



Developed Asia Pacific: Economic Review September 2011

Export-driven growth in developed Asia Pacific under pressure

Developed Asia Pacific nations continued to face headwinds to growth in September. With factory output across the world slowing down to a trickle, major developed Asia Pacific economies ranging from Japan to New Zealand started witnessing pressure on their economic output. **As exports still act as the backbone for many of Asia's developed countries, a global decline in manufacturing is causing concerns.** A slowdown in the U.S. and Europe also cast a shadow on the economic prospects for Asian nations. The index of manufacturing activity in the U.S. compiled by the Institute of

At a Glance

- **Japan:** Revised second quarter GDP figures showed a deeper contraction in the economy. Output in the earthquake hit nation fell 2.1% for the second quarter ended June according to the latest reports. Previous reports showed only a 1.3% contraction in output during the second quarter.
- **Australia:** Although mining and energy investment rose, a slump in manufacturing resulted in unemployment climbing to 5.3% in August from 5.1 in July.
- **New Zealand:** Second quarter GDP rose just 0.1%, on lower exports and farm output, substantially lower than the 0.6% growth predicted by the central bank.
- **Hong Kong:** High rentals pushed consumer price inflation to 5.7%.
- **Singapore:** Non-oil exports jumped robustly by 5.1%, powered by ship-building and pharmaceutical output.



Supply Chain Management edged lower to 50.6, with any reading below 50 generally viewed as a contraction in manufacturing output. **With manufacturing growth slowing, even in the strongest of European economies such as Germany, Asian exporters of machinery and other critical electronics and automotive parts have started suffering.** Japan's trade ministry reported that exports from the country gained less than forecasted during August, as global demand came under pressure. Furthermore, leading Asian emerging economies that were supporting export growth from Asian powerhouses like Japan lost momentum during the month, while output from Taiwan and South Korea, which trade with Japan significantly, also showed signs of strain. Manufacturing indices in both countries dipped below 50, renewing concerns about a manufacturing contraction.

What's more, other countries such as New Zealand and Hong Kong reported slower-than-expected export growth. Although Australia's growth was supported by strong investments in the mining and energy sectors, the manufacturing industry continued to shed jobs primarily due to a strong domestic currency. **The only country among Asia Pacific's developed economies to show improvement in exports was Singapore, where heavy engineering industries such as shipbuilding supported output.** Nonetheless, even the city state could not avoid a significant slowdown in electronics output.

Japan: Strong yen pressures Japanese enterprises

Japan revised its GDP figures for the second quarter of 2011 ended June during early September. The revised data revealed that the country's GDP growth contracted 2.1% during the second quarter against earlier figures that showed a contraction of just 1.3%.

The revised data comes on the back of weak investment spending among businesses and a strong yen that is hurting Japanese exports. Machinery orders, which roughly indicate the demand for capital spending, had fallen substantially during the second quarter, reaching a 10-month low during July. The new data also indicated that capital spending actually declined 0.9% during the second quarter against earlier figures that showed a 0.2% jump. Furthermore, the Japanese yen, as of the last week of September, was still hovering around the post-war high of 75.19 against the U.S. dollar, despite a move by Japan's central bank in the currency markets to push the yen down.

The strength of the yen is proving to be a significant obstacle for many Japanese enterprises. Many companies such as Toyota, Panasonic and Nissan complained about the strength of the yen. As electronics and auto exports slumped, Japan's exports, a major contributor to the country's economy, increased only 2.8% in August against an 8% growth predicted by a group of 22 economists surveyed by *Bloomberg*.



A trade ministry's survey showed that large Japanese companies were worried about their profits as a strong yen continued to weigh on the bottom line. According to the survey, 15% of the companies estimated that their operating profits would be down 20% if the yen stood at around 76 per U.S. dollar. Some Japanese companies, such as Panasonic and Elpida, frustrated by erosion to their bottom line from a strengthening yen, announced that they are considering shifting their operations away from Japan.

Such a move from Japanese enterprises could not have come at a worse moment for the earthquake-hit nation. **Japan, which is struggling to boost consumption within the country, said that it will announce incentives and subsidies to prevent Japanese companies from shifting their operations to other countries.** The country's new Prime Minister Yoshihiko Noda announced that he is working on an incentive package for Japanese companies to build new factories within Japan. Mr. Noda's plan, which is expected to be unveiled along with a reconstruction budget to address earthquake-related damages, is widely expected to help the finances of small and medium scale industries as well.

Japan's new prime minister also proved to be more open to nuclear power, allaying concerns about an electricity crunch in the country. Naoto Kan, who was the prime minister of Japan before Mr. Noda took charge in September, had ordered the closure of nuclear reactors after a devastating tsunami in March caused the collapse of a nuclear power plant in Fukushima.

