

A New Wave of Change in Global Economic Paradigm: Issues & Challenges



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Road Map For the Presentation

- World Economy: Recent Trends
- International Financial Crisis: A Catalyst for change in Global Economic Paradigm
- The Future of World Economy

Objective of the Paper...

- Present paper makes an attempt to explain the variables that determine the Economic Supremacy of any Country.
- It explains how the next 20 years (2010-2030) will be a period of transition in global economic order, and
- Also visualizes the shift in key variables of global economic order i.e. the emergence of BRICs, especially China and India on the basis of the recent data published by International Monetary Fund.

What exactly happened.....

- The shockwave which was termed as Global financial meltdown is nothing but the financial crisis which occurred in USA resulted in failure of top financial giants.
- USA could not even save Lehman Bros having a great legacy of 158 years from this shockwave of global downturn.

AUGUST 2007

Sub-prime mortgages



Structured financial products



Where are the toxic products?



Inter bank lending freezes



**THE PARTY
STOPS !**

DECEMBER 2007

Central banks start to ease
credit and money supply



AUGUST 2008

US Fed bails out Fannie
Mae and Freddie Mac

15 SEPTEMBER 2008

Lehman Brothers collapses

16 SEPTEMBER 2008

US injects \$85bn into
American International
Group (AIG)

The list of casualties kept growing.....



In this wayit has been managed

GLOBAL IMBALANCES

The United States No 1 economy

- From balanced budget (Clinton)
- To record public deficits (Bush: tax cuts and Iraq war)
- Big trade deficit

EU/Euro zone No 3 economy

- Growth slowing
- Higher unemployment

Developing countries

Africa, Asia/Pacific, Central/South America, Caribbean

Japan No 2 economy

Coming out of « the lost decade »

