EUROMONEY SEMINARS

TRADE FINANCE

8th Annual

Structured Trade and Export Finance Asia-Pacific Conference

The Ongoing Crisis and Asia's Trade: What to Expect?

Alicia García-Herrero, BBVA

Chief Economist for Emerging Markets

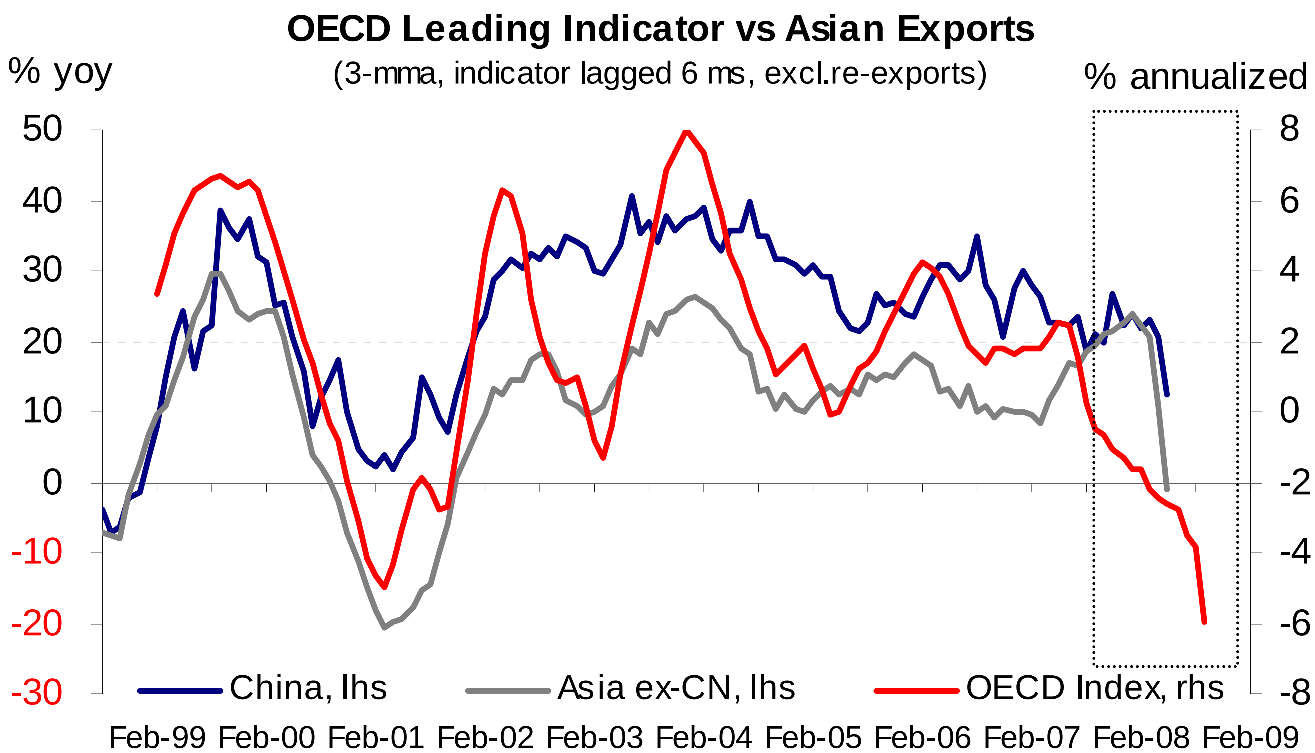
BBVA

February 2009

Contents

- ***What is happening with Asian exports?***
- Is it due to lack of external demand or to financing constraints?
- Consequences for intraregional trade
- Biggest players’ situation: China and India

What is happening with Asian exports?



Source: Thomson Financial, ERD BBVA

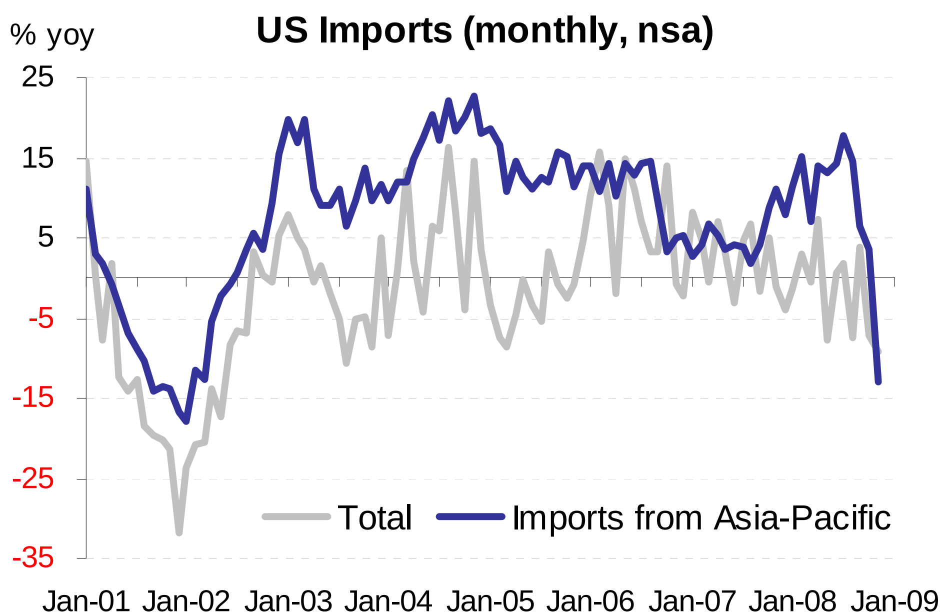
Nominal exports plunged in the last quarter of 2008, while leading indicators in developed countries point to a deterioration at least as sharp as in the 2001 tech bubble crisis

BBVA

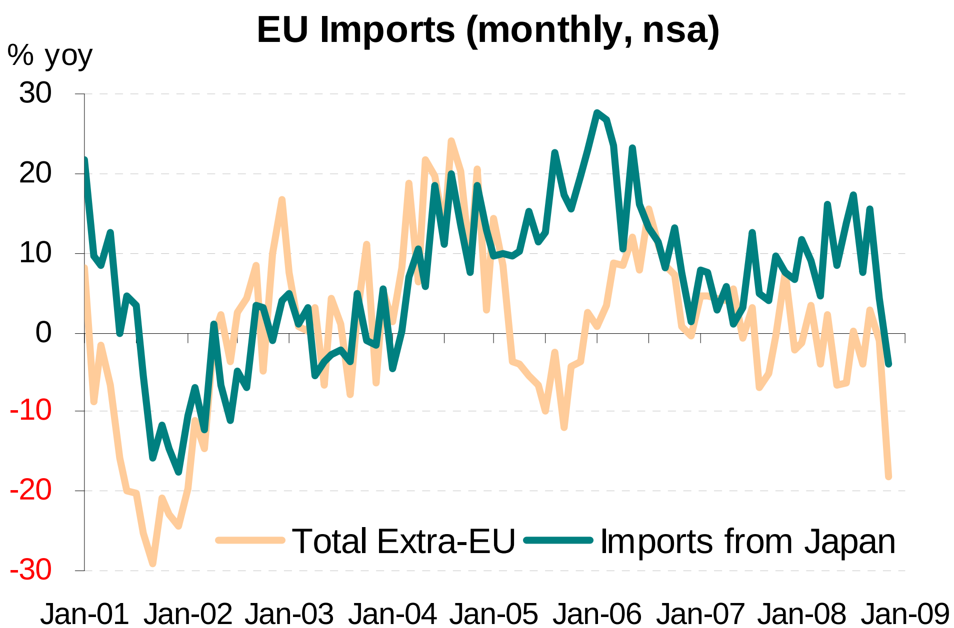
Contents

- What is happening with Asian exports?
- ***Is it due to lack of external demand or to financing constraints?***
- Consequences for intraregional trade
- Biggest players’ situation: China and India

Lack of external demand?



