

VIEWPOINT

Election Fever and the US Economy

Here we are already well into autumn. Though temperatures are falling, across the Pacific in the United States the fever pitch of the presidential campaign is intensifying, with less than a month to election day. The round of debates between the two candidates has started, and the race is now in the final stretch. People around the world are watching the contest closely, interested to see if President George W. Bush will get another term or if Senator John Kerry from Massachusetts will win back the White House for the Democrats.

Every day I check a website that tracks the state-by-state outlook for the electoral vote (<http://www.electoral-vote.com>). The states where Bush leads are colored red, and those where Kerry leads are blue, with lighter shades showing a smaller margin. It is interesting to watch the changing pattern of colors as the campaign progresses.

The outcome of the quadrennial presidential race has a major impact on US government policy, with direct repercussions on Americans' everyday lives. Depending on whether it is the Republicans or the Democrats who win, there are people who will lose their jobs and others who will get jobs. It is only natural that public interest in the election runs high.

Following the end of the Cold

War, the focus in electoral campaigns shifted away from national security toward the economy and other issues relating to everyday life. But this is the first presidential election since the 9/11 terrorist attacks in 2001, and with the situation in Iraq remaining unsettled and the war on terror continuing, it is hard to tell whether the economy or national security will be a bigger factor in voters' minds as they make their choices. According to the results of a Harris Poll this September, when asked "What do you think are the two most important issues for the government to address?" 30% of respondents cited the economy (compared with 12% in 1994), followed by the war, 24% (0% in 1994), health care, 21% (45%), terrorism, 14% (0%), and employment/jobs, 12% (14%). These results clearly show the impact of 9/11.

Taking a broad look at the global economy, the biggest changes over the past few years have been the rise of East Asia and particularly China's rapid emergence. Here in Japan, meanwhile, the economy continues to depend heavily on external demand to power its growth. And the United States accounts for a large share of this demand. The pattern remains one in which final demand in the US market, supported by

lively consumer spending, is a crucial factor on which the Japanese economy relies. This pattern also ties in with the twin deficits in the US balance of payments and government budget, whose immense size poses a serious risk for the global economy.

The United States, with 291 million people, has just 4.6% of the world's total population, but its gross domestic product, at \$11 trillion, accounts for 29.9% of the world total, its annual trade volume, at about \$2 trillion, for 13.3%, and the market capitalization of its stock exchanges (current market value of traded stocks), at \$14 trillion as of the end of 2003, for 45.7%. These and other statistics show that its eco-

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conomic weight is disproportionately large in comparison with its population size. Also, according to the October 13 issue of *Newsweek's* Japan edition, 43 of the world's top 100 companies ranked by profits were American (incidentally, 8 were Japanese). America exerts a tremendous draw on people, money, and goods from around the world, and its influence on the global economy is huge. Also, this year's Nobel prizes were just announced, and the bulk of the winners in scientific categories like physiology and medicine, physics, and chemistry were Americans; the United States holds

an overwhelming share of all the prizes awarded in the past as well. Over the medium to long term, the United States seems likely to maintain its dominant position in the sciences, and based on this, US industry should be able to hold on to its global lead.

The US economy is continuing to expand despite concerns over rising oil prices, but the failure of the recovery to generate many new jobs has become a major issue. As of August the unemployment rate stood at 5.4%. Since the end of World War II, the incumbent has won in presidential elections when joblessness

was under 6%. Another interesting indicator is that over the past 100 years, whenever the Dow Jones industrial average has gained more than 3.3% in the October before a presidential election, the incumbent has won, and whenever it has fallen more than 0.5%, the challenger has been victorious.

Recently the rumor mills have been suggesting that Osama bin Laden will soon be captured. It will be interesting to see if this or some other "October surprise" will occur and to find out how the electoral map is colored on November 2.

■ *Akio Okawara, October 8, 2004*

REPORT

Corruption in China: Top Issue for Hu Jintao's Administration

The 16th Central Committee of the Communist Party of China met in Beijing for its fourth plenum from September 16 to 19. At this session Jiang Zemin resigned from his final leadership post, the chairmanship of the CPC's Central Military Commission, and Hu Jintao was selected as his successor. This marked the completion of the transition of power from Jiang to Hu, who now heads the party as general secretary, the Chinese state as president, and the military as chairman of the CMC.