Other OECD countries

Eg. Australia: Commodities

Emerging economies

China ➔ big trade surpluses

India, Brazil, Chile, South Africa
➔ outsourcing

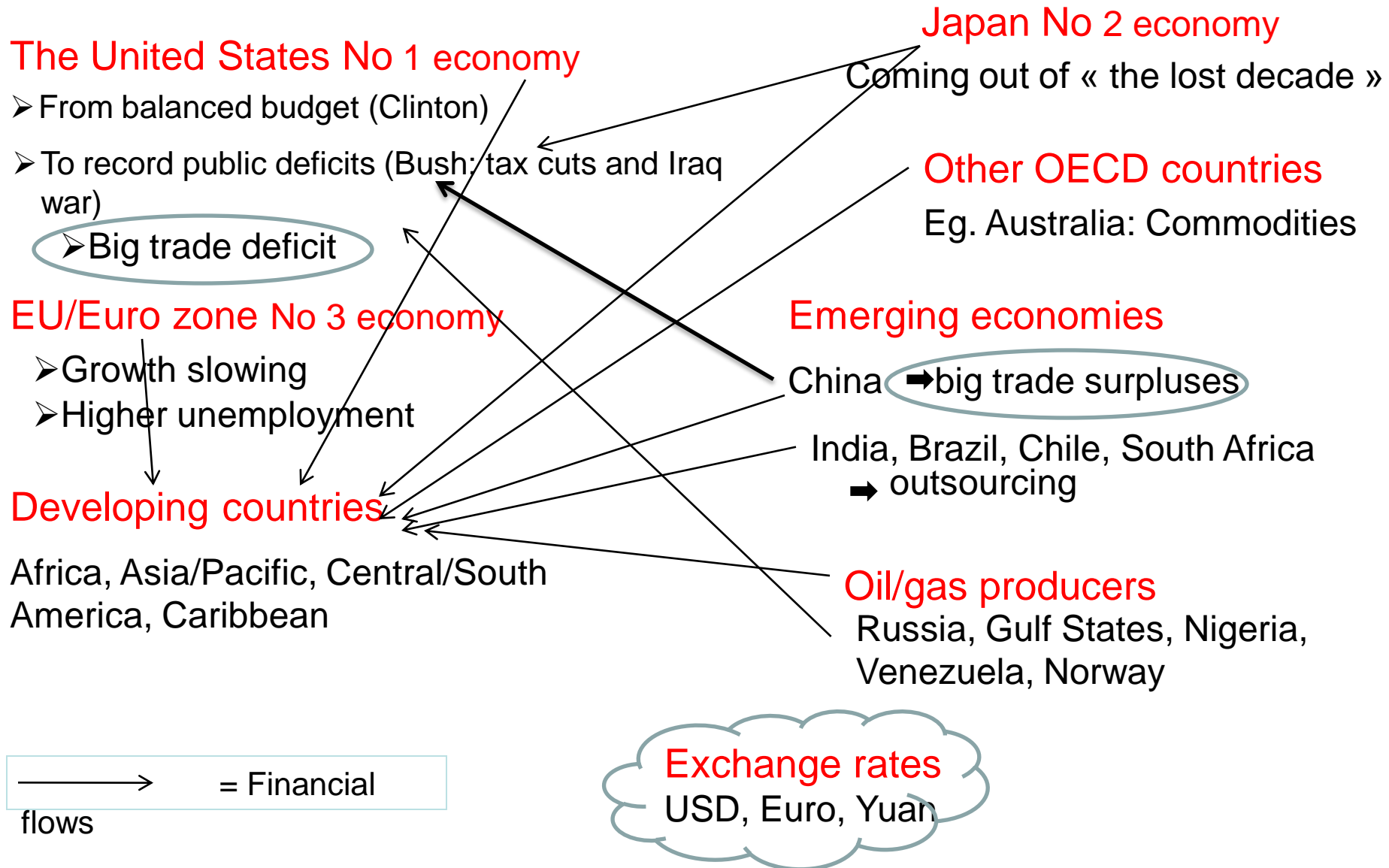
Oil/gas producers

Russia, Gulf States, Nigeria, Venezuela, Norway

→ = Financial flows

Exchange rates

USD, Euro, Yuan



Recent Trends in World Economy...

- The acute phase of financial crisis has passed and a global economic recovery is underway. However, the recovery remains fragile and is expected to slow in the second half of 2010 as the growth impact of fiscal and monetary measures wane and the current inventory cycle runs its course.
- While the baseline scenario calls for global growth firming to 2.7 percent in 2010 and 3.2 percent in 2011 after a 2.2 percent decline in 2009, neither a double-dip scenario where growth slows appreciably in 2011, nor a strengthening recovery can be ruled out

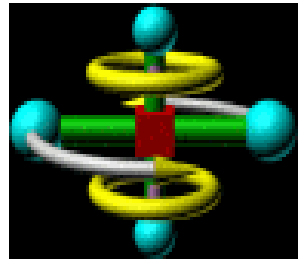
Summary of Global Outlook

2007-2011

A Ray of Hope.....

- But amidst the gloom of the meltdown the shockwave has shown a ray of hope for emerging economies like India and china.
- The global financial crisis paved the way for China to shorten by more than two years, from the time necessary to catch up with industrialized countries, including the USA.
- The USA and Europe underwent “two lost years” due to the financial crisis and Japan for 4-5 years. (IMF, 2008)

The future is a design problem



What is the Future of World Economy?

How do we find the future we prefer?

Design is the ability to move from the existing to the preferred

Economic Supremacy of a Country depends upon its state in terms of Hard and Soft Power

Economic supremacy



In 2007

2020, 2030

Economic Power

Economic Size (GDP)

US (26%), EU (31%)
Asia (22%)

Financial Power,
Science & Technology

Absolute Advantage
of the US

Resource
Power

Key Currency

(International Monetary System)

Pax Dallarium
(Dollar 65%, Euro 26%)

Global Governance

(Influence within International Organizations)

