

ECONOMIC AND SOCIAL COMMISSION FOR ASIA AND THE PACIFIC

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**ADDRESSING THREATS TO DEVELOPMENT: KEY CHALLENGES TO
INCLUSIVE AND SUSTAINABLE ECONOMIC AND SOCIAL
DEVELOPMENT IN THE ASIA-PACIFIC REGION: ADDRESSING THE
FINANCIAL CRISIS AND ITS CONVERGENCE WITH OTHER THREATS
TO DEVELOPMENT: TOWARDS A STABLE AND SUPPORTIVE
FINANCIAL SYSTEM FOR DEVELOPMENT**

(Item 9 (a) of the provisional agenda)

**ANALYSIS OF REGIONAL IMPACT AND POLICY RESPONSES
TO THE CRISIS: UPDATE**

Note by the secretariat

Addendum

Introduction

1. The present document is issued under sub-item (a) of item 9 of the provisional agenda entitled “Addressing threats to development: key challenges to inclusive and sustainable economic and social development in the Asia-Pacific region”, as an addendum to document E/ESCAP/65/30. Given the rapidly evolving nature of the financial crisis, the purpose of the present addendum is to provide members and associate members of the Commission with an updated regional analysis on the impact of the economic crisis, policy responses and secretariat initiatives. The update covers the period from 15 January to 5 April 2009.

I. IMPACT OF THE CRISIS ON ASIA AND THE PACIFIC

2. The crisis has moved rapidly from stage one (financial crisis with its source in developed countries and limited contagion in Asia and the Pacific) to stage two (Great Recession in developed countries and inevitable contagion in Asia and the Pacific).

3. Stage two is characterized by plummeting exports, from the double-digit growth of the past decade to double-digit declines (table 1), declining domestic demand and rising unemployment.

4. While the region has to date shown remarkable crisis resilience, having implemented wide-ranging reforms following its own financial crisis in 1997, banking sector vulnerabilities remain on the radar because a further deepening of the crisis in the manufacturing sector would lead to financial sector stresses, for example, through a rise in non-performing loans.

5. Even more alarming is the accelerating decrease in imports. For example, in China, the year-on-year decline was 43.1 per cent in January 2009. Given the regionally integrated nature of the production base in South-East and East Asia, these import declines reflect the beginning of an industrial crisis, and it is expected that future export growth will continue to be negative for some time to come.

Table 1. Export performance of selected ESCAP developing economies
Value of exports, year-on-year percentage change

	2008			2009		
	Oct	Nov	Dec	Jan	Feb	Mar
China	19.1	-2.2	-2.8	-17.5	-25.7	--
Hong Kong, China	9.4	-5.0	-10.8	-21.3	-23.0	--
Taiwan Province of China	-8.3	-23.3	-41.9	-44.1	-28.6	-35.7
India	-12.1	-9.9	-1.1	-15.9	-21.7	--
Japan	-6.4	-15.8	-20.0	-35.3	-41.4	--
Malaysia	-6.7	-11.0	-20.1	-33.9	-25.5	--
Philippines	-14.8	-11.4	-40.3	-40.6	--	--
Republic of Korea	7.8	-19.5	-17.9	-34.2	-18.3	-21.2
Singapore	-5.0	-15.4	-22.0	-40.2	-29.1	--
Thailand	5.2	-18.6	-12.5	-26.5	-11.3	--

Source: CEIC database.

Note: Derived from figures in United States dollars.

