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Emerging Asia Outlook 2021

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Luctor et emergo

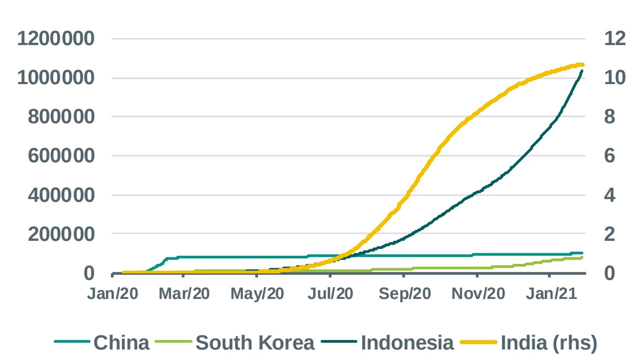
- **Progress with containing pandemic and vaccination diverges and so does economic fall-out**
- **After rare contraction in 2020, we expect regional growth of 7.5% this year, helped by base effects**
- **Chinese and emerging Asian exports lead sharp recovery in global trade from covid-19 collapse**
- **January PMIs divergent, confirming drag from mobility restrictions in China**
- **Portfolio inflows into emerging Asia back at solid levels**
- **After an impressive easing wave in 2020, most of the monetary easing cycle is now behind us**
- **Following fiscal stimulus in 2020, we will see some (but no massive) retrenchment in 2021**
- **Main risks to the outlook stem from pandemic, rising debt, banking distress and (geo)politics**

Success in containing covid-19 diverges …

Last year, regional growth prospects have been shaped by the covid-19 pandemic, that broke out in Wuhan, China in late 2019 but quickly started to spread throughout Asia and the rest of the world in early 2020. The path to normalisation and recovery has started, but will remain bumpy and full of pandemic-related uncertainties. That said, there is strong divergence between countries with regard to the strength of public health systems, the handling of the pandemic and the severity of economic pain suffered from it.

North Asia does better than South Asia on virus control

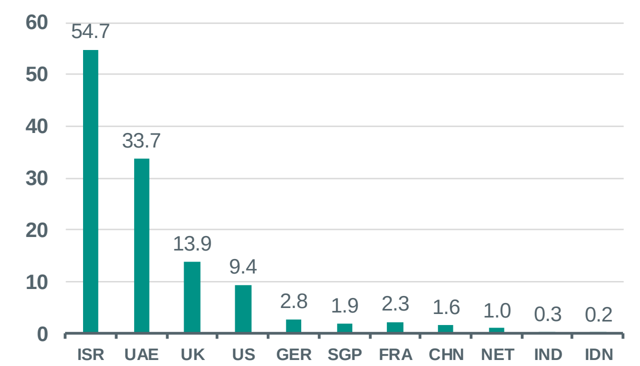
Total number of confirmed covid-19 cases (India in millions, rhs)



Source: Bloomberg

The vaccination race is underway

Total vaccination doses per 100 (single dose, per 31 January 2021)



Source: Our World in Data

In North Asia, the authorities gained control over the virus relatively quickly, particularly in mainland China and Taiwan, although China faces flare-ups and renewed regional lockdowns. South Korea saw a serious second wave in December

2020 and January 2021, while Hong Kong is experiencing a third wave and its first lockdown. In South Asia authorities have generally been less successful in getting the pandemic under control, with Singapore and Vietnam as positive exceptions. India experienced a lengthy, messy but quite ineffective lockdown last year. Although daily new cases continue to drop from the peak reached in September 2020, total confirmed cases in India have surpassed the level of 10 million, with only the US having more registered cases. We have recently also seen serious flare-ups in Indonesia, Malaysia and Thailand, with Malaysia declaring a state of emergency a few weeks ago.

… and so does the race to vaccination …

Emerging Asia is reporting much less covid-19 casualties in relative terms than Europe and the Americas. Perhaps that explains in part why in the 'vaccination race' the region is so far lagging behind frontrunners Israel, UAE (that uses Chinese vaccines) and UK. Within the region (as far as data are available), China and Singapore are ahead, while India and Indonesia are lagging so far. China aims to have 3.5% of the population inoculated before the Lunar New Year break mid-February. Their sequencing of the vaccination is similar to the Netherlands (but the pace is quicker): the roll-out has started with key worker groups, followed by vulnerable segments before widening to all people over 60 years old. For China – well ahead in terms of pandemic control and economic 'normalisation' – success of the vaccination programme is most probably less of a 'make or break factor' for the overall macro outlook compared to most developed economies.

