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They say it may get bumpy

With soaring growth, and a bright future, Asia appears strapped in for another year of stellar growth

Even as the massive policy boost fades, the region should have enough fuel to overcome the lure of gravity

But, inflation could explode as Asia goes full throttle, and rate hikes may yet throw the region out of orbit

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Disclosures and Disclaimer This report must be read with the disclosures and analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it

Summary

It feels, at times, like riding a rocket. Over the past year, Asia saw the wildest swings in industrial output in recent memory. Then, growth rebounded, and soaring markets started to worry about impending exits from extreme policy accommodation. What will the coming year bring? Good news, we remain convinced. Asia's economies have entered a sustained growth cycle, and even the withdrawal of official stimulus measures will do no harm. Still, a key risk remains: inflation. Commodities are already surging ahead, and core measures are perking up as well. If price pressures erupt, rapid rate hikes may bring the region back to earth. But, for now, it remains suspended in flight.

One thing leads to another

Speaking of a bounce. Breathtaking as Asia's collapse may have been, so was the subsequent recovery. By the third quarter of last year, the region had recouped all of its losses, and more: now output comfortably exceeds the previous peak. The initial burst, to be sure, was sparked by a hefty dose of policy adrenalin. Rates were slashed, bankers told to lend, and bridges built in every country. But, it is wrong to see Asia's recovery as being entirely policy-driven. Already over the course of last year, the private sector began to respond swiftly to public initiatives. With its banking systems unaffected by Western calamity, this turned out to be a cyclical, not a structural, recession for Asia. As in any such episode, a boost from policy-makers helped to bring the economy back to life. Now, the region has entered a self-sustaining expansion cycle.

Start with Asia's pump-priming. Massive public works projects, rolled out at an impressive speed, helped to boost demand in the initial phase. As firms began to hire workers, incomes started to recover. Then, with more cash jangling in their pockets, consumers returned to the shops, further boosting the economy. Lastly, rebounding domestic demand revived trade as imports fed into the local economy. A simple picture, to be sure, but one that isn't too far from the truth. Consider the evidence. By the middle of the second quarter, real household spending turned positive in Asia in annual terms, and goods such as cars and electronics, admittedly with a few incentives from the public purse, began to fly off the shelves. China, after all, was the world's biggest car market last year, and more and more consumer electronics are finding a home in Asia.

Labour markets too have begun to tighten, with hiring turning positive in the third quarter. By the end of the year, our regional employment index hovered near record highs. With resurging demand, the regional trade cycle also fired up. While exports to the West recovered only gradually, shipments to China by its neighbours consistently hit highs, suggesting that a good chunk of these are now consumed domestically. The process worked in the other direction as well: China exported more and more goods to other Asian

economies, not quite making up for weakness in advanced countries, but enough to push the country's shipments back to near peak levels.

This self-reinforcing cycle of regional growth is expected to persist well beyond this year. Even if the policy stimulus, most notably from the fiscal side, begins to wane over the course of 2010, Asia's economies should have enough momentum to carry through. Growing intra-regional trade should also insulate the region against a double dip in the West and the inevitable fading of an impending restocking bounce. Of course, rapidly rising exchange rates and asset bubbles might lead to headaches, but a fatal blow from either of these appears unlikely for the time being. In short, Asia enters 2010 in robust shape and growth should settle into a comfortable pace for a while. As a result, we expect the region, excluding Japan, to grow by 7.8%, with China and India leading the way. Given our long-standing bullish view on the region, we have left most of our forecasts untouched as these already anticipated events that continue to unfold.

One key risk, however, remains. Inflation may yet rear its head in 2010, bringing back dreaded memories of 2008 when it spiralled relentlessly upwards. Already, the cost of raw materials has started to climb and firms are reporting soaring output prices, which usually foreshadows a pick-up in core CPI readings as well. For now, our base case remains that inflation will stay bottled up. If anything, it currently appears that it may soar over the first half only to temper later in the year. Still, complacency is not warranted, and there are growing signs that the behaviour of inflation has changed in Asia over time, with core readings more and more sensitive to second-round effects of volatile food and energy costs. As monthly inflation readings begin to rise, policy-makers may stay aloof for longer than markets may like, with central banks taking the heat from their political authorities who remain overly wedded to perceived growth risks from a Western double dip. In that case, Asia would only delay the inevitable, which is a tightening of monetary policy, implying the need for more aggressive action later on. The risk for Asia, in short, is not lack of growth, but the inability of policy-makers to anticipate the implications of its strength.

HSBC Main Forecasts (current vs. Asian Economic Quarterly 4Q 2009)

	2009 (old)	2009 (new)	2010 (old)	2010 (new)	2011 (old)	2011 (new)	2009 consensus	2010 consensus
Australia	0.8	0.8	2.6	2.6	2.8	2.8	1.1	2.9
China	8.1	8.5	9.5	9.5	8.9	8.9	8.5	9.6
Hong Kong	-4.0	-3.6	3.8	3.8	4.3	4.3	-2.9	4.5
India	6.2	7.2	8.0	8.5	8.5	8.3	6.6	7.7
Indonesia	4.3	4.3	5.8	5.8	5.5	5.5	4.5	5.6
Japan	-5.7	-5.2	1.2	1.0	1.1	1.2	-5.3	1.5
Korea	-0.4	0.4	4.6	5.2	4.9	4.8	0.0	4.7
Malaysia	-2.0	-2.0	6.8	6.8	5.5	5.5	-2.2	4.9
New Zealand	-1.4	-0.4	1.5	2.1	2.4	3.1	-1.2	2.5
Pakistan	0.8	0.8	2.6	2.6	3.7	3.7	2.9	3.5
Philippines	1.8	1.1	4.2	4.2	4.7	4.6	1.2	3.7
Singapore	-2.5	-2.2	6.5	6.5	5.5	5.5	-2.1	5.6
Sri Lanka	4.0	3.8	7.0	7.0	7.2	7.2	3.5	6.0
Taiwan	-4.2	-2.8	4.4	5.1	4.9	4.9	-3.4	4.6
Thailand	-2.8	-2.9	4.5	4.6	4.7	4.7	-3.0	4.2
Vietnam	4.9	5.3	6.8	6.8	5.9	5.9	4.9	6.4
Asia x JP	4.7	5.2	7.6	7.8	7.4	7.4	5.1	7.6
Asia x JP & CH	1.4	2.0	5.8	6.1	6.0	5.9	1.8	5.6
Asia x JP, CH & IN	-0.4	0.0	4.9	5.2	5.0	4.9	0.0	4.8

Source: HSBC, Consensus Economics; NB: Asia aggregates USD GDP weighted and excluding Australia and New Zealand

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Key forecasts

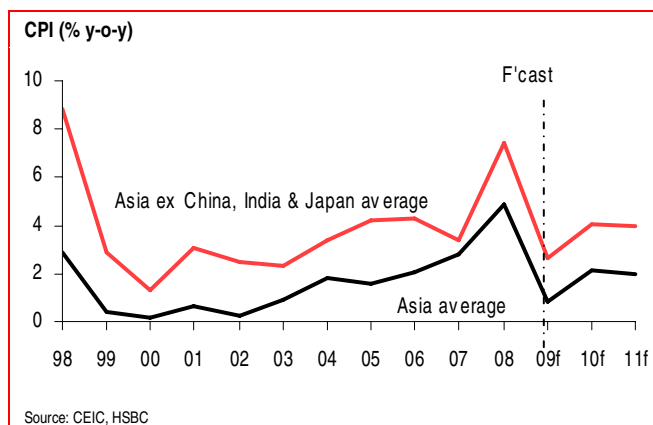
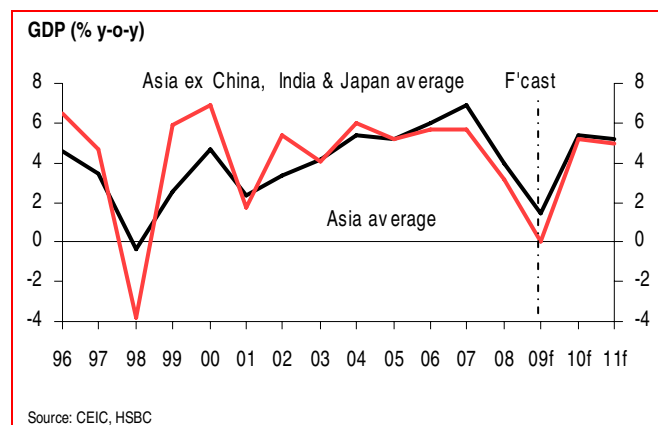
(% y-o-y)	Asia average	AU	CN	HK	IN	ID	JN	KR	NZ	MA	PK	PH	SG	SL	TW	TH	VN
Real GDP																	
2008	4.0	2.2	9.6	2.4	6.7	6.1	-1.2	2.2	-0.7	4.6	3.7	3.8	1.1	6.0	0.7	2.5	6.2
2009f	1.5	0.8	8.5	-3.6	7.2	4.3	-5.2	0.4	-0.4	-2.0	0.8	1.1	-2.2	3.8	-2.8	-2.9	5.3
2010f	5.4	2.6	9.5	3.8	8.5	5.8	1.0	5.2	2.1	6.8	2.6	4.2	6.5	7.0	5.1	4.6	6.8
2011f	5.2	2.8	8.9	4.3	8.3	5.5	1.2	4.8	3.1	5.5	3.7	4.6	5.5	7.2	4.9	4.7	5.9
Private consumption																	
2008	3.5	2.6	8.9	1.7	2.9	5.3	-0.7	0.9	-0.3	8.5	5.2	4.7	2.4	6.7	-0.6	2.7	7.6
2009f	2.8	2.1	8.0	-1.0	3.5	5.1	-0.9	0.1	-0.9	2.1	1.0	3.6	-1.2	3.5	0.9	-1.5	3.4
2010f	5.1	3.9	9.2	3.4	8.0	5.4	1.4	3.9	0.9	5.7	2.0	4.7	4.4	6.8	2.4	3.0	5.8
2011f	5.0	3.2	9.0	3.2	7.7	4.9	1.3	4.9	3.5	5.0	3.5	5.2	3.2	7.0	2.1	3.3	5.0
Fixed investment																	
2008	8.4	8.3	26.1	0.0	8.2	11.7	-2.6	-1.7	-2.7	0.8	-6.5	2.9	13.7	11.0	-11.2	1.2	13.2
2009f	4.4	-2.0	29.5	-5.5	8.0	3.8	-14.0	-1.0	-13.7	-8.0	3.0	-3.8	-4.9	4.5	-14.2	-8.1	3.2
2010f	9.1	3.2	26.0	6.6	14.0	8.7	-5.2	4.9	-1.4	4.1	4.0	5.6	8.0	13.0	7.1	5.4	8.0
2011f	8.2	4.6	20.0	5.8	12.3	7.4	-1.9	5.1	2.3	7.0	4.0	5.9	7.6	12.0	6.6	4.2	6.0
Current account balance* (% of GDP)																	
2008	4.5	-4.5	9.4	10.9	-3.1	0.0	3.2	-0.7	-8.8	17.5	-5.1	2.3	14.8	-9.3	6.2	0.6	-11.6
2009f	3.9	-3.6	4.9	9.7	-1.0	1.6	2.8	5.1	-1.8	16.1	0.7	4.9	10.8	1.2	10.1	8.3	-7.6
2010f	3.7	-3.7	4.1	10.3	-1.6	0.6	4.3	2.6	-8.5	13.9	2.0	5.2	10.3	0.5	6.5	3.5	-13.3
2011f	4.0	-4.1	4.0	11.1	-1.8	0.9	5.1	1.9	-7.8	13.4	2.7	4.9	10.9	-1.2	7.0	2.5	-5.9
CPI (period average)																	
2008	4.9	4.3	5.9	4.3	8.3	10.2	1.5	4.7	3.9	5.4	20.3	9.3	6.5	22.7	3.5	5.5	23.0
2009f	0.8	1.8	-0.9	0.7	10.5	4.8	-1.2	2.8	2.1	0.7	13.4	3.3	0.2	3.4	-0.9	-0.8	7.8
2010f	2.2	2.8	2.6	2.7	9.6	6.8	-1.2	3.3	2.2	3.3	7.7	5.2	2.9	7.5	1.2	3.0	10.1
2011f	2.0	3.0	2.5	3.0	6.0	7.0	-0.8	3.0	2.6	2.5	7.6	5.6	2.0	6.7	1.7	3.3	7.0
Money market interest rate** (% , year-end)																	
2008	3.9	4.1	1.7	1.0	8.5	12.0	0.4	4.7	5.1	3.4	n/a	6.1	1.0	n/a	1.0	3.0	n/a
2009f	2.4	4.1	1.7	0.1	4.2	6.9	0.3	2.8	2.8	2.2	n/a	5.5	0.7	n/a	0.5	1.4	n/a
2010f	3.0	5.0	2.0	0.4	5.0	8.1	0.3	3.2	3.9	2.5	n/a	6.8	0.8	n/a	1.9	2.3	n/a
2011f	3.4	5.0	2.0	1.3	5.3	8.1	0.3	4.2	3.9	6.5	n/a	6.8	1.0	n/a	-0.4	2.8	n/a
Exchange rate (vs. USD, year-end)																	
2008	n/a	0.70	6.82	7.75	48.7	11,325	91	1,260	0.58	3.45	79.0	47.4	1.44	113.3	32.8	34.7	17,483
2009f	n/a	0.90	6.83	7.80	46.5	9,480	95	1,164	0.72	3.44	84.4	46.1	1.40	114.4	31.5	33.4	18,479
2010f	n/a	1.00	6.66	7.80	46.5	8,800	105	1,075	0.76	3.46	92.0	43.5	1.34	118.0	29.0	31.5	18,400
2011f	n/a	1.00	6.40	7.80	44.5	8,800	105	1,050	0.76	3.42	92.0	42.5	1.32	118.0	28.0	31.0	18,400

* Hong Kong: current account refers to visible and invisible trade balance only

** China: 3-month time deposit; Hong Kong: 3-month HIBOR; India: 3-month T-Bill; Indonesia: 3-month SBI; Korea: 3-month CD yield; Malaysia: 3-month KLIBOR; Philippines: 3-month T-bill; Singapore: 3-month SIBOR;

Taiwan: 91-day secondary CP; Thailand: 3-month BIBOR. ***India GDP forecasts are fiscal-year basis.

Source: HSBC, CEIC; NB: Asia aggregate data are based on 2008 nominal USD weights and does not include Australia and New Zealand



Monetary & fiscal policy assumptions

Monetary policy

Period end (%)		1Q09	2Q09	3Q09	4Q09	1Q10e	2Q10e	3Q10e	4Q10e
Australia	RBA cash rate	3.25	3.00	3.00	3.75	4.00	4.25	4.25	4.50
China	1 year base lending rate	5.31	5.31	5.31	5.31	5.31	5.31	5.58	5.85
Hong Kong SAR	Base rate	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
India	Repo rate	5.00	4.75	4.75	4.75	5.00	5.25	5.75	6.25
Indonesia	SBI 28 day rate	7.75	7.00	6.50	6.50	6.50	7.00	7.50	8.00
Japan	Overnight call rate	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Korea	Overnight call rate	2.00	2.00	2.00	2.00	2.25	2.25	2.75	3.00
Malaysia	Overnight rate	2.00	2.00	2.00	2.00	2.00	2.00	2.25	2.50
New Zealand	RBNZ cash rate	3.00	2.50	3.50	2.50	2.50	2.75	3.00	3.25
Pakistan	Repo rate	15.00	14.00	13.00	13.00	10.00	9.00	9.00	9.00
Philippines	Reverse repo rate	4.75	4.25	4.00	4.00	4.00	4.25	4.50	4.75
Singapore	3 months rate	0.67	0.69	0.68	0.68	0.60	0.70	0.70	0.80
Sri Lanka	Repo rate	11.75	11.00	10.50	9.75	9.75	9.75	10.00	10.25
Taiwan	Rediscount rate	1.250	1.250	1.250	1.250	1.500	1.750	2.000	2.000
Thailand	1-day repo rate	1.50	1.25	1.25	1.25	1.25	1.50	1.75	2.00
Vietnam	Policy rate	7.00	7.00	7.00	8.00	9.00	10.00	11.00	12.00

Source: HSBC, CEIC

Fiscal policy assumptions for 2010

Australia	The stronger economic outlook has improved the outlook for tax receipts which will deliver lower deficits at 4.5% of GDP for 2009-10 and 3.6% for 2010-11. Net debt is now expected to peak at 10% of GDP, which is around AUD50bn. In 2010-11 the fiscal stimulus will be withdrawn in line with the gathering pace of the private sector recovery to avoid sudden changes.
China	Expansionary policy to stay in place to support growth but fiscal spending will shift from infrastructure investment to education and healthcare in an effort to reduce precautionary savings and achieve more balanced growth.
Hong Kong	With 10 major infrastructure projects commencing construction progressively since late 2009, the expansionary fiscal position will be maintained.
India	With stronger economic growth should come some structural tightening measures, although we are far from certain this will occur. There is a danger that capital spending will bear the brunt of any squeeze. We expect the central government deficit to fall below 6% of GDP in FY 2010/11.
Indonesia	In 2010, with growth picking up and the government likely to continue to underspend, we expect the budget deficit to improve to 1.7% of GDP.
Japan	According to the initial budget plan for FY10, most of the DPJ's election manifesto will be implemented, except for the gasoline tax, which will be maintained at current rates.
Korea	The National Assembly passed the 2010 budget with a 3% reduction compared to total spending of KRW302trn in 2009. The government frontloaded 70% of the budget in the first half of 2010 to boost the economy further. Despite a gradual economic recovery, a balanced budget is unlikely in 2010, suggesting that gross public debt will remain above 36% of GDP for the next five years. The scheduled tax cut for top corporate tax and individual income tax rates is postponed by two years considering the rising national debt level.
Malaysia	The government expects to reduce the 2010 budget deficit from 7.4% of GDP in 2009 to 5.6% via a near 14% drop in operational expenditure. We also expect a sharp drop in this year's deficit but more because of the cyclical benefits of strong growth.

Source: HSBC, CEIC

Fiscal policy assumptions for 2010

New Zealand	Higher expenditure is forecast to leave the fiscal balance in deficit over the medium term. We expect a budget deficit of 3.2% of GDP for 2010 and 3% of GDP for 2011, reflecting declining government spending as the economy recovers. According to Treasury, net debt, which was 9.5% of GDP at June 2009, will increase to 29% of GDP by June 2014.
Pakistan	Fiscal consolidation will have to endure, which means further caps on spending and efforts to mobilise government revenues. The fiscal sector should thus remain a drag on overall GDP growth, provided the government heeds the need for further consolidation of its accounts.
Philippines	Post elections in 2Q10, government spending should soften once more before the incoming administration draws up new spending plans. Revenue collection may improve as the economy embarks on recovery and commodity prices surge but will remain subdued given structural bottlenecks, keeping the deficit elevated.
Singapore	The February budget for 2010 is likely to see most of the stimulus measures of last year continued, but scaled back somewhat. It probably won't be until 2011 that Singapore returns to budget surplus.
Sri Lanka	Reconstruction work will remain high, though with growth turning around government finances should improve somewhat. We expect the budget deficit to tighten to 9.5% of GDP.
Taiwan	Fiscal stimulus packages carried out last year prompted the island's budget deficit to widen. However, gradual recovery in the economy will raise government revenue. Policymakers may consider raising various tax rates towards the end of 2010 to alleviate the financial burden. We expect the FY10 budget deficit to narrow to -2.6% of GDP from -3.5% last year.
Thailand	The government has embarked on a three-year public investment program of THB1,431bn (15% of GDP). The government expects that the next round of fiscal stimulus will raise the fiscal deficit of 4.5% of GDP in the current fiscal year ending September 2010, up from 3.4% in 2008/09. Thus, we expect the public sector debt to GDP ratio will rise to 48% in 2010 from 38% in 2009 with the widening budget deficit.
Vietnam	With the trade deficit and inflation both rising sharply and the dong under downward pressure, the government needs to tighten the purse-strings significantly. The question is: will it be prepared to do so?

Source: HSBC, CEIC

Enter the virtuous circle

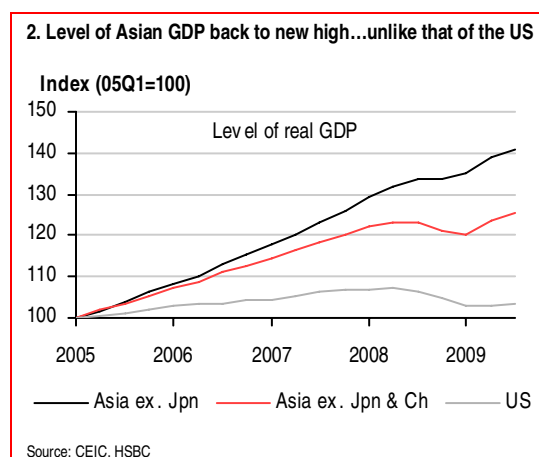
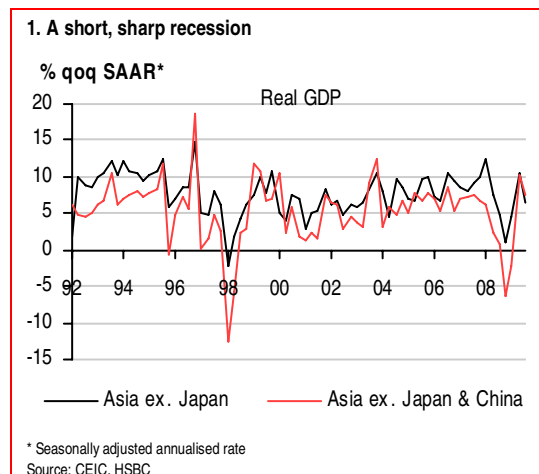
- ▶ Asia's economic recovery looks well entrenched...
- ▶ ...having entered a self-sustaining phase
- ▶ Worries about growth appear overdone

20/20 hindsight

This time last year, we argued that investors and forecasters should not panic about the economic outlook in Asia. Our key thesis was that, while first quarter GDP would surprise on the downside, there would be plenty of green shoots in evidence by the middle of the year, with a strong V-shaped recovery emerging in the second half.

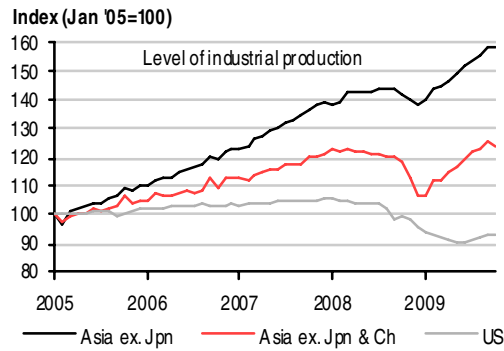
Hindsight is a wonderful thing, and we now know that the economic recovery actually started earlier and was even stronger than we anticipated during the dark days of early 2009 (chart 1). According to our calculations, the level of Asia ex. Japan and China GDP rose an annualised 8.8% from April to September (chart 2). This represents a stronger recovery than the region experienced in the six months following the end of the Asian Financial Crisis in early 1998.

The strength of the improvement meant that, by 3Q last year, the level of Asia ex. Japan and China GDP had more than recovered from the output losses suffered during the recession from 3Q08 to 1Q09 (chart 2). If we include China, the level of Asian GDP never actually contracted during the "global" recession and was already up 5.6% year-on-year in the third quarter. However, as the chart shows, the same cannot be said of the US, where real GDP recorded its first rise in 3Q09 and is still more than 3% below the previous peak.



The comparison with the US is even more striking if we look at industrial production (again, in seasonally adjusted terms). From the bottom of Asia's industrial cycle in December 2008 to October 2009, Asian ex. Japan output rose nearly

3. Spot the difference



Source: CEIC, HSBC

15%, while US production fell 3% over the same period (chart 3). If “decoupling” was not such a dirty word these days it would be tempting to use it in this context.

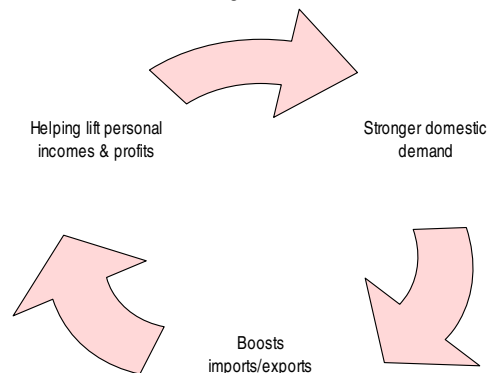
Against this background, the debate has now shifted from when the Asian recovery will start and how strong the initial bounce will prove to be, to the sustainability of the improvement. There are many who remain nervous, and we will address their key concerns in this section. Before doing so, however, it is worth reiterating the reasons behind our relatively upbeat 2010-11 growth forecasts for the region.

A virtuous circle of growth

In a nutshell, we believe Asia has entered a virtuous, self-sustaining period of economic growth. A recovery in domestic demand was kick-

started by relief that the World was not heading in to a second Great Depression as well as the initial effects of the huge global policy response. This is then boosting imports (and therefore, by definition, exports), in turn pushing personal incomes and profits up, the impact of which is to further support domestic demand, and so on (chart 4).

4. Asia's virtuous circle of growth

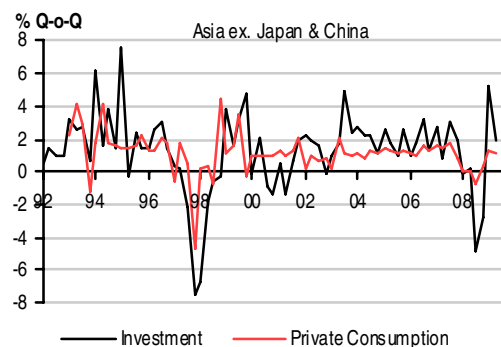


Source: HSBC

Where's the evidence?

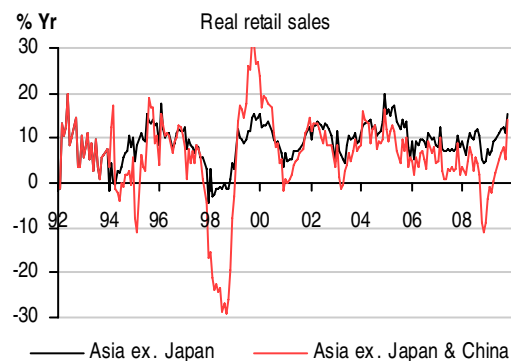
So what evidence is there to suggest that this process is under way? Luckily, there is quite a lot. First, consumer spending and fixed investment bounced back smartly in 2Q and 3Q last year, and not just in China (chart 5). Also, more timely real retail sales data are looking increasingly encouraging, as shown in chart 6.

5. Decent rebound in investment and private consumption



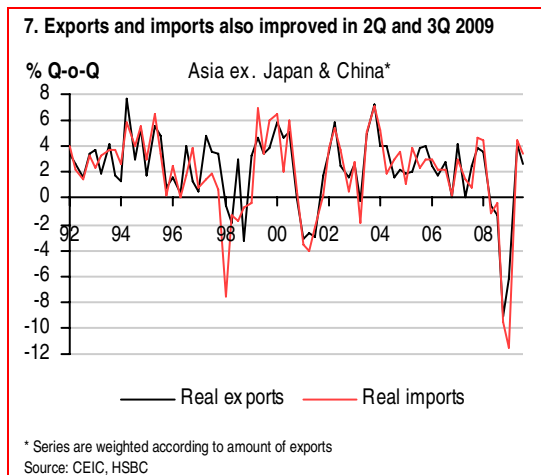
Source: CEIC, HSBC

6. Real retail sales rebounding nicely



Source: CEIC, HSBC

Second, imports and exports have begun to expand again on a quarter-on-quarter basis, as shown in chart 7, which extends to 3Q09 (here we have had to exclude China because it does not publish volume numbers on a quarterly basis).

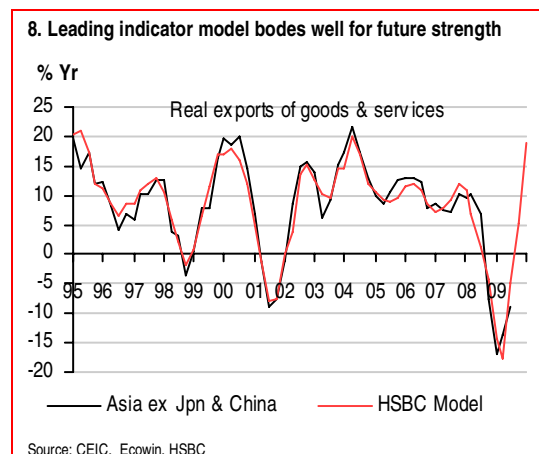


The improvement may not seem so impressive given the scale of the downturn, but there are a couple of points to bear in mind here:

- ▶ The extent of the pick-up would have been bigger if not for sizeable ongoing falls in Indian exports and imports. No other Asian country has seen such declines recently and, to be frank, they are hard to rationalise. They do not fit with what has been happening to Indian export and import *values* which, according to our calculations, both registered quarter-on-quarter non-annualised gains of 9.8% in seasonally adjusted terms in the July-September quarter. Past experience suggests that the expenditure breakdown of Indian GDP is often revised significantly, and we won't be surprised if history repeats itself.
- ▶ The recent improvement in regional real exports and imports has been sharper than that witnessed after either the Asian Financial Crisis or the tech-related bust of 2001. Contrary to conventional wisdom, as we have pointed out many times in the past, Asian

export growth is often a lagging indicator of Asian consumption and investment growth rather than vice versa.

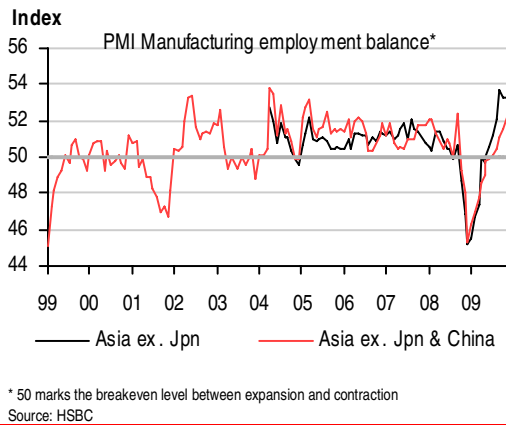
Looking ahead, our export lead indicator, which we constructed in mid-2008, bodes well for further strength (chart 8). The model extends to the first quarter of 2010, where it suggests Asian real export growth could be running at close to 20%. Although this is on a year-on-year basis, it should be stressed that to achieve this kind of growth rate would require the *level* of exports to rise roughly 10% from 3Q09 in seasonally adjusted terms.



The remaining element of the virtuous circle is rising real incomes and profits. Here, data lags, or holes, make it impossible to know precisely how things are developing in a timely fashion, though clues are provided by a couple of series.

We know, for example, that the profits of quoted companies in Asia are on the mend again. Also, our aggregated PMI employment variable for Asia has shot up and is again consistent with positive job growth in both manufacturing and services (given that the indices are above the 50 no-change level – see chart 9). If correct, this is likely to be consistent with improving personal incomes and consumer confidence.

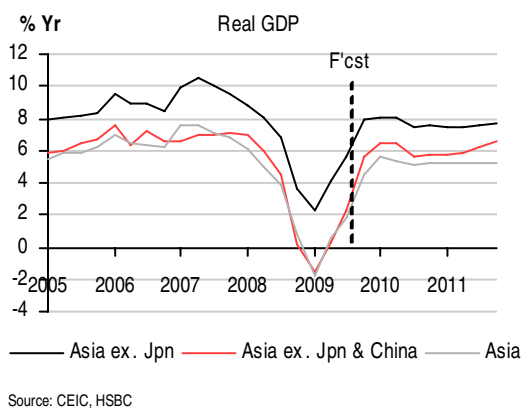
9. Asia is recruiting again, and strongly



The forecasts

With all this in mind, chart 10 shows how we expect Asian economic growth to unfold over the next couple of years. That is, a further improvement in year-on-year growth rates up to the first quarter of this year, followed by a dip, as last year's huge quarter-on-quarter GDP increases fall out of the annual comparison, and then stability in 2011. In quarter-on-quarter terms, we may well already have passed the strongest increase (in 2Q09), but the sequential growth rates are likely to remain firm for the reasons discussed.

