

University of Stellenbosch Business School – Executive Development

Assignment Cover Page

Surname: FORSTER
Initials: DA
Telephone number: 083 456 4855
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Facilitator: Prof A Roux
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CERTIFICATION

I certify the content of the assignment to be my own and original work and that all sources have been accurately reported and acknowledged, and that this document has not previously been submitted in its entirety or in part at any educational establishment.



Dion Forster
14302470

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1. Introduction.

Economics, and more specifically changes in the world's economy, have become a hot topic for debate, discussion and research in recent months. Whereas such topics may have had less popular interest in better economic times, there are now far more persons who are making the effort to understand the principles and consequences of economic shifts and changes in the world. The world economic crisis of the last two years has had tangible consequences for so much of the world's population. As the economic superpowers have strained under the weight of the recession the ripple effects have been felt in households all across the globe. What is certain is that there is a marked shift in economic power from the traditional economic superpowers towards certain emerging economies.

This paper will explore these shifts in the global economic power balance. In doing so it will present and discuss some the basic principles of economics. It will also be necessary to consider some historical perspectives on the current world economic situation. This foundation will form the basis from which to make some considered projections of how the global economic power base will shift in the next decade (towards 2020). In conclusion some attention will be given to an evaluation of the factors that are contributing towards this global economic power shift.

Before commencing with the abovementioned discussion I would like to make a brief comment about the referencing style employed in this paper. In the interest of expediency I have employed an internationally accepted referencing standard with which I am most familiar; namely a version of the Chicago Manual Style¹. All references will be provided in a full and consistent manner in footnotes at the bottom of each page.

2. What is 'economics' and how has it shaped the current economic world balance?

In order to more fully understand the projected shifts in global economic power that will be discussed in section 3 below it is necessary to consider the current economic situation by way of reference to the economic theory and history of the economic systems that underpin it.

¹ Please refer to University of Chicago (2007). "[The Chicago Manual of Style Online](http://www.chicagomanualofstyle.org/home.html)". [History of the Manual](http://www.chicagomanualofstyle.org/home.html), and [What's New](http://www.chicagomanualofstyle.org/home.html). The University of Chicago. <http://www.chicagomanualofstyle.org/home.html> (accessed 26 July 2009, 10.09).

A. What is economics? An analogous definition.

In its most basic form economics "...is the study of the way in which human beings employ scarce resources... to satisfy their many needs"². Thus, as this definition points out, economics is a study of 'an economy' in which persons make choices about how they shall employ the resources they have in order to gain what they want or need. One of the simplest and clearest explanations of the etymology of the word 'economy' that I have read comes from Botman who says, "The term *economy* derives from the Greek terms *oikos* and *nomos* (meaning management of the *oikos*). The Greek term *oikos* is normally translated with the English term *household* but can also mean *community*"³. If one were to employ an analogous definition of economics it can be likened to the management of a household budget – one has a specific income and some specific needs and wants. Based on these factors one must decide how to use this income to gain the goods and services that are wanted and needed in order to run the household.

B. What makes a nation economically powerful?

This basic understanding of economics, as presented above, relates quite well to the manner in which nations manage their economies. A nation has to manage its income, its debt, and its services and resources in order to gain the goods and services it needs for its population to survive (and hopefully even to grow). The world's nations tend to manage their economies within three broad approaches⁴:

- The *traditional* system in which decisions about the economy are made on the basis of traditions that are carried down through the generations. Growth is not of great importance in this model.
- The *command* system. The most common example of this is communism where, as the term suggests, decisions are made by the command of a few on behalf of a larger community.
- Last, there is the *free market* system (frequently called 'capitalism'). This is based on the idea that a household, or a business, has the freedom, and the

² Roux, A. *Everyone's guide to the South African economy*. 9th edition. Zebra Press. Cape Town. 2008:4.

³ Botman, RH "Covenantal Anthropology: Integrating Three Contemporary Discourses of Human Dignity" in *God and human dignity*. Kendall Soulen, R and Woodhead, L. Wm B Eerdmans Publishing. London. 2006:80.

