

## Asian Economies in 2010

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2010 is the year when Asia will become a bigger driver of global growth, as predicted by several economists. The developing Asian Economies will grow at 7 per cent, whereas China and India are likely to grow at 9.5 per cent and 7.5 per cent respectively. The emerging Asia could grow by more than 5% over the previous years, and the global economy is expected to grow at the rate of 2.7 per cent in 2010. Several reports say that the Asian nations were continuing a V-shaped recovery from the sharp downturn prompted by the onset of the global financial crisis in 2008. Surprisingly this V-shaped recovery is not being driven by the US, Europe or Japan.

<sup>1</sup>Asia today features five of the twenty largest economies in the world. There will be an increasing emphasis on emerging markets. China will overtake Japan to become the world's second largest economy. In India agriculture will account for a smaller share of GDP than manufacturing. Asia's rapid development has led to four fold increase in average per capita income, lifting more than 500 million people out of poverty during last 3 decades. The poverty rate in Asia has remarkably declined from 80 percent to 16 per cent of the total population during the period.

In <sup>2</sup>an ASEM conference on "Beyond the Global Crisis: A new Asian Growth Model?", held at Kuala Lumpur in October 2009, several strategies have been discussed that contributed to Asia's successful economic transformation: The success of Asia was not because of a single factor, but instead a confluence of factors that have driven economic development.

The following four features have been critical in the development of most of the Asian Economies:

A sustained economic growth has always been a priority in the Asian economies. The East Asia and South East Asian countries have focused on institution building and promoting industrialization. Institutions have been established to plan, drive and monitor the laying of necessary economic foundations; while aiming at promoting environment conducive to growth. Industrial policies of these countries targeted at enhancing efficiency, higher productivity and competitiveness. Incentives and some domestic protectionism have become necessary at the initial stage to advance the industrialization process.

Another important feature is Asia's high rate of savings, exceeding 30 percent of gross national product (GNP) in most Asian economies, which enable the public and private sectors to fund capital accumulation from domestic sources. The combination of efficient capital and productive labour in turn, generated higher value added activity, accelerating economic growth.

The Asian economies by and large adopted an outward only –oriented development path rather than depending only on domestic path. Whereas countries like India developed mostly on domestic demand, and as a result it was not affected by global recession as much as its neighbours.

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<sup>1</sup> Refers to Japan (rank:2), P.R.China (3), India (12), Korea (15) and Indonesia (19) based on 2008 nominal GDP in USD terms.

<sup>2</sup> ASEM (Asia-Europe Meeting) Conference on Beyond the Global Crisis: A new Asian Growth Model?- Paper on Asia's New Development Strategy: Where Now? –Dr. Zeti Akthar Aziz 2009.

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Most of Asia, has been very open to international trade and foreign direct investment (FDI) rapidly integrating with the global economy. The trade volume of Asia of total world trade increased from 14 per cent in 1970 to 28 per cent in 2008, while flow of FDI increased from 7 per cent to 20 per cent. The foremost advantage of Asian economies is in its heterogeneity and diversity was never a restraint in its progress, but complemented the region's economic development.

The region's different development levels and technological capabilities, known commonly as the<sup>3</sup> 'Flying Geese model.' In 1970's, Japan relocated the more labour intensive stages of production processes to the newly industrialised Asian economies including Malaysia, Indonesia and Thailand. The emergence of China, further provided significant impetus to this pattern which has promoted globalization of the production chain among regional economies, thus strengthening the trade links within the region, the transfer of capital, knowledge and technologies for strengthening industrial capabilities of this region.

#### **After Financial Crisis:**

The 1997-98 Asian financial crisis exposed several structural weaknesses, and following this, these countries have undertaken wide ranging financial reforms, while developing more stable, resilient and affective financial systems. This promoted the Banking sector to broaden access to credit to other economic agents. The once bank dominated financial systems have become more diversified and competitive with strengthened governance, disclosure and regulation.

The current global crisis, the most severe in the post world war II period revealed weaknesses to the current global system. While signs of economic stabilization are now emerging, the prospects of recovery are slow and gradual in advanced economies. Asia's relatively strong and resilient financial systems are in a sound position to accelerate growth much faster in this region, for ensuring sustainable economic growth, Asia's regional and global integration and inclusive development contributed for its success.

