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Risk and opportunities. Global trends affecting Asia

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1 The long term trend

It is a common mistake to see what you expect to see. Most predictions are based upon extrapolation of past and present trends. The challenge however is to detect the underlying trends and even more so where and when trend shifts—the point in time when the curve starts to bend—will occur.

People living in the first decade of the 20th century did look upon the British Empire as invulnerable, a mighty and powerful industrial powerhouse, an unrivalled military power, the political driver of 19th century globalisation, the universally accepted arbiter, the policeman of the world and highly respected as such, a cultural magnet—like the Roman empire in its heyday apparently to last for ever as a truly global political and economic power. Just 20 years later—in the mid 1920s—the British Empire had exhausted its resources in a bloody war, the flower of the British youth had perished on the muddy battlefields of Flanders in Northern France, it faced an unprecedented slump and further 10 years down the road abandoned its strife for free trade in favour of semi-protectionism plus imperial tariff preferences.

The perception of the US Empire today may be congruous to how people felt about the British Empire 100 years ago. Invincible, untouchable, almighty.

There is unfortunately one more parallel. Underlying trends point to not necessarily a fall of the US Empire but a decline of its almighty power raising questions about where the world hitherto under American leadership is heading?

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2 The challenge

The challenge comes primarily but not exclusively from China and India. Those cherishing long term trends may spot the reversal of the trend shift from Asia to Europe, let us for convenience call it the Western World, taking place 500 years ago. Now the ball starts to roll back. Asia stands for more and more power and influence signaling a rise instead of decline and fall.

Speaking about Asia politicians and academics often framed it: China OR India. To day we know the answer. It is China AND India.

The political imperative for these two nations runs as follows. To avoid domestic chaos and disorder, and that is what they fear most, they need social stability. The unconditional condition for that is high employment and that requires high economic growth. The pull factor has been the American growth engine but if, what is possible even likely, the US economy starts to splutter, a substitute must be found and that can only be domestic growth. To do it in tandem will not only be easier but also provide much stronger results. Their choice is quite simple. Either they get together to stimulate their economies inside some kind of economic integration or they face an uncertain and ugly prospect of growing unemployment pointing to social unrest jeopardizing the political system. They will choose the first option: Together. They will put behind them all the trivial but often mentioned rivalries, recriminations and jealousies. The future of these two big and great nations forging ahead will not be compromised.

Just one figure: In the beginning of the 1990s mutual trade was about 150 million US dollar. To day it is more than 14 billion. An increase in little more than 10 years of 100 times. Indian flagship enterprises like Infosys, Wipro, Tata are entering the Chinese market with confidence. Chinese flagship enterprises like Haier, TCL are savouring the consumer market in India seeing it as a platform for expansion to other markets.

Scepticists mention demand for energy as a potential spanner in the works. Unlikely. Again, both of them are keenly aware that competition or rivalry will be detrimental to both. Better to shape some kind of implicit understanding, not to tread on each other's corns. High level talks in Beijing mid-August about how to exploit energy reserves around the globe in common reveals an emerging consensus to that effect.

How far, how fast, how deep will the integration go? I will reveal the red dot on the speedometer: The different legal systems. Economic integration is built upon trust and mutual benefit but at some stage it starts to produce mergers & acquisitions, competitive litigations of which some end up in court. Unless some degree of convergence and congruity appears between the two legal systems—and we haven't seen the slightest attempt—they can not be resolved. Integration runs into a barrier. This is one of the crucial lessons from 50 years of European integration.

3 Share with others

Any politician will confirm that stability and coherence require a degree of sharing of wealth. Otherwise society starts to break up. The same goes for a large region like Asia. If growth and wealth tend to be lopsided and concentrated in some albeit large nations while the rest find it difficult to keep step animosities start to emerge with unwanted and unpredictable political consequences.

In the coming decades China and India will grow faster than the rest of Asia and position themselves with powerful consumer markets. These two nations, even if they for a long period were lagging behind, must offer to share some of their growth and some of their wealth. If not what might have been a prosperous Asia with nations comfortable and at ease with each other might turn into sterile rivalries and mutually destructive competition for markets and investments. In short: China and India must turn Asia into a self-sustaining economic growth area.

Magnanimity may look costly in the short run but in a longer term perspective it lays the foundation for mutual trust.