Public opinion had markedly swung against nuclear power generation in Japan in the aftermath of the Fukushima nuclear accident. Although Japan sailed through the temporary closure of other nuclear reactors during the summer, many industries, in particular carmakers, reported worries about uncertainties arising from a possible power crunch. However, Mr. Noda stressed the importance of nuclear power to Japan after becoming the country's prime minister. In an interview to *Bloomberg*, Mr. Noda said that he will devise a blueprint for bringing closed nuclear reactors back into operation to ensure a reliable supply of power.

In other developments, Japan signed the first-ever investment accord with Taiwan. The agreement is viewed as an inaugural step in establishing a free-trade deal between the two Asian economies. Japan's Ministry of Economic Affairs said that the Japan-Taiwan accord provides for cross-border investment protection between the countries, and seeks to promote and liberalize the business environment.

Australia: Decline in manufacturing offset by mining and energy investments

Australia's economy sent mixed signals about its strength during September. The first week of September started with good news when the country's Bureau of Statistics announced that



retail sales in Australia advanced 0.5% in July, the first instance of growth in the past three months. In June, retail sales had fallen 0.1% over the previous month. But July's higher sales were powered by a 1.2% jump in department store sales, as consumers loosened their purse strings to indulge in cafes and restaurants.

Another report from the agency also showed that capital spending for the second quarter ended June rose 4.9%. Major investments in the energy and the mining sector continued to provide some much-needed support to Australia, which has been suffering from a slump in manufacturing. A strong domestic currency, the Australian dollar, had affected the prospects of the country's manufacturing sector. But with major energy and mining companies like BHP Billiton and Chevron lining up billions of dollars to invest in the country, business investment was largely expected to go up according to a report from *Bloomberg*. Indeed, mining investment in the country zoomed 45% to A\$82.1 billion (\$84.3 billion) for the 12-month period ended June 30 as companies built more factories and bought new plants and equipment to exploit the country's natural resources.

However, data that were released during the middle of September painted a less bright picture of Australia's economy. **With manufacturing industries and tourism declining due to a strong domestic currency, consumer confidence in August hit the lowest point since the first quarter of 2009, according to CoreData, a research firm.** The company, which surveyed over 820 investors, reported that 80% of the group expected an economic slowdown and more than two-thirds expected business conditions to deteriorate for the rest of 2011.

The country's job market, which is under strain, has also been widely blamed for slumping business and consumer confidence. Australian employers continued to shed their workforce for the second straight month in August and the number of those employed fell 9,700. The Sydney-based Bureau of Statistics reported that the unemployment rate climbed to 5.3% in August up from 5.1% in July. This is the highest level of unemployment recorded in the past ten months. Australia's manufacturing sector, in particular, shed more jobs than other industries. While the country's largest beverage maker, Coca-Cola Amatil, closed a food-processing unit and terminated over 150 workers, steelmakers OneSteel Ltd and BlueScope Steel also alluded to a possible closure of blast furnaces, citing heavy competition from cheaper imports.

What's more, the job losses in the manufacturing sector are expected to spill over to other parts of the economy. One of the country's largest banks, Westpac Banking Corp, also said that it might downsize its operations if demand for credit does not grow in the coming months.

Meanwhile, the slowing economy and slumping consumer confidence are weighing heavily on inflation expectations, according to the country's central bank, the Reserve Bank of Australia (RBA). In mid-September, the central bank's governor, Glenn Stevens, said that global volatility and belt-tightening by Australian consumers are likely to "curtail" inflation in

the coming months. The RBA kept borrowing costs unchanged at 4.75% for the ninth straight meeting in September this year.

New Zealand: Business confidence slumps among New Zealand companies

New Zealand's economy slowed substantially during the second quarter of 2011 ended **June**. The country's GDP rose 0.1% during the quarter, much below the central bank's prediction of 0.6% growth. Weakness in the construction and manufacturing segments, in particular, affected growth. However, strong exports from the farm sector and a resurgent financial sector helped the economy during the second quarter.

But the momentum from the agriculture sector, which played a major part in boosting New Zealand's output in the eight months since the Christchurch earthquake in February, witnessed a seasonal slowdown. In August, New Zealand posted its first trade shortfall since February, primarily due to lower exports of farm-based commodities.

Agriculture and farm output, which contributes nearly 30% of New Zealand's economy, slowed substantially during August according to reports from Statistics New Zealand. Exports during August fell almost 27%, down from the peak of April. Still, New Zealand's imports of crude oil, electrical machinery and farm equipment rose during August, a sign of resurgent earthquake reconstruction efforts.

Despite the reconstruction efforts, the confidence level among New Zealand's businesses fell to its lowest-level in five months. In a survey by ANZ National Bank Ltd, companies expecting an improvement in business conditions dropped to 30.3% in September from 34.4% in August. Further, the number of companies expecting souring business prospects grew to the highest level in April.

