

Voice of Asia

Edition 8
November 2020



Deloitte.
Insights

Our Voice of Asia series brings to life the challenges and opportunities facing the region today and tomorrow. Voice of Asia is the result of significant collaboration across the Deloitte Asia Pacific and Global Network.

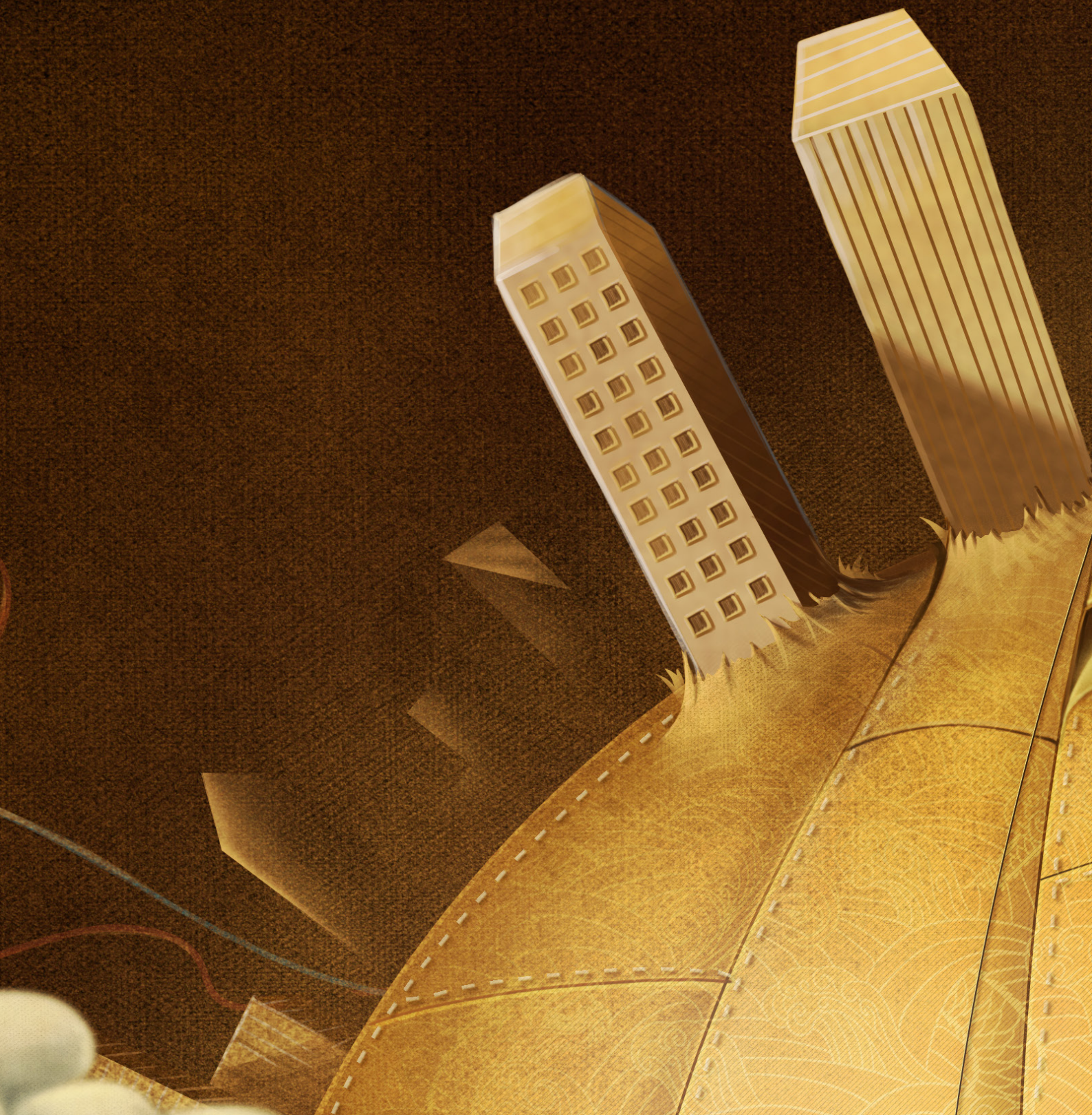
Contents

Three Themes Driving the Outlook: Rehabilitation, rectification, and reforms | 2

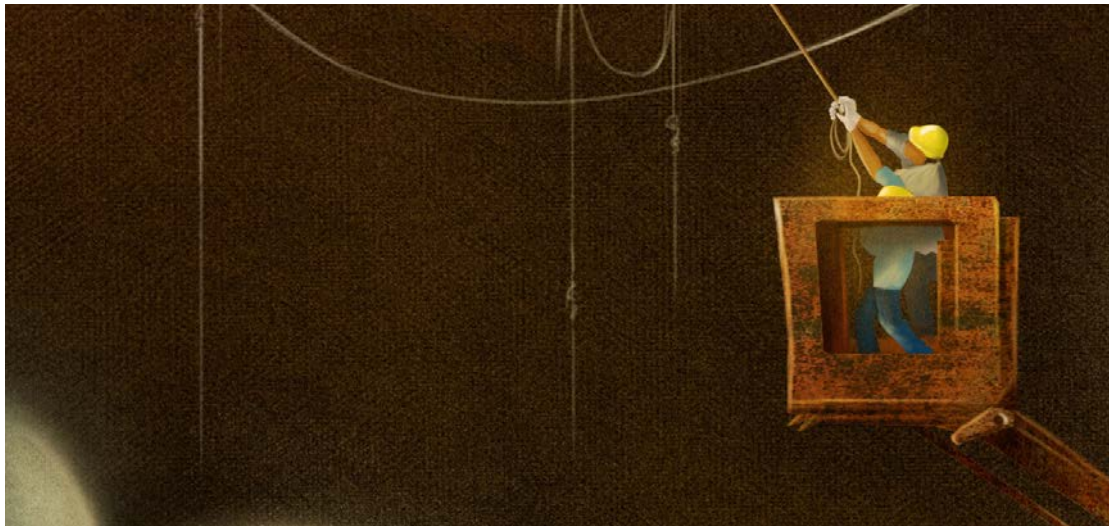
The Next Wave: Emerging digital life in South and Southeast Asia | 27

Acknowledgements | 39

Three Themes Driving the Outlook: Rehabilitation, rectification, and reforms



Introduction



THE year 2020 will undoubtedly linger long in our collective memories as an annus horribilis of extraordinary proportions. But all bad things eventually pass and so will COVID-19. As we move into 2021, the Asia-Pacific region can look forward to a better year as the pandemic is brought under control and economic activity gradually revives.

We believe three forces will help to shape the regional economic landscape in the coming year:

First, economies will undergo a period of rehabilitation as governments use every policy tool available to get their economies back on track and corporations make the repairs needed to resume normal operations.

Second, we are likely to see a process of rectification across the region. Some economies outperformed others during this crisis, a testament to their better fundamentals. The crisis cast a harsh light on those countries which had neglected getting important basics right. Now, there is a greater sense of urgency to address weaknesses that reduced countries' capacity to absorb and bounce back as fast as possible from unexpected shocks like the pandemic.

Third, several countries in the region are also likely to introduce additional fundamental reforms, directed at producing a new model for economic management and development, so as to adapt to the substantial changes that the post-pandemic world will bring.

Rehabilitation — the return to a more normal economic track

Key assumptions for the global environment that the Asia-Pacific will face

In thinking about the economic trajectory in 2021, there are many areas of uncertainty that require us to make some assumptions:

- We assume that improved clinical management of COVID-19 and the availability of more effective medications will mitigate the health-related risks of the pandemic. Thus, even before a vaccine is developed and widely distributed, the threat posed by the virus will diminish. By 2021, hospital capacity should increase, as governments implement protocols for testing, isolating and monitoring potentially infected people. If these assumptions hold, then the economic dangers posed by further waves of infection can be contained: There should be fewer alarming surges in infections, placing healthcare systems in a better position to handle new waves of infection.
- Consequently, we believe all this will help generate more confidence among policymakers to cut back on restrictions, among consumers to resume more of their normal activities, and among businesses to overcome their hesitation to hire, invest in new technology and increase capacity. Of course, some sectors could take longer to recover — travel and tourism related activities, for instance, as well as activities that bring large numbers of people together in close proximity such as sports events, conventions and the like. However, even in these areas, we sense policymakers are trying to find ways to resume normal business: Travel bubbles are being created between countries that have more successfully contained the pandemic, thus allowing some degree of recovery in air travel, hotels and other tourism-related industries.
- These assumptions lead us to believe that the global economy will have returned to its pre-pandemic level of output by the end of 2021: The developed economies such as the United States, Europe, and Japan, are likely to be modestly below that level and emerging economies led by China, South Korea, and Taiwan, slightly above it. Australia should also have returned to pre-pandemic output levels by the end of 2021, with New Zealand would lagging behind by a few months.
- Even with travel bubbles and the like, some sectors of economic activity such as travel and tourism, plus affiliated activities, will take years to return to their pre-pandemic levels of output. Nevertheless, other sectors will see better opportunities to expand materially beyond their pre-pandemic levels, helping to offset that damage. These should include infrastructure spending, investment in IT goods and services, and spending on healthcare systems, pharmaceuticals, and equipment. Increased super-power competition should also lead to more money being directed to research and development, and we also expect stepped-up defence spending.

- While world trade growth was undermined by increased protectionism, the US-China trade war in particular, we assume there will not be a material hardening of protectionism. We offer an expanded analysis of the impact of the recently concluded American presidential and congressional elections in a separate section below. The basic assumption is that big powers such as the US and China will avoid a descent into greater protectionism, though technological bifurcation remains a risk.

Expect continued and expansive policy support to reduce downside risks

With the above in mind, we believe that the key element of rehabilitation will be policy efforts to spur the regional economies to return to a normal growth trajectory. In general, our view is that:

- Monetary policies will remain highly supportive of economic activity, with scope for more rate cuts in some countries such as India and Indonesia. In some jurisdictions, rate cuts might not be employed but there will be a greater willingness to experiment with unconventional policies such as yield curve control and forward guidance. The monetary authorities in South Korea and Thailand have shown a willingness to contemplate unconventional policies, including targeted approaches to help borrowers and avoid a liquidity crunch.
- Fiscal support was extraordinarily large during the recent crisis, so it is not a surprise that the level of fiscal support is being reduced as governments in the region remain wary of the longer term risks of raising public sector debt levels. However, governments are aware of the dangers of premature withdrawal of fiscal support. As the recent Malaysian budget for 2021 suggests governments will maintain expansionary fiscal conditions.
- Policymakers are also likely to use other means to mitigate downside risks. For example, moratoria on loan repayments and

other regulatory forbearance will, we believe, be extended where possible. This is already happening, for example, in Malaysia. Government guarantees on loans or other forms of risk sharing will also continue in places such as Singapore, so policy support should not be withdrawn so precipitously as to destabilize the economic recovery.

Given this policy emphasis on rehabilitation, several other factors will determine economic outcomes in the region:

First, is the capacity of the state in two key areas.

- One is the management of the pandemic. In some countries, such as China, the capacity to test, isolate and treat patients on a massive scale is impressive, as is the ability to plan and enforce calibrated lockdowns. In other economies such as Australia, New Zealand, Hong Kong, South Korea, Taiwan, and Singapore, the quality of the healthcare system enables a very low fatality rate, while people have generally been cooperative in efforts to contain the pandemic. The speed of economic recovery will correspond with healthcare capacity and the cooperation of the community.
- The other is in the policy arena. Territories that have greater fiscal and monetary space will eclipse others, since they can continue to extend substantial support to the economy without being severely constrained by issues of debt sustainability or financial markets' lack of confidence in central bank management. This group should include Australia, New Zealand, China, South Korea, Taiwan, Hong Kong, and Singapore. In some countries where fiscal space does exist — such as Thailand — the capacity of the state to effectively implement projects and disburse payments is wanting.

