

# Is developing Asia's growth decelerating?

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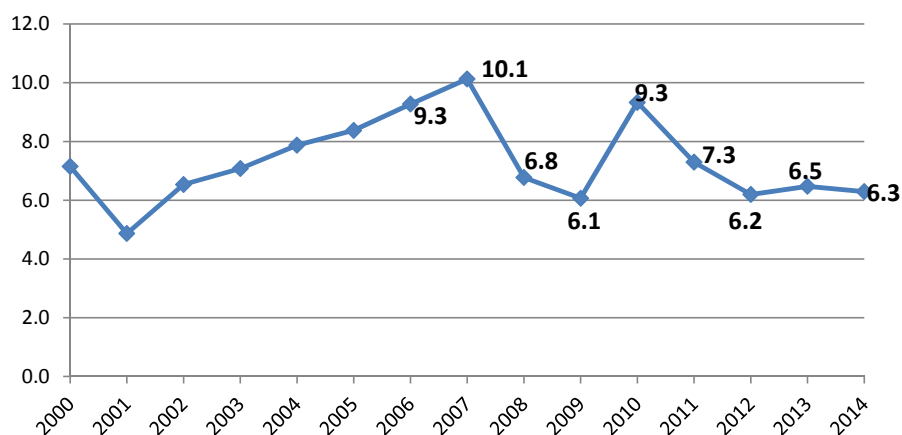
Asian Development Bank

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# Developing Asia's actual growth rate is down

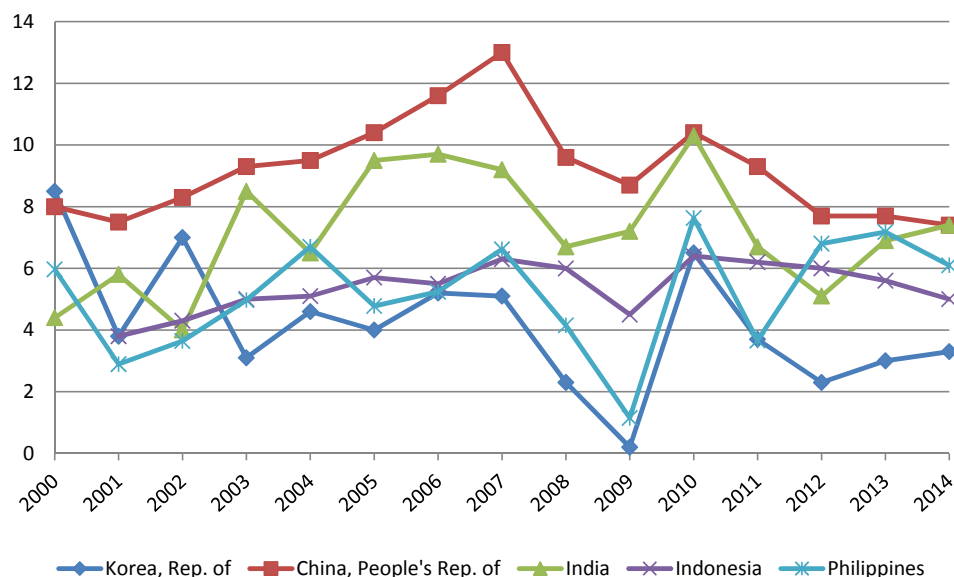
## But nothing compared with the AFC: 1.6% in 1998

Developing Asia's average  
growth rate of GDP  
(% per year)



Latest ADO estimates: 6.1% growth rate in 2015  
and 6.2% in 2016

Growth rate of GDP (% per year)

