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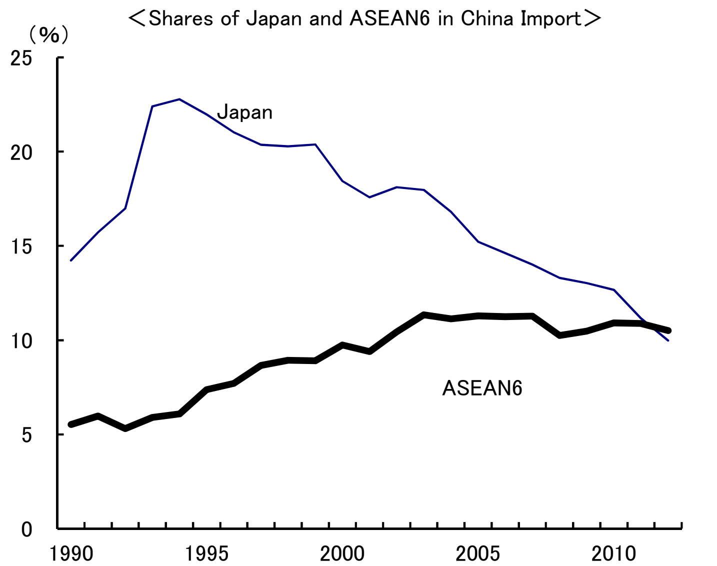
Topics *ASEAN exporters rush to court Chinese markets*

Chinese imports from ASEAN in the period from January to June of this year outstripped those from Japan, in terms of import value. Since ASEAN – China FTA activity will reach a new stage within 2012, Japanese companies have to consider how to leverage the ASEAN production base to develop markets in China.

■ ASEAN imports increasing rapidly

While China's economy has slowed in the wake of the Eurozone economic crisis, its growth rate for the whole year is still expected to exceed 7%. For the past 30 years, China's average economic growth rate has been 10%, and no other country has been able to sustain such a high level of growth over such a long period of time. The second largest economy in the world, its robust purchasing power has begun to attract a lot of attention to China in recent years as a "world marketplace".



Note: 2012 shows January to June
Source: UN, *COMTRADE*

China's imports grew from $225.1 billion in 2000 to $743.4 billion in 2011, expanding by almost eight times. The size of China's imports is second only to the US in the world, and imports come from a diverse range of countries. The number of countries and regions importing an annual value of over $100 million has grown rapidly from 65 in 2000 to 120 in 2011. China's imports from Japan increased from $41.5 billion in 2000 to $194.6 billion in 2011, making Japan China's biggest importing country in term of value. Exports to China now play in important part in ensuring Japan's sustainable economic growth. However, it needs to be noted that Japan's share of imports into China has fallen from 18.4% in 2000 to 11.2%.

Meanwhile, imports from ASEAN6 (Indonesia, Malaysia, the Philippines, Thailand, Singapore and Vietnam) have grown from $21.9 billion to $189.8 billion in 2011, with the market share rising from 9.7% to 10.9%. And, in the period January to June, 2012, imports from ASEAN6 were worth $92.9 billion, surpassing Japan's $88.3 billion. While Japan remains China's top importing country, ASEAN6 has become the number one importing region.

■ Industrial product centric import structure

ASEAN6 import items used to feature many raw materials, such as petrol and timber, but are now mainly industrial products and their parts and components. The top import item from ASEAN6 is integrated circuits. Second are computer related products including HDDs, with semiconductor devices in seventh place and computer related parts in eighth place. China is the world's number one exporter of computers, but many of the parts are imported from ASEAN6, due to the growing supply chains between China and ASEAN. The number three import item is natural rubber (used as raw material for automobile tires), reflecting China's burgeoning car market, and number six is palm oil, reflecting the growing foodstuffs market in China. Encouraged by high levels of economic growth, China's energy demands are growing, and many items, such as coal (4th place), refined petroleum products (5th place), crude oil (11th place), and lignite (12th place) depend on imports from ASEAN6. Further, imports of petrochemical products, such as cyclic hydrocarbons (13th place), ethylene polymers (14th place), and acyclic alcohols (19th place), are increasing.