10. A strong, sustainable recovery



Our precise year average growth forecasts are as follows:

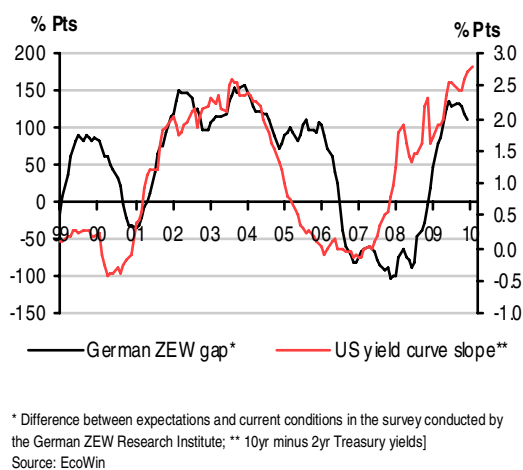
- ▶ In Asia as a whole, after just 1.5% growth in 2009 (the lowest since 1998), we expect a

5.4% GDP rise in 2010, followed by 5.2% in 2011. The pace of growth should be held back by Japan, where we expect GDP to rise just 1% this year and 1.2% next.

- ▶ For Asia excluding Japan, we are looking for GDP to register 7.8% growth in 2010 and 7.4% in 2011 (following a 5.2% rise in 2009, the weakest since 2001).
- ▶ Excluding both Japan and China, Asia is likely to expand around 6.1% and 5.9% respectively this year and next (after a 2% rise in 2009, the lowest since 1998).

Some support for the view that the economic recovery will prove durable is provided by chart 11. This shows the two lead indicators which have consistently provided a 2-2½ year lead to turning points in global/Asian GDP growth. Neither has shown a definitive turn for the worse as yet, although the ZEW measure is looking as though it might be topping out now.

11. Long leading indicators support the case



Considering the risks

So far, we have described how, in theory, the virtuous circle of growth works and provided evidence that it has indeed begun in Asia. But that is not to say that the circle cannot be broken, and we will consider five of the most oft-heard

concerns in the rest of this chapter, leaving the issue of inflation risk to the next section.

1. US double-dip

At the top of the risk list, as far as most are concerned, is the possibility of a renewed recession in the States. After all, it is widely accepted that US households, financial institutions and the government continue to hold far too much debt on their balance sheets and must deleverage significantly. This could lead to a devastating period of debt deflation similar to that of Japan.

The US policy authorities continue to fight hard against such an outcome and so far look to be winning the battle, as the housing market is on the mend, manufacturing orders have soared, and the US consumer is even spending again (perhaps prematurely). In the view of our colleagues, a move back into recession will be avoided in the US (as well as Europe and Japan), although economic activity, particularly consumer spending, is hardly likely to be stellar. Nevertheless, plenty of uncertainty inevitably surrounds such a view, and it is possible that, even if the developed world avoids another outright recession over the next couple of years, growth could still soften again.

In Asia, we have spent a fair chunk of the last two years analysing in detail the linkages between the western world and our own region, with the following conclusions:

- ▶ The importance of the developed world in general and the US in particular as drivers of Asian growth is often overstated. This is *not* to say that what happens there is irrelevant; but it is only one of several factors that drive Asian activity. Even in the most open of Asian economies, such as Malaysia and Singapore, simple correlation analysis suggests that the US is not the be all and end all for the performance of these countries. Asia itself is a major source of domestic

demand, with capital spending in the region, even excluding Japan, 20% higher than the US in 2008. This gap will have grown wider in 2009 and will likely continue to do so.

- ▶ This prompts the question, Why did Asia suffer so badly during the US-inspired credit crunch? Here, we have argued that the crisis was so severe (the worst since the Great Depression) that it dominated the other drivers. Also, many of those other drivers, including interest rates and commodity prices, were acting to depress Asian growth at roughly the same time as the crisis struck. In fact, domestic demand in Asia began to soften *before* exports did in 2008.
- ▶ The issue of causality is also important. Interestingly, we can find no statistical evidence to support the widespread notion that US growth *leads* that in Asia. In reality, the causality increasingly looks to be working both ways; in other words, Asia and the emerging markets in general are now large enough to have a noticeable influence on developed world growth. We would also reiterate the point that all Asian economies (or at least part of them, in the case of Japan) recovered earlier and far more strongly last year than any western developed country.

To further investigate the issue and check these conclusions, we have deployed our own Asian growth model. By way of a reminder, the model is designed to explain year-on-year GDP growth on the basis of a number of factors, including real and nominal commercial bank interest rates, changes in fiscal policy, and oil price moves. We also include a weighted average of Asian equity markets (to capture both confidence and wealth effects) as well as exports.

First of all, it is important to note that exports do not dominate the show – other factors also play

statistically significant roles. Nevertheless, we decided to see what would happen if we replaced the export term with US and European import growth. The answer may be surprising to many: US imports were not significant while European demand was, with a 1% fall in the latter cutting 0.1% from Asian GDP growth. In reality, this makes some sense, as Europe is a bigger trading partner for many Asian countries than the States.

However, the failure of the US term to show up may be because total US imports are not that representative of what the States demands from Asia, thereby distorting the result. Conventional wisdom has it that consumer spending is the key factor, so we tried real US consumption in the equation instead. This did indeed turn out to be significant, knocking out the European import term and implying that a 1% fall in US consumer spending typically reduced Asian GDP growth 0.3% (personal consumption in the States was down 0.2% year-on-year in 3Q and 1.8% in 2Q).

Also, US/European developments may impact some of the other variables in the equation, potentially implying that we are still under-representing the aggregate effect. In particular, what happens to western world demand will influence Asian equity prices and capital flows.

But before tearing up the results of our previous analysis, there are several points to keep in mind:

- ▶ We have never argued that US/European developments do not matter for Asia, just that they are not the only determinant (there is a huge misperception about this in relation to the decoupling debate).
- ▶ Indeed, all the Asia-related variables we mentioned, including equity prices, remained in the equation as statistically significant drivers of GDP growth when the US consumption term was included. It is increasingly apparent that Asian economic

developments, particularly those in China, are becoming more important in driving the global equity markets.

- ▶ The US consumption term was contemporaneous; in other words, yet again, there was no evidence of a US lead.
- ▶ Ironically, negative western world growth developments might, *with a lag*, have some positive effects on the region. This is exactly what is happening right now as near-zero US interest rates help keep a lid on Asian rates. Oil prices are presumably lower than they would otherwise have been as well.

Overall, if the US/European economies were to double-dip or soften, contrary to our expectations, then the extent to which this drags down activity in the region will depend on how equities are impacted and what the other growth drivers are doing. The good news is that if the developed world slowdown occurs this year, then policy conditions should provide a powerful offset, as described below.

2. End of policy support and budget deficits

This brings us to the next risk – Asian growth could collapse when the positive effects of the extensive fiscal and monetary stimulus measures come to an end. It is an issue most often heard in relation to China, where the government has publicly stated that it wants to halve credit growth from 33% last year to 17% in 2010, edging up rates recently as a signal of its intent.

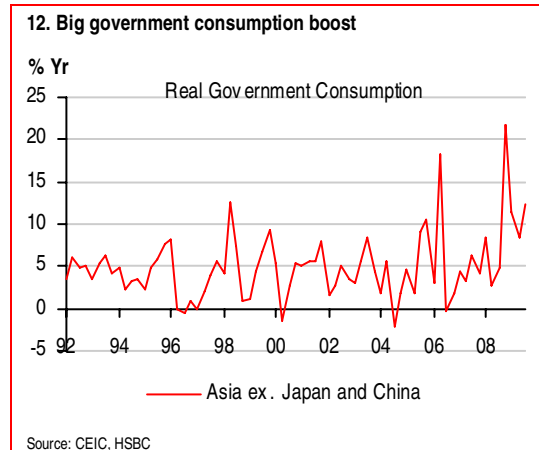
In the view of our China economist, Qu Hongbin, there is no reason to panic, and he is maintaining his 2010 GDP growth forecast of 9.5%. The following points help explain the reasons:

- ▶ While overall credit growth is targeted to slow, the government hopes to ensure that the money lent is used for productive purposes. In

particular, state banks will be encouraged not to lend to new infrastructure projects and other sectors where there is over-capacity.

- ▶ History suggests that 17% bank lending growth, if used well, is more than enough to sustain near double-digit GDP growth in the country.
- ▶ If weaker lending growth and other measures mean that a full-scale housing bubble (and subsequent bust) is more likely to be avoided, this should be considered good news, at least for the country's long-term growth prospects. It is a bit of a stretch for the pessimists to worry about a slowdown in lending growth on the one hand, but to point to the threat of a housing market collapse on the other.
- ▶ One of the government's top priorities is to boost consumer spending, making it a more important driver of economic growth in both the short and the long term. Consequently, the authorities will continue to provide income support and subsidies to the poor, while spending more on health, education and public housing to reduce the need for precautionary savings (see *China's New Deal II: Unleashing consumer power*, 4 January 2010).

Outside China, it is true that plenty of interest rate cuts and fiscal easing measures were introduced by the policy authorities of the different countries at the end of 2008 and in early 2009 (see chart 12, for example), which have not been added to recently. However, it is often forgotten that policy works with a long lag. Our analysis, and that of others, suggests that it take 12-24 months for rate cuts and some fiscal measures to take full effect, meaning that 2010 GDP will receive significant benefits from the earlier policy actions.



The year 2011 could prove to be a very different story, particularly if policy is tightened significantly during the course of this year. But, as the next chapter describes, a rapid unwinding of the policy support seems most unlikely while, if we are right, the region has already embarked on a virtuous circle of growth that is independent of policy stimulus.

A potentially important adverse consequence of all the budgetary support provided by governments is the ensuing rise in budget deficits. Take Japan, for example, where countless fiscal packages have been introduced over the years and yet the economy continues to struggle badly, still unable to stand on its own two feet 20 years after the bubble burst.

The problem here is not that all the extra spending/tax reductions have led to higher bond yields, in turn "crowding out" private investment and consumer spending, but rather that there has been no private demand to crowd out in the first place. This was initially because companies and households were anxious to pay down their own debts, while now it reflects worries about the level of government debt (close to 250% of GDP). The fear is that taxes will have to be raised and public spending cut significantly in the future, and this fear is encouraging private savings and discouraging private investment.

Japan's experience in this area represents an important lesson for all countries, but much more for developed countries in the West than for the less developed countries in the east. In addition to still having huge catch-up potential and favourable demographics, most Asian countries are generally in much better fiscal shape. Table 13 shows our estimates of government deficits and debts in 2009 for a range of different countries.

The key exception in Asia is India, where new structural fiscal measures introduced to support the poor, while welcome, have yet to be financed (see *India Economics: The road to recovery and beyond*, 29 April 2009, by Robert Prior-Wandesforde). It is vital that the funding for these measures should come sooner rather than later (through cuts in bureaucracy and an extension of the tax base, for example). Our long-held fear is that the government will instead choose to control the deficit by continuing to underspend on infrastructure.

13. Asia (ex. Japan) fiscal position not too bad – 2009 data

	Budget balance (% GDP)	Gov. debt (% GDP)
Japan	-10.5	245
China	-2.9	17
India*	-11.0	80
Korea	-2.4	33
Taiwan	-4.8	35
Indonesia	-2.4	42
Thailand	-5.3	52
Hong Kong	-3.9	n/a
Malaysia	-8.5	58
Singapore	-2.5	n/a
Philippines	-4.0	58
US	-9.9	85
Eurozone	-7.1	85
UK	-11.5	55

Source: HSBC. * Fiscal year 2009/10 including State deficits

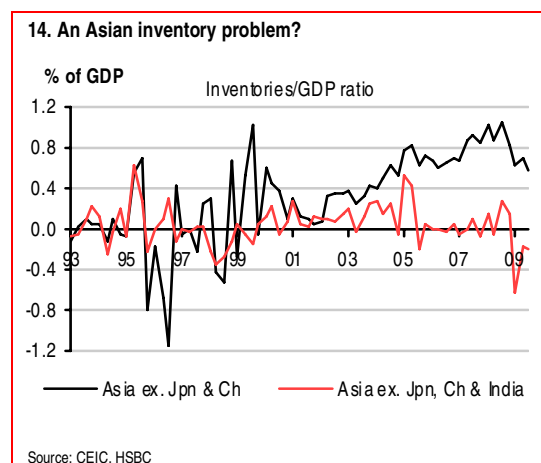
3. Inventory-led growth

One commonly held misperception about the global and Asian economic recovery is that it has been led by a rebuilding of inventories rather than an improvement in final domestic demand (consumer spending and investment).

This is very easy to dismiss, however. In the case of Asia, as we saw earlier, private consumption and investment have improved sharply, although admittedly the improvement in the latter partly reflects higher government capital expenditure (unfortunately we do not have the data to know exactly how much).

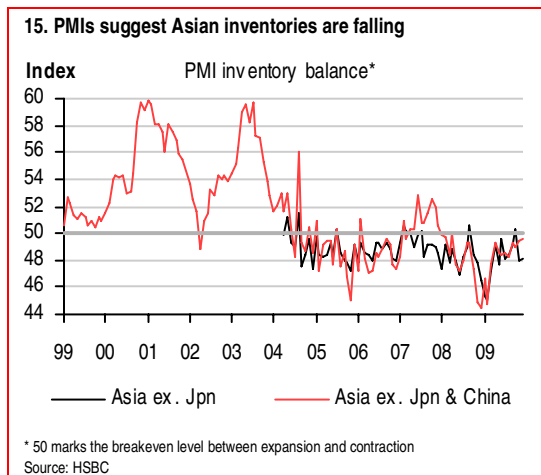
It should also be stressed that neither capacity utilisation (which is quite low) nor bank lending growth (which continues to soften outside China) have been good lead indicators of investment growth in the past.

As for what is happening to inventories themselves, we have presented seasonally adjusted inventory changes as a percentage of GDP in chart 14 (again having to exclude China, as such numbers are not published there).



Looking at the black line, one might be forgiven for being a little concerned. However, the apparent structural increase in the ratio since 2000 reflects developments in just one country – India. As we mentioned earlier, the expenditure breakdown of Indian GDP needs to be taken with a large pinch of salt. If the India numbers are stripped out, as we have done in the red line, then the picture is very different – in fact, there looks to have been destocking through 2009. The same is also true of the US and most European countries.

Our conclusion is supported by chart 15, which shows the inventory component of the Asian PMIs (or similar measures). The black line, which includes China, has risen from the lows of early 2009 but is still consistent with falling rather than rising stocks.



Although less destocking is, in itself, good news for economic growth, and may partly explain the improvement in Asian industrial production, it looks very much as though inventories are still some way from actually rising (particularly in the US).

4. Exchange rate effects

Another concern expressed by some relates to the strength of the Asian currencies, which re-started when risk sentiment turned decisively from March last year. With the Chinese also effectively re-pegging the renminbi against the weak US dollar, the rest of Asia has, so the argument runs, suffered a huge competitive loss, crushing any hopes of an export recovery.

Again, such fears seem overdone. Table 16 shows the year-on-year move in the real effective exchange rate (REER) for the main Asian countries, as well as the difference between the current level of the REER and its long-term average (calculated from 1994). The REER numbers come from the Bank for International Settlements and are derived by weighting up (using trade weights) the change in each country's currency against a basket of other

currencies while adjusting for relative consumer price moves. We have also included in the table the export share in GDP as a means of judging the importance of exports in each of the economies.

Only Indonesia and Korea have seen significant rises in their REER in the year to November (the latest available data) while Indonesia, China and the Philippines are the only countries where the level of the exchange rate is above the 15-year average. The China result might seem surprising but reflects the fact that the renminbi appreciated significantly from 2004 to mid-2008. It should be stressed that this does not necessarily mean China's currency is overvalued right now.

16. Is the exchange rate a problem?

	% y-o-y change in REER*	% diff. from LT avg in REER**	Exports as % of GDP
Japan	-2	-8	13
China	-8	11	Approx 30
India	1	-2	20
Korea	15	-14	45
Taiwan	-6	-18	63
Indonesia	17	6	43
Thailand	-1	-14	65
Hong Kong	-6	-20	194
Malaysia	-4	-8	107
Singapore	-1	-1	234
Philippines	0	3	41
Av. excl. Jpn	-2	2.1	45

* Real Effective Exchange Rate based on CPI. **Average since January 1994
Source: CEIC, Bank for International Settlements, HSBC

There are four other, more general, points to make:

- ▶ As we showed earlier in chart 7, Asian exports have already begun to improve.
- ▶ Our analysis over the years on the impact of currency moves on exports relative to changes in Global demand have always suggested that the latter is far more important. As a rough rule of thumb, we estimate that for a 1% change in both variables, Global demand has four times the impact on exports.
- ▶ All major Asian countries have been intervening in the foreign exchange markets over much of

the last nine months to limit appreciation or, in the case of China, to prevent their currency from appreciating against the US dollar. In most cases, the central bank is not always completely effective at mopping up the resulting rise in liquidity, some of which seeps into the real economy, boosting demand.

- ▶ The rise in the Asian currencies against the US dollar had led many governments to provide fiscal support to their export industries. It also helps explain the caution among central banks in raising interest rates.
- ▶ A widespread belief that Asian currencies represent a one-way play against the US dollar has encouraged dollar-denominated capital outflows into the region, which again has supported activity/asset markets.

5. Asset bubbles and busts

Talking of asset markets this brings us on to our final risk – that of bubbles and subsequent busts. We have written a lot about this in recent times (see, for example, Frederic Neumann, *Blowing bubbles: Money's too loose in Asia*, 15 July 2009 and his *Asian Economics Comment: Anatomy of bubbles, parts One, Two and Three*, August and September 2009) arguing that, while the conditions for asset bubbles, such as exceptionally low interest rates and sizeable capital inflows, are very much in place in Asia, there is little to suggest that bubbles have actually formed, at least not yet.

Several misperceptions surround the issue at present: In particular, the fact that asset prices have jumped sharply in many Asian countries since early last year does not necessarily mean that bubbles (defined as asset values hugely above what is justified by fundamentals) exist.

Take equities, for example. Many argue that, because some indices have doubled from their lows, and all are up sharply since March, markets must therefore have entered a period of, to use a

worn-out phrase, “irrational exuberance”.

However, our equity strategists have made a couple of interesting points in this context. First valuations are not particularly stretched at present, while some of those valuations are based on analysts’ earnings expectations that are ultra-conservative relative to post-recessionary periods in the past. If history is any guide, consensus profit numbers may not be 2 or 3 percentage points too low but 20-30 percentage points below the eventual outcome.

It is also noteworthy, that, with the exception of China, leverage has yet to contribute to the rise in asset values. Past bubbles have always been associated with a period of rapid credit expansion.

To our minds, the more important question to address is, Can the policy authorities prevent asset bubbles from developing this time, and will they? As listed in table 17, several Asian governments and central banks have taken steps to try and temper rapid asset price moves. Arguably these have come earlier than has normally been the case, perhaps because the authorities are trying to learn from the perceived mistakes of the US. It is also interesting to note that they have not hiked interest rates so far but preferred to implement more targeted measures.

17. Asia measures to tackle foreign inflows/asset prices

Korea (Sep)	Higher taxes on ownership of multiple properties
Singapore (Sep)	Increase in land supply and restrictions on interest only loans
Taiwan (Oct)	Restrictions on foreign inflows into time deposits
Hong Kong (Oct)	Intro. of “best practice” guidelines for mortgage lending and cut in LVR* on luxury property
India (Oct)	Increase in provisioning requirement for bank lending to commercial real estate companies
Malaysia (Oct)	5% tax on property gains
China (Jan)	Increased “monitoring” of property loans

*Loan-to-value ratio
Source: HSBC

It is too early to fully judge their effectiveness, although the initial signs are mixed. Arguably, Korea has met with the most success as the property market has clearly cooled there.

However, the same cannot be said of Singapore, as private residential property prices leapt a further 8% in the fourth quarter from the third, after a nearly 16% rise in 3Q, while Housing Development Board (HDB) flat resale prices rose another 4% to a new all-time high. Money also continues to flow rapidly into Taiwan.

With the problems of the US fresh in the minds of policymakers, one can make the argument that they will continue to deal with escalating asset prices earlier and more aggressively this time. But, if risk aversion and interest rates remain low, we are sceptical about their eventual success.

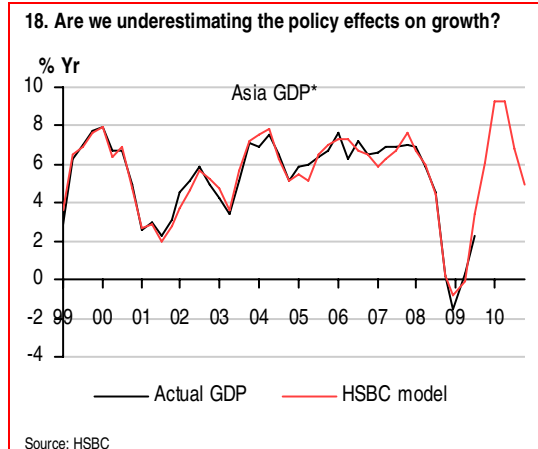
In our view, the bursting of asset bubbles is the biggest of the downside risks to growth we have considered in this chapter, albeit one that is perhaps two or three years away.

Upside risks as well

In view of the fact that we still expect most to be surprised by the strength of the Asian recovery, we have focused here on the downside risks to Asian growth. But this is not to say that all the risks are negative. In particular, inventories could bounce back aggressively, while strength of western world growth could surprise on the upside.

Also, judging precisely the impact of policy moves is generally very difficult, but particularly so when the size of the policy reaction is unprecedented, as it was in late 2008/early 2009.

For what it is worth, our growth equation suggests that we are underestimating the positive impact of the fiscal and monetary action taken in the region (as well as the scale of the growth correction in the second half of 2010). According to the model, Asia ex. Japan and China growth will average 7.5% in 2010, compared with our 6.1% published forecast.



Risks and rewards

2010 is undoubtedly a year of high risks but, then again, when is the outlook ever risk free? The year will also deliver high rewards in terms of economic activity. Unless, of course, inflation explodes.

The return of inflation?

- ▶ Rising commodity prices may spark another jump in headline CPI readings over the coming year, followed by a perk-up in core
- ▶ Already, companies are reporting soaring input and output prices and wage pressures are likely to rebound after slowing in 2009
- ▶ With perceived growth uncertainties still looming large and central banks under political pressure, the rate response may be delayed

Been here before

It's been a tough couple of years for Asia. Inflation alone tells the tale: first, prices started to spiral up, as everything from the price of pork to gasoline touched all time highs; then, with economic collapse, price pressures disappeared and a number of markets even flirted with deflation. Now, after the ship has stabilized, so have inflation readings. But, a nagging feeling lingers that something is cooking again. Price pressures are bubbling up once more, and it feels a bit like early 2008. Investors better pay attention.

Let's do a quick run through the latest inflation trends. For the region overall, inflation is currently in an acceptable range. As our first chart shows, inflation has only ticked up in annual terms. But, sequentially, the picture is more worrying. This, in itself, is not reason enough to ring the bell. In fact, it may be seen, in the first instance, as a welcome reassurance that Asia is not succumbing to protracted deflation. Asian officials, after all, are quite familiar with Japan's battle against falling prices over the past decade, something that no-one wants to see repeated elsewhere.

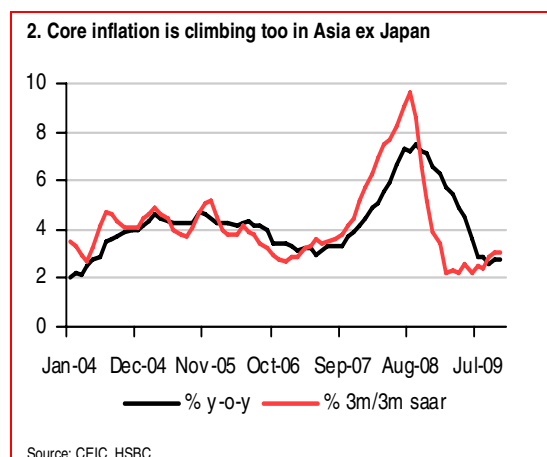
But, there is no room for complacency. Inflation remains a real risk for Asia, even if the global

economy may not quite fire at full throttle over this year and next. Already, signs are popping up all over the region that price pressures are gaining momentum. Take, for example, food. In places like India and Vietnam, the cost of staples such as rice has surged in recent months. Even in China, which has enjoyed a relatively good harvest over the past year and maintains ample stocks, food prices have risen 11.8% 3m/3m saar in November.



But, the issue is larger than food, or even headline, price pressures. The core components of national CPI measures have also started to climb, even if less impressively than the headline index. Remarkably, for the region as a whole, although

excluding Japan, core inflation never turned negative over the past year, even in sequential terms, despite the dramatic collapse in output over the latter half of 2008 and early 2009.



This matters for monetary policy. To be sure, policy-makers tend to shrug off a spike in the headline index if this is triggered by a supply shock, such as geopolitical events or natural disasters. Moreover, a shift in relative prices, like a structural rise in oil prices against the cost of manufacturing goods, does not warrant a monetary policy response. However, what does matter is a rise in the general price level. Thus, if higher food or energy prices begin to push up core inflation, or if core rises for other reasons, monetary policy needs to be tightened.

Over the next several sections, we address the key issues pertaining to inflation risks over the coming year. Firstly, how much evidence is there of building price pressures at the moment? Secondly, what's the risk of inflation rising more briskly over the coming year than currently anticipated? Lastly, what are the implications for monetary policy and investors?

Before delving into these issues, however, we need to emphasize that the discussion is confined to Asia ex Japan. The situation in Japan differs considerably from that found elsewhere in the region. Here, CPI measures are stuck in deeply negative territory, and this is expected to remain the case for the coming year. For example, our Chief Japan economist, Seiji Shiraishi, recently pointed out that service deflation, a key component of the core measure, continues to register record declines both in magnitude and duration (see *Japan Economic Topics: Service prices falling at record rate and duration* 7 January). For 2010, he expects the overall price level to decline 1.2%, after a 1.5% drop last year.

Something's cooking

More than in other regions, commodity prices matter greatly for inflation in Asia. In fact, in most of the region, core readings have traditionally been well behaved, reflecting the relatively gradual ascent of wages over time, healthy competition among manufacturers and domestic service firms, as well as an array of price controls and subsidies. In addition, and unlike more advanced economies, food and energy comprise a fairly large share of local CPI baskets.

Let's start with food. Across the region, the cost of staples has started to rise, reflecting either disruptions in local food production or simply the cumulative effect of soaring consumption. In India, the lack of monsoon rains has led to a sharp decline in agricultural output, with the price effect being felt in farmers' markets across the country. In the Philippines, meanwhile, the recent typhoons have also disrupted food production, with the

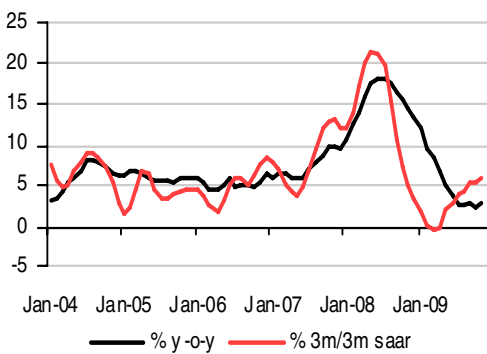
3. Latest core and headline CPI readings in Asia (annual % y-o-y, and sequential % 3m/3m saar)

	CH	HK	IN	ID	JP	SK	MY	PK	PH	SG	SL	TW	TH	VN
CPI ann	0.6	0.5	13.5	2.8	-1.9	2.8	-0.1	10.5	4.4	-0.2	2.8	-1.6	1.9	4.0
CPI % seq	5.2	4.3	3.7	5.2	-1.6	3.0	2.3	13.5	7.8	2.2	7.1	-0.3	5.3	10.5
Core CPI ann	-0.6	0.4	5.9	4.4	-1.0	2.2	1.6	11.9	2.7	-1.4	5.9	-0.7	0.0	7.4
Core CPI seq	2.6	0.4	5.3	5.4	-1.1	2.4	1.0	9.7	5.7	2.0	3.2	0.9	0.8	7.8

Source: CEIC, HSBC

impact likely to be felt well beyond one planting season. Here, food prices have started to rise too, and the government, worried about supply next year, has purchased already vast quantities of rice on the international market, which is one reason for the global price spike of the cereal last year.

4. Food prices up sequentially in Asia ex Japan (CPI basis)



Source: CEIC, HSBC

Food prices in the region appear to have become more sensitive to such supply disruptions. This, most likely, reflects the rapid growth of incomes, which, in turn, raises calorific intake and boosts demand for animal proteins, especially beef and pork. As a result, demand for agricultural products puts strain on the supply chain, rendering the system more vulnerable to temporary shocks, such as droughts or floods. But, even in countries so far spared major production bottlenecks, like China over the past year, food prices have started to rise again strongly along with rebounding incomes.

With oil topping USD 80bn at the start of this year, the upside risks for regional CPI readings are only all too evident. A recurrence of 2008, when crude touched almost USD 150bn, still seems unlikely, with most of the world stuck in low gear, especially some of the big Western consumers. We certainly do not want to engage in bold predictions to what lofty levels benchmarks may soar this year. But, it is worth spelling out risks involved, and to tackle the notion that oil could not top USD100bn or push even higher, as long as

advanced economies are showing signs of only muted growth.

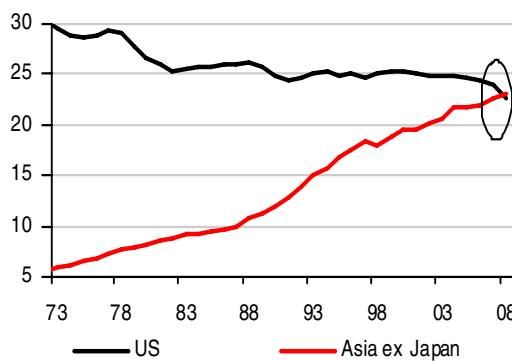
5. Food and energy weights in regional CPI baskets (%)

	Food	Energy
China	33.0	5.0
HK SAR	26.9	3.6
India	60.2	14.2
Indonesia	45.3	15.2
Japan	25.9	7.4
Korea	15.9	5.9
Malaysia	31.4	13.8
Pakistan	40.3	7.3
Philippines	46.6	13.6
Singapore	23.4	5.3
Sri Lanka	46.7	N/A
Taiwan	25.1	3.7
Thailand	36.1	9.7
Vietnam	42.7	n/a
Asia ex J average	36.4	8.8

Source: National authorities, HSBC; NB: for Asia ex Japan simple average

The reason for this is the structural shift in global oil demand. Whereas the West accounted for the bulk of global consumption only two decades ago, emerging economies, and especially Asia, have rapidly raised their share. In 2008, for the first time, Asia ex Japan devoured more oil than the US, long the dominant consumer of crude in the world. This year and next, we expect the gap to widen sharply, with the region now becoming the most important driver of global oil demand, and thus prices.

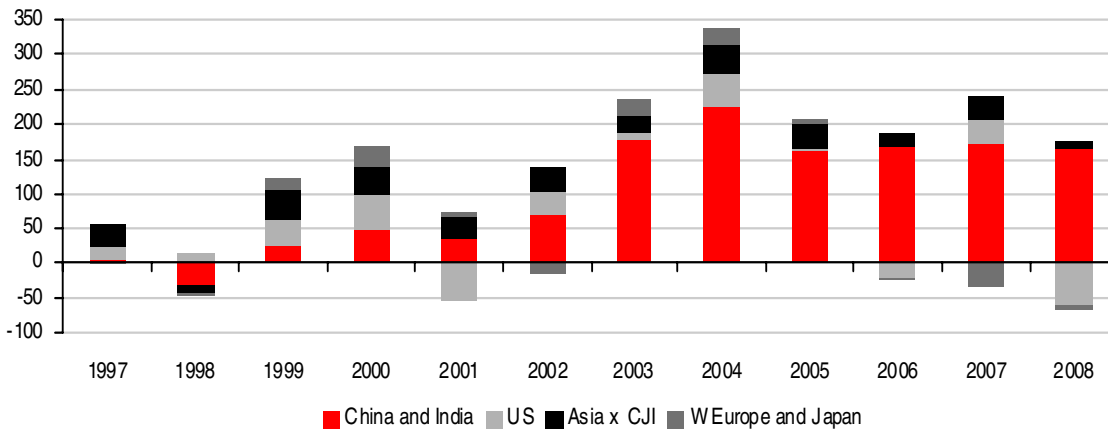
6. Global share of oil consumption (%)



Source: BP, HSBC

Even as demand for energy in advanced economies dwindled, the marginal increase in consumption in Asia more than compensated for

7. Annual change in primary energy demand (millions of metric tons)



Source: BP, HSBC

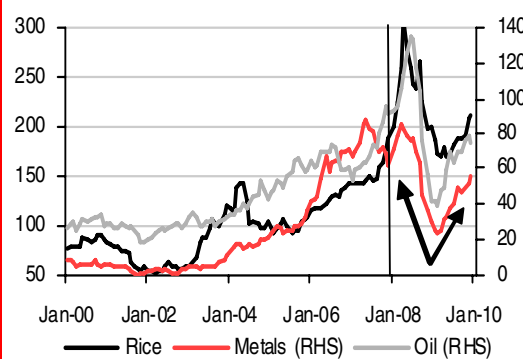
the loss elsewhere. In 2008, for example, the last year for which comprehensive data is currently available, the incremental increase in primary energy demand in China and India was over 160 million metric tons, easily making up for the 60 million ton loss in the US (Europe and Japan were down about 5 million tons).

