





# INTRODUCTION: WHY FORWARD-LOOKING MACROECONOMIC POLICIES FOR INCLUSIVE AND SUSTAINABLE DEVELOPMENT IN ASIA AND THE PACIFIC?

 The things that ensure people's welfare, those that are poor-friendly, which boost the country's economy and those having durability and sustainability should be the subjects of the progressive economists. 

Sheikh Hasina,  
Prime Minister of the People's Republic of Bangladesh

The *Economic and Social Survey of Asia and the Pacific 2013* comes at a time of continued global economic crisis and growing uncertainty over the economy, the environment and the type of politics or governance arrangements that can lead to equitable, inclusive and sustainable development. In less than a decade after the global community mobilized around the Millennium Declaration with commitments to “make poverty history”,<sup>1</sup> the world was shaken by the worst economic crisis since the Great Depression, which has come to be known as the Great Recession.



The Great Recession of 2008-2009 has exposed the weaknesses of the development paradigm, including the macroeconomic policies pursued since the early 1980s, which resulted in a rise in inequality of income, wealth and opportunities within and among countries. The global interdependence on which shared prosperity was premised had become instead a conduit for inequality, crisis and economic insecurity. Rising and volatile commodity prices, especially of food and fuel, coming on top of the economic crisis, are being exacerbated by extreme weather conditions. The interrelated shocks in food, fuel and financial markets have undermined the already precarious livelihoods of millions of people, threatening the limited progress of previous decades. Financial crises, commodity price volatility and extreme weather conditions seem to have become a “new normal”.

Thus, today’s challenges to economic and social development are now of a magnitude and complexity that was not imagined at the turn of the millennium. Therefore, the new context or “new normal” calls for reframing the development problem, including the rethinking of the macroeconomic policy paradigm that focuses not just on return to growth, but also on equality and rights, social development and environmental protection.

It is in this backdrop of acute uncertainty, that the world leaders gathered at the United Nations Conference on Sustainable Development (Rio+20), which was held in Rio de Janeiro, Brazil, from 20 to 22 June 2012, and declared: “We recognize that people are at the centre of sustainable development and in this regard we strive for a world that is just, equitable and inclusive, and we commit to work together to promote sustained and inclusive economic growth, social development and environmental protection and thereby to benefit all”.<sup>2</sup>

They also recognized the importance of job creation by calling for “adopting forward-looking macroeconomic policies that promote sustainable development and lead to sustained, inclusive and equitable economic growth...”. In recognizing

the lessons learned and successful policies and approaches in the implementation and achievement of the Millennium Development Goals, the same call was also made in paragraph 23(b) of the outcome document of the 2010 High-level Plenary Meeting of the United Nations General Assembly<sup>3</sup> (commonly known as the MDG Summit).

One might think that the above is not applicable for Asia and the Pacific in the light of the fact that the region is generally regarded as an early achiever of many of the Millennium Development Goals. The region’s unprecedented decline in poverty is the main factor behind the attainment of the Millennium Development Goal of halving the global poverty rate well ahead of the target year, 2015. The Asia-Pacific economies have been the drivers of the global economy, especially since the Great Recession. They showed remarkable resilience to the global economic turmoil, and earlier were able to recover quickly from the major regional financial crisis of 1997-1998.

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*There is a need to emphasize the inclusiveness of development in the Asia-Pacific region as well as to adopt forward-looking macroeconomic policies for addressing the large development gaps that still exist*

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The rapid transformation of some of the Asia-Pacific economies over the past four decades has been unparalleled in the history of economic development. Their transformation defied the pessimism contained in the *Asian Drama*, the three volume 1968 *magnum opus* of Nobel Laureate, Gunnar Myrdal (Myrdal, 1968). These rapidly transforming economies have often been described as “miracle economies”. One of the key features of this miracle was shared growth – the ability to achieve rapid growth without deteriorating income inequality – which has not been commonly observed in other parts of the world in the past.<sup>4</sup>

Therefore, at first sight, the additional adjective, “inclusive”, used in the title of this study, may

also appear unnecessary. Furthermore, sustainable development already encompasses social aspects, which, to some observers, would include inclusiveness. However, as elaborated below, there is a need to emphasize this particular aspect of development in the Asia-Pacific region as well as to adopt forward-looking macroeconomic policies for addressing the large development gaps that still exist.

