

Combining macroeconomic stability and micro-based growth: The South East Asia/Asia Pacific Experience

Ahmed M Khalid

**Universiti Brunei Darussalam, Brunei & Bond University,
Australia**

Macroeconomic Stability

- A stable macroeconomics system allows individuals, businesses and the Government to plan more effectively for the future, increases investment and helps to raise productivity.
- Growth-promoting policies play an important role in shaping the vulnerability and resilience of an economy to macroeconomic shocks.
- Financial stability is needed to achieve macroeconomic stability.
- Finally, financial development to financial integration to macroeconomic stability. This is East-Asian Experience.

Achieving Macroeconomic Stability through Financial Stability and Financial Market Integration

Huang and Wajid (2002) suggests a three way approach:

- Comprehensive assessment of financial sector vulnerabilities and development needs
- Strengthening the monitoring and analysis of financial sector, developing guidelines, and promoting transparency and integrity
- building strong institutions

Volz(2013) suggests:

Financial integration requires rigorous regional institutional building to ensure effective monitoring and surveillance.

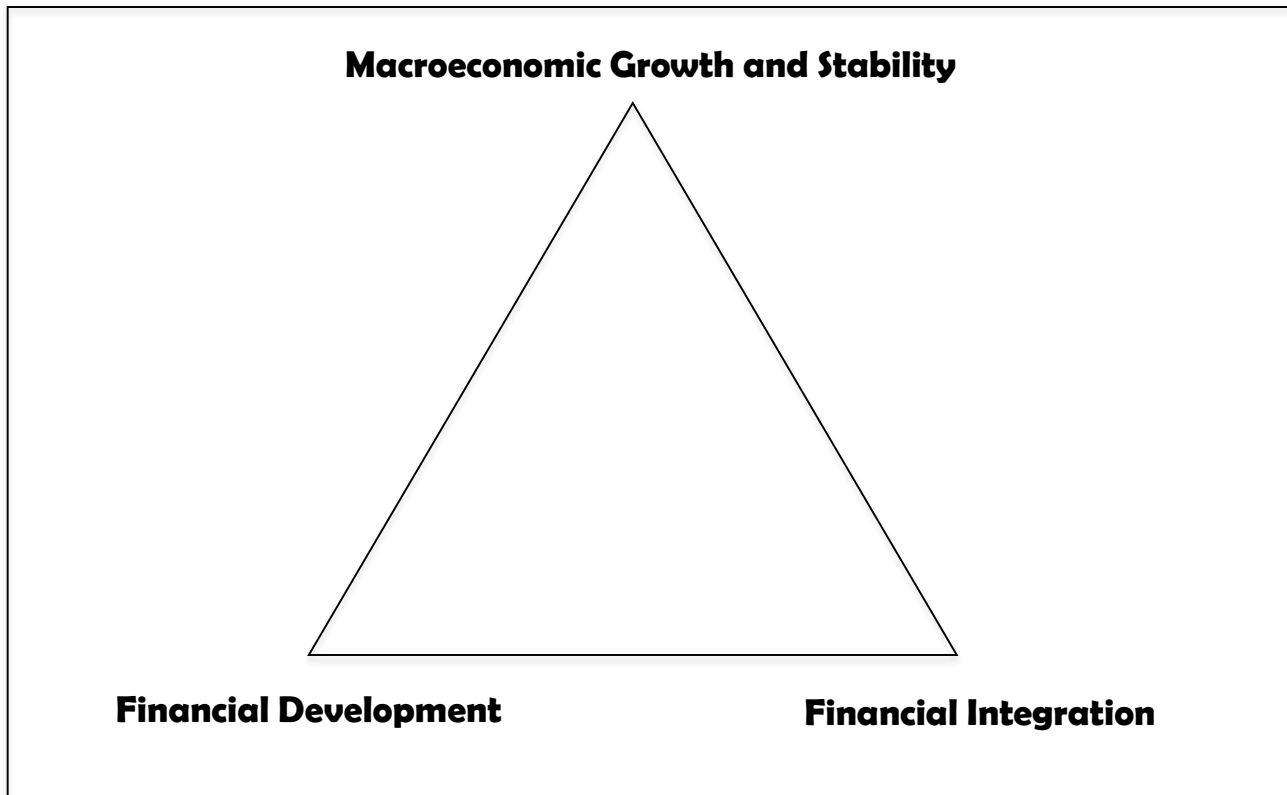
Borensztein and Loungani; IMF; 2011 observed:

- Asian financial system is more financial integrated with global financial markets than with the regional neighbours.
- Cross-border holdings among Asian countries are significant in many cases and have increased over the last decade.

