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NEW REGIONAL EXPORT OPPORTUNITIES
IN THE GROWING GLOBAL ECONOMY

The global economy expanded by 5.5 percent in 2006 and had been projected to grow at annual rates of more than 5 percent both this year and next. However, reverberations from U.S. credit market problems could slow future global growth. China and India had been expected to pick up any economic slack caused by the projected U.S. economic slowdown. However, if U.S. imports decline sufficiently, even their booming economies could be hurt. At present, relatively strong global economic growth coupled with the weaker U.S. dollar have created new export opportunities for regional businesses. This article discusses current business conditions abroad in terms of their potential impact on the demand for regional exports.



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The Robust Global Economy

The global economy is growing faster than it has in many years. The need to build new factories, expand ports and pave roads in developing countries has increased the demand for U.S. capital goods exports. Rising employment and wages abroad are creating lucrative markets for U.S. consumer goods exports. The latest economic growth projections by the International Monetary Fund, made prior to recent U.S. credit market turbulence, indicated that the global economy would continue to grow at a relatively rapid pace. (See Table 1) This implies a favorable outlook for U.S. exports.

A favorable export outlook is particularly important for New York State businesses because exports play a significant role in the state's economy. The state exported goods and services valued at almost \$57.4 billion in 2006. Its biggest export customers were Canada, Israel and the United Kingdom. Japan, Hong Kong and China were also among the state's top ten export destinations. (See Table 2)

An Overview of Asian Business Conditions

Asia's economies, led by China and India, have been growing vigorously. Moreover, many of them are shifting from export-based economic growth to growth fueled by domestic consumption. This transformation, which is good news for U.S. exporters, poses significant risks for many Asian countries because their

which made China America's second largest trading partner after Canada. America's 2006 trade deficit with China, almost \$233 billion, accounted for more than one-quarter of the total U.S. trade deficit in that year. Chinese imports currently account for 80 percent of the U.S. toy market, half the U.S. footwear market and almost half the U.S. market for consumer electronics. China's massive trade surplus has exacerbated trade tensions with the

United States, which is pressuring China to allow its currency, the yuan, to appreciate faster. It is estimated that the dollar is overvalued relative to the yuan by as much as 40 percent. This keeps the price of Chinese exports to the U.S. artificially low and perpetuates

the current trade imbalance between the two countries. China is expected to have \$1.389 trillion in foreign exchange reserves by the end of this year, much of it in dollar-denominated assets.

China's economy grew by more than 11 percent last year and is expected to do so again this year. China has taken measures to cool its economy amid con-

Table 1

Economic Growth Projections for Selected Countries and Zones

Country/Zone	2006 Actual	2007 Projected	2008 Projected
China	11.1%	11.2%	10.5%
India	9.7	9.0	8.4
Euro Zone	2.8	2.6	2.5
Japan	2.2	2.6	2.0
U.S.	3.3	2.0	2.8
World	5.5	5.2	5.2

Source: International Monetary Fund

fledgling financial systems may be unable to withstand significant consumer loan defaults.

China. China currently has the world's fourth largest economy and it may soon surpass Germany as the world's third largest. U.S. trade with China totaled \$343 billion in 2006,

cerns about accelerating inflation and emerging asset bubbles. Surging food prices have pushed China's consumer inflation rate to its highest level in a decade. China is also attempting to rebalance its economy by downplaying exports and increasing consumer demand. By strengthening its social safety net and spending more on health care and social programs, China hopes to give its population the confidence to spend more freely. It is also encouraging its companies to focus more on the domestic market and less on exports. This strategy appears to be working. Chinese retail sales increased by more than 16 percent in July, the fastest growth rate in three years. Although China also recorded its second largest monthly trade surplus in July, recent tax changes are expected to slow future export growth. If China is successful in encouraging consumer spending, it could become a lucrative market for U.S.-produced consumer goods, financial and business services.

