

## Omicron Variant Rattles Economic Recovery



### Recovery in major Asian economies softens in Q3 2021

Most Asian economies lost momentum in their economic recovery in Q3 2021. For instance, annual growth of South Korea’s gross domestic product (GDP) decreased from 6% in Q2 to 4% in Q3, while Taiwan’s GDP rose by 3.7% year on year, down from 7.8% in Q2. Meanwhile, Malaysia’s economy returned to contraction with a yearly drop of 4.5% in Q3, after a 16.1% annual growth recorded in Q2.

Repeated outbreaks of Covid-19 and stringent lockdown measures to contain the virus have added significant pressures to consumer sentiment, leading to subdued domestic demand. In the period between early-July and late-August, the Covid-19 situation in Malaysia and Vietnam deteriorated, with surging confirmed cases. The 7-day average of confirmed cases in Malaysia jumped from a level of around 6,000 to 21,800, while cases in Vietnam surged from around 500 to 13,000.

Inflation in the Asian economies continues to accelerate in recent months. South Korea’s inflation rate advanced to 3.8% in November, up from 2.4% in September. Consumer prices in Singapore also accelerated to 3.8% in November, up from 3.2% in the previous month. India’s inflation rate rebounded to 4.9% in November from 4.5% seen in October.

### Challenges remain ahead for Asia’s economic recovery

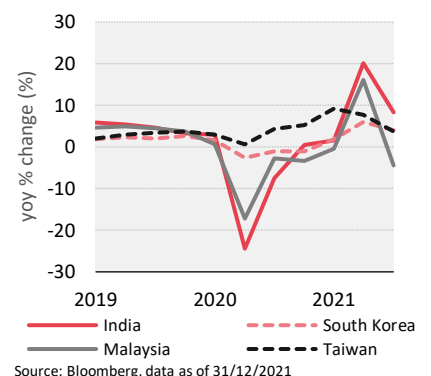
Looking ahead into 2022, Asian economies continue to face multiple downside risks including global supply chain disruptions and ongoing shortages of key raw materials, which are particularly problematic for the manufacturing sector. Furthermore, the emergence of the Omicron coronavirus variant is stoking concerns over the efficacy of existing vaccines and the potential re-imposition of stringent lockdown measures.

**Asia’s economies continue to face headwinds, including the Omicron variant and supply chain bottlenecks.**

**Asia’s central banks encounter increasing pressure of capital outflows sparked by faster tapering off of asset purchases and sooner-than-expected rate hikes in the US.**

**Investor sentiment in the financial markets is being affected by concerns over the Omicron variant’s impact on economic recovery.**

GDP of Selected Asian Economies



## Economic Research

January 2022

Consumer sentiment in Asia's economies is likely to further deteriorate if another round of social distancing restrictions is made necessary by the spread of the Omicron variant.

Against the backdrop of rising downside risks, governments will roll out fresh fiscal support in a bid to protect the economy from adverse impacts. For example, the Malaysian government has announced a spending plan in its 2022 budget, with an expansion in cash aid and financing support for households and businesses, as well as an allocation of MYR 4.8 billion to generate 600,000 job opportunities.

Additionally, the pace of recovery may continue to diverge between economies relying on trade in goods and/or services. In particular, goods exporters with a focus on technology products, such as Taiwan, will continue to benefit from solid external demand. On the other hand, with the Covid-19 pandemic still raging across the world, service exporters such as Thailand will be constrained by strict cross-border travel restrictions. Therefore, Covid-19 is expected to continue to widen the recovery gap between various Asian economies.

Forecasts by the International Monetary Fund indicate a softening economic growth ahead, with Asian economies as a whole expected to grow by 5.7% year on year in 2022, easing from a projected annual growth of 6.5% in 2021. Asia's advanced economies are expected to expand by 3.4% in 2022, while its emerging markets and developing economies are projected to accelerate by 6.3% annually.

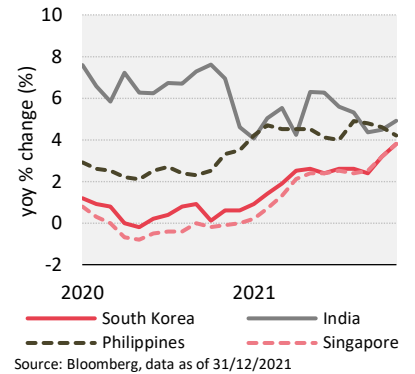
### Hawkish monetary stance of the US Federal Reserve may put further pressure on Asia's central banks

Along with rising inflationary pressures, the Bank of Korea (BOK) announced on 25<sup>th</sup> November that it was further raising the benchmark rate by 25 basis points to 1%, following its hike in August 2021. Rate hikes are expected to increase debt repayment burdens for households, weighing on their financing and consumption incentives. Meanwhile, other Asian central banks including Thailand, India, and Malaysia stuck to an accommodative monetary policy and kept their key interest rates unchanged.

