



McKinsey & Company



ASEAN Insights: Regional trends

June 2016



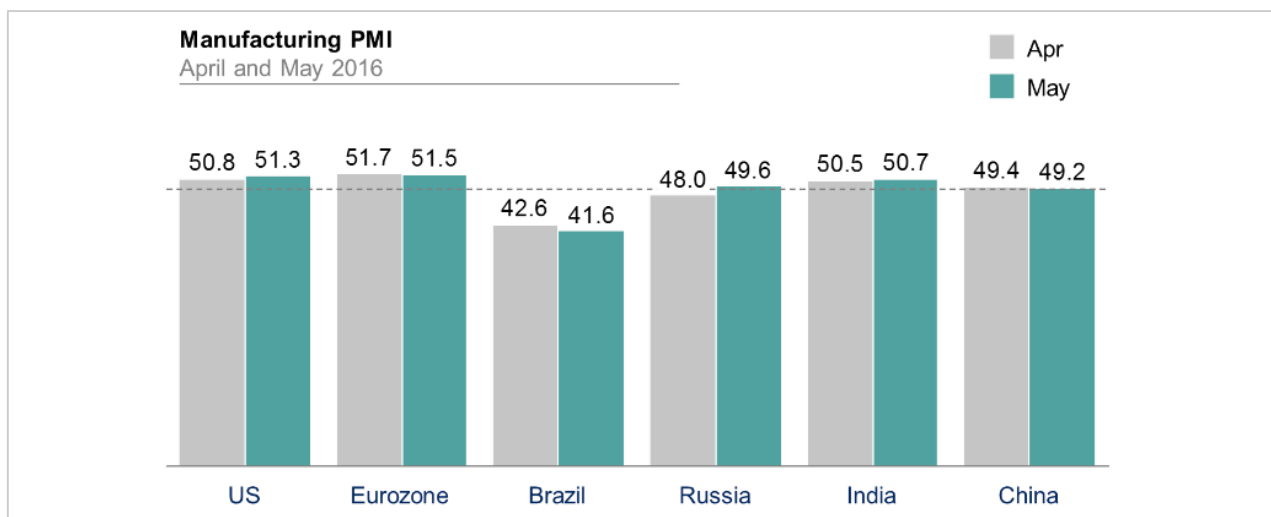
1. Global trends

GLOBAL GROWTH REMAINS STABLE BUT IN LOW GEAR

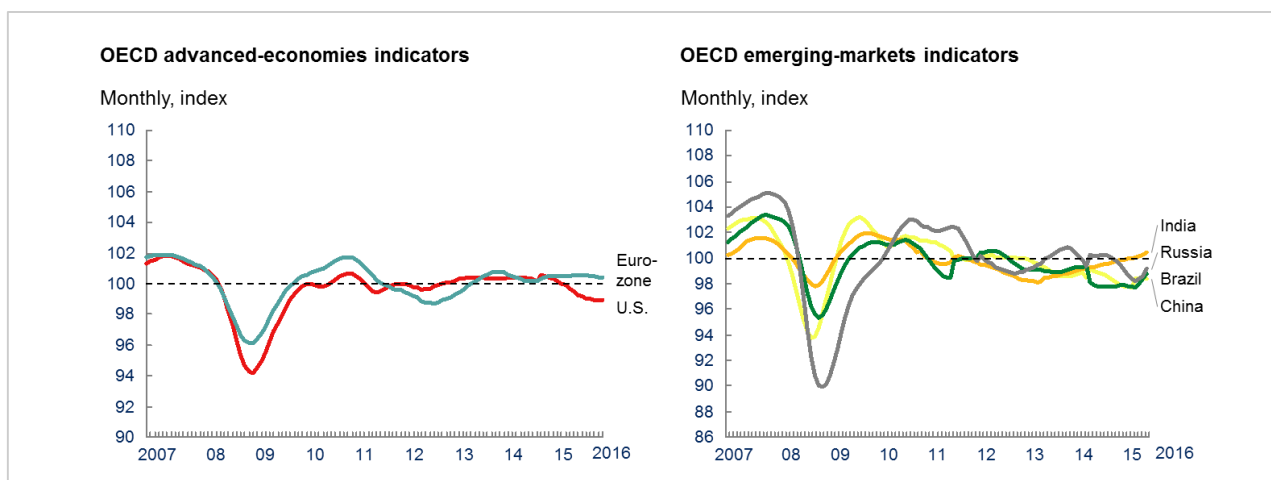
The global economy continued on a low-growth track in June, clouded by mixed signals for Q2 2016 and worries about the fallout from the Brexit referendum. The United States posted a revised first-quarter growth rate of 0.8% (up from an initial figure of 0.5%), while the Eurozone registered annualized quarter-on-quarter growth in Q1 2016 at 2.2%. Both overall growth figures were driven by consumer spending, which grew strongly again in May.

In terms of leading indicators, the global purchasing managers indices (PMIs) remain in expansion territory—with services at 51.4 and the manufacturing PMI decelerating slightly by 0.2 points to 51.1. Consumer confidence across most regions increased, albeit only slightly, reflecting subdued global economic stabilization.

Manufacturing PMIs in advanced economies remain in expansion territory, although manufacturing conditions in China continue to remain challenging¹



Key global economies show signs of improving outlook and emerging growth momentum²



1 Note: A reading above 50.0 indicates an increase from the previous month and a reading below 50.0 indicates a decrease. The country-level data are the PMIs for individual countries as sourced from Markit Economics or the Institute for Supply Management.
 2 Composite leading indicators (CLIs): CLIs attempt to identify turning points in economic activity approximately 6 months in advance. The horizontal line at 100 shows the long-term trend in industrial production (the reference series). An increase above 100 indicates expansion; a decrease, but still above 100, indicates a downturn; a decrease below 100 indicates a slowdown; and an increase below 100 indicates a recovery.

BREXIT REFERENDUM CONCLUDES WITH AN UNEXPECTED “LEAVE” VOTE

On June 24, the United Kingdom voted to leave the European Union. Reactions to the result have been both swift and severe.

