United Nations ESCAP/81/16

Economic and Social Council

Distr.: General
4 February 2025

Original: English

Economic and Social Commission for Asia and the Pacific

Eighty-first session
Bangkok, 21–25 April 2025
Item 5 (g) of the provisional agenda*
Review of the implementation of the 2030 Agenda for Sustainable Development in Asia and the Pacific and issues pertinent to the subsidiary structure of the Economic and Social Commission for Asia and the Pacific: macroeconomic policy, poverty reduction and financing for development

Macroeconomic prospects, challenges and policy issues for the Asia-Pacific region

Note by the secretariat

Summary

Economic growth in Asia-Pacific developing countries is projected to remain largely steady in 2025 and 2026. Lower inflation owing to declining global energy and food prices is expected to ease the cost of living and open space for a more accommodative monetary policy stance. Lower borrowing costs, in turn, could allow proactive fiscal policy measures to support household consumption and capital investments in some countries. To boost long-term economic prospects and ensure adequate job creation, countries will need to focus on boosting productivity.

While developing long-term economic strategies that promote structural transformation for sustained and inclusive economic development, policymakers cannot ignore the headwinds in the near-term macroeconomic outlook. The escalation of trade tensions attributable to additional restrictions and the continuing technological fragmentation could disrupt regional value chains, posing a risk to the region's exports and near-term economic outlook. At the same time, geopolitical tensions remain a source of uncertainty, may disrupt shipping routes and could push up global commodity prices. For many developing economies in Asia and the Pacific, the fiscal resources needed to support vulnerable people remain constrained as public debt distress levels remain high. Moreover, improvements in labour productivity have moderated in recent decades, which does not bode well for sustaining economic prospects.

In the present document, the secretariat discusses recent economic performance and highlights the near-term economic prospects and the main challenges and risks faced by macroeconomic policymakers in Asia and the Pacific. It also highlights the importance of increasing economy-wide productivity, which is necessary for sustained economic development.

* ESCAP/81/1.

Please recycle

The Economic and Social Commission for Asia and the Pacific may wish to take note of the findings contained in the present document and provide feedback and guidance to the secretariat for its forthcoming analytical work and for the planning and preparation of future technical assistance and capacity-building work.

I. Introduction

1. Asia-Pacific economies remained vibrant relative to other parts of the world in 2024, contributing about 60 per cent to global economic growth. Many countries in the region have demonstrated notable economic resilience despite having faced a series of adverse shocks in recent years. Some economies have also emerged as world leaders in technologies, equipment and products that promote environmental sustainability. Nevertheless, average economic growth among Asia-Pacific developing countries moderated in 2024 compared with 2023 and remained below the pace recorded prior to the onset of the coronavirus disease (COVID-19) pandemic. Revived merchandise exports and, to a lesser extent, consumer spending underpinned output growth. The regional average inflation rate steadily decreased in 2024 amid lower global commodity prices and reduced pressure on currency depreciation, although some countries did face persistently high inflation. After a series of shocks in recent years, especially the COVID-19 pandemic and the cost-of-living crisis, poverty has persisted and income inequality has widened as the result of an uneven employment recovery, the reduced purchasing power of many wage earners and inadequate social protection. Together with an increasingly uncertain and fragmented global economy, high sovereign debt risks in several Asia-Pacific countries are undermining the region's ability to accelerate sustained and inclusive economic growth and thus contribute to the achievement of the Sustainable Development Goals.

2. Against this background, the present document contains an overview of recent socioeconomic developments in Asia-Pacific developing economies, covering issues such as economic growth, inflation, employment, poverty, inequality and fiscal and public debt positions. It also contains an examination of the near-term economic prospects and downside risks for the region.

3. The present document includes a discussion on selected challenges to the region's economic growth and development in the medium term. These challenges include a slower pace of income convergence with developed economies, increasing difficulty in diversifying into higher value added economic sectors and a policy dilemma between pursuing traditional macroeconomic objectives, such as economic stability and growth, and fostering green economic transformation. The document contains suggested policy actions to address these challenges, namely prioritizing productivity enhancement and sectoral upgrading, embracing regional green value chains and promoting inclusive regional cooperation.

