ASIA MONTHLY

December 2009

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

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

Asian economic recovery in 2010 fails to pack a punch

It is expected that, while the economies of Asia will return to positive growth in 2010, encouraged by a recovery in domestic and foreign demand, economic stagnation among the industrialized nations will likely mean that an Asian economic recovery will lack real power. China looks forward to 9% growth, boosted by expanding domestic demand.

1. Asia's economic performance in 2009

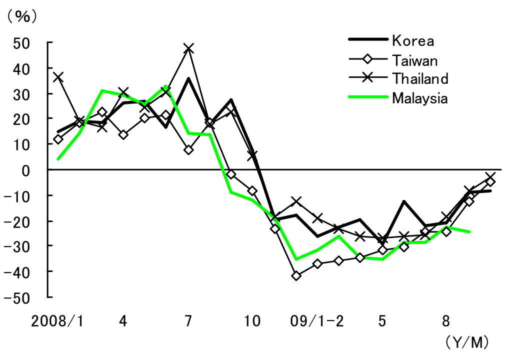
The global economic downturn caused Asia's economies to slow dramatically from the autumn of 2008, but the pace of recovery has been strengthening since mid 2009. China's economic growth in the period July to September was 8.9%, compared to the same period in the previous year, thanks to growing domestic demand.

■ From freefall to recovery

(1) Domestic demand bolstering Asia's economies

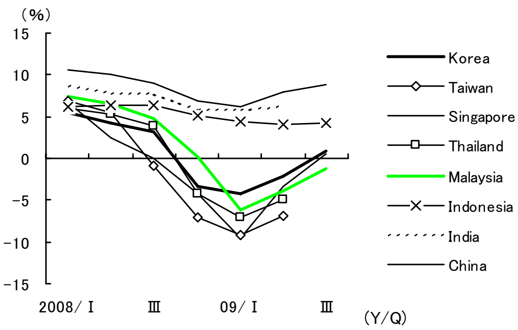
With the impact of the global economic slowdown, exports fell rapidly from the autumn of 2008. Consequently, countries with a high export dependency, such as NIEs, Malaysia and Thailand, suffered drastic economic deceleration. In the period January to March, 2009, real GDP growth rates (compared to the same period in the previous year) were minus 9.5% for Singapore, minus 9.1% for Taiwan, minus 7.8% for Hong Kong, minus 7.1% for Thailand, minus 6.2% for Malaysia, and minus 4.2% for Korea. In Taiwan, the sudden export slump caused fixed capital formation to fall significantly and pushed up the unemployment rate from 4.3% in September, 2008, to 5.8% in March, 2009. Also, the fall in primary produce prices in countries like Malaysia and Thailand caused consumption in agricultural communities to slump, and in Thailand in particular the effect of continuing political instability has caused consumption to cool even further.

<Increase Rate of Exports (YoY)>



Source: National statistics

<Real GDP Growth Rate (YoY)>



Source: National statistics

Subsequently, both domestic and foreign demand began to recover slowly and trends of economic recovery are strengthening, with Singapore and Korea managing to turn economic growth around in the period July to September, growing 0.6% and 0.9%, respectively, and Thailand and Malaysia seeing negative growth reduced.

Among the factors behind the economic recovery have been a series of policy interest rate reductions in various countries and the implementation of positive fiscal policies, such as expanded public works investments and consumption stimulus measures, measures to support agricultural communities, and enhanced and expanded safety nets, as well a rapid recovery in exports to China as a result of China's measures to promote domestic consumption, which will be touched on later.

Additionally, though Indonesia, India and China experienced some deceleration, their domestic demand has performed solidly, enabling them to avoid major economic deceleration.

India has a low export dependency (exports/ nominal GDP) and is, therefore, only slightly affected by foreign economies, so private consumption and total fixed capital formation have been able to maintain positive growth. Additionally, imports fell by a significant margin so that real GDP growth in the period

April to June was 6.1%, topping the 5.8% achieved in January to March. The development of infrastructure projects has contributed to increased total fixed capital formation. Still, India's power shortages and underdeveloped distribution infrastructure, such as harbors and roads, etc., are a real hindrance to achieving sustainable growth. For example, the lack of a highway between New Delhi and Mumbai means excessive transportation times, and the volume of freight in Mumbai has exceeded capacity, leading to containers being stacked up, waiting to be handled. To address these problems, work is going ahead on trunk route construction and the expansion of harbor capacity (particularly, container terminals), and the development of road networks linking the ports with major industrial sites.

Also, among the reasons that consumption has been growing so solidly are, in addition to lower interest rates, the effects of the government's actions in 1) implementing poverty countermeasures (exemption from financial obligations, raising the buying prices for grain produce), 2) raising the salaries of public employees, and 3) lowering the value added tax rate. In addition to these stimulus measures, car manufacturers have been investing in a series of new cars so that automobile sales have continued double digit growth since July, and this has contributed to a recovery in manufacturing production.

The links between China's economy and the global economy have become stronger and, as a result, China's economy has felt the effects of the global economic slowdown to a greater degree than ever before, with real GDP growth falling to 6.1% in January to March. In particular, exports dropped rapidly from the autumn of 2008 and the impact was felt hardest in coastal areas such as Shanghai, Zhejiang and Jiangsu, where export businesses are concentrated, and not only industrial production but also fixed asset investment decelerated noticeably. These areas have seen continuous bankruptcies and layoffs and fears have arisen that the increased unemployment among day laborers arriving from rural areas may damage social stability, prompting the government to switch its macro-economic policies from the erstwhile 'prevention of economic overheating' to 'maintaining steady and comparatively fast economic development'. In the interests of securing growth, aggressive plans have been made to expand infrastructure investment and stimulate consumption (see 'China' section for details). Measures implemented to stimulate consumption include tax reductions, gradual expansion of the eligible items and regions of the rural household appliance project, in which 13% of the purchase price of household electrical goods is paid as a subsidy, and support with the purchase of automobiles and motorbikes (applicable to purchases from March 1).

Positive measures to stimulate domestic demand have been successful, and the economy managed to pull off a rapid recovery, with the growth rate improving to 7.9% in the period April to June, and to 8.9% in July to September (up 7.7% in January to September, compared to the same period in the previous year). Domestic demand's contribution to economic growth was 8.2% in 2008 (final consumption 4.1%, total fixed capital formation 4.1%) and rose to 11.3% during January to September, 2009 (final consumption 4.0%, total capital formation 7.3%), making up for the slump in external demand (minus 3.6%).

The Huanan (Guangdong and Fujian provinces) and Huadong (Shanghai and the provinces of Jiangsu and Zhejiang) regions, which are home to concentrations of exporters, suffered major economic deceleration in the wake of the global economic slowdown, but it has been noted that, even the coastal areas of Tianjin and the province of Liaoning, as well as many provinces in the interior, have continued to post economic growth of 10% and over. A trial calculation of the contribution rates of individual regions to China's overall growth shows that that of Huanan plus Huadong fell from 36.7% in 2007 to 30.5% in 2009 (January to September), while that of the rest of the nation rose from 63.3% to 69.5%.

Amidst this shift to domestic demand-driven economic growth, the presence of the interior has increased. Moreover, this trend can be seen over the long term. Based on the intra-regional gross production values of province level administrative districts from 1979 to 2008, a calculation of the respective shares of eastern, central and western regions shows that the eastern region's share peaked in 2006 at 59.7%, then lowered to 58.4% in 2008, while the central region's share grew. This was due to the fact that fixed asset investment growth in the interior has begun to exceed that in the eastern region. The eastern region's share of fixed asset investment worth peaked in 1994 at 65.2%, falling to 53.7% in 2008, while the interior's share grew from 34.8% to 46.3%. Some of the factors behind this include the facts that 1) new investment growth in the eastern region began to peter out once investments had reached a certain level, 2) the effects of investment curbing measures designed to control investment overheating tended to make themselves felt mainly in the eastern region, 3) rising production costs in the eastern region prompted a shift of production facilities into the interior, 4) regional development initiatives in the interior have begun to get fully underway, and 5) recent economic stimulus measures have been implemented with priority on agricultural communities and the interior.

(2) Exports to China drive economic recovery in Asia

One of the characteristic features of this economic recovery process is that expanded domestic demand in China has not only supported China's economic growth, but has boosted exports from neighboring Asian countries, contributing to their economic recovery also.

As China's economy grew at a fast pace from the 1990s onward, exports from surrounding Asian nations to China increased rapidly and Asian intra-regional trade expanded as well. One factor behind this expansion in intra-regional trade was that, as manufacturers from Japan, Korea and Taiwan shifted their production facilities to China, China's role as 'the world's factory' strengthened and this led to an increase in imports from Japan and NIEs of things that could not be supplied within China, such as raw materials, parts and components, and machinery, and from ASEAN, primary products such as natural rubber and palm oil, and electronic parts and components and semiconductors. There was an international division of labor relationship wherein China took care of the final assembly step of the process and surrounding Asian nations took care of the other steps. Another factor was the growing demand for finished products within China itself. As income levels rise, China's domestic consumption market has also grown, and this too has contributed to an increase in Asian exports to China.

Thus, Asian exports to China have comprised 1) demand deriving from Chinese production of goods destined for the world's markets and 2) final demand within China itself. It is surmised that, until recently, the former played the greater role. In actual fact, Asian exports to China slowed drastically as China's industrial production and exports decelerated. Subsequently, as the Chinese government embarked upon serious efforts to stimulate consumption, China's 'role as a market' has strengthened, and Asian exports to China have increased again. Taiwan's exports to China of mainly IT related equipment, such as liquid crystal displays and semiconductors, have recovered rapidly.

China is already becoming the largest export trading partner for Korea and Taiwan and it is expected that China will become Malaysia's biggest export customer in 2009.

2. Asia's economies in 2010

■ Recovery will continue through 2010, though lacking impetus

As described above, Asia's economies have been supported by domestic and external economic measures, and the recovery trend has been strengthening from mid 2009 onward. In 2010 it is expected that Asia's economies will continue to grow, with countries continuing to implement policies prioritizing economic stimulus (though their scale will be smaller than that of 2009) and newly emerging economies experiencing steady growth in demand (with countries other than China seeing an increase in exports to China). However, as it is expected that the effects of economic stimulus measures will begin to fade and that the economies of the developed countries will continue to stagnate (assuming 0.6% economic growth for the US and 0.2% for EU), recovery overall will lack any real strength. As described below, with the exception of China (9.0%), India (7.4%) and Vietnam (6.2%), growth rates of between 2% and 5% are expected.

Among the NIEs, Korea and Taiwan are expected to achieve growth of 4.0% and 3.8%, respectively. The lack of a full recovery in exports will mean that recovery in facilities investment will be limited, and the outlook is that budget growth in 2010 will be more restrained than in the previous year, leading to a contraction in total fixed capital formation growth. In terms of consumption, a recoil from the boost gained by the tax reduction on automobile replacement purchases introduced in 2009 (due to end at the end of 2009) is expected to appear, and delays in improvements to the income and employment situations are expected to be a hindrance so that there is very high probability that consumption growth will be held to between 2% and 3%. In Korea, the rapid economic recovery meant that the unemployment rate began to fall (as of October, 3.4% after seasonal adjustment), however, 1) much new employment was of a temporary nature, 2) work sharing was introduced in order to avoid layoffs and 3) the burden (social security, tax, interest payments) on family budgets increased. All these conspired to restrain consumption. In Taiwan, the unemployment rate continues to rise, reaching 6.09% (seasonally adjusted), as of

September, 2009. Although this might be expected to fall in the weeks ahead, due to the recovery in exports, it will take some time before the rate can return to pre-crisis levels, and it may be expected that incomes, which fell significantly compared to the previous year, will not recover sufficiently.

In Hong Kong, in addition to the fact that the export recovery has been slower than that of other countries, private consumption, which had been gaining strength in recovery since mid 2009 onwards thanks to the wealth effect (positive growth in July to September, compared to the same period in the previous year), will likely decelerate again in 2010, and this and other factors will probably restrain growth to 2.1%.

In ASEAN, Thailand and Malaysia are expected to see a recovery in exports, and given that a range of economic stimulus measures, such as Thailand's "Strong Thailand" strategy (planned implementation of projects worth over Bt500 billion in 2010) and Malaysia's 60 billion ringgit investment in infrastructure development will be implemented, the forecast is for 3.2% and 3.6% growth, respectively. The Philippines is expected to achieve 3.4% growth, underscored by stable expansion in private consumption and greater fiscal expenditure. Also, in Indonesia and Vietnam, due to expectations of continued solid performance in private consumption, a recovery in investments and the continuation of economic stimulus measures, the economic forecast is for 5.3% and 6.2% growth respectively, exceeding the previous year's figures.

Expectations in India are that infrastructure related investments will continue to grow and that the implementation of fiscal stimulus measures (such as raising the salaries of public officials, debt relief for farmers, and lowering of value added tax) will continue, encouraging domestic demand to grow quickly. Also exports are predicted to grow by around 10%, compared to the previous year. Consequently, India's economic growth rate for fiscal 2010 is expected to be on the order of 7.4%. There are concerns that lower rainfall will have a severe impact crop harvests, which will in turn have a negative effect on incomes and consumption among farming communities, but it is believed that this will be balanced out to a considerable degree by the government's multi-faceted measures in support of farming communities.

