ASEAN: Resilience amid recessionary risks

Summary

With major central banks around the world still embarking on interest rate hikes to fight off inflationary pressures, associated risks on growth, either taking the form of recessionary risks or marked slowdown are inevitable. Even as the surge in inflation has somewhat slowed, it may still settle at elevated levels, requiring higher rates to stay on longer than expected, further heightening risks of prolonged sluggish economic growth, though possibilities of averting outright recession remain.

ASEAN have proven resilient amidst such recessionary risks, with growth holding up relatively well while inflation is notably below those in the G3 economies and fared much better compared to other Emerging Markets (Ems). The fiscal positions are comparatively more prudent with manageable levels of deficit, during and in the aftermath of the pandemic. Stronger external positions as evident from their current account positions and reserves have served as extremely important buffers in weathering the volatility storms that are still raging on.

Nevertheless, Asia's resilience should not be taken for granted. With rising reshoring risks and possible reduced momentum of global trade integration as well as the economic repercussions from likely outcome of prolonged slowdown, **ASEAN should continue to focus on its connectivity to enhance its intra-regional trade for this region to continue growing sustainably amid recessionary risks**.

Data and analysis show that ASEAN region could build more synergy through its intra-ASEAN trade connectivity to build up more resilience in some of the key strategic areas that will sustain the ASEAN growth prospects in the future, such as in the areas of E&E (Singapore, Malaysia, and Vietnam), vehicles & parts (Thailand), apparels and clothing (Vietnam) and mining and natural resources commodities (Indonesia and Malaysia). Opportunities also lie in the area of pharmaceutical to further sustain resiliency, connectivity, and intra-regional trade within ASEAN.

Growth-inflation balance remains favorable for ASEAN

The COVID-19 pandemic has clearly left an indelible economic scar to the global order even as the pandemic itself is fading in a rear view. Following deep global economic contraction of 3% in 2020, the subsequent sharp rebound of 6% in 2021 was immediately followed by slower growth last year, forecasted at circa 3% and is projected to come in even slower at around 2.7% this year. A combination of supply disruption during the pandemic year and in 2021 that has also spilled over to a good part of last year, was met by the incessantly stronger than expected pent-up demand. This has resulted into spiraling higher inflation around the world. The situation is further exacerbated by the ongoing Russia-Ukraine conflict that added bouts of supply disruption that caused prices to remain at elevated levels for more than a year now, notably on food and energy prices. In addition, with China's reopening, another source of pent-up demand could also keep inflationary pressures to remain elevated for a while more.

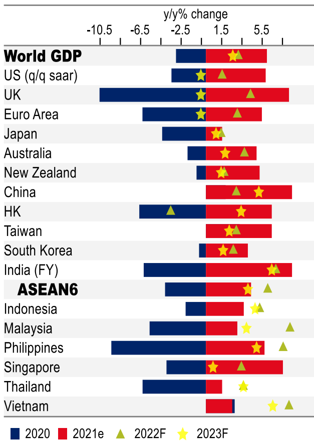
In a classic response to stem off inflation and to anchor inflation expectations, central banks globally responded via interest rate hikes to levels that are comparable to its previous highs. This combination of slowing global growth ahead but with prolonged higher inflation that resulted in higher interest rates is likely to heighten recessionary risks, or at least periods of marked slowdown from here.

In ASEAN, most of the economies have returned to their respective pre-pandemic output levels starting from 3Q21, with the exception of Thailand as its tourism-dependent economy has only recently saw more hopeful push from China's reopening.

ASEAN6 (including Vietnam) is expected to grow at 4.2% this year (2022: 6.2%; 2021: 4.5%), well above the forecasted slowdown in global growth, sustained by the region's large domestic markets and relatively less tight monetary policy and still-supportive fiscal posture. Many of the sectors have also exceeded their pre-pandemic output levels and with sustained re-opening of global & regional economic activities, the near-term outlook remains positive, reflecting resilience for the ASEAN region that weathered through the pandemic years.

