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Topics Stable economic growth forecast for Asian economies in 2008

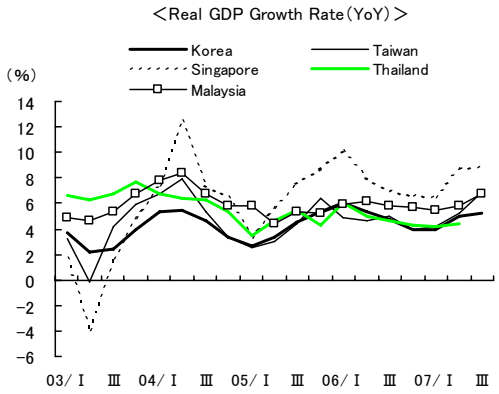
In 2008, with the deceleration of the US economy and the continuing rise of the price of crude oil, the economies of Asia overall are looking at slightly lower economic growth than in 2007. China and India will likely see growth of 10.4% and 8.3%, respectively.

1. Asia's economies in 2007

In 2007, the NIEs and ASEAN economies rallied and managed to sustain comparatively high economic growth. China continued to post growth of over 10% and India over 9%, leading the economies of the region..

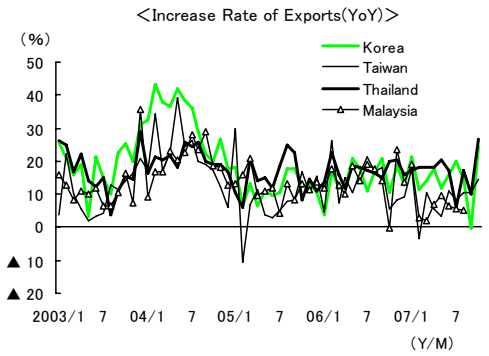
■ NIEs economies deliver solid performance

The Asian economies (excluding China and India) are performing quite stably overall, due to growing exports and recovering domestic demand, against a backdrop of an expanding global economy and accelerated economic growth particularly in the newly emerging markets and oil producing countries.



Source: National Statistics

Korea's real GDP growth rate for April to June was 1.8% up on the previous period (5.0% up compared to the same period in the previous year), and up 1.3%, similarly for July to September (5.2% up similarly), translating into a 4.7% growth for January to September, compared to the same period in the previous year. The forecast for the whole year is 4.7%. Exports and fixed capital formation continue to perform solidly, and the contribution of private consumption to economic growth is growing. Private consumption did cool as a result of consumer credit restrictions set in place in the wake of increasing credit delinquency, and posted year on year negative growth for two consecutive years in 2003 and 2004. Subsequently, there was a modest recovery, and in 2007 (January to September) momentum picked up and growth was 4.3%, compared to the same period in the previous year.



Source: National Statistics

In Taiwan, the prices of IT related devices such as semiconductors and liquid crystal panels, plummeted from the autumn of 2006, causing the economy to decelerate gently and real GDP growth (compared to the same period in the previous year) for October to December of that year was 4.0%, but rose to 5.2%, similarly, for April to June, 2007, and 6.9% in July to September. Depressed by the failure of real wage growth and credit card delinquency issues, private consumption growth slowed to just 0.8% for the period July to September, 2006, but recovered to 3.5% growth in July to September, 2007, encouraged by improvements in the employment and income situations. Recent trends show that exports, supported by a recovery in IT related demand, have posted high levels of growth, with 10.6% growth in September, compared to the same month in the previous year, and 14.4% in October, similarly. Export orders received have managed to maintain a comparatively high level of growth so, for the time being, there is a strong possibility that exports will be the drivers of economic growth (with 5.4% growth forecast for the whole year). Meanwhile, there is a slight sense of uncertainty with regard to the economic future, including growing concern that the economy of the US, Taiwan's main export destination for IT related devices, could lose momentum, and worries that inflationary pressure could increase.

Singapore's real GDP growth rate for July to September (compared to the same period in the previous year) was 8.9%, surpassing the 8.7% of the previous period (however, the year on year growth was down

to 4.3% from 14.5% in the previous period). In terms of specific industries, the service industry posted growth of 7.1%, manufacturing 10.5% and construction 17.7%. Within manufacturing, the bio-medical industry's contribution to growth was significant and industry development is pushing ahead.

■ Accelerated growth among ASEAN4

The real GDP growth rates for the ASEAN 4 (Association of South East Asian Nations) in 2006 were all in the 5% range, with 5.9% for Malaysia, 5.5% for Indonesia, 5.4% for the Philippines and 5.0% for Thailand.

Indonesia's growth rate for July to September (compared to the same period in the previous year) was 6.5%, exceeding April to June's 6.3% (outlook for the whole year 6.2%). Exports have performed strongly at 7.8%, and total fixed capital formation was up 8.8% and private consumption up 5.3%, making domestic demand the growth driver. One factor behind the expansion in domestic demand was that consumer goods prices began to fall from the latter half of 2006, which in turn caused interest rates to come down. Automobile sales, which posted negative year on year growth in 2006, grew 30.3% in 2007 (January to June), compared to the same period in the previous year. Also, following the government's efforts in infrastructure provision, construction investment is trending upwards.

In Malaysia also, domestic demand has been the growth driver, with the economy posting 5.5% growth in January to March and 5.7% in April to June. Private consumption grew 8.6% in January to March and 11.3% in April to June and fixed capital formation grew 9.9% in January to March and 6.6% in April to June, due to the growth in investments and foreign direct investment, in line with the Ninth Five Year Plan (2006 to 2010). The expectation is that domestic demand will sustain its strong performance through the year end, and the forecast for the whole year is 6.0%.

The Philippines posted high levels of growth, with 7.1% in January to March and 7.5% in April to June. A special feature of the period April to June was the greatly expanded election related expenditure by the government, and with 6.0% growth in individual consumption and 8.2% growth in fixed capital formation, domestic demand has also contributed significantly to growth. Curbs on inflation and money remitted home by workers abroad contributed to consumption growth. Also, gross fixed capital formation has grown, encouraged by the improvements made to the fiscal deficit.

In addition, there had been fears that Thailand's economy would lose its momentum as a result of the coup d'état (September, 2006), but economic growth has continued in the 4% range for four consecutive quarters since July to September, 2006. Despite sluggish domestic demand, exports have performed solidly. In recent times, in addition to solid export growth, domestic demand has begun to show signs of recovery, with private consumption indices and investment indices on the rise, and 4.2% growth is forecast for the whole year.

Thus, while the ASEAN 4, with the exception of Thailand, have continued to post comparatively high levels of growth, in addition to cyclical factors, other factors may be mentioned, for example (1) improved fundamentals, such as improved current account balances and contracted fiscal deficits, as a result of economic reforms implemented in the wake of the currency crisis, (2) increased foreign direct investment, (3) in addition to China, new export opportunities due to the recent emergence of India and Vietnam; and (4) positive effects (see below) brought about by accelerated growth in the crude oil exporting countries.

■ Continued high growth for China and the emergence of India

While China has continued to post high levels of economic growth of 10% and over, thanks to expanded fixed assets investments and exports, huge trade surpluses and trade friction with other countries and domestic issues such as investment overheating, soaring real estate prices, electrical power shortages and growing wealth gaps, have become more pronounced of late, prompting the government to attempt to evolve to a more stable growth pattern, with the realization of 'an harmonious socialist society' as its long term goal. In order to curb investment overheating, the government has implemented a series of measures, including lowering the face value of construction bonds, stricter financing conditions for real estate investments, higher reserve rates, higher base interest rates on bank deposits and loans, prohibitions on new investments in investment-overheated industries and the introduction of personal income taxes on real estate liquidation sales. Also, in order to correct trade imbalances with other countries, efforts to make the foreign exchange system more pliable and to expand domestic consumption are advancing.

However, real GDP grew 11.9% in April to June, compared to the same period in the previous year, and 11.5% in July to September (11.3% forecast for the whole year), and with a balance of trade surplus at

$212.4 billion, higher than the previous year up till October, the reality is that the curbs are so far insufficient. This is because local governments, in pursuit of their own high economic growth, are negative towards investment curbs, and exchange intervention by Central Bank in order to restrain the renminbi's appreciation to within a specific range, has resulted in excess liquidity. The correction of domestic and foreign imbalances has been carried over to 2008.

Against this backdrop, the phenomenon of concentrated foreign direct investment in China, first noticeable in early 2000, has begun to change. China is still the largest investment recipient in Asia, but its share of investment worth globally has dropped from 9.5% in 2003 to 5.3% in 2006, and its share among the developing countries dropped from 29.9% to 18.3% over the same period. The amount received in investments in 2006 was $69.5 billion, falling below the previous year's total ($72.4 billion) for the first time in seven years. This was because of the fact that, while investments in non-manufacturing sectors increased, the decrease in investments in manufacturing industries was larger. Among the causes listed, in addition to the fact that some investments have run their course, were (1) a worsening investment environment (rising wages and a rising renminbi), (2) the increasing risks of concentrating investment in China, and (3) the emergence of new markets. Also, the Chinese government has intensified the selection of foreign investments in an attempt to enhance the level of sophistication of its industries, and this stance has also had its impact. There is a growing tendency now for manufacturers in labor intensive industries (products) to shift local production away from China to countries like Vietnam.

Also, India has seen continued high growth in recent years. Since independence, India's private sector corporate activity has been under government control, and continued import-substitution industrialization kept the economy stagnating. However, in 1991, a serious foreign currency shortage ushered in major economic reforms, centered around the shrinking of the public sector, the abolition of the industrial permit system, the liberalization of trade and foreign exchange, and the introduction of foreign capital. India's trade dependency (trade worth / nominal GDP) increased from 8.6% in 1991 to 20.3% in 2005, and the globalization of the Indian economy has advanced at a rapid pace, with increased direct investment as foreign investors pursue the rapidly expanding domestic market. The real GDP growth rate for fiscal 2005 (April, 2005, to March, 2006) was 9.0%, 9.4% in fiscal 2006, and 9.3% in April to June, 2007, compared to the same period in the previous year.

As might be expected from the large scale of its GDP, India's high level of economic growth is a factor in boosting economic growth in Asia, and is contributing to export growth in other Asian countries. In Taiwan in 2007 (January to October), exports overall have grown 8.9%, and exports to India have grown 67.3%, compared to the same period in the previous year. Further, the rapid expansion of trade between India and China is another recent feature. According to Chinese statistics, exports to India grew 67.5% in 2007 (January to September), compared to the same period in the previous year, while imports from India grew 31.7% similarly. China has become India's second largest import partner, after the EU (European Union).

2. Asia's economies in 2008

■ Economic growth rates slightly below those of 2007

While Asia's economies are expected to grow overall, boosted by expanding domestic demand, growth rates are expected to be slightly lower than those of 2007 (table on page 6). Korea and Taiwan are expected to post growth rates in the 4% range and, with the exception of Thailand, the ASEAN4 are expected to post stable economic growth. In contrast, China is likely looking at a very high 10.4% growth, and India and Vietnam 8.3% and 8.5%, respectively.

Among the negative factors affecting economic growth will be the deceleration of the US economy, spurred by the sub-prime loan issue (housing loans granted to persons with poor credit capability) and the soaring price of crude oil (the US economic growth rate for 2007 is presumed to be 2.3%, and the price of crude oil an annual average of $90 per barrel).

Firstly, with regard to the deceleration of the US economy, it is expected that this will cause Asian exports to the US (including roundabout exports) to fail to grow until mid 2008. However, the US share of global import worth fell, and as the Asian economies progress with the diversification of their export destinations, making very impressive increases in their exports within Asia, to the EU, and to the new emerging markets and crude oil producing nations, it is believed that they will be able to cover any

shortfall in exports to the US by quite a significant degree.

Then there is the soaring price of crude oil. If the price of crude oil remains high, it is likely to have a negative impact on the economic situation in terms of (1) inflation brought about by increases in the prices of manufactured goods and public utility charges, (2) sluggish consumption due to a reduction in real incomes, (3) higher interest rates in an attempt to curb inflation, and (4) pressure on corporate profits. The Asian economies have expanded domestic demand against a backdrop of low interest rates, so these impacts are a cause for concern (the degree of impact will depend upon whether that specific country is an oil producing country or a non-oil producing country, and upon its industrial structure and energy utilization ratio).

That said, the following factors are thought likely to soften the impact of the rising price of crude oil.

First, since 2006, with the exception of Indonesia and Taiwan, many countries have adjusted their currencies upwards against the dollar, and have been keeping inflation under control through lowering import commodity prices.

Second, the governments of some countries control fuel prices, and some countries are considering freezing fuel prices for a certain period of time.

Third, in light of the soaring price of crude oil and worsening environmental issues, some countries have begun full blown energy saving methods. At the Second East Asia Summit held in January, 2007, in the Philippines, it was agreed that the Asia Energy Efficiency and Conservation Collaboration Center (AEEC), a Japanese government initiative, should be established. It is hoped that this will lead to the spread of energy saving technology.

