Box 3.1
Will the economic slowdown of the US and EU affect East Asia?

When the global financial crisis pulled the advanced economies into deep recession in 2009, East Asia was severely hit despite their sound fundamentals(1). But over the past three years, East Asia recovered well while economic growths in the advanced economies are still noticeably below trend. While this seems to suggest that the business cycle synchronisation between East Asia and the advanced economies had weakened, several pieces of evidences indicate that East Asia is still notably exposed to the vicissitudes of the advanced economies. Given the current escalated downside risks facing the US and EU, it is worthwhile to revisit these linkages to shed some light on the growth prospects of East Asia this year.

Fact 1: The US and EU are still important export markets of East Asia

Given the enormous scale of their economies, the US and EU are important export markets of East Asia. The US and EU together still accounted for about 28% of East Asia’s total export value in 2010, though their combined share was already lower than 10 years ago. As such, East Asia’s external trade performances are still directly affected by the import demand in these two economies in a significant way (Chart 1).

![Chart 1: The US and EU still feature prominently in East Asia’s total exports](chart)

Fact 2: East Asia’s export dependence on the US and EU markets when measured in terms of GDP remains very large

The large external sector of East Asia means that a sharp swing in their exports could cause notable fluctuations in the GDP growth of East Asia. To further illustrate the economic significance of East Asia’s export dependence on the advanced economies, it is worth noting that total exports to the US and EU represented about 8% of East Asia’s GDP in 2010. Although this ratio had diminished from about 11% before the global financial crisis, the pressure it could exert on East Asia remains sizeable (Chart 1).

(1) In this Box, East Asia refers to the following 10 economies: the Mainland, Japan, Hong Kong, Taiwan, South Korea, Singapore, Indonesia, Thailand, Malaysia and the Philippines.
Box 3.1 (Cont’d)

Fact 3: East Asia as intricate production supply chains

While intra-regional exports surged over the past decade and now account for about half of East Asia’s total exports, a large part of these intra-regional exports comprise trade in raw materials (roughly about 40% in 2010)(2). This is a manifestation of the intricate production supply network within Asia, propelled by globalisation and trade liberalisation over the past two decades. It is impossible to trace where these raw materials would go after rounds of processing, but the close relationship between growth rates of intra-regional exports of raw materials and East Asia’s total exports to the US and EU provided a clue (Chart 2). This, together with the fact that the US and EU are the major export destinations of East Asia, suggests that a significant share of intra-regional exports of raw materials is related to East Asia’s eventual exports to the US and EU, and in turn the final consumption demand in these two markets. Indeed, when the demand in the advanced economies shrank in 2009, East Asia’s exports to the US and EU fell by more than 20% and intra-regional exports of raw materials also fell sharply by around 15%.

Chart 2: Intra-regional exports of raw materials conceivably hinge on eventual exports to the US and EU

As such, the direct and indirect economic influences of the US and EU on East Asia are still substantial. In this connection, if both the US and EU economies sink into a recession, East Asia would still be severely affected. This relationship had become evident again since the second quarter of 2011. When the demand in the US and EU weakened, not only did East Asia’s direct exports to these two markets slow, intra-regional trade and industrial production in the region also trended down generally. In short, East Asia is yet to decouple from the advanced economies and remains closely tied to the vicissitudes of the US and EU markets in the near term. The growth rebalancing process towards more domestic demand-led growth in East Asia is likely to be more a long term goal that will take time to accomplish.

(2) East Asia’s exports by end-use figures were crudely estimated based on the UN Comtrade database.