

[2021-23 Economic Outlook: Asia]

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Acceleration of US rate hikes threatens stable growth in Asia

—Global inflation risk posed by supply-chain problems will remain—

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- ◆ The Asian economy will likely record a high growth rate of + 7.1% in 2021. However, in H2 2021, the ASEAN economy deteriorated significantly as severe restrictions on activities were implemented, and the Chinese economy slowed owing to measures to curb investment. We expect the Asian economy to grow at + 5.4% in 2022, but it could become vulnerable due to weak external demand and limited support from fiscal and monetary policies.
- ◆ Supply shortages originating in Asia could continue to contribute to global inflation. In addition to semiconductor shortages, electricity shortages might cause a new supply chain issue. The worst-case scenario for Asia is that supply shortages originating in Asia will fuel global inflation and accelerate the pace of monetary tightening in developed countries, notably the U.S., which will lead to policy rate hikes in Asia as countermeasures.
- ◆ By country, China experienced a slowdown in H2 2021 due to power shortages, tighter restrictions on activities and adjustments in the real estate market. We expect the growth rate in 2022 to reach + 5.4%, the same level as the potential growth rate, thanks to expanded investment and the elimination of electricity shortages.
- ◆ We expect India's GDP to grow at a relatively high rate of + 6.9% in FY 2022 as the economy continues to expand due to further easing of restrictions on activities. However, U.S. policy rate hikes, the problem of nonperforming assets and the pressure to cut fiscal spending could become downside risks.

1. Asia

- (1) The pace of Asia's economic recovery will return to cruising speed in 2022・・・ p.3
- (2) Global inflation caused by the supply shortages originating in Asia will remain as a risk threatening Asia's stable growth・・・ p.6
- (3) The recurrence of the U.S.-China conflict heightens uncertainty in the Asia region・・・ p.10

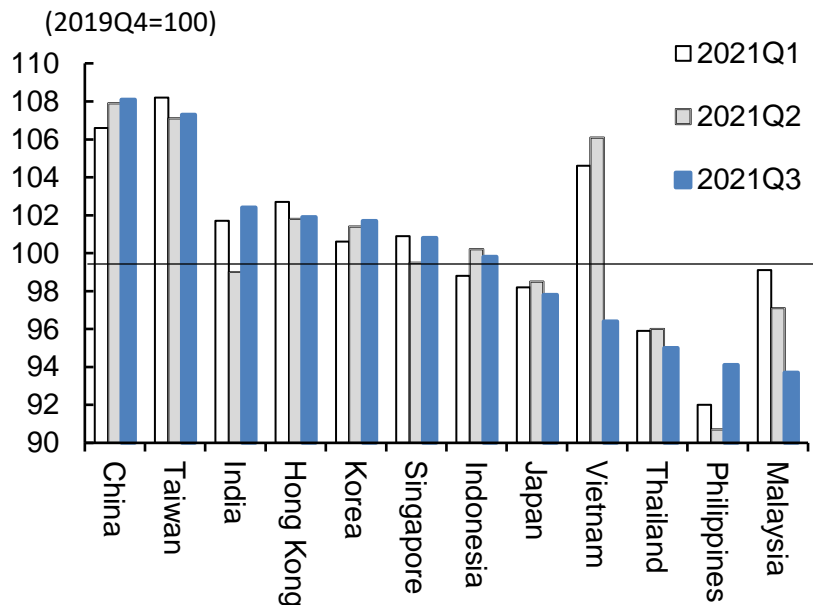
2. China ・・・ p.11

3. India ・・・ p.15

1. Asia (1) We expect stable growth in Asia for 2022

- Overall, the Asian economy continued to recover in 2021. In H2 2021, however, the economy deteriorated significantly in ASEAN countries due to the spread of the novel coronavirus, and the Chinese economy slowed down significantly due to anti-investment policies.
- We expect the Asian economy to grow at a stable rate of + 5.4% in 2022 as the economies of both ASEAN and China stabilize, but downside risks remain.

<Real GDP, seasonally adjusted>



Source: Prepared by The Japan Research Institute, Limited based on CEIC

<Growth Forecasts for Asian Economies>

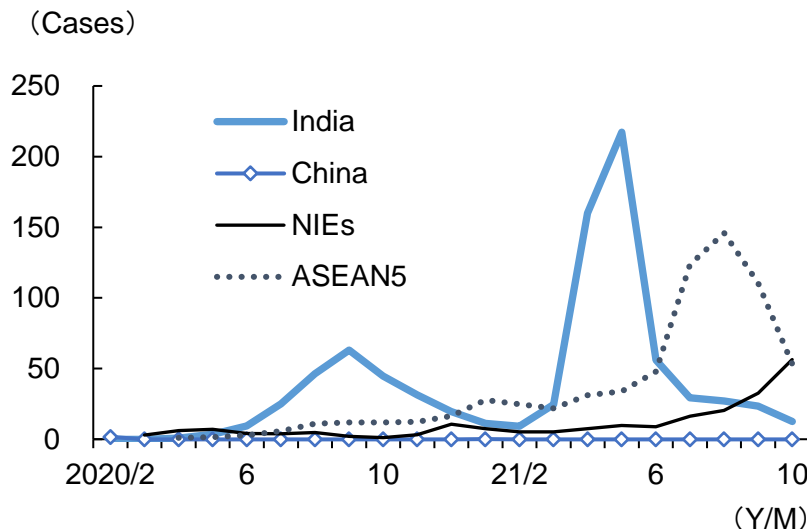
	2020	2021 (Forecast)	2022 (Forecast)	2023 (Forecast)
Asia	-0.7	7.1	5.4	5.6
Northeast Asia	2.0	7.6	5.0	4.9
China	2.3	8.0	5.4	5.3
Hong Kong	-6.1	6.5	2.2	2.1
Taiwan	3.1	5.8	2.8	2.5
South Korea	-0.9	3.9	2.4	2.4
ASEAN	-3.6	2.9	5.2	5.4
Thailand	-6.1	1.0	2.1	3.3
Malaysia	-5.6	3.1	6.1	5.5
Indonesia	-2.1	3.5	5.2	5.5
Philippines	-9.6	4.8	6.0	6.2
Vietnam	2.9	1.2	8.3	7.0
India (FY)	-7.3	9.0	6.9	7.9

Source: JRI

1. Asia (1) Downside pressure in H2 2021 has been eased, but....

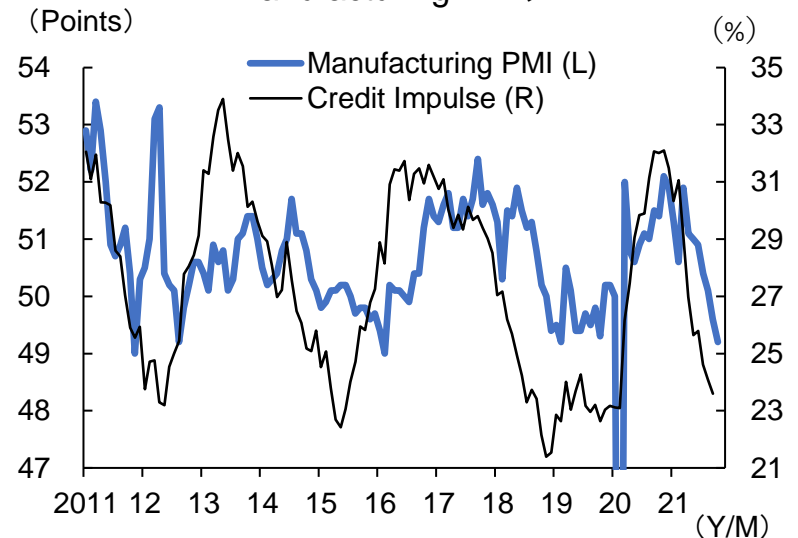
- Although strict curbs on activities are expected to be avoided in the event of a resurgence of the Covid-19 infection due to the progress of vaccination and other factors, the authorities remain vigilant.
- In China, excessive monetary tightening is expected to be avoided ahead of a Communist Party congress next autumn. However, there have been no signs of a rapid recovery.