Fourth, the accelerated economic growth of the crude oil exporting nations will have positive effects on the economies of Asia. Specifically, these would be (1) increased exports from Asia as the purchasing power of the oil exporting nations grows and investments in those countries increases, (2) increased investment and tourism in Asia by the oil exporting nations, and (3) increased remittances from overseas workers in the oil producing nations. For example, Korean exports to Saudi Arabia in 2007 (January to September) increased 41.2% compared to the same period in the previous year. In Malaysia, where Islam is the state religion, there has been an increase in tourists from the Middle East, and investments are also growing. The government is aggressively targeting new investments through the development of 'Islamic finance'. Also, India and the Philippines are well known for their great numbers of workers overseas and many construction laborers from those countries are working in Middle East and the money remitted home by these workers is contributing to an expansion in domestic consumption.

Given the above, the governments of the affected countries need to develop appropriate policy mixes to minimize the impact of high crude oil prices and to strengthen their efforts to realize sustainable economic growth..

■ Important future trends

In addition to the above, there are three other important points to be considered as we look to the future of Asia's economies.

First, there is the changing pattern of development in China. With the realization of 'an harmonious socialist society' as its foundation policy, the Hu administration has developed a range of measures targeting improvements in the quality of life of agricultural communities and regional development, environmental and energy saving measures, and measures aimed at expanding consumption. In particular, in 2008, it is thought likely that measures to reform the exchange system, including the renminbi rate, will be pushed further forward in an effort to speed up the elimination of excess domestic liquidity and the correction of trade and other imbalances with foreign countries.

These ongoing changes in China's circumstances are forcing foreign enterprises to review their businesses in China, and at the same time represent the possibility of new investment destinations in other Asian nations. It must also be noted that the Chinese government is encouraging Chinese enterprises to invest abroad (production shift), as part of its efforts to correct imbalances with other countries.

Second, in a related matter, the possibility has emerged of progress in the industrialization of Cambodia and Laos, both of which are among the slowest developers of the ASEAN member nations. Increased industrialization will contribute to the correction of intra-regional wealth gaps. In Cambodia in recent years the garment and weaving industry has undergone very rapid growth as businesses in Hong Kong, Taiwan, China and Korea that produce brand goods for the US market have begun shifting production.

The industry employs many in the poorest classes and is, therefore, instrumental in reducing poverty. In Laos, eying the completion of the Second Mekong Bridge (the completion in December, 2006, of a bridge connecting Savannakhet in Laos and Mukdahan in neighboring Thailand in the East-West Economic Corridor), the construction of trade centers and factories in areas adjacent to the bridge and factories, warehouses and cargo terminals, etc., in areas connected by major highways, is underway. Handicapped by its interior location, industrialization in the region had been slow, but there are expectations now of a production shift from Thailand, as the international distribution network develops.

Third, efforts to realize Asian economic integration are picking up speed. Hitherto, attempts at Asian economic integration have taken the form of (1) economic integration within ASEAN (targeting the realization of an 'economic union' by 2015), (2) the concluding of economic partnership agreements with countries outside of ASEAN (China, Korea, Japan, etc.), and (3) the concluding of bilateral economic partnerships, but collaboration among Japan, China and Korea has been insufficient. In 2008, economic partnership talks between Japan and Korea are due to be restarted, and inter-governmental talks between China and Korea are also due to start. Thus, it is expected that efforts towards economic integration will gather momentum.

As to what form of economic integration should be sought in Asia, discussions among the concerned nations will likely become more intense, and some of the most important issues will surely be the further liberalization of trade, investment and the movement of people, as well as the correction of intra-regional wealth gaps and the formation of stratified collaborative relationships in the fields of finance, energy and natural resources, the environment, etc. The Japanese government will be expected to show initiative in these areas..

(Hidehiko Mukoyama)

Economic Prospects for 2008

(year-on-year, %)

1. Economic Growth

	2004	2005	2006	2006 (forecast)	2008 (forecast)
Korea	4.6	4.2	5.0	4.7	4.6
Taiwan	6.2	4.2	4.9	5.4	4.2
Hongkong	8.5	7.1	6.8	5.8	4.6
Thailand	6.3	4.5	5.0	4.2	3.7
Malaysia	6.8	5.0	5.9	6.0	6.1
Indonesia	4.9	5.7	5.5	6.2	5.7
Philippines	6.4	4.9	5.4	6.8	5.4
Vietnam	7.8	8.4	8.2	8.4	8.5
India	7.5	9.0	9.4	8.6	8.3
China	10.1	10.4	11.1	11.3	10.4

2. Consumer Prices

	2004	2005	2006	2006 (forecast)	2008 (forecast)
Korea	3.6	2.7	2.2	2.4	2.7
Taiwan	1.1	2.3	0.6	1.8	2.3
Hongkong	−0.4	1.0	2.0	1.6	2.4
Thailand	2.8	4.5	4.7	2.2	3.8
Malaysia	1.5	3.0	3.6	1.8	3.4
Indonesia	6.4	17.2	6.6	6.5	8.5
Philippines	5.9	7.6	6.2	3.0	5.0
Vietnam	9.5	8.3	6.6	8.3	8.5
India	3.8	4.4	8.7	6.5	6.5
China	3.9	1.8	1.5	4.7	4.0

3. Exports

	2004	2005	2006	2006 (forecast)	2008 (forecast)
Korea	31.0	12.0	14.4	14.3	10.5
Taiwan	21.1	8.8	12.9	9.6	8.1
Hongkong	15.9	11.6	9.5	6.9	9.8
Thailand	20.6	14.9	16.9	15.0	6.6
Malaysia	20.7	11.3	14.0	7.9	9.1
Indonesia	11.1	16.4	9.2	9.7	8.5
Philippines	9.5	4.0	13.9	5.4	6.0
Vietnam	31.4	22.4	22.0	20.0	20.0
India	28.5	28.0	22.0	15.0	10.0
China	35.4	28.4	27.2	24.0	11.8

4. Imports

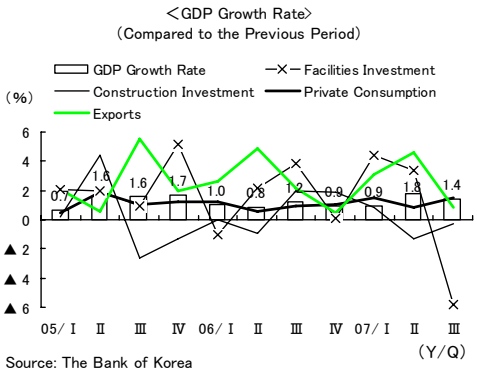
	2004	2005	2006	2006 (forecast)	2008 (forecast)
Korea	25.5	16.4	18.4	14.3	11.6
Taiwan	31.8	8.2	11.0	7.4	7.5
Hongkong	16.9	10.5	11.7	6.9	9.9
Thailand	16.8	25.3	25.7	8.0	18.0
Malaysia	25.8	9.0	14.4	9.7	10.9
Indonesia	25.6	16.7	9.2	9.7	8.5
Philippines	8.8	7.7	8.7	2.2	7.0
Vietnam	25.4	16.7	20.4	33.0	25.0
India	38.2	34.2	27.4	25.0	20.0
China	36.0	17.6	19.9	19.1	17.0

Notes: The figures in 2007, 2008 are forecasts by JRI.
Source: National Statistics

Korea *Expanded domestic and external demand leading to 4.6% growth in 2008*

■ Expanded domestic and external demand brings solid economic performance

Korea's economy is performing solidly, supported by expanded domestic and external demand. The real GDP growth rate for the period April to June was up 1.8% on the previous period (up 5.0% compared to the same period in the previous year), and up 1.3%, similarly, in July to September (up 5.2%, compared to the same period in the previous year). The growth rate for January to September was up 4.7%, compared to the same period in the previous year.



Source: The Bank of Korea

Growth in construction investment in July to September was negative for the second consecutive period, and that of facilities investment was negative in reaction to its hitherto positive growth, but exports continued to expand, with 0.8% growth over the same period. Private consumption was up 1.2%, similarly, driving economic growth.

As the economy continued to perform solidly, the government's policy interest rate was raised 0.25 percentage points on July 12, and then again on August 9. Part of the reason behind this was that continued low interest rates had caused massive amounts of capital to flow into the real estate and stock markets. Purchase prices for apartments in the Seoul area had soared in 2006, but have become more stable in 2007.

One recent characteristic of the Korean economy is the growing recovery capability of private consumption. Private consumption had expanded rapidly between 2001 and 2002, due to the effects of tax reductions and increased amounts of consumer credit. However, growing numbers of credit delinquencies prompted the government to introduce measures to curb consumer credit, and consumption growth quickly cooled, posting negative year on year growth in 2003 and 2004. Although growth did begin to recover, the growth rate was 0.8 percentage points below the real GDP growth rate in both 2005 and 2006. The rate recovered to 4.3% in 2007 (January to September), compared to the same period in the previous year, not far behind the economy's 4.7% growth rate in the same period. The factors behind this have been 1) the recovery in the national income (GNI: net overseas factor income and trading gains/ losses added to GDP), 2) a lower unemployment rate, 3) low interest rates, and 4) the asset effects of soaring stock prices (KOSPI went from 1,434 at the beginning of 2007 to 1,967 on November 14th). The consumer expectation index, indicating economic and living standard trends six months hence, was above the reference 100 mark (103.3 in October) for the first time since April, 2007.

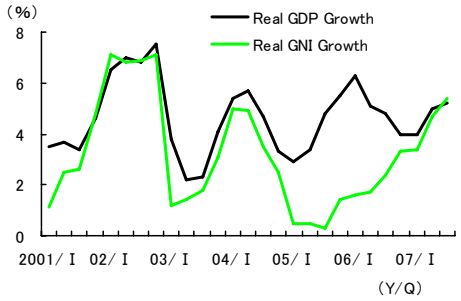
Another characteristic feature is that, in spite of the won's strength (the won – dollar rate went from $1 = 1,038 won in January, 2005, to 914 won by November 14, 2007), exports (customs cleared basis) are performing robustly. September's export value (dollar basis) was 0.3% down on the same month in the previous year due to the reduced number of working days because of the Chuseok holiday, but reversed the trend in October, growing 24.4% compared to the same month in the previous year.

This recent robust export performance is believed to be due to the facts that 1) while the won may be strong, it is still below its pre-currency crisis level ($1 = 850.8 won in January, 1997), 2) in the wake of the currency crisis, many businesses and others worked hard to cut costs, thus improving their export competitive strength, and 3) aggressive efforts have been made to cultivate new markets in growing markets. In terms of export partners, while exports to the US and Japan have failed to perform so well, exports to the EU (European Union) and BRICs, and other emerging markets and oil exporting nations have been growing. In 2007 (January to September) growth in exports to Korea's biggest export partner, China, grew 16.2%, slightly over the total growth of 12.7% (compared to the same period in the previous year), that for Russia grew 46.6% and that for Saudi Arabia 41.2%.

Given the foregoing, it is envisaged that the economic growth rate for 2007 will be 4.7%, supported by expanded domestic and external demand..

■ Economy progressing solidly, despite downside risks

In 2008, in spite of factors likely to limit economic growth, such as the deceleration of the US economy and the continuing high price of crude oil, domestic and external demand will continue to expand and the growth rate will probably be on a par with that of 2007.



Source: The Bank of Korea, Economic Statistical System

Private consumption is expected to perform as the driver of economic growth. Improvements in the income and employment situations are expected to keep private consumption growth in the 4% range. First, the GNI growth rate, which is closely connected with consumption, is rising. Second, the unemployment rate is coming down. The unemployment rate has fallen from 3.7% in 2005 to 3.5% in 2006 and to 3.2% in 2007, and is expected to be the same if not slightly lower in 2008. Third, the state of employment has improved. The Law on Non-Regular Work came into effect from July 1, 2007 (applying in 2007 to enterprises and public organizations with 300 or more employees, and from July 1, 2008, to enterprises with between 100 and 300 employees, and from July 1, 2009, to enterprises with between 5 and 100 employees), in conjunction with which, many non-regular workers are now being made regular workers. Since non-regular workers' average monthly salaries are about 60% of those of regular workers, and only roughly one quarter of non-regular workers receive bonuses, the promotion of non-regular workers to regular worker status will surely be a boost for consumption.

On the other hand, factors believed likely to inhibit consumption include 1) increases in non-consumption expenditure (direct taxation, public pension and social security insurance) and 2) rising consumer goods prices. Consumer goods prices rose by 3.0% in October, compared to 2.0% in August. This was caused by increases in transportation fares and food prices, reflecting the rises in international crude oil prices and raw materials prices. However, in addition to the fact that the strong won has kept imported goods prices down, the government is considering reducing the special consumption tax on heating fuels, so price rises through 2008 will probably stay at around 2%, and the impact on consumption is expected to be limited.