Achieving Macroeconomic Stability through Financial Stability and Financial Market Integration

- Bleaney's (1996); 41 developing countries
He finds some evidence that his measures of policy induced macroeconomic instability are significantly negatively associated with growth
- Ulvedal & Mehлум (2013)
Argue the effect that these, and many other, variables have on economic growth are dependent on the circumstances in which they operate.
- Policies include, for example, the implementation of an open international trade regime, the adoption of national innovation policies, well-functioning factor markets, and an investor-friendly legal and regulatory environment.

The Trilemma in Financial Integration



Source: Author

Some Facts A Global Picture

Financial Development Scores

Source: World Economic Forum (Max Score: 7)

Country	Overall	Institutional Environment	Business Environment	Financial Stability	Banking Financial Services	Non-Banking Financial Services	Financial Markets	Financial Access
Hong Kong	5.31	5.77	6.03	5.35	6.15	3.76	5.04	5.08
Singapore	5.1	6.24	6.03	5.67	4.78	3.44	5.11	4.45
South Korea	4.42	4.18	5.41	4.08	4.37	5.04	3.78	4.06
Malaysia	4.24	5.12	4.85	5.24	4.71	3.23	2.71	3.79
China	4	4.1	3.95	4.89	4.43	4.48	2.98	3.15
India	3.63	3.42	3.61	4.67	2.61	3.24	2.99	4.90
Thailand	3.55	4.22	4.14	4.4	4.08	1.77	2.27	3.94
Pakistan	3.46	3.09	3.48	4.11	3.91	1.73	3.58	4.33
Philippines	3.12	3.94	3.44	3.87	3.02	2.68	2.18	2.74
Indonesia	2.95	3.46	3.49	4.4	2.82	2.38	1.39	2.69
Vietnam	2.92	3.44	3.32	3.26	3.87	1.53	1.99	3.06

Global views: *Financial Development Barometer*

(% of all respondents)	Agree?
"Access to basic financial services is a significant problem for households in my country."	61 %
"Limited access to finance is a significant barrier to the growth of small enterprises in my country."	76 %
"In my country, access to finance has improved significantly over the last 5 years."	78 %
" Social banking (that is, state banks and targeted lending programs to poorer segments of the population) is potentially a useful tool to increase financial access."	80 %
" Social banking actually plays an important role in financial access in my home country."	43 %
"The lack of knowledge about basic financial services is a major barrier to financial access among the poor in my country."	78 %

Source: Financial Development Barometer.

Note: The barometer is an informal global poll of country officials and financial sector experts from 21 developed and 54 developing economies. From 265 polled, 161 responded (61 %). Results are percentages of "fully agree" and "partially agree" responses out of total responses received.

Seven Pillars of Prosperity (IMF Blog; May 2011)

- Reduce the Role of the State
- Generate Openness to new domestic and foreign firms
- Competitive and Efficient Banking Sector
- Governance and Quality of Institutions
- Improvement in Business Environment
- Improvement in Transport and Communications
- Improvement in Regional Trade and Investment Links

East-Asian Experience

- Macroeconomic Policy – a priority
- Coordination among policies
- Specific targets with assessment and accountability
- Learning with experience and flexibility to revise

**Let's
Talk
About**

PAKISTAN

Current Challenges



Security
Challenges

Governance
Challenges

Market Failure

Governance Indicators

Region/Country	Rule of Law	Control of Corruption	Political Stability	Accountability	Government Effectiveness	Regulatory Quality
East Asia	0.13	0.00	0.37	0.08	-0.06	-0.17
Latin America	0.05	0.24	0.25	0.39	0.22	0.18
MENA	-0.17	-0.26	-0.65	-0.90	-0.15	-0.15
SSA	-0.17	-0.59	-0.54	-0.60	-0.75	-0.67
South Asia	-0.62	-0.65	-1.17	-0.50	-0.47	-0.71
Bangladesh	-0.72	-1.00	-1.50	-0.31	-0.85	-1.54
India	-0.08	-0.56	-1.20	0.41	-0.03	-0.34
Pakistan	-0.90	-1.00	-2.70	-0.83	-0.82	-0.61
Sri Lanka	-0.07	-0.42	-0.54	-0.53	-0.08	-0.09

Source: J Lopez-Calix and I Touqeer (forthcoming)

