to go through some adjustment in 2003 as the result of a rise by 10.8% y-y (figures issued by the State Statistics Bureau) in the vacancy rate of residential housing from January to October. Meanwhile, following WTO-linked liberalisation FDI should continue to flow in.

*The government is backing autos as a leg to growth*

Third, while we expect private consumption to remain strong in cities (backed by policy of supporting urban areas) activity in the countryside should remain sluggish. In early 2003, it appears that to encourage car purchases by city-dwellers, the government is going ease some of the regulations on car purchases, reducing expenses when a consumer buys a car or arranges a car loan.

*Deflation should taper off during the year*

While we predict deflation will continue well into 2003, price declines should ease. This is because we expect to see some improvement in the over-supplied market situation, which is one of the main causes of deflation. After completion of the change of leadership, SOE reform is expected to be moved forward and the over-supplied market for consumer goods should see some improvement.

*The currency looks well supported*

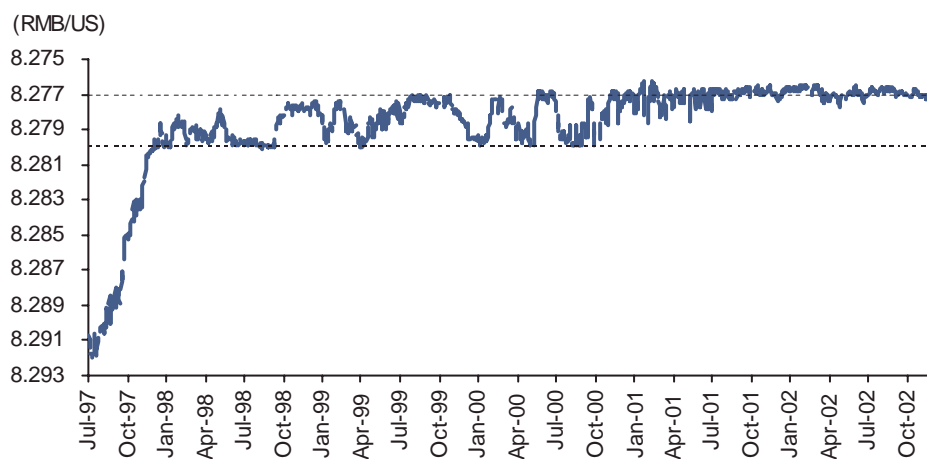
According to remarks from the central bank, the renminbi will be allowed to trade in a wider band next year. We expect the renminbi will remain strong, as China continues to add to its already large current-account surplus.

**Suiyo LI**

**Short-term economic outlook**

(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	7.1	8.0	7.3	8.0	7.5
Real value-added industrial production	8.5	11.4	8.9	12.5	10.4
Nominal fixed-asset investment	5.1	10.3	12.1	20.5	13.3
Real retail sales	8.2	9.3	9.4	9.5	9.0
Consumer price	-1.4	0.4	0.7	-0.8	-0.2
Customs-cleared export	6.1	27.9	6.8	21.1	10.6
Customs-cleared import	18.2	35.8	8.2	18.3	12.6
Customs-cleared trade balance (US\$bn)	29.2	24.1	22.5	34.2	31.8
Current account balance (US\$bn)	15.7	20.5	17.4	31.6	29.8
(as % of GDP)	1.6	1.9	1.5	2.6	2.2
One-year lending rate for working capital	5.85	5.85	5.85	5.31	4.77-5.31
RMB:US\$1 (year-end)	8.279	8.277	8.277	8.277	8.20-8.35

Source: Nomura Research Institute, from official statistics

**Exchange rate**

Note: Dotted lines (8.2770-8.2800) are considered the trading band

Source: Nomura Research Institute, from the People's Bank of China

## Singapore's economy: weak local demand

*A protracted slump in domestic demand is crimping Singapore's economy*

The Singapore economy is facing a slump in domestic demand that is turning out to be worse than expected. The growth rate for private consumption and fixed capital formation in 3Q02 fell by 1.9% y-y and 11.4% q-q, respectively, in real terms. For fixed capital formation, while the fall was partly on an increase in inventory in the chemical industry in 2Q02, a fall was also evident in construction. At NRI, we have cut our GDP forecasts to 2.4% in 2002 (from 3.5%) and 2003's figure to 3.9% from 5.2%.

