The Economic and Social Survey of Asia and the Pacific Year-end Update 2017 contains data and information on the latest macroeconomic trends, while identifying emerging risks and challenges and taking stock of economic and structural policy developments in the Asia-Pacific region. Its aim is to provide policy recommendations for policymakers, civil society and academia.

Economic growth in the region has picked up momentum in 2017, supported by stronger exports and robust household spending. Private investment, however, remains weak amid overcapacity and corporate and banking debt overhang in some major economies. The growth outlook for 2018 is broadly stable, mainly underpinned by growing domestic consumption. While rising intraregional demand is expected to support output growth, its strength may be clouded by increasing trade protectionism in the region and beyond.

Despite generally positive economic prospects, consumption-led economic growth amid loose monetary policy could aggravate overleveraging and is a source of financial vulnerability. Strengthening financial regulation and supervision should be one of the policy priorities in going forward.

Given that fiscal sustainability is not a concern in most Asia-Pacific countries, fiscal policy should continue playing an active role in lifting domestic demand and supporting development priorities. Its effectiveness will depend on fiscal management and good governance, both of which can be enhanced by using information technology to reshape the environment in which Governments operate.

To achieve the 2030 Agenda for Sustainable Development, higher wages supported by productivity gains, job creation, especially for youth and women, and improving environmental sustainability are critical. Moreover, as achieving the 2030 Agenda requires a significant increase in investments, Governments need to adopt innovative ways to enhance fiscal space, broaden participation of the private sector and promote deepening of capital markets.
The Economic and Social Commission for Asia and the Pacific (ESCAP) serves as the United Nations’ regional hub promoting cooperation among countries to achieve inclusive and sustainable development. The largest regional intergovernmental platform with 53 member States and 9 associate members, ESCAP has emerged as a strong regional think-tank offering countries sound analytical products that shed insight into the evolving economic, social and environmental dynamics of the region. The Commission’s strategic focus is to deliver on the 2030 Agenda for Sustainable Development, which it does by reinforcing and deepening regional cooperation and integration to advance connectivity, financial cooperation and market integration. ESCAP’s research and analysis coupled with its policy advisory services, capacity building and technical assistance to governments aims to support countries’ sustainable and inclusive development ambitions.
ECONOMIC AND SOCIAL SURVEY OF ASIA AND THE PACIFIC 2017: Year-end Update
KEY MESSAGES

Economic growth in the region has picked up momentum but challenges remain; improving the quality of growth will require policy focus.

- Stronger exports and robust private consumption, supported by favourable external conditions and accommodative domestic policies, are expected to lead to an upswing in economic growth in 2017. Private investment, however, remains weak partially as a result of overcapacity and debt overhang in the corporate and banking sectors of some major economies.

- The outlook for 2018 is broadly stable, underpinned by growing domestic and intraregional demand. Growth in intraregional trade, however, may lose some intensity as the positive base effect of the 2017 uptick in trade fades and demand for imports from China diminishes given the marginal slowdown in its economy due to ongoing structural reforms. Many protectionist measures continue to cast a shadow on the chances for a consistent revival in trade.

- The region’s current growth pattern, based on private consumption and loose monetary policy, could aggravate overleveraging and is a source of financial vulnerability. High corporate debt and distressed bank balance sheets are clouding prospects for a much-needed increase in private investment. At the same time, the probability of a tightening in global financial conditions is rising, and this could limit policy space in going forward.

- To achieve a stable and sustained economic growth momentum, higher wages supported by productivity gains and revival of private investment will be needed. To effectively support the 2030 Agenda for Sustainable Development, the region’s stronger economic growth must be translated into the creation of decent jobs, especially for youth and women, to facilitate poverty reduction. At the same time, attenuating inequalities with regard to income and opportunities and improving environmental sustainability will require policy focus.

A wide array of policies and reforms can improve the prospects for achieving the 2030 Agenda, which underscores the role of good governance. Special attention should be paid to expanding fiscal space.

- Monetary policy is expected to maintain its accommodative stance in support of economic growth, given the low and stable level of inflation. However, central banks need to pay closer attention to financial and external sector stability issues and continue with their deleveraging efforts to address the build-up of systemic risks. Strengthening macroprudential frameworks, regulation and supervision should be a priority.

- Fiscal policy should continue playing an active role in lifting domestic demand, “crowding in” private investment and supporting development priorities, such as improving social protection and stemming environmental degradation. The effectiveness of fiscal policy in addressing this host of issues will depend critically on good governance. In addition, good governance can prove vital for Governments to successfully lead the structural reforms that will enhance the supply side of their economies and transform them for the implementation of the 2030 Agenda.

- Currently, fiscal sustainability is not a concern in most countries. Nevertheless, to fill the wide financing gap – the difference between financial investments required to effectively pursue the 2030 Agenda and the prevailing trends - fiscal space must be enlarged, including through innovative ways to mobilize fiscal resources, broaden participation of the private sector and enhance deepening of capital markets.

- Technology can be effectively leveraged to improve governance and fiscal management and reshape the environment in which the Government operates. For instance, through use of technology, Governments can improve tax administration and compliance, and the implementation of direct benefit transfers while improving public expenditure efficiency.
ACKNOWLEDGEMENTS

The main purpose of the Economic and Social Survey of Asia and the Pacific 2017 Year-end Update is to provide policymakers, civil society and academia with recommendations on the current macroeconomic situation and trends in the region.

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<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
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<tbody>
<tr>
<td>CPEC</td>
<td>China-Pakistan Economic Corridor</td>
</tr>
<tr>
<td>CPI</td>
<td>consumer price index</td>
</tr>
<tr>
<td>CSP</td>
<td>customs service provider</td>
</tr>
<tr>
<td>ETS</td>
<td>emission trading systems</td>
</tr>
<tr>
<td>ESCAP</td>
<td>Economic and Social Commission for Asia and the Pacific</td>
</tr>
<tr>
<td>FDI</td>
<td>foreign direct investment</td>
</tr>
<tr>
<td>GDP</td>
<td>gross domestic product</td>
</tr>
<tr>
<td>GST</td>
<td>goods and services tax</td>
</tr>
<tr>
<td>ICT</td>
<td>information and communications technology</td>
</tr>
<tr>
<td>ILO</td>
<td>International Labour Organization</td>
</tr>
<tr>
<td>IT</td>
<td>information technology</td>
</tr>
<tr>
<td>NPL</td>
<td>non-performing loans</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
</tr>
<tr>
<td>OPEC</td>
<td>Organization of the Petroleum Exporting Countries</td>
</tr>
<tr>
<td>PMI</td>
<td>purchasing managers’ index</td>
</tr>
<tr>
<td>PPP</td>
<td>public-private partnerships</td>
</tr>
<tr>
<td>Q1</td>
<td>first quarter</td>
</tr>
<tr>
<td>Q2</td>
<td>second quarter</td>
</tr>
<tr>
<td>Q3</td>
<td>third quarter</td>
</tr>
<tr>
<td>Q4</td>
<td>fourth quarter</td>
</tr>
<tr>
<td>TFP</td>
<td>total factor productivity</td>
</tr>
<tr>
<td>TPP</td>
<td>Trans-Pacific Partnership</td>
</tr>
<tr>
<td>TSP</td>
<td>technological service provider</td>
</tr>
<tr>
<td>UNICEF</td>
<td>United Nations Children’s Fund</td>
</tr>
<tr>
<td>VAT</td>
<td>value-added tax</td>
</tr>
</tbody>
</table>
The essence of the 2030 Agenda for Sustainable Development is recognition that the welfare of a country encompasses much more than just expansion of economic output. The 2030 Agenda is aimed at promoting a broader concept of well-being through emphasis on social inclusiveness and environmental sustainability. However, while assessing economic conditions and growth prospects is necessary, it certainly is not sufficient to do justice to the spirit of the 2030 Agenda. In this context, although the Economic and Social Survey of Asia and the Pacific 2017 contained an examination of economic conditions in the Asia-Pacific region, its findings also highlighted that the benefits of economic expansion have accrued less to the poor, that inequality is high and that environmental degradation needs to be checked. To improve the quality of economic growth, comprehensive measures are needed, including labour market policies on such issues as minimum wages, fiscal measures, such as progressive taxation and social assistance, and environment policy instruments, such as energy subsidy reform and carbon pricing.

In the Survey for 2017, it was argued that effective pursuit of such a comprehensive policy agenda requires better and more effective governance, particularly in the context of fiscal management given the growing demands on fiscal policy to support economies and address diverse social and environmental challenges. In that publication, it was shown that good governance can help enhance the current low levels of tax revenues in several countries in the region and improve the composition and efficiency of public spending. The present report, the Year-end Update of the Survey for 2017, contains a further examination of the subject and analyses of the role of technology for better governance in fiscal management. In recognition of the sizeable financing gap between required and current investments in support of the Sustainable Development Goals, the Update also provides a preliminary assessment of means for strengthening public finances and effectively leveraging the private sector. Before these issues are discussed, however, a detailed updated assessment of recent economic developments in Asia and the Pacific is provided as well as the various policy options that could improve economic, social and environmental prospects.

For the region, in view of its low and stable inflation rate, monetary policy is expected to maintain its accommodative stance in providing support for economic growth. The desired impact, however, has been muted. Given high household and corporate debt in some major economies and the potential volatility and outflow of capital from the region due to gradual interest rate increases in the United States of America, monetary policy authorities need to pay close attention to financial and external sector stability issues as well, and continue with their deleveraging efforts to tackle the build-up of systemic risks. Strengthening macroprudential frameworks, regulation and supervision should therefore be a priority.

Fiscal policy on the other hand can continue playing an active role in supporting domestic demand, “crowding in” private investment and meeting long-term
development priorities, such as social protection. In shedding light on the notion of “fiscal space” - how much countries can stretch the national budget to support development priorities without risking fiscal sustainability - it is noted in the Update for 2017 that, other than primary balance (fiscal balance net of interest payments) and the differential between economic growth and borrowing costs, the feedback between fiscal policies and private sector behaviour, in terms of fiscal impact on economic growth, is of consequence with regard to debt sustainability as well. As emphasized in the Survey for 2017, good governance and transparent and accountable institutions are critical for ensuring the effectiveness of fiscal policies. Moreover, good governance also has proven vital for successfully leading the structural reforms that will enhance the supply side of economies.

Fiscal policy is of special importance because the region’s steady economic growth, driven by globalization and technological progress, is not being translated into proportional creation of decent jobs. This situation represents obstacles to efforts to reduce poverty and inequality. To attenuate this negative circle, social protection continues to be vital for addressing inequality of income and opportunity. At the same time, the region experienced several natural disasters in 2017, which reflects the region’s vulnerability and underscores the importance of effective government response in tackling climate change - both in mitigating it and adapting to it. Weak governance could undermine all three dimensions of sustainable development - for instance by damaging investment prospects, widening inequalities and meeting environmental degradation with inaction. As illustrated in the Survey for 2017, fiscal management is an important channel through which governance affects such development outcomes. To provide further insights, in the Update for 2017 two specific cases are discussed in which technology is applied to improve fiscal management: one in the context of tax administration and compliance; the other in implementation of direct benefit transfers and public expenditure efficiency. In emphasizing the importance of “financing for development”, it is concluded in the Update for 2017 that the amount of financial investment required to effectively pursue the 2030 Agenda for Sustainable Development far exceeds that reflected in prevailing trends. Efforts to close this wide investment gap involve calls for the mobilization of larger amounts of fiscal resources and greater private sector participation than in the past.
1. ECONOMIC OUTLOOK, QUALITY OF ECONOMIC GROWTH AND ASSOCIATED RISKS AND CHALLENGES

1.1 Output and inflation: update and forecast

Economic conditions in Asia and the Pacific are stable, and economic growth is expected to increase slightly in the near future. After experiencing an economic growth rate of 5.2% in 2016, developing economies in the region may expect the average GDP to grow by an estimated 5.4% in 2017 and 5.3% in 2018 (table 1). This represents an upward revision by 0.4 and 0.2 percentage points for 2017 and 2018, respectively, compared with the figures contained in the forecast of the Survey for 2017. The main reason for this revision is a recent upturn in global trade - growth in the volume of merchandise trade in 2017 has been estimated at 3.6% compared to 1.3% in the previous year (WTO, 2017). This increase in trade is primarily due to better economic performance in the Euro area and the United States as well as China's increased imports from other economies in the region. Together, these two elements explain the recent export and overall growth momentum in the Asia-Pacific region.

For 2018 the economic outlook is stable, and continues to be driven by growing domestic demand. Intraregional trade is expected to lose some intensity (mainly due to a high base effect), although it is still expected to grow at a healthy pace - the volume of exports is projected to grow by 3.5% (ESCAP, 2017b). The likely moderation in intraregional trade during 2018 can be attributed to a slightly lower demand for imports from China, where structural reforms are ongoing to address overleveraging in the corporate sector. High leverage in the corporate and banking sectors of other major economies, such as India, and distressing household debt in countries, such as the Republic of Korea, still must be addressed if private investment is to drive economic growth.

In the first half of 2017, China’s economy grew at an annualized rate of 6.9%, the performance of which was better than earlier forecasts, and they beat market expectations. This growth was underpinned by robust private consumption and public sector investments along with higher levels of exports. Consequently and keeping in view the country's ongoing deleveraging and rebalancing efforts, the economic growth forecast for China in 2017 has been revised upwards by 0.3 percentage points to 6.8% (table 1). For 2018, structural reforms to address the country's excess capacity and vulnerabilities in its corporate and banking sectors are likely to result in moderation of the economic growth rate to 6.6% (table 1). Indeed, some sectors seem to have reached their peak; for instance, recent data would suggest that industrial output and fixed-asset investments may be losing steam.4

In the Russian Federation, robust economic growth in the first half of 2017 was driven mainly by a surge in private consumption, which increased by 3.3% year on year in the first quarter (Q1) of 2017. The economy benefited from an increase in oil prices during the year. From an average of $42.81 per barrel in 2016, oil prices have stabilized at about $50.60 per barrel in the first eight months of 2017. The economy of the Russian Federation is expected to grow by 1.7% in 2017 and leave behind its two-year contractionary period. The outlook for the economy, however, hinges upon the outlook for the price of oil. Production cuts agreed among OPEC members will end in Q1 of 2018, which may lead to a dip in oil prices as the supply of oil increases in 2018. Azerbaijan's economy is also gradually improving. In the first half of 2017, it contracted by 1.3%, which is much less than the 2.5% contraction in 2016. The country is still undergoing adjustments in the oil sector to recover from the 2014 plunge in oil prices. While public sector capital outlays are cushioning some sectors, such as construction, other sectors are already growing, such as services and agriculture. It is expected that Azerbaijan’s economy will start expanding again in 2018.

Several other economies in the region are also exhibiting sturdy economic growth. For instance, for 2017 Thailand’s economic growth forecast has been revised upwards from 3.3% to 3.5%, with private consumption providing the highest net contribution to this expansion. Robust private consumption growth is being assisted by a buoyant tourism sector and an accommodative monetary stance. Robust performance of the agricultural sector and the external sector have also supported Thailand’s growth acceleration. The Malaysian economy is also expected to perform better than had earlier been projected; it is predicted to grow by 5.2% in 2017. Investments surged in the first six months of the year; robust private consumption was supported by higher wages and employment. Exports from Malaysia also grew at a relatively higher rate, thanks to stronger external demand for such products as rubber and palm oil. Viet Nam’s economy is also performing well. In Q2, it grew by an annualized 6.2%, up from a considerably lower 5.2% economic growth rate in Q1 of 2017. It is
Table 1. Economic growth rates in selected subregions/countries/groups in Asia and the Pacific, 2016-2018

<table>
<thead>
<tr>
<th>Subregion/country</th>
<th>Real GDP growth</th>
<th>Change from that covered in the Survey for 2017 (percentage points)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2016*</td>
<td>2017*</td>
</tr>
<tr>
<td>Developing ESCAP economies&lt;sup&gt;c&lt;/sup&gt;</td>
<td>5.2</td>
<td>5.4</td>
</tr>
<tr>
<td>East and North-East Asia (excluding Japan)</td>
<td>5.9</td>
<td>6.1</td>
</tr>
<tr>
<td>China</td>
<td>6.7</td>
<td>6.8</td>
</tr>
<tr>
<td>Republic of Korea</td>
<td>2.8</td>
<td>3.0</td>
</tr>
<tr>
<td>South-East Asia</td>
<td>4.5</td>
<td>4.8</td>
</tr>
<tr>
<td>Indonesia</td>
<td>5.0</td>
<td>5.1</td>
</tr>
<tr>
<td>Malaysia</td>
<td>4.2</td>
<td>5.2</td>
</tr>
<tr>
<td>Philippines</td>
<td>6.9</td>
<td>6.6</td>
</tr>
<tr>
<td>Thailand</td>
<td>3.2</td>
<td>3.5</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>6.2</td>
<td>6.3</td>
</tr>
<tr>
<td>South and South-West Asia</td>
<td>6.6</td>
<td>6.0</td>
</tr>
<tr>
<td>Bangladesh&lt;sup&gt;d&lt;/sup&gt;</td>
<td>7.1</td>
<td>7.2</td>
</tr>
<tr>
<td>India&lt;sup&gt;e&lt;/sup&gt;</td>
<td>7.1</td>
<td>6.6</td>
</tr>
<tr>
<td>Iran (Islamic Republic of)</td>
<td>11.5</td>
<td>5.3</td>
</tr>
<tr>
<td>Pakistan</td>
<td>4.7</td>
<td>5.3</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>4.4</td>
<td>4.5</td>
</tr>
<tr>
<td>Turkey</td>
<td>3.2</td>
<td>5.1</td>
</tr>
<tr>
<td>North and Central Asia</td>
<td>0.1</td>
<td>2.0</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>-2.5</td>
<td>-1.0</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>1.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Russian Federation</td>
<td>-0.2</td>
<td>1.7</td>
</tr>
<tr>
<td>Pacific island developing economies</td>
<td>2.0</td>
<td>2.9</td>
</tr>
<tr>
<td>Fiji</td>
<td>0.4</td>
<td>4.2</td>
</tr>
<tr>
<td>Papua New Guinea</td>
<td>2.0</td>
<td>2.5</td>
</tr>
<tr>
<td>Least developed countries</td>
<td>6.0</td>
<td>6.9</td>
</tr>
<tr>
<td>Landlocked developing countries</td>
<td>1.9</td>
<td>4.1</td>
</tr>
<tr>
<td>Small island developing States</td>
<td>2.4</td>
<td>3.2</td>
</tr>
</tbody>
</table>

Source: ESCAP, based on national sources; United Nations Department of Economic and Social Affairs (2017); IMF, International Financial Statistics database; ADB (2017a); and CEIC Data (www.ceicdata.com).

