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* The shaded areas of the map indicate ESCAP members and associate members.
2013 Year-end Update

ECONOMIC AND SOCIAL SURVEY
OF ASIA AND THE PACIFIC
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KEY MESSAGES AND FINDINGS

Growth performance in developing Asia-Pacific economies is expected to rebound moderately after a sluggish 2013 but growth will remain subpar

» GDP growth in developing Asia-Pacific is now expected to expand by 5.6% in 2014, up from an expected 5.2% in 2013, but lower than the 6.0% projection indicated in the Survey 2013.

» The key economies of China, India, Indonesia and Thailand with large domestic markets have experienced moderate growth in 2013 compared to their recent strong performance.

» The region may continue to experience a “new normal” of lower growth compared to recent years—as highlighted in the Survey 2013.

The region will be impacted by an uncertain recovery and related policies in the developed world

» Slow recovery and policy uncertainty in developed economies continue to impact the region.

» The negative effect of a possible reversal of the easy money policy of the United States could be offset by a budget agreement to prevent automatic budget cuts.

» Trade protectionist policies in the developed world are significantly impacting exports and GDP growth rates in the region.

Inherent macroeconomic weaknesses and structural impediments continue to affect larger economies of the region

» Growing economic and social inequality, including remaining gender inequalities, are having considerable negative impacts on shared prosperity.

» The low growth environment is challenged by rising inflationary pressure and balance-of-payments deficits.

» The region, especially South and South-West Asia, continues to have large infrastructure and productive capacity gaps.

Job creation is mixed and concerns about job quality remain pervasive

» Only seven developing economies in the region witnessed year-on-year job growth in 2013, with varying magnitudes compared to 2012.

» Informal and vulnerable jobs remain high in the region.

» Young people continue to face serious challenges in securing decent and productive employment.

The economies of Asia and the Pacific are at a turning point and their policies during this period of transition will determine the outlook for more inclusive and sustainable development

» Forward-looking macroeconomic policies will be required to address structural impediments and policy challenges.

» There is a clear opportunity for regional cooperation to address structural impediments.
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<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
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<tr>
<td>ESCAP</td>
<td>Economic and Social Commission for Asia and the Pacific</td>
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<td>FAO</td>
<td>Food and Agriculture Organization of the United Nations</td>
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<td>GDP</td>
<td>gross domestic product</td>
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<td>IFAD</td>
<td>International Fund for Agricultural Development</td>
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<td>ILO</td>
<td>International Labour Organization</td>
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<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
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<tr>
<td>OECD</td>
<td>Organization for Economic Cooperation and Development</td>
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<tr>
<td>SME</td>
<td>small and medium-sized enterprise</td>
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<tr>
<td>UNCTAD</td>
<td>United Nations Conference on Trade and Development</td>
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<td>UNDP</td>
<td>United Nations Development Programme</td>
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<td>World Food Programme</td>
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<td>World Meteorological Organization</td>
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INTRODUCTION

The economies of Asia and the Pacific are at a turning point. Thus, the manner in which the current transition is managed will have a long-term impact on the region's inclusive and sustainable development path. Economies will experience a relatively muted growth performance in the coming months as exports to the developed world are still below the pre-crisis level while intraregional growth led by major economies within Asia and the Pacific is unable to make up the slack. This is in contrast to the past two years, when the region's emerging powerhouses had been buttressing the Asia-Pacific economic recovery in the face of weakness and uncertainties in the developed world.

Developing Asia and the Pacific is forecast to expand by 5.6% in 2014, up from an expected 5.2% in 2013

On the whole, growth performance in developing Asia-Pacific economies is expected to rebound moderately after a sluggish 2013. Developing Asia and the Pacific is forecast to expand by 5.6% in 2014, up from an expected 5.2% in 2013. Support will come from governments' emphasis on domestic-led growth, with greater attention given to improving infrastructure and other types of social investment in line with recommendations in the Survey 2013.¹

On the other hand, the prospects for the developed world are still volatile and subject to a number of potential speed bumps, especially in the economies of the European Union. The United States has recorded some positive growth since 2010, but unemployment remains stalled at high levels. The economy of Japan is expected to grow relatively robustly in the coming year, as dormant consumer and business confidence seems to have been reignited by recent macroeconomic stimulus policies.

The year 2013 has been marked by a considerable slowdown in the domestic markets of some of the largest developing economies in the region, specifically India and Indonesia. Other important economies with significant domestic markets, such as Malaysia and Thailand, have also not maintained their previous growth dynamism. There are considerable concerns that the structural causes behind the slowdown in domestic demand in these economies are not likely to be dealt with adequately in the year ahead. Therefore, despite the forecast of a modest pick-up in growth in 2014, the region may continue to experience lower growth compared to recent years—a “new normal” for many economies in the region—as highlighted in the Survey 2013.

The Survey 2013 also highlighted the need for shifting policies to focus on greater and sustained development-oriented investment to boost domestic demand, protect the basis for inclusive economic growth and enable the economies in the region to build the conditions of economic and social progress. These are prerequisites for achieving sustainable development that will lie at the core of the United Nations development agenda beyond 2015.²

Many countries in the region would have to diversify their economies and sources of demand by addressing past policy inadequacies that contributed to growing structural impediments and by strengthening intraregional

cooperation. The export-led model of the past two decades did produce a decline in absolute poverty in the region, but that has been accompanied by high and rising levels of inequality. The future sustainability of such a model is also debatable since these export-dependent economies would have to depend on the low and volatile levels of absolute growth in the developed world which continues to struggle to sustain a recovery from the Great Recession of 2008–2009.

Due to uncertainties in the overall prospects and resulting policy developments of the developed world, there is continued potential for negative spillover effects on economies in the region. For example, possible “tapering” (claw back of excess liquidity) of the quantitative easing programme of the Federal Reserve of the United States caused short-term financial and asset market jitters in mid-2013. The longer-term impact of such a move will have significant macroeconomic implications for the region, and policymakers need to adapt national economic strategies accordingly.  

For example, long-term interest rates are expected to rise when the quantitative easing does come to an end and the Federal Reserve claws back excess liquidity in the United States. Thus, economies in the region may have to impose higher interest rates than otherwise desired in order to preserve some degree of portfolio inflows or prevent net capital outflows. This will mean that economies will not find it as easy as in the recent past to use accommodative monetary policies to counteract downward growth pressures. Higher interest rates are likely to have detrimental impacts on businesses, especially on SMEs, and hence on growth and productive employment generation. In parallel, the constrained domestic growth prospects of the region have increased the need for productive government spending to ensure inclusive growth and sustainable development in coming years. This is also needed to address critical infrastructure shortages and productive capacity gaps. However, a number of countries, especially in South and South-West Asia subregion, do not seem to have enough fiscal space for such spending.

The constrained domestic growth prospects of the region have increased the need for productive government spending

The slowdown in larger economies of the region and the outflow of capital from countries viewed as suffering from inherent macroeconomic weaknesses highlight key development gaps and policy challenges in these economies. These include infrastructure shortages and the lack of effective government policies to support broad-based agricultural and industrial development. These deficiencies have led to significant gaps in productive capacity which are contributing to inflationary pressure as supply fails to keep pace with demand in growing economies. Inflationary pressure has been exacerbated in emerging economies by capital inflows in recent years due to the easy money policy in the developed world, especially the United States. This has manifested in asset market bubbles, significantly increasing risk to domestic financial sector stability.