It is doubtless that many of these industrial products come from the ASEAN factories of multi-national corporations including many Japanese companies. Incidentally, Japanese manufacturers' direct investment in ASEAN6 was worth 5.3 trillion yen at the end of 2011, exceeding 4.8 trillion yen for China.

＜Top 20 Items of Import from ASEAN6 in China＞

(Million dollars)

	HS Code	Name	Value	Main Import Country			
				1st	Value	2nd	Value
1	8542	Integrated Circuits	44,134	Malaysia	28,096	Philippines	5,567
2	8471	Computer-related Products	14,865	Thailand	7,665	Philippines	3,126
3	4001	Natural rubber	8,971	Thailand	4,685	Indonesia	2,061
4	2701	Coal	8,289	Indonesia	6,410	Vietnam	1,827
5	2710	Refined Petroleum Products	7,927	Singapore	4,838	Malaysia	2,551
6	1511	Palm Oil	6,621	Malaysia	4,281	Indonesia	2,337
7	8541	Semiconductor Devices	4,598	Malaysia	2,619	Philippines	938
8	8473	Computer-related Parts	4,131	Thailand	1,822	Philippines	1,040
9	2604	Nickel Ore	4,082	Indonesia	2,711	Philippines	1,370
10	4005	Compounded Rubber	3,702	Malaysia	1,736	Thailand	1,711
11	2709	Crude Oil	2,990	Malaysia	1,427	Vietnam	750
12	2702	Lignite	2,891	Indonesia	2,661	Philippines	191
13	2902	Cyclic Hydrocarbons	2,723	Indonesia	1,023	Thailand	812
14	3901	Ethylene Polymers	2,488	Thailand	1,227	Singapore	814
15	8517	Communication Equipment	2,383	Malaysia	1,079	Thailand	686
16	2601	Iron Ore	2,216	Indonesia	1,077	Malaysia	622
17	8443	Printers	2,191	Malaysia	680	Singapore	618
18	8523	Recording Media	2,149	Singapore	2,043	Malaysia	55
19	2905	Acyclic Alcohols	1,973	Singapore	1,138	Malaysia	445
20	2606	Aluminum Ore	1,574	Indonesia	1,570	Malaysia	4
		Others	58,345				
		Total	189,240				

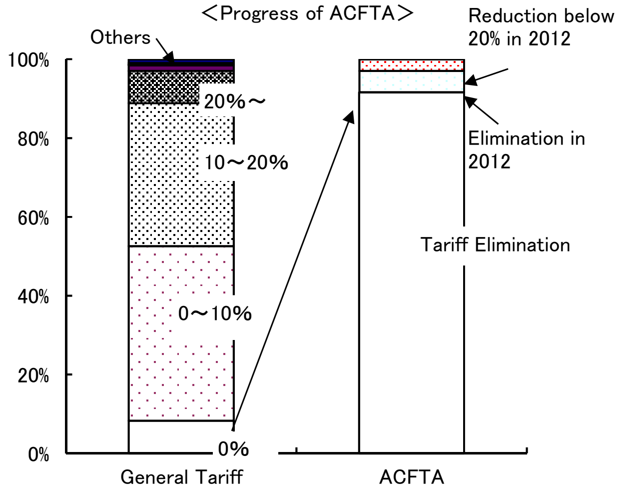
Source: World Trade Atlas

■ ASEAN – China FTA entering new phase

Against this backdrop, the ASEAN – Chin FTA (ACFTA) is heading towards a new phase.

ACFTA came into force in 2005, and tariffs have already been removed from 7,262 items (91.6% of the total). By the end of 2012, tariffs will be removed from a further 232 items (2.9% of the total), while tariffs on the remaining 429 items (5.4% of the total) are due to be reduced to less than 20%.