Additionally, exports will inevitably suffer some negative effects as a result of the deceleration of the US economy, but due to the facts that 1) Korea's dependency on US exports is gradually lessening (down from 20.7% in 2001 to 13.3% in 2006), 2) exports to China, whose economy continues to grow strongly, are growing at a steady pace, and 3) exports to the newly emerging economies and oil exporting nations, where domestic demand is expanding, are growing, it would seem safe to assume that 2008 will see a growth rate just slightly lower than that of 2007.

While export growth loses some momentum, the recovery in domestic consumption will move forward and growth in facilities investment will probably be in the mid 7% range, close to 2007's figures (estimate 8.6% growth). There is a strong possibility that construction investment will grow by only the most modest of margins, influenced by the poor growth rate in housing loans. Given the above, the forecast is that private and other domestic consumption will expand stably and that exports will continue to grow solidly, giving an economic growth rate of 4.6%.

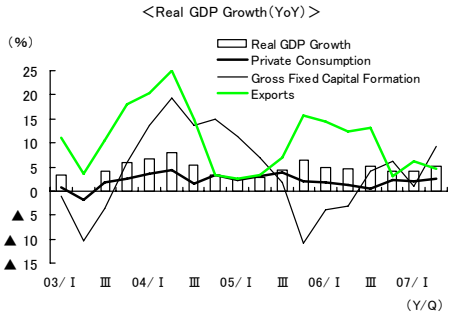
The downside risks are that the deceleration of the US economy will have domino effects globally, causing stock prices to fall sharply, and that the subsequent period of adjustment will be a protracted one. The latter is likely to be triggered by growing fears of a deceleration in the global economy and tighter monetary policies in China. The recent recovery in consumption has been supported by the mid to high income brackets and any drastic fall in stock prices will surely blunt the purchasing appetites of those in the higher income brackets. Also, Korea will hold presidential elections in December, 2007. The conservative vote is split by the candidacies of the Hannara Party's Lee Myung-Bak and Lee Hoi-chang (the party's former general secretary), making it impossible for anyone to predict the outcome of the election. However, whichever candidate wins, the correction of domestic wealth gaps and the vitalization of the economy will still be the main issues.

(Hidehiko Mukoyama)

Taiwan 4.2% economic growth in 2008

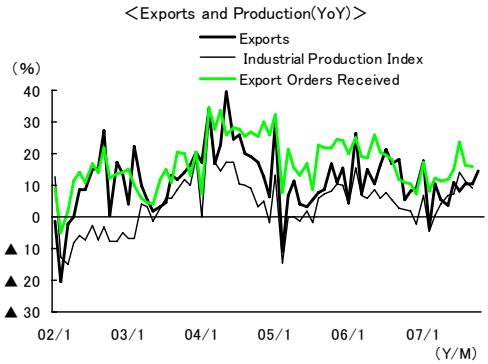
■ Economy rallies, supported by export recovery

Taiwan's economy began to decline ever so slightly from the autumn of 2006, and the real GDP growth rate for October to December of that year (compared to the same period in the previous year) was 4.0%, then 4.2% in January to March, 2007, and recovered to 5.2% in April to June and 6.9% in July to September. July to September saw export momentum pick up with 11.1% growth, compared to the same period in the previous year, and total fixed capital formation grew by a solid 5.0% (private sector fixed capital formation grew 6.5%). Also, the failure of real wages to grow and issues of credit card repayment delinquency, caused private consumption growth to slow to just 0.8% in July to September, 2006, but subsequent improvements in the employment and income environments helped this figure to recover to 3.5%.



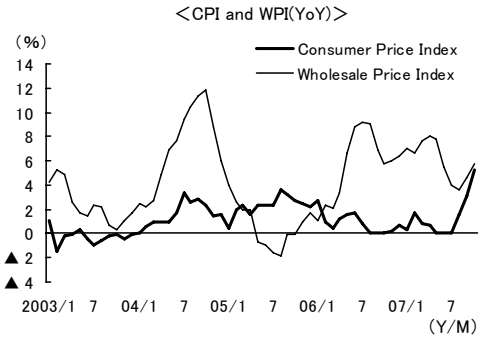
Source: Directorate General of Budget, Accounting and Statistics

Recent trends indicate more and more clearly that the economy is in recovery. First, encouraged by the recovery in IT related demand, export growth in September was 10.6%, compared to the same period in the previous year, strengthening to 14.4% in October. Reflecting increased export growth and on-going inventory adjustments, the manufacturing production growth rate has risen. The value of export orders received, which is an indication of the future performance of exports, grew 16.3% in August, followed by 16.1% growth in September, a robust performance. To date, there is no sign of any impact from the US sub-prime loan issue.



Source: Department of Statistics, Ministry of Economic Affairs

As export growth picks up the pace, sales figures in IT related industries are also gathering momentum. The semiconductor and liquid crystal panel industries had ramped up production in anticipation of the 'Vista Effect', but computer demand failed to grow as expected and business showings declined from the start of 2007. However, semiconductor foundry manufacturer TSMC (producing semiconductors for other companies) recovered to positive growth in July. Liquid crystal panel manufacturers enjoyed their highest ever sales figures in the period July to September.



Source: Directorate General of Budget, Accounting and Statistics

Private consumption is also recovering with automobile sales (registered basis) posting positive year on year growth in July for the first time in 21 months, reaching 32.6% in September.

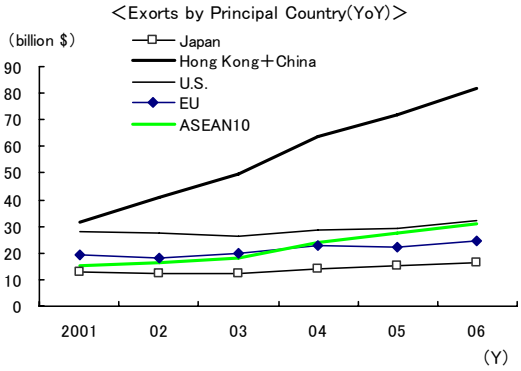
While the economy is indeed rallying, the rise in commodity prices has emerged as a new problem. Soaring prices of crude oil and raw materials caused wholesale prices to begin to rise from the middle of 2006, causing the government to raise its policy interest rate in September and December of that year, and also in March and June of 2007. However, the wholesale price rise rate accelerated again in September and October, causing consumer prices to rise very sharply from August onward (October's 5.3% rise was due to the skyrocketing price of vegetables in the wake of typhoon damage, and the rise in the prices of petroleum prices) and these and other inflationary pressures are growing in strength. For this reason, the policy interest rate was raised a further 0.125 percentage points on September 21(bringing the rate to

3.25% as of September 25).

The real GDP growth rate for 2007 is expected to turn out to be 5.4%, but the fact is that the future is becoming ever more unclear.

■ **Domestic and external demand will continue to expand, despite threat of downside risk**

In 2008, in spite of the effects of the deceleration of the US economy and rising commodity prices, Taiwan's economy will likely achieve growth in the 4% range, boosted by expanding domestic and external demand.



Source: Department of Statistics, Ministry of Finance

First of all, exports are expected to play the role of driver of the economy. Through the first half of the year, exports to the US (including those via third countries) will probably weaken, due to the effects of slowing private consumption in the US, but increased exports to other countries and regions are expected to push export growth for 2008 (customs cleared basis) to around 8%. The top export destinations in 2007 (January to October) currently are 1) China and Hong Kong (40.6%), 2) ASEAN 6 (14.4%), 3) US (13.1%), and 4) EU (10.9%). Export dependency on the US is gradually trending downwards and export value, in contrast to that of exports to China and Hong Kong which are growing at an outstanding pace, is just managing to hold steady.

Amidst overall export growth of 8.9% in 2007, exports to China and Hong Kong grew 11.5% and to the EU 11.8%, while exports to the US contracted by 2.7%. Outstanding growth was shown by exports to the emerging economies and oil producing nations, such as India (67.3%), Saudi Arabia (41.0%), Vietnam (33.2%) and the UAE (32.7%). This trend is highly likely to continue in 2008. Among the reasons are 1) the increased purchasing power of the oil producing nations as the price of crude oil rises, 2) the continuing production shift of Taiwanese businesses to mainland China and the recent expansion of ventures into countries like Vietnam, raising expectations of increased exports of raw materials, parts and components, and machinery, and 3) the fact that the New Taiwan dollar has held more or less steady against the US dollar, unlike other Asian currencies that have all appreciated against the dollar, enhancing Taiwan's competitive edge.

Next, it can be considered that private consumption, fixed capital formation and other forms of domestic demand will contribute to economic growth. While improvements in the household accounts balance sheet will likely sharpen consumption appetites, the slow pace of improvement in incomes and employment, and rising consumer goods prices, will probably hold private consumption growth to within the 3% range. While there are concerns over inflation, in addition to the relaxation of temporary factors such as the sudden increase in vegetables due to typhoon damage, the government has begun efforts to tackle commodity prices and inflation is expected to be contained to within the 2% range.

As regards fixed capital formation, both the private and public sectors are expected to show stable growth. In the semiconductor and liquid crystal panel industries, the construction of next-generation factories continues to push ahead. Taiwan has ten factories capable of producing large scale silicon wafers of 300mm diameter (making it No. 1 in the world), and this number is due to be increased to 18 in 2008. In the case of liquid crystal panels also, it is expected that there will be investments in projects to increase scale, against a backdrop of expanding demand (for PCs, mobile telephones, TVs, etc.).

Further, there are expectations of investments in fields such as digital content and bio-technology. Additionally, the Taiwanese government set out its '2015 Economic Development Vision' in 2006, as a successor to 'Challenge 2008'(a comprehensive six year development plan, formulated in 2002). As the first step in the project, a three year plan (2007 to 2009) has started, centered on the provision of infrastructure and the development of an environment in which to foster new industries, and gross fixed capital formation is expected to grow on the order of 8%.

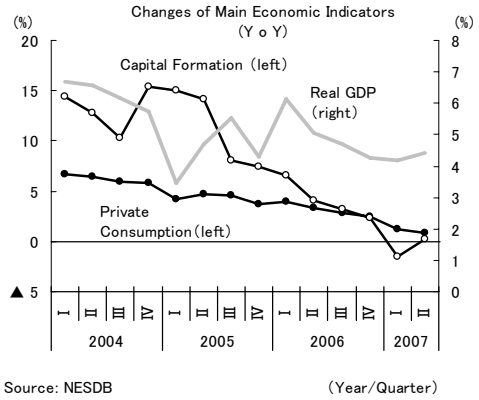
From the foregoing, it can be expected that, due to the expansion of domestic and external demand, Taiwan's economy will grow by 4.2% in 2008.

(Hidehiko Mukoyama)

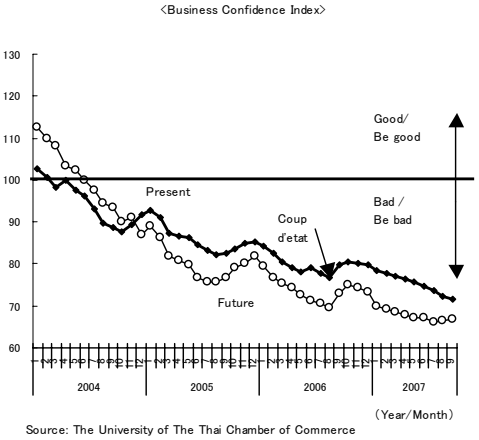
Thailand 3.7% economic growth forecast for 2008

■ Stagnant domestic demand holds 2007 growth to 4.2%

Thailand's real GDP growth rate in 2007 could only manage 4.2% in January to March, compared to the same period in the previous year, then 4.4% in April to June, due mainly to political uncertainty in the country as well as the continued stagnation of domestic demand. Though the new constitution was promulgated in August, on schedule, real recovery in domestic demand has had to be carried over till the new year, and economic growth for the whole year is expected to turn out to be 4.2%, year on year.



Private consumption growth dropped noticeably from 1.3% in January to March to 0.9% in April to June. In particular, there were very significant decreases in expenditure on consumer durables, down 7.4% in January to March, and down 9.0% in April to June. Sales of automobiles and motorbikes in the period January to September were 451,325 (down 7.6% compared to the same period in the previous year) and 1,156, 152 (down 22.5%, similarly), respectively, falling below the previous year's levels in both cases.