The biggest issue for Hu's administration is to eradicate pervasive corruption so as to achieve enhancement of the party's governance capability, the objective that was the main theme of the fourth plenum. This month we look at corruption in China and the campaign to eradicate it.

A tradition of living off the people

At the second session of the 10th National People's Congress in Beijing this past March, Procurator General Jia Chunwang announced figures for cases of corruption and other job-related crimes by Chinese civil servants in 2003. According to Jia, there were 39,562 officially investigated cases, involving 43,490 suspects; of these suspects 2,728 were at or above the level of county or section chief, including 167 at the prefectural-chief level and 4 at the provincial-chief or ministerial level. Other statistics he reported included 123 cases involving 10 million yuan (about \$1.2 million) or more (see the table).

China has a long tradition of selecting senior civil servants through a system of rigorous examinations. Those who passed were eligible to

become administrators of provincial districts, assisted by lower-ranking bureaucrats. The administrators wielded total power over the districts for which they were responsible, but they received very little pay from the central imperial government. Early in the twentieth century, Sun Yatsen noted that the governor of the region encompassing Guangdong and Guangxi, with an area and population comparable to those of Great Britain, received an annual salary of a mere 60 pounds sterling. Moreover, the lower-ranking bureaucrats received no salary at all and made their living by collecting fees from the common people. Under this setup, the administrators enriched themselves by taking money from the bureaucrats working for them, and these lower-ranking bureaucrats in turn enriched themselves by extracting fees from the public, using

Job-Related Crimes of Chinese Civil Servants

	Cases officially investigated	Major cases involving corruption, bribery, or embezzlement of public funds	Suspects at or above county- or section-chief level
1998	35,084	1,773 (0.5 million yuan or above)	1,820
1999	38,382	—	—
2000	45,113	1,335 (1 million yuan or above)	2,680
2001	45,266	1,319 (1 million yuan or above)	2,670
2002	43,258	—	—
2003	39,562	123 (10 million yuan or above)	2,728

Source: Annual reports on the work of the Supreme People's Procuratorate submitted to the National People's Congress by the procurator general.

the authority of the administrator as their shield.

This traditional set of arrangements was thought to have been swept away with the establishment of the People's Republic of China in 1949. In fact, however, something like the old pattern persisted. Civil servants in the PRC enjoy various privileges and benefits, but their salaries are extremely low, and with the shift to a market economy, the gap between their pay levels and those of employees at private-sector enterprises has grown steadily wider. Under these conditions, it is hardly surprising that low-ranking bureaucrats seeking to live a life of ease are tempted to seek bribes and the like, and that those at a more senior level are liable to abuse their powers for personal gain.

Senior officials fall from their horses

Looking at Chinese websites about current events, one often sees the four-character phrase *gaoguan luoma*. Literally translated, this means "senior official falls from horse." It is an apt expression, referring to the fall from power of a prominent person who had been on the fast track toward the top. In almost every case, the cause of the fall is corruption. The first official of ministerial level to be arrested in such a case is said to have been Li Xiaoshi, who was vice-minister of the State Science and Technology

Commission. In 1994 he was sentenced to 20 years in prison.

Major cases of ministerial-level officials convicted of corruption over the past five years include the following: Cheng Kejie, former vice-chairman, Standing Committee of the National People's Congress, sentenced to death for taking 41.1 million yuan in bribes (Cheng is the highest-ranking official to receive a death sentence); Tian Fengshan, former minister of land and resources, currently awaiting trial on charges of corruption amounting to just over 5 million yuan; Wang Xuebing, former president of the China Construction Bank, sentenced to 12 years in prison on charges of bribe taking and embezzlement amounting to 1.15 million yuan; and Li Jiating, former governor of Yunnan Province, sentenced to death for accepting over 18 million yuan in bribes.

It has become more common to see reports of high-level officials being prosecuted for corruption, but it is hard to bring cases to justice when the suspect is a protégé of a senior leader. Charges involving high-ranking bureaucrats are handled by the Supreme People's Procuratorate, and this makes it relatively easy for powerful figures in the central government to intervene.

