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SHIFTING OF ECONOMIC POWER TOWARDS THE ASEAN ECONOMIES

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Abstract

It has become the new truth of the early twenty-first century that the Western world we have known is fast losing its pre-eminence to be replaced by a new international system shaped either by the so-called BRICs comprising Brazil, Russia, India and China, the 'rest', or more popularly by that very broadly defined geographical entity known as Asia. Today, the Asia Pacific accounts for 38% of the world economy. Europe come second and North America third. Within Asia over 67% of the GDP comes from three countries – China, India and Japan. It is predicted that Asia will be the main driver of global growth over the next two decades with a newly-emerging Asian middle class of nearly 1.5 billion. There is an irresistible 'power shift' in the making and that the West and the United States are in steep decline.

This paper discusses conceptually what is meant by the term shifting economic power and traces through some of its possible dimensions and implications. It also sets out alternative approaches that might be used to develop quantitative matrix of economic power shifts.

Keywords: BRICS, Shifting power, Quantitative matrix, GDP, Global growth.

1. INTRODUCTION

We are currently witnessing a major shift in the balance of economic, financial and political power from the advanced countries to emerging markets – from West to East. This is, of course, not the first time that we have observed this kind of global shift. The rise of the West from the 15th century and its concomitant, the decline of China, was itself an earlier instance, if mirror image, of this kind of shift. The industrial revolution, which gave rise to what is sometimes called "The Great Divergence" (the growing divergence in manufacturing capability and in capacity to project power between the first countries to industrialize, principally in Europe, and other regions) marked another global shift. It is no coincidence that the first industrial nation, Great Britain, came to control fully a quarter of the world's population and land mass by the end of the 19th century. There was the shift in economic power from the pioneer industrializer, Britain, to followers like Germany that contributed to the economic and geopolitical tensions helping to set the stage for World War I. There is Charles Kindleberger's thesis that that Great Depression of the 1930s was a consequence of the global shift in power from Britain to the United States, one that left an exhausted Britain incapable of managing the world economy and an inexperienced United States unwilling to do so. There is the shift after World War II toward the two great superpowers, the United States and the Soviet Union, and the dominance of the U.S. over the Western world. There is then the relative decline of the United States owing to catch-up growth, first in Europe, next in Japan, and finally in East Asia and elsewhere, which gradually closed the per-capita-income gap. The current shift toward emerging markets like China and India is usefully seen in this light.

Today, as much as China is the centre of global manufacturing, India has become the international hub for global service industries. The economic resurgence of China and India has also made way for the emergence of Thailand, Indonesia, Pakistan and Vietnam as manufacturing bases. This shift of world economic power back to Asia is highlighted in the ADB Key Indicators.

However, China and India to fuel global economic growth need to encourage inclusive growth and oppose all forms of trade protectionism. They need to improve the global monetary system and promote new modes of development. One of the most significant changes today is the collective rise of emerging countries. The emerging countries have become an important force in global affairs. They are no longer in the backseat of global economic governance. The emerging economies are now institutional players, rule makers and protectors of interests. Many global issues cannot be solved without the participation and support of emerging economies.

2. OBJECTIVES OF THE STUDY

- ✓ The study of east and west economies.
- ✓ To make future predictions based on the available data sources.
- ✓ To analyze the importance of varied factors in promoting the growth.

3. RESEARCH METHODOLOGY

This research is primarily based on secondary data. It is collected from varied sources like- journals, magazines, websites etc.

4. MEANING OF POWER SHIFTING

Shifting of power means major shift in the balance of economic, financial and political power from the advanced countries to emerging markets. The main shifts in power distribution are between the developed West and emerging economies, many of which are in the Asia-pacific.