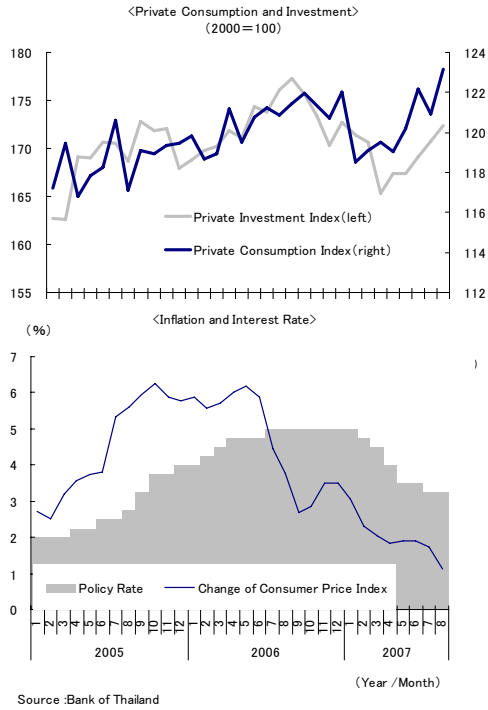
Additionally, capital formation has been in decline in recent years and was minus 1.5% in January to March, compared to the same period in the previous year. Though it did recover somewhat in the period April to June, this was a very modest 0.2% increase. One of the main reasons behind this appears to have been the fact that both domestic and foreign enterprises decided to hold off on new investments, waiting to see how the political situation developed. This is clearly shown in the business confidence index produced by the University of the Thai Chamber of Commerce. Though the index did turn upwards in the wake of the coup d'état of September, 2006, the government's subsequent lack of consistency over foreign exchange regulations, terrorist attacks in Bangkok, the resignation of the deputy Prime Minister, etc., served to bring down the index through 2007 overall. However, confidence in the future did appear to rally slightly in September, after the new constitution was promulgated.

Under these circumstances, with domestic demand performing so poorly, it was export performance that drove economic growth. Exports for January to September earned $110.6 billion, up 16.1%, compared to the same period in the previous year. This reflects the fact that the production in many of the multi-national enterprises that have set up business in Thailand in recent years is now getting up to full steam. Among those, automobiles and other types of transportation equipment were up 29.6% in the same period, worth $9.4 billion, and hard disk drives (HDD) were up 34.2%, worth $6.4 billion, both massive increases. In addition, imports were hampered by poor domestic demand and could only manage 6.4% growth in the same period, worth $102.1 billion, resulting in a trade balance surplus of $8.5 billion.

■ 2008 likely to see a recovery in domestic demand, but increases in the price of crude will present a new barrier

Domestic demand is expected to make a recovery in 2008, on condition that a new government is in place in the new year. The general election scheduled for late 2007 will be closely contested between the new pro-Thaksin People's Power Party (Palang Prachachon), and the anti-Thaksin Democratic Party,

and there is no way to forecast the result, but since the election system has changed from a single member constituency system to a multi-seat constituency system, it will be difficult for any single party to gain a simple majority, thus forcing a coalition government. And, whichever party ends up with the majority, the prevailing view is that coalition policies will hold sway. For example, in response the to the People's Power Party's declaration that it will continue the poverty relief and regional economy vitalization policies of the old Thaksin administration, the Democratic Party, in an attempt to win over the pro-Thaksin element in the Northeast and Northern provinces, is promising free education up to high school level and free medical treatment and expanded social security. Also, in an attempt to restore foreign investors' confidence, the Democratic Party has promised to discontinue the Foreign Business Act, which has tightened restrictions on foreign investments, and to relax the foreign currency restrictions introduced at the end of 2006, but even if the People's Power Party gains power, they will have to implement similar measures.



Source :Bank of Thailand

Real recovery in domestic demand will need to wait until 2008 and recent figures suggest that private consumption indices and private sector investment indices are trending upwards since the completion of the draft new constitution in June. Meanwhile, the manufacturing industry's capacity utilization rate was over 75% in September, which means that new investments can be expected. According to the Board of Investment (BOI), the cumulative total foreign investment applications (January to October) were up in terms of the number of applications, from 598 in the same period last year to 696, and also in terms of investment worth, from Bt199.7 billion to Bt371.8 billion. Further, the policy interest rate had risen in step with rises in commodity prices since 2004, but was lowered five times in 2007, coming down from 5.0% at the start of the year to 3.5%. In addtion, in order to get economic recovery properly on track, the provisional Surayud administration has put together a budget for fiscal 2008 (October, 2007, to September, 2008) that includes a Bt165 billion deficit. Also, the rail network and other mega projects that had been put on hold due to political uncertainty have kicked off again.

Nevertheless, the potential impact of the high price of crude oil must not be viewed too lightly. Thailand relies on imported crude oil, accounting for a huge 12% of imports. Incidentally, Thailand's balance of trade for 2005 went from a $2.5 billion surplus to a $7.2 billion deficit because of the rise in the price of crude oil the previous year. In comparison with those days, the baht is appreciating steadily against the dollar and energy saving initiatives have been put into practice, so it is likely that much of the shock of soaring crude oil prices can be absorbed, but if prices such as $100 a barrel were to continue, there is every possibility that the balance of trade surplus could turn into a deficit. Further, if rising crude oil prices push up consumer prices, private consumption will be inhibited and, if the consumer price rise were to exceed 4%, Bank of Thailand (Central Bank) would have no choice but to raise the policy interest rate, which would be an inhibitor of private sector investment.

Based on the foregoing, it would appear reasonable to expect that the economic picture in 2008 will be one of competition between the positive factor of the return to political stability and the negative factor of rising crude oil prices. However, given that crude oil prices can be expected to continue to rise to some extent, the economic growth rate will likely be below the previous year's level, at 3.7%. Of course, even after the new government is installed, there is always the risk of continued fighting between the new pro-Thaksin camp and the anti-Thaksin camp. If this were to be the case, then even 3% growth might prove difficult.

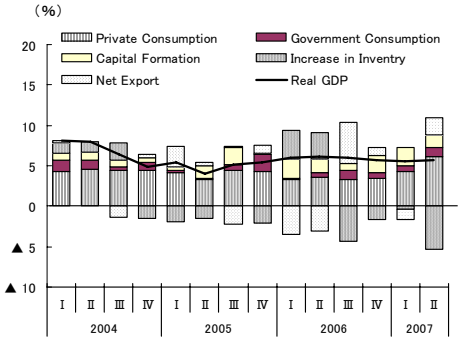
(Keiichiro Oizumi)

Malaysia 6.1% economic growth forecast for 2008

■ 6.0% growth in 2007, fed by domestic demand

Malaysia's real GDP growth rate for 2007, powered by solid private sector investments and vigorous private consumption, was 5.5% in January to March, compared to the same period in the previous year and 5.7% in April to June, similarly. Healthy domestic demand has been maintained through the end of 2007, and the growth rate for the whole year is expected to be 6.0%.

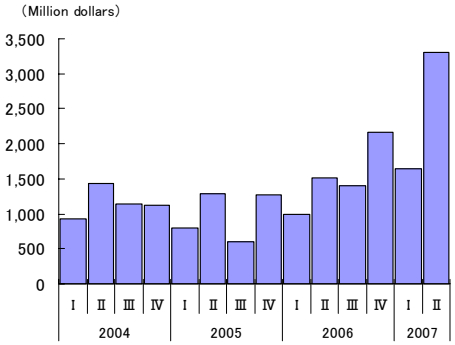
<Contribution of Expenditures to Real GDP>



Source: Malaysia Central Bank (Year/Quarter)

Private consumption in particular, encouraged by a healthy employment environment, stable interest rates and greater disposable income in agricultural households due to the increases in international prices of agricultural products, grew strongly in January to March, compared to the same period in the previous year, at 8.6%, and at 11.3% in April to June, similarly. In addition, fixed capital formation, boosted by increased investments on the part of state-run enterprises as part of the Ninth Five Year Plan (2006 to 2010) and increased private sector investments mainly in the service sector, grew 9.9% in January to March compared to the same period in the previous year, and 6.6% in April to June, similarly. Foreign direct investment, which has fared poorly in recent years, tended to increase more strongly throughout 2007, and the balance of payments shows that the amount of capital flowing in during the period January to June was up 97.5%, compared to the same period in the previous year, at $4.941 billion. Part of the reason for this has been that, as investors review China's overheating investment environment and shy clear of neighboring Thailand's political instability, Malaysia has once again become a candidate for direct investment. Further, in addition to a capacity utilization rate of over 80% in the manufacturing industry, the investment worth of projects approved by Malaysia's Ministry of International Trade and Industry (MITI) in the period January to August was up 23.8% compared to the same period in the previous year, at 35.8 billion ringgit. Investments are thought likely to continue to grow from the end of the year through the first half of 2008.

<Inflow of Foreign Direct Investment in Balance of Payment>



Source: Malaysia Central Bank

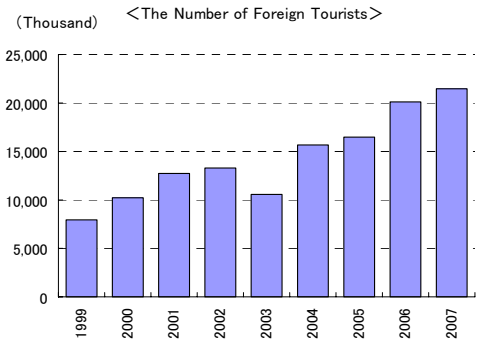
External demand was up 7.3% in January to August, compared to the same period in the previous year, at $111.8 billion. Broken down by industry, electrical and electronic goods, which account for 48% of exports, were up by a mere 1.3% in the same period, at $53.9 billion, but chemical products did better, growing 25.7%, similarly, worth $7.1 billion, as did palm oil, growing 38.2% over the same period, worth $3.5 billion. Elsewhere, although expanded internal demand has meant an increase in imports of consumption goods, imports of intermediate goods for electrical and electronic products were down so that imports overall grew by only 9.8% in the same period, worth $94.3 billion, resulting in a trade surplus of $17.5 billion. As a result, the foreign trade reserves at the end of September stood at a record high of $79.5 billion..

■ Growth in 2008 boosted by recovery in external demand to 6.1%

In 2008, due to a healthy employment situation and an increase in disposable incomes, brought about sustained economic performance, private sector investment will maintain 7.5% year on year growth.

The number of foreign tourists (arrivals basis) grew 23.9% in January to July, 2007, compared to the same period in the previous year, to 12.4 million and looks likely to top 200 million for the year. The forecast for 2008 is 21.5 million. In recent years, there has been an increase in the number of foreign tourists, particularly from fellow Islamic nations in the Middle East. As regards fixed capital formation, though public utilities investments will likely be restrained to 0.2% year on year growth, from the perspective of improving financial health, domestic and foreign enterprises' investments will pick up and 6.5% growth is forecast. In terms of external demand, exports are expected to show 10% year on year growth, thanks to a recovery in the international market for electrical and electronic goods and the effect of the rising price of crude oil and petrochemical products, beneficial to Malaysia as an oil producer. On the other hand, though capital goods will increase, imports will likely only grow at about the same pace as exports. Thus, robust domestic demand will double up with a recovery in external demand so that the outlook for the real GDP growth rate in 2008 is just over that of 2007 at 6.1%.

While the rising price of crude oil is seen as a potential hindrance to economic growth in Asia overall, it may be thought of as bringing positive benefits to Malaysia. Of course, rising crude oil prices will inevitably mean rising commodity prices, and there are concerns over the impact on consumption. However, as an oil producer, Malaysia can expect an increase in exports and, given that Malaysia depends on crude oil related tax revenues and income transfers from petroleum related state-run enterprises for close to 40% of its fiscal income, government policy freedom is increasing. In actual fact, the rising and continually high price of crude oil in recent years has made it possible to expand public utilities investments and to increase the wages of public officials. In addition, plans are to continue to reduce taxation on private sector enterprises, with the corporate tax rate due to be lowered from its current 28% to 27% in 2008 (and to 26% in 2009). Also, Malaysia has succeeded in procuring $1.2 billion from oil exporting nations in the Middle East as financing for the provision of infrastructure in the Iskandar Development Region (IDR: southern Johor, adjacent to Singapore), modeled on Hong Kong and Shenzhen. Further, the financial sector has also grown remarkably, centered on Islamic financing, and plentiful capital is flowing into the stock market. The Kuala Lumpur Composite Index (KLCI) rose from 1,189 points at the start of the year to 1,336 points in September and the increased assets brought about by this rise in stock prices is a new factor supporting vigorous private consumption. This trend will likely be sustained in 2008 also.



Note: 2006,Estimate; 2007,Projection
Source: Ministry of Tourism, Ministry of Finance

Against this backdrop, the Abdullah administration has worked out its own economic policies. For example, in November Malaysia concluded an Economic Partnership Agreement (EPA) with Pakistan. This not only targets the liberalization of trade, but aims to promote investment as well and is planned as a means of enhancing Malaysia's role as a window to the Middle East. Also, in order to improve the quality of personnel in the financial sector, in addition to domestic personnel training, the government is looking into a unique scheme that will involve issuing multi-visas to Chinese and Indian workers resident in the international financial capitals New York, London, Hong Kong and Singapore.