⁴ Roux, A. *Everyone's guide to the South African economy*. 9th edition. Zebra Press. Cape Town. 2008:6.

right, to grow their economic base by engaging in trade. The exchange of goods and resources is done carefully and should hold mutual benefit for the parties involved.

In relation to the topic of this essay one could apply a further analogy to understand the relationship between *power* and *economy* in the world's economic system. If one had a number of households (countries) living in a village (the earth) one would find that each household would be subject to a variety of factors that determine their economic power. Amongst others, these would include⁵:

- The household's income or wealth: Some households would have a higher income that can be used to buy goods and services for the members of the household, while other households would have less income to do so. Economic power increases in situations where income increases, or in situations where income exceeds the necessary requirements for sustaining the household. It would make sense that a household should have a greater income than the required expenses in order to be economically healthy.
- The household's debt: Sensibly, even if a household had a good income but had to use a large portion of that income to service debt, that household would struggle to grow economically (i.e., in this instance growth is equated with meeting and exceeding the needs and wants of its citizens. If there are not sufficient resources to do so the economy will either stagnate or shrink).
- The population of each household in relation to their income: Economic growth is stunted in a situation where the population increases and the income remains the same or decreases, thus placing a greater demand on the available resources within the household. The net effect is that each member of the household gets a smaller share of the available resources as the number of persons in the household grows.
- The household's skills and resources: Skills and resources make up a significant part of economic power. If a household has resources that they can sell to others to generate income, or has a particular set of skills out of which they can generate income, it stands to reason that they will grow economically as long as these are well managed and traded fairly with other households.

⁵ For a detailed discussion of these concepts please refer to Roux, A. *Everyone's guide to the South African economy*. 9th edition. Zebra Press. Cape Town. 2008:9-24.

In summary all of the factors above have to do either with wealth (the relationship between income and expenditure needs), or sustainability (development of skill, the careful management of human and natural resources), or a combination of these two factors.

The wealth of a household is made up not only of their capacity to earn an income (Gross National Income or GNI), but also their available assets both (this is the value of income derived within the geographic borders of a country, most frequently referred to as the Gross Domestic Product or GDP), and the capacity to leverage these assets to finance development and growth (borrowing money to buy better equipment to plough their field, or borrowing money to send their children to university to study and gain valuable skills)⁶. Furthermore, if a household is made up of more than one family, there is a need to maintain some flow of money between the families in a household to stimulate the spread of resources and development. It does not help that only one member of the household is wealthy while the rest, who are also expected to contribute towards the growth of the household's economic power, are impoverished and are unable to contribute towards the growth of the household.

Thus, the nations with the greatest economic power are those that are currently most wealthy (measured in total GNI, which includes GDP) and most sustainable. In the section that follows I shall discuss the notions of global economic wealth and sustainability in relation to the world's most powerful economies at present (2009/2010).

3. What does balance of world economic power look like at present?

The world's wealthiest nations are currently the following⁷:

⁶ For an accessible introduction to national wealth, with some tools that compare the costs of services and goods in different nations (Purchasing Power Parity, or PPP), please see <http://www.geographyteachingtoday.org.uk/ks3-resources/resource/who-wants-to-be-a-billionaire/how-do-we-measure-a-nations-wealth/> (accessed 27 July 2009, 13.21).

⁷ Slide from Roux, A *SMP 2009 (Powerpoint Presentation)*. Slide number 8. Detailed figures and statistics are available from <http://siteresources.worldbank.org/DATASTATISTICS/Resources/GDP.pdf> *The world bank development indicators database, 1 July 2009. Gross domestic product (2008) (accessed 27 July 2009, 19.04)*. Naturally one could spend a great deal of time discussing and analysing these figures. However, at this point it is only necessary to make the point that certain economies are stronger and wealthier than others based on the factors discussed in section 2

