Economic Outlook for Southeast Asia, China and India 2020 - NOVEMBER UPDATE

ONGOING CHALLENGES OF COVID-19

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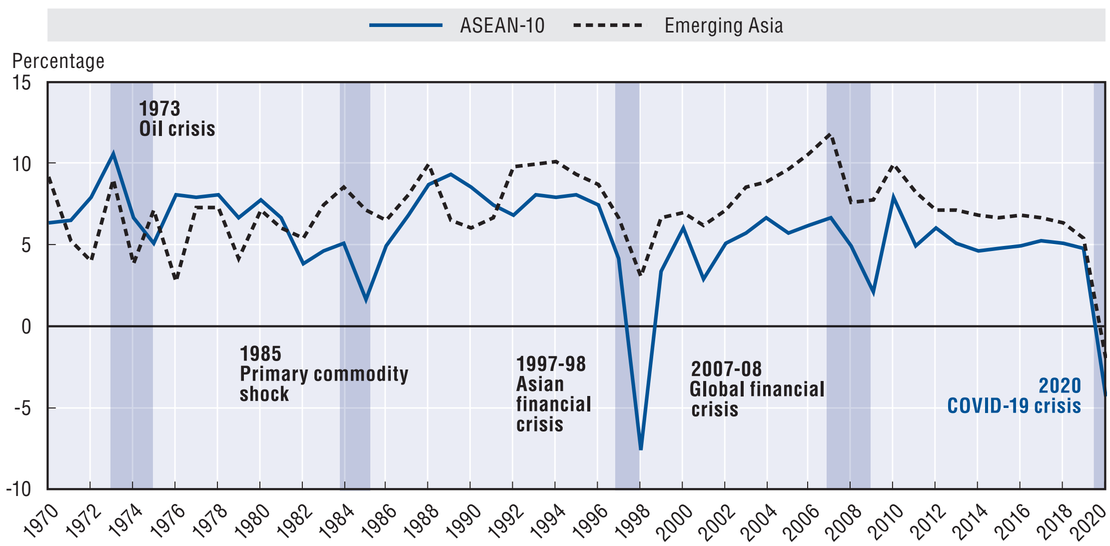
Key points

- The coming months will be a period of great uncertainty in Emerging Asia, due to continuing turmoil from the COVID-19 pandemic. Momentum in the region was particularly weak in the second quarter and growth prospects for the rest of this year are also limited by a weak investment environment and rising unemployment. GDP is forecast to decline by 4.3% in ASEAN and by 2.0% in Emerging Asia in 2020 - weaker than forecasts in late July 2020 (OECD, 2020) - while country-level divergences are widening.
- Financial markets are relatively stable, but a prolongation of the health crisis risks accentuating existing financial vulnerabilities. Asset price overvaluations and rising corporate indebtedness are downside risks. Exchange rate volatility is likely to persist amid increasing trade tensions, uncertainty surrounding the outcome of the US elections and rising COVID-19 cases in Emerging Asian countries.
- Overall, net capital flows to Emerging Asia are expected to decrease this year, with investor sentiment weighed down by concerns over a resurgence in COVID-19 cases and the downbeat global outlook for growth. Foreign direct investment (FDI) flows are anticipated to decline on both the asset and liability sides, while remittances by overseas workers will plunge in an unprecedented manner.
- Trade growth will be subdued, weighed down by weak external demand and slowing industrial activity, as well as through disruptions of global value chains (GVCs). Heightened trade tensions are an additional downside risk. The crisis has shown the need for countries to rethink their supply chain strategies, potentially by adopting innovative technologies.
- Unemployment will reach high levels in Southeast Asia, depressing real disposable incomes, which will in turn take a toll on private consumption. Although it is currently difficult to quantify the ultimate impact of the crisis on the various economic sectors, the damage is already apparent for workers in the travel and tourism industry, where job losses could be on the order of millions.
- Although the COVID-19 crisis has affected nearly all economic sectors, the travel and tourism industry will remain one of the hardest hit sectors. The impact of the pandemic on demand for travel and tourism, and the significant reduction in tourists' purchasing power, suggest that the industry's recovery will be long and slow. On the other hand, the crisis triggered by the outbreak will lead to lasting transformations, which should benefit firms that enable online and technology-based services.
- Abundant monetary support is needed to buttress the recovery. The outlook for inflation is subdued, while financing conditions have yet to return to pre-pandemic levels. At the same time, maintaining an expansionary fiscal policy seems crucial for safeguarding employment. Countries will need to meet the challenge of ensuring effective spending while at the same time achieving prudent fiscal management.
- The vulnerability of Emerging Asian economies to the effects of the pandemic will accelerate regional cooperation. ASEAN and ASEAN+3 leaders are expected to refine their strategies in several key areas, including financial integration and liberalisation, e-commerce, and digital infrastructure. The inclusion of sustainability aspects in the recovery strategy will also rank high on the regional agenda.

COVID-19 hit Southeast Asia hard in the first half of this year

Emerging Asian economies – the ASEAN-10 countries, China and India – experienced a profound recession in the first half of 2020 due to the COVID-19 pandemic. The unwinding of restrictive measures is proceeding more gradually than projected in the *OECD Economic Outlook for Southeast Asia, China and India 2020 Update: Meeting the Challenges of COVID-19* (OECD, 2020). The impact on economic activity in 2020 will therefore be greater than anticipated when the *Update* was published on 31 July. The COVID-19 crisis represents the fifth serious downturn experienced by Emerging Asian economies since 1970. For the first time since the Asian Financial Crisis of 1997-98, ASEAN economies are expected to record negative growth in 2020 (Figure 1).

Figure 1. **Real GDP growth rate of ASEAN-10 and Emerging Asia, 1970-2020**



Note: Projections for 2020 are as of 26 October 2020.

Source: OECD Development Centre and IMF (2020), *World Economic Outlook Database*.

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This *November 2020 Update* projects that the economies of the ASEAN-10 countries – Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Viet Nam – will contract by 4.3% in 2020 before growing by 5.4% in 2021. The economic output of the broader Emerging Asia region is forecast to decline by 2.0% in 2020 and rebound by 8.1% in 2021, though the base year effect needs to be taken into consideration for the 2021 growth projection. Indicators for Q2 2020 point to unprecedented GDP decreases, with double-digit declines in Malaysia (-17.1%), the Philippines (-16.3%), Singapore (-13.2%) and Thailand (-12.1%). The contraction in 2020 is therefore anticipated to be more significant than the 2.8% projected for ASEAN-10 and the 2.9% for Emerging Asia when the *Update* was released in July.

