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Asia: Headwinds for China are intensifying ahead of "Trump 2.0"

In contrast to China, which faces increasing headwinds due to such factors as tariff hikes, other Asian economies will benefit from tailwinds such as the relocation of production from China. However, the policies that the incoming Trump administration will adopt are impossible to predict, and there is a risk of an across-the-board deterioration in the economies of Asia.

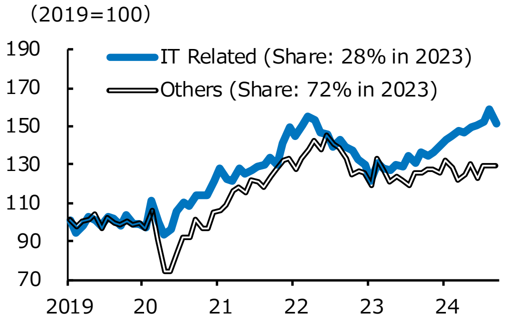
1. As China's economy stalls, other Asian economies aim to reap rewards from U.S.-China squabbles.

(1) With the exception of China, Asian economies have generally been strong in 2024

In 2024, there has been a disparity in economic performance between China and other Asian countries/territories (hereafter, "other Asian economies"). China's economy remains in a difficult phase. At the beginning of the year, sectors such as domestic tourism and eating out, which had been sluggish due to the COVID pandemic, saw recoveries, and exports of new-energy products such as electric vehicles (EVs) increased significantly, but the Chinese economy slowed in the second half of the year, and the slump in the real-estate market and waning consumer confidence pushed down domestic demand.

In contrast to China, other Asian economies continued to recover. Background factors included 1) a resurgence in IT-related exports, 2) an acceleration in the relocation of production from China, and 3) an easing of inflationary pressures. Demand for AI-related semiconductors and electrical products has been rising worldwide, and related capital investment has also been strong. As a result, IT-related exports from Asia have been increasing. Amid the growing trend of moving away from dependence on China, the transfer of production, mainly to Vietnam and Taiwan, has also been boosting exports. Inflationary pressures in these economies have also been subsiding, and inflation rates have fallen back to pre-pandemic levels in most of the countries/territories. Households' purchasing power has been recovering as inflationary pressures abate, and this is supporting personal consumption.

<Exports of Asia ex Japan/China>
(USD, SA)



Source: JRI based on CEIC
Note: IT related producsts include semiconductors and electric products.

The growth rate of Asia as a whole is expected to be +5.4% in 2024, unchanged from +5.4% in 2023. This is a slight upward revision from the forecast made in July (+5.3%). The growth rates of Taiwan, which is strong in IT-related industries, and Malaysia were revised upward to +4.1% (July forecast: +3.6%) and +5.3% (+4.5%), respectively. The forecasts for Indonesia and India remain +5.0% and +7.8%, respectively, unchanged from July. Both economies remain resilient, so growth is expected to be in line with the earlier forecasts. China, however, having announced economic stimulus measures in the second half of the year, looks set to see growth for the full year of 2024 of +4.8% (+4.7%), barely surpassing the government's target (around +5%) and slowing from the previous year (+5.2%).

(2) Trump's re-election will create even more challenges for the Chinese economy

In 2025, the trade policy of the incoming Trump administration is likely to have a significant impact on the Asian economy. The economic gap between China and other Asian economies is expected to widen further. Mr. Trump has long vowed to implement radical policies, centered on tariff hikes. As was the case during his first term in 2017-21, his administration will probably use tariffs as leverage in foreign-policy negotiations. Mr. Trump is likely to present a particularly hardline stance toward China, using the threat of tariffs to gain an advantage in trade negotiations.

If the U.S. raises tariffs on imports from China to 60%, as Mr. Trump has promised, this would put strong downward pressure on the Chinese economy. Estimates indicate that the measure would likely reduce China's real GDP growth rate by 1.0 percentage points, which would be larger than the push-down effect on U.S. real GDP growth of -0.3 points and on average global real GDP growth of -0.2 points. As a result, China's share of U.S. imports would plummet from 21.5% in 2015 to around 10% in 2025. In other Asian economies, however, growth rates would be pushed up through export circumvention or substitution, as well as the relocation of production facilities from China. The tariff hike would boost Vietnam's real GDP growth rate by 2.1 points and also have a small positive impact on the Taiwanese (+0.5 points), Thai (+0.3 points), and Malaysian (+0.2 points) economies. In response to the recent U.S.-China confrontation, multinational companies have tended to choose other Asian economies as alternative production locations. Already, imports from other Asian economies are accounting for an increasing share of U.S. imports, and this trend would likely be further cemented by higher tariffs on Chinese imports.

In China, in response to its floundering economy, the government has announced an aggressive package of measures. At a Politburo meeting at the end of July 2024, it was emphasized that the focus would be on expanding domestic demand, and hints were given that measures to shore up the economy would be expanded. In September, the People's Bank of China announced a wide range of measures for monetary easing and supporting the real-estate market.

However, these measures are small in scale, and unlikely to deliver a full-fledged economic recovery. Measures to stimulate consumption, such as incentives for replacing older cars with new energy vehicles, also remain piecemeal. In November, a massive local-government debt refinancing program worth 10 trillion yuan was announced, but because it only involves replacing "hidden debt," such as that on the books of local-government financing vehicles (LGFVs), with local government bonds, the direct impact on the economy will be small. Since interest rates on local government bonds are lower than those of LGFV debt, the program will reduce interest payments (by about 600 billion yuan over five years), but any boost to investment and consumption from this will be limited.

