

To what extent has the world's economic and financial power moved from West to East?



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## Introduction

Just over thirty years ago, in November 1978, Deng Xiaoping, China's then leader, chaired a month-long 'work conference' of the Communist Party's Central Committee that is now seen as the beginning of China's economic and political reforms. This year, the People's Republic of China celebrates its 60<sup>th</sup> birthday and does so as a much different, much more economically powerful, country than that of 1978. Yet it is not just China that has become economically and financially much stronger in recent decades but a whole range of countries across the world, the majority of which lie in the East.

Few would dispute that the world's economic and financial power has moved from West to East but the extent of this movement is unclear without detailed examination, something that this essay addresses. The subject is particularly topical in light of the 'Credit Crunch', which many commentators have argued represents a rapid shift in power from west to east.

The 'West' is considered here as the United States, Canada, Western Europe, Australia and New Zealand. These countries from the early nineteenth century until relatively recently dominated the world's economic landscape. There is no single definition of the 'East' and so it is defined widely here, largely on a geographical basis. The economies of Asia, the Middle East, Eastern Europe and Russia have all been included. These countries have typically experienced much faster economic growth than the West in recent years<sup>1</sup>.

The essay discusses the key issues of Economic Output, Balance of Payments, National Wealth and Economic and Financial Influence. The impact of the Credit Crunch, which has shaken the world's economies, is then also considered. Through careful examination of the facts, it is demonstrated that, although there are significant exceptions, the movement of the world's economic and financial power from West to East has been on an enormous scale.

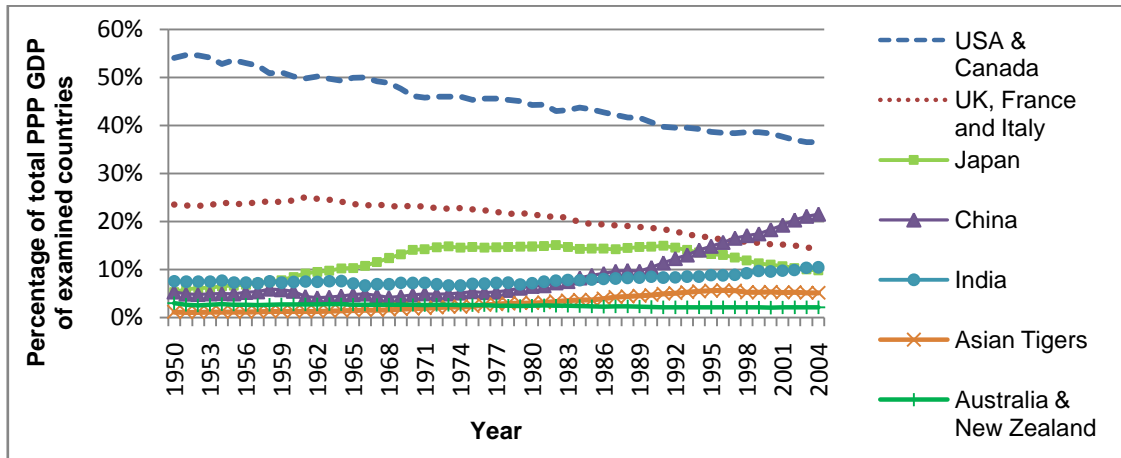
## Economic Output

The last two decades in the West have generally seen increasing prosperity. Economic growth has averaged 5% per annum<sup>2</sup>, disposable incomes have increased, and the service sector has boomed. Today, the United States still has by far the world's largest economy<sup>3</sup>, London and New York remain by far the most competitive cities for financial services<sup>4</sup> and the New York Stock Exchange remains by far the largest in the world<sup>5</sup>.

Yet, although the West has continued to grow, the East as a whole has grown faster so that the proportion of the world's economic power located in the East has increased at the expense of the West. This has been happening for over fifty years, starting with the Japanese 'economic miracle', followed by the rise of the 'Asian tigers'<sup>6</sup> and most recently continuing with China, India and many other countries (see Figure 1).

The extent of the economic shift can clearly be seen by examining Gross Domestic Product (GDP) data. Measured by Purchasing Power Parity (PPP<sup>7</sup>), the West's share of world GDP declined from over 50% in 1988 to 44.3% in 2008<sup>8</sup>. Over the same relatively short period, the East's share increased from 35.8% to 44.2%, meaning that today the East and West produce approximately the same amount (see Figure 2).

Figure 1: 1950-2004 Relative PPP GDPs of selected countries. GDP expressed as a percentage of total GDPs of these countries.



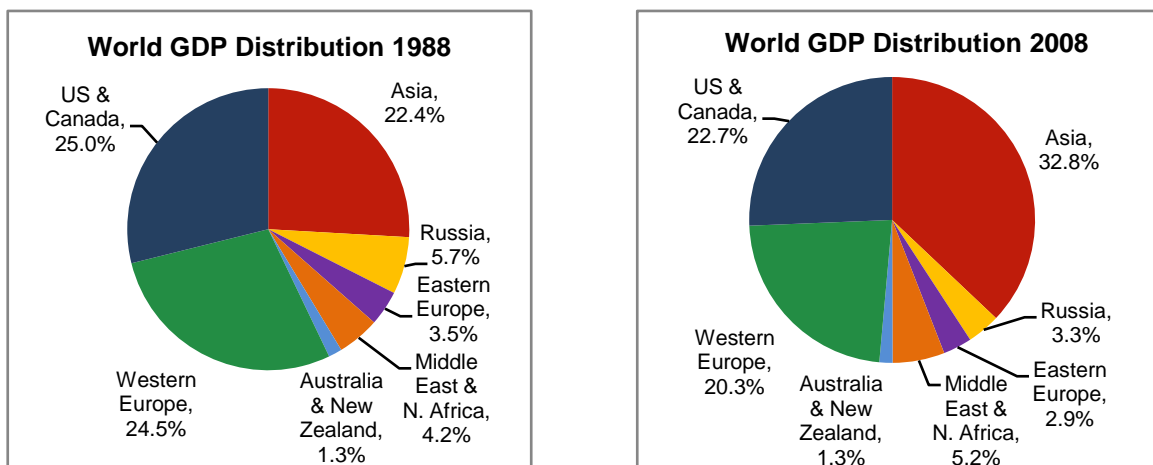
Source: Penn World Table (Heston, Summers et al. 2006)<sup>9</sup>. 'Asian Tigers' comprise Hong Kong, Singapore, Taiwan and South Korea. Lack of Penn data for Russia, Germany, the Middle East and Eastern Europe meant these countries could not be included here.

