

Economic and Social Survey of Asia and the Pacific 2009

Addressing Triple Threats to Development

CLIMATE



FINANCE

FUEL

FOOD

RICE



UNITED NATIONS
ESCAP

Economic and Social Commission for Asia and the Pacific

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ECONOMIC AND SOCIAL SURVEY OF ASIA AND THE PACIFIC 2009

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FOREWORD



We are living through a period of tremendous turmoil and uncertainty. The current global economic downturn is not the only crisis. Volatility in food and fuel prices has raised levels of poverty, hunger and malnutrition in many countries. The overarching menace of climate change, meanwhile, threatens to undermine all our work for development.

These crises are interrelated. All have profound social and political implications. Each needs solutions that take the others into account. The *Economic and Social Survey of Asia and the Pacific 2009* analyses how these multiple threats have affected the region, and considers ways in which the region can address them. The *Survey's* central thrust is that the convergence of the crises and the fundamental changes they have brought to the macroeconomic landscape present a unique opportunity for the region to make growth more fair and inclusive. Furthermore, by implementing reforms in unison, the region can make a major contribution to reshaping the global economic architecture.

We face unprecedented threats to development. Our immediate task is to help the poor and vulnerable get through these hard times, the devastating effects of which are still unfolding. Over the long term, we must find a more equitable and sustainable path for all the world's people. The recommendations in this publication are meant to inspire policy-makers to be bold and collaborative. In that spirit, I commend this *Survey* to a wide global audience.

A handwritten signature in black ink that reads "Ban Ki-moon". The signature is fluid and cursive, with a long vertical line extending downwards from the end of the name.

BAN Ki-moon
Secretary-General of the United Nations

March 2009

PREFACE



In 2008, three global crises converged to threaten development in the Asia-Pacific region, bringing to the fore particularly testing challenges for policymakers – a Great Recession in developed countries, food and fuel price volatility and climate change calamities. The *Economic and Social Survey of Asia and the Pacific 2009* analyses these threats and outlines ways in which economies in the region can move forward in unison from crisis resilience to crisis resistance. It concludes that some countries in the region are in a stronger position to help not only themselves but also others to smooth the impact of the crises and strengthen regional solidarity. The converging crises could be turned into an opportunity to jump-start a regional reorientation towards a more inclusive and sustainable development path.

Asia and the Pacific as a crisis-prone region...

During the first part of the year, crude oil prices soared to historical record levels and food commodity prices increased to the highest levels in over 20 years, causing alarm across the developing countries of the Asia-Pacific region because of the disproportionate impact of these increases on the poor. The impact was particularly severe in this region, where the price of main staple food, rice, increased by a staggering 150% in only four months. As the second half of the year unfolded and commodity prices started to retreat from their peaks, financial turbulence that had remained largely confined to the United States subprime market took a dramatic turn for the worse, turning into a full-fledged global financial crisis and setting in motion the most severe economic downturn of the world economy in post-war history. By early September, it was clear that, for the second time in a decade, the region would be hit by a financial crisis and that the crisis would be particularly damaging in view of the region's heavy reliance on exports to industrial countries for growth. A total of 24 million people are in danger of losing their jobs, with women and youth – who make up a large share of the manufacturing workforce – disproportionately affected, and this is aggravated by an increase in the number of undernourished to 583 million in 2007 (from 542 million in 2003-2005). A worsening of the state of poverty and hunger in the region is now impossible to avoid.

In 2008, yet a third global crisis loomed on the horizon – a stealthier but potentially more virulent one than the first two: climate change calamities. Natural disasters, often associated with climate change stresses and lower tolerance to increased heat in lower latitudes of this region, struck with intensity in 2008. The number of deaths in Asia and the Pacific in 2008 reached 232,500 persons, accounting for a staggering 97.5% of such fatalities worldwide. One of the deadliest storms ever to occur in the North Indian Ocean Basin, Cyclone Nargis, made landfall in Myanmar's Ayeyarwady Delta on 2 May 2008 and left a heart-wrenching trail of death and destruction – 84,500 people dead and 53,000 missing. Australia's "big dry", the worst drought in more than 100 years, entered its seventh year with fires – believed to be the worst in its history – causing widespread devastation and hundreds of deaths in the south-eastern part of the country. Natural disasters tore apart communities at the opposite ends of the development spectrum, just as the origin of financial crises showed that they no longer fit into easy developed- versus developing-country classifications.