US leadership

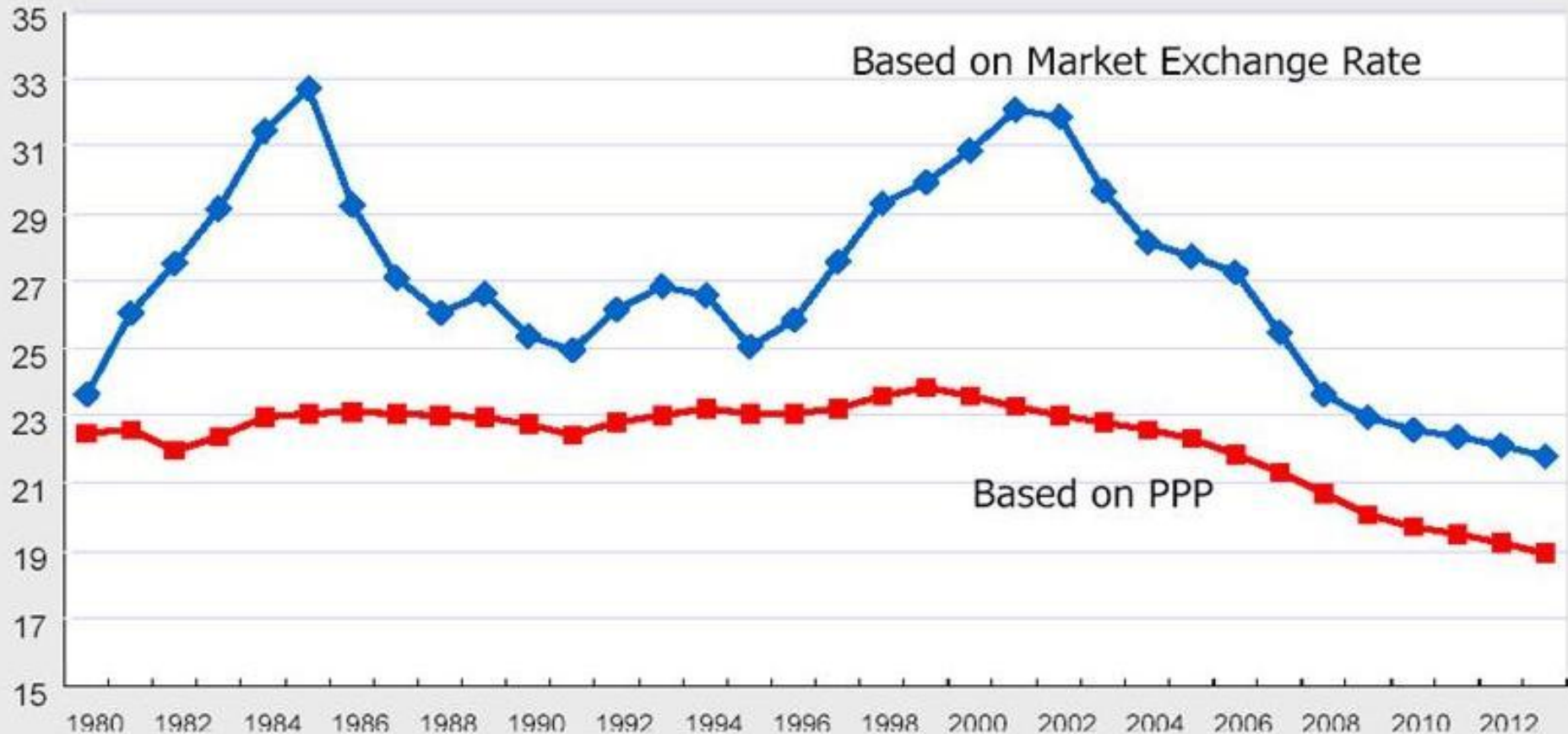
Regional-
ism

Seismic
Shift in the
Global
Economic
Hegemony

Weight of US Economy on the Skids Since 2000

Global Weight of US GDP

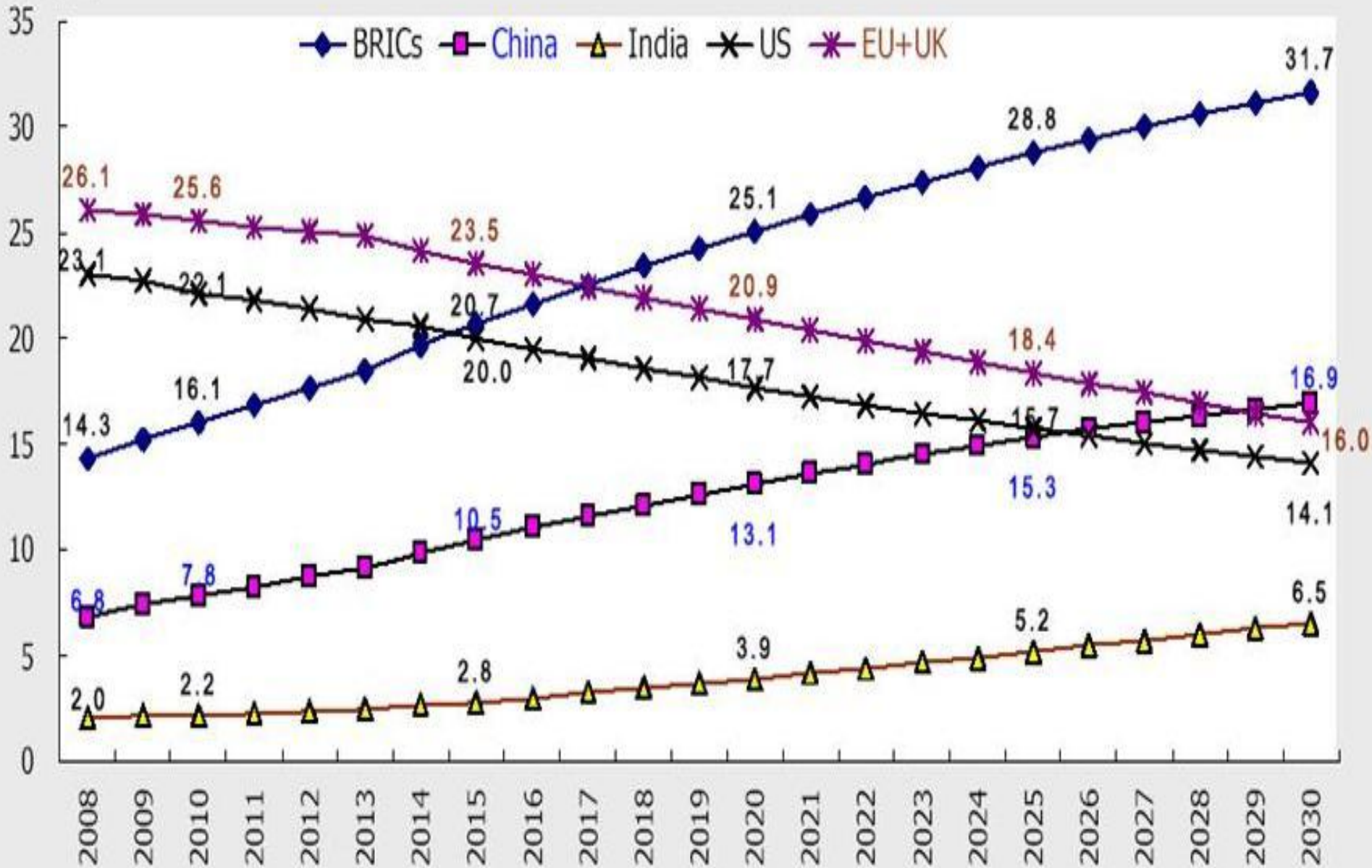
(%)



Source: IMF, World Economic Outlook DB, Oct. 2008

Growth Rate Predictions.....

(Unit : %)



Source: IMF, World Economic Outlook, 2008

Hard Power

Size of Economy

Position of USA till 2008

- Since the early 20th century, the US has been the top economic power in the world.
 - World's largest consumer market
- The US's economic weight has fallen steadily since 2000.
 - 2000: 32% → 2007: around 25%



Predictions in the wake of Current Meltdown

- Global economy is expected to slow down.
 - Despite a rise in productivity driven by technical innovation, global economic growth will slow overall due to aging population and shrinkage in economically active population

Cont...

- Emerging economies, including BRICs, are growing rapidly.
- Average growth of 6.9% during 2002-2007 (Global economy grew 3.3%)
- Weight of BRICs: 5.3% in 1992
→ 12.8% in 2007



- Emerging countries will lead the global economic growth.
- US: 2-3% growth (inflow of immigrants and productivity improvement)
- Euro: 2-3% → 1-2% growth (shrinking labor population)
- Japan: 1-2% growth (rapidly aging population)
- China: 6-7% growth → 4-5% growth from 2020 (declining economically active population and slowing productivity growth)
- India: 6-7% growth (growing population and productivity improvement)

Cont...

- China showed especially fast growth.
 - Annual average growth of 10% since entering WTO in 2001
 - IMF predicts China will overtake Japan in 2010 to become the No. 2 economy



- As early as 2026, China may replace the US as the world's largest economy.
- India is expected to overtake Japan in 2023.
- Economic weight of BRICs will continue to rise.
 - 16.1% in 2010 → 25.1% in 2020
→ 31.7% in 2030

Key Currency....

Current Status

- Since the World War II, US dollar has been the world's key currency.
- The Bretton Woods system created the key currency
- US dollar remained as the key currency thanks to the US's economic power, financial network and the absence of competing currency

Mid/Long-term Forecast

- US dollar will remain the leading currency.
- Due to abundant liquidity in financial market and network effect

Cont...

