



# Reviving Growth

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## East Asia and Pacific Economic Update, April 2023



**THE WORLD BANK**

East Asia & Pacific • Chief Economist Office

# Structure

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1. Recent developments
2. Prospects for 2023
3. A long view of growth
4. Looming challenges

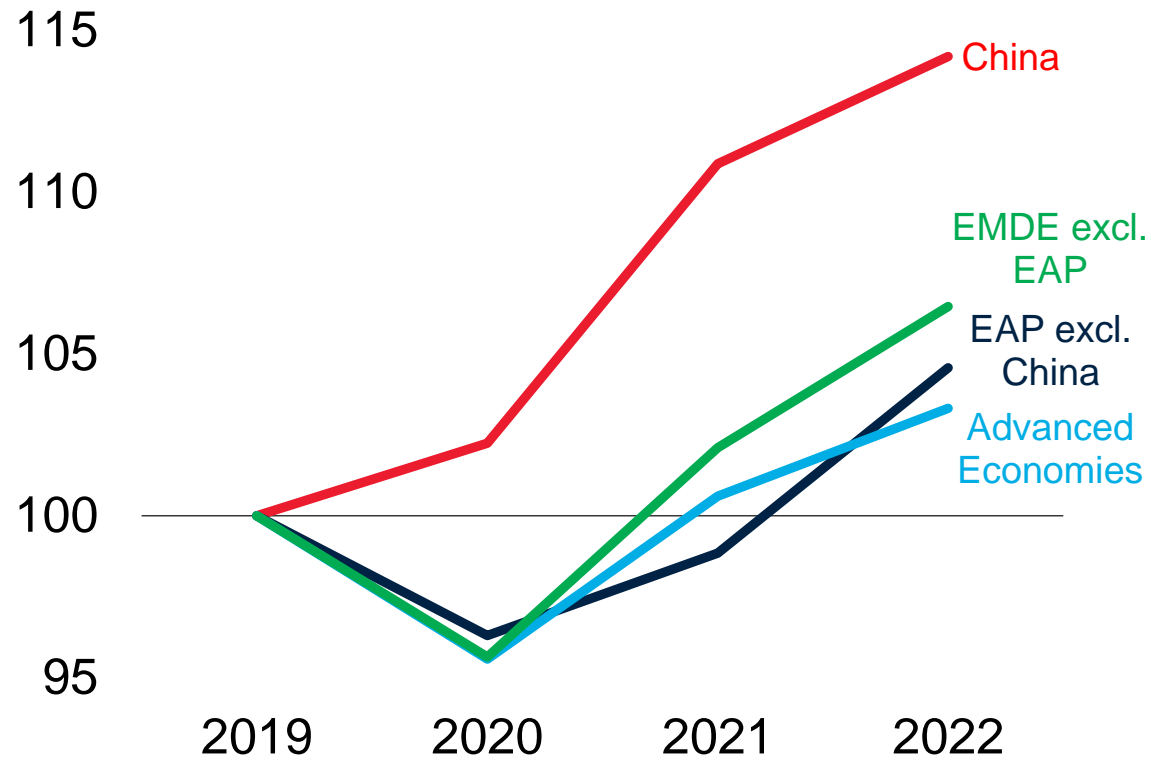
# Recent developments

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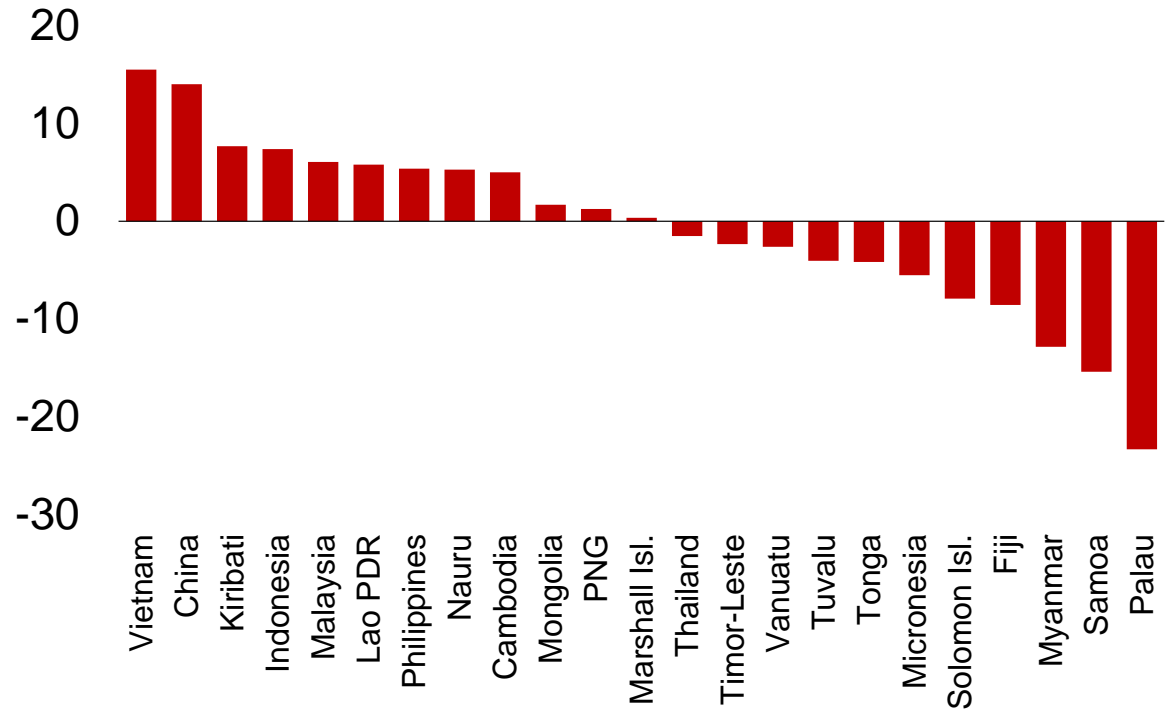
# Most major EAP economies have recovered and are growing, but output in most Pacific Island Countries is still not back to pre-pandemic levels

## GDP relative to pre-pandemic levels

INDEX: 100 = 2019



Percent

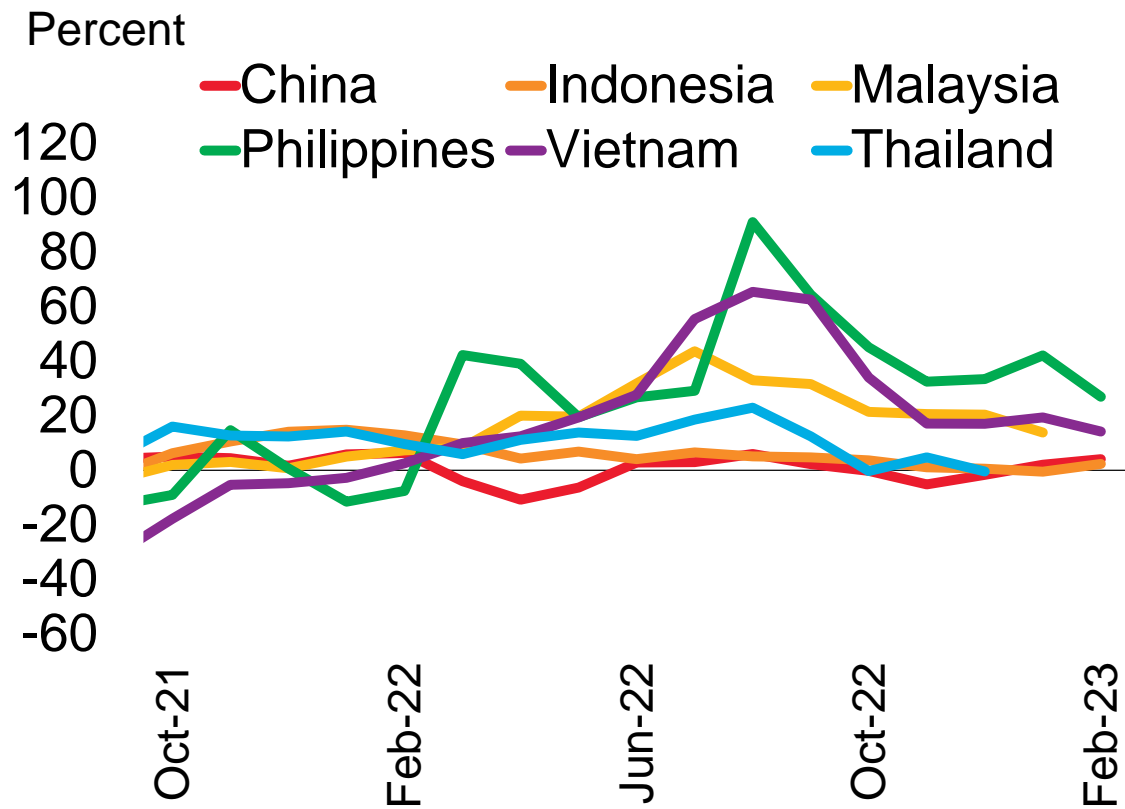


Source: World Bank, Haver Analytics

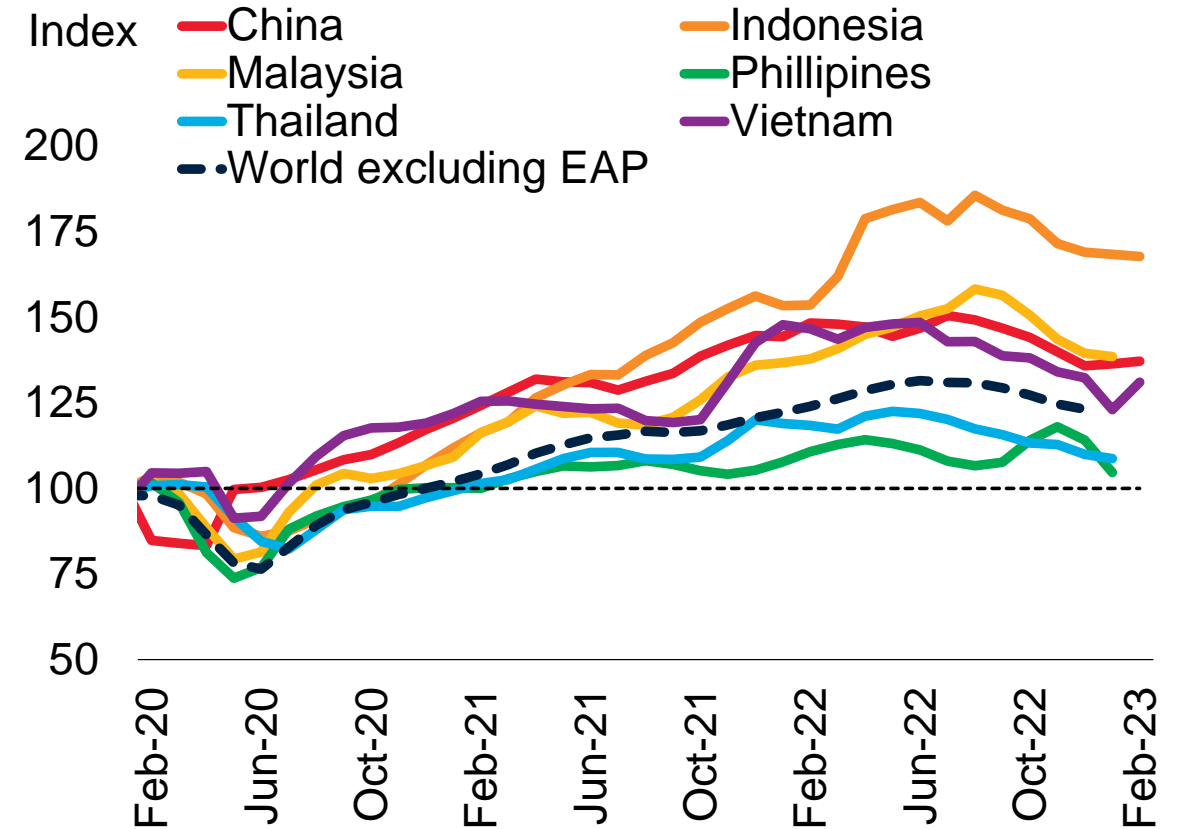
Note: right panel: Bars show the latest quarterly or annual GDP in 2022 relative to 2019 level