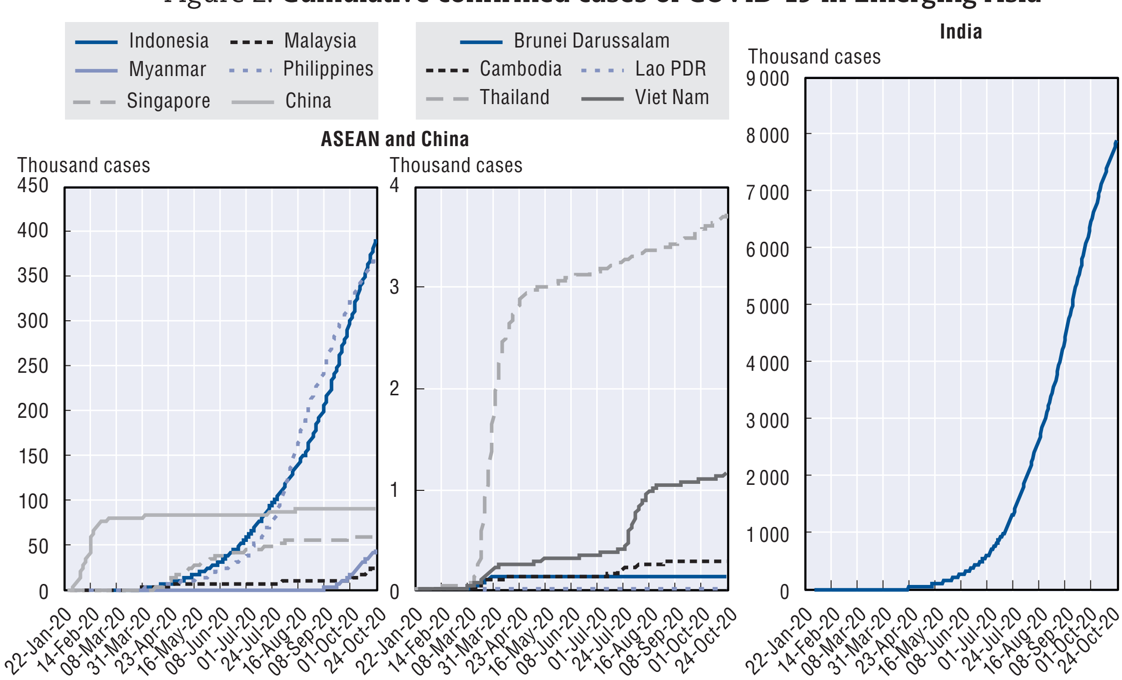
Table 1. **Real GDP growth in ASEAN, China and India, 2020-21**

Percentage

	2020	Changes from the previous forecast (July 2020)	2021
ASEAN-5 countries			
Indonesia	-3.3	↓	5.3
Malaysia	-6.9	↓	6.0
Philippines	-8.4	↓	6.2
Thailand	-8.2	↓	4.2
Viet Nam	1.5	↓	6.2
Brunei Darussalam and Singapore			
Brunei Darussalam	1.4	-	3.3
Singapore	-5.5	↓	5.0
CLM countries			
Cambodia	-3.4	↓	5.4
Lao PDR	1.0	-	5.0
Myanmar	1.7	↓	6.6
China and India			
China	1.8	↑	8.0
India	-10.2	↓	10.7
Average of ASEAN-10	-4.3	↓	5.4
Average of Emerging Asia	-2.0	↑	8.1

Note: Data are as of 26 October 2020. Data for India and Myanmar relate to fiscal years. The projections for China, India and Indonesia are based on the OECD Economic Outlook, Interim Report September 2020.
Source: OECD Development Centre.

Figure 2. **Cumulative confirmed cases of COVID-19 in Emerging Asia**



Note: Data as of 26 October 2020.
Source: Johns Hopkins University.
StatLink https://doi.org/10.1787/888934192965

Looking forward, there are some signs of recovery for the second half of the year, although new cases of COVID-19 continue to appear in some Emerging Asian countries (Figure 2) and households' purchasing power has slackened amid rising unemployment. A potential re-escalation of trade tensions between the United States and China is an ongoing concern in the region. Other downside risks to the outlook include a surge in non-performing loans (NPLs) and a possible sharp correction of asset prices that could lead to large outflows. On the upside, the early availability of a COVID-19 treatment or vaccine could put the global economy back on track sooner than anticipated.

Country-level divergences are widening in Emerging Asia

The shock to Emerging Asia has affected all countries, but the evolution of output in 2020 and 2021 is set to differ markedly. The strength of each country's economic recovery will depend not only on the evolution of the epidemiological situation, but also on structural factors and the capacity to respond with stabilising policies.

ASEAN-5

- The situation on the epidemiological front remains bleak in **Indonesia,** with over 350 000 COVID-19 cases confirmed in the country since the onset of the pandemic. Large-scale physical distancing measures, similar to the ones applied in April, were reinstated in the capital, Jakarta, during the September-October period. Continuing disruption from COVID-19 will have a lasting impact on consumption and investment. Growth forecasts for 2020 are therefore revised downwards, with real GDP expected to shrink by 3.3%. As the global economy recovers in 2021 and public infrastructure projects resume, real GDP is expected to rise by 5.3%.
- **Malaysia** has seen a resurgence of confirmed cases of COVID-19 since mid-September. The country's Recovery Movement Control Order, which lifted most restrictions but kept several sectors closed, will remain in place until the end of the year. With the exception of government expenditure, all components of GDP will have a negative contribution to growth in 2020. Exports will be particularly impacted, partly due to Malaysia's high reliance on China. Domestic political uncertainty represents an additional major drag on the growth outlook. The Malaysian economy is expected to contract by 6.9% this year, the worst performance since the Asian Financial Crisis of 1997-98, and return to growth in 2021 (+6.0%), assuming a gradual normalisation of global trade and tourism flows.
- The **Philippines** entered a recession in Q2 2020 with a 16.5% year-on-year contraction in GDP. This decline followed a 0.7% drop in the first quarter. Differentiated measures to contain the pandemic will be in effect across the country through at least October, as the Philippines' COVID-19 case tally exceeded 350 000 as of mid-October. These restrictions add to the ongoing pressure on private consumption and investment spending. Rising debt costs put additional strain on the government's ability to service debt on existing infrastructure projects and could jeopardise investment into future projects. Real GDP growth is expected to move deep into negative territory in 2020, posting a decline of 8.4%. Assuming the economy starts to recover towards the end of the year, in part supported by the government's pledge to accelerate public infrastructure investment, real GDP will return to a growth rate of 6.2% in 2021.
- **Thailand**'s COVID-19 situation has remained remarkably stable since the publication of the *Update*, with fewer than 200 new cases reported from August through October. Nonetheless, the government extended the state of emergency through October. Prior to the extension, the country was to start accepting foreign tourists as of

October, albeit under a rigid arrangement. The significant loss of tourism revenue, combined with subdued consumption and private investment, as well as pre-existing vulnerabilities following the 2019 drought, will drive a steep decline of 8.2% in the country's real GDP in 2020. Political tensions constitute an additional risk to the outlook, although local markets have been relatively unscathed so far. Recovery in the months ahead will be held back by a shrinking tourism sector, which has reportedly seen its revenues plummet by 70% this year. The government's scaled-up investment in infrastructure will be the main driver of the rebound in 2021.