II. Recent socioeconomic developments

A. Economic growth

4. Average economic growth among Asia-Pacific developing countries moderated to 4.7 per cent in 2024 from 5.1 per cent in 2023 and 5.5 per cent during the pre-pandemic period of 2015–2019. Despite this slowdown, the region's economies remained vibrant compared with other parts of the world, contributing about 60 per cent to global economic growth in 2024.

5. Strong merchandise exports mainly drove the overall economic expansion. The export volume increased by 3.4 per cent in 2024 after a contraction of 0.9 per cent in 2023.[1] Exports to the United States of America and countries within the Asia-Pacific region (excluding China) underpinned the turnaround. In 2024, intraregional trade (excluding China) accounted for 54.5 per cent of the region's total trade, while the shares of trade with China, the European Union and the United States stood at 15.3, 11.9 and 10.5 per cent, respectively.

6. Rising demand for electronics and artificial intelligence-related semiconductors was notable, although this directly benefited only few major regional players, such as China, Malaysia, the Republic of Korea and Singapore. Services exports also registered a strong performance, with the number of tourist arrivals approaching or surpassing pre-pandemic levels in many countries, including Pacific islands with sizeable tourism sectors, such as Cook Islands, Fiji, Samoa and Solomon Islands. Similarly, growth of remittance inflows increased to 7.1 per cent in 2024 from 1.4 per cent in 2023, with much higher growth in countries with large diaspora communities, such as Pakistan and Tajikistan. Albeit to a lesser extent than exports, consumer spending also supported the region's economic growth in 2024, recording a robust performance in the first half of the year before losing some momentum in the second half.

7. The overall slower output growth was largely driven by a slowdown in the larger economies of the region. For instance, economic growth in China decelerated slightly from 5.2 per cent in 2023 to 5.0 per cent in 2024, not least because of escalating international trade tensions. And although economic growth in India remained robust at 7.1 per cent in 2024, it had come down from 8.2 per cent in 2023, attributable to a deceleration in private consumption and total capital investment growth.

8. Economic performance varied greatly across Asia-Pacific subregions in 2024. In East and North-East Asia, output growth in the Republic of Korea picked up amid robust exports of high-technology products despite sluggish household consumption and investment. In Mongolia, a strong mining sector helped drive economic growth. In contrast, the Japanese economy slowed as a result of relatively high inflation and weaker activity in the automotive sector. In South and South-West Asia, the economies of Pakistan and Sri Lanka resumed expanding in 2024 after having contracted in 2023, while higher tourism arrivals and investments in large infrastructure projects supported output growth in Bhutan, Maldives and Nepal. In contrast, the economies of Bangladesh and Türkiye decelerated amid high inflation and macroeconomic uncertainties. In North and Central Asia, while the economy of the Russian Federation grew rather strongly in 2024, by 4.0 per cent, owing to resource exports and government spending on construction and social payments, there were signs of a slowdown towards the end of the year amid higher inflation and interest rates. Economies in South-East Asia recorded stronger output growth in 2024, underpinned by robust domestic demand and solid merchandise exports and foreign direct investment inflows. In the Pacific subregion, economic growth picked up amid a continued recovery in the tourism and resources sectors and expanded seasonal worker programmes in Australia and New Zealand, which provided remittance incomes.

[1] Economic and Social Commission for Asia and the Pacific (ESCAP), "Asia-Pacific trade and investment trends 2024/2025: trade in goods and commercial services" (Bangkok, 2024).

9. As in 2023, economic growth in Asia-Pacific countries in special situations – least developed countries, landlocked developing countries and small island developing States – grew by 4.5, 4.3 and 3.6 per cent, respectively, in 2024, all below the regional average of 4.7 per cent. Output growth among least developed countries also fell short of the 7 per cent target set out in Sustainable Development Goal target 8.1. Several factors weighed down economic performance in these groups of countries. For instance, commodity-exporting landlocked developing countries faced lower demand for oil and other key primary commodities, and many least developed countries and small island developing States continued to face large debt burdens, low levels of capital investment and macroeconomic instability concerns.