# Domestic demand was strong but is now moderating; goods exports were robust but are now declining

## Retail sales (year-on-year growth)



## Goods exports (2019=100)

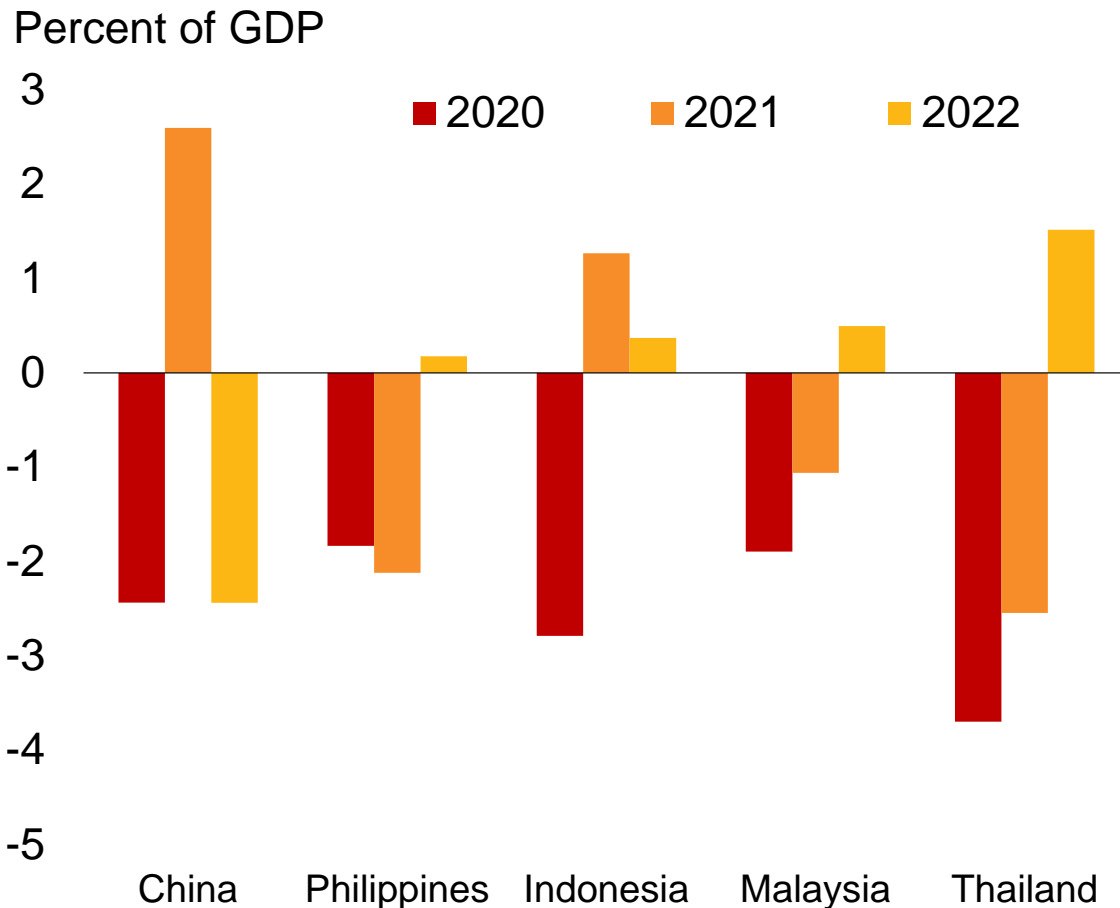


Source: Haver Analytics

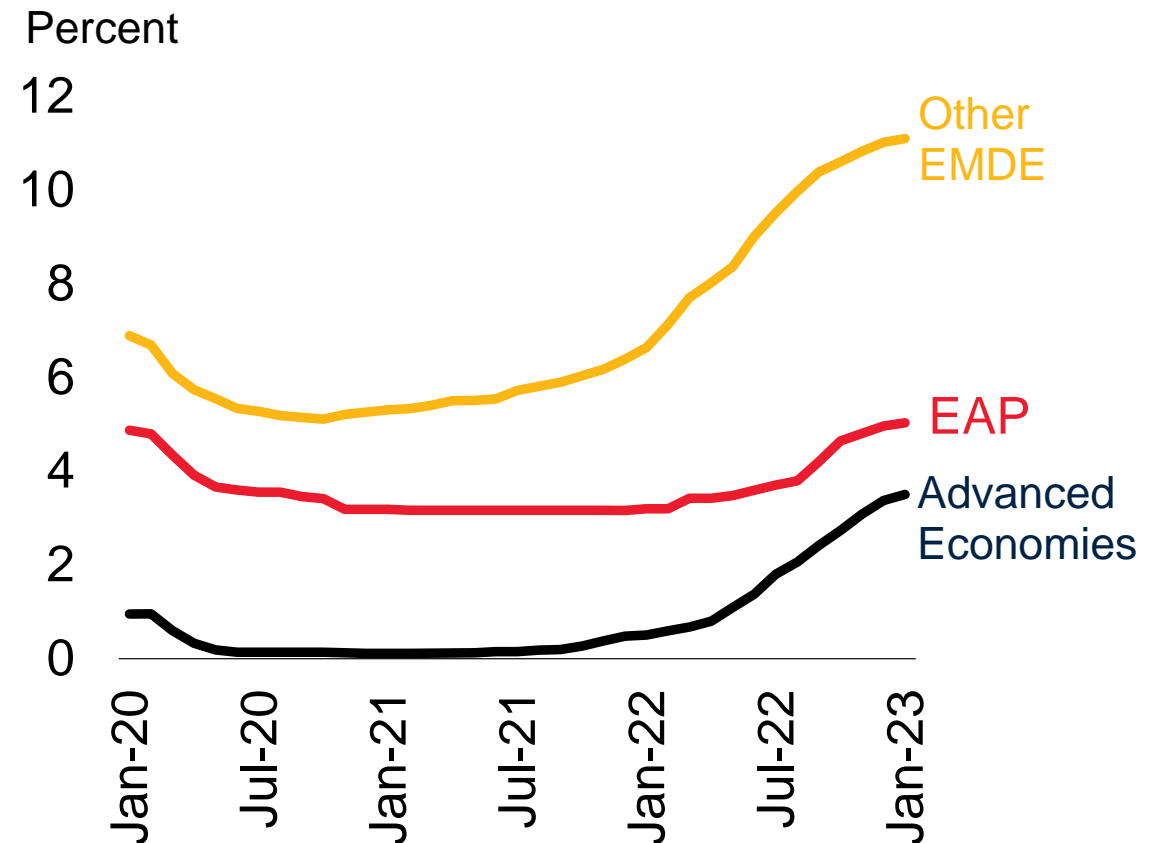
Note: left panel: Philippines refers to auto sales

# Fiscal policy became less expansionary in most countries, and monetary policy began to tighten in 2022

## Change in structural balance



## Policy rates



Source: World Economic Outlook Database, October 2022, Haver Analytics

# Prospects in 2023

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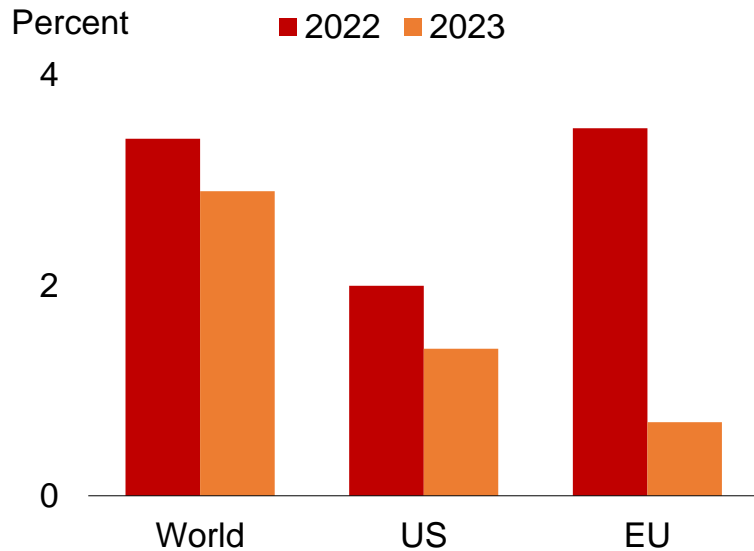
# Three linked international developments will shape economic performance in the EAP countries

