



**Asia-Pacific
Economic Cooperation**

Advancing Free Trade
for Asia-Pacific **Prosperity**

APEC Regional Trends Analysis

Globalisation: The Good, the Bad, and the Role of Policy

APEC Policy Support Unit
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The views expressed in this paper are those of the authors and do not necessarily represent those of the APEC Member Economies.

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KEY ABBREVIATIONS

| | |
|--------|--|
| ADB | Asian Development Bank |
| FDI | foreign direct investment |
| FTA | free trade agreement |
| GDP | gross domestic product |
| IMF | International Monetary Fund |
| OECD | Organisation for Economic Co-operation and Development |
| PMI | Purchasing Manager's Index |
| PPP | purchasing power parity |
| PSU | Policy Support Unit (APEC) |
| RTA | regional trade agreement |
| UNCTAD | United Nations Conference on Trade and Development |
| WTO | World Trade Organization |

KEY MESSAGES

I. Globalisation: The Good, the Bad, and the Role of Policy

- Globalisation and international trade have contributed to unprecedented growth in human prosperity and welfare, especially in the last 50 years. The material, technological and information exchanges enabled by globalisation have vastly improved living standards and reduced poverty around the world.
- One of the more tangible ways globalisation has helped improve human well-being is in the trade in vaccines. Between 1988 and 2015, tariffs on vaccines were reduced and trade in vaccines grew an average of 24 percent per year. Trade has helped make life-saving vaccines widely available, enabling public health systems to reduce infant and child mortality and practically eliminate debilitating diseases such as polio.
- However, globalisation has not brought benefits to everyone. While trade liberalisation improves overall welfare in the long-run, the process entails difficult adjustments for firms and workers in the short- and medium-run. Trade has indeed increased overall prosperity and employment in economies that open up, but it also brings with it structural unemployment as internationally uncompetitive firms or industries fold up and lay off workers.
- Unfortunately, low- and medium-skilled workers – who are among the least able to cope with structural unemployment – are more likely to be adversely affected by globalisation. In an analysis of trade and employment data from 125 economies over 2000–2014, we find that every 10 percent increase in exports correlates with a reduction in employment among low- and medium-skilled workers of 1.1 to 2.1 percent.
- However, the same data also show that protectionism is not the answer to structural unemployment. There is no evidence that import growth is directly correlated with reduction in employment. Rather, the data seem to point to a positive association between imports and employment.
- Unlike capital, which can seamlessly shift from sector to sector, it takes time and resources for workers to shift from an uncompetitive sector to one offering opportunities. Thus, trade-related adjustments are needed to ameliorate the plight of workers disadvantaged by globalisation. At the economy level, these adjustments include lifelong access to skills training (and retraining), temporary support for households affected by structural unemployment, as well as access to credit to enable entrepreneurial activity.
- At the international level, trade-related adjustment could be facilitated through rules-based trade-related policies that promote greater openness in international markets, as secure access to open global markets will aid in local adjustment due

to fewer trade distortions. Trade could also be made more inclusive through soft laws (i.e., non-legally binding guidelines or policy declarations) in areas such as labour or environmental standards to ensure fair competition.

- Although the concept of inclusiveness in globalisation has been mentioned in APEC declarations as early as the 1994 Bogor Goals, in recent years APEC Leaders have placed ever greater emphasis on ensuring inclusive and sustainable growth in the region. Continuing efforts on quality growth, structural reform, the internationalisation of micro-, small- and medium-sized enterprises (MSMEs), and human capital development are aimed at widely sharing the opportunities and benefits from globalisation among all sectors of society.
- Globalisation is no panacea for society's inequities; but the prosperity, information, and people exchange associated with globalisation could be harnessed to achieve a more equitable distribution of opportunities and benefits. Globalisation alone will not lead to a fairer or more equal society. Maximising the benefits from globalisation requires complementary policies that will ensure inclusiveness and sustainability. It will require the hard work of policymakers and the strength of will of politicians to turn opportunities into reality.

II. Global Economic Momentum and Optimism Fuelling Near-term Growth

- The APEC region expanded by 3.5 percent in 2016, just slightly lower than the year-ago gross domestic product (GDP) growth of 3.6 percent.
- The sustained strength in domestic private and government consumption remained the main fuel of APEC's growth, which, in turn, was boosted by below-peak interest rates and commodity prices as well as government action to pump-prime the economy via fiscal stimulus measures and infrastructure-related expenditures.
- Trade performance in the APEC region started to improve in the second half of 2016. For the whole year of 2016, the aggregate value of APEC's merchandise exports contracted by 4.1 percent, which compares favourably to the 8.7 percent contraction in 2015. The same trend could be observed in imports. This improvement follows world trade which also performed better in 2016 compared to a year ago.
- The improvement in trade growth toward the latter half of 2016 could be traced to stronger global demand, a recovery in commodity prices, and idiosyncratic factors relating to individual economies' pursuit of diversified markets, products and trade partners.
- APEC member economies constituted half of the top 10 foreign direct investment (FDI) recipient economies in 2016. Taken together, FDI inflows to those five APEC economies reached USD 710 billion, equivalent to 46.7 percent of global FDI flows in 2016.
- The entry of FDI into the APEC region was facilitated by investment-friendly measures, which continued to outweigh investment-restrictive measures in the

period mid-May to mid-October 2016. Trade-facilitating measures also outnumbered trade-restrictive measures during the period.

- Near-term GDP projections point to a higher APEC growth of 3.8 percent for 2017–2018, above expected world GDP growth. The APEC region is anticipated to converge with the world economy at 3.7 percent in 2019.
- Forecasts of a higher growth trajectory for both the APEC region and the world in the near term are supported by expectations of more buoyant trade and investment activity; the implementation of fiscal stimulus measures, particularly from the US and China; and the gradual recovery of commodity prices. However, there is also significant uncertainty about trade, monetary and fiscal policies which could give pause to trade and investment activity, adversely affecting economic growth.
- The clarity, transparency and consistency of economic policies could determine the magnitude and direction of economic growth in the near term. In the medium term, macroeconomic management needs to be supported by structural reforms that promote innovation, lead to more competitive markets, facilitate the participation of all segments of society and enhance economic resilience, to contribute to APEC’s aim of achieving sustainable, equitable and inclusive growth.

1 GLOBALISATION: THE GOOD, THE BAD, AND THE ROLE OF POLICY ¹

1.1 INTRODUCTION

Globalisation is increasingly unpopular these days. After decades of trade liberalisation and global interconnectedness, many constituencies are rethinking whether globalisation is working for them, and whether it is in their interest to continue down the globalisation path or to find an alternative one. While there are no serious calls for a return to closed-door autarky (yet), the discourse has shifted, from globalisation as a source of prosperity for all, to one that is more zero-sum and winner-take-all.