Figure 1. Slower growth in Asia, possible recession in US and Europe

Source: Macrobond, UOB Global Economics & Markets Research

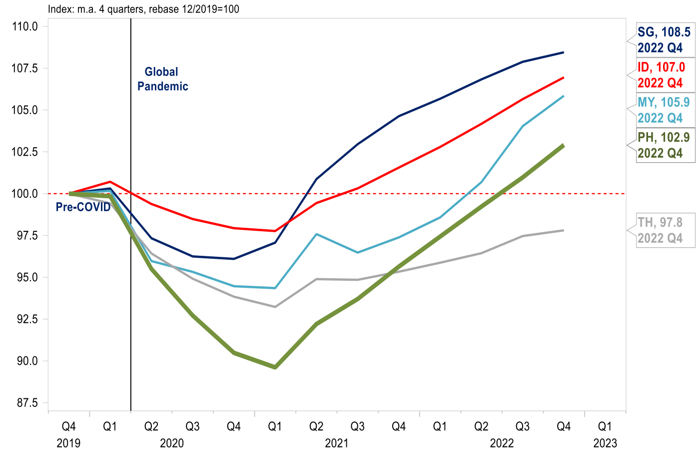


Real GDP Growth Rate (Annual)

	2018	2019	2020	2021e	2022F	2023F
World GDP	3.6	2.8	-3.0	**6.0**	**3.2**	**2.7**
US (q/q saar)	2.3	2.3	-3.4	**5.9**	**1.6**	**-0.5**
UK	1.7	1.6	-11.0	**8.2**	**3.4**	**-0.5**
Euro Area	1.8	1.6	-6.3	**5.5**	**2.7**	**-0.5**
Japan	0.7	-0.4	-4.3	**1.6**	**1.5**	**1.0**
Australia	2.8	1.9	-1.8	**5.0**	**3.8**	**1.9**
New Zealand	4.2	3.2	-0.9	**5.3**	**1.8**	**1.5**
China	6.6	6.2	2.0	**8.8**	**3.0**	**5.2**
HK	2.9	-1.6	-6.6	**6.5**	**-3.5**	**3.5**
Taiwan	2.8	3.0	3.3	**6.5**	**3.0**	**2.3**
South Korea	2.9	2.2	-0.7	**4.1**	**2.7**	**1.7**
India (FY)	7.3	4.6	-6.1	**9.8**	**6.9**	**6.5**
ASEAN6	5.2	4.3	-4.0	**4.5**	**6.1**	**4.2**
Indonesia	5.2	5.0	-2.0	**3.7**	**5.3**	**4.9**
Malaysia	4.8	4.4	-5.6	**3.1**	**8.3**	**4.0**
Philippines	6.3	6.1	-9.3	**5.5**	**7.6**	**5.0**
Singapore	3.6	1.3	-3.9	**7.6**	**3.5**	**0.7**
Thailand	4.2	2.1	-6.3	**1.6**	**3.7**	**3.7**
Vietnam	7.1	7.0	2.8	**2.6**	**8.2**	**6.6**

Figure 2. ASEAN's real economic output largely above Pre-COVID level

Source: Macrobond, UOB Global Economics & Markets Research



Resilience in the ASEAN region this year is further underpinned by sustained recovery of the travel and tourism-related businesses and personal services sectors (such as accommodation & food, retail, transport, entertainment, among others), which we believe will benefit from China's reopening of borders that should lead to greater outbound travels from China. The ongoing Russia-Ukraine conflict is expected to keep commodities prices supported due to the disruptions to supplies, which will be favourable to ASEAN members with strong endowment of natural resources.

Visitors from China accounted for more than 20% of all the inbound travelers into ASEAN before the pandemic hit, which is a key reason for optimism for the tourism sector's fast recovery along with China's reopening. This is particularly positive for Thailand and Malaysia (see Thailand Monthly: China's Reopening Bode Well For Services Exports And THB and Malaysia: Tourism Rides On A High Note).

For commodity exporters, relatively elevated global commodity prices are also a boon for economies such as Indonesia and Malaysia, whereby revenues from the recent commodity boom have helped to boost their exports revenue and further enhance their current account position (see Indonesia: Strong Trade Surplus To Start The Year). The mining industry continues to be the best-performing sectors for Indonesia even during the pandemic on the back of firm demand for resources that includes processed rubber, coal, copper, crude palm oil and base metals, and other.

