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Agenda Item: 7

Making Growth Work for the Poor: The Challenge of Inclusive Growth

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4-5 February 2015

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Making Growth Work for the Poor: the Challenge of Inclusive Growth

Presentation to the APEC Economic Committee First Plenary Meeting - Clark, Philippines, February 2015

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Contents

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Global trends

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Global outlook: disappointments and divergences

- **World economy**
  - *Global recovery:* slow-moving
  - *Three drivers:* low commodity prices; easy financial conditions; but weak global trade
- **Country groups**
  - *Major Economies:* Upswing in U.S. and U.K.; setbacks in Euro Area and Japan; managed slowdown in China
  - *Developing Economies:* New divergences (commodity exporters vs importers); medium-term growth challenges

Source: Global Economic Prospects, World Bank, January 2015

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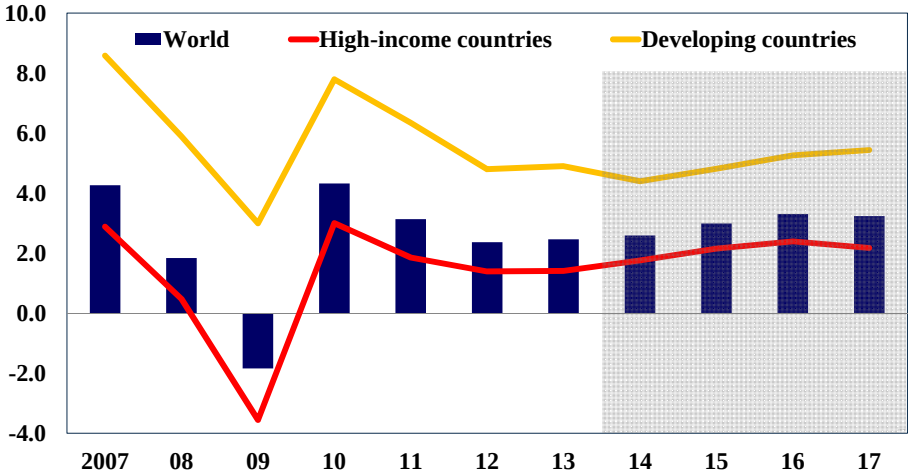
Global recovery: slow moving

GDP growth
(percent)



Source: Global economic prospects

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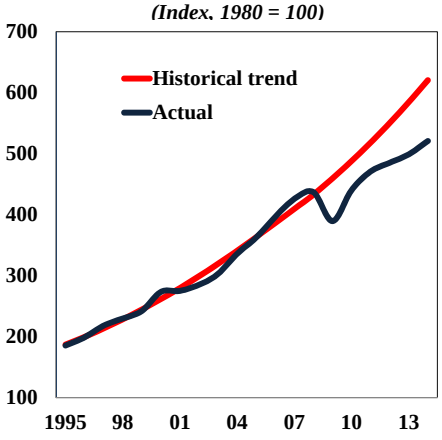
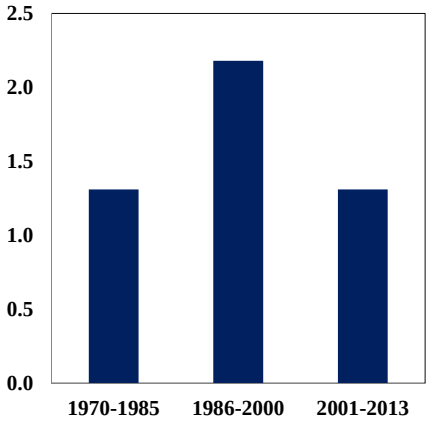
Weak global trade: are we in a new era?

