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Economic Headwinds in 2019: Navigating Priorities for ASEAN

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SYNOPSIS

To face economic headwinds in 2019, ASEAN member states should prioritise implementing ASEAN Economic Community 2025 and concluding RCEP negotiation.

COMMENTARY

THE NEW Year will likely see Southeast Asian economies face major economic headwinds namely the US-China trade tensions and the interest rate increases by the US Federal Reserve. While some observers think that the 90-day truce between Washington and Beijing could beget better relations between these two powers, they may overestimate China's ability to make concessions to the US.

As reflected in his speech at a gathering to celebrate the 40th anniversary of China's reform and opening up on 18 December 2018, President Xi Jinping stressed that "No one is in a position to dictate to the Chinese people what should or should not be done". Given that such remark came against the backdrop of the truce, it connotes that Beijing may not easily bow to Washington's demands.

Coping with Economic Headwinds

Even though China finally makes concessions in March 2019, it may not fulfill what the Trump administration wants. For instance, buying more American soybeans is easy, but implementing measures to address "unfair" trade practices to the degree that satisfies the US is more difficult to get done within the 90-day timeframe.

Consequently, the world in 2019 may witness more rounds of tariff escalations or trade-restricting measures being rolled out by Washington and Beijing. Regional economies will have to brace themselves again for future impacts.

On the financial front, on 19December the US Federal Reserve raised the interest rate from 2.25 to 2.50 points and forecast two increases in 2019. The Fed did so to ensure there will be room for it to use a monetary policy, especially decreasing the interest rate, to fight the next US recessions. These future moves can still affect the ASEAN region.

The additional 2019 hikes could trigger capital pullouts from Southeast Asian countries as investors move funds to seek higher yields in the US. If not well-managed, such capital outflows may instigate financial instability and crisis in regional economies.

How ASEAN Can Avoid Headwinds

While it is unlikely to avoid the effects of such headwinds on regional economies, ASEAN member states in 2019 can nevertheless counter such impacts via regional initiatives, namely ASEAN Economic Community 2025 (AEC 2025), ASEAN-Hong Kong Free Trade and Investment Agreements (AHKFTAs), Regional Comprehensive Economic Partnership (RCEP), and Chiang Mai Initiative Multilateralization (CMIM).

First, Southeast Asian policymakers should prioritise the complete implementation of AEC 2025. This is a regional economic integration project by ten ASEAN member states purposed to achieve five objectives: a highly integrated and cohesive economy; a competitive, innovative, and dynamic ASEAN; enhanced connectivity and sectoral cooperation; a resilient, inclusive, people-oriented, and people-centred ASEAN; and a global ASEAN.

Advancing AEC 2025 will enable businesses to better tap on the integrated market of 630 million people, rendering regional economies more resilient amidst the incoming headwinds.

Second, Southeast Asian governments should ratify ASEAN-Hong Kong Free Trade and Investment Agreements (AHKFTIAs) signed in November 2017 so that these treaties can enter into force in early 2019 as expected. The agreements will enhance cross-border flows of goods, services, and investment between ASEAN and Hong Kong economies.

They not only allow firms to enjoy greater access to goods and services markets and better investment protection, but also enable ASEAN nations to further tighten trade and investment ties with China and recuperate from the damage that future Washington-Beijing trade spats will inflict on them.

Wrap Up RCEP Soon

Moreover, ASEAN authorities should concentrate on wrapping up the RCEP talks. RCEP is a free trade agreement among 16 economies. If concluded, this bloc will encompass the market of 3.6 billion people and contribute to a third of the global GDP. It will cover 29% of the global trade and 26% of the world's foreign direct investment flows.

Concluding the negotiation will not only create more opportunities for businesses to deepen their supply chains, but also enable RCEP economies to diversify and cushion the negative consequences of the future U.S.-China trade wars.

In addition, Southeast Asian nations (together with China, Japan, and South Korea) should advance the CMIM, a regional financial safety net under the ASEAN+3 financial cooperation process. Launched in 2010, the scheme provides financial support via a network of currency swaps to help ASEAN+3 nations weather their balance-of-payments difficulties.

Because future Fed rate hikes could trigger investors' panic leading to financial instability and capital flights in certain regional economies, CMIM can provide financial assistance to alleviate such problems.

How to Get There from Here?

Admittedly, the above initiatives face their own challenges. For example, a main hurdle for completely implementing AEC 2025 is in little coordination among domestic ministries and agencies. Thus, individual ASEAN countries must sort out how to better coordinate work among the involved authorities.

Also, the elections in Australia, India, Indonesia, and Thailand may likely delay the conclusion of RCEP negotiation in the first half of 2019 as the politicians in these nations will likely prioritise their electioneering over international matters. As the momentum in RCEP talks will tend to pick up in the second half of next year, the parties' different positions and preferences need to be reconciled to seal the deal.

Certain domestic hurdles must be cleared for a successful ratification of the ASEAN-Hong Kong treaties. Regarding CMIM, while an agreement on 14 December to create more favourable conditions enabling the regional financial safety net to better assist crisis economies is laudable, efforts to advance the other CMIM aspects have been lackluster in recent years.

For one thing, its size has remained the same US$240 billion since 2012. With this amount, the scheme can at best simultaneously provide lending support to a few small- and medium-sized economies should they come under a crisis. Hence, the participants must seriously push for the expansion of the CMIM size.

In sum, the U.S.-China trade tensions and Fed rate hikes will likely generate some undesired effects on regional economies next year. Despite the challenges of the above initiatives, ASEAN countries must collectively pursue them to navigate through the economic headwinds. As time is running out, the authorities must act fast.

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