Global growth

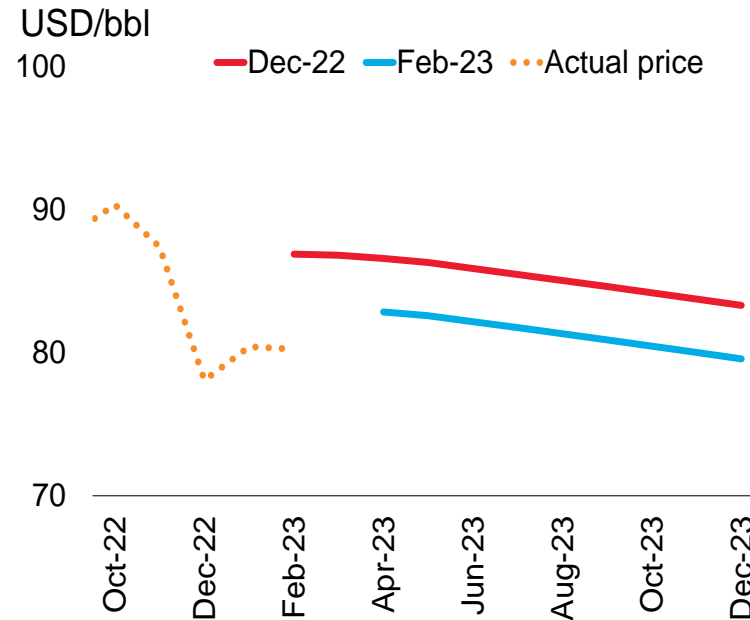
Commodity prices

Financial tightening

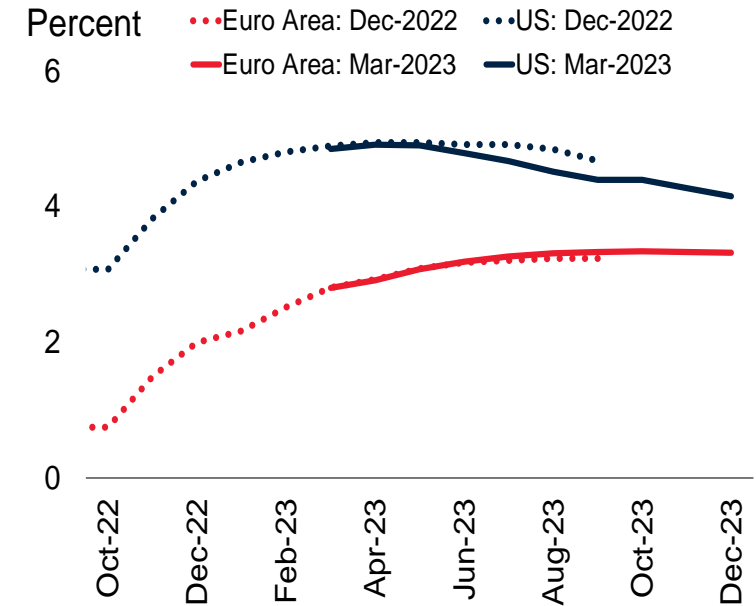
GDP growth



Oil price futures



Expectation of interest rate

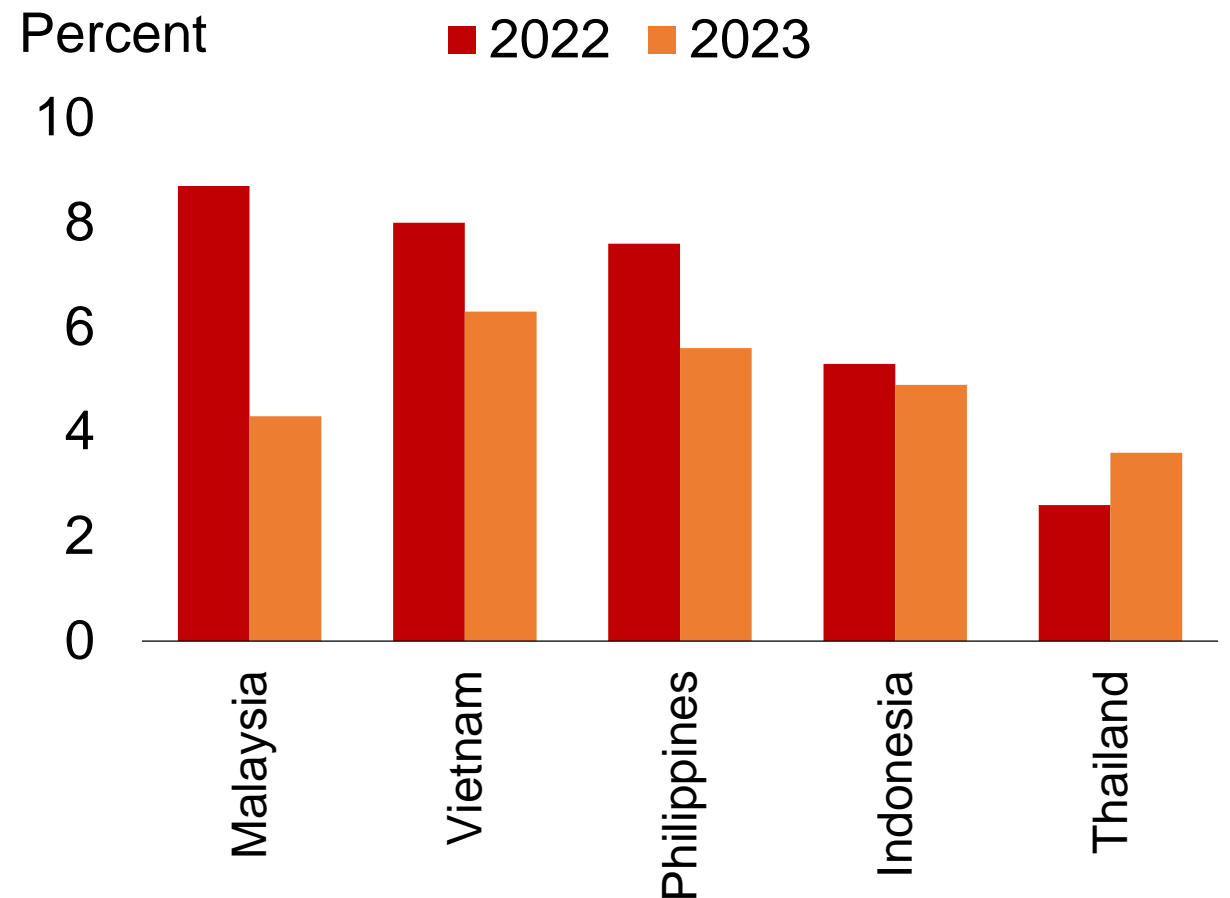
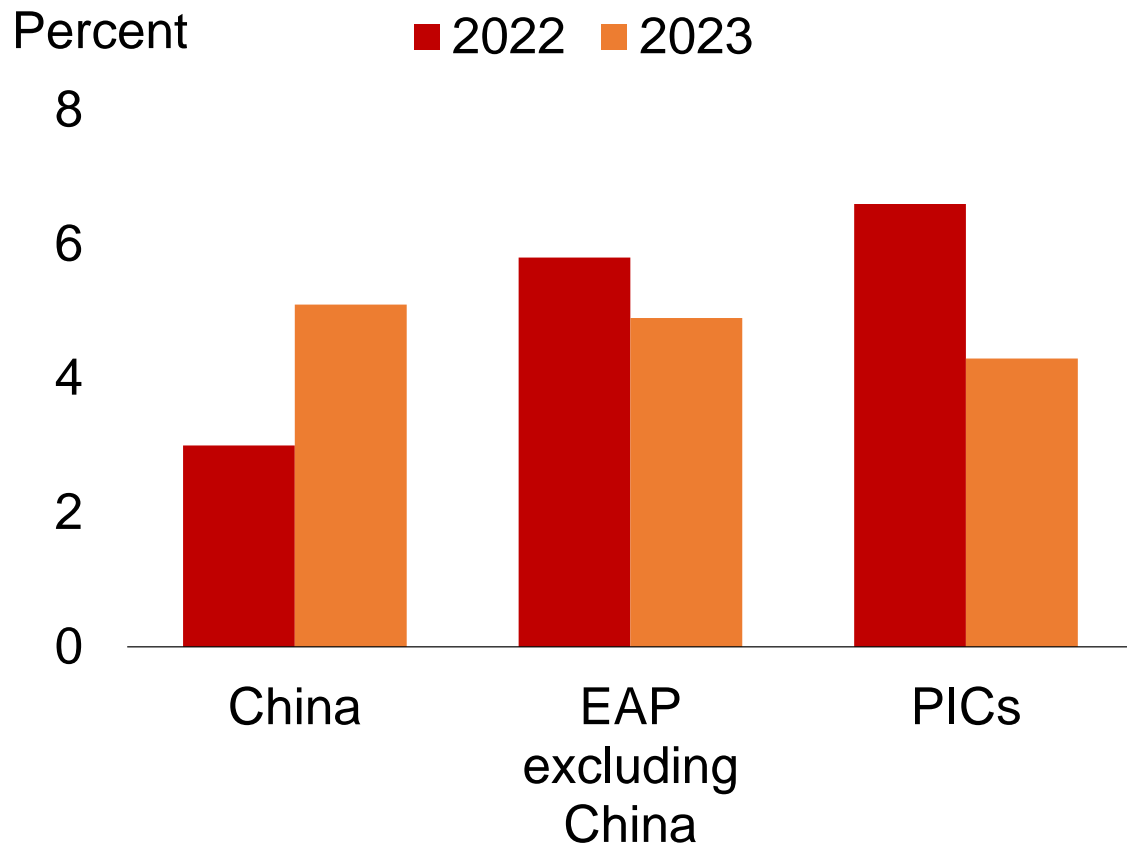


Source: World Bank staff illustration



# China will grow faster in 2023 than in 2022 but much of the rest of the region will slow down

GDP growth in 2022 and 2023 forecast

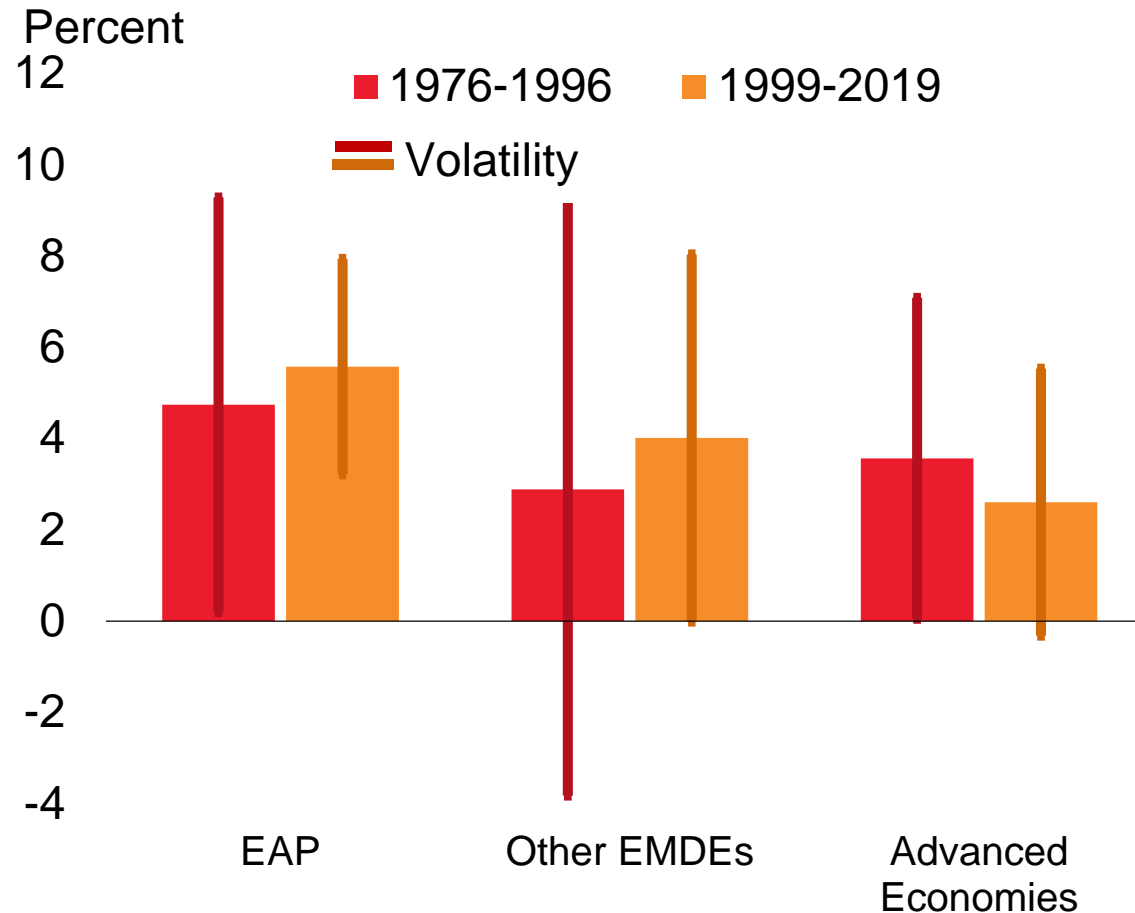


# A long view of growth and structural change

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# EAP countries have seen two decades of higher and more stable growth than other economies

