5. ASEAN Economy facing need to expand domestic demand amid an export plunge

(1) Overview of ASEAN Economy

ASEAN, which was founded in 1967 based on a declaration of the foundation of ASEAN, was the first regional cooperative organization in Southeast Asia. Its purposes were (1) promoting economic growth and social and cultural development in the region, (2) securing political and economic stability in the region and (3) resolving regional problems. The combined GDP of the 10 ASEAN member countries stands at $1.5 trillion, almost equal to Canada's GDP. The populations of the 10 countries total around 590 million people, about twice as large as the U.S. population, about four times as large as the Japanese population and larger than the EU population (about 450 million people) (see Table 1-2-5-1).

ASEAN is comprised of countries which have widely different political systems, cultures, races and languages and which are in broadly different stages of economic development. It has succeeded in increasing its membership by overcoming a conflict of complex interests between the Asian countries and deepened cooperative relationships among them in a variety of fields, including regional, political, economic and social issues.

Table 1-2-5-1 Outline of ASEAN countries

	(Year joined)	Population (million people)	GDP ($100 million)	Per-capita GDP ($)	GDP growth (%)	Percentage of exports to Japan (%)	Percentage of imports from Japan (%)
Indonesia	1967	230.8	5,118	2,246	6.1	18.5	8.7
Thailand	1967	67.1	2,732	4,115	2.6	11.9	20.3
Philippines	1967	92.2	1,686	1,866	4.6	11.8	14.7
Malaysia	1967	27.8	2,222	8,141	4.6	9.1	13.0
Singapore	1967	4.8	1,819	38,972	1.1	4.8	8.2
Vietnam	1995	87.5	898	1,040	6.2	12.0	10.1
Myanmar	1997	60.0	272	462	4.5	5.7	3.8
Brunei	1984	0.4	146	37,053	-1.5	31.0	5.9
Cambodia	1999	13.9	112	818	6.0	3.2	2.2
Laos	1997	6.4	53	841	7.2	0.9	2
ASEAN total		590.9	15,057	2,548		10.0	11.8

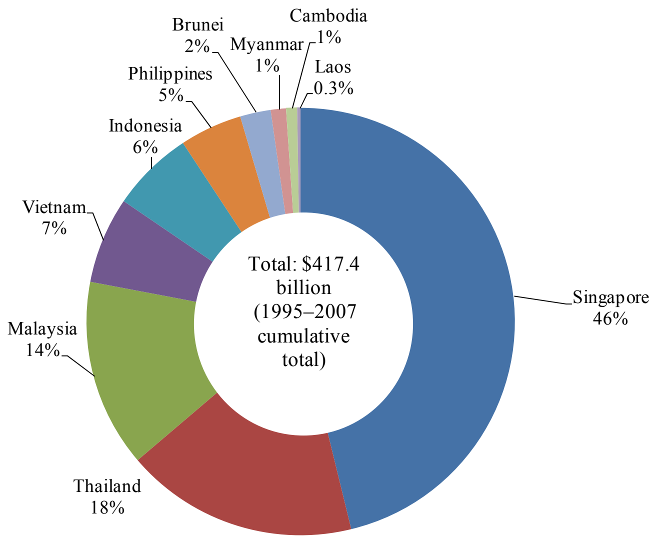
Notes: Population and GDP figures are based on 2008 data. Population and per-capita GDP figures for countries other than Thailand and Malaysia are estimates.
GDP figures for countries other than Thailand, Malaysia, Indonesia and Vietnam are estimates.
Percentages of exports to Japan and of imports from Japan are based on 2007 data.
Source: *World Economic Outlook Database, April 2009, Direction of Trade Statistics, World Trade Atlas* (IMF) (2009).

As the ASEAN countries have actively accepted direct investment from Japan, the United States and Europe since the 1990s, they have achieved rapid growth as bases for processing and assembly of final goods bound for the United States and Europe as a result of a transfer of labor intensive industries from the developed countries to them.

Cumulative direct investment from abroad in the ASEAN countries between 1995 and 2007 amounted to $417.4 billion. Singapore was the largest recipient of investment, accounting for about half of the total. Singapore was followed by Thailand, Malaysia, Vietnam and Indonesia in that order (see Figures 1-2-5-2 and 1-2-5-4).

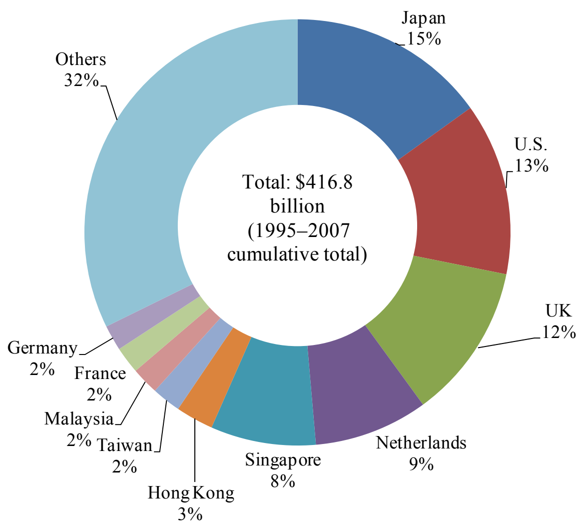
Among investing countries, Japan accounted for 15% of total direct investment in ASEAN, becoming the largest investor. In recent years, Japanese direct investment in ASEAN has grown remarkably, with ASEAN replacing China as the largest recipient of Japanese direct investment in 2006 (see Figures 1-2-5-3 and 1-2-5-5).

Figure 1-2-5-2 Breakdown of direct investment made in ASEAN by recipient country (cumulative total from 1995 to 2007)



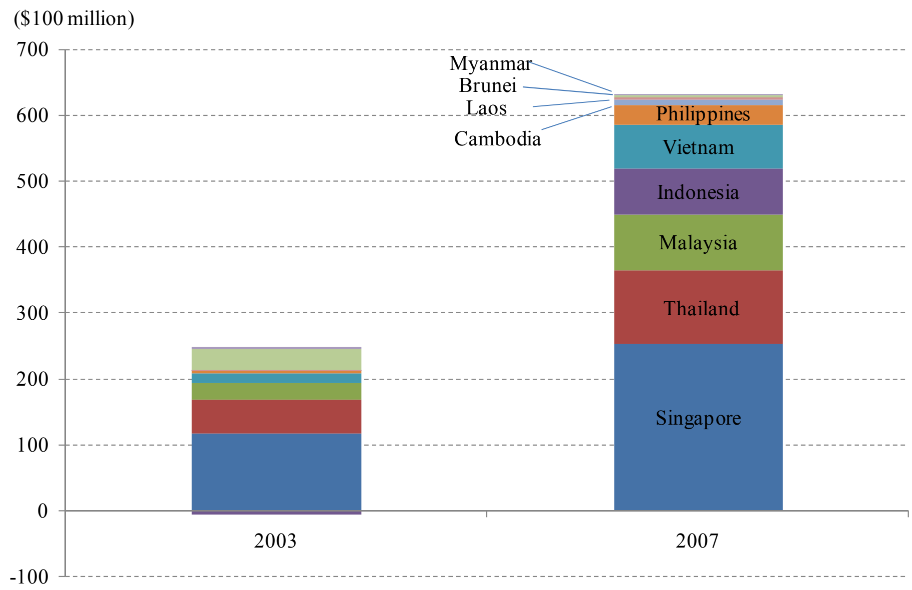
Source: *Statistics of Foreign Direct Investment in ASEAN, 2008* (ASEAN Secretariat).

Figure 1-2-5-3 Breakdown of direct investment made in ASEAN by investing country (cumulative total from 1995 to 2007)



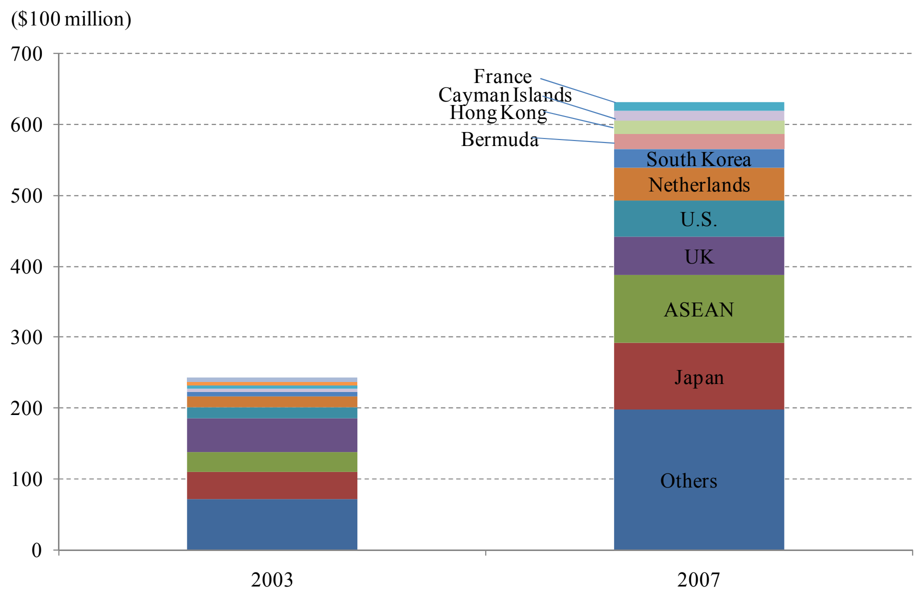
Source: *Statistical Pocketbook 2008* (ASEAN-Japan Centre), *Statistics of Foreign Direct Investment in ASEAN, 2008* (ASEAN Secretariat).

Figure 1-2-5-4 Direct investment in ASEAN by recipient country (2003 and 2007)



Source: *Statistics of Foreign Direct Investment in ASEAN, 2008* (ASEAN Secretariat).

Figure 1-2-5-5 Direct investment in ASEAN by investing country (2003 and 2007)

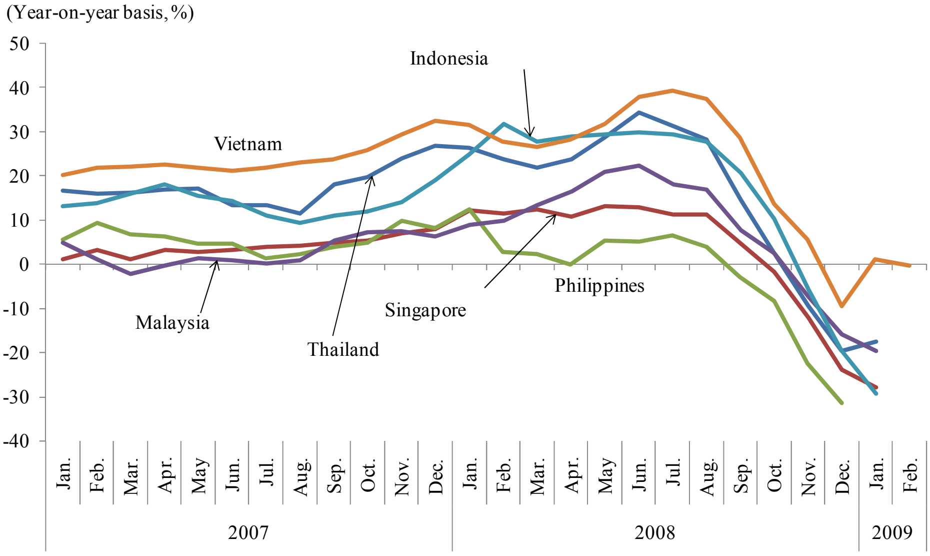


Source: *Statistics of Foreign Direct Investment in ASEAN, 2008* (ASEAN Secretariat).

(2) Impact of the financial and economic crisis

Exports to all regions, the driving force behind ASEAN's growth, increased 35.1% in July 2008 on a year-on-year. However, the growth has slowed down sharply since the financial and economic crisis broke out in September of the same year (see Figure 1-2-5-6).

Figure 1-2-5-6 Changes in ASEAN 6's exports



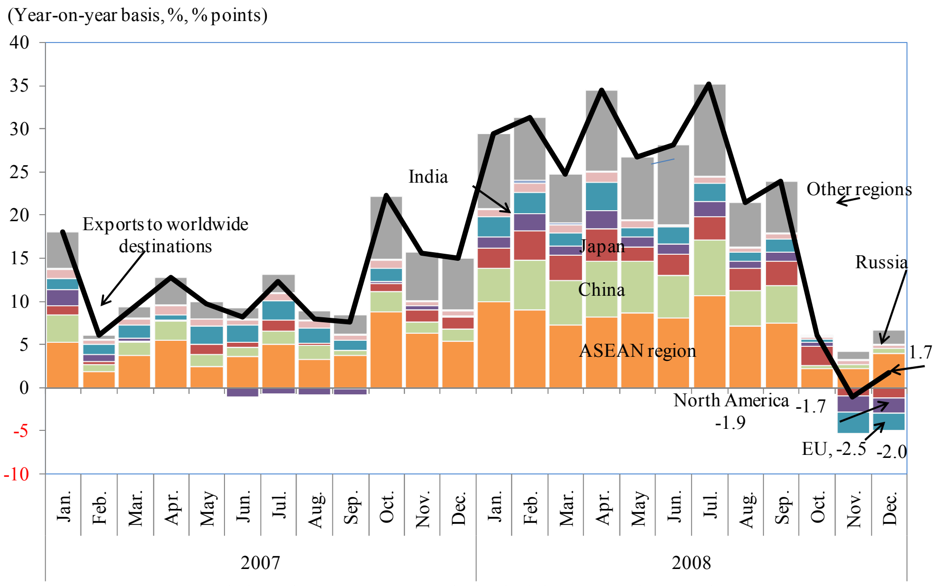
Notes: Three-month moving average.
Source: CEIC Database.