*Any recovery will likely have to wait until 2H03*

The first reason for the cuts is weakness in the external environment that is worse than previously expected. While the US economy in 2003 is expected to maintain a real growth rate of 2.0%, exports of electronics-related products such as semiconductors are slowing. To our view, a robust recovery will have to wait until 2H03.

*Unemployment is worsening and becoming structural*

The second reason is the worsening employment situation. Since the employment system in Singapore is quite flexible, unemployment has risen fast since 2001, hit by a hollowing out of the manufacturing and service industry (banking stands out here). While cutbacks in manufacturing began to ease in 2002, a second round of job cuts took place in services. The unemployment rate (seasonally adjusted) rose to 4.8% in 3Q02. This likely reflects a shift in FDI to more capital-intensive areas that employ fewer workers per unit of output.

*A softening of the planned rise in the GST does not look as though it will lift consumer sentiment*

The rise in the GST by 2% to 5%, which had been scheduled for the start of 2003, has since been put off. The GST will rise by one percentage point (pp) at start-2003 and by a further 1pp at start-2004. So, any hit to private consumption will be blunted, though we do not see the relaxation as enough to improve consumer sentiment much. In the fiscal 2003 budget (start-April 2003), we expect further stimulus measures will be unveiled.

*We see the currency trading flat over the year, though the government has the option of a weaker Singapore dollar*

Since domestic demand is expected to remain sluggish through 2003, the current-account surplus should improve. As far as the exchange-rate policy is concerned, there should be no change in the Monetary Authority of Singapore's (MAS) policy of a stable Singapore dollar (nominal effective exchange rate terms). Based on the assumption of an underlying weaker yen and firm euro, we forecast an end-2003 rate of S\$1.79:US\$1. But we note: a risk is that MAS may shift policy in favour of a weak currency should the yen show an unexpected rise against the US dollar.

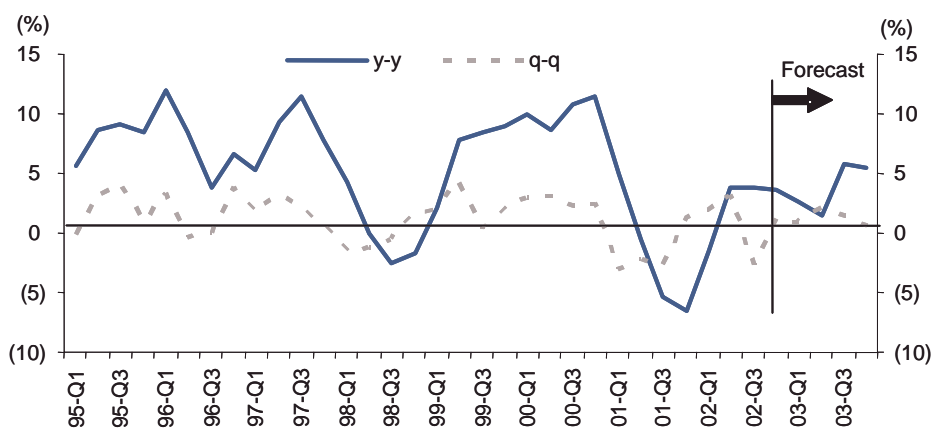
**Tomo KINOSHITA**

**Short-term economic outlook**

(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	6.9	10.3	(2.0)	2.4	3.9
Private consumption	6.4	9.9	0.5	(0.1)	1.5
Government consumption	6.1	14.0	6.6	4.5	6.7
Fixed capital formation	(4.0)	6.3	(4.6)	(11.0)	(0.3)
Inc in stocks (contr to the real GDP growth)	2.4	2.4	(6.7)	1.1	1.8
External demand (contr to the real GDP growth)	3.1	0.5	5.3	4.4	0.8
CPI	0.5	1.3	1.0	(0.3)	1.0
Current account (US\$bn)	16.5	15.9	17.9	18.2	19.4
(as % of GDP)	20.0	17.2	20.9	20.9	21.2
S\$:US\$1 (period average)	1.70	1.72	1.79	1.79	1.79