First, in a number of countries the environment, including forest covers, fisheries, and fresh water availability, has taken a big toll as the economies grew rapidly. More importantly, the growth has been highly resource-intensive, especially fossil fuel-intensive, causing not only a rapid rise in emissions of greenhouse gases but also making countries increasingly vulnerable to shocks in the global supply chain and price volatility. Second, despite significant reduction in poverty, the region is still home to more than 800 million poor, accounting for nearly two-thirds of the poor around the world who struggle to survive on an income of less than \$1.25-a-day. Third, there was “miracle no more”; disappointingly, the rapid growth in income since the 1990s has not benefited the poor as much as the rich, causing income inequality to rise and diminishing significantly the region’s progress in social development.

Economic insecurity has also risen amid rapid growth. More than 1 billion workers in the region, comprising in excess of 70% of the global vulnerable workforce (ILO, 2013), are in vulnerable employment characterized by low wages, no benefits, no job security and difficult conditions of work that undermine workers’ fundamental rights. Food security is also very low: an estimated 563 million people are undernourished (FAO, 2011), and a large number of people are vulnerable to global food price volatility. ESCAP estimates, published in the *Economic and Social Survey of Asia and the Pacific 2011* showed that high food prices in 2010 kept an additional 19.4 million in poverty in the region. This comprised 15.6 million who would otherwise have emerged from poverty and 3.8 million who were pushed below the poverty line.

Economic insecurity and vulnerability are exacerbated by increasingly damaging natural disasters, which many believe are related to climate change and environmental degradation. Natural disasters in 2011, including the Great East Japan Earthquake and the South-East Asian floods, caused a staggering \$294 billion worth of economic losses in the region, representing 80% of global losses due to disasters in 2011 and largely exceeding the region’s 25% share in the world’s gross domestic product (GDP) (ESCAP and UNISDR, 2012). Human insecurity in the region has also risen. For example, between 1970 and 2010, the average number of people exposed to yearly flooding in Asia has more than doubled from 29.5 million to 63.8 million, and the population residing in cyclone-prone areas has grown from 71.8 million to 120.7 million. Three-quarters of global disaster deaths during the same period have taken place in the Asia-Pacific region (ESCAP and UNISDR, 2012). Nevertheless, the Asia-Pacific economies have bounced back strongly after each major natural disaster, including the 2004 Indian Ocean tsunami and recent earthquakes and severe floods.

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*Despite resilience to economic crises  
and natural disasters,  
there is much vulnerability  
and insecurity of people*

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Economic insecurity and vulnerability are particularly high in the region because most Asia-Pacific developing countries lack a comprehensive social protection system to help people regenerate their livelihoods when affected by economic crises, natural disasters or personal misfortunes. In spite of significant progress in recent years in a number of countries, including through the provision of basic health-care access and income support to the poor, public social security expenditure remains low, at less than 2% of GDP in half the countries in the Asia-Pacific region. On average, only 30% of persons above the retirement age in Asia and the Pacific receive a pension, while only 10% of the unemployed receive any benefits (ILO, 2010a).

Thus, despite the remarkable resilience of the Asia-Pacific economies to economic crises and natural disasters, the people living in this region continue to be highly vulnerable and insecure. In other words, there is a disconnect between the resilience of the economies and the resilience of the people in the region as rapid growth and economic recovery have not been inclusive and did not increase security of jobs and livelihoods. Instead, growth has been mostly jobless, that is without a commensurate growth of decent and productive employment in the formal sector. As a result, livelihood insecurity and disparities of opportunities and outcomes, including income and wealth, are on the rise and reinforcing one another, especially in the absence of a decent social protection system.

Therefore, enhancing resilience of livelihoods and the inclusiveness of the development process must be explicitly recognized as key priorities for the Asia-Pacific region when considering the development agenda beyond 2015 and assessing the challenges that lie ahead.

