Asia: Weathering the Economic Crisis

Its banks are strong, while debt loads and inflation are low. But that doesn't mean there aren't challenges for investors

By Frederik Balfour

Cebu, Philippines - Painful economic slowdowns are nothing new to Southeast Asia. The region went through its own gut-wrenching financial crisis more than a decade ago in what now seems like a dress rehearsal for today's turmoil. Companies defaulted, banks collapsed, stock markets tanked, and economies shrank at double-digit rates as foreign investment slowed to a trickle. But Southeast Asia dutifully swallowed the bitter pill of austerity, devaluing currencies and working off debt while banks restructured and companies patched up balance sheets.

Now Southeast Asia is getting whacked again, a victim of sins on the other side of the globe. Last autumn the region's exports plunged as the U.S., and then China, slumped. Foreign investment, meanwhile, has plummeted as multinationals rein in spending. "It's frustrating that we are in a crisis that is not of our own making," says Thai Prime Minister Abhisit Vejjajiva.

Yet this downturn is hardly a full-blown repeat of the Asian crisis. That's testament to the surprising strength of the 10 countries that belong to the Association of Southeast Asian Nations (ASEAN). The region's banks are virtually free of toxic assets and haven't needed government bailout money. Years of trade surpluses and high savings rates have contributed to record foreign reserves. Debt loads—for governments, corporations, and consumers—are a fraction of those in the U.S. and Europe, and inflation and interest rates have fallen dramatically. "Of course there is a slowdown, but [these countries] are well prepared to weather the storm," says Mark Mobius, president of Templeton Emerging Market Funds. "They have outperformed global markets, which is telling us they are going to do quite well." ASEAN bourses have led the recovery in emerging-market stocks, with Jakarta's benchmark index up 70% and Vietnam's up 80% from recent lows.

Some companies operating in the region continue to do well, as demand for everything from computers to discount airline tickets remains strong. Unilever Indonesia has sold so much Pepsodent toothpaste, Lifebuoy shampoo, and other goods that its first-quarter revenue jumped 18%, to $412 million, boosting earnings 9%, to $70 million. "The impact from the global crisis is minimal," says Franky Jamin, Unilever Indonesia's corporate secretary. And London's Standard Chartered Bank, which gets two-thirds of its revenue in Asia, says first-quarter profits were its best ever, indicating that the region's slump will be shallower and shorter than elsewhere. Consumer banking and lending to small companies are strong, while the mortgage business continues to grow, says Ray Ferguson, the bank's CEO for Southeast Asia. Foreclosures, he adds, "are not a feature of the market."

Southeast Asia's strength is an encouraging sign that the region is still a player. Though it may have been half-forgotten by many investors since the crisis, its educated workers, natural resources, and—in some countries, at least—first-class infrastructure make it worth paying attention to. ASEAN has a total population of 560 million,
and its combined gross domestic product of $1.3 trillion is greater than India's. Indonesia, Thailand, Malaysia, the Philippines, Vietnam, and Singapore—which account for about 95% of the region's economy—attracted nearly $50 billion in foreign direct investment last year, vs. China's $92 billion.

General Electric (GE), for instance, has committed more than $1 billion to Southeast Asia in the past 18 months. Those investments include expanded aircraft maintenance facilities in Kuala Lumpur and a water-technology research center in Singapore. And in May, GE broke ground on its first project in Vietnam, a $61 million plant in the port city of Haiphong to produce wind turbine generators for export. "We wanted to put the GE footprint into a high-potential country," says Stuart Dean, the company's Southeast Asia president.

**SCUTTLED SUMMIT**

That's not to say the region doesn't pose significant challenges for investors. Red tape and corruption are rampant; Indonesia is ranked 126 out of 163 by Transparency International, behind Nigeria and Nepal. Jakarta's opaque laws have prevented a country rich in gold and copper from attracting a single new foreign mining project in a decade. In Vietnam, traffic moves at a snail's pace along roads that can barely handle motorbikes, let alone the growing number of cars. And in Thailand, tourists and investors alike have been spooked by instability as anti-government demonstrators in recent months have forced the cancellation of an ASEAN summit and closed Bangkok's airport for days.

Those troubles, combined with the global crisis, are weighing on growth. Singapore and Thailand—which depend on exports—are contracting. The Asian Development Bank expects Vietnam to expand 4.5% this year, Indonesia 3.6%, and the Philippines 2.5%—near-recession levels for those countries. And new foreign investment in Malaysia fell 79%, to $931 million, in the first quarter, while in Vietnam investment inflows dropped 71%, to $2.8 billion.

Governments are fighting back by formulating stimulus plans. In Thailand, where the economy could shrink as much as 4%, retail sales have held up thanks to $58 checks mailed to 10 million low-income workers as part of a three-year, $45 billion stimulus package. Chipmaker Intel (INTC) expects stimulus-driven spending on health care and education to boost sales of computers that use its chips. Retail PC sales for the five biggest economies in ASEAN grew 17% year-on-year in the first quarter, more than twice as fast as in China, research firm GFK Asia estimates.