The need is ever greater for the region to forge cooperation to find permanent solutions to these problems and thus promote inclusive and sustained

growth from within. A major initiative in this regard has been recent renewed interest in the formation of an Asia-Pacific infrastructure bank to match the huge investment needs of many economies with the large foreign exchange reserves of some of their neighbours, as proposed over many years by ESCAP and recently discussed at the preparatory meetings for the Ministerial Conference on Regional Economic Cooperation and Integration in Asia and the Pacific, which is to be convened by ESCAP in December 2013.

**GROWTH RECOVERY UNDER PRESSURE FROM WITHIN**

Developed economies on a volatile and uncertain trajectory

There are still uncertainties about the growth prospects for most of the major developed economies. While in the past few years the United States had been the first to display positive though volatile growth, the country has recently been joined by Japan. Recovery in the European Union is, however, in danger of remaining stagnant, as indicated by the data from the grouping in recent quarters (see figure 1). It is expected that the developing economies in the region will continue to face an uncertain global growth environment in the near term. The role of Japan remains important and the effects of the macroeconomic stimulus policies of the government are likely to have a host of effects for the region in coming months.

Due to the importance of the United States economy for the region, there will be significant implications of the major policy developments there in 2014 of “tapering” and budget cuts. ESCAP analysis suggests that under a worst-case scenario, the effects of capital volatility due to “tapering” could cut GDP growth in the most affected countries in the region — Malaysia, the Philippines, the Russian Federation and Thailand — by up to 1.2-1.3 percentage points in 2014. However, if the United States could avoid the automatic spending reductions, called “sequestration”, due to the Budget Control Act in 2014, the negative output effect of the “tapering” would be at least partially offset. For instance, under the worst-case “tapering” scenario, but with a budget deal to prevent sequestration, output levels in Malaysia and Thailand would fall by about 0.8% relative to the baseline, as opposed to 1.2% under the worst-case “tapering” scenario in the absence of a budget deal.

The prospects of the European Union continue to look uncertain in coming months. For example, GDP growth was estimated to have slowed in Germany and contracted in France during the third quarter of 2013, as compared to the previous quarter. The unemployment rate is stubbornly high among many member countries of the grouping. The risk of further prolongation of the crisis requires constant monitoring and policy coordination, especially in order to balance austerity with growth.

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Within the region, the economy of Japan has seen an upturn in its growth with a set of macroeconomic expansionary policies which came into effect in 2013. The bond-buying programme instituted by the Bank of Japan with the objective of achieving an inflation rate of 2% has been the largest quantitative easing programme ever seen globally as a proportion of GDP. The programme was increased from 91 trillion yen in March 2013 to 126 trillion yen in September 2013. The injection of money into the domestic financial system has led to a boost in asset prices and thus household wealth and consumer expenditure. The other component of policies proposed to be introduced in coming months is a programme of domestic reforms to increase the effectiveness of the private sector. These are proposed to include, among others, tax breaks to: encourage business firms to purchase equipment; fund research and development; commit to environmentally friendly or earthquake-resistance construction; boost investment in start-up technologies; raise workers’ salaries by 2% from recent levels; encourage homebuyers; and make cash payments to 24 million people in low-income households. A careful balancing act will be required between short-term policies to kick-start self-


Note: GDP growth rates are based on seasonally adjusted, annualized data.
sustaining growth in the economy and long-term policies to maintain debt at manageable levels.

It is notable that while Japan is similar to some European economies in having relatively high public debt, the country has remained free of pressure from financial investors and therefore has had more macroeconomic policy independence. The composition and ownership of government debt has major implications for the flexibility of fiscal policy and monetary policy. Japan benefits from low foreign ownership of the country’s government bonds. The available estimates indicate that foreigners own about 5% of Japanese government bonds while this figure is significantly higher, for example, in Greece (70%) and Spain (38%).

**The composition and ownership of government debt has major implications for the flexibility of fiscal policy and monetary policy**

This is a significant macroeconomic policy lesson. That is, countries should try to avoid foreign borrowing, especially short-term in nature. This policy lesson is also reinforced by recent turmoil in some of the emerging economies in the region which have been financing large balance of payments deficits through short-term capital flows as highlighted in the following section.

The financial markets in the region have seen an increase in portfolio inflows from Japan. In a way, funds from Japan have provided a buffer at a time when money has exited to the United States in expectation of the eventual ending of that country’s quantitative easing programme. Nevertheless, the inflow of funds from this new source has introduced a potential new source of volatility for regional financial markets. This also means that expansionary monetary policy in Japan is less effective as excess liquidity leaks abroad.

**Slowdown in major economies in the region due to domestic challenges**

For a number of internal reasons, the key economies of China, India and Indonesia, which have large domestic markets, have experienced moderate growth in 2013 compared to their recent strong performance. However, the moderation of growth in China is of somewhat less concern. This is because, first, the growth (current estimate of 7.5% in 2013; forecast of 7.3% in 2014), though moderate, remains high by international standards. Second, the country, while having an important domestic market, is also a major exporting power and remains attractive for foreign direct investment. Therefore, Chinese growth, though moderate compared to recent historical past, is likely to remain stable in the year ahead. Third, the country has been actively attempting to address inequality and establish a more balanced economy, which has caused growth moderation, but the growth is likely to be more inclusive than in the previous investment-dominated model.

Of greater concern are the recent performance and policy challenges of other large countries in the region. For example, India and Indonesia have seen sharp falls in their currency vis-à-vis the United States dollar. These events are, however, a symptom of deeper challenges for these economies. It is increasingly clear that foreign short-term capital cannot be depended upon to manage rising balance of payments deficits caused mainly by high imports of non-essential consumer goods. A more sustainable approach in the long-run would be through addressing productive capacity gaps to enhance exports and tackling rising inequality which
is fuelling conspicuous consumption. In the short-run, countries would need to manage consumer import levels.

It is increasingly clear that foreign short-term capital cannot be depended upon to manage rising balance of payments deficits caused mainly by high imports of non-essential consumer goods

In the case of India, growth has declined in recent years, and virtually remained the same between 2012 to 2013. This has been driven by lower business confidence due to government policy uncertainty, high inflation (10.9% in 2013) caused among others by deregulation of administered prices, surge in food prices and falling Indian rupee, and infrastructure bottlenecks. Relatively high interest rates to tackle inflation and prevent currency depreciation have prevented supportive monetary policies. On the other hand, fiscal policy is constrained by the budgetary position of the government (with budget deficit of 6.9% of GDP in 2013) and its pledge to reduce the deficit in coming years. The budgetary situation of the government and its resulting inability to engage in adequate productive spending highlights the ongoing challenge of addressing the revenue side of the fiscal equation.\(^5\) Implementing fiscal reforms, involving both revenue raising measures and non-development expenditure cutting may be difficult with elections due in 2014. While this may have some positive impact on GDP growth in the short-run, it will also add to the inflationary pressures and the current account deficit. Nevertheless, there is considerable potential for renewed growth dynamism in the country given appropriate policy actions.

The difficulties of Indonesia in the capital markets have also been a symptom of the deeper challenges facing the country’s future performance. This year has seen the lowest growth (5.7% in 2013) in the economy in recent years. Similarly to India, the lingering challenge of high inflation currently estimated at 8.9% in 2013 compared to 4.3% in 2012 driven by fuel subsidy cuts, currency depreciation and food prices is a serious obstacle to growth. With the country’s growing domestic market fuelled mainly by a rise in the consumption of the more affluent, the current account experienced a record deficit. At the same time, export performance was constrained by the slowdown in global natural resource demand, most significantly from China. Indonesia, too, has been financing growing current account deficits with foreign short-term portfolio capital inflows. Interest rates have had to remain relatively high because of inflation and to maintain currency values as well as inflows of foreign capital. The Government of Indonesia, with a budget deficit estimated at 2.4% of GDP in 2013, is in a better position than India in terms of fiscal resources to support the economy amid the current slowdown. However, this may change due to expected higher spending in view of the election in 2014.