There is a clear need for forward-looking macroeconomic policies that focus on productive and decent employment, human and social development and environmental protection as well as on protecting the development gains in times of crisis, instead of just on inflation and the budget deficit or public debt (see box A). Experience over the past three decades has shown that low inflation and a primary

budget surplus may be a necessary but not sufficient condition for enhancing the resilience of people and attaining inclusive and sustainable development.

Forward-looking macroeconomic policies, thus, must promote the provision of “universal access to public and social services” and “social protection floors” in order to make development more inclusive and protect development gains.<sup>5</sup> As the ESCAP 2011 Theme Study, *The Promise of Protection: Social Protection and Development in Asia and the Pacific* reiterated, “a robust system of social protection not only fulfils people’s basic rights, it also establishes a firm platform for both social and economic development and provides an automatic stabilizer for vulnerable groups affected by crisis”. Therefore, “social protection must not simply be seen as a handout. It is an investment in inclusive growth. It is an investment in human capabilities to get people out of exclusion and poverty and to build resilience to risks and vulnerabilities”.<sup>6</sup>

In the context of the Asia-Pacific region, both resilience and inclusiveness have specific meanings beyond what is generally understood. In particular, as highlighted in the ESCAP 2013 Theme Study, *Building Resilience to Natural Disasters and Major Economic Crises*, resilience entails not only the ability to steer the economy and sustain growth during economic crises but also protect livelihoods and hence the resilience of people.

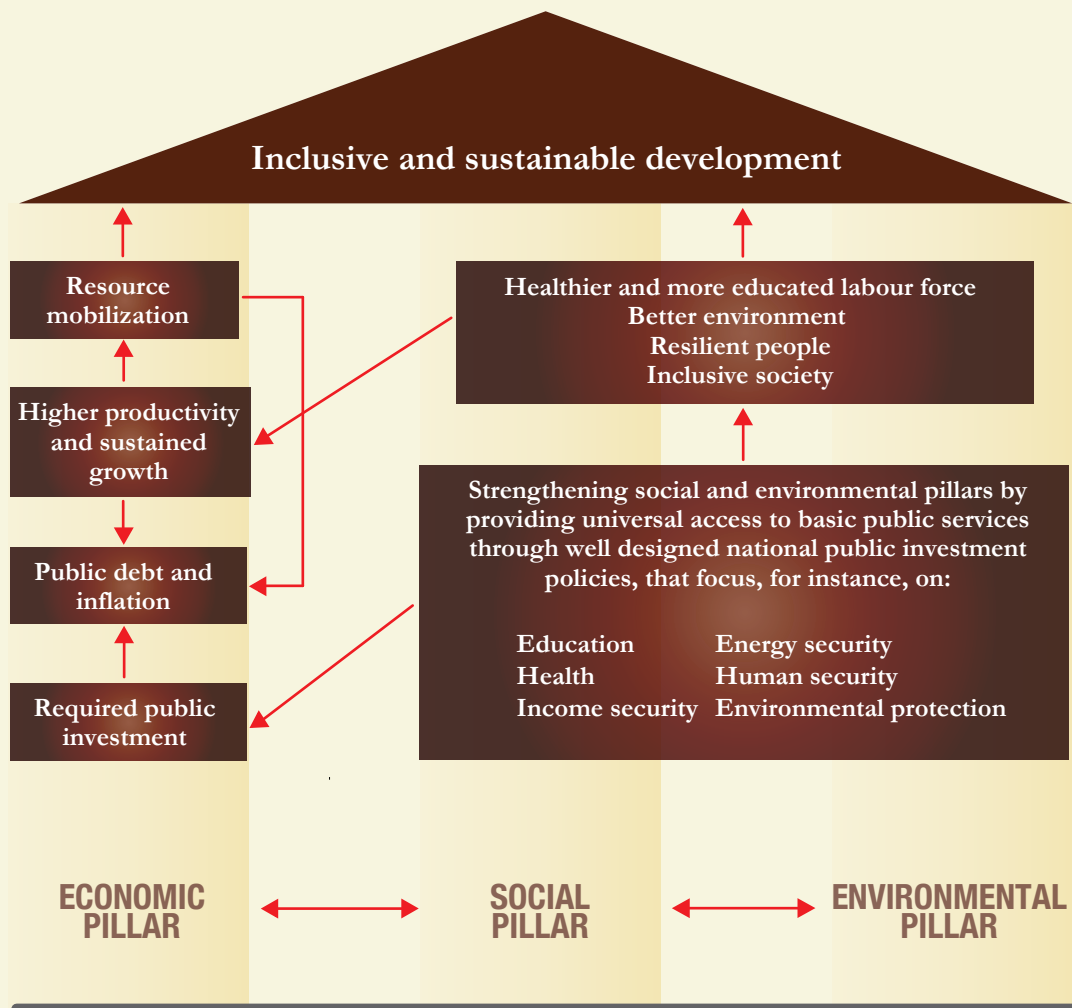
#### Box A. Forward-looking macroeconomic policies