Simply looking at the last decade, the impact of emerging Asia becomes even more visible. From 1997 to 2002, the region's marginal demand increase for primary energy was about 150 million metric tons, whereas in the period from 2003 to 2008, incremental demand jumped to 1,070 million tons.¹ With growth recovering swiftly in Asia, and the economies themselves being larger from year to year, the region may well cause another spike in energy prices, especially if demand in the West begins to recover gradually.

Another issue to consider is the impact of liquidity on commodity markets. There is, to be sure, a long-running debate, whether the spike in the price of traded commodities, such as oil, soybeans, or a number of base metals, in recent years was due to

the inflow of speculative capital into these markets or simply a reflection of global demand outstripping the world's supply capacity. The debate still appears unsettled, although we suspect an element of truth in both of these explanations. Therefore, to the extent that low interest rates and excess liquidity can drive up commodity prices, the risk evidently remains of another price spike this year given current global financial conditions.

8. Commodities up in early 2008 and now (index 2005 = 100)



Source: CEIC, IMF, HSBC

Taken together, there are evident parallels between the beginning of this year and early 2008, the year when a super-spike in global commodity prices led to a blow-out of inflation across Asia and many other emerging markets. First, growth in Asia looks set to accelerate further over the first half of

¹ Primary energy includes coal, gas, oil, hydro and nuclear power. Given that the West generates far more nuclear power than emerging Asia, the relative incremental demand impact of the region in fossil fuels is likely to be even bigger.

2010, approaching in sequential terms the red-hot pace last seen before the global financial crisis.

Second, global financial conditions remain extremely loose, with low interest rates and excess liquidity, at least in certain parts of the world, possibly injecting another speculative element into the market for raw materials. Third, we are entering the year with commodity markets already feeling perky, with upward momentum possibly proving sustained if economic data continues to surprise on the upside over the coming months.

To the core

But, there are even more signs that inflation may become a more pervasive challenge over the course of this year and beyond: not only are commodity markets coming under pressure, pushing up headline readings, but core inflation, arguably of equal, if not greater, concern to policy-makers, may be rearing its head as well. Coming so rapidly on the back of economic collapse, this is certainly a surprise. But, at heart, this suggests a structural change in the behaviour of inflation in Asia, with output gaps being narrower than previously thought and excess labour no longer as abundant as before to keep a lid on wage and production costs.

For example, our proprietary Asian Business Index (ABI), a composite of regional PMI and business surveys, points to soaring input and output costs

across the region. Input prices, of course, are in large part driven by raw material prices and so the recent run-up in this sub-component is not entirely surprising. However, our output price index is rising sharply as well, and this particular series is well correlated with core price inflation in most Asian economies. Sequentially, therefore, core CPIs are likely to accelerate further.

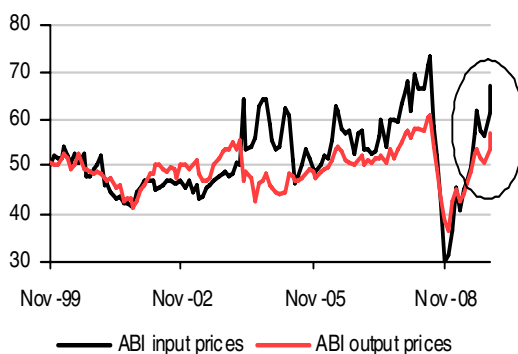
10. PMI surveys point to rising price pressures (December 2009)

	Output	Input
Australia	n.a.	60.5
China HSBC	60.9	69.9
Hong Kong	53.4	60.8
India	52.6	58.9
Japan	42.4	49.9
Korea	49.6	54.8
Singapore	n.a.	49.5
Taiwan	54.1	72.9

Source: Markit, HSBC

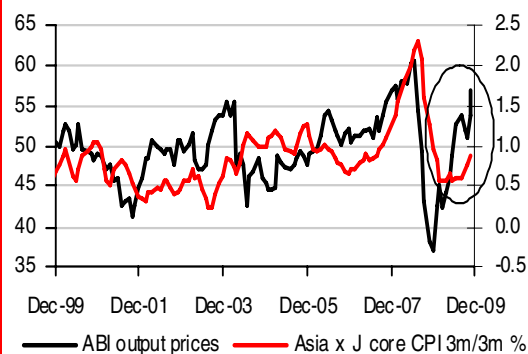
Apart from a jump in commodity prices, the recent bounce in reported input prices may also reflect rising wage costs. In the wake of the financial crisis, labour markets in the region surprised in their resilience, with large-scale layoffs, as seen in the West, being largely avoided, even though the overall decline in industrial output was much sharper than in advanced economies. At the time, we had termed this phenomenon “Asia’s labour market riddle” and attributed it to the relatively strong cash flow position of firms in the region and the health of banks, which continued to supply loans.

11. Businesses are reporting soaring input and output prices



Source: CEIC, Markit, HSBC

12. Higher output prices to push up core inflation further



Source: CEIC, Markit, HSBC

But, there is also another explanation that recent data releases have unveiled: wage costs in Asia fell precipitously in the wake of the crisis, helping employers to avoid lay-offs. This suggests that the region's job markets are inherently more flexible than those found in many advanced economies. But, while this may have helped the region to cushion the blow from the financial crisis, it may now pose a new challenge. After all, downwardly flexible wages also imply that salaries can go up rapidly if labour demand rebounds. As late as the third quarter, as our table shows, wage growth was deeply negative.

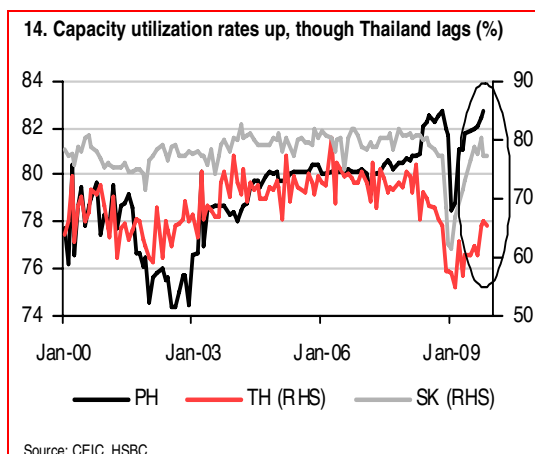
13. Falling wages helped cushion the blow (3Q, 2009, % y-o-y)

	nominal	real
China	1.0	1.9
Hong Kong	-11.7	-11.6
India*	9.2	1.2
Indonesia	5.4	-6.3
Japan	-5.9	-3.7
Korea	-1.4	-3.4
Malaysia	-2.1	0.1
Philippines**	6.0	-0.9
Singapore	-2.5	-1.9
Taiwan	-7.9	-6.6
Thailand	-0.9	0.9

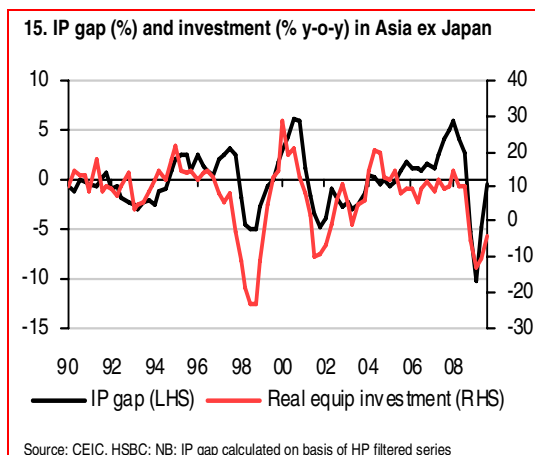
Source: ILO, CEIC, national authorities, HSBC

However, anecdotal reports suggest that this has quickly changed into year-end, with reports of Taiwanese tech firms, for example, bringing forward their New Year bonuses to retain staff, and Chinese firms in southern regions complaining about labour shortages. These bottlenecks, therefore, point to another risk, that rising PMI input price components already imply: wages are rising again rapidly in the region, which may eventually show up in bouncy core prices as well.

Worries at the depth of the financial crisis that Asia may have to grapple with excess capacity for years to come have not been substantiated. To be sure, most economies do not provide a reliable series of capacity utilization. But, where available, they have shown a rapid narrowing of the output gap over the past year, suggesting that price pressures, at least for industrial goods, may return quite rapidly.



Given the lack of reliable capacity utilization series in other economies in Asia, we compiled a monthly IP gap series, which measures the deviation of factory output from its long-run trend. This series, while admittedly only a rough indicator of spare capacity, has a reliable long-term relationship with investment spending on facilities and equipment, suggesting that it is at least a useful proxy.



For Asia as a whole, our IP gap has now turned slightly positive, which implies not only that investment spending needs to rise over the coming quarters, but also that price pressures could develop rapidly if this is not forthcoming. By this measure, only Indonesia, Malaysia, Singapore, Pakistan, and Sri Lanka still have spare capacity available, while in other markets the gap is already positive.

16. HSBC estimated industrial production gap (%)

	CH	IN	ID	KR	MY	PK	PH	SG	LK	TW	TH	VN
Latest	2.2	0.5	-0.4	0.7	-0.3	-6.6	2.9	-6.6	-0.9	4.6	1.6	2.1
Dec-08	-1.9	-2.9	0.2	-10.0	-4.5	-2.5	-0.7	-6.6	0.6	-15.9	-4.8	-2.7

Source: CEIC, HSBC

To provide a little more rigor on the matter, we estimated simple polynomial lag models. These help to illuminate the drivers of core inflation in the region, and provide a sense of their relative importance in various countries. The table below, shows in the second column the percentage point pass-through on core CPI (measured in sequential, three months terms) of a one percentage point narrowing of the output gap. The third column provides an estimate of the duration it takes before the impact is fully felt (expressed in quarters).

The biggest pass-through on core inflation occurs in Vietnam and Indonesia, although in China and Korea the effect is also quite prominent. However, in Indonesia, Korea, and Hong Kong, it takes some 5 to 6 quarters before the effect fully comes through. In China, meanwhile, it takes only 6 months before changes in the output gap impact core inflation, a relatively rapid pass-through, especially given the relative magnitude of the effect in the country. On the other end of the spectrum, in Taiwan, Malaysia, and Thailand the pass-through is

relatively small, while in the Philippines it is virtually no-existent.

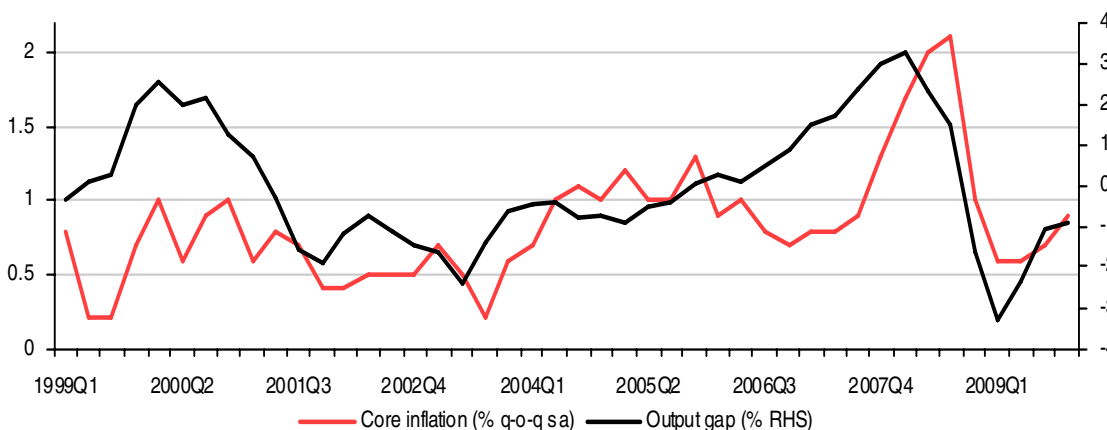
18. Pass-through of changes in the output gap on core inflation

	ppt pass-through	lag time
China	0.25	2
Hong Kong	0.15	6
India	0.16	5
Indonesia	0.36	6
Korea	0.28	5
Malaysia	0.04	2
Philippines	-0.01	4
Singapore	0.15	1
Taiwan	0.08	2
Thailand	0.14	2
Vietnam	0.42	4
Asia ex Japan	0.15	1

Source: HSBC; NB: simple average for Asia ex Japan

So far, the discussion has highlighted the risk of rising commodity prices in 2010, with evident implications for headline inflation in the coming quarter, especially in a region so sensitive to the cost of raw materials. Moreover, we have shown that price pressures are even beginning to emerge in the core segment of the CPI, which may be of arguably even greater concern to policy-makers

17. Output gap and sequential core inflation in Asia ex Japan



Source: CEIC, HSBC

than a temporary spike in non-core components. Taken together, inflation remains a real risk in Asia, even if readings so far remain benign.

Who's sensitive?

Rising inflationary pressures raise the risk that monetary policy may have to be tightened in Asia earlier than currently anticipated, a realization that may well come to rattle policy-makers and financial markets alike, especially if after a long spell of accommodation, interest rates suddenly need to be raised in quick succession. This, certainly, is not our base case, but it is worth spelling out some of the risks around this scenario.

Since we have drawn extensive parallels between the situation currently and early 2008, when inflation started its deafening ascent, consider the monetary policy debate at the time. Back then, officials initially resisted tightening monetary policy arguing that rising commodity prices amounted to a supply shock that didn't warrant a hike in rates. Only belatedly was policy tightened, but then so decisively that it pushed domestic demand into a recession, rendering the region vulnerable to the subsequent collapse in exports.

The debate in essence boiled down to the risk of second-round effects that rising non-core items would have on core. In the event, the debate was short-circuited by the global economic collapse.

But, we present evidence here about the behaviour of core inflation in various Asian markets in response to changes in non-core items, specifically food and energy costs. Our approach helps to map out national sensitivities to second-round effects and, by extension, should provide some clue to the interest rate response of national authorities should commodity prices rise.

Table 19 provides the results from our regression model introduced above, this time with core CPI regressed on the food and energy components of the local price index. Surprisingly, food prices tend to have bigger second round effects than energy costs. This, presumably, is due to the fact that a rise in the price of oil eventually curtails economic growth. Especially among energy importers, which virtually all countries in Asia are, with the exception of Malaysia, a rising import bill will eventually reduce domestic spending and, therefore, the pass-through onto core. With food, however, the story is different: when prices rise, this amounts in most economies to a redistribution of income from urban to rural areas, rather than leakage of income to foreign exporters, leaving aggregate demand largely unaffected.

The pass-through of rising food costs is especially pronounced in Singapore, Hong Kong, and India, while in the Philippines and Indonesia, the effect

19. The pass-through of food prices on to core inflation generally outweighs the effect of energy costs

	Energy		Food	
	ppt pass through	lag time (months)	ppt pass through	lag time (months)
China	-0.30	7	0.12	3
HK	-0.04	1	0.59	2
India	-0.04	5	0.23	6
Indonesia	-0.04	6	-0.37	9
Korea	0.03	4	0.08	1
Malaysia	0.01	6	0.11	3
Philippines	0.31	5	0.03	10
Singapore	0.15	3	0.62	8
Taiwan	0.05	6	0.25	1
Thailand	0.05	6	0.09	6
Vietnam	0.22	5	0.22	6
Asia x Japan	0.10	3	0.11	3

Source: HSBC; NB: estimated ppt change in 3m sequential inflation in response to a 1% (3m sequential) rise in the food or energy component of the CPI

is, surprisingly, low or even negative. As for energy costs, core inflation in Vietnam and the Philippines is especially sensitive, although the relationship is negative for China, Hong Kong, India, and Indonesia.

Taking a step back, there is growing evidence that the underlying performance of inflation has changed over the years in Asia, consistent with the notion that output gaps are beginning to narrow not just in a cyclical, but also in a structural sense. Since about 2005, core inflation has started to react more sensitively to changes in the headline rate.

Possible explanations for this include the gradual dissipation of excess labour as economies develop, especially in China, and growing pricing power among firms as the region produces increasingly sophisticated goods. Second- round effects, in short, have become more prevalent over time. This shift has important implications for monetary policy: as core responds more sensitively to changes in headline inflation, central banks will have to take a more pro-active stance when it comes to changes in food and energy prices.

The below table presents simple correlation coefficients between headline and core inflation,

with readings above 50 marked in red. Evidently, the association between core and headline inflation has risen in the period of 2005 to 2009 compared to the previous five years. Technically, this suggests that while core inflation was the statistical “attractor” of headline inflation in the past, as it should be, the relationship has now reversed, something which raises questions about the suitability of current core measures for a guide to monetary policy, since the it should in theory present an unbiased average of headline inflation over time, but has lately clearly become unrepresentative of broader inflation trends (for more details, see for example, [Thailand Economics: Headline attraction: why low core inflation is misleading](#), 29 April 2008).

But will they act?

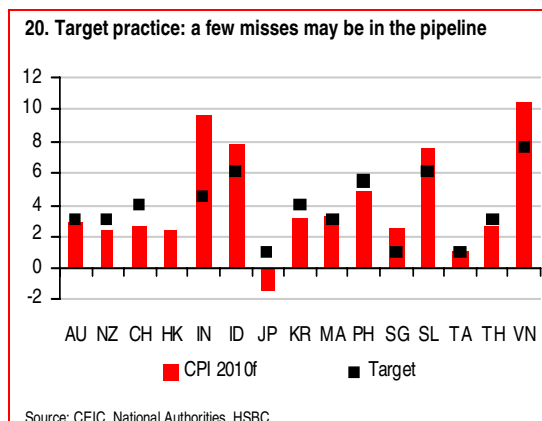
The upside risks to inflation, both core and headline, outlined above are not our base case. Based on our relatively conservative view of energy prices (assuming USD 70/bbl on average for 2010) and the assumption of reasonably well behaved food prices, we do not anticipate inflation to breach the official or implicit inflation target in most of the larger Asian markets. The only economies where inflation may top the comfort zone for this year are India, Indonesia, Singapore, Sri Lanka, and Vietnam.

20. Core starting to react more sensitively to changes in headline inflation (correlations coefficients, above 0.5 marked in red)

	CH	HK	IN	ID	JP	SK	MY	PK	PH	SG	SL	TW	TH	VN	Asia S	Asia W
2000-2004																
current	0.22	0.91	0.28	0.79	0.25	0.66	0.71	0.66	0.89	0.85	0.56	0.28	0.19	0.52	0.72	0.17
1 lag	0.20	0.75	0.37	0.67	0.29	0.61	0.65	0.62	0.85	0.78	0.51	-0.03	0.21	0.47	0.68	0.16
2 lag	0.16	0.43	0.44	0.49	0.31	0.45	0.53	0.60	0.71	0.61	0.48	-0.13	0.20	0.40	0.56	0.13
3 lag	0.17	0.08	0.41	0.38	0.34	0.31	0.35	0.61	0.52	0.43	0.42	-0.17	0.20	0.34	0.40	0.13
4 lag	0.23	-0.10	0.34	0.36	0.42	0.21	0.18	0.60	0.36	0.30	0.04	0.11	0.17	0.32	0.22	0.14
5 lag	0.27	-0.15	0.22	0.39	0.49	0.09	-0.05	0.52	0.24	0.20	-0.39	0.25	0.09	0.33	0.06	0.10
6 lag	0.25	-0.08	0.08	0.42	0.50	-0.05	-0.27	0.40	0.16	0.13	-0.34	0.40	0.00	0.35	-0.03	-0.01
2005-2009																
current	0.65	0.69	0.63	0.93	0.76	0.60	0.09	0.65	0.90	0.91	0.33	0.71	0.75	0.92	0.83	0.67
1 lag	0.67	0.47	0.64	0.83	0.78	0.59	0.25	0.70	0.90	0.89	0.44	0.71	0.62	0.89	0.89	0.73
2 lag	0.69	0.20	0.58	0.56	0.78	0.57	0.34	0.74	0.77	0.82	0.52	0.62	0.42	0.80	0.88	0.74
3 lag	0.70	-0.05	0.53	0.29	0.75	0.55	0.33	0.75	0.56	0.71	0.59	0.45	0.27	0.67	0.81	0.72
4 lag	0.70	-0.06	0.48	0.14	0.69	0.57	0.24	0.75	0.32	0.63	0.62	0.28	0.26	0.49	0.70	0.67
5 lag	0.64	-0.02	0.43	0.09	0.61	0.59	0.16	0.73	0.11	0.55	0.58	0.14	0.32	0.30	0.57	0.57
6 lag	0.52	0.03	0.38	0.07	0.51	0.57	0.13	0.69	-0.05	0.48	0.49	0.03	0.38	0.11	0.44	0.44

Source: HSBC; NB: Asia S refers to Asia ex Japan simple average, Asia W refers to Asia ex Japan GDP weighted average

But, if commodity prices should continue their recent run, and output gaps close more rapidly than currently forecast, a number of markets may quickly face escalating inflation. Most at risk, all considered, are Vietnam, India, Sri Lanka, and Indonesia, although we have also flagged the possibility of growing price pressures in Hong Kong, the Philippines, and Korea. Notably absent from the list, so far, is China, where our Chief China economist, Qu Hongbin, does not see consumer price inflation as a near-term risk, not least because of ample food stocks, price controls, and the possibility of gradual appreciation over the second half of the year, which should help temper import costs and help redirect export capacity to meet domestic demand.



More generally, even if inflation surprises on the upside, it is not clear whether policy-makers will react promptly with rate hikes. After all, in 2008, the tightening response was repeatedly delayed until more forceful action needed to be taken. This time around, a similar hesitancy may prevail, only to give way to eventually more aggressive rate hikes. In fact, in 2010 the delay may prove even longer, with the attendant risks of financial market volatility once action is finally taken. Unlike two years ago, perceived growth risks are currently far more pronounced, leaving policy-makers reluctant to hike rates, especially if central banks elsewhere refuse to budge.

Political considerations have already raised the pressure on local monetary authorities to leave policy rates near their record lows. To be sure, central bank independence was never especially well cemented in the region. But, recently, it appears that in a number of countries political pressure on central bankers has become larger than at any time since the Asian financial crisis. What complicates the matter is that only three central banks in the region adhere to an explicit inflation targeting regime (Korea, Thailand, and the Philippines). Elsewhere, while we detect some implicit inflation preferences by the authorities, mandates are often decidedly muddied, rendering the authorities thus more liable to interference.

Political expediency, in short, is taking in some cases precedence over prudent monetary management. In the long run, however, there is no way to escape economic reality: policy rates will have to be raised if inflation, and especially core readings, begins to spiral upwards. The risk, however, is that such response will be delayed, thus necessitating a far more aggressive response than if the issue had been dealt with pre-emptively. What makes monetary policy so tricky, admittedly, is the long lag time with which interest rates affect inflationary conditions. But, dithering carries costs.

Growing political pressure, clearly, renders it more difficult to predict the reaction of central banks to growing inflation pressures. As noted, in practice, monetary authorities in the region have always pursued a multitude of goals, reflecting their sensitivity to foreign exchange rate fluctuations, asset price movements, growth performance, as well as inflation. In a comprehensive recent study, we estimated historical reaction functions for various Asian central banks, based on a VAR model (see Frederic Neumann and Song Yi Kim, *What do they target? A profile of Asian central banks*, 17 August 2009).

21. Monetary policy frameworks

Country	Objective of Monetary Policy	Monetary Policy Framework (IMF)	Policy rate	Target	Inflation Target	Inflation Target Horizon
China	Stability of the value of the currency, thereby promote economic growth	Exchange rate anchor	1-year base lending rate	implicit money growth targets and implicit CPI targets	target: 4% for 2010	1-year
India	price stability, financial stability, return to high growth, positive economic development	Multiple indicator approach (since April 1998)	Reverse repo (binding with current excess liquidity), repo	both WPI and CPI matter, even if in recent years the two have diverged	implicit 4% CPI March 2010	generally 3-year
Indonesia	internal and external stability of rupiah;	Inflation targeting framework (Initiated May 1999)	Overnight interest rate	Headline CPI	for 2010: 5% +/- 1%	1-year
Japan	Price stability	Other - BoJ has not committed to any inflation target but discloses the "understanding of medium- to long-term price stability" once a year in the second April meeting	Overnight call rate	The unofficial target is all Japan CPI (not core). This framework started in March 2006.	0% to 2%	1-year
Korea	Price stability	Inflation targeting framework (Initiated January 1998)	March 2008: changed from the call rate on overnight inter-bank lending to repo rate	Headline CPI 1998-99, core CPI 2000-06, since headline CPI	for 2010-2012 3.0 +/- 1	1-year
Malaysia	"promoting economic growth, a high level of employment, maintaining price stability and a reasonable balance in the country's international payments position, eradicating poverty and restructuring society"	Multiple indicator approach (focus on core inflation)	Overnight policy rate	Core CPI inflation (not explicit)	3% implicit inflation target	unspecified
Pakistan	monetary policy consistent with government's goal for inflation, growth	Other	Repo rate	N/A	N/A	6 months
Philippines	"promote low and stable inflation conducive to a balanced and sustainable economic growth"	Inflation targeting framework (initiated January 2002)	Overnight reverse repo rate	Headline CPI (also monitors core CPI)	3.5% to 5.5% for 2010; 3% to 5% in 2011	2 year
Singapore	"price stability for sustained economic growth"; since 1981 using S\$ trade weighted exchange rate index with secret basket composition	Exchange rate anchor (basket composition periodically reviewed)	None - exchange rate anchor	implicit use of CPI and unit labour costs	2009 CPI forecast 2.5-3.5% in 2010	6-months
Sri Lanka	economic and price stability	Monetary aggregate targeting framework.	Repo rate	Reserve money growth, though recently taking into account CPI level too	14.5% on average for 2010 (Reserve Money) and 5-6% on average for 2010 (CPI)	3-month
Taiwan	"promoting financial stability, ensuring sound banking operations, maintaining the stable internal and external value of the currency and, within the scope of the above three objectives, fostering economic development"	Not classified by IMF - HSBC classification: multiple indicator approach	Rediscount rate	No official inflation targeting - but core CPI (excluding fresh food and energy) is closely monitored. Also M2 target.	0.9-1.0% for headline CPI, M2 growth 2.5-6.5% (2010)	1-year
Thailand	"low inflation and stable exchange rate"	Inflation targeting framework (Initiated April 2000)	1-day repo rate (changed in 2007 from 14-day repo rate)	Core CPI inflation (excluding fresh food and energy)	0% to 3% for quarterly average of core CPI	Indefinite (taken as 8 quarters ahead)
Vietnam	"stabilising the value of the currency, controlling the inflation rate, facilitating socio-economic development, ensuring national defence, security and improving the living standards of the people" (Article 2)	Exchange rate anchor	Policy rate	Unofficial inflation target	7-8% comfort	1 year ahead

Source: National Authorities, HSBC

The main results from this exercise are reproduced in Table 22. The arrows denote the direction of interest rates to a positive shock to inflation, the exchange rate asset price, and growth. The number of stars provides a sense of the relative strength of the response, while red cells denote statistically highly significant results, while grey cells contain estimates of slightly more moderate significance.

The table, in short, provides a rough map of how central banks have reacted in the past to various shocks. The most inflation sensitive central banks, according to this exercise, are Malaysia, the Philippines, Thailand, and Vietnam, while growth matters especially in India. Among the most hawkish central banks when it comes to asset prices are Taiwan and Korea, which is one of the reasons why we have pencilled in these two central banks as the first hikers in the region, especially if financial markets maintain their recent ascent. Among the most sensitive central banks to respond to pressure in foreign exchange markets are Indonesia and China.

Taken together, few banks in Asia can be considered strict inflation targeters, with most following several objectives. Especially with perceived growth risks still prevalent and foreign exchange rates under

pressure from capital inflows, regional central banks may delay for too long the necessary hikes to squeeze out inflation pressures. A delayed reaction, which inevitably involves a more aggressive subsequent move, may then introduce considerable volatility into financial markets.

Of course, monetary tightening doesn't have to take the form of interest rate hikes. In Asian markets especially a number of tools may be deployed to address inflationary pressures, including (a) a withdrawal of fiscal stimuli, most notably in China, (b) tighter bank supervision, including a beefing up of capital requirements or stricter lending guidelines, most notably for mortgages (c) a cap on aggregate credit growth, again most obviously in China, and (d) a more rapid appreciation of exchange rates.

In practice, a combination of these measures will be deployed, varying in emphasis from market to market. China, Korea, India, the Philippines, and Indonesia especially may be candidates for more rapid exchange rate appreciation should inflation pressures rise markedly. However, as our FX strategists have repeatedly pointed out, ongoing concerns about the economic recovery, as well as the political strength of export lobbies, should prevent any radical moves for the time being.

Table 22: Summary assessment of central bank sensitivity to inflation, growth, exchange rate, and asset price shocks (from * = low to ** = high; red denotes highest, grey second highest sensitivity; arrow denotes direction of policy rate to positive shock)**

	CH	IN	ID	SK	MY	PH	TW	TH	VN
After 6 months									
Inflation	**▲	***▲	**▲	***▲	****▲	****▲	*▼	****▲	****▲
FX	*▼	*▲	****▼	*▲	**▲	***▲	**▲	**▼	***▲
Growth	*▼	***▲	***▲	***▲	****▲	**▲	***▲	**▼	*▲
Assets	***▲	*▲	**▲	***▲	**▲	***▼	****▲	***▲	**▲
After 12 months									
Inflation	*▲	**▲	*▲	**▲	***▲	****▲	**▼	****▲	****▲
FX	***▼	**▲	****▼	***▲	**▲	***▲	**▲	**▼	***▲
Growth	*▼	****▲	***▲	**▲	****▲	*▲	**▲	*▼	*▼
Assets	***▲	*▲	**▲	****▲	***▲	***▼	****▲	***▲	*▲
After 24 months									
Inflation	**▼	***▼	*▼	**▲	***▲	****▲	**▼	****▲	****▲
FX	****▼	**▲	****▼	***▲	**▲	****▲	**▼	***▼	***▲
Growth	*▼	****▲	***▲	**▲	****▲	*▲	**▲	**▼	**▼
Assets	**▼	*▼	***▲	****▲	****▲	**▼	****▲	***▲	***▲

Source: HSBC;
NB: the arrows denote the direction of policy rates if (a) inflation increases, (b) the exchange rate appreciates faster than trend, (c) output exceeds potential, (d) asset prices rise faster than trend

Moreover, from a monetary policy perspective it is difficult to see how all these alternative tools, including exchange rate appreciation could really be effective without a significant hike in interest rates as well. After all, a more rapid rise in the currency may only invite more capital to pour into the country, raising liquidity if interest rates are not raised sufficiently in compensation. Also, lending restrictions and tighter supervision may not do the trick: what matters for economies is the price of capital, which is determined by interest rates. Fiddling with the regulatory framework may only provide temporary relief.

Where the ship's headed

The risks outlined in this chapter, as noted, do not represent out base case. In general, we expect inflation pressures to remain muted for the time being, with commodity markets being sufficiently restrained by weakness in advanced economies, and core pressures likewise remaining well contained. However, the risk is clearly to the upside. For example, structural shifts in the behaviour of inflation in the region, renders our forecasting exercise more precarious. Moreover, the policy response by central banks may be delayed, adding temporarily to prices pressures until rates are finally raised.

Our forecasts for both headline inflation and policy rates are presented in the following two tables, with increases marked in red. For inflation, Indonesia and Sri Lanka are likely to see the biggest ppt increase over the coming year, while the pace of acceleration is also significant in China, Vietnam, the Philippines, Malaysia, and Singapore. In Hong Kong and India, inflation is expected to fall by the fourth quarter of 2010, although in the former it may spike mid-year.

For policy rates, we expect the biggest ppt hikes in the base rate over the coming year in Vietnam, India and Indonesia. Although in Australia, New Zealand, Taiwan, the Philippines and Thailand rates are also going up markedly. In general, however, we have pencilled in a fairly muted response by the monetary authorities, reflecting both uncertainties over the trajectory of underlying inflation as well as the traditional behaviour of Asian central banks not to allow spreads over the US policy rate to become too wide. But, as outlined, the risks are on the upside, both on inflation and with regards to the fact that rates may eventually have to rise more sharply than anticipated.