Financial markets reacted negatively, with the pound falling more than 10% against the dollar to reach 1.32 USD/GBP—a level not seen since 1985 although it has seen recovered. Equity markets have also been adversely affected, with the FTSE 100 index falling more than 8% on the morning of the vote led by a decline in banking stocks. A global decline of stock markets followed suit thereafter.

The political fallout has also been severe, with Prime Minister David Cameron resigning in the aftermath of the vote. Domino effects are anticipated, with a potential second Scottish referendum to leave the United Kingdom becoming a major possibility.

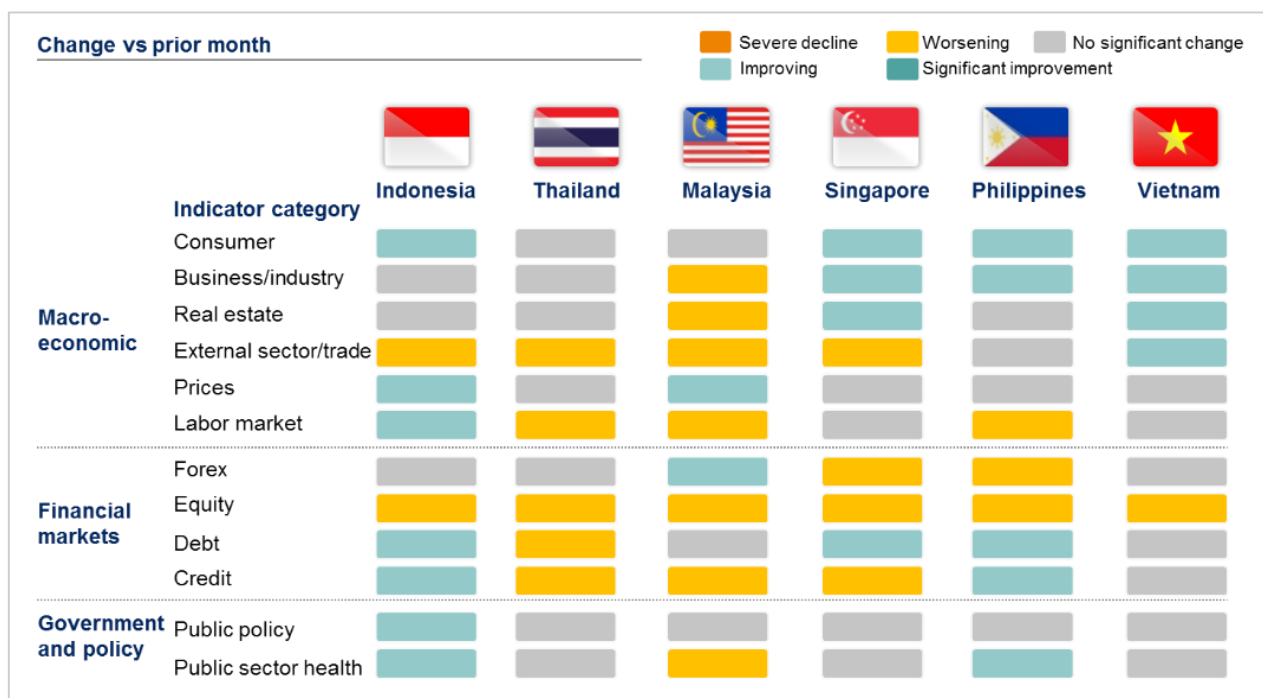
Going forward, the consensus view for the United Kingdom’s economic outlook is unfavorable. IHS has slashed its UK GDP forecasts from 1.9% to 1.5% for 2016, 2.4% to 0.2% for 2017 and 2.3% to 1.3% for 2018, noting that the country will face major economic and political uncertainties which will dampen business and household confidence, adversely impairing corporate investment, employment, and consumer spending.



2. Regional trends: ASEAN

A MIXED MONTH AS DOMESTIC CONDITIONS IMPROVE BUT TRADE CONDITIONS REMAIN CHALLENGING

Trade volumes fell across the region; domestic conditions continue their improvement from last month with the exception of Thailand and Malaysia where conditions remain challenging



Overall, ASEAN recorded a mixed month. Most countries saw an improvement in their domestic conditions, but external indicators reflect a challenging environment with exports generally declining.

Macroeconomic trends

Trends are generally more positive on the domestic front, with the exception of Malaysia and Thailand. Singapore was a surprise positive performer with a better-than-expected improvement in industrial production (+2.9% year-on-year in April versus consensus -0.3%), while Vietnam and Philippines continue to post encouraging signs of growth with both consumer and business conditions improving. However, Malaysian conditions remain challenging as manufacturing production missed expectations (2.9% year-on-year vs consensus 3.5%) and the PMI slid further into contraction to 47.2 from 48.1.

In terms of the external economy, exports generally remain depressed (with the exception of Vietnam). Thailand recorded a second month of contraction, recording a -4.4% growth in exports, led by a large drop in exports of industrial goods and slowing trade with China.

Financial markets

Regional equity markets remain volatile as the results of the Brexit referendum continue to weigh upon markets. All ASEAN equity markets posted losses following the results, with Singapore's Straits Times Index posting the largest losses at -2.3%