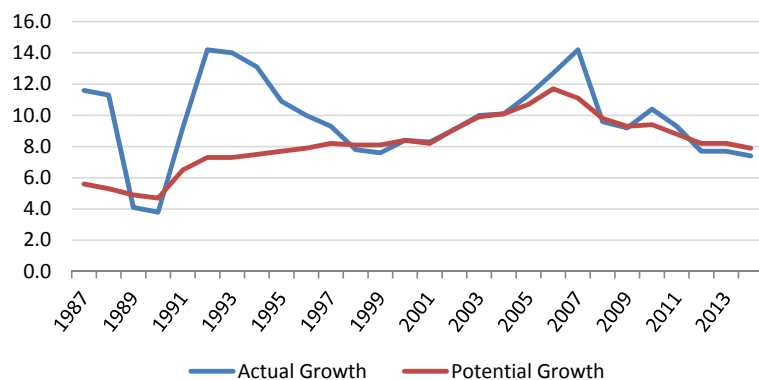


## **But what is happening to productive capacity?**

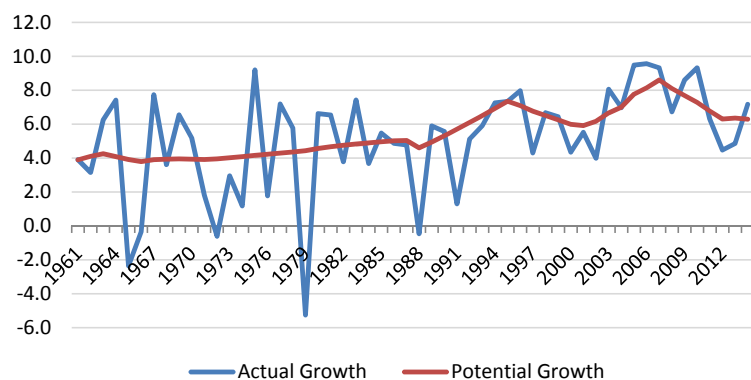
- Is potential growth rate declining?
- If yes, is it cyclical or structural?
- Are we entering a new normal in Asia?
- Appropriate policy responses depend on the nature of the decline

