DISCUSSION ON THE REBOUND OF SOME ASIAN EMERGING ECONOMIES AFTER THE GLOBAL FINANCIAL CRISIS IN 2008

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Abstract:

The 2008 global financial crisis (GFC) was considered as the largest and sharpest crisis in recent 60 years as it had profound impacts on most economies in the world. Asian emerging economies were also seriously affected by the crisis. However they did in fact initiate their recovery sooner, faster and more strongly than advanced countries, then returning to high growth rates more quickly. This research analyses the impacts of GFC on some Asian Emerging Economies and the rebound of these countries after the GFC, as well as discusses the reasons for the rebound. Some main reasons indicated in the paper include the resilient financial system and sound monetary and fiscal policies and increase in investment and domestic demand.

Keywords: *financial crisis, emerging economies, crisis vulnerability, recovery*

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The global economic crisis was caused by the coming together of several structural as well as business cycle factors that conspired to produce a "perfect storm" of epic proportions. These factors ranged from the collapse of the housing market in the United States, imbalances between the West and the East in terms of trade deficits, reckless and risky speculation and finally, the sovereign debt crisis that was a culmination of years of fiscal profligacy and loose monetary policies.

The global economic crisis basically originated in the West but had its effects on all economies of the world. Asian Emerging Economies includes Southeast Asia, China and India (OECD, 2013) also sufferred the impacts of GFC. However, after the crisis, those countries have recovered strongly with higher speed than other advanced economies. In the first part, this paper analyses how some Asian emerging countries fared the GFC by documenting their performance during the fallout from the crisis and the subsequent recovery is mentioned in the second part. Finally, some main reasons are stated to explain for the rebound of Asian Emerging

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countries post GFC.

1. The impacts of the GFC on Asian emerging economies

Emerging economies are those which rapidly growing and volatile economies of certain Asian and Latin American countries. They promise huge potential for growth but also pose significant political, monetary, and social risks (Businessditionary, 2015). According to OECD (2013), Asian emerging economies consist of ten countries in ASEAN and China, India. Much of the focus in this paper will be on three economies namely Malaysia, Indonesia and Thailand because of their notable recovery after the GFC.

Impacts of the GFC on Asian emerging economies

When the GFC erupted, Asian emerging economies were perceived to be insulated from the financial crisis because their financial institutions were not much exposed to distressed markets. However, when the crisis intensified, the Asian emerging economies were also affected because of multiple transmission channels originating from globalization as well as economic integration, which can be called "domino effect". The global crisis did not originate in Asia, and, indeed, the direct damage to the financial sector in Asia has been much less than in Europe and the US. Nevertheless, Asian economies were also hit by the crisis by two main ways, when export decreased and capital fled away.

Exports:

During the GFC, as global demand plummeted, the price of goods and other commodities declined as well, leading to a drop in trade volumes and prices. For example, when the U.S. economy began its recession in late 2007 and as its economic slowdown deepened, it not only demanded fewer exports from China, but it also depressed commodity prices, hitting all net commodity exporters regardless of the final destination of their exports. Naturally, the countries that were more open to trade and dependent on exports were hit severely. Most Asian emerging economies showed declines in exports in 2009. China experienced the biggest fall, over 40% year-on-year in this year, while large decreases were seen in Singapore, Indonesia, Thailand, Malaysia, India as well.

Along with the drop in exports, industrial production had declined sharply in year-on-year terms in almost all Asian emerging countries, with the notable exception of China. In particular, large declines (from 10% to 15%) have been observed, again, in India, Malaysia, Korea and Singapore (Masahiro Kawai, 2009).

Capital investment:

When a crisis of global dimensions affects the world economy, like the post Lehman Brothers panic, the negative wealth effects suffered in high income countries lead to a decrease in foreign investments and, therefore, to less available capital, especially for emerging countries. For example, international investors might have to reduce their exposures to emerging economies in response to shocks affecting their assets. In addition, international banks and other agents might generate capital outflows during crises, for example if a parent bank in another country finds itself in need to boost its capital. Therefore, losses in a crisis-hit economy might lead international investors

to sell off assets or curtail lending in other economies as well (T.Didier, C.Hevia and S. L. Schmukler, 2011). BIS-reporting banks' cross-border claims on Asia declined by about 15 percent between the third quarter of 2008 and the first quarter of 2009. This was roughly twice the reduction experienced in other regions and surpassed the decline seen during the worst of the Asia Financial Crisis (P. Jeasakul, CH.Lim, E.Lundback, 2014).

