

# *Prepare for the Asian Century*

## **1. Introduction**

The idea that this century – the 21<sup>st</sup> century – could be the *Asian Century* first emerged in the late 1980s, as a number of Asian economies began to grow at historically unprecedented rates. The idea has since been taken seriously by policy-makers, politicians, academics and business leaders across the world, both within and beyond Asia itself. For some, the Asian century is an optimistic idea – one which entails billions of people being lifted out of poverty and the construction of a new, and more balanced, international order. For others, the Asian century implies the destabilisation of global society, volatility, and even war, as rising powers in Asia push back against the US led international order. These two perspectives are, of course, at the extreme ends of the spectrum, and a number of more nuanced perspectives lie in between.

The concept of an ‘Asian Century’ can be understood by drawing an analogy between Asia’s future role in the 21<sup>st</sup> century and America’s role in the 20<sup>th</sup> century (the ‘American Century’) or Europe’s role in the 19<sup>th</sup> century (the ‘European Century’)<sup>1</sup>. During each of these periods, one power or region has been the ‘driver of globalisation’, acting as a catalyst for global growth, integration and cooperation, whilst shaping the structure of global society and spreading its ideological and cultural influence. The European Century was driven by the industrial revolution, starting in Britain, before spreading to the rest of Europe. During this period, European powers established colonies in every continent, spreading European languages, religions, and institutions around the world. After Europe’s self-destruction at the start of the 20<sup>th</sup> century, America became the driver of globalisation, promoting capitalism and democracy, and establishing an international regime that persists to this day.

During each of these periods, ideological and cultural influence, or ‘soft power’, has been preceded by rapid economic growth. The correlation between these two forms of power can be observed in *Portland’s* ‘soft power index’<sup>2</sup>, in which the five countries ranked highest also rank in the top 10 in terms of GDP (PPP) and account for about 40% of the world economy. As the global economy’s centre of gravity shifts toward Asia<sup>3</sup>, many anticipate the decline of ‘Americanisation’ and the rise of ‘globalisation with Asian characteristics’<sup>4</sup>. As yet, there is little indication of such a transition occurring. Despite Asia’s impressive economic rise, Asian countries are noticeably absent from the soft power index. Of the top 20 countries, only three are Asian, the remaining 17 are predominantly from Europe, as well as the US, Canada and

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<sup>1</sup> ICMAC (2013). Proceedings of the International Conference on Managing the Asian Century. Springer

<sup>2</sup> Portland (2016). The Soft Power 30. (<http://softpower30.portland-communications.com/ranking/>)

<sup>3</sup> Quah, D. (2011). The Global Economy’s Shifting Centre of Gravity. *Global Policy* 2:1, pp. 3-9

<sup>4</sup> Bajpae, C. (2016). Globalization with Asian characteristics. *The Diplomat*. (<http://thediplomat.com/2016/07/globalization-with-asian-characteristics/>)

Australia. Nevertheless, many remain confident that it is only a matter of time before this changes. According to Martin Jacques, “with Europe in precipitous decline and America at a rather earlier stage of the same process, the high-water mark of Westernisation has now passed”<sup>5</sup>.

Asia’s rapid economic growth began in Japan in the 1960s, and was soon followed by the “Four Tigers”, Hong Kong, Korea, Singapore, and Taiwan<sup>6</sup>. In the 1980s, Malaysia, Thailand and China joined this group, and by the early 2000s, China was growing at more than 10% a year. In 2015, China overtook America as the largest economy in the world, measured in GDP adjusted for purchasing power parity. This period, known as the “Asian Miracle” has already lifted billions out of poverty and is changing the structure of international society. From a historical perspective, this recent era of growth should not be seen as the ‘rise of Asia’, but rather, its ‘re-emergence’. In the year 1700, Asia’s share of global GDP was approximately 60%, whilst Europe accounted for about 30% and America less than 5%<sup>7</sup>. This largely reflected the regions’ shares of global population at the time, with Asia accounting for over 65% of global population in 1700. With the industrial revolution in Europe and then America, Asia’s share of global GDP fell to below 20% by the early 1900s. Since the 1980s, it has risen again to 27%, and is set to continue rising.

In spite of this, the Asian Century should not be considered inevitable. Changes occurring within and beyond Asia present unprecedented opportunities and risks that could lead down very different paths. This report begins by considering the key driving forces of change in Asia in the 21<sup>st</sup> century (section 2) as well as changes in the international environment (section 3). In section 4, four future paths are considered: an ‘Asian Century Scenario’ (seen by many as the best-case scenario), followed by four alternative scenarios (‘Middle Income Trap’, ‘Unsustainable Growth’, and ‘Regional Conflict’).

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<sup>5</sup> Jacques, M. (2014). China’s growing global influence. Gaiko (<http://www.martinjacques.com/articles/articles-geopolitics-globalisation/chinas-growing-global-influence/>)

<sup>6</sup> Nakaso, H. (2015). Asian Economy: Past, Present, and Future. Keynote Address at the Securities Analysts Association of Japan International Seminar ([https://www.boj.or.jp/en/announcements/press/koen\\_2015/data/ko150424a1.pdf](https://www.boj.or.jp/en/announcements/press/koen_2015/data/ko150424a1.pdf))

<sup>7</sup> Asian Development Bank (2011). ASIA 2050: Realising the Asian Century

## 2. Drivers of Change in Asia

*Few consider the Asian Century to be inevitable or certain. Rather, if there is one thing that everyone seems to agree on, it is that the prospect of an Asian century rests on a number of important variables, some of which could drive Asia forward, others which may hold it back. In this section, I briefly outline seven drivers of change in Asia.*

### 2.1 Capital deepening

A major element of economic growth in any economy is the accumulation of capital. Asia's high savings rate was a significant contributor to the Asian miracle, allowing countries such as Japan, South Korea and Singapore to rapidly accumulate capital<sup>8</sup>. Capital deepening occurs when capital growth exceeds growth in the labour force, such that capital stock per worker increases. This is occurring at impressive rates in several countries in Asia – 8.6% in China, 8.3% in India, 9.8% in Vietnam, and 9.5% in Cambodia<sup>9</sup>. Given that Asian countries have lower initial levels of capital per worker, they are able to grow their capital stock at faster rates than developed countries where capital per worker is already very high. At present, approximate 70% of the world's capital is in advanced economies (mostly in Europe and North America). Between 2030 and 2050, the Asian Development Bank predicts that this will change, with Asia accounting for 70% of the world's added capital stock<sup>10</sup>.

