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The possible adverse effects of currency instability on SMEs should not be underestimated

At present, many economies are facing significant appreciation of currency as well as inflow of hot money. Domestic property prices and the prices of raw materials both are continuing to rise. The currency appreciation and the uncertainty about the future have already inserted serious impact on the operation of SMEs (small and medium enterprises) in the APEC member economies. Since SMEs hardly have the ability to avert currency risks, their export margins will narrow under currency appreciation, and export competitiveness will also be weakened. The increasing price of raw materials will also lead to a higher production cost of SMEs.

Competitive devaluation, now triumphant on the stage of the global economy, occurs because every economy intends to keep its price competitive. This competition is a behavior of “beggar thy neighbor” that results in more uncertainty of currency value as well as conflicts in trade. It is obviously not a solution beneficial for SMEs. The currency mess can be cleaned up only by international cooperation and the enhancement of crisis management capabilities.

Hence, we appeal to each leader of the major economies that the risk position of SMEs should be taken into consideration in the G20 meeting next month, November 2010, and an agreed solution that stabilizes the exchange rates should be found. Each participating economy must not think of merely its self-interest, for this will enmesh the global economy in currency conflict, and no economy will be benefited from it indeed.

This current issue will focus on apparent currency instability. This issue will feature our premier issuance of a crisis warning since our inaugural publication, indicating that present currency instability has already resulted in an incipient snowballing effect accumulating a number of diverse inherent risks. In regional report, this issue has focused on any changes in exchange rates, asset pricing, and consumer goods prices as efficient monitoring targets, to help steer our attention to the seriousness and potential eruptive crisis effects of this wave of currency instability around the globe.

At the same time, in this issue, we have specially invited two experts to discuss the effect of the Japanese exchangerate interventions on global economic recovery and how small and medium-sized enterprises can interpret macro economic indicators to reduce their operational risk exposure. With respect to the Japanese government currency intervention, our expert believes, the prevalent wide disparity in exchange rate regimes around the globe serves to impede any appreciable rapid improvements, and thus it is imperative to assiduously deploy coordinative mechanisms for concerted joint action on exchange rates.

In this issue, we have also extended a special invitation to Ms. Myrna Yao, President, Filipino Chinese Federation of Business & Professional Women of the Philippines, to share with readers about the Philippines experience among female micro-enterprises and small and medium enterprises dealing with crises in the Pangasinan region. Additionally, we have also selected the most pertinent news of interest to share insights with our readers about: increasing pressures for currency appreciation among emerging market economies, conflict among international institutions regarding currency matters, and continuing upward price trends for basic commodities and agricultural goods. In this issue we also introduce Dr. Doom, Nouriel Roubini, co-authoring in 2010 with Stephen Mihm of the work, Crisis Economics—A Crash Course in the Future of Finance.

The current threats could result in outbreak of a crisis, and we are pledged to continue our constant global crisis monitoring for any adverse developments and provision of appropriate response strategies, to help ensure that APEC SMEs can safely engage and overcome any crisis.

Robert Sun-Quae Lai, Ph.D.
Executive Director
APEC SME Crisis Management Center
In response to the economic downturn caused by the global financial crisis, many economies have adopted quantitative easing policies and maintain a low interest rate. As a result, the global economy as a whole has been flooded with “hot money.” The inflows of hot money have driven the value of currencies and price of asset upward in many APEC economies. The flood of hot money has also led to significant increases in global raw materials prices. With the economic outlook for the developed economies still looking bleak, some major economies have already decided to embark on a further round of quantitative easing. Therefore, the amount of hot money sloshing around the world can be expected to increase still further.

This increase in the volume of hot money has the potential to spark off a number of different crises. Both the Asian Financial Crisis of 1997 and the Global Financial Crisis of 2008 were caused by hot money. The flow of hot money from place to place stimulates the formation of a variety of bubbles; even slight errors in government responding policy can then bring about a disastrous outcome. So far, hot money has already caused dramatic fluctuations in currency valuations, the formation of asset bubbles, and skyrocketing raw materials prices. Any one of these could trigger a crisis, and in the worst-case scenario, multiple crises could develop simultaneously.

The risk of a currency crisis lies mainly in East Asia and a number of Latin American economies. They have seen a dramatic rise in the value of the currencies due to the inflow of hot money. Of course, many currency crises were triggered by a sudden depreciation of a currency that has appreciated in value dramatically. At present, the currencies are still rising in value, with governments doing their best to curb the increase. Therefore, the danger of a sudden devaluation is still some way off. What gives cause for concern is the possibility that, by making too aggressive an effort to stop the appreciation of their currencies, governments may trigger a large-scale outflow of the hot money that has been flooding in, thereby causing a currency slump.

A currency crisis is often accompanied by the bursting of asset bubbles and by banking crisis. Here again, the risk is most serious in East Asia and in some Latin American economies. The most likely scenario is that an inflow of hot money gives rise to asset speculation, and then the asset bubble bursts and asset values fall. This could cause the banking system to collapse and lead to an exodus of foreign capital. Subsequently, the currency value drops, making it difficult for both banks and businesses to meet repayment obligations on overseas debt.

The impact of rising raw materials prices is more widespread. The whole world is feeling...
its effects, and there is a danger of worldwide inflation, of the kind that had developed in the first half of 2008. If economies take joint action to block the inflow of hot money, then these funds may flood into raw materials markets instead, leading to even faster rises in the price of raw materials.

Besides the possible crises outlined above, the protectionism sparked by currency devaluation also poses a significant threat to the operations of small and medium enterprises (SMEs). A race to the bottom in terms of currency devaluation constitutes “beggar-thy-neighbor” behavior that can exacerbate monetary instability and trade friction, and may also encourage protectionism.

With the exception of inflation caused by rising raw materials prices, which could occur in the near future, the other crises outlined above would all take some time to develop. There might be just one crisis, several crises occurring simultaneously, or even several crises merging into one mega-crisis. In any event, SMEs need to be prepared.

Of the types of crisis referred to above, a currency crisis or the bursting of an asset bubble would have been preceded by a period of sustained price increase. The crucial point would be when prices stopped rising and the bubbles burst. SMEs would find it very difficult to forecast when this would happen. The best they can do is to begin exercising caution when prices start to skyrocket upwards, and to undertake hedging and risk aversion activities. As regards the commodity markets, the rising price of raw materials has already had an impact on SMEs, so SMEs should immediately start to hedge against further increases in raw materials prices.

Besides making use of the forecasts produced by the APEC SME Crisis Management Center, SMEs should also try to monitor the following five key indicators: exchange rates, real estate prices, the consumer price index, international raw materials prices, and the state of banks’ balance sheets.

At the same time, we appeal to SMEs in APEC member economies to activate their crisis prevention/management mechanisms as soon as possible. Those SMEs that have yet to formulate a crisis management plan should immediately set to work on drawing up such a plan, and on the creation of a crisis response team. The APEC SME Crisis Management Center has compiled the “Principles and Checklist of Financial Crisis Management for APEC SMEs” for the reference of SMEs; this document can be downloaded from the Center’s website: http://www.apecscmc.org.
The United States

In September, the unemployment rate was unchanged at 9.6%. A broader measure of the unemployment rate, which includes people who stopped looking for work and those settling for part time jobs, increased to 17.1%, from 16.7%. While the private sector added 64,000 workers, the Federal government shed 159,000 workers, half of them temporary workers for the 2010 Census. Tight government budgets forced State and Local governments to shed another 83,000 workers. Still the increase in private sector employment suggested the economy was unlikely to slip back into a double-dip recession.

Since late August, the mood in the U.S. has improved considerably, and the stock market has risen over 10%. Why has the stock market risen when the real economy still appears so weak? Some analysts believe that the rising stock market is a consequence of expected Federal Reserve Board monetary policy. These analysts believe that in early November, the Fed will embark on another purchase spree of longer-term U.S. Treasury securities (so-called “Quantitative Easing”) in an attempt to further lower bond yields, currently 2.4% (on a 10-year Treasury bonds). By lowering yields and thereby bank lending rates, the Fed is hoping that there will be more borrowing, which would help the U.S. economy recover. As bond yields decline, naturally stock prices will tend to increase.

This aggressive monetary stance will likely have the following consequences. First, to lower the already low 10-year bond rates by another 50 basis points would require Fed purchases of government bonds of about 1.5 to 2 trillion dollars—which is quite a large injection of money. This increase in money supply is likely to raise inflationary expectations, actual inflation rates, and depreciate the dollar further.

Higher inflation and a weaker dollar, however, are actually consistent with current U.S. economic policy. U.S. asset prices such as housing prices are severely depressed, and inflation will be helpful in restoring housing prices. The U.S. is also heavily indebted internationally, and it is in U.S.’s interest to lower the burden of financing this debt by depreciating the dollar. A depreciated dollar will also help expand U.S. exports, aggregate demand, and employment.

Some analysts question whether a further decline bond yields and in bank lending rates are even the right ingredients to spur business activity. Many small and medium-sized enterprises (SMEs) are in retail and wholesale and are close to their customers, but many of them are holding back on hiring as these businesses are pessimistic about the future. However, at the same time customers are not buying since their income is not back yet, many of them are delinquent payers, and small businesses cannot hire unless consumer demand improves. A
recent survey shows that only 8% of SMEs intend to hire, while 31% of large firms intend to hire.

Rather than looser monetary policy, these analysts argue for more direct policies to expand hiring, by providing worker-retraining programs, and tax cuts for businesses that hire more workers.

**Canada**

The Canadian economy is cooling, as growth in its largest trading partner, the U.S. is still muted. Although the unemployment rate held steady at 8% in September, employment fell by 6,600 jobs and housing starts slowed. Many Canadian workers left the labor force, discouraged by the lack of jobs. The Bank of Canada has raised policy interest rates three times already this year, to 1.0%. Given the weakening economy, it is unlikely that the Bank of Canada will raise interest rates again this year. (The author is Professor at University of Southern California.)

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**The U.S.**

In recent months, the US dollar has depreciated rapidly against some key currencies such as the Japanese yen. Idiosyncratic reasons, however, such as the status of the yen as a “safe-haven” often influence bilateral exchange rates. To get a broader view of the recent movements in the US dollar, we should examine trade-weighted exchange rates. A well-known trade-weighted exchange rate index is calculated by the Federal Reserve Board of Governors, and weighs U.S.’s bilateral exchange rate with a particular economy, by U.S.’s total trade (sum of exports and imports) with that economy. Twenty-six of the largest trading partners of the U.S. are included in this index.

