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FINANCIAL INSTITUTIONS GROUP INSIGHTS

FUTURE OF ASIA IN A FRACTURED WORLD: CONVERSATION WITH PROFESSOR KISHORE MAHBUBANI



Geopolitics remains a key area of concern for financial institutions in 2023. At a luncheon hosted by ANZ's Financial Institutions Group (FIG) in Singapore, experts shared views on the global geopolitical landscape, and the long-term prospects for the paradigm dubbed the CIA (China-India-ASEAN) century.

ASIA IN A FRACTURED WORLD

Attended by executives from global banks, insurers, fund managers and private-equity firms, the discussion, titled 'Future of Asia in a Fractured World', featured Professor Kishore Mahbubani, Distinguished Fellow at the Asia Research Institute, as the keynote speaker. Joining him for a follow-on panel discussion was Khoon Goh, ANZ's Head of Asia Research, who offered his insights on the structural changes transforming the global economy.

FRAYING TIES

The world is becoming an increasingly complex place due to a confluence of factors threatening to upend a well-established geopolitical order built up over the last few decades. This will have a long-lasting impact on the global economy, according to the experts at the event.

"We're facing unprecedented events with the ongoing conflict in Europe, the climate commitments being made globally, and the geopolitical shifts influencing economies in this part of the world," Mark Harding, Global Head of Financial Institutions Group at ANZ, said.

While the ongoing European conflict is driving up energy prices and forcing some countries to reconsider their climate commitments, in Asia, tensions between the US and China are also simmering, Mahbubani said.

"No matter what happens, the US-China geopolitical contest will gain momentum," he said, referring to a millennia-old theory¹ which posits conflict is a likely outcome when an emerging power seeks to displace the incumbent.

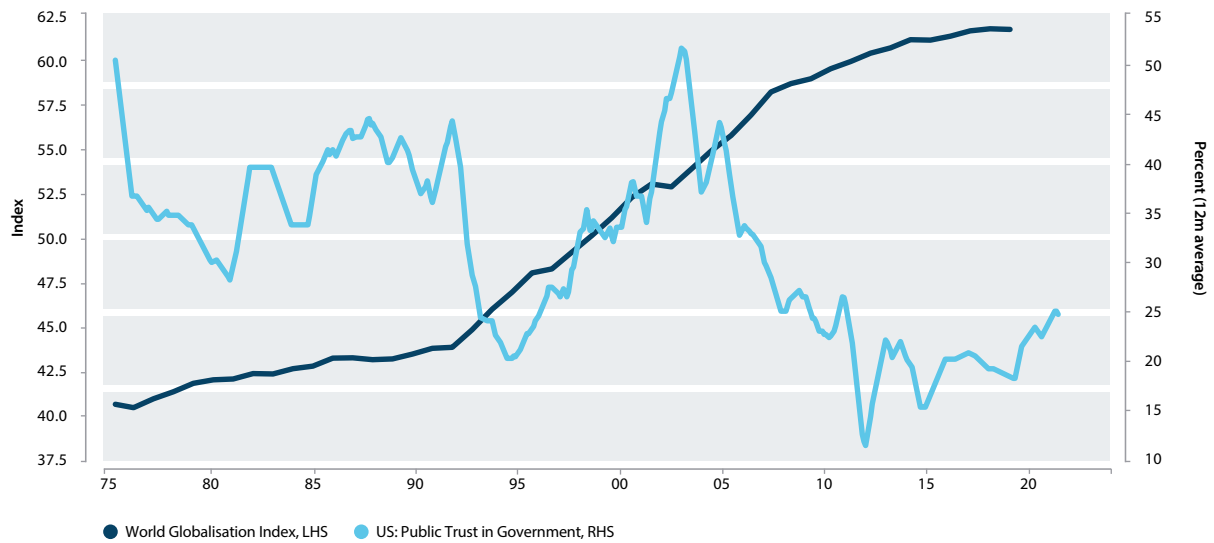
While a global order where both China and the US continue to grow and flourish is a possibility, it will require America to focus on cooperating on common goals while competing in areas of strategic interest, Mahbubani said.

Meanwhile, as the schism between the two superpowers widens and the US attempts to develop a long-term strategy to manage the rise of China, globalisation could be the casualty, Mahbubani and Goh agreed.

**FURTHERMORE, GOH NOTED, WITH SOME
FREE-TRADE AGREEMENTS LOSING
DOMESTIC POLITICAL SUPPORT, THERE
IS A RISK COUNTRIES TURN INWARD AND
SET UP BARRIERS TO OFFSHORE TRADE,
PUSHING UP PRODUCTION COSTS.**