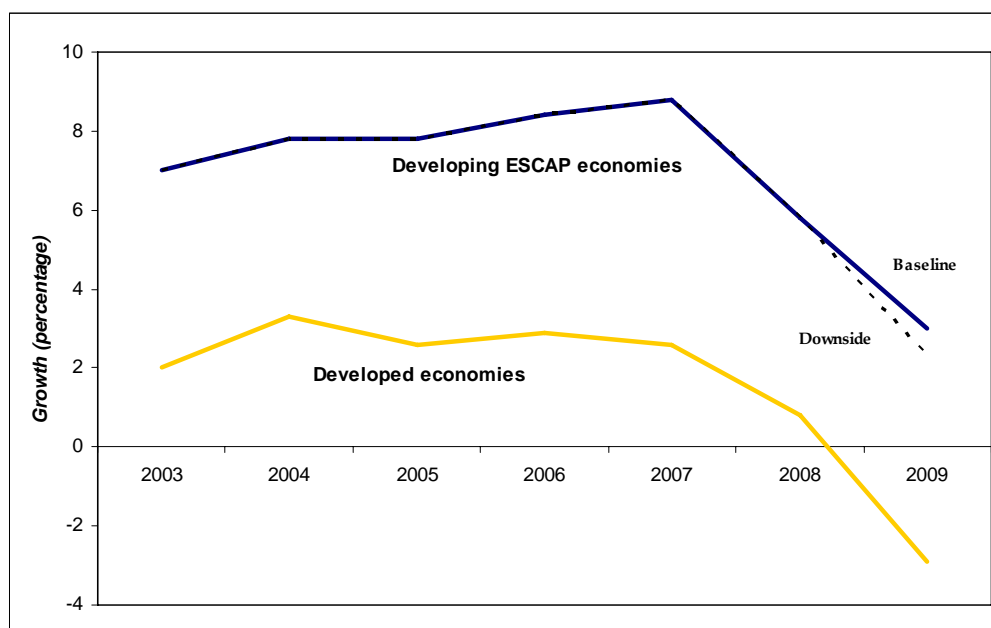
6. Despite aggressive countercyclical fiscal and monetary policy measures implemented at the global level, the economic outlook over the past three months darkened further globally, so that the recourse that mitigated the economic crisis in 1998—boosting exports to developed countries—lost all its prior effectiveness. Even intraregional trade had limited cushioning effects because more than 80 per cent is made up of trade in manufactures parts and components that are in turn linked to demand for final consumer products in recession-hit developed countries. Economies with enterprises that are most directly linked through vertically integrated production networks supplying markets in the United States of America and the European Union, such as China; Hong Kong, China; Malaysia; the Republic of Korea; Singapore and Thailand, are those experiencing the strongest downward pressure on economic growth.

7. As the crisis unfolds, it is estimated that unemployment in the Asia-Pacific region could increase by as much as 23 million workers in 2009. Rising unemployment, particularly in the manufacturing sector, will have a disproportionate effect on the most vulnerable segments of the population and on the least developed countries in the region.

8. A particularly worrisome signal on the trade front is growing protectionist pressures in recession-hit countries, where, for example, preferential treatment favouring domestic sourcing of inputs over imports—often as conditionalities imposed on bailout packages, or additional subsidies, notably those given to support declining farm incomes in developed countries, could distort market-entry conditions for exports from the Asia-Pacific region.

9. Growth will be severely impacted across Asia and the Pacific. Developing economies are projected to grow at 3 per cent in 2009 as compared to 5.8 per cent in 2008, with significant downside risks (figure 1). There will also be considerable variation in performance across subregions. It is expected that the relatively resilient economies will be those that have (a) domestic demand shares that are more important than the export sector, and (b) significant room to enact expansionary fiscal and monetary policies.

Figure 1. Real gross domestic product growth of selected developing ESCAP economies and developed economies, 2003-2009

