

ASIA MONTHLY

May 2010

<i>Topics</i>	<i>China's NPC pushes theme of sustainable growth</i>	1
<i>Korea</i>		3
<i>Hong Kong</i>		4
<i>Indonesia</i>		5
<i>India</i>		6



株式会社 日本総合研究所
The Japan Research Institute, Limited

<http://www.jri.co.jp/english/asia/index.html>

Topics *China's NPC pushes theme of sustainable growth*

At the NPC in March, though there were signs of slightly stronger inflationary concerns, the main economic management policy direction presented was one of sustainable economic growth, including plans for the continuation of monetary and fiscal policy and for a new growth pattern.

■ Great interest shown in review of economic policy

China's Third Plenary Session of the Eleventh National People's Congress (NPC) was held over ten days, between March 5 and 14. While the basic policy for the year's economic management is actually decided at the end of the previous year's Central Economic Work Conference, the concrete numerical targets, such as budgets and economic development plans, need to be officially announced and approved at the NPC. For that reason, the NPC is one of the most important conferences in terms of China's economic development.

Further, since the start of 2010, growing concerns over soaring real estate prices and inflation have become more pronounced (figure upper right). Given these circumstances, one of the most discussed points of this year's NPC was to what extent the economic management policy of prioritizing sustainable growth would be revised.

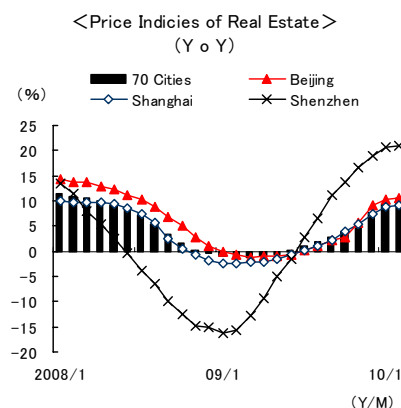
■ Concerns over economic relapse, policies presented aim at sustaining economic growth

From reports such as the 'Report on the Work of the Government' and others, the characteristics of the economic policy seen at this year's NPC can be summarized in the following three points. First, there is evidence of slightly stronger concern over inflation and with regard to spiraling real estate prices.

The government has set a target of around plus 3% for the CPI for 2010 (table lower right). This level is not only higher than the actual figures for 2009, but is also higher than levels since the start of 2010, and may be said to have incorporated the message that the government, one way or another, will try to control CPI increase to within 3%. The phrase 'keep the overall level of prices stable' has been added to reports like the 'Report on the Work of the Government', and the government's desire to keep commodity prices stable has been felt all the more keenly since the Central Economic Work Conference at the end of 2009. Further, although limited to some cities, there appears to be a much stronger resolve to curb spiraling real estate prices.

Nevertheless, at a press conference held during the NPC, the People's Bank of China (China's central bank) governor, Zhou Xiaochuan, expressed his concern over inflation and commented that, as the government shifts its priority from policies in response to emergencies to policies in response to normal circumstances, it should do so with caution. These comments would suggest that the government is not disposed towards any drastic change to the tight monetary policy.

Second, it is certain that the government intends to continue with the implementation of policies geared towards sustaining growth. The government has set a growth rate target of around 8% for the whole year 2010. When the fact that the Eleventh Five Year Plan (2006 to 2010) had an annual growth rate of 7.5% as



Source: National Development and Reform Commission, National Bureau of Statistics

2010 Major Economic Targets

Index	Main points
Economic numeric targets	<ul style="list-style-type: none"> • Economic growth rate target set for approx. 8% • Consumer price index increase rate restrained to approx. 3%
Financial numeric targets	<ul style="list-style-type: none"> • M2 growth rate target approx. 17% • Annual new lending total target approx. 7.5 trillion yuan
Fiscal and monetary policy	<ul style="list-style-type: none"> • Continue with 'positive fiscal policy', with a deficit of 1.05 trillion yuan → Deficit bigger than previous year by 100 billion yuan • Continue with 'appropriately relaxed monetary policy'
Growth model switch	<ul style="list-style-type: none"> • Prioritize the completion of important investment projects, and examine new applications more strictly. → Appropriately restrained target of 20% total social fixed asset investment for the year • Energetic expansion of private consumption as well as the continuation and expansion of government subsidies in support of new and replacement purchases of household appliances and automobiles • Promotion of growth industries, including alternative energy, energy conservation, environmental protection, biotechnology and pharmaceutical, etc.