#### **Future strategies:**

The positive features of Asia are its favourite demographic structures, fast rising income levels and the growing middle income class. A world bank report suggests that both China and India have large and growing domestic middle class markets, estimated at about \$ one trillion in China and \$250 billion in India annually: This trade is expected to continue given an increasing young population in Asian countries with new spending pattern.

The second factor is the relatively sound financial position of households in Asia, with high saving rates of above 30 per cent of GNP and relatively low debt levels compared to advanced economies. This is supported by the ability of the financial sector to provide financing to support consumption.

Another strategy is further diversification of the external markets, to accelerate the efforts to foster greater regional trade ties for Asia. The rapidly rising Asian middle income class will increase final demand for goods and services. Asia can take full advantage on its immense diversity as a source of economic complementarities. The third strategy is the promotion of deeper financial integration, which is important for further advancing the economic development of the region. According to the economic experts, a fully integrated financial system will be one in which potential market participants, both the banking sector and financial markets, adopt a

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<sup>3</sup> C.H.Kwan, 2002,RIETI, paper on "The Rise of China and Asia's Flying Geese pattern of Economies development: An Empirical Analysis Based on US import Statistics

single set of rules, have equal access and treated equally. The end goal of financial integration is to establish a free flow of finance and capital, which aims for unrestricted mobility of goods and services.

Greater financial integration would bring about three key benefits. It fosters greater competition; there by improving the efficiency in the allocation of capital with the region while the individual Asian financial markets are small, an integrated market would raise Asia's attraction to both regional and global investors. Secondly, financial integration would facilitate a more efficient transfer of surplus funds for investments with in the region, with more optimal returns. Thirdly, financial integration enables countries to build on the complementarities between countries. Thus with greater integration, countries in the Asian region can expand on financial products and services.

Regional financial integration is particularly important at this stage of Asia's economic development. Indeed, a more integrated financial market within the region would lead Asia to a higher stage of economic development. First, while many of the Asian economies have large surplus funds, there also exist many development needs across the Asian economies, including more advanced infrastructure development including transportation, healthcare and education, which require substantial financing. However, cases of mismatched funding needs are not uncommon. In this regard, a more integrated regional financial system would enable for a better matching of saving and investment in the region, thus effectively channeling Asia's large pool of saving into productive uses within the region that would support growth and development.

<sup>4</sup>All high growing Asian Economies embrace trade openness, the trade barriers being progressively reduced. Trade liberalization need not be just reducing tariff rates on imports, but it can take the form of de-monopolizing and de-licensing. Trade liberalization broadens the set of firms that could directly participate in international trade. Demonetization of trading rights could dramatically increase a country's trade openness.

The second aspect<sup>4</sup> of the Asian growth model is the use of government policies to promote high tech and high domestic value-added industries, which is called a leapfrogging strategy. While most of the economists view that trade openness does help to promote economic growth and played a key role in the success stories in Asia, some economists are of the opinion that there is no strong evidence to show that the leapfrogging strategy-a government-led industrial policy that tilts resource allocation to technologically sophisticated industries that contribute to higher growth rate.

Stephen Roach of Morgan Stanley cautions that Asian economies still have to "do a lot of heavy lifting", if they are to emerge as the new engine of the global economy, but they are becoming complacent that the post-crisis world "is theirs for the asking". Asia remained heavily dependent on external demand from the west and until Asia embraces a new model, which is more balanced and reliant on internal private consumption, the fury is out on whether or not this is Asia's moment.

Asian economies with vast diversity in populations, ethnicity and social structure have made remarkable progress, despite challenges from urbanization, rising income inequalities and social instabilities. This miracle was achieved not by chance, but by pragmatic policies, ensuring sound economic fundamentals and strong institutions. A long-term growth depends on supply factors, not just demand. A country's long-term potential growth rate with out igniting inflation is

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<sup>4</sup> Zhi wang, shang-jin wei and Anna wang's article "Does a Leapfrogging Growth strategy Raise Growth Rate? Some International Evidence (2009)

determined by growth in its labour supply and productivity. Sustainable growth in Asia is possible only with a long-term concerted effort with more regional co-operation and greater understanding within the neighbouring countries.

*This article is based on the deliberations held in ASEM conference on “Beyond the Global Crisis: A New Asian Growth Model”? at Kuala Lumpur from (18th-20<sup>th</sup> October 2009)*