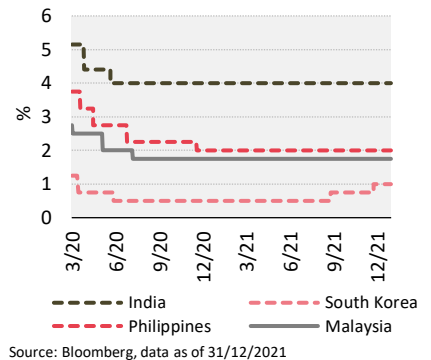
The US Federal Reserve (Fed) announced after its monetary policy meeting in December that it would accelerate the pace of reducing its monthly asset purchases. Additionally, more Fed officials now expect interest rate hikes of at least 75 basis points in 2022.

The growing strength of the US dollar, spurred by reduced asset purchases and an increased expectation of rate hikes, may weaken the currencies of Asian countries going forward, where some central banks are currently holding to a dovish monetary policy stance. Nevertheless, Asian economies are expected to be better prepared than in the 2013 taper tantrum, with more substantial foreign reserve cushions on hand to reduce the pressure created by capital flight.

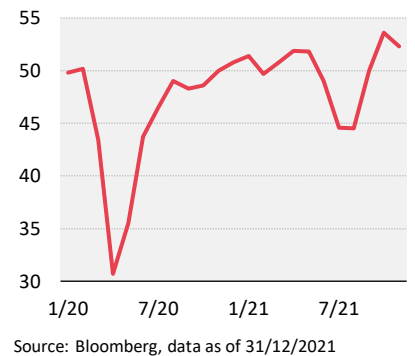
### CPI of Selected Asian Economies



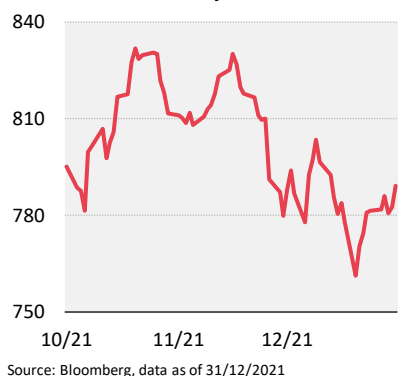
### Policy Rates in Selected Asian Economies



### Markit ASEAN Manufacturing PMI



### MSCI AC Asia ex Japan Index



## Economic Research

January 2022

### Financial markets impacted by emergence of Omicron variant and hawkish stance of the US Federal Reserve

Market sentiment was impacted in the fourth quarter of 2021 by an unpredictable Covid-19 situation. As of 31<sup>st</sup> December, the MSCI Asia ex-Japan index had declined by 1.5% compared to the end of September (when it saw a 9.9% drop from the second quarter). Most major Asian currencies stayed substantial against the US dollar, rising at between 0.2% and 1.5% by 31<sup>st</sup> December. However, the Indian rupee, Korean won and Japanese yen weakened against US dollar, decreasing by 0.3%, 0.3% and 3.3%, respectively in the same period.

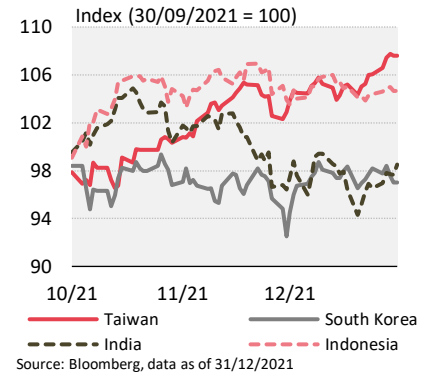
In early November, the South Korean government launched a plan to gradually lift virus-containment restrictions under a “Living with COVID-19” policy. However, the country then saw a rapid rise of newly confirmed cases, from 4,000 to approximately 6,000 as of mid-December, putting significant pressure on its medical facilities. Meanwhile, with the global spread of the Omicron coronavirus variant, the South Korean government announced in mid-December that it would re-impose social distancing measures to curb the spread of the virus. Concerns over the Omicron variant and a re-imposition of Covid-19 restrictions have worsened market expectations regarding economic recovery, extending the market decline. As of 31<sup>st</sup> December 2021, South Korea’s benchmark equity index had declined by 3% compared to the end of Q3 2021.

Meanwhile, India’s equity market registered a loss of 1.5% between the end of Q3 2021 and 31<sup>st</sup> December 2021. Foreign institutional investors were seen shifting capital away from emerging markets like India, against the backdrop of the US Fed’s hawkish monetary stance.

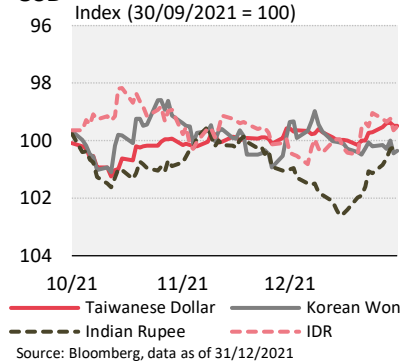
In the meantime, Taiwan’s equity market advanced by a substantial 7.6% and Indonesia’s equity market rose by 4.7% in the period from the end of Q3 2021 through 31<sup>st</sup> December 2021. The rally in the broader semiconductor industry fuelled capital inflows into Taiwan’s equity market. For Indonesia, rising commodity prices for major exports such as palm oil have boosted market sentiment.

Looking forward, the emergence of the Omicron variant and the pace of the US Fed’s rate hikes will continue to affect Asia’s equity markets.

#### Selected Asian Equity Indices



#### Selected Asian Currencies against USD



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