According to this index, from June 2008 to March 2009, the US dollar appreciated by about 20%. However, since March 2009 to October 2010, the dollar depreciated by about 13%. The earlier appreciation occurred because in the depth of the global economic crisis, investors viewed U.S. assets as safer than non-U.S. assets, although ironically, the global economic crisis actually started in the U.S..

As the deep uncertainty from the global crisis was lifted, investors shifted their attention to the record low U.S. interest rates, and the loose liquidity policies of the Federal Reserve. In 2008 and early 2009, the Federal Reserve purchased over $1.6 trillion of U.S. government bonds and other assets, greatly expanding the assets of the U.S. banking system. These monetary factors depreciated the US dollar relative to the currencies of the other economies, as these economies had tighter liquidity than the U.S..

It appears likely that during November, the Federal Reserve will embark on another large purchase of U.S. government bonds, perhaps in the order of between $500 billion to over $1 trillion dollars. The expectation of such a large liquidity injection is driving the current instability and weakness in the dollar.

**Canada**

After initially depreciating against the US dollar, the Canadian dollar started to appreciate against the US dollar in the summer of 2009, and has appreciated by 25% since that time.

The Bank of Canada also publishes a trade-weighted exchange rate of the Canadian dollar, weighted by Canada’s total trade with Canada’s 6 largest trading partners. This index is dominated by movements in the US dollar since the U.S. accounts for about 75% of Canada’s total trade. Since the summer of 2009, this index has appreciated by 13%.

Excluding the US dollar, since the summer of 2009, the Canadian dollar has appreciated against all other trading partners by 3%. Thus, excluding its movements against the US dollar, the Canadian dollar has been quite stable against other economies. This probably reflects the fact that the Canadian economy is making a stronger recovery than the U.S. economy, and that its monetary policy is tighter. (The author is Professor at University of Southern California.)
China’s exchange rate policy has been the most controversial issue discussed at recent international forums and bilateral meetings involving China and advanced economies. The United States has been at the forefront of the growing criticism of China’s inflexible attitude toward the movement of the renminbi. The U.S. House of Representatives passed a bill on 29th September 2010 that would regard the maintenance of a substantially undervalued renminbi as an export subsidy and thus penalize Chinese exports. U.S. President Barack Obama pressured the Chinese Premier Wen Jinbao at a top-level meeting scheduled on 23rd September and expressed strong disappointment over the slow adjustment of the exchange rate against the US dollar since China’s introduction of a supposedly more flexible exchange rate regime on 21st June 2010; simultaneously, Canada supported the view of the U.S.

Moreover, European officials—the EU President Herman Van Rompuy, the ECB President Jean-Claude Trichet, the Chairman of the Eurozone Financial Ministers’ Group Jean-Claude Juncker, and the EU Monetary Affairs Commissioner Olli Rehn—jointly called for further revaluation of the renminbi in their meetings with Wen Jin-bao held on 6th October. The European concerns arise from the recent re-strengthening of the euro against the US dollar and thus the renminbi and are related to the potential damage to the sluggish European economic recovery. They are also concerned about the growing trade imbalance with China.

Given that since 2001 the euro has been a non-intervention currency, it appears that the foreign exchange interventions by China, Korea, Chinese Taipei and Japan, together with the Federal Reserve Board Chairman Ben Bernanke’s suggestion for further easing of monetary policy, have caused a disproportionate burden on the euro in the adjustment of global exchange rates. This has led to a deterioration of Europe’s price competitiveness against Asia and the United States.

In early October 2010, Dominique Strauss-Khan, the IMF Managing Director, warned against a potential competitive devaluation war that might occur if other economies attempted to increase their competitiveness; as a result, generate serious risks to the global economic recovery.

In response to growing criticism, the Chinese Premier has repeatedly rejected any proposal for a large-scale revaluation of the renminbi, on the ground that the greater volatility of the exchange rate would cause bankruptcies of Chinese firms on a massive scale, with resultant unemployment and mounting social unrest. While the Premier’s remarks are comprehensible, some argue that the high economic growth of 11% in the first half of 2010 and the disappearance of an output gap (a shortage of demand over supply) may make it harder for China to justify its continued reliance on exports as the economic growth engine.

Since early September, China accelerated the pace of renminbi’s appreciation. It may be a temporary action before the G20 Finance Ministers’ and Central Governors’ Meetings in October 21st—
23rd and G20 summit in November 11th—12th. Nonetheless, Timothy Geithner, the US Treasury Secretary, commended on the initiative in October 15th and made a statement that “China will be able to eliminate the undervaluation of the renminbi if the current pace is maintained.”

Such political tensions may encourage some advanced economies to increasingly seek recourse to trade protectionism and then generate even greater volatility in foreign exchange markets. If this should happen, negative factors will adversely affect the global economy and particularly hurt the most vulnerable SMEs engaged in foreign trading.

JAPAN

Since August 2010, Japan has been struggling with the issue of the yen’s appreciation. The government reacted by: (1) the introduction on 30th August 2010 by the Bank of Japan (BOJ) of a 6-month liquidity-providing operation totaling ¥10 trillion, (2) since 15th September 2010 an intervention of ¥2.1 trillion by the Government/BOJ in the foreign exchange market through the purchase of the US dollar in exchange for the yen, and (3) on 5th October 2010, the re-introduction by the BOJ of a virtually zero interest rate policy and the establishment of a ¥5 trillion Asset Purchase Program in which eligible assets included JGBs (Japanese Government Bonds), commercial paper, corporate bonds, Exchange-traded Funds (ETFs), and Japan Real Estate Investment Trusts (J-REITs). However, even with these efforts, the yen did not depreciate on a sustainable basis. The yen reached ¥80 against the US dollar in mid-October—the high level seen in the past 15 years.

Japan’s foreign exchange intervention, the first since March 2004, has complicated the debate surrounding China’s exchange rate policy. Some argue that such a move gave China and other Asian economies an excuse to stabilize their own currencies against the US dollar. Amid growing political pressures, the Finance Minister Yoshihiko Noda in October 16th criticized Korea for its active intervention in the foreign exchange market and said “Korea’s role as a hosting economy of G20 will be intensively questioned.” On the same day, the Prime Minister Naoto Kan stated “China and Korea should take a more responsible action under the same rule,” implicitly criticizing their exchange rate policies. A spokesperson of China’s Ministry of Commerce and the Bank of Korea Governor (the central bank) Choongsoo Kim immediately rejected these remarks.

Based on the prospect of a weakening global economy in the second half of 2010 and a persistence of a large output gap (equivalent to minus 4.5% of GDP) for Japan, on 8th October 2010 the Prime Minister Naoto Kan’s cabinet endorsed a ¥5.1 trillion ($62 billion) stimulus package to revitalize the economy by assisting local government and SMEs. According to the Cabinet Office, the new package was projected to increase GDP by 0.6% and generate 45,000–50,000 jobs. Given the huge government debt (over 220% of GDP projected in 2010), the new package will be financed without issuing new JGBs—mainly through the use of higher-than-expected tax revenue, reserves, and a carry-over from the previous year’s accounts. The government plans to submit the stimulus package to the current Diet as a part of the 2010 supplementary budget.

KOREA

After enjoying high profitability in the first half of 2010, major exporting firms in the electronic, steel, and petrochemical industries are expected to record a decline in the profits in the second-half. This reflects a decline in demand from major U.S. to European markets and a recent appreciation of the won. The prices of semiconductor products and LCD panels have begun to decline due to a growing excess of supply—a situation completely reversing that in the first half of 2010 when these prices rose because of increasing demand.

In particular, the appreciation of the won has adversely affected Korean exporting SMEs through an erosion of Korea’s price competitiveness. Some firms increasingly worry that their competitiveness will be deteriorated further by U.S. imposition of an anti-dumping duty against Korean-made stainless steel products and possible pressure by the international community on Korea’s exchange rate policy, as expressed by Japanese officials. (The author is Professor of Economics, Keio University.)
Booming Capital inflows and more intervention shake the stability

Honghui Cao

Indices of emerging economies in South East Asia like Indonesia, Thailand, Malaysia, the Philippines, etc. are above pre-crisis peaks for the sake of rushing capital inflows with the depreciation expectation of US dollar against the local currencies in Asia. Excessive appreciation would decrease the competitive advantages of those economies heavily relying on the export in this region. If Fed continues to adopt the quantitative ease monetary policy, further intervention in South East Asia region would be expected to prevent greater capital inflow and therefore would cause more uncertain impacts on the stability of macro-economy and financial markets.

Just in the wake of Japanese Yen (JPY) appreciation, Malaysian Ringgit against USD has been appreciated at 9.4% up to now this year. Thai Baht also has been ascending continuously and peaked at 29.87 on October 19th, with an increase by more than 7% appreciation this year. But the cabinet has just approved the new regulations to control the capital inflows and the rapid appreciation. Thailand would keep an eye on the ongoing appreciation and would be expected to take further actions.

Singapore central bank also prepares to intervene in the foreign exchange market once Singapore Dollar (SGD) reaches the historic peak again. Actually, since the policy to encourage the gradual currency appreciation has been adopted by the Singapore government to reduce the pressure of the inflation to date, SGD against USD has been appreciated almost 7%.

As discussed in the previous issues, the Philippines has been suffering from the rapid growing external debt. Now, it has been confronted with another pressure that the external debt has raised to US$ 57bn in June due to a revaluation of the currency. From late July Peso against USD continuously has been appreciated; at the same time in October it has reached the new peak since May 2008. The Yen-denominated external debt increasing at 28.8% is probably attributed to a large degree of the upward currency revaluation. JPY against USD has been appreciated at 10% by this year and has peaked during the past 15 years. However, the lack of deterioration in the external debt ratio suggests the nominal GDP can support financial obligations arising from the higher debt stock.

Compared with the 3.4% appreciation of Peso and 4.4% appreciation of Indonesia Rupiah in 2010, Viet Nam Dong has appreciated much more slightly with the frequent intervention of the central bank. But it is still close to the historic peak at 19450 last November before the first intervention. Its intervention in the foreign exchange market gets much stronger than the expectation this year. Dong has been depreciated twice with 10% each time, and it is expected to be depreciated further or the band would be expanded to fluctuate in the coming two years.

