MOODY'S RATINGS

SECTOR IN-DEPTH
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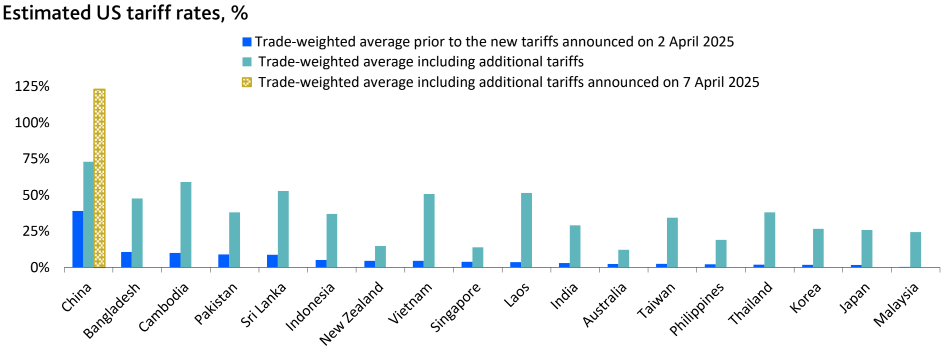
Tariffs – Asia-Pacific

Sweeping US tariffs will be credit negative for Asia-Pacific

US President Donald Trump's sweeping new tariffs announced on 2 April represent the largest increase in tariffs since the 1930s and the implications of these announcements are still unfolding across the world. Starting 5 April, a universal 10% tariff will be applied on all imports to the US (Aaa negative), and, starting 9 April, higher rates will apply to roughly 60 economies, around a third of which are in APAC. These newly announced tariffs will be in addition to most already existing tariffs and are likely to upend global trade dynamics. Some imports, such as pharmaceuticals and semiconductors, are excluded from the new tariffs for now. While there were no further tariffs for the automotive industry announced on 2 April, the previously announced 25% tariff on all US imported vehicles started on 3 April and similar tariffs on auto parts will start on 3 May.

The new tariffs on APAC economies are more draconian than market expectations and will be credit negative for the region, but with some differentiation. Some of the highest tariffs (>30%) were applied to a number of economies in the ASEAN bloc, such as Cambodia (B2 stable), Laos (Caa3 stable), Vietnam (Ba2 stable), Thailand (Baa1 stable) and Indonesia (Baa2 stable), as well as South Asian economies such as Bangladesh (B2 negative) and Sri Lanka (Caa1 stable). The elevated tariffs — on Cambodia and Vietnam in particular — are likely to close the third-country loophole[1] claimed by the US administration. However, at the time of writing, total new tariffs on China (A1 negative) will still be the highest across the region at 104% (50% new tariffs announced on 7 April on top of the 34% announced on 2 April, plus a previously imposed 20%) (see Exhibit 1).

Exhibit 1
China continues to have the highest tariffs, while regional economies see sharp increases
Estimated US tariff rates, %



The tariffs for China before the second Trump administration are according to Peterson's Institute for International Economics' estimates, with 20% rates announced in February stacked on top of the 34% rates announced on 2 April and 50% rates announced on 7 April. Tariffs for all other regional economies are based on 2022 Most-Favored-Nation weighted average rates. These tariffs do not include exemptions for autos, auto parts, steel and aluminum, semiconductors and pharmaceuticals.
Sources: World Integrated Trade Solution, White House, Peterson's Institute for International Economics and Moody's Ratings

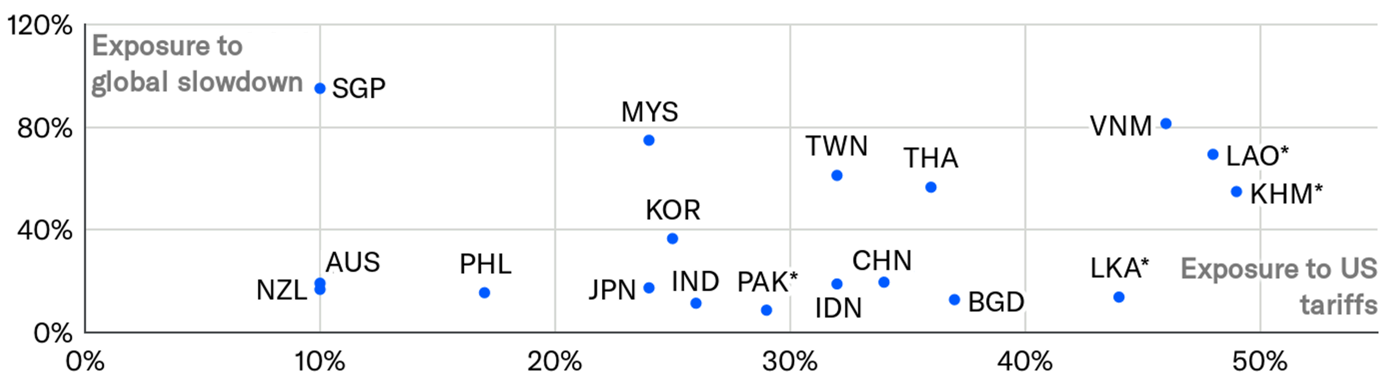
The new tariffs will hurt the 'China+1' strategy, and an acceleration in supply chain diversification away from China is more uncertain at this stage. However, APAC economies may still be incentivized to deepen trade and investment ties intra-regionally. Meanwhile, lower-tariff countries in the region may stand to gain market share on the margin from potential trade triangulation to serve the US market in the near term. For example, Malaysia (A3 stable), India (Baa3 stable) and the Philippines (Baa2 stable), which are subject to tariff rates in the middle band (10%-30% range), may benefit from some trade diversion activity. Economies in the region with large domestic markets, such as India, could also benefit from companies seeking to access large markets while keeping operating costs reasonable by shifting production to these economies but this would only happen over a number of years.

