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Towards an inclusive, resilient and sustainable economic recovery from the coronavirus disease pandemic

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Note by the secretariat

Summary

The coronavirus disease (COVID-19) pandemic took a heavy toll on the socioeconomic well-being of people in Asia and the Pacific and exposed chronic development challenges in the region. The disproportionate impact on poor and vulnerable groups and the uneven access to COVID-19 vaccines have exacerbated economic inequality both within and across countries, posing a significant risk of a K-shaped economic recovery. In addition, the pandemic has revealed the region’s vulnerability to non-economic shocks and their cross-border economic spillovers. It is a reminder of the devastating economic impact that long-term and systematic development risks can have when they materialize and of the need for a green economy transformation to hedge against climate change. Moreover, the lack of fiscal means, especially in the developing countries of the region, is threatening the continuity of essential fiscal spending and investments with regard to the post-pandemic recovery and future development.

Nevertheless, the pandemic also provides a valuable opportunity to align post-pandemic recovery efforts with the principles of inclusiveness, resilience and sustainability as set forth in the 2030 Agenda for Sustainable Development. With regard to inclusiveness, member States can explore a broad mix of socioeconomic policies, such as regional cooperation in pandemic response efforts, government support for labour market recovery, public investment in productive capital accessible to the poor, economic redistribution, and policies to shield the poor from macroeconomic, sectoral and environmental disruptions and hazards. With regard to resilience, member States can benefit from an integrated approach to manage economic and non-economic shocks, informed by lessons from past crises, that serves to prioritize swift and forceful responses when crises hit. With regard to transitioning towards a green economy, three options are of central importance, namely carbon pricing, green public procurement and fiscal incentives for green private investments.

* ESCAP/CMPF/2021/L.1.
The secretariat of the Economic and Social Commission for Asia and the Pacific estimates that a “build forward better” policy package incorporating such measures as those described above can offer sizeable economic, social and environmental benefits, but significant effort would be needed to mobilize untapped fiscal and financial resources to meet the spending needs. In that regard, member States can explore options including public expenditure and taxation reforms, innovative bond instruments, debt swaps for development, emergency financing mechanisms and Sustainable Development Goal investments by public institutional investors, while simultaneously strengthening regional cooperation for debt relief and combating tax evasion.

The Committee on Macroeconomic Policy, Poverty Reduction and Financing for Development may wish to discuss the region’s existing development challenges that the COVID-19 pandemic exposed and to deliberate on the strategies required for an inclusive, resilient and sustainable recovery from the pandemic, with a view to offering feedback and guidance to enable the secretariat to provide targeted technical assistance and capacity-building.

I. Introduction

1. The coronavirus disease (COVID-19) pandemic took a heavy toll on the socioeconomic well-being of people in Asia and the Pacific and exposed chronic development challenges in the region. Its disproportionate impact on poor and vulnerable groups and the uneven access to COVID-19 vaccines have exacerbated the economic inequality problem, posing a significant risk of a K-shaped economic recovery characterized by widened inequality gaps both within and across countries. In addition, the pandemic has revealed the region’s vulnerability to non-economic shocks and further demonstrated that even those countries not directly affected by the shocks can still be deeply harmed by cross-border spillovers. It is a reminder that long-term and systematic development risks, when they materialize, can cause years of socioeconomic progress to evaporate. However, climate change, the single greatest known systematic development risk, has yet to be fully incorporated into macroeconomic policy considerations in many countries. Furthermore, public support for post-pandemic recovery in the developing countries of the Asia-Pacific region has been significantly lower than in advanced countries owing to fiscal and financial constraints. This lack of fiscal means has left little space for investments in the transformation required to attain resilient and sustainable economies. The increasing debt stress in some countries also threatens the continuity of essential fiscal spending and investments in future development.

2. Nevertheless, the pandemic also provides an opportunity to revisit economic policy priorities to better align them with the principles of inclusiveness, resilience and sustainability as set forth in the 2030 Agenda for Sustainable Development. In the present document, the case is made for a post-COVID-19 recovery that advances the transformation towards inclusive, resilient and sustainable economies, and contains potential policy options to that end.

II. Ensuring an inclusive recovery from the pandemic

3. High and rising economic inequality was a major development challenge in Asia and the Pacific even before the COVID-19 pandemic. The secretariat of the Economic and Social Commission for Asia and the Pacific (ESCAP) estimates that the region’s average income inequality, measured by the Gini coefficient, increased by more than 5 percentage points between the early 1990s and the early 2010s, with wealth concentration reaching unprecedented levels in
some places. The rise is mostly driven by significant increases in inequality in the region’s major emerging market economies and economic stagnation in some of its poorest countries.