Source: Thomson Financial, ERD BBVA



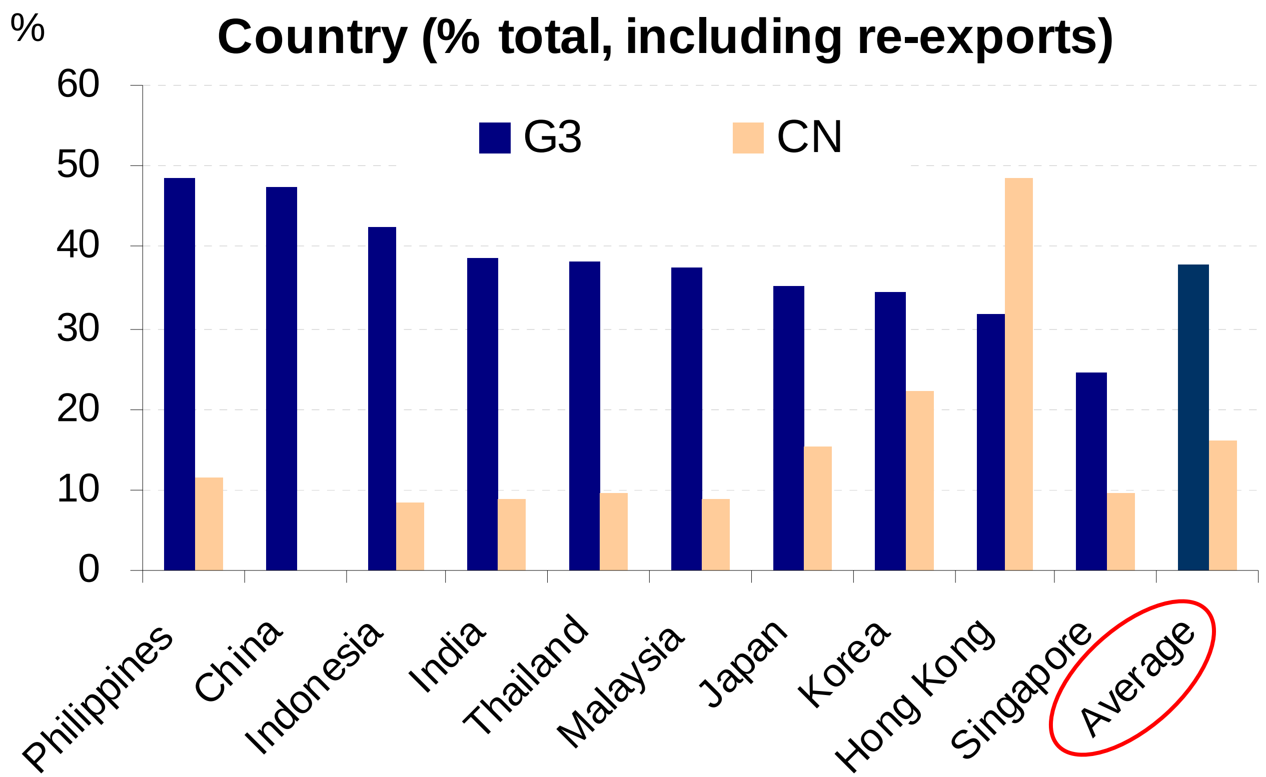
Source: Thomson Financial, ERD BBVA

Demand from the developed economies contracted, in some cases as in the US, the decline of imports from Asia-Pacific outpaced overall imports

BBVA

Which country is most exposed in Asia?

Asia: Share of Exports to China vs G-3 By Country (% total, including re-exports)

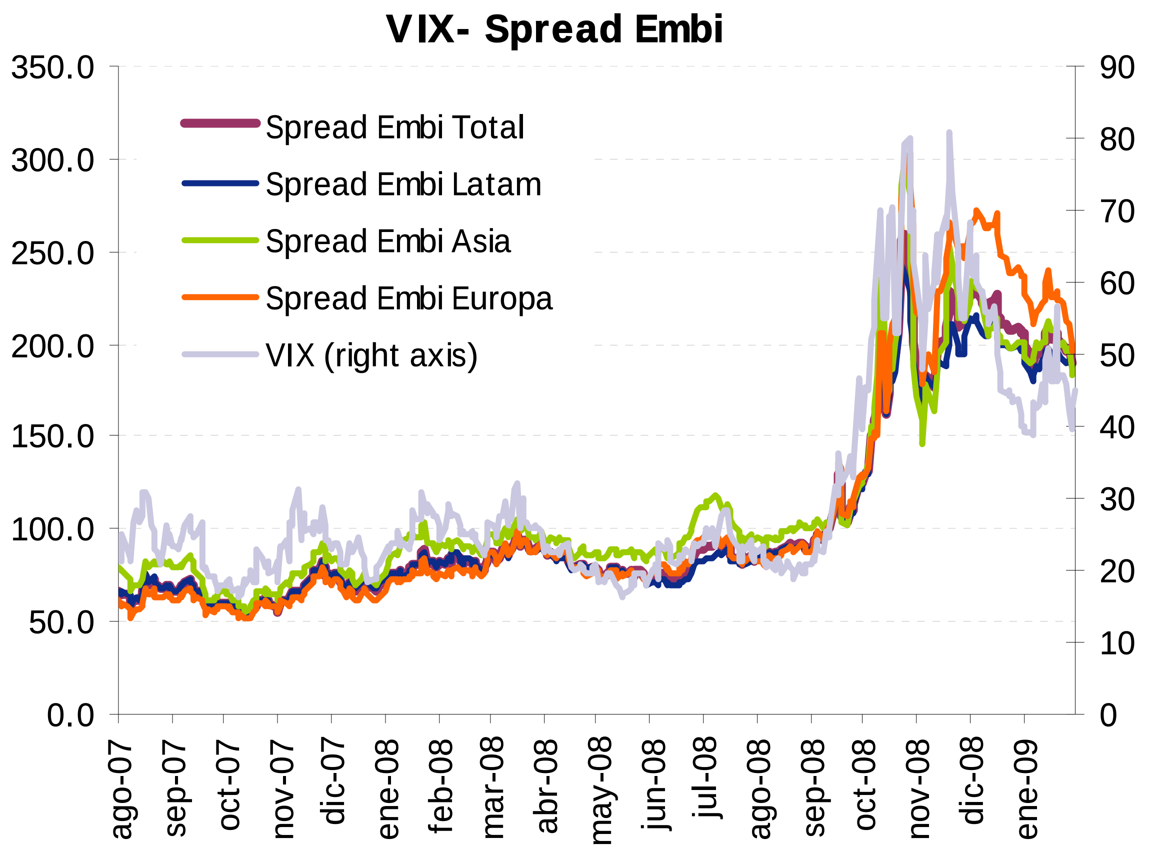


Source: IMF DOTS (2007), ERD BBVA

China has been gaining share in Asian exports but direct exports to the G-3 economies still represents, in average, 40% of total exports

BBVA

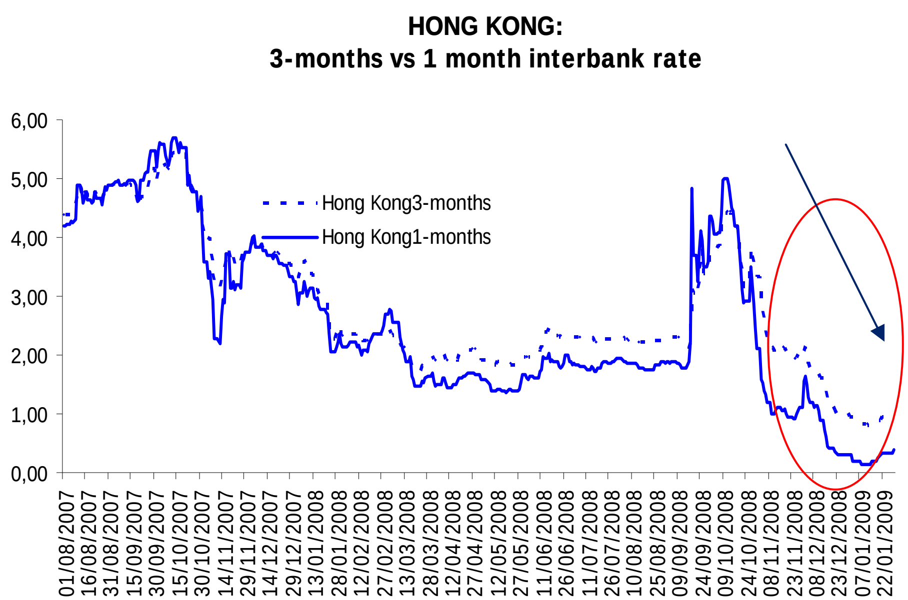
Financing constraints: from the decoupling dream to contagion