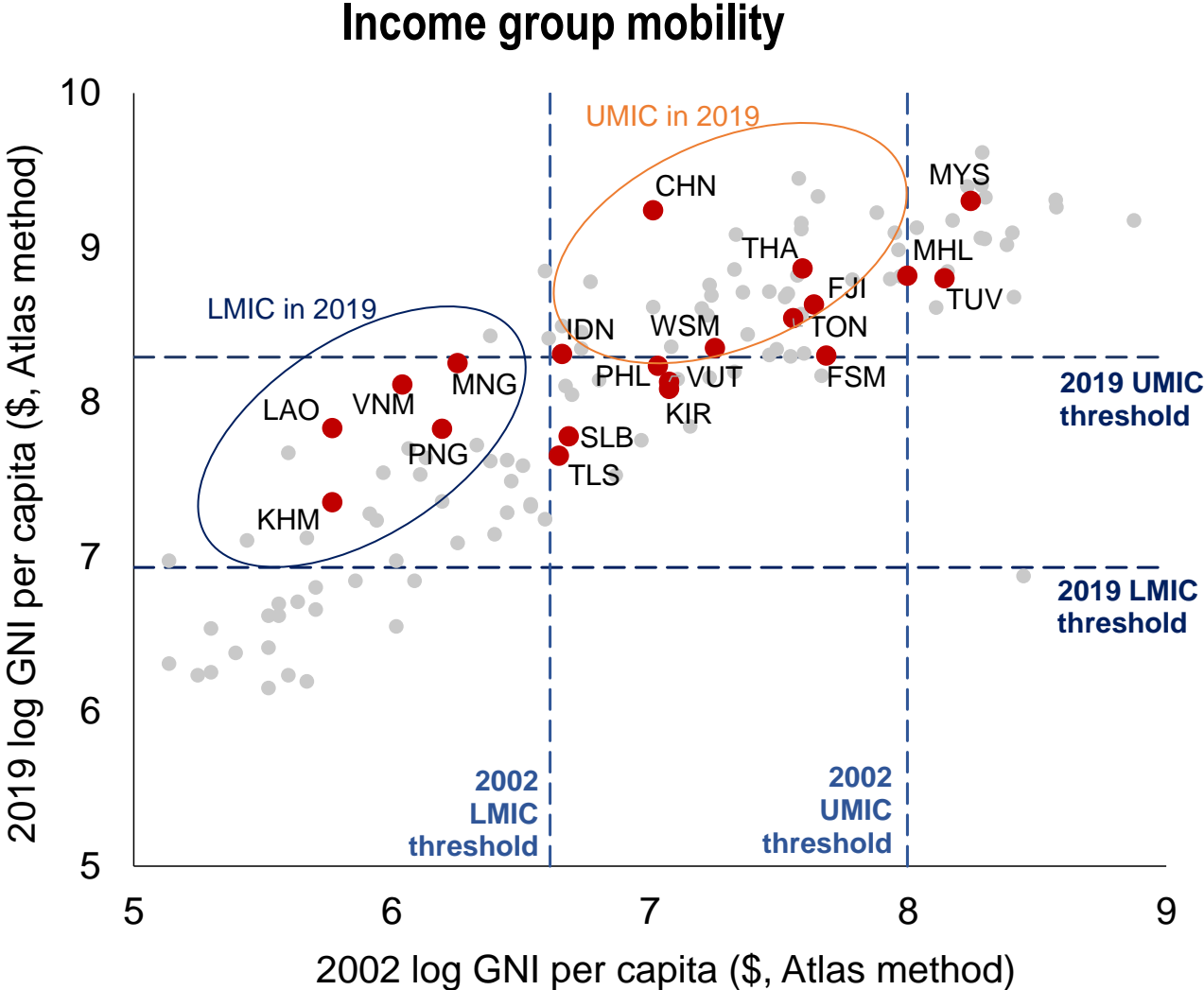
GDP growth and GDP growth volatility



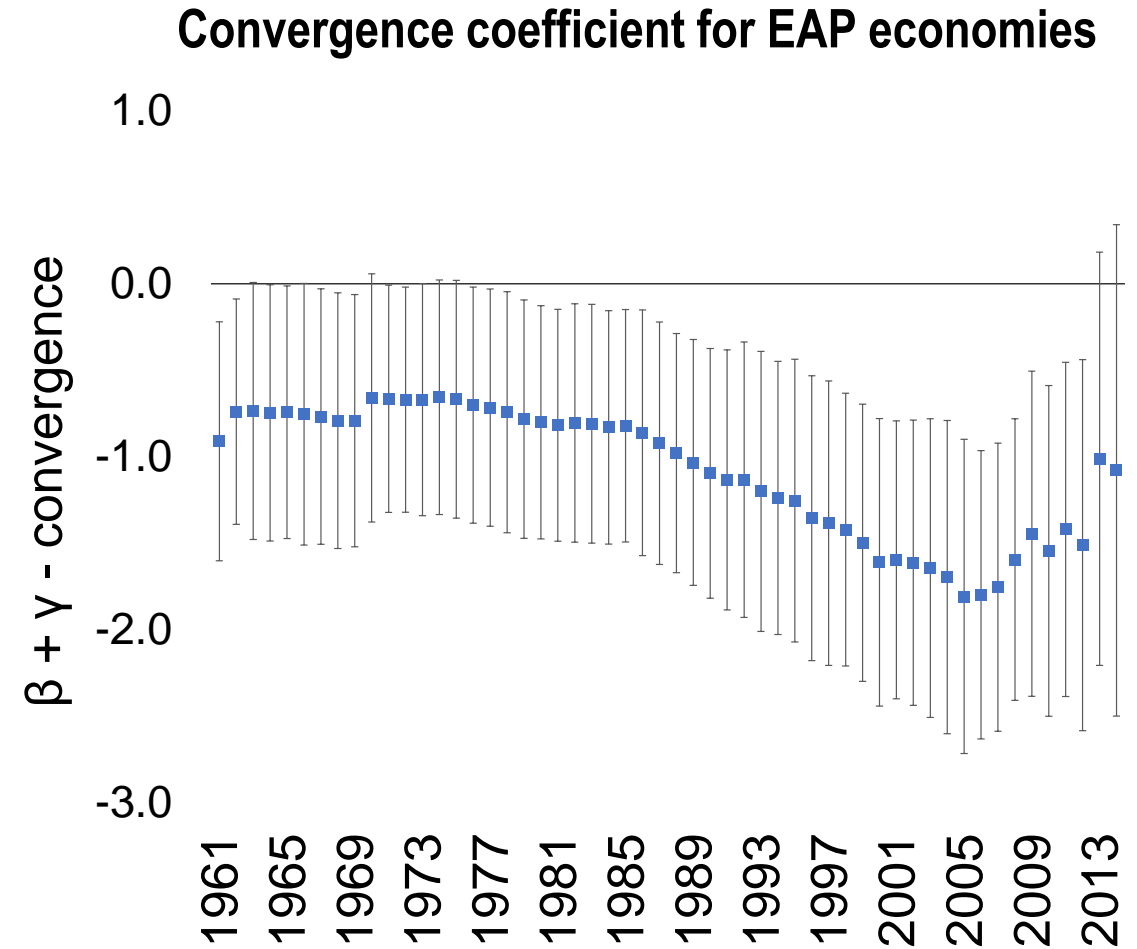
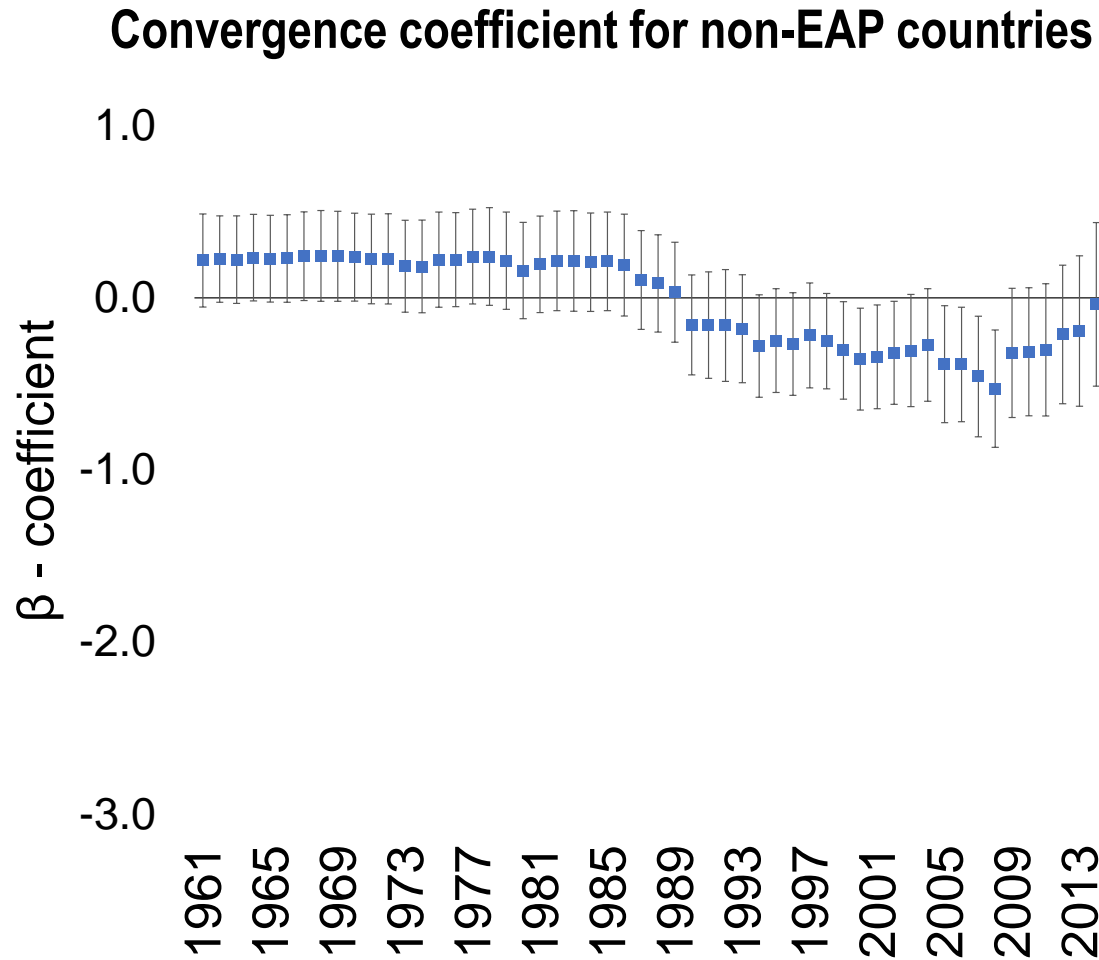
Source: PWT

Note: Bar height shows average annual growth rate; whiskers show average standard deviation over the period.

# Consequently, EAP countries have all transitioned either to lower or upper middle-income status



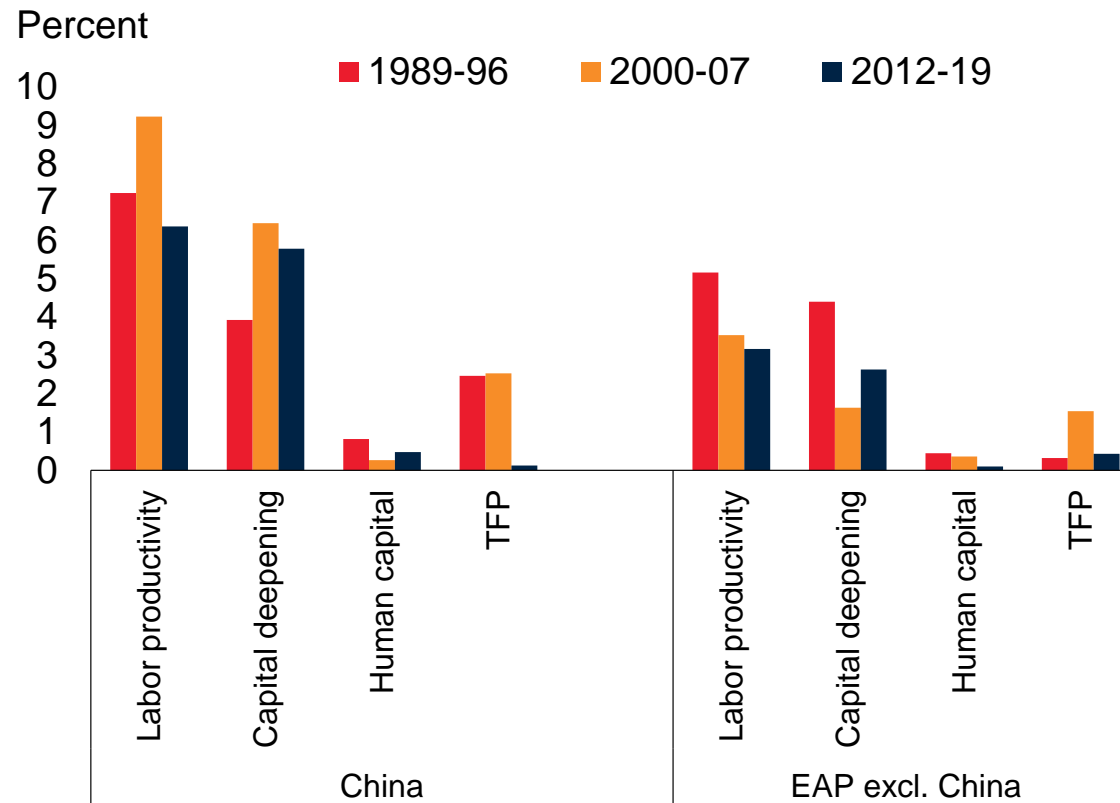
# But EAP convergence with high income countries, which was faster than in other countries, has recently stalled



Note: x-axis denotes initial year.  $\gamma$  represents the marginal effect of convergence in developing EAP while  $\gamma + \beta$  represents the total effect.