Actual and Trend Import Volume
(Index, 1980 = 100)



Long-Run Trade Elasticity
(Estimates of elasticity)



Sources: World Bank, Constantinescu, Mattoo and Ruta (2014)
Note: Left panel: The post-crisis trend level growth is assumed to be equivalent to the average growth rate during 1980-2008.Using this, the trend level for 2014 is rebased to 100. Hence, bars below or above 100 show deviations from trends in 2014; Right panel: Each bar represents the long-run elasticity estimated from a cointegration model between imports and GDP

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Emerging APEC growth projections: good performance

			Estimate/Forecast		
	2012	2013	2014	2015	2016
East Asia	6.0	6.1	6.0	6.1	6.1
Developing East Asia	7.4	7.2	6.9	6.7	6.7
China	7.7	7.7	7.4	7.1	7.0
Indonesia	6.3	5.8	5.1	5.2	5.5
Malaysia	5.6	4.7	5.7	4.7	5.1
Philippines	6.8	7.2	6.1	6.5	6.5
Thailand	6.5	2.9	0.5	3.5	4.0
Vietnam	5.2	5.4	5.6	5.6	5.8
APEC	3.7	3.4	3.3	3.6	n/a
Emerging APEC	7.0	6.6	6.2	6.3	n/a
Advanced APEC	2.3	2.1	2.0	2.4	n/a
Selected APEC economies					
Mexico	4.0	1.1	2.1	3.3	3.8
Chile	5.5	4.2	2.0	3.3	n/a
Peru	6.0	5.8	2.4	4.8	5.5
World	2.4	2.5	2.6	3.0	3.3
High-income countries	1.4	1.4	1.8	2.2	2.4
Developing countries	4.8	4.9	4.4	4.8	5.3

Sources: World Bank - Global Economic Prospects and IMF - World Economic Outlook

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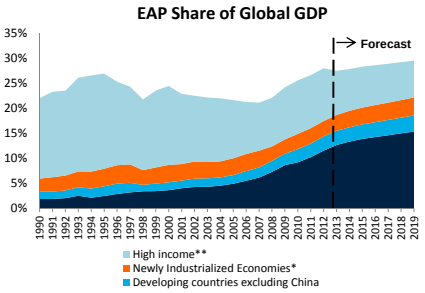
East Asia Pacific (EAP): global driver of growth

- **EAP accounts for over 25% of world nominal GDP, and its share will continue to rise.**
  - At current real growth rates of 7% annually, developing EAP countries will add a further $7 trillion by 2019: China 2nd largest economy, Indonesia 10th
  - Connected through trade and FDI with all regions
- **China will remain growth driver in the region and globally.**
  - Growth model being recalibrated to emphasize economic and environmental sustainability
  - Focus on land, labor, and capital market reforms
- **Regional integration is increasing.**
  - ASEAN integration this year presents opportunities for furthering reforms
  - Nearly 50% of FDI in ASEAN countries originates within EAP
  - TPP, APEC: opportunities to increase the other 50%
- **Challenges and Risks**
  - Need to move forward with structural reforms and investments to raise factor productivity and address vulnerabilities



*Includes Hong Kong SAR, China; Taiwan, China; Singapore; and Korea, Rep
**Includes Japan, Australia, New Zealand, and Brunei

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Global goal to reduce extreme poverty to a 3% headcount by 2030: Business as usual will not get us there.

Global Poverty in 2030 at $1.25 per day (2005 PPP), assuming unchanged inequality

Scenario	Headcount (percent)	Number of poor (million)
Average income growth of 4% p.a. in each country	3	252
Each country sustains avg per capita growth during past 20 years	6.8	573
Each country sustains avg per capita growth during past 10 years	4.8	405.4
Each country sustains avg per capita growth during past 10 years (survey-based growth)	6.7	564.8

Source: World Bank, 2014, *A Measured Approach to Ending Poverty and Boosting Shared Prosperity*