**UP FROM CALL CENTERS**

The region is also growing fast as an outsourcing center. In the Philippine city of Cebu, nestled between emerald hills and luminous coral reefs, the seven-year-old Asiatown IT Park is home to two dozen call centers and software outsourcing shops. "It's not an easy job, but the salary is pretty good," says 29-year-old Leyland Canoy, who earns $470 a month at locally owned eTelecare, where he provides tech support to customers of Internet phone company Vonage (VG).

The Philippine outsourcing industry has been operating for years, but now it has big plans to grab as much as 10% of the global IT outsourcing market. Wipro (WIT), Accenture (ACN), HSBC (HBC), and others have opened scores of new back-office and tech-support centers in the country, helping to build an industry that saw $6 billion in revenue and employed more than 370,000 in 2008. "We are growing like crazy," says Marife Zamora, Philippines chief for Cincinnati-based Convergys (CVG), which hopes nearly to double its Philippines staff, to 20,000, this year. By 2010, industry leaders expect the sector to employ 900,000 and generate sales of $13 billion.
That's an ambitious target, but the country is just starting to move up from call centers. "There's work in finance and accounting, and corporate back offices have yet to be tapped," says Oscar Sañez, CEO of the Business Process Association of the Philippines. Accenture, which employs about 16,000 in the country, is helping clients upgrade IT systems to keep up with financial regulatory changes in the recession-racked U.S. JPMorgan Chase (JPM), S.C. Johnson & Sons, and Siemens (SI) are expanding their back-office work there. And Wipro is doubling its Philippine staff, to 1,550, by October. "The talent is really good," says Sanjeev Bhatia, vice-president for international operations at Wipro BPO. "We are really bullish."

Global corporations still come to Southeast Asia-to find manufacturing alternatives to China. First Solar (FSLR), of Tempe, Ariz., has chosen Kulim, Malaysia, for a $680 million solar panel manufacturing plant. British motorcycle maker Triumph is building a $73 million plant in Thailand. And Volkswagen (VLKAY) this summer is launching a joint venture to produce Touran minivans in Indonesia.

Vietnam, though, is the primary beneficiary of the move to diversify away from China. Its proximity to the mainland and the low tariffs it enjoys in Southeast Asia thanks to ASEAN trade agreements are big pluses, as are its productive labor force and entrepreneurial culture. In April, Samsung Electronics opened a $50 million mobile-phone plant outside Hanoi. Some 700 miles to the south near Ho Chi Minh City, Jabil Circuit (JBL) is building a $100 million circuit board plant in the Saigon Hi-Tech Park. Nearby, across former rice paddies muddled by afternoon rains, workers are readying a $1 billion Intel (INTC) plant that will open next year. "We expect more high-tech companies to follow," says Rick Howarth, general manager of Intel Products Vietnam. "The global crisis may have dampened companies' desire to invest, but they are also being forced to look at new markets for growth."

One of the region's greatest strengths is also a weakness: a growing reliance on exports, especially to China. The mainland's coastal factories use countless parts made in Southeast Asia for goods that are ultimately destined for the U.S. and Europe. When those Chinese exports get slammed, ASEAN economies suffer. "The region is excessively dependent on China, which does assembly, while ASEAN does components," says Charles Adams, a professor at Singapore's Lee Kuan Yew School of Public Policy. "What's needed is more intraregional trade in final goods."

THE CHINA CONNECTION
There are few signs Southeast Asia will wean itself from that dependence anytime soon. Philippine outsourcers work primarily with U.S. customers. Intel plans to export most of its production from Ho Chi Minh City, since Vietnamese will buy just 3 million or so computers this year, while the Intel plant will be able to turn out hundreds of millions of chips annually. And Canon's (CAJ) $100 million laser printer facility outside Hanoi, its largest anywhere, ships its products overseas.

An ASEAN agreement that allows free trade in autos around the region may help reduce the importance of China and the West. Ford Motor (F), for example, ships sport-utility vehicles from Thailand to Vietnam, Indonesia, and the Philippines. The free trade "gives us enough volume," says David N. Alden, president of Ford's operations in Southeast Asia, where auto sales are about the same as in India. "Thailand's market alone could not have made this a business base."

AirAsia, a scrappy budget airline based in Malaysia, shows the potential of the regional market. In 2001, entrepreneur Tony Fernandes took a bankrupt carrier and relaunched it with just two planes flying out of Kuala Lumpur. Thanks to liberalization of air travel in much of the region, Fernandes has ramped up to 81 aircraft and 122 destinations in 16 countries—often smaller cities others had ignored. He expects to carry 24 million
passengers in 2009, up 30% from last year. "We focused on building an ASEAN brand," says Fernandes. "We saw a huge opportunity no one was exploiting."

**BUSINESS EXCHANGE: READ, SAVE, AND ADD CONTENT ON BW'S NEW WEB 2.0 TOPIC NETWORK**

**China's Merchant Class**

Southeast Asia is home to more than half a billion people, but the region's economy is dominated by some 40 families, most of Chinese descent. In *New Asian Emperors*, authors George Haley, Usha Haley, and Chin Tiong Tan highlight the business models and management practices of these family-run conglomerates, drawing lessons for Western multinationals.

To read a sample chapter from the book, go to [http://bx.businessweek.com/emerging-markets/reference/](http://bx.businessweek.com/emerging-markets/reference/)

*Balfour* is Asia Correspondent for BusinessWeek based in Hong Kong.