Chapter 2 Japan growing with Asia's development – Asia –Pacific framework toward sustainable growth
Section 1 : Asia increasing its presence in the world

2. Asian economy that shows quick recovery

While the developed countries such as the U.S. and European countries are expected to gradually recover from the recession affected by the global financial crisis, the Asian economy already started demonstrating a significant improvement in the second quarter of 2009 (see Figure 2-1-2-1).

The recovery of Asia can be broadly divided into two patters. As for export-dependent countries including Singapore and Thailand, real GDP growth showed a significant minus growth in the first quarter of 2009. Then, in the fourth quarter of 2009, their year-on-year growth rates came back to the level of prior to the global financial crisis registering 6.0% in Korea, 4.0% in Singapore and 5.8% in Thailand. Japan is expected to turn to a positive growth driven by the growth of Asia including vigorous China in 2010[2].

On the other hand, countries such as India and Indonesia that are relatively less export-dependent and have stable domestic demand did not fall in to a negative growth and is growing to the pre-crisis level. India's growth rate of the third quarter of 2009 was a 7.9% increase from the previous year. The year-on-year growth rate of the fourth quarter of 2009 in Indonesia was 5.4%. Moreover, China has achieved the high growth marking 11.9% of year-on-year growth rate in the first quarter of 2010 backed by expanding investment and consumption.

(1) Each country's economic stimulus measures that contributed to the increase of demand in Asia

Each country in Asia including China implemented large-scale economic stimulus measures mainly in the form of public investment and subsidies and stimulated investment and consumption to increase demand. As a result, it achieved swift recovery ahead of other regions in the world.

The ratio of the government expenditure for economic stimulus plans to GDP was 6.0% in Japan and 13.3% in China. The ratios were higher in Asia compared to the average of 2.2% in the U.S. and European developed countries (see Figure 2-1-2-2).

Economic measures of major Asian countries are described below (see Table 2-1-2-3).

(A) Japan

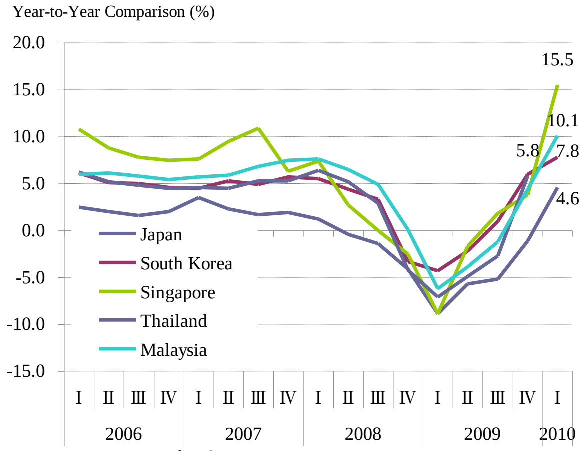
From August 2008 to December 2008, total about 7.5 trillion yen of economic stimulus programs were implemented divided into three times to provide the support to household through the payment of cash benefit, the employment measures and the financing support for small-to-medium businesses. The economic stimulus measures of April 2009 executed low-carbon related projects including the promotion of the introduction of solar power use and the promotion of replacement for

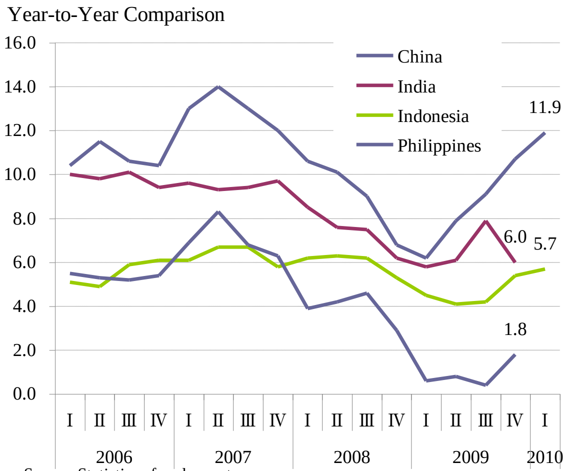
---

2 IMF "World Economic Outlook 2010" forecasts Japan's real GDP growth in 2010 to be 1.7%. Cabinet Office, Government of Japan, estimated Japan's real GDP growth for fiscal year 2010 to be 1.4% in its report, "HEISEI 22 NENDONO KEIZAIMITOUSHITO KEIZAIZAISEIUNEINO KIHONTEKI TAIDO"

environment-friendly car, the scheme to support parenting and the plan to assist the finance of small-to-medium businesses. The total expenditure was about 5.7 trillion yen and about 1.5 trillion was national expenditure. The economic stimulus measures of December 2009 include employment measures and extension of guarantee as government urgent economic measures. The total budget was about 2.4 trillion yen and about 7 trillion yen was allocated from the national budget.