### 2.2 Technological change and the information revolution

In addition to capital deepening, Asia's economies have been pushed forward by the information revolution and the opportunities both to produce and to use communication technologies that spur growth. Improved access to information is widely recognised as important for development, bringing with it the potential to boost human capital and productivity. But Asia has been especially well-placed to benefit from the information revolution, arriving at a time when China's economy was opening up and Asia was experiencing a dramatic period of growth<sup>11</sup>. This has allowed a number of Asian economies (Japan and South Korea in particular) to become world leaders in the supply of ICT products.

Technology is also changing Asian citizens' relationship with their governments (as it is across the globe) and this could have a major influence on the future of governance in Asia. In China, for example, Yongnian Zheng finds that the internet has made the government more open, transparent, and accountable, as well as increasing the

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<sup>8</sup> Page, J. (1994). The East Asian Miracle: Four Lessons for Development Policy. The World Bank (<http://www.nber.org/chapters/c11011.pdf>)

<sup>9</sup> Asian Development Bank (2011). ASIA 2050: Realising the Asian Century

<sup>10</sup> Asian Development Bank (2011). ASIA 2050: Realising the Asian Century

<sup>11</sup> West, J. (2014). Asia and the information revolution. Asian Century Institute (<http://asiancenturyinstitute.com/society/97-asia-and-the-information-revolution>)

responsiveness of the state<sup>12</sup>. A less positive study by Hiroki Takeuchi, finds that whereas in democracies, the internet increases the influence of moderates over governments (as this group has leverage in elections), in authoritarian states, the internet is likely to increase the influence of extremists (in the case of China, nationalists) as these are seen as the biggest threat to the government<sup>13</sup>. Thus, paradoxically, the internet may fuel nationalism in some countries whilst enhancing democracy in others.

There is a wide technological divide in Asia, with some economies already caught up with the technology frontier, and others lagging behind. Whether or not Asian economies can overtake Western economies will depend on whether they can become innovators, pushing the technology frontier forward, as opposed to just imitators (as China is famous for, with its reverse engineering approach).

### 2.3 The Asian Middle Class

Along with the global top 1%, the Asian middle class are amongst the major winners from globalisation, seeing a 60-80% rise in real income between 1988 and 2008<sup>14</sup>. A report by the Asian Development Bank predicts that by 2030, 75% of the PRC's population will enjoy middle class standards, 19% in India and Vietnam, and 13% in Indonesia<sup>15</sup>. This growth in Asia's middle class could drive further economic growth in a number of ways. Firstly, it may lead to growth in human capital, as a wealthier portion of society are capable of investing in their education and so boost their productivity. Secondly, as a source of savings and entrepreneurship, the emerging middle class will drive innovation<sup>16</sup>.

A third, and more controversial, way in which the growing middle class could boost growth is by boosting demand. The new middle class may serve as a lucrative market, spurring economic activity. At present, Asia's consumption, as a share of gross income is unusually low<sup>17</sup>. Jonathan Woetzel, a director of McKinsey & Company, views this as a big opportunity: "The good news is the kids want to buy stuff—the so-called Generation-2 [G2] consumers, people who are under the age of 25 today"<sup>18</sup>. Others view the concept of "consumption-led growth" as a myth – pointing out that output growth results from the accumulation of factors of production and technological

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<sup>12</sup> Zheng, Y. (2007). *Technological Empowerment: the internet, state, and society in China*. Stanford University Press

<sup>13</sup> Takeuchi, H. (2014). Sino-Japanese Relation: Power Interdependence, and Domestic Politics. *International Relations of the Asia Pacific* 14(1)

<sup>14</sup> Milanovic, B. (2016). Why the Global 1% and the Asian Middle Class have gained the most from globalisation. *Harvard Business Review*. (<https://hbr.org/2016/05/why-the-global-1-and-the-asian-middle-class-have-gained-the-most-from-globalization>)

<sup>15</sup> Asian Development Bank (2011). *ASIA 2050: Realising the Asian Century*

<sup>16</sup> Asian Development Bank (2011). *ASIA 2050: Realising the Asian Century*

<sup>17</sup> Asian Development Bank (2011). *ASIA 2050: Realising the Asian Century*

<sup>18</sup> Woetzel, J. (2015). How Asia can boost productivity and economic growth. Interview with McKinsey Global Institute (<http://www.mckinsey.com/global-themes/employment-and-growth/how-asia-can-boost-productivity-and-economic-growth>)

progress, with consumption being a residual<sup>19</sup>. For those with an environmental perspective, this expansion of the Asian middle class and the high levels of consumption that come with it is a cause for concern. Not only is demand induced growth a flawed growth strategy, it may also put a major strain on the environment and its limited resources<sup>20</sup>.

## 2.4 Demographic changes

Over the past couple of decades, especially during the 'Asian Miracle', Asia has benefitted greatly from a 'demographic dividend', whereby birth rates surpassed death rates, meaning that Asia has a favourable dependency ratio. In fact, some have argued that the Asian miracle was driven primarily by this demographic dividend<sup>21</sup>. Population growth, especially amongst those of working age, leads directly to economic growth due to growth in the labour force. This demographic deficit follows a pattern similar to that experienced by Western countries in the 20<sup>th</sup> century, and is at different stages across Asia<sup>22</sup>.