Two other important economies in the region which have a significant domestic component, Malaysia and Thailand, have also experienced growth slowdowns partly attributable to local factors. Both countries have been affected by the difficult global trade environment in 2013, which has led to sharp reductions in their current account surpluses. While in the past similar situations were countered with strong domestic expenditure, increasing domestic debt — both public and private — is preventing such

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\(^5\) For further information, see India, Ministry of Finance, Annual Report 2012-13. (New Delhi, Budget Division, 2013).
balancing in the current circumstance. Government debt in Malaysia is the highest of all countries in South-East Asia and of many emerging economies in Asia and the Pacific. The unfavourable fiscal position has been partly a result of government non-development spending. Household debt (about 80% of GDP in 2012) is similarly one of the highest in the region, fuelled by easy access to loans. Government attempts to reduce public debt have impacted public spending this year, while measures taken to control household spending on assets such as property is also impacting private consumption.

In the case of Thailand, the major challenge is in the household sector. As in Malaysia, household debt in Thailand, at nearly 80% of GDP, is one of the highest in the region.\(^6\) The recent slowdown in consumption can be partly attributed to consumers’ balance-sheet adjustment because of the build-up of repayments. Furthermore, delays in government implementation of its large infrastructure spending plan have constrained the contribution of investment to growth.

Recent research reveals a strong positive relationship between inequality and rising household debt.\(^7\) Preliminary ESCAP analysis of selected country level data during the post-crisis period from 2008 to 2010 with regard to household debt and inequality supports this. With income growth lagging behind, low- and lower-middle-income populations have to resort to debt-financed consumption, made possible by the easy availability of credit, leading to ever rising household debts in some economies. The easy availability of credit, however, has not only served to temporarily dampen wage demand and hide rising inequality, but also made this group of people more vulnerable to shocks.

Among the major economies with large domestic markets in the region, a bright spot has been the performance of the Philippines. The economy has seen its highest growth in years — above 7% in the last four quarters through the third quarter of 2013. The role of remittances in supporting buoyant domestic consumption in the country has been important. The latest available figure suggests that, until October 2013, the Philippines had received remittances of about $26.1 billion, which constituted 9.8% of GDP.\(^8\) Investment has also benefited from a supportive policy environment. Inflation has remained benign, offering the opportunity to support growth through accommodative monetary policy. In the Philippines, a relatively low budget deficit (2% of GDP in 2013) has also allowed for substantial government spending during 2013 in infrastructure and other basic services. The prospects are positive in 2014, despite the losses resulting from Typhoon Haiyan in 2013 (see box 1). Concerns remain, however, regarding the high unemployment rate and relatively low investment level compared to other similar South-East Asian economies.

**Struggling export performance**

World trade growth fell to 2.0% in 2012 from 5.2% in 2011, and is predicted to grow by only 3.3% in 2013. Due to the weak recovery in international trade in 2013, several economies in the region registered decelerating export growth during the first three

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\(^8\) For latest data and analysis on migration and remittances, information is available from http://go.worldbank.org/092X1CHH4D0 (accessed 21 November 2013).
Box 1: The Typhoon Haiyan disaster in the Philippines

On 8 November 2013, Typhoon Haiyan (known locally as Yolanda) wreaked havoc on the Philippines with winds estimated at 315 kilometre per hour (195 miles per hour). It affected over 14.9 million people in nine regions, and caused enormous loss of life, with 5,759 (as of 5 December 2013) confirmed dead, 4.13 million people have been displaced and 1,210,179 houses destroyed. The destruction caused by the super-typhoon was especially serious for vulnerable communities. For example, in the city of Tacloban, it is the poor and marginalized, particularly women, children, the elderly and persons with disabilities, who have been hit hardest. The loss is expected to be severe among small-scale business owners and the informal sector, marginal farmers and poor households, as they often lack buffers against sudden, external shocks. Small and medium-sized enterprises were particularly at risk, as the typhoon wiped out all or major parts of business infrastructure.

A recent ESCAP report finds that disasters can adversely affect the achievement of the Millennium Development Goals. When a portion of GDP is lost because of a disaster, progress towards the attainment of the Goals is set back, as resources allocated for poverty reduction may be diverted towards recovery and reconstruction. Therefore, the scale of impact of this devastating typhoon underscores the need for further mainstreaming disaster risk reduction into development strategies.

As with other natural disasters in the region, Typhoon Haiyan served as a stark reminder that several economies in the Asia-Pacific region are the most vulnerable to climate-related disasters globally and are likely to be among the most affected by the consequences of a changing climate.

ESCAP has long been advocating the strengthening of regional cooperation among countries in Asia and the Pacific to address vulnerabilities and risks associated with natural disasters and the effects of climate change in order to pursue a sustainable development path.

The ESCAP/WMO Typhoon Committee, an intergovernmental body comprising 14 member States including the Philippines established in 1968, has been promoting and coordinating the planning and implementation of measures to minimize the loss of life and material damage caused by typhoons in the ESCAP region. In particular, the Committee provides practical policy recommendations on how the typhoon early warning system can be made more efficient and effective by regional cooperation among ESCAP member States.

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b Figures continue to change as additional reports are verified. These figures are as of 5 December 2013.
d For example, in November 2013, Viet Nam experienced massive flooding which swept the central provinces, costing lives and causing severe damage to property.
quarter of the year.\footnote{See World Trade Organization, World Trade Report 2013: Factors Shaping the Future of World Trade (Geneva, 2013), Available from www.wto.org/english/news_e/pres13_e/pr688_e.htm. The report noted that the projected trade growth of 3.3% in 2013 would be below the 20-year average of 5.3% and well below the pre-crisis trend of 6.0% (1990-2008).}


High-frequency monthly data in 2013 shows that several countries in East and North-East Asia and South-East Asia were struggling to register positive export growth in year-on-year terms (see figure 2). In particular, Indonesia and Malaysia have recorded several months of negative export growth, as have the Philippines, the Republic of Korea and Thailand. While China’s export growth continued to expand in 2012 and until the third quarter of 2013, India’s export growth remained under stress although improving somewhat in 2013. Export growth in both China and India remains significantly lower than their pre-crisis growth rates (19.5% and 14.5%, respectively, between 1990 and 2008). The Republic of Korea’s exports have recovered in recent months due to strong growth in the information technology sector. The Russian Federation has registered some positive export growth in recent months, while Fiji’s performance is relatively slow.

More positively, merchandise exports in South and South-West Asia have, in general, rebounded in 2013 as compared to their growth in 2012. Bangladesh, India, Pakistan and Turkey recorded several months of positive export growth in 2013 due to improvement in some sectors including ready-made garments in Bangladesh, and also to currency depreciation in the case of India. However, Sri Lanka has recorded several months of negative export growth, as has Nepal.