- **Viet Nam** continues to post impressive results in the fight against the pandemic. Despite the emergence of local clusters, the daily number of new cases has dropped significantly between August and October. On the downside, a US investigation into Viet Nam's trade practices risks threatening the country's vibrant export performance. Although real GDP growth will remain below its trend rate in 2020 (+1.5%), owing to lower domestic and external demand, Viet Nam's economy is showing stronger resilience than most others in the region. The forecast for 2021 projects an output growth rate of 6.2%, with Viet Nam well positioned to benefit from a potential reorganisation of global supply chains in the wake of the COVID-19 crisis.

Brunei Darussalam and Singapore

- **Brunei Darussalam**'s emergency response has been remarkable as assessed against several parameters, including a slowing pace of newly confirmed COVID-19 cases and a comparatively low case fatality rate. The economic growth forecast for 2020 has held steady at 1.4%, supported by a stronger than anticipated increase in global oil prices. Growth in 2021 is expected to reach 3.3%, driven by sustained domestic consumption and increased investment activity for the second phase of a major petrochemical refinery.
- **Singapore** seems to have brought the pandemic under control, with a decline in the number of newly confirmed cases of COVID-19 over the past several weeks. However, the COVID-19 crisis has dealt a major blow to Singapore's economy, though third quarter GDP growth improved. Singapore's GDP is expected to decline by 5.5% in 2020, before returning to its pre-shock growth rate in 2021 (+5.0%).

Cambodia, Lao PDR and Myanmar

- While **Cambodia** has so far managed to avoid a health crisis, the country has been severely impacted by the economic crisis. The economic repercussions of the pandemic have spread via three main channels: tourism, exports (in particular garments, travel goods and footwear) and FDI. Private consumption growth will be weak, with job losses caused by lockdown restrictions unlikely to be recouped immediately. One of the pillars of the Cambodian economy, tourism has been severely damaged by travel restrictions, with the number of visitor arrivals down by nearly 72% in the first eight months of 2020, compared with the same period one year ago. While borders have been officially reopened, international arrivals are still controlled by very strict rules. Output is projected to fall by 3.7% in 2020, while the government's comprehensive support package is expected to lift the 2021 growth rate to 5.4%.
- **Lao PDR** remains one of the countries in Southeast Asia where the pandemic has caused the least damage on the health front. Major infrastructure projects are expected to contribute substantially to economic growth over the near term. On the downside, public debt is rising and the country's highly dollarised banking system is particularly vulnerable in the event of a financial crisis. Rising unemployment

and falling disposable income will continue to hinder aggregate consumption growth. GDP growth is anticipated to slow to 1.0% in 2020, as in the previous forecast, and initiate a recovery of 5.0% in 2021, subject to post-pandemic global economic performance.

- **Myanmar** is feeling the economic consequences of the COVID-19 crisis, and the number of confirmed cases of COVID-19 has spiked in recent weeks, leading to approximately 33 000 cumulative confirmed cases as of mid-October. The country is expected to post modest economic growth of 1.7% in fiscal year (FY) 2020 and 6.6% in FY 2021. Downside risks to the outlook persist in view of ongoing weakness in domestic consumption and gross fixed investment and the looming general elections. Myanmar's reliance on imports, due to a loss of local manufacturing capacity during the health crisis, will also slow the pace of economic expansion in 2021 and beyond.

China and India

- In **China**, economic recovery from the COVID-19 crisis is gaining momentum. Industrial production and construction activity staged a solid rebound in the second quarter and stabilised in Q3. Nevertheless, household consumption will likely remain sluggish due to the fall in urban household disposable income and persistent economic uncertainty. In 2020, output is anticipated to expand by 1.8%, with infrastructure investment and net exports expected to provide a fairly positive contribution to growth. Economic growth should further accelerate to about 8.0% in 2021, on a low base and assuming consumption recovers somewhat.
- **India** has seen the number of confirmed cases of COVID-19 increase at an alarming rate, exceeding the 7.3 million mark as of mid-October. Indian authorities have varied the stringency of restrictions based on regional COVID-19 case tallies. Real GDP is expected to shrink by 10.2% in FY 2020-21, the steepest yearly decline on record. This stems primarily from a 23.9% year-on-year contraction in the first quarter of FY 2020-21 (April to June), reflecting the impact of restrictions on consumption and private investment. The growth forecast for FY 2021-22 (+10.7%) is overshadowed by risks to the banking sector, emanating from a marked deterioration in the creditworthiness of households and firms that could result in rising NPL ratios.

The risks facing the region are remarkably high and mainly tilted to the downside as the scale and duration of the pandemic remain unknown. A prolonged pandemic could lead to extended lockdowns and other restrictive measures. Such restrictions would harm business and consumer confidence, disrupting both supply and demand. Indeed, retail sales have dropped sharply in Malaysia (-32.4%) and Indonesia (-16.8%) in April 2020, following the implementation of restrictions. ASEAN countries are not currently under a full-scale lockdown like the one experienced during spring, but localised lockdowns with varying degrees of stringency are in place (Table 2). For instance, Indonesia, Malaysia, Myanmar and India have had to impose tighter restrictions in some areas as the number of infected individuals rises. The outcome of the US presidential elections will also have an impact on Southeast Asian economies, adding an extra layer of uncertainty to the regional outlook.

Table 2. **Examples of lockdown measures in Emerging Asia**

Country	Date of first announcement	Coverage	Most recent announcement	Coverage
Indonesia	30 March	State of emergency announced in the area of Jakarta	25 October	The transitional large-scale social restrictions in the Jakarta region are extended.
Malaysia	16 March	Nationwide lockdown	14 October	Strict restrictions reimposed in Kuala Lumpur, Putrajaya and Selangor state. Businesses allowed to resume in Sabah state.
Myanmar	18 April	Lockdown in multiple regions	25 October	Stay home order in effect for all of Rakhine State, Yangon Region (excluding Cocogyun Township), and select townships in each of Mon State, Ayeyawady Region, Bago Region and Kachin State.
Philippines	12 March	Lockdown announced in Metro Manila area	19 October	Curfew hours in Metro Manila shortened from 10pm-5am previously to 12am-4am, except in Navotas City.
India	24 March	Nationwide lockdown	30 September	Strict lockdowns to remain in containment areas until 31 October. Non-containment areas are gradually reopened.

Source: Oxford University (2020), *Coronavirus Government Response Tracker* database (as of 26 October), and national sources.

