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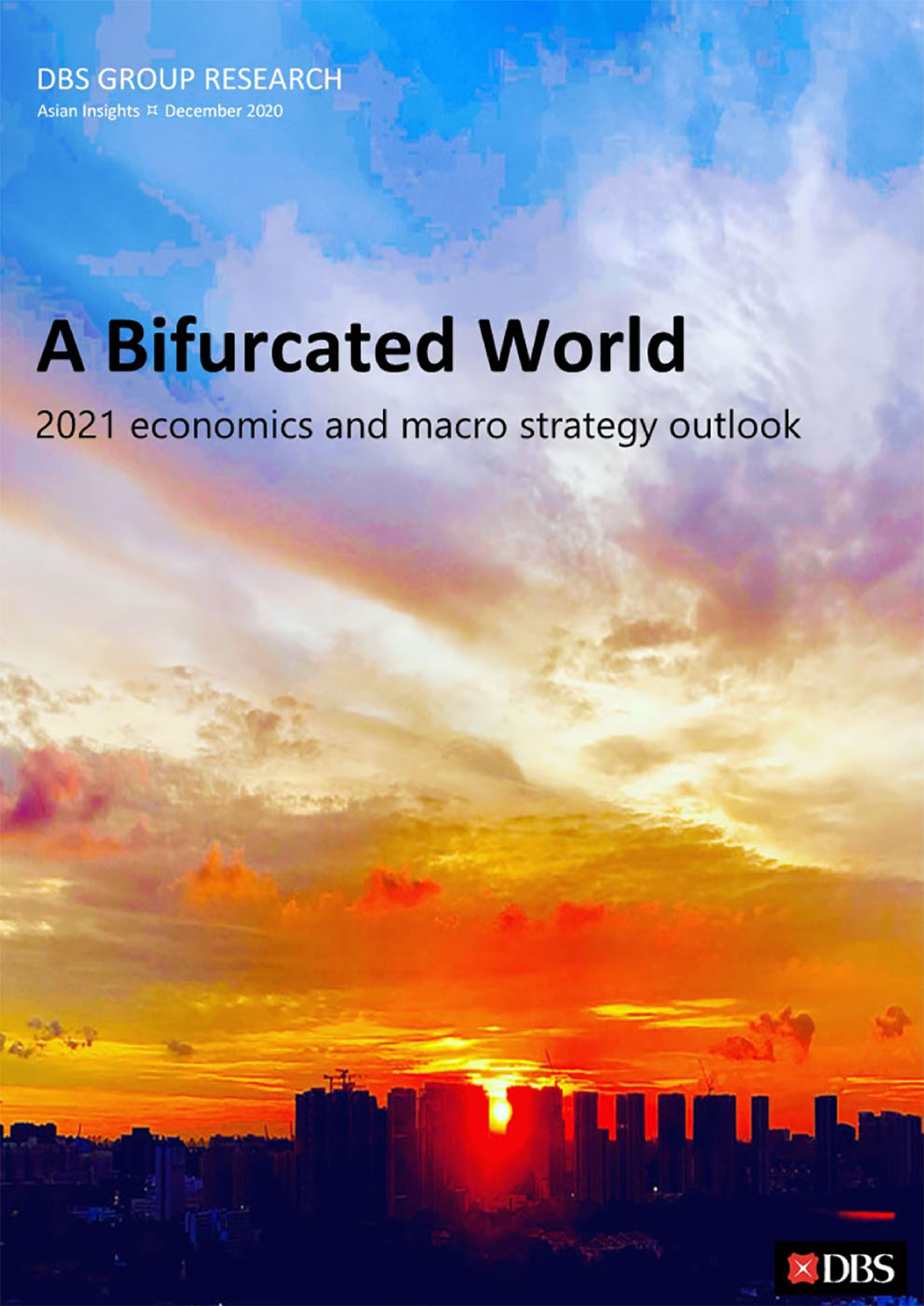
Asian Insights ¤ December 2020

A Bifurcated World

2021 economics and macro strategy outlook



DBS

Economics and Macro Strategy

DBS 2021 Outlook

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Group Research

December 2020

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After a pandemic like no other, and after incurring an extraordinarily large loss of lives and livelihoods, the world will strive to pick up the pieces and move on in 2021. Thanks to the tireless work of scientists and healthcare professionals, both treatments and cures will characterise 2021. We think that Asia is primed for outperformance for three reasons: tailwind from a favourable trade cycle, strong FX buffers and savings, and a strong pull from an accelerating China.

Still, global challenges will remain. Some developing countries outside of Asia could fall into economic and financial crises, contagion from which could be destablising in these shores. Geopolitical tensions may ease but won't disappear. There is an acute need to rise up to generational challenges like climate change, inequality, weak structural growth, aging, and white-collar job displacing technology.

In this publication, we go over detailed overview and forecasts of the countries and asset classes in our coverage.

Investment Strategy
***Rates**: we see steeper DM yield curves, relative outperformance of SGD rates, and rebound in Indo govt bonds. We also see curve flattening in India, rally in CGBs, and wider South Korea-Thailand spreads.*
***Currencies:** We like a basket of Asian high yielding currencies (IDR, INR, PHP) against the USD*
***Credit**: Our picks are Indonesian investment grade USD credit, Indian senior financials, and Chinese real estate and cyclical consumer sectors*
***Equities**: Tailwind for Asian stocks likely as earnings rebound. Valuation and growth differential metrics also favour Asian equities.*

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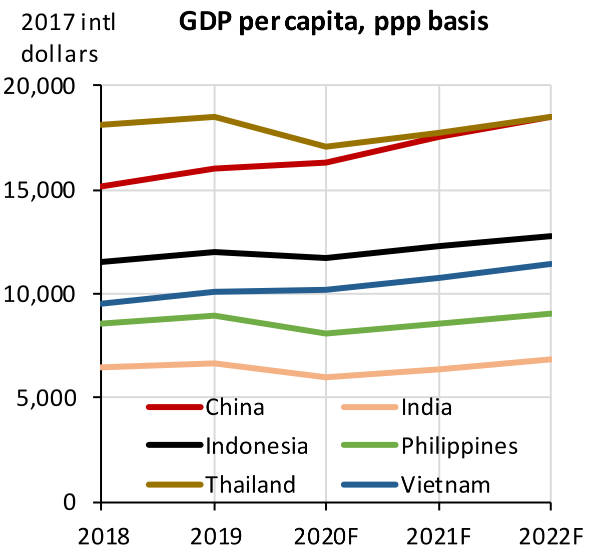
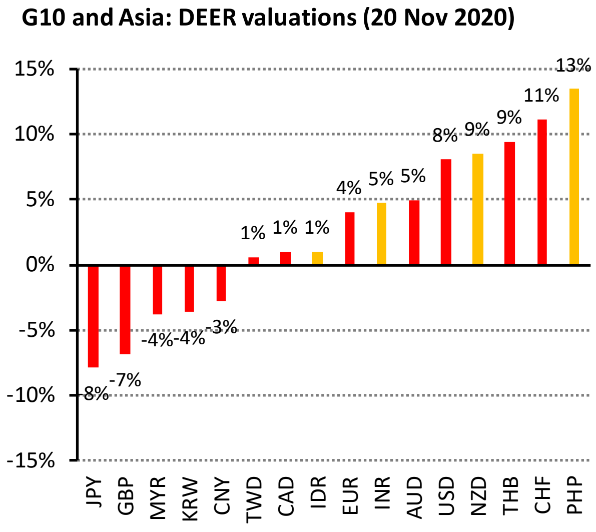
For many countries, it will be at least 2022 before per capita income returns to the levels of 2019



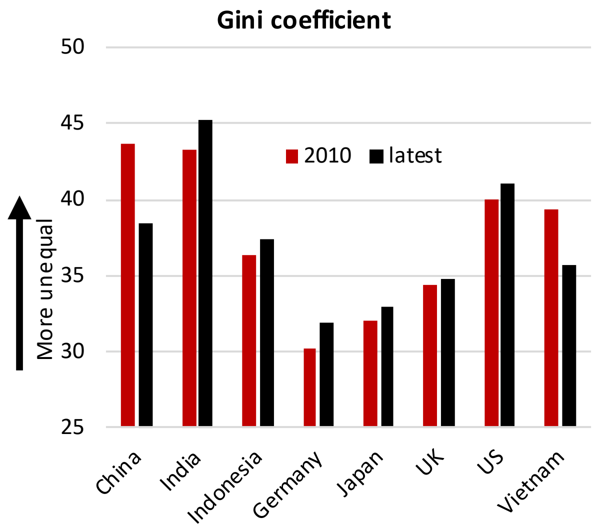
Source: CEIC, IMF, DBS

Our valuation models suggest USD has room for further weakness in 2021



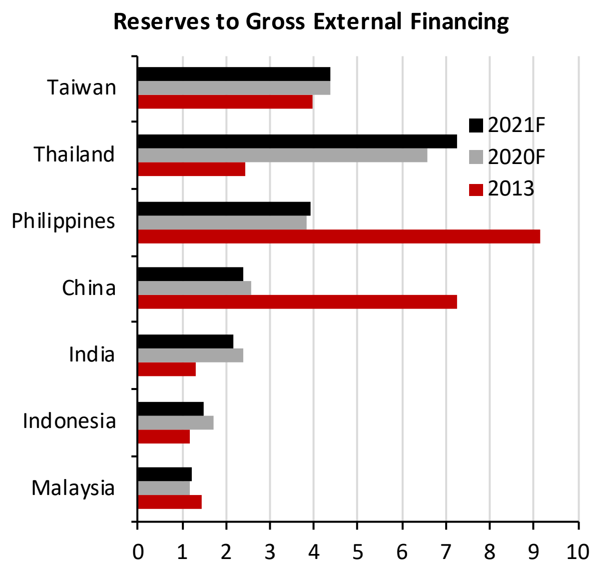
Source: IMF, CEIC, DBS

Many nations came to the pandemic with worsening inequality trends, which will likely worsen in the coming year



Source: World Bank Development Report, DBS

External buffers have improved for India, Indonesia, Taiwan, and Thailand; worsened for China, Malaysia, and the Philippines



Source: IMF. World Bank, country authorities, DBS

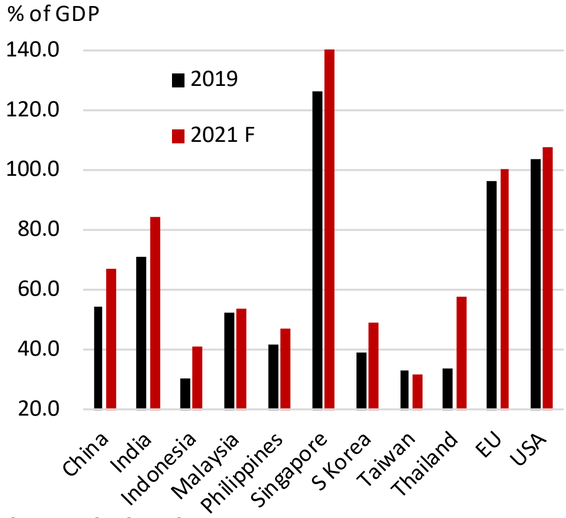
Key charts

Overview: A Bifurcated world

After a pandemic like no other, and after incurring an extraordinarily large loss of lives and livelihoods, the world will strive to pick up the pieces and move on in 2021. There are reasons to be optimistic: the tireless efforts of scientists and healthcare professionals have produced, in record time, a wide range of anti-viral treatments and vaccine candidates to reduce suffering and loss of lives. We are hopeful that next year, scientific innovation, private sector initiative, and public sector resolve will converge to address the global pandemic in a comprehensive and equitable manner.