Notes:
- <sup>a</sup> Estimate.
- <sup>b</sup> Forecast (as of 31 October 2017).
- <sup>c</sup> An earlier estimate of real GDP growth for 2016 for developing ESCAP economies was 4.9%, as reported in the Survey for 2017. However, based on the latest available data, this figure has been updated.
- <sup>d</sup> Fiscal year from 1 July 2016 to 30 June 2017.
- <sup>e</sup> Fiscal year from 1 April 2017 to 31 March 2018.

Estimated to grow by 6.3% and 6.4% in 2017 and 2018, respectively, boosted notably by foreign investment. Disbursed foreign investment is expected to reach a record $16 billion in 2017, equivalent to about 7.5% of GDP.<sup>5</sup>

Turkey’s economy also grew faster than expected - by 5.1% in Q2, mainly because gross capital formation rose by 9.5% year on year. It is forecasted to grow by 5.1% in 2017 compared with an earlier estimate of 2.8%. Bangladesh ended fiscal year 2017 exceeding earlier forecasts as well. Despite a slowdown in exports and remittance inflows, it grew by 7.2% in fiscal year 2017, which is its best performance in a decade, supported by the manufacturing, services and agricultural sectors.<sup>6</sup> The momentum is expected to continue in 2018 on the back of strong domestic demand and infrastructure investments.

India’s experience is rather different. So far in 2017, the economy has not performed in line with earlier expectations. The 5.7% annualized economic growth
ECONOMIC AND SOCIAL SURVEY OF ASIA AND THE PACIFIC 2017 : YEAR-END UPDATE

rate in Q1 of fiscal year 2017 was the lowest in the last three years. Lingering effects of demonetization, weakening investment expenditures and sharply declining manufacturing growth as firms held back production to prevent inventory build-up before the new goods and services tax (GST) was implemented in July 2017 are the main reasons for this performance; there was considerable uncertainty about the GST policy. As a result, India's economic growth forecast for 2017 has been revised downwards by 0.5 percentage points to 6.6%. Notwithstanding this downward revision, the disruptive effects of reforms are expected to gradually fade away, and private consumption is set to recover. A good harvest is expected to bolster agricultural output, while the uptick in rural wages and a pay hike for central Government and state employees will support rural and urban consumption. Ongoing reforms are also expected to enhance the ease of doing business and thereby support stronger investment. Therefore, for 2018 India's economy is projected to expand by 7%.

A broad risk currently casting its shadow on the region's economic outlook stems from geopolitical tensions, notably in the Korean peninsula. Factors such as these can have only dissuasive effects on investment (unless, perhaps, in defense companies), and often result in directing resources to security - and less to development spending.

Other risk factors consist of high social tensions, especially when they relate to crisis situations. Notably, Myanmar is currently undergoing a crisis that has led more than 500,000 Rohingya Muslims to flee into Bangladesh (IOM, 2017). Similarly, a risk that should not be underestimated is that of climate change-induced meteorological phenomena. Many natural disasters have occurred in 2017, and these have hampered not only economies growth but prospects for sustainable development as well.

**Key drivers of economic growth**

Domestic private consumption remains the dominant source of economic growth (figure 1). This is facilitated by relatively low and steady inflation, low interest rates, growing purchasing power and high consumer confidence. The global top 10 ranking of consumer confidence in Q2 of 2017 included 6 countries in the region: the Philippines, India, Indonesia, Viet Nam, China and Thailand (in that order). The increase in consumer confidence has been supported by declining economic uncertainty since January 2017 (figure 2) and is visible in the upward revisions in economic growth forecasts.

In China, consumption provided the largest contribution to economic growth in the first half of the year (5 percentage points), with retail sales rising to 10.8% and

---

**Figure 1. Demand-side contributions to growth, first half of both 2016 and 2017**

<table>
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<tr>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>-7.5%</td>
<td>-1.9%</td>
<td>0.7%</td>
<td>0.8%</td>
<td>14.7%</td>
<td>15.0%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>India</td>
<td>-8.6%</td>
<td>-0.1%</td>
<td>0.8%</td>
<td>0.8%</td>
<td>13.7%</td>
<td>14.5%</td>
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<tr>
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<td>0.8%</td>
<td>0.8%</td>
<td>13.7%</td>
<td>14.5%</td>
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<tr>
<td>Republic of Korea</td>
<td>0.5%</td>
<td>0.5%</td>
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<td>13.7%</td>
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<tr>
<td>Malaysia</td>
<td>-1.2%</td>
<td>-0.2%</td>
<td>0.8%</td>
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<td>13.7%</td>
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<tr>
<td>Philippines</td>
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<tr>
<td>Russian Federation</td>
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<td>0.8%</td>
<td>0.8%</td>
<td>13.7%</td>
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<tr>
<td>Thailand</td>
<td>-1.4%</td>
<td>-0.4%</td>
<td>0.8%</td>
<td>0.8%</td>
<td>13.7%</td>
<td>14.5%</td>
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<tr>
<td>Turkey</td>
<td>-1.3%</td>
<td>-0.3%</td>
<td>0.8%</td>
<td>0.8%</td>
<td>13.7%</td>
<td>14.5%</td>
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Note: Data on China's investments refer to gross capital formation, while India's data refer to the first quarter of fiscal year 2016/17 compared with the first quarter of fiscal year 2017/18.
an upswing in consumer confidence. The recent strengthening of online retail growth, accounting for up to approximately 18% of total retail sales, and the advent of mobile payments are expected to result in an increased number of transactions (Sheng and Geng, 2017) and contribute to consumption growth in China. Such growth has been an objective of China’s rebalancing efforts. In India, consumption growth declined in early 2017, primarily due to the country’s demonetization policy. Nevertheless, in the new fiscal year, there have been some signs of resurgence (for instance, sales of two-wheel vehicles increased in August 2017 above pre-demonetization levels), along with a rebound in the manufacturing purchasing managers index (PMI) (figure 3).

Figure 3. Purchasing managers indices in China and India


Note: A PMI value higher than 50 indicates that the manufacturing economy is expanding, while a PMI value of less than 50 indicates that the manufacturing economy is contracting.
3). In the Russian Federation, consumption and business sentiments are being nurtured by lower consumer price inflation and interest rates, while real wages are rising and unemployment has shrunk to about 5.5%.

Consumption-led economic growth may turn out to be rather fragile over time. This is because, without consistent increases in real wages backed by rising productivity, such growth can lead to debt accumulation and entail financial vulnerability. For productivity gains and higher real wages to sustain economic growth in the long term, private investment has considerable room for improvement. Furthermore, growth in real wages should not be limited to a few countries. Inequality in the region - especially wealth inequality - has expanded since the 1990s. Beyond moral and/or social cohesion considerations, however, it seems clear that high inequality adversely affects the income growth of the poor but not the rich; hence, it is deleterious for economic growth (Deininger and Squire, 1998). Avoiding excessive inequality and sustaining economic growth may therefore be two sides of the same coin (Berg and Ostry, 2017).

Growth in private investment in the region remains relatively weak overall, although it is partially due to efforts by China to rebalance its economy and tackle high leverage in the corporate sector (figure 4). Other than the impact of Chinese reforms, the reasons for slower growth include excess capacity and low capacity utilization in certain industrial sectors, such as energy and utilities. Furthermore, there are outstanding balance sheet pressures due to debt overhang in the corporate and banking sectors of some major economies, as well as burdening household debt in others.

In China, investment contributed a meagre 1.8 percentage points to economic growth, amid a slowdown in credit growth and a less accommodative monetary policy. Notably, investment slowed in manufacturing, which is in line with the rebalancing efforts of the Government of China towards innovation-led economic growth. Indeed, investments in the high-technology sector soared (figure 5), indicating a shift to support higher value added in line with the Government’s policy.

China’s property market is also cooling down (figure 5), as seen for instance in the slower pace of growth in real estate investment. Home sales slowed as well due to purchase restrictions, such as limiting the number of properties an individual can buy, or requiring buyers to have permanent residence permits (hukou). Some measures implemented by commercial banks, such as increasing the size of down payments and raising mortgage rates, have also slowed the pace of mortgage lending. Thus, real estate investment is expected to support economic growth to a lesser extent in the future as a result of the new policies.

**Figure 4. Private investment growth in selected countries**


Note: The data presented are the growth rates in constant 2011 international dollars. As shown by the dotted lines, the median value of private investment in 33 regional economies declined from 10.3% in the period 2005-2007 to 3% in the period 2013-2015.
Stringent policies in China designed to favour deleveraging are leading to progress on tackling high levels of indebtedness. Overall leverage at the end of Q1 in 2017 grew at a slower pace than previously. As a result, the extension of credit to the non-financial sector increased from 250% of GDP in Q1 of 2016 to 258% in Q1 of 2017. Chinese banks’ leverage declined for the first time in seven years as the Government’s campaign to curb risks in the $40 trillion financial system started to make an impact. Corporate leverage has also declined slowly in the past three quarters. As deleveraging efforts to curb financial risks and achieve rebalancing continue, private investment is likely to lose more steam. The effects of the slowly declining leverage along with the cooling real estate sector and tighter monetary measures will become more apparent from the second half of 2017 through to 2018. A factor that may boost progress is the rising level of corporate profits, as they are providing Chinese policymakers with room to do more to deal with debt problems without inflicting major damage on the economy.

In other countries, such as India and Indonesia, deleveraging initiatives are ongoing, including debates about the creation of “bad banks”, and the climate is still not fully conducive for investments to thrive. In Indonesia, credit data showed a decline in growth from 12% in January 2017 to 4.12% in July 2017, even though the central bank has held the policy rate at the historically low level of 4.25%. Other countries, such as the Republic of Korea, are showing signs of a gradual increase in investments, helped by an improvement in global trade (figure 1). In the Russian Federation, investments recovered mildly after a three-year contraction, but further growth may be hampered due to new sanctions restricting access to financial markets. In Pakistan, investments grew and business sentiment improved in a climate characterized by low interest rates and increased infrastructure spending, with the bulk of private sector credit being extended to fixed investments. In reiterating the point made previously and highlighted in the Survey for 2017, if Asia-Pacific economies want to sustain their current economic growth momentum, they will need to keep investment growth high enough to generate productivity gains, real wage growth and employment creation. In this vein, an important consideration is boosting public sector investment to crowd in private investment.

Public sector spending and fiscal stimulus packages remain significant in the region, as large public infrastructure outlays have partially offset weak private investment. In Turkey, outlays on construction, where big-ticket projects were backed by the Turkish Government in public-private partnerships, have increased by 25%. Thailand is pursuing its public infrastructure development plan, which is worth $25.2 billion (equivalent to 6% of total GDP). In China, infrastructure investments have been remained significant as part of public spending despite ongoing deleveraging efforts. India’s growth in the first quarter of the year was also driven by government spending, although the...
country is making efforts towards a fiscal consolidation plan. In the Russian Federation, however, ongoing fiscal consolidation is expected to constrict public spending on infrastructure, while sanctions have placed restrictions on access to financial markets that may limit potential foreign direct investment. (Further discussion on the role of the public sector in supporting economies is provided in the fiscal policy section.)

In the external sector, export and import volumes are showing a clear uptick in 2017, which has contributed to an upward revision in the region's economic growth outlook (figure 6). Steady growth in manufacturing PMI and industrial output in the first half of 2017 indicate strong demand both domestically and from abroad, with high-technology manufacturing rapidly expanding. For instance, since mid-2016 exports in electronics have increased by 15% in Malaysia. Thailand benefited from steady growth in tourism and stronger merchandise exports in 2017. Indonesian exports also improved thanks to a rebound in the prices of key commodities, such as coal, palm oil and rubber. The Islamic Republic of Iran is also benefiting due to the lifting of sanctions.

In the Russian Federation, higher oil prices and increased external demand boosted the value of exports, peaking at a six-year high in January 2017, although their net contribution to growth was small because imports also rose as domestic demand picked up; however, the appreciating rouble may constrain the country's export performance.

Despite strong export performance in the region, the contribution of net exports to economic growth is negative in some countries, which reflects increased imports of capital goods in line with strong public investment. Widening trade deficits can lead to vulnerabilities for some economies and therefore should be monitored. For example, Pakistan’s current account deficit has increased rapidly, reaching $12.1 billion in fiscal year 2017 (approximately 4% of GDP), due to lower volumes of commodity exports, increased imports of capital goods related to both the China-Pakistan Economic Corridor (CPEC) and non-CPEC infrastructure projects. Similarly, in India the contribution of net exports to economic growth was negative in Q1, which is partly attributable to the recent appreciation of the Indian rupee. As was the case in other countries, India’s growth in exports may improve but strong domestic consumption may lead to an increased demand for imports - a stronger rupee could lower India’s export competitiveness as well.14

Two factors explain the recent uptick in export and import volumes. First, there was better economic performance in the Euro area and the United States. In 2017, consumer confidence in the Euro area rose to record levels last observed prior to the 2007/08 global financial and economic crisis, as accommodative fiscal and monetary policies and relatively lower policy and political uncertainty paved the way for improved market confidence and investments. In the United States, economic growth in Q2 of 2017 rose at the fastest pace in two years, primarily due to stronger household spending and larger gains in business investment, with unemployment being at its lowest level in six years. Growth in global merchandise trade volumes has been projected at 3.6% in 2017 compared with 1.3% in 2016.15

**Figure 6. Year-on-year export and import growth, in volume terms**

![Figure 6. Year-on-year export and import growth, in volume terms](image-url)

Second, within the region, stronger trends in China’s trade have contributed to intraregional economic growth momentum (figure 7). In 2017, the volumes of exports and imports for the Asia-Pacific region have been projected to grow by 4.5% and 8%, respectively (ESCAP, 2017b). Notably, China’s import demand grew by 18.9% in the first half of 2017 compared with the same period in 2016. This rise is attributable to increased demand for inputs to produce exports, which grew by 8.5% in the same period. As part of China’s rebalancing efforts, the manufacturing bases and supply chains in the region are shifting. Viet Nam is an example, as many firms consider it as an alternative to China (where wages are rising) in such sectors as manufacturing.\(^{16}\)

The rising prominence of domestic demand and intraregional trade underscores the importance of enhancing regional economic cooperation and integration in the region. There have also been bilateral initiatives to reach agreements that could potentially enhance trade. For instance, in September 2017 Cambodia and Thailand vowed to achieve bilateral trade targets and agreed to open four additional border checkpoints. Other liberalization measures have been taken unilaterally. Notably, in Uzbekistan several important measures are in the process of being adopted to liberalize foreign exchange operations, such as allowing private individuals to buy foreign currency.\(^{17}\) While all such initiatives are in principle commendable, the ideal option would be unilateral opening within multilateral frameworks, as bilateral initiatives could exacerbate the negative effects of the “Noodle Bowl”.\(^{18}\)

With a combined GDP of $27.25 trillion that is growing at a significantly higher pace than that of the rest of the world, Asia and the Pacific is well on its way to becoming the largest market in the world, opening possibilities for further expansion of trade and investment within the region. The expansion of trade and investment within the region, however, needs to be consistent with the principle of leaving no one behind. For that purpose, the focus should be on regional blocs that are less integrated, such as that of South and Central Asia, as well as on the least developed countries, landlocked developing countries and small island developing States. Furthermore, such expansion must be consistent with the Sustainable Development Goals of the 2030 Agenda in contributing to social progress and environmental sustainability.

In looking forward, trade growth in the Asia-Pacific region is projected to be somewhat restrained in 2018, with export and import volumes expected to grow by 3.5% and 3% respectively (ESCAP, 2017b). There are several reasons for this moderation. First, the recent uptick in trade growth in 2017 is measured against weak performance in 2016. Thus, a high “base effect” is likely to kick in for 2018. Second, given that intraregional trade takes up more than half of total trade means that intraregional demand plays a key role in sustaining trade recovery, especially from China as a quarter of intraregional trade takes place with that country. In view of the likely marginal slowdown in China’s GDP growth in 2018 due to ongoing structural reforms, its import demand may moderate as well, leading to a slight

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**Figure 7. China’s import growth, by origin**

![China's import growth, by origin](image_url)

decline in intraregional demand for imports. Third, protectionism can still hinder long-term trade and investment. In the past few years there has been a considerable rise in the backlash against globalization and its perceived negative implications for national economies. On average, for each liberalizing trade measure that Asia-Pacific economies have implemented between 2014 and 2017, an average of 3.7 restrictive measures were adopted. Given the recent 2017 uptick in exports and imports, however, it seems that such protectionist measures have not had a substantial constraining impact. Nevertheless, there is a risk that a consistent revival in exports and imports may be adversely affected due to protectionist measures, such as sanctions, non-tariff measures or even tariffs.