23. HSBC headline CPI forecast (% y-o-y, red denotes acceleration, last two columns change from 4Q 2009)

	Q4 09	Q1 10f	Q2 10f	Q3 10f	Q4 10f	Q1 11f	Q2 11f	Q3 11f	Q4 11f	09 to Q4 10	09 to Q4 11
Australia	2.0	2.5	2.8	3.0	2.8	3.0	3.0	3.0	3.0	0.8	1.0
New Zeal.	1.9	2.0	2.2	2.3	2.4	2.4	2.5	2.6	2.8	0.5	0.9
China	0.1	1.7	3.0	2.7	3.0	2.8	2.3	2.5	2.5	2.9	2.4
Hong Kong	1.9	1.9	3.0	4.2	1.8	3.4	2.4	2.8	3.2	-0.1	1.3
India	11.8	12.5	11.5	8.0	7.0	6.0	6.0	6.0	6.0	-4.8	-5.8
Indonesia	2.7	4.8	6.8	7.5	8.3	7.8	7.2	6.7	6.4	5.6	3.7
Japan	-1.6	-1.0	-1.4	-1.3	-1.3	-1.1	-0.7	-0.7	-0.6	0.3	1.0
Korea	2.5	2.9	3.4	3.5	3.6	3.3	3.1	3.1	3.2	1.1	0.8
Malaysia	0.1	2.7	3.5	3.5	3.3	2.5	2.5	2.5	2.5	3.2	2.4
Pakistan	7.9	8.3	7.4	7.0	8.0	8.0	8.0	7.5	7.0	0.1	-0.9
Philippines	2.2	4.1	4.9	5.5	5.8	5.7	5.6	5.6	5.7	3.6	3.5
Singapore	-0.3	1.8	3.5	3.0	3.2	2.2	2.0	1.9	1.9	3.5	2.2
Sri Lanka	2.5	4.0	6.5	9.8	9.6	7.7	5.6	6.5	7.2	7.1	4.7
Taiwan	-1.0	1.2	0.9	1.4	1.9	1.8	1.7	1.7	1.7	2.9	2.7
Thailand	1.5	2.6	2.4	3.3	3.6	3.8	3.7	3.4	2.9	2.2	1.5
Vietnam	5.0	9.3	12.0	11.0	8.5	7.5	7.0	6.9	6.8	3.6	1.9

Source: CEIC, HSBC; NB: last two columns measure bp change from end 2009 to end 2010 and 2011, respectively

24. HSBC policy rate forecasts (%; increases denoted in red, last two columns change from 4Q 2009)

	Q4 09	Q1 10f	Q2 10f	Q3 10f	Q4 10f	Q1 11f	Q2 11f	Q3 11f	Q4 11f	09 to Q4 10	09 to Q4 11
Australia	3.75	4.00	4.25	4.25	4.50	4.75	4.75	5.00	5.00	0.8	1.3
New Zeal.	2.50	2.50	2.75	3.00	3.25	3.50	3.75	4.00	4.25	0.8	1.8
China	5.31	5.31	5.31	5.58	5.85	5.85	5.85	5.85	5.85	0.5	0.5
Hong Kong	0.50	0.50	0.50	0.50	0.50	0.50	0.50	1.00	1.50	0.0	1.0
India	4.75	5.00	5.25	5.75	6.25	6.50	6.75	7.00	7.00	1.5	2.3
Indonesia	6.50	6.50	7.00	7.50	8.00	8.00	8.00	8.00	8.00	1.5	1.5
Japan	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.0	0.0
Korea	2.00	2.25	2.25	2.75	3.00	3.25	3.50	3.75	4.00	1.0	2.0
Malaysia	2.00	2.00	2.00	2.25	2.50	2.75	3.00	3.00	3.00	0.5	1.0
Pakistan	11.00	10.00	9.00	9.00	9.00	9.00	9.00	10.00	10.00	-2.0	-1.0
Philippines	4.00	4.00	4.25	4.50	4.75	5.00	5.50	5.50	5.50	0.8	1.5
Singapore	0.60	0.60	0.70	0.70	0.80	0.80	0.90	0.90	1.00	0.2	0.4
Sri Lanka	9.75	9.75	9.75	10.00	10.25	10.50	11.00	11.00	11.00	0.5	1.3
Taiwan	1.25	1.50	1.75	2.00	2.00	2.25	2.25	2.50	2.75	0.8	1.5
Thailand	1.25	1.25	1.50	1.75	2.00	2.00	2.25	2.50	2.50	0.8	1.3
Vietnam	8.00	9.00	10.00	11.00	12.00	12.00	12.00	12.00	12.00	4.0	4.0

Source: CEIC, HSBC; NB: last two columns measure bp change from end 2009 to end 2010 and 2011, respectively

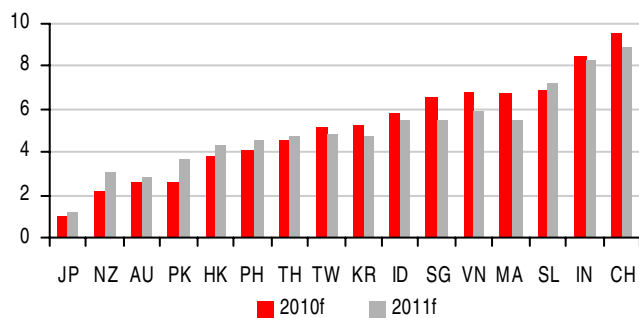
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GDP

(% y-o-y)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	9.1	10.0	10.1	10.2	11.6	13.0	9.6	8.5	9.5	8.9
Hong Kong	1.8	3.0	8.5	7.1	7.0	6.4	2.4	-3.6	3.8	4.3
Japan	0.3	1.4	2.7	1.9	2.0	2.4	-1.2	-5.2	1.0	1.2
Korea	7.2	2.8	4.6	4.0	5.2	5.1	2.2	0.4	5.2	4.8
Taiwan	5.3	3.7	6.2	4.7	5.4	6.0	0.7	-2.8	5.1	4.9
North Asia-ex Japan	7.7	7.2	8.3	8.0	9.4	10.5	7.6	6.0	8.3	7.8
Australia	3.9	3.2	3.6	3.1	2.7	4.8	2.2	0.8	2.6	2.8
India	3.8	8.5	7.5	9.5	9.7	9.0	6.7	7.2	8.5	8.3
Indonesia	4.5	4.8	5.0	5.7	5.5	6.3	6.1	4.3	5.8	5.5
Malaysia	4.4	5.4	7.3	5.3	5.8	6.2	4.6	-2.0	6.8	5.5
New Zealand	4.7	4.4	4.0	3.1	2.3	3.3	-0.7	-0.4	2.1	3.1
Pakistan	4.8	7.4	7.7	6.2	5.7	2.0	3.7	0.8	2.6	3.7
Philippines	4.4	4.9	6.4	5.0	5.3	7.1	3.8	1.1	4.2	4.6
Singapore	4.0	2.9	8.7	8.7	8.4	7.8	1.1	-2.2	6.5	5.5
Sri Lanka	4.0	5.9	5.5	6.2	7.7	6.8	6.0	3.8	7.0	7.2
Thailand	5.3	7.0	6.4	4.7	5.1	4.9	2.5	-2.9	4.6	4.7
Vietnam	7.1	7.3	7.8	8.4	8.2	8.5	6.2	5.3	6.8	5.9
Asia-ex China, India & Japan	5.3	4.1	6.0	5.2	5.7	5.7	3.1	0.0	5.2	4.9
Asia-ex China & Japan	5.0	5.1	6.4	6.2	6.7	6.6	4.1	2.0	6.1	5.9
Asia-ex Japan	6.6	7.1	7.9	7.9	8.8	9.5	6.8	5.2	7.8	7.4
Asia	3.3	4.2	5.3	5.2	6.0	6.9	4.0	1.5	5.4	5.2

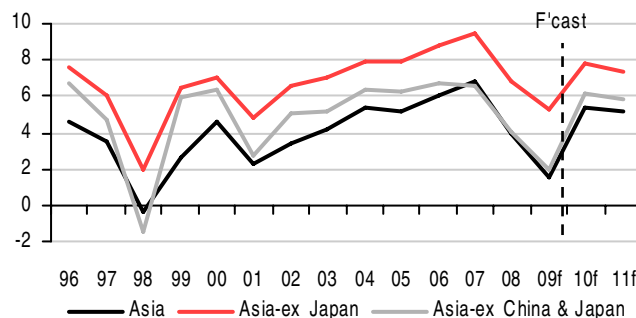
Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

GDP (% yr): China, India and Sri Lanka to expand the most in 2010



Source: HSBC, CEIC

GDP (% yr): A sharp rebound in 2010 across the region



Source: HSBC, CEIC

GDP

(% y-o-y)	2008				2009				2010f			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Qf	1Q	2Q	3Q	4Q
Australia	3.2	2.4	2.3	1.0	0.7	0.4	0.5	1.8	0.7	0.4	0.5	1.8
China	10.6	10.1	9.0	6.8	6.1	7.9	8.9	10.2	9.7	9.5	9.3	9.4
Hong Kong	7.3	4.1	1.5	-2.6	-7.8	-3.6	-2.4	-0.5	5.9	3.4	2.7	3.3
India	8.6	7.8	7.7	5.8	5.8	6.1	7.9	7.7	7.2	7.9	7.1	9.1
Indonesia	6.2	6.4	6.4	5.2	4.4	4.0	4.2	4.7	5.4	5.8	6.0	5.8
Japan	1.3	-0.3	-1.4	-4.1	-8.9	-5.8	-5.1	-1.7	1.3	0.8	0.9	0.9
Korea	5.5	4.3	3.1	-3.4	-4.2	-2.2	0.9	6.8	5.2	7.3	5.3	3.3
Malaysia	7.4	6.6	4.8	0.1	-6.2	-3.9	-1.2	3.3	10.1	7.4	5.0	5.0
New Zealand	1.1	-0.7	-1.2	-2.1	-1.7	-1.0	-0.7	1.7	2.9	2.4	2.1	1.1
Philippines	3.9	4.2	4.6	2.9	0.6	0.8	0.8	2.0	5.3	7.8	0.6	3.0
Singapore	6.7	2.5	0.0	-4.2	-9.5	-3.3	0.6	3.7	10.0	5.6	5.1	5.7
Sri Lanka	6.2	7.0	6.3	4.3	1.5	2.1	4.2	7.2	7.0	7.5	6.8	6.5
Taiwan	6.9	5.4	-0.8	-7.1	-9.1	-6.9	-1.3	5.7	8.1	5.9	4.2	2.9
Thailand	6.4	5.2	2.9	-4.2	-7.1	-4.9	-2.8	3.2	3.7	0.7	6.7	7.1
Vietnam	7.5	5.8	6.5	5.7	3.1	4.5	5.8	7.7	6.5	7.0	7.0	6.8

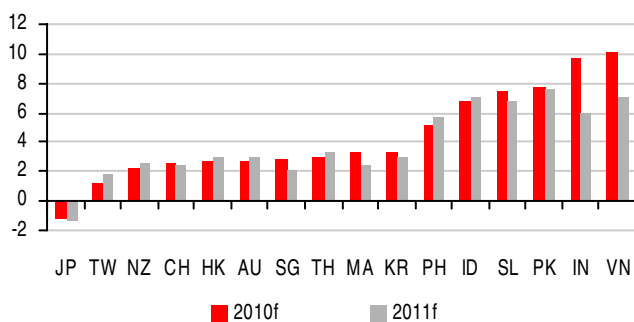
Source: HSBC, CEIC

Inflation

(% y-o-y)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	-0.8	1.2	3.9	1.8	1.5	4.8	5.9	-0.9	2.6	2.5
Hong Kong	-3.0	-2.6	-0.4	0.9	2.0	2.0	4.3	0.7	2.7	3.0
Japan	-0.9	-0.2	0.0	-0.3	0.2	0.0	1.5	-1.2	-1.2	-0.8
Korea	2.8	3.5	3.6	2.8	2.2	2.5	4.7	2.8	3.3	3.0
Taiwan	-0.2	-0.3	1.6	2.3	0.6	1.8	3.5	-0.9	1.2	1.7
North Asia-ex Japan	-0.1	1.4	3.4	2.0	1.6	4.0	5.5	-0.3	2.6	2.5
Australia	3.0	2.8	2.3	2.7	3.5	2.3	4.3	1.8	2.8	3.0
India	4.0	3.7	3.9	4.0	6.3	6.4	8.3	10.5	9.6	6.0
Indonesia	11.9	6.8	6.1	10.5	13.1	6.4	10.2	4.8	6.8	7.0
Malaysia	1.8	1.1	1.4	3.0	3.6	2.0	5.4	0.7	3.3	2.5
New Zealand	2.7	1.8	2.3	3.0	3.4	2.4	3.9	2.1	2.2	2.6
Pakistan	3.5	2.9	7.4	9.1	7.9	7.6	20.3	13.4	7.7	7.6
Philippines	2.9	3.5	6.0	7.7	6.3	2.8	9.3	3.3	5.2	5.6
Singapore	-0.4	0.5	1.7	0.5	1.0	2.1	6.5	0.2	2.9	2.0
Sri Lanka	10.2	2.6	9.0	11.0	10.0	15.8	22.7	3.4	7.5	6.7
Thailand	0.7	1.8	2.8	4.5	4.6	2.2	5.5	-0.8	3.0	3.3
Vietnam	4.1	3.1	7.8	8.3	7.5	8.3	23.0	7.8	10.1	7.0
Asia-ex China, India & Japan	2.5	2.3	3.4	4.2	4.3	3.4	7.4	2.6	4.1	4.0
Asia-ex China & Japan	2.8	2.7	3.5	4.1	4.8	4.2	7.7	4.8	5.6	4.5
Asia-ex Japan	1.4	2.1	3.7	3.2	3.4	4.5	6.8	1.9	4.1	3.5
Asia	0.2	0.9	1.9	1.6	2.1	2.8	4.9	0.8	2.2	2.0

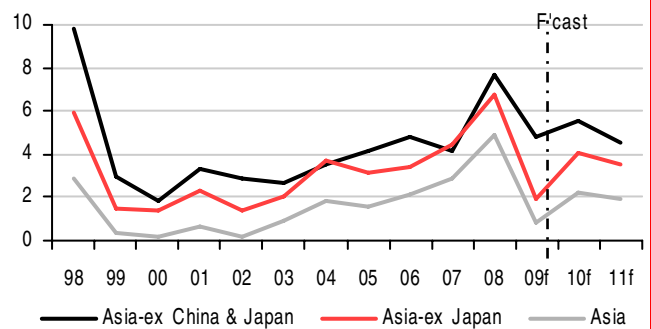
Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

CPI (% yr): Inflation to return for most of the countries in 2010



Source: HSBC, CEIC

CPI (% yr): Inflation to pick up sharply in Asia ex-Japan in 2010



Source: CEIC, HSBC

CPI

(% y-o-y)	2008				2009				2010f			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Qf	1Q	2Q	3Q	4Q
Australia	4.2	4.5	5.0	3.7	2.5	1.5	1.3	2.0	2.5	2.8	3.0	2.8
China	8.0	7.8	5.3	2.5	-0.6	-1.5	-1.3	-0.2	1.7	3.0	2.7	3.0
Hong Kong	4.6	5.7	4.6	2.3	1.7	-0.1	-0.9	1.9	1.9	3.0	4.2	1.8
India	6.3	7.8	9.0	10.2	9.4	8.9	11.8	11.8	12.5	11.5	8.0	7.0
Indonesia	6.5	9.0	12.0	11.5	8.6	5.7	2.8	2.6	4.6	6.8	7.5	8.3
Japan	1.0	1.4	2.2	1.0	0.0	-1.0	-2.3	-1.6	-1.0	-1.4	-1.3	-1.3
Korea	3.8	4.8	5.5	4.5	3.9	2.8	2.0	2.4	3.1	3.3	3.3	3.4
Malaysia	2.6	4.9	8.4	5.9	3.7	1.3	-2.3	0.1	2.7	3.5	3.5	3.3
New Zealand	3.4	4.0	5.1	3.4	3.0	1.9	1.7	1.9	2.0	2.2	2.3	2.4
Pakistan	12.4	19.3	24.5	24.3	20.2	14.9	10.7	7.9	8.3	7.4	7.0	8.0
Philippines	5.5	9.7	12.2	9.7	6.9	3.2	0.3	3.0	4.5	4.9	5.5	5.8
Singapore	6.6	7.5	6.6	5.4	2.1	-0.5	-0.4	-0.3	1.8	3.5	3.0	3.2
Sri Lanka	22.1	26.5	25.2	16.9	7.8	2.4	0.9	2.5	4.0	6.5	9.8	9.6
Taiwan	3.6	4.2	4.5	1.9	0.0	-0.8	-1.3	-1.2	0.9	0.9	1.4	1.8
Thailand	5.0	7.5	7.3	2.1	-0.2	-2.8	-2.2	1.9	2.9	2.4	3.3	3.5
Vietnam	16.4	24.5	27.7	23.6	14.5	6.3	2.7	7.7	9.0	12.0	11.0	8.5

Source: HSBC, CEIC

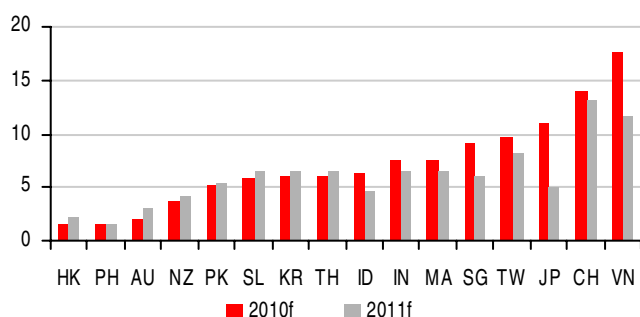
Industrial production & unemployment

Industrial production

(% y-o-y)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China (VAI)	12.7	16.7	16.3	15.9	16.2	16.0	12.9	9.5	14.0	13.0
Hong Kong	-9.7	-9.2	2.9	2.5	2.2	-1.5	-6.6	-8.7	1.5	2.3
Japan	-1.3	3.3	5.5	1.1	4.8	2.8	-3.2	-22.7	11.0	5.1
Korea	8.0	5.5	10.4	6.3	8.4	6.9	3.1	-3.1	6.0	6.6
Taiwan	7.5	9.1	9.3	3.8	4.7	7.8	-1.8	-12.4	9.7	8.2
North Asia-ex Japan	9.5	11.7	13.5	11.8	12.8	12.7	9.7	5.4	12.0	11.3
Australia	2.7	0.4	0.5	1.6	1.7	3.0	2.9	-3.3	2.0	3.0
India	5.8	7.0	8.4	8.2	11.5	8.5	2.6	6.1	7.5	6.5
Indonesia	5.3	5.3	6.4	4.6	4.6	4.7	3.7	1.7	6.3	4.7
Malaysia	4.3	8.4	11.3	5.2	6.7	3.1	1.4	-9.8	7.5	6.5
New Zealand	5.3	3.4	4.2	0.5	-3.7	1.3	-0.8	-7.8	3.8	4.1
Pakistan	4.0	13.3	17.8	14.9	10.7	5.5	-0.3	-4.2	5.2	5.5
Philippines	3.5	4.2	5.0	5.3	4.2	3.3	4.3	-4.9	1.5	1.5
Singapore	8.4	-30.3	13.9	9.5	11.9	5.9	-4.2	-3.4	9.2	6.0
Sri Lanka	2.3	5.9	5.6	6.0	5.7	7.6	5.5	1.5	5.8	6.5
Thailand	9.1	14.0	11.7	9.1	7.3	8.2	5.3	-7.0	6.0	6.6
Vietnam	14.2	19.8	17.6	25.5	16.0	18.2	15.9	8.6	17.5	11.5
Asia-ex China, India & Japan	5.5	4.5	9.7	6.5	7.0	6.0	1.9	-4.4	6.5	6.0
Asia-ex China & Japan	5.6	5.1	9.4	6.9	8.1	6.6	2.1	-1.6	6.8	6.1
Asia-ex Japan	8.4	9.7	12.2	10.6	11.6	10.8	7.5	4.0	10.4	9.5
Asia	3.4	6.4	8.9	6.3	8.8	7.9	3.7	-5.6	10.6	7.9

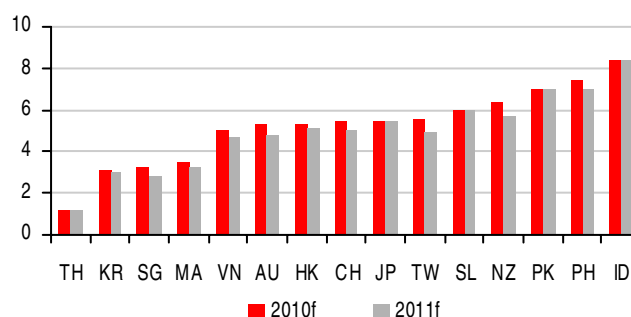
Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

Industrial production (% yr): Vietnam and China to lead in 2010



Source: HSBC, CEIC

Unemployment rate (%): Highest in Indonesia, Philippines and Pakistan



Source: HSBC, CEIC

Unemployment rate ave.

(%)	2002	2003	2004	2005	2006	2007	2008f	2009f	2010f	2011f
China	4.0	4.3	4.2	4.2	4.1	4.0	4.2	6.0	5.5	5.0
Hong Kong	7.3	7.9	6.8	5.6	4.8	4.0	3.6	5.3	5.3	5.1
Japan	5.4	5.2	4.7	4.4	4.1	3.9	4.0	5.1	5.5	5.5
Korea	3.3	3.6	3.7	3.7	3.5	3.2	3.2	3.6	3.1	3.0
Taiwan	5.2	5.0	4.4	4.1	3.9	3.9	4.1	5.9	5.6	4.9
North Asia-ex Japan	4.2	4.4	4.2	4.1	4.0	3.8	4.0	5.6	5.1	4.7
Australia	6.4	5.9	5.4	5.1	4.8	4.4	4.2	5.6	5.3	4.8
Indonesia	8.6	9.3	9.7	10.6	10.8	9.7	8.8	8.5	8.4	8.4
Malaysia	3.5	3.6	3.6	3.6	3.3	3.2	3.3	3.7	3.5	3.3
New Zealand	5.3	4.8	4.1	3.8	3.8	3.7	4.2	6.1	6.3	5.7
Pakistan	8.3	7.7	7.7	6.2	5.2	5.2	8.0	8.0	7.0	7.0
Philippines	11.5	11.5	11.9	8.0	7.9	7.2	7.5	7.7	7.4	7.0
Singapore	3.6	4.0	3.5	3.2	2.7	2.2	2.1	3.2	3.2	2.8
Sri Lanka	8.8	8.4	8.5	7.2	6.5	6.0	5.3	6.0	6.0	6.0
Thailand	2.4	2.2	2.1	1.9	1.5	1.4	1.4	1.4	1.2	1.2
Vietnam	6.0	5.8	5.6	5.3	4.8	4.6	4.7	5.2	5.0	4.7
Asia-ex China & Japan	5.2	5.4	5.2	4.9	4.7	4.4	4.6	5.1	4.8	4.6
Asia-ex Japan	4.7	4.9	4.7	4.6	4.4	4.2	4.4	5.6	5.2	4.8
Asia	5.0	5.1	4.7	4.5	4.3	4.1	4.2	5.4	5.3	5.1

Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

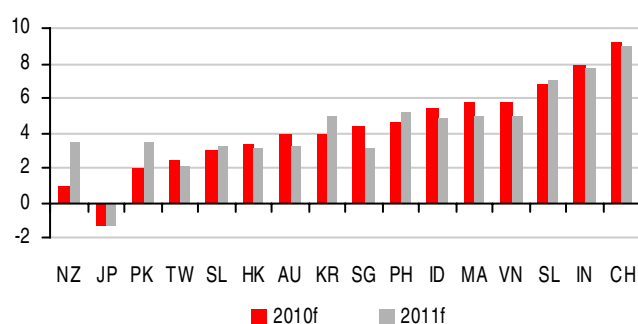
Consumption & saving

Consumer expenditure

(% y-o-y)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	6.2	6.5	7.2	8.5	8.7	9.0	8.9	8.0	9.2	9.0
Hong Kong	-0.9	-1.3	7.0	3.0	5.9	8.5	1.7	-1.0	3.4	3.2
Japan	1.1	0.4	1.6	1.3	1.5	1.6	-0.7	-0.9	1.4	1.3
Korea	8.9	-0.4	0.3	4.6	4.7	5.1	0.9	0.1	3.9	4.9
Taiwan	3.3	2.9	5.2	2.9	1.5	2.1	-0.6	0.9	2.4	2.1
North Asia-ex Japan	6.0	4.0	5.4	6.8	7.0	7.6	6.7	5.9	7.7	7.7
Australia	3.9	3.6	5.9	3.0	3.2	4.4	2.6	2.1	3.9	3.2
India	2.9	8.2	5.2	7.1	6.3	8.5	2.9	3.5	8.0	7.7
Indonesia	3.8	3.9	5.0	4.0	3.2	5.0	5.3	5.1	5.4	4.9
Malaysia	4.4	6.6	10.5	9.1	6.8	10.4	8.5	2.1	5.7	5.0
New Zealand	4.3	5.9	5.4	4.7	2.2	3.9	-0.3	-0.9	0.9	3.5
Pakistan	0.4	10.1	12.9	1.0	4.7	-1.3	5.2	1.0	2.0	3.5
Philippines	4.1	5.3	5.9	4.8	5.5	5.8	4.7	3.6	4.7	5.2
Singapore	4.9	0.9	5.9	3.1	4.0	5.2	2.4	-1.2	4.4	3.2
Sri Lanka	7.5	6.5	4.7	2.6	7.3	7.8	6.7	3.5	6.8	7.0
Thailand	5.4	6.4	6.1	4.9	3.2	1.7	2.7	-1.5	3.0	3.3
Vietnam	7.6	8.0	7.1	7.3	8.2	9.6	7.6	3.4	5.8	5.0
Asia-ex China, India & Japan	5.1	2.5	4.5	4.2	4.3	4.8	2.9	1.2	4.0	4.2
Asia-ex China & Japan	4.6	3.8	4.6	5.0	4.8	5.8	2.9	1.8	5.1	5.1
Asia-ex Japan	5.3	4.9	5.7	6.4	6.4	7.2	5.9	4.9	7.2	7.1
Asia	3.1	2.6	3.7	4.1	4.4	5.2	3.5	2.8	5.1	5.0

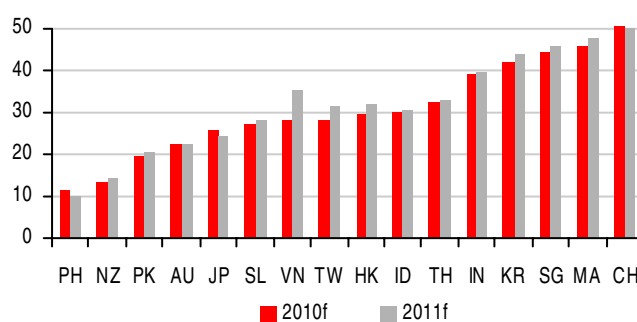
Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

Consumer expenditure(% y-o-y): China and India are still leading



Source: HSBC, CEIC

Saving as a % of GDP: China, Malaysia and Singapore the highest



Source: HSBC, CEIC

Gross saving ratios

% of GDP	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	40.4	43.2	45.7	48.2	50.1	51.0	51.4	50.0	50.5	50.0
Hong Kong	30.7	30.4	30.2	33.3	33.3	31.0	30.4	29.4	29.5	31.8
Japan	24.5	25.7	26.7	26.2	27.1	26.5	26.0	26.0	25.5	24.5
Korea	31.4	33.0	35.0	33.2	31.5	30.8	37.6	38.9	42.0	43.7
Taiwan	26.5	26.9	27.4	27.1	28.8	30.1	27.6	25.2	28.1	31.3
North Asia-ex Japan	36.0	38.3	40.5	41.9	43.2	44.4	46.9	45.9	46.9	47.1
Australia	20.0	20.4	19.6	20.3	21.6	22.3	24.3	22.2	22.2	22.5
India	27.1	29.3	33.8	35.1	37.0	38.1	36.3	40.0	39.0	39.5
Indonesia	25.1	23.7	24.9	27.5	28.7	28.1	30.6	29.4	29.9	30.4
Malaysia	42.3	42.5	44.0	43.5	43.4	46.1	49.1	42.8	45.5	47.5
New Zealand	18.3	18.1	17.6	16.5	14.9	15.8	14.3	12.0	13.1	14.1
Pakistan	22.2	17.1	14.6	13.9	14.3	11.2	12.5	18.3	19.7	20.5
Philippines	19.1	19.3	21.2	21.0	20.1	20.8	19.2	9.8	11.3	10.0
Singapore	40.9	42.0	46.8	48.7	49.9	51.7	48.3	45.3	44.4	45.8
Sri Lanka	20.3	19.5	21.6	21.6	23.7	25.3	25.0	25.9	27.1	28.1
Thailand	31.7	32.0	31.7	30.9	32.4	34.4	32.5	32.3	32.1	32.7
Vietnam	32.0	30.6	32.0	34.6	36.5	31.8	29.9	33.4	28.0	35.3
Asia-ex China, India & Japan	29.9	30.1	31.4	31.4	31.3	31.3	33.1	32.2	33.7	35.3
Asia-ex China & Japan	29.3	30.0	32.0	32.3	32.7	33.1	34.0	34.4	35.2	36.5
Asia-ex Japan	33.7	35.2	37.6	38.9	40.1	41.1	42.7	42.2	42.8	43.2
Asia	29.0	30.4	32.2	33.0	34.8	35.8	36.7	36.4	36.6	36.5

Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

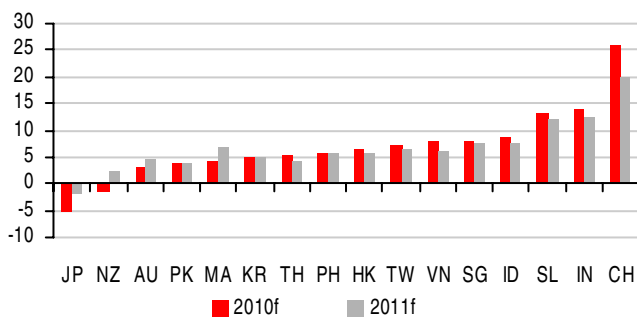
Investment

Total investment

(% y-o-y)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	16.9	27.7	27.6	27.2	24.5	25.8	26.1	29.5	26.0	20.0
Hong Kong	-4.6	1.0	2.7	4.1	7.1	3.4	0.0	-5.5	6.6	5.8
Japan	-4.9	-0.5	1.4	3.1	0.5	-1.2	-2.6	-14.0	-5.2	-1.9
Korea	7.1	4.4	2.1	1.9	3.4	4.2	-1.7	-1.0	4.9	5.1
Taiwan	1.1	-0.1	14.0	2.7	0.1	0.6	-11.2	-14.2	7.1	6.6
North Asia-ex Japan	11.3	17.6	19.0	17.7	16.7	18.4	18.3	20.5	20.7	16.2
Australia	15.8	9.6	7.0	8.8	4.6	9.6	8.3	-2.0	3.2	4.6
India	7.7	9.7	18.9	17.6	14.5	12.9	8.2	8.0	14.0	12.3
Indonesia	4.7	0.6	14.7	10.9	2.6	9.4	11.7	3.8	8.7	7.4
Malaysia	0.3	2.7	3.1	5.0	7.5	9.6	0.8	-8.0	4.1	7.0
New Zealand	10.8	10.4	12.8	5.2	-1.0	5.5	-2.7	-13.7	-1.4	2.3
Pakistan	4.1	-6.1	13.5	19.9	13.6	3.8	-6.5	3.0	4.0	4.0
Philippines	2.3	3.6	1.3	-6.6	3.9	10.9	2.9	-3.8	5.6	5.9
Singapore	-11.4	-3.2	10.2	-2.0	13.3	19.2	13.7	-4.9	8.0	7.6
Sri Lanka	6.4	10.1	17.8	9.8	13.9	12.0	11.0	4.5	13.0	12.0
Thailand	6.5	12.1	13.2	10.5	3.9	1.5	1.2	-8.1	5.4	4.2
Vietnam	12.9	11.9	10.4	9.7	9.9	23.0	13.2	3.2	8.0	6.0
Asia-ex China, India & Japan	3.1	2.7	7.7	4.6	4.6	6.2	1.3	-3.2	6.2	6.0
Asia-ex China & Japan	4.1	4.3	10.4	7.8	7.1	8.0	3.2	-0.1	8.4	7.7
Asia-ex Japan	9.1	13.6	17.4	15.8	14.5	16.0	14.6	14.6	17.2	13.8
Asia	1.9	6.5	9.5	10.0	8.7	9.7	8.4	4.4	9.1	8.2