Given the shocking nature of the pandemic and glaring leadership gap in many counties, there have been failings in dealing with the crisis, unfortunately. History is unlikely to judge policy makers and health experts kindly for their initial response, as they fell short in giving the public clear, realistic, and science-based information, protocols, and guidelines to deal with the pandemic. As our understanding on the health and economic dimensions of the pandemic improves, it is incumbent upon all concerned to make next year the one when the world rises up to the grave challenges posed by this once-in-a-century predicament.

Pademic's cost, soaring public debt



Source: CEIC, DBS

As the death toll and infection numbers point out clearly, Asia as a region has done the best in managing the pandemic, with the Americas (both North and South) and Europe struggling. After a respite in the summer, the fears of a winter surge are unfortunately materialising. Encouragingly, and in contrast to the West, there have been only sporadic cases of Asian societies and governments tussling with the lives versus livelihood matter. Here, most accept that one can't protect one without the other. Consequently, there has been widespread public compliance with mobility restrictions, social distancing, and hygiene measures in Asia. Elsewhere, however, the public's patience has run thin, while policy makers have given often confusing messages.

We believe that Asia's success with dealing with the pandemic (admittedly at great economic and social costs) will pave the way for relative economic and financial outperformance in 2021. Pandemic management is not the only reason behind out optimism. Three additional factors support our notion:

- First, the region's trade intensity. As the world has woken up to the need for substantially more remote work and education, medical supplies, and home improvement, Asia stands ready to meet the global craving for screens, computers, sound equipment, PPEs, computer desks, home gym gear, etc. Already, the pick-up in export demand is visible in the region's PMIs and in the order books of electronics and a wide range of consumer goods exporters.

- The second reason for likely outperformance is the relatively high levels of foreign exchange reserves, savings, and investor participation in the region. We don't see the markets worrying about debt or current account sustainability in the region next year; in fact, we expect a great deal of interest among external investors to pick up Asia's positive yielding bonds and high growth stocks, while taking exposure in regional currencies that are likely to appreciate or remain stable.

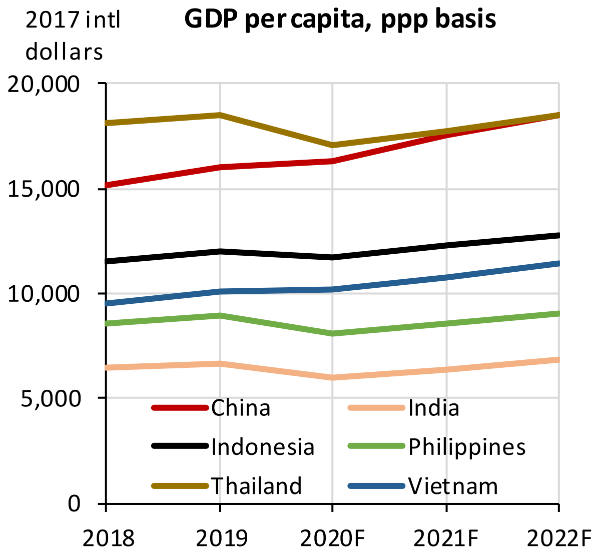
- Third, China. As the country that was at the epicentre of the pandemic during the first quarter of 2020, China will enter 2021 with some tailwind, having made up for the pandemic-induced loss in output. Expecting some dissipation of the tension with the US as the Biden administration gets going, enjoying strong domestic travel and production, buoyed by sentiment-improving initiatives like asset market liberalisation, RCEP, and e-RMB, China would be looking at 7% growth in the coming year, as per our forecast.

This final upside is material for the obvious fact that the region presently has deeper trade and investment ties with China than ever before. Our growth correlation analysis shows that once controlled for US growth and oil price, China enters significantly in growth regressions of a large number of Asian economies. Notably, in these regressions, the size and statistical significance of the China coefficient has risen in the past decade when compared to the 1990s and 2000s. **Asian economies that now benefit considerably from the China growth dynamic are Hong Kong, Indonesia, Malaysia, Singapore, South Korea, and Taiwan**.

But Asia is not in a cocoon; the likelihood of relative outperformance should not cheer us too much. Many developing economies are in precarious positions, weakened by the economic cost and social toll of the pandemic. Several economies in Africa, Latin America, and Middle-East could see deep economic contraction and financial crisis next year, weighed down by debt, funding deficit, and loss of investor confidence. Contagion from such dislocation could readily arrive in Asia's shores, a risk that we need to track closely. Even among developed economies, macro imbalances could create financial instability, challenging policy makers tremendously.

Beyond the pandemic, many cyclical and structural headwinds remain entrenched. Global imperatives like climate change and inequality are not being tackled forcefully, while populism, nationalism, protectionism, and great power rivalry won't go away with Trump. Aging and white-collar job displacing technology are two additional considerations that could hamper growth and dampen employment.

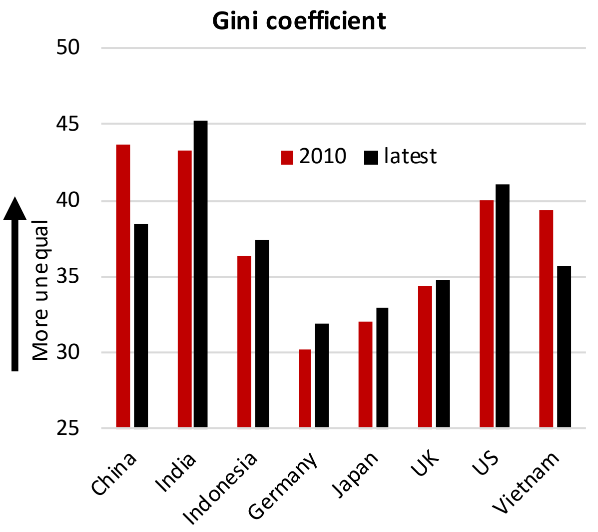
There should also be no confusing rebound for recovery. After a sharp contraction, it is easy to report strong year-on-year growth numbers, thanks to arithmetic base effects. But recovery is when all the lost output is made up, i.e. the level of GDP is back to the pre-pandemic level. We see little chance of a full recovery, on a per capita basis, in many countries before 2022 or 2023.



Source: CEIC, IMF, DBS

Even among economies that recover relatively quickly, there will be a variety of bifurcations. As firms and individuals rethink travel, work, retail commerce, and hospitality, investment will flow into some sectors more readily than others. Additionally, some skills may well seem redundant in the post-pandemic world. Many workers would potentially struggle to find jobs even as other types of vacancies soar. Skills mismatch was already a source of concern pre-pandemic, but now with accelerated economic disruption and transformation, these differences will become more acute, in our view. On one hand, there is a worldwide shortage of nurses, on the other hand, there is probably an excess supply of hotel and airline staff. Same can be said about jobs in the area of data analytics (excess demand) and conventional energy production (excess supply).

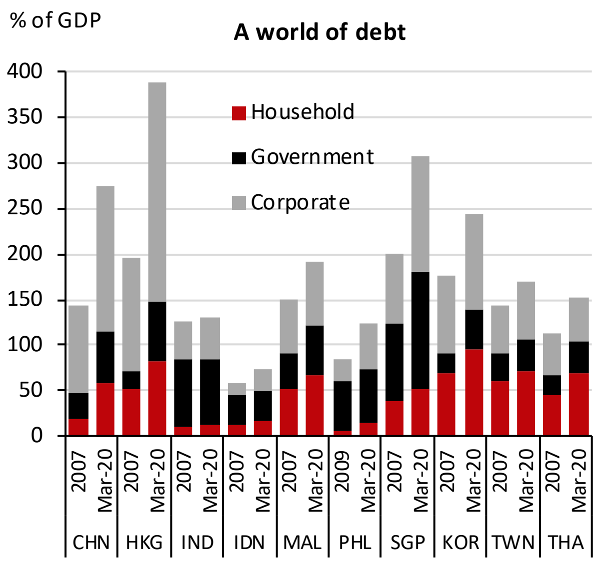
More bifurcation will be evident in corporate balance sheets. Impacted by the aforementioned disruptions, some companies will struggle even if debt financing remains cheap. A prolonged period of monetary and fiscal accommodation, as well as crisis-era regulatory forbearance, could get in that way of healthy creative destruction, leading to a class of zombie companies. Low rates and ample liquidity could cause housing prices to soar, as well as push the valuation of a wide array of financial assets. These trends will inevitably accentuate inequality in many parts of the world.



Source: World Bank Development Report, DBS

In the aftermath of crises of this magnitude, the key fear is long-term scarring. Sectors that received a lot of investment pre-pandemic but are not particularly relevant post-pandemic could cause lenders to take large haircuts, making them reticent about future lending even if there is ample liquidity. Those who miss out on jobs for several years during the Covid mayhem could see a permanent decline in lifetime earnings and wealth. Economies that fall into a crisis now could take years if not decades to recover, dashing the aspirations of their population.