Japan. Japan is just emerging from a decade-long deflationary cycle. Its economy grew by 2.2 percent in 2006 and could expand by 2.6 percent this year. Japan's exports are benefiting from its weak currency. The yen has been falling against other major currencies because Japan's target interest rate is only 0.50 percent. The export boom has triggered increased hiring, which has driven Japan's unemployment

rate below 4 percent for the first time in nine years. The Bank of Japan had hoped to raise its target interest rate to 0.75 percent in August. However, turmoil in global stock and credit markets coupled with its slowing economy has put future interest rate increases on hold. Japan's GDP grew at an annualized rate of only 0.5 percent in the second quarter of this year, following growth of 5.4 percent and 3.2 percent respectively in the previous two calendar quarters. Japan may have difficulty transitioning to a consumer-based economy because of its shrinking workforce and aging population. With more of its population slated to retire, Japan may be forced to raise its consumption tax, currently at 5 percent, to meet future social security payments. This would tend to inhibit consumer spending.

India. India's economy grew by 9.7 percent last year. It is expected to grow by at least 9.0 percent this year. However, the boom in high-technology services, which is fueling current growth, is based on a shaky foundation. India lacks a modern infrastructure and its existing infrastructure is crumbling under the stress of rapid growth. Economic losses from congestion and poor roads are estimated at as much as \$6 billion annually. Since India cannot expand its manufacturing base without major infrastructure improvements, it plans to significantly increase its spending for highways,

bridges, airports, power plants and water treatment facilities. This should result in increased demand for U.S. exports of professional and technical services and capital goods. India's economic boom has pushed its inflation rate to almost 7 percent, a two-year high. Real estate prices in some areas have doubled over the past year. Inflation is a particularly onerous problem for India because a majority of its 1.1 billion people earn less than \$3 a day. In this situation, even slight price increases can have devastating economic consequences.

South Korea. South Korea, the world's tenth largest economy, is America's seventh largest trading partner. Its economy, driven by its booming shipbuilding and service industries, is projected to grow by about 4.5 percent this year. Rapid economic growth and the wealth it has generated have resulted in real estate and stock market bubbles. In response, the Bank of Korea has started raising interest rates to cool the economy. America recently signed a free trade pact with South Korea. The agreement would eliminate tariffs on 95% of consumer and industrial products on both sides within three years. If approved by Congress, Korean carmakers and textile firms would gain better access to U.S. consumer markets and U.S. farmers, banks, insurance companies, movie and telecommunications companies would get a foothold in the thriving north-

Table 2

New York State's Principal Export Customers, 2006

Country	Rank	Dollar Value (\$000)	% Of Total Exports
Canada	1	\$12,225,961	21.3
Israel	2	4,560,686	7.9
United Kingdom	3	4,197,748	7.3
Switzerland	4	3,640,629	6.3
Japan	5	2,846,714	5.0
Hong Kong	6	2,607,905	4.5
Germany	7	2,446,174	4.3
Mexico	8	2,430,715	4.2
Belgium	9	2,265,794	3.9
China	10	2,179,384	3.8
Total Exports		57,369,299	100.0

Source: TradeStats Express; <http://tse.export.gov>

east Asian market. U.S. trade with South Korea, valued at about \$79 billion annually, could increase to \$99 billion annually as a result of the new trade agreement.

An Overview of European Business Conditions

The Euro Zone. Thirteen European countries, encompassing 317 million people, share a common currency, the euro. The region is experiencing renewed economic growth following an extended period of economic stagnation. Labor markets have tightened, wages are increasing and consumer spending is rising. The euro-zone unemployment rate fell to only 6.9 percent in June, its lowest level since data collection started in 1990. The euro-zone economy grew by 2.8 percent last year and is expected to expand by 2.6 percent this year. However, inflation is accelerating due to higher food and energy prices. The European Central Bank, which sets monetary policy for euro-zone countries, raised its key interest rate to 4 percent in June and was expected to raise interest rates at least once more this year. However, credit market turbulence could delay future rate increases. Exposure to U.S. subprime credit woes on the part of some euro-zone banks recently prompted the European Central Bank to pump massive amounts of liquidity into the euro-zone economy.