The first phase is a decline in infant mortality rates which leads to an increase in the young population. The second phase occurs when this cohort reaches working age and society's labour supply increases and the dependency ratio decreases. In this period, we would expect to see high economic growth due to the 'demographic dividend'. However, fertility rates tend to decrease as countries become wealthier and modernise, with citizens becoming better educated, improvements in women's rights and urbanisation<sup>23</sup>. This results in a decline in the birth rate, meaning that the subsequent cohort grows by a smaller amount, and when the booming cohort exits the workforce, the dependency ratio increases, leading to a 'demographic tax'. Some countries are already experiencing this – notably: Singapore, Japan and South Korea. These countries will face major challenges in the 21<sup>st</sup> century and we can expect their growth to slow. For these countries, increased participation from women and over 65s, as well as increased immigration, could reduce the demographic tax. Other countries are just entering the first phase meaning they can expect an increase in the pace of growth in the coming decades.

## 2.5 Climate Change and Resource limitations

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<sup>19</sup> Izvorski, I. (2010). Private consumption in East Asia is not too low. The World Bank (blog) (<http://blogs.worldbank.org/eastasiapacific/private-consumption-in-east-asia-is-not-too-low>)

<sup>20</sup> Nair, C. (2011). Consumptionomics: Asia's role in reshaping capitalism and saving the planet. Oxford: Infinite Ideas Limited

<sup>21</sup> Krugman, P. (1994). The Myth of Asia's Miracle. Foreign Affairs (<https://www.foreignaffairs.com/articles/asia/1994-11-01/myth-asias-miracle>)

<sup>22</sup> West, J. (2014). Asia's looming demographic dilemmas. Asian Century Institute (<http://asiancenturyinstitute.com/society/688-asia-s-looming-demographic-dilemmas>)

<sup>23</sup> West, J. (2014). Asia's looming demographic dilemmas. Asian Century Institute (<http://asiancenturyinstitute.com/society/688-asia-s-looming-demographic-dilemmas>)

Natural resources are an essential component of any economy and preserving these resources will be integral to ensuring that Asia's growth is sustainable and equitable. Globally, according to the Earth Policy Institute, we are 30% beyond the planet's sustainable capacity<sup>24</sup>. What this means in economic terms is that our present levels of consumption are depleting the Earth's natural capital, thus reducing its long run productive capacity. What this means for Asia is that it cannot follow the same growth pattern as Western developed nations. This growth pattern was, according to Chandran Nair, founder of the Global Institute for Tomorrow, "based on excluding environmental and social costs"<sup>25</sup>. This model can only work, Nair argues, when a relatively small proportion of the world population are using it (Western developed economies). Asia's ambitions to catch up with Western economies may therefore be untenable, in that it involves the expansion of the global consumption on a massive scale.

Water is a striking example of resource depletion that is already occurring in Asia, and could only worsen if a consumption-driven growth pattern is pursued. India's per capita renewable water resources fell by 7% from 2000 to 2005 and China's fell by 5%<sup>26</sup>. In Pakistan, which relies heavily on water resources for its agricultural based economy, per capita renewable resources fell by more than half in the same period – from 2961 cubic metres in 2000 to 1420 cubic metres in 2005<sup>27</sup>. Forest depletion is another major concern, especially in Indonesia, where rainforest cover has fallen from 82% to less than 50% in the last 50 years<sup>28</sup>. Climate change presents a similar concern. The World Bank forecasts that developing countries will need to spend a total of between \$40 to \$100 billion every year from now until 2050 on adapting to the effects of climate change on their farming sectors<sup>29</sup>.

Not only do these environmental issues raise major challenges to Asia's growth ambitions, it could also have a devastating impact of the continents poorest people as their environment is depleted. It is already well-documented that the poorest are frequently the worst affected by environmental damage. The inequality and social tensions this would lead to could be a source of major instability both within and between nations. Although the environmental depletion caused by the West over the past century has placed significant limits on Asia's development path, this does not preclude growth entirely. Rather, it will be necessary for Asia to adopt a sustainable path, based on technological innovation rather than natural resource exploitation. This path is economically feasible – the major question is whether it is politically feasible.

## 2.6 Domestic Institutions

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<sup>24</sup> Nair, C. (2011). Consumptionomics: Asia's role in reshaping capitalism and saving the planet.

<sup>25</sup> *ibid.*

<sup>26</sup> *ibid.*

<sup>27</sup> *ibid.*

<sup>28</sup> *ibid.*

<sup>29</sup> *ibid.*

Growth and prosperity depend crucially on domestic institutions. Policy uncertainty has a major impact on investment, and when political regimes go wrong, the consequences for the rule of law and property rights can completely halt economic growth. The development of market institutions in a number of Asian economies has played an important role in facilitating growth. A white paper by the Australian Defence Department reports that “nearly all the high-performing Asian economies deliberately set out to support prosperity by investing in people, building capital and undertaking institutional change, including expanding the role of markets”<sup>30</sup>. The maintenance and continued development of these institutions is an important factor in Asia’s future growth prospects.

A number of evolving features of Asia’s domestic politics may impact on the stability and growth prospects of the region. Firstly, although Asia has drastically changed perceptions of the role of democracy in economic growth, with many of Asia’s fastest growing economies under authoritarian regimes, the volatility of such regimes may be a source of instability in the future. Secondly, there has been a notable increase in nationalism in certain countries such as China, Japan, India<sup>31</sup>. This could lead to militarism or aggressive foreign policy, which would have an obvious destabilising effect. Finally, a frequently observed consequence of globalisation-induced-growth is an increase in *within* country inequality (in spite of a decrease in *between* country inequality)<sup>32</sup>. The consequences of such inequality for domestic institutions is unpredictable and may also lead to instability.

