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Topics China' economic policy debate heats up in run up to party congress

There has been a series of treatises issued in recent times by some economists, calling for policy course corrections. Much attention is being paid as to how far their demands will be incorporated into future economic policy.

Income disparity in cities is times 28.9, not times 9.2

In China there is a growing debate around the issue of so-called "grey income". Grey income refers to off-the-books income that falls somewhere in between legal income and illegal income : for example, overly generous gifts presented by interested parties to government officials on the occasion of their child's wedding. The argument is that this kind of activity has had some effect on widening income disparities. The debate began with the publication of a paper by the Deputy Director of the National Economic Research Institute of the China Reform Foundation, Wang Xiaolu, titled "Grey income and national income distribution". Wang calculated actual incomes based on 4,909 urban samples and proved that the income disparity was far above the level stated by the National Statistics Bureau.

The table on the right shows both sets of figures. The National Statistics Bureau claims that the disparity between lowest income households in the bottom 10% and the highest earning households in the top 10% is 9.2 times. While this is a fairly high level, Wang Xiaolu suggests that, as the higher the income level, the more grey earnings there are, the actual disparity is well above that at 28.9 times. He claims that the widening income disparity is not the result of competition but improper income gained from the use of position and title, and argues that there is a need for regulations to restrict opportunities for people to earn such grey income, and also for income redistribution policies.

<Income Inequality, Urban(2008)> (Yuan, Times, %)

Income Class	National Statistics Bureau			Wang		
	Income	Inequality	Share	Income	Inequality	Share
Lowest Income (10%)	4,754	1.0	3.8	5,685	1.0	2.0
Low Income (10%)	7,363	1.5	5.9	8,646	1.5	3.0
Lower Middle Income (20%)	10,196	2.1	8.1	13,392	2.4	4.6
Middle Income (20%)	13,984	2.9	11.2	20,941	3.7	7.2
Upper Middle Income (20%)	19,254	4.1	15.4	29,910	5.3	10.3
High Income (10%)	26,250	5.5	20.9	47,772	8.4	16.5
Highest Income (10%)	43,614	9.2	34.8	164,034	28.9	56.5

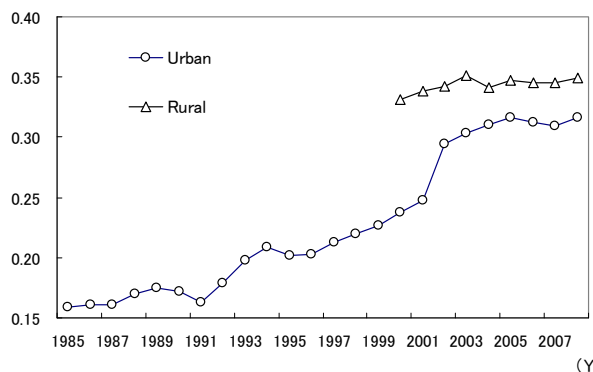
Source: Wang and National Statistics Bureau

The National Statistics Bureau, whose data were used for comparison, posted several articles on its website by individual bureau staff personnel rebutting Wang's arguments in late August. These articles, while praising Wang's paper to some extent, assert that 1) the study's sample was too small, starting from a small group and snowballing outwards to friends and relations, resulting in a significant sampling bias, 2) the data were not from accounts ledgers or records, but from people's memories, casting doubt on their accuracy, and 3) the metric model used to calculate the incomes lacked reliability, etc., and claim that Wang has overestimated the earnings of those in the highest bracket.

Part of the reason for this growing concern over income disparity produced by grey incomes is that people are becoming more sensitive to income disparity in the cities. Income disparity in China has conventionally been discussed in terms of urban versus rural, or coastal versus inland, but now income disparities within the cities are becoming greater. The figure on the right, based on data from the National Statistics Bureau, computes the urban and rural Gini coefficients, and shows that in the past ten years the income disparity within the cities has widened rapidly.

The National Statistics Bureau's rebuttal accurately points out problems with Wang's argument. However, these are questions of methodology and are not to do with the conclusions. Wang's argument that, if the income figures issued by the government are correct then the urban real estate boom and high car ownership rates cannot be explained, is still a convincing one.

