

HOW TO STAY COMPETITIVE

Export and currency woes have given the region a wake-up call, but the smart money has long been gearing up for competition

By Ricardo Saludo and Sangwon Suh

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IT SEEMED A SIMPLE BUSINESS DECISION. Last year Wing Tai Holdings, a pioneer clothing manufacturer in Singapore, closed its plants in the Lion City. "They decided -- correctly -- that real estate was more profitable," says an industry analyst. "Labor costs and the strong Singapore dollar were factors, but it was more a case of property being more attractive." In 1992, real estate became the group's top grosser; last year, it brought in \$312 million, and fashion a mere \$22 million. Founded in 1963 as Wing Tai Garment Manufactory (S) Pte. Ltd., the company now builds serviced apartments in Singapore, Malaysia, Indonesia and China. It still exports apparel from affiliates in Hong Kong and Malaysia. But in Singapore, its business is shelter, not clothing.

Now, replicate Wing Tai's move out of manufacturing across the region, and you'll get an idea of the challenge facing East Asia's tiger economies. Rising production costs, cheap foreign competition and the lure of fast-growing domestic markets are giving pause to exporters, once the main engines of Asian growth. One worrying result: while the region's newly industrialized countries continue to expand, gobbling up imports, an export slowdown is saddling key NICs with burgeoning deficits in their trade in goods and services. And that yawning gap in the current account is ammunition for currency speculators in their shifting battle against central bankers defending Asia's money.

Take a look at the charts on the opposite page. They show the current account deficits of four countries whose currencies have recently faced attack. In each economy, the payments shortfall shot up in recent years and, despite efforts to contain it, still remains above 3% of gross domestic product. That means as far as overall trade is concerned, more local currency is being sold for foreign exchange than the other way around, an imbalance that usually weakens the domestic denomination. This year only the Philippines is expected to possibly show a surplus, although that prospect didn't seem to sway the currency bears who stalked the peso last week.

Asian economic planners have long maintained that current account deficits are normal in economies investing heavily in industry and infrastructure. The imbalance is supposedly well covered by long-term loans and investments from abroad, and it should fall when the new factories begin exporting and better facilities improve economic efficiency. But no one counted on Paul Krugman and his assertion that Asia's world-beating, trade-led boom won't go on forever. Last year's export slowdown seemed to confirm the MIT professor's prognosis. It did not help that countries like Thailand lavished much capital spending on rows of condominiums and shopping malls, which tend to boost consumer spending but not exports.

Economic managers have two options to prevent a blowout in the current account: reduce imports or increase exports. Asia has been working on both. In March, Malaysia's imports declined for the fifth month in a row, as the economy decelerated faster than expected. But curtailing growth to rein in trade shortfalls is hardly a recipe for economic dynamism. Moreover, the need for new planes, trains, phones lines, power plants and other infrastructure will keep capital

imports high. So the mega-question is: Can exporters continue to generate the earnings that fuel growth and contain deficits?

To be sure, the export picture is hardly a hopeless one. The Japanese, who have seen every dollar of export revenue shrink in value from \$250 in 1986 to as low as \$80 a decade later, have faced the competitiveness challenge and largely triumphed. Their strategy -- "Economize, mechanize, merchandise" -- is one that can be and is being adopted by Asian NICs. By cutting costs, automating operations and developing products for new or higher-margin markets, exporters like those featured in these pages are showing that the export-powered boom need not be a thing of the past.

The global economy is helping out. Last year's export slump is now looking more cyclical than systemic. Nicholas Brooks, senior economist for Peregrine Securities in Singapore, blames weaker demand from industrial nations. "In 1996, import growth in the most advanced economies collapsed," he explains. "In the 1993-1995 period, most saw a surge in inventories. In 1996, there was a de-stocking of inventories, which led to lower imports."

This year, global demand is surging due to continued U.S. growth and recovery in Europe and Japan. But production capacity, especially in America, is getting used up fast. Kenneth Courtis, senior economist for Deutsche Bank Group Asia Pacific, says the U.S. is now operating near the optimum 85% of capacity, and any growth in excess of 2.5% will have to be supplied by imports. A recent survey of American economists came up with a consensus GDP forecast of 2.6% for 1997.

"At this point, the export recovery in Asia is still fairly moderate," says Brooks, "but I expect exports to start picking up faster toward end of this year and early next." Rajeev Malik, a senior economist at Jardine Fleming International Securities in Singapore, sees such a scenario for Malaysia. The electronics sector, one of the pillars of the country's exports, suffered gravely in last year's slowdown, with layoffs and plant shutdowns virtually every month. But with the microchip market showing signs of recovery, Malik says "export growth in Malaysia will pick up in the next two months."