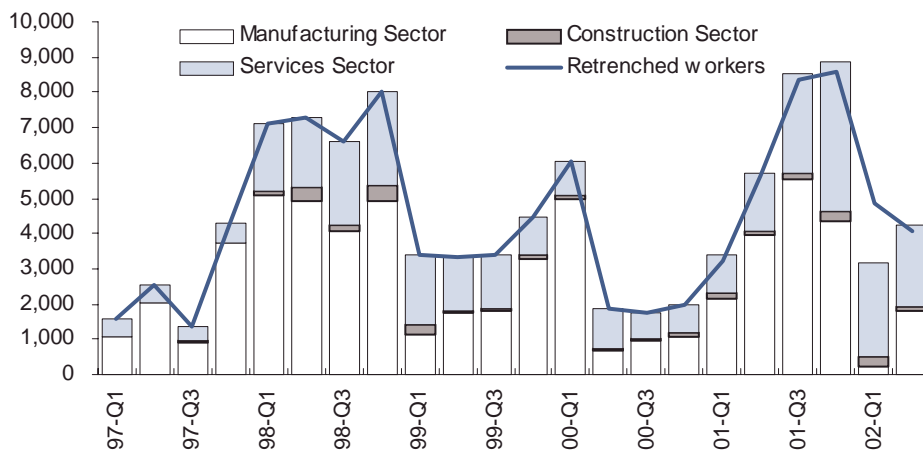
Source: Nomura Research Institute Singapore, official statistics

**GDP growth forecast**



Source: Nomura Research Institute Singapore

**Unemployment by industry**



Source: Nomura Research Institute from CEIC data

## Malaysia's economy: domestic demand still solid

*Growth in 3Q02 was a bit weaker than we had expected, but the underlying economy still looks solid*

Malaysia saw economic growth in 3Q02 of 5.6% y-y. While this is lower than expected, the growth shows a solid economy, driven by the three engines: private consumption, fiscal expenditure and exports. We maintain our view that domestic demand will continue to expand steadily. However, we have cut our real GDP estimates/forecasts as follows: to 4.1% from 4.8% in 2002; and to 4.9% from 5.6% for 2003.

First, the external environment is expected to be weaker. Exports of electronics-related products, which have been a strong growth driver, are expected to slow in 1H03.

*The attack in Bali will have effects on tourism that are not limited to Indonesia*

Second, private domestic demand is seen slowing on the effects of the Bali bombing. According to 2001 BOP statistics, gross receipts from tourism were RM26bn, or 7.8% of GDP. Since the bombing in Bali has un-nerved tourists, particularly from Europe, the impact on the economy should be considerable and most pronounced in 1H03.

While housing investment is slowing, it is logical to take the slump as temporary in view of the near full employment in the labour market and the steady growth in income at home.

*Fiscal policy remains stimulatory*

In fiscal policy, the government's target is to balance the budget by fiscal 2005. But at the same time, the government continues to push an expansionary policy that should add 1.6pp to growth in 2003. Moreover, further measures may be taken should these prove necessary. We also note: the transfer of power from Dr Mahathir to Mr Abdullah is scheduled for October 2003. This may also provide an incentive for further stimulatory measures.

*We don't expect much in the way of inflation, more so since the government can easily subsidise energy prices*

We expect CPI will remain stable. Even if crude prices rise, oil-exporting Malaysia can, and likely will, subsidise domestic energy prices. However, the current-account surplus in 2003 should be close to our original forecast, or 6.9% of GDP, since we have cut our forecasts for exports and domestic demand. We see the fixed exchange rate holding at RM3.8:US\$1; we do not see pressure here, either at home or in the external environment.