5. THE DRIVERS OF POWER

The current narratives of power distribution in the Asia-Pacific oversimplify a number of the structural instruments of change in the capabilities of each state. These narratives also disregard the extent to which relations between the region's major powers are in flux. Ongoing transitions include the following:

- **Military:** The role of traditional military power is diminishing relative to other instruments, from development assistance to cyber offence. Despite this, spending on traditional military platforms and capabilities is rising fast among the key actors in the Asia-Pacific. By this measure, the United States has and will continue to have for some time the largest, most advanced, best-trained and most integrated military. While China's defense spending has-been rising at double-digit rates for most of the past two decades, its capabilities remains weaken many areas. Their potential effectiveness is hampered by a lack of interoperability with other powers in the region. Meanwhile, the militaries of Japan and India are becoming – in very different ways – more versatile and potentially expanding their remit. In the future, there will be more capable military powers in the region, potentially able to act alone or jointly with others. Current perceptions of China's rising capabilities outstripping those of others in the region will need to be tempered.

- **Economic:** While China has the world's second-largest economy and – despite recent problems – is growing faster than other major economies, its growth rate is in secular decline. The United States is still the largest economy and will continue to be so for many years (though purchasing-power calculations complicate this). The future of Japan – the world's third-largest economy – is uncertain, and dependent on the success of Prime Minister Shinto Abe's 'three arrows' of economic reform. India's economy remains notably smaller than those of the other three, but it is on the point of surpassing China's rate of growth, and the formation in 2014 of a new government led by Prime Minister Narendra Modi has significantly boosted confidence in it. If the Trans-Pacific Partnership (TPP) is successfully negotiated, the potential for growth-boosting integration between the United States, Japan and the other 10 TPP members may mitigate their current dependencies on China.

- **Demographics:** Japan (more immediately) and China (over the coming years) face significant demographic challenges from ageing populations, decreasing numbers of workers and gender imbalances. The United States is also beginning to age, although not as rapidly, while India, with its relatively youthful population, has some decades of demographic dividend ahead of it. The United States is a more open society in terms of immigration, something neither Japan nor China shows much likelihood of emulating.

- **Partnerships:** The historical US 'hub and spokes' model of regional relations is set to change. A more networked structure is developing within the region, with an increasing number of overlapping plurilateral groups. Japan and India, in particular, are building and participating in more formal and informal regional groupings, although these often focus more on strategic dialogue than action.

6. CHARACTERISTICS OF THE ASIA-PACIFIC IN FUTURE

Change will be more rapid and more volatile: This will result in the power distribution between the principal actors becoming more complex, finely balanced and difficult to assess clearly. Change is already being facilitated by new technologies, particularly in media and communications, making control of information increasingly difficult. The rise of new, often disruptive businesses in the emerging Asian economies will affect the economic balance in unpredictable ways. Demographics are changing, with corresponding implications for social services. Natural resource challenges are becoming tougher.

Power will become more diverse and diffuse, with more state and non-state actors having influential roles. Regional groupings are proliferating and in some cases becoming institutionalized, with varied impact. Moreover, power is becoming more diffuse within states, making it harder for governments to manage internal debates and to send clear messages to neighbours, particularly where nationalism is growing.

The region will become more complex, unpredictable and thus hard to govern as a result of the rise of new actors, challenges and tools. This could lead to policy paralysis on the part of leading state actors, as a swiftly changing environment and too many choices lead to greater uncertainty and, in the end, hesitancy or no action being taken.

Countries, companies and other actors in the region will become more interdependent, which makes the previous point troubling. Already, all states in the Asia-Pacific are increasingly dependent on one another for growth, stability and security.

7. IDEOLOGIES

- **<u>Flexi-Nodal approach</u>**

In a flexi-nodal environment, there will not be one or two dominant powers but many influential actors taking the lead and/or collaborating on different issues of concern. Regional alliances will vary, depending on the specific area of focus, and could play out formally or informally. Their make-up and leadership will depend on who has the interests, will and capabilities to act. The Association of Southeast Asian Nations (ASEAN) and its various iterations (such as ASEAN+1 or +3) could provide the right context for a discussion on a maritime code of conduct for the South China Sea. On broader security issues, such as territorial tensions in the South China Sea, an ad hoc coalition could emerge involving, for example, China, the United States, India, Vietnam, the Philippines, Japan and Australia.