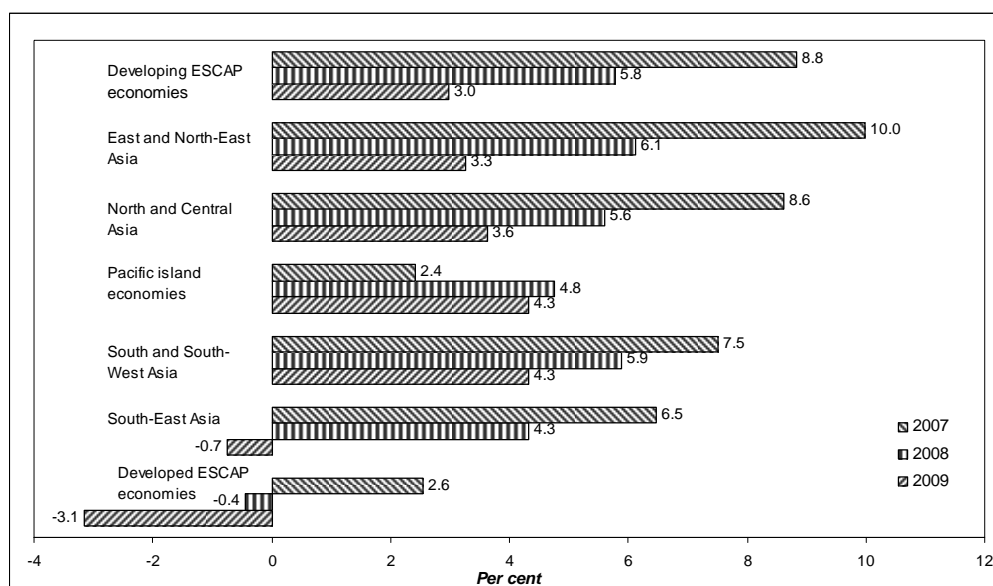


Sources: Calculated based on national sources; IMF, International Financial Statistics CD-ROM (Washington, D.C., November 2008); ADB, *Key Indicators for Asia and the Pacific 2008* (Manila, 2008); website of the CIS Inter-State Statistical Committee, <www.cisstat.com>, 3 February 2009; and ESCAP estimates and forecasts. Figures for developed economies are extracted from World Bank, *World Development Indicators* database and *Global Economic Prospects 2009*, Forecast update (March 30, 2009).

Notes: GDP growth for 2008 and 2009 are estimates and forecasts respectively. Developed economies refer to high-income economies.

10. For these reasons, China and India are among the countries expected to provide an anchor of economic growth in 2009, albeit at a much slower pace than in 2008. Among all developing subregions, GDP growth is expected to be the slowest in South-East Asia, plummeting further to -0.7 per cent in 2009. Growth forecasts for East and North-East Asia have also been revised downwards, to 3.3 per cent for 2009 (figure 2).

Figure 2. Rates of economic growth of selected developing and developed ESCAP economies, 2007-2009



Sources: ESCAP, based on national sources; International Monetary Fund, *International Financial Statistics CD-ROM* (Washington, D.C., November 2008); Asian Development Bank, *Key Indicators for Asia and the Pacific 2008* (Manila, 2008); Economic Intelligence Unit, *Country Reports and Country Forecasts*, various issues (London, 2008); data from the Interstate Statistical Committee of the Commonwealth of Independent States, accessed from www.cisstat.com on 30 March 2009; and ESCAP estimates and forecasts.

II. REGIONAL RESPONSES TO THE CRISIS AND POLICY GAPS

A. Monetary policy and its limitations

11. At the onset of the crisis, most economies in the Asia-Pacific region turned to monetary policy as the first line of defence against the economic downturn. However, the conventional method of aggressive interest rate cuts to inject liquidity into the financial system has reached its limits in some economies. Deflationary pressures combined with negative growth and close to zero interest rates have reduced the effectiveness of monetary policy, in particular in developed countries. Unconventional and still untested measures in developing countries may need to be considered and implemented in these economies if the downturn deepens and inflation moves into negative territory in the region. For example, Thailand's inflation rate in 2009 is forecast at zero per cent.

B. Fiscal policy: a key policy response

12. A key issue for the region is how Asia and the Pacific will use fiscal policy in 2009. Countries across the region have implemented a wide variety of fiscal stimulus packages. These packages have shown diverse approaches, depending on the level of development and the national priorities of countries: for example, in China and India infrastructure spending with employment-creating activities to support domestic demand features prominently. Support for small- and medium-scale industries and private consumption in Japan and a Green New Deal in the Republic of Korea are given emphasis. The *Economic and Social Survey of Asia and the Pacific 2009* contains information on the salient features of fiscal stimulus packages announced