… and the macro economic fall-out from the pandemic

Asian economies have felt the impact from lockdowns and mobility restrictions. They also suffered from other pandemic related headwinds such as the collapse in global trade and tourism and – for commodity exporters such as Malaysia and Indonesia – the corrections in commodity prices (although global trade and commodity prices have shown a clear rebound in the second half of last year). Due to the covid-19 pandemic, annual growth in emerging Asia will be negative in 2020 (our estimate -1.1%, versus +5.0% in 2019), a rare phenomenon. Still, partly in line with variations in pandemic control, there was a remarkable divergence in economic growth as well. Reflecting their successes in pandemic control, China (+2.3%), Taiwan (+3.0%) and Vietnam (+2.9%) posted positive annual growth in 2020. South Korea posted a GDP contraction over 2020, but only a shallow one (-1.0%). For the other Asian countries, we expect negative annual growth in 2020 as well, with India, Philippines and Thailand showing the sharpest contractions. Meanwhile, global trade and financial hubs Hong Kong and Singapore are also feeling the impact from the shock to global GDP and trade growth.

Emerging Asia: Economic growth (forecasts)

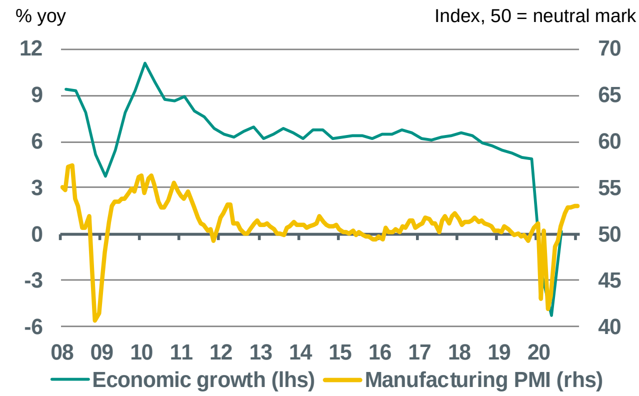
% yoy	Q2-20	Q3-20	Q4-20	2019	2020	2021f	2022f
China	3.2	4.9	6.5	6.1	2.3	8.5	5.5
Hong Kong	-9.0	-3.5	-3.0	-1.2	-6.1	4.0	3.0
India^	-23.9	-7.5	-	4.2	-8.0	9.5	6.0
Indonesia	-5.3	-3.5	-	5.0	-2.0	6.0	5.0
Malaysia	-17.1	-2.7	-	4.3	-5.5	6.5	5.0
Singapore	-13.4	-5.6	-3.8	0.7	-6.0	5.0	3.5
South Korea	-2.7	-1.1	-1.4	2.0	-1.0	3.5	3.0
Taiwan	0.4	3.9	4.9	3.0	3.0	3.5	2.5
Thailand	-12.1	-6.4	-	2.4	-6.5	4.0	4.5
Emerging Asia	-5.3	0.2	-	5.0	-1.1	7.6	5.3
PM: Em. Asia ex CN	*-14.4*	*-4.8*	-	*4.2*	*-5.2*	*7.1*	*5.1*

Source: ABN AMRO Group Economics, Bloomberg, EIU.
* Forecasts 2021-22 rounded ^ India: fiscal years

We expect above trend growth of 7.5% for emerging Asia in 2021 helped by base effects

In line with the recovery of PMIs and foreign trade and the return of portfolio inflows and supported by monetary and fiscal easing (see below), real GDP growth for emerging Asia turned marginally positive again in Q3 (+0.2% yoy) and we expect a further improvement in Q4. China is the key driver of this, with Chinese GDP growth in Q4-20 back at 6.5% yoy, even higher than the latest pre-pandemic figure (+6.0% in Q4-19). This shows that the foundations have been laid for a return to above trend growth in 2021, driven by base effects. True, at the near term virus flare-ups, new mutations and a re-tightening of mobility restrictions will form a drag, but the roll-out of vaccination programmes should reduce this drag in the course of this year. All in all, we expect regional growth to accelerate to an ‘above trend pace’ of around 7.5% in 2021, after which growth will normalise in 2022 (5.3%). Still, while emerging Asia’s growth outperformance continues, we expect regional GDP to stand almost 5% lower by end 2021 compared to our pre-corona base case.