Inflation

The average headline inflation in the developing countries of Asia and the Pacific, 3.5% in 2016, is moderate and expected to decline further to 3.2% in 2017 (table 2). Compared with the projections reported in the Survey for 2017, this updated forecast represents a downward revision of 0.6 percentage points. Subdued inflation compared with historical trends is partially explained by stable and somewhat declining global commodity prices, 

Table 2. Inflation in selected subregions/countries/groups in the Asia-Pacific region, 2016-2018

<table>
<thead>
<tr>
<th>Subregion/country</th>
<th>Inflation (percentage)</th>
<th>Change from that recorded in the Survey for 2017 (percentage points)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Developing ESCAP economies</strong></td>
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</tr>
<tr>
<td>East and North-East Asia (excluding Japan)</td>
<td>3.5</td>
<td>3.2</td>
</tr>
<tr>
<td>China</td>
<td>2.0</td>
<td>1.6</td>
</tr>
<tr>
<td>Republic of Korea</td>
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<td>2.0</td>
</tr>
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<td><strong>South-East Asia</strong></td>
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<tr>
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<tr>
<td>Philippines</td>
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<td>3.1</td>
</tr>
<tr>
<td>Thailand</td>
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<td>0.7</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>2.7</td>
<td>3.7</td>
</tr>
<tr>
<td><strong>South and South-West Asia</strong></td>
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<td>6.1</td>
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<td>Bangladesh</td>
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<td>India</td>
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<td>Iran (Islamic Republic of)</td>
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<td>10.5</td>
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<td>Sri Lanka</td>
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<td>7.5</td>
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<td><strong>Landlocked developing countries</strong></td>
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<td>8.2</td>
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<tr>
<td><strong>Small island developing States</strong></td>
<td>4.1</td>
<td>5.1</td>
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Notes: 

- Estimate.
- Forecast (as of 31 October 2017).
- Fiscal year from 1 July 2016 to 30 June 2017.
- Fiscal year from 1 April 2017 to 31 March 2018.
particularly for metals and minerals, and for the cost of energy (figure 8). Inflation is expected to increase to 3.6% in 2018 (table 2), reflecting the lagged impact of the current increase in economic activity, while transient factors, such as lower food prices due to abundant recent agricultural production, will dissipate in going forward.

Country-specific circumstances also help to explain the evolution of prices, especially in the absence of large swings in energy prices. In China, headline inflation moderated in the first eight months at 1.5% compared with 2% in 2016. This moderation reflects a slowdown in the growth of house prices in large cities due to restrictions on home purchase. Food prices, however, have risen since the beginning of 2017. In India, inflation is expected to be 3.5% for 2017, down from 4.6% in 2016. This decline is the result of the prolonged effects of demonetization, which adversely affected consumption, and a decline in food prices due to a bountiful agricultural harvest and the consequent decline in the prices of grain and pulses.

In net commodity exporters, such as Azerbaijan, inflation has “normalized”, that is, it has receded after a few years of very high inflation caused by the 2014 plunge in oil prices (as those countries’ external sector deteriorated, their exchange rate depreciated, which in turn pushed up prices). Similarly, in the Russian Federation, inflation fell from a yearly average of 7.1% in 2016 to 4.1% in the first nine months of 2017; a robust harvest of agricultural products and a strengthened rouble also helped.

Similarly, in Bangladesh inflationary pressures eased towards the end of the fiscal year as global oil prices stabilized, non-food inflation declined and food inflation was kept at bay due to a decent harvest in the agricultural sector.

This historically low and stable rate of inflation, especially in the South and South-West Asian subregion, against steadily increasing economic growth and an accommodative monetary policy, may seem somewhat puzzling. Specifically, the recent boost in external demand is facilitating economic growth in the region, and countries continue to maintain their expansionary monetary stances. Yet strong consumption is not driving up inflation. In fact, there are countries, such as Indonesia, where policy rates were reduced several times in 2016 and 2017, but low inflation persists; in the case of Indonesia, it even declined in August 2017. This seemingly counterintuitive pattern can be explained by five factors.

First, country-specific factors, such as good harvests, represent a positive supply shock and can explain the low-price pressures, especially in developing countries where food is a hefty component in the CPI basket. This has happened in Bangladesh, India, Pakistan and Thailand, where the current year’s harvest has been plentiful.
Second, currency appreciation in some countries, such as India, and in commodity exporters that are still recovering from recent significant depreciations, such as Azerbaijan, or from foreign exchange rebalancing, such as the Russian Federation, have greatly eased price pressures through cheaper imports.

Third, inflation typically increases rapidly when actual economic output goes beyond its estimated potential level. In the Asia-Pacific region, however, there is still significant slack capacity that has remained unused since the 2008 global financial and economic crisis; that is why countries are undertaking reforms and tackling overindebtedness. A factor that supports this explanation is the weak growth in real wages and slower creation of jobs. As firms are still deleveraging and addressing overcapacity, they are not investing and hiring, or feeling the need to raise wages of existing workers. In other words, it is still too early for the region’s economic growth to result in higher prices.

Fourth, in terms of long-run regional and global trends, more structural explanations can be posited. Arguably, rapid globalization during the past few decades has resulted in global value chains helping meet demand at lower costs (that is, a global positive supply-side shock), thus keeping costs contained and inflation low. The globalization argument would suggest that global factors have become more important in explaining inflation than domestic factors. This situation has implications for the role of domestic monetary policy having a considerable impact on inflation or on the economy, thereby eroding its function at the national level. Some policymakers argue, however, that basic correlations on headline inflation are too simplistic, and that domestic factors are still the main drivers of inflation; therefore, the role of monetary policy in influencing domestic inflation by individual central banks remains pertinent (Carney, 2015).

Finally, and in the spirit of medium-to-long-run trends, it can be argued that production processes are increasingly demanding less labour because humans are being replaced by robots. Hence, the remuneration of labour (wages) is stagnating, a phenomenon that becomes more important when labour is in abundance and unskilled, such as in developing countries with high birth rates and poor education systems. This situation leads to high structural unemployment and low pressure on wages and prices.

All five factors put together explain the current phenomenon as to why inflation is not inching up and is rather stable. Indeed, the short-run explanations (namely, abundant harvests, recovery from episodes of hyperinflation and economic recovery that is still incipient) would seem to be in accordance with 2017 data. More evidence and research is needed though, especially because a thorough understanding of the phenomenon is vital to devise appropriate policies. For example, to the extent that globalization plays a significant role in the evolution of inflation at the national level, the role of national monetary policy would have to be carefully re-examined. On a slightly different yet related note, monetary policy frameworks probably need to be revisited as well in order to see what additional potential role, if any, they can play, and how they can support the 2030 Agenda for Sustainable Development. For instance, is there, or should there be, a role for monetary policy in mitigating high levels of inequality?

This section of the Update for 2017 provided an overall view of the current assessment of economic growth and inflation in Asia and the Pacific, emphasizing that the growth has been stronger than expected (thus pushing up the forecast slightly), while inflation remains subdued. To better understand the dynamics and sustainability of growth trends, each component was analysed as well. Despite the recent uptick in trade, which has contributed to stronger-than-expected performance, economic growth remains driven by private consumption. This is facilitated by low and stable inflation, which in turn is due to abundant harvests, recovery from episodes of hyperinflation and still relatively nascent economic growth momentum.

Over time, however, relying excessively on private consumption alone to sustain economic growth can be problematic. For economic growth to be stable throughout 2018 and beyond, growth in productivity and real wages must increase. To facilitate such growth, private investment must be stronger. However, at the same time, some countries are still grappling with high and rising private debt. How can stronger investment be promoted while avoiding financial vulnerabilities?

In the next section, policy considerations are explored that can be used to address such concerns: monetary policy and financial stability measures, and the role of fiscal policy and structural reforms. Furthermore, this section of the Update embeds the spirit of the Agenda 2030 and goes beyond the economic dimension and incorporates selected social and environmental perspectives as well. The key issues highlighted consider some important questions: Is the stronger economic growth in the region being translated into the creation of decent jobs, attenuating inequality and improving environmental sustainability? What can Governments do...
about these issues, especially from the fiscal policy perspective?

1.2. Policy considerations

1.2.1. Monetary policy and financial stability

Against a backdrop of stable inflation, policymakers continue with the expansionary monetary policy stances adopted in recent years. Specifically, accommodative monetary measures were introduced most notably in 2014 and 2015. Some economies, such as India and Indonesia, have continued with further reductions in policy rates, while others are following a wait-and-see approach by keeping policy rates unchanged (figure 9). In some countries, the current policy rates are even lower than during the 2007/08 global financial and economic crisis when dire economic conditions called for drastic reductions in policy rates around the globe. Other than lowering policy rates, some countries lowered the required reserve ratio as well, such as China in September 2017.

The objective of these accommodative monetary policy measures has been to stimulate economic growth; stable inflation in most economies made this policy option easier. Consequently and as noted previously, consumption has been boosted to become the major driver of current economic growth, although this has been accompanied by rapid increases in household debt in several economies. The impact of expansionary monetary policies on fixed investment has been mixed, however, as credit extension by banks and debt accumulation by the corporate sector cannot take place endlessly, especially if there is slack in productive capacity.

Indeed, private debt has increased rapidly in recent years; it has become a source of concern for policymakers in some economies, both at the corporate level, such as in India and China, and at the household level, especially in Malaysia, the Republic of Korea and Thailand (figure 10). For instance, in the Republic of Korea household debt in 2016 was at the highest level in the region at 95% of GDP (whereas it was 76% of GDP in 2007); the ratio of household loans in total loans rose from 27.7% in 1998 to 43.4% in 2016 (Choi, 2017). In Malaysia, household debt as a share of GDP grew from 64% in 2007 to 88% in 2016. At 80% of GDP in 2016, having increased from 52% of GDP in 2007, Thailand’s high household debt is a source of risk for banks. Similarly, by the end of Q1 of 2017, total private debt in China was 210.8% of GDP; households accounted for 45.5% of GDP; the corporate sector, 165.3% (government debt was equivalent to 46.9% of GDP).

While private debt levels tend to rise with higher incomes, a rapid pace of increase in a relatively short period can lead to financial vulnerability. Such an increase

Figure 9. Policy rates in selected economies in Asia and the Pacific

![Policy rates in selected economies in Asia and the Pacific](image-url)

also poses the risk of a banking crisis. Evidence suggests that, while a rise in household debt can boost economic growth in the short run, it makes economic growth three to five years down the line lower than it would otherwise have been (IMF, 2017). For politicians who depend on votes, the incentive structure can be problematic: it has been persuasively argued that democratic political systems frequently turn to credit expansion as a substitute for creating real prosperity (Rajan, 2011).

The normalization of monetary policy, including hikes in interest rates in the United States or other advanced economies, could also have negative impacts on household and corporate borrowings in the region. Such economies and those with currencies pegged directly to the United States dollar, such as Hong Kong, China; and Singapore, would be much more prone to these negative impacts than others. The normalization of monetary policy might also result in capital outflow and exchange rate volatility, which could have a negative impact on developing economies in the region, especially those with high external debts and low levels of reserves, such as Indonesia and Sri Lanka.

Rapid increases in private debt and associated issues can easily affect whole financial systems, as happened 20 years ago as a result of the 1997 Asian financial crisis (box 1). Currently in Tajikistan, four banks are facing a liquidity crisis due to bad debts in the banking system. In Bangladesh, eight State banks had a capital shortfall of 126.8 billion taka (approximately $1.55 billion)\textsuperscript{24} at the end of June 2017 (Byron, 2017). In India, defaults on corporate bonds and syndicated loans are at the record level of almost $2 billion as of August 2017 compared with $494 million for all of 2016. The State Bank of India, the country’s largest lender in terms of assets, recently reported that bad loans had risen to 10% of the bank’s liabilities following the acquisition of smaller lenders (Mundy, 2017). Total non-performing loans in India have risen from 5.9% of total loans in 2015 to 9.2% in 2016; currently, bad loans amount to $180 billion in value (Winkler and Antony, 2017).

Some countries are putting in place measures to address high leverage and strengthen financial stability. In China, monetary policy remains focused on slowing excessive credit growth by tempering speculative non-bank credit and deleveraging public sector debt through various mechanisms, such as the restructuring of State-owned enterprises. In the Republic of Korea, the Financial Services Commission is prepared to gradually introduce tougher rules for home-backed lending and will lower the maximum legal lending rate to 24% starting in 2018 to help ease financial burdens for borrowers.\textsuperscript{25} Similarly, the Bank of Thailand has tightened rules governing credit cards and personal loans in order to curb overspending and further expansion of household debt, including by cutting the ceiling interest rate to 18% on credit cards debt.
Box 1. Twenty years after the Asian financial crisis

The year 2017 marks the twentieth anniversary of the Asian financial crisis, which had profound effects on macroeconomic policy and regional cooperation in Asia and the Pacific, especially in South-East Asia. The major crisis-affected economies were Indonesia, Malaysia, the Republic of Korea and Thailand, although the crisis also dampened economic growth in several other Asian economies, such as Hong Kong, China; the Philippines; and Singapore. The crisis was caused primarily by burgeoning macroeconomic and external imbalances, and financial and corporate vulnerabilities, such as foreign debt-fuelled business investment. Loose prudential regulation and supervision exacerbated the vulnerabilities leading to the crisis. Since that crisis, the region’s macroeconomic fundamentals have improved, and progress has been made towards achieving financial stability. These factors have helped emerging Asian economies to benefit from a long period of financial stability, including during the 2007/08 global financial crisis. Some policy measures that made this progress possible were:

(a) Better monetary policy and macroeconomic management. The move towards more flexible exchange rates increased the space for and effectiveness of monetary policy to address inflation and related domestic imbalances. For instance, in 1996, the year before the Asian financial crisis began, the current account deficit in the crisis-affected economies amounted to 3.4-8% of GDP, while foreign exchange reserves were equivalent to only 2.5 months of imports. Since then, these economies have enjoyed sizeable current account surpluses or much smaller deficits in recent years, and foreign exchange reserves are at comfortable levels;

(b) Strengthened macroprudential regulation and supervision. To achieve greater financial stability, the crisis-affected economies closed or merged financial institutions, introduced new laws and financial supervisory agencies and promoted transparency and data disclosure. Such policy changes helped reduce the share of non-performing loans from its peak of 19-49% of total loans in Indonesia, Malaysia and Thailand in 1998 to less than 2.9% (Indonesia) and 3% (Thailand) in 2016;

(c) Increased regional financial cooperation. Countries have also worked more closely on regional financial cooperation to help cushion future shocks. A key example is the Chiang Mai Initiative, which was started in 2000 as a series of bilateral swap agreements among ASEAN+3 countries to address balance of payments and short-term liquidity issues. The initiative became a single, multilateral agreement in 2010; the current size of the fund is $240 billion.

Source: ESCAP, based on World Bank data.

Note:  
\(^{a}\) Average of 2014-2015 for Malaysia and Thailand.  
\(^{b}\) Data from 1999 instead of 1998.  
\(^{c}\) Data from 2014 instead of 2016.
Despite the commendable progress made, potential sources of financial vulnerabilities remain. Structurally, an effort to diversify sources of financing beyond traditional, dominant bank finance has produced mixed results. On debt instruments, while the size of the local currency corporate bond market is quite large at 45-75% of GDP in Malaysia and the Republic of Korea, the ratio is lower at 20% in Thailand and only 3% in Indonesia. The small size is exacerbated by low levels of market liquidity and relatively short maturity periods. On equity instruments, Indonesia’s stock market capitalization remains relatively small and has remained largely unchanged over the past two decades at close to half of GDP.

Another source of financial vulnerability is high private sector debt. In 2016 corporate and household debts amounted to 122%-195% of GDP in Malaysia, the Republic of Korea and Thailand. In all three economies, private sector indebtedness in 2016 increased relative to that of 2007, especially household debt in Malaysia and Thailand. Available data also suggest that debt repayment ability is lower among individuals and companies with larger debt burdens.

Maintaining financial stability in Asia remains a challenging task. Rising private sector debt in the region comes at a time when global economic uncertainty is high and interest rates in major developed economies, particularly the United States, are on an upward trend. Nonetheless, the risk of a sharp reversal of portfolio capital inflows remains, especially if geopolitical tensions in the region surge. Finally, rising intraregional trade and financial linkages call for greater vigilance and cooperation among policymakers in the region.

Nevertheless, in the context of low inflation and weak investment, policymakers still see room for policy rate reductions to support economic growth. During 2017, monetary easing was conducted in some countries, such as the Russian Federation (in September 2017, it reduced the policy rate by 0.5 percentage points to bring it down to 8.5%) and Viet Nam (in July 2017, it reduced the policy rate by 25 basis points to set it at 6.25%). Such easing was carried out even in economies with high indebtedness, such as India and Indonesia. In August 2017, the Reserve Bank of India cut the policy rate by 25 basis points, lowering the repurchase rate to its lowest rate in 6 years. The rate cut was justified by a growth slowdown in Q1 of fiscal year 2017/18 and low headline inflation. In Indonesia, the central bank surprised markets in August 2017 by cutting its benchmark policy rate (the first change since October 2016, and it was followed by another cut in September 2017) to boost sluggish lending and economic growth.