Vietnam's economy recorded its best year since the 1997-98 Asian financial crisis, growing by a strong 8% in 2022, up from 2.6% in 2021, underpinned by higher private consumption expenditures, investments, and most notably the export of services (tourism revenue). Vietnam's services sector is likely to perform well in 2023 as tourist flows have been very encouraging, just in time to pick-up the slack amidst uncertainty in the external sector that is likely to see downward pressure while domestic-oriented sectors pick up the slack.

On the inflation front, the impact of higher food and fuel prices have indeed been felt in ASEAN. However, compared to G3 economies and other large EMs (see figures below), ASEAN's inflation rates are relatively more benign and have already peaked some months back for the majority of the countries in the group, generally due to improvements in domestic & regional supply chain processes for key food items and to some extent, government subsidies for energy and petrol prices. Inflation rates in the ASEAN region remain within single digits as compared to high double digits in other EMs.

Nevertheless, to fight off inflation risks and to anchor inflation expectations, central banks in the ASEAN region have been responding by hiking their respective benchmark interest rates to moderate excessive demand while the supply-side constraints are working its way out. The extent to which the ASEAN central banks tightened monetary policy, however, are less aggressive compared to their counterparts in developed economies and other global EMs, giving room for a less tight monetary policy to continue supporting growth recovery.

Moreover, as the global supply side disruptions continue to ease and with many of the economies around the world opening up, we believe that inflation pressures may ease towards the later part of the year. This is due to the combination of improved supply chains and stable commodities supplies, as well as moderating demand resulting from tightened monetary conditions and consolidative fiscal policies.

However, there remain risks on the inflation front in light of the global uncertainty and possibly further upheaval in the geopolitical tension that could again disrupt supply chains and commodities supplies.

All in all, inflation expectations are well anchored in the ASEAN region while the extent of monetary policy tightening is reasonable enough for it not to inhibit growth recovery materially.

Figure 3. Inflation In Turkey Surged To More Than 80%!

