Risks and Policy Priorities for Inclusive Economic Recovery in East and Northeast Asia

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Building Forward Fairer

ECONOMIC AND SOCIAL SURVEY OF ASIA AND THE PACIFIC - 2022
A very well-done survey that contains a set of useful information as well as some challenging arguments

- Very useful information such as
  - Favorable impact of education, health and social protection spending in reducing income inequality
  - Importance of pre-distribution (or market) income versus redistribution income in measuring income inequality
  - A new look at the Kuznets curve
  - Impact of Russia and Ukraine’s economy on Asia-Pacific economies

- Challenging arguments on the role of central banks in promoting inclusive development
Some issues on Economic & Social Survey 2022

• Inclusive fiscal policies (spend smart)
  □ There is not much discussion on green spending, which is vital to not only sustainable but also inclusive development

• Inclusive fiscal policies (tax fair)
  □ Comparison with OECD countries suggests that Asian developing countries need to expand personal income tax (through higher progressivity) and social security contributions
  □ They should also consider introducing inheritance tax and real estate (or property) tax

• Central bank’s role in promoting inclusive development
  □ Lack of sufficient evidence on the effect of monetary policy on income and wealth distribution
  □ Not all central banks manage foreign exchange reserves
  □ Central bank digital currency promotes financial inclusion for payment settlements, but not for other financial services (such as loans, insurance)

• Structural transformation for inclusive development
  □ It is unclear whether the government should or can “keep the pace of technological developments at a more manageable pace,” and a better policy would be to encourage the private sector to adapt to the pace of technological development which can be rapid
  □ Countries which are aging fast and face labor shortages need more rapid adoption of digital-robotic-AI technologies
Central bank’s role in promoting inclusive development

• This is a very interesting but challenging issue
• The question is how to translate various central banks’ official statements, strategies and objectives to promote inclusive finance and development into action (or concrete policy)
• Some central banks are promoting financial inclusion by encouraging commercial banks to allocate a portion of loans to SMEs, but beyond this what sort of policies would be effective is unclear
• More evidence would be needed in order to make definitive recommendations on the role of monetary policy
Major risks to economic recovery (1)

Hikes in interest rates in the United States that are faster in pace than have been expected

• The U.S. Federal Reserve has been raising policy interest rates due to high inflation rates together with strong consumption, investment and job gains
• High inflation in the U.S. has been triggered by the rising prices of fuels and commodities due to global increases in oil and gas prices as well as domestic supply constraints (such as labor shortages and the disruptions of supply chains) in the wake of strong recovery of demand
• Given the rising U.S. interest rates, If emerging economies do nothing, they may face higher inflation through currency depreciation as they already face rising prices of resources and commodities, or they may even face the risk of rapid capital outflows and currency & financial crisis particularly when large external debts have been accumulated
• On the other hand, if they tighten monetary policy, they may be able to control inflation to some extent but face the risk of economic slowdown or even recession
Risks to economic recovery (2)

China’s economic slowdown due to lockdowns in major cities induced by the “zero-COVID” strategy

• “Zero-COVID” policy of China has been negatively affecting the Chinese economy, its exports and imports in a significant way, can have adverse impact on the Asian and world economy, and thus poses risks to economic recovery

• One of the reasons for the “zero-COVID” policy is the low vaccination rates particularly among old-age people (while in advanced economies the vaccination rates among old-age people are very high), which could lead to the collapse of the medical system once the pandemic spreads in China and infects a large number of aged people and people with material medical problems

• In addition, China needs to introduce effective COVID-19 vaccines and treatment medicines to cope with the spread of infections

• To move from the “zero-COVID” policy to the policy of coexisting with the pandemic, China has to redouble its efforts at improving the effectiveness of vaccines and vaccination rates (including the import of foreign vaccines) and manufacturing treatment medicines
Risks to economic recovery (3)

Rapidly rising energy, food and other resource prices, which have been aggravated by the Russia-Ukraine war

- Energy, food and other resource prices were rising even before the Russian invasion of Ukraine, reflecting a combination of the strong recovery of demand in advanced economies and inadequate supply capacities.
- The Russia-Ukraine war has been disrupting not only energy and food supplies (both Russia and Ukraine which are large suppliers of grain for the global market have not been able to export much) but also logistics and distribution systems, thereby contributing to further increases in these prices.
- Some food producing countries have begun to restrict exports of food to ensure their own food security.
- The rising energy, food and resource prices are raising concerns for energy and food security in many import-dependent developing countries, posing threat particularly for poor and vulnerable people.
Conclusion

Importance of policies in promoting inclusive development

• Fiscal policy is the best suited policy instrument to promote inclusive economic development, e.g., public spending on education, health and social protection and on green projects financed by taxes that also support inclusiveness, such as progressive personal income tax, inheritance tax and property tax.

• Monetary policy to achieve stable inflation and sustained growth is also important; Avoiding economic disruptions (high inflation, high levels of unemployment and financial crises) protects the poor and socially vulnerable who are significantly affected by these.

• Structural transformation due to globalization and digitalization can benefit people if they acquire sufficient skills and knowledge and are also protected by adequate social safety nets.

• Economic cooperation at the global, regional (Asia-Pacific), and subregional (East and Northeast Asia) level is vital in a highly interdependent world; Policymakers should jointly avoid trade restrictions, re-open the border for people’s movement by adopting the policy of coexisting with the pandemic, and address common risks such as the rising U.S. interest rates, energy & food prices.