This presents a challenge to APEC, which was founded on the principles of free and open trade and a multilateral approach to regional integration. Since its inception, APEC has advocated a unilateral reduction in tariffs and trade barriers, convinced that this would be beneficial for the economy implementing it as well as its trading partners. It prides itself on building consensus among a diverse group of economies, tackling problems and proposing solutions multilaterally. Its meetings and fora are a crucible of ideas for promoting free and open trade, and more recently inclusive and sustainable growth. The questions on globalisation, on whether it has been a force for good for humanity, is a question for APEC itself. Has APEC's work in the past quarter century been beneficial for its constituents? Should APEC do more of the same or start doing things differently?

In their 2016 Lima declaration, APEC Leaders issued a call 'to reach out to all sectors of our societies to better explain the benefits of trade, investment and open markets, and to ensure that those benefits are widely distributed'. This theme chapter is but a humble response to the call. It will show some of the benefits of globalisation, in terms of its impact on economic growth and poverty reduction. But that is just half of the Leaders' call. It will also attempt to shine a light on those who have lost out from trade openness; and perhaps begin to understand the sources of discontent. It will end with a brief discussion of possibilities: what has been done and what can be done to ensure that the benefits of trade and globalisation are widely distributed.

1.2 THE GOOD

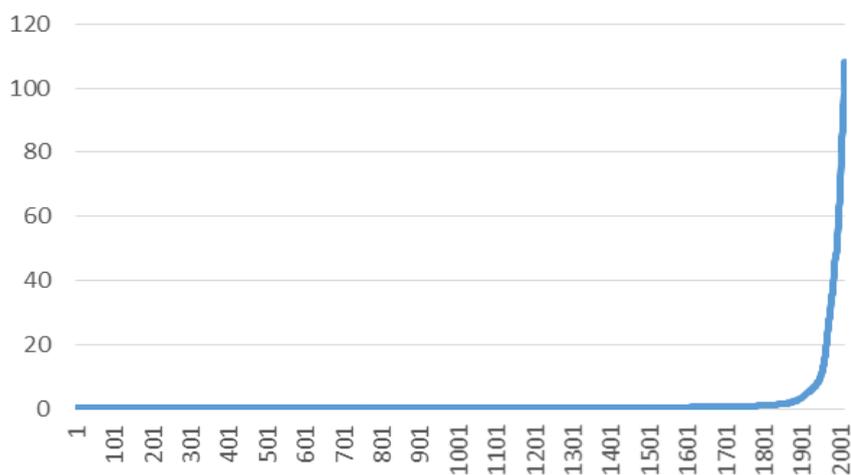
Historically, the global economy experienced very slow growth until the second half of the nineteenth century, when a combination of factors such as technological development (the invention of the steam engine and the utilisation of electricity) and industrialisation, as well as the opening of the Suez Canal, helped to increase productivity and reduce transaction costs.

However, it is only after World War II that the world witnessed rapid progress in terms of economic growth and poverty reduction. Figure 1.1 shows the historic evolution of the global gross domestic product (GDP), whose sharp increase coincided with the times that

¹ Prepared by Carlos Kuriyama, Emmanuel A. San Andres and Satvinderjit Kaur Singh, who are Senior Analyst, Analyst and Intern at the APEC Policy Support Unit (PSU), respectively. Research assistance from Kathrina G. Gonzales is gratefully acknowledged.

economies started to open up and seek ways to economically integrate with others. At the same time, technological developments helped to enhance economic growth through faster and cheaper transportation and access to information technology. Between 1950 and 2015, the world's output grew at an annual average rate of 3.8 percent, much higher than the rates achieved during the periods 1900–1950 (2%), 1820–1900 (1.3%) and 1700–1820 (0.5%).

Figure 1.1 World GDP (in constant 2011 USD, trillions), 1 AD – 2015



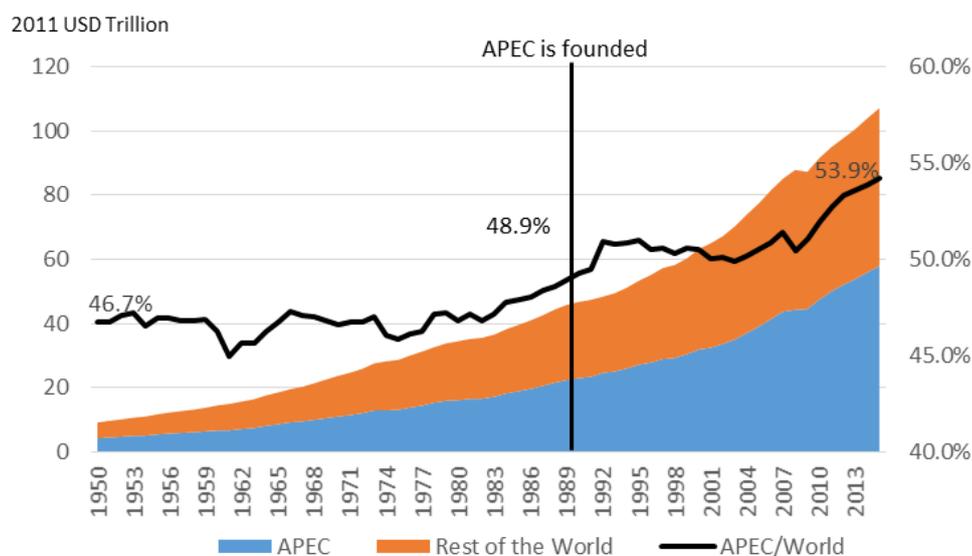
Source: *Our World in Data*, based on World Bank and the New Maddison Project Database.

Part of this rapid economic growth could be attributed to trade. Trade increases demand from overseas, which spurs domestic economic activity by encouraging the production of goods and services for export. At the same time, imports are not necessarily bad for the economy. They could facilitate technological transfers, increase productivity and improve export competitiveness. Companies could benefit from a wider range of suppliers, and customers from a wider range of products. Long-term foreign investment could also help to increase the productive capacity of economies and assist in the creation of jobs.²

² See: Kuriyama, C. and E. San Andres, 'Trade and economic growth: 25 years of a stronger relationship within APEC' (policy brief, Singapore: APEC Secretariat, 2014), 2.

The creation of APEC in 1989 spurred its members to encourage business facilitation and promote economic openness, which in turn contributed to economic growth in the APEC region. Figure 1.2 shows that the share of APEC in world GDP increased from 48.9 percent to 53.9 percent between 1989 and 2015. In fact, the historical data show that the upward trend in the contribution of APEC economies in world GDP became more apparent after APEC's inception.³

Figure 1.2 Share of APEC in world GDP, 1950–2015



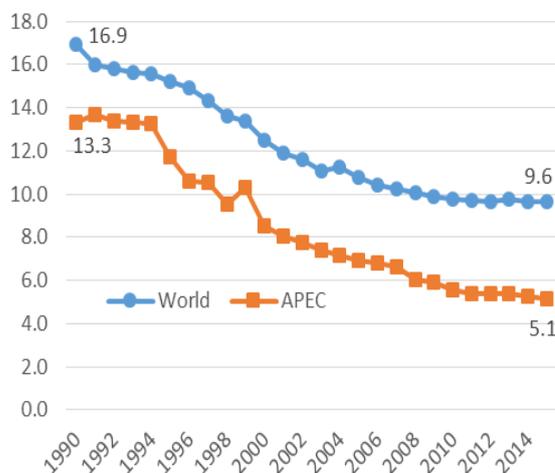
Source: Penn World Tables; Stats APEC; APEC PSU calculations.

