Economic Policies for an Inclusive Recovery and Development

Economic and Social Survey of Asia and the Pacific 2022

Policy Dialogue
North and Central Asia
9 June 2022
Concerns about persisting inequalities have come to the fore in the aftermath of the COVID-19 pandemic ... macroeconomic policies need to address these concerns.

Despite a reasonably strong economic rebound from the pandemic, people are left behind... this calls for more attention to inclusive policies.

The 2022 Survey goes beyond traditional macroeconomic thinking and provides new insights on how macroeconomic and structural policies can tackle inequality:
Economic performance and Outlook

– a nascent recovery and uncertain outlook
Asia-Pacific region experienced **a strong economic rebound** in 2021.
Driven by partial normalization in socioeconomic activities and robust external demand in 2021

- Strong export performance made up for slow recovery in domestic demand

  Monthly export volume index

- Economic activities started to return to normal

Source: Based on CEIC data and CPB Netherlands Bureau for Economic Policy Analysis
Yet, the level of output is below the pre-pandemic path...

- Rebound supported by robust external demand
- In turn, manufacturing and industrial production responded to strong external demand
- Still, the level of output is about 2% below the pre-pandemic path
Inflation has been on a rising trend **surpassing targets** in many countries

- Rising global commodity prices
- Soaring food price index
- High shipping costs
- Currency depreciation
- Pandemic related expansionary fiscal and monetary response

Source: Based on CEIC data (accessed 4 March 2022).
Note: Inflation and core inflation are for the latest month available between December 2021 and February 2022.
Outlook is riddled with uncertainty

- Recovery expected at a more moderate pace in 2022 and 2023
- Full resumption influenced by availability of vaccines, stringency of restrictions, labour market recovery
- Inflation, along with interest rates, is expected to remain elevated in the near term
- Risks of long-lasting scars and macroeconomic stability are rising
- The Russia-Ukraine war has dealt a significant blow to the NCA region & casts a shadow on recovery prospects

Source: ESCAP estimates and projections.
The Russia-Ukraine war is expected to severely dent the economic recovery in NCA

Direct impact include:

- Higher inflation
- Slowdown in economic activity and growth
- Pressure on fiscal positions and tightening financing conditions

The shocks will be particularly severe for NCA countries

- Russian economy is expected to contract by 8.6% in 2022
- NCA countries are directly affected through trade and remittance channels
- Although fuel exporters may benefit from high oil and gas prices, global economic deceleration and uncertainties cast clouds over the outlook

Source: ESCAP estimates and projections.
Why should we care about inequality?
The K-shaped recovery has brought the issue of inequality to the fore, with vulnerable sections disproportionately affected...
...and 85 million people have been pushed back into extreme poverty, making the issue all the more pertinent.

Source: ESCAP estimates.
Addressing this gap and *building forward fairer* will require coordinated government action.
Policy Considerations

Video – summary of Survey 2022 messages

https://www.youtube.com/watch?v=Wtbde1wLd4I&ab_channel=UnitedNationsESCAP
Government’s role in reducing inequality
Fiscal policy matters...
Fiscal spending can **tackle inequality** ..... but **impact varies**...

**Impact of seemingly same category fiscal policies varies greatly raising questions on effectiveness and targeting**

Impact of fiscal policies on inequality, according to 1 per cent of GDP expenditure/revenue

Gini coefficient (0-100)

Source: ESCAP estimates based on CEQ data.
Fiscal spending can **tackle inequality** ..... but impact varies...

**Impact** of seemingly same category fiscal policies **varies greatly** raising questions on effectiveness and targeting

Impact of fiscal policies on inequality, according to 1 per cent of GDP expenditure/revenue

Gini coefficient (0-100)

Source: ESCAP estimates based on CEQ data.

**Expenditure and tax categories**

1 - Education
2 - Health

**Gini change, points, 0-100 scale**

Source: ESCAP estimates based on CEQ data.
Impact of seemingly same category fiscal policies varies greatly raising questions on effectiveness and targeting

Impact of fiscal policies on inequality, according to 1 per cent of GDP expenditure/revenue

Gini coefficient (0-100)

Fiscal spending can **tackle inequality ..... but impact varies**...