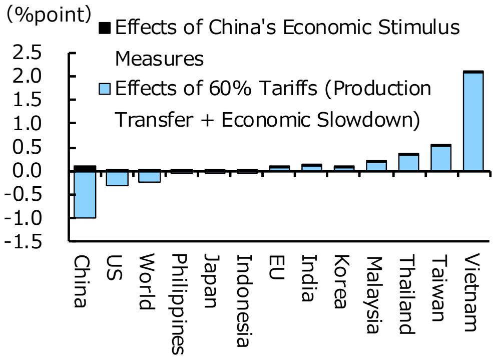
Considering the above, the economic growth rate of Asia as a whole is expected to be +5.0% in 2025, lower than the rate of growth in 2024. This is partly because India's growth will return to a more moderate pace, having hovered around +8% during the rebound following the pandemic. In addition, the Chinese economy is expected to slow, with growth expected

＜Trump's Claims in The Media＞

Sanctions against China	(1) Imposition of tariffs exceeding 60% on imports from China
	(2) Elimination of China's Most Favoured Nation (MFN) treatment
	(3) Impose 100% tariffs on autos made in Mexico by Chinese manufacturers
Others (Mainly Negative Effects on The Rest of Asia)	(4) Install a blanket tariff of 10% to 20% on all imports
	(5) Emphasis on the USMCA, which substituted NAFTA
	(6) Withdrawal from IPEF
	(7) Reduce or scrap the Inflation Reduction Act (IRA)
	(8) Curtail CHIPS Act funding
	(9) Call on Japan, Korea, Taiwan to increase defense spending

Source: JRI based on various media reports

＜Effects of China's Economic Stimulus Measures and Trump's Tariffs : Impact on GDP＞



Source: JRI estimates based on OECD

＜Asia Economic Forecasts＞

(%)

	2022	2023	2024 F	2025 F	2026 F
Asia	**4.2**	**5.4**	**5.4**	**5.0**	**5.0**
Northeast Asia	2.8	4.7	4.5	4.3	4.1
China	3.0	5.2	4.8	4.6	4.4
Korea	2.6	1.4	2.3	2.3	2.1
Taiwan	2.6	1.3	4.1	3.0	2.7
Hong Kong	-3.7	3.3	2.6	2.4	2.2
ASEAN 5	6.0	4.4	5.0	4.9	5.1
Indonesia	5.3	5.0	5.0	4.8	4.8
Malaysia	8.9	3.6	5.3	5.0	5.1
Philippines	7.6	5.5	6.0	5.8	5.9
Thailand	2.5	1.9	2.9	3.0	2.9
Vietnam	8.1	5.0	6.5	6.6	7.2
India (FY)	7.0	8.2	7.8	6.9	7.2

Source: JRI estimates based on various statistics to slip to +4.6% in 2025 and +4.4% in 2026. On the other hand, Taiwan (+3.0%) and Malaysia (+5.0%) are expected to achieve high growth in 2025, on par with before the pandemic, as they enjoy an economic boost from the relocation of production.

2. An economic downturn in China and broad adverse impacts from "Trump 2.0" pose risks.

The main scenario for Asia in 2025 is that China's economy stalls and other Asian economies do well by reaping rewards from U.S.-China squabbles. Risks to such a scenario include a significant downturn in the Chinese economy and broad adverse impacts from Trump 2.0.

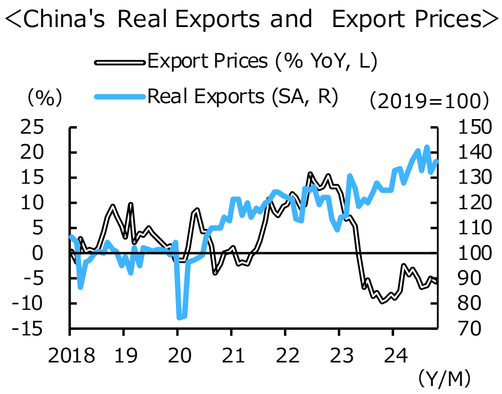
(1) Economic downturn in China: Caution is required about the real-estate market correction and excessive competition

In China, there is a risk that the economy will deteriorate at an accelerated pace due to worsening structural problems. While additional fiscal stimulus may be announced at the National People's Congress in March 2025, its impact on the economy will probably only partially offset the negative effects of U.S. policy toward China. And if the ongoing correction in the real-estate market and slump in consumption become more serious, there is a possibility that the Chinese economy will deteriorate and that the negative effects of that will spill over to impact the economy of Asia as a whole.

Source: JRI based on CEIC

China's property market remains in a deep correction phase. The root of the problem is excess housing supply, and housing investment has been in freefall. In May 2024 the Chinese government responded by announcing measures to dispose of housing inventory. The plan is for the People's Bank of China to lend local governments 300 billion yuan to buy housing inventory and convert it into homes for low-income people. However, not only is the amount of the loans small, but local governments are reluctant to purchase housing stock because they are likely to incur losses when they resell it. As a result, little housing inventory has been purchased, and the prospect of a big increase in the future is unlikely. If the real-estate market adjustment becomes prolonged, the financial situations of related companies and financial institutions could deteriorate, leading to a decline in financial intermediary functions and turmoil in financial markets. There is therefore a risk of the interplay between the economy and the financial system dealing China a crippling economic blow.

In China, households' restraint in consumption has become more serious, and the deflationary trend is strengthening. As price competition in China has become fiercer, Chinese companies have been looking to export as a way of maintaining their earnings, a situation that has led to the "export of deflation" to the rest of the world. This trend has also been spurred by the Chinese government's aim of expanding the country's global market share in strategic fields such as new-energy products. Criticism of China's export offensive has been widespread in developed countries, and China is dealing with trade tensions with a wide range of countries/territories.

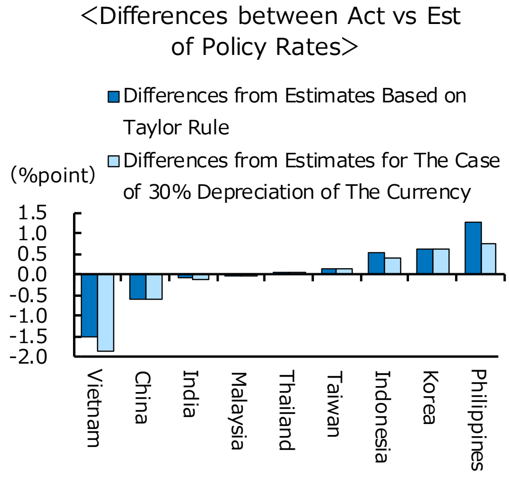


Source: JRI based on CEIC and CPB

As domestic consumption continues to stagnate, Chinese companies are being forced to fight a war of attrition due to price competition of their own making, and corporate bankruptcies are on the rise. If it becomes difficult for companies to tap foreign demand in the future, corporate bankruptcies may accelerate and the Chinese economy could deteriorate rapidly.