On August 8 Huang Jingao, the secretary of the CPC committee in Lianjiang County, Fujian Province, posted an open letter on the website of *Renmin Ribao* (People's Daily)

calling for an examination of corruption in a public works project in which his predecessor was involved. Huang also declared that he had had to wear a bulletproof vest for the last six years in fear of revenge for his anticorruption activities in his previous post as head of the finance committee in the city of Fuzhou. This public call of distress from an incumbent party official created great waves within China, and both the central and provincial party committees immediately initiated investigations. But the affair was soon closed with the finding that Huang's claims were the result of psychological stress and had no basis in fact, and he was ordered to undergo ideological reeducation.

This incident is reminiscent of a case that occurred in March 2003, when Li Changping, party secretary for the township of Qipan in Hubei Province, wrote a letter to Premier Zhu Rongji describing the plight of rural villagers plagued with corruption. Fortunately the letter actually reached the hands of Premier Zhu, at whose instructions a top-secret team thoroughly investigated the situation in Li's township. But despite the support he received from the central authorities, Li came under heavy pressure from those around him and finally resigned from his position, leaving Qipan to revert to its former condition.

Since 2000 China has stepped up its official campaign against corruption. The Chinese public is disgusted with the prevalence of this sort of misbehavior among officialdom. It is to be hoped that Hu Jintao's administration will step up the anticorruption drive and achieve results to meet popular expectations.

■ *Yutaka Kitamura, October 5, 2004*

INTERNATIONAL AFFAIRS

This section takes a look at major topics on the international scene, offering an outline of developments together with highlights of media commentary and reports from research institutes.

Hu Jintao takes full control in China

Hu Jintao (61) has replaced Jiang Zemin (78) as chairman of the Central Military Commission of the Communist Party of China. Jiang's resignation and Hu's election were announced at the end of the fourth plenum of the CPC's 16th Central Committee on September 19. Hu succeeded Jiang as general secretary of the CPC in November 2002 and as president of China in March 2003, but Jiang had held on to the top military post. Now that he has yielded it, the official transfer of power is complete.

This is said to be the first time since the People's Republic of China was founded in 1949 that a leadership transition has proceeded without turmoil. But some question whether Jiang, who held power for 15 years, has truly let go. One British think tank has suggested it may be premature to say that the Jiang era has ended, citing three possibilities: (1) Jiang will indeed rapidly lose any remaining political power, though he will be treated with respect; Hu and the other younger leaders, including Premier Wen Jiabao, will have a clear advantage and can hope to lead China until at least 2012. (2) Though Jiang has ceded his institutional power base, he will continue to exercise some power indirectly through his protégés. However, given his age, his influence will wane rapidly. (3) Jiang

has made a deal under which he will continue to be consulted on major issues, such as Taiwan and foreign policy, and he will continue to wield influence over the Hu administration.

The *New York Times* took the development at face value, declaring, "The transition is a significant victory for Mr. Hu" (September 20). The *Times* observed, "Jiang's retirement suggests that the party now operates more according to the consensus of its elite members than the whims of its most senior leader." It also noted, "Jiang did not appear to have extracted any special concessions as the price of his retirement. Notably, he failed to arrange for [his protégé] Vice President Zeng Qinghong to be elevated to the Central Military Commission."

Another British think tank has suggested that the failure of Zeng to get a seat on the CMC is a development with potentially significant implications, observing that it had been widely expected that this would be a trade-off for Jiang's resignation. But it also notes that Zeng continues to be responsible for some important areas, such as the handling of Hong Kong affairs, indicating that the development may not be a serious blow to him.

The new leadership team headed by Hu confronts a number of challenging tasks. The administration must deal with some serious domestic problems that emerged under the growth policies pursued in the Jiang era, including the gap in economic development and personal incomes between the coastal regions and the interior, along with environmental issues. It must also tackle matters involving China's position in the international community, such as trade

liberalization and the hosting of the Beijing Olympics in 2008 and of the 2010 World Expo in Shanghai. Hu and his colleagues will be the object of growing attention as they take on these urgent but difficult jobs.

Curtains for Indonesia's Megawati

On October 4 Indonesia's election commission published the official results of the September 20 runoff election for president, announcing that challenger Susilo Bambang Yudhoyono (55) won by over 20 percentage points with a 60.6% share of the vote, against 39.4% for incumbent Megawati Sukarnoputri (57). This means that Megawati will be leaving office after just three years. A British think tank has attributed Yudhoyono's victory to his reformist appeal and to Megawati's failures in economic policy and in fighting terrorism and corruption.

