Economics

Asia: vulnerability dashboard

DBS Group Research | 19 December 2014

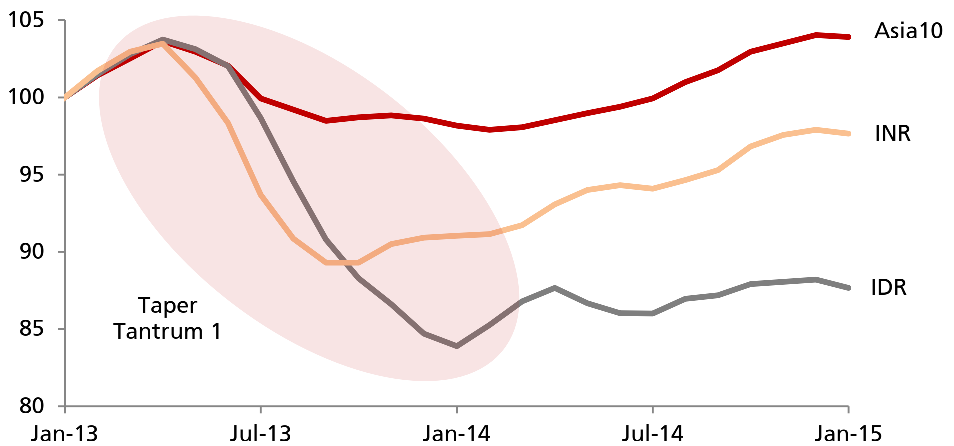
- **The Fed is inching closer to interest rate hikes. Oil prices have fallen by 45% leading to problems for some emerging markets. Contagion is a concern whether it 'makes sense' or not. Who in Asia is vulnerable to a bout of poor sentiment?**
- **As in the first 'taper tantrum' of 2013, India and Indonesia remain most vulnerable. Malaysia and Korea attract occasional attention**
- **But debt coverage ratios have improved since 2013, mainly because current account balances have improved**
- **Lower oil prices, if sustained, would benefit Asia greatly**
- **Fed hikes have been fully anticipated for more than a year**
- **Asia is well-placed to ride out another bout of weak sentiment in 2015**

The Fed is inching closer to interest rate hikes and oil prices have plunged to $60/bbl – a 45% drop from levels averaged in the first half of 2014. This has raised investor concerns about capital outflow from emerging markets similar to the 'Taper Tantrum' in 2013. Inevitably, comparisons are also drawn once again with the Asian financial crisis of 1997/98 and the Russian debt default of 1998, which was hastened / exacerbated by a 55% drop in crude prices.

Falling oil prices are, in theory, good for Asia. And markets have fully anticipated a first Fed hike in mid-2015 for more than a year now. Still, as most are aware, investors often don't distinguish one market from another nor one risk from another when sentiment sours. Contagion is a risk that has to be considered by all whether it 'makes sense' or not.

Asia – currency values vs tri-ccy

Jan13=100, incr= appr'n, 3mma, last data point is single day (Dec 18)



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Who in Asia is vulnerable to a bout of poor sentiment? Countries with low foreign currency reserves and / or large amounts of foreign borrowings. Generally, that means India and Indonesia, as it did in 2013, though Malaysia and Korea attract attention in this regard as well. For the most part, Asia's debt fundamentals have improved modestly since 2013 and very significantly since 1997/98, owing to improved current account balances.

From the longer-term perspective, most of Asia has – and much to the chagrin of developed nations – run large trade (current account) surpluses for the past 15 years. Surpluses mean you are lending to other countries (or paying down earlier debts), not building up new liabilities. For a detailed report about how Asia's debt fundamentals have evolved since 1997, readers are referred to "Asia-vu 3: are we there yet?", written in September of 2013 as the first taper tantrum unfolded.

But balances and other debt fundamentals have generally improved since 2013 as well. The charts and tables below are provided as rough-and-ready reference to current accounts, debt and reserves since 2013 – a 'vulnerability dashboard' to capital outflow in the current environment. Before turning to them, however, we consider the risks of US interest rate hikes and the gain to Asia from lower oil prices.

Taper tantrum 2?

Emerging markets sold off sharply following Fed ex-chairman Bernanke's announcement in mid-2013 that QE3 would likely start to be tapered by that year's end. Fortunately, Asia was spared most of the turmoil. Most currencies and markets remained stable or even rose. Between May13 and Jan14, Asia's currencies fell by 3%-4% against the dollar (chart page 1) and then regained lost ground over the course of 2014. India and Indonesia were the exceptions – the rupiah fell by 18% and has recovered relatively little of its lost ground; the rupee fell by 12% but has recouped two-thirds of its losses (chart on page 1).