Evidence that international capital flows contributed to business cycle synchronization was provided by Kim and Kim (2013). They find that capital movements caused boom-bust cycles in the region. An output boom is driven by increases in consumption and investment following capital market liberalization. If this hypothesis is true, then an output *contraction* might have been expected to reduce during GFC. In fact, output shrank for Asian Emerging Economies as a whole for two consecutive quarters. Real GDP in ASEAN fell by 2 percents in the fourth quarter of 2008 on an annualized basis. This was also the modest shrink compared to other regions. China also experienced the decline of 2,5% in GDP growth due to the impact of GFC.

Table 1: Impact of the GFC

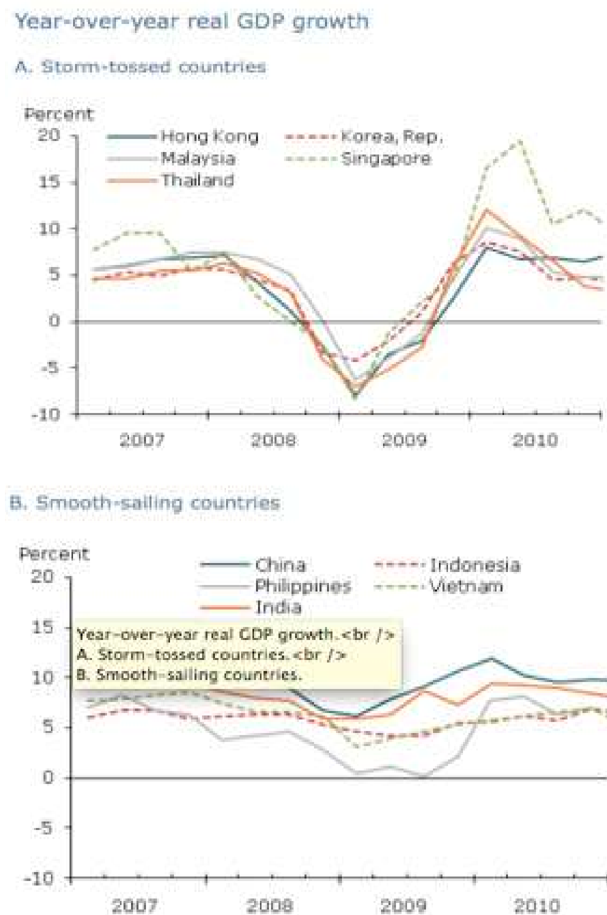
	1991	1992/93[2]	2001	2008/09[2]
Changes in GDP growth				
US	-2.1	1.5	-3.0	-2.7
eurozone	-1.1	-1.7	-1.8	-3.6
East Asia[3]	-1.2	-0.9	-2.8	-2.9
Japan	-2.2	-1.6	-2.7	-4.3
EEA	1.6	0.4	-3.0	-2.3
ASEAN[4]	-1.4	0.2	-2.3	-2.0
NIEs[5]	0.5	-0.8	-6.4	-3.2
PRC	5.4	2.4	-0.1	-2.5
Median for EEA	0.5	0.2	-2.0	-2.6

Source: ADB calculations using data from World Economic Outlook Database and Direction ofTrade Statistics, International Monetary Fund; and CEIC.

Nevertheless, Asian emerging economies, which were affected by GFC varied. They can be divided into two groups, one group of "smooth-sailing" countries, including China, India, Indonesia, the Philippines, and Vietnam, which were affected relatively less by the crisis. Another group of "storm-tossed" countries, including Malaysia, Singapore, South Korea, and Thailand, suffered more (Galina Hale and Alec Kennedy, 2012). During the first quarter of 2009, after the crisis had intensified globally, overall Asian emerging economies GDP growth hit a low point. However, the storm-tossed countries fell much deeper, declining by –6.7%. By contrast, the below graph represents none of

the smooth-sailing countries experienced a negative growth rate during the crisis. In fact, during the first quarter of 2009, these countries averaged a robust growth rate of 4.1%.