Still, the turns of business cycles cannot explain all the pains of Asian exporters. Prosperity has in fact brought higher costs to the enterprises that spearheaded growth. Lower-cost producers are emerging from less developed nations seeking to replicate the NICs' climb from farm- and resource-based economies to manufacturing-based ones. For Michael Taylor of W.I. Carr Securities, the cheap rival is easy to trace: "In China, we can find quite severe factory-gate price deflation in the face of major overcapacity and a very flat market." Translation: With so many factories and limited consumer buying power, China is undercutting exporters elsewhere.

Today, such pressure is weighing most heavily on Thailand. As in other NICs, textile-making was a mainstay of Thai industry. Survival has meant tough decisions. Leading manufacturer Thai American Textiles recently laid off 835 workers and is planning a more efficient, machine-based operation. Chavalit Nimla-or, head of the Thai Garment Manufacturers' Association, maintains that there is still life in the sector. Italy remains a top clothing exporter despite high wages; he attributes its success to design and promotion.

"We have to improve our marketing strategy to increase awareness of Thai goods," Chavalit argues. But for Charl Kengchon, head of banking and money at Thai Farmers Research Center, "some factories may have to close." Indeed, in recent years, the country's export scene has gradually shifted from T-shirts and sport shoes to computers and high-tech electronics. Exports of computers and computer parts increased 44.2% last year, making up 12.8% of the country's exports.

Peter Brimble heads the Brooker Group, a Bangkok-based business consultancy. He says "the future of Thai exports depends on these more sophisticated products." He cites exports that did especially poorly in the past year: garments and textiles, footwear, plastic products, canned fruit and seafood, and gems and jewelry. "Thailand has two alternatives," Brimble says. "Phase them out or move into higher, value-added niche markets where cheap labor is not an important advantage."

Achieving such a transition has been the region's main challenge, involving the reorientation of workers, the restructuring of industries and the development of new markets. Trade liberalization, although mind-numbingly slow, will accelerate this trend, as uncompetitive firms and industries eventually find that they have no tariffs and other trade barriers to hide behind. The ASEAN Free Trade Area will prod members to specialize. Once Vietnam, Cambodia, Laos and Myanmar join AFTA, they will pressure the Philippines and Indonesia to move upscale faster.

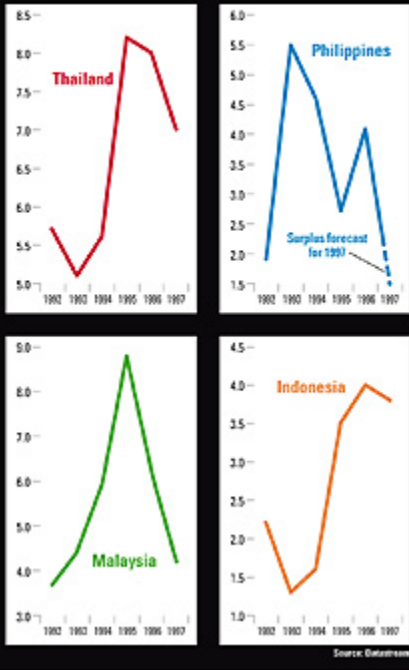
The smart money, of course, takes action before costs and competition get too big to ignore. Over the past decade, Jakarta-based textile giant Texmaco has been pursuing vertical integration. Last month it paid \$50 million for British clothing firm S.R. Gent, part of a process of tie-ups in Europe and America that will give it greater access to lucrative markets. At the other end of the apparel business, Texmaco has opened a \$645-million purified terephthalic-acid plant 35 km east of the capital, to produce raw materials for its polyester operations. Its engineering division will earn \$500 million from sales of textile machines in 1998 and 1999, says group president director Marimutu Sinivasan. Texmaco is also planning a steel mill and venturing into motor vehicles and components.

Barito Pacific is another Indonesian company that isn't letting the advantages of cheap labor and resources lull it into complacency. The world's largest timber company, with 5 million hectares of forest concessions -- larger than Switzerland -- is enjoying the highest demand for its products ever. But publicly listed Barito isn't content to simply turn trees into rupiah with the least effort and thought. "We're concentrating on efficiencies," says finance director Susana Sutanto. That means buying machinery that saw logs faster and with less wastage.

The company is also investing in tree farms, to assure supply within easy reach starting 1999. And to squeeze more value and profit from each tree, Barito has been undertaking ventures in wood processing, including a \$1.2-billion pulp and paper plant and factories for doors, flooring, laminated plywood, knocked-down furniture and moldings. While the past year's export and currency trials may be a wake-up call for much of Asia, the region's top exporters have never stopped working to stay ahead of the competition.

-- Reported by Assif Shameen, Julian Gearing / Bangkok, Keith Loveard / Jakarta, Steven K.C. Poh / Kuala Lumpur and Santha Oorjitham / Singapore

NATIONS IN THE RED Current Account Deficits As a percentage of GDP



Source:Datastream