In a report that appeared on its website, CNN observed, "While both contenders were nearly identical on many issues, the upstart Yudhoyono put security at the top of his campaign agenda after three major attacks in the nation in two years. Apart from security, analysts have said Yudhoyono's biggest draw is the electorate's dissatisfaction with Megawati's performance over the last three years. The former military general is seen as a strong, decisive and capable leader."

In the national legislature, however, Megawati's camp (the National Coalition made up of her Indonesian Democratic Party of Struggle, Golkar, and other parties) holds about 60% of the seats and Yudhoyono's supporters only about 20%. In order for the new president to push ahead

forcefully with reforms on the economic and security fronts as the public expects, his administration must first of all firm up its legislative support base.

Yudhoyono canceled his planned victory announcement at the last minute because President Megawati had not yet acknowledged her defeat. According to a spokesman, he decided to wait in the interests of national reconciliation. A story on the BBC's website noted, "It was not clear why Mrs Megawati was refusing to concede defeat, or whether she would do so. Some members of her team have speculated about challenging the result, though the scale of her defeat suggests any challenge

is unlikely to get far." In the end, her camp did not submit a challenge to the constitutional court by the deadline of October 7, and so the results became final.

Indonesia is the world's fourth most populous country, third most populous democracy, and biggest Muslim country; it has the largest economy among the countries of Southeast Asia, and it is the only one of them that belongs to the Organization of Petroleum Exporting Countries. So it has major roles to play in economic and security affairs and the supply of energy. The rest of the world is hoping that democracy will take firm root in this country and that it will achieve stability and growth

both politically and economically.

The reason for Yudhoyono's victory can be summed up as "big hopes for strong leadership." Observers will be closely watching his performance between now and his inauguration, scheduled for October 20, as he names his cabinet and announces plans for his first 100 days in office.

■ *Takaya Mitamura, October 8, 2004*

INSIDE WASHINGTON

The First Presidential Debate

The first of three televised debates between the major candidates for the US presidency was held September 30, beginning at 9:00 P.M. Eastern Standard Time. Before the debate President George W. Bush had pulled ahead of his challenger, Democratic Senator John Kerry, in the polls, so the big question was how Kerry would perform. Being a "policy wonk," Kerry has a tendency to long speeches and was considered to be at a disadvantage in the debate, where the time allowed to answer questions would be limited. On the night, however, Bush's scowls and hesitations drew more attention. In most polls conducted right after the debate, respondents judged Kerry's performance superior.

Media discussion following the debate focused on the two candidates' style. Bush's frowns and ver-

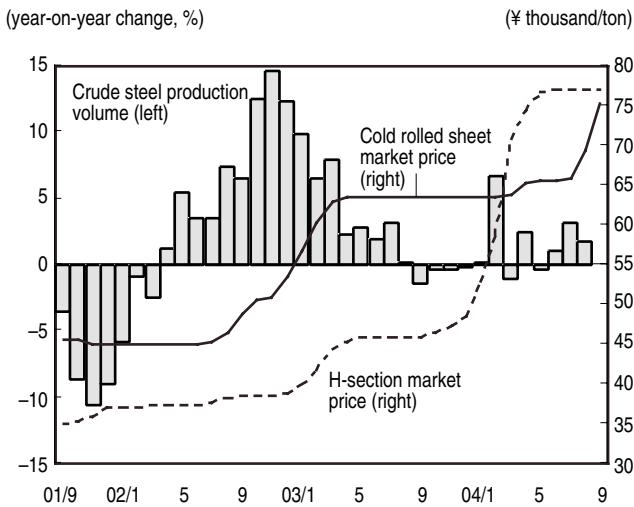
bal fumbling were televised over and over. This TV technique of emphasizing idiosyncrasies had been used in coverage of past presidential primaries and campaigns, molding voters' image of the candidates. In 1960, when the first televised debates were held, John F. Kennedy, who had prepared meticulously, came across as youthful and vigorous, while his opponent, Richard Nixon, looked tired and colorless. Those debates played a crucial part in Kennedy's victory. And in the debates held during the 2000 presidential race, Al Gore's sighs and exaggerated gestures made him seem arrogant, an image that dogged him for the rest of his campaign. TV's dominance of the media today is probably why image—expressions, gestures, and so on—makes a more lasting impression on voters than content—what the candidates actually say.

