Economics

DBS Flash

Taiwan: No recession, but tepid growth ahead

Group Research

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- *Real GDP has avoided a contraction in 1Q, posting a positive 2.0% QoQ saar (1.7% YoY).*
- *This should be enough to eliminate the concerns about a technical recession this year (like during the China slowdown in 2015).*
- *Tepid growth is expected ahead. Exports are unlikely to stage a V-shaped rebound, despite China stimulus, easing of China-US trade tensions, and bottoming of the tech cycle.*
- *Positive impact from overseas funds repatriation and 2020 election campaign should be small in the near term.*
- *Implication for our forecasts: The 1Q GDP results allow us to maintain the full-year growth forecast at 1.9%.*
- *Implication for investors: The pressure for the central bank to downgrade growth outlook or to ease monetary policy has been reduced.*

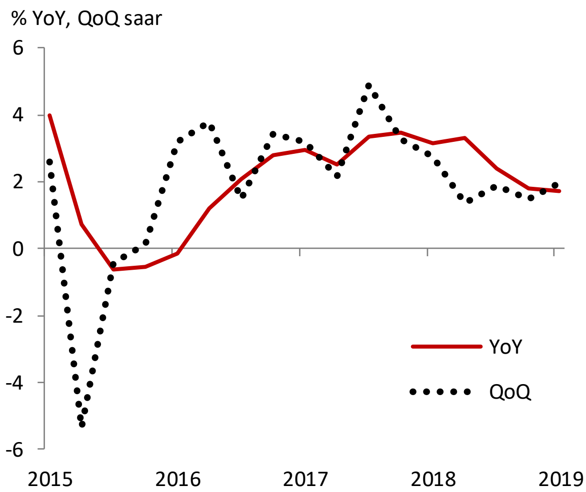
Recession has been avoided

According to the preliminary estimate, the Taiwanese economy has avoided a contraction in the first quarter of this year. **Real GDP grew 2.0% on the QoQ saar basis**, a similar pace as in the previous four quarters (1.9% on average). The YoY growth also stayed firmly positive at 1.7%, not very different from 1.8% in 4Q18 (chart below).

The steady GDP numbers were in contrast with the notable decline in monthly indicators in 1Q19, such as industrial production (-4.6% YoY), exports (-4.2%), and retail sales (-0.3%). This also made Taiwan outperform the neighbouring South Korea, where a QoQ GDP contraction of -1.4% was reported for 1Q19.

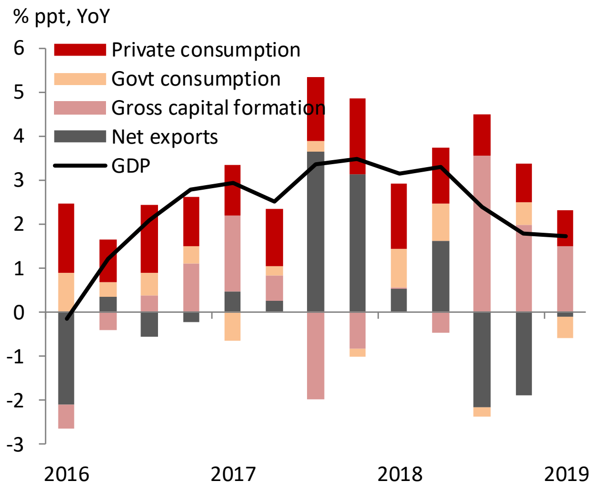
Data details were not as encouraging as the headlines. The rapid slowdown in goods and services imports largely offset that in exports. As a result, the negative contribution of net exports to GDP growth narrowed sharply to -0.1ppt (YoY) from about -2ppt in the previous quarter. Among the other major components, private consumption expenditures and gross capital formation both slowed markedly in 1Q19, while government consumption contracted (chart next page).

Taiwan: Headline GDP growth



Overall, we think the 1Q19 GDP data are enough to eliminate the concerns about a technical recession this year (like during the China slowdown episode in 2015). But there is nothing much to cheer about either.

Taiwan: GDP growth contributions



Tepid growth ahead

Tepid growth lies ahead. It is reasonable to expect an export revival in the later part of this year, taking into account China's policy stimulus, easing of China-US trade tensions and bottoming of the tech cycle (e.g., iPhone price cuts, Huawei's new smartphone models, initial rollouts of 5G). But **a V-shaped export recovery is unlikely.** The dip in China's April PMI suggests that the stimulus-driven economic recovery in China has remained fragile. Despite the prospect of a China-US trade deal in the coming months, chances are not high for the US to completely withdraw its tariffs imposed on the USD 250bn Chinese exports. It would also prove overoptimistic to expect a strong, full-scale upturn in the tech sector, given the lack of comprehensive 5G rollouts and other revolutionary technology changes this year.

On the domestic front, **an interesting development is the rise in funds repatriation from overseas Taiwanese** and the resultant boost on investment growth. The cabinet has passed a draft bill in April to offer tax incentives to encourage Taiwanese companies and individuals to repatriate their overseas funds, especially those used for tangible domestic investment. According to the Ministry of Economic Affairs, about 40 Taiwanese companies with offshore operations have committed to invest a total of TWD 205.7bn (USD 6.7bn) in Taiwan during the first four months of this year. In addition to supportive government policies, there have also been external push factors at play, namely, the lingering China-US trade conflicts, rising wage and other production costs on the mainland, as well as China's implementation of Common Reporting Standard to crack down cross-border tax evasion. Having said that, domestic pull factors have remained weak and some important structural issues have remained unresolved (e.g., labour and land supply shortages), which still constrain the outlook for long-term capital repatriation / investment in Taiwan.

Another focus on the local front is the January 2020 presidential election. Terry Gou, the founder and chairman of Foxconn, has said in April that he will contest the election and take part in the opposition KMT party's primaries. Foxconn is the world's largest contract manufacturer of electronics, and the largest private employer and exporter in China; which bolsters the expectations for Gou to support the pro-business and pro-trade policies. Any election-related impact should be mainly on investor and consumer sentiments this year. Real economic impact will only be available in 2020, which to a large extent, still depends on the election outcome and the post-election policy delivery.

Forecast implications

The 1Q19 GDP results allow us to keep the full-year growth forecast unchanged, at 1.9%. The Directorate General of Budget, Accounting and Statistics, which originally projects 1.8% growth in 1Q19, will probably need to revise down its full-year forecast (2.3%) slightly during the upcoming review in May.

The central bank (CBC) has been relatively conservative compared to the DGBAS on the 2019 growth outlook (2.1%). There is no serious pressure for the CBC to downgrade growth forecast or to ease monetary policy at the next review in June. **We continue to expect the benchmark discount rate to stay flat through this year, at 1.375%.**

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Sources: Data for all charts and tables are from CEIC, Bloomberg and DBS Group Research (forecasts and transformations).