Anne Krueger
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THE ROLE OF TRADE OPENNESS IN STRUCTURAL CHANGE AND THE RISE OF ASIA

Increasing trade openness and integration has been a hallmark of global economic growth since the industrial revolution, and probably even before. But nowhere has the opening of trade and integration of the economy been more central to successful and rapid growth than in Asia. Moreover, over the foreseeable future, the continuing integration of the Asian economies into the global economy will be essential to sustaining their rapid economic growth.

Naturally, rapid Asian growth has meant structural change for the Asian economies and also for the world. Continued rapid growth will imply further changes. In this paper, I first address some of the similarities and differences across the Asian economies. Next comes a review of the rapid rise of Asia and the role of trade in its rapid growth. Attention then turns to the structural changes in Asia and the global economy that have accompanied that growth. On that basis, it is possible to assess the prospects for Asia and further structural change in the world economy.

The Asian Economies

It is all too easy to regard the Asian economies as being a fairly homogeneous group and they do, of course, have some features in common. But for assessing structural change and future prospects, the differences are significant, and it is useful to think of three groups. Japan has been an industrial economy for many years, with a very high rate of economic growth until the mid-1970s, but with slower growth through the 1980s and then stagnation thereafter. Hong Kong, the Republic of Korea, Singapore, and Taiwan experienced extremely rapid growth for more than three decades, and are now advanced countries with high, but no longer spectacular, growth rates. Japan and the four are advanced industrial economies. The rapidly growing middle income group is the one that has attracted most attention recently. China has been the most prominent, both because of size and of the spectacular growth which started in the early 1980s and, until recently, showed no signs of slowing down – even now many observers believe the currently reported growth rates represent a cyclical phenomenon rather than a break in the trend. India's growth accelerated (from a very slow "Hindu rate of growth" of 3.8 percent from the l950s to the l970s) to 5 percent in the l980s, 6 percent in the l990s, and around 8 percent for the last decade. But China and India still have relatively low per capita incomes, as does Indonesia. These countries plus the smaller Southeast Asian countries (Thailand, Malaysia, Vietnam, Cambodia, Laos and the Philippines), have lower per capita incomes than the East Asian ones, but much greater potential for continuing high growth rates. Also, given their size, the growth of India and especially China is immediately transmitted into changes in the structure of global trade and investment.

For purposes of analyzing probable structural change and its likely effects both on the Asian economies themselves and on the rest of the world, the sheer size of the Chinese and Indian economies makes their outlook crucially important for assessing prospects for Asian economies. Seven countries (China, India, Indonesia, Japan, South Korea, Malaysia and Thailand) accounted for 78 percent of the total Asian population of 3.1 billion and 87 percent of Asian GDP in PPP terms in 2010. They include the two large industrial countries, the two rapidly growing lower middle income giants, and three other countries – Indonesia, Malaysia and Thailand. Indonesia had fairly rapid growth from the late 1960s until the Asian crisis, and has resumed growth. Her large population and growth potential therefore matter. Malaysia and Thailand sustained rapid growth for decades.

For the most part, I shall focus on prospects for China and India. While the advanced countries are important in the international economy and will be discussed to some extent, their rapid growth phase has passed and they are not likely to significantly change the structure of the international economy.

It should first be recalled that the current "rise of Asia" is, to a very great extent, the "reemergence" of Asia. Maddison (2003) estimates Asia's population to have been 68 percent of the global total in 1000 AD, and 55 percent I950, rising again, to 59 percent in 2001. (Maddison, Table 8a, P. 256). He estimates Asia to have had 70 percent of world GDP in 1000 and 18 percent in l950, a precipitous decline. Asia's population grew to 38 percent in 2001 (Table 8b).

The drop in per capita income relative to the rest of the world was also precipitous: excluding Japan, Asia's per capita income in ppp terms was about $575 in 1600 and $634 in 1950 while for the world as a whole, it is estimated that per capita incomes rose from $566 in 1500 to $2,111 in 1950.[1] Hence, Asian per capita incomes had fallen from slightly above the world average in 1500 to only 30 percent of the world average in 1950. Moreover, while the growth rate of Asian per capita incomes accelerated from 1950 to l973, the growth rate of world per capita income also rose, and by more ($1226 in Asia in 1973 contrasted with the world's average of $4091). Hence, Asia's relative per capita income had fallen still further by the 1970s.[2]

As is well known, the situation since then has changed markedly. By 2001 the Asian average (still excluding Japan) was $3,256 while the world average was $6,049. With rapid growth during the 2000-2010 decade, the gap has closed even more.

Since the l950s, more and more Asian countries have experienced accelerated growth of real incomes (and falling rates of population growth). Japan was already a developed country, albeit a relatively poor one, in the early 1950s, but then began growing rapidly. By the late 1950s, the Taiwanese economy's growth had accelerated. South Korea, Hong Kong and

[1] All numbers in this paragraph are in 1990 international Geary-Khamis dollars). See Maddison (2003) for data for individual countries.

[2] The Asian Development Bank's estimates differ from Maddison's. The ADB puts the Asian share of the world economy at 60 percent in 1750, 20 percent in 1950 and 28 percent in 2010. See ADB (2011), P. 19.

