The InsightBureau

Café Insights

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As part of the Café Insights series of interviews with insightful speakers, The Insight Bureau recently caught up with Dr Yuwa Hedrick-Wong, Senior Fellow at the Lee Kwan Yew School of Public Policy, National University of Singapore, and Global Economic Advisor to Mastercard International. I asked Yuwa about the state of the world economy, whether the US-China 'trade war' would threaten this, and how Asia's economy is shaping up.

Andrew Vine (AV)	Well, hello and welcome to another in the series of Cafe Insights. I'm Andrew Vine, Managing Director of The Insight Bureau, and today I'm in conversation with Dr. Yuwa Hedrick-Wong. How are you?
Yuwa Hedrick-Wong (YHW)	Very well, thank you.
AV	Good to see you again. Yuwa is a global economist and business strategist. In fact, he's the chief economist and chair of the academic advisory council of Mastercard. Welcome back to Singapore. In fact, you're going to be quite a regular visitor next year.
YHW	Indeed, I will be.
AV	… having just being appointed a Senior Fellow at the Lee Kuan Yew School of Public Policy which within the National University of Singapore. Congratulations on that
YHW	Thank you very much.
AV	One of the things I really wanted to take the opportunity to ask you today --because it's a big topic of conversation --- is on global trade and the trade war with China that Donald Trump seems to be hellbent on pursuing. But before we do that, I would like to take a quick check on the state of the world economy; I always trust you to give me a straight answer on this! We seem to be doing okay. The US economy is doing okay, Europe as well and Asia …
YHW	The operative word, Andrew, that you said is it "seems" to be ...
AV	Okay ...
YHW	What's going on in the US is that you've had a very long and slow -- and in fact anaemic -- recovery since 2008, through 2009. And then, just as the economy is gathering strength, as slowly we saw unemployment rate dropping down -- today it's more or less at full employment -- it's right at this upturn cycle that Donald Trump decided to pump this massive fiscal stimulus into the economy. It's as post-cyclical as you can get. So that's why all the vital signs are great! There's been such an amount of stimulus in the last two years, both with the tax cuts and then increased military spending. And now increased subsidies to all sorts of industries, that are perceived to be affected by his tariffs.

So, the American fiscal deficit is going to double in the next few years, and then, with such a post-cyclical spending, the whole thing is going to collapse. It's not sustainable! It's the wrong timing, the wrong thing to do, the wrong sectors to focus on ... It's all wrong, wrong, wrong. But in the short term, yes, it's looking just fantastic.

AV So, there's only one way the US economy should be looking, which is very strong, because of these reasons ..

YHW Completely, yes.

AV What about Europe?

YHW Well, Europe sadly, at the centre – the centre being Germany and to a lesser extent France -- is not holding. Merkel's position is seriously eroded. In fact, I think she's basically struggling to stay in power at this point. So, there's no chance of any kind of 'bold action' or big decisions to tackle the difficult reforms to make Europe more sustainable. Sadly, one of the deciding factors is that Europe is in no position to make concessions to the UK.

AV ... as it's racing towards March next year, when Brexit is supposed to happen …

YHW Yes, that's right, precisely. So, I would argue that the centre is folding, with the strongest leader in the Eurozone becoming inward-looking, which is the exact opposite of what they should be doing. Of course, when the centre is folding, that's when the fringes come alive with populists, the far-right and so on. It's going to be quite chaotic, I think.

AV Okay, and now racing across the world to Asia ...

YHW Well, I think Asia is the opposite. Quietly, without much media fanfare, my argument is that Asia is becoming the most economically integrated region in the world. A crude but useful indicator is to look at a percentage of trade that is transacted within the region: Asia is now number two in the world, second only to the Eurozone. And this is achieved without a pan-regional free trade agreement of any kind. In fact, intra-regional trade as a percentage total is higher than NAFTA, the North America free Trade zone! So, all kinds of new developments in terms of supply chains are drawing in, both the really, really high-income countries like Japan, South Korea, Singapore, with the very low-income countries, say, Laos, Myanmar, and others.

AV And I think it's fair to say that the Asia story was largely a China story for a long while -- and will always be -- but we also have ASEAN developing very strongly now ...

YHW ASEAN is, I think, taking a lead in pushing for regional economic integration. And increasingly, ASEAN, I think, is becoming a lot more synergistic with North East Asia; think about North East Asia as a region with an ageing population, but with surplus savings. So, what do they need? Well, they need to put their surplus savings to work to earn enough to meet the pensions liabilities of their ageing populations. So, the way to put that money to work is not at home, but in ASEAN ,so you have a very mutually beneficial, synergistic relationship being developed, and it's very good for the region.

AV The topic of the day I want to focus on now is the trade war issues and Donald Trump. I mean, first of all, my first question I guess is why is this even happening? I mean, what is Donald Trump thinking? Well, what are his thoughts behind taking this type of approach?

YHW Well, Donald Trump, along with his core supporters, have never believed international trade is beneficial to America. And America, being the largest economy in the world, being the leader of the free world, as it were, for so long and literally the champion of the liberal economic order, has been ripped-off by the others. So, the rest of the world are free riders! That's what they believe. So, any kind of rules-based, international system that treats America as one of the many is wrong. Donald Trump's agenda is to create bilateral relations in the way that he believes could benefit America; case-by-case, “let's make a deal!”. So that's what he's pushing the world into.