- Despite the rapidly rising status of Euro, US dollar still holds over 60% share.
- Foreign currency reserve (as of the end of June 2008): 62.5% is US dollar, 27% is Euro
- Foreign currency assets held by private banks: 55.3% is US dollar
- Foreign transactions: 86.3% is US dollar, 37% is Euro
- Outstanding amount of international bonds (Sept. 2008): US\$8.2 trillion, 10.8 trillion euro

- Euro will become a powerful competing currency, resulting in a bipolar currency system of US dollars and euros.
- After the global financial crisis, restructuring in the international financial order will alter the US-led global currency system

Cont.....

- Stability of US economy and dollar shall get weakened because of sharp rise in US current account deficit and foreign debts.
- **Meanwhile, Foreign currency reserves of emerging countries are expected to further rise.**
- China's foreign currency reserves are expected to swell to more than US\$3 trillion in 2015 from the current US\$2 trillion

Soft Power or Knowledge Capital

Determinants for key currency

- Size of economy and trade, macroeconomic and monetary stability, development of financial market, external network effects
 - › Size of trade and macroeconomic/monetary stability: Euro holds superiority
 - › Size of economy, development of financial markets, external network effects: US dollar holds superiority

Position of USA till 2008

- US holds dominant position in all areas that create financial power; financial hub, center of financial assets and institutions.
- US holds 56.1% of the world's financial assets
- 34% of bonds (as of 2006)
- Stock market capitalization: 4.5 times that of Japan, the world's second-largest market
- Among the world's ten major banks, three are US banks
- New York is the global financial hub
- Except for London, most other financial hubs specialize in narrow financial services



Predictions in the wake of Current Meltdown

- Financial power of Europe and emerging countries will strengthen.
- Significant advancement expected in sovereign wealth funds and emerging countries

- **US maintains financial power based on its key currency status and advanced financial acumen.**
- **US Dollar Recycling Mechanism**
- **US's current account deficit → Increasing liquidity in countries with current account surplus → Swelling foreign currency reserve of these countries → Investment in the US**
- **US has quality workforce, core factor of financial industry**



- **Absolute financial power of the US will weaken but its superior status will continue.**
- **In the wake of the financial crisis, the US financial industry will undergo a temporary contraction**
- **US will continue to hold competitiveness thanks to large comprehensive financial groups**
- **Commercial banks and investment banks combined**

- **Financial crisis caused contraction in US investment banks.**



- **Financial power will be divided between the US and Europe.**
- **Impact of China's rapidly growing financial power will be limited to Asia.**