Singapore began experiencing rapid growth by the beginning of the 1960s. Thailand and Malaysia followed soon.

But the big change, from the viewpoint of the structure of the world economy, was China. Until the 1980s, the Chinese economy had been inner-oriented, with very little foreign trade. China's economy and that of the rest of the world were virtually independent. In the 1980s, however, Chinese economic reforms began, and Chinese growth accelerated. Growth was from a very low base, however, and for more than a decade, China could grow rapidly with very little effect on the rest of the world. By the turn of the century, China's growth of output and exports had continued for a sufficiently long period so that interdependence between China and the rest of the world was increasing rapidly.

Meanwhile, Indian economic policy makers had adopted policies of import substitution right after independence, and India's share of world trade fell markedly over the next two decades. India's growth of per capita income was also relatively slow. Then, in the early 1990s, policy reforms went far toward changing the growth prospects of the Indian economy. By the early 2000's, Indian growth had accelerated enough so that there was talk of equaling or exceeding the Chinese growth rate, although except for one quarter that did not quite happen.

Indian policy makers did not shut the country off from the international economy to the extent the Chinese did. But policies of import substitution discouraged exports, and India's share of world trade, which had been around 2 percent right after the Second World War, had fallen to about 0.5 percent by the l980s. But after policy reforms, Indian exports began growing rapidly, and India's share of world trade (and world GDP) began rising, reaching over 2 percent in 2010.

The rise of India and China alone would have been sufficient to change the structure of the world economy and international trade. But other countries, including Vietnam, Indonesia, Thailand and Malaysia, were growing at rates above those in the non-Asian world.

At the same time, growth rates of Japan, South Korea, Taiwan, Singapore and Hong Kong decelerated – by the late 1980s in the case of Japan and in the 1990s for the others. The Japanese growth rate slowed significantly after 1973, although it was still well above that in the rest of the world. But growth in Japan then virtually ceased after 1990. The other East Asians continued their rapid growth into the 1990s, and while they resumed growth after the Asian crisis, they did not again attain the strikingly high rates of earlier decades. Much of this was "natural" as the scope for rapid gains enabled by "convergence" with the rich countries fell. With the exception of Japan, however, the early starters have maintained growth rates well above the world average in the first decade of this century.

The growth rates of these countries, combined with the very high growth of India and China were sufficient to more than offset the reduction in growth rates of Japan and the East Asians. Although some Asian countries have not yet experienced sharp accelerations in growth, Asia as a whole is still growing at a rate well in excess of the rest of the world. And given the size of India and China, it is likely that that more rapid growth will be sustained as long as those two countries grow rapidly. Even with some slowing down of growth, the increased importance of the two giants would assure that Asia as a whole will have a rising share of world output and trade.

Trade and the Rise of Asia

World trade was a very small fraction of world GDP until at least the twentieth century. For 1820, Findlay and O'Rourke (2007, P. 510) estimate that merchandise exports were about 1 percent of world GDP. Even among European countries that practiced free trade in the late nineteenth century, they estimate that as late as 1870, merchandise exports were only 10.0 percent of European GDP. On the eve of World War 1, merchandise exports were 7.9 percent of world GDP.[3] A major part of the explanation for these low numbers lies in the high transport and communications barriers relative to the early 21st century.

Nonetheless, it may be significant that the major Asian countries – Japan, China, and Korea all chose to insulate themselves from the international economy and India, the other large one, was a British colony.[4] Japanese policy reversed after the Meiji reforms in the mid-1800s, while the others preserved their insulation for another century. As already noted, In the 1950s the Chinese economy was virtually entirely closed to trade, at least with the West, and it remained that way until the early 1980s. Taiwan opened up her trade in the mid-1950s. South Korea followed policies of import substitution until 1960, with a very low rate of economic growth for a period of postwar reconstruction, but then adopted an outer-oriented trade strategy in 1960, and the growth rate rose sharply. South Korean exports were 3 percent of GDP In 1960, and rose rapidly after policy had been altered. By the late 1980s, South Korean exports were 40 percent of GDP. By 2010, South Korea's exports were 52 percent of GDP and South Korea was the 8th largest exporter in the world, despite the fact that the country had only 48 million people.[5]

Hong Kong and Singapore, both city-states, had open trade policies by necessity and experienced very rapid growth of GDP, with exports a "leading growth" sector. Thailand and Malaysia also opened their economies significantly in the l970s, and their growth rates, too, accelerated.

Both because the early openers were relatively small and because they were poor, their rapid rise was hardly noticed until the 1990s. The biggest change, China, started in the early 1980s, as the Chinese opened up their economy. Exports rose from 1.5 percent of GDP in exports in l973 to 2.3 percent in 1992 and 4.9 percent in 1998. Chinese export earnings rose

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[3] World exports were only 5.5 of world GDP in 1950, as they had fallen from a peak of 9.0 percent in the Great Depression and, despite some recovery late in the 1930s, fell further during the Second World War. (Findlay and O"Rourke, P. 510).