AV But when you talk about globalization, that hasn't benefited everyone, and this is one of the things he's latching on to, isn't it?

YHW Yes, absolutely correct. And what we often pay insufficient attention to is how globalization and technology have interacted in the last few decades to the disadvantage of specific segments of workers in high-income countries. Manufacturing is a case in point; back in the 1970s, a quarter of all jobs in the United States was in manufacturing, and in the 1970s up to the early 1980s, a job in manufacturing was the way for an American with a high school education or less to earn a middle-class income. It's literally almost the only option. The second one is driving a truck. And with the decline of manufacturing employment, at that speed and on such a scale, you can imagine … they have left a whole chunk of workers literally out in the cold.

AV So, if this carries on and it keeps escalating as it seems to be right now, what can we expect in terms of the effect on the global economy? What are we going to see shake out of this?

YHW Well, we're going to see Balkanisation. We're going to see the US increasingly absent in the international system of trade, as we have understood it, and regional integration will take place. And again, earlier I mentioned Asia and that's going to continue. You see the global supply chain supported by rapidly advancing technology, and it has changed how we produce things. So, Donald Trump's paradigm is still very much a country-based production story; you have a country that can produce A, B, C, and then another country that produces X, Y, Z and they trade. The problem today, for people like Donald Trump, is that by the time the product is made, it's probably been traded about 27 times between 10 countries or more! So it’s the supply chain that literally taps into the smallest bit of comparative advantage and leveraging for greater efficiency. Other countries will get increasingly involved in this intertwining of the deeper supply chains between countries, and the US will continue to be left out.

AV Is this going to knock whole percentages off global GDP, or is it just a redistribution do you think?

YHW Well, in the short term, in all the econometric models that I look at about the impact about the trade war, there's a strong consensus among them that the impact's minimal. But I think that's wrong, because what the models fail to take into account is the impact via deepening uncertainty, and investment sentiment. These are not captured by the models and I think they can do untold damage, seriously increase the volatility, I think, in the global economy.

AV Is part of this also Donald accusing China as being a currency manipulator? The first thing he said he was going to do when he took power was to take issue with this …

YHW Well, his primary economic advisers actually believe that China is far more than just a currency manipulator, that the entire system of China's production is unacceptable. That's why you have a situation where Trump seems to be at least open to some kind of compromise with Europe, with Mexico, with Japan and so on, but not with China. The issue with China is not simply the issue of trade deficit; it's that China is actually the only country in the world today that can challenge the US in terms of global dominance. And that's a deep issue for Donald Trump: how do you stop China's rise? It is, I think, as deep as that.

AV We've kind of seen this before haven't we? If we think back to the 1980s, America was trying to stop Japan …

YHW Well, at least try to mitigate Japan's trade surpluses …

AV Yes, the trade surpluses …

YHW And of course Japan basically caved in! It accepted the so-called 'voluntary restraint' on car exports, and then when that did not work, agreed to the Plaza Accord, to basically engineer a tremendous appreciation of the Japanese yen against the US dollar. Now, talk about currency manipulation; that's the currency manipulation of the century, let me tell you! But the point is, is that it did not work. Japan continued to run trade surpluses against the US despite the voluntary restraint on exports, and in spite of the appreciation of currency.

AV And so China will be watching this as well, thinking the same thing ...

YHW Yes. There's absolutely no way China will follow Japan's path.

AV And then talking of China then: obviously the big question's going to be: how is China responding and how will it respond? Or are there things domestically in China that are going to prevent it from escalating its response?

YHW Well, China's response, essentially, is they're going to fight it out with the US, and they believe they can win. And it's interesting in a sense that China is already, before the trade war, in the process of upgrading its production, de-risking its dependency on exports, and encouraging stronger domestic demand, both in consumption and investment. So, I think what Donald Trump is doing is actually *accelerating* China's movement in that direction. In other words, making China stronger faster, and less dependent on the US.

AV And although China's economy is slowing, we shouldn't interpret that as being a negative at all, should we?

YHW No, I think it's natural. With China's per capita GDP at about US$10,000 now, it's totally natural -- and desirable – for growth to come down to about the 6% range. So, I think within China's policy circle, the debate has been, how do we substitute quality for quantity in terms of economic growth? And I think that's what they're getting. So increasingly better jobs have been created, higher value-added is built into the production process, and there's much stronger emphasis today on the quality of life, on environment, for instance. So, this headlong rush just to grow and create jobs is very much a thing of the past. And in so doing, China will become less and less dependent on low value-added exports. And also, focusing on the level of economic growth of China today, being alarmed at 6% -- oh my God! -- is completely wrong-headed. If you go back to 2010, at 10% GDP growth versus 6% today and you look at how much has been *added* in the economy, at 6% China is adding more; in fact, *double* what it added to the economy at 10% in 2010.

AV Well, Yuwa, it's a great pleasure to see you again. Thank you very much for answering my questions today and, we'll see a lot more of you next year in Singapore

YHW Thank you.

Dr Yuwa Hedrick-Wong is a global economist and business strategist, advisor and author. He presents on the world economy, emerging markets, inclusive growth, trade and investment, and China. He has been an economic advisor to MasterCard International and has served as the Chairman of the Academic Council for the Mastercard Institute of Inclusive Growth. He is now a Fellow of the Lee Kwan Yew School of Public Policy, NUS. He is based in Canada with extensive periods in Singapore. He is represented as an exclusive speaker with The Insight Bureau.

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