Emerging Economies and Changing Trade and Investment Patterns in Asia
—New Rivals for China—

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Summary

1. The economic environment in Asia is going through a period of major changes. One of those changes is a shift in China’s economic direction. Another is the growing presence of a new generation of emerging economies in China’s wake. These include India and Vietnam in Asia, and Russia, Brazil and the Middle Eastern Gulf States in other regions. The accelerating growth of these economies is having a significant effect on the Asian economic environment.

2. China assumed the role of Asia’s economic driving force in the second half of the 1990s. However, trends in recent years have characterized by (1) the increasing stability of the ASEAN economies, (2) the provision of growth opportunities to other Asian economies, especially by India and Vietnam, and (3) the growth of Asian economies through expanding relationships with non-Asian emerging economies. These trends have been accompanied by a decline in the weight of the United States in the world economy, and in its ability to influence Asia.

3. Emerging economies are also raising their profile in a global context. The value of world exports has shown double-figure growth since 2003 and increased by 15.3% in 2006. While the United States and the EU recorded steady export of growth of 14.7% and 12.3% respectively, China’s export growth rate reached 27.1%. Emerging economies, such as Russia and Brazil, which are classed as “Other regions,” also achieved remarkable export growth.

4. There have been three key trends in export activity in Asia over the past few years. First, China’s exports continue to show high growth. Second, India’s exports are also rising, although the total remains low in value terms. Third, trade within the Asian region is expanding. Emerging economies, such as India and Vietnam, are starting to contribute to the expansion of intraregional trade.

5. The world total of direct inward investment reached a peak in 2000 and then began to decline. It returned to a growth trend in 2003, and the total for 2006 was 38.1% above the previous year’s level. Cross-border M&A by developed countries increased by 45.3% year-on-year, reflecting factors that include global economic expansion, increased business earnings and low interest rates. The growth rate for developing countries was 20.6%, and that for South-East Europe and the CIS was 97.5%.

There have been three key trends in investment in Asia. First, the tendency for investment to be concentrated in China, which was apparent at the start of this decade, has started to wane. Second, investment in ASEAN is tending to increase. Third, India has become a major recipient of investment. In 2006, direct investment in India reached approximately one-quarter of the total for China. There are signs that major investors in Asia, including Japan, South Korea and Taiwan, have started to diversify their investment targets to a greater or lesser degree.

6. The rising profile of emerging economies and policy changes in China are expected to bring further change in trade and investment patterns in Asia. Industrialization is spreading to India, Vietnam and their neighbors, and the resulting creation of employment opportunities has provided the potential to alleviate poverty problems. Governments will need to ensure that the benefits of growth are widely distributed through infrastructure improvement and human resource development. They will also need to take appropriate steps to counter the risk of increasing disparity as a consequence of the industrialization process.
Introduction

In the second half of the 1980s, bonds of interdependence began to evolve across East Asia through trade and direct investment, spreading economic dynamism throughout the region. In the early 1990s, China stepped up the pace of its “reform and open-door” process and entered a period of consistently high economic growth. There was also a shift of production activity into China through direct investment and contract production, especially from Japan, South Korea and Taiwan. This led to increased trade between China and other Asian economies and brought dramatic changes in trade and investment flows within the region.

Changes are again starting to affect the economic environment in Asia. One of those changes is a shift in China’s economic direction. Within China, the consequences of continuing high growth have included increasing disparity, overheated investment, and increasingly serious energy and environmental problems. It has also produced expanding imbalances, including a gigantic trade surplus and trade friction. The Chinese government has responded by adopting the development of a “harmonious society” as its long-term goal. The aim is to make a transition to stable growth through policies targeting growth in rural incomes, regional development, and gradual reform of the currency system, as well as major environmental initiatives.

Another change is the growing presence of a new generation of emerging economies in China’s wake. The accelerating growth of India and Vietnam in Asia, and Russia, Brazil and the Middle Eastern Gulf States in other regions has started to have a significant effect on the Asian economic environment. Of particular importance is the conspicuous economic progress made in recent years by India, which has traditionally been regarded as a stagnant, impoverished economy. Like China, India is a population giant, and it is difficult to predict the impact of growth in its economy.

The profile of the Association of Southeast Asian Nations (ASEAN) has also started to rise again. One reason for ASEAN’s increasing importance is the expansion of foreign direct investment in response to increasing economic stability and progress toward regional economic integration.

This article analyzes the phenomena now occurring in Asia from the perspective of their relevance to global economic trends and presents a scenario for Asia’s future economic direction. Part 1 examines Asia’s current economic environment and analyzes changes compared with the situation at the start of this decade. Part 2 and 3 show how these changes are being manifested in trade and investment. Part 4 presents a scenario for Asia’s future economic direction and studies some of the issues confronting the region.

1. Changes in Asia

Asia’s current economic environment is analyzed in this section, together with changes compared with the situation at the start of the present decade.

(1) The Emergence of New Growth Factors

Ten years have passed since the currency crisis that struck Asia in 1997 and 1998. In recent years Asia has generally enjoyed stable growth, reflecting not only export growth driven by the expansion of the world economy, but also expanding domestic demand (1) (Fig. 1). The most important feature of this 10-year period is China’s role as Asia’s economic engine. However, with a growth rate exceeding 8% over the past few years, India has also emerged as a driving force. The impact of this shift to sustained economic growth has been further magnified by India’s status as a population giant, and by its past image as an economy strongly characterized by stagnation and poverty. This phenomenon can best be described as the “India shock.”

The Asian economy is expected to maintain relatively high growth in 2008, despite moderate deceleration caused by soaring crude oil prices and the slowdown of the U.S. economy in the wake of the subprime mortgage crisis. Asian regional growth will be boosted by strong growth in China and India, both of which have large gross domestic products (GDPs), as well as by the factors list-
ed below. These factors characterize the present state of the Asian economy and will determine its future direction.

First, the ASEAN members are achieving greater economic stability. Evidence of this change includes the growing importance of domestic demand as a growth driver. Malaysia’s real GDP growth rate (hereinafter referred to simply as “growth rate”) in the July-September quarter of 2007 was 6.6%, compared with 5.8% in the April-June quarter. Private consumption expenditure increased by 14.0%, while fixed capital formation showed 13.5% growth, reflecting the launch of the ninth five-year plan (2006-2010) and increased foreign direct investment. Indonesia recorded 6.5% growth in the July-September quarter, with fixed capital formation rising by 10.4% and private consumption expenditure by 5.1%. One reason for the expansion of domestic demand is a fall in the rate of increase in consumer prices, accompanied by a reduction in interest rates, since the second half of 2006. The Philippines has also continued to achieve high growth, at 7.5% in the April-June quarter and 6.6% in the July-September quarter. Price stability and remittances from overseas workers are helping to boost consumer spending. Despite concern about the impact of the September 2006 coup, Thailand’s growth rate has remained above 4%. The July-September quarter growth rate of 4.8% was 0.5 points above the result for the April-June quarter. This performance reflects not only firm export trends, but also a recovery in domestic demand. Private consumption expenditure grew by 1.8% in the July-September quarter, compared with 0.9% in the April-June quarter. Fixed capital formation grew by 2.6% in the July-September quarter after registering growth of 0.2% in the April-June quarter.