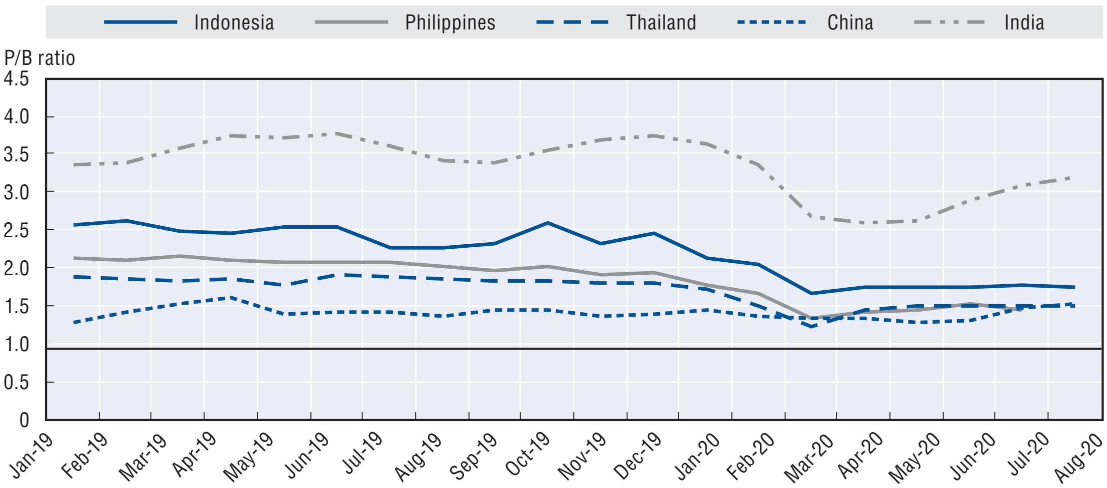
The labour market could suffer greater long-term damage than expected, and liquidity problems could turn into solvency difficulties for many firms. Lower corporate earnings and higher unemployment would have a negative impact on the capacity of firms and households to service their debts. The COVID-19 crisis could therefore cause a re-emergence in non-performing loans. High levels of NPLs depress the supply of credit to the real economy and delay economic recovery. However, a recovery that is swifter than anticipated cannot be ruled out if the situation on the epidemiological front allows faster unwinding of the remaining restrictions. The early availability of a vaccine or effective treatment against COVID-19 would also get the global economy back on track.

A prolongation of the COVID-19 crisis might risk accentuating financial vulnerabilities

The COVID-19 crisis has tested the soundness of the financial sector across Emerging Asia. It has held up well so far, but this is largely due to the massive supportive interventions by public authorities. Markets have been very volatile, but overall they have endorsed these measures and the trend is likely to reverse only if policy support for the recovery is withdrawn soon. The financial sector manifested its strength with proper functioning of contingency plans and the absence of any adverse events with systemic impact. Nevertheless, the COVID-19 crisis is accentuating the financial imbalances already present prior to the shock. The risk of elevated price volatility and high indebtedness remain the primary vulnerabilities.

Massive and immediate policy reaction in response to the pandemic allowed stock market valuations and financial market activity to stabilise, and then rebound, although the situation has varied depending on the sector and market segment. However, this stabilisation remains fragile as stock market valuations seem to be high with regard to fundamentals, signalling a potential disconnect between the real and financial spheres of the economy (Figure 3).

Figure 3. **Price-to-book value (P/B) ratio of benchmark stock market indices in selected Emerging Asian economies, January 2019 to August 2020**



Note: P/B ratios of the following stock market indices: Shanghai Stock Exchange Composite Index (China), Nifty 50 Index (India), Jakarta Stock Exchange Composite Index (Indonesia), the Philippine Stock Exchange PSEi Index (the Philippines) and the SET Index (Thailand). Unweighted average of constituent shares' P/B ratios. A P/B ratio lower than 1 could indicate that the stocks composing the index are undervalued, while a price-to-book ratio above 1 could indicate stock overvaluation.

Source: CEIC and national sources.

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One consequence of the economic crisis has been increases of corporate and public debt levels (Figure 4). In the notable case of Thailand, corporate debt has grown faster than public debt since the onset of the health crisis. The risk of insolvency constitutes a major vulnerability, particularly in those countries where indebtedness was already high before the start of the crisis. In addition to the social impact, this would have severe consequences for governments, especially those with strained public finances and limited fiscal space.

Figure 4. **Corporate and public debt in selected Emerging Asian economies**

Change in corporate debt to GDP and government debt to GDP, Q4 2019-Q1 2020

Source: Bank for International Settlements and Thomson Reuters Refinitiv.

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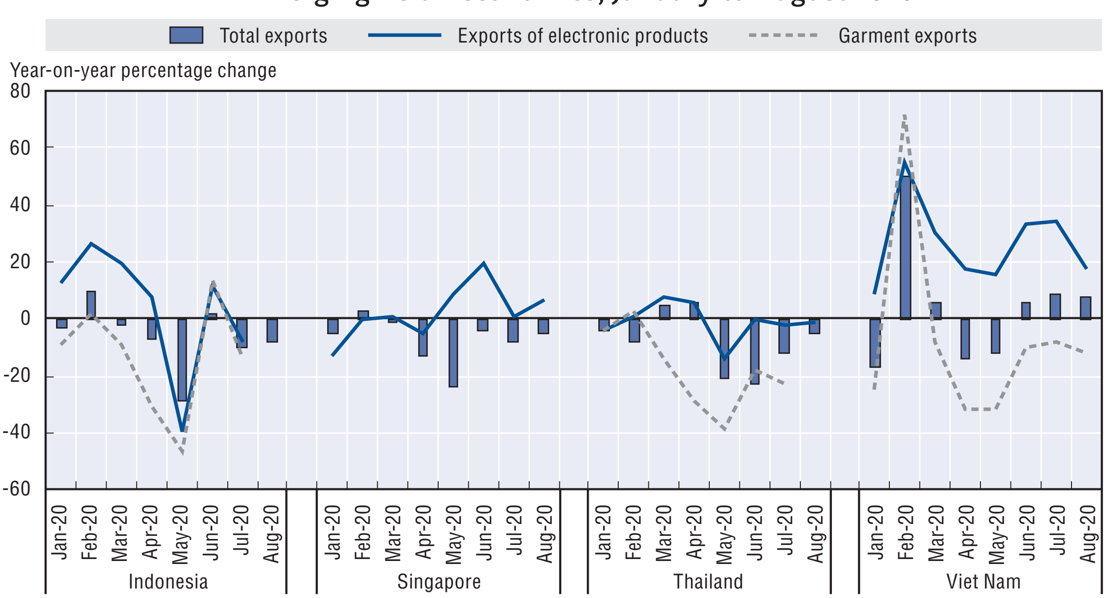
The weakening of non-financial agents also contributes to increasing the risk of contagion from the real sphere to the banking sphere. This could in turn jeopardise banks' ability to sustain the economic recovery. An increase in the NPL ratio would hamper banks' ability to continue to support the corporate sector, thereby deepening the recession.

Trade will continue to suffer due to weak external demand and supply chain disruptions

Global trade is still deeply affected by the COVID-19 pandemic. Many Emerging Asian economies are highly reliant on global supply chains and are therefore very exposed to global macroeconomic developments. Export growth in the region is expected to remain weak until the end of 2020 but gradually strengthen in 2021. In addition to the impact of the pandemic on tourism and transportation, trade is also expected to suffer from supply chain disruptions and a potential re-escalation of trade tensions between the United States and China, which would particularly affect electronics supply chains. A recovery in trade is anticipated for 2021 and the expansion of exports will accelerate in line with external demand.