While China's economic growth has accelerated recently, there are also concerns over inflation and excess liquidity in the wake of the relaxation of monetary policies. In response, it may be envisaged that the Hu administration, while attempting to sustain economic recovery, will shift its economic policy stance from 2009's prioritization of economic growth to the prevention of overheating in 2010. Among the economic measures being pursued at the moment, investment projects for 2010 will go ahead as planned and the relaxation of fiscal policies will likely be maintained. However, it is thought that, in the interests of curbing inflation expectations, it is possible that the base interest rate may be raised at least once, and that a small degree of yuan appreciation may be tolerated within foreign exchange policy. With the continued implementation of such economic stimulus measures and the continued steady increase of domestic demand, exports, principally from new emerging economies, including Asia, will exceed the previous year's levels, and the outlook is for 9.0% growth in 2010.

■ Future risk factors

In terms of risk factors in the future, first is the fact that crude oil prices are on the rise again. Recently, some Asian countries have started to try to control liquidity because of 1) rising real estate prices as a result of extended monetary relaxation and 2) emerging fears of inflation due to soaring food prices, for example. This means that, if crude oil prices increase again, there is a possibility that policy interest rates will be raised in order to curb inflationary expectations.

As the global economy continues to stagnate, it is not thought likely that crude oil prices can rise by much (Asian currency appreciation will restrict import inflation to a degree), but if crude oil prices do jump this could trigger a negative chain reaction of worsening current account balances, inflation and rising interest rates. Further, the growth of housing loans in Korea in recent years has meant that household debt has swollen and household budgets will strain under the pressure of increased interest rates.

Secondly, there are growing fiscal deficits. Due to the positive fiscal policies of 2009, many countries will not be able to avoid a worsening of their fiscal balances. In particular, India's fiscal deficit is swelling and the deficit for fiscal 2009 against GDP is expected to be on the order of minus 6.8%. Expanded fiscal deficit serves to restrain private sector demand through higher long term interest rates. While most governments will continue with policies that prioritize the economy, the need to secure fiscal soundness means that budget growth in 2010 will be restrained more than in the previous year and, depending on how the economy fares, it is possible that fiscal deficits could balloon.

Third, there is the risk of political instability. In this regard, the political situation in Thailand needs to be watched carefully. The UDD (United Front for Democracy Against Dictatorship) is still involved in anti-government activity, with three million people signing a petition in September, 2009, asking for a pardon to be granted to former Prime Minister Thaksin. In November, Thaksin was appointed as a financial adviser to the Cambodian government. Upon his arrival in Phnom Penh, the Thai government recalled its ambassador in Phnom Penh and cancelled its agreement to a bilateral maritime joint development project, straining relations with Cambodia. Also, there will be presidential elections in the Philippines in 2010. The elections are expected to go ahead smoothly but the current lack of any leading contender, and the emergence of populism, may lead to some destabilization of the political situation, and future developments need to be monitored.

(Hidehiko Mukoyama)

Economic Prospects for 2010

(year-on-year, %)

1. Economic Growth

	2006	2007	2008	2009 (forecast)	2010 (forecast)
Korea	5.1	5.0	2.2	0.3	4.0
Taiwan	4.8	5.7	0.1	−3.9	3.8
Hong Kong	7.0	6.4	2.4	−2.3	2.1
Thailand	5.1	4.9	2.5	−3.6	3.2
Malaysia	5.8	6.2	4.6	−2.7	3.6
Indonesia	5.5	6.3	6.1	4.3	5.3
Philippines	5.3	7.1	3.8	1.5	3.4
Vietnam	8.2	8.5	6.2	5.2	6.2
India	9.6	9.0	6.7	6.2	7.4
China	11.6	13.0	9.0	8.1	9.0

2. Consumer Prices

	2006	2007	2008	2009 (forecast)	2010 (forecast)
Korea	2.2	2.5	4.7	2.5	2.8
Taiwan	0.6	1.8	3.5	−0.9	1.1
Hong Kong	2.0	2.0	4.3	0.1	−0.2
Thailand	4.7	2.2	5.4	−1.2	2.5
Malaysia	3.6	2.0	5.4	0.5	2.0
Indonesia	13.1	6.4	9.8	4.5	6.5
Philippines	6.3	2.8	9.3	3.2	4.0
Vietnam	7.5	8.5	23.1	4.0	7.0
India	6.8	6.2	9.1	7.5	5.5
China	1.5	4.8	5.9	−0.9	2.6

3. Exports

	2006	2007	2008	2009 (forecast)	2010 (forecast)
Korea	14.4	14.1	14	−17	12.1
Taiwan	12.9	10.1	4	−21	15.6
Hong Kong	9.4	8.8	5	−14	2.3
Thailand	16.9	17.2	17	−16	12.5
Malaysia	14.0	10.0	13	−23	24.0
Indonesia	17.6	13.2	20	−14	8.2
Philippines	14.9	6.4	−3	−21	10.0
Vietnam	22.1	22.2	30	−10	10.0
India	22.7	29.0	5	−15	10.0
China	27.2	26.0	17	−18	13.5

4. Imports

	2006	2007	2008	2009 (forecast)	2010 (forecast)
Korea	18.4	15.3	22.0	−26.5	13.9
Taiwan	11.0	8.2	9.7	−27.3	17.4
Hong Kong	11.6	10.0	5.6	−13.0	3.4
Thailand	9.0	8.7	27.6	−26.3	15.0
Malaysia	14.4	12.4	6.3	−26.5	32.0
Indonesia	5.8	22.0	73.5	−19.8	9.2
Philippines	9.2	7.2	2.2	−22.0	14.0
Vietnam	20.4	37.0	32.2	−20.0	12.0
India	25.6	34.9	13.9	−25.0	15.0
China	19.9	20.8	18.5	−15.7	15.0

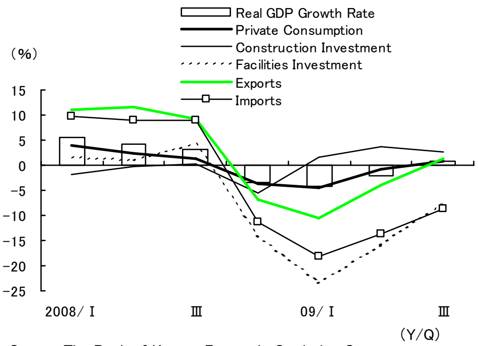
Notes: The figures in 2009, 2010 are forecasts by JRI.
Source: National statistics

Korea 4.0% growth in 2010

■ Rapid economic recovery

Korea's economy worsened significantly from the autumn of 2008, but has recovered rapidly, as shown by a real GDP growth rate (compared to the same period in the previous year) of 0.1% in the period January to March, 2009, 2.6% in April to June and 3.2% in July to September. In the third quarter, July to September, domestic and external demand were the growth drivers, with private consumption growing 1.5%, facilities investment 10.4% and exports 4.8%. In terms of comparison to the same period in the previous year, private consumption was up 0.8% and exports 1.2%, resulting in 0.9% growth.

＜Korea's Real GDP Growth Rate (YoY)＞



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

As far as reasons behind the rally in private consumption are concerned, in addition to the significant lowering of the policy interest rate, the following factors may also be considered.

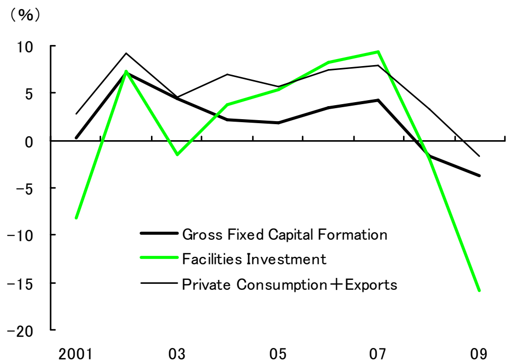
First, real GDI (Gross Domestic Income) has recovered. The soaring price of crude oil caused income terms of trade to deteriorate (incurring trading losses), which led the real GDI growth rate to fall to minus 6.2% in the period October to December, 2008. However crude oil prices subsequently fell and GDI recovered in 2009 to minus 4.4% in January to March, 0.2% in April to June and 3.6% in July to September. Second, consumption sentiment has improved. Consumer sentiment improved with the curbing of inflation and the economy bottoming out. The consumer survey index related to living trends six months hence improved from 78 in March to 111 in October. Third, the effects of economic stimulus measures need to be considered. As part of a series of economic stimulus measures, tax reductions, cost of living support measures for low income earners, and employment measures have been implemented. In terms of tax reduction measures, the income taxation rate for those earning an annual wage of 12 million won or less (taxation threshold) was lowered in 2009 from the previous 8% down to 6%. Also, from May 1, a 70% tax reduction was introduced on the purchase of replacement purchase cars (new registrations replacing cars bought before the end of 1999). As a result, automobile sales have been growing at a double digit pace since May, with the consumption recovery driving economic performance.

Also, exports (customs cleared basis) declined rapidly from October, 2008, in the wake of the global economic deceleration, but began to recover gradually from early 2009. Export growth in September was minus 9.0%, compared to the same period in the previous year, and 8.5% in October, with the pace slowing to single digit deceleration. Improved price competitiveness due to the weaker won, and increased exports to China (Korea's biggest export customer) have contributed to the rapid recovery in exports. Exports had been growing at a slower overall place from the latter half of 2008, but with China's rural household appliance project getting fully underway, production of televisions and PCs has been ramped up and exports from Korea of liquid crystal displays and semiconductors are increasing.

Along with this recovery in domestic and external demand, the manufacturers' production index (seasonally adjusted) in September recovered to higher than pre-crisis levels, and the unemployment rate (seasonally adjusted) fell to 3.4% in October. The unemployment situation has begun to improve, with the number of those at work increasing for two consecutive months in September and October, compared to the same periods in the previous year. Also, against the backdrop of an improved balance of current account and the economic recovery, the won - dollar exchange rate as of November 16, was moving in the $1 to upper 1,100 won range.

As part of a series of economic stimulus measures, the implementation of the budget for this fiscal year (January to December) is being brought forward, so the boost effect from government expenditure in October to December will peter out, but the recovery trend in domestic and external demand has been strengthening of late, so growth for 2009 is expected to be on the order of 0.3%.

■ **Poor growth in domestic/ external demand will hold growth to 4.0% in 2010**



Note: The figure of 2009 is up to the third quarter.
Source: The Bank of Korea、*Economic Statistics System*

In 2010, as explained below, it is forecast that economic stagnation among the industrialized economies and the slowing of the effects of economic stimulus measures will cause domestic and external demand to fail to grow and this, in turn, will restrain economic growth to 4.0%.

First, exports will surely achieve positive year on year growth, driven by exports to the newly emerging economies, but 1) economic stagnation among the developed economies and the failure of the employment environment to improve, 2) the decline of the effect of consumption stimulus measures in other countries, and 3) the correction of the won's 'excessive' depreciation, will all very probably cause growth throughout the year to be very modest. Due to the very high possibility that there will be further correction (assuming an annual average of $1 to 1,100 won) of the won's depreciation in the near future, there can be little hope of any cheap won effect (increased export volume and increased won conversion sales).

Though private consumption continues to recover, growth for the whole year will likely be no more than around 3%. One reason for this is the appearance of the recoil from the effect of consumption stimulus measures implemented in 2009. In particular, automobile sales were boosted by the tax reduction on new automobile replacement purchases, but this reduction is due to finish at the end of 2009, and the impact of this will be unavoidable in 2010. Another reason is the continuing tough pressure on household budgets. According to employment statistics, the increase in the numbers of those at work is seen in social overhead capital and other service sectors, but many of these new jobs are temporary. In addition, given 1) the implementation of work sharing in order to avoid layoffs, 2) the time limits imposed upon cost of living support measures for those in low income jobs, and 3) the possibility that rising crude oil prices will once again cause income trading terms to deteriorate, the aforementioned recovery in income growth may very well lose impetus over time.

While incomes fail to grow satisfactorily on the one hand, the burden of 'non-consumption expenditure', such as social security payments, taxes and interest payments, is increasing year by year, and this will surely hinder consumption growth . In recent times in particular, it should be noted that, against the backdrop of a lengthy spell of low interest rates, housing loans have increased, with the result that household debt has burgeoned.

That other pillar of domestic demand, total fixed capital formation, will also likely grow by only the most modest of margins. Over the past few years, total fixed capital formation growth has been well below that of final demand. This has been part of the reason for President Lee Myung-bak's attempts to vitalize the economy through the expansion of investments.

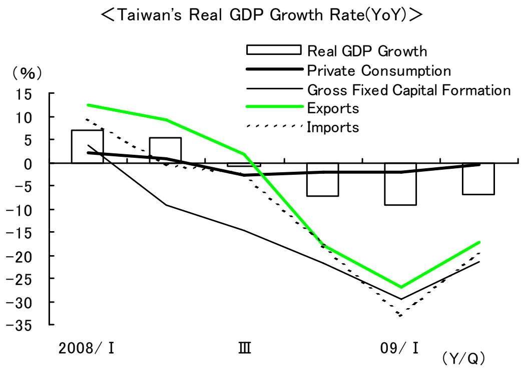
Based on improved corporate performance figures and the recent trend of increased machine orders received, though facilities investment will likely exceed the previous year's levels, the lack of strength in private sector demand recovery and uncertainty over the future will likely mean that the recovery will not be full-scale. Also, it is expected that growth in the 2010 budget will be restrained even more than in the previous year (the budget proposal calls for a 0.3% increase in the budget allocation for public works projects, compared to the initial budget of the previous fiscal year), so that construction investment will be more or less at the same level as the previous year and the forecast is that total fixed capital formation overall will grow by only just under 4%.