2-1-2-1 Real GDP Growth Rates of Major Asian Countries



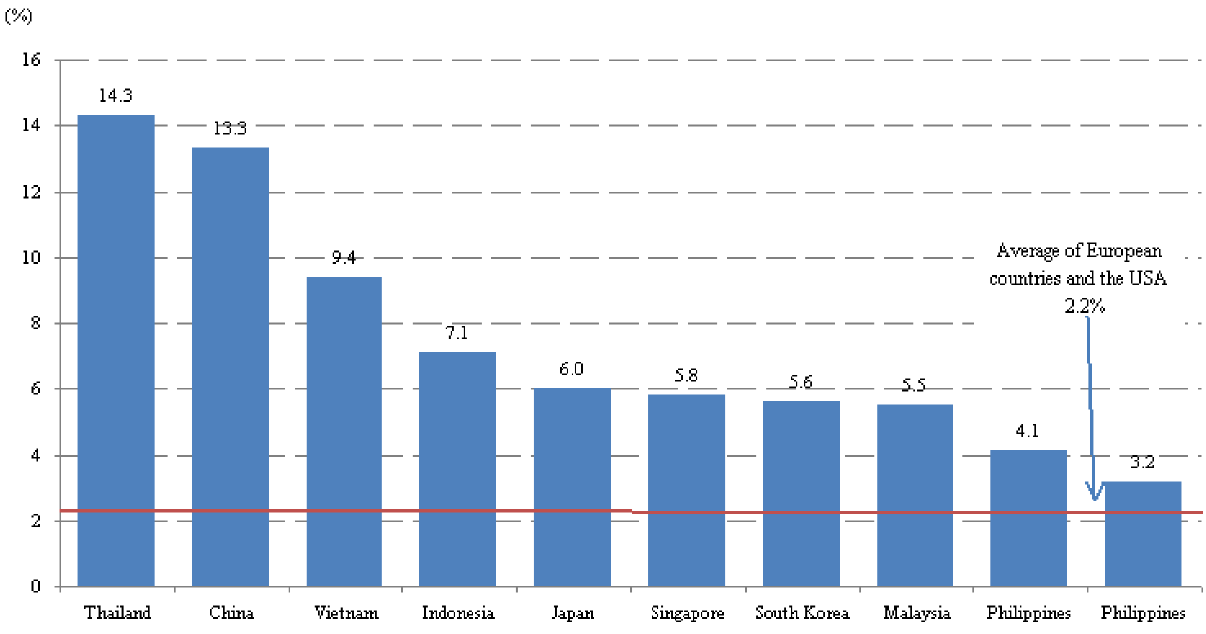


Source: Statistics of each country
Note: The figures for Thailand include values until the fourth quarter of 2009.

Quarter of the year

Source: Statistics of each country
Note: The figures for India and Philippines include values until the fourth quarter of 2009.

2-1-2-2 Fiscal Expenditure of Countries based on Economic Policy (as Prop. Of GDP)



Note: "European countries and the USA" includes the USA, Canada, 15 countries of EU(except Greece and Ireland), Norway and Switzerland.
Source: UN "World Economic Situation and Prospects 2010"

(B) China

On November 2008, Standing Committee of State Council of the People's Republic of China announced “10 measures for the promotion of domestic demand and the development of economy[3]”

---

3 The project areas include (i) housing construction for the low-and-moderate income segment as a social insurance measure, (ii) infrastructure development in rural areas, (iii) large-scale infrastructure development such as railroads, roads, airport and power plants,

that plans to spend 4 trillion yuan by the end of 2010. The government also released a policy to promote 10 major industries including automobile and steel industry as well as plans to stimulate consumption by extending subsidiaries to purchase home electronic appliances and automobile with "Home Electronics Appliances Subsidy Program in Rural Areas" and "Rural Auto Subsidy". On December 2009, Standing Committee of State Council of the People's Republic of China decided to extend the consumption stimulus plan and added "Building Material Subsidy Program" that provides subsidies for the purchase of building material in the rural areas.

(C) Korea

On November 2008, the Korean government released "Comprehensive measures to conquer the economic difficulties" worth 14 trillion won including government spending of 11 trillion won and tax cut of 3 won to recover the economy that quickly deteriorated after the financial crisis. Subsequently, the government announced "Green New Deal" policy on January 2009. This is to invest total investment amount of some 50 trillion (to be exact, 50,049.2 billion won) won in 9 core projects and 27 related businesses that are expected to create some 960,000 of job opportunities. Further more, 28.4 trillion of fiscal year 2009 additional revised budget (additional economic stimulus measures) was approved in April 2009. Moreover, to support domestic demand, the government also executed tax cut for automobile individual consumption tax (December 2009 to June 2009) and tax reduction to promote the replacement with new cars (May 2009 to December 2009).