# Potential and Actual output growth rates

PRC

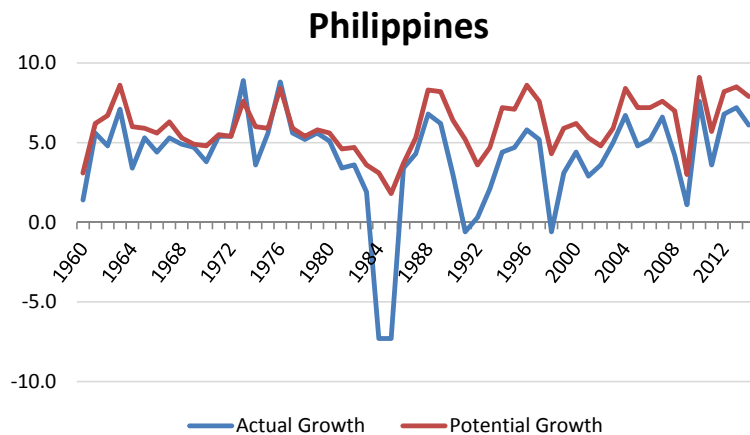


India



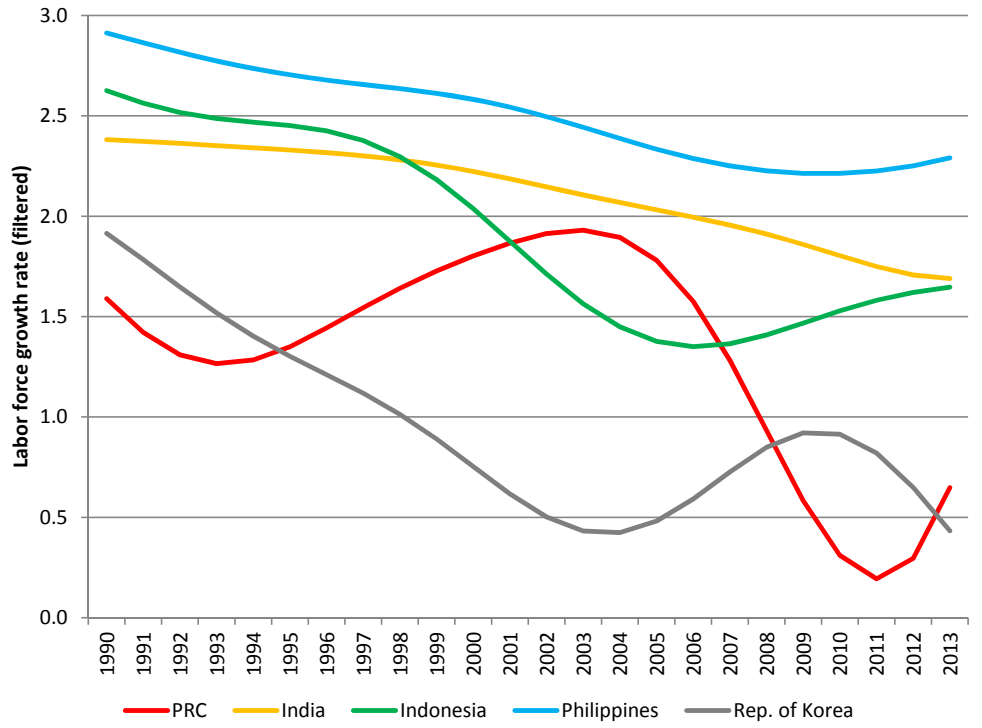
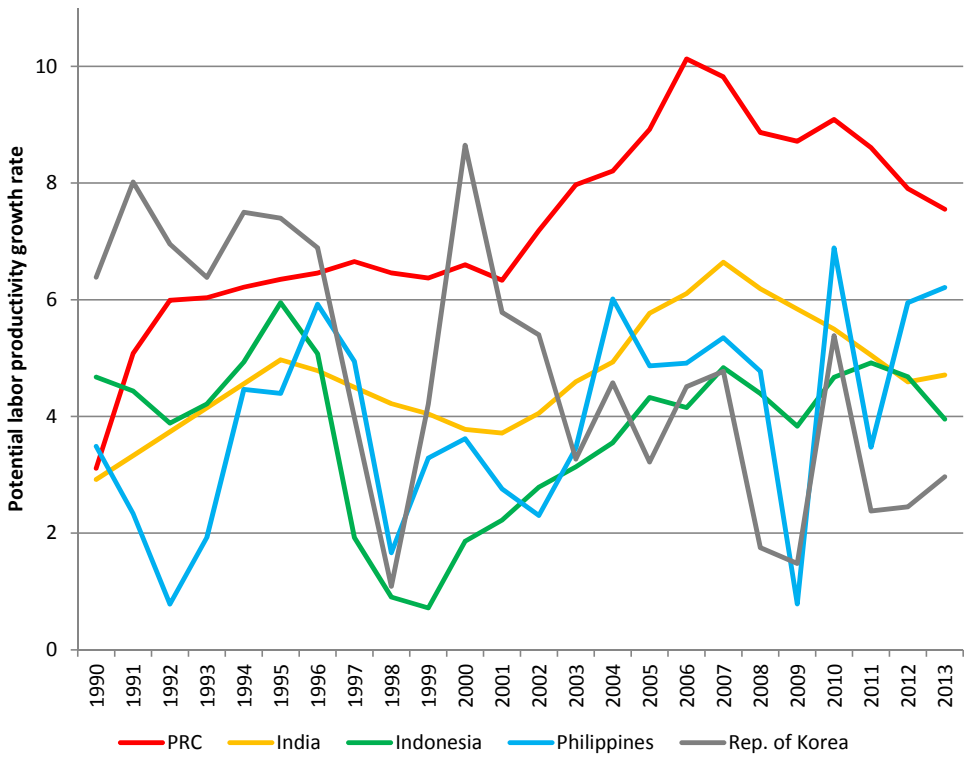
	PRC	India
Average before crisis, 2000-07 (%) Actual/Potential	10.51 / 9.90	7.17 / 7.03
Output Gap (Actual-Potential)	<b>0.61</b>	<b>0.14</b>
Average during crisis, 2008-14 (%) Actual/Potential	8.75 / 8.80	6.78 / 6.95
Output Gap (Actual-Potential)	<b>-0.05</b>	<b>-0.17</b>
Percentage point change in Actual and Potential growth rates, During-Before	-1.76 / -1.10	-0.39 / -0.08
Potential before crisis	Increasing	Increasing
Potential during/post crisis	Declining (7.9% in 2014)	Declining (6.3% in 2014)