Protectionism fears continue

There are growing concerns about possible impacts on Asia and the Pacific of trade protectionist policies in the developed world due to a weak recovery of international trade and limited progress in WTO Doha Round trade negotiations.\footnote{Despite the very pessimistic outlook leading up to the ninth WTO Ministerial Conference in Bali, an agreement on such areas as trade facilitation, agriculture and a package for least developed countries was reached on 7 December 2013. For further information, see www.wto.org/english/thewto_e/minist_e/mc9_e/mc9_e.htm.}

Protectionism fears continue

In view of a long delay in successful multilateral trade deals, 2013 has witnessed a growing pace and scale of negotiations on regional trade agreements, including the proposed trans-Atlantic trade and investment partnership between the United States and the European Union\footnote{See www.ustr.gov/ttip.} and the proposed trans-Pacific partnership agreement.\footnote{For details on the measures, see Simon J. Evenett, “What Restraint? Five Years of G20 Pledges on Trade”, The 14th GTA Report, Global Trade Alert, (London, Centre for Economic Policy Research, 2013). Available from www.globaltradealert.org/sites/default/files/GTA14_0.pdf} As a result, the economies of the region are expected to face severe constraints from outside the region that could negatively affect normal trade and investment flows.
ESCAP analysis shows that the protectionist trade measures enacted by developed countries in 2012 and 2013 are having significant implications for the region’s economies in terms of lowering export growth and GDP. As a result of these trade restrictive policy measures, the estimated total loss in exports was over $62 billion in the Asia-Pacific region, which translates into over 0.4 percentage points of loss in regional GDP, during the period 2012 and 2013. At the subregional level, the estimated loss of exports was the greatest for East and North-East Asia at $33 billion, followed by $12 billion in South-East Asia, $11 billion in North and Central Asia, $6.4 billion in South and South-West Asia, and the lowest in the Pacific island developing economies. The impacts were also significant in least developed countries, as these measures negatively affected $500 million worth of their exports, about $2.6 billion in landlocked developing countries, and over $100 million in small island developing States of the region.

The estimated impact varied across subregions and economies, depending on their degree of export dependence on developed economies, especially the European Union and the United States. The current scenario assumes that import restrictive measures introduced by developed economies reduce their import growth by 1.1% compared to the baseline case in 2012. In figure A, panel a shows the impact on five subregions and least developed countries, landlocked developing countries and small island developing States, and panel b shows selected Asia-Pacific economies in 2012-2013.

China was the most impacted economy, with exports of over $13.5 billion affected in 2012-2013, followed by the Russian Federation and the Republic of Korea. Among other economies greatly affected were India, Malaysia, Thailand, Indonesia and Bangladesh. In general, it is clear that restrictive trade-related policy measures most affect those countries with higher direct and indirect exposure through regional value chains.
Figure A. Cost for exports of Asia-Pacific economies of trade protectionism measures employed by developed economies, 2012-2013

Panel a: Subregions and countries with special needs

Panel b: Selected economies


Note: The figure shows the estimated impacts of trade restrictive measures by the developed economies including the United States and the European Union in terms of exports losses in 2012 and 2013. The regional estimates are based on 40 developing countries and three developed countries in the Asia-Pacific region.
Figure 2. Growth in merchandise exports in selected developing Asia-Pacific economies, year-on-year, 2008-2013

Panel a: East and North-East Asia, North and Central Asia, South-East Asia and the Pacific

Panel b: South and South-West Asia

remedy (anti-dumping measures and countervailing measures), and on imports (tariff, tax, custom procedures, quantitative restrictions, and others), exports (duties, and quantitative restrictions) and others (local content and others). ESCAP analysis of these measures at the sectoral level shows that the manufacturing sector has been the most affected by protectionist measures in the region, followed by the agricultural sector. The most targeted products by initiations of trade remedy measures in the region have been steel, organic chemicals, machinery and mechanical appliances, paper and man-made staple fibres.\textsuperscript{15}

\textbf{Due to trade restrictive policy measures, the total estimated loss in exports was over $62 billion in the Asia-Pacific region during 2012 and 2013}

As a result of these trade restrictive policy measures, the total estimated loss in exports was over $62 billion in the Asia-Pacific region during the period 2012 and 2013, which translates into over 0.4 percentage points of loss in regional GDP.

\textbf{Growing role of services trade, remittances and tourism}

Despite volatility resulting from global economic slowdown, the developing economies have shown more resilient growth in service exports than the developed economies. This has been mainly driven by strong growth in exports of computer and information services, communication and travel services. The region is also becoming an increasingly important player in commercial services exports, broadly categorized as transportation, travel and other commercial services in recent years as analysed in the ESCAP Asia-Pacific Trade and Investment Report 2013. In particular, commercial service exports registered growth rate of 5.2\% in 2012. The use of information and communications technology, logistics and distribution services are critical to expand the scope of regional value chains, and have helped increase the export opportunities of services sectors in some countries in recent years.\textsuperscript{16} Particularly, economies in South-East Asia, such as Indonesia, the Philippines and Thailand have recorded strong growth in commercial services between 12\% and 18\% in 2012, while China and India have both witnessed modest growth of 4\% and 8\%, respectively in 2012.\textsuperscript{17}

There is an enormous potential for remittances and tourism sector development in the region to promote inclusive economic growth and social development, providing an alternative source of foreign exchange earnings. The remittances to developing countries in Asia and the Pacific increased from $49 billion in 2000 to $265 billion in 2013, while international tourism receipts increased from $169 billion in 2004 to $320 billion in 2013.\textsuperscript{18} More importantly, the region captured almost 23\% of total global international tourist arrivals. Thus, remittances, tourism and related services have been significant in sustaining economic growth of the region, especially least


\textsuperscript{16} ESCAP developed the International Supply Chain Connectivity Index (ISCCI) measuring the overall trade facilitation performance of a country along the international supply chain. This index is based on the Trading Across Border indicators from the World Bank Doing Business Report and the Liner Shipping Connectivity Index of UNCTAD. The top five world performers (out of 180 economies) in terms of their connectivity to international supply chains are all Asia-Pacific economies, namely Singapore; Hong Kong, China; the Republic of Korea; China; and Malaysia. In general, countries from East and North-East Asia and South-East Asia have better Connectivity Index scores than those from other subregions in Asia and the Pacific. ISCCI provides some useful insights on how to improve international supply chain connectivity. (ESCAP, Asia-Pacific Trade and Investment Report 2013. Turning the Tide: Towards Inclusive Trade and Investment (United Nations publication, Sales No. E.14.II.F.2) (Bangkok, 2013). Available from www.unescap.org/tid/ti_report2013/download/aptr2013.

\textsuperscript{17} See World Trade Organization, World Trade Report 2013: Factors Shaping the Future of World Trade (Geneva, 2013).

\textsuperscript{18} For latest data and analysis on migration and remittances, the information is available from http://go.worldbank.org/092X1CHHD0. The Information on tourism is also available from the World Bank online database. (accessed 21 November 2013).
developed countries and Pacific Island developing economies during 2013. Existing research shows that remittances have not only reduced poverty, but also lessened inequality since the income share at the bottom of the distribution increases, while the income share at the top declines. This is particularly evident in low-income developing countries. A preliminary analysis by ESCAP finds a negative association between remittances (as a percentage of GDP) and income inequality (Gini index) for 24 selected economies.

The growing interlinkage between services, on the one hand, and production and marketing of merchandise goods, on the other, has become much stronger over the past years in the region. Services value added in gross export values is increasing rapidly. Therefore, apart from a removal of barriers to goods trade, it is equally critical to undertake policy steps to remove barriers to services trade, specially to enhance regional integration for shared prosperity. This could be done through sequencing of liberalization and complementary policy reforms, including in the case of foreign direct investment, particularly to enhance productive capacity.

Region buffeted by looming end of easy global money

This year has seen a preview of the possible impact on the region of the end to the era of easy global money which had been primarily driven by the quantitative easing programme of the United States. The suspicion that a winding down of the level of bond purchases by the Federal Reserve was about to be announced in September 2013 led to dramatic falls in the currency and asset markets of some economies in the region as investors repatriated their funds to the United States. Nevertheless, not all countries which had been favoured by foreign portfolio investors in the past suffered the same withdrawal of funds. Investors most penalized those economies which were perceived as having relatively weaker macroeconomic fundamentals and growth prospects. In this sense, the losses suffered by the financial markets in these countries were a symptom of their deeper structural challenges.

