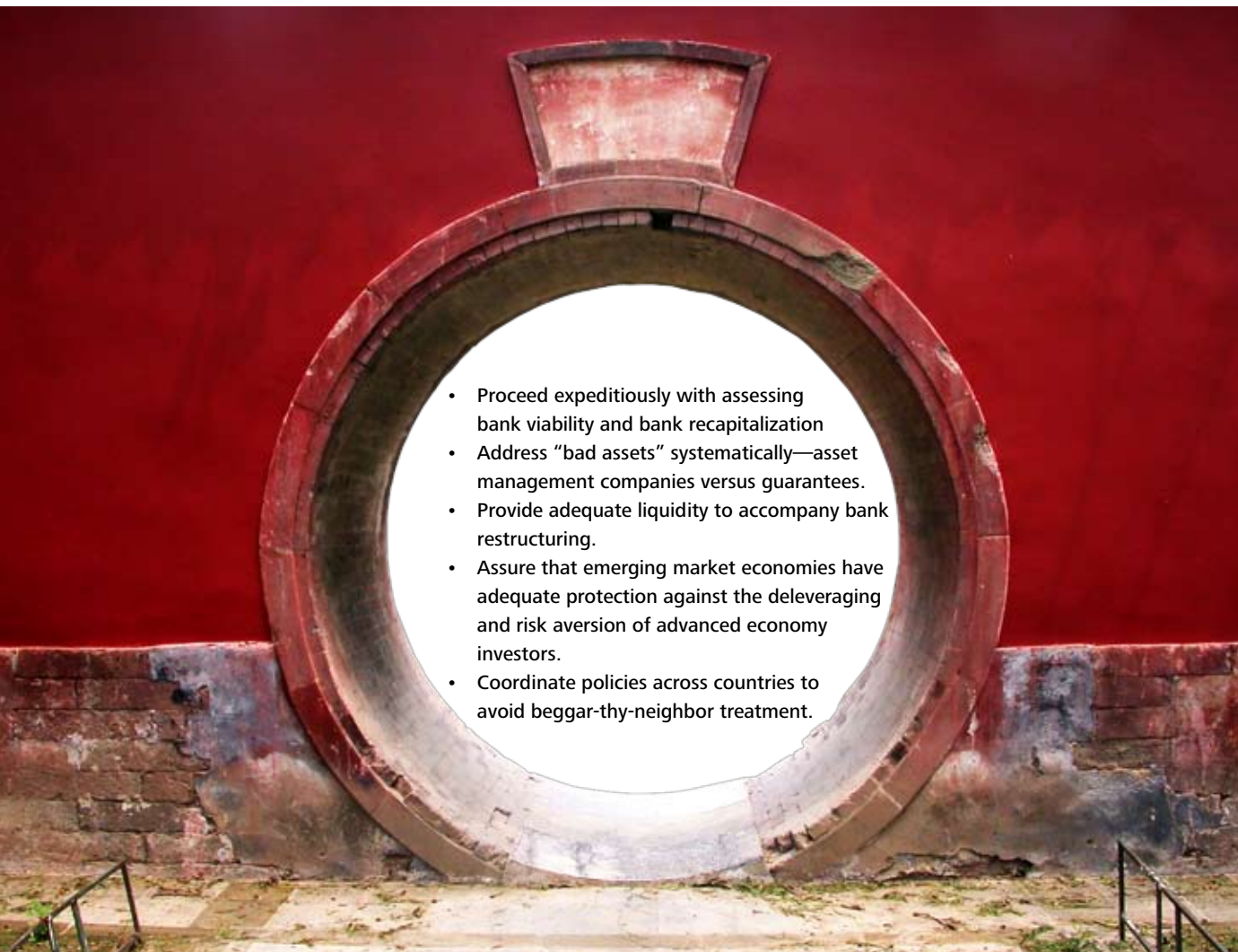


Asia Pacific
Economic
Outlook





- Proceed expeditiously with assessing bank viability and bank recapitalization
- Address “bad assets” systematically—asset management companies versus guarantees.
- Provide adequate liquidity to accompany bank restructuring.
- Assure that emerging market economies have adequate protection against the deleveraging and risk aversion of advanced economy investors.
- Coordinate policies across countries to avoid beggar-thy-neighbor treatment.