Asia has led the way and the continent now accounts for a third of the world's economic output. Falling transport costs, improved communications and reduced political barriers have opened up Asia in recent decades and Western factories, with relatively expensive input costs, have generally struggled to compete.

To a lesser extent, the Middle East has also gained a larger share of the world's economic power, principally propelled by demand for its huge oil and gas reserves. Annual export growth in the twenty years to 2007 averaged 11%<sup>10</sup> and together with North Africa the region now produces 5% of world output.

The collapse of the USSR has meant that Russia and Eastern Europe's share of the world's economic power has actually declined in the last twenty years. Russia's PPP GDP in 1998 was just two thirds of that of 1989 but Russia and Eastern Europe have both seen significant increases in power in the last decade. In recent years, Russia's economy has reached new heights as a result of increased commodity prices, a more stable political environment and Western investment<sup>11</sup>. Furthermore, Eastern Europe has benefitted from improved links with Western Europe, particularly EU expansion, which has facilitated the move of manufacturing companies from West to East<sup>12</sup>.

Figure 2: Distribution of world GDP 1988 and 2008.



Source: EIU. GDP expressed in PPP terms.

Of all the Eastern countries, China is worthy of particular mention. Over the last decade it has achieved average annual economic growth of 12.4% and, although its economy is still only about half the size of the US's by PPP GDP, in a wide range of areas it is now ahead of the US. For example, in 2007 China overtook the US to become the world's second largest exporter (behind Germany) following a decade of annual export growth averaging 21%<sup>13</sup>.

In commodities, China has gone from generally being a relatively minor player twenty years ago to being a world leader today. In 2007, China produced around half the world's iron, half the world's cement, 40% of the world's coal, 40% of the world's tin, a third of the world's steel and a third of the world's aluminium<sup>14</sup>. It also became the world's largest producer of gold, produced a third of the world's meat and produced huge quantities of many other commodities<sup>15</sup>.

China's success is repeated across much of the East. India recently overtook Germany to become the world's fourth largest economy by PPP GDP (see Figure 3) and the economies of Malaysia, Vietnam, Laos, Hong Kong<sup>16</sup> and Indonesia have all doubled in size in the last decade. Of the larger Eastern economies, only Japan is notable as having a declining share of world economic power; largely a consequence of its more mature economy and limited natural resources.

*Figure 3: The world's eight largest countries by PPP GDP. Poland, Australia and Iran, as the largest economies in regions not represented in the top eight, are also shown.*

West/East	Country	Size Rank		2008 PPP GDP (\$ millions)	Average Annual Growth Rate 1988-2008	Percentage of world's GDP in 2008	Change in share since 1988
		1988	2008				
West	United States	1	1	\$14,508,820	5.4%	20.8%	-2.0%
East	China	8	2	\$8,197,207	12.3%	11.8%	+8.2%
East	Japan	2	3	\$4,445,441	4.2%	6.4%	-2.4%
East	India	9	4	\$3,405,400	9.0%	4.9%	+2.2%
West	Germany	4	5	\$2,908,662	4.8%	4.2%	-1.0%
East	Russia*	3	6	\$2,316,413	2.9%	3.3%	-2.4%
West	UK	7	7	\$2,230,147	5.0%	3.2%	-0.6%
West	France	6	8	\$2,176,402	4.7%	3.1%	-0.8%
...	...	...	...	...	...	...	...
East	Iran	17	14	\$847,675	7.9%	1.2%	+0.4%
West	Australia	14	16	\$805,473	5.9%	1.2%	0.0%
East	Poland*	15	17	\$677,279	5.6%	1.0%	-0.1%

Source: EIU<sup>17</sup>. \*For Russia and Poland figures are based on 1989, the earliest data available, and the following 19 years.

## Balance of Payments

One of the most important pieces of evidence of the movement in world economic and financial power is seen in balance of payments current accounts<sup>18</sup>.

Eastern exports have generally risen much faster than Eastern imports resulting in the East producing large current account surpluses. At the same time, most Western countries have consumed more than they have produced resulting in current account deficits (see Figure 4).

This has been happening on a huge scale. China's surplus went from \$0.3 billion in 1987 to \$372 billion in 2007 while the US's deficit went from \$161 billion to \$731 billion in the same period<sup>19</sup>.

There are many exceptions. In the West, Germany, Scandinavia and Switzerland have built up healthy surpluses offsetting the deficits built up by most other Western European countries and resulting in Western Europe as a whole producing a small surplus. In the East, Eastern Europe is a major exception and, like the West, its power has fallen as current account deficits have widened<sup>20</sup>. These deficits are now causing major problems, something discussed later.

Overall, a clear movement in power from the West towards Asia, the Middle East, and Russia can be seen. Asia and the Middle East now have a combined surplus of \$850 billion (4.9% of GDP). The West in comparison has an overall deficit of \$680 billion (2.3% of GDP). This huge imbalance is not sustainable in the long-term and represents a large debt the West owes to the East<sup>21</sup>.