# And productivity growth has been declining

## Labor productivity growth and drivers

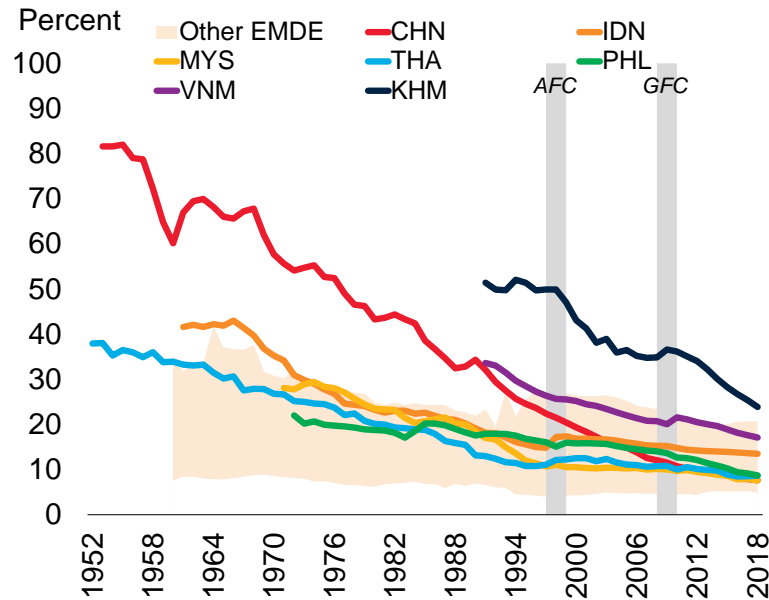


Source: APO Productivity Database; Penn World Tables World Bank

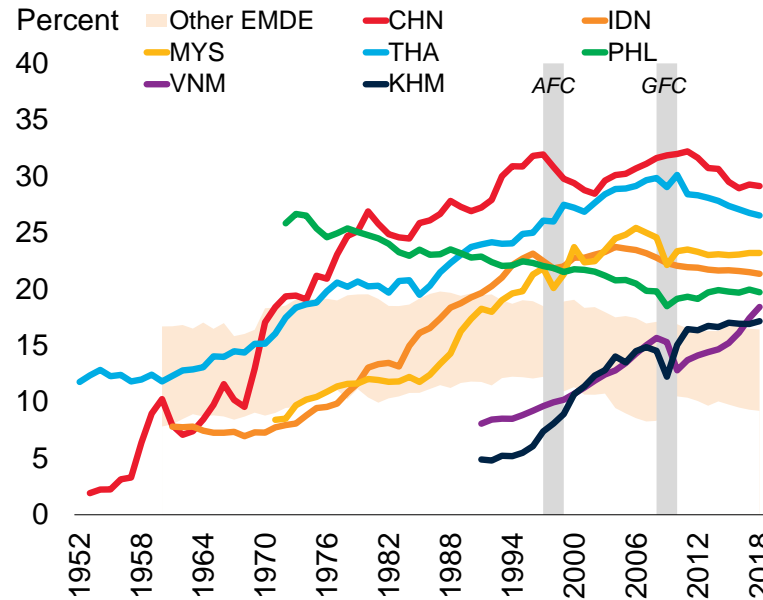
Note: EAP excl. China shows weighted average of ASEAN-4 countries.

# In recent years, the share of manufacturing in GDP declined in EAP economies (other than Cambodia and Vietnam), and the share of services in GDP increased

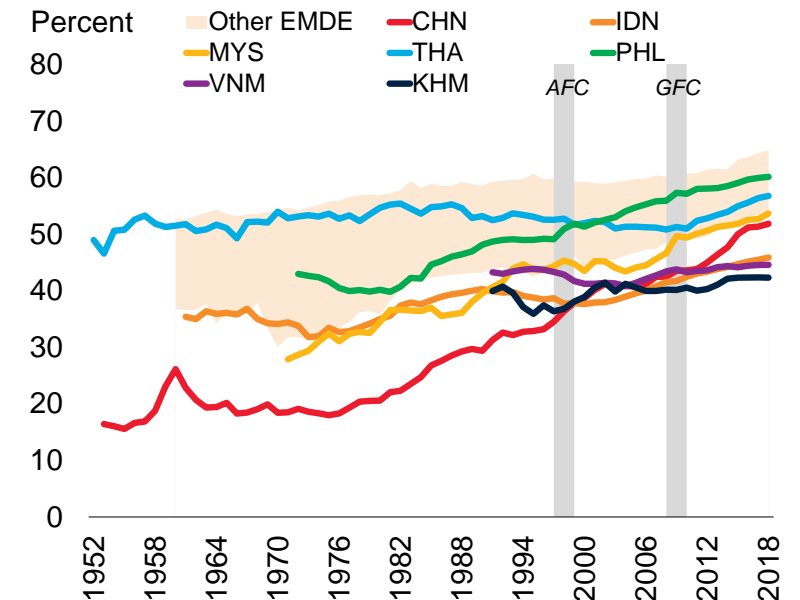
## Agriculture



## Manufacturing



## Services

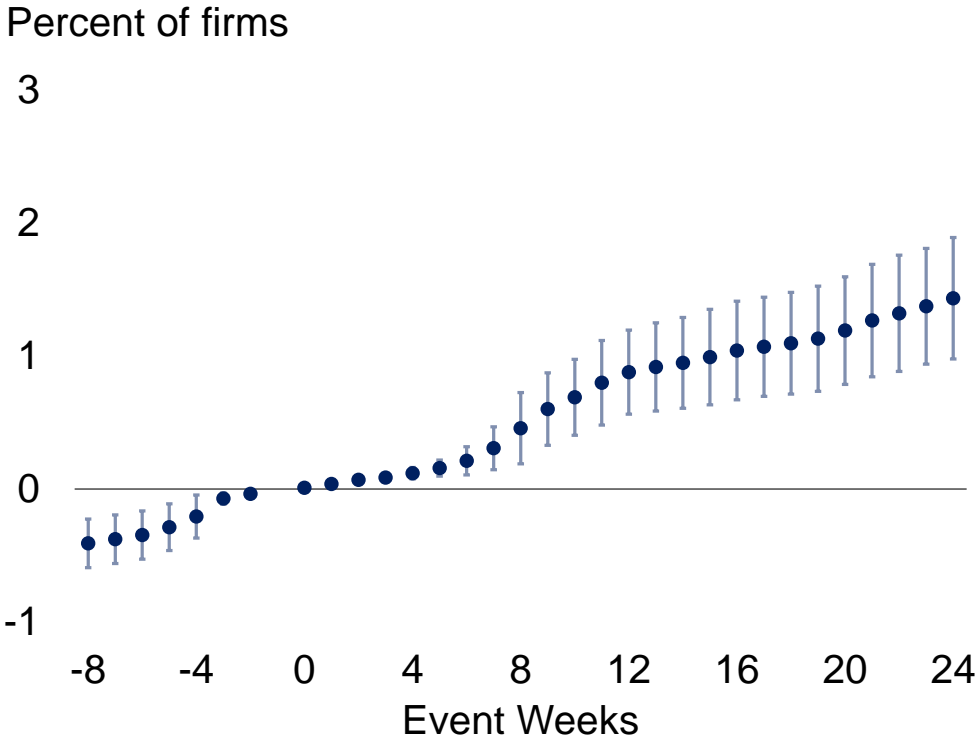


Source: GGDC/UNU-WIDER Economic Transformation Database

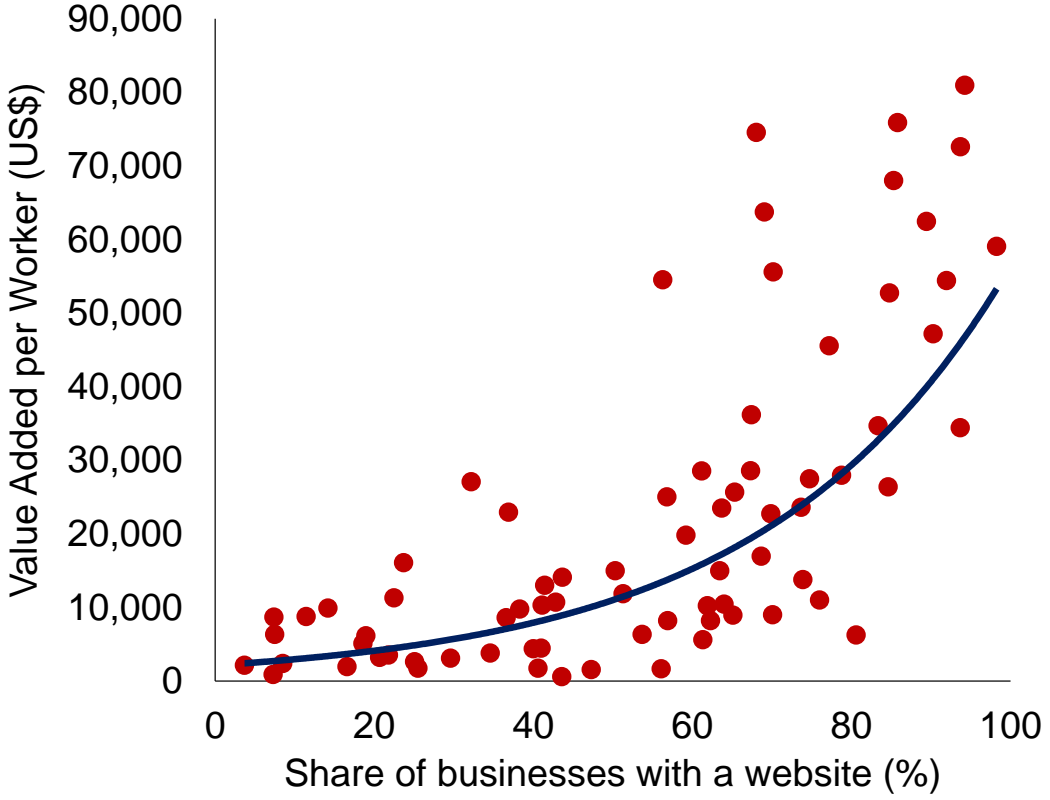
Note: Other EMDE shows 25 -75 percentile of 20 major EMDEs outside EAP

# New digital technologies could boost productivity growth in services

## Adoption of E-commerce technologies after COVID-19



## Correlation between website use and labor productivity of retail firms



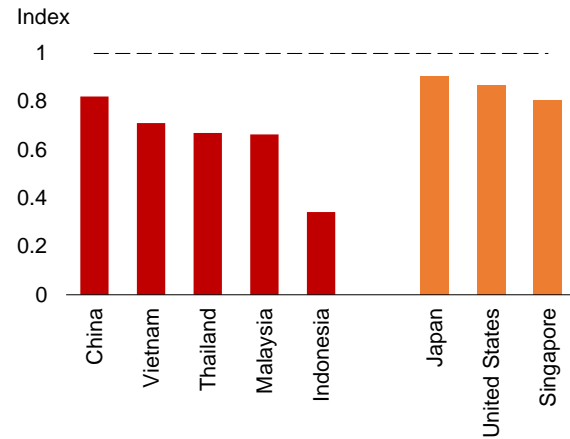
Source: ILOSTAT, UN National Accounts, World Bank Enterprise Surveys, Nayar et al. (2021).  
Note: Website data for 2016 or most recent available year.