The ability of these states to work with one another will be vital in minimizing risk and addressing regional concerns, while still enabling them to promote and protect their particular national interests. Employing different policy-making tools and resources, states in the Asia-Pacific must become more versatile and adaptive. Successful states will not only need to work with non-state actors, but also, where appropriate, with other relevant external factors, including those in Europe for trade relations and those in the Middle East for energy security, While this new flexi-nodal approach may reflect the future reality for the Asia-Pacific, existing and alternative narratives will also likely persist, driven as much by the interests (and ideologies) of various regional and extra-regional actors.

- **Multi-Polar Approach**

In 20th century, the US provided the world with economic and political leadership. After the Cold War receded and capitalism was seen to win out over communist ideologies, we entered a relatively stable, uni-polar world where the US was the undisputed economic and military heavyweight. Expect this to change as the world becomes multi-polar.

The growth of emerging powers, principally Brazil, Russia, India and China (the BRICs), is increasingly challenging the uni-polar model. In 2050, we are likely to have a very different-looking economic 'top 10'. China is almost certain to be the largest economy in the world; indeed, the very latest figures from Goldman Sachs suggest that after the asymmetric impact of the western-inspired financial crisis, China may overtake the US as soon as 2027. India will not be far behind the US, while Brazil and Russia will demote the major Western European powers into the lower echelons of the top 10. It is clear that the world is becoming increasingly multi-polar as gaps in national power narrow between developed and developing countries.

8. REASON FOR DECLINING WEST

- **The Ascent Of Emerging Markets**

The rise of emerging markets in the last ten years has been extraordinary. As the panel below shows, emerging markets have improved their current account positions immeasurably in recent years through the export of commodities and manufactures, while consumption-hungry western nations have largely provided the demand side of the equation, resulting in a consistent current account deficit for the G7 since 2000.

The turnaround in the fortunes of many emerging economies has been dramatic, given that only12 years ago Russia suffered a debt default and Brazil a major currency crisis. The current account surpluses and consequently healthy foreign reserves have been driven by increases in oil and commodity prices, which have generated windfall profits for the Gulf States, Russia and Brazil. Meanwhile, the competitive advantage of low cost labor has seen Asia establish itself as the world's manufacturing powerhouse.

These excess foreign reserves have been invested in US financial assets such as Treasury Bond sand have led to the establishment of sovereign wealth funds that have been active in the equity investment and corporate finance arena. After a flurry of activity at the start of the credit crisis, they have been a little quieter recently, but are sure to play a significant role going forward.

- **The Credit Crisis**

The recent financial crisis was different from previous crises in many ways. In terms of its ferocity, it was the most gut-wrenching event for investors in living memory. But, perhaps even more uniquely, it was the first widespread credit crisis to have its epicenter in the west. Such crises used to happen in Russia, Latin America and Asia, with only the ripples affecting western economic shores. This time the shoe was on the other foot as the crisis took root in the US. Not only that, its impact was also most firmly felt in the US and Europe. Asian economies saw limited impact and the growing consensus view is that they have emerged relatively stronger than before.

The 1997-98 Asian currency crises was, in retrospect, an important watershed, as governments vowed to learn from their mistakes. The Asian economies have since built up significant currency reserves to avoid the need for IMF help. Time will tell if the recent financial crisis is also looked back on as a transformational moment when the centre of gravity in the global economy decisively shifted. What is certain is that it has clarified and accelerated an ongoing shift in investors' minds.