It is encouraging to see how the Asian nations by free trade agreements (FTA) have chosen this path opening the door for economic integration precisely to offer some kind of sharing. Hopefully the East Asian Summit scheduled for the end of 2005 will give directions for a future more broad integration and institutionalisation.

4 Institutionalisation

The broader aspect of this is institutionalisation or organisation of Asia in the same way as the Europeans institutionalised after 1945. Asia should not imitate the European integration but make its own integration based upon Asia' s need, traditions, background and political conditions.

The great vision that recently jumped from the drawing board to the negotiating table is a FTA comprising China, India and the ten Asean countries. It will add up to about 3 billion people, an average annual growth of let us say 7% and in 2010 or thereabout when it is fully implemented an income per capita of about 1,500 US dollars depending upon growth rates from now until then.

But Asia should not stop there. Institutionalisation means that countries create a platform on three levels:

First
: Each country endorse a stronger discipline knowing that its policies have repercussions for adjacent nations.

Second
: A framework is established for helping each other inside the region as was the case for the Tsunami and could, should but wasn't for the financial crisis in 1997.

Third
: Asia gets influence on the global scene corresponding to its economic weight and political clout while presently each Asian nation is gunning for itself—sometimes out of step with other Asian nations.

The tough question is sovereignty. Integration does not mean abandoning sovereignty—a common and often heard misrepresentation. No, it signifies transfer of sovereignty to exercise it in common with adjacent nations pursuing analogous even identical political objectives. This clarification is of paramount importance if or when the Asian nations decide to test the water and jump into the next phase of integration.

5 Chinese/Indian multinational companies

Let us turn the spotlight from the governmental sector to the private sector. No economic superpower is worthy of that name unless it originates multinational companies in the true sense of that word.

And that will, in a not too distant future, be supranational companies operating out of the national context not constrained by a national straitjacket.

Hitherto almost all multi- or supranational companies have been European or American. The Japanese companies operating worldwide are mostly Japanese companies operating internationally but mentally still inside the national box.

Chinese companies are on the prey for American enterprises or parts of American enterprises—Lenovo/IBMs PC division, CNOOC/Unocal, Haier/Maytag. It is now within financial reach for China to throw the dice but apparently the Chinese companies primarily buy expertise to run a multinational company. They are buying knowledge about the international marketplace and how to operate on it.

The Indian companies will soon become catalogued in the hall of fame, but it is not clear whether they will try to go it alone or choose to buy expertise as the Chinese companies are doing.

The Chinese companies being brought up in a non-market incubator lack instincts to operate in the marketplace thus buying such abilities while the Indian companies born and bred in the market place do possess that knowledge.

A multinational or supranational company needs to safeguard itself against legal repercussions not only from a variety of national legal systems but also from the emerging international legal framework. Illustration: A large company taking an important maybe strategic investment decision must be sure that its validity will not be contested by, not only the well known national legal systems, but also rules implemented by EU, WTO and other institutions. One step further: It has to build into its legal arsenal a defense against possible law suits from international pressure groups such as Greenpeace, Amnesty International etc. A whole new dimension for these companies.

6 US dollar versus the Yuan

The US insistence on an appreciation of the Yuan reflects nothing else but China' s growing economic weight on a global scale. China implemented an extremely modest appreciation (2.1%) end of July. It was more a change of the currency rate regime for the Yuan than an appreciation. In fact the Chinese message was: The US dollar does not carry the same weight as before. In the longer term however the Yuan will mature into a truly international currency, not linked to the US dollar and probably much stronger than its current value. It will be an international currency like the Yen, the EURO and the US dollar—but it will take time. And we should give it time.

I would focus upon two points not always given their rightful place.

First
When China delinked the Yuan from the US dollar the rest of Asia faced a strategic choice: Follow the US dollar or the Yuan. The appreciation (2.1%) was too small to bring that out in the open but the reaction clearly showed that most Asian countries followed the Yuan some of the way. Asia said goodbye to its role as a steadfast member of the US dollar zone. The economic impact will be limited. The strategic signal as an omen of a weakened US position in Asia will be tremendous. It may turn out to be a seminal shift away from the US dollar and that was hardly what the US asked for.