4. Such high and persistent economic inequality not only stifles long-term economic growth by shortening the duration of growth spells, but also poses threats to overall social harmony and stability. Its incompatibility with the Sustainable Development Goals, together with the growing demand among the region’s more informed and empowered population for greater equality in economic opportunities and outcomes, deserves a central spot in economic policy considerations.

5. The COVID-19 pandemic further aggravated the inequality challenge. It has triggered a worldwide deceleration in economic convergence between developed and developing countries due to the uneven access to COVID-19 vaccines, fiscal support packages and post-pandemic adaptations such as teleworking and distance learning.

6. At the national level, the pandemic has disproportionately affected low-skilled and low-income workers, who are concentrated in contact-intensive sectors. Rural-urban and cross-border migrant workers were confronted with the dual challenge of losing their jobs and not being able to return home when transportation became unavailable or unaffordable. The vulnerability of those in informal employment was further exposed, not only because of job insecurity but also because informal workers often lacked access to the limited public support available during the pandemic. Among informal workers, women and youth were the most disadvantaged.

7. Low-skilled and low-income workers were further marginalized with regard to their ability to adapt to new job requirements, even where the digital divide was limited. For example, teleworking is only possible for 1 out of every 26 jobs in low-income countries, while the global average is 1 in 5. To make matters worse, persistent unemployment or partial employment can result in skill loss. In addition, access to distance learning is also uneven. This combination of circumstances indicates not only that income gaps will further widen in the short term but also that new inequalities of opportunity will arise and social mobility will decline in the long term.

8. The combined effect of economic recession and widening inequality is estimated to have already pushed 89 million people in Asia-Pacific developing countries back into extreme poverty as of 2020 year end, as measured by the $1.90 per day threshold. The figure more than doubles if measured by the higher poverty thresholds of $3.20 or $5.50 per day. Given the new waves of COVID-19 outbreaks in recent months and an outlook of prolonged economic difficulties in parts of the region, such increases in poverty may prove persistent and hard to reverse.

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1 Inequality in Asia and the Pacific in the Era of the 2030 Agenda for Sustainable Development (United Nations publication, 2018).
9. Therefore, it is paramount that Asia-Pacific policymakers take deliberate and concerted policy measures to ensure that the post-pandemic recovery is inclusive, for several reasons. First, a more synchronized recovery across countries, especially in vaccination and pandemic control, serves everyone’s interest with regard to resuming normal economic activities. Second, an inclusive economic recovery can better support the rebound in aggregate demand, as poorer households have much greater marginal propensity to consume. Third, an inclusive economic recovery would help member States to hedge against the risk of post-pandemic social unrest, given the positive relationship between high inequality and social unrest. If such a risk materializes, it could erase much of the economic gains achieved during the recovery phase and inflict more permanent damage on long-term economic development prospects.

10. To this end, a broad mix of well-coordinated socioeconomic policies would be needed. First, regional cooperation on the health front against COVID-19 should be prioritized. Together, three COVID-19 vaccine developers of the region, namely China, India and the Russian Federation, possess 7 of the 11 COVID-19 vaccines that had been approved as of early 2021 and have built up significant vaccine production capacities. Decent domestic progress in COVID-19 vaccination efforts in these three countries would create much greater space for them to contribute to multilateral and bilateral vaccine cooperation programmes. Such cooperation would be vital to a sustained economic recovery of the highly integrated Asia-Pacific region.

11. Second, government support for labour market recovery needs to be sustained and strengthened. Approximately 70 per cent of member States implemented temporary employment protection policies in 2020 in response to the pandemic, which included the following measures: wage subsidies; public works schemes; loans or cash allowances for employers to pay salaries; reduced or suspended social security tax burdens; and financial assistance for employers on the condition that employment relations were maintained. However, the duration of support and the level of spending have been much more limited in low- and lower-middle-income economies compared with rich economies, and the overall job-retention benefits of the policies are likely to be hampered a result.

12. The slow employment recovery in places where stringent lockdowns have been lifted suggests that it takes time for severed employment ties to be restored and new ones to be established. Thus, the earlier the extended or new government support for employment or re-employment is deployed, the smoother the recovery. In addition to fiscal incentives for private hiring, public measures should be put in place to facilitate the job search and the reskilling of workers, especially in view of the upcoming disruptions caused by the accelerated digitalization of the economy.