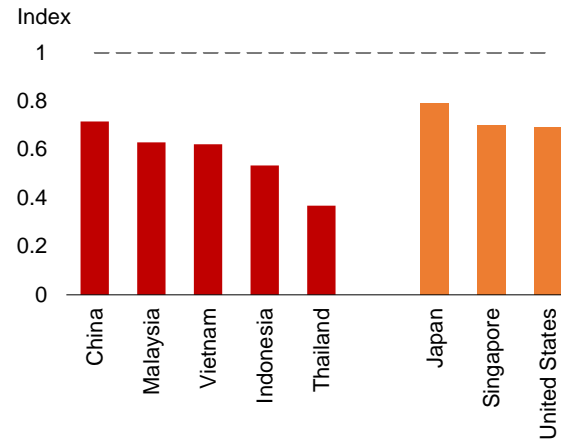
# But countries will need to address the reform gap in the services sectors

## Services Trade Restrictiveness Index (2021; 1=most liberalized)

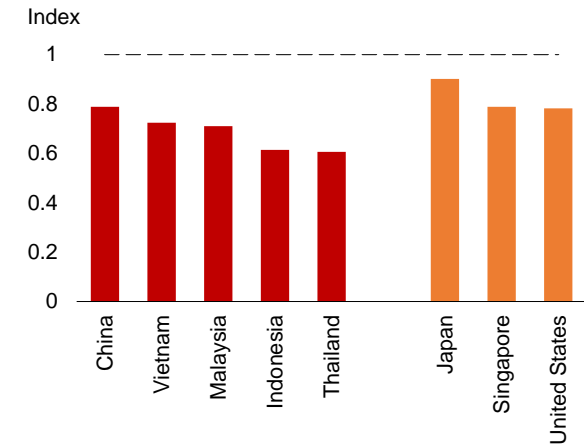
### Distribution Services (Wholesale and retail trade)



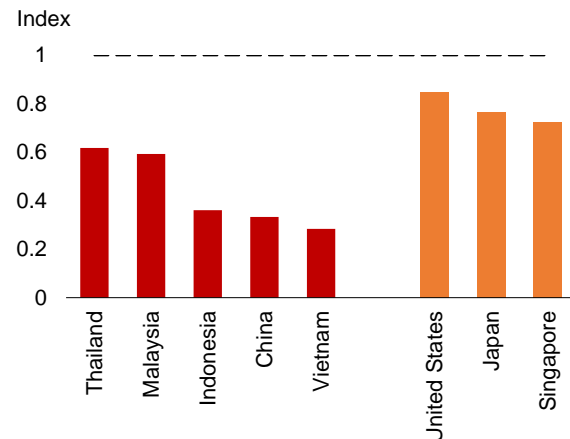
### Transportation



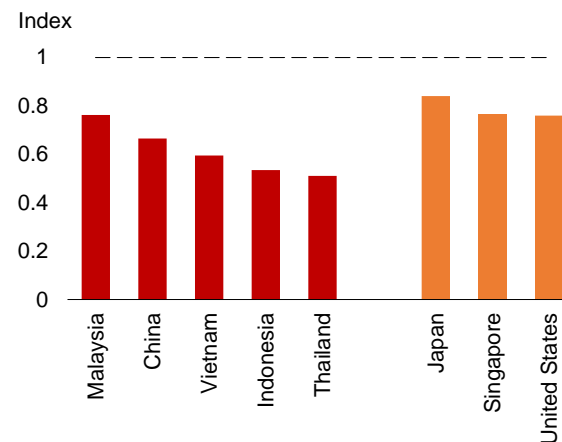
### Construction



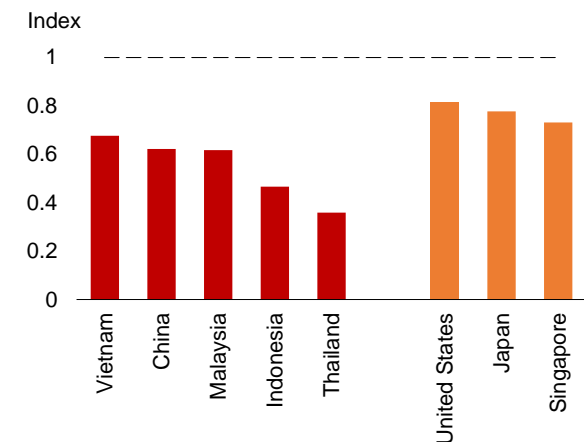
### Telecom



### Financial Services



### Professional Services



# Looming challenges

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Decoupling?; Aging; Adaptation

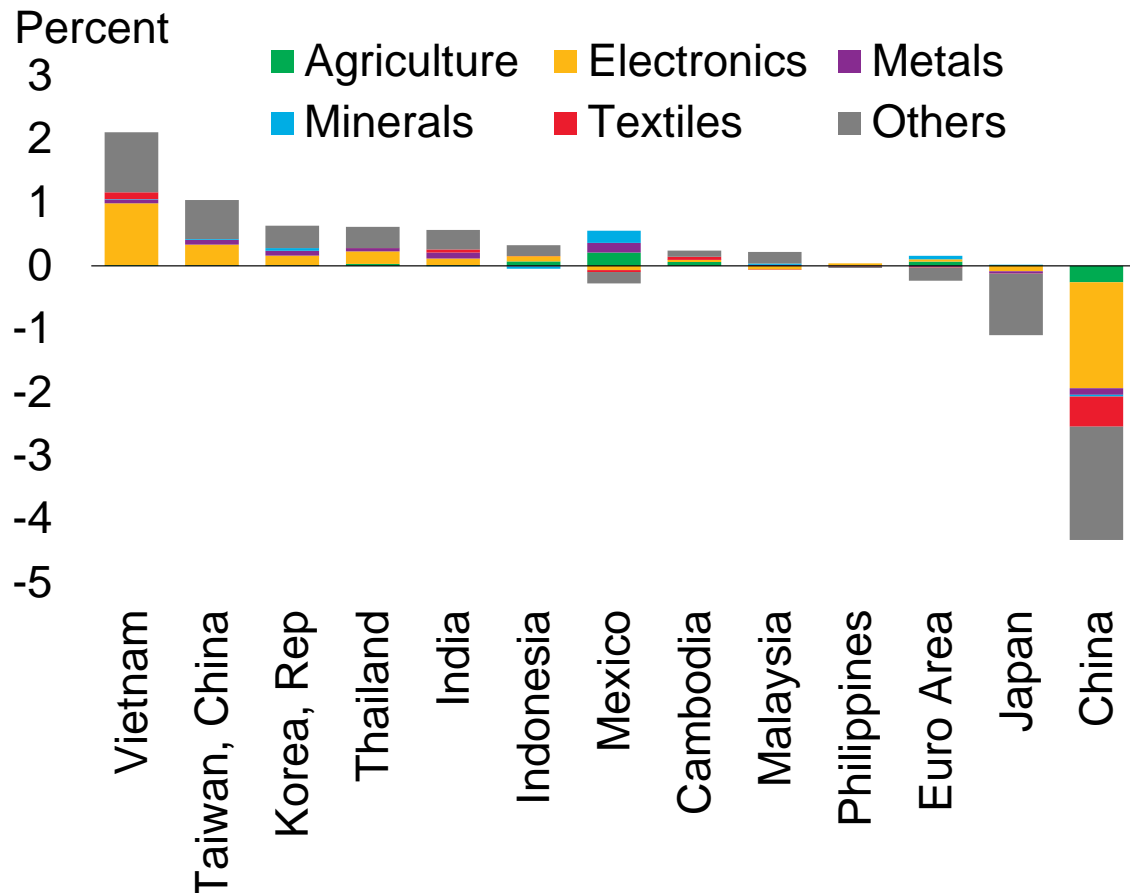
# Decoupling?

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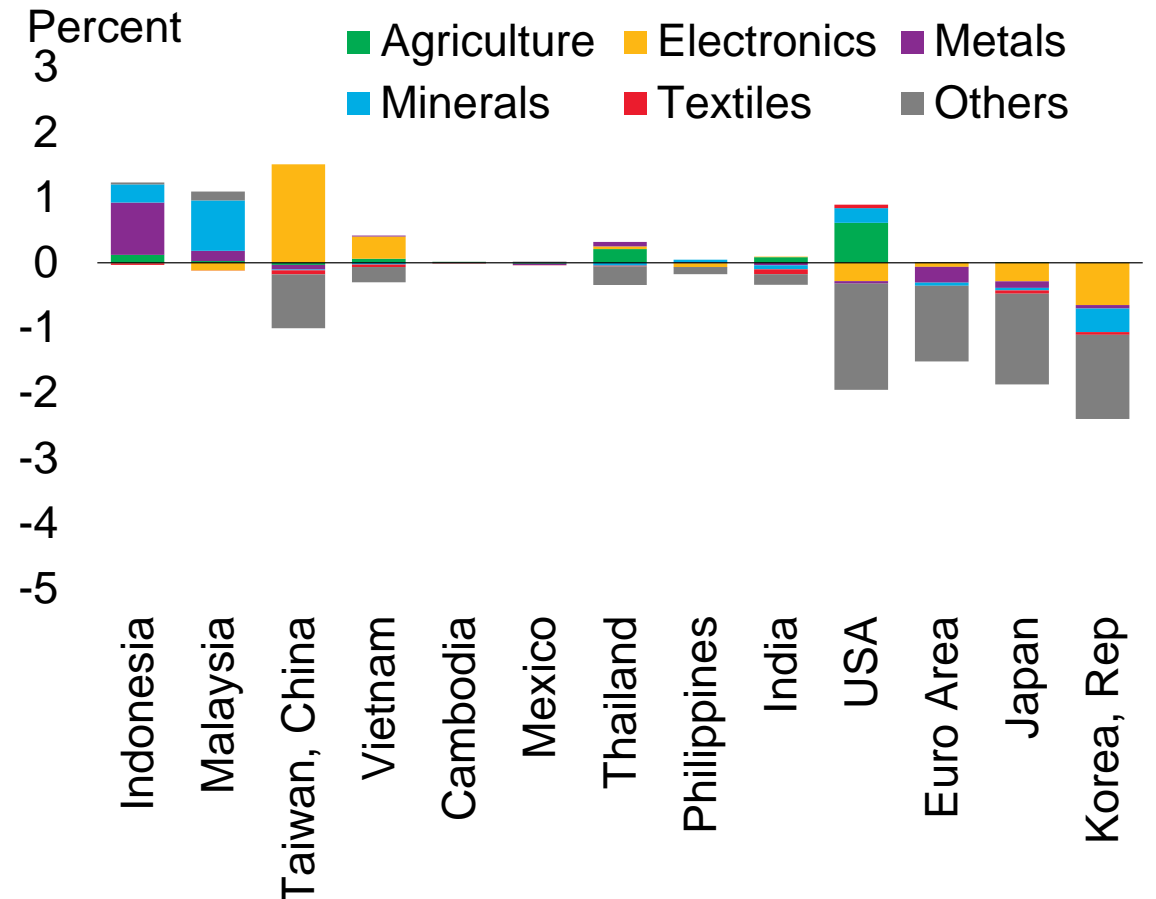
# Some developing EAP economies have reaped the export benefits of US-China trade tensions

Sectoral decomposition of changes in the share of US and China's imports during 2018-2022

Changes in share of US imports, 2018-2022



Changes in share of China's imports, 2018-2022



Source: Customs data

***Uncertain politics* rather than reliable economics are now molding trade patterns**

- **Friend-shoring may lead to a less predictable environment for third-countries than rules-based trade**

***Divergent standards* for goods and services; e.g., different approaches to data governance in China and the US, could segment markets...**