When prospects of investment are weighed down (due to too much debt) and non-performing loans are rising, the policy of trying to stimulate investment entails a trade-off. On one hand, central banks want to stimulate investment and economic growth; on the other, they do not want to encourage any more bad loans or promote “zombie companies”. According to the managing director of India’s Housing Development Financial Corporation Bank, “Getting rid of the country’s $180 billion of bad loans is crucial to reviving credit growth and investment in the Indian economy” (Puri, 2017). Hence, expansionary monetary policy must be accompanied by financial sector reforms to avoid a build-up of bad loans. Examples of these reforms can be, on the demand side, credit registries with deep levels of information on borrowers; on the supply side, implementation of capital adequacy ratios, such as Basel III, thus affecting both supply and demand, and an efficient court system that can effectively settle financial disputes.

Another important economic variable that influences a country’s monetary policy stance is the exchange rate. In 2017, most of the currencies in the region strengthened (figure 11). Overall, strong economic and financial fundamentals continue to attract capital inflows into the region’s economies, while low inflation is providing foreign investors with incentives to extend their portfolio duration. One of the currencies that has appreciated most is the Thai baht. The situation has raised some concern about the potential for a negative effect on the country’s exports. In September 2017, the Bank of Thailand announced that it had relaxed curbs on capital outflows in order to widen overseas investment.

\[\text{Box 1. (continued)}\]

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\[\text{China, Japan and the Republic of Korea along with the 10 members of the Association of Southeast Asian Nations (ASEAN): Brunei Darussalam, Cambodia, Indonesia, the Lao People’s Democratic Republic, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Viet Nam.}\]
opportunities for local investors. This may help ease the current appreciation pressure on the baht.

The currency that is experiencing depreciating pressure most is the Philippine peso. In October 2017 alone, it depreciated by about 3.7% against the United States dollar. The efforts of the Philippines to build infrastructure has increased capital imports, thus worsening the country’s external position and increasing its reliance on foreign financing; this situation is amplifying the downside for the currency despite rising remittances.26

After significant outflows in 2015 and 2016 and pressure to depreciate the renminbi, Chinese authorities intervened in the foreign exchange market by selling United States dollars. This action led to some reduction in the country’s enormous foreign exchange reserves. Since late 2016, however, the country’s authorities have used capital controls to relieve the pressure on the renminbi and the need to intervene. In the first half of 2017, China’s cross-border capital flows stabilized and financial inflows strengthened, as market expectations for renminbi depreciation eased due to a weaker United States dollar. By September 2017, China’s foreign-exchange reserves posted a seventh straight monthly increase and the renminbi strengthened, which suggests that pressure from capital outflows has largely subsided.27 It has been estimated that most of the increase was due to valuation effects, with the People’s Bank of China likely having had little or no need for intervention (Evans-Pritchard, 2017).

The current strength of Asian currencies is unlikely to last long, as advanced economies are normalizing their monetary policies by gradually increasing interest rates from historically low levels, and folding up their quantitative easing measures. Such measures have been widely anticipated and thus are unlikely to lead to any sudden movement of capital and/or exchange rates. Nevertheless, it is important to monitor such developments closely, especially in economies that have vulnerable external positions, as those factors could lead to a strengthening of the United States dollar in global markets. For instance, Pakistan’s current account deficit reached $12.1 billion (approximately 4% of GDP) in fiscal year 2017 due to lower volumes of commodity exports and higher capital imports. The authorities are keeping the exchange rate stable by intervening in the foreign exchange market, which is leading to a reduction in the country’s foreign exchange reserves. In these circumstances, if the United States dollar appreciates against most major currencies in global markets, the policy approach currently being pursued by Pakistan could become unsustainable.

For the region as a whole, given the low and stable rate of inflation, monetary policy is expected to maintain its accommodative stance and provide support for

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**Figure 11. Recent evolution of currencies in the Asian and Pacific region**


Note: A positive trend represents appreciation, and vice versa.
economic growth. However, central banks need to pay close attention to financial and external sector stability issues as well and continue with their deleveraging efforts to tackle the build-up of systemic risks. Strengthening macroprudential frameworks, regulation and supervision should therefore be a priority. While measures such as financial institutions’ liquidity requirements are already in place, other options could include: (a) limits to foreign currency lending, such as requiring more capital and tighter loan-to-value and debt-to-income ratios for foreign currency loans; (b) maximum loan-to-value ratios to reduce systemic risk from “boom-bust” episodes, including in specific sectors, such as real estate; (c) enhanced capital adequacy ratios; (d) better credit registries and reforms to make the court system more effective in handling financial disputes; and (e) dynamic provisioning, whereby banks set aside money to cover loan losses when credit losses are relatively low so that bank balance sheets would be better prepared to absorb losses during downturns.28 Furthermore, in the choice and design of the different policy options available, a central element to keep in mind should be the complementarity of monetary and fiscal policy, a topic which is explored next.

1.2.2. Fiscal policy

In the current context of weak investment and limited space for further monetary easing, fiscal policy can continue playing an active role in lifting domestic demand, “crowding in” private investment and supporting development priorities, such as social protection. Its effectiveness depends critically on good governance, as emphasized in the Survey for 2017. Compared with other parts of the world, the Asia-Pacific region has relatively low government expenditures as a share of GDP, but revenues are also low. This situation has resulted in some concern over fiscal space - how much countries can stretch the national budget to support development priorities without risking fiscal sustainability. (The following section will contain some preliminary discussion on recent fiscal developments.)

Recent fiscal developments

As background, in 2015 and 2016 overall fiscal balance in the region deteriorated as global trade was unusually weak and commodity exporters experienced large terms of trade losses. The cyclically adjusted overall fiscal balance (an estimated balance assuming that the economy is at a “normal” level of activity) and the primary balance (fiscal balance net of interest payment) in the region exhibited similar trends (figure 12).29 The government debt-to-GDP ratio rose marginally over the past decade, from 33.5% to 36.7%, reversing the previous declining trend but still remaining at a manageable level. In 2017, major economies in the region continued to pursue generally expansionary fiscal policies. Based on official targets and estimates, the fiscal deficit in the region in 2017 is projected to stabilize at about 3% of GDP on average.

China maintained an expansionary path in 2017, carrying over the fiscal deficit target of 3% of GDP from 2016, when the actual on-budget deficit was 3.7% (China, Ministry of Finance, 2017). This was due to wide-ranging tax cuts as well as a modest increase in government spending, including for infrastructure projects (State

![Figure 12. Fiscal position in Asia and the Pacific](image-url)


Note: Numbers in parentheses indicate the number of countries, based on which the median is presented.
Council of China, 2017c). Such fiscal stimulus has contributed to investment and output growth, mitigating some of the short-term drag on activity resulting from structural reforms. However, the expansionary stance and perceived slow progress in addressing local government debt and contingent liabilities triggered a credit rating downgrade on long-term sovereign debt. Currently, China’s gross general government debt remains relatively low, and net assets are estimated at 80% of GDP. Fiscal management has also improved with the revision of the country’s budget law in 2014 and the complete transition to value-added taxes in 2016.

Box 2. India’s goods and services tax

On 1 July 2017, India replaced various central and State-level indirect taxes in favour of a simpler, nationwide goods and services tax (GST), which is expected to enhance tax compliance and thereby strengthen the country’s fiscal position, while boosting economic growth over the medium term by making Indian industries more competitive. The need for such reform had been recognized for decades, but implementation was elusive until the passage of the relevant constitutional amendment in September 2016, after which the Goods and Services Tax Council was established to determine a rate structure and revenue-sharing arrangements.

GST is essentially a value-added tax (VAT), the key feature of which is credit or refunds furnished to registered VAT taxpayers on tax that they have been charged on their purchases. This approach minimizes tax cascading and distortions on production decisions. India replaced general sales tax laws with the Value Added Tax Act in 2005, but stringent rules for claiming tax credit and different tax rates imposed by the central Government and 29 states left the system without fundamental changes, and it remains extremely complex.

GST subsumes almost all the existing indirect taxes into a unified structure wherein the same rates are applied on the same base across the country. Compared with the old VAT, the new GST provides input tax credits for a wider range of capital goods. It has been estimated that this channel alone would increase GDP by half a percentage point. Reduction in tax complexity will also help attract direct foreign investment and boost domestic and international trade. GST simplifies interstate duties and provides exporters with a full refund of duties and taxes. This arrangement could result in significant additional increases in GDP, especially if accompanied by reduced logistical costs related to interstate transportation.

Although the GST rates were chosen to be revenue neutral, there is a compelling case that the GST could contribute to higher tax revenues in the long run. GST significantly expands the scope for the Government to verify invoice matching, which could significantly improve tax transparency and compliance. Over the medium term, the GST electronic platform could also reduce the number of hours that firms spend on filing taxes. Moreover, GST marks important progress in fiscal federalism. Designing an “optimum” indirect tax in federal systems is inherently challenging, and India’s GST is designed to strike a balance between harmonizing the tax structure and continuing to provide the country’s states with some fiscal autonomy.

Nevertheless, there is scope for further study and improvement over the medium term. Compared with most other countries which have opted for a single rate, India’s GST has a multirate structure – the key rationale being equity considerations. For instance, more than 80% of goods of mass consumption are either exempt or taxed under a 5% slab, while high-end goods fall under a 28% slab, with an additional cess being applied on certain luxury goods; most other goods and services fall under the two “standard rates” of 12% and 18%.

This multirate structure makes the tax system less efficient and more susceptible to leakages. Moreover, given that in absolute terms the rich still consume more of exempt or low-rated goods and services than other social classes, little progressivity is achieved and at a huge loss of revenue. An important question is whether the Government could use tax and transfer mechanisms other than indirect taxes more effectively for redistribution purposes. The implementation of direct benefit transfers using biometric identity holds promise. GST could also help improve tax compliance in income and wealth taxes, which are deemed more progressive.

India is pursuing a gradual consolidation path, with the central Government targeting a fiscal deficit of 3.2% of GDP for fiscal year 2017/18, smaller than the actual deficit of 3.5% in the past two years but larger than the 3% recommended by the Fiscal Responsibility and Budget Management Review Committee (India, Ministry of Finance, 2017c; 2017b). This was a balancing act, as the implementation of the demonetization initiative and the new goods and services tax weighed on immediate economic activity despite their expected medium-term benefits (see box 2). The general government deficit is estimated to have widened, however, in part due to debt restructuring of State power distribution companies through the UDAY programme. Under the Government’s medium-term fiscal strategy, the debt-to-GDP ratio is expected to stabilize at between 68.6% and 60% by fiscal year 2022/23 (India, Ministry of Finance, 2017a). Various fiscal reforms are under way, including tax reforms, phasing out of fuel subsidies and adoption of direct benefit transfers (India, Ministry of Finance, 2016).

In Indonesia’s revised 2017 budget, a fiscal deficit of 2.9% of GDP was targeted, just below the 3% legal limit, although the actual deficit will likely be lower due to stronger revenues from higher commodity prices and the country’s tax amnesty programme, which resulted in collection of additional taxes and fees equivalent to 10.5% of 2016 tax revenues. The Government intends to increase the tax-to-GDP ratio from the current level of 10.4% to 16% by 2019 through tax reforms, including international tax cooperation to stem cross-border evasion. The emphasis of the draft 2018 budget is on inclusive growth and spending quality, including through wider coverage or higher benefit level of existing cash transfer and scholarship programmes for low-income families. Infrastructure investment, for which State-owned enterprises are being mobilized, may receive a further boost from the country’s recent credit rating upgrade.

**Fiscal sustainability: a preliminary assessment**

The developmental role of fiscal policy has received renewed attention in recent years (ESCAP, 2013). Various estimates point to significant financing needs and gaps in meeting the 2030 Agenda, as will be discussed subsequently in the Update. Although a share of the financing needs could potentially be privately financed, most countries in the region would require additional public financing – which is why the issue of fiscal space becomes so important.

Fiscal space is a complex concept with alternative definitions. Moreover, different measures of fiscal space, or debt sustainability, could provide different pictures. For instance, a Government’s long-term debt service capacity could be proxied by GDP or alternatively, tax revenue, over which it has more control. Table 4 shows that Indonesia’s government debt-to-GDP ratio is among the lowest in the world at 28%, but the debt-to-tax revenue ratio is on par with such countries as the Republic of Korea and Thailand. Fiscal space also depends on how much buffer would be desirable against possible shocks, such as in terms of global interest rates or exchange rates in the case of external debt or debt denominated in foreign currencies.

A popular approach to measuring fiscal space is to calculate the “fiscal gap”, defined as the difference between the current fiscal balance and the constant balance that stabilizes debt over a medium-term horizon at a sustainable level. The sustainability of government debt depends not only on the primary balance but also on the differential between economic growth and borrowing costs. Thus, even Governments with persistent deficits can reduce their debt-to-GDP ratio if the economy grows at a sufficiently high rate. Conversely, even countries with surpluses can see their debt-GDP ratio increase with an economic slowdown - which is why fiscal austerity can be self-defeating. Slower economic growth was also behind the recent marginal increase in debt-to-GDP ratios in the Asia-Pacific region, as interest rates were stable or even trending downwards. In this situation, there is a need for fiscal sustainability analysis to incorporate the fiscal impact on economic growth.

Basic calculation of the fiscal gap would suggest that, despite fiscal deficits, if current economic growth rates are sustained, for most Governments of countries in the region debt-to-GDP ratios would stabilize in coming years (figure 13, left panel). As long as countries remain below the zero-horizontal line on the y-axis, their debt would be stable - even if they have a negative primary balance on the x-axis and are therefore in the bottom left quadrant. In other words, there is room for pursuing an expansionary fiscal stance without adversely affecting fiscal sustainability. However, what if economic growth slows or interest rates suddenly spike? Governments should be prepared for such alternative scenarios in the light of recent experiences, such as large terms of trade loss among commodity exporters or potential interest rate hikes prompted by capital flow reversals, as happened in some countries. In the figure, a one standard deviation shock to the differential between economic growth and interest rate is applied based on country-specific historical data for the period 1990-2016. Under this alternative scenario of a negative shock, to keep the debt ratio stable, fiscal policy would have to
Table 3. Selected indicators of fiscal space

<table>
<thead>
<tr>
<th>Country/area</th>
<th>General government debt (percentage of GDP)</th>
<th>General government debt (percentage of tax revenues)</th>
<th>Public external debt (percentage of GDP)</th>
<th>Concessional external debt (percentage of government debt)</th>
<th>External debt (percentage of exports plus remittances)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Afghanistan</td>
<td>8.3</td>
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<td>49.9</td>
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<td>13.3</td>
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Source: ESCAP, based on World Bank, Fiscal Space Database and other datasets, and ESCAP calculations.

Note: Figures shown are for 2016 or the latest year available. Public external debt includes publicly guaranteed external debt.
make up for less favourable growth performance, higher interest rates, or both. As a result, more than half the countries would then experience upward pressure on their debt ratios (figure 13, right panel), although many are still below the stable debt horizontal line.

Assuming steady economic growth, what might affect the interest rate? For an open economy with external debt or debt denominated in foreign currency, Governments also need to consider global interest rate and exchange rate developments. For least developed countries and others relying heavily on external concessional debt (table 3), it is also likely that interest rates would eventually increase with the graduation of such countries from “least developed” status and over time.

On the other hand, for most developing countries, interest rates on domestic debt tend to be much higher owing to the narrow domestic investor base, comprising mostly public and commercial banks and a few pension funds and insurers.

Figure 14 (top panel) shows the investor profile in respect of government bonds for selected ASEAN+3 economies. Local government bond markets have also developed in some countries, but they often suffer from low liquidity. Based on a survey among market makers, enhancing liquidity would require not only greater diversity in the investor profile but also transparency and hedging mechanisms, among various other factors (figure 14, bottom) (Asian Bonds Online, 2017).

While the fiscal gap approach is forward-looking and incorporates assumed policy plans, the role for feedback between fiscal policies and private sector behaviour tends to be limited. As previously noted, the fiscal impact on economic growth, or fiscal multipliers, does matter for debt sustainability. This would include potential “crowding in” of private investment through public investment, which would matter more in the current economic environment of weak investment. In assessing how fiscal policy affects economic growth, it is useful to distinguish between the short-term demand channel and the long-term supply channel, or the “level” and the “growth” effect.

There has been considerable interest in short-term fiscal multipliers in the wake of the 2008 global financial and economic crisis and the sovereign debt crisis. There has also been much rethinking on this issue, although interestingly, compared with the renewed enthusiasm for deploying fiscal policy in developed economies, policymakers and academics in developing countries seem more cautious. While the precise size and persistence of multipliers, and sometimes even the sign, remain subject to debate, commonly identified determinants of multipliers include the business cycle, the fiscal position, the type of fiscal instrument and response to monetary policy as well as traditional factors related to the structure of the economy, such as the marginal propensity to consume, the degree of openness and the exchange rate regime. In some studies, it was also found that financial depth increases the size of multipliers as there is less “crowding out” through interest rates.
Figure 14. Developing domestic or local-currency government debt markets

Investor profile in respect of government bonds

Raising liquidity in local currency government bond markets


Note: Upper panel: Contractual savings institutions include national provident funds, private pension funds and life insurance companies. Lower panel: In an Asian Development Bank survey, market makers from ASEAN+3 countries were asked about the importance of specific initiatives that could raise liquidity in local currency government bond markets; they were also asked to rate each as “very important” (4), “important” (3), “somewhat important” (2) or “not important at all” (1).
negative) in developing countries, suggesting that they could crowd out other demand components, at least in the short run. In contrast, most studies have found higher multipliers (often greater than 1) for public investment, confirming the potential “crowding in” of private investment. While this effect may not be surprising in the long run as public capital stock would increase the productivity of private investment, for instance by providing relevant infrastructure, such as electricity, roads and ports, the short-run explanation may be closely related to why private investment has been weak in recent years - that is, the situation may be due to the accelerator effect, where investment responds to changes in output and sales.

