



## Matthews Asia Perspective

### Impact on South and Southeast Asia If Trade Dispute Further Escalates



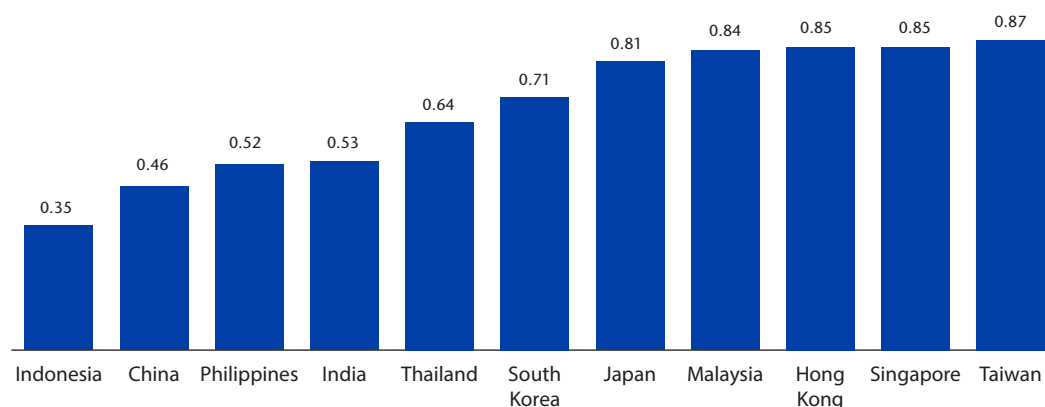
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The U.S. government recently hiked the tariff on US\$200 billion of Chinese exports to 25% from 10%. In response, China raised tariffs on nearly US\$60 billion of U.S. goods to 25% from 10%.

The further issue is whether the U.S. will impose tariffs on the remaining US\$300 billion or so of Chinese exports, with President Trump having ordered the U.S. trade representative to begin the process of raising tariffs on remaining imports from China by around the end of June 2019. These differ from the other Chinese exports, as they include mostly consumer goods such as smartphones, computers and textiles, and U.S. consumers are more dependent on China for these goods. If the U.S. proceeds to impose these tariffs, it would clearly hit China's trade partners as many products in the list depend on global supply chains.

In South and Southeast Asia, the more domestic-oriented economies such as India, Indonesia, and the Philippines will be more resilient. More open economies in the region such as Singapore, Vietnam, and Malaysia are likely to be harder hit (although Vietnam and Malaysia are likely to see some offsetting benefits from trade diversion and production relocation in the medium term). The chart below shows correlations between real GDP and trade in Asia.

**FIGURE 1. REGIONAL CORRELATIONS TO GLOBAL TRADE**



Source: Bloomberg, data between 2001–2018

Last year's (2018) monetary policy tightening in India, Indonesia, and the Philippines has also opened up some policy space which can be used to cushion the economy. Real policy rates are high in India, Indonesia, Malaysia and the Philippines, with Malaysia and the Philippines having made early moves to ease policy. For Indonesia and the Philippines, despite the positive steps taken to stabilize the current account and capital flows, the external uncertainty around regional trade tensions looms large for sentiment. This could limit in practice the extent to which monetary policy could be used. That said, the Philippines central bank, BSP, last week noted concerns over the global growth outlook while also nudging down its inflation forecast, suggesting that it will remain undeterred in easing interest rates.

On the fiscal side, Thailand and Indonesia have relatively more fiscal space to provide stimulus, while India is also likely to run a wider central government deficit post-election. The charts below show both monetary and fiscal positioning in Asian economies.

Potential spillover effects are worth noting. On the exchange rate channel, the Chinese yuan (CNY) may be under pressure in the near term, in the event that China might use its currency to mitigate the impact from higher tariffs. A weaker CNY will tend to drive regional currencies lower to maintain competitiveness, with Singapore, Vietnam and Malaysia having the largest relative exposure to China in terms of exports as shown in the chart on page 2.