Apart from cyclical factors, the comparatively strong performance of the ASEAN economies can also be attributed to the improvement of fundamentals, including a positive shift in the current account balance of payments and the reduction of fiscal deficits, as a result of economic reforms implemented after the currency crisis (Fig. 2). In addition, foreign direct investment in ASEAN is tending to increase because of regional economic integration, and also because of deterioration in China’s investment environment, including rising wages and the revaluation of the yuan. (These aspects are discussed in Part 3, which examines recent trends in Asia from the perspective of direct investment.) The increased concentration of foreign direct investment in China at the start of this decade led to fears of economic subsidence in

Fig. 1 Real GDP Growth Rates of Key Asian Economies

Fig. 2 Fiscal Balances of the Philippines and Indonesia (Relative to GDP)
ASEAN. It is significant that foreign direct investment has again started to flow into ASEAN.

Fixed capital formation ratios (nominal fixed capital formation/nominal GDP) fell sharply after the currency crisis and are still falling in Malaysia and the Philippines. However, the ratios for Thailand and Indonesia have shifted to upward trends \(^{(2)}\) (Fig. 3).

Second, the rising profile of emerging economies in Asia, notably India and Vietnam, is creating growth opportunities for other Asian economies. Since independence, India suffered decades of economic stagnation resulting from government control over private business activity, and a continuing emphasis on industrialization through import substitution. A severe shortage of foreign currency in 1991 prompted economic reforms centering on the reduction of the public sector, the abolition of industry licensing, trade and foreign exchange liberalization, and the acceptance of foreign investment. Since that time, India has become increasingly integrated into the global economy, as evidenced by trade growth and increased foreign direct investment (Fig. 4). The yearly growth rate of the Indian economy reached 8.4% in fiscal 2005 (April 2005-March 2006), 9.4% in fiscal 2006, and 9.1% in the first half of fiscal 2007. The main driver of this growth is the service sector, especially IT-related services such as data processing and systems development \(^{(3)}\). India has been especially successful as a provider of offshore services (work carried out for overseas customers), and this type of service has become a major export industry. Local businesses, such as Tata Consultancy Services and Infosys Technology, are key players in this field.

**Fig. 4 The Openness of the Indian Economy**

[ Graph showing proportion of trade to GDP and proportion of direct investment inflows to GDP ]

**Fig. 3 Trends in Fixed Capital Formation Ratios**

[ Graph showing trends in fixed capital formation ratios for various countries ]

Notes: Fixed capital formation ratio = nominal fixed capital formation ÷ nominal GDP

Source: Same as for Fig. 1
Vietnam is also achieving high growth. Its growth rate reached 8.4% in 2005 and 8.2% in 2006. Procedures for the establishment of new businesses were simplified under the new company law, which took effect in 2000. The number of new private businesses created has surged as a result, and there has also been an increase in foreign direct investment. These factors have led to export growth.

At present the biggest export category is textile products. However, exports of electrical and electronic goods are also expanding, and this is now the biggest export category after footwear, seafood and timber products. Substantial investment from South Korea, Japan, Taiwan and other sources is giving Vietnam the potential to rewrite the industrial map of Asia.

As discussed later in this article, the accelerating growth of India and Vietnam is also creating new growth opportunities for other economies, including opportunities for increased exports from Asian economies to these two countries.

Third, another source of growth for Asian economies is their expanding relationships with emerging economies in other regions. While Asia’s status as the world’s growth center remains unchallenged, recent trends have been characterized by the proliferation of growth regions, including the rise of emerging economies in regions other than Asia. There is room for debate over which countries should be classified as emerging economies. However, Brazil, Russia and the Gulf States of the Middle East all appear to qualify.

Rapid reforms pushed Russia into a period of hyper-inflation in the second half of the 1990s. Prices have since stabilized gradually, and since 2003 Russia has consistently achieved growth in excess of 5%, reflecting increased exports of crude oil and natural gas. In 2007, China and South Korea recorded increases of 79.9% and 56.2% respectively in their exports to Russia.

At 3.7% in 2006, Brazil’s growth rate is lower than those of China, India and Russia. However, its per capita GDP is the highest among the BRICs (Fig. 5). In recent years it has gained increasing prominence as a major supplier of resources, including iron ore, soybeans and crude oil. Particularly significant is its new role as a supplier of resources to China. China now accounts for 6.1% of Brazil’s exports and is that country’s third biggest export market after the United States (17.8%) and Argentina (8.5%). Imports from China are also growing. As with exports, China is ranked third among Brazil’s sources of imports.

Rising crude oil prices have accelerated economic growth in the Middle Eastern Gulf States. Saudi Arabia and the United Arab Emirates (UAE) have consistently recorded growth in excess of 5% since 2003 (Fig. 6). In recent years the scope of investment has expanded to include non-petroleum sectors, such as finance, manufacturing and service industries. The growth of domestic infrastructure investment and consumer spending has been accompanied by increased exports of goods and services from Asia, and by expanding flows of investment, tourism and remittances from the Gulf States to Asia. In 2007, South Korea’s exports to Saudi Arabia increased by 35.2% year-on-year, and there was also a dramatic increase in construction orders from Middle Eastern countries.

Many people from India and the Philippines travel to the Gulf States as migrant workers. In 2006, the biggest source of remittances to the
Philippines from overseas workers was the United States, followed by Saudi Arabia, Canada, Italy and the United Kingdom (Table 1). These overseas remittances are contributing to the expansion of domestic consumer spending and housing investment, and in recent years funds from this source are being applied to social development through microfinance (4).

(2) The Declining Influence of the U.S. Economy

As suggested by the preceding discussion, the ability of the U.S. economy to influence the Asian economy appears to be waning. An obvious example of this change is the declining reliance of Asian economies on exports to the United States because of export market diversification and the shrinking capacity of the United States as an export absorber. Since the 1990s, most Asian economies other than China and Vietnam have reduced their dependence on exports to the United States and Japan, while increasing their dependence on exports to China and other Asian markets.