How government expenditures affect long-run economic growth is a different matter as the process concerns the supply side. Key factors to long-run economic growth, such as education, research and development and infrastructure, depend on public provision of such goods and services. In endogenous growth models, government expenditures could be categorized as “productive” and “non-productive”, and to account for how they are financed, taxes could be categorized as “distortionary” and “non-distortionary”. While just what falls under which category may be debatable, and fiscal policy serves purposes other than growth, redistribution for example, such models are useful for thinking about the developmental role of fiscal policy. As has been shown in some of these models, good governance and transparent and accountable institutions are critical for ensuring government effectiveness. Indeed, good governance has proven to be vital in successfully leading the structural reforms that enhance the supply side of economies.

1.2.3. Structural reforms

Structural reforms are measures aimed at increasing productivity; they are particularly relevant for the Asia-Pacific region as it undergoes further economic transformation amid profound shifts in the global economy and trade, technology and demographics. Interest in structural reforms increased in recent years amid the slowdown in productivity growth and the decline in potential growth. For developing Asia-Pacific economies, ESCAP (2016a) contained an estimation showing that growth in total factor productivity (TFP) declined by more than half between the periods 2000-2007 and 2008-2014 while growth in labour productivity declined by a third over the same time frame. Although cyclical elements may have contributed to this phenomenon, structural constraints in skills and infrastructure are holding back the productivity potential of the region. Furthermore, weak governance is undermining productivity-enhancing innovation and investment (ESCAP, 2017c). This situation is worrying because productivity levels in the region remain generally low (figure 15).

Figure 15. Labour productivity in developing countries in the Asia-Pacific region

![Graph showing labour productivity in the Asia-Pacific region](image-url)

Source: ESCAP, based on ILOSTAT data (accessed 9 October 2017).
Note: Labour productivity is measured by GDP per person employed (in constant 2011 purchasing power parity dollars). Compound annual growth rate is given for the period 2007-2016.
While the overall objective of structural reforms is to increase productivity, the question of which reforms to prioritize will depend on individual country circumstances and stage of development. Productivity payoffs of reforms could differ as countries close their gap with regard to the global technological frontier. It would seem to be suggested in empirical studies that, while trade liberalization and agricultural reforms are associated with higher productivity growth in low-income countries, banking system reforms and streamlining business regulations are particularly important for middle-income countries (Dabla-Norris and others, 2016).

Despite the trend in recent years of increases in new restrictive measures, countries in the Asia-Pacific region have implemented various trade liberalization measures (ESCAP, 2017b). Land reforms and rural infrastructure are contributing to higher agricultural productivity, although much more progress is needed. Banking sector reforms and insolvency laws are also helping to improve the efficient allocation of capital. The business environment is being improved through the easing of administrative burdens, including compliance with tax and labour laws, better infrastructure and more effective enforcement of contracts. Several countries, including China and India, are also taking a proactive approach to encourage startups by lowering the entry barrier in product markets. Progress has been relatively slow in terms of labour market reforms, where efforts are needed to both increase workers’ skills through effective training programmes and address outdated or excessive regulations that undermine the growth of jobs in the formal sector.

With globalization, however, structural changes in the economy and the productivity payoff of reforms are also determined largely by external circumstances, including developments in major manufacturing and trading countries, such as China. China’s ongoing shift towards consumption, services and high-technology industries has significant domestic and international implications. The country is moving up the value chain, increasing its capacity in new sectors while upgrading traditional sectors, as also reflected in its labour market through sectoral shifts in employment (ESCAP, 2016b). These developments are supported by various reforms on the supply side aimed at increasing productivity. Besides the near-term task of cutting overcapacity and deleveraging, in the pipeline are land reforms and mechanization to increase agricultural productivity, reforms to increase labour mobility both geographically and across sectors, gradual financial liberalization and measures to allow freer flow of capital and exchange rates. Such reforms, by improving the efficiency of resource allocation, are expected to help China sustain its economic growth even as the country undergoes rapid population ageing and a shrinking labour force.

Yet for most developing countries in the region, including India, expanding the manufacturing base to relatively labour-intensive sectors will be important for making broad-based productivity gains. This expansion is also tied to the countries’ ambition to become more integrated with global value chains and create more jobs to realize the demographic dividend. Such sectors as apparel and leather also offer tremendous job opportunities for women.

An important question is whether China’s move up will create space in manufacturing, which in the past has delivered both productivity gains and job creation but only in very few countries. For instance, China’s share in global manufacturing grew fivefold since the 1990s and reached 25% in 2015, while other countries realized much smaller gains or even declines (figure 16, left panel). Excluding China, the share of the developing Asia-Pacific region in global manufacturing stood at only 14% in 2015.

Whether this pattern will significantly change is an open question. While some relocation of production to lower-wage economies, such as Bangladesh and Viet Nam, are under way, the extent of relocation may be smaller than expected given China’s remaining surplus labour in inland provinces and its rapid adoption of labour-replacing industrial robots in assembly lines. Such new technologies as the so-called Internet of Things, advanced robotics and 3-D printing - which only a few countries are well positioned to adapt rapidly - may further reinforce this concentration, effectively making manufacturing a less accessible pathway for most developing countries.

1.2.4. Labour market and social protection

Even if countries secure more manufacturing activities, their labour intensity appears to have generally declined. Whereas the share of manufacturing in total employment used to peak at more than 20% in countries which currently enjoy a high income, this share has fallen to between 13% and 15% for a typical developing country today (figure 16, right panel). Meanwhile, skill-intensive service jobs, such as ICT, computer systems design, finance and other business services, exhibit relatively low employment shares. Such trends could result in greater job polarization and have adverse consequences for income distribution.
Therefore, Governments’ policies should be aimed at not only fostering innovation-led economic growth but also ensuring that the benefits of growth are widely shared. For instance, Governments could support industries that have dynamic linkages to other economic sectors, thereby stimulating broad-based productivity and employment gains. Enhancing industry-services linkages, as the availability of such cost-efficient services as distribution and business and logistics-related services, would be crucial for improving overall productivity. Similarly, Governments could promote technological diffusion across a wider range of firms, including small enterprises, while upholding intellectual property rights.

These actions are particularly important because the region’s steady economic growth is not leading to commensurate increases in real wages: available data show that real wages often grow less than the rate of economic growth and can even be negative: China (6.9%), Malaysia (4.0%), Thailand (2.8%), Republic of Korea (2.7%), India (1.0%) and Indonesia (–0.4%).

 Furthermore, 2017 data show that this growth is not being translated into a sizeable creation of decent jobs in the region (figure 17). In China, robust economic activity helped create an estimated 3.3 million jobs in Q1 of 2017, but recent growth in real wages has slowed (State Council of China, 2017a). In India, the relatively disappointing economic growth in 2017 so far has raised doubts about the economy’s capacity to create enough decent jobs to absorb its rapidly expanding labour force. In considering other developing economies, gains in employment growth were robust in Sri Lanka (3.3% year on year), an expansion spurred by an increase (11.5%) of 238,000 industrial jobs, which offset a contraction in agricultural employment. In Indonesia, employment increased annually by 3.3%, as sizeable gains in agriculture helped to counter a decline in construction jobs. In Malaysia, employment growth reached 1.8% in May 2017 (ILO, 2017). By contrast, in Viet Nam employment growth slowed to 0.1% due to declines in agriculture. Employment decreased by 1% in the Philippines owing to employment loss in wholesale and retail trade.

Given the relatively mixed trends in employment creation, unemployment in the Asia-Pacific region is expected to remain unchanged at 4.2% in 2017. During the first half of 2017, unemployment decreased very slightly in 8 of the 14 economies with available data, rising in only 4 of them (figure 18, left panel). The largest increase (0.5%) was in Singapore thanks to the services sector. Small increases (0.2%) were seen in the Republic of Korea and Thailand; in Macau, China, there was a rise of 0.1% (ILO, 2017). Moreover, unemployment is higher for women and youth in most economies (figure 18, right panel). The conditions and quality of work tend to be poor throughout the region as well. For instance, an estimated 925 million women and men in Asia and the Pacific are engaged as own-account workers or contributing family workers, equivalent to 47.8% of total employment (ILO, 2017).

Critical dimensions of the quality of work are its stability and security. Of countries with available data (Indonesia, Pakistan, Sri Lanka and Viet Nam), nearly one in four wage employees were employed casually, according to a recent study. Pakistan exhibited the highest rate of
Figure 17. Percentage change in employment in selected countries/areas in the Asia-Pacific region

![Graph showing percentage change in employment in selected countries/areas in the Asia-Pacific region]

Source: ILO estimates based on labour force survey data from national statistical offices; for additional details, see ILO (2017).

Note: Non-seasonally adjusted data. For all entries, ages are for persons 15 years and older, except for Macau, China (ages 16+); regional figures are annual estimates; China, India and Pacific island countries are not included due to a lack of comparable survey data.

Figure 18. Unemployment rates in selected countries/areas in the Asian and Pacific region

![Graph showing unemployment rates in selected countries/areas in the Asian and Pacific region]

Source: ILO estimates based on labour force survey data from national and official statistical offices; for further information, see ILO (2017).

Note: Total unemployment covers the labour force (persons aged 15 years and older) except for Macau, China (persons aged 16 years and older); youth unemployment covers the labour force (ages 15-24) except for Macau, China (ages 16-24) and Singapore (residents aged 15-29 years); regional figures are annual estimates; and China, India and the Pacific island countries are not included due to a lack of comparable survey data.
casual work, at 33.3% in 2015, which had increased from 29.4% in 2010. Sri Lanka had the lowest rate, at 12% of all employees in 2013. A key determinant of casual employment is education. In Indonesia, nearly 90% of casual employees had at most only a primary education – compared with 37% of regular employees. By industry, the four sectors that consistently had the highest shares of casual work were agriculture, manufacturing, wholesale and retail trade, and construction, which together accounted for more than 85% of all casual jobs in Indonesia, Pakistan and Viet Nam and about 60% in Sri Lanka (ILO, 2017). Highly skilled employment also remains relatively low in most economies in the Asia-Pacific region – as it is the flip side of casual work.

The above discussion shows that employment that is of poor quality, unstable and based on low education and skills is pervasive in the Asia-Pacific region, and this situation hinders the prospects of boosting living standards and alleviating poverty. Evidence shows that, although poverty – especially extreme poverty – in the region decreased considerably since the late 1990s, the pace of poverty reduction has weakened (ESCAP, 2017c). Furthermore, large segments of the population remain vulnerable to falling back into poverty, that is, they are living just above the poverty line and run the risk of falling back into poverty again. For instance, although Turkey’s share of people living in extreme poverty declined from 3.7% of the population in 2003 to 0.3% in 2013, the income of the poorest quintile during those years rose from 5.5% to only 5.8%, which means that many people in Turkey are living just above the poverty line. If a more holistic definition of poverty, such as multidimensional poverty, is adopted, the number who are poor would tend to increase.

Furthermore, income inequality in Asia and the Pacific has risen relative to the 1990s, especially in some countries. China, India and Indonesia are examples of large countries where inequality has grown, while in others, such as Papua New Guinea, the Russian Federation and Thailand, inequality has decreased relative to the 1990s (table 4) (ESCAP, 2017c). Several measures, such as the Gini coefficient, Palma ratio and income growth among the bottom 40% of the population in the last five years, can be considered in this regard. In China, the Gini coefficient increased from 32.4 in 1990 to 42.2 in 2012 (World Bank, 2016), and in 2009 the country had a Palma ratio of 2.1, which was among the highest in the region. Furthermore, the income of the wealthiest 60% of the population has been growing more than that of the rest of the population even in recent years. In India, the Palma ratio stood at 1.4 in 2010. Thus, the region’s economic success in past decades has led to accumulation of private wealth with a concentration

<table>
<thead>
<tr>
<th>Table 4. Evolution of inequality in selected countries in Asia and the Pacific</th>
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<td><strong>GINI index (latest year)</strong></td>
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<tr>
<td>32.4 1990s</td>
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<td>India 35.2 (2011)</td>
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<td>30.8 1990s</td>
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<td>Indonesia 39.5 (2013)</td>
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<td>55.4 1990s</td>
</tr>
<tr>
<td>48.4 1990s</td>
</tr>
<tr>
<td>45.3 1990s</td>
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Source: ESCAP, based on World Bank World Development Indicators.

Note: The Palma ratio is the share of all income received by the 10% of people with the highest disposable income divided by the share of all income received by the 40% of people with the lowest disposable income. For more information, see OECD (2017). The rate of income growth of the bottom 40% is the annualized average growth rate in per capita real survey mean consumption or income of the bottom 40% of the population over a roughly five-year period.
at the top, a situation which aggravated wealth inequality in such countries as India, Indonesia, the Russian Federation and Thailand, where the top 1% of the population account for more than half the total wealth pool in those countries (ESCAP, 2016a). Indeed this phenomenon is visible in the growth of income experienced by the poorest 40% of the population (lower than economic growth in such countries as China and Indonesia). However, this indicator also shows that, in recent years for some countries, the income of the poorest might be catching up as the rate is higher than GDP growth (table 4).

Inequality and lack of social protection are highly correlated, and social protection is an area where developing countries in the Asia-Pacific region have ample room for improvement, that is, the region falls behind the rest of the world in terms of both coverage and financing. Coverage remains weak in most countries, although some countries, such as China, Thailand and Viet Nam, have made notable progress. The main challenge is financing social protection schemes, as their delivery needs to be consistent with fiscal sustainability considerations. Average total public spending on social protection, including health, as a percentage of GDP increased from 3.5% in 2000 to 5.3% in 2010/11 (latest year for which data are available) in the Asia-Pacific region, but such spending is still lower than that of the global average − 8.6%.

Several broad policy measures can be considered which may facilitate mitigating inequality of income and of opportunity. To reduce income inequality, fiscal measures, such as progressive taxation, can greatly help while creating needed revenues for better public education, training and social protection. Measures to improve the creation of high added-value employment can target the demand for high added-value jobs, or their supply. On the demand side, upgrading the education and training of the workforce is critical, as workers with higher skills and technical competency can fill more productive and better paid jobs as managers, professionals and technicians. Efforts can be made to equip them with the right skills through technical vocational education and training and a greater focus on education emphasizing science, technology, engineering and mathematics. Other measures to stimulate the demand for high added-value workers relate to minimum wages or protection against casualization. Casual workers should be extended similar treatment as more regular workers through the reshaping and enforcement of labour regulations, which could include the provision of minimum wages for casual employees. Strengthening social dialogue and the capacity of unions to organize workers in casual and other non-standard employment relationships could also help improve working conditions (ILO, 2017).

In considering the supply side of high added-value jobs, it must be recognized that, if such supply is fixed, higher education will create more competition for the same number of jobs. Hence, the goal must be to increase the number of high added-value jobs available. This can be done by tackling key bottlenecks in such areas as infrastructure, communications, research and development, and business incubators focused on innovation − often in universities.

Social protection can be used to tackle both inequality of income and of opportunity. In relation to income inequality, it can assist workers when they fall ill or when they switch jobs, among other reasons. Furthermore, social protection is particularly significant for reducing inequality of opportunity, which works in the medium to long run and affects new generations. The objective is to achieve a level playing field for all children, so that vicious self-perpetuating circles (that is, children of poor families tending to grow up poor as well) can be broken. Hence, social spending on education, health and other forms of social protection are critical. A social protection scheme particularly worth exploring is the universal basic income scheme being considered by such countries as India (India, Ministry of Finance, 2017a), after it implemented pilot unconditional cash transfer schemes.60

The previous section has illustrated how a holistic approach to development must go beyond an economic growth-centred paradigm to include closely intertwined dimensions of development under a social perspective (labour market, poverty and inequality, and social protection). In the next section, a similar exercise will be conducted in considering environmental perspectives.

1.2.5. Environmental sustainability

Asia and the Pacific is a region of the world very vulnerable to climate change and its associated adverse consequences in the form of natural disasters. Between 2005 and 2014, the top 10 countries with the most natural disasters included 8 from Asia and the Pacific: China, the Philippines, India, Indonesia, Viet Nam, Afghanistan, Japan and Pakistan (ordered by highest number of disasters) (UNISDR, 2014). Consequently, the costs associated with climate change are very high, not only in terms of financial and material costs but also human costs. Furthermore, the negative effects of climate change tend to affect poorer countries more than others.
Between 2000 and 2015, the low and low-middle-income countries in the region experienced by far the most deaths due to natural disasters, losing the highest number of people per disaster (ESCAP, 2017e). On average, more than 8,000 people died per disaster — almost 15 times the average toll in the region’s high-income countries.61

Vulnerability to climate change seems to be increasing as the effects of climate change have been accelerating over the years. Months when no natural disasters occur are very rare, as can be seen from the experience so far in 2017: in January, Thailand and New Zealand were inundated by floods, while Fiji experienced a severe tsunami following an earthquake that registered 7.2 on the Richter scale. In February, avalanches, snowfall and rain-related disasters caused great damage to homes and livelihoods in 22 of Afghanistan’s 34 provinces, while Australia suffered from an extreme heat wave, and the Philippines registered a 6.7 magnitude earthquake that affected more than 53,000 people. In March, Mongolia went through a dzud62 that was detrimental to more than 157,000 people across 17 of the country’s 21 provinces and required emergency responses, while Japan was adversely affected by copious snowfall that provoked avalanches that killed 8 people. In April, Cyclone Cook battered New Zealand. In June, heavy rains led to floods and landslides in Bangladesh, China, India and Nepal, causing hundreds of deaths in total. In July, there were torrential rains and floods in China and New Zealand. In August, China was shaken by a 6.5 magnitude earthquake, and Typhoon Hato ranged over Hong Kong, China; Macao, China; and southern China, severely damaging houses and farmland. In September, Mount Agung’s volcanic activity disrupted life in Bali, Indonesia, including its economy via its main source of income — tourism. In October, Vanuatu faced the threatened eruption of the volcano Monaro, for which thousands of people had to be evacuated.