<Gini Index, Urban and Rural>

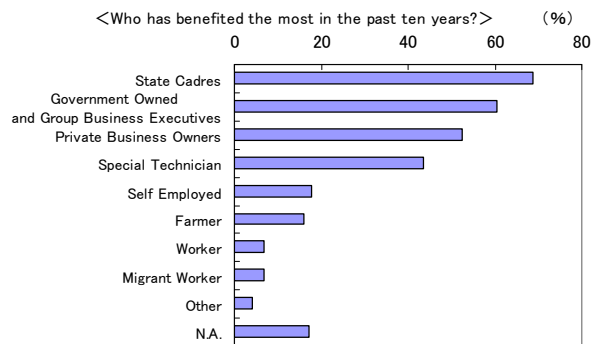


Source: Author's calculation from the data of National Statistics Bureau

■ Debate heating up prior to party congress

A The National Statistics Bureau's rebuttal of Wang's paper is likely due to a sense of crisis that Wang's arguments may well invite criticism of the government. This is Mr. Wang's second paper dealing with income disparity in the cities, as he published a similar one in 2007. At that time also, the paper was widely reported in the media and caused much interest in society. Particular attention is being paid to the fact that, at around that time, the term *choufu xinli* (resentment of the rich) was being widely used in the media. The rich have hitherto generally been viewed with approval and yearning, but as the notion that they may have earned their wealth by abusing their positions and titles has spread, this sentiment has begun to turn to one of contempt and loathing.

This change in the public's sense of awareness of the income disparity is also clear from social studies that have been done. The Blue Book of China's Society 2009 reports that, in answer to the question "Who has benefited the most in the past ten years?" 68.8% of respondents answered "state cadres", followed by "government owned and group business executives" (60.4%) and "private business owners" (52.3%). The fact that government cadres and state owned business executives come out on top hints that the problem of grey and black income has become part of daily life.



Note: Multiple Answer
Source: Blue Book of China's Society 2009

In just the same way as the debate over grey incomes, the issue of *guojin, mintui* (state sector advances, private sector retreats) has been raised by many economists. *Guojin, mintui* means that, while state owned enterprises are flourishing, private sector enterprises are in decline, and is being seen as a sign that China's market economy is in retreat. Senior researcher Ma Jun, of the State Council's Development Research Center points out that, along with the economic stimuli introduced after the Lehman Brothers shock, the growth rate for state owned enterprises' fixed asset investment was well above that of non government owned enterprises. In response, the National Statistics Bureau in August explained that the urban fixed asset investment figures for the period January to June, 2010, show that the growth rate among non government owned enterprises is now above that of government owned enterprises, and that the economy has returned to a 'normal course'.

Several economists have pointed to emerging issues that may threaten the sustainability of China's economic growth. One of the most notable comments has been by Mr. Yao Yang, Deputy Dean of the National School of Development at Peking University, in an article titled 'The End of the Beijing Consensus' in the on-line version of the US magazine 'Foreign Affairs'. In the article, Yao asserts that the benefits of China's economic growth are being monopolized by state owned businesses and local governments, while many ordinary citizens feel poorer, so that the communist party's strategy of seeking to improve legitimacy in exchange for economic growth has reached the limits of what it can achieve, and that there is no real alternative to further democratization.

Part of the background to the vigorous upsurge in debates over economic policy is believed to be the fact that the 18th National Congress of the Communist Party of China is due to be held in 2012. There appear to be conflicting voices within the party as to how China can be set on the path to economic development, and some economists seem to be speaking out after having secured support for their own views.

In fact, though both Wang and Yao have published articles that may be deemed critical of the government, they do not seem to have suffered demotion or any other sort of punishment, at least as far as can be told from the websites of their respective institutes. This kind of public debate may, at first glance, appear to indicate domestic turmoil, but it may also be seen as part of China's strength, unknown in other countries that maintain a single party rule by the communist party. It is to be hoped that the debate will address the successes and problems of economic development objectively, and will trigger the development of policies designed to improve the sustainability of China's economic growth.