But it is not the only trouble for this economy. Viet Nam actually has been suffering from the inflation. The major cause is that the government has printed too much money almost every year, similar as a pump of underlying macro bubbles. Even by the standards of emerging market, Viet Nam runs extraordinary high trade and current account deficit. Official foreign exchange reserves have declined steadily to such low levels as a
share of imports. The currency has already been in a weak position during the past 3 years. If the authorities could not handle properly on such the situation of the credit growth, we would foresee the collapse of the banking system and the external crisis. Though the latest trade data shows that the credit growth is settling down somewhat, the information of the Viet Nam banking system has a really significant lag for the disclosure.

Another striking phenomenon is that

The high value of the currency provides a mixed blessing

Kenneth Waller

Different responses to the falling $US in Asia Pacific

The recent depreciation of the US dollar ($US) reflecting continuing concerns over the U.S. economy and strong expectations that the Federal Reserve will initiate quantitative monetary easing has led to a corresponding appreciation of other currencies, including those in the Asia Pacific region. The reaction by the economies of the Asia Pacific region to the falling $US has varied, and markedly so.

The Australian dollar ($A) has appreciated to its highest value against the $US since the $A was floated in 1983. The $A has been on an upward appreciation for some months, reflecting also buoyant commodity prices, a strengthening trade account and a firm interest rate structure relative to many other economies. The expectation is that the $A will be at parity with the $US within days, and may well start to move ahead of the $US over coming weeks and months. The high value of the currency provides a mixed blessing for the economy. The minerals resources industry would

appreciation of RMB against USD in the first half of this year is the slightest in East Asia, which leads to more serious conflicts between China and the U.S. and stimulates more global currencies depreciation competition. And therefore this would hurt the global economic recovery and shake the stability of the international economic and financial system. SMEs in this region would be confronted with very serious and uncertain challenges with the macroeconomic circumstances.

SA is measured according to the exchange rate at the end of the month besides October 2010 which uses an average. $NZ and Rs use a monthly average.
be particularly impacted if the $A continues its rise. Major Australian minerals exports are priced in $US and the falling $US could lead to falls in export revenues by this sector (in $A terms) impacting not just on the income of the sector but on tax revenues anticipated by the government through the new minerals resources rent tax. Whether or not there is any actual significant fall in income by the sector will be dependent on the market responses by China, India and Japan, major sources of Australian commodity exports. There is a strong consensus that the floating of the $A has been a major contributor to enhancing competitiveness and to a long period of strong growth; as a consequence of these benefits, there is no expectation that there will be any change in exchange rate policy.

The $NZ has appreciated to its highest level within 27 months reaching $US 76.40c, and the economy is moving into a positive phase after the global financial crisis. In these circumstances there is concern that the rise in the $NZ will blunt recovery, and there is an expectation that the currency will remain high over the next 12 to 18 months. Even so, it is judged that there will be no intervention by the Reserve Bank in the currency market.

India has responded to concerns arising from the appreciation of the rupee which has in part contributed to a rise in the current account deficit and external debt. The rupee recently climbed to a 25-month high of INR 44.16 to the $US, causing the Reserve Bank of India to intervene in the currency market. RBI Governor Subbarao confirmed at the recent IMF annual meeting that India would intervene to stabilize the rupee. This choice to intervene by a major developing economy adds to concerns that the world may be seeing the emergence of a period of destructive currency devaluation.

While currency concerns have dominated economic news in recent news, other important events have had an impact on the short-term outlook.

**Challenges to economic management in Australia**

The recent half-yearly review of the economy by the Reserve Bank of Australia points to a relatively strongly performing economy and one with a robust financial system. Unemployment in September remains at 5.1% and GDP growth for the year to June is 3.3%. Inflation for the quarter of September is 3.1%. While this is a positive assessment for the new Government, there is no room for complacency about the medium- to long-term challenges confronting the economy. These include the perceived need by the government to bring the current budget deficit into balance by 2013. However, the government faces a short-term problem in gaining political support for the introduction of minerals resources rent tax and which is required to be implemented in the near term if its debt reduction objective is to be achieved. A further and complex challenge is arriving at any politically acceptable decision to introduce a price on carbon. Given the uncertainties surrounding the mining resources rent tax, the government will almost certainly be faced with the need to make further sizeable cuts to its expenditure plans over the next two years or so if it is to achieve budget balance.

At this stage these political challenges do not seem to dampen business and consumer confidence. The latest NAB Business survey points to stabilization of business confidence in September, consolidating around +10 points.

**Positive economic gains in India, and financial system reforms**

In its latest World Economic Outlook, the IMF views India’s economic direction as positive. Inflation has eased to 8.51% in August from 9.78% in July; however, the wholesale price index remained unchanged at 140.3 in August. The HSBC manufacturing purchasing managers’ index (PMI) showed some slowing in the manufacturing sector in September, but nonetheless the sector maintains a strong rate of expansion. In the SME sector, companies involved in computer services, real estate and trade activities are embracing the limited liability partnership structure due to its greater functional flexibility and lower operational costs. The India-Japan trade pact has been finalized. Despite generally positive news, industrial production dropped to 5.6% growth in August from 15.2% in July, due to lower demand for capital goods and consumer nondurables. The
service sector, according to HSBC’s services PMI showed the rate of expansion slowing for the third consecutive month to 55.6. FDI flows have fallen by nearly 25% in the period from January to July in part due to unfavourable criticisms of India’s hosting of the Commonwealth Games. Despite those criticisms, India retains the second place in the world as a top-priority investment destination.

The government is creating a register of business to monitor commercial activity more accurately. In order to help the disadvantaged, a new pension scheme in the unorganized sector is being established to assist those without access to the existing social security net. The government is to set up a Financial Stability and Development Council (FSDC) to undertake macro prudential supervision of the economy. In addition, a committee of experts from outside the government is to be established to advise on modernising the financial system. There is opposition by state governments to the introduction of goods and services tax. There are also strong concerns about differing policy aims between the Ministry of Finance and the RBI. The former is committed to a strong growth policy while the RBI seeks to contain inflationary pressures.

New Zealand back on track

After a period of uncertain economic activity indicators show the economy moving in a positive direction. Inflation grew by 1.1% last quarter and by 1.5% over the last 12 months. This has been attributed to a pre-emptive rise in prices in response to a rise in the GST being introduced this month. According to BusinessNZ, the services sector index has grown, seasonally adjusted, to 54.8 after two previous months of modest growth. However, retail sales figures remain flat. The current account deficit increased from 2.4% of GDP to 3% for the year ended June 30th. BusinessNZ has observed no change in the manufacturing sector index for the second month in a row, measuring a seasonally adjusted 49.2.

New Zealand now ranks third in the Economic Freedom of the World Index for 2008. Cabinet ministers are to be authorized to exercise greater authority in reference to decisions relating to foreign investment. The NZX futures market opened on October 8th and saw its first sale on October 12th. In its annual report the Treasury noted a decision to lower the Government’s operating allowance to $1.1 bn, the new budget’s tax reform initiatives, the work of the National Infrastructure Unit in helping plan NZ’s infrastructure needs and investment, and the partial shutdown of initiatives introduced in response to the global financial crisis, namely the Crown Wholesale Guarantee Facility and Crown Deposit Guarantee Scheme. (The author is Director, Australian APEC Study Centre at RMIT University.)

Latin America

Weak US dollar has put Latam governments on alert

Cheng-Mount Cheng

US dollar started to fall in June as the worries of European sovereign debt crisis spilt over to hit the US economy. In particular, Fed officials changed their sanguine view on US economic outlook in September Federal Open Market Committee meeting and showed their concerns on the slow progress in employment pickup and the lower-than-target inflation rate such that further accommodation in monetary policy is hinted. As a result, US dollar took another downturn thereafter as the dollar index plunged to 22-month low.
Weak US dollar has put Latam (Latin America) currencies on the rise in the second half of this year as hot money once again flowed into this region. Chilean Peso led the currency appreciation against the greenback by revaluing 11.4% from June 30 to October 19, followed by 6.6% of Brazilian Real, 4.7% of Colombian Peso, 3.8% of Mexican Peso, and 1.1% of Peruvian New Sol.

The inflow of hot money also put Latam governments on alert. In a move aimed at curbing excessive inflows, the Brazilian government announced on October 4th to increase the IOF tax (Investment of Foreigners tax, a tax on financial transaction) on Fixed Income Foreign inflows from 2% to 4%. For equity inflows, IOF tax stayed at 2% and foreign direct investment remained exempted from IOF tax. Two weeks later, Brazil Finance Minister Guido Mantega announced another IOF tax hike to 6% from 4% on foreign investment in domestic fixed income products. In addition, the tax on margin deposit in the futures market was raised to 6% from 0.38% for foreigners. Brazilian Central Bank President Henrique Meirelles said the hypothesis of a bubble in Brazilian asset prices was worrisome on the same day. This is the third time Brazilian government has raised the IOF tax in one year. On October 19th, 2009 the IOF tax on fixed income inflows was raised to 2% from 0%. Mantega warned of a “currency war” and urged other economies to take coordinated action against the weak dollar.

In addition to measures of the Brazilian government, the Colombian and Peruvian central banks have stepped up dollar purchases while Chilean government was urging monetary authorities to take a more aggressive stance against the currency’s appreciation. Other measures taken by Latam economies include financial sector supervision, tighter liquidity control and management, prudential capital control and further liberalization of selected outflows.

In general, volatility in the foreign exchange markets so far has not yet derailed the economic recovery in the Latam, despite mixed outlook for member economies in this region. According to IMF’s most recent World Economic Outlook in October, growth in Latam is projected to average 5.7% in 2010 and 4% in 2011. Solid macroeconomic policy fundamentals, sizable policy support, favorable external financing conditions, and strong commodity revenues all contributed to a faster exit of the global crisis for the Latam economies.

Risks to the outlook emerge from both external and domestic factors. External risks are tilted to the downside, reflecting mainly slower recovery in advanced economies and its negative spillovers on commodity prices. A large presence of foreign banks in Latam may enlarge this contagion channel, even though these banks have relied primarily on subsidiaries funded by local deposits rather than cross-border flows. On the other side, there are risks of overheating, particularly if unwinding of earlier stimulus takes longer than currently anticipated.

