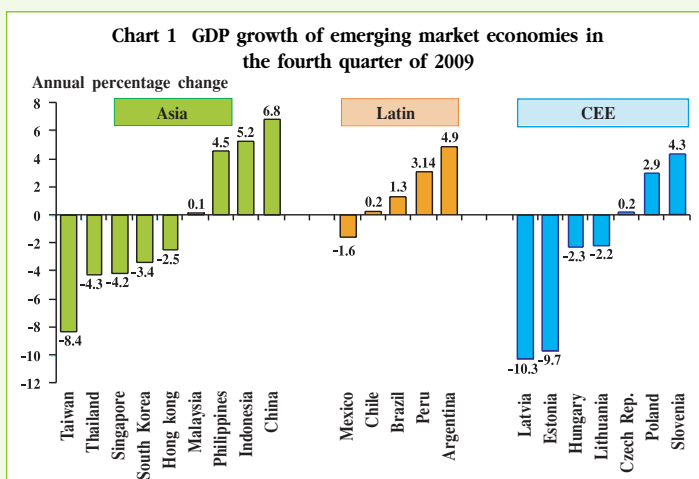


The impact of the global financial crisis on Asia and other emerging market economies

The global financial crisis, originating in the US, has affected every region of the world. At the start, advanced economies that are financially integrated with the US, notably UK, Euro area and Japan, have gone into recession, the result of which has been a sharp slowdown in emerging market economic activities, as reflected by a marked deceleration in 2008 Q4 GDP growth in emerging economies. The G3 recession has transmitted to emerging markets via 2 main channels, namely financial and trade.

(1) The financial channel: The financial crisis affected Central and Eastern Europe (CEE) directly since financial institutions in this region had consistently relied on external borrowing, particularly from the Euro area, to support domestic credit expansion. When Euro area financial markets locked up, several economies in the CEE faced liquidity shortfalls and were unable to roll over their external debt, mostly denominated in euro; the effect of which had been an erosion in confidence and capital outflows. Capital reversal then led to a sharp currency depreciation and undermined domestic investment and domestic demand. As a result, some CEE economies including Hungary, Ukraine, Latvia and Romania, have requested financial assistance from the International Monetary Fund (IMF).

Having experienced crisis episodes within the last two decades, financial institutions in Asia and Latin America have been cautious with external debt accumulation. Thus, they have been spared a direct hit during this crisis. Nevertheless, with heightened risks and uncertainties in the global financial market, Asian and Latin American economies have been affected indirectly through higher costs of borrowing, particularly from increasing credit spreads. Moreover, stricter financial institutions' lending standards, deleveraging by international investors and the decline in foreign direct investment have caused financial market conditions in these regions to tighten. In fact, curtailed trade credits have been a cause of economic slowdown in Asia.



Source: Bloomberg

Table 1 Foreign claims on the CEE

| Claims | Value (In billion of US dollars) | Per cent of total borrowing |
|-----------------|-------------------------------------|-----------------------------------|
| United States | 53.6 | 3.2 |
| United Kingdom | 46.8 | 2.8 |
| Japan | 28.3 | 1.7 |
| EU | 1,511.3 | 91.2 |
| Austria | 277.6 | 16.8 |
| Germany | 219.9 | 13.3 |
| Italy | 219.6 | 13.3 |
| France | 155.1 | 9.4 |
| Belgium | 136.7 | 8.3 |
| Netherlands | 122.2 | 7.4 |
| Sweden | 106.5 | 6.4 |
| Switzerland | 58.6 | 3.5 |
| Others | 215.0 | 13.0 |
| Other countries | 16.6 | 1.0 |

Source: Calculations by the Bank of Thailand, based on BIS Quarterly Review in March 2009. (Data as of September 2008).

(2) The trade channel: The impact of the crisis on emerging market economies through trade have come from both price as well as volume.

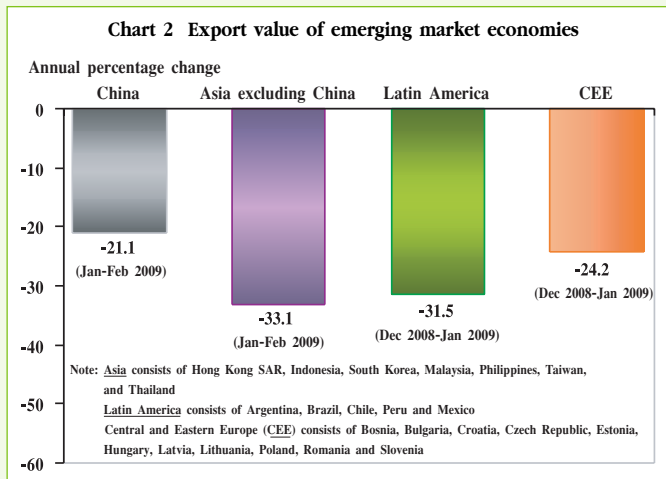
Price: Since the second half of 2008, commodity prices have declined drastically, following a deterioration in global demand. Falling commodity prices have affected most Latin American economies as well as some economies in Asia and CEE where commodities are major export products. Falling commodity prices have lowered income and caused some retrenchment in domestic consumption.

Trade volume: Since 2008 Q4, the impact of the global financial crisis on the G3 real economies have started to intensify, leading to a decline in private consumption. Emerging market exports have declined sharply in volume terms, especially for the Asian economies that are highly open to international trade and dependent on the G3 .

Impact on economic activities

The BOT's scenario analysis concerning the relationship between exports and domestic demand^{1/} shows that, with reference to the baseline case, a decline in trading partners' demand will affect Asia's GDP growth more pronouncedly than those of the CEE and Latin America; because as exports fall, investment and consumption decline more significantly in Asia than in the CEE and Latin America. Net export positions of Asian economies will be stronger than in other two regions as imports decline more sharply in response to export contraction particularly from machinery and raw material imports for the manufacturing sector. However, Asia faces a deeper contraction in investment than other regions because a larger proportion of investment in Asian economies are in high and medium-to-high technology manufacturing production for exports.

To conclude, the global financial crisis had an impact on Asian economies and other emerging market economies through both financial and trade channels in varying magnitudes and timing. Several CEE economies have experienced a large impact via the financial channel while all emerging market economies, Asia included, have been adversely affected mostly through trade contraction, which have also led domestic demand to slow down significantly.



Source: Bloomberg and CEIC

Table 2 Changes in GDP components as a consequence of 10 per cent decrease from baseline case in trading partners' demand for imports
 (percentage change from baseline case in 2009, in real terms)

| | Real GDP | C | I | X | M |
|-------|----------|------|------|-------|------|
| Asia | -4.1 | -1.8 | -4.0 | -10.6 | -8.6 |
| CEE | -3.0 | -1.1 | -1.1 | -8.6 | -4.8 |
| Latin | -2.5 | -1.0 | -2.1 | -9.5 | -4.1 |

Note: Values in the table are simple averages.

Asia consists of China, Indonesia, South Korea, Malaysia, Singapore and Thailand
 Central and Eastern Europe (CEE) consists of Bulgaria, Czech Republic, Hungary, Poland and Romania

Latin America consists of Argentina, Brazil, Chile and Mexico

Source: Calculated by BOT staff using Oxford Global Macroeconomic Model

^{1/} BOT staff calculation, based on simulations from the Oxford Global Macroeconomic Model.