Graph 1: Countries influenced by the GFC (by group)



Source: Bloomberg, Fame data

2. The recovery of Asian emerging economies after the GFC

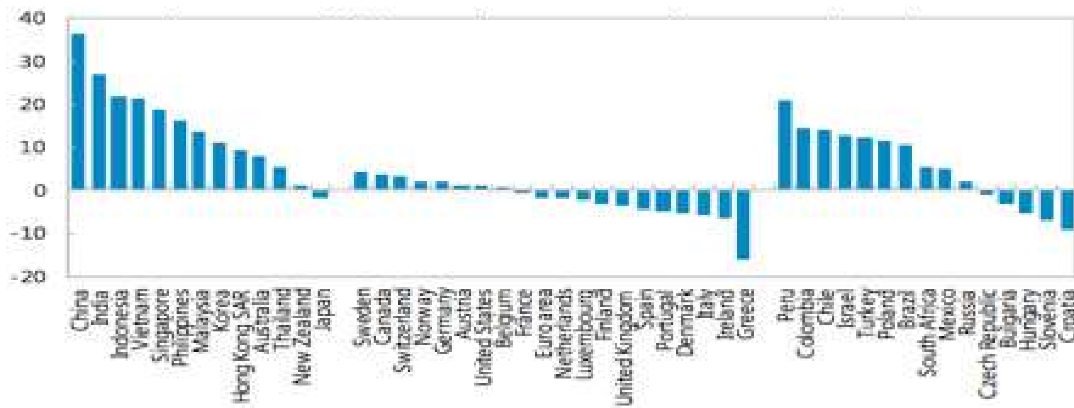
The rate of recovery from the global financial crisis of 2008–09 has varied between advanced and emerging market economies. Many emerging market economies, particularly in Asia, recovered quite quickly. In remarks opening the 2011 Asia Economic Policy Conference, Federal Reserve Board of Governors Vice Chair Janet Yellen noted that emerging Asia has been leading the global recovery in the wake of the financial crisis. Furthermore, in contrast to the Asian financial crisis of 1997-1998, no country in the region experienced a collapse of its banking sector or a balance of payments crisis.

The recovery in industrial production happened earlier and more strongly in emerging than in advanced economies. For instance, the pre-crisis peak in industrial production took place around April 2008 for both advanced and emerging economies. But a sustained recovery started around January 2009 for emerging economies while advanced countries started to rebound 4 months later, in May 2009. In other words, the recessionary phase of the business cycle lasted on average 9 months for emerging economies and 13 months for advanced countries (T.Didier, C.Hevia and S. L. Schmukler, 2011).

By mid 2012, output in most Asian Emerging countries was significantly higher than their pre-crisis levels, a sharp contrast to some other parts of the world. In which, China's real GDP increased by about 40 percentage points compared to pre-crisis peak, other countries like India, Indonesia and Vietnam also had impressive growth with real GDP rocketed by 20 percentage points. Whereas, about half of European countries showed less signal of recovery (Sweden, Switzerland, Norway etc.), and other European economies even got worse with lower GDP.

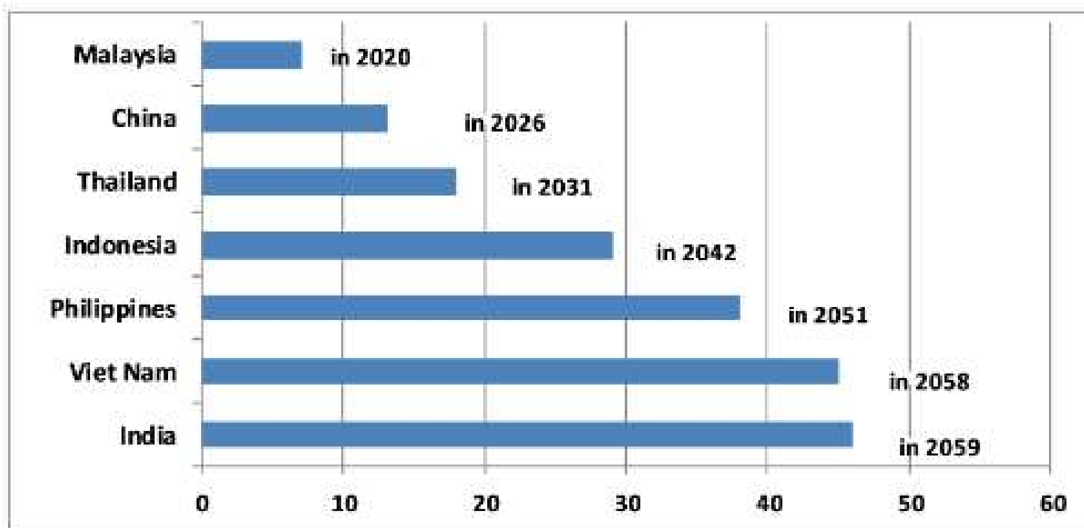
In a recent report of OECD about The Economic Outlook for Southeast Asia, China and India (2014), most of the Asian Emerging Economies had the GDP growth rate higher than 5% (excluding Brunei) in 2012. Indonesia was projected to be the fastest-