(2) "Trump 2.0" could also have an adverse impact on Asia ex. China

Attention also needs to be paid to the risk that damage caused by the policies of the incoming Trump administration extends beyond China's economy to encompass Asia as a whole. This could occur via three routes: 1) destabilization of foreign exchange markets, 2) economic sanctions, and 3) increased dependence on China.



Source: JRI estimates based on CEIC

The first route is through the destabilization of foreign exchange markets. Many of President-elect Trump's policies are expected to lead to inflation, and the rate cutting by the Federal Reserve Board may be halted sooner or later. If U.S. interest rates remain high, funds will likely flow out of the financial markets in Asian economies, increasing downward pressure on their currencies. When Mr. Trump took office the last time, the currencies of economies with issues such as current account deficits that made them vulnerable to external shocks, such as Indonesia, India, and the Philippines, fell sharply. Central banks in Asian economies have a strong tendency to take account of currency movements when making monetary policy decisions, and they are likely to hesitate to cut interest rates if exchange rate volatility increases. In the Philippines, Korea, and Indonesia, in particular, policy interest rates are higher than conditions in the real economy would warrant, and these high rates could pile heavy downward pressure on these country's economies. Conversely, in Vietnam, where the policy rate is low in relation to real economic conditions, currency depreciation could lead to the rate being raised.

The second route is through economic sanctions imposed by the U.S. In other Asian economies, trade surpluses with the U.S. have been expanding. There is a possibility that Mr. Trump will take issue with this and impose punitive tariffs. In fact, he has hinted at the introduction of a "universal baseline tariff," i.e., a flat tariff of 10-20% on all imports, from wherever they are in the world. The Biden administration advocated "friend-shoring," declaring its intention to reorganize supply chains to favor friendly countries, while also utilizing frameworks such as the IPEF. In other words, whereas the Biden administration clearly positioned other Asian economies as friendly countries, Mr. Trump emphasizes bilateral deals and has a disdain for multilateral frameworks. The incoming Trump administration is likely to withdraw from the IPEF, which will dampen moves to relocate production. Moreover, in the U.S. Treasury Department's foreign exchange report released in November, many Asian countries/territories (Japan, China, Korea, Taiwan, Singapore, and Vietnam) were on the Monitoring List for currency manipulation. Issues like this mean that there is a danger that the U.S. will also ramp up pressure on economies other than China.

The third route is through increased dependence on China. If Mr. Trump opts for a strong version of the "America First" policy, Asian economies such as the ASEAN countries and India will have no choice but to become more reliant on China. Thailand and Indonesia, for example, have already become more positive about accepting investment from Chinese EV manufacturers. Looking ahead, if they become unable to count on heavy investment from U.S. companies, they may become even more enthusiastic about welcoming Chinese capital instead. In India, too, there are growing calls to accept investment from China as a way to strengthen the manufacturing sector. As ASEAN countries and India become more dependent on China, friction with the U.S. and other developed countries, which harbor growing concerns about China from an economic security standpoint, is expected to intensify. Furthermore, in the ASEAN zone, China is expanding its share of the markets for EVs and various other goods. It is essential to keep in mind that China is employing so-called "economic statecraft" to increase geopolitical threats.

(Minoru Nogimori)

NIEs Semiconductors boost growth, but U.S.-China tensions threaten

■ Semiconductor exports are driving economic recoveries

In general, the NIEs (Korea, Taiwan, and Hong Kong) are experiencing economic recoveries. For the full year of 2024, the NIEs are expected to grow by 2.9%, accelerating from +1.6% in 2023. Exports of semiconductors and other IT-related products are especially strong, which is driving the economic recovery. According to WSTS (World Semiconductor Trade Statistics), global semiconductor sales growth jumped to +23.3% YoY in September. In Hong Kong, however, the economy is losing steam in response to the slowdown in the economy of mainland China, with which Hong Kong has close economic relations.

<NIEs (Korea, Taiwan, Hong Kong) Growth Rate Forecasts>

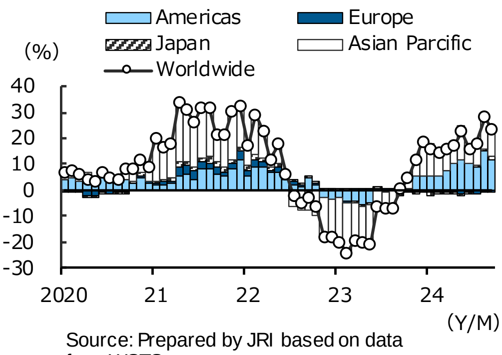
(%)

	2021	2022	2023	2024 F	2025 F	2026 F
NIEs	5.3	2.0	1.6	2.9	2.5	2.3
Korea	4.3	2.6	1.4	2.3	2.3	2.1
Taiwan	6.6	2.6	1.3	4.1	3.0	2.7
Hong Kong	6.5	-3.7	3.3	2.6	2.4	2.2

Source: Prepared by JRI based on data from national statistical bureaus, central banks, and the IMF

Real GDP growth in 2025 is projected to be +2.5% for the NIEs as a whole. In Hong Kong, growth is expected to be weak due to the slowdown in mainland China, but the economies of Korea and Taiwan are expected to see robust recoveries. Global demand for products for generative AI and data centers should continue to grow, and this will drive exports from the NIEs. In addition, the incoming Trump administration in the U.S. is expected to raise tariffs on Chinese goods to 60%, which will lead to the NIEs substituting China as production bases, boosting the growth rates of the former. Among the NIEs, Taiwan ought to do especially well from the higher tariffs on Chinese goods as production facilities are relocated from China to Taiwan.

<Total Semiconductor Revenues (YoY)>



Source: Prepared by JRI based on data from WSTS

However, depending on the policies adopted by the incoming Trump administration, the economies of Korea and Taiwan could also deteriorate. For example, if the U.S. government introduces a "universal baseline tariff," the export sectors in all the NIEs would be more likely to incur damage. And if the U.S. and China tighten restrictions on each other's semiconductors and other products in a tit-for-tat fashion, exports to the U.S. from Korea and Taiwan could also decrease. Moreover, in the U.S. Treasury Department's foreign exchange report, Taiwan and Korea are on the Monitoring List for currency manipulation. If they are ultimately recognized as currency manipulators, they may become subject to U.S. penalties such as higher tariffs. In Hong Kong, uncertainty about the business environment is increasing due to the U.S.-China rivalry, and there is a possibility that the economy there will weaken as more companies pull out.

