

# ASIA MONTHLY

## June 2017

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## Topics *Korea's employment environment deteriorating behind the scenes*

While Korea's overall unemployment rate continues to rise at a mild pace, the rise in unemployment among the young and the growth in the number of the long term unemployed indicate that the actual employment environment in Korea is much worse than it would seem. The new administration of Moon Jae-in will need to introduce measures that bear this fact in mind.

### ■ Anxiety over employment environment even as economy recovers

In Korea, the trend of economic recovery is continuing. In spite of growing uncertainty over the future against the backdrop of domestic political turmoil and geopolitical risk, the economy has recently returned to a pattern of export driven growth, and the expectation is that fairly solid growth will continue for the time being.

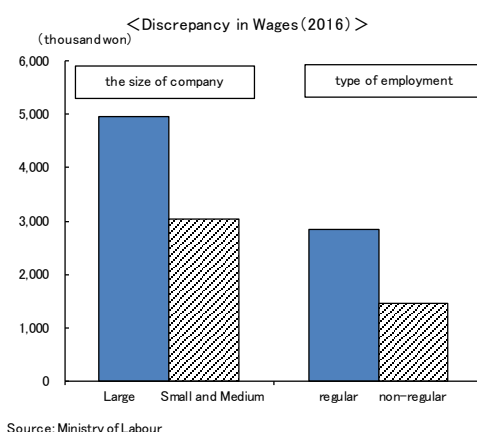
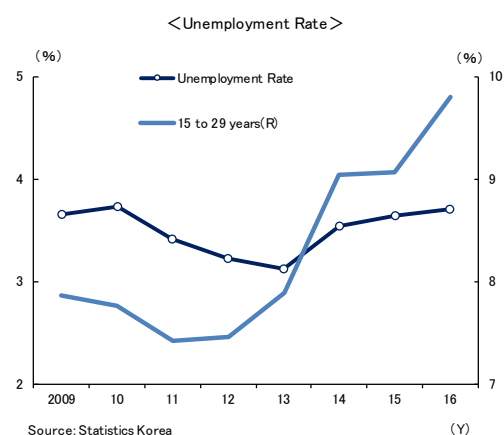
On the other hand, examination of the employment and incomes environments, which are sources of consumption, shows that the unemployment rate for 2016 was 3.7%, only slightly up from the previous year, in spite of the layoffs that were carried out in response to corporate restructuring. Nevertheless, a detailed look at the employment indices shows that the actual employment situation is deteriorating more than the statistics would suggest. In particular, the deterioration is continuing on two fronts.

### ■ Rising unemployment rate among the young

First, there is the rising unemployment rate among the young (15 to 29 years). The unemployment rate among the young in 2016 was 9.8%, a level well above the overall unemployment rate. In 2014, the rate rose suddenly to the 9% range and then continued to rise after that. When compared with 2013, before the rate began its sudden surge, the labor participation rate rose from 43.2% to 46.9%, and the increase in the working population brought about the increase in the number of unemployed. Although certain factors, such as the increase in the number of women seeking work, appear to be among the causes of the rise in the labor participation rate, the increase in the number of young people seeking work, following the economic recovery that has continued since 2013, is another factor, as is the increase in the number of young people seeking work after graduating from high school, as evidenced by the falling university rates. The fact that, although the labor participation rate is going up, the unemployed rate among the young is surging, indicates that there are growing numbers of young people who cannot find work, even if they do enter the labor market.

The backdrop to this is that, in the first place, there are few vacancies. The jobs to applicants ratio is around 6 to 10, meaning that the number of vacancies is seriously short of the number of job seekers. Since 2014, the jobs to applicants ratio has continued to fluctuate up and down and, given the fact that large companies are cutting back on new hires as part of structural adjustment, restructuring is being carried out in shipbuilding and marine transportation, and many companies are downsizing unprofitable sections in pursuit of greater efficiency, there is little prospect of an early improvement in the labor supply and demand situation.