The IMF recommends that Latam economies establish policies to achieve strong and sustainable growth like Asia. The priority is to use the window provided by the cyclical upswing to start unwinding stimulus, regain room for policy maneuver, and sustain its relatively recent track record of strong macroeconomic policy management. For instance, fiscal tightening will help address risks of inflation pressure for economies, like Peru and Uruguay and exchange rate overvaluation for Brazil, reduce public debt and provide a cushion for future contingencies. With respect to the approach to capital inflows, the IMF supports the possible use of capital controls supported by other measures such as the flexibility of two-way exchange rate to discourage speculative inflows, fiscal consolidation, and enhanced financial sector monitoring and supervision. (The author is Vice President, Citi Taiwan.)

Appreciation against USD among major Latam economies (from June 30th to October 19th)

<table>
<thead>
<tr>
<th>Currency</th>
<th>Appreciation</th>
</tr>
</thead>
<tbody>
<tr>
<td>CLP</td>
<td>11.4</td>
</tr>
<tr>
<td>BRL</td>
<td>6.6</td>
</tr>
<tr>
<td>COP</td>
<td>4.7</td>
</tr>
<tr>
<td>MXN</td>
<td>3.8</td>
</tr>
<tr>
<td>PEN</td>
<td>1.1</td>
</tr>
<tr>
<td>VEB</td>
<td>0.0</td>
</tr>
<tr>
<td>ARS</td>
<td>-0.6</td>
</tr>
</tbody>
</table>

Source: Bloomberg
As European workers return from their summer holidays, there is an altogether more relaxed mood amongst policy makers about the challenges they face, even though there are an increasing number of worrying signs and signals emerging from the markets, from international developments and from domestic political developments that suggest that serious threats to economic recovery remain.

It may perhaps be because these danger signs are not closely interconnected and will have varying affects in the short, medium and long terms, and across various sectors. Their implications for growth, employment, export and the SME sectors are not at all clear.

Perhaps the most significant of these developments are the growing tensions over exchange rate management, currency values and the possible impact of Quantitative Easing (QE) measures in the U.S, Japan and the U.K. At the same time, European policy makers are torn between consolidation and austerity strategies to reduce debt and deficits; and expansionist strategies to preserve employment and growth. The beginnings of a two-speed Europe would thus appear to be emerging, with uncertain consequences.

As an enduring backdrop remains the problem of credit. Borrowing is difficult and expensive and the SME sector in particular is struggling for trade finance, while larger businesses can raise funds through deleveraging and by issuing IPOs. There are few signs of change in this crucial area even though interest rates remain historically low.

The implications of these developments on the APEC SME sector, though largely indirect, would appear to fall into the following four broad areas.

First of all, the EU is likely to find it harder to export its way out of recession with the Euro gaining against the dollar. EU products will be more expensive, which conversely means that imports will be cheaper which could provide a stimulus to APEC SMEs. However, lower EU growth levels (if at all) will perhaps keep overall demand low, especially if unemployment remains high – which seems likely. At the same time, enduring credit problems could mean that payments (especially to SMEs) could be delayed in all categories of payments, which adds risks to importers and exporters where exchange rates fluctuate.

Secondly, QE measures together with low returns on EU investments, means that investment flows to Asia in particular (though not necessarily for the whole APEC region) will likely increase sharply. Asset price bubbles are likely to result which together with rising currency values, could prove to be destabilising in a number of ways. Indeed, signs of this are already being reported and governments in Asia have been considering appropriate policy responses ranging from capital controls to taxes on capital flows into non-priority sectors. At the same time, QE measures will give rise to calls for interest rate increases in anticipation of inflationary pressures developing.
Thirdly, the sovereign debt crisis in several EU economies, which could prove to be more serious and enduring than earlier expected, is likely to mean that state assets will be put on sale, and relatively cheap for international investors. How this could affect APEC SMEs is obviously unclear (partly because it hasn’t happened yet) and could presage some reorganisation of supply and manufacturing chains.

And finally, financing problems are contributing to be persistent high unemployment and is making the EU more protectionists while also generating anti-immigrant sentiment. Indeed, the unemployment problem is a particularly complex structural problem for EU policy makers that will take years to solve.

Looking ahead, the November G20 meeting in Seoul is likely to be important for EU policy makers, especially with respect to coordinating policy responses to the current crisis through Central Banks, through Finance Ministries and through banking regulators. There are questions being asked in the EU as to whether policy coordination between a mixed group like the G20 is at all possible across this complex range of issues, or whether the G20 should confine itself only to addressing the issue of global imbalances. China’s exchange rate management regime is thus considered a test case.

At a more EU level, Ireland’s levels of debt were far higher than expected and caused significant concern, together with a downgrading of sovereign debt in Ireland and Spain. The belief is that Ireland (and Spain) will have to continue with very severe policy changes to restore investor confidence. The question being asked in this context is whether this is politically manageable. (The author is Associate Director & Senior Programme Advisor, International Policy Unit, London School of Economics and Political Science.)
The issue of European sovereign debt has been looming over the markets in recent months. Although it is a problem more related to the Euro area, East Europe has also been shadowed, due to its close ties to the region. Fortunately, since June only particular areas have been affected, excluding one exception that occurred briefly in early September.

Despite the negative development, East Europe continued to see progress in its economic recovery, as the ESI survey suggested a general improvement in September. In addition, in the past month, the CDS of East Europe public debt declined, partially due to the ailing US dollar, which fueled demand for alternative assets, and relieved refinancing pressure for indebted sovereign borrowers. In the near term, as concerns in the market will mostly focus on currencies, it may be a suitable time now to discuss the issue of sovereign debt from a more fundamental and longer term point of view.

Economic growth and borrowing costs are the key to debt managing

Public indebtedness is usually compared to its GDP size as “debt to GDP ratio.” The theoretical annual cost of servicing public debt would be the yield (the nominal rate of return demanded by creditors) from its bond auctions, multiplying the size of outstanding debt. Considering all debt services are refinanced with debt and there are no further government deficits, for an economy to service debt indefinitely and maintain the debt to GDP ratio at current levels, the size of the economy has to grow (nominally) by the size that matches the cost of servicing debt. For example, for an economy with debt 80% of the GDP size and bond yield 5%, the cost of debt servicing is 4% of GDP per annum. The nominal economic growth rate of the economy, which is its real growth rate plus inflation rate, will have to be at least 4% to maintain the current debt to GDP ratio.

Troubled economies need each and every remedy-asset sale, economic reform, cheap money, and budget surplus

The above subtitle means the ability of an economy to service debt is better if its economy grows faster in the long run, and when the market demand on yield is more modest. But in the case of economies that are currently having too much debt for them to maintain, given their hampered growth and very demanding market yields, their options are limited. If the outstanding debt is less than its GDP, they can choose to run a slightly higher inflation – though it pushes up yields, it would beef up nominal growth rate more since the GDP is greater than debt (though not too high or cause inflation to be too unstable, as it would push up yields and deflate the currency more than desirable in the long run).

But for the case of Greece, its debt is more than their GDP and being part of a common currency rules out the inflation option. Hence, the remaining option is to enhance growth and to find cheap money for an indefinite period, or drop the entire idea of maintaining debt indefinitely. The Greek economy has been a lagging performer for many years already. With no obvious change to the current status, they won’t be able to find cheap money either. Thus, the Greeks have been left with the repay option. This is exactly what is occurring now – the Greeks are now committed to remove
the deficits and asset sales, while also receiving affordable money from non-market sources and restructuring the economy to make it productive in the long run. Recently, the IMF just announced its funds provided for Greece would extend beyond 2012, a positive response to Greece’s efforts in taking the right steps in curbing debt. In addition, the Chinese now see purchasing Greek’s debt as a way to increase its influence in Europe - thus the emergency alarms can be turned off for the moment and we can wait for further reforms to be made.

**Most East Europe economies are satisfied with their debt, though a few laggers need a little helping hand**

For the other economies in the East Europe region, most of them are emerging economies that have just been released from the Iron Curtain for a mere two decades. Each respective economy is still on their way to make up for the lost time and reach their productivity potentials. There is plenty of room and abundant resources for growth, which thereby helps solve the problem of debt in the long term, as long as borrowed money is used properly to support economic development. We thus look at the second best scenario, to see if economies of the region were able to maintain their current debt to GDP ratio indefinitely under current inflation and economic growth levels. The maximum bond yield that each economy can afford to just maintain its current debt to GDP ratio is given in the 4th column of Chart 1 (2010 data) and Chart 2 (2011 estimates).

Compared to the PIIGS economies in which affordable yields are hardly to be positive, almost every economy in the region can afford yields above 10%, with the exception of Hungary, Latvia and Cyprus. In reality, sovereign bond yields are hardly ever above 10% (not even for Greece), thus this result is quite satisfactory. The only question regarding the results is whether the economic growth rate and inflation rate in these economies are sustainable. For the former, as the region is still emerging, and just suffering from the financial crisis, growth rates in 2010 and 2011 would be more likely to be under their long term growth potentials rather than being overestimated. For the latter, inflation is a more susceptible issue only in Romania (constantly around 5.5%) and Hungary (ranging from 4%~6%). That is why Hungary and Romania are the two economies that needed IMF assistance during the crisis.

Hence, we draw our conclusion as follows: As long as economic growth is accomplished with a sustainable foundation (i.e. avoid bubbles) and inflation is controlled reasonably with prudence when running deficit spending, there is no reason for fear of a widespread sovereign debt crisis of the region. The worst case scenario may occur for Hungary and Romania, but this would need to be handled by the IMF. (The author is President, Polaris Research Institute & Honorary Professor, and Professor College of Technology Management, National Tsing Hua University.)