The who's who of the world economy
World Bank, 2009

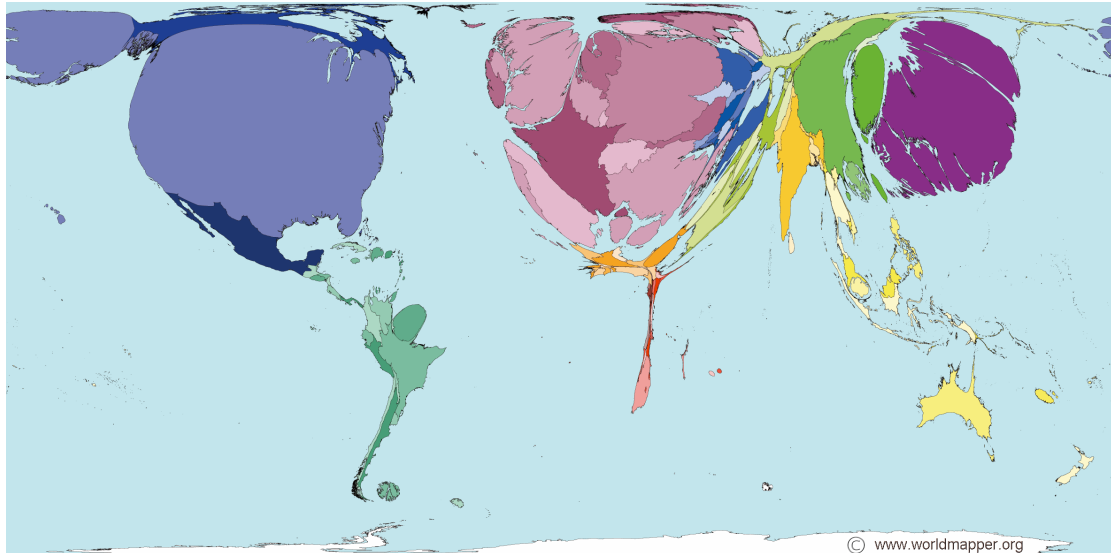
Rank	Country	GNI as % of world (PPP) 2007 (65 752)	Cumulative share of world GNI	Population as % of world 2007 (6 610)	GNI per capita (PPP \$) 2007
1	USA	21.0	21.0	4.6	445 840
2	China	10.9	31.9	19.9	5 420
3	Japan	6.8	38.7	1.9	34 750
4	India	4.7	43.4	17.0	2 740
5	Germany	4.3	47.7	1.2	34 740
6	France	3.2	50.9	0.9	33 850
7	UK	3.1	54.0	0.9	34 050
8	Russ Fed	3.1	57.1	2.1	14 330
9	Italy	2.7	59.8	0.9	30 190
10	Brazil	2.7	62.5	2.9	9 270

©US/A Roux 2009

This chart shows each of the top ten nations wealth (GNI) in relation to the size of their population. If one were to represent this wealth graphically overlaid on a map of the world (to illustrate the comparative wealth of the world's nations by geographical territory) it would look like this⁸:

of the paper above. I would encourage the reader to read the World Bank's detailed report for detailed information on these statistics.

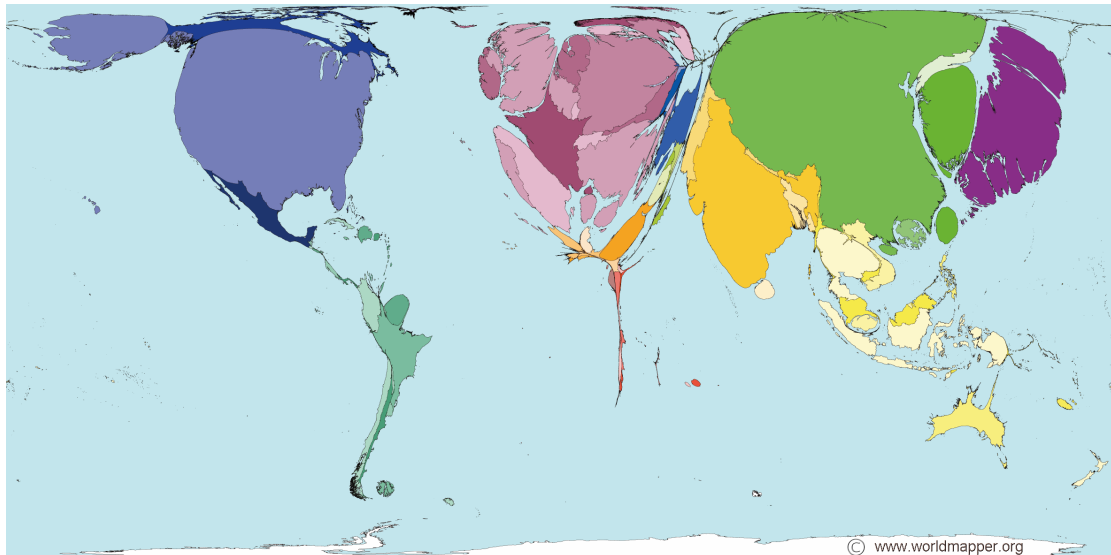
⁸ This image comes from <http://www.sasi.group.shef.ac.uk/worldmapper/display.php?selected=169> and represents GDP wealth graphically in 2002. A detailed Excell spreadsheet of this data can be downloaded from here http://www.sasi.group.shef.ac.uk/worldmapper/data/withmap/169_worldmapper_data.xls (accessed 27 July 2009, 13.43).