(D) Thailand

In January 2009, Thailand announced 116.7 baht of economic stimulus package that includes job training for employed people, public investment such as railroads, roads and airports, agricultural infrastructure development, energy-efficient car promotion through the reduction of import tariff, cash benefit provision to the low-income group and small-to-medium business support enhancing the application of the lowest tax rate. Later in March, the government announced an economic stimulus project, "Strong Thailand 2012" of which budget amounts 1,430.0 billion baht planning to implement in 3 years from October 2009.

(iv) promotion of health and medical services and cultural and educational programs, (v) facilitation of living environment, (vi) self-motivated innovation and structural adjustment, and (vii) disaster rehabilitation for the areas hit by the earthquake.

2-1-2-3 Economic Policies and Financial Expenditure by Major Asian Nations

	Economy-Boosting Measures	Amount of Financial Expenditure ($ 100 million)
Japan	・Supplementary Income Payments / Tax breaks (e.g. Raising the upper limit of deduction amount in income-tax break for new homeowners) / Employment measures / Measures for cash-flow problem of small and medium sized companies ・Low Carbon Emission Revo	2,975
China	・Measures for domestic demand expansion ・Measures to stimulate consumption such as purchase aid (including tax break) for home electrical appliances and vehicles	5,853
South Korea	・Comprehensive economic measures (expansion of finance expenditure and tax break) and employment support by supplementary budget ・Public project with Green New Deal Program ・Support for financial stabilization	534
India	・Lowering of commodity tax / Support for exporting companies / Support for investments for infrastructures / Support for home purchase ・Relaxation of regulations on loan from foreign financial organization / capital infusion to state-run bank	384
Thailand	・Support for small and medium sized companies / Measures to stimulate real estate market ・Support for job creation / Fixed-amount benefits to low-income earner	390
Malaysia	・Support for private companies and investment to infrastructures ・Construction of low- and middle- priced houses and development of local infrastructure	121
Indonesia	・Tax cuts (income tax and corporation tax) / Lowering of electricity rate for industrial use ・Public project / Investment to infrastructures etc.	71
Singapore	・Protection of employment and support for companies as "Recover Package" ・Support for financing of companies / support for financing to small and medium sized companies (e.g. expansion of credit line and government guarantee)	106

Source: Ministry of Economy, Trade and Industry "Tsusho hakusho 2009 (Trade White Paper 2009)" / Cabinet Office "Sekai keizaino choryu - June 2009 (Trends of the World Economy - June 2009)" /UN "Economic Situation and Prospects 2010"

(E) Malaysia

Malaysia announced two economic stimulus packages in November 2008 and March 2009. The budget was allocated in the construction of low-to-medium price range housing and the development of infrastructure in rural areas.

(F) Indonesia

In October 2008, the Indonesian government made an announcement on the 12.5 trillion rupia of urgent economic measures including the redemption of national bonds and foreign currencies. In February 2009, the government approved a supplement budget that covers infrastructure development through public investment as well as the measures for companies including the reduction of corporate tax and the subsidy for import tariff, value-added tax and energy-cost, and the plans to support consumers such as tax cut including the reduction of income tax. The size of this budget and the urgent economic measures totals 73.3 trillion rupia.

(G) Singapore

The government enhanced the loan commitment and government guarantee to small-to-medium businesses to 2.3 billion Singapore Dollar to support the corporate financing. In the fiscal year 2009 budget, 20.5 billion Singapore Dollar of “recovery package” was allocated to provide employment guarantee which subsidizes 12% of monthly salary to employers, job training, business support such as the reduction of corporate tax and household support through the redemption of commodity tax and service tax.

(2) Trend of industrial production in Asia

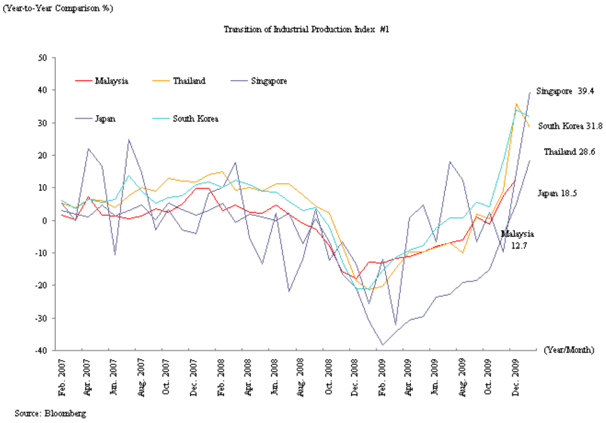
In each Asian country, industrial production is recovering due to the demand increased by the consumption stimulus measures (see Figure 2-1-2-4). In China, the policy to subsidize home electronic appliances pushed up the demand for devices and panels. Particularly in Korea and Taiwan, China-bound exports and production of IT-related products substantially improved. In addition, in China, it is considered that the increase of demand for construction material stimulated by the economic measures also contributed for the production increase. In Korea, tax cuts resulted in the expansion of automobile production. Singapore demonstrated the rebound of production of non-IT related items such as chemical products as well as IT-related production. Furthermore, weak won and strong yen supported the increase of Korean companies' market share in the world and Korea's production recovered ahead of Japan.

