

The shift in the world's centre of gravity: the rise of Asia and implications for the UK

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Mr President, thank you for your kind introduction.

My Lords, Ladies and Gentlemen, good evening, and my thanks to Universities UK for the invitation to give your annual lecture.

As we enter 2009, we are literally living through economic history in the making. The fact that the Bank of England last week cut interest rates to the lowest level since the Bank was founded in 1694 is testimony to that. Many of your future students, in the years and decades ahead, will be analysing the credit crunch of 2008 and the global downswing of 2009. Let's hope that they are not analysing anything worse.

My theme for this evening – the shift in the world's centre of gravity – was perhaps the most widely discussed topic, certainly in business circles, until a year or so ago. It has, quite understandably, been a casualty of the credit crunch. There has been little airspace for any other subject in the last year.

But they are in fact related themes. Let me begin with the credit crunch, to explain why. This is clearly the worst financial crisis since 1929, and also the most complex. It has spread from the financial services industry into the real economy. We are now facing the worst annual synchronised global economic downturn since the great depression.

All G7 economies are now in recession and our forecast is for global GDP to contract in 2009 by 0.1 per cent. This figure of course masks widely varying performances in individual countries – the developed world will contract by 1.1 per cent, with the UK faring particularly badly.

Economic growth in emerging economies is also slowing sharply – but it will still grow – at round 3 per cent in 2009, less than half the growth rate in 2007.

The speed and unpredictability of the way the crisis has unfolded makes forecasting a more speculative pursuit than usual, but we all know that 2009 will be a difficult and painful year at an international, national, corporate and individual level. Falling consumption, failing businesses and rising unemployment will create real pain for people in this country and elsewhere.

The origins of this crisis are very complex and you will, I am sure, be pleased to hear that I don't intend to

belabour them all now. Suffice to say that there are many lessons to be learned by us all.

Banks have not covered themselves in glory; they became over-gearred and too reliant on wholesale funding which has subsequently evaporated. Regulators did not pay enough attention to liquidity management in banks. Borrowers succumbed too often to the temptations of jam today. We were all happy enough with the benefits of the boom period.

All these factors certainly contributed to the current crisis, but it is also important to see it in its broader context – that is, as one of the consequences of the rise of Asia, and the growing interdependency between national economies that we have seen in the last few decades.

In other words, the crisis is very much linked to my theme this evening – the shift in the world's centre of economic gravity that has been a feature particularly of the last two decades.

At the end of the second world war, the world economy was highly fragmented after the huge disruptions of depression, tariff barriers and war. Today, all that has changed. Interdependence between national economies has increased hugely. We now operate in a genuinely global economy as a result of overall geographic stability, the lowering of trade barriers, and the dramatic falls in the cost of transport and communications that have been features of the post-war world.

We have seen the rise of dynamic Asian economies starting with Japan in the 1950s; spreading in the 1960s and 70s to the Asian Tigers – Hong Kong, Singapore, Taiwan and South Korea.

Their economic success – based initially on low-value added manufacturing, and later on a wider economic base – has brought tremendous prosperity. Their people's incomes are now among the world's highest. But none of these economies attracted the world's attention in the way that the rise of China and India in the last 20 years has done. And no wonder – a third of humanity lives in these two nations, and the awakening of the Chinese dragon in particular is, to borrow the words of Napoleon two centuries ago, 'shaking the world'.

**lessons
to learn**

These, and other emerging markets, have become the workshops of the world, manufacturing everything from cars, computers and cameras to toys, televisions, and trousers. In vast quantities and at low prices. As well as becoming software powerhouses.

No wonder that these products found such ready markets among consumers in the developed world. Consumption became the main driver of economic growth, especially in the US. The consumer was truly king and queen.

Western demand for products, and increasing wealth in emerging economies, drove commodities prices up to new highs, also benefiting resource-rich nations. They, along with the workshop countries, generated surpluses that they lent to the developed world at very cheap rates, which enabled western consumers to continue to spend.

Together these factors created what you might call a macro-economic triangle between workshop nations, resource producers and consuming nations.

