

Asia: A Look At The Fiscal Measures

- With the exception of China, India, Vietnam and Indonesia, we expect all the other Asian economies to record full-year GDP contraction in 2009. In response to the sharp collapse in exports and increasing strains on the retail numbers and more gloomy employment outlook, Asian central banks and governments have been quick to embark on aggressive monetary and fiscal measures even in late last year.
- All the Asian central banks that target interest rates have slashed their respective rates by at least 100bps from their peak in 2007/08. This is in addition to the government guarantees in some countries.
- On the fiscal front, the governments in Asia have since announced stimulus packages ranging from 1% to 12% of their respective GDP to prevent the economies from stalling. Given the severity of the recession and no signs of any meaningful upturn soon, there are hints of a second round of fiscal boost in some of these economies such as Malaysia and China.
- So far, a variety of measures have been announced by the various governments. There were measures to protect jobs in Singapore and we could see similar measures being rolled out in other Asian economies as it becomes more evident that the global recession is more protracted.
- In Taiwan and Thailand, the governments are targeting to boost domestic demand through vouchers and cash but the bulk of the government money is still being spent on infrastructure projects in most of Asia. This will also position Asia for the eventual economic recovery.
- In Asia, private consumption-to-GDP ratio has fallen to 52.7% in 2007 from 56.2% in 2000 and the higher savings rate in Asia also reduces the multiplier effects of the spending. In Singapore and China, the ratio is less than 40% and the import leakages also reduce the effectiveness of some of the measures in countries such as Singapore.
- Among the Asian countries, we feel that Hong Kong and Singapore have the scope for further stimulus spending as a result of the huge fiscal reserves. Following fiscal surpluses since 2000, South Korea is also in the position to finance the huge spending which it has announced. China, which has the lowest debt-to-GDP ratio also appears to be in the position to do more.

DoLing Out The Fiscal Measures

The NIEs (Hong Kong, South Korea, Taiwan and Singapore) in Asia are already in a recession and these countries will be the most affected due to their significant exposure to global trade and finance. In our earlier report, we estimate conservatively that most key Asian countries face the prospects of an unprecedented 10%-20% decline in their exports in 2009 based on the reversion to trend growth. In a pessimistic scenario, the extent of exports slump could be as much as 20% to 40% this year. As a result of NIEs' relatively stronger fiscal position, these countries will also likely be most aggressive in their fiscal policies. Both Hong Kong and Singapore have not ruled out further stimulus measures if the recession deepens and South Korea is already working on a supplementary budget.

We expect **Hong Kong's** budget deficit to surge to as much as 5.4% of GDP for the fiscal year beginning April 2009 although the government has a more conservative projection of 2.4%. The proposed package includes one-time salary and property tax relief measures as well as infrastructure projects worth HK\$39.3bn.

Singapore's response to the downturn was the Jobs Credit Scheme and its Risk-Sharing Initiative in which the government takes up 80% of the risk of bank lending to the corporates. Singapore's S\$20.5bn (8% of GDP) Resilience Package was focused mainly on protecting jobs in the downturn. The Jobs Credit scheme will pay employers 12% cash on the first S\$2,500 of each employee's wages every month. We also note that the government has room to bring forward more infrastructure projects to counter weakness in the construction sector. Singapore has not ruled out plans for using more of its reserves. For Singapore, the estimated net investment income contribution of S\$7.7bn in FY2009 will help to tone down the overall fiscal deficits to around 3.5% of GDP.

South Korea has announced KRW14 trn (US\$9bn) in new spending (KRW11 trn) and tax cuts (KRW3 trn) in November last year. The key areas include infrastructure projects and programmes for the agricultural sector and SMEs. Since then, the government has also put forth the KRW50 trn 4-yr 'Green New Deal' to invest in infrastructure, energy and water resources. The project is expected to create more than 956,000 jobs in the country. The government is likely to announce a supplementary budget by the end of March. All these fiscal spending came on top of liquidity injections into banks and the government's guarantee of banks' US\$100 bn of foreign currency debt.

In November, the **Taiwan** government announced a NT\$500bn 4-yr (2009-2012) economic stimulus package. For this year, the country is expected to record a 2.6% of GDP fiscal deficit. Besides the infrastructure spending and tax breaks, the government has already spent NT\$85.7bn on a shopping voucher programme to stimulate domestic demand. So far, the impact from the voucher programme has been fairly subdued. Meanwhile, the tax cuts which are still subject to legislative approval, will only kick in starting 2010 with the corporate tax rate to be reduced to 20% from 25% and the personal income tax rate by 1ppt for the lowest tax brackets.