Trade has played an important role in the APEC region's economic growth, with APEC economies being particularly active in implementing open trade and investment policies. APEC economies have substantially reduced their average tariffs and have been very active in pursuing free trade agreements (Figure 1.3 and Figure 1.4). These factors played an important role in expanding APEC's trade and prosperity.⁴

³ APEC GDP per capita growth rates have also increased since its inception. During the period 1989–2015, it was equivalent to 2.8 percent per year, greater than that of the period 1950–1989 (2.5 percent per year).

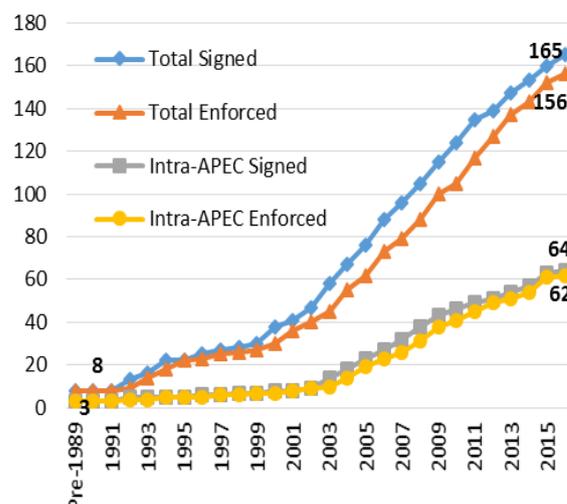
⁴ When APEC was founded in 1989, its share in world merchandise trade was equivalent to 40.2 percent. By 2015, APEC's participation had increased to 50.1 percent of the world merchandise trade.

Figure 1.3 Average tariffs, APEC and world



Note: The figures take into account ad-valorem equivalent duties as calculated by UNCTAD.
Source: UNCTAD Trade Analysis Information System (TRAINS); WTO; APEC PSU calculations.

Figure 1.4 FTA/RTAs signed and enforced by APEC economies



Source: APEC PSU.

APEC's openness has made its GDP growth comparatively more responsive to trade growth. According to estimates by Kuriyama and San Andres,⁵ in the period 1989–2013, a 10 percent growth in trade in APEC was correlated with a 5.6 percent growth in GDP (around USD 123 billion of additional GDP in real terms⁶), while for the rest of the world, a similar increase in trade was associated with a 3.9 percent increase in GDP (around USD 68 billion in real terms).⁷

Trade openness has been linked not just to economic growth, but also to poverty reduction, as trade could create new job opportunities, lower prices for consumers and increase wages in sectors that can export competitively.⁸ The gains from trade also provide fiscal space for governments to improve public services to benefit the population, including the most disadvantaged groups. Panagariya found that no economy growing consistently – at 3 percent or more in per capita terms – had not had its trade growing rapidly and failed in reducing poverty.⁹ In many cases, globalisation has contributed to increasing household incomes, and consequently has played a role in reducing poverty worldwide. According to Roser and Ortiz-Ospina, the change has been very impressive, especially if compared with

⁵ Kuriyama, C. and E. San Andres, 'Trade and economic growth'.

⁶ In 2005 US dollars.

⁷ A number of studies have corroborated this positive relationship between trade and economic growth. See: Frankel, J.A. and D. Romer, 'Does trade cause growth?' *American Economic Review* 89, no. 3 (June 1999): 379–99; Wacziarg, R. and K.H. Welsh, 'Trade liberalization and growth: new evidence', *The World Bank Economic Review* 22, no. 2 (2008): 187–231; Edwards, S., 'Openness, productivity and growth: what do we really know?' (working paper, Cambridge, MA: National Bureau of Economic Research, 1997); Gries, T. and M. Redlin, 'Trade openness and economic growth: a panel causality analysis' (working paper, Paderborn: University of Paderborn, Center for International Economics, 2012).

⁸ World Bank and WTO, *The Role of Trade in Ending Poverty* (Geneva, WTO, 2015), 19–25.

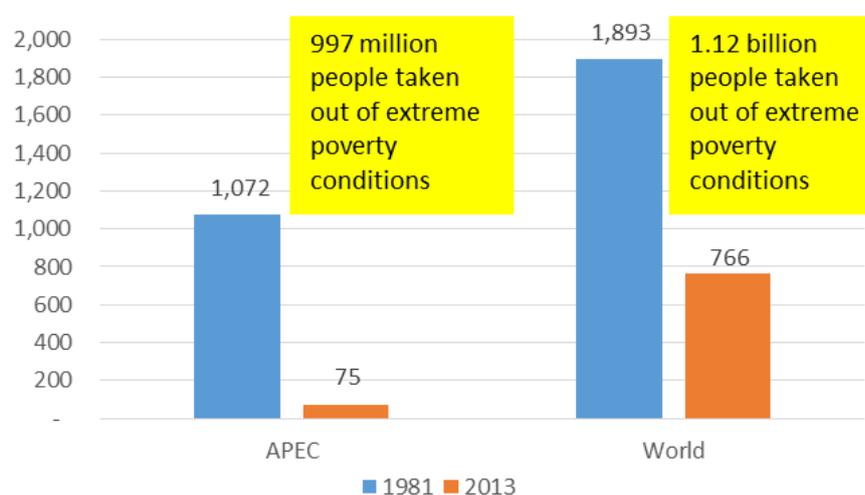
⁹ Panagariya, A., 'Miracles and debacles: do free-trade skeptics have a case?' (policy paper, 2003).

historical estimates;¹⁰ in 1820, 84 percent of the population lived under extreme poverty conditions, subsisting on less than USD 1 per day.

However, to take full advantage of trade, it is critical that trade policies go hand-in-hand with other policies that help the poor to benefit from the opportunities that openness could provide. In this regard, a study by Le Goff and Singh noted that more openness results in a reduction of poverty when the access to private credit is deeper, education levels are higher and the quality of institutions is strong.¹¹

Our own calculations using the World Bank's poverty data indicate that the share of the world population living under the new definition of extreme poverty (USD 1.90 per day) fell from 41.9 percent to 10.7 percent between 1981 and 2013 (Figure 1.5). In absolute terms, this amounted to 1.12 billion people getting out of extreme poverty.

Figure 1.5 People living under extreme poverty conditions (million)



Note: Extreme poverty is defined as living on less than USD 1.90 per person per day, in 2011 PPP dollars.