This trend is typified by South Korea (Fig. 7). South Korea’s dependence on exports to the United States began to decline when South Korean companies started to establish production operations in North America in response to the rising value of the won and trade friction. Another factor was a production shift to Asia with the aim of reducing costs. South Korea began to trade with China on a significant scale following the normalization of relations in 1992. Trade subsequently expanded, reflecting the relocation of production operations by South Korean firms. In the current decade, China’s admission to WTO membership

Table 1 Remittances from Overseas Workers to the Philippines

<table>
<thead>
<tr>
<th>Country</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S.A.</td>
<td>6,425</td>
<td>6,526</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>949</td>
<td>1,118</td>
</tr>
<tr>
<td>Canada</td>
<td>117</td>
<td>591</td>
</tr>
<tr>
<td>Italy</td>
<td>430</td>
<td>575</td>
</tr>
<tr>
<td>U.K.</td>
<td>301</td>
<td>562</td>
</tr>
<tr>
<td>Japan</td>
<td>357</td>
<td>453</td>
</tr>
<tr>
<td>UAE</td>
<td>257</td>
<td>427</td>
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<tr>
<td>Hong Kong</td>
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<td>414</td>
</tr>
<tr>
<td>Singapore</td>
<td>240</td>
<td>285</td>
</tr>
<tr>
<td>Taiwan</td>
<td>87</td>
<td>169</td>
</tr>
</tbody>
</table>


Fig. 7 South Korea’s Export Dependence

Notes: Figures for 2007 cover the January-October period.
Source: Korea International Trade Association
in December 2001 and the expansion of domestic markets in China have provided the impetus for dramatic export growth, and in 2003 China became South Korea’s biggest export market.

However, a number of factors must be taken into account when considering dependence on trade with the United States. First, as illustrated by the example of South Korea, the shift to offshore production has meant that some goods that were previously exported directly to the United States are now included in China’s export statistics. China’s dependence on exports to the United States has remained basically static at 21% (Fig. 8). Vietnam has become more dependent on exports to the United States since the signing of a trade agreement with the United States in July 2000, and in 2006 the ratio was 21.2%.

Asia still seems to be heavily dependent on the United States in the area of services, such as financial services, transportation and software. While it is difficult to measure service export patterns statistically, we can use trends in India’s exports of IT services as a case study. One trigger for the growth of India’s IT service industry was the establishment of technical colleges by the government. This has resulted in the formation of a large pool of specialized human resources with excellent IT skills and the ability to speak English. Another factor was the construction of software parks\(^5\). However, the industry’s growth owes much to the expansion of outsourcing by American companies \(^6\). According to India’s National Association of Software and Service Companies (NASSCOM), the biggest export market for IT service in fiscal 2006 was the United States (67.2%), followed by Europe (25.1%).

Intermediate goods account for a large share of intraregional exports by Asian economies, while most final goods are exported outside of the region. Trade data that include intermediate goods therefore tend to exaggerate dependence on intraregional trade. Estimates cited in ADB \([2007a]\) indicate that G3 markets (the United States, the EU and Japan) account for 61.3% of demand for final goods exported from Asia, compared with a 21.2% share for markets within the region, and 17.5% for other markets. These figures suggest that the G3 group continues to exert a strong influence on the Asian economy. It is not possible to estimate export dependence on the United States for final goods, since the data are not broken down into individual G3 markets. However, there has been a gradual decline in America’s share of world GDP, while Asian markets, especially those of the population giants, China and India, are expanding rapidly. Based on these factors, we can assume that the influence of the United States is waning in real economic terms.

The emergence of the subprime mortgage crisis in the United States has triggered a debate on economic coupling or decoupling between Asia and the United States. This is not a new topic of debate, and it tends to attract discussion whenever an economic recession (negative quarterly growth in two successive quarters) is predicted in the United States. Interest is more intense this time, however, because the Japanese economy is just emerging from the period of stagnation that followed the collapse of the bubble, and because Japan’s economic performance will be significantly influenced by external demand, especially exports to Asia.

Since the 1980s, the United States has experienced recessions in 1982, 1991 and 2001. With the exception of 1991, the growth rates of Asian economies have fallen during each U.S. recession.
The minimal impact of the 1991 recession is explained by the fact that increased direct investment from Japan boosted the exports of the NIEs and ASEAN and lifted their growth rates in the second half of the 1980s and the early 1990s. Another factor was the acceleration of China’s reform and open-door policy in the early 1990s.

The last recession in the United States was in 2001. It marked the end of over 10 years of continuous economic expansion and caused the growth rate to fall from 3.7% in 2000 to 0.8% in 2001 (1.6% in 2002). After showing double-figure growth up until 2000, imports declined by 2.7% in 2001 and grew by 3.4% in 2002. This recession in the United States, combined with the impact of reduced world IT demand, caused the growth rates of Singapore and Taiwan to fall to minus 2.4% and minus 2.2% respectively in 2001.

In contrast, Thailand achieved growth of 4.2% and South Korea 3.8%. This wide divergence of growth rates resulted from differences in several factors, including export dependence (exports/GDP), mixes of export markets and export products, and government actions. For example, while Taiwan is heavily reliant on its IT sector, South Korea had diversified its export mix. Another factor that helped to minimize the decline in growth rates was government measures to stimulate the economy through the expansion of domestic demand. The extent to which Asian economies were affected by the economic recession in the United States thus depends both on the economic environment in Asia, and also on factors specific to individual economies.

What will be the outcome this time? The differences from the situation in 2001 include the fact that the China continues to achieve growth in excess of 10%, and the increased profile of non-Asian emerging economies. These changes have been cited as evidence for the economic decoupling of Asia and United States. Taiwanese export statistics can be used to illustrate how this shift is being manifested.

An analysis of rates of increase in total exports (customs-cleared, dollar-based) and exports to the United States between January 1999 and September 2007 (Fig. 10) points to the following conclusions. First, the two growth rates remained basically linked between late 2000 and early 2002. During this period, a decline in exports to the United States led directly to a similar decline in

![Fig. 9 Real GDP Growth Rates of the United States and Asia](image)

![Fig. 10 Taiwan’s Exports (Compared with the same month a year earlier)](image)
spicuous growth in exports to emerging economies and Gulf States has helped to ease the impact of slower exports to the United States.

Asian economies will inevitably be affected by the economic slowdown in the United States. However, the economic influence of the United States on Asia has clearly been reduced by the rising presence of emerging economies.

2. Recent Trends in Asia from a Trade Perspective

In this section we will look at recent changes in the world trade situation. We will also consider whether there has been any strengthening of a presence of emerging economies. This will be followed by an analysis of recent trends in Asian economies, using trade matrices.

(1) The Growing Presence of Emerging Economies

Global Exports the Driving Force for Emerging Economies

Total world exports (The figures cited below are mostly based on IMF, Direction of Trade Statistics), showed negative annual growth in 1998 and 2001 because of the impact of the Asian currency crisis and global economic deceleration. However, 2003 brought a return to positive double-figure growth (Fig. 12). Exports have since been supported by an expanding world economy, and a 13.5% annual increment in 2005 was followed by an even bigger yearly increase of 15.3% in 2006. Exports from the developed economies have remained on a steady growth trend, with U.S. exports increasing by 14.7% and those from the EU by 12.3%.