(3) Invigoration of trade in Asia led by China

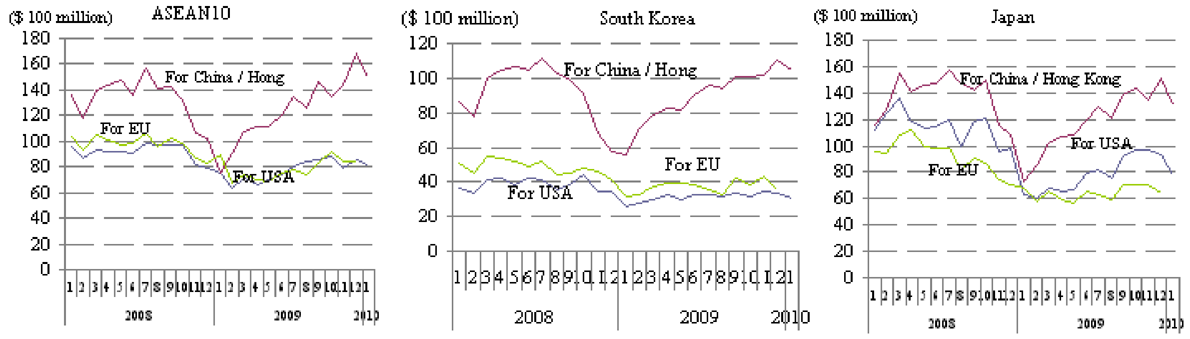
China's economic measures have been giving a great impact on not only China itself, but also the economy in Asia. The exports from ASEAN, Korea and Japan to China, the U.S. and EU shows that the exports of each country and region to the U.S. and China are sluggish, however, China-bound exports started recovering in 2009 (see Figure 2-1-2-5).

The economic stimulus plan of each country is invigorating the trade in the area, mainly the one with China, making the ties among countries strong. The trade ratio within Asia started increasing in 2009 and registered 53% in October 2009 exceeding the level prior to the global financial crisis.

2-1-2-4 Trends in Industrial Production for Major Asian Countries



2-1-2-5 Trends in Exports to China, the US and the EU of Major Asian Countries/Regions



Source: World Trade Atlas

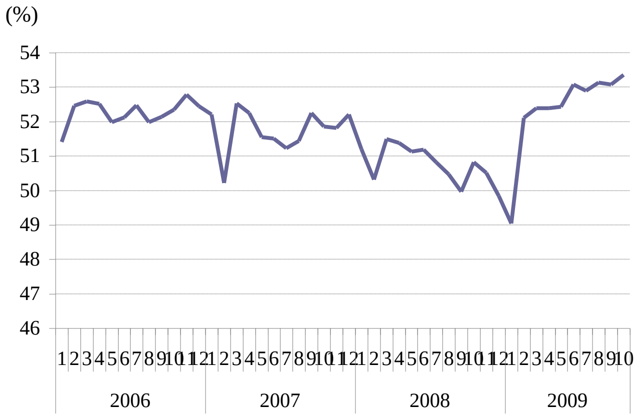
Furthermore, the analysis of China imports using the breakdown of Chinese statistics on general trade excluding raw materials and processing trade reveals that the gradual recovery of processing trade that imports parts to China to assemble and export to the U.S. and Europe. General trade (raw material is excluded) of which final consumption market is assumed to be the China's domestic market has been expanding with a faster pace than that of processing trade since February 2009 (see Figure 2-1-2-7).

In light of the above, the increase of exports from ASEAN, Korea and Japan to China is considered to be the results of the expansion of general trade that would be consumed in China's domestic market rather than the increase of processing trade destined for the U.S. and Europe. While it is necessary to pay attention to the sustainability of the effect of China's economic stimulus measures, the analysis indicates that the domestic demand of China is enlarging.

In China, the source of the rapid recovery of final product imports is the economic growth in inland areas. China's 4 trillion yuan of economic stimulus measures which have been implemented since November 2008 focuses the development of infrastructure in the inland areas. In 2009, the real GDP growth of Chungching city, Sichuan province and Shensi province considerably exceeded the China's total average of 8.7% marking 14.9%, 14.5% and 13.6% year-on-on increase respectively (see Figure 2-1-2-8). On the other hand, the substantial drop of exports affected by the global financial crisis resulted in the lower GDP growth of export-dependent areas including Shanghai city, Zhejiang province and Canton province compared to that of inland areas.