Having said that, the APAC sovereigns we cover account for around 40% of US goods imports and form the backbone of global supply chains. Tariffs of this magnitude will weigh on global trade activity, reduce demand for regional exports, and undermine business confidence, leading to reduced investment in APAC.

Even economies subject to the lowest tier of tariffs at the 10% baseline level, such as New Zealand (Aaa stable), Australia (Aaa stable) and Singapore (Aaa stable), will not be spared. While these economies face a smaller direct shock from US tariffs, these economies (Singapore in particular) have high exposure to a global trade slowdown (see Exhibit 2). Moreover, for Australia, New Zealand and Indonesia, a potential slowdown in Chinese final demand – China being their largest trading partner – would spill into lower demand for commodity exports.

Frontier markets such as Sri Lanka, Pakistan (Caa2 positive) and Bangladesh, which do not have the capacity to import as much from the US and whose current account balances are relatively fragile, could see a worsening of their broader external positions that will potentially weigh further on the outlook for economic growth.

Exhibit 2
Lower-income emerging economies are vulnerable to higher US tariffs and a global trade slowdown
Economies in the top right quadrant are more vulnerable



Cambodia – KHM; Laos – LAO; Vietnam – VNM; Bangladesh – BGD; Thailand – THA; Sri Lanka — LKA; China – CHN; Taiwan – TWN; Indonesia – IDN; Pakistan – PAK; India – IND; Korea – KOR; Malaysia – MYS; Japan – JPN; Philippines – PHL; New Zealand – NZL; Singapore – SGP; Australia – AUS.
Exposure to a global slowdown denotes exports as a % of a country's GDP in 2024. *2023 data. Exposure to US tariffs is defined by new US tariff rates imposed on its trading partners.
Sources: International Trade Centre, IMF, White House and Moody's Ratings