Sectoral recovery remains asymmetric. The textile and clothing sector, where Emerging Asian countries are leading global exporters, has been subdued in recent months (Figure 5). In addition, increased unemployment in some of the largest importers of Asian garments will affect the purchasing behaviour of consumers, hurting Southeast Asian garment exports. Many factories in Cambodia, Myanmar and Viet Nam temporarily closed in the first half of the year owing to the cancellation or reduction in orders from distributors and retailers in the European Union and the United States.

Figure 5. **Exports (total, electronic products and garments) in selected Emerging Asian economies, January to August 2020**



Source: CEIC and national sources.
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The electronics industry, deemed essential to the functioning of the economy during lockdown, has weathered the crisis relatively well. According to the latest *Goods and Trade Barometer* of the World Trade Organisation (WTO), trade in electronic components posted a notable rebound in Q2 2020. A similar pattern can be observed in several Southeast Asian economies (Figure 5). The rebound in the electronic machinery sector in the major trading partners of Emerging Asian countries could generate growth in demand for intermediate products from Asian manufacturers. However, the recent re-escalation of US-China trade tensions could take a toll on the region through declining Chinese demand for imported intermediate goods.

Linkages through GVCs could magnify the decline in global trade. In a context of widespread uncertainty, the crisis has particularly highlighted the fragility of Southeast Asian economies vis-à-vis China in terms of supply chains. The impact of GVC spillovers on activity will depend on how individual countries are positioned in the GVCs. For instance, in countries situated downstream in global value chains, such as Viet Nam, the decline in imports could exceed that of exports, thereby fostering domestic activity. This reflects the fact that production in Viet Nam is highly reliant on imported inputs, which are subsequently re-exported in the form of finished goods. Conversely, in countries situated upstream in value chains, such as Singapore, exports are likely to fall more than imports, translating into an overall negative impact on activity.

The COVID-19 crisis highlights the need for countries to rethink, reorganise and strategically transform their supply chains. This revamped supply-chain strategy must account for new health and safety hazards that go well beyond traditional perils such as market volatility or disruptions in logistics supply. The change in strategy is essential in terms of managing both the demand and supply sides. Rapidly changing environments – a trend already visible prior to the COVID-19 crisis – require businesses to react promptly to sudden and more frequent changes in demand. In addition to customers, suppliers and distributors also significantly increase supply-chain risks. As such, an effective supply-chain strategy must be able to monitor and predict risk accurately in order for businesses to react in a proper way.

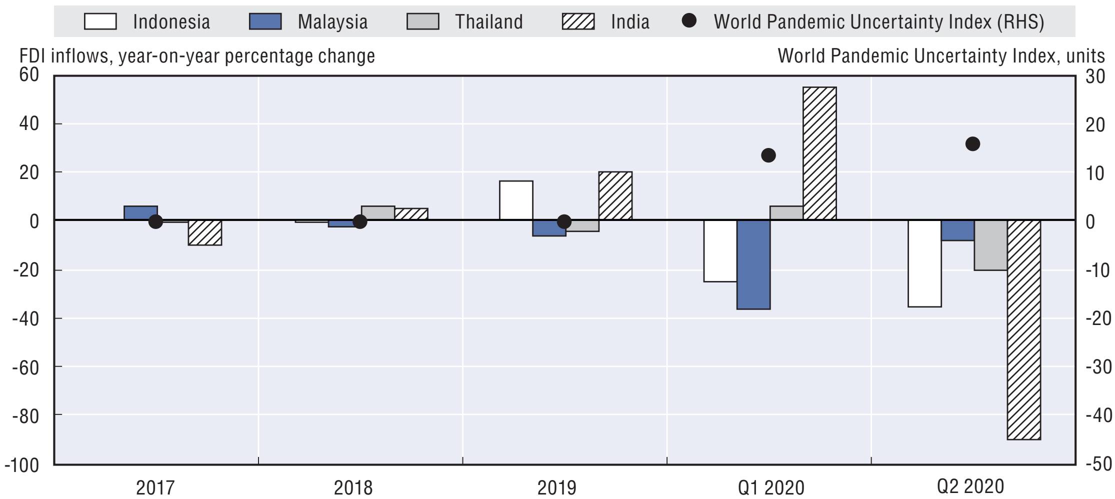
A potential avenue for implementing a novel supply-chain strategy consists in relying on digital management technologies such as blockchain (OECD, 2019a) or artificial intelligence (AI). The crisis has underscored the importance of securing trade. Blockchain technology, which allows the decentralised storage and transmission of information, could provide an appropriate response to this problem through better transparency, traceability and visibility of transactions throughout the supply chain. Recently adopted in the food industry by major retailers, blockchain technology thus enables reliable and secure information exchange, and considerably reduces risks.

Artificial intelligence could also provide a response to this new paradigm by improving the reactivity and efficiency of supply chains. Indeed, AI tools could be deployed to support the real-time management and monitoring of production, inventories, logistics and distribution, as well as maintenance, all of which are essential during a health crisis.

Uncertainty surrounding the pandemic will depress capital flows

Net capital flows to Emerging Asian economies are expected to decrease this year. The robust growth trend of FDI, one of the most stable sources of foreign capital in Southeast Asia, is anticipated to be reversed in 2020 due to the uncertainty surrounding COVID-19 (Figure 6) and the accompanying supply-chain disruptions and economic slowdown. Prior to the onset of the pandemic, Southeast Asian countries attracted a record level of investment flows, amounting to USD 156 billion in 2019, the equivalent of approximately 1% of ASEAN GDP. FDI inflows to developing Asia[1] are expected to contract by 25-40% in 2020 (UNCTAD, 2020). At the same time, the growing liquidity challenges faced by firms in the region will precipitate a fall in outward FDI. In addition, the withdrawal of foreign investors risks impairing banks' ability to obtain funding on markets, particularly in countries with vulnerable banking sectors.

Figure 6. **FDI inflows in selected Emerging Asian economies and the World Pandemic Uncertainty Index, 2017 to Q2 2020**



Note: The World Pandemic Uncertainty Index (WPUI) is a sub-index of the broader IMF World Uncertainty Index. The WPUI captures the incidence of the word "uncertainty" (and its variants) in relation to pandemics in various reports. A higher value of the index means higher uncertainty and the opposite. RHS means right-hand scale.

Source: OECD Development Centre based on data from CEIC and the IMF *World Pandemic Uncertainty Index* (WPUI).