Source: Macrobond, UOB Global Economics & Markets Research

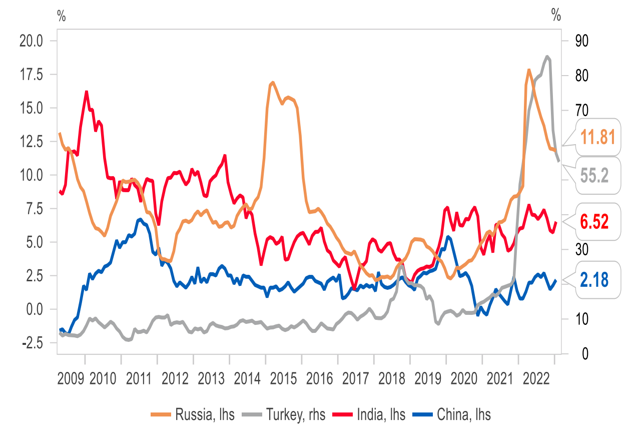


Figure 4. More Manageable Inflation Trajectory In ASEAN

Source: Macrobond, UOB Global Economics & Markets Research

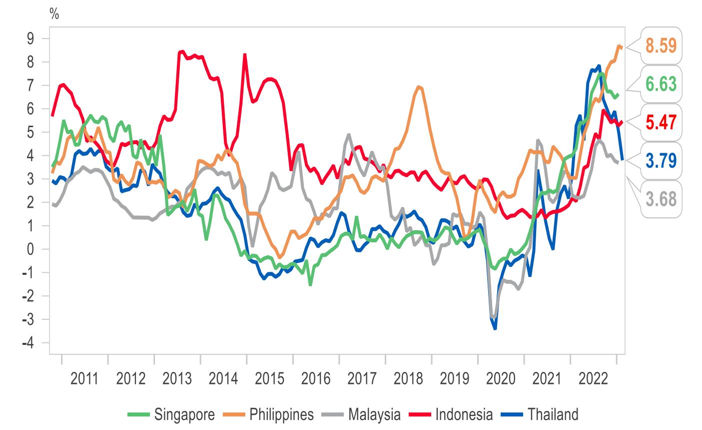


Figure 5. Higher And Much Elevated Inflation Rates In G3 Countries

Source: Macrobond, UOB Global Economics & Markets Research

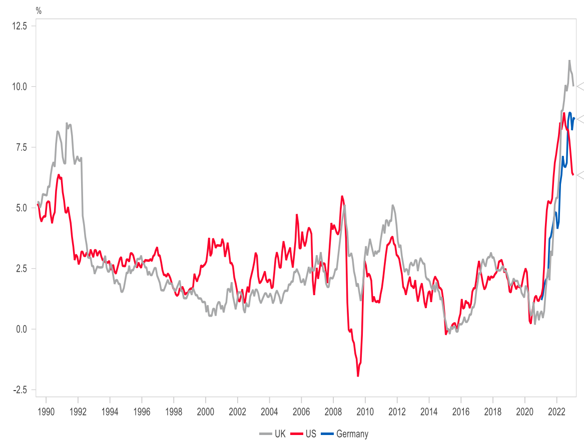
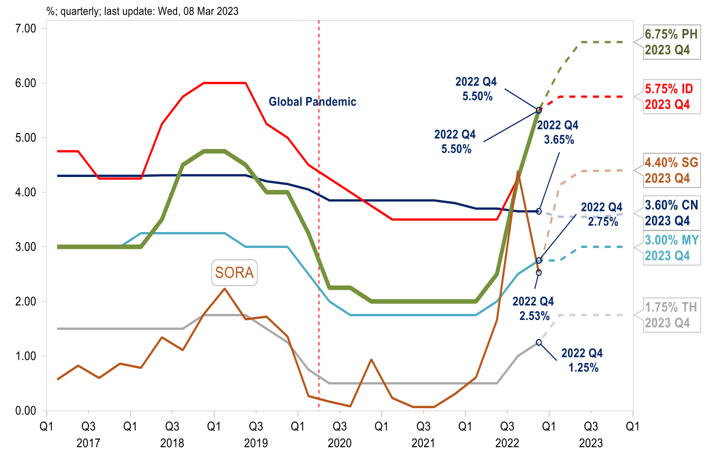


Figure 6. Regional Central Banks Expected To Hold Steady In 2023

Source: Macrobond, UOB Global Economics & Markets Research



Resilient external sector to anchor stability in ASEAN

On the external front, quite a number of ASEAN economies have enjoyed a strong export-led growth performance in 2021-2022, helped by higher global commodity prices. At the start of this year, global commodity prices are seen softening but remains at elevated levels and likely to continue supporting commodity export revenues for countries in the region such as Indonesia and Malaysia. Expected higher services exports' receipts due to higher inbound tourists into this region will also benefit economies such as Thailand, Vietnam, Singapore, and Malaysia.

All these have resulted in resilient external sector of the ASEAN region as evident from their current account positions and FX reserves (which has continuously built up over the years since the Asian financial crisis back in 1997). Relatively prudent fiscal and monetary policy in the region have also shielded the economies in ASEAN from facing a more dire hard currency crunch as external debt levels soar in the aftermath of the pandemic.

Singapore always has a very strong current account surplus position even during the pandemic time, averaging around 17% of GDP in 2019-2022 periods and is forecast to only lower marginally to circa 16% in three years ahead. By the same token, Malaysia averaged a robust current account surplus of 3.5% of GDP in 2019-2022 and is projected to average slightly lower to around 2.7% from this year to 2025. Thailand is forecast to return to a current account surplus of almost 2% this year amidst an expected strong services exports that will also see it returning to the pre-pandemic position of more than 4% in 2025. Similarly, Vietnam is also expected to see stronger recovery in its services exports that will underpin its return to current account surplus position from this year onwards. Indonesia, for the first time in a decade, have witnessed its persistent current account deficit since late 2011 turned into a surplus of 0.3% of GDP in 2021 and subsequently higher to record a 1% surplus in 2022 (see Indonesia: High Current Account Surplus In 2022 After More Than A Decade Of Deficit). It is still expected to register a slight surplus this year before turning into a sub-1% deficit in 2024 and 2025. Lastly, having recorded a large current account deficit of 5.2% of GDP last year, consensus forecast indicated that the Philippines is likely to see narrower deficit to around 2.6% of GDP in 2025.

