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SHIFT IN GLOBAL ECONOMIC POWER

This is S-E Asia's moment

By Joergen Oerstroem Moeller THE first half of this year has seen a seminal shift in global economic power. Instead of the United States dominating, there is now a more even spread than at any time over the past 60 years. Other nation-states and groups of nation-states are catching up with the US.

Remarkably, the significant slowdown of the US economy has had little or no impact on other major economies such as the European Union, Japan, China, India or South-east Asia.

US economic growth fell in the first quarter to 0.6 per cent. Official predictions for the year have been lowered from 2.9 per cent to 2.3 per cent. Economic growth in other major areas has, however, remained resilient. The Euro zone revised its forecast up from 2.4 per cent to 2.6 per cent. Japan too is doing reasonably well, with growth estimated at 2.3 per cent. Together, they more than make up for the American shortfall, keeping global growth near the 5 per cent mark.

Just a few years ago, a US slowdown would have hit both Japan and the Euro zone badly. The Europeans used to say: 'When the US sneezes, Europe gets a cold.' Now it looks like the US can be flu-ridden without any apparent contagious effect on the rest of the world.

The reason? The US share of global gross domestic product (GDP) has been falling in recent years. According to purchasing power parity calculations, it is now at about 19 per cent compared to about 16 per cent for China and 5 per cent for India. Asia's two rising giants account for more of global GDP than the US alone.

The US market as an outlet, in particular for Asian exporters, has lost its preponderant position. Goldman Sachs has calculated that with an average annual Chinese growth rate of 10 per cent from 2005 to 2007, exports to the US accounted for 2.7 percentage points for 2005, 2.2 for 2006 and a forecast 1.6 points for 2007.

A similar observation arises from an analysis of Chinese trade figures. In 2000, 31 per cent of Chinese exports went to the US. This year, the figure is estimated at 23 per cent.

The share to Europe and Japan has barely changed, but the share to the rest of the world has risen by almost a third.

This augurs a fundamental switch of global trade flows away from the US (and probably also Europe), and more towards what used to be called the developing nations.

Much of the trade flow is in the form of raw materials to stoke China's rapid economic growth. But it does include manufactured goods. China and Asia are fast expanding trade with regions such as Africa, the Middle East and South America.

Of course, it is still early days and much can happen. Economic and trade figures can be mischievous; they have to be monitored for a while before firm conclusions can be drawn. But so far there have been no indications to suggest this is not a permanent shift.

Another observation is that the Asian supply chain now looks robust enough to support growth in Asia even with weaker US demand. Hitherto, semi-manufactured goods were put together in one country - normally China - and from there, the final product was exported to the US. But increasingly, manufacturing and selling are both taking place in Asia, thanks to the rising domestic markets in China and India.

For South-east Asia, such a shift in global economic power raises a number of opportunities. There is nothing wrong, of course, in being dependent on the US market, but increased diversification improves the outlook for high and stable economic growth. This is even more so when the rising economic powers are in the same geographical area and are partners in a regional supply chain.

The strong Chinese economy, with a currency reserve of US$1.2 trillion (S$1.8 trillion), marks the coming of a new global investor. There can be no doubt that part of this enormous amount of money will make its way to South-east Asia. The policy challenge is to mastermind new investment patterns that will bring about win-win situations - politically and economically - for China and the South-east Asian countries.

To attract the Chinese dollar, South-east Asian countries need to analyse, define and enhance their already existing competitive strengths. They must cooperate and integrate to avoid a potentially destructive reciprocal competitive game to attract funds and investments. Integration must make it more profitable to invest in South-east Asia compared to other regions of the world.

Whoever wins in this investment quest will move into a prominent position in the supply chain that China is building to serve its economy for the next decades. This supply chain will be dominated by Chinese domestic demand instead of exports to the US. The suppliers must tune in to this new demand pattern.

Some South-east Asian countries will face the same problems that outsourcing has brought to the US and Europe, such as the loss of jobs. The solution is to figure out which competitive parameters cannot be copied easily elsewhere. Typically, these are rooted in tradition and training and are not based on costs. The European experience suggests that the way ahead is to switch from pure manufacturing to include accompanying services in a total package, offering not just the product, but also elements such as regular upgrading, training of staff, repair and maintenance, design, finish, quality as well as high performance. Competitive parameters are thus disengaged from the more technical factors that tend to be ephemeral.

The world will see a growing number of Asian multinational companies. South-east Asia - or at least some countries in the region - can capitalise on its existing reputation for good corporate governance to harbour such companies. Several of the biggest European

multinational companies have their corporate headquarters in the Netherlands, even if their industrial activity in that country is limited. The same may happen in Asia and South-east Asia. The spin-off effect can be substantial.

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THE NEW CHALLENGE

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