The second determinant of the outlook is the degree of dependence on domestic demand rather than external demand, which will rebound, but fairly slowly. China, India, and Indonesia have large engines of domestic demand that they can turn to if external demand remains patchy.

Third, where countries have to rely on external factors, which of them can leverage the more positive trends in the global economy?

- The technology cycle: We remain upbeat on technology as a driver of export demand throughout the region. There might be some near-term deceleration in tech demand due to transient inventory dynamics. However, the underlying structural story is positive. There are many next-generation technologies on the cusp of taking off. These include artificial intelligence and machine learning, plus all their many applications. That will mean increased silicon content per device. Asian economies that are highly specialized in tech production i.e. South Korea, Taiwan, Singapore, Malaysia, and the Philippines, will be major beneficiaries.
- Reconfiguration of supply chains: The relocation of production out of China to lower-cost destinations began some time ago as China moved up the value chain and costs rose. However, growing American protectionism directed at China, and the prospects of technological bifurcation as the US and China pursue their own technological paths separate from each other, will add to the incentive for producers to leave China. Active government

efforts — such as incentives provided by the Japanese and Taiwanese governments to relocating firms — will also speed up this relocation. We see Vietnam continuing to be a major beneficiary. However, Malaysia and Thailand are also benefitting, and recent reforms in India and Indonesia could also bring some relocation to those countries.

- As foreign direct investment recovers from its sharp plunge this year, we expect a degree of recovery in 2021. The major winners from that, we suspect, will be the larger economies that offer large, scalable markets, such as China, India, and Indonesia, as well as those whose reforms (see below) offer a compelling story of improved returns and greater business opportunities.

The end result will be a fairly good year in 2021

We see economic growth gathering momentum, price pressures remaining largely benign, external imbalances at muted levels, and currencies largely steady, as shown in Table 1:

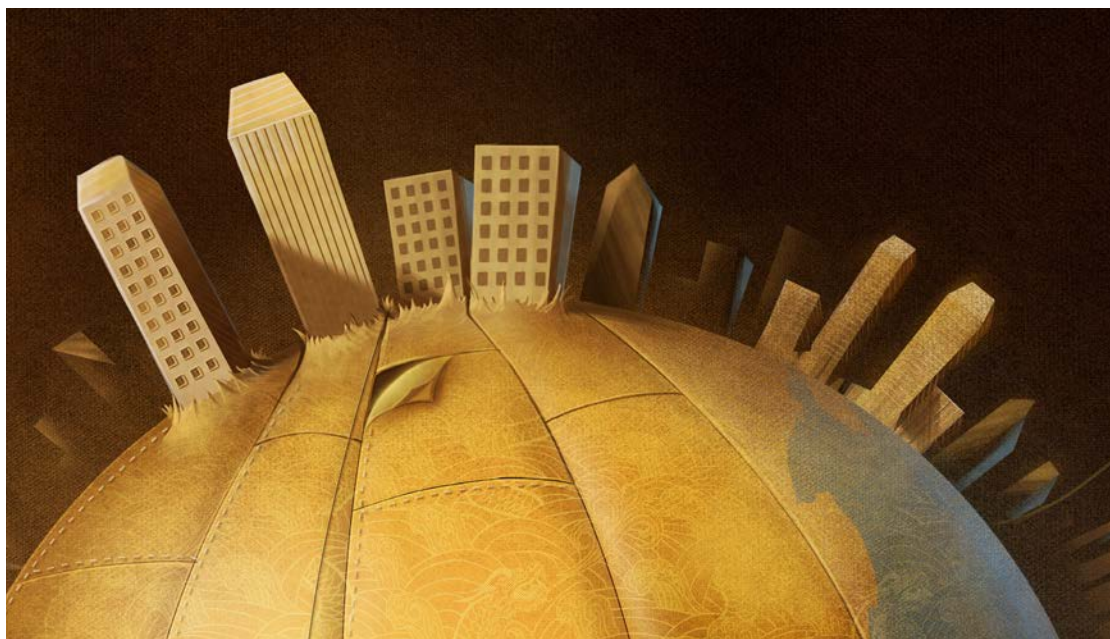


Table 1

Summary of Economic Forecasts for 2021

| Economy | GDP growth (%) | Inflation (%) | Current Account (% of GDP) | Currency (vs USD, end-year) | Benchmark Policy rate (% end year) |
|--------------------|-----------------------|----------------------|-----------------------------------|------------------------------------|---|
| Australia | 3.10 | 1.40 | -0.20 | 0.73 | 0.25 |
| China | 7.50 | 3.00 | 0.50 | 6.95 | 2.00 |
| Hong Kong | 3.00 | 1.40 | 10.50 | 7.75 | NA |
| India | 10.00 | 5.40 | 0.20 | 73.10 | 3.70 |
| Indonesia | 5.60 | 2.40 | -1.80 | 14,100.00 | 3.25 |
| Japan | 1.90 | 0.30 | 3.20 | 103.00 | -0.10 |
| South Korea | 3.00 | 2.20 | 4.00 | 1,125.00 | 0.50 |
| Malaysia | 6.70 | 1.60 | 1.80 | 4.00 | 1.75 |
| New Zealand | 3.80 | 0.80 | -3.60 | 0.68 | -0.50 |
| Philippines | 7.00 | 2.60 | 0.50 | 50.50 | 1.75 |
| Singapore | 5.50 | 0.60 | 16.50 | 1.34 | NA |
| Taiwan | 3.50 | 0.70 | 12.00 | 28.50 | 1.125 |
| Thailand | 5.50 | 3.40 | 5.30 | 30.50 | 0.50 |
| Vietnam | 7.90 | 3.50 | 9.90 | 23,010.00 | 4.00 |

Source: Forecasts prepared by Deloitte Asia and Centennial Asia Advisors

Rectification — building resilience against future shocks

AS explained above, the pandemic exposed weaknesses that need to be rectified in the countries of the region. We expect responses in several areas to address the following gaps:

The first priority will be healthcare systems, which need improvement in several areas:

- The supply of critical equipment for pandemic control, including equipment for intensive care such as ventilators, personal protective equipment for medical staff, and testing kits.
- The adequacy of trained medical personnel including doctors, nurses and others who can quickly deploy to evolving situations. Several countries in the region fall short of the recommendation of the World Health Organization for a doctor-patient ratio of 1:1,000, and need to close this gap.
- Easily accessible medical facilities, especially in rural areas.

The management of debt in each territory is another area where improvements are needed to boost resilience. China has realized this and reined in the growth of debt in the corporate sector. Consumer debt remains high in South Korea,

Thailand, and Malaysia where central banks will renew efforts to contain its growth once the crisis is over.

A third area is infrastructure spending: Economies such as India, Indonesia, and the Philippines raised their spending on infrastructure as a share of economic output. Sadly their efforts were set back as a result of the disruptions brought about by the pandemic. For example, in Indonesia, planning was delayed for the relocation of the country's capital from Jakarta in Java to a location in central Kalimantan. Several large projects such as the Jakarta-Bandung high speed railway have slowed. In Thailand, the disbursement rate for budgeted spending on infrastructure fell to just 37% in 2020, partly as a result of the disruptions caused by COVID-19. As the pandemic comes under control and economic growth resumes, governments across the region will step up infrastructure spending.

Finally, governments have been trying to improve business ecosystems to encourage domestic and foreign investors to increase investment. India and Indonesia have made considerable progress in moving up in the World Bank's ease of doing business rankings. However, progress has stalled over the last couple of years.

Reforms — creating game changers to progress to new development models

A PART from the pandemic, policymakers in Asia-Pacific have had to contend with a series of challenges to their economic development models. The pace of globalization has slowed with the rise of protectionism and US-China trade tensions. New technologies are disrupting whole industries and some may alter the value of competitive advantages that developing economies enjoy, such as cheap unskilled labour. Recent extreme weather events have concentrated minds on the risks posed by climate change.

Several countries in the region are responding to this.

China has probably been the economy with the most comprehensive response. The recent meeting of the Chinese Communist Party's Central Committee approved the outlines of the country's 14th Five Year Plan, which sketch out how China's economic model will adapt to the new world. First, it will step up efforts to strengthen domestic demand, especially consumer spending, as an engine of growth to reduce its dependence on exports. Second, despite confusion about the notion of dual-circulation among investors, China will persist in opening up its economy, including its financial markets. Third, it will substantially ramp up efforts to build technological self-sufficiency in key areas such as semiconductors. Innovation will develop as a much more important driver of economic growth and competitiveness. Fourth, it will raise the priority accorded to sustainability, especially with regard to carbon emissions, by diverting more resources to developing a low-carbon economy.

India has also started to make a bigger effort to implement needed reforms. In recent months, it has passed potentially game-changing reforms that should accelerate the modernization of Indian agriculture. It has also begun reforming its archaic labour market regulations.

Indonesia recently passed an Omnibus Bill in a piece of grand legislative reform of regulations covering a great many sectors. The most transformative is in the labour market, where onerous impositions on companies have been reduced without compromising worker protection. In particular, the burden of compensation for retrenchments — a major bugbear for foreign investors — was reduced. But the Bill went further, addressing other areas of weakness in the investment environment. It will now be easier for companies to secure permits and licenses. The government has reformed its negative investment list, cutting the number of industries where private investment is limited to just six from more than 300 sectors. The often confusing and contradictory issuance of regulations by central versus provincial versus local governments is tackled in the Bill, with the central government now having primacy in issuing such regulations.

These are just three examples from large economies in the region. But even the smaller economies are looking at ways to adapt to a new and possibly more challenging environment. Vietnam, for example, has pursued a strategy of free trade agreements (FTAs) with as many economic partners as possible, with its FTA with the European Union the latest major improvement in the country's economic connectivity.

Conclusion: The near term outlook is modestly good

THE COVID-19 pandemic has caused immense dislocation throughout the world and Asia-Pacific is no exception. It is natural for many of us to feel disheartened about the prospects for 2021. Our analysis, while acknowledging the potential risks, offers reasons why the outcome could be more buoyant. Asia-Pacific economies will benefit from rehabilitation, rectification, and reforms, making for faster and higher quality growth over time.

These factors will also prepare the region for game-changing innovations and disruptive new technologies that are rapidly approaching take-off. We examine one such area of innovation — the digitalization of payments — in some detail in the last section of this report.



Australia: Strong cyclical recovery

AUSTRALIA has done very well to date in battling the coronavirus and its impact on the economy. Even with the second wave in Victoria, Australia has outperformed the world on the virus, and that's allowed outperformance in its economy too.

Rehabilitation

2021 looks challenging: this recession arrived fast but will leave slowly. In particular, families and businesses face a cash crunch between now and March 2021 as wage subsidies and increased support for the unemployed are dialled back, money from early access to personal pension savings dries up, and as mortgage and rent deferrals run out. Hence the importance of new measures such as personal tax cuts to encourage families to spend, and temporary investment incentives and wage subsidies to get firms to spend and hire. At the same time, the health policy response to future outbreaks is to aim for local lockdowns rather than wider metropolitan lockdowns.