Exports to North America, the EU and Japan all started to decline in November 2008, and exports to the entire world also decreased 1.1%. Persumably, this was mainly due to a drop in exports of electric appliances and machinery.

In addition, the contribution of China-bound exports declined. Presumably, this was caused primarily by a decrease in Chinese demand for electric appliances and machinery parts, which are the ASEAN countries' main export items, as well as drops in prices of natural resources exported from Malysia and Indonesia, including crude oil and palm oil.

On the other hand, intra-ASEAN exports have so far avoided dropping, although growth has slowed down since October 2008 (see Figure 1-2-5-7).

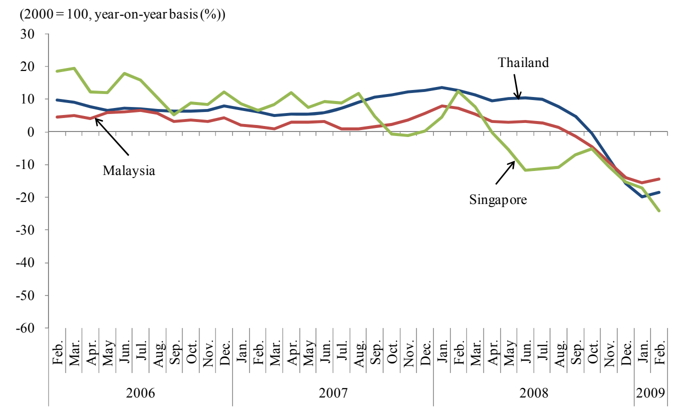
Figure 1-2-5-7 Year-on-year changes in ASEAN 6's exports and percentage contribution, by destination



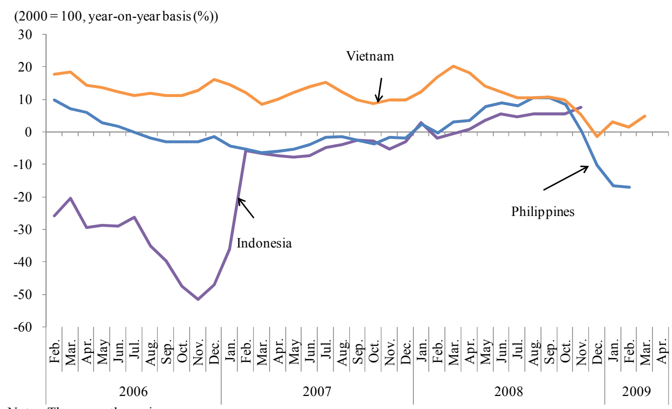
Notes: ASEAN region includes Indonesia, Singapore, Thailand, Philippines, Malaysia and Vietnam.
Source: *Direction of Trade Statistics* (IMF).

Following the rapid drop in exports, the industrial production index fell sharply in most ASEAN countries. The fall was especially sharp in Singapore, Malaysia and Thailand, a large portion of whose exports of electric and electronic industrial products were bound for the United States and China (see Figure 1-2-5-8).

Figure 1-2-5-8 ASEAN 6's industrial production index



Notes: Three-month moving average.
2005 = 100 for Malaysia.
Source: CEIC Database.



Notes: Three-month moving average.
1994 = 100 for Vietnam.
Source: CEIC Database.

Based on the lesson of the Asian currency crisis of 1997, during which a huge amount of overseas funds, mainly short-term funds, flowed out, the value of currencies plunged and a shortage of foreign currency reserves occurred, the ASEAN countries have curbed short-term borrowings, shifted to a floating rate system, expanded their holdings of foreign currency reserves and strengthened regional cooperation in the financial sector.[119] As a result, the ASEAN countries' holdings of foreign currency reserves have increased steeply in recent years. In addition, whereas many ASEAN countries were suffering a current account deficit during the currency crisis, most are now enjoying a current account surplus.

According to the growth outlook for the ASEAN economy in 2009 that was announced by the Asian Development Bank (ADB) in March 2009, the ASEAN economy will post growth of 0.7%, the lowest since the Asian currency crisis, with Singapore, the Philippines, Cambodia and Laos expected to register negative growth.

(3) Overview of the state of major ASEAN countries' economies

(A) Singapore

Impact of the financial and economic crisis first appears in very export-dependent Singapore

Singapore, with an area of only 707 square kilometers (around 20% larger than the area covered by Tokyo's 23 wards) and a population of some 4.8 million people, places priority on securing access to the global economy through a free trade system. Data on the contribution of demand components to real GDP show that Singapore's growth is driven by fixed capital formation and net exports (see Figure 1-2-5-9).

In 2008, in terms of the trade value, Japan was Singapore's fourth largest source of imports and the sixth largest export destination.[120] Singapore's export dependency ratio[121] is extremely high, at 230.9%, far higher than Japan's 17.6%.

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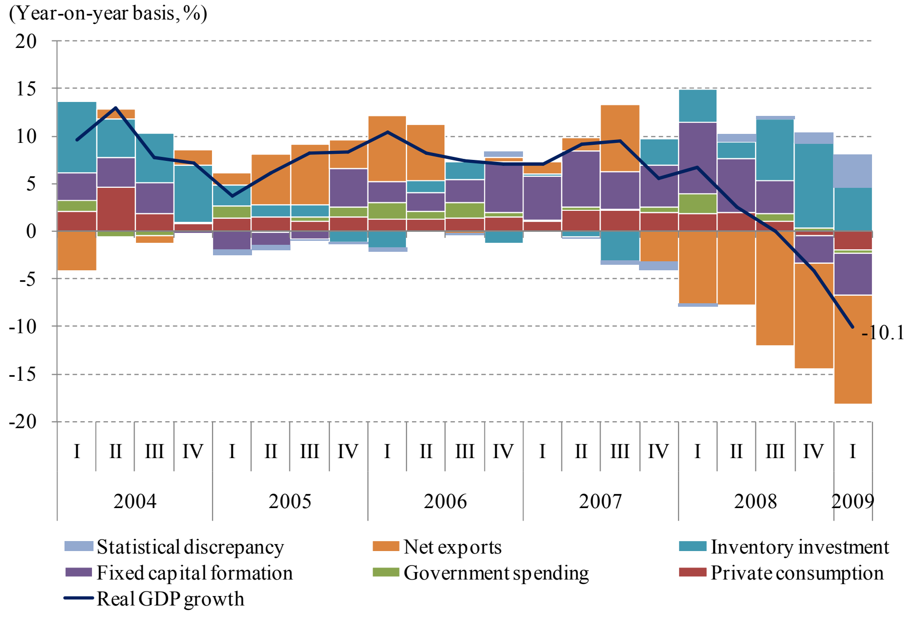
[119] In order to resolve a currency and duration mismatch, which was a cause of the Asian currency crisis, ASEAN plus Three (Japan, China and South Korea) agreed in May 2000 on the Chiang Mai Initiative. Under the initiative, a country in the region facing a liquidity problem that could threaten external payments receives short-term foreign currency funds from other countries in the region through currency swap arrangements. In addition, the Asian Bond Markets Initiative was agreed upon in August 2003 in order to utilize the abundant pool of private savings in Asia for investment in economic development.

[120] Major export items are electrical appliances and mineral fuels. Singapore is the seventh largest export destination for Japan.

[121] The export dependency ratio is calculated by dividing the value of exported goods and services by nominal GDP. The figure cited here was extracted from the "National Accounts Main Aggregates Database," compiled by the United Nations.

Figure 1-2-5-9 Singapore's real GDP growth and percentage contribution by demand component



Source: Singapore Department of Statistics.

(a) Impact of the financial and economic crisis

Singapore maintained annual real economic growth of 7 to 9% each year between 2004 and 2007 and posted strong growth in the first quarter of 2008, too. The growth started to slow down in the second half of the year and turned negative in the fourth quarter, reaching an annual real growth rate in 2008 of 1.1%.

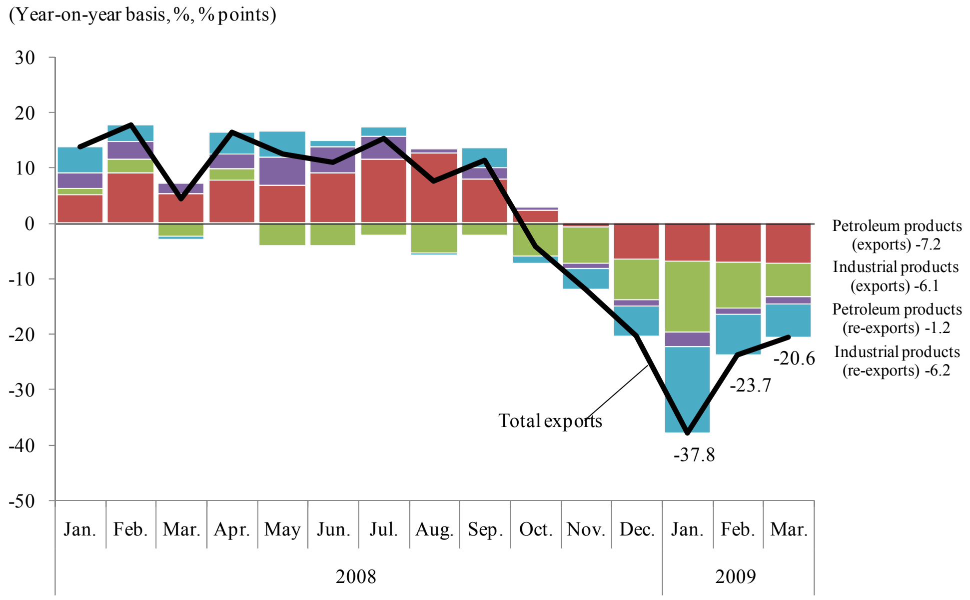
A breakdown of GDP growth by demand component shows that drops in fixed capital formation and exports had a significant impact. Fixed capital formation, almost 90% of which is accounted for by private investment, grew steadily until the second quarter of 2008. However, growth started to slow down in the third quarter of the year, immediately after the outbreak of the financial and economic crisis, and turned negative in the fourth quarter. In the first quarter of 2009, the margin of decline widened further.

Net exports dropped even more sharply than fixed capital formation. Net exports started to decline in the fourth quarter of 2007, earlier than fixed capital formation. Since the third quarter of 2008, immediately after the outbreak of the financial and economic crisis, the margin of decline has widened as exports and re-exports of both petroleum products and industrial products declined (see Figure 1-2-5-10).

In contrast to the high ratio of exports, the ratio of private consumption to Singapore's real GDP is relatively low, at 40%. Amid the deterioration in the employment environment, private consumption in Singapore also started to decline in the fourth quarter of 2008.

As a result, Singapore's real GDP growth deteriorated significantly, to −10.1%, in the first quarter of 2009.

Figure 1-2-5-10 Year-on-year changes in Singapore's exports and percentage contribution by type of product



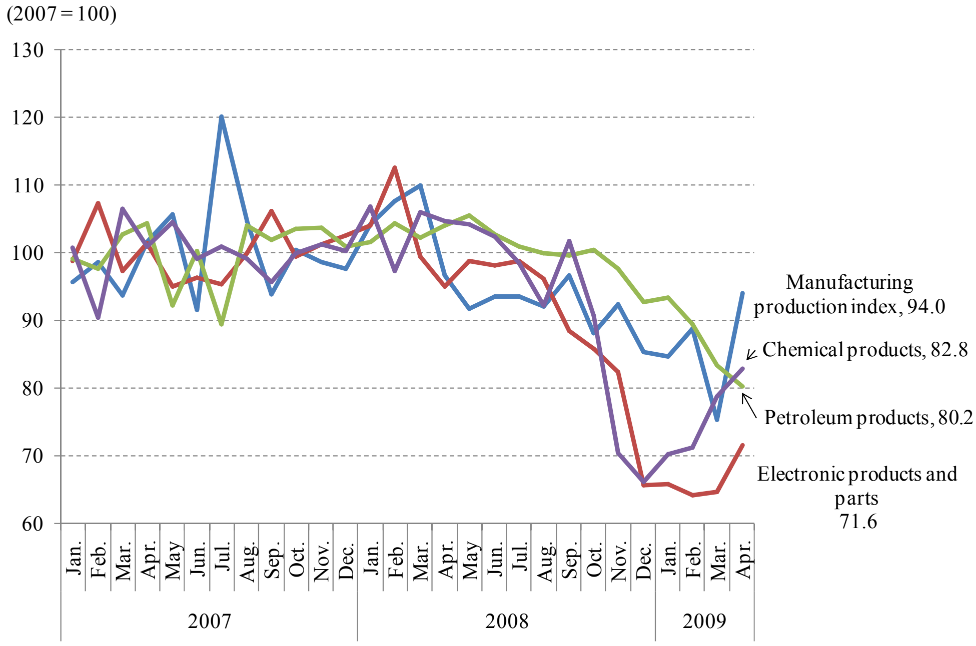
Notes: In Singapore dollars.
Source: CEIC Database.