Political and diplomatic factors also pose downside risks to the NIEs. In Korea, political turmoil is increasing the downward risks to the economy after President Yoon was impeached by the National Assembly. Escalating military tensions on the Korean Peninsula could also destabilize the Korean economy. In Taiwan as well, cross-strait relations have rapidly deteriorated, potentially subjecting the island to increased military pressure. Such risks could encourage the curtailment of corporate production and investment activity in Taiwan, causing the economy to worsen.

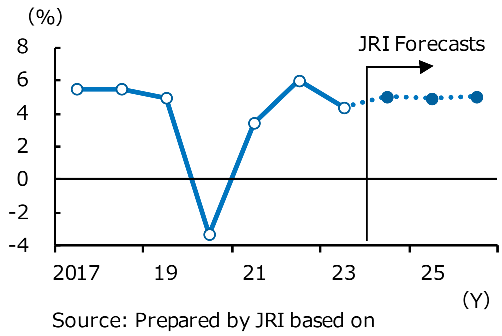
(Wu Zijing)

ASEAN5 *The pace of economic recovery will vary in each country*

■ Growth in 2025 is expected to be more or less unchanged at around +5%

In the ASEAN5 (Indonesia, Malaysia, Philippines, Thailand, and Vietnam), real GDP growth is expected to have accelerated to +5.0% in 2024, up from +4.4% in 2023. Background factors include increasing moves to transfer production from China and circumvent controls on exports for China, as well as rising exports and inward direct investment due to an upturn in the IT cycle. The boost to growth rates in Vietnam and Malaysia, which are highly dependent on exports, is particularly strong. On the other hand, domestic demand seems to be running out of steam in some countries. Specifically, domestic demand has been sapped in Indonesia and the Philippines, where soaring food prices have pushed up inflation and interest rates have remained high.

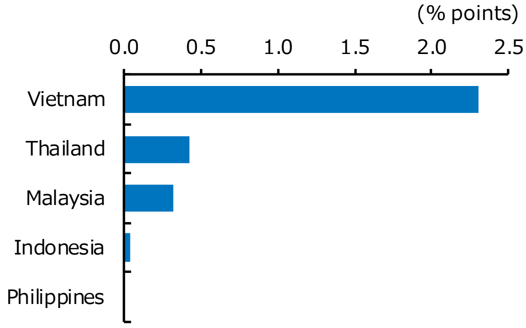
<ASEAN5 Real GDP Growth Rate>



Source: Prepared by JRI based on statistics from each country

In 2025, real GDP growth is projected to be +4.9% for the ASEAN5 as a whole, more or less unchanged from 2024. However, the momentum of economic recovery is expected to vary from country to country. The main reason for this will be the increase in tariffs on China by the incoming Trump administration. This policy will have both positive and negative effects on the ASEAN economy. As a positive impact, ASEAN can be expected to replace the decline in China's exports to the U.S. Production/export facilities will be relocated to the ASEAN zone from China, boosting the bloc's economy. On the other hand, negative impacts for ASEAN include 1) a decline in exports to China due to the deterioration of the Chinese economy, 2) pressure to reduce production due to an influx of cheap products from China, and 3) currency depreciation due to higher U.S. interest rates. In Vietnam, Thailand, and Malaysia, which are popular destinations for the relocation of production from China, the positive effects will be significant, and the pace of economic recovery is expected to be rapid. In the Philippines and Indonesia, however, the negative effects will be significant, as compounding a decline in exports to China, a resurgence of inflation and continued high policy interest rates due to currency depreciation will likely exert downward pressure on their economies.

<Production Relocation Effects of Tariff Hikes on China (Impact on GDP) >



Source: Prepared by JRI based on data from OECD, CEIC, etc.

With global uncertainty increasing ahead of the return of Mr. Trump to the presidency, the ASEAN economy faces risks on both the upside and downside. Downside risks include 1) the introduction of a "universal baseline tariff" by the U.S. and 2) a further deterioration in the Chinese economy due to a deepening of the real-estate recession. If the tariff is introduced, there is a risk of exports from Vietnam and Thailand, which are highly dependent on the U.S., being depressed significantly. And if the Chinese economy worsens, exports from Indonesia, which is heavily reliant on China, will slump, while in other countries inbound demand will be pushed down due to a decrease in numbers of Chinese tourists. Upside risks, meanwhile, include a potential upturn in the Chinese economy due to aggressive fiscal stimulus. If this happens, it could be expected to boost goods exports, especially from Vietnam and Indonesia, which are big exporters to China, and boost inbound demand across the ASEAN zone.

(Kazushi Morita)

India Stable growth is continuing but manufacturing remains a challenge

■ Both domestic and foreign demand are strong in FY2024

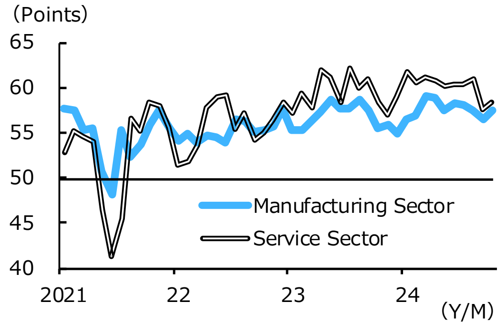
India's economy has been expanding steadily. Business confidence among companies is improving, and the PMI (purchasing managers' index) remains above the 50-point borderline between economic expansion and contraction in both the manufacturing and service sectors. Consumer sentiment among households is also improving, with the consumer confidence index reaching 94.7 in September 2024, well above the monthly average of 88.8 recorded in 2023.

On the domestic demand front, favorable employment conditions have been supporting growth in personal consumption. The urban unemployment rate in the July-September quarter was 6.4%, lower than it was before the pandemic (December 2019: 7.9%). The number of employees enrolled in the Employees' Provident Fund (EPF), a government-run pension scheme, also rose by 1.85 million in August, a significantly higher margin of increase than the 1.14 million rise recorded in the same month last year. In India, employees working in establishments above a certain size are required to join the EPF, so the increase in the number of enrollees indicates that employment is expanding steadily.

