



of trade liberalization, trade restrictions have risen sharply among the G-20 in recent years, as per UNCTAD data. We don't think any of these drags are going away. Therefore, Asian exporters may well have to settle for a new normal of anemic exports growth. Within the region, there are some additional challenges, starting with China's import substitution drive (which has hurt intermediate and capital goods exports from Japan, Taiwan, and Korea), rising cost of production (Singapore and Thailand), and failure to move up the value chain (Taiwan and Thailand).

For aspiring economies like India and Indonesia, these developments are disappointing. The prevalence of regional excess capacity and weak G2 demand for Asian exports will make it particularly hard for these economies to join the club of major export-oriented manufacturers. They will do better relying on manufacturing to satisfy domestic demand, in our view.

#### Debt

The rise in regional debt, especially in China, is under a great deal of focus, evidenced by a plethora of reports issued by multilateral agencies. Taking advantage of years of strong growth, favorable investor sentiment, relatively low rates, ample liquidity, expectations of stable currency, and supportive fiscal and financial sector policies, Asian borrowers have accumulated substantial debt in recent years. But the optimistic projections associated with these borrowings have turned out to be mostly wrong. Both nominal and real growth rates have slowed, pushing down ROE, real rates have turned out to be high owing to sharp disinflation or deflation, and for those with foreign currency borrowing, expectations of stable currency have been off by a large margin due to the strong USD cycle. For those in the commodity sector, the risks are the greatest due to the combination of sharp revenue declines and soaring cost of servicing foreign currency debt.

In addition to corporates, Asian households have amassed sizable debt in recent years, with Hong Kong, Malaysia, Singapore, South Korea, Taiwan and Thailand characterized by burdens amounting to over 60% of GDP. China's reported household debt figures are lower (slightly below 40% of GDP), but strikingly, its households have added more than 20% of GDP worth of debt in the past five years. Gross debt figures for wealthy economies like Singapore, South Korea, and Taiwan may be less alarming due to households' strong asset position, but for the rest of the cohort the high debt level can act as a major deterrent to the credit cycle and consumption outlook. High household debt may not be a source of systemic risk in the near term, but could readily become a chronic drag to growth. Unlike corporations, households don't have particularly orderly routes to restructuring debt. Hence firm level defaults and restructuring could form the headlines in the coming year, but the household debt burden that lies side-by-side could well be a bigger source of long-term headwind to the economy.

#### Conclusion

- Against this background, Asian policy makers need to recognize the near-term risk of deflation, debt, and trade dependency, and the medium-term risk of aging and lower potential growth. **Aggressive demand generating policy in the immediate future and well thought-out structural policies to address aging and competitiveness are needed.** The previously successful model of growing fast as a global beta is unlikely to be replicable for most Asian economies. The key is to recognize the challenges mentioned here and strive for a more domestically (and perhaps regionally) sustainable growth model

Taimur Baig