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8 Ibid. For instance, for 13 out of 15 low- and lower-middle-income economies for which data are available, the implementation of labour protection lasted less than three months, compared with more than six months in most high-income economies.
13. Given the job shortages, the large informal sector presence and a general lack of unionized labour in most Asia-Pacific developing countries, workers will be at a significant disadvantage in employment negotiations in the early phase of the post-pandemic recovery. The pressure may continue to disproportionately fall on vulnerable groups, such as informal or migrant workers, youth and women. Governments in many Asia-Pacific developing countries made an effort to target their employment protection policies to help the vulnerable groups during the pandemic, but most assistance still only covered formal sector or registered employees while leaving out informal or self-employed workers. Additional employment support for the vulnerable groups will be needed in the post-pandemic recovery phase. In particular, the share of gender-sensitive measures should be substantially increased, considering that women are far more exposed to informal employment and job discrimination and shoulder far more of the burden of family obligations.

14. Third, public investment in productive capital, including in people, and deliberate efforts to ensure that such public investments benefit the people equally, if not progressively, should be stepped up. The evaluation of public expenditures should not stop at aggregate spending figures but also include an examination of the expenditures’ structure and distributional implications. For instance, education and infrastructure spending in poor rural regions should not be crowded out by spending in rich urban districts, and access to basic public services needs to be equalized as much as possible. Only adequate public investments in the poor and fairer access to infrastructure and public services can safeguard the equality of economic opportunities in the post-pandemic recovery.

15. Fourth, economic redistribution through progressive taxation, targeted fiscal transfers and broad-based social protection will remain indispensable for an inclusive economic recovery. The use of digital technology and strengthened efforts in data collection and the production of statistics can enable better-targeted, more-transparent and more-accountable fiscal transfers, taxation and public service delivery in many Asia-Pacific developing countries. Equipped with technology and data, governments will have a better chance to address the undesirable inequality side effect associated with market mechanisms and provide social protection in a more cost-efficient manner, for example by improving beneficiary identification and reducing leakages.

16. Fifth, the macroeconomic aspects of the evolution of inequality need to be taken into consideration in the design of various policy measures. Macroeconomic instability, including prolonged periods of high and volatile inflation, tends to lead to increases in inequality. Monetary and financial policies can affect long-term capital returns and, thus, wealth accumulation. In developing countries, financialization of the economy tends to result in higher

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10 The employment protection measures adopted in these countries include concentrating support in the garment and tourism sectors which provide the bulk of employment for women (Bangladesh, Cambodia and Samoa), prioritizing micro-, small and medium-sized enterprises (Maldives, Philippines and Thailand) and setting a maximum threshold of beneficiary wage levels in cash/financial support programmes (India, Indonesia, Malaysia and Thailand). See ILO, “COVID-19 and employment protection policies: a quantitative analysis of the Asia-Pacific region”.

11 Financialization in this context refers to the increasing importance of finance and financial markets and institutions in the workings of the economy. In developing countries, rapid financialization of the economy affects household income structure and wealth concentration, driving up inequality. This inequality-enhancing effect can be greater still if the financialization of the economy comes before the completion of its structural transformation towards productive sectors such as industry.
inequality as well. The economic structural transformations involved in transitioning from agriculture to industries and services and to more innovative and technology-driven sectors have profound implications for long-term inequality dynamics, as the associated short-term economic disruptions may disproportionately affect vulnerable workers and lead to potentially temporary but acute inequality surges. Digitalization and automation, two pre-existing macroeconomic trends accelerated by the pandemic, are of particular concern.

17. Lastly, urgent and focused policy efforts to protect the poor and disadvantaged from disproportionate impact of environmental hazards will also be needed. Investments in environmental safeguards and climate actions are by nature inclusive, given their vast positive spillovers in favour of the long-term economic well-being of the poor. Hence, synergies between inclusive and green economies should be pursued in the post-pandemic recovery strategy.

III. Building economic resilience to future shocks

18. In light of the COVID-19 pandemic, building resilience to shocks has become a top policy priority. Shocks leave behind long-term scars, including social and environmental damage. Moreover, a rebound from crises should not be mistaken for recovery, as income levels could remain permanently lower than the pre-crisis trend. In the past, the mitigation of setbacks, or building resilience, did not receive as much policy attention as the acceleration of growth. The significant socioeconomic costs of COVID-19, however, have led to a shift in perspectives. For Asia-Pacific developing countries, ESCAP estimates that 89 million people may have been pushed back into extreme poverty and that the cumulative output loss for the period 2020–2022 will be close to $2.6 trillion.\(^ {12}\) For some countries, it will likely be years before pre-crisis income levels are recovered.