B. Inflation

10. Average headline inflation in the developing economies of the Asia-Pacific region eased to 4.8 per cent in 2024 from 5.2 per cent in 2023 and 7.6 per cent in 2022. Yet the 2024 inflation rate was still higher than the average of 3.4 per cent during the pre-pandemic period of 2015–2019. The latest monthly inflation rates in more than half of the region's countries are below official targets or within target ranges. As inflation has been driven recently by supply-side factors in many parts of the region,[2] lower global commodity prices have helped to bring it down. The international food price index is currently about 20 per cent lower than it was in 2022, when global commodity prices surged because of the war in Ukraine and the related international sanctions, while oil prices fell by 2.3 per cent in 2024. The tight monetary policy stances previously adopted across the region also played a role in bringing inflation down.

11. Currency appreciation in several economies of the region also helped lower inflation. After a period of tight monetary policy that began in early 2022, the European Central Bank and the United States Federal Reserve started reducing policy interest rates in June and September 2024, respectively. As a result, interest rate differentials between developed markets and Asia-Pacific developing economies narrowed and net capital inflows into the region turned positive in 2024. This helped to soften the pressure of currency depreciation that the region had been facing in the past few years and to reduce prices of imported goods and services.

12. Following monetary easing in major developed economies and as demand weakened domestically, many central banks in the region began interest rate reductions in the second half of 2024. Starting in July, the central banks of China, Nepal, Pakistan, the Philippines, the Republic of Korea, Sri Lanka and Thailand introduced their first policy rate cuts in several years.

13. Despite an overall downward trend, some Asia-Pacific countries continue to face high inflation. In the Lao People's Democratic Republic, inflation stood at 32 per cent in 2023 and 23 per cent in 2024, partly attributable to currency depreciation amid limited foreign exchange reserves and high external debt service obligations. The kip depreciated by almost 14 per cent in 2024. In response to the high inflation, the Government facilitated the sale of common household items at discount prices and stockpiled rice. In the Islamic Republic of Iran, annual inflation ran at between 30 and 45 per cent during the period 2020–2024, with international sanctions weighing on the balance of

[2] Andrew Tsang, Catharine Kho and Megan Chong, "Changing dynamics of core inflation in ASEAN+3", analytical note, ASEAN+3 Macroeconomic Research Office, 28 February 2024.

payments and the local currency. The Government has been providing subsidies for fuel and basic food items to mitigate the impacts of high inflation.

14. Although prices of goods and services have increased at a slower pace in recent months, the cost of living has remained high since the global commodity price spikes in early 2022. For developing economies in the Asia-Pacific region, overall prices were 19 per cent higher in 2024 compared with 2021. In least developed countries, prices were almost 34 per cent higher. Even in countries with a more manageable inflation environment, temporary price increases of essential goods can have significant impacts on people's well-being. For example, in India, where malnutrition is widespread, vegetable prices surged by almost 30 per cent in June 2024 because of a heatwave. The same event also pushed up food prices and overall inflation in Bangladesh.

C. Employment, poverty and inequality

15. Largely stable overall job market conditions in recent years mask differences in employment performance across sectors. Employment growth in the region moderated slightly from 1.9 per cent in 2023 to 1.2 per cent in 2024, while the unemployment rate was unchanged from 2023 at 4.2 per cent. Yet this means that almost 88 million people remain jobless. Overall, the current unemployment rate is still 0.6 percentage points above the pre-pandemic rate. Uneven employment recovery across sectors could also widen within-country income inequality. As at mid-2024, employment in manufacturing and in accommodation and food services – sectors that employ high numbers of low-skilled workers – had surpassed their pre-pandemic levels by only 0.5 and 1.0 per cent, respectively. In the information and communications technology sector, the figure was much higher, 18.6 per cent.

16. Young people in several economies of the region are facing employment challenges. As new entrants to the job market, young people are generally more vulnerable to economic downturns and structural shocks. Across the region, the youth unemployment rate stood at 13.7 per cent in 2024, representing nearly 36 million young people. In China, a combination of economic slowdown, lingering pandemic effects and skill mismatches pushed up the youth unemployment rate, which peaked at 18.8 per cent in August 2024 before coming down to 15.7 per cent in December. In Thailand, 68 per cent of young people not in employment, education or training recently reported that they lacked the motivation to develop skills or seek a job.[3] In South and South-West Asia (excluding Türkiye), the youth unemployment rate remained high in 2024, coming in at 26.5 per cent, although this was down from a peak of 31.6 per cent in 2020. Among other objectives, these situations hamper Governments' ability to achieve Sustainable Development Goal targets 8.5 and 8.6, which are aimed at achieving employment for all, including young people, and reducing the proportion of youth not in employment, education or training.