Singapore's trade is mainly comprised of processing trade, which refers to processing and assembly of imported parts and intermediate goods for re-exports. Exports of electric appliances account for about half of the value of Singapore's total exports except for those of mineral fuels. While the manufacturing production index continued to decline in April 2008 and thereafter, production of electronic products and parts, which account for about 30% of the value of production by the entire manufacturing industry, posted a particularly steep drop because of increased pressure for domestic production adjustments following a slowdown in exports of such products and parts caused by the global financial and economic crisis. In February 2009, the production index for these items fell to 64.1. Among other items, production of petroleum products and chemical products, which account for some 20% and 10%, respectively, of the overall value of production, dropped rapidly in October 2008 and thereafter.

However, as the margin of decline in the value of exports started to narrow in February 2009, the manufacturing production index began to recover in January 2009 for chemical products and in April of the same year for electronic products and parts. In April 2009, the manufacturing production index recovered significantly as a result of a sharp rise in the pharmaceutical/biotechnology sector (see Figure 1-2-5-11).[122]

[122] It should be kept in mind that the production amount in the pharmaceutical/biotechnology sector may vary extremely from month to month due to the need for temporary factory shutdowns for lot changes and maintenance work.

Figure 1-2-5-11 Singapore's manufacturing production index



Source: CEIC Database.

Despite the recent signs of a recovery, pressure for production adjustments is likely to continue, since the economies of the United States and other developed countries, which are major destinations of exports of electronic products and parts, chemical products and pharmaceutical products, Singapore's major export items, are not expected to recover soon.

When Singapore's Ministry of Trade and Industry announced preliminary GDP data for the first quarter of 2009 on April 14, 2009, it revised downward the estimated growth range of −2% to −5% for 2009, which had been announced in January of the same year, to a range of −6% to −9%.

(b) Economic stimulus measures

In January 2009, the Singapore government announced an economic stimulus package worth 20.5 billion Singapore dollars (SGD) (around ¥1.2 trillion), which was larger than the 12.5-billion-SGD economic stimulus package adopted during the Asian currency crisis of 1998 and which was equivalent to around 8.8% of real GDP in 2008.

With its top priority placed on securing employment, the new economic stimulus package features employment-support measures, including the provision of employment subsidies to employers and support for vocational training and corporate tax reduction as well as support for households and the development of infrastructures, including those related to medical care and education. The Singapore government is actively implementing policy measures, including the promotion of research and development concerning new growth sectors, such as biomedical science, water-related technologies, digital media and the environment, and measures related to the labor and immigration policies.

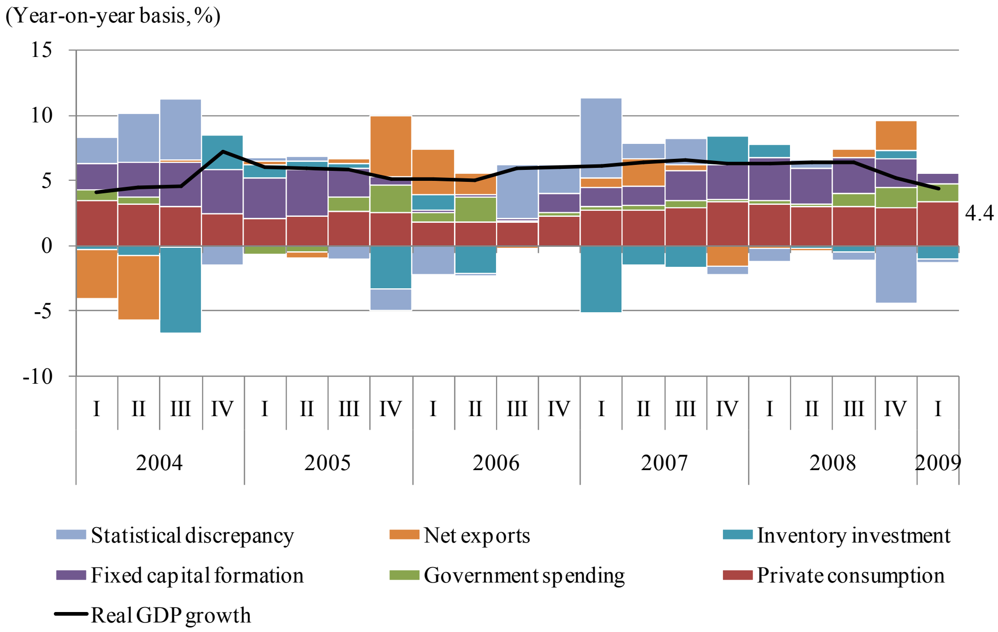
(B) Indonesia

Indonesian economy attracting attention for the firmness of domestic demand after the financial and economic crisis

Indonesia, a multi-racial country comprised of around 18,000 islands, has a population of 230 million people, the largest among the 10 ASEAN countries. It also has the largest population of Muslims.

Indonesia's real GDP growth has held steady at around 6% for the past several years. Data on the contribution of demand components to economic growth show that growth has been driven by private consumption, mainly purchases of consumer durable goods, such as automobiles and home electronics appliances; exports of natural resources, including crude oil, natural gas and palm oil, which account for about 30% of the overall value of exports; and fixed capital formation like capital expenditures financed by inward direct investment (see Figure 1-2-5-12).

Figure 1-2-5-12 Indonesia's real GDP growth and percentage contribution by demand component



Source: Statistics Indonesia.

(a) Impact of the financial and economic crisis

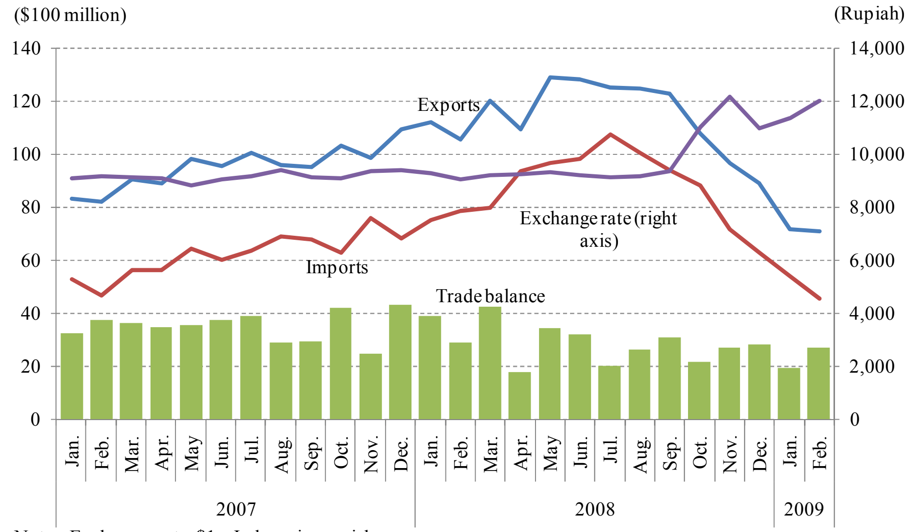
In response to the outbreak of the financial crisis in September 2008, the Indonesian rupiah, which had stayed stable at an exchange rate of around 9,200 rupiahs to the dollar, dropped sharply. Even though the drop was arrested by exchange market interventions made by Bank Indonesia, the central bank, the rupiah has remained weak since then (see Figure 1-2-5-13).

Although exports continued to post growth of around 30% on a year-on-year basis until September 2008, the growth slowed down in October and turned negative in November. Exports of oil and natural gas, which account for around 20% of Indonesia's exports and 90% of which are bound for Asian countries like Japan, South Korea and China, increased sharply in terms of value in the whole of 2008. However, exports of oil and natural gas started to decline in November on a year-on-year basis. In addition, exports of palm oil, another major export item for Indonesia, also started to decline in the second half of 2008 and exports of industrial products gradually slowed down and decreased. Consequently, the overall value of exports posted a year-on-year drop of 32.3% in February (see Figure 1-2-5-14).

In the first quarter of 2009, while private consumption remained firm, real GDP growth came down to 4.4% due to a decline in exports and a slowdown in fixed capital formation.

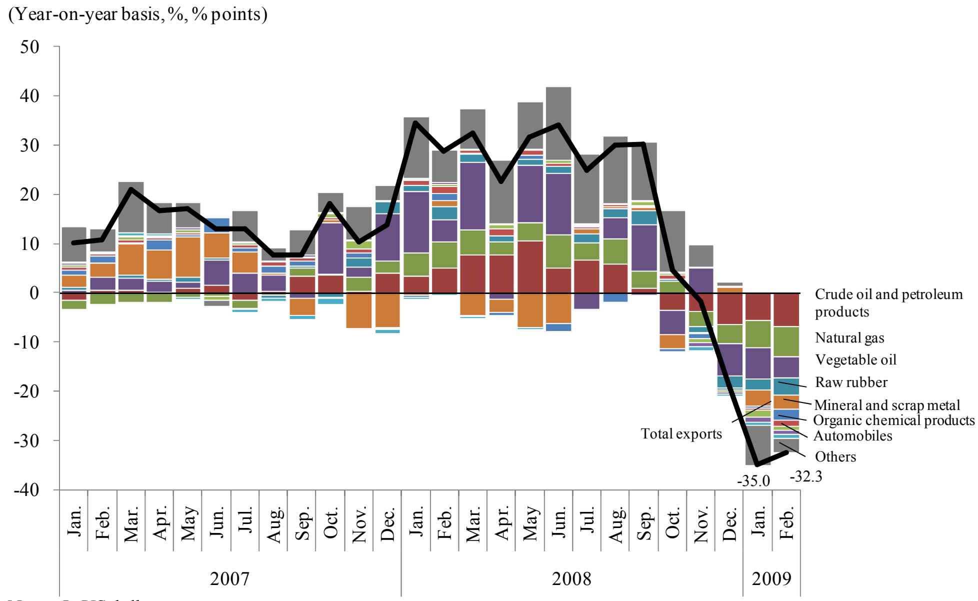
The ADB forecasts real GDP growth of 3.6% for Indonesia in 2009, while the IMF predicts growth of 2.5%.

Figure 1-2-5-13 Changes in Indonesian imports and exports and Indonesian rupiah exchange rate



Notes: Exchanges rate: $1 = Indonesian rupiah.
Source: Statistics Indonesia, Central Bank of Republic of Indonesia.

Figure 1-2-5-14 Changes in Indonesian exports and percentage contribution by type of major product



Notes: In US dollars.
Source: CEIC Database.

(b) Economic stimulus measures

In October 2008, the Indonesian government, in an effort to stabilize the domestic economy, announced an emergency economic package comprised of 10 measures, including the securing of foreign currencies, repurchases of government bonds and strengthening of the prevention of illegal imports. In addition, it revealed a plan to stimulate the economy by granting import duty exemption to 10 business sectors: foods and beverages, home electronics appliances, parts for home electronics appliances, auto parts, communications equipment, parts for ships, chemical products, steel products, heavy machinery and parts for small-scale steam turbine power plants (Table 1-2-5-15).

Table 1-2-5-15 Indonesia's economic stimulus measures

(1) State-controlled companies will return all foreign currencies to domestic banks. They will report their demand for foreign currencies and their foreign currency profit to the Ministry of State-Owned Enterprises. Foreign currency transactions will be made through state-run banks.
(2) Launching bilateral or multilateral foreign currency-denominated infrastructure projects ahead of schedule, in order to secure foreign currencies and stabilize the balance of payments.
(3) Stepping up efforts to stabilize liquidity by instructing state-controlled companies not to transfer funds between banks, and avoiding competition to secure foreign currencies.
(4) Repurchasing government bonds in stages in a joint effort between the government and the central bank, stabilizing the bond market, and maintaining confidence in the market.
(5) Where necessary, utilizing currency swap agreements with the central banks of Japan, South Korea and China, as part of the second line of defense, in order to secure foreign currencies and stabilize the balance of payments.
(6) Introducing a guarantee system for trade settlement on November 1, 2008, in a bid to promote exports.
(7) Abolishing tariff on crude palm oil (CPO) exports (2.5%) starting from November 1, 2008, in an effort to ensure sustainable development of real economy.
(8) Announcing new stimulus measures in a supplementary budget upon passing the FY2009 budget bill through the Diet.
(9) Stepping up anti-smuggling measures starting from November 1, 2008. Issuing rules on imports of specified products, including clothes, electronic and electrical products and foodstuff, allowing only registered companies to import such products, and requiring them to obtain certification at the port of dispatch. Restricting imports of specified products to major ports and airports in the capital, such as Tanjung Priok Port and Soekarno-Hatta Airport.
(10) Setting up a task force led by government-affiliated agencies to reinforce the oversight of goods distribution.