Figure 4: Regional current account surpluses/ deficits

Region	1987	2007	1987	2007
	Deficit/ Surplus as % of GDP		Deficit/ Surplus	
<b>Middle East</b>	1.3% deficit	11.2% surplus	\$9 billion deficit	\$146 billion surplus
<b>Asia</b>	2.3% surplus	4.4% surplus	\$88 billion surplus	\$701 billion surplus
<b>Russia</b>	Not known (0.8% surplus in 1994)	3.6% surplus	Not known (\$8 billion surplus in 1994)	\$76 billion surplus
<b>Western Europe</b>	0.6% surplus	0.8% surplus	\$31 billion surplus	\$106 billion surplus
<b>Eastern Europe</b>	Not known (0.3% deficit in 1994)	3.3% deficit	Not known (\$3 billion deficit in 1994)	\$80 billion deficit
<b>US &amp; Canada</b>	3.4% deficit	4.8% deficit	\$174 billion deficit	\$719 billion deficit
<b>Aus. and New Zealand</b>	3.9% deficit	7.7% deficit	\$11 billion deficit	\$67 billion deficit

Source: IMF Balance of Payments Statistics, EIU PPP GDP statistics. Deficit/ Surplus expressed in current prices.

## National Wealth

The movement of power is also clearly evident by examining national wealth. Large current account surpluses have allowed Eastern central banks to accumulate huge international reserves<sup>22</sup> (see Figure 5). Again, China is particularly worthy of comment. Its reserves are now 21 times those of the US<sup>23</sup> and it now holds \$652.9 billion of US Treasury securities, up from \$59.5 billion in 2000<sup>24</sup>. Even Thailand and Malaysia now have more reserves than the US. The West, by contrast has generally seen little change in reserve values<sup>25</sup>.

Figure 5: The world's ten largest holders of international reserves. The US, Poland, the UK and the United Arab Emirates (UAE), typical for their regions, are also shown for comparison.

Country	International Reserves (Millions of SDRs <sup>26</sup> )	% Change since 1988	Multiple of US Reserves
China (excluding Hong Kong)	1,083,780	+7,257%	21.2
Japan	661,358	+828%	13.0
Russia	297,886	Not known (+6,369% since 1993)	5.8
Taiwan	187,368	251%	3.7
India	161,534	+3,993%	3.2
South Korea	142,577	+1,414%	2.8
Singapore	108,966	+801%	2.1
Hong Kong	104,014	Not known (+502% since 1990)	2.0
Thailand	70,051	+1,496%	1.4
Malaysia	65,481	+1,244%	1.3
...	...	...	...
United States	51,047	+38%	1.0
Poland	45,868	+3,220%	0.9
UK	30,292	-8%	0.6
United Arab Emirates	28,665	+782%	0.6
Australia	19,310	+86%	0.4

Source: IMF Financial Statistics<sup>27</sup>.

These reserves give the East significant power. They are effectively 'savings' that can be used to support economies if problems occur<sup>28</sup> and, by buying US debt, China uses its reserves to maintain its artificially low currency value and so boost exports.

Large Eastern reserves have also led to the growth of Sovereign Wealth Funds (SWFs); another sign of the power shift. The vast majority of SWFs belong to Eastern countries<sup>29</sup> and, according to IFSL<sup>30</sup>, assets under management of SWFs doubled between 2001 and 2007 to stand at \$3.3 trillion at the end of 2007. Recently, as some of the few organisations with plenty of equity, SWFs have also shown the movement of financial power by supporting troubled Western institutions, something discussed further later.

As a whole, the West's personal savings as a proportion of GDP have been reducing in recent years and the East's typically higher proportional savings give it more power in the current Credit Crunch<sup>31</sup>. Although likely to change in the future, there is currently little evidence of a difference between Eastern and Western public debt<sup>32</sup>. However, personal and corporate debt has generally been increasing at a much faster rate in the West in the last decade<sup>33</sup>. This is now having major implications as asset prices fall and companies 'deleverage'.

Lastly, further evidence of the movement of wealth comes from examining oil and natural gas reserves. Although the vast majority of reserves have always been in the East, in recent decades the West's reserves have generally decreased while the East's proven reserves have often increased due to increased exploration<sup>34</sup>. For example, UK and Norwegian oil production fell by a third in the decade to 2007 and the UK went from being a net oil exporter to a net importer<sup>35</sup>. In contrast, Russia's proven oil reserves increased by 42% between 1998 and 2007<sup>36</sup> and Russia has gained power as the West's share of world gas reserves has declined<sup>37</sup>. Again, Eastern Europe is a significant exception as the recent Gazprom-Naftogaz dispute has highlighted<sup>38</sup>.

## Economic and Financial Influence

The word 'power' is used not just to describe output, performance and wealth but also influence and here again considerable movement can be seen.

The influence of Eastern companies has grown steadily in recent decades to the point that Eastern companies now comprise over a quarter of the Fortune Global 500 list of the world's largest companies<sup>39</sup>. Japanese and South Korean companies have generally gained market share and the rise of companies such as Tata, Gazprom and Rosneft has been meteoric. Eastern research and development ('R&D') has also increased rapidly. In terms of PPP R&D expenditure, Japan is second in the world, South Korea recently overtook the UK and China's impressive R&D growth means it now undertakes more R&D than the UK and France combined<sup>40</sup>.

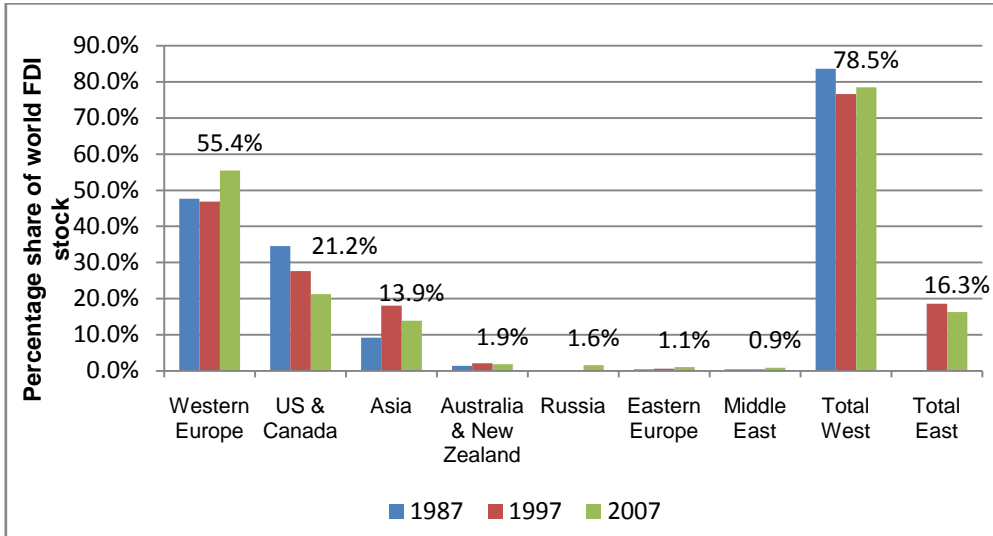
Generally Eastern influence has not grown as fast as GDP and the movement in power must not be overestimated. The US still remains by far the world leader in R&D<sup>41</sup> and the West is still home to the vast majority of the world's top companies<sup>42</sup> and top brands (91 of the top 100 according to Interbrand<sup>43</sup>).