# Potential and Actual output growth rates



	Rep. of Korea	Indonesia	Philippines
Average before crisis, 2000-07 (%) Actual/Potential	5.40 / 5.59	5.04 / 4.95	4.90 / 6.57
Output Gap (Actual-Potential)	<b>-0.19</b>	<b>0.09</b>	<b>-0.67</b>
Average during crisis, 2008-14 (%) Actual/Potential	3.18 / 3.47	5.75 / 5.81	5.23 / 7.05
Output Gap (Actual-Potential)	<b>-0.29</b>	<b>-0.06</b>	<b>-1.82</b>
Percentage point change in Actual and Potential growth rates, During-Before	-2.22 / -2.12	<b>+0.71 / +0.86</b>	<b>+0.33 / +0.48</b>
Potential before crisis	Declining	Increasing	Increasing
Potential during/post crisis	Stable (3.3% in 2014)	Stable (5.0% in 2014)	Increasing (7.9% in 2014)

# Potential Labor productivity and Labor force growth rates

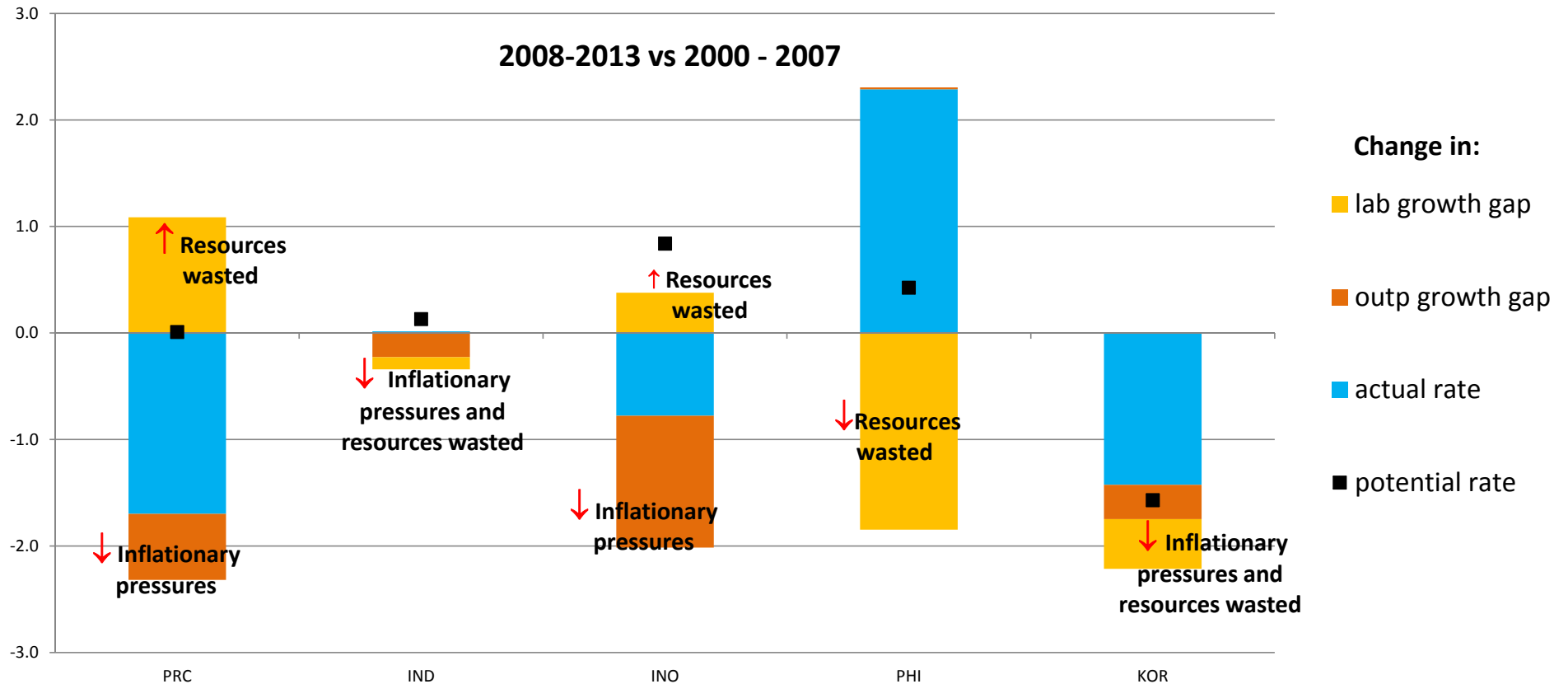


# A decomposition of potential growth rate of labor productivity ( $\hat{y}^*$ )

$$\Delta \hat{y}^* = \Delta \text{Actual productivity growth} - \Delta \text{Output growth gap} + \Delta \text{Employment growth gap}$$

We compare change between crisis and pre-crisis periods

2008-2013 vs 2000 - 2007



# Actual and Potential growth - Policy

		Potential Output Growth	
		Low: <4% in 2008-14 and declining	Medium-High: >4% in 2008-14 (declining in most cases)
Actual Output Growth	Low	<p><b>Boost both rates in tandem</b></p> <p><u>Actual:</u> Stimulus package  <u>Potential:</u> (i) Increase firm-level productivity (service sector); (ii) implement policies to increase labor force growth (e.g., immigration)</p> <p><b>Japan; Korea Rep. of.; Taipei,China; Hong Kong, China; Thailand</b></p>	<p><b>Cyclical downturn (negative temporary shock) – Dislocations in the labor market (unemployment)</b></p> <p><u>Actual:</u> (i) Stimulus package; (ii) Diversify the economy  <u>Potential:</u> (i) Do not create excess capacity; (ii) Facilitate the reallocation of labor (especially out of agriculture) into sectors of higher productivity as actual growth increases; (iii) Tackle low organizational capabilities; (iv) Training</p> <p><b>Pakistan; Malaysia; Kazakhstan</b></p>