It is tempting to conclude from the prospect of higher economic growth rates next year, and the tailwind from asset price rally in 2H20, that prosperity would return despite this mega crisis. But **prosperity is not necessarily progress**. Rise in stock market, increase in housing wealth, or even a steady increase in average income can mask rising inequality, anxiety about future job prospects, burden of debt, health and education outcomes, and social cohesion. Debt will loom large, and financial sector stability may be undermined as frothy valuations have their comeuppance. 2021 may be pleasing from a numbers perspective, and there could well be a time to celebrate as the world begins to move past the pandemic, but generational challenges to progress, to financial stability, and the formation of a global community based on mutual respect and less bifurcations will loom large.



Source: CEIC, World bank, DBS

Taimur Baig

US: A presidential reset

	2019	2020F	2021F	2022F
GDP growth, yoy%, ave	2.3	-3.5	5.0	2.2
Inflation, yoy%, ave	2.3	1.3	1.7	2.2
Fed funds rate, %, eop	1.75	0.25	0.25	0.25
USD per EUR, eop	1.09	1.17	1.20	1.25
10-year yield, %, eop	1.85	0.95	1.30	1.70

The US has had a particularly tumultuous year, marked by considerable self-inflicted economic challenges in dealing with the pandemic, compounded by a highly divisive and acrimonious election.

The silver lining has been vigorous fiscal and monetary support. Thanks to public sector support, low interest rates, and low inflation. US consumers, despite considerable uncertainty about livelihood and still-high Covid-19 infection rates, went back to shopping during the summer and early autumn.

The CARES act, enacted in late March, put cash in the hands of unemployed Americans, provided pay check support to those still on the payroll, and extended a range of credit facilities to businesses. Hence, businesses that lost out on foot traffic continued to earn revenues; consumers who did not have jobs continued to have their purchasing capacities largely intact. This pushed up savings rate during stringent lockdowns, and since then has supported consumption. Additionally, exceptionally low interest rates have supported demand for housing and home renovation. Consumption sentiment could soften if new stimulus support does not come in commensurate dose while the pandemic intensifies, but accommodating monetary policy and confidence from vaccine developments ought to keep the consumption train moving.

The picture is less bright on the production side. US exports recovery has been slow, with goods exports contracting by 13%yoy in 3Q. In contrast, during the same period, China's exports were up by 9%. Industrial production has begun to recover, but at a far slower pace than consumption. Putting these data together, along with assumptions of continuation of supportive fiscal and monetary policies, we see US real GDP contracting by 3.5% in 2020, while rebounding by 5% next year.

By the time vaccination reaches a level wide enough to make a difference, it will likely be the second half of next year. In the meantime, use of therapeutics to treat the ill and dedicated adherence to mask and social distancing for the healthy would be warranted. Unfortunately, it seems that the US public is losing its patience with stringent restrictions on mobility and social behaviour. US government officials would need to adhere to science, transparent reporting, and inspirational leadership to keep the fight against Covid-19 going.

On leadership, the incoming Biden administration will be competent, pro-multilateralism and pro-engagement, stable, and will strive to make progress on inequality, diversity, green infrastructure, progressive taxation, education, healthcare, and financial inclusion. How much can be achieved depends on the ability to pass legislation through the Senate. President-elect Joe Biden has spent many decades in Washington DC, building working relationship with many Republican counterparts. If he can manage to successfully reach across party lines in these acrimonious times, it would be the ultimate reflection of his political acumen.

Taimur Baig

Eurozone: Navigating tricky waters

	2019	2020f	2021f	2022f
Growth (y/y %)	1.3	-8.0	4.0	3.5
Inflation (y/y %)	1.2	0.3	1.0	1.2
Currency, vs USD eop	1.12	1.17	1.20	1.25
Policy rate, % eop	0.0	0.0	0.0	0.0
10-year yield, % eop	-0.2	-0.55	-0.4	-0.3

The Eurozone economy's growth trajectory will be dictated to a great extent by how the pandemic evolves and efficacy of the vaccine availability. Tapering of the first wave of infections into August convinced authorities to lift lockdowns and ease movement restrictions. This led output to rebound 12.6% q/q (-4.4% y/y vs 2Q's -14.8%) in 3Q20, shaking off the pandemic-led recession. This 'V' shaped pickup proved short-lived due to the onset of a ferocious second wave, with the daily count touching record high in some instances, more so in the economically key core-4 countries. Premature easing in social curbs as well as poor communication were named as few of the shortfalls. Considering the significant economic impact to earlier lockdowns, authorities resisted the option to reinstate lockdowns but have since re-imposed strict curbs in France, Germany, Greece, Ireland, Belgium etc., to gain an upper hand on the infection curve.

Restrictions vary across the countries and is not as stringent as back in April-May. Nonetheless, this is likely to impinge on 4Q20 growth as well as 2021 prospects, leaving recovery as more of a 'W' shaped rather than 'V'. 4Q20 GDP is poised to slip back into negative q/q (and y/y) growth and remain in red into early 2021. 2020 GDP growth is seen at -8.0% y/y, followed by a shallow bounce to 4% y/y in 2021.

Beyond the deep scarring economic impact, repercussions of weaker fiscal health and jump in public debt levels will reverberate for a longer time, if 2012-2013 debt crisis is any indication. At an aggregate level, Eurozone debt to GDP ratio is expected to surpass 100% of GDP this year and stay elevated next year. National fiscal stimulus spending is underway, however, optimism from the EU-wide recovery plan has temporarily hit a hurdle by legal reservations raised by Warsaw and Budapest.

As monetary policy support runs its course, the ball will fall back on the national governments' court, worryingly, causing a vicious cycle of higher spending, debt and monetisation as growth stays sub-potential. The ECB is set to continue with its pandemic-driven asset purchase program, raising the size from EUR1.35trn by another EUR500bn, alongside conducting another round of TLTROs. This is likely to keep a lid on the financial system stress indicator, which retreated from highs since the PEPP was announced earlier in the year. Extraordinary asset purchases have seen ECB's balance sheet swell by 19% of GDP between Sep20 vs Dec19.

Concurrently, the future trading linkage between the UK and the EU remains uncertain beyond December 2020, when the Brexit transition period ends. Passage of the Brexit deadline without a bilateral treaty will impose onerous tariff limitations on both parties, given the large weight of intra-trade and investment between the UK and EU. This could potentially compound the fallout from the pandemic and resultant recession.

Radhika Rao

Japan: An election year

	2019	2020F	2021F	2022F
GDP growth, yoy%, ave	0.7	-5.0	2.8	1.5
Inflation, yoy%, ave	0.5	-0.1	0	0.5
Policy rate, %, eop	-0.10	-0.10	-0.10	-0.10
JPY per USD, eop	109	105	106	105
10-year yield, %, eop	-0.02	0.05	0.10	0.10

In Japan, all eyes are on the general election (lower house election), which is scheduled to be held before October 2021. Although the ruling LDP party is very likely to win the election, the scale of its victory will have significant implications for the outlook of PM Suga's tenure. Suga has vowed to push for a series of reforms after the pandemic, including upgrading digital capability, promoting competition in the telecom sector, facilitating consolidation among SMEs, revitalizing regional economies, and diversifying the supply chain of essential goods. Implementing these reforms, which involves the efforts to tackle vested interest, will require a long period of political stability and a strong leadership.

We expect real GDP to grow 2.8% in 2021, a partial recovery compared to the -5.0% contraction in 2020. Exports are expected to take the lead, thanks to the restoration in Japan's manufacturing supply chains and the revival in global durable goods demand. In contrast, the pace of domestic recovery would be relatively moderate. On the positive side, the Japanese government has approved a bill to cover all costs of COVID-19 vaccination for all residents, and agreed with pharmaceutical companies BioNTech/Pfizer, Moderna and AstraZeneca to receive a total of 290mn doses of vaccines when successfully developed. Meanwhile, the government's massive support on households and businesses through the supplementary budgets, including the "Go to Travel" subsidies, should lend support to consumption and investment in 2021. Nonetheless, the country still struggles with a third wave infection in the near term, the labor market remains weak, deflation risk lingers, and the 2021 Tokyo Olympic Games will likely be simplified. The upside potential of domestic demand would be limited, in our view.

Monetary and fiscal policies will remain loose in 2021, but extra easing is not very likely after the massive rollout this year. The government is currently drafting a third supplementary budget for FY20, which is expected to take the total scale of COVID-19 stimulus packages to about 15% of GDP. The Bank of Japan has boosted the size of its balance sheet by 20% this year, through the buying of government securities, commercial paper, corporate bonds, ETFs, REITs, as well as the expansion of special lending programs. The BOJ is expected to continue increasing asset purchases next year to anchor the long-term yield at the 0% target.

On external ties, Biden's victory in the US presidential elections has positive implications for Japan. The new US administration may move to rebuild relations with international allies in the next several years, including considering a return to the CPTPP, a multilateral FTA that is currently led by Japan. Meanwhile, the recent launch of the RCEP is also positive for Japan. The country presently does not have bilateral FTAs with China and South Korea, the two important RCEP members; and its capital goods exports are relatively competitive. As far as the boosting impact on exports is concerned, Japan would be a major beneficiary of the RCEP in the coming years, in our view.

Ma Tieying

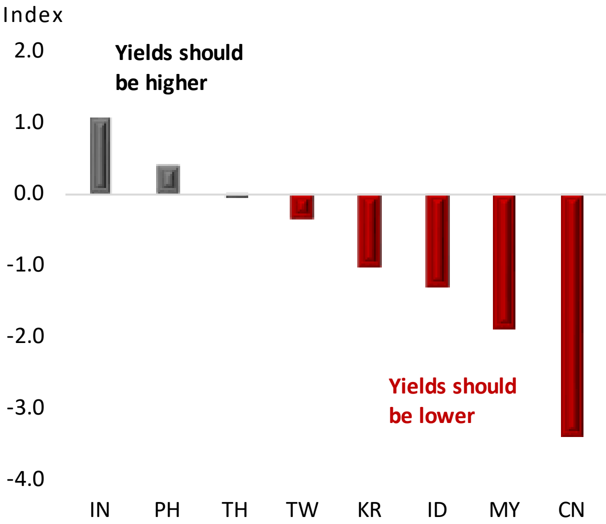
Rates: A more normal 2021

2021 should mark a return to normalcy after a tumultuous 2020 gripped by COVID-19 fears and uncertainties over the US elections. Defining what normal is for the economy is arguably easier than defining what normal is for global interest rates. Moreover, the speed of recovery of the market (which can be split into different asset classes) and the real economy can differ. Our key point was that without a vaccine(s), the initial V-shaped recovery would slow as selected industries (tourism-linked) cannot normalize. However, that changed when Pfizer reported encouraging preliminary vaccine results. Vaccine approval(s) could be in the offing, setting the stage for a more complete global economic recovery in 2H21 when vaccines become widely distributed.