19. In fact, the Asia-Pacific region is no stranger to shocks with deep and persistent impacts. In an analysis of 450 major adverse events in the region since the 1960s, ESCAP determined that following a financial crisis, investment tended to collapse by nearly 20 per cent in the first year and fail to return to pre-crisis levels even after five years.\(^ {13}\) Similarly, the unemployment rate and income inequality increased notably following the pandemics associated with severe acute respiratory syndrome; haemagglutinin-neuraminidase, a subtype of orthomyxovirus that causes influenza A (H1N1), which infects birds, pigs and humans; and Middle East respiratory syndrome. The increases were possibly due to uncertainty and reallocation effects, as well as unequal access to health care. Environmental performance, as measured by a composite index, also deteriorated from shocks; natural disasters generate waste and pollution, while economic recessions divert resources away from green investments. Unless they are well managed, adverse shocks could reverse hard-won gains across the three dimensions of sustainable development.

20. Efforts should be made, therefore, to determine how Asia-Pacific countries can enhance resilience against future shocks. According to ESCAP research,\(^ {14}\) policy choices, such as a swift and strong response, health and social investments, quality of infrastructure and economic diversification, matter for resilience against shocks. It is as important to reduce setbacks by investing in
resilience as it is to grow faster. With that overarching lesson in mind, three policy lessons are worth highlighting.

21. First, Governments that responded swiftly and aggressively through countercyclical fiscal and monetary measures were more successful in securing recovery. This lesson is confirmed by previous studies. For instance, whereas fiscal support helped countries to recover faster from banking crises, the fiscal austerity imposed following the 2008 global financial and economic crisis increased long-term unemployment and inequality. Similarly, the impacts of pre-COVID-19 twenty-first century pandemics on gross domestic product (GDP) and inequality were felt less in countries with strong fiscal support. At the same time, monetary policy and macroprudential measures can mitigate shocks, and so can external buffers such as adequate official foreign exchange reserves and flexible exchange rate regimes.

22. Second, Governments could learn from previous crises and adopt preventive measures that reduce the likelihood of a crisis and mitigate losses when a crisis occurs. For instance, the development of local currency bond markets after the 1997 Asian financial crisis helped Asian countries to cope better with the 2008 global financial crisis. Similarly, with regard to natural disasters, such preventive measures as the establishment of early warning systems, climate-resilient infrastructure and insurance mechanisms could reduce human and economic losses. According to ESCAP research, pre-crisis vulnerabilities can amplify shocks and make recovery more difficult. When faced with trade shocks and pandemics, countries with low health and social protection expenditures and widespread vulnerable employment suffered larger setbacks in GDP, poverty, inequality and human capital. By the same token, natural disasters had a more devastating impact on countries with low-quality infrastructure and less diversified economies. Therefore, investing in people and addressing development gaps will be important for building resilience.

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21 Economic and Social Survey of Asia and the Pacific 2021.
23. Third, countries could benefit from an integrated rather than siloed approach to managing economic and non-economic shocks. The COVID-19 pandemic is a reminder that non-economic shocks, such as public health emergencies and climate-related disasters, can cause large economic losses and social and environmental damages. Policy responses to such cross-cutting shocks require effective government-wide coordination. A siloed approach will be less efficient and achieve only partial solutions. Governments could consider putting in place certain institutional arrangements as they prepare for future shocks. For instance, dedicated committees consisting of policymakers and independent experts could be established to identify major risks that call for a government-wide response and provide recommendations for the consideration of relevant ministries. Such a multirisk framework has been adopted in Singapore, for example.

IV. Supporting the transition towards a green economy

24. In addition to building resilience and ensuring an inclusive economic recovery, it is also important to address environmental degradation and introduce policy measures that facilitate a transition towards a low-carbon, climate-resilient green economy. Green transformation, including the mitigation of future environmental disasters and hedging against long-term climate risks, has the potential to increase future economic growth by increasing resilience and preserving development gains. As a major component of the new economy, the green economy can create clean and well-paid jobs by hosting numerous sunrise sectors, such as renewable energy, smart urban management and sustainable agriculture. Some of the regional pioneers in green industries have already taken the opportunity to seek synergies between their post-pandemic economic recovery plans and their climate commitments and environmental ambitions.

25. Fiscal policies can play a critical role in this regard in Asia and the Pacific. Overall, the region has either regressed or made limited progress on all the environmental Sustainable Development Goals. Indeed, China, India and the Russian Federation are among the world’s top carbon emitters. There is considerable room for a greener regional response to the COVID-19 pandemic, as funds committed to fossil fuels constitute most of the public spending on energy in several countries. There are various fiscal policy options available to governments in the Asia-Pacific region to achieve a green recovery and sustainable development. Three such options are highlighted below, namely carbon pricing, green public procurement and fiscal incentives for green private investments.

