

Caution advised regarding risk of further capital outflow and currency depreciation if COVID-19 situation worsens

SHOHEI TAKASE
ECONOMIC RESEARCH OFFICE

MUFG Bank, Ltd.
A member of MUFG, a global financial group

13 MAY 2020

(ORIGINAL JAPANESE VERSION RELEASED ON 30 APRIL 2020)

Since the start of March, there has been a sharp rise in the number of COVID-19 cases in Asia (excluding China) and public health measures have been tightened in order to prevent the spread of infection. Due to the large contraction in economic activities resulting from the measures, one by one, growth rates in the January-March quarter are slowing or turning negative. For instance, in South Korea, where the spread of COVID-19 has been successfully suppressed, the real GDP growth rate for the January-March quarter released at the end of April was 1.3% YoY – the lowest since the July-September 2009 quarter. It appears the trade-off from their measures to control the virus was costly. Since April, many countries have decided to continue with or tighten their public health measures, such as prohibiting going outside, by imposing penalties amongst other methods. As a result, there will be an unavoidable, large contraction in economic activities within the region in the April-June quarter too.

In addition to these headwinds to the real economy, the problems of capital outflow and currency depreciation which are unique to emerging countries are also becoming a source of concern. In March, there was a net outflow of USD 43.1 billion in securities investment in emerging Asian countries (excluding China), which is the largest outflow since 2010 when the earliest data is available (Chart 1). When it comes to exchange rates, the depreciation of ASEAN currencies has been limited compared with that of emerging countries in other regions, such as Mexico, Brazil and Turkey, owing to differences in the level of freedom in trading based on economic fundamentals and various regulations. Nevertheless, there has been an overall trend of depreciation since around March, when the number of infections started to rise in Asia (Chart 2).

Currently, there appears to be a lull in the risk-off sentiment that had been dominant in financial markets and was an indicator of economic policies in major developed countries, and there are signs that the depreciation of emerging countries' currencies is coming to a halt. However, it seems the health care infrastructure in ASEAN countries is more fragile than that of developed countries (the number of PCR tests per 1000 people: 21.7 in Italy and 17.5 in the US compared with 4.8 in Malaysia, 2.7 in Vietnam, 0.9 in Thailand, 0.8 in the Philippines and 0.3 in Indonesia). As a result, there are concerns in these countries about the risk of infection spreading further at a faster pace and not being able to assess the situation. Even though the number of cases is comparatively low at present, the capital outflow and currency depreciation

mentioned earlier mean it is important to bear in mind that the economy will worsen further and that there is an undeniable possibility of another large-scale net outflow of capital if the effects of COVID-19 become more serious.

Chart 1: Net Securities Investment in Newly Emerging Countries in Asia (excluding China)

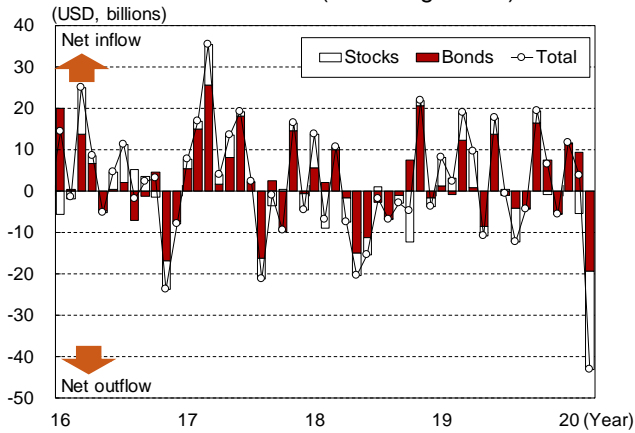
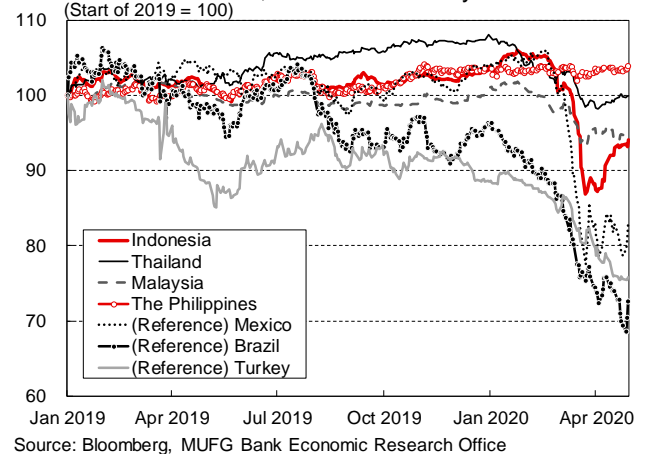


Chart 2: Exchange Rates of Major ASEAN Members, Mexico, Brazil and Turkey



(Translated by Elizabeth Foster)

For further details, please contact the Economic Research Office, MUFG Bank

Managing Director, Rei Tsuruta Tel: +81-(0)3-3240-3204

Written by Shohei Takase<shiyouhei_takase@mufg.jp>

This report is intended for information purposes only and shall not be construed as solicitation to take any action such as purchasing/selling/investing financial market products. In taking any action, each reader is requested to act on the basis of his or her own judgment. This report is based on information believed to be reliable, but we do not guarantee its accuracy. The contents of the report may be revised without advance notice. Also, this report is a literary work protected by the copyright act. No part of this report may be reproduced in any form without express statement of its source. This report is also available for viewing online.