Bank of Korea is watching commodity prices and real estate prices very closely and, because these are being restrained at the moment, the Bank is set to keep interest rates low. The Lee administration, besides making sure that the economic recovery is a substantial one, will need to exert some effort on tackling mid term issues, such as the vitalization of investments and the creation of a stable employment environment. The Green New Deal projects and efforts to stimulate service industries (medicine, education, distribution, contents) have been made clear, and 2010 is the year when the results will be expected.

(Hidehiko Mukoyama)

Taiwan 3.8% growth in 2010

■ Economic recovery picks up pace from mid 2009



Source: Directorate General of Budget, Accounting and Statistics

Taiwan's domestic demand began to decelerate from early in 2008. In addition, there was a sharp drop in exports from autumn onwards which caused the economic situation to worsen, so that real GDP growth for the first quarter, January to March, 2009, fell to minus 9.1%, compared to the same period in the previous year, the lowest growth rate in Asia. This was due to minus 2.0% growth in private consumption, on top of major slumps in total fixed capital formation (minus 29.4%) and exports (minus 26.9%). Private consumption growth had been very poor in recent years, owing to the introduction of measures to curb consumer credit, taken in response to the credit card debt problem. Then the compound effects of 1) worsening trade terms and the contraction in real wages in the wake of economic deceleration and 2) a sharply rising unemployment rate (up from 4.3% in September, 2008, to 5.8% in March, 2009) caused private consumption to cool further.

Subsequently, domestic and external demand began to rally and real GDP growth in the second quarter, April to June, improved slightly to minus 6.9%. Also, the rates of decline of total fixed capital formation, exports and private consumption contracted, posting minus 21.4%, minus 17.2%, and minus 0.6%, respectively.

In recent months, the recovery trend in consumption has been continuing, with real retail sales figures up 4.5%, compared to the same period in the previous year, in September, and 5.9%, similarly, in October. The main reason behind this is the increase in automobile sales. Thanks to the introduction of a special measure (promulgated January 17) wherein purchases made with in the year of cars of less than 2,000cc displacement received a NT$30,000 commodities tax exemption, and the halving of the import tariff rate on some automobile parts and components (23 items) from May 25, automobile sales have been growing at a double digit pace since June.

Also, the recovery trend in exports (customs cleared basis) has been gaining in strength since the middle of the year, with minus 12.7%, compared to the same period in the previous year, in September improving to minus 4.7%, similarly, in October. Exports to China were up 2.1% in September and 9.8% in October, two consecutive months of year on year positive growth, and the rate of decline in exports to the US contracted significantly to minus 16.5%, due to the Windows 7 effect. Import value had continued to decline at a rate of over 20% from December, 2008, to September, but stood at minus 6.7% in October. Capital goods grew by 12.3%, suggesting a recovery in facilities investment in the period October to December.

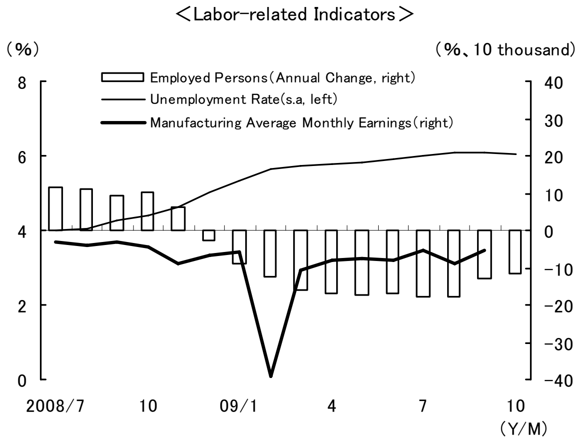
Along with this rally by domestic and external demand, manufacturers' production has continued to improve, posting positive year on year growth in September. Semiconductor foundry giant TSMC's sales for October were higher than the previous year's levels. In addition, there are signs that the employment environment is improving: the unemployment rate (seasonally adjusted) improved from 6.09% in September down to 6.04% in October, and the decline in the number of those at work contracted in September.

As private sector demand falls, it is hoped that social capital development related investment (the 'i-Taiwan 12 Projects' plan includes the development and improvement of island-wide transit and information networks, reinforced logistics functionality at Kaohsiung International Airport and other airports and sea ports, as well as construction to link existing science parks and the construction of new industrial areas) will play a role in supporting the economy, but their effect in boosting the economy will likely be limited to around 0.5%

Reflecting the impact of the slump of the first part of the year, the real GDP growth rate for the whole year is forecast to be on the order of minus 2.6%.

■ Export increase lacking in strength, 3.8% growth in 2010

Economic growth in 2010, supported by the recovery in domestic and external demand, is forecast to be on the order of 3.8%.



Source: Department of Statistics, Ministry of Economic Affairs

Firstly, in terms of export performance, the export recovery from the early spring of 2009 onwards has been contributed to by 1) China's rural household appliance project, 2) the stable growth of demand in the newly emerging economies, 3) rallying economies among the industrialized nations, 4) the Windows 7 effect, and 5) rises in the prices of semiconductors and liquid crystal displays. Through 2010 also, these plus factors are expected to continue to have effect, but the effect of consumption stimulus measures in China and the Windows 7 effect will gradually weaken, and the continuing stagnation among the economies of the industrialized nations will hinder consumption growth so that exports for 2010 (customs cleared basis) are likely to grow by no more than around 10%. Bearing in mind the scale of the slump suffered in 2009, this can scarcely be called a high level of growth.

Private consumption is likely to continue to recover but, for the following reasons, it is expected that growth over the whole year will be no more than 2% at best. One reason is that figures for 2009 were boosted considerably by the impact of automobile sales promotion measures, and the recoil from that will make itself felt. Another is that the employment and income environment has been slow to improve. Along with export recovery, the unemployment rate will fall in the future also but, as explained above, this export recovery has not yet become a full scale recovery and the probability is high that it will do no more than contract the rate of decline by 1% point. Also, even though manufacturers' average monthly revenues, which were well down on the previous year in 2009, may be expected to rise in 2010, it will surely be a small rise. The delay in real improvement in the income and employment environment is thought likely to curb consumption growth.

Any growth in total fixed capital formation is also thought likely to be of a small margin. As regards trends in total fixed capital formation (divided broadly into private and public sectors, with the private sector accounting for around 70%) over the last ten years, it can be seen that there is a strong synchronicity between exports and total fixed capital formation and, with the exception of 2004 and its series of large scale investments, from 2000 onward, even if exports grow by around 10%, total fixed capital formation will grow by no more than around 2% (between 3 and 6% in the private sector). In 2010, encouraged by 1) the recovery in export growth, 2) expected investments related to the 'i-Taiwan 12 Projects' plan, 3) continuing low interest rates, and 4) expectations of increased investments from China (on June 30, 2009, restrictions on Chinese firms making direct investment in Taiwan were lifted), the previous years will probably be exceeded, but as long as the export recovery is not a full one, major industries such as semiconductors and liquid crystal displays also are increasing their production shifts to China, so any growth in total fixed capital formation is forecast to be around 3%.

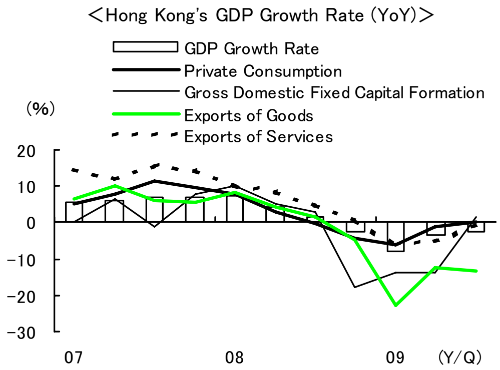
Thus, based on a gradual recovery in domestic and external demand, the economy is forecast to grow by 3.8% in 2010. Since the inauguration of his administration, President Ma has promoted the i-Taiwan 12 Projects and the development of industry, from the standpoint of the vitalization of the economy, and at the same time has worked to strengthen economic ties with China, by realizing the 'Three Linkages', relaxing restrictions on Taiwanese firms' investment in China and rescinding restrictions on Chinese firms investing in Taiwan. In future, there are plans to begin an ECFA (Economic Cooperation Framework Agreement) with China, but the opposition Democratic Progressive Party and some in industrial circles are still opposed to the idea, citing worries over China's growing influence. The Ma administration's approval rate is already low, and attention should be paid to the fact that any deepening of the row between the ruling and opposition parties runs the risk of destabilizing the political situation.

(Hidehiko Mukoyama)

Hong Kong 2% range growth in 2010

■ Economic recovery led by domestic demand

Hong Kong's real GDP growth rate for July to September, 2009, was minus 2.4%, compared to the same period in the previous year, with the rate of decline showing a slight contraction from the minus 3.6% recorded in April to June (+0.4%, compared to the previous period). Thanks to the rally shown by domestic demand, Hong Kong's economy, which had suffered badly, has been able to maintain its recovery trend.



Source: Census and Statistics Department of Hong Kong

External demand stayed at low levels, due mainly to stagnating economies in the US and Europe. Exports of goods for the period July to September were at minus 13.2%, compared to the same period in the previous year, a slight contraction from minus 12.4% for April to June, similarly (minus 2.8% compared to the previous period). In terms of specific regions, exports to China, which account for 50% of the total, were minus 8.0%, compared to the same period in the previous year, deteriorating from minus 5.4% posted for the period April to June. A major reason is felt to be that China's process trade is struggling, due to economic stagnation in Europe and the US. Exports to China can be divided roughly into two types, those for China's domestic demand and those for process trade. In process trade parts and components and raw materials are at first imported from Japan and ASEAN, for example, then assembled into products in China and exported to Europe and the US. Process trade exports account for over half of the total, so economic stagnation in Europe and the US has affected not only Hong Kong's exports to those countries and regions, but has also had a serious negative impact on Hong Kong's exports to China. Exports to the US, which account for 10% of the total export value, were minus 24.3% in the same period and are still falling. Service exports in the third quarter, July to September, rallied to minus 0.9%, compared to the same period in the previous year, from minus 5.2% in the second quarter, April to June (+4.6% compared to the previous period).

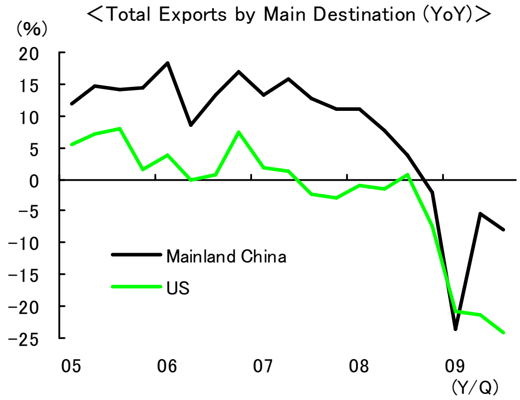
Meanwhile, domestic demand, household, corporate and government, were all up compared to the previous period. Private consumption expenditure is sensitive to the impact of share prices and housing prices, and converted from minus 1.1% negative growth in the period April to June to +0.2% in July to September (+0.5% compared to the previous period). Real retail sales in the same period were minus 1.9%, similarly, with the rate of decline contracting from the minus 5.4% posted in April to June. Among the reasons behind the rally in consumption, the first is that consumer sentiment has been encouraged by rising asset prices, against the backdrop of capital inflow from abroad. Hong Kong's Hang Seng Index and housing prices, both of which plummeted from the autumn of 2008, have made steep gains of 45.6% and 22.8%, respectively. It is estimated that housing prices would be about 30% lower than recent levels, if not for capital inflow. The second reason is that there have been improvements in the employment situation in some industries with high income levels, such as finance. Gross domestic fixed capital formation for the period July to September was 1.4%, compared to the same period in the previous year, topping the previous year's level (April to June's figure was minus 13.6%, similarly). In addition to public sector investment, private sector investment is also beginning to pick up, encouraged by the economy's bottoming out and government support measures, such as credit assurance.

Deterioration in the employment situation appears to have stopped, thanks to signs of economic recovery and government support measures. The rate of totally unemployed for July to September was 5.3%, a 0.1% point improvement on April to June. In terms of specific industries, transportation and communications, finance, construction, and manufacturing have improved. Thus, while the economy may be seen to be on the road to recovery in recent months, the effects of the economic recession through the first half of 2009 will make themselves felt. The forecast is for minus 2.3% growth for the whole year in 2009.

■ External demand recovery delayed in 2010 and domestic demand will fail to grow

For Hong Kong, goods exports are 1.7 times the size of GDP, and trade related services, such as transportation and intermediary trade, account for 25% of GDP and over 20% of gross fixed asset investment. The number of people employed in trade related industries is the largest in Hong Kong and accounts for 30% of the total, and its added value also accounts for 30% of all industries, and is on a par with finance. Therefore, a rally in trade is the key to economic recovery.