¹Note: Referring to Thucydides Trap

FIGURE 1:
World Globalization Index

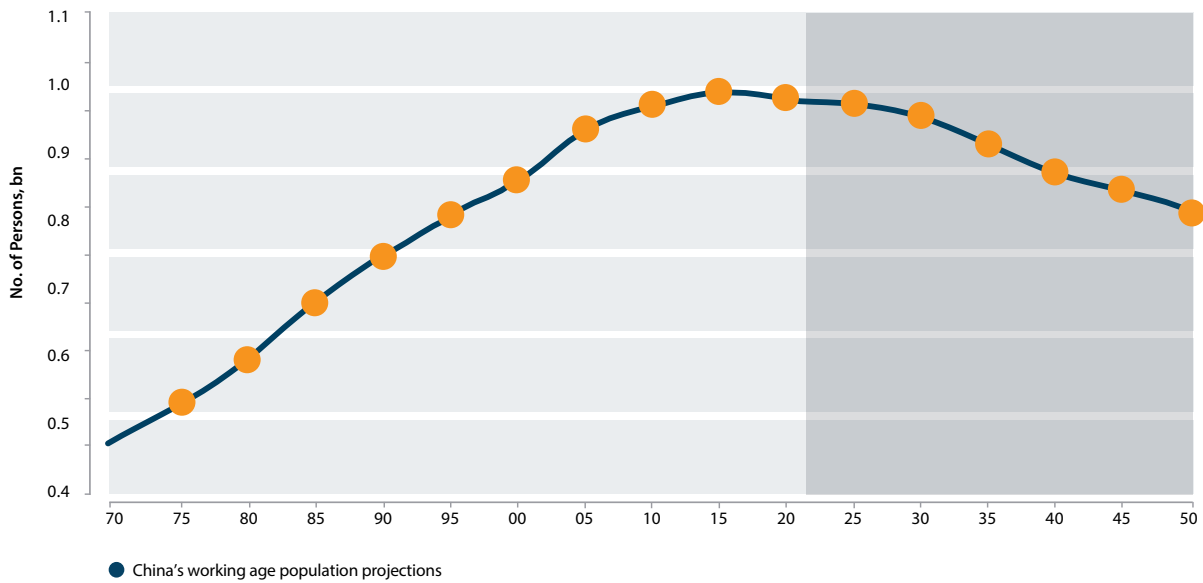


Source: KOF, Pew Research Center, Macrobond, ANZ Research

THIS IN TURN COULD HASTEN THE DEMISE OF A PRIMARY DRIVER OF GLOBAL GROWTH - THE LOW-INFLATION ENVIRONMENT - WHICH WAS MAINLY SUPPORTED BY CHINA'S MASSIVE AND RELATIVELY INEXPENSIVE WORKFORCE PRODUCING LOW-PRICED GOODS FOR THE WORLD TO CONSUME, EXPLAINED GOH. WHILE THIS DEMOGRAPHIC DIVIDEND ENSURED THE COUNTRY BECAME THE ECONOMIC POWERHOUSE IT IS TODAY, CHINA'S SHRINKING POOL OF CHEAP LABOUR, FOLLOWING THE COUNTRY'S ASCENT INTO THE UPPER MIDDLE-INCOME NATION CATEGORY², WILL NOT HELP RESURRECT GLOBALISATION AS WE KNOW IT, GOH SAID.

²Source: <https://www.worldbank.org/en/country/china/overview#2>

FIGURE 2:
Demographic Shift in China



Source: World Bank, Macrobond, ANZ Research

Additionally, as extreme weather events and the European conflict push up energy and commodity prices, “the world is experiencing inflationary pressures that it has not seen since the 1970s,” Goh said.

These challenges, given their structural nature, cannot be addressed by traditional monetary policy levers and will blunt the ability of central banks to tame inflation, he added.

“We have to be prepared for a period ahead where inflation is going to be structurally higher than what we have experienced in the last two or three decades,” Goh said. “I’m not talking about double-digit inflation, but inflation higher than what we’ve grown accustomed to.”

THE CIA CENTURY

The answer to taming inflation could be found in our region, according to Goh. India, the south Asian emerging market giant, which stands poised to reap the kind of demographic dividend enjoyed by China for decades, can serve as a deflationary force and help fuel global growth, he said.

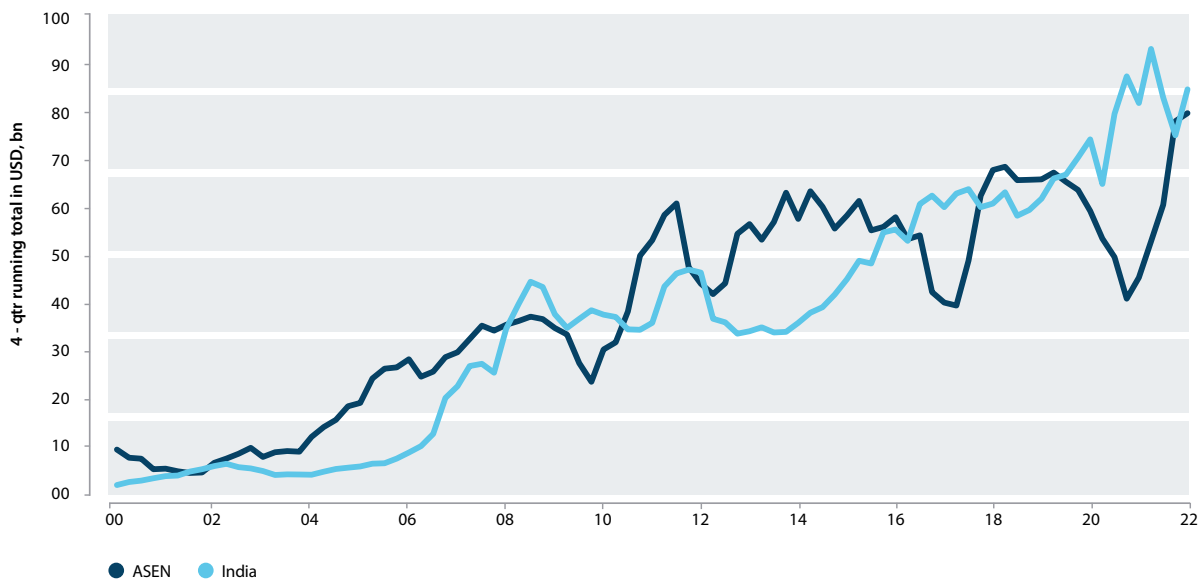
As the wind turns in India’s direction, investors sense an opportunity on the subcontinent if recent changes in Asia’s FDI inflows are anything to go by.