Investors most penalized those economies which were perceived as having relatively weaker macroeconomic fundamentals and growth prospects

During June–August 2013, the currency of India lost over 13% of its value, while those of Indonesia, Malaysia, the Philippines, Thailand and Turkey lost between 6% to 9% (see figure 3). Over this period, Turkey’s equity market index was marked down by about 25% and nearly 20% in Indonesia and Thailand (see figure 4). In August 2013 alone, stock market capitalization in seven economies in the region was $323 billion lower than in July.

In September 2013, several stock markets in emerging Asia-Pacific economies regained the index levels recorded prior to the August sell-off, although market volatility was still very high. The currencies of India, Malaysia, the Russian Federation, Thailand and Turkey also strengthened somewhat but in many cases remained weaker than their levels at end-May 2013. Despite the recent respite, the events revealed how vulnerable many economies in the region still are to external developments. In particular, they point to a fundamental policy lesson; that is, short-term capital

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20 According to ESCAP, *Asia-Pacific Trade and Investment Report 2013*, global foreign direct investment inflows have declined by 18%, from $1.65 trillion in 2011 to $1.35 trillion in 2012. The developing countries in the Asia-Pacific region account for 33% of global inflows compared to the 18% share of countries in Latin America and the Caribbean, and the 4% share of countries in Africa.
Figure 3. Exchange rate indices in selected developing Asia-Pacific economies, 2013


Note: These indices are calculated vis-à-vis the United States dollar. Lower value signifies depreciation against the United States dollar.

Figure 4. Equity markets indices in selected developing Asia-Pacific economies, 2013

flows cannot be relied upon to address long-term structural issues, such as productive capacity gaps and growing inequality, that lie at the root of rising current account deficits.

Foreign portfolio capital has been observed to trigger macroeconomic instability through a vicious cycle of events. Among countries which lost most favour with investors were those which displayed macroeconomic weakness in the form of current account deficits funded by portfolio capital. Prominent examples are India, Indonesia and Turkey. Targeted countries also tended to exhibit relatively high inflation (see figure 5), with foreign investors viewing the higher interest rates in these countries as being expected to prove deleterious to maintaining economic growth (see figure 6). Higher global oil prices seen recently were also recognized as pushing up fuel import bills in these net oil-importing countries, and widening current account deficits further.

Notably, the levels of foreign exchange reserves relied upon as a buffer in such situations raised concern in some economies when called upon. By end-August, in attempting to defend currency values the foreign reserves of India, Indonesia and Thailand dropped by between $11.5 billion and $19.3 billion from their levels at end-2012, while not managing to stave off the sharp depreciations seen in these countries (see figure 7).

The ESCAP vulnerability yardstick displays the risk faced by many economies of potentially inadequate foreign exchange reserves to adequately cover the possibility of exit of foreign funds from their financial markets (see figure 8).

The ineffectiveness of current regional mechanisms such as the Chiang Mai Initiative Multilateralization (CMIM), to assist in episodes of currency pressures was also seen once again, as at the start of the global

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**Figure 5. Consumer price inflation in selected developing Asia-Pacific economies, 2008-2013**


Note: The CPI is calculated on a year-on-year basis.
Figure 6. Policy interest rates in selected developing Asia-Pacific economies, 2008-2013


Figure 7. Foreign reserves indices in selected Asia-Pacific developing economies, 2009-2013

financial crisis. For example, in August 2013, instead of using the CMIM, Indonesia turned to Japan for a precautionary line agreement, while India tripled the size of its agreement with Japan in September 2013. Similarly, in October 2013, the Republic of Korea and Malaysia signed a three-year currency-swap agreement, of up to $4.75 billion to curb liquidity risk while also providing an impetus for bilateral trade and investment activities.

**Jobs growth and quality still show mixed progress**

With concerns about the speed of the economic growth recovery in the region, especially in major developing countries, labour market outcomes in terms of job creation and quality of jobs have been decidedly mixed in 2013. Recent ILO and national-level labour market data on 11 economies in the region, including three developed economies, indicate that seven developing economies witnessed year-on-year job growth in 2013 with varying magnitudes as compared to 2012. In 2013, the rate of job growth was highest in Malaysia (8.8%), Sri Lanka (6.9%) and Singapore (4%). In terms of total job increases, the highest increases were 1.2 million and 1.1 million in Indonesia and Malaysia, respectively. Growth in jobs was also positive in Viet Nam (912,000) and the Philippines (620,000). The new data also indicate, however, that job growth turned negative by 1.2% (466,000) in Thailand, with the largest declines in agriculture and the hotel and restaurant industry.

*Figure 8. Vulnerability yardstick as a percentage of foreign reserves in selected Asia-Pacific economies, latest available data*


Note: Vulnerability yardstick is the sum of short-term external debt, latest quarterly imports based on four-quarter moving average and estimated international portfolio investment position.
In the developed economies of the region, job expansion was less than 1% in Australia, Japan and New Zealand. Similarly, job creation in the Pacific economies was also mixed according to the latest available information.

With continuing growth uncertainties in developed economies and underperformance of major emerging economies of the region, job creation has remained slow paced. Concerns about job quality remain pervasive throughout developing Asia and the Pacific as seen from poor working conditions reflected by a majority of workers being employed as own-account or contributing family workers. For example, based on available data for recent years the share of own-account and contributing family workers in total employment was 55.6% in Indonesia (64.9% in 2000), 55.9% in Thailand (57.1% in 2000), 60.2% in Pakistan (63.6% in 2000) and 62.5% in Viet Nam (80.1% in 2000). In the Pacific economies, the figures are also mixed, such as around 39% in Fiji and 70% in Vanuatu, according to the latest available data. These own-account and contributing family workers are often informally employed with limited opportunities for regular, salaried jobs that are more productive and secure. Notably, women are more likely than men to be in these types of jobs. In Pakistan, for instance,
the share of employment as own-account and
contributing family workers was 23.4 percentage
points higher for women than for men.

The youth unemployment rate is almost three
times the adult unemployment rate in the region

In most economies overall unemployment rates
remained relatively low in 2013, around 5% or less,
but there were some marked exceptions such as
Fiji, Indonesia, the Philippines, Pakistan and Samoa
as well as Australia and New Zealand (see figure 9).

However, open unemployment rate does not reveal
the extent of decent and productive jobs deficits
in developing countries with no formal or very
rudimentary social protection measures. As the
growing workforce looks for jobs in the informal
sector, young people continue to face serious
challenges in securing decent and productive
employment. In four of nine developing economies
with recent 2013 data, the youth unemployment
rate exceeded 10%. Also, youth unemployment is of
major concern in the Pacific economies.

The youth unemployment rate was highest in Fiji
(25%), followed by Sri Lanka (20.1%), Indonesia
(18%), the Philippines (16.8%), Samoa (16%) and
Pakistan (11.2%). Among developed economies,
New Zealand and Australia were impacted recently
with the problem of high youth unemployment
rates, 15.6% and 12.6%, respectively.

In general, the youth unemployment rate is almost
three times the adult unemployment rate in the
region. In addition to inadequate availability of
decent and productive jobs, some major factors
behind this outcome are the mismatch between
education and employers’ requirements, between
curricula and labour market needs, low secondary
schooling completion rates, gender inequality and
youth aspirations. High youth unemployment,
particularly among young women, underscores
the need for policy measures in order to harness
the potential of the demographic dividend. While
countries need to reorient policies to accelerate
decent and productive job creation, they would
benefit from policy measures to improve overall
educational attainment, matching school curriculum
to project labour market needs, and access to
decent work. In this context, the expansion of
educational attainment was one of the key priority
actions highlighted by ESCAP countries during
the Sixth Asian and Pacific Population Conference
(see box 3).