Rectification/risk management

Is that enough? With the environment still uncertain and overall fiscal support falling away

through 2021, risk management remains a central task for policymakers. In particular, the policy swing towards incentives will work best if future outbreaks are small and relatively rapidly contained, and if vaccines or good antivirals are relatively effective and arrive soon. There are reasons for hope on both fronts.

Yet much still could go wrong, so if our forecast for calendar 2021 GDP growth of 3.1% is to be achieved, policymakers will need to remain vigilant, and be willing to add renewed income supports if required. Luckily, Australia entered the current crisis with net central government debt at just 19% of GDP, and is projected to exit with net debt at 44% of GDP. Both are low by developed country standards.

Renewal and reforms

What has been harder to achieve has been policy reforms to help Australia navigate the post-crisis world. Although there were welcome moves towards the reform of insolvency laws and the freeing up of regulatory restraints on credit provision, bigger picture reforms have — to date — been mostly consigned to the “too hard” basket. That suggests a strong cyclical recovery is in the offing through 2021, but structural support for those cyclical gains could be harder to achieve.

China: A self-sustaining recovery underway

CHINA'S V-shaped recovery after it conquered the pandemic is nothing short of spectacular. Policymakers have got many things right through early and stringent lockdowns such as that in Wuhan on 23 January. Contact tracing is most effective, even compared to star performers such as South Korea, Singapore, and Germany. China also mounted extraordinary campaigns to test populations for the virus whenever a new cluster of infections was discovered. For example, the mass swab testing campaign for nine million residents within five days in Qingdao.

The government has mobilized resources for business resumption. Strong export performance since Q2 reflects how quickly China was able to resume manufacturing activities and gain from a diversion of export demand from countries whose supply chains remained disrupted. China's almost double-digit export growth in September also suggests global recovery is now gathering pace fast enough to boost China's growth. In addition, the strong recovery has boosted consumer confidence, helped by a buoyant property market.

The US dollar's persistent weakness coupled with interest rate differentials have resulted in capital inflows in 2020 that helped create a capital account surplus of USD37.4 billion over the first three quarters.

With this success behind it, policymakers are likely to focus on improving the quality of growth, first by addressing the uneven recovery between investment and consumption through more efforts to support SMEs and consumers in 2021. PBOC Governor Yi Gang has also pledged to stabilize leverage after China's debt-to-GDP ratio rose in 2020, a clear change in Beijing's policy stance from the past two years, which allowed for gradual increases in leverage to promote growth. Yi's remark also suggests there will not be any large fiscal stimulus. In all likelihood, Beijing is

expected to rely more on the fiscal levers of poverty reduction and social programs, but stay away from large infrastructure projects.

The biggest potential downsides for China are external, mainly deriving from the increased frictions with the US. What started as a trade war has since spilled over to other areas, especially technology. Trade will remain a source of friction – the US trade deficit with China did not narrow over the past two years, virtually ruling out any lowering of tariffs by a future US administration.

Nevertheless, China has found ways to contain this downside risk. Chinese authorities have exercised restraint with the US, for example by limiting the number of American companies covered by Beijing's Unreliable Entity list. Beijing has also wooed US businesses, particularly financial services. The offer of more progress in market access through licenses and eased ownership restrictions could even be a catalyst for Beijing and Washington to find a new equilibrium in their bilateral relationship. If China's new dual circulation strategy means a wider social safety net and not massive import substitution, China will remain highly attractive to US corporations, who would be a force pressing for better US-China ties. Beijing's efforts to mitigate climate change could also be an area where the US and China can still collaborate.

And finally, simply due to the low base in 2020, we see 2021 GDP growth at about 7.5%. We expect USD to rebound because the three factors that strengthened CNY in 2020 are set to reverse, at least partially. First, relative growth momentum between China and the US will shift. Second, interest rate differentials will narrow. Third, the decline in Chinese outbound tourism, which vastly expanded its current account surplus in 2020, should begin to reverse.

Hong Kong: Returning to a growth track after two bad years



THE coming year, 2021, will certainly be a better one in terms of economic growth, simply due to the low base effect caused by the pandemic and the earlier protests. Two key factors will determine how well the Hong Kong economy revives — support from the Chinese economy and the Hong Kong government's policies.

China's boost to Hong Kong's financial services is tangible in the avalanche of mainland company IPOs. That will keep trading volumes and related activities in Hong Kong's financial market buoyant amid a lacklustre real economy. US-China trade tensions will remain a wild card for Hong Kong, where sentiment is often on a roller-coaster ride. Assuming Beijing and Washington find a new equilibrium, which would entail adjustments by both, Hong Kong's position as one of the world's leading financial centres will likely remain intact.

The other key driver from China is tourism. There is some concern that Chinese tourists may not return after Chinese New Year. Even if tourists eventually return, we could see gingerly gradual

steps in restoring cross-border travel, with travel bubbles first formed in the Greater Bay Area, then expanded to other major cities such as Beijing and Shanghai. At least before a vaccine becomes commercially available, Beijing authorities are likely to maintain their efforts to limit imported cases. Therefore, Hong Kong's recovery in tourism is expected to be moderate.

On the domestic front, Hong Kong's good fundamentals will count. COVID-19 has amplified differences in approach taken by various governments in containing the virus. Beijing's approach of mobilizing resources to nip the virus in the bud was proven to be highly effective and Hong Kong also did quite well. Hong Kong's world-class medical facilities are another positive factor in how it faced the challenges from the pandemic.

The good news is that Hong Kong could continue to buy growth on the back of its vast fiscal reserves, just as it did in 2020. Furthermore, low interest rates and the weakness of the greenback will continue to underpin the housing market.

India: Strategic focus on jobs, the services sector, and private demand will aid growth

ECONOMIC activity is showing signs of traction. The PMI manufacturing index is at its highest since 2008. Stronger car sales, rising production of finished steel and diesel consumption, and higher goods and services tax revenue collections indicate that the economy has bounced back strongly since “the unlock”, backed by pent-up and festive season demand. Nevertheless, sustaining this rebound could be a challenge next year, if infection cases continue to be high. We expect India’s GDP to rebound to double digits in FY2022 after contracting in FY2021.

Three drivers will ensure a sustained economic revival and rehabilitation:

Inclusive job growth: Government policies that focus on the infrastructure, construction, manufacturing, and retail industries can quickly generate employment for low-skilled workers, improve private sector performance, and increase activity amongst micro, small, and medium enterprises (MSMEs). The government’s measures, such as interest-free 50-year loans to state governments to boost infrastructure spending, and its vision of a self-sufficient India (the Atmanirbhar Bharat package), among others, are expected to improve infrastructure investment and tap into the potential of the capital goods, chemicals, and electronics industries. Strategic partnerships with private players are key.

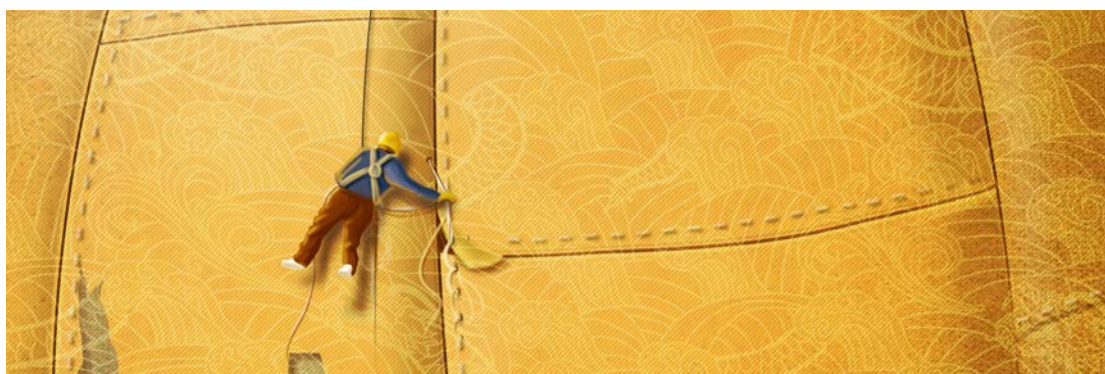
A robust services sector rebound: Services account for over 55% of GDP and the sector’s recovery is gradual so far. According to PMI, it returned to growth in October for the first time since the pandemic. The trade, hotels, transport, and communication sector (contributing a fifth of GDP) could

witness a modest rebound as social distancing and consumer caution ease. A renewed focus on improving the skills base (education) and digitization could help the sector rationalize costs, improve productivity, and address new markets. An effort to build the Global In-house Centres (GIC) of the world by prioritizing the above and being agile in doing business could revive the services sector.

A sustained recovery in private demand: Rural demand will continue to benefit from the good monsoon in 2020 and the government’s support for rural employment. However, urban demand could be restrained by the continued fear of infections, uncertainties around employment, and consumers increasing precautionary savings. Weak demand could translate into slow investment and the economy might get stuck in a low demand-supply vicious circle.

Hence, the key role of policy support. Since the pandemic the government has announced a series of stimulus packages in phases. The first, announced in May, intended to boost the supply side of the economy and provide credit to vulnerable segments of the population to support lives and livelihoods. Over the past month, the government announced two additional stimulus packages (targeting the demand side) to boost consumer spending, investment, and employment. Several difficult labour and agricultural reforms over and above the stimulus packages were announced as well. The government’s effective policy measures together with prudent business strategies should help the economy grow strongly from the next fiscal year.

Indonesia: Recovery delayed, but not derailed



INDONESIA was particularly hard hit by the pandemic as the government struggled to enforce effective measures to restrain the spread of the virus. Other factors have also worked against Indonesia in 2020. For example, demand for crude palm oil, which supports millions of smallholders, was hurt by the economic slowdown in Europe and India, two of the largest importers, despite the B30 mandate to gird domestic demand for the vegetable oil. Although China, by far the single most important destination for Indonesian coal exports, has recovered from the pandemic, that has not translated into higher commodity prices yet, underscoring the importance of a global synchronous recovery even for a domestically-driven economy like Indonesia's. Moreover, the tardy disbursement of public funds has not helped either, so the impact of promised spending on social transfers to keep the economy afloat has been more limited than desired.

A sharp rebound is unlikely, considering the lasting hit to consumer and business confidence across the sprawling archipelago. But there is reason to be upbeat over the economy's prospects once the pandemic subsides.

First, the infrastructure agenda will be a focused one, as indicated in the revised list of national strategic projects. Plans to construct a new capital city will proceed, and if done right will create economic synergies in Borneo.

Second, Indonesia will continue to make some progress in moving up the value-chain, with more investments in smelter projects, the development of a buzzing eco-system for electric vehicles, and petrochemical refineries for import substitution.

Third, labour reforms approved by the administration will help Indonesia attract a bigger slice of outbound investments from China that have hitherto bypassed the archipelago due to sky-high severance costs and bureaucratic hurdles.

But the effects will only be apparent once the pandemic subsidies in Indonesia, and there is more clarity on the implementing regulations, which is due by early-2021 at the latest.

Japan: Well-contained, economic recovery is consistent

IN late May the government lifted the state of emergency, and the Japanese economy is recovering, but slowly. Some of the factors that mitigated the damage caused by the pandemic will continue to hold into 2021.

First, Japan contained the spread of COVID-19 relatively well. Although there were rebounds in the number of cases after lockdown was eased, the number of daily cases is around 2,000, well below those of countries with severe rebounds. Second, the government and the central bank moved quickly to address economic risks from the pandemic. Further quantitative easing, encouragement for banks to extend funding to consumers and businesses and the JPY230 trillion (USD2.2 trillion) fiscal stimulus package have all helped. Third, some sectors such as communications and IT are benefiting from increasing demand from tele-commuters and workers from home, and digitalization. Retailers expanded on-line sales to meet consumers' demands.