“Forward-looking macroeconomic policies are needed to safeguard the sustainability of public investment strategies in support of broad-based growth and the achievement of the Millennium Development Goals. Macroeconomic policies should not focus narrowly on debt stabilization and curbing inflation, but should ultimately be supportive of growth of real output and employment. It is often necessary, therefore, to relax unnecessarily stringent fiscal and monetary restrictions and to use countercyclical fiscal and monetary policies to boost employment and incomes and to minimize the impact of external and other shocks on poverty. This requires countries to strengthen mobilization of domestic resources and adopt mechanisms that promote countercyclical policy responses. Enhanced international cooperation to strengthen tax revenue collection and increase sovereign debt sustainability can greatly buttress the fiscal capacities of all Governments”.

*Source:* Report of the Secretary-General A/64/665: Keeping the promise - a forward-looking review to promote an agreed action agenda to achieve the Millennium Development Goals by 2015, para. 50.

**Box B. Mainstreaming social and environmental pillars for inclusive and sustainable development**

Figure A below contains a schematic presentation of an integrated framework in which the strengthening of social and environmental pillars through the state provision of basic income security and public services to all and investment in environmental protection reinforces the economic pillar and hence helps achieve resilient and inclusive sustainable development. It also recognizes that strengthening the social and environmental pillars has a direct fiscal implication, which, in turn, has a direct macroeconomic impact on, for instance, inflation and debt. This may consequently affect growth. The framework also includes resource mobilization. It is easier to mobilize resources when they are earmarked for socially desirable causes. Moreover, increased access to basic public services, such as improved health and education, as well as greater income security will make growth more inclusive. It will also over time lead to a more productive labour force and thereby to more sustainable growth as the total factor productivity increases, strengthening in turn resource mobilization. As a result, the impacts of such public actions to strengthen social and environmental pillars on public debt and inflation may not be large, and should not destabilize the macroeconomy. Thus, it is a win-win solution.

**Figure A. An integrated framework**

Source: ESCAP.

Likewise, the inclusiveness of growth and development would mean not only social inclusion and a reduction of inequality of opportunities and income but also a reduction of people's vulnerability to crises, disasters and misfortune. This is a much broader concept than, for example, pro-poor growth, which targets only a subset of vulnerable people. In this case, the focus is on preventing people from falling back into extreme poverty by helping them regenerate their livelihoods after they are hit by shocks.

Thus, there is a close affinity between resilience and the inclusiveness of the development process. As a result of their interconnectedness, development strategies that are aimed at enhancing resilience and inclusiveness mutually reinforce each other and strengthen both the economic and social pillars of sustainable development.

There is also a feedback loop from environmental sustainability, the third pillar of sustainable development, to both the economic and social pillars, in particular resilience and inclusiveness in their broader sense (see box B). For example, better air quality or an improvement in access to better sanitation leads to better health, higher productivity and hence less vulnerability. Similarly, less dependence on environmentally harmful resource use would eventually decrease vulnerability to both disasters and price volatility and hence improve resilience. Improved access to efficient and renewable sources of energy has the potential to reduce poverty and inequality while at the same time abate harm to the environment.