Fiscal balances in the ASEAN region have also been largely stable at low single digits even during the pandemic year, with many of the key economies in the region having turned more prudent towards their respective fiscal positions. From almost a 7% fiscal deficit in 2020, Singapore immediately returned to almost neutral fiscal balance in 2021-2022. In Indonesia, following the constitutional decree to allow for more than 3% of GDP deficit for 2020-2022 in response to pandemic emergency, registered only a 2.4% deficit in 2022 from more than 6% shortfall in 2020 and is well underway to keep its self-imposed fiscal deficit ceiling of 3% from this year onwards. Malaysia is expected to record a narrower fiscal gap of 5.0% of GDP from 5.6% in 2022 and similarly the Philippines is expected to register a lower fiscal deficit of 5.4% from 6.5% in 2021. Thailand is expected to sharply consolidate its fiscal position to 3.5% deficit from a high of 7% in 2021. Only Vietnam is expected to take a while longer in bringing its fiscal deficit from its current level of almost 5% to below 4%, which is forecast only later in 2026 onwards.

In summary, stronger and more resilient external sector will likely be another important factor that continues underpinning ASEAN's economic stability and cushioning external-driven volatility amidst recessionary headwinds in the imminent future ahead.

Figure 7. International Reserves, Official Reserve Assets, In USD

Source: Macrobond, UOB Global Economics & Markets Research

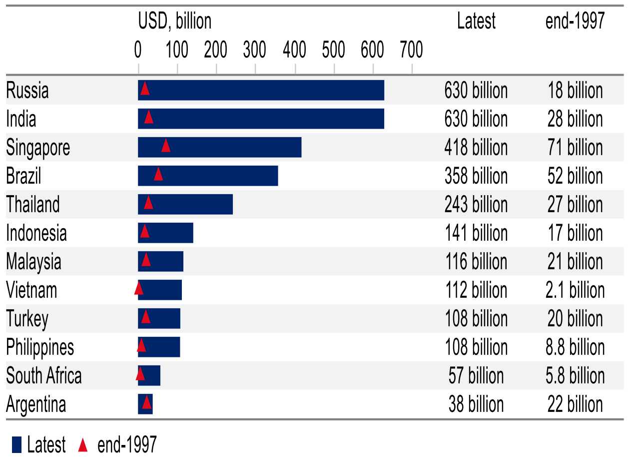


Figure 8. Fiscal Balance As % Of GDP

Source: Macrobond, UOB Global Economics & Markets Research

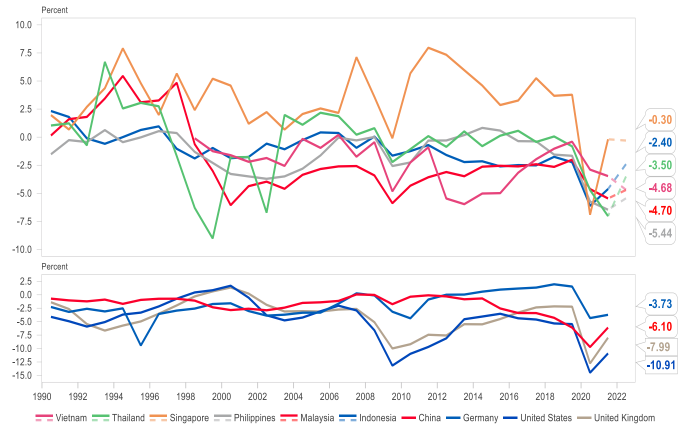


Figure 9. Strong Current Account Position To Anchor External Stability

Source: Consensus Economics, UOB Global Economics & Markets Research

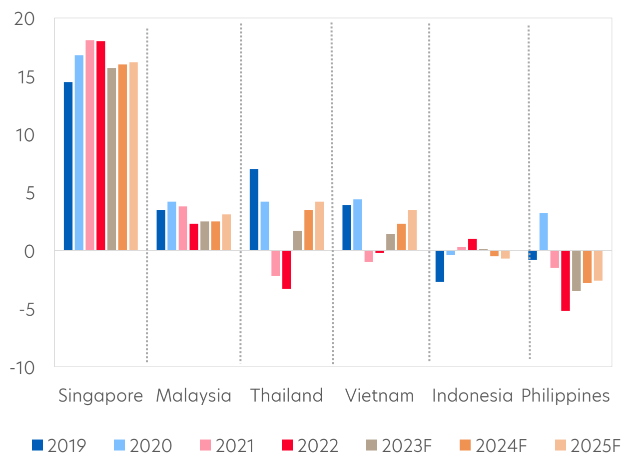
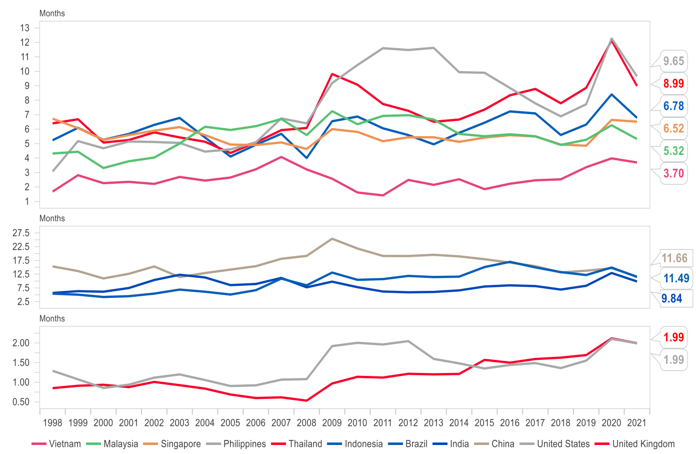


Figure 10. Import Cover Ratios (In Months Of Imports)

Source: Macrobond, UOB Global Economics & Markets Research



Understanding focus areas to enhance resilience in ASEAN

The resilient factors in ASEAN are not to be taken for granted. With rising reshoring risks and possible reduced momentum of global trade integration as well as the latent economic repercussions from the likely outcome of prolonged slowdown, ASEAN should continue to focus on its connectivity through enhancing intra-regional trade to continue growing sustainably amid recessionary risks.