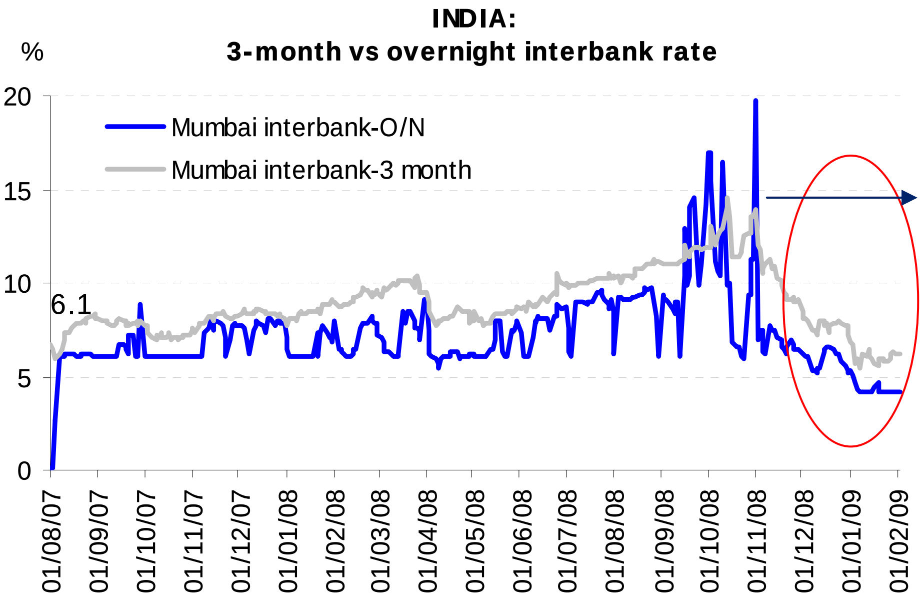


Source: Datastream

BBVA

Credit crunch in Asia?





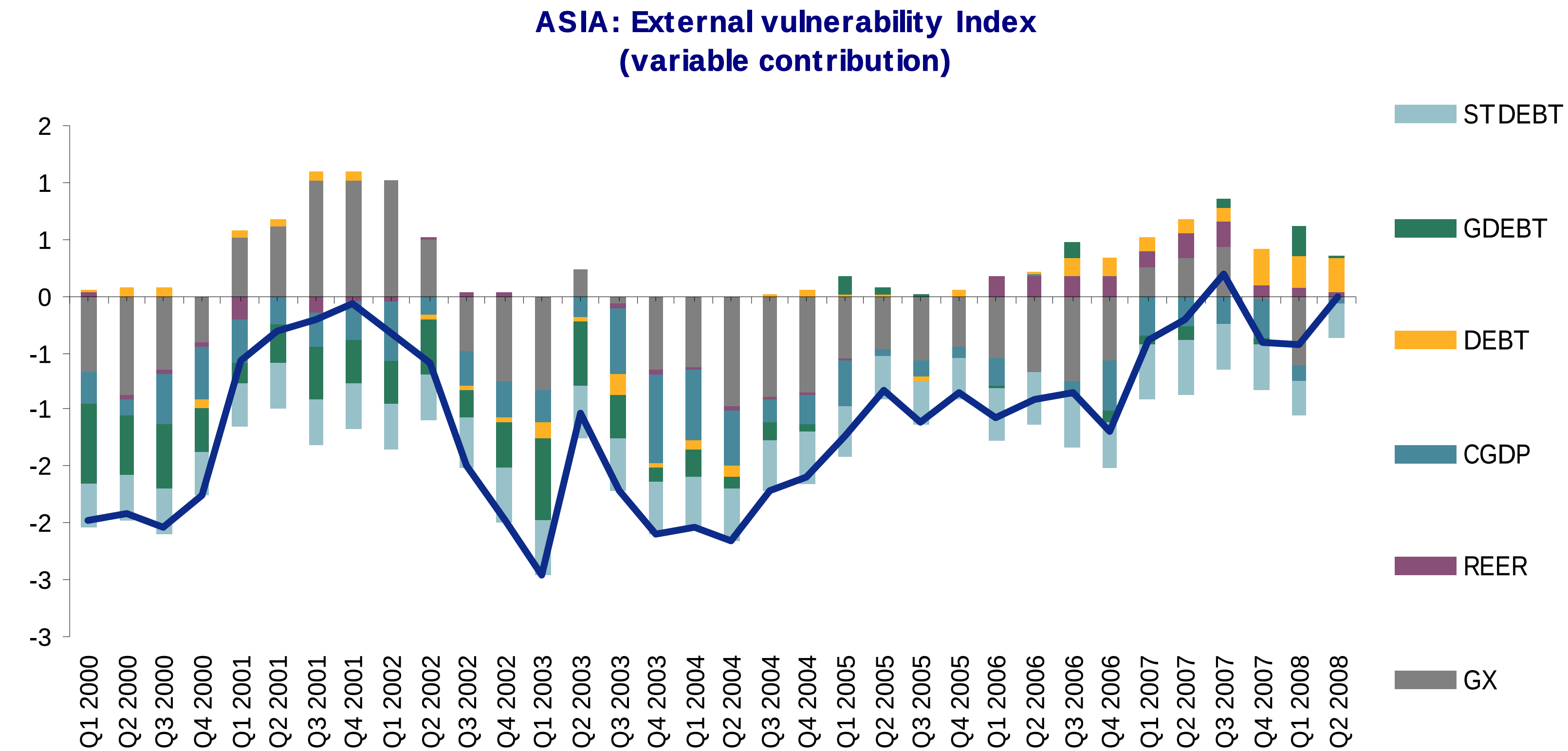
Source: Thomson Financial, ERD BBVA

Sharp increases in the spreads in September-October. In most cases they have come down but dollar liquidity remains tight.

BBVA

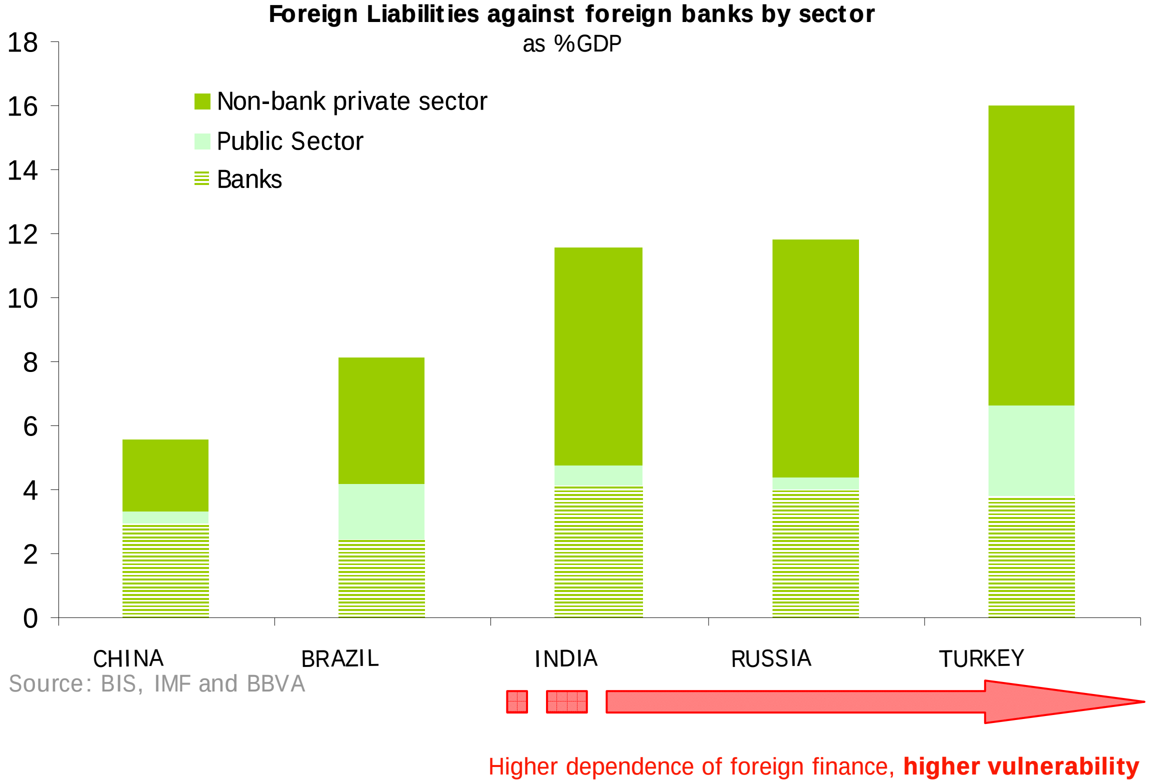
8th Annual Structured Trade and Export Finance Asia-Pacific Conference

External financing constraints?



Source: IMF, BIS, IFS and BBVA calculations.

What to expect?



