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Asia-Pacific Region: Gearing Up for the Next Transformation

By Christine Lagarde, IMF Managing Director
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Introduction: Asia Today and Tomorrow

First Vice Minister, Governor, Ladies and Gentlemen—*Anyoung haseyo*.

I would like to thank the Ministry of Strategy and Finance, the Bank of Korea, and the Peterson Institute for co-organizing this important conference. Our discussions will focus on how to **promote sustained and inclusive growth** in the world's most dynamic region.

When we think about Asia's economic future, we know that this future is being built on strong foundations—on the richness and diversity of its cultures, on the incredible energy and ingenuity of the people who have changed the world by transforming their own economies.

China and India have been driving the greatest poverty reduction in human history by creating the world's largest middle classes. In a single generation, Vietnam has moved from being one of the world's poorest nations to being a middle-income country.

And Korea has transformed itself into a thriving advanced economy—inspiring those who are working hard to avoid the so-called "middle income trap". These are only some of the many Asian success stories that have captured the imagination of policymakers and economists around the world.

Why? Because this region is not just about sound macroeconomic policies and embracing global economic integration. It is also about resourcefulness and immense determination.

Twenty years ago, so many communities and companies were deeply hurt by the Asian financial crisis. So many countries in this region suffered a lot. But they also learned a lot—as did the IMF—and they are much stronger today. As the famous Korean proverb puts it: "*After rain, the ground becomes firmer*."

This resilience was earned through bold, post-crisis reforms. Many countries adopted more flexible exchange rates and reduced external vulnerabilities. They also strengthened their financial sector regulation and supervision, and developed domestic capital markets.

With these reforms, Asia was able to weather the global financial crisis, and has since emerged as a key engine of global growth. Over the past decade, the Asia-Pacific region has contributed two thirds of global growth, and now accounts for about 44 percent of global GDP[1].

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[1] GDP measured at purchasing power parity. Emerging and developing Asia has contributed 56 percent to global growth from 2007-2016.

Today we see the beginning of another economic transformation across Asia. What does that mean? It means that countries can build on the progress made so far, while addressing *new vulnerabilities*.

These include immediate challenges such as high corporate debt and the risk of protectionism—but also *longer-term* challenges such as population ageing and lower productivity growth.

There is a huge opportunity for policymakers to take the best of today's Asia to build the best possible tomorrow for Asia. How? Through bold policy actions and strong international cooperation.

Here the Korean government has provided leadership—and not just by hosting international economic conferences. Next year, for example, Korea will host the **Winter Olympics in PyeongChang**, bringing together the world's top athletes.

I believe that policymakers can take inspiration from these athletes—because that is what the next transformation requires: a ***relentless focus on training***, on the nitty-gritty of economic reform.

Let me briefly discuss this from three perspectives:

- First, how can Asia seize its demographic opportunities?
- Second, what can governments do to boost productivity?
- And third, how can the IMF best serve its member countries in managing the next transformation?

1. Seizing the Demographic Opportunities

Let us start with demographics. Reforms in this area can lift potential growth and help societies share the benefits of growth more widely. Consider the immense potential of *young* and *growing* populations in countries such as India, Indonesia, and the Philippines.

By lifting productivity and creating more, higher-quality jobs for a *growing* workforce, these economies can reap this demographic dividend. IMF analysis[2] shows that a growing workforce can add one full percentage point to their annual GDP growth over the next three decades.

There are also *rapidly ageing* populations in countries such as China, Japan, Korea, and Thailand. They will have *smaller* workforces in the future and potentially lower productivity growth.

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[2] IMF Regional Economic Outlook: Asia and Pacific, Chapter 2: "Asia: At Risk of Growing Old before Becoming Rich?" (May 2017).

We estimate that these countries could face lower annual GDP growth, again by up to a percentage point—although some of the negative effects of ageing remain subject to debate.[3]

So what can Asia do to step up its demographic "training"?

One avenue that has worked in *all* countries around the world is to boost the proportion of women in the workforce. Korea and Japan, for example, could further increase their focus on reforming secondary earner taxation and boosting childcare benefits and tax incentives for part-time work.

Emerging and developing countries, such as Cambodia and India, can benefit from expanding girls' access to high-quality education and promoting women's access to finance.

Taken together, these initiatives could become an economic game changer. By some estimates, closing the gender gap in the labor market could boost GDP by 9 percent in Japan, 10 percent in Korea, and 27 percent in India.[4]

We have also seen benefits from fostering *more inclusive* growth—especially in countries where income and wealth inequality are high and rising. To put it simply, when the benefits of growth are shared more broadly, growth is stronger, more durable, and more resilient.