Source: Report on the Work of the Government

its target, and that in the years from 2006 to 2009 the growth rate was well over the target, is taken into account, a slightly lower growth target could have been set. 8% seems likely to have been set because this level of growth is essential to the creation of employment.

Also, fiscal and monetary policy has still prioritizes growth support. Fiscal policy will continue to be positive, and the fiscal deficit for 2010 is expected to be China's biggest ever at 1.05 trillion yuan (figure upper right). Much of the money is earmarked for the completion of major projects, and the continuation and enhancement of measures designed to encourage consumption. In terms of monetary policy, a target of around 7.5 trillion yuan worth of new lending has been set for the year. This is below the 9.6 trillion yuan of new lending in 2009, but is well above the levels of 2007 and 2008, which had tighter monetary policies.

Third, there have been concrete indications of a switch in the growth pattern, or growth engine. The 'Report on the Work of the Government' calls for the energetic expansion of private consumption and, in addition to direct measures such as the continuation and expansion of government subsidies in support of new and replacement purchases of household appliances and automobiles, there are also initiatives to help increase the incomes of low income earners and farmers, by raising the minimum standard of living security level and pension payments. Elsewhere in the Report, there is clear mention of 'improving people's lives' (such as reviewing income distribution and correcting income disparity) and 'the driving force of economic development', and it is clear that the government considers these initiatives as contributing to the sustainable expansion of consumption overall.

In contrast, with regard to investments, while the government is committed to carrying out major investment projects, it has made it clear that it will conduct very rigorous inspections with regard to new proposed projects. In the National Economic and Social Development Plan, reported at the NPC on March 5, a target of 20% year on year increase in total social fixed asset investment has been set, significantly restrained in comparison with 2009's growth figure (30.1%). Given the falling percentage of GDP occupied by household consumption, from the perspective of sustainable growth, it would be reasonable to assume that that aim has been to switch the growth pattern from investment-led to consumption-led (figure lower right).

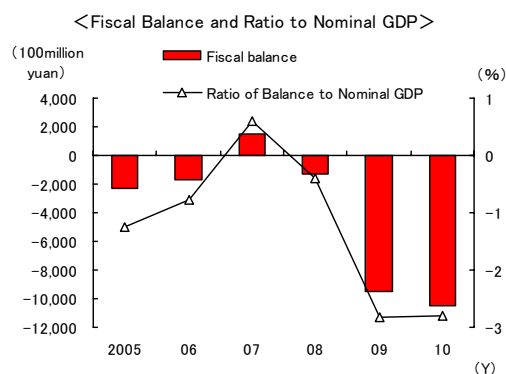
At the press conference at the closing of the NPC on March 14, Premier Wen Jiabao commented that fears of a global economic double dip also concerned China, and that economic recovery depended greatly on policy measures, and could not be considered autonomous. It must be said that the press conference strongly reflected the government's cautious economic forecast and intention to continue with policies designed to sustain economic growth.

■ **'Fine tuning' of policy measures continues as issues are tackled head on**

As China's economy sustains 8% growth and the government attempts to switch its growth pattern, the biggest issue will be how best to deal with inflation and the soaring prices of real estate. The government is gradually tightening control, recovering excess liquidity and ordering 78 state-owned enterprises whose main business is not real estate to withdraw from real estate dealings, and other such activities. It is assumed that this kind of progressive review (fine tuning) will continue for the time being. Nevertheless, while the government has announced its intention to continue with appropriate easier monetary policies, the danger is that it will miss its chance to implement inflation evasion measures. On the other hand, there is also a danger that early and overly simple price countermeasures will disrupt the pace of economic recovery. The government faces the same dilemma with regard to the control of soaring real estate prices.

Giving consideration to the trends shown in economic indices and polls, the Hu Jintao administration will need to work ever harder to produce a balanced economic management style that can deliver both sustainable growth and stable prices.