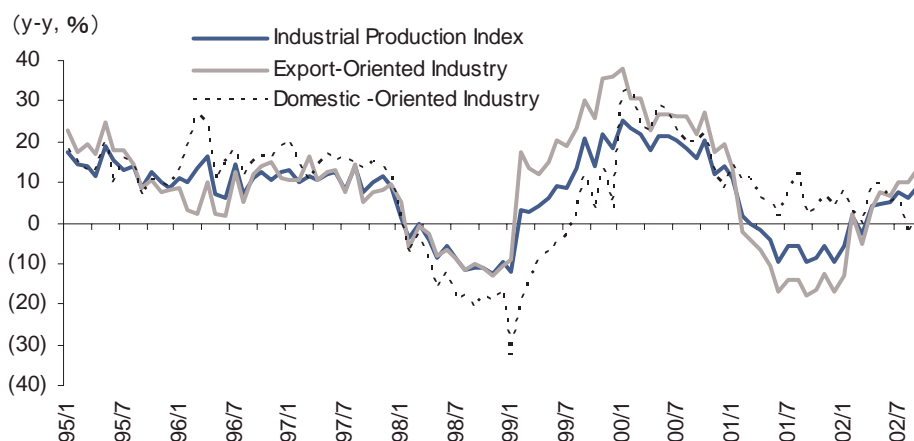
**Tomo KINOSHITA**

**Short-term economic outlook**

(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	6.1	8.3	0.5	4.1	4.9
Private consumption	2.9	12.5	2.8	4.2	4.9
Government consumption	17.1	3.0	17.6	13.8	8.5
Fixed capital formation	(6.5)	25.7	(2.8)	(0.9)	4.4
Increase in stocks (contr to the real GDP growth)	0.8	0.6	(2.3)	3.0	0.1
Exports	13.2	16.1	(7.5)	4.0	5.8
Imports	10.6	24.4	(8.6)	7.0	6.2
CPI	2.8	1.6	1.4	1.8	2.3
Current account (US\$bn)	12.6	8.5	7.3	6.5	6.9
(as % of GDP)	15.9	9.4	8.3	7.0	6.9
RM:US\$1 (period average)	3.80	3.80	3.80	3.80	3.80

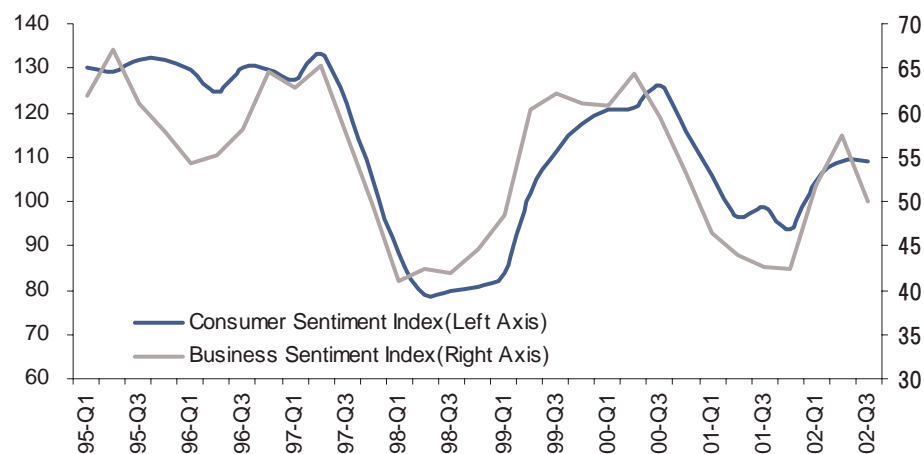
Source: Nomura Research Institute Singapore, from official statistics

**Industrial production index**



Source: Nomura Research Institute Singapore, from official statistics

**Survey by Malaysian Institute Economic Research**



Source: Nomura Research Institute Singapore from, official statistics

## Indonesia's economy: the aftermath of Bali

*We expect Indonesia's economy will feel the aftershocks of the attack in Bali through 2003...*

The most important factor for the Indonesian economy in 2003 should be the impact of the Bali bombing. The government's response was to take Abu Bakar Bashir, the spiritual leader of militant Islamic group Jamar Islamia, into custody and identify the alleged culprits in the bombing. These moves generally met the expectations of the international community. However, since it was later found that a stage in the attack had been carried out by a suicide bomber, concerns over terrorism linger. Meanwhile, in the run-up to the presidential election in 2004, there are signs of deepening discord between the Islamic parties and the ruling PDI-P (Ms Megawati's party). Another concern is that many political parties appear to have armed organisations under their wings.

