Emerging Asian economies – ASEAN, China and India, are in the midst of their deepest recession in decades. The downturn is expected to be widespread across demand components, with the exception of government consumption that was supported by substantial budgetary stimulus. Economies heavily dependent upon tourism and exports have been particularly affected by the pandemic-induced global recession. Inflation is expected to remain subdued, while unemployment soars and budget deficit and debt rise sharply. A recovery is anticipated to gradually take hold on the back of favourable financing conditions and supportive macroeconomic policies. Substantial uncertainties regarding the outlook prevail as the health crisis continues to unfold in most countries in Emerging Asia and globally. Policy makers in the region need to continuously strengthen the capacity of their health care systems to withstand potential new waves of the pandemic or more virulent strains. As monetary and fiscal space have narrowed appreciably, the focus in 2021 should be on improving monetary policy transmission and making fiscal spending more targeted.
Introduction

The COVID-19 pandemic triggered a severe economic crisis in Emerging Asia: Southeast Asia, China and India. A nascent recovery in the third quarter of 2020 was interrupted by a resurgence of the pandemic, which led to a reinstatement of containment measures in several countries in the region. Notwithstanding, 2020 growth rates have been mostly revised upwards from the projections released in the July 2020 and November 2020 Update. Although the economic downturns stem from a common source, the impact of the crisis varies vastly across economies. Viet Nam is the main driver of growth in ASEAN, while India is expected to post the weakest performance among its peers (Figure 1.1). The major economic drivers have encountered material challenges across the region. The pandemic has radically changed the role of private consumption and investment in driving growth, while the manufacturing and services sector were negatively impacted by the lockdown measures.

Financial markets held steady, while accommodative monetary policy stances maintained favourable financing conditions. However, the impact of the crisis on sectoral balance sheets is already apparent, with rising public and private debt levels. The pandemic is also expected to have a large and unequal impact on current account balances, with the largest corrections in countries that are dependent on tourism and exports. In parallel, trade has mostly benefited from growing Chinese demand, while intra-ASEAN exports dwindled. The signing of the Regional Comprehensive Economic Partnership (RCEP) agreement is anticipated to support the economic recovery going forward. With regards to labour markets, job losses since the onset of the pandemic have been unprecedented. Inflationary pressures are low, with the pandemic-induced global downturn leaving its mark on both domestic and global factors underpinning price developments. Finally, the pandemic is broadly responsible for the current growth observed in e-commerce and e-payment activity in the region.

Looking ahead, uncertainty is remarkably high. The economic recovery will largely depend on each country’s ability to manage possible new waves of the pandemic and cope with potential virus mutations. It will also hinge on the ability of governments to support the economy amid narrowing monetary and fiscal space.
Overview and main findings

Economic output is unlikely to return to pre-pandemic levels across most Emerging Asian economies in 2021. Average ASEAN real GDP growth in 2021 is forecast at 5.1%, following a contraction of 3.4% in 2020 (Table 1.1). In Emerging Asia, real GDP will increase by 7.4% on average in 2021, from a low base, after inching 1.7% lower in 2020. The performance is anticipated to be very uneven across countries. Viet Nam has recovered quickly (+2.6% in 2020), benefitting from an early end to its lockdown phase at the beginning of 2020, as well as from increasing foreign demand and targeted policy support. At the other extreme, real GDP growth in 2020 will be sharply negative in India (-9.9%) and the Philippines (-9.0%). In many countries in Emerging Asia, an uncertain situation on the health front and limited policy space hinder recovery prospects for 2021.
Table 1.1. Real GDP growth in ASEAN, China and India, 2019-21

<table>
<thead>
<tr>
<th>Percentage</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
</tr>
</thead>
<tbody>
<tr>
<td>ASEAN-5</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indonesia</td>
<td>5.0</td>
<td>-2.4</td>
<td>4.0</td>
</tr>
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<td>-5.2</td>
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<td>Philippines</td>
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<td>-9.0</td>
<td>5.9</td>
</tr>
<tr>
<td>Thailand</td>
<td>2.4</td>
<td>-6.4</td>
<td>4.5</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>7.0</td>
<td>2.6</td>
<td>7.0</td>
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<td>Brunei Darussalam and Singapore</td>
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<tr>
<td>Brunei Darussalam</td>
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<td>3.1</td>
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<td>Singapore</td>
<td>0.7</td>
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<td>CLM countries</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Cambodia</td>
<td>7.1</td>
<td>-2.9</td>
<td>5.4</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>5.5</td>
<td>0.6</td>
<td>5.0</td>
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<tr>
<td>Myanmar</td>
<td>6.8</td>
<td>1.7</td>
<td>5.0</td>
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<td>China and India</td>
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<td>China</td>
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<td>India</td>
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<td>-9.9</td>
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<td>Average of ASEAN-10</td>
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<td>-3.4</td>
<td>5.1</td>
</tr>
<tr>
<td>Average of Emerging Asia</td>
<td>5.4</td>
<td>-1.7</td>
<td>7.4</td>
</tr>
</tbody>
</table>

Note: Data are as of 5 January 2021. Data for India and Myanmar relate to fiscal years. The projections for China, India and Indonesia are based on the OECD Economic Outlook, December 2020.
Source: OECD Development Centre.

ASEAN-5

- In Indonesia, COVID-19-related restrictions were implemented more slowly and were relaxed sooner than in similarly affected countries, and the number of COVID-19 cases surged in recent weeks. Private consumption was hit particularly hard in 2020, while weaker corporate balance sheets limited private investment. Commodity prices and a weak tourism sector could present further downside risks to a sustained recovery. After an anticipated drop of 2.4% in 2020, real GDP is forecast to bounce back in 2021 (+4.0%), starting from a low base.

- The pandemic and the recent reinstatement of restrictions in Malaysia led to an unprecedented downturn in economic activity in 2020, with real GDP projected to contract by 5.2%. By averting large-scale lay-offs, Malaysia is anticipated to see economic growth rebound in 2021 from a low base (+7.0%), unless the current movement restrictions are extended or tightened for a prolonged period. The focus on the digital economy and new growth sectors, as well as gains from the RCEP agreement, are anticipated to sustain Malaysia’s economy over the medium term.

- In the Philippines, the pandemic and ensuing restrictions dragged the economy into a deep recession in 2020. The contraction of real GDP in the Philippines is projected to be the most severe among ASEAN economies in 2020 (-9.0%). Public investment and net exports are expected to support a partial economic recovery in 2021 (+5.9%), although rising debt costs and the capacity of the government to service debt remain major downside risks to the outlook. At the same time, uncertainty about international travel and the muted recovery in major economies should affect services exports and remittances by overseas workers.

- Thailand has been severely affected by the pandemic, as its dependence on international tourism make it particularly vulnerable to shocks triggered by travel restrictions. The number of cumulative confirmed cases of COVID-19 saw a spike
over the past few months, in particular during the month of December 2020. The rapid appreciation of the Thai baht in the final quarter of 2020 has been another drag on a fragile economic recovery. Additional risks are related to rising household debt and an escalation of social tensions that could further hamper growth. A swift policy response has helped to cushion the impact on employment and businesses, translating into a recovery in 2021 (+4.5%) following an anticipated 6.4% decline in 2020.

- The successful measures implemented to contain the pandemic in Viet Nam have supported a relatively quick rebound of the economy in 2020 (forecast at 2.6%), the strongest in the Emerging Asia region. The resilience of the industrial sector contributed decisively to growth, despite the fact that major factories were initially affected by supply-chain disruptions. Real GDP is anticipated to grow by 7.0% in 2021. Other downside risks come from rising unemployment, potential tensions with the United States and the budgetary costs of the crisis, which will continue accumulating.

**Brunei Darussalam and Singapore**

- The economy of Brunei Darussalam is in for a solid performance in 2021 (+3.1%), following relatively robust growth in 2020, anticipated at 1.8%. The external sector made a large positive contribution to growth in the first three quarters of 2020, as exports increased steadily in the second and third quarters. Industrial production also remained robust, driven by construction works at a major petrochemical refinery, more than offsetting the decline in services.

- Singapore’s economy contracted sharply in 2020 due to the pandemic (forecast at -5.5%). External demand collapsed, especially for business services, as travel restrictions choked the tourism sector. Sizeable budgetary and financial support measures have cushioned the fall in GDP and the rise in unemployment, and are expected to push the general government balance deep into negative territory. The anticipated recovery in 2021 (+5.0%) is highly uncertain and will largely depend on external demand.

**Cambodia, Lao PDR and Myanmar**

- The economy of Cambodia suffered its sharpest contraction in decades in 2020, anticipated at -2.9%. Overall, the tourism shock is having severe knock-on effects on domestic consumption and investment, while supply bottlenecks and weak external demand have led to a slowdown in the production of garment, textile and footwear products. A recovery is foreseen for 2021 (+5.4%), with some of the recent trade agreements signed by Cambodia expected to start delivering benefits.

- The substantial disruptive effects of the pandemic further slowed Lao PDR’s real GDP growth in 2020, expected to settle at 0.6%. The downturn was largely driven by a steep fall of private consumption due to worsening labour market conditions and rising poverty. Exports also contracted steadily, while supply-chain disruptions particularly affected the garment industry. Real GDP growth is forecast at 5.0% in 2021, although the depreciation of the Lao kip, the bumpy recovery in tourism receipts and the fall in migrant remittances represent considerable downside risks to the outlook.

- After a relatively mild first wave of COVID-19 cases in Myanmar during the spring, a much larger second wave followed in the autumn of 2020, prompting authorities to reinstate tight restrictions. The shock had widespread effects across the economy, depressing private consumption, industrial activity and net exports. In addition, domestic political risks remain substantial. Following an anticipated modest increase of 1.7% in 2020, real GDP growth is seen gathering pace in 2021 (+5.0%), provided the recovery in manufacturing picks up pace.
China and India

- **China** is expected to post positive GDP growth in 2020 (+1.8%). As the pandemic was brought under control early, economic activity rebounded strongly in the second and third quarters of 2020. Despite weaker activity in services, real GDP growth of 8.0% is expected in 2021. Leverage in the public sector and the broader economy will rise significantly, keeping contingent liabilities as a key source of risk to the outlook. Uncertainty surrounding the trade tensions with the United States also tilt the risk balance to the downside.

- **India** is expected to record a historic recession in 2020 (-9.9%), the sharpest fall in Emerging Asia. GDP growth is expected to be 7.9% in 2021, starting from a low base. Uncertainty is high due to underlying structural bottlenecks, such as high reliance on services and vulnerabilities in the banking and financial sectors, while unfavourable developments on the health front and narrowing policy space constitute additional threats to the near-term growth outlook.

Other key points of the economic outlook and assessment

- The pandemic has put the key growth drivers under strain. Private consumption, which tends to decline less than other more volatile components during an economic downturn, contracted sharply in most countries. On the supply side, the resilience of the services sector, which supported the economy during other episodes of weak growth, was severely compromised.

- Continued cases, high case fatality rates and potentially more contagious virus strains will continue to put considerable strain on local health care systems. This risk will likely remain elevated until a vaccine against COVID-19 or an effective treatment become widely available. Policy makers in Emerging Asia need to continuously strengthen their pandemic management strategies. In the short run, they need to ensure the vaccine is stored in appropriate conditions and that it is equitably distributed among the population. In the longer run, the training of health care professionals and strengthening hospital capacity are primordial.

- Emerging Asian countries kept very accommodative policy stances in order to maintain favourable financing conditions. Over the last few months, yields on long-term government bonds have fallen relative to yields on short-term tenors in most countries. On the other hand, conditions in short-term interbank markets had rather mixed evolutions, with interbank spreads widening in several countries, amid rising concerns over banking-sector stability. The potential for additional monetary policy rate cuts is limited in most countries in the region. Several policy options could be explored to preserve monetary space, while continuing to support the economy. Among these, a regime shift to average inflation targeting or focusing on the natural rate of interest as a reference for monetary policy, or a tiered interest rate system appear to be potential avenues in this regard.

- Inflationary pressures are subsiding in most Emerging Asian countries and are expected to be broadly balanced due to the remaining slack in the economy.

- The pandemic exacted a toll on sectoral balance sheets. Both public and private debt increased by several percentage points between the first quarter of 2019 and the second quarter of 2020. The situation is particularly preoccupying in countries that entered the crisis with already elevated debt levels. These developments carry significant implications in terms of solvency, in particular for firms in sectors most affected by the pandemic-induced recession.

- The fiscal stance is projected to be strongly expansionary in 2020, owing to the sizeable emergency fiscal measures implemented to shore up the economy. Prior to the onset of the pandemic, most Emerging Asian economies had room to expand...
their primary balance deficits in response to the economic fallout triggered by the pandemic. However, government debt levels and budget deficits are projected to increase across the board in 2020. With narrower fiscal space, policy makers should strive to make fiscal spending more targeted.

- Nearly all ASEAN countries are anticipated to experience a deterioration of their current account balances, with the sharpest corrections in those countries that are highly dependent on tourism and trade. At the same time, the pandemic has weakened the contribution of exports to the growth of Emerging Asian countries. Exports initiated a recovery in the second half of 2020, mostly supported by strong demand from China and, to a lesser extent, the United States. The pandemic has led to stronger than anticipated growth in e-commerce and e-payments.

- The pandemic also delivered a major blow to labour markets. Job losses since the beginning of the COVID-19 crisis have been more significant than those recorded during the same period of past recession episodes. The labour market adjustment has been more acute for the most vulnerable categories of workers.

Box 1.1. Measuring the economic impact of COVID-19: Growth resilience to large external shocks

The economic forecasts that are regularly published in the Economic Outlook for Southeast Asia, China and India (Outlook hereafter) are derived from the Medium-term Projection Framework for Growth and Development (MPF). The MPF is an analytical tool developed in 2010 for the first edition of the Outlook. Concisely, the MPF has two components, namely baseline models for medium-term projections and economic projection models. Baseline models determine potential output and the output gap, while the economic projection models provide the components of output and other variables. The estimates of potential output gaps used in the baseline models are based on the dynamic stochastic general equilibrium (DSGE) approach. The economic projection models, based on general equilibrium approach, comprise a set of equations describing the five sectors of the economy: the real sector, the monetary sector, the fiscal sector, the balance of payments sector and the debt sector (OECD, 2012). The baseline model was revised for the 2015 edition of the Outlook (OECD, 2015).

The COVID-19 outbreak represents a large external shock, different from other crises experienced by Emerging Asian countries in the past, chiefly the Asian financial crisis of 1997-98 (AFC) and the global financial crisis of 2007-08 (GFC). Measuring the economic impact of external shocks on economic activity is challenging for several reasons. First, gauging how countries will differ in their shock absorption capacity must take into account a variety of parameters that pertain to countries’ economic structures. Second, large exogenous shocks tend to occur less frequently, limiting the potential for comparative studies. Third, the behaviour of economic agents in crisis times may deviate from that prescribed by conventional wisdom. General equilibrium approaches like the MPF may therefore not be suitable for forecasting economic activity during the current crisis period.

A review of the literature shows that there are several approaches to measuring the direct and indirect economic costs of large-scale external shocks, such as natural disasters. Several distinct methods have been utilised, including approaches based on case studies, event studies or input-output tables. However, a large number of academic papers rely on the analysis of time series for quantifying the impact of external shocks, in particular by using structural vector autoregressive (SVAR) methods, whose versatility is widely acknowledged (Bordo and Murshid, 2002; Canova, 2005; Mackowiak, 2006; Ludvigson et al. 2020).
Box 1.1. Measuring the economic impact of COVID-19: Growth resilience to large external shocks (cont.)

Variations of the SVAR model have been utilised, for instance by Gupta et al. (2020), who develop a time-varying parameter structural vector autoregressive (TVP-SVAR) model to analyse the dynamic impact of uncertainty due to pandemics on output growth.

Figure 1.2. Impact of large natural disasters on GDP growth in the Philippines and Thailand

Note: The dotted lines are the error bands (lower bound and upper bound) and the blue line in the middle is the impulse response function. The horizontal axis indicates the time after the shocks in quarters.

Source: OECD Development Centre based on Tanaka, Ibrahim and Lagrine (2021).

In light of these considerations, we use a time-series based approach, as a supplementary tool of the MPF for estimating the growth impact of external shocks of Emerging Asian countries for the Outlook 2021 projections. The analysis is undertaken within a structural vector autoregressive (SVAR) model, which is suited to capture both the size and the speed of the impact (For more details, please see Tanaka, Ibrahim and Lagrine, 2021). We use data on large-scale natural disasters (LNDs) that Emerging Asian countries have faced over the past decades as a sort of proxy variable for large external shocks. Insights on the size and speed of external shocks are derived from impulse response functions. For instance, our empirical results show that LNDs have a large negative impact on GDP growth in Thailand and the Philippines, although the speed at which the impact wanes differs, with a more persistent impact in the Philippines (Figure 1.2). Growth resilience to large external shocks will be determined by economic systems and policy reactions.

Recent developments and near-term outlook

Emerging Asian economies remain in the grip of the COVID-19 pandemic, and supply and demand shocks are still shaping economic activity. Nearly all Emerging Asian countries recorded negative quarterly growth rates in the second quarter of 2020 (Table 1.2), with double-digit declines in Malaysia (-17.1%), the Philippines (-16.3%), Singapore (-13.3%) and Thailand (-12.1%). High-frequency indicators of economic activity and business surveys in most Emerging Asian economies point to an improvement in the third quarter. The recovery is proceeding at different speeds across the region, shaped mainly by developments on the pandemic front but also by other factors, such as the success of policies in shoring up the economy and the pace of the recovery in major trading partners. In the third quarter, real GDP growth rates ranged from roughly -11.5% in the Philippines to 4.9% in China.
Entering the final quarter of 2020, however, momentum is subdued and is expected to be hit by the latest round of restrictions. All in all, restrictions were relaxed in phases as of June, while the August-December period was marked by a new round of tightening (Figure 1.3). As the pandemic continues to spread (Figure 1.4), increasing the risk of hospital congestion, the reinstatement of restrictive measures, which already took place in India, Indonesia, Malaysia and Myanmar, could become more widespread. However, recent efforts have focused more on restrictions at the local level and targeted containment measures rather than full-scale lockdowns. These restrictions are anticipated to weigh on economic activity and sentiment in the short term, with negative effects on private consumption and investment. Nevertheless, the impact on Q4 GDP growth is expected to be more contained than in the March-April period, as the approach to curbing the recent surge in infections has been more targeted.