Source: JETRO website.

(c) Hopes for an expansion of domestic demand led by consumption

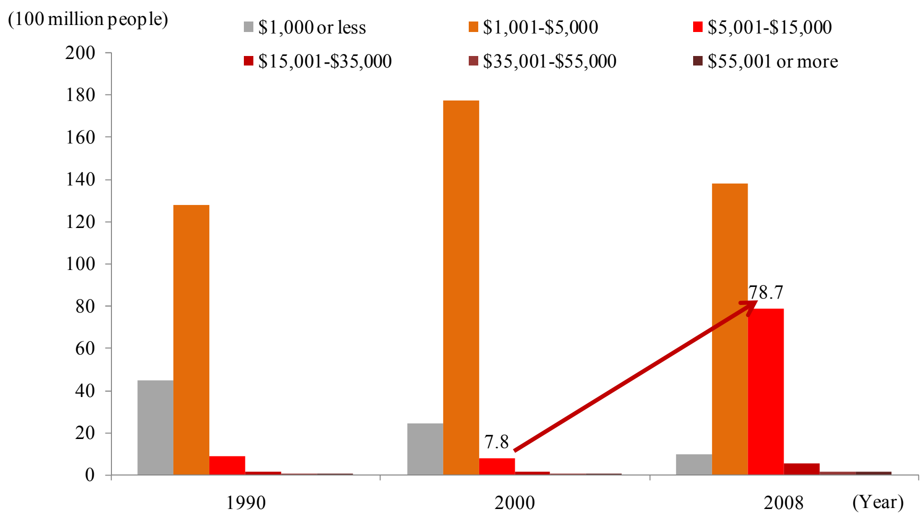
Indonesia is the world's fourth most populous country, after China, India and the United States, and its private consumption accounts for around 60%[123] of real GDP.

The number of people with a household disposable income of $5001 or more is estimated to have

[123] In 2008, private consumption accounted for 57.2% of real GDP.

increased 10-fold from some 7.8 million in 2000, to around 79 million[124] in 2008 (see Figure 1-5-2-16). Indonesia's domestic demand, led by consumption by the 230-million-population, is expected to continue expanding on the back of the country's abundant reservoir of natural resources.

Figure 1-2-5-16 Indonesia's demographic changes in terms of the size of household disposable income



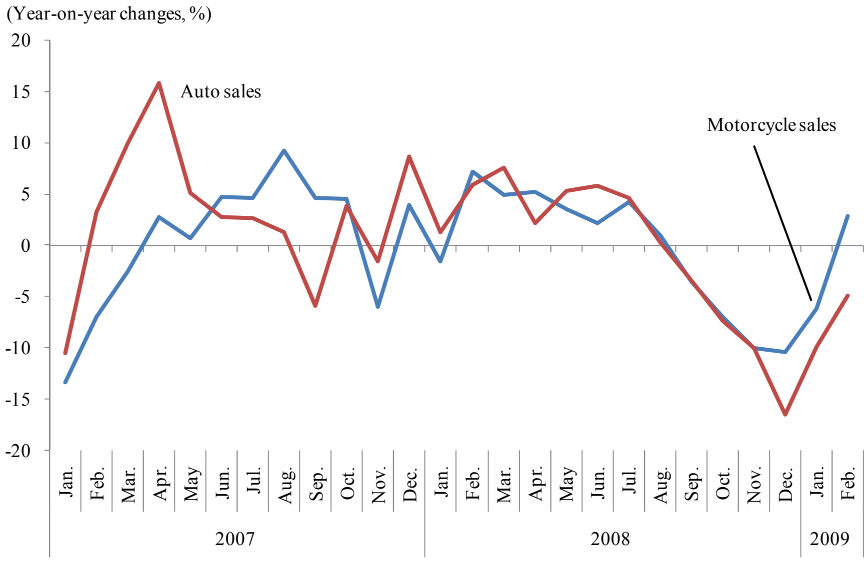
Source: Created by Nomura Research Institute using data from *World Consumer Lifestyle Databook 2009* issued by Euromonitor International.

The consumer confidence index (preliminary) rose in April 2009 for the fourth consecutive month, to 102.5,[125] its first rise above 100 since November 2007, indicating that consumption by the Indonesian people remained strong despite the recession.

According to the Indonesian Ministry of Industry, sales of foods and beverages grew 1.4% in the first quarter of 2009 compared with the same period of the previous year, with sales of daily necessities increasing 8.1%. According to a global confidence survey report announced by Nielsen, the confidence index was higher than 100 only in Indonesia (104) and Denmark (102) among the 50 countries surveyed.[126] Sales of motorcycles, which had grown strongly since 1998, declined for some time starting around August 2008 but rebounded in February 2009 (see Figure 1-2-5-17).

[124] The number of people in this household disposal income bracket was calculated by multiplying the ratio of households in the same disposable income bracket in each year by the population number in the year.
[125] The figure was announced by Bank Indonesia on May 6, 2009. A reading of 100 or higher indicates optimism and a reading of less than 100 indicates pessimism. Extracted from an article carried by NNA・ASIA.
[126] The results of the survey were announced by Nielsen on May 4, 2009.

Figure 1-2-5-17 Auto and motorcycle sales in Indonesia



Notes: Three-month moving average.
Source: Bloomberg.

(d) Relations with Japan

Indonesia exports mineral and natural resources, including oil, natural gas, iron ore, nickel and rubber, to Japan, which is its largest export destination.[127]

On July 1, 2008, the Japan-Indonesia Economic Partnership Agreement went into effect. As a result, Japan has abolished tariffs on most industrial products imported from Indonesia, while Indonesia will gradually reduce tariffs on electronic parts and auto parts to zero. In addition, Japan started accepting prospective nurses and welfare nursing workers from Indonesia. In August 2008, the first year of the program, around 200 prospective nurses and welfare nursing workers arrived in Japan from Indonesia.

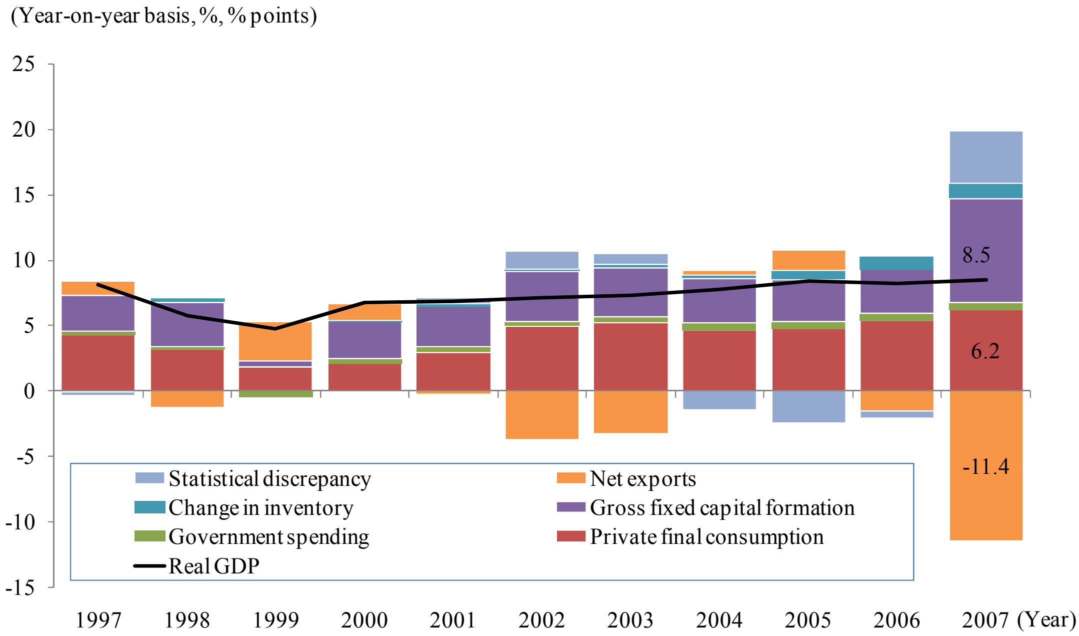
(C) Vietnam

Vietnam's high growth led by foreign capital

Vietnam started accepting foreign capital based on the "Doi Moi" (reform) initiative launched in 1986. Vietnam joined ASEAN in 1995, and the amount of direct investment from abroad, mainly real estate investment by the United States, has grown sharply in recent years, as the country is regarded as a promising post-China investment target under the "China-plus-one" strategy. In 2007, Vietnam's trade deficit expanded due to significant import inflation caused by an upsurge in prices of natural resources and raw materials, and this temporarily raised concerns over a possible currency crisis. However, the Vietnamese economy has maintained growth, supported by fixed capital formation and firm private consumption (see Figure 1-2-5-18).

[127] Japan exports automobiles, electrical machinery, etc. to Indonesia.

Figure 1-2-5-18 Vietnam's real GDP growth and percentage contribution by demand component



Source: CEIC Database.

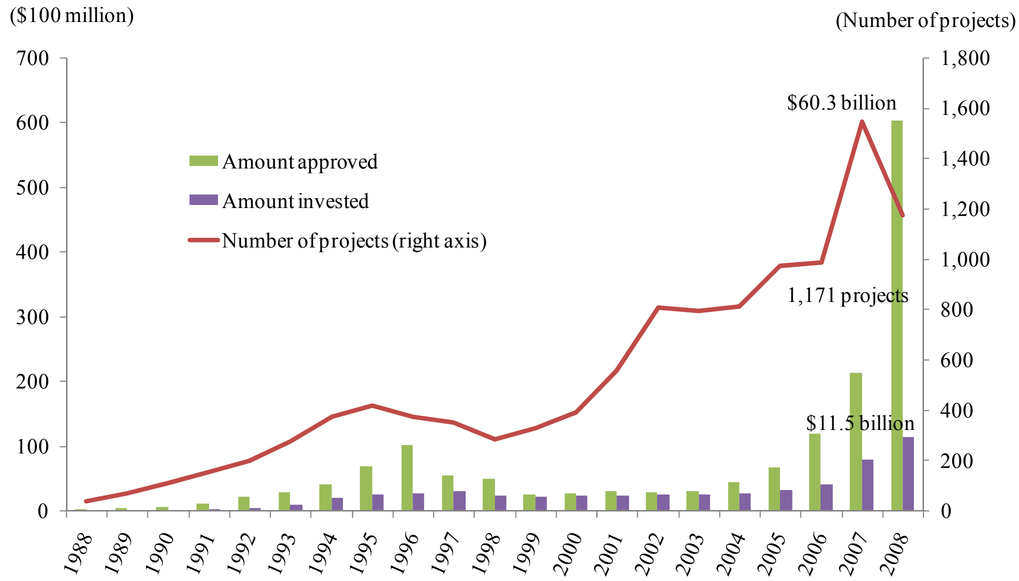
(a) Increasing direct investment

Direct investment in Vietnam is made mainly in the form of the establishment of a 100%-foreign-capital company engaging in export processing in an industrial zone. The heavy industry is particularly popular as an investment target, and investment in services, transport and IT sectors is also active. Although the number of inward direct investment projects approved in 2008 fell 24.2% from the previous year to 1,171, the value of approved projects tripled to $60.3 billion.[128] Malaysia was the largest investor in 2008 in terms of the value of approved direct investment projects, followed by Taiwan and Japan in that order.

Despite concerns that large-scale projects might not be implemented as planned as a result of the impact of the economic crisis, the value of projects implemented in 2008 grew 43.2% from the previous year to $11.5 billion.[129] The number of Japanese direct investment projects in Vietnam approved in 2008 stood at 105, with their value reaching a record high of some $7.3 billion due to factors such as the approval of a large-scale oil refinery construction project (see Figures 1-2-5-19 and 1-2-5-20).