[4] It is of interest that India's trade was larger as a percentage of GDP than the other countries', and India's growth rate was also somewhat faster (about 0.5 percent annually until 1914 compared to zero growth in per capita income for the others.

[5] South Korean data are taken from International Monetary Fund, International Financial Statistics Yearbooks, 1996 and 2011, Korean Country Pages.

from US $21 billion in 1982 (the first year for which they were reported in IMF publications) to $69.5 billion in 1992, and US$1.6 trillion in 2010. As a share of world exports, this represented an increase from a negligible fraction in l980 to 10.6 percent in 2010. Thus, China emerged as a systemically important trader by the first decade of the 21st century. If, as expected, the Chinese economy and Chinese trade grow at rates above the world average, Chinese importance will increase still further, as will be discussed later. Moreover, since China is already a large trading nation, continuing increases in share can be expected even if there is no further increase in the share of exports in Chinese GDP.

The Indian economy, while not centrally planned, was heavily controlled by the government until the 1990s. Import-substitution policies were followed until the l980s, in the expectation that domestic industries could develop and reduce or eliminate the need for imports. As late as 1991, Indian exports constituted only 5 percent of GDP and, as already noted, India's share of world exports had fallen to just over a half a percent of global exports. In the 1990s, economic policy reforms addressed the inner-oriented nature of the trade regime. A devaluation, and subsequent adjustments in the exchange rate, provided enhanced incentives for exports. Moreover, quantitative restrictions and prohibitions on imports of intermediate and capital goods enabled potential exporters to obtain needed items at lower cost, both because they could import and because domestic producers of import-competing commodities were confronted with competition. In addition, tariffs were sharply reduced, on intermediate and capital goods imports, and then early in the last decade on consumer goods imports.[6] The profitability of producing for the domestic market (often with monopoly positions) was greatly reduced and that of producing for exports increased markedly. Export earnings began growing rapidly, with an average rate of growth of about 20 percent, and thus rising from 5 percent of GDP immediately after the start of reforms to 21.5 percent of GDP in 2010.[7]

Acceleration of the Indian growth rate followed these reforms, with near-Chinese rates of growth in the 2004-08 period. How much of the slowdown in growth after 2008 was the result of the worldwide recession, and how much was attributable to the economy having been growing at an unsustainable rate is an open question. But what is not in question is that Indian exports boomed. By 2010 India's exports of goods and services constituted 21.5 percent of GDP. This contrasts with 6.6 percent in 1980. In U.S. dollar terms, Indian exports had risen from $11.2 billion in 1980 to $349 billion in 2010.[8]

[6] India lowered her tariffs unilaterally, and has lowered the rates bound under WTO rules to a far smaller extent. This has been a bone of contention between India and her trading partners during WTO multilateral tariff negotiations in the Doha Round.

[7] The import content of Indian exports is much lower than that of Chinese exports. Hence, the difference in shares of exports in GDP between the two countries overstates the difference in their relative importance to their respective economies. Even so, exports represent a significantly larger share of Chinese GDP than they do of India's GDP.

[8] Indian exports of services (software, IT, etc.) grew much more rapidly than merchandise exports. Indeed, Indian growth was unusual in that the manufacturing share of GDP did not rise as it had in many other countries at India's stage of development. See Krueger (xxxx) for fuller analysis. Reduction in the barriers to merchandise exports,

An open trade regime has been central to the success of the rapidly growing countries of Asia (and elsewhere). The experience of South Korea demonstrates why opening up to trade was so important. In the 1950s, the country had followed policies of import substitution, as did most developing countries. The results were similar to those elsewhere. Most industries were heavily protected from competition from abroad and faced little competitions domestically. More than 70 percent of the population lived in rural areas, and the land/man ratio was estimated to be the lowest of any country. Despite postwar reconstruction after the end of the Korean war in 1953, which usually offers opportunities for rapid growth, the Korean economy failed to achieve more than 5 percent in any year between 1953 and 1960, while the inflation rate was among the highest in the world, there was chronic "foreign exchange shortage" as multiple exchange rates were systematically overvalued, and large current account deficits were financed by foreign aid.

Export earnings grew very slowly in the 1950s in large part because producers found it far more profitable to sell in the domestic market than to compete overseas, while simultaneously they were unable to obtain needed inputs at the same prices that overseas producers paid. Foreign exchange was scarce as the currency was overvalued, and there was a sizeable black market. By 1960, exports constituted just over 3 percent of GDP while imports were 13 percent of GDP. The difference was financed largely by foreign aid, as the domestic savings rate was close to zero. Korea had one of the lowest per capita incomes in the world, and the outlook was bleak.

By that time, it was recognized that the country had very poor growth prospects under the existing policies. South Korea was not well endowed with any primary commodities, although 88 percent of exports were primary commodities. The country could not hope to grow rapidly isolated from the world economy. So, over a period of about 5 years, policies were greatly altered. The exchange rate was adjusted to a more realistic level and then incentives for exporters were maintained in the face of domestic inflation by adding premia to the exchange rate between formal devaluations to keep exporters' real proceeds per US dollar relatively constant. Exporters were permitted to import needed goods without paying any duty and without delays. The protection accorded to producers of import competing goods was reduced, so that incentives for export production were at least as great as those for import competing production.