Source: BIS, IMF and BBVA

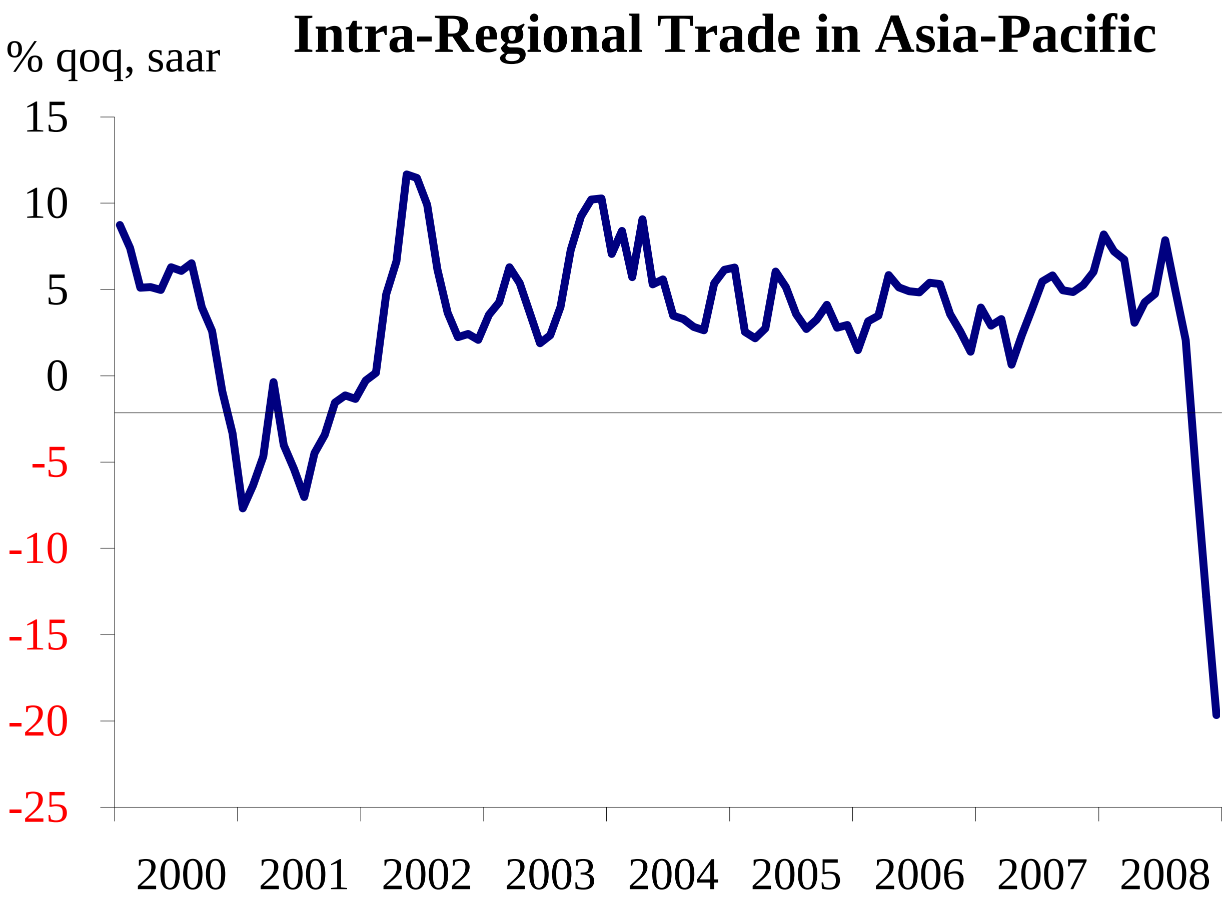
Not only the banking system, but higher levels of external corporate funding is a growing source of concern in some emerging markets.

BBVA

Contents

- What is happening with Asian exports?
- Is it due to lack of external demand or to financing constraints?
- **Consequences for intraregional trade**
- Biggest players' situation: China and India

Intra-regional trade is plummeting



Source: ERD BBVA estimates

BBVA

Contents

- What is happening with Asian exports?
- Is it due to lack of external demand or to financing constraints?
- Consequences for intraregional trade
- ***Biggest players' situation: China and India***

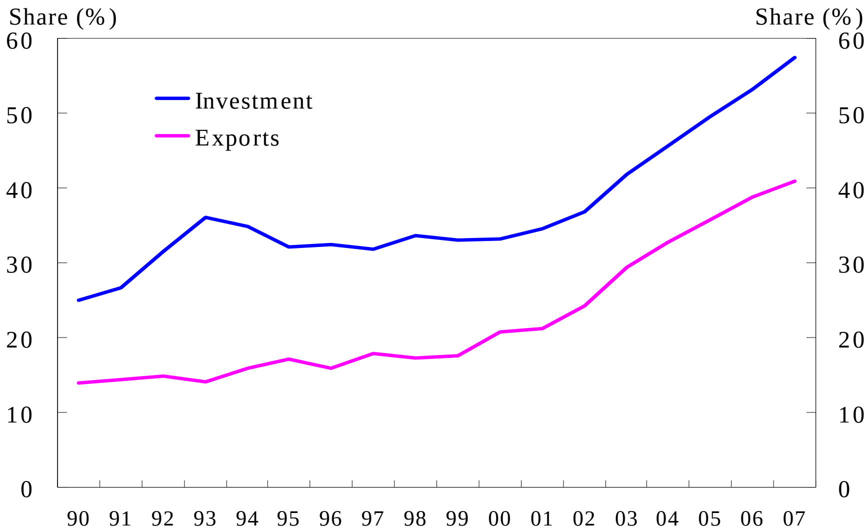
8th Annual Structured Trade and Export Finance Asia-Pacific Conference