**Chart 1 Economic growth, Inflation, Public indebtedness figures (2010)**

<table>
<thead>
<tr>
<th></th>
<th>Real GDP growth %</th>
<th>Inflation %</th>
<th>Debt to GDP %</th>
<th>Affordable yield %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greece</td>
<td>-3.971</td>
<td>4.6</td>
<td>130.243</td>
<td>0.482943</td>
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<td>Ireland</td>
<td>-0.273</td>
<td>-1.601</td>
<td>93.634</td>
<td>-2.00141</td>
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<tr>
<td>Italy</td>
<td>1.003</td>
<td>1.627</td>
<td>118.358</td>
<td>2.222072</td>
</tr>
<tr>
<td>Portugal</td>
<td>1.122</td>
<td>0.928</td>
<td>83.134</td>
<td>2.465898</td>
</tr>
<tr>
<td>Spain</td>
<td>-0.345</td>
<td>1.497</td>
<td>63.453</td>
<td>1.815517</td>
</tr>
<tr>
<td>Cyprus</td>
<td>0.415</td>
<td>2.233</td>
<td>60.834</td>
<td>4.336391</td>
</tr>
<tr>
<td>Poland</td>
<td>3.361</td>
<td>2.428</td>
<td>55.169</td>
<td>10.49321</td>
</tr>
<tr>
<td>Romania</td>
<td>-1.94</td>
<td>5.884</td>
<td>35.494</td>
<td>11.11174</td>
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<tr>
<td>Bulgaria</td>
<td>0</td>
<td>2.218</td>
<td>18.184</td>
<td>12.19754</td>
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<tr>
<td>Hungary</td>
<td>0.573</td>
<td>4.67</td>
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<td>6.691085</td>
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<td>Slovak Rep.</td>
<td>4.1</td>
<td>0.7</td>
<td>41.84</td>
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<tr>
<td>Slovenia</td>
<td>0.849</td>
<td>1.5</td>
<td>34.542</td>
<td>6.800417</td>
</tr>
<tr>
<td>Estonia</td>
<td>1.785</td>
<td>2.537</td>
<td>8.131</td>
<td>53.15459</td>
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<tr>
<td>Latvia</td>
<td>-0.979</td>
<td>-1.424</td>
<td>42.151</td>
<td>-5.70093</td>
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<tr>
<td>Lithuania</td>
<td>1.289</td>
<td>1.047</td>
<td>39.483</td>
<td>5.91647</td>
</tr>
</tbody>
</table>

**Note 1:** “Affordable yield” is computed by adding column 1 to column 2, and then is divided by column 3.

**Note 2:** Negative figures in column 4 are inconclusive.

**Note 3:** Italics indicates member of Euro area.

**Source:** IMF WEO database.
Note 1: “Affordable yield” is computed by adding column 1 to column 2, and then is divided by column 3.

Note 2: Negative figures in column 4 are inconclusive.

Note 3: Italics indicates member of Euro area.

Source: IMF WEO database

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Russia and Middle East

Currency appreciation threatens the export in the Middle East

*Ming-Hsin Kung*

With a stable sovereign finance, Russia will embrace a free-trade era.

Under the circumstances that the food export sector of Russian has been impacted and its energy sector has increased investments, the question of whether Russia has a stable finance has become an issue of concern. Russian Prime Minister, Vladimir Putin said in this month that although Russia is going to invest more in industries, its debts are limited to around 11% of GDP in 2011, and its total debts in the future will also be limited to less than 20% of GDP.

Russia set up an anti-crisis fund in its federal financial budgets in 2009 and 2010, but as Putin pointed out, there will be no such mechanism in the federal budgets in 2011 to 2013. Since the second half of this year, the exchange rate of Russian ruble to US dollar has depreciated by about 6%. Compounding the fact, the government increases investments. Why is the Russian government not worried about the risks of sovereign debt? The main reason is that several future large projects of industrial developments do not need the government to invest in by incurring debts; the investment will come from overseas partners with whom Russia has medium- and long-term stable relations.

The increased cooperation of Russia and China in the sector of energy resource is an example. China in cooperation with Russia is going
to invest 22 billion rubles in building an iron mine factory in order to manufacture 6 million tons of raw irons production per year to the Russian and China markets. This instance reveals that Russia is adopting the “China mode”—with both the investments and markets necessary for its industrial developments coming from overseas. In this way, Russia is assured that China will be a support for the funds that the Russian energy industry needs in the early development, as well as the cash inflow in the later operation. Besides, Russia is also planning to promote a project of privatizing state-owned corporations in the next five years, which will yield about five billion US dollars and contribute to the government finance.

Another point of concern this month is after the long efforts of 17 years, Russia finally completes the stage of bilateral negotiation with WTO, and it is expected to become the 154th WTO member in 2011. At this final key point of the important progress to the relationship with Russia, the U.S. obtains concrete commitments from Russia regarding the issues of the protection of intellectual property rights, the government procurement, and policy-making transparency, etc.. The U.S. will help Russia complete the multilateral negotiation procedure of entering WTO, as well as incorporate Russia into the regulations of the world trade system. This has a long-term positive significance to the reduction of risks that the SMEs of the APEC members would have in their trade-investment relations with Russia.

Middle East has a stable political situation, yet with its export influenced by the depreciation of US dollars

When it comes to the Middle East, the U.S. economic block against Iran has encountered passive boycott from the Middle East economies. As Turkey has a bilateral trade with Iran, which reaches one billion US dollars annually and which has a high potential of growth, it is now attempting to convince the U.S. to amend its sanctions, lifting the ban on trading with Iran. At present, the political situation in the Middle East is likely to continue being moderate due to the influence of economic profits.

Another fact worth attention: as the US dollar goes down and the hot money flows into the emerging markets, the exchange rates of the various Middle East currencies to the US dollar are generally rising. So far the central banks of the Middle East economies have not take any strong measures against the depreciation of the US dollar, which leads to greater pressure on many Middle East economies with larger export sectors, such as Turkey. The exchange rate of Turkish lira against US dollar has risen by over 9% since June, 2010, causing a great damage on the profits of exporters. Moreover, the situation also brings some degree of risks in the future economic stability of some Middle East economies. (The author is Vice President, Taiwan Institute of Economic Research.)
In the last one month period (mid-September to mid-October), there have been slight warning signs of a crisis in the global commodity market. There was a steady gain in commodity prices due to continued US dollar depreciation and expectations for a second round of quantitative easing (QE2). But, still in terms of demand, it is uncertain whether commodity prices will continue rising amid an increasing possibility of a slowdown in the global economy.

Following the collapse of Lehman Brothers in 2008, the Federal Reserve (Fed) quickly expanded money liquidity to the real economy. This first round of quantitative easing amounted to approximately 1.7 trillion USD. The Fed’s intervention helped swiftly push up asset values including commodities; however, it was not enough to keep boosting the US economy. Furthermore, world economic growth rates were showing signs of a slowdown. It is consequently expected that the Fed will again inject massive amounts of money into the markets although the effectiveness of the second round of QE is still controversial among economists. However, the one thing for sure is that the QE2 will lead to US dollar depreciation and an increase in commodity prices.

The top two commodity indices, the Reuters CRB Index and LME non-ferrous index, have shown apparent gradual increases from mid-September to mid-October. The Reuters CRB index (year 1967=100) moved up from 525 points to 556 and the LME index (April 1999=1,000) increased from 3,508 to 3,871. The average for the Reuters CRB index from mid-September to mid-October increased 6.9% while the average for the LME index rose 8.7%. Such changes are positive signs that there are still upward trends and steep slopes within the commodity indices compared to the previous month. In terms of price variations, daily price changes of both the Reuters CRB index and the LME index were higher than those in the mid-August to mid-September period, indicating an increase in investment risk in commodities.

As for energy prices, the WTI near month futures price moved within the range of 73.52 and 83.23 USD/barrel and Dubai crude prices moved between 74.67 and 82.0 USD/barrel during the same period. Both the minimum and maximum values were larger than those in the mid-August to mid-September period.

Among non-ferrous metals or more commonly known as base metals, tin and zinc prices raised the most following the previous period, with the average prices of tin and zinc rising 15.1% and 11.6% respectively. The hottest base metals in the first half of this year, nickel and copper, also showed rising price patterns. The maximum price of copper and nickel for the last one month period were 8,412 USD/ton and 24,875 USD/ton, respectively. The recent price for copper broke the previous yearly high of 7,950 USD/ton recorded in April and nickel prices rose to almost approach the yearly high of 27,600 USD/ton. Other base metals including aluminum and lead also revealed increasing variations.

The most important variable we must keep a closer eye on during the coming month (mid-October to mid-November) is the commencement of the QE2 and how much it will impact the value
of the US dollar. The Bank of America expects the Fed to expand its quantitative easing program by 500 billion USD to 750 billion USD as early as the first quarter of 2011. Recently, commodity prices have become more dependent on monetary movement mainly due to the anticipation of the QE2 rather than the global economic slowdown. Therefore, further quantitative easing by major economies will likely boost commodity prices even if global demand stays weak. However, this means there is an increasing possibility that SMEs, especially manufacturing firms, will face difficulties in terms of production costs. (The author is Research Fellow at Samsung Economic Research Institute.)

\begin{table}
\centering
\caption{Changes in Raw Material Prices - September 16\textsuperscript{th} to October 15\textsuperscript{th}, 2010.}
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|}
\hline
 & Index & Crude Oil (USD/barrel) & Non-ferrous Metals (USD/ton) \\
 & & & & & & & & & \\
\hline
 & Reuters CRB & LME & WTI & Dubai & Copper & Lead & Nickel & Zinc & Tin & Aluminum \\
\hline
Min. & 528 & 3,508 & 73.52 & 74.67 & 7,670 & 2,126 & 22,300 & 2,129 & 23,175 & 2,132 \\
Max. & 556 & 3,871 & 83.23 & 82.00 & 8,412 & 2,408 & 24,875 & 2,399 & 27,600 & 2,402 \\
Average & 538 & 3,697 & 78.99 & 78.20 & 8,041 & 2,258 & 23,627 & 2,233 & 25,003 & 2,289 \\
Mid-August to Mid-September Average & 503 & 3,401 & 74.53 & 73.39 & 7,420 & 2,094 & 21,688 & 2,083 & 21,356 & 2,085 \\
\hline
\end{tabular}
\end{table}

Note:
1. The Reuters CRB index recorded 100 in 1967 and LME non-ferrous index recorded 1,000 in April 1999.
2. The WTI price is based on the near month futures price traded in NYMEX and non-ferrous metal prices are based on the spot prices traded in LME.
The global economic crisis drove the Japanese economy into recession, with real GDP for 2009 plunging by 5%. Japan’s economy has since entered a recovery phase, as evidenced by a high real GDP growth rate of 5% on an annualized quarter-to-quarter basis in the first quarter of 2010. However, the growth rate dropped to 1.5% in the second quarter, indicating a weakened pace of economic recovery. This partly reflects: (1) the fading impact of stimulus measures that spurred household spending on cars and electronics, (2) a cut in the temporarily increased government expenditure, and (3) a deceleration of the export growth. As a result, output gaps (difference between actual and potential GDP) have remained large at minus 4.5% of GDP, making it difficult for the economy to increase employment and eliminate deflation.