Asia-Pacific countries will need to address their macroeconomic, social and ecological imbalances in an integrated manner. Strategies will therefore need to take into account the economic, social and environmental imbalances simultaneously. They will need to consider the impacts of policy measures on the three imbalances, giving the highest priority to policies that address more than one imbalance at the same time.

The *Economic and Social Survey of Asia and the Pacific 2013* comprises four chapters. Chapter 1 entails an examination on how the ongoing global economic crisis is affecting the resilience, inclusiveness and sustainability of the region's development process and to what extent its impacts are exacerbated by structural impediments caused by past policy inadequacies, such as declines in public investment in agriculture, a concern raised in the ESCAP 2008 Survey, *Sustaining Growth and Sharing Prosperity*.

The assessment finds that the prolonged global economic crisis, in particular the double dip recession in many European countries and uncertainty in the United States surrounding its fiscal policy, is testing the resilience of the Asia-Pacific economies. There has been a generalized slowdown in almost all countries in the region, including the two regional powerhouses, China and India. It is likely that this generalized slowdown is being compounded by the existence of structural impediments, such as rising inequality, falling investment in agriculture, low social protection and low fiscal revenues.

Therefore, in responding to the generalized slowdown, the countries need to simultaneously address their long-term impediments by careful design of stimulus policies, a message also contained in the ESCAP 2010 Survey, *Sustaining Recovery and Dynamism for Inclusive Development*. As the ESCAP 2012 Survey, *Pursuing Shared Prosperity in an Era of Turbulence and High Commodity Prices* noted, most countries are in a favourable position to undertake a wide range of measures to simultaneously stimulate and address structural bottlenecks to achieve inclusive, equitable and resilient sustainable development.

Chapter 2 contains an analysis of subregional impacts of the ongoing global developments in which structural impediments are identified at the subregional and country levels. The analysis indicates, for example, that progress in South and South-West Asia is being seriously hampered by power shortages; that structural problems in North and Central Asia are related to the subregion's



resource dependence and narrow economic base; and that geography and size continue to be serious obstacles for the Pacific island developing economies. In addition, over dependence on exports and a rapidly ageing population are posing a challenge for countries in East and North-East Asia and South-East Asia.

Following the identification of structural impediments in chapters 1 and 2, an argument is made in chapter 3 for the implementation of forward-looking macroeconomic policies with government playing a critical role in enhancing the resilience and inclusiveness of development in the region. The macroeconomic policy paradigm that has dominated since the early 1980s emphasizes stabilization in the narrow sense of keeping inflation at a very low single digit level and achieving a primary budget surplus or a very low deficit-to-GDP ratio. Many countries have achieved these stabilization targets at the cost of development, for example, by cutting public investment in key areas and expenditures on education and health. As shown in chapter 1, many of the current structural impediments were the result of this short-termist policy paradigm and its focus on nominal targets.

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*There is a need to bring back a balance between the stabilization and the developmental roles of macroeconomic policies*

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The dominant paradigm sees macroeconomic stability or achieving inflation and debt targets as being both necessary and sufficient for development outcomes. The experience of the 1997-1998 Asian financial crisis and the Great Recession have, however, proven this belief wrong (see box C). Macroeconomic stability since the late 1990s, what many have termed as the “great moderation” with its smoother business cycles, could not prevent the Great Recession. Worse, the pre-eminence of keeping variables, such as inflation and debt, within narrow nominal targets has made macroeconomic policies procyclical and exacerbated crises, as can be seen in the continuing economic meltdown in

the euro zone and uncertain economic recovery in the United States.

Thus, there is a need to bring back a balance between the stabilization and the developmental roles of macroeconomic policies. This would entail changing the way fiscal and monetary policies are designed and implemented and how issues of public debt or inflation are viewed. In particular, there has to be greater emphasis on the quality and composition of public expenditure, rather than on aggregate budget deficits and public debts, an argument alluded to in the ESCAP 2009 Survey, *Addressing Triple Threats to Development*. Likewise, in the case of monetary policy, there has to be more careful scrutiny of the direction or disbursement of credit instead of aggregate credit growth. In sum, the aim of fiscal and monetary policies should be to enhance the inclusiveness, resilience and sustainability of development, which will also contribute to improving human security.