Inequality hampering growth

The Survey 2013 highlighted that growing inequality
could potentially have considerable negative
impacts on shared prosperity. Inequality cannot
only constrain domestic demand growth and
hence productivity and industrial growth, but also
paradoxically can contribute to balance of payments
difficulties. As mentioned earlier, inequality is
found to correlate positively with household debt
and current account deficits, both of which can
constrain economic growth as well as contribute to
financial instability.

The cost of social and income inequality can
considerably increase due to its impact on social
cohesion and the prevention of economies realising
their full potential. The lack of opportunities arising
from inequality promotes risks of societal conflict
and jeopardizes the well-being of large segments
of the population with low incomes leading to a
reduction in healthy lives and development. A
population trapped in the vicious circle of inequality
and lack of job opportunities would constrain the
Nearly 500 representatives from 46 nations endorsed a new course of action on population and development policies at the Sixth Asian and Pacific Population Conference, held from 16 to 20 September 2013 in Bangkok. As the region looks ahead to ways to encourage sustained economic growth and reduced inequality, the Asia-Pacific Ministerial Declaration on Population and Development adopted at the Conference provides a regional framework for priority action on population and development issues, including incorporating population dynamics into national development planning.

The results of the recent review of the 20-year implementation in Asia and the Pacific of the Programme of Action of the International Conference on Population and Development considered by the Conference indicated a number of gaps and emerging issues, including reducing fertility in those countries that still have high fertility, improving education for children and youth, and reducing remaining gender inequalities. Improving access to education, particularly for girls and young women, first came to prominence on the population and development agenda with the Programme of Action, given the important effect of increasing education on the reduction of high fertility and rapid population growth, and the deleterious effect of these on economic growth.

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Box 3: Sixth Asian and Pacific Population Conference provides new way forward on population and development policies

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\[a\] For further information, see www.unescapsdd.org/appc.
size of domestic consumption and thus growth prospects.

To gauge the negative impact, the Survey 2013 discounted levels of per capita income by a factor proportional to the extent of income inequality and found that GDP per capita declined substantially for many countries with relatively high levels of Gini index. For example, GDP per capita (PPP 2005, United States dollars) for the year 2012 in Singapore declined from $53,266 to $28,071 when adjusted for income inequality. In the case of China, the decline was from $7,958 to $4,472.

Among many structural factors, income inequality and other forms of lack of opportunity in the access of goods and services emanate from shortfalls in social and economic policies at the national level. In particular, the growing divide between the rich and the poor is a result of unequal access to ownership of assets, particularly land in agrarian societies. As shown in the Survey 2013, inequality (Gini index) is negatively associated with tax-to-GDP ratios and proportions of GDP spent on social protection. That is, the lower the tax-to-GDP ratio and social protection expenditure as a percentage of GDP, the higher the value of the Gini index.

It is increasingly evident that the weakening of labour market regulations and institutions, vulnerable social protection systems, lack of quality in education systems, inadequate credit market operations, inadequate emphasis on land reform and excessive asset concentration or business conglomeration are some of the key factors influencing the widening income gaps across societies and within communities in the region. In the recently launched ESCAP-ADB-UNDP Regional MDGs Report 2012/13, the issue of containing inequality, along with the target of zero-poverty, emerged as a central concern in consultations with Asia-Pacific stakeholders.\(^{21}\)

The rising and/or persistently high level of income inequality of over 0.30 (Gini index) in major developing countries, such as China, India, Indonesia, Malaysia and Thailand, has already led to substantial internal policy discussion as to how to contain its further rise. The concern stems from the significant cost being exerted on achieving an inclusive and equitable income distribution. The issue of inequality is expected to acquire further momentum during the ongoing formulation of the sustainable development agenda for the United Nations post-2015 development framework.

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Another social challenge is the prevalence of undernourishment in the Asia-Pacific population, which affects a total of 533 million people, accounting for about 15% of the population in 2013.\(^{22}\) The region accounts for about 63% of the world’s hungry people. Undernourishment is high in a number of countries, including Bangladesh, China, India, Pakistan, the Philippines, Solomon Islands and Sri Lanka. Poverty and hunger are intertwined in a vicious cycle since undernourished people are less productive, have lower disposable incomes and consumption to conduct an active fulfilling life, and are therefore more prone to fall into the poverty trap. Another social challenge in the region is that of

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achieved gender equality, and specifically women’s economic empowerment.

OUTLOOK FOR 2014

Subpar pick-up in growth ahead

The near-term growth prospects in the region are set to improve modestly. Developing Asia and the Pacific is forecast to expand by 5.6% in 2014, up from an expected 5.2% in 2013 (see table 1). This, however, depends on the gradual recovery in developed economies, particularly an increase in growth momentum in the United States, expansion in Japan, and progression to positive growth territory of the European Union. If the positive outlook in the advanced economies does materialize, import volume growth by these economies is expected to reach a three-year high in 2014. Growth performance in developing economies is thus expected to resume some strength after a sluggish 2013. Growth is also expected to receive support from governments’ continued emphasis on domestic-led growth through greater attention to improving infrastructure and other types of social investment, as was recommended in the Survey 2013.

The expected pick-up of growth in 2014 is, however, subpar. A projected growth of 5.6% in 2014 would have been seen as deceleration had growth in 2013 remained at 6% as previously projected in the Survey 2013. Moreover, under the current projections, the period of 2012-2014 would be the first time in at least two decades that developing Asia and the Pacific grows less than 6% annually for three consecutive years. The region’s economic growth has thus shifted over an extended period to a slower pace. Moreover, this slowdown has been broad-based rather than dominated by a decelerating China.

Under the current projections, the period of 2012-2014 would be the first time in at least two decades that developing Asia and the Pacific grows less than 6% annually for three consecutive years

The economy of China is likely to continue its transition to a more moderate pace of growth. Output is projected to advance by 7.3% in 2014, lower than the rates seen in 2012-2013, due to, among other factors, a weak pick-up in industrial activity. The shift of the growth engine away from fixed investment would particularly have implications on commodity exporters in the region. In India, the pace of growth is expected to increase by 6% in 2014 but would still remain below its potential. Due to good rainfall in 2013, agricultural growth could boost GDP growth prospects and reduce inflationary pressures. Economic optimism appears fragile in 2014 and remains conditional on the progress made in unlocking supply-side constraints. As China and India together account for over half of the GDP of developing Asia and the Pacific, their growth performance would markedly influence the growth outlook in the Asia-Pacific region and beyond.

Export-oriented economies, such as Malaysia and Thailand, are expected to experience somewhat faster growth – 5% and 4.5%, respectively in 2014 – underpinned by a pick-up in manufacturing activities and global trade. The Philippines is projected to grow faster.


24 Economic growth in developing Asia-Pacific is projected to soften from 8.4% during the pre-crisis years of 2002-2007 to 5.4% during 2012-2014. The equivalent figures for the group excluding China are from 6.6% to 3.9%. Across Asia-Pacific subregions, only the Pacific islands are projected to enjoy faster growth between these two periods.
by 6.7% in 2014 and could see further acceleration due to reconstruction activities in the aftermath of Typhoon Haiyan. Furthermore, remittances will continue to serve as a stable source of support for the Philippine economy given the better outlook for receiving countries as well as the general lack of short-term volatility in remittance flows. For most other economies which are less tied to global developments, their modest inflation, generally solid employment conditions and accommodative macroeconomic policy stances would sustain consumer confidence and spending. Meanwhile, growth prospects for developing economies in the Pacific are set to strengthen on the back of expected recovery of the global economy, especially if there is growth acceleration in Australia and New Zealand. Among the Pacific economies, Papua New Guinea is expected to see growth pick-up in 2014 against the backdrop of investment in infrastructure and social sectors. In addition, Solomon Islands is projected to grow by 4% in 2014 due to robust activities in the agricultural and manufacturing sectors.
The inflation outlook is generally moderate in the region although prices remain at high levels. Headline inflation is projected at 5% in 2014, down from 5.5% in 2013 (see table 2). While global energy prices are expected to be stable in 2014, global food prices may decline amid weaker demand from developing economies and solid harvests that are building up global food stocks. The relatively muted inflation, however, masks some concerns.