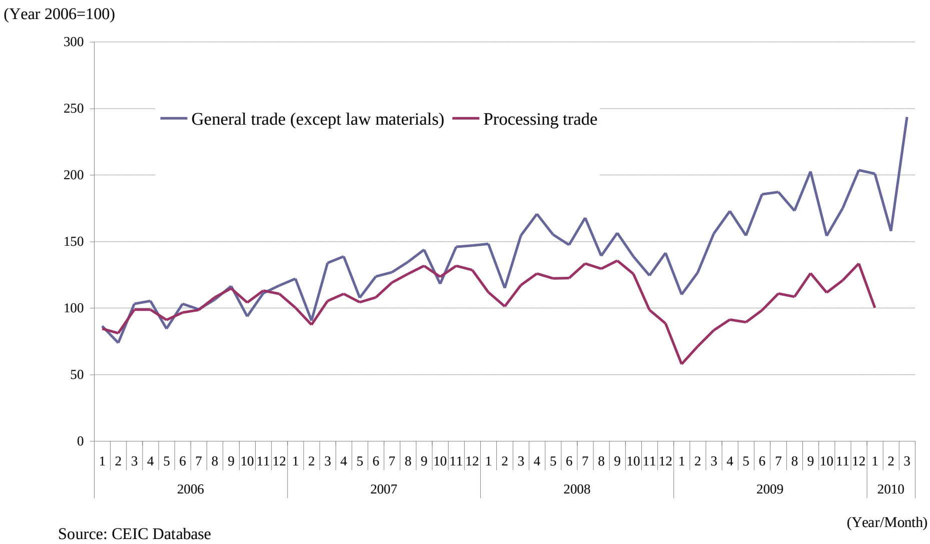
Furthermore, due to the recovery of the demand in Asian emerging countries, China's exports of final products to ASEAN and India have been showing positive year-on-year growth since August 2009 registering a 42.7% increase in December 2009 (see Figure 2-1-2-9). While China's exports to Asian emerging countries are enlarging, the recovery of its exports to the U.S. and EU is delayed.

2-1-2-6 Trends in Asian Trade Ratios



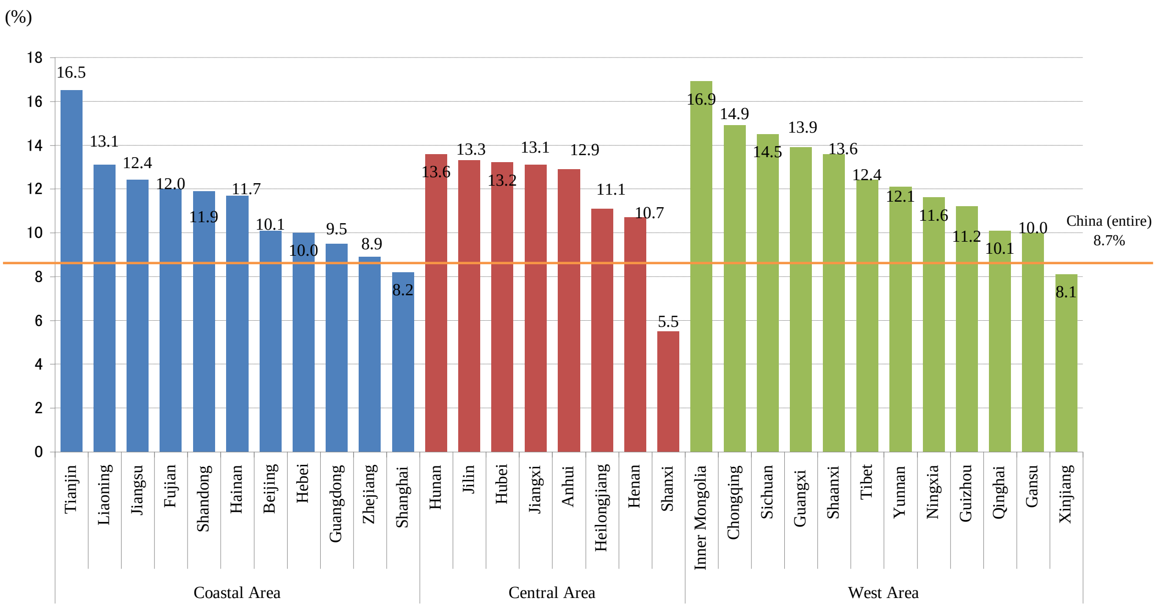
Note: "Asia" includes ASEAN and 6 countries.
Source: IMF "Balance of Payments Statistics" / Global Trade Information Services