(Junya Sano)

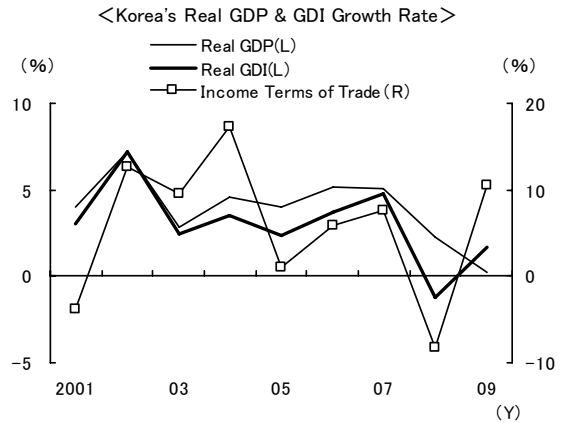


Note: Fiscal figure in 2009, 2010 and the ratio of deficit to Nominal GDP in 2010 are shown by the Budget Reports 2010
 Source: National Bureau of statistics, the Budget Reports 2010

Korea Lower income families feel the impact of continuing depression

Low income earners see earnings fall further

In recent years, Korea has experienced a worsening of its income terms of trade (income flowing abroad), leading to a situation where its real GDI (Gross Domestic Income: including operating surpluses and indirect taxation, in addition to employees' remuneration) growth rate is continually lower than its real GDP growth rate (so that even if there is economic growth, incomes fail to grow). The government's swift implementation of economic countermeasures in 2009 paid off and real GDI growth was 1.7%, exceeding 0.2% growth for real GDP. This was due to an improvement in the income terms of trade resulting from falling crude oil prices from the start of autumn, 2008. However, as real GDI contracted in 2008, it needs to be borne in mind that incomes have shown almost no growth at all in the last two years.



Source: The Bank of Korea, *Economic Statistics System*

According to the 'Household Income and Expenditure Survey' (National Statistics Office), average household incomes (for 2009) posted 1.5% nominal growth, which is minus 1.3% real growth. By income level (Yearly Income Quintile Group), nominal disposable income (income remaining after taxes, social security and other 'non-consumption expenses' are deducted) grew negatively in Group 1 (lowest 20% of households) at minus 3.1%, and positively in Group 2: 2.0%, Group 3: 1.8%, Group 4: 1.1%, and Group 5: 0.7%, indicating the depth of the income slump at the lowest level. This is also closely connected to an increased poverty rate and an expanding income disparity. The Gini coefficient (the closer to 1, the greater the inequality) for 2009 was slightly below that of the previous year but the relative poverty rate continues to rise and the income disparity between those at the highest and lowest levels continues to grow.

The current recession has caused a lot of unemployment among the self employed and irregular workers. These people have few savings and so the risk of falling below the poverty line is great. Therefore, the government has introduced living support measures (expanded eligibility of basic livelihood security payments, and other types of livelihood support) for those on low incomes. On an income basis, the relative poverty rate rose from 17.5% to 18.1%, but on a disposable income basis the rise was only from 15.0% to 15.2%, indicating that the policies have been effective to a degree, but have not been able to prevent an increase in the number of poor households.

Employment creation needed

In an attempt to minimize the deterioration of the employment situation, the government has implemented a range of measures, including 1) raising the subsidy rate of employment adjustment subsidies, 2) support for work sharing, and 3) temporary employment services. As a result, the increase in the unemployment rate (seasonally adjusted) is believed to have been restrained (during the period January, 2008, to December, 2009, the highest was 3.9%, in June, 2009). However, though temporary employment services were suspended, employment seeking activities were vitalized, bringing the rate up to 4.8% in January, 2010 (4.4% in February). Thus, the private sector's employment creation capacity is extremely weak.

The government is attempting to expand investment and create employment through the promotion of the Green New Deal projects and new service industries (medicine, education, logistics, contents, broadcasting and communications, consulting, etc.). Recently, the government has also been trying to foster middle sized companies with global competitive strength. President Lee Myung-bak's true worth will be tested by whether his government is able to enhance support measures for low income earners while developing new domestic industries and creating high quality employment opportunities.