*...and note that arrivals to Bali comprised 28% of the nation's tourist arrivals in 2002*

Indonesia's tourism receipts (these appear in the international BOP statistics) were equivalent to 3.8% of nominal GDP in 2000. Since tourists visiting Bali accounted for 27.6% of total foreign tourists visiting Indonesia in 2001, the bombing should be quite a heavy blow to the macro-economy. We take the view tourist arrivals in Indonesia will fall by about 20% y-y in 2003. Given the ripple effect, this looks a serious constraint to growth. Aside from global event risk (such as a war in Iraq), Indonesia may have to contend with the effects of El Niño on the agricultural sector. We estimate growth in 1H03 will fall to 3.1% y-y.

*Possibility of pump-priming ahead of the election*

But the effects of fiscal stimulus should start to show in 2H03, where we see growth recovering to 4.4% y-y. While state finances are strained, the administration will have to make the economy a priority in the run-up to the general and presidential elections in 2004.

*We do not expect the stability in the rupiah will hold during the year*

Since the service account deficit is expected to rise on the decline in tourist arrivals, the current-account surplus should shrink to 2.9% of GDP, despite rising crude prices. The rupiah has been broadly stable against the US dollar, supported by: 1) speculative transactions being generally controlled by exchange regulations; 2) foreign currency revenue from the asset sales by the Indonesian Bank Restructuring Agency (IBRA), which looks to have been converted to rupiah; and 3) the rising price of crude. But we believe the rupiah will weaken in coming months, given a shrinking current-account surplus and increasing political uncertainty.

**Tomo KINOSHITA**

**Short-term economic outlook**

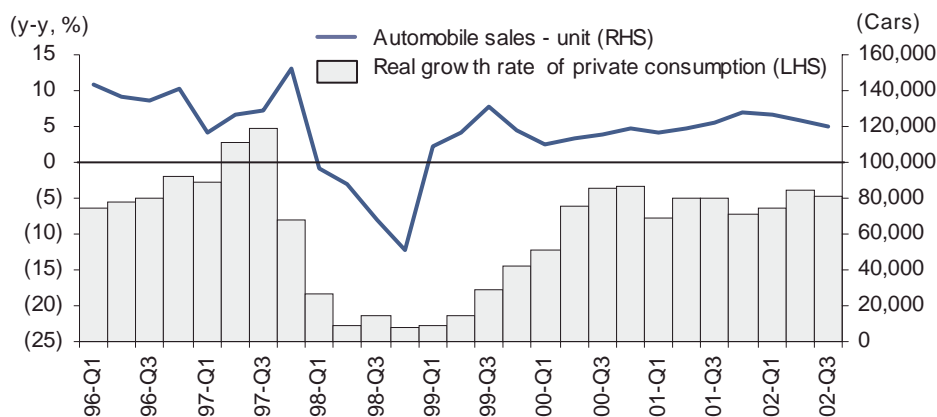
(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	0.8	4.9	3.3	3.3	3.7
Private consumption	4.6	3.6	5.4	4.9	3.6
Gov. consumption	0.7	6.5	8.2	9.5	4.6
Capital formation	(18.2)	21.9	0.3	(1.4)	4.8
Export	(31.8)	26.5	1.9	(2.6)	1.9
Import	(40.7)	21.1	8.1	(11.8)	5.8
Contribution by domestic demand	(2.1)	2.9	4.7	1.1	4.5
Contribution by foreign demand	2.9	2.0	(1.4)	2.2	(0.7)
CPI	20.7	3.8	11.5	11.9	7.7
Current account (US\$bn)	5.8	8.0	6.5	6.7	6.0
(as % of GDP)	4.0	5.2	4.5	3.6	2.9
Rp:US\$1	7,800	8,346	10,253	9,336	9,280