Overall, ASEAN economies are forecast to have contracted by an average of 3.4% in 2020, while the projection for the broader Emerging Asia region is set at -1.7%. This implies that the average 2021 output growth in ASEAN (+5.1%) and Emerging Asian economies (+7.4%) will barely return to pre-pandemic levels. The projected growth in 2020 is very uneven across Emerging Asian countries. Viet Nam’s economy has recovered quickly (+2.6%), benefitting from an early end to its lockdown restrictions and increasing foreign demand. However, in many other countries in the region, limited policy space combined with falling foreign currency revenues and an uncertain situation on the health front have hindered recovery prospects. Growth rates in 2020 are forecast to range between -9.9% in India and 2.6% in Viet Nam.
Figure 1.3. Stringency of COVID-19-related restrictions in Emerging Asian economies
January-December 2020, stringency index on a scale of 0-100

Note: The figure illustrates the number of Emerging Asian countries in each of the five stringency categories during the respective month. Data as of 20 December 2020, except for Cambodia and Viet Nam (14 December). Monthly values of the index represent the average of daily values for the respective month. An index between 0 and 20 denotes the lowest level of stringency; an index between 80 and 100 corresponds to the highest level of stringency, that could include full-scale lockdowns.

Source: OECD Development Centre based on Oxford COVID-19 Government Response Tracker.
StatLink https://doi.org/10.1787/888934227906

Figure 1.4. Cumulative confirmed cases of COVID-19 in Emerging Asia

A. ASEAN and China

Note: Data as of 5 January 2021.
Source: Johns Hopkins University.
StatLink https://doi.org/10.1787/888934228324
Uncertainty is remarkably high, as would be expected following an economic crisis triggered by a global health crisis that is not yet over. The impact on output, unemployment and balance sheets is likely to be profound, and the prospective recovery may prove different from earlier cycles. As a result, non-negligible downside risks loom further out on the forecast horizon for Emerging Asian economies. The main risk is undoubtedly related to the evolution of the COVID-19 pandemic. Escalating tensions between the United States and China could have wide-reaching implications, spanning trade, financial flows and technology. A deterioration in global financial conditions could aggravate pre-existing vulnerabilities, push vulnerable firms into bankruptcy and worsen credit risk and financial stability. In addition, the asymmetric impact of the pandemic on the poor and most vulnerable could give rise to social tensions, as generally thin welfare systems have exacerbated the uneven distribution of the pandemic's costs. On the other hand, the key upside risks to the forecast are faster advances in the deployment of COVID-19 vaccines or effective treatments that would allow a return to a “business as usual” economic environment together with waning US political uncertainty.

**ASEAN-5**

**Indonesia** saw its real GDP contract by 5.3% in the second quarter of 2020 and by a further 3.5% in Q3, with the main drivers of growth weakened by the effects of restrictive measures implemented since March. The breakdown of GDP growth in the first three quarters of 2020 shows that the contraction was mainly driven by exports and investment (Figure 1.5). Private consumption fell, with the intensification of concerns over job security eroding consumer sentiment (Figure 1.7). Investment was weak, as a series of infrastructure projects were postponed due to the pandemic. Net exports made a negative contribution to growth in the first three quarters, as some of Indonesia's major trading partners saw their economic activity contract sharply in Q2 and only slightly rebound in Q3. On the supply side, agriculture made a positive contribution to growth, while industry and services contributed negatively (Figure 1.5). Transportation and storage, together with wholesale and retail trade, contributed the most to the decline in services, while information and communication activities showed greater resilience (Figure 1.6).

**Figure 1.5. Contribution to GDP growth in Indonesia, 2018-20**

Source: OECD Development Centre based on data from CEIC and national sources.

StatLink  
https://doi.org/10.1787/888934228343
From 5% in 2019, Indonesian GDP growth is forecast to settle at -2.4% in 2020 and to pick up to 4% in 2021. The forecast is subject to considerable risks, however, as COVID-19 continues to spread within the country. Overall, higher unemployment and lower household and corporate incomes are expected to keep consumer demand depressed in the early quarters of 2021, with a more forceful rebound likely only towards the end of 2021. Indonesia’s reliance on portfolio investment and commodity exports could make the country particularly vulnerable to new rounds of external risk aversion and other shocks. Recovery in the tourism industry, which accounts for approximately 4% of GDP, will be slow, as international borders remain closed. Higher government spending and lower revenue due to the slowdown will lead to a deterioration of the fiscal balance and a higher debt burden. On the upside, trade prospects are expected to be supported by the recovery of key trading partners. The recent signing of the RCEP is also anticipated to provide a boost to intraregional trade (Box 1.2). The gradual reduction in corporate tax rates between 2021 and 2023, from 25% to 20%, might result in higher corporate investment over the medium term.
Box 1.2. Regional agreements could accelerate economic recovery in Asia

On 15 November 2020, ASEAN member states, together with Australia, China, Japan, Korea and New Zealand, signed the Regional Comprehensive Economic Partnership (RCEP), covering around 30% of the world’s population and GDP and 28% of global trade (MoFA, 2020). The RCEP aims to eliminate at least 92% of tariffs on imports among the signatory parties within 20 years of coming into effect, which could be as early as 2021. At the same time, around 65% of services sectors are to be fully open, with increased foreign shareholding limits. Common rules for e-commerce, investment flows, labour mobility, competition, intellectual property, government procurement and development of small and medium-sized enterprises (SMEs) are also expected to be established in the region under RCEP (MTI, 2020a). A joint statement from RCEP signatories highlights the potential for the agreement to support an inclusive and sustainable post-COVID-19 economic recovery, job creation and strengthening of regional supply chains (MoFA, 2020).

RCEP is another multilateral free trade agreement involving countries in Asia-Pacific concluded in the last two years, after the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) was signed in March 2018 and entered into force in December 2018. Of the 15 RCEP member countries, Australia, Brunei Darussalam, Japan, Malaysia, New Zealand, Singapore and Viet Nam are also signatories to CPTPP (MTI, 2020b). The CPTPP foresees tariff cuts on approximately 90% of items upon entry into force, followed by tariff cuts on nearly all other items within 10 years. In addition to tariff cuts, CPTPP contains provisions on, among others, customs and trade facilitation; standards and technical barriers to trade; investment; services; intellectual property; e-commerce; procurement; labour; environmental issues; regulatory coherence; and others (New Zealand Foreign Affairs and Trade, 2018).

The Peterson Institute for International Economics (PIIE) estimates that incremental income gains from RCEP will reach USD 209 billion globally by 2030, building upon USD 121 billion in gains from CPTPP over the same horizon (Petri and Plummer, 2020). These estimated economic gains are projected to counterbalance the USD 301 billion in losses anticipated by PIIE because of the US-China trade conflict, notably the trade barriers in the Phase I trade agreement reached in January 2020. At the country level, projected real income gains by 2030 due to RCEP are anticipated to be largest for Korea, Japan, Malaysia, Brunei Darussalam, Thailand and Viet Nam, augmenting the benefits for Viet Nam, Brunei Darussalam and Malaysia stemming from CPTPP (Figure 1.8). For Brunei Darussalam, China and Singapore, these gains will provide an important offset to the losses of trade diversion resulting from the US-China trade conflict (Petri and Plummer, 2020).
Box 1.2. Regional agreements could accelerate economic recovery in Asia (cont.)

Figure 1.8. Projected gains from CPTPP and RCEP versus gains/losses from US-China trade conflict of selected signatory countries

Incremental real income change by 2030, percentage

<table>
<thead>
<tr>
<th>Country</th>
<th>Gains from CPTPP</th>
<th>Gains from RCEP</th>
<th>Gains/losses from US-China trade conflict</th>
</tr>
</thead>
<tbody>
<tr>
<td>Malaysia</td>
<td>3.2%</td>
<td>1.8%</td>
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<tr>
<td>Singapore</td>
<td>4.0%</td>
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<td>Brunei Darussalam</td>
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<td>-0.5%</td>
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<tr>
<td>Viet Nam</td>
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<tr>
<td>New Zealand</td>
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<td>-0.3%</td>
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<td>China</td>
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</tr>
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<td>ASEAN average</td>
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</tbody>
</table>


Overall, the CPTPP and RCEP agreements are a positive development for intra-Asia trade and regional co-operation, as they come amid a severe economic downturn and at a time when the gradual erosion of multilateral trading norms and an increased tendency towards global protectionism are curbing global trade. CPTPP and RCEP are expected to reorient trade and economic ties away from global linkages and towards regionally focused partnerships in East Asia. While the economic benefits stemming from RCEP are more modest than those inherent in CPTPP, the former maintains its symbolic importance, being the world’s largest trade agreement (White & Case, 2020). The RCEP agreement allows for the accession of other countries within 18 months from entering into force. In this regard, the agreement includes a specific clause on the possibility for India to re-join after having opted out of the deal in November 2019 (ASEAN, 2020a).

Due to the upsurge in COVID-19 cases, authorities in Malaysia reinstated partial containment measures as of 14 October in several federal territories. Recent data show that the Malaysian economy contracted by 2.7% year-on-year in Q3 2020, recovering from a 17.1% collapse in the previous quarter. Weak growth was registered across most economic sectors in the first three quarters of 2020 (Figure 1.9), due to the imposition of a restrictive nationwide Movement Control Order (MCO) and the subsequent transition to the Conditional MCO in May and to the Recovery MCO in June. The fall in private consumption, albeit significant, was somewhat limited by stimulus measures such as cash transfers and the implementation of a six-month moratorium on loan repayments. Government consumption continued to expand, although at a moderate pace, while investment and net exports were a drag on overall GDP growth. The improvement in Q3 was largely due to the reopening of the economy and a more benign external environment. The manufacturing sector recovered due to strong electrical and electronics production, while services continued to retreat amid persisting weakness in travel and tourism activity. Wholesale and retail trade along with transportation and storage contributed the most to the sharp fall in services activities in the second and third quarters of 2020 (Figure 1.10).
Figure 1.9. Contribution to GDP growth in Malaysia, 2018-20

Percentage points

A. Demand-side factors

<table>
<thead>
<tr>
<th>Year</th>
<th>Private consumption</th>
<th>Investment</th>
<th>Net exports</th>
<th>Statistical discrepancy</th>
<th>GDP growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>2019</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q1-Q3 2020</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

B. Supply-side factors

<table>
<thead>
<tr>
<th>Year</th>
<th>Agriculture</th>
<th>Industry</th>
<th>Net taxes</th>
<th>Services</th>
<th>GDP growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2019</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q1-Q3 2020</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: OECD Development Centre based on data from CEIC and national sources.

StatLink https://doi.org/10.1787/888934228419

Figure 1.10. Contribution to services growth in Malaysia, 2019-20

Percentage points

<table>
<thead>
<tr>
<th>Services Growth Rate</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food and beverage</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Electricity and gas</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Finance and insurance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accommodation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real estate</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wholesale and retail trade</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Motor vehicles</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transportation and storage</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Information and communication</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other services</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Services growth rate</td>
<td>0.0</td>
<td>0.0</td>
</tr>
</tbody>
</table>

Note: Other services are defined as the sum of the following sub-categories: business services; private education services; private health services; and miscellaneous services.

Source: OECD Development Centre based on data from CEIC and national sources.

StatLink https://doi.org/10.1787/888934228438
Real GDP growth is forecast to fall to -5.2% in 2020 and to stage a recovery in 2021 (+7.0%), starting from a low base. Economic activity has resumed significantly since the relaxation of restrictions in early May. High frequency indicators such as industrial production point to an expansion in Q3 (Figure 1.11), but uncertainty about the short to medium-term prospects is unusually high due to the fading of earlier principal growth drivers. While private consumption and investment are expected to benefit from the broad measures in the fiscal stimulus packages and the low interest rate environment, a weaker-than-anticipated recovery in the global economy poses significant downside risks to growth. The prospect of a second peak of COVID-19 outbreaks that leads to the re-imposition of restrictive measures, along with more persistent weakness in labour market conditions, pose additional threats to the outlook. Adding to the balance of risks is the deterioration of the fiscal balance, amid rising expenditure to finance stimulus packages and lower revenue collection, in particular due to a fall in taxes and royalties from the energy sector.

The continued implementation of the National Policy on Industry 4.0, aimed at boosting digital transformation in the Malaysian manufacturing sector and its related services (MITI, 2018), is likely to speed recovery from the implications of COVID-19 and improve Malaysia’s competitiveness going forward. In addition, Malaysia is expected to derive some of the largest benefits from the RCEP trade agreement (Box 1.2). However, growing interlinkages between the sovereign and the banking sector represent a challenge that could have financial stability implications.
Sovereign risk is transmitted to banks through various channels. This transmission can occur via the asset side of banks’ balance sheets. A deterioration or improvement in the solvency of a state, as perceived by the markets, can lead to losses or gains in the sovereign debt portfolios of banks and can also affect the solvency of banks. As such, sovereign exposures do not differ conceptually from claims on any other debtor, but they are often significant, representing a sizeable portion of domestic public debt. In Malaysia, banks’ holdings of domestic sovereign debt, in particular Treasury bills, have increased since the onset of the COVID-19 crisis (Figure 1.12). The impact of sovereign tensions on bank financing conditions is measured not only in terms of credit risks, but also in terms of liquidity and financing risks. Indeed, government bonds are generally used as collateral, for example via repurchase agreements concluded with wholesale banks. In addition to lowering the value of the collateral, a fall in the price of sovereign bonds can have significant repercussions through margin calls or rising safety margins, thereby reducing the amount of liquidity that can be obtained through a given nominal amount of sovereign bonds. The transmission from the sovereign to the banking sector also takes place via the link between the ratings of public and private issuers. The downgrading of the sovereign rating often leads to the downgrading of domestic banks.

While the lockdown measures imposed in the Philippines appear to be the strictest in the ASEAN region, latest data suggest that the virus continues to spread in the country, albeit at a slower pace. A gradual resumption of economic activities was authorised from early June to early August 2020. Faced with the risk of hospital saturation, local authorities enacted a return to stricter measures as of mid-August. In the third quarter of 2020, Philippine GDP fell by 11.5% year-on-year, after a drop of 16.3% and 0.2%, in the second and first quarter respectively. On the demand side, private consumption and investment...
contracted markedly in the first three quarters of 2020, while government spending and exports made a positive contribution to growth (Figure 1.13). On the supply side, both services and manufacturing fell sharply in Q2, while the decline moderated in Q3 (Figure 1.14).

Figure 1.13. Contribution to GDP growth in the Philippines, 2018-20
Percentage points

Real GDP in the Philippines is projected to decline by 9.0% in 2020, the weakest performance in ASEAN, before increasing by 5.9% in 2021, from a low base. This severe contraction is mainly attributable to the strict containment measures imposed as early as mid-March. Private consumption is expected to remain weak under the combined effect of rising unemployment and the drop in remittances by the Philippine diaspora. Cumulative remittances for the first eight months of 2020 declined by 2.6%, reflecting lower transfers by both land-based and sea-based workers (BSP, 2020a). The recent promulgation of the Bayanihan to Recover as One Act, which provides for a new PHP 165.5 billion (Philippine peso) fund (PNA, 2020a), equivalent to approximately USD 3.4 billion, is expected to further mitigate the economic and social impact of the pandemic in the short term. The ability of public authorities to disburse the funds remains a real source of uncertainty. Indeed, the Philippine authorities have already experienced a certain delay in the distribution of emergency grants due to the difficulty of identifying beneficiaries and the financial exclusion of a large part of the population. Only 29% of Filipino adults owned a bank account in 2019, up from 23% in 2017 (BSP, 2020b).
The “Build, Build, Build” public and private infrastructure investment programme is still perceived as the main driver of economic recovery. The list of priority areas has been revised to include more projects in the domains of food security, water supply, health care and digital infrastructure. Rising debt costs and the capacity of the government to service the debt remain a downside risk to the outlook. Sovereign risk is nevertheless mitigated by the composition of the public debt, mainly denominated in domestic currency, and by its maturity profile, with the bulk in the form of long-term debt.

While relatively spared on the health front, Thailand is suffering the full brunt of the economic consequences of the crisis, in particular due to the almost complete closure of its borders. Since the economy lost momentum at the end of 2019, the starting point for 2020 was already weak. The pandemic and the introduction of travel restrictions devastated Thailand’s large tourism sector, causing one of Emerging Asia’s steepest declines in second and third quarter GDP. Thai GDP contracted by 6.4% year-on-year in the third quarter of 2020, after a contraction of 12.1% in Q2 and 1.8% in Q1. This contraction is mainly due to the impact of the COVID-19 crisis on services and exports (Figure 1.15). Private consumption and investment also made a negative contribution to growth. Exports to ASEAN and the European Union were subdued, while exports to China and the United States started to pick up as of May (Figure 1.16, Panel A). A large proportion of Thai merchandise exports was affected by the crisis, especially automobiles and machinery and equipment, while electronics and machinery and equipment made a positive contribution to export growth in October (Figure 1.16, Panel B).
The estimated output growth rate in 2020 stands at -6.4%. The anticipated rebound for 2021, very dependent on the resumption of tourist flows, would be equal to 4.5%. The risks weighing on the Thai economy in 2021 are mainly related to a potential resumption of the pandemic. The recent spike in COVID-19 cases in Thailand could derail the continued...
upturn in domestic activity and a hypothetical recovery in tourism. The reopening of the tourism sector was expected to commence with the Special Tourist Visa (STV) scheme in Q4, albeit under very strict arrangements (NNT, 2020). The domestic political context could also impact growth, with the large-scale protests that took place in the fourth quarter of 2020 further exacerbating uncertainty. The late implementation of the 2020-21 budget could delay the dynamics of public investment, while there is virtually no room for further policy rate reductions. The rapid appreciation of the Thai baht (THB) during Q4 2020 may affect the fragile recovery of the economy, prompting the Bank of Thailand to bring forward capital outflow rules to curb THB strength (BOT, 2020a). Finally, rising household debt, combined with a sharp rise in unemployment and underemployment, is likely to have a lasting impact on domestic consumption. On the upside, public-private partnership (PPP) projects related to the Eastern Economic Corridor (EEC) special development zone, and investment in the 5G network, are likely to help foster private investment in the medium term.