The statistics show particularly large increases for China, the oil-exporting countries, and others, including Russia and Brazil. Rising prices for primary products helped Russia, the world’s second biggest exporter of crude oil, to achieve 21.7% export growth. Brazil, which exports iron ore and crude oil, recorded 16.7% growth.

The rate of increase for Asia (excluding China) was moderately lower than the total increase at 14.2%. The main countries/regions contributing to export growth in 2006 were the EU (31.5%),
First, China’s exports continue to grow rapidly. The 2006 increase of 27.1% marked the fifth straight year of growth in excess of 20%. In 2006, China was the third biggest exporting nation after Germany (9.3%) and the United States (8.7%). At 19.6%, China’s dependence on exports to the EU is approaching the same level as its dependence on the United States (21.0%). In terms of total trade, including imports, the EU is China’s biggest trading partner.

China’s emergence as a major exporting country over such a short period of time is the result of massive inflows of foreign direct investment. This is apparent from the fact that foreign-owned companies account for 58.2% of total exports (according to Chinese customs statistics for 2006). The sources of China’s export competitiveness were low production costs, and the fact that the yuan was pegged against the dollar until comparatively recently. However, the situation has changed in recent years. First, wages are rising, especially in coastal regions. Second, the value of the yuan is rising. Third, as discussed later in this article, changes in the investment environment, including increased selectivity on the part of foreign investors, are reflected in a tendency toward slower growth in direct investment in China. These fac-

Growth for China, Vietnam and India

Based on the preceding analysis, we can identify a number of characteristics in trends in Asia. First, China’s exports continue to grow rapidly. The 2006 increase of 27.1% marked the fifth straight year of growth in excess of 20%. In 2006, China was the third biggest exporting nation after Germany (9.3%) and the United States (8.7%). At 19.6%, China’s dependence on exports to the EU is approaching the same level as its dependence on the United States (21.0%). In terms of total trade, including imports, the EU is China’s biggest trading partner.

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tors could easily cause a gradual slowing of export growth.

In addition to China’s rising export profile, its role as a market is also expanding, as evidenced by the growth of its share of world imports from 1.8% in 1991 to 6.4% in 2006 (Fig. 14). The biggest sources of imports into China are Japan (14.6%), the EU (11.5%), South Korea (11.3%) and the United States (7.5%).

Second, though still small in absolute terms, India’s exports are expanding. India has recorded export growth in excess of 20% in four consecutive years since 2003 (25.4% in 2006).

As outlined earlier, India has rapidly become integrated into the global economy since the implementation of economic reforms in 1991. The main types of goods exported by India are petroleum products, gemstones and jewelry, textile products and machinery. However, the development of export industries in the manufacturing sector has been generally slow because of the emphasis on import substitution in India’s industrialization strategy for many years, and also because of inadequate logistics infrastructure.

This situation is about to change. First, motor vehicle manufacturers in India (including those intending to establish operations there) plan to increase their exports. Second, India is improving its logistics infrastructure. Third, India plans to foster exporting of labor-intensive products. These factors point to a sustained rise in the export potential of manufacturing industries in the years ahead.

India’s biggest export industry is IT services. Service exports do not appear in customs clearance statistics, but according to NASSCOM the total for 2006 was $23.6 billion. Further rapid growth is predicted (Fig. 15). Service exports are now worth more than exports of petroleum products, and service industries directly employ 1.29 million people. According to the Reserve Bank of India, India recorded a surplus of $9.15 billion in its service trade balance in the April-June quarter of 2007, compared with a $21.58 billion deficit in its balance of payments for goods. There was a $7.88 billion surplus in India’s trade in software services.

An important difference between India’s export market mix and those of other Asian economies is the fact that oil-exporting countries, including Middle Eastern countries, account for a large share of its exports (Fig. 16). India has started to build close relationships with Asian economies and is beginning to function as a bridge between Asia and the Middle Eastern Gulf States.

Third, intraregional trade in Asia is expanding. Reasons for this trend include direct investment in
Asian economies and increased trade with China and other Asian economies by Japan, South Korea and Taiwan since the second half of the 1980s, and progress toward economic integration within the region. This aspect is examined in the following section.

(2) Trade Matrix Analysis of Trends in Asia

We will next analyze intraregional trade trends in Asia by compiling a trade matrix based on the IMF’s Direction of Trade Statistics Database (Table 2). To identify recent trends, we will compare figures for 2001 and 2006. ASEAN is defined as six countries: Thailand, Malaysia, Indonesia, the Philippines, Singapore and Vietnam, and India is included in Asia.

Several trends are apparent in the table. First, intraregional exports within East Asia (excluding India) have expanded from $712.6 billion in 2001 to $1,591.9 billion in 2006. Second, China has increased both its intraregional and extraregional exports. Third, there has been a conspicuous increase in exports from Asian economies to China. Fourth, trade between Asian economies and India and Vietnam has started to expand.

The first point to note here is that trade between Asian economies and China is leading to growth in intraregional trade. Between 2001 and 2006, exports from China to East Asian economies increased by $256.3 billion, and exports from East Asian economies to China by $281.5 billion. These two figures alone make up 61.2% of the total increase in intraregional exports.

Two factors are involved in this growth in exports to China. The first is the export-inducing effect resulting from the expansion of direct investment and local production. Companies in industries ranging from footwear and apparel to electrical and electronic equipment and IT equipment have progressively relocated their production operations from Japan, South Korea and Taiwan to China. In these three economies, this has induced increased exports of intermediate goods, including raw materials and parts, and capital goods. In the ASEAN economies, this trend has been reflected in increased exports of items that cannot adequately be supplied within China, such as natural rubber, petrochemical products, semiconductors and electronic parts. The other factor leading to growth in exports to China is the expansion of domestic markets due to rising income levels. China’s expanding markets have attracted increased local production and exports. China is the second biggest motor vehicle market after the United States, and the world’s biggest market for mobile phones.

The second key point is the positive effect of an expanding framework of free trade agreements (FTAs) on the expansion of intraregional trade. Moves toward regional economic integration are occurring on multiple levels in Asia, including bilateral FTAs, FTAs between ASEAN and non-ASEAN countries, and economic integration within ASEAN.

In 2003, the six original ASEAN members (Thailand, Malaysia, the Philippines, Indonesia, Singapore and Brunei) reduced tariffs on the majority of items covered by the Common Effective Preferential Tariff (CEPT) system to 5% or lower. The six original members will abolish tariffs on all but a few items by 2010, followed by Vietnam, Laos, Myanmar and Cambodia in 2015.