The market will be ahead of the real economy. DM curve steepening took place in earnest in 4Q as the market gained clarity on US elections, fiscal spending and a potential COVID-19 vaccine. With the Pandemic crisis having an expiry date and about to transition to a more conventional economic crisis, there no longer is any need to place a sizable COVID-19 premium on longer-term US Treasuries. Our regression model suggests that neutral 10Y US yields should be closer 1.3%.

Stances of the authorities will probably be accommodative into the first quarter of 2021. However, there will be rumblings of support pullback in mid-2021 when the recovery is on firmer footing. For rates, there will be nuances amongst DM central banks. In general, we believe that monetary easing will largely be done in 2020 with the European Central Bank (ECB) possibly firing the last bullet (more QE and possibly deeper negative rates) in December. The Fed and the Bank of Japan (BOJ) have been on pause for several months. Speculation of Fed taper is probably premature, but this could get contentious as we get into late 2021. The US unemployment rate is already below 7%. Under the old regime, the Fed would probably be thinking about reducing asset purchases. Similarly, while the dot plot indicated no hikes through 2023, risks of earlier tightening should not be underestimated. Steepening in the 2Y/10Y and 2Y/30Y segments may give way to steepening in the 1Y/5Y segment in 2H21. We expect German and Japanese government bond curves to steepen in tandem, but to a smaller extent.

Asia: Gap to ARVI Indicator



Source: Bloomberg, DBS

The impact on Asia rates will be nuanced. While vaccines are undeniably positive for Asia economies, we are cognizant that Asian govvies do well under selected conditions (weak USD, low US yields and weak domestic inflation). It would well be a tale of two halves with supportive factors starting to dissipate towards the end of 2021, especially if overheating risks weigh. **Thematically, we think assets in Asia economies worst hit by COVID stands to benefit the most from a viable (cheap and easily transportable) vaccine. Economies that have large trade and travel linkages is another area to explore.** As a starting point, we filter govvies by their relative performance since the Pandemic crisis. China, Korea and Thailand stand out to be the laggards. Meanwhile, our Asia Rates Valuation Indicator (ARVI) suggest that Indonesia, China and Korea debt are cheap from a macro perspective.

Eugene Leow

Currencies: Not a one-way trade

The US dollar is widely expected to extend its decline into 2022. Its weakness has become synonymous with risk appetite. Optimism has increased for the world economy to be put on a sounder footing from a safe and effective vaccine, and out of America, more predictable policies and dependable leadership under President-elect Joe Biden. Investors have embraced the "pandemic put" or the assumption that populist fiscal spending and expansive monetary policies would keep getting expanded and extended to insulate economies from self-induced recessions and new waves of infections.

In the short-term, the euphoric post-US election/vaccine market rally in November may give way to a year-end correction that extends into 1Q21. The global economy is set to slow in 4Q20 from the new lockdowns and tighter restrictions to counter the record new infections in the G3 economies. The prospect of a large US stimulus bill is contingent on the Democrats winning the Senate runoff in Georgia on 5 January. There is no assurance that extended UK-EU talks can avert a no-deal Brexit at the end of the transition period on 31 December.

The greenback's depreciation pace in 2021 will, all things considered, become more tempered and less one-sided. Despite its bearish tone, the USD has become less overvalued after its 11% depreciation over 8 months. Since the global financial crisis, major USD falls have resulted in 15-18% depreciation over 9-13 months. Emerging Asian currencies have, by November, also caught up with the recovery in their Developed Market peers.

Major USD depreciations after the GFC

Recovery from:	From	To	Change
Global financial crisis	89.624 Mar-09	74.170 Nov-09	-17.2% 9 mths
USD confidence crisis	88.708 Jun-10	72.696 May-11	-18.1% 11 mths
Currency war	103.820 Jan-17	88.253 Feb-18	-15.0% 13 mths
Covid-19 coronavirus	102.992 Mar-20	91.758 Nov-20	-10.9% 8 mths

Overall, judicious prudence is advisable regarding excessive USD pessimism sometime next year. Unlike the GFC, aggressive US fiscal and monetary stimuluses have been accompanied by unprecedented easing in the rest of the world too. A return to positive US growth is set to be accompanied by a steeper US treasury yield curve; our rates strategist has forecast a higher 10-year yield of 1.30% by end-2021. Emerging Asian currencies have already caught up with their Developed Market peers in currency appreciation. Time will tell if vaccines and Mr Biden will commensurate with the hopes that investors have for getting ahead of the pandemic crisis and US-China tensions respectively. Medical experts believe that Covid-19 vaccines, when they become available, have yet to substantiate themselves as safe and effective enough to replace the effectiveness of masks, social distancing and tighter restrictions. US's bipartisan policy to contain China has not changed and is likely to involve its democratic allies. Under Mr Biden's "Made in America" policy and China's "dual circulation strategy", US-China relations will remain more about competitive rivalry than cooperation and center increasingly on tech bifurcation than bilateral trade imbalances.

Philip Wee

Credit: Turning the corner

Credit defaults picked up sharply in 2020 with lockdowns wreaking havoc on sectors as varied as oil, retail, airlines and leisure. US credit fared the worst, as US corporate bond defaults doubled to near USD120bn in 2020, with default rates reaching GFC highs. In Asia, defaults were far smaller. Hong Kong and Korea remarkably saw no defaults, while India and Indonesia reported a lower quantum of defaults compared to 2019. Robust loan growth in North Asia, and a greater reliance on bank financing in South Asia—supported by loan moratoriums—have helped Asian firms tide through this difficult period better.

China was the outlier in Asia as corporate bond defaults rose by over 50% to around CNY 170bn in 2020. Yet, this accords with a fast-growing bond market, with the ratio of defaults to maturing bonds having in fact eased from 2019. Nevertheless, a rise in SOE defaults mean **investors should stay cautious on Chinese SOEs that are heavily leveraged and marginally profitable**. Markets are becoming more judicious in assuming the availability of local government support, with the government having declared that it will foster more market-based credit decisions.

China's real estate sector is a particularly key credit market driver, given a large proportion of Chinese developer credits, and high leverage in some firms. The pandemic has fallen unevenly across different sectors and different parts of the labor force, and the same is seen in Chinese residential sales. Eastern China is slated to record its fastest annual sales growth since 2016, while Central and Western China will see their worst growth, outlining truly **divergent real estate credit risks by geography**.

For India, the bond market has been through a wrenching journey due to a prolonged credit crunch for NBFCs. **However, credit stress is now nearer the end than the beginning.** Corporate bond defaults stand at around INR150bn in 2020, but more than two-thirds is from known distressed NBFCs—IL&FS, Dewan HFC and Reliance Capital. Incremental new bond defaults in 2020 are just INR47bn, close to India's pre-crisis average. While moratoriums have helped to staunch cashflow difficulties, subdued new defaults do give reason to hope that most non-performing assets are already weeded out. Meanwhile, the largest Indian private sector banks have also raised their capital buffers to ample levels, supported by a stirring equity market. Should asset quality outcomes meet expectations, COVID disruptions subside and India's sovereign rating is held steady at IG, **Indian credit may finally enter a more confident phase in 2021.**

Indonesian credit should also see an improving environment. Investors have become more comfortable with one-off debt monetization, with a steady compression seen in Indonesian USD credit spreads. Bond issuance may finally rise meaningfully, having stagnated since 2017.

Broadly, defaults should turn the corner in 2021, which is conducive for a further easing in credit spreads. With multiple vaccines in the pipeline, 2021 should also see activity normalization that supports a return of demand across the worst-hit countries and sectors. On the supply side, USD liquidity is flush, while banking liquidity is also ample in India and Indonesia. The positive confluence of demand and supply should support a catch up in credit growth for both economies.

Wei Liang Chang

Equities: Re-rating time for Asia

Regional Market Data

	Earnings Gth (%)		PE (x)		Div Yield	
	20F	21F	20F	21F	20F	21F
Singapore	-34.5	43.8	21.4	14.9	3.5	4.1
HK HSI	-21.4	19	13.7	11.5	2.8	3.3
Malaysia	-16.9	23.6	23.2	18.0	2.7	3.5
Indonesia	-26	21.8	21.5	17.7	2.9	2.4
Thailand	-39.6	28.9	27.4	21.3	2.5	2.7

Source: DBS Bank

Asian equity markets head into 2021 carrying the optimism of regional trade partnerships, improving US-China trade ties, and COVID-19 vaccine deployment. Forward PEs have surged, driven by a combination of the steep YTD earnings cut and the recent 'vaccine powered' equity markets rally. Asia Ex-Japan currently trades at 16x 12-mth forward PE that is slightly above +2SD over a 15-yr period. We see similarities between now and the post GFC recovery bull market in 2009 when PE valuations remained elevated as stock markets recovered. This phenomenon continued for a year until consensus earnings revision caught up with the stock market rally.

In the region, Singapore offers the strongest EPS recovery for FY21 at +40% y-o-y and the highest yield at 4.1%. We also see solid FY21F EPS recovery of 29% and 22% for Thailand and Indonesia, respectively.

Being a small and open economy, Singapore stands to benefit most from the COVID vaccine recovery, the regional trade pack and a friendly global trade environment. Singapore stock market is heavily weighted on cyclical companies such as banks, properties and conglomerates, which ought to benefit from the normalisation trade.

The HK/China equity markets are expected to benefit from Biden's more moderate stance towards China and successful pandemic management. Given the inexpensive valuation and relatively underperformance of the HK market vs the US market and A-shares, risk appetite should improve next year.

The Thai stock market was significantly affected by this year's travel collapse as tourism accounts for 20% of GDP. It was also weighed down by heightened political risks. With investors currently underweight, we expect a boost next year as they rebuild their positions to neutral weight. However, political risk remains a major overhang.

Re-starting the domestic economy will be crucial for Indonesia as it is not as heavily reliant on tourism and travel. The government stimulus program is extended into next year to support growth while Bank Indonesia will continue to provide low rates and bond buying program. Omnibus Law could be another driver for 2021. With better growth prospects in 2021, we believe cyclical recovery and domestic growth will be the themes for 2021.