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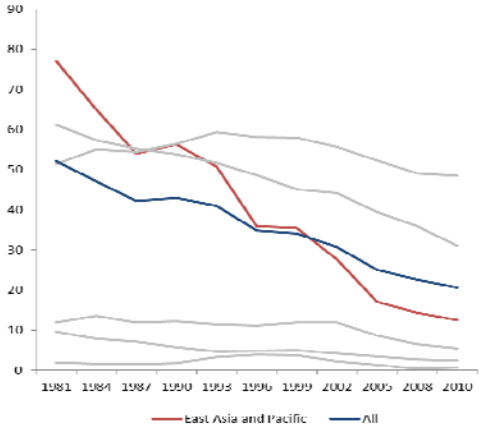
But extreme poverty has fallen faster in EAP than in any other region.

Extreme poverty ($1.25 a day) (percent of the population)



Shared prosperity in EAP and other regions

Regions	Shared Prosperity (2005-2010)[a]	Growth rate of bottom 40%[b]
Africa	33.3%	2.4%
East Asia & Pacific	**55.6%**	**5.7%**
Eastern Europe & Central Asia	59.3%	5.2%
Latin America & Caribbean	82.4%	5.0%
Middle East & North Africa	80%	2.2%
South Asia	83.3%	3.1%

a/ Percentage of countries with growth in mean income of bottom 40% positive and greater than growth in mean income of total population
b/ Median of growth rates of average real per capita income of the bottom 40%

Source: Interim Global Database of Shared Prosperity (I-GDSP)
*Note: * annualized growth in income/consumption computed only for those countries where the latest household survey is no older than 2008, and there is a comparable survey (5 +/-2) years prior to the latest survey.*

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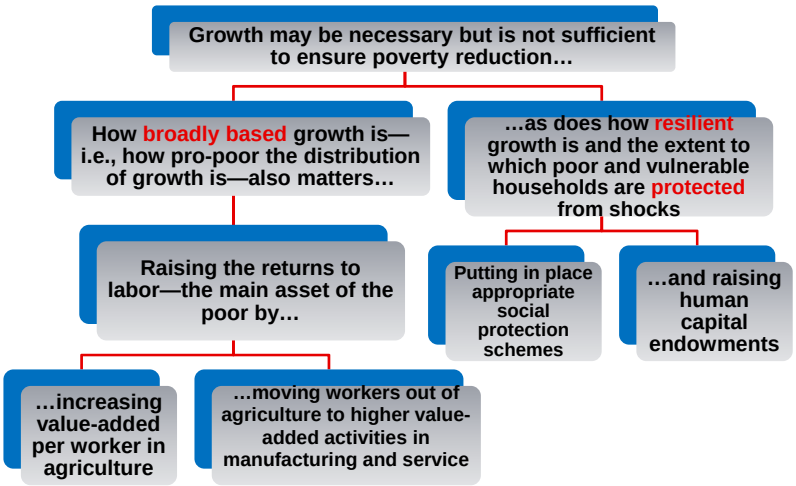
Inclusive growth challenge: In addition to extreme poverty reduction, need to create more and better jobs



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Structural transformation: essential for inclusive growth

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The normal pattern of economic transformation

- **Before economic transformation takes off, agriculture:**
  - Large shares in economic output and the labor force
  - But the share in economic output *less* than its share in the labor force
  - *Lower* productivity of labor than in industry and services.
- **Industrial growth takes off:**
  - Industry, and in particular manufacturing, increases its share in the economy
  - Pulls labor out of agriculture more or less rapidly
- **In advanced economies, this transformation will reduce the shares of agriculture in GDP and in the labor force to very small numbers.**
- **This transformation is now taking longer and longer, because manufacturing has become less labor-intensive.**