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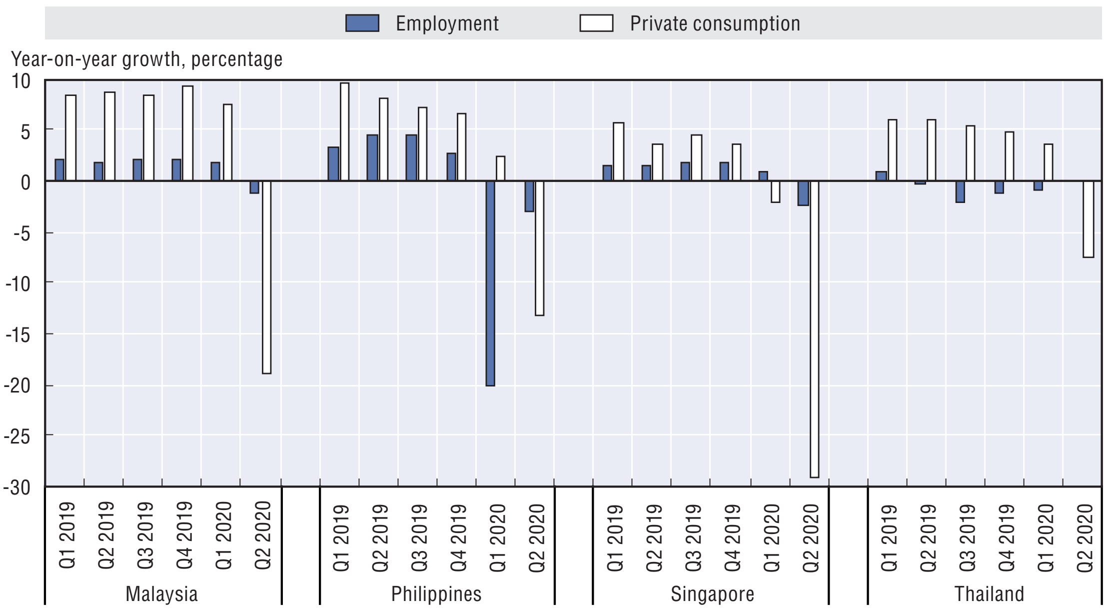
Several factors give good reason to anticipate a resumption of capital flows to Emerging Asia in the medium to long term. The first is the value placed by major world economies on the diversification of production chains, related to some extent to recent trade tensions, while overseas investors' continued interest in the digital economy is another. Indeed, the digital economy was already a major FDI recipient before the pandemic, and the trend is likely to strengthen due to increased reliance on digital tools.

Households delay consumption amid subdued employment prospects

The pandemic is expected to have a considerable impact on the labour market in the second half of 2020, although there is a time lag of up to two quarters to observe the consequences of the economic crisis. In addition to rising unemployment, global underemployment has increased substantially as businesses observe strict sanitary rules and strive to reduce operating costs. The rise in unemployment and underemployment will lead to significant income loss for many workers, with informal labourers particularly affected. The damage on sectoral employment is already apparent for workers in the travel and tourism industry.

Growth of private consumption was subdued in the second quarter of this year. The pattern of consumption largely mirrors developments in employment (Figure 7), and is also impacted by restrictions placed on non-essential businesses, which will likely result in the contraction of discretionary spending. Real income is expected to be negatively affected by the fall in employment, but to be supported by low inflation as well as by the fiscal packages implemented in most Southeast Asian countries, which increase transfers and reduce taxes. The anticipated modest growth in consumption also reflects an increase in precautionary savings in view of high economic uncertainty, rising unemployment and declines in financial asset prices.

Figure 7. **Change in employment and private consumption in selected Emerging Asian economies, Q1 2019 to Q2 2020**



Note: Data refer to the number of people employed aged 15 and over.

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

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Remittances from overseas workers are an important source of funds for households in several countries in the region. A real safety net for dependent families, remittances by Southeast Asian migrants to their countries of origin are expected to drop by as much as 19.8% in 2020 (ADB, 2020). The fall is unprecedented and reflects the fact that many migrants reside in countries particularly affected by the pandemic and where strict measures have been taken to close down non-essential businesses, for instance the United States, EU and Middle Eastern countries. In comparison, remittances to the Asia-Pacific region declined by only 2.7% during the 2007-08 global financial crisis (ADB, 2020).

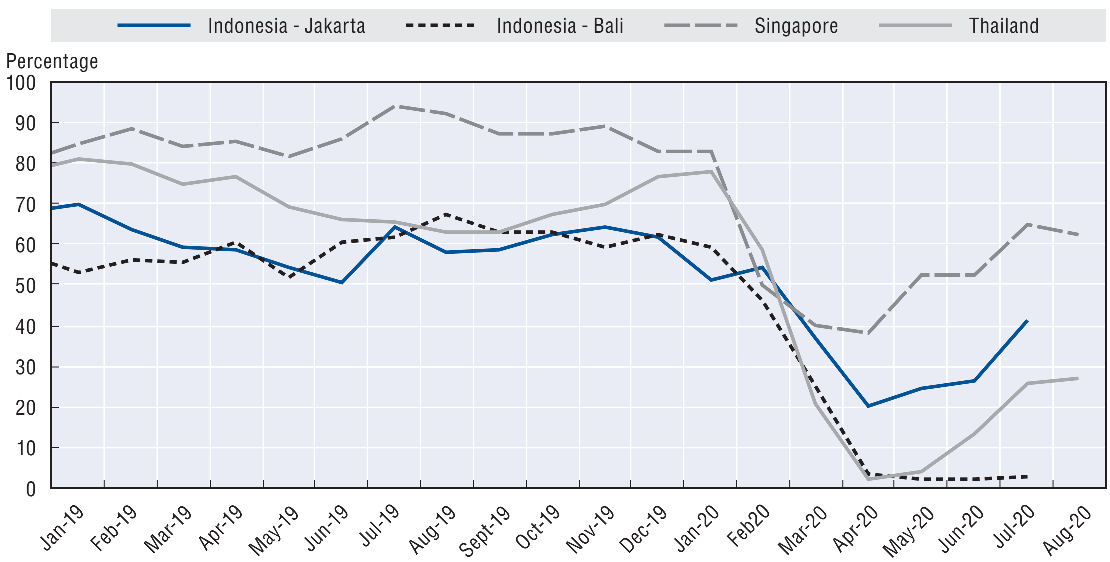
Looking forward, the evolution of unemployment rates is expected to differ substantially across Emerging Asian economies. Countries with a high share of temporary workers are expected to witness larger repercussions on unemployment rates and income. An additional risk is that some persons may move out of the labour force, discouraged by the decline in hiring opportunities due to lockdowns and other restrictive measures. Furthermore, ongoing social unrest in some ASEAN countries risks undermining the effectiveness of government policies.

Travel and tourism face a bumpy path to recovery

The tourism industry has become one of the sectors most affected by the crisis. This has major repercussions on regional economies, as the sector represents 6% of GDP, on average, across ASEAN countries. Following the unprecedented blow of initial measures to combat the pandemic, and the reinstatement of restrictions more recently to curb a resurgence of confirmed cases of COVID-19, the path to recovery in travel and tourism is likely to be very slow in Southeast Asia. Travel activity in ASEAN countries will be slower to recover than elsewhere, since these countries rely on overseas travel to a greater extent.