Nevertheless, some headwinds remain. First, a slow recovery in global demand could hold back a recovery in key sectors such as manufacturing. Tourism spending will stay restrained by con-

tinued restrictions on cross-border travel. Second, once fiscal support is scaled down, personal incomes could contract and depress consumer spending. The administration of new Prime Minister, Yoshihide Suga, started planning the third supplementary budget and is likely to maintain policy continuity. Still there is some uncertainty as to how the government will maintain fiscal policy given its inflated debt, which is expected to jump up to 216.4% of GDP in 2020 from 192.5% in 2019.

Finally, there is still severe damage to business and household economic conditions, which would require fundamental reforms to sustain growth. We estimate it will take more than five years for Japan GDP to return to pre-COVID levels. A potential surge in credit losses in the banking sector could weaken financial stability.

We expect the economy to rebound to 2% annual growth in 2021 after a 6% contraction in 2020. The economy should return to its potential growth rate of 1.4% in 2022.

South Korea: A solid rebound in the offing

IN 2021, South Korea should recover sufficiently from its contraction in 2020 and progress toward its pre-COVID-19 level. Domestic economic activity will benefit from effective yet relatively less disruptive virus control measures and targeted fiscal policy aimed at supporting household income and employment. External demand should also recover, prompting increases in outbound shipments of semiconductors, electronic devices, and healthcare products.

South Korean telecommunications companies will benefit from the technology bifurcation between the United States and China as they increase global market share due to the retreat of China telecoms companies such as Huawei. US restrictions on sales to Huawei will affect South Korean semiconductor manufacturers, but it is expected that the related loss in revenue will be offset partly by increased sales to other buyers in China and elsewhere, which are likely to raise orders in an attempt to increase market share.

Policy measures will continue to support the economy in 2021:

- Under the “Korean New Deal”, the government will invest KRW160trn (USD133bn) in 2020-25 to improve job creation and enhance the competitiveness of the domestic manufacturing sector through public projects in digital and green energy infrastructure. The initiative will also expand unemployment insurance coverage to people engaged in all forms of employment. These initiatives are expected to help maintain employment and facilitate a steady economic rebound from 2021.
- Meanwhile, the government will encourage domestic innovation and sourcing in the manufacturing sector in the face of growing competition from China and global trade protectionism (particularly Japan’s export restrictions targeting South Korean high-technology manufacturing). The government is expected to maintain its policy support for domestic manufacturers, while remaining open to foreign investment.
- In 2021, Bank of Korea (BOK) is likely to retain its moderate monetary policy stance, by maintaining its policy rate at a record low of 0.5% throughout the year, while extending its program of incentivizing commercial banks to provide low-interest loans to SMEs. BOK will also probably extend its government-bond purchase program to keep long-term interest rates low. That, and the good appetite for South Korea sovereign bonds among international investors, should prevent sharp spikes in bond yields.

Malaysia: Headwinds to limit degree of rebound

THE Malaysian economy will enter 2021 weakened by the imposition of new lockdowns in areas that account for close to half of GDP. Lower-for-longer oil prices are a double-whammy for the economy, as petroleum revenues and exports of petroleum products take a beating. The tourism, aviation and hospitality sector, which is increasingly reliant on tourists from China, has been gutted by the pandemic and a full recovery is unlikely to take root any time soon. Sub-par crude palm oil prices haven't helped.

Looking forward, several headwinds are likely to buffet the economy in 2021, with some tailwinds as well:

- Political uncertainty and the prospect of snap elections could hold back the recovery in spending by corporations and households.
- The expiration of the loan moratorium scheme from 4Q20 could also depress household spending, especially given rising levels of household debt.
- But the trade-driven economy should benefit from the normalization of external demand. The resilient tech sector, particularly consum-

er electronics, has been a standout performer in Malaysia, thanks to a well-diversified economic base.

- It is also expected that the budget for 2021 will contain handouts and social assistance for households, providing a tailwind for private spending.
- Inflows of investments from China are another likely tailwind. These consist of infrastructural investments that have restarted development in earnest, such as the East Coast Rail Link and Melaka Gateway, plus manufacturing and electronics investments from firms moving out of China. This, combined with more clarity on the government's medium- and long-term development plan (due for release in December 2020), and the revamped 12th Malaysia Plan (to be released in January 2021) should provide a fillip to and crowd-in private investments in the medium-term, expanding the economy's productive capacity.

New Zealand: Still highly susceptible to global conditions

NEW Zealand seems to be in a better situation than many of its major trading partners in terms of minimizing the number of coronavirus cases, but has had to maintain tight border restrictions to do so. Still, some green shoots are beginning to appear. Recent business surveys suggest firms are feeling much more optimistic about the economy and their own prospects than they were a few months ago. Households, on the other hand, remain cautious, with those working in the hospitality and tourism sectors particularly downbeat.

One big positive for the local economy is a surge in house prices, driven by ultra-low interest rates and the removal of bank lending restrictions. Strong demand from investors and first-home buyers, combined with limited supply in the market, saw prices appreciate 13.5% over the year to October, according to the Real Estate Institute of New Zealand. New Zealanders typically use housing as a large store of their wealth, so rising house prices boost consumer confidence and people's propensity to spend.

The Official Cash Rate (OCR) has remained on hold at 0.25% since March this year, but banks have been told to prepare for a negative policy interest rate. The Reserve Bank of New Zealand (RBNZ) also introduced a Large-Scale Asset Pur-

chase quantitative easing program of NZD30bn in March, which was later increased to a total purchase ceiling of NZD100bn extending to mid-2022. In November, the RBNZ added further to its policy toolkit with a Funding for Lending Programme (FLP) which will start in December 2020 and provide an estimated NZD28 billion. The FLP aims to further depress market interest rates and RBNZ has left the door open to move its bank policy rate into negative territory in 2021 if economic data remains soft. Inflation fell further to 1.4% year-on-year in September, adding to market expectations that the RBNZ will lower OCR further near the start of 2021.

Although the New Zealand economy is weathering the economic fallout of the pandemic better than initially predicted, it remains highly susceptible to global conditions. As a small exporting nation, continued weak offshore demand will prevent a full recovery. Tourism, education and businesses that rely heavily on exports will not be able to gather enough momentum without the help of the rest of the world. With many regions now experiencing big second coronavirus outbreaks, risks to New Zealand's outlook are skewed toward the downside.

The Philippines: Sharp rebound in abeyance

THE Philippines has borne the brunt of the pandemic with one of the most stifling lockdowns in the region. Although it has now turned to localised lockdowns, there will still be a toll on the economy so long as the virus continues to claim victims. Given the fiscal constraints on the administration's capacity to disburse funds to keep the economy afloat, authorities are likely to decide on a calibrated reopening of the economy in the near-term. But a number of headwinds will continue to hurt the Philippines in 2021:

- Political risk has risen in light of President Duterte's ill-health and the re-positioning of congressmen for the 2022 general elections, evinced by the political machinations that rocked Congress recently. Geopolitical risks remain salient, evinced by the exodus of gaming companies that used to cater to Chinese gamblers, and possible tensions with China in the South China Sea.
- Persistent instability in the mineral-rich, restive south — twin bombings in the south of Sulu Province in August 2020 — remains another area of concern, as authorities look set to revive the mining industry through a new bout of liberalization.

Still, we believe the Filipino economy is poised for better days.

- A recovery in remittances (accounting for a tenth of GDP) is likely once the global economy perks up, and will prop up household spending while shoring up external accounts.
- A reset of the infrastructure agenda is also on the cards, as funds will no longer need to be diverted towards healthcare in 2021. That, together with the looming 2022 general elections, should see a renewed emphasis on public works project as authorities would want to get these up and running if and before they hand over to a new administration.
- The business process outsourcing (BPO) sector has coped well with work-from-home arrangement, thanks to better internet connectivity in the capital region, which is where the industry is concentrated. But there are some longer-term concerns of dislocation to BPO, spurred by the march of automation and AI.
- The administration is eyeing the mining sector as a new growth driver with plans to privatize several mining assets. Economic managers hope that this will not only raise additional revenues for cash-strapped governments, but also help buoy the sector and unleash employment opportunities for rural residents.

Singapore: A precarious recovery

WITH a GDP contraction of 5.8% year-on-year in 3Q20, an improvement from -13.2% in 2Q20, the supply-side recovery of the Singapore economy is mostly complete.

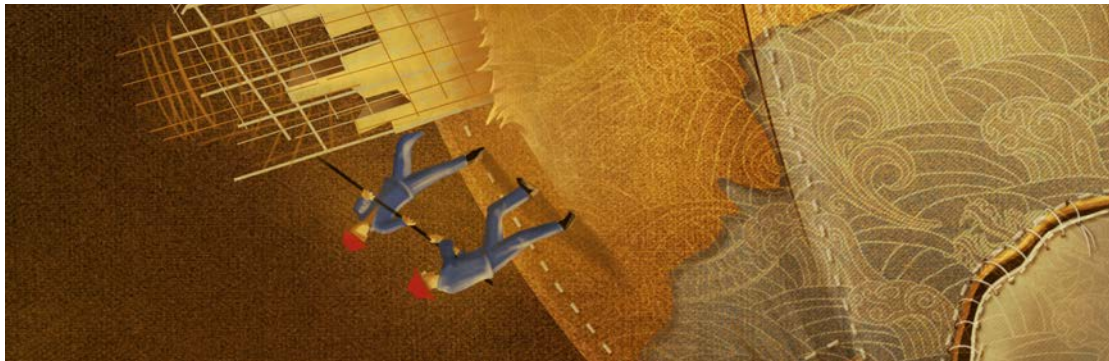
- We envisage a broader recovery in manufacturing in 2021 as the shape of global demand broadens, while tech demand remains vibrant enough to boost the all-important electronics sector.
- However, the performance of the services sector will remain highly uneven. Even with more travel bubbles, the travel and tourism sector will likely stay in low-gear for some time as international borders are reopened very cautiously. Consumer-facing sectors are likely to taper off after a sharp rebound in 3Q20 as soft labour market conditions weigh on confidence.
- External-oriented services, such as wholesale trade, transportation, and storage, will stage a fuller recovery in 2021 as the shape of global demand and trade broadens beyond electronics and pandemic-related demand for pharmaceuticals and medical equipment, which has been robust year-to-date. The finance and insurance sector, which powerfully supported growth in 2019, will continue to expand, albeit more modestly, as sluggish output weighs on credit demand.

- The lone area where we envisage a material acceleration is the information and communications technology sector, on account of stronger demand for IT solutions as digital transformation, already advanced, is accelerated. The relocation of Chinese technology firms such as Bytedance and Tencent will add a fillip to the sector as well.

There are three key risks to the economy in the near-term.

- First, elevated unemployment will weigh on aggregate demand as households cut back on discretionary spending. The recent flurry of tax and fee increases could also hurt consumer confidence.
- Second, there is a risk that credit conditions tighten as we head into 2021 as banks become cognizant of the health of their balance sheets and begin to pare back lending.
- Third, the lack of commitment to new and significant fiscal support for the economy suggests “fiscal cliff” effects are likely to be material.

Taiwan: Surprising on the upside?



TAIWAN'S economy has performed remarkably well in 2020 and is likely to avoid the contractions seen in much of the world with GDP growth close to 2%. This is particularly impressive given most small, highly-open economies (such as Hong Kong and Singapore) have struggled.