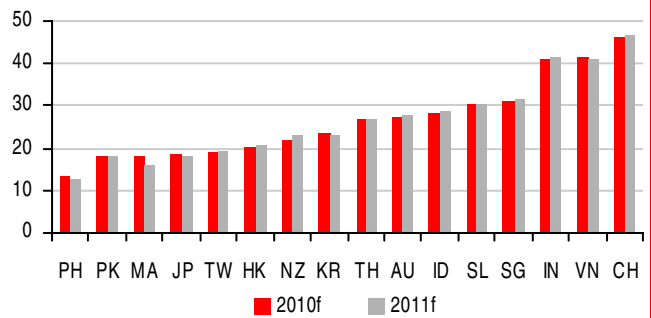
Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

Investment growth (% yr): China, India & Sri Lanka to lead in 2010



Source: HSBC, HSBC

Investment as a % of GDP: High in China, room to rise elsewhere



Source: HSBC, CEIC

Investment / GDP

(%)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	37.9	41.0	43.2	42.7	42.6	42.2	43.5	45.0	46.0	46.6
Hong Kong	22.4	21.2	21.3	20.9	21.9	20.1	19.5	19.7	20.3	20.7
Japan	23.6	23.2	22.9	23.2	22.9	22.2	21.9	19.7	18.5	17.9
Korea	29.1	30.0	30.4	30.1	29.8	29.4	25.4	24.3	23.5	22.9
Taiwan	19.3	19.9	23.7	22.7	22.7	22.1	22.7	17.0	19.0	19.2
North Asia-ex Japan	32.6	34.9	37.0	36.7	37.0	37.0	38.4	39.0	39.7	40.1
Australia	22.6	23.9	24.8	26.1	26.6	28.0	30.0	28.5	27.3	27.8
India	26.7	28.1	33.2	36.8	38.4	41.1	41.4	41.5	41.0	41.5
Indonesia	21.4	25.6	24.1	25.1	25.4	24.9	27.8	27.5	28.1	28.7
Malaysia	24.0	21.6	22.7	19.9	20.0	22.1	21.4	31.5	18.0	16.0
New Zealand	22.8	24.1	26.1	26.6	25.8	26.3	25.8	22.2	21.8	23.3
Pakistan	17.3	15.2	16.0	17.8	19.0	19.4	17.5	17.5	17.7	17.8
Philippines	17.7	16.7	16.7	14.6	14.5	15.4	15.2	13.2	13.1	12.6
Singapore	23.6	16.0	21.8	20.2	20.1	20.7	30.9	29.4	31.1	31.5
Sri Lanka	22.0	21.2	22.1	25.0	28.7	29.9	29.9	30.2	30.0	30.0
Thailand	23.8	25.0	26.8	31.4	28.3	26.4	28.9	22.0	26.9	26.7
Vietnam	31.3	32.7	33.5	35.6	36.8	41.6	41.5	41.0	41.3	41.3
Asia-ex China, India & Japan	24.0	24.3	25.5	25.6	25.5	25.2	25.0	23.8	23.6	23.4
Asia-ex China & Japan	24.6	25.2	27.3	28.3	28.7	29.4	29.4	28.7	28.3	28.3
Asia-ex Japan	29.8	31.5	33.8	34.3	34.6	35.1	36.5	36.8	37.1	37.4
Asia	26.6	27.3	28.4	29.2	29.8	30.4	31.2	30.7	30.5	30.4

Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

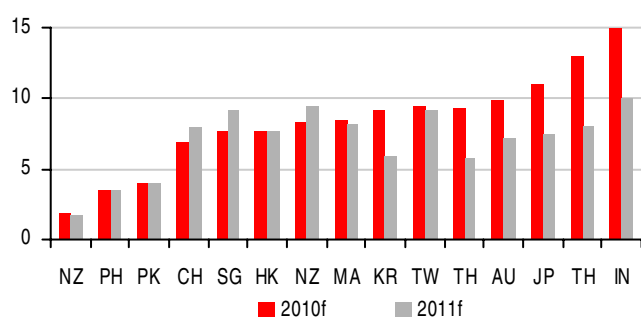
Trade

Real exports

(% y-o-y)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	18.0	32.0	32.0	29.0	25.0	23.8	11.2	-14.0	7.0	8.0
Hong Kong	9.0	12.8	15.4	10.6	9.4	8.3	2.7	-11.2	7.6	7.7
Japan	7.5	9.2	13.9	7.0	9.7	8.4	1.6	-24.5	11.0	7.5
Korea	12.1	14.5	19.7	7.8	11.4	12.6	5.7	-1.1	9.2	5.9
Taiwan	11.4	10.2	15.4	7.8	11.4	9.6	0.6	-10.8	9.4	9.2
North Asia-ex Japan	15.3	24.4	26.6	21.0	20.0	19.7	9.3	-11.6	7.5	7.7
Australia	11.2	11.0	14.8	9.0	7.1	11.9	10.3	-7.6	9.9	7.2
India	21.1	9.6	27.2	17.6	21.1	2.1	12.8	-3.0	15.0	10.0
Indonesia	-1.2	5.9	13.5	16.6	9.4	8.5	9.5	-9.7	8.5	8.2
Malaysia	4.5	5.7	2.3	8.3	6.6	4.5	1.3	-11.3	8.4	9.4
New Zealand	6.4	2.3	6.1	-0.4	1.7	3.8	-1.2	0.4	1.8	1.8
Pakistan	28.4	-1.5	9.6	9.9	2.3	-5.3	9.0	-1.0	4.0	4.0
Philippines	4.1	4.8	15.0	4.8	13.4	5.4	-1.9	-11.4	3.5	3.6
Singapore	7.2	13.7	20.6	11.7	11.7	8.7	1.3	-11.6	7.6	9.2
Sri Lanka	8.7	10.6	17.0	7.4	11.6	17.7	5.4	-14.0	13.1	8.0
Thailand	12.0	7.0	9.6	4.2	9.1	7.8	5.1	-12.6	9.4	5.8
Asia-ex China, India & Japan	9.6	10.1	15.1	8.8	10.0	8.8	4.5	-7.3	8.1	6.9
Asia-ex China & Japan	12.1	10.0	18.0	11.0	12.7	7.1	6.8	-6.1	10.0	7.7
Asia-ex Japan	14.4	18.7	23.7	18.4	17.9	14.6	9.0	-10.0	8.5	7.9
Asia	10.9	13.9	18.9	13.2	14.5	12.3	6.3	-15.2	9.4	7.7

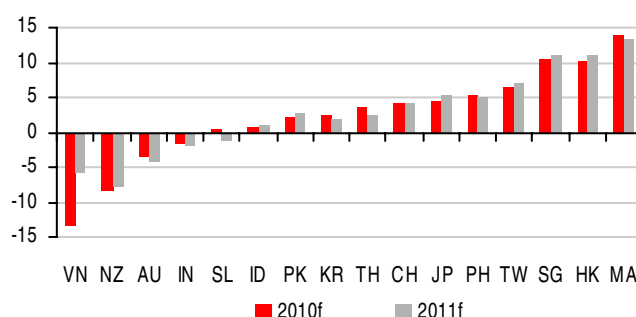
Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

Real exports (% yr): Back to positive growth across Asia in 2010



Source: HSBC, CEIC

Current account % GDP: First line of defence and not all negative



Source: HSBC, CEIC

Current account balance

(% of GDP)	2002	2003	2004	2005	2006	2007	2008	2009f	2010f	2011f
China	2.4	2.8	3.6	7.2	9.5	11.0	9.4	4.9	4.1	4.0
Hong Kong	8.3	9.2	8.9	12.4	11.4	10.8	10.9	9.7	10.3	11.1
Japan	2.9	3.2	3.7	3.7	3.9	4.9	3.2	2.8	4.3	5.1
Korea	1.0	2.0	4.1	1.9	0.6	0.6	-0.7	5.1	2.6	1.9
Taiwan	8.8	9.8	5.8	4.8	7.0	8.4	6.2	10.1	6.5	7.0
North Asia-ex Japan	3.2	3.8	4.2	6.0	7.3	8.6	7.7	5.4	4.2	4.1
Australia	-3.6	-5.2	-6.0	-5.6	-5.2	-6.1	-4.5	-3.6	-3.7	-4.1
India	1.5	1.6	0.1	-1.9	-1.1	-1.0	-3.1	-1.0	-1.6	-1.8
Indonesia	3.9	3.4	0.6	0.1	3.0	2.4	0.0	1.6	0.6	0.9
Malaysia	8.4	12.8	12.1	15.0	16.3	15.6	17.5	16.1	13.9	13.4
New Zealand	-3.8	-4.2	-6.2	-8.4	-8.6	-8.2	-8.8	-1.8	-8.5	-7.8
Pakistan	5.0	1.9	-1.4	-3.9	-4.8	-8.2	-5.1	0.7	2.0	2.7
Philippines	6.9	0.9	1.1	2.0	4.5	4.8	2.3	4.9	5.2	4.9
Singapore	17.7	31.0	26.4	27.5	25.4	23.5	14.8	10.8	10.3	10.9
Sri Lanka	-1.4	-0.7	-3.2	-2.7	-5.0	-4.0	-9.3	1.2	0.5	-1.2
Thailand	5.5	5.6	1.7	-4.3	1.1	6.6	0.6	8.3	3.5	2.5
Vietnam	-1.7	-4.9	-2.1	-1.1	-0.3	-9.8	-11.6	-7.6	-13.3	-5.9
Asia-ex China, India & Japan	5.3	6.1	5.2	4.1	4.6	4.7	2.8	6.2	4.2	4.3
Asia-ex China & Japan	4.4	5.1	4.0	2.6	3.2	3.2	1.2	4.2	2.6	2.6
Asia-ex Japan	3.6	4.2	3.8	4.5	5.9	6.7	5.3	4.5	3.4	3.3
Asia	3.2	3.7	3.8	4.1	5.1	6.0	4.5	3.9	3.7	4.0

Source: HSBC, CEIC; NB: Australia and New Zealand are not included in Asia aggregate and data are based on IMF nominal USD weights for the respective year, for which 2009, 2010 and 2011 use 2008 weights

Exchange rates & interest rates

Exchange rates

(vs USD, period end)	2006	2007	2008	2009				2010f			
				1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
Australia (AUD)	0.79	0.88	0.70	0.69	0.81	0.88	0.90	0.94	0.96	0.98	1.00
China (RMB)	7.81	7.30	6.82	6.83	6.82	6.83	6.83	6.80	6.80	6.73	6.66
Hong Kong (HKD)	7.77	7.80	7.75	7.75	7.75	7.80	7.80	7.80	7.80	7.80	7.80
India (INR)	44.3	39.4	48.7	50.7	47.9	48.1	46.5	48.0	47.5	47.0	46.5
Indonesia (IDR)	8,994	9,400	11,325	11,700	10,208	9,665	9,480	9,200	9,000	8,900	8,800
Japan (JPY)	118.9	112.0	90.7	99	96	90	95	100	100	105	105
Korea (KRW)	930	935	1,260	1,383	1,274	1,178	1,164	1,150	1,125	1,100	1,075
Malaysia (MYR)	3.53	3.31	3.45	3.65	3.52	3.46	3.44	3.50	3.50	3.48	3.46
New Zealand (NZD)	0.67	0.76	0.58	0.53	0.64	0.72	0.72	0.73	0.74	0.75	0.76
Pakistan (PKR)	60.9	61.5	79.0	80.5	81.4	83.2	84.4	92.0	92.0	92.0	92.0
Philippines (PHP)	49.0	41.2	47.4	48.4	48.1	47.6	46.1	45.5	45.0	44.5	43.5
Singapore (SGD)	1.53	1.44	1.44	1.52	1.45	1.41	1.40	1.40	1.38	1.36	1.34
Sri Lanka (LKR)	107.7	108.7	113.3	115.5	115.0	114.8	114.4	118.0	118.0	118.0	118.0
Taiwan (TWD)	32.6	32.4	32.8	33.9	32.8	32.2	31.5	31.0	30.0	29.5	29.0
Thailand (THB)	35.5	33.7	34.7	35.5	34.1	33.4	33.4	32.5	32.0	31.5	31.5
Vietnam (VND)	16,050	16,017	17,483	17,797	17,798	17,841	18,479	18,400	18,400	18,400	18,400

Source: HSBC, CEIC, Bloomberg Note: Thai baht forecasts are for onshore rate.

3-month interest rates

(% pa, period end)	2006	2007	2008	2009				2010f			
				1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
Australia	6.52	7.27	4.11	3.17	3.25	3.35	4.10	4.30	4.30	4.60	4.60
China	1.80	3.33	1.71	1.71	1.71	1.71	1.71	1.71	1.71	1.98	1.98
Hong Kong	3.90	3.45	0.95	0.90	0.36	0.22	0.14	0.10	0.20	0.20	0.40
India	8.24	8.01	8.45	7.07	4.35	4.26	4.18	5.00	5.25	5.75	6.25
Indonesia	9.50	7.83	11.98	8.61	7.05	7.00	6.90	6.75	7.15	7.55	8.05
Japan	0.55	0.40	0.40	0.35	0.35	0.28	0.28	0.28	0.28	0.28	0.28
Korea	4.76	5.73	4.68	2.45	2.41	2.64	2.82	2.45	2.45	2.95	3.20
Malaysia	3.71	3.61	3.37	2.11	2.13	2.14	2.27	2.10	2.10	2.35	2.60
New Zealand	7.70	8.90	5.12	3.38	2.85	2.82	2.81	3.10	3.40	3.70	3.70
Philippines	4.84	3.67	6.12	4.42	4.50	3.99	5.50	6.00	6.50	6.50	6.75
Singapore	3.44	2.38	0.96	0.67	0.69	0.68	0.68	0.60	0.70	0.70	0.80
Taiwan	1.76	2.16	1.01	0.41	0.41	0.41	0.53	1.35	1.50	1.70	1.85
Thailand	5.25	3.85	2.95	1.80	1.40	1.35	1.35	1.55	1.80	2.05	2.30

Source: HSBC, CEIC, Bloomberg

Country profiles

Australia

Still buying homes

The good run continues. Already, the Australian economy has elegantly side-stepped the global slump with a mixture of decisive policy action and the helpful exposure to fast-growing emerging economies. Now, the data points to further gains. Most impressively, house prices continue to power ahead, which should support both construction as well as consumption. As the fiscal stimulus fades, worries that this may dent the pace of recovery have so far not been substantiated.

This leaves the path open to further rate hikes. The Reserve Bank of Australia has taken the lead among large central banks and pushed rates up from their emergency low of 3%. As the economy gathers steam, and accelerating job creation points in that direction, more tightening seems likely.

But, as the policy rate climbs above 4%, the going may get tougher. Most importantly, massive household debt, which is for the most part financed at variable rates, may break the spurt in consumption spending that underpins the recovery. As the RBA found out over the past rate-cut cycle, monetary policy is exceedingly potent in Australia given the quick pass-through onto local purchasing power. But what holds on the way down, also holds on the way up.

Consumer confidence has already started to ease back, even if it remains in solid bullish territory. But perhaps more importantly, rate hikes are also giving wings to the Australian dollar, which itself helps to slow growth. As a result, Australia's central bank may proceed more cautiously in 2010 after its bold moves the previous year.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	2.3	1.0	0.7	0.4	0.5	1.8	1.9	2.2	2.9	3.3
Industrial production (% y-o-y)	3.2	0.2	-3.6	-4.8	-3.8	-1.0	1.0	2.0	2.0	3.0
CPI, end quarter (% y-o-y)	5.0	3.7	2.5	1.5	1.3	1.8	2.0	2.3	2.5	2.8
PPI, end quarter (% y-o-y)	5.6	6.4	4.0	2.1	2.1	2.4	2.7	3	3.4	3.2
Trade balance (% GDP)	4.0	8.1	10.1	-1.6	-1.8	-2.2	-2.0	-1.8	-2.3	-2.6
Current account (% GDP)	-3.8	-2.6	-1.8	-3.9	-5.5	-3.2	-3.5	-3.5	-3.8	-3.9
Policy rate, end quarter (%)	7.00	4.25	3.25	3.00	3.00	3.75	4.00	4.25	4.25	4.50
10yr yield, end quarter (%)	5.40	3.98	4.41	5.52	5.45	5.60	5.80	5.80	5.80	6.00
USD /AUD, end quarter	0.79	0.70	0.69	0.81	0.88	0.90	0.94	0.96	0.98	1.00
EUR /AUD, end quarter	0.53	0.53	0.53	0.59	0.62	0.60	0.63	0.64	0.65	0.67

Source: HSBC, CEIC

Australia: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	3.1	2.7	4.8	2.2	0.8	2.6	2.8
Nominal GDP (USDbn)	731.9	780.8	973.4	1,034.3	1,059.9	1,307.6	1,424.3
GDP per capita (USD)	35,628	37,406	45,832	47,789	48,664	59,304	63,816
Private consumption (% y-o-y)	3.0	3.2	4.4	2.6	2.1	3.9	3.2
Government consumption (% y-o-y)	2.2	3.6	3.3	3.3	2.3	2.3	1.4
Investment (% y-o-y)	8.8	4.6	9.6	8.3	-2.0	3.2	4.6
Industrial production (% y-o-y)	1.6	1.7	3.0	2.9	-3.3	2.0	3.0
Gross domestic saving (% GDP)	20.3	21.6	22.3	24.3	22.2	22.2	22.5
Unemployment rate, end-year (%)	5.1	4.8	4.4	4.2	5.6	5.3	4.8
Prices & wages							
CPI, average (% y-o-y)	2.7	3.5	2.3	4.3	1.8	2.8	3.0
CPI, end-year (% y-o-y)	2.8	3.3	3.0	3.7	2.0	2.8	3.0
PPI, end-year (% y-o-y)	3.4	3.9	2.6	5.4	2.7	3.1	3.5
Manufacturing wages, nominal (% y-o-y)	3.6	2.8	2.8	4.9	3.5	3.4	2.8
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	7.3	11.1	13.9	5.3	9.3	11.3	7.5
Broad money supply M3, average (% y-o-y)	8.6	11.0	18.1	18.6	13.8	15.5	13.5
Real private sector credit growth (% y-o-y)	13.4	14.3	17.2	7.7	5.2	6.7	7.8
Policy rate, end-year (%)	5.50	6.25	6.74	4.25	3.75	4.50	5.00
10yr yield, end-year (%)	5.34	5.58	5.99	5.82	5.25	5.85	6.15
USD /AUD, end-year	0.73	0.79	0.88	0.70	0.90	1.00	1.00
USD /AUD, average	0.76	0.75	0.85	0.84	0.82	0.97	1.00
EUR /AUD, end-year	0.62	0.61	0.61	0.53	0.60	0.67	0.67
EUR /AUD, average	0.61	0.60	0.62	0.57	0.58	0.65	0.67
External sector							
Merchandise exports (USDbn)	106.1	123.8	145.2	185.3	161.4	185.1	200.7
Merchandise imports (USDbn)	119.4	133.4	163.3	190.1	166.8	214.4	235.7
Trade balance (USDbn)	-13.3	-9.5	-18.1	-4.8	-5.4	-29.2	-35.0
Current account balance (USDbn)	-41.2	-40.7	-59.2	-47.1	-39.2	-48.1	-58.5
Current account balance (% GDP)	-5.6	-5.2	-6.1	-4.5	-3.6	-3.7	-4.1
Net FDI (USDbn)	7.0	6.0	30.0	11.3	-6.8	4.9	8.0
Net FDI (% GDP)	1.0	0.6	3.0	1.3	-0.7	0.4	0.6
Current account balance plus FDI (% GDP)	-4.6	-4.6	-3.1	-3.2	-4.3	-3.3	-3.6
Exports (% y-o-y)	18.1	18.4	2.9	31.7	-8.8	-2.6	5.3
Imports (% y-o-y)	10.4	13.1	7.2	19.7	-9.9	6.1	7.3
International FX reserves (USDbn)	52.3	64.3	58.5	38.9	49.8	N/A	N/A
Import cover (months)	5.3	5.8	4.3	2.5	3.6	N/A	N/A
Public and external solvency indicators							
Central government balance (% GDP)	1.7	1.9	1.8	1.0	-3.5	-3.0	-1.0
Gross external debt (AUDbn)	779	927	1,031	1,263	1,100	1,050	1,000
Gross public domestic debt AUDbn)	60.1	59.1	58.3	60.5	70.0	76.0	80.0
Gross public sector debt (% GDP)	6.2	5.6	5.1	4.9	8.0	10.0	11.0

Source: HSBC, CEIC

China

Unleashing consumer power

China's growth has rebounded strongly amid massive fiscal and monetary stimuli. This infrastructure-led recovery will likely be sustained into 2010, not least because the long-term railway and road projects won't fade overnight. We expect GDP growth to accelerate to 9.5% this year, from an estimated 8.5% in 2009. Continued investment in ongoing infrastructure projects, plus strong housing sales, implies that growth in fixed investment should stay above 20% this year. Meanwhile, the filtering through of second-round effects from the stimulus measures should continue to support growth in the industrial sector this year.

Inflation is likely to pick up, reflecting excessive monetary growth and demand recovery. But the pace of the acceleration in inflation should still be manageable this year considering that the recovery in global demand will be slow and there will still be excess capacity in the Chinese manufacturing sector. We do not expect any aggressive monetary tightening this year. Even if inflation picks up faster than expected, we believe that the most effective way to contain the

overheating risk is to slow the pace of new infrastructure projects.

With GDP growth exceeding the 8% target for 2009 and still accelerating, policymakers decided during the annual work conference to shift stimulus spending from new construction to education and healthcare in 2010. This should create more balanced growth in the coming year, with a greater contribution from consumer spending. The government has initiated healthcare reforms with RMB850bn of spending in the next three years. It has also committed to spend more on education and public housing in the coming years. We believe the jump in government spending on the social safety net, combined with surging consumer credit, will encourage consumers to loosen their purse-strings and lower their savings rate (currently 35%) by five percentage points over the next three years.

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	3Q08	4Q08	1Q09	1Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	9.0	6.8	6.1	7.9	8.9	10.2	9.7	9.5	9.3	9.4
Industrial production* (% y-o-y)	13.0	6.4	6.0	9.6	10.6	12.6	14.2	14.0	13.8	14.0
CPI, end quarter (% y-o-y)	4.6	1.2	-1.2	-1.7	-0.8	0.3	3.1	2.8	2.6	3.3
PPI, end quarter (% y-o-y)	9.1	-1.1	-6.0	-7.8	-7.0	3.5	2.5	3.0	3.5	4.0
Trade balance (% GDP)	7.9	7.4	6.5	1.7	3.3	4.4	4.7	1.0	5.6	3.2
International reserves (USDbn)	1,906	1,946	1,954	2,132	2,273	2,250	2,286	2,303	2,354	2,399
Policy rate, end quarter (%)	7.20	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.58	5.85
5yr lending rate, end quarter (%)	7.56	5.76	5.76	5.76	5.76	5.76	5.76	5.76	6.03	6.30
RMB/USD, end quarter	6.85	6.82	6.83	6.82	6.83	6.83	6.80	6.80	6.73	6.66
RMB/EUR, end quarter	9.73	9.48	9.02	9.55	9.97	9.77	10.20	10.20	10.10	9.99

* Industrial production is the output of companies with annual sales over RMB5m.
Source: HSBC, CEIC

China: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	10.2	11.6	13.0	9.6	8.5	9.5	8.9
Nominal GDP (USDbn)	2,239	2,661	3,386	4,524	4,946	5,603	6,468
GDP per capita (USD)	1,723	2,035	2,576	3,424	3,725	4,198	4,822
Nominal retail sales (% y-o-y)	12.9	13.7	16.8	21.6	15.0	17.0	16.8
Fixed Asset Investment (nominal, % y-o-y)	27.2	24.5	25.8	26.1	29.5	26.0	20.0
Industrial production (excl. small enterprises % y-o-y)	15.9	16.2	16.0	12.9	9.5	14.0	13.0
Gross domestic saving (% GDP)	48.2	50.1	51.0	51.4	50.0	50.5	50.0
Unemployment rate, average (%)	4.2	4.1	4.0	4.2	6.0	5.5	5.0
Prices & wages							
CPI, average (% y-o-y)	1.8	1.5	4.8	5.9	-0.9	2.6	2.5
CPI, end-year (% y-o-y)	1.6	2.8	6.5	1.2	0.3	3.3	2.3
PPI, end-year (% y-o-y)	3.2	3.1	5.4	-1.1	3.5	4.0	3.3
Manufacturing wages, nominal (% y-o-y)	12.3	14.0	16.2	17.0	9.0	13.0	11.5
Money, FX & interest rates							
Central bank money M0, average (%)	9.9	13.2	13.6	12.4	8.0	11.0	11.0
Broad money supply M2, average (%)	16.0	18.1	17.5	16.7	21.9	21.5	16.0
Policy rate, end-year (%)	5.58	6.12	7.47	5.31	5.31	5.85	5.85
5yr yield, end-year (%)	5.85	6.48	7.74	5.76	5.76	6.30	6.30
RMB /USD, end-year	8.07	7.81	7.30	6.82	6.83	6.66	6.40
RMB /USD, average	8.18	7.96	7.60	6.94	6.83	6.77	6.55
RMB /EUR, end-year	9.52	10.30	10.66	9.48	9.77	9.99	9.60
RMB /EUR, average	10.19	10.01	10.56	10.11	9.54	10.15	9.82
External sector							
Merchandise exports (USDbn)	762.0	969.0	1,219	1,429	1,258	1,371	1,508
Merchandise imports (USDbn)	660.0	791.5	956.0	1,133.1	1,009	1,160	1,265
Trade balance (USDbn)	102.0	177.5	262.7	295.5	248.8	210.7	243.2
Current account balance (USDbn)	161	253	372	426	240	230	260
Current account balance (% GDP)	7.2	9.5	11.0	9.4	4.9	4.1	4.0
Net FDI (USDbn)	72.4	72.7	83.5	108.3	85.0	86.0	98.9
Net FDI (% GDP)	3.2	2.7	2.5	2.4	1.7	1.5	1.5
Current account balance plus FDI (% GDP)	10.4	12.2	13.4	11.8	6.6	5.6	5.5
Exports (% y-o-y)	28.4	27.2	25.8	17.2	-12.0	9.0	10.0
Imports (% y-o-y)	17.6	19.9	20.8	18.5	-11.0	15.0	9.0
International FX reserves (USDbn)	818.9	1,066	1,528	1,946	2,250	2,400	2,550
Import cover (months)	13.8	15.0	17.7	18.9	26.1	25.3	25.8
Public and external solvency indicators							
Commercial banks' FX assets (USDbn)	169.3	200.3	188.4	180.9	211.6	245.4	291.8
Gross external debt (USDbn)	281.0	323.0	373.6	374.7	350.0	330.0	360.0
Short term external debt (% of int'l reserves)	19.1	17.2	14.4	10.8	6.7	5.0	5.1
Consolidated government balance (% GDP)	-1.2	-1.0	0.6	-0.4	-2.8	-3.3	-2.8

Note: Industrial production is the output of all industrial companies
Source: HSBC, CEIC

Hong Kong SAR

Domestic demand leads recovery

The recovery in domestic demand in Hong Kong is likely to be sustained into 2010. Private consumption rose sequentially in two quarters in a row. Meanwhile, private investment also had started to pick up in 3Q09 (8% q-o-q (sa)). This, plus strong PMI figures over the last four months, suggests business confidence is beginning to rise.

The expansion in business investment is likely to feed into the labour market. This, together with a number of the government's public projects to be released next year, suggests employment growth should bottom out in coming months. Although we still expect the jobless rate to rise after a temporary fall in October and November due to the return of 'discouraged workers' into the labour force, we now expect the jobless rate to peak at 5.3% in 1Q10 as against our previous estimate of 6.2%.

In addition, as loose monetary policy in the global economy is unlikely to reverse anytime soon, the influx of capital into Hong Kong will continue and should benefit local asset markets. This prolonged positive wealth effect and the increased job security will together allow local residents to increase their spending.

Exports have not yet shown a solid recovery. However, various economic data suggest the developed world is improving and thus will eventually stimulate external demand. We therefore maintain our positive estimate on export growth in 2010, which is also supported by a low base effect.

We still hold the view that GDP growth will recover to 3.8% y-o-y this year from an estimated -3.6% last year. Inflation, especially asset price inflation, will be a real risk this year given weakening dollar, ultra-low interest rates and capital inflows.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	1.5	-2.6	-7.8	-3.6	-2.4	-0.5	5.9	3.4	2.7	3.3
Industrial production (% y-o-y)	-7.0	-10.6	-10.2	-9.5	-8.6	-6.5	2.3	0.8	1.3	1.5
CPI, ave quarter (% y-o-y)	3.1	2.1	1.2	-0.9	0.5	2.1	1.8	3.1	4.1	1.6
PPI, end quarter (% y-o-y)	5.4	3.8	-1.4	-3.0	-2.0	-1.3	0.3	1.1	1.6	1.8
Trade balance (% GDP)	-9.6	-7.0	-9.1	-10.0	-15.6	-7.5	-9.3	-10.5	-15.9	-7.4
G&S balance (% GDP)	13.2	15.8	10.6	7.3	5.9	14.8	10.5	8.3	6.5	15.5
International reserves (USDbn)	160.6	182.5	186.3	207.0	226.9	255.8	263.0	253.0	250.0	247.0
Policy rate, end quarter (%)	3.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
5yr yield, end quarter (%)	2.57	1.19	1.62	2.07	1.73	1.93	1.65	1.50	1.50	1.50
HKD /USD, end quarter	7.80	7.80	7.75	7.75	7.80	7.80	7.80	7.80	7.80	7.80
HKD /EUR, end quarter	11.08	10.84	10.23	10.85	11.39	11.15	11.70	11.70	11.70	11.70

Source: HSBC, CEIC

HKSAR: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	7.1	7.0	6.4	2.4	-3.6	3.8	4.3
Nominal GDP (USDbn)	177.8	189.9	207.1	215.2	208.7	220.0	233.7
GDP per capita (USD)	25,629	25,630	25,630	25,631	28,924	29,770	30,743
Private consumption (% y-o-y)	3.0	5.9	8.5	1.7	-1.0	3.4	3.2
Government consumption (% y-o-y)	-3.2	0.2	3.0	1.8	2.1	1.5	2.0
Investment (% y-o-y)	4.1	7.1	3.4	0.0	-5.5	6.6	5.8
Industrial production (% y-o-y)	2.5	2.2	-1.5	-6.6	-8.7	1.5	2.3
Gross domestic saving (% GDP)	33.3	33.3	31.0	30.4	29.4	29.5	31.8
Unemployment rate, end-year (%)	5.2	4.4	3.4	4.1	5.1	5.3	4.9
Prices & wages							
CPI, average (% y-o-y)	0.9	2.0	2.0	4.3	0.7	2.7	3.0
CPI, end-year (% y-o-y)	1.4	2.3	3.8	2.1	2.1	1.6	3.2
PPI, end-year (% y-o-y)	1.0	2.1	4.2	3.8	-1.3	1.8	1.9
Overall wages, nominal (% y-o-y)	2.6	1.3	0.3	3.7	1.0	3.3	3.5
Money, FX & interest rates							
Central bank money M1, average (% y-o-y)	1.2	11.9	17.8	4.6	30.0	15.0	10.0
Broad money supply M3, average (% y-o-y)	7.4	12.7	18.4	7.0	7.7	27.0	15.8
Real private sector credit growth (% y-o-y)	6.9	6.9	13.2	12.5	-2.7	11.1	12.1
Policy rate, end-year (%)	5.75	6.75	5.75	0.50	0.50	0.50	1.50
5yr yield, end-year (%)	4.11	3.69	3.10	1.19	1.93	1.50	2.10
HKD /USD, end-year	7.75	7.77	7.80	7.75	7.80	7.80	7.80
HKD /USD, average	7.77	7.77	7.80	7.78	7.78	7.80	7.80
HKD /EUR, end-year	9.14	10.26	11.39	10.77	11.15	11.70	11.70
HKD /EUR, average	9.68	9.76	10.84	11.33	10.87	11.70	11.70
External sector							
Merchandise exports (USDbn)	288.7	316.3	346.0	364.6	316.3	343.4	374.3
Merchandise imports (USDbn)	296.3	330.3	365.7	387.7	338.4	367.1	399.2
Trade balance (USDbn)	-7.6	-14.0	-19.7	-23.1	-22.1	-23.7	-24.8
G & S balance (USDbn)	22.1	21.7	22.4	23.5	20.3	22.6	25.8
G & S balance (% GDP)	12.4	11.4	10.8	10.9	9.7	10.3	11.1
Net FDI (USDbn)	6.4	0.1	-6.7	3.1	-2.0	8.0	10.0
Net FDI (% GDP)	3.6	0.0	-3.3	1.4	-1.0	3.6	4.3
G & S balance plus FDI (% GDP)	16.0	11.4	7.6	12.3	8.8	13.9	15.3
Exports (% y-o-y)	11.1	9.6	9.4	5.4	-13.4	8.8	9.0
Imports (% y-o-y)	10.1	11.5	10.7	6.0	-12.9	8.7	8.7
International FX reserves (USDbn)	124.3	133.2	152.7	182.5	255.8	247.0	230.0
Import cover (months)	5.0	4.8	5.0	5.6	9.1	8.1	6.9
Public and external solvency indicators							
Commercial banks' FX assets (USDbn)	531.4	603.9	789.1	864.0	870.0	900.0	950.0
Gross external debt (USDbn)	43.0	52.0	83.0	47.6	40.0	45.0	50.0
Consolidated government balance (% GDP)	1.0	4.0	7.7	0.1	0.1	0.0	2.6

Note: Public debt refers to government debt only
Source: HSBC, CEIC

India

Recovery on track

Post the Lehman failure in September 2008, India's policymakers responded swiftly – the central bank cutting interest rates by 425bps while the government announced fiscal stimulus measures totalling 2.2% of GDP (USD24bn) in the previous fiscal year and increased spending by 36% y-o-y (USD212bn) in its 2009-10 budget.

