PART 2

TURNING THE TIDE

towards inclusive trade and investment
The interplay of several factors was behind the choice of theme for this year’s issue of the Asia-Pacific Trade and Investment Report. First, the global economic crisis has caused a departure from the previous trend of high and sustained economic growth among the Asia-Pacific developing economies. This has prompted a rethink over the sustainability of an export-led growth model which depended on continuing strong demand in advanced economies. More fundamentally, the slowdown also exposed other weaknesses in the region’s dominant development approach including: a high dependency on low-priced labour; lax adherence to labour standards; high resource-intensity of production; and weak regulatory regimes with inconsistent enforcement. Second, the international community has agreed on the Rio+20 outcome document “The Future We Want” as a framework for achieving internationally accepted development goals. The document stresses the need for inclusive and equitable growth and will shape the global agenda following the United Nations campaign to achieve the Millennium Development Goals which draws to a close in 2015. Trade and investment are instrumental parts of that framework. Third, there is increasing awareness of, and objections to, the rising inequalities in the region. This points to the risks inherent in pursuing trade and investment under “business as usual” conditions; further increases in inequality are a growing threat to social stability and sustainability. Trade and investment are intimately linked with issues of employment, income distribution and inequality; hence any change in approach to trade policy will have important implications on the overall development of any market-oriented economy.
Therefore, turning the tide and making trade and investment inclusive has become extremely important for the region, which, globally, is home to the largest number of absolute poor. Delivering on this involves consideration of all aspects of inclusive development which trade and investment affect. In the first place, it is about the fair and free access of producers and consumers to global and regional markets for goods, services, capital, finance and labour. This is especially critical for micro and small and medium-sized enterprises as well as individual producers or service providers. But it is also about consultative decision-making processes on trade, investment and related policies at the local, national, regional and global levels. In other words, achieving inclusive trade and investment requires giving a voice to those who have been so far excluded from sharing in the benefits of trade and investment-led economic growth.

A. STYLIZED FACTS

There are plenty of stylized facts supporting the notion that greater economic openness (through trade and investment) is an important element in explaining higher economic growth. In many countries, greater openness and integration has been the critical factor behind successful development. Openness is normally understood as the size of international transactions (that is, mostly trade and investment) in the overall economy. This is usually measured by the share of overall trade value in a country’s gross domestic product (GDP). Empirical evidence supports the argument that the fastest growing countries have been those associated with an expansion of their share in the global merchandise and services trade. Few countries have grown over the long term without experiencing a large expansion of trade. This is especially so for developing Asian economies, which have, on average, outperformed other developing economies in terms of real GDP and trade growth over the period 1990-2011 (figure 7.1). Thus, growth is often associated with openness to trade and investment; indicating that, in principle, higher openness leads to higher growth.

Similarly, there is ample evidence on the relationship between strong economic growth and sustained poverty alleviation (for example, Bhagwati and Srinivasan, 2002; Giordano and Li, 2012). Asia’s strong growth over the past two decades was translated into a significant decline in poverty (table 7.1). This was a major contributor to the global success of halving poverty five years ahead of the MDG target timeframe. Whereas in

**FIGURE 7.1**

Fast growth of trade and real GDP go hand-in-hand, 1990-2011

<table>
<thead>
<tr>
<th>Region</th>
<th>GDP (% change)</th>
<th>Exports (% change)</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia &amp; Pacific</td>
<td>10.5</td>
<td>12.0</td>
</tr>
<tr>
<td>South Asia</td>
<td>8.0</td>
<td>9.5</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>4.5</td>
<td>6.0</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>2.0</td>
<td>3.0</td>
</tr>
<tr>
<td>Europe &amp; Central Asia</td>
<td>1.5</td>
<td>2.0</td>
</tr>
</tbody>
</table>

1990 the region accounted for 81% of the world’s poor, this had fallen to 62% just two decades later. While all developing countries contributed to this achievement, China led the way. In China, the share of the population in extreme poverty dropped from 60% in 1990 to 12% in 2010. In South Asia, poverty rates fell by an average of one percentage point annually, from 54% in 1990 to 31% two decades later. While these falls in poverty in South Asia are encouraging, because of better performances elsewhere, the subregion now accounts for a higher share of the world’s poor than in 1990. The largest number of the world’s poor still live in Asia, with Bangladesh, China, India and Indonesia together being home to more than half. Furthermore, there is some evidence that inequality among the poor is worsening: some countries report more people living on less than $1.25 a day, while the number of people just above them at the next income tier shrinks (figure 7.2). This suggests that growth, which mostly was of trade-led type, is not benefitting the very poorest.