9. DRIVERS OF GROWTH FAVOUR DEVELOPING COUNTRIES

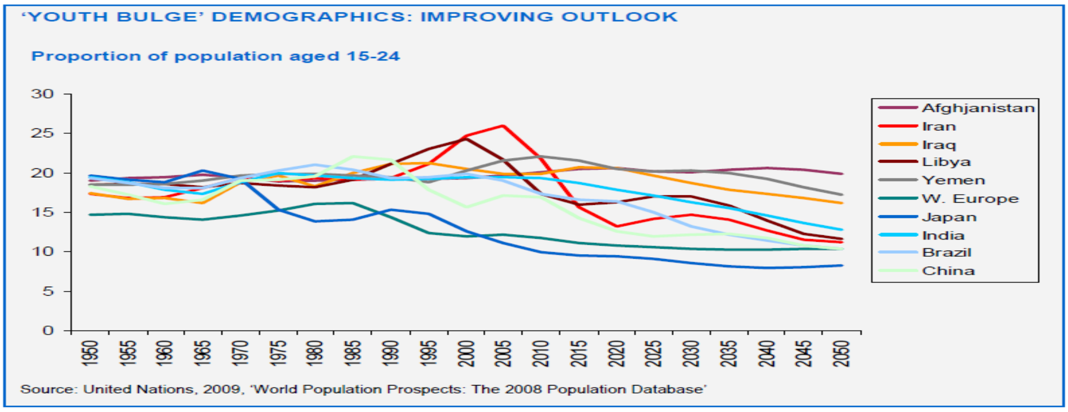
- **The Demographics Of Power**

Demographics have an important part to play in power shifts in combination with other political andeconomic factors. China is the most populous country on earth with around 1.3 billion people, while India is a firm second with around 1.2 billion. The next largest country is the US with just over300 million.

While the sheer number of people can give an economy obvious labor market advantages, the composition of populations can also have a significant impact on economic power and stability. One of the challenges that Japan and many Western European countries face is the ageing of their populations, which is putting increasing pressure on the state and working populations. Due to its 'one child' policy, China will also to have to face this problem in the next 30 years, at a much earlier stage of its economic development. Recently China changed its policy of "one child" due to the crisis of youth & adopted "Two Child" policy.

Another interesting strand of population theory that affects the balance of economic power and world stability, and which has also been a significant influence on recent US foreign policy, is the subject of 'youth bulge' demographics.

Many developing countries have a prominent youth bulge; these often tend to correlate well with increased geopolitical tension. For instance, parts of the Middle East and North Africa are currently experiencing prominent youth bulges (Libya, Iran and Yemen on the chart below, which shows the proportion of various populations in the critical 15-24 demographic grouping since 1950).Improvements in health care, beginning in the 1960s, created the conditions for a population surge which has meant that many developing countries are today overwhelmingly made up of younger people. The chart indicates that, with a few exceptions, youth bulges are projected to diminish in the next 30 years, which could bode well for greater geopolitical stability. We will be analyzing demographics in more detail later in the '21st Century Investment Themes' series.



- **BRICs As Power Shift Leaders**

One of the interesting aspects of the power-shift is that loose affiliations, such as the BRICs, have actually bonded, finding common ground in their pursuit of national power and economic progress. All the BRICs have large populations, underdeveloped economies and governments that are willing, to varying degrees, to embrace global markets. However, the similarities begin to end there; these are very different countries. China is now an acquisitive, high-investment economy with a powerful competitive position in low-cost manufacturing. India's economy is more closed and insular, with the jewels being a globally competitive software industry and a large outsourcing sector. The Brazilian economy is dominated by agro-exporters, while Russia is overwhelmingly biased to oil and gas. Given that the growth of the BRICs has been built on differences, we should not assume they will behave as a group going forward. In future, they may find they have as much to quarrel about as to celebrate.

- **<u>Capital Stock</u>**

Physical capital stocks will continue to accumulate as incomes rise and savings rates cover depreciation and allow for new investment. However, as the marginal contribution of capital to output declines, the incentive to invest will be reduced. In industrialized countries, savings as a share of GDP will likely decline as population's age and the dependency ratio increases. In developing countries, where capital to output ratios are much lower, capital stocks will rise substantially as the working population increases.

China stands out as an exception; despite a shrinking population, investment is expected to remain high. Historically, developed countries have invested approximately 20 percent of GDP in fixed capital formation each year. Developing countries, on the other hand, have invested significantly more, with investment in some countries peaking around 35–40 percent.