While foreign-owned companies develop production and distribution networks throughout Asia, governments are starting to establish institu-
tional frameworks for regional economic integration. These factors are driving the expansion of intraregional trade in intermediate goods. This trend is expected to accelerate with the development of international logistics networks, as described below.

First, there is the logistics network linking China and Vietnam. In December 2005 an expressway was opened linking Nanning (capital of the Guangxi Zhuang Autonomous Region) with the Friendship Pass on the border with Vietnam. This was followed in March 2007 by the establishment of a container shipping route between Guangdong and Haiphong.

Second, logistics networks are evolving within ASEAN. In December 2006, the Second Mekong International Bridge was completed (using a Japanese government loan). The bridge links Savannakhet in Laos with Mukdahan in Thailand and forms part of the East-West Economic Corridor (Da Nang–Savannakhet-Mukdahan-Mawlamyine). Previously goods had to be carried by sea from Bangkok to Hanoi, a voyage of around 10 days. The new bridge has drastically reduced transportation time (12).

Third, the rising profile of Asian emerging economies, such as India and Vietnam, has started to contribute to the expansion of intraregional trade.

In 2006, Vietnam’s exports increased by 22.8% over the previous year’s level. Its dependence on export to the United States is high at 21.2%,

<table>
<thead>
<tr>
<th>Table 2 Trade Matrix (Upper: 2006, Lower: 2001)</th>
</tr>
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<tbody>
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<td>(Billions of dollars)</td>
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<tr>
<td>Thailand Malaysia Indonesia Philippines Singapore Vietnam South Korea Taiwan Hong Kong China Japan East Asia total India U.S.A. EU Total</td>
</tr>
<tr>
<td>Thailand 8.7 3.3 2.6 8.4 3.1 2.7 3.0 7.2 11.8 16.5 65.3 1.8 19.6 18.1 130.6</td>
</tr>
<tr>
<td>Malaysia 8.5 4.1 2.2 24.7 1.8 5.8 5.4 7.9 11.6 14.2 86.2 5.1 30.2 20.5 160.7</td>
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<td>Indonesia 3.4 1.6 1.3 14.9 0.5 3.0 3.8 3.8 4.1 11.8 48.2 0.3 17.8 12.5 88.2</td>
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<td>East Asia total 22.9 13.2 7.4 9.0 19.5 4.1 50.3 41.7 36.4 92.8 297.3 4.5 147.2 94.1 646.8</td>
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<td>U.S.A. 1.5 1.3 1.7 0.4 4.4 0.6 2.9 1.1 4.3 9.5 3.7 27.1 20.9 25.9 122.8</td>
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<td>EU 0.6 0.7 0.4 0.2 1.0 0.2 0.2 0.6 2.1 1.5 2.0 10.1 9.4 11.2 45.6</td>
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<td>Total 8.2 10.5 3.1 7.6 24.7 1.1 32.5 20.4 17.8 55.2 59.6 239.6 10.1 215.0 1,037.1</td>
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Notes 1: Shaded areas indicate 3-fold or higher growth. 2: Because IMF statistics do not include Taiwan, each country’s exports to Taiwan have been estimated by multiplying Taiwan’s imports by 0.9. 3: The EU consists of 25 countries. Source: IMF, Direction of Trade Statistics Database, Republic of China, Monthly Statistics of Trade
part because of the signing of a trade agreement with the United States in July 2000. However, exports within Asia are also expanding. There has also been a marked increase in exports to Vietnam from Asian economies, especially Thailand and China. Rapid growth in trade between Vietnam and other economies within the region appears inevitable, given the development of international logistics networks and the expansion of investment in Vietnam over the past few years.

India’s exports within Asia are expanding dramatically. In 2006, its exports to South Korea, China and Thailand increased by 81.2%, 47.7% and 45.9% respectively. The rapid growth in trade with China is especially significant, and China now accounts for 7.8% of total Indian exports, making it India’s fourth biggest market after the EU (21.1%), the United States (17.0%) and the UAE (8.3%). The main export items are iron ore and steel.

China supplies 8.7% of India’s imports and has overtaken the United States (6.0%) to become the second biggest source after the EU (18.2%). According to Chinese statistics, exports to India increased by 64.7% and imports from India by 42.4% in 2007. A joint communiqué issued after a summit meeting between China and India in November 2006 called for a doubling of trade between the two countries by 2010.

Fourth, there is considerable variation in levels of dependence on intraregional exports. Most economies in Asia (including India) increased their dependence on intraregional trade between 2001 and 2006 (Fig. 17). Those recording especially large increases included Taiwan (12.6 percentage points), the Philippines (11.5 percentage points) and Japan (7.3 percentage points). In contrast, China’s dependence on intraregional trade fell by 7.3 percentage points, reflecting a dramatic increase in its exports to the United States and EU. Vietnam’s ratio also fell, by 12.6 percentage points, because of rapid growth in exports to the United States, while the figure for India remained unchanged at 22.1%.

Intraregional trade is clearly expanding. We will next examine the real situation behind this trend, using data from ITI Zaibetsu Kokusai Boeki Ma-
growth in exports of parts from ASEAN to China has been characteristic of recent trends in the trade in parts (Fig. 19).

In the case of motor vehicles, dependence on intraregional exports of finished (assembled) products is 7.2%, compared with 33.1% for parts. There are several reasons for the low figure for assembled vehicles. First, in most Asian economies, vehicles are basically manufactured locally to meet local demand. Second, Japan and South Korea have high export ratios but export most of their products to the United States and the EU. Third, Thailand has become a world production center for one-ton pick-up trucks, most of which are exported to Europe and the Middle East. One reason for the higher dependence on intraregional trade in parts is the development of reciprocal supply systems by Japanese-affiliated companies, especially in ASEAN.

Parts clearly make up a large share of intraregional trade. The statistics highlight the existence of a lively intraregional trade in intermediate goods.

3. Recent Trends in Asia from a Direct Investment Perspective

These changes in trading patterns are closely linked to trends in direct investment. In this section we will look at recent developments in direct investment.

(1) Shift away from Concentrated Investment in China

In terms of world totals, direct investment has been expanding in recent years. According to the World Investment Report 2007 published by the United Nations Conference on Trade and Development (UNCTAD), world foreign direct investment \(^{(15)}\) reached a peak of $1,411.1 billion in 2000 and then began to decline \(^{(16)}\). A new growth trend emerged in 2003, and investment is again approaching the 2000 peak. The 2006 total of $1,301.6 billion was 38.1% higher than the previous year’s level (Fig. 20). Investment in developed economies increased by 45.3% year-on-year. This reflects growth in cross-border M&A and leveraged buy-outs (LBOs), driven by global economic expansion, increasing business earnings, low interest rates and other factors. Investment in developing economies rose by 20.6%, but there was a 97.5% increase in investment in the transitional
economies of South-East Europe and the CIS.