＜Progress of ACFTA＞



Note: Number shows tariff rate

Source: Table of China Tariff

If the tariff removals and reductions of the ACFTA framework were to be applied to Japan – China trade, some 91.4% of the import value from Japan would be tariff-free. Of course, it would be unrealistic to think that all of Japan's exports to China could be replaced by those from ASEAN, but given the fact that Japanese manufacturers own large production facilities in ASEAN, that the Japan – China – Korea FTA will likely take some time to be concluded and effectuated, and that salaries in China are rising quickly, the leveraging of production facilities in ASEAN, and the ASEAN – China FTA, must surely be considered as one extra possible strategy in developing and securing new markets in China.

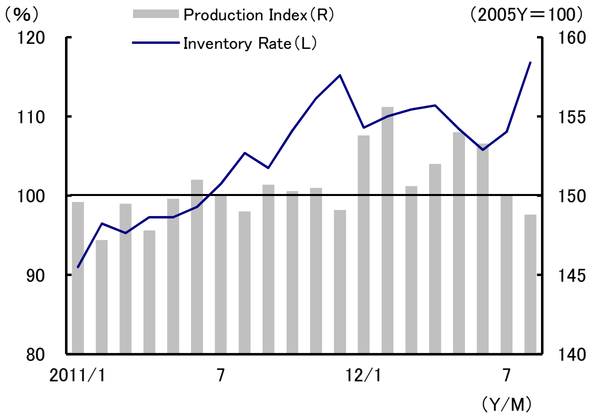
(Keiichiro Oizumi)

Korea Economic situation getting worse

■ Economic situation getting worse

South Korea's domestic and foreign demand continues to decelerate, while the economic situation deteriorates. Exports (customs cleared basis) were minus 6.0% in August, compared to the same period in the previous year, then minus 2.0% in September, falling below the previous year's levels for three consecutive months.

In terms of consumption, real retail turnover (seasonally adjusted) in July saw household electrical appliances grow 2.6%, due to the effects of the hot summer and the London Olympiad. However, growth slipped minus 0.5% in August. Automobile sales in that month (including imported vehicles) suffered from the effects of the Hyundai Motors strike, and fell to minus 21.9%.



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

Consumption has been impacted by 1) poor growth in real incomes, 2) increased debt repayment burden, 3) debt restraint measures, 4) falling housing prices, and 5) deteriorating consumer sentiment (the consumer confidence index fell below the reference 100 point mark in August and September). Prices of apartment housing (similar to Japan's "mansion" flats) in Seoul city slumped 3.6% in September, the biggest drop in recent times, highlighting the seriousness of the market's stagnation. There are more than a few people who took out a loan to purchase an apartment (as an investment), only to find that they could not sell it, and are now saddled with the burden of loan repayment.

In addition to exports and consumption, facilities investment also appears to be slowing. Domestic private sector machinery order value (excluding vessels), which indicates the future performance of facilities investment, has been contracting since May. This deceleration in domestic and foreign demand has caused the manufacturers' production index (seasonally adjusted) to fall below the previous month's level for three consecutive months, and inventory ratios (inventory index/ shipment index) are on the way up again. Deteriorating corporate performance has caused a rise in the banks' corporate loan delinquency rates.

■ Concerns over falling domestic demand

Bearing in mind the economic cooling in Europe and the deceleration of the new emerging economies, including China, exports are not expected to recover any time soon. Additionally, there are concerns about the cooling of domestic consumption. As the economic environment gets tougher, many companies are beginning to implement "emergency management systems", and are beginning to cut staff numbers, and the number of filings for individual bankruptcy (including the self-employed) appears to be on the increase.

In response to the economic deceleration, interest rates were lowered in July and October, and real estate financing restrictions were partially eased. Tax reduction measures were announced on September 10. The main feature of these measures will be a lowering (until the end of the year) of the real estate transaction tax and special consumption tax on purchases of automobiles and large household appliances. Recovery in consumption will require an improvement in household balance sheets. Lower interest rates will ease the burden of interest payments, and if the vitalization of real estate markets can do something to halt the fall in housing prices, balance sheets will likely improve in response. Still, concerns remain, such as whether the real estate market can pull itself out of a protracted slump, and whether household debt is likely to swell further.

Recently, the opinion is being voiced that South Korea's economic downturn could be a long one. In the runup to the presidential elections on December 19, much attention will be focused on what kinds of economic policies the candidates can come up with.