How likely is another round of Fed-led capital outflow? We think quite low. When Bernanke announced the taper, it caught most people by surprise. QE3 had only run for 8 months and all of a sudden it looked like it was being re-called. Nobody knew how quickly that might occur nor how quickly interest rates might rise thereafter. Uncertainty reined; markets understandably reacted sharply.

Things are different today. The US economy has undergone another 6 quarters of modest recovery and QE has been smoothly / uneventfully tapered out of existence. Most importantly, markets have fully anticipated a mid-2015 Fed hike for more than a year. If hikes do come in mid-2015, markets would have completely anticipated the event for 18 months. Volatility can't be ruled out but 'tantrums' like what occurred in 2013 seem most unlikely.

As in 2013, Asia has so far been spared most of the recent market volatility. Compared to November average levels, Asia-10 currencies are down by 1.5% against the dollar. But they are up against the yen and down by only a little against the euro. Against a tri-currency basket of dollars, euros and yen, Asia-10 currencies have fallen only 0.5% since November (table below). This time, the ringgit has suffered along with the rupee and rupiah. The peso, baht, won and HK dollar have all strengthened against the tri-currency basket.

Asia – FX appreciation since Nov 2014

% appreciation, Dec 18 relative to Nov14 avg

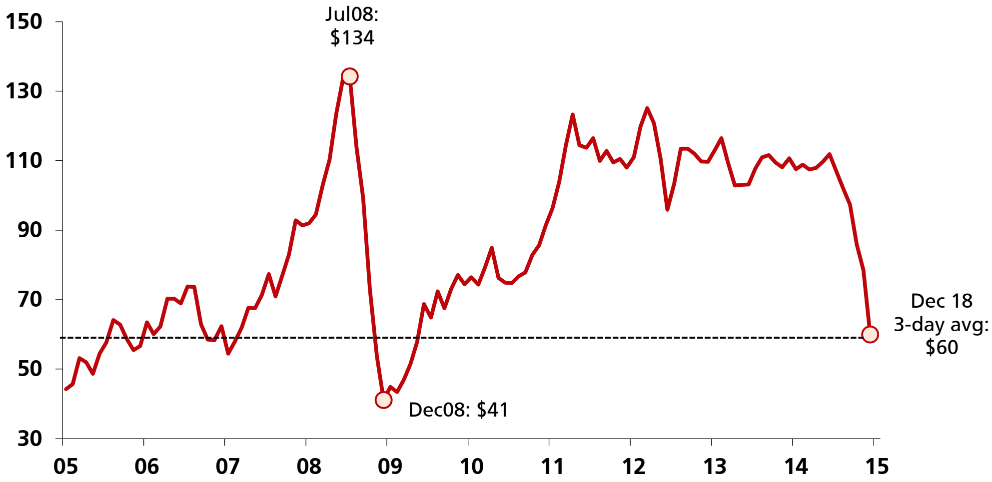
	CNY	HKD	KRW	TWD	IDR	SGD	MYR	PHP	THB	INR	A10	A9	A Big 3	Asean5
vs USD	-1.4	0.0	-0.5	-2.1	-3.3	-1.2	-3.7	0.5	-0.4	-2.4	-1.5	-1.5	-2.4	-1.6
vs JPY	0.4	1.8	1.3	-0.3	-1.5	0.6	-1.9	2.4	1.4	-0.7	0.3	0.3	-0.6	0.2
vs EUR	-0.4	1.0	0.5	-1.1	-2.3	-0.2	-2.7	1.6	0.6	-1.4	-0.4	-0.4	-1.4	-0.6
vs Tri ccy	-0.5	0.9	0.4	-1.2	-2.4	-0.3	-2.8	1.5	0.5	-1.5	-0.5	-0.5	-1.4	-0.7

Oil prices

At US$60/bbl for Brent crude, oil prices have fallen by 45% from the $109/bbl averaged in 2013 and 1H14. To the extent this is due to more supply and not less demand, Asia benefits very significantly. This is because all Asia-10 countries are net importers of oil / petrochemical products. If oil prices fall, Asia keeps more of its hard-won GDP at home, rather than sending it abroad in payment for oil. Who benefits most? Those with the biggest deficits – Thailand, India, Singapore and the Philippines.