A triangle that worked, but that was intrinsically unstable and created the financial imbalances that lie at the heart of this crisis. The most obvious of which was the US's large current account deficit, which was offset by massive surpluses in, primarily, the emerging world. In other words, the world's poorest nations became creditors to the world's richest – contrary to normal expectations which would have surplus capital flowing from rich nations to poorer ones. And into this already potent cocktail, was added a significant loosening of US, and therefore of global, monetary conditions after the dot.com boost and 9/11. All of this generated a massive increase in financial market leverage, which created the illusion of a world awash with liquidity.

It is these imbalances that are now unwinding, sharply and painfully. As I said earlier, 2008 will be a year for the history books.

Some people have questioned whether, in light of the current crisis, the fundamental trend in the world economy – the rebalancing towards Asia – will be derailed. The answer – in my opinion – is fundamentally 'no'. There is no reason to believe the crisis will put globalisation into reverse. I wonder even if there is anything that could put it into reverse. There is no reason to expect that emerging markets, which are home to billions of people, will not continue to seek growth. There is no reason to expect that the emerging world will not continue to reclaim a greater share of the world's wealth.

If the 19th century belonged to Britain, and the 20th to America, it seems likely that the 21st century will belong to Asia. Many Asian economies will make their presence felt in the 21st century – India, as well as

China, and many of the smaller economies are contributing to the global economic shift. Although it is always worth remembering that not all 'small' Asian nations are so very small - Vietnam, for example, has a population as large as Germany's. So, many Asian economies are contributing to this economic shift, but tonight I want to concentrate on China, the second-biggest and much the fastest growing Asian economy. Her sheer size will make the rise of China the most important fact of the first half of the 21st century.

I think it is important to remember that although the rise of China is an event of tremendous significance, we are witnessing not the rise of a new power, but the re-emergence of one of the world's oldest and greatest civilisations. Charles Murray, the author of *Human Accomplishment*, describes the *Song Dynasty*, which ran from the 10th to the 13th century, as the apogee of Chinese culture. At a time when Europe's cities were no more than market towns, Hangzhou, the capital of Song China, was a city of a million people with an advanced municipal administration, with widespread public facilities, including bath houses, tea houses, restaurants, theatres and hotels. It had a national economy, paper money. Art and literature were highly valued, and huge private and public collections were established by connoisseurs.

England in the middle ages, by contrast – at around the time our two oldest universities were founded – had only ten towns of over 2,000 people and a total population estimated at between 1 and 3 million. London, England's largest town with 40,000 souls, was in comparison not much more than a market town. While the wealthy few may have lived in great houses with fine furniture and silver, London's infrastructure was poor, hygiene non-existent: it was noisy, cramped, dirty and disease-ridden.

Famously, the balance began to change from the 15th century on. China lost her edge as a result of centuries of autarky – a disengagement from the rest of the world whose consequences became fully apparent in the 19th century. Meanwhile, rapid economic growth in Europe and then the US meant that western economies pulled further and further ahead.

But in 1820, China still accounted for about a third of the world economy, compared with the US at under 2 per cent. By 1950, however, China's share was under 5 per cent, while the US accounted for over a quarter of the world economy, with just 6 per cent of its population. So the world's economic centre of gravity has been based in western economies, latterly the US of course, in the last 200 years.

Since China started re-engaging with the rest of the world 30 years ago, the consequences have been stunning – for China herself, and for the world at large.

**21st century
belongs to Asia**

Ushered in by Deng Xiaoping's proposals to 'reform and open up' China in December 1978, China has moved from a state-directed to a market oriented economy. "It does not matter whether the cat is black or white," Deng famously said, "as long as it catches mice."

Deng's reforms started on a very small scale, with an experiment allowing small farmers to farm a small portion of their land for themselves. This was not the most desirable land – it was the ditches and shaded areas, some of it virtually unfarmable. But almost as much was produced on that 15 per cent as on the more fertile government-owned land. Deng told former US president Carter that farmers would stay up all night with a sick pig if it was their own, but if it belonged to the government, the pig would die.

In less than 30 years since these small experiments in free-enterprise, China has become the world's manufacturer; home to the world's largest shopping mall; and the most talked about economy on earth.