17. Given a decreasing inflation trend, inflation-adjusted wage levels in the region increased by 2.9 per cent in 2024 compared with 1.6 per cent in 2023 and 1.4 per cent in 2022.[4] In some countries, the increase was also driven by wage hikes. For example, increases in monthly minimum wage levels were announced in Fiji, the Lao People's Democratic Republic and the Russian

[3] United Nations Children's Fund (UNICEF) and College of Population Studies, Social Research Institute, Chula Unisearch, *In-depth Research on Youth Not in Employment, Education or Training (NEET) in Thailand* (Bangkok, UNICEF, 2023).

[4] International Labour Organization, *Global Wage Report 2024–25: Is Wage Inequality Decreasing Globally?* (Geneva, 2024).

Federation in 2024, and minimum wages in Malaysia, the Philippines and Thailand are set to increase in early 2025. However, available data show that wage levels have not kept pace with inflation in some countries. In Nepal, for example, average real wages increased by 4.6 per cent during the period 2021–2023, whereas average annual inflation was 7.1 per cent. Inflation also outpaced earnings growth in India, the Lao People's Democratic Republic, Malaysia, Mongolia, Pakistan and the Philippines in 2023.

18. Despite the vibrancy of the Asia-Pacific economy relative to other parts of the world, poverty has persisted in the region. It is home to about 500 million people living in multidimensional poverty, meaning they lack access to adequate healthcare, education and basic public services.[5] In South and South-West Asia, about 10.2 per cent of the population is living in extreme monetary poverty, which is defined as living below the international poverty line of $2.15 a day.[6]

19. Progress made in recent years towards poverty eradication and other Sustainable Development Goals has been set back by adverse shocks, especially the COVID-19 pandemic and high inflation. In 2022, an additional 42 million people in the region fell into extreme poverty.[7] At the country level, according to a survey conducted in the Lao People's Democratic Republic in mid-2024, 63 per cent of low-income households needed to reduce their food consumption as a result of high inflation, and around one third of respondents reported having cut spending on either education or healthcare.[8] In the Philippines, although the poverty rate dropped from 18.1 per cent in 2021 to 15.5 per cent in 2023, unusually high inflation in 2023 prevented more people from escaping poverty.[9] Meanwhile, climate-induced shocks, such as the impacts of extreme rainfall in China in mid-2024 and of Typhoon Yagi in several South-East Asian countries in September 2024, also caused severe damage to agricultural land and outputs, leaving affected households with larger debt burdens.

20. Socioeconomic inequality is also rising. Income inequality increased in over half of Asia-Pacific developing countries between 2019 and 2022. In terms of gender disparities, less than half of working-age women in the region participate in the labour force, and the regional gender gap in labour force participation remains high, standing at 30 percentage points in 2024.[10] A large part of persistent poverty and widening inequality in the region is driven by inadequate social protection systems, with only 36 per cent of vulnerable people having any form of income security. To support poor and vulnerable people, Governments in the region have launched various measures. For example, the Government of the Philippines rolled out a livelihood programme for people who lost their jobs during the COVID-19 pandemic, the

[5] *Social Outlook for Asia and the Pacific: Protecting Our Future Today – Social Protection in Asia and the Pacific* (United Nations publication, 2024).

[6] ESCAP and others, "SDG1: no poverty" (2024). Available at www.unescap.org/sites/default/d8files/event-documents/SDG%201%20Goal%20Profile%20FINAL_040424_0.pdf.

[7] *Economic and Social Survey of Asia and the Pacific 2024: Boosting Affordable and Longer-Term Financing for Governments* (United Nations publication, 2024).

[8] World Bank, "Household welfare monitoring in the Lao PDR", 3 September 2024.

[9] Philippines, National Economic and Development Authority, "PH makes significant progress in poverty reduction, single-digit poverty rate achievable by 2028 - NEDA", 22 July 2024.

[10] ESCAP/APPC(7)/INF/3.

Government of Sri Lanka provided financial transfers to about 2 million low-income households and the Government of Thailand provided cash transfers of around $290 to eligible individuals.