Finally, the Malaysian equity market will be underpinned by an improvement in domestic demand and the recovery in external trade. Budget 2021 places strong emphasis on the well-being of the people that is expected to help the nation in its transition into economic recovery. The construction sector is a key winner with the government's commitment and revival of two major transportation infrastructure projects.

Yeo Kee Yan

China: Normalising monetary policy

	2019	2020F	2021F	2022F
GDP growth, yoy%, ave	6.1%	2.0%	7.0%	5.5%
Inflation, yoy%, eop	2.9%	2.6%	2.5%	2.5%
Core inflation, yoy%, eop	1.6%	0.8%	1.7%	1.7%
Policy rate, %, eop	4.15	3.85	3.85	4.05
CNY per USD, eop	6.96	6.60	6.61	6.50
10-year yield, %, eop	3.13	3.20	3.40	3.40

China's recovery from the deepest downturn since the Cultural Revolution has been faster than expected. We forecast annual GDP growth will reach 7.0% in 2021. Year-on-year expansion will persist in 1H21 before stabilising in the second half of the year.

Public investment will remain an important pillar. Surging credit impulse indicates continued support from government infrastructure investment in coming months. The contribution from new infrastructure projects may become more salient in the medium to long term, thanks to Beijing's push for self-reliance in technology.

A tightening property lending constraint means the post-lockdown surge in housing investment may have reached its peak. Developers are indeed turning more cautious, evidenced by slumping land purchases. Which suggests that new construction will be tepid at least in 1H21.

Households are turning more upbeat. High-frequency data such as traffic volume and box office revenues indicate continued signs of normalisation. Though labour market slack still exists, unemployment rate has reversed half of its rise earlier in the year. Relaxation of social distancing measures and spending at home in lieu of outbound travel should help support the consumption recovery down the road.

On the external front, we expect shipments for pandemic-related to remain resilient given a resurgence in COVID-19 cases overseas. The recovery in non-COVID-related demand will also support export growth. For instance, retail sales have gone strength-to-strength lately in the US. China's exports of furniture and household appliances have been particularly strong. Imports recovered at tandem notwithstanding, import values are being held down by energy prices. Meantime, a collapse in outbound tourism will narrow the nation's services deficit.

The reviving domestic demand may be indicative that core CPI will soon bottoming out. PPI has started rising again month-on-month since June. This trend looks set to continue as activities advance and energy prices gradually recover. Which should in turn feed through to higher non-food consumer prices. We expect headline inflation to pick up to 2.5% by mid-2021, after reaching a trough on 4Q20.

Amid macro recovery, the PBOC will be more reluctant to step up easing in 2021. We expect LPR to stay unchanged over the course of next year. Policy focus will shift toward maintaining stability and keep a tighter rein on leverage. On the fiscal front, next year's budget is set to be less supportive. We forecast general government debt-to-GDP to stabilise at 67%, after rising from 54.4% in 2019 to 2020's 63%. Debt risk is manageable as public debt is largely supported by domestic savings. Modest fiscal stimulus, neutral monetary policy, and a strong external trade position will continue to buttress the yuan exchange rate.

Chris Leung and Nathan Chow

Hong Kong: A brighter year ahead

	2019	2020F	2021F	2022F
GDP growth, yoy%, ave	-1.2	-7.0	4.0	2.3
Inflation, yoy%, eop	2.9	0.7	2.0	2.5
HKD per USD, eop	7.79	7.76	7.77	7.80
10-year yield, %, eop	1.79	0.60	0.90	1.30

The real GDP is expected to drop by 7.0% in 2020. The fourth wave of COVID outbreak will weigh on the recovery and we expect it will shrink by another 6.4% YoY in 4Q. CPI will slow to 0.7%, in our view. Hopefully, the GDP could rebound by 4.0% in 2021, assuming the border could be reopened in the first quarter.

Over the past year, the consumption and tourism sector took the hardest hit. Retail sales dropped by 28.7% YoY YTD in September amid straight social distancing and immigration policies. The relative improvement in retail sales, which narrowed from -44.0% YoY in February to -12.8% in September, is largely a result of the low-base comparison from heightening China-US trade tension and an unprecedented social unrest in 2019. In fact, performance of tourist hot-picks such as jewelry and clothing remained subdued. CPI therefore fell to negative territory since July.

Hotel occupancy rate rebounded from 29% in February to 52% in September due to unusual demand from 'staycation'. Yet, the overall room rate after discounted by CPI dropped to HKD627 per night, even more affordable than that HKD660 during SARS in 2003. Looking ahead, the retail sales value is expected to rebound by 12.0% in 2021 if the border could be reopened timely. Afterall, around 30% of the retail sales receipts are contributed by tourists.

The external sector is the bright spot amid a fully recovered production capacity of China. Exports rebounded to growth of 0.3% in 3Q after contracting by 6.9% in 1H20. However, the pace of recovery will be constrained by the sluggish global demand. PMIs of Hong Kong's major trading partners, except China, have held below 50 or the expansion threshold. Worldwide new daily cases also revived. Hopefully, the easing trade tension between China and the US under the Biden Administration could help the situation.

Against this backdrop, another round of timely stimulus package is needed to avoid the next wave of lay-off. The budget deficit as percentage of GDP is expected to reach 11.1% FY20/21, up from 0.4% last year. However, another round of rescue package is restrained by the fiscal reserve, which could maintain government expenditure for another 12 months. Further stimulus will require the government to issue government bonds. This will add upward pressure to the interest rates.

Yet, we expect the asset market will remain largely resilient. Hang Seng Index rose by 23.6 % from the trough. Inflow through Southbound Stock Connects soared by 200% YoY YTD. Residential property prices on the secondary market have only fallen 7.7% from its peak before the social movement in June 2019, or 1.3% YTD. The fourth wave of outbreak could weigh on both transactions and prices. Prices set by developers in the primary market was less aggressive lately. The rising unemployment rate also added downward pressure on rental yield. In the near-term, the property prices movements stay diverged. That for small and medium size units will be well supported by the strong local housing demand. Yet, we should see more downside risks for the luxurious market. The cloudy economic environment may lead business owners to liquidate their assets. Investment demand from Mainland investors for large units will also remain subdued with a closed border. We expect the overall residential prices to stay flat in 2020 and 2021.

Samuel Tse

India: Recovery gains traction

	2019	2020f	2021f	2022f
Growth (y/y %)*	4.2	-8.0	7.7	4.5
Inflation (y/y %)*	4.8	6.3	4.3	4.0
Currency, vs USD eop	73.8	74.4	74.5	74.1
Policy rate, % eop	5.15	4.00	4.00	4.00
10-year yield, % eop	5.90	5.80	6.20	6.50

**in fiscal year terms; 2019 = FY20 i.e. YE Mar20*

Reverberations of the stringent lockdown imposed in 2Q20 (1Q FY21) in response to COVID-19, dealt a heavy blow to economic activity, resulting in a -24% y/y contraction in growth. Gradual unlocking process thereafter, notwithstanding high cases, led to faster normalisation in business activities, sustained rural demand, firmer farm output, and inventory restocking alongside festive demand, lifted 3Q20 (2QFY) and is expected to buoy 2020 GDP to -7.4% y/y (FY21f -8% y/y).

Passage of festival tailwinds and pent up demand is expected to moderate into 4Q20 and early 2021, in addition to easing inventory restocking demand. Daily caseload of COVID-19 infections had halved but has since stalled introducing a sense of caution. Even if the caseload escalates, a nationwide shutdown/ lockdown is out of consideration. Encouragingly, states and districts have taken a proactive stance and already selectively imposed restrictions e.g. night curfews, delayed of reopening of schools, increase in penalties for not wearing masks, stepped up COVID-19 testing for inter-state travel especially inbound from more affected states. Authorities are also laying the ground for vaccine readiness, with local companies with a tie-up with international manufacturers seen as frontrunners.

Fiscal and monetary action was undertaken concurrently, but of varied intensity. The RBI initiated broad-ranging measures, including rate cuts, liquidity injections, moratorium for borrowers, supporting bond markets through the secondary markets as well as introducing a two-year restructuring window for stressed accounts (of affected sectors). Focus in 2021 will be on anchoring rates, by strong forward guidance, keeping the repo rate unchanged even if base effects drive GDP growth higher and maintain secondary market debt purchases.

The government adopted a prudent and cautious stance on the scale of fiscal boost during the pandemic, with additional spending requirement at ~2% of GDP. Measures were a mix of credit guarantees, higher outlays towards a rural employment guarantee program, subsistence support by way of cash handouts, provision of food and necessitates for vulnerable sections, etc. A concurrent medium-term push led to agriculture reforms, fiscal incentives to more manufacturing sectors, efforts to reduce import dependence amongst others. We expect FY21 fiscal deficit (states and centre) to rise to 12.5% of GDP, with general government debt level to rise to 85% of GDP. Debt levels will remain high into FY22 as GDP (on level terms) remains below pre-COVID levels in 2021, despite the base-effect driven jump in headline growth. The central bank and domestic banks are likely to remain at the drivers' seat to absorb strong bond supply next year as well, with foreign interests hinging on broader risk uptake and INR stability.

External debt metrics, meanwhile, received a boost by a record jump in FX reserves. A concurrent current account surplus (DBSf -1.4% of GDP) will add to the dollar surfeit, supporting the currency.

Radhika Rao

Indonesia: Looking beyond the pandemic

	2019	2020f	2021f	2022f
Growth (y/y %)	5.0	-2.0	4.0	4.5
Inflation (y/y %)	2.8	2.0	2.2	2.8
Currency, vs USD eop	13645	14200	14286	14000
Policy rate, % eop	5.0	3.75	3.75	3.75
10-year yield, % eop	7.1	6.0	6.6	7.0

2020 was dominated by the pandemic fallout as authorities sought to balance lives vs livelihoods. Indonesia's total caseload is the highest in the ASEAN-6 bloc, with the latest total count past 500k. As demonstrated during the depths of the first wave, the authorities are not in the favour of full scale shutdowns given the sizeable economic repercussions. Any re-steepening in the pandemic curve is likely to be met by localised restrictions. There are also notable strides towards access to vaccines, as the government arranged for licences with a Chinese pharma firm and under discussion of tieups either for clinical trials, vaccine manufacturing or procurement, with other drugmakers.

Imposing strict movement restrictions instead of full-scale shutdown saw the economy register a comparatively shallow -5.3% y/y contraction in 2Q20 GDP, before recovering on sequential terms to -3.5% y/y in 3Q. While the back-to-back negative prints see output enter a recession, the path ahead will be dictated by the COVID-19 curve. Mobility reports and high frequency numbers signal some fatigue going into 4Q, albeit, our expectation for a small negative on the headline is likely to leave full-year growth this year at -2% y/y.