Recommendations of the IMF’s Global Financial Stability Report (April 2009) on policies that need to be implemented immediately

China

The Chinese economy is being seen as the bellwether for future economic growth worldwide: if the Chinese economy has a hiccup in growth, the rest of the world, particularly Asia will be in dire straits. Fortunately, that is unlikely to happen. The economy grew at 6.1 percent in 1Q09, well below the psychological comfort level of 8 percent, but there is optimism. One reason for that optimism — domestic consumption accounted for 4.3 percent of the 6.1 percent growth. It rose because consumers responded to the government’s use of the \$585 billion stimulus package to build a social safety net as well as incentives to buy cars, and consumer durables. Retail sales increased 14.7 percent in March compared to 11.6 percent in February. Car sales were also up 5 percent in March after a period of decline. Domestic consumption also grew because of the phenomenal rise in urban fixed-asset investment; it grew 28.6 percent in the first-quarter. Apart from spending billions on physical infrastructure projects, the government has directed banks to increase their lending. Banks extended credit worth approximately \$670 billion in the first quarter of 2009 — slightly less than their total lending in 2008 — leading to concerns of bad loans in the coming years. This increase in domestic consumption is leading to a rise in industrial production, which grew by 8.3 percent in March, slightly worse than the 11 percent seen in February but much better than the 5.7 percent in January. The relatively low industrial production growth number is because of the still weak export market, which contracted by 17.1 percent in March — its fifth straight contraction.

Export Growth (Percent YoY)



Source: Bloomberg



“Money Building”
Liaoning Shengyang, China

Looking forward, there are signs that the economy is improving, but on the back of government spending — infrequently a good thing in the long-term. The government is predicting a growth rate of 7–8 percent in 2009, while some investment banks predict it will be a little over 8 percent. For that to happen, growth in the last three quarters of 2009 will need to average approximately 8.5 percent, a tough deal at the given moment. That said, the government has ample money at its disposal should it want to pull off 8 percent growth in 2009; but it should,

however, be wary of getting the economy dependent on government money.

A leading indicator, the manufacturing purchasing managers index (PMI), has been on the up for a few months now, but the fear is that it is merely responding to government spending. The export sector is still fragile, there is substantial overcapacity and most importantly, the investment sentiment in

the private sector is still weak. This weak sentiment has the potential to derail the government’s efforts to boost

the economy, and is leading to a debate about whether China's growth pattern will be a 'V' or a 'W'. There is also a latent threat from the real estate sector, which has seen significant price drops; and though there are indications that purchases of houses are up, there is still substantial inventory that will need to be cleared before prices start rising. Rising unemployment is of concern, and remains a serious threat to any plans of sustainable growth.

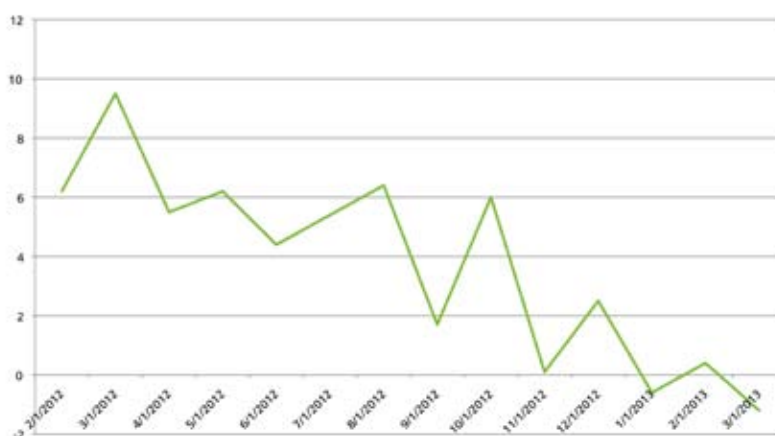
However, one-year forwards are at unusually high levels on speculation that the government may let the yuan appreciate further, an unlikely possibility.