Oil price — brent crude

US$ / bbl, month avg

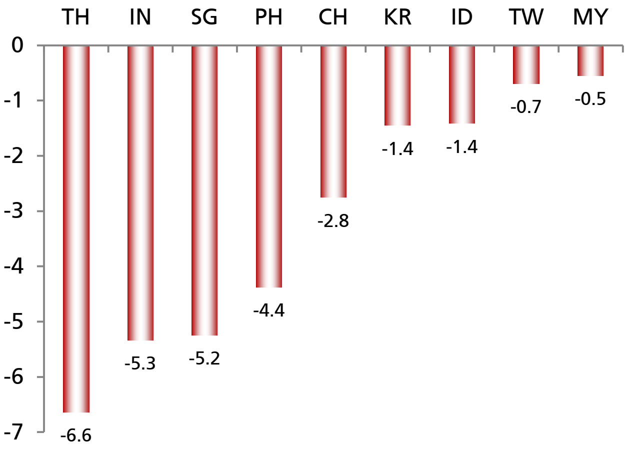


In 2014, Thailand's petrochemical trade deficit amounted to 6.6% of GDP. India's amounted to 5.3% of GDP. If oil prices were to remain at $60/bbl over the course of 2015, petrochemical balances would, in the first instance, improve by about 45% – giving each country an effective 'tax reduction' equal to that dollar amount. In Thailand, that 'gift' amounts to 3% of GDP; in India and Singapore, it's worth 2.4% of GDP. China's 'tax reduction' is worth 1.2% of GDP. The average tax reduction in the Asia-10 is 1.4% of GDP.

The drop in oil prices thus brings a very significant one-off boost to GDP. The caveat / risk is that some of the drop in oil prices is likely due to weak global demand. To the extent this is true, the nominal improvement in petrochemical trade balances would be offset by slower global growth.

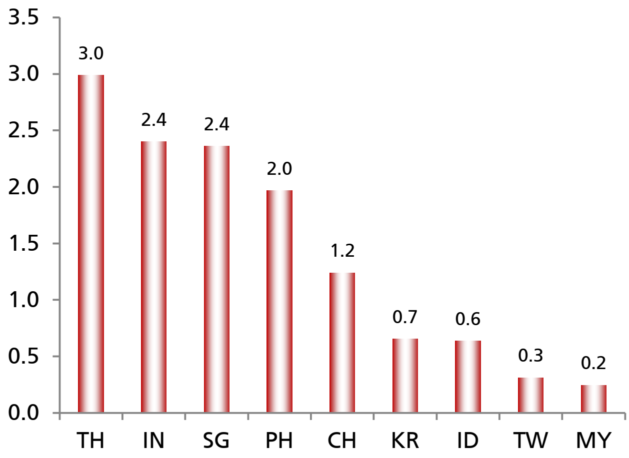
Asia – petrochemical trade balance

% of GDP



Asia – improvement in trade bal if $60 oil persists

% of GDP



Foreign reserves and external debt

Prospects for US rate hikes were surely priced in long-ago. Lower oil prices should be highly beneficial for Asia. But sentiment is sentiment and when investors want out they want out. Who's vulnerable in Asia? The tables and appendices below may offer some guidance.

Growth in Asia's foreign reserves slowed dramatically in late-2011 and in some countries, most notably Singapore, they have fallen since then. As a percentage of GDP, Singapore's 'effective' reserves remain the largest in Asia at 100% [1]. Taiwan also has large foreign reserve holdings equivalent to 83% of GDP. Most countries hold reserves equivalent to 30%-45% of GDP. India and Indonesia hold the least foreign reserves in Asia, with ratios of 16% and 11% respectively.

Relative to external debt, India, Indonesia and Malaysia again hold the fewest reserves. Coverage ratios are some 30% of total external debt in Indonesia and run about 60% in India and Malaysia.

Fortunately, countries have reduced their short-term (< 1 year) borrowings significantly. As a percentage of short-term external debt, reserve cover runs between 100% (Malaysia) and 828% (Philippines) with an average of 355% for the countries shown in the table below (See also Appendix III).