Another measure of the survey showed that expectations for higher sales and profits among New Zealand companies fell to 35.4% in September from 43.3%. On the other hand, the labor market looked more buoyant. The survey, which was conducted with a sample of 474 companies, showed that employers are willing to hire more in the coming months. Corroborating this trend was a report from New Zealand's Department of Labour, which showed that the number of job vacancies advertised online jumped 6.3%. The number of vacancies for skilled jobs had climbed 3.9% from the previous month and 21.3% from the year-ago period.

The country's central bank, for its part, left interest rates untouched from a record-low of 2.5% during its September policy meet. The central bank's governor Alan Bollard stressed the



need to not only lower interest rates due to uncertainty in the global markets, but stimulate the housing sector at home.

Hong Kong: Consumer inflation continues to haunt the financial center

Hong Kong's property market, which was red-hot for the greater part of the past eighteen months, is showing some signs of cooling. The number of property transactions in Hong Kong fell to a 30-month low in July. Further, the competition among property developers to acquire land parcels from the government also dwindled. For instance, during June, the Hong Kong government called for an auction to sell a piece of land, and only one bidder was attracted. What's more, the bid price of HK\$5.5 billion was almost 33% less than the expected. Some of the country's property-based private-equity funds quoted by *Bloomberg* forecasted a 30% fall in rent for office buildings and a 20% slump in home values over the next two years.

The slowdown in the property market along with sluggish exports in the country has already led to a 0.5% contraction in the Hong Kong economy during the second quarter ended June. The slowdown is also spilling over into the labor market. Hong Kong, which is one of the largest financial centers in Asia, is expected to lose some jobs in the financial services industry. In early September, HSBC, Hong Kong's largest consumer bank in terms of customer deposits, said that it was looking to pare down its workforce in the regional headquarters over the next two to three years. The bank's preliminary reports showed that it might cut 3,000 jobs in Hong Kong during this period. Although, the labor market in the financial center held well during the May-July period, with unemployment falling to 3.4% from 3.5% in the April-June period, private economists surveyed by *Dow Jones* opined that the unemployment rate could inch upwards in the coming months.

Meanwhile, despite the slowdown in the economy, consumer price inflation continued to trouble Hong Kong, with inflation during August jumping 5.7% primarily due to high rentals. These high rental costs impacted food and other essential items, as restaurants and shops passed on the higher rental costs to customers. Adjusting for one-time subsidies, consumer price inflation during August climbed at the fastest pace since August 2008. With this, three prominent banks in the region trimmed their outlook for Hong Kong's economy for the rest of the year due to a combination of high inflation and slowing export growth.



Singapore: Heavy industries and pharmaceutical sector boost output

Singapore's strong and diversified manufacturing base propelled industrial output and growth for the month of August. The city-state, which years ago had diversified its manufacturing into industries such as ship building, pharmaceuticals, and optical instruments, is reaping rich dividends. In August, the country's non-oil exports jumped almost 5.1% despite a slump in electronics output. This was contrary to expectations for a 6.5% decline in exports predicted by a group of economists surveyed by Bloomberg.

In fact, the country's manufacturing output surged almost 21.7% despite weak output from the electronics industry. Manufacturing primarily drew its strength from the pharmaceutical sector, where output jumped almost 156%. Other heavy industries such as shipbuilding also powered the country's industrial output. Consequently, despite a 21.9% decline in electronics production, the country's industrial production surged 3.9%. A group of economists surveyed by Bloomberg had forecasted a 5% decline in industrial output for August. Singapore registered a fall in electronics output for August as demand from North American companies remained lukewarm. North American orders for semiconductor equipment declined 8.8% in August. Some of Singapore's top electronics contract manufacturing and assembling companies reported a drop in sales, while many chip-equipment toolmakers in the country witnessed slowing new business orders.

But despite the surge in industrial output, the country's policy makers remained cautious about the outlook for the rest of the year, given the volatility in Singapore's export markets. In mid-September, Singapore's Finance Minister Tharman Shanmugaratnam had warned that his country will not be immune to economic problems in the U.S. and Europe. Analysts from Bank of America Merrill Lynch also opined that Singapore could experience a significant fall in output.

Meanwhile, Singapore witnessed a bout of inflation along with a surge in industrial production during August. Although the prices of some energy commodities eased a bit, Singapore's consumer price index jumped 5.7% in August according to the Department of Statistics. Still, inflation during the month primarily came from domestic issues such as more expensive housing and food prices rather than imported inflation. Singapore, which uses the exchange rates of its currency to direct monetary policy, is scheduled to release its monetary policy course in October. The country so far has allowed its currency to strengthen to fight inflation. Singapore's central bank now expects consumer inflation to hover in the range of 4 – 5% rather than its preliminary estimate of 3 – 4%. 🌍

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