Japan provides a useful case study, as its investment in capital stock can be traced through the different stages of development. Japan's yearly investment rate peaked at 36 percent when its economy was growing rapidly and moderated toward 20 percent in recent years. Over the next forty years, China and India are expected to have the highest average investment rates at 33–34 percent per year. The UK and Germany are projected to invest at the lowest rate, at 17–18 percent per year.

- **Technological Progress and Productivity**

Spreading technology will bolster world economic growth. Developing countries will continue to absorb well established technologies, such as electricity and sanitation. While the largest urban agglomerations and elite firms and individuals in developing countries typically have access to such technologies, rural areas and less favored segments of society often do not.

However, newer technologies such as mobile phones and the Internet are spreading rapidly to developing countries, partly because they are relatively inexpensive and require little government expenditure on infrastructure. Though advanced countries will remain the dominant source of cutting edge technological innovation, a few developing countries with rich pools of highly educated individuals (Russia is a good example) may also innovate at the frontier, and many more developing countries will innovate by modifying technologies to suit local conditions. As described in a comprehensive World Bank report5 on technology and development, "Part of the strong projected performance for developing countries derives from stronger labor force growth, but much can be attributed to technological progress."The potential for technological catch-up is greater when productivity and per capita income are low.

Thus, convergence of the poorest countries will potentially be the most rapid. However, actual rates of catch-up will depend on each country's ability to adopt and adapt technology—a function of openness, educational attainment, communication and transportation infrastructure, governance, and business and investment environment. Thus, two countries at the same level of income may catch-up at different rates depending on these conditions.

- **Exchange *Rate Appreciation***

As productivity in the developing countries increases relative to that in developed countries, wages will increase and the price of non tradable relative to tradable will rise in developing countries, as predicted by the Balsa-Samuelson effect. Additionally, rapid growth in emerging markets will make them more attractive destinations for investment, increasing the capital inflows to these countries. Both of these shifts will put upward pressure on exchange rates in developing countries, and real exchange rates will appreciate.

Though a higher real exchange rate can make the fastest growing developing countries less competitive in basic labor-intensive manufactures, this is, on net, a positive development. A stronger currency implies improved terms of trade and cheaper imports, which both boosts the purchasing power of consumers and lowers the cost of imported inputs for producers relative to the cost of labor. Higher exchange rates can also spur innovation and productivity improvement, since domestic producers must now compete with cheaper imports.

- **Europe's Changing Role**

The next forty years will be a critical period for the European Union (EU) and its 27 members. Germany, the UK, France, and Italy—currently the fourth through seventh largest economies in the world— are expected to grow by only 1.5 percent annually from now until 2050. These four countries' share of G20 GDP is will shrink from 24 percent to 10 percent in 2050.

As economic interests shift away from Europe to favor Asia and Latin America, Europe will likely undergo a difficult and turbulent transition. To ease the strain caused by these changes and to retain their historic influence in the world economy, European nations will increasingly need to conduct foreign policy under an EU banner. In 2009, the total GDP of the EU was over $14 trillion, larger than that of any single country. In 2050, assuming the region follows the 1.5 percent average growth rate of its four largest countries, the EU's real U.S. dollar GDP will increase to $25.8 trillion, placing it among the three largest economies in the world. If they stand alone, Germany, the UK, and France will all be surpassed by China, India, Brazil, and Mexico; Italy will fall even farther behind and be larger than only four other G20 countries.

Despite the recent ratification of the Treaty of Lisbon, however, and the initial success of the single currency among a subset of members, Europeans appears either unwilling or ill-prepared to promote further cohesion. The crisis emerging in Greece—and potentially in other vulnerable countries—has highlighted the shortcomings of a customs and monetary union that still lacks coordinated macroeconomic policies and is far from any kind of fiscal union. Europeans must confront these issues if they are to operate as a credible unified economic block.

- **New Alliances in a More Balanced World**

The economic balance of power within the rest of the G20 will tilt toward emerging markets. Several other emerging economies will add new, authoritative voices to the international dialogue.