The combined benefits of these measures are still flowing into the economy as witnessed by the impressive GDP growth figure posted in 2Q FY10 – 7.9% vs. 6.1% in 1Q FY10.

The biggest downside risk concerns the potential impact from the drought, which by some measures is the worst in several decades. Our own analysis shows that weaker consumption by India's rurally dependant population, as a result of the drought, could reduce GDP growth by at least 0.8%.

A substantial part of the additional spend from the budget is, however, being targeted at the rural sector, particularly via income-protecting schemes such as the rural employment guarantee scheme. These

measures will help support farm incomes to some extent, although some hit is almost inevitable.

Industrial production is likely to level off at an 8-10% rate before dropping back somewhat in 2010 as the inventory build subsides. In our view, the lagged effects from the monetary policy easing will spur spending, which in turn bodes well for the services sector.

Surprisingly, droughts in the past have typically had little influence on consumer price inflation, perhaps reflecting the various measures taken by the government to mitigate the adverse impact on poorer consumers. We expect the RBI to start tightening monetary policy with a reserve requirement hike in January and rate hike cycles beginning March 2010.

Overall, we have revised upwards our 2009/10 GDP growth forecast to 7.2% from 6.2% considering the significant spurt in consumer spending and the surprisingly early return of fixed capital investment. Our 8.5% projection for 2010/11 remains unchanged.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	7.7	5.8	5.8	6.1	7.9	7.7	7.2	7.9	7.1	9.1
Industrial production (% y-o-y)	4.7	0.8	0.5	3.8	9.2	11.0	9.0	7.0	6.8	7.3
CPI, end quarter (% y-o-y)	9.8	9.7	8.0	9.3	11.6	12.2	12.0	9.8	7.5	6.5
WPI, end quarter (% y-o-y)	12.3	6.1	1.2	-1.0	0.5	6.0	8.0	7.2	6.8	6.3
Trade balance (% GDP)	-14.4	-12.0	-5.3	-9.4	-9.7	-8.5	-5.1	-9.9	-10.7	-9.4
Current account (% GDP)	-4.6	-4.5	1.7	-2.1	-1.8	-1.8	1.8	-2.9	-3.4	-2.1
International reserves (USDbn)	277.3	246.6	241.4	254.1	271.2	287.6	318.5	332.4	345.8	361.0
Policy rate, end quarter (%)	9.00	6.50	5.00	4.75	4.75	4.75	5.00	5.25	5.75	6.25
5yr yield, end quarter (%)	8.58	5.35	6.65	6.50	7.03	7.26	7.21	7.50	7.25	7.00
INR /USD, end quarter	47.0	48.7	50.7	47.9	48.1	46.5	48.0	47.5	47.0	46.5
INR /EUR, end quarter	66.7	67.7	66.9	67.1	70.2	66.5	72.0	71.3	70.5	69.8

Source: HSBC, CEIC

Note: Data pertain to fiscal year, e.g. 2005 numbers are for FY05/06 (April 05 – March 06)

India: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	9.5	9.7	9.0	6.7	7.2	8.5	8.3
Nominal GDP (USDbn)	784.7	877.3	1,115	1,175	1,175	1,381	1,638
GDP per capita (USD)	690.2	762.7	949.5	976	889	895	915
Private consumption (% y-o-y)	7.1	6.3	8.5	2.9	3.5	8.0	7.7
Government consumption (% y-o-y)	6.2	5.5	7.4	20.2	15.0	3.0	3.0
Investment (% y-o-y)	17.6	14.5	12.9	8.2	8.0	14.0	12.3
Industrial production (% y-o-y)	8.2	11.5	8.5	2.6	6.1	7.5	6.5
Gross domestic saving (% GDP)	35.1	37.0	38.1	36.3	40.0	39.0	39.5
Prices							
CPI, average (% y-o-y)	4.0	6.3	6.4	8.3	10.5	9.6	6.0
CPI, end-year (% y-o-y)	5.3	6.7	5.5	9.7	12.2	6.5	6.4
WPI, average (% y-o-y)	4.5	4.8	4.8	9.1	1.9	7.1	5.4
WPI, end-year (% y-o-y)	4.4	5.7	3.8	6.1	6.0	6.3	5.0
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	14.7	17.3	15.0	18.9	16.2	18.0	17.0
Broad money supply M3, average (% y-o-y)	16.1	19.6	21.8	20.4	19.6	20.0	19.0
Real private sector credit growth (% y-o-y)	19.9	18.4	15.6	14.0	6.8	12.0	15.0
Policy rate, end-year (%)	6.75	7.75	7.75	6.50	4.75	6.25	7.00
5yr yield, end-year (%)	6.66	7.52	7.67	5.35	7.26	7.00	7.00
INR /USD, end-year	45.1	44.3	39.4	48.7	46.5	46.5	44.5
INR /USD, average	44.1	45.2	40.9	44.7	48.3	47.3	45.5
INR /EUR, end-year	53.1	58.4	57.5	67.7	66.5	69.8	66.8
INR /EUR, average	54.9	56.8	56.8	65.1	67.5	70.9	68.3
External sector							
Merchandise exports (USDbn)	102.2	123.8	149.3	192.6	167.6	187.9	209.6
Merchandise imports (USDbn)	149.4	184.9	231.0	320.2	265.0	309.5	350.7
Trade balance (USDbn)	-47.3	-61.2	-81.7	-127.6	-97.4	-121.6	-141.1
Current account balance (USDbn)	-14.7	-9.3	-11.3	-36.2	-12.2	-22.8	-28.9
Current account balance (% GDP)	-1.9	-1.1	-1.0	-3.1	-1.0	-1.6	-1.8
Net FDI (USDbn)	4.6	6.0	7.8	22.8	17.5	23.0	18.0
Net FDI (% GDP)	0.6	0.7	0.7	1.9	1.5	1.7	1.1
Current account balance plus FDI (% GDP)	-1.3	-0.4	-0.3	-1.1	0.5	0.0	-0.7
Exports (% y-o-y)	31.1	21.1	20.6	29.0	-13.0	12.1	11.6
Imports (% y-o-y)	41.0	23.8	24.9	38.6	-17.2	16.8	13.3
International FX reserves (USDbn)	131.0	170.2	266.6	246.6	287.6	361.0	430.3
Import cover (months)	10.5	11.0	13.8	9.2	13.0	14.0	14.7
Public and external solvency indicators							
Commercial banks' FX assets (USDbn)	162.8	209.5	324.3	265.4	270.0	300.0	320.0
Gross external debt (USDbn)	138.1	172.4	224.4	224.6	235.0	250.0	270.0
Short term external debt (% of int'l reserves)	6.6	7.0	16.4	19.5	13.9	12.2	11.6
Consolidated government balance (% GDP)	-9.3	-7.0	-6.5	-9.8	-11.5	-10.0	-8.5
Central government balance (% GDP)	-4.2	-3.6	-2.8	-6.3	-6.9	-5.8	-4.9
Primary balance (% GDP)	-0.7	-0.1	-0.1	-3.0	-4.5	-3.5	-2.5

Note: Data pertain to fiscal year, e.g. 2005 numbers are for FY05/06 (April 2005–March 2006)
Source: Central Statistical Organisation, Reserve Bank of India, Bloomberg, CEIC and HSBC

Indonesia

All change?

The resilience of the Indonesian economy during the recent global recession and the re-election of the Yudhoyono government with an unprecedented mandate for reform have sparked huge interest in the country and its markets.

Having had a relatively shallow downturn (GDP growth has bottomed at 4.0% in 2Q09) Indonesia's upturn will continue to be less impressive than most in the region. But we still expect it to record above-consensus growth of 5.8% next year. It will also do so while maintaining a comparatively low budget deficit and a modest current account surplus.

We put the country's trend growth rate at about 5%, although it has the potential to do a lot better than that. Indonesia enjoys sizeable commodity resources, a huge domestic market and excellent demographics, for example.

If this potential is to be unlocked, the pace of economic reform will need to be stepped up significantly. President Yudhoyono's first terms

saw some progress made on corruption, as well as the introduction of an Investment Law, designed to level the playing field for foreign investment, and a Tax Law, involving a reduction in the top rate of corporate tax to 25%, amongst other things.

But much remains to be done. Indonesia is 111th out of 180 countries in the Corruption Perception Index, 122nd out of 183 countries in the World Bank's Ease of Doing Business survey and 54th out of 133 countries in the World Economic Forum's Global Competitive Index.

Given a more comfortable position in parliament than before, progress should be easier for the government. But with hopes so high we now believe there is greater risk of disappointment than pleasant surprise. In particular, significant labour market reforms and allowing foreign investment in many key sectors are likely to remain off-limits.

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	3Q08	4Q08	1Q09	1Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	6.4	5.2	4.4	4.0	4.2	4.7	5.4	5.8	6.0	5.8
Industrial production (% y-o-y)	4.3	1.8	1.5	1.5	1.3	2.5	5.0	6.0	7.0	7.0
CPI, end quarter (% y-o-y)	12.1	11.1	7.9	3.7	2.8	2.8	6.5	7.0	8.0	8.0
PPI, end quarter (% y-o-y)	27.5	9.7	4.9	-5.9	-3.3	10.0	12.0	15.0	12.0	10.0
Trade balance (% GDP)	4.1	3.4	6.1	6.7	5.3	4.2	4.5	5.1	4.3	3.2
Current account (% GDP)	-0.7	-0.5	2.4	2.3	1.2	0.6	0.5	1.4	0.9	-0.4
International reserves (USDbn)	57.1	51.6	54.8	57.6	62.3	63.6	63.9	65.8	67.1	65.8
Policy rate, end quarter (%)	9.25	9.25	7.75	7.00	6.50	6.50	6.50	7.00	7.50	8.00
5yr yield, end quarter (%)	13.01	11.80	11.69	10.00	9.00	9.00	8.76	7.50	7.25	7.00
IDR/USD, end quarter	9,506	11,325	11,700	10,208	9,665	9,480	9,200	9,000	8,900	8,800
IDR/EUR, end quarter	13,499	15,742	15,444	14,291	14,111	13,556	13,800	13,500	13,350	13,200

Source: HSBC, CEIC

Indonesia: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	5.7	5.5	6.3	6.1	4.3	5.8	5.5
Nominal GDP (USDbn)	285.6	364.4	432.0	517.4	523.9	683.4	791.2
GDP per capita (USD)	1,300	1,635	1,914	2,264	2,225	2,874	3,293
Private consumption (% y-o-y)	4.0	3.2	5.0	5.3	5.1	5.4	4.9
Government consumption (% y-o-y)	6.6	9.6	3.9	10.4	12.0	2.8	2.3
Investment (% y-o-y)	10.9	2.6	9.4	11.7	3.8	8.7	7.4
Industrial production (% y-o-y)	4.6	4.6	4.7	3.7	1.7	6.3	4.7
Gross domestic saving (% GDP)	27.5	28.7	28.1	30.6	29.4	29.9	30.4
Unemployment rate, end-year (%)	11.2	10.3	9.1	8.4	8.6	8.2	8.5
Prices & wages							
CPI, average (% y-o-y)	10.5	13.1	6.4	10.2	4.8	6.8	7.0
CPI, end-year (% y-o-y)	17.1	6.6	6.6	11.1	2.8	8.0	6.4
WPI, end-year (% y-o-y)	24.4	6.6	21.9	9.7	10.0	10.0	8.0
Manufacturing wages, nominal (% y-o-y)	8.5	6.3	4.8	8.5	6.0	7.5	8.5
Money, FX & interest rates							
Broad money supply M2, average (% y-o-y)	12.4	15.5	15.9	16.1	16.0	15.0	17.0
Real private sector credit growth (% y-o-y)	18.9	1.1	15.0	19.6	9.5	8.0	12.0
Policy rate, end-year (% y-o-y)	12.75	9.75	8.00	9.25	6.50	8.00	8.00
5yr yield, end-year (%)	13.31	9.43	9.22	11.80	9.00	7.00	7.00
IDR /USD, end-year	9,830	8,994	9,400	11,325	9,480	8,800	8,800
IDR /USD, average	9,705	9,166	9,143	9,575	10,494	9,060	8,800
IDR /EUR, end-year	11,595	11,871	13,724	15,742	13,556	13,200	13,200
IDR /EUR, average	12,083	11,519	12,708	13,944	14,665	13,590	13,200
External sector							
Merchandise exports (USDbn)	87.0	103.5	118.0	139.6	114.5	124.2	135.4
Merchandise imports (USDbn)	69.5	73.9	85.3	116.7	85.3	95.1	104.8
Trade balance (USDbn)	17.5	29.7	32.8	22.9	29.2	29.1	30.6
Current account balance (USDbn)	0.3	10.9	10.5	0.1	8.2	4.2	7.0
Current account balance (% GDP)	0.1	3.0	2.4	0.0	1.6	0.6	0.9
Net FDI (USDbn)	5.3	2.2	2.3	3.4	1.5	3.0	3.5
Net FDI (% GDP)	1.8	0.6	0.5	0.7	0.3	0.4	0.4
Current account balance plus FDI (% GDP)	1.9	3.6	3.0	0.7	1.9	1.1	1.3
Exports (% y-o-y)	22.9	19.0	14.0	18.3	-18.0	8.5	9.0
Imports (% y-o-y)	37.2	6.3	15.4	36.9	-26.9	11.4	10.2
International FX reserves (USDbn)	34.7	42.6	56.9	51.6	63.6	65.8	72.0
Import cover (months)	6.0	6.9	8.0	5.3	8.9	8.3	8.3
Public and external solvency indicators							
Gross external debt (USDbn)	130.7	128.7	136.6	149.1	145.8	147.8	152.0
Short term external debt (% of int'l reserves)	53.9	47.0	50.2	53.8	40.9	42.5	41.6
Private sector external debt (USDbn)	50.6	52.9	56.0	62.6	59.8	60.8	62.0
Central government balance (% GDP)	-0.5	-0.9	-1.3	-0.1	-2.4	-1.7	-1.0
Primary balance (% GDP)	1.8	1.5	0.8	1.7	-0.5	-0.2	0.5
Gross public domestic debt (IDRtrn)	1270.0	1302.2	1385.0	1448.3	1580.2	1685.5	1755.1
Gross public domestic debt (% GDP)	45.2	39.7	34.1	24.7	31.8	28.0	25.2
Gross public external debt (USDbn)	80.1	75.8	80.6	86.6	86.0	87.0	90.0
Gross public external debt (% GDP)	28.0	20.8	18.7	16.7	16.4	12.7	11.4
Gross public sector debt (% GDP)	73.3	60.5	52.8	41.5	42.0	40.8	36.6

Source: HSBC, CEIC

Japan

Slow recovery to continue

We have raised our forecast for real GDP growth in 2009 to -5.2% from -5.7%, mainly to reflect the revisions of past data. We have slightly revised our 2010 and 2011 forecasts. The Japanese economy will move into a cyclical lull in 1H10, due mainly to the waning of fiscal stimulus effects and restocking of inventories, but a double dip should be avoided as sizable additional stimulus measures (including the US and China) are already scheduled in 2010 and exports to rapidly developing Asian countries are expected to remain firm.

Japan will remain burdened with a large negative output gap throughout the forecast period, forcing companies, especially manufacturers, to cut capital investments and personnel costs. Unemployment looks set to stay around 5.5% and employees' income to contract y-o-y throughout the forecast period. Thus, capex and private consumption, which account for about 70% of real GDP, will not drive growth, so the recovery will be basically very moderate.

The initial budget plan for FY10 was decided in late December, which was almost in line with the manifesto of the DPJ at the previous general election last summer, except for gasoline taxes, which will be maintained at current rates due mainly to the historical shortage of revenues.

The large negative output gap will be a persistent source of downward pressure on prices. We project core CPI deflation to continue through 2011.

A rate hike by the Bank of Japan is unlikely until at least 2011. Rather, there remains some possibility that the BoJ will have to take additional easing measures. In the case of yen appreciation, the BoJ will probably extend the duration of special fund supplying operations to 6 months from the current 3 months, to encourage further flattening of the yield curve. And the BoJ may clarify the target levels of term interest rates along with the current overnight call rates, especially in the event that double-dip recession risks strengthen.

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	3Q08	4Q08	1Q09	1Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	-1.4	-4.1	-8.9	-5.8	-5.1	-1.7	1.3	0.8	0.9	0.9
Industrial production (% y-o-y)	-1.4	-14.5	-34.6	-27.8	-21.4	-5.0	24.3	14.2	6.0	2.3
CPI, end quarter (% y-o-y)	2.2	1.0	0.0	-1.0	-2.3	-1.6	-1.0	-1.4	-1.3	-1.3
Dom. CGPI, end quarter (% y-o-y)	7.3	2.6	-1.8	-5.4	-8.3	-4.8	-1.8	-1.6	-1.7	-1.6
Trade balance (% GDP)	-0.1	-0.5	0.4	1.0	0.6	1.7	1.3	1.8	3.2	2.5
Current account (% GDP)	3.0	1.7	2.3	2.6	2.5	3.4	3.4	3.8	5.3	4.5
International reserves (USDbn)	1032.0	1030.6	1060.0	1090.0	1110.0	1,115	1,130	1,150	1,175	1,200
Policy rate, end quarter (%)	0.5	0.1	0.1	0.1	0.1	0.10	0.10	0.10	0.10	0.10
10-yr yield, end quarter (%)	1.5	1.3	1.3	1.4	1.3	1.3	1.1	1.2	1.2	1.3
JPY/USD, end quarter	106	91	99	96	90	93	100	100	105	105
JPY/EUR, end quarter	151	126	131	134	131	133	150	150	158	158

Source: HSBC, CEIC

Japan: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	1.9	2.0	2.4	-1.2	-5.2	1.0	1.2
Nominal GDP (USDbn)	4,555	4,376	4,385	4,659	4,875	4,608	4,644
GDP per capita (USD)	36,090	34,686	34,775	39,262	36,920	35,333	35,500
Private consumption (% y-o-y)	1.3	1.5	1.6	-0.7	-0.9	1.4	1.3
Government consumption (% y-o-y)	1.6	0.4	1.5	0.3	1.4	0.8	-1.6
Investment (% y-o-y)	3.1	0.5	-1.2	-2.6	-14.0	-5.2	-1.9
Industrial production (% y-o-y)	1.1	4.8	2.8	-3.2	-22.7	11.0	5.1
Gross domestic saving (% GDP)	26.2	27.1	26.5	26.0	26.0	25.5	24.5
Unemployment rate, end-year (%)	4.4	4.1	3.9	4.0	5.1	5.5	5.5
Prices & wages							
CPI, average (% y-o-y)	-0.3	0.2	0.0	1.5	-1.2	-1.2	-0.8
CPI, end-year (% y-o-y)	0.2	0.1	0.4	1.0	-1.6	-1.3	-0.6
Domestic CGPI, average (% y-o-y)	1.7	2.2	1.8	4.6	-5.1	-1.6	-1.0
Total wages, nominal (% y-o-y)	0.6	0.2	-1.0	-0.3	-4.5	-1.5	-1.0
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	2.0	-13.3	-7.8	0.1	5.8	3.0	2.0
Broad money supply M2+CDs, average (% y-o-y)	1.8	1.0	1.6	2.1	2.7	2.9	2.5
Policy rate, end-year (%)	0.00	0.26	0.50	0.10	0.10	0.10	0.10
10yr yield, average (%)	1.4	1.8	1.7	1.5	1.3	1.2	1.3
JPY /USD, end-year	118	119	112	91	95	105	105
JPY /USD, average	112	117	117	91	95	105	105
JPY /EUR, end-year	139	157	164	126	136	158	158
JPY /EUR, average	140	147	163	133	133	158	158
External sector							
Merchandise exports (USDbn)	593.8	645.9	712.6	780.7	547.7	578.8	622.7
Merchandise imports (USDbn)	516.1	579.0	622.1	762.9	499.8	475.3	478.4
Trade balance (USDbn)	77.7	66.9	90.5	17.8	47.9	103.4	144.3
Current account balance (USDbn)	166.6	172.6	213.2	157.3	137.9	198.7	239.5
Current account balance (% GDP)	3.7	3.9	4.9	3.2	2.8	4.3	5.1
Net FDI (USDbn)	-43.0	-56.8	-53.9	-103.6	-106.0	-61.9	-50.0
Net FDI (% GDP)	-0.9	-1.3	-1.2	-2.2	-2.2	-1.3	-1.1
Current account balance plus FDI (% GDP)	2.7	2.6	3.6	0.9	0.7	3.0	4.1
Exports (% y-o-y)	7.5	14.8	11.6	-3.5	-32.9	11.9	7.6
Imports (% y-o-y)	15.7	18.3	8.6	8.0	-37.3	0.8	0.7
International FX reserves (USDbn)	834.3	879.7	952.8	1,030.6	1,060	1,100	1,150
Import cover (months)	38.8	36.5	36.8	32.4	50.9	55.5	57.7
Public and external solvency indicators							
Commercial banks' FX assets (USDbn)	1,369	1,523	1,783	1,850	1,900	1,950	1,950
Gross external debt (USDbn)	1,281	1,243	1,402	1,250	1,200	1,220	1,220
Private sector external debt (USDbn)	973.8	824.1	818.7	900.0	900	900	900
General government balance (% GDP)	-6.1	-1.0	-1.4	-3.5	-10.5	-10.5	-10.0
Primary balance (% GDP)	-4.1	-2.9	-2.8	-2.0	-8.2	-8.2	-7.7
Gross public domestic debt (JPYtm)	930.9	964.8	990	1,066	1,105	1,140	1,140
Gross public domestic debt (% GDP)	181.9	188.0	192.7	251.5	238.6	235.6	233.8
Gross public external debt (USDbn)	307.3	418.8	583.8	350.0	300.0	320.0	320.0
Gross public external debt (% GDP)	6.7	9.6	13.3	7.5	6.2	6.9	6.9
Gross public sector debt (% GDP)	188.7	197.6	206.0	259.0	244.8	242.6	240.7

Note: Public debt refers to government debt only
Source: HSBC, CIEC

Korea

Strong all round

Korea is on a run. Growth rebounded with such vigour over the course of 2009 that the economy edge out a slight expansion for the full year, after earlier predictions of an unprecedented recession. Exports, helped by a hugely competitive currency, continue to barrel ahead, driven of late by rising demand from China in particular. This looks set to last: Korean shipments are sensitive to the global inventory cycle, and, with stocks extremely lean across the board, more orders should be coming in.

But, the real surprise in Korea wasn't the rebound in exports. Rather, domestic demand, especially household consumption, bounced back nicely. With the labour market defying earlier predictions of soaring job cuts, income growth continues to support spending. Consumer confidence, meanwhile, is hovering near multi-year highs. As a result, 2010 is shaping up to be a strong year for Korea, both externally and domestically.

This will likely prompt the Bank of Korea to raise interest rates, especially if the housing market, which cooled slightly into year-end, bounces back

again. For the first quarter, we now expect 25bp in rate hikes, reflecting in part the unease among officials about keeping interest rates at record lows, but the second quarter may see a temporary hold, before tightening resumes over the second half. In fact, we believe inflation should remain well-behaved over the coming year.

The bullish outlook, however, should not distract from the more fundamental challenges that Korea is facing. First, the economy has to withstand the withdrawal of the fiscal stimulus. Especially the construction industry, which takes up a big chunk of the country's GDP and still relies on the public contracts. Second, and more long term, labour market reforms need to be tackled to sustain private investment in the manufacturing sector. Third, household debt is high and rising. This needs to be addressed. With this in mind, be prepared for a cool-down of growth into 2011.

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	3Q08	4Q08	1Q09	1Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	3.1	-3.4	-4.2	-2.2	0.9	6.8	5.2	7.3	5.3	3.3
Industrial production (% y-o-y)	5.6	-11.3	-15.5	-6.2	4.3	6.0	12.0	7.0	4.0	2.0
CPI, end quarter (% y-o-y)	5.1	4.1	3.9	2.0	2.2	2.8	3.5	3.5	3.5	3.0
PPI, end quarter (% y-o-y)	11.3	5.6	3.5	-3.1	-2.6	0.7	1.4	3.5	3.0	3.6
Trade balance (% GDP)	-1.4	2.2	4.6	8.9	6.6	4.8	2.9	4.9	4.5	3.2
Current account (% GDP)	-3.6	3.7	4.8	6.6	4.7	4.3	1.8	3.3	2.5	2.5
International reserves (USDbn)	239.7	201.2	206.3	231.7	254.2	277.2	282.1	291.5	299.0	306.9
Policy rate, end quarter (%)	5.25	3.00	2.00	2.00	2.00	2.00	2.25	2.25	2.75	3.00
5yr yield, end quarter (%)	5.77	4.25	3.78	3.86	4.34	4.32	5.00	4.75	4.50	4.75
KRW /USD, end quarter	1,207	1,260	1,383	1,274	1,178	1,164	1,150	1,125	1,100	1,075
KRW /EUR, end quarter	1,714	1,751	1,826	1,783	1,720	1,665	1,725	1,688	1,650	1,613

Source: HSBC, CEIC

Korea: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	4.0	5.2	5.1	2.2	0.4	5.2	4.8
Nominal GDP (USDbn)	790.8	890.1	970.9	943.6	839	1,022	1,175
GDP per capita (USD)	16,428	18,430	20,036	19,415	17,210	20,932	24,027
Private consumption (% y-o-y)	4.6	4.7	5.1	0.9	0.1	3.9	4.9
Government consumption (% y-o-y)	4.3	6.6	5.4	4.2	4.7	0.5	3.3
Investment (% y-o-y)	1.9	3.4	4.2	-1.7	-1.0	4.9	5.1
Industrial production (% y-o-y)	6.3	8.4	6.9	3.1	-3.1	6.0	6.6
Gross domestic saving (% GDP)	33.2	31.5	30.8	37.6	38.9	42.0	43.7
Unemployment rate, end-year (%)	3.5	3.3	3.1	3.3	3.2	3.0	3.0
Prices & wages							
CPI, average (% y-o-y)	2.8	2.2	2.5	4.7	2.8	3.3	3.0
CPI, end-year (% y-o-y)	2.6	2.1	3.6	4.1	2.8	3.0	3.2
PPI, end-year (% y-o-y)	1.5	0.3	3.6	5.6	0.7	3.6	2.6
Manufacturing wages, nominal (% y-o-y)	7.8	5.6	6.9	3.7	2.3	4.3	5.5
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	2.7	6.4	18.1	7.5	25.0	5.6	9.0
Broad money supply M3, average (% y-o-y)	7.0	8.2	10.3	11.6	8.0	9.0	11.0
Real private sector credit growth (% y-o-y)	5.8	11.7	12.4	9.4	4.2	4.7	5.0
Policy rate, end-year (%)	3.75	4.50	5.00	3.00	2.00	3.00	4.00
5yr yield, end-year (%)	5.04	4.82	5.65	4.25	4.32	4.75	5.60
KRW /USD, end-year	1,008	930	935	1,260	1,164	1,075	1,050
KRW /USD, average	1,025	953	928	1,085	1,262	1,124	1,053
KRW /EUR, end-year	1,189	1,228	1,365	1,751	1,665	1,613	1,575
KRW /EUR, average	1,276	1,197	1,290	1,580	1,763	1,685	1,580
External sector							
Merchandise exports (USDbn)	289.0	331.8	379.0	433.4	370.0	404.7	438.6
Merchandise imports (USDbn)	256.3	303.9	350.9	427.4	317.5	364.5	401.3
Trade balance (USDbn)	32.7	27.9	28.2	6.0	52.5	40.2	37.3
Current account balance (USDbn)	15.0	5.4	5.9	-6.4	42.9	26.2	22.0
Current account balance (% GDP)	1.9	0.6	0.6	-0.7	5.1	2.6	1.9
Net FDI (USDbn)	2.0	-4.5	-13.8	-15.6	-5.4	-4.0	-4.0
Net FDI (% GDP)	0.3	-0.5	-1.4	-1.7	-0.6	-0.4	-0.3
Current account balance plus FDI (% GDP)	2.1	0.1	-0.8	-2.3	4.5	2.2	1.5
Exports (% y-o-y)	12.1	14.8	14.2	14.3	-14.6	9.4	8.4
Imports (% y-o-y)	16.4	18.6	15.4	21.8	-25.7	14.8	10.1
International FX reserves (USDbn)	210.4	239.0	262.2	201.2	276.9	306.8	332.4
Import cover (months)	9.9	9.4	9.0	5.6	10.5	10.1	9.9
Public and external solvency indicators							
Gross external debt (USDbn)	187.9	260.1	383.2	377.9	350.0	335.0	330.0
Short term external debt (% of int'l reserves)	31.3	47.6	61.1	74.5	56.9	43.7	39.7
Private sector external debt (USDbn)	172.3	240.2	329.5	325.6	242.9	212.0	192.3
Central government balance (% GDP)	0.4	0.4	3.8	1.2	-5.0	-2.5	-1.9
Primary balance (% GDP)	1.7	1.9	5.2	2.6	-3.4	-0.9	-0.3
Gross public domestic debt (KRWbn)	227,055	262,369	278,790	288,720	358,479	411,951	461,008
Gross public domestic debt (% GDP)	28.0	30.9	30.9	28.2	33.9	35.9	37.2
Gross public external debt (USDbn)	15.5	19.9	53.6	52.4	107.1	123.0	137.7
Gross public external debt (% GDP)	2.0	2.2	5.5	5.5	12.8	12.0	11.7
Gross public sector debt (% GDP)	29.5	32.2	32.1	31.4	35.7	37.8	39.2

Source: HSBC, CEIC

Malaysia

Structural change continues

The Malaysian economy has bounced back with a vengeance over the last couple of quarters, with GDP rising an estimated 4% in 2Q on a seasonally adjusted, quarter-on-quarter basis and a further 3.1% in 3Q. Since 1Q, therefore, the level of GDP is up over 7% and has recovered all but 1.2% of the loss in output during the recession.

The question now is whether the recovery will continue and, if so, at what pace? We remain optimistic and are sticking with our 6.8% GDP growth forecast for 2010. This is well above that of the consensus as well as the government's ultra-conservative 2-3% range.

Consumer confidence has snapped back and is consistent with 8% private consumption growth, no doubt buoyed by supportive policy conditions and high palm oil/rubber prices. Government infrastructure projects are coming on-stream, while private sector CAPEX will return in due course partly as a result of the lagged effects of lower interest rates. Export growth should also trend

higher as the regional/global trade cycle continues to gather momentum.

Even so, Bank Negara is unlikely to deliver the first rate hike until around the middle of next year. By that time the deflation that Malaysia is currently experiencing will probably have turned to inflation of around 3%. The government is planning to cut the budget deficit from an expected 8.5% of GDP in 2009 to 5.6% in 2010. This largely reflects a 14% drop in operational expenditure and comes despite a 1% point reduction in the top income tax rate to 26%.