Growing Concerns about the Yen’s Appreciation

Further increasing Japan’s pain, the yen has appreciated against many currencies. In particular, the yen against the US dollar appreciated rapidly from ¥94 in early May to ¥83 in early September. Japanese firms and politicians are seriously concerned because the strong yen deteriorates the price competitiveness of Japan’s export sector, which has been functioning as the main engine of economic growth. When the yen reached ¥82 yen, therefore, the government broke a six-year hiatus and on 15th September 2010 decided to intervene unilaterally in the foreign exchange market. The scale of intervention for one day amounted to ¥2 trillion, the largest amount in the history of such moves. The government has since continued with sporadic interventions with the total volume now amounting to ¥2.1 trillion throughout September.

In addition, the Bank of Japan (BOJ) on 30th August introduced a 6-month liquidity-providing operation totaling ¥10 trillion. This was followed by a re-introduction of a virtually zero-interest rate policy, and on 5th October, the establishment of a ¥5 trillion asset purchase program; eligible assets included JGBs (Japanese government bonds), commercial paper, corporate bonds, and exchange-traded funds (ETFs), as well as Japan real estate investment trusts (J-REITs).

However, even with these efforts, the yen did not depreciate on a sustainable basis. The yen appreciated further to ¥80 against the US dollar in mid-October—a 15-year peak record.

Rationales for the Currency Intervention

Interestingly, the Financial Times on 15th September 2010 called Japan’s intervention as “a very political intervention” rather than an economically-justified one. This was because (a) the yen (measured in terms of real effective exchange rate) has not been excessively overvalued as compared with its historical average, (b) Japan’s...
trade surplus has been growing, and (c) Japan’s prolonged deflation is likely to have improved the value of the yen relative to the currencies of the United States and other trade partners, whose prices have been rising.

Moreover, the sheer fact that Japan is the largest net external creditor in the world and that the United States is the largest net external debtor supports a stronger yen relative to the US dollar. Chart 1 shows the movements of real effective exchange rates (exchange rates adjusted for price differences) of the major currencies. The trends appear to indicate that the current value of the yen has been consistent with the historical average despite the recent rapid appreciation.

Mr. Jean-Claude Juncker, chairperson of the Eurozone finance ministers’ meeting, also expressed uneasiness about Japan’s unilateral intervention, suggesting that an uncoordinated intervention would not be effective and that the current value of yen against the euro has been too low, rather than too high.

The view of the International Monetary Fund (IMF) is in line with the aforementioned opinions. According to the IMF Consultative Group on Exchange Rate Issues (CGER), the current levels of the yen as well as the euro (measured in terms of real effective exchange rates) have been in line with the fundamentals; the dollar has been overvalued; and the renminbi has been largely undervalued. The undervaluation of the renminbi appears obvious given the huge accumulation of foreign reserves, $2.65 trillion (accounting for 71% of total foreign assets) as of end-September 2010. This is also supported by China’s substantial current account surpluses and large FDI inflows.

To date, criticism by the U.S. government and the European Union of Japan’s currency intervention have been muted relative to those made against mainland China, because it has been felt that the yen has not been undervalued and thus is less problematic than the renminbi. There appears a growing consensus in the international community, as articulated in the recent G7 finance ministers’ and central bankers’ meeting on 8th October 2010 that emerging economies, typically China, should conduct greater reforms aimed toward more flexible exchange rate regimes.

Asian Exchange Rate Policies and Global Economic Recovery

Although the scales of intervention have been milder and more sporadic than that of mainland China, Korea and Chinese Taipei have also actively intervened in the foreign exchange markets. The pace of the accumulation of foreign reserves accelerated since the second quarter of 2009 for Korea and the fourth quarter of 2008 for Chinese Taipei, thanks to the increase in current account surpluses. At the end of 2009, foreign reserves
accounted for 45% of the total foreign assets held by Korea and 35% of those held by Chinese Taipei.

The CGER notes that the Korean won has been undervalued, notwithstanding Korean officials’ claims that the intervention was aimed at smoothing the volatility of exchange rates (especially vis-à-vis the US dollar). This assessment appears to be in line with the fact that the Korean won has remained below its pre-crisis level (see Chart 2). The CGER has not assessed Chinese Taipei’s currency, but the declining trends for the Taiwan dollar, despite the growing trade surplus and accumulated foreign reserves, seem to suggest that the currency has also been undervalued.

When the yen began to appreciate rapidly against the US dollar, it also appreciated against the Korean won and the Taiwan dollar. Korean and Chinese Taipei’s firms increasingly compete with Japanese ones in the fields of electronics, electronic components, and machinery. Japanese industry leaders have expressed anxiety about the potential loss of price competitiveness of their export products against those of Korea and Chinese Taipei.

However, the underlying problem is with the exchange rate movements of those Asian currencies vis-à-vis the US dollar, not moves against the Japanese yen. Globally, non-intervention currencies (such as the US dollar, euro, and the British pound) and intervention currencies (namely, Asian ones) coexist. The euro authorities have stopped intervening in the currency market since the last intervention conducted by the European Central Bank (ECB) and by itself in 2000, and have let the market determine exchange rates.

There is a widely accepted view that the presence of different exchange rate regimes makes it difficult to reduce global imbalances—a large current account deficit in the United States and large current account surpluses in Asia inhibit any global economic recovery achieving a sound footing. It is becoming increasingly important that major economies hold intensive discussions on currency issues and improve coordination of macroeconomic policies. On the one hand, the Asian economies now in a remarkable economic recovery phase confront capital inflows and inflationary pressures (mainly as a result of positive output gaps). On the other hand, advanced economies, such as Japan, the United States and Europe, suffer from a shortage of domestic demand and high unemployment rates. A need for greater coordination is more critical than ever. A coordinated currency intervention is obviously better than a unilateral intervention as conducted by Japan. (The author is Professor of Economics, Keio University.)

Chart 2 Trends in the Real Effective Exchange Rates: Korea and Chinese Taipei

(2005Q1=100)

Note: An increase indicates an appreciation of the particular currency. Source: Prepared by the author based on IMF data.
How can SMEs reduce risk through interpreting business indicators? - an introduction

*Ming-Hsin Kung*

Because of the scale and resource constraints, it is difficult for small and medium enterprises (SMEs) to cope with the dynamic changes and potential risks of the current market environment. The first step that SMEs can manage the market environment changes is proper understanding of the method to interpret business indicators. In terms of operational risk management, a comprehensive understanding of the method to interpret indicators is considerably a subject matter worth learning for SME owners. Hence, this article aims to introduce the systematic approach in interpreting business indicators and enable SME owners to make rational business decisions and reduce risks caused by fluctuations.

In terms of definition and scope, business indicators are analytical figures which reflect the activities of economies’ consumption, investment, and export/import trade. The characteristics of the indicators can be divided by supply and demand sides. From the demand side (B2C) perspective, SMEs can identify the indicators of the overall spending on target market, including unemployment rate and related indicators, Consumer Price Index (CPI), retail sales and related data, and the average disposable income of households. From the supply side (B2B) perspective, SMEs can identify the indicators of the product/material markets’ overall supply and price trends, including Industrial Production Index (IPI), Purchase Management Index (PMI), currency rate, interest rate, employee salary, and Producer Price Index (PPI).

Besides, business indicators can also be classified into three categories based on which stages in the time sequence the indicators can reflect the economic development, namely: leading, coincident, and lagging indicators. The main function of leading indicators is to signal possible economic turning points. Based on the nature of rational expectation in capital markets, leading indicators usually include not only a few monetary indicators such as “interest rates, money supply, and stock prices”, but also other indicators which respond to the situation of future demand/supply such as “Consumer Confidence Index (CCI), Construction Permits, and Purchase Management Index (PMI)” Coincident indicators signal the instant trend in the economic cycle such as the IPI, retail sales index, and working hours per week. Lagging indicators usually act as a confirmation to the economic orientation. Lagging indicators usually respond to the behaviors which businesses could only start to adjust in the middle or long term. Currently the most widely used lagging indicators for supply are related indicators responding to the labor market, such as average time length of unemployment, number of employees, standard salary, and many more. Stock to sales ratios and installment credit to personal income ratios can also be used to confirm lagging indicators of the demand and supply orientation.

As to how SMEs can combine and apply the business indicators to analyze the economic trends and make strategic decisions, the table below is provided as a basis for simple interpretations. The economic cycle can be simply classified into four phases: prosperity, contraction, recession and recovery. If we want to verify that the current economy is continuing to rise up the ladder and have not yet reached “prosperity phase” before reaching a high point, the above three set indicators should basically present a uniformed rising pattern. Basically it can be confirmed that the economy is in prosperity phase as long as the leading indicators
do not present any changes and lagging indicators rise steadily. At this time, businesses can adopt more active expansion strategies on the scale of their production and sales.

### Table 1 Economic cycle and trend indicators

<table>
<thead>
<tr>
<th>Economic Cycle Phases</th>
<th>Trend Indicators</th>
<th>Possible Business Strategies</th>
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<td>Prosperity</td>
<td>Three indicators uniformly rise</td>
<td>Expand scale for production and sales</td>
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<td>Contraction</td>
<td>1. Leading indicator slides.</td>
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<td>Recession</td>
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<tr>
<td>Recovery</td>
<td>1. Leading indicator rises.</td>
<td>Business restructuring</td>
</tr>
<tr>
<td></td>
<td>2. Coincident and lagging indicators slide slowly.</td>
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</table>

However, when leading indicators start to present a slide with the rise of coincident and lagging indicators starting to slow down, the economy has reached to a relatively high point and will turn to “contraction phase”. Businesses at this time need to begin adopting cautious expansion strategies if many of the leading indicators start to slow down or slide. When the three main indicators uniformly slide, the economy has come to a confirmed recession phase and SMEs during this period must continuously adjust the structure of their costs to survive the low season of the economic cycle. Until leading indicators rise up again and coincident and lagging indicators’ slides slow down, then the economy is confirmed to be entering the recovery phase; this time, SMEs can seize another opportunity in the economic cycle through business restructuring.

