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ECONOMIC OUTLOOK (1988-1989) FOR ASEAN COUNTRIES AND ASIAN NIES

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SUMMARY OF ECONOMIC OUTLOOK (1988-1989) FOR ASEAN COUNTRIES AND ASIAN NIES

The Institute of Development Economies maintains the Econometric Link System for ASEAN (ELSA) in which the macro-models of the ASEAN countries (excluding Brunei), Asian NIEs (excluding Hong Kong) and some other countries are interlinked by a trade model. We have made country economic forecasts for this year and next year, using the macro-models.

I) Overview and Estimation of the 1988 Economies

The international economic environment surrounding the four ASEAN countries (Indonesia, Malaysia, the Philippines, and Thailand) and the Asian NIEs (Singapore, South Korea, and Taiwan) has been characterized by the continuous expansion of economics of developed countries, high yen value against the U.S. dollar, falling crude oil prices, and rising prices for non-oil primary products.

As in 1987, the robust economics of developed countries this year have boosted the manufactured exports of this region, which are heavily dependent on external demand, especially the United States, EC and Japan.

Also, the continued strong yen against the U.S. dollar situation had brought drastic increases in exports from South Korea and Taiwan to developed countries and accelerated direct investment by Japan and other advanced countries in the Asian NIEs in 1986 and 1987. Hence, the Taiwanese yuan and South Korean won have been appreciated against the U.S. dollar since 1986 and 1987 respectively. In addition, the Singapore dollar started to be appreciated against the U.S. dollar in October, 1988. The appreciation of the Asian NIEs' currencies have strengthened international competitiveness of the ASEAN countries and caused large increases in their manufactured exports. The appreciation of Asian NIEs' currencies against the U.S. dollar has shifted Japanese and other developed countries' overseas direct investments from these economies toward the ASEAN four countries. Moreover, the Asian NIEs, themselves, are now increasing their direct investments to the ASEAN four countries.

The drop in crude oil prices, coupled with the appreciation of the Asian NIEs' currencies, has contributed to their domestic price stability. In the meantime, oil producing Indonesia and Malaysia are performing solidly in exports of non-oil, non-gas primary products as well as manufactured goods. Thus, despite the oil price decline, they have escaped the kind of damage they suffered in 1986.

Recovery of prices for non-crude oil primary products (rubber, rice, vegetable oils and others) has partly contributed to an economic expansion of Malaysia, Thailand and the Philippines.

Considering these factors in our model simulations, we forecast, among Asian NIEs, two-digit growth for South Korea and Singapore, both enjoying rising demand at home and abroad, though the growth rate for Taiwan we anticipate dropping to 6.8% or about half the previous year's figure. The four ASEAN countries will attain higher growth rates than in 1987 due to growing exports of non-oil primary products and manufactured goods and active direct investment from overseas. Thailand in particular should manage an extremely high growth rate of 11.2%.

II) Economic Outlook for 1989

In 1989, the economic growth rate of developed countries will lose a little momentum, causing the export growth rates of the Asian NIEs and the ASEAN to slacken to a certain extent. The prices of primary products including crude oil are expected to level out at, or slightly fall short of the 1988 levels. While the yen vis-a-vis the U.S. dollar rate is expected to continue in the current range; i.e., around 120 yen per dollar. The South Korean won is likely to appreciate 10% against the U.S. dollar, while the Taiwanese yuan and Singapore dollar will be higher against the U.S. dollar by 5%. The South Korea and Taiwan will shift from a highly export-dependent growth pattern to the one with relatively more reliance on domestic demand. In the ASEAN four countries, on one hand, we cannot expect vigorous production and exports of primary commodities as vivid as in 1988. On the other hand, however, exports of manufactured goods and direct investments from overseas are expected to continue vigorous in 1989 in these countries. As a result, in our forecast, South Korea, Singapore, and Thailand are expected to see their growth rates decline from two-digit figures in 1988 to 8-9% in 1989 but the other countries and region are likely to register growth rates about as high as in 1988.

In summary, the economies of this region will expand smoothly in 1989, showing increased inter-dependence amongst themselves as well as between themselves and Japan through expansion of trade and foreign direct investments.