Elsewhere, the manufacturing industry, which accounts for 40% of Malaysia's GDP, posted 3.9% year on year growth in 2007, and this is expected to grow to no more than 4.0% in 2008. In particular, as the US is Malaysia's main export partner for electrical and electronic goods, a deceleration in the US economy, spurred by the sub-prime loan issue or other factors, will possibly delay a recovery in that sector. In response, the Abdullah administration is putting its efforts into the fostering of uniquely Malaysian industrial technology in fields such as bio-technology and bio-energy, utilizing Malaysia's natural resources, and is hurrying to evolve out of an industrial structure that is overly dependent on the production of electrical and electronic goods. 2008 will see much attention paid to how the Abdullah administration implements policies in the tailwind of rising crude oil prices.

(Keiichiro Oizumi)

Philippines 2008 economic growth rate down to 5.4%

■ 2007 real GDP growth rate expected to be 6.8%

Real GDP in the Philippines grew a healthy 7.3% in the period January to June, 2007 (7.1% in January to March, 7.5% in April to June), compared to the same period in the previous year. Though growth did reach 6.4% in 2004, the average for the period 2001 to 2006 was 4.6%, and 2007's performance can be said to be of a very high level. Among the contributing factors are the falling consumer price increase rate, increased government and personal consumption as a result of mid-term elections, increased amounts of money remitted home by workers abroad, and a rapid increase in public investments in the wake of improvements to the fiscal deficit.

Figures for July to December are expected to show solid performance also, even if the economy does decelerate slightly. Money remitted home by overseas workers in the period January to June increased by 18.1% compared to the same period in the previous year, worth around $7 billion, and this figure is expected to grow strongly in the future, and along with a stably low consumer price increase ratio will likely support personal consumption. Meanwhile, the public investment growth rate is expected to drop slightly and the continued rise of the exchange rate will likely have a negative impact on export growth.

2007's real GDP growth rate is expected to turn out to be on the order of 6.8%. Personal consumption in the period January to June was 6.0%, compared to the same period in the previous year, encouraged by the significant drop in the consumer price increase rate and steady increases in the amounts of money remitted home by overseas workers. It is expected that personal consumption will maintain its robust pace in the future.

＜Real GDP by Expenditure Shares＞

(compared with the same quarter of last year、%)

	2006-Q1	2006-Q2	2006-Q3	2006-Q4	2007-Q1	2007-Q2
Real GNP	6.3	6.4	5.6	6.1	7.7	8.3
Real GDP	5.7	5.5	5.1	5.5	7.1	7.5
Personal Consumption	5.3	5.4	5.2	5.8	5.9	6.0
Government Consumption	7.6	3.3	4.5	9.9	9.9	13.5
Fixed Capital Formation	2.4	▲ 1.0	2.1	2.2	8.5	10.0
Exports	13.0	21.2	9.2	2.3	9.9	4.2
Imports	0.7	4.0	1.2	1.4	▲ 2.1	▲ 11.2

Source: National Statistical Coordination Board

Fixed capital formation grew rapidly by 9.3% in January to June. However, this was due to the 18.7% growth in construction investment, centered mainly on a 33.8% increase in the public sector, and durable equipment investment, which had languished for some time, managed to recover to positive growth, but even this was only 2%. Moving on, fixed capital formation will likely begin to decelerate.

Exports grew 6.3% in January to June, compared to the same period in the previous year (export and import figures both on customs cleared basis). In electronics related exports, semiconductor exports grew 8.6%. Mineral product exports also did well, growing 52.6% thanks to increased exports to China, but clothing exports suffered from the rising exchange rate and suffered minus 11.3% growth, as did agricultural products at minus 5.1% growth. Looking forward, there are fears of a global economic slowdown and a real recovery in export growth would appear to require some time yet. On the other hand, imports could only manage 4.1% growth in January to June. Consumer goods posted a very respectable 12.8% growth, but capital goods were down 9.2%, reflecting the failure of durable equipment investment to grow.

The consumer price index was up 2.6% in January to August, compared to the same period in the previous year. Lower food prices reflecting healthy agricultural production, and lower import prices due to the peso's appreciation have contributed in this case. However, there are still many causes for concern, such as the rising price of crude oil and the fact that the money supply growth rate was over 20% compared to the same period in the previous year. Central Bank, after reducing interest rates by a hefty margin in July, implemented yet another 0.25% cut in October. The aim here is to try to curb the rising exchange rate accompanying capital inflow, as well as to support flagging durable equipment investments. Meanwhile, policies designed to absorb liquidity have also been implemented.

In the period January to June, the fiscal deficit was 41 billion pesos (target was 31.3 billion), and the target of 63 billion pesos for the year looks difficult to achieve. One of the main factors involved is that tax revenues have fallen short of the target amount by 12.9%. In addition to reduced value added tax revenues due to the low consumer price index, and lower customs revenues due to falling import growth, it appears that tax collection vacillated in the runup to the mid-term elections, and the securing of tax revenues as part of attempts to balance the budget has surfaced as a pressing issue.

■ 2008 real GDP growth rate expected to be 5.4%

In 2008, the Philippine economy will likely slow down due to the effects of the high price of crude oil, and real GDP is expected to grow by around 5.4%.

Money remitted home by overseas workers is expected to continue to grow confidently in the future and there will probably be little change in the economic structure, where personal consumption plays the role of growth driver. However, the rising exchange rate means that when money remitted home by overseas workers is converted into pesos, the take home value will decrease, and this could become a serious problem for those consumers whose livelihoods depend largely on this income.

Turning to fixed capital formation, the expansion of public investments, such as infrastructure provision, is expected to continue, and construction investment will continue to grow strongly, albeit slightly weaker than the previous year. It is expected that this will contribute to a fundamental boost in the mid-term growth rate. Meanwhile, export recovery is taking time, and the failure of durable equipment investment is likely to continue.

＜Main Economic Indicators＞

(YoY、%)

	2005	2006	2007	2008
Real GDP	4.9	5.4	6.8	5.4
Agriculture	1.8	4.1	4.0	3.5
Industry	4.9	4.8	6.5	4.8
Services	6.4	6.3	8.0	6.6
Personal Consumption	4.8	5.5	5.9	5.4
Government Consumption	1.6	6.1	10.5	8.5
Fixed Capital Formation	▲ 6.6	1.4	1.5	1.4
Exports(in US Dollars)	4.0	13.9	5.4	6.0
Imports(in US Dollars)	7.7	8.7	2.2	7.0

Notice: forecasts for 2007 and 2008
Source: NSCB and others

While the real GDP growth rate is thought likely to trend upwards in the mid term, among the short term risk factors are, firstly, external influences such as the US economy and the price of crude oil. A deceleration in the US economy and lowering of US interest rates will increase room for Philippine interest rate cuts, but will have the effect of inhibiting export growth and money sent home by overseas workers. With the continued upward pressure of the peso, the possibility is very strong that export growth recovery will still take some time. Also, since more than 95% of petroleum demand depends on imports, if crude oil prices stay high, imports will increase and the consumer price index will go up, causing domestic demand to slacken and economic growth will probably be affected as well. The annual consumer price indices since 2004 have been 5.9%, 7.6% and 6.2%, clearly reflecting the impact of rising crude oil prices. Since the end of 2006, the year on year rise of the price of crude oil appears to have taken a break and the consumer price increase rate has fallen acutely, but if the price of crude oil stays high in the near future it is likely that the consumer price index will rise again. Nevertheless, since the end of 2005, the peso has been increasing in value at around 10% per annum, so that the impact of crude oil and other international commodity price rises on domestic prices has been softened to some degree, and this trend is expected to continue in the future.

＜Fiscal Balance＞

(billion pesos,%)

	2002	2003	2004	2005	2006
Revenue	578.4	639.7	706.7	816.2	978.7
Tax Revenue	507.6	550.5	605.0	705.6	859.2
Other Revenue	70.8	89.3	101.8	110.5	119.5
Expenditure	789.1	839.6	893.8	962.9	1040.9
Interest Payments	185.9	226.4	260.9	299.8	310.1
Fiscal Balance	▲ 210.7	▲ 199.9	▲ 187.1	▲ 146.7	▲ 62.2
of Nominal GDP	▲5.0	▲4.3	▲3.6	▲2.5	▲1.0

Source: Bangko Sentral Pilipinas

Secondly, the increase in capital inflow and exchange rate trends need to be considered. The rise in the exchange rate has served to inhibit inflation, but any drastic rise will need to be avoided if solid economic performance and social stability are to be maintained. Also, increased capital flow is making it difficult to curb the money supply. Central Bank will need to implement the most appropriate policies, such as exchange rate intervention, monetary policy and the change of regulations for capital transactions.

Thirdly, there is the instability of the political situation and fiscal balance trends. In the mid-term elections the ruling party gained a majority of seats in the lower house, making any impeachment motion virtually impossible and raising the possibility that the president will see out her term of office until 2010. However, there are many junior officers in the military who harbor serious dissatisfaction against the current administration. And, according to a September opinion poll, the percentage of those supporting the president was 11 points below those opposing her. This fact shows that there is continuous criticism of the government among the poor. As the president's term of office nears closure, it cannot be denied that the current administration's power base has become ever more fragile. Against this backdrop, it is a matter of some concern as to whether the government can improve the taxation system and strengthen tax collection in order to reduce the fiscal deficit. **(Satoshi Shimizu)**

Indonesia 5.7% economic growth forecast for 2008

■ Lower interest against a backdrop of solid economic performance

Indonesia's real GDP growth rate for the period January to June, 2007, was 6.1%, compared to the same period in the previous year, with domestic demand in the role of growth driver. Bank Indonesia estimates that the growth rate for July to September will be 6.3%, compared to the same period in the previous year, and with the economic situation looking up over the latter half of the year, economic growth for the whole year looks like it will achieve 6.2%.

A market awareness survey conducted by Bank Indonesia for the period July to September reveals that many economists have placed both their real GDP growth rate estimates for 2007 and their inflation rate estimates at between 6.1 and 7.0%, the exchange rate (against the dollar) at between 9,001 and 9,500 rupiah and the balance of current account (against GDP) at between 1.5 and 3.0%. In comparison with the survey for April to June, the growth rate is up 1 point, and there seems to be consensus that the economy is looking up over the latter half of the year.

In terms of GDP demand items during January to June, private consumption grew 4.7% compared to the same period in the previous year, and fixed capital formation grew 7.3%, similarly. The addition of domestic demand to external demand-dependent growth has meant that the economy has begun to regain some of its strength. On the supply side, only agriculture was significantly below the previous year's performance, and all other sectors performed solidly.

Automobile and motorbike sales for January to August were up 11.0% and 37.6%, respectively, compared to the same period in the previous year. In September, the Indonesian Automobile Manufacturers Association revised its 2007 automobile sales forecast upwards to 410,000 vehicles, and also announced a forecast of 460,000 vehicles for 2008. The Association commented that the lowering of the policy interest rate (BI rate) and investment in new vehicles had spurred consumption, although the pace of recovery was still mild and it would likely take some time before the record levels of 2005 (530,000 vehicles) could be repeated.

On the other hand, the recovery in investments has been outstanding. Foreign direct investments (approved basis) in the period January to August totaled 1,320, worth $31.3 billion. This represents a 17.5% increase in the number of applications, compared to the same period in the previous year, and an increase of 3.5 times in the investment worth. Domestic private sector investment (approved basis) also grew 41.0% compared to the same period in the previous year in terms of numbers of applications, at 189 applications, and 50.9% in terms of investment value, at 146 trillion rupiah. Both foreign and domestic investments are performing well, but some 60% of the approved amount of foreign direct investment is accounted for by large projects like the construction of oil and gas refineries and the expansion of chemical plants, and it is uncertain as to whether these can maintain their momentum in the future.

