Japan, India and China: Engines of Asian Economic Integration

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Outline

1. Introduction: Asia’s Three Giant Economies
2. Asia’s Economic Integration
3. Regional Cooperation for Economic Integration
4. Concluding Remarks
1. Introduction: Asia’s Three Giant Economies

• Asia is recovering from the global financial crisis as the most dynamic region in the world
• The three giant economies in the region, Japan, India and China, are highly **complementary**
  - Japan has: strong institutions; high human capital and technology; aging society
  - India has: large, growing market size; English speaking graduates; technology & services (ICT); young population
  - China has: large, growing market size; low- to mid-tech manufacturing sectors; outward orientation (trade & FDI)
• India and China have two faces: growth & dynamism and poverty & inequality, with huge **structural and governance challenges**
• How can the three giants cooperate to sustain “quality” growth?
## Growing China, India, ASEAN...

<table>
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<tr>
<th>Size of GDP</th>
<th>2009</th>
<th>2014</th>
<th>2020</th>
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<tr>
<td></td>
<td>Trill. USD</td>
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<td>1.2</td>
<td>1.9</td>
<td>3.0</td>
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**Note:** The figures for 2014 are IMF projections, and those for 2020 are estimated by the author.

**Source:** IMF, *World Economic Outlook*, October 2009.
Share of major economies in the world (% in 1990 international dollars)

## Key economic and structural indicators

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<tr>
<th>Year</th>
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<td>GDP per capita (current US$)</td>
<td>Poverty Ratio¹</td>
<td>Gini Coefficient</td>
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Notes: NA = Not Available; (1) Latest figure available based on a US$1.25 a day poverty line using 2005 purchasing power parity (PPP) rates as calculated from the PovcalNet online poverty analysis tool of the World Bank; (2) HDI rank out of 181 economies; Index score: 0 = no human development, 1 = maximal human development³
Sources: World Bank, World Development Indicators Database 2009; UNDP, Human Development Report 2009
Sectoral composition of output
Japan, India and China, 2006

Demographic complementarity: Japan, China, India
1950-2050
2. Asia’s Economic Integration
Market-driven economic integration

- Market-driven trade and FDI integration between Japan and China
  - Large trade and FDI flows due to outward-oriented policies and focus on infrastructure
  - Formation of production networks and supply chains by global MNCs and Asian firms
  - This has also involved Asian NIEs (like Korea and Taipei, China) and ASEAN

- Trade & FDI integration of India with Japan and China has been limited
  - Largely due to high tariff and non-tariff barriers to trade, lack of trade related infrastructure
  - India is not well-integrated with other South Asian economies, either

- But Japan’s FDI in India is rising in recent years
Trade among Japan, India and China
(US$ Billion)

Source: IMF, Direction of Trade Statistics
Japan’s FDI in India is rising, though still small in comparison to China and others

Japan’s FDI Outflows

Japan’s Outward FDI Stocks

Note: ASEAN and Asian NIEs include Singapore
Source: Compiled by JETRO, using Bank of Japan’s balance of payments data
Intra-regional trade in South Asia is limited

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<td>2001</td>
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<td>2002</td>
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<td>2004</td>
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<td>2008</td>
<td>52.06</td>
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Note: Intra-regional trade share is the percentage of intra-regional trade to total trade of the region, calculated using exports data. A higher share indicates a higher degree of dependency on regional trade.

Source: ADB Asia Regional Center (ARIC) Database
But trade links are rising between India and East Asia

- India-East Asia trade has started to rise in recent years
- China became India’s top trade partner in 2009

Drivers of India-East Asia trade links: India’s “Look East Policy”

- East Asia’s economic dynamism (outward-oriented growth), offering good policy lessons for India’s development strategy
- East Asia’s market-driven economic integration and FTA initiatives, stimulating India to strengthen links with East Asia
Financial links are weak even in East Asia

Limited financial integration

• Financial links are weak even in East Asia due to the varying degrees of market opening and capital account liberalization across countries

• Intra-Asian portfolio investment is very limited in comparison to many parts of the world

Macroeconomic synchronization

• Surprisingly, macroeconomic synchronization is increasingly observed among Japan, India and China (and ASEAN)
But Asia is much less integrated through portfolio investment. Nonetheless, Asia’s regional financial integration is increasing.