Real GDP in Brazil and Mexico is expected to increase by over 4 percent per year, nearly matching the GDP of Japan, today's second largest economy, in 2050; Russia and Turkey are both expected to be larger than present-day China.

Russia, historically a great power, may become a political outlier under this scenario. Geographically the largest country and enormously rich in natural resources, its population in 2050 will be down to 109 million from 140 million today. With China, India, and the United States—not only the world's three largest economies in 2050 but also the world's three most populous—to its south and east, pressure may mount for Russia to increase its economic and security ties with Europe and to promote a balance of power among its large neighbors.

10. PROJECTED GDP RANKING (2015-2020)

This ranking is based on projection by IMF outlook April 2015. In 2015, Top ten countries in nominal terms will be: United States, China, Japan, Germany, United Kingdom, France, India, Italy, Brazil and Canada. In PPP terms, Top ten countries will be: China, United States, India, Japan, Germany, Russia, Brazil, Indonesia, United Kingdom, and France. In top 10, eight countries are common in both methods. Others two are Italy and Canada is in top 10 on nominal basis, while Russia and Indonesia is in top 10 on PPP basis. Top ten economies will share 67.34 percent and 60.99 percent of total global wealth in nominal and PPP terms, respectively.

In both methods, United States and China occupied first two places. US is the largest economy of world on nominal basis where as China is largest on PPP basis. US is ahead of China by $6583 billion in 2015. This margin will come down to $5194 in 2020. China will remain the world's largest economy on PPP basis.

Japan is at third place in nominal and at 4th in PPP ranking. Germany is at 4th in nominal and at 5th in PPP. United Kingdom is at 5th in nominal and 9th in PPP. Ranking of these three will be same in 2020 as of 2015.

India is at 3rd in PPP and 7th in nominal ranking. By 2020, India will be at 6th position ahead of France with GDP (Nominal) of $3444 billion on PPP basis, India will remain at 3rd place.

GDP (Nominal) Ranking (IMF)							
Rank	Country	GDP (Nominal) (billions of $)					Continent
		2015	% Share	2020	% Share	Rank	
1	United States	17968	24.44	22294	23.18	1	North America
2	China	11385	15.49	17100	17.78	2	Asia
3	Japan	4116	5.60	4747	4.93	3	Asia
4	Germany	3371	4.59	4005	4.16	4	Europe
5	United Kingdom	2865	3.90	3852	4.00	5	Europe
6	France	2423	3.30	2940	3.06	7	Europe
7	India	2183	2.97	3444	3.58	6	Asia
8	Italy	1819	2.47	2144	2.23	8	Europe
9	Brazil	1800	2.45	2054	2.14	9	South America
10	Canada	1573	2.14	1958	2.04	10	North America
11	Korea	1393	1.89	1899	1.97	11	Asia
12	Australia	1241	1.69	1516	1.58	13	Oceania
13	Russia	1236	1.68	1792	1.86	12	Europe
14	Spain	1221	1.66	1498	1.56	14	Europe
15	Mexico	1161	1.58	1496	1.55	15	North America
16	Indonesia	873	1.19	1194	1.24	16	Asia
17	Netherlands	751	1.02	941	0.98	17	Europe
18	Turkey	722	0.98	906	0.94	18	Asia