<Number of New COVID-19 Cases
(Number of Cases Per Million Population,
Daily Average)>



Source: Prepared by The Japan Research Institute, Limited based on CEIC

<Increase/Decrease of China's Credit and
Manufacturing PMI>



Source: Prepared by The Japan Research Institute, Limited based on Bloomberg L.P.

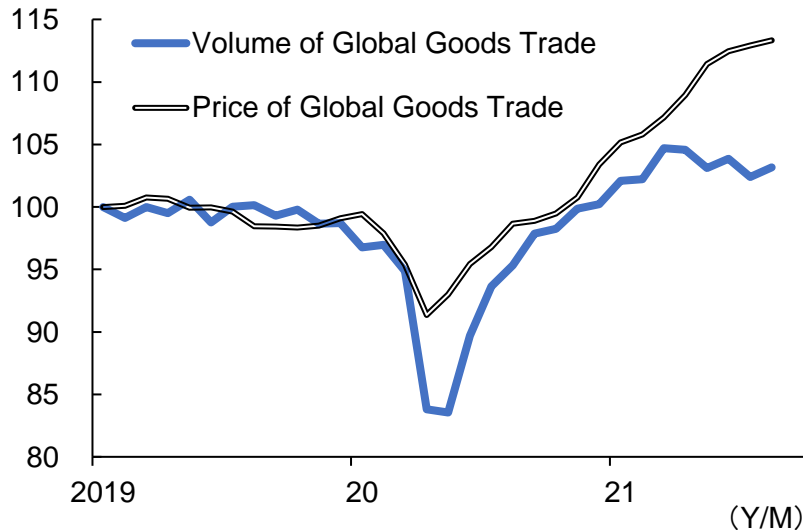
Note: Credit impulse is the percentage of new credit growth to GDP.

1. Asia (1) Headwinds amid more severe external conditions

- As the volume of the global goods trade has been leveling off, it will become more difficult for Asian exports to maintain a fast pace.
- In Asia, interest rates have been lowered since the 2008 financial crisis. However, with the normalization of monetary policy in the U.S. progressing in 2022, there is little room for additional monetary easing or fiscal expansion in Asia.

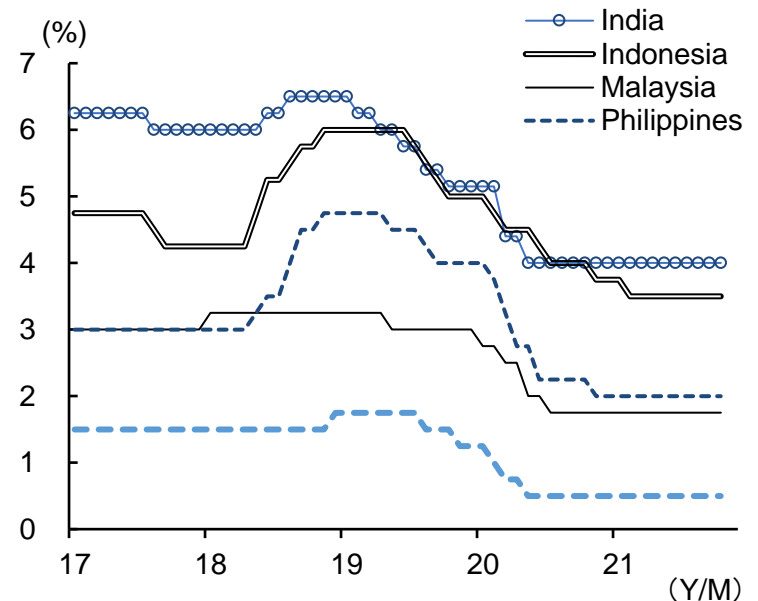
<Volume and Price of Global Goods Trade>

(January 2019 = 100)



Source: Prepared by The Japan Research Institute, Limited based on CPB Netherlands Bureau for Economic Policy Analysis