India

Like China, India is also seeing some 'glimmers of hope'. However, in the case of India, these glimmers may be a bit illusory. The economy is slowing down but there are two problems: one, the government doesn't have money to execute fiscal stimulus, and two, the government is in the midst of elections. India's mammoth elections, which take place over a month, will be done on May 16th, and it will be some time before any new government puts a new stimulus plan in place. The current government has been hamstrung by election laws and accordingly hasn't been able to get new legislation issued in the past few months.

Exports have been falling sharply over the previous months; they fell 21.7 percent in February and 15.8 percent in January. Unlike South Korea, India has failed to capitalize on its depreciating currency and boost its exports, despite the rupee depreciating sharply. This has had a negative effect on the industrial sector, which shrank by 1.2 percent in February. This sector has seen lethargic growth since August 2008. The glimmer of hope, however, is the auto sector, which has been on an upward trend for the past few months, largely buoyed by deep interest rate cuts and the depreciating currency.

Industrial Production (Percent YoY)

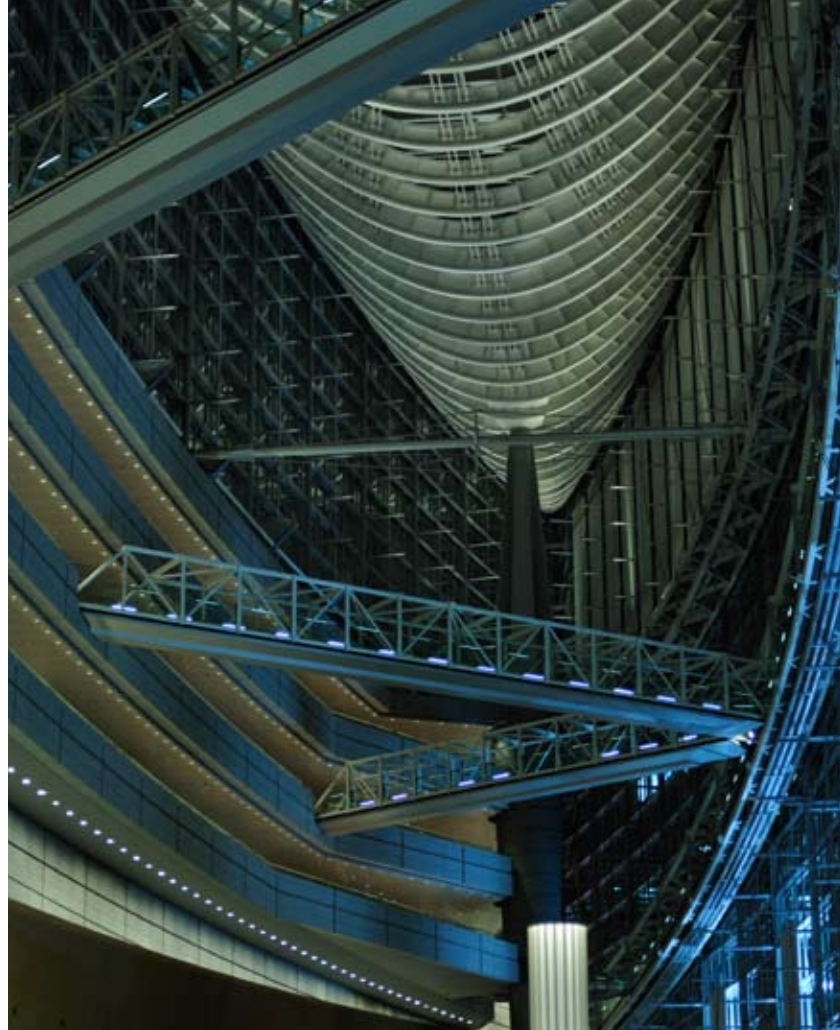


Source: Bloomberg

The Reserve Bank of India (RBI) has forecast that growth in FY10 will be 6 percent compared to the government's very optimistic forecast of 7 percent. The IMF's forecast

“The RBI has been cutting its benchmark rate, the repo rate, quite aggressively but banks, especially the private ones, haven't been as aggressive when cutting their lending rates, causing the RBI much heartburn.”