FIGURE 2. REAL POLICY AND MARKET INTEREST RATES

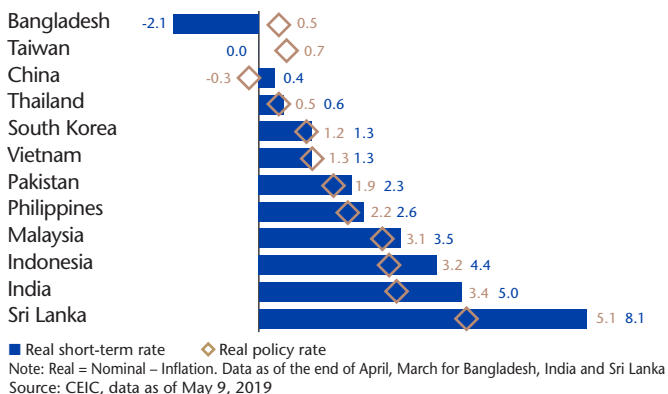


FIGURE 3. PUBLIC DEBT/GDP (%)

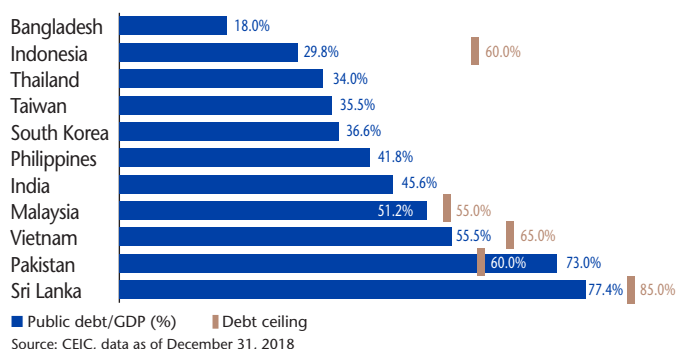


FIGURE 4. CENTRAL FISCAL SURPLUS/DEFICIT (% OF GDP)

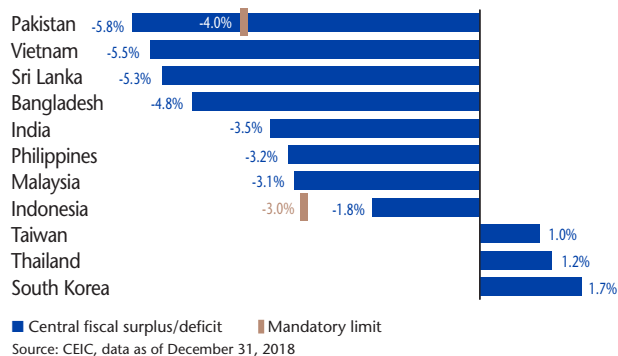
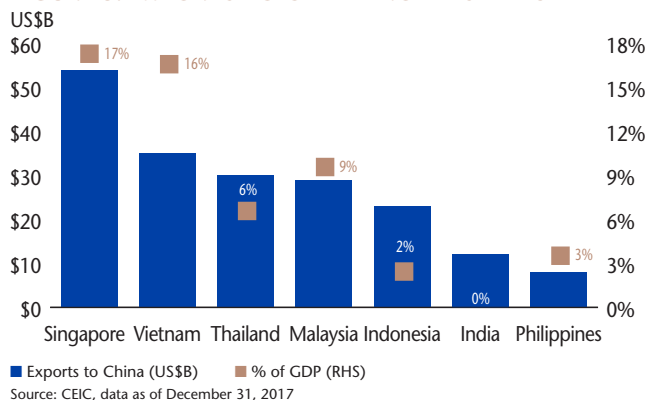


FIGURE 5. EXPORTS TO CHINA FROM ASEAN-6 AND INDIA



Overall, Singapore appears most vulnerable to the US–China crossfire, while the negative effects of supply chain linkages with China are offset for Vietnam, Malaysia and Thailand by potential benefits from trade diversification and production relocation. India and Indonesia have low supply chain exposure to China, and may well benefit from FDI flows into low-value export industries that overlap with China.

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