Most significantly, there is no evidence that the East has increased its share of foreign investment. The West still owns almost 80% of world Foreign Direct Investment (FDI)<sup>44</sup> and Asia's share of world FDI actually declined in the last decade (see Figure 6)<sup>45</sup>. The Middle East, Russia and Eastern Europe all have very little of the world's power in this area.

The below Western growth of the Tokyo Stock Exchange<sup>46</sup> in the last twenty years has meant that the East has not increased its market share of world stock markets<sup>47</sup>. However, both the Hong Kong and Shanghai Stock Exchanges (the latter founded in 1990) are now larger than Frankfurt's Deutsche Börse<sup>48</sup> and, according to City of London research, many Eastern cities have rapidly increased their financial services competitiveness in recent years (see Figure 7)<sup>49</sup>.

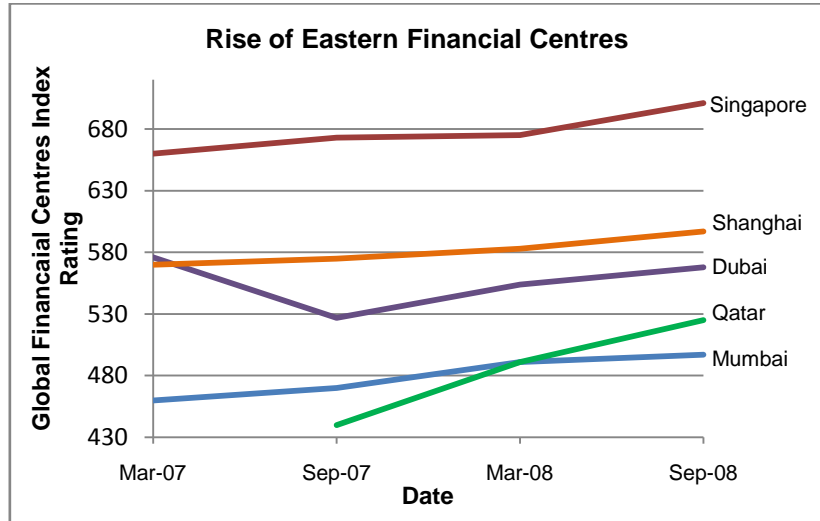
Overall, the East's increased influence can be seen in all corners of the globe. Russia's influence on the EU has already been discussed, as has SWF influence in capital markets. China has also gained huge influence in Africa. In the twenty years to 2007, China overtook seven other countries<sup>50</sup> to be behind only the US as Africa's largest trading partner<sup>51</sup>. Eastern FDI remains well below Western FDI in most African countries but through strategic investments and trade, the East has become economically very influential.

Figure 6: Location of world FDI stock holders



Source: UNCTAD. 1987 data for Russia (and the USSR) is unavailable and so there is no entry for Russia or 'Total East' in this year.

Figure 7: Rise of Eastern Financial Services Competitiveness



Source: City of London Global Financial Centres Indices (GFCI). These centres were identified in GFCI 4 as those most likely to become more significant in the future.

## Impact of the Credit Crunch

The movement of power from West to East has been complicated by the Credit Crunch.

The first year of the Crunch (to around August 2008) saw a quickening of the movement of power from West to East. Western financial institutions, the pride of the US and UK, saw major problems. This resulted in falling Western economic output, rising market share for Japanese banks<sup>52</sup> and often prominent 'bail outs' from Eastern SWFs. Commodity prices soared sending power rapidly from West to East and particularly benefitting the Middle East and Russia.

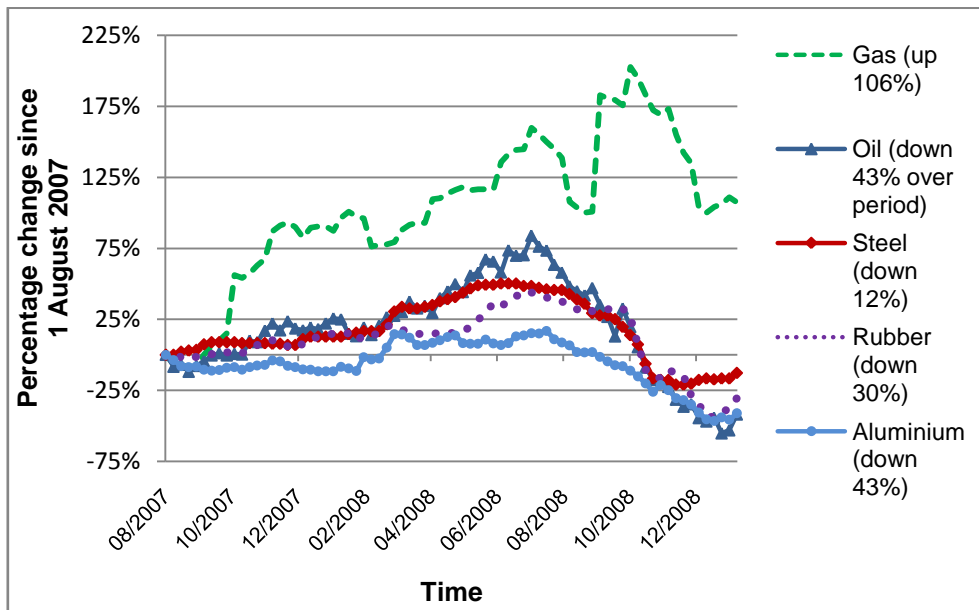
Since then, the West's economies have continued to rapidly deteriorate. However, the East has also been hurt very badly and talk of the East 'decoupling' from the West has vanished. Falling commodity prices (see Figure 8) have had major negative consequences in the East while often benefitting Western consumers<sup>53</sup>. Meanwhile Eastern SWFs have incurred such enormous losses that many no longer plan to invest in the West in the near future<sup>54</sup>.