Source: World Bank, PovCal; APEC PSU calculations.

Progress in the APEC region has been outstanding as well, with 997 million people taken out of extreme poverty conditions between 1981 and 2013. More impressive is the fact that APEC economies accounted for 88.5 percent of the reduction of the extreme poor population in the world. Currently, only 9.8 percent of the world's extreme poor live in the APEC region and only 2.7 percent of the APEC population live in extreme poverty, a substantial improvement from 1981 when 53.4 percent of people in the APEC region were considered extremely poor.

Poverty is still a pressing issue: 2.48 billion people, or 34.6 percent of the global population, currently live in poverty (i.e., less than USD 3.80 per person per day).

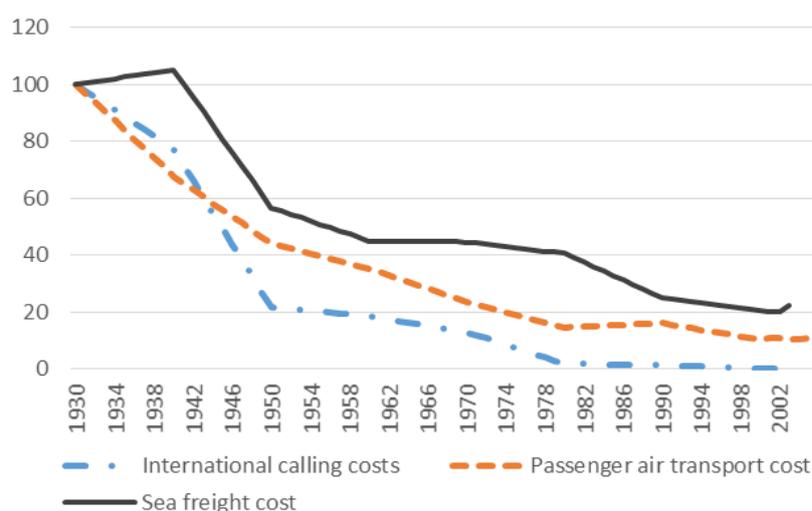
¹⁰ See: Roser, M. and E. Ortiz-Ospina, 'Global extreme poverty', *Our World in Data*, 27 March 2017, <https://ourworldindata.org/extreme-poverty/> (accessed 5 May 2017).

¹¹ Le Goff, M. and R.J. Singh, 'Does trade reduce poverty? A view from Africa' (working paper, Washington, DC: World Bank, 2013), 10–12.

However, it is also important to acknowledge the massive reduction in poverty in the last three decades, coinciding with the period when economies implemented important economic reforms and gradually opened their markets. In 1981, 2.71 billion people were poor; there are 227 million fewer poor people now.

Globalisation is making life easier, cheaper and faster for firms and households alike. Transportation and telecommunication costs have fallen significantly in recent decades (see Figure 1.6). Investments in infrastructure and new inventions have allowed goods to be shipped faster and at a lower cost and they have opened the door to global value chains. Travel has become more affordable, while advanced technologies in telecommunications are making it possible to have access to information faster than ever. It is easier to coordinate business and agree on (and enforce) contracts regardless of geographic distance. Firms and customers are closer and have more access to a myriad of services and products. In general, globalisation has been very positive: more information is flowing across borders and people have more opportunities to learn from other cultures and places around the world.

Figure 1.6 Transport and communication costs (index 1930 = 100)



Source: *Our World in Data*; based on OECD Economic Outlook 2007.

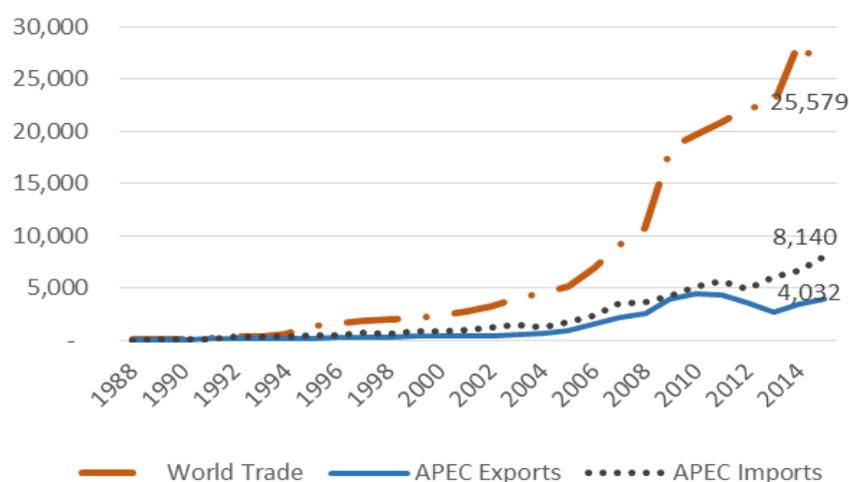
Living conditions have significantly improved since the end of the World War II. Between 1960 and 2015, the average life expectancy worldwide at birth went up from 52.5 to 71.7 years.¹² Progress in the medical sciences and increased affordability of medicines are allowing people to live longer. For example, in the nineteenth century, even the richest people could die of an infection that could be treated nowadays with cheap antibiotics.¹³ In the twentieth century, the development of vaccines and their accessibility helped reduce infant and child mortality rates and contributed to the eradication of smallpox and the near eradication of polio.

¹² Based on data from the World Bank's World Development Indicators.

¹³ Roser and Ortiz-Ospina, 'Global extreme poverty'.

Trade liberalisation has been a key component in the accessibility of vaccines for human use worldwide. In the 1990s, vaccines were charged most favoured nation (MFN) tariffs of at least 5 percent in at least 73 economies and at least 10 percent in 30 economies. By 2015, only 16 economies imposed tariffs of 5 percent or more and only one economy imposed tariffs on vaccines of above 10 percent. Figure 1.7 shows an exponential growth in the worldwide trade in vaccines for human use. During the period 1988–2015, their global trade multiplied 353 times, from USD 73 million to USD 25.6 billion (i.e., 24.3 percent growth per year).

Figure 1.7 Worldwide trade in vaccines for human use (USD million)



Source: World Integrated Trade Solution (WITS), UN Comtrade; APEC PSU calculations.

On the environment, while it is true that greenhouse gas emissions have escalated substantially since the Industrial Revolution, globalisation also provides an opportunity to protect the environment. Environmental awareness is rising and there have been efforts to implement global actions. For example, the Montreal Protocol, a multilateral agreement, has been effective in phasing out substances affecting the ozone layer and restricting their trade. Furthermore, governments are trying to tackle the emission of sulphur dioxide (SO₂). It is a promising sign that SO₂ levels worldwide fell by 36 percent and death rates from air pollution fell from 132 to 104 per 100,000 people between 1980 and 2010.¹⁴

Pro-globalisation policies could also help to reduce child labour and increase school attendance. A study on child labour in Viet Nam found that the implementation of export quotas in 1989 had suppressed domestic rice prices. The subsequent relaxation and removal of rice export quotas in the mid-1990s helped to increase farmers' incomes, as they were able to take advantage of the higher international price of rice. Higher incomes then motivated rice farmers to send their children to school and contributed to 1 million fewer working children in Viet Nam.¹⁵ Expanding on this finding, Edmonds and Pavcnik conducted a cross-economy study on child labour and trade, and reported that a 10 percent

¹⁴ Ritchie, H. and M. Roser, 'Air pollution', *Our World in Data*, 2017, <https://ourworldindata.org/air-pollution/> (accessed 5 May 2017).

