Economic and Social Survey of Asia and the Pacific 2024

Boosting affordable and longer-term financing for governments

Launch event
4 April 2024
Overall steady economic performance is masking declining purchasing power of people and rising poverty and socioeconomic inequalities.

Increasing public investments for SDGs is looking difficult, due to higher government borrowing costs and shorter loan maturities.

Domestic policy measures related to taxes and capital markets can help lower borrowing costs and boost supply of long-term capital.

International development partners – donors, multilateral development banks and credit rating agencies – can revisit their approaches to increase affordable and long-term financing.

Fiscal policymakers need to keep in view global megatrends (such as demographic shifts, climate change and technological advancements) while pursuing affordable and long-term financing.
Macroeconomic prospects and challenges
Steady, yet below-trend GDP growth and declining, yet relatively high inflation

Source: ESCAP estimates and projections as of February 2024.
Subdued post-pandemic job recovery and weaker purchasing power

Number of persons employed (Q4/2019 = 100)

- Accommodation and food services
- ICT
- Manufacturing
- Wholesale and retail

Declines in inflation-adjusted national minimum wages in 2022 (%)

- Türkiye
- Sri Lanka
- Lao PDR
- Samoa
- Palau
- Vanuatu
- Republic of Korea
- Bangladesh
- Thailand
- Nepal
- India
- Pakistan
- Solomon Islands
- Kiribati
- Timor-Leste
- Philippines
- Cambodia
- China
- Marshall Islands

Source: ESCAP, based on CEIC.
Source: ESCAP, based on ILOSTAT database.
Increase in poverty and income inequality

Millions of people in Asia-Pacific who could have been pushed into poverty in 2022

$2.15 per day

$3.65 per day

Source: ESCAP estimates.

Change in income shares between 2019 and 2022 (percentage points)

Source: ESCAP, based on World Inequality Database.
Key risks to the economic outlook

- **Uncertain inflation trends** and monetary policy stance within Asia-Pacific and beyond
- Weak **debt repayment ability** of households, businesses and governments amid a high interest rate environment
- Uncertainty around economic growth momentum in **China**
- Escalation of **geopolitical tensions** and **trade fragmentation**
The need for affordable and long-term financing for governments in developing Asia-Pacific
Government borrowing costs in Asia-Pacific are rising, with shorter loan maturity.

Average interest on new external debt commitments (%)

- All creditors
- Private creditors
- Official creditors

Average local-currency sovereign bond yields (%)

- United States
- Developing Asia-Pacific

Average maturity on new external debt commitments (years)

- All creditors
- Official creditors
- Private creditors

Source: ESCAP, based on World Development Indicators database and Bloomberg.
Strong macroeconomic fundamentals keep government borrowing costs at low levels

Government borrowing costs have been higher in Asia-Pacific economies with ...

- Higher inflation and policy interest rates
- More volatile exchange rates
- Higher perceived fiscal risks
- Less financial market liquidity

Source: ESCAP analysis.
What can governments do to increase affordable long-term financing?

*Closing the tax collection gaps to reduce fiscal risks*
Low tax-to-GDP ratios and wide tax collection gaps in several Asia-Pacific countries

Source: ESCAP, based on the IMF World Revenue Longitudinal Data set.
Less conventional fiscal policy tools to close the tax gaps

### Property-based fiscal revenue

<table>
<thead>
<tr>
<th>Property tax</th>
<th>Land value capture</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Negligible property tax revenues</td>
<td>▪ Governments could leverage part of higher land and property values brought about by public infrastructure</td>
</tr>
<tr>
<td>▪ A low hypothetical property tax rate of 0.5% with no exemption can generate <strong>sizeable additional fiscal revenue</strong></td>
<td>▪ Complementing property taxes</td>
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<td></td>
<td>▪ Being implemented in <strong>China</strong> and explored in many other regional economies</td>
</tr>
</tbody>
</table>

### Tax morale

**Raising society’s willingness to pay taxes**

- Ensure and communicate that taxes are well spent on development
- Self-pride and image
- Peer and social pressures
- Increase the perceived probability that tax avoidance will be caught
What can governments do to increase affordable long-term financing?