As for external demand, exports of services, including IT and business process outsourcing (BPO), increased by 12.2% year over year (YoY) in the July-September quarter, up from +9.8% YoY in April-June.

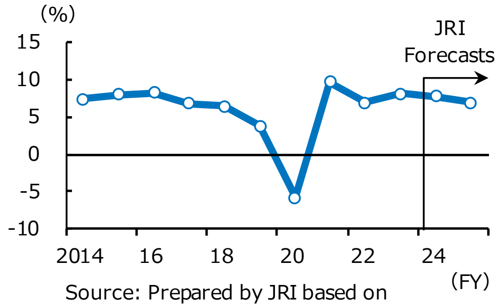
Real GDP growth in FY2024 is expected to be +7.8%, maintaining the roaring growth recorded in FY2023 (+8.2%). The economy should also remain strong in the second half of the fiscal year, in terms of both domestic and foreign demand. On the external demand side, service exports are expected to continue their rapid rise, reflecting the global digitalization trend. Regarding domestic demand, lower inflation should support expansion. Although consumer price inflation accelerated to 6.2% in October from 5.5% in September due to higher prices of food prices, which accounts for a large share of the consumer price index (CPI), the Reserve Bank of India expects inflation to fall back to the 4% level in the second half of the year on the back of a recovery in grain production.

<PMI (Purchasing Managers' Index) >



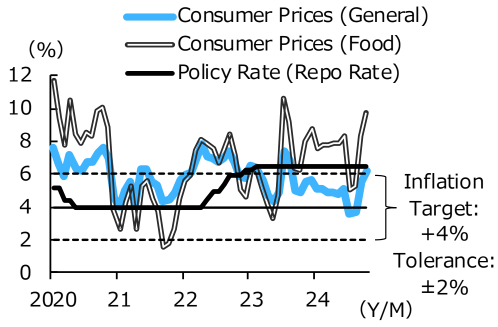
Source: Prepared by JRI based on data from S&P Global

<India Real GDP Growth Rate (YoY) >



Source: Prepared by JRI based on data from CEIC

<Inflation Rate and Policy Interest Rate>



Source: Prepared by JRI based on data from CEIC

■ Growth will continue in FY2025, led by foreign demand

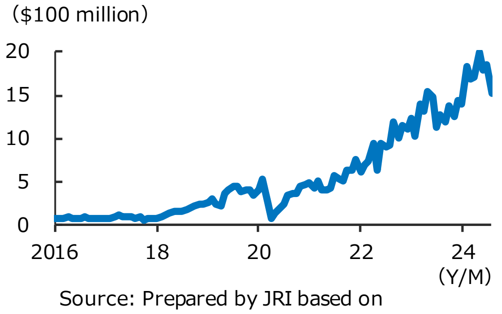
Real GDP growth in FY2025 is expected to slow compared to FY2024 to +6.9%, which will mean that stable growth on par with pre-pandemic levels will be maintained. The economic driver will be foreign demand. Services exports will continue their rapid rise, and goods export growth also looks likely to gain momentum. One of the reasons for this is that the incoming Trump administration in the U.S. is expected to implement hardline measures against China, including tariff hikes. Global companies are likely to move production out of China, and India is a strong candidate. In addition to its abundant labor force, India is a democratic nation that has friendly relations with Western countries, making it a highly attractive destination for relocation. In India, production has already been transferred from China in some areas, such as mobile phones. As a result, exports are also increasing, and the value of mobile phone exports has risen more than tenfold in a decade. Going forward, a similar trend is likely to be seen in fields where the manufacturing process is relatively simple, which should lead to further increases in exports.

India's likely escape from U.S. sanctions will also boost its exports. The incoming Trump administration will be positioning the U.S. trade deficit as a key issue, and may impose sanctions on countries with which the U.S. runs large deficits. India's share of the U.S. trade deficit is smaller than those of neighboring Canada and Mexico, the ASEAN countries, Korea, and Taiwan, and India is absent from the Monitoring List for currency manipulation in the U.S. Treasury Department's foreign exchange report.

With regard to domestic demand, the pace of increase is expected to slow overall, as while an expansion in fiscal expenditure will stimulate demand, the effects of tighter monetary policy will become pervasive. Looking at fiscal policy, in the FY2024 budget, which was reworked after the Lok Sabha (lower house) general election, the figure for infrastructure investment was much higher than in the previous year. It also included support for middle- and low-income groups, such as a job creation package worth about two trillion rupees and an increase in the threshold at which workers have to start paying income tax. Next fiscal year's budget is also expected to be designed with the economy in mind, with support for both investment and personal consumption.

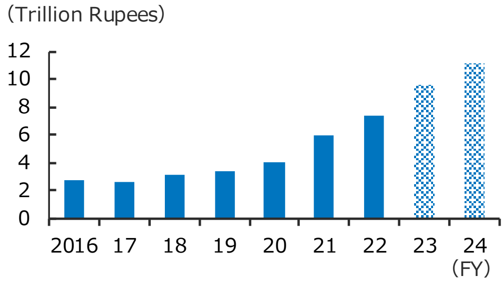
On the other hand, monetary policy is expected to remain tight for some time. In the U.S., inflation is expected to rise through 2026 as the incoming Trump administration raises tariffs on Chinese goods to 60% and implements large-scale tax cuts. As a result, the Federal Reserve is likely to stop cutting interest rates next spring and leave the Federal Funds Rate above 4%, a high level. To prevent the depreciation of the rupee and the resulting inflation, the Reserve Bank of India will probably follow the U.S. in keeping interest rates unchanged. With the release of pent-up demand from the pandemic coming to an end, domestic demand growth is likely to decelerate slightly as monetary policy remains tight.