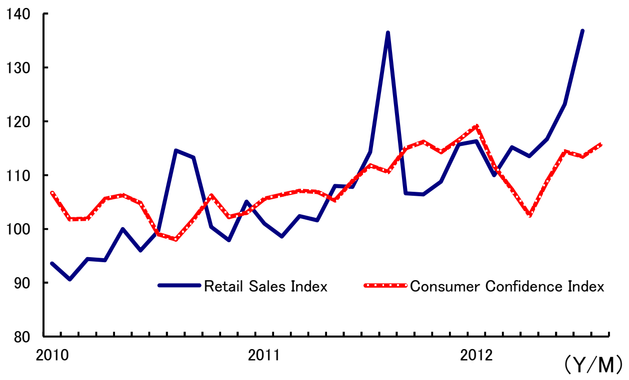
(Hidehiko Mukoyama)

Indonesia Economic growth over 6% expected to be sustained

■ Private consumption and investment solid

Bank Indonesia's monthly report for September warned of the risk of global deceleration, but also revealed that the country's economic growth for July to September was expected to be on track to achieve forecast targets. In the Bank's monthly report for July, the real GDP growth rate forecast was given as 6.3% for the period July to September, and between 6.1% and 6.5% for the whole year. While the September monthly report avoided quoting these figures, it reaffirmed the optimistic view of the future.

<Consumer Confidence Index and Retail Sales Index>



Note: Retail Sales Index is based on 2010=100. The net balance+100 method has been used to construct the consumer confidence index , where the index above 100 points indicates optimism.
Source: CEIC

One fact in support of this view is the solid performance of private consumption. Tighter restrictions on consumer loans caused motorbike and automobile sales for August to fall to more than 20% below the previous month's levels, but the recent consumer confidence index and retail sales index are trending upwards. Strong expectations of commodity price stability, improved employment conditions and increased incomes are expected to translate into solid private consumption growth.

One other factor is investment. According to the Investment Coordinating Board, foreign direct investment（FDI）in the period January to June, 2012, grew 30.3%, $12 billion, compared to the same period in the previous year. In terms of countries and regions, investments from Asia were the largest, growing 32.2%, $4.8 billion, accounting for 40% of the total. Singapore was also noticeable, up 4.2% in the same period, $2 billion, followed by Japan (up 53.7%, $1.1 billion), and South Korea (up 96.7%, $1 billion). Meanwhile, domestic investments for the period January to June were up 22.6%, 40 trillion rupiah. Investments in mining and manufacturing, paper making and printing, chemicals and pharmaceuticals, metals, machinery and electronics are flourishing. Central Bank's Business Survey forecasts that, in spite of the fact that corporate business expansion appetite waned slightly during the January to March timeframe, it recovered in April to June, and domestic private sector investment growth is expected to maintain its momentum going forward.

■ Current account deficit expanding

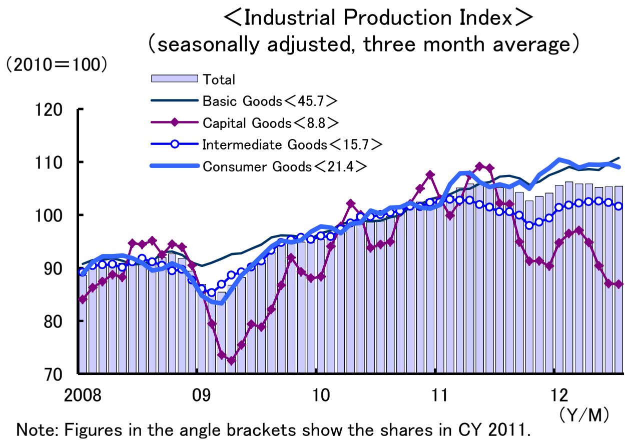
The International Monetary Fund (IMF) published its Global Outlook in October, in which Indonesia's real GDP growth rate for 2012 was forecast at 6.0%. World Bank revealed a forecast of 6.1% in the same month. While this is definitely slower than the previous year (6.5%), the employment improvement target of 6% certainly seems sustainable. Meanwhile, according to Central Bank's Macro-economic Index Forecast Survey (conducted in the second quarter, 2012), which targets private sector economists, 85.5% of those surveyed responded that the economic growth rate for the period July to September was likely to be between 6.1% to 6.5%, with 83.5% forecasting the same level for the whole of 2012.