## 2.7 Regional tensions

Asia’s historical regional conflicts casts a long shadow over the 21<sup>st</sup> century. Between 1945 and 2010, there were 71 major wars, accounting for the deaths of over four million people<sup>33</sup>. Whilst most people consider the Cold War a bloodless one, the story in Asia was very different, with Korea and Vietnam bearing the burden of proxy wars between the USSR and the US. Continued tensions on the Korean peninsula, between India and Pakistan and across the Taiwan Strait threaten to disrupt the relative peace of the 21<sup>st</sup> century, in which there have been no major inter-state wars. This relative peace has been an underlying factor in Asia’s economic rise and will be key in determining the future of the Asian Century.

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<sup>30</sup> Australian Government, Department of Defence (2012). White Paper: Australia in the Asian Century. ([http://www.defence.gov.au/whitepaper/2013/docs/australia\\_in\\_the\\_asian\\_century\\_white\\_paper.pdf](http://www.defence.gov.au/whitepaper/2013/docs/australia_in_the_asian_century_white_paper.pdf))

<sup>31</sup> Wagner, D. (2015). Rising Nationalism a Threat to Asia. International Policy Digest (<http://intpolicydigest.org/2015/06/08/rising-nationalism-a-threat-to-asia/>)

<sup>32</sup> International Monetary Fund (2007). Globalization and Inequality, in *World Economic Outlook*, Ch. 4 (<https://www.imf.org/external/pubs/ft/weo/2007/02/pdf/c4.pdf>)

<sup>33</sup> Alagappa, M. (2014). International Peace in Asia: Will it Endure? Carnegie Endowment International Peace (<http://carnegieendowment.org/2014/12/19/international-peace-in-asia-will-it-endure-pub-57588>)

Many of the wars of the 20<sup>th</sup> century in Asia were directly related to the nation-building projects that occurred after colonialism ended in 1945. Tensions between China and Taiwan, North and South Vietnam, India and Pakistan and North and South Korea were all reactions to the attempts to build states, fuelled by identity and sovereignty claims. According to Muthiah Alagappa<sup>34</sup> of the Carnegie Endowment for International Peace, the transition to peace in the 21<sup>st</sup> century can be explained by growing international legitimacy, economic development and greater state capacity, which have led to a decline in the utility of war as an instrument of state policy. Nevertheless, tensions fuelled by nationalism may drive irrational security policy and with the shifting balance of power that comes with uneven economic development, old stalemates may once again become conflicts.

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<sup>34</sup> Alagappa, M. (2014). International Peace in Asia: Will it Endure? Carnegie Endowment International Peace (<http://carnegieendowment.org/2014/12/19/international-peace-in-asia-will-it-endure-pub-57588>)



### 3. The international environment of the 21<sup>st</sup> century

*The changes that are happening in Asia, outlined in the previous section, will occur in the context of the larger global economy and international environment. A number of trends can be identified in this regard that will impact on Asia's prospects, politically and economically. Below, I briefly outline four such trends.*

#### 3.1 Geopolitics supplanted with geo-economics

With increasing economic interdependence in a globalised economy, economic statecraft is supplanting military conflict as the most effective way for major powers to exert influence internationally. The World Economic Forum describes this new trend as having the “grammar of commerce but the logic of war”, taking the form of sanctions, competition for markets, and foreign direct investment<sup>35</sup>. Sanctions inflict damage on the target country by denying it access to key markets. The most prominent example of the use of sanctions in recent years is the sanctions against Russia by the US and EU in response to the Ukraine crisis. When sanctions persist, they can often lead to major economic adjustments and political realignments as both players search for new economic partners. In the case of Russia and the EU, Russia looked to China to fill the demand gap for its oil, signing an unprecedented \$300 billion deal lasting 30 years. Beyond the use of sanctions, economic costs and benefits are increasingly attached to political objectives – for example, China rewards Taiwanese companies that follow Beijing's line and penalising those that do not<sup>36</sup>; India is extending new credit lines to Nepal and Mauritius in order to secure access to their markets<sup>37</sup>. This type of economic statecraft could lead to ‘de-globalisation’, as markets become aligned with allied blocs to insure against trade wars<sup>38</sup>. Such a development would be a major backward step for the global economy.

#### 3.2 Breakdown of global institutions and increased regionalism

A second major trend in global political economy identified by the World Economic Forum is the decline in significance of global institutions, such as the IMF, World Bank and WTO, and the rise of regional ones, such as the AIIB, New Maritime Silk Road, and EU<sup>39</sup>. This is all part of what some view as the end of “Pax Americana”. The IMF, for example, which gives out loans to countries struggling with debt, has come under increasing criticism for imposing “structural reform” – reforms to the recipient economy along the lines of the “Washington Consensus”. On the one hand, these reforms are

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<sup>35</sup> Leonard, M. (2015). Geo-economics: seven challenges to globalisation. World Economic Forum

<sup>36</sup> Harris, J. (2016). America's fatal flaw in its competition with China is thinking militarily, not economically.

<sup>37</sup> Harris, J. (2016). America's fatal flaw in its competition with China is thinking militarily, not economically.

<sup>38</sup> Leonard, M. (2015). Geo-economics: seven challenges to globalisation. World Economic Forum

<sup>39</sup> Leonard, M. (2015). Geo-economics: seven challenges to globalisation. World Economic Forum

necessary for the IMF to avoid moral hazard<sup>40</sup>. On the other hand, they represent the imposition of American ideological values on often unwilling countries. Regional financial institutions, such as the Asian Investment and Infrastructure Bank (AIIB), led by China and India, directly challenge the IMF, and are premised on a rejection of the IMF's structural reform approach.