Asia-10: Foreign reserves and key ratios

	SG	MY	ID	TH	PH	IN	KR	TW	CH
Reserves (effective, USD bn)									
end-2012	364	134	104	195	87	248	365	403	3,312
end-2013	340	125	83	182	84	261	397	417	3,821
2014	309	116	97	173	79	326	423	421	3,810
Reserves (effective, % of GDP)									
end-2012	127	44	12	53	35	13	30	85	39
end-2013	114	40	10	47	31	13	30	85	40
2014	100	35	11	46	28	16	30	83	36
Reserves (effective, % of total gross external debt)									
end-2012		68	41	147	144	63	89		
end-2013		59	31	130	143	61	95		
2014		50	33	120	137	73	99		
Reserves (effective, % of short-term gross external debt)									
end-2012		145	236	322	1,023	266	285		
end-2013		120	191	304	746	282	345		
2014		103	199	294	828	371	336		

Notes
1. Effective reserves are the sum of spot holdings and forward holdings [1].
2. Gross debt liabilities of SG, TW and CH are excluded as they are large net creditors.

Current account balances

It's been a year and a half since the Taper Tantrum of 2013. For the most part, Asia's debt fundamentals and foreign reserve holdings haven't changed significantly since then. India's, Indonesia's and Korea's debt cover has remained stable. Thailand's and the Philippines' coverage ratios have slipped marginally but remain high. Malaysia's coverage ratio has fallen more significantly and is beginning to worry.

Asia-10: current account balances
% of GDP

	SG	MY	ID	TH	PH	IN	KR	TW	CH
2013	19.0	3.0	-3.3	-0.8	3.7	-4.7	6.2	11.2	1.9
2014	19.0	4.3	-3.0	1.9	2.9	-1.7	5.9	12.5	3.1
2015f	20.0	5.0	-2.7	1.1	1.8	-1.6	6.7	13.0	3.7
With $60 oil for full year									
2015f	22.4	5.2	-2.1	4.1	3.8	0.8	7.4	13.3	4.9

Note: India refers to FY beginning April.

Importantly, current account balances in India and Indonesia have improved since mid-2013, some very significantly. In terms of full year totals, Indonesia's deficit improved by 0.3 percentage points of GDP in 2014 to 3.0%. India's deficit sharply improved to 1.7% of GDP in FY14 from 4.7% in FY13. Thailand moved from deficit in 2013 to a surplus of 2% of GDP in 2014. Malaysia maintains a solid surplus of 4%-5% of GDP; China's surplus has risen again in 2014 to 3% of GDP. Singapore, Korea and Taiwan all maintain exceptionally large surpluses. And, as explained above, all of Asia should benefit significantly in 2015 if oil prices remain low and this will come mainly via improved current account balances (see table above).

Bottom line

With debt ratios steady, current accounts improved, oil prices lower and Fed hikes long-ago priced in, Asia appears more than able to ride out any bouts of weak investor sentiment that may arise in the months ahead.

Notes

[1] Effective reserves are the sum of spot holdings and forward holdings. As a part of the IMF reforms following the Asian crisis in 1997/98, most countries now report forward currency holdings to the IMF. This gives investors a truer and more transparent view of reserve holdings. The issue arose out of the experience in Thailand, which had, during the crisis, sold its reserves forward to support the baht. While (spot) reserves appeared large, they had already been sold forward and would have to be delivered in 2-3 months' time. In effect, foreign reserves were already zero. The same transparency is gained when countries try to keep currency values low by buying reserves forward rather than selling them. For a fuller discussion of effective reserves, see "Singapore attempts the impossible", Dec 6, 2010.

Sources:

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

Appendix I

Gross External Debt (USD bn)

	MY	ID	TH	PH	IN	KR	TW
Total							
end-2012	196.5	252.3	133.2	60.3	394.1	408.9	130.8
end-2013	213.8	265.9	139.8	58.5	427.6	416.1	170.1
2014	230.1	292.3	143.9	58.1	450.1	429.1	191.7
Short-term							
end-2012	92.3	44.2	60.6	8.5	93.3	128.0	116.5
end-2013	103.9	43.6	59.9	11.2	92.7	115.2	155.6
2014	113.1	48.9	58.8	9.6	87.9	126.1	176.6
Long-term							
end-2012	104.2	208.1	72.6	51.8	300.8	280.9	14.3
end-2013	109.9	222.3	79.9	47.3	334.9	300.9	14.5
2014	117.1	243.4	85.1	48.5	362.2	303.0	15.1
Private-sector							
end-2012	124.2	126.2	107.0	15.1	#N/A	286.3	127.5
end-2013	139.7	142.3	114.6	18.0	#N/A	285.1	167.8
2014	154.0	159.3	117.6	17.1	#N/A	297.4	189.7
Public-sector							
end-2012	72.3	126.1	26.2	45.2	#N/A	122.6	3.3
end-2013	74.0	123.6	25.2	40.5	#N/A	131.0	2.3
2014	76.2	133.0	26.3	41.0	#N/A	131.7	2.0