Looking further ahead, economic performance is anticipated to be influenced by structural issues facing the Thai economy. Thailand is very dependent on exports, in particular to China and the United States. In addition, the Thai education system is struggling to fill a growing shortage of skilled labour necessary for the deployment of the Thailand 4.0 strategy.

The economic performance of Viet Nam in 2020 will be relatively mildly affected by the pandemic, which has nevertheless put an end to the robust growth rates recorded in the past. Real GDP climbed by 2.7% year-on-year in the third quarter of 2020, after rising by a meagre 0.4% in Q2. While industry and services contributed fairly evenly to growth in 2019, services have played a smaller role in 2020, on the back of a relatively dim outlook for the region and the global economy (Figure 1.17). Manufacturers with highly integrated supply chains – in particular in the textile and garment industry, where nearly 60% of materials are sourced from China – suffered from major disruptions in the early months of 2020. Industrial production in Q2 and Q3 largely benefited from solid manufacturing activity, while mining and quarrying made a negative contribution to industrial activity (Figure 1.18). In parallel, lower demand from China has dealt a blow to Viet Nam’s agriculture, forestry and fisheries sector.

Figure 1.17. Contribution to GDP growth in Viet Nam, 2018-20

Source: OECD Development Centre based on data from CEIC and national sources.
StatLink https://doi.org/10.1787/888934228571
In view of the ongoing global crisis, economic growth in Viet Nam is expected to slow in 2020, but to remain the strongest in Emerging Asia (+2.6%). The projection for 2021 points to a real GDP growth rate of 7.0%. The outlook for exports, which rebounded sharply over the past months, is particularly uncertain due to economic deterioration in some of Viet Nam’s major trading partners. The labour market will remain under considerable pressure, with 31.8 million workers negatively affected by the pandemic, in the form of job losses, cuts in working hours or income reductions. The services sector has been the hardest hit, with 68.9% of workers affected, followed by the industry and construction sector, with 66.4% of workers affected (GSO, 2020). Adding to the balance of downside risks, the fiscal deficit is forecast to increase substantially in 2020, as the government has launched large stimulus packages to support businesses and consumers. At 56.1% of GDP in 2019, public debt is high by regional standards, increasing the risk of debt distress and limiting the room for fiscal manoeuvre. Another challenge stems from the US Section 301 investigation concerning Viet Nam’s practices with respect to timber imports and currency undervaluation, which could potentially result in the imposition of tariffs (USTR, 2020).

The medium to long-term prospects are particularly benign, as Viet Nam is well positioned to benefit from the trade diversification trend, which was triggered by the US-China trade tensions. In addition to low production costs, other factors are expected to reinforce Viet Nam’s attractiveness as an investment destination. These include participation in several free trade agreements, such as, CPTPP, RCEP and the recent one with the European Union having come into force in August 2020 (EC, 2020). Investments and exports are likely to expand steadily in the coming years if the relocation trend continues.

**Brunei Darussalam and Singapore**

Quarterly growth in Brunei Darussalam came in at 0.5% in the third quarter of 2020, after an increase of 3.0% in Q2 and a 2.3% rise in Q1. Net exports contributed the most to growth in the first three quarters of 2020 (Figure 1.19), due to strong growth of exports. Industry contributed the most to the increase during Q1-Q3, driven by construction works at a major petrochemical refinery slated for completion by 2022. Strong liquefied gas and...
methanol production supported industrial activity in the first three quarters of last year (Figure 1.20). Nevertheless, high-frequency indicators point to a deterioration of the trade balance entering Q4. Exports fell by 24.2% year-on-year in July 2020, as both crude oil and liquefied natural gas (LNG) exports dwindled, by 36.1% and 47.6%, respectively. Export growth remained negative in August (-9.6%) and September 2020 (-3.5%).

Figure 1.19. Contribution to GDP growth in Brunei Darussalam, 2018-20
Percentage points

Source: OECD Development Centre based on data from CEIC and national sources.
StatLink 123 https://doi.org/10.1787/888934228609

Figure 1.20. Contribution to industrial sector growth in Brunei Darussalam, 2019-20
Percentage points

Source: OECD Development Centre based on data from CEIC and national sources.
StatLink 123 https://doi.org/10.1787/888934228628
Output growth is forecast to be relatively solid in 2020, at 1.8%. It is anticipated that the growth rate will pick up pace in 2021 and settle at 3.1%. With the pandemic under control domestically, the unwinding of the remaining restrictions is anticipated to proceed at a steady pace. The government passed sizeable expansionary measures, whose impact is likely to be felt in 2021, bolstering consumption. The most significant economic drag stems from weak global energy demand and prices. Another downside risk is the possibility that trade tensions between China and the United States will escalate further.

Efforts by the government to diversify the economy away from oil and LNG exports, by accelerating investments in the manufacturing and services sectors, are expected to yield significant results in the medium-term. Several projects are underway, including a fertiliser plant, which is scheduled to commence operations in Q2 2021, and the completion of the second phase of the Hengyi petrochemical refinery by 2022. These are likely to boost job creation and investment considerably.

Amid continued slack in external economies, the Singapore GDP shrank by 5.6% year-on-year in Q3 2020, moderating from a 13.4% contraction in Q2. The contraction in the first three quarters of 2020 was driven mainly by a substantial fall in private consumption, but also by a decline in investment and net exports (Figure 1.21). The second quarter’s sharp contraction was largely due to a decline in construction and travel-related services, which together account for approximately 8% of GDP. The construction sector was particularly affected by the implementation of Circuit Breaker measures and a rise in COVID-19 cases among foreign workers, which brought many construction sites to a near standstill. Wholesale and retail trade, business services, together with transportation and storage, mainly drove the contraction in services in the first three quarters of 2020 (Figure 1.22). Manufacturing was also affected, but less than the services sector, as the former benefited from a surge in the production of pharmaceutical ingredients and an expansion in petrochemical output.

Figure 1.21. Contribution to GDP growth in Singapore, 2018-20

Note: Services include the ownership of dwellings.
Source: OECD Development Centre based on data from CEIC and national sources.
StatLink https://doi.org/10.1787/888934228647
Economic activity is expected to fall in 2020 by 5.5% and return to growth (+5.0%) in 2021, from a low base. Singapore is being hit hard by the global downturn because of its high export dependence and specialisation in particularly volatile investment goods. Given the sustained fall in investment orders and continued spread of the pandemic globally, exports are likely to contract further in the course of 2021, though the rate of decline should gradually decelerate. Faced with a weak business outlook and a plunge in capacity utilisation, companies might further curtail investment spending. On the other hand, the squeeze of household disposable incomes will be partly compensated by higher transfer payments and tax relief measures adopted as part of the government’s successive stimulus packages, which together amount to a total of approximately SGD 93 billion (Singapore dollars) or roughly USD 70 billion.

The financial sector in particular is well positioned to emerge stronger from the COVID-19 crisis. The Monetary Authority of Singapore (MAS) launched an SGD 125 million (approximately USD 94 million) package in April 2020 to support and enhance capabilities in the financial services and Fintech sectors (MAS, 2020a). The Fintech sector is expected to accelerate its development further; Fintech firms raised SGD 462 million (nearly USD 347 million) in equity funding in the first half of 2020, which represents a 19% increase from the previous year. Sustainable finance is also anticipated to expand at a steady rate in the coming years, as Singapore has become the largest market for green finance in ASEAN (MAS, 2020b).
Box 1.3. Singapore aims to become green finance hub in Asia

The Monetary Authority of Singapore (MAS) has launched several initiatives to support the development of green financing solutions. MAS unveiled its Green Finance Action Plan in November 2019, aimed at transforming Singapore into a leading centre for green finance in Asia and globally. This long-term strategy is articulated around three pillars: (i) strengthening resilience vis-à-vis environmental risks; (ii) developing markets for green finance, which includes the creation of a subsidy programme for green and sustainable loans; and (iii) mobilising innovation and technology, in particular through the creation of centres of excellence. In November 2020, MAS announced the launch of the Green and Sustainability-Linked Loan Grant Scheme (GSL). The grant will enter into force in January 2021 and is the first of its kind in the world. The GSL aims to support corporates of all sizes in obtaining green and sustainable financing by discharging the expenses of engaging independent service providers to certify the green and sustainability credentials of the loan. The scheme also encourages banks to develop green and sustainability-linked loan frameworks to render such financing options more accessible to small and medium-sized enterprises (MAS, 2020c). Another related initiative is the Sustainable Bond Grant Scheme, which encourages the issuance of green, social, sustainability and sustainability-linked bonds in Singapore (MAS, 2020d). Meanwhile, with seven other central banks around the world, the MAS has launched a network called the Central Banks and Supervisors Network for Greening Financial System. This network intends to promote green financing and share knowledge about it with other countries (Chang, 2019).

The private sector also plays an important role towards achieving this goal. Banks such as BNP Paribas, OCBC Bank and UOB have initiated systems that spell out clear and comprehensive criteria on how to evaluate green and sustainable finance transactions and projects, aligned with the environmental objectives of the UN Sustainable Development Goals. Many of these projects are characterised by a circular economy, where waste is recycled and resources are kept in use for as long as possible. Examples include renewable energy projects, energy efficiency activities and sustainable supply-chain processes (MAS, 2020e).

Figure 1.23. Green bond issuance by new issuers in selected ASEAN economies, January-August 2020

Note: Data refer to green bond issuance by new issuers entering the market. Subsequent issuances from repeat issuers are not included. Data capture issuance by all issuer sectors.

Box 1.3. Singapore aims to become green finance hub in Asia (cont.)

In 2020, issuers based in Singapore took the lead for first-time green bond issuance in the ASEAN region (Figure 1.23). However, green bond issuance in Singapore started several years ago. In 2017, for instance, City Development Limited (CDL), a real estate development company and Development Bank of Singapore (DBS), a commercial bank, each issued a green bond, the country’s first. The proceeds from the CDL green bond were distributed to finance the upgrading and restoring of commercial buildings in the city area, while the proceeds of the DBS green bonds were invested in renewable energy and climate projects (Chang, 2019).

Through these initiatives, the Monetary Authority of Singapore together with banks aim to promote sustainable development in the region and to set standards of sustainable financial development. These plans have become an important part of the green finance network that Singapore is building to support Asia’s important step towards a more sustainable future.

Cambodia, Lao PDR and Myanmar

In comparison with other ASEAN countries, Cambodia is particularly dependent on the tourism sector, which accounted for nearly 14% of its GDP in 2018. While international borders are officially open, entry conditions are drastic and the granting of tourist visas is suspended until further notice. International tourist arrivals declined by more than 95% year-on-year in October. Tourist arrivals plummeted in line with a sharp fall in the number of travellers from ASEAN and China (Figure 1.25). Estimates point to nearly 3 000 business closures and 45 000 job losses in the sector in the first half of 2020 (ADB, 2020a). Already weakened before the crisis, the textile industry was gripped by a twin supply-demand shock. On the one hand, supply bottlenecks led to a slowdown in production, with nearly one-third of factories in the garment, textile and footwear industry reported to have closed temporarily (ADB, 2020a). In parallel, international orders have been postponed or cancelled in the context of a general decline in demand.

Figure 1.24. Contribution to GDP growth in Cambodia, 2017-19

Percentage points

Source: OECD Development Centre based on data from CEIC and national sources.
StatLink © http://dx.doi.org/10.1787/888934228704
The economy of Cambodia is anticipated to register growth of -2.9% in 2020, the sharpest decline in decades. If restrictions continue into 2021 in one form or another, the tourism sector will experience a lasting recession. The outlook for private consumption is particularly lacklustre, as the ultimate impact of the crisis on the labour market has yet to be fully ascertained. The World Bank estimates that at least 1.76 million jobs are at risk in Cambodia because of the pandemic (World Bank, 2020a). The return of overseas workers to Cambodia will add to pressure on the domestic labour market and could lead to an increase in the overall poverty rate. Agriculture, the only sector to have been relatively spared from the economic consequences of the COVID-19 crisis, may not be able to absorb the laid-off workers from the tourism sector and the textile industry. The emergency measures put in place by the Cambodian government, such as tax exemptions, allowances for dismissed workers or the facilitation of access to credit with the creation of the Small and Medium Enterprise Bank of Cambodia (SME Bank), should enable a recovery in 2021 (+5.4%).

Real GDP growth in Lao PDR slowed in 2019. The slowdown largely reflects the contraction in the industrial and agricultural sectors (Figure 1.26). In 2020, the Lao economy was hit hard by the pandemic and the containment measures imposed to curb its spread. Private consumption expenditure was affected by adjustments in labour markets and worsening poverty. Exports fell by more than 15% year-on-year in the second quarter of 2020, in the midst of severe supply chain disruptions, which particularly affected the garment industry. The depreciation of the Lao kip (LAK) is exerting additional pressure on the domestic economy. Restrictions on the sale of foreign currency by commercial banks have forced many traders to buy foreign currency from the parallel market. The gap between the official and the parallel exchange rates widened in recent months, while the depreciation of the LAK led to pressure on importers and higher food prices in July 2020 (Figure 1.27).
Real GDP growth for 2020 has been revised downwards, at 0.6%, while the projection for 2021 is of a 5.0% growth. However, risks remain tilted to the downside due to domestic vulnerabilities. The recent decision to continue suspending the issuance of tourist visas for travellers arriving from countries affected by the COVID-19 outbreak will drag on recovery in the important tourism industry. The fall in migrant remittances complicates matters further, hurting foreign exchange reserves and increasing the risk of poverty for as many as 214,000 people in Lao PDR (World Bank, 2020b). In addition, the non-performing
loan (NPL) ratio increased to 3.21% in Q2 2020, from 3.04% at the end of 2019. This will further weaken banks’ balance sheets and could reinforce the downward momentum in Lao PDR’s corporate sector.

The medium-term outlook is overcast by significant downside risks, mostly related to the government’s ability to meet its debt service obligations. The credit rating agency Moody’s recently downgraded the government’s issuer rating from B3 to Caa2. According to the assessment underpinning the rating decision, the country faces serious liquidity problems due to unpaid amounts exceeding USD 1 billion per year in its external debt service until 2025, as well as to the limited financing options available (Moody’s, 2020).

In Myanmar, several hundred cases of COVID-19 have been confirmed per day in recent weeks following months without any. In 2019, the economy grew by 6.8%, mostly driven by consumption and the services sector (Figure 1.28). The first half of 2020 was marked by an extended period of job losses as factories suspended operations and private consumption plunged during Q2. Although industrial production rebounded in August, the manufacturing sector has again been at a near standstill since the second half of September due to the closure of non-essential production sites in the face of rising infections. Exports fell by 13.5% in the first half of 2020, largely due to a contraction in garment exports. Imports, driven by capital goods, rose by 7.8% during the same period.

Growth will decelerate sharply in 2020 (+1.7%) and is seen gathering pace in 2021 (+5.0%), provided the pandemic recedes globally. The outlook remains subdued, as COVID-19 movement restrictions will continue to disrupt economic activity, including agricultural activity. Recovery in manufacturing will likely be very gradual, partly reflecting a lack of momentum in demand. Lower gas prices, in line with the fall in global oil prices and external demand for gas, will also reduce export earnings for Myanmar. The government
will continue to provide loans at reduced interest rates, from the USD 70 million COVID-19 fund, extending an important lifeline to firms in the most affected sectors.

China and India

The number of daily confirmed COVID-19 cases has remained low in China, while swift and targeted measures to address localised outbreaks have shielded the economy from another imposition of nationwide restrictions. China is expected to record positive growth throughout 2020. The strong recovery in Q2 2020 (+3.1%) and Q3 (+4.9%) offset the sharp decline in the first quarter (-6.8%). The recovery is driven by investment and industry, rather than consumption and services, as shown by detailed analysis of the Q3 GDP figures (Figure 1.29). Consumption remained weak and made a negative contribution to year-on-year growth, while investment made a positive contribution. This bifurcated recovery is also reflected in the figures for industrial production and retail trade. The year-on-year industrial production growth rate has accelerated since April, reaching 6.9% in September. The rebound was fuelled in particular by the mining and utilities sectors. Retail sales growth was still negative (-7.2%) in the first three quarters of 2020.

Figure 1.29. Contribution to GDP growth in China, 2018-20
Percentage points

Annual growth in China is expected to reach 1.8% in 2020 and return to its pre-crisis trend from 2021 onwards. Chinese exports have recovered strongly since April, most notably in November. This performance is explained not only by sales of medical products, but also by a strong demand for mechanical, electrical and electronics equipment (Figure 1.30). As restrictions were relaxed earlier than in other parts of the world, China has gained market share, particularly in Europe and the United States. Foreign reserves reached USD 3.1 trillion in September 2020, the level of public debt is relatively low and monetary policy still has some room to deliver cuts. One of the key challenges is related to the sluggishness of private consumption, which could limit the rebound of supply. Despite a rebound in sales of luxury items, labour market strains and falling disposable incomes will keep a lid on aggregate private consumption. In addition, strained relations
with the United States could increase market volatility. There are also growing concerns over stress in corporate credit that could leak to financial markets.

**Figure 1.30. Contribution to export growth in China, March-November 2020**

<table>
<thead>
<tr>
<th>Contribution to year-on-year growth, percentage points</th>
</tr>
</thead>
<tbody>
<tr>
<td>Percentage points</td>
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</table>

Source: OECD Development Centre calculations based on data from CEIC and national sources.
StatLink [https://doi.org/10.1787/888934228818](https://doi.org/10.1787/888934228818)

China will continue to be a hub for investment, as demonstrated by the resilience of foreign direct investment (FDI) and portfolio inflows during the COVID-19 crisis. The outlook is nevertheless weighed down by the recent re-escalation of trade tensions with the United States.