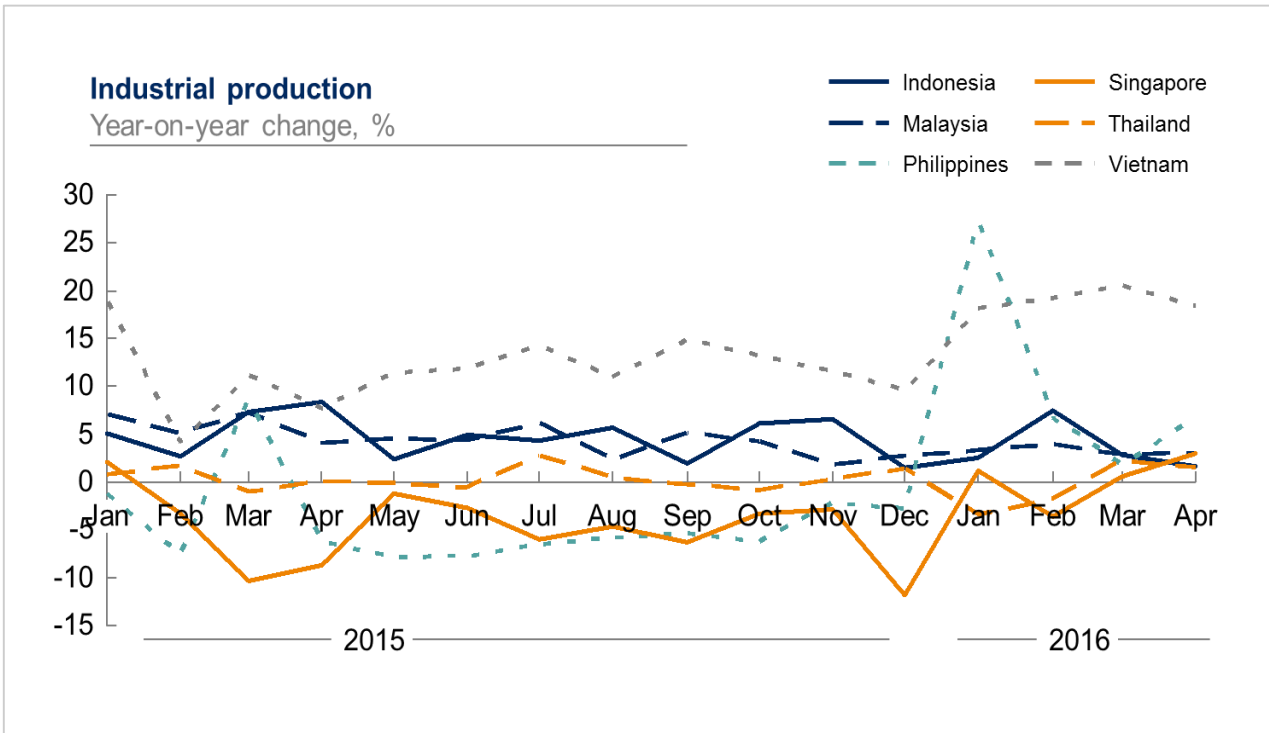
Government and policy

In other key developments, Bank Indonesia (BI) adopted further easing measures by cutting its benchmark rate by 25 bps from 6.75% to 6.50%. While unexpected, a stabilizing rupiah and low inflation have provided room for BI to execute its fourth rate cut in seven months.

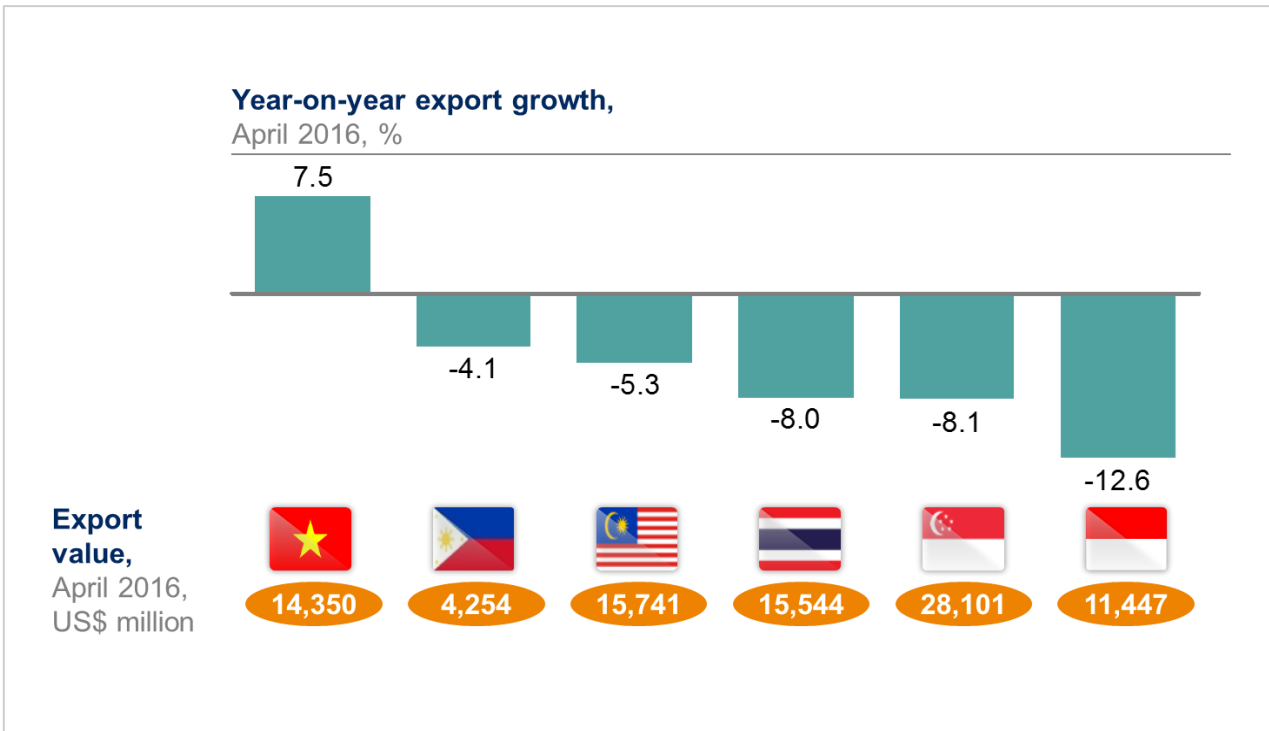
Incoming Philippines President Rodrigo Duterte has announced his new cabinet. Among the priorities announced are reforms to the tax structure and tax administration, increased spending on infrastructure and a relaxation of foreign ownership limits.