＜Total Exports by Main Destination (YoY)＞

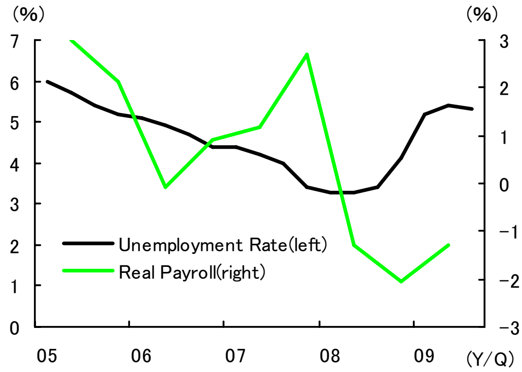


Source: Census and Statistics Department of Hong Kong

The outlook for 2010 is that external demand will be slow to recover, due to economic stagnation in Europe and the US. In terms of the export of goods, while there will likely be an increase in exports due to China's domestic demand, the scale will be minor and its effect in boosting the economy overall will be limited. Given the expectation that the European and US economies will continue to stagnate, there can be little hope of a rapid recovery in exports to China and for process trade. The possibility is high that exports to Europe and the US will stay at a low level. Thus, exports of goods are likely to be around 90% of 2008's levels, while some benefit may be expected from the effect of China's economic recovery.

The pace of recovery in the exports of services also is believed to be fairly slow, due to the stagnation in trade related services. Services exports are big in Hong Kong, accounting for 43% of GDP. It is expected that the travel industry will recover comparatively quickly, due to increased numbers of visitors from mainland China. But because the travel industry is much smaller than trade related industry, accounting for just 7% against GDP, it will not be enough to make up for the poor performance by trade related services. A partial lifting of the ban on using the yuan for trade settlement means that other services (including finance) can expect some positive benefit, but as there is little possibility of capital transactions in mainland China being liberalized, a major expansion cannot be expected.

＜Unemployment Rate and Real Payroll＞



Note: Unemployment Rate is on a seasonally adjusted basis. Real Payroll is on % changes from the previous quarter basis.
Source: Census and Statistics Department of Hong Kong

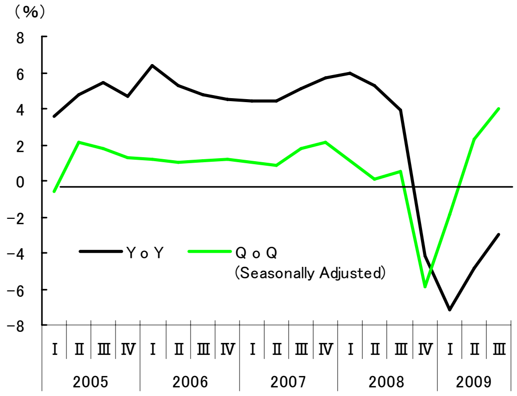
Also, domestic demand is not expected to grow strongly. Since there is little expectation of major wide ranging improvements in the employment situation or in salary levels, the weakening of the assets effect means that there is a high probability that individual consumption, which accounts for 60% of GDP, will decelerate. Adjustments in asset prices are predicted for the following three reasons. First, due to the change in China's financial policies, there is a strong possibility that the brakes will be applied to any sudden increase in capital inflow. Second, growing concerns, both within Hong Kong and externally, over a possible bubble mean that investments in stocks and real estate will likely be done very cautiously. Third, Hong Kong's government has showed its stance to repress jumping real estate prices.

Gross domestic fixed capital formation is expected to stay at more or less the same level. Private sector investments will probably stay at roughly the same levels as the previous year, due to corporate profit failure to improve and the fading of the effects of economic stimulus measures. It is thought that trade related industries will continue to face tough times ahead, due to the downturn in trade. While public sector investments will increase, the scale will be small, accounting for only 2% of GDP, and its impact on the economy overall will be limited.

Thus, the forecast is that Hong Kong's economy in 2010 will post low growth, at 2.1%. The possibility is strong that the unemployment rate also will be above 5.0%. **(Seki Shinichi)**

Thailand 3.2% economic growth in 2010

■ 2009 growth falls to minus 3.6% thanks to slump in domestic and foreign demand



Source: NESDB

Thailand's real GDP growth in 2009 suffered the effects of decreased exports and continuing political instability and fell to minus 7.1% in Q1, January to March, compared to the same period in the previous year, minus 4.9%, similarly, in Q2, April to June, and minus 2.8%, similarly, in Q3, July to September. However, the rate of decline contracted gradually through each quarter, and seasonally adjusted figures from Q2 onwards were positive compared to each previous quarter. Further, though Q4, October to December is expected to post positive growth, compared to the same period in the previous year, the negative slump in the first half of the year has been quite significant and growth for the whole year is expected to do no better than minus 3.6%, year on year.

In terms of exports, the period January to September saw a massive deceleration, minus 11.0%, $109.3 billion, compared to the same period in the previous year. The deceleration was particularly noticeable in automobile related products and computer related products, and amidst tough production adjustments, the unemployment rate topped 2% for the first time in two years. Though exports began to trend toward recovery in the second half of the year, growth for the whole year is expected to be minus 16.0%, worth $149.4 billion. Meanwhile, imports are expected to return minus 26.3% growth, worth $131.7 billion, due to poor domestic demand and falling crude oil prices, so that a balance of trade surplus of $17.7 billion is forecast. The rapid decline in exports caused the manufacturers' capacity utilization rates to fall to 58.1% for Q1. In addition, growing political instability meant that private sector companies were hesitant about investments, and fixed capital investment was minus 15.9% in Q1, minus 10.2% in Q2 and minus 6.3% in Q3. The outlook for the whole year is minus 8.6%, year on year. Private consumption also fared poorly, with exports declining and against a backdrop of employment unease and political instability, and posted minus 2.5% in Q1, minus 2.3% in Q2 and minus 1.3% in Q3. More particularly, the durable consumer goods market contracted and automobile sales for January to September were minus 20.3%, compared to the same period in the previous year, at 370,000 automobiles, and sales look set to fall below the previous year's figures for the fourth year running.

■ Economic recovery trend will strengthen in 2010, but political instability is a downturn risk

In 2010, it is expected that Thailand's economy will turn around to 3.2% positive growth, against a backdrop of increased exports in the wake of a global economic upturn and the full implementation of the Thai Khem Khaeng (Strong Thailand Strategy), which has a total investment worth of Bt1.431 trillion.

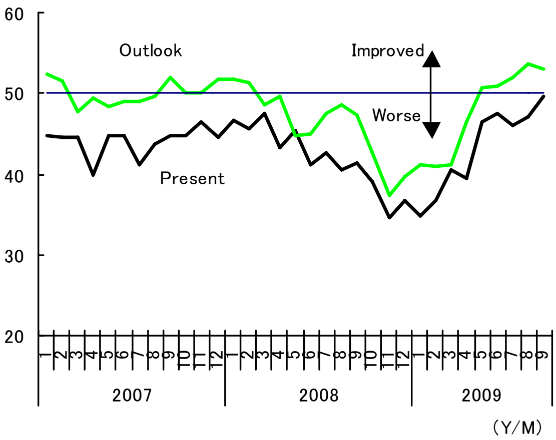
In the case of exports, those destined for Japan, Europe and the US will continue to languish, but those bound for China, the Middle East and Australia, will be the drivers of growth. In 2009, the majority of exports returned large year on year negative growth, but exports to China grew 1.2%, compared to the same period in the previous year, in August and 4.5% in September, two consecutive months of positive growth. Exports to China cover a wide and diverse range, - industrial products, raw materials, foodstuffs,- and are expected to play a driving role in export growth in 2010, performing at 20% or more, year on year.

Industry by industry, it is supposed that the recovery in electronic products and electrical machinery will be quick, with HDD (hard disk drive) production levels expected to reach their highest ever levels, and September production indices were 10.3% up on the same month in the previous year. In addition, there is good news ahead in that the recovery trend in transportation equipment, including automobiles, is picking up the pace.

In 2010, tariffs will be abolished within ASEAN and between ASEAN and China. In addition, an ASEAN - India FTA and an ASEAN - Australia - New Zealand FTA will come into effect. These and other major changes in Thailand's trading environment will probably also boost an increase in exports. However, a full export recovery will require economic recovery in Japan, Europe and the US, and performance for the whole year is looking to be between 10 to 15% growth, year on year.

This recovery in export performance has led to great improvements in manufacturers' business confidence. According to the business confidence survey issued by Bank of Thailand, those respondents who answered that conditions were 'getting better' from May onwards exceeded those who answered 'getting worse', and in recent weeks the number of those companies responding 'getting better' has been increasing. Further, the Stock Exchange of Thailand Index (SET Index) has risen from 450 points in early 2009 to 700 points in September, and a business confidence survey and consumer confidence survey conducted by the University of the Thai Chamber of Commerce have both indicated five consecutive months of month on month improvement. The private consumption index, which has been posting minus year on year growth every month since the start of 2009, is expected to return positive growth figures by the end of the year and, given that this trend will continue into 2010, the forecast for private sector investment is 1.8%, year on year. As regards of fixed capital formation, plant and equipment capacity utilization rates are still low so, though a recovery in private sector investment may take some time, public works investments in the form of the Bt1.431 trillion 'Strong Thailand' strategic plan will be the growth driver. The plan started in September of 2009 and some Bt500 billion of projects are slated to get underway in 2010. Fixed capital formation is reckoned to be on the order of 2.4% for the whole year.

＜Business Sentiment Index in Manufacturing＞



Source: Bank of Thailand

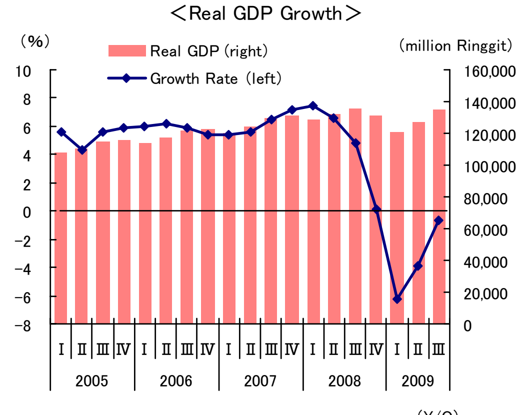
As described, while some economic recovery may be expected in 2010, it needs to be remembered that political instability continues. In April, 2009, anti-government activity on the part of the UDD (United Front for Democracy Against Dictatorship) led to the postponement of the ASEAN leaders' summit, and the anti-government activity continues. In September, three million people signed a petition calling for a pardon for former Prime Minister Thaksin. In November, Thaksin was appointed as a financial adviser to the Cambodian government. Upon his arrival in Phnom Penh, the Thai government recalled its ambassador in Phnom Penh and cancelled its agreement to a bilateral maritime joint development project, straining relations with Cambodia.

Again, in terms of new economic downturn risk, an October ruling of the Central Administrative Court granted an injunction halting 76 projects of construction and other work (worth a total of Bt400 billion) on the Eastern Industrial Estate Project (Rayong province), which had already received government approval. The action was grounded on the fact that the provisions of the new constitution had not been followed, but there has been considerable anger among businesses that a project approved by the government has been stopped. There is some concern as to how Thailand's position as an investment recipient country will be affected by how the government handles this issue. In addition, attention needs to be paid to the fact that, after the October rise in fuel prices, the consumer price index increase rate showed a positive increase compared to the same month in the previous year. In consideration of the fact that earlier rises in commodity prices have been linked to increased anti-government activity, it would appear that the government needs to respond quickly to the situation. If political uncertainty and new downturn risk factors become more serious, the possibility is that economic growth will be constrained to the 2% range.

(Keiichiro Oizumi)

Malaysia 3.6% economic growth in 2010

■ Minus 2.7% growth in 2009



Source: Bank Negara Malaysia

Malaysia's real GDP growth in 2009 was minus 6.2% in Q1, January to March, minus 3.9% in Q2, April to June and minus 1.2% in Q3, July to September, reflecting the adverse impact of the global economic slowdown. Though the pace of recovery has strengthened in the latter half of the year, the forecast for the whole year is minus 2.7% growth.

More particularly, the sudden decline in exports hastened Malaysia's economic slowdown. Export growth in the period January to September was minus 29.3%, worth $110.9. The main factors behind this sudden drop in exports were the minus 25.5%, $49 billion, suffered by electronics and electrical goods, which make up 40% of the total, and the massive drops suffered by palm oil and related products and crude oil as a result of falling prices, minus 33.6%, $10.4 billion, and minus 55.5%, $4.7 billion, respectively. Imports, meanwhile, suffered the effects of dwindling domestic demand and severe inventory adjustment and posted minus 29.6% growth, $86.8 billion, leaving a balance of trade surplus of $24 billion. Though exports are expected to strengthen in recovery over the end of the year, performance for the whole year is expected to be on the order of minus 23.0%, $181.2 billion.