Graph 2: Real GDP (percentage points, relative to pre-crisis peak)



growing ASEAN-6 economy with an average annual growth rate of 6.0% in 2014-18, followed by the Philippines with 5.8%. Real GDP growth in Malaysia and Thailand was projected to increase by an annual 5.1% and 4.9% respectively, led by domestic demand, especially in infrastructure investment and private consumption. Singapore's economy was forecast to grow by 3.3%. Cambodia, Lao PDR, Myanmar and Viet Nam were expected to grow at a robust pace over the medium term. China was forecast to remain economic growth rate at 7.7% in 2014-18, this growth rate is lower than China's historical growth, however, China is still the fastest-growing country in the world. India was also expected to grow at 5.9% in 2014-18. In the "best scenario", if fundamental changes are applied, China and Thailand could become high-income countries within 20 years. On the other hand, Viet Nam and India will need more than 40 years to reach the high-income group

Graph 3: Best scenario simulation of estimated time required to become high income countries for selected Asian middle income countries (years)



Source: OECD Development Centre; http://www.oecd.org/newsroom/seaopr.htm

3. The determinants of recovery and the growth of Asian emerging economies after the global financial crisis

As a result of further integration into the world economy, Asian emerging economies are expected to be exposed more to economic shocks than 30 years ago. However, emerging market countries did in fact recover quickly after the GFC. This section will examine the reasons as well as policies taken by Asian governments, particularly Malaysia, Indonesia and Thailand to recover their economies.

a. The resilient financial system and sound monetary and fiscal policies

Financial system

One of the key strengths can be attributed to the sound fiscal and monetary policies and a reinforced financial system introduced in the wake of the 1997/98 Asian economic crisis. Indonesia instituted an overhaul of its macroeconomic structures and moved to build sound, economic foundations, hence entering the crisis in a relatively sound fiscal position and thus effectively carry out counter-cyclical policies. In 2008, the fiscal balance as a percentage of GDP was close to zero compared to nearly -1.0% in South East Asia. Moreover, Indonesia enjoyed a healthy financial sector, which included stricter financial market supervision and regulation, and the introduction of a deposit insurance system. Banks remain generally well-capitalised, having avoided overexposure to bad assets that triggered recent economic crisis (Jacobo Bermudez, 2012).

The financial intermediation process in Malaysia has been in good order through the economic turbulences as the credit continued to flow to the real economy. Outstanding loans increased by 10.1% per year between July 2007 and July 2009. The resilience of the banking system, which took up to 59.7% of the total assets of the financial system, was to ensure the continuing flowing of credits into the economy and providing borrowers who suffered from temporary cash flow shortages ample liquidity. Moreover, the Central Bank of Malaysia has actively been enhancing the credit risk management infrastructure and underwriting practices in the period following the Asian financial crisis. Therefore, the quality of credit of the banking systems' portfolios hardly experiences significant deterioration. Total non-performing loans (NPL) dropped by 33.4% while the net NP ratio improved to 2.1% as at Sep 2009 from 4.6% at the beginning of 2007. The "originate and hold" model used in banking institutions together with the legal requirement for all foreign institutions in Malaysia to be locally incorporated with capital committed to support Malaysia operations and obligations, also helped to mitigate the contagion effect of the foreign parent banks located in the countries severely affected by the crisis. (Muhammad bin Ibrahim, 2009).

Similarly, Thailand banking sector succeeded in remaining sound during the financial turmoil as the Thai banking system's foreign investment exposure was only about 1% of its total assets at the end of 2008. Thanks to the significant improvement in risk management practices post the Asian financial crisis, Thai banks have relied heavily on domestic deposits and hence the pulling back of financing did not happen (Pongpattananon, N and

Tansuwanarat, K, 2009). The diversification of bank revenue, which focusing on expanding their services to retail customers and small to medium size enterprises have improved their risk profile, reducing earnings volatility and lowering concentration risk associated with lending to larger corporates.