Regional growth positive, PMI above 50 since Q3-20



Source: ABN AMRO Group Economics, Bloomberg, Refinitiv.

India and China expected to outperform in 2021

Source: ABN AMRO Group Economics, EIU (India: fiscal years)

While we expect strong growth in all emerging Asian countries this year, we project that India (9.5%) and China (8.5%) will be the outperformers this year, followed by Philippines and Vietnam (both 7.5%), Malaysia (6.5%) and Indonesia (6.0%). The others are expected to show above-trend growth as well: Hong Kong and Thailand (both 4.0%) and South Korea and Taiwan (both 3.5%).

Chinese and EM Asian exports lead sharp recovery in global trade from covid-19 collapse

Notwithstanding pandemic related headwinds, most countries left the trough in economic activity behind in Q2-20 (China Q1-20). Our regional manufacturing PMI dropped to a post global financial crisis low of 41.9 in April 2020, but has since then gained back more than ten points. This rebound has gone hand in hand with a revival of foreign trade from the covid-19 collapse, that set in in Q3-2020 and extended so far in Q4-20, with China and to a lesser extent the rest of emerging Asia outperforming the global average. China’s strong export performance stems from 1) the fact that Chinese firms were back to business earlier than foreign competitors and 2) pandemic-specific global demand for medical and computer related products. Exports from the rest of EM Asia have been on a revival as well, in China’s slipstream.

January PMIs divergent, confirming drag from mobility restrictions in China

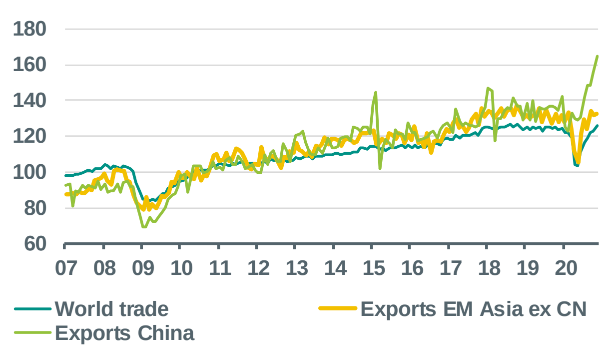
Meanwhile, the manufacturing PMIs published for January this morning also point to divergence. They climbed further to high levels in Taiwan (60.2) and India (57.7). They are also above the 50 neutral mark for South Korea, Indonesia, Vietnam and China, but still below 50 for Malaysia and Hong Kong (December). Meanwhile, both the NBS and Caixin versions of China’s manufacturing PMI have come down significantly over the past months. This fits to our projection that quarterly growth in China will be weak in Q1-21, partly because tighter mobility restrictions will weigh on travelling and consumption, particularly around the Lunar New Year period (see our China 2021 Outlook for more background).

Portfolio inflows back at solid levels

Another positive development stems from the return of portfolio flows to EM Asia (and to other EMs). In early 2020, as the pandemic started to spread beyond China, portfolio inflows from non-residents into the region came to a halt and even turned negative on a net basis. Equity outflows even lasted for five months (February-June), while net debt outflows took place in March only. All of this was the worst episode for EM Asian portfolio flows since the unexpected yuan devaluation mid 2015. However, since then portfolio flows have started to return. This recovery was initially quite modest, but the picture improved further on positive vaccine news and the confirmation of a Biden victory in the US presidential elections (despite longlasting attempts by his predecessor to question the election results) . In fact, in November monthly portfolio flows into emerging Asia jumped to USD 42.9 bn in November 2020, the highest level since January 2018. This rebound went hand in hand with a recovery of Asian FX and an easing in credit risk premia in the course of 2020.