EUROMONEY SEMINARS

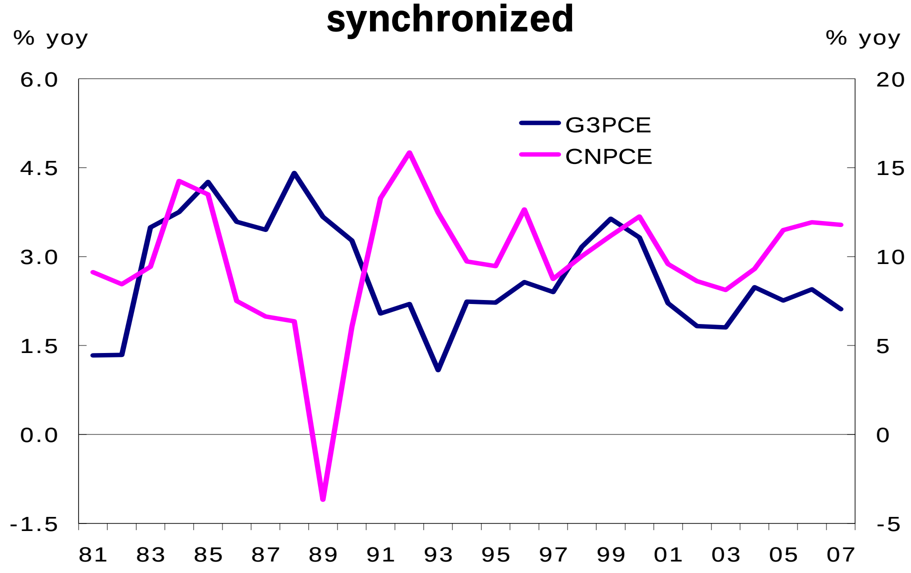
TRADE FINANCE

China: External Demand Dependence

China's investment and export share



Growth in private consumption more synchronized



Source: ERD BBVA

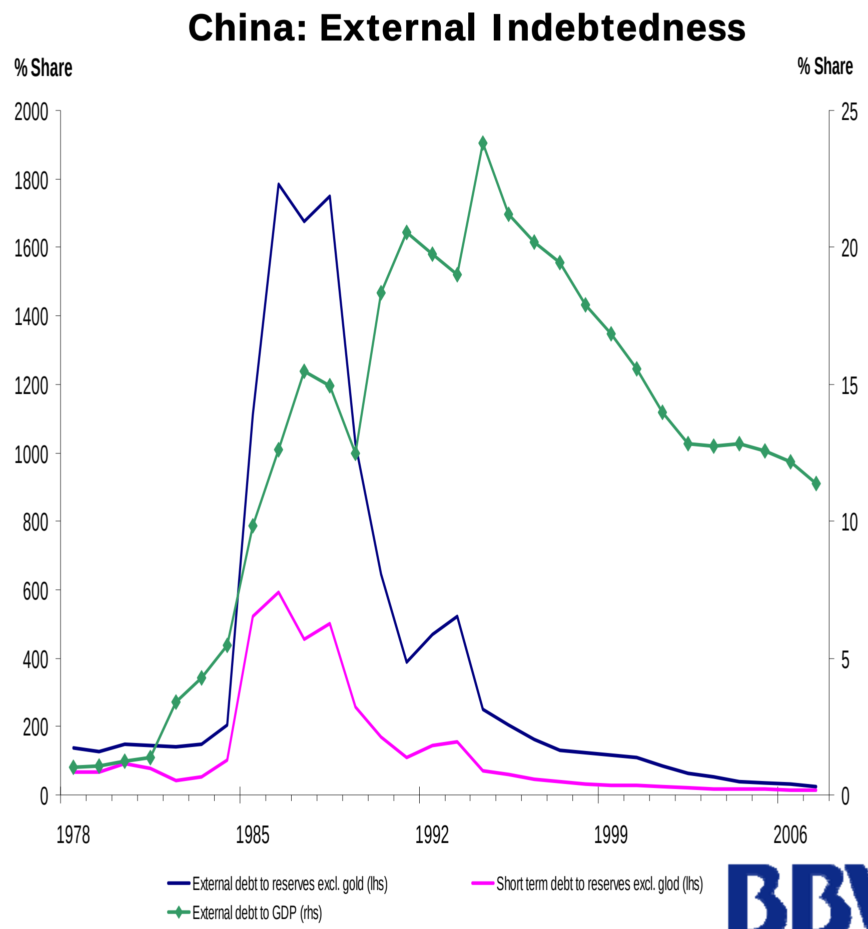
BBVA

China: but not dependent on external finance

China is clearly the soundest of all countries studied given its massive reserves and the very low levels of internal and external debt.

The latest IMF figures suggest total external debt and short term debt as shares of FX reserves is at 24% and 13%, respectively.

Cross-border liabilities from international banks are also very low. The BIS statistics show that China's short-term cross-border bank loans (maturity within one year) are less than 9% of its FX reserves in June 2008.



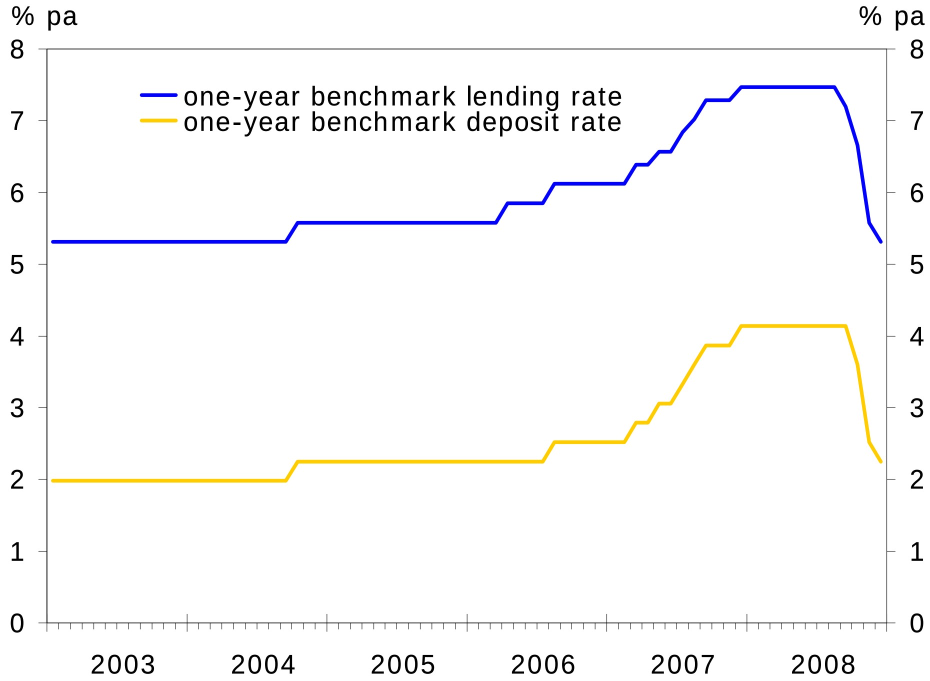
BBVA

China: Ample room for monetary stimulus

The monetary policy has become aggressively accommodative. The PBOC has cut the one-year benchmark lending and deposit rate by 135 basis points (27bps*5) and the required reserve ratio (RRR) to 14% for 6 largest banks was lowered to 14%, from peak at 17.5% (0.5 p.p. for smaller banks)

More room exists to cut rates/RRR further

Benchmark Interest Rates



Source: ERD BBVA

China: Huge fiscal stimulus

Table B4.1: The RMB 4 trillion fiscal stimulus package (USD 586 billion)

	RMB billion	Percentag
Affordable housing for low income population	280	(7%)
Rural infrastructure facilities and programs to boost rural income	370	(9%)
Investment in transportation network	1,800	(45%)
Investment on medical services, culture and education	40	(1%)
Spending on ecology protection	350	(9%)
Technical innovation and economic restructure	160	(4%)
Sichuan post-earthquake reconstruction	1,000	(25%)
Total	**4,000**	**(100%)**

Source: State council, China.

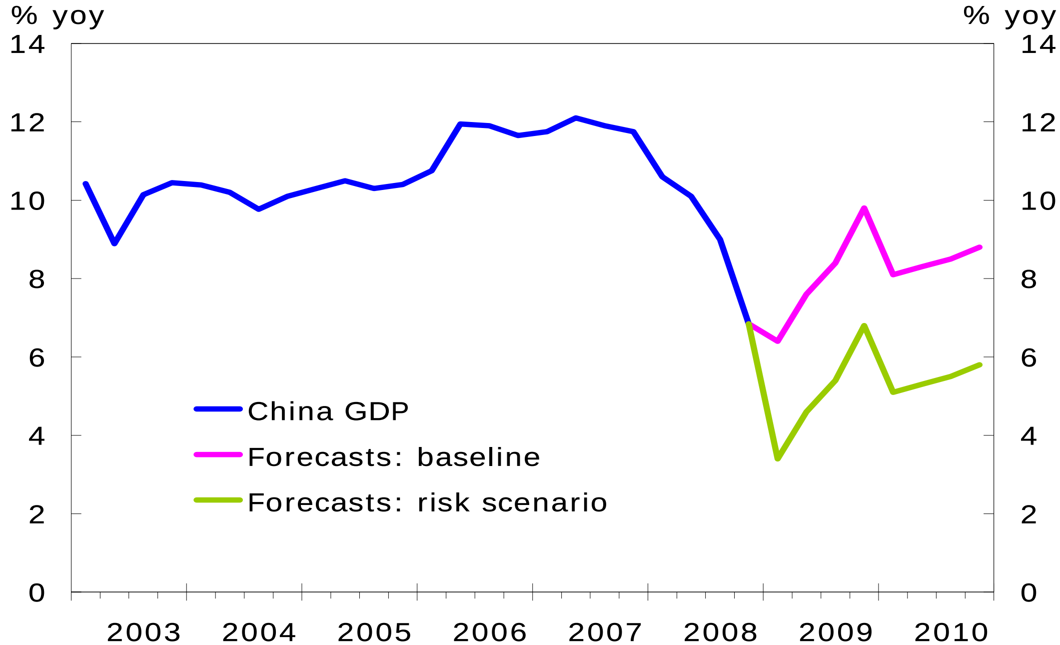
The fiscal program (16% of GDP, to be distributed between 2009 & 2010) entails a comprehensive and, a priori, effective package: it is timely, generous, and sustainable. We estimate an elasticity of 0.6%.

It is designed to improve the transport network and to rebuild the areas hit by the recent earthquake (about 70% of the funds). Thus, part of the program also aims to improve income distribution.

BBVA

Growth with be maintained a a good 8%

China's GDP forecasts



Source: ERD BBVA

Very favorable fiscal and monetary condition, strong external positions and the still relatively controlled economy will help China achieve 8.1 % growth in 2009.