<Policy Rates in Asia>

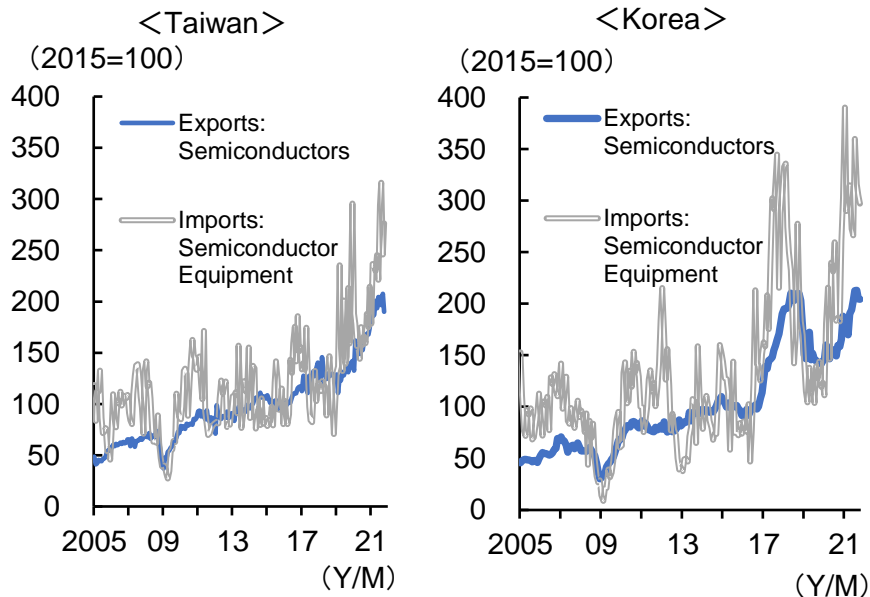


Source: Prepared by The Japan Research Institute, Limited based on CEIC

1. Asia (2) Supply chain issues: Semiconductor shortage

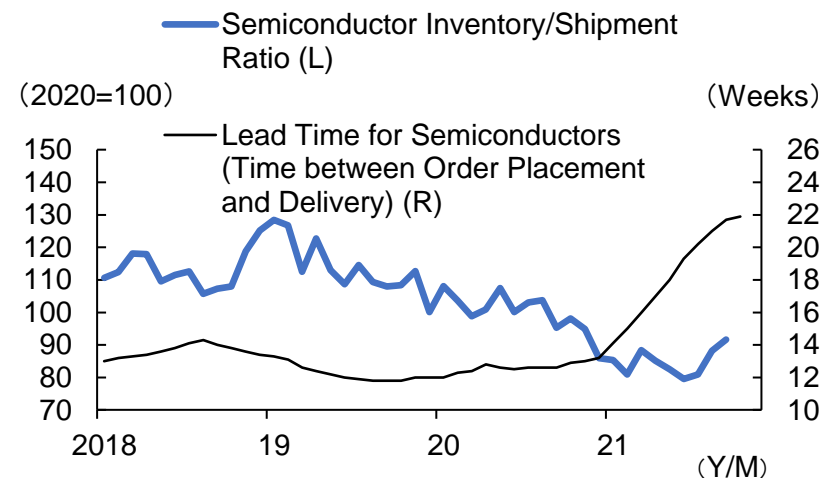
- The problem of semiconductor shortage remains. In Taiwan and Korea, investment has been made mainly in the leading-edge areas, but investment in so-called legacy chips such as those for automobiles still seems to be weak.
- The inventory ratio of semiconductors bottomed out in the middle of 2021, but the level remains low, suggesting continued tight supply and demand conditions. It will take a certain amount of time to resolve the supply shortage.

<Semiconductor Exports and Imports of Semiconductor Equipment>



Source: Prepared by The Japan Research Institute, Limited based on CEIC

<Inventory-Shipment Ratio of Semiconductors and Lead Time>



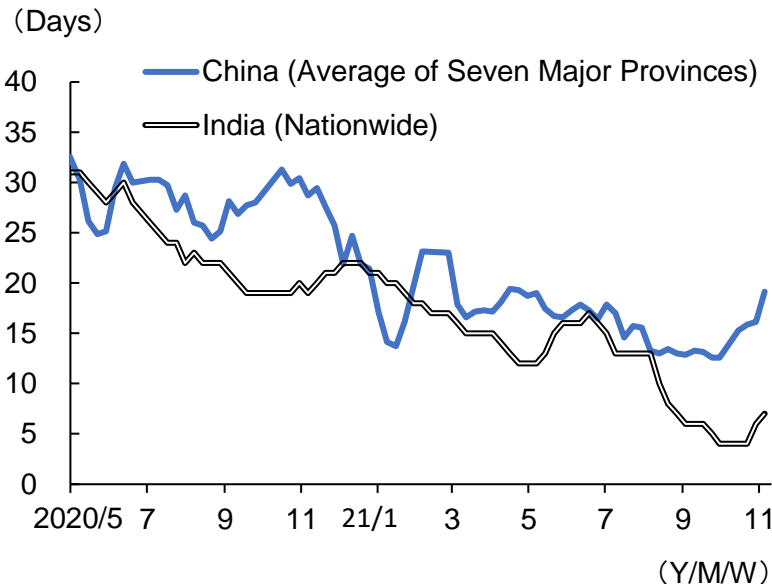
Source: Prepared by The Japan Research Institute, Limited based on CEIC and Bloomberg L.P.

Note: Semiconductor inventory/shipment ratio is the weighted average of exports by Japan, the United States, Korea and Taiwan in 2020.

1. Asia (2) Supply chain issues: Electricity shortage

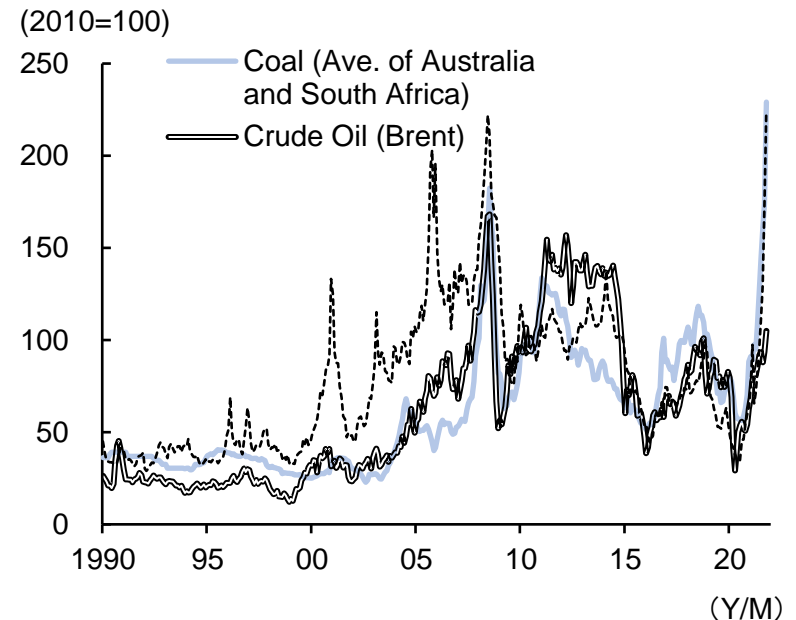
- In China and India, electricity shortages in September were triggered by sharply reduced inventories of coal. As the global trend toward environmental measures intensifies, the supply of electricity poses a risk not only to China and India but also to other Asian countries.
- Strict restrictions on activities are unlikely to be re-imposed in Asia, but electricity shortages could create new supply chain problems.

<Coal Inventory Days in Power Plants in China and India>



Source: Prepared by The Japan Research Institute, Limited based on CEIC and the Central Electricity Authority (India)