Meanwhile in Malaysia, Prime Minister Najib Razak has reshuffled his cabinet, with two Members of Parliament being promoted to full ministerial posts.

On the domestic front, industrial production is generally stabilizing with all countries returning to positive growth.

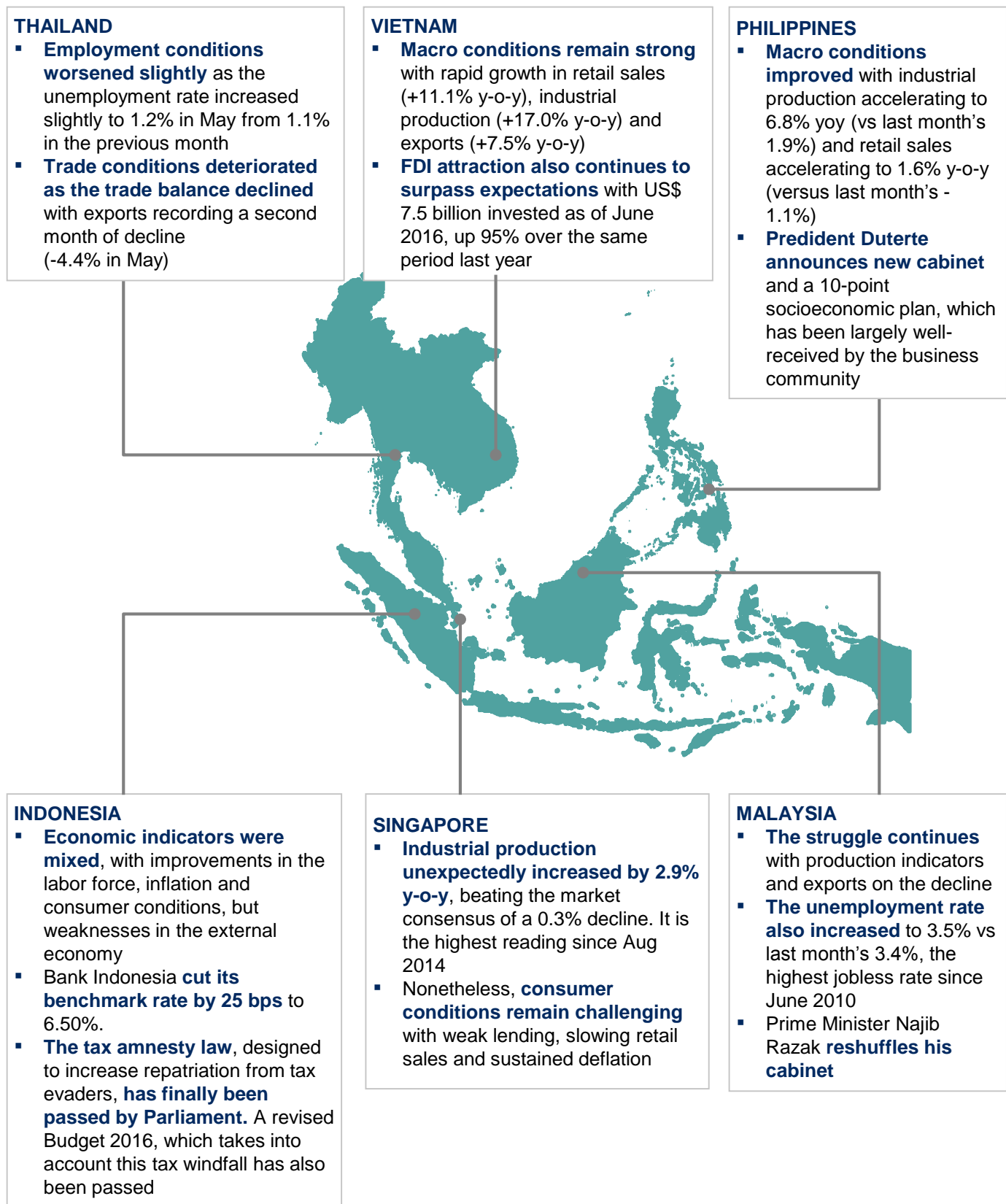


However, trade conditions remain challenging as exports continue to deteriorate



3. ASEAN Insights: Country analysis

THE REGION AT A GLANCE



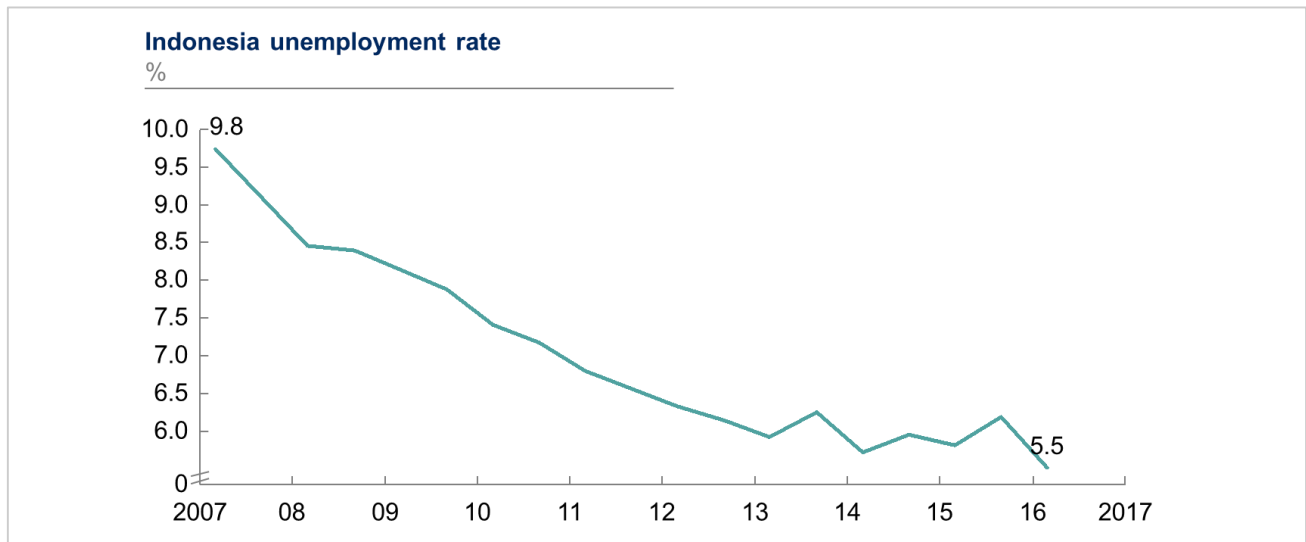
MIXED SIGNALS FROM ECONOMIC INDICATORS; BANK INDONESIA CUTS RATES

Indonesia experienced a mixed month.