In addition, employment mismatching is getting worse. In Korea in recent years, while job seekers tend to concentrate on large companies and others with good employment conditions, large companies are relocating offices as part of the advance of structural adjustment and globalization, causing the number of new hires to decrease. At the same time, small and medium sized enterprises continue to suffer from a chronic labor shortage. Part of the reason for this is the considerable discrepancy in wages between large and small and medium sized companies. The average monthly wage for small and medium sized companies in 2016 was 3.05 million won, only about 60% of the 4.97 million won per month paid by large companies. In addition, there is a strong tendency for job seekers to try to avoid non-regular



employment. The wages for non-regular work are half those for regular work, and the conditions are not as good. For that reason, even when people are looking for work, there is a growing number of unemployed people who will actually choose not to work, if the only jobs they can find are low-paying ones. In addition, with the raising of the retirement age, it is possible that employment opportunities for the young are being absorbed by older workers.

As a result, there is a continuing trend for the number of unemployed who have no work experience at all to increase, generally among the young. As of March, 2017, the number stood at 144,000 people, its highest level ever. Unemployed people with no work experience find it more difficult to find jobs than those who have some work experience, and there is a strong possibility that they will join the ranks of the long term unemployed, as mentioned below. The deterioration of the employment situation among the young has the potential to intensify feelings of dissatisfaction against the government and businesses.

**Some people leaving the labor market**

Second, there is the change in the “characteristics” of the unemployed. In recent years, there has been a rapid increase in the number of long term unemployed, that portion of the labor force unable to find employment for six months or longer. The number now accounts for 13.1% of the unemployed, the highest level since 2002. In addition to the failure of labor demand to improve, it is also possible that, as businesses tighten their hiring criteria, there is a stronger preference to select from among the short term unemployed. If this kind of situation continues, where people cannot find work even over an extended period of time, there is a danger that the lack of experience will further restrict their employment opportunities.

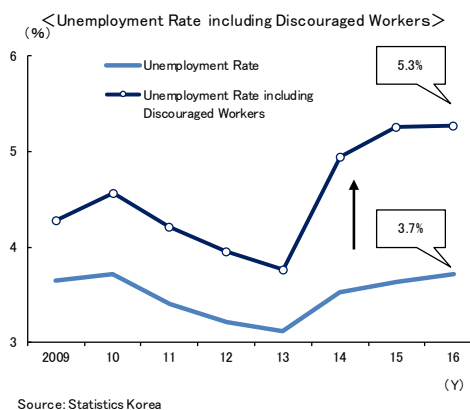
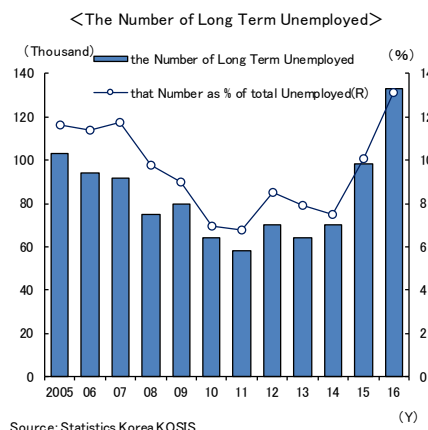
In fact, in recent times there has been an increase in the number of discouraged workers and they have become part of the non-working population. This number was an average of 518,000 in the period January to March of 2017, its highest level ever. Given the increase in the labor participation rate among the young, and the growth in the non-working population among those educated to university level or higher, there is a possibility that those in the 30 and over age group, who find it difficult to change jobs, are now leaving the labor market. Given that they are the parenting generations, the potential impact on consumption cannot be ignored.

Furthermore, should discouraged workers begin job hunting again at some later date, this could have the effect of pushing up the unemployment rate. If these discouraged workers are considered the latent unemployed, and the unemployment rate is calculated to reflect this, then it comes out at 5.3% for 2016, 1.6% points higher than the official figure (3.7%).