While foreign investments into ASEAN have grown as businesses execute their ‘China-plus-one’ strategy, India has surpassed other Asian economies in attracting FDI inflows.

“We are starting to see a reallocation of FDI flows away from China towards other countries,” Goh said.

“INDIA, FOR EXAMPLE, HAS SEEN MASSIVE FDI INFLOWS IN THE LAST FEW YEARS ESPECIALLY AFTER THE MODI GOVERNMENT CAME INTO POWER AND BEGAN MAJOR ECONOMIC REFORMS.”

FIGURE 3:
FDI Inflows into India and ASEAN



Source: State Bank of Vietnam, BI, IMF, DOSM, BSP, BOT, RBI

According to Mahbubani, while investing in India is still a challenge due to bureaucratic hurdles, the country offers a viable alternative to China as companies, especially American ones, seek to limit their China exposure and look for alternative bases in the region.

While India has not yet wholeheartedly embraced globalisation – refusing to join³ the Regional Comprehensive Economic Partnership (RCEP) and most recently shunning trade talks⁴ with the 14-nation Indo-Pacific Economic Framework – internal reforms implemented by Prime Minister Narendra Modi have led to optimism among domestic as well as foreign investors, and contributed to a bullish outlook for the country's economic growth.

At the same time, ASEAN will be the other beneficiary of the 'China-plus-one' strategy and will do well over the long term, according to Mahbubani. He noted the bloc – one of the most diverse economic groupings in the world – had managed to advance economically in the last two decades.

For example, the ASEAN economy has narrowed its GDP gap with Japan⁵ from eight times in 2000 to 1.5 in 2020. By 2030, ASEAN's GDP is expected to surpass that of Japan's.

The bloc's unity - and maintaining the region's neutral stance in the face of pressure from US and China to choose sides - will be crucial to maintaining its growth trajectory, Mahbubani said.

While India and ASEAN work on cementing their path to greater relevance on the global stage, China is expected to tackle macro issues such as a struggling property sector and the slowing economy.

"China might go back to its pragmatic self, and find solutions for the challenges they face," Mahbubani predicted. "In the next 10 years, global economic growth will be driven by the new CIA. - not the Central Intelligence Agency, but China, India and ASEAN."

For Singapore, perennially vying for regional hub status with Hong Kong and billed as the capital of the CIA., these developments will be highly beneficial, the speakers agreed.

"The region's attractiveness to foreign investors and capital remains as strong as ever," Goh said. "If ASEAN, India and China prosper, Singapore will too."

³ Source: <https://www.eastasiaforum.org/2022/04/13/indias-rcep-exit-and-its-regional-future/>

⁴ Source: <https://www.bloomberg.com/news/articles/2022-09-09/india-avoids-trade-negotiations-with-us-led-indo-pacific-group?ref=C3PowTFL>

⁵ Source: <https://ari.nus.edu.sg/app-essay-kishore-mahbubani/>

NEW OPPORTUNITIES

While the CIA grouping may be well-placed to drive future growth, the world must first reckon with three major challenges in the near-term, according to Mahubani: inflation, China's zero-Covid policy, and the European conflict.

For Goh, if high inflation rates sustain over the next five to ten years, they will have important implications for monetary policy. With central banks exhausting their options to control inflation, they will have limited flexibility to leverage aggressive interest rate cuts to cushion the blow from the next economic crisis.

Furthermore, the transition to net-zero is expected to keep energy prices high, as investments in new technologies will take time to show results.

Yet, there is also immense opportunity if businesses choose to look beyond the short-term volatility and position themselves for the long term, observed Yeekei Chan, ANZ's Head of Financial Institutions Group, Singapore.

The role of the financial services industry is to keep the wheels of the global economy turning, he said, by facilitating the smooth flow of capital and goods around the world.

"The positive news is, the financial services industry has a strong track record of responsiveness and agility in navigating complex challenges," Chan said.

"And we find opportunities when we collaborate with each other."

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