The People's Bank of China (PBC) has said that “relatively loose monetary policy should be conducted and policy consistency be maintained,” but it may slow down the lending effort or at least monitor it more carefully. Loans made in the first-quarter already account for 90 percent of the 2009 loans target. The bank can afford to have a loose monetary policy since inflation is low and likely to remain low in the near future. The PBC is unlikely to reduce the 1-year lending rate from the current level of 5.31 percent anytime soon because it has already managed to increase credit without cutting rates, and also because the inter-bank rate is well below 1 percent. The yuan rose by a paltry 0.16 percent in April but is at a 7-month high. Three-month forwards indicate a very slight appreciation from current levels, only natural given the high level of spending in the economy and the general weakness of the U.S. dollar.



Tokyo International
Forum Building

RBI could ideally cut the Statutory Liquidity Ratio (SLR), which is currently at 24 percent and used to finance government debt — a huge opportunity cost for financial institutions. However, that may not come to pass given the record government deficit. Because of the general weakness in the economy, the rupee will likely remain at current levels, something that the three-month forwards also indicate.

Japan

In a bid to avoid what is euphemistically referred to as the 'lost decade' (the 1990s), the Japanese government is doing

is below 6 percent. There is good reason to believe the low number. An industry group expects exports to remain flat in FY10. This will hurt industrial growth and is already showing in the credit ratings of companies, which have fallen to levels not seen in a decade. What could also potentially hurt Indian companies is that they have \$1.4 billion in foreign convertible bonds maturing this year and \$2.7 billion in the next. Given the fall of the stock market from its height, it's likely that lenders will want these companies to pay up and convert the loan into equity. Indian companies are also being hurt by their inability to get loans, both domestic and foreign.

everything it can possibly do. After the economy shrank 12.1 percent on an annualized basis in the third-quarter of FY09 (Oct – Dec '08), the government launched its fourth stimulus plan in less than 8 months. This plan calls for 15.4 trillion yen (\$153 billion) in tax cuts and spending measures, bringing the total stimulus spending to 27 trillion yen. Apart from the 27 trillion yen, the government's plans also include a 75 trillion yen package in the form of financial guarantees, etc. There is good reason for the government to be worried.

Given the fact that the government (this one and the next one) has significantly depleted its cash reserves, the RBI will have to do the heavy lifting. The RBI has been cutting its benchmark rate, the repo rate, quite aggressively but banks, especially the private ones, haven't been as aggressive when cutting their lending rates, causing the RBI much heartburn. The private banks have their own set of considerations, with the largest private bank saying that they would need to raise \$1 billion in fresh capital. The other problem that the RBI faces is that banks have been lending well below the RBI's target. Given the reduced forecast for FY10, the RBI will likely cut rates by approximately 50 basis points in the near to medium-term. The RBI has leeway to cut rates because the inflation rate will likely remain low, though they need to pay heed to the fact that food prices are rising. If the economy doesn't improve as expected, the

Auto Production (Percent YoY)



Source: Bloomberg

In a note explaining the 15.4 trillion stimulus plan, the Cabinet Office said: "Amid the deepening global financial crisis and the synchronized global recession, the Japanese economy is facing a rapid contraction of exports and a severe financial environment. Under these circumstances, the risk of a negative spiral, including the case that the deterioration of the real economy destabilizes the financial system further, which in turn will aggravate the economic condition, is growing." The Bank of Japan (BOJ) has forecast that the economy will contract by 3.1 percent in FY10 and recover in the next.

Exports contracted by a massive 45.3 percent in March compared to 49.4 percent in February. Some commentators suggest that this is a positive development — it definitely is — but there is no trend to suggest that there is an actual improvement. Predictably, industrial production also contracted; it fell 34.2 percent in March though there was a 1.6 percent gain in MoM terms. One of the main reasons for the fall in the industrial sector was the auto sector, which contracted 50 percent in March (auto exports fell 64.3 percent in March). The slowdown has caused corporate bankruptcies to rise to a six-year high. Unemployment is at a four-year high, leading to reduced spending in the retail sector. Companies are reducing wages to prevent job cuts, but that may not really solve anything. These measures will not protect the temporary workers who make up one-third of the workforce.

