NIKKEI ASIA REVIEW
27-3-22

ASEAN faces 'collateral damage' from Ukraine war's Europe impact

From Singapore to Thailand, spillover threatens COVID-hit economies anew

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SINGAPORE -- The Russia-Ukraine war is threatening Southeast Asia's economic recovery from the pandemic -- if not always directly, then by dealing damage via Europe.

While analysts have downplayed the Association of Southeast Asian Nations' economic exposure to Russia and Ukraine, they caution that a protracted conflict that hurts the European Union will have spillover effects, hitting everything from trade to tourism.

Malaysia's Maybank this month warned of "collateral damage on ASEAN" from the conflict and resulting sanctions against Russia.

"A broader Europe downturn will have larger knock-on effects on ASEAN's exports, foreign direct investment and growth," Maybank's report said. "The European Union accounts for a substantial 9% of ASEAN exports, and more than 11% for Vietnam and the Philippines." It added that foreign direct investment from the EU makes up 11% of ASEAN's total.

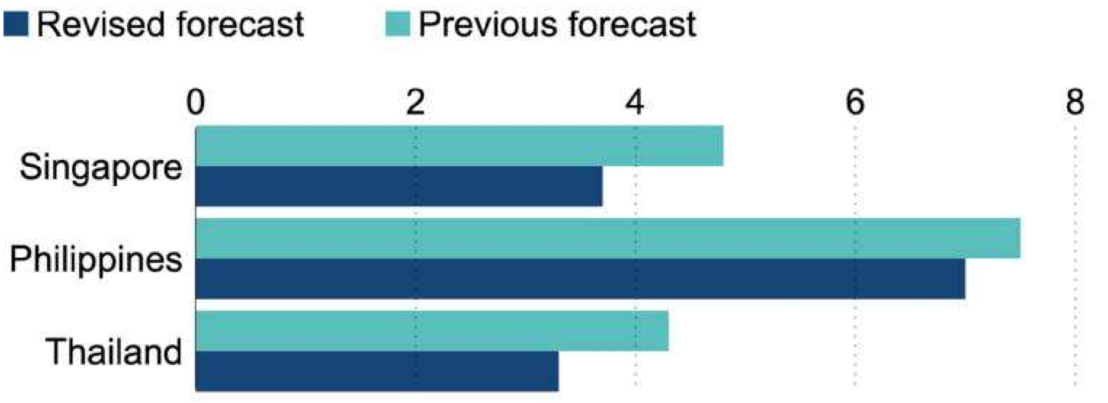
For Singapore, analysts Chua Hak Bin and Lee Ju Ye noted that the EU accounts for 9.2% of the financial hub's total non-oil domestic exports. They cut their forecast for growth in the city-state's gross domestic product this year to 2.8% from 3.8% "on the back of lower global and EU growth, higher energy prices [and] manufacturing supply chain disruptions."

"We are more worried about a broader Europe slowdown or a possible EU recession," they stressed.

Likewise, financial services firm Morgan Stanley Asia this month downgraded its growth projections for Singapore to 3.7% from 4.8%, for Thailand to 3.3% from 4.3%, and for the Philippines to 7% from 7.5%.

ASEAN economies' dimming growth prospects

(Morgan Stanley's revised projections as of March 9, in percent)



Source: CEIC, Morgan Stanley Research forecasts

DBS Group Holdings recently raised a similar alert over trickle-down risks to ASEAN. "In terms of direct trade, the region's overall linkages with Russia and Ukraine are limited," economists from the Singaporean bank wrote, noting that Russia and Ukraine make up negligible shares of its exports and imports. "The economic toll on ASEAN's exports could come instead from a broader European slowdown, should the conflict be prolonged."

At the same time, the DBS team did highlight some direct risks from "specific commodity dependencies." Chua Han Teng, Radhika Rao and Irvin Seah wrote that considering Russia's and Ukraine's roles as major wheat exporters and Ukraine's position as a major player in corn, Indonesia and the Philippines would be vulnerable to wheat supply shocks and Vietnam exposed to corn disruptions.

On the Philippines, they wrote that higher oil prices could hurt its "terms of trade by (around) 1.4% of nominal GDP, pressuring its record-wide trade deficit and the peso."

Travel, too, is a concern -- just as ASEAN countries start to revive the battered industry. One by one, the region's governments have been dropping tight border restrictions to try to give their economies a shot in the arm.

Thailand has announced that tourists will no longer need to certify that they are COVID-free before boarding inbound flights, starting April 1. The Philippines and Vietnam have reopened for tourism, and Malaysia will do the same at the beginning of next month, though these countries will still require testing. Singapore will allow vaccinated travelers from all countries to enter quarantine-free, starting April 1.

"The latest round of easings marks the most synchronized and forceful removal of entry rules yet for the region," Wellian Wiranto, an economist at Singapore's Oversea-Chinese Banking Corp., wrote recently. "The beleaguered tourism industry now enjoys its best hope of recovery in the last two years."

Yet the war could dash that hope to an extent.

Maybank noted that before the pandemic, Europeans accounted for the largest share of visitors to Thailand, at 17%. They also made up 13% of Indonesia's arrivals and 11% of Singapore's. But a worsening European economy and inflationary pressure could dampen travel demand.

Maybank suggested that Russia is also a direct risk to the Thai travel outlook in particular, since it "forms the third-highest share (5.4%) of Thailand tourism revenue after China (28%) and Malaysia (5.6%)." The Malaysian bank observed that "Russian visitors are already cancelling trips to Thailand due to the plunging ruble, flight cancellations and money-transfer difficulties."

How bad could European conditions get?

French asset management company Amundi this month warned that Europe faces high stagflationary risks -- combining slow economic growth and rising prices -- with a temporary recession possible this year.

"We expect eurozone inflation to remain stubbornly high through the year, particularly for energy and food, negatively affecting both demand and production," Amundi said. "The economic outlook has deteriorated and the main scenario is now less benign, with lower growth and higher inflation -- particularly in Europe over the short term."

Other agencies have dampened their growth outlooks as well. Credit rating outfit Fitch this month cut its world GDP forecast for 2022 by 0.7 percentage point to 3.5%, with the eurozone cut by 1.5 points to 3.0%.

Noting that Russia supplied around a quarter of the eurozone's primary energy consumption in 2019, Fitch's Chief Economist Brian Coulton wrote that "outright shortages and energy rationing are possible in Europe if there is an abrupt halt to Russian supply."

As the upward pressure on energy and food prices builds, experts say it will put a damper on ASEAN economic rebounds.

"Many studies that we have gathered found that there is a significant long-term relationship between inflation and economic growth as measured by GDP growth," Enrico Tanuwidjaja at Singapore's United Overseas Bank wrote this month. "One estimate for Indonesia suggests that for every percentage point of higher inflation, economic growth is negatively affected by 0.08 percentage points, as higher inflation will lead to slower economic growth."

Credit rating outfit Moody's says inflationary pressure is likely to build faster in economies where fuel and electricity prices have a heavier weighting in consumption baskets, or where imported fuel is predominant, such as Laos, the Philippines and Vietnam.

This will put ASEAN governments in a tight spot, after two years of pandemic pain.

"Pressure on governments to raise subsidies will increase, leading to greater fiscal strains," Moody's noted