As some of these natural catastrophes are the direct outcome of climate change, the region still has much to do in terms of addressing these phenomena. For example, the volume of greenhouse gas emissions in the region remains high, mainly due to fossil fuel-based generation of electricity and households burning coal and biomass for cooking and heating purposes. Currently, the region accounts for roughly half the world’s global greenhouse gas emissions. Furthermore, the efficiency of resource use in the Asia-Pacific region is lower than in the rest of the world. Energy intensity is high, especially among the large oil-exporting countries and China — although it has been slowly declining over time. The situation with regard to other types of pollution is no better. Countries in the Asia-Pacific region have failed to control the pollution of their rivers, more than 80% of which are in “poor health” (UNEP, 2017); the sources of pollution are untreated or partially treated sewage, agricultural runoffs, industrial wastewater and landfill leachate, and nutrients and sediments washed from degraded land by heavy rainfall.

To address climate change, strategies can be focused on mitigation or adaptation — ideally both. Climate change mitigation refers to the efforts to reduce pollution and the emission of greenhouse gases, and/or enhance the sinks of those gases.63 Such mitigation efforts can range from planning an energy-efficient new city to improving the design of cook stoves. Typical examples of mitigation strategies include innovative technologies, such as using fossil fuels more efficiently for industrial processes and electricity generation, switching to renewables, such as solar energy or wind power, improving the insulation of buildings, and expanding forests and other carbon sinks to remove carbon dioxide from the atmosphere. Some countries, such as Bhutan, emphasize the development of carbon sinks, for example through forests — either in the form of afforestation (planting of new trees on land that did not contain forests) or reforestation (replanting of trees on land that previously contained forests but had been converted to some other use).64 This approach has helped Bhutan to become the only carbon-negative country in the world.65

Adaptation to climate change refers to changes in natural or human systems in response to actual or expected climatic stimuli, or their effects, in order to moderate harm and exploit beneficial opportunities.66 Innovative instruments can be developed to adapt; one of these is risk-pooling against natural disasters.67 Notably, in 2012 Pacific islands States set up an innovative pilot programme for risk-pooling, which determined payouts according to a rapid estimate of losses based on a risk model. In January 2014, Tonga was the first of these island countries to benefit from the payout programme, receiving an immediate payment of $1.27 million towards recovery from the effects of Cyclone Ian.

Policy instruments to address environmental degradation and climate change comprise three types of measures: regulatory, market-based and voluntary or information-based (ESCAP, 2017c). The advantage of regulation lies in exerting direct control over the environmental outcome it is seeking to address, but typically no incentives are provided for the polluter to reduce emissions further. This approach is usually inefficient, however, in the sense that it does not direct pollution abatement towards the
lowest-cost polluter. Regulation is often used to control sources of hazardous pollution. For example, in July 2017 Viet Nam announced that in order to curb pollution motorbikes would be banned by 2030 (Qiuyi, 2017).

By contrast, market-based economic instruments rely on prices or markets to function. They encompass taxes, emission trading systems or subsidies, including the removal of inefficient fossil fuel subsidies. The advantages of market instruments derive from their superior allocative efficiency, the positive incentives they provide and their revenue-generating ability. For example, China recently announced that farmers will be paid to turn farm waste into fertilizer and power, as Beijing cracks down on agricultural pollution that has for years leaked into rivers and lakes (Xueying, 2017).

Third, voluntary and information-based measures include inventories of organizations that release pollutants and toxic substances, transfer registers, ecolabels, consumer awareness-raising campaigns and corporate sustainability reporting. One of the advantages of information instruments is their relatively low implementation cost compared with the complex administration needed to implement regulatory or market-based approaches. However, voluntary measures may provide only limited coverage and are sometimes considered less effective than other approaches. A notable example in the region has been Singapore’s Green Labelling Scheme. In November 2015, shortly after the emergence of South-East Asia’s worst haze event on record, the Singapore Environment Council encouraged companies to come forward and declare that their procurement of wood, paper and pulp materials were from sustainable sources; in the end, 145 companies did so (Singapore Environment Council, 2015). Then, the Council announced that an eco-label would be used to certify sustainable palm oil products not produced by mass clearing and burning of forested areas and other land. In February 2016, new assessment criteria were launched for assessing compliance by manufacturers of products containing palm oil (Singapore Environment Council, 2016).

In addition to a design that promotes environmentally friendly incentives, policy measures may also require substantial financial resources. Countries in the region are aware of and dedicating resources to such an approach - although arguably much more should be done. In August 2017, the Environmental Protection Fund of the Lao People’s Democratic Republic committed more than 14.5 billion kip (approximately $1.75 million) to support the protection of forests via forest resource management activities in five target provinces and Vientiane (Sengpaseuth and Phetphoxay, 2017). In addition to financial resources, institutional support is required as well. Policymakers should consider climate change as a priority in their development of infrastructure; a possibility would be the creation of national green financing vehicles to catalyse environmentally and financially sustainable infrastructure investments (ADB, 2017b).
2. MEDIUM-TERM CONSIDERATIONS

In the previous section on policy considerations it was shown that, although some aspects affecting development outcomes can be external, such as climate change-induced natural disasters, policymakers have a wide array of tools that they can use to promote sustainable development. In terms of monetary policy, there is room to remain accommodative, although external and domestic stability factors should be closely monitored. The potential impact of monetary policy normalization in the United States should not be underestimated, while high private debt calls for financial stability and macroprudential measures. Fiscal policy can continue playing an active role in lifting domestic demand and “crowding in” private investment. To tackle the issue of weak creation of decent jobs, policy measures in the labour market should not be focused only on promoting higher education and skills but also on increasing the supply of high added-value jobs. Furthermore, there is room for improvement of social protection systems in the region, which remain vital as they can help tackle both inequality of income and inequality of opportunity. In the environmental dimension, three types of policy measures were discussed (regulatory, market-based and information-based), and examples from the Asia-Pacific region were provided.

The availability of so many policy tools underscores the importance of good governance, with a special focus on fiscal management and effective institutions. These aspects of policy are more fundamental and operate in the medium term as opposed to interest rate changes for example. The next two sections are focused on exploring specific ways to improve fiscal management, such as through putting technology at the service of development, and adopting alternative approaches to mobilize public resources for development through taxes, effective debt management, or new actors, such as the private sector. While all these elements are different, they are not unrelated; their interconnection is underpinned by the role of governance as facilitator of structural transformation for implementation of the 2030 Agenda.

2.1. Leveraging technology for better governance in fiscal management

“Good governance is perhaps the single most important factor in eradicating poverty and promoting development”, declared United Nations Secretary-General Kofi Annan in 1998. Two decades later, countries continue to grapple with various governance challenges in both public and private spheres. The Survey for 2017 illustrated how weak governance could undermine all three dimensions of sustainable development - for instance, by damaging investment prospects, widening inequalities and ignoring environmental degradation through inaction. Moreover, in that issue of the Survey, fiscal management was identified as an important channel through which governance affects development outcomes. It was also found that the beneficial impact of public spending on education and health tended to be lower in countries that score poorly on various aspects of governance. It was also shown that poor governance undermines the tax morale of people and limits the fiscal space needed to improve public services. The situation could even become worse as these two effects reinforce each other. To break this cycle, it was recommended in the Survey that transparency and accountability in public administration be enhanced, by requiring public officials to make financial disclosure, making meaningful fiscal information accessible to the public, promoting participatory budgeting and leveraging e-government systems, among other means. For instance, the increased use of e-government systems has been associated with improvements in the perception of corruption control (figure 19).

In this section, a deeper look will be taken into how technology - broadly defined to encompass information and communications technology (ICT), digital finance and “big data” - could contribute to better governance in the context of fiscal management. Technology is reshaping the environment in which Governments operate as well as furnishing new tools for improving fiscal management. The digital economy potentially expands the information base of Governments while better information technology (IT) infrastructure enables Governments to better use and act upon such information. For instance, government agencies responsible for anti-poverty programmes could more easily monitor the impact of economic shocks on poor households and act swiftly through direct benefit transfers, based on a shared database that facilitates coordination. Tax authorities, on the other hand, could more easily track transactions and taxpayers and use new software to process huge amounts of data to cross-check and validate the data and information declared by taxpayers.

Aside from increasing government effectiveness, technology can help curb corruption by easing principal-agent constraints and information asymmetries that in the past resulted in leakages and bribes. The outcome could be a noticeable improvement in governance within a relatively short timespan. Moreover, it has been
Figure 19. E-government and corruption perception in Asia and the Pacific

Source: ESCAP, based on data from the United Nations Department of Economic and Social Affairs, and Transparency International.

Note: The e-government index is on a scale of 0 to 1 (1 being the most developed); the corruption perception score is on a scale of 0 to 100 (100 being the least corrupt). The left panel shows the level in 2016; the right panel, the change between 2012 and 2016.

suggested in studies that technology could be cost-effective, as savings tend to outweigh implementation costs. For instance, in a recent study it was estimated that digital finance could save developing country Governments $110 billion annually by plugging leaks in expenditures and non-collection of taxes, improving the targeting of subsidies and effecting efficiency gains in government operations as a result of digitizing payments (Woetzel and others, 2016).

To provide more insight, two specific cases are discussed in which technology is applied to improve fiscal management – one in the context of tax administration; the other in the implementation of direct benefit transfers. While illustrating the potential benefits of technology, both cases point to the importance of broader reform measures, including upgrading of staff skills and changes in organizational culture, without which the benefits could be much lower than otherwise would be expected.

Technology and tax administration

One of the main reasons why tax revenue as a share of GDP remains persistently low in several countries in the region is weak tax administration and low tax compliance. Although precise estimates are not available, tax evasion and avoidance are believed to be widespread. Addressing tax evasion is important because it affects not only tax revenues but also society’s perception of fairness and fiscal responsibility. There is an extensive literature which shows that strengthening tax administration is a core component of building fiscal capacity, or State capacity (Besley and Persson, 2013). Given the importance of strengthening tax administration, the potential benefits of technology have been well summarized by Bird and Zolt (2008) who called for the following actions:

- Change the tax environment by altering distribution methods and reducing cash transactions;
- Improve the quantity and quality of information available to taxing authorities and their ability to use that information effectively;
- Make tax administrations more effective by improving information flow, facilitating coordination and improving their allocation of resources;
- Reduce taxpayer compliance costs by improving information and services to taxpayers, such as through software for maintaining books and records, calculating tax liabilities and/or electronic or return-free filing alternatives;
- Reduce opportunities for corruption by moderating face-to-face interaction between taxpayers and taxing authorities.

The potential benefits of technology tend to be higher in developing countries due to the existence of “low-hanging fruit”. In the Asia-Pacific region, priorities in the use of online platforms include: online or electronic filing of tax returns for major taxes; enhanced websites that include more information and applications; integrated taxpayer accounts; and enhanced data capture methods (table 5).

Particularly in the context of improving tax compliance, technology could play a key role in improving the quantity and quality of information available to taxing authorities and their ability to use that information effectively. For instance, the increased use of credit cards or other electronic payment mechanisms provides not only information concerning the financial capacity of the purchaser but also confirmation of the VAT and income-filing status of the sellers (Bird and Zolt, 2008).
Another example is Internet-based resources, such as Google Earth, which furnish satellite imagery that can assist in identifying and monitoring specific property locations and property improvements. Technology could also help in processing such information, for instance by detecting discrepancies between the information declared by the taxpayer and the large quantity of information gathered from third parties, such as banks, credit card providers, online vendors, stock exchanges, customs and other government agencies, including registries of land and property, which in turn would enable more effective risk-based audits.70

Fundamental areas of tax compliance risk and the appropriate application of technology can vary by country. In the Asia-Pacific region, the most frequently reported risk types include: unpaid tax debts; tax avoidance schemes; corporate profit shifting; non-filing of tax returns; hidden economic activities, such as unreported cash transactions; and VAT fraud (table 6). One area which has received greater attention in recent years than in the past is corporate profit shifting and other forms of cross-border tax evasion and avoidance, which require international tax cooperation to remedy. Several countries in the region have committed to participating in automatic exchange of information, which requires, among other things, some harmonization of information technology modalities for secure transmission of data.71

The flipside of tax enforcement is voluntary tax compliance, and here too the role of technology could be significant. Several countries have been able to reduce the number of hours that firms spend on filing taxes through better provision of information and use of online platforms.72 Indirectly, open budget initiatives may boost tax morale and voluntary compliance. For instance, individuals may comply as a result of reciprocal motivation: the willingness to pay taxes in exchange for benefits that the State provides them and others, even though pecuniary payoffs would be higher if they did not pay taxes (Luttmer and Singhal, 2014). Technology could support open and participatory budget initiatives through information services that enable Governments to provide real time information on how taxes are put to use and for taxpayers to access such information through online platforms and mobile devices.

Adopting technology in tax administration, however, is not without costs while the gains can fail to reach

### Table 5. Priorities for use of online services by tax authorities

<table>
<thead>
<tr>
<th>Service</th>
<th>Australia</th>
<th>Brunei Darussalam</th>
<th>Cambodia</th>
<th>China</th>
<th>Hong Kong, China</th>
<th>Indonesia</th>
<th>Japan</th>
<th>Kyrgyzstan</th>
<th>Lao People’s Democratic Republic</th>
<th>Malaysia</th>
<th>Maldives</th>
<th>Mongolia</th>
<th>New Zealand</th>
<th>Papua New Guinea</th>
<th>Philippines</th>
<th>Republic of Korea</th>
<th>Singapore</th>
<th>Tajikistan</th>
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<tbody>
<tr>
<td>Online filing</td>
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<td>Prefilled returns</td>
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<td>Online payment</td>
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<td>Website service or tools</td>
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<td>Integrated taxpayer accounts</td>
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<td>Other online service</td>
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<td>Enhanced data capture</td>
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<td>Digital mailbox</td>
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Note: The absence of a tick mark means the type of service is not a priority.
Table 6. Main reported areas of tax compliance risks

<table>
<thead>
<tr>
<th>Country</th>
<th>Profit shifting/transfer pricing</th>
<th>Other tax avoidance schemes</th>
<th>Value added tax fraud</th>
<th>Other tax fraud</th>
<th>Hidden economy</th>
<th>Evasion-illegal activities</th>
<th>Other evasion</th>
<th>Unpaid tax debts</th>
<th>Non-filing of returns</th>
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</thead>
<tbody>
<tr>
<td>Australia</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
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<td>Brunei Darussalam</td>
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<td>Cambodia</td>
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<td>China</td>
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<td>Hong Kong, China</td>
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Note: The absence of a tick mark means the type of service is not a priority.

expectations. Public sector ICT projects are often criticized for not being able to deliver the desired results and/or leading to unproductive investments in ICT systems and infrastructure without much enhancement in the quality of service delivery. Such factors as strategic planning, commitment from the Government, ICT maturity levels among stakeholders, acceptance of the system within and outside the Government and technological complexities influence the outcomes of these projects (ADB, 2014). Successful reform efforts did not simply computerize antiquated processes, but re-engineered entire systems (Bird and Zolt, 2008). Successful use of IT requires restructuring and retraining the tax administration. Successful introduction of new technologies may also require consideration of the susceptibilities of existing staff and their resistance to change.

Technology and direct benefit transfers

Public expenditure efficiency tends to be low in developing countries in part due to leakages in the transfer of subsidies and other social assistance programmes (table 7). A recent study conducted by the Abdul Latif Jameel Poverty Action Lab (Dodge and others, 2016) captured the issue:

Increasingly, countries across the world use social protection programs to redistribute gains from economic growth and protect poor households from downturns. Yet, programs often face challenges ensuring that intended recipients are targeted successfully and receive benefits in a timely fashion. State capacity is often inadequate to administer these programs effectively and without corruption, often to the detriment of vulnerable beneficiaries. In environments with corruption, government officials may be limited in their ability to monitor program implementation, such as being able to correctly identify the sources of payment delays and determine who to hold accountable. In such contexts, can technological innovations to share information help social protection programs reach their intended beneficiaries?