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24 See www.energypolicytracker.org.
A. Carbon pricing

26. The two most common approaches for carbon pricing are carbon taxes and emissions trading systems.\(^{25}\) Currently, carbon taxes have been introduced in Japan and Singapore, while emissions trading systems are in place in China, Japan, New Zealand and the Republic of Korea. As these instruments entail different advantages and implementation challenges, the choice of instrument depends on national context. General concerns regarding carbon pricing schemes, including higher inflation and weakened economic competitiveness, have been the subject of political lobbying by various interest groups.

27. An important fiscal policy option to help to secure public buy-in is financial compensation for affected households and economic sectors, in the form of either a lump-sum rebate, income tax credits or social welfare benefits. This option would also address distributional implications, as poorer households are disproportionally affected by higher energy prices. A recent IMF study on selected Asia-Pacific countries shows that identifying groups affected by carbon taxes is feasible and that fiscal space would still improve after such compensations were made.\(^{26}\) Another method of securing public buy-in is to clearly communicate with the public about the purpose that the remainder of the carbon tax revenue will serve, such as to incentivize green technologies and innovations.

B. Green public procurement

28. Green public procurement refers to government purchases of goods and services that are considered environmentally friendly, such as electric vehicles and eco-friendly accommodations. While many member States encourage such practices, only an approximate dozen of them have public procurement laws that contain regulation clauses regarding sustainability.\(^{27}\) As public procurement accounts for a sizeable 13 per cent of GDP, approximately, in the world’s developing countries, and more than 20 per cent of GDP in Bhutan, Kiribati, the Philippines and Turkey in 2018,\(^{28}\) the potential of green public procurement to drive responsible production and consumption and encourage green innovations is significant.

\(^{25}\) In emissions trading systems, a cap is imposed on the total level of carbon emissions, and industries/companies with low emissions are allowed to sell their extra allowance to large carbon emitters. Carbon taxes, meanwhile, are certain tax rates applied to carbon emissions. In effect, while emissions trading systems serve to set the carbon emissions cap and let market participants determine carbon prices, a carbon tax serves to specify the carbon price and let the amount of reductions in carbon emissions be determined by the market.

\(^{26}\) IMF, Fiscal Policies to Address Climate Change in Asia and the Pacific (Washington, D.C., 2021). The finding of the IMF study is in line with the Economic and Social Survey of Asia and the Pacific 2021, which shows that the public debt-to-GDP ratio in Asia and the Pacific would decrease after implementing a policy package that includes the introduction of carbon taxes, cancellation of fuel subsidies, and additional public spending on energy access and efficiency, climate-resilient infrastructure and biodiversity conservation.

\(^{27}\) According to the Global Public Procurement Database of the World Bank, these member States include Bhutan, Fiji, India, Indonesia, Mongolia, Nepal, the Philippines and Tajikistan. Several other member States have national policy frameworks on green public procurement.

\(^{28}\) Erica Bosio and Simeon Djankov, “How large is public procurement?”, World Bank Blogs, 5 February 2020.
29. Some of the main challenges in implementing green public procurement include higher initial prices of green products and services, lack of established green criteria and procurement tools, and limited understanding of green criteria among government officials. To overcome these barriers, Governments should assess market potential, introduce transparent national procurement frameworks and green criteria, provide more technical trainings and adopt the whole-life costing analysis that takes into account the lower operating costs of green products and services. Good practices employed in China, India and the Republic of Korea can provide policy lessons for regional peers.29

C. Fiscal incentives for green private investments

30. In addition to using public procurement as a tool in the transition towards the green economy, governments also have at their disposal fiscal incentives to promote green investment by the private sector. Examples of these incentives include reduced or zero corporate income tax rates; exemptions from indirect taxes such as import duties; investment allowances and tax credits; and accelerated depreciation of capital goods. In this regard, however, it is important to avoid incentivizing activities that would have been carried out regardless and avoid guiding markets to adopt less-than-optimal green technologies.

31. Asia-Pacific Governments have adopted a wide range of fiscal incentives to encourage green private investments. For example, to promote renewable energy, the Government of Thailand waives corporate income tax payments for the first three to eight years of operation and exempts new machinery for eligible waste-to-energy and bioplastics projects from import duties. Similarly, the Government of Viet Nam offers reduced corporate tax rates for a period of up to 30 years and waives value added tax payments on investment equipment for renewable projects.30 Meanwhile, for green activities carried out by non-environmental companies, the Government of Australia provides rebates for the installation of renewable energy water pump systems; the Government of China grants tax credits for investments in energy conservation equipment; and the Government of India offers a tax deduction for profits derived from biotechnology.31 Lastly, the Government of Japan allows special depreciation for eligible recycling facilities.