A sector breakdown shows an upward trend in the percentage of investment flowing into service industries, reflecting their growing contribution to economic activity. Service industries accounted for 62% of the cumulative total of investment in developed economies up to 2005. The corresponding figure for developing economies was 58%. In developed economies, the biggest recipient is the financial sector, followed by business services, and hotels and restaurants. In developing economies, business services receive the largest share, followed by the financial sector and commerce.

Statistics for individual countries/regions show that the biggest recipient of foreign direct investment is the EU (25 countries), which recorded a 9.2% increase. Investment in the United States surged by 73.6% due to increased M&A activity by European companies. At 19%, the increase in investment in Asia (excluding West Asia, the total for East Asia, Southeast Asia and South Asia) was smaller than the increase in total investment.

Foreign direct investment in Asia has been affected by several trends in recent years. First, in the early years of this decade investment tended to be concentrated in China, but this pattern is now waning. Though China remains biggest recipient of investment in Asia, the 2006 total of $69.5 billion was smaller than the previous year’s figure ($72.4 billion) for the first time in seven years (Fig. 21). Investment in the non-manufacturing sector increased, but this was more than offset by a decline in investment in the manufacturing sector.

Apart from the investment cycle, reasons for this decline in investment in the manufacturing sector also include a worsening investment environment, the heightened risk of concentrated investment in China, and the rising profile of emerging economies. In addition to rising wages and labor shortages in coastal regions, China’s massive trade surplus is pushing up the value of the yuan. A liquidity excess triggered by central bank intervention has magnified domestic imbalances, and there is a strong possibility that the exchange rate against the U.S. dollar will rise still further.

Furthermore, the Chinese government wants to develop a more advanced industrial structure and reduce environmental problems through a more selective approach to investment (17). Future investment trends are likely to be affected by a shift in priorities from quantity to quality. Corporation tax concessions were abolished in January 2008, and foreign-owned companies are now subject to the
same 25% tax rate as domestic companies.

Changes in China’s investment environment are causing investment in labor-intensive manufacturing industries to shift to other targets. The shift of production activities from China to other countries is also intensifying. Taiwanese companies are now expanding their production operations in Vietnam, and production and distribution networks are now being established between Vietnam and industry clusters in southern China. This trend has gained additional momentum from improvements in logistics infrastructure, including the completion of an expressway linking China and Vietnam (Nanning Friendship Pass) and the establishment of a container shipping route between Guangdong and Haiphong.

This shift away from concentrated investment in China is confirmed by a decline in China’s share of total world foreign direct investment, which has fallen from 9.5% in 2003 to 5.3% in 2006. China’s share of total investment in developing economies has also declined, from 31.7% in 2002 to 18.3% in 2006 (Fig. 22). This is linked to growth in investment in ASEAN and other emerging economies, such as India, Brazil and Russia, as described below.

A second trend affecting foreign direct investment in Asia is the growth of investment in ASEAN. After the currency crisis, investment in the ASEAN10 declined until 2003, when it began to expand again. In 2006 investment increased by 25.3% (Fig. 21). As noted earlier in this article, this upward trend in investment is linked to improving fundamentals and progress toward regional economic integration.

Investment statistics for individual economies show conspicuous growth in investment in Singapore. Singapore’s total of $24.2 billion was 61.3% higher, while investment in Malaysia increased by 52.8% to $6.1 billion. There was a 14.5% increase in investment in Vietnam, which has become a key focus of strategies designed to spread the risk of investment in China. Vietnam joined the WTO in January 2007, and the resulting improvement in its investment environment is expected to bring increased investment not only in the manufacturing sector, as in the past, but also in service industries. Investment in Indonesia was negative (net outflows) in four consecutive years from 1998. However, investment has started to recover, with total of $1.9 billion in 2004, $8.3 billion in 2005 and $5.6 billion in 2006.

Cambodia and Laos, which are less industrialized than other ASEAN members, are also attracting increased investment. Investment in Cambodia has risen from $130 million in 2004 to $380 million in 2005 and $480 million in 2006. In Laos, expanding investment in the electric power sector is reflected in figures of $28 million in 2005 and $187 million in 2006.

A third trend with significant implications for foreign direct investment in Asia is the emergence of India as a major investment target. In 2006 investment in India increased by 152.9% over the previous year’s total to $17.0 billion, which is equivalent to about one-quarter of the total for China, and one-third of the ASEAN total. The service sector accounted for 35.5% of this figure. Apart from services, the biggest recipient of investment was the electronics industry (including software), followed by telecommunications, transportation equipment, including motor vehicles and motorcycles, and chemicals. Except for software,
these are basically domestic demand industries. With its economy firmly on a growth path, India has also seen rapid expansion in its domestic consumer markets. Factors contributing to this expansion include the existence of a growing middle class with purchasing power, remittances from overseas workers, and a distribution revolution, as evidenced by the construction of shopping malls and supermarkets. According to the National Council of Applied Economic Research (NCAER), India’s population of consumers with annual incomes of $1,300-6,000 is expected to reach 450 million by 2010.

In 2006, domestic sales of motor vehicles increased by 23.7% to 1,847,000, making India the second biggest market in Asia (excluding Japan) after China. Several manufacturers, including Hyundai, Toyota, Honda and GM, have moved into India or expanded their facilities there. More recently, Nissan established a joint venture with Renault and Mahindra and Mahindra in February 2007. Arcelor Mittal and POSCO plan to build integrated steel mills to meet the expanding demand for sheet steel.

These three trends all provide evidence of a shift away from concentrated investment in China, which characterized direct investment in the early years of this decade, toward greater diversification of investment targets.

(2) Trends in Investment by Japan, South Korea and Taiwan

This diversification of investment targets has also been manifested in the investment behavior of Japan, South Korea and Taiwan, which are all major sources of investment in Asia. (Overseas direct investment by Taiwan was examined in Mukoyama-Sano [2007], so we will focus on more recent trends here.)

Overseas direct investment from Japan has increased from ¥5,045.9 billion in 2005 to ¥5,845.7 billion in 2006, and ¥6,758.7 billion in 2007 (January-October). However, its share of total investment in Asia has fallen, from 35.6% in 2005 to 34.2% in 2006 and 28.0% in 2007. The most significant trends in Japanese investment are the fact that investment in the ASEAN6 is estimated to exceed investment in China in 2007, as in 2006, and the growth of investment in India (Fig. 23).