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*Policy attention must also be devoted to elements of the social and environmental pillars*

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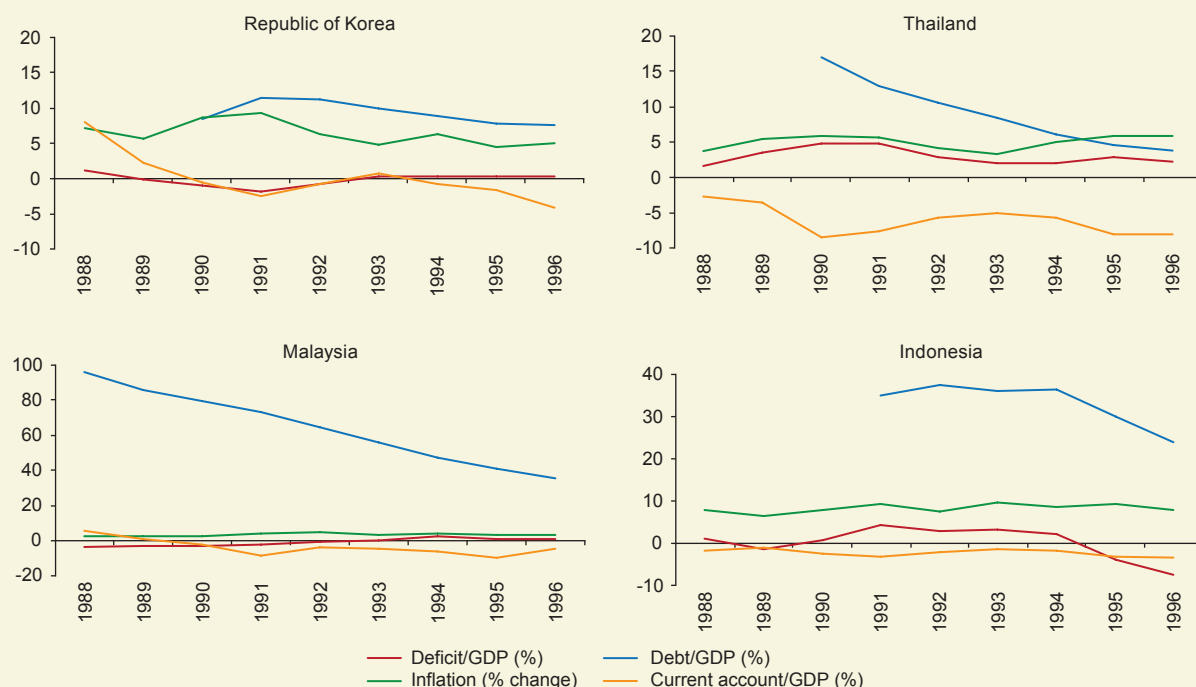
As the experience of the financial crisis has shown, it is possible to design fiscal stimulus packages and formulate monetary policies to increase public expenditure on critical infrastructure, health, education and social protection, and to extend more credit to productive and employment-intensive sectors, such as agriculture and small and medium sized enterprises (SMEs) (see box D). Carefully designed fiscal and monetary policies to support production and employment creation can support economic activity without causing inflationary pressures. Notably, countries that have retreated from developmental macroeconomics have jeopardized economic recovery at a great human and social cost. For example, Malaysia, the Republic of Korea and Thailand responded to the Asian financial crisis of 1997-1998 with well-targeted expansionary fiscal and monetary policies, which helped them recover quickly. On the other hand, Indonesia took longer to recover as it lingered in a vicious cycle of low



### Box C. Asian financial crisis despite macroeconomic stability

Macroeconomic stability in the conventional sense of single-digit inflation and low or no budget deficit did not protect countries in East and South-East Asia from external shocks, which resulted in a major financial crisis in 1997-1998. For instance, both the Republic of Korea and Thailand experienced the shock despite more stable inflation and lower debt burdens relative to GDP. Having a balanced or surplus budget also proved inadequate (see figure B).