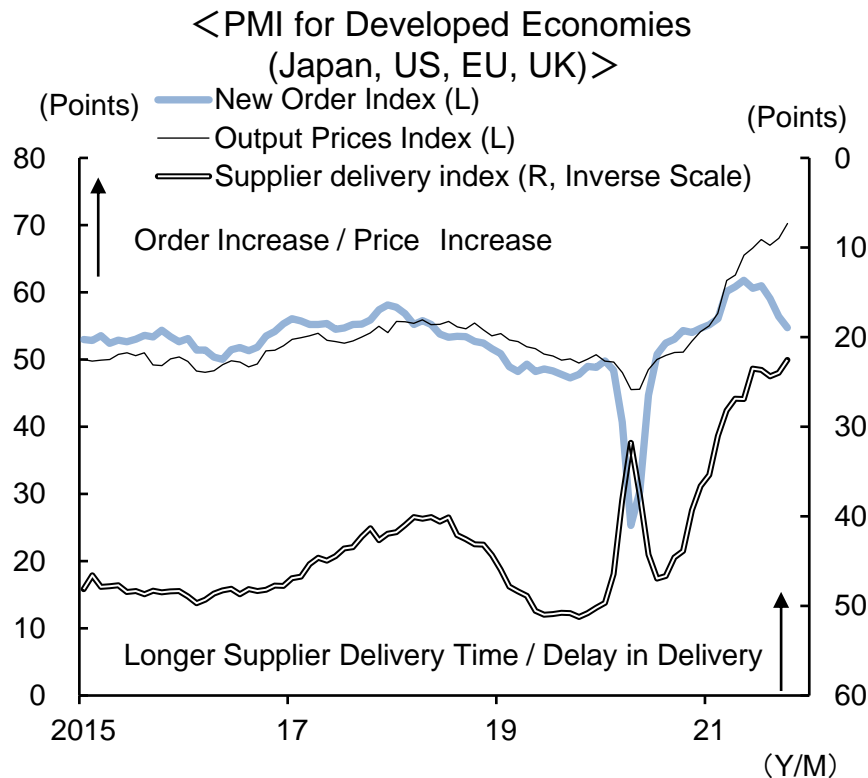
<Prices of Major Natural Resources>



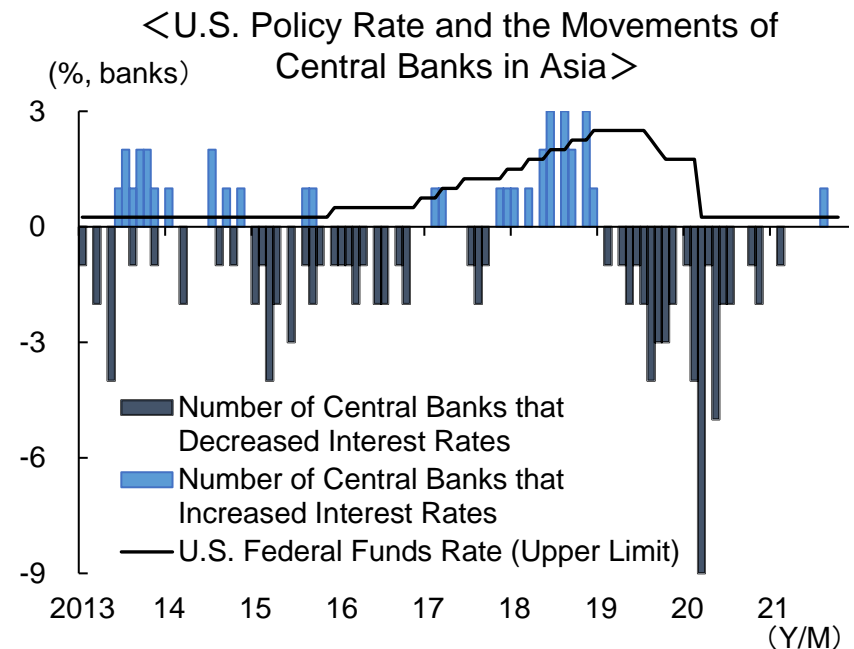
Source: Prepared by The Japan Research Institute, Limited based on World bank

1. Asia (2) Worst-case scenario is acceleration of rate hikes in the U.S.

- If supply shortages intensify along with persistently high resource prices, global inflationary pressures will increase further.
- If the higher global inflation accelerates the pace of monetary tightening in advanced economies, particularly the United States, Asia will also come under pressure to tighten monetary policy.



Source: Prepared by The Japan Research Institute, Limited based on IHS Markit



Source: Prepared by The Japan Research Institute, Limited based on CEIC

Note: Calculated as +1 if central banks in nine Asian countries and regions (China, South Korea, Taiwan, India, Indonesia, Philippines, Malaysia, Thailand, and Vietnam) raise interest rates, and -1 if they lower rates.

1. Asia (2) Possible acceleration of inflation due to supply shortages

- If rate hikes accelerate in the United States, international liquidity could shrink, forcing Asian countries to lower their currencies sharply or implement rate hikes to defend their currencies themselves, which could dampen economic recovery significantly.
- In particular, attention should be paid to the possibility of financial market instability in the Philippines, India and Indonesia, which are expected to post current account deficits in 2022.

<Indicators Assessing Stability of the Currency Market>

		Current Account Balance (% of GDP)			Fiscal Balance (% of GDP)			Inflation (2021Q3, % y-y)		ARA Metric (%)	Mineral Fuels Net Exports (% of GDP)
		2020	2021 (IMF forecast)	2022 (IMF forecast)	2020	2021 (IMF forecast)	2022 (IMF forecast)		Inflation target (%)	End-2020	2020
Asia	Philippines	3.6	0.4	-1.8	-5.7	-7.6	-6.2	4.6	2~4	237.6	-2.0
	India	0.9	-1.0	-1.4	-12.8	-11.3	-9.7	5.1	2~6	190.7	-2.9
	Indonesia	-2.7	-0.3	-1.0	-5.9	-6.1	-4.8	1.6	2~4	125.2	0.9
	China	1.8	1.6	1.5	-11.2	-7.5	-6.8	0.8	3.5	74.8	-1.6
	Thailand	3.5	-0.5	2.1	-4.7	-6.9	-3.4	0.7	1~3	251.3	-4.5
	Vietnam	3.7	1.8	3.2	-3.9	-4.7	-4.7	2.5	4.0		-3.0
	Malaysia	4.2	3.8	3.7	-5.2	-5.9	-4.1	2.1		118.3	1.1
	Korea	4.6	4.5	4.2	-2.2	-2.9	-2.8	2.6	2.0	99.0	-3.7
	Taiwan	14.2	15.6	15.2	-2.9	0.3	1.4	2.3			-3.5
Other	Brazil	-1.8	-0.5	-1.7	-13.4	-6.2	-7.4	9.6	3.8	163.8	0.6
	Turkey	-5.2	-2.4	-1.6	-5.3	-4.9	-5.6	19.3	5.0	76.4	-3.4
	South Africa	2.0	2.9	-0.9	-10.8	-8.4	-7.0	4.8	3~6	75.2	-0.8
	Mexico	2.4	0.0	-0.3	-4.5	-4.2	-3.5	5.8	2~4	128.9	-0.8
	Argentina	0.9	1.0	0.8	-8.6			51.9		68.5	-0.1
	Russia	2.4	5.7	4.4	-4.0	-0.6	0.0	6.8	4.0	359.2	9.5

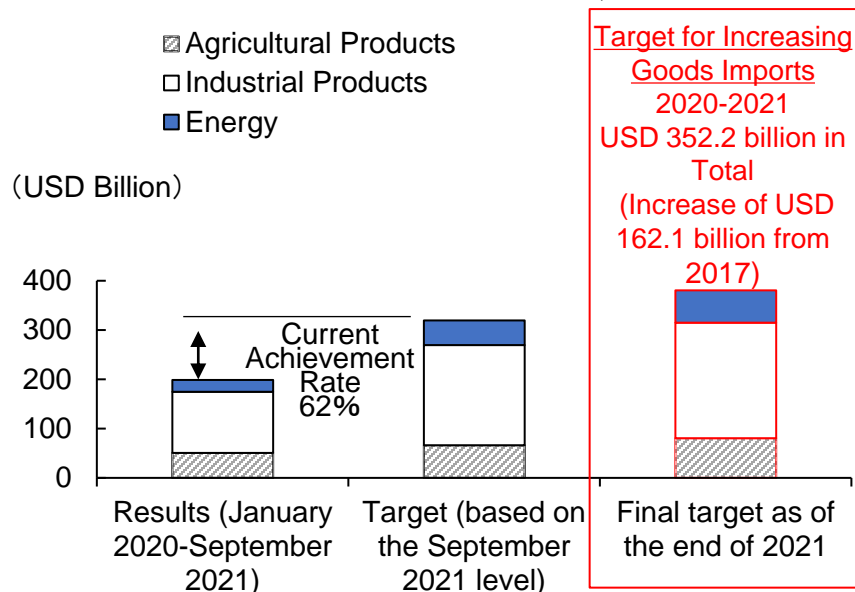
Source: JRI, based on IMF and CEIC

Note: ARA Metric (Assessing Reserve Adequacy Metric) is the ratio of actual reserves to a composite of reserve adequacy indicators based on exports, broad money, short-term debt and other liabilities, assessing the appropriate level of FX reserves. The metric for many countries assumes floating exchange rates, but for China assumes a fixed exchange rate (In case of floating rates in China, the metric rises to over 100%).