Sources: Kuznets and Chenery, and Timmer, 2009

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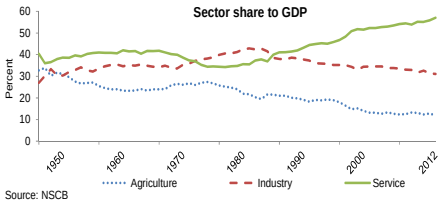
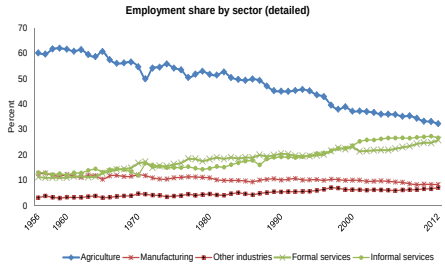
Structural transformation: Philippines' incomplete process

- Long history of policy distortions has slowed the growth of agriculture and manufacturing in the last six decades.
- Incomplete structural transformation
- Agricultural productivity has remained depressed, manufacturing has failed to grow sustainably, and a low-productivity, low-skill services sector has emerged as the dominant sector of the economy.



Source: NSCB



Source: LFS

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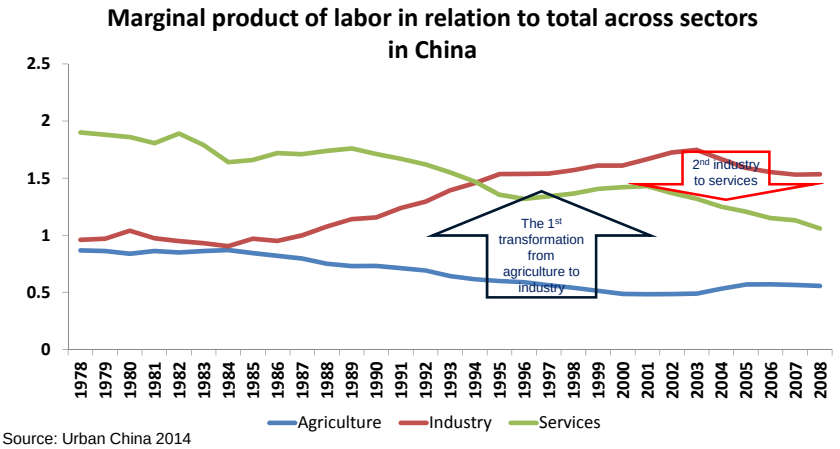
Structural transformation:
China lifted 600 million people out of poverty
300 million people moved from farms to factories.



Source: Urban China 2014

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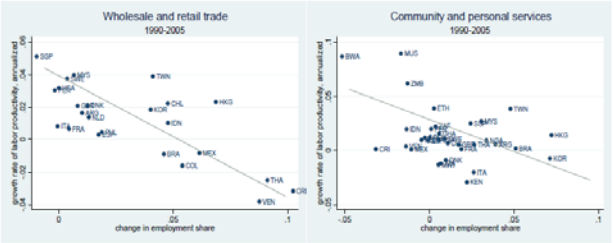
Dani Rodrik's pessimism:
services taking over from manufacturing as jobs engine
"old" export-driven growth strategies

Not many examples of productivity growth and employment expansion in services



Service sectors that have best productivity performance typically shed labor; labor absorbing sectors typically have worst productivity performance.

- Growth in the future will have to come the hard way, through economy-wide improvement in capabilities
  - requiring broad-based investments in human capital and institutions
- Potential growth rates will be lower in the future

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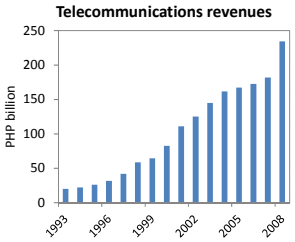
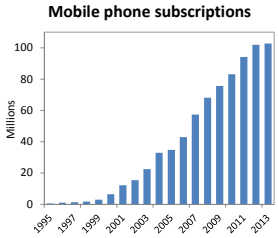
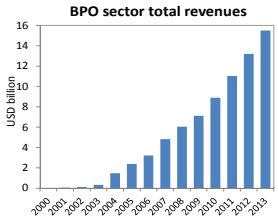
Services:
Philippines has a booming service sector with 5 million direct jobs created



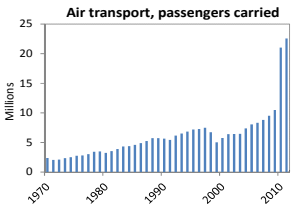
Sources: Securities and Exchange Commission (SEC)



Source: WDI



Source: Business Processing Association of the Philippines (BPAP)



Source: WDI
Note: Data include passengers of both domestic and international flights.