Monetary Policies

The reduction in interest rate was the response of most central banks in the regions, for instance, the Bank of Thailand cut interest rate four times down to 1.25% per year. The Bank Negara Malaysia both aggressively cut interest rate three times to a low 2.0% per year and lowered the reserve requirement by 200 basis points to 1.0% while the Bank of Indonesia lowered its benchmark interest rate by 375 basis points, from 9.25 per cent in December 2008 to 6.5 per cent in September 2009.

In Indonesia, the reduced lending rates helped lower the costs of credit but more importantly, the Government established a loan guarantee facility within the People Business Credit (KUR) for firms facing financing difficulties during the crisis. The KUR was established in 2007 to provide increased credit access to small and medium-sized enterprises (SMEs).

Fiscal Policies

To supplement monetary policy easing, Asian economics also used an expansionary fiscal policy. Substantial economic stimulus packages were announced, with its size relative to GDP was as followed: Malaysia more than 5% of GDP, Thailand between 2% and 5% of GDP and Indonesia between 0.5% and 2% of GDP.

Malaysia government imposed two stimulus packages, the first one (ESP 1) and the second one (ESP 2) amounted to $1.9 billion and $16.2 billion, equivalent to 1.04% of GDP and 9% of GDP, launched in November 2008 and March 2009 respectively. The second package was much larger than the first one due to the heightened concerns that the economic deterioration was becoming severe. Some might argue that the first rescuing package was introduced quite late as other countries had embarked on similar programs much earlier. However, the introduction of the first stimulus was seemingly logical as its economy was still experiencing growth until the third quarter of 2008. The two packages were said to bring the country's fiscal deficit to higher position, i.e 4.8% in 2008 and 7.6% in 2009. The ESP 1 was to ensure the well-being of citizen, developing human capital and strengthening national resilience while the ESP 2 was ESP 2 aims to reduce unemployment and increase employment opportunities, ease the burden of citizens, assist the private sector in facing the crisis, and build capacity for the future. Details about the size and the target of the rescuing packages will be discussed later (Malaysia Ministry of Finance, 2009)

The Thai government in 2009 initiated the first and second stimulus package (known as SP1 and SP2). The SP1, totalling THB 116.7 billion, was to respond to the weak domestic demand and accommodate economic activities. The SP2, totalling THB 1.43 trillion, was allocated for investment projects during 2009-2012.

On the set of the crisis, Indonesian government announced a stimulus package of 7.1 billion USD, 1.4% GDP which is the smallest

package among other Asian countries averaging 7% GDP. Furthermore, 75% of the stimulus packaged was allocated for tax cuts, concentrating on personal income, corporate income or tax exemptions for lower-income households. (Ministry of Finance, Indonesia, 2009). As part of the stimulus efforts, corporate tax rates were reduced by 5 percentage points to 25 per cent. Moreover, small enterprises, i.e. corporate taxpayers with an annual turnover with no more than IDR 50 billion (USD 4.8 million), are entitled to a tax discount of 50 per cent off the standard rate. Hence, the combination of demand and supply support created the effect of employment, generating 3.7 million jobs.

b. Shifting towards domestic demand

Domestic demand was the key to Indonesia's robust growth. Indonesia was not lopsidedly reliant on exports and Douglas McWilliams, ICAEW chief economic advisor and chief executive of CEBR said "Indonesia's export to GDP ratio stands at 30%, compared to almost 100% in Malaysia and over 208% in Singapore, which indicates that it would not be as badly affected by a worsening global climate". In 2011, population of about 240 million with 60.9% belonged to the middle class, according to a survey by the Indonesian central bank, therefore, domestic demand played a key role in driving Indonesia's growing market. Consumption accounted for 55.5% of GDP, which helped to provide Indonesia with some protection against international fluctuations in prices and demand. Bank Indonesia reported that retail sales, a gauge of domestic consumption grew 22% year-on-year. And if Indonesia's economy continues to grow as it has, millions will enter the middle class over the next decade. The Chinese central planners should envy since Chinese officials have long been trying to "rebalance" China's economy to depend more on consumer spending at home rather than exports.