More importantly, the budget signalled the government's intention to reduce its involvement in the economy and encourage a greater role for the private sector. Inevitably there will be huge scepticism that such measures will be delivered but, bearing in mind earlier moves to liberalise large parts of the service sector, the Prime Minister is at least trying to take the economy in a different direction. We hope and expect further measures to be forthcoming.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q09e	2Q09e	3Q09e	4Q09e
GDP (% y-o-y)	4.8	0.1	-6.2	-3.9	-1.2	3.3	10.1	7.4	5.0	5.0
Industrial production (% y-o-y)	1.8	-8.8	-17.9	-14.5	-8.6	2.0	4.0	7.0	9.0	10.0
CPI, end quarter (% y-o-y)	8.2	4.4	3.5	-1.4	-2.0	1.5	3.1	3.5	3.4	2.7
PPI, end quarter (% y-o-y)	8.7	-3.4	-8.9	-12.2	-9.6	3.5	6.5	7.5	6.5	11.5
Trade balance (% GDP)	25.1	21.9	23.8	20.6	19.3	18.6	18.4	19.3	18.2	17.1
Current account (% GDP)	19.5	16.7	20.2	17.8	14.6	12.5	13.9	16.5	14.8	10.8
International reserves (USDbn)	97.8	91.6	87.9	91.7	96.6	93.5	94.7	98.8	103.1	101.3
Policy rate, end quarter (%)	3.50	3.25	2.00	2.00	2.00	2.00	2.00	2.00	2.25	2.50
5yr yield, end quarter (%)	4.06	3.00	3.49	3.90	3.74	3.79	3.84	3.80	4.00	4.20
MYR/USD, end quarter	3.44	3.45	3.65	3.52	3.46	3.44	3.50	3.50	3.48	3.46
MYR/EUR, end quarter	4.88	4.80	4.82	4.93	5.05	4.92	4.48	4.48	4.45	4.43

Source: HSBC, CEIC

Malaysia: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	5.3	5.8	6.2	4.6	-2.0	6.8	5.5
Nominal GDP (USDbn)	137.9	156.3	186.3	222.5	191.2	212.5	233.0
GDP per capita (USD)	5,002	5,581	6,857	8,025	6,755	7,360	7,909
Private consumption (% y-o-y)	9.1	6.8	10.4	8.5	2.1	5.7	5.0
Government consumption (% y-o-y)	6.5	5.0	6.5	10.9	3.9	1.0	1.0
Investment (% y-o-y)	5.0	7.5	9.6	0.8	-8.0	4.1	7.0
Industrial production (% y-o-y)	5.2	6.7	3.1	1.4	-9.8	7.5	6.5
Gross domestic saving (% GDP)	43.5	43.4	46.1	49.1	42.8	45.5	47.5
Unemployment rate, end-year (%)	3.8	3.0	3.0	3.1	3.6	3.4	3.2
Prices & wages							
CPI, average (% y-o-y)	3.0	3.6	2.0	5.4	0.7	3.3	2.5
CPI, end-year (% y-o-y)	3.3	3.1	2.4	4.4	1.5	2.7	2.5
PPI, end-year (% y-o-y)	9.9	4.9	10.8	-3.4	3.5	11.5	2.0
Manufacturing wages, nominal (% y-o-y)	3.9	10.1	7.3	0.5	-5.0	2.0	4.0
Money, FX & interest rates							
Central bank money M0, end-year (% y-o-y)	5.1	10.6	9.8	7.2	8.0	10.0	8.0
Broad money supply M3, average (% y-o-y)	11.7	8.6	12.7	12.5	7.3	11.3	13.0
Real private sector credit growth (% y-o-y)	5.8	4.2	6.1	4.9	7.0	6.0	5.0
Policy rate, end-year (%)	3.00	3.50	3.50	3.25	2.00	2.50	2.75
5yr yield, end-year (%)	3.73	3.76	3.78	3.00	3.79	4.20	4.20
MYR /USD, end-year	3.78	3.53	3.31	3.45	3.44	3.46	3.42
MYR /USD, average	3.79	3.67	3.43	3.32	3.52	3.48	3.43
MYR /EUR, end-year	4.46	4.66	4.83	4.80	4.92	5.19	5.13
MYR /EUR, average	4.72	4.62	4.77	4.83	4.92	5.22	5.15
External sector							
Merchandise exports (USDbn)	142.3	160.6	176.5	200.1	156.2	171.1	190.0
Merchandise imports (USDbn)	108.3	123.2	139.3	148.7	117.1	132.3	149.1
Trade balance (USDbn)	34.0	37.4	37.2	51.4	39.1	38.7	40.9
Current account balance (USDbn)	20.7	25.4	29.2	39.0	30.8	29.6	31.1
Current account balance (% GDP)	15.0	16.3	15.6	17.5	16.1	13.9	13.4
Net FDI (USDbn)	1.0	0.0	-2.7	-7.8	-4.4	0.6	2.3
Net FDI (% GDP)	0.7	0.0	-1.4	-3.5	-2.3	0.3	1.0
Current account balance plus FDI (% GDP)	15.7	16.3	14.2	14.0	13.8	14.2	14.4
Exports (% y-o-y)	11.9	9.4	2.7	9.6	-17.3	8.4	9.4
Imports (% y-o-y)	8.9	10.3	5.6	3.2	-16.6	11.9	11.0
International FX reserves (USDbn)	76.8	82.3	88.6	92.2	93.5	101.3	115.3
Import cover (months)	8.5	8.0	7.6	7.4	9.6	9.2	9.3
Public and external solvency indicators							
Gross external debt (USDbn)	53.1	56.0	55.8	54.3	52.0	53.0	55.0
Short term external debt (% of int'l reserves)	15.1	16.2	14.6	17.1	12.8	12.8	12.1
Private sector external debt (USDbn)	29.1	31.0	29.8	27.3	27.0	24.0	28.0
Central government balance (% GDP)	-3.6	-3.3	-3.2	-4.8	-8.5	-5.8	-4.0
Primary balance (% GDP)	-1.4	-1.2	-2.2	-3.5	-7.5	-4.0	-2.0
Gross public domestic debt (MYRbn)	198.7	217.2	247.1	286.1	300.0	340.0	360.0
Gross public domestic debt (% GDP)	38.0	37.8	38.6	38.7	44.6	45.9	45.1
Gross public external debt (USDbn)	24.0	25.0	26.0	27.0	25.0	29.0	27.0
Gross public external debt (% GDP)	17.4	16.0	14.0	12.1	13.1	13.6	11.6
Gross public sector debt (% GDP)	55.4	53.8	52.6	50.9	57.7	59.6	56.6

Source: HSBC, CEIC

New Zealand

Turning a corner

For all the evident macroeconomic imbalances, including a bloated current account deficit, negative household savings rates, and a stretched fiscal purse, New Zealand's economy has turned a corner, and far more quickly than anticipated. High frequency data suggest that output has bounced back in the last few months, reflected not least in climbing business confidence.

After a steep slump over the past years, the housing sector continues to recover, with sales up strongly over the year and house prices even pushing into further positive territory. This should provide some boost to household spending in the coming months. The debt servicing burden of households also keeps falling, reflecting both rock-bottom interest rates as well as an absolute decline in the level of debt that consumers carry.

But challenges remain. The unemployment rate, for example, continues to push higher, which will restrain the rebound in consumer spending that emerged in the past few months. This complicates the job of the Reserve Bank of New Zealand. The policy rate may need to go up over the course of 2010, not least to prevent another surge in consumer debt, and to encourage greater savings among households to rectify one of the most glaring structural economic imbalances. But, a rise in the policy rate could also push up the debt servicing burden of consumers and undermine the fragile recovery.

Fortunately, inflation pressures should remain relatively muted, given the persistent output gap and the relative strength of the currency. This allows the RBNZ to stay relatively relaxed about the timing and pace of rate hikes.

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	3Q08	4Q08	1Q09	1Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	-1.2	-2.1	-1.7	-1.0	-0.7	1.7	2.9	2.4	2.1	1.1
Industrial production (% y-o-y)	-0.9	-7.2	-11.0	-10.0	-8.1	-2.0	4.0	5.0	3.0	3.0
CPI, end quarter (% y-o-y)	5.1	3.4	3.0	1.9	1.7	1.9	2.0	2.2	2.3	2.4
PPI, end quarter (% y-o-y)	9.8	9.9	6.5	2.1	2.1	-1.8	1.2	2.0	2.5	2.8
Trade balance (% GDP)	-3.0	-0.7	1.0	-0.7	-0.7	0.6	1.5	-0.9	-1.4	0.4
Current account (% GDP)	-6.1	-4.0	-0.7	0.1	0.1	-4.2	-6.6	-6.7	-9.9	-10.4
Policy rate, end quarter (%)	7.50	5.00	3.00	2.50	3.50	2.50	2.50	2.75	3.00	3.25
10yr yield, end quarter (%)	5.65	4.62	5.34	5.96	5.60	6.10	5.80	6.10	6.20	6.20
USD /NZD, end quarter	0.71	0.58	0.53	0.64	0.72	0.72	0.73	0.74	0.75	0.76
EUR /NZD, end quarter	0.48	0.44	0.41	0.47	0.49	0.48	0.49	0.49	0.50	0.51

Source: HSBC, CEIC

New Zealand: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	3.1	2.3	3.3	-0.7	-0.4	2.1	3.1
Nominal GDP (USDbn)	109.6	106.3	129.1	127.8	116.9	134.3	137.0
GDP per capita (USD)	26,426	25,315	30,444	29,854	27,241	31,048	31,442
Private consumption (% y-o-y)	4.7	2.2	3.9	-0.3	-0.9	0.9	3.5
Government consumption (% y-o-y)	3.9	5.3	4.1	4.8	1.1	0.3	1.8
Investment (% y-o-y)	5.2	-1.0	5.5	-2.7	-13.7	-1.4	2.3
Industrial production (% y-o-y)	0.5	-3.7	1.3	-0.8	-7.8	3.8	4.1
Gross domestic saving (% GDP)	16.5	14.9	15.8	14.3	12.0	13.1	14.1
Unemployment rate, end-year (%)	3.8	3.8	3.7	4.2	6.1	6.3	5.7
Prices & wages							
CPI, average (% y-o-y)	3.0	3.4	2.4	3.9	2.1	2.2	2.6
CPI, end-year (% y-o-y)	3.1	2.6	3.2	3.4	1.9	2.4	2.8
PPI, end-year (% y-o-y)	3.7	4.1	4.0	9.9	-1.8	2.8	3.4
Manufacturing wages, nominal (% y-o-y)	2.8	3.2	3.2	3.6	3.1	3.4	2.8
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	-0.2	1.9	0.5	2.6	-0.2	1.6	1.3
Broad money supply M3, average (% y-o-y)	8.0	12.8	10.2	6.8	4.2	5.8	5.3
Real private sector credit growth (% y-o-y)	10.9	10.5	13.4	9.7	2.3	2.8	4.0
Policy rate, end-year (%)	7.25	7.25	8.25	5.00	2.50	3.25	4.25
10yr yield, end-year (%)	5.67	5.94	6.38	4.62	6.10	6.20	6.40
USD /NZD, end-year	0.69	0.67	0.76	0.58	0.72	0.76	0.76
USD /NZD, average	0.70	0.65	0.74	0.71	0.65	0.75	0.76
EUR /NZD, end-year	0.58	0.52	0.53	0.44	0.48	0.51	0.51
EUR /NZD, average	0.57	0.52	0.54	0.48	0.46	0.50	0.51
External sector							
Merchandise exports (USDbn)	7.3	7.8	9.3	10.0	9.4	11.1	11.5
Merchandise imports (USDbn)	8.7	8.5	10.1	11.3	9.6	11.2	11.6
Trade balance (USDbn)	-1.4	-0.7	-0.7	-1.3	-0.1	-0.1	-0.1
Current account balance (USDbn)	-9.2	-9.1	-10.6	-11.3	-2.1	-11.4	-10.6
Current account balance (% GDP)	-8.4	-8.6	-8.2	-8.8	-1.8	-8.5	-7.8
Exports (% y-o-y)	2.1	15.4	6.3	11.8	-3.9	2.8	5.3
Imports (% y-o-y)	2.5	5.6	5.0	16.1	-4.1	3.7	6.9
International FX reserves (USDbn)	18.8	29.5	29.1	33.3	27.4	N/A	N/A
Import cover (months)	26.0	41.9	34.7	35.5	34.4	N/A	N/A
Public and external solvency indicators							
Central government balance (% GDP)	4.7	4.6	3.7	3.0	-1.4	-3.2	-3.0
Gross external debt (NZDbn)	168.4	191.0	216.4	249.7	N/A	N/A	N/A
Gross public domestic debt (NZDmn)	34,233	28,928	30,405	31,627	38,008	44,168	50,232
Gross public sector debt (% GDP)	22.0	17.7	17.4	17.6	20.3	22.9	24.9

Source: HSBC, CEIC

Pakistan

A long, long road

Pakistan's economy has finally stabilized. The trade deficit is starting to fall and inflation is cooling. This has allowed the central bank to relax its stance and cut interest rates. But more work needs to be done. Tax revenue growth, for example, has slowed again over the second half of 2009 while the government faces expenditure pressures in light of escalating security risks.

One lingering concern is that non-performing assets in the banking system continue to climb. While so far this does not appear to carry systemic implications, it may at the margin restrain credit growth and thus blunt the effect of a falling policy rate on investment. Other structural bottlenecks are also weighing on capital spending, including the chronic shortage of energy, which is still leading to periodic blackouts in key industrial centres.

This highlights one of the key risks for the economy over the coming years. Massive public infrastructure investments are needed to revive the economy and sustain growth. However, funds for

such endeavours remain scarce. Taken together, these factors mean that the government will likely continue to run large budget deficits, which can only partly be financed with increased foreign aid inflows, both military and civilian.

In recent years, the structural budget shortfall was also financed to a large extent by privatization, an avenue that now appears difficult to sustain with the economic upheaval in the Middle East and political turmoil at home. Another earlier funding option that has recently dried up is direct central bank financing: under pressure from the IMF, the practice was severely curtailed this year – for the best over the long term, but it creates the risk of a near-term funding squeeze.

All this points to the need for further economic adjustment in the country. While the trade deficit has started to fall, the country still requires nearly USD1bn in monthly financing, either via remittances or via capital inflows. Pakistan's dependence on foreign financing is not likely to disappear anytime soon.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10e	2Q10e	3Q10e	4Q10e
Industrial production (% y-o-y)	-5.6	-3.3	-12.1	-10.0	4.0	4.0	5.0	5.0	5.0	6.0
CPI, end quarter (% y-o-y)	23.9	23.3	19.1	13.1	10.1	8.0	8.0	8.0	8.0	8.0
WPI, end quarter (% y-o-y)	30.6	33.2	17.6	11.1	4.1	7.0	6.0	8.0	9.0	9.0
M2 growth (% y-o-y)	13.4	8.7	9.0	9.6	10.7	10.0	10.0	10.0	7.0	7.0
Trade balance (USDbn)	-5.6	-4.0	-3.1	-4.3	-3.1	-2.9	-3.0	-4.4	-3.1	-2.8
Remittances (USDbn)	1.9	1.8	2.0	2.2	2.3	2.1	2.4	2.4	2.6	2.4
International reserves (USDbn)	8.2	10.0	10.5	12.4	14.8	10.1	10.6	12.5	15.0	10.2
Policy rate, end quarter (%)	13.00	15.00	15.00	14.00	13.00	13.00	10.00	9.00	9.00	9.00
2 yr yield, end quarter (%)	13.30	14.88	12.25	12.13	12.33	12.43	9.80	8.80	8.80	8.80
PKR /USD, end quarter	78.1	79.1	80.5	81.4	83.2	84.4	92.0	92.0	92.0	92.0
PKR /EUR, end quarter	111.0	110.0	106.3	114.0	121.4	120.7	138.0	138.0	138.0	138.0

Source: HSBC, CEIC
Note: Data pertain to fiscal year, eg. 2005 numbers are for FY05/06 (April 2005–March 2006)

Pakistan: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	6.2	5.7	2.0	3.7	0.8	2.6	3.7
Nominal GDP (USDbn)	128.0	143.8	169.3	184.5	174.0	170.3	185.2
GDP per capita (USD)	816.2	901.3	1,042.5	1,126.7	1,059	1,034	1,121
Private consumption (% y-o-y)	1.0	4.7	-1.3	5.2	1.0	2.0	3.5
Government consumption (% y-o-y)	48.3	-9.6	39.0	-13.5	4.0	3.0	3.0
Investment (% y-o-y)	19.9	13.6	3.8	-6.5	3.0	4.0	4.0
Industrial production (% y-o-y)	14.9	10.7	5.5	-0.3	-4.2	5.2	5.5
Gross domestic saving (% GDP)	13.9	14.3	11.2	12.5	18.3	19.7	20.5
Unemployment rate, end-year (%)	6.2	5.2	5.2	8.0	8.0	7.0	7.0
Prices							
CPI, average (% y-o-y)	9.1	7.9	7.6	20.3	13.4	7.7	7.6
CPI, end-year (% y-o-y)	8.5	8.9	8.8	23.3	8.0	8.0	7.0
WPI, average (% y-o-y)	8.7	8.5	8.2	25.3	6.9	6.4	8.6
WPI, end-year (% y-o-y)	11.0	8.0	12.1	17.6	7.0	9.0	8.0
Money, FX & interest rates							
Central bank money M1, end (% y-o-y)	17.0	74.9	24.4	11.5	10.0	8.0	8.0
Broad money supply M2, end (% y-o-y)	17.2	14.7	20.0	8.7	10.0	7.0	7.0
Real private sector credit growth (% y-o-y)	18.8	9.7	7.6	-7.3	2.1	0.0	1.0
Policy rate, end-year (%)	9.00	9.50	10.00	15.00	13.00	9.00	10.00
2 yr yield, end-year (%)	8.75	9.50	9.58	14.88	12.43	8.80	9.80
PKR /USD, end-year	59.8	60.9	61.5	79.0	84.4	92.0	92.0
PKR /USD, average	59.6	60.3	60.8	71.0	81.9	91.1	92.0
PKR /EUR, end-year	70.5	80.4	89.8	109.8	120.7	138.0	138.0
PKR /EUR, average	74.2	75.8	84.5	103.4	114.5	136.6	138.0
External sector							
Merchandise exports (USDbn)	15.9	16.8	17.2	19.9	17.4	18.4	19.8
Merchandise imports (USDbn)	17.8	25.3	29.8	32.6	42.1	30.8	31.6
Trade balance (USDbn)	-1.9	-8.5	-12.6	-12.7	-24.7	-12.4	-11.8
Current account balance (USDbn)	-5.0	-6.9	-13.9	-9.3	1.3	3.4	5.1
Current account balance (% GDP)	-3.9	-4.8	-8.2	-5.1	0.7	2.0	2.7
Net FDI (USDbn)	3.5	5.0	5.3	3.7	3.0	3.0	3.0
Net FDI (% GDP)	2.7	3.5	3.2	2.0	1.7	1.8	1.6
Current account balance plus FDI (% GDP)	-1.2	-1.3	-5.0	-3.1	2.4	3.8	4.4
Exports (% y-o-y)	14.2	5.4	12.1	-3.7	-12.6	5.6	8.0
Imports (% y-o-y)	29.6	6.3	28.7	-13.7	-27.0	2.8	6.0
International FX reserves (USDbn)	11.7	12.9	15.6	10.0	10.1	10.2	10.3
Import cover (months)	7.9	6.1	6.3	3.7	2.9	4.0	3.9
Public and external solvency indicators							
Commercial banks' FX assets (USDbn)	2.4	2.3	2.2	3.3	3.4	3.5	3.6
Gross external debt (USDbn)	35.9	39.0	44.5	51.1	56.3	60.2	64.4
Short term external debt (% of int'l reserves)	1.4	0.2	4.6	7.7	8.4	8.9	9.4
Private sector external debt (USDbn)	1.6	2.3	2.9	2.3	2.5	2.6	2.8
Consolidated government balance (% GDP)	-4.3	-3.7	-7.6	-5.2	-6.3	-5.6	-4.6
Gross public domestic debt (PKRbn)	233.7	261.0	322.7	392.9	442.1	489.6	532.4
Gross public domestic debt (% GDP)	30.7	30.1	31.4	30.0	31.0	31.6	31.3
Gross public external debt (USDbn)	35.9	39.0	44.5	46.6	51.5	55.8	59.6
Gross public external debt (% GDP)	28.0	27.1	26.3	25.2	29.6	32.7	32.2
Gross public sector debt (% GDP)	64.2	58.7	57.2	57.6	55.2	60.6	64.3

Note: Fiscal and national accounts data pertain to fiscal year, eg. 2005 numbers are for FY05/06 (July 2005–June 2006)
Source: Central Statistical Organisation, Reserve Bank of India, Bloomberg, CEIC and HSBC

Philippines

Lots more red ink

After riding the wave of higher public spending in 2Q09, growth in the Philippines buckled again, pointing to a rather bumpy road to recovery in the coming months. In seasonally adjusted terms, economic growth decelerated to 1% q-o-q in 3Q09 from 1.7% in 2Q09, while annual growth remained unchanged at 0.8%. A crucial harbinger of the current state of the economy is fragile exports, which is projected to contract 21% in 2009 and may recover only gradually given sluggish consumer demand in the West.

Had the weakness been limited to exports, the impact on the overall recovery would have been modest. But large excess capacity continues to dent investment. Moreover, the recovery faces stiff headwinds after the country was slammed by back-to-back typhoons, causing massive damage of USD4.4 billion (2.7% of GDP). This has also led to a slight downward revision in our 2009 GDP forecast to 1.1%.

Against this backdrop, public spending is bound to rise. Yet, at the same time, structural bottlenecks and a weak economy have caused a massive shortfall in revenues. As a result, the budget deficit widened sharply in 2009 and may push higher still in 2010, breaching 4% of GDP in both years. The risk for this year, in particular, is political turnover may stall revenue reforms and prevent more aggressive belt tightening. Still, monetary policy will remain expansionary for a while, with a tentative rate hike expected only in the second quarter.

But it's not all discouraging. Remittances have been growing at a robust pace, boosting private consumption. Given strong deployment statistics, and widespread geographical and skill-set diversification, remittances will continue to mark steady growth. In fact, leading indicators such as motor vehicle sales and business confidence have finally started to improve. In a nutshell, the Philippine economy is expected to turn around in 2010, even though gradually, growing at 4.2%.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10ef	3Q10e	4Q10ef
GDP (% y-o-y)	4.6	2.9	0.6	0.8	0.8	2.0	5.3	7.8	0.6	3.0
Industrial production (% y-o-y)	5.4	3.4	-7.6	-7.4	-7.6	2.0	1.0	1.0	2.0	2.0
CPI, end quarter (% y-o-y)	11.8	8.0	6.4	1.5	0.7	4.4	4.5	5.3	5.7	5.8
PPI, end quarter (% y-o-y)	6.5	7.3	0.4	-1.4	-3.6	3.0	3.0	3.5	3.7	4.8
Trade balance (% GDP)	-10.4	-5.0	-5.8	-6.4	-4.9	-7.6	-6.1	-6.9	-5.7	-8.0
Current account (% GDP)	-1.1	4.9	5.6	5.6	5.2	3.4	6.7	5.6	6.8	2.5
International reserves (USDbn)	36.6	37.4	38.9	39.4	42.4	42.6	44.4	47.3	50.7	52.5
Policy rate, end quarter (%)	6.00	5.50	4.75	4.25	4.00	4.00	4.00	4.25	4.50	4.75
10yr yield, end quarter (%)	8.05	7.25	7.85	8.00	7.90	7.88	8.04	8.20	8.50	8.50
PHP /USD, end quarter	47.1	47.4	48.4	48.1	47.6	46.1	45.5	45.0	44.5	43.5
PHP /EUR, end quarter	66.9	65.9	63.9	67.3	69.5	65.9	68.3	67.5	66.8	65.3

Source: HSBC, CEIC

Philippines: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	5.0	5.3	7.1	3.8	1.1	4.2	4.6
Nominal GDP (USDbn)	99.0	117.6	147.1	167.1	160.6	185.2	214.5
GDP per capita (USD)	1,171	1,375	1,700	1,909	1,802	2,042	2,300
Private consumption (% y-o-y)	4.8	5.5	5.8	4.7	3.6	4.7	5.2
Government consumption (% y-o-y)	2.3	10.4	6.6	3.2	8.5	8.7	6.4
Investment (% y-o-y)	-6.6	3.9	10.9	2.9	-3.8	5.6	5.9
Industrial production (% y-o-y)	5.3	4.2	3.3	4.3	-4.9	1.5	1.5
Gross domestic saving (% GDP)	21.0	20.1	20.8	19.2	9.8	11.3	10.0
Unemployment rate, end-year* (%)	8.1	7.8	7.4	7.7	7.5	7.6	7.1
Prices & wages							
CPI, average (% y-o-y)	7.7	6.3	2.8	9.3	3.3	5.2	5.6
CPI, end-year (% y-o-y)	6.7	4.3	3.9	8.0	4.4	5.8	5.9
PPI, end-year (% y-o-y)	12.1	3.7	-3.0	7.3	3.0	4.8	0.9
Manufacturing wages, nominal** (% y-o-y)	8.5	7.9	4.5	5.3	3.8	4.5	5.5
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	11.5	20.7	35.1	17.2	8.9	5.5	7.0
Broad money supply M3, average (% y-o-y)	7.0	13.8	17.1	14.2	12.6	9.0	8.0
Real private sector credit growth (% y-o-y)	-4.0	-2.3	2.7	10.0	9.0	2.6	2.4
Policy rate, end-year (%)	7.50	7.50	5.25	5.50	4.00	4.75	5.50
10yr yield, end-year (%)	10.19	6.38	6.37	7.25	7.88	8.50	8.50
PHP /USD, end-year	53.1	49.0	41.2	47.4	46.1	43.5	42.5
PHP /USD, average	55.0	51.3	45.2	44.4	47.7	45.0	42.9
PHP /EUR, end-year	62.6	64.7	60.2	65.9	65.9	65.3	63.8
PHP /EUR, average	68.4	64.4	62.8	64.7	66.7	67.4	64.3
External sector							
Merchandise exports (USDbn)	40.3	46.5	49.5	48.3	36.5	38.7	42.6
Merchandise imports (USDbn)	48.0	53.3	57.9	61.1	46.6	51.2	57.9
Trade balance (USDbn)	-7.8	-6.7	-8.4	-12.9	-10.0	-12.5	-15.3
Current account balance (USDbn)	2.0	5.3	7.1	3.9	7.8	9.7	10.4
Current account balance (% GDP)	2.0	4.5	4.8	2.3	4.9	5.2	4.9
Net FDI (USDbn)	1.7	2.8	-0.6	1.1	1.1	1.4	1.9
Net FDI (% GDP)	1.7	2.4	-0.4	0.7	0.7	0.8	0.9
Current account balance plus FDI (% GDP)	3.7	6.9	4.4	3.0	5.5	6.0	5.8
Exports (% y-o-y)	3.8	15.6	6.4	-2.5	-24.3	6.0	10.1
Imports (% y-o-y)	8.0	10.9	8.7	5.6	-23.8	10.0	13.1
International FX reserves (USDbn)	18.4	22.8	33.6	36.5	42.6	52.5	55.6
Import cover (months)	4.6	5.1	7.0	7.2	11.0	12.3	11.5
Public and external solvency indicators							
Commercial banks' FX assets (USDbn)	11.8	14.8	15.9	17.7	18.2	20.2	22.5
Gross external debt (USDbn)	54.2	53.4	54.9	53.9	52.0	50.0	50.0
Short term external debt (% of int'l reserves)	34.8	21.9	21.1	19.2	14.7	11.4	10.8
Private sector external debt (USDbn)	22.8	20.3	21.5	13.2	13.9	6.6	2.0
Consolidated government balance (% GDP)	-1.8	0.2	0.3	-0.9	-4.0	-4.4	-3.2
Central government balance (% GDP)	-2.7	-1.1	-0.2	-0.9	-4.0	-4.4	-3.2
Primary balance (% GDP)	2.8	4.1	3.8	2.7	-0.4	-1.0	0.2
Gross public domestic debt (PHPbn)	2,164	2,154	2,201	2,414	2,614	2,808	2,960
Gross public domestic debt (% GDP)	39.8	35.7	33.1	32.5	34.1	33.7	32.2
Gross public external debt (USDbn)	31.4	33.1	33.5	40.7	38.1	43.4	48.0
Gross public external debt (% GDP)	31.7	28.1	22.7	24.3	23.7	23.5	22.4
Gross public sector debt (% GDP)	71.4	63.9	55.8	56.9	57.9	57.2	54.6

Note: * Sep 2005, the ILO definition of unemployment has been adopted by official sources; **refers to minimum wage index
Source: HSBC, CEIC

Singapore

Recovery remains

Singapore has swung from huge recession to remarkable recovery and back to GDP contraction again in the space of the last 12 months. While 4Q08 and 1Q09 saw the biggest-ever absolute decline in GDP over a six-month period (of 7.4%), the following six months witnessed the biggest-ever rise (of 8.6%), before GDP fell 1.7% in 4Q09. The net result has been to leave the level of real GDP 3.7% below its high in 1Q08.

So how worried should we be about the return to contraction at the end of last year? In our view, not very much. The key point is that virtually all of the weakness reflected a renewed collapse in the highly volatile pharmaceuticals sector, which should prove short-lived. In 2010 as a whole, we expect GDP growth to top the government's 3-5% forecast range, coming in at 6.5%.

The highly trade-dependent nature of the economy, which left Singapore so exposed to the collapse in global trade in late 2008/early 2009, should once again become its advantage. Meanwhile, the launch of the two Integrated

Resorts and the expansion of the pharmaceuticals sector could provide new impetus to activity in 2010. Wealth effects and domestic policy conditions remain very helpful to growth and we doubt the government will be heading rapidly towards the exit in its February budget. It has, however, demonstrated its willingness to counter sharp property price moves by introducing a couple of measures to take some heat out of the market, where private residential prices rose an astonishing 15.9% in 3Q relative to 2Q.

CPI inflation has also experienced a roller-coaster ride in the last 18 months, soaring to a multi-decade high of 8% in mid-2008 before slipping into negative territory in recent months. We expect a return to positive inflation in December and a year average rate of 2.9% in 2010, reflecting the impact of higher commodity prices and the annual housing revaluation in January.