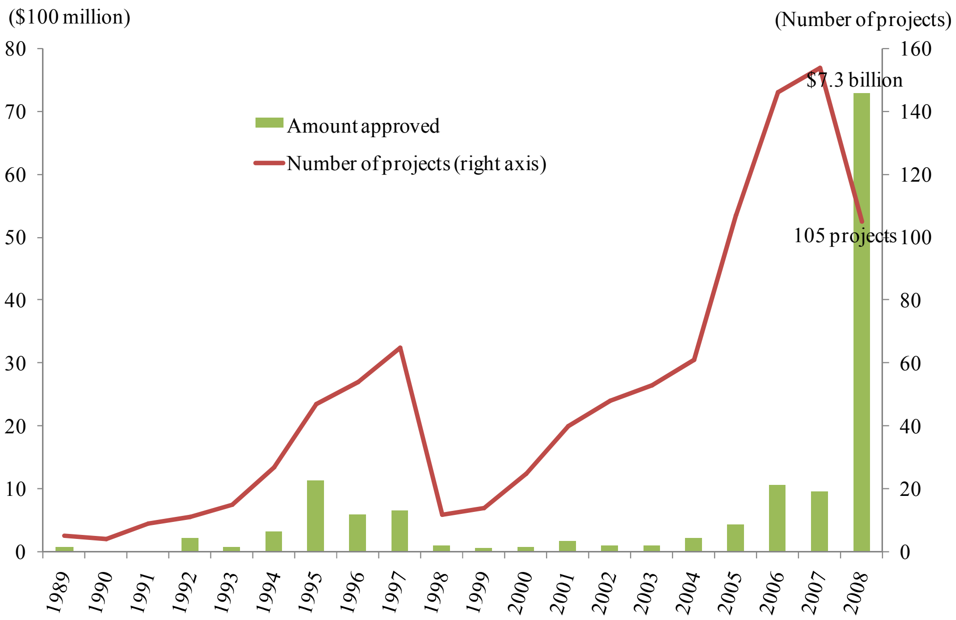
[128] Approved projects include real estate development projects, such as the construction of resort facilities and large-scale urban development, and the construction of steelworks.
[129] This amount is equivalent to around 12.8% of Vietnam's real GDP.

Figure 1-2-5-19 Changes in global direct investment in Vietnam



Source: General Statistics Office of Vietnam.

Figure 1-2-5-20 Changes in Japanese direct investment in Vietnam



Source: Ministry of Planning and Investment of Vietnam.

Vietnam, which stretches long from north to south, is divided into two economic areas: the northern area centering on Hanoi, which is affected by the economic influence of China's Huanan region, and the southern area centering on Ho Chi Minh City, which is affected by the economic influence of Thailand

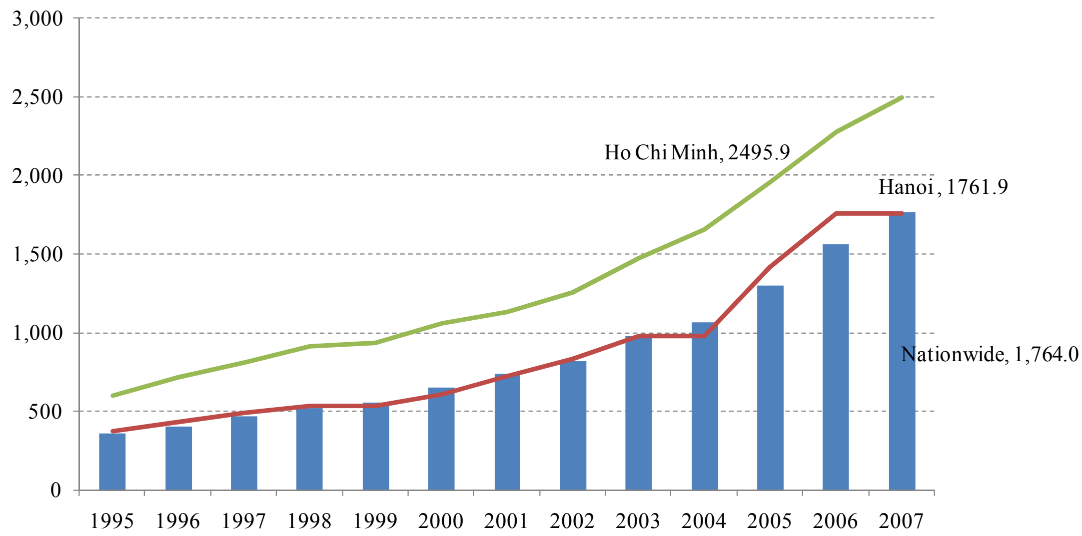
and Singapore. There are many manufacturers of products for external demand in the Hanoi area, while the Ho Chi Minh area is host to many companies that make products for domestic demand, such as foods and household products.

For Vietnam, which has continued its economic growth by accepting direct investment, there are also some causes for concern. Although low wages are cited as an attractive factor about Vietnam, wages are continuing to rise in line with inflation (see Figure 1-2-5-21). There is a risk that labor costs will rise further as a result of a labor shortage in urban areas and inflation given the ongoing competition to secure employees due to the entry of foreign-owned companies as well as a shortage of people suitable for middle management positions.

According to a questionnaire survey[130] conducted by JETRO on its member companies, more than half of the respondents cited underdevelopment of infrastructures, including facilities related to electricity and other energies and roads, as a problem with Vietnam. Another impediment to doing business in Vietnam cited by the respondents is the underdevelopment of local industries, which makes it necessary to procure parts from somewhere else and pushes up costs. In addition to infrastructure development, the provision of support concerning know-how and personnel matters is regarded as important.

In December 2008, Japan and Vietnam signed an Economic Partnership Agreement, under which tariffs on some 92% of the value of two-way trade will be abolished within 10 years after the entry-into-force of the agreement. They also signed a document concerning cooperation in fostering supporting industries for production of automobiles and electric products.

Figure 1-2-5-21 Vietnamese employees' wages



Notes: Monthly wages. 2007 figures are estimates.
Source: General Statistics Office of Vietnam.

[130] JETRO (2009), "Survey of Japanese-Affiliated Firms in Asia and Oceania (FY 2008 Survey)"

(b) Impact of the financial and economic crisis

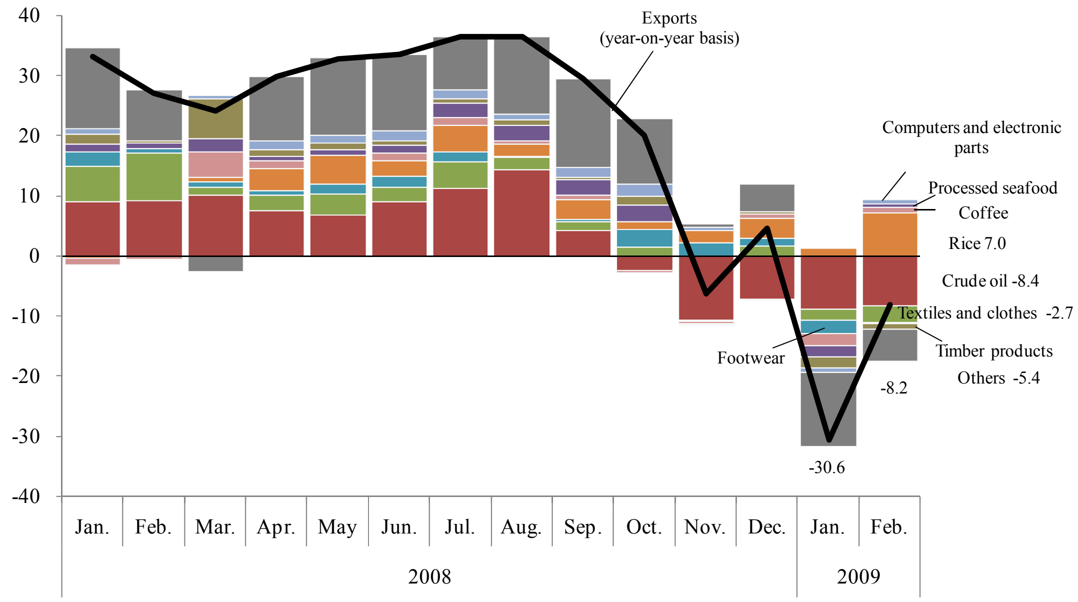
Items with high export value are crude oil, textiles and clothes, footwear, electronic products/computer parts, timber products and rice. In particular, production of industrial products, including electronic products and computer parts, grew remarkably due to investment from both within and outside Vietnam. As there was no oil refinery in Vietnam until recently,[131] the country imported oil products in exchange for exporting crude oil. Therefore, its trade deficit temporarily expanded after an upsurge in resource prices. However, the trade deficit later narrowed because of import restrictions imposed by the government and the stabilization of resource prices.

As Vietnam's export industries (export-processing companies, the textile industry, etc.) were affected by the recession in the United States and the EU, which are its major export destinations, growth in exports started to slow down in August of 2008 and turned negative in November. In the whole of 2008, exports totaled $62.9 billion and imports amounted to $80.4 billion, resulting in a trade deficit of $17.5 billion. As an export promotion measure, the Vietnamese government allowed a floating exchange rate system in 2008, expanding the exchange trading band from ±0.75% to ±3%. In addition, it reduced the official exchange rate of the Vietnamese currency twice, in June and December of 2008, for total cuts of 5.36% amid concerns that the trade deficit was boosting demand for the U.S. dollar.

Exports of crude oil were firm until around the summer of 2008 in line with a rise in prices but started to decline in October on a year-on-year basis. Exports of textiles and clothes as well as timber products also started to drop in January 2009 due to a slump in demand from developed countries. Figure 1-2-5-22 shows that exports of rice and other foods, which are seen as resilient to economic cycles, are growing steadily.

[131] In Vietnam, where the government is implementing an oil refinery construction project, the country's first oil refinery started production in February 2009. In addition, the construction of an oil refinery by a joint venture of Japanese-owned companies, Kuwait Petroleum International and Vietnam National Oil and Gas Group has started.

Figure 1-2-5-22 Changes in Vietnamese exports and percentage contribution by type of major product[132]



Notes: The figure excludes rare minerals/metals and arts.
Source: CEIC Database.

(c) Trend in consumption

Vietnam has a population of some 87.5 million people, the second largest among the ASEAN countries, after Indonesia's population. While its economic growth has slowed down due to the impact of the global financial crisis, per-capita GDP came to $1,040 and per-capita real GDP on a purchasing power parity basis stood at $2,784.

Monthly wages for employees in Ho Chi Minh City in 2007 stood at around 250,000 dong (around $140) (see Figure 1-2-5-21). The rise in labor costs that we mentioned earlier, if seen from a different angle, means a rise in wages.

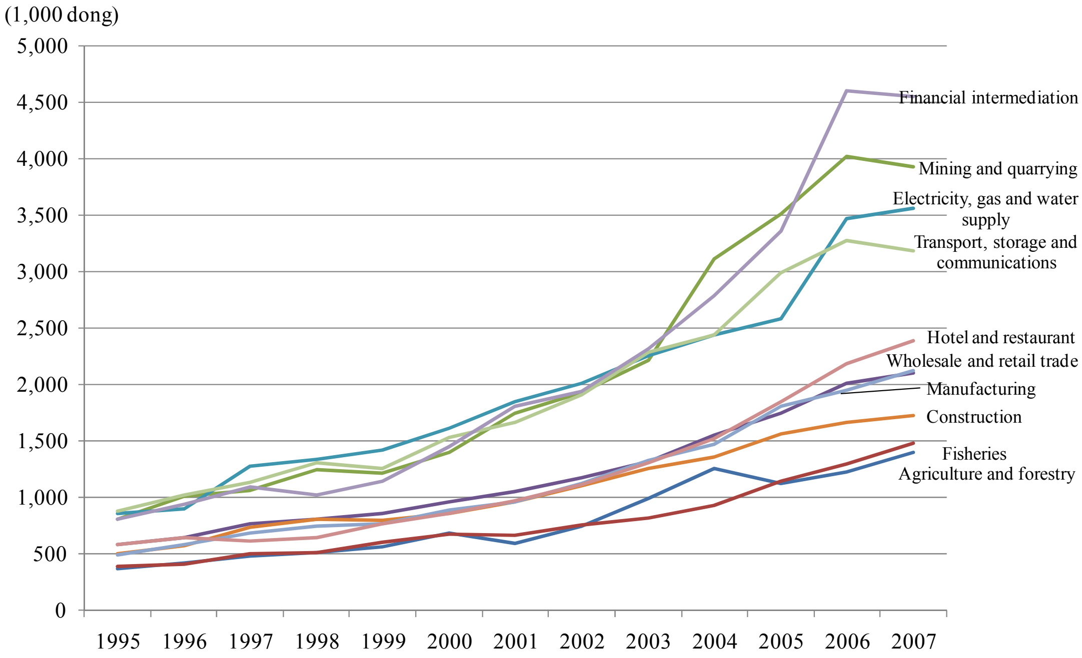
In Vietnam, the income of people engaging in primary industries, who account for about half of all employees (53.9% as of 2005) tripled between 1995 and 2007. Even if inflation is taken into consideration, income is continuing to grow significantly (see Figure 1-2-5-23). As for the industry-by-industry contribution to real GDP, the contributions of the services, mining and manufacturing industries are large but unstable while the contributions of the agricultural, forestry and fisheries industries, which are not susceptible to changes in external demand, remain almost constant (see Figure 1-2-5-24). In 2008, the

[132] Usually, the payments for real estate transactions in Vietnam are made in gold. Therefore, when land prices were rising, imports of gold grew. However, a decrease in real estate transactions due to a land price drop that started in the second half of 2008 reduced the need for holding gold. The value of exports in January and February 2009, when gold prices rose sharply, included the value of the large amount of gold that was sold by banks and importers that had actively bought gold in 2008 amid the inflation. In light of this, we excluded from the above figure the value of exports of precious minerals/metals and artistic craftworks. (Ref. "An interview with Ms. Pham Chi Lan, Vice President of Institute of Development Studies, (1) - (Vietnam), " World Business News by JETRO, April 13, 2009

number of people with a household disposable income of between $1,001 and $5,000 is estimated to have increased to around 55 million people and the number of people with a household disposable income of $5,001 or more is estimated to have grown to around 11 million people (see Figure 1-2-5-25).