<Value of India's Mobile Phone Exports>
(Nominal, SA)



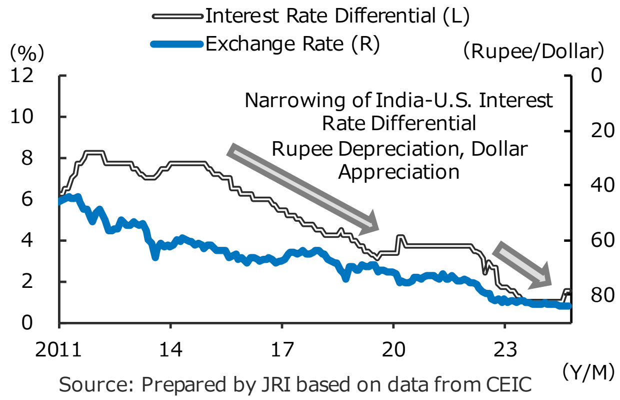
Source: Prepared by JRI based on data from CEIC

<Fiscal Expenditure for Infrastructure Development>



Source: Prepared by JRI based on data from Indian Ministry of Finance
Note: Actual figures until FY2022

<Policy Interest Rate Differential between India and U.S. and Rupee-Dollar Exchange Rate>



Source: Prepared by JRI based on data from CEIC and FRED

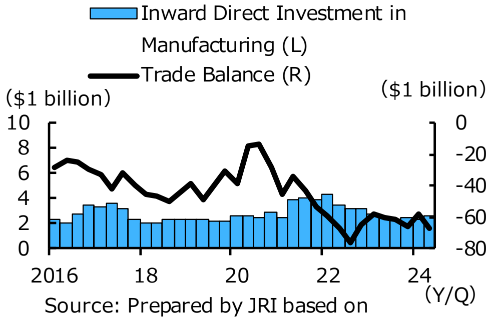
■ Scant progress is being made with strengthening the manufacturing sector, and India may start actively courting Chinese capital

In India, the competitiveness of the manufacturing sector has not increased as much as had been hoped, and this has become an impediment to medium- to long-term economic growth. Under the banner of

"Make in India," the Modi government has sought to strengthen the competitiveness of Indian manufacturing to reduce dependence on imports. It has been trying to get manufacturers to build facilities in India by providing subsidies that increase as production value rises and fiscal support to cover up to 50% of the cost of construction of new semiconductor factories. However, these efforts have so far only produced results in a few areas, one being mobile phones, and little progress has been made with strengthening the international competitiveness of the manufacturing sector as a whole. India's trade deficit has widened further since the beginning of the 2020s, with imports from China, in particular, surging. Sluggish growth in inward direct investment is one of the factors hindering the improvement of competitiveness. Based on the rationale of safeguarding economic security, since 2020 direct investments from neighboring countries have required prior government approval, and partly as a result of this, direct investment from China and Hong Kong has declined, leading to a slump in investment from abroad.

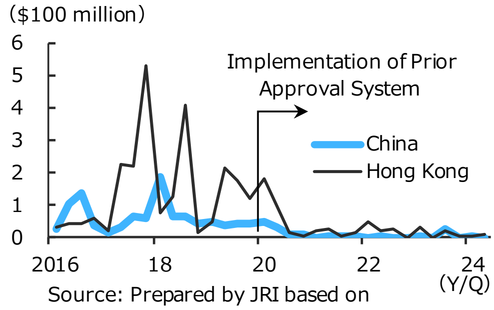
In light of this situation, some in the government are of the opinion that India should start actively welcoming direct investment from China. In its annual economic report published in July this year, the Ministry of Finance expressed the view that increasing domestic production capacity by accepting Chinese capital would lead to an increase in exports and a

<Inward Direct Investment in Manufacturing and Trade Balance in India (Nominal, SA) >



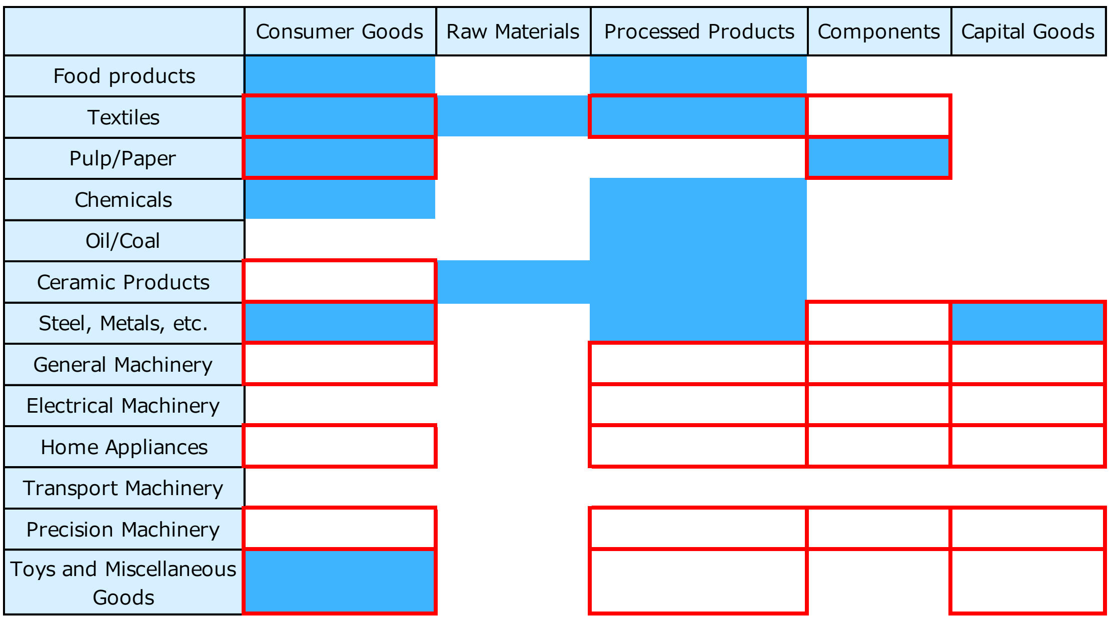
Source: Prepared by JRI based on data from CEIC

<Inward Direct Investment from China in India (Nominal, SA) >



Source: Prepared by JRI based on data from CEIC

<Relative Dominance of India and China by Sector (2022) >



Source: Prepared by JRI based on data from RIETI-TID
Note: Sectors where India's revealed comparative advantage (share of India's exports / share of global exports) is greater than one is shadowed in blue. Those of China are framed in red.

reduction in the trade deficit with China. After crude oil and petroleum products, the biggest components of India's trade deficit are electronic parts and electrical equipment, and these industries would be candidates for the acceptance of Chinese capital. Whereas India lags behind in high-value-added industries like these, China has been gaining dominance in them in recent years, and they are vital fields to nurture if Indian manufacturing is to be strengthened.