<Main Economic Indicators>

(Rupiah,%)

	2005 Actual	2006 Actual	2007 Estimation 2007/Ⅱ Survey	2007 Estimation 2007/Ⅲ Survey
GDP Growth Rate	5.7	5.5	5.1-6.0	6.1-7.0
Inflation Rate	17.1	6.6	6.1-7.0	6.1-7.0
Exchange Rate	9,713	9,167	9,001-9,500	9,001-9,500
Current Account (% of GDP)	0.10	2.70	1.5-3.0	1.5-3.0
Export Growth Rate	22.93	18.98	15.1-22.5	15.1-22.5
Import Growth Rate	37.24	6.34	7.6-15.0	7.6-15.0
Budget Balance (%of GDP)	0.90	1.04	2.1-2.5	2.1-2.5
Unemployment Rate	11.24	10.40	10.1-11.0	10.1-11.0

Source: Bank Indonesia, *Market Perception Survey Quarter Ⅲ 2007*

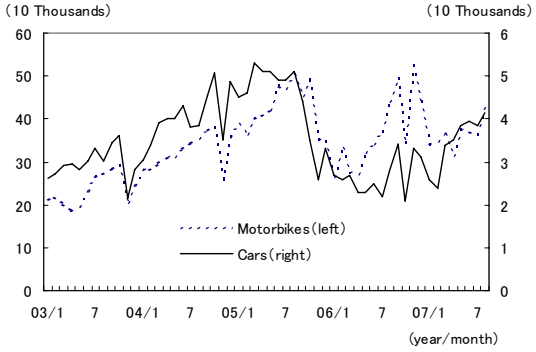
<Economic Growth>

(Trillion Rupiah,%)

	2005	2006	Growth Rate	2007 Jan-Jun	Growth Rate
Private Consumption Expenditure	1,043.8	1076.9	3.2	554.4	4.7
General Gov. Consumption Expenditure	134.6	147.6	9.7	69.5	3.8
Gross Domestic Fixed Capital Formation	393.2	404.6	2.9	210.0	7.3
Change in Stock	18.7	13.1	▲ 29.9	7.0	-
Statistics Discrepancy	4.3	24.1	460.5	17.9	-
Export of goods and services	792.0	864.5	9.2	477.9	9.4
Import of goods and services	635.9	684.1	7.6	355.2	7.8
GDP	1,750.7	1846.7	5.5	961.5	6.1
Agriculture, Livestock, Forestry & Fishery	253.7	261.3	3.0	134.4	0.7
Mining and Quarrying	165.1	168.7	2.2	86.6	4.9
Manufacturing Industry	491.4	514.2	4.6	264.8	5.4
Electricity, Gas and Water Supply	11.6	12.3	6.0	6.5	9.5
Construction	103.5	112.8	9.0	59.2	8.6
Trade, Hotel and Restaurant	293.9	311.9	6.1	163.8	8.2
Transport and Communication	109.5	124.4	13.6	66.5	11.6
Financial, Ownership & Business Services	161.4	170.5	5.6	90.1	7.8
Services	160.4	170.6	6.4	89.6	7.0
GDP WITHOUT GAS	1,605.2	1703.1	6.1	890.5	6.7

Note: Constant price year 2000
Source: BPS

<Domestic Sale of Motorbikes and Cars>



Source: Astra International

■ 5.7% growth forecast for 2008

5.7% economic growth is forecast for 2008, slightly below the previous year's figures. According to Bank Indonesia's survey of economists during the period July to September, many were of the opinion that the economic growth rate for 2008 would be between 6.1 and 7.0%. However, given the skyrocketing price of crude oil and the increasingly pessimistic views on the future of the American economy, many have quickly retreated from optimistic views of the economic future. In late October, Bank Indonesia stated its opinion that, were the price of crude oil to continue at around $75 per barrel, then the real GDP growth rate forecast would need to be revised downwards from the intial 6.4% to 6.1%. The price of crude oil looks set to exceed Central Bank's predictions and there is a strong possibility that the economic growth rate will fail to penetrate the 6% ceiling.

According to Central Bank's consumer surveys with regard to the future of household incomes, the economy and employment, consumers are not predicting increases anything like those of 2006. On the other hand, with regard to commodity prices, given that these seem to have bottomed out in November, 2006, and are trending upwards again, consumers appear to be predicting that increases in commodity prices will blunt economic growth to some extent. Bank Indonesia had targeted an inflation rate of 5±1% in 2008, but if the price of crude oil stands at $75, then the rate will apparently rise to 6.4%. In response to the rising price of crude oil, Central Bank will have no choice but to switch to a tight monetary policy, and private consumption, which had seemed well on the way to recovery, will likely be forced into stagnation again.

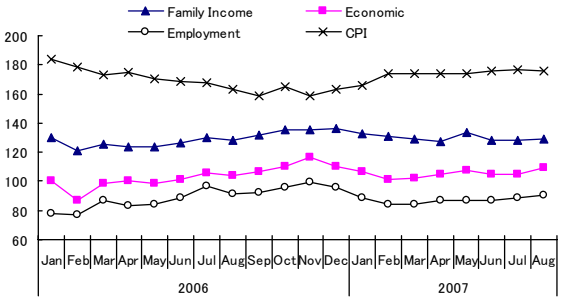
＜2008 Main Economic Indicators＞

(%,Rupiah)

	Survey Period		
	2007/Ⅰ	2007/Ⅱ	2007/Ⅲ
GDP Growth Rate	>6.0	>6.0	6.1-7.0
Inflation Rate	6.1-7.0	6.1-7.0	6.1-7.0
Exchange Rate(US$)	9,001～9,500	9,001～9,500	9,001-9,250
Unemployment Rate	10.0-11.0	10.1～11.0	10.1～11.0

Source:Bank Indonesia,*Market perception Survey*

＜Consumer Survey (Expectation for Six Months Hence)＞



Note: Indexes are calculated by balance score method (% up - % down)+100
Source: Bank Indonesia,Consumer Survey Aug 2007

＜Foreign Trade ＞

(Million US$)

		Total	Oil and Gas				Non-Oil and Gas
			Sub Total	Crude Oil	Petroleum Products	Gas	
Jan-Aug 2007	Export	64,709	14,365	5,600	1,809	6,957	50,344
	Import	40,058	12,598	5,158	7,426	14	27,460
	Balance	24,651	1,767	442	▲ 5,617	6,943	22,884
Jan-Aug 2007	Export	73,347	13,439	5,553	1,817	6,070	59,908
	Import	46,817	12,825	5,445	7,349	31	33,993
	Balance	26,530	615	108	▲ 5,532	6,038	25,916

Source: BPS

Pessimism has reared its ugly head with regard to investments also. The Business Confidence Index (when the Index exceeds 100, it indicates that the majority of companies feel that the business environment has improved on the previous period) for July to September, issued by the Statistics Bureau in August, was 111.43, its highest level since October to December, 2004. However, the Investment Coordinating Board has expressed the view at the end of October that rising costs in the wake of soaring crude oil prices will inhibit corporate investment, and expects investment growth in 2008 to be below that of 2007.

External demand is also expected to perform poorly. Exports grew 13.3% in January to July, 2007, compared to the same period in the previous year. While exports of petroleum and gas fell to minus 6.4% growth in the same period, it was exports in the non-petroleum, non-gas sectors that drove export growth, with an increase of 19.0%.

The government places great importance on fiscal discipline so that, even if the economic growth rate loses some of its impetus, there is very little risk that any fiscal and current account defecits, or foreign debt, will expand much. The assessment of Indonesia's macro-economic health and growth potential is very good, and expectations are that funds will continue to flow into the securities market. Presidential elections are slated for 2009 and, at this moment in time, there are no candidates powerful enough to offer a serious challenge to the Yudyohono administration, now seeking a second term. Therefore, there is hardly anyone at all expecting any kind of political turmoil. For the time being, the main issues would appear to be the restraining of commodity price rises and the minimizing of their impact on the poor.

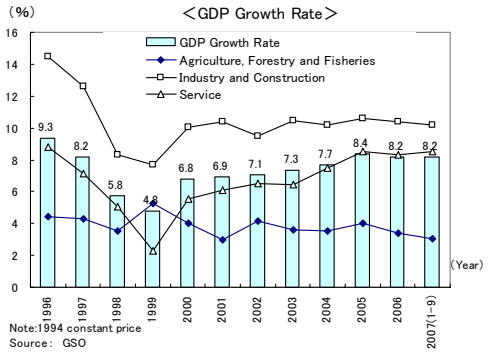
(Yuji Miura)

Vietnam *8.5% economic growth rate for 2008*

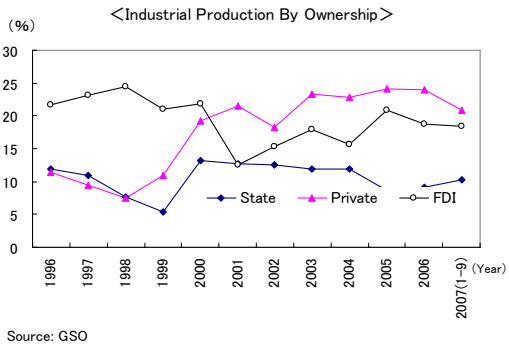
■ 8.4% growth in 2007

Vietnam's real GDP growth rate for January to September, 2007, was 8.2%, compared to the same period in the previous year. The growth rate has been rising each quarter and it is expected that the rate for 2007 will be 8.4%.

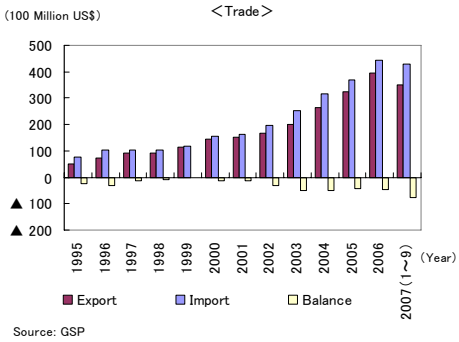
In terms of GDP supply items for the period January to September, agriculture and fisheries grew 3.0% compared to the same period in the previous year, industry and construction 10.2%, similarly, and service industries 8.5%, all sterling performances. As for industry, low production of crude oil kept mining from doing much, growing only 0.3% in the same period, but manufacturing, which accounts for 70% of the total, posted a respectable 12.5%, compared to the same period in the previous year.



Viewed sector by sector, the industrial production index showed that both private and foreign enterprises (with the exception of crude oil) performed well, with growth figures of 20.9% and 23.4%, respectively. In addition, while the state-run sector also managed to grow 10.3%, similarly, in recent years the growth gap between state-run and non state-run businesses has become more pronounced, and private and foreign enterprises now account for 74.8% of industrial production.



Domestic private sector investments and foreign direct investments are driving economic growth. In particular, the growth in foreign direct investment is outstanding. Between January and October there were 1,144 foreign direct investments (approved basis), worth $9.75 billion. This represents a 62.2% increase in the number of investment projects, compared to the same period in the previous year, and a 104.1% increase in investment worth, similarly. Both of these levels are record highs. Praised for its low labor costs, huge population and its political and economic stability, Vietnam is attracting more and more investment, not only from Japan, but also from Korea and Taiwan, as it becomes ever more important to shift away from the over-concentration of investments in China.



Exports from January to September were up 19.4%, compared to the same period in the previous year, worth $35.2 billion, while imports were up 30.3%, similarly, worth $42.9 billion. This leaves a balance of trade deficit of $7.7 billion. The government is expecting the deficit for the whole year to top $10 billion, making it the biggest ever. However, the main cause of the deficit appears to be imports of capital goods in the wake of increased foreign direct investments, and there are few in the government who see this as a significant problem.

Exports have begun to diversify since Vietnam's WTO (World Trade Organization) accession and the influx of foreign capital. In the period January to September, suffering from reduced production, crude oil exports were down 11.3% compared to the same period in the previous year, worth $5.78 billion, but textile products grew 13.1% over the same period, worth $5.81 billion, and were the biggest export item.

Also, electronics related exports grew 23.6%, similarly, worth $1.51 billion, followed by footwear (13.1%, $2.97 billion), marine produce (13.4%, $2.73 billion), and wood products (24.9%, $1.761 billion).

■ 8.5% growth forecast for 2008

The real GDP growth rate for 2008 is expected to be slightly above that for 2007 at 8.5%. In a parliamentary session at the end of October, the government set the growth target for 2008 at between 8.5 and 9.0%. Though investments are expected to be the growth driver in 2008 also, and a high growth rate is expected, it is thought that the effects of the soaring price of crude oil will keep the economic growth rate to the lower limit of the target figure.

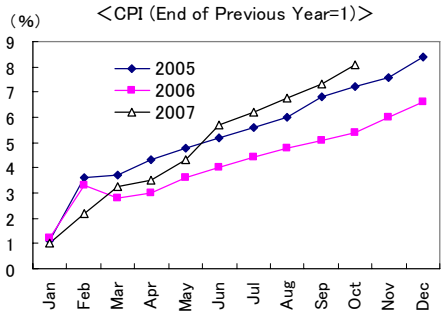
<Macro Economic Indicators>

(%)

	2007(Estimation)	2008(Target)
GDP Growth Rate	8.5	8.5-9.0
Agriculture,Forestry and Fisheries	3.5	3.5-4.0
Industry	10.6	10.6-11.0
Service	8.7	8.7-9.2
Export Growth Rate	20.5	20.0-22.0
Import Growth Rate	27.0	20.0-22.0
CPI	<8.5	<9.0
Budget Balance(% of GDP)	4.95	5.00
Poverty Ratio	14.7	11.0-12.0

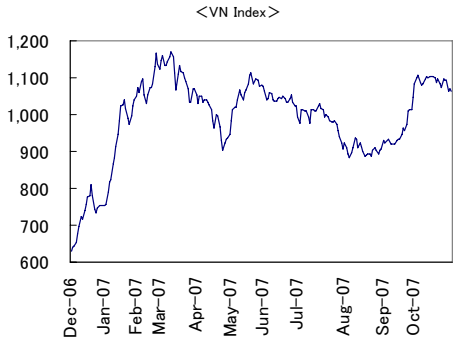
Source: Vietnam News

Reflecting rapid commodity price rises since October, there is growing concern, even within the government, over future performance. The government has stated that October commodity prices rose by 0.74% on the previous month, and that the rate of increase for January to October was 8.12% compared to the end of the previous year. It appears certain that the rate of increase will surpass 2007's target level of 8.2%. In an attempt to hold down commodity prices, the government lowered import duties on consumer goods and capital goods in August, and further cuts are scheduled. Also, the government has expressed the view that it would be difficult to pass on current rises in petroleum products to retail prices and that it intends to tighten price controls for petroleum products and to reimburse importers for losses.