India is anticipated to post a sharp GDP contraction as COVID-19 continues to spread throughout the country. Real GDP contracted more severely than anticipated in Q1 2020 (-23.9%), while the contraction in Q2 was more moderate (-7.5%). The first two quarters of fiscal year 2020/21 were characterised by a sharp compression in consumption (Figure 1.31) as unemployment skyrocketed after the implementation of a national lockdown. The unemployment rate stood at 6.5% in November 2020 (CMIE, 2020). Investment has also dwindled, while government consumption positively contributed to growth. Imports have fallen faster than exports as India continues to grapple with cases of COVID-19 and supply disruptions caused by regional lockdowns. On the supply side, the services sector recorded a deep contraction as retail trade, transport services and the hospitality industry were nearly brought to a halt by the nationwide lockdown measures. Industrial activity was also penalised by remaining COVID-19-related restrictions, while agriculture made a modestly positive contribution to growth.
No tangible acceleration of growth is expected in the final quarters of 2020, and thus GDP growth for the year as a whole is forecast to be around -9.9%, the worst contraction among Emerging Asian countries. Indian GDP should return to positive growth in 2021 (+7.9%), from a low base, but the risk balance is mainly tilted to the downside. With the COVID-19 case curve yet to be flattened, recovery in the services sector will likely lag behind a rebound in manufacturing. Banks’ NPL ratio, which stood at 9.1% on average at the end of 2019, is expected to increase, as small and medium-sized enterprises (SMEs) were heavily strained during the national lockdown. As a result, banks and non-bank financial intermediaries could tighten credit conditions at a time when access to credit is most needed to revive the economy. Weaker investment combined with mobility restrictions will continue to drag on the labour market. At the same time, and despite the improvement in overall financial market resilience, pockets of vulnerability remain. For instance, liquidity risks continue to be elevated in the debt-oriented mutual fund segment (Box 1.4). On the upside, foreign exchange reserves remain at comfortable levels (15.9 months of imports in November 2020), which would help the Reserve Bank of India (RBI) shield the rupee from depreciation.
Box 1.4. Liquidity risks and debt-oriented funds in India

Liquidity risks could remain elevated for debt-oriented mutual funds in India owing to concerns over the viability of the circulating debt papers. A sharp fall in prices could be accompanied by significant redemptions from investment funds. The vast majority of funds in terms of net assets under management are open-ended, suggesting growing preference towards funds that can accommodate continuous flow of capital with lower investment requirements. Open-ended funds are more prone to redemption risks than close-ended funds because the latter have long lock-up periods during which investors cannot redeem shares (Cortes et al., 2018).

The Reserve Bank of India responded with a new credit facility that fund managers can tap into in order to avoid distressed asset sales and ease investor concerns. The RBI offered a credit facility of INR 500 billion (Indian rupees, USD 6.6 billion) that banks can use to lend to mutual funds or to purchase investment-grade debt held by the funds (RBI, 2020a). The scheme was initially available until 11 May 2020, with the RBI committed to reviewing the timeline and amount, depending on market evolutions. Market liquidity improved overall following RBI interventions, but further falls in asset prices or a sharp rise in market volatility could prompt renewed outflows from funds.

Due to concerns about inflation, which breached the upper tolerance band of the 6% target during July-August 2020, the RBI may not be able to implement further rate cuts until the target range is reached. This could add to the pressures on domestic liquidity as the government attempts to revive economic growth. The fiscal balance is expected to deteriorate as the restrictions induced by the pandemic continue to weigh on revenues, adding to concerns over the government’s ability to implement its vast recovery plan, which amounts to 10% of GDP.

Financial markets have stabilised, but vulnerabilities persist

While a systemic financial meltdown was avoided due to parallel interventions by monetary authorities, vulnerabilities remain in several parts of the financial markets. Equity and bond markets have remained quite resilient despite the pandemic-related damage and the resurgence of infections around the world. Although favourable market-financing conditions have helped cushion the economic impact of the pandemic, they may also reveal disconnection of the financial sphere from the real economy. The banking sector remains fragile, with new concerns arising about the soundness of banks’ balance sheets. A negative feedback loop could therefore arise from the real side to the financial side of the economy. Moreover, the large policy interventions have involved governments taking considerable financial risks and have led to deteriorating public finances, which are already under heavy stress due to the decline in economic activity related to COVID-19.

After firming up in the second quarter of 2020, most stock markets in Emerging Asia recorded a slight correction in Q3 and the beginning of Q4. The stock markets of countries that were relatively less affected economically by the pandemic shock, such as Viet Nam, recorded gains during the third quarter of last year, while those of severely affected economies, most notably Indonesia, Singapore and Thailand, underperformed. Throughout 2020, stock markets have been particularly volatile in the Philippines, Thailand and India, as reflected by the wide amplitude between minimum and maximum stock price changes between January and December (Figure 1.32, Panel A). A steady procession of adverse developments, from concerns over rising COVID-19 case tallies to fears of disinflation, has led to a downward revision of corporate profit forecasts. Average
price-to-earnings ratios have plunged close to multiyear lows in Indonesia (Figure 1.32, Panel B), in line with rising uncertainty over corporate earnings. The onset of COVID-19 also gave rise to a decline in initial public offerings (IPOs), with year-to-date volumes as of September 2020 sharply lower, particularly in Malaysia (-81.9%) and Indonesia (-53%). Yet IPO activity could see an uptick in Q4, as several deals were announced in sectors that were spurred by the crisis, such as e-commerce and food delivery, and communication and information technologies.

Figure 1.32. Change in benchmark stock price indices and price-to-earnings (P/E) ratios in Emerging Asian countries

![Change in benchmark stock price indices and price-to-earnings (P/E) ratios in Emerging Asian countries](image)

Note: Latest stock price data are as of 5 January 2021. Data for Q3 2020 are as of end-September. Data refer to the following stock market indices: SSE Composite (China), BSE Sensex 30 (India), JSE Composite (Indonesia), FTSE KLCI Index (Malaysia), PSE Index (the Philippines), FTSE Straits Times Index (Singapore), SET Index (Thailand) and VNI Index (Viet Nam).

Source: OECD Development Centre based on data from Refinitiv Eikon, CEIC and national sources.

Financing conditions have remained relatively favourable overall across Emerging Asia. Since August, benchmark long-term yields have fallen significantly in Indonesia, Singapore and China, leading to a compression of term premia (Figure 1.33, Panel A). By contrast, broader yield declines at the short-end of the curve in Malaysia, the Philippines and, to a certain extent Thailand, reflect investors’ preference for short-dated securities amid rising risk aversion. Over the past few months, the spreads between Emerging Asia government bond yields and US Treasury yields have been broadly stable (Figure 1.33, Panel B), although they have yet to return to pre-pandemic levels in most countries. Both sets of yields staged marked declines in the third quarter of 2020, amid improving sentiment as economic activity showed signs of recovery in Southeast Asian countries and the United States. Conditions in short-term bank funding markets depict a rather mixed picture (Figure 1.34). The recent widening of spreads between three-month interbank rates and equivalent-maturity sovereign yields in Malaysia and the Philippines, seen as a proxy for risks in the banking sector, reflects concern over bank balance sheets as the pandemic exacts its toll on the economy. Inversely, spreads tightened in India, Indonesia and Singapore.
Figure 1.33. Sovereign yield curve and spreads in selected Emerging Asian economies, 2020-21

Note: Data as of 5 January 2021. The yield curve is calculated as the difference between the 10-year sovereign yield and the 1-year sovereign yield. Spreads of 10-year sovereign bonds of selected Emerging Asian economies on 10-year US Treasuries.
Source: OECD Development Centre based on data from Refinitiv Eikon.
StatLink https://doi.org/10.1787/888934228875

Figure 1.34. Spread between three-month interbank rates and three-month sovereign yields in selected Emerging Asian economies, January-December 2020

Note: Latest data for the Philippines and Singapore are as of end-November 2020.
Source: OECD Development Centre calculations based on data from CEIC and Refinitiv Eikon.
StatLink https://doi.org/10.1787/888934228894
Financial markets in Emerging Asia are expected to remain closely tied to developments outside the region. Overall, an unprecedented increase in the debt ratio of Emerging Asian countries is very likely in the coming months. The financial impact from the global downturn has yet to be fully felt, as corporate defaults will possibly continue increasing through 2021. As a result, financial market volatility could surge anew, especially in vulnerable countries where public finances are already under strain or where dependence on debt (public or private) in foreign currencies is high.

**Pressure on bank balance sheets could intensify**

The health crisis also highlights the vulnerability of Emerging Asian economies associated with the rise in debt levels. The level of debt increased between 2019 and the second quarter of 2020. Private sector debt grew alongside public debt, or even faster in the notable case of Thailand (Figure 1.35). When the current debt levels in the private sector are taken into account to complete the picture, Thailand seems to be more exposed to household debt, while Indonesia, Malaysia, Singapore and China are more concerned by the rise in corporate debt. The contraction in income linked to the drop in turnover and the overall deterioration of the market will increase the burden of debt on businesses and households.

Figure 1.35. Level and change in private and public sector
debt in selected Emerging Asian economies, 2020

As a result of uncertainty about the quality of bank balance sheets in Emerging Asia, investors seem to be focusing increasingly on economic rather than regulatory capital. On this basis, the capital adequacy ratio demanded by markets as evidence of bank solvency appears to have moved well above regulatory minima (Figure 1.36, Panel A), which could have significant implications for bank lending activity. There are also downside risks to asset quality. For instance, the value of gross NPLs on bank balance sheets in Indonesia increased sharply in the second quarter of 2020, mostly driven by a spike in non-financial gross corporate NPLs (Figure 1.36, Panel B). The value of gross NPLs in the Thai banking sector also edged higher in Q2, mostly driven by non-financial corporations. Close monitoring, as well as prudent management of non-performing loans, will thus be required.
Pressure on banks’ balance sheets has increased, and the impact may become more acute once debt relief measures are withdrawn. As government support ends, banks could become more risk averse and tighten lending standards to the private sector. Weakening operating conditions, particularly in key sectors such as retail and hospitality, will likely lead to a deterioration in loan performance and profitability. India, and to a lesser extent Lao PDR and Thailand, are most exposed to the economic and fiscal consequences of a shock to the financial sector. Over the medium term, the soundness of the banking sector will be vital for its capacity to provide funding to the real economy.

Current account imbalances will widen as trade and tourism take time to recover

The pandemic will exact a heavy toll on the current account balances of Emerging Asian economies (Figure 1.37) through several channels, especially trade, tourism and remittances by migrant workers. The effects are expected to be particularly acute for major tourist destinations (Figure 1.38, Panel A) and exporters (Figure 1.38, Panel B). Countries with large tourism sectors are anticipated to experience considerable corrections of their current account balances. The collapse in remittance flows, which play a significant role in the domestic economy of many Emerging Asian countries, will be another major driver of deteriorating current account balances in 2020. Remittances by Southeast Asian migrants are forecast to decline by 19.8% in 2020 (ADB, 2020b), while the World Bank foresees a rebound of merely 6% in 2021 (World Bank, 2020c).
1. Macroeconomic Assessment and Economic Outlook in Emerging Asia

Figure 1.37. Current account balances in Emerging Asia, 2020-21

Note: Data are as of 5 January 2021. Data for India and Myanmar relate to fiscal years. The projections for China, India and Indonesia for 2020 and 2021 are based on the OECD Economic Outlook, December 2020.
Source: OECD Development Centre.
StatLink: https://doi.org/10.1787/888934228932

Figure 1.38. Change in current account balance, trade balance and visitor arrivals in selected Emerging Asian economies

Note: Data on trade balance and tourist arrivals represent totals between January and October 2019 and, respectively, January and October 2020. Latest data on trade balances are as of September 2020 for Brunei Darussalam and August 2020 for Cambodia. Latest data on visitor arrivals are as of September 2020 for Malaysia and July 2020 for Myanmar.
Source: OECD Development Centre; CEIC; national sources; and IMF World Economic Outlook database (October 2020).
StatLink: https://doi.org/10.1787/888934228951
Foreign direct investment flows into Emerging Asian countries are trending downwards (Figure 1.39). As net FDI tends to flow out of advanced economies towards emerging economies, the economic downturn in the former group of countries is the main driver of diminishing inflows in the latter. Although all industries have been affected, the impact will be stronger in several services sectors, including aviation and tourism, as well as in manufacturing industries that are intensive in global value chains (GVCs). FDI inflows in June hovered near multi-year lows in Brunei Darussalam, China, India, Indonesia, the Philippines and Thailand. By contrast, FDI proved to be more resilient in Viet Nam, where inflows in the first half of 2020 were roughly equal to those in 2019 over the same period.

**Figure 1.39. Foreign direct investment in Emerging Asia, 2018-20**

USD billion, annualised

As financing conditions remain less favourable than before the pandemic, some Emerging Asian countries might face greater challenges financing larger current account deficits. However, the unprecedented portfolio outflows during the sell-off triggered by COVID-19 seem to have stabilised in June, as most countries in the region recorded net inflows. The acute portfolio outflows recorded in the first quarter of 2020 seem nevertheless to have weakened domestic currencies. Overall, countries where the current account position is expected to deteriorate in 2020 have experienced much larger depreciations in nominal effective terms, while countries where the current account position is forecast to improve have seen their currencies appreciate (Figure 1.40, Panel A). Reserve accumulation increased in several countries in the region (Figure 1.40, Panel B), in line with the deterioration in current accounts, partially attenuating the strain induced by higher deficits. Despite the fact that accumulating reserves helps to cushion economies against foreign currency shocks, holding excessive levels of reserves could trigger price distortions in exchange rates.
Figure 1.40. Current account balance, Nominal Effective Exchange Rate (NEER) and official reserves of selected Emerging Asian economies

A. Change in current account balance versus change in NEER
Average of monthly year-on-year changes of the NEER between January and November 2020, percentage

B. Official reserve assets (end-period)
USD billion

Source: OECD Development Centre and data from the Bank for International Settlements and the IMF World Economic Outlook database (October 2020).
StatLink: https://doi.org/10.1787/888934228989

Looking ahead, economic stability in Emerging Asian economies could be undermined by renewed capital outflows and currency depreciations.

Rebound in Chinese economy benefits ASEAN exports

The net trade balances of Emerging Asian economies have started to improve in the second quarter of 2020, supported by increased demand from major trading partners. China and the United States have been the main drivers of export growth, while intra-ASEAN exports remained weak. In the first half of 2020, trade between ASEAN and China increased by 5.6% year-on-year and these trends are reflected in the growth of China’s share in the total exports of several ASEAN countries between the first and the second quarters of 2020 (Figure 1.41). Exports to China recorded double-digit growth rates in several ASEAN member countries, in a context of falling trade volumes overall. Malaysia benefited the most from increasing Chinese demand, with exports to China inching 16.3% higher year-on-year in Q2, even as total exports fell by 15% over the same period. The expansion of ASEAN-China trade was partly supported by growth in agricultural trade, but also by exports of medical supplies and teleworking-related equipment.
In several Emerging Asian countries, the slump in exports was very large during April-May 2020. A key factor for these cross-country differences is the sectoral composition of exports. Diminishing exports of machinery and transport equipment were the main driver of the contraction in goods trade in Malaysia in the early stages of the crisis, while they contributed to the rebound throughout June-October, together with vegetable oil and fats (Figure 1.42). For Indonesia, a sizeable drop in mineral fuel exports was partly offset by commensurate exports of manufactured goods, chemical products and food items (Figure 1.42). In Singapore, falling exports of crude materials had the largest contribution to the overall decline in the most recent months (Figure 1.42).
Export growth is anticipated to gain traction in the second half of 2020, in tandem with the recovery in the main trading partners of Emerging Asian countries. This notwithstanding, the COVID-19 crisis is set to weigh heavily on exports for the year as a whole and continue to exert a negative impact into 2021. Supported by pent-up demand, exports of goods are expected to outperform those of services. The latter will be dampened by a slow normalisation in hospitality and transportation services, as travel restrictions and income losses take their toll. Recovery in the medium term will be held back by the enduring global aftershocks of the crisis. On the upside, the RCEP and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) trade agreement are expected to deliver benefits to the most trade-oriented Emerging Asian countries over the next years (Box 1.2).

**Inflationary pressures remain low due to ongoing slack in the economy**

Inflationary pressures in Emerging Asian countries are subsiding as the pandemic-induced global recession leaves its mark on both global and domestic factors underpinning price developments. Headline inflation fell into negative territory in Malaysia, Singapore and Thailand, and has remained there since March, mostly driven by the substantial drop in core inflation (Figure 1.43). The marked decline in core inflation mostly reflects an easing in services inflation and falling demand for durable goods, as non-essential businesses were ordered to close during the lockdown period and households reduced discretionary spending. Energy prices also contributed to the decline, while food prices increased during the lockdown period, affected by supply chain disruptions.
The effect of the sharp weakening in activity is particularly visible in producer price inflation. Producer prices fell sharply in the second quarter of 2020 (Figure 1.44), on the back of sharply decelerating prices for energy inputs. However, the pace of the drop in producer price inflation seems to have slowed in Q3, suggesting an easing of downward pressures. Available survey data on input and output prices suggest that the general weakening of economic activity in Q2 2020 may have induced some revisions to pricing strategies in both the manufacturing and services sectors. Signs of rising agricultural prices are visible in Thailand, but they can be mainly attributed to a severe drought that battered the country’s rice and aquaculture production (USDA, 2020).
With regard to the situation in individual Emerging Asian countries, inflation remains low in Indonesia due to weak domestic demand and continued exchange rate stability (BI, 2020a). In Malaysia, headline inflation declined slightly in August, mainly due to lower fresh meat and fuel inflation (Bank Negara Malaysia, 2020). Philippine headline inflation eased to the slowest rate in three months in August, owing to a deceleration in food prices, while core inflation inched up, driven by transportation and communication (PSA, 2020). In Thailand, headline inflation edged higher in September, as food prices increased because of supply-side factors, while core inflation firmed up due to the smaller than anticipated impact of government measures to reduce utility bills (BOT, 2020b). In Singapore, both headline and core inflation came in higher in August, the former due to a more gradual decrease in private transport costs, while the latter was primarily driven by smaller declines in the cost of services and electricity and gas (MAS, 2020f). China’s CPI inflation also moderated in October due to lower food price inflation and in particular the rapid decline of pork prices. India’s headline inflation breached the upper tolerance band of the target during June-August 2020, propelled by upside pressures stemming from supply chain disruptions and higher taxes on petroleum products (RBI, 2020b), and it accelerated in October on account of a further rise in food prices due to heavy rain and a hike in fuel taxes.