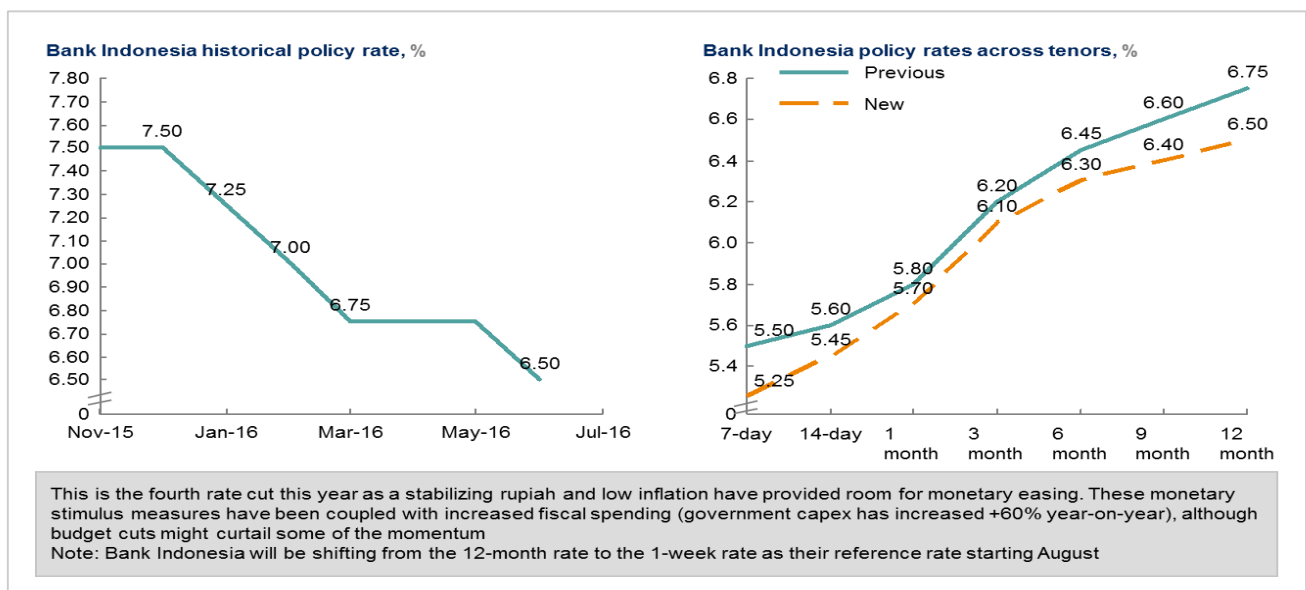
On the positive side, aspects of the real economy are improving. The unemployment rate for Q1 2016 saw a marked improvement, falling to 5.5% vs the previous quarter's reading of 6.2%, while inflation remains manageable, slowing to 3.3% in May from 3.6% in April. Meanwhile, consumer confidence in May increased to 112 vs the previous month's 109.

However, some dark clouds remain as business conditions appear to be weakening. The trade surplus declined to US\$376 million in May from the previous month's US\$662 million, as exports remained flat but imports rose, mainly on increased fuel imports as fuel prices begin to recover. Industrial production and retail sales, while still continuing to post strong gains (3.4% and 10.4% year-on-year respectively), have also seen a slowdown in their rate of growth compared with the previous month.

Q1 2016 saw Indonesia recorded its lowest unemployment rate since the global financial crisis



Indonesia continues its stimulus measures with latest round of monetary easing





Malaysia

ECONOMIC CONDITIONS DETERIORATE; CABINET RESHUFFLED



Malaysia’s struggles continue with production indicators and exports on the decline, and with unemployment also creeping upwards.

Industrial production missed expectations, growing 3.0% year-on-year in April vs expectations of 3.5%. On a month-on-month basis, this was a contraction of -0.8%. In terms of leading indicators, the Manufacturing PMI remains firmly in the contraction zone at 47.2.

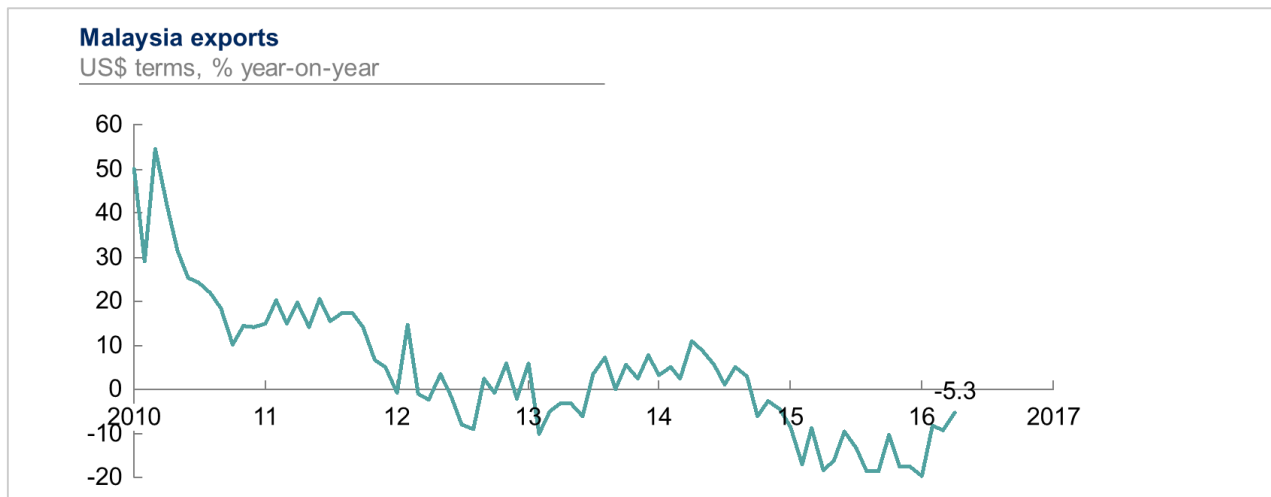
Malaysia’s overall trade volume and balance of trade also saw a decline, with exports reducing faster than imports in April. This is the 19th straight month of contracting exports, extending back to October 2014.