Eastern Europe has been decimated. Ukraine, Hungary, Belarus and Latvia have all required major loans<sup>55</sup> and Romania's government debt has been downgraded to junk. Before the Credit Crunch, finance in Eastern Europe was commonly provided by Western banks in Euros or Swiss francs<sup>56</sup>. These banks have now largely retreated and national currency values have fallen significantly (see Figure 9) making finance difficult to find and foreign currency loans expensive. Eastern European reserves have fallen and Russia's reserves are reportedly down 25% since August<sup>57</sup>.

Japan has been hurt by much lower demand for its (often highly income-elastic) exports and the rising value of its currency<sup>58</sup>. As well as reducing export demand, this has meant foreign profits have fallen when converted into Yen. Taiwan's exports have fallen 42% in the last year<sup>59</sup> and even China's exports have shrunk<sup>60</sup>. Thousands of factories in China have closed and unemployment has risen<sup>61</sup>. Furthermore, the Financial Times<sup>62</sup> notes that "China has little choice but to keep buying more US securities because a collapse in bond prices and the dollar would also have a huge impact on China's dollar holdings and its own economy".

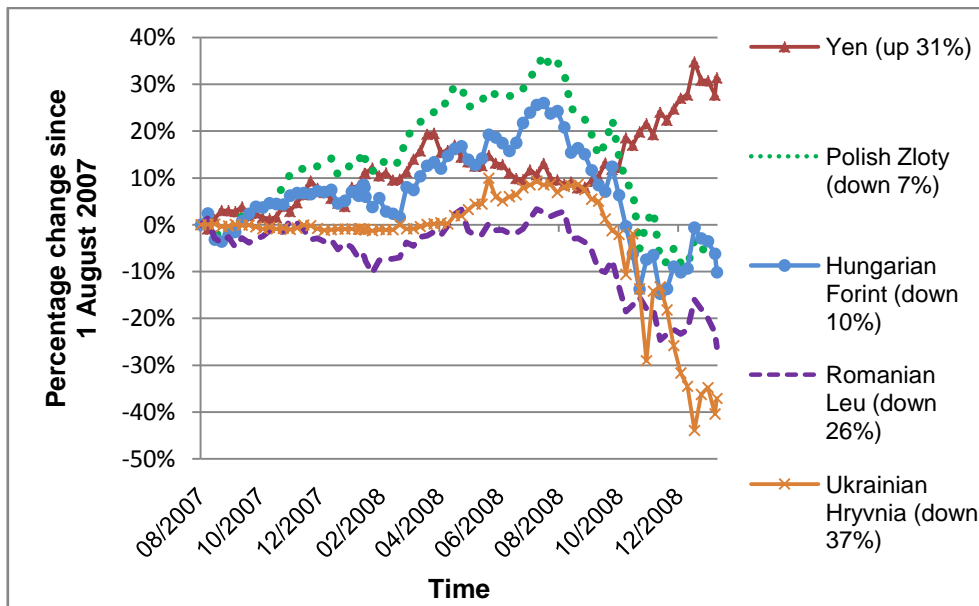
Overall, Western economic power has fallen very quickly. However, reduced Western consumption has meant that the movement of power towards Asia has arguably slowed significantly since autumn 2008. Furthermore, much lower commodity prices and other problems have probably caused the movement of power towards the Middle East, Russia and Eastern Europe to reverse.

Figure 8: Movement of key commodity prices since August 2007



Source: Thomson DataStream<sup>63</sup>. Since 1 August 2008, Oil is down 53%, Gas is up 8%, Steel is down 22%, Aluminium is down 36% and Rubber is down 39%.

Figure 9: Movement of selected currency values since August 2007: exchange rate to US dollar



Source: Thomson DataStream. Since 1 August 2008, the Yen is up 17%, the Zloty is down 29%, the Leu is down 26% and the Hryvnia is down 43%. The Euro is down just 1% since August 2007 (14% since August 2008) and therefore the Latvian Lats, Lithuanian Litas and Estonian Kroon (all pegged to the Euro under ERMII) have not declined in line with other Eastern European currencies.

## Conclusion

For over 150 years, the West has been the most prosperous and economically successful group of economies in the world. Today, the United States still has the world's largest economy and the West continues to dominate in business, innovation, finance and foreign investment.

However, the evidence examined here shows that the West's share of world power has been declining at a rapid pace in the last twenty years. Western economies have not shrunk but the East has generally grown much faster resulting in more of the world's power being located in the East.

The differences regarding balance of payments are enormous and represent perhaps the biggest single piece of evidence of the movement of power. This is reinforced by international reserves data showing spectacular Eastern growth. The East's influential power has not grown as fast as Eastern production and here the West remains very dominant. Nevertheless, clear evidence of a movement of power is still evident.

It has been shown that the rise has not been uniform. The movement of power towards Russia has been slower and more volatile than the movement of power towards Asia. Japan has generally not increased its power in the last twenty years, while the growth of China is simply incredible. Eastern Europe is repeatedly an exception and therefore it must be concluded that, on balance, no significant power has moved from the West to Eastern Europe as a whole.

The growth of the tertiary sector in the West has ensured power has not moved faster but the Credit Crunch has hurt this sector more than any other, significantly weakening the West's power. However, reduced Western consumption and lower commodity prices have also hurt the East in recent months and the overall power shift has therefore probably slowed. Figure 10 summarises the evidence.

