

The Emerging Middle Class in Developing Countries

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Introduction

- Middle class consumers in the US and other G7 powers have been a key source of demand in the global economy for the last 50 years. But with weak expected growth in US and European consumption going forward, where will future global demand growth come from?
- ***The middle classes in emerging economies, especially in Asia***
- We are reaching a tipping point, where over the next several years the global middle class will expand dramatically. This is one of the most important features of today's global economic landscape.

Why is the middle class important for growth?

- Income elasticities of demand greater than one (esp. durables)
 - » Kink in demand curves at PPP\$6000
- Preference for product differentiation leads to value added in branding
- Values (hard work, meritocracy, saving, education)
- Catalytic class (economic policymaking, but not entrepreneurship)
- More sustainable than “export-led” growth; less risk of middle income trap (Gill and Kharas 2007)

Defining the Global Middle Class

- Relative vs. absolute definitions
- Between the poor in Portugal/Italy and the rich in Luxembourg: \$10 to \$100 a day, 2005 PPP\$
- Calculate current population and spending of the middle class for 145 countries – accounting for 98 percent of global population and 99 percent of global GDP – using data on distribution and mean consumption per capita in 2005 PPP\$

The Global Middle Class Today

Size of the Middle Class, 2009
(millions of people and global share)

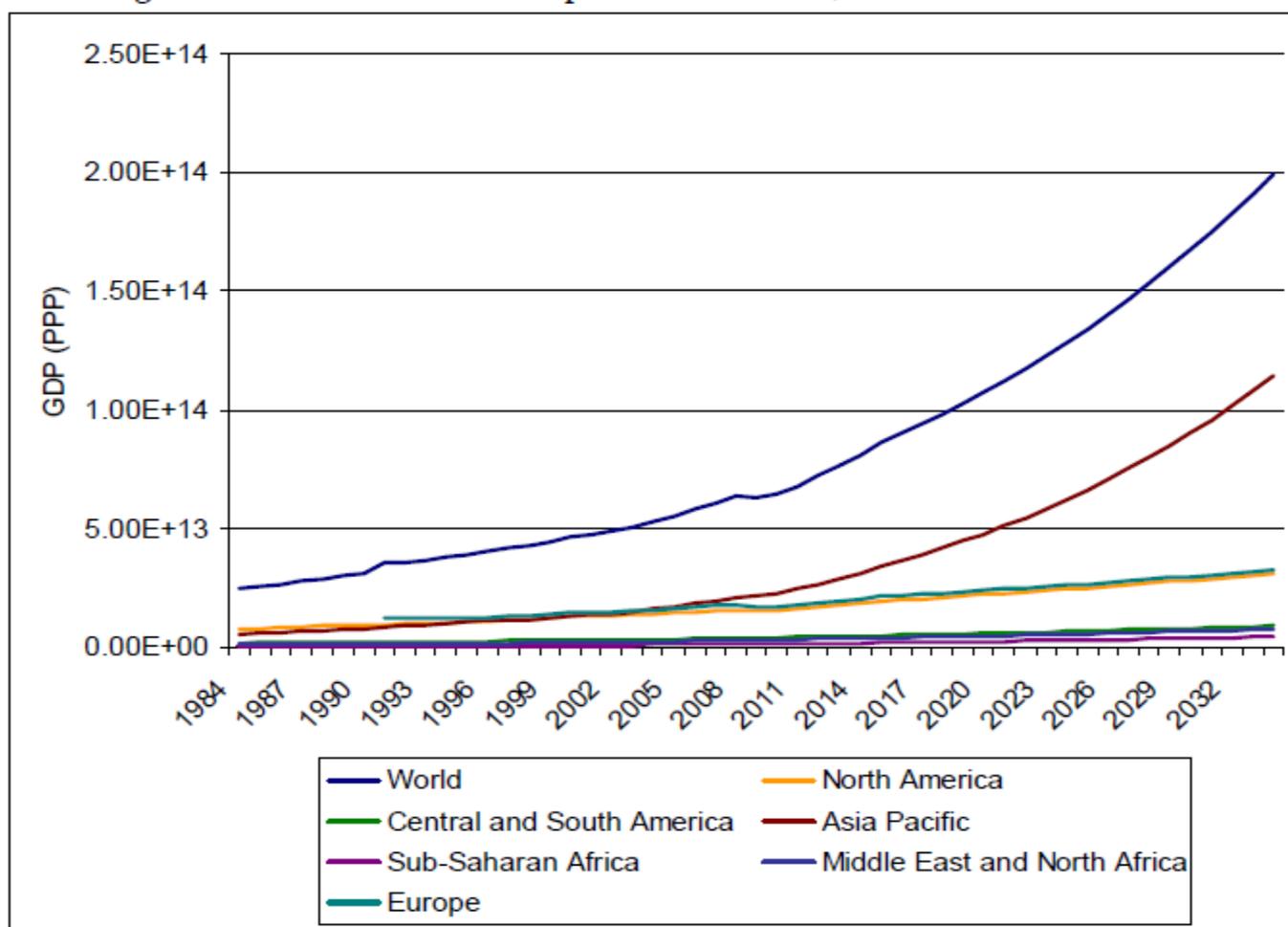
	Number of People (millions and global share)		Consumption (billions PPPUSD and global share)	
North America	338	18%	5602	26%
Europe	664	36%	8138	38%
Central and South America	181	10%	1534	7%
Asia Pacific	525	28%	4952	23%
Sub-Saharan Africa	32	2%	256	1%
Middle East and North Africa	105	6%	796	4%
World	1845	100%	21278	100%