### 3.3 Slowing growth in Europe and America

There is wide disagreement between the so-called 'techno-optimists', who believe that we are in a period of rapid technological innovation that is yet to create unforeseeable and hitherto unimaginable changes to our lives, and the sceptics, such as Robert Gordon<sup>41</sup> (author of "The Rise and Fall of American Growth), who believe that the technological innovations of the 19<sup>th</sup> and 20<sup>th</sup> century are over, and will not be repeated. This disagreement is of major significance for the growth prospects of Europe and America, since the nations of these regions are already at the "technology frontier", meaning growth is primarily driven by new innovations, and not by catching up with existing ones or through capital accumulation. For this reason, as well as decreasing population growth, some highly influential economists, such as Thomas Piketty<sup>42</sup> and Robert Gordon forecast that Europe and America will enter an era of slow growth. Although by nature technological innovations are unpredictable, recent experience in Europe and America provides some support for this interpretation.

If these predictions are correct, this could have a major impact on the national politics of these economies, and hence their role in international affairs. As Adam Davidson<sup>43</sup> of the New York Times argues: "Economies that are stagnant lead to conflict; if the pie isn't getting bigger, after all, the only way to improve your lot is to grab someone else's slice". This reflects a common view in political economy that as growth slows, rent-seeking increases, and as rent-seeking increases, so does protectionism. A report by the World Trade Organisation (WTO) identifies a significant rise in protectionist measures amongst G20 countries since the financial crisis of 2008<sup>44</sup>. Anti-establishment backlashes in the form of Donald Trump and Bernie Sanders in the US, Jeremy Corbyn and Brexit in the UK, as well as many others across Europe, have made a significant impact of policy, turning public attention inward not outward<sup>45</sup>. This trend, along with the growing importance of geo-economic and regionalism, may lead to deglobalisation amongst slow growth Western nations.

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<sup>40</sup> Vasquez, I. (1999). The International Monetary Fund: Challenges and Contradictions. Cato Institute (<http://www.cato.org/publications/congressional-testimony/international-monetary-fund-challenges-contradictions>)

<sup>41</sup> Gordon, R. (2016). The Rise and Fall of American Growth. New Jersey: Princeton University Press

<sup>42</sup> Piketty, T. (2014). Capital in the twenty first century

<sup>43</sup> Davidson, A. (2016). Are we doomed to slow growth? The New York Times Magazine ([http://www.nytimes.com/2016/02/21/magazine/are-we-doomed-to-slow-growth.html?\\_r=0](http://www.nytimes.com/2016/02/21/magazine/are-we-doomed-to-slow-growth.html?_r=0))

<sup>44</sup> Donnan, S. (2014). Protectionism rising as growth slows. Financial Times. (<https://www.ft.com/content/4ee2d69a-6aa3-11e4-bfb4-00144feabdc0>)

<sup>45</sup> Bajpae, C. (2016). Globalization with Asian characteristics. The Diplomat. (<http://thediplomat.com/2016/07/globalization-with-asian-characteristics/>)

### 3.4 Emerging economies beyond Asia (non-Asian BRICS and MINT)

If the advanced economies of the West become increasingly inward looking as growth slows in the coming century, there is potential for emerging economies to take on the role as drivers of globalisation. Whilst Asia's emerging economies appear to be obvious candidates, they will not be the only ones vying for influence. Non-Asian emerging economies include Brazil, Russia and South Africa, which, along with India and China, form the BRICS development group. In addition to the BRICS, some commentators have identified another layer of developing economies, known as MINT, which consists of Mexico, Indonesia, Nigeria and Turkey. More generally, a number of economists predict that, with slowing growth in Europe and America, the global economy is entering an era of convergence, whereby poorer countries will catch up with richer ones<sup>46</sup>. As Paul Hubbard suggests, the rise of Asia (along with other BRICS and MINT economies) may be conceived as the re-emergence of a world in which population size and economic size are closely linked<sup>47</sup>.

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<sup>46</sup> Piketty, T. Capital in the Twenty First Century

<sup>47</sup> Hubbard, P. (2014). Asiaphoria or Asiaphobia? East Asia Forum  
(<http://www.eastasiaforum.org/2014/12/14/asiaphoria-or-asiaphobia/>)

## 4. Future Paths for the Asian Century

*The variables outlined above will each bear on the development of Asia in this century, and will therefore determine the future path of the Asian Century. As has been made clear, Asia encounters high opportunities as well as high risks resulting from the various changes occurring within and beyond Asia. In this section, I will consider a number of potential scenarios based on the frequent themes found in the commentary surrounding Asia's development. I begin with the 'Asian Century Scenario', which might be considered the best-case scenario, before considering four alternative scenarios.*

### 4.1 The Asian Century Scenario

The Asian Century Scenario is the best-case scenario identified by experts and organisations seeking to steer Asia in the right direction. It is based on a number of assumptions, each of which will be relaxed in the alternative scenarios that follow. First, it is assumed that Asia avoids the middle income trap by transitioning from resource-driven growth to productivity and innovation-based growth. Secondly, it is assumed that there is adequate consideration of the environment to ensure that growth in the region is sustainable, and does not eventually undermine itself. Thirdly, it is assumed that Asia avoids regional conflict through cooperation and integration, allowing it to deal with the major challenges of the 21<sup>st</sup> century. If all three of these conditions are met, there is significant optimism that this could indeed be the 'Asian Century'.

The Asian Development Bank reports that Asia's growth rate has reached a 'rough equilibrium' of 5.6% and this will continue for the next 40 years (under the assumptions of Asian Century Scenario). Although advanced economies in the region may slow, developing economies will compensate. On this basis, they predict that by 2040, "it is unlikely that any Asian countries will be poor by today's standards" and by 2050 Asia's GDP per capita could be above the global average at \$38,600. In total, they predict that Asia will once again account for over half of global output (more than double its current share).