1. Asia (3) Geopolitical Risk: Recurrence of the U.S.-China conflict

- The U.S.-China phase one agreement has expired, but China's expansion of imports seems to have fallen short of the agreed-upon targets. Talks on a phase two agreement, which includes measures to subsidize domestic industries in China, will likely begin.
- China has little chance of joining the CPTPP. Also, the U.S. is emphasizing "friend shoring" from the viewpoint of economic security and is moving to launch a new economic framework.

<China's Target for Increasing the Import of Goods from the United States>



Source: Prepared by The Japan Research Institute, Limited based on PIIE: US-China phase one tracker

Note: Target for increasing goods imports based on the 2017 level is USD 162.1 billion in total between 2020 and 2021, but when service imports are included, it is USD 200 billion.

<Challenges Concerning China's Participation in the CPTPP>

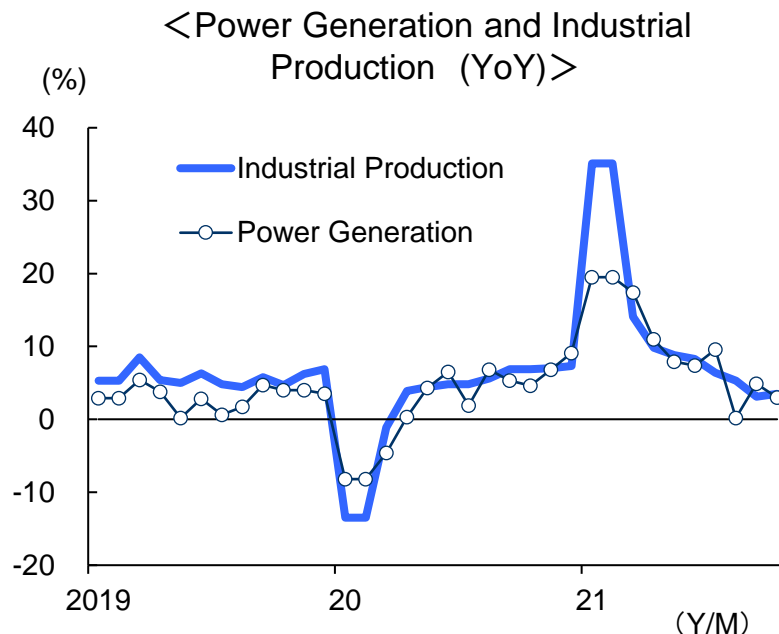
Point at issue	Provisions of the CPTPP	China's response	Issues
State-owned enterprises	Chapter 17	Reform has been implemented with an awareness of the CPTPP's rules related to the chapter on state-owned enterprises based on the "Three-Year Action Plan for Reform of State-owned Enterprises."	The use of state-owned enterprises to secure national economic security and the promotion of business combinations among state-owned enterprises may violate the rules of the CPTPP. China may assume to be exempted from application of the rules.
Labor	Chapter 19	With regard to the ILO Declaration on Fundamental Principles and Rights at Work, China has ratified the abolition of child labor, and the elimination of employment and occupational discrimination, but has not ratified the recognition of freedom of association and the right to collective bargaining and the elimination of forced labor.	China does not guarantee the right to form a labor union, and forced labor is suspected of occurring. It is highly questionable whether China is prepared to accept work-related rules.
Electronic commerce	Chapter 14	China has accepted the RCEP provisions that prohibit cross-border information transfer restrictions and prohibit data localization.	Under the RCEP, exceptions are made where the country "deems it necessary to achieve legitimate public policy objectives." China may be considering making extensive use of security exceptions.

Source: Prepared by The Japan Research Institute. Limited based on RIETI Policy Discussion Paper Series 21-P-016 "China and CPTPP", <https://www.rieti.go.jp/en/publications/summary/21090002.html>

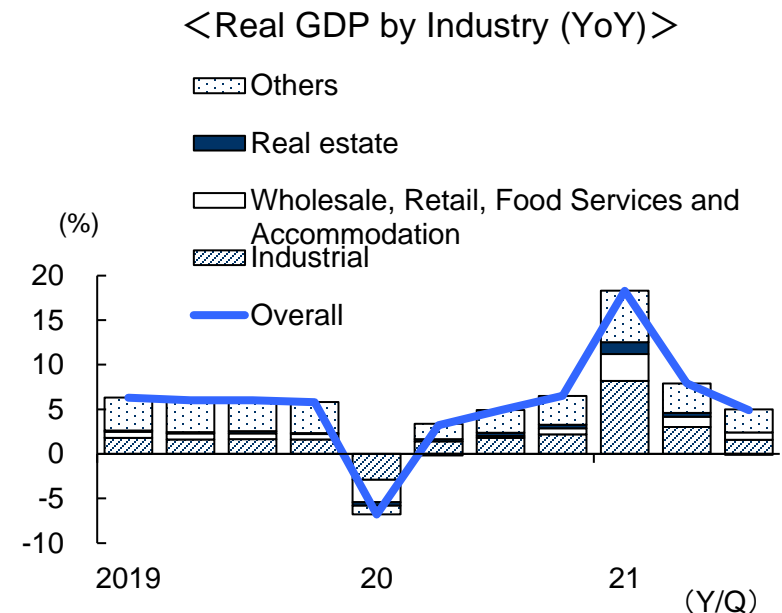
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2. China (1) Sharp slowdown of the economy in H2 2021

- Industrial production growth slowed due to electricity shortages caused by high coal prices.
- Tighter restrictions on activities to contain the coronavirus outbreak, adjustments in the real estate market, shortages of semiconductors and government measures to curb investment in infrastructure are also weighing on the economy.



Source: "Increase in Industrial Production by Enterprises of a Certain Size" by the National Bureau of Statistics of China

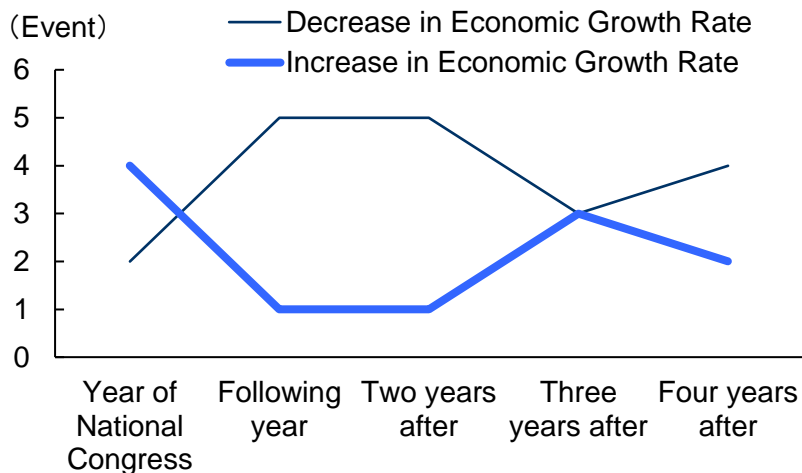


Source: Prepared by The Japan Research Institute, Limited based on "System of National Accounts" by the National Bureau of Statistics of China

2. China (2) The economy is expected to grow by +5.4% in 2022

- The government is likely to ease its measures to curb investment ahead of the Communist Party National Congress in autumn 2022. Investment in fixed assets, mainly in digital and environment-related facilities and infrastructure, is expected to expand.
- The power shortage is expected to be resolved with support from the government, including the resumption of operations at suspended coal mines.