(Hidehiko Mukoyama)

Hong Kong Economic recovery continues, exit strategies vital

■ Economy stays on recovery course

Hong Kong's economy has continued to recover since the beginning of 2009. In the fourth quarter of 2009, GDP increased by 2.6% in real terms over a year earlier (2.3% up on the previous period), thanks to the rally in domestic and foreign demand.

Growth in exports of goods was minus 2.6% in the fourth quarter of 2009, compared to the same period in the previous year, moderating from the 13.2% decline in the third quarter of 2009 (up 7.5% on the previous period), thanks to a recovery in exports to China. Growth in exports of services was up 7.7%, similarly (up 2.1% on the previous period), due to the recovery in transit trade and increased numbers of travelers from the Chinese mainland.

In terms of domestic demand, private consumption expenditure grew by 4.9% in the fourth quarter of 2009 over a year earlier (up 2.1% on the previous period), encouraged by rising asset prices and improvements in the employment situation, maintaining the recovery trend. Gross domestic fixed capital formation increased by double digits compared to the same period in the previous year, up 14.7%, due mainly to improved corporate earnings.

In the period January to February, 2010, exports to China grew by a massive 36.1%, compared to the same period in the previous year. Meanwhile, exports to the US recovered at a gentler pace, growing 4.1%, similarly. Total retail sales for January to February were up 15.1% in volume, similarly, picking up the pace significantly from 10.0% growth in the period October to December 2009.

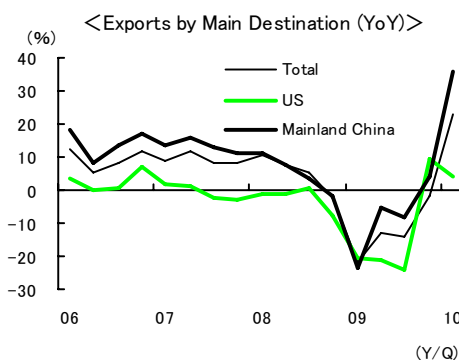
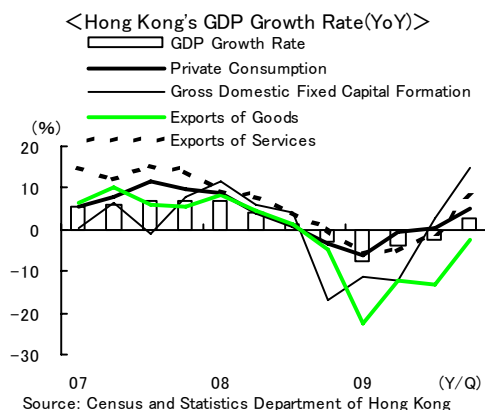
The economic recovery and government unemployment measures helped the unemployment rate for the period December, 2009, to February, 2010, to come down to 4.6%, shaving 0.3 points off the figure for October to December, 2009. In terms of specific industries, improvements in domestic demand related industries, such as retail, accommodations and food services, showed remarkable improvements.

■ Focus on exit strategies

As the economy maintains the recovery trend, Hong Kong's government has worked out its exit strategy. First, the special Credit Guarantee Plan for small and medium sized enterprises will be scrapped. The Plan, which started at the end of 2008, provided for a higher portion of government assurance in loans to small and medium sized enterprises, as well as higher loan limits. According to the government, the Plan has encouraged banks to approve more than HK\$68 billion worth of loans so far, and helped address the credit crunch. 16,000 companies benefited and, indirectly, some 280,000 jobs were protected. Applications to the Plan will be accepted up until the end of June, 2010. Also, plans to reduce the scale of salary tax reductions are drawing attention. In fiscal 2009, the salary tax reduction was 100% (with a ceiling of HK\$8,000). In fiscal 2010, this has been scaled back to 75% (ceiling: HK\$6,000).

While there are concerns over what will happen when the policy effects are removed, the impact is expected to be limited. Given that bank lending for 2009 was HK\$3.3 trillion, the extra financing provided under the Credit Guarantee Plan was a mere 2% of the total. Therefore, there is only a slight possibility that the cancellation of the Plan will cause enterprises' investment sentiment to cool drastically. And it is the custom in Hong Kong to pay the salary tax in one lump at the end of the financial year, so the negative effect within 2010 of reducing the scale of tax cuts is thought likely to be slight.