Real Growth Rates and Inflation Rates in ASEAN and Asian NIEs (%)

	Growth rates (1)			Inflation rates (2)		
	1987(3)	1988(4)	1989(4)	1987(3)	1988(4)	1989(4)
Indonesia	3.6	4.3	5.0	15.4	10.8	11.7
Malaysia	5.2	8.3	7.3	7.7	1.6	0.8
Philippines	5.2	6.4	6.6	7.1	10.2	10.1
Thailand	7.1	11.2	9.5	3.9	7.6	8.1
Singapore	8.8	11.4	8.6	0.9	1.3	1.7
South Korea	11.1	11.5	8.8	3.7	4.3	4.2
Taiwan	12.4	6.8	7.1	0.5	1.1	2.7

Notes: (1) The economic growth rates are GDP growth rates in real terms.
(2) Measured by GDP deflator.
(3) Actual figures for 1987.
(4) Estimates for 1988 and 1989.

Indonesia

	1987	1988	1989
GDP growth rate (%)	3.6	4.3	5.0
Inflation rate (%)	15.4	10.8	11.7

(Actual figures for 1987)

The Indonesian economy, having been forced to carry out drastic adjustment of its economic structure following the sharp decline in the crude oil price in 1986, has entered into a phase of gradual economic growth by lessening its dependence on exports of crude oil and natural gas.

With the easing of restrictions on foreign direct investments and the appreciation of the Japanese and Asian NIEs' currencies against the U.S. dollar, their investments in Indonesia sharply increased in 1987 and further accelerated in 1988, especially those from Asian NIEs. These direct investments are primarily in the export sector where Indonesia has comparative advantages in terms of abundant low wage labor. Thus, Indonesia's manufactured exports (which accounted for 27% of the total exports in 1987) are expected to make a spectacular 50%-plus increase (in nominal terms) in 1988. In the meantime, the crude oil price dipped from $17 in 1987 to $15 in 1988, and the share of crude oil and natural gas in the country's exports will certainly fall from 50% in 1987 to approximately 40% in 1988. The fiscal budget is still tight due to diminishing oil-related revenues and growing burdens of debt-services, making it difficult for the government to increase its public investments to stimulate economic activities. Economic management thus having to depend largely on the activation of private business, the government is taking steps to ease restrictions on foreign direct investment, deregulating the financial system, and liberalizing trade restrictions. In addition to the above-mentioned situations, if we consider the fact that the rupia is being devalued at a modest annual rate of 5% or so and that the government is cautiously controlling the money supply, we forecast that the GDP growth rate in 1988 will turn out to be 4.3%, slightly up on the 1987 figure, with a 10.8% inflation rate in terms of the GDP deflator.

In 1989, whereas developed economies may slow down somewhat, Indonesia's GDP growth rate is expected to rise to 5.4% assuming that the crude price stays in the neighbourhood of 15 U.S. dollar per barrel, supported by an expansion of production capacity induced by active foreign direct investments and robust domestic investments. The inflation rate, however, will rise to 11.7% owing to internal and external demand pressures.

Malaysia

	1987	1988	1989
GDP growth rate (%)	5.2	8.3	7.3
Inflation rate (%)	7.7	1.6	0.8

(Actual figures for 1987)

In 1988 the worldwide demand has been active for rubber, palm oil, and lumber, all important export items for Malaysia. In fact, Malaysia has succeeded in increasing its exports and production of these products in 1988. Manufactured goods capturing an expanding share in the country's export drive also continue to grow in the year. Consequently, Malaysia sees its exports jump by 15% in real terms. Direct investments from Japan and Asian NIEs have been mounting since the third quarter of 1987, centering on the manufacturing sector. The government has switched to a lax fiscal policy such as increasing its development expenditures. Taking these factors into consideration, the country's GDP growth rate is estimated to be 8.3% in 1988. In the meantime, the inflation rate, measured by the GDP deflator, is predicted to be 1.6% mainly because unemployment still remains high at 9%, and therefore, the rate of wage increases is held down.

