



THOUGHT LEADERSHIP BRIEF

Recovery on the Horizon? An Analysis of the Performance of External Sectors in Asia Through COVID

David Skilling

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KEY ISSUES

- ▶ Many Asian economies have performed well through COVID in terms of GDP growth, exceeding the performance of economies in other parts of the world. This is partly due to high quality COVID management in many Asian economies, but is also due to a strong contribution from export growth.
- ▶ This has been supported by a surprisingly resilient globalisation profile. World trade growth (excluding international tourism) has recovered strongly; and is now well above pre-COVID levels. And Asian export growth has out-performed world trade growth.
- ▶ In addition to the strong global economic recovery, world export growth has been supported by the rotation in consumer demand during the pandemic away from (locally-produced) services towards durable goods that tend to be traded across borders. As a major production node in global supply chains, emerging Asia benefited from this.
- ▶ Looking forward, however, there are several storm clouds on the horizon: post-COVID normalisation of demand patterns, supply chain disruptions/costs, and risks to the global economic outlook, as well as the economic impact of the Russian invasion of Ukraine, is likely to reduce world trade growth. And there are structural risks to Asia's position in global supply chains. Adaptation will be required in many Asian economies in order to remain competitive, and benefit from export-led growth.



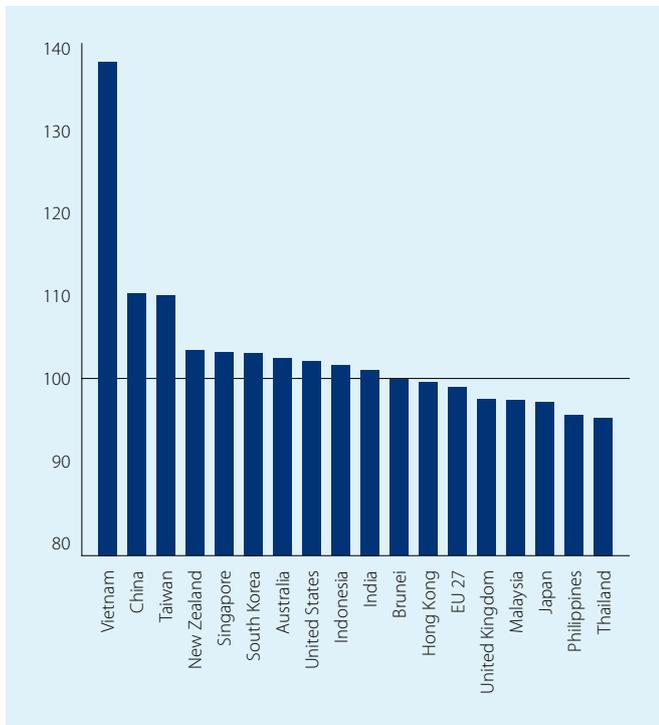
ECONOMIC PERFORMANCE THROUGH COVID

In general, Asian economies have performed well through COVID in terms of GDP outcomes. GDP for the year to Q4 2021 was meaningfully higher than for the year to Q4 2019 across multiple Asian economies.

In particular, Asian economies like Vietnam, China, Taiwan, Singapore, South Korea, and Australia and New Zealand have generated strong economic performance through the pandemic. This GDP performance has out-paced the US, which was by far the strongest performing of the G7 economies, as well as many large European economies where GDP levels that have not yet recovered to pre-COVID levels.

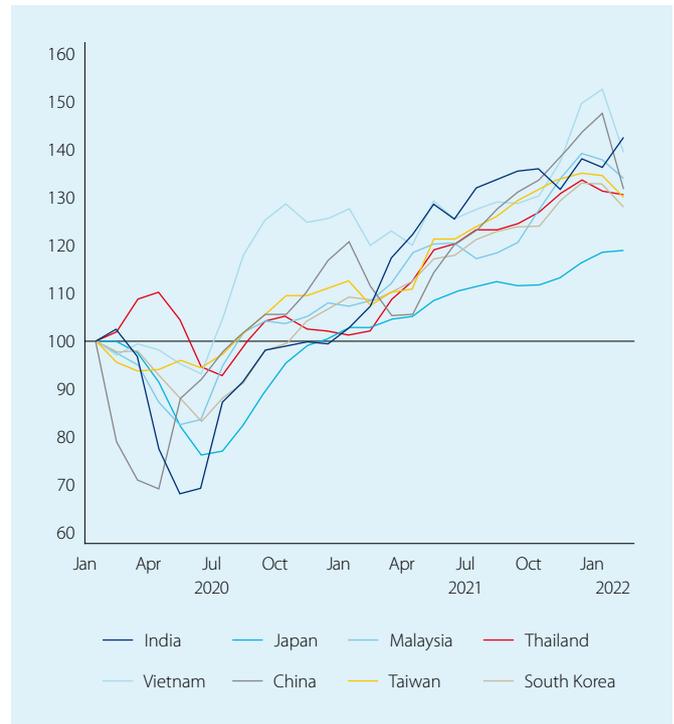
There are several reasons for this relatively strong Asian performance. The tight restrictions that controlled the spread of COVID in many Asian economies, allowed for the rapid re-opening of domestic economies from mid-2020. This allowed for stronger private consumption and investment activity in many Asian economies.

