Asian markets plummet amid fears of global recession

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Markets throughout Asia plunged yesterday following large losses on Wall Street on Wednesday and growing fears about the impact of a protracted global recession on the region's economies. The falls abruptly ended the market euphoria earlier in the week, after the announcement of huge bank bailouts in the US and Europe, and sent share values plummetting toward the record lows reached last week.

Japan's Nikkei 225 led the way with a decline of 11.4 percent—its worst one-day fall since the October 1987 share market crisis. Underscoring its volatility, the Tokyo stock market had rocketted up by a record 14 percent just two days earlier. Last week, share values plunged by 24 percent in five days—the worst weekly performance in the Nikkei's 50-year history.

Share markets throughout the region followed suit. South Korea's Kospi lost 9.4 percent and the Australian S&P/ASX index was down 6.7 percent. Hong Kong's Hang Seng fell by 4.8 percent, but the sub-index covering mainland Chinese companies fell even further. The Shanghai Composite Index dropped by 4.3 percent and the Shenzhen Composite Index by 4.7 percent. The MSCI Asia Pacific Index of share prices across the region fell by 8.5 percent, its biggest drop on record.

Throughout the region, there are deep concerns that export markets in the US and Europe will rapidly shrink as the world economy slows down. The debate is no longer about whether there will be a global recession but rather how long and how deep it will be. Figures released on Wednesday showing a marked monthly decline in consumer spending in the United States—the third in a row—translated into sharply falling shares for Asian exporters.

Takashi Ushio, investment strategy head at Marusan Securities, told Reuters: "There's a certain degree of panic selling in Tokyo but the sentiment's different from last week. Last week people were panicking over the financial system, nobody really knew what would happen. But now it's the real economy." Yoshinori Nagano, a strategist at Daiwa Asset Management, told *Bloomberg.com*: "The American spending spree in the past few years has totally evaporated. The earnings outlook for auto manufacturers and electronic makers is particularly harsh."

Toyota, Japan's biggest automaker, slumped 9.3 percent and Honda, which makes half its profit in North America, lost 7.9 percent. Mazda fell 4.2 percent, on top of a decline of 9.2 percent on Wednesday. Sony, Japan's second largest manufacturer of consumer electronics, dived 13 percent. Sharp fell by 11 percent. Nintendo, which generates 90 percent of its revenue from exports, plunged by 10 percent. Steelmakers, shipping companies and corporations trading in commodities were all hard hit. Mitsubishi Corp, which derives half of its profit from commodities, fell by 15 percent, while Mitsui Co plunged by 17 percent.

Japan has already recorded a 3 percent contraction in GDP for the second quarter on an annualised basis with predictions the economy is heading deeper into recession. Taro Saito, a senior economist with NLI Research Institute, told Agence France Presse that Japan's economy could shrink throughout 2008 as a whole. "That was unthinkable a while ago," he said.

The relative stability of the Japanese financial system has contributed to a rising yen as investors have sought safe havens. The so-called carry trade—borrowing in Japan where the benchmark interest rate is just 0.5 percent to invest in countries with higher rates—has slumped. But the rise of the yen by 22 percent against the US dollar since late June is hitting exporters hard. Analysts have calculated that Toyota, for instance, loses 35 billion yen ($350 million) for every one yen fall of the US dollar.

Having virtually no room to cut interest rates, the Japanese government has drawn up an $18 billion emergency stimulus package in a bid to halt the slide into recession. In a measure of the fear gripping ruling circles, the opposition dropped its plans to block the measure, which passed yesterday in the upper house as share values plunged. Newly installed Prime Minister Taro Aso expressed the hope that the package would be "effective to a certain degree" but warned that "further steps may be needed".

China's slowdown

China is often viewed as the growth engine that will pull the world economy out of recession. But its rapid growth rates are heavily dependent on export markets in the US, Europe and Japan as well as continuing huge inflows of foreign investment. The *Wall Street Journal* concluded from statistics published by China's central bank on Tuesday that capital flows into China had "slowed sharply and even reversed in recent months… analysts estimate that anywhere from $10 billion to $25 billion left the country in September, just as the financial crisis intensified."