V. Policy scenarios to build forward better

32. To build forward better from the COVID-19 pandemic, member States should implement coherent policy packages that enhance their ability to withstand future shocks and facilitate a more inclusive and greener form of development. In this regard, ESCAP has proposed and analysed an illustrative policy package aimed at ensuring access to social services, closing the digital divide and strengthening climate and clean energy actions.32 This “build forward better” package comprises a wide range of policy actions, including increases in public and private spending on health-care services, social protection, education, information and communications technology, energy access and efficiency, climate-resilient infrastructure and biodiversity preservation, as well as the introduction of a carbon tax and the elimination of fuel price subsidies.

32 Economic and Social Survey of Asia and the Pacific 2021.
33. Such a policy package is estimated to offer sizeable economic, social and environmental benefits. The quantitative analysis of the package suggests that it could reduce the number of poor people by almost 180 million, cut carbon emissions by approximately 30 per cent and boost the potential output level by nearly 12 per cent relative to the baseline scenario in the long run. Income inequality is also expected to decrease, while air quality should improve notably. The projection of these significant benefits is based on the assumption that Governments increase spending levels to match the additional investment needed to achieve the Sustainable Development Goals by 2030. In contrast to those benefits, in an alternative spending scenario in which the magnitude of the increases in spending is based on each country’s past trend of financial flows, the estimated benefits would be much smaller. For example, the poverty reduction impact in that scenario is estimated at only 55 million people.

34. Given the large fiscal resources needed to finance the build forward better package and combat the pandemic, public debt sustainability could be at risk in many Asia-Pacific economies, especially in South and South-West Asia and least developed countries. For Asia-Pacific developing countries overall, the government debt-to-GDP ratio is projected to rise sharply, from 51 per cent of GDP in 2019 to approximately 74 per cent of GDP by 2030. During the same period, the ratio in the least developed countries could surge from 35 per cent of GDP to 90 per cent of GDP. The analysis also suggests that slower-than-expected economic growth, which is likely to occur as economies tentatively recover from the pandemic, would exert much more pressure on public debt levels, especially in small island developing States.

35. As member States seek to build forward better, they need to step up efforts to explore untapped financial resources to meet large fiscal needs and maintain public debt sustainability. Less developed countries in the region would benefit from greater technical and financial support from multilateral development partners and closer regional cooperation.

VI. Securing the fiscal means for recovery: options and actions

36. Substantial fiscal and financial resources are needed to implement the mix of policies that can help governments to achieve an inclusive, resilient and sustainable economic recovery from COVID-19, as discussed in the previous section, and resume the march towards the Sustainable Development Goals. In response to the pandemic, governments around the world have already spent trillions of dollars on emergency health response efforts and support for households and firms. It is unclear whether the necessary fiscal space to continue such support can be generated in developing countries without bringing about adverse implications for fiscal and debt sustainability.

37. Despite shrinking fiscal space, member States have responded in an unprecedented manner to the pandemic. Among the Asia-Pacific developing countries, the average fiscal deficit is estimated to have grown, from 1.5 per cent of GDP in 2019 to 6.8 per cent in 2020, followed by a slight decline to 5.6 per cent in 2021. It is expected to rise considerably in the least developed countries, landlocked developing countries and small island developing States. Increased deficit financing, together with the economic slowdown, will increase debt-to-GDP ratios. Among the Asia-Pacific developing countries, the ratio is projected to rise from 41 per cent in 2019 to 47 per cent in 2020 and 49 per cent in 2021.

Economic and Social Survey of Asia and the Pacific 2019: Ambitions beyond Growth (United Nations publication, 2019).
38. Nonetheless, Governments should avoid premature fiscal consolidation, as it may delay economic recovery and contribute to higher long-term debt ratios. Instead, they may create additional fiscal space through several domestic measures, with support at the multilateral level.

A. Public expenditure and tax reforms

39. Governments can create more fiscal space by curbing and reorienting non-development expenditures, notably on defence. Some member States are among the world’s highest defence spenders, allocating far more to defence than they do to health and education. According to the Stockholm International Peace Research Institute, military spending in 2019 stood at a record high of $1.92 trillion, of which Asia and Oceania accounted for 27 per cent. In some Asia-Pacific countries, defence accounts for more than 10 per cent of total public expenditure. In fact, expenditure on defence is often greater than expenditure on health and education combined.

40. Governments can also free up more resources for investments oriented towards the Sustainable Development Goals by removing subsidies that are not targeted or necessary, particularly those on fossil fuels, which in 2018 amounted to $240 billion a year. By removing fossil fuel subsidies, some Governments could fully or largely finance their stimulus packages. As discussed above, Governments can also consider introducing carbon taxes. A moderate carbon tax of $35 per ton of carbon dioxide could provide revenues equivalent to 2 to 3 percentage points of GDP.