In forecasting the 1989 figures, it is assumed that the price of crude oil and other primary product will either level at, or be slightly lower than the 1988 figures. Also, Malaysia's exports of manufactured goods are assumed to increase continuously in 1989, though at a slower pace than in 1988. As tax revenues are growing, the government plans to increase further public investments and other expenditures. Another presumption for our forecast is that the corporate tax rate will be reduced to 35% from 40% in 1989. On these assumptions, we forecast GDP growth rate at 7.3% and the inflation rate at 0.8%.

The Philippines

	1987	1988	1989
GDP growth rate (%)	5.2	6.4	6.6
Inflation rate (%)	7.1	10.2	10.1

(Actual figures for 1987)

The GDP in real terms in the first half of 1988 grew 6.0% over the same period of the previous year, indicating that the Philippines economy as in the previous year (an annual growth rate of 5.2%) was in a steady process of recovery mainly guided by the IMF conditionality. Accountable for this recovery are first, at large increase in investments by private business (up 14.6% in the first half of 1988 from a year earlier, in real terms), second, growing commodity exports (up 8.4%) and third, the expansion of government investments (up 9.1%).

The above trends that characterized the first half of 1988 will be carried into the second half and the annual private investment is expected to increase by 15%, commodity exports by 9% and government investment by 10%. However, the exports of services have been sluggish, such as revenues from tourism dropping sharply, causing the annual service export revenue to fall by 12%. Taking these into consideration, the real GDP growth rate in 1988 is estimated at 6.4%. Given the still-prevailing shortfall of production capacities, even this modest economic growth will tighten domestic market conditions. For this reason the inflation rate measured by the GDP deflator is estimated to be as high as 10.2%.

For 1989, active private investments coupled with a slight decline in merchandise exports are foreseen. Government investments are supposed to increase 9% mainly for industrial infrastructure while government consumption spendings are also assumed to grow 9%. Considering these factors, the 1989 GDP growth rate is estimated at 6.6% and inflation rate at 10.1%.

Thailand

	1987	1988	1989
GDP growth rate (%)	7.1	11.2	9.5
Inflation rate (%)	3.9	7.6	8.1
(Actual figures for 1987)			

Thailand is expected to achieve an annual economic growth rate of 11.2% in 1988, the first two-digit growth in 10 years. There are mainly two factors accounting for this high growth. The first is brisk private investment mainly from abroad and the second is the drastic increase in exports of industrial products. The investments made since 1987 by now have been turned into effective production capacities. Thailand's exports of manufactured goods are expected to shoot up 35% in 1988. Moreover, the agricultural sector, enjoying good harvest, is estimated to increase its output by an impressive 9% this year. A rapid expansion of internal and external demand and rising import prices, however, contribute to a price rise, resulting in the inflation rate, measured by the GDP deflator, reaching 7.6% in 1988.

A high growth rate is also forecasted in 1989. In the manufacturing sector, direct foreign investments on an approval basis increased three-fold in 1988. Most of these approved investments will be implemented in 1989. The fiscal 1988/1989 budget, effective as from October 1988, is 17% larger than that of the previous year as the government is going to build infrastructure to cater for burgeoning investments and production and to raise public employees' salaries. This is another factor supporting high growth. One negative factor to the economic growth is that agricultural and mineral production will remain almost the same as in 1988, and therefore, will grow modestly. Considering all these, we estimate a GDP growth rate of 9.5% which, however, will be accompanied by an inflation rate of 8.1%.

Singapore

	1987	1988	1989
GDP growth rate (%)	8.8	11.4	8.6
Inflation rate (%)	0.9	1.3	1.7
(Actual figures for 1987)			

The Singaporean economy in 1988 enjoys a large increase in output and exports of manufactured goods. The output of manufactured goods rises 20% and their export 30% over the year. Also, the commercial sector has been expanding by two-digits every quarter since the third quarter of 1987.