Overall, it cannot be doubted that the movement of economic and financial power from West to East has been substantial. In the future this is likely to continue further, albeit at a slower and potentially more balanced pace. The world's economic and financial power is effectively limitless and hopefully through further trade and integration, the movement of economic and financial power will continue to the benefit of West and East.

Figure 10: Summary of Evidence

Indicator	Summary of Evidence	Conclusion
Economic Output	The US still has by far the world's largest economy but faster growth by Eastern economies has meant the East's share of world GDP now roughly matches the West's. Asia has particularly performed well, especially but not only China, which is now ahead of the US in many areas. Russia and Eastern Europe are exceptions. They have lost share over a twenty year period (although gained slightly over a ten year period). Japan has also lost share of the world's economic power.	<b>Major movement</b> of world economic power towards the East with principal exceptions of Eastern Europe, Russia and Japan.
Balance of Payments	Balance of payments current account data represents one of the most significant pieces of evidence supporting a major movement of power eastwards. The West as a whole has built up huge a deficit of \$680 billion (2.3% of GDP) and the East (excluding Eastern Europe and Russia) has built up a huge surplus of \$850 billion (4.9% of GDP). Eastern Europe is a major exception. There are also many exceptions in Western Europe.	<b>Major movement</b> of power towards the East with exception of Eastern Europe.
National Wealth	Enormous increases in Eastern international reserves and impressive rise of SWFs. In the West, personal and corporate debt has rapidly accumulated in the last decade reducing Western power. Shift in world share of oil and gas reserves has also moved power eastwards with main beneficiary being Russia.	<b>Major movement</b> of power towards East.
Economic and Financial Influence	Eastern influence has not increased as fast as Eastern economic output but nevertheless a movement can be seen. Eastern companies comprise 25% of the Fortune Global 500 and Eastern R&D growth has been impressive. The major limit of the East is that outside Japan and Korea it has relatively few genuine multinationals. This can be seen not just with the Fortune list but by looking at Interbrand data and a very low Eastern FDI share. As well as having no entries on the Fortune and Interbrand lists, the Middle East, Russia and Eastern Europe have very low FDI stocks. Asia's FDI stock has declined in recent decades. China has become very influential in Africa. Russian and Middle Eastern influence is highly correlated with commodity prices. National Wealth indicators such as the rise of SWFs, China's use of reserves to peg its currency, and Russia's rising oil and gas power also indicate increased influence.	<b>Significant movement</b> of power towards Asia, the Middle East (because of SWFs) and Russia (because of oil and gas) but increases typically below GDP growth. No shift towards Eastern Europe.
The Credit Crunch	Power shifted rapidly from West to East in the first year as Western financial institutions in particular encountered problems and commodity prices spiked. The second year has seen rapidly falling Western output but also major problems across the East principally a cause of falling demand and much lower commodity prices. Eastern Europe has been particularly badly hurt.	<b>First year saw rapid acceleration</b> of movement. <b>Since autumn shift towards Asia has slowed</b> and power movement has <b>reversed concerning the Middle East, Russia and Eastern Europe.</b>

## Notes

<sup>1</sup> Note that the definitions of East and West exclude many countries, principally those of South America, Central America and Africa. While these countries are not examined here, it should be remembered that many have grown rapidly in recent years and are likely to be economically more powerful in future.

<sup>2</sup> EIU PPP data has been used for all GDP references in this essay except in Figure 3.

<sup>3</sup> Source: EIU (confirmed by IMF, World Bank, CIA).

<sup>4</sup> Source: City of London (September 2008).

<sup>5</sup> Source: World Federation of Exchanges (WFE).

<sup>6</sup> The phrase 'Asian Tigers' refers to Hong Kong, Singapore, Taiwan and South Korea.

<sup>7</sup> Purchasing Power Parity (PPP) GDP has been used throughout the essay to ensure accurate portrayal of GDP. In order to compare GDPs of countries with different currencies, the 'traditional' approach is to convert the local currency GDP to a common currency (typically dollars) at the current market exchange rate. However, exchange rates fluctuate considerably (particularly evident in the last six months) and often do not reflect the purchasing power of a currency at home at a given point in time. Therefore GDP is converted into a common currency at a PPP exchange rate rather than a market exchange rate. This exchange rate is calculated to allow a given sum of money in one country to buy the same amount of goods in another country after exchanging it into the currency of the other country.

<sup>8</sup> For Russia and Eastern Europe, 1988 figures are unavailable and so figures are based on 1989 shares of world GDP.

<sup>9</sup> Heston, A., Summers, R., Aten, B., (September 2006). PPP GDP data not directly provided but calculated by multiplying PPP GDP per capita data by provided population data. Some minor extrapolation based has been undertaken where information was missing. Extrapolation based on average growth in following ten years (preceding ten years for India's 2004 GDP). Extrapolation used for China (4.5% rate/ years 1950-1951), India at (8.0%/2004), Hong Kong at (13.0%/1950-1960), Singapore (8.0%/1950-1960), Taiwan (9.5%/1951) and South Korea (5.0%/1950-1952).

<sup>10</sup> Source: IMF Direction of Trade Statistics.

<sup>11</sup> In the last year much lower commodity prices and reduced Western investment (in part due to the Credit Crunch and in part due to high profile political problems such as at TNK-BP) have worsened this situation but Russia remains much stronger economically than a decade ago.

<sup>12</sup> The announced move of Dell from Ireland to Poland on 8 January 2009 provides a recent example of this. Dell currently employs 1,900 people in Ireland and according to The Times (9 January 2009) each job underpins a further four to five jobs. The Times also reports that Dell contributed about 5% to Ireland's GDP in recent years.

<sup>13</sup> Source: IMF Direction of Trade Statistics.

<sup>14</sup> Source for all metal and mineral statistics except coal and gold: United States Geological Survey (USGS) (steel statistics confirmed in OECD *Factbook 2008*). 'Iron' refers to pig iron. Source for gold statistics: Gold Fields Mineral Service (GFMS), *Gold Survey 2008*, April 2008 and China Mining Association. China produced around 276 tonnes of gold (9.7 million ounces) in 2007. Note that production is not necessarily sustainable: according to USGS, China only has around 1,200 tons of gold reserves (South Africa in comparison has around 6,000 tons while Australia has 5,000 tons). Source for coal statistics: BP. Source for agricultural statistics: UN Food and Agriculture Organisation (FAO).