Source: Calculations using Consolidated Portfolio Investment Survey, International Monetary Fund.
GDP growth rate correlations are rising among Japan, India, China and ASEAN (10-year moving windows)
3. Regional Cooperation for Economic Integration

Regional cooperation architecture

- Trade and FDI cooperation (FTA)
- Infrastructure cooperation
- Environment and energy cooperation
- Social inclusion
- Monetary and financial cooperation

Structural reform challenges are huge
East Asian economic cooperation architecture

• ASEAN as the integration hub for an EAFTA (FTA for ASEAN+3 countries) and/or a CEPEA (FTA for ASEAN+6 countries)
• ASEAN+3 focusing on financial cooperation, including the Chiang Mai Initiative (CMIM), and Asian Bond Markets Initiative
• ASEAN+6 dealing with wider issues
• APEC connects East Asia with the Americas
• ASEM connects East Asia plus India with Europe

This architecture suggests a “variable geometry” approach
Asia’s evolving economic architecture suggests the effectiveness of variable geometry.
ASEAN+3 and East Asia Summit (ASEAN+6) cooperation
Benefits of economic integration

Deeper economic integration in Asia creates a large market and economic potential for all

- Narrowing the development gap by integrating landlocked and/or low-income countries to large ones like India and China
- A consolidated FTA for an ASEAN+3 FTA (EAFTA) or an ASEAN+6 FTA (CEPEA) will bring much larger income gains than ASEAN+1 FTAs
- ASEAN+6 FTA (CEPEA) creates larger benefits than ASEAN+3 FTA (EAFTA)
Potential gains in world income from ASEAN+3 and ASEAN+6 integration

Note: Covers all world trade and production
Source: Francois and Wignaraja (2008) and Kawai and Wignaraja (2009)
Seamless infrastructure connectivity for Asia’s integration

- Seamless regional infrastructure, connecting East Asia and South Asia, through transport, energy distribution, fiber-optic cables, and IT systems to enhance intraregional trade and investment and enhance regional demand.
- Developing Asia will need to invest $8.3 trillion in infrastructure during 2010-2020 (or about $750 billion per year), which will create income gains of about $13 trillion.
- Asia may establish a “Pan-Asian Infrastructure Forum” and “Asian Infrastructure Fund” to foster connections within and between subregions of Asia, such as East Asia and South Asia.

* ADB/ADBI, “Infrastructure for a Seamless Asia” (2009)
## Governance, competitiveness, infrastructure

<table>
<thead>
<tr>
<th>Year</th>
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<th>2009-2010</th>
<th>2010</th>
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<tbody>
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<td>GCI²</td>
<td>Infrastructure</td>
</tr>
<tr>
<td></td>
<td>Rank</td>
<td>Score</td>
<td>Rank</td>
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<td>India</td>
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</table>

Notes: NA = Not Available; (1) WGI = Worldwide Governance Indicators, composite is arithmetic average of 6 WGI indicators; WGI Rank out of 212 economies; Score: -2.5 to 2.5, with higher values corresponding to better governance outcomes; (2) GCI = Global Competitiveness Index; GCI and Infrastructure Ranks out of 133 economies; Score: 1 = poorly developed and inefficient, 7 = among the best in the world; (3) DBR = Doing Business Ranking; Overall business ranking out of 183 economies

Sources: World Bank, World Development Indicators Database 2009 and Doing Business Index Database 2010; World Bank Institute, Worldwide Governance Indicators Database 2010; World Economic Forum, Global Competitiveness Report 2010
Environment and energy cooperation

• India and China need to focus on protecting the environment and improving energy efficiency to achieve a lower-carbon society while pursuing their socioeconomic objectives

• A holistic approach is needed:
  - Mainstream environmental protection and carbon emission reduction in the development strategy, using the co-benefits approach
  - Invest in energy efficiency and renewable energy development, acquire new technologies
  - Adopt market friendly policies (reducing fuel subsidies and raising energy prices) while paying adequate attention to social protection

• Japan’s technology cooperation is vital
Asia’s share in global carbon emissions from energy consumption is expected to rise.