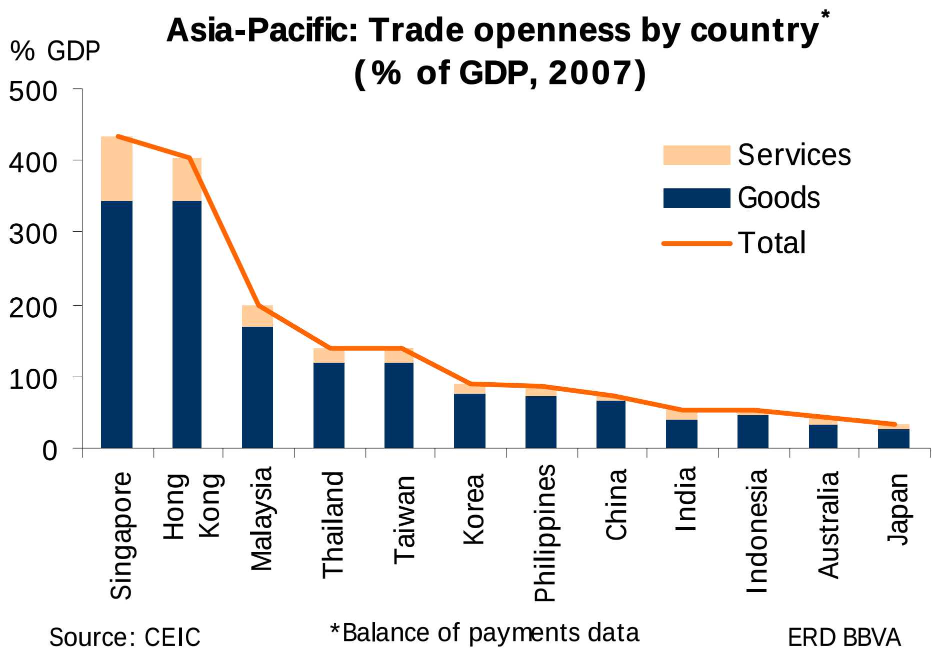
BBVA

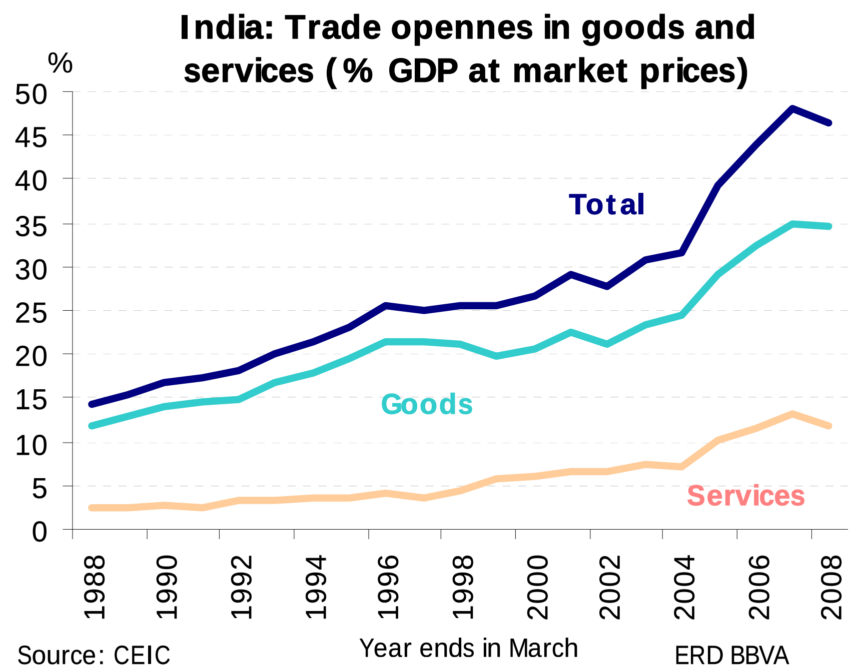
However there are important risks to such benign scenario

Growth could be as low as 5 - 5,5% in 2009 and 2010 in the case of:

- **ineffective and poorly executed fiscal stimulus**
- **sharper contraction in G3 activity**
- **Worsening of the financial crisis worldwide**

India: More external demand dependence than generally thought

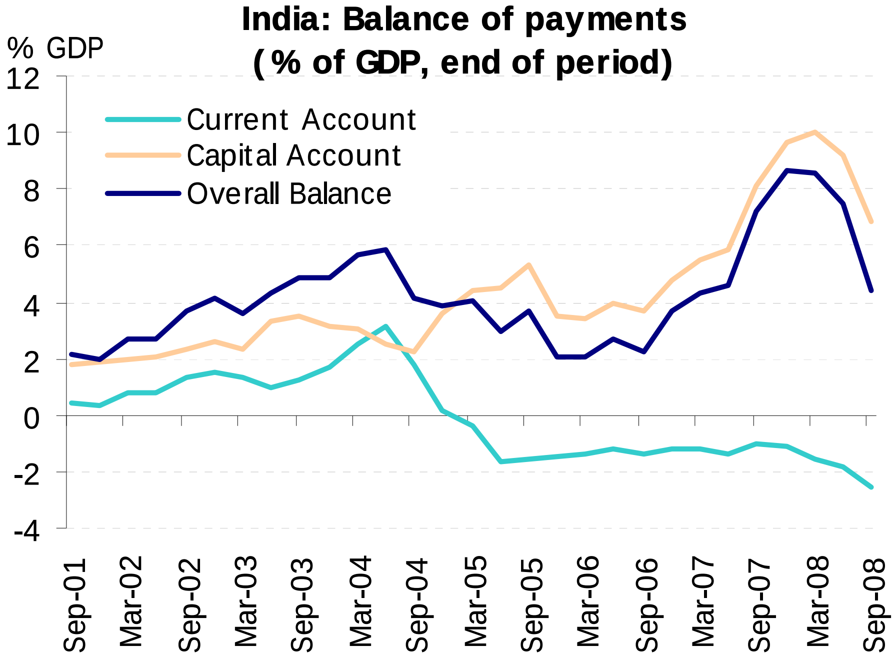


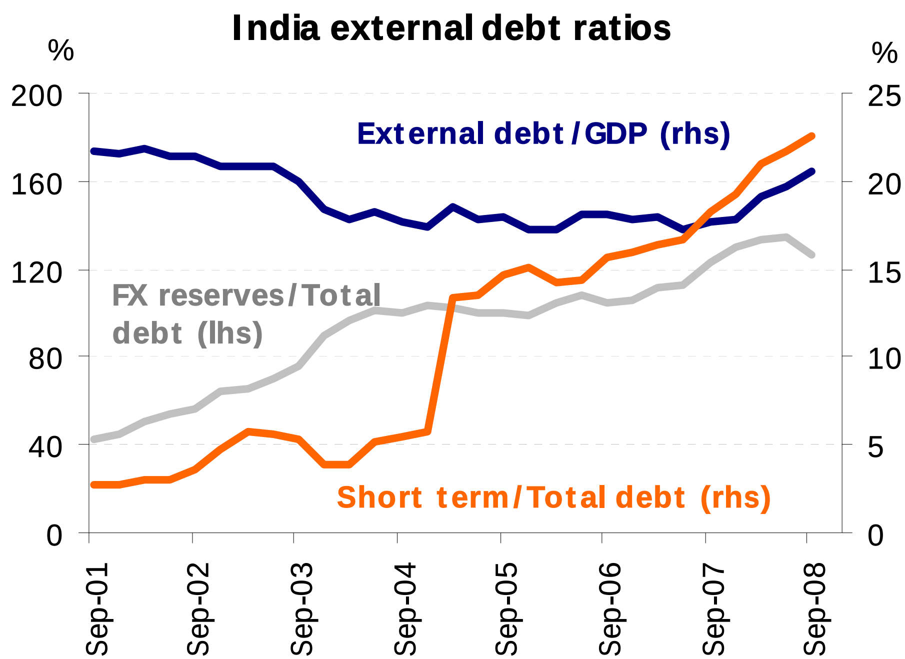


In view of the external orientation of the global crisis, India is relatively closed and thus, in better position than China (or MX) to cope with the external slowdown. However, India's trade openness has been progressively gaining higher importance, particularly, in recent years.