Notice the difference in wealth between countries in the Northern Hemisphere (particularly North America and Europe) in relation to countries in the Southern Hemisphere (Latin America and most of Africa). This map illustrates that currently the countries with the greatest wealth are developed countries in Europe and North America – this is where the world's economic power lies at present.

However, in the previous section we said that ongoing economic power lies not only in current wealth. Whilst one may be wealthy at present, if this position is not sustainable, or sustained, other countries will soon occupy these places of economic dominance in the globe. The following map displays the geographical territories that have charted the greatest economic growth between 1995 and 2002⁹:

⁹ This map comes from <http://www.sasi.group.shef.ac.uk/worldmapper/display.php?selected=171> it represents percentage growth in geographical territories in a comparative graphic format. Detailed statistics can be found in the follow Excel spreadsheet: http://www.sasi.group.shef.ac.uk/worldmapper/data/withmap/171_worldmapper_data.xls (accessed 27 July 2009, 14.02).



It is worth noting that on this map the Asian economies (India and China) dominate. In other words, Japan's growth has remained fairly constant, Africa's growth has not been significant at all, while Europe and North America have not grown as fast as India and China. Not the spatial representation of China (Green) in this map in relation to the United States and Europe.

Having presented the current world economic power statistics I shall now move on to present some projections of world economic power shifts towards 2020.

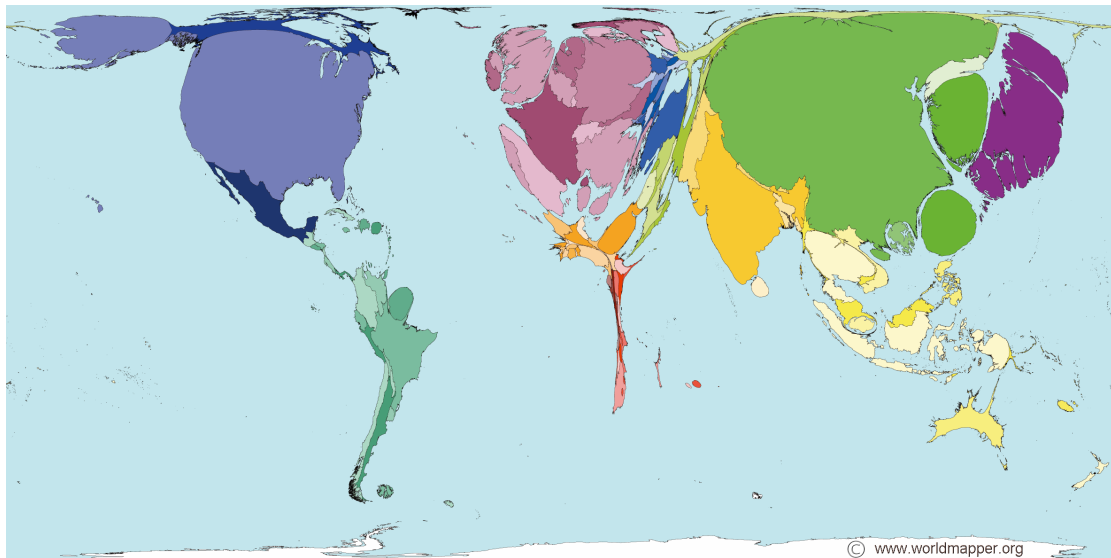
4. A projected perspective on the balance of global economic power in 2020.