(Yuji Miura)

Taiwan Double digit growth for two consecutive quarters, concern over future growth

High growth rate in April to June

Taiwan's real GDP growth rate for the second quarter, April to June was 12.5% (compared to the same period in the previous year), slightly down on the previous quarter's 13.7% (revised), but still a high level of growth. Exports were up 37.5%, fixed capital formation 30.8% (37.5% in the private sector), and the fast paced rally in export growth and a recovery in investments powered economic growth.

Recently, export figures (customs cleared basis) in August were up 26.6%, compared to the same month in the previous year. While exports to India grew 72.2%, U.S. 51.2% and EU 28.4%, exports to China grew 22.5%, falling below the overall growth rate. In terms of export items, general machinery grew by 68.4%, but precision instruments (including liquid crystal displays), which had hitherto posted high growth levels, could only manage 17.6%. As described later, this is believed to be due to the fact that exports to China of liquid crystal displays failed to grow as expected.

In terms of consumption, retail turnover benefited from the effects of a very hot summer, and growth in July was 8.8%, the highest growth level in the last three months. Also, automobile sales have fallen below the levels recorded at the end of last year, due to the end of the tax reduction measures, but a last minute rush in July before *gui yue* (the inauspicious 'Ghost Month', which in 2010 is from August 10 till September 9), helped boost sales.

Along with the recovery in both domestic and external demand, the unemployment rate (seasonally adjusted), having peaked in September, 2009, at 6.09%, fell to 5.17% in August (number of persons engaged in employment up 285,000, year on year), but was 5.22% in Jun and 5.20% in July, indicating that the pace of improvement is slowing.

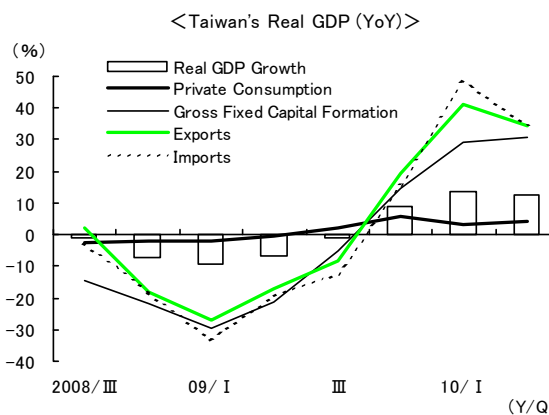
Deceleration expected in second half

Growth levels in the first half of the year were close to the levels of recent years, but as the effects of economic stimulus measures begin to wane both domestically and externally, it is expected that there will be a significant deceleration over the latter half of the year. In fact, while part of this may be said to be due to a recoil from the rapid recovery, growth rates compared to the previous period (annual rate conversion) have been falling for three consecutive quarters. They fell from 16.7% in Q3, October to December, 2009, to 10.9% in Q1, January to March, 2010, to 7.2% in Q2, April to June, 2010, and the government is expecting negative growth in the latter half of the year (though maintaining positive growth compared to the same period in the previous year).

In particular, since the Taiwanese economy is heavily dependent on the IT industry, careful attention needs to be paid to trends in that sector. In global terms, sales of smart 'phones, portable music players and portable multi-functional terminals, for example, have been strong, but inventories of flat screen displays and notebook PCs are beginning to swell, and in July, Acer and a major contract PC manufacturer saw their sales decrease by a huge margin on the previous month (one cause appears to have been potential purchasers holding back in anticipation of new models). Further, in response to the growing inventory of liquid crystal TVs in China, major liquid crystal panel manufacturer AU Optronics (AUO) cut back their production in the period July to September by 10%. Export order volume has also begun to peak, and orders received for July were below the previous month's level.

Therefore, due to the effects of the recoil from the recent rapid recovery and the global economic deceleration, economic growth is expected to slow between now and the end of the year, and growth for the whole of 2010 is forecast to be 7.4%.

(Hidehiko Mukoyama)



Source: Directorate General of Budget, Accounting and Statistics

Malaysia Economy maintains healthy 8.9% growth in Q2

2010 growth rate looks set to exceed 6%

Malaysia's real GDP growth rate for the period Q2, April to June, was 8.9%, compared to the same period in the previous year. On an actual basis, economic growth is at higher levels than it was before the global financial crisis, and the economy may be said to be transitioning out of the recovery phase and into an expansion phase.