<sup>15</sup> According to USGS, in 2007, China also produced around 61% of the world's lime, 73% of the world's mercury, 86% of the world's tungsten, 40% of the world's magnesium and a fifth of the world's zinc, salt, lead and silver. The FAO also estimates that it produced around a fifth of the world's cereals.

<sup>16</sup> Although Hong Kong is part of China, as a Special Administrative Region (SAR) it is largely self governing and therefore discussed listed separately throughout this essay. It is also considered as 'Eastern' throughout despite being part of the UK until 1997.

<sup>17</sup> The US's GDP is slightly distorted compared to other countries in this table as EIU calculate GDP for the US and Canada to the end of each year whereas for all other countries it is calculated to the end of each June.

<sup>18</sup> The balance of payments current account is calculated as the country's exports less imports plus net income from abroad plus net unilateral transfers of money from abroad. A surplus means exports and received money is greater than imports and outgoing money.

<sup>19</sup> Source: IMF Balance of Payments Statistics, EIU (for PPP GDP data).

<sup>20</sup> To give some examples, Estonia's is 13.6% of GDP, Latvia's is 16.3% of GDP and Lithuania's is 8.8% of GDP. These large current account deficits have resulted in falling currency values recently, something discussed further later. Outside Eastern Europe, the main exceptions are Pakistan and (perhaps surprisingly) Vietnam, both of which have built up significant current account deficits.

<sup>21</sup> Currency values for countries with surpluses should rise over the long-term making exports less competitive and imports cheaper so allowing the balance to be restored. The Chinese Yuan and other Eastern currencies not being allowed to appreciate to market levels has to some extent prevented this occurring at present. In Eastern Europe, the pegging to the Euro of several currencies (notably those in ERMII) has prevented depreciation of their currencies so exaggerating their current account deficits.

<sup>22</sup> International reserves are central bank holdings typically consisting of foreign exchange, gold, SDRs and IMF reserve positions.

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<sup>23</sup> Excluding reserves held in Hong Kong. Source: IMF Financial Statistics.

<sup>24</sup> Source: US Treasury TICS. October 2008 (latest available) and October 2000 figures used.

<sup>25</sup> This is despite inflation and a small increase in the gold price over the period (since 1987 the LME bullion price has climbed 77%).

<sup>26</sup> The Special Drawing Right (SDR) was created by the IMF in 1969 to support the Bretton Woods fixed rate exchange rate system but today its main role is as the unit of account of the IMF. It is calculated daily based on the value of the Pound, Euro, Yen and US Dollar weighted according to the importance of each currency in international trade and finance. At the time of writing (early January 2009), 1 SDR was roughly equivalent to £1.

<sup>27</sup> Latest monthly data available used (typically that of October or November 2008) and compared with the same month in 1988. It should be cautioned that government debt growth for Japan in particular has outstripped reserves growth (source: IMF) so examining Japan's reserves growth in isolation can be slightly misleading.

<sup>28</sup> Some Middle Eastern countries, for example, aim to use reserves (and SWFs) to smooth the peaks and troughs in oil prices.

<sup>29</sup> According to IFSL and the SWF Institute, in 2007 around 45% of SWFs by value were Middle Eastern and 28% by value were Asian. 76% of SWF assets were owned by the UAE, Singapore, China, Saudi Arabia, Kuwait and Russia. The only major Western SWF is the Government Pension Fund of Norway, the second largest SWF controlling around 12% of SWF assets.

<sup>30</sup> International Financial Services London (April 2008).

<sup>31</sup> Source: IMF Main Economic Indicators. Gross savings are referred to. As an example, Japan's savings as a proportion of GDP (28.5%) are around double that of the US's and UK's proportions (14.2% and 14.6% respectively). Other Western nations fare better but a clear divide is still evident.

<sup>32</sup> Source: IMF Main Economic Indicators (this shows net time series debt for the G7), OECD (this shows gross debt time series data for OECD members) and CIA World Factbook (shows gross debt for all countries as at 2007 but not time series data). None of these datasets (usually only running to 2007) show evidence of an East-West split regarding public debt. IMF data shows Japan's net debt increased substantially in the decade to 2007 (35% to 91% of GDP) while net debt in all other (Western) countries except France and Germany actually fell in the same period (although Italy's net debt remains extremely high at 101%). According to the CIA World Factbook, Japan has the third highest gross debt in the world (170% of GDP), Egypt has the sixth highest, Singapore has the eighth highest and Israel has the 15<sup>th</sup> highest. In the West, Italy, Belgium, Norway and Germany are all in the top 20 for public gross debt. Generally, comparing public debt data between countries can be misleading. For example, in the UK it is sometimes argued that public debt is underrepresented by not including the huge PFI liabilities and public sector pensions (while this is partly true, these are liabilities (rather than debt in the traditional sense) and are gross rather than net). In the future, the divide between Eastern and Western public debt will probably be clearer as Western governments borrow heavily to spend in the Credit Crunch.

<sup>33</sup> Source: The Economist (6 December 2008).

<sup>34</sup> Source: BP, *Statistical Review of World Energy*.

<sup>35</sup> Source: COMTRADE. 'Oil' refers to petroleum oils, oils obtained from bituminous minerals and crude. Between 1997 and 2007 UK oil exports dropped from 69,850,931,200kg to 47,058,701,754kg resulting in the UK moving from being a net exporter to the value of \$4,361,550,848 of oil to a net importer to the value of \$1,985,941,607. Norway's production in the same period has fallen from 137,548,136,448kg to 99,245,180,068kg but because of its relatively low consumption it remains a major net exporter.

<sup>36</sup> Source: BP, *Statistical Review of World Energy*. 1998 represents the earliest available data concerning Russian reserves.