China leads revival in foreign trade

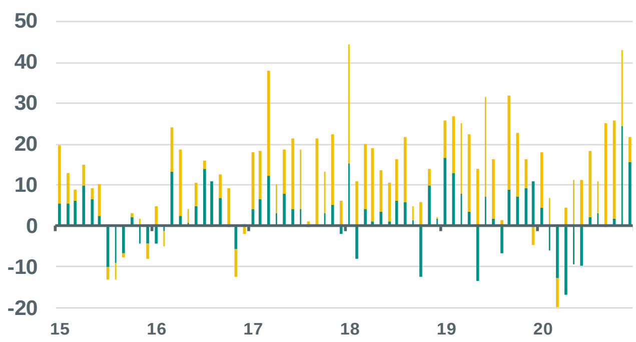
Trade volume indices, 2010 = 100



Source: CPB

Portfolio inflows into EM Asia back to solid levels

Monthly portfolio inflows, USD bn



Source: IIF

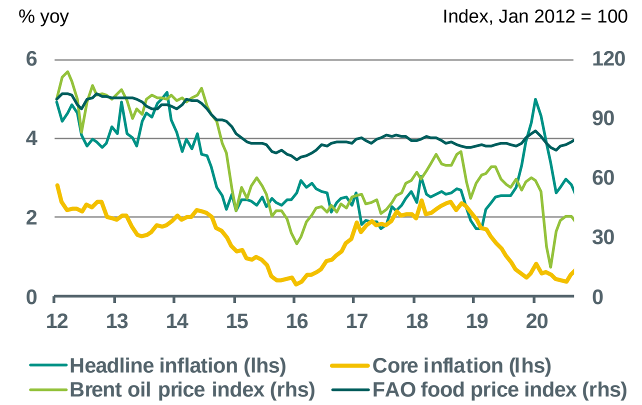
We expect CPI inflation to generally pick up from the current low levels in 2021

In 2020 regional headline inflation followed a downward trend, as the pandemic caused a GDP collapse and a correction of energy and food prices in the first half of the year. Our regional CPI-index dropped from a cyclical peak of 5.0% yoy in January 2020 to 1.3% yoy in December, the lowest level this century. This decline was to a large extent driven by China, following a sharp turn in the pork and food price cycle. Still, there was wide variation: from persistent deflation in Taiwan, Thailand, Malaysia, Singapore and Hong Kong to a food-price driven spike in India, although Indian inflation fell sharply in December (to 4.6% yoy). Looking forward, we expect CPI inflation to pick up from current levels in most countries, even though we expect average annual inflation to fall in 2021 compared to 2020 (driven by China and India). Meanwhile, reginal core inflation remains very low as well from an historic perspective.

After impressive easing wave in 2020, most of the monetary easing cycle now is behind us

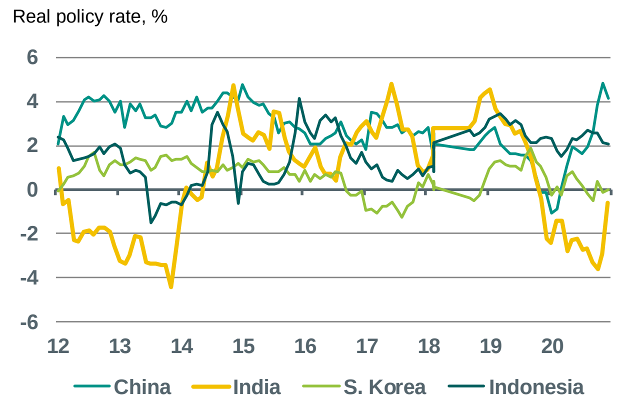
With inflation generally coming down last year, Asian central banks have used the additional room for monetary easing, to try to mitigate the impact from the covid-19 shock. In China, the PBoC cut the one-year lone prime rate by 30 bps in early 2020 and some other policy rates were cut as well. The Reserve Bank of India cut the repo rate by 115 bps (despite the rise of inflation), which brought the real policy rate to a 7-year low of -3.6% in October 2020. Elsewhere in EM Asia, the sharpest rate cuts in 2020 were seen in Hong Kong, Philippines and Vietnam (200 bp, to 0.5%, 2% and 4%, respectively), followed by Malaysia and Indonesia (125 bp, to 1.75% and 3.75%), South Korea and Thailand (75 bp, to 0.5%) and Taiwan (a modest 25 bp, to 1.125%). Meanwhile, Singapore eased its currency policy. Many central banks also introduced or broadened the use of other instruments, to help governments supporting pandemic fiscal spending programmes and/or to safeguard overall bank liquidity. For instance, central banks in India, Indonesia, Philippines and Thailand bought substantial amounts of government bonds. Going forward, we think that most of the monetary easing cycle is behind us (with India being one of the exceptions), but we generally do not foresee Asian central banks to start hiking rates either.