Risks to the inflation outlook appear broadly balanced. The outlook will continue to be affected by global oil and commodity prices. An increase in oil and commodity prices implies upward price pressures, but these are expected to be largely offset by downward pressure from the remaining slack in the economy. Notwithstanding market expectations of higher inflation as the new US administration has pledged more stimulus, external inflation is also forecast to remain at low levels, as negative output gaps are likely to persist in the major trading partners of Emerging Asian countries. However, core inflation could edge slightly higher in 2021, with demand for some domestic services anticipated to pick up gradually as remaining restrictions to curb the spread of the virus are removed.

**Labour markets suffer biggest blow in decades due to health crisis**

The labour market in Emerging Asia is undergoing a pronounced slowdown due to the COVID-19-related containment measures, with significant job losses occurring across many countries. The labour market response to the global slowdown varies considerably across Southeast Asian countries, with differences in the share of the most affected industries, pre-existing vulnerabilities, exposure to international trade, and public support policies in response to the pandemic. Recourse to teleworking and flexible working arrangements has also differed markedly across countries.

Compared to 2019, the most pronounced increases in unemployment are expected in the Philippines, Indonesia and India (Figure 1.45). Workers with weaker contracts and less experience have borne the brunt of the current downturn. In Malaysia, for instance, the unemployment rate for young people (15 to 24 years) increased by 2 percentage points (pps) in the second quarter of 2020, compared to the same period in 2019, above the 1.8 pps increase in the total unemployment rate, while the same tendency was observed in Q3 (Figure 1.46, Panel A). Similarly, the number of persons unemployed in the 25-29 age group in Thailand increased more than the figure for the total population in both the second and third quarters of 2020 (Figure 1.46, Panel B).
Figure 1.45. **Unemployment rate in selected Emerging Asian economies**

<table>
<thead>
<tr>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
</tr>
<tr>
<td>2020 September</td>
</tr>
<tr>
<td>2020 forecast</td>
</tr>
</tbody>
</table>

Note: The 2020 forecast for India is not available. The September 2020 unemployment rate for Indonesia is not available.

Source: OECD Development Centre based on data from CEIC, national sources and IMF World Economic Outlook database (October 2020).

StatLink [https://doi.org/10.1787/888934229065](https://doi.org/10.1787/888934229065)

Figure 1.46. **Change in unemployment by age group in Malaysia and Thailand, 2019-20**

Source: OECD Development Centre based on data from CEIC and national sources.

StatLink [https://doi.org/10.1787/888934229084](https://doi.org/10.1787/888934229084)

Looking at previous recessions can give clues about the extent to which the current labour market adjustment is congruent with past experiences. In previous recessions, unemployment spiked quickly but fell back during the year that followed the recession.
(Figure 1.47). There is a striking contrast between the behaviour of unemployment during the recessions of the 1990s and late 2000s and the current downturn. Indeed, the unemployment rate in Malaysia, the Philippines and Thailand increased faster in the two quarters since the onset of the COVID-19 crisis compared to the same period of past crisis events. This reflects the unprecedented nature of the current crisis, and a key question is to what extent the actual increase in unemployment fully reflects the decline in output observed so far.

Figure 1.47. Changes in unemployment around recession periods in selected ASEAN economies, 1991-2020

Note: Recessions are defined as two consecutive quarters of negative real GDP growth. The horizontal axis reports the starting and ending quarter of the recession. Data on quarterly GDP growth for Malaysia are only available starting from Q1 2001. Data on the quarterly unemployment rate in Thailand are not available for the period Q2 1997 to Q4 1998, which has also been identified as a recession. “Change in unemployment rate during the recession” refers to the difference between the unemployment rate prevalent in the ending quarter of the recession and the unemployment rate prevalent in the starting quarter. “Change in the unemployment rate during the year following the end of the recession” refers to the difference between the unemployment rate four quarters after the end of the recession and the unemployment rate prevalent in the ending quarter of the recession. The 1991 Philippine recession was triggered by a combination of fiscal imbalances and exogenous shocks, including worldwide interest rate increases and an unprecedented succession of natural disasters.

Source: OECD Development Centre based on data from CEIC and national sources.

https://doi.org/10.1787/888934228020

Given the crucial role of the labour market for a sustained recovery to materialise, a major challenge is to halt the worsening of labour market conditions. With substantial restructuring across certain sectors to be expected in some Emerging Asian countries, part of the challenge will be to reduce the skills mismatch and facilitate the reintegration of displaced workers into employment. The provision of government support to pay for a portion or the entirety of such training schemes could be an option. For instance, as part of its COVID-19 stimulus, Singapore is offering a 6-12 month training programme, which includes monthly allowances to cover participants’ living expenses (SSG-WSG, 2020). The implementation of this type of measure will undoubtedly take time, but decisions taken early will help to anchor expectations and underpin the recovery.
Box 1.5. Consumer behaviour in times of large external shocks: Evidence from natural disasters

Several studies have investigated whether large external shocks, such as natural disasters or extremely disruptive civil conflicts, have an effect on consumption. In particular, Miguel and Roland (2011) explore the long-run impact of the war in Viet Nam on local economic conditions. The authors find a moderate negative effect of the conflict on consumption levels through 1992-93, but also faster consumption growth between 1992-93 and 2002. In a similar vein, Gignoux and Menendez (2016) study the short and long-term effects on individual economic outcomes of a set of earthquakes in rural Indonesia since 1985. The empirical estimates show that an earthquake reduces household per capita consumption in the short run (i.e. between year t and year t-1), but that this negative effect fades away and eventually turns out to be positive and statistically significant in the long term. These results suggest that any negative short-run impact from the large external shock on consumption dissipated over time, consistent with the permanent income hypothesis posited by Milton Friedman (1957). Moreover, the impact of natural disasters largely depends on the intensity and duration of the disaster. For instance, Baez et al. (2015) investigate the causal consequences of tropical storm Agatha (2010) on household welfare in Guatemala. The authors find that households reduced food consumption by 10% on average, with a larger impact among urban households, for which average per capita consumption dropped by 12.6%. This difference is attributed to the strength of the shock itself, excessive precipitation being much stronger in urban areas.

Analysis of consumer behaviour in the aftermath of selected natural disasters in the Philippines and Thailand shows that consumption fell within the quarter immediately following the disaster in both countries, though the level of reduction varied by countries (Figure 1.48, for more details, Tanaka, Ibrahim and Hean, 2021). However, in line with the literature (Miguel and Roland, 2011; Gignoux and Menendez, 2016) and the permanent income hypothesis (Friedman, 1957), the study finds that private consumption returns to pre-disaster levels after the event for both countries.

Figure 1.48. Private consumption behaviour in the aftermath of selected natural disasters in the Philippines and Thailand

A. Thailand (Indian Ocean earthquake and tsunami, 2004)
B. Philippines (Typhoon Bopha, 2012 and Haiyan, 2013)

Note: The data represent quarterly household consumption. “THB” stands for Thai baht and “PHP” stands for Philippine peso.

Source: OECD Development Centre, based on Tanaka, Ibrahim and Hean (2021).
StatLink https://doi.org/10.1787/8889342227944
Box 1.5. Consumer behaviour in times of large external shocks: Evidence from natural disasters (cont.)

The change in consumption behaviour in crisis times is asymmetric across different categories of goods. It is well documented that purchases of non-essential goods can be easily postponed, but when the reason for postponement wanes some portion of the missing demand tends to recover (Hai et al., 2013). For instance, Forbes (2017) studied short-term consumption patterns in the aftermath of the 2011 earthquake in Christchurch, New Zealand. The study shows that immediately after the event, namely within the first week, consumers mostly purchased essential items, such as water, non-perishable food, products providing communication services and cleaning products (Forbes, 2017). Anttila-Hughes and Hsiang (2013) assess the economic effects of typhoons in the Philippines. They conclude that the typhoon-induced income losses translate into a 7.1% decrease in household expenditures, with the sharpest adjustments on items that most closely resemble human capital investments, such as medicine, education and high-nutrient food. By contrast, expenditure declines much less on pure consumption goods, namely recreation, alcohol and tobacco.

A growing number of studies explore the consumption effect of the COVID-19 outbreak on different expenditure items in advanced economies and, to a lesser extent, in Emerging Asian countries. For instance, Baker et al. (2020) use card transaction data for the United States. The authors show that spending increased sharply at the beginning of the pandemic, particularly in retail, credit-card spending and food items, while spending on restaurants, air travel and public transport fell sharply in mid to late March (Baker et al., 2020). As for Emerging Asia, Mishra and Dhanerwal (2020) assess the impact of the COVID-19 pandemic on consumption demand for non-essential commodities in India. The empirical findings indicate that people deferred the consumption of goods classified as discretionary (i.e. domestic tourism, automobiles or real estate) by a few months.

Digital transactions in Emerging Asia surpass expectations

E-commerce markets in Emerging Asia have maintained double-digit growth since 2015, and this trend is likely to continue in the medium term. ASEAN’s e-commerce market is expected to see a compound annual growth rate (CAGR) of 20%, with this market in China and India growing by 12.5% and 17.7%, respectively. By the end of 2020, the combined e-commerce revenue of Emerging Asia will account for half of that of the global market, increasing from a combined share of 43% in 2017.

The outbreak of COVID-19 has driven digital transaction growth, which is expanding much more quickly than forecast in 2017 (Figure 1.49). With the implementation of physical distancing and lockdowns, e-commerce has provided effective solutions for the support of daily life. This is changing the behaviour of both consumers and producers. In Indonesia, Lao PDR and Myanmar, for example, the e-commerce market will increase by nearly 50% between 2019 and 2020.
The year-on-year (YoY) increase in e-commerce revenue between 2019 and 2020 is projected to reach USD 17 billion in ASEAN, USD 253 billion in China and USD 13 billion in India. In comparison, the YoY increase from 2018 to 2019 stood at USD 11 billion in ASEAN, USD 142 billion in China and USD 8 billion in India. From 2020 to 2021, it is expected to amount to USD 13 billion, USD 143 billion and USD 9 billion, respectively. The ASEAN market is expanding rapidly, with total e-commerce revenue surpassing India’s in 2018 and the gap expected to narrow over time with China, the world’s largest e-commerce market.

Indonesia is ASEAN’s largest and fastest growing e-commerce market, contributing to more than half of the region’s e-commerce revenue since 2018. Thailand and Viet Nam follow as the second and third largest e-commerce markets. The ranking is not likely to change in the next five years, but Indonesia’s market share is expected to expand to 57% in 2024, while the combined share of Thailand and Viet Nam is projected to decrease from 25% in 2019 to less than 22% in 2024. Myanmar, the Philippines, Malaysia and Lao PDR are projected to maintain growth, with a CAGR higher than 20%. The distribution of e-commerce revenue in ASEAN is not strictly proportional to the distribution of e-commerce users (Figure 1.50).

Source: OECD Development Centre, based on data from Statista.
StatLink  
https://doi.org/10.1787/888934229122
E-commerce penetration is rising across the region

From 2019 to 2020, the number of e-commerce users is projected to increase by 37 million in ASEAN, 71 million in China and 50 million in India. Figure 1.51 displays the increasing number of e-commerce users and the changes in per-user online spending between 2019 and 2020. By the end of 2020, more than 60% of the Chinese population will have shopped on line at least once. E-commerce penetration in ASEAN will increase to nearly 44% in 2020 from 38% in 2019, while in India it will increase to 40% from 36%.

Figure 1.51. Increasing e-commerce penetration and average revenue per user, 2019-20

The reason for the increasing value of average revenue per user (ARPU) could be that consumers are purchasing higher-value products on line, but it is more likely that users are shopping on line more often. Assuming there is no significant change in the price index of products traded on line between 2019 and 2020, the frequency of each user’s online shopping is projected to increase by 17% to 30%.1

In both ASEAN and India, most goods sold on line are electronics and media products or fashion items, while in China the top two groups are fashion items and toys, hobby and DIY (Table 1.3).

Table 1.3. Goods sold on line in Emerging Asia, 2019

<table>
<thead>
<tr>
<th></th>
<th>Electronics and media</th>
<th>Fashion</th>
<th>Food and personal care</th>
<th>Furniture and appliances</th>
<th>Toys, hobby and DIY</th>
</tr>
</thead>
<tbody>
<tr>
<td>ASEAN</td>
<td>27.0% (25.0%)</td>
<td>26.7% (27.1%)</td>
<td>16.6% (17.7%)</td>
<td>14.7% (14.6%)</td>
<td>15.6% (15.6%)</td>
</tr>
<tr>
<td>China</td>
<td>20.2% (18.3%)</td>
<td>25.2% (25.5%)</td>
<td>17.1% (19.3%)</td>
<td>12.8% (11.9%)</td>
<td>24.7% (24.9%)</td>
</tr>
<tr>
<td>India</td>
<td>33.9% (32.1%)</td>
<td>28.4% (28.7%)</td>
<td>20.3% (22.8%)</td>
<td>6.1% (5.7%)</td>
<td>11.4% (10.6%)</td>
</tr>
</tbody>
</table>

Note: The figures in parentheses are the estimated values for 2020. DIY stands for “do it yourself”. Source: Statista.

However, food and personal care products are expected to increase their online market share. This market, worth USD 160 billion in 2019, is projected to expand by nearly 50% to reach nearly USD 240 billion by the end of 2020, a growth rate higher than the other product groups (Table 1.4). In Thailand, food and personal care products are expected to take as
much market share as electronics and media in 2020. One possible driver is that improved e-commerce connectivity and services make it easier for consumers to place orders and get products delivered on time. Another could be changes in consumer behaviour due to lockdowns and physical distancing during the COVID-19 pandemic.

Table 1.4. E-commerce revenue, year-on-year changes 2019-20

<table>
<thead>
<tr>
<th></th>
<th>Electronics and media</th>
<th>Fashion</th>
<th>Food and personal care</th>
<th>Furniture and appliances</th>
<th>Toys, hobby and DIY</th>
</tr>
</thead>
<tbody>
<tr>
<td>ASEAN</td>
<td>1.34</td>
<td>1.48</td>
<td>1.60</td>
<td>1.43</td>
<td>1.45</td>
</tr>
<tr>
<td>Brunei Darussalam</td>
<td>1.26</td>
<td>1.27</td>
<td>1.33</td>
<td>1.26</td>
<td>1.25</td>
</tr>
<tr>
<td>Cambodia</td>
<td>1.33</td>
<td>1.42</td>
<td>1.52</td>
<td>1.47</td>
<td>1.38</td>
</tr>
<tr>
<td>Indonesia</td>
<td>1.38</td>
<td>1.51</td>
<td>1.61</td>
<td>1.48</td>
<td>1.52</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>1.39</td>
<td>1.49</td>
<td>1.63</td>
<td>1.53</td>
<td>1.47</td>
</tr>
<tr>
<td>Malaysia</td>
<td>1.34</td>
<td>1.44</td>
<td>1.38</td>
<td>1.37</td>
<td>1.30</td>
</tr>
<tr>
<td>Myanmar</td>
<td>1.41</td>
<td>1.50</td>
<td>1.66</td>
<td>1.54</td>
<td>1.47</td>
</tr>
<tr>
<td>Philippines</td>
<td>1.37</td>
<td>1.28</td>
<td>1.64</td>
<td>1.46</td>
<td>1.48</td>
</tr>
<tr>
<td>Singapore</td>
<td>1.30</td>
<td>1.31</td>
<td>1.37</td>
<td>1.31</td>
<td>1.31</td>
</tr>
<tr>
<td>Thailand</td>
<td>1.23</td>
<td>1.35</td>
<td>1.74</td>
<td>1.37</td>
<td>1.42</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>1.32</td>
<td>1.37</td>
<td>1.46</td>
<td>1.34</td>
<td>1.35</td>
</tr>
<tr>
<td>China</td>
<td>1.17</td>
<td>1.31</td>
<td>1.47</td>
<td>1.20</td>
<td>1.31</td>
</tr>
<tr>
<td>India</td>
<td>1.31</td>
<td>1.39</td>
<td>1.55</td>
<td>1.30</td>
<td>1.30</td>
</tr>
</tbody>
</table>

Source: Statista.

Cross-border digital transactions are growing, and e-payment is increasingly popular

Domestic e-commerce still dominates in all markets, but cross-border e-commerce is steadily increasing its share, particularly in China (Figure 1.52). By the end of 2019, cross-border e-commerce accounted for around 6% of total e-commerce revenue in India and 1.6% in China. The cross-border e-commerce market is projected to expand by 150% in India and nearly 300% in China in 2024.

Figure 1.52. Cross-border e-commerce in China and India

At the same time, the use of e-payment tools is becoming increasingly popular in the region (Figure 1.53). Consumers in China, India and Indonesia are using the e-wallet as their preferred form of payment for e-commerce. By the end of 2019, nearly two-thirds of online
purchases in China were made via e-wallet, while the share in India increased from 26% in 2017 to 43% in 2019 and is projected to increase to 70% by 2022. In comparison, the share of cash on delivery is shrinking rapidly, especially in India, the Philippines and Indonesia.

Figure 1.53. Forms of payment used in selected Emerging Asian countries

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Indonesia</th>
<th>Malaysia</th>
<th>Philippines</th>
<th>Singapore</th>
<th>China</th>
<th>India</th>
</tr>
</thead>
<tbody>
<tr>
<td>E-wallet</td>
<td>0%</td>
<td>20%</td>
<td>30%</td>
<td>40%</td>
<td>50%</td>
<td>70%</td>
</tr>
<tr>
<td>COD</td>
<td>90%</td>
<td>70%</td>
<td>60%</td>
<td>50%</td>
<td>40%</td>
<td>30%</td>
</tr>
</tbody>
</table>

Note: “COD” stands for cash on delivery.
Source: Statista.
StatLink: https://doi.org/10.1787/888934229160

Governments have encouraged people to choose cashless payment during the pandemic in order to minimise physical contact and lower the chance of viral transmission. This has accelerated the decline of cash-on-delivery and reinforced increased use of e-wallets.