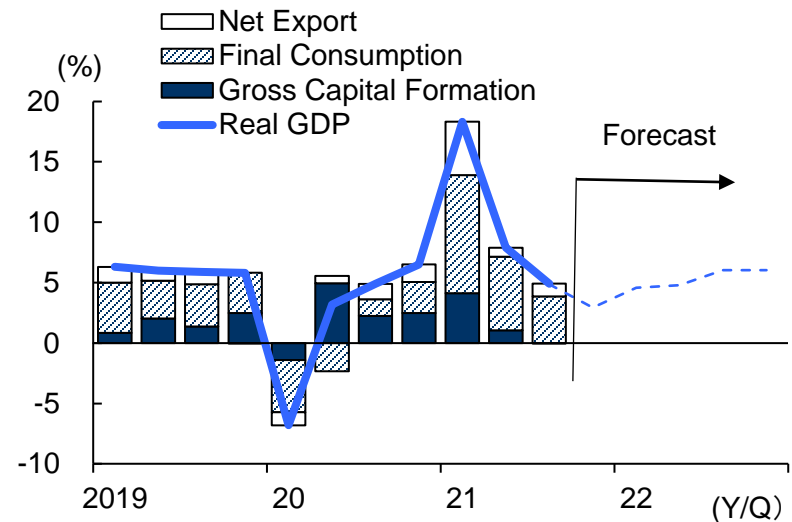
<Relationship Between Political Events and Economic Changes>



Source: Prepared by The Japan Research Institute, Limited based on "System of National Accounts" by the National Bureau of Statistics of China

Note: Data between 1991 and 2020. Real GDP growth rate for the year in which the National Congress was held increased from the previous year four times in total.

<Real GDP by Expenditure (YoY)>

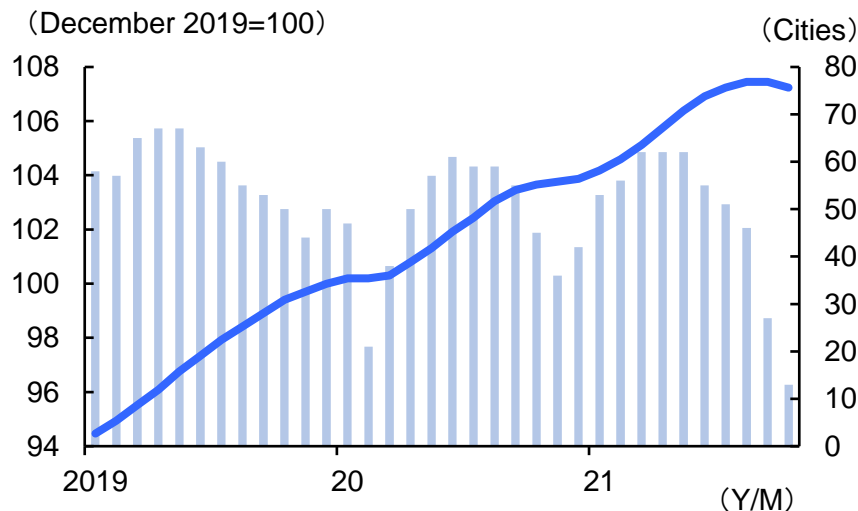


Source: Prepared by The Japan Research Institute, Limited based on CEIC and "System of National Accounts" by the National Bureau of Statistics of China

2. China (3) Real estate market heading for a soft landing

- Housing prices in major cities fell for the first time in 6.5 years, but serious adjustments such as a sharp drop in real estate prices and a drastic decline in investment in real estate development are unlikely.
- There is no overstock in the real estate industry. The rise in house prices is within the range of income growth on a national average. The government's measures to curb real estate investment will be eased.

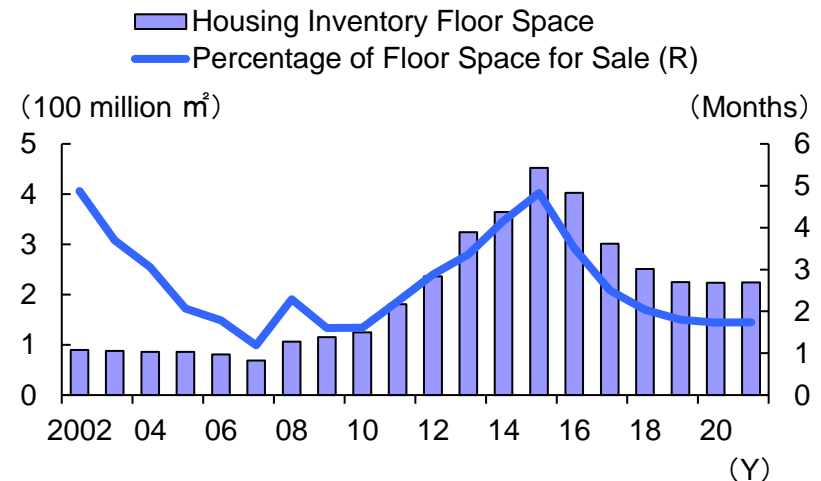
<House Prices in 70 Major Cities>



Source: JRI based on the National Bureau of Statistics of China

Notes: Index was compiled using month on month changes in the selling prices of housing.

<Real Estate Inventory>



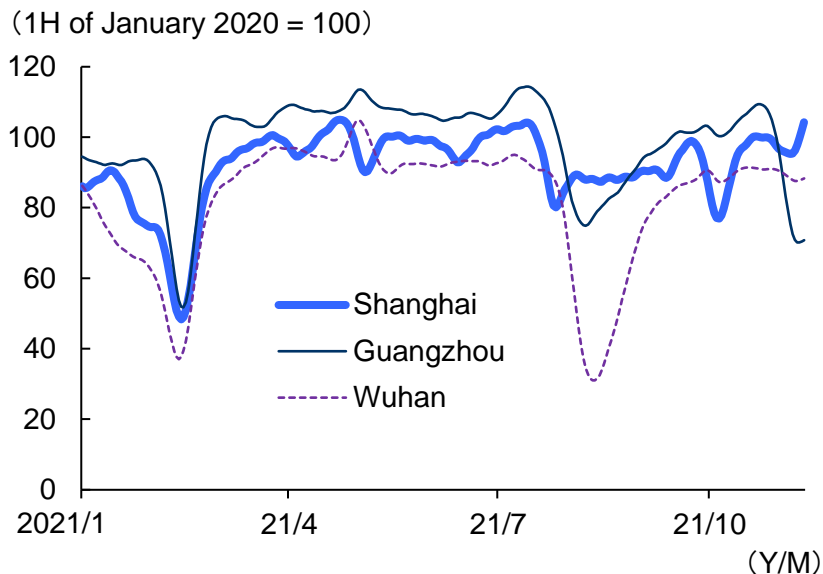
Source: Prepared by The Japan Research Institute, Limited based on "National Real Estate Development Investment and Sales Report" by the National Bureau of Statistics of China

Note: The latest figure is as of the end of September 2021.