...yet, its developing countries show remarkable resilience to the financial crisis

Developing countries in the region have shown that they are better prepared for a financial crisis. Over the past decade, their regulatory reforms in the financial sector, combined with cautious macroeconomic management policies, have improved current account balances, fiscal deficits and other macroeconomic shortcomings and built a protective shield of foreign exchange reserves. To a large extent, therefore, the region possesses the resilience to withstand the worst of the deleveraging process that caused the global financial system to spiral downwards, leaving no financial institution unaffected.

Export growth in 2008 remained strong until the third quarter, buoyed by weakening currencies and relatively robust external demand. The developing countries of the region managed to maintain an average growth rate of 5.8%, as compared with –0.4% in Asia-Pacific developed economies. The region continued on its long-term development path, which is predicated on an outward-oriented and export-led development paradigm that enabled

it to attain astounding progress and remarkable transformations over the past two decades. In 2009, the region's developing countries are expected to grow at 3.6%, which – compared with growth of –2.0% in the world's major developed countries – further highlights the region's resilience to the crises. This comparatively high growth, coupled with the large aggregate size of the region's economies, could result in the Asia-Pacific region being the locus of any global growth that may take place in 2009.

Of course, not all countries exhibited this resilience. Some countries have been more exposed than others to short-term financial flows, and their currencies have suffered from the retreat of those flows from the region in the last quarter of 2008. Other countries have substantially less fiscal space to implement necessary expansionary fiscal policies. Nevertheless, major developing countries in the region were in a stronger position, which presents them with an opportunity to renew partnerships among themselves and with developed countries to bridge equity divides and contribute to strengthened regional solidarity.

...but major vulnerabilities remain

Resilience notwithstanding, this is no time for complacency. The crisis-prone nature of the region has brought to the fore vulnerabilities that need to be carefully tracked and for which forward planning and policy action will be essential.

Paradoxically, some of the region's vulnerabilities are the very reasons for its success. The fact that the region is more integrated through finance, trade, investment, technology, transport and knowledge with the rest of the world than with itself has allowed it to benefit for decades from export-led growth. But these linkages are also channels through which global instabilities and economic recession are transmitted to the region.

Trade – once the engine of growth in the region – moved from double-digit growth to double-digit declines in some economies during the fourth quarter of 2008, and fresh evidence indicates that the worst is yet to come. As the economic outlook continues to darken at the global level, the tried and true recourse that mitigated the economic crisis in 1998 – boosting exports – has lost its effectiveness. Although intraregional trade has grown dynamically over the last decade, its cushioning effects are stymied by the fact that it consisted largely of trade in parts and components in the manufacturing sector that are, in turn, linked to demand for final consumer products in recession-hit developed countries. Economies with enterprises that are most directly linked through vertically integrated production networks supplying the United States and European Union markets – such as China, the Republic of Korea, Singapore, Thailand, and Hong Kong, China – are those experiencing the strongest downward pressure on economic growth. Another worrisome signal on the trade front is the growing protectionist pressure in recession-hit countries, where domestic sourcing of inputs is given preferential treatment over imports – often as conditionalities imposed on bailout packages – could distort market-entry conditions for exports from Asia-Pacific countries. Furthermore, declining – or at best sluggish – exports will keep exchange rates in the region under pressure, with a marked possibility of further devaluations both among currencies within the region and vis-à-vis the currencies of main trading partners outside the region, in an effort to enhance export competitiveness. If conducted in an uncoordinated manner, devaluation could lead to unnecessary losses in foreign exchange earnings across the region and increased debt burdens.

An area of immediate concern for the region is the significant share of foreign portfolio capital in external financial liabilities in some economies of the region. At a time of generalized international risk aversion in which flights to

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