**Addressing employment issues is an imperative for the new government**

As discussed, the changing characteristics of the unemployed, and the increase in the number of those who are no longer looking for employment and are not included in unemployment statistics, suggest that the actual employment situation is worse than it would appear to be. Even though the ageing of society in Korea is accelerating, the desire of young people to work is not currently being fully leveraged. In addition, the inability to find work over a protracted period of time may well lead to income instability among the parenting generations. If these issues are not addressed, it is anticipated that the danger will not only be a loss of growth strength in the mid to long term, but that there is an intensifying risk of increased social instability. The new administration will be expected to do more than simply promote policies for employment creation, but also to implement growth strategies that take the entirety of employment related problems into account, and to radically reform the labor market.

(Kentaro Matsuda)



## Indonesia Economy seesawing

### ■ 5.0% growth in Q1

Indonesia's economy continues to seesaw, despite having managed, in mid-2015, to brake the deceleration that had continued until then. Real GDP grew 5.0%, compared to the same period in the previous year, in the January to March quarter of 2017, scarcely changed from the previous period (4.9%, similarly).

A detailed look at the January to March quarter shows that, in addition to robust private consumption and investment growth, expanded exports and government consumption also helped to support the economy. Against a backdrop of economic improvement in China, Japan and the ASEAN countries, there was expanded growth in exports of petroleum and other natural resources, and of automobiles, etc.

In addition, government consumption also rallied. With the cabinet reshuffle of July, 2016, Sri Mulyani, a proponent of the importance of financial soundness, was appointed Finance Minister and, after having been subject to scrutiny, government expenditure fell below the previous year's levels throughout the latter half of 2016. However, after the normalization of budget implementation from the start of the new budget year, government expenditure reverted to 2.7% year on year expansion.

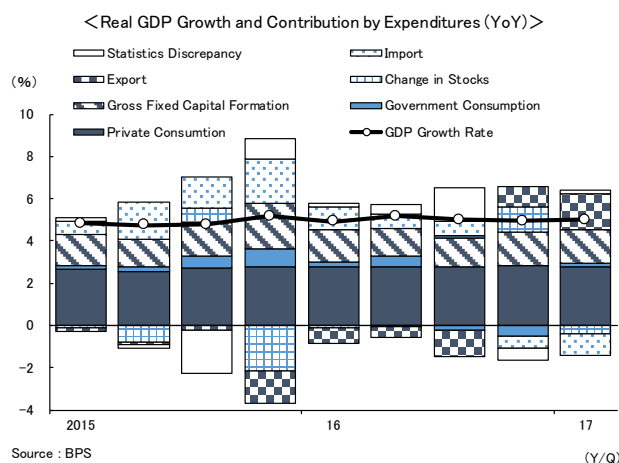
Looking ahead to the latter half of 2017, Indonesia's economy is expected to continue to recover at just over 5.0%. First, exports are expected to continue to increase as the global economy continues its gradual recovery. Also, with the progress of infrastructure projects and other public works, gross fixed capital formation will likely continue to grow steadily. However, there is little hope for faster growth in consumption. As US interest rates continue to rise, the weak rupiah will cause inflationary pressure to intensify, and this and other factors are thought likely to hinder consumption activity.

### ■ Tax amnesty puts finances on road to improvement

One important point when considering Indonesia's economy in the mid-term is finance. It has long been pointed out that Indonesia needs fiscal expenditure on infrastructure development and the nurturing of human capital. However, the government lacks sufficient income, due to low tax collection rates and other factors, and the fiscal deficit has continued to swell.