2-1-2-7 Trends in Chinese Imports by Item



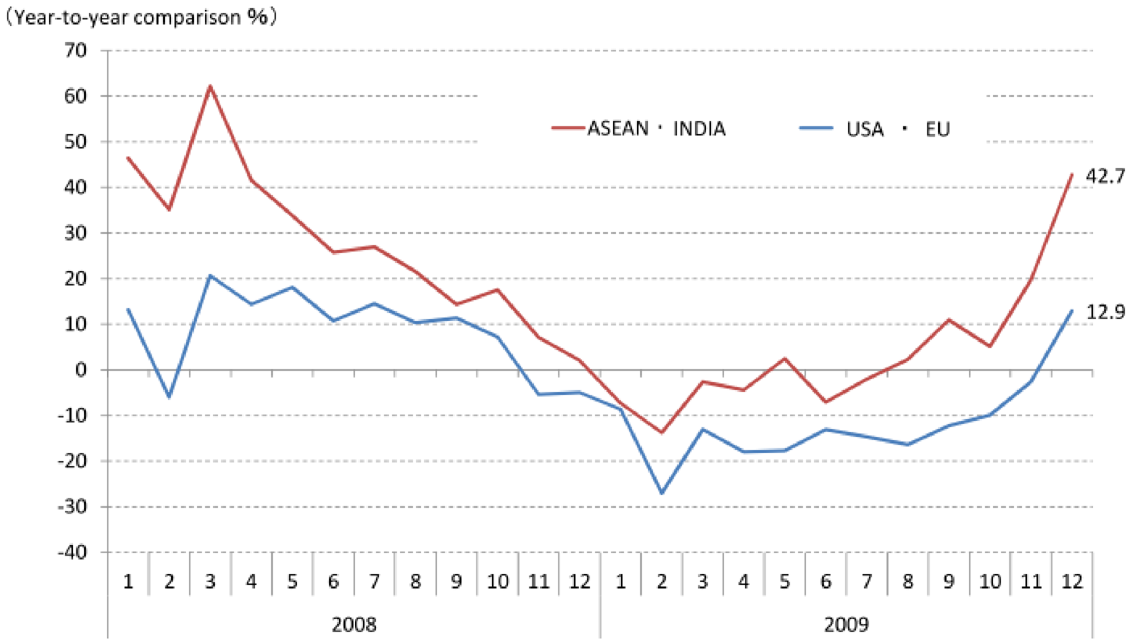
Source: CEIC Database

2-1-2-8 Real GDP Growth Rates by Region in China (2009)



Source: CEIC Database

Figure 2-1-2-9 Final exporting activity depending on areas in China



Source : World Trade Atlas

It is estimated that about 60% of Asia's total final product exports are bounded for Japan, U.S. and Europe[4]. In China where is considered to be the final assembly base of Asia, its total exports eventually turned to a positive growth in December 2009 demonstrating its slow pace of the recovery. The upturn of the economy of Japan, the U.S. and EU is the preconditions for the full-scale recovery of the Asian economy. In the medium-to-long term, Asian countries are required to change their economic structure to achieve their economic growth not only with external demand but also along with the domestic demand. Therefore, it is expected that Asian countries continue their effort to expand domestic demand.

(4) Expansion of investment in Asia

Financial stabilization policy of each country with capital infusion and government guarantee is reducing the uncertainty of the financial markets and supporting the recovery of the global capital flow. The outward direct investment and securities investment in Asia are increasing and the capital flow to the Asian financial markets that had less impact of the global financial crisis is accelerating (see Figure 2-1-2-10). Moreover, Asian currencies including Korean won and Indonesian rupia are improving overcoming the large drop after the global financial crisis (see Figure 2-1-2-11).

While these investment and capital infusion are expected to serve as the engine for the growth of the Asian economy, each country's move on monetary policy is gaining attention due to the concern for property price hike and asset inflation in some areas.

---

[4] Estimated by ADB with Global Trade Analysis Project (GTAP) Database, 2004

(5) Asia to start tightening its monetary policy

Each Asian country had been lowing policy interest rates under the monetary relaxation policy provided along with the government expenditure. However, the governments started seeking exist strategies and some countries raised policy interest rates due to the concern for asset inflation such as rising inflation expectations and increasing property prices and the recent upward trend of consumer prices (see Figure 2-1-2-12).

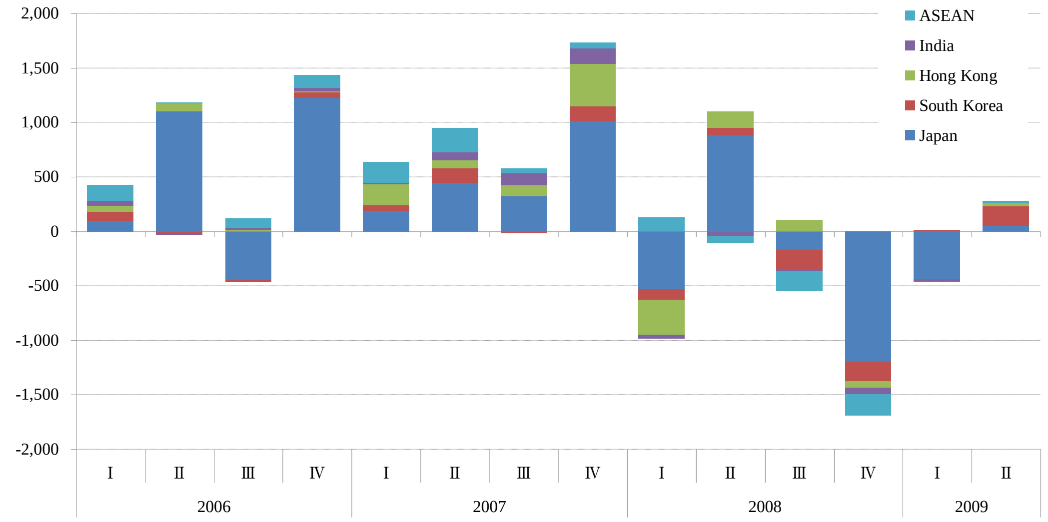
Followings section summarizes major Asian countries' move on monetary policy.