¹⁵ Edmonds, E., 'Globalization and the economics of child labor' (Dartmouth College, 2002), 4.

increase in the share of trade in GDP was associated with a 7 percent decline in child labour.¹⁶

1.3 THE BAD

While trade and globalisation have indeed resulted in increased prosperity and rapid poverty reduction especially in the long-run, these gains can come with difficult and costly adjustments for some workers and industrial sectors. Even the devoted trade liberaliser would agree that the competition and specialisation from trade will result in uncompetitive sectors dwindling and associated jobs disappearing.

Name any theory in international economics – Ricardo, Heckscher-Ohlin, Stolper-Samuelson, Krugman – and you will not find one that says international trade will always be painless for everyone. This is because the benefits of trade – which come from specialisation in the production of goods and services in which an economy has a comparative advantage – necessarily mean a reduction in the production of goods and services in which the economy does not have a comparative advantage. While this may improve efficiency in the economy and raise overall welfare levels, it does mean that the firms in non-competitive industries will not survive, and their workers will become structurally unemployed. The displacement of some workers due to international trade, predicted in theory, and cautioned against before the advent of globalisation in the 1990s, has been taking place in recent decades.

When firms in non-competitive sectors close, factor and production reallocation do not automatically occur; and workers who are laid off may not easily find alternative employment. At a time when APEC Leaders are focusing on inclusive growth, a valid question is whether trade growth is conducive to inclusive growth. Empirically, the relationship between international trade and inequality is complicated. While many economists have studied this issue, there is no clear scientific consensus on whether trade ameliorates or worsens inequality (Table 1.1). This may be because many of the factors that affect inequality – like ex-ante wealth distribution, access to social services and insurance, institutions, or human capital investment – have nothing to do with trade.

¹⁶ Edmonds, E. and N. Pavcnik. 'International trade and child labor: cross-country evidence' (working paper, Cambridge, MA: National Bureau of Economic Research, 2004), 22–3.

Table 1.1 Selected papers examining the relationship between trade and inclusive growth

| No. | Paper | Type of analysis | Measures of trade openness | Measures of inclusive growth | Relationship between trade openness and inclusive growth |
|-----|--|--|--|--|--|
| 1 | Aoyagi and Ganelli (2015) | Cross-country | Sum of export and import divided by GDP | Measure of growth in average income corrected for the equity impact | Positive and significant |
| 2 | IMF (2007) | Cross-country | - Export-to-GDP ratio - 100 minus tariff rate | Income distribution as measured by Gini coefficient ^a | Reduction in Gini coefficient (i.e., positive and significant) |
| 3 | Perry and Olarreaga (2006) | Cross-country | Adjusted trade volume divided by GDP | Gini coefficient | Increase in Gini coefficient (i.e., negative and significant) |
| 4 | Lundberg and Squire (2003) | Cross-country | Sachs-Warner index ^b | Measurement-adjusted Gini from augmented Deininger-Squire dataset | Increase in Gini coefficient (i.e., negative and significant) |
| 5 | Dollar and Kraay (2002) | Cross-country | Sum of export and import divided by GDP | Income of the poorest 20 percent of the population | Trade does not reduce the income of the poor (i.e., insignificant) |
| 6 | Razaque and Raihan (Vols I and II, 2008) | Review of individual economy experiences | Various | Various | Economy- and sector-specific (i.e., inconclusive) |
| 7 | Goldberg and Pavcnik (2007) | Review of individual economy experiences | Various | Various | Economy-, case- and time-specific (i.e., inconclusive) |
| 8 | Topalova (2007) | Individual economy | Tariff data | - Proportion of population below poverty line - Normalised aggregate shortfall of poor people's consumption from the poverty line | Increase in poverty rate and gap in rural districts (i.e., negative and significant) |
| 9 | Wei and Wu (2007) | Individual economy | Export-to-GDP ratio | Ratio of per capita incomes in urban to rural areas | Decline in urban-rural inequality (i.e., positive and significant) |

Notes: a. The Gini coefficient is a measure of income inequality which ranges from 0 (perfect equality) to 100 (complete inequality); b. Sachs-Warner index: An economy is deemed to be open to trade if it satisfies four tests: (1) average tariff rates below 40 percent; (2) average quota and licensing coverage of imports of less than 40 percent; (3) a black market exchange rate premium that averaged less than 20 percent during the decade of the 1970s and 1980s; (4) no extreme controls (taxes, quotas, state monopolies) on exports.

Source: Hernando, R.C., E. San Andres and A. Wirjo, *Trade, Inclusive Growth, and the Role of Policy* (Singapore: APEC Secretariat, 2015), Table 1.

One argument is that while trade cannot be blamed for inequality, it does not contribute to reducing it either. A study by San Andres and Wirjo found that the relationship between trade growth and inclusive growth (defined as growth in mean household incomes coupled

with reductions in inequality) ranges from insignificant to significantly negative.¹⁷ They hypothesise that this could be due to the skill bias of APEC trade. Practically all of the top 10 most traded products in the region are skill-intensive, hence trade growth is most likely to directly benefit skilled workers (who are more likely to be well-off) than non-skilled workers (who are more likely to be poor).

