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## Riding first class on Asia's middle class

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AS EACH year passes, Australia has more riding on Asia's success. Even after the once-in-a-century commodities boom now reshaping our economy passes, Asia's new middle class will be a key to our prosperity. In recent months Australia's economic guardians in the federal Treasury have repeatedly reminded us this will be the source of new opportunity for Australia - a massive potential market for knowledge-based exports such as education, high-end manufacturing, services such as tourism, and rural commodities.

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But how rich will Asia become? At the moment there are striking economic disparities. In 2010, per capita GDP of Singapore - Asia's richest country - was 45 times that of Nepal, the poorest.

Asia's emergence is not pre-ordained and economic history tells us that there will be many ups and downs along the way. The nations of Asia will have to negotiate a raft of political challenges if the rosiest economic forecasts are to be realised.

The "middle-income trap" is one of the big dangers. This syndrome is illustrated by the relative performance of Brazil, South Africa and South Korea.

Back in the mid-1970s, South Korea had a GDP per capita well below that of Brazil and South Africa. But during the 1980s South Korea experienced a development takeoff.

Its GDP-per capita surged from less than \$US4000 in 1985 to well above \$US20,000 by 2008. South Korea now ranks among the world's 25 wealthiest nations with a per capital income higher than New Zealand's, according to the International Monetary Fund. Brazil and South Africa, on the other hand, have had bursts of growth followed by periods of stagnation and even decline. They've been caught in a middle income band between about \$US3000 and \$US8000 since the mid-1970s.

A raft of other developing countries have fallen into the middle-income trap because they have been unable to make the difficult transition from growth driven by low-cost labour or resources exports to productivity driven growth. This has left them unable to compete with low-income, low-wage economies in manufactured exports and with advanced economies in high-skill innovations. The stagnation and turbulence experience by the Latin American economies in the 1980s and 1990s illustrates the potential dangers of the middle income trap.

Asia's march to prosperity will be led by the "Asia seven" - China, India, Indonesia, Japan, South Korea, Thailand and Malaysia. Only two of those - Japan and South Korea - are already developed. Malaysia and Thailand are already arguably in the "middle-income" category and the rest are fast approaching. To avoid the middle income trap they will have to improve their ability to innovate, dramatically upgrade their industrial structure and reduce income inequality.

A recent study by the Asian Development Bank posed two economic scenarios for Asia by mid-century.

Under the first, Asia continues on its recent trajectory of historic economic transformation. The second assumed the region's fast growing economies fall into the middle-income trap over the next 5-10 years.

The contrast between the two is huge. Under the first scenario, per capita incomes rise sixfold in purchasing power parity (PPP) terms and vault 3 billion additional Asians to affluence on a par with Europe and North America. Asia's combined GDP reaches a mighty \$US174 trillion by 2050 or 52 per cent of the projected global total. Under this best-case projection Asia would regain the dominant economic position it held 300 years ago, before the Industrial Revolution.

But under the alternative "middle income trap" scenario the region's GDP will reach only \$US65 trillion by 2050, or 31 per

cent of the projected global total. In that event Asia's GDP per capita would be \$US20,600 (PPP) by mid-century rather than the \$US40,800 reached under the first case.

The ADB warns that "would deprive billions of Asians of a lifetime of affluence and well-being".

It wouldn't be too good for Australia either.

*This story was found at: <http://www.smh.com.au/business/riding-first-class-on-asias-middle-class-20110905-1ju4r.html>*