Comprehensive strategies are needed to maximise the use of e-commerce

The global boom in e-commerce and its acceleration during the COVID-19 crisis is changing mindsets, for example by helping micro, small and medium sized enterprises (MSMEs) to maintain their business operations during lockdowns. To maximise the use of e-commerce, Emerging Asia needs more holistic strategies at both the national and regional levels. Governments should adopt digital tools to improve the coverage and quality of online public services. They should also create better conditions for self-learning. Partnerships with the private sector should be particularly encouraged. In addition, policy makers need to ensure that antitrust rules are fit for the digital age.

Risks to growth and policy challenges in light of COVID-19

Overall, Emerging Asian economies are anticipated to initiate a recovery over the medium and near term as the COVID-19-induced downturn gradually dissipates. However, several risks could derail the growth momentum:

- Given the potential for new local and national surges in COVID-19 cases, policy makers in Emerging Asia need to strengthen their health care management strategies continuously and, most notably, guarantee the quick and large-scale deployment of COVID-19 vaccines as soon as these become available.
• Although the scope for additional monetary policy rate cuts is limited in most Emerging Asian countries, the focus of monetary policy will likely need to shift to improving policy transmission. Several policy options could be envisaged in this regard.

• On the fiscal front, the most pressing challenge is to continue to develop policy programmes that address the legacy of the crisis, while restoring fiscal rectitude.

Current health situation and challenges in the fight against COVID-19

The emergence of the COVID-19 pandemic came unexpectedly and posed new challenges for the region and the world at large. It also highlighted pre-existing challenges that had been identified and addressed over the years, particularly in the health care field. Each country’s initial government response to the pandemic provides an insight into the level and sophistication of the policy tools implemented to face these challenges. Amid the spread of the coronavirus, and an increasingly enhanced scientific understanding of its nature, governments were able to adapt their policy tools to contain the virus while attempting to minimise the negative socio-economic effects as much as possible. This careful balancing act has been challenging for every country in the region. But with vaccine deployment efforts on the horizon, governments will gradually be able to reduce containment restrictions and position their countries for a sustainable economic rebound.

Moving forward, it is important to implement optimal health responses to the current situation and to understand the vulnerability of Emerging Asian countries post-COVID in the face of many uncertainties. Short-term health policy responses to help the region in the aftermath of the crisis include: i) scaling up current good practices; ii) better allocation of resources; and iii) safe and efficient distribution of a vaccine.

Policy makers need to scale up health responses to the pandemic

The pandemic is forcing governments to make quick decisions and take drastic actions to protect the region. Despite differing levels of health preparedness across countries, overall health policy responses from Emerging Asia have been efficient and effective in limiting the virus from spreading. Public health responses relying on human behaviour are economical and easy to implement: wearing masks, washing hands, covering the mouth and nose when coughing or sneezing, disinfecting surfaces and physical distancing. Policy makers should therefore keep raising public awareness about personal hygiene through government campaigns, the news media and social media.

Singapore’s Ministry of Health has published multiple easy-to-implement action infographics in the English, Chinese, Malay and Tamil languages (MOH, 2020a). The infographics highlight a variety of actions that can be taken to suppress the spread of the virus. These include public service announcements on how to maintain personal hygiene and physical distancing, and more general health information. The Health Ministry has also published videos of the prime minister and experts talking about the current COVID-19 situation. Similar awareness-raising actions have been widely introduced, including COVID-19 related governmental info webpages, hotlines and guidelines.

Given the risk of lockdown fatigue, governments need to demonstrate a continuous commitment to prevention and control measures, and must urge the public to stay vigilant to any potential resurgence until a vaccine or effective treatments are widely available. Some countries have started to lift restrictions on social and economic activities. The reopening should be gradual and closely monitored to avoid repeated waves. Continued adherence to safe management measures should be promoted, such as pre-event testing, regular temperature scans and a limit on the number of attendees at public events.
Reopening measures and the lifting of restrictions vary among Emerging Asian countries. Almost every country in the region closed its borders at some point (IMF, 2020). Larger countries like Malaysia, Thailand and Viet Nam introduced very strict policies for opening their borders to foreign citizens after closing them at the outset of the pandemic. Foreigners meeting certain conditions may enter Thailand; Malaysia has kept its borders closed, with very limited exceptions; and Viet Nam has kept its borders closed to all foreign tourism (DDC, 2020; IMF, 2020). In contrast, Singapore has kept its borders open because its economy very heavily depends on this. Singapore’s published roadmap on lifting restrictions includes guidelines on testing, contact tracing and safe distancing, among other measures that will be used while moving back to the pre-pandemic situation. The Philippines introduced a roadmap for the COVID-19 vaccine rollout in November (PNA, 2020b).

With COVID-19 still posing a huge threat to communities, an effective regime of testing, contact tracing and case management needs to be prioritised to cope with high case numbers and to prevent new clusters from forming. Sufficient testing is needed to detect both symptomatic and asymptomatic individuals. In cases of a community outbreak, a spike in testing may occur, with a potentially long wait between a positive test result and directing close contacts to quarantine. Relevant authorities should thus try to maximise the likelihood of self-quarantine of people awaiting results. After the results are verified, the confirmed cases should be contacted rapidly and ordered into immediate isolation at home or in a supervised facility. Contact tracing is another key strategy to contain the virus.

The World Health Organization (WHO, 2020a) suggests that extensive testing is a key to suppressing the virus. The countries in the region differ in how they report daily tests, and some countries do not report the extent of testing at all. In general, richer countries tend to test more than poorer countries (Hasell et al., 2020). Extensive testing also helps track the virus, and it has been mentioned as a way of keeping societies open if all the new cases can be found and the patients can be quarantined.

Several concerns have been raised following an increase in testing numbers, most notably compliance with proper testing standards. In April 2020, the Philippines, similarly to other ASEAN countries, quickly established guidelines for clinics to secure a license in order to operate COVID-19 testing laboratories. The guidelines were originally implemented for ensuring the safety of patients and the quality of the tests, while also providing a strategy to expand testing capacity (Philippines Department of Health, 2020b). In November 2020, the Department of Health had to issue an advisory on health facilities offering COVID-19 testing services, reminding them that health facilities must be licensed and that offenders would be subject to penalties. The advisory was issued in response to evidence that some health facilities were not following the mandatory guidelines (Philippines Department of Health, 2020c). This development is a reminder of both the pressing need for better enforcement of the testing guidelines as testing capacity increases, and of the need for governments to continue to have an active role in guiding both patients and health care providers during the pandemic.

**Resources can be reallocated to prevention as the health crisis stabilises**

COVID-19 has created opportunities to reform health care systems in ways that were rarely possible during ordinary times. A government has the obligation to ensure the provision of health care for all, which cannot be achieved without adequate staffing and sufficient medical equipment. There is still a real need for health professionals in hospitals, both in big cities and in rural or remote areas, where health staff is typically sparser. The workforce needs to be expanded and ongoing investment in training and education of health professionals should be provided for a more sustainable health care system.
With the stabilisation of the COVID-19 situation in more countries, the health care focus could be shifted from treatment back to prevention. Persistent shortages of critical medical supplies, such as personal protective equipment (PPE), present a danger not only to the public but also to doctors and nurses. Health care workers are more vulnerable than the general population due to their frequent contact with infected individuals and long working hours under stressful conditions. Health care systems were overstretched in the early stages of the pandemic. As the crisis eases, policy makers need to maintain a skilled and qualified workforce by ensuring adequate supplies of PPE, including face masks, goggles, face shields, gloves and protective suits.

As the number of cases soars in some countries within the region, hospital capacity is another important policy focus. During a pandemic, hospital beds are used as an indicator of health care service availability. In the event of an outbreak, the influx of patients can rapidly lead to hospital saturation. More hospitals thus need to be planned and built, and this requires the readying of space, human capital and equipment. Demand for critical care resources, such as ventilators and beds in intensive care units, can be high during disease outbreaks, especially in rural areas and smaller hospitals. Individuals should have equal access to health care facilities regardless of location of residence.

Emerging Asian nations have performed traditional and modernising proactive measures to address the overstretching of health care systems and to confirm the availability of resources. For example, Lao PDR has budgeted nearly USD 2.6 million for protective gear and received more than USD 11.2 million in donations, both in kind and in cash (IMF, 2020). Malaysia responded to the lack of accurate data and inefficient resource allocation by publishing an e-COVID19 system, which shares real-time data and ensures efficient reporting and usage of information among government officials (MAMPU, 2020).

As the Philippines eased lockdown measures, the government recognised that it should allocate substantial resources to draft and apply policies that encourage physical distancing as a primary preventive tool. It enacted an administrative order with guidelines on the proper use of transportation during and following the COVID-19 pandemic, with a broad multilateral approach including the departments of Health, Transportation, Interior and Local Government, Public Works and Highways (Government of the Philippines, 2020). The guidelines address challenging issues like maintaining physical distancing inside a public bus or tram, and they promote alternative modes of transport such as cycling and walking, with instructions for local governments and agencies on building more adequate walking and cycling infrastructure networks.

Thailand is making substantial efforts to attract foreign investment to increase its industrial base for medical supplies in an attempt to address the COVID-19 situation and to develop the country’s potential as a hub for medical products. According to the government, Thai and international investors filed 50 project applications for the medical sector during the first half of 2020, at a total value of USD 400 million. The projects include the production of medical devices or supplies, including masks and gloves (Government of Thailand, 2020a). This will also allow the country to build its preventive capacity by ensuring a stable supply of PPE. The Thai government has even dispatched millions of masks to citizens of neighbouring countries, notably Myanmar in October (Government of Thailand, 2020b). These developments are a testament to Thailand’s engagement within ASEAN, and they provide a glimpse of the country’s future engagements following its current increase in PPE production.

Japan is increasing its allocation to technological advances in its quest to stop COVID-19, envisaging greater use of its supercomputing capabilities. Fugaku, the fastest supercomputer in the world, is expected to play a prominent role in the global fight against the coronavirus. The computer is currently in the process of being built and is planned to be fully operational by 2021. Its capabilities will be focused on solving societal problems such as disaster prevention and environmental protection (Government of Japan, 2020).
The trial version of the computer was used for COVID-19 research, initially coming to the conclusion that masks are indeed an effective tool for helping curb the spread of the virus. The computer was also used for COVID-19 drug research, where it demonstrated its impressive calculation speeds by analysing 2 128 potential drugs and narrowing them down to a few dozen. The government of Japan believes that Fugaku will play an increasing role in preventing outbreaks and combatting COVID-19 in the near future (Government of Japan, 2020).

**Obtaining and distributing a vaccine is a challenging priority**

Researchers around the world are racing to develop, test and produce a vaccine against COVID-19. Vaccines produced by Indonesia’s Bio-Farma working with China’s Sinovac are in the final stage of clinical trials. Singapore and Viet Nam are also at various stages of vaccine development. Although developed countries may have a higher success rate in finding a vaccine, Emerging Asian countries can potentially operate as a manufacturing hub to facilitate production and distribution in order to meet global needs. China is the global leader, with five final-stage vaccines. Indonesia and Singapore are developing vaccines in co-operation with global pharmaceutical companies, while Viet Nam and Thailand have co-operation projects as well as sovereign projects.

As of mid-December no vaccine had received WHO authorisation for use, but the first approvals were expected in late December or in early 2021. Three vaccines have been approved by national authorities, and two more have been proven efficient and safe in clinical research (WHO, 2020b). The Pfizer vaccine was approved by the Singaporean Health Sciences Authority in mid-December (HSA, 2020). China reports that it has been vaccinating Chinese citizens since July, with Sinopharm reporting that it has vaccinated one million people in China (Nature, 2020).

With governments under pressure to secure vaccines for their population, it is important that countries in the region work together to maintain a steady and affordable supply. Singapore called for “vaccine multilateralism” and decided to contribute USD 100 000 to the COVID-19 ASEAN Response Fund. India announced USD 1 million in aid to the fund, which aims to help the region tackle the pandemic. China has promised priority access to underdeveloped and developing countries to strengthen vaccine security. A total of 92 low-income countries globally are set to get access to the vaccine through the COVAX Advanced Market Commitment (AMC) of Gavi, The Vaccine Alliance. A country is eligible for the programme if it has a Gross National Income per capita below USD 4 000 or is eligible according to the World Bank International Development Association (GAVI, 2020a). In ASEAN, Cambodia, Indonesia, Lao PDR, Myanmar, the Philippines and Viet Nam have so far been confirmed as part of AMC (GAVI, 2020a).

The distribution of a vaccine requires a substantial and developed logistical infrastructure with cold-storage facilities. In order to be effective, the COVID-19 vaccine requires cold temperatures, essentially between -80 and +8 degrees Celsius, during both transportation and storage. This can be provided through so-called cold chain equipment, which provides a temperature-controlled supply chain that runs from the time of production to final delivery and injection. Deficient power supplies or a power outage can break this chain and result in the vaccine becoming ineffective. A WHO report estimated that roughly 2.8 million vaccine doses were lost in 2011 due to inadequate cooling during transportation or storage (WHO, 2014). As of 2014, only a quarter of GAVI-eligible countries surveyed had optimal or adequate cold chain equipment.

Several Emerging Asian nations are addressing the cold supply chain issue. Cambodia is working with the WHO to build a National Deployment and Vaccination Plan (WHO, 2020c). Indonesia, which lies along the Equator and has more than 17 000 islands, faces unique challenges in maintaining cold supply chains. Starting before the pandemic, Indonesia developed a digitalised cold supply chain vaccination system, SMILE, in co-operation with the...
United Nations Development Programme. The system was developed to ensure all children had access to safe and efficient vaccinations (GAVI, 2020b). Based on its successful experience, Indonesia could use the SMILE programme to deploy its COVID-19 vaccination strategy. India is strengthening its readiness for vaccine distribution by augmenting cold chain and other vaccination product stocks. A National Expert Group on Vaccine Administration set up by the government is working to implement vaccination of priority groups when the vaccine is released (PIB, 2020). Singapore, as a centre of trade with strong logistic capabilities of handling pharmaceutical supplies, is well prepared to supply the vaccine to its population.

Another issue countries are facing is the efficient and fair distribution of the vaccine. When supply is insufficient, resources should be allocated based on an ethical framework and epidemiological models, depending on the situation in each country. A US study by Buckner et al. (2020) found that the optimal prioritisation strategy is to target elderly essential workers. However, depending on a country’s policy objective, younger essential workers could be prioritised to curb infections, or elderly people to curtail mortality. Overall, the study’s findings suggest that an optimal prioritisation outperforms non-targeted strategies by up to 18%.

In Indonesia, where supplies of the vaccine are likely to remain insufficient to immunise the whole population in 2021, the government has published a vaccination plan giving priority to citizens according to their contribution to combating the virus (Table 1.5). Singapore’s Expert Committee on COVID-19 vaccination is planning a strategy consistent with the priority group guidelines of the WHO Strategic Advisory Group of Experts on Immunisation (SAGE) and has promised to make this strategy public by the end of 2020. Groups at highest risk, such as frontline health care workers and vulnerable groups determined by age and health, will be among the top priorities (WHO, 2020d; MOH, 2020b). The government of the Philippines is implementing a vaccine rollout strategy with hopes of launching nationwide vaccination programmes in the first quarter of 2021 (Table 1.6).

Table 1.5. Priority groups for COVID-19 vaccination in Indonesia

<table>
<thead>
<tr>
<th>Priority group</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>• Frontline health care workers involved in COVID-19 handling&lt;br&gt;• Personnel of the Indonesian National Defence Forces and the Indonesian National Police, law enforcement officials&lt;br&gt;• Public servants</td>
</tr>
<tr>
<td>2</td>
<td>• Community members&lt;br&gt;• Religious leaders&lt;br&gt;• Regional apparatus in districts, villages and neighbourhood units</td>
</tr>
<tr>
<td>3</td>
<td>• Teachers and educators from early childhood level to universities</td>
</tr>
<tr>
<td>4</td>
<td>• Central and regional government officials, legislators</td>
</tr>
<tr>
<td>5</td>
<td>• Beneficiaries of the premium subsidy of the Social Security Agency for Health Care (BPJS Kesehatan)</td>
</tr>
</tbody>
</table>

Source: CSI (2020), Gov’t working on road map for COVID-19 vaccination: Coordinating minister* (news release), 12 October.

Table 1.6. Vaccine rollout strategy in the Philippines

<table>
<thead>
<tr>
<th>Roadmap phase</th>
<th>Action</th>
<th>Responsible authority</th>
</tr>
</thead>
<tbody>
<tr>
<td>First phase</td>
<td>Scientific evaluation and selection of the vaccines</td>
<td>Department of Health (DOH), Department of Science and Technology (DOST)</td>
</tr>
<tr>
<td>Second phase: guarantee of access</td>
<td>Acquisition of vaccines</td>
<td>Department of Foreign Affairs, Department of Finance (DOF)</td>
</tr>
<tr>
<td>Third phase</td>
<td>Cost- and time-efficient vaccine procurement process</td>
<td>Procurement Service of the Department of Budget and Management (PS-DBM), DOF, TaskGroup Resource Management &amp; Logistics (TGRML)</td>
</tr>
<tr>
<td>Fourth phase</td>
<td>Distribution and deployment of the vaccine</td>
<td>PS-DBM, TGRML</td>
</tr>
<tr>
<td>Fifth phase</td>
<td>Nationwide implementation of the vaccination plan</td>
<td>DOH, national and local government agencies, local government units</td>
</tr>
<tr>
<td>Sixth phase</td>
<td>Assessment, evaluation and monitoring of the vaccine rollout</td>
<td>DOH, DOF, University of the Philippines-National Institute of Health</td>
</tr>
</tbody>
</table>

A number of surveys in recent decades have found that trust in vaccines is declining (Wellcome, 2019). This can lead people to refuse taking a vaccine. Policy makers and health authorities need to tackle this important issue, not only to increase the percentage of the population that is vaccinated, but for public health as a whole. Wellcome’s survey showed that, among ASEAN populations, Indonesians are least likely to strongly or somewhat agree that vaccines are effective.