The results were astounding. South Korea's growth rate shot up, as did exports. From $30 million in 1960, exports reached $100 million by 1964, and kept on growing at an average annual rate of around 40 percent for 3 decades. In 2010, exports were US$464 billion, or 52 percent of GDP.[9] To be sure, other reforms also facilitated rapid growth; for example, a major fiscal reform in 1964 enabled a permanent reduction in inflation rates to single digits. While the

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especially of jgoods using high proportions of unskilled labor in production, could release further export potential for India.

[9] Data are from International Monetary Fund, _International Financial Statistics Yearbook 2011._ *Country pages. Because some imports are used in producing exportable goods, the 52 figure may slightly overstate the importance of exports in GDP.*

financial markets were not fully liberalized, the bite of credit rationing (at negative real interest rates) was reduced and real interest rates for depositors and borrowers became positive, if not market-clearing.[10]

Reasons for this result were several. First, given the very low productivity of the rural population, the movement of workers from farm to industrial jobs automatically resulted in an increase in average labor productivity. For several decades, the movement of people out of agriculture into the industrial labor force contributed significantly to overall growth. In addition, industrial productivity grew as workers gained experience (and as educational attainment of the population increased). Second, many of the inefficiencies associated with strict foreign exchange regulation, black markets, and other aspects of the earlier regime were reduced or eliminated; the rate of productivity growth also increased because low-cost firms were enabled to increase their share of output through exporting while high cost firms either failed or lost share. Third, the focus of attention of most of the population shifted from obtaining needed permits and licenses to producing more efficiently. Releasing producers from allocating time and resources to competing for bureaucratically restricted favors undoubtedly resulted in increased productivity. Even the bureaucracy was spurred to facilitating production and exporting. As growth accelerated, the importance of access to the international market to learn about innovations and trends in other economies became increasingly important.

When Korea embarked on an outer oriented trade policy, the structure of the economy was fairly simple, but also heavily biased toward an abundance of unskilled labor and a severe shortage of capital (and land). Opening up the economy to trade enabled rapid increases in production and exports of goods, such as textiles and apparel and shoes, which used relatively large amounts of unskilled labor. Workers migrated from the countryside at a rapid rate, and gained experience in these export industries. Over time, the savings and investment rate increased, and Koreans began “moving up the value added chain”, as the experience of the industrial labor force increased and the supply of rural labor willing to shift to industrial activities dried up. With a higher rate of investment, which had risen from around 13 percent of GDP in the early 1960s to over 35 percent by the mid-1980s, production shifted toward goods using more capital relative to labor, and employing more skilled workers. That process continues to this day, as focus in the country has turned increasingly to strengthen capacity for innovation. Without question, the Korean economy has been transformed into an advanced economy, with a per capita income in real terms more than 8 times what it was in the early 1960s

Today, South Korea is a rich country, and the economy is heavily integrated with the global economy. To achieve that goal, it was necessary to do much more than open up the economy, but success was certainly dependent on trade opening as well. As world economic growth has continued, the complexity of modern economies has increased, and with it, the importance of trade to enable producers to obtain the goods that most closely fit their requirement in terms of price and quality has increased.

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[10] It can be persuasively argued that failure to liberalize financial markets by the 1980s was a major contributor to Korea’s financial crisis in 1997-98.

The Korean story is unusual because of both the very poor initial circumstances in which the Koreans found themselves and the extent of their success. But the need for an open economy to enable rapid growth has been the same elsewhere. It was and is certainly true of the other East Asian economies. Hong Kong, Singapore, and Taiwan all had very rapid growth of exports as a key feature of their rapid growth years. Despite China's size, rapid growth did not take place until China opened up the economy. While it is possible that the percentage of GDP accounted for by exports and by trade may not rise and could even fall somewhat in future years, trade will continue to grow rapidly as long as the Chinese growth rate is above that of the rest of the world.

While India's export growth has not been as rapid as that of China, the potential for further growth is probably even larger. Exports of services have grown rapidly, but to date, India's exports of goods intensively using unskilled labor in production have not grown as rapidly. Bottlenecks to more rapid export growth (in a country with 70 per cent of the population still in rural areas) include relatively poor infrastructure and rigid labor market regulations which discourage the employment of unskilled workers. Indeed, the increase in industrial production in India from the beginning of reforms in the early 1990s to the middle of the last decade came with virtually no increase in industrial employment and was accomplished with capital deepening. This means that were India to improve infrastructure significantly and liberalize the labor market, there would be great scope for accelerated export growth, especially of unskilled labor intensive manufactures. Indonesia, and some of the other populous labor-abundant countries also have potential to accelerate their real growth rates by increasing export of goods using relatively large amounts of unskilled labor.

When the Chinese began accelerating their exports of unskilled labor intensive goods, the Japanese, and later the other advanced economies of East Asia were "moving up the value added chain" and reducing their production of these commodities. Their wage rates had risen to a point where they no longer had comparative advantage in goods using lots of unskilled labor in production. Chinese development has proceeded sufficiently far that the process of moving up the value added chain seems to have started. As such, a part of the expansion of exports of goods intensive in the use of unskilled labor by India and other Asian countries at earlier stages in their growth process can be expected to be offset by reduced Chinese competition in these markets. Already there are reports of Chinese exporters shifting some of their production offshore to countries such as Vietnam.