Here in Korea, the Parliament recently approved a budget that includes transfers to the elderly, subsidies for job-seeking youth, and higher unemployment benefits. A stronger social safety net—including a more reliable pension system—is also crucial for China, because it facilitates the transition to consumption-led growth.

In other words, increasing the economic "fitness level" can help ensure that the next generation will be better off.

2. Boosting Productivity

So much for demographics. What about productivity?

Over the *long term*, **productivity growth** is the most important source of higher income and rising living standards. For example, countries such as Bangladesh, India and Indonesia are benefiting from steady investment, which can help boost innovation and potential growth.

The not-so-good news is the sharp slowdown in productivity growth since the global financial crisis in countries such as China, Japan, Korea, and Thailand. This is part of a global trend, affecting advanced economies and many emerging market countries.

[3] Acemoglu and Restrepo (2017), for instance, highlight an offsetting mechanism, namely the greater incentives for fast-aging societies to introduce labor-saving innovations, which raises productivity, all else equal.

[4] Korea data: Korean government estimate. Japan and India data: Aguirre, Hoteit, Rupp, and Sabbagh (2012), "Empowering the Third Billion. Women and the World of Work in 2012".

We estimate that, if productivity growth had followed its pre-2008 crisis trend, overall GDP in the Asia-Pacific region would be about 9 percent higher today[5]. That would be the equivalent of adding to the global economy a country with an output of Japan.

So how can governments step up their productivity "training"? **Fostering innovation is one way**. This includes providing tax incentives for research and development, and investing more in infrastructure and education reform.

For example, Korea and Vietnam are world champions in educational achievement. Here a greater emphasis on vocational training could help reduce skills mismatches in some sectors.

Of course, **Asia has been a world champion in entrepreneurship**, most recently in smartphone apps, e-commerce, and fintech. In these and other sectors, the region could benefit from reducing overly stringent regulations and fostering new ventures and fresh ideas, rather than protecting incumbents.

More trade can also play a role. Why? Because trade promotes innovation-sharing and pushes firms to invest in new technologies and more efficient business practices.

For example, we estimate that China's integration into the global trading system accounted for as much as 10 percent of the average overall productivity increase in advanced economies between the mid-1990s and mid-2000s.[6]

Gains like that illustrate **the transformative power of trade**. Today, billions of people across the globe enjoy higher incomes and living standards, because we are—collectively—world champions in trade and technological progress.

But we also know that these structural changes come with negative side-effects, from job losses in shrinking sectors to social challenges in some communities.

Each country has a responsibility in this area—it is a *global* responsibility as well. What do I mean by that? I mean pushing for better and smarter trade agreements, including better protecting labor and environmental standards. Here international cooperation has a key role.

As the famous Korean proverb puts it: "*Even a sheet of paper is held more easily by two people*".

3. The IMF as a Partner

That brings me to my third and final topic—the **IMF as a partner, as a "fitness coach"**.

In many ways, the IMF has been going through its own transformation, and continues to adapt to better serve our member countries here in Asia and around the world.

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[5] IMF estimate.

[6] IMF Working Paper: Ahn and Duval (2017), "Trading with China: Productivity Gains, Job Losses".

Our raison d'être is to work *with* our members to foster resilient and inclusive growth. This means engaging deeply through analysis, policy advice, and hands-on assistance and training on how to strengthen institutions and improve economic management.

For example: when Myanmar began opening its economy, the IMF helped modernize its tax administration and revamp its central bank and foreign exchange market. We also supported Myanmar in building a statistics program and strengthening its anti-money laundering regime.

More broadly, we work with our members every day to address the challenges posed by demographic pressures, climate change, and new technology—but that is not the whole story.

We are constantly learning from our members and sharing that knowledge—so *all* members can enhance their own performance.

Think of what has been achieved since 2010, when Korea chaired the G20. Our discussions have contributed to the IMF's reassessment of the role of capital flow management measures.

We have also been working with our members to strengthen the global financial safety net—by enhancing our toolkit and by deepening our cooperation with regional financing arrangements, including the Chiang Mai Initiative.

And there is now a greater representation of dynamic emerging economies in the governance of the IMF. With the most recent quota reforms, the BRIC countries are now among our top 10 shareholders.

This is a *new* Fund in a *new* world, serving our membership in new and better ways.

Conclusion

Let me conclude on a personal note: **I have learned so much from Asia**—from the young entrepreneurs in Vietnam to the students in Cambodia, China, Korea, and India. They embody Asia's tremendous potential.

I see a generation that will have a unique opportunity to lead Asia's next transformation. By working and learning together—by stepping up our "training"—we can help improve the lives of people in this region and across the globe.

Thank you—*kamsa hamnida!*