The danger in Asia's demographics

Last week's move by Standard & Poor's (S&P) to downgrade China, the first time since 1999, didn't have the same shock value as its 2011 call to strip "AAA" status from the US. But it's a timely reminder of the biggest problem facing Beijing and much of Asia.

No, not the soaring debt that S&P's cited, as did Moody's when it downgraded Beijing in May. The real reason S&P's cut China's sovereign rating to "A+" from "AA-" is demographics. Yes, China has immense savings. As it churns out tens of trillions of dollars of fresh credit, though, a dwindling workforce, lost productivity and deflation could strain the central government's ability to balance servicing exploding debt with financing its social development. And China is hardly alone. Hong Kong, Japan, Singapore, South Korea and Taiwan also face demographic headwinds.

It's understandable that those riding demographic tailwinds might feel smug. But officials in India, Indonesia and the Philippines must consider their own population-growth-related vulnerabilities. So must investors.

Warnings of China's demographic reckoning come just as Deloitte LLP delights governments in Jakarta, Manila and New Delhi enjoying young and growing labour pools. India came out on top. In Asia, generally, the ranks of those over 65 will rise from 365 million now to more than half-a-billion in 2027, Deloitte said.

By 2030, Asia will have 60% of the global share. Young India, by sharp contrast, will drive the next Asian tailwind as its potential workforce surges to 1.08 billion people from 885 million over the next 20 years. Equally important, it will hold around there for roughly 50 years. Indonesia and the Philippines also are looking at decades of swelling-workforce magic.

Or not. If Narendra Modi, Joko Widodo and Rodrigo Duterte aren't losing sleep over these trajectories, they're delusional. Demographic dividends only matter if Modi can create future jobs for the roughly 25% of his 1.3 billion people under the age of 15. So far, that hasn't been the case. For all the excitement about Modi's 'Make in India' push, job creation in export-related industries isn't anywhere near what New Delhi advertised. Nor is domestic retail-sector growth picking up the slack with well-paying new positions. It's hard to be too optimistic about the consumption outlook.

That's especially so now that Modi appears to be resting on his laurels. After steps to open the aviation, insurance and defence industries, all indications are that the Bharatiya Janata Party is already focused on the 2019 election. Unfortunately, the real big bang will only come when Modi revolutionizes labour, land and tax policies and goes markedly further to cut red tape and increase government efficiency.

That goes, too, for Indonesia's Widodo, who's known as Jokowi, and Philippine President Duterte. Jokowi is indeed working to improve infrastructure, reduce graft, increase transparency and, via tax tweaks, facilitate the return of billions of dollars of investment into South-East Asia's biggest economy. Yet it's not enough. Neither Indonesia's urbanization boom nor its enviable store of national resources nor its growing middle class will matter if Jokowi doesn't hasten reforms.

Efforts to improve roads, bridges, ports and power grids, rein in the bureaucracy and ensure legal contracts are enforced are lagging today's 5% growth, argues Elizabeth Pisani, author of *Indonesia Etc: Exploring the Improbable Nation*. For all Jokowi's efforts to decentralize democracy and take on what she terms the "judicial mafia", a menace that complicates doing business, Indonesia will have a hard time climbing the global competitiveness rankings, Pisani says.

The Philippines may be an even bigger risk. Duterte's economy is experiencing China-like growth of 6.5%, but his policy priorities are more about guns than butter. His bloody drug war has already filled more body bags (at least 7,000) in 456 days than brutal dictator Ferdinand Marcos did in 20 years. Policing drug pushers and users is important, but it's eclipsed all else—including economic upgrades.

The mandate voters gave Duterte, remember, was to accelerate the reform successes of predecessor Benigno Aquino. From 2010 to 2016, Aquino strengthened the national balance sheet, increased transparency and accountability, went after tax cheats and ignored the powerful Catholic Church to cap a population growing faster than incomes. Voters turned to strongman Duterte to take things to new levels. Sadly, his priority is deputizing bands of gunmen to shoot alleged drug-trade members extrajudicially. Not surprisingly, the peso is Asia's worst performing currency so far this year.

The US Federal Reserve's rate hike campaign won't help efforts in Jakarta, Manila and New Delhi to maintain growth consistent with rising living standards. But it's crucial that Jokowi, Duterte and Modi hit the reform accelerator to create enough decent jobs to employ their swelling populations. That means spreading the benefits of rapid growth, investing more in human capital and attracting ample foreign investment.

If not, China's challenges may pale in comparison to hundreds of millions of young Filipinos, Indians and Indonesians turning on governments running afoul of demographic trajectories.

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