Source: Nomura Research Institute Singapore, official statistics

**Real GDP growth by industry (1993 base)**

(y-y, %)	2001				2002		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Real GDP	4.8	3.8	3.1	1.6	2.4	3.8	3.9
Agriculture, forestry & fishery	3.7	1.7	(0.4)	(2.8)	(1.3)	6.1	6.7
Mining	6.8	(0.3)	(2.4)	(5.9)	(1.5)	2.4	0.8
Manufacturing	4.2	4.8	4.7	3.6	4.3	2.7	3.0
Utilities	7.3	9.9	8.9	7.6	7.9	4.7	5.1
Construction	6.2	5.7	3.5	0.7	1.7	3.0	5.7
Wholesale & retail & hotel & restaurant	6.8	5.5	5.7	2.6	3.2	3.8	4.3
Transportation & communication	6.4	7.0	7.6	8.9	7.4	8.3	6.1
Financials & real estate	3.9	3.4	2.7	2.0	2.7	3.2	3.4
Services	1.3	1.6	2.3	2.7	2.4	1.5	1.2

Source: Nomura Research Institute Singapore, official statistics

**Private consumption index**

Source: Nomura Research Institute Singapore, CEIC

## The Philippines' economy: forecast cuts

### *Solid GDP growth in 3Q02*

The Philippines' real GDP growth in the 3Q02 was a solid 3.8% y-y. The rate is off 2Q02's 4.8%. But by category, the growth rate of private consumption (about 80% of GDP) expanded by 4.1% y-y and capital formation by 5.4% y-y: these rose by 3.7% and 3.6%, respectively, in the previous quarter. The contribution by inventory investment was down by 1.8% y-y.

### *Our view on the Philippine economy is largely unchanged*

There is no significant change in our view on the Philippines economy. For 2003, while private consumption should fall slightly in 1H03 as El Niño hits agricultural output, it should pick up in 2H03 as exports and capital investment rise. But against our previous forecast, the pace of recovery in the electronic products market (about 50% of exports) will likely remain weak, and the attack in Bali should hurt consumer and corporate sentiment. In line with these trends, we have revised our estimate for GDP growth to 3.6% from 4.0%. For 2002, we maintain our forecast of 3.9% taking into consideration the upward revision in 2Q02 performance.

CPI rose by less than 3% over July to November. We see inflation ticking up from here, pushed by higher prices for oil and produce.

### *Interest rates should see little upward pressure...*

On interest rates, the benchmark 91-day T-bill rate will likely rise in line with the moderate increase in CPI. In this case, the risk factor is a serious fiscal deficit. The deficit has been expanding faster than expected owing to lagging tax receipts. In light of this, S&P and Fitch have downgraded their outlook on the sovereign rating to "negative": current ratings are BB+ at each rating agency. The initial financing plan in the 2003 budget was to raise funds mainly overseas to prevent domestic interest rates from rising. Since the fiscal deficit is expected to exceed the initial plan, and as the rating agencies have downgraded their outlooks, the revised plan features a greater amount of financing from the domestic market. In view of the ample liquidity in the domestic financial market, upward pressure on interest rates should be limited.

### *...and we look for a broadly stable peso in 2003*

As far as the exchange rate is concerned, the current-account surplus and the increase in foreign reserves are factors supporting a rising peso. An expected weaker yen and stronger US dollar would suggest a weaker peso. We think the two sets of trends will offset one another and expect the exchange rate to remain around the current level of P52-53:US\$1.