To address these leakages and increase transparency, countries are increasingly leveraging IT. Digital payments, often facilitated through digital identity systems, are being deployed on a massive scale in such countries as India, where more than 975 million people have been enrolled in a unique identification system known
Table 7. Selected magnitudes of corruption

<table>
<thead>
<tr>
<th>Paper</th>
<th>Country</th>
<th>Context</th>
<th>Strategy for assessing corruption</th>
<th>Corruption estimate</th>
<th>Corruption estimate (percentage)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Olken (2006)</td>
<td>Indonesia</td>
<td>Theft of rice from a programme that distributed subsidized rice.</td>
<td>Compare administrative data to a generally administered household survey.</td>
<td>At least 18% of the programme’s rice disappeared before reaching households.</td>
<td>18% of programme expenditures</td>
</tr>
<tr>
<td>Niehaus and Sukhtankar (2010)</td>
<td>India</td>
<td>Wages in the National Rural Employment Guarantee Scheme.</td>
<td>Compare officially paid wages to wages as reported in a survey.</td>
<td>236 rupees stolen per actual day paid, where the wage for an actual day paid would be about 60 rupees.</td>
<td>79% of labour expenditures</td>
</tr>
<tr>
<td>Besley and others (2011)</td>
<td>India</td>
<td>Beneficiary (for anti-poverty programme) selected by village council.</td>
<td>Conditional on eligibility: does political office predict beneficiary status?</td>
<td>Chief village councillor is 10% more likely to be a beneficiary.</td>
<td>2% of beneficiaries selected</td>
</tr>
</tbody>
</table>

Source: ESCAP, based on Olken and Pande (2011).

as Aadhaar. By moving towards digital payments, the traceability of the payment process is improved. For instance, evidence from the state of Andhra Pradesh in southern India showed that the use of a biometrically authenticated payments infrastructure (“Smart cards”) by beneficiaries of a rural employment guarantee scheme and social pension programmes resulted in a faster, more predictable and less corrupt payments process - including a significant reduction in the incidence of demands for bribes and payments to fake recipients - without adversely affecting programme access (Muralidharan and others, 2014). In that study, it was also found that the investment was cost-effective as time savings to beneficiaries alone were equal to the cost of the intervention, and there was also a significant reduction in the leakage of funds. Moreover, beneficiaries of both programmes overwhelmingly preferred the new system.73

Such application of technology has been possible only with broader institutional changes. In the case of Andhra Pradesh, the Government contracted with banks to manage payments, and these banks in turn contracted with technology service providers (TSPs) to manage the “last mile” logistics of delivery. TSPs then hired and trained customs service providers (CSPs), who came into direct contact with the beneficiaries and disbursed the amount of cash requested after confirming their identity through fingerprint scanning devices. For all of this to happen, the Reserve Bank of India had to allow banks to partner with TSPs to jointly offer and operate no-frills accounts that could be used for savings, benefit transfers, remittances and cash withdrawals, given that the fixed cost of bank branches is typically too high to make it viable to profitably serve people in rural areas. The Government also stipulated norms for CSP selection and required that CSPs be women resident in the villages where they served, have completed secondary school, not be related to village officials, preferably be members of historically disadvantaged castes and be members of a self-help group.

Digital transfer systems are effective when they include sensible policies to address privacy and data integrity concerns and to prohibit passive exclusion when documents for registration are difficult to obtain (ESCAP, 2017c). To address increasing privacy concerns, legal safeguards are being implemented to check data theft or misuse. An issue that should be considered in the application of technology is the potential exclusion of eligible beneficiaries, particularly in rural areas with limited access to the banking system. There is an important gender dimension in e-government to ensure that new policies include and empower women (table 8).

The information in this section illustrated that technology is indeed reshaping the environment in which Governments operate and presented examples of new tools for improving fiscal management. Other aspects not covered in this section but which are prominent examples may include the application of ICT in managing the delivery of public services in health, education, subsidized food, or electronic delivery of administrative services, such as certificates and licenses, to rural populations.74 Hence, technology, together with complementary institutional changes, can bring about significant fiscal savings while contributing directly to enhanced transparency and accountability in public administration. Several other institutional changes could complement technology; a central one, mobilizing more resources to implement the 2030 Agenda, is covered in the next section.
Table 8. Components of gender-responsive e-government policies

| Service delivery | - Balance between digital processes and human mediation  
|                  | - Robust governance of emerging boundary-spanning arrangements in service delivery  
|                  | - Investments in both data and connectivity capacities  
|                  | - Gender-responsive data governance to balance transparency and privacy  
| Citizen uptake   | - Technology design that is aimed at expanding women’s choices and engagement in government structures  
|                  | - Frontline workers to nurture women’s appreciation for, and trust in, digitalized service delivery  
|                  | - Leadership of national women’s machineries to encourage gender-responsive e-government  
| Connectivity     | - Models to promote meaningful online participation for women  
|                  | - Subsidized access and safe public spaces for including all women  


2.2. Mobilizing development finance to support the 2030 Agenda

Several studies have shown that the amount of financial investment required to achieve the Sustainable Development Goals far exceeds current trends. Closing this wide investment gap calls for mobilization of larger public fiscal resources and greater participation by the private sector. How Asia-Pacific countries can mobilize more development finance to support the 2030 Agenda is the thematic topic of the Survey for 2018, in which the issue will be investigated in detail. In this section of the Update for 2017, a preview of the forthcoming analysis is provided along with highlights of some key issues and research questions that will be explored in the 2018 report.

2.2.1. Sizeable financing gaps must be closed in order to support sustainable development

The 2030 Agenda for Sustainable Development is a comprehensive and ambitious endeavour. Achieving the 17 Sustainable Development Goals and their 169 targets by 2030 would mean, among other things, that extreme poverty and hunger would be eradicated; primary and secondary education would be free; universal health coverage would be in place; and all segments of the population would have access to affordable housing, safe drinking water, modern energy and sustainable transport systems. To achieve these Goals, financing is considered as one of the main means of implementation, along with technology, trade and capacity-building.

Globally, it has been estimated that low and lower-middle-income countries would need on average an additional $1.4 trillion per year, or about 11.5% of their combined GDP, during the period 2015-2030 in order to achieve the Sustainable Development Goals relating to health, education, food security, infrastructure, ecosystem services and humanitarian work (Schmidt-Traub, 2015). Also globally, it has been estimated that the required additional investment would rise to $2.5 trillion per year during the same period based on annual investment needs of about $3.9 trillion and current spending of $1.4 trillion (UNCTAD, 2014). In both studies, it is suggested that investment needs for economic infrastructure, such as transport, energy, telecommunications, and water and sanitation, are much higher than for other areas. In Schmidt-Traub (2015), infrastructure accounted for about 70% of the total need. In UNCTAD (2014), transport, such as roads, rail and ports, alone were found to cost more than health and education combined.

Studies that are focused only on infrastructure also suggest sizeable investment gaps. In Woetzel and others (2016), it was estimated that global infrastructure investment needs would be $3.3 trillion per year over the period 2016-2030 (China and India together would account for about 35% of this amount). Based on these estimates, the infrastructure investment shortfall would be about $350 billion or 0.4% of the world’s GDP per year. In ADB (2017c), it was suggested that the infrastructure investment gap for a group of 25 economies in the Asia-Pacific region, after taking into account the additional cost involved with making infrastructure more climate-resilient, would be about $460 billion or 2.4% of GDP per year during the period 2016-2020. If China, which has a relatively small investment gap, is excluded, the average gap for the remaining countries would rise to about 5% of GDP. For individual Asia-Pacific economies, Global Infrastructure Hub (2017) showed that infrastructure investment shortfalls would range from 4-7% of GDP in Cambodia, Myanmar and Pakistan to 1-2.5% of GDP in Bangladesh, India, the Russian Federation and Viet Nam (figure 20). In countries with special needs, in ESCAP (2017a) it was estimated that infrastructure investment needs in 26 Asia-Pacific economies would be up to 10.5% of GDP on average per year during the period 2016-2030. Such an estimate far exceeds the current infrastructure spending of 4-7.5% of GDP in this group of economies.

While available estimates on investment gaps to achieve the Sustainable Development Goals and ensure adequate infrastructure are all indicative, varying and not strictly
comparable, they point to the need for a considerable boost to future investment in order to promote sustainable development. Past spending has not been sufficient, as demonstrated by the large number of people who are still malnourished and lack access to electricity and clean water. Ongoing structural shifts are likely to place even greater pressure on future investment needs, especially in terms of infrastructure. For example, rapid urbanization would require better urban transport and telecommunications systems, while climate change is increasing the demand for climate-resilient infrastructure.

### 2.2.2. Mobilizing additional financing for development

To close the enormous investment gaps, a substantial amount of financing is needed so that the 2030 Agenda can be pursued effectively. The need for financing points to the requirements for stronger resource mobilization strategies in the Asia-Pacific region. It is possible to increase the magnitude of development finance through the strengthening of public finance and effective leveraging of private finance.

#### Strengthening public finance

There are various means to enhance fiscal space. The most common of these is better and higher tax collection that benefits from a wider tax base and/or improved tax administration. Beyond tax revenues, there is a wide range of non-tax revenue sources, such as the operation of State-owned enterprises, management of sovereign wealth funds and budget support from foreign aid and multilateral development banks. On the expenditure side, efficient and effective public spending can help deliver greater development impacts for the same amount of fiscal resources. Finally, when revenue falls short of expenditure, prudent government borrowing from financial markets can help augment fiscal space.

The analysis on strengthening public finance in the forthcoming Survey for 2018 will focus on two areas: better and higher tax collection and prudent borrowing from financial markets by Governments. Various aspects of these issues have been examined in some detail in recent issues of the Survey. The Survey for 2018 will expand and deepen the earlier analyses.

On the issue of tax collection, in the Survey for 2014 estimates were made of the tax potential in Asia-Pacific economies based on each country’s economic structure, including such factors as agricultural value added, GDP per capita level and the degree of trade openness (ESCAP, 2014). Actual tax collection levels were below their potential in 17 Asia-Pacific economies for which data were available. Such tax gaps were estimated to be more than 6% of GDP in Afghanistan, Bangladesh, Bhutan, Islamic Republic of Iran and Maldives (figure 21). In the Survey for 2014, policy options were put forward in three areas: expanding the tax base by rationalizing existing tax exemptions and introducing new taxes; enhancing tax administration through, among other measures, streamlining procedures and making greater use of information and communications technology; and promoting regional cooperation on tax policies.

#### Figure 20. Estimated infrastructure investment gaps in selected Asia-Pacific economies

<table>
<thead>
<tr>
<th>Country</th>
<th>Percentage of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Myanmar</td>
<td>6.8</td>
</tr>
<tr>
<td>Cambodia</td>
<td>5.1</td>
</tr>
<tr>
<td>Pakistan</td>
<td>3.7</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>2.5</td>
</tr>
<tr>
<td>India</td>
<td>2.3</td>
</tr>
<tr>
<td>Russian Federation</td>
<td>1.8</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>1.5</td>
</tr>
<tr>
<td>Philippines</td>
<td>1.4</td>
</tr>
<tr>
<td>Turkey</td>
<td>1.4</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>1.3</td>
</tr>
<tr>
<td>Thailand</td>
<td>0.8</td>
</tr>
<tr>
<td>Malaysia</td>
<td>0.6</td>
</tr>
<tr>
<td>Indonesia</td>
<td>0.6</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>0.4</td>
</tr>
<tr>
<td>China</td>
<td>0.4</td>
</tr>
</tbody>
</table>

In the tax policy analysis in the Survey for 2018, there will be an investigation of the scope of the tax gaps for each major tax, such as corporate income tax, personal income tax and sales/value-added tax. Another issue is the extent to which the tax policies recommended in the Survey for 2014, if implemented, would help to narrow the tax gap in Asia-Pacific economies. For example, how large is the potential revenue impact of improved tax administration? What room is there for introducing less conventional types of taxes, such as carbon tax and financial transaction tax, and how much additional revenue could they potentially generate? These taxes would help not only to raise government revenue but also to address social and environmental concerns.

The second area on strengthening public finance that will be considered in the Survey for 2018 will be whether Asia-Pacific economies could make greater use of government borrowing in a prudent manner from financial markets, and how that could be done. In the Survey for 2013, it was argued that the goal of macroeconomic policies should not be focused solely on ensuring macroeconomic stability but also on promoting sustainable development through job creation, social development and environmental protection (ESCAP, 2013). Hence, there is a need to think - and rethink - about the correct balance between the stabilization and the developmental roles of macroeconomic policies. For example, while public debt sustainability should be closely monitored and maintained, Governments also should ensure that meeting targeted fiscal outcomes and fiscal rules does not come at the cost of reducing spending on essential areas, such as infrastructure development and education.

Experiences from the Asia-Pacific region would suggest that macroeconomic stability alone is not sufficient for achieving sustainable development.

In the Survey for 2018, there will be an examination of whether Asia-Pacific economies can afford higher public debt levels in order to increase spending in areas that would help improve economic fundamentals and the potential for economic growth. In Japan and Singapore, government debt-to-GDP ratios are very high but perceived sovereign risk remains low, largely because the economic fundamentals are stable. Another issue relates to factors that have constrained Governments from issuing more domestic and foreign bonds, such as the size of the domestic capital market and sovereign credit risk, as well as legal frameworks. In the Survey for 2018, there will be a discussion of available policies aimed at addressing these constraints and an examination of the extent to which government bond issuance could be increased as a result of improvements in the quality of policies.

**Leveraging private finance**

The wide investment gap for achieving the Sustainable Development Goals would suggest that financing from public sources alone will not be enough. Policy efforts should be made to increase participation by the private sector beyond their contribution to tax revenues. As the size of assets that are being managed by commercial banks and institutional investors worldwide is estimated to be about $120 trillion (Woetzel and others, 2016), the focus should be on how to effectively leverage private finance. The most obvious channel is through

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**Figure 21. Estimated tax gaps in selected Asia-Pacific economies**

<table>
<thead>
<tr>
<th>Country</th>
<th>Tax Gap (Percentage of GDP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bangladesh</td>
<td>7.5</td>
</tr>
<tr>
<td>Bhutan</td>
<td>6.7</td>
</tr>
<tr>
<td>Afghanistan</td>
<td>6.2</td>
</tr>
<tr>
<td>Maldives</td>
<td>5.8</td>
</tr>
<tr>
<td>Indonesia</td>
<td>4.7</td>
</tr>
<tr>
<td>Cambodia</td>
<td>3.0</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>2.1</td>
</tr>
<tr>
<td>Pakistan</td>
<td>1.8</td>
</tr>
<tr>
<td>China</td>
<td>1.8</td>
</tr>
<tr>
<td>Philippines</td>
<td>1.5</td>
</tr>
<tr>
<td>Malaysia</td>
<td>1.3</td>
</tr>
</tbody>
</table>

philanthropy or charitable giving. While not trivial, funding by various global foundations aligned with efforts to achieve the Goals has remained small, at $18.8 billion per year during the period 2010-2015, although the amount is expected to grow to an average of $22.8 billion annually in the period 2016-2030.

Another area in which the private sector could contribute significantly is through co-financing infrastructure projects. Relative to other Sustainable Development Goal investment areas, infrastructure often exhibits greater potential for private investor participation in view of its expected steady revenue stream. For example, private commercial financing could contribute at least half the required investment in energy, transport and telecommunications (Schmidt-Traub, 2015).

While public-private partnerships (PPPs) are becoming more common in the region, their potential is still largely untapped in most countries. The overall policy aim should be to enhance an enabling environment that promotes the viability of projects by offering reasonable risk-adjusted returns. To create such an environment, the broad focus could be on ensuring a business-friendly regulatory framework, maintaining political and macroeconomic stability and facilitating access to project finance, including channels beyond traditional bank financing. More specific policies include introducing specialized PPP agencies and PPP laws and offering guarantees in order to reduce operational risks. These factors have been examined in 16 developing Asia-Pacific economies; the environment for PPP projects has been found to be more enabling in such countries as India, the Republic of Korea and the Philippines (EIU, 2015). The Survey for 2018 will contain an assessment of countries’ readiness to implement PPPs in a broader group of Asia-Pacific economies.

A more developed domestic capital market is needed to enhance access to finance by PPP projects. Except in few economies, such as Hong Kong, China; and Singapore, capital markets in Asia and the Pacific remain relatively small, with low levels of market liquidity. Overreliance on bank lending in the region has constrained financing for long-term infrastructure projects as bank loans are typically short term and collateral-based in nature. A more mature capital market would also help increase the role that public debt instruments play in supporting fiscal space.

Beyond PPPs, another policy issue is how to better align profit-driven business operations with sustainable development. For institutional investors, such as pension funds and insurance companies, a key challenge is to design policies that incentivize such investors to finance longer-term instruments, such as infrastructure funds. For companies, incentives and regulations could be introduced to encourage them to incorporate social and environmental considerations into commercial decisions. Examples of ongoing initiatives include India’s corporate social responsibility law and Singapore’s green public procurement, although overall policy effort in this area remains rather limited in the Asia-Pacific region.

CONCLUDING REMARKS

Over recent decades, it has become clear that the region’s excellent economic growth performance would not necessarily guarantee progress in the new era of sustainable development. In that spirit, the 2030 Agenda for Sustainable Development was conceived as the most comprehensive global endeavour ever undertaken to achieve sustainable development. It is no longer sufficient, however, to consider whether countries are able to achieve the Sustainable Development Goals called for under that Agenda. Rather, it is essential to ensure that the three dimensions of development - economic, social and environmental - are integrated within such an undertaking in a holistic manner. The 2030 Agenda was launched in 2015; time is passing rapidly, yet the aspirations of the 2030 Agenda must be materialized in a time frame not much longer than just a single decade.