On 24 November 2020, Malaysia became the first Southeast Asian country to sign an initial COVID-19 vaccine purchase agreement with the American pharmaceutical company Pfizer. Its purchase of 12.8 million doses will be sufficient for 6.4 million people, or approximately 20% of the Malaysian population. The agreement ensures a supply of 1 million doses for the first quarter of 2021, followed by 1.7 million doses in Q2, 5.8 million in Q3 and a final 4.3 million in Q4. Priority will be given to high-risk groups, including frontline health care workers, and will subsequently move down to lower-risk groups (PMO of Malaysia, 2020a). On 27 November, Prime Minister Muhyiddin declared that vaccines will be free for Malaysians but that foreigners will have to pay a charge set by the Ministry of Health (PMO of Malaysia, 2020b). The Pfizer vaccine requires a cold supply chain infrastructure, which will pose a challenge for a country with a tropical climate.

Indonesia is slated to deploy vaccines manufactured by China’s Sinovac Biotech as early as the end of January 2021. Some 1.2 million doses are carefully stored for clinical trials at a biopharmaceutical storage facility in Bandung and are scheduled to be examined by the Food and Drug Supervisory Agency. The inspection is expected to take 3-4 weeks. Although distribution of the vaccine will be challenging for the archipelagic country, Sinovac’s vaccine’s does not need to be transported and stored at below-zero temperatures, as it requires temperatures between 2 and 8 degrees Celsius (Information Portal of Indonesia, 2020). This is advantageous compared to Pfizer’s recommended storage temperature conditions of -70 ±10 degrees Celsius (Pfizer, 2020). However, Indonesia is currently in talks to purchase Pfizer vaccines as well. These vaccines would be administered in larger hospitals near large urban areas and are not expected to be transported to remote areas of the country.

Unlike other countries that are purchasing vaccines from elsewhere, Viet Nam is opting to develop its own. As of December 2020, Nanogen Biopharma in Ho Chi Minh City was in the first phase of testing its leading vaccine product on 60 volunteers. Viet Nam’s Ministry of Health is providing support and evaluations in order to ensure that the vaccine is safe and meets required standards (Viet Nam Ministry of Science and Technology, 2020).

**Monetary policy has entered unconventional territory**

Over the past seven months, Emerging Asian authorities have implemented various measures through a broad range of tools to counteract market dysfunctionality, including policy rate cuts, interventions in foreign exchange (FX) markets and liquidity provision. Central banks have brought down key policy rates and reserve requirements for banks in several steps. The central banks of China, India, Indonesia, Malaysia, Myanmar, the Philippines, Thailand and Viet Nam lowered policy rates by between 30 and 300 bps (Figure 1.54, panel A). For its part, the Monetary Authority of Singapore has kept its exchange rate-based monetary stance unchanged since April. China, India, Indonesia and the Philippines also implemented reductions in reserve requirement ratios applicable to banks (Figure 1.54, panel B).
The successive policy rate cuts have narrowed monetary space across Emerging Asian countries. Policy rates have been brought closer to the zero lower bound, with Thailand a case in point. The monetary arm of the response has therefore entered unconventional territory in order to preserve monetary space and avoid further deepening of the economic downturn. To further ease financing conditions, policy makers have designed a variety of unconventional monetary policy tools, including “lower-for-longer” forward guidance, large-scale asset purchases, large-scale liquidity injections to alleviate financial institutions’ liquidity problems or the expansion of collateral acceptance.

Several countries launched purchases of government bonds denominated in domestic currency to rectify market dislocations and act as buyers or dealers of last resort. Indonesia is one of the largest emerging market economies to have called upon the central bank to support the economy through unconventional measures. Bank Indonesia (BI) announced in October 2020 that it had purchased a combined total of IDR 60.18 trillion (Indonesian rupiah, USD 4.3 billion) of tradable government securities in the primary market through auction schemes, greenshoe options and private placements since April (BI, 2020b). The Bangko Sentral ng Pilipinas (BSP) also acquired government securities from banks in the secondary market via a daily purchase one-hour window (BSP, 2020c). For its part, the Bank of Thailand (BOT) purchased government bonds in several rounds in March and April 2020, amounting to a total of THB 88.3 billion (Thai baht, USD 2.9 billion) (BOT, 2020c).
The impact of unconventional measures on local financial markets appears to have been positive overall. In particular, government bond purchases by the central banks of Indonesia and Thailand have helped bring down sovereign bond yields, without leading to a substantial depreciation of the domestic currency (Figure 1.55). On the other hand, a major concern with unconventional policies is related to the unintended consequences they could have. By narrowing credit and term spreads, unconventional monetary measures lead to a flattening of the yield curve, reducing banks’ profitability and resilience (Borio and Gambacorta, 2017). The flattening of the yield curve could prompt investors to seek higher yields, which could result in an accumulation of risk on their balance sheets (Chami et al., 2020). Low long-term bond yields could also have an adverse impact on financial intermediaries with long-term liabilities, such as insurance companies (ECB, 2015) and pension funds. A careful assessment and a deeper understanding of the undesired effects of unconventional policies is therefore warranted.

Narrowing monetary space calls for alternative policy options, such as asset purchase programmes

Quantitative easing (QE) lowers bond yields, thereby reducing the cost of borrowing, and boosting the price of financial assets, generating a wealth effect. Central banks could maximise the effectiveness of their asset purchase programmes (APP) in several ways. As shown by Andrade et al. (2016), an increase in the average duration of the sovereign bonds purchased through the APP would be desirable for enhancing the impact of the asset valuation channel. Their results suggest that an increase in the average maturity of purchased assets from 8 to 11 years would lead to an additional increase in peak inflation by 10 basis points. Another option to enhance the impact of the asset valuation channel is to purchase riskier bonds. Model simulations suggest that the purchase of private securities included in the 2015 European Central Bank (ECB) asset purchase programme played a disproportionately large role in terms of the macroeconomic impact of the APP (Andrade et al., 2016).
The central banks of Indonesia, the Philippines and India have resorted to quantitative easing, as narrowing monetary space called for alternative forms of balance sheet expansion (Figure 1.56). At the onset of the pandemic, Bank Indonesia received provisional authority to purchase sovereign bonds in the primary market to assist the government in managing the impact of the crisis. The Reserve Bank of India (RBI) resorted to buying long-tenor government bonds and selling short ones to drive market yields lower (RBI, 2020c).

Figure 1.56. Total assets held by the central banks of Indonesia, the Philippines and India, 2017-20

![Total assets held by the central banks of Indonesia, the Philippines and India, 2017-20](image_url)

Note: September and October 2020 data are not available for the Philippines.
Source: OECD Development Centre based on data from CEIC and national sources.
StatLink [https://doi.org/10.1787/888934229198](https://doi.org/10.1787/888934229198)

However, central banks may be confronted with difficulties in their sovereign bond purchases. Central banks could expand the range of assets they buy under QE. In general, in the United States, QE was limited to government bonds and mortgage-backed securities (MBS), whereas in the euro area the ECB also purchased corporate bonds. For its part, the Bank of Japan (BoJ) is also buying equity and real estate under its QE programme (Shirai, 2018).

Yield curve control could be an alternative option, but also riskier

Yield curve control (YCC) makes quantitative easing more sustainable. In terms of implications for markets, yield curve control would likely reduce the volatility of interest rates and exchange rates. The central banks of Japan and Australia have implemented a sovereign yield-curve control scheme. Indeed, the BoJ has kept the 10-year sovereign interest rate at 0% since September 2016 (BoJ, 2016). For its part, the Reserve Bank of Australia set the 3-year interest rate at 0.25% in March 2020 following the COVID-19 outbreak (Low, 2020). With an YCC policy, a central bank can convey its monetary policy decisions more clearly and provide financial markets with greater certainty. In addition, YCC could be a more efficient tool than the current sovereign asset purchases. More precisely, if investors were convinced of the central bank’s intention and ability to maintain an interest rate at a given level, then the central bank could achieve its goal with a less active participation in the sovereign-bond market. For example, the effects of BoJ’s yield-curve control policy were quickly evident in financial markets. Ten-year sovereign yields settled close to the target and remained remarkably stable over the two years after the YCC policy was implemented.
At the same time, yield curve stability has come with a marked decline in the pace of BoJ asset purchases (Higgins and Klitgaard, 2020).

On the other hand, a YCC policy may put a central bank in a precarious situation because exiting the rate targeting policy could pose challenges. Furthermore, the process of unwinding YCC could also pose considerable challenges. For example, the withdrawal of the US Federal Reserve from the YCC scheme in the early 1950s proved more complicated than initially anticipated and the US Treasury had to intervene in order to absorb part of the associated losses (FOMC, 2003). In addition, YCC has the potential to create a powerful nexus between monetary and fiscal policy, posing a risk to central bank independence. In the absence of a YCC control policy, unexpected changes in the supply of government debt can influence sovereign yields. If higher government borrowing rates are passed on to other market rates, then this increase in government borrowing could reduce or “crowd out” private spending by households and firms (Bundick and Smith, 2020).

### Adjusting the monetary regime in response to COVID-19

Adjustments to the monetary regime through a potential switch to “average inflation targeting” or the implementation of a tiered interest rate system are potentially more promising avenues than QE and YCC.

The relationship between economic slack and inflation has changed considerably since the 2000s (Milani, 2010; Forbes, 2019), when inflation targeting became a widely adopted monetary policy framework in both advanced and emerging economies. In Emerging Asia, inflation-targeting regimes are currently in place in Indonesia, the Philippines, Thailand and India (Table 1.7). However, over the past few years the central banks of some countries have struggled to maintain headline inflation within the target range (Figure 1.57). In an attempt to raise prices, central banks kept policy rates relatively low throughout 2019, limiting their room for manoeuvre when the pandemic disrupted the economy at the beginning of 2020.

### Table 1.7. Overview of inflation-targeting regimes in Emerging Asia

<table>
<thead>
<tr>
<th>Country</th>
<th>Date of adoption</th>
<th>Current target range</th>
<th>Measure of inflation subject to target</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indonesia</td>
<td>July 2005</td>
<td>3% ± 1% deviation</td>
<td>Headline</td>
</tr>
<tr>
<td>Philippines</td>
<td>January 2002</td>
<td>3% ± 1 percentage point</td>
<td>Headline</td>
</tr>
<tr>
<td>Thailand</td>
<td>May 2000</td>
<td>1-3%</td>
<td>Headline</td>
</tr>
<tr>
<td>India</td>
<td>May 2016</td>
<td>2-6%</td>
<td>Headline</td>
</tr>
</tbody>
</table>

Note: Information as of 5 January 2021.  
Source: OECD Development Centre based on BIS (2019), and national sources.
With the outlook for inflation highly uncertain in the aftermath of the health crisis, a strategy shift, for instance in the form of average inflation targeting, could represent an appropriate policy reaction going forward. Average inflation targeting may indeed be an effective tool in the current economic environment, where sluggish price increases have obliged central banks to implement hefty policy rate cuts, thus narrowing monetary space. The US Federal Reserve, for example, has recently revised its monetary policy framework. The Fed unveiled a new approach, centred on “average inflation targeting” (Powell, 2020). In other words, inflation would be allowed to exceed the 2% target to make up for periods where it falls below 2%. This marks a shift from the policy orthodoxy of past decades and could become the new norm in the fight against the COVID-19-related economic fallout.

In order to launch average inflation targeting, a central bank would need to define several parameters. The length of the inflation averaging period could be fixed (such as the most recent five years), or it could be allowed to vary over time, namely setting the starting point at the last business cycle peak and continuing it through the present business cycle.
Furthermore, the central bank would need to determine how quickly it would intend to move average inflation back to target (Reifschneider and Wilcox, 2019). Research shows that an average inflation-targeting framework that aims for above-target inflation is more effective than classical inflation targeting in the presence of a low natural rate of interest and a lower bound on interest rates (Mertens and Williams, 2019).

In addition, the COVID-19 crisis, accompanied by lacklustre growth, weak investment and high unemployment has drawn renewed attention to the natural rate of interest as a potential benchmark for monetary policy makers (Box 1.6).

**Box 1.6. The natural rates of interest in Emerging Asian countries**

The natural rate of interest is a theoretical concept that has received various definitions. In a nutshell, the natural rate of interest can be defined as the rate that would prevail when actual output equals its potential. The natural rate of interest of an economy depends on several real economic factors, including productivity; demographic change; the effectiveness of financial intermediation; and other structural factors.

Estimating the natural rate of interest in emerging economies is challenging due to the limited length of data series and ongoing structural changes (Goyal and Arora, 2013). However, some studies have tried to provide estimations for Asian countries. Perrelli and Roache (2014) document the sizeable decline in the natural rate of interest in 24 emerging economies, including Asian economies. The authors reveal that in emerging economies, the likely ranges for the natural rate of interest plummeted by more than 200 basis points between 2002 and 2013. Similarly, Zhu (2016) shows that, with the exception of China, the natural rate of interest in Emerging Asian economies has fallen by more than 4 percentage points in recent decades, mostly due to low-frequency demographic and global factors. Other estimates show that the natural rate in ASEAN has been declining since the start of the new millennium, suggesting that country-specific factors, like saving and investment rates, cannot alone explain the change in the natural rate of interest. Global factors that are also likely to have contributed to the decline include lower global interest rates, lower public debt, reduced sovereign risk and an increased supply of savings that have translated into financial deepening (Maybank, 2018).

**Figure 1.58. Natural rates of interest of Indonesia and Thailand**

Source: OECD Development Centre, based on Tanaka, Ibrahim and Brekelmans (2021).

StatLink [https://doi.org/10.1787/888934229236](https://doi.org/10.1787/888934229236)
**Box 1.6. The natural rates of interest in Emerging Asian countries (cont.)**

Given the importance of the natural rate of interest as a reference for monetary policy and potentially as an indicator of the monetary stance, Tanaka, Ibrahim and Brekelmans (2021) estimate the natural rate of interest for several countries in Emerging Asia; namely Indonesia, Malaysia, the Philippines, Singapore and Thailand. For this purpose, we use the method outlined by Jorda et al. (2020) to estimate the impact of the Asian financial crisis of 1997-98 (AFC) and global financial crisis of 2007-08 (GFC) on the natural real interest rate of the five Emerging Asian countries included in the sample. Their findings point to a decline in the real natural rates of interest over the period under analysis (Figure 1.58).

**Figure 1.59. Average impact of the AFC and GFC on the natural rates of interest of Indonesia and Thailand**

![Average impact of the AFC and GFC on the natural rates of interest of Indonesia and Thailand](image)

- **Note:** The dotted lines are the error bands (90% confidence intervals) around the projection estimate. LB stands for lower bound and UB stands for upper bound. The blue line in the middle is the projection estimate (IRF standing for impulse response function). The vertical axis refers to the natural rate of interest and the horizontal axis to the months after the shocks.

- **Source:** OECD Development Centre, based on Tanaka, Ibrahim and Brekelmans (2021).

  [StatLink](https://doi.org/10.1787/888934228077)

Natural rates of interest tend to decline significantly during crises. The decline of natural rates of interest in Emerging Asian countries was already in progress in the early 1990s, a trend exacerbated by the AFC and GFC. Figure 1.59 shows that the decline was of larger magnitude in Indonesia, but more persistent in Thailand.

Low and negative interest rates boost the economy by keeping borrowing costs low and encouraging banks to lend. However, they have harmful side effects as they squeeze bank profitability. Central banks could commit to keeping rates lower for longer by making low or negative rates more sustainable. A tiered system could also facilitate the transition towards monetary policy normalisation. Tiered interest rates have been implemented in several economies and refer to the situation whereby low or negative rates are limited to only a part of a bank’s overall balance sheet.

For instance, the ECB introduced a two-tier system for reserve remuneration, which exempts parts of credit institutions’ excess liquidity holdings (i.e. holdings in excess of minimum reserve requirements) from negative remuneration at the rate applicable on the deposit facility. More precisely, the exempt tier will be remunerated at an annual rate of 0%, while the non-exempt tier of excess liquidity holdings will continue to be remunerated at...
0% or the deposit facility rate, whichever is lower. The goals of the ECB’s two-tier policy were twofold. On the one hand, the two-tier policy aimed to support bank-based transmission of monetary policy. On the other, the policy attempts to preserve the positive contribution of negative rates to the accommodative stance of monetary policy and the convergence of inflation to ECB’s aim (ECB, 2019).

**Policy makers need to be mindful of the capital flow implications of monetary policy**

Capital flow volatility is a key area of concern and vulnerability for emerging market economies. Surges in capital flows are often followed by sudden drops. This volatility is often the result of changes to the monetary policy stance and other developments in advanced economies, and may not necessarily be related to domestic factors. Low interest rates in advanced economies encourage a yield-search behaviour, triggering outflows from these economies into emerging market economies. A large number of studies have documented the importance of global factors, such as advanced-economy interest rates, in affecting capital flows to emerging market economies (Forbes and Warnock, 2012; Ahmed and Zlate, 2014; Kiendrebeogo, 2016). The room for manoeuvre has narrowed considerably as higher capital mobility confronted central banks with corner choices in implementing monetary policy.

Some studies support the view that inflation targeting corroborated with a free-floating exchange rate regime is an appropriate response to capital flows (Eichengreen, 2002). Long-term capital flows, in particular FDI flows, can also influence the conduct of monetary policy under an inflation-targeting framework. For instance, high levels of foreign investor participation in the banking sector have the potential to alter the functioning of the credit channel in the monetary transmission mechanism, given that domestic banks have access to funding sources in foreign parent institutions. However, for an inflation-targeting regime to tackle capital flow volatility effectively, several prerequisites are necessary. For instance, Pruski and Szpunar (2008) assess the experience of Poland with inflation targeting. The authors conclude that an inflation-targeting regime encompasses several important features, namely: central bank instrument independence; an adequately developed financial system, with an interbank deposit market as the key ingredient; sufficient money market infrastructure (i.e. effective interest-rate setting, reflecting market conditions); and efficient liquidity management by the central bank (i.e. monetary operations).