Many believe that the continued economic rise of Asia, as projected in the Asian Century Scenario, would lead to major geopolitical shifts as new Asian 'superpowers' (such as China or India) challenge the US to be the global hegemon. The establishment of the Asian Investment and Infrastructure Bank (AIIB) and One Belt One Road Scheme by China is seen by many as an attempt to challenge the US dominated international financial architecture. Rising military spending in China is given a similar interpretation. Gideon Rachman<sup>48</sup>, author of *Easternisation: War and*

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<sup>48</sup> Rachman, G. (2016). *Easternisation: War and Peace in the Asian Century*

*Peace in the Asian Century* describes “the emerging contest for supremacy in the Asia-Pacific between the US and China” as “quite finely balanced”. Others are more sceptical. Paul Dibb, a national security expert, argues that even if Chinese military expenditure exceeded American spending (which it does not), America would maintain a technological edge over China that economic power could not provide<sup>49</sup>. Others predict that China’s rise will not be like that of others that have rivalled the hegemon (for example, America against Britain during the war of independence, or Germany against Britain during the world wars). Rather, America, as an extant power, has been able to establish a resilient international regime that will be capable of assimilating China<sup>50</sup>. Although these questions are beyond the scope of this report, it is reasonable to anticipate that under the Asian Century Scenario, the role of Asian powers, such as China and India, over global governance would be significantly increased.

## 4.2 Alternative Scenario I: The Middle Income Trap

Many economists have cautioned against the ‘presumption of continuity’ when it comes to growth in Asia<sup>51</sup>. The experience of countries such as South Africa and Brazil tells us that it is not unusual for developing countries to ‘hit a wall’ at a certain level of economic development, and struggle to get beyond that - economists call this the ‘middle income trap’. Of 101 economies classified as ‘middle income’ in 1960, only 13 progressed to the high income stage by 2008<sup>52</sup>. This reflects the fact that it is easier to progress from low-income to middle-income than it is from middle-income to high-income. The reason for this is that low-income countries can use their poverty to fuel resource-driven growth<sup>53</sup>. Low wages give poor countries a competitive edge in the export market; the pool of unskilled labour that can be transferred from agriculture to industry means that the labour force keeps growing; and there is ample room for technology to catch-up<sup>54</sup>. However, the transition from low-income to middle-income has the effect of undoing these conditions. Wages rise, the pool of transferrable unskilled labour is exhausted; and technology is caught up. The challenge for a middle-income country is to shift from resource-driven growth to productivity and innovation-based growth. This requires an array of institutional, social and economic transformations.

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<sup>49</sup> Dibb, P. (2011). Two Geopolitical Fallacies: the rise of China and the inevitable decline of America. Speech to ANU College of Asia and the Pacific (<https://www.youtube.com/watch?v=QiZ6391DCis>)

<sup>50</sup> Ikenberry, J. (2008). “The rise of China and the future of the West: Can the liberal system survive?”, *Foreign Affairs*, 23-37.

<sup>51</sup> Pritchett, L. & L. Summers (2014). Asiaphoria meets regression analysis to the mean. NBER Working Paper No. 20573

<sup>52</sup> Agénor, P., O. Canuto & M. Jelenic (2012). Avoiding middle income growth traps. The World Bank (<http://siteresources.worldbank.org/EXTPREMNET/Resources/EP98.pdf>)

<sup>53</sup> Agénor, P., O. Canuto & M. Jelenic (2012). Avoiding middle income growth traps. The World Bank (<http://siteresources.worldbank.org/EXTPREMNET/Resources/EP98.pdf>)

<sup>54</sup> Nakaso, H. (2015). Asian Economy: Past, Present, and Future. Keynote Address at the Securities Analysts Association of Japan International Seminar ([https://www.boj.or.jp/en/announcements/press/koen\\_2015/data/ko150424a1.pdf](https://www.boj.or.jp/en/announcements/press/koen_2015/data/ko150424a1.pdf))

A report by the Asian Development Bank distinguishes between three country groups in Asia: (i) high income, developed economies – consisting of the seven most advanced Asian economies; (ii) fast growing, converging economies – consisting of 11 countries led by China and India; and finally, (iii) aspiring economies with slow or modest growth – which includes the remaining 31 countries with low or lower-middle income<sup>55</sup>. The report suggests that countries in groups (ii) and (iii) are vulnerable to falling into the middle income trap. Indeed, the recent history of Asia’s growth fits with the middle income trap narrative. Its growth has been export-led, based on manufacturing – becoming the “factory of the world”<sup>56</sup> – at expense of other industries. As has already been discussed, the demographic changes going on in Asia at the moment may only exaggerate the dynamics of the middle income trap as the demographic dividend transforms into a demographic tax.

However, the middle income trap is not inevitable. Research at the University of Western Australia suggests that the stagnation of growth in many middle income countries may be caused by bad luck or bad policy rather than structural reasons. As Robertson and Ye argue, “perhaps what appears to be a pattern of behaviour across many countries is just the way things panned out”<sup>57</sup>. Some of the institutional features that contribute to the middle income trap are: insufficient investment in human capital and higher-value-added activity, political instability and under-developed financial markets that fail to facilitate innovation<sup>58</sup>. These factors do not respond automatically to market forces, rather, they require action on the part of governments and other key actors. The success of Asia’s seven high income economies in avoiding the middle income trap could serve as a useful example of other countries in the region. Of the 13 economies able to transition from middle to high income since the 1960s, five were from East Asia: Hong Kong, Japan, Korea, Taiwan, China, and Singapore (also known as the “Asian Tigers”). A World Bank report highlights three key features that characterise all of these cases: (i) advanced infrastructure networks (in the form of high-speed communications and broadband technology); (ii) strong intellectual property rights protection (facilitating home-grown innovation and pushing forward the technology frontier); and (iii) flexible labour markets and open economic policies that allow the reallocation of labour across sectors<sup>59</sup>.