Trade barriers in almost all of Asia have fallen sharply, although there is scope for further trade liberalization, especially in agriculture and services. Japanese quantitative restrictions on imports of manufactures were virtually all removed by the 1960s; Taiwan, South Korea, and Singapore all have very little protection remaining on manufactured goods.[11] As already noted, India's reforms included the removal of quantitative restrictions on imports and huge reductions in applied tariff rates with the consequent rapid growth of exports described

[11] Japan and Korea both have very high rates of protection on agricultural goods, and have significant barriers to trade in commercial services. Reducing these barriers would permit more rapid growth in both countries.

earlier. Other Asian countries have lowered their tariff walls somewhat. So, while, exports have risen rapidly in the fast-growing Asian countries, imports by those countries have also risen.

One result of trade liberalization has been that intraregional trade within Asia has grown even more rapidly than overall trade. In 2000, about 49 percent of Asia's exports were destined for other Asian countries.[12] By 2010, intraregional trade had risen to 58 percent of total Asian exports. That figure was still below intraregional trade in the European Union (over 70 percent of total EU trade), but above that of North America. The increasing importance of intra Asian trade reflects four factors: the increasing openness of the Asian economies; the increased importance of those economies; increasing resort to placement of production of specific parts and components in countries with comparative advantage best suited to those components; and, finally, preferential trading arrangements within the region. The third factor represents the "chopping up" of the value added chain, a worldwide phenomenon in which Asia has participated. South Korea's largest trading partner for her exports, for example, is now China. Much of that trade represents the export of sophisticated items for assembly in China.

The fourth factor, preferential trading arrangements, is increasing over time. The best-known arrangement is that of ASEAN, but almost countries have entered into, or are negotiating, some agreements. For example, South Korea is working to establish a network of free trade agreements to attempt to insure that the country's exports do not face trade barriers abroad with any of her major trading partners. Already, free trade agreements are in place with ASEAN, Chile, the European Free Trade Association, the European Union, India, Peru, Singapore and the United States. An agreement has been signed with Turkey, and negotiations are under way for Canada, the 6 Gulf Coast countries, Mexico, Australia, New Zealand, Colombia, Indonesia and China.[13] Many other Asian countries are following the same pattern, although it is probably fair to say that the large trading countries are less far along the path of multiple preferential trading arrangements than are the smaller ones.[14]

Trade and Structural Change in Asia

The increasing importance of Asia in the global economy and in global trade has been the single most important structural change in the international economy in the past decade. While Asian economies and Asian trade were growing rapidly before that, the base (except for Japan) was small enough so that rapid growth did not really represent a structural change for the global economy (again, except for Japan). Japan's emergence as a modern industrial trading nation had been a major feature of the l970s and l980s, but the slowdown in that country's growth meant that there was little notice of Asia's emergence in the 1990a.[15]

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[12] World Trade Organization (2011), Appendix Table A2.

[13] There are a number of possible additional agreements under study, including Japan.

[14] Several preferential trading arrangements among South Asian countries have been negotiated and some implemented but the slow pace of agreed upon implementation and the large number of exceptions in these arrangements have made them less of a factor than the ASEAN preference s.

[15] The breakup of the Soviet Union and the emergence of Eastern Europe and the CIS in the l990s was headline news and may have distracted attention somewhat from Asia's rise.

But by 2000, China's export-led growth had been proceeding for almost two decades. China's entry into the World Trade Organization appears to have resulted in acceleration in that already-rapid growth. By 2010, China was exporting US$$1,568 billion, up from US$249 billion in 2000. The country's share of world exports had increased from 3.9 percent at the beginning of the decade to 10.3 percent ten years later.

Future Structural Changes

China's size and her virtually unprecedented (and certainly unexpected) rate of growth focused world attention on China, So, too, did the Chinese need for raw materials and the large trade surplus with the United States. But other Asian economies were also increasing their role in the world economy. India's exports rose, as already noted, from $42.4 billion in 2000 to $220 billion in that decade. Malaysia's rose from $98 billion to $199 billion, and Thailand's from $69 billion to $195 billion. Even Vietnam's exports rose from $14.4 billion in 2000 to $71.1 billion in 2010, and several other small (by Asian standards) exporters had large increases in their exports. Emerging Asia's share of world exports rose from 9.6 percent to 15.8 percent a decade later, while exports from advanced countries in Asia rose from $1,327 billion to $2,065 billion. While their rate of growth of exports was far less rapid, it was from a larger base, and the overall share of Asia in world exports rose from 30.4 percent to 37.2 percent. Indeed, the advanced economies' share of world trade, not including Asia, fell from 65 percent in 2000 to 47 percent by 2010.

China's size has led to a focus on the emergence of that country. Not only is overall Chinese (and Asian) trade of increased and increasing importance, but issues are arising with respect a number of goods. Some producers of unskilled labor-intensive manufactured goods in other advanced countries have sought redress through WTO processes. China's demand for raw materials has been large enough and grown sufficiently rapidly to lead to concerns about future supply and demand, and therefore prices, of some primary commodities.