The government undertook timely fiscal stimulus earlier in the year, which accompanied by a burden-sharing arrangement (debt financing) with the central bank, secured funding lines. Disbursements have been gradual, with only 60% of the stimulus likely to be spent by end-year, due to administrative capacity constraints and delay in beneficiary identification. This will impede household purchasing power, delaying normalcy in business and employment conditions. For 2021, we count on consumption, corporate restocking and net exports, to provide support, while slower fiscal support and direction of the pandemic curve are risks to the outlook. Base effects are expected to buoy GDP growth to 4% in 2021, with recast windows for corporates and deferred NPL classification to provide some succour to the banking system in the near-term.

BI adopted a coordinated policy push, lowering the BI rate by 125bps to 3.75% year-to-date, boosting liquidity for the banking system, private placement support in the bond markets and partly financing the government's fiscal program. A similar active presence in the debt markets is unlikely in 2021, however, the BI has signaled that it will remain as a standby buyer. We don't anticipate further rate cuts as the yield advantage will narrow further. However a sharp increase in the infection caseload and strong IDR appreciation are triggers that might push them to consider further easing.

Taking a medium-term approach, we expect the legislations passed under the Omnibus law, particularly labour, corporate tax cut and easing in investment limits to be pursued. While these are unlikely to boost near-term growth, these are imperative to improve the economy's investment appeal amidst shifts in the global supply chain.

Radhika Rao

Malaysia: Outlook remains challenging

	2019	2020F	2021F	2022F
Growth, yoy%, ave	4.3	-6.8	6.0	4.8
Inflation, yoy%, ave	0.7	-1.1	1.4	2.0
Policy rate, %, eop	3.00	1.75	2.00	2.50
Currency, vs USD, eop	4.15	4.11	4.07	4.00
10-year yield, %, eop	3.31	2.75	3.10	3.40

Malaysia's economic prospects appear to be heading south again against the backdrop of a third wave, and perhaps the most severe bout of COVID-19 infections in Malaysia thus far. While high frequency data seems to suggest that the recovery in the external sector remains unabated, there have been renewed concerns on the growth performance, considering the impact of the latest wave of infections on domestic growth. Moreover, the labour market has remained weak. Although job vacancies picked up marginally in the summer, it remained way below the monthly average of 81K vacancies prior to this crisis. With the ongoing recession, a slump in the labour market and now, a resurgence of COVID cases resulting in the implementation of the CMCO in some key states, the pace of recovery in private consumption could come up short. As such, we think growth momentum in the fourth quarter could wane amid the current pandemic situation. **Overall GDP growth for the year is now expected to register -6.8%.**

The government has projected a robust expansion of between 6.5% to 7.5% in 2021, but we reckon that this could be too optimistic. A big part of the so called "rebound" is merely arithmetic (base effect). Beyond that, while external economic conditions may continue to improve, domestic growth outlook is expected to remain weighed down by the ongoing pandemic.

We are taking a more cautious stance, opting to maintain our growth forecast for 2021 at 6.0%. It will therefore be at least early 2022 before the end-2019 level of real GDP is fully retraced.

We expect policymakers to rely more on fiscal policy to stimulate growth going forward. After a total of 125bps of rate cuts, Bank Negara paused on monetary policy in the last two meetings, maintaining the Overnight Policy Rate at 1.75%. Rhetoric from the most recent policy statement does not suggest any further monetary action in the near future, mirroring the stance from key central banks around the region. **We reckon that Bank Negara will be on pause until the second half of 2021 when recovery momentum is expected to become more pronounced.**

Budget 2021 was announced recently. A record expenditure allocation of MYR 322.5bn (20.6% of nominal GDP) has been put forth in a bid to mitigate the impact of the COVID-19 crisis and support the recovery process. However, should the government fail to bring down the number of infections or that the pandemic continues to wage on in the country, additional stimulus package could be warranted.

Growth could also fall short of expectation, which could worsen the fiscal shortfall. **Overall fiscal deficit is projected to register 5.4% of nominal GDP, down from 6% in FY2020, but risk is on the upside.**

Irvin Seah

Philippines: Balancing act

	2019	2020f	2021f	2022f
Growth (y/y %)	6.0	-9.5	7.0	6.0
Inflation (y/y %)	2.5	2.4	3.0	2.8
Currency, vs USD eop	48.2	48.3	48.0	47.3
Policy rate, % eop	4.0	2.0	2.0	2.0
10-year yield, % eop	2.7	3.0	2.9	3.1

Prolonged spate of lockdowns, extended quarantines and strict restrictions depressed growth, with 1Q-3Q20 GDP averaging -9.7% y/y, amongst the weakest in the region. The economically important National Capital Region (NCR) accounts for more than half of the total COVID-19 cases, makes a third of overall output. Our assumption for a sequential rise in 4Q GDP will see 2020 wind down with -9.5% annual growth.

Worst of the pandemic-led slump is likely behind the economy as restrictions continue to ease, aiding mobility and economic activity. Besides a base effect driven rebound in 2021, the path will be bumpy as a resurgence in the caseload could necessitate stricter quarantine measures.

Turnaround will, therefore, be tentative given the overhang of income and employment uncertainty, weighing on household balance sheets. Unemployment rate had risen to double-digits by April, with remittances down -1.1% y/y in first nine months of 2020. With the pandemic dealing a global shock amidst prevailing weak oil prices, about 200k Overseas Filipino Workers (OFW) are expected to return home after job losses in the host country. Tepid consumption and slower government disbursements will restrain investment growth as spending priorties shift towards essential and non-discretionary spending. Into 2021, we expect the annual contraction to extend to 1Q21, beyond which the pandemic curve, vaccine availability and resumption of infrastructure spending/ reform agenda with dictate the path ahead. Factoring in base effects, we expect a bounce to 7% y/y in 2021.

The government has prioritised fiscal prudence, with expenditure being extended cautiously in light of a slump in revenues. The monthly run-rate is running short of guidance, at 4% of GDP, compared to the projected 9%. Support measures announced yet far have been modest, amounting to 2.3% of GDP, while the second tranche worth PHP165bn is being deployed at a slow pace. **Senate's passage of the CREATE law** immediately lowers the corporate tax rate by 5% and kickstarts rationalisation in FDI policies next year.

The BSP has done much of the heavy-lifting this year, with the benchmark rate cut by 200bps to a record low of 2%, alongside 200bps reduction in the reserve requirement ratio (RRR). Another 200bps worth cut in the RRR has been approved and is likely by end-2020. Benign inflation and inflationary expectations leave the door open for further easing, albeit policymakers are likely to seek fiscal support to and for the pandemic to come under control to spur growth, as real rates slip into negative territory. This year saw the BSP also provide unorthodox policy support has been via loans to the government and direct debt purchase of bonds. Given the spectre of weak growth and likelihood of the need for higher fiscal support, the debt purchase program might extend into 2020. One upshot is the stronger current account position which is likely to only turn into a less than < -1.0% of GDP deficit in 2021.

Radhika Rao

Singapore: Emerging optimism

	2019	2020F	2021F	2022F
Growth, yoy%, ave	0.7	-6.0	5.5	3.2
Inflation, yoy%, ave	0.6	-0.2	0.9	1.5
Core inflation, yoy%, ave	1.1	-0.3	0.6	1..2
Currency, vs USD, eop	1.35	1.35	1.35	1.31
10-year yield, %, eop	1.74	0.95	1.10	1.35

The economy expanded by 9.2% QoQ sa (DBSf: 9.5%) in 3Q20, which translates into a year-on-year contraction of 5.8% (DBSf: -5.4%). The strong turnaround came largely on the back of the phased re-opening of the economy, after the Circuit Breaker (CB) was lifted in June.

Fourth quarter growth momentum has continued to improve, but perhaps at a slower pace. The sharp rebound in economic activities in 3Q20 that came after the lifting of the CB in June is unlikely to be sustained in 4Q20. Moreover, sectors that have been the worst impacted by the pandemic, the hospitality and the aviation sectors, have also continued to struggle as the borders have generally remained shut to tourists. As such**, we are maintaining our full year GDP growth forecast for 2020 at -6.0%.**

Nevertheless, the economy is on the mend. Despair and disappointment that had dominated the global backdrop for much of the year is gradually giving way to hope and optimism of a recovery as we head into 2021 (*see DBS report "Singapore outlook 2021: Emerging optimism" dated 18 Nov20*). The manufacturing sector will continue to remain a key driver of growth, bolstered by strong electronics demand and biomedical production, while the construction and services sectors are expected to play catch-up in 2021 as domestic economic activities gradually resume to normalcy.

Growth improvement in regional markets such as China will be crucial, and likely to be sustained if expansionary fiscal and monetary policies remain intact. The new Biden administration could potentially provide more certainty to the US-China relationship, which will be beneficial to small and trade dependent countries such as Singapore.

However, Singapore can ill afford another Circuit Breaker. Yet, it is also extremely difficult to continue to keep the borders closed without taking a huge toll on the economy. A cautious and calibrated approach has been taken in this regard, but much will also depend on the ability of its regional economic partners such as China, Indonesia, and Malaysia in keeping the pandemic in check until an effective vaccine becomes available. The recent encouraging progress in vaccine development notwithstanding, the subsequent distribution of the vaccines and vaccination process in countries around the world will be just as crucial. Growth momentum will remain tepid and uneven in this K-shaped recovery. Different countries, industries and segments of the society will experience different pace of improvement. All these will have significant impact on Singapore's outlook.

The growth figures in the first half of next year will be highly volatile, due to the base effects this year. However, growth performance will be way above potential as the recovery gains momentum in the second half of next year, assuming that vaccines will become available and global travel can safely resume thereafter. **With that, we are maintaining our growth forecast of 2021 at 5.5%**.