As business confidence improved, private sector consumption grew 9.7% in the same period, amid 1) a favorable labor market, 2) comparatively low commodity prices, and 3) a solid increase in income levels. Automobile sales were up 9.1%, similarly, to 120,000 vehicles, and may pass the 550,000 vehicle mark in 2010. Additionally, accompanying the rapid growth in exports, an increase in plant and equipment investment and the implementation of public investments as part of economic stimulus measures boosted fixed capital formation growth to a high 12.9% in the same period.

On the supply side, manufacturing and services performed strongly. Manufacturing grew 15.9%, similarly, with growth being driven by electronic and electrical equipment, up 23.2%, similarly, and vehicle equipment and related products up 26%. The service sector posted a solid 7.9% growth, mainly in wholesale and retail, finance and insurance, and transportation. Given these trends, Bank of Negara (Malaysia Central Bank) has judged that the economic recovery is now fully underway, and raised the policy interest rate by 0.25% points in March, May and June (rate at 2.75% as of September). Towards the end of the year, though in addition to some economic slowdown among the industrialized nations, there is also a risk of falling exports to ASEAN. Nevertheless, with domestic demand as the engine of growth, economic growth for 2010 is expected to exceed 6%, compared to the previous year.

Strengthening trade ties with China

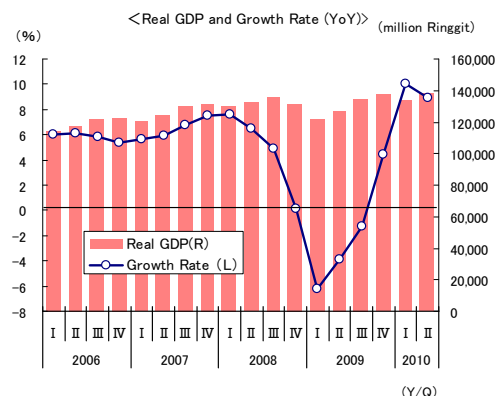
While domestic demand is indeed solid, Malaysia is highly dependent on foreign demand and export expansion is still very important to sustaining economic strength.

In terms of exports, in addition to a rapid increase in electronic and electrical goods, there has also been an increase in exports of mineral resources and other items to neighboring countries, resulting in a 40.8% growth in the period Q1, compared to the same period in the previous year, and 33.2% in Q2. In monetary terms, however, export value has only recovered to 90% of its levels just before the world financial crisis (July to September, 2008).

Exports to the U.S. are still only at around 75% of their pre-crisis levels. Exports to other major destinations, such as Europe, Japan and ASEAN, have not yet reached their pre-crisis levels either. Only those destined for China have recovered to better than pre-crisis levels. In particular Chinese domestic demand for electronic and electrical goods and palm oil is strong.

In order to strengthen trade ties with China, the Malaysian government has announced the establishment of a one-stop service in Kuala Lumpur in support of application procedures for export licenses for China, and from August 19, the Chinese government has permitted the settlement of trading transactions in yuan. China is still Malaysia's second largest export destination next to Singapore, and given the Najib administration's policy of prioritizing China, may well become the largest export destination in 2011.

(Keiichiro Oizumi)



Source: Bank of Negara

<Export Destinations>

	(million dollars)		
	Q3 in 2008 (a)	Q2 in 2010 (b)	(b)/(a)
China	5,860.8	6,032.2	1.03
U.S.	6,557.1	4,836.0	0.74
EU	6,077.0	5,218.6	0.86
Japan	5,314.4	4,736.7	0.89
ASEAN	14,189.1	12,218.1	0.86
Singapore	8,070.2	6,455.6	0.80
Total	54,965.5	48,474.3	0.88

Source: Bank of Negara

Philippines Real GDP growth rate 7.9% in the second quarter

Real GDP growth rate 7.9% in Q2

The Philippines' real GDP growth rate fell from 3.7% in 2008 to 1.1% in 2009, the lowest level since the currency crisis of 1997, but began to recover in 2010, reaching 7.8% in Q1, January to March, and 7.9% in Q2, April to June (compared to the same period in the previous year). This was the first time that over 7% growth has been sustained for two consecutive quarters since Q1 and Q2 of 2004, at the time of the previous presidential election. Among the contributory factors to this high level of economic growth are 1) the successful completion of the presidential election with minimal unrest, 2) the recovery in overseas investor confidence in the Philippines, and 3) increased government expenditure on public works.