It is likely, however, that China's export growth will not be so rapid in the future as it has been. As already mentioned, Chinese producers are beginning to offshore production of some labor-intensive commodities. Perhaps even more significant, the share of consumption in GNP is, as noted earlier, well below levels that appear warranted and the authorities are gradually adopting measures to encourage a large reliance on the domestic market for future growth. As Chinese real wage rates rise and the supply of unskilled labor from rural areas diminishes, these trends are likely to continue.

For assessing the order of magnitude of future structural changes, a crucial question is whether the growth of the Asian economies and their trade will be sustained. While the future can never be known, one can point to certain factors that will play a key role in providing the answer, assuming that major unforeseen events (geopolitical, for example) do not take place.

Based on the "known unknowns", the question can be divided into several interrelated parts. The first two parts focus on events taking place within the Asian economies while the third concerns the evolution of the international economy.

Turning first to the Asian economies themselves, one must ask what will happen to growth rates, first, if their policy makers satisfactorily confront the economic challenges with which they are faced. Second, the question of the extent to which these challenges will be met is discussed. But the evolution of the Asian economies will also depend on the evolution of the international economy. Here, issues can be raised about prospective growth rates in advanced countries and non-Asian developing countries, assuming that countries' policies concerning the international economy continue on their present path. Finally, there are questions about the future of the open multilateral trading system.

I turn to each of these in turn, but must first note three important things. First, any country's growth prospects are better if its own economic policies are sound. Second, policy stances that permit growth at early stages of development may be inappropriate to sustain growth beyond middle income status. Third, all countries' growth prospects will be improved if the open multilateral trading and financial system is healthy, and their prospects could be greatly impaired if protectionist forces were strengthened.

Growth Prospects for Asia. To date, countries that have experienced rapid economic growth have found that, after they have digested the benefits of trade opening and of rural-urban migration, the growth rate inevitably slows down. This happened to Japan in the 1970s, and to Hong Kong, Korea, Singapore and Taiwan in the 1990s. How much scope there is for rapid "catch-up", or "convergence" in Asian countries is a matter of judgment.

Turning first to the advanced industrial economies in Asia, slowdown from the rapid pace of earlier decades has already occurred, but is likely to be further experienced because of demographic factors. As is well known, the industrial countries of East Asia have very low rates of population growth. Indeed, for Japan, the labor force is already falling in numbers. It is projected that Japan's total population will decline from 127 million in 2010 to 109 million in 2050, while the drop in the labor force will be even greater. The other advanced Asian countries are not far behind. South Korea's working age population is projected to peak in 2018 and its total population in 2029.

Slowing labor force growth has two negative impacts on the overall growth rate of GDP. First, the very fact that labor becomes scarcer means that more capital investment will be needed (assuming no change in the rate of innovation) as additional capital is needed to substitute for labor. Second, as life expectancy increases, the fraction of the population that must be supported by the labor force rises. The fiscal challenges of supporting an older population may drain private savings (and result in deteriorating fiscal situations) and thus hinder growth. If old age is supported privately, the savings rate will likely fall as the elderly consume out of earlier savings.

There can be certain offsets. Policies that increase the labor force participation rate (child care, immigration, a higher retirement age) can reduce the negative effects of these factors. Likewise, incentives for innovation which enhance the productivity of labor and capital can provide an offset to some degree. But the world as a whole is facing demographic challenges of a type not heretofore encountered in the industrial age and it will take enlightened policy responses in the countries undergoing demographic transition to offset the negative effects of population aging.

In Asia, not only are the advanced countries experiencing or about to experience demographic problems, but some of the emerging markets are facing challenges before they have reached industrial status.[16] China's demographic prospects are much the same as those of the advanced economies, despite her still-low level of per capita income. It is estimated that China's working age population will peak in 2018 and the labor force in 2029.

India's demographic profile is different, as population and labor force are projected still to be growing in 2010. And there are some "young" Asian economies, including Pakistan and Afghanistan. But overall, the Asian economies will experience much slower growth of the labor force than they have done over the past half century.

In itself, slower population and labor force growth will result in a retardation of real GDP growth. In addition, for the countries that have been growing extremely rapidly, the benefits of urban-from-rural migration will slow as the supply of would-be migrants decreases as a percentage of the total population. The gains to be had by catch-up will also slow. How soon this will occur, how much of a slowdown there will be, and whether it will be relatively sudden (as it was in the cases of East Asia) or more gradual will depend in significant part on the policy responses of the Asian countries to their domestic economic challenges.

Concerns have been raised that the "middle-income trap" might take place for some of the rapidly growing Asian economies.[17] Fear that such a trap might occur is raised because, while some middle-income countries have successfully transitioned to advanced economies, other countries have experienced serious slowdowns in their growth rates and appear to be stuck, at least to date, in a "middle income trap".