in the Asia-Pacific region.¹ The scale of fiscal stimulus has also varied widely depending on the state of budget deficits in particular countries. Most countries will have significant flexibility to undertake expansionary policies due to relatively solid budgetary situations and an easing of monetary policy due to moderating inflation but not all countries have this flexibility. Whereas China has enacted the largest plan in the region, of nearly 13 per cent of GDP and second only to the United States in absolute size, some other major economies, such as India, have large existing budget deficits (estimated to rise to 6 per cent in 2008). Other South Asian economies also face strained fiscal positions together with inflationary pressures, while developed countries in the region are hampered by long-term structural recession, deflationary pressures and fiscal deficit. For example, Japan's public debt currently represents 170 per cent of GDP and is expected to rise.

13. A major concern in the region is that fiscal stimulus packages do not pay sufficient attention to social protection programmes. Fiscal stimulus packages have been largely confined to job creation programmes and to boosting consumption, with less spent on the protection of those who become unemployed. The coverage of basic social protection programmes remains very low in the Asia-Pacific region. It is estimated that only 20 per cent of the population has access to health-care assistance, only 30 per cent of the elderly receive pensions and only 20 per cent of the unemployed and underemployed have access to labour market programmes. Given the more immediate and consistent countercyclical effects of social protection programmes, using fiscal stimulus packages to create an effective social floor can bring about the desired outcome of boosting consumption, stabilizing macroeconomic conditions and, by reaching the most vulnerable segments of the population, strengthening the social foundations of society.

C. Strengthening cooperation at the regional and global level: recent developments

14. As attention turns from immediate crisis-fighting measures to building resistance to future crises, reform of the global financial architecture is under intense debate. The leaders of the Group of Twenty (G-20), who met at the London Summit on 2 April 2009, agreed, inter alia, to increase the resources of the International Monetary Fund through, among other things, a general allocation of Special Drawing Rights which will inject \$250 billion into the world economy, and to support an increase in lending by multilateral development banks of at least \$100 billion. In addition, they agreed to establish a new Financial Stability Board that expands membership of the previous Financial Stability Forum to the G-20 countries, among others.² The leaders have imparted a political momentum that will ensure that these issues remain at the top of the international agenda for some time to come. Although there are a number of actions that each country could take independently, it is highly unlikely that any one country can ride out this crisis on its own.

15. At the regional level as well, coordinated monetary and fiscal responses have greater credibility and help to shore up confidence while enhancing regional and global multiplier effects. The crisis response to managing financial vulnerability in Asia and the Pacific should be focused on regional policy measures while also maintaining an active role in the design of the evolving multilateral financial

¹ United Nations publication, Sales No. E.09.II.F.11; see pp. 100, 111, 119, 132, 142 and 148.

² See the Washington Declaration of the Summit on Financial Markets and the World Economy, 15 November 2008 (available at www.londonsummit.gov.uk/en/summit-aims/washington-follow-up/washington-declaration1); and The Global Plan for Recovery and Reform, communiqué of the London Summit, 2 April 2009 (available at www.londonsummit.gov.uk/resources/en/PDF/final-communique).

architecture. Furthermore, coordinated responses will enable countries to institute measures to “insulate themselves from regulatory and macroeconomic failures in systemically significant countries”, as recommended by the Commission of Experts of the President of the United Nations General Assembly on Reforms of the International Monetary and Financial System at its first meeting, held in New York from 4 to 6 January 2009.³ Exchange rate coordination and, closely related to this, the challenge of managing vulnerability to reversals in short-term capital flows would benefit from the establishment of more coordinated and durable regional arrangements.

16. The agreement between the Ministers of Finance of the ASEAN+3 countries reached in Phuket, Thailand, on 22 February 2009 in preparation for the Fourteenth ASEAN Summit, which provides for accelerating the implementation of a multilateral pool of foreign exchange reserves, is an important first step in regional financial cooperation. The agreement paves the way for the conversion of the existing bilateral fund of \$80 billion into a multilateral pool of \$120 billion, with 80 per cent of the new funds being provided by the +3 countries, while the remainder will come mainly from the more developed ASEAN economies. Nevertheless, many issues remain unresolved.