(Shinichi Seki)



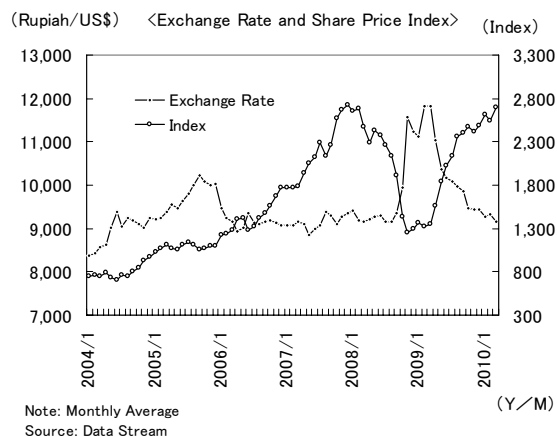
Note: The figures in 2010Q1 are for January–February.
Source: Census and Statistics Department of Hong Kong

Indonesia Speed of reform needs to pick up pace

■ Share prices rising, commodity prices settling

March's composite share price index (monthly average) was 2,691, close to December, 2007's record high. Part of the background to the rising share prices has been the fact that, since Indonesia's economic growth rate is expected to be higher than that of neighboring Asian countries, the rupiah has been solid, causing domestic and foreign capital to flow into the stock market. The rupiah - dollar exchange rate for March was 9,164 rupiah (monthly average), up 22.5% compared to the same month in the previous year, placing the rupiah as the best performing currency in Asia.

Commodity prices are also stabilizing at low levels. March's consumer price index increase rate was 3.4%, compared to the same period in the previous year, down from 3.8% in February. In response, Central Bank decided at its Monetary Policy Decision for April to keep the policy interest rate (BI rate) at 6.5%. Although the government has come in for some strong criticism for the delay in tackling domestic political issues, such as corruption, and for the major delay in infrastructure development, these issues have not, as yet, had any apparent effect on share prices or the exchange rate. President Yudhoyono would like to beat the government's forecast of 5.5% economic growth and to increase his administration's level of cohesive force.



■ Concerns over rising crude oil prices

That having been said, attention needs to be paid to the direction of commodity prices. Crude oil futures rose to \$86 a barrel in early April, the highest level in 18 months. Should the situation of new record highs continue, the impact will inevitably reach commodity prices. Any rise in commodity prices will very likely dampen individual consumption, which bolsters economic growth.

There is a growing sense of unease with regard to the expanding fiscal deficit. The budget for fiscal 2010 assumes a crude oil price of \$65 a barrel. Indonesia has a fuel subsidy system, so an increase in the price of crude oil will likely lead to a swelling of the fiscal deficit. However, if the price of crude oil can be contained to a level of \$80 a barrel, then the fiscal deficit ratio against GDP will only increase from the originally planned 1.6% to 1.7%, a margin that is hardly likely to bring about capital outflow or rupiah selling.

In his first period in office, President Yudhoyono cut fuel subsidies twice, and was able to strengthen fiscal health. This was a clear signal, both domestically and overseas, that the government prioritized financial discipline, and was a major factor in winning praise for Indonesia's economy. Nevertheless, although cuts have been made, fuel subsidies are a huge expense, 157.8 trillion rupiah, second after personnel costs (158.1 trillion rupiah), and well in excess of the 83.2 trillion rupiah in development expenses aimed at infrastructure provision.

In order to change the country's economic structure into one where government finance is not swayed by the price of crude oil and where there can be more development expenditure, a further round of subsidy cuts is indispensable. The government has made clear its intention to discontinue electricity subsidies by March, 2014. The reason is, naturally, to reduce the fiscal burden, and also to escape the vicious cycle where suppressing charges removes the incentive to invest in state run power companies, which then leads to power shortages.

The direction of reform is correct. What is lacking is a sense of urgency. In order to increase his administration's cohesive force and to achieve the mid term target of 7% economic growth by 2014, President Yudhoyono will need to exercise bold leadership and change criticism of the domestic political scene into driving energy for reform.

