Asia in 2021: Ascendant

Fiscal and monetary policymakers have ripped up the rule book in Asia this year to battle the pandemic, but the strength of the recovery in 2021 will depend on how much Asian central banks push the boundaries in terms of unorthodox monetary policies, the nature of fiscal support rather than just the amount and the momentum for the semiconductor industry

Rob Carnell: Asia in 2021

Watch video

Three main themes for Asia in 2021

Three issues most likely to dominate the outlook for Asia in 2021, excluding China are:

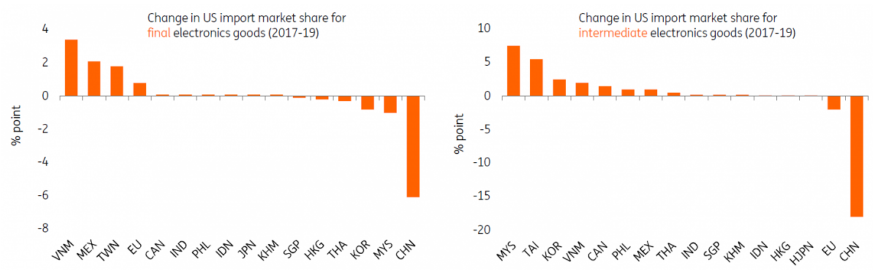
1. The development of the semiconductor cycle
2. The effectiveness of Covid-19 support measures
3. Central banks drift towards unorthodox monetary policies

1 Semiconductor upcycle

Recent export and industrial production releases around the region have shown recovery from the depths of the pandemic. But the recovery has been uneven. Most industries are still struggling. The big exception to this is semiconductors and select electronic components.

This is of especial importance to the region's semiconductor giants - South Korea and Taiwan. But there are few countries in Asia that are not tightly linked into the semi-conductors cycle. Increasingly Vietnam, Thailand and Malaysia have been taking market share from China in this sector, attracting new inward foreign direct investment as well as some relocations from China. Indonesia and India are the two least affected economies and will likely miss out on any upturn.

Gains of electronics market share from China



Source: ITC, MAS - Market share gains

While the momentum for the semiconductor industry is currently strong, this is a notoriously fickle sector, prone to overinvestment and excess capacity, price plunges as well as gains. With relations between the US and China over technology hanging in the balance, backing a continued technology upswing is not without risks.

On the other hand, China's push towards "new infra" and roll out of 5G could well provide a multi-year push for the sector, which would provide all of Asia with a considerable boost.

2 Effectiveness of fiscal support

The outlook for 2021 will be heavily tempered by how the pandemic evolves, possibility of a vaccine and potential return to more normal work and leisure practices.

But the difference between solid recoveries for some, and tepid and erratic recoveries for others, might be the scale and effectiveness of fiscal support measures put in place in 2020. All countries in Asia have provided considerable fiscal support measures, though there has been a considerable exaggeration of the scale of support in many instances, making a reliable comparison impossible.

What 2021 will show, is the effectiveness of these efforts in three important areas:

1. Protecting the business sector, and maintaining the productive capacity of the economy
2. Providing the same support/insurance, for the labour force
3. Longer-term reform measures undertaken in some economies

While there is probably some overlap between the amounts set aside for fiscal spending and the strength of the recovery in 2021, the nature of that spending may well prove as important as the amounts.

3

Unorthodox central bank policies in Asia

As well as ripping up the rule books on fiscal policy during the crisis, monetary policy has also come under assault from central banks running out of traditional support tools.

The assumption has always been that emerging market economies would not be "allowed" negative real interest rates, and if so then certainly not quantitative easing and definitely not direct deficit financing.

But while fiscal policy easing has been less constrained during the pandemic, emerging market economies have still had to pay heed to the mood of rating agencies, and that has meant preserving some vestige of fiscal respectability, some have been pushed towards more monetary easing.

Asian central banks' conventional and unconventional policy easing during Covid-19 crisis

Economies	Conventional			Unconventional					
	Rate Cuts	Near-zero/ -ve rates	CRR/SLR * cuts	Govt. bonds	Corp bonds	Comm paper	ABS **	Yield Control	Advances to govt.
Australia	√	√ / X	X	√ / X	X	X	√/X	√/X	X
China	√	X	√	X	X	X	X	X	X
India	√	X	√	√ / X	√ / X	√	X	√	√
Indonesia	√	X	√	√	X	X	X	X	√
Japan	X	√ / √	X	√	√	√	X	√	X
Korea	√	√ / X	X	√	√ / X	√ / X	X	X	X
Malaysia	√	X	√	√	X	X	X	X	√
New Zealand	√	√ / X	X	√	X	X	X	√	X
Philippines	√	X	√	√	X	X	X	√	√
Taiwan	√	X	√	X	X	X	X	X	X
Thailand ***	√	√ / X	X	X	√	X	X	X	X

* Cash Reserve Ratio/Statutory Liquidity Ratio

** Asset-backed securities

*** The Bank of Thailand has set up the Corporate Bond Stabilization Fund (BSF) to provide liquidity support and stabilize the corporate bond market as well as maintain overall financial stability.