The Bank Indonesia retail survey found the rise in retail sales was due to higher demand for home appliances, drinks, cigarettes and food. Euro-monitor predicts that between 2012 and 2020, consumer spending per household and household disposable income is likely to grow by 39.2% and 40.5% respectively (Adriyanto, 2011). Stronger purchasing power of Indonesian consumers offset the decline in exports of Indonesia against the global tide, standing it in good stead in the future.

At the same time, government strengthened the program of social security and social assistance. Therefore, it is in a better position to continue to allocate for series of social welfare programs. These mainly target at 30% low-income households, financial support for women and families with children up to the age of 15, on the condition that the children fulfill certain health-care and education requirements. It is the recognition of Government about vital role of domestic demand that tax cuts and social protection measures were implemented.

As the global crisis had a profound impact on the Asia countries such as Malaysia and Thailand, actions have been taken to rebalance growth away from its high dependence on exports to advanced economies, promoting domestic demand. High household savings rates are partly due to precautionary demand for savings as a result of low levels of

government spending on social programmes, such as unemployment insurance, health insurance and retirement pensions and educations. A reduction in household savings could promote growth by strengthening public spending in these areas.

Thailand introduced its tax stimulus package in March 2008. The objective was to alleviate the tax burden of individuals and businesses, providing tax incentives for private investments and for the property sector. Moreover, the “6 measures - 6 months” package received the cabinet approval in July 2008, aiming at cushioning the public’s high costs of living. These measures included the reduction of oil excise tax rates, electricity and water consumption fee subsidies, fixing of liquefied petroleum gas (LPG) price for household uses, and free fares for the third-class trains and 800 buses.

For Malaysia, the focus is targeted at low and middle-income earners through efforts to increase household disposable income. These cover subsidies to avert increases in the prices of daily food staples, measures to encourage home ownership, issuance of Syariah-compliant Government Savings Bonds, and improvements in public infrastructure. In Sabah and Sarawak, basic amenities will be provided in the states’ rural areas and there will be infrastructure projects, such as the expansion of Sibu Airport and deepening of Miri Port. Measures encompassed in the second thrust will also aim to improve school facilities, provide micro-credit programmes for farmers and agro-based businesses in rural areas, improve facilities at daycare centres for children and the elderly as well as women shelters, ensure the welfare of retrenched workers through tax incentives, and provide incentives for banks to defer repayments of housing loans.

ESP 1 and 2 are focused on expanding the domestic economy, as the global crisis has affected the disposable income of workers due to retrenchments and the economic slowdown. Nonetheless, measures relating to employment, welfare of people, education, and infrastructure development such as hospitals, roads and broadband facility, amongst others, are closely associated with the MDGs.

With the aim to promoting domestic consumption by raising disposable income, partly subsidising high living cost, the countries gradually reduce dependence on exports to major economies in the world, which are still suffering from the global crisis. What each economy needs today is a new path for growth that relies more on domestic and regional demand, therefore, reducing the negative consequences resulting from any external shocks (Masahiro Kawai, 2009).

c. Increasing investment

Another driving force for economic recovery was the huge influx of investment, especially FDI. With its demographic features: large and young population, associated with high domestic demand, potential labour market and stable economic climate, Indonesia is attracting more FDI. FDI reached almost US$12 billion in 2010 and topped US$10 billion in the first half of 2011. Most of the investments were in mining, transportation, warehousing, telecommunications, electricity, gas, and water projects. Fitch and Moody’s recently upgraded Indonesia to an investment

grade whilst S&P is expected to follow suit in the near future. As a consequence, the Domestic Investment Coordinating Agency (BKPM) is optimistic that the rating upgrade will attract more investors to Indonesia. Multinationals such as Toyota, Nissan and Suzuki have all announced plans to expand operations in Indonesia, especially by taking advantage of its large potential domestic market and growing middle class. Swedish home goods retailer IKEA is opening its first outlet in Indonesia in 2014, and foreign investors have poured money into the country thanks to the strong consumer base. With big companies flocking to Indonesia and with the media a buzz, foreign investors are cashing on the bright future of this archipelago. According to BKPM, the investment promotion agency of Indonesia, foreign investment in 2011 increased 18.9 percent to $19.28 billion. The delivery, storage and the telecommunications industry attracted the most foreign investment (19.8 percent), mining (18.5 percent), electricity, gas, and water for industrial use (9.6 percent).