Expenditure and tax categories

1 - Education
2 - Health
3 - Direct transfers
4 - Indirect subsidies

Source: ESCAP estimates based on CEQ data.
Fiscal spending can **tackle inequality ...... but impact varies**...

**Impact of seemingly same category fiscal policies varies greatly raising questions on effectiveness and targeting**

Impact of fiscal policies on inequality, according to 1 per cent of GDP expenditure/revenue

Gini coefficient (0-100)

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Source: ESCAP estimates based on CEQ data.
However, fiscal space has dwindled

Fiscal indicators
Asia-Pacific developing countries, as a percentage of GDP
Percentage

Source: ESCAP estimates based on IMF data.
However, fiscal space has dwindled, debt is up,

Fiscal indicators
Asia-Pacific developing countries, as a percentage of GDP
Percentage

f – forecasts, shaded

Source: ESCAP estimates based on IMF data.
However, fiscal space has dwindled, debt is up, and consolidations are expected.

**Fiscal indicators**
Asia-Pacific developing countries, as a percentage of GDP
Percentage

**Fiscal balance**
Asia-Pacific developing countries, as a percentage of GDP
Percentage

f – forecasts, shaded

Source: ESCAP estimates based on IMF data.
Consolidations are likely to increase inequalities and reduce output.

**Inequality, Gini coefficient (0-100)**

- Change in Gini coefficient over years after fiscal episode.

**GDP per capita growth, percentage points**

- Impact on GDP growth over years after fiscal episode.

Source: ESCAP estimates.
Hence, need to maintain expenditures in healthcare, education and social protection.

which are likely to get cut first....
...but matter the most for recovery and inequality reduction.
Level of spending on healthcare is already low...

Health expenditures remain much below world and high-income countries averages...
Current health expenditure, percentage of GDP.

Source: World Bank data.
Expenditure on education in Asia and the Pacific remains below the global target

Spending on education in the Asia-Pacific region, percentage of GDP.

Source: ESCAP estimates based on IMF data.
... and **social protection** coverage remains low and varies across countries in the region

Social protection coverage rates vary considerably across Asia-Pacific subregions

Social protection coverage by at least one area in Asia and the Pacific, latest year available

**SOCIAL PROTECTION**

<table>
<thead>
<tr>
<th>Region</th>
<th>Percentage</th>
</tr>
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<tr>
<td>ESCAP region</td>
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<td>South and South-West Asia</td>
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<td>Pacific</td>
<td>78</td>
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<td>North and Central Asia</td>
<td>78</td>
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</tbody>
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*Source: ESCAP and ILO, 2020*
Policy recommendations – Bigger bang-for-the-buck

**Spend Smart**

**Inclusiveness**
**Impact**
**Efficiency**

### Health care
- Provide universal health coverage

### Education
- Strengthen early age education for all

### Social protection
- Provide universal basic social protection
Policy recommendations – Bigger bang-for-the-buck

**Health care**
- Provide universal health coverage
- Reduce wasteful and inefficient spending

**Education**
- Strengthen early age education for all
- Eliminate socio-economic barriers at all levels of education

**Social protection**
- Provide universal basic social protection
Policy recommendations – Bigger bang-for-the-buck

**Health care**
- Provide universal health coverage
- Reduce wasteful and inefficient spending
- Deploy digital health technologies

**Education**
- Strengthen early age education for all
- Eliminate socio-economic barriers at all levels of education
- Close the digital divide

**Social protection**
- Provide universal basic social protection
- Improve efficiency via digital technologies
Alongside targeted fiscal spending, revenues need to be increased as tax collection remains low in the region.

Source: OECD (2021a)
...due to tax avoidance and informality

**tax avoidance is high**

7.6 per cent of the tax revenue in the Asia-Pacific region was estimated to be lost due to misinvoicing in 2016.

