ECONOMIC VIEWPOINT

Global Economy in the Decades to Come

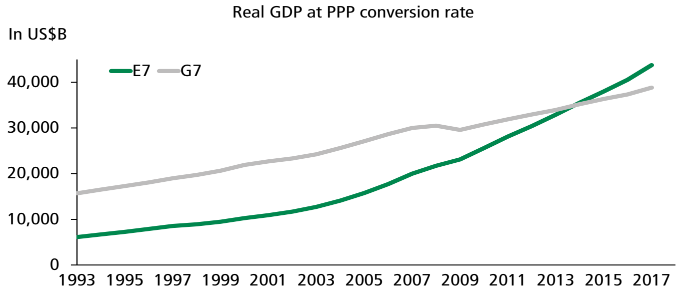
India and China Could Be the Two Biggest Economic Powers by the Next 20 Years

The world's economic order is in transition, with emerging nations gaining an expanding place in the global economy. In terms of purchasing power parity (PPP), China's GDP has even outstripped the United States since 2014, while India's economy continues to post strong growth, which could drive it into second place globally by 2050, according to some estimates. Living standards are also expected to rise more quickly in emerging nations than in advanced nations, although it should remain much lower. Demographic trends, climate changes, technological innovation, and political and social progress are issues that will have a major impact on all countries' economic growth.

Economically, the world looks very different today than it did 25 years ago. Back then, emerging economies represented just 42% of global GDP at PPP conversion rate[1]. That number reached 59% in 2017, while the seven leading emerging economies (E7) alone—China, India, Russia, Brazil, Indonesia, Mexico and Turkey—represented 35% of global GDP. In comparison, the G7 economies—United States, United Kingdom, Japan, Italy, Germany, France and Canada—saw their share of global GDP drop from 46% in 1993 to 31% in 2017. This illustrates the theory of economic convergence, i.e., that developing economies tend to grow faster than more advanced economies (graph 1). In just a few short years, the emerging nations have become quite important in the global economic landscape, even outstripping certain advanced economies.

Despite the progress, however, emerging nations still fall short on living standards. GDP per capita at PPP conversion rate of E7 nations was just US$18,000 in 2017, close to a third of the average for G7 nations. This is still an improvement: in 2000, the per capita GDP of E7 nations was a quarter of the G7. The E7 nations' higher population growth has played a role in the slower convergence of per capita GDP. Note that the planet's two most populous countries are part of the E7: China and India.

GRAPH 1
Emerging nations' GDP has exceeded that of advanced nations in 2014



PPP: Purchasing power parity; E7: China, India, Brazil, Russia, Indonesia, Mexico, Turkey;
G7: United States, Canada, Germany, France, Italy, United Kingdom, Japan
Sources: International Monetary Fund and Desjardins, Economic Studies

Extrapolating these major trends helps paint a picture of the global economy of the future. Studies by PricewaterhouseCoopers (PwC) and the Organisation for Economic Co-operation and Development (OECD) also offer some predictions for the global economic order until 2050 and 2060. Clearly, these forecasts reflect general trends, and assume a stable political environment. Armed conflicts, abrupt changes in political regimes, and other major, unexpected events cannot be factored in, and could change the results dramatically. However, it is still interesting to analyze the implications that today's trends have for the future.

[1] Purchasing power parity (PPP) expresses in U.S. dollar different currencies' purchasing power. This theoretical rate then takes into account the exchange rate of a currency against the U.S. dollar for a certain reference period, as well as the country's price level spread with the United States.

François Dupuis, Vice-President and Chief Economist • Mathieu D'Anjou, Deputy Chief Economist • Carine Bergevin-Chammah, Economist
Desjardins, Economic Studies: 514-281-2336 or 1 866-866-7000, ext. 5552336 • desjardins.economics@desjardins.com • desjardins.com/economics