Figure B. “Sound” macroeconomic indicators before the crisis

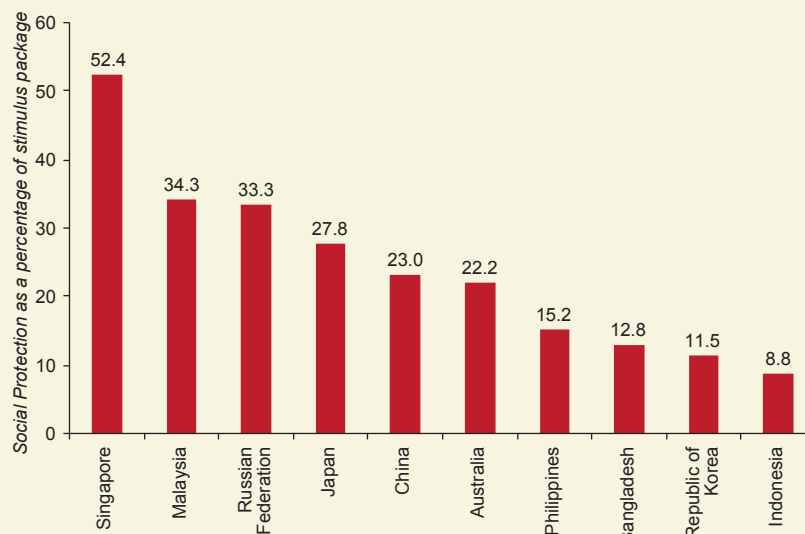


Sources: International Monetary Fund, International Financial Statistics. Available from [elibrary-data.imf.org/FindDataReports.aspx?d=33061&e=169393](http://elibrary-data.imf.org/FindDataReports.aspx?d=33061&e=169393); and International Monetary Fund, Government Financial Statistics. Available from <http://elibrary-data.imf.org/FindDataReports.aspx?d=33061&e=170809>.

growth and high public debt as the Government implemented procyclical macroeconomic policies to contain debt and keep inflation low. In sum, rethinking of macroeconomics in the region is needed in order to simultaneously tackle the short-term effective demand problem and long-term structural impediments to resilient and inclusive sustainable development.

The final chapter of the *Survey 2013* contains estimates of required public investment for a set of policies to enhance the region's resilience and inclusiveness. These policies include the provision of

an employment guarantee for a limited number of days in a year, basic social services in education and health, income security to older persons and persons with disabilities and ensuring efficient energy for all by 2030. The choice of these elements was determined partly by the structural impediments identified in chapters 2 and 3. They were also derived from the commitments made by the countries at various United Nations conferences and summits, leading to global campaigns, such as “health for all”, “education for all”, “education first”, “social protection floor” and “sustainable energy for all”.

**Box D. Stimulus packages and social protection**

Source: Zhang, Yanchun, Nina Thelen and Aparna Rao (2010). *Social protection in fiscal stimulus packages: some evidence*. Office of Development Studies Working Paper, United Nations Development Programme.

Notes: These total amounts may understate the actual size of the social protection components of the fiscal stimulus measures in some countries. This may be the result of differences in definition and the classification of additional social expenditures under different categories. Social protection measures are defined here as policy interventions to reduce poverty and vulnerability and to improve human welfare. Examples of such interventions include public education, health and housing, labour market and social protection measures, as well as contributory social insurance programmes and non-contributory safety net (social assistance) programmes.

A number of countries responded to the 2008-2009 economic crisis with significant stimulus packages. Many of these included spending on the construction and maintenance of public and social housing. For example, China announced that it would spend 400 billion yuan (\$64 billion), 10% of its total stimulus package on public housing. The stimulus package of Viet Nam included 24 trillion dong (\$1.41 billion), equivalent to 17% of the total allocated for stimulus measures, to build houses for workers and low-income families. China, Indonesia, Japan and Thailand also announced direct or indirect health funding, such as increased spending on public health. Some countries included new measures for education. For example, China spent 150 billion yuan on primary education, including on pro-poor and pro-rural health care and education; Malaysia committed 200 million ringgit (\$64.3 million) to preschool education.