Irvin Seah

South Korea: The K-New Deal

	2019	2020F	2021F	2022F
GDP growth, yoy%, ave	2.0	-1.1	2.9	2.8
Inflation, yoy%, ave	0.4	0.2	0.5	1.0
Policy rate, %, eop	1.25	0.50	0.50	0.75
KRW per USD, eop	1156	1113	1115	1113
10-year yield, %, eop	1.67	1.70	1.90	2.30

The economy is expected to grow 2.9% in 2021, a moderate rebound compared to the -1.1% contraction this year. Both consumption and exports will likely pick up at a moderate pace. The South Korean government plans to secure early supply of vaccines for 60% of its population, through the COVAX facility co-led by the WHO and the purchases from private drug makers. In the near term, however, the country still faces challenges from a third wave infection. Externally, as US, Europe and Japan achieve vaccine coverage in 2021, exports to advanced economies are likely to pick up. That said, demand from emerging markets would remain weak as some of them have limited access to vaccines. In our baseline forecast, South Korea's real GDP will revert to the pre-pandemic level by mid-2021, but the output gap will remain negative by the end of next year.

To reinvigorate the economy after the pandemic, President Moon's government has introduced the so-called K-New Deal in July. The government will spend KRW160tn (8% of GDP) in the next five years, to create jobs in in the digital and green energy sectors and to enhance the social safety net. The **Digital New Deal** involves investment in big data, 5G and AI to build digital education infrastructures, smart hospitals, smart cities, smart industrial complexes, smart logistics centers, among others. The **Green New Deal** requires investment in eco-friendly infrastructures and renewable energy, to achieve the 2030 greenhouse gas emission reduction target and to reach 20% renewable energy production by 2030. Moon's government should be in a good position to implement the K-New Deal in 2021. Although his approval ratings have declined, the ruling Democratic Party controls close to 180 of the total 300 seats in the parliament. There should be no strong hurdles for Moon's government to pass the needed bills in 2021, which is not an election year in South Korea.

Fiscal policy will remain expansionary. Net fiscal deficit (excluding social security funds) is likely to have exceeded 6% of GDP this year, as a result of the four supplementary budgets to cushion the impact of COVID-19. Under the general budget for 2021, fiscal deficit ratio will remain at 5.4% and public debt ratio will rise further to 47% from 44%. **Monetary policy will remain accommodative, but further easing is unlikely**. The Bank of Korea has cut the short-term policy rate by 75bps this year and conducted ad hoc purchases of government bonds to contain the long-term yields. Fueled by abundant liquidity, property prices in Seoul soared by almost 8%, despite the tightening of tax measures. Asset inflation risk is likely to dissuade the BOK from extra easing in 2021.

On external ties, Biden's administration may move to adopt a multilateral approach on trade and thus reduce tensions with South Korea (Trump demanded the renegotiation of South Korea-US bilateral FTA). Meanwhile, the launch of the RCEP should be positive for South Korea, given its close trade and investment ties with China, Japan and ASEAN and the lack of a bilateral FTA with Japan at present.

Ma Tieying

Taiwan: Riding the tech wave

	2019	2020F	2021F	2022F
GDP growth, yoy%, ave	3.0	1.8	4.2	2.8
Inflation, yoy%, ave	0.6	0.1	0.5	1.0
Core inflation, yoy%, ave	0.5	0.3	0.5	0.9
Policy rate, %, eop	1.375	1.125	1.125	1.25

Along with China and Vietnam, Taiwan is one of the three Asian economies that has maintained positive growth this year despite the COVID-19 pandemic. Thanks to the government's early and effective response to the pandemic as well as the strong performance of the technology sector, GDP growth contracted briefly in 1H (-1.8% QoQ saar in 1Q, -2.8% in 2Q) and staged a resilient rebound in 2H (16.6% in 3Q). The seasonally adjusted real GDP has recovered to the pre-pandemic normal levels by end-2020.

Looking ahead, **we expect GDP growth to pick up to 4.2% in 2021 from around 2% this year, and CPI inflation to rise to 0.5% from around zero**. The tech sector – semiconductor in particular – will likely remain as the key driver. Global demand for computers and consumer electronics is expected to decline next year, as the one-off purchases related to remote work and distance learning dissipate. On the other hand, demand for cloud, data centers and 5G will likely continue to increase in 2021, as many countries around the world build digital infrastructures and push for the process of digital transformation after the pandemic. In addition, smartphone demand is poised to recover in 2021, as global income conditions improve and more consumers move to upgrade smartphones amid the expansion of 5G networks. Overall, the outlook for semiconductor demand remains constructive.

Fiscal and monetary policies are expected to stay the course next year. Fiscal deficit is likely to have exceeded 2% of GDP this year due to tax revenue declines and the special budgets to counter the impact of COVID-19. Under the general and special budgets for 2021, the government intends to keep the fiscal deficit ratio roughly unchanged at 2%. On monetary front, the benchmark discount rate was lowered by 25bps this year, and the TWD appreciated about 5% versus the USD, thanks to the relatively stable domestic interest rate environment. We expect the central bank to hold the discount rate steady at 1.125% through 2021. The urgency of rate normalisation would remain low in the near term, given the mild inflation outlook and the strong TWD. The authorities may move to tighten macro-prudential measures next year, in response to the surge in real estate prices.

On the external side, **potential impact of the US's leadership transition is worth watching**. There could be some tactical adjustments in China-US trade issues as multilateralism regains US support under Biden's administration. But the two countries' rivalry in the tech sector would continue, given the bipartisan concerns in the US about the national security risk resulting from China's advances in 5G, AI and other new technologies. To Taiwan, the trade disruption risk as a result of China-US trade war may decrease in 2021. But pressure would remain for the Taiwanese tech companies to diversify their supply chains to hedge the risk of China-US tech tensions. In addition, leadership transition in the US creates some uncertainties for the outlook of a bilateral FTA between Taiwan and the US. The focus of Taiwan's FTA talks may shift towards the multilateral agreements like the CPTPP going forward.

Ma Tieying

Thailand: Banking on external normalcy

	2019	2020f	2021f	2022f
Growth (y/y %)	2.4	-6.3	3.5	2.2
Inflation (y/y %)	0.7	-1.0	1.0	1.3
Currency, vs USD eop	29.7	30.5	30.4	29.6
Policy rate, % eop	1.25	0.50	0.50	0.50
10-year yield, % eop	1.47	1.55	1.75	2.05

Thailand is amongst the few countries in the region to have efficiently contained the COVID-19 curve, keeping total cases below 4000 alongside a low mortality rate. Domestic activity is gradually returning to normalcy, with benign inflation also boosting real purchasing power. While capital investment plans are likely to stay on hold due to the pandemic-driven overhang and pressure on margins, the private sector (domestically-oriented) is seeking to raise capacity utilisation to meet demand. External-linked sectors, mainly trade and tourism, are still under a cloud. Factoring in the likelihood of a sequential improvement in 4Q20 due to higher public spending and better export growth, full-year **2020 growth is likely to average -6.3% y/y, better than our earlier forecast of -7.5% forecast.**

For 2021, base effects, fiscal spending and external trade are expected to underpin recovery. Accelerating public spending (stimulus ~8.2% of GDP (IMF)) might also provide support at the margin, with lagged lift to consumption by cash aids in 2020 as well as extra headroom for more support on account of extra budgetary firepower still left in the coffers from this year's outlays. Cyclical lift in the global trade cycle, especially in particular sectors of medical equipment, pharma, electronics, auto etc. is expected to sustain.

However, **there will be counterweights** by way of sub-par domestic drivers, as consumption spending is weighed by income and employment uncertainty on the back of excess capacity in tourism (20% of GDP including allied sectors) and discretionary service sectors. Thai authorities have considered long-stay tourist visas, which might be adopted on ad-hoc basis, however a complete reopening of international borders will still prove elusive unless mass vaccination is rolled out. Legacy concerns over high household debt and an ageing society impose some longer-term constraints on structural growth trend. 2021 GDP growth there is likely to be below trend at 3.5% y/y, with a earlier than assumed revival in tourism sector performance and faster demand revival posing upside risks.

With policy rates at a record low of 0.5%, we expect the BOT to stay on pause in 2021, backed by its optimism on recovery prospects, limited policy space, calls for higher fiscal policy participation and diminishing utility of rates on the THB. Non-rate measures will dominate efforts to tame the currency after sharp gains in 2020, following up with November 2020 measures, for instance allowing residents can use foreign currency deposit transactions to diversify investments, increase in overseas investment limit for retail investors, allowing local listing of foreign securities such as ETFs etc. Ongoing protests calling for constitutional reforms warrant attention, with sporadic escalation in tensions. While the government has initiated discussions, we don't expect any material imminent changes.

Radhika Rao

Vietnam: Still shining bright

	2019	2020F	2021F	2022F
Growth, yoy%, ave	7.0	2.7	6.7	6.8
Inflation, yoy%, ave	2.8	3.7	3.3	3.6
Core inflation, yoy%, ave	2.0	2.5	2.4	2.6
Currency, vs USD, eop	23155	23190	23050	22850
Policy rate, %, eop	6.00	4.00	5.00	5.00

Vietnam has been a shining example in the region in terms of its ability to contain the spread of the pandemic. Not only does it have the least number of cases amongst ASEAN-6 but also broader Asia, together with preventing fatalities. This can be attributed to early detection, decisive actions taken by the state, such as being the first to close its land borders with China and imposing strict lockdown on towns at the early onset of the pandemic. Thorough contact tracings, mass testing and travel ban were also implemented swiftly to contain the spread. As the country doesn't have a robust healthcare system, it opted to act pre-emptively and aggressively to contain the spread.

Yet, the economy has not been spared the impact of the pandemic. Like many countries in the region, GDP growth dipped in the second quarter, to just 0.4% YoY. Though the downturn has been less severe compared to most regional peers, it is by no means moderate in Vietnam's context. Yet, economic activities soon recovered in 3Q20 with an expansion of 2.6%. Coupled with a projected growth of 4.0% in the fourth quarter, full year GDP growth for 2020 is expected to register 2.7%, way lower than the strong showing of 7.0% in 2019. Indeed, a recovery now lies ahead but not without significant costs to the economy.

Export growth has been strong in recent months, and will likely remain so heading into 2021, particularly given the economic turnaround in some of the key regional markets such as China. We expect the manufacturing sector to be a key driver of growth, bolstered by gradual improvement in domestic services and construction activities. Private consumption and investment growth could provide added impetus to growth, beyond the expected boost from the recovery in external demand and trade flows. **This should lift GDP growth to 6.7% in 2021, but with more pronounced improvement from 2Q21 onwards**.