Taiwan's economic resilience has been underpinned by a combination of the government's success in containing the pandemic (which meant the economy was not dislocated by severe lockdowns) and Taiwan's expansive exposure to the global technology cycle. Looking forward to 2021, several factors will come into play. First, the Chinese Mainland remains a curious mix of massive opportunity and perturbing uncertainty. If the Chinese economy accelerates as much as we anticipate in 2021, there will be positive spill overs for Taiwan's manufacturing sector. However, the risk in Sino-US relations could cast a shadow

over the Taiwan Straits. Meanwhile, Taiwan's high tech companies are reallocating their supply chains and increasing their investment in digitalization and green energy.

Policy responses will be another factor. Taiwan's central bank is expected to keep short-term interest rates unchanged, and fiscal policy is expected to play a counter-cyclical role by extending relief to consumers, and firms that have seen their supply chains disrupted in the wake of COVID-19. With global interest rates staying low and the New Taiwan Dollar relatively under-valued, Taiwan could easily tolerate a higher debt-to-GDP ratio. Assuming the global economy continues to recover in 2021, we anticipate Taiwan to register strong GDP growth of about 3.5% in 2021. Finally, Taiwan would also benefit from the global shift to new energy and the "new normal" of cheap crude in 2021, as it did in 2020.

Thailand: On the edge

THE Thai economy has underperformed the region this year despite containing the COVID-19 pandemic. The economy's heavy dependence on tourism has hurt it deeply. Tourist receipts amount to 11% of GDP, but with indirect spill overs added in drives close to 25% of GDP.

We see this underperformance continuing in 2021, as borders to international travel re-open only cautiously given elevated virus caseloads in Europe (16.8% of tourist arrivals in 2019) and parts of Emerging Asia (26.6%). On this count, a mooted travel arrangement with China, which drove nearly 30% of tourist arrivals to Thailand in 2019, could if implemented provide much needed succour to the systemically-important tourism sector, and lift the growth outlook for 2021.

Crucially, we expect Thailand's export growth to remain relatively sluggish as global demand picks in 2021 vis-à-vis regional peers like Singapore, Malaysia and Vietnam, whose export mix exhibits a greater tilt to technology. In turn, a moribund export outlook and still-elevated industrial capacity are expected to weigh on business investment.

As a consequence, private domestic demand will largely be driven by consumer spending, which we see supported by improving farm incomes

from more favourable weather conditions and a fiscal package designed to provide substantial relief to households. That said, the sluggish, uneven pattern of recovery in coming quarters suggests a high degree of labour market slack that could weigh on wage growth and thus dent consumer confidence.

Fiscal largesse will also play a role in supporting the economy in 2021, with the government attempting to expedite several planned infrastructure projects in the pipeline. However, we expect sub-par disbursement efficiency to constrain the eventual impact on GDP growth. New finance minister Arkhom Termpittayapaisith has signalled expanded fiscal stimulus, given ample policy space with public debt-to-GDP still low.

Bank of Thailand likely sees limited policy space for further rate cuts, but has kept the door open to unconventional policies such as yield curve control and quantitative easing, which could complement fiscal largesse.

Political risks have also risen, which could lead to protracted uncertainty.

Vietnam: Poised for acceleration

REAL GDP growth rebounded sharply to 2.6% from a year earlier in the third quarter of 2020, up from 0.4% in 2Q20, led by accelerating momentum in services that added to resilient agricultural exports and manufacturing activity.

With all growth engines oiled and ready for ignition, the country successfully containing a second wave of virus caseloads in July, and support from fiscal and monetary policy, the economy is poised for further acceleration. The main drivers of growth will be exports and private investment, with consumer spending also playing an accretive role.

In a sign of confidence in the near-term growth outlook, Prime Minister Nguyen Xuan Phuc raised the government's growth target for 2020 to 3.0% from 2.5%.

Vietnam's highly open frontier economy has several structural tailwinds behind it that will continue to shore up growth in 2021.

First, it is a major beneficiary of ongoing supply chain shifts in the region, which have accelerated amid geopolitical and trade tensions between the US and China, and calls for supply chains in "stra-

tegic" sectors such as pharmaceuticals and medical equipment to be diversified and/or re-shored.

Second, Vietnam's economy is deeply integrated into the regional technology supply chain, so will benefit strongly from the continued upturn in the global electronics cycle that we envisage on account of stronger consumer spending on gaming products in the holiday season, 5G handset upgrades, and automobiles — the sector most geared to global GDP — making for a smooth handoff from enterprise IT and work-from-home related spending that supported the cycle this year.

Third, Vietnam's comprehensive set of free-trade agreements with its major trading partners will play an important role in supporting export growth amid a likely more protectionist trade environment.

On the policy front, we expect State Bank of Vietnam, which has cut major policy interest rates across the board three times this year, to refrain from further stimulus on account of the manifestly improved growth outlook and residual inflation fears, given the large share of food in its CPI basket.

What the US election means for Asia-Pacific

THE election of Joe Biden as President of the United States has four broad sets of implications for the Asia-Pacific.

1. Better management of still-tense US-China relations:

The United States-China relationship is now the single most important bilateral relationship in the world. No one should expect frictions between the US and China to diminish substantially, as the fundamental strategic interests of China and the US now diverge in many ways, especially in the western Pacific. The incoming Biden Administration will have to accommodate the fact that a large part of the American political spectrum has come around to the view that China poses a strategic threat to it, and that the United States has to meet this challenge across diplomatic, military and economic fronts. On the Chinese side, meanwhile, the Chinese political elite has developed a more dour view of the United States. Trust has been fractured and there cannot be a return to the relationship that existed before President Trump.

Nevertheless, we anticipate that although the Biden Administration will make no bones about the need to contain China, it is also likely to adopt a more nuanced approach than its predecessor did.

- **Trade:** The new administration will not be soft on China. We expect current tariffs to remain in place, as the two sides negotiate a new trade pact. However, Biden does not appear inclined to aggressively expand the trade war.

- **Technology:** Here too, the US side will continue to be wary of China. The new administration will continue with restrictive measures on China, but we expect these to be more selective. The risk of technology bifurcation will remain.

Against this, we also believe the Biden team will be open to combining a tough posture on China on the above issues with a greater willingness to collaborate with China on issues of mutual interest. President-elect Biden is committed to action to tackle climate change and his advisors realize cooperation with China and other large economies will be vital in this area. Similarly, containing possible threats posed by North Korea in the Korean peninsula will remain an important objective for the US administration. Biden is unlikely to shift away from the Trump Administration's implicit acceptance of North Korea as a nuclear power, but will want to maintain strict sanctions on the North Korean regime to constrain its ability to threaten the mainland United States. To be successful, any American strategy on North Korea will need some degree of Chinese support.

2. Trade policy is likely to be managed with some finesse:

Biden's track record has been one of multilateralism, and this should apply to the trade arena, but only up to a point. He is not likely to be as committed to free trade as, say, President Clinton was. Under Biden, the United States will still adopt a robust approach on issues such as "currency manipulation", market access and bilateral trade deficits, which could give rise to trade tensions with China, Japan and East Asian exporters.

Still, while Biden's trade team won't want to be seen as soft on its trading partners, the United States approach will become less confrontational. We see continued efforts to press its trade partners to adopt voluntary actions to adjust their bilateral trade deficits with the United States. We also expect Biden's trade advisors to return to a more cooperative policy towards the World Trade Organization (WTO). There is likely to be a compromise on the appointment of a new WTO director-general, and the US is likely to resume allowing new appointments to the WTO's arbitration panel, thus allowing the WTO's dispute resolution function to resume.

There is little likelihood of the US returning to the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) agreement, but the administration could be open to selective paths to greater economic engagement with the members of the CPTPP.

3. More policy stimulus will boost US demand for Asian exports:

Several factors are likely to confluence to produce stronger US demand for Asian commodity and manufactured exports:

- There is a good likelihood of continued strong fiscal spending that will boost the US economy and thereby raise global demand. Such additional fiscal stimulus, which the economy needs, but has been delayed by political gridlock, is likely to at last be implemented.
- Over the course of the year, we also expect agreement on a large infrastructure program.
- Defence spending and government support for R&D is also virtually certain to grow.

Not only should overall US import demand grow, but the pattern of spending described above

should also be positive for intermediate goods such as electronics components, which East and Southeast Asian economies specialize in.

4. Rebuilding alliances and greater outreach to allies:

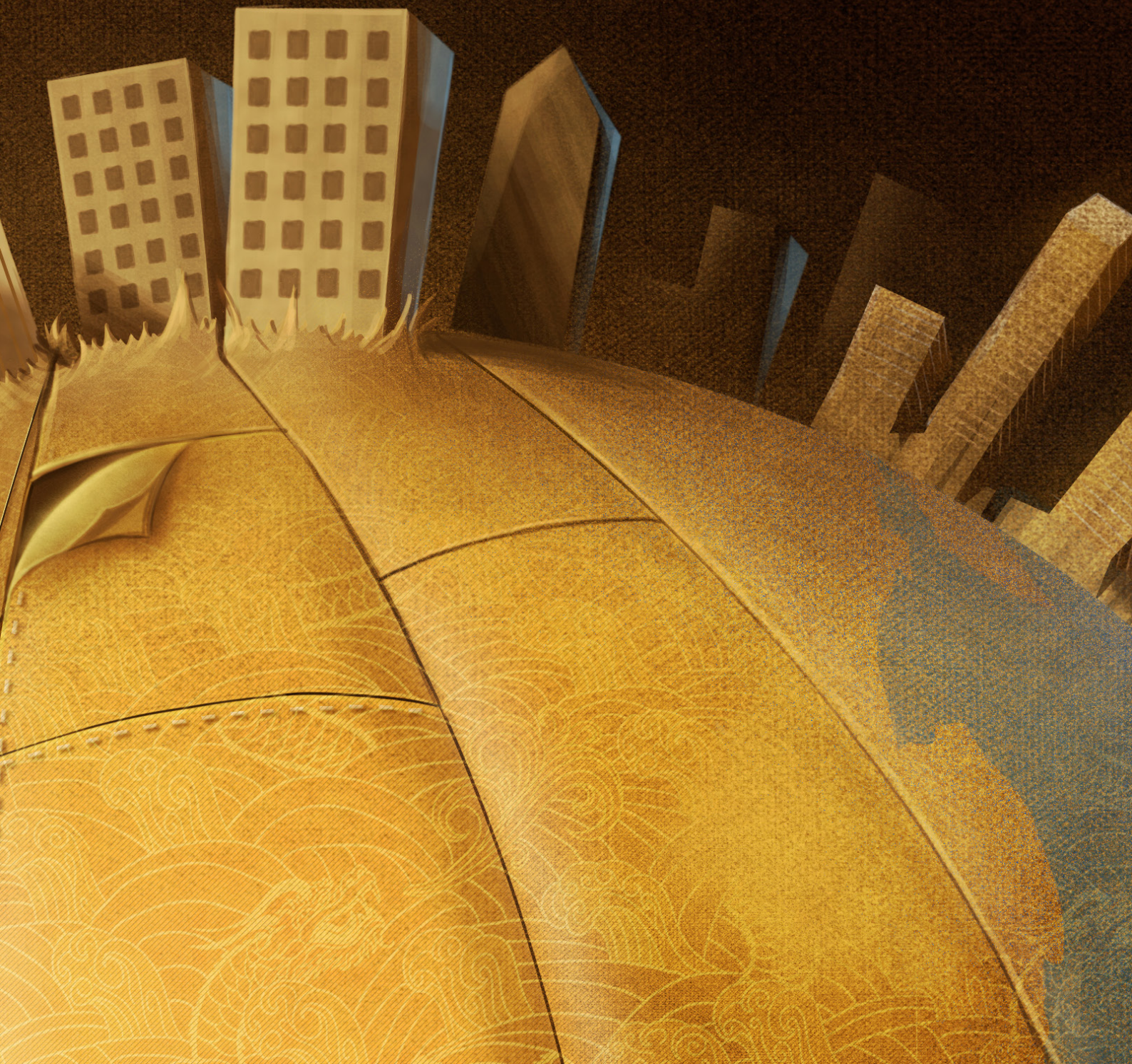
The new administration's approach is likely to be welcomed by smaller nations in Asia-Pacific, especially trade-oriented economies. For the latter, a rules-based trade regime centered around the WTO is key, as is an international political and security order based on agreed "rules of the game". An America that veers away from the transactional and bilateral approach favoured by President Trump will be seen positively in the region, as will the expected return of the United States to the Paris climate accord and the World Health Organization.