Figure 1. Real GDP (Rolling 12 Monthly), Q4 2021, Q4 2019 = 100



Source: Macrobond; National sources; Landfall Strategy Group calculations

Figure 2. Exports of Goods (Rolling 3 Monthly), Current Prices, Local Currency, January 2020 = 100



Source: Macrobond; National sources; Landfall Strategy Group calculations

In addition, resilient external demand was an important supporting factor. Export growth made a strong contribution to GDP growth. This contribution has occurred despite the collapse in international tourism revenues, to which many Asian economies are exposed. But strong growth in merchandise trade has more than offset this reduction in services exports.

The Asian economies that have generated strong GDP growth have also experienced robust rates of export growth. Exports in several leading Asian economies, such as China, South Korea, Japan, Taiwan, Singapore, are 30-40% higher in February 2022 than in January 2020.

This export growth, in the context of high exports/GDP ratios in these Asian economies, has supported strong GDP growth rates. Asian economies with export-oriented growth models have done well. Vietnam provides a good example. Exports contracted only slightly in Q2 2020 before recovering strongly. It has an export share of ~80% of GDP. This combination is a core part of the explanation for Vietnam’s very strong economic performance through the pandemic.



DRIVERS OF EXPORT PERFORMANCE

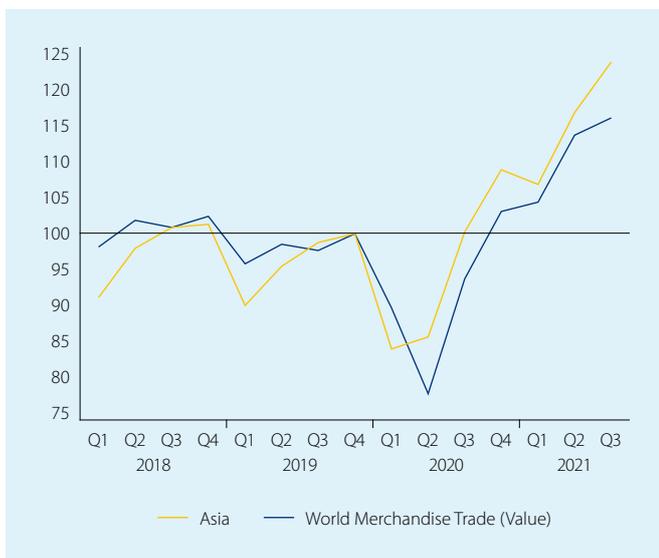
This strong export growth performance is due to a surprisingly resilient globalisation profile. World trade growth (excluding exports of services, such as international tourism) has recovered strongly; and is well above pre-COVID levels. The WTO report that world merchandise trade is ~16% higher in Q3 2021 (the latest data available) than it was in Q4 2019.

This has supported Asian economies, which are at the centre of global supply chains of manufactured goods. Indeed, Asian exports increased by 24% over this period.

An important contributing factor to this strong world trade growth, in addition to the strong overall global economic recovery, was the rotation in consumer demand during the pandemic away from (locally-produced) services towards durable goods that tend to be traded across borders. As a major node in global supply chains, Asian economies benefited from this shift in consumer demand.