After the September 30 debate, most pundits predicted that although Kerry had won there would probably be little effect on the two candidates' support. But polls published four days after the debate indicated that support for Kerry had risen above or come very close to that for Bush. It may be that some uncommitted voters had been swung toward Kerry by the debate. In the four weeks left until election day there will be two more debates between the presidential contenders and one debate between the vice-presidential candidates. The race looks set to remain very close.

■ *Kunio Tsurumi, Washington
October 4, 2004*

JAPANESE INDUSTRY

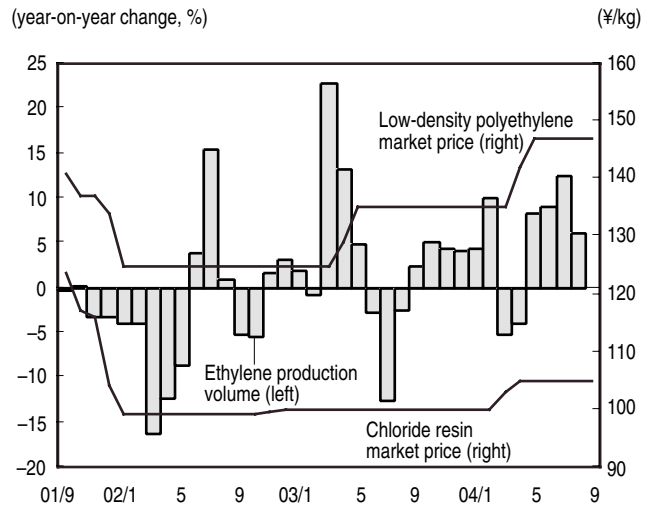
IRON & STEEL



Sources: Economy, Trade, and Industry Statistics Association, etc.

Crude steel production in August was up 1.7% from a year before, and the government forecast is for an increase of 2.9% to 28.79 million tons in October–December, the highest figure for the quarter in 30 years and the third-highest ever. With demand running strong, steelmakers were able to hike prices again in October.

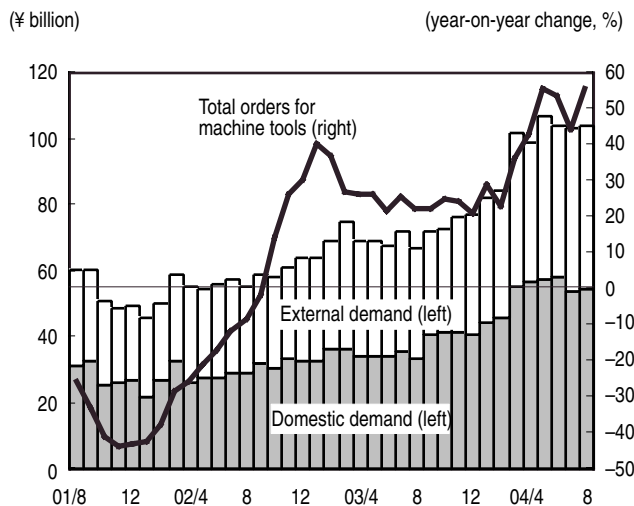
CHEMICALS



Source: Research Institute of Economy, Trade, and Industry.

Ethylene production rose by 6.0% from a year before in August, and plants were running at 98.5% of capacity. The price of polystyrene, whose uses include food packaging and consumer electronics, has been hiked three times this year in response to higher material costs, an unprecedented move for a general-purpose plastic.

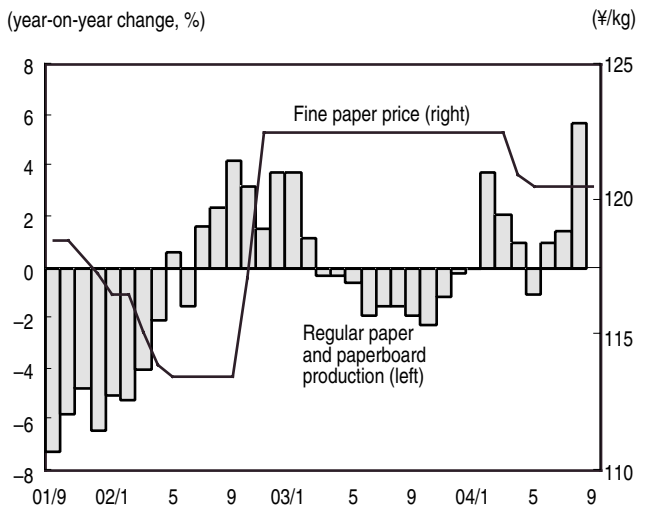
MACHINE TOOLS



Source: Japan Machine Tool Builders Association.