Second
Any student of economic history will tell you that the surplus on China' s balance of payments and the strong Yuan is contradictory to conventional wisdom. China is saving. The US is dissaving. It should be the other way around. China should as an emerging economy borrow to finance investment. Instead the US borrows to consume. This augurs fierce global economic upheavals in the coming years.

The main problem is that the global economic structures expect savings to be made in rich countries and borrowing in poor countries. Presently it is the other way round. We do not know whether the international financial system can adapt to channel the funds in the opposite direction of what they were designed to do.

7 US economy—iceberg right ahead

A closer look at the American economy confirms the problems. The combined deficit on public finances and balance of payments amount to about 10% of Gross National Product.

The global economy is defined by American over-consumption and under-production, Chinese (and partly) Indian under-consumption and over-production, too much international liquidity that should ignite a global inflation spiral but doesn't because of low wage cost in Asia and China plus Japan financing this mismatch between production and consumption. These imbalances have to be redressed. The key is a transfer of purchasing power from US to primarily China to reduce American and increase Chinese consumption.

It can be done in the following ways.

First
The first arrow in the quiver is a more restrictive economic policy in the US by fiscal tightening. It is very unlikely under the Bush administration. Monetary policy is being tightened but too late and too little. Indeed the FED has for several years been stoking the engine.

Second
Currency rate adjustments. US dollar must depreciate reducing real incomes in the US and beefing up real incomes in Asia. The US dollar has depreciated but against the EURO. Adjustment has failed to come off among other things

because of growth disparities between US and Europe. A sharp drop in the US dollar against the Asian currencies should be in the offing but has not yet materialised.

Third

Protectionist or semi-protectionist measures in the US. This is actually happening as the US posture on textile exports from China bears witness to. The demand for a Yuan appreciation reflects the same attitude. In short: Trying to throw the burden of adjustment on other countries.

Fourth

Leave it to the market not knowing how and when it will happen and which form it will take but running the risk that any adjustment will be abrupt and throw a spanner into the smooth working of the global financial system.

It is alarming that the policy controlled options seem to be out of reach pointing to a gradual slide towards option three and four raising severe doubts over who if anybody is in control of the global economy precisely at a moment when astute policy-making is called for.

8 The American dilemma

The US strategy focusing—rightly—upon terrorism, rogue states, weapons of mass destruction (WMD) as the main threat forces a choice upon the US.

The US may invite the rising powers to align themselves with this global strategy. Steps to that effect were initiated after 911. There is much to say for such a strategic move as we talk about a genuinely global threat befalling all countries enrolled in globalism. It is, however, unlikely that the rising powers join the US policy without a political price and the name of that price is power sharing. So far the US has not been willing to square this circle.

The US stands a good chance to rally most of the world under the banner of fight against terrorism. The immediate aftermath of 911 proved this. Recently when the terrorists seem on the defensive and the US on the course to win this war—not yet won but militarily going well—US flirts with a fall back on the foreign—and security policy on the drawing board before 911 classifying China as a potential enemy. We can also catch a glimpse of a more classic role for an empire in the US policy vis-à-vis India and Pakistan.

The imperative of choosing political course and whether to do it with or without partners is a classic dilemma for the super power in pole position. But at the present juncture it becomes even more crucial because it may involve the future of globalisation.

9 Implications for globalisation

The world has been incredibly lucky that the rising powers such as China and India have chosen to join the existing global system instead of tabling their own model. It is within reach to shape a truly global system. Whether the world will rise to the challenge depends to a large extent upon US attitude towards China and India and in particular, towards Asian integration forged by these two countries.

US benevolence like the posture towards European integration 50 years ago will facilitate an Asian integration inside and in conformity with the existing global system. The world will glide towards a convergence of economic models very much based upon the market economy may be even a lower profile edition of American capitalism. A less accentuated convergence of political systems upgrading notions like democracy and human rights may be attainable, albeit more heterogeneous than for the economic model.

If the US choose to be sullen or even prefer to curb Asian integration, China and India will sooner or later ponder whether the existing global system is the right one for them. The world may then see divergent economic models and distinct political systems. Globalisation in its existing form even as a concept may be contested and the question being put forward whether that particular model is unrivalled and second to none.

The US posture vis-à-vis Asian integration forged by China and India may determine the future of globalisation: Whether it will continue, and if so, in what form or whether another model will replace it. The stakes are high.