A cause for concern going forward is rupiah depreciation in the wake of a worsening current account deficit. The $2.19 billion current account deficit for the period October to December, 2011, expanded to $6.94 billion in the period April to June, 2012, due to a shrinking trade surplus caused by falling crude oil prices. Central Bank is looking forward to an improved capital account balance as a result of increased securities investment and direct investment, and is, therefore, optimistic about the future. Currently, securities investment is growing at a steady pace, but as investments in China and India, which have thus far been drivers of export growth, begin to lose their edge, there are signs that direct investment may come to a halt, such as the contraction in import of capital goods since August, and it is by no means certain that the current account deficit will contract as envisioned by Central Bank.

(Yuji Miura)

India Embarking on economic reform

■ Economy weakening, especially manufacturing



Note: Figures in the angle brackets show the shares in CY 2011.
Numbers in parenthesis are weight.
Source:The Japan Research Institute, Ltd, based on the data of The Mnistry of Statistics and Programme Implementation.

India's economy is continuing to lose momentum, especially in the manufacturing sector. Real GDP for the period April to June, 2012, grew 5.5%, compared to the same period in the previous year, slightly stronger than January to March (5.3%, similarly), but economic indices since July show that India's economy is still not yet on track for a strong recovery. July's industrial production index was no more than a wafer thin 0.1% increase compared to the same period in the previous year. In particular, capital goods have slumped significantly. This has been caused by the economic stagnation in Europe, which accounts for a high proportion of India's exports, and a major drop in plant and equipment investment appetite, against a backdrop of high domestic interest rates. In addition, widespread power outages in the north and east in July had the effect of restraining manufacturing.

Although consumer goods have been performing relatively strongly, high interest rates and soaring gasoline prices have caused demand for automobiles, motorbikes and other durable consumer goods to lose momentum, and growth continues to be sporadic. Despite the economic slowdown, Central Bank and the government are concerned about the expanding fiscal deficit and accelerating inflation, and while they have not been able to come up with positive fiscal or financial policies, in mid September the government announced an economic reform plan.

■ Major economic reforms in pipeline, but economy expected to stay slow in the short term

The basic framework of the reforms is comprised of 1) diesel price hikes, 2) relaxation of restrictions on foreign direct investment in sectors such as retail, private sector airlines, broadcasting and power, and 3) selling off shares in state owned enterprises. The government expects to reduce the fiscal deficit and improve productivity with these measures. In particular, it is hoped that the relaxation of restrictions on foreign direct investment in retail will allow major retailers that are skilled in refrigerated distribution and inventory and demand management to become involved, resulting in improvements in the currently very high rate of food products lost to decay before they can be sold, and strong inflation restraint. Riding the tailwind of additional monetary easing in the US, and positive feeling about a number of recent announcements, share prices at the end of September were at their highest level since June, 2011, and the exchange rate also saw the rupee strengthen quite significantly at one point.

Of course, there remains much uncertainty as to how far economic reform can actually proceed in some sectors. For example, with regard to foreign direct investment in the retail sector, there are still many restrictions in place. The decision on whether to allow new stores to open in provinces with no cities with populations of over a million is to be left to the provincial government. However, from the perspective of local small and medium sized enterprises who fear an adverse impact, many provinces are currently opposed to the move. Also, political parties opposed to these reforms have quit the coalition, causing the coalition government to lose its parliamentary majority, and it is feared that this loss of centripetal power will bode ill for reforms in the future. Even if a series of reforms were able to be implemented according to plan, it will take some time for the positive effects of these measures to make themselves felt, whereas measures such as raising diesel prices may be expected to have an immediate and negative impact. Even though the economic reform measures themselves may be significant in scale, in the short term, economic growth is likely to continue to plod along slowly.