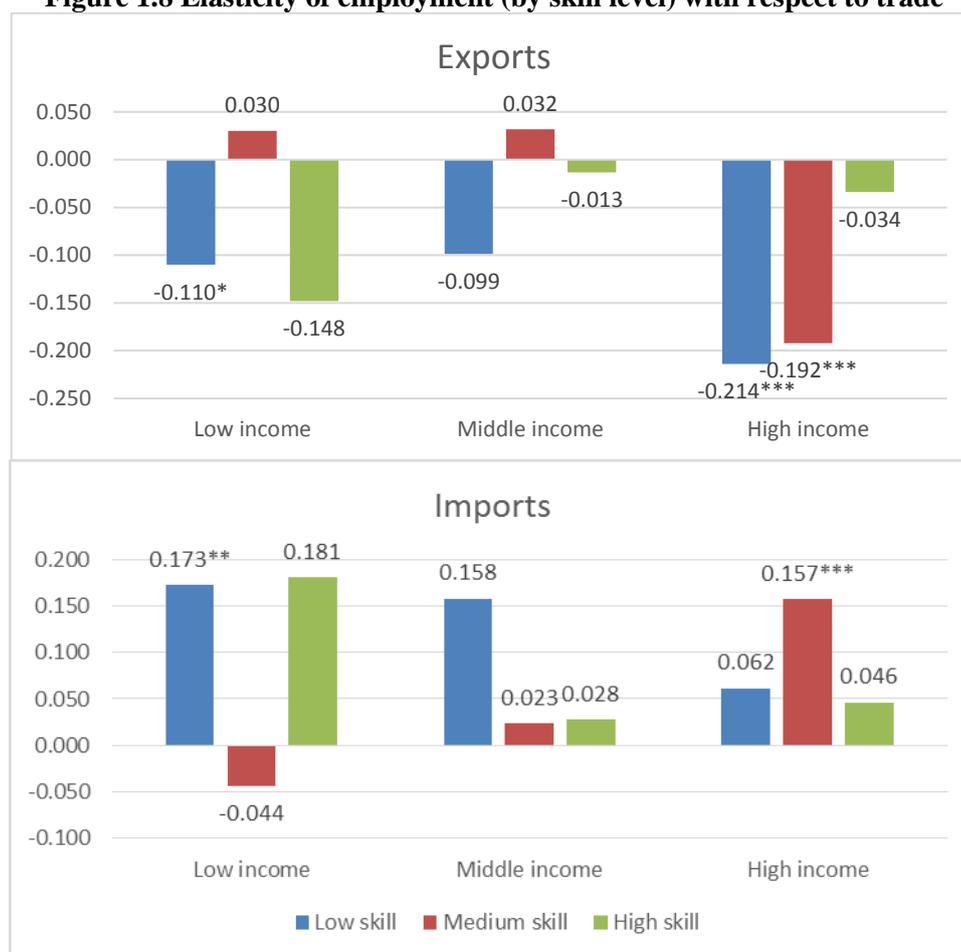
For a deeper understanding of the issue, we analyse skill-disaggregated employment data from 125 economies over the period 2000–2014, looking at the relationship between increases in exports and imports and increases (or decreases) in employment of workers of various skill levels. This involves estimating the percentage change in employment that is correlated with a 10 percent increase in imports or exports while controlling for changes in other variables such as GDP or population growth as well as reverse causality.¹⁸ Skill levels are based on International Labour Organization (ILO) definitions; and are classified into three categories: low skill (elementary occupations with simple and routine tasks), medium skill (clerical, service and sales workers; skilled agricultural and trades workers; plant and machine operators and assemblers) and high skill (managers, professionals and technicians). We also do separate analyses for high-, middle- and low-income economies based on the International Monetary Fund (IMF) classification.¹⁹

Elasticity estimates are shown in Figure 1.8. The first observation is that the majority of the elasticity estimates of employment with respect to trade, after controlling for indirect effects coursed through GDP, are statistically insignificant. This implies that trade per se has varying impacts on employment at most skill levels; it can increase it or decrease it depending on the industry and economy so at the aggregate the results are inconclusive.

¹⁷ E. San Andres and A. Wirjo, ‘Trade, inclusive growth, and the role of policy’, in Hernando, R.C., E. San Andres and A. Wirjo, *Trade, Inclusive Growth, and the Role of Policy* (Singapore: APEC Secretariat, 2015), 1–10.

¹⁸ Technically, we estimate elasticities of employment by skill level with respect to trade (i.e., imports and exports) separately. To control for reverse causality, we use the Arellano-Bond estimation method using lags of employment as the instrument. We use robust standard errors and control for GDP, population, structural transformation (i.e., proportion of agriculture value-added in GDP), WTO membership and year-specific idiosyncrasies.

¹⁹ Among APEC economies, the low-income economy based on the IMF classification is Viet Nam. Middle-income economies are Chile; China; Indonesia; Malaysia; Mexico; Peru; the Philippines; Russia; and Thailand. High-income economies are Australia; Canada; Hong Kong, China; Japan; Korea; New Zealand; Singapore; Chinese Taipei; and the United States. Brunei Darussalam and Papua New Guinea are not included in the econometric analysis due to data constraints.

Figure 1.8 Elasticity of employment (by skill level) with respect to trade

Notes: *** = significant at 95% confidence level; ** = significant at 90% confidence level; * = significant at 85% confidence level.

Source: ILO; IMF; World Bank; Directorate-General for Budget, Accounting, and Statistics (Chinese Taipei) data; APEC PSU calculations.

There are nevertheless a few significant findings. With respect to exports, two groups seem to be adversely affected: low-skilled workers in low-income economies and low- to middle-skilled workers in high-income economies. For these workers, every 10 percent increase in exports is significantly correlated with a contemporaneous reduction in their employment by 1.1 to 2.1 percent. While these findings are preliminary, these could be a clear identification of the ‘losers’ from globalisation, those whose jobs disappeared because the economy has reallocated resources away from their sectors. Unfortunately, these low- to medium-skilled workers are also more likely to be from poorer households, so structural unemployment will have a serious impact. They would also likely have less access to skills training or entrepreneurial capital, making structural unemployment a persistent situation if their skills are not transferrable to another sector. Hence, these workers could be the constituencies that would demand more protection for their jobs and livelihoods, no matter how uncompetitive their industries are.

Yet, despite conventional knowledge, the findings in Figure 1.8 indicate that protectionism is not necessarily the answer to trade-related shifts in labour demand. Only two elasticities from the imports perspective are statistically significant – for low-skilled workers in low-income economies and middle-skilled workers in high-income economies – and they are

both on the positive side. This shows that imports are not the bogeyman of domestic employment they are portrayed to be. They either have no significant impact on employment, or have a significantly positive impact. Note that this is a pure imports effect; the effects through value chains and imported inputs are already controlled for. Rather, these could be pointing to the impacts of imports on employment in import-heavy services such as tourism, retail or transportation, many of which hire low- to medium-skilled workers.²⁰

Workers lose out from globalisation mainly due to two reasons: changes in demand for labour and changes in demand for skills.²¹ Changes in demand for labour come about due to differences in the export competitiveness of various sectors, which lead to the expansion of some sectors and contraction of others.²² Demand for labour hence changes in a particular economy as different industries expand and compete in the globalised economy.

The demand for skilled workers increases when there are shifts in technology or when the high-skilled sector becomes competitive after trade liberalisation and starts to draw in factors of production. Skilled workers also become more sought after when the low-skilled sector flourishes, as this creates opportunities and incentives for the low-skilled sector to invest in technology in order to stay competitive. Skill-biased technological change results in some workers losing out to globalisation as the more technologically advanced sector demands more skilled labour and raises the relative return to skills.²³ This also widens wage disparities between skilled and unskilled workers, and could render some skilled workers unemployed or underemployed if their skills become obsolete or automated. This issue of skills mismatch is a problem for APEC economies, where many workers remain unemployed while a large number of firms are constrained by the lack of an adequately skilled workforce.²⁴

As a result of labour market frictions and skill mismatches, many people are left structurally unemployed and firms forced to shut down. Firms may move their operations offshore or outsource their activities abroad to remain competitive, leaving former domestic employees without jobs.²⁵ Moreover, workers who are adversely impacted by globalisation enter into a vicious cycle of poor health and financial conditions.²⁶ Hence, without any mitigating measures to ameliorate the pain of structural unemployment and to open new doors of opportunity, negatively affected workers will see globalisation as a bane and gravitate toward policy directions that can promise relief.