- **2006 Actual**
  - Total = 27,889 Mil tons CO₂

- **2030 Projection**
  - Total = 40,553 Mil tons CO₂

Source: IEA World Energy Outlook 2008
Carbon emission is growing fast in China, India …

![Graph showing carbon emissions growth in various countries from 1971 to 2005.](image)

**Country** | **Per cent of global emissions in 2000** | **Per cent of global emissions in 2050**
---|---|---
US | 20.6% | 15.1%
China | 14.7% | 22.9%
EU25 | 14.0% | 7.8%
Russia | 5.7% | 2.8%
**India** | 5.6% | 9.2%
Japan | 3.9% | 1.8%
Brazil | 2.5% | 2.2%
Canada | 2.0% | 1.3%
Republic of Korea | 1.5% | 1.0%
Mexico | 1.5% | 1.7%
Indonesia | 1.5% | 2.2%
Australia | 1.5% | 1.0%
South Africa | 1.2% | 1.1%
Rest of the world | 23.8% | 29.9%

*Source: Compiled by the Ministry of the Environment from the data of IEA, CO2 Emissions from Fuel Combustion 2007*
Human development index (HDI) rises with per capita electricity consumption

- Nearly 1 billion people lack access to energy in the world
- Developing countries have every right to grow and consume more electricity
- The development challenge is to achieve it without much strain on the environment and huge emissions of CO2

*Source: UNDP, 2006*
Social inclusion

• Success of poverty reduction, and a rapid decline in the number of poor in India & China
• A rise of low-income (with $1,000-$5,000 per year) households and the middle class (with $5,000-$35,000), resulting in the emergence of diverse needs of society, not simply poverty reduction
• A shift of policymakers’ attention towards policies supporting the diverse needs of low-income households and the middle class
• Inclusive growth policy promotes access to opportunities for growth, through infrastructure, rule of law, education, health, employment
## A rise of low-income and middle class households in Asia (% of population)

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Social protection expenditure as % of GDP

Monetary and financial cooperation

- Financial integration facilitates mobilization of large savings in Japan and China for investment, particularly infrastructure, in other parts of Asia
  - Financial market development and deepening
  - Capital account liberalization (well-sequenced liberalization in an integrated program)
  - Harmonization of rules, regulation and market practices
- Managing capital flows
  - Exchange rate policy coordination
  - Regional liquidity arrangement (CMIM) and bilateral currency swaps (Japan-India)
- Creation of an Asian Financial Stability Board to promote regional financial system stability
Structural reform challenges

Economic reforms to improve governance, business climates

- **Japan** to develop a credible growth strategy that addresses public debt consolidation
- **China** to focus on **rebalancing** for sustainable growth—production & spending; growth & the environment; and growth & social inclusion
- **India** to focus on improving the investment climate (infrastructure, impediments to business and trade, FDI, labor market reform) and inclusive growth
- India and China need to improve human development and overall governance quality
India’s faces huge challenges: infrastructure; health & primary education; labor market efficiency; technological readiness

Notes: GCI = Global Competitiveness Index; Score: 1 = poorly developed and inefficient, 7 = among the best in the world;
Sources: World Economic Forum, Global Competitiveness Report 2010
4. Concluding Remarks

- Japan, India and China are key engines of growth, integration and development in Asia.
- Asia can prosper through greater regional economic links and connectivity—China and India can be the driver of growth for neighboring economies.
- A CEPEA and an East Asia-South Asia FTA can provide large benefits—Japan, India, China, and ASEAN play a critical role.
- Infrastructure connectivity between East and South Asia is essential in lowering trade and logistics costs.
Concluding Remarks (cont’d)

- India’s leadership is vital in carrying other South Asian countries and bridging whole South Asia with East Asia
- Japan-India-China cooperation should go beyond trade, investment and infrastructure and include the environment & energy, social inclusion, and money & finance
- China and India need further economic reforms to improve governance and invest for the future—education, health, environments, and knowledge
Thank you

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