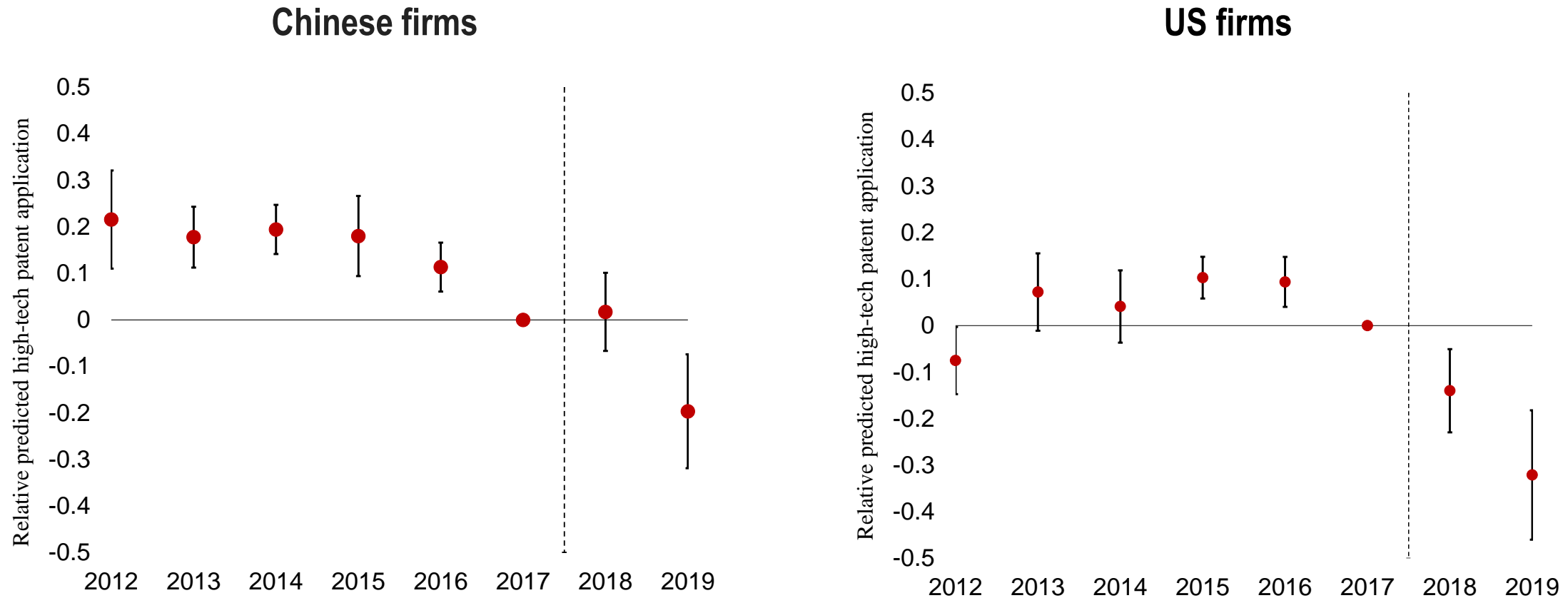
- **Segmentation of large markets prevents third country exporters from reaping economies of scale**

***Export restrictions* on ultimate destination as well as import restrictions on ultimate source, can disrupt GVCs and third country trade**

- **EAP countries differ in how they participate in GVCs, but most are significantly integrated with the world and with China, especially in electronic products**

## Policy-induced innovation decoupling?

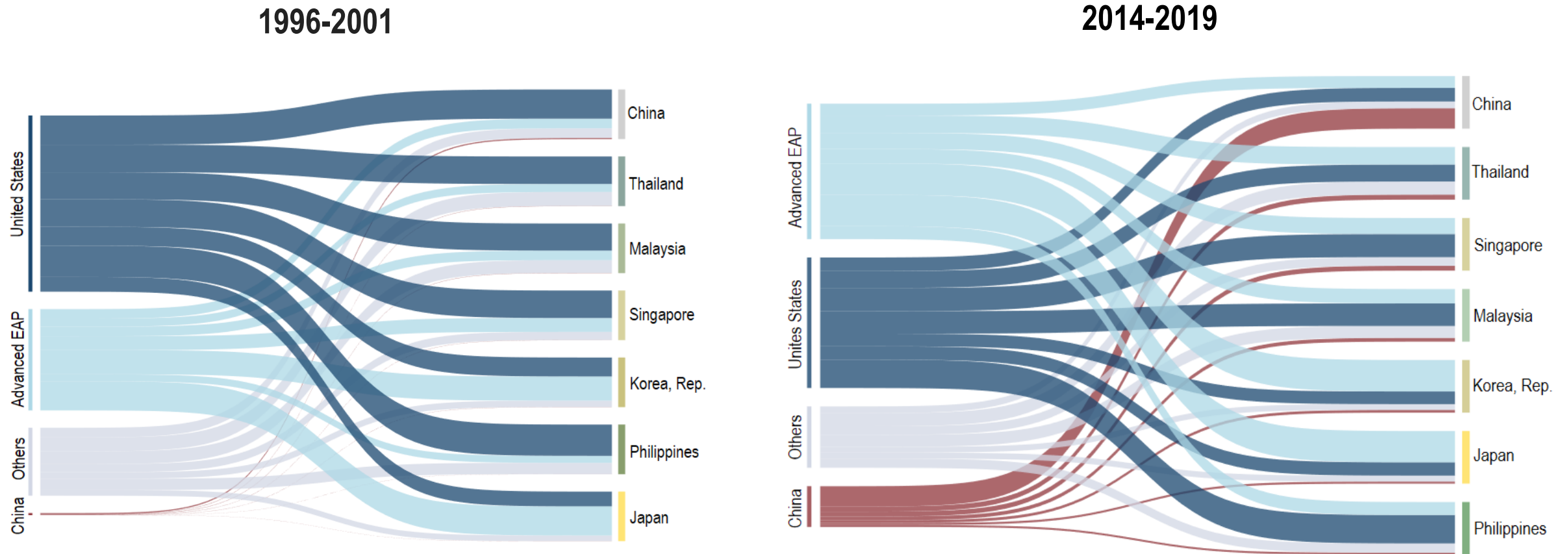
Measures taken after 2018 adversely affected innovation of Chinese firms which had prior collaborations with the US, and of US firms which had prior collaborations with China



Notes: Event study plots of the patent applications of US (Chinese) firms with collaborations before 2018 with inventors in China (US).

**Bilateral restrictions on technology flows and collaboration between large countries could reduce the global availability of knowledge**

# The US and, increasingly, China are important sources of knowledge for other East Asia and Pacific countries

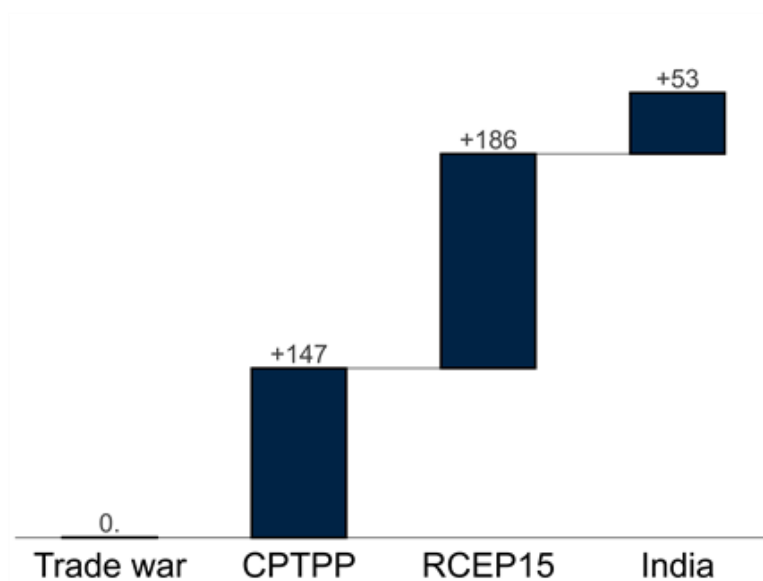


Notes: The chart shows the source of backward citations (on the left-hand scale) for patent applications to EPO/USPTO/WIPO patent offices by assignees in EAP countries (on the right-hand scale)

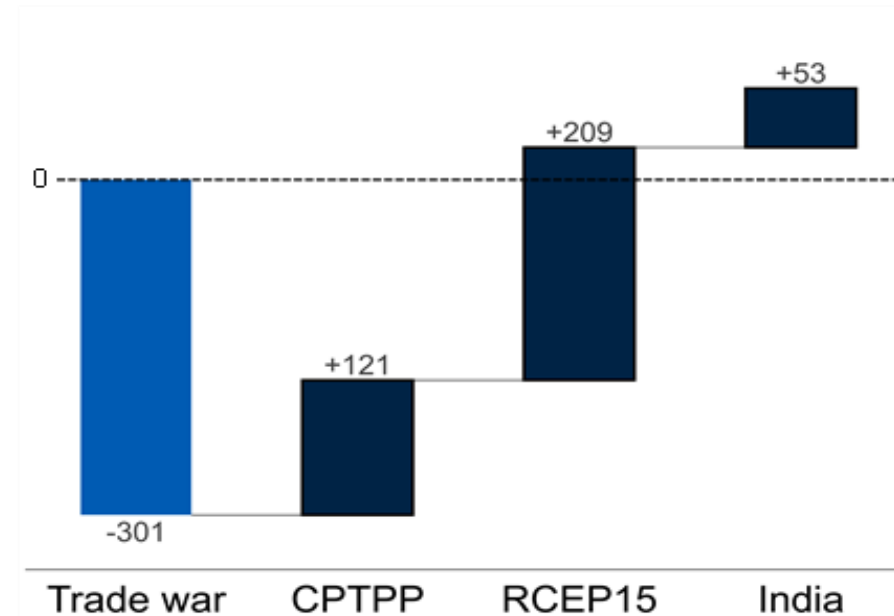
# The adverse effects of a trade and technological rift between large countries can be reduced by third countries forming (separate) trade agreements that ideally include each large country

## Global Income effects of Asia-Pacific trade policies in 2030

Business as before



Under sustained trade war



## Third countries benefit from being “hubs” rather than “spokes” or members of exclusive trade blocs

Source: Drawing on Petri and Plummer (2020)

Note: “Business as before” assumes a return to a pre-trade war path. “Sustained trade war” assumes path defined by post-phase one tariffs. Bars show incremental effects of adding each policy to all previous policies. The policy denoted “India” involves adding India to the RCEP15 agreement to form RCEP16