The crisis has also prompted Governments to accelerate plans to expand social protection coverage. For instance, China launched a major reform in December 2009 to introduce a basic pension scheme for 700 million rural inhabitants (ILO, 2010c). Pakistan introduced the Benazir Income Support Programme for 6-7 million poor households. The Philippines launched a conditional cash transfer programme which is being rapidly scaled up in response to the crisis.

In the Asia-Pacific region, several countries provided unemployed and laid-off employees with job-training programmes. For example, Thailand targeted new graduates, while Bangladesh focused on laid-off returning migrant workers. Viet Nam offered loans at preferential rates to the poorest members of the population to encourage production and trade in rural areas. Public works programmes, sometimes referred to as cash-for-work programmes or employment guarantee schemes, were adopted in many countries in response to rising unemployment.

By highlighting these specific elements, attention is drawn in chapter 4 to the fact that rather than focusing exclusively on the economic pillar, policy attention must also be devoted to elements of the social and environmental pillars. Ensuring that public services are made available to all is a critical element in making development more inclusive. Additionally, strengthening the social and environmental pillars also fortifies the economic pillar, thereby making development more sustainable. For instance, investments in health, education and social protection will strengthen the economic pillar by increasing productivity through a healthier and more educated labour force and by reducing the precautionary motive for saving and thus increasing the amount of capital available for investment. As another example, broadening access to energy through investments in renewable energy and in technologies to improve energy efficiency contribute to reducing the impact of economic growth on energy prices and carbon emissions. These investments could also offer opportunities for technological innovations, business development and employment in promising “new economy” industries, thereby fostering development.

The exercise in chapter 4 shows that the required public investment for the set of policies to enhance resilience and inclusiveness would range between 5 and 8% of GDP for most of the countries analysed. Within these estimates, the contribution of individual policies varies, reflecting different demographic and economic characteristics. For example, the required expenditure for providing a job guarantee for a limited number (100) of days at the wage rate equivalent to respective national poverty lines ranges between 1% of GDP in China and the Russian Federation and 8% of GDP in Bangladesh. Similarly, ensuring income security to older persons would require between 1 and 4% of GDP for most countries. Such investment requirements (1) are within the affordable range for most Governments, (2) will remain fiscally sustainable and (3) will not destabilize the macroeconomy even with debt financing due to the reinforcing impact that greater investment and expenditure on inclusive development has on sustainable growth. In the

chapter, it is argued that the region will benefit from stronger productivity growth underpinned by stronger social and environmental pillars.

These results are very encouraging for fulfilling Governments’ commitment to full employment, enshrined in the *United Nations Charter* (article 55),<sup>7</sup> as well as their commitments to internationally agreed development goals derived from United Nations conferences and summits since the early 1990s. Therefore, forward-looking macroeconomic policies are needed not only to enhance the resilience of the people and inclusiveness of sustainable development but also to enhance human security and deliver on the right to development. Finally, the public policies discussed in this Survey can strengthen the social glue that binds communities and enhances citizenship.

## Endnotes

<sup>1</sup> See General Assembly resolution 55/2 of 12 February 2010.

<sup>2</sup> See General Assembly resolution 66/288 of 27 July 2012.

<sup>3</sup> See General Assembly resolution 65/1 of 22 September 2010.

<sup>4</sup> See for example Fei, Ranis and Kuo (1979), Adelman and Robinson (1978) and Campos and Root (1996).

<sup>5</sup> See General Assembly resolution 65/1 of 19 October 2010.

<sup>6</sup> See <http://southwest-sro.unescap.org/oes/statements/2010/ST20100421-social-protection-agenda.html>.

<sup>7</sup> United Nations, *Charter of the United Nations and Statute of the International Court of Justice* (San Francisco, 1945). Available from <http://treaties.un.org/doc/Publication/CTC/uncharter.pdf>.