The BOJ's prediction is dependent on the stimulus money being spent productively. Elections to the Diet are scheduled for September and there are genuine fears that the government may indulge in 'pork-barrel' spending, which are not likely to revive the economy. This is necessary given the fairly pessimistic business conditions forecast seen in the Tankan survey. This is further reinforced by the machinery order numbers which have seen big falls. However, the Economy Watchers survey, which polls merchants that deal with consumers directly, was at an eight-month high in March. Interest rates, currently at 0.10 percent, are likely to remain unchanged. The yen is back at about the 100 level after gaining 10 percent, giving some breathing space to exporters. There could be appreciation of the yen if the government goes

ahead with the massive bond issue (\$109 billion) to pay for the stimulus package, and pushes up yields.

South Korea

The South Korean economy may be on the cusp of an economic recovery though it may not seem evident at first glance. The economy beat market expectations and unexpectedly grew by 0.1 percent QoQ in 1Q09, compared to a contraction of 5.1 percent in the previous quarter, thus narrowly avoiding a technical recession. In YoY terms, however, the economy contracted 4.3 percent. The market was expecting a contraction of 0.2 percent QoQ, but the 50 trillion won (\$37 billion) allocated for stimulus spending, sharp interest rate cuts, and the depreciating won helped counter the slowdown. Encouraging news was that private consumption saw a positive uptick in growth.

As mentioned, the economic recovery is certainly not immediately evident when one looks at the macro numbers. Exports fell by 19 percent in April, slight better than the 22 percent contraction in March. As with any economy that is export dependent, a fall in exports typically hits the industrial sector; it contracted by 10.5 percent in March but that is much better than the 25.4 percent contraction in January. Retail sales contracted by 2.5 percent in March compared to 3.9 percent in February. Retail sales and overall goods consumption remain weak because of falling household income and a rise in precautionary saving. It hasn't helped that the unemployment rate is at its highest level since 2005 and that partially explains the rise in precautionary saving.

GDP Growth (Percent YoY)



Source: Bloomberg

Going forward, there is reason to believe that the economy may have likely bottomed out in the first quarter. When keeping the benchmark rate constant at a monetary policy meeting on April 9, the Bank of Korea (BOK) said: "Domestic economic activity has kept on declining due to the continued decrease in both domestic demand and exports, but the pace of the slowdown has moderated somewhat." That is however unlikely to prevent a YoY contraction in 2009. The BOK has forecast that the economy will contract 2.4 percent in 2009, but the contractions will become smaller on a quarterly basis.

President Lee Myung Bak has warned against over-optimism but there are 'glimmers of hope'. One glimmer of hope in Korea is manufacturers' confidence index which rose by 11 to 71 for May from 60 in April. Another glimmer is consumer sentiment, which climbed to a nine-month high in April. Newspaper reports suggest that, at the government's urging, companies are hiring new workers by having existing workers take pay-cuts to accommodate the new hires. The government is planning to spend \$3.5 billion to create approximately half-a-million jobs. This share-the-pain strategy is not without its risks, especially if the slowdown lasts longer than anticipated, particularly since most of the jobs that the government plans to create are temporary.

The BOK is unlikely to cut interest rates anytime in the near future because they believe that the economy is already on the mend. The won, which lost a significant amount of value in 2008, is unlikely to lose much from this point on. The central bank has already achieved its objective of increasing exports and the government is planning to sell \$3 billion in bonds to bolster the defense of the won.

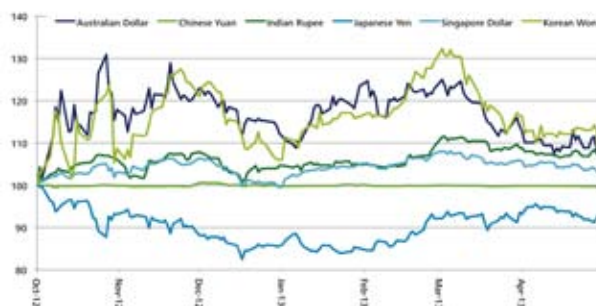
“Domestic economic activity has kept on declining due to the continued decrease in both domestic demand and exports, but the pace of the slowdown has moderated somewhat.”