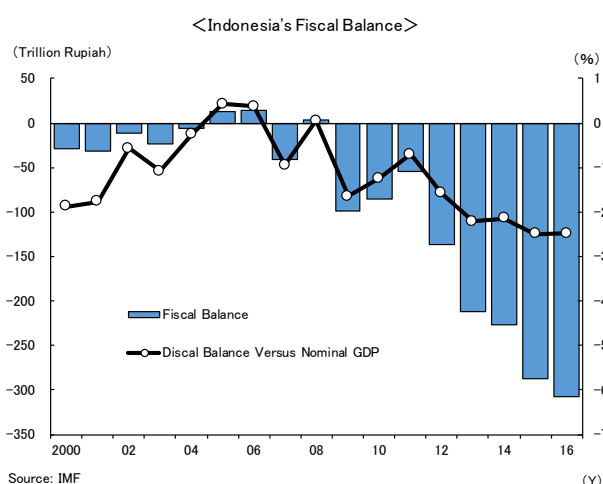
Under these circumstances, the Indonesian government implemented a tax amnesty from July, 2016, to March, 2017, in order to try to shrink the fiscal deficit by increasing tax collection revenue. The tax amnesty is a system whereby, if all hidden assets, at home or abroad, are declared honestly, then a low tax is applied to them, and punitive measures waived. The tax amnesty netted 135 trillion rupiah in additional tax revenues, falling short of the government's target (165 rupiah), but accounting for 44% of the fiscal deficit for 2016. In addition, the value of assets declared was around 4,800 trillion rupiah, above the government's target (4,000 trillion rupiah). This is the equivalent of about 40% of nominal GDP. The essence of the tax amnesty, rather than simply netting extra tax revenue through increased tax collection, was to expand the tax base. This latest implementation of the amnesty appears to have been a success in that respect. The challenge going forward will be whether these results can translate into stable tax revenues in the future.

(Yuta Tsukada)



Source : BPS

(Y/Q)



Source : IMF

(Y)

## India Impact of demonetization of high denomination banknotes waning gradually

### ■ Household and corporate sectors improving

Though India's sudden demonetization of high denomination banknotes last November caused a temporary economic slowdown, the economy has recently changed to a tone of recovery.

Examination of recent automobile sales figures shows that sales of passenger cars, mainly in the cities, grew a steady 10.0% compared to the same period in the previous year (and the same below), while sales of two wheeled vehicles, mainly in agricultural communities where the impact of the lack of cash was strongly felt, also recovered to levels exceeding those of the previous year. Though negative effects persist in sectors where accurate statistics cannot be captured, such as micro enterprises and one man businesses, the cash distribution volume has picked up again after bottoming out in December, and private sector consumption is expected to be able to maintain its trend of recovery in the months ahead.

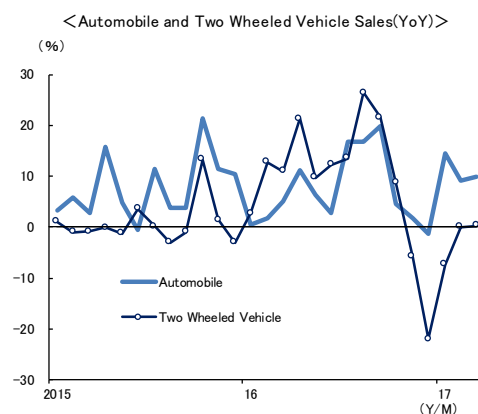
These kinds of improvements are also being observed in the corporate sector. Though February's manufacturing industry production slowed by a small margin to 1.4% growth, the purchasing managers' index in the manufacturing industry recovered to mid 2016 levels. Also, in the service industry, which had been in a noticeable slump, the index passed the watershed 50 mark. In addition, there has been increased expansion in export growth recently. Exports grew 27.6% in March, the highest level of growth since October, 2011. Though exports account for only 19% of GDP, the recent economic recovery in industrialized and other nations has provided something of a tailwind. Following this recovery in domestic and foreign demand, the corporate sector looks to be gradually recovering its strength. Further, the negative growth of capital goods production, which serves as a future indicator of plant and equipment investment, has contracted significantly. The expectation is that economic growth, until now largely driven by private sector consumption, will get a growth boost from the corporate sector.