### 4.3 Alternative Scenario II: Unsustainable Growth

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<sup>55</sup> Asian Development Bank (2011). ASIA 2050: Realising the Asian Century

<sup>56</sup> Nakaso, H. (2015). Asian Economy: Past, Present, and Future. Keynote Address at the Securities Analysts Association of Japan International Seminar ([https://www.boj.or.jp/en/announcements/press/koen\\_2015/data/ko150424a1.pdf](https://www.boj.or.jp/en/announcements/press/koen_2015/data/ko150424a1.pdf))

<sup>57</sup> Robertson, P. & Y. Longfeng (2016). China’s greatest challenge will be escaping the middle income trap. The Conversation (<https://theconversation.com/chinas-greatest-challenge-will-be-escaping-the-middle-income-trap-53567>)

<sup>58</sup> Agénor, P., O. Canuto & M. Jelenic (2012). Avoiding middle income growth traps. The World Bank (<http://siteresources.worldbank.org/EXTPREMNET/Resources/EP98.pdf>)

<sup>59</sup> Agénor, P., O. Canuto & M. Jelenic (2012). Avoiding middle income growth traps. The World Bank (<http://siteresources.worldbank.org/EXTPREMNET/Resources/EP98.pdf>)

A separate but related challenge to growth faced by Asian economies is posed by the limits of the environment and the already visible costs of climate change. In many ways, this challenge is analogous to that of the middle income trap. Just as a growth strategy based on cheap labour cannot be sustained because it leads to an increase in the price of labour, a growth strategy based on the exploitation of natural resources cannot be sustained because it leads to the depletion of those resources. But unlike the middle income trap, the challenge of resource limitations and climate change is not well-documented by economists – rather, it is unprecedented. Following the same growth path as presently high-income economies may not be an option for Asia's aspiring economies.

The predominant attitude amongst Asian governments at the moment is “grow now, clean up later”<sup>60</sup>. This approach fits into the narrative provided by the Kuznets Curve theory, which posits that as economies grow, they first increase their pollution and damage to the environment as they discover and utilise dirty but efficient (in the narrow sense) technology; then, after reaching a certain level of development, the trend begins to reverse and cleaner technologies are adopted. The Kuznets Curve story fits nicely with the development of advanced Western nations, where the first industrial revolution occurred well before the consequences of environmental exploitation were known or observed. However, according to Chandran Nair, the situation facing Asia today is fundamentally different: “We are not looking at a static or slowly changing situation involving just a single environmental variable, but a massive and absolute rise in resource use and environmental impact arising from billions of people reaching consumption thresholds”<sup>61</sup>. Thus the consequences of environmental exploitation will be felt much sooner and more severely for Asian nations than it was for advanced Western nations.

Aside from the humanitarian consequences of environmental exploitation (including natural disasters and public health issues resulting from air and water pollution), the issue bears directly on the feasibility of future growth in Asia. A report by the United Nations Environment Programme (UNEP) warns that growth without environmental considerations could offset economic gains and future growth in the near future<sup>62</sup>. It also finds that between 1990 and 2014, climate change and extreme events have displaced millions of people costing US\$1 trillion in economic losses. In addition, Asian economies must deal with their increasing dependence on fossil fuels, especially in countries where traditional, carbon-neutral fuels such as biomass are being replaced<sup>63</sup>. Without adequate consideration for the resource limitations that Asia

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<sup>60</sup> Shah, V. (2016). Why green growth is the key to Southeast Asia's future. Eco-Business (<http://www.eco-business.com/news/why-green-growth-is-the-key-to-southeast-asias-future/>)

<sup>61</sup> Nair, C. (2011). Consumptionomics: Asia's role in reshaping capitalism and saving the planet.

<sup>62</sup> UNEP (2016). GEO-6 Regional Assessment for Asia and the Pacific. United Nations Environment Programme, ([http://uneplive.unep.org/media/docs/assessments/GEO\\_ASSESSMENT\\_REPORT\\_ASIA%20Wam\\_Edited.pdf](http://uneplive.unep.org/media/docs/assessments/GEO_ASSESSMENT_REPORT_ASIA%20Wam_Edited.pdf))

<sup>63</sup> Fueyo, N., A. Gómez & C. Dopazo (2014). Energy security, sustainability, and affordability in Asia and the Pacific. ADB Economic Working Paper Series No. 401

faces, GDP growth may be illusory. As Nair argues, “There is no point in raising people out of poverty to consume if their environment is not fit to live in”<sup>64</sup>.

#### 4.4 Alternative Scenario III: Regional Conflict

Asia’s history of conflict and tensions between nations threatens to undermine the Asian Century by exposing the region to major threats that can only be dealt with through regional cooperation and integration. It will not be enough for Asian nations to refrain from engaging in direct conflict with each other, rather, positive cooperation will be required to mitigate crises on several fronts: economic, environmental and political.

There are a number of plausible scenarios in which the region fails to cooperate sufficiently. The first, and most obvious, is if existing regional tensions escalate into full-scale conflicts. Potential sites of conflict include: the Korean peninsula, where tensions are raised over a nuclear North Korea; the South and East China Sea, where there are competing maritime claims; and the India-Pakistan border, where territorial disputes over the Kashmir region have already caused three wars in the 20<sup>th</sup> century<sup>65</sup>. These conflicts could escalate if nationalism continues to fuel provocative foreign policy in countries such as China, India, and Japan. Anti-Japanese sentiment in China, for example, has been linked to the CCP’s “Patriotic Education Campaign”, established in the aftermath of the Tiananmen Square uprising in 1989. A recent survey of 1,400 Chinese urban residents found 90% support for China’s maritime claims with over 40% support for sending troops to deal with crises in the Senkaku/Diaoyu Island and South China Sea disputes<sup>66</sup>. This form of nationalism is fuelled in part by China’s historical grievances, dating back to the period known as the “Century of Humiliation”, in which China suffered atrocities at the hands of numerous foreign enemies, including Japan.

Another factor that may precipitate conflict is erratic behaviour by a ‘rogue state’ such as North Korea. Repeated attempts to get North Korea to halt its nuclear programme have failed, and foreign policy experts struggle to understand what motivates the regime<sup>67</sup>. Even China, the regime’s biggest ally and provider of aid, has waning influence. The regime’s aggressive behaviour creates fear uncertainty, prompting nations to build-up arms, even if it does not lead directly to violent conflict. Japan, for example, which has been a pacifist nation since the second world war, has recently

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<sup>64</sup> Nair, C. (2011). Consumptionomics: Asia’s role in reshaping capitalism and saving the planet.