	Medium - High	<p><b>Watch out if government pushes demand-side levers (inflation)</b></p> <p><u>Potential:</u> (i) Increase firm-level productivity (move into highly complex activities); (ii) Implement policies to increase labor force growth (e.g., fertility)</p>	<p><b>Do not do harm...monitor both rates to keep them high and at about the same rate</b></p> <p><u>Nevertheless:</u>            (i) Do not create excess capacity; (ii) Increase firm-level productivity, reduce factor misallocation and tackle low organizational capabilities; (iii) Facilitate the reallocation of labor (especially out of agriculture) into sectors of higher productivity; (iv) Training</p> <p><b>PRC; India; Indonesia; Philippines; Vietnam; Cambodia; Bangladesh; Singapore; Sri Lanka; Azerbaijan; Uzbekistan; Turkmenistan; Tajikistan</b></p>



# Developing Asia's potential growth is decelerating

- Significant decline in potential growth rate across all the region's major economies and across most of the smaller economies with respect to before the crisis (declined in 16 out of 21 estimated)
- Potential growth did not decline during 2008-14 in: Indonesia, Philippines, Bangladesh, Pakistan, Uzbekistan
- PRC's potential growth, potential labor productivity and labor force growth slowed down during 2008-14
- India's "dream run" for a few years was more a mirage (debt-led, cyclical boom, coinciding with favorable international scenario) than a build up of capacity. Potential growth below the PRC's

# A new normal in Asia? Is the glass half full or half empty?

- Given that the PRC represents about 50% of ADB's developing Asia, India 11% and Rep. of Korea 9%, and that potential has declined in another 13 economies, obviously the region's potential has declined
- But:
  - The region's potential growth is still high
  - A new normal (i.e., lower potential) in developing Asia? Difficult to distinguish cyclical fluctuations from changes in trend growth: fast structural transformation...toward services
  - ✓ PRC: much of the recent slow down is probably structural rather than cyclical
  - ✓ India: cyclical boom pre-crisis followed by possibly also another cyclical slowdown + Plenty of room in terms of demographics and labor productivity growth
  - ✓ Asia's advanced economies: Clearly down both labor productivity and labor force growth
  - ✓ Other DMCs: not clear that their declines are structural

**THANK YOU**