BBVA

India: Weak external Position

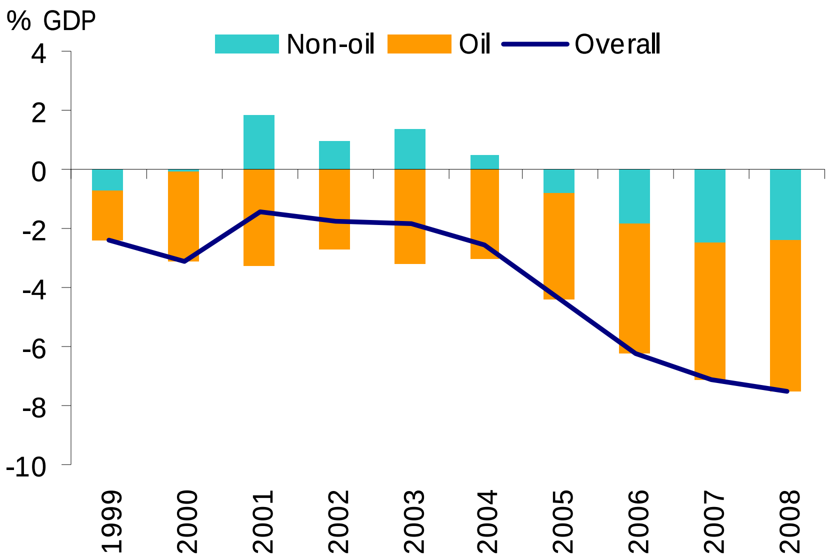




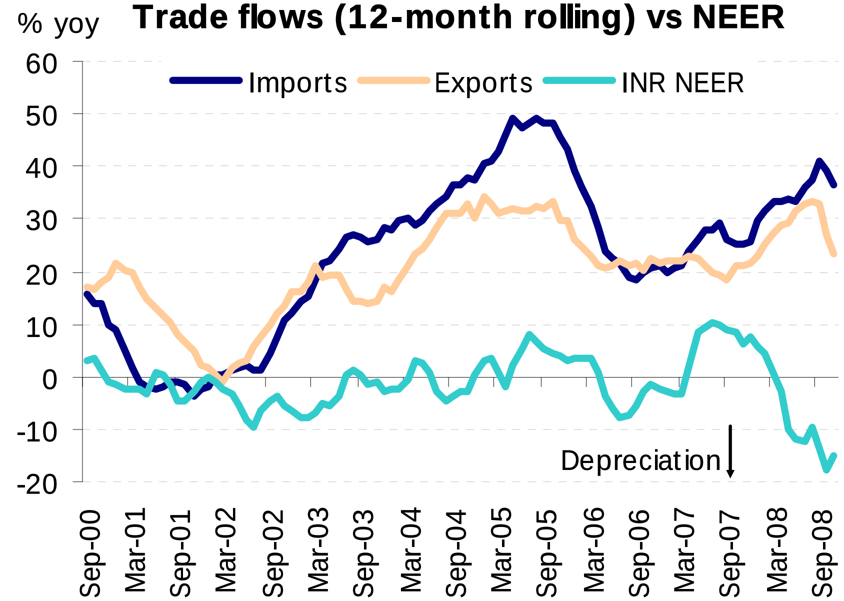
India's external position remains weak. Notwithstanding US$242 bn in FX reserves, India is still a net international debtor (IIP) that owes the world ~US$50 bn (end-June 2008). In addition, India's build up of reserves mainly stems from portfolio flows instead of from current account surpluses.

BBVA

India: Worsening trade balance to worrisome levels



Source: CEIC ERD BBVA

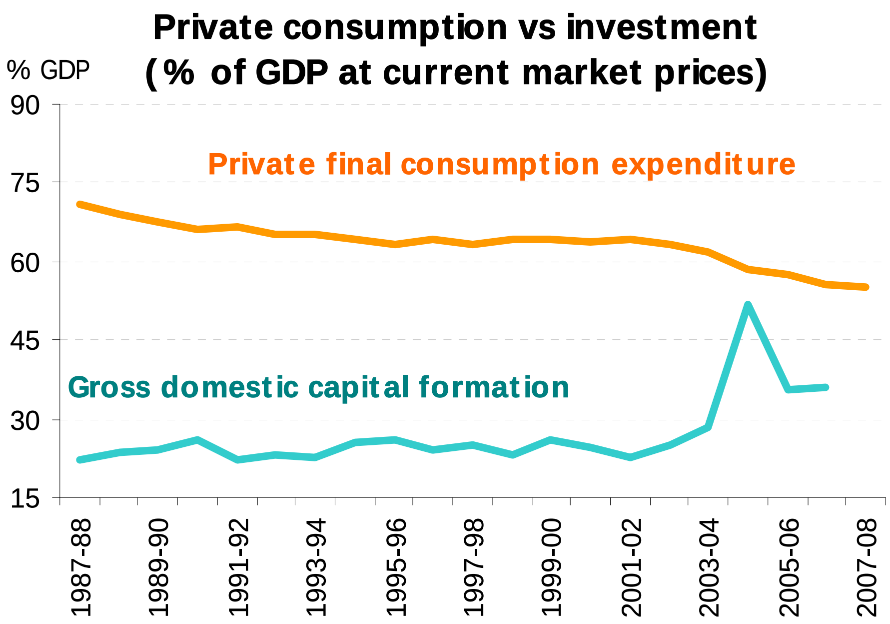


Source: CEIC ERD BBVA

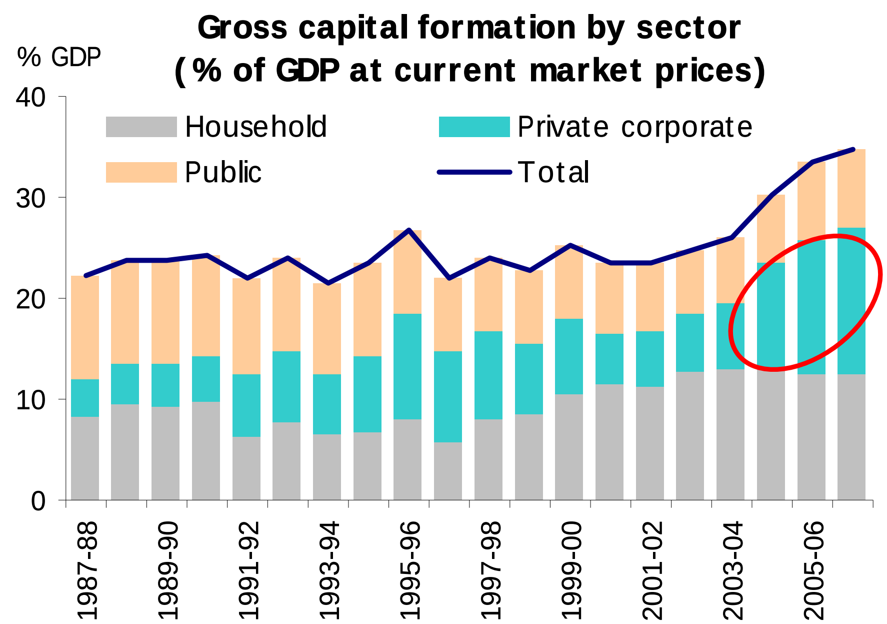
Exports momentum is slowing down at a higher pace than imports. This is at odds with the sharp fall in oil prices. Going forward, there is a risk of trade deficit ballooning and increasing pressures on the current account in case the weakening of the rupee vis-à-vis other currencies fails to lift up exports due to lack of external demand while imported good prices rise.

