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MACROSCOPE

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Asia has the means to boost growth as manufacturing slows

The region must use a new model for expansion as it looks to speed up the integration of goods and services, trade and finance

Asia's slowing growth is poised to reshape the existing development model towards a more service-oriented and integrated economy.

Burgeoning domestic consumption and an economic recovery in the United States and Europe helped the region remain a major driver of the world economy.

However, the World Bank expects the East Asian and Pacific region to grow 6.3 per cent, 6.1 per cent and 6 per cent in 2018, 2019 and 2020 respectively, still faster than the world average but below the 6.6 per cent growth last year and 6.3 per cent in 2016. The International Monetary Fund and the Asian Development Bank also projected lacklustre growth.

In the short term, Asia's exposure to trade and foreign capital means it will suffer greatly from rising trade protectionism and financial tightening. Much of the growth slump can be ascribed to China entering the "new normal" of slower but quality growth. The double-digit growth before the 2008 financial crisis has settled into the 6 to 7 per cent band since 2015.

But even excluding China, Asia's growth slowdown will be broad-based in the long run.

First, labour supply is constrained by an ageing population. Japan will see its 127 million population shrink by a third by 2060, with 38 per cent aged above 65. Unfavourable demographic markers are also seen in emerging economies such as Thailand.

Second, industrialisation has stalled in some countries. Historically, a strong industrial base has been vital for low-income countries to transition to middle- or high-income status because manufacturing can absorb a large amount of unskilled labour from the agricultural sector. This has been the experience of Japan, South Korea, Taiwan and, recently, mainland China.

However, some Asian countries are experiencing what Dani Rodrik, a professor at Harvard University, calls "premature deindustrialisation". For instance, in Indonesia, the contribution of manufacturing (excluding oil and gas) shrank to 18 per cent of gross domestic product between 2011 and 2016, from 30 per cent before the 1997-98 Asian financial crisis. And even if these countries were able to establish a good manufacturing base, it no longer produces as many jobs, owing to labour-saving technologies.

Lastly, the development of global value chains plateaued in 2010. The hallmark of Asian growth was assisting the flow of capital and technology through regional production networks, lowering the barrier for developing countries to take part in and benefit from trade. But the rise of domestically sourced intermediates owing to industry upgrading, particularly in mainland China, coupled with anti-globalisation sentiment, poses a threat to that model.

Asia has to seek a new growth model, different from the traditional manufacturing-driven growth. Indeed, most services in the developing world are usually informal and non-tradeable, and the tradeable segments such as financial services and information and communications technology demand high-skilled labour. However, technological improvement and digitalisation have allowed services to be commoditised like goods in the global supply chain.

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The productivity of modern services – finance, transport and telecommunications – is comparable to high-growth manufacturing. The region must either increase international migration of low-skilled care workers or create large amounts of high-skilled jobs in the field of artificial intelligence.

With protectionism in the West unlikely to disappear soon, Asia, which views globalisation positively, looks set to speed up regional integration in goods and services, trade and finance. In fact, intra-regional trade and foreign direct investment reached 57.3 per cent in 2016, compared with 55.9 per cent between 2010 and 2015, according to the Asian Development Bank. And intra-regional cross-border tourism is becoming a new growth engine for countries such as Thailand and the Philippines. The trend is poised to continue.

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