Source: GSO

However, these measures will surely cause the fiscal deficit to expand so that, sooner or later, the government will need to raise the prices of petroleum products. Also, commodity prices are being pushed up not only by the rising price of crude oil, but are also greatly affected by the large amounts of capital flowing into the stock market, and it is doubtful whether the measures described above will have any real effect. The Vietnamese stock index (VN index), which was at 400 points in August, 2006, rose to 1,100 points in just six months, due to continued buying on balance by foreign investors. The aggregate market value at October, 2007, was the equivalent of 20% of GDP in 2006.



(Source)http://vietnamstock.com/vnindex.php?lang=EN

Responding to rising commodity prices, the government is due to raise the minimum wage from 2008. What the government is considering now is raising the minimum wage in foreign companies by between 13 to 15% from the current level to between $50 to $62.5 (monthly wage, may differ by region), and raising the minimum wage in local companies by 20 to 40% up to between 540 thousand dong to 620 thousand dong (as above). As increased investment brings expanded demand, there is growing pressure to raise wage levels and it is highly unlikely that they will be lowered.

The government will most likely be forced into raising interest rates and appreciating the dong in order to curb commodity prices. With regard to appreciating the dong, Central Bank is already considering expanding the exchange fluctuation range from the current 0.5% to 1%. In any case, appreciation is expected to be implemented gradually, and its impact on the economy will likely be limited.

However, raising interest rates will cool consumption and investments, and appreciating the dong will hurt competitive strength and may result in increased foreign debt. In the future, the main issues will likely be how well the government can overcome the fragility that accompanies globalization, all the while pursuing high economic growth levels.

(Yuji Miura)

India *Economic growth rate expected to be sustained at around 8.3% in fiscal 2008*

■ Outlook is for 8.6% real GDP growth rate in fiscal 2007

India's real GDP growth rate in fiscal 2006 (April, 2006, to March, 2007) was 9.4%, surpassing the 9.0% of the previous fiscal year and the highest growth level in 18 years. The growth rate in April to June, 2007, was 9.3%, compared to the same period in the previous year, making that the tenth consecutive quarter that the growth rate had exceeded 8%. In addition to a comparatively high growth of 3.8% maintained by the agricultural sector, the industry sector posted 10.6% growth, mainly from manufacturing, while the services sector also posted 10.6%, mainly from trade, hotels, transportation and communications.

The outlook for fiscal 2007 is a real GDP growth rate of around 8.6%. As regards the agricultural sector, the North and Northeast regions suffered crop damage due to flooding in July and August, but the weather is expected to continue to be fairly good in the future, and growth of around 3% is forecast for the whole year.

In the industry sector, the industrial production index for April to July grew 10.0% compared to the same period in the previous year. In manufacturing, foodstuffs, metals and machinery all performed particularly well. In terms of use, capital goods grew 19.9%, reflecting strong investment demand, but consumer durables could only manage 1.5% growth, and intermediate and consumer goods growth rates were slightly down on the same period in the previous year. However, against a backdrop of strong investment sentiment fuelled by solid corporate profits, rising capacity utilization rates, expanding bank loans, etc., corporate investment and production activities are expected to continue solidly. Also, construction is expected to continue to perform well, reflecting the effects of the real estate boom and increased infrastructure provision.

In the services sector, trade, hotels, transportation and communications are the growth drivers. The hotel and transportation industries have done well in the wake of the vitalization of economic activity, and in the period April to July, the number of aircraft passengers increased 28.2%, compared to the same period in the previous year. In communications, the number of mobile telephone subscribers as of the end of August was up 71.0% compared to the same period in the previous year, at 148.09 million persons. The finance, insurance, real estate and business services sectors also have posted high levels of growth, as bank financing continues to increase rapidly. The services sector will maintain a good pace of growth in the future.

In terms of external sectors, there is some concern over the future of exports. Exports for the period April to August were up 18.3%, compared to the same period in the previous year, while imports were up 31.2% in the same period. In rupee terms, export growth was 5.6% and import growth was 17%. The rupee's appreciation on the same period in the previous year is particularly high, even among the Asian currencies, at around 12%, and is a major factor inhibiting export growth. As the rupee is expected to stay high in the foreseeable future, the government has lowered its fiscal 2007 export growth target (dollar based) from the original 28% to 12%.

Price trends appear to have settled down. The wholesale price index rose by 6.6% in March,

<Real GDP Growth Rate>

(compared with the same quarter of last year、%)

	2005					2006					2007
		Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4	Q1
Real GDP Growth	9.0	8.4	8.0	9.3	10.0	9.4	9.6	10.2	8.7	9.1	9.3
Agriculture, etc.	6.0	4.0	4.0	8.7	6.2	2.7	2.8	2.9	1.6	3.8	3.8
Industry	9.6	10.5	7.7	9.6	10.4	10.9	10.6	11.3	10.6	11.2	10.6
Mining and Quarrying	3.6	6.1	0.1	2.7	5.2	5.1	3.7	3.9	5.5	7.1	3.2
Manufacturing	9.1	10.7	8.1	8.2	9.4	12.3	12.3	12.7	11.8	12.4	11.9
Elec., Gas & Water Supply	5.3	7.4	2.6	5.0	6.1	7.4	5.8	8.1	9.1	6.9	8.3
Construction	14.2	12.7	11.3	16.6	16.1	10.7	10.5	11.1	10.0	11.2	10.7
Services	9.8	9.2	9.3	9.5	11.1	11.0	11.7	11.8	11.0	9.9	10.6
Trade, Hotel, Trans., Commun	10.4	10.2	9.5	10.0	11.8	13.0	12.4	14.2	13.1	12.4	12.0
Finance, Insurance, Real Estat	10.9	8.9	10.6	9.8	14.2	10.6	10.8	11.1	11.2	9.3	11.0
Social, Personal Services, etc	7.7	7.5	7.9	8.3	7.2	7.8	11.3	8.3	6.7	5.7	7.6

Notice: Q1：Apr.－Jun., Q2：Jul.－Sep., Q3：Oct.－Dec., Q4：Jan.－Mar.
Source: CMIE

compared to the same period in the previous year, but the implementation of a strict monetary policy proved effective and the index gradually came down after that, reaching 3.3% in September, its lowest level in five years. It is expected that the index will settle at its current level for a while. However, there are concerns that the prices of some products, such as foodstuffs and cement, will rise because of the supply limitations in the wake of healthy economic performance, and the price of crude oil looks set to trend upwards. Therefore, attention still needs to be paid to inflation risk.

■ Real GDP growth rate of 8.3% forecast for fiscal 2008

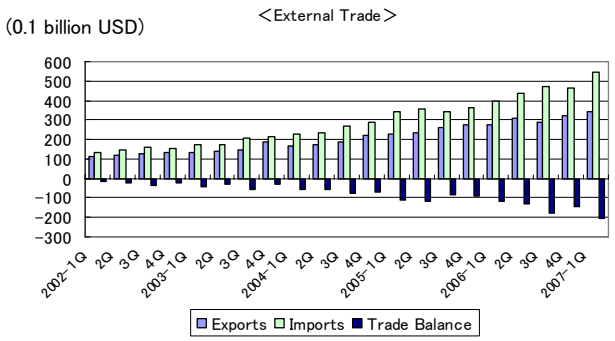
The real GDP growth rate for fiscal 2008 is expected to be on the order of 8.3%. There is a possibility that exports will continue to perform poorly, due to the effects of the rupee's appreciation, but it is believed that domestic demand will maintain its healthy pace and the industry and services sectors are expected to maintain high growth levels. The investment ratio to GDP in fiscal 2006 was 29.5%, having risen approximately six points over four years, and reflecting this, the potential rate of growth is thought to have risen quite significantly.

Meanwhile, the improvement of the agricultural sector is a major topic. Growth in that sector has been below 2% on average for the last five years, and it has been reported that the suicide rate among farm workers has reached its highest level in ten years. Approximately two thirds of the population work on the land, so agricultural reform may be said to have political significance.

The 11th Five Year Plan (fiscal 2007 to 2011) calls for average growth of 4.0% in the agricultural sector, but this will not be easy to achieve. In August, the government announced a series of measures in support of the agricultural sector, worth some $7.2 billion, particularly for public utility investments. Prime Minister Singh has declared that the fruits of economic growth are not reaching the poorest in rural areas, indicating his awareness that the agricultural sector is in a critical condition. It may be said that increased agricultural production and the steady implementation of measures to improve the quality of life of the agricultural community are essential to the long term maintenance of economic growth.

The most immediate risk factors are, first, the US economy and crude oil price developments. Should the US economy decelerate, export growth will be reduced, and strong domestic demand will sustain import growth. Therefore, the trade deficit will surely expand. The external sector does not really have that much weight, but in terms of economic growth, a certain amount of impact is inevitable.

Also, crude oil and petroleum products account for approximately 31% of India's imports, so increases in the price of crude oil may very well result in domestic inflation over the long term. However, the government has reduced customs duties and commodity taxes on crude oil and petroleum products, and has forced government-run petrol companies to keep retail prices steady, thus inhibiting the pass-through of the crude oil price rises onto domestic prices. Also, given that the rupee's appreciation is likely to continue, and that fuels account for only about 14% of the wholesale price index, the rise of crude oil will most likely only have a limited effect on domestic inflation.



Notice: Quarters are based on fiscal year.
Source: CMIE

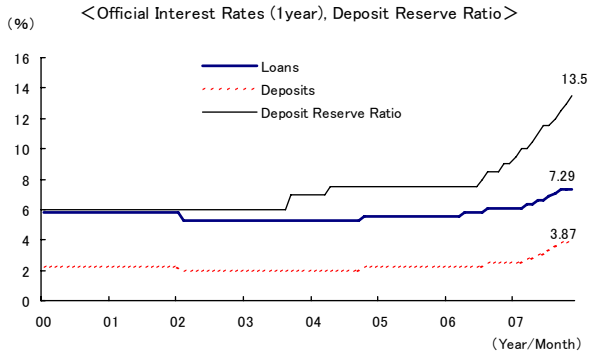
Second, there is the increase in capital inflow. This is having a variety of effects, such as causing exchange rate rises, share price volatility and increased domestic liquidity. Rupee selling intervention can encourage increased liquidity and a certain degree of exchange rate rise needs to be tolerated. Also, Central Bank raised the cash reserve ratio at the end of July by 0.5%, and finds itself with no option but to continue with this and other tight monetary policies. Measures such as tightening inflow restrictions and gradually easing restrictions on capital outflow are being implemented, but it will be important to avoid upsetting the market when implementing these measures, and the domestic financial system will need to be strengthened in conjunction with the capital account liberalization. In particular, India's current account is constantly in the red, so it must be borne in mind that there is a relatively high danger of a currency crisis happening..

(Satoshi Shimizu)

China 2008 will see economic growth sustained at around 10.4%

■ 2007 real GDP growth expected to be 11.3%, compared to previous year

In spite of a series of curbing measures implemented by the government, China's economy continued to grow at very high levels throughout 2007. Real GDP for the period July to September was 11.5%, compared to the same period in the previous year, maintaining a similar level of growth to the 11.9% posted in April to June. Towards the year end, since the penetration of tight monetary policies and the deceleration of the US economy are envisaged, China's economy is expected to cool slightly, but the GDP growth rate for the whole year is still expected to be on the order of 11.3%.



Source : The People's Bank of China

The greatest motive force behind this double digit growth is investments. Since the beginning of the year, the People's Bank of China has intensified its investment curbing measures, such as raising the deposit reserve rate ten times and the benchmark interest rate six times. Though the growth rate did show signs of gentle deceleration in the period January to March, it soon turned upwards again, and total investment in fixed assets for the period January to September grew 25.7%, compared to the same period in the previous year, and growth remained high. Part of the reason for this has been factors such as 1) expanded investments aimed at correcting regional wealth gaps and enhancing competitive strength, 2) a positive stance towards lending on the part of the banks, and 3) speculative activity in some real estate projects.