²⁰ Cf. study on the linkages between tourism, inclusive growth, and trade in: San Andres, E., D. Cheok and L. Othman, 'Tourist arrivals and inclusive growth' (issues paper, Singapore: APEC Secretariat, 2016).

²¹ IMF, World Bank and WTO, *Making Trade an Engine of Growth for All: The Case for Trade and for Policies to Facilitate Adjustment* (policy paper, Washington, DC: IMF, 2017).

²² Harrison, A., J. McLaren and M.S. McMillan, 'Recent findings on trade and inequality' (working paper, Cambridge, MA: National Bureau of Economic Research, 2010).

²³ Goldberg, P.K. and N. Pavcnik, 'Distributional effects of globalisation in developing countries' (working paper, Cambridge, MA: National Bureau of Economic Research, 2007).

²⁴ APEC, 'Mismatch in Asia-Pacific labour markets' (submission by Australia at the *Roundtable Conference on Building Human Resource Development Partnerships for Innovative Growth and Sustainable Development*, Medan, Indonesia, 22–25 June 2013),

http://mddb.apec.org/Documents/2013/HRDWG/FOR/13_hrdwg_for_014.pdf (accessed 5 May 2017)

²⁵ Levine, L., 'Unemployment through layoffs and offshore outsourcing' (Washington, DC: Congressional Research Service, 2010).

²⁶ Davis, S.J. and T. von Wachter, 'Recessions and the costs of job loss' (Washington, DC: Brookings, 2011), 1–72.

1.4 THE ROLE OF POLICY

Unlike capital, which can seamlessly shift from sector to sector, it takes time and resources for workers to shift from an uncompetitive sector to one offering opportunities. An automotive mechanic today will not suddenly be an app developer tomorrow. Thus, trade-related adjustments are needed to ameliorate the plight of workers disadvantaged by trade liberalisation. These include investments in activities that facilitate switching of jobs and industries, and implementation of social safety nets to reduce the insecurities related to frictions in the labour market.²⁷ These adjustments are costly, time-consuming and involve a reallocation of resources toward the activities.

Longer-term adjustment policies to ameliorate structural unemployment include investments in retraining programmes. An example is the Trade Adjustment Assistance (TAA) programme in the United States that provides retraining and job search assistance, which has been found to increase the employment rates of the participants.²⁸ Another is the retraining and placement services provided by Mexico's labour retraining programme (PROBECAT),²⁹ which has been successful in increasing employment and wages in the medium term.³⁰ Likewise, China's 'Three Year 10 Million Program', which aims to retrain 10 million laid off workers within three years, was able to achieve a re-employment rate of 65 percent (i.e., 8.82 million workers) after its first implementation between 1998 and 2000.³¹

At the same time, shorter-term measures like income support and unemployment insurance are necessary to alleviate the immediate effects of structural unemployment and enable participation in job search and retraining activities. Canada introduced Employment Benefits and Support Measures (EBSM) in 1996 to get unemployed people back into the labour market quickly with the help of wage subsidies, earnings supplements and loan grants. An analysis of the programme found 293,000 participants returning to the labour market during the period 1999 to 2000.³² The European Globalisation Adjustment Fund (EGF) was set up by the European Union (EU) in 2007 to help those affected by mass redundancies resulting from structural changes. The programme's training, relocation and subsistence allowances supported 27,610 people during 2013 to 2014, achieving a 50 percent re-employment rate.³³

Complementary policies like providing access to credit and housing and better infrastructure and education have also been shown to stabilise the economy and facilitate the adjustment process. Aid for Trade, led by the WTO, has helped developing economies

²⁷ IMF et al., *Making Trade an Engine of Growth for All*.

²⁸ Rosen, H.F., 'Reforming trade adjustment assistance: keeping a 40-year promise' (paper presented at *Trade Policy in 2002*, Peterson Institute for International Economics, Washington, DC, USA, 26 February 2002).

²⁹ PROBECAT = *Programa de Becas de Capacitacion para Trabajadores* (Worker Training Scholarship Programme).

³⁰ Baker, J.L., 'Evaluating the impact of development projects on poverty' (Washington, DC: World Bank, 2000).

³¹ Liu, Y., 'Massive retraining programs in China', *World Bank*, 2004, http://siteresources.worldbank.org/EDUCATION/Resources/278200-1126210664195/1636971-1126210694253/Retraining_Programs.pdf (accessed 5 May 2017).

³² OECD, *OECD Reviews of Regulatory Reform: Canada 2002 – Maintaining Leadership through Innovation* (Paris: OECD Publishing, 2002).

³³ European Commission, 'Employment: almost 30 000 workers supported by the European Globalisation Adjustment Fund during 2013 and 2014', press release, 22 July 2015, http://europa.eu/rapid/press-release_IP-15-5412_en.htm (accessed 5 May 2017).

build the capacity and infrastructure required to exploit free trade opportunities. A study found that a 10 percent increase in trade-related infrastructure investment through the initiative led to a 2.3 percent increase in an economy's exports-to-GDP ratio.³⁴ Another example is Viet Nam's investment in education, infrastructure and welfare, which along with rapid growth in trade and GDP, has enabled the economy to reduce poverty by half in a span of 10 years.³⁵ Easier access to credit also supports adjustment by empowering the unemployed to start their own businesses and pursue education or training. Schemes providing greater access to credit have enabled small- and medium-sized enterprises (SMEs) to flourish in Brunei Darussalam. The SMEs have in turn contributed 92 percent of the private-sector employment opportunities.³⁶

On a global level, trade-related adjustment can be facilitated through rules-based trade-related policies that promote greater openness in international markets, as secure access to open global markets will aid in local adjustment due to fewer trade distortions.³⁷ Customised policies to ease the local adjustment process are desirable as well. For example, policies that facilitate gradual opening of markets can prevent labour market congestion resulting from layoffs.³⁸ Trade can also be made more inclusive through soft laws.³⁹ For example, greater enforcement of ILO labour standards will assure fair treatment of domestic workers despite foreign competition. Likewise, mutual efforts toward maintaining environmental standards will prevent situations where some economies are disadvantaged by exclusively incurring the cost of investments in environment-friendly equipment and practices.⁴⁰

In order to maximise the benefits of globalisation, these domestic and international policies need to be implemented along with efforts to liberalise markets. Trade openness needs to go hand-in-hand with complementary structural and social reforms to generate a growth path that is inclusive and sustainable, and avoid sluggish or sputtering growth which could slow down future efforts toward further liberalisation and create scepticism about globalisation and its benefits.