Three factors mainly account for the robust exports: first, the improvement of Singapore's international competitiveness due to the wage constraint since 1986 as well as to the appreciation of the South Korean and Taiwanese currencies against the U.S. dollar; second, worldwide demand for semiconductors and office machines, for which Singapore has comparative advantages, is expanding rapidly; and third, Singapore's capacity to supply these products is growing thanks to increasing foreign direct investments from Japan, the United States and other development countries. Reflecting the burgeoning exports, Singapore's GDP is estimated to grow by an impressive 11.2% in 1988. In the meantime, the general prices measured by the GDP deflator, is forecasted to be a 1.3%. The price increase reflects the recent relaxation of the wage freeze policy, which has resulted in the average wage rate to rise 5%.

In 1989 the economy will continue to expand relying mainly on external demand, but the growth rate is forecasted to be lowered to the 1987 level of 8.6%. The major constraint on growth is the tight labor supply. This bottleneck is already evident in 1988, but in 1989 the situation is likely to become more serious as the government will increase the levy on employing foreign workers.

In the meantime, the prices will rise by a modest 1.7%. Increases in import prices and wages will combine to raise prices, but the price rise will be contained below 2% as the monetary policy is basically anti-inflationary.

South Korea

	1987	1988	1989
GDP growth rate (%)	11.1	11.5	8.8
Inflation rate (%)	3.7	4.3	4.2
(Actual figures for 1987)			

Although some apprehensions were expressed early this year that a recession might set in after the Olympics, the South Korean economy has been growing smoothly all through 1988. It is true that the sizeable 14% won appreciation against the U.S. dollar has slowed down the pace of export growth. Domestic demand is, however, very active this year. The growth rate of investment is as high as in the previous year due to active investments in equipment modernization to cope with the strong won situation. The consumption boom caused by rising wages over two consecutive years has pushed up private consumption expenditures more than enough to compensate a slight decline in the export growth. Supported by the active domestic demand, the South Korean economy is estimated to achieve a 11.5% GDP growth in 1988. Despite the large wage increase (19% over the previous year on average), the inflation rate measured by the GDP deflator will be 4.3% in 1988, assuming a 20% increase in the money supply (M2) and taking into consideration the won appreciation against the U.S. dollar and the decline of oil prices.

In 1989 the export growth rate will slightly decline as the growth rates of developed economies will lose a little in momentum, and equipment modernization investment will also slow down. Domestic consumption demand is, however, still expected to grow vigorously mainly due to an increase in a real wage rate. The nominal wage is predicted to grow at 10% while prices, especially for imported goods, will be stable because of the appreciation of won and a slightly declining prices of primary commodities. By the end of 1989, the won will appreciate against the U.S. dollar by another 10% to 610 won to the dollar. This would not, however, cause exports to fall drastically since South Korea will adjust its industrial structure and diversify its foreign markets successfully. For these reasons, the GDP growth rate is estimated at 8.8% and the inflation rate at 4.2% in 1989.

Taiwan

	1987	1988	1989
GDP growth rate (%)	12.4	6.8	7.1
Inflation rate (%)	0.5	1.1	2.7

(Actual figures for 1987)

The export growth rate has plummeted in 1988 to 6.6% under the impact of the large scale of currency appreciation and the wage hikes in the two preceding years. Also, lowered import prices and trade liberalization have caused an upsurge in imports. Consequently, net external demand has made a significant negative contribution to the growth rate. Concerning domestic demand, both investments and consumption continue active. Private consumption registers a brisk 10.8% increase owing to a purchasing power increase induced by around 10% wage-hikes and the yuan appreciation as well as by large capital gains caused by the drastic increases in land and stock prices. Private investments continue to grow at a high rate, chiefly in the areas of industrial upgrading, rationalization and pollution-preventive systems. Private investments in 1988 will thus grow 14.9% over the previous year. With all these factors considered, the GDP growth rate in 1988 is estimated to be a 6.8% with a 1.1% inflation rate. The quite low level inflation rate, though it is higher than in 1987, is obtained in spite of the wage hike.

In 1989 about the same export growth rate as in 1988 is envisaged: the effects of another yuan appreciation are likely to be canceled by successful diversification of export markets and upgrading of export products. Public investments are expected to be expanded by a drastic 25%. Assuming these, we estimate Taiwan's GDP growth in 1989 at 7.1%. The general price, in the meantime, will rise 2.7% partly reflecting the two-digit wage increase in the two previous years.