- The Association of Southeast Asian Nations (ASEAN) is likely to be a big winner. Southeast Asia is China's backyard and a likely arena for big power contests. Biden's likely foreign policy team has considerable knowledge of the region and its importance: there will be more US engagement with ASEAN in trade, infrastructure, investment, and technology.
- India is likely to be another major beneficiary. The Biden Administration is likely to continue the Trump Administration's strong push for closer military and strategic ties with India.

Conclusion

In short, the incoming administration is likely to help reinforce a more benign outlook for the region in 2021. A United States with a stronger economy, more willing to engage productively with its economic partners, and that pursues its strategic goals rationally and in concert with allies, can only be good for Asia-Pacific.

The Next Wave: Emerging digital life in South and Southeast Asia



Young and emerging economies in South and Southeast Asia are rising stars when it comes to the digital economy. Given that digital life ecosystems in digitally developed Asia (such as South Korea, Japan, and China) are maturing, it's this region that'll be home to the next emerging "wave". There are four key factors behind the rapid rise of digital life in South and Southeast Asia.

1. The region's mobile penetration is growing rapidly — for example, Indonesia's mobile penetration rate is estimated to grow to 69% by 2025 while India's is projected to reach 63%, according to GSMA. As such, consumers in South and Southeast Asia are more inclined towards smartphone-aided e-commerce.
2. The region's population is large as well as young—and high on digital life is boosted by social media. Young adults are particularly keen and quick to adopt new types of mobile technologies.
3. This population includes a large number of "unbanked" and "underbanked" consum-

ers, spurring rapid adoption and growth of digital financial services that are accessible via smartphones. Interestingly, smartphones have become a conduit for further adoption of digital payments.

4. Most governments in the region have introduced supportive policies in recent years to boost development of the digital economy and digital infrastructure.

So, to create a portrait of digital life in South and Southeast Asia, we surveyed consumers across eight countries and every age group. We wanted to find out consumers' attitudes towards digital life, such as mobile payment and social media usage, as well as their concerns.

The survey was conducted in August 2020 with over 2000 samples across eight countries: Singapore, Malaysia, Thailand, Indonesia, the Philippines, India, Bangladesh, and Pakistan. The sample age ranges from 21-60.



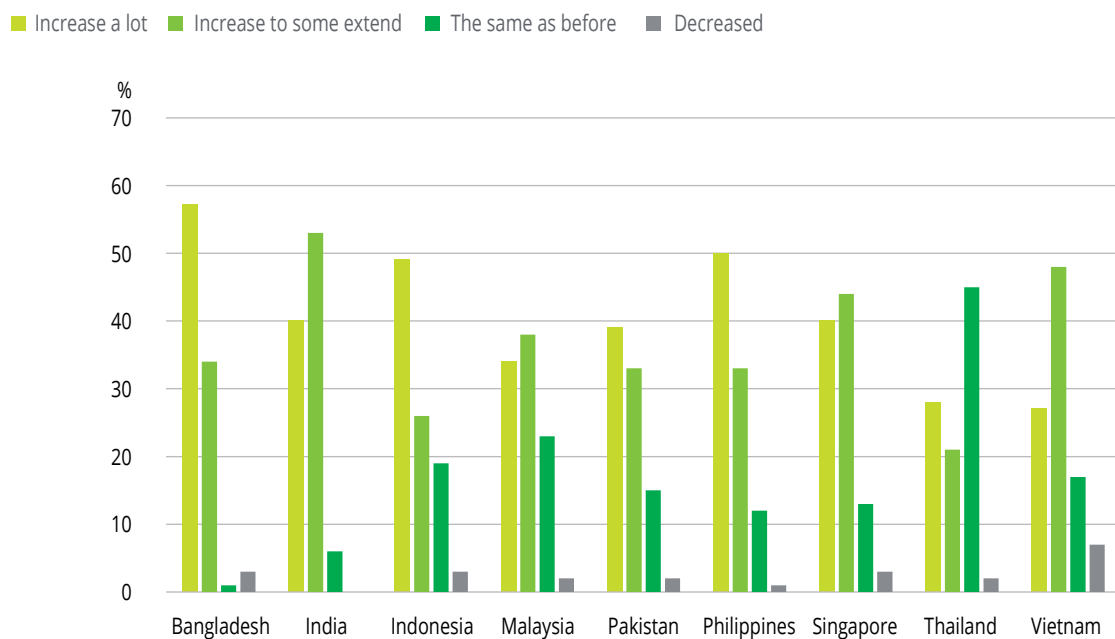
Demand for digital services surged in the pandemic

THE COVID-19 pandemic triggered an unprecedented expansion of consumers' digital life. About 78% of respondents said their use of digital services has increased since the COVID-19 pandemic started, with 41% reporting a substantial increase and 37% saying it has increased somewhat (Figure 1). Bangladesh, the

Philippines and Indonesia were the countries where more people cited a substantial increase. Demand for TV shows, online games, e-commerce, social networking, online office access and online education saw a marked rise.

Figure 1:

Use of digital services has increased since the pandemic started



Source: Deloitte Research

Digital payments central to digital life

AT the heart of the digital life lie digital payments. They are a key enabler in creating and connecting consumers' digital lives and supporting a fundamental shift in social interactions, financial transactions, digital entertainment, daily life services and shopping.

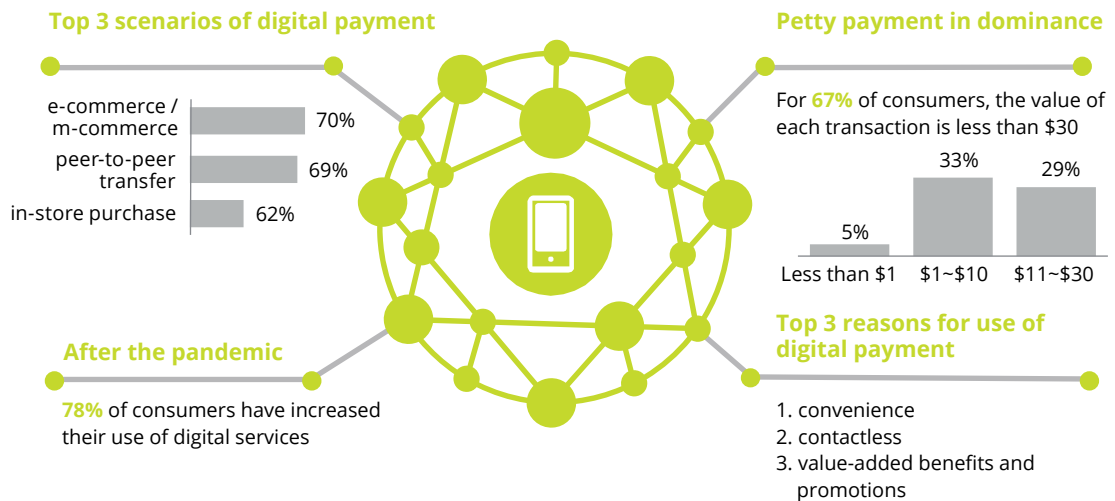
Our survey data revealed that the three most common daily scenarios where consumers use digital payments are e-commerce/m-commerce, peer-to-peer transfers and in-store purchases, with a majority of transfers being small sums. Consumers favour digital payments mainly because they

are convenient, contactless and offer extra benefits and discounts.

The developing countries of South and Southeast Asia have high mobile phone usage and robust connectivity, but low bank penetration rates. This makes digital payments attractive to the population. Since only a relatively small number of people hold bank accounts in these countries, financial technology companies have the opportunity to utilize digital platforms to provide services that are convenient.

Figure 2:

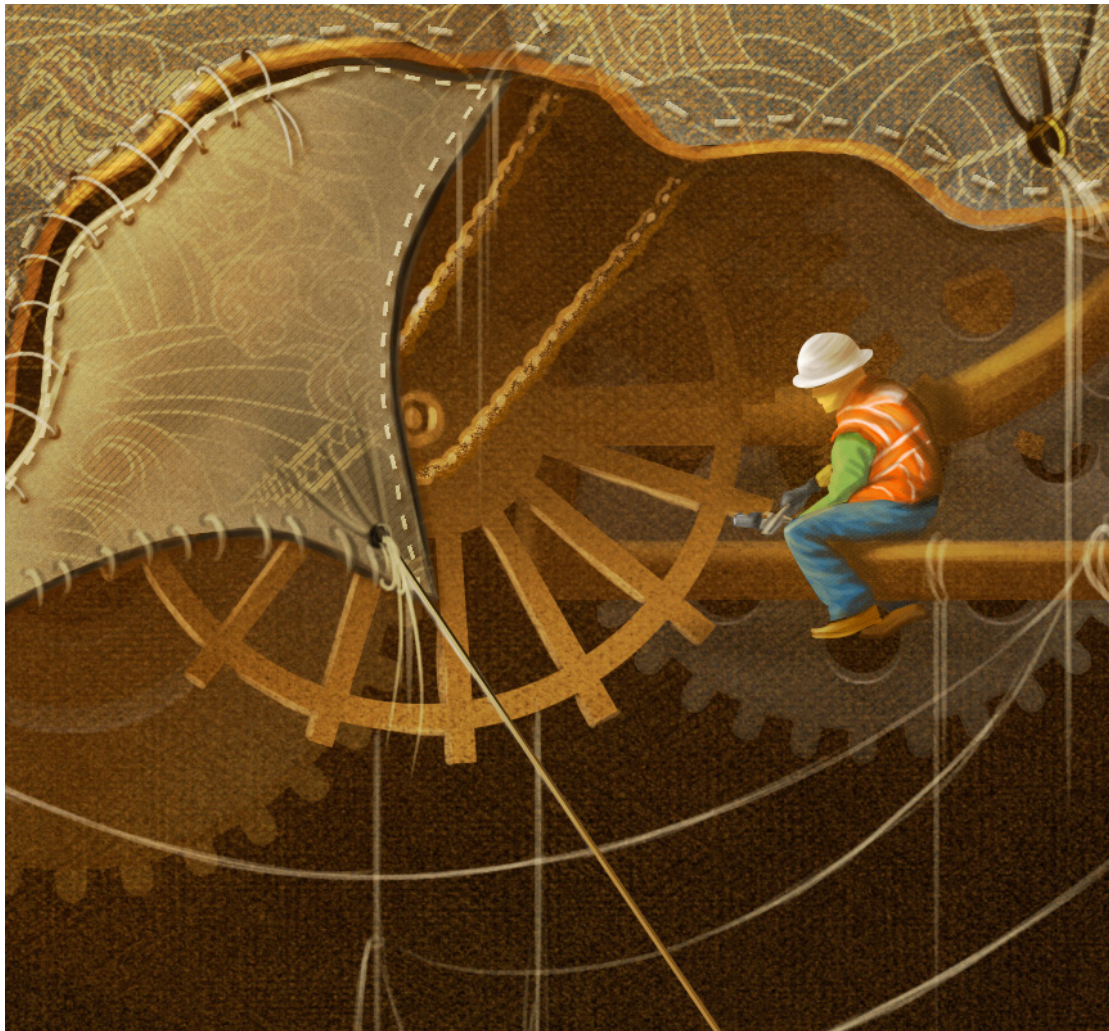
Digital payments are picking up in South and Southeast Asia



Source: Deloitte Research

Compared to matured digital payment models in other regions, South and Southeast Asian countries have demonstrated unique characteristics:

- For various reasons (including consumers' continued preference for cash), the e-wallet model, which enables ready exchange for cash, is a popular choice.
- The various modes of digital payment adopted range from personal identification numbers (more popularly known as PIN) and QR codes to biometric markers.
- Governments are playing a strong role in promoting digital life by establishing standards for identification, determining and supervising a uniform payment standard, and using policy tools to drive the popularization of digital payment.
- Many consumers still rely on offline channels, such as convenient store networks, due to the wide gaps in the availability of traditional finance and weak binding relationships between digital payment, bankcards, and bank accounts.