In terms of specific sector performance in the period April to June, agriculture was minus 3.0%, industry up 15.8%, and services up 6.4%. Agriculture suffered the effects of El Niño, with harvests of rice, corn and sugar cane falling well below the previous year's levels. In industry, manufacturing fared well from the recovery of domestic and external demand, posting 12.4% growth. In addition to the 56.4% growth enjoyed by electrical machinery, the Philippines' principal exports, petroleum and coal products, chemical products and metal products all returned double digit growth figures. In the construction industry, which posted 22.6% growth, in addition to the high levels of growth maintained by public works projects, the private sector also enjoyed high growth. Electricity, gas and water, too, posted a healthy 8.4% growth, encouraged by the vitalization of production activities.

In the services sector, in the wake of economic recovery, a wide range of industries have shown high levels of growth, with the sector as a whole growing 6.4%. Particularly noteworthy were aircraft transportation (18.6%), retail trade (10.2%), other private sector services that include BPO (business process outsourcing) and hotels and restaurants (6.7%), and real estate (9.4%). In real estate, sales and rentals of real estate grew strongly and posted the highest ever quarterly growth rate for that industry.

Future outlook

New President Benigno Aquino gave his first state of the nation address in July. In addition to promising tougher action against corruption and tax evasion, the President spoke of enhancing education, medical treatment and other social policies, advancing infrastructure development through greater collaboration between the public and private sectors, and basically did not stray far from traditional policy content, bringing a sense of ease to the market.

In response to the announcement of the growth figures for January to March, the government upgraded its economic growth forecast for 2010 from between 2.6 and 3.6% to between 5.0 and 6.0%. Due to the high levels of growth returned in the first half of the year, growth for the whole year may well be around 6%. Personal consumption is expected to continue strongly due to a number of factors, such as the fact that money remitted home by Filipinos working abroad in the period January to June increased 6.9% compared to the same period in the previous year, that consumer sentiment is continuing to improve, that while the consumer price index increase rate is a little high at around 4%, it is still well within Central Bank's target range (3.5 to 5.5%), and that any rise in the policy interest rate is not expected to happen until after the year end. Additionally, exports of semiconductors and other major electronics related export items are increasing rapidly and are expected to continue to do so in the near future, so that durable equipment investment is expected to expand solidly. However, in order to sustain high levels of growth over the mid term, structural policies, such as cutting the fiscal deficit, which is expected to be 3.9% against GDP in 2010, and fostering industries through the development of the investment environment, will need to be pushed forward.

<GDP Growth Rates by Industrial Origin (YoY)>

	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	2010Q2
Real GNP	3.3	4.4	4.1	4.1	8.6	7.9
Real GDP	0.5	1.2	0.2	2.1	7.8	7.9
Agriculture, Fishery, Forestry	2.1	0.2	1.4	-2.9	-2.7	-3.0
Industry Sector	-2.6	-0.6	-4.8	3.8	15.9	15.8
Manufacturing	-7.6	-7.4	-7.9	3.9	20.4	12.4
Construction	13.8	22.2	2.0	1.1	4.3	22.6
Service Sector	1.9	2.7	3.4	3.1	7.1	6.4
Transportation, Communication, Storage	5.6	1.0	-1.5	-2.6	-1.1	4.2
Finance	1.2	5.8	11.5	6.0	6.5	2.2

Source: National Statistical Coordination Board

(Satoshi Shimizu)

China From rapid recovery to cruising speed expansion

■ As investment growth continues to decelerate, some indices appear to stop falling

Investment growth in China is keeping to a gradual slowdown, amidst a recoil reaction to the recent rapid recovery, and the implementation of measures designed to curb investments in the real estate market, and other industries prone to over-production. Investment in Fixed Assets in Urban Areas in the period January to August was up 24.8% compared to the same period in the previous year, 0.1% points down on the growth rate for January to July. Investment in real estate development, which accounts for 18.7% of that total (in 2009), was up 36.7%, compared to the same period in the previous year, and has started to decelerate from mid year onwards. The August real estate price index for 70 major cities grew 9.3%, compared to the same period in the previous year, slowing on the previous month's figures for the fourth consecutive month.