³⁴ Negin, J., 'Understanding Aid for Trade part one: a dummy's guide', blog, *DevPolicyBlog*, 28 February 2014, <http://devpolicy.org/understanding-aid-for-trade-part-one-a-dummys-guide-20140228/> (accessed 5 May 2017).

³⁵ Dollar, D., 'Making globalisation work for the poor', discussion transcript, *World Bank*, 2 February 2004, <http://live.worldbank.org/making-globalisation-work-poor> (accessed 5 May 2017).

³⁶ APEC, 'Women and SMEs in Brunei Darussalam' (submission by Brunei Darussalam to the *1st Joint Ministerial Meeting on Small and Medium Enterprises and Women*, Bali, Indonesia, 7 September 2013).

³⁷ IMF et al., *Making Trade an Engine of Growth for All*.

³⁸ Bacchetta, M. and M. Jansen, *Making Globalisation Socially Sustainable by 2011* (Geneva: ILO and WTO, 2011).

³⁹ Soft laws are quasi-legal instruments that are not legally binding. In the context of international law, these could refer to resolutions, guidelines, declarations or codes of conduct.

⁴⁰ IMF et al., *Making Trade an Engine of Growth for All*.

1.5 THE ROLE OF APEC

While APEC has historically focused on cross-border economic issues such as trade and investment liberalisation, it has been promoting inclusive growth among its members albeit in a limited capacity. Inclusiveness has been discussed as early as 1994 as part of the Bogor Goals Declaration, when Leaders stated their goal to ‘attain sustainable growth and equitable development of APEC economies, while reducing economic disparities among them, and improving the economic and social well-being of our people’.⁴¹

Inclusiveness as a goal was explicitly mentioned in the 2010 APEC Leaders’ Growth Strategy,⁴² where it is stated that ‘APEC members cannot continue with “growth as usual” and “the quality of growth” needs to be improved, so that it will be more balanced, inclusive, sustainable, innovative, and secure’. This is also expounded in the APEC Strategy for Strengthening Quality Growth initiated in 2015, part of which aims to pursue job creation, entrepreneurship development and social welfare in a sustainable manner.

The Boracay Action Agenda 2015 aims to increase inclusivity by improving opportunities for micro-, small- and medium-sized enterprises (MSMEs) to participate in global trade. To do so, the agenda prioritises strengthening institutional support for MSMEs, giving greater focus to those led by women, streamlining custom-based rules and regulations, providing accurate procedural information, and increasing financing options and infrastructure. These objectives will create a more desirable trade environment for MSMEs.

On training and skills development, the APEC Education Strategy 2016 aims to have a cohesive education community that supports sustainable economic growth by 2030 by increasing employability, accelerating innovation and aligning competencies to the needs of the economy. The aim is for APEC economies to be better equipped to provide human resources with the skills needed by labour markets.

APEC’s work on structural reform – the Leaders’ Agenda to Implement Structural Reform, or LAISR (2004); the APEC New Strategy on Structural Reform, or ANSSR (2010); and the Renewed APEC Agenda on Structural Reform, or RAASR (2015) – also addresses the issues related to the distribution of benefits from globalisation. These initiatives focus on making markets more open, improving labour market opportunities through training and education, and initiating programmes to empower vulnerable groups through capacity building and training. More open and competitive markets will help reduce economic distortions, facilitating local trade-related adjustment. Moreover, structural reform in human capital development can contribute to making education and labour markets more efficient, reducing frictions in the movement of workers from one sector to another.

⁴¹ APEC, *1994 Leaders’ Declaration*, Bogor, Indonesia, 15 November 1994, para. 8, http://www.apec.org/Meeting-Papers/Leaders-Declarations/1994/1994_aelm.aspx (accessed 5 May 2017).

⁴² APEC, *The APEC Leaders’ Growth Strategy*, Yokohama, Japan, 14 November 2010, http://www.apec.org/Meeting-Papers/Leaders-Declarations/2010/2010_aelm/growth-strategy (accessed 5 May 2017).

1.6 CONCLUSION

Globalisation is not a panacea for society's inequalities. Globalisation has always been a way to induce efficiency in trading economies through competition and specialisation; it was never meant as a tool to reduce inequality or create a fairer society. But globalisation does affect distribution and, in the absence of equity-inducing policies and institutions, could exacerbate an already inequitable distribution of wealth and opportunities.

At the same time, globalisation also brings with it opportunities to create a more equitable society. The benefits from trade and investment liberalisation could be used to invest in social services and trade-adjustment measures in order to reduce existing gaps and take full advantage of globalisation. The prosperity, information, and people exchange globalisation brings could be used to invest in suitable infrastructure; provide access to education, skills retraining, and health care; as well as give relief for workers and households affected by economic shocks or structural unemployment. It can open up opportunities for enterprise and innovation, as well as open minds to different cultures and ideas.

But the key word is 'opportunity'. Globalisation alone will not lead to a fairer or more equal society. Globalisation alone will not reduce bigotry or hate. It will require the hard work of policymakers and the strength of will of politicians to turn opportunity into reality.

2 GLOBAL ECONOMIC MOMENTUM AND OPTIMISM FUELLING NEAR-TERM GROWTH⁴³

2.1 APEC GDP GROWTH

The world economy was shaped by three major events in 2016: (1) the United Kingdom's withdrawal from the European Union via a referendum in June 2016, more commonly known as Brexit; (2) the United States' elections in November 2016; and (3) the decision

*Major external events
in 2016:*

(1) Brexit

(2) US elections

(3) OPEC output cut.

by the Organization of the Petroleum Exporting Countries (OPEC) to cut production levels in November 2016. These key developments gave rise to policy changes and associated uncertainty, which have affected both the speed and direction of world economic growth, either directly via trade and investments, or indirectly via consumer and business confidence.

The initial impact of Brexit was manageable, but there remains some uncertainty regarding the magnitude of its effects in the medium term given that the formal withdrawal process commenced only on 29 March 2017 and is expected to be completed by April 2019.

The anticipated shift in economic policies with the new US administration, including trade and fiscal policies, could have implications not only for the US economy, but also for the overall output of its trade partners and the pace of global economic activity as a whole.

The OPEC decision in November 2016 to significantly reduce output by about 1.2 million barrels a day starting in January 2017 had an immediate impact. The stock prices of energy companies surged, movements in the currencies of large oil exporters were observed, and benchmark oil prices recorded an increase of as much as 10 percent in New York. More importantly, the OPEC agreement helped nudge the oil market toward a level of rebalancing where the supply of oil aligns with demand, translating to higher prices. Higher oil prices should provide relief to commodity exporters by easing fiscal constraints, thereby allowing economies to spend on infrastructure and social initiatives that will augment households' purchasing power, resulting in increased economic activity.

⁴³ Prepared by Rhea C. Hernando, Researcher