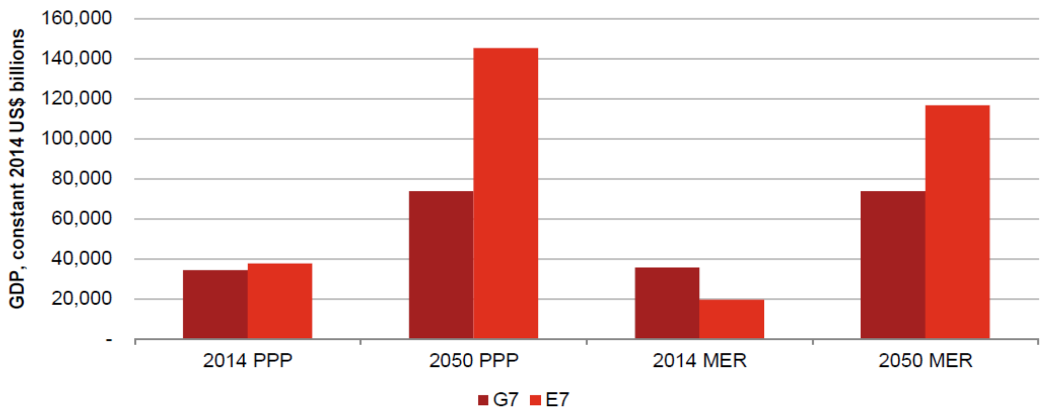
GDP (PPP) Ranking							
Rank	Country	GDP (PPP) (billions of Int. $)					Continent
		2015	% Share	2020	% Share	Rank	
1	China	19510	17.24	28921	19.35	1	Asia
2	United States	17968	15.88	22294	14.92	2	North America
3	India	8027	7.09	12706	8.50	3	Asia
4	Japan	4842	4.28	5512	3.69	4	Asia
5	Germany	3842	3.40	4514	3.02	5	Europe
6	Russia	3474	3.07	3998	2.67	7	Europe
7	Brazil	3208	2.83	3828	2.56	8	South America
8	Indonesia	2839	2.51	4103	2.75	6	Asia
9	United Kingdom	2660	2.35	3251	2.17	9	Europe
10	France	2647	2.34	3160	2.11	10	Europe
11	Mexico	2220	1.96	2844	1.90	11	North America
12	Italy	2174	1.92	2520	1.69	12	Europe
13	Korea	1849	1.63	2408	1.61	13	Asia
14	Saudi Arabia	1681	1.49	2125	1.42	14	Asia
15	Spain	1636	1.45	1990	1.33	16	Europe
16	Canada	1628	1.44	1982	1.33	17	North America

In nominal calculation, top ten countries will contribute 67.09 percent in 2020 compare to 67.34 percent in 2015. In PPP calculation, contribution will be 61.75 percent in 2020 compare to 60.99 percent in 2015.

11. COMPARISION BETWEEN G7&E7

“G7”grouping includes (Canada, France, Germany, Italy, Japan, the UK, and the US, and Australia, South Korea and Spain) and the “E7” – that is, the seven-largest emerging market economies (Brazil, China, India, Indonesia, Mexico, Russia, and Turkey).The below figure shows that, in 2014, the E7 countries have already overtaken the G7 countries in terms of total GDP at PPP exchange rates. This is a measure of the volume of goods and services produced, after correcting for price level variations across countries. Based on total GDP at MERs (Market Exchange Rates), however, the G7 economies are still around 80% larger than the E7 economies. This reflects the much lower average price levels in emerging than advanced economies at current market exchange rates.

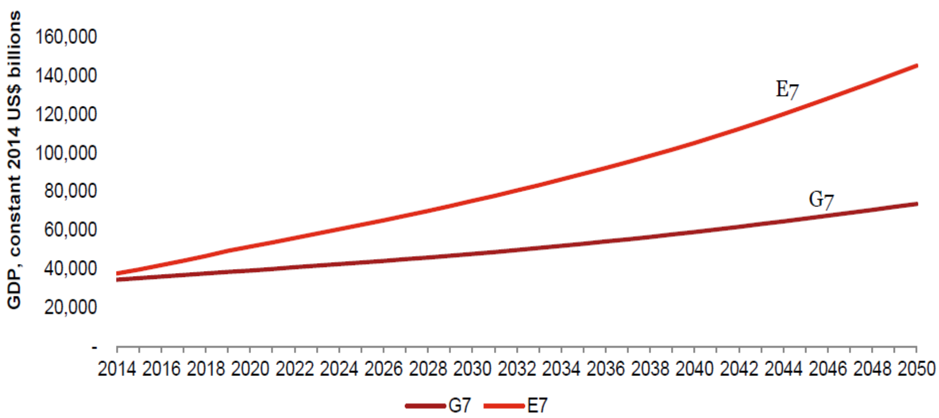
Looking forward, our base case projections suggest that the GDP of the E7 countries will be around twice as high as that for the G7 countries by 2050 in PPP terms, and more than 50% higher in MER terms.