Foreign ownership in Indonesian government bonds amounted to approximately $24,281 billion by the end of 2011. This figure is nearly quadruple that of the 2006's balance of $5.988 billion. During the year, foreign investors were also investing in equities. Based on Bloomberg and IDX data, foreign investors have been net buyers every year, ranging from $1.524 billion-$3.593 billion per annum, over the past five years. Foreign investors have accumulatively been net buyers of $12.195 billion from 2007-2011. It is believed that the political stability, stable macro-economic environment, low interest rate, strong fiscal policy, and the stable Rupiah currency are the main factors impacting investors' risk appetite to invest in Indonesia.

Almost 43% of Malaysia's first stimulus package is for infrastructure, such as the upgrading, repair and maintenance of public amenities (including schools, hospitals, roads, dwelling quarters for police and armed forces, and police stations); building of low-cost houses; public transport; and high-speed broadband infrastructure. Malaysian government also pay attention to capacity building for the future covering investments, off budget projects, creative arts, and the effective management of government financial resources. Specific measures on investment include increasing the funds of Khazanah National Berhad for domestic investments, dedicating more funds to projects in telecommunication, technology, tourism, agriculture and life sciences, as well as those in Iskandar Malaysia. Also covered are PFI projects such as those in infrastructure and biotechnology (Ministry of Finance, Malaysia, 2009).

In Thailand, most of the investment projects under the SP2 focused on the country's infrastructure system development, which encompassed transportation, education, health-care, irrigation and environmental management, science and technology, as well as capacity-building programmes for rural community and local intellect.

Considerations beyond the crisis

The further integration into the global economy in the years ahead will also pose significant challenges to Asian emerging economies. The new competitive dynamics

mean that structural adjustments by all parties are necessary. But these adjustments will be difficult against a backdrop of differences in demographics, saving and consumption habits, and exchange rate regimes and institutional arrangements, among others.

The global financial crisis is an important reminder to all countries that structural reforms in the real economy are inevitable. Asian emerging economies did quite well in pursuing institutional, banking, and corporate sector reforms following the Asian crisis. In the aftermath of the global financial crisis, Asia needs to continue with structural reforms. *First*, these economies must enhance investment rules and investors' protection to promote investment in physical capital, including infrastructure. Infrastructure remains underdeveloped in many Asian economies, presenting significant bottlenecks to growth. *Secondly,* the 2008 financial crisis and global turbulence with freefall of economic giants more or less reshaped the backdrop for the term "decoupling" of Asian countries in the wake of the crisis storm. Therefore, being more tied to young and strong neighbors could bring greater resilience to emerging economies in Asia, rather than their conventional extra-regional orientations, which created a self-propelling and sustainable growth mechanism (Choong Yong Ahn, 2011). The progress of integration should be continued through trade, tourism, capital markets, and macroeconomic links, with output correlations during the global crises most likely reflected the impact of the global shock. An upward trend in regional integration was shownin the following figure. *Third*, over the next several years, the external demand that has provided a key impetus for growth of Asian emerging economies may be subdued, as advanced economies would likely grow at a rate below potential, held back by significant balance sheet weaknesses (Heng Swee Keat, 2012). Asia has to rely more on domestic demand, but in the short term, few economies can do so meaningfully without placing stresses on macroeconomic and financial stability. Most Asian economies are not yet at a stage where domestic demand can take over as the primary source of growth.

4. Conclusion

The Asian emerging economies were hit by the GFC through two channels, which are export and capital flow. Most of those countries experienced declines in export, industrial production and the reduction in foreign investment. This led to the decreases in real GDP of Asian emerging economies in 2009, however, the levels to which those economies affected by crisis were varied. Some countries fell much deeper like Thailand, Singapore, Malaysia, while none of the smooth-sailing countries (including China, India, Phillipines, Indonesia, Vietnam) suffered negative growth rate. The rebound of Asian Emerging Economies was also stronger than advanced economies, which can be illustrated by the recovery in industrial production and GDP growth rates. The growth rates of some economies were even higher than pre –crisis. The author also stated three main reasons to explain for the rebound of Asian Emerging Economies, which are resilient financial system and sound monetary, fiscal policy; increasing investment and increase in domestic demand.

It is recommended that Asian countries should rebalance their growth towards more sustainability and more quality, shifting from export-oriented growth to domestic-demand. This will prove effective because Asian emerging economies are noted for young, dynamic and abundant population. They need to take advantage of this endowment as a consolidated backyard in times of weak external demand these days.

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