In general, history shows that continuing growth is never assured: even as the advanced economies have grown, policy challenges have arisen which, when unmet, reduced or even stifled future growth. Japan has been struggling for two decades with problems that are as yet unresolved, especially in the services and financial sectors. Argentina was regarded as having an advanced economy at the beginning of the last century, but is now middle income, and has not resolved the fundamental policy challenges that would enable achievement of advanced economy status.

For the rapidly growing middle income countries of Asia, the challenge will be to adapt policies to the needs of their economies as they grow. Policies that delivered rapid growth when much of the population was rural and could move into unskilled labor-intensive jobs can no longer deliver the same rate of growth: improvements in the quality of human capital, increasing the flexibility of labor markets, upgrading infrastructure, and much more is required and is an ongoing challenge. The relative importance of reforming different growth-inhibiting policies varies, of course, from country to country.

[16] See Kohli et al (2011), Chapter 3 for a fuller discussion of demographic prospects.
[17] See Kohli et al. (2011), Pp. 48 ff. for a fuller discussion of the "middle income trap".

Even with a significant slowdown in growth, however, Asia's role in the global economy is likely to increase for some time to come. It is likely that the countries with lower per capita incomes can maintain above-average growth rates for several more decades if they sustain appropriate economic policies. And, for some (especially including most of South Asia but also a few others), growth of exports and of trade is likely to result in increasing shares of exports and imports in their GDPs for a considerable period in the future. India, for example, still retains an average tariff on manufactures of over 10 percent and neither agricultural trade nor trade in services has yet been significantly opened up. Even if the share of exports in Chinese GDP does not increase, the Chinese share of world trade would almost surely continue to grow as long as China's GDP growth rate remains above that of the rest of the world.

As already mentioned, a major challenge for China is to shift the sources of demand somewhat more toward the domestic economy. This is essential not only for China's economic growth, but also to reduce the risk of a reemergence of global imbalances as a major problem. Chinese consumption is estimated to have been only 35.5 percent of GDP in 2009 while net exports were 12.4 percent of GDP, with a commensurate current account surplus. Such a low share of consumption is historically unprecedented for any sustained period of time, and increasing it would clearly increase the welfare of China's citizens.

Kohli et al (2011 P. 47) estimate that overall Asian growth will average 6.7 percent in the decade to 2020, 5.9 percent in the following decade, and slow to a still very high 5.3 percent in the decade prior to 2050. In their estimates, global growth over the same period would slow from 4.6 percent in the 2010-2020 decade to 4.0 percent in the 2040s. That would result in Asia's share of world GDP increasing from 27.7 percent in 2010 to 33.7 percent in 2020, 39.9 percent in 2030, and 51.2 percent in 2050.

While these estimates depend both on Asian and on world growth, they give a broad picture of coming structural shifts. They would, as already noted, require continuing policy reforms in Asia as development proceeds. Among these reforms, a greater contribution of domestic consumption to growth is high on the list. But other reforms, many specific to individual countries, would also be required.

It should be remembered that, as Asia's share increases, so, too will Asia as a market. And some of the increase in exports of countries at earlier stages of development would replace the exports of unskilled-labor intensive goods from China.

Needed Global Policies

But achieving the rates of growth envisaged in the Kohli report would also require adjustments in the global economy. These will be needed in individual countries. Needed adjustment for changing demographics has already been pointed out. In many countries, including especially the Eurozone, fiscal challenges loom large.

A major challenge for all is to maintain the open multilateral trading system and, indeed, to strengthen it. Trade frictions are greater when there are new entrants rapidly gaining share. If those frictions were to result in competitive increases in trade barriers, the prospects both for

Asian economies and for the advanced economies would be greatly diminished. Indeed, a vicious circle in which heightened trade barriers in advanced countries resulted in reduced Asian and world growth rates and retaliation with increases in trade barriers in the emerging markets with further diminution of growth rates could well result. The structural challenges arising from the emergence of Asia are small relative to what might happen should protectionist pressures. I return to this issue later.

But trade frictions themselves are greater when growth rates are low. It must be recognized that the financial crisis is by no means over. Some policy challenges are country-specific. But if the global economy is to grow at anything like the rates suggested by Kohli et al, there are numerous problems concerning the international financial and trading system that must be satisfactorily resolved.

These problems concern global economic governance generally, the capacity and authority of the International Monetary Fund to address global imbalances, international financial coordination on key issues, and the open multilateral trading system.

While time does not permit a full analysis here, a few points must be made. First, growth at the sort of rates envisaged by Kohli et al will certainly entail further increases in international interdependence. Trade in goods and services as a percentage of global GDP would increase, both as an efficiency-increasing measure that would enhance growth and as a result of rapid growth. To that end, the role of the World Trade Organization should be strengthened, both to cover new issues (such as export restraints on commodities in times of high world prices and environmental concerns), and to move further toward efficiency-enhancing opening of trade in services and in agriculture.

In contrast with the urgent need for a strengthened open multilateral trading system, the Doha Round of trade negotiations is languishing, and protectionist pressures seem on the rise in many countries. Failure to complete the Doha Round has greatly increased the difficulty of addressing the new issues and prevented realization even of the gains that would have occurred if Doha had concluded on the basis of agreements reached as of July 2008.