Asia-Pacific economies have differential performance records in alleviating poverty. Another concern they face is worsening inequality despite having enjoyed sustained periods of economic growth. Inequality (measured by different metrics\(^6\)) has increased across the region in the past two decades (figure 7.3). More worryingly, the 2008/2009 global economic crisis exacerbated the inequalities in economies which until then were thriving on export-led growth. The number of people without full, or even partial, access to productive employment and social services has been rising over the last decade. Many developing countries are becoming familiar with the phenomena of jobless growth, under-employment, and insecure jobs. This reflects a failure to share the benefits of the larger overall economic pie created by international openness. Continuing risks to growth in many major global economies, alongside increasing environmental pressures and vulnerabilities to natural disasters, raise concerns about the future development prospects for the poorest and most vulnerable. It is clear that the paradigm of trade and investment-led growth needs to change.

Traditional economic theory and policy were based on the belief that opening an economy to international trade and investment was justified on the basis it would produce aggregate gains.

### TABLE 7.1

<table>
<thead>
<tr>
<th>Region</th>
<th>Number of people living on less than $1.25 per day</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Percentage of population</td>
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<tr>
<td>-------------------------------</td>
<td>--------------------------</td>
</tr>
<tr>
<td>Europe and Central Asia</td>
<td></td>
</tr>
<tr>
<td>Latin America and the Caribbean</td>
<td></td>
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<tr>
<td>Middle East and North Africa</td>
<td></td>
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<tr>
<td>Sub-Saharan Africa</td>
<td></td>
</tr>
<tr>
<td>Asia</td>
<td></td>
</tr>
<tr>
<td>Bangladesh</td>
<td></td>
</tr>
<tr>
<td>China</td>
<td></td>
</tr>
<tr>
<td>India</td>
<td></td>
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<tr>
<td>Indonesia</td>
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<td>Nepal</td>
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<tr>
<td>Philippines</td>
<td></td>
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<tr>
<td>Viet Nam</td>
<td></td>
</tr>
<tr>
<td>East Asia and Pacific</td>
<td></td>
</tr>
<tr>
<td>South Asia</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
</tr>
</tbody>
</table>

While undeniably some groups would lose out from trade, these losers, it was argued, should be dealt with through distributional policies after the overall gains from opening had been secured. Redistribution could take the form of fiscal transfers to affected groups, or re-training and adjustment assistance to enable people to shift employment away from sectors adversely affected. In other words, it was expected that the gains created through enhanced economic growth will be sufficient to outweigh losses accruing to certain sectors. Society as a whole was expected to benefit. In contrast, what has been observed is that gains have been evaporating from the bottom of the social pyramid and been accumulating at the top; much like the idea that money is like helium and floats upwards if not restrained. As the stylized facts show, in many countries, and especially in the Asia-Pacific region, growth has benefited the rich faster than it benefited the poor. While the gains and prosperity created by dynamism and openness have been undeniably large, they are not producing inclusive outcomes.

FIGURE 7.2
Changes in poverty headcount, measured at $1.25 and $2 per day a
(in percentage points since 1990)

Source: Based on data from Balakrishnan, Steinberg and Syed (2013), p.5.
 a At 2005 PPP prices. In parentheses are the latest available year and corresponding poverty headcount ratios at $1.25 and $2 per day, respectively.

Today inequality is higher in many economies ... than pre-1990

FIGURE 7.3
Stylized facts: Asia’s experience in addressing inequality over last two decades

Source: World Bank, national authorities and IMF staff calculations.
1In parenthesis the latest available year and corresponding Gini Coefficients.
... and more pronounced than elsewhere in most other emerging economies...

Emerging economies: Change in Gini Index
(in Gini points)

Source: CEIC Data Company Ltd; World Bank, PovcalNet database; WIDER income inequality database; Milanovic (2010); National authorities and IMF staff calculations.

Source: Based on data from Balakrishnan, Steinberg and Syed (2013, p.5).

B. TOWARDS A NEW MODEL OF INCLUSIVE TRADE AND INVESTMENT

To understand all the potential benefits of trade and investment, this report investigates the conditions under which international openness would deliver inclusive growth. As the orthodox approach of “trade and invest first, and distribute gains later” does not produce the necessary and desirable inclusive outcomes, the missing elements in the model need to be explored. First the report examines the transmission channels through which trade, investment and other policies affect household welfare. This is done based on review of theoretical and empirical literature on the linkages between trade, investment and growth; and growth and poverty and inequality. Subsequently, the role of trade and investment in producing inclusive growth is also assessed through a macro-level econometric analysis. This analysis also identifies important complementary policies, for instance related to public investment, which can be deployed alongside trade and investment policy and which can produce more inclusive outcomes. In addition to econometric analysis which is primarily at the aggregate level, the report also uses a number of real world case studies and examples illustrating how the combination of trade and investment, with adequate complementary policies, can work together for the betterment of people’s lives. These findings from these different strands of analysis are the basis for proposed policy options and actions at the national, regional and international levels.

Some of these proposals require countries to join forces, at least at the regional level, and cooperate in pursuing solutions. This could be through a regional trade-financing scheme or open cumulation rules of origin for least developed countries. Here, the role of ESCAP as the leading United Nations regional organization, can be best utilized. ESCAP has been working on giving voice to the countries in regional and global forums, through its mandate to strengthen regional cooperation in the Asia-Pacific region. The organization has also been working to improve regional integration by building capacity to use WTO membership and accession to regional trade blocs and value chains, as trade-led engines of growth.