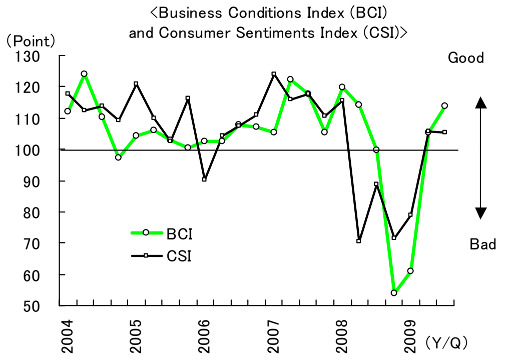
Malaysia's export dependence (ratio of exports against GDP) is over 100% and the export slump has had a serious effect on the manufacturing industry. The manufacturers' production index has continued to fall, year on year, every month since September, 2008, reaching minus 7.9% in September. Under these circumstances, investors have been hesitant about making new or expanded investments, and the number of investment applications approved by Malaysia's Industrial Development Agency (MIDA) in the period January to June was minus 59.9%, compared to the same period in the previous year, worth 15.8 billion ringgit ($4.5 billion), and the total for foreign investment in the balance of payments was minus 83.5%, similarly, worth $100 million. As a result, fixed capital formation was down to minus 10.8% in Q1, minus 9.8% in Q2 and minus 7.9% in Q3. The forecast for fixed capital formation for the whole year is minus 20%, compared to the previous year.

On the other hand, thanks to the government's prompt implementation early in the year of economic stimulus measures worth some 7 billion ringgit (approx. $2 billion), private consumption has been able to prop up the economy. Though private consumption started off the year at minus 0.7% in Q1, it switched to positive growth, posting 0.5% in Q2 and 1.5% in Q3, due to the effect of measures to reduce the amount of social security savings, as part of economic stimulus measures. While a full recovery in private consumption will need to wait until 2010, the expectation is that the performance for the whole year will be a 1.6% increase compared to the previous year.

■ 3.6% growth in 2010

In the wake of the recovery trend in the latter half of 2009, economic growth is expected to reach 3.6% in 2010.

Exports are not expected to make a full recovery, since Malaysia's main export customers, Japan, Europe and the US are still in economic slowdown, but there is some good news in that Malaysia's main export items, electronic and electrical goods, are improving. Exports of electronic and electrical goods were minus 18.5% in July to September, compared to the same period in the previous year, but this was a 15.2% increase on the previous period and exports are expected to increase along with sales of Windows 7. In addition, while exports of crude oil and agricultural produce were down in 2009, forecasts are that there will be increased demand and higher prices and that these exports will grow by 24%, year on year, in 2010. However, 2009's slump was so big that export value in 2010 will be around $181.2 billion, just 9% of 2008's level.



Source: MIER

Thanks to the government's prompt implementation of economic stimulus measures, business confidence improved greatly in Q2. The consumer confidence index put together by the Malaysia Institute of Economic Research (MIER) improved from 78.9 points in Q1 to 105.8 points in Q2 and 105.4 points in Q3. The outlook for private consumption in 2010 is 3.8% growth, compared to the previous year, boosted by improvements in the employment situation and increased disposable household incomes, as well as rising asset value due to stable commodity prices and rising share prices.

With regard to fixed capital formation, the improvement in export performance has led to higher capacity utilization ratios among manufacturers, but as the economic recovery is still weak among Malaysia's main export customers, Japan, Europe and the US, investments in Malaysia from these countries cannot be expected to grow very much and, for this reason, private sector investment will likely only grow 3% on the previous year. In this respect, the government is planning to implement foreign investment attraction policies based on the deregulation of its Bumiputra stance (providing for preferential treatment for indigenous Malays). Already, as a first step, in May the government introduced wide ranging relaxations of restrictions on investment ratios in 27 service industries. Furthermore, since there is little prospect of a recovery in investments from major investing nations such as Japan, Europe and the US, the government is studying policies to attract investment from China, India and the Middle East.

Since its inauguration in April, 2009, the Najib administration has not only moved quickly to implement bold policy changes, but at the same time has made the objectives of its policies clear, as well as the result that it expects, and this has won the administration the approval of the people. The Abdullah administration's rapid loss of cohesive force from mid 2008 onwards led to a temporary heightening of political turmoil, but the Najib administration's approval rating is high and this will likely be a positive factor in economic recovery in 2010.

The Najib administration is due to implement economic stimulus polices worth 60 billion ringgit, including infrastructure provisions, and plans to fund the initiative from domestic and foreign private sectors. Plans call for funds for the development of the Iskandar Special Economic Zone to be borrowed from Middle Eastern countries, and for funds for the Penang 2nd bridge construction to be procured from China. In addition, the total amount of the proposed budget for 2010, announced in October, 2009, is minus 13.7% compared to the previous year, and development expenditure, including public works investments, has been kept to minus 4.5%, similarly. Though some are of the opinion that a full scale recovery will still require fiscal support from the government, the budget is to be praised in that it takes the long term perspective and has cast a critical eye on the existing fiscal structure which depended on the transfer of funds from the state run petroleum company Petronas.

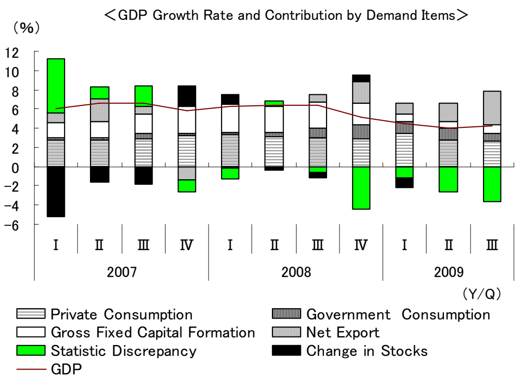
Preparations for the introduction of the goods and services tax (GST: equivalent to Japan's consumption tax), which were put off under the Abdullah administration, are now approaching the final stages, and in this respect and others, the Najib administration's focus is on the national competitiveness that is due to get underway with the Tenth Five Year Plan (2011 to 2015) starting in 2011, rather than on immediate economic recovery. In November, Prime Minister Najib announced the shift of the Plan's vision to Malaysia's becoming a high income nation, and set a numerical target of 6% growth as necessary for the realization of that objective. At the same time, the Prime Minister announced plans to foster and develop sectors in which Malaysia has competitive strength, such as tourism and environment related industries, Halal (Islamic foodstuffs) industries and Islamic finance, as major supports in addition to information and communications technology (ICT) in the effort to accelerate the change of the country's industrial structure from a manufacturing led structure to a service industry led structure.

Malaysia's economy is highly dependent on exports to Japan, Europe and the US so, while full recovery will require some time, if the change in the industrial structure can be quickened, there is every possibility that there will be major improvement in the latter half of 2010. **(Keiichiro Oizumi)**

Indonesia *5.3% GDP growth in 2010*

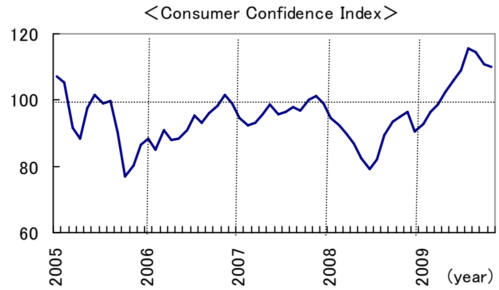
■ 4.3% growth in 2009

Indonesia's real GDP growth rate for January to September, 2009, was 4.2%, compared to the same period in the previous year, a high growth rate in comparison with neighboring countries. Quarterly growth has been stable, at 4.4%, 4.0% and 4.2%. Thanks to economic stimulus measures equivalent to 1.3% of GDP and monetary policy relaxation measures, economic growth for the whole year is estimated to be 4.3%.



Source: BPS

Equivalent to 60% of GDP, it was individual consumption that drove economic growth. This, in turn, was supported by 1) lower interest rates in the wake of stable commodity prices, 2) elections, 3) higher salaries for public officials, and 4) tax reductions and cash payments for the poor. The consumer confidence index announced by Central Bank climbed steadily from the end of 2008 till August, 2009. Motorbike and automobile sales are also tending to increase towards the end of year.



Note: Balance Score Method (net balance+100) has been adopted to construct the index, where the index is above 100 points indicates optimism.
Source:CEIC

Further, since imports have declined further than exports, the contribution of external demand has increased. Exports in the period January to September, 2009, decreased by 25.6%, compared to the same period in the previous year, but imports (including tariff free zones) decreased by 32.8% over the same period. For both exports and imports, petroleum and gas saw a year on year reduction of about 50%, due to the effects of the fall in crude oil prices, but imports (as above) saw a 26.9% decrease in non-petroleum and gas items over the same period, and exports an 18.2% drop, similarly.

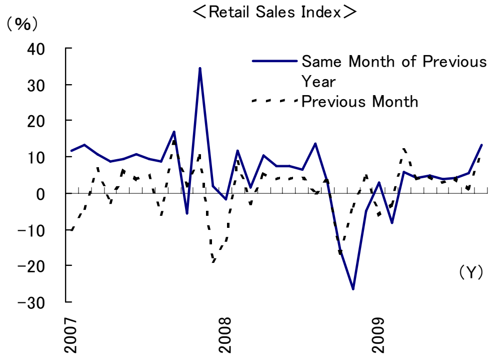
As regards non petroleum - gas export items, animal and vegetable fat/oil (HS 15, principally palm oil) fell to minus 34.3%, compared to the same period in the previous year, but mineral fuels (HS 27, principally coal), ores, slag and ash (HS 26), and ships, boats and floating structures (HS 89) grew by 26.9%, 21.4% and 46.0%, respectively. In terms of exports to individual countries and regions, ASEAN (minus 21.2%), Europe (minus 16.0%), Japan (minus 22.3%) and the US (minus 22.7%) all suffered drastic slumps, but the deceleration in exports to newly emerging economies such as China (minus 5.1%), Korea (minus 9.6%) and Taiwan (minus 4.5%)., were less drastic.

Meanwhile, investments have performed poorly. According to surveys by Central Bank and the Statistics Bureau, the corporate appetite for business expansion slumped in the period January to March, 2009, but recovered in April to June. However, bank lending totals have hardly changed since November, 2008. Central Bank has lowered the policy interest rate intermittently since late 2008, and market interest rates have come down very slowly, and this has been a factor in curbing investment.

■ 5.3% growth in 2010

In 2010, external demand will keep a low profile but individual consumption will maintain a steady pace, so a recovery in investments is envisaged. Further, economic stimulus measures are expected to continue, albeit smaller in scale than those of the previous year, so real GDP growth will likely be 5.3%, topping the previous year's figures. Approaching his second term, President Yudhoyono, in a conference at the end of October that included new cabinet members, heads of local governments and industry representative, among others, outlined a growth scenario in which economic growth would be raised to 7% by 2014, while an 8% unemployment ratio would be reduced to between 5% and 6%, and the head count ratio of the poor would be reduced from its current 14% to between 8% and 10%.

The recovery in investments will depend fairly heavily on how far the Yudhoyono administration can advance with improvements in the investment environment. The president's Democratic Party has a parliamentary majority thanks to a coalition with smaller parties. Aburizal Bakrie, appointed Coordinating Minister for Public Works and Welfare, was elected head of the opposition Golkar Party, and when that party joined the coalition, the president's power base became stronger, allowing him to exert leadership much more easily.

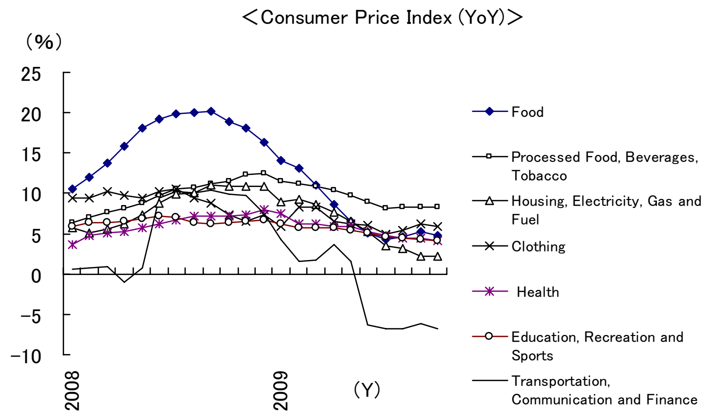


Source: Bank Indonesia

The issues to be addressed are manifold: a review of the strict labor laws that businesses face, infrastructure development, the sweeping away of corruption, etc. In its 100 days program, announced at the beginning of November, the government outlined plans for the expansion of preferential measures through reductions in corporate tax, the advancement of infrastructure development through reform of land law, and the eradication of excess bureaucracy and regulatory duplication through administrative reform. Much attention will be on whether the government is able to get down to a review of the labor laws, something that it was unable to do in its first term. Further, in late August, Central Bank, among other measures that it has taken to promote investment growth, asked the major banks to reduce their interest rates, feeling that the market's high interest rates were restraining investments.

Individual consumption is expected to continue to perform solidly. According to a survey conducted by Central Bank, the real retail sales index for September was up dramatically 13.4% compared to the same period in the previous year, and up 11.5% compared to the previous (figure upper right). Automobile sales in 2010 are projected to be between 550,000 to 600,000, close to 2008's record breaking level (600,000 vehicles).

On the other hand, external demand's contribution to economic growth will likely decline. While the export growth rate will convert to positive growth due to the rise in crude oil prices, it is expected that imports will grow even more. Exports of non petroleum and gas exports look certain to be sluggish, due to the slow pace of economic recovery among the industrialized nations and the fact that there is little prospect of any increase in the prices of palm oil and other primary produce.