Macro Research – a Priority **BUT**

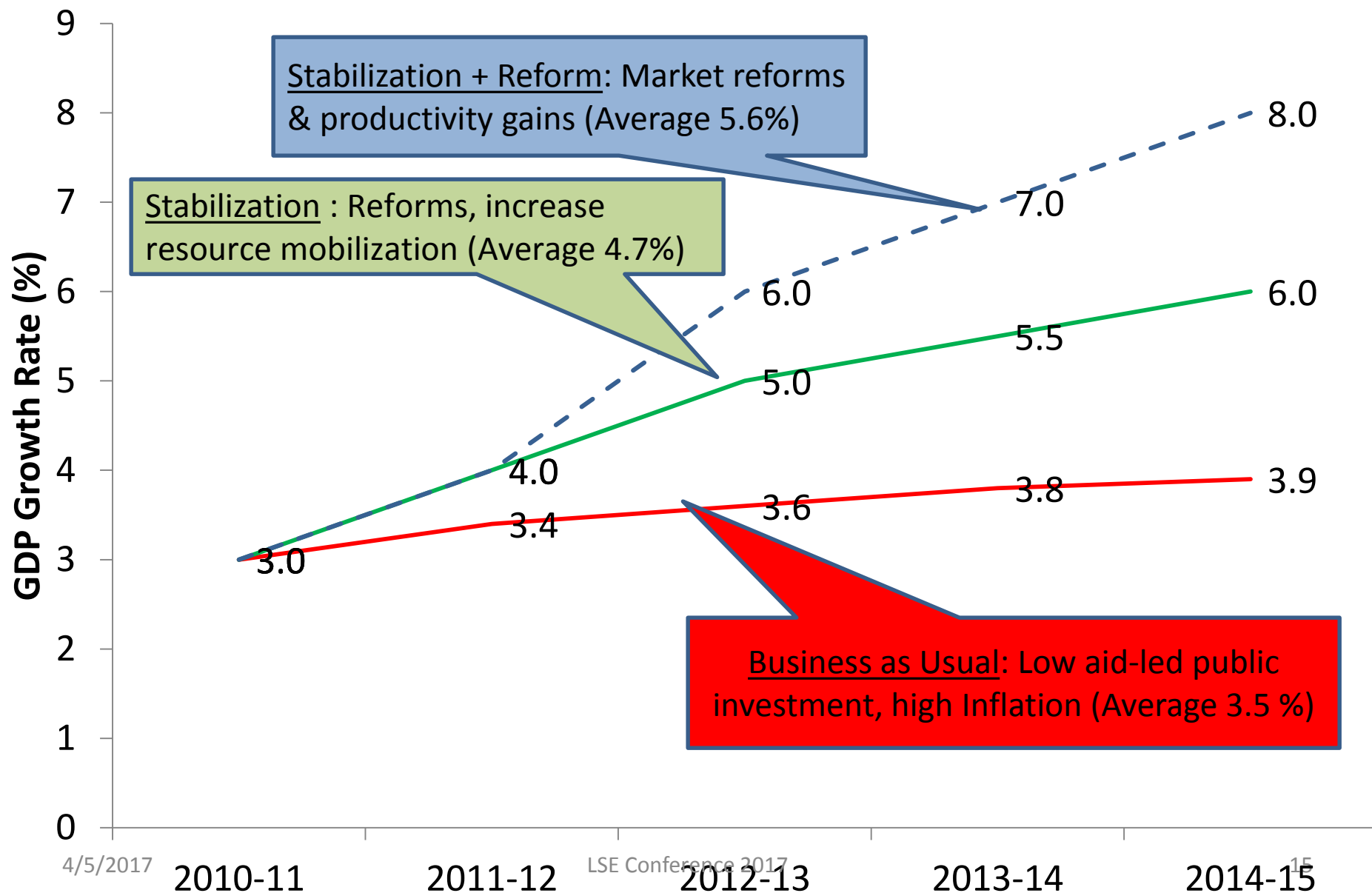
**Macroeconomic Planning without
Macroeconomic Research**

Result – Slow Growth, Unsustainable

**Are not we (macroeconomists and policy
makers) to be blamed?**

Growth Alternatives (2011-15)

False Hopes – Plans but no Implementation



Growth through Integration

Now some empirical evidence

Testable Equation

The underlying model with fixed effects takes the form

$$g_{it} = \beta_0 + \beta_1 FDI_{it} + \beta_2 integ_{it} + \beta_3 controls_{it} + \eta_i + \theta_t + \varepsilon_{it}$$

where g_{it} is economic growth measured by growth of the real GDP in country i at time t . η_i is a country-specific fixed effect, θ_t is a time effect and ε_{it} is a multivariate normally distributed random disturbance.

A fixed effects model, rather than a random effects model is estimated, as the η_i 's are likely to represent omitted country-specific characteristics which are correlated with other explanatory variables.

Variables

- **Growth: real per capita GDP growth**
- **FDI: ratio of FDI to GDP**
- **GFCF: ratio of gross fixed capital formation to GDP**
- **Trade Open: ratio of total trade to GDP**
- **Integr: FII**
- **Chinn-Ito**
- **KOF Index**
- **INF: inflation**
- **GE: ratio of government expenditure to GDP**
- **Pop: growth rate of population**
- **PrCredit: ratio of private credit to GDP**

Data Sources

GDP data came from the U.N. National Accounts database

FDI data were taken from the UNCTAD FDI online database

Data regarding financial assets and liabilities (to calculate the financial integration index) are from the External Wealth of Nations (EWN) database (see Kose et al., 2006)

Population and inflation collected from the World Development Indicators 2005 (World Bank)

Chinn-Ito index is obtained from http://web.pdx.edu/~ito/Chinn-Ito_website.htm

KOF index is downloaded from <http://globalization.kof.ethz.ch/>

Now a Larger Sample

Time: annual, 1989-2013 (25 years).