China's growth rates are still predicted to remain at around 8 to 9 percent, down from 10 percent in the second quarter of this year and 12.6 percent a year earlier. However, there are already signs that this slowdown is having a dramatic impact on Chinese manufacturing. China's customs agency announced on Monday that 52.7 percent of the country's toy exporting companies—3,631 in all—had ceased operations in the first seven months of the year. Most were small, but this week a major manufacturer, Smart Union, shut its doors, throwing more than 6,000 employees out of work.

The mood was bleak at the Canton Fair, the world's largest export exposition, which opened on Wednesday. Kevin Cao, export manager for HuangYang Bronze Company, bluntly told the *New York Times*: "It's a disaster." The company has seen its exports of aluminium wire cut by 50 percent and has cut its workforce by a quarter. Other manufacturers reported sharp declines.

While China is still reporting rising exports and large trade surpluses, the *New York Times* pointed out that when adjusted for inflation and the rising yuan, exports actually shrank by 0.5 percent in August. While inflation figures for September are not yet available, the article predicted that the 21.5 percent rise in exports for September, announced on Monday, was likely to vanish as well.

Any decline in the Chinese growth rate will hit countries throughout the region that rely on exports of commodities and components to China. On the Australian share market, the major mining companies were particularly hard hit—BHP Billiton was down by 13 percent and Rio Tinto by 16 percent—amid fears of falling demand and commodity prices. A slowdown in China will also reverberate in Japan and South Korea, which have profitted through the export of capital goods. China is now the largest export market for both countries.

South Korea has also been badly affected by the global financial crisis. Yesterday, the won plunged by 9.7 percent against the US dollar—its worst one-day fall in a decade—as fears grew over the country's banking system. South Korean banks have a high ratio of loans to deposits and have been heavily reliant on international borrowing, which has dried up. The international credit rating agency Standard & Poor's warned this week that it may downgrade seven South Korean banks.

Economic commentators are warning that Asia is by no means safe from the global economic crisis. Recalling the 1997-98 Asian financial crisis, the *Economist* magazine noted this week: "In many ways the region is far better placed to withstand the present shock. Its banks are stronger, its currency regimes less rigid, its foreign-exchange reserves bigger. On the other hand, a decade of accelerated globalisation has seen every country integrated even more closely into the world economy. None can hope to be immune from a global economic slowdown.

"The region may not face the sort of meltdown experienced at the end of the 1990s. But prospects for growth look much bleaker than they did even a fortnight ago. Exports to rich countries still matter, albeit less than they did. And so does trade finance, which lubricates Asia's trading machinery. Ships are sitting empty in big Asian ports, their cargoes piled up on the dockside because no bank will guarantee them. Despite strong balance sheets, Asian banks may need more capital if they are to make up a shortage of Western trade credit."

An editorial in the *Financial Times* on Wednesday entitled "Stimulating Asia: Those who live by export-led growth can also die by it," concluded that Asian economies had to make a major readjustment. "Export-led growth has served Asia well and can continue to do so. Export-led growth that relied on the US to run a vast trade deficit was always unsustainable, however, and vulnerable to precisely this kind of reversal." Like a number of other commentators, the editorial called for measures to encourage greater domestic consumption in Asia as a means of boosting regional and international economic growth.

However, as Ifzal Ali, chief economist of the Asian Development Bank, told the *New York Times*: "Consumer behaviour cannot be changed by the wave of a wand. Domestic demand-led growth is easier said than done." Stephen Roach, chairman of Morgan Stanley Asia, has calculated that total personal consumption in China and in India, each with a population of more than a billion, is still behind that of Germany with a population of just 82 million. Moreover, any attempt by the major Asian economies to spend on stimulating domestic consumption may well rebound on the United States, which has relied on the investment of the trade surpluses from Asia to prop up its huge deficits.

Those looking for a ray of economic hope in Asia will be disappointed. It is particularly noteworthy that despite the gathering storm clouds, there have been no displays of regional cooperation. No one has even suggested emergency meetings of the various regional forums—from the Asia Pacific Economic Cooperation (APEC) to the much-vaunted East Asian Summit. South Korea's appeals to Japan and China for stronger measures to defend Asian currencies have fallen on deaf ears. On Wednesday, Philippine President Gloria Macapagal Arroyo grandly announced that a $10 billion standby fund would be established to assist countries in the region with liquidity problems, only to be undercut by World Bank officials who declared that the plan was not final.

Far from producing greater cooperation, the economic crisis will only sharpen existing tensions in the region and internationally as each government scrambles to defend its own economic interests at the expense of others.

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