Source: IMF for 2014 estimates, PwC projections for 2050

Figure: Relative size of G7 and E7 economies, 2014 and 2050

Below figure shows the growth paths of the E7 and G7 countries in PPP terms. Again, it shows that the E7 economies have already overtaken the G7 economies as of 2014. This is earlier than the 2017 'crossover date' in our previous model projections in the January 2013 version of this report, which can mainly be attributed to new data on GDP in PPP terms released during 2014 by the World Bank/IMF/UN/OECD's International Comparison Program (ICP). Methodological improvements have been made that suggest lower relative price levels in some major emerging economies relative to the advanced economies. National GDP revisions have also played a smaller part in this shift.

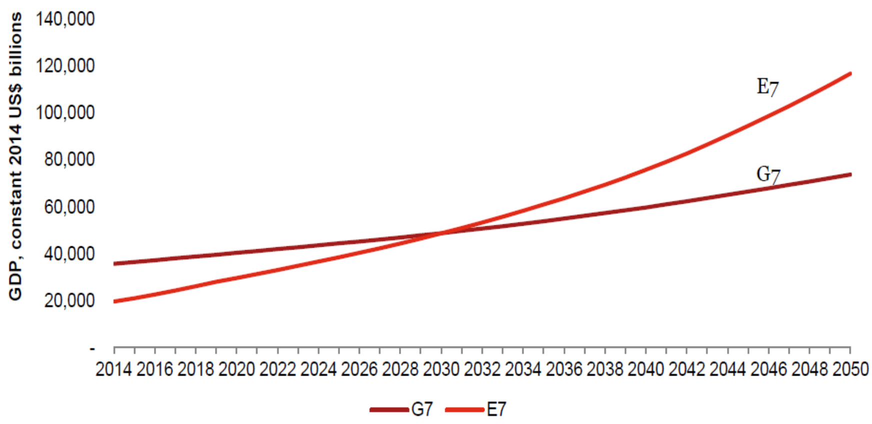


Source: PwC analysis

Figure: E7 and G7 growth paths in PPP terms

It is expected that the E7 economies will continue to be the driving force of the world economy in 2014 – 2050. Our model suggests that the E7 could grow at an average rate of 3.8% p.a. during the period 2014 – 2050, whilst the G7 could grow at an average rate of just 2.1% p.a. over the same time period.

Below figure shows the growth paths of the E7 and G7 countries in MER terms. This shows that the E7 economies were still around 45% smaller than the G7 countries in terms of the value of their output at current exchange rates. Our model projections suggest, however, that the E7 countries could overtake the G7 countries in around 2030 in MER terms.



Source: PwC analysis

Figure: E7 and G7 growth paths in MER terms

As noted above, the difference between the PPP and MER estimates reflects the fact that price levels in the E7 economies are, on average, still well below G7 levels when compared using current market exchange rates. This is a commonly observed phenomenon for many emerging economies. However, past experience with fast-growing countries such as Japan in the 1960s-1980s or South Korea in the 1970s-1990s suggests that market exchange rates tend to converge gradually with PPP rates as economic development continues. This could occur through nominal exchange rate appreciation or relatively high price inflation in the emerging economies, but in either case the result is likely to be long-run real currency appreciation for these economies. We have incorporated this effect into our model through an econometric equation estimated based on past data. This results in a gradual long term convergence with PPP rates that forms the basis for our projections of GDP in MER terms.

12. CONCLUSION

On a number of issues concerning modern Asia there can be no serious disagreement. Its weight in the world economy has clearly got bigger. It can boast two of the BRICs - China and India. It presents major investment opportunities. And it is home to an increasingly significant regional organization in the shape of ASEAN. Asia's rapid growth over the last two decades has also been accompanied by a dramatic reduction in poverty.

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