Source: Newswires, ING

With negative real rates seemingly posing few problems, some governments have been emboldened to supplement their fiscal constraints with more imaginative monetary support – namely thinly-veiled direct deficit financing, or quasi-quantitative easing.

A number of economies have dabbled in this area, including South Korea, with their "Korean style" QE, and the Philippines, with some outright bond purchases in secondary markets. But perhaps most blatantly of all, Indonesia's central bank, is engaged in small-scale (currently) direct primary market financing "burden-sharing", and the independence of the Bank is also being watered down.

Read more about the depth of Asia's unconventional central bank easing

Asia Pacific – unorthodox policy by country

	Philippine central bank	Indonesia central bank	Reserve Bank of India	Bank of Korea
What has happened?	BSP unloaded a hefty monetary response with a flurry of conventional easing – 175bp of rate cuts and 200bp reduction in reserve requirements. As a result, PHP 1.9 trillion was released into the system.	BI has carried out its fair share of conventional easing, with rates slashed by 100 bp and reserve requirements reduced for both dollar and specific IDR-denominated accounts in first-quarter. But Indonesia is constrained by a vulnerable currency- the rupiah.	India's central bank action has been a mix of both conventional and unconventional measures. The RBI cut policy interest rates by a total of 115 bp and banks' cash reserve ratio by 100bp from March to May.	The Bank of Korea leapt in to help with a quick 50bp rate cut in March followed by another 25bp of easing in May. This is still where policy rates stand today, at 0.50% - still above zero, and indicating some slight additional room for further orthodox easing should it be required.
Quantitative Easing	**FULL** - The central bank has bought up government securities with no volume limits or target tenors. To date, we estimate, it has bought up roughly PHP 1.1 trillion worth of bonds & given the heft of their holdings relative to the outstanding total (20%).	**FULL** - At the onset of the pandemic, BI received provisional authority to expand its scope to purchases of long-term securities in the primary market via "perpu" or presidential declaration to assist the govt. manage the impact of Covid. Currently, BI's monetary operations have totalled roughly IDR 658 trillion, worth roughly 4.2% of GDP.	**LITE** - When hefty rate cuts failed to revive growth and CPI started to rise towards the year-end, the RBI resorted to buying long tenor govt bonds and selling short ones to drive market yields lower. Given the long-term nature of this operation (1 to 3-years), assets created remain on the RBI's balance sheet until the maturity of TLTRO. As of August, the outstanding balance on this account was INR 2.5 trillion (1.2% of GDP).	**LITE** – The Bank has been keen to enter the unorthodox club with talk of "Korean-style QE". At its 9 April meeting, it announced the adoption of an unlimited liquidity support facility. This was to use a weekly repo purchase facility to supply an "unlimited" amount of liquidity at set interest rates for a period of 3 months. The new measures were also linked to the implementation of the government's financial support package.
Deficit financing	**LITE** - The Bank's charter allows short-term cash advances to the govt, capped at PHP 810 bn. Given the cash crunch faced by authorities in October, the Bank agreed to purchase PHP 540 bn worth of 3-month paper directly from the government. As time goes by, it looks like BSP may be willing to move on to full-on deficit financing .	**FULL** - Indonesia's central bank has also recently entered into a "burden-sharing" agreement with the govt, as the Bank carries out full deficit financing. Despite subsequent pronouncements highlighting the independence of BI, investors remain wary of future burden-sharing agreements in the coming months with BI tagged as standby financier of the deficit.	**LITE** - Under Governor Das, the RBI has been generous in helping the govt to fund a wide budget deficit. The main channel here is the RBI's dividend payment and transfer of excess reserves to the government. The Bank also boosted its Ways and Means Advance limits for central and state governments. This isn't a source of deficit financing per se – just a mean to tide over short-term (usually up to 3 months) mismatch of government's receipts and spending.	
Where do we go from here?	Despite, pledging the use of unconventional policies was "time-bound" and will be phased out, authorities have secured legislation to extend and upsize the budget for cash advances, setting the precedent for more cash advances between monetary and fiscal authorities.	The Bank appears ready to resort to unconventional measures to support the govt's recovery efforts. Bank officials have repeatedly declared independence from fiscal authorities but we expect the Bank to carry out more deficit financing activities in 2021 and also use QE measures to ensure adequate liquidity in the system.	The RBI balance sheet doesn't provide sufficient grounds for thinking about outright QE or deficit monetisation. Total assets/GDP ratio of 27% is small compared to many developed market central banks pursuing full QE. We look for signs of significant balance sheet expansion to indicate policy has switched from its current lite measures to full QE or deficit financing.	Despite the Governor raising the possibility of purchasing corporate bonds or commercial paper as an expansion of this exercise, the Korean-style QE program concluded at the end of July, having supplied around KRW19tr. With market rates having stabilised, the liquidity benefits of this program are not required. Nor does the Governor seem keen to embark on mainstream QE.

Source: ING

Author

Robert Carnell
Regional Head of Research, Asia-Pacific
robert.carnell@asia.ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("**ING**") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.