(Yuji Miura)

India Economic expansion sustained

■ 6.0% real GDP growth in October to December, 2009

India's real GDP grew by 6.0% (compared to the same period in the previous year) in October to December, 2009, down from 7.9% growth in July to September. In terms of industrial origin, agriculture grew minus 2.8%, industry 11.6%, and services 6.3%. Poor rainfall in the period June to September caused the agricultural sector to grow negatively. In industry, improvements in corporate sentiment and the financing environment boosted by recovery in the global economy caused vigorous production activity, and the manufacturing sector grew rapidly by 14.3%. Indices of industrial production show that production of capital goods and consumer durable goods enjoyed healthy growth, reflecting solid domestic demand. Also, increases in infrastructure and private housing construction meant that the construction sector was able to maintain a high 8.7% growth.

The quarterly growth of services fell into the 6% range for the first time since January to March, 2002. A major factor here is that community, social and personal services fell to minus 2.2%. This was due to the fact that, compared to the same period in the previous year, which was just after the Lehman shock, government expenditure growth fell drastically. By contrast, trade, hotels, transport and communications growth accelerated to 10.0%.

■ Future outlook and concerns

As described, manufacturing and private sector services are enjoying high growth levels and the economy may be said to be firmly on track to recovery. Whereas fiscal 2009's real GDP growth will be around 7%, growth of around 8% is projected for fiscal 2010. Given the further improvement in consumer and corporate sentiment, domestic demand growth will accelerate, and the export recovery since the middle of last year is expected to continue.

Improvements in the employment and income situation are expected to continue, leading to higher growth in personal consumption. In the urban areas, fast recovery in investments will lead to the expansion of employment opportunities in construction and other industries, and double-digit growth is expected in salaries, principally of government officials and others in the organized sector. Further, in the rural areas, the implementation of agricultural policies such as employment promotion programs, recovery in agricultural production, and increased agricultural credit and debt waivers will surely bolster an increase in farmers' purchasing power. Also, in terms of fixed capital formation, major improvements in corporate earnings are expected to be followed by the implementation of many investment projects. Solid inward direct investment will also play a supporting role.

One item of concern for the future is inflation. Currently, around 60% of rising wholesale prices is accounted for by foodstuffs and related products. Therefore, in the future, as agricultural production improves, the inflation rate will likely trend downwards. However, fuel prices have been rising since late November, domestic demand is likely to increase further in the months ahead, and an increase in capital inflow from abroad is expected. Therefore, the inflation pressure is expected to continue. The Reserve Bank raised policy interest rates by 0.25% in March. As the fiscal expenditure growth will fall in order to reduce the deficit, The Reserve Bank has to care about maintaining economic recovery even in a tight monetary stance.

(Satoshi Shimizu)

<Real GDP Growth Rates by Industrial Origin>

	FY2008					FY2009			
	Apr.-Jun.	Jul.-Sep.	Oct.-Dec.	Jan.-Mar.	Apr.-Jun.	Jul.-Sep.	Oct.-Dec.	(yoy. %)	
Real GDP	6.7	7.8	7.7	5.8	5.8	6.1	7.9	6.0	
Agriculture	1.6	3.0	2.7	▲ 0.8	2.7	2.4	0.9	▲ 2.8	
Industry	3.9	6.0	6.1	2.3	1.4	5.0	8.3	11.6	
Mining, quarrying	3.6	4.6	3.7	4.9	1.6	7.9	9.5	9.6	
Manufacturing	2.4	5.5	5.1	0.9	▲ 1.4	3.4	9.2	14.3	
Elec., gas & water	3.4	2.7	3.8	3.5	3.6	6.2	7.4	4.9	
Construction	7.2	8.4	9.6	4.2	6.8	7.1	6.5	8.7	
Service	9.7	10.2	9.8	10.2	8.6	7.8	9.3	6.3	
Trade, hotels, transp., comm.	9.0	13.0	12.1	5.9	6.3	8.1	8.5	10.0	
Fin., insur., real est.	7.8	6.9	6.4	8.3	9.5	8.1	7.7	7.8	
Comm., social, perso. services	13.1	8.2	9.0	22.5	12.5	6.8	12.7	▲ 2.2	

Source: Center for Monitoring Indian Economy