In other parts of Asia, the **Thai** government has unveiled a THB116.7bn supplementary budget which contains one-time cash handouts to low-income families, tax cuts and more free education and subsidies for transport and utilities. On top of this, there is an additional THB1bn budget to boost the country's tourism industry. **Philippines'** PHP330 bn (4.4% of GDP) economic resiliency package includes infrastructure projects in the rural areas and tax rebates. The Philippines government has already raised its budget deficit ceiling to PHP177.2bn (2.2% of GDP) for this year from PHP102bn.

So far, one of the largest stimulus plans came from **China** which announced a 2-yr RMB4 trn (US\$586bn) stimulus package in November last year, equivalent to 12% of GDP. About 70% of the spending will be on infrastructure. However, only about a quarter of the package is new spending. There is expectation of further spending plan and tax cuts although the Chinese government has not announced any new stimulus at the National People's Congress which will be in session from 5-13 March.

Similarly, **Malaysia** is due to unveil a second fiscal stimulus package on March 10. Earlier stimulus package of MYR7 bn (1% of GDP) announced in November was dwarfed by those in other Asian economies. Central to the stimulus package were low cost housing projects and transport infrastructure and around 75% of the money has been disbursed. Given constraints from an already large budget deficit, the upcoming package might yet disappoint in terms of size but the government will be careful as there is limited ammunition left. In general, the market is expecting another package of around MYR10-30 bn which will focus more on reducing business costs (e.g. cutting taxes) and more spending on infrastructure projects. The Deputy Fin Min has said that the supplementary budget will be at least MYR10bn.

| Country | USD bn | % GDP |
|-------------|--------|-------|
| China | 586.0 | 12.0 |
| Taiwan | 14.3 | 4.0 |
| Singapore | 13.2 | 8.0 |
| South Korea | 9.0 | 1.5 |
| Philippines | 6.8 | 4.4 |
| Indonesia | 6.1 | 1.5 |
| Thailand | 3.2 | 1.3 |
| Malaysia | 1.9 | 1.0 |

Source: Newswires and various governments

The **Indonesia** government has raised its budget deficit forecast to IDR137 trn (2.6% of GDP) from original budget of IDR51trn (1.0% of GDP) for this year. The IDR73.3 trn fiscal stimulus package which kicks off this month, comprise mainly tax incentives (76%) and some spending on infrastructure development. With the parliamentary and presidential elections looming, there is pressure for the government to spend more to boost its economy this year.

Ballooning Fiscal Deficits is a Concern

We expect Asian governments' budget deficits to balloon this year amid the large spending plans and lower revenue resulting from the economic downturn as well as the tax relief measures being unveiled. However, most of the Asian governments are well-placed to splash out expansionary fiscal measures as a result of the strong fiscal positions built up over the years but the debt market remains the key avenue for the financing of the deficits although there is also some scope for multilateral and bilateral loans. Public debt has remained manageable at under 50% of GDP for most of the Asian countries although the ratio could rise further as the government finance their new stimulus plans. The strong foreign reserves positions of the Asian countries and their currency swap facilities should also help to reassure investors.

Singapore would be drawing S\$4.9 billion from past surpluses. For **Hong Kong**, the fiscal reserves balance was at HK\$523bn at end-2008. Officially the estimated deficits for FY09 are around HK\$40bn (or 2.4% of GDP), which only accounts for less than 10% of the reserves. Despite the buffer and a fairly conservative budget, Hong Kong government said it would issue sovereign debt for the first time since 2004 during which it issued HKD20bn. **South Korea** has a strong fiscal position after running budget surpluses since 2000. However, the country will issue bonds for the first time since 2006 to finance some of the spending.

China's fiscal deficit is expected to be financed through domestic bond issuance, as the national debt-to-GDP ratio is relatively low at around 10%. The RMB4tn fiscal stimulus package is likely to boost the ratio towards 15%, which is still benign and the lowest in Asia. However, there are some concerns over the financing at the provincial level as only a fraction of the announced stimulus package will come from the central government budget although the lifting of banks' lending quota is expected to help.

Savings from its fuel subsidies program as a result of the lower global oil prices will go towards the financing of **Malaysia's** first MYR7bn stimulus package. The financing of the second fiscal package could pose some problem with the country's budget deficit already at an estimated 5.2% of GDP this year.