2. China (4) Downside risks remain amid a prolonged pandemic

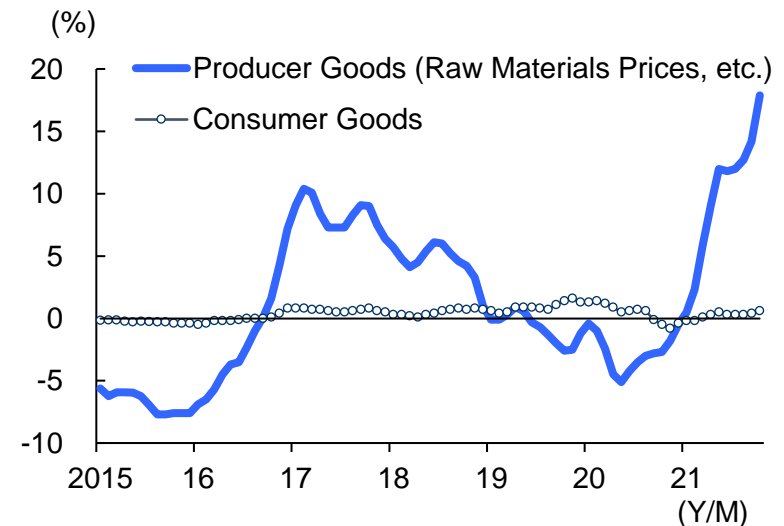
- Outbreaks of new Covid-19 variants may again require major restrictions on activity.
- If there is no halt to the rise in energy prices and production goods prices, corporate profits will be squeezed, and capital investment and production activities may decline.

<Number of Subway Passengers (HP Filter)>



Source: Prepared by The Japan Research Institute, Limited, based on "Subway Passenger Volume" by Wind Database

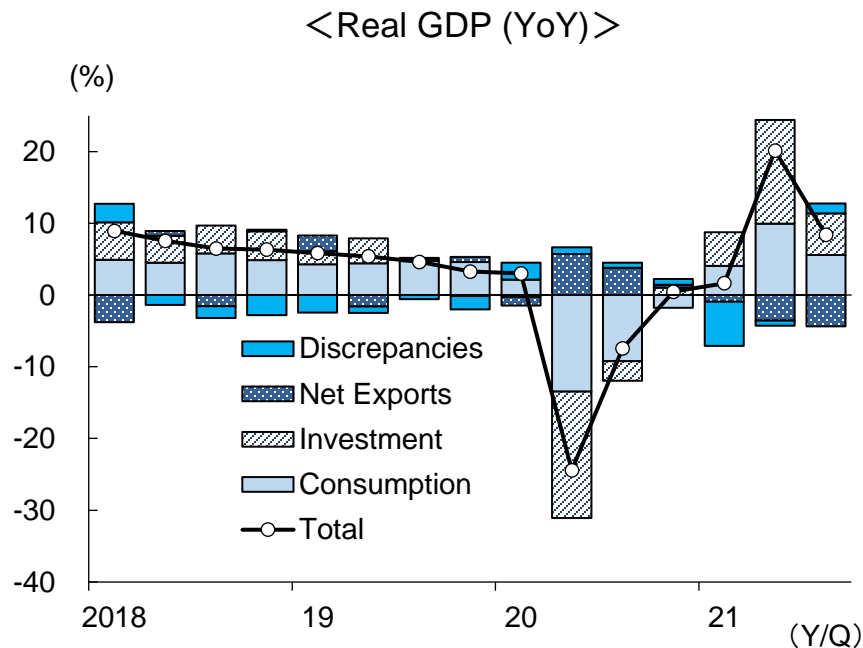
<Producer Price Index (PPI) for Industrial Products (YoY)>



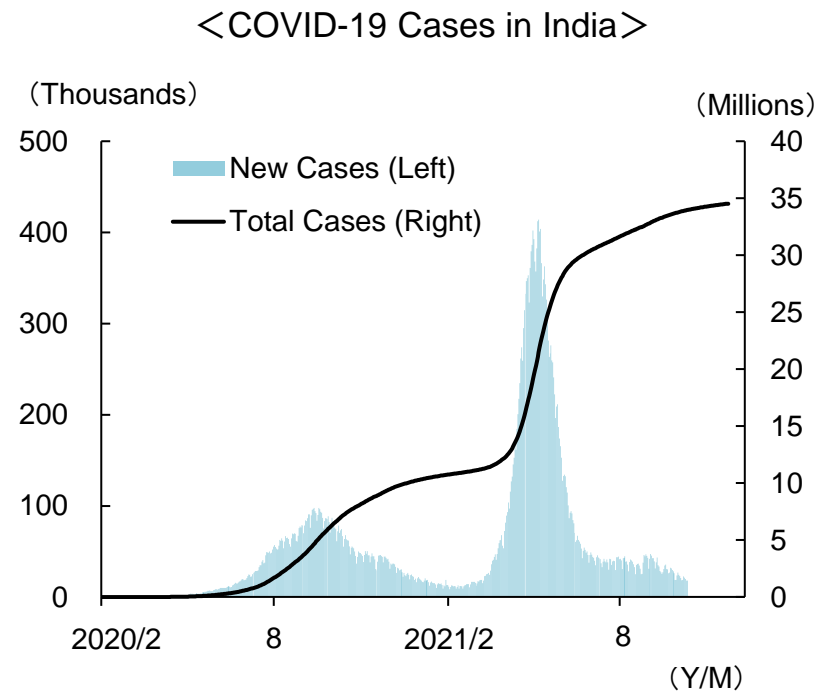
Source: "Producer Price Index for Industrial Products" by the National Bureau of Statistics of China

3. India (1) The economy recovered after a temporary deterioration

- The Indian economy temporarily deteriorated through the middle of 2021 due to the explosion of infection mainly caused by the Delta variant of Covid-19.
- The economy has returned to a recovery trend following the resumption of economic activities following a decrease of infection cases.