Source: CEIC

One cause for concern is the rise in commodity prices. Although commodity prices are currently low and stable, crude oil prices are set to rise in 2010 and Central Bank will probably need to raise its policy interest rate sooner or later. It is desirable to maintain low interest rates in order to achieve high growth, but any delay in responding to rising commodity prices will run the risk of losing market confidence and Central Bank will need to make some careful decisions.

The impact on fiscal policy is also a worry. The budget for fiscal 2010 assumes a crude oil price of $65 a barrel. Fuel subsidies are expected to reach 60 trillion rupiah, topping the previous year's 54 trillion rupiah. If it becomes necessary to top up the subsidies because of rising crude oil prices, concerns over an expanding fiscal deficit will possibly lead to rupiah selling and capital outflow. All eyes will be on the Yudhoyono administration as it tries to cut subsidies while minimizing the impact on individual consumption and investment.

(Yuji Miura)

Philippines *Growth rate to recover to 3.4% in 2010*

■ Real GDP growth rate for 2009 expected to be 1.5%

<Real GDP by Expenditure Shares (YoY) >

(%)

	2008-Q1	2008-Q2	2008-Q3	2008-Q4	2009-Q1	2009-Q2
Real GNP	6.4	5.3	6.2	6.7	3.1	4.4
Real GDP	3.9	4.2	4.6	2.9	0.6	1.5
Personal Consumption	5.1	4.1	4.4	5.0	1.3	2.2
Government Consumption	−0.3	0.0	11.8	2.6	4.5	9.1
Fixed Capital Formation	3.0	1.7	7.1	0.1	−7.2	−1.9
Exports	−7.7	6.1	3.3	−11.5	−14.7	−16.0
Imports	−2.6	0.0	6.7	5.0	−20.6	−2.7

Source: National Statistical Coordination Board

The Philippines' real GDP growth rate for the period January to June, 2009, was 1.0%, compared to the same period in the previous year (0.6% in Q1, January to March, 1.5% in Q2, April to June), well down from 3.8% in 2008. Reflecting the global economic deceleration, exports have been falling at a double-digit rate since October last year. Therefore, equipment investment contracted, and the employment situation in export and other industries deteriorated, leading in turn to a slump in personal consumption.

The period July to December saw a slight recovery, and the real GDP growth rate for the whole of 2009 is thought be around 1.5%. Reflecting the bottoming out of the global economic slowdown, exports began to increase, month on month, from the start of 2009, and consumer and corporate sentiment with regard to the economy has begun to improve. Nevertheless, the economic recovery lacks real strength.

Personal consumption in the period January to June grew a meager 1.8%, compared to the same period in the previous year. Part of the background to this is the worsening of the employment situation, with a quick succession of layoffs announced among electronics companies, as well as a drop in the growth of money remitted home by overseas workers, down to 3.7% in the period January to August, in contrast to the double-digit growth it had managed to maintain up till 2008, and the accompanying adverse impact on personal incomes and consumer sentiment. The government is doing its best to promote employment in various countries. However, for the foreseeable future, there can be little expectation of any major recovery in the growth of money sent home from abroad, and any recovery in personal consumption will likely be a very gradual one.

Growth in fixed capital formation in the period January to June was a very lackluster minus 4.4%. Though construction investment growth was 9.7%, thanks to the implementation of infrastructure projects as part of the government's economic stimulus measures, equipment investment fell to minus 18.6%. In the months ahead, development will likely continue, supported by public investments. As the manufacturers' production index continues its double-digit dive, private sector production activity is stagnant, and it will probably take some time before any real recovery is seen there.

Export growth languished, at minus 28.9% growth in the period January to September, compared to the same period in the previous year (both exports and imports are expressed in terms of customs cleared basis). Electronics related exports, which account for about 60% of the total, were down to minus 30.0%, due mainly to a minus 32.4% slump in semiconductor exports. Also, clothing, the second major item (weight is approx. 5%) was down to minus 24.7%. Meanwhile, imports were down to minus 30.8% in the period January to August, due to contracted domestic demand and the falling price of crude oil. In the future, in step with the gradual recovery of the global economy, imports and exports will likely continue to increase at a very slow pace.

In January 2009, the government announced a package of fiscal stimulus measures worth 330 billion pesos. About 50% of that is earmarked for labor intensive infrastructure construction and social welfare programs, with another approximately 30% for large scale infrastructure programs and the remainder used to reduce individual and corporate taxes. As a result of these measures, government consumption in the period January to June was up 7.0%, compared to the same period in the previous year. The expectation is that the contribution to economic growth will increase through the latter half of the year.

As the economy reeled from the Lehman shock, and early in 2009, the consumer price index fell sharply mainly due to the drop in the rice price, the policy interest rates were lowered by a total of 2% over the period from December 2008 to July 2009. This move did serve to prop up domestic demand to some degree. However, with concerns that crude oil prices and foodstuff prices may rise, it is thought likely that the Central Bank will keep the policy interest rates where they are for the foreseeable future.

■ 3.4% real GDP growth forecast for 2010

The real GDP growth rate is predicted to recover to around 3.4% in 2010. The recovery in personal consumption and equipment investment will not be all that strong, and domestic demand will depend on support from fiscal expenditure. Presidential elections are due to take place in May 2010, and budget expansion will be inevitable. Therefore, while it will not be of the same scale as the previous year, it will surely contribute positively to economic recovery. Also, an increase in some service expenditure related to the election may be expected, and this will very likely boost personal consumption, even if only temporarily. In terms of external demand, though there is only faint hope of economic recovery among the developed nations of Europe and America, China's economic recovery is expected to pick up the pace a bit. So, exports are thought to be capable of recovering to around 10%.

Regarding personal consumption, while the economy goes through a slow recovery, the fact that both the consumer price index and the interest rate level are expected to stay low is sure to be a plus factor. Money remitted home by workers abroad will trend towards recovery, and growth of 5%, year on year, is reasonably certain. On the other hand, the extended worsening of the employment situation is a negative factor. The shift from regular employment to non-regular employment and from skilled labor to cheap labor is having a detrimental effect on personal incomes, and any improvement in the situation will probably not happen until mid year or later. Overall, growth in personal consumption is likely to be fairly pedestrian. Also, there are concerns over potential increases in crude oil prices and foodstuff prices, which will have an impact on the consumer price index in the wake of economic recovery, and there is every possibility that monetary policy will be tightened in 2010. This, if it happens, will surely discourage personal consumption and investment.

As regards fixed capital formation, along with the implementation of the infrastructure projects, it is thought likely that public investments will continue to shore up construction investment. If exports increase, there may well be some recovery in equipment investment, but the pace of growth there has been very poor in recent years, reflecting the fragility of the Philippines' manufacturing industry, and there is little if any hope of a major recovery in that sector. At the very least, until the presidential election is completed and political uncertainty laid to rest, equipment investment will continue to perform poorly. Direct investment from overseas also has contracted as a result of economic deceleration.

Diversification of the Philippines' exports is continuing, with around 15% each destined for the US, Japan and Europe and around 45% within Asia. Therefore, export recovery may be expected to center on Asia centric exports. Electronics related demand is on the upswing, and this is a supportive factor. Meanwhile, imports are very much raw materials focused and their performance tends to be similar to that of exports. Should the price of crude oil rise by a significant margin, there is a strong possibility that the import growth will also rise, having an adverse affect on the trade balance.

Fiscal balance is a major risk factor. The deficit targets for 2009 and 2010 are 250 billion pesos (3.2% against GDP) and 233.4 billion pesos (2.8% against GDP), respectively, with the elimination of fiscal deficit being put off till 2013. Given that the economic recovery will very likely be very pedestrian at best and that extra spending is usually the norm in the runup to a change of administration, the targets are not likely to be achieved easily. Also, if the targets are not achieved, should the economic recovery be delayed, this will very probably be one factor restricting the implementation of another fiscal stimulus measure.

Further, the outcome of the presidential election is one factor behind uncertainty over the future. Basically, a smooth transition of power is expected, but a decisive and powerful candidate has yet to appear. There are concerns that, under a new president, there may be political turmoil and unsound macro-economic management.

＜Fiscal Balance＞

(billion pesos,%)

	2005	2006	2007	2008	2009
Revenue	816.2	979.6	1,136.6	1,202.9	644.1
Tax Revenue	705.6	859.9	932.9	1,049.2	569.2
Other Revenue	110.5	119.7	203.7	153.7	74.9
Expenditure	962.9	1,044.4	1,149.0	1,271.0	832.1
Interest Payments	299.8	310.1	267.8	272.2	183.7
Fiscal Balance	−146.7	−64.8	−12.4	−68.1	−188.0
of Nominal GDP	−2.7	−1.1	−0.2	−0.9	—

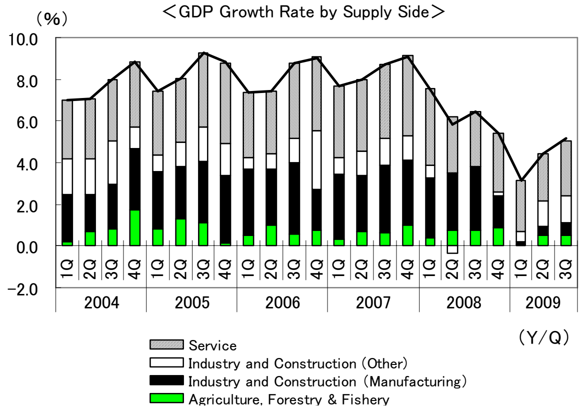
Nnotice: Jan. to Jul. for 2009.
Source: Bangko Sentral Pilipinas

(Satoshi Shimizu)

Vietnam 2010 real GDP growth rate 6.2%

■ 5.2% growth in 2009

Vietnam's real GDP growth rate for the period January to September was 4.6%, compared to the same period in the previous year. Economic growth has been increasing, quarter by quarter, 3.1% in January to March, 4.5% in April to June and 5.8% in July to September, and a high growth rate is expected for October to December also, with a 5.2% forecast for the whole of 2009.



Source: CEIC

Considering the January to September GDP in terms of supply items, the service industry performed well over the same period at 5.9% but industrial manufacturing and construction, and agriculture, fared poorly at 4.5% and 1.6%, respectively. A closer look at industrial manufacturing and construction shows that, while construction growth was high over the same period at 9.3%, the industrial manufacturing sector lacked vitality and grew by only 3.3%, similarly.

The government has not issued statistics for each demand category, but it is clear that individual consumption has been a driver of economic growth. The real growth rate for retail sales in the period January to March was 6.5%, compared to the same period in the previous year, but began to move upwards in January to June, 8.8%, and January to September, 10.2%. Until September, cumulative automobile sales contracted by 12% compared to the same period in the previous year, but month on month sales have been increasing since May and were around 30% up for July to September, a fairly high growth rate.

Investments have been low key, but at least maintaining the same levels as the previous year. Gross capital formation in the period January to September was up 14.4%, compared to the same period in the previous year. A closer examination reveals that, while private sector investment grew 12.6% and foreign investment contracted by 11.2%, state investment grew 45.5%, similarly, making it fairly clear that the mobilization of treasury funds as part of economic stimulus measures bolstered investment growth. The funds required by the economic stimulus measures are the equivalent of 4% of GDP and the forecast is that the fiscal deficit, including expenditure extra to budget, will expand from the previous year's minus 4.1% against GDP to minus 9.0%.

Meanwhile, due to the significant contraction of import growth, the contribution of external demand to economic growth has grown by a large margin. Export growth for the period January to October was 13.8% down on the same period in the previous year, but the contraction in import growth was greater at minus 21.8%. This is believed to have been largely due to a recoil from the previous year's increase in imports of capital goods following the start of multiple large scale plant construction projects by foreign companies.

■ 2010 growth rate predicted to be 6.2%

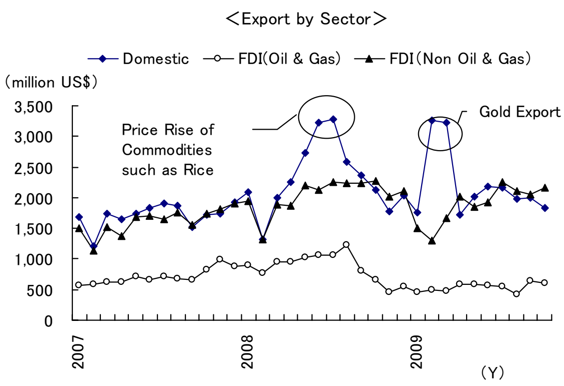
In 2010, economic stimulus measures will continue, albeit on a contracted scale, and easy money policies will be maintained, so the outlook is for solid, steady growth in individual consumption and investment. However, the contribution of external demand will decline by a large degree so, even though the real GDP growth rate will likely surpass that of the previous year, it is expected to come in at 6.2%, slightly under the government's target (6.5%).

Individual consumption is thought likely to perform more or less according to plan. A global marketing research firm, ACNielsen, conducted a consumer survey of 52 countries between September and October and listed Vietnam's consumer confidence very high at 109 points, following India (120) Indonesia (115) and Norway (110). This is 24 points higher than the same rank for April, the biggest increase of any of the 52 countries. In 2009, the Vietnamese government increased spending on social security related payments by 68% on the previous year and, with this and other measures, has enhanced its provision of support for the poor and is set to maintain this provision through 2010, intending by these means to reduce the percentage of the population in poverty.