On the other hand, some domestic demand indices show signs of ending their downward drift. For example, automobile sales for August were up on the previous month's performance for the first time in five months. This is due to the fact that the enhancement of stimulus measures has begun to pay off. The Purchasing Managers' Index (PMI) of the manufacturing industry and Value Added of Industry also posted slightly better year on year growth in August.

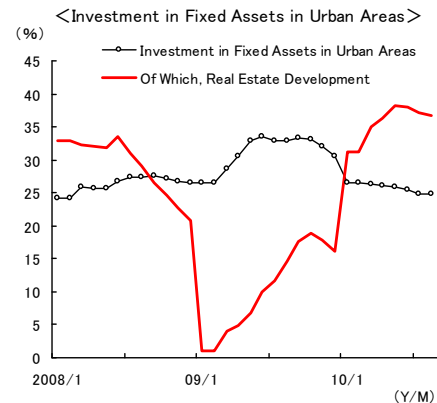
August exports were worth \$139.3 billion, up 34.4% on the same month in the previous year. While growth has continued to slow since May, the pace of decline is easing somewhat. Imports were up 35.2%, similarly, exceeding the previous month's performance for the first time in five consecutive months. Processing trade, such as consignment processing and assembling, accounts for slightly less than half of all exports (in 2009) and, given that import trends are an advance indicator of export performance, it may be comfortably expected that exports will enjoy solid expansion for the foreseeable future.

In consideration of the above, it would be reasonable to think that the Chinese economy has come out of the period of rapid recovery and is now entering a period in which steady expansion at a more moderate pace may be expected to be maintained.

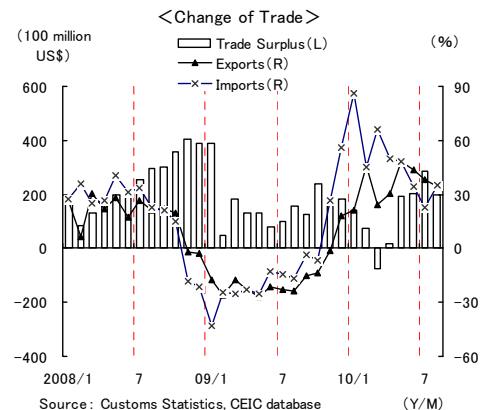
■ Chinese government focuses efforts on long term initiatives

In the face of these circumstances, the economic and industrial policies announced by the government in recent times have tended to emphasize a long term view instead of a short term view. On September 6, the State Council issued two instructions concerning notion on the handling of industries relocating to central and western (interior) provinces, and notion on corporate takeovers, mergers and restructuring. The former was intended to encourage labor intensive industries (such as textiles, toys) and agricultural processing, and so on, to move from the eastern (coastal) provinces and regions to the interior and western provinces, while the latter described the implementation of fiscal and monetary support measures designed principally to enhance competitive strength and avoid duplication of investment. At the Executive Meeting of State Council on September 8 it was decided to reinforce initiatives to promote seven strategic industries, such as bio technology, energy and environmental conservation. Although these moves smack strongly of forward preparation in advance of the 12th Five Year Plan, starting from 2011, they are both important measures from the perspective of the long term maintenance of China's healthy economic growth. The Hu Jintao administration will surely find itself tasked to implement these measures steadily while avoiding any drastic economic changes.

(Junya Sano)



Note: Figures are year-to-date. The growth rate in January is not announced. Therefore, this graph used growth rate in January-February compared to previous period.
Source: National Bureau of Statistics



Source: Customs Statistics, CEIC database