**Fiscal stimulus will be the primary driver of growth at the expense of budgetary strength**

Southeast Asian countries have announced stimulus packages amounting to approximately 0.1% to 15% of their respective GDPs. The launch of these large-scale packages will lead to a significant worsening of fiscal balances, with a double-digit deterioration anticipated in Singapore (Figure 1.60). The size of the fiscal response tends to be greater in countries with large SME sectors (Figure 1.61).
Figure 1.60. Total amount of fiscal packages and estimated impact on the fiscal balance of selected ASEAN economies

Note: The cut-off date for the fiscal stimulus data is 30 November 2020. Data on amount of fiscal stimulus are not available for Brunei Darussalam. Data on fiscal balance refer to the general government. The 2019 data on fiscal balances are based on the IMF World Economic Outlook database, October 2020. The 2020 forecasts of the fiscal balance for Cambodia, Lao PDR, Myanmar and Singapore are based on the IMF World Economic Outlook database, October 2020. The 2020 forecast of the fiscal balance for Indonesia is based on the OECD Economic Outlook, December 2020.

Source: OECD Development Centre; OECD Economic Outlook, December 2020; ADB COVID-19 Policy Database; and IMF, World Economic Outlook database, October 2020.

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Figure 1.61. Population covered by social protection, contribution of SMEs to domestic GDP and size of fiscal stimulus in selected Emerging Asian economies

Note: Fiscal stimulus data as of 30 November 2020. Data on coverage by social protection and labour programmes refer to 2013 for Malaysia and the Philippines; 2015 for India; 2016 for Thailand; and 2017 for Indonesia and Viet Nam. Data on contribution of the SME sector to domestic GDP refer to 2016 for India and the Philippines; 2018 for Indonesia, Malaysia and Viet Nam; and 2019 for Thailand. The bubble size indicates the total fiscal stimulus amount as a percentage of GDP.


StatLink https://doi.org/10.1787/888934229255
The fiscal policy response to the COVID-19 crisis to date has been a patchwork of increased allocations to health care systems and spending on pandemic-related equipment, transfers to households and transfers to firms (Table 1.8). In regard to household support, the main theme across countries has been to provide immediate relief to the most vulnerable, while some countries also sought to ensure food security. Indonesia, for example, expanded its social welfare programme to include food assistance. As for measures aimed at the corporate sector, the initial response in most countries focused on shielding vulnerable SMEs and companies operating in the most affected sectors, namely tourism, transport and travel. The most common approaches have been to reduce labour and corporate taxation. Corporate tax reductions have had a temporary character across all countries in the region, except for Indonesia, where corporate income tax rates will be lowered from 25% to 22% for fiscal years 2020 and 2021, and to 20% for fiscal year 2022 onwards.

Table 1.8. Examples of fiscal stimulus measures in Emerging Asia in response to the COVID-19 pandemic

<table>
<thead>
<tr>
<th>ASEAN-5</th>
<th>Increased health care spending</th>
<th>Direct support to household income</th>
<th>Wage subsidies/labour tax reductions</th>
<th>Corporate tax exemptions/reductions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indonesia</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Malaysia</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Philippines</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Thailand</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Brunei Darussalam and Singapore</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Brunei Darussalam</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Singapore</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>CLM countries</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cambodia</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>Myanmar</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>China and India</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>China</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>India</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
</tr>
</tbody>
</table>

Note: The cut-off date is 30 November 2020. The information provided in this table is for illustrative purposes only and is not intended to be exhaustive. Source: OECD Development Centre based on data from ADB (2020c), ADB COVID-19 Policy Database, https://covid19policy.adb.org/ and national sources.

Narrowing fiscal space calls for more targeted fiscal spending

In the current context of large-scale fiscal actions, and with monetary space significantly reduced, GDP growth in Emerging Asian countries will be primarily driven by fiscal policy. With rising public debt and fiscal deficits, fiscal space has narrowed appreciably in the region. Governments may therefore not be able to maintain the same level of fiscal spending in 2021 as in 2020. Consequently, the priority for policy makers should be to render fiscal spending more targeted, for instance, to the area of health and education (see Chapter 2 for more detailed discussion). Theoretical arguments support the effectiveness of targeted fiscal policy (Elmendorf and Furman, 2008). In general, targeting fiscal stimuli to areas where demand and supply are most likely to be responsive will lead to the largest increase of fiscal multipliers. For instance, measures targeted at lower-income households or those that are liquidity-constrained should produce larger fiscal multipliers, as these households have a higher marginal propensity to consume (Brinca et al., 2016).
The effect that fiscal stimuli will have on growth depends on several factors, among them the composition and duration of the stimuli and the degree to which the economy is credit constrained. The impact of government shocks could also differ substantially across countries, depending on the level of development, exchange rate regime, openness to trade and public indebtedness (Ilzetzki et al., 2013). In general, the GDP effects of fiscal stimuli that take the form of public spending shocks (i.e. government consumption and investment) tend to be larger than those involving tax reductions or direct transfers to households (Barrell et al., 2012). However, when monetary policy is accommodating, the impact of transfers on GDP is considerably larger (Coenen et al., 2010). The impact of a given stimulus also depends on whether the shock is temporary or not. A temporary corporate tax rate cut would arguably have little impact, as firms calculate the tax burden related to a new investment project over its entire life cycle, while the effect of a permanent reduction could be more substantial (Zellner and Ngoie, 2015).

Box 1.7. Fiscal multipliers in Emerging Asian countries

The variability of fiscal multipliers across advanced economies (AEs) and emerging markets (EMEs) has been widely documented in the literature. In particular, Kraay (2010) and Ilzetzki et al. (2013) demonstrate that, in developing countries, the response of output to government consumption is relatively brief, often negative and not statistically different from zero. Comparatively fewer studies provide insights on fiscal multipliers in Emerging Asian economies. Using an SVAR model, similar to Blanchard and Perotti (2002), Tang et al. (2010) show that in all ASEAN-5 countries the overall impact of government spending on output is largely benign, with the impact fiscal multiplier below one and statistically insignificant. In the case of tax measures, output is shown to expand in line with fiscal contraction, but the results are only statistically significant in Indonesia and Thailand. Relatedly, Beyer and Milivojevic (2019) show that changes in tax revenue have no significant impact on economic activity in South Asia, in line with Tang et al. (2010).

A large number of studies have sought to explain the lower fiscal multipliers in EMEs in various ways (Tanaka, 2021, for more details). A first set of explanations relates the lower fiscal multipliers to leakages through higher imports or the heterogeneous responses of exchange rates (Corsetti et al., 2006; Ilzetzki et al., 2013; Shremirov and Spirovska, 2019; Miyamoto et al., 2019). This is particularly true for small and highly open economies, such as Singapore, Malaysia and Thailand and, to a lesser extent, the Philippines and Indonesia (Tang et al., 2010). Another type of explanation points to fiscal strength as a key factor behind fiscal policy effectiveness (Corsetti et al., 2012; Huidrom et al., 2020). Among ASEAN-5 countries, many have run a persistent budget deficit, with well-known fiscal weaknesses in Indonesia and the Philippines (Tang et al., 2010). Other explanations for lower fiscal multipliers include the combination of low financial depth and a largely liberalised interest rate environment (Tang et al., 2010), lower institutional quality (Avellan et al., 2020) or poor data availability and quality (Batini et al., 2014). As for the persistence of fiscal multipliers, the duration of the effect varies depending on several factors, including the persistence of the fiscal shock; the type of fiscal instrument; and conjunctural factors such as the cyclical position and whether monetary policy responds to the fiscal shock (Coenen et al., 2012; DeLong and Summers, 2012, Batini et al., 2014).

Substantial fiscal response to the economic fallout narrows fiscal space

Prior to the onset of the pandemic, Emerging Asian economies had room to expand their primary balance deficits in response to the economic fallout triggered by the health crisis (IMF, 2018; AMRO, 2020). Debt levels are comparatively lower than in most OECD countries, while prudent fiscal management had translated into overall stable budgetary
balances. Nevertheless, the COVID-19 crisis will leave a lasting mark on public finances in the region. In addition to substantial fiscal stimulus, the declining revenue-to-GDP and rising expenditure-to-GDP ratios through the operation of tax breaks and revenue shortfalls also contribute to explaining the unfavourable fiscal outlook. Government debt levels and budget deficits are projected to increase across the board in 2020 (Figure 1.62). However, the situation tends to differ substantially across countries. As such, the increase in the level of government debt to GDP in 2020 will range from roughly 0.6 percentage points in Brunei Darussalam to 17 percentage points in India. At the same time, fiscal deficits are projected to widen by between 1.4 percentage points in Lao PDR and 14.6 percentage points in Singapore.

Figure 1.62. Government debt and budget deficits in ASEAN countries, 2019-20

The residual maturity of public debt is an important factor affecting government refinancing conditions. A large share of debt with a short residual maturity implies that this part must be renewed within a relatively short period, which could turn out to be more costly in times of weak investor sentiment (Al Amine and Willems, 2020). The share of securities with a residual maturity of one year or less currently ranges from 3.6% in Cambodia to 14.9% in China (Figure 1.63, panel A). The current share of short-term debt instruments is high when compared to post-global financial crisis averages in the countries considered. Furthermore, a country’s financial vulnerability to a significant deterioration in its fiscal position depends on the share of public debt held by foreign investors. Some governments make use of foreign borrowing to avoid crowding out domestic borrowing by lifting bond yields. One of the main risks associated with foreign borrowing is that, as interest costs rise over time, servicing foreign debt exerts substantial deflationary pressures on the domestic economy (Hawkins and Turner, 2000). The share of public debt held by external creditors in 2020 varies greatly across countries, roughly from 9.1% to 53.4% (Figure 1.63, panel B).
In the aftermath of the global financial crisis, low deficit and debt levels strengthened confidence in Emerging Asian countries’ fiscal sustainability, broadly compressing credit default swap (CDS) spreads (Figure 1.64). While the spike in spreads at the early stages of the COVID-19 crisis has been largely reversed, the recent relative calm in Emerging Asian financial markets may breed complacency in terms of fiscal consolidation. A high level of public debt tends to increase investors’ concerns about holding government securities, as demonstrated by the surge in government bond spreads during the global financial crisis of 2007-08. Any associated wavering in the credibility of public finances harbours the potential to increase uncertainty and, at the limit, to trigger negative rating actions on sovereigns, with adverse feedback loops to the financial sector (Gennaioli et al., 2014).

Such developments could potentially have an adverse impact on recovery and on the potential growth rate of the economy, which may subsequently dampen the prospects for the financial system (Das et al., 2010; Jorda et al., 2016).
To some extent, sovereign financing needs could be smoothed via recourse to existing financial assets (Henao Arbelaez and Sobrinho, 2017). Globally, the utilisation of financial assets for mitigating governments’ financing needs depends on their liquidity, which is arguably inversely related to sovereign stress. As at the end of 2019, Indonesian government’s total holdings of financial assets equalled 27.1% of GDP, while government’s financial asset holdings amounted to 48.5% of GDP in Thailand at the end of 2018 (Figure 1.65). Short-term liquid assets, such as currency and deposits, can be more easily used to cover short-term financing needs. Currency and deposits amounted to 3.7% of GDP in Indonesia in 2019 and 8.5% of GDP in Thailand in 2018. Equity and investment fund shares accounted for the largest part of financial assets in Indonesia (19.6% of GDP in 2019), while in Thailand the bulk of the government’s financial assets are held in the form of debt securities (26.3% of GDP in 2018). Another major component of financial assets is the other accounts receivable, which incorporate various claims of the general government vis-à-vis the rest of the economy. This component, whose degree of liquidity can vary considerably, ranged from 2.8% in Indonesia in 2019 to 5.1% in Thailand in 2018. Overall, financial assets of governments are an important element in assessing sovereign liquidity and debt sustainability issues.
The fiscal situation is likely to remain challenging in Emerging Asian countries. Concerns over the ability of governments to restore sustainable public finances over the medium to long term are likely to persist. Increasing debt-to-GDP ratios suggest that sufficiently large primary surpluses need to be created and then maintained by governments over an extended period to put the debt ratio on a decreasing track (Abbas et al., 2013). In the current context, lower potential growth after the COVID-19 crisis could mean that the primary surpluses necessary to stabilise government debt ratios would need to be higher than in the past. Uncertainty surrounding governments’ ability to bring debt levels back to a sustainable path could cast doubts over the resilience of corporates in affected sectors that are most reliant on government support. At the same time, the high refinancing needs facing some countries over the next one or two years exacerbate the risk of an adverse feedback loop between the public and corporate sectors, as public finance needs might crowd out private sector issuance.

In the context of narrowing policy space at the country level, regional co-operation could provide an important complement to domestic policies in supporting post-pandemic recovery. The ASEAN Comprehensive Recovery Framework (ACRF) lays the ground for the launch of cross-border initiatives in a number of strategic areas, including health care, trade and digitalisation (Box 1.8).
Conclusion

With Emerging Asian economies still in the grip of the COVID-19 pandemic, a multitude of supply and demand shocks continue to shape economic activity. The growth slowdown in the region will be significant relative to previous crisis episodes, but will still be moderate compared to the slowdown in other regions. The outlook varies vastly across countries due to differences in the length and severity of lockdowns and differing economic structures, as well as differences in government capacity to offset the loss of income for households and firms. The new restrictions imposed since August amid a resurgence of infections are anticipated to weigh on economic activity and sentiment in the short term. Nevertheless, the impact is expected to be less acute than in the March-April period, as the approach has been more targeted.

Overall, the impact on GDP components in the first three quarters of 2020 has been broad based. The impact of the pandemic on private consumption was particularly severe, while on the supply side the services sector was heavily disrupted by the lockdown measures. Financial markets have held up well over the past few months, mainly due to central banks’ massive liquidity provision, but vulnerabilities remain in specific segments.

Box 1.8. Asean Comprehensive Recovery Framework (ACRF) lays the foundation for a sustainable recovery in the region

On the occasion of the ASEAN Summit in November 2020, ASEAN member states adopted the ASEAN Comprehensive Recovery Framework (ACRF). The ACRF is comprised of a set of the broad strategies and key priority measures to be employed for ASEAN recovery and long-term development post-COVID-19 (ASEAN, 2020b). The ACRF is accompanied by an implementation plan, which identifies specific initiatives to be undertaken towards recovery. ASEAN adopted the ACRF to guide the region through the different phases of the post-pandemic recovery, towards long-term resilience. The strategic response is adapted to the three phases of the recovery. First is the “Reopening” phase where the member countries are still at different stages of curbing the spread of the virus, and strive to strike a balance between minimising a resurgence in cases and restarting the economy. The second phase is “Recovery”, when economic activity returns to its pre-COVID-19 level. Support will need to be targeted for sectors or groups that have been strongly adversely affected by the pandemic. The third and final phase is “Resilience”, which entails a convergence towards ASEAN’s shared vision of long-term regional resilience. At this stage, preparations will take into account emerging trends and challenges, including the risk of future pandemics (ASEAN, 2020b).

The ACRF identifies five broad strategies that would guide ASEAN member states through the recovery process. These broad strategies and their key priorities are the following: (1) Broad Strategy 1: Enhancing Health Systems; (2) Broad Strategy 2: Strengthening Human Security; (3) Broad Strategy 3: Maximising the Potential of Intra-ASEAN Market and Broader Economic Integration; (4) Broad Strategy 4: Accelerating Inclusive Digital Transformation; and (5) Broad Strategy 5: Advancing towards a More Sustainable and Resilient Future. One of the early initiatives of the ACRF was the signing of the Memorandum of Understanding on the Implementation of Non-Tariff Measures (NTMs) on Essential Goods under the Hanoi Plan of Action on Strengthening ASEAN Economic Cooperation and Supply Chain Connectivity in Response to the COVID-19 Pandemic (ASEAN, 2020c; ASEAN, 2020d). Another initiative was the adoption of the ASEAN Declaration on an ASEAN Travel Corridor Arrangement Framework (ASEAN, 2020e).
As debt burdens are increasing and incomes are dwindling, the impact on bank balance sheets could become more acute going forward. In addition, current account balances are anticipated to deteriorate, as most components are forecast to contribute less than in 2019. Trade has slightly recovered over the past months, mostly due to strong demand from China, while the agreement on the RCEP, together with the CPTPP, are anticipated to support the recovery. The pandemic has put labour markets under severe strain, with unprecedented job losses during the first three quarters of 2020. Consequently, downward pressures on prices are set to dominate the inflation outlook. Another major trend observed during the pandemic is a substantial rise in e-commerce and e-payment transactions.

There are many threats that could cloud the outlook. First, potential new waves of COVID-19 cases could prevent a timely withdrawal of social restrictions and a return to normal economic conditions. This risk will likely remain elevated until an effective vaccine or treatment against COVID-19 has become widely available across Emerging Asian countries. Second, governments in Emerging Asia have much less room for manoeuvre to ramp up countercyclical policy if growth momentum weakens. After broad-based monetary easing during 2020, real interest rates are at historical lows. Policy makers may turn to unconventional policy, a trend that has gained traction throughout 2020. Additionally, the focus of monetary policy will likely shift from lowering policy rates to improving policy transmission. Third, fiscal policy is expected to remain an important growth driver. For many governments, the key focus in 2021 will be to stabilise budget deficits and debt burdens. Fiscal stimuli will therefore need to become more targeted in order to achieve the dual goal of tackling the legacy of the crisis while restoring fiscal rectitude.

**Note**

1. $\Delta$ Total e-commerce revenue = $\Delta$ ARPU + $\Delta$ the number of e-commerce users + $\Delta$ frequency of shopping on line.

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1. Macroeconomic Assessment and Economic Outlook in Emerging Asia


Please cite this chapter as:


DOI: https://doi.org/10.1787/7b62bdcb-en

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