In the previous point it was clearly shown that the economic power of certain countries, particularly China and India, has grown much more effectively than other countries. In particular it was suggested that if the trend of global economic growth continues as it did between 1995 and 2002 then the global economic power landscape would differ drastically from what it currently is.

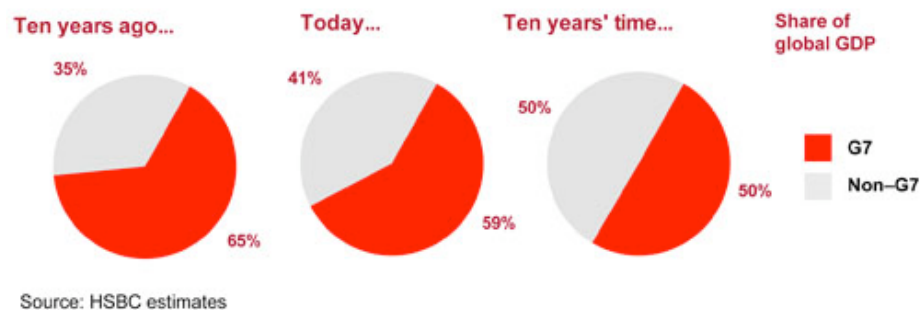
A. The changing landscape for world economic power.

The following map shows a projected picture of what the world's economies will look like in 2015 based on GDP¹⁰.

¹⁰ This map comes from <http://www.sasi.group.shef.ac.uk/worldmapper/display.php?selected=164> and it represents the projected economic power of the world's economies in 2015 based on geographical territory. A detailed spreadsheet of the figures that make up this map can be found here:



What is most striking in this visual representation of global economic power shifts is the absolute dominance of the Chinese economy across the globe. HSBC made the following chart to show the shift in global economic power between the G7 and non G7 nations from 1999 to 2009, and then projected towards 2019



In 1999 the G7 nations controlled 65% of the world's GDP, in early 2009 they had slipped to 59% and the projection is that they will have a share of only 50% of the world's GDP by 2019¹¹.

B. Some suggested reasons for these changes:

http://www.sasi.group.shef.ac.uk/worldmapper/data/withmap/164_worldmapper_data.xls (accessed 27 July 2009, 14.23).