The estimated food and energy price levels in 2014 are still as high as those recorded in 2008 during the global commodity price spikes. Poor and vulnerable households will be disproportionately affected as they spend a higher proportion of their income on food purchases. Another concern is that price pressures are set to stay strong in some subregions. In South and South-West Asia, supply-side bottlenecks would keep inflation at around 10% in 2014, food prices being particularly affected. This would tend to result in negative real wage growth for many low-wage workers and negative real deposit rates for pensioners and other savers.

<table>
<thead>
<tr>
<th>Country</th>
<th>2012</th>
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</table>

Developing ESCAP economies 5.3 5.1 5.5 5.0

Table 2. Rates of consumer price inflation in selected developing Asia-Pacific economies, 2012-2014 (Percentage)

Source: ESCAP projections, based on national sources.
Note: Developing ESCAP economies comprise 37 economies in the region. Calculations are based on the weighted average of GDP in United States dollars in 2010 (at 2005 prices). Forecasts are as of 5 December 2013.
The overall risks to the growth outlook for the region are to the downside. The slight improvement in the growth outlook in Asia and the Pacific is conditional, to a sizeable extent, on a smooth economic rebalancing in China, the return of some economic dynamism in India, as well as intraregional trade and investment growth. Another risk is sharp commodity price increases due to continued geopolitical risk in the Middle East or worse-than-expected weather and harvests in major food producing economies. If this were to occur, high price pressures would not only dampen household spending but also real sector activities in general due to monetary policy tightening.

**POLICY CHALLENGES**

**Renewed role for forward-looking macroeconomic policies to support inclusive growth**

The new scenario under which the region is likely to pass in 2014, the constrained growth of major regional growth centres and a possible rise in United States long-term interest rates, will make the need for productive fiscal spending by governments more pressing. Most affected would be economies in the region with open capital markets, such as Indonesia, Malaysia and Thailand. Clearly, monetary policy could play a greater role to support growth if economies reduced their dependence on short-term foreign capital. They could do this by implementing capital flow management measures (see the following section) and therefore regain independence in decision-making regarding the setting of interest rates, and also by strengthening regional policy coordination.

Even within the constrained circumstance, monetary policy can support growth. This would require careful designing of measures to enhance financial inclusion and to support growth of SMEs and the agricultural sector, which is still employing nearly 762 million people in the region. This would also require rigorous analysis of causes of inflation and the use of tools, other than policy interest rates, to manage credit growth and to address the sources of inflation without hampering growth.

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financed consumption, lower tax revenues constrain the government’s ability to pursue countercyclical policies.\textsuperscript{26}

\textbf{Higher income inequality adversely affects domestic demand and paradoxically contributes to balance-of-payments deficits}

Additionally, a number of policy considerations suggest that universal social protection is critical for inclusive growth. Universal and comprehensive social protection measures can also reduce the need for higher wage demands in order to meet the living costs of citizens and therefore can lower inflation and improve competitiveness. By helping price stability, universal social protection measures can also create space for growth-supporting expansionary macroeconomic policies.

However, substantial gains on inclusive growth will depend on the ability of governments to invest in people and planet. This may require strengthening domestic institutional mechanisms to enhance availability of funds for enabling development-oriented budget expenditure, including increased social protection and environmental investments.\textsuperscript{27}

Several countries in the region have initiated targeted policies and programmes designed to enhance social protection and to promote inclusive economic growth, resource-efficient and sustainable development, including in China, India, Indonesia, Republic of Korea, Thailand and Viet Nam. Box 4 highlights the case of Indonesia.

When fiscal policy is productive as outlined above, spending may even be financed by debt or deficits as the long-term impact on macroeconomic variables will be positive. For the purpose of development, attention should shift to where the deficit is being spent. Is it, for example, for enhancing human, physical or social capital that improves productivity, export competitiveness and hence growth? As discussed in the Survey 2013, there should be a fuller consideration of the growth effects of various kinds of government expenditure in designing fiscal policy. Thus, the emphasis should be on “functional finance” which looks at the composition of government expenditure, instead of “sound finance” which focuses on aggregate debt or fiscal deficit.

Notwithstanding the significant efforts that have been made in many countries, more domestic resources may have to be mobilized. The forthcoming Survey 2014 will thus examine how countries can foster domestic resource mobilization to strengthen development. In doing so, the Survey 2014 will address pressing concerns for governments, including, for instance, identifying policies that are needed to enhance revenue mobilization and how to address and overcome potential policy challenges.

\textbf{Increasing need for capital flows management measures}

The recent sharp downward movements in currency and asset markets have highlighted significant macroeconomic vulnerability in many open economies in the region. Falls in Asia-Pacific emerging markets have indeed been sharper than global declines, reflecting the higher initial inflows into the region and the greater sensitivity of flows to emerging markets.

\textsuperscript{26} For further discussion of other characteristics of forward-looking macroeconomic policies apart from developmental fiscal policies, such as monetary policy, exchange rate policy and management of capital flows, see ESCAP, “Developmental macroeconomics”, MPDD Policy Briefs, No.13 (Bangkok, 2013). Available from www.unescap.org/pdd/publications/me_brief/pb13.pdf.

In January 2012, the Government of Indonesia announced a major reform plan to reduce gasoline subsidies. Despite the delay in implementation due to strong opposition, the reform finally took effect in June 2013 involving an increase in the price of subsidized gasoline and diesel by 44% and 22% respectively.\(^a\) Assuming stable exchange rate and oil prices, the World Bank estimates that, in 2014, there will be fiscal savings of IDR 85.2 trillion (or 0.8% of GDP) from the increase in subsidized fuel prices. In addition to keeping the country's fiscal deficit in check, it is also expected that the reduction in fuel subsidy will help strengthen the Indonesian rupiah and improve the country's trade balance as petroleum imports decrease.

To buffer poor households from the immediate impacts of higher fuel prices and to strengthen the country’s social protection system in the long-run, the Government of Indonesia has put in place a comprehensive fuel subsidy support package, the “Kompensasi Khusus” programme, which consists of both short-term and long-term social protection measures. These policy measures consist of the following: an unconditional monthly cash transfer of IDR 150,000 ($13.20) for a duration of four months to 15.5 million poor households; an increase in the distribution of rice from 15 kilogramme to 45 kilogramme for the same 15.5 million households; and investments in community-level housing infrastructure and drinking water management systems.

Authorities also reallocated savings from subsidy reductions to increase both the extent and level of coverage for two existing social protection programmes. The level of coverage available under the Bantuan untuk Siswa Miskin (BSM) programme, which provides tuition support for poor primary and junior secondary school children, will be increased. The BSM programme will also increase the extent of coverage, almost doubling in reach from 8.7 million to 16.6 million beneficiaries. Savings have also been reallocated to the Program Keluarga Harapan (PKH), a conditional cash transfer programme for families, which will be increased from 1.5 million households to 2.4 million households by the end of 2013 and 3.2 million households by the end of 2014. By reallocating fuel subsidy savings to its long-term social programmes, Indonesia is effectively using this opportunity to both scale up and reform its emerging social assistance system.\(^b\) Finally, the Parliament allocated IDR 29.05 trillion ($3.2 billion) for this compensation package and for other social support measures in the revised 2013 budget.