41. In addition to redirecting expenditure, governments can also increase fiscal space by using more equitable forms of taxation. To do so would entail moving away from indirect taxes, such as sales tax on goods, and towards direct taxation on income, which can be more progressive, as those with higher incomes can pay at higher rates. The richest citizens can also contribute more through taxes on wealth and property. There is a general bias in the region towards indirect taxes as opposed to direct taxes. Direct taxes account for 38 per cent of the total tax revenue in the region, compared with 56 per cent in OECD countries.

42. Apart from raising and redirecting funds, Governments can also increase their resources by improving the efficiency of spending. They can do so through effective national public debt management, including through independent debt management offices, strong fiscal-monetary policy coordination mechanisms and transparent and accurate debt reporting.

B. Innovative bond instruments

43. Governments can also raise more resources through innovative financing instruments. Instruments such as offshore bonds and diaspora bonds are potentially low-hanging fruit that can leverage economic opportunities in many Asia-Pacific economies. For example, during the period 2013–2020, there were a total of 43 issuances of baht-denominated bonds in Thailand by the Government of the Lao People’s Democratic Republic and other entities.

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35 Economic and Social Survey of Asia and the Pacific 2020: Towards Sustainable Economies (United Nations publication, 2020).

44. In the Asia-Pacific region, there has also been steady growth in the green bond market, where the proceeds are used to finance projects and assets that are 100 per cent green. In August 2020, as part of a COVID-19 recovery package, the Government of Thailand issued its first sovereign sustainability bonds for approximately $1 billion. Similarly, in September, the Government of Bhutan issued its first sovereign bonds to support its COVID-19 response.37

45. International investors can be encouraged to invest in bonds, issued by Governments of developing countries in the region, that have been independently verified as being directed towards investments in the Sustainable Development Goals. Bonds from developing countries that are not as attractive to such investors can be supported by partial guarantees from multilateral financial institutions, which can use a mix of green, social or sustainable bonds to create funds that are aligned with the Sustainable Development Goals.

C. Debt swaps for development

46. There is scope to engage in bilateral and multilateral debt swaps for development. Debt swaps for development offer benefits beyond reducing debt obligations and improving debt sustainability. Compared with other debt reduction modalities, swaps tend to have more direct benefits for sustainable development. In the past, such swap agreements have been used to support development areas such as health care, education and environmental protection. Other benefits of debt swaps include the reduced exposure of debtor countries to exchange rate risks, the potential to attract co-financing from other development partners and the increased capacity of local organizations that implement the projects. Several Asia-Pacific economies have engaged in debt swaps for development, both as creditors and debtors.

47. Recent shifts in the financial landscape could foster the use of these swaps. Unlike in the first wave of debt swaps, in which developed economies played a leading role, some Asia-Pacific economies have emerged as key bilateral creditors. Another important shift in the financial landscape is the emergence of sustainability-oriented financial institutions and investors. For emerging Asia-Pacific economies with much of their external public debt owed to commercial creditors, these financial institutions and investors can help to promote the use of swap agreements, both as creditors and donors or third parties.

D. Emergency financing mechanisms

48. To better handle future emergency situations, member States need to have a mix of financing modalities capable of addressing catastrophe risks. Several Asia-Pacific Governments have already established national and subregional emergency funds to cope with shocks. For natural disasters, there are dedicated national reserve funds in Fiji, Myanmar, Pakistan, Solomon Islands, Tonga and Tuvalu. To combat the pandemic, two emergency funds have been introduced at the subregional level: the South Asian Association for Regional Cooperation (SAARC) introduced the SAARC COVID-19 Emergency Fund, in March 2020, and the Association of Southeast Asian Nations introduced the COVID-19 Response Fund.

49. In the short term, an effective financing mechanism can provide quicker, larger financial assistance during emergency situations, when the speed and scale of spending are critical to limiting the devastating impacts of shocks. In the longer term, an effective financing mechanism can also help countries to reduce contingent fiscal liabilities and post-event budgetary disruptions.

E. Sustainable Development Goal investments by public institutional investors

50. There is great potential to increase sustainable investments in the Asia-Pacific region by public institutional investors. The assets of the region’s pension funds and sovereign wealth funds are very large, valued at approximately $7.6 trillion in 2019. Institutional investors have also demonstrated keen interest in contributing to the achievement of the Sustainable Development Goals. In a survey of 175 Asia-Pacific institutional investors, the share of respondents who did not believe in sustainable investments fell from 23 per cent in 2017 to only 10 per cent in 2019.38

51. Such investments could be increased by relaxing certain national restrictions that limit the investment of domestic pension funds and sovereign wealth funds. For example, the overseas investment of only 1 per cent of assets managed by the pension funds of India would amount to 1.5 times the foreign aid that neighbouring country Nepal received in 2018. Adjustments in the investment policies of sovereign wealth funds could also mobilize additional financial resources for sustainable development by allowing larger investments, with due careful review, in countries and financial instruments with higher risks.