Using Harmonized System (HS) specific goods trade codes for ASEAN, we analyze and identify key opportunities for this region to enhance their collective resilience further, by looking through the net exports revenue generated and establishing individual members' trade advantages and competitiveness

Figure 11 below shows the top 10 trades (exports and imports) in goods for ASEAN, which covers almost 70% of their total trade with the world. Using the latest available data to us (year 2021) from UN Comtrade, the top 3 trades are in the areas where ASEAN is more exposed to as re-exporters, which are in the areas of electrical machinery & electronics equipment (E&E), nuclear reactors and boilers, and mineral fuels and oils.

However, the data that we used for the calculation also show that in the E&E sector, Singapore, Malaysia, and Vietnam have comparative advantage as net exporters of these goods. Individually, they managed to gain a net revenue of USD39bn, USD32bn, and USD13.2bn respectively.

For mineral fuels and oils, the calculated data shows that Indonesia and Malaysia are net exporters in this category, highlighting their absolute advantages as countries rich in natural resources exports.

Going down the list further, ranked 5th and 6th are exports of animal/vegetable fats or oils and rubber that ASEAN, of which again Indonesia and Malaysia have some degree of absolute advantage, whereby in 2021, total exports of this category, predominantly driven by crude palm oil (CPO) surged to almost USD100bn amidst high prices.

In the vehicles & parts category, Thailand recorded a net export receipt of more than USD21.4bn in 2021, highlighting its strength as a regional motor vehicles hub serving the global and regional demand.

Ranked 10th for ASEAN exports is apparel & clothing accessories, worth around USD30bn in 2021. More than half of the ASEAN's exports of this category came from Vietnam alone with predominantly non-ASEAN destinations, such as the US (61%), Japan (10%), Korea (6%), followed by Canada and China at 3% each. As the imports for apparel & clothing is nowhere near the top 10 imports for ASEAN, this gap implies that most of the supply chain are domestically-oriented, with Vietnam being the dominant player in the apparel & clothing space within ASEAN.