In terms of practice, since their small scale and more focused range of services and products, SMEs need to only select the supply/demand indicators related to their own industry. For example, the IPI, sales index, price index and business performance of the major companies from upper/lower stream affiliated industries are selected together with important macroeconomic indicators, such as: interest rate, money supply, and currency rate. The growth rate and supply-/demand-related indicators of the target market can also help SMEs roughly project the economic trends in their industry. (The author is Vice President, Taiwan Institute of Economic Research.)
Rainbow after the Storm: Pangasinan Women MSME Best Practices on Crisis Management

Myrna T. Yao

The Philippines is vulnerable to many natural hazards. It is affected by tropical cyclones, volcanic eruptions, El Nino and La Nina episodes, earthquakes, tsunamis, droughts and floods. The worst of these disasters have caused the loss of human lives, homes and livelihoods, and resulted in economic disruptions in billions of Philippine pesos.

In 2009 alone, two typhoons wreaked havoc to northern Philippines in a matter of ten days. First, it was tropical storm Ondoy (Ketsana) on September 26th, 2009. The heavy rainfall drowned Metro Manila in less than six hours. Floods rose at an unusual fast speed, taking only thirty minutes to reach six feet depth. It let many Filipinos take refuge over their rooftops where they remained at least for twenty hours before the rescue team came to their way. Meanwhile, floods slowly receded, if not at all, and destroyed many properties. Some houses and other means of livelihood were left beyond repair or recovery. Those rescued were given temporary shelter in evacuation centers.

Unbelievably, another typhoon struck the Philippines a week later and brought further destruction to Northern provinces like Cagayan and Isabela. Tropical storm Pepeng’s (internationally known as Parma) fierce winds uprooted many trees and likewise destroyed major infrastructures and means of livelihood. As if it were not enough yet, the tropical storm not only lingered still for a few days, but also and caused serious flooding and landslides in La Union and Benguet, especially in Pangasinan.

The aftermath is a vision of not just devastated areas but also devastated spirits. Many people died; a thousand families left homeless. The National Disaster and Coordinating Council (NDCC), a lead coordinating agency tasked to prepare for and respond to disaster situations, reported the estimated total damage amounting to P5.08 billion, including P3.99 billion to agriculture and private property and as well as P1.09 billion to infrastructure.

Northern Women Resiliency

“Before tropical storm Pepeng hit Pangasinan, our women members earned more than Php200 per day,” says Chole Penuliar, the president of Local Councils of Women of Mapandan (LCW-Mapandan). Mapandan is one of the low-lying municipalities of Pangasinan that were submerged in the flood.

LCW-Mapandan started its operation in 1998 with 120 marginalized women members from different barangays. Under the leadership of Penuliar, these women are producing pickled papaya (atsara), pickled sayote, and peanut butter,
among other products. The group sells their products in markets or restaurants in the nearby cities (Urdaneta and Dagupan); besides, some have established the networks for customers from private and government offices.

Penuliar generously lent her 2-hectare family farm lot for their growing members to till. Some of their members are also maintaining backyard gardens to add with the growing requirements of production. “Our members are widows, single-mothers and wives of carpenters, farmers, construction workers, etc. They are really in need of the additional income to fend for their respective families. With the farm lot, our group teaches them to plant rice, mango, and other vegetables. We also raise hogs and goats and sell them in the market,” explains Penuliar, who now leads a group of more than 300 women from different barangays.

What used to be the source of meager income for some 300 families had quickly dashed when the Typhoon Pepeng struck last year as the onslaught left them with almost nothing. “After the typhoon, nothing was left. Our farm was completely covered with flood water,” Panuliar says in vernacular, “heavy winds blew our work area’s roofs.”

Many of the local women members lost their homes; some even lost their loved ones. They were overwhelmed by the damage caused by the typhoon. Recovery was indeed a long way to go. “Before we could think of recovering the small enterprises we have established, we had to help build the homes of affected families,” recalls Penuliar. LCW-Mapandan coordinated with the local Department of Social Welfare and Development (DSWD) in restoring what was left of the storm.

Two weeks after temporarily rehabilitating some of the members’ homes, LCW Mapandan resumed its operation. There was neither papaya nor other vegetable to be harvested except for the mangoes that the wind blew and fell to the ground. Understanding the need to earn, these women MSMEs picked up those good mangoes from the ground and turned them into mango pickles. Even before the typhoon, they had capital to build up and savings from their monthly group earnings. “From our group savings, we bought bananas. Cooked turon and banana cue and sold them in the market,” says Penuliar, who is a nominee for 2011 National Outstanding Volunteer.

Through these alternative products, they were able to regain their capital within a month. When the Provincial Government of Pangasinan offered them a loan assistance, LCW Mapandan submitted all the requirements and were granted a total of Php130,000. “A good amount of money to expand their small-scale enterprises,” said Mona Alavaso, Pangasinan provincial social worker, who facilitated LCW-Mapandan’s loan request. According to Alavazo, all grants are given two months leeway before the borrowers will actually start paying their loans.

Lessons Learned

If there is one thing mightier than the wrath of nature, it is the resiliency of the Pangasinan women-led MSMEs. This crisis taught our LCWs that sheer practical skills coupled with the assistance from our partner Local Government Units, our marginalized women of the North successfully emerged from the calamity. Thus, GO-NGO partnership should be strengthened. In the province of Pangasinan both the municipal and provincial governments provided financial grants to women-led MSMEs.

Further, this eventuality showed the value of group savings and anticipating future events that might hamper the operation such as natural calamities. In the case of LCW Mapandan, each member pays Php30 monthly for their group savings and Php20 monthly for capital build-up. They have established the loan retention program. Under the loan retention program, each member can borrow money from the group savings without collateral but 3% of the loaned amount will be automatically deducted as part of savings.

MSMEs should also be trained on alternative means of earning in case that crisis occurs. Like what LCW-Mapandan did when their farm had nothing to offer but mangoes, they proved to be capable of doing other means of livelihood because they had acquired proper training.

Finally, organized women MSMEs should...
develop a mechanism for paying their loans on time. “LCW-Mapandan is a good borrower. The group once borrowed Php90,000.00 from the Provincial government and our record shows that they always pay on time. This is the reason why their second loan of Php130,000.00 was instantaneously granted,” affirms Alavazo.

As this article is being written, some homes of our women members in Mapandan, Pangasinan are still being repaired. The money they are using for their house repair come not from dole outs or loans but from their individual earnings. However, with the presence of La Nina phenomenon this year, more storms are expected to strike the Northern Philippines and the women MSMEs shall rise again after this debacle and will stand stronger than ever before. (The author is President, Filipino Chinese Federation of Business & Professional Women of the Philippines.)
Currencies of emerging economies have difficulty counteracting the appreciation pressure

Since the Japanese Yen appreciated to the highest point ever seen in 15 years, one after another the Korean Won, Taiwanese Dollar, Thai Baht, Indonesian Rupiah, Philippine Peso, Indian Rupee, Malaysian Dollar, Brazilian Real, South African Rand, Australian Dollar, and the Canadian Dollar have all risen to their highest point. The Chinese Renminbi has also faced an appreciation; after China loosened its currency peg in June, the Renminbi rose in October to the highest level since the Chinese government unified the official exchange rate with the market rate in 1993. However, in terms of degree of appreciation, Renminbi rose by only 2%, while the exchange rates of other Asian currencies to the US Dollar have risen by 6% in average, among which the Malaysian Yuan and Thai Baht rose by 9%, the highest degree among the Asian currencies. With this contrasting comparison to such other highly appreciating Asian currencies, Renminbi’s relatively minor rise is actually depreciated.

The problem of currency disputes between economies is rooted primarily in the fact that the economic growth continues to slow down in major economies, making the U.S., Japan and Europe maintain their loose monetary policy or quantitative easing measures to simulate aggregate demand. The overflow of money resulted from these measures can also be the first step. The Brazilian government has increased the tax on foreign investment in fixed-income securities (i.e. the IOF tax) from 2% to 6% within one month, and yet the high yield rate of Brazilian bonds still attracts the hot money. Likewise, Thailand plans to impose a withholding tax of 15% on foreign investors that buy its bonds.

Another feasible approach is to impose limits on foreign investors’ purchase of the domestic assets. South Korea limits its banks on their holding of financial commodities that are relevant to foreign exchange, and is very likely to enact more policy on limiting the exchange rate fluctuation. As to other emerging economies that have not adopted capital control measures such as Philippines and India, they have proceeded to intervene in the exchange rate because of their concern about the possibility of the hot money transferring into them. Nonetheless, there are also some economies that are not able to prevent their exchange rates from rising, including South Africa, who has already announced to intervene in the exchange rate fluctuation no more. Preventing the currency from appreciating can indeed enhance an economy’s export competitiveness, but it also brings about the risks of inflation and rise of asset prices, which have to be seriously considered by governments when weighing whether to intervene actively in markets or not.

How the international organizations face the currency competition

Facing the currency debates that are growing fiercer, the International Monetary Fund (IMF) was not able to reach an agreement on solution in its meeting in mid-October. Due to the huge disparity in economic performance among different places in the world, such conditions of the emerging economies as the over-fluctuation of the exchange
rates, the expansion of credits, the bubble of asset prices and the financial turmoil, plus the inflation pressure, the IMF has to warn about the economic stability in the emerging market areas. Moreover, it suggested a more active capital regulation on the hot money, so as to reduce the possibility of a new financial crisis. Although the IMF meeting failed to reach an agreement on how to solve the current problems of slow economic growth and competitive depreciation of currencies, in addition to the capital regulation, it also proposed some more suggestions about the strategies, such as the measures of lowering the interest rates, increasing the foreign reserves and retrenching the finances.