The government views these as serious matters and has adopted the stance of trying to restrain new investment projects, focusing principally on industries prone to excess production, and those that consume large amounts of energy and produce large volumes of waste pollutants. Also, there is a strong possibility that tight monetary policies will continue more strongly. Taken together, these factors suggest that investment growth in October to December may be expected to slow somewhat. Even so, total investment in fixed assets looks likely to be 24.3%, compared to the same period in the previous year, just slightly over the figures (23.9%, similarly) for 2006.

External demand also continues to contribute to high economic growth. Exports for the period January to October grew 26.5%, compared to the same period in the previous year, worth $985.8 billion, while imports grew 19.8%, similarly, worth $773.5 billion, leaving the balance of trade surplus at its highest ever level of $200 billion. In response, the government has trotted out a series of measures aimed at curbing exports, such as the levying of export duties on steel materials, reviewing the export rebates on increased direct taxation on some 2,831 items, and so on. Also, against the backdrop of a growing trade deficit with China, the US and some other nations have asked for a reform of the exchange system, and the Chinese government has given some thought to the matter. In May, the daily trading band of the exchange rate against the dollar was widened from ± 0.3% of the reference price quoted in the morning of the day in question to ± 0.5%.

Exports seemed to have reached a high in July, and have begun to slow since, and some of the curbing measures mentioned above appear to be beginning to have an effect. However, with factors such as a loss of growth in imports of parts and materials accompanying measures to curb investments and exports, and the development of domestic production, the pace of growth of imports has slowed overall. A trade surplus of $250 billion is forecast for the whole year.

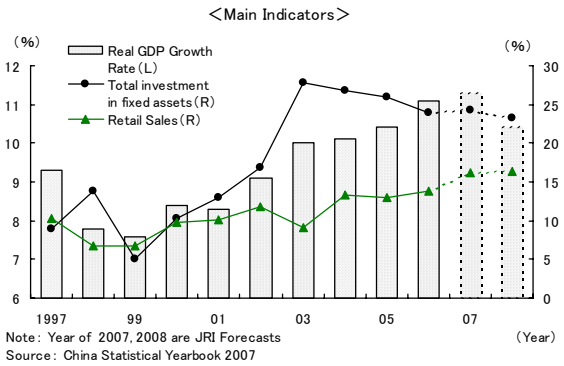
Meanwhile, consumption continues to grow. Retail sales for the period January to September were up 15.9% compared to the same period in the previous year, 2.4% points higher than the growth rate for the same period in 2006. On an annual basis, year on year growth in consumption is expected to be 16.2%, the second highest growth rate since the late 1990s, when the rate was 20.1% in the same period. In addition to improvements in the income and employment situations, such as higher minimum wages and

fairly large increases in the average wages of city workers (up 19.0% in January to September, 2007, compared to the same period in the previous year), better distribution systems in agricultural communities have brought about a solid expansion of consumption. The rising trend in share prices since the end of 2006 has also been cited as one factor that has boosted consumption among the wealthy.

Given these trends, the National Bureau of Statistics has praised consumption as having contributed very significantly to economic growth. Nevertheless, consumption growth is still at a lower level than that of investment growth, and it must be said that, in 2007 also, there was no serious change from China's investment led growth model.

■ Double digit growth expected to continue in 2008, supported by firm domestic demand

In 2008, though there are forecasts that the balance of trade surplus will shrink, it is expected that real GDP growth will be around 10.4%, continuing the double digit growth trend and supported by firm and steady expansion in domestic consumption.



In terms of demand items, consumption can be expected to continue to expand confidently. In the Political Report at the 17th Communist Party National Congress in October, 2007, General Secretary Hu Jintao outlined a policy of expanding consumption and announced plans to raise minimum wage levels and encourage regular wage increases. In the months to come, it seems that more concrete measures will be forthcoming.

If the expansion of consumption is to be sustained, it is vital that the standards of living of the agricultural communities, who account for 56% of the population, be raised. In the agricultural communities, the provision of social safety nets has lagged behind, and this is one factor inhibiting consumption. Currently, the government is putting effort into enhancing the provision of safety nets in agricultural communities as well as in the cities, and the restricting factors are gradually being alleviated. Further, the government is working on raising the wages of day laborers and resolving issues involving unpaid wages, as well as revenue improvement strategies, such as the payment of subsidies to producing farmers. As a result of this series of measures, a steady growth in consumption in agricultural communities may be expected.

The Beijing Olympic Games in August will surely be a major factor in spurring consumption growth, with increased tourism, including visitors from abroad, demand for consumer durables, the sales of related goods, etc. Taken together, retail sales for 2008 look likely to increase by around 16.3%, compared to the same period in the previous year.

As regards investments, even after the Party Congress, it was confirmed that the restraining of excessive growth was an item of major importance for economic management for the foreseeable future. Throughout 2008, it is expected that restraining measures will continue to be implemented. In particular, with regard to the development of apartment blocks and office buildings, there is a strong possibility that there will be attempts to curb investment totals through the use of measures such as further interest rate hikes and the toughening of development approval restrictions. Nevertheless, total fixed asset formation for the whole year is thought likely to grow 23.3% year on year, with only the most modest decline in the growth rate.

The grounds for this assumption are expectations of 1) infrastructure provision accompanying full scale measures to stimulate local economies and 2) continued development in fields such as plant and equipment investment from the perspective of improved competitive strength and environmental and energy saving measures. Given that it is not the economically developed coastal regions that are driving investment growth, but north eastern and interior provinces like Guilin and Anhui, it would be difficult to envisage any significant short term drop in investments aimed at correcting regional wealth gaps. The saving of natural resources, the reduction of waste pollutants and the technical advancement of local industries are all part of the state's basic policies and will, therefore, surely be exempt from investment

curbing measures.

On the other hand, it seems as if foreign demand cannot be counted on to boost economic growth to the same degree as in the previous year. The compounding of factors such as the export curbing measures that have been implemented up until now, and the deceleration of the US economy, will take much of the edge off export growth in the first half of the year. Over the latter half of the year, the US economy is expected to make a gradual recovery, and this will probably halt the deceleration of export growth. However, lacking the strength to bounce back completely, export growth for the whole year will likely be 11.8% up on the previous year, the lowest year on year growth rate since 2001 (6.8%). Additionally, since the pace of appreciation of the renminbi against the US dollar is likely to be accelerated, from the perspectives of correcting excess liquidity and easing trade friction, this is cited as another factor likely to stunt export growth.

In contrast, because the purchase of raw materials to manufacture goods for export will have restrictions applied, imports are thought likely to suffer the same loss of momentum as exports. However, since a certain degree of import growth may be envisioned, in terms of the promotion of plant and equipment imports for the purpose of enhancing industrial advancement, and the correction of trade imbalance and the expansion of consumption demand, imports for the whole year can be expected to grow 17.0%, year on year, slightly below the pace of growth in the previous year. In particular, domestic production of crude oil cannot keep pace with the rapid increase in consumption, and import volume is increasing every year. This situation is compounded by soaring international prices, so that the value of crude oil imports is expected to rise sharply in 2008, easily surpassing the growth of imports as a whole. Considering all things together, the annual trade surplus will probably contract compared to the previous year and end up at around $240 billion.

Looking forward to the economy in 2008, the following two points give cause for concern over downside risk. First, there is the domino effect of the slowdown in the US economy. This outlook presumes that American economic deceleration, triggered by the sub-prime loan issue, will gradually begin to recover from mid 2008, and that the impact on Chinese imports to the US will be very slight. The US is China's largest import partner (since 1999), but any serious shock as a result of loss of growth in exports to the US will very possibly be avoided by the growth in exports to the EU, China's second largest export partner (30.7% in January to October, 2007, compared to the same period in the previous year), as well as India (up 66.4%, similarly) and Russia (up 83.1%, similarly). However, if the deceleration of the US economy should turn out to be a protracted one, with the economies of Europe and newly emerging markets cooling also, there are concerns that the employment situation in export and other industries may suffer, and that consumption appetites will be blunted.

Second is the trend in the value of direct investment in China. The new 'Corporate Income Tax Law' will go into effect from January 1, 2008. Under the provisions of the new law, foreign firms and domestic firms will have the same tax rates applied to them, and the existing preferential treatment offered to foreign firms will gradually be cut back. Also, the government will be redoubling its efforts to improve working conditions, through measures such as the thorough implementation of the concept of 'the same pay for the same job' (correcting the income gap between regular employees and temporary employees) and encouraging wage increases. These steps may be said to be essential to the sound development of China's economy, and part of the shift to a consumption driven economic model, but any hasty implementation might easily result in a serious drop in foreign direct investment. If rising business costs end up forcing a succession of foreign businesses to pack up and leave, the positive cycle of growth through high levels of investment by foreign businesses and expanded exports will fail and the economy will not be able to avoid running out of steam.

For this second Hu administration, the tasks will be to curb the drastic increase in investments and soaring asset prices, as well as finding ways to avoid the economy overheating. Meanwhile, the government will also need to implement countermeasures to address the uncertainties and downside risks referred to above. It will be necessary to work out the most appropriate means of dealing with situations that often run counter to each other, while consolidating the foundations for long term sustainable growth.

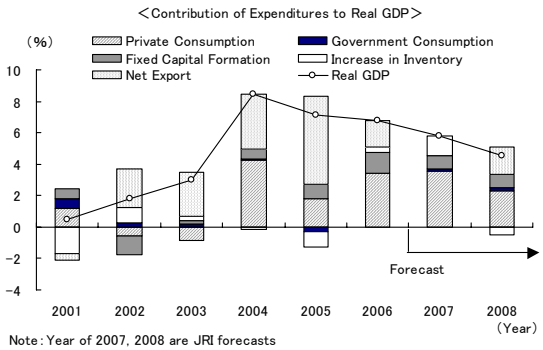
(Junya Sano)

Hong Kong 2008 growth expected to fall below 2007 at 4.6%

■ Real GDP driven by domestic demand, reaches 5.8% growth in 2007

Hong Kong's economy is performing strongly, with the real GDP growth rate for July to September, 2007, up 6.2%, compared to the same period in the previous year (up 1.7% on the previous period) and 6.6% in the period April to June (up 1.9%, similarly).

Domestic demand is the growth driver. In particular, with improved income and employment conditions, where the unemployment rate is falling and wages are rising, etc., private consumption continues to post high levels of growth at over 4%, year on year. The rise in share prices may be cited as one factor instrumental in accelerating these trends. Also, due to strong corporate appetites for business expansion, gross fixed capital formation has maintained positive growth for 11 consecutive quarters, since January to March, 2005.



Note: Year of 2007, 2008 are JRI forecasts
Source: Census and Statistics Department

As the US economy is expected to slow further through the end of the year, there would seem to be little prospect of economic growth being boosted by foreign demand. Meanwhile, domestic demand is expected to perform strongly in October to December, on the whole. All things considered, Hong Kong's real GDP growth rate for 2007 is expected to be 5.8%.

■ As consumption drivers lose momentum, economic growth in 2008 falls to around 4.6%

In 2008, the outlook is that a slowing in consumption and delay in the recovery of exports of goods will mean that the economic growth rate will fall below that of the previous year, to about 4.6%

As regards private consumption, the reduction of salary tax rates and other measures may be expected to stimulate the economy to a certain degree. On the other hand, after falling to 4.1%, the lowest level since the latter half of 1998, the most recent unemployment figures have largely stayed the same, so the driving effect of improvements in the employment environment is expected to lose momentum gradually. Further, rising commodity prices caused by the sharply rising price of crude oil look likely to weaken consumption appetites, particularly in the first half of the year. Given these factors, private consumption for the year will likely turn out to be 4.0% up on the previous year, falling below 2007's growth performance.

In terms of external demand, in addition to the slowing of the US economy, as measures designed to curb investments and exports, etc., get under way in China, Hong Kong's biggest export partner, re-exports, which account for over 90% of total exports, will probably fail to grow adequately. Since it will most probably take some time to improve from this position, the forecast is that exports of commodities and services for the whole year will peak at around 9.3%, year on year, which is a poor performance by Hong Kong standards. However, as imports of commodities for re-exports slow and growth in exports of commodities and services falls below that of exports, the contribution of external demand to the economic growth rate will probably be higher than in the previous year.

In fact, as potential downside factors, there are concerns over the growing linkage with changes in China's economic policies and fluctuations in economic performance. For example, the Hong Kong stock market began to rise more quickly after the Chinese government announced the relaxation of some restrictions on stock transactions in August. In fact, however, since reports that Premier Wen Jiabao had hinted that the implementation of this relaxation might be delayed, Hong Kong's share prices have trended weakly. As illustrated by this case, changes in Chinese policy can greatly sway the direction of Hong Kong's economy. From the standpoint of maintaining stable economic growth, the Donald Tsang administration has many compound issues to address, such as finding ways to strengthen linkages with countries and regions other than China, for example, by pushing ahead with the study of the issue of Islamic bonds, as presented in October's policy address, and so on, all the while maintaining close economic ties with China.

(Junya Sano)