And Deng's vision, which unleashed the Chinese people's natural entrepreneurialism, has lifted, quite literally, hundreds of millions of people from poverty. This has been a tremendous boon for humanity as a whole.

The rapidity of the change has been astonishing. I visit China half a dozen times every year now; yet when I started my career, China was largely a closed country. When I lived in Hong Kong in the early 80s, I remember going to the Lok Ma Chau lookout in Hong Kong's New Territories, right on the border, from where you had a spectacular view into mainland China. In those days, Shenzhen was a small fishing village surrounded by paddy fields and duck ponds. Today, it's a modern metropolis and manufacturing powerhouse with a population of eight and a half million people.

If the speed of change has been breathtaking, the size of the task has been so too, by which I mean the sheer logistical task of managing the world's largest population. As Premier Wen has remarked, any small problem multiplied by 1.3 billion becomes a very big problem indeed. To put it in context, it is the equivalent of multiplying Britain's infrastructure, trade or indeed, educational needs by 20 times.

So we should not be naïve about the difficulties that such rapid change has entailed. Economic development is rarely linear and there have been plenty of bumps along the way. There have been and will be in the case of China. But this is true of the rapid industrialisation of any nation, including the US and the UK.

As late as the turn of the 20th century, two out of every ten children born in industrial cities in the UK died – a rate that is higher than almost anywhere in the world today. And the inter-war urbanisation of the

Soviet Union was characterised forced people movements and unspeakable brutality.

The point of these comparisons being simply to emphasise the relatively problem-free transition China has managed so far.

Of course, China is only part way along her transformational journey. Economic development has so far touched the lives of 3 or 400 million people – about three-quarters of China's population is still rural and poor. "China today is utterly different from the China of two decades ago," the former *Economist* editor, Bill Emmott, wrote in his recent book, *Rivals*. And "China in ten, 15 or 20 years' time is going to be utterly different again."

For all that she has experienced 30 years of rapid and accelerating growth, income per head remains just under US\$2,500. There are many challenges ahead, as China's leaders know very well. Those challenges range from pushing economic growth out into rural regions from where they are currently concentrated on China's coast and in the Yangtze and Pearl River Delta areas; to infrastructure development; to dealing with environmental damage and pollution; to the need to establish a pension and welfare system, to the need to find jobs for the 10 million or so people who join the job market in the cities each year.

But by any measure, China's success on the journey so far has been astounding. And China announced her arrival centre of the world's stage at the Beijing Olympics last summer in spectacular style.

Of course, China is far from immune to the current economic crisis – exports have fallen sharply as western markets have moved into recession, as have expectations of GDP growth. Nevertheless, growth rates are likely to remain high when compared with the west, for the next generation at least. So despite the current economic crisis, the fundamental economic shift is unlikely to be de-railed. And what's true of China is true more generally of Asia.

Indeed, forecasts of world GDP growth for the next 20 years suggest that two thirds of the world's growth will be driven by emerging economies. This major economic rebalancing will inevitably lead to a major rebalancing in all aspects of our lives. I have already spoken in some detail about the economic rebalancing that is needed in the world. Put simply, US and UK consumers need to learn to save more and borrow less, Chinese consumers need to learn to spend more and save less. Solving the current crisis is not something that any individual country will be able to do on its own.

It is striking to see how the G20, a grouping which includes the world's key emerging markets as well as

breathtaking speed of change

the wealthiest nations, is starting to eclipse the G7 as the major forum for the discussion of economic issues. Quite rightly, in my view, as the solutions to the current crisis – that lie in an economic rebalancing – need to be synchronised.

More broadly, as the world and economies become more interconnected and as the influence of countries such as China, India and other emerging economies grows, the need for the world to engage all the major players in discussions affecting us all – such as international trade, resource scarcity, climate change – will become increasingly urgent.

Socially and culturally we will need to adjust and learn too. To adjust to a world in which there is no single dominant cultural model. That is more multiplex. We need to broaden our understanding of China and other rising nations.