Similarly, the World Bank warned that, as the result of the high inflow of capitals into the East Asian economies, the loose fluidity will lead to a rise in stock markets and real estate market prices. The East Asian economies must cautiously control the inflation and avoid the bubbling of assets, which will both affect Asian economic stability. WTO (World Trade Organization) also pointed out that exchange rate fluctuations out of control will destabilize the trade system, causing harm to the global trade and economic revival; the scenario of economies competitive depreciation and possible trade wars and protectionism will especially influence the global trade revival and stability.

The G20 financial ministers’ meeting in October had an emphasis on the currency conflicts. In order to counteract the intervention of some economies in the foreign exchange market, others are likely to set up trade barriers by imposing revengeful tariffs on products from economies that manipulate the exchange rates. This scenario, however, triggers a deep concern about the prospect of the global economy—will each economy adopt protectionist measures against imported foreign products, as what happened in the 1930s, thus flaring trade wars and leading to another Great Depression?

The Institute of International Finance, consisting of more than 420 major financial institutions around the world, proposes cooperation as the way to ensure stability. It hopes there can be a new global agreement on the exchange rates of currencies, which will be the one taking the place of the Plaza Accord signed in 1985, and which it thinks will prevent the messy currency war. As the current situation shows, nevertheless, there is little hope that such an agreement can be reached.

The prices of raw materials and agricultural products continue rising

The hot money around the world not only flows into the emerging market economies but also the markets of raw materials. The prices of energy, such as fuel oil and coals, are very likely to rise to a highest point in recent times. In addition, under the influence of the hot money, the prices of metals including gold, bronze, platinum, aluminum, lead, nickel, tin, zinc, etc. have also reached to the recent high point. With the US Dollar continuing to go down, the price of gold recently keeps rising to the historical highest level. Even though gold is deemed as the “ultimate bubble” in the markets, as a safe haven for capitals and a means to maintain value, gold will continue to attract the hot money with the continuing fall of the US Dollar. Moreover, economies such as Korea, India, Thailand and Bangladesh are still increasing the proportion of gold in their foreign reserves, and this is another important reason for the little hope in the falling back of gold price.

There is also an influx of the hot money in the markets of agricultural products, with a dramatic increase in the prices of grains, including wheat, corn, bean, barley, oat, etc. The sharp rise in grain prices, in turn, caused a rise in the prices of fertilizers, which then brought the meat prices in the U.S. to the highest point in 25 years. Besides, the food prices, including that of sugar, coffee and palm oil, are also rising as the supply decrease under the influence of weather, and the demand increases due to higher income.

The tension continues in the global supply of agricultural products, triggering concerns on global food crisis. It is expected that the climate abnormality will becomes more severe in the future and have an influence on the growth condition of the major grains, as well as on their supply and demand around the world. Moreover, as a result the hot money will continue speculating in the markets, and the rise of global food price cannot be mitigated in the short term.
The 17th APEC Small and Medium Enterprises Ministerial Meeting

Chia-Wen Huang

Introduction

On October 2nd-3rd 2010, ministers and senior officials from the APEC economies gathered in Gifu city, Japan, for the 17th APEC Small and Medium Enterprise Ministerial Meeting (SMEMM), seeking ways to boost the growth of SMEs amid global economic recovery. The meeting was attended by Ministers or other representatives responsible for the SME policy of APEC 21 economies.

The purpose of SMEMM is to have APEC ministers meet together under the main theme, “Strategy for Reinvigorating Economic Growth with Dual Engine: SMEs and Asia Pacific Economy”, and discuss long-term growth strategies for SMEs in the region, including three sub-themes:

1. The impact of the economic crisis on SMEs, and the countermeasures implemented in response
2. Short-term prospects for SMEs, and SME measures required of APEC
3. Prospects for APEC SME policy: Looking forward 2020

The meeting was a “well-timed event as the SMEs are recovering from one of the worst economic recession in decades”, said Muhamad Noor Yacob, Executive Director of APEC Secretariat, at the opening ceremony. The current economic crisis has significantly influenced economic conditions in the APEC region. APEC economies asked to present their views on the three sub-themes in plenary. Nevertheless, we will emphasize on the impact of the economic crisis on SMEs, and the countermeasures implemented in response.

The past economic crisis has significantly influenced economic conditions in the APEC region. A review of these influences showed that the degree of influence differs from economy to economy. Ministers shared information among member economies on countermeasures implemented in response to the crisis and on self-assessments of their measures. Ministers not only spoke about when those measures ended or will end, but was also able to deepen their awareness of the differences in policy measures according to the degree of influence and the diversity of economic situations. The presentations mainly have two focuses:

Impact

Many representatives, generally speaking, provided a short review of the impact of the economic crisis particularly on the SMEs. Under the impact of the crisis, sales growths were low, and the demand conditions were poor. The level
of new orders was low, and the capital investment expectations were also negative, which lead to the confidence of small businesses to be very weak, and hesitant to expand and move forward. With this mindset, under the impact of the recession, many jobs were lost, simply because SMEs could not sustain the pressure of the poor market conditions or financial constraints. However it comes to no surprise that during the recession, SMEs were negatively impacted in terms of access to financing, which is a key for successful SME growth. Resulting from the negative economic growth and financial instability, pricing for SME credits was poor and the amount of loans available for SMEs were also limited.

**Responding policy**

**Having a positive macro-economic** fundamental framework is important for SME growth. The unhealthy fundamental framework causing highly imbalanced government budget is one of the reason leading up to the crisis. Some economies have spent a significant amount of time and effort to reduce its government debt.

In order to make it easier for banks to loan money, many economies increased the threshold in terms of percentage of loan guaranteed by government for SMEs, encouraging banks to give out loans instead of being afraid of possibly losing their initial lending money. Another important measure adopted by the economies is lowering tax burden. These measures help to improve business environment, and promote competitiveness of industries.

Economies have also invested a significant amount of money in state owned development bank in order to enhance liquidity in the markets, and provide more capital for SMEs. Some economies had created special programs for assisting SMEs in access to loans. For example, in the US, the small business jobs bill which was signed in October establishes a new small business lending fund that will be operated by the Department of Treasury.

**Other economies have created more opportunities for government contracting, cut taxes for SME’s, supported policies that spur innovation, exporting, and regional economic development, and provided services of information, training, technology, entrepreneurship, and management through public service platform.**

**Most important, economies not only emphasized the establishment of a joint crisis management mechanism, but also highlighted the importance of APEC SME Crisis Management Center. Ministers welcomed the establishment of the APEC SME Crisis Management Center as a tangible example of collaboration among SME Working Group (SMEWG) members.**

In light of meeting discussions probing into the impact and policy responses to the crisis, we proved that responding policies and exit strategies reflected the different situations of each economy. Bank loan is likely to remain the leading source of external finance for the majority of SMEs. International experiences and sharing mechanisms suggest that specific credit guarantee countermeasures on supporting SMEs’ growth can play an essential role in the mitigation of the impact on SMEs. What is more, enhancing the crisis management capability of SMEs is a significant measure for coping with economic crises; consequently, all economies should jointly take root to crisis management mechanisms in the APEC region.
Far from being the exception, crises are the norm

-cited From "Crisis Economics – A Crash Course in the Future of Finance", authored by Nouriel Roubini and Stephen Mihm

Hui-Wen (Teresa) Huang

In 2010, known for his prediction of the financial crisis, Dr. Doom (Nouriel Roubini) co-authored with Stephen Mihm in a book titled Crisis Economics – A Crash Course in the Future of Finance. The book provides answers to the problems related to the past crisis, and searches for the solutions for the crises that occurred in previous times and regions throughout the globe. It also elaborates that crises are not exception, but are normal phenomenon, and are neither unpredictable nor unpreventable as well. The book listed several principles for tracking and monitoring the economic crisis and utilized the past global financial crisis to explain crises prediction, prevention, response and methods of recovery.

The book points out that the financial crisis is not unprecedented as the world considered it to be, it’s just an infrequently occurring situation throughout the history, and crisis could often be identified through regular patterns. Perhaps detailed characteristics of the past global financial crisis is not entirely similar to those happened in the past hundreds of years, yet its pattern of development is extremely identical to the crises that took place over centuries. The author pinpoints that the reason causing this crisis can be tracked back to many pre-existing ailments. In other words, decades of trends and policies have created a bunch of complicated and non-transparent financial tools, risks embedded in the global financial system, problems with moral ethics, failures in company management, as well as the role that governments play on. As these similar economic and financial weaknesses accumulate, crisis would suddenly erupt into explosion as soon as it reaches breaking point.

The book further indicated that all crises shared the same beginning. At first, all situations seem to be relatively mild. It would take some time to progressively incubate before the dramatic outbreak, probably taking years or decades. In this time, several different forces gradually develop into the conditions suitable for the deterioration of the economic stability. Most crises began with soaring prices of specific assets, well beyond the basic standards of pricing. These phenomenons usually co-exist with large amount of debt, which often are positively related to the excessive growth in credit supply. The author thinks that the evolvement of crises always follows the same track, and the current crisis which exploded in 2007 is no exception. Therefore by generating the same expected results, the occurrence of crises becomes predictable.

The author indicated that although global economy has begun to recover, implicit risks and weaknesses may still trigger new crisis within a couple of years, plus the globalization development
could increase the frequency of risk occurrences and its lethality. For example, financial capital and hot money flowing in and out specific markets and economies has been increased, resulting in the rise of asset prices. While financial globalization is taking place, financial regulatory authority are still attached to their own economies; once the crisis breaks out, it would be difficult to come up with an effective response, hence making it more lethal. Besides, the power of the U.S. would be waning in the next few years, which means that one less superpower can cooperate with other emerging forces in achieving stable global economy. At that time, not only may the rate of crisis occurrence go up, but rate of fatality may increase. The author considered the recent financial crisis of the 21st century as the prelude of many crises to come.

SMEs have exposed to the major financial crisis in the 21st century, and therefore are able to gain better understandings of crisis. In the 21st century where the Earth is flat, the contagion of crisis becomes more unexpectedly severe. As a result, if SMEs seize this opportunity to actively and profoundly learn about the pattern of operation mode for the global economy and the impact of potential crisis, they would further understand the trajectory of crisis which may occur in the future. This book anatomizes diverse approaches to analyze the past financial crisis, allowing SMEs to review the danger in a different perspective. Furthermore, it helps to understand that such major financial crisis is not a single event throughout the century. Yet, readers can also realize from the book that crises are not as horrible as they have imagined because they can be predicted or even prevented in advance.