(Shotaro Kumagai)

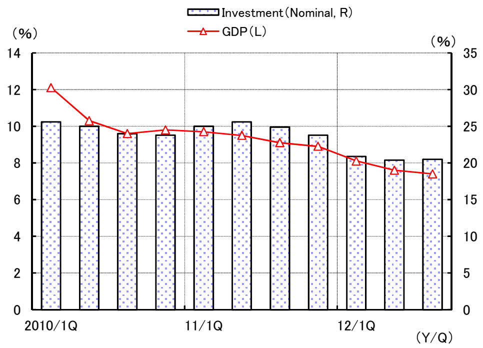
China Economic deceleration may be not for much longer

■ 7.4% growth in July to September

On October 18, the National Bureau of Statistics announced a real GDP growth rate for the period July to September of 7.4%, compared to the same period in the previous year. This was the seventh consecutive quarter that the growth rate has fallen below the previous quarter's figures, and the economy is continuing to run out of steam.

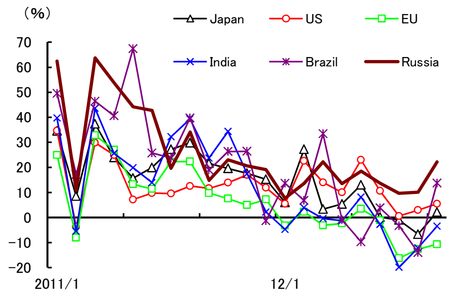
In terms of demand items, the drop in the investment growth rate has been stopped. Investment in fixed assets (excluding rural households) in the period January to September grew 20.5%, compared to the same period in the previous year, more or less the same level as for January to June (20.4%). A more detailed look reveals that the downward trend in real estate development investment growth has begun to brake, and that the margin of negative growth in railway investment is beginning to contract, indicating the beginnings of a rally. Total retail sales of consumer goods maintained 14% growth, compared to the same period in the previous year (14.2% in September, similarly), but the pace of growth has slackened compared with a year ago, or even the beginning of this year.

＜Real GDP, Investment in Fixed Assets＞
(Y o Y)



Note: Nominal Investment figures are year-to-date. The scope was changed as of 2011.
Source: National Bureau of Statistics

＜Exports by Countries and Areas＞
(Y o Y)



Source: Customs Statistics

September's exports grew 9.9%, compared to the same period in the previous year, performing more strongly than in July (1.0%) and August (2.7%). In terms of countries and regions, the contraction of the negative growth margin in exports to the EU and a switch to positive growth in exports to Japan, for example, all point towards a recovery. Also, an examination of import performance in that month shows an overall increase for the first time in two months (up 2.4%, compared to the same period in the previous year), but exports to some countries, like Indonesia and Thailand, contracted by a larger margin than in the previous month. Factoring in elements such as trends in indices for new orders received, etc., the decline does appear to be slowing, but the possibility is strong that the pace of recovery in the months ahead will be pedestrian at best.

■ Economic stimuli also a problem

The government is attempting to stimulate the economy with measures such as accelerating the speed of project approval and expanding financing, and these are expected to be successful in causing the economic growth rate to rally from October to December onwards. However, with respect to some of the economic stimulus measures, questions have been raised and problems pointed out with regard to their effectiveness. For example, from the standpoint of reducing corporate burden, some customs-related tariffs were abolished (including some that are being waived only until the end of the year) from October 1. However, the expected effect is very slight, at just 3.5 billion yuan (according to the government's estimates at the time of announcement), and voices within China are calling for measures that would have a more immediate effect, such as raising the value added tax export rebate rate. Also, though the government is considering extending the household appliances in farming communities program (providing subsidies for purchases of certain electrical household appliances), there is uncertainty as to the value of extending the scheme while the economy is slowing, and some fear a recoil reaction when the scheme comes to an end.

In the runup to the National Congress of the Communist Party of China (November 8), there is little possibility of changes being made to established policies and direction. It is hoped that a smooth transition of leadership will enable the correction of difficulties and problems, and the early development of a stance that will allow the enforcement of appropriate economic stimulus measures.

(Junya Sano)