D. Fiscal and public debt conditions

21. Among developing economies in the Asia-Pacific region, the average fiscal deficit-to-gross domestic product (GDP) ratio is estimated to have remained stable at 3.2 per cent in 2024, down from a peak of 5.8 per cent in 2020 but still above the average of 2.1 per cent during the pre-pandemic period of 2015–2019. Part of the fiscal deficit increase in recent years can be attributed to public spending needed to protect people's well-being from the high cost of living; public investment in infrastructure development; slower economic growth, which undermined government revenue collection; and larger sovereign debt-service burdens as a result of higher public debt and interest rate levels.

22. The average public debt-to-GDP ratio also remained stable at 53.8 per cent in 2024, but it was still 13 percentage points above the average level during the pre-pandemic period of 2015–2019. Although ensuring the productive use of borrowed funds and sound debt management is more important for long-term debt sustainability than what the public debt-to-GDP ratio may suggest, elevated debt levels did weigh on some countries of the region that are in vulnerable economic positions. For instance, out of 21 Asia-Pacific countries that have undergone a debt sustainability analysis for low-income countries by the International Monetary Fund and the World Bank, one has been deemed to be in debt distress[11] and 10 have been rated as having a high risk of debt distress,[12] many of which are small island developing States in the Pacific. More worryingly, average interest payments on public debt as a share of public revenue increased by 3.6 percentage points in 2023 from the level during the pre-pandemic period of 2015–2019. In Pakistan and Sri Lanka, such interest payments accounted for around 60 and 78 per cent of public revenue, respectively, in 2023.

23. Amid relatively high public debt levels, countries in the region have adopted measures to restore fiscal space. Many such initiatives are aimed at increasing the efficiency of public spending. For example, the Government of Malaysia shifted from blanket subsidies to targeted subsidies for fuel and social support. In Maldives, fuel and electricity subsidies were cut and direct income transfers targeting vulnerable households were rolled out. Other initiatives are aimed at generating fiscal resources through measures focused on health, social equity or environmental sustainability. For instance, the Government of Indonesia imposed higher taxes on entertainment-related sectors and e-cigarettes; the Government of the Lao People's Democratic Republic raised excise tax rates on vehicles and gaming devices; the Government of Singapore hiked its carbon tax; and the Government of the Russian Federation introduced a new progressive personal income tax regime. In addition, several Governments in the region raised tax rates, including those of Fiji and Sri Lanka, where the value added tax was raised from 15 to 18 per cent, and Viet Nam, where the corporate tax rate applicable to 122 multinational companies was increased from 5 to 15 per cent.

[11] The Lao People's Democratic Republic.

[12] Afghanistan, Kiribati, Maldives, Marshall Islands, Papua New Guinea, Samoa, Tajikistan, Tonga, Tuvalu and Vanuatu.

24. Ongoing fiscal consolidation is likely to disproportionately affect vulnerable populations. Amid increased fiscal risks and inadequate multilateral initiatives to increase the volume, duration and affordability of financing for Governments, further fiscal tightening through tax hikes and the diversion of fiscal resources away from essential public services would widen socioeconomic disparities. For example, scaling down social protection programmes would negatively affect the welfare of children, women and persons with disabilities in particular, as these populations already have low coverage rates and insufficient benefit levels.

III. Near-term macroeconomic prospects

25. Economic growth among Asia-Pacific developing economies is projected to moderate slightly in the near term, declining from an estimated 4.7 per cent in 2024 to a projected 4.4 per cent in 2025 and 4.3 per cent in 2026. While the merchandise exports of some countries should still benefit from strong global demand for electronics and semiconductors, overall external demand is likely to be constrained by relatively sluggish economic activity in major developed economies. Output growth in the United States is projected to trend down from 2.8–2.9 per cent during the period 2023–2024 to 1.9–2.1 per cent during the period 2025–2026.[13] In the European Union, a modest economic rebound is projected, with estimated output growth of 1.3–1.5 per cent during the period 2025–2026. In this context, domestic demand in individual countries is expected to drive the economic growth of the region over the next few years. Stable employment conditions and lower inflation could buoy consumer demand, which would support business investment, but the expansion of business investment could be held back by increased global economic uncertainties related to trade protectionism and geopolitical tensions. Room for fiscal support, if needed, has also shrunk amid tighter fiscal positions.