Source: Ministry of Statistics and Programme Implementation

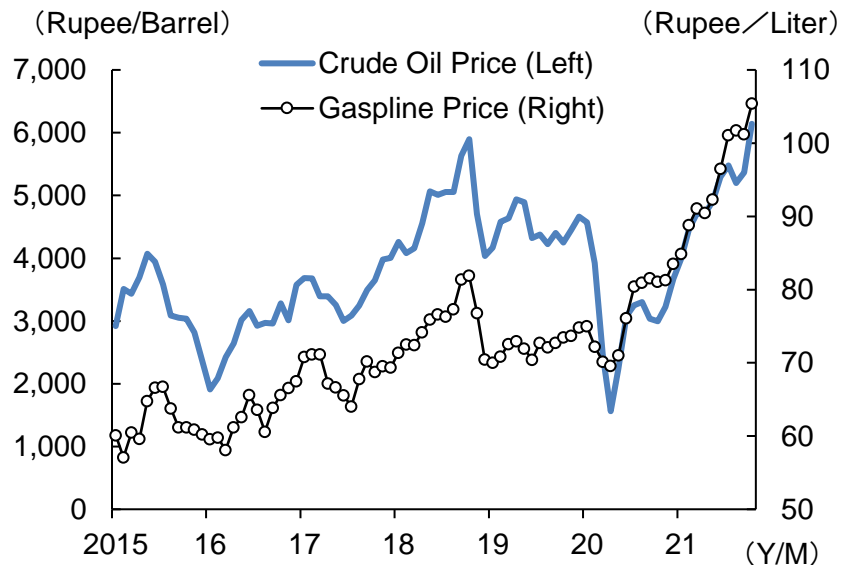


Source: WHO

3. India (2) Further acceleration of economic recovery is not expected

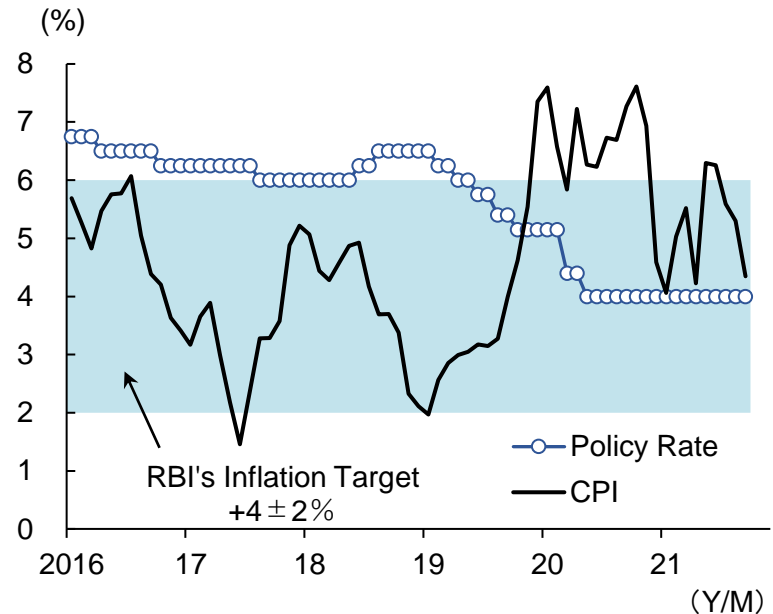
- Against the backdrop of widespread vaccination and other factors, the risk of another outbreak like the one in early spring has declined.
- However, a strong recovery in the H2 FY2021 is unlikely given the inflationary pressures stemming from soaring resource prices and electricity shortages.

<Crude Oil Price and Gasoline Price>



Source: Indian Oil Corporation, Ministry of Petroleum and Natural Gas

<CPI (YoY) and Policy Rate (Repo Rate)>

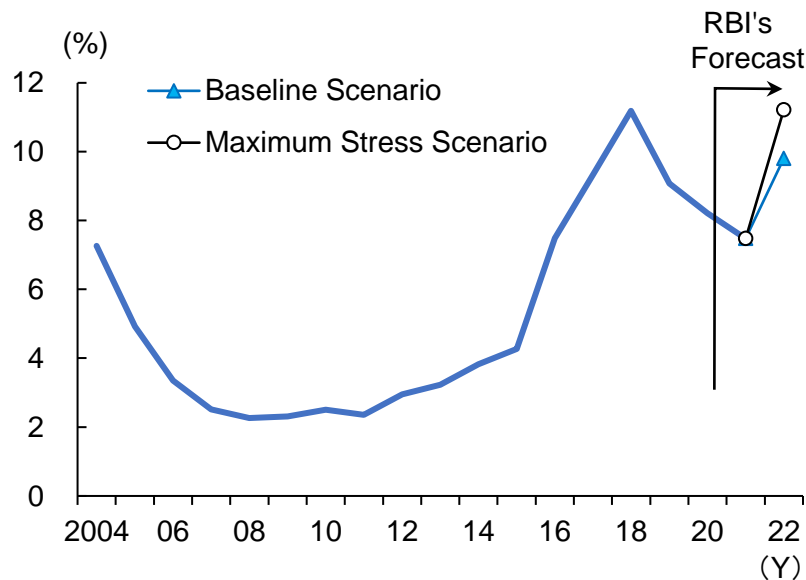


Source: Reserve Bank of India

3. India (3) Downside risks remain

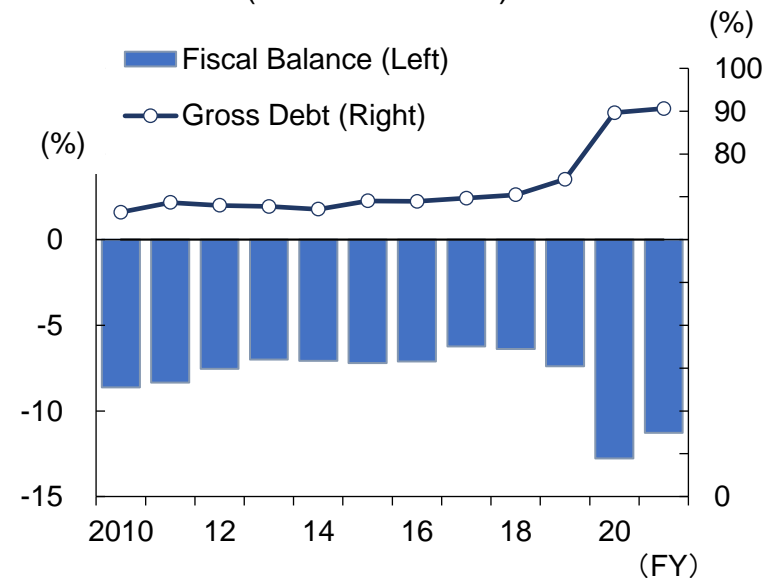
- Risks of economic downturns include (1) an outflow of funds from India due to the U.S. policy rate hikes, (2) a rise in the ratio of nonperforming loans held by commercial banks, and (3) a shift in policy toward fiscal reconstruction.
- In order for India to enhance the stability of its economic growth, it is essential to accelerate structural reforms, such as land and labor reforms, which will lead to an increase in inward FDI in the manufacturing industry, and reform of state-run banks.

<Commercial Bank's Gross Non-Performing Assets Ratio>



Source: Reserve Bank of India

<General Government's Fiscal Situation (Percent to GDP)>



Source: IMF "World Economic Outlook 2021 October"

**This is a English version of 【アジア経済見通し】アジアの安定成長を脅かす米利上げ加速 ～供給問題がグローバル・インフレのリスクに～ ” in JRI Research Report
(<https://www.jri.co.jp/MediaLibrary/file/report/researchreport/pdf/13038.pdf>)**

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