<sup>65</sup> Council on Foreign Relations (2016). Global Conflict Tracker (<http://www.cfr.org/global/global-conflict-tracker/p32137#!/conflict/conflict-between-india-and-pakistan>)

<sup>66</sup> Chubb, A. (2014). Exploring China’s “Maritime Consciousness”. ([http://perthusasia.edu.au/usac/assets/media/docs/publications/2014\\_Exploring\\_Chinas\\_Maritime\\_Consciousness\\_Final.pdf](http://perthusasia.edu.au/usac/assets/media/docs/publications/2014_Exploring_Chinas_Maritime_Consciousness_Final.pdf))

<sup>67</sup> Cha, V. D. (2009). What do they really want?: Obama’s North Korea Conundrum. *The Washington Quarterly*, 32:4 pp. 119-138



begun to normalise its military policy, partly prompted by North Korea's development of long range missiles<sup>68</sup>.

A second reason why regional cooperation may breakdown, or fail to develop sufficiently, may stem from domestic or international conflict arising out of resource scarcity. As has already been emphasised environmental limits are likely to be a key variable in the development of Asia this century. Dwindling supplies of key natural resources has been identified by a number of security experts as a potential source of conflict<sup>69</sup>. The uneven impacts of climate change are also likely to result in an unequal redistribution of natural resources, which may magnify the impact for some groups over others, perhaps leading to climate induced migration. It has been noted that this can aid rebel organisations in recruitment, which increases domestic conflict<sup>70</sup>. Such domestic conflict would have repercussions for the security and stability of the region. Furthermore, although rarer, international conflict over resources may also occur.

Water scarcity is of particular concern in this regard. The supply of water to states is often dependent on the actions of other states, thus giving one state the ability to cut off water supplies to the other (ie. Malaysia against Singapore)<sup>71</sup>. The impacts of climate change threaten water supplies as a result of flooding as well as severe droughts. Increased agricultural water demand will also put a strain on water supplies due to the use of irrigation techniques. Given the unpredictability of climate change, severe shortages cannot be forecast with any accuracy, but are a real possibility. Although few historical inter-state conflicts can be attributed directly to resource scarcity, resources play an increasingly important role in international affairs, especially with respect to energy security. China's manoeuvring in the South China Sea is a case in point.

Even in the absence of violent conflict, a lack of cooperation in Asia will expose the region to a number of economic and environmental threats. For example, regional cooperation with respect to energy security will be vital, given that, by 2035, domestic energy resources are predicted to meet less than 50% of Asia's annual energy demands<sup>72</sup>. Thus Asian nations will be forced to become dependent on each other in order to meet energy demands. A report by the Asian Development Bank highlights the importance of energy integration for improving security and affordability, but also notes unsustainability of Asia's "business as usual" approach to fossil fuel

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<sup>68</sup> Moore, G. (2008). How North Korea threatens China's interests: understanding Chinese 'duplicity' on the Korean nuclear issue. *International Relations of the Asia-Pacific* 8:1 pp. 1-29

<sup>69</sup> Mildner, S. et al. (2011). A literature review on natural resources and conflict. *International Journal of Conflict and Violence* 5:1 pp. 155-172

<sup>70</sup> Mildner, S. et al. (2011). A literature review on natural resources and conflict. *International Journal of Conflict and Violence* 5:1 pp. 155-172

<sup>71</sup> Smith, P. & C. Gross (1999). Water and Conflict in Asia. Asia-Pacific Center for Security Studies ([http://apcss.org/Publications/Report\\_Water&Conflict\\_99.html](http://apcss.org/Publications/Report_Water&Conflict_99.html))

<sup>72</sup> Fueyo, N., A. Gómez & C. Dopazo (2014). Energy security, sustainability, and affordability in Asia and the Pacific. ADB Economic Working Paper Series No. 401

consumption<sup>73</sup>. Asia's current CO<sub>2</sub> emissions intensity is one of the highest in the world (only Russia and the Middle East surpass it). With large coal reserves, this state of affairs could be maintained for a while to come – but only with disastrous consequences for the environment. As such, additional cooperation to steer the region toward sustainable energy consumption.

Regional cooperation is also important to protect Asian economies from the volatility of the global economy. According Razeen Sally<sup>74</sup>, director of the European Centre for International Political Economy (ECIPE), “South Asia is the most malintegrated region in the world ... and east and south Asia are much less integrated in finance than they are in trade and FDI”. Regional financial safety nets are needed to minimise the adverse effects of a global economic contagion for Asian economies. ASEAN offers a strong foundation for future economic integration in East Asia, although Sally notes that “it is way off-track to talk of emulating the “EU model” in terms of building common institutions and strengthening common policies”. In South Asia, initiatives such as SAARC are even weaker. Further integration is currently inhibited by a combination of geopolitical tensions (as outlined above) and lack of regional leadership.

Dealing with the major environmental and economic challenges of the 21<sup>st</sup> century and avoiding regional conflict go hand in hand for Asian countries. Regional cooperation will be vital to deal with climate change, transboundary pollution, energy security, economic volatility and inequality. Avoiding conflict will require deliberation and constructive diplomacy between powers. Many of the regional forums that already exist offer a promising foundation, but more will be needed to meet Asia's needs in the coming century.

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<sup>73</sup> Fueyo, N., A. Gómez & C. Dopazo (2014). Energy security, sustainability, and affordability in Asia and the Pacific. ADB Economic Working Paper Series No. 401

<sup>74</sup> Sally, R. (2010). Regional Economic Integration in Asia: The Track Record and Prospects. ECIPE Occasional Paper (<http://www.ecipe.org/app/uploads/2014/12/regional-economic-integration-in-asia-the-track-record-and-prospects.pdf>)

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