Around 70% of **Indonesia's** budget deficit will be covered by unspent budget from 2008 and US\$3.8bn standby loans (out of total US\$5.5bn) from multilateral and bilateral lenders. The government has also raised US\$3bn from the global bond market and IDR26 trn (US\$2bn) from the domestic debt market this year. Similarly, **Thailand** has also said that it is tinkering with the option to borrow US\$2bn from multilateral institutions or bilateral partners to support additional stimulus plans.

Room For More

There are questions over the efficacy of some of these measures which aimed to boost domestic spending to compensate for the anemic external demand. Afterall, in Asia, private consumption-to-GDP ratio has fallen to 52.7% in 2007 from 56.2% in 2000 and the higher savings rate in Asia also reduces the multiplier effects of the spending. In Singapore and China, the ratio is less than 40% and the import leakages also reduce the effectiveness of some of the measures in countries such as Singapore. Conversely, government spending would likely work better in countries such as the Philippines, Indonesia and Hong Kong which have larger share of private consumption. In the absence of a pick-up in external demand, the Asian governments are still depending on domestic consumption but the turnaround in US consumer demand will eventually lead the recovery in the economies.

| FX Reserves in Asia (USD bn) | |
|---------------------------------|---------|
| Country | Latest |
| Singapore | 167.1 |
| Malaysia | 90.4 |
| Indonesia | 50.9 |
| Thailand | 107.9 |
| Philippines | 39.3 |
| South Korea | 201.5 |
| China | 1,946.0 |
| Taiwan | 292.7 |
| Hong Kong | 181.7 |
| Source: Bloomberg | |

| Public Debt (% of GDP) | |
|------------------------|-------|
| Country | 2008 |
| Malaysia | 43.3 |
| Indonesia | 29.5 |
| Thailand | 23.5 |
| Philippines | 63.8 |
| South Korea | 32.1* |
| China | 10.0 |
| Taiwan | 31.6 |
| Note: * 2007 | |
| Source: CEIC, UOB, EIU | |

Among the Asian countries, we feel that Hong Kong and Singapore have the scope for further stimulus spending as a result of the huge fiscal reserves. Following fiscal surpluses since 2000, South Korea is also in the position to finance the huge spending which it has announced. China, which has the lowest debt-to-GDP ratio also appears to be in the position to do more to prevent slippage in the country's growth as it struggles to contain the expected increase in the country's unemployment rate.

| Aggressive Interest Rate Cuts in Asia | | |
|---------------------------------------|-------------------------|----------------------------|
| Country | Benchmark Interest Rate | From Peak in 2007/08 (bps) |
| Malaysia | Overnight Policy Rate | 150 |
| Indonesia | Overnight Rate | 175 |
| Thailand | 1-Day Repo | 225 |
| Philippines | Overnight Reverse Repo | 100 |
| Hong Kong | Base Rate | 575 |
| South Korea | Base Rate | 325 |
| China | 1-Year Working Capital | 216 |
| Taiwan | Official Discount Rate | 237.5 |

Source: Bloomberg, UOB

| Budget Balance (% of GDP) | | | | | |
|---------------------------|-------|-------|-------|------|-------|
| Country | 1998 | 2001 | 2003 | 2008 | 2009F |
| Singapore | 0.7 | -1.8 | -1.2 | -0.8 | -3.5 |
| Malaysia | -1.8 | -5.2 | -5.0 | -4.8 | -5.2 |
| Indonesia | 0.7 | -2.5 | -1.7 | 0.1 | -2.6 |
| Thailand | -0.5* | -1.94 | -3.05 | -1.8 | -3.5 |
| Philippines | -1.9 | -4.0 | -4.6 | -0.9 | -2.2 |
| Hong Kong | -2.5 | -4.9 | -3.2 | -0.5 | -5.4 |
| South Korea | -3.9 | 1.2 | 1.1 | 0.3 | -3.6 |
| China | -1.1 | -2.3 | -2.2 | -0.4 | -3.1 |
| Taiwan | -3.2 | -6.4 | -2.7 | -1.9 | -2.6 |

Note: * 1999

Source: CEIC, UOB

| Comparing the Size of Exports and Private Consumption | | |
|---|----------------------|----------------------------|
| Country | Total Exports-to-GDP | Private Consumption-to-GDP |
| Singapore | 185.0 | 38.6 |
| Hong Kong | 166.0 | 59.0 |
| Malaysia | 94.3 | 50.0 |
| Taiwan | 61.1 | 55.0 |
| Thailand | 60.0 | 52.0 |
| South Korea | 38.3 | 49.3 |
| Philippines | 34.9 | 77.0 |
| China | 33.0 | 35.5 |
| Indonesia | 26.4 | 58.0 |

Source: CEIC, UOB

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