Hideki KISHIDA

**Short-term economic outlook**

<b>(y-y, %)</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002E</b>	<b>2003F</b>
Real GNP	3.7	4.8	3.4	4.1	3.8
Net factor income from abroad	10.1	12.8	7.2	7.0	6.8
Real GDP	3.4	4.4	3.2	3.9	3.6
Private consumption	2.6	3.5	3.6	3.5	3.1
Gov.consumption	6.7	6.1	0.3	(0.6)	(1.1)
Capital formation	(2.3)	3.1	(2.2)	1.4	1.1
External demand (contribution to growth)	3.0	5.3	(2.0)	0.9	0.5
CPI	6.7	4.3	6.1	3.1	3.9
Current account (US\$bn)	73.6	90.5	46.0	49.0	59.1
(% of GDP)	9.7	12.1	6.4	6.5	7.4
P:US\$1	39.1	44.2	51.0	51.6	52.6

Source: Nomura Research Institute Singapore, official statistics

**Budget outlook (national government)**

<b>(Pbn)</b>	<b>2002</b>		<b>2003</b>	
	<b>(budget)</b>	<b>(estimate)</b>	<b>(initial)</b>	<b>(revised)</b>
Fiscal surplus (deficit) (A)	(130.0)	(223.0)	(142.1)	(202.0)
(% of GDP)	(3.3)	(5.6)	(3.3)	(4.7)
Revenue	624.3	550.6	640.7	584.1
y-y (%)	10.7	(2.3)	16.4	6.1
Expenditure	754.3	773.6	782.8	786.1
y-y (%)	6.1	8.8	1.2	1.6
Non-budgetary accounts and change in cash (B)	18.2	(27.2)	5.5	1.4
Net financing-(A+B)	111.8	250.2	136.6	200.6
Domestic (net)	63.3	172.0	40.5	100.5
Gross domestic borrowing	128.8	247.1	142.1	202.1
Less: amortisation	65.6	75.1	101.6	101.6
External (net)	48.5	40.1	96.1	100.1
Gross external borrowing	138.6	133.1	182.8	188.5
Less: amortisation	90.0	93.1	86.6	88.3

Note: (1) The initial programme for 2003 is as of July 2002.

The estimation for 2002 and the revised programme for 2003 are as at November 2002

(2) The y-y in 2002 budget is against actual in FY01

(3) The y-y in initial and revised programmes for 2003 are against estimation for 2002

Source: Philippines Department of Finance, NRI Singapore

## Thailand's economy: private demand holding up

*An economy showing solid, stable growth*

Thailand's economy remains on a well balanced up-trend, driven by the three engines of growth: exports, private consumption and private investment. We expect 2002 GDP will see a 4.8% rise. Here, our previous forecast is unchanged. We have cut our forecast for 2003 to 4.3% from 4.7%, reflecting the weaker external environment and the impact of the attack in Bali.

*Even with less support from the banks, we think private consumption will hold up*

Private consumption remains strong, as shown by automobile sales (by unit), which rose by 54.4% y-y in October. Stimulated by government policy and as a result of the rising prices of agricultural products, rural income is rising. Furthermore, urban consumption has remained strong on the expansion of consumer finance. For the coming year, while the pace of expansion should slow in 1H03, we see a pick-up in 2H03. We believe the November move by the Bank of Thailand to tighten regulations on issuing credit cards is an appropriate means of maintaining market health long term. However, there will be a short-term effect, as the ability to offer credit by non-bank financial institutions will weaken.

*Still attracting strong private investment inflows*

Private investment has been a standout in Asean and investment in construction and plant and machinery is increasing steadily. This reflects a continuing in-flow of FDI in areas including the automobile sector. We expect this trend to continue in 2003.

*We expect the baht to strengthen over the year*

In fiscal policy, backed by strong private demand, the central government has already shifted to a cautious stance. It is likely, though, that the government will take additional measures if the external environment worsens unexpectedly. However, we believe the risk of sharp slowdown in the local economy is low.

On the consumer price side, we expect full-year CPI to rise by 2.1% — an assumption that builds in the rise in value-added tax from 7% to 10% from October 2003.

Since domestic demand remains strong, the current account surplus for 2003 should shrink to 2.5% of GDP. However, with FDI in the automobile industry expected to remain strong, we anticipate the baht will appreciate slightly against the US dollar.