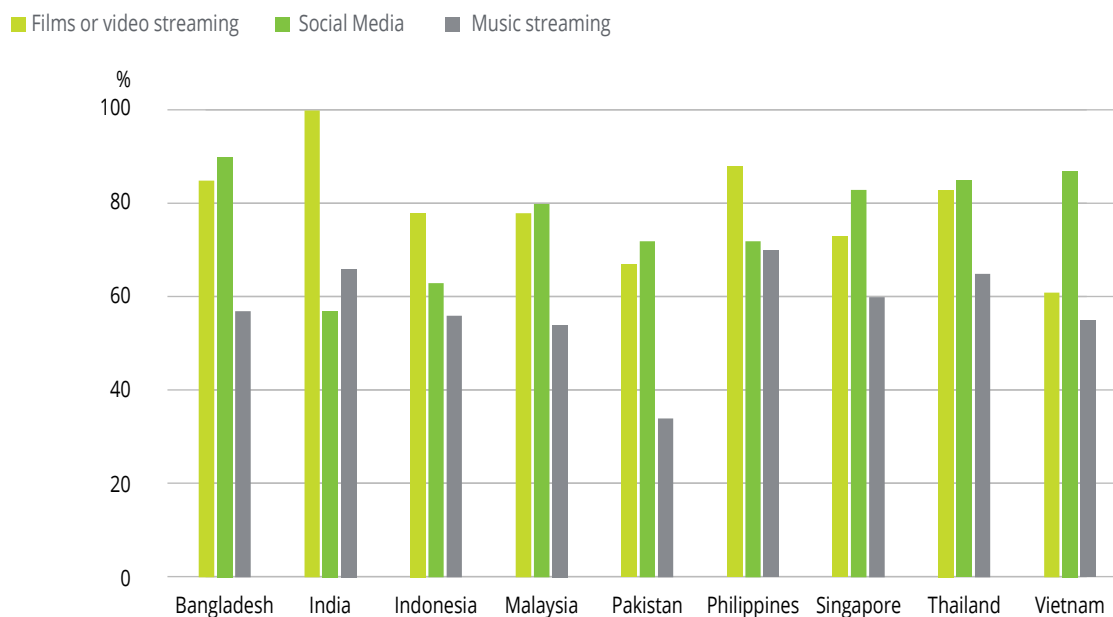
A socially connected digital life

MOBILE phone apps for social media, videos and music streaming are among the most popular in the region (Figure 3). The rapid development of digital technology and emergence of the service economy have led to a

surge in digital entertainment consumption. Interestingly, the pandemic has triggered explosive growth in the “at-home economy” — as more and more people are leaning on technology for e-commerce and grocery delivery.

Figure 3:

Film/video streaming are most popular in India, while social media is popular with Bangladesh and Vietnam



Source: Deloitte Research

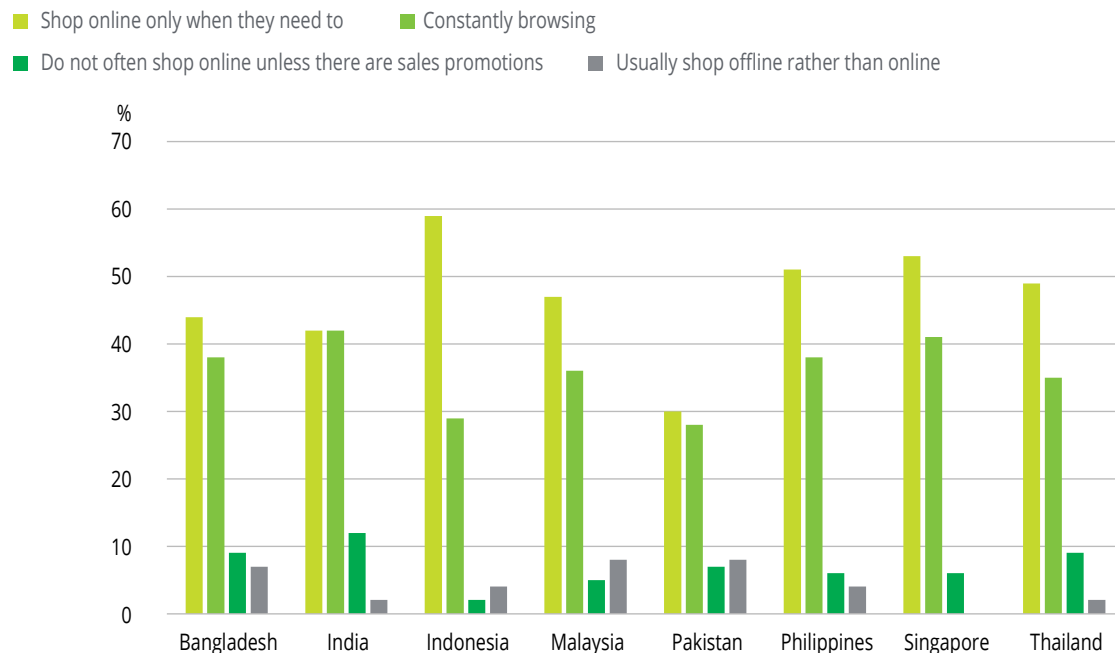
E-commerce is ramping up, but there are some bumps on the way

EVER increasing consumer traffic have made social networks a major means of attracting consumers. Social interactions have fuelled social media, which is driving visits to ecommerce websites. However, most respondents said they shop online when they need to, implying online shopping isn't their first choice (Figure 4). In Singapore, Indonesia and the Philippines, a large

proportion of people shop online. But in countries such as Pakistan, the largest proportion of people — 25% of total population — reported having never done any online shopping. Thus, in more advanced developed economies, consumer are used to shopping online, while less developed economies present a big opportunity for new entrants.

Figure 4:

A great majority in South and Southeast Asia shops online only when it has to



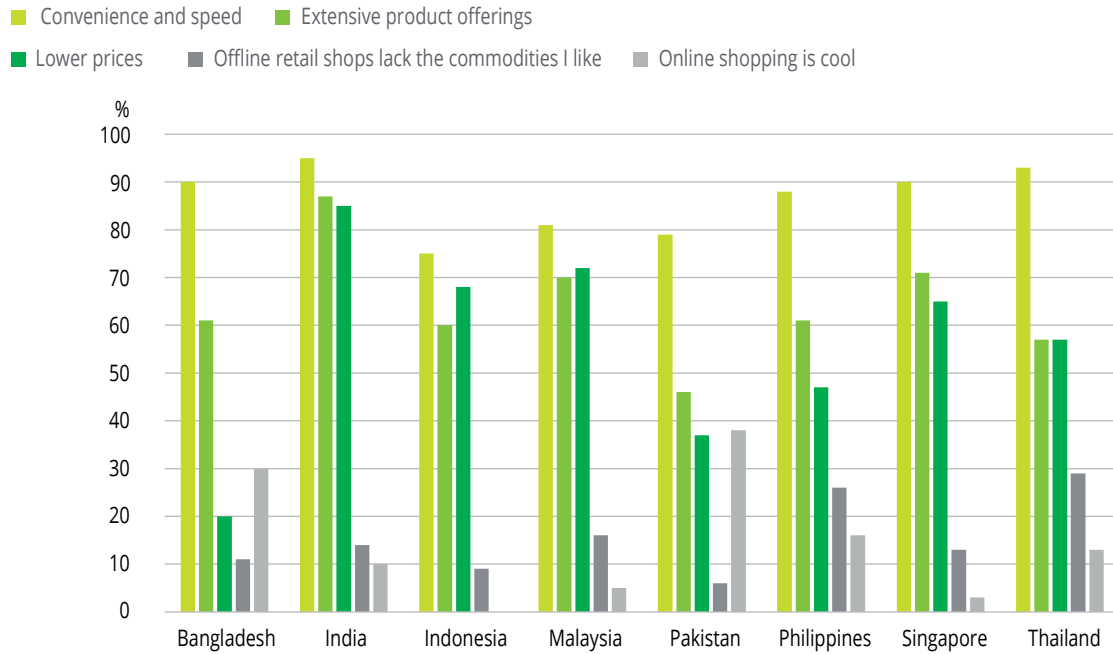
Source: Deloitte Research

As for why those shopping online do so, respondents' top three reasons are convenience and speed, extensive product offerings and lower prices. Thus e-commerce has a great opportunity

to change people's shopping habits since it offers better pricing and wider selection of products, which appeals to consumers. (Figure 5).

Figure 5:

Online shopping is convenient, fast, and, for some shoppers, even cool



Source: Deloitte Research



Youngsters leading adoption of digital life

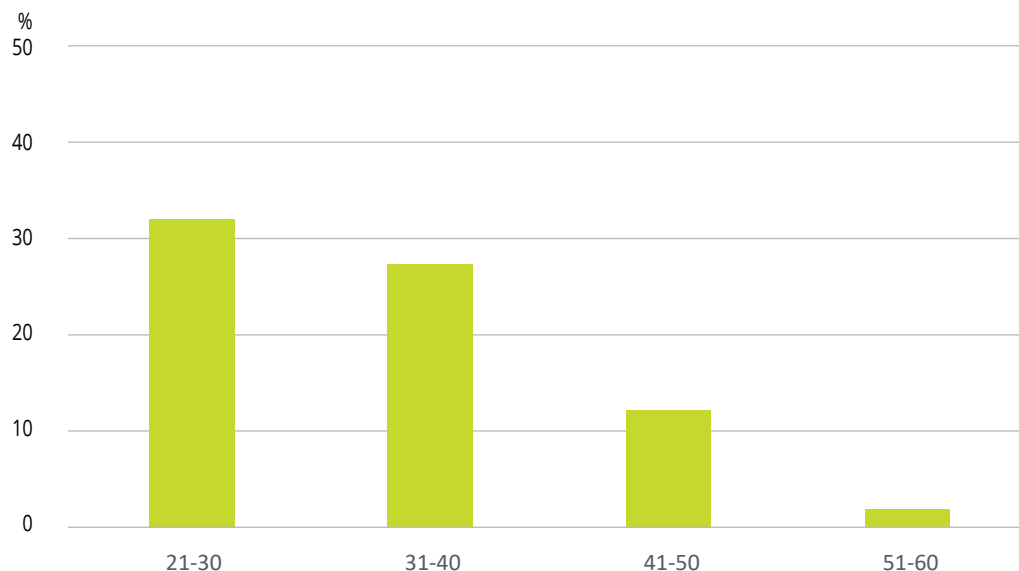
AS of 2019, the total population of South-east Asia was about 660 million. Add to that the populations of India, Pakistan and Bangladesh in South Asia, and we have total population in excess of 2.5 billion, nearly double that of China's. A sizeable population in South and Southeast Asia is underpinned by young demographic. Additionally, the proportion of young adults is much higher in the region than in Europe or the United States. In South Asia, the ratio of people aged 40 or under to total population is almost 63%. In Southeast Asia, the ratio is 70%.