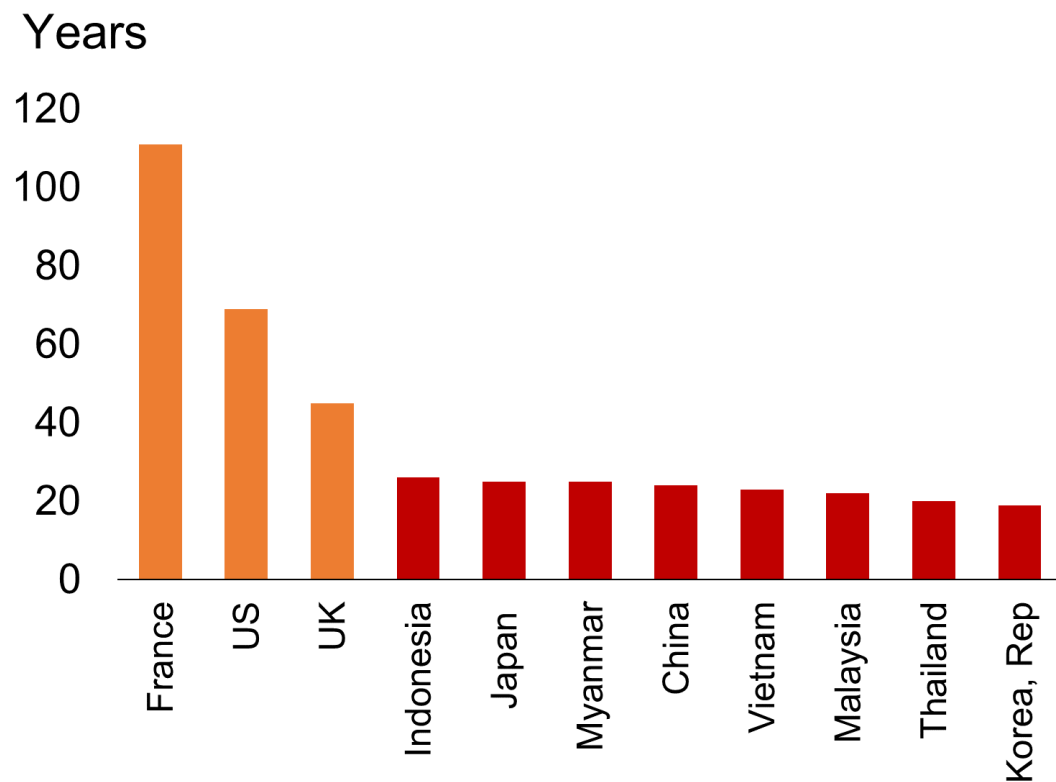


# Aging

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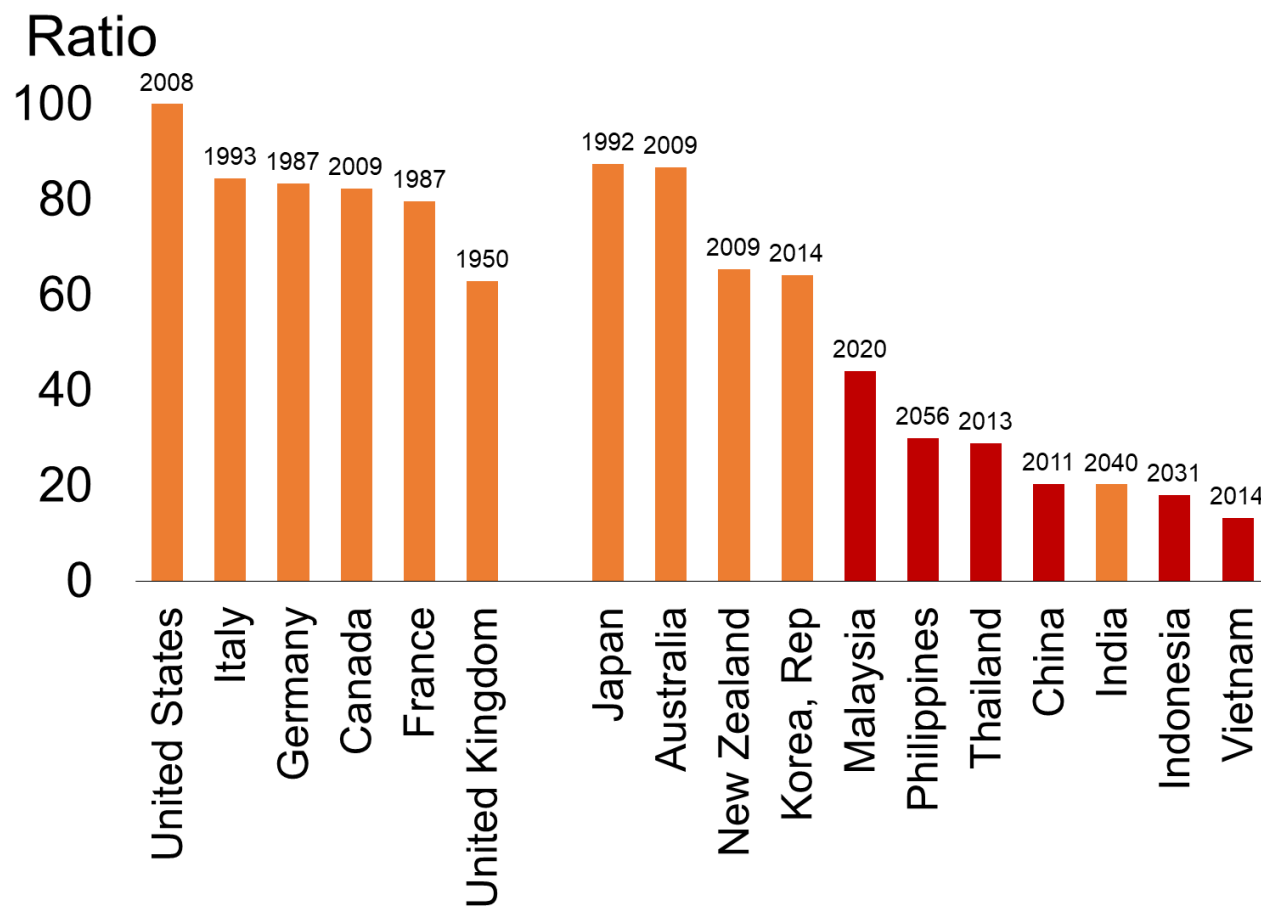
# EAP countries are aging faster than rich countries did, and the working age population will peak at lower levels of income per capita

Transition from aging to aged societies (i.e., from population 65+ reaching 7% to 14% of total)



UN Population projections, 2022, medium fertility variant

GDP per capita at peak working age population relative to US



# Aging will impact economic activity, fiscal balances and health services

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Lower share of the conventional “working age” population, unless older people (especially women) continue to work

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Higher burden of pensions, unless the gap is narrowed between actual and actuarially fair contribution rates

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Higher burden of age-related non-communicable diseases, unless efforts are made to prevent, control and manage these diseases across the life-cycle

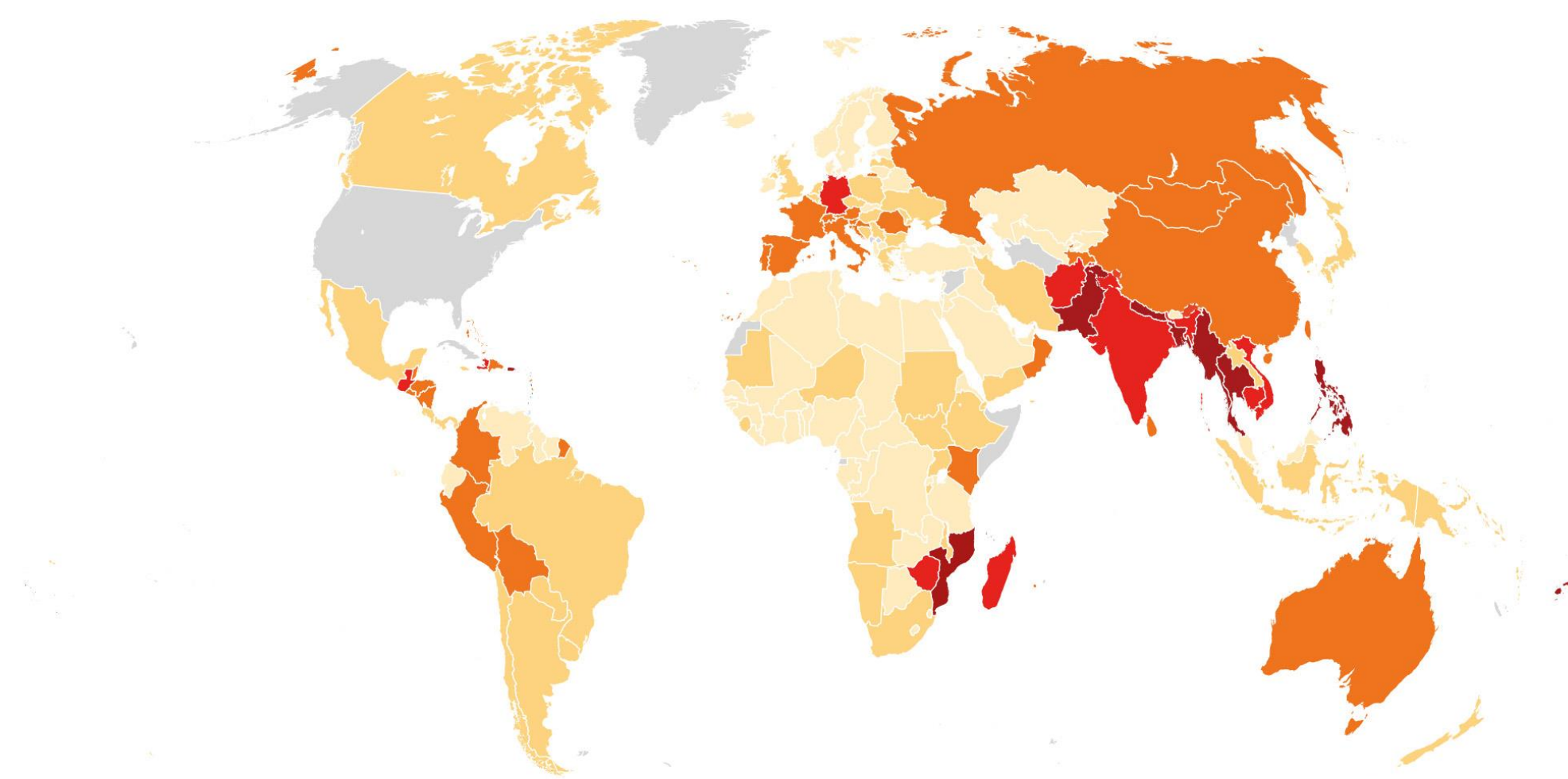
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# Adaptation

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# EAP countries are highly exposed to climate change impacts

Global Climate Risk Index: Ranking 2000 – 2019



# Investing in adaptation will deliver a triple dividend

## Investing in Adaptation Yields:

Avoided Losses

Induced Economic Benefits

Social and Environmental Benefits

= Triple Dividend

- ✓ Early warning systems save lives and assets and are worth at least 10 times their cost.
- ✓ Climate-resilient new infrastructure typically adds 3% to upfront costs but has benefit-cost ratios of 4:1.

- ✓ Reduced flood risks lower financial costs, increase security, and help induce high-value investment in cities.
- ✓ The Thames barrier induced development of Canary Wharf and East London
- ✓ Drip irrigation increases yields as well as reduces drought risk.

- ✓ Nature-based flood protection also increases biodiversity, makes air and water cleaner, offers recreation, and improves health.
- ✓ Mangrove protection and restoration abate coastal surges, support local fisheries and forestry, and store carbon. Combined benefits are up to 10 times greater than the costs.

# Policy priorities

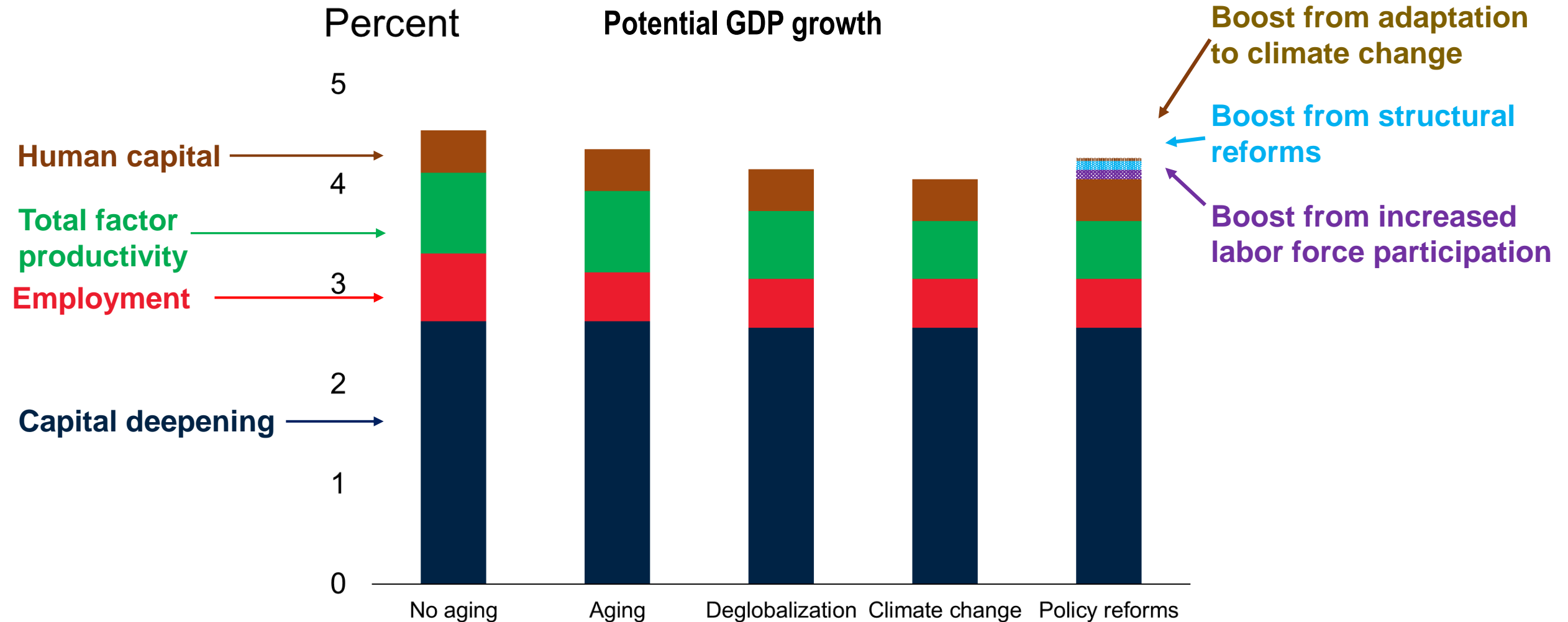
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# Four types of policy action are needed





# Aging, deglobalization and climate change can reduce potential growth, but reforms can offset the impact





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