This pattern is expected to intensify. In fiscal 2007, Japan Bank for International Cooperation conducted a survey of overseas business development by Japanese companies. The results show that while China is still the most popular choice as a likely investment target in the medium-term future (over the next three years or so), its share of the vote is falling, in contrast with a steady rise in the percentages of votes going to India and Vietnam (Table 3). India has overtaken China as the most likely target for investment in the long-term future over a time-frame of around 10 years (Table 4). These results are indicative of a major shift in the positioning of China by Japanese companies over the past few years.

A similar trend is occurring in South Korea. Research by the Export-Import Bank of Korea shows that direct investment in China (implementation basis) is still expanding in absolute terms. However, China’s share of total direct investment peaked out at 41.1% in 2003 and has since fallen to 30.9% in 2006 and 26.9% in the first half of 2007 (Fig. 24).

Fig. 23 Distribution of Japanese Overseas Direct Investment among Key Asian Economies (International BOP Basis)

Notes 1: The ASEAN6 are Thailand, Malaysia, Singapore, Indonesia, the Philippines and Vietnam.
2: Figures for 2007 cover the January-October period.
Source: Ministry of Finance, Kokusai Shushi Tokei [Balance of Payments Statistics]
Recent investment activity has been characterized by increased investment in the BRICs other than China, including India, Russia and Brazil. There has also been an increase in investment in the EU, especially the former socialist countries, such as Slovakia, Kazakhstan, Poland and the Czech Republic. In Asia (excluding India), there has been growth in investment in less-developed ASEAN members, especially Vietnam and Cambodia.

Major investments projects in India include the construction of a second motor vehicle plant by Hyundai (scheduled for completion in the second half of 2007), and plans for the construction of a third steelworks by POSCO, in addition to its existing facilities at Pohang and Gwangyang. POSCO aims to build a steelworks with capacity for 4 million tons per year by 2010. By 2020 it aims to develop integrated steel production facilities with capacity for 12 million tons per year.

As in 2006, Investment from South Korea is estimated to have been the biggest in 2007. Apart from changes in China’s investment environment, this growth in investment in Vietnam also reflects an economic growth rate that has remained around 8% for several years, market expansion, and the prospect of improved investment conditions following Vietnam’s admission to WTO membership. Other factors include the start of work on the development of international logistics infrastructure linking Vietnam with parts manufacturing centers in southern China, Thailand and elsewhere. This

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**Table 3 Medium-Term Targets for Business Investment (Multiple Responses)**

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<td>3rd Vietnam</td>
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<td>10th Taiwan</td>
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Source: Japan Bank for International Cooperation, Kaigai Chokusetsu Toshi Anketo Chosa Hokoku [Report on Overseas Direct Investment Survey]

**Table 4 Long-Term Targets for Business Investment (Multiple Responses)**

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<td>6th Thailand</td>
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<td>7th U.S.A.</td>
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<td>8th Indonesia</td>
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Source: Same as for Table 3
will enhance Vietnam’s attractiveness as a site for assembly facilities. Samsung Electronics is building a second plant to manufacture monitors, printers and other computer equipment and also plans to build a new mobile phone plant. POSCO aims to capture local demand for steel sheet by progressively building cold-rolling, hot-rolling and galvanizing facilities.

Taiwan has concentrated its investment in China more than Japan and South Korea. One reason for this is the fact that many Taiwanese companies have moved into southern China and established electrical and electronic industry clusters. This has created a mechanism in which clusters generate more clusters. Another factor is ease of communication, which allows Taiwanese firms to recruit local employees.

However, there are also signs of a shift in Taiwan’s investment behavior. China’s share of Taiwan’s total overseas investment has fallen from 71.1% in 2005 to 63.9% in 2006, and 60.6% in 2007. Hon Hai Precision Industry (Foxconn), the biggest Taiwanese IT company, has recently stepped up its investment in Vietnam. In 2007 it built a second factory in Bac Ninh Province, which located between Hanoi and the Chinese border. Compal Electronics has announced plans for a plant in Binh Phuoc Province in northern Vietnam.

4. Future Outlook and Issues

(1) Future Directions and New Possibilities

The rising profile of emerging economies has started to alter trade and investment flows in Asia. Since the 1990s, and especially since the currency crisis, the Asian economy has been strongly influenced by the Chinese economy. More recently, however, there has been an increase in direct investment from Asian economies, especially into India and Vietnam. Trade with these countries is also expanding. Another important change is the development of Islamic finance systems by Malaysia, which is actively seeking to bring Middle Eastern funds into the region. Links with emerging economies are expected to expand in the future.

The Asian economy is expected to go through a period of restructuring, driven not only by the increasing importance of emerging economies, but also by a policy shift in China. China aims to achieve a transition to stable growth while working to correct the imbalances that expanded as a consequence of high economic growth. In 2008, it will step up the pace of its currency reforms, including the reform of the yuan exchange rate system, with the aim of eliminating its liquidity surplus and correcting external imbalances. There is a strong possibility that the shift of labor-intensive (manufacturing) industries from China into less industrialized countries will accelerate as a result. The results of these changes could be highly significant for the region, as described below.

First, having transformed the NIEs, ASEAN and China, the industrialization process is now spreading to India and Vietnam and other neighboring countries. This will reduce poverty in the region. From a global perspective, Asia still has a vast impoverished population. Poverty ratios are especially high in south Asian countries, such as India, Bangladesh, and in the less developed ASEAN members (Table 5). Industrialization and
export growth, especially in labor-intensive sectors, has the potential to reduce poverty through the following process. ① Export expansion in labor-intensive industries triggers a population shift from rural to urban areas, reducing the rural labor surplus. ② The expansion of export production stimulates growth in industries manufacturing intermediate goods. ③ Agricultural production increases through the use of chemical fertilizers and farm machinery. ④ Rural incomes are lifted by a combination of factors, including the production of cash crops for sale in urban areas, and opportunities for migrant work in the cities.

Cambodia’s sewing industry has expanded rapidly over the past few years. This has resulted from the relocation of production facilities for designer goods by Hong Kong, Taiwanese, Chinese and South Korean firms for the U.S. market. According to Yamagata [2006], export-oriented apparel industries are helping to reduce poverty in Bangladesh and Cambodia by providing employment for impoverished people. In Laos, the completion of the Second Mekong International Bridge has triggered the construction of trading centers and factories in the surrounding areas, and industrial facilities, including manufacturing plants, warehouses and cargo terminals, are now being built near crossroads of major highways. In the past industrialization in Laos has been hindered by the country’s landlocked situation. However, the development of international logistics networks is expected to lead to a shift of production activity from Thailand.

Poverty in inland regions of China is also likely to be reduced through the relocation of production activity from coastal regions. The government is implementing regional development schemes, including infrastructure projects. If these initiatives result in industrialization and urbanization, the resulting growth of service industries will create employment opportunities.