**informality is ubiquitous**

68 per cent of workers being employed in informal economy across Asia-Pacific

Source: Kravchenko, 2018.
Policy recommendations – increase revenues

Pay fair share
- Ensure all individuals and companies comply with existing regulations
- Close loopholes
- Fight illicit financial flows

Expand tax base
- Formalize business activities
- Expand taxation of digital economy

Shift tax burden
- Take tax burden off from the lowest income households
- Make corporate and personal income taxes more progressive
Government’s role in reducing inequality
Addressing the root cause through structural policies...
Traditional hypothesis of Kuznets postulates an initial increase in inequality before a subsequent decline, following an inverted U-shape...
... but diversity in national pathways suggests space for policies to have an impact

Source: UN-ESCAP based on SWIID & WDI.
Taxes and transfers play an important role in addressing the symptoms of inequality in advanced countries...

Source: ESCAP, based on the Standardized World Income Inequality Database (SWIID) 9.1 (accessed on 26 November 2021)
...but their equalizing impact is still highly limited in developing countries

Source: ESCAP, based on the Standardized World Income Inequality Database (SWIID) 9.1 (accessed on 26 November 2021).
These findings suggest that:

To build forward fairer, policy effort would also be needed to proactively shape structural and market forces that determine inequality levels and trends in the first place.

Even for fiscal policies, greater attention should be devoted to using taxes and spending to tilt such structural and market forces in favor of inclusive development.
... which requires action on three fronts for more equal market outcomes

**Guide**

*Structural transformation towards a job-rich path*

- Mobilize support for strategic sectors
- Leverage public R&D investment
- Establish correct market signals for private sector technological choices

**Shape**

*Income-distribution outcomes of the market*

- Strengthen labor’s position in the job market
- Empower labor in corporate decision-making processes
- Prioritize equal access in education policies

**Manage**

*The socioeconomic disruptions of technological revolution*

- Preserve progresses made in broad-based social protection as a first line of defense
- Strengthen support for on-the-job training, lifelong learning and vocational education
- Keep technological changes at a more manageable pace
Role of Central Banking in Inclusive Development
Central banks **should** and **can** promote **inclusive development**
Central banks should and can promote inclusive development.

- Monetary Policy Conduct
- Official Reserve Management
- Currency Issuance
- Financial Regulation
Promote inequality-mindful monetary policy

Inflation stability

Inequality-mindful monetary policy conduct

• Communicate the distributional impacts to the public
• Consider income/wealth distribution when making monetary policy decisions
Central banks should and can promote inclusive development

- Monetary Policy Conduct
- Official Reserve Management
- Currency Issuance
- Financial Regulation
Invest official reserves with social gains

Safety & liquidity

Reserve allocations with social gains

• Set up investment committee to make allocation decisions

• Use excess reserve as seed capital for local social projects

• Allocate part of asset purchases to social bonds
Central banks should and can promote inclusive development.

- Monetary Policy Conduct
- Official Reserve Management
- Currency Issuance
- Financial Regulation
Foster financial inclusion through CBDC

Adequate cash in circulation

Central bank digital currency (CBDC) for financial inclusion

- Choose design features that help financial access
- Improve digital and financial literacy
- Identify associated risks and mitigation measures
Central banks should and can promote inclusive development

- **Monetary Policy Conduct**
- **Official Reserve Management**
- **Currency Issuance**
- **Financial Regulation**
Support innovative social-oriented financial instruments

Robust financial sector

Innovative, social-oriented financial instruments

• Increase understanding among market players

• Develop/harmonize taxonomies for pro-social financial instruments

• Grant financial support to cover high verification cost
Key Takeaways – Survey 2022

- Inclusion should be at the center of economic policies.
- Focus on efficiency and impact of fiscal policy.
- Expand domestic revenues, shifting the burden away from low-income households.
- Target market outcomes – promote job-rich transformation and empower the labor.
- Inclusive central banking is possible.
- Redesign monetary policy, reserve management, innovative finance, and digital currencies for inclusive development.
Thank you!