Recent graduates from Korea University remain hopeful for job prospects in an economic upturn

Select economic indicators

Indexed Daily Movement of Major Currencies
 (Oct 1, 2008 to Apr 30, 2009)



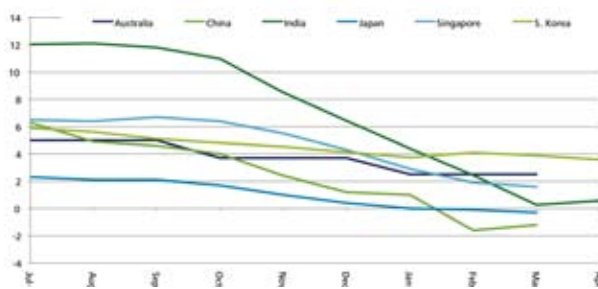
Source: Bloomberg
 Note: Above 100 means depreciation and below 100 means appreciation.
 All exchange rates are against the U.S. dollar.

Indexed Daily Movement of Major Stock Exchanges
 (Oct 1, 2008 to Apr 30, 2009)



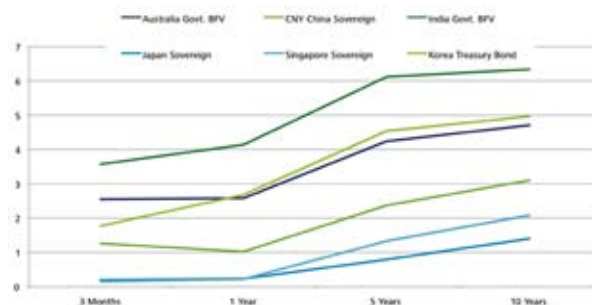
Source: Bloomberg

Inflation Rates



Source: Bloomberg
 Note: Australia's inflation rate is a quarterly rate. India's is a weekly rate that is averaged.

Yield Curves*



Source: Bloomberg
 * As on May 04, 2009

About the economist



Sunil Rongala
 Deloitte Research
 Deloitte Support Services India
 Private Limited
 Tel (U.S.): +1 615 718 2430
 Tel (India): +91 40 6670 2430
 Email: srongala@deloitte.com

Sunil Rongala is a Manager with Deloitte Research, Deloitte Support Services India Private Limited. He holds a Ph.D. in International Economics from Claremont Graduate University, California and a Post-Graduate Diploma in Economics from the London School of Economics. Prior to joining Deloitte, Sunil was the economist for a large manufacturing conglomerate in India. He has co-authored a book on Asian macroeconomic issues titled *Asia in the Global Economy: Finance, Trade and Investment*.

About Deloitte Research

Deloitte Research, a part of Deloitte Services LP, identifies, analyzes, and explains the major issues driving today's business dynamics and shaping tomorrow's global marketplace. From provocative points of view about strategy and organizational change to straight talk about economics, regulation and technology, Deloitte Research delivers innovative, practical insights companies can use to improve their bottom-line performance. Operating through a network of dedicated research professionals, senior consulting practitioners of the various member firms of Deloitte Touche Tohmatsu, academics and technology specialists, Deloitte Research exhibits deep industry knowledge, functional understanding, and commitment to thought leadership. In boardrooms and business journals, Deloitte Research is known for bringing new perspective to real-world concerns.

Please visit www.deloitte.com/research for our latest thought leadership or contact us at: delresearch@deloitte.com. For more information about Deloitte Research, please contact the Director of Operations, Vikram Mahidhar, Deloitte Services LP, at +1 617 437 2928 or via Email: vmahidhar@deloitte.com or the Global Director, Mark Klein, Deloitte LLP, at +1 212-492-3821 or via Email: markklein@deloitte.com.

Contacts

For more information, please contact:

Chinese Services Group Leaders

Global

Lawrence Chia

Deloitte Touche Tohmatsu CPA Ltd
China
Tel: +86.10.8512.5615
Email: lawchia@deloitte.com.hk

U.S.

Clarence Kwan

Deloitte LLP
USA
Tel: +1.212.436.5470
Email: clkwan@deloitte.com

Japanese Services Group Leaders

Global

Yoichiro Ogawa

Deloitte Touche Tohmatsu
Japan
Tel: +81.3.6213.1009
Email: yogawa@deloitte.com

U.S.