In contrast, Europe and North America are at just 47% and 52%.

“Digital natives” born in the 1990s are more familiar with digital life and have higher acceptance and a steeper learning curve for digital products. Survey data also revealed that young people aged 21-40 are leading rapid adoption of digital life in the COVID-19 pandemic world. The massive population and young demographics are set to bring boundless potential for digital life in both regions.

Figure 6:

Younger adults have been faster than others in picking up digital services



Source: Deloitte Research

Filling the digital chasm

WE believe once digital life really kick-starts in South and Southeast Asia, it will contribute significantly to the economies in both regions. South and Southeast Asian countries have good potential for rapid digitalization, but they still need to catch up in six key areas. Needless to say, mobile players and governments need to work together to realize the full potential of these regions.

1. Accelerate construction of digital infrastructure: Most internet users in South and Southeast Asia are concentrated in large cities and suburban areas, partly due to late infrastructure development and the high cost of setting up the network. Expectedly, the digital infrastructure need lies mainly in rural and remote areas. Both regions have set their eyes to accelerating digital infrastructure construction, and the focus should turn to populations that are “under-connected” or unconnected. To start with, 4G should gradually replace 3G. Bangladesh, for example, launched 3G in 2012 and 4G in 2018. Even then, the country’s communication network is still dominated by 2G. This hinders the development of digital life services, such as live broadcasting and e-commerce, which all rely on higher transmission speed.

Additionally, internet coverage in rural and remote areas should be improved. To understand why, let’s look at Thailand. Most internet and digital wallet users in Thailand are concentrated around Bangkok. Internet coverage in rural and remote Thailand is inadequate, and most of its “digital non-natives” are in rural and remote areas. Thus, there is an urgent need to improve the coverage of rural networks to strengthen digital life, and this can be done by accelerating digital infrastructure construction. India is another example of an underserved market — India’s rural

internet users reached 227 million in 2019¹, surpassing those in cities for the first time, which will give powerful impetus to the digital economy in the long run. Therefore, governments should build better digital infrastructure in rural India and help create a market for digital solutions.

2. Encourage use of digital payments: Despite the rapid development of Southeast Asia economies, e-commerce accounts for only 3% of total retail sales, far below the global average of 16%². The six major Southeast Asia economies account for less than 1% of global e-commerce transactions. One of the reasons for the slow development of e-commerce transactions is that consumers still have concerns about online shopping, and traditional consumption habits still dominate shopping preferences in many places. Even in countries with high banking penetration, such as Singapore, 15%-20% of payments are still made in cash. In India, cash has long been the main payment method. Thus, despite the rapid growth of digital payment there, consumers are concerned about security, privacy and transparency. Therefore, consumer awareness remains the top obstacle to large-scale adoption of digital financial transactions.

Most Fintech companies are more or less technologically ready, but one of their biggest challenges is encouraging people to transit from cash payments to cashless wallets, and getting potential users to understand the benefits digital transactions can bring. Fintech companies and the e-commerce industry need to establish public trust in online shopping and digital consumption through continuous education activities, and nurture consumer’s habit of using digital payment.

¹ Times of India, For-the-first-time-India-has-more-rural-net-users-than-urban, May 2020

² Statista, E-commerce share of total global retail sales from 2015 to 2023, June 2019

On the flip side, offline digital payment is a key part of the digital economy, and its popularity largely depends on the acceptance of digital payment by merchants. Traditional payment methods, such as cards, require merchants to install expensive terminal equipment and pay service charges. But digital payments via QR codes, etc., have changed this dynamic. Businesses can simply collect money through QR codes and smartphones without installing equipment. The promotion of digital payment among businesses may well rely on low service charges, the integration of national identity application program interfaces, merchant systems, and other elements.

3. Seek opportunities to serve the “under-banked”: With continued investment in financial technology across South and Southeast Asia, the region is striving to bridge the gap between mobile connectivity and financial inclusion. Mobile connectivity in the region is at 133% (meaning some users have more than one SIM card or mobile phone), but only 27% of people in Southeast Asia have bank accounts. Of the nearly 400 million adults in Southeast Asia, only 104 million enjoy adequate financial services. Another 98 million people have bank accounts but not enough money in them, and have scarce channels for credit, investment and insurance. About 198 million adults still have neither bank deposits nor bank accounts³.

These are all obstacles to getting loans and make savings, but banking apps and other Fintech products can provide solutions for individuals and small businesses. The region’s future may well be “cashless”, like China. Therefore, those with inadequate financial services (i.e. the “under-banked”) are likely to become the real growth engine of digital financial services companies. Consumer technology platforms, due to their large user bases, can meet the needs of this market. In the next few years, this market will likely be the main battleground as players compete to win consumers’ trust.

4. Establish a robust network security mechanism: Network security is one of the most pressing issue in the digital economy. A series of security incidents have cast a shadow on development of the digital economy and limited trust of the public in the security of payment could hinder the development of digital payment and e-wallets. For example, some 32% of Thai technical professionals personally experienced payment fraud related to e-commerce in 2019⁴. In 2016, the website of the Philippine’s Commission on Elections was hacked and a large amount of voter information was leaked⁵.

There are three main considerations in information security. The first is the “digital trap” that primarily strikes first-time “digital non-native” users. Hence, it’s important to ensure payment platforms comply with necessary security protocols. Second, banks and Fintech companies must actively address security issues. Enterprises can deploy machine learning based on artificial intelligence to identify and reduce fraud. In fraud detection, it is more important to determine the source of fraud rather than the transaction itself. Third, information security has become a necessary component of the digital economy development policies of almost every country.

Countries are also introducing biometric measures to reduce fraud in digital payment processing. Measures that establish legal, institutional, technical and other mechanisms to protect information security and reduce payment fraud will provide solid security backing for development of the digital economy. Although network security and digital payment fraud cases are a substantial risk, the digital payment ecosystem can be strengthened, and organizations, users and governments should all play their part to ensure its security.

³ Observation Group of Digital Finance Research Center, Beijing University, “Observation Report on the Financial Technology of Four Asian Countries, February, 2019

⁴JPMorgan, Global Payment Trends, 2019

⁵WikiMili, Commission on Elections data breach, Apr 2016

5. Collaborate and communicate consistently across the region: A common requirement among participants in digital financial services is that policies should be consistent and predictable. Regulatory uncertainty is the biggest drag on investment and risks entire business models suddenly becoming infeasible. A fragmented regulatory landscape, such as substantial differences in licensing procedures, is a major challenge facing regional players operating across multiple markets. Without robust coordination, variations in local regulatory requirements can lead to higher costs and delays in businesses' regional expansion plans.
6. Encourage localised digital innovation and talent development: Due to the varying social and economic development conditions and customs of different countries, digital services that are in line with local considerations are more likely to be favoured by local consumers. Thus, encouraging local digital innovation can give work to each country's advantages and become a path to unique digital services.

Governments of South and Southeast Asian countries would do well by coordinating regulation related to the financial services industry across regions, which will help promote the development of regional business models and direct resources towards better technology and talent. For example, digital identification data, including digital IDs, and e-Know Your Customer processes, can significantly increase opportunities in digital financial services, including opportunities to serve the unbanked. Promoting common standards for payment and remittance will be key to promoting interoperability among solutions. Additionally, there is fragmented supervision across both regions. And because digital payments involve financial services, countries have very strict regulatory standards for multinationals. These may include business licensing, service scope, banking relations, and partnerships. To address these often heterogeneous standards, a unified payment platform or standard should be established at the national level. In sum, governments should establish communication and consultation mechanisms, eliminate unnecessary regulatory measures, unify standards as much as possible, and realize joint supervision and collaborative communication.

With rapid development of digital technology in South and Southeast Asia, there is a growing talent gap. Demand for the internet and financial talent is substantial, particularly in digital payments. Traditional training establishments struggle to provide a sufficiently large pool of such talent. Therefore, developing talent with "digital thinking" and an ability to adapt to fast-paced work have become key to the long-term, sustainable development of South and Southeast Asia digital economies. School-enterprise cooperation and international cooperation are two possible solutions to address this talent challenge. Through targeted training and cooperation, talent with solid financial and technological knowledge can be developed. Through international cooperation, companies as well as their potential employees can access the world's most advanced digital knowledge and concepts, and learn about the digital economy models of large multinational internet enterprises, which will in turn help improve local digital economic models.

Acknowledgements

Our *Voice of Asia* series brings to life the challenges and opportunities facing the region today and tomorrow. *Voice of Asia* is the result of significant collaboration across the Deloitte Asia Pacific and Global Network.

The following economists contributed to creating the rich tapestry of insights that feature in *Voice of Asia*, Edition 8 November 2020:

Manu Bhaskaran

CEO, Centennial Asia Advisors Pte Ltd;
Alliance Partner,
manu@centennialasia.com

Chris Richardson

Partner,
Canberra
chrichardson@deloitte.com.au

Rumki Majumdar

Associate Director,
Bengaluru
rumajumdar@deloitte.com

Roger Yun Tai Chung

Deloitte Research Director,
Shanghai
rochung@deloitte.com.cn

Spencer Yao

Clients & Industries Leader,
Taiwan
speyao@deloitte.com.tw

Shiro Katsufuji

Director,
Tokyo
shiro.katsufuji@tohmatsumoto.co.jp

SukKi Kim

Partner,
Seoul
sukkim@deloitte.com

Sitao Xu

China Chief Economist and Partner,
Voice of Asia Leader,
Beijing
sxu@deloitte.com.cn

Zoe Wallis

Chief Economist,
Wellington
zwallis@deloitte.co.nz

Deloitte.

Insights

Sign up for Deloitte Insights updates at www.deloitte.com/insights.



Follow @DeloitteInsight

About Deloitte Insights

Deloitte Insights publishes original articles, reports and periodicals that provide insights for businesses, the public sector and NGOs. Our goal is to draw upon research and experience from throughout our professional services organization, and that of coauthors in academia and business, to advance the conversation on a broad spectrum of topics of interest to executives and government leaders.

Deloitte Insights is an imprint of Deloitte Development LLC.

About this publication

This publication contains general information only, and none of Deloitte Touche Tohmatsu Limited, its member firms, or its and their affiliates are, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your finances or your business. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser.

None of Deloitte Touche Tohmatsu Limited, its member firms, or its and their respective affiliates shall be responsible for any loss whatsoever sustained by any person who relies on this publication.

About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. In the United States, Deloitte refers to one or more of the US member firms of DTTL, their related entities that operate using the "Deloitte" name in the United States and their respective affiliates. Certain services may not be available to attest clients under the rules and regulations of public accounting. Please see www.deloitte.com/about to learn more about our global network of member firms.

Copyright © 2020 Deloitte Development LLC. All rights reserved.
Member of Deloitte Touche Tohmatsu Limited

Designed by CoRe Creative Services. RITM0568304