The findings suggest that each ASEAN country has its own core strength that they can continue to enhance by deepening the intra-ASEAN trade, leveraging on the different nature of absolute and comparative advantages that each of the economy has. The unprecedented pandemic has also highlighted an important trend that ASEAN as a region could focus on and build strategic synergy amongst member countries.

Available data show that the pharmaceutical sector (and adjacent to this, organic chemicals) may provide an area of opportunity for ASEAN going forward. Before the pandemic, pharmaceutical imports were not key imports for the ASEAN region, lagging far behind iron & steel as well as aluminum imports, with import demand growing at only 2% in 2016 to register slightly below USD10bn worth of imports. Imports of pharmaceutical subsequently surged to almost 40% higher to more than USD14bn in 2020 and a further 65% to reach USD23.2bn in 2021, making it part of the top 10 import list of ASEAN. Nevertheless, the surge is likely to be largely attributed to vaccine imports amidst the fight to exit the pandemic. That said, we are of the view that although it is yet to be seen whether such uptrend will continue further, beefing up intra-ASEAN trade in the pharmaceutical sector is likely to be another key area to further enhance resilience for the ASEAN economies. (For country-specific note along this area, please refer to Indonesia: Healthcare Reforms Are Necessary For A Stronger Economy).

In this potentially promising area, UN Comtrade data shows that Singapore is in the top of the list for pharmaceuticals imports in this region with USD6bn worth of total imports in 2021 (26% of the total import in the category of total pharma import in ASEAN). This was followed by Indonesia at USD4.4bn (19%), Vietnam at USD4.2bn (18%), Thailand, the Philippines, and Malaysia at USD3.8bn (16.4%), USD3.7bn (16%), and USD2.7bn (11.6%), respectively.

However, the sources of these pharmaceutical imports vary across these key ASEAN economies. Singapore sourced almost 70% of its total pharmaceutical imports from the US and European regions, where arguably medical and pharmaceutical goods are relatively more advanced. In a similar vein, Vietnam imported around half of their total pharmaceutical needs from the US and Europe. Indonesia received half of its pharmaceuticals need from China, much higher compared to Malaysia's 22%, the Philippines' 19%, Thai's 18%, and Singapore's 5%. Meanwhile, China imported around 86% of its USD42bn pharmaceutical products from the US and Europe, indicating that the ultimate source of pharmaceutical imports from many Asian countries remain from North America and the European region. At the same time, intra-ASEAN trade remains very sparse and negligible in this category of important goods.

Strategically, given Singapore's strength in pharmaceuticals sector development, in particular research & development, intellectual property (IP) rights protection and high standard of Good Manufacturing Practice (GMP), synergies could be made within the ASEAN region itself to shore up intra-region self-sufficiency in the pharmaceutical trades. For example, Singapore could play a central role in pharmaceutical products research and manufacturing using rubber and vegetable oils that are important components in some key pharmaceutical products, which could be sourced from Malaysia and Indonesia. Meanwhile, apparels and clothing basic materials are another important pharmaceutical and medical item (e.g. personal protective equipment or PPE in short) that can be sourced regionally from Vietnam, *inter alia*.

In conclusion, our analysis using a more detailed and goods-specific trade data continue to highlight each of ASEAN member countries' strength that can be further capitalized to build sustained resilience of this region in the future.

We continue to believe that the ASEAN region could build more synergy through its intra-ASEAN trade connectivity to build up more resilience in some of the key strategic areas that will sustain the ASEAN growth prospects in the future such as in the areas of E&E (Singapore, Malaysia, and Vietnam), vehicles & parts (Thailand), apparels and clothing (Vietnam) and mining and natural resources commodities (Indonesia and Malaysia). The pharmaceuticals sector could be another factor enhancing intra-regional trade, connectivity and resiliency.

The key towards a more resilient region going forward is to understand and capitalize ASEAN collective and intertwined strength as a uniting factor while keeping each ASEAN economies' unique comparative advantages intact.