(A) China

China had been taking credit easing measures lowering policy interest rates since the second half of 2008. In December 2009, China announced a policy to continue "adequately relaxed monetary policy" at the Central Economic Work Conference that decided "Microeconomic Foundations of Economic Policy" for 2010. Meanwhile, the People's Bank of China has increased reserve requirement by 0.5% each in January, February and May. Although policy interest rates have not been changed, there is a move for phased monetary tightening.

2-1-2-10 Trends Flow of Securities Investment for Major Asian Countries (Net)

($ 100 million)

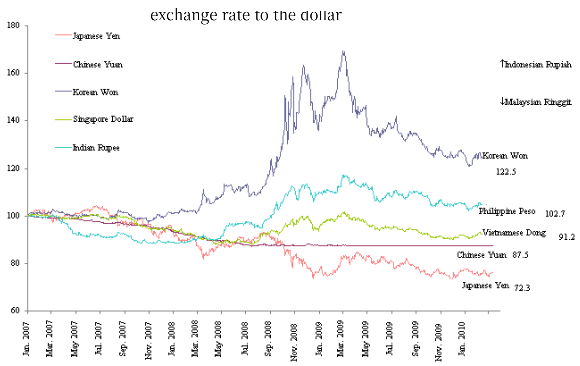


(Year/Term)

Note: "ASEAN" includes Indonesia, Thailand (until 2009I), Malaysia (until 2008IV), Singapore (until 2008IV), Philippines and Vietnam. Figures for India is until 2009I.
Source IMF "BOP"

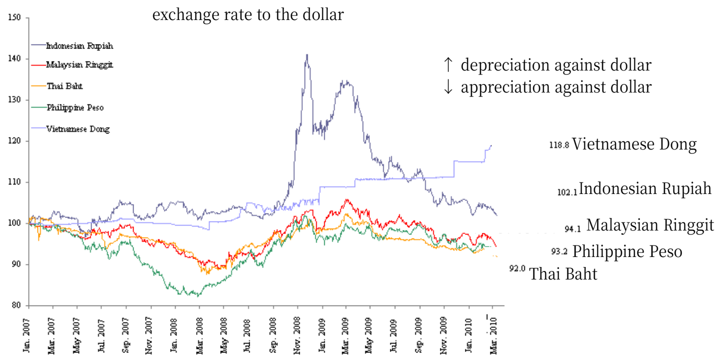
2-1-2-11 Trends in Exchange Rates of Major Asian Countries

(1/1,2007=100)