26. Near-term economic prospects vary across Asia-Pacific subregions. In East and North-East Asia, the Chinese economy, which accounts for 46 per cent of the economic output of the wider Asia-Pacific region, is projected to remain under pressure as it navigates several near-term economic challenges. The country's economic growth is projected to moderate from 5.0 per cent in 2024 to 4.5 per cent in 2025 and 4.3 per cent in 2026. In South-East Asia, the ongoing diversification of manufacturing value chains, robust global demand for high-tech goods and stronger domestic consumption are likely to contribute to a stable economic expansion. In South and South-West Asia, the Indian economy is expected to grow at a slower pace as a result of a deceleration in household consumption and capital investment growth. While this would lead to an overall slowdown in the subregion, output growth in Bhutan, Nepal and Pakistan is expected to pick up in 2025. In North and Central Asia, an economic slowdown is expected as a result of weaker prospects in the Russian Federation attributable to high interest rates and currency depreciation. In the Pacific, economic growth in small island economies is projected to rise amid continued increases in tourist arrivals and remittance inflows.

27. Headline inflation among Asia-Pacific developing economies is projected to ease further, declining from an estimated 5.1 per cent in 2024 to a projected 4.3 per cent in 2025 and 3.7 per cent in 2026. Lower global commodity prices and stronger domestic currencies are expected to help

[13] *World Economic Situation and Prospects 2025* (United Nations publication, 2025).

contain inflationary pressure. After falling 5.8 per cent in 2024, the global energy price index is projected to decrease by a further 6.2 per cent in 2025.[14]

28. The baseline macroeconomic projections are subject to at least three major factors. The first is rising trade protectionism. Globally, the number of trade-restrictive measures spiked in 2024, surpassing the number in effect at the peak of trade tensions between China and the United States during the period 2018–2020. The trade covered by the expanding stockpile of import restrictions imposed by the Group of 20 economies was estimated at $2.3 trillion in 2024, or the equivalent of 9.4 per cent of world imports.[15] Trade protectionism is intensifying further. The import tariff hikes announced by the United States and the retaliations that are likely to follow would lead to further technological decoupling and disruptions in regional value chains, thus exposing several Asia-Pacific emerging economies to economic shocks with negative spillovers to other regional peers.

29. The second factor affecting the projections is a longer-than-expected period of high interest rates globally. Despite the gradual decline in global inflation and the beginning of monetary easing in the second half of 2024, further disinflation is subject to several uncertainties. For example, higher import tariffs and stricter immigration policies being proposed in the United States are inflationary in nature. Indeed, uncertainty around the timing and magnitude of these policy changes has raised economic uncertainty and already delayed central banks' decisions to reduce interest rates in some developing countries. Meanwhile, the potential escalation of geopolitical conflicts in parts of Europe and the Middle East may again disrupt key shipping routes and global supply chains and cause fluctuations in world commodity prices, with direct implications for monetary policy stances.

30. The third factor is the performance of major economies. In China, to address relatively slower economic growth, weaker market sentiment and lower capital returns, the Government has recently implemented several policy initiatives, including state subsidies to encourage trade-ins of vehicles and various household items, as well as reductions in policy interest rates, the required reserve ratio for banks and the minimum down payment ratio for residential mortgages. While it is widely expected that additional fiscal and monetary stimulus measures will be introduced, what remains less clear is the focus, pace and magnitude of such measures. In India, the Government recently raised income tax exemption limits to boost spending by middle-class consumers, maintained large public investments in infrastructure projects and introduced fiscal support for small-scale industries. These policy measures could revive economic growth, although the spillover impacts beyond neighbouring economies may be limited given the smaller levels of trade between India and the rest of the region.

31. Economic policymakers in the region need to remain vigilant and be prepared to cope with these uncertainties. Continued efforts to enhance fiscal resources by spending smart and taxing fairly will be important, as will prudent macroeconomic management to ensure that accommodative fiscal and monetary policy support is not withdrawn prematurely. Moreover, an effective way to hedge against unforeseen external shocks is to keep supportive economic policies at the ready, for instance by preparing a pipeline of investment projects that could be supported by fiscal stimulus when needed.

[14] World Bank, *Commodity Markets Outlook: October 2024* (Washington, D.C., 2024).