¹¹ Please refer to *A new evolving economic stage*

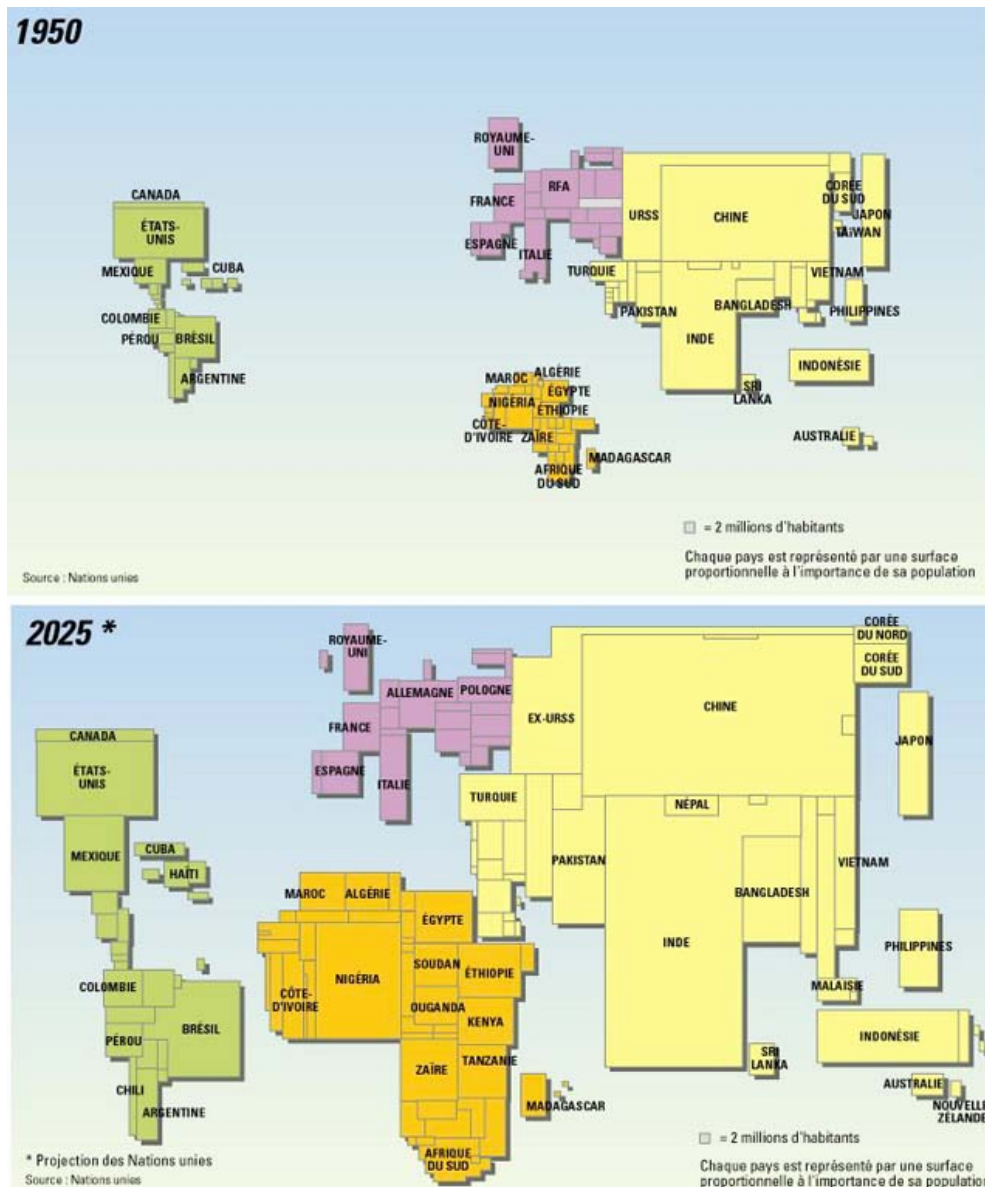
http://www.hsbcnet.com/solutions/emerging-markets/evolving_economic.html (accessed 27 July 2009, 15.07).

What accounts for these shifts in global economic power? As was suggested in section 2 above, a shift in economic power is as a result of changes in the relationship between wealth and sustainability. Factors that influence such changes are a decreased capacity to generate national income, an increase in serviceable national and international debt, a shift in available resources (both human and natural resources) and issues of sustainability. HSBC notes that “Emerging markets represent approximately 80 per cent of the world’s population and 20 per cent of the world’s economy”¹², it is not surprising then, when one considers the growth in emerging economies, and the availability of human resources to fuel income and expenditure in these economies, that one begins to understand why the world’s largest nations (India and China) are showing such remarkable economic growth¹³. Thus it is necessary to note that there is a significant difference between ‘large’ emerging economies (such as China and India) that are charting growth by their sheer dominance in the global economic markets, and ‘small’ emerging economies (such as those in Latin America and Africa) that while they are charting some growth it is comparatively small on a global scale. Population numbers are a critical contributor to the shift in economic power. The following graphic shows the projected population growth of the nations in the world by comparing population statistics from 1950 to 2025¹⁴.

¹² Please refer to *A new evolving economic stage* http://www.hsbcnet.com/solutions/emerging-markets/evolving_economic.html (accessed 27 July 2009, 15.07).

¹³ For a detailed academic discussion of the notion of ‘developing’ economies and ‘emerging’ economies please refer to Bensidoun, I; Lemoine, F and Unal, D “The integration of China and India into the world economy: a comparison” in *The European Journal of Comparative Economics* Vol. 6, no1, 2008:131-155.

¹⁴ From <http://sun-bin.blogspot.com/2005/12/map-world-population-and-gdp-scaled.html> each square equals 2 million inhabitants (accessed 28 July 2009, 05.36).