Gross External Debt (% of GDP)

	MY	ID	TH	PH	IN	KR	TW
Total							
end-2012	64.4	28.8	36.4	24.1	20.8	33.4	27.5
end-2013	68.3	30.6	36.1	21.5	22.1	31.9	34.7
2014	69.8	34.4	38.2	20.3	21.6	30.0	37.9
Short-term							
end-2012	30.3	5.0	16.6	3.4	4.9	10.5	24.5
end-2013	33.2	5.0	15.5	4.1	4.8	8.8	31.7
2014	34.3	5.8	15.6	3.4	4.2	8.8	34.9
Private-sector							
end-2012	40.7	14.4	29.2	6.0	#N/A	23.4	26.8
end-2013	44.6	16.4	29.6	6.6	#N/A	21.8	34.2
2014	46.7	18.7	31.2	6.0	#N/A	20.8	37.5
Short-term external debt (% of total)							
end-2012	47.0	17.5	45.5	14.1	23.7	31.3	89.1
end-2013	48.6	16.4	42.8	19.1	21.7	27.7	91.5
2014	49.1	16.7	40.9	16.5	19.5	29.4	92.1

Note: 2014 numbers are as of Sep-14, except for SG, PH and IN as of Jun-14

GDP (USD bn)

	MY	ID	TH	PH	IN	KR	TW
2012	305	877	366	250	1,894	1,223	476
2013	313	870	387	272	1,936	1,305	490
2014f	330	850	377	286	2,081	1,429	506

Appendix II

	SG	MY	ID	TH	PH	IN	KR	TW	CH
Net oil exports (USD bn)									
2012	-19.1	1.3	-5.6	-20.9	-13.2	-107.6	-79.2	-14.5	-290.0
2013	-17.0	0.5	-12.6	-25.6	-12.2	-101.3	-77.2	-11.0	-290.0
2014f	-16.2	-1.8	-12.0	-25.0	-12.5	-111.0	-20.7	-3.5	-290.0
Net oil exports (% of GDP)									
2012	-6.7	0.4	-0.6	-5.7	-5.3	-5.7	-6.5	-3.0	-3.5
2013	-5.7	0.1	-1.4	-6.6	-4.5	-5.2	-5.9	-2.2	-3.0
2014f	-5.2	-0.5	-1.4	-6.6	-4.4	-5.3	-1.4	-0.7	-2.8
Improvement in oil trade balance with persistent $60 oil									
USD bn	7.3	0.8	5.4	11.3	5.6	50.0	9.3	1.6	130.5
% of GDP	2.4	0.2	0.6	3.0	2.0	2.4	0.7	0.3	1.2
GDP (USD bn)									
2012	287	305	877	366	250	1,894	1,223	476	8,391
2013	298	313	870	387	272	1,936	1,305	490	9,541
2014f	309	330	850	377	286	2,081	1,429	506	10,525

Appendix III

Foreign reserves and key ratios

	SG	MY	ID	TH	PH	IN	KR	TW	CH
Reserves (effective, USD bn)									
end-2012	364	134	104	195	87	248	365	403	3,312
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end-2013		120	191	304	746	282	345		
2014		103	199	294	828	371	336		
Reserves (effective, % of Private sector debt)									
end-2012		108	83	182	576	#N/A	127		
end-2013		90	58	159	464	#N/A	139		
2014		75	61	147	465	#N/A	142		
GDP (USD bn)									
total 2012	287	305	877	366	250	1,894	1,223	476	8,391
total 2013	298	313	870	387	272	1,936	1,305	490	9,541
est total 2014	309	330	850	377	286	2,081	1,429	506	10,525

Notes
1. Effective reserves are the sum of spot holdings and forward holdings. See end note 1
2. Gross debt liabilities of SG, TW and CH are excluded as they are large creditor countries.