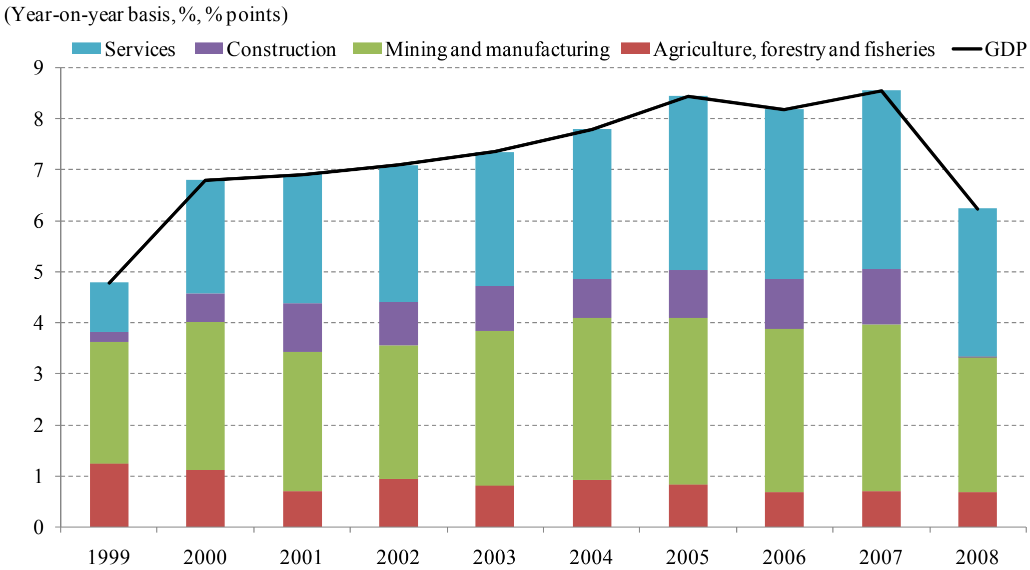
Vietnam, which gradually relaxed regulations on a variety of industries following its accession to the WTO in January 2007, abolished restrictions related to the retail sector in January 2009. This expands room for retailers and services providers to explore a new market and raises hopes for a further increase in investment opportunities for manufacturers of such products as daily necessities and foods.

Figure 1-2-5-23 Vietnamese employees' wages by industry



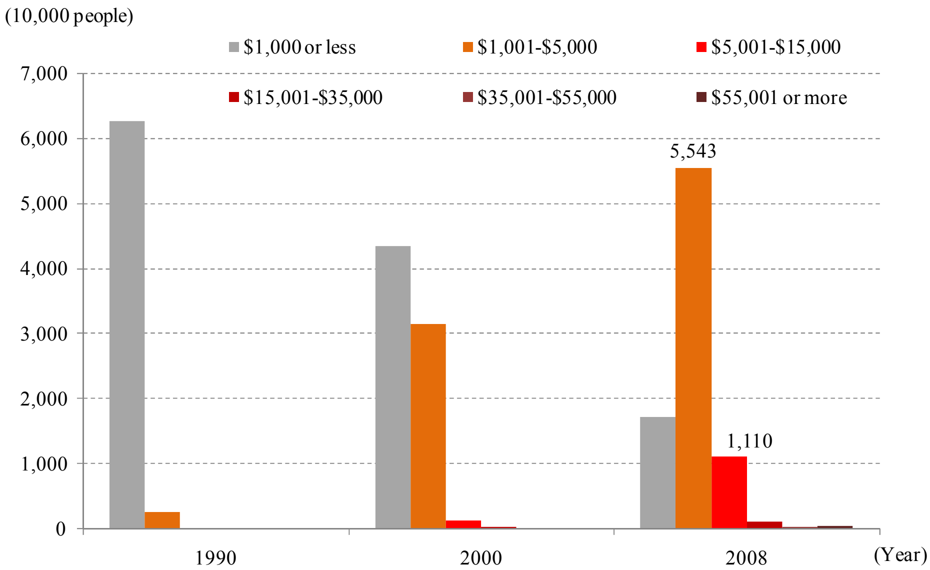
Notes: 2007 figures are estimates.
Source: General Statistics Office of Vietnam.

Figure 1-2-5-24 Percentage contribution to Vietnam's real GDP by industry



Source: CEIC Database.

Figure 1-2-5-25 Vietnam's population by size of household disposable income



Source: Created by Nomura Research Institute using data from *World Consumer Lifestyle Databook 2009*, issued by Euromonitor International.

(d) Economic stimulus measures

Under a five-year plan for 2006 to 2010, the Vietnamese government has set the goal of achieving an average annual GDP growth of 7.5 to 8% and increasing nominal GDP in 2010 by a factor of 2.1

compared with 2000.[133] In a session of the National Assembly in October and November of 2008, a GDP growth target of 6.5% in 2009 was approved. Judging that the impact of the world economic crisis would have a larger impact than previously expected, the Vietnamese government announced a one-billion-dollar economic stimulus package at the end of 2008 in order to spur demand. In a session of the National Assembly in May 2009, a downward revision of the GDP growth target to around 5% was proposed. In the same month, the Vietnamese government revealed a 143-trillion-dong (around ¥760 billion) economic stimulus package comprised of seven measures, including an interest subsidy scheme (around ¥91 billion), a temporary withdrawal of funds for infrastructure development (around ¥18.2 billion) and the issuance of additional government bonds (around ¥107 billion).

(D) Thailand

Thailand facing an export slump and political instability

Thailand has a population of some 67 million people, equal to around half of Japan's population, of which some 15% are concentrated in Bangkok and its metropolitan area. Thailand's industrial structure, which had centered on agriculture,[134] began rapidly industrializing around the second half of the 1980s, as a result of the entry of companies from developed countries into the country in pursuit of preferential treatment of investment and low-cost labor. Thailand exports computers and related parts, automobile and auto parts and integrated circuits to the United States, Japan, China and NIEs. In 2007, it exported automobiles and auto parts totaling around $12 billion, equivalent to some 8% of the overall exports. Japan is Thailand's largest source of imports and its second largest export destination. Japan exports electrical appliances, steel products and automobiles to Thailand and imports electrical machinery, rubber and foods from it.

(a) Impact of the financial and economic crisis

The Thai economy was underpinned by strong growth in exports until 2007 despite a slowdown in consumption and investment caused by political instability as well as inflation and high interest rates. Although exports, especially those to emerging economies, remained strong in the first half of 2008, Thailand's trade balance swung into a deficit because of an increase in imports of consumer goods and capital goods[135] due a recovery in domestic demand and an increase in the value of imports due to an upsurge in crude oil prices.

After the outbreak of the financial and economic crisis, GDP contracted 4.2% in the fourth quarter of 2008 as a result of declining net exports and fixed capital formation. Although the contribution of net exports to GDP turned positive in the first quarter of 2009, real GDP contracted even more sharply, by 7.1%, as the negative contribution of fixed capital formation widened and the contribution of private

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[133] This goal was set before the outbreak of the financial crisis. The World Bank forecasts GDP growth of 5.5% for Vietnam in 2009 in "East Asia & Pacific Update — Battling the forces of global recession" (April 2009). The IMF and the ADB forecast GDP growth of 4.75 and 4.5%, respectively.

[134] Although agriculture accounted for 25% of GDP in 1970, the ratio was down to 11% in 2007. However, the population of farmers is still large.

[135] Thailand imports crude oil, machinery and related parts, chemical products, integrated circuits, etc. from countries like Japan, China, the United States, Malaysia and the UAE.

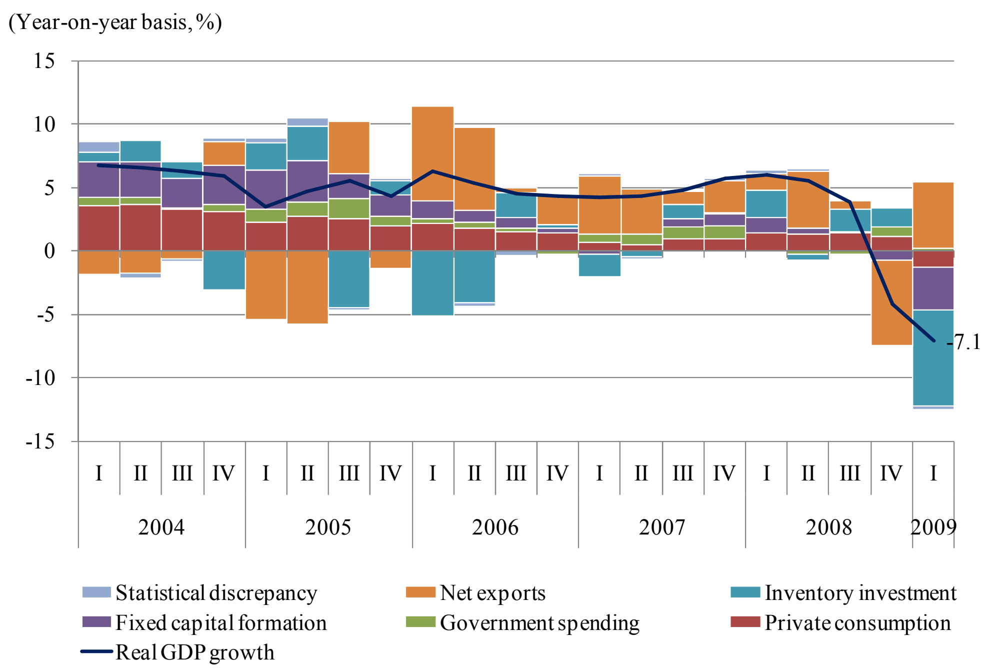
consumption turned negative (see Figure 1-2-5-26).

Growth in the value of exports started to slow down in August 2008, and the value declined steeply in November. For all items, the value of exports dropped, with electric appliances and machinery, which account for some 30% of the overall value of exports, and natural rubber posting a sharp drop due to a decrease in demand from the United States, Japan and China, all of which are major export destinations for Thailand (see Figure 1-2-5-27).

The manufacturing industry accounted for around 35% of Thailand's GDP in 2008, which stood at around $270 billion. However, the manufacturing production index has declined because of a slowdown in growth in exports caused by the global economic downturn (see Figure 1-2-5-28).

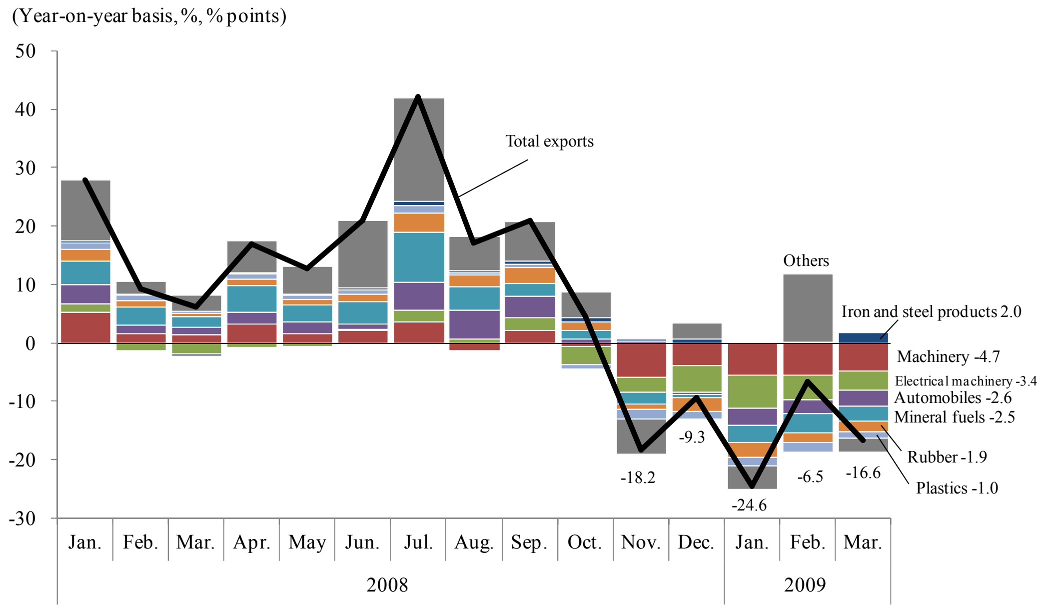
Political turmoil as exemplified by anti-government demonstrations is continuing in Thailand on and off, and this is expected to continue to have a significant impact on consumption and investor sentiment.