Higher interest rates have also led to friction between individual euro-zone countries. Although Germany is doing relatively well, France's economy has been flat and Italy's has slowed. All three countries experienced slower economic growth in the second quarter of this year. Germany has restructured its economy so that it is more productive and better able to withstand the economic stresses created by higher interest rates and a stronger euro. However, France and Southern Europe have yet to implement the labor market, health care and pension reforms that would allow them to remain competitive in a higher interest rate environment. France's new president proposes to slash the payroll taxes that fund its social welfare system in order to create more jobs. Italy has similar plans. This should even-

tually reduce interest rate tensions within the euro zone.

The United Kingdom. The United Kingdom, which has remained outside the euro zone, is enjoying robust economic growth due to increased consumer spending. However, price inflation in the housing market and rising levels of consumer debt prompted the Bank of England to begin raising interest rates. Recent floods could exacerbate inflation as households replace damaged goods and washed out crops lead to higher food prices. The Bank of England's key-lending rate, currently 5.75 percent, had been expected to rise to 6 percent by year-end. However, the potential fallout from U.S. credit market problems coupled with a recent drop in inflation may postpone future rate increases. The UK inflation rate fell from 2.4 percent to 1.9 percent between June and July and business lending, which had been growing at an unsustainable rate of almost 20 percent annually, is expected to slow.

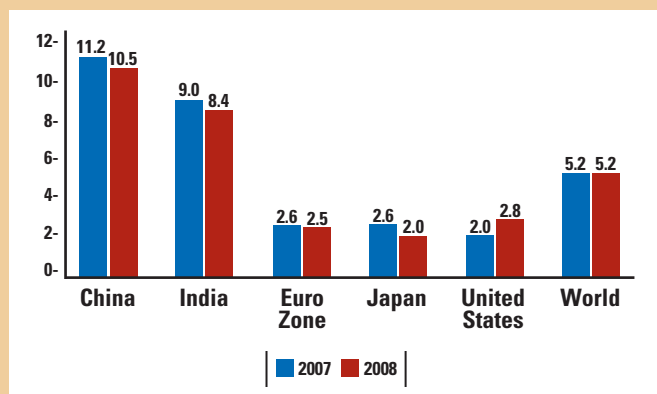
The Nordic Region. The economies of Norway, Sweden, Denmark and Finland are considerably stronger than those in the euro zone. Labor market reforms have pushed unemployment to

record lows in Norway, Denmark and Finland. Double-digit increases in consumer spending in Sweden have produced the country's fastest economic growth since the 1970s. Norway's oil-driven economy is benefiting from record crude oil prices. Finland's economy is thriving due to increased trade with Eastern Europe. However, rising wages throughout the region are generating concerns about inflation.

Russia, Central and Eastern Europe. Russia has enjoyed seven years of robust economic growth, fueled by its strong energy sector. The weak ruble following Russia's 1998 financial default made its exports more affordable and supported export growth. The windfall created by rising crude oil prices stimulated consumer demand, which in turn led to a wave of business capital spending. Business capital investment rose by more than 13 percent last year. Business spending has been broadly based by industry, setting the stage for future economic growth even if crude oil prices were to decline.

Eastern Europe has become a haven for low-cost manufacturing and a magnet for foreign investment. Last year, Slovakia's

Projected GDP Growth, 2007, 2008 Selected Countries and Zones (Percents)



economy grew by more than 8 percent and Poland's economy, the largest in the region, expanded by almost 6 percent. Eastern Europe's average wages are 16 to 34 percent of those in Western Europe. An exodus of skilled workers to Western Europe in search of higher wages is creating workforce shortages and pushing up wages. This is undercutting the region's competitive advantage as a low-cost producer. However, existing wage disparities between Eastern and Western Europe are likely to persist for some time. Russia, Central and Eastern Europe have also become an important market for euro-zone exports, thereby offsetting any decline in euro-zone exports to the U.S. This is helping to rebalance global economic demand and has reduced the world's dependence on U.S. consumers.

The Western Hemisphere Economy

Canada. Canada remains America's largest trading partner. Historically, if the U.S. economy sneezed, the Canadian economy caught cold. Today, Canada's economy has enough momentum to survive a moderate U.S. downturn. Its economy is expected to grow by 2.4 percent this year. However, a tight labor market and strong housing market are generating inflation and the Bank of Canada is likely to raise its overnight lending rate at some point this year.