A second potential outcome is the expansion of markets within Asia. As described earlier in this article, Asia is still heavily dependent on the United States and the EU as markets for final goods. If markets in China (especially rural China) and other Asian economies expand, goods produced in Asia will increasingly be consumed in Asia, further strengthening the region’s economic independence. India in particular is expected to follow this path.

India’s consumer markets are expanding rapidly in response to factors that include sustained economic growth, the expansion of the middle class, and the distribution revolution. The Indian motor vehicle market is now the biggest in Asia after the Chinese and Japanese markets, and several foreign-affiliated manufacturers have established facilities. McKinsey & Company [2007] makes the following predictions. First, Indian consumer markets will expand from 17 trillion rupees (about $385.5 billion, twelfth biggest in the world) in 2005 to 40 trillion rupees (fifth biggest in the world) in 2025. Second, the percentage of

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<th>Poverty Ratio (Population below Poverty Line)</th>
<th>Poverty Ratio (Income below $1 per Day, PPP Basis)</th>
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<tr>
<td></td>
<td>Total</td>
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<td>Thailand</td>
<td>9.8</td>
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<td>Malaysia</td>
<td>7.5</td>
<td>3.4</td>
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Source: Asian Development Bank, Key Indicators 2007
middle-class households (households with annual incomes of 200,000–1,000,000 rupees) will reach 41% (approximately 583 million people) by 2025.

Another factor that is likely to make India more attractive from a long-term business development perspective is the fact that demographic aging is occurring more gradually than in China.

(2) Issues

The emerging economies will become increasingly important in the region, and their growth is expected to bring benefits to developed economies. However, we also need to be aware of the risks. By definition, emerging economies have fragile economic structures. In addition to continuing problems relating to inflation and currency stability, there are also political stability risks. Political corruption and bureaucratic inefficiency are issues in Russia, while in Brazil the taxation system causes problems for businesses.

The biggest problem for businesses in India is the inadequacy of infrastructure (Fig. 25). The power transmission loss ratio is high, even compared with China, Russia and Brazil, and the road pavement ratio is far lower than in China (Fig. 26)(18).

The government is aware of these problems and will take steps to alleviate power shortages and unreliability. It has also given priority to the development of logistics infrastructure, and there are plans for the expansion of port capacity (especially container terminals) and the improvement of road networks linking ports with major production centers, such as Mumbai and Delhi.

Another priority is the alleviation of poverty. Since World War II, India has maintained an official rationing system under which the government sells rice, wheat and other products below market prices. Other poverty reduction measures have included general agricultural development programs, and government employment schemes. In the 1990s, accelerating growth reduced the poverty ratio to below 30% of the population, compared with more than 40% in the mid-1980s. However, millions of Indians still endure life below the poverty line (Table 5).

China achieved rapid export growth as a result of massive inflows of foreign investment, especially into labor-intensive industries.
service industries have enjoyed rapid growth as export industries. With the exception of apparel manufacturing and a limited range of machinery industries, however, its manufacturing industries are not well developed. The IT service industries create only 300,000 jobs annually. Moreover, these industries depend on elite graduates of engineering universities, most of whom come from households that have already achieved a certain level of economic affluence. Apart from indirect benefits resulting from economic growth, this sector has made only a small contribution to increased employment for impoverished and low-income people. Poverty reduction will not be possible without the absorption of surplus labor from rural areas, and this will require export expansion in labor-intensive industries. This is one of the reasons why the development of logistics infrastructure will be an urgent priority.

The government needs to ensure that the benefits of growth are widely distributed, by developing infrastructure and facilitating the growth of export industries. It also needs to take appropriate steps to deal with the risk of expanding disparity during the industrialization process.

As described in this article, the Asian economy is entering a period of dramatic change. Japan’s economic interdependence with Asia is expected to intensify in the years ahead, and it will be more important than ever for Japan to provide support for the development of emerging economies, especially in the areas of infrastructure, human resource development, poverty reduction, environmental measures and energy conservation, and for sustainable development throughout Asia.
End Notes

1. In this article, the region is referred to as “Asia” if India is included, and as “East Asia” when India is excluded.

2. Thailand’s conspicuous recovery can be attributed to large-scale infrastructure projects in Bangkok (including railroad projects, such as the construction of an elevated railroad and subway extension, and the construction of a new airport) during the Thaksin administration (2001-06). While increased fixed capital formation helped to drive growth, it also caused increased inflation and a worsening of the trade balance. From mid-2005, the government’s policy priorities shifted to the improvement of the trade balance and the curbing of inflation.


4. This aspect is examined in Mukoyama, H. [2006]

5. The establishment of the Indian Institutes of Technology (IITs) began with Jawaharlal Nehru’s concept of economic development based on education. The IITs were the subject of a fascinating program produced by an NHK special reporting team in 2007.

6. See UNCTAD [2004] and Sekishita et al. [2006] for a discussion of service offshoring. The former work, which was the first to focus on this question, identifies four categories: ① call center/contact center services, ② shared (back office) services, ③ IT services, and ④ regional HQs.

7. Related measures in South Korea included the stimulation of private consumption expenditure and the facilitation of credit card use. However, these measures led to an increase in credit defaults and an unprecedented slump in consumer spending.

8. A unit root analysis based on ADF tests indicated the existence of a unit root at a 10% significance level in each case (and showing the existence of a trend), thereby negating the null hypothesis.

9. According to Chinese statistics, exports to the EU increased by 29.2% in 2007 and exceeded the total for exports to the United States.


11. The six original members will abolish tariffs in nine categories, including motor vehicles, electronics and textiles, in January 2007, followed by other members in January 2012. ASEAN also plans to liberalize services, facilitate flows of people (e.g., the abolition of visa requirements for tourism, reciprocal recognition of technical qualifications), introduce common certification systems (integration of product standards and certification, safety standards, etc.), and conduct studies concerning a common currency, with a view to the establishment of an economic community by 2015.

12. There are several issues at present. First, while demand for transport from Thailand to Vietnam is high, demand in the other direction is low. Second, under existing systems, goods traveling from Thailand via Laos to Vietnam (and in the opposite direction) must be loaded onto different vehicles in Laos. Some companies that need to transport precision parts have rejected the route for this reason.

13. The word “intraregional” refers here to 16 economies: Japan, the NIEs, the ASEAN10 and China.


15. Figures are on a net basis, including new share acquisitions, reinvestment and parent-subsidiary loans.

17. Current foreign investment policy sets three criteria. First, will the investment lead to the introduction of advanced technology and management methods? Second, will it contribute to environmental protection, resource conservation, and energy policy? Third, will it contribute to the advancement of domestic industry and the improvement of technology levels? Changes in China’s foreign investment policy are discussed in Mukoyama-Sano [2007].

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