Figure 1-2-5-26 Thailand's real GDP growth and percentage contribution by demand component



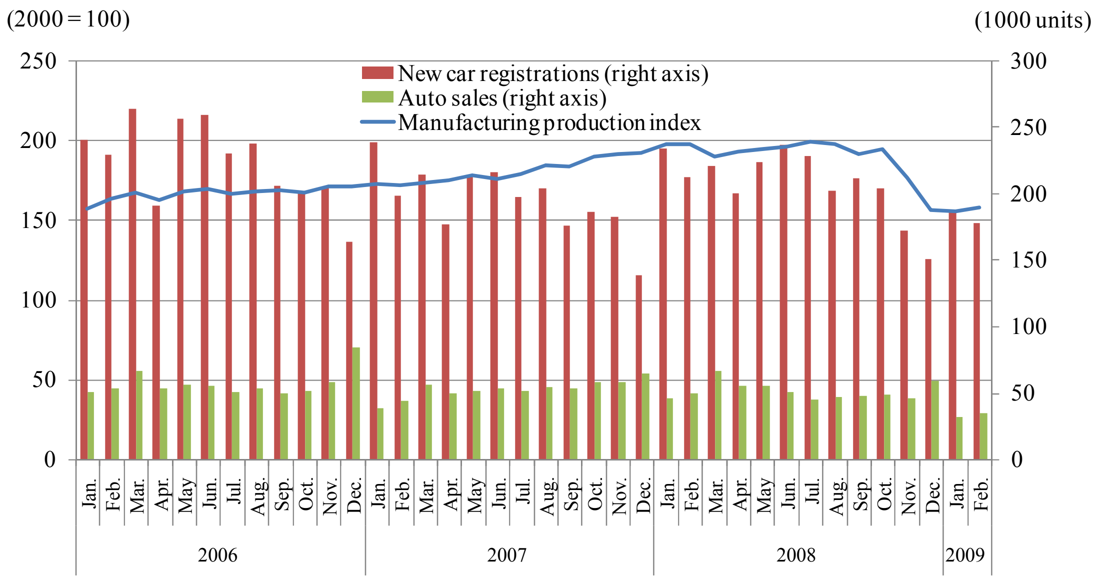
Source: National Economic Social Development Board of Thailand.

Figure 1-2-5-27 Changes in Thai exports and percentage contribution, by type of major product



Notes: In Thai baht.
Source: World Trade Atlas.

Figure 1-2-5-28 New car registrations and auto sales in Thailand



Source: CEIC Database.

(b) Economic stimulus measures

The Thai government has announced a series of economic stimulus measures, including support measures for low-income people worth 116.7 billion baht (around ¥320 billion), such as the provision of fixed-amount benefits and exemption from utility fee payments; tax cuts totaling 40 billion baht (around ¥110 billion), such as corporate tax reduction and tax breaks for home purchases by individuals and tourism promotion; and borrowings of external loans totaling some 70 billion baht (around ¥200 billion) for the implementation of public works and a government guarantee scheme to facilitate fund-raising by small and medium-size enterprises. The Thai government also regards it as an important task to revive the consumption and investment that have been significantly dampened by the political instability since the beginning of 2006. In addition, it is devoting efforts toward the promotion of investment and tourism through infrastructure development projects, including the development of the Bangkok Mass Transit System, and the Thailand Investment Year and Tourism Year campaigns.

The National Economic and Social Development Board forecasts GDP growth of between −2.5 and −3.5%[136] for Thailand in 2009, while the World Bank predicts growth of −2.76%.[137]

(c) Japanese-owned companiescompanies operating in Thailand

As a result of the Thai government's policy of actively inviting foreign capital, the business operations of Japanese automakers and electric and electronics products manufacturers are heavily concentrated in Thailand. The auto industry is the largest industry for Thailand. Production of automobiles in Thailand by Japanese automakers,[138] which started in the 1960s, has grown steadily as parts manufacturers as well as U.S. and European automakers followed suit in advancing into the country, thereby leading to industrial agglomeration. Japanese direct investment in Thailand amounted to around $550 million (December 2008), accounting for 25% of direct investment from around the world.

(E) Malaysia

Malaysian economy maintaining firm growth despite the impact of the economic crisis

Malaysia is a federal country with a predominantly Muslim population. Its area is roughly the same size as Japan (around 330,000 square kilometers) and its population is a quarter the size of Japan's population (around 27 million people).

After Malaysia became independent of the colonial rule of the United Kingdom in 1957, the agricultural and mining industries, including rubber plantation and tin and natural gas mining, prospered in the country for a while. However, under the leadership of Mahathir bin Mohamad, who took office as Malaysia's Prime Minister in 1981, the country shed its dependence on tourism and exports of agricultural products and mineral resources, and achieved economic development as an industrial ASEAN country.[139] Malaysia is an emerging country with GDP totaling $222 billion, and in terms of per-capita GDP, it comes fourth in Asia with $8,141, after Japan, South Korea and Singapore. Since the 1980s, Malaysia's economic development has been driven mainly by the manufacturing industry (electric and electronic products), and Japanese-owned companies have used the country as a base for exports. As of April 2009, a total of 1,435 Japanese-owned companies (741 manufacturers and 694 non-manufacturers) had business

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136 The forecast was announced on May 25, 2009.

137 The forecast was announced on April 7, 2009.

138 Initially, automobiles were produced under a knock-down system, which refers to the assembly of imported parts at a local factory.

139 Then Prime Minister Mahathir advocated the "Wawasan 2020" initiative ("wawasan" is the Malay word for vision), which aimed at turning Malaysia into a developed country by 2020.

operations in Malaysia.[140]

While Mr. Mahathir was prime minister, Malaysia adopted the policy of promoting domestic production in a variety of sectors.[141] In recent years, Malaysia especially promoted IT infrastructure development and support for domestic companies[142] in a bid to become an advanced IT-oriented country, and this effort has brought about some benefits, including growth of IT-related local industries.

Moreover, Malaysia is constructing the Multimedia Super Corridor, a comprehensive development with a cutting-edge IT infrastructure, around the capital city of Kuala Lumpur. The corridor includes Cyberjaya, a high-tech industrial zone that serves as the core of the corridor, Putrajaya, an administrative city where the prime minister's residence and government buildings are located, the Kuala Lumpur International Airport, which is the country's new air gateway, and Sepang International Circuit, a facility located within the airport where the F1 Malaysia Grand Prix is held.

(a) Impact of the financial and economic crisis

The Malaysian economy has maintained average annual growth of around 6% for the past five years, led by strong private consumption. In 2008, the services industry, including the wholesale and retail sectors, as well as the financial and insurance industries held relatively firm although their growth slowed down. However, the manufacturing and mining industries contracted in the fourth quarter of 2008 due to a slowdown in exports caused by the world economic crisis. Consequently, the economy remained almost flat in the fourth quarter, with real GDP growing only 0.1%. For the whole of 2008, real GDP growth came to 4.6%.

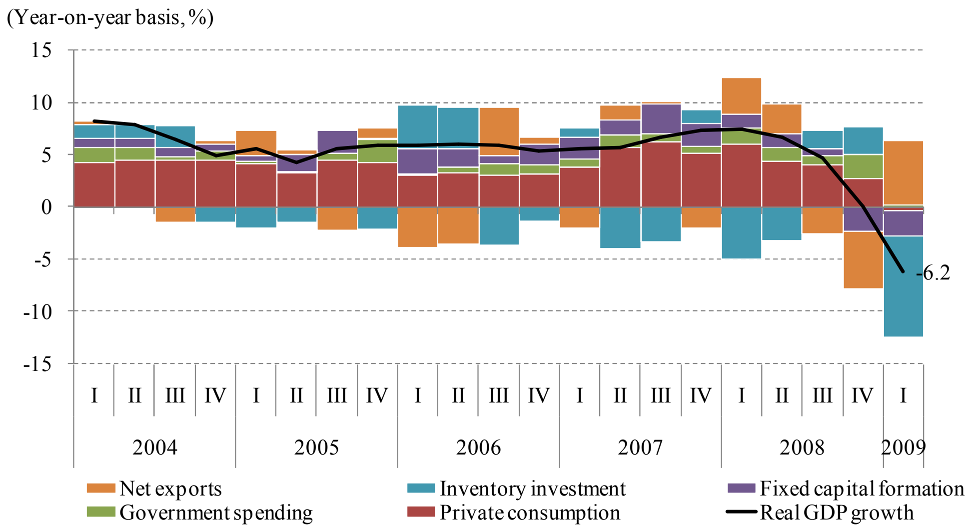
In the first quarter of 2009, real GDP contracted 6.2% because of a decline in exports and a slump in private consumption in addition to the shrinkage of the manufacturing industry (see Figures 1-2-5-29 and 1-2-5-30).

[140] A survey by the JETRO office in Kuala Lumpur

[141] Proton, which makes automobiles in Malaysia based on technology introduced from Mitsubishi Motor Corp of Japan, and Perodua, a manufacturer of small cars which introduced technology from Daihatsu Motor Corp, also of Japan, export automobiles to other Asian countries and European countries.

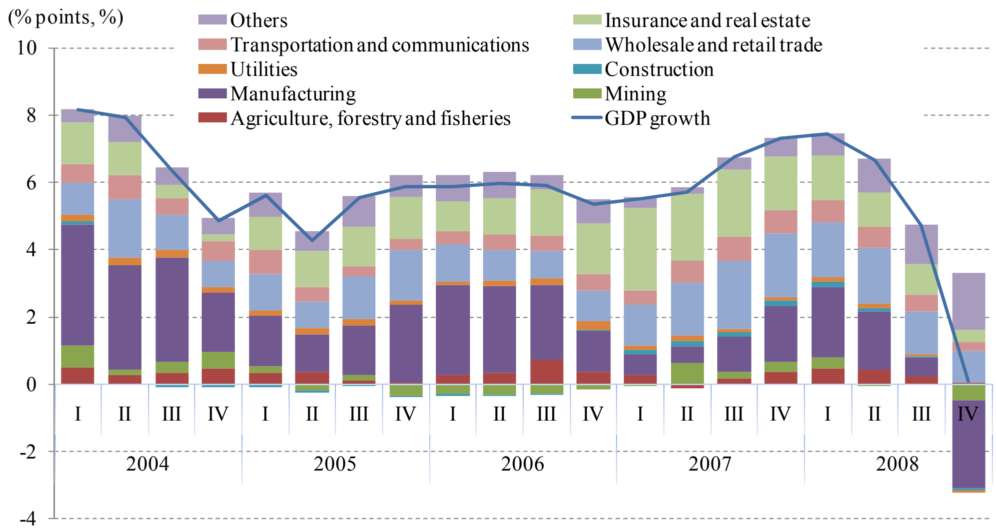
[142] It is well known that Dell Computers of the United States selected Malaysia as its Asian production base because of infrastructure improvements made by the Malaysian government.

Figure 1-2-5-29 Malaysia's real GDP growth and percentage contribution by demand component



Source: Central Bank of Malaysia.

Figure 1-2-5-30 Malaysia's real GDP growth by industry

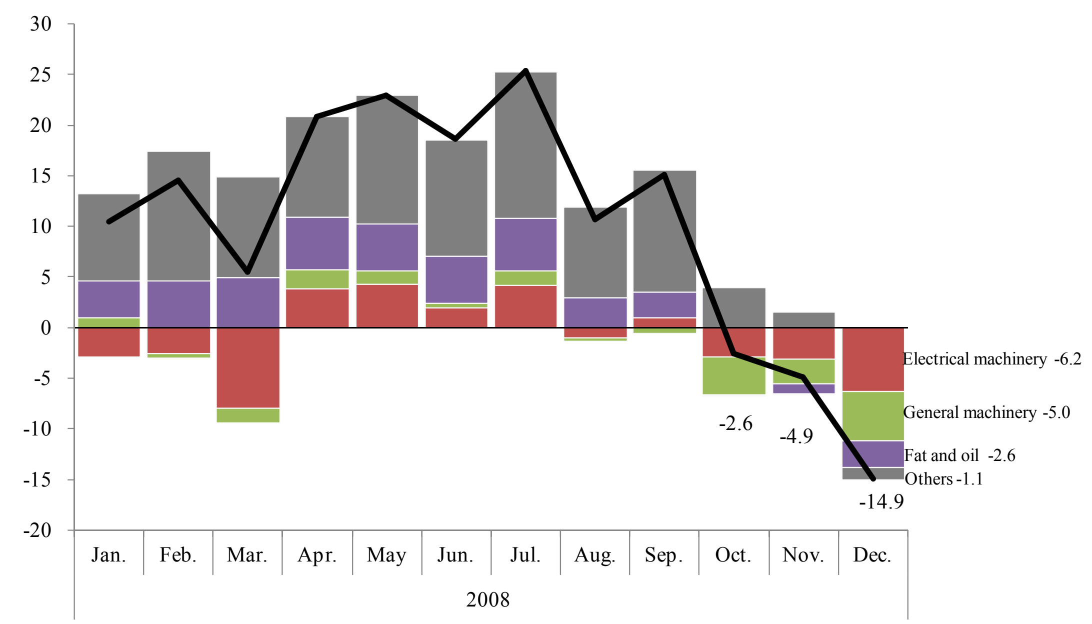


Source: CEIC Database.