Investments are also looked to as a potential driver of economic growth. The number of new foreign direct investments approved between January and October, inclusive, reflected a recoil from the previous year, which posted the highest number ever, and languished at a poor 78.3% down on the same period in the previous year. However, it is expected that several large scale projects, including urban development projects, will be approved within the year, bringing the value of approved projects for the whole year to over the government's target of $20 billion, a similar level to the year before last. As regards foreign direct investment in 2010, as the real estate market trends towards recovery, the government has set a year on year 20% increase as its target.

Also, it is expected that state investment will become rather more focused. Given that there are strong concerns over the possibility of fiscal deficit expansion, the government will be pushing ahead with screening and concentration, and placing importance on improving efficiency. With regard to private sector investment, given that corporate confidence is on the upswing, improvements in the business environment may be expected, along with a swing towards recovery, but the poor health of external demand will likely mean that growth will be very pedestrian.

The contribution of external demand in 2010 will very probably be well below that of the previous year. With the rise in the price of crude oil, both exports and imports will convert to positive growth, but since there is no prospect of a rise in primary produce prices (2008) and the raising of standards by gold exports (2009), export growth will most probably be a poor 10%, year on year. On the import front, with the start of construction on an approved Taiwanese - Thai joint venture steel plant, imports of capital goods have started to increase and growth is expected to be around 15%, similarly.



Source: CEIC

One cause for concern over economic health in 2010 is the growing fragility of the banking sector. Banks' loan growth in the period January to September, 2009, was 33.3%, compared to the same period in the previous year, topping the previous year's 21.0%. On the other hand, growth in mining and industrial production for January to October was just 8.5%, compared to the same period in the previous year, well below the 30% posted similarly in the previous year. This will undoubtedly push up the non performing loan rate. And, while there is a ceiling on loan interest, increasing competition to increase deposit interest for the purposes of gathering funds means that banks are having to sacrifice revenue, and this is a cause for concern.

One other worry is the drastic depreciation of the dong. In early November, the dong traded against the dollar at 19,000 dong on the black market, with a wide gulf opening up between this and the bank rate (approx. 17,800 dong). The direct cause is said to be the spreading rumor that Central Bank may be ready to raise the allowable fluctuation range from its current 5%, but other factors include the falling number of tourists and a fall in the amounts of money remitted home by overseas Vietnamese and workers traveling away from home in search of work, with investment in the market becoming all the more speculative.

In addition, foreign direct investment is changing from export oriented to domestic demand oriented, and there is a concern that it will provide a diminished contribution to employment creation and export growth. If increased imports of capital goods lead to an expansion of the trade deficit, concerns over a balance of current account crisis will become heightened. The government has to develop a system capable of attracting high added value export industries by improving government sector efficiency through infrastructure development, personnel education and development, and the eradication of excess bureaucracy.

(Yuji Miura)

India 7.4% growth forecast for fiscal 2010

■ Fiscal 2009 real GDP growth rate expected to be 6.2%

India's real GDP growth rate for April to June, 2009, was 6.1%, a slight improvement on the 5.8% of the previous two quarters. In addition to a growing sense that the global economic slowdown has bottomed out, Lower House elections were held between April and May, resulting in a victory for the ruling coalition and removing political instability. Also, the recovery in capital inflow and the rising share prices have led to a growing feeling that the economic growth rate has stopped falling. In terms of industry trend over the period April to June, against a backdrop of recovering corporate sentiment and improvements in the financing environment, production activity in the industry sector has become active again with manufacturing growth recovering from minus 1.4%, in January to March, to 3.4%. Also, progressing infrastructure construction has helped the construction industry to maintain a high level of growth at 7.1%.

Policies implemented by the government have also contributed to economic recovery. In the wake of the Lehman shock, in fiscal 2008 the government brought out three different economic stimulus packages, worth a total of 1.86 trillion rupees (3.5% against GDP), providing increased government expenditure, reduced commodities and services taxes, support for labor intensive export industries, and the promotion of infrastructure development. In addition, as a result of having lowered the policy interest rates in steps, the repo rate has come down from 9.0% to 4.75%, and the reverse repo rate from 6.0% to 3.25%.

In the future, domestic demand and external demand are both expected to recover, albeit slightly, but it will be a stop - start affair and real GDP growth for fiscal 2009 will likely be around 6.2%. Positive factors encouraging economic recovery include the fact that production activity, particularly for automobiles and steel, is expected to maintain momentum, and that a high level of growth looks likely in the services sector, encouraged by continued expansion of government spending and growth in financial services.

On the other hand, as rainfall in the months June to September was down by more than 20% compared to an average year, the outlook for the agricultural sector is that growth will be negative for the whole year, on a year on year basis. This will probably cause the inflation rate to rise and will have a negative impact on growth in the trade, hotels, transportation and communication industries.

Growth in private consumption is flagging, as the deteriorating employment and income environment in the wake of the global financial crisis have affected consumer sentiment deeply. However, though consumers have been holding off from making non-essential purchases, this restraint appears to be coming to an end, and sales of automobiles, motorbikes and houses are rising. In the months to come, it is expected that private consumption will recover mildly. Among the contributory factors will be the fact that the falling inflation rate, inauguration of the new administration, and the recovery in share prices have improved consumer sentiment and that the consumption of durable goods, which had been languishing since fiscal 2007, is now beginning to recover.

Fixed capital formation also looks set to make a gentle recovery, encouraged by the gradual recovery in corporate confidence, the recovery in corporate earnings, lower lending rates, and increased public investments. However, as there is little prospect of any sudden recovery in exports, the recovery in investments will likely be limited.

Exports in the period April to September were minus 25.3%, compared to the same period in the previous year, and imports were minus 34.2%, resulting in a significant contraction of the trade deficit.

＜Real GDP by Expenditure Shares (YoY)＞

(%)

	F2007					F2008					F2009
		Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4	Q1
Real GDP	9.1	9.2	8.8	9.4	8.8	6.1	8.2	7.8	4.8	4.1	6.0
Private Consumption	8.5	8.4	7.5	8.9	9.0	2.9	4.5	2.1	2.3	2.7	1.6
Government Consumption	7.4	−2.4	10.0	2.0	18.6	20.2	−0.2	2.2	56.6	21.5	10.2
Gross Fixed Capital Formation	12.9	13.6	16.0	14.1	8.8	8.2	9.2	12.5	5.1	6.4	4.5
Exports	2.1	−4.0	−4.8	6.1	9.8	12.8	25.6	24.3	7.1	−0.8	−10.9
Imports	6.9	−0.7	−3.6	6.7	24.4	17.9	27.4	35.3	21.7	−5.7	−21.2

Source: Center for Monitoring Indian Economy

Petroleum related imports, which account for approximately one third of the total, were minus 49.6%, and others minus 25.3%. From May onwards, exports and imports changed to positive month on month growth, but the recovery is expected to be very gradual.

■ Fiscal 2010 real GDP growth rate forecast 7.4%

The real GDP growth rate for fiscal 2010 is forecast to be on the order of 7.4%. Due to the effect of the economic stimulus measures, growth in domestic demand will increase and exports are expected to grow by around 10%, year on year. Also, rainfall is expected to be average and this will likely have the effect of increasing agricultural output and improving private consumption growth.

As the economy recovers, it is expected that consumer sentiment will continue to improve and that private consumption will grow. The fact that the economy seems to have bottomed out appears to have put an end to fears that the employment situation will worsen and it is expected that full scale infrastructure development will help to create new employment. Also, the effect of a series of fiscal stimulus measures (raising the salaries of public officials, debt relief for farmers, and lowering commodities and service taxes) is expected to continue, and hopes are that they will expand further. There are concerns that the fall in agricultural production in fiscal 2009 will have a serious negative impact on incomes and consumption in rural areas, but it is likely that much of this will be offset by the diverse support measures that the government has set in motion to assist farmers.

As far as fixed capital formation is concerned, the economic recovery and increase in exports is expected to bring about a significant improvement in business confidence, and high growth rates can be expected. In the months ahead, it is expected that expanded corporate activity will bring about higher capacity utilization, and that a continued recovery in corporate earnings will bring further improvement to the financing environment, which will in turn lead to increased investments. Currently, the main focus is on investments to expand existing plant and equipment, but the outlook is that there will gradually be more and more investment on new ones. In addition, the fact that infrastructure development and other types of public investment will continue, in line with the Eleventh Five Year Plan (fiscal 2007 to 2011), is another positive factor.

Amidst all this, the growth of the fiscal deficit is likely to be one factor limiting economic recovery. The deficit is estimated to be 6.8% against GDP in fiscal 2009, possibly reaching around minus 11% once oil bonds and other non-budget deficits and local state deficits are factored in. This means that further expansion of the deficit will restrict liquidity, which will in turn make things tougher for private sector investment and may possibly lead to higher long-term interest rates and a downgrading of sovereign ratings. The government, while trying to secure the allocation of funds for infrastructure development and other important expenditure on the one hand, is committed to trying steadily to reduce the fiscal deficit against GDP, and will find it difficult to implement additional economic stimulus measures. In all likelihood, the contribution of government spending to the real GDP growth in fiscal 2010 will be lower than that of the previous year.

Rising concerns over inflation are another important risk factor. Along with the low rainfall, the prices of vegetables, tea, sugar and some other foodstuffs have shot up, and this has affected wholesale prices and consumer prices. Also, since early 2009, share prices, real estate prices in major cities and gold prices have all gone up rapidly. The Reserve Bank, in an October review of its monetary policy, out of consideration for sustaining the economic recovery and the appropriate provision of funding to the productive sector, adopted the stance of careful study of the timing of an interest rates hike, in order to prevent the rising of inflation expectation. If interest rates are in fact raised, this will surely have a negative effect on private consumption and investment.

As far as exports are concerned, primary products (agriculture, mining) and petroleum products, which account for close to one third of the total, will likely continue to perform solidly. In addition, it is estimated that exports of automobiles and electronic machinery by foreign companies are increasing, with an overall export recovery of about 10%. In terms of export destination, there will be growth in exports to China and other parts of Asia, which account for just over 30% of the total. In January 2010, an FTA with ASEAN will come into effect, and this will surely be another positive factor. Meanwhile, roughly two thirds of imports are accounted for by petroleum and petroleum related products, capital goods and intermediate goods. The recovery in domestic production and investment activity, and the rise in crude oil prices, is likely to lead to a rise in import growth, with the possibility that the trade deficit will expand.

(Satoshi Shimizu)

China 2010 real GDP growth rate forecast 9.0％

■ Economic measures take effect, 8.1% growth in 2009

As the global economic situation worsened dramatically, China's economy began to decelerate noticeably from the latter half of 2008 onward. The Hu Jintao administration made a policy switch, from the tight monetary policies introduced with the aim of cooling down investment overheating and soaring asset prices, to ones that set the securing of economic growth as a priority in the country's economic management. Nevertheless, at the beginning of 2009, the major indices were still trending low. After a series of countermeasures that were implemented began to have effect in the spring, the process of economic recovery began.

Real GDP growth (compared to the same period in the previous year) was 6.8% in October to December, 2008, and then fell to 6.1% in January to March, 2009, but recovered to 7.9% in April to June, exceeding the previous quarter's growth rate for the first time in eight quarters. Further, the growth rate went to 8.9% in July to September with the pace of recovery quickening and in October to December, the boosting effect of a series of measures designed to stimulate investment and consumption, as well as a gentle recovery in exports, are expected, so the forecast real GDP growth rate for the whole year is 8.1%, meaning that the government's target of 'around 8%' economic growth looks set to be achieved.

＜Main Economic Measures＞

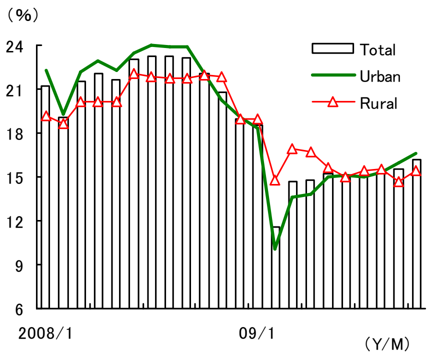
Fields	Countermeasures
Investment	・Implementation of economic stimulus measures of 4 trillion yuan scale ・Abolition of restriction on loan amounts
Consumption	・Reduction of Vehicle Purchase Tax (10%⇒5%) ・Subsidies paid for the purchasing of home electronics and cars
Export	・Raising of the value-added tax export rebate rate ・Expansion of support initiatives for export companies

Source：Chinese Government's official site

Investments have been the driver of economic recovery (of 7.7% growth in January to September, 7.3% points were accounted for by investments). In November, 2008, the State Council announced economic stimulus measures worth 4 trillion yuan. Those measures contained a range of investment projects for the development of transportation networks, the improvement of standards of living, and so on. These projects have been implemented according to plan and this has resulted in 33.4% growth in total investment in fixed assets (nominal basis, plant and equipment plus construction), maintaining a growth rate of over 30%. Also, in the wake of a monetary easing policy, such as the abolition of restrictions on lending amounts (announced in November, 2008), financial organizations have been encouraged to be more positive in lending. In order to secure 8% growth, the government had set a target of at least 5 trillion yuan of new loans for the year, but monthly data shows that the 5 trillion yuan mark was already passed by April and that, by October, the cumulative total was already 1.8 times the target at around 8.9 trillion yuan of new loans. Urban investment in fixed assets growth for the period January to October was 33.1%, compared to the same period in the previous year. This is actually 0.2% points lower than the rate for January to September, but is still a high rate of growth (urban investment accounts for approximately 86% [as of 2008] of the total. The data are released every month except January's data and are a very useful index for estimating total investment in fixed assets, which are only released quarterly). Considering the continuation of economic boosting factors and recent trends in urban investment, it is expected that total investment in fixed assets for the whole of 2009 will be up 30.4%, year on year, the highest rate of growth since the late 1990s.