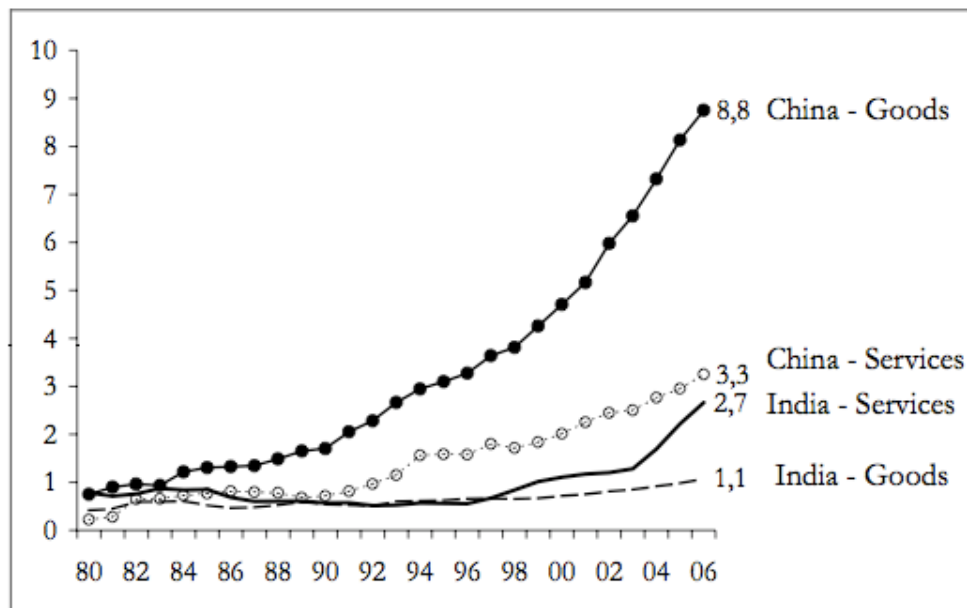


Clearly the growth of Asian populations is massive compared to most of the developed world. It is also worth noting that Sub-Saharan Africa is not showing massive growth in population – this is as a result of the projected impact of HIV/AIDS related deaths on the subcontinent.

What has made India and China such a significant competitor on the global economic stage has been a massive increase in trade and services as a result of changes in their economic policies in recent decades¹⁵.

¹⁵ Bensidoun, I; Lemoine, F and Unal, D “The integration of China and India into the world economy: a comparison” in *The European Journal of Comparative Economics* Vol. 6, no1, 2008:136.

Figure 1 - Share of China and India in world exports of goods and of services (%)



Source: Authors' calculations from CEPIL, CHELEM-GDP database.

In short they have moved into the production of high tech goods and low cost expert services. India has, however, lagged behind China somewhat in the production of goods and services. China is the largest producer of goods in the world, whilst India is second only to Brazil. However, at the rate at which Indian and China are growing in both goods and services production they will both quickly leave Brazil and Mexico behind¹⁶ (China already out-produces all other nations in the world).

This reality will significantly shift the base of economic power in the next decade.

5. Conclusions.

The discussion above is by no means exhaustive. However it has illustrated what factors account for a position of dominance and economic power within the world's economy. Taking these concepts into account it made some predictions to show that the world's large emerging economies would grow significantly in global economic power towards 2020 as a result of sheer numbers and a dominance in the production of goods and services. The current economically powerful nations in Europe and North America are likely to suffer the effects of national and international debt,

¹⁶ Bensidoun, I; Lemoine, F and Unal, D "The integration of China and India into the world economy: a comparison" in *The European Journal of Comparative Economics* Vol. 6, no1, 2008:137.

coupled with an aging population and diminishing natural and human resources. Other smaller emerging economies are not likely to show significant growth as a result of the challenges of sustainability, in Africa these are related most specifically to international debt and the impact of HIV/AIDS. What is clear across the board is that the strongest economies in the world will be dominated by goods and services. As such, any economy that wishes to grow will need to be prudent in managing its spending and debt, placing as much money as it possibly can towards developing both products and skills (or harvesting its resources) to stimulate internal and external economic growth.