In the Survey for 2017 and the present Update, governance, including the “political will” to undertake reforms, have been emphasized as the engine for progress. Fiscal management and effective institutions are vital transmission mechanisms. In this Update, policy options, tools and key means of implementation, such as technology and financing for development, have been emphasized. Fiscal policy has a central role to play in this regard. While aimed at ensuring long-term fiscal sustainability, the developmental role of such policy must be fully embraced, as this will lead policymakers to enable such welfare-enhancing aspects as social protection and to correct others, such as negative environmental externalities, while tackling negative by-products, such as high inequality - both of income and, most importantly, of opportunity. In turn, monetary policy must be devised to prevent financial vulnerability and ensure stability for it is in these conditions that investment will thrive. It is investment that will make the 2030 Agenda possible: the right investments in the economy, people and the environment. ESCAP will therefore continue supporting policymakers in increasing the understanding of the policy options at their disposal.
ENDNOTES

1 General Assembly resolution 70/1.
2 Such issues will be studied in detail in the Economic and Social Survey of Asia and the Pacific 2018, which will be published in May 2018.
3 Notably, in China productivity growth has decreased from an average annual increase of 9.5% in the 2000s to 7.6% in the 2010s – in 2016 it grew by 6.4% relative to that of 2015. These figures have been calculated from World Bank data on GDP per person employed (constant 2011 purchasing power parity in United States dollars).
4 In August 2017, according to CEIC Data industrial output increased by 6% year on year compared with 6.4% in July, which is the slowest pace recorded in the current year; retail sales increased by 10.8% year on year in the first half of 2017 but the rate trended downward in July and August to 10.4% and 10.1% respectively. Fixed-asset investments in urban areas increased by 7.8% in August, cooling from 8.3% in the first seven months of the year.
5 Pledged foreign investment will increase to as high as $28 billion (Nguyen, 2017).
6 The fiscal year in Bangladesh ends on 30 June.
7 For more information, see Nielsen (2017).
8 As highlighted in the Survey for 2017 (figure 1.19, panel A, p. 28), the region’s steady economic growth is not leading to a commensurate increase in real wage growth. Nevertheless, real wage growth in the Asia-Pacific region, however uneven, is relatively robust and outperforms that of the rest of the world.
9 A hukou is an official record of household registration in China. Since early 2016, many second-tier cities and cities neighbouring Beijing and Shanghai have issued restrictions on the purchase of housing in order to cool property markets. In Nanjing for example, a potential home buyer would need to possess a local hukou or a permanent residence permit, and must not own a house in any of its three districts (Liuhe, Lishui and Gaochun) to qualify to buy a house. In Qingdao, people without a local hukou must provide records on 12 months’ worth of income tax and social security payments in the last two years to be able to purchase a house in the urban area; non-locals do not qualify to make a purchase at all. For further information, see Xinhua (2017) and China Daily (2017).
10 This implies a growth rate of 3%, while in the previous year credit grew by 8.5%, according to Bank for International Settlements data.
12 In August 2017, the rate was reduced to 4.5% and in September it was further cut to 4.25%.
13 The number of tourists grew by nearly 9% in 2016.
14 Having a current account deficit is not necessarily a negative feature for an economy. When countries experience a higher current account deficit, they are attracting investments from abroad and/or borrowing capital. As long as the overall economic environment remains conducive for foreign investments and the borrowed capital is put to productive use, the management of the current account deficit should not be an issue.
15 For details, see www.wto.org/english/news_e/pres17_e/pr800_e.htm.
16 Especially low-cost manufacturing, such as garments and shoe-making, but more recently also low-cost electronics. For further information, see Low-cost (2017) and Carbone (2017).
17 Such purchases had been banned since shortly after the dissolution of the Union of Soviet Socialist Republics in 1991, according to the Times of Central Asia (2017).
18 This term refers to the multitude of trade facilitation agreements in the Asia-Pacific region; they often overlap and are redundant, which can result in transaction costs for firms trying to benefit from such agreements.
19 This estimation was calculated by ESCAP based on Global Trade Alert data (www.globaltradealert.org).
20 For example, potential shifts in United States policies on immigration, such as the travel restrictions announced in September 2017 affecting nationals from the Democratic People’s Republic of Korea and the Islamic Republic of Iran, among other countries, could have negative impacts on the Asia-Pacific region.
21 For example, wage growth in Australia remained at record lows in 2017, as workers received a pay rise of just 0.5% in Q1, according to a 2017 forecast by the Korn Ferry Hay Group (www.haygroup.com/en/our-library/infographics/2017-global-salary-forecast).
22 According to some estimates, in 2018 real wages in the Asia-Pacific region are expected to rise by 4.3% - the highest globally. The largest real wage increases are forecast for Viet Nam (7.2%), Thailand (5.6%), Indonesia (4.9%) and India (4.8%). If these forecasts materialize, private consumption should strengthen further and be translated into upward pressure on prices. For further information, see the Korn Ferry Hay Group forecast for 2017 (www.haygroup.com/en/our-library/infographics/2017-global-salary-forecast).
23 As the world becomes more globalized, there have even been calls for a more global monetary policy, which would support this explanation.
24 Equivalent to about 1% of the country’s GDP.
25 By law, private lenders can charge an interest rate of 27.9% per annum, but the ceiling is often disregarded (Choi, 2017).
26 Remittances have risen in 2017; they increased by 4.5% between January and May from the same period in 2016 to a total of $11.35 billion, according to data from the central bank.
27 The value of the reserves amounted to more than $3.1 trillion at the end of September, up by $17 billion compared with a month earlier.
28 For example, see www.imf.org/external/pubs/ft/fandd/basics/macropru.htm.
29 Note that country coverage differs among these measures. This might explain why the cyclically adjusted deficit was larger than the overall deficit in some years, which would imply a positive output gap. The primary balance – overall balance net of interest payment – better reflects the fiscal stance.
30 Structural reforms include reductions in steel production capacity and excess urban real estate inventory, and deleveraging in the non-financial corporate sector, including State-owned enterprises (State Council of China, 2017b).
31 Following the credit rating downgrade by Moody’s in May and Standard and Poor’s in September 2017, China’s Ministry of Finance made a statement that the “contingent liabilities” are in fact not government liabilities.
32 Estimated by researchers of the Chinese Academy of Social Sciences, as cited in media reports.

33 The VAT structure was further simplified in 2017 (Wei, 2017; Wong, 2016).

34 Economic growth from April to June 2017 (Q1 of fiscal year) slowed to 5.7% in part due to sharp inventory cuts and weak new orders in preparation for the rollout of the goods and services tax in July.

35 The acronym stands for “Ujwal DISCOM Assurance Yojanda”, which is the financial turnaround scheme for the country's electricity distribution companies. For more information, see Reserve Bank of India (2017).

36 The Government of Indonesia's Tax Amnesty Statistics Dashboard involved a nine-month tax amnesty programme that ended in March 2017; it resulted in declaration of previously hidden assets equivalent to 39% of the country's GDP, significantly higher than that of similar programmes recently implemented by India and a few Latin American countries.

37 For further information, see Bank Indonesia (2017) and the speech of the Indonesian Minister of Finance delivered at the opening of the Joint IMF-Indonesian High-level Conference on International Taxation in Asia, held in Jakarta on 12 July 2017 (www.kemenkeu.go.id/sites/default/files/press%20release%20joint%20 IMF-indonesia.pdf).

38 Standard and Poor's in May 2017 upgraded the country's credit rating to investment grade. It should be mentioned that the World Bank has estimated that Indonesia will have to spend $500 billion to meet its infrastructure needs over the next five years.

39 Definitions include: “the availability of budgetary room that allows a government to provide resources for a desired purpose without any prejudice to the sustainability of a government’s financial position” (Heller, 2005); and “the financing that is available to government as a result of concrete policy actions for enhancing resource mobilization, and the reforms necessary to secure the enabling governance, institutional and economic environment for these policy actions to be effective, for a specified set of development objectives” (Roy and Heuty, 2009). The first definition emphasizes sustainability; the second, policy reform. In practice, both definitions are relevant.

40 Formally, the law of motion of the government debt-to-GDP ratio is:

\[ d_t = \frac{(1+i)}{(1+g)} \left( \frac{1+\pi}{1+g} \right) d_{t-1} - (b_t + \Delta m_t), \]

where \( d \) denotes stock of debt; \( b_t \), primary balance; \( i, g, \pi \), nominal interest rate, real growth rate and inflation rate, respectively; and \( m \), seignorage, all as a ratio to GDP.

41 The fiscal gap calculation would need to use weighted average interest rates (domestic and global) and weighted average economic growth rate (local and foreign currency).

42 Central banks also hold/buy government debt, but they are not technically “investors” in government debt; they simply serve as an agent of the Government to help raise debt from the domestic market.

43 Among alternative, model-based approaches, an interesting study, wherein the investment-growth linkage and debt dynamics are made explicit, was undertaken by Berg and others (2012). They found that well-executed high-yielding public investment can substantially raise output and consumption and be self-financing in the long run.

44 The enthusiasm, also reflected in a recent OECD analysis, was clearly laid out by Jason Furman of President Barack Obama’s Council of Economic Advisors in an October 2016 speech. In contrast, India’s Economic Survey 2016/17 (India, Ministry of Finance, 2017a) reflected a more cautionary tone, and so have Chinese academics (Bai and others, 2016).

45 For an elaboration on these factors, see Ilzetzki and others (2013). Such studies often rely on a quarterly structural vector auto-regression (VAR) approach to identify fiscal shocks.

46 For a basic conceptual framework, see Barro and Sala-I-Martin (1992); for empirical estimates, Devarajan and others (1996). Their extensions generally use the multi-country panel regression method.

47 India’s new bankruptcy code will facilitate time-bound closure of ailing businesses; Thailand has introduced a streamlined provision for liquidation of small and medium-sized enterprises.

48 India has streamlined the process for getting a new commercial electricity connection and introduced unified portals and self-certification for some labour and environmental laws. Indonesia has introduced a dedicated procedure for small claims that allows for parties’ self-representation to enforce contracts.

49 China is reducing administrative burdens and fees on startups and encouraging private entry, while India's Start-up India initiative supports the creation of firms by providing financial and technical support. Indonesia has also streamlined procedures for setting up and running business, although inconsistencies in regulation across levels of government remain. For more information, see the recent World Bank report available from www.doingbusiness.org/-/media/WBG/DoingBusiness/Documents/Annual-Reports/English/DB17-Report.pdf.

50 In Indonesia, a relatively high severance pay requirement is a key reason why firms tend to employ workers on a temporary basis.

51 For instance, the Government of India intends to increase the manufacturing value added in the economy to 25% by 2020 compared with 16% in 2015. India is behind China (27%) and Indonesia (22%) as well as high-income countries, such as the Republic of Korea (29%) and Germany (23%), in manufacturing value added.


53 Compared with its income level, China’s agricultural share of total employment is high and urbanization rate low, which suggests possible further across-sector relocation in coming years. At the same time, China’s proportion of robots per industrial worker (robot intensity) remains below the global average despite a recent rapid increase, leaving ample room for a further increase.

54 For further information, see Felipe and others (2014).

55 All data pertain to 2015, except for India; those data pertain to 2012, according to CEIC Data.

56 While related to informal work, casual and informal forms of work are not necessarily the same. Casual work generally refers to unstable work with very little protection, such as part-time work, very short hours of work, on-call work and even zero-hour contracts. For further information, see ILO (2016).

57 The extreme poverty headcount is defined as the share of the population living on less than $1.90 per day (in purchasing power parity).
Although that depends on the threshold of multidimensional poverty used, multidimensional poverty measures deprivation, as it refers to the share of the population that are deprived in terms of a certain set of indicators, such as poor health, lack of education and poor living conditions.

The income definition can change, in which case the figures may vary. Notably, based on a different, non-comparable income definition, India’s Palma ratio grew from 2.88 in 2004 to 3.09 in 2011. For details, see OECD (2017).

Different regions in the country have proposed a universal basic income scheme (UBI) numerous times, and some have implemented UBI schemes in the form of unconditional cash transfers. In 2011, a project named “Madhya Pradesh Unconditional Cash Transfers Project” was launched in that state in an attempt to reduce poverty. For 18 months, 6,000 people in rural Madhya Pradesh received a basic income: 300 rupees ($4.47) per adult per month and 150 rupees ($2.23) per child per month. As a result, there was an increase in school enrolment of children, both females and males. For persons 14-18 years of age, the school enrolment rate was 76% among the basic income villages, whereas in the control villages it was only 51.3%. The increase in income earnings among basic income households increased by 21% during the trial, whereas the control households improved by only 9%, according to the Seven Pillars Institute for Global Finance and Ethics (http://sevenpillarsinstitute.org/case-studies/universal-basic-income-empirical-studies).

The actual death toll in the poorest countries is probably higher, as many of these countries lack the means to record the number of deaths. For more information, see ESCAP (2017c).

A summer drought followed by a severe winter during which many livestock die of starvation.

The most important of these is the United Nations Framework Convention on Climate Change, which was adopted through General Assembly resolution 48/189.

Not only is the destruction of forests linked to climate change but it also has a clear adverse impact on other environmental pillars, such as biodiversity. For instance, Indonesia has been dubbed the orangutan capital of the world, but the great apes in the forests of Sumatra are under threat from palm oil plantations that annually clear thousands of hectares of forests - the habitat of such apes - to grow the trees that produce the most widely consumed vegetable oil on the planet.

For additional information, see www.scienceabc.com/social-science/carbon-negative-country.html.

As described in the United Nations Framework Convention on Climate Change. For a glossary of climate change acronyms and terms, see http://unfccc.int/essential_background/glossary/items/3666.php#.

Being able to rapidly access financial resources after a natural disaster is crucial for saving lives and livelihoods. Traditional post-disaster response financing, however, covers only a fraction of disaster losses. To address this shortfall, disaster risk-pooling involves a proactive and more cost-effective approach to financial planning, which involves planning ahead to better manage the cost of disasters, ensure predictable and timely access to much needed resources and ultimately protect national budgets from the adverse impacts of disasters.

For tackling climate change-related challenges, policymakers have various tools at their disposal, although given the nature of climate change, international collaboration is necessary to deal effectively with this challenge.

Governments in some OECD and Latin American countries estimate and publish tax compliance gaps, but this is not the case in the Asia-Pacific region. There is, however, much evidence that the identification and the registration of taxpayers are weak in many countries, and that underreporting or misreporting of incomes is widespread. For instance, in Pakistan the number of active personal income filers is fewer than 1 million, significantly below the 5.7 million people reportedly earning above the income tax threshold. In countries where agricultural income receives special tax treatment, taxpayers tend to abuse the legislation by declaring business income as agricultural income.

This aspect is consistent with the economic literature on tax evasion, which suggests that taxpayers decide whether and how much to evade taxes based on the expected probability of detection as well as the penalty if detected and the potential gains if undetected (Allingham and Sandmo, 1972; Kleven and others, 2011). The use of technology could increase the probability of detection, subject to access to relevant information. Tax laws typically include provisions that enable tax officials to obtain information from taxpayers and other parties on request, and to gain adequate access to taxpayers’ accounting books and records. A notable exception is the Philippines, where repeal of the Secrecy of Bank Deposits Law is currently under way.

Jurisdictions undertaking first exchanges by 2017 or 2018 include: Australia; Azerbaijan; China; Cook Islands; Hong Kong, China; India; Indonesia; Japan; Marshall Islands; Macao, China; Malaysia; Nauru; New Zealand; Pakistan; Republic of Korea; Russian Federation; Samoa; Singapore; Turkey; and Vanuatu.

For specific country examples, see PwC and World Bank (2017).

Similar studies have been conducted in other states of India and similar results were found, for instance in Bihar (Banerjee and others, 2016). Similarly, under Pakistan’s Benazir Income Support Programme, 4.5 million beneficiaries receive their payments through debit cards linked to a biometric identity database (World Bank, 2016).

For instance, in the Philippines, a UNICEF programme helped to gather real time data on maternal and child health indicators, using mobile telephones, and consolidate the data to help the local government make informed and well-planned decisions on health issues, especially in geographically isolated and disadvantaged areas. In India, the implementation of e-government projects to manage land records and issue copies of the record of ownership, which are used to obtain crop loans from banks, resulted in a reduction in the citizens’ cost of accessing such services by 100 rupees per service transaction, after incorporating costs, such as the number of trips to the delivery point, waiting time and payment of bribes (Bhatnagar, 2014).

Countries with special needs comprise least developed countries, landlocked developing countries and small island developing States.

Estimates on infrastructure investment needs contained in ADB (2017c) also show that needs are higher in Central Asia, the Pacific and South Asia, which are the subregions that are home to many countries with special needs.


In a study by Smith (2016), it was estimated that the amount would be $364 billion between 2016 and 2030.

For more details about both initiatives, see ESCAP (2017d).
REFERENCES


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The shaded areas of the map indicate ESCAP members and associate members.

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The Economic and Social Survey of Asia and the Pacific Year-end Update 2017 contains data and information on the latest macroeconomic trends, while identifying emerging risks and challenges and taking stock of economic and structural policy developments in the Asia-Pacific region. Its aim is to provide policy recommendations for policymakers, civil society and academia.

Economic growth in the region has picked up momentum in 2017, supported by stronger exports and robust household spending. Private investment, however, remains weak amid overcapacity and corporate and banking debt overhang in some major economies. The growth outlook for 2018 is broadly stable, mainly underpinned by growing domestic consumption. While rising intraregional demand is expected to support output growth, its strength may be clouded by increasing trade protectionism in the region and beyond.

Despite generally positive economic prospects, consumption-led economic growth amid loose monetary policy could aggravate overleveraging and is a source of financial vulnerability. Strengthening financial regulation and supervision should be one of the policy priorities in going forward.

Given that fiscal sustainability is not a concern in most Asia-Pacific countries, fiscal policy should continue playing an active role in lifting domestic demand and supporting development priorities. Its effectiveness will depend on fiscal management and good governance, both of which can be enhanced by using information technology to reshape the environment in which Governments operate.

To achieve the 2030 Agenda for Sustainable Development, higher wages supported by productivity gains, job creation, especially for youth and women, and improving environmental sustainability are critical. Moreover, as achieving the 2030 Agenda requires a significant increase in investments, Governments need to adopt innovative ways to enhance fiscal space, broaden participation of the private sector and promote deepening of capital markets.