Consumption continues to recovery steadily. The nominal growth rate for retail sales peaked at 23.3%, compared to the same period in the previous year, in July, 2008, and slowed to 11.6%, similarly, in February, 2009, but has gradually improved again since March. October's growth was 16.2%, similarly, the highest this year since January (18.5%, similarly).

＜Retail Sales (YoY)＞



Source：National Bureau of Statistics

One of the main reasons for the conversion to recovery in consumption has been the full scale implementation of some of the government's efforts to stimulate demand, such as 1) a reduction in the vehicle purchase tax on passenger cars of 1,600cc or lower, 2) subsidies paid to encourage farmers to purchase electrical household appliances and automobiles and motorbikes, and 3) subsidies paid for the replacement purchase of certain items of electrical household appliances and cars that no longer meet environmental standards.

Though the boosting effect of a series of consumption stimulus measures is expected to pick up the pace towards the end of the year, the effects of the slump early in the year will make themselves felt and retail sales growth for the whole year is expected to be 15.6% for the whole year, year on year, coming in 6.0% points under 2008's figures.

In contrast with domestic demand, the recovery in external demand is unsound. From November, 2008 onwards, export value has grown negatively, year on year, and from early 2009 the rate of decrease has been in double digits. In response, the government has raised the export rebate on the value added tax (four times in the first half of the year) and has implemented what measures it could other than the expansion of support initiatives for export companies (increased lending and reduced levying of related costs).

The global economy is pulling out of the worst of the recession and with a series of policy measures being implemented, the pace of decline in export growth has begun to slow, contracting from minus 15.2% in September, compared to the same month in the previous year, to minus 13.8% in October, similarly. It is thought likely that the recovery trend will be seen to have continued from November onwards, but that it will lack impetus, and the export growth for the whole year is expected to be minus 17.6%, year on year, making it the largest such drop in the last 40 years.

Additionally, encouraged by the positive turnaround in industrial manufacturing, imports have begun to rally in advance of exports. Import growth for the whole year, year on year, is forecast to be minus 15.7%. As a result, the year's surplus of the balance of trade will likely contract, with net exports working to push up the growth rate (the net export contribution to the economic growth rate in the period January to September was minus 3.6 points).

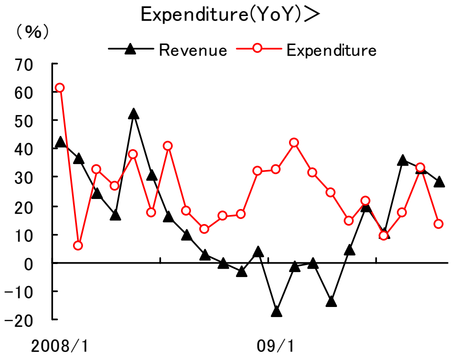
■ Domestic demand led recovery to continue, 9.0% growth in 2010

When considering China's economic outlook for 2010, it is apparent that policy factors, such as to what extent the current domestic demand stimulus measures can be continued, the timing and degree of any policy changes, will have much more of an impact on economic performance than in a usual year. This report will attempt to forecast the growth rates of major economic indices, assuming that economic management, fiscal and monetary policy will be based on the recently announced China Monetary Policy Report and statements by high ranking government officials.

Economic management itself will likely shift from 2009's prioritizing of economic growth to a policy of preventing overheating while working to maintain economic recovery. However, economic management is not thought likely to lean as far towards restraint policy as the 'double prevention' (inflation and economic overheating controls) introduced at the start of 2008. This point of view is backed up by Premier Wen Jiabao's address at the Shanghai World Expo China Forum (November 12).

In his address, Premier Wen mentioned 'maintaining stable and relatively fast economic growth, readjusting the economic structure and managing inflationary expectations' as the most important points of China's economic management. These three items may be considered as all having the same weight, but at least as far as achieving 'maintaining stable and relatively fast economic growth' is concerned, 'positive fiscal policies' and 'appropriately relaxed monetary policies' are being continued. With regard to the other two items, Premier Wen did not mention anything specific, but closed his comments on the economic situation by restating the need to 'promote higher quality economic growth and the stable and relatively fast growth of China's economy'. It would appear, therefore, that economic growth is to take precedence over the other two items.

Also, 'maintaining stable and relatively fast economic growth, readjusting the economic structure, and managing inflationary expectations' was adopted as the economic management until the end of the year at the meeting of the Executive Meeting of the State Council on October 21, but Premier Wen's address did not configure any target deadlines. If this is to be the policy only till the end of 2009, it would be rather strange for the Premier to mention it during an address at a forum for the Shanghai Expo, which is due to start in May, 2010. Therefore, Premier Wen's statement could be construed as referring to economic management in 2010. With no evidence of any contradictory decisions at other important meetings, the possibility that this will be approved at the Central Economic Work Conference (held by central government and the Communist Party in order to decide upon economic management policy) is very high. Therefore, this report assumes that the Chinese government's economic management in 2010 will prioritize the sustaining of economic growth through the implementation of economic measures, at the same time working to prevent overheating of the economy.

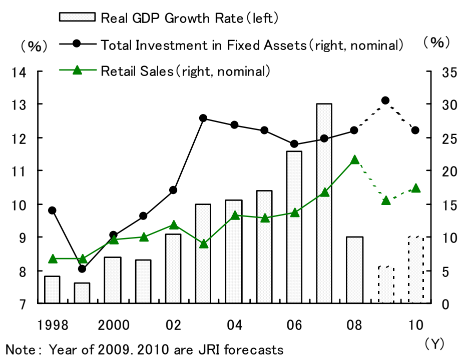


Note : State means Central and Local
Source : Minisrty of Finance

On the fiscal front, the focus is on whether 'positive fiscal policies' can be continued or not. Monthly state (include local) revenue switched to positive growth, compared to the same month in the previous year, from May, 2009, eventually exceeding expenditure from July, evidence that the fiscal situation is improving along with automatic increases in revenue from the economic recovery. As long as fiscal action is kept within a reasonable level, it should not interfere with the implementation of economic stimulus measures.

On the monetary front, in spite of action to strengthen restrictions on loans for certain industries, the authorities themselves appear reluctant to implement tighter monetary policies, such as the reintroduction of restrictions on loan amounts (according to a comment by the People's Bank of China Deputy Governor on August 7, 2009). The latest China Monetary Policy Report, issued in November, 2009, emphasized the financial support of economic growth and the continuance of the easy monetary policy, so the possibility of an overall switch to a tighter monetary policy would seem to be low.

However, this report estimates that, in order to preempt a rapid rise in prices, the base interest rate will be raised once during 2010, by a narrow range. The China Monetary Policy Report no longer speaks of the 'stabilization of the exchange rate at a rational level', but talks of an exchange policy that 'takes into account international capital flow and the trends of major currencies'. This may be interpreted as tolerance of a certain amount of yuan appreciation, but sharp yuan appreciation would damage export recovery and would possibly mean downside risk for economic growth. In consideration of these points, it is forecast that, by the end of 2010, the renminbi's exchange rate against the US dollar will be in the US$1 to RMB6.6 range and will appreciate only very slightly from recent levels (US$1 to RMB6.82, as of November, 2009).



Note : Year of 2009. 2010 are JRI forecasts
Source : National Bureau of Statistics

Based on the foregoing, it is envisaged that domestic demand will continue to lead the economic recovery through 2010 also. The outlook is that real GDP growth for the whole year will be 9.0%, surpassing 2009's level.

In terms of the individual demand component in investments, a few factors may be mentioned which will cause the increase in momentum to be sustained. In particular, the boosting effect of 4 trillion yuan worth of economic stimulus measures is expected to continue to function as the motive power behind investment expansion. According to the Ministry of Finance, of that 4 trillion yuan, central government will be responsible for providing 1.18 trillion yuan, and in the final year, 2010, plans are to put 588.5 billion yuan in infrastructure development and improving the quality of living of the people, and so on, 101 billion yuan more than in the previous year (104 billion yuan invested in 2008). In these most recent economic stimulus measures, central government's investments are pump priming measures, intended to encourage investment by local government and the private sector, and it would seem that funding greater than the increased input by central government will be allocated to project implementation.

Further, there are signs of improvements in corporate earnings, and it is believed that plant and equipment investments for the purposes of improving competitive strength and as part of energy conservation and environmental measures will increase. In addition, increased vitality in investment activity in the central and western regions will surely be a plus factor in the sustainable expansion of investment overall. This is because the development of transportation and electrical power networks is an issue in the central and west regions, and it may be expected there will be demand for infrastructure development over the long term.

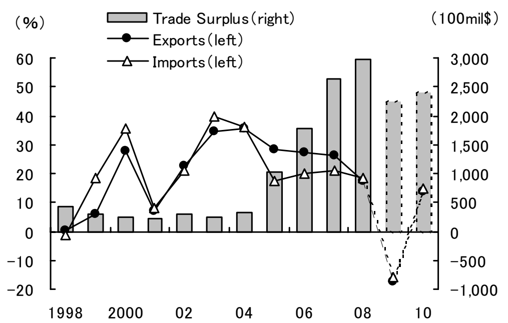
In contrast, there are concerns that efforts by the government to exert control on increased plant and equipment investment in some industries will be a discouraging factor, but by curbing coverage down to a few industries, the impact will likely be limited. Since the monetary authorities, while they are being asked to curb lending to certain industries in which there is evidence of excess production, are at the same time being asked to increase lending to small and medium sized enterprises, there would be seem to be little possibility of any sudden contraction in lending. From the foregoing, the forecast is that in 2010 the total investment in fixed assets nominal growth will be 26.0%, 4.4% points lower than the previous year, but still a high level of growth.

With regard to consumption, there are fears of a recoil in demand due to stimulus measures, but in 2010 at least any dramatic contraction as a result of such a recoil can probably be avoided. For example, the reduction of vehicle purchase tax measures pertaining to small cars is due to end at the end of 2009, and in that event a major decrease in automobile sales cannot be avoided. It is being reported that an extension of the tax decrease measures is being considered, from the perspective of avoiding radical changes. Some are of the opinion that tax decrease measures will continue in the interests of realizing the calls of the Automobile Industry Adjustment and Promotion Plan (2009 to 2011) for the market share of small cars to be increased (see page 31 of the JETRO report ' Risk and Opportunity for Japanese Businesses, the effects of the Chinese government's economic stimulus measures'), so it would appear that there is every possibility that tax decrease measures will be extended, though their scope may be reduced.

As regards the rural household appliance project, cumulative sales for January to October passed the 50 billion yuan mark, but this was short of the level that the government had hoped for (1.6 trillion yuan in four years, including indirect effects). With additional measures such as the abolition of a ceiling price on the applicable electric appliances, it is expected that the project will continue to encourage consumption in rural areas.

In addition, the consumer confidence index released by the National Bureau of Statistics bottomed out in March, 2009, and has continued to improve ever since. The unemployment ratio (4.3% for three consecutive quarters) and the deceleration in the rise in salaries (average salaries for urban employed persons in the period January to September, 2009, grew 12.4%, compared to the same period in the previous year, the same growth rate as for the period January to June) appears to be coming to an end, and an improvement in consumer sentiment is expected. Taken together, this would anticipate that retail sales growth in 2010 will slightly surpass that of 2009, with a forecast of 17.5% for the whole year.

＜Growth of Trade(YoY),Trade Surplus＞



Note: Year of 2009, 2010 are JRI forecasts
Source: Customs Statistics

Exports are expected to grow 13.5% on the previous year. At the China Import and Export Fair, held between mid October and early November, 2009, the export order growth was 16.2%, compared to the previous event (April to May, 2009). However, the expectation is that there will be a significant recoil to the sudden contraction in external demand that occurred from the latter half of 2008 onward, and that it will be difficult to realize the same level of recovery that the figures would suggest. Exports to ASEAN, India, Taiwan and Africa, to which the pace of negative growth has been contracting since the autumn of 2009, have been driving the recovery in exports overall, and a self-sustained recovery of exports to the markets of the developed nations will likely not happen until the economies of those countries and regions go through the recovery process of the latter half of the year onward. The outlook for imports is that they will grow by 15.0%, compared to 2009, against the backdrop of a recovery in domestic demand. Consequently, it is expected that the scale of trade surplus will surpass that of 2009, albeit slightly.

As economic recovery pushes ahead, the Hu administration will be expected to strengthen its efforts to achieve self-sustained economic growth. **(Junya Sano)**