I wonder how many people here – and this is hardly a representative sample! – I wonder how many people here could name the first Chinese Emperor? He was active around a century after Alexander the Great and is at least as important a figure in world history. Or why it was that the great voyages of Zheng He in the early 1420s were brought to an end by the Ming dynasty, in the same century when Europeans began to venture into the Indian and Atlantic oceans, with such momentous consequences. Many people have a sense of China was a great civilisation with a sophisticated society, but the understanding runs only skin deep.

Where does all this leave Britain? What are the implications of China's rise and the global economic shift for this island? Partly, I've covered some of this already. There are clearly economic adjustments ahead for the UK. We all understand that an economy like the UK is not the place for low- value-added manufacturing.

We are an affluent country, so unit labour costs are high; if we are to continue to prosper, we will need to continue to move up the value chain – a process of disruptive transformation that has been underway since the Industrial Revolution. It's the same process of development and reinvention that all successful economies have to deal with, and places a major responsibility on the education system to ensure that successive generations are equipped to meet the new challenges and opportunities that constantly arise. So a key component in the UK's success in the 21st century will be its education policy and its implications for the skills base of the population.

But it's not just about skills, but about a more fundamental need for us all to gain a broader and deeper understanding of the history, culture and language of countries whose influence is growing so hugely. It brings to mind the Kipling quote: "What

should they know of England, who only England knows?" We believe this so strongly that HSBC is funding teaching of Putonghua in UK schools.

And clearly this has implications for the education sector at all levels. Now, I have no expertise whatsoever in the subject of education and would not presume to address this august gathering on its specialist subject. But I would like to offer you a few thoughts as a 'consumer' of the product – graduates.

HSBC is a multinational company. We happen to be in banking, but the sector is not of especial relevance except for the fact that we have relatively few special technical requirements from our recruits, unlike say, a Rolls Royce or a Shell who need engineers or geologists. We have archaeologists, anthropologists and medics all working at HSBC, but not in specialist roles... That said, almost half of graduates on our UK schemes have a business-related degree.

Typically, we might recruit up to 1,500 graduates onto one of our 70 graduate programmes around the world – in the UK last year we recruited some 400 graduates. For those jobs, globally, we receive almost 100,000 applications. As 90 per cent of graduates get a 2.2 or 2.1 and will therefore meet our academic criteria, it takes something else to stand out from the crowd.

In other words, what they can offer over and above their academic qualifications. Relevant work experience – internships for example, rather than working in the union bar. Some form of experience in the wider world – travel, but not just on holiday! – travel that demonstrates energy, openness to the world and initiative. Activities that demonstrate leadership. It's hard to define and measure these qualities, but you know it when you see it.

Recent recruits include a graduate who taught English and Spanish in Guatemala; one who ran a restaurant; another who worked at the Beijing Paralympics; a Punjabi singer who's been on TV. Another graduate from Cameroon had published a book, and set up a small business shipping second hand clothes from New York to Africa, before joining HSBC. These and many activities provide hard evidence of energy, motivation, leadership. Cultural sensitivity is key too – and hard to measure – but we test for it carefully in our screening process.

One of our schemes is particularly interesting, our international management programme. This is for people who want a genuinely international career and is a fasttrack programme to senior management positions. These young recruits can expect to move jobs – and probably countries – every two years or so in their first few years, so it is self-evident that openness to the world in general and language skills are critical requirements.

adjusting to the new global marketplace

In our latest recruitment drive, we had applications from students of 88 nationalities. Every candidate must speak English and at least one other language fluently but we find that speaking only two languages is unusual; most candidates speak three or more.

What is my point? That in today's world, we are all competing on a much wider playing field, not within national borders. This is true for UK students; true for UK universities; it is also true for much of UK plc. We all need to ask if we are adequately prepared for this new environment.

To sum up then. We are in the midst of a global economic downturn, the worst economic crisis since 1929. It is the main focus of the world's attention, quite rightly, and has replaced the rise of Asia as the main subject of discussion in the world at large. However, the fundamental trend – the shift in the world's economic centre of gravity – remains intact. In a generation China is likely to be the largest economy in the world, with India also a major force. As countries, individuals, companies, educators, we will all need to adjust to this new global marketplace.