The unemployment rate worsened, recording an increase to 3.6% in April vs 3.5% in March—the highest jobless rate since June 2010.

However, some silver linings are expected going forward. With commodity prices recovering, oil exports are expected to prop up Malaysia’s trade balance, while also being a positive catalyst for mining-related manufacturing output.

On the political front, Prime Minister Najib Razak announced a number of changes to his cabinet, appointing two full ministers and four new deputy ministers. Key appointees include a new Second Finance Minister (MP Johari Abdul Ghani) and a new Minister for Urban Wellbeing, Housing and Local Government (MP Noh Omar).

Malaysian exports have experienced 19 straight months of contraction



ECONOMIC GROWTH ACCELERATES; PRESIDENT DUTERTE ELECTS NEW CABINET

Domestic conditions in the Philippines improved strongly.

In terms of business activity, industrial production accelerated, recording 6.8% growth year-on-year in April vs the previous month's 1.9%. This is the fourth consecutive month of positive growth, following a protracted decline last year (due to base effects).

On the consumer-end, retail sales continued to accelerate, growing at 1.6% year-on-year in April vs the previous month's 1.1%. Going forward, consumer conditions in the Philippines remain broadly positive with both debt and credit conditions continuing to be supportive of growth, resulting in sustained consumer confidence, increased consumer spending, and increased bank lending.

However, inflation and labor conditions require closer monitoring. The inflation rate, although benign by Filipino standards, now stands at a 13-month high of 1.6%.

The unemployment rate has also spiked to 6.1% in Q2 2016 from 5.8% in the previous quarter, while the underemployment rate has also increased to 18.4% from 17.8%, prompting worry in some quarters.

In terms of political developments, President Duterte has announced his new cabinet comprising a non-traditional mix of candidates. A ten-point socioeconomic plan has also been announced, with its centerpieces being tax reform, FDI attraction measures, and infrastructure spending. The plan has been largely well-received by the business community.

Key economic managers in the new Philippines cabinet



Finance: Mr. Carlos Dominguez

- Former agriculture minister under President Corazon Aquino
- Ex-chief executive of flag carrier Philippines Airlines
- Owns several businesses in Davao City including the biggest hotel and other real estate developments



Budget: Mr. Benjamin Diokno

- Former budget minister under President Joseph Estrada
- Former Undersecretary for Budget Operations under President Corazon Aquino
- An economist by training, he is currently a professor at the University of Philippines School of Economics



Economic Planning: Mr. Ernesto Pernia

- Former lead economist at the Asian Development Bank
- A graduate of University of California's Berkeley, he is a professor emeritus at the University of Philippines School of Economics

Other members

Transport and Communication: Mr. Arthur Tugade

- Head of Clark Development Corp., a government agency tasked to manage the Clark Freeport and Clark Special Economic Zone
- A self-made businessman who founded Perry Group, a conglomerate with holdings in transport and logistics

Public Works and Highways: Mr. Mark Villar

- A congressman whose family owns Vista Land, one of the largest real estate conglomerates

Energy: Mr. Alfonso Cusi

- Former GM of Manila International Airport Authority
- Also served as head of the Civil Aviation Authority and the Philippine Ports Authority under President Arroyo

Agrarian Reform: Rafael Mariano

- Nominee from the National Democratic Front, a group of communist cadres who are allies of Mr. Duterte
- Head of a militant farmers' group that has been pressing for an overhaul of the country's agrarian reform programme

Foreign: Mr. Perfecto Yasay

- Former chairman of the Securities and Exchange Commission
- Testified in the impeachment trial against President Joseph Estrada on charges of corruption

Defence: Mr. Delfin Lorenzana

- Retired major-general, previously led the Army Special Operations unit
- Previously served as a military attache to Washington

Labour: Mr. Silvestre Bello

- Former justice minister under both President Corazon Aquino and President Fidel Ramos

Education: Ms. Leonor Briones

- Former national treasurer under President Joseph Estrada
- Currently a professor emeritus at the University of Philippines

Social Welfare: Ms. Judy Taguiwalo

- Currently a professor in the University of Philippines
- Was a political prisoner under the Marcos regime and is a women's rights advocate