John Jeffrey

Deloitte LLP
USA
Tel: +1.212.436.3061
Email: jjeffrey@deloitte.com

Global Industry Leaders

Consumer Business

Lawrence Hutter

Deloitte MCS LLP
UK
Tel: +44.20.7303.8648
Email: lhutter@deloitte.co.uk

Energy & Resources

Peter Bommel

Deloitte Netherlands
Netherlands
Tel: +31.6.2127.2138
Email: pbommel@deloitte.com

Financial Services

Jack Ribeiro

Deloitte LLP
USA
Tel: +1.212.436.2573
Email: jribeiro@deloitte.com

Life Sciences & Health Care

Robert Go

Deloitte Consulting LLP
USA
Tel: +1.313.324.1191
Email: rgo@deloitte.com

Manufacturing

Hans Röhm

Deloitte & Touche GmbH
Germany
Tel: +49.711.16554.7130
Email: hroehm@deloitte.de

Public Sector

Greg Pellegrino

Deloitte Consulting LLP
USA
Tel: +1.617.850.2770
Email: gpellegrino@dc.com

Prof. Dr J. (Hans) Bossert

Deloitte Netherlands
Netherlands
Tel: +31.0.70.3372413
Email: jbossert@deloitte.com

Telecommunications, Media & Technology

Igal Brightman

Deloitte Brightman Almagor
Israel
Tel: +972.3.608.55.00
Email: ibrightman@deloitte.co.il

U.S. Industry Leaders

Banking & Securities and Financial Services

Jim Reichbach

Deloitte LLP
Tel: +1.212.436.5730
Email: jreichbach@deloitte.com

Consumer & Industrial Products

Craig Giffi

Deloitte LLP
Tel: +1.216.830.6604
Email: cgiffi@deloitte.com

Health Plans and Health Sciences & Government

John Bigalke

Deloitte LLP
Tel: +1.407.246.8235
Email: jbigalke@deloitte.com

Power & Utilities and Energy & Resources

Greg Aliff

Deloitte LLP
Tel: +1.703.251.4380
Email: galiff@deloitte.com

Telecommunications, Media & Technology

Phil Asmundson

Deloitte LLP
Tel: +1.203.708.4860
Email: pasmundson@deloitte.com

Asia Pacific Industry Leaders

Consumer Business

Yoshio Matsushita

Deloitte Touche Tohmatsu
Japan
Tel: +81.3.4218.7502
Email: yomatsushita@deloitte.com

Energy & Resources

Kappei Isomata

Deloitte Touche Tohmatsu
Japan
Tel: +81.9.2751.0931
Email: kappei.isomata@tohmatsu.co.jp

GFSI

Dr. Philip Goeth (Leader)

Deloitte Touche Tohmatsu CPA Ltd.
China
Tel: +86.10.8520.7116
Email: phgoeth@deloitte.com.cn

David Pulido (Deputy Leader)

Deloitte Touche Tohmatsu
Japan
Tel: +81.3.6213.1818
Email: dpulido@deloitte.com

Life Sciences & Health Care

Keiji Watanabe

Deloitte Touche Tohmatsu
Japan
Tel: +81.3.6213.3493
Email: keiji.watanabe@tohmatsu.co.jp

Manufacturing

Kevin Gromley

Deloitte China
Email: kegromley@deloitte.com.cn
Tel: +86.21.6141.2228

Telecommunications, Media & Technology

Ian Thatcher

Deloitte Touche Tohmatsu
Australia
Tel: +61.2.9322.7640
Email: ithatcher@deloitte.com.au

Deloitte.

Disclaimer

This publication contains general information only and Deloitte Services LP is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. Deloitte Services LP its affiliates and related entities shall not be responsible for any loss sustained by any person who relies on this publication.

About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu, a Swiss Verein, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.com/about for a detailed description of the legal structure of Deloitte Touche Tohmatsu and its member firms. Please see www.deloitte.com/us/about for a detailed description of the legal structure of Deloitte LLP and its subsidiaries.

Copyright © 2009 Deloitte Development LLC. All rights reserved.

Member of
Deloitte Touche Tohmatsu