A New Economic Order

A few major findings emerge from the PwC and OECD studies. Firstly, the leading economies of today could continue to give way to the emerging nations, as their GDP would exceed that of the larger economies. According to PwC, in 2050, the seven countries with the highest GDP at PPP will be made up of emerging nations and the United States, pushing Germany, Japan and the United Kingdom to lower ranks (table 1). The OECD anticipates a similar shift, with the euro zone and the U.S. share of global GDP, declining in favour of China and India. However, the emerging nations' economic growth should slow in the decades to come, as their economies reach a more advanced level of development, particularly in China and India. Global GDP could therefore also slowly decelerate. The OECD thinks that global economic growth could go from an average of 3.4% in 2010–2030 to 2.4% in 2031–2050. China's economic growth has already started to slow, partly as a result of the government's efforts to modernize its economy and shift it to lower but more stable growth over the long term. China has posted average real growth of 9.6% since 1980, the strongest growth rate of the major economies. However, growth has been under 7% since 2015, which currently puts India in the lead for GDP growth among the major economies. It could exceed the U.S. GDP at PPP in 2037, according to the OECD. This would make China and India the two largest economies in the world. Seven of the ten countries with the highest forecasted growth rates through to 2050 are in Asia (graph 2), which would make the continent a front-runner for economic growth in the years to come.

Africa is also expected to post high growth rates over the next decades, although that would primarily be a result of its population growth rate. According to the United Nations (UN), Africa will have the strongest demographic growth until 2100. Latin America, whose share of global GDP has been dwindling slowly since 2000, should continue to post relatively low growth rates with respect to its level of economic development, according to the OECD. As the world's most urbanized region, Latin America experienced a very fast urbanization rate, which introduced problems that were a drag on growth. Inadequate infrastructure, the development of shantytowns, heightened violent crime rates and high pollution will continue to weaken these countries' economic growth, unless they devote a larger share of their revenue to financing infrastructure. As for the advanced economies, in 2050, they should post real GDP growth that is slightly lower than it is now. PwC, the OECD, and the Department of Finance Canada believe that Canada's average long-term growth, i.e., until 2050 and 2055, would be around 1.8%, compared with an average of 2.4% between 1980 and 2017.

The Large Living Standards Gap between Countries Should Persist

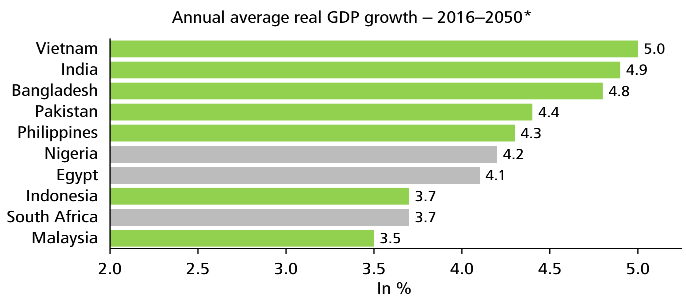
With respect to the evolution of countries' wealth as measured in GDP per capita at PPP, the OECD, the International Monetary Fund (IMF) and PwC expect the emerging countries to improve in the coming decades, but not catch up completely (graph 3). In China, the world's largest economy, GDP per capita only represented 28% of the United States in 2017; according to the OECD, this ratio would be 50% in 2050. Thus, despite strong GDP growth in emerging nations, their population would remain in relative poverty in comparison with advanced nations, and it could take many more years before they reach that standard of living. The U.S. population would remain the major economies

TABLE 1
Today's emerging nations could outstrip the major global powers by 2050

RANKING ACCORDING TO GDP	GDP (US$B) IN 2017		PROJECTED GDP (US$B) IN 2030 ACCORDING TO PWC*		PROJECTED GDP (US$B) IN 2050 ACCORDING TO PWC*	
1	China:	23,159	China:	38,008	China:	58,499
2	United States:	19,391	United States:	23,475	India:	44,128
3	India:	9,459	India:	19,511	United States:	34,102
4	Japan:	5,429	Japan:	5,606	Indonesia:	10,502
5	Germany:	4,171	Indonesia:	5,424	Brazil:	7,540
6	Russia:	4,007	Russia:	4,736	Russia:	7,131
7	Indonesia:	3,243	Germany:	4,707	Mexico:	6,863

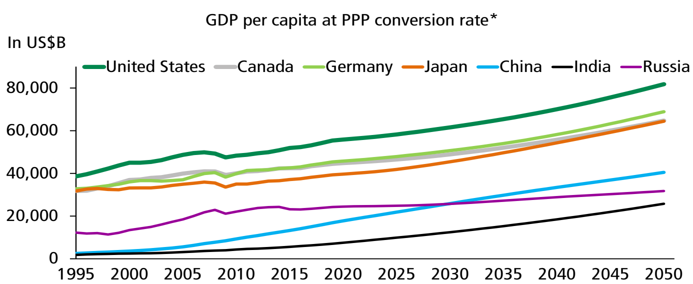
Note: The posted GDP is adjusted based on the purchasing power parity (PPP) conversion rate;
* The projections are taken from the PricewaterhouseCoopers (PwC) estimates published in their study "The World in 2050."
Sources: International Monetary Fund, PwC and Desjardins, Economic Studies

GRAPH 2
Most of the countries with higher growth rates are in Asia



* The projections are taken from the PricewaterhouseCoopers (PwC) estimates published in their study "The World in 2050."
Sources: PwC and Desjardins, Economic Studies

GRAPH 3
Emerging nations' per capita revenue could remain weaker



PPP: Purchasing power parity; * The projections are taken from the Organisation for Economic Co-operation and Development (OECD) estimates published in "Economic Outlook No. 103 – July 2018 – Long-term baseline projections."
Sources: OECD and Desjardins, Economic Studies

with the highest income per capita in the years to come, but the gap with most emerging nations could narrow. Moreover, the OECD thinks that the poorer economies' GDP per capita could rise faster than that of richer economies. To ensure living standards convergence, emerging nations will have to transform their economies, now based on commodities and low-cost labour, into service and consumption-based economies, which will require substantial structural reforms.

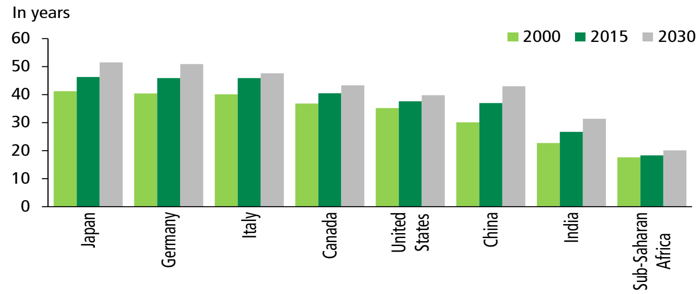
Countries' Demographic Trends Will Diverge

Demographic change is one of the major trends that could impact how the economy evolves in the coming years. The population of some countries are currently ageing. Japan, Germany and Italy are the oldest economies (graph 4). In 2017, the median age in Japan was 47.3, whereas it was 41.2 in 2000; the population even began to shrink in 2010. Population ageing is not only an issue in advanced nations. China is also starting to feel the effects of its one-child policy instituted in 1979, as its elderly dependency ratio, i.e., the ratio of the population over age 65 to the working age population (15 to 64 years old), is rising. The one-child policy was amended in 2016 to allow two children, but this does not seem to be enough to promote a higher fertility rate. According to the UN, in China, the proportion of working age population will decline substantially by 2030 (graph 5), taking the elderly dependency ratio from 14.8% in 2017 to 25.3% in 2030. Europe is currently the oldest continent, with an elderly dependency ratio of 27.7% in 2017. Canada is facing a similar situation: its ratio was 25.4% in 2017 and could rise to 38.1% by 2030. Population ageing in the advanced countries also results in a drop in their share of the global population, which could fall from 16% in 2017 to 13% in 2050.

At the same time, some countries in Asia and Africa are seeing their working age population increase. In India, the proportion of people aged 15 to 64 should go from 66% to 68% by 2030, according to the UN. While India's elderly dependency ratio should rise, it could remain low until 2050. In Africa, the youngest continent, several countries have a median age that is under 20. According to the UN, Africa's share of the global population should go from 17% in 2017 to 26% in 2050, with growth mainly coming from sub-Saharan Africa. However, these countries are still very poor. In India and sub-Saharan Africa, the GDPs per capita at PPP conversion rate were US$7,200 and US$4,000 respectively in 2017. These countries will need to be able to provide an education, healthcare and job opportunities to the 1.5 billion new people who will be added to these markets by 2050, to ensure that the population's standard of living rises in tandem with GDP growth. Low education levels, the concentration of employment in agriculture and manufacturing, and inadequate infrastructure in these countries will have to be addressed to ensure economic development.

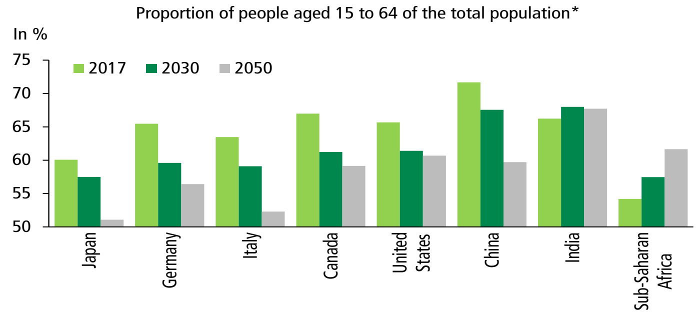
The division between countries with younger population and older countries could prompt migration from the former to

GRAPH 4
In many nations, the median age could go over 40 by 2030*



* United Nations (UN) forecasts.
Sources: UN and Desjardins, Economic Studies

GRAPH 5
Lower-income nations should get an increase in their working age population



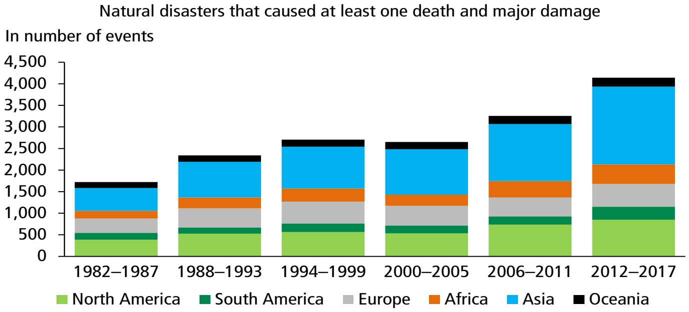
* United Nations (UN) forecasts.
Sources: UN and Desjardins, Economic Studies

the latter. Countries with higher demographic growth rates could struggle to integrate new workers into the market. On the other hand, countries with significant population ageing should see a decrease in the labour force participation rate, as the working population is too small to fill the vacant jobs. To prevent a decline in economic potential, these countries will probably have to take in more immigrants from countries with a surplus of young workers. Population ageing will also impact public finances, as the costs of healthcare and pensions will rise while the labour force is declining. Technological progress, e.g., artificial intelligence, could increase productivity, particularly in advanced countries where GDP growth per hour worked has been weak for the last decade or so. This could ease the burden of an ageing population and minimize the impact on growth potential. It is, however, difficult to quantify the future impact of these technologies. Unless the fertility rate bounces back, or technological innovation has a substantial impact, governments will probably have to institute policies to foster the integration of immigrants into the job market, while also encouraging workers to keep working longer.

Climate Change Could Have Disproportionate Impacts

Another major factor that could affect how the global economy develops is the issue of climate change. As extreme climates become more frequent, the cost of climate change will grow. However, these costs tend to be distributed unequally. According to a simulation conducted by Berkeley and published in *Nature*, the costs of global warming as measured in GDP per capita at PPP would be greater in southern nations. Northern nations, including Canada and most of Europe, could even benefit from climate change, as milder winters could improve their productivity. This also means that the poorest and most populous countries in Africa and Asia would be the hardest hit. The consequences are already being felt: the incidence of extreme climate events is rising, and such events tend to occur disproportionately in Asia (graph 6). Moreover, the National Intelligence Council believes that population growth will be concentrated in low elevation coastal zones, which are more susceptible to flooding and hurricanes. According to their estimates, the population of such areas will increase by 50% by 2035 from 2000. The poorest countries also tend to be more vulnerable to climate change as they are less equipped to prepare and respond to it than more developed nations. Investing in preventing climate change and the infrastructure needed to adapt to it is often not a priority in poorer countries. Aside from the direct costs, the long-term impact of pollution and recurring disasters has to be considered, because it affects productivity, as well as people's health and overall well-being. It could slow the convergence of living standards of emerging nations, as the consequences of global warming could be more felt by them.

GRAPH 6
Natural disasters are occurring more frequently and are concentrated in Asia

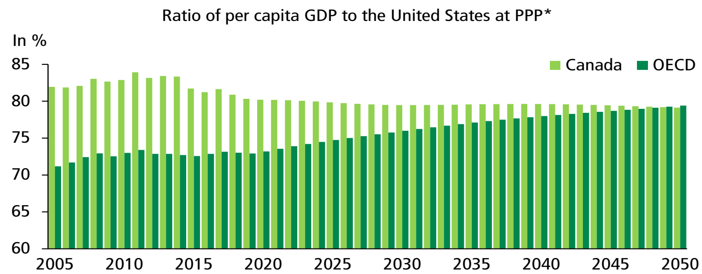


Sources: Munich Re and Desjardins, Economic Studies

Focus on Canada: The Ageing Population Will Be a Drag On the Economy

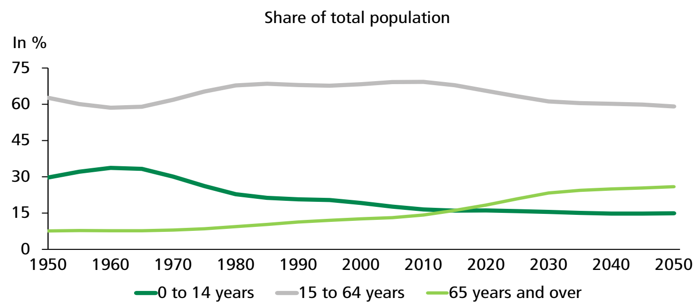
Taking a closer look at Canada's faith from these projections, the main trend that stands out is the lagging economic growth compared to OECD countries. The share of Canada's GDP among the OECD could go from 3.16% in 2017 to 3.11% by 2050 at PPP, according to OECD data, indicating that the Canadian economy would grow slower than its peers. This would mark a deviation from its past trend as this share generally followed an upward path since 1995. At a more global level, Canada's ranking of GDP at PPP could go down from 17th in 2017 to 22nd by 2050 according to PwC. In terms of GDP per capita at PPP, Canada is not expected to catch up to the U.S. level, contrary to the OECD which should post a certain convergence (graph 7). One of the main reasons for this slower growth is a higher decrease in the working age population share. Canada's fertility rate went from an average of 2.61 children per woman in 1965–1970 to 1.61 in 2010–2015, combined with a longer life expectancy, this means that the share of the elderly population will grow constantly while the share of younger age groups will decline (graph 8). As explained earlier, this puts a strain on the labour market as fewer workers are available to fill the vacant jobs left by those going on retirement. Public finances would also be affected since fewer people can contribute to government's coffers and public expenses rise.

GRAPH 7
Canadians' income is moving away from that of Americans contrary to the OECD's average



OECD: Organisation for Economic Co-operation and Development; PPP: Purchasing power parity;
* The projections are taken from the OECD estimates published in "Economic Outlook No. 103 – July 2018 – Long-term baseline projections."
Sources: OECD and Desjardins, Economic Studies

GRAPH 8
Starting 2040, a fourth of Canada's population could be over 65 years old



* United Nations (UN) forecasts.
Sources: UN and Desjardins, Economic Studies

Some Issues Could Derail These Projections

If the last few decades are an indication of the global economy's future evolution, we should see rapid GDP growth in emerging nations, and a decrease in poverty. However, the poorest countries still have many obstacles to overcome to be able to achieve the same standard of living as more advanced nations. The emerging economies still tend to be focused on agriculture and manufacturing, which require relatively unskilled labour and do not pay well. Many of these economies are dependent on the exploitation of commodities and international trade, which also means that they tend not to be very diversified and tend to be more volatile and vulnerable to external shocks. Many poor nations are also falling behind in the areas of education and infrastructure. Access to education, electricity, healthcare and basic sanitation infrastructure is still lacking. Moreover, democracy is often unstable or non-existent. These factors explain why emerging nations are lagging on per capita income; improving them is critical to ensuring a rise in living standards. According to the OECD, structural reforms to the labour market and economic liberalization could increase GDP by an average of 16% by 2060 compared with a scenario that features modest reforms. For their part, today's developed nations will have to be proactive in tackling the demographic problem and maintaining relatively constant potential growth. The technological innovations that are taking place could offer an opportunity to increase productivity in many nations and mitigate the impact of population ageing.

Carine Bergevin-Chammah, Economist