Singapore

POSITIVE SURPRISE IN GROWTH OF INDUSTRIAL PRODUCTION

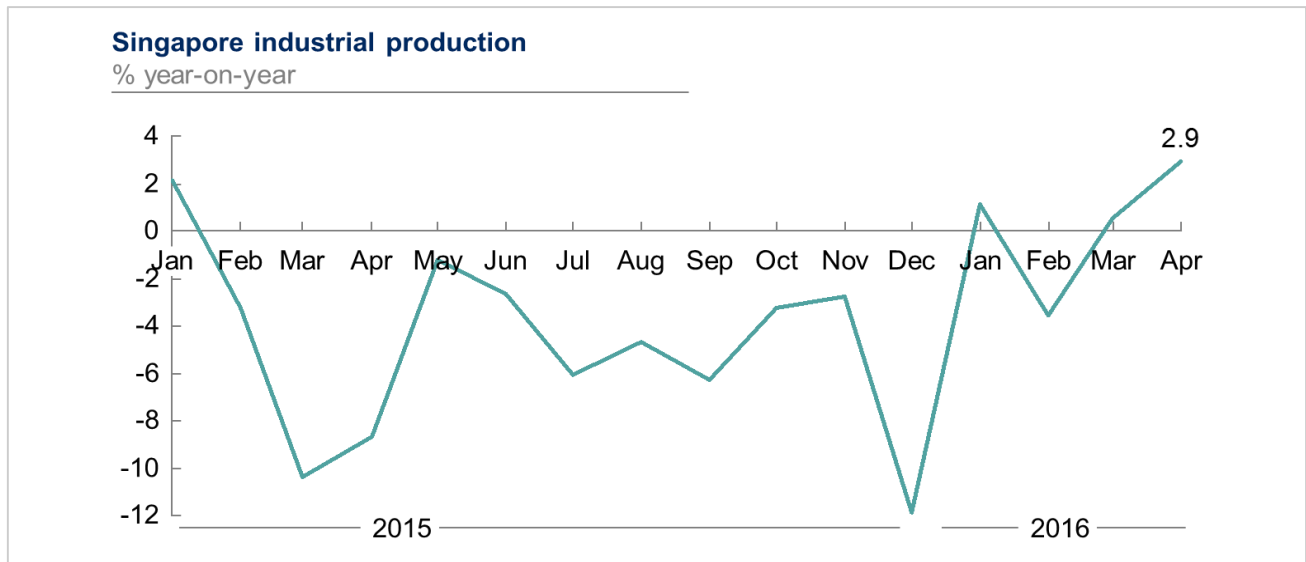
Singapore recorded a positive surprise in its industrial production on the back of increased output from its biomedical manufacturing clusters, surging to 2.9% year-on-year in April vs a consensus estimate of a -0.3% decline. This is the second consecutive month of positive growth following a sustained period of contraction.

However, it remains to be seen if Singapore's growth momentum can be sustained, with the manufacturing PMI continuing on the threshold between expansion and contraction at 49.8.

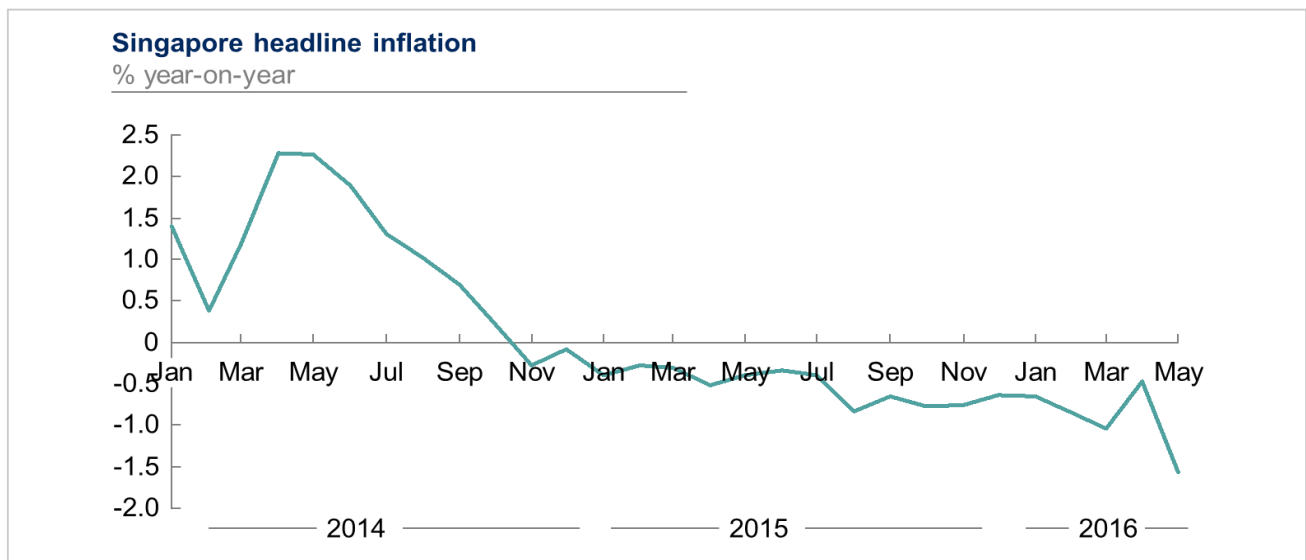
Other macroeconomic indicators, particularly on the consumer front, remain mixed—suggesting that Singapore's prolonged period of poor growth might continue. Credit conditions remain subdued, with bank loans contracting by -0.9% in April. Retail sales, while positive, have also slowed to 3.8% from the previous month's reading of 5.1%.

Meanwhile, deflationary pressures persist. Inflation was recorded at -1.6% in May, the 19th consecutive month of deflation and the sharpest decline since 1986.

Singapore recorded surprise growth in industrial production in April after a prolonged period of contraction



Singapore's deflationary pressures worsen with 19th straight month of deflation





Thailand

INDUSTRIAL PRODUCTION SLOWS: EXPORTS CONTRACT FOR THE SECOND CONSECUTIVE MONTH

Thailand recorded a poor month as the country's recovery continues to stutter.