[15] World Trade Organization, *Report on G20 Trade Measures* (Geneva, 2024).

32. The prospects of moderating economic growth in Asia and the Pacific and increased trade restrictions and economic uncertainty globally will have direct impacts on the region's ability to achieve the Sustainable Development Goals and implement other global commitments, including the Paris Agreement. Heightened uncertainty drives up precautionary saving by households, constrains lending by banks and delays investment decisions by firms, which altogether undermine employment and wage conditions. An extended period of high borrowing costs would aggravate fiscal risks and undermine the public provision of basic social services. More broadly, deteriorating trust in multilateralism would hold back global and regional cooperation to support countries most in need.

IV. Challenges to medium-term economic growth and development[16]

33. At least 15 Asia-Pacific developing countries, accounting for around 85 per cent of the region's population, have included specific targets for economic growth or income levels in their national development plans and strategies, alongside various development models and approaches to achieve them. At the same time, the validity of the current growth and development models used by Asia-Pacific developing countries is increasingly being tested, as the region faces various emerging challenges to sustaining economic growth and development in the medium term.

34. The first such challenge is that the pace of convergence of per capita income levels between Asia-Pacific developing economies and the world's most developed economies has decelerated. The ratio of per capita gross national income in South-East Asia relative to that in the United States reached its peak in 2013. For both North and Central Asia and South and South-West Asia, these ratios peaked in 2014.[17] This slower pace of income convergence is closely associated with a broad-based deceleration in labour productivity growth in the region since the 2007–2008 global financial crisis.

35. Several factors have contributed to the slower pace of income convergence. First, the positive impacts of capital accumulation on productivity gains and output growth have diminished as Asia-Pacific countries have become more developed. While it helped many countries in the region to progress from low-income to middle-income status, capital accumulation alone is not sufficient to allow them to escape the middle-income trap and transition to high-income status. Second, rapid population ageing in some large Asia-Pacific countries has weighed on regional productivity growth, as there tends to be less innovation in an increasingly aged workforce. Third, sizeable and persistent disparities in productivity levels across firms within the same sector point to some misallocation of labour and capital in the region. Fourth, a broad-based deceleration of global productivity growth may have exerted downward pressure on productivity growth in Asia and the Pacific.

36. The second challenge pertains to the smaller share of the production segment in global value chains and the growing difficulty in diversifying into higher value added segments. Value creation is increasingly being shifted towards the upstream end (such as headquarters services and research and

[16] This section is based on ongoing research by the secretariat to be presented in the forthcoming publication *Economic and Social Survey of Asia and the Pacific 2025*.

[17] Per capita gross national income levels in Asia-Pacific subregions are calculated as median values.

development) and the downstream end (such as logistics and marketing) of value chains, both of which are dominated by developed countries and large multinational companies. Developing countries, including those in Asia and the Pacific, remain trapped in the middle segments of these value chains, which consist of production activities with lower value added.

37. The adverse effects of such functional specialization along the value chain can already be observed in Asia-Pacific developing economies. For example, analysis by the secretariat shows that the contribution of manufacturing activity to both output growth and non-agricultural employment growth has declined since the 2007–2008 global financial crisis,[18] which coincides with a slowdown in labour productivity growth in the region. A further challenge is the region's dependence on manufacturing for its exports, as value addition in exports has largely shifted from the manufacturing sector to service sectors.[19] Going forward, the region's export-oriented manufacturing activity may face growing pressures on profits and wages if it fails to diversify into higher value added segments along global value chains.

38. However, moving up global value chains is an increasingly challenging task in the current global economic environment. Rising trade protectionism is limiting access to developed markets by developing countries. International technological competition has also intensified and expanded to involve more economic sectors. The strategic importance of emerging technologies, such as next-generation telecommunications and artificial intelligence, for both national economic competitiveness and national security suggests that further technological competition and decoupling are likely, which would undermine technology diffusion and innovation.