However, there are incipient signs of recovery across the region. Hotel occupancy in Thailand reached 27% on average in August after bottoming out at around 3% in April and May, while the situation has also improved in Singapore and Jakarta (Figure 8). These figures need to be qualified, however, as they may also capture stranded tourists or quarantined guests. The economy and mid-tier segments are likely to drive the recovery, owing to the fall in tourists' purchasing power and preference for proximity and lower-cost travel. The Meetings, Incentives, Conferencing, Exhibitions (MICE) sub-segment is expected to remain dampened for a long time due to lingering concerns about gatherings and the potential restoration of strict physical-distancing rules.

Figure 8. **Average hotel occupancy rates in selected Emerging Asian economies, January 2019 to August 2020**



Source: CEIC and national sources.

StatLink https://doi.org/10.1787/888934193079

All modes of transport will continue to face headwinds, with air transport most affected. Many airlines have reduced their activity to a minimum, while others have ceased operations altogether. The longer the health crisis lasts, the less the sector's survival can be guaranteed without government aid. The establishment of travel agreements between "safe" countries should nevertheless enable a modest resumption of services in the near term. Cruise operators, meanwhile, face a very high degree of uncertainty as to when operations can resume and which ports will be available to them. Even when operations resume, demand for cruises is likely to remain muted against the backdrop of consumer concerns around the pandemic and weaker real disposable incomes.

The gradual reopening of the sector is a fine balancing act that requires in-depth analysis of the activities that are ready to restart, as well as careful monitoring of the health situation. The most likely model will focus on domestic tourism, with short trips over short distances. The travel and tourism industry will need to adapt to increase profit margins in order to guarantee the necessary funds to face any future health crises. The use of digital tools, such as artificial intelligence software, will be vital for understanding consumer requirements and better adapting to them. At the same time, it is fundamental to invest in upgrading services in order to ensure an adequate and safe environment for lodging and transportation.

Macroeconomic support policies will continue to underpin the recovery

The pursuit of a sustained recovery in the near term remains highly dependent on the evolution of the pandemic and the success of containment policies. While the uncertainty surrounding the evolution of the situation on the health front is likely to weigh on the labour market, as well as on the recovery in consumption and investment, Southeast Asian economies must be supported by favourable financing conditions and an expansionary fiscal stance.

Ample monetary stimulus is necessary for a sustained recovery

High uncertainty about the economic outlook continues to weigh on private consumption and business investment. Headline inflation is being held back by low price pressures amid sluggish demand and significant underuse of capacity in the labour market. The overall outlook for inflation remains subdued, although there have been changes to the underlying factors influencing prices. While food and oil prices have increased more than anticipated, the combined effect is expected to be offset by the slowdown in demand and the weaker economic outlook. In this context, ample monetary stimulus remains essential to support the economic recovery in the medium term.

Despite the maintenance of an accommodative monetary stance, financial conditions in Southeast Asia have yet to return to pre-pandemic levels. Long-term sovereign bond yield spreads tightened starting from May, driven by a combination of monetary and fiscal support measures, but they remain above the levels recorded prior to the onset of the health crisis. At the same time, spreads between the rates on interbank loans and equivalent-maturity government bonds remain relatively wide. The price of risky assets edged up, mainly due to a generally more positive outlook for short-term earnings, but deteriorating sentiment could reignite volatility. In foreign exchange markets, domestic currencies have posted mixed performances in trade-weighted terms and against the US dollar.

Expansionary fiscal policy is crucial for preserving employment and purchasing power

The COVID-19 pandemic continues to have a strong impact on public finances in Emerging Asia. The fiscal cost of stimulus measures has been substantial for all Southeast Asian countries, although the fiscal burden and response capacity vary from country to country. Due to the economic downturn and substantial budgetary support, general government budget deficits in ASEAN are expected to widen significantly in 2020. The deficit ratio is forecast to improve in 2021, assuming a gradual elimination of emergency measures and a more favourable economic situation. Southeast Asian countries will need to continue supporting their economies to recover, while at the same time achieving prudent medium-term fiscal positions and ensuring debt sustainability.

One of the biggest challenges is finding the necessary resources to ensure that households and businesses can stay afloat until the crisis is over. Government room to manoeuvre has narrowed, especially for countries where debt sustainability raises concerns, although debt-to-GDP levels are lower in Emerging Asian economies than in most of their OECD counterparts. Countries in the region could consider broader fiscal policy options to cope with the current crisis, including co-ordination between monetary and fiscal policy – for instance, a sort of debt monetisation, or market-based tools such as a coronabond – and region-wide co-operation. However, unconventional policies should be carefully assessed prior to implementation.

Digital transformation presents new opportunities for the corporate sector

Digital transformation is permanently changing the way Southeast Asian firms operate by promoting connectivity and the use of digital tools. The development of digital tools and online platforms could lower economic costs and improve productivity, offering new growth opportunities and access to new markets. The Internet and digital technologies enable firms of all sizes to go into new markets and expand their reach, allowing them to grow, scale and benefit from knowledge spillovers as they participate more easily in GVCs (OECD, 2019b). By facilitating access for consumers, digitalisation could enable companies to participate in the global economy regardless of their size.

Digital transformation could represent a key element in the growth of firms in the region (Box 1). SMEs form the backbone of ASEAN economies on many fronts, including output, employment, exports and economic development at large. To reap the full benefits of the digital transformation, SMEs must align their strategy with this objective, whether in terms of approaching consumers, designing products and services, or processes.

Box 1. **Digital transformation creates new opportunities for Southeast Asian SMEs**

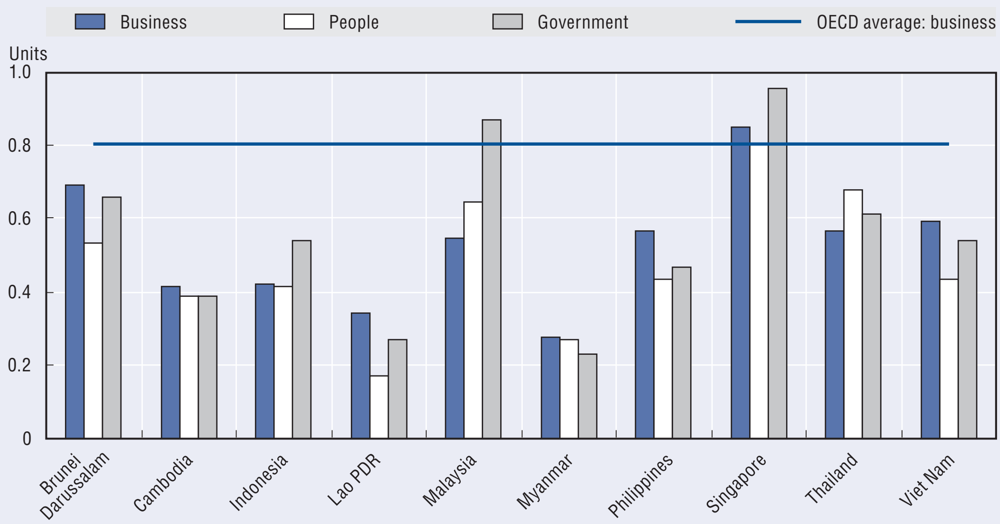
Digitalisation fosters the growth of SMEs in various ways. First, digitalisation enables SMEs to increase their turnover and base of customers or vendors. By promoting the participation of companies in the global economy regardless of their size, digitalisation allows SMEs to compete with larger firms. As digital transformation has accelerated, the e-commerce landscape has become ever more dynamic. E-commerce developed principally as a means to facilitate repeated transactions between large firms, and it relied on custom networks for the electronic exchange of data. With the expansion of open networks such as the Internet, e-commerce is now spreading to smaller firms and it is increasingly used for transactions between firms and consumers (OECD, 2019b). Virtual marketplaces allow companies to enter new markets through virtual shops, providing them access to global consumer bases and established distribution infrastructures. E-commerce represents an opportunity for Southeast Asian economies to tap into a growing global market.