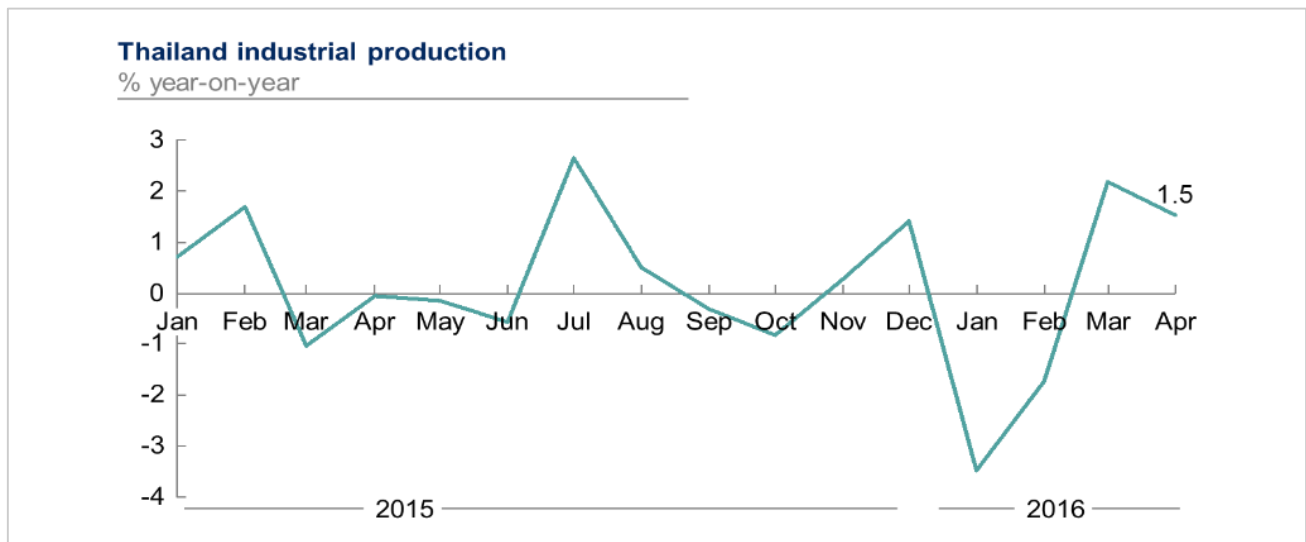
Industrial production slowed to 1.54% year-on-year in April vs March's 1.83%. On a month-on-month basis, this was a -17.46% decline, the first decline this year and the sharpest since October 2011. Nonetheless, this reading still beat market expectations of a 0.8% increase year-on-year.

Exports also contracted for a second month in a row, recording a -4.4% decline year-on-year in

May, largely driven by a drop in outbound shipments to China (-5.9%). China, which until 2015 was Thailand's largest export market, has also lost its top spot to the USA.

In terms of fiscal developments, Prime Minister Prayut Chan-o-cha presented his government's USD 78 billion budget for fiscal 2017 to the National Legislative Assembly, acknowledging that fast-growing project costs will necessitate cuts to other parts of the government budget.

Thailand's industrial production growth has slowed but remains in positive growth territory as the country struggles to sustain a prolonged period of growth



Thailand's merchandise exports to China, its second-largest export market, continue to contract





Vietnam

STRONG GROWTH MOMENTUM MAINTAINED

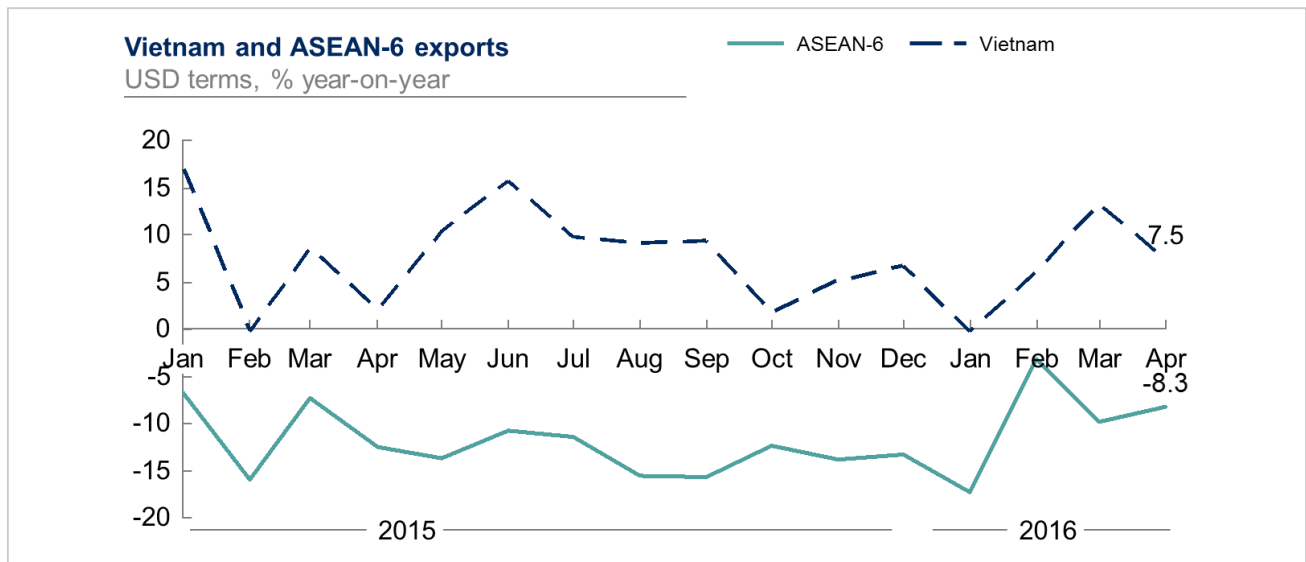
Vietnam continues to be the region's strongest economy.

Its industrial production index continues to grow at double digits, with May recording a year-on-year growth rate of 17.0%. The country's manufacturing PMI has also increased to 52.7 in May from 52.3 in April, suggesting that its growth momentum is unlikely to slow anytime soon.

Vietnam's exports also continue to grow rapidly, recording a year-on-year growth rate of 7.5%—the only country in the region with positive growth.

Increased FDI attraction is likely to fuel this growth going forward. The country has already attracted US\$7.5 billion as of June 2016, up 95% on the same period last year. Approximately 70% of this FDI has gone to the manufacturing and processing sectors, which will likely see increased outputs.

Vietnam's exports have maintained strong growth, despite the region as a whole contracting



FDI into Vietnam has accelerated significantly over the past few months, as the country's recent reforms make Vietnam increasingly attractive to businesses