Under these circumstances, if the incoming Trump administration, pursuing an "America First" policy, becomes more isolationist and heavy investment from U.S. companies can no longer be counted on, voices arguing that there is no alternative but to accept investment from China could become louder. However, India's Ministry of Commerce and Industry is cautious about accepting Chinese capital because increasing dependence on China would also increase economic security risks. Furthermore, if India becomes more proactive about welcoming Chinese capital and Western countries become reluctant to operate in India, there is a risk of investment from abroad becoming insufficient as a result. India will therefore be watched closely to see what choices it makes going forward.

(Tomohiro Hosoi)

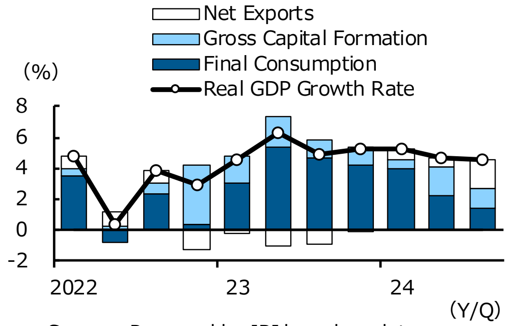
China Sluggish economic growth is expected to continue in 2025

■ Lackluster domestic demand will cause growth to further decelerate

In China in 2024, annualized real GDP growth in 2024 was relatively high in the January-March quarter (5.3%), but slowed for two consecutive quarters in the April-June (4.7%) and July-September (4.6%).

Breaking this down by demand component, domestic demand has fallen into a serious slump. Fixed asset investment has been tepid, and real-estate development investment, in particular, has been plummeting, with year-over-year (YoY) falls of around 10% continuing to be recorded. Infrastructure investment, which had been counted on as a government tool for resuscitating the economy, has also been sluggish.

<Real GDP Growth Rate (YoY) >



Source: Prepared by JRI based on data from the National Bureau of Statistics of China and CEIC

Personal consumption also remains lackluster. Against the backdrop of a harsh employment environment, especially for young people, and the protracted adjustment in the real-estate market, anxiety about the future persists, and households are increasingly keen to save money.

Exports, particularly of automobiles such as EVs and IT-related products, have been rising in volume terms, but the profits of exporting firms have been flat due to falling prices, and the higher volume has not led to increases in employment or wages.

To put a stop to this economic downturn, the government has announced a series of measures to reflate the economy since late September, and these are centered on 1) monetary policy tools, 2) measures to shore up the real-estate market, and 3) fiscal policy tools.

The monetary policy tools were deployed immediately, and involved cutting the policy interest rate, reducing the reserve requirement ratio, and taking steps to boost stock prices (including loans to fund share buybacks). The measures for the real-estate market included the relaxation of restrictions on home purchases and reductions in mortgage interest rates and minimum down payment ratios. In addition, tax relief measures related to housing transactions will come into effect on December 1 this year. As for the fiscal policy tools, the government will complete 100 billion yuan in investment originally set for 2025 ahead of schedule, and use cash raised from additional government bond issuance to inject capital into state-owned commercial banks.

<Measures for Chinese Real-estate Market (From Late September)>

Restrictions on home purchases	Easing of restrictions on number of properties that can be purchased
	Easing of requirements when purchaser is a not a permanent resident (number of years of residence in the city, period of payment of income tax and social insurance premiums, etc.)
Mortgages/ Downpayments	Reduction of mortgage interest rates
	Reduction of minimum downpayment ratio
Other	Expansion of application of eased requirements for VAT exemption when selling a purchased home to four large cities including Beijing
	Expansion of application of reduced deed tax rates when purchasing a home (from area of 90m^2 to 140m^2) and expansion of the measure nationwide
	Expansion of "white list" housing construction projects eligible for bank loans and expansion of scale of lending

Source: Prepared by JRI based on various media reports
Note: The easing of restrictions on purchases covers the four tier-1 cities (large cities), which include Beijing.

As a result of this set of stimulus measures, market sentiment in Shanghai and Hong Kong has improved since late September, with stock prices rising significantly. And considering that exports have continued to increase recently, China's economy is expected to pick up in the October-December quarter of this year. Even so, real GDP growth for the full year of 2024 is still expected to come in at 4.8%, which is only at the lower end of the government's target (around 5.0%) and down from the 5.2% growth registered in 2023.

■ The impact of the stimulus measures will soon peter out and growth will be slower in 2025

In 2025, Chinese economic growth is expected to slow to 4.6%, lower than the previous year. Although the economy should pick up in the first half of the year, the momentum is unlikely to last long.

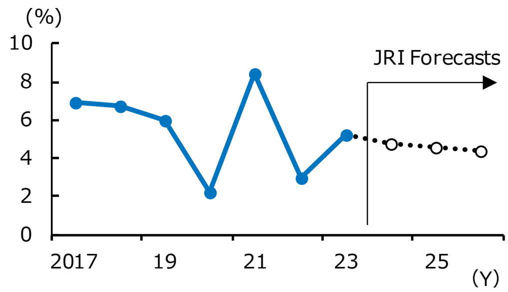
There are three factors that could boost the economy in the first half of the year:

The first is a pick-up in capital investment thanks to financial support. Various measures have been introduced to encourage facility upgrades, and an increase in lending by financial institutions through monetary easing and other policy tools is expected to lead to expansions in investment in manufacturing and other sectors.

The second is an upturn in housing transactions thanks to real-estate measures. Since the measures to shore up the property market were announced, there have been signs of a bottoming out in housing transactions following the protracted slump. Although recently announced real-estate measures will not reverse the long-term downward trend in housing demand, they are expected to temporarily whet the appetite for purchasing homes, which had seen a steep decline.