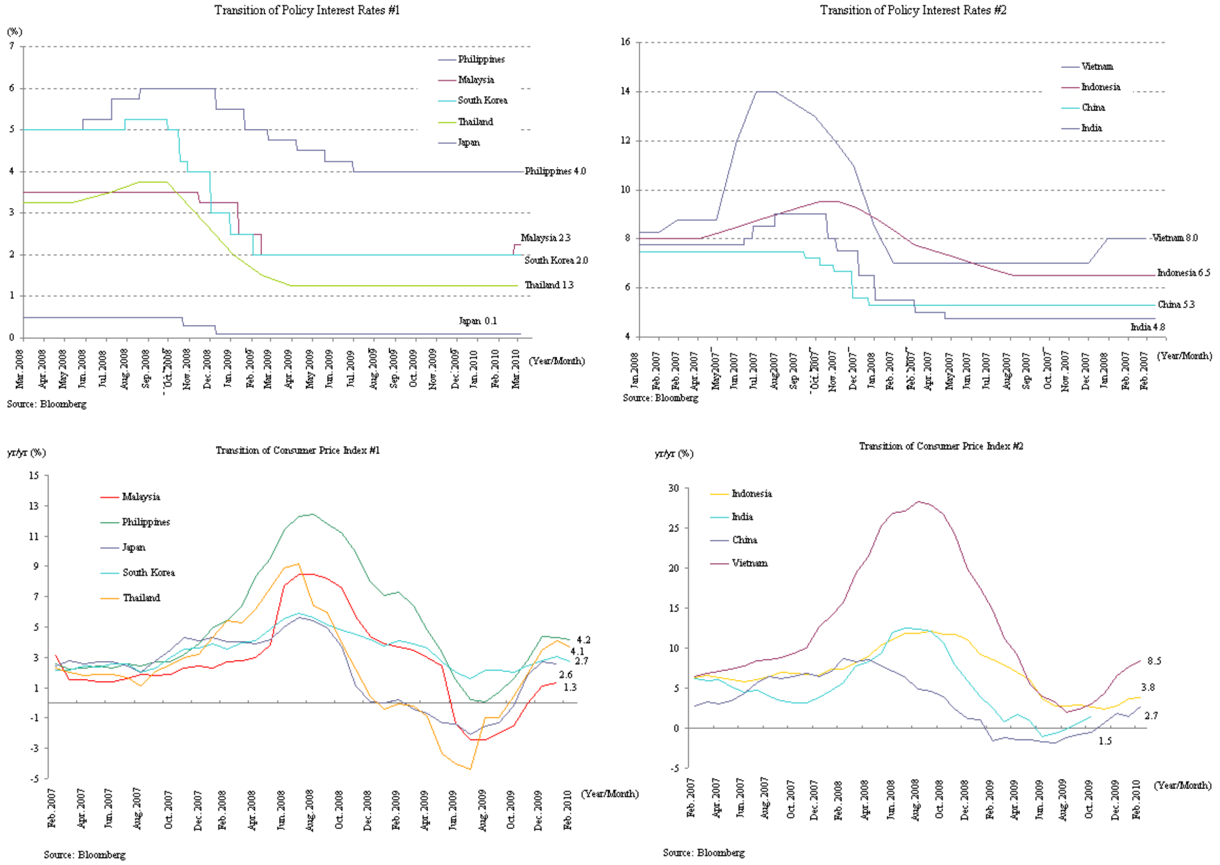
Source: Bloomberg

(1/1,2007=100)



Source: Bloomberg

2-1-2-12 Trends in Policy Interest and Consumer Price Index in Major Asian Countries



(B) Korea

The Bank of Korea (central bank) set up its policy interest rates at the record lowest of 2.0% in October 2008 and has been maintaining the level since then. At the policy-making meeting of November 2009, considering the situation that the domestic production is at the peak of business cycle, the Governor of the Bank of Korea stated that “Sustaining low interest rates gives more beneficial impact on economy rather than negative influence” and decided to keep the monetary relaxation policy. In the same month, the Bank of Korea increased inflation target limit from 3.5% to 4.0%.

(C) India

India implemented monetary relaxation policy conducting policy interest rates cut from October 2008 to April 2009. However, the hiked food product prices have been pressuring price level to go up since the end of 2009. Therefore, the Reserve Bank of India increased reserve requirement by 0.75% in January 2010. Moreover in March and April in the same year, the Bank has raised the policy interest rates, repo rate, by 0.25% each for the two consecutive months and has been promoting the tightening of its monetary policy.

(D) Indonesia

After lowering policy rates to 6.5% in August 2009, the Central Bank of republic of Indonesia has been maintaining this rate since the consumer prices are within its inflation target of 2010 which is 4 to 6%.

(E) Malaysia

In Malaysia, the policy interest rates were raised by 0.25% each in March and May 2010 to 2.25% backed by the recovery of the world economy and the improved domestic economy after the period from October to December 2009. Inflation is expected to show a moderate upward trend, however, foreign capital inflow is increasing. Therefore, Malaysia is likely to promote the stabilization of monetary policy continuously through small step increase of interest rates.

(F) Thailand

The Bank of Thailand that lowered policy interest rate to 1.25% in April 2009 is maintaining the level. Although there is less concern for the deceleration of economy, the Bank judges the current level is adequate considering the world economy trend and domestic risk factors.

(G) The Philippines

The Central Bank of the Philippines maintains current policy interest rates projecting inflation rate would be within a target and economic recovery slowly proceed. The authority announced its stance to maintain current monetary policy since the inflation rate is within the assumed range and there is no clear sign for the self-sustaining economic development supported by domestic demand.

As for the timing to shift to monetary tightening policies, generally speaking in case of developed countries, while an output gap[5] is wide, an inflation rate will likely stay low. Therefore, central banks will have enough reserves to maintain their monetary relaxation policies. On the other hand, when emerging countries are practicing monetary relaxation policies over the long period of time, they will face different risks compared to that of developed countries. For example, the capital inflow from foreign countries that expect the high economic growth of emerging countries may increase the risk for property bubble. In light of the above, it is pointed out that many emerging countries should end the monetary relaxation policy sooner than developed countries[6] and it is important to keep close eye on the course of the progress.

---

[5] While many factors influence on the fluctuation of prices, the most important determiner is basically considered as how much total demand actually exists against the supply in the economy as a whole. This gap between “the supply in the economy as a whole” and “total demand” is generally called “output gap” and serves as one of fundamental indexes to evaluate price fluctuation pressure.

[6] IMF “World Economic Outlook October 2009”