Beyond fiscal measures, monetary policy has been a fundamental support for the economy. The State Bank of Vietnam (SBV) cut the refinance rate by 200bps to 4.00% this year, which is much in line with our expectation. Going forward, it is imperative to sustain the recovery process by maintaining an accommodative monetary policy. And with inflation expected to remain benign in 2021, the central bank will stick to the status quo before resuming its hiking cycle in 2H21. **We expect the SBV to hike policy rate by 100bps to 5.00% in the second half of next year.**

The external environment could remain conducive, with the new US administration providing more certainty in trade, and easing pressure on Vietnam amid the its rising trade surplus with the US. Indeed, the trade surplus with the US will continue to growth amid the diversification of trade and investment flows from China to ASEAN. **Vietnam will remain a key beneficiary in the reshuffling of regional supply chains in the coming years**.

Irvin Seah

Growth, Inflation, & Policy Rates forecasts

	GDP growth, % YoY					CPI inflation, % YoY, ave				
	2018	2019	2020f	2021f	2022f	2018	2019	2020f	2021f	2022f
China	6.7	6.1	2.0	7.0	5.5	2.1	2.9	2.3	2.5	2.5
Hong Kong	2.8	-1.2	-7.0	4.0	2.3	2.4	2.9	0.7	2.0	2.5
India	6.8	4.9	-7.4	7.6	4.3	4.0	3.7	6.7	4.2	4.0
*India (FY basis)**	*6.2*	*4.2*	*-8.0*	*7.7*	*4.5*	*3.4*	*4.8*	*6.3*	*4.3*	*4.0*
Indonesia	5.2	5.0	-2.0	4.0	4.5	3.2	2.8	2.0	2.2	2.8
Malaysia	4.7	4.3	-6.8	6.0	4.8	1.0	0.7	-1.1	1.4	2.0
Philippines**	6.2	5.9	-9.5	7.0	6.0	5.2	2.5	2.4	3.0	2.8
Singapore	3.1	0.7	-6.0	5.5	3.2	0.4	0.6	-0.2	0.9	1.5
South Korea	2.9	2.0	-1.1	2.9	2.8	1.5	0.4	0.2	0.5	1.0
Taiwan	2.8	3.0	1.8	4.2	2.8	1.3	0.6	0.1	0.5	1.0
Thailand	4.2	2.4	-6.3	3.5	2.2	1.1	0.7	-1.0	1.0	1.3
Vietnam	7.1	7.0	2.7	6.7	6.8	3.5	2.8	3.7	3.3	3.6
Eurozone	1.9	0.9	-8.0	4.0	3.5	1.8	1.2	0.3	1.0	1.2
Japan	0.3	0.7	-5.0	2.8	1.5	1.0	0.5	-0.1	0.0	0.5
United States***	2.9	2.3	-3.5	5.0	2.2	1.9	2.3	1.3	1.7	2.2

* refers to fiscal years i.e. 2020 represents FY21 - year ending March 2021 ** new CPI series *** eop for CPI inflation

	Policy interest rates, eop							
	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22
China*	3.85	3.85	3.85	3.85	3.85	3.85	3.85	4.05
India	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00
Indonesia	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Malaysia	1.75	1.75	2.00	2.00	2.25	2.50	2.50	2.50
Philippines	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Singapore**	0.12	0.12	0.12	0.12	0.12	0.12	0.12	0.12
South Korea	0.50	0.50	0.50	0.50	0.50	0.50	0.75	0.75
Taiwan	1.13	1.13	1.13	1.13	1.13	1.13	1.13	1.25
Thailand	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Vietnam***	4.00	4.50	5.00	5.00	5.00	5.00	5.00	5.00
Eurozone	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Japan	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
United States	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25

* 1-yr Loan Prime Rate; ** 3M SORA OIS ; *** prime rate

FX forecasts

	Exchange rates, eop							
	1Q21	2Q21	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22
USD/CNY	6.70	6.67	6.64	6.61	6.59	6.56	6.53	6.50
USD/HKD	7.76	7.76	7.77	7.77	7.78	7.79	7.79	7.80
USD/INR	74.8	74.7	74.6	74.5	74.4	74.3	74.2	74.1
USD/IDR	14500	14429	14357	14286	14214	14143	14071	14000
USD/MYR	4.12	4.10	4.09	4.07	4.05	4.03	4.02	4.00
USD/PHP	48.5	48.3	48.2	48.0	47.8	47.7	47.5	47.3
USD/SGD	1.36	1.35	1.35	1.34	1.33	1.32	1.32	1.31
USD/KRW	1,116	1,116	1,116	1,115	1,115	1,114	1,114	1,113
USD/THB	31.0	30.8	30.6	30.4	30.2	30.0	29.8	29.6
USD/VND	23200	23150	23100	23050	23000	22950	22900	22850
AUD/USD	0.73	0.73	0.73	0.74	0.74	0.75	0.75	0.76
EUR/USD	1.16	1.17	1.19	1.20	1.21	1.22	1.24	1.25
USD/JPY	106	106	106	106	105	105	105	105
GBP/USD	1.29	1.30	1.31	1.32	1.33	1.34	1.35	1.36

Australia, Eurozone and United Kingdom are directed quotes

Rates Forecasts

Interest rate forecasts

		2020	2021				2022			
		Q4	Q1	Q2	Q3	**Q4**	Q1	Q2	Q3	**Q4**
US	3M SOFR OIS	0.10	0.10	0.10	0.10	**0.10**	0.10	0.10	0.10	**0.10**
	2Y	0.20	0.20	0.20	0.23	**0.25**	0.30	0.35	0.40	**0.45**
	10Y	0.95	1.05	1.15	1.25	**1.30**	1.40	1.50	1.60	**1.70**
	10Y-2Y	75	85	95	102	**105**	110	115	120	**125**
Japan	3M TIBOR	0.07	0.07	0.07	0.07	**0.07**	0.07	0.07	0.07	**0.07**
	2Y	-0.13	-0.13	-0.10	-0.10	**-0.10**	-0.10	-0.10	-0.10	**-0.10**
	10Y	0.05	0.05	0.05	0.08	**0.10**	0.10	0.10	0.10	**0.10**
	10Y-2Y	18	18	15	18	**20**	20	20	20	**20**
Eurozone	3M EURIBOR	-0.50	-0.50	-0.50	-0.50	**-0.50**	-0.50	-0.50	-0.50	**-0.50**
	2Y	-0.80	-0.80	-0.70	-0.65	**-0.60**	-0.60	-0.60	-0.60	**-0.60**
	10Y	-0.55	-0.55	-0.50	-0.45	**-0.40**	-0.35	-0.30	-0.30	**-0.30**
	10Y-2Y	25	25	20	20	**20**	25	30	30	**30**
Indonesia	3M JIBOR	4.25	4.25	4.25	4.25	**4.25**	4.25	4.25	4.25	**4.25**
	2Y	4.50	4.50	4.55	4.65	**4.80**	4.90	5.00	5.00	**5.00**
	10Y	6.00	6.00	6.20	6.40	**6.60**	6.80	6.90	7.00	**7.00**
	10Y-2Y	150	150	165	175	**180**	190	190	200	**200**
Malaysia	3M KLIBOR	1.95	1.95	1.95	2.20	**2.20**	2.45	2.70	2.70	**2.70**
	3Y	1.80	1.80	1.80	2.10	**2.10**	2.40	2.60	2.60	**2.60**
	10Y	2.75	2.75	2.85	3.05	**3.10**	3.30	3.40	3.40	**3.40**
	10Y-3Y	95	95	105	95	**100**	90	80	80	**80**
Philippines	3M PHP ref rate	1.75	1.75	1.75	1.75	**1.75**	1.85	1.95	2.05	**2.15**
	2Y	2.00	2.00	2.00	2.00	**2.00**	2.05	2.10	2.15	**2.20**
	10Y	3.00	3.00	3.00	2.90	**2.90**	2.80	2.90	3.00	**3.10**
	10Y-2Y	100	100	100	90	**90**	75	80	85	**90**
Singapore	3M SORA OIS	0.12	0.12	0.12	0.12	**0.12**	0.12	0.12	0.12	**0.12**
	2Y	0.25	0.25	0.25	0.25	**0.25**	0.27	0.30	0.35	**0.40**
	10Y	0.95	1.00	1.05	1.10	**1.10**	1.15	1.20	1.30	**1.35**
	10Y-2Y	70	75	80	85	**85**	88	90	95	**95**
Thailand	3M BIBOR	0.62	0.62	0.62	0.62	**0.62**	0.62	0.62	0.62	**0.62**
	2Y	0.50	0.50	0.50	0.50	**0.50**	0.50	0.50	0.50	**0.50**
	10Y	1.55	1.55	1.65	1.70	**1.75**	1.80	1.90	1.95	**2.05**
	10Y-2Y	105	105	115	120	**125**	130	140	145	**155**
China	1Y LPR	3.85	3.85	3.85	3.85	**3.85**	3.85	3.85	3.85	**4.05**
	2Y	3.05	3.05	3.10	3.15	**3.20**	3.20	3.20	3.20	**3.20**
	10Y	3.20	3.25	3.30	3.35	**3.40**	3.40	3.40	3.40	**3.40**
	10Y-2Y	20	20	20	20	**20**	20	20	20	**20**
Hong Kong	3M HIBOR	0.40	0.40	0.40	0.40	**0.40**	0.40	0.40	0.40	**0.40**
	2Y	0.20	0.20	0.20	0.23	**0.25**	0.30	0.35	0.40	**0.45**
	10Y	0.60	0.70	0.80	0.85	**0.90**	1.00	1.10	1.20	**1.30**
	10Y-2Y	40	50	60	62	**65**	70	75	80	**85**
Korea	3M CD	0.65	0.65	0.65	0.65	**0.65**	0.65	0.65	0.90	**0.90**
	3Y	1.05	1.05	1.10	1.15	**1.20**	1.30	1.40	1.50	**1.50**
	10Y	1.70	1.70	1.75	1.85	**1.90**	2.00	2.10	2.20	**2.30**
	10Y-3Y	65	65	65	70	**70**	70	70	70	**80**
India	3M MIBOR	3.75	3.75	3.75	3.85	**3.95**	4.05	4.15	4.25	**4.25**
	2Y	4.30	4.40	4.50	4.50	**4.50**	4.50	4.60	4.70	**4.80**
	10Y	5.80	5.90	6.00	6.10	**6.20**	6.30	6.40	6.50	**6.50**
	10Y-2Y	160	150	150	160	**170**	180	180	180	**170**

%, eop, govt bond yield for 2Y and 10Y, spread bps

Rates Forecasts

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