August machine tool orders soared 55.3% year on year to ¥104.2 billion. It was the first time the August figure topped ¥100 billion since 1990. The wave of investment in digital appliance equipment has spread to smaller firms; US and European demand is also up.

PAPER & PULP



Source: Economy, Trade, and Industry Statistics Association.

August production of regular paper and paperboard was up 5.7% year on year; domestic shipments rose 4.6%. Paper for printing and information uses was up 7.2%, partly due to extra newspaper pages for the Olympics.

■ Soichi Okuda and Etsuko Toyama, October 5, 2004

WORLD ECONOMY

The global economy is in the course of shifting from rapid growth to a slower-paced expansion, but the continuing rise in oil prices is generating increased wariness about future prospects.

In its autumn *World Economic Outlook*, the International Monetary Fund predicts that the growth rate of global gross domestic product in real terms will slip from 5.0% in 2004 to 4.3% in 2005, and it noted the heightening of downside risks. The IMF has estimated that a permanent increase of \$5 per barrel in the price of crude oil would lower the real global GDP growth rate by about 0.3 percentage point.

Japan

Despite the ongoing rise of the feeling that production levels have peaked in **Japan**, primarily because of inventory adjustment in the electronics parts sector, ex-

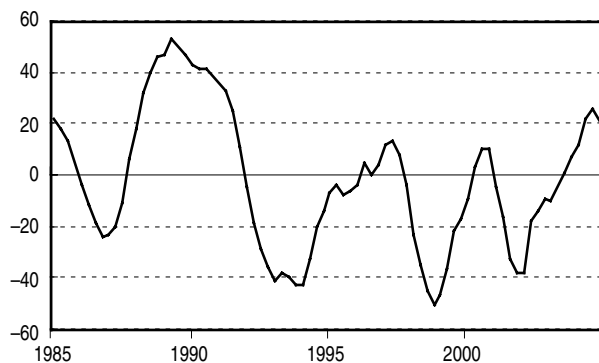
ports and capital investment are holding firm, and the economy is still in an expansionary phase.

On October 1 the Bank of Japan released the results of its September *tankan* survey of business sentiment. The latest quarterly survey showed a greater-than-expected improvement in views of the current state of the economy, and the decline in sentiment about the period to come was relatively modest, despite concerns that it would be depressed by factors like high oil prices. The diffusion index of business sentiment at major manufacturers was a positive 26, up 4 points from the June survey. It was the sixth straight quarter of improvement in this indicator (Figure 1). And the index for small manufacturers was up for the tenth quarter in a row.

The overall forecast for capital investment in the current fiscal year called for an increase of 3.5% over fiscal 2003, up from the 2.0% forecast reported in the June survey. The upward revision was largely a reflection of improvement in the outlook among small businesses. Major manufacturers are planning a hefty increase of 20.7% in their investment this fiscal year, the biggest annual rise since 1989.

Figure 1. Business Sentiment at Major Japanese Manufacturers

(diffusion index, favorable – unfavorable)

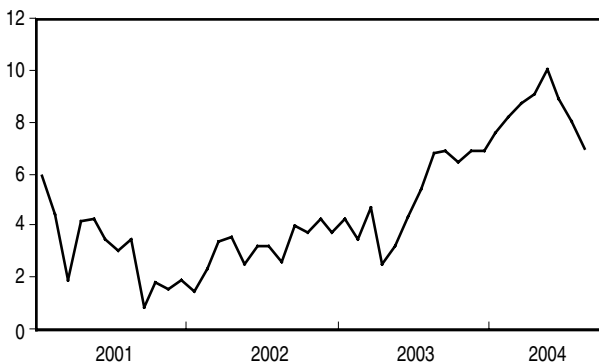


Source: Bank of Japan *tankan* surveys.

Note: The figure for December 2004 (end of graph) is the forecast as of the September 2004 survey.

Figure 2. US Retail Sales

(year-on-year change, %)



Source: Department of Commerce.