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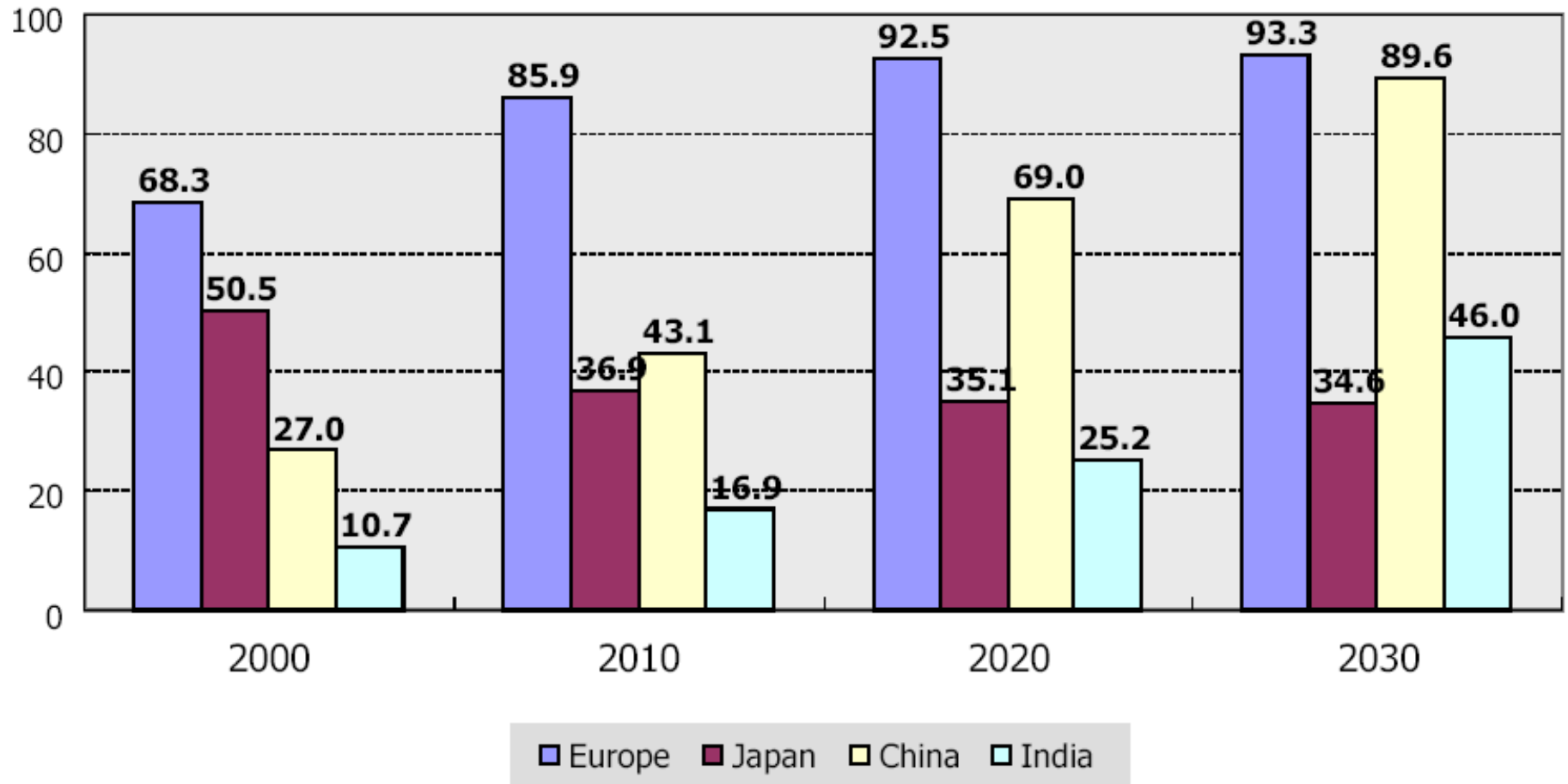
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Creation of a Tri-Polar Global Structure by 2030

Economic Power Index



Note : The Economic Power Index (EPI) represents **scores based on the sum of comparative outlook in seven areas (US=100) – economic scale, key currency, financial power, resource-securing capability, science & technology, regional leadership, and global governance.**

**Can we think of Global
Prosperity without Developed
Countries.....??**

Emerging Markets Can't Drive Global Recovery without Growth in the Developed World

- While most emerging markets have proven remarkably resilient to the effects of the global financial crisis, they cannot act as the locomotive of global recovery unless the developed countries revive their own economies and address the structural problems that led to crisis.

WEF- Davos-Klosters Switzerland, 28 January, 2010

Cont....

- Large emerging markets such as Brazil and China are unlikely to be able to maintain rapid growth without a stronger economic recovery in the developed world.
- Greater regulatory coordination between the developed and developing countries is needed.

USA back from depression...

- The latest US GDP report, which shows the economy expanded at a 5.7% rate in the fourth quarter, demonstrates that the massive fiscal and monetary stimulus measures proposed or endorsed by the Administration have “pulled the [US] economy back from the brink of a depression, and created an environment for economic growth

The Real Solution

- The global recovery is fragile, and now is the moment to rethink values as the world rebuilds prosperity
- All countries in the G20 and beyond should find new pathways to sustainable growth and job creation
- As per conclusion made in 40th World Economic Forum Annual Meeting, 2010, participants decided to rethink, rebuild and redesign the global economy based on sustainable principles.

VARIABLE GEOMETRY

G7

Canada, France, Germany,
Italy, Japan, UK, US

G8

Canada, France, Germany,
Italy, Japan, UK, US
+ Russia

G20

Brazil, Canada, China, France, Germany, India,
Italy, Japan, Mexico, Russia, South Africa, UK, US,
+
Argentina, Australia, Indonesia, Saudi Arabia, South
Korea, Turkey, European Union

G14

Canada, France, Germany,
Italy, Japan, Russia, UK, US
+ Brazil, China, Egypt, India,
Mexico, South Africa

[BRIC]

Brazil, Russia, India, China



Thank You All For the Patient Listening !
For Further Queries Contact us at :
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