Issues on the financial side are equally in urgent need of resolution. The financial crisis certainly indicated the need for increased incentives for financial institutions to improve their evaluation of risk-reward trade-offs. Some measures to improve their incentives to do so, such as increased capital adequacy requirements, have already been put in place, but much more remains to be done. But a country that acts unilaterally runs the risk of handicapping its financial institutions compared to those in other countries. The need for a coordinated set of actions beyond Basel III seems evident. The need for some degree of coordination of policies concerning resolution of banks with multicountry ownership became apparent during the financial crisis, but as yet no agreement has been reached.

Moreover, there is a risks that global imbalances might once again lead to overly aggressive risk-taking with low or negative real interest rates. The IMF has no more authority now than it did a decade ago to do more than comment on risks, unless a country seeks its financial support.

As this brief sketch of major issues suggests, the international community has much work to be done to strengthen the international system both on the trade and on the finance side. To improve the functioning of the system, agreement has to be reached both on the ways in which problems will be addressed and on the procedures to reach agreement.

In that regard, the rise of Asia means that Asians must fully participate in the process of decision-making, and recognize their stake in the international economic institutions. Until recent years, for understandable reasons, Asians (and policy makers in most other developing countries) tended to view themselves as bystanders, benefitting from reduced tariffs in industrial countries and the expansion of world trade, for example, but not engaging in multilateral trade negotiations. With Asia's increased importance, that is no longer a viable strategy. Moreover, Asians need to recognize that a healthy international economy is in their own self-interest and they have an interest in the system as a whole above and beyond their concerns about conditions governing their own production and trade.

Issues concerning commodities (agricultural, mineral, and energy) are ones to which the international community will need increasingly to turn its attention in the coming years. Here, the importance of Asia, and especially China, as a consumer of raw materials and implies that meaningful understandings cannot be reached without Asia's full participation. Yet, it is in Asia's as well as the world's, interest that these issues be addressed and "rules of the game" or other agreements be negotiated. If countries can, for example, restrict or prohibit exports in times of high prices to shelter their domestic economies, such restrictions would adversely affect all commodity importers, advanced and emerging. In addition, failure to reach such understandings would surely lead to increased price fluctuations for the affected commodities to the detriment of the efficiency of the entire world economy.

Asia's rising share will also affect the global environment. Both because of her rising share and because satisfactory measures to address the issues will be less likely to happen in advanced countries if Asians do not participate, ways must be found to enable global understandings on environmental issues that address Asian (and other developing countries') concerns about environmental measures that might unduly restrict their growth and simultaneously enable reassure industrial countries' producers that environmental regulation will not unfairly handicap them in the international economy. This will be important for the world's environment, but is also necessary to gain continued support for the open multilateral trading system.

Likewise, Asians (Japan excepted) have tended to view themselves as borrowers from the International Monetary Fund and saw the Fund's policies reflecting the interests of the advanced countries. That, too, must change, as the healthy functioning of the international financial system is strongly in their interest. The impact of the Euro crisis on Asia is ample demonstration of the importance to Asia of a well-functioning and stable international financial system.

Fully supporting the international economic system requires, of course, that Asians have a say and a stake in governance commensurate with their increased importance in the world economy. At the formal level, of shares in the voting structure, that is happening, but proceeding but very slowly. It also, however, calls for constructive participation in academic and policy discussions about the functioning of the system.

Supporting and strengthening the system, both financial and trade, also requires open discussion and debate of the need for change and types of changes that might prove beneficial. To date, fewer Asians have participated in policy discussions (including op-ed articles, contributions to policy-oriented journals, and conferences) than will be needed in the future.

CONCLUSIONS

Sustained Asian growth will continue the trend in structural changes in the international economy that have characterized the past several decades. The rapid growth of Asia is good news for Asia and the world. It is in the world's interest both because the rich world can ill accept poverty of the sort that characterized many Asian countries in earlier years, and because larger Asian markets enable further specialization and growth in the advanced countries as well. It is in the interest of the Asian countries themselves for obvious reasons. Higher living standards, more resources with which to confront national problems, and other benefits result.

But enabling Asia to sustain growth rates will require actions both on the part of Asians and on the part of the rich countries. For Asia, the challenge includes recognition of those policies that diminish the prospects for continuing to move up the per capita income ladder and carrying out appropriate reforms. It also includes participating fully and constructively in the policy making processes that govern the international economic system, both in discussions and in formal arena.

The rich countries also are confronted with challenges. First and foremost, the advanced countries must meet the problems arising from their demographic and fiscal prospects. But they also must recognize the rise of Asia and enable full participation of Asian countries in the various international bodies. The G-20 was a step in that direction, but it is only a partial substitute for a greater voice in the IMF and World Bank. (I would add the WTO except that the WTO's requirement of unanimity probably requires a change in that institution's governance of a different sort). Focus has been on changing voting shares, and that process has commenced, but only slowly. In addition to voting rights, however, there is also a need for increasing participation by emerging market representatives in fora which are important in influencing opinion. Finally, all countries must eschew protectionist measures and reassert their support for the open multilateral trading system, first by concluding the Doha Round and then by addressing further issues of agricultural and services trade and other new issues.

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