Americas

In the **United States** the Federal Reserve Board raised its federal funds rate by 0.25 point to 1.75% on September 21. In its statement announcing the interest rate hike, the FRB noted that growth slowed in the first half because of higher energy prices, but that production was picking up and that the labor market was gradually improving.

Statistics on consumer spending were generally on the weak side in August, partly because of the effects of hurricanes. Retail sales for the month were down from July, reflecting the drop in automobile sales, and the year-on-year rate of increase is showing clear signs of deceleration (Figure 2).

Housing starts picked back up to above the 2 million mark in annualized terms in August, but housing start permits, which are a leading indicator of residential investment, declined, and the number of existing homes sold was down for the second straight month, leading many to judge that higher interest rates are making their impact felt in this sector of the economy.

In the corporate sector, meanwhile, the ISM indexes (the Institute for Supply Management's indicators of business activity) were down in September for both manufacturing and nonmanufacturing, following a similar set of declines in August.

Reflecting higher oil prices, the deficit in the current account balance has increased sharply; follow-

Economic Growth Outlook for Asia, 2005

(%)	Baseline scenario	Slowdown-in-China scenario	Higher-oil-price scenario
China	8.0	6.0	6.8
South Korea	3.6	3.2	2.8
Hong Kong	6.0	5.1	5.1
Taiwan	4.8	4.4	4.3
Singapore	4.2	3.8	1.8
Indonesia	5.2	5.0	5.2
Malaysia	6.0	5.7	4.2
Philippines	5.5	5.2	2.5
Thailand	6.6	6.4	3.3

Source: Asian Development Bank, *Asian Development Outlook 2004 Update*.

Notes: The slowdown-in-China scenario assumes that real GDP in China will increase by only 6.0% in 2005. The higher-oil-price scenario assumes that Brent crude will cost \$50 a barrel through the first quarter of 2005.

ing a record high in January–March, it rose again in April–June, reaching \$166.1 billion.

In **Brazil** the economy has been showing clear signs of improvement since the latter part of 2003. The pace of growth in industrial production has been accelerating; the figure for July was up 9.6% from a year before. In September both Moody's and Standard & Poor's raised their ratings of the country's long-term government debt. And **Argentina's** economy has continued to expand, with real GDP up 7.0% year on year in April–June.

Europe

The IMF has upgraded its forecast for this year's real GDP growth in the **euro area** to 2.2%, a 0.4-point increase from its outlook as of April. It notes that the expansion is dependent on external demand, but also that the composition of growth varies considerably from country to country, with domestic demand growing strongly in France and Spain but weaker in Italy and "dormant" in Germany.

The pace of the recovery in **Germany** is extremely slow. Business sentiment has not improved, and the sluggishness of the upturn in employment has been dampening performance in the household sector. Retail sales were down 1.1% year on year in August.

In **France**, by contrast, the household sector has been registering increased demand. Household consumption of manufactured goods was up 1.8% from the previous quarter in April–June, and housing starts were up 6.3%.

The relatively high pace of growth in **Britain** has continued, with real GDP up 0.9% from the previous quarter in April–June, but recently there have been some indications that a slowdown is on the way. The housing market, which had seemed to be overheating, has settled down somewhat, with home prices dipping in August for the first time in two years.

Asia

The IMF observes that the expansion in Asia has been running faster than expected, thanks to strong growth in China, the global recovery in the information-technology sector, and supportive macroeconomic policies. But it cites such possible negative factors as a slowdown in China, higher oil prices, and a downturn in the IT sector. In its September outlook the Asian Development Bank notes a similar set of downside risks, observing that the impact of a Chinese slowdown would be felt especially strongly in places like Hong Kong, Taiwan, and South Korea, while higher oil prices would come as a major blow to Thailand and the Philippines (see the table).

Industrial production has been growing at a double-digit pace in **South Korea** ever since February; the figure for August was up 10.6% year on year.

In **China** the pace of growth in consumer spending has begun to slow, with July retail sales rising by a relatively modest 8.4% from a year before. The authorities' tightening of monetary policy seems to be having a visible effect.

India's real GDP growth rate in April–June was a somewhat disappointing 7.4% year on year. The slow growth in agricultural production, up only 3.4%, was the main factor. The performance of the services and manufacturing sectors has been improving.

■ *Soichi Okuda and Fumio Oi, October 6, 2004*

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