In fact, “Asia-Pacific Trade and Investment Report 2009: Trade-led recovery and beyond” examined the role of transparent and inclusive processes in forming trade, investment and related policies. This highlighted the need for countries to be able to easily access the international trading system through accession to WTO, or regional markets by participation in regional trade blocs (see ESCAP, 2009b, Part II in particular chapter 1). It also considered how trade policymaking could adequately represent all segments of society.
This year’s Report is a small step in providing further insights into factors and circumstances driving the inclusive impacts of various trade and investment policies and activities. Its objectives are: (1) to gain a better understanding about how trade, investment, facilitation and integration policies can support inclusive development, and, wherever possible, to measure the progress of countries in this regard; and (2) to propose a mix of policies for Asia-Pacific economies towards achieving inclusive development results, nationally and regionally.

The Asia-Pacific Trade and Investment Report 2013 Part II comprises chapters 7 to 10. Following this introduction, chapter 8 deals with definitional issues, and introduces concepts such as inclusive growth and inclusive trade and investment, which will be used in the report’s analysis. Chapter 9 is a macro-level econometric assessment of the significance of some of the more obvious trade and investment-related drivers of inclusiveness. Chapter 10 introduces sectoral and micro studies as real-world stories showing trade and investment working towards inclusive growth. Policy recommendations and proposed initiatives for regional action that have been identified through the report’s analysis are outlined in the concluding chapter and are summarized in the executive summary.

REFERENCES


Fritz, Johannes (2013). What supplementary policies may contribute to the inclusiveness of international openness? ESCAP Trade and Investment Division, Staff Working Paper No. 02/13, October. Bangkok.


ENDNOTES

77See, for example, the document entitled “Thematic Think Piece on Trade” issued by UN System Task Team on the Post-2015 UN Development Agenda (United Nations, 2012). The document also brings due attention to the interdependence between the principles of inclusivity and sustainability. However, the Asia-Pacific Trade and Investment Report addresses only inclusiveness aspect, while readers are invited to refer to “Climate-Smart Trade and Investment in Asia and the Pacific”, which explores linkages between trade and sustainability (Ratnayake, Proksch and Mikic (eds), 2012).

78A note on terminology: while the Report uses a phrase “trade and investment” when discussing the issues, this phrase is also meant to encapsulate all relevant international activities and related policies. This includes international flows of merchandise and services, capital and labour, transfer of technology, knowledge, ideas and information and policies instrumental to these flows as trade policies (border and behind-the-border measures influencing trade flows), trade facilitation procedures and measures, foreign direct investment policies and promotion, policies related to promotion of small and medium-sized enterprises, transfer of technology, etc.

79Notwithstanding, it is also important to address fair and free access of marginalized and vulnerable developing and least developed countries to the global and regional markets, affecting distribution of gains from international openness among countries. These issues have been addressed in previous APTIR issues and also mentioned in this report.

80Here are some of the comprehensive reviews of literature on openness and growth, openness and employment, and growth and poverty in alphabetical order: Balakrishnan, Steinberg and Syed (2013), Berg and Krueger (2003), Bhagwati and Srinivasan (2002), Dollar (1992), Dollar and Kray (2004), Lee, Syed and Wang (2013), Edwards (1998), Jansen, Peters and Salazar-Xirinachs (2011), Newfarmer and Sztajerowska (2011); also see a background paper for chapter 8 of this report (Fritz, 2013). Given this rich literature with re-examined empirical evidence, this report does not attempt to provide independent stylized facts on these linkages, nor to test relationships between openness and growth, or growth, poverty and inequality. Instead, it attempts to add value by providing additional insights into context ensuring that openness leads to inclusive growth outcomes. In addition to macro level econometric analysis, this is done by relying on case studies and community experiences of complementing trade and investment policies.

81Of course, this will be determined by a large number of factors; most importantly by trade and investment restrictions like tariffs, non-tariff barriers, foreign exchange regimes, non-trade policies and the structure of national economies. Some commentators refer to this indicator as reflecting a country’s trade dependence. For more, see ESCAP (2009a).

82Poverty can be measured in several different ways; based on income per day or consumption (headcount), poverty-gap, inequality among the poor or as the multidimensional concept. Giordano and Li (2012) provides further discussion on issues in relation to alternative measures.

83According to the MDG 2013 Report, the world reached the MDG poverty (goal 1) target five years ahead of the 2015 deadline. Globally “in developing regions, the proportion of people living on less than $1.25 a day fell from 47 per cent in 1990 to 22 per cent in 2010.”

84Similar to measuring poverty, inequality can be measured in terms of income, wages, consumption or assets. There are different metrics in measuring inequality, from the most frequently used Gini coefficient, Theil index, decile dispersion ratio, to the share of income/consumption of the poorest share of population etc. Furthermore, addressing inequality concerns, in the context of international exchange, implies not only distribution among the groups within the country, but also distribution among the countries.