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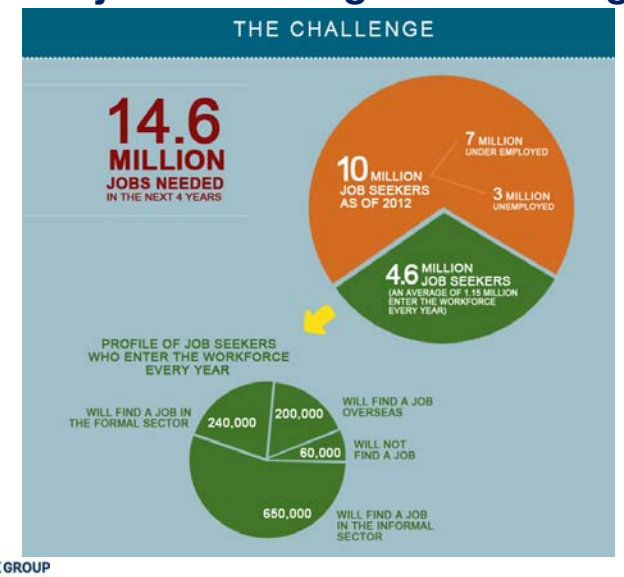
But that is not enough: the jobs challenge is daunting



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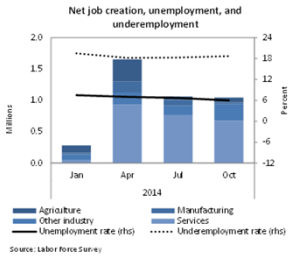
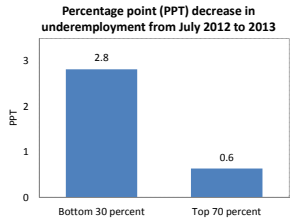
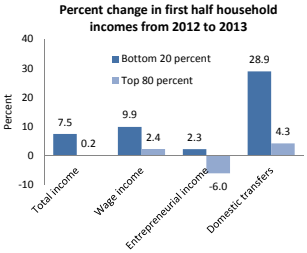
Sustained economic growth has begun to translate into stronger job creation and faster poverty reduction.

- Over a million jobs were created between October 2013 and October 2014 (latest labor force survey).
- Unemployment declined to its lowest level in 10 years at 6 percent.
- The improvement in poverty incidence in 2013 is supported by higher growth of real income and lower underemployment among poorer households compared to the rest of the population.





Sources: PSA, World Bank staff computations
Note: Data refer to July estimates from the linked 2012 FIES-LFS and the 2013 APIS-LFS.



Sources: PSA, World Bank staff computations
Note: Data refer to first semester estimates from the 2012 FIES and the 2013 APIS.

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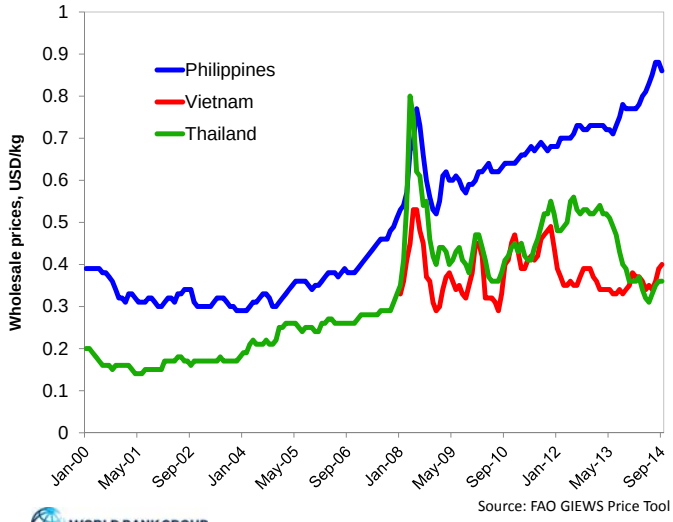
Need to enhance competition: example of rice trade