We have pencilled in a move back to a policy of "modest and gradual" currency appreciation at the April Monetary Authority of Singapore meeting but it is a low conviction call right now.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	0.0	-4.2	-9.5	-3.3	0.6	3.7	10.0	5.6	5.1	5.7
Industrial production (% y-o-y)	-10.9	-10.7	-23.7	-0.5	7.9	5.0	12.0	10.0	8.0	7.5
CPI, end quarter (% y-o-y)	6.7	4.3	1.6	-0.5	-0.4	0.3	2.2	3.2	3.0	3.1
PPI, end quarter (% y-o-y)	9.1	-11.2	-16.3	-18.6	-16.8	1.0	5.0	8.0	6.0	4.0
Trade balance (% GDP)	19.8	10.9	14.6	19.3	20.8	9.0	9.4	18.3	19.1	7.8
Current account (% GDP)	17.1	10.4	12.2	14.0	13.0	4.7	6.4	16.3	16.6	2.4
International reserves (USDbn)	169.4	173.9	166.5	173.0	181.7	183.1	184.0	192.3	201.4	203.5
3M interbank rate, end-quarter (%)	1.85	0.96	0.67	0.69	0.68	0.68	0.60	0.70	0.70	0.80
5yr yield, end-quarter (%)	2.40	1.40	1.42	1.45	1.43	1.28	1.30	1.35	1.00	1.00
SGD /USD, end-quarter	1.43	1.44	1.52	1.45	1.41	1.40	1.40	1.38	1.36	1.34
SGD /EUR, end-quarter	2.03	2.00	2.01	2.03	2.06	2.00	2.10	2.07	2.04	2.01

Source: HSBC, CEIC

Singapore: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	8.7	8.4	7.8	1.1	-2.2	6.5	5.5
Nominal GDP (USDbn)	120.8	139.7	167.5	184.0	173.3	199.6	222.7
GDP per capita (USD)	28,324	31,743	36,503	38,014	35,629	39,785	41,740
Private consumption (% y-o-y)	3.1	4.0	5.2	2.4	-1.2	4.4	3.2
Government consumption (% y-o-y)	9.6	6.6	2.2	8.1	2.5	2.9	0.0
Investment (% y-o-y)	-2.0	13.3	19.2	13.7	-4.9	8.0	7.6
Industrial production (% y-o-y)	9.5	11.9	5.9	-4.2	-3.4	9.2	6.0
Gross domestic saving (% GDP)	48.7	49.9	51.7	48.3	45.3	44.4	45.8
Unemployment rate, end-year (%)	2.6	2.7	1.7	2.5	3.7	3.6	3.4
Prices & wages							
CPI, average (% y-o-y)	0.5	1.0	2.1	6.5	0.2	2.9	2.0
CPI, end-year (% y-o-y)	1.3	0.8	4.4	6.7	0.3	3.1	1.9
PPI, end-year (% y-o-y)	4.1	-2.9	4.9	-11.2	1.0	4.0	3.0
Manufacturing wages, nominal (% y-o-y)	4.3	3.5	4.1	5.0	-0.7	3.0	4.0
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	7.1	6.9	7.0	12.2	10.0	9.0	7.0
Broad money supply M3, average (% y-o-y)	5.2	11.9	20.6	10.9	10.5	15.0	12.0
Real private sector credit growth (% y-o-y)	1.8	2.6	8.1	12.8	4.0	8.0	7.0
3M interbank rate, end-year (%)	3.25	3.44	2.38	0.96	0.68	0.80	1.00
5yr yield, end-year (%)	3.01	3.03	2.33	1.40	1.28	1.00	1.80
SGD /USD, end-year	1.66	1.53	1.44	1.44	1.40	1.34	1.32
SGD /USD, average	1.67	1.58	1.50	1.40	1.45	1.38	1.33
SGD /EUR, end-year	1.96	2.03	2.10	2.00	2.00	2.01	1.98
SGD /EUR, average	2.07	1.99	2.09	2.04	2.03	2.07	1.99
External sector							
Merchandise exports (USDbn)	232.3	276.0	305.0	347.6	270.3	304.1	344.2
Merchandise imports (USDbn)	196.0	233.0	257.8	316.4	242.8	277.0	313.0
Trade balance (USDbn)	36.3	43.0	47.2	31.2	27.4	27.1	31.2
Current account balance (USDbn)	33.2	35.5	39.3	27.3	18.8	20.6	24.4
Current account balance (% GDP)	27.5	25.4	23.5	14.8	10.8	10.3	10.9
Net FDI (USDbn)	3.2	14.4	7.0	13.9	10.2	8.7	9.0
Net FDI (% GDP)	2.6	10.3	4.2	7.5	5.9	4.4	4.1
Current account balance plus FDI (% GDP)	30.1	35.7	27.7	22.4	16.7	14.7	15.0
Exports (% y-o-y)	16.4	18.8	10.5	14.0	-22.2	12.5	13.2
Imports (% y-o-y)	16.1	18.9	10.6	22.7	-23.3	14.1	13.0
International FX reserves (USDbn)	115.9	136.2	162.9	173.9	183.1	203.5	222.0
Import cover (months)	7.1	7.0	7.6	6.6	9.0	8.8	8.5
Public and external solvency indicators							
Consolidated government balance (% GDP)	-0.2	0.6	2.9	1.2	-2.5	-0.7	1.0

Source: HSBC, CEIC

Sri Lanka

Unleashing its potential...

Recovery from the global credit crisis has been more modest in comparison to Asian peers, though 3Q09 GDP posted 4.2% y-o-y and was the fastest sequential expansion (+9%) since the series began in March 2002. Increased integration with the liberated North will benefit GDP growth, particularly from the agricultural sector. Slower private credit growth has somewhat dampened growth in 2009. We lower our 2009 GDP growth forecast to 3.8% y-o-y with risks slightly on the downside but retain our bullish 7% in 2010 forecast.

Recovery in external trade has been more sluggish due to weakness in its principal markets – the US and Europe. We expect to see a pick-up in regional trade which should put Sri Lanka's exports in a bright spot.

Sri Lanka's external position is on a strong footing, with official reserves crossing USD5bn. Revenue and expenditure figures since May show a drastic cutback in expenditure and significant improvement in revenue receipts. Overall, we still believe the government is most likely to overshoot the 7% deficit target set by the IMF for 2009. We

have projected the fiscal deficit to reach 7.5% for 2009 and 6.5% for 2010.

CPI inflation averaged 3.4% in 2009 which is the lowest in 5 years. Accommodative monetary policy and gains from an increase in agricultural production are likely to exert opposing pressures on food prices. We believe CPI inflation could reach 10% y-o-y by September 2010 and can expect to see the central bank tighten monetary policy as early as 3Q10.

Sri Lanka holds immense potential and, at the start, will benefit from strong growth in tourism, agriculture and infrastructure investments, particularly in energy and ports. Its closeness to large markets such as India and a strategically located port are among long-term benefits. The positive shock from the end of the civil war will no doubt bring lasting benefits to the country and the USD41bn economy. In the near term, however, greater political certainty after the presidential elections on 26 January 2010 will help to speed up the recovery and rebuilding process.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	6.3	4.3	1.5	2.1	4.2	7.2	7.0	7.5	6.8	6.5
Industrial production (% y-o-y)	6.2	4.3	3.0	-2.3	2.3	3.0	4.0	6.0	6.3	6.8
CPI, end quarter (% y-o-y)	24.3	14.4	5.3	0.9	0.7	4.8	6.0	8.0	10.0	9.6
WPI, end quarter (% y-o-y)	20.6	0.7	-15.1	-10.0	-6.0	6.0	8.0	12.0	15.0	15.0
Trade balance (% GDP)	-13.8	-12.0	-6.7	-6.3	-5.6	-5.9	-7.2	-7.0	-6.3	-6.1
International reserves (USDbn)	2.6	2.4	2.3	2.3	2.4	5.2	4.8	4.5	4.8	5.0
Policy rate, end quarter (%)	12.0	12.0	11.8	11.0	10.5	9.75	9.75	9.75	10.00	10.25
2-yr yield, end quarter (%)	19.2	20.6	16.9	12.8	11.0	10.2	11.0	11.5	13.0	12.5
LKR/USD, end quarter	107.9	113.3	115.5	115.0	114.8	114.4	118.0	118.0	118.0	118.0
LKR/EUR, end quarter	154.9	159.5	152.9	162.3	167.9	163.7	177.0	177.0	177.0	177.0

Source: HSBC, CEIC

Sri Lanka: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	6.2	7.7	6.8	6.0	3.8	7.0	7.2
Nominal GDP (USDbn)	24.4	28.3	32.4	40.7	44.6	50.2	57.3
GDP per capita (USD)	1,241	1,421	1,634	2,014	2,184	2,430	2,743
Private consumption (% y-o-y)	2.6	7.3	7.8	6.7	3.5	6.8	7.0
Government consumption (% y-o-y)	4.8	6.0	5.5	6.0	6.0	8.0	8.0
Investment (% y-o-y)	9.8	13.9	12.0	11.0	4.5	13.0	12.0
Industrial production (% y-o-y)	6.0	5.7	7.6	5.5	1.5	5.8	6.5
Gross domestic saving (% GDP)	21.6	23.7	25.3	25.0	25.9	27.1	28.1
Unemployment rate, end-year (%)	7.2	6.5	6.0	5.3	6.0	6.0	6.0
Prices							
CPI, average (% y-o-y)	11.0	10.0	15.8	22.7	3.4	7.5	6.7
CPI, end-year (% y-o-y)	7.5	13.5	18.7	14.4	4.8	9.6	7.2
WPI, end-year (% y-o-y)	1.7	17.3	26.8	0.7	6.0	15.0	8.2
Minimum wages, nominal (% y-o-y)	3.3	1.1	39.6	23.3	6.0	7.0	6.0
Money, FX & interest rates							
Central bank money M0, end (% y-o-y)	22.4	12.6	2.7	4.0	10.0	11.0	10.0
Broad money supply M2, end (% y-o-y)	19.6	20.7	15.6	11.7	15.0	16.0	11.0
Real private sector credit growth (% y-o-y)	15.4	18.3	9.3	-10.8	11.6	17.5	18.3
Policy rate, end-year (%)	10.3	11.5	12.0	12.0	9.8	10.3	11.0
2yr yield, end-year (%)	11.20	13.35	17.63	20.63	10.20	13.00	12.50
LKR /USD, end-year	102.1	107.7	108.7	113.3	114.4	118.0	118.0
LKR /USD, average	100.5	103.9	110.7	109.2	114.9	118.0	118.0
LKR /EUR, end-year	121.1	141.5	160.2	159.5	163.7	177.0	177.0
LKR /EUR, average	125.0	130.7	154.1	163.7	161.7	177.0	177.0
External sector							
Merchandise exports (USDbn)	6.4	6.9	7.6	8.1	7.0	7.9	8.5
Merchandise imports (USDbn)	8.9	10.3	11.2	14.0	9.5	11.0	12.6
Trade balance (USDbn)	-2.5	-3.4	-3.5	-5.9	-2.5	-3.0	-4.1
Current account balance (USDbn)	-0.7	-1.4	-1.3	-3.8	0.6	0.3	-0.7
Current account balance (% GDP)	-2.7	-5.0	-4.0	-9.3	1.2	0.5	-1.2
Net FDI (USDbn)	0.2	0.4	0.5	0.7	0.7	0.8	0.8
Net FDI (% GDP)	1.0	1.6	1.7	1.7	1.6	1.6	1.4
Current account balance plus FDI (% GDP)	-1.7	-3.4	-2.3	-7.6	2.8	2.1	0.2
Exports (% y-o-y)	10.1	8.5	11.0	6.4	-14.0	13.1	8.0
Imports (% y-o-y)	10.7	15.6	8.9	25.3	-32.2	15.3	15.1
International FX reserves (USDbn)	2.0	2.2	2.4	2.4	5.2	5.0	6.0
Import cover (months)	2.7	2.6	2.6	2.0	6.6	5.5	5.7
Public and external solvency indicators							
Gross external debt (USDbn)	12.0	13.3	15.2	18.7	20.1	20.1	21.2
Short term external debt (% of int'l reserves)	33.5	27.9	45.2	61.9	32.6	40.2	38.2
Budget balance (% GDP)	-8.4	-8.0	-7.7	-7.7	-7.5	-6.5	-5.0
Gross public domestic debt (LKRbn)	12.6	14.2	15.5	19.7	20.1	20.1	21.2
Gross public domestic debt (% GDP)	51.6	50.3	47.9	48.3	45.0	40.0	37.0
Gross public external debt (USDbn)	9.5	10.6	12.0	13.4	17.9	18.6	20.6
Gross public external debt (% GDP)	39.0	37.5	36.9	32.8	40.0	37.0	36.0
Gross public sector debt (% GDP)	90.6	87.9	84.9	81.1	85.0	77.0	73.0

Source: HSBC, CEIC

Taiwan

Engine's still running

Taiwan is back in business. Real GDP growth came in at a surprising -1.3% y-o-y in 3Q, well above the bleak readings seen over the past few quarters and in solidly positive territory sequentially. This is not just an export story. Most remarkably, perhaps, private consumption has come back full force. A stronger labour market and a positive wealth effect from rising stock and real estate prices is bringing shoppers back where they belong. For all of 2009, we now expect Taiwan's economy to contract by 2.8%, a far cry from earlier doomsday projections, and expand by 5.1% next year.

Strong external demand from emerging Asian countries, particularly China, has underpinned Taiwan's export recovery, despite the still-sluggish demand in the US and Europe. This looks set to continue. Moreover, the ongoing normalization of cross-strait relations will attract further capital inflows into Taiwan, benefiting Taiwan's economy by boosting onshore investment and confidence. The next cross-strait focus will be the potential signing of the Economic Framework Cooperation Agreement,

which Taiwan aims to sign by May. The agreement would reduce tariffs on trade between China and Taiwan, enhancing Taiwan's export competitiveness in the long term.

Pricing pressures are already mounting within the Taiwanese manufacturing sector. Given that domestic demand is picking up and global commodity prices rising, Taiwan will shift gradually from deflation to inflation next year, with CPI rising 1.4% and 1.7% in 2010 and 2011, respectively.

In terms of monetary policy, policymakers will continue to fight against speculative inflows and implement further measures if necessary. Moreover, officials will shift their focus to monetary tightening as the economy shows more signs of recovery. We now expect the central bank to hike rate by 75bps throughout next year, delivering 25bps in each of the first three quarters to fend off potential asset bubbles and inflationary pressure.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	-0.8	-7.1	-9.1	-6.9	-1.3	5.7	8.1	5.9	4.2	2.9
Industrial production (% y-o-y)	0.5	-24.2	-32.4	-16.6	-5.4	8.8	13.4	11.2	8.5	6.7
CPI, end quarter (% y-o-y)	3.1	1.3	-0.1	-2.0	-0.9	-0.2	1.0	1.8	2.0	1.8
WPI, end quarter (% y-o-y)	6.1	-9.7	-9.3	-13.7	-9.5	5.5	3.0	3.8	4.2	4.5
Trade balance (% GDP)	1.8	6.5	10.1	8.4	7.0	7.8	9.8	6.0	4.3	6.3
Current account (% GDP)	2.1	7.6	14.2	11.4	8.5	6.8	9.5	6.2	4.1	6.2
International reserves (USDbn)	281.1	291.7	300.1	317.6	332.2	349.9	360.3	367.9	372.4	380.1
Policy rate, end-quarter (%)	3.500	2.000	1.250	1.250	1.250	1.250	1.500	1.750	2.000	2.000
5yr yield, end-quarter (%)	2.00	1.03	1.04	1.03	0.81	1.02	1.00	1.00	0.75	0.75
TWD /USD, end-quarter	32.2	32.8	33.9	32.8	32.2	31.5	31.0	30.0	29.5	29.0
TWD /EUR, end-quarter	45.7	45.6	44.7	45.9	47.0	45.0	46.5	45.0	44.3	43.5

Source: HSBC, CEIC

Taiwan: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	4.7	5.4	6.0	0.7	-2.8	5.1	4.9
Nominal GDP (USDbn)	365.1	374.9	393.8	404.4	380.4	439.4	498.3
GDP per capita (USD)	16,092	16,449	17,223	17,627	16,535	19,044	21,534
Private consumption (% y-o-y)	2.9	1.5	2.1	-0.6	0.9	2.4	2.1
Government consumption (% y-o-y)	0.2	-0.7	2.1	0.7	3.9	2.2	0.9
Investment (% y-o-y)	2.7	0.1	0.6	-11.2	-14.2	7.1	6.6
Industrial production (% y-o-y)	3.8	4.7	7.8	-1.8	-12.4	9.7	8.2
Gross domestic saving (% GDP)	27.1	28.8	30.1	27.6	25.2	28.1	31.3
Unemployment rate, ave. (%)	4.1	3.9	3.9	4.1	5.9	5.6	4.9
Prices & wages							
CPI, average (% y-o-y)	2.3	0.6	1.8	3.5	-0.9	1.2	1.7
CPI, end-year (% y-o-y)	2.2	0.7	3.3	1.3	-0.2	1.8	1.6
WPI, end-year (% y-o-y)	1.7	6.4	8.6	-9.7	5.5	4.5	3.6
Manufacturing wages, nominal (% y-o-y)	2.7	1.4	1.7	-0.3	-1.2	1.8	2.5
Money, FX & interest rates							
Central bank money M0, average (% y-o-y)	8.5	5.1	2.4	7.0	9.4	10.5	10.4
Broad money supply M2, average (% y-o-y)	6.2	6.2	4.3	2.7	7.5	9.2	6.1
Real private sector credit growth (% y-o-y)	6.0	1.9	0.9	-1.0	-1.1	-0.7	0.3
Policy rate, end-year (%)	2.250	2.750	3.375	2.000	1.250	2.000	2.750
5yr yield, end-year (%)	1.75	1.93	2.49	1.03	1.02	0.75	1.15
TWD /USD, end-year	32.8	32.6	32.4	32.8	31.5	29.0	28.0
TWD /USD, average	32.2	32.7	32.8	31.4	32.8	30.2	28.4
TWD /EUR, end-year	38.7	43.0	47.3	45.6	45.0	43.5	42.0
TWD /EUR, average	40.0	41.0	45.6	45.7	45.8	45.3	42.6
External sector							
Merchandise exports (USDbn)	198.5	223.8	246.5	254.9	201.4	232.5	263.2
Merchandise imports (USDbn)	179.0	199.6	216.1	236.4	169.9	203.7	228.7
Trade balance (USDbn)	19.5	24.2	30.4	18.5	31.5	28.8	34.5
Current account balance (USDbn)	17.6	26.3	33.0	25.1	38.3	28.4	34.9
Current account balance (% GDP)	4.8	7.0	8.4	6.2	10.1	6.5	7.0
Net FDI (USDbn)	-4.4	0.0	-3.3	-4.9	-2.2	3.5	-2.2
Net FDI (% GDP)	-1.2	0.0	-0.8	-1.2	-0.6	0.8	-0.4
Current account balance plus FDI (% GDP)	3.6	7.0	7.5	5.0	9.5	7.3	6.6
Exports (% y-o-y)	8.8	12.8	10.1	3.4	-21.0	15.5	13.2
Imports (% y-o-y)	8.5	11.5	8.2	9.4	-28.1	19.9	12.3
International FX reserves (USDbn)	253.3	266.1	270.3	291.7	349.9	380.1	419.8
Import cover (months)	17.0	16.0	15.0	14.8	24.7	22.4	22.0
Public and external solvency indicators							
Commercial banks' FX assets (USDbn)	324.5	336.3	346.6	411.9	406.6	454.5	498.1
Gross external debt (USDbn)	86.7	85.8	94.5	90.4	94.2	104.7	103.6
Private sector external debt (USDbn)	72.8	75.2	91.1	88.9	89.7	97.0	93.0
Central government balance (% GDP)	-0.3	0.4	0.2	-0.7	-3.5	-2.6	-0.8
Gross public domestic debt (TWDbn)	2,831	3,046	3,395	3,705	4,126	4,475	4,623
Gross public domestic debt (% GDP)	24.1	24.9	26.3	29.2	33.1	33.7	32.7
Gross public external debt (USDbn)	13.9	10.6	3.5	1.5	4.5	7.7	10.6
Gross public external debt (% GDP)	3.8	2.8	0.9	0.4	1.2	1.8	2.1
Gross public sector debt (% GDP)	27.9	27.7	27.2	29.5	34.3	35.5	34.8

Source: HSBC, CEIC

Thailand

Long road ahead

Thailand always looked more vulnerable compared to other Asian economies during the recent global slump. Not only were the country's exports hard hit by the slowdown in overseas demand, not least for autos and car parts, one of the country's principal exports, as well as the sharp decline in tourism, but domestic demand was also weighed down by ongoing political uncertainties.

Still, the Thai economy is beginning to live up to its well-deserved reputation of extraordinary resilience. Exports have rebounded strongly in recent months, lifting overall production. Even more remarkably, there are now signs that private consumption is springing back to life: domestic car sales, for example, rose strongly in recent months. Private investment, too, has started to revive, helping to bring down unemployment.

That's the good news. But Thailand's recovery is lagging behind that of its regional peers. Into 3Q09, for example, growth slowed again, as the government stimulus started to fade. More government spending is needed into 2010 to sustain the recovery. Caution evidently still reigns among consumers and investors after years of political turbulence.

Thailand, in short, continues to punch below its weight and there remains a long road ahead to bring growth back up to full potential. Politics remains the key to help dissipate uncertainties that continue to restrain domestic demand, even if growth overall has now turned positive. As a result, inflationary pressures, especially as measured by core prices, which the central bank targets, should remain well-behaved, allowing officials to maintain monetary accommodation for longer than elsewhere in Asia.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09e	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	2.9	-4.2	-7.1	-4.9	-2.8	3.2	3.7	0.7	6.7	7.1
Industrial production (% y-o-y)	5.4	-6.8	-14.4	-8.7	-5.9	3.0	11.0	9.0	8.0	8.0
CPI, end quarter (% y-o-y)	6.1	0.4	-0.2	-4.0	-1.0	3.5	2.5	3.1	3.5	3.8
PPI, end quarter (% y-o-y)	19.0	-1.7	-4.0	-10.5	-7.2	10.0	9.4	10.0	8.8	6.7
Trade balance (% GDP)	-0.4	-2.2	12.5	6.1	7.7	8.6	2.2	0.1	5.0	8.3
Current account (% GDP)	-1.4	-2.4	15.4	4.4	5.6	8.2	3.2	-1.5	4.3	7.4
International reserves (USDbn)	102.4	111.0	116.2	120.8	131.8	138.9	143.0	144.2	150.5	159.5
Policy rate, end-quarter (%)	3.75	2.75	1.50	1.25	1.25	1.25	1.25	1.50	1.75	2.00
5yr yield, end-quarter (%)	4.34	2.48	2.58	3.17	3.21	3.57	3.68	3.20	3.40	3.60
THB /USD, end-quarter	33.9	34.7	35.5	34.1	33.4	33.4	32.5	32.0	31.5	31.5
THB /EUR, end-quarter	48.1	48.2	46.8	47.7	48.8	47.8	48.8	48.0	47.3	47.3

Source: HSBC, CEIC

Thailand: Macro framework

	2005	2006	2007	2008	2009e	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	4.7	5.1	4.9	2.5	-2.9	4.6	4.7
Nominal GDP (USDbn)	176.1	206.9	236.8	272.7	261.6	300.8	336.8
GDP per capita (USD)	2,708	3,160	3,740	4,103	3,934	4,305	4,629
Private consumption (% y-o-y)	4.9	3.2	1.7	2.7	-1.5	3.0	3.3
Government consumption (% y-o-y)	11.4	2.2	9.7	4.6	4.7	6.3	6.1
Investment (% y-o-y)	10.5	3.9	1.5	1.2	-8.1	5.4	4.2
Industrial production (% y-o-y)	9.1	7.3	8.2	5.3	-7.0	6.0	6.6
Gross domestic saving (% GDP)	30.9	32.4	34.4	32.5	32.3	32.1	32.7
Unemployment rate, end-year (%)	1.4	1.0	0.8	1.4	1.1	1.2	1.1
Prices & wages							
CPI, average (% y-o-y)	4.5	4.6	2.2	5.5	-0.8	3.0	3.3
CPI, end-year (% y-o-y)	5.8	3.5	3.2	0.4	3.5	3.8	2.6
PPI, end-year (% y-o-y)	8.0	2.7	8.7	-1.7	10.0	6.7	4.1
Manufacturing wages, nominal (% y-o-y)	6.9	6.2	3.0	10.2	-1.9	5.0	5.0
Money, FX & interest rates							
Central bank money M0, end (% y-o-y)	5.2	2.7	7.9	11.3	7.0	8.0	8.0
Broad money supply M2, end (% y-o-y)	8.2	6.0	6.3	9.2	4.0	5.0	0.0
Real private sector credit growth (% y-o-y)	2.0	-0.9	3.4	15.7	5.8	7.0	6.5
Policy rate, end-year (%)	4.00	5.00	3.25	2.75	1.25	2.00	2.00
5yr yield, end-year (%)	5.49	4.87	4.62	2.48	3.57	3.60	3.60
THB /USD, end-year	41.0	35.5	33.7	34.7	33.4	31.5	31.0
THB /USD, average	40.3	37.9	34.6	33.3	34.3	32.1	31.1
THB /EUR, end-year	48.4	46.8	49.2	48.2	47.8	47.3	46.5
THB /EUR, average	50.2	47.7	48.1	48.5	47.9	48.2	46.6
External sector							
Merchandise exports (USDbn)	109.4	127.9	151.3	175.2	149.4	166.5	183.6
Merchandise imports (USDbn)	117.6	126.9	138.5	175.1	126.5	154.2	172.7
Trade balance (USDbn)	-8.3	1.0	12.8	0.1	22.8	12.3	10.9
Current account balance (USDbn)	-7.6	2.3	15.7	1.6	21.8	10.7	8.5
Current account balance (% GDP)	-4.3	1.1	6.6	0.6	8.3	3.5	2.5
Net FDI (USDbn)	7.5	8.5	8.5	6.0	2.7	6.7	6.7
Net FDI (% GDP)	4.3	4.1	3.6	2.2	1.0	2.2	7.9
Current account balance plus FDI (% GDP)	-0.1	5.2	10.2	2.8	9.4	5.8	10.4
Exports (% y-o-y)	15.2	17.0	18.2	15.9	-14.8	11.5	10.3
Imports (% y-o-y)	25.8	7.9	9.1	26.5	-27.7	21.9	12.0
International FX reserves (USDbn)	52.1	67.0	87.5	111.0	138.9	159.5	177.9
Import cover (months)	5.3	6.3	7.6	7.6	13.2	12.4	12.4
Public and external solvency indicators							
Gross external debt (USDbn)	52.2	59.8	61.9	65.2	60.0	56.5	58.1
Short term external debt (% of int'l reserves)	31.5	27.7	24.7	21.8	13.7	12.5	11.8
Private sector external debt (USDbn)	38.0	45.6	49.7	52.1	49.0	46.0	47.0
Central government balance (% GDP)	0.3	1.2	-2.3	-1.1	-4.2	-4.7	-3.6
Gross public domestic debt (THBbn)	2,705	3,187	3,197	3,434	4,310	4,480	4,605
Gross public domestic debt (% GDP)	38.1	40.6	39.0	37.8	48.1	46.4	44.0
Gross public external debt (USDbn)	14.1	14.2	12.2	13.1	9.3	10.5	11.1
Gross public external debt (% GDP)	8.0	6.9	5.1	4.8	3.5	3.5	3.3
Gross public sector debt (% GDP)	46.2	47.5	44.2	42.6	51.6	49.9	47.3

Source: HSBC, CEIC

Vietnam

Trade troubles...again

Vietnam has been hitting the economic headlines again, and not for the right reasons. On 25 November, the government announced a much-anticipated 5% devaluation of the dong, together with a 1% rise in the base rate to 8%.

The pressure on the currency had been building for some weeks, mainly as a consequence of the renewed and rapid deterioration in the trade position. Surpluses in the first three months of 2009 gave way to deficits of USD1-2bn per month (equivalent to 12-25% of GDP at an annualised rate). This is not too distant from the "crisis" levels of early 2008 but, worryingly, is happening at a time when GDP growth is not all that strong by Vietnam's standards.

Meanwhile, inflation is set to become more of a problem as higher oil and food prices feed through to the headline rate. Indeed, we continue to expect a combination of adverse base effects and higher commodity prices to see inflation return to double

digits by 2Q10, if not earlier. Credit growth is also of concern, rising by nearly 40% in 2009 from the end of 2008, thereby busting the government's upwardly revised target of 30%.

All in all, the time has come for the Vietnam government to exit rapidly from what has been a huge relaxation of both monetary and fiscal conditions (involving a 7% point rate cut and an 8.5% of GDP fiscal easing). The 1% point rate rise is a step in the right direction but there are plenty more increases to come, in our view. We are looking for another 400bps of hikes before the end of 2010, while some reversal in the fiscal stance is also likely.

This will help cap the trade deficit, although not for some months yet, given the time it typically takes for policy to impact domestic demand. In the meantime, downward pressure on the dong, which is trading at the weak side of the new band, is likely to remain fairly intense.

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	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10e	2Q10e	3Q10e	4Q10e
GDP (% y-o-y)	6.5	5.7	3.1	4.5	5.8	7.7	6.5	7.0	7.0	6.8
Industrial production (% y-o-y)	15.8	14.1	2.9	6.8	10.7	14.0	18.0	20.0	17.0	15.0
CPI, end quarter (% y-o-y)	27.9	19.9	11.3	3.9	2.4	6.9	11.0	13.0	9.0	8.0
Trade balance (% GDP)	-5.5	-5.9	8.5	-15.2	-19.7	-18.6	-30.3	-21.9	-20.5	-14.8
International reserves (USDbn)	24.1	24.2	23.3	19.0	18.0	16.0	15.0	14.0	13.0	12.0
Policy rate, end quarter (%)	14.00	8.50	7.00	7.00	7.00	8.00	9.00	10.00	11.00	12.00
5-yr yield, end quarter (%)	15.90	10.00	9.17	9.42	10.10	11.68	12.50	13.20	14.00	14.50
VND/USD, end quarter	16,600	17,483	17,797	17,798	17,841	18,479	18,400	18,400	18,400	18,400
VND/EUR, end quarter	23,572	24,301	23,492	24,917	26,048	26,425	27,600	27,600	27,600	27,600

Source: HSBC, CEIC

Vietnam: Macro framework

	2005	2006	2007	2008	2009	2010e	2011e
Production, demand and employment							
GDP growth (% y-o-y)	8.4	8.2	8.5	6.2	5.3	6.8	5.9
Nominal GDP (USDbn)	53.0	60.9	71.0	79.5	92.0	104.5	117.9
GDP per capita (USD)	638	724	833	921	1,053	1,183	1,319
Private consumption (% y-o-y)	7.3	8.3	9.6	7.6	3.4	5.8	5.0
Government consumption (% y-o-y)	8.1	8.6	9.0	5.8	6.5	5.0	3.0
Investment (% y-o-y)	9.7	9.9	23.0	13.2	3.2	8.0	6.0
Industrial production (% y-o-y)	25.5	16.0	18.2	15.9	8.6	17.5	11.5
Gross domestic saving (% GDP)	34.6	35.0	32.5	32.6	31.9	32.0	31.7
Unemployment rate, end-year (%)	5.3	4.8	4.6	4.7	5.2	5.0	4.7
Prices							
CPI, average (% y-o-y)	8.3	7.5	8.3	23.0	7.8	10.1	7.0
CPI, end-year (% y-o-y)	8.8	6.6	12.6	19.9	6.9	8.0	6.7
PPI, end-year (% y-o-y)	4.4	4.2	6.8	20.0	6.0	8.0	6.0
Money, FX & interest rates							
Broad money supply M2, average (% y-o-y)	29.8	33.6	43.2	25.0	35.0	28.0	25.0
Real private sector credit growth (% y-o-y)	28.7	23.5	41.7	4.7	35.0	25.0	20.0
Policy rate, end-year (%)	7.75	7.75	8.25	8.50	8.00	12.00	12.00
5yr yield, end-year (%)	8.75	8.30	8.73	10.00	11.68	14.50	12.00
VND /USD, end-year	15,896	16,050	16,017	17,483	18,479	18,400	18,400
VND /USD, average	15,866	16,006	16,096	16,759	17,979	18,400	18,400
VND /EUR, end-year	18,751	21,164	23,385	24,301	26,425	27,600	27,600
VND /EUR, average	19,753	20,114	22,373	24,405	25,125	27,600	27,600
External sector							
Merchandise exports (USDbn)	32.4	39.6	48.6	63.1	56.8	65.3	78.4
Merchandise imports (USDbn)	33.3	44.4	62.7	80.6	69.3	87.3	90.0
Trade balance (USDbn)	-0.8	-4.8	-14.1	-16.3	-11.8	-22.0	-13.0
Current account balance (USDbn)	-0.6	-0.2	-7.0	-9.2	-7.0	-13.9	-7.0
Current account balance (% GDP)	-1.1	-0.3	-9.8	-11.6	-7.6	-13.3	-5.9
Net FDI (USDbn)	2.0	2.4	6.6	11.5	10.0	8.0	10.0
Net FDI (% GDP)	3.8	3.9	9.3	14.5	10.9	7.7	8.5
Current account balance plus FDI (% GDP)	2.7	3.7	-0.6	2.8	3.3	-5.6	2.5
Exports (% y-o-y)	22.5	22.1	22.7	29.9	-10.0	15.0	20.0
Imports (% y-o-y)	15.7	33.4	41.2	28.5	-14.0	26.0	3.0
International FX reserves (USDbn)	9.0	13.4	23.5	24.2	16.0	15.0	14.0
Import cover (months)	3.2	3.6	4.5	3.6	2.8	2.1	1.9
Public and external solvency indicators							
Gross external debt (USDbn)	14.2	15.6	19.3	21.8	23.0	25.0	26.0
Short term external debt (% of int'l reserves)	17.8	13.4	20.9	19.8	28.1	36.7	35.7
Private sector external debt (USDbn)	1.6	1.7	2.7	3.0	3.0	3.0	3.0
Consolidated government balance (% GDP)	-4.9	-5.0	-5.0	-5.0	-8.0	-7.0	-5.5
Primary balance (% GDP)	-3.0	-3.5	-3.4	-2.5	-6.0	-4.0	-3.0
Gross public domestic debt (VNDbn)	9.2	11.3	12.4	14.5	19.0	23.0	25.0
Gross public domestic debt (% GDP)	17.4	18.6	19.4	20.8	24.0	26.0	27.0
Gross public external debt (USDbn)	12.6	13.9	16.6	18.8	20.0	22.0	23.0
Gross public external debt (% GDP)	23.8	22.9	23.4	23.6	24.5	25.5	25.0
Gross public external debt (% GDP)	41.2	41.5	42.8	44.4	48.5	51.5	52.0

Source: HSBC, CEIC

Notes

Notes

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