17. This facility needs to evolve further before it serves the purpose of a region-wide insurance system from the standpoint of geographical coverage, scale of resources and institutional linkages. Many countries that are most in need of such assistance lie outside the ASEAN+3 area. The pool should be further expanded so that the potential use of funds goes beyond balance-of-payments support to include support for banking liquidity and solvency problems. Furthermore, in the event of contagion, size matters, as requests for assistance from multiple countries would curtail its functioning and lead to a potentially devastating loss of confidence in the very reason for its existence. The importance of expanding arrangements such as the ASEAN+3 reserve facility was highlighted by the Commission of Experts of the President of the United Nations General Assembly on Reforms of the International Monetary and Financial System in January 2009.

18. The curtailment of trade has been exacerbated by the lack of trade credit. This trade-oriented region is the only one in the world that does not have a regional institution specifically dedicated to export credit and export credit guarantees. There should be an accelerated process of analysis and dialogue in order to establish such a facility. The announcement by the Government of Japan that a \$1 billion fund would be set up through the Japan Bank for International Cooperation, in collaboration with the Asian Development Bank, is an important step in the right direction. The announcement made at the London Summit that the G-20 countries would ensure the availability of at least \$250 billion over the next two years to support trade finance further underlines the importance of reinvigorating world trade and investment to restore economic growth.

D. The role of ESCAP

19. The secretariat has been at the forefront of analysing the impacts of the global financial and economic crisis on the Asia-Pacific region. To support the regional process of designing appropriate policy solutions and to assist regional economies to improve monitoring systems, the secretariat is expanding its existing analytical work. The recently published *Economic and Social Survey of Asia and the Pacific 2009* contains a more detailed discussion on these issues.

³ The recommendations are available at www.un.org/ga/president/63/commission/firstmeeting.pdf.

20. At the G-20 London Summit, the leaders entrusted the United Nations with the task of establishing a mechanism to monitor the impact of the crisis on the poorest and most vulnerable. The secretariat, together with the secretariats of the other regional commissions, will play an integral part in that United Nations system monitoring mechanism.

21. Furthermore, the Executive Secretary, as the current Coordinator of the regional commissions, has on various occasions stressed that action at the regional level is part of the solution to the crisis, as demonstrated by several regional responses. Consequently, the Executive Secretary has advocated for the secretariat to play a central role, together with the secretariats of the other regional commissions, in the design and implementation of operational responses by the United Nations system in support of the countries in their regions, including in providing policy advice as a “second opinion” for policy options in response to the crisis.

22. In this regard, the secretariat is coordinating, together with the secretariats of the other regional commissions, the preparatory process of the regional commissions for the high-level Conference on the World Financial and Economic Crisis and Its Impact on Development to be held in New York from 1 to 3 June 2009.

23. To assist countries and the global community to confront the crisis, accelerate recovery and build a fair and inclusive globalization allowing for sustainable economic, social and environmental development for all, nine joint United Nations system initiatives have been agreed upon. The secretariat, within its existing mandate, has been called upon to actively participate in the following four initiatives:

(a) A Social Protection Floor: ensuring access to basic social services, shelter and empowerment and protection of the poor and vulnerable;

(b) A Global Jobs Pact: boosting employment, production, investment and aggregate demand, and promoting decent work for all;

(c) A Green Economy Initiative: promoting investment in long-term environmental sustainability and putting the world on a climate-friendly path;

(d) Monitoring and analysis: strengthening macroeconomic and financial surveillance and implementing an effective economic early warning system; and urgently establishing a United Nations system-wide vulnerability monitoring and alert mechanism to track developments and report on the economic, social and environmental dimensions of the crisis.

24. In line with the above, the secretariat will serve as a forum for exploring policy options and forging consensus on regional policy coordination in an effort to see the region emerge from crisis resilience to crisis resistance.

25. Members and associate members of the Commission may wish to provide the secretariat with guidance on its programme of work and recommend further activities that the secretariat should pursue.

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