In September 2014, 1kg of rice cost PHP 41 in Philippine supermarkets. Consumers in Vietnam were paying the equivalent of PHP 16.

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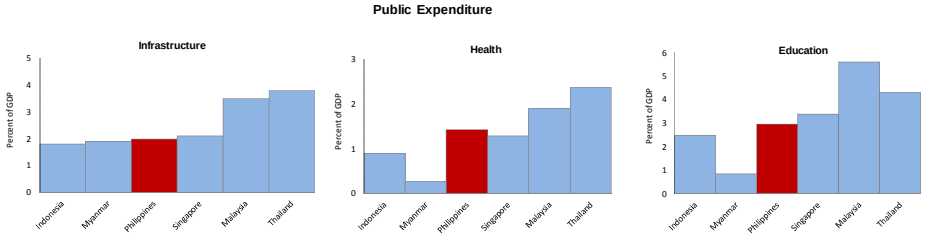
Need to invest more in infrastructure, education and health

However, the Philippines has an investment deficit

- Spending on infrastructure, health and education has been lower than in some neighboring countries.
- Low spending has contributed to weak health outcomes and lower quality of education, and tremendous traffic.
- More revenues needed to sustainably ramp up spending



Source: WDI and ADB estimates
Notes: Education and health figures are from 1995 to 2012 (Some countries have missing values for certain years.). Infrastructure data is from 2008 to 2012.

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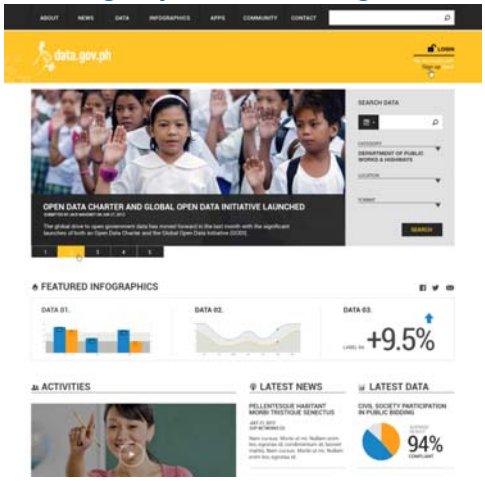
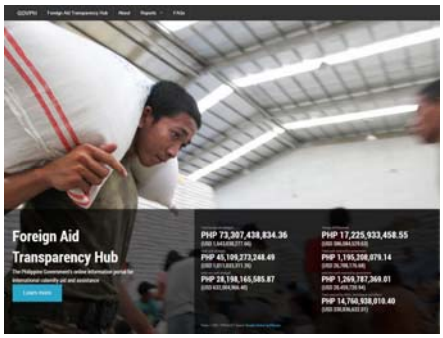
But:

citizens will demand more transparency in return for paying more taxes

data.gov.ph – over 600 government data sets are now public





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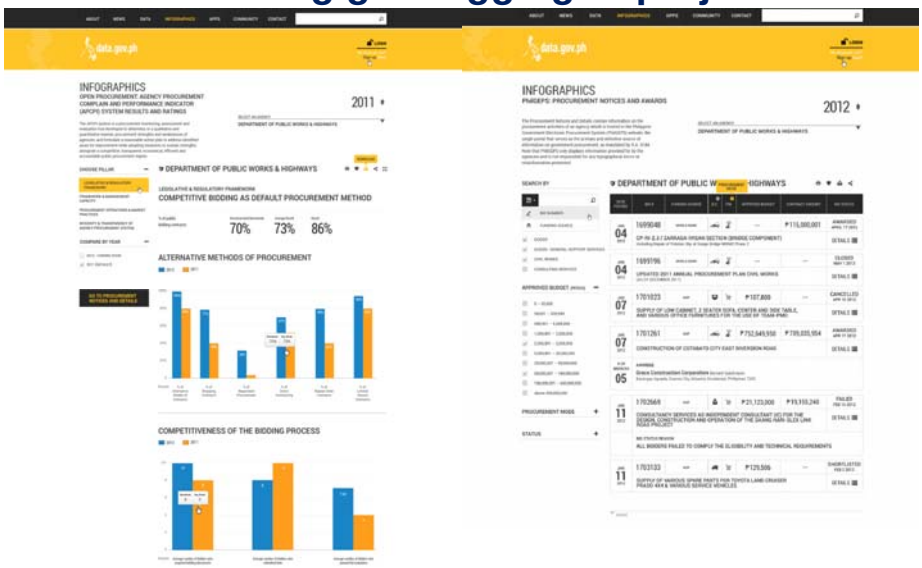
More transparency in procurement …including geo-tagging of projects



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Domestic reforms can be anchored in international partnerships: Open Government Partnership (OGP)

- Single Access Window for Data and suite of digital accountability platforms
- Convergence of diverse and group of actors, processes and technologies.
- Policy Framework for Open Government
- Workshop in Manila/Official launch
- OGP Summits in London and Indonesia

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Reform challenges and coalitions for inclusive growth

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East Asia and Pacific: Structural challenges

Social vulnerabilities

- About 300 million people live on $2 to $1.25/day, 140 million below $1.25/day
- Poverty pockets in MICs (i.e. ethnic minorities)—harder to reach
- High poverty rate, child and maternal mortality in LICs (Mongolia, Timor-Leste, Myanmar)
- Income inequality high in some countries

Barriers to growth & jobs

- Financial and external vulnerabilities
- High informality, low factor productivity
- Gender gap in economic opportunity
- Impediments to doing business
- Lack of access to formal finance
- Skills and training for productive jobs
- Aging population in most MICs

Huge infrastructure needs & urbanization

- 130 million have no access to power (more than half in Indonesia)
- 600 million lack access to adequate sanitation
- Rapid migration to cities generating pressure on service delivery, including infrastructure
- Large urban slums, pollution
- Relatively low private sector engagement in infrastructure

Natural disasters & climate change

- Over 70% of world's natural disasters (e.g. Philippines Typhoon Yolanda)
- 13 of world's 30 most climate affected countries
- Generates 1/3rd of global CO2 emissions
- Depletion of forests and fisheries

Governance & service delivery

- Weak institutions, corruption
- Lack of transparency of government budgets
- Weak service delivery at sub-national level

Conflicts at regional and national levels

- Potential for escalation of territorial tensions
- Sub-national conflicts (Philippines, Mindanao; Southern Thailand)
- Myanmar ethnic minorities

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However, the challenge of inclusive growth is not to identify lists of reforms… To implement reforms, coalitions are needed

- The challenge is not in identifying lists of specific reforms and calling for strong leadership and political commitment to implement…
- The challenge is in fostering a broad coalition of stakeholders which supports the reform package, because they anticipate that inclusive growth makes everybody better off in the long run, even if some will face losses in the short run.
- Because given the political economy, *individual, specific* reforms will face strong opposition from vested interests.

  Example: sin tax reform or rice policy reform in the Philippines
- These coalitions can form at many levels and around many themes.
- International partnerships, such as APEC, can be part of such reform coalitions.

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Thank you

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