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Abbreviations and Acronyms

ABMI	Asian Bond Markets Initiative	Lao PDR	Lao People's Democratic Republic
ADB	Asian Development Bank	LIBOR	London Interbank Offered Rate
AEM	Asia Economic Monitor	MSCI	Morgan Stanley Capital International
AMRO	ASEAN+3 Macroeconomic Research Office	m-o-m	month-on-month
AMU	Asian Monetary Unit	NIE	newly industrialized economy
ARIC	Asia Regional Integration Center	OCA	optimum currency area
		OECD	Organisation for Economic Co-operation and Development
ASEAN	Association of Southeast Asian Nations	OPEC	Organization of the Petroleum Exporting Countries
ASEAN+3	ASEAN plus People's Republic of China, Japan, Republic of Korea	OREI	Office of Regional Economic Integration
ASEAN-4	Indonesia, Malaysia, Philippines, Thailand	PCOMP	Philippine Composite Index
ASEAN-5	Indonesia, Malaysia, Philippines, Thailand, Singapore	PRC	People's Republic of China
BIS	Bank for International Settlements	PMI	purchasing managers index
bps	basis points	QE2	second round of quantitative easing
CMI	Chiang Mai Initiative	q-o-q	quarter-on-quarter
CMIM	Chiang Mai Initiative Multilateralization	repo	reverse repurchase
EMS	European Monetary System	saar	seasonally adjusted annualized rate
ERM	Exchange Rate Mechanism	SBI	Sertifikat Bank Indonesia
ERP	economic review and policy dialogue	SET	Stock Exchange of Thailand
EU	European Union	STI	Straits Times Index
FY	fiscal year	SVAR	structural vector autoregression
G20	Group of Twenty Finance Ministers and Central Bank Governments	TED	treasury bill and eurodollar futures contract
G3	US, eurozone, Japan	TWSE	Taipei, China's stock exchange index
G7	Canada, France, Germany, Italy, Japan, United Kingdom, United States	US	United States
GDP	gross domestic product	VAR	vector autoregression
IMF	International Monetary Fund	VIX	Chicago Board Options Exchange Volatility Index
IT	information technology	VNINDEX	Ho Chi Minh Stock Index
JCI	Jakarta Composite Index	WB	World Bank
KLCI	Kuala Lumpur Composite Index	y-o-y	year-on-year
KOSPI	Korean Stock Price Index		

Note: Unless otherwise indicated "\$" refers to US dollars

Emerging
East Asia—
**A Regional
Economic
Update**

Highlights

Recent Economic Performance

- Robust recovery was the norm across most of emerging East Asia in 2010, though moderating somewhat in the second half as stimulus was withdrawn; domestic demand continued to drive economic growth but at a slower pace.
- Inflation edged up on strong economic performance across the region.
- Balance of payments remained in surplus throughout the region amid healthy current account surpluses and continued capital inflows.
- Most emerging East Asian stock markets recovered dramatically in the second half following the region's rapid economic turnaround.
- Almost all of the region's currencies appreciated as capital continued to return to the region.
- Bond yield curves flattened in several emerging East Asian markets as monetary policies normalized, and yield curves in other economies shifted downward.
- Across the region, authorities continue to normalize macroeconomic policy and have begun introducing measures to manage capital flows.
- Fiscal consolidation continues across much of emerging East Asia, even as several governments continue spending to address structural reforms and ensure long-term growth.

- Financial vulnerability in emerging East Asia remains low as most economies maintain healthy fiscal balances and have low external debt; banking systems across the region should remain healthy, with strong capitalization, profitability, and low levels of nonperforming assets.

Outlook and Risks

- The external economic environment for emerging East Asia has weakened as the US economy continues to struggle and doubts remain over the sustainability of the eurozone recovery.
- With stimulus being withdrawn and the recovery intact, growth in 2011 should moderate as the post-recovery phase kicks in; economic growth is forecast at 8.8% for 2010, tapering to 7.3% in 2011.
- The economic outlook is subject to four major risks: (i) persistent weak growth in advanced economies; (ii) destabilizing capital flows; (iii) inflation and asset price bubbles in some economies; and (iv) protectionism.

Policy Issues

- With the V-shaped recovery in hand, many emerging East Asian economies now face the challenge of managing strong growth and capital flows amid a weaker external environment.
- Continued robust growth in many emerging East Asia economies suggests authorities are on track in normalizing macroeconomic policy.
- A "money first with somewhat faster appreciation" strategy for withdrawing stimulus seems appropriate for many emerging East Asian economies to both sustain economic growth, while helping rebalance the region's sources of growth.

- Mitigating the negative effects of surging capital flows will require an appropriate mix of sound macroeconomic management, flexible exchange rates, resilient financial systems, and—in some cases—temporary and targeted capital controls.
- Deeper and more comprehensive structural reforms are needed to improve productivity growth and to build an environment more conducive for private consumption and business investment.
- Rapidly growing interdependencies in trade and finance in the region and increasing importance of spillover and contagion effects make regional exchange rate cooperation essential.
- Regional dialogue leading to agreements on stabilizing exchange rates; pegging currencies to a basket of currencies or to each other; or adopting a common currency and forming a monetary union are three options for achieving cooperative exchange rate objectives.

Exchange Rate Cooperation: Is East Asia Ready?

- Regional exchange rate cooperation—if handled wisely—can ensure intra-regional exchange rate stability while allowing inter-regional flexibility, thus helping promote intra-regional trade and investment, and rebalance the region's sources of growth.
- Following the 2007/08 global financial crisis, intra-regional exchange rates have shown greater dispersion, potentially affecting the further expansion of intra-regional trade.
- For East Asia, cooperation needs to be “institution-lite” rather than based on the full range of institutions—a realistic short-term objective would be to reduce intra-regional exchange rate variability, while allowing exchange rates to respond to shocks outside the region.
- The region could start by adopting informal reference or monitoring zones for regional exchange rates to gradually reduce intra-regional exchange rate variability over time—the reference currency should come from outside the region and monitoring zones be wide enough to allow for some intra-regional flexibility.

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The Asia Economic Monitor is a semiannual review of emerging East Asia's growth and policy issues. It covers the 10 members of the Association of Southeast Asian Nations; People's Republic of China; Hong Kong, China; Republic of Korea; and Taipei, China. This issue includes a special section on exchange rate cooperation in East Asia.

About the Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries substantially reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to two-thirds of the world's poor: 1.8 billion people who live on less than \$2 a day, with 903 million struggling on less than \$1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.