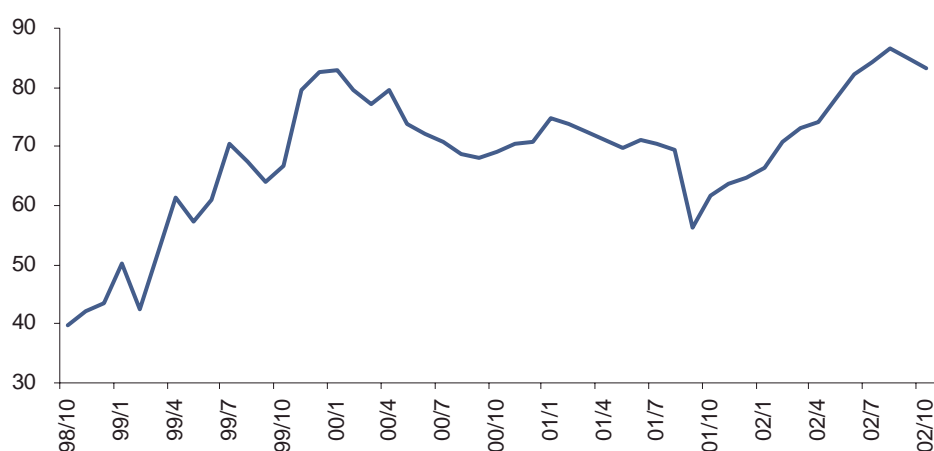
**Tomo KINOSHITA**

**Short-term economic outlook**

(y-y, %)	1999	2000	2001	2002E	2003F
Real GDP	4.4	4.6	1.8	4.8	4.3
Private consumption	4.3	4.9	3.4	4.4	4.9
Government consumption	3.2	2.6	1.6	(0.6)	(0.8)
Fixed capital formation	(3.2)	5.5	0.8	6.9	6.7
Increase in stocks (contr to real GDP growth)	2.3	1.1	(0.0)	0.4	0.9
Exports	9.0	17.6	(4.2)	8.4	5.3
Imports	10.5	27.3	(8.3)	10.1	8.2
Errors and omissions	(0.7)	0.7	(1.7)	0.0	0.0
Contribution of domestic demand	4.2	5.0	2.1	4.1	4.8
Contribution of external demand	0.9	(1.1)	1.4	0.6	(0.5)
CPI	0.3	1.6	1.6	0.8	2.1
Current account (US\$bn)	12.5	9.3	6.2	5.0	3.3
(as % of GDP)	10.2	7.6	5.4	4.0	2.5
THB:US\$1 (period average)	37.8	40.1	44.4	43.0	43.1

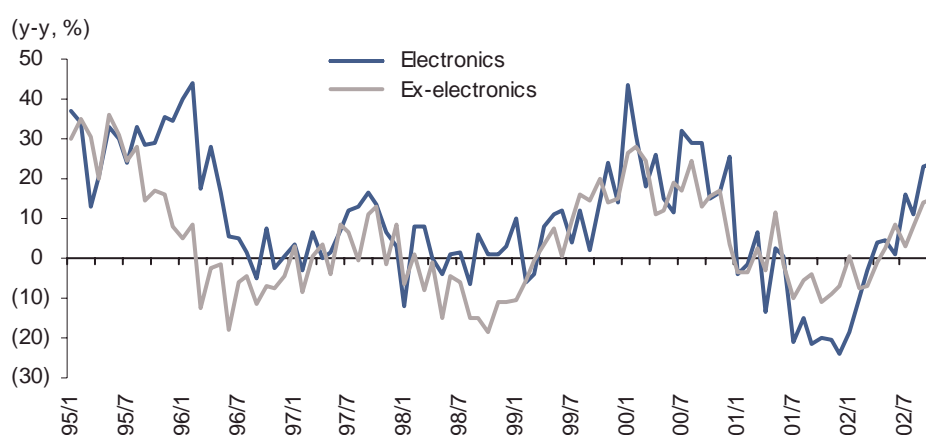
Source: Nomura Research Institute Singapore, official statistics

**Consumer sentiment index**



Note: Consumer survey on economy by Thai Chamber of Commerce  
 Source: Nomura Research Institute Singapore, CEIC

**Exports (US\$bn)**



Source: Nomura Research Institute Singapore, official statistics