52. Furthermore, Asia-Pacific public institutional investors should step up the use of more-active environmental, social and governance strategies. A revision in corporate investment guidelines is one way to facilitate such a shift. For instance, the Government Pension Fund of Thailand introduced new guidelines in 2019 that included environmental, social and governance criteria across all investments.39 Another factor in stepping up such strategies is ensuring the solid technical capacity of investment teams that is needed to prepare complex investment analyses, such as quantitative investment models that feature environmental, social and governance scores. Financial market regulators can also play an important role. They should seek to ensure common environmental, social and governance definitions and standards and provide incentives for, or legally require, environmental, social and governance reporting by firms.

F. Regional cooperation for debt relief and combating tax evasion

53. Many poor countries have less capacity to respond to the pandemic or support sustainable recovery owing to already high levels of debt. The Secretary-General has argued for global action on debt and solidarity, which should involve debt write-downs in the poorest and most vulnerable countries.40 To support this effort, the Governments of less developed countries in Asia and the Pacific should participate more actively in debt negotiations with official and

38 Schroders, “Institutional investor study 2019: geopolitics and investor expectations” (Singapore, 2019).
multilateral creditors, while emerging economies should focus their efforts on dialogues with commercial creditors.

54. Debt relief could be achieved in two phases. The first phase should be to provide targeted debt relief to address solvency concerns. Depending on national circumstances, the international community could address the problem of unsustainable debts through debt cancellations or write-downs, debt swaps for the Sustainable Development Goals, or debt buy-backs, to be financed either bilaterally or multilaterally. In this regard, in October 2020, the Group of 20 announced the Common Framework for Debt Treatments beyond the Debt Service Suspension Initiative. While the Initiative is helpful, it is not sufficient; it excludes many affected countries that do not qualify as low-income, making them ineligible for assistance. The second phase should involve fundamentally changing the international debt architecture to prevent defaults leading to prolonged financial and economic crises. To address future debt crises, there are proposals to set up a sovereign debt forum for early engagement among diverse creditors, debtors and other stakeholders. As open and inclusive platforms that are acting as neither debtor nor creditor, the regional commissions such as ESCAP could support discussions between member States to establish a regional sovereign debt forum in support of such global efforts.

55. Governments also need to cooperate to combat tax evasion and harmful tax competition and to eliminate legal but harmful tax practices. At present, corporations aiming to reduce or avoid taxation can exploit gaps created by international tax rules and differences in domestic tax rules to shift their profits to a lower-tax jurisdiction, in a practice referred to as base erosion and profit shifting. Some member States have taken steps to stop this practice by taxing not just profits but also sales. A goal worthy of consideration is that developing countries commit all additional flows arising from such taxation of multinational enterprises to finance the Sustainable Development Goals.

VII. Issues for consideration by the Committee

56. With only eight years left to deliver on the 2030 Agenda, it is evident that a successful pursuit of the Sustainable Development Goals within existing fiscal and financial constraints hinges upon policies and financing strategies that take account of synergies between economic, social and environmental goals. The COVID-19 pandemic has provided an opportunity to think afresh.

57. In this vein, the Committee on Macroeconomic Policy, Poverty Reduction and Financing for Development may wish to discuss the region’s existing development challenges that the COVID-19 pandemic exposed and to deliberate on the strategies required for an inclusive, resilient and sustainable recovery in the aftermath of the pandemic. Securing the necessary fiscal means to support investments in inclusiveness, resilience and environmental sustainability are one of the main and urgent tasks ahead in that regard.

58. On the basis of the issues highlighted in the present document, potential questions for discussion by the Committee could include the following:

(a) What policy lessons can be learned from the region’s response so far to the COVID-19 pandemic, in terms of mitigating the development damages and supporting an inclusive, resilient and sustainable recovery?

(b) How can member States address the fiscal constraints that are impeding post-pandemic recovery and use the available fiscal levers to catalyse inclusive, resilient and sustainable development?
(c) How can the Committee and the secretariat have more regular and substantive communication on economic policies for inclusive, resilient and sustainable development, and what specific mechanisms might be explored?

59. Considering the long-term nature of relevant policies and reforms, the Committee may also wish to explore potential mechanisms that can facilitate more regular and substantive communication between itself and the secretariat, and relevant government ministries, in particular ministries of finance, to promote the exchange of policy ideas, better guide the secretariat’s work and support policy initiatives in member States.