GDP & inflation forecasts

	GDP growth, % YoY					CPI inflation, % YoY				
	2011	2012	2013	2014f	2015f	2011	2012	2013	2014f	2015f
US	1.6	2.3	2.2	2.2	2.5	3.1	2.1	1.5	1.8	1.9
Japan	-0.5	1.5	1.5	0.3	1.3	-0.3	0.0	0.4	2.8	1.5
Eurozone	1.6	-0.7	-0.4	0.8	0.9	2.7	2.5	1.3	0.5	0.8
Indonesia	6.5	6.2	5.8	5.0	5.5	5.3	4.0	6.4	6.4	6.5
Malaysia	5.1	5.6	4.7	5.9	5.2	3.2	1.7	2.1	3.2	4.2
Philippines	3.6	6.8	7.2	5.9	6.2	4.7	3.2	2.9	4.2	4.0
Singapore	6.0	1.9	3.9	3.0	3.2	5.2	4.6	2.4	1.1	1.7
Thailand	0.1	6.4	2.9	0.8	3.8	3.8	3.0	2.2	2.0	2.6
Vietnam	5.9	5.0	5.4	5.7	6.0	18.6	9.3	6.6	4.8	5.8
China	9.3	7.7	7.7	7.5	7.0	5.4	2.6	2.6	2.7	2.2
Hong Kong	4.9	1.5	2.9	2.6	2.3	5.3	4.1	4.3	4.4	3.4
Taiwan	3.8	2.1	2.2	3.5	3.7	1.4	1.9	0.8	1.3	1.0
Korea	3.7	2.3	3.0	3.4	3.4	4.0	2.2	1.3	1.3	1.7
India*	6.7	4.5	4.7	5.6	6.1	9.0	7.4	9.5	6.8	6.1

* India data & forecasts refer to fiscal years beginning April; prior to 2013.
Source: CEIC and DBS Research

Policy & exchange rate forecasts

	Policy interest rates, eop					Exchange rates, eop				
	current	1Q15	2Q15	3Q15	4Q15	current	1Q15	2Q15	3Q15	4Q15
US	0.25	0.25	0.25	0.25	0.50	...	...	...	...	...
Japan	0.10	0.10	0.10	0.10	0.10	118.9	121	122	123	124
Eurozone	0.05	0.05	0.05	0.05	0.05	1.228	1.23	1.22	1.21	1.20
Indonesia	7.75	7.75	7.75	7.75	7.75	12,500	12,375	12,550	12,725	12,900
Malaysia	3.25	3.25	3.50	3.50	3.50	3.47	3.38	3.40	3.42	3.43
Philippines	4.00	4.00	4.00	4.00	4.25	44.8	45.2	45.2	45.3	45.4
Singapore	n.a.	n.a.	n.a.	n.a.	n.a.	1.31	1.32	1.32	1.32	1.33
Thailand	2.00	2.00	2.00	2.00	2.00	32.8	33.1	33.3	33.4	33.6
Vietnam^	6.50	6.00	6.00	6.00	6.00	21,408	21,250	21,250	21,250	21,250
China*	5.60	5.60	5.35	5.35	5.35	6.22	6.14	6.11	6.08	6.05
Hong Kong	n.a.	n.a.	n.a.	n.a.	n.a.	7.76	7.76	7.77	7.77	7.78
Taiwan	1.88	1.88	1.88	1.88	2.00	31.5	31.4	31.5	31.7	31.8
Korea	2.00	1.75	1.75	1.75	2.00	1102	1110	1130	1140	1150
India	8.00	8.00	7.50	7.50	7.50	63.1	63.4	64.4	65.5	66.5

^ prime rate; * 1-yr lending rate

Market prices

	Policy rate	10Y bond yield		FX		Equities		
	Current (%)	Current (%)	1wk chg (bps)	Current	1wk chg (%)	Index	Current	1wk chg (%)
US	0.25	2.21	0	89.2	0.2	S&P 500	1,990	-3.4
Japan	0.10	0.35	-7	118.9	0.6	Topix	1,379	-4.7
Eurozone	0.05	0.62	-10	1.228	-0.8	Eurostoxx	2,836	-7.7
Indonesia	7.75	8.14	18	12500	-0.9	JCI	5,108	-0.7
Malaysia	3.25	4.29	28	3.48	0.2	KLCI	1,697	-2.5
Philippines	4.00	4.40	7	44.8	-0.3	PCI	7,276	0.6
Singapore	Ccy policy	2.22	-7	1.314	0.2	FSSTI	3,294	-0.1
Thailand	2.00	2.83	-9	32.8	0.0	SET	1,478	-7.5
China	5.60	...	...	6.22	-0.8	S'hai Comp	2,953	-2.2
Hong Kong	Ccy policy	1.77	-6	7.75	0.0	HSI	23,028	-4.2
Taiwan	1.88	1.59	-5	31.5	-0.8	TWSE	8,986	-2.2
Korea	2.00	2.73	-8	1102	0.6	Kospi	1,909	-3.1
India	8.00	7.93	2	63.1	-2.0	Sensex	27,320	-2.8

Source: Bloomberg

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