BBVA

India: Investment may have a financing problem



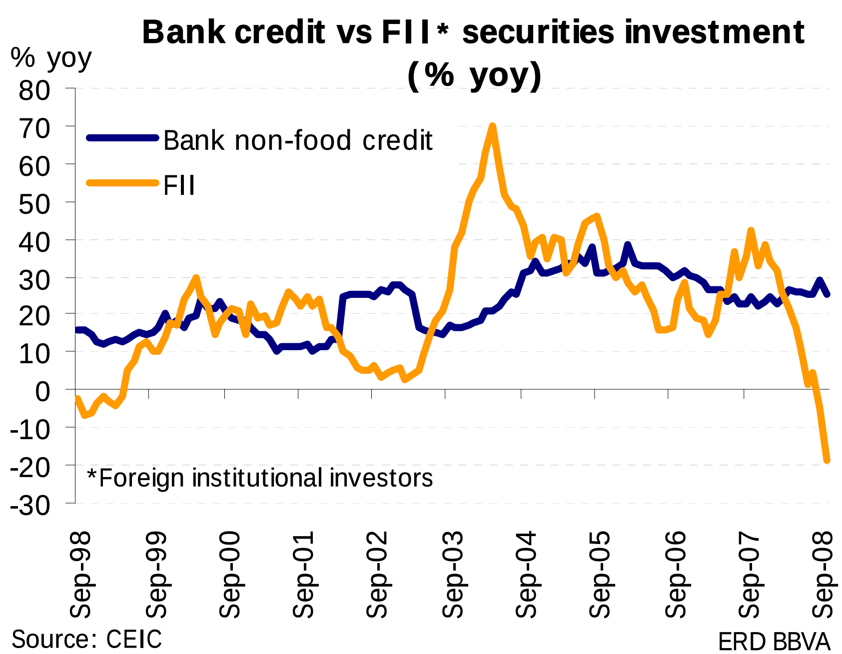
Source: Reserve Bank of India ERD BBVA

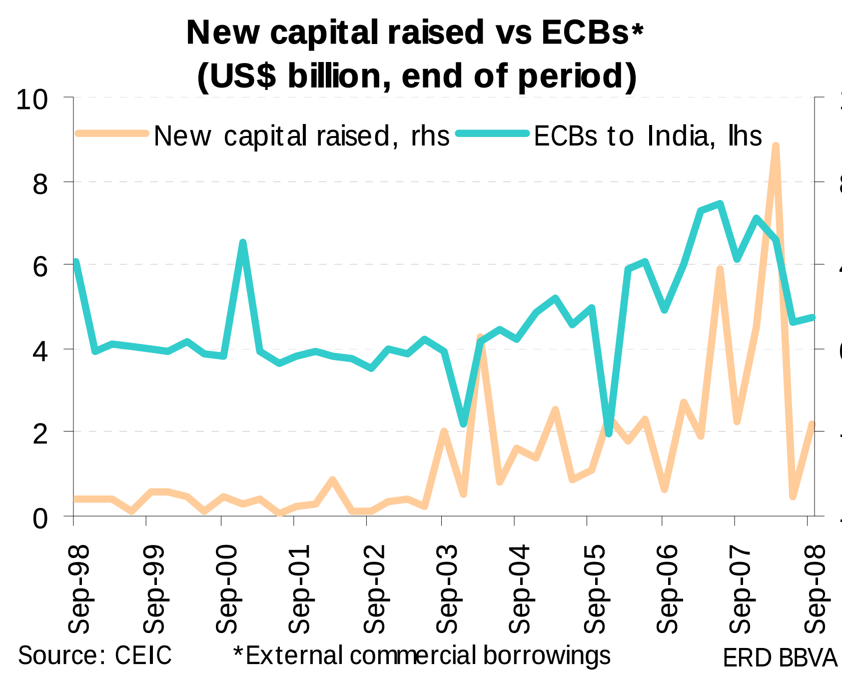


Source: National statistics ERD BBVA

India's industry will bear the brunt of the slowdown. Corporate investments such as capex and infrastructure projects are dependent on international finance due to lack of domestic sources of long-tenor funding (non-significant corporate debt market and no development finance institution).

BBVA

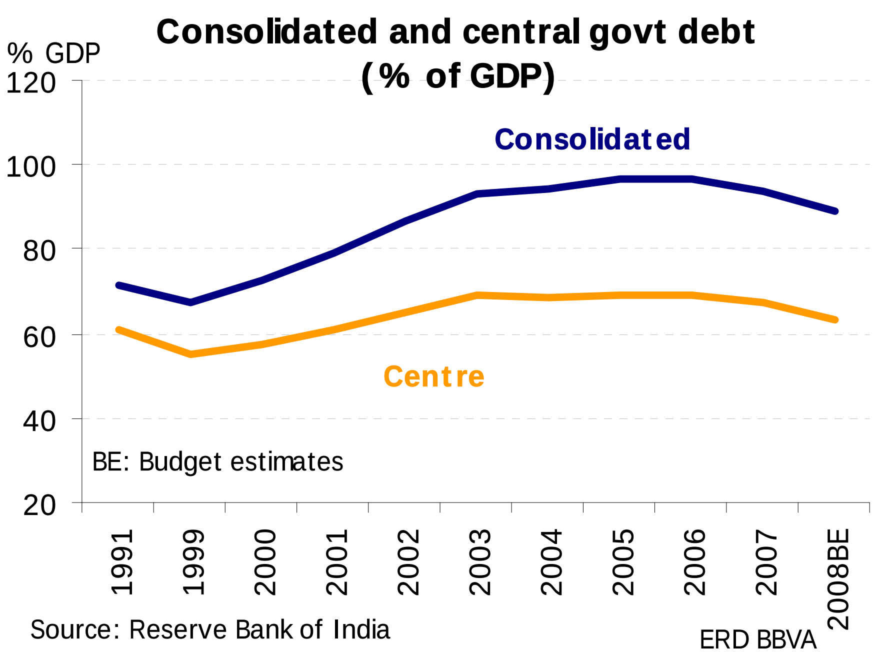


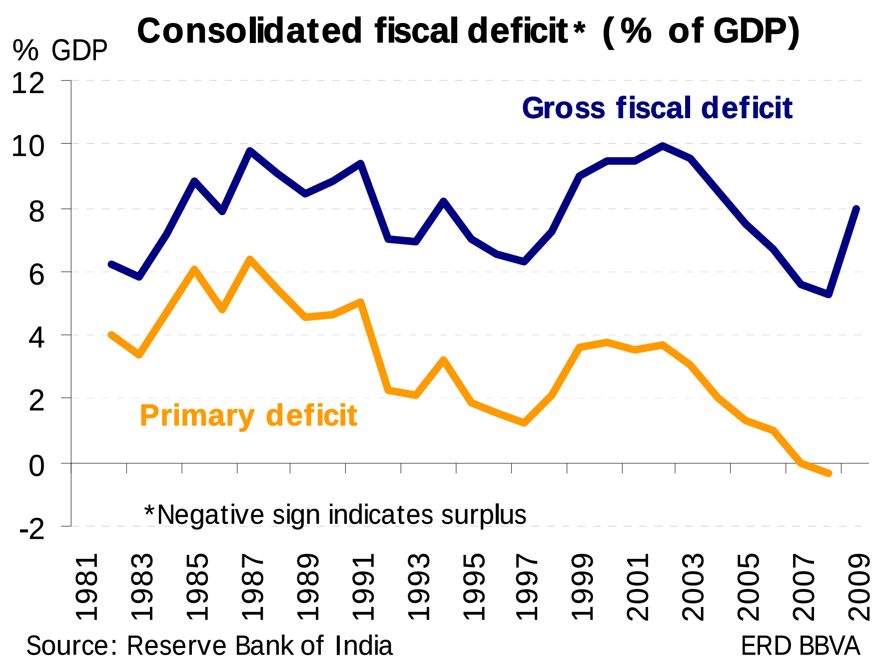


Apart from bank loans, major sources of funding for Indian corporates (foreign institutional investments in IPOs, external commercial borrowings and equity issuances) have now dried up and are unlikely to return in the near term.

BBVA

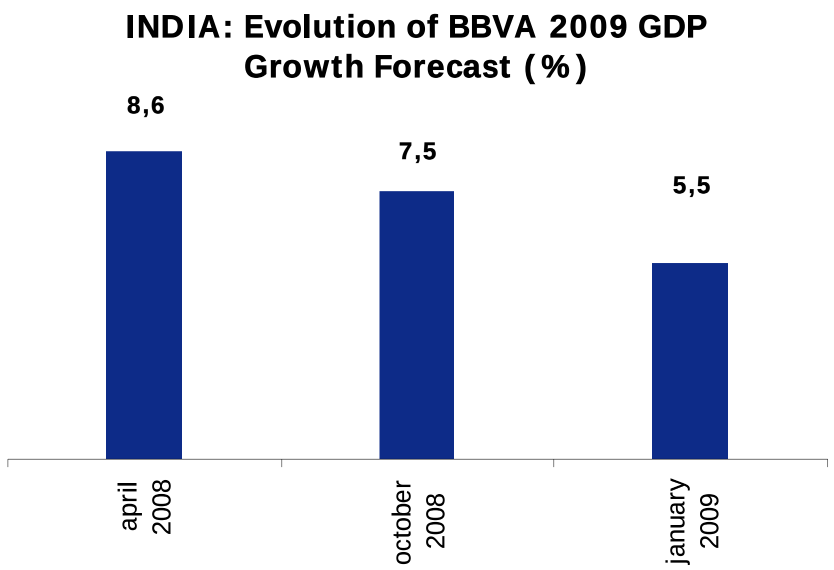
India: Public Finances are worsening





Despite the deficit reduction in the last few years, the progress is unwinding and with high levels of public debt, they leave no fiscal room to maneuver. Budget deficit, including issuances of oil and fertiliser bonds, has been revised up to 8% GDP from 4.6% in FY2009.

Our projections are gloomier but still good performance



Source: BBVA

Source: WEO and BBVA

All things considered, we have revised downward our GDP growth forecast for 2009 (5.5% baseline/4% risk), with the balance of risks on the downside

BBVA

What to expect for China and India?

A closer view on the dimensions of the crisis and perspectives in :

- **China** is the least vulnerable country in Asia due to strong international reserves, high current account surpluses, very low external indebtedness and ample room for fiscal and monetary policies. The slowdown in the yuan appreciation should help to support the export activities but protectionism in developed economies is a risk.

- **India** is more vulnerable. The credit squeeze is affecting the corporate sector investment plans, mostly funded with external credit. Unlike Furthermore, there no room for fiscal or monetary action. Although will remain clearly above world average (even that of the emerging world), a real risk in India is that of a sovereign rating downgrade due to the country's rising fiscal and trade deficits

Thank you for your attention

BBVA