### ■ Reserve Bank of India prioritizes price stability

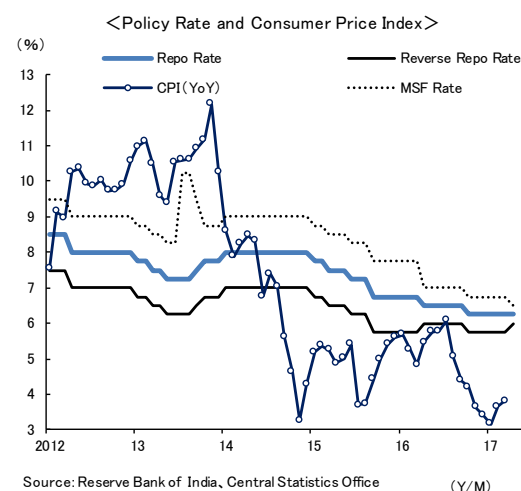
At the April meeting of Reserve Bank, while it was decided to keep the repo rate, Reserve Bank's policy interest rate, unchanged at 6.25%, the reverse repo rate was raised by 0.25% points, and the MSF interest rate lowered by 0.25%. These actions are thought to have been in an attempt to absorb excess liquidity in response to the falling interbank interest rates that resulted from increased bank deposits in the wake of the demonetization of high denomination notes.

Further, the rate of increase of the CPI was 3.9% in March, increasing from the previous month, and with future increases in civil servants' salaries and the introduction of GST, prices may well increase at a faster pace for a time. In response to this situation, in February, Reserve Bank changed its stance on monetary policy from easy to neutral. Given the fact that the Bank did not lower the policy interest rate at the time of the confusion following demonetization, out of concern over possible inflation, it is anticipated that, depending on how prices trend, interest rates may well be raised in the future.

(Kentaro Matsuda)



Source: Society of Indian Automobile Manufacturers



Source: Reserve Bank of India, Central Statistics Office

## China Trade continues recovering

### Exports and imports recovering since the start of 2017

Though China's trade figures faced tough conditions for two consecutive years, with both exports and imports falling below the previous year's levels in 2015 and 2016, they have been improving since the start of 2017.

In terms of exports, excluding February where there was a temporary slump due to the Lunar New Year holiday, they appear to have broken free from negative growth. Exports grew 16.4% in March, compared to the same month in the previous year, posting double digit growth. Though April's growth slowed slightly in comparison with March, at 8.0%, similarly, the trend of recovery continued. In terms of individual countries and regions, including the US, China's biggest export destination, exports to the majority of countries and regions have revived to increased growth.

Meanwhile, import growth also is continuing to improve, posting 11.9% in April, compared to the same period in the previous year, despite a sluggish pace of recovery after peaking in February. The rise in the global prices of crude oil and iron ore may be considered one factor behind this. However, the driving force behind the recovery has been the expansion of infrastructure investment and the recovery in industrial production.

With regard to the balance of trade, the surplus growth has contracted from the same period in the previous year, but still continues to grow at a high level. In particular, China's trade deficit with the US is noticeably high and, depending on the trade policies of the Trump administration, may well become the focus of trade friction between the US and China.

### New policies contributing to trade expansion

Looking ahead to the future of exports and imports, against the backdrop of economic recovery in the US and new emerging economies, it is expected that a modest acceleration in growth will continue. Under these circumstances, in April the Chinese government brought out two policies in quick succession that were designed to contribute to the expansion of trade.

First was the expanded establishment of new free trade zones. The free trade zones, where there are very few regulations restricting corporate activities, are expected to provide a booster effect to trade and direct inward investment. Only four such free trade zones had been established as of March, 2017, with all of them sited in coastal provinces and municipalities. In this most recent move, seven new zones were opened up all at one time, with one sited in Zhejiang province and the remaining six in mid-western and north-eastern (Liaoning province) regions.

Second was the announcement of the "Mid-and-Long Term Development Plan of the Auto Industry". The plan calls for intensive focus on the penetration of new energy vehicles, in order to improve the competitive strength of the industry, and may be said to be a policy that will contribute mainly to export expansion. Meanwhile, the plan also includes the policy of "a step by step relaxation of joint venture company investment ratio restrictions". If this is implemented, it will make it possible for foreign companies to take the initiative in the management of these companies (they are currently limited to 50% control), and there will likely be an increase in the import of automobile parts and components and production equipment by foreign manufacturers.

These policies are believed to be aimed at alleviating the criticisms that China's markets are too closed, and are also seen as being indispensable for the upgrading of China's industries and the sustaining of long term growth. However, there is expected to be a strong backlash from local industries that have been protected by restrictions on market participation, and it is as yet impossible to predict to what extent these policies can be implemented.

(Junya Sano)