Countries: Sample of 130 countries

Summary Table

Variables	Overall	High Income	Upper Middle Income	Lower Middle Income	Low Income
FDI + GFCF	+	+	+	+	+
FDI+ Trade	+	+	+	+	+
FDI+ Fin Integ	+	+	+	+	+
FDI+ Chinn-Ito	+	+	+	+	+
FDI+ KOF	+	+	+	+	+

Note: *, **, and *** represent 1%, 5% and 10% level of statistical significance.

Source: Khalid-Marasco (2016).

Policies for Macroeconomic Stability and Sustainable Growth Emerging and Developing Economies

- **Need for sustainable and inclusive growth**
- **Reliance on market system for resource allocation**
- **Effective governance and leadership in building consensus (for policy implementation and enforcement)**
- **Managing the economy (macroeconomic environment)**
- **Focus to mobilize 'Saving and Investment'**
- **Resource mobility (labour productivity is the key)**
- **Transfer of knowledge and technology (G2G, B2B, and G2B)**

THANK YOU!

Pakistan Lacks Growth Software

Hardware

Software

Infrastructure Quality

Country	Score
Indonesia	2.5
India	3.3
China	3.4
Pakistan	3.4
Thailand	5.0
Korea	5.1
Taiwan	5.4
Malaysia	5.7
Hong Kong	6.4

Country	Global Innovation Index (out of 132 countries)	Quality of Education System	Spending on R&D
Pakistan	79	99	80
India	30	37	36
Indonesia	39	44	28
Thailand	57	67	47
Malaysia	24	23	19
China	26	52	23

4/5/2017

Source: Global Competitiveness Report

ISS Conference 2017

Granger Causality Tets

Country	To GDP	From GDP
Bangladesh	Trade to real gdp Chin-Ito to real gdp	real gdp per capita to KOFindex
India	Trade to real gdp	
Pakistan	GFCF to real gdp M2/gdp to real gdp Trade to real gdp	real gdp per capita to Trade real gdp per capita to KOFindex
Sri Lanka	KOF index to real gdp	

Granger Causality Tets

Country	To GDP	From GDP
China		real gdp per capita to GFCF real gdp per capita to M2/gdp
Indonesia	GFCF to real gdp M2/gdp to real gdp	real gdp per capita to Chin-Ito
Malaysia	FDI to real gdp	
Philippines	Trade to real gdp KOF index to real g	
Singapore	GFCF to real gdp	real gdp per capita to FDI real gdp per capita to Chin-Ito

Summary Table

Variables	Overall	High Income	Upper Middle Income	Lower Middle Income	Low Income
FDI + GFCF	+	+	+	+	+
FDI+ Trade	++ ++	+ +	+++ +++	+ +	+ -
FDI+ Fin Integ	+	+	+++ +	+ ++	+ +
FDI+ Chinn ITO	+	+	++ -	+ -	+++ -
FDI+ KOF	+	+	++ +	+++ ++	+ ++
FDI+ Trade + FDI*Trade	- ++ +	- ++ +++	- + ++	- + ++	- - +
FDI+ Integr + FDI*Integr	++ ++ +	++ + ++	++ + ++	+ ++ +	- + -
FDI+ KOF + FDI*KOF	+ + -	+ + +	+ + +	- +++ ++	+ + -
FDI+ Chinn ITO + FDI*Chinn ITO	+	+	++ - +	+ - +	+ - +

Note: *, **, and *** represent 1%, 5% and 10% level of statistical significance.

Source: Khalid-Marasco (2016).

4/5/2017



OUTLOOK FOR PAKISTAN ECONOMY 2013

Due to the recession, economic uncertainty, and to save on energy costs, the light at the end of the tunnel is currently switched off



OUTLOOK FOR PAKISTAN ECONOMY 2018

Hope

Optimism

Encouragement

Relationship between financial stability and financial integration

- Interesting question is, whether financial integration also enhances financial stability
- Research suggest, it does but with certain conditions
 - use of appropriate policy tools which helps to maintain transparency and market confidence
 - ensure long-term viability of financial institutions in business decisions (through reducing agency costs and underlying risk attitude)
 - preventive measures to avoid excessive concentration of risks and leverage to achieve systematic stability
 - tools to reduce the risk of contagion
 - prompt corrective actions in case of a forthcoming crisis (crisis management resolution)
 - good monitoring, assessment and supervision of financial activities leading to financial stability