We expect CPI inflation to pick up from current levels



Source: ABN AMRO Group Economics, Refinitiv

Most of the monetary easing cycle is behind us

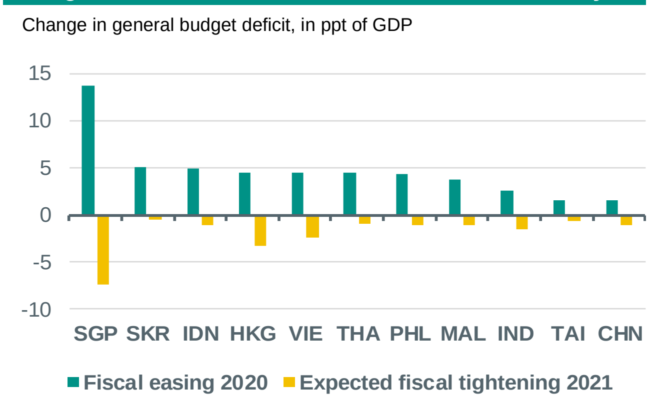


Source: ABN AMRO Group Economic, Refinitiv

Following fiscal stimulus in 2020, we will see some (but no massive) retrenchment in 2021

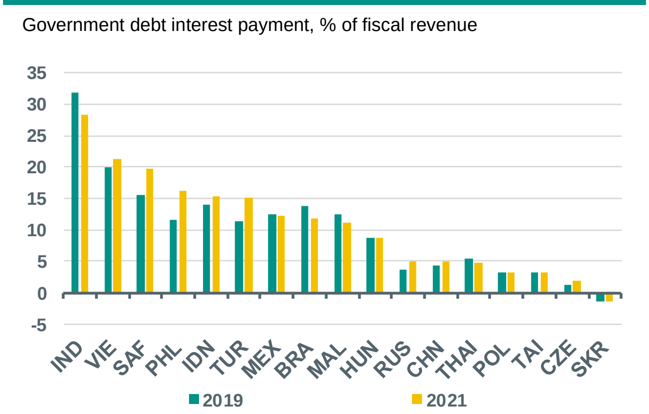
Supported by central banks pushing interest rates lower, EM Asian governments have eased fiscal policy as well to fight the fall-out from the pandemic, although not as much as their counterparts in developed economies. The fiscal impulse in 2020 (combining discretionary spending and 'automatic stabilisation') was the strongest in Singapore (14 ppt), at a wide distance followed by Indonesia and South Korea (± 5 ppt), and was relatively modest in India (±2.5 ppt) and Taiwan. In China, the fiscal impulse was much larger than the change in the general budget balance suggests (±1.5 ppt), as much of it took place in the realm of local governments. Following the fiscal easing mode, public debt ratios have increased throughout the region. Except for Singapore (2020: 155% of GDP), these ratios are generally still at manageable levels, although they have now surpassed the 60% of GDP level in Malaysia and India as well. Looking forward to 2021, we will see some fiscal retrenchment, but not massively (budget deficits will generally remain higher this year compared to the pre pandemic year of 2019). The biggest retrenchment is expected in Singapore, Hong Kong and Vietnam.

Budget deficits will not be back at 2019 levels this year



Source: EIU, ABN AMRO Group Economics

Interest burden substantial for India and some others



Source: EIU, ABN AMRO Group Economics

Main risks to the outlook

In our base case we expect the recovery in regional growth to continue in 2021 and annual growth to reach an above-trend pace of 7.5% helped by base effects. However, we are still living in extraordinary times and global uncertainty remains high. In our view, the main risk factors that could derail our base case for emerging Asia are:

1. Pandemic-related risks. Virus flare-ups, new mutations and delays in vaccination programmes could result in more and/or longer lockdowns and mobility restrictions that impact economic activity. That could be not only true for Asian countries themselves, but also for developed economies that are important export markets. Moreover, a manifestation of pandemic-related risks may give rise to a more risk averse environment in global financial markets that goes hand in hand with portfolio outflows and rising pressures on EM Asian currency and credit spreads.