The traditional approach of governments in the region in dealing with such risks is to accumulate foreign exchange reserves. This method of protection, however, is far from ideal. At the onset of the financial crisis, when currency support was required, the amount of reserves of some countries proved insufficient. In the most recent episode of capital outflows, reserves also proved to be inadequate to prevent the large falls seen in the currencies of some countries. Moreover, a large accumulation of foreign currency reserves has a social and economic opportunity cost as these reserves could have been used for addressing development challenges.\textsuperscript{28}

It is increasingly clear that more effective and less costly capital management measures are required at the national level. Capital account regulations, also known as capital controls or capital flow management, have been gaining in popularity in recent years, as recommended by ESCAP over a number of years.\textsuperscript{29} Recent capital account regulations in the region have been varied in their characteristics. Some have been market-based, such as taxes or levies on particular instruments, while others have been quantitative, such as caps or prohibitions on purchases of particular instruments. Furthermore, while most measures have been directed at capital inflows or purchases, some have also been targeted at discouraging capital outflows or sales. Such measures may be usefully extended and improved through lessons learned from recent implementation. A general guideline should be for such regulations to not be viewed as temporary but instead as a central component of long-run policies to prevent economic booms and busts.

**Regional cooperation urgent to tackle emerging impediments to growth**

The increasingly evident signs of structural impediments to inclusive growth in the region provide a clear opportunity for strengthening regional cooperation to address the development challenges. The slowdown in major economies in the region with large domestic markets indicates that home-grown challenges are holding back the potential for higher growth and development in these economies. A key underlying challenge for many of the affected economies is the inability of production to keep up with increasing demand, thus leading to inflation and the need to dampen demand as a second-best solution to control price growth. In the industrial sector, a major cause of inefficiency in production is inadequate provision of physical infrastructure, be it in terms of transport or energy or water supplies. In the agricultural sector, inefficiency of production also emanates from lack of investment in new technologies and resources for farmers over many decades, as well as inadequate attention to make progress in land reforms. For export-dependent economies, there has also been inefficiency of trade within the region, which has meant a failure to take full advantage of the relative dynamism of regional growth.

In its resolution 68/10 of 23 May 2012 on enhancing regional economic integration in Asia and the Pacific, the Commission called upon all members and associate members to further promote regional cooperation.


Box 5: ESCAP-led regional cooperation activities in 2013

At the sixty-ninth session of the Commission, Governments discussed the theme of building resilience to natural disasters and major economic crises as one of the key development priorities in the region. The ESCAP secretariat had proposed a new regional framework for resilience-building which would rebalance economic, social and environmental systems. The Commission adopted resolution 69/12 on enhancing regional cooperation for building resilience to disasters in Asia and the Pacific, this is in addition to resolution 69/11 on the implementation of the Asia-Pacific Plan of Action for Applications of Space Technology and Geographic Information Systems for Disaster Risk Reduction and Sustainable Development, 2012-2017.

In another landmark event, at the second session of the Forum of Asian Ministers of Transport, which was held in Bangkok from 4 to 8 November 2013, 14 member countries signed the Intergovernmental Agreement on Dry Ports, underscoring their pledge towards achieving the shared vision of an international integrated intermodal transport and logistics system. The agreement will create transport and trade corridors of prosperity, transforming landlocked countries into land-linked centres of development. Similarly, at the Asian and Pacific Energy Forum, which was held in Vladivostok, Russian Federation, from 27 to 30 May 2013, member States adopted two outcome documents, namely: (a) the Ministerial Declaration on Regional Cooperation for Enhanced Energy Security and the Sustainable Use of Energy in Asia and the Pacific: Shaping the Future of Sustainable Energy in Asia and the Pacific; and (b) the Plan of Action on Regional Cooperation for Enhanced Energy Security and the Sustainable Use of Energy in Asia and the Pacific, 2014-2018. This will promote regional and subregional cooperation and coordination in the area of energy security and the sustainable use of energy.

Finally, the Asia-Pacific Ministerial Dialogue: From the Millennium Development Goals to the United Nations Development Agenda beyond 2015, which was organized jointly by the Government of Thailand and ESCAP and was held in August 2013, adopted a declaration underscoring and reiterating support for South-South cooperation and triangular cooperation, and recognizing the need to continue development assistance and technical cooperation to the least developed countries, landlocked developing countries and small island developing States for increasing partnership and development cooperation.

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a ESCAP, Building Resilience to Natural Disasters and Major Economic Crises (ST/ESCAP/2655) (Bangkok, 2013).
b The intergovernmental agreement was signed by the following governments: Armenia; Cambodia; China; Indonesia; Islamic Republic of Iran; Lao People’s Democratic Republic; Mongolia; Myanmar; Nepal; Republic of Korea; Russian Federation; Tajikistan; Thailand and Viet Nam. More information is available from www.unescap.org/news/milestone-asia-pacific-agreement-signed-dry-ports.
c See E/ESCAP/APEF/3.
d For further information, see http://apmd2013.unescap.org.
economic integration and cooperation and to formulate and implement coherent policies to increase the effectiveness of existing cooperation mechanisms.\textsuperscript{30}

\textbf{The ESCAP intergovernmental mechanism will aim to foster trade, investment, economic and development cooperation among countries in Asia and the Pacific}

To support this effort, the ESCAP secretariat is emphasizing the need to substantially enhance the degree of connectivity in the region, involving, among other things, investment in physical transport, energy and information and communications technology infrastructure, trade and transport facilitation, and the strengthening of people-to-people connectivity (see box 5). Cooperation among countries in the region is critical in order to tackle common risks and vulnerabilities, such as those related to food and energy insecurity, disasters and pressures on natural resources.

In particular, the Asia-Pacific Ministerial Conference on Regional Economic Cooperation and Integration, which will be held in December 2013 under the auspices of ESCAP, will be critical. Its goals will be to reaffirm the imperatives of sustainable development, reducing poverty and inequalities, increasing the resilience of economies in the region to natural and economic disasters and the effects of climate change, sustainable management of natural resources, enhancing food and energy security, closing the digital divide, and reducing development gaps across countries to enhance social cohesion. The ESCAP intergovernmental mechanism will aim to foster trade, investment, economic and development cooperation among countries in Asia and the Pacific in order to support inclusive economic growth and to achieve wider developmental objectives.

Growth performance in developing Asia-Pacific economies is expected to rebound moderately after a sluggish 2013 but growth will remain subpar. The key economies of China, India, Indonesia and Thailand with large domestic markets have experienced moderate growth in 2013 compared to their recent strong performance. The region may continue to experience a “new normal” of lower growth compared to recent years—as highlighted in the Survey 2013.

The region will be impacted by an uncertain recovery and related policies in the developed world. Trade protectionist policies in the developed world are significantly impacting exports and GDP growth rates in the region.

Inherent macroeconomic weaknesses and structural impediments continue to affect larger economies of the region. Growing economic and social inequality, including remaining gender inequalities, are having considerable negative impacts on shared prosperity. Job creation is mixed and concerns about job quality remain pervasive.

The 2013 Year-end Update of the annual ESCAP flagship publication, Economic and Social Survey of Asia and the Pacific, considers the implications of these challenges for policymakers in the region. The key policy messages of the Update are the need for forward-looking macroeconomic policies and enhanced regional cooperation for more inclusive and sustainable development.