Figure 11. Top 10 ASEAN Trade (Exports And Imports Using HS Codes)

Source: UN Comtrade, UOB Global Economics & Markets Research

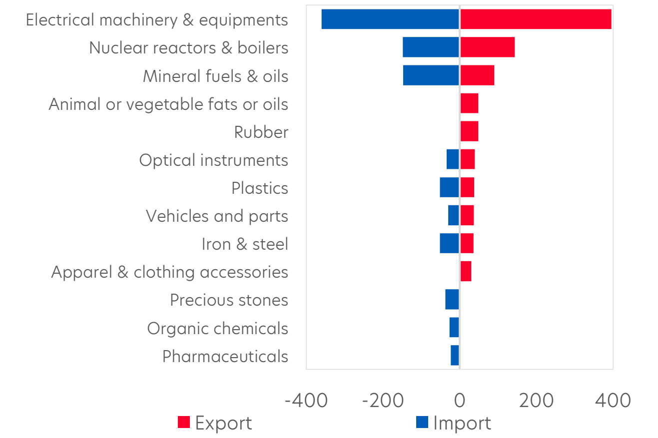


Figure 12. Major Destinations For Vietnam's Apparel Exports

Source: UN Comtrade, UOB Global Economics & Markets Research

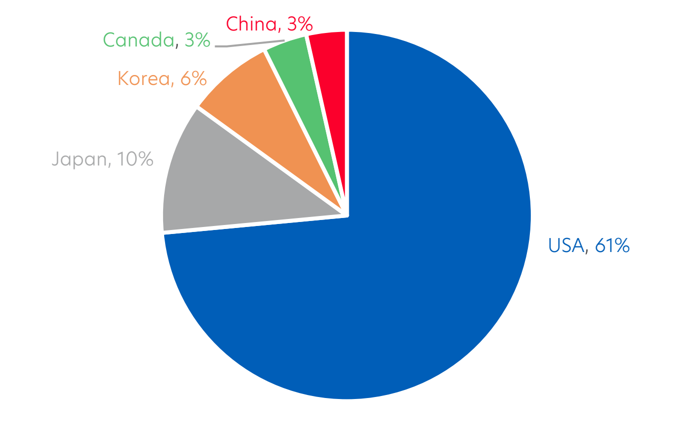


Figure 13. Exponential Increase In Imports Of Pharmaceuticals In ASEAN

Source: UN Comtrade, UOB Global Economics & Markets Research

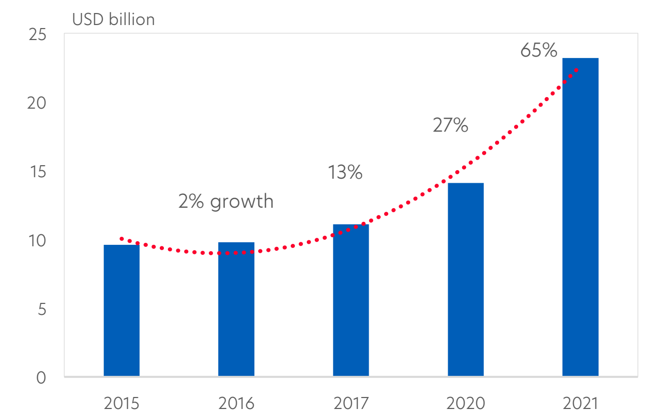
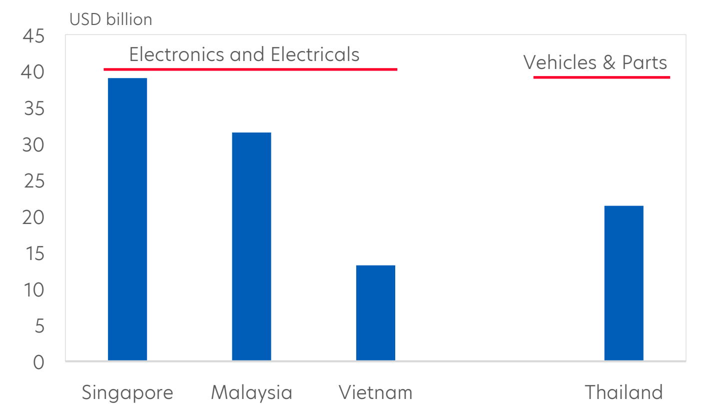


Figure 14. Net Exporters In Electronics & Electrical And Vehicle & Parts

Source: UN Comtrade, UOB Global Economics & Markets Research



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