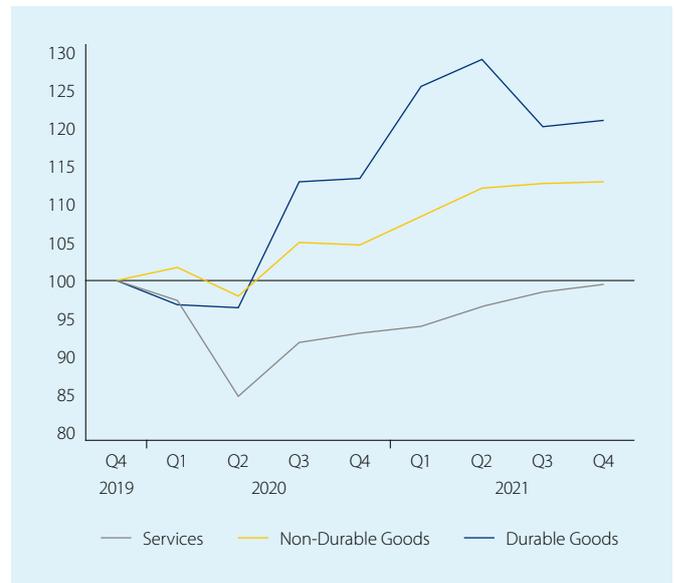
Some export categories bounced back very quickly, after an initial loss of demand in the early days of the pandemic. Exports of electronics and semiconductors, for example, experienced very strong demand over the past two years (partly reflecting the growth of the digital sector during COVID). Asian economies that were exposed to these sectors had a better record than those that were not. For example, economies like South Korea and Taiwan had very strong export performance from mid-2020.

Figure 3. World Trade, Annual % Growth



Source: Macrobond; WTO; Landfall Strategy Group calculations

Figure 4. US Household Consumption Expenditure, Q4 2019 = 100



Some Asian economies, such as Indonesia as well as Australia and New Zealand, also benefited from high commodity prices over the COVID period.

Some of Asia’s export growth potential has likely been constrained by global supply chain disruptions over the past several months, which have made it difficult to physically export goods. But even so, Asian economies have out-performed other regions in terms of both GDP and export growth.

LOOKING FORWARD

But there are questions about whether the relatively resilient Asian export performance can be sustained. There are a few sets of reasons to expect a weakening contribution from external sectors in Asia.

For example, as COVID lockdowns are lifted in many advanced economies, it is likely that consumer spending will rotate away from durable goods towards services. This will reduce the demand for traded goods, and will likely constrain demand for Asian exports.

This will likely be reinforced by a weakening of the inventory building that many firms in advanced economies have been engaged in over the past year or so. Some firms have responded to widespread global supply chain disruptions by building up inventories, which has temporarily increased the demand for exported goods. But as this inventory building ceases, and then begins to unwind, there will be a weakening in import demand.

The second set of factors relate to a weakening pace of the global recovery. As mentioned above, there was an unexpectedly vigorous economic recovery process across much of the world from mid-late 2020. However, world GDP growth forecasts are now being marked down – due to the prospect of monetary tightening as inflation rates increase, higher energy and commodity prices, supply chain disruptions, and so on. The IMF forecast a slowing in world export growth over the next few years, returning to around pre-COVID levels. This will also be the case for Asian economies.

And of course, the Russian invasion of Ukraine – and the accompanying economic sanctions – will reinforce these headwinds to global trade.

Overall, the external balance is unlikely to make the same contribution to overall Asian economic performance as has been the case over the past two years. Indeed, the merchandise trade balance across several externally-oriented Asian economies has weakened over the past several months.

Additional growth engines will be required, either in the domestic economy – or increasing competitive advantage in external sectors to generate export growth even in a less supportive environment.

The final set of reasons for expecting a weakening in Asian export growth relate to the emerging structural challenges to globalisation that may constrain the contribution of externally-oriented growth models for some Asian emerging markets. As discussed in a previous IEMS note, changes to global supply chains, the increased use of technology and reduced labour intensity, may weaken the ability of some Asian economies to rely on external sectors for growth.¹

Asian economies will need to adapt their growth models in order to continue to perform.

¹ David Skilling, 'Emerging Markets in Asia need to adapt their growth model in a post-COVID world', IEMS, 2021.

CONCLUDING REMARKS

Overall, Asian economies have performed particularly well during the COVID – particularly those that have strong export sectors. However, some of these supporting factors are likely to weaken over the coming period – likely leading to a period of weaker economic growth, unless additional domestic growth engines are identified, or competitive advantage is strengthened to support continued export growth even in a weaker global economic context. The external outlook will be more challenging for many Asian economies.



David Skilling is the Founding Director of Landfall Strategy Group, an economic and policy advisory firm that works with governments, firms and financial institutions in Australasia, Asia, the Middle East, and Europe. David has previously worked in various roles in the New Zealand Government, founded an independent economic think tank in New Zealand, and was with the McKinsey Global Institute and McKinsey & Co in Singapore.

David holds a Ph.D. in Public Policy and a Master in Public Policy degree from Harvard University, as well as a Master of Commerce degree in Economics from the University of Auckland. David was named as a Young Global Leader by the World Economic Forum in 2008.

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