*Boosting and channeling domestic savings to increase supply of long-term capital*
Strengthening capital markets to channel sizeable domestic savings for investment

**Domestic savings (% of GDP)**

- Africa
- Latin America and the Caribbean
- Middle East and Central Asia
- Asia and Pacific
- Europe
- Developed economies

**Capital market development index**

- Africa
- Middle East and Central Asia
- Asia and Pacific
- Europe
- Developed economies

Source: ESCAP, based on World Development Indicators database and IMF Financial Development Index database.

### Further developing capital markets

- Widen the investor base
- Increase secondary market liquidity
- Improve risk-sharing mechanisms
- Protect investor rights
Increasing domestic savings: policy options at country and individual levels

**Domestic savings (% of GDP)**

- **Enhance the ability of households to save**
- **Boost labour productivity**
- **Ensure social protection to cut precautionary savings**

- **Raise household saving rates**
  - Provide financial incentives and platforms
  - Improve financial access and literacy

Source: ESCAP, based on World Development Indicators database.
As domestic policy actions take shape, how can international development partners help?
Donors: towards a larger and fairer concessional finance system

### Provision

- Official development assistance (ODA) in 2022 at **half of the commitment** of 0.7% of gross national income (GNI) made since 1970
- Official **climate finance** should not be counted as part of ODA commitments

### Allocation

- **Bilateral** ODA is often shaped by **historical and political factors**
- **Multilateral** ODA still uses **GNI per capita** as a starting allocation criterion
- The UN-led initiative on the **multidimensional vulnerability index** is a way forward
Multilateral development banks: addressing underutilized resources and capacities

Boost lending capacities

- Increase capital
  - New round of capital injections

- Optimize existing capital
  - Adjust the capital adequacy frameworks

Improve lending terms

- Increase lending in local currencies
  - Now 80% is in US dollar

- Cut administrative burden of loan packages
  - Safeguard assessments for a World Bank project costs $13.5 million on average

Strengthen systemic coordination and resource allocation among MDBs
Credit rating agencies: more development-aligned and long-term sovereign ratings

★★☆☆☆ What should global credit rating agencies do?

- Clearly distinguish judgement-based ratings from those that purely rely on objective information
- Incorporate long-term issues into assessments, e.g. public investment in SDGs raises fiscal credibility
- Increase dialogues with governments and other stakeholders in developing countries to reduce bias

What should international financial and development communities do?

- Reduce mechanistic reliance on credit ratings in making investment decisions
- Explore the idea of setting up a new regional credit rating agency for Asia-Pacific
Wider perspectives: what do **global megatrends** mean to fiscal policymakers?
Global megatrends affect fiscal policy through various channels

Demographic shifts

Climate change and environmental degradation

Technologies and digitalization

Fiscal space and public debt sustainability

Fiscal policy conduct

Revenue
Expenditure
Borrowing cost
Design and implementation
Effectiveness
Potential fiscal impacts are notable, diverse and sometimes uncertain: examples

<table>
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<tr>
<th>(Lower) revenue</th>
<th>(Higher) expenditure</th>
<th>Borrowing cost</th>
<th>Design and implementation</th>
<th>(Lower) effectiveness</th>
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<tr>
<td>Shrinking workforce</td>
<td>Old-age health care and social protection</td>
<td><strong>Higher</strong> inflation</td>
<td>Disaster risk-informed fiscal planning</td>
<td>Old-age consumption responds less to fiscal stimulus</td>
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<td>Lower production capacity</td>
<td>Public investment in climate projects</td>
<td><strong>Green taxes &amp; investment</strong></td>
<td>Digitalizing public financial management</td>
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<td>Profit shifting in digital economy</td>
<td>Post-disaster rebuild of public infrastructure</td>
<td><strong>Output loss due to natural disasters</strong></td>
<td>Stronger multilateral tax cooperation</td>
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<td></td>
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<td><strong>Lower</strong> inflation</td>
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<td><strong>Less demand for durable goods</strong></td>
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Poverty and socioeconomic inequality concerns persist despite steady economic performance.

Urgency of boosting affordable and long-term financing for governments:
- Governments: increase fiscal credibility and the supply of long-term capital
- International development partners: adopt fresh perspectives to guide operations.

Implications of demographic shifts, climate change and technological advancements for fiscal policymaking should not be ignored.