2.Risks related to higher debt ratios. The global low interest environment helps lowering the cost of issuing additional EM debt. However, particularly in India (and to a lesser extent in Vietnam, Indonesia, Philippines and Malaysia), the interest burden on government debt has become quite significant. Meanwhile, external debt in EM Asia is relatively high in Indonesia. Corporate and household debt combined is also quite high in countries such as China, Hong Kong, Malaysia, Singapore, South Korea, Thailand and Vietnam. This debt load increases the risk of defaults, certainly in case financing conditions deteriorate, and could also add to pressures on EM banking systems. See our Emerging Markets Outlook 2021 for more background on these topics.

3. Financial sector risks. The severe shocks created by the pandemic and the rise of debt ratios may well go hand in hand with a deterioration of the credit quality in EM Asian banking portfolios, certainly when government support packages are being withdrawn, regulatory forbearance measures are lifted and/or liquidity conditions tighten. This is also reflected in the fact that regarding sovereign, bank and corporate ratings negative outlooks still dominate positive ones. In China, where the overall leverage ratio has risen again and several (regional) banks have run into trouble over the past years, we expect systemic banking sector risks to remain contained. That said, Beijing's more tolerant attitude vis-à-vis defaults as the implicit guarantee framework is fading (even of well-rated SOEs), shows that creditors should be aware that defaulting may also be a form of deleveraging (see our China Outlook 2021 for more background).

4. **(Geo)political risks.** We expect US-China relations to remain challenging under the Biden-administration, as in the US the 'being tough on China' attitude is bipartisan and a Democratic administration will also be concerned about strategic competition and human rights issues. That said, we anticipate that US-China tensions will become more of a structural issue under Biden, instead of taking the form of macro economic and/or financial market shocks that were typical during the Trump era (we do not expect a revival of the bilateral tariff war).Other regional geopolitical risks that could flare up from time to time have to do with the relationship between China and Taiwan/Hong Kong, China's more assertive stance in the South China See and other territorial conflicts (e.g. with India) and the situation on the Korean peninsula. On the domestic front, the risk of social unrest remains present as well, as recent developments in for instance India (farm protests), Thailand and Hong Kong have shown.

Main economic indicators/forecasts

GDP growth (%)	2019	2020e	2021e	2022e	Inflation (%)	2019	2020e	2021e	2022e
Emerging Asia	5.0	-1.1	7.6	5.3	Emerging Asia	2.9	3.1	2.4	3.0
Emerging Europe	2.0	-3.3	3.3	3.6	Emerging Europe	6.6	5.2	5.2	5.2
Latin America	0.0	-8.2	3.7	2.8	Latin America**	9.2	7.5	8.8	6.9
Eurozone	1.3	-7.2	2.7	5.4	Eurozone	1.2	0.3	1.1	0.5
US	2.2	-3.5	5.8	4.1	US	1.8	1.2	2.0	2.0
Budget balance (%GDP)	**2019**	**2020e**	**2021e**	**2022e**	**Current account (%GDP)**	**2019**	**2020e**	**2021e**	**2022e**
Emerging Asia	-4.1	-6.0	-5.0	-4.5	Emerging Asia	1.1	2.0	1.5	1.0
Emerging Europe	-0.4	-6.0	-3.5	-2.5	Emerging Europe	1.5	0.0	0.5	0.5
Latin America	-4.1	-10.0	-5.5	-4.0	Latin America	-1.8	0.5	0.0	-1.0
Eurozone	-0.6	-8.5	-7.2	-4.7	Eurozone	3.1	2.6	3.0	2.8
US	-4.5	-14.6	-10.3	-7.0	US	-2.5	-2.6	-2.5	-2.7

Source: EIU, ABN AMRO Group Economics ** figures Emerging Markets regions are rounded*
***Inflation Latin America without Venezuela*