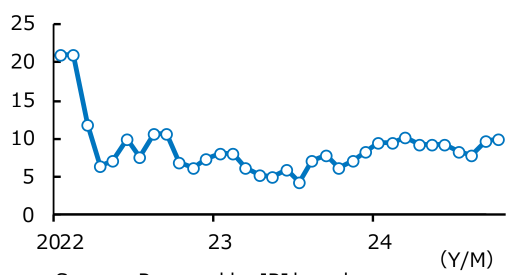
The third is the effect of fiscal policy. At a press conference after the November 2024 meeting of the Standing Committee of the National People's Congress, Minister of Finance Lan Fo'an announced the issuance of an additional 10 trillion yuan of local government bonds over the next five years, which was approved by the National People's Congress. The 10 trillion yuan raised will be used to convert the debts of entities such as local-government financing vehicles (LGFVs), so-called "hidden debt," to local government bonds, so by its nature, it is not expected to stimulate demand. However, since it will reduce the interest payment burden of local governments, including the LGFVs under their purview, it will give local governments room to expand spending. Minister Lan said that he expects the issuance of the local government bonds to reduce interest payments by a total of 0.6 trillion yuan over the next five years, and that the savings will be used for infrastructure development and measures to stimulate consumption, which will boost the economy.

<Real GDP Growth Rate (YoY) >



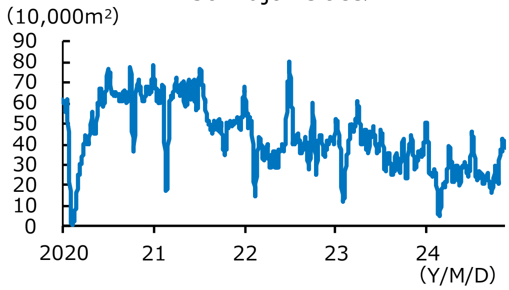
Source: Prepared by JRI based on data from CEIC

<Manufacturing Sector Investment> (YoY)



Source: Prepared by JRI based on data from CEIC

<Housing Floor Area Sold in 30 Major Cities>



Source: Prepared by JRI based on data from Wind
Note: Trailing 14-day moving average

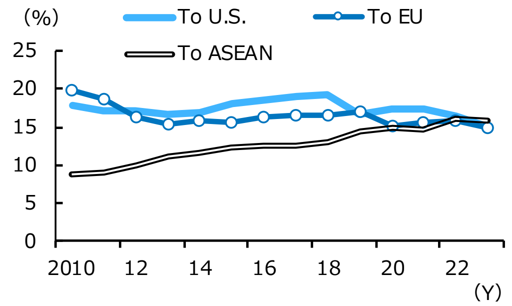
From the second half of 2025, the economy is expected to re-enter an adjustment phase due to two factors: 1) the U.S. raising tariffs on Chinese goods and 2) the petering out of the effects of the stimulus measures.

First, Mr. Trump, who won the U.S. presidential election, has pledged to raise tariffs on all Chinese goods to 60%. And presidential authority alone is enough to allow him to keep this promise. In 2018-20, during his first term, Mr. Trump imposed additional tariffs of 7.5-25% on imports from China, so the 60%

figure he has promised this time is far higher than that. The proportion of Chinese exports heading to the U.S. declined as a result of the worsening of bilateral tensions during the period of the last Trump administration, falling as low as 15.0% in 2023. Yet even today, the U.S. remains a major export destination for China.

Taking these factors into account, it is estimated that if tariffs on Chinese goods are raised to 60%, China's exports to the U.S., mainly products such as apparel and toys, will decline precipitously, and depress China's real GDP growth rate by one percentage point.

<Shares of Exports from China>



Source: Prepared by JRI based on data from CEIC

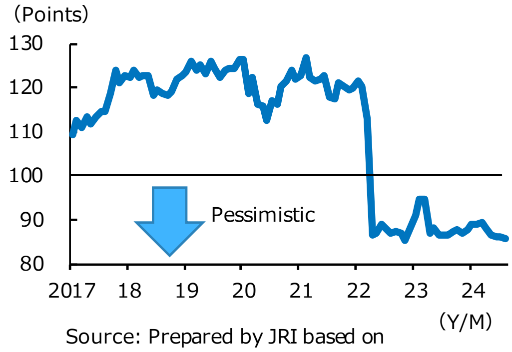
Second, the economic stimulus measures announced by the Chinese government have so far not been sufficient to reverse the structural downward pressures on the country's economy, and their impact is expected to diminish in the second half of 2025. As mentioned above, the specific fiscal policy tools that have already been revealed are mainly focused on reducing the burden on local governments rather than stimulating demand, and they are not expected to give a strong, sustained boost to the economy. And the monetary easing measures, too, are far from radical, and are not powerful enough to dispel the anxiety among companies and households about their futures.

■ All eyes will be on the National People's Congress in March

Given these circumstances, the Xi Jinping administration will face an even harder time navigating the management of the economy. The focus in the near term will be on the National People's Congress, which is scheduled for March 2025. Despite the heavy downward pressure on the economy, the economic measures the government has come up with so far have been small-scale. It is therefore highly likely that additional fiscal stimulus will be announced at the National People's Congress in March, while the government will be keeping an eye on future developments in the domestic economy and U.S. policy toward China. Besides the recapitalization of state-owned commercial banks, details of which had not been provided as of November 2024, concrete measures that could be on the menu include more incentives to replace durable and capital goods and broader measures to encourage local governments to purchase housing. The government's growth target for 2025 is expected to be 4.5-5.0%, but if additional fiscal stimulus is implemented, this will lift the economic growth rate and it may get close to the upper end of the range.

However, if large-scale economic measures are deployed, there is a risk that while they may boost the economy in the short term, they could further exacerbate structural problems over the medium to long term. In particular, if large-scale measures that are heavily skewed toward investment are adopted, there will probably be side effects such as spurring overproduction in the manufacturing sector. At a time when many countries have come to regard Chinese overproduction as a problem, on the grounds that it leads to the "export of deflation," any further expansion of China's production capacity as a consequence of economic measures will intensify frictions with other countries. In addition, if measures are skewed toward helping companies and insufficient action is taken to support households, the latter may become more anxious about the future, causing consumption to decline further. The Chinese government is thus faced with a tricky balancing act that combines short-term economic stimulus measures with medium- to long-term structural reforms.

<Consumer Confidence Index>



Source: Prepared by JRI based on data from CEIC

(Junya Sano)