Mexico. Mexico's economy is expected to grow by 3.4 percent this year. However, the downside risks to its economy have increased due to its reliance on exports to the United States. Trade between the U.S. and Mexico more than tripled since the North

American Free Trade Agreement (NAFTA) was implemented in 1994. There is concern that slower U.S. growth will hurt Mexico's auto, textile and electrical equipment industries. Price pressures within the Mexican economy seem to be contained and Mexico's inflation rate could decline to about 3 percent by the end of 2008. Mexico's central bank appears to be maintaining the status quo in terms of interest rates. Its reference interest rate was 7.25 percent as of June.

Latin America. Latin America's economies are benefiting from higher global prices for various commodities, including oil, grains, coal and copper. Regional economic growth could range between 4.0 and 4.5 percent this year, barring a significant decline in exports to the United States. Economic growth in Brazil is projected at 4.4 percent this year. Brazil's high real interest rates make it a haven for high-yield investors.

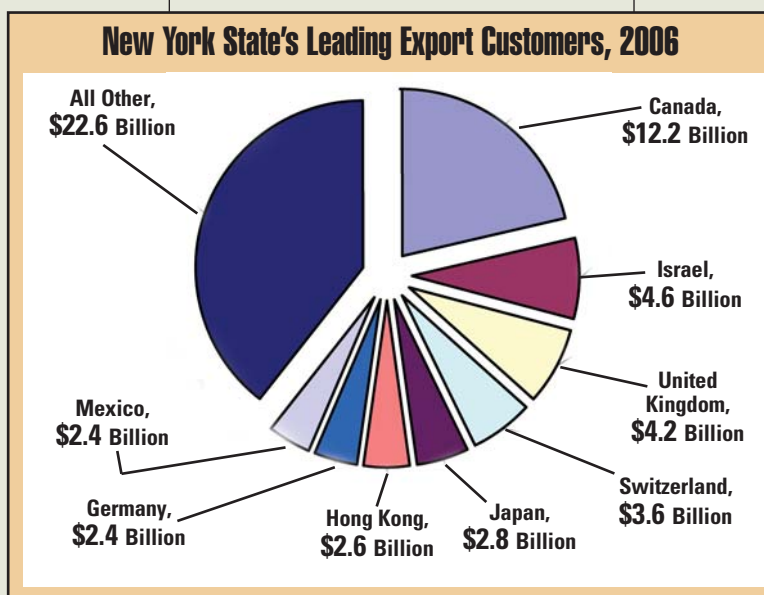
year. Argentina has posted economic growth exceeding 8.5 percent for four straight years. The country's economic revival is being driven by booming agricultural exports. Latin America's economic growth has been dependent on high prices for its commodity exports. Any downturn in global commodity prices could seriously hurt the region's economies.

The Prospects for Global Economic Growth

Although the prospects for global economic growth remain relatively bright, turmoil in U.S. credit markets have added an element of uncertainty to the global economic outlook. At first, the fallout from the U.S. subprime mortgage crisis appeared to be contained to a relatively narrow segment of the U.S. mortgage market. It has since spread to other sectors of the credit market, prompting the U.S.

Federal Reserve to lower its discount rate by 50 basis points to ensure adequate liquidity within the U.S. banking system. It also spread to overseas financial institutions that bought U.S. securities backed by subprime mortgage loans. This reaffirmed how quickly financial problems can spread in a globally linked financial system. Because bonds backed by subprime loans are derivative financial instruments, part of an array of arcane financial instruments developed in recent years, it is difficult to ascertain who is at risk and where

the risk exists. This uncertainty may cause lenders to pull back, leading to higher interest rates and slower global economic growth. To date, however, the world's central banks have been able to calm credit market jitters and keep the loan spigot open.



Brazil's economy is on a stable footing due to booming exports, moderate inflation and falling unemployment. Chile's export-dependent economy is being helped by increased copper exports. Its GDP, which grew by 4 percent in 2006, is expected to grow by 5.8 percent this