<sup>37</sup> The West's share of world gas reserves fell from 13.6% in 1987 to 8.5% in 2007 according to BP. USGS data shows the picture of declining Western proven reserves and often increasing Eastern reserves does not apply to other metal and mineral commodity reserves.

<sup>38</sup> The January 2009 dispute between Russia (Gazprom) and Ukraine (Naftogaz) shows the extent of Russia's increasing power concerning natural gas. Eastern Europe has been most severely affected, although to a lesser extent the West has also been impacted. According to Reuters (7 January 2009), 42% of Germany's gas is from Russia, 60% of Austria's gas is from Russia, 24% of France's gas is from Russia and 28% of Italy's gas is from Russia.

<sup>39</sup> Companies are ranked by revenue in US dollars. Since 2005 (the first publication of the list) no East-West change can be seen. However, within each region a change can be seen with the number of Japanese companies declining, China and South Korea's share increasing, the US's share decreasing and Western Europe's share increasing. China's proportion of companies has roughly doubled to 6% and South Korean companies now comprise 3% of the list. Japan has just 13% of the total (down from 16% in 2005) while US companies represent just 31% of the list (down 5%). 37% of the top 500 companies are European (up from 35% in 2005).

<sup>40</sup> Source: OECD Main Science and Technology Indicators. Countries such as China are often wrongly perceived as undertaking relatively little R&D. This is partly due to outdated stereotypes and partly because R&D is often not adjusted for Purchasing Power Parity. An example of this can be found in the UK Department for Innovation, Universities and Skills (DIUS)'s 2007 R&D Scoreboard, which by expressing R&D in sterling at current prices, overestimates the UK's position.

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<sup>41</sup> Source: OECD Main Science and Technology Indicators.

<sup>42</sup> 72% of companies in the 2008 Fortune Global 500 list have their headquarters in the West.

<sup>43</sup> Interbrand Best Global Brands List 2008. The nine Eastern companies were Toyota, Honda, Samsung, Sony, Canon, Nintendo, Hyundai, Panasonic and Lexus all of which are Japanese apart from Hyundai which is South Korean. This means despite China's impressive growth, neither it nor the Middle East, Russia or Eastern Europe have leading, world recognisable, brands. However, the above-named Eastern brands have risen in recent years and in the Interbrand 2001 list there were only six Eastern brands.

<sup>44</sup> Source: UNCTAD. For clarity, FDI outflow stock is being referred to, that is the value of Eastern investments outside home countries rather than foreign FDI stock in the East (inflow stock).

<sup>45</sup> Source: UNCTAD. The decline in Asia is primarily a consequence of the decline of Japan's FDI share from 7.3% of world FDI in 1997 to 3.5% in 2007. Other Asian countries' FDI has grown significantly in nominal terms but their share of the world total has generally not increased.

<sup>46</sup> Source: World Federation of Exchanges (WFE). Of the WFE members, Japan's market share declined from 33% in 1990 to around 9% today.

<sup>47</sup> Source: WFE, Federation of European Stock Exchanges (FESE), Russian Trading System (RTS) and various other exchanges.

<sup>48</sup> Source: WFE.

<sup>49</sup> Source: City of London Global Financial Centres Indices and, regarding the Gulf, City of London (May 2008).

<sup>50</sup> Source: IMF Direction of Trade Statistics. The seven other countries were France, Germany, Italy, Japan, the UK, the Netherlands and Spain.

<sup>51</sup> Source: IMF Direction of Trade Statistics. The US's position as number one is due to its huge imports from Africa, five times the size of its exports to Africa. China's imports and exports to Africa roughly balance.

<sup>52</sup> Source: Financial Times (3 December 2008).

<sup>53</sup> The oil price is the most prominent example. The price of a barrel of Brent Crude has fallen from \$145 per barrel in July 2008 to around \$45 per barrel today principally benefitting the West while significantly reducing the power of Russia and the Middle East.

<sup>54</sup> Source: Reuters (3 December 2008) and The Times (27 November 2008).

<sup>55</sup> At the time of writing, Ukraine has agreed a \$16.4 billion loan from the IMF. Hungary will receive loans of \$15.7 billion from the IMF, \$8.4 billion from the EU and \$1.3 billion from the World Bank. Belarus will receive a \$2.5 billion loan from the IMF and \$2 billion from Russia and Latvia will receive a \$2.4 billion loan from the IMF and \$550 million from the World Bank.

<sup>56</sup> See MoneyWeek (14 November 2008) for further details of Eastern European problems. MoneyWeek reports that 90% of new mortgages taken out in Eastern Europe between 2006 and publication of the article were in Swiss Francs or Euros. Austrian banks were notably some of the biggest lenders to Eastern Europe.

<sup>57</sup> Source: The Economist (10 January 2008).

<sup>58</sup> This is largely attributable to the Yen Carry Trade, which was very popular prior to the Credit Crunch. Western investors borrowed in the low yielding Yen and lent at higher rates in their home countries. As Western economies deleverage they have had to buy Yen to pay back these loans increasing the value of the Yen significantly. The Economist (1 February 2007) quotes Pi Economics in estimating that as much as \$1 trillion may have been staked on the Yen carry trade.

<sup>59</sup> Sources: The Economist (10 January 2008) and Financial Times (11 December 2008).

<sup>60</sup> Chinese year on year exports fell 2.2% in November 2008 (the latest data available) according to Chinese customs figures quoted in the Financial Times (11 December 2008).

<sup>61</sup> Source: The Economist (10 January 2008). See also The Economist (22 December 2008).

<sup>62</sup> Source: Financial Times (21 November 2008).

<sup>63</sup> 'Oil' refers to the per barrel price of Brent Crude. 'Gas' refers to the London Natural Gas Index. 'Steel' refers to the price of Guangzhou 10mm medium plate. 'Aluminium' refers to the London Metals Exchange ('LME') price for 99.7% Aluminium. 'Rubber' refers to Malaysian Rubber Exchange ('MRE') Standard Malaysian Rubber ('SMR') GP FOB.

The front page picture is of Kwai Chung Port, Hong Kong. Source: hkskyline, www.skyscrapercity.com.

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