Second, digitalisation offers opportunities for the development of new business models and removes many of the obstacles to the creation or growth of new businesses. The digital transformation is also promoting the rise of alternative funding sources, including crowdfunding, which provides start-ups with the capital they need in order to grow. Crowdfunding generated USD 6.12 billion for companies in the Asia-Pacific region in 2018 (P2PMarketData, 2020).

However, for technology diffusion to lead to productivity gains, firms must integrate the technology into their business processes and make complementary investments in skills and business models (OECD, 2019c). While a growing number of Southeast Asian firms are striving to master the use of digital tools and platforms, most ASEAN countries still lag behind the OECD in terms of digital adoption (Figure 9). ASEAN SMEs could achieve fast and sustainable growth by tapping into new markets. In some countries, most notably Malaysia and Thailand, the degree of digital-tool adoption is higher for individuals than for businesses (Figure 9), suggesting that firms in these countries could capture a greater share of domestic online demand by strengthening their digital footprint.

Box 1. **Digital transformation creates new opportunities for Southeast Asian SMEs** *(cont.)*

Figure 9. **Digital Adoption Index by type of agent in ASEAN economies, 2016**



Note: The *Digital Adoption Index* is defined for each type of agent on a scale from 0 (minimum) to 1 (maximum).
Source: OECD Development Centre based on data from the World Bank *Digital Adoption Index*.
StatLink https://doi.org/10.1787/888934193098

Various obstacles could hinder the adoption of new technologies by SMEs. The lack of digital skills is a major bottleneck in Southeast Asian countries (OECD, 2019d) and a large number of SMEs may not be aware of the variety of digital tools available or the potential benefits of adopting them. Some companies, especially the smaller ones, could be hesitant about adopting digital solutions due to a distorted perception of the associated costs and complexity.

Policymakers have the opportunity to initiate collaborative work with SMEs to address some of these shortcomings. New legislative and non-legislative measures could offer significant opportunities to SMEs and foster their growth. Across ASEAN, local authorities have adopted numerous initiatives to increase SMEs' awareness of the opportunities offered by digital technology and to develop environments that foster digital entrepreneurship while strengthening innovation. This trend has been accelerated by the pandemic (Table 4). The adoption of such policies could unleash many benefits for SME managers and employees in an environment marked by growing uncertainties. This would have a significant impact on the national and regional economy, given the importance of SMEs for employment and the competitiveness of Southeast Asian economies.

Box 1. **Digital transformation creates new opportunities for Southeast Asian SMEs** *(cont.)*

Table 3. **Government initiatives to spur digital transformation in response to the pandemic**

Country	Initiative	Overview
Brunei Darussalam	eKadaiBrunei	Launched in April 2020, eKadaiBrunei is an online e-commerce directory that lists online grocery stores, department stores, delivery systems, payment platforms, etc.
Indonesia	Partnerships with various technology companies	The government announced in June 2020 that it would join forces with the e-commerce platform Lazada Indonesia to help SMEs with digital marketing and with establishing stores on the platform. The government is also pursuing a project with the online ride-hailing company Grab Indonesia to develop an application for business management.
Malaysia	Initiatives to promote digitalisation and automation	The government announced it would allocate grants to local entrepreneurs to promote the sale of their products on e-commerce platforms. Subsidies will be provided for short courses in digital skills. The government also plans to promote higher-value-added private-sector investments through an SME Automation and Digitalisation Facility.
Philippines	MinDATienda Portal	The portal was opened in June 2020 to facilitate the marketing and trading of fishermen's and farmers' products.
Singapore	Grow Digital	Announced in June 2020, Grow Digital is an initiative under which SMEs can participate in Business-to-Business (B2B) and Business-to-Consumer (B2C) e-commerce platforms to sell overseas without a need to establish physical stores.

Source: OECD Development Centre based on national sources, as of 26 October.

COVID-19 crisis provides the impetus for renewed and more targeted action at regional level

ASEAN leaders have stressed the importance of a proactive approach to tackling the health crisis, including through the ASEAN Comprehensive Recovery Framework. They also reaffirmed ASEAN's determination to prevent, detect, control and address the serious and multifaceted challenges posed by the COVID-19 pandemic. Regional leaders called for the development of an ASEAN COVID-19 Response Fund, with the perspective that a comprehensive recovery framework and the implementation plan for this programme would be submitted to the ASEAN Summit later this year.

Faced with the unprecedented economic impact of the health crisis, ASEAN leaders also reiterated the commitment of member countries to keep their markets open to promote trade and investment, and to refrain from imposing unnecessary non-tariff measures. This commitments will help ensure supply chain connectivity, especially for food items, medicines, medical supplies and other essential goods. Significant progress is also expected to be achieved in terms of financial integration and liberalisation, which would be conducive to greater intra-ASEAN trade and investment. Promoting e-commerce, strengthening digital infrastructure and reducing the digital gap will be high on the regional agenda. ASEAN policymakers are expected to refine their approach in several critical areas of the digital economy, including data governance, digital skills and cyber resilience. Finally, the recovery strategy is also expected to focus on sustainable investment and sustainable finance.

Note

1. "Developing Asia" consists of the following countries: Bahrain, Bangladesh, Bhutan, Brunei Darussalam, Cambodia, China, India, Indonesia, Iran, Iraq, Jordan, Korea, Kuwait, Lao PDR, Lebanon, Malaysia, Maldives, Mongolia, Myanmar, Nepal, Oman, the Philippines, Qatar, Saudi Arabia, Singapore, Sri Lanka, Thailand, Timor-Leste, Turkey, the United Arab Emirates and Viet Nam.

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ONGOING CHALLENGES OF COVID-19

The *Economic Outlook for Southeast Asia, China and India* is a regular publication on regional economic growth, development and regional integration in Emerging Asia. It focuses on the economic conditions of the Association of Southeast Asian Nations (ASEAN) member countries: Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Viet Nam. It also addresses relevant economic issues in China and India to fully reflect economic developments in the region. This November update of the Outlook, following the Update 2020, released in July, presents a regional economic monitor, depicting the economic outlook and macroeconomic challenges in the region amidst the COVID-19 pandemic.

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