Malaysia has posted a trade surplus for the past 10 years, with the value of both exports and imports increasing some 70% over the past five years. While an increase in the value of exports in crude oil and natural gas reflects an upsurge in natural resource prices, the value of exports of integrated circuits, which account for 13% of the overall value of exports, has grown 33% over the past five years and the value of exports of computers, which accounts for 9%, has risen 68%.

However, after continuing to grow strongly, Malaysia's exports declined in October 2008. This was attributable in large part to a decline in the value of exports of industrial products bound for the United States, China and Hong Kong, including electric appliances and machinery, and natural resources bound for China, such as palm oil, rubber and crude oil (see Figure 1-2-5-31).

Figure 1-2-5-31 Changes in Malaysian exports and percentage contribution by type of major product



Notes: In Malaysian ringgit.
Source: World Trade Atlas.

According to the Malaysian Industrial Development Authority, inward direct investment in the manufacturing sector rose to a new record high of 62,785 million ringgits (¥1,884 billion based on an exchange rate of ¥30 per ringgit) in 2008, boosted by a series of large-scale projects concerning products with high value added. Foreign direct investment projects related to the metals product sector and the electric and electronics sectors, especially solar power generation, are increasing. The largest investing country was Austria, followed by the United States and Japan in that order.

Although Malaysia maintained steady economic growth as shown above, its real GDP contracted sharply after the outbreak of the financial crisis last year as a result of a steep drop in external demand triggered by the global economic downturn. Moreover, a rise in wages associated with economic development has made its economic management tricky in recent years.

(b) Future potential of Malaysia

Because of Malaysia's fairly well-developed human resources and rising labor costs, the target of investment in the Malaysian industry is shifting from simple assembly operations to more advanced fields.[143] As Malaysia is a multi-racial country with a pool of human resources adept in languages spoken

[143] U.S. companies operating in Malaysia have advanced into the country mainly because of the country's advantage in distribution and IT infrastructure and English proficiency, rather than because of its manufacturing skills.

in major Asian markets, such as China and India, some Japanese-owned companies use Malaysia as a base for product development and after-sales services for the region. Given the diversity of races and religions in Malaysia and the deep penetration of Japanese-owned companies and products into the country, there are presumably more business opportunities for Japanese-owned companies.[144]

In addition, as an international office for Islamic finance[145] is located in Kuala Lumpur, Malaysia is also expected to serve as a window for Islamic finance.

(4) Greater Mekong Subregion (GMS) Program

In 1992, the Greater Mekong Subregion (GMS) economic cooperation program, whose members comprise six countries in the Mekong region, namely China (Yunnan province), Myanmar, Laos, Thailand, Cambodia, and Vietnam, started under the initiative of the Asian Development Bank. Currently, development projects are underway in nine fields: (i) transport, (ii) telecommunications, (iii) energy, (iv) the environment, (v) human resource development, (vi) trade, (vii) investment, (viii) tourism and (ix) agriculture.

The GMS program’s basic concept is to identify major economic corridors in the region and give priority to the development of those corridors. The program aims to achieve economic growth for the entire region through efficient development of cross-border infrastructures. It includes plans for the construction of power and telecommunications infrastructures, development of mineral resources and establishment of free trade areas and industrial zones in addition to the construction of transportation infrastructures, such as roads and bridges, and some projects are already underway.

1. North-South Corridor: Kunming (China)–Bangkok (Thailand)
2. Eastern Corridor: Kunming (China)–Ho Chi Minh City (Vietnam)
3. East-West Corridor: Mawlamyine (Myanmar)–Danang (Vietnam)
4. Southern Corridor：Dawei (Myanmar)–Qui Nhon/Vung Tau (Vietnam)
5. Southern Coastal Corridor: Bangkok (Thailand)–Nam Can (Vietnam)
6. Central Corridor: Kunming (China)–Sihanoukville/Sattahip (Cambodia)
7. Northern Corridor: Fangcheng (China)–Tamu (Myanmar)
8. Western Corridor：Tamu (Myanmar)–Mawlamyine (Myanmar)
9. Northeastern Corridor: Nanning (China)–Bankgkok/Laem Chabang(Thailand)

An expansion of transport options in the Mekong region to include land transport using trucks and railways in addition to air and ocean transport is expected to bring about significant benefits to East Asia’s

[144] As Malaysia is a multi-racial country whose inhabitants include ethnic Malays, Chinese and Indians as well as Vietnamese and Filipino emigrant workers, the country is regarded as a suitable place for research and development of products adapted to the local tastes of various Asian markets. In addition, a network of human connections formed in Malaysia may be used for sales activity in other countries. Therefore, Japanese-owned companies are pinning hopes on Malaysia, where sentiment toward Japan is favorable, as an important source of human resources and a reliable partner in promoting the internationalization of their business operations.

[145] The Islamic Financial Services Board (IFSB) was established in 2002 mainly by Islamic countries in the Middle East and other regions. Its secretariat office is located in Malaysia. The IFSB comprises 24 full members, mainly the central banks of Islamic countries, and 19 associate members, including the IMF and the World Bank, and 142 observer members, including JBIC. It conducts studies on such matters as the unification of rules and standards concerning Islamic finance.

industrial network, including reduction of the lead time for raw materials and products.

In 2006, the construction of the Second Mekong International Bridge, which forms a part of the East-West Corridor, was completed through Japanese ODA.

On the other hand, it is necessary not only to support infrastructure in tangible form, such as road construction and improvement, but provide intangible support. For example, in the Greater Mekong region, customs and quarantine procedures, both of which are usually implemented twice, once in the exporting country and once in the importing country, need to be implemented only once, either in the exporting country or in the importing country, under an arrangement known as single-stop customs and quarantine clearance, based on the Cross-Border Transport Agreement.[146] In addition, there is a system that allows trucks carrying cargos loaded at the exporting country to enter the importing country without re-loading in order to reduce the time for customs clearance, thereby facilitating cross-border transport. For the efforts to facilitate customs clearance, it is necessary to support the drafting of agreements, the installation of equipment and training of customs officials.

The economic development of Cambodia, Laos and Myanmar, which are apparently underdeveloped, compared with other ASEAN countries, is important for the development of the entire Mekong region. It is necessary to support these countries in human resource development and industrial development in addition to infrastructure development.

(5) Integration of the ASEAN economy

The ASEAN countries are preparing to establish the ASEAN Community. The ASEAN Charter took effect in December 2008, and this is expected to represent a step toward the establishment by 2015 of the ASEAN Community, which centers on security, economic and socio-cultural cooperation.[147]

In the field of economy, intra-region economic integration is accelerating in line with the deepening of the integration of the AFTA (ASEAN Free Trade Area)[148] and the signing of FTAs and EPAs with countries outside the region. Japan signed an EPA with ASEAN in 2008, and its EPAs with Singapore, Laos, Vietnam, Myanmar, Brunei, Malaysia and Thailand have already taken effect.

ASEAN signed FTAs with Australia and New Zealand in February 2009, in addition to FTAs with China and South Korea. With India, ASEAN signed an agreement on commodity trade and an agreement on the dispute settlement mechanism in December 2008 and aims to conclude an agreement on services trade and investment by the end of 2009.

Column 7 Asian currency crisis and global economic crisis: South Korea coping with second shock wave

South Korea, whose status fell to one of the world's poorest countries in terms of per-capita GDP after it was devastated by the Korean War, achieved remarkable economic growth known as the

[146] The Cross Border Transport Agreement (CBTA) includes 17 annexes and three protocols.
[147] The goal of establishing the ASEAN Community was declared at the Ninth ASEAN Summit in 2003.
[148] The six founding member countries of ASEAN are scheduled to abolish intra-regional tariffs on most items by 2010 and the other four member countries are scheduled to do so by 2015.

"Miracle on the Han River" through economic assistance provided by Japan and the United States, among other countries, and continuous efforts made jointly by its own public and private sectors, including an export promotion policy.[149] In the meantime, South Korean companies studied the practices of Japanese-owned companies and introduced the Japanese business model as exemplified by long-term employment, a seniority-based pay system and cooperative management-labor relationship.

However, the South Korean economy was effectively placed under the control of the IMF after receiving an IMF emergency loan amid the Asian currency crisis of 1997. South Korean companies were forced to implement drastic restructuring as a result of structural adjustment measures under an austerity program prescribed by the IMF. This is said to have given an impetus for South Korean companies to shift to the U.S. model of manufacturing. In particular, companies affiliated with conglomerates introduced a results-oriented evaluation system and promoted the consolidation of businesses under a top-down initiative. As Samsung Electronics and LG Electronics made intensive investment in technologies related to consumer electronics products, they succeeded in establishing their own brands and captured larger market shares than Japanese manufacturers in many countries.[150] On the other hand, the decline of family-based management has undermined social stability and brought about serious social problems related to the widening social gap and the absence of social safety nets. One example is an increase in a class of low-paid workers known as the "880,000 won generation."

After quickly recovering from the economic contraction of 6.9% in 1998 that was caused by the Asian currency crisis, South Korea posted growth of 9.5% in 1999 and 8.5% in 2000. Over the period through 2007, its annual economic growth averaged 5.6%. Meanwhile, its export dependency ratio exceeded 40%,[151] with semiconductors, automobiles, mobile phones, computers and ships growing as major export items. Although sales of these items were hit hard by the current world economic crisis, the contribution of their net exports to GDP growth remained positive because of a sharp drop in imports.[152]

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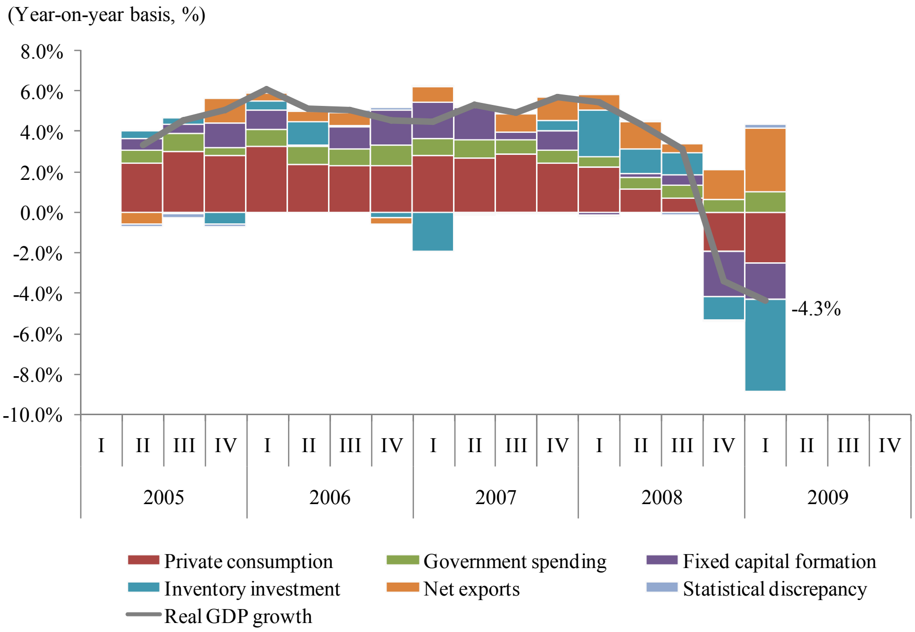
[149] South Korea achieved annual average economic growth of 8.6% between 1962 and 1979, and 8.0% between 1981 and 1997. South Korea's nominal GDP in 2008 stood at some $950 billion, about a fifth as large as Japan's.

[150] For example, Samsung Electronics of South Korea had the largest share of 21.5% in the global TV set market in the January-March quarter of 2009, followed by LG Electronics, also of South Korea, with a share of 13.3%, according to Display Research, a U.S. research company.

[151] United Nations, "National Accounts Main Aggregates Database." The export dependency ratio represents the ratio of the value of exported goods and services to nominal GDP.

[152] South Korean exports have quickly recovered because of the won's weakness, leading to a record trade surplus in March.

Column Figure 7-1 Korea's real GDP growth and percentage contribution by demand component



Source: Central Bank of Korea.

South Korea's GDP contracted at an annualized rate of around 20% in the fourth quarter of 2008, representing the largest contraction among Asian economies, although the country posted a trade surplus. To cope with the economic crisis, the South Korean government announced the Green New Deal initiative, with total expenditures of 50 trillion won (around ¥4 trillion), and a plan for drastic structural adjustments of the shipbuilding and construction industries (under which companies are rated on a scale of A to D, with companies rated D to be urged to go out of business). Meanwhile, the South Korea government is continuing to try to halt the vicious circle of corporate restructuring and concerns over job security weakening domestic demand by introducing measures to support job sharing.

The South Korean economy, like the Japanese economy, is dependent on exports, and the two countries' social systems are similar in many aspects. Measures taken by the South Korean government and companies may provide useful lessons for Japan.