39. The third challenge is that of a policy dilemma between pursuing traditional macroeconomic objectives, such as economic stability and growth, and fostering green economic transformation. As a vast and populous region, Asia and the Pacific is the world's largest carbon emitter, accounting for around 60 per cent of total global carbon emissions. But even on a per capita basis, the emission levels in some Asia-Pacific developing economies are approaching those in developed countries as a result of heavy industrialization and high energy intensity. As the climate crisis escalates, there is increasing pressure on the economies of the region to accelerate climate action. At the same time, green economic transformation can be desirable from a domestic economic perspective. For instance, for countries seeking to expand domestic energy supply, prioritizing renewable energy sources can be a viable option as they have become more cost-competitive relative to fossil fuels. It would also help to avoid acquiring new power infrastructure that may become stranded assets as the energy transition moves forward. In addition, the region should be prepared for a potential proliferation of carbon taxes or green requirements on exports, such as the carbon border adjustment mechanism introduced by the European Union in 2023.

40. Asia-Pacific developing countries may encounter macroeconomic challenges, however, as they pursue green economic transformation. The cost of renewable energy may still be higher than fossil fuels in countries with large

[18] *Economic and Social Survey of Asia and the Pacific 2022: Building Forward Fairer – Economic Policies for an Inclusive Recovery and Development* (United Nations publication, 2022).

[19] Richard Baldwin and Tadashi Ito, "The smile curve: evolving sources of value added in manufacturing", *Canadian Journal of Economics,* vol. 54, No. 4 (November 2021), pp. 1842–1880.

fossil fuel reserves and mining capacity. In less developed countries with constrained fiscal space, Governments may have to choose between sustaining essential public services, such as healthcare and education, and subsidizing the energy transition to avoid higher inflation and eroded export competitiveness caused by higher domestic energy prices. The pressure to accelerate the energy transition is complicating Governments' decisions on how best to use limited public financial resources. Even where renewable energy is cost-competitive, some countries may still have to rely on imported technology, equipment and maintenance services to achieve a green transformation. This could worsen external current account balances, put downward pressure on foreign exchange reserves and increase external debt burdens, especially for countries in a vulnerable macroeconomic position.

V. Economic policies for sustained economic growth and development

41. Keeping in view the challenges highlighted in the previous section, there are at least three policy actions that economic policymakers in Asia and the Pacific should consider. The first is prioritizing productivity enhancement and sectoral upgrading. Labour productivity growth is key for sustained economic and income growth. To increase labour productivity, Governments should provide targeted education and vocational training programmes, foster technological innovation, enhance economic efficiency in resource allocation, promote economic upgrading into high value added sectors and improve the business environment. To support sectoral upgrading, industrial policies can be leveraged to address market failures and support local champions of technological progress and upgrading. Implementation of such policies, however, should be conditional on having clear objectives, time-horizons and lines of accountability.

42. The second policy action is embracing regional green value chains. Developing countries in the Asia-Pacific region are well positioned to capture opportunities presented by the fast-growing global green economy. The region has emerged as a leading supplier of renewable energy technology, lithium batteries and electric vehicles, among others, by leveraging its critical mineral endowments, domestic technological innovations and unparalleled manufacturing value chains. Stronger regional green value chains would further reinforce the region's competitiveness and resilience in these sectors, while also promoting a more equitable distribution of green economic opportunities within the region.

43. The third policy action is promoting inclusive regional cooperation. Despite a general decline in global economic cooperation and integration, recent adverse shocks and growing trade fragmentation, intraregional trade and investment have flourished in Asia and the Pacific and contributed to the region's economic resilience. This regional commitment to economic openness and cooperation offers mutual benefits to those involved. It is important for the region to strengthen its collaborative and inclusive approach to economic development as economic and technological competition intensifies among major global economies.

VI. Issues for consideration by the Commission

44. The Economic and Social Commission for Asia and the Pacific is invited to review and discuss the macroeconomic assessment and policy ideas contained in the present document and provide feedback and guidance to the

secretariat for its forthcoming analytical work and for the planning and preparation of future technical assistance and capacity-building work.

45. The Commission is encouraged to share information about country-specific experiences and initiatives in relation to these issues so that participants can learn from each other and inform their policy discussions. Members and associate members may wish to share experiences and perspectives regarding:

(a) Maintaining fiscal and monetary policy space and readiness to use them in the event of economic uncertainties;

(b) Making proactive policy interventions to promote labour productivity growth and sectoral upgrading;

(c) Promoting domestic green economic sectors and participation in regional green value chains;

(d) Sharing best practices for inclusive regional economic cooperation.