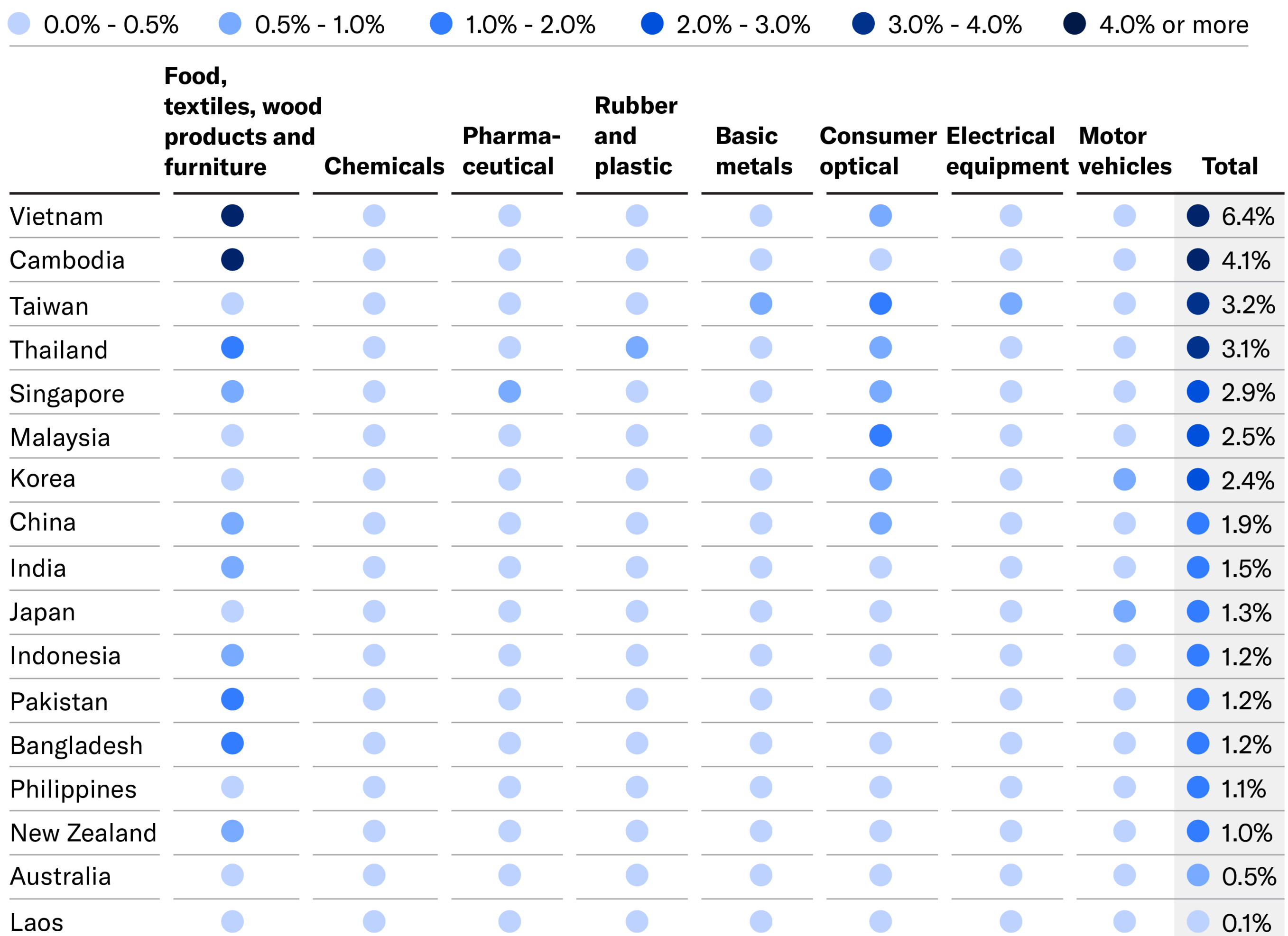
APAC exposed to higher tariffs directly and indirectly

APAC will be exposed to the higher US tariffs both directly and indirectly. Across the region, direct export exposure to the US is the highest for Vietnam, followed by Cambodia, Thailand and Taiwan, China (Aa3 stable) (see Exhibit 3). While Pakistan and Bangladesh have lower overall exposure, their exposure to the US is heavily concentrated in the food, textiles and wood products sectors. Exports in these sectors tend to have higher price elasticities and will therefore be more vulnerable to shortfalls in US demand. India also has a relatively low overall exposure but more diversified exports to the US. Across the region as a whole, electronics, machinery and equipment as well as food and textiles are among the most exposed sectors to US demand.

Exhibit 3

APAC economies have high exposure to US demand in a few key sectors

Domestic value added in gross exports to the US (% of respective country's GDP, 2020)*



*Latest year available. Value added in exports represents the value created within the exporting country during the production process and excludes the value of imported inputs used in that process.

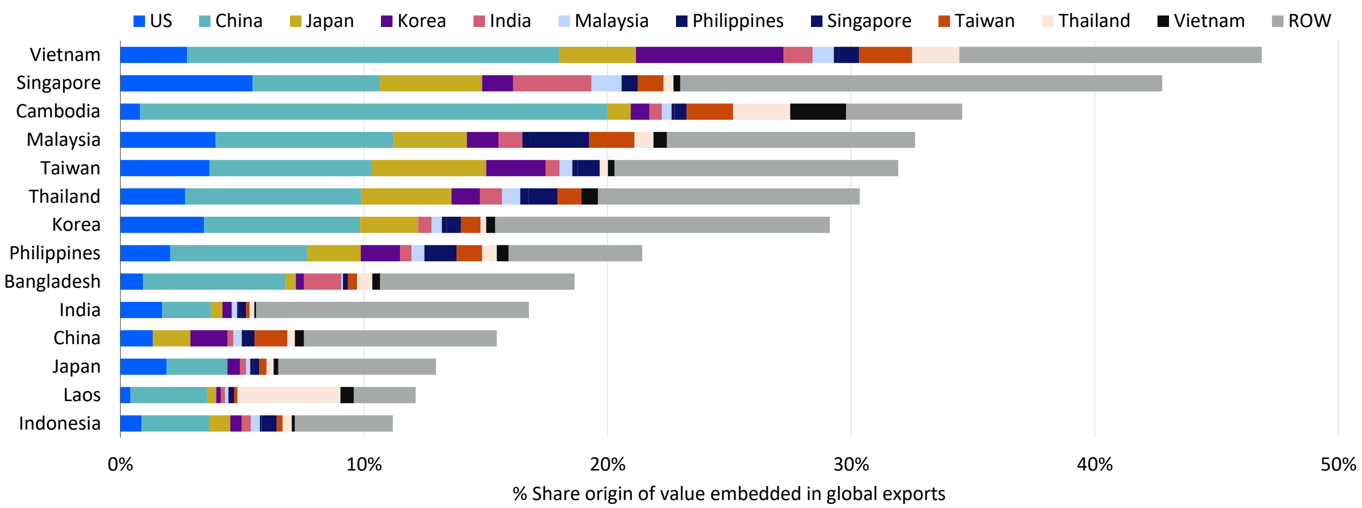
Sources: OECD Trade in Value Added and Moody's Ratings

In addition to direct export exposure to the US tariffs, countries in the region will also be indirectly exposed through their value-added contributions to other countries' exports. As Exhibit 4 shows, the region's supply chains are heavily linked to connector economies such as Vietnam, Singapore and Malaysia, the global exports of which contain significant value added from other Asian economies. For example, China, Korea (Aa2 stable) and Japan (A1 stable) are the largest contributors of value added to Vietnam's exports to the world.

Exhibit 4

Regional exporters contain high value added from other Asian countries

Origin of value added (% share, 2020)*



*Latest year available. To reflect the complexity of value chains, we show the value added by other countries through imported intermediate inputs used in a country's exports and exclude the exporting country's domestic value added.
Sources: OECD Trade in Value Added and Moody's Ratings

Both Japan and Korea have relatively high exposure to US vehicle tariffs, but the share of vehicles that Japanese and Korean automakers produce in the US to serve the US market is growing, which can help mitigate significant cost increases. Although automakers have been shifting production to the US, this will take time, and the immediate competitive threat for cars manufactured outside of the US remains. Taiwan may also face growing pressure to shift more chipmaking capacity to the US as part of future negotiations, although chips have been excluded from the higher tariffs for now.

China's government has announced a 34% duty on all US imports — set to begin on 10 April — matching President Trump's additional tariff on China announced on 2 April, breaking away from its previously more restrained responses. The government also further tightened export controls on rare earth minerals and retaliated against several US companies. The escalation in Sino-US trade tensions would be detrimental for the global economy and poses significant downside risks to the region's economic outlook.

This major shift in US trade policy is credit negative for APAC but we expect the vast majority of countries to negotiate rather than retaliate, through strategies such as seeking talks with the US (such as Singapore and Vietnam), establishing bilateral trade agreements (such as India) or buying more US goods (such as Thailand). Even through negotiations, APAC as a whole will face significantly higher tariffs than before.

Given a more restrictive trading environment and weakened investment sentiment, currencies of APAC economies, particularly those facing higher tariffs, could face continued downward pressure given potentially higher capital outflows. Financial market volatility could heighten refinancing risks of non-investment grade issuers. Currency depreciation could also exacerbate already weak debt affordability for frontier markets, although, for most parts of the region, adequate macroprudential buffers and sound monetary policy frameworks will partially offset the impact of external shocks. Some governments have taken steps to shore up activity. For example, Japan has announced loan support measures for small and medium enterprises in the autos supply chain, and Chinese sovereign fund Central Huijin is carrying out market stabilization operations in the stock market.

Given the disruptions that lie ahead for the world trading system as a result of the US trade policies, governments in the region will likely be further incentivized to achieve an enhanced degree of cooperation with one another. At the same time, regional economies will likely promote substitution of US exports with exports to other markets. With inflation near or at target for most economies in the region, central banks are likely to ease monetary policy more quickly to support growth. Meanwhile, tariffs will likely add to deflationary pressures in the region, as products that were previously sold in the US market will now need to be redirected elsewhere.

The fiscal policy response of governments to mitigate the negative impact of tariffs on growth could also potentially weigh on sovereign credit. Fiscal accommodation would threaten or otherwise disrupt the progress on gradual fiscal consolidation across the region, although higher debt burdens emerging from the pandemic will likely constrain the extent to which governments could provide support to their respective economies.

The impact on banks is credit negative, albeit at different levels, leading to heightened uncertainty for investors and consumers. On a relative basis, the higher tariffs will be more negative for banks in Vietnam, Thailand and Bangladesh because of their economies' higher reliance on exports to the US compared with other economies in the region

Endnotes

1 This refers to ASEAN increasingly sourcing inputs from China to feed into its manufacturing sector to serve the US market.

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