Projecting the Evolution of the Global Middle Class

- Project GDP growth for 145 countries using simple Cobb-Douglas growth model featuring catch-up for a set of rapidly converging economies, including China and India
- Assume no change in middle of income distribution or in household expenditure share of GDP
- Most changes in Gini are dominated by changes in shares of top and bottom deciles, not the middle class (Palma 2007)

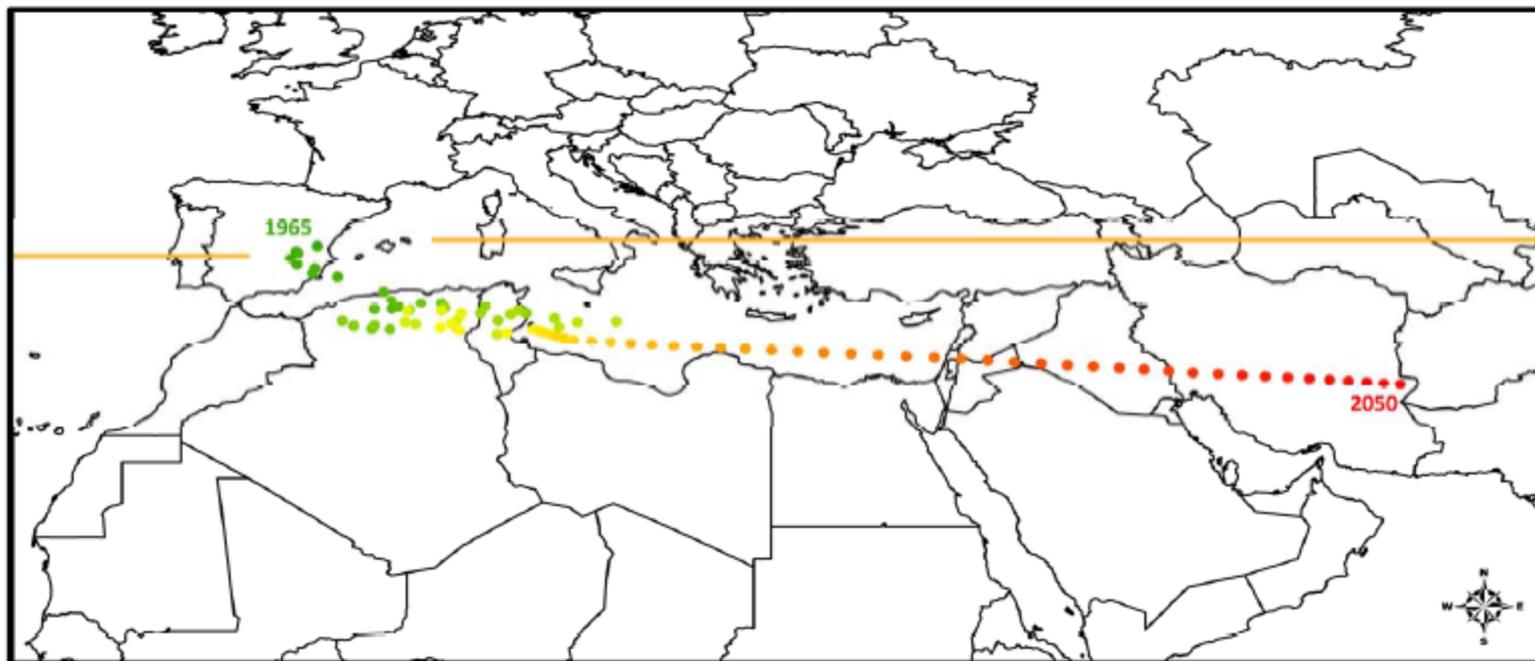
Growth in Global GDP Accelerates, Driven by Asia

Figure 3. World Economic Output Over 50 Years, 1984-2034 (2005 PPP dollars)



The Economic Center of Gravity Shifts East

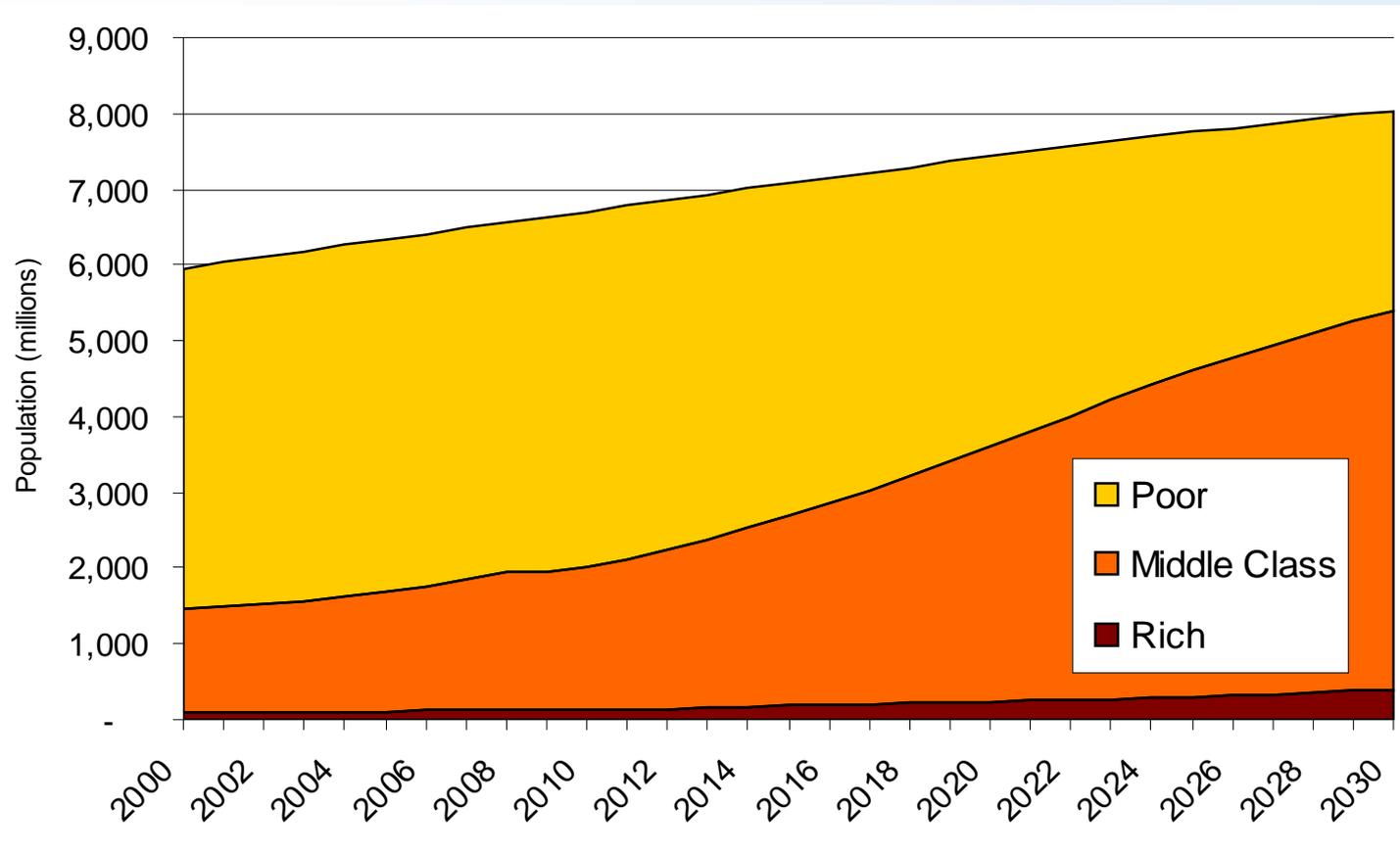
Economic Center of Gravity: 1965 - 2050
GDP, Market Exchange Rates



*Note: Green indicates earlier years, red indicates later years.
Orange lines highlight the latitudes of DC and Beijing (for reference).

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A Surge in the Global Middle Class



A Crossover from West to East

Size of the Middle Class, 2009 - 2030
(millions of people and global share)

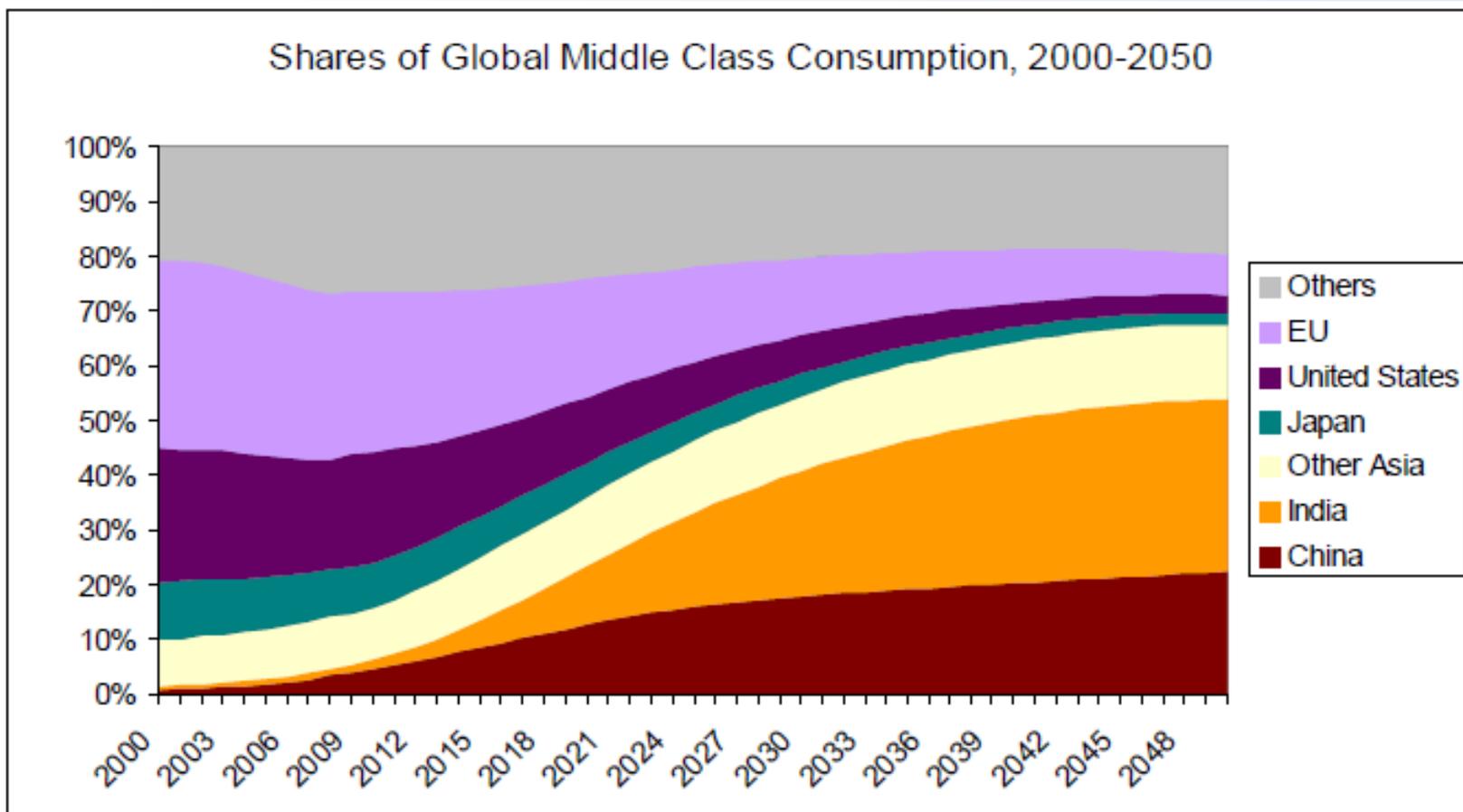
	2009		2020		2030	
North America	338	18%	333	10%	322	7%
Europe	664	36%	703	22%	680	14%
Central and South America	181	10%	251	8%	313	6%
Asia Pacific	525	28%	1,740	54%	3,228	66%
Sub-Saharan Africa	32	2%	57	2%	107	2%
Middle East and North Africa	105	6%	165	5%	234	5%
World	1,845	100%	3,249	100%	4,884	100%

A Crossover from West to East

Middle Class Consumption
(billions of 2005 PPP\$ and global share)

	2009		2020		2030	
North America	5,602	26%	5,863	17%	5,837	10%
Europe	8,138	38%	10,301	29%	11,337	20%
Central and South America	1,534	7%	2,315	7%	3,117	6%
Asia Pacific	4,952	23%	14,798	42%	32,596	59%
Sub-Saharan Africa	256	1%	448	1%	827	1%
Middle East and North Africa	796	4%	1,321	4%	1,966	4%
World	21,278	100%	35,045	100%	55,680	100%

India and China Make Waves in the Global Middle Class



The New Big Spenders

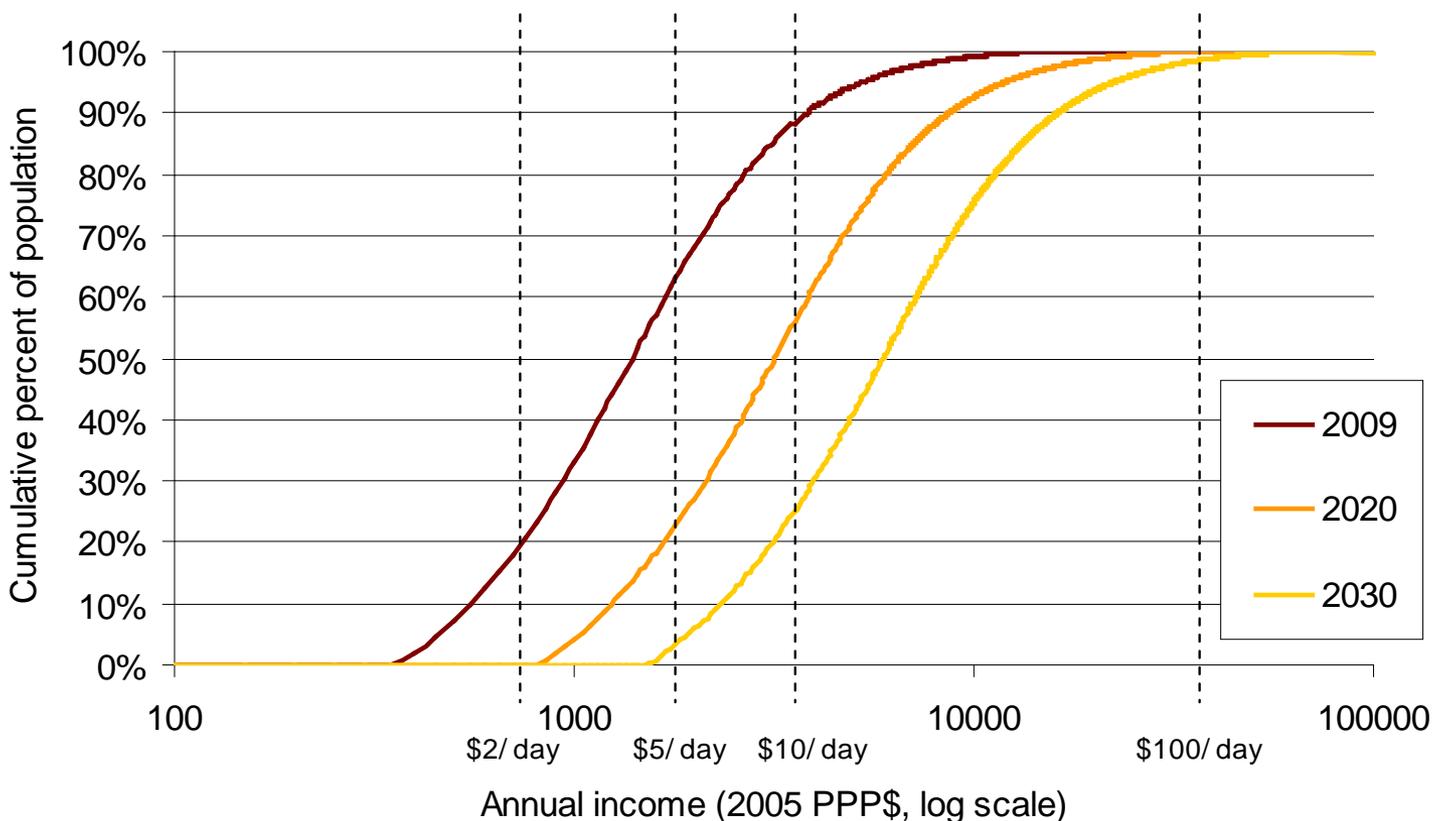
Middle Class Consumption – Top 10 Countries
(billions of 2005 PPP\$ and global share)

	2009			2020			2030		
1	United States	4,377	21%	China	4,468	13%	India	12,777	23%
2	Japan	1,800	8%	United States	4,270	12%	China	9,985	18%
3	Germany	1,219	6%	India	3,733	11%	United States	3,969	7%
4	France	927	4%	Japan	2,203	6%	Indonesia	2,474	4%
5	United Kingdom	889	4%	Germany	1,361	4%	Japan	2,286	4%
6	Russia	870	4%	Russia	1,189	3%	Russia	1,448	3%
7	China	859	4%	France	1,077	3%	Germany	1,335	2%
8	Italy	740	3%	Indonesia	1,020	3%	Mexico	1,239	2%
9	Mexico	715	3%	Mexico	992	3%	Brazil	1,225	2%
10	Brazil	623	3%	United Kingdom	976	3%	France	1,119	2%

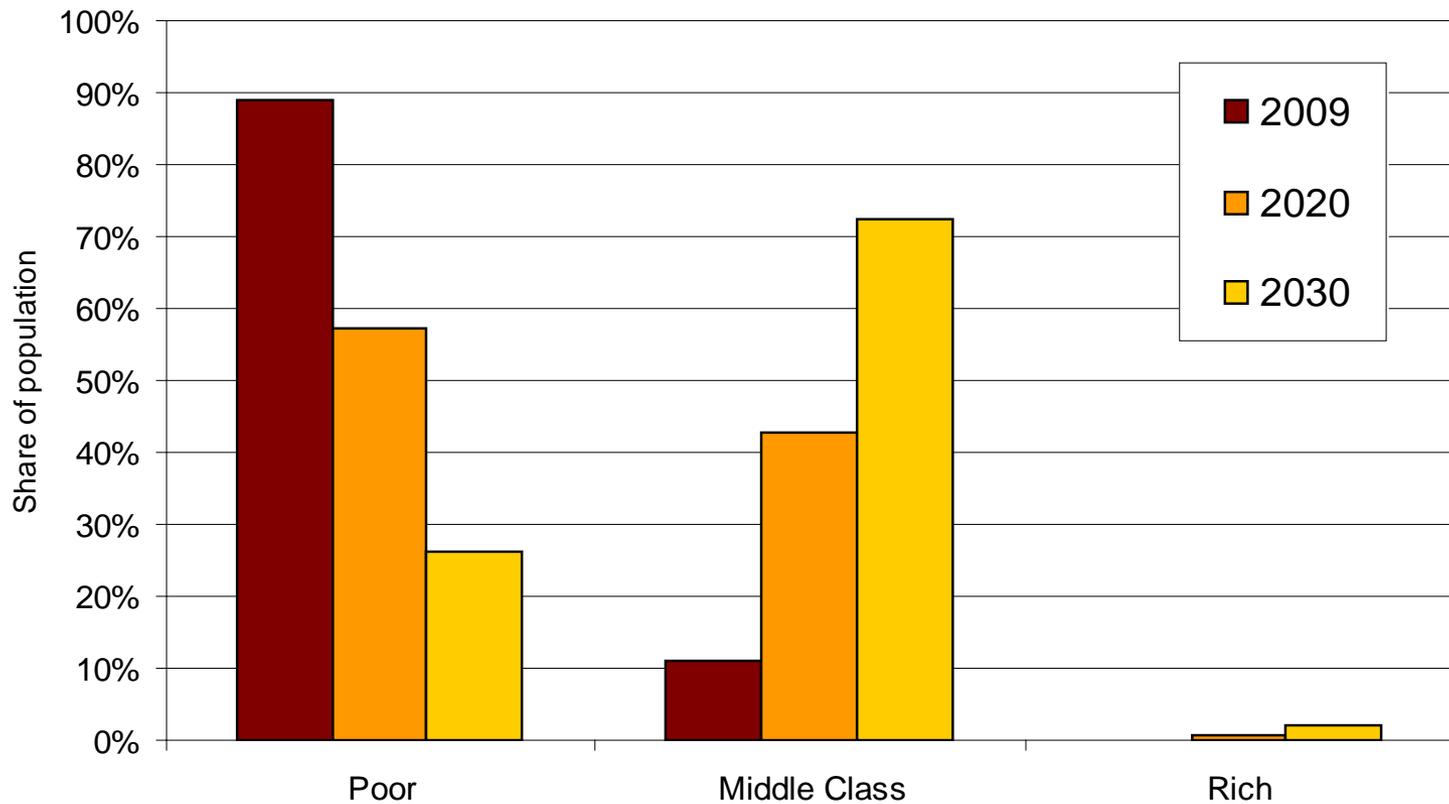
A Closer Look at China's Middle Class

- Already the second largest middle class in absolute terms, at 157 million consumers (US is #1)
- But small in relative terms (only 12% of the population)
- Also small given its level of development, due to income inequality and (especially) small share of household expenditure in GDP
- By 2030 over 70 percent of China's population could be middle class, consuming nearly \$10 trillion in goods and services

China is on the verge of becoming a middle class nation



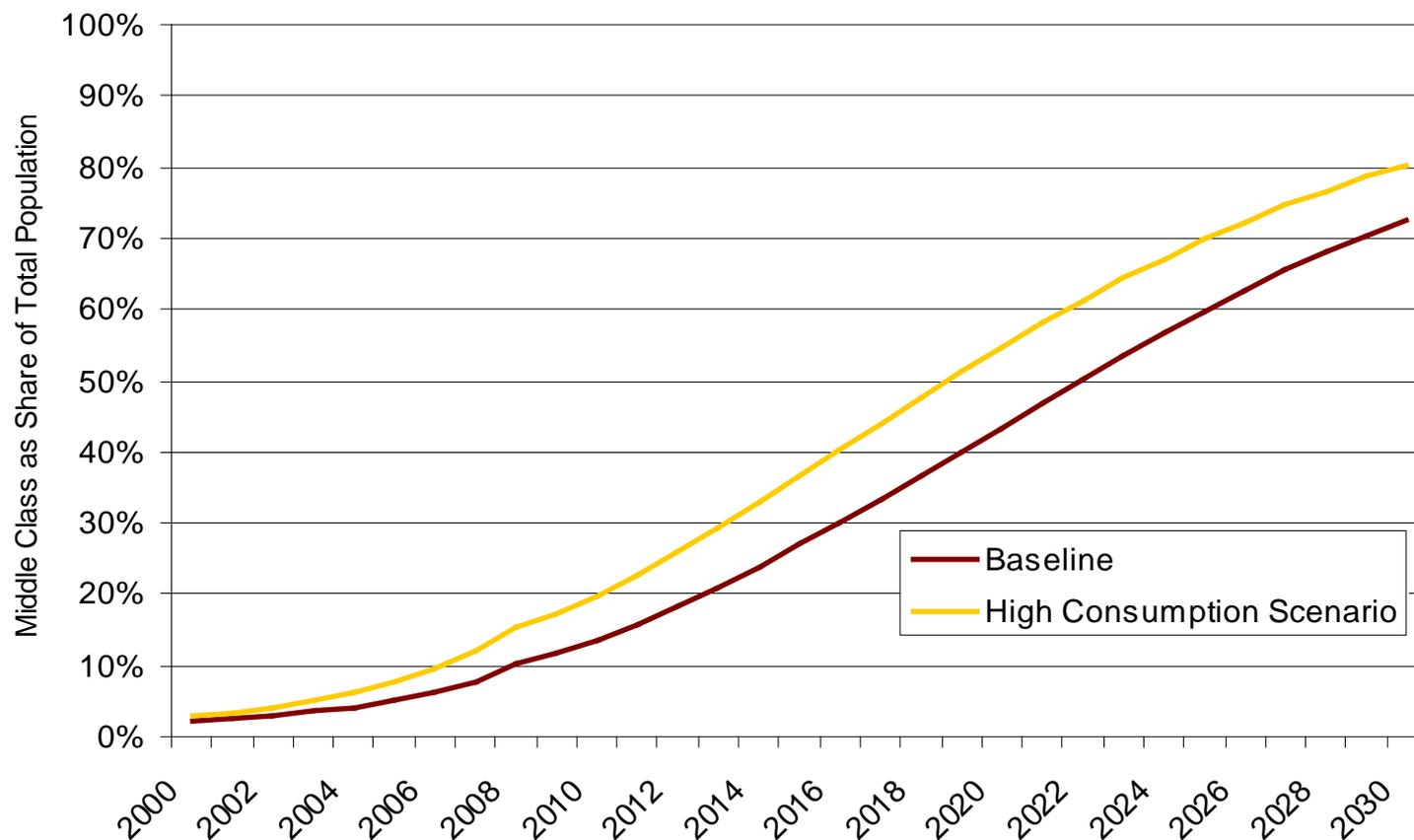
China's Booming Middle Class



How Can China Increase the Size of its Middle Class?

- Address Inequality (current spatially adjusted Gini 45.3)? Important in the long term, but won't help middle class in the short term.
- Lower household savings rates? Perhaps desirable, but difficult to achieve (even the near poor save 17%). Will require significant institutional reform.
- Best policy response is to increase share of household income in GDP.
 - Raise household consumption from 36 percent of GDP to at least 46 percent in the short run
 - Aggressively use profits from SOEs to reduce taxes, increase social services
 - Reduce labor taxes
 - Address housing shortages

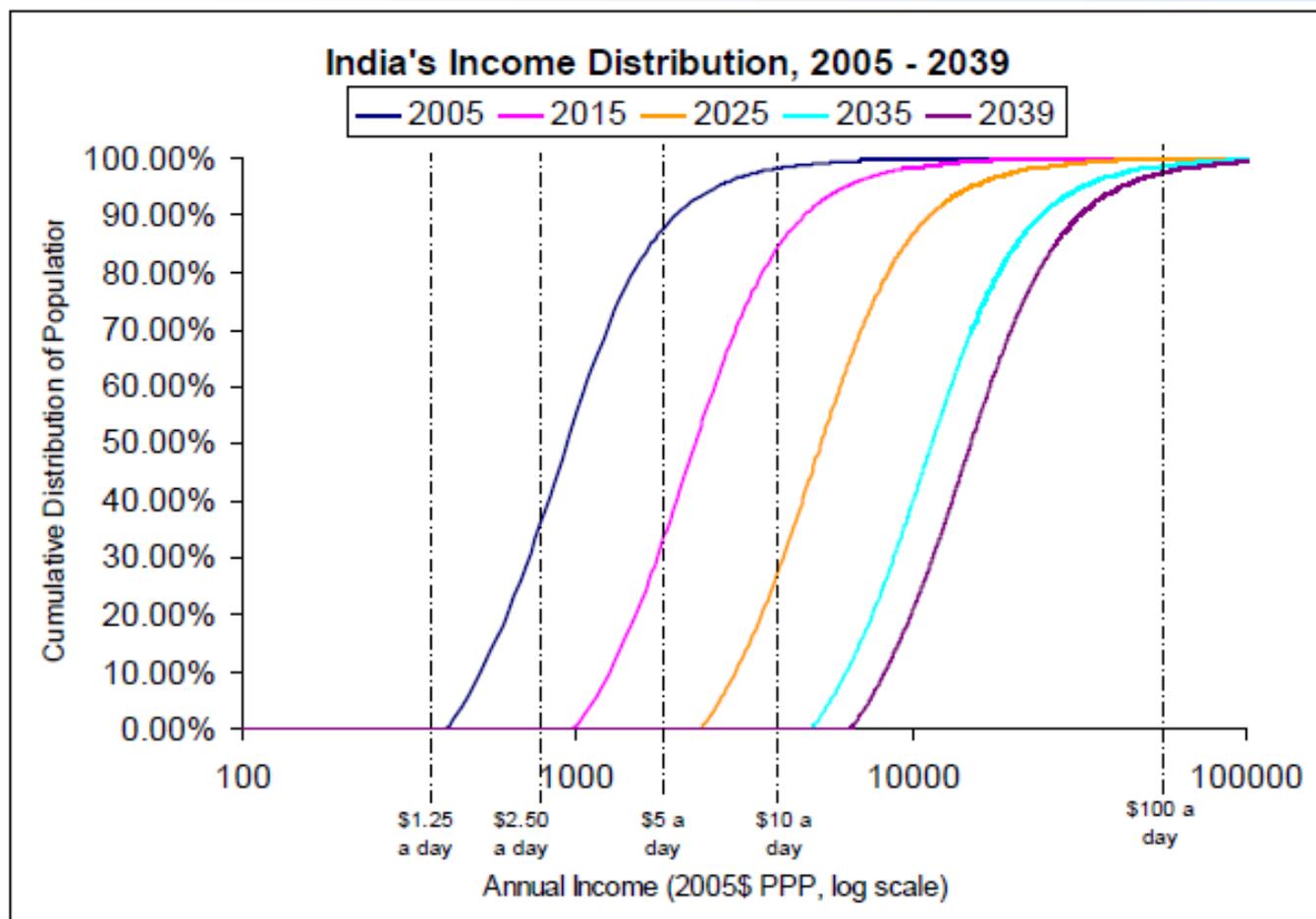
Higher Consumption Accelerates the Rise of China's Middle Class



A Closer Look at India's Middle Class

- Small today (5% of population), but set to expand dramatically.
- India could be the world's largest middle class consumer market by 2030, surpassing both China and the US.
- Between now and 2039, India could add over 1 billion people to the global middle class.

Dramatic Expansion of India's Middle Class



Conclusion

- The world is in the throes of a major expansion in the middle class, particularly in emerging Asia. The global middle class is expected to grow from under 2 billion consumers today to nearly 5 billion within two decades.
- Middle classes are an important key driver of growth, as the income elasticity for durable goods and services for middle class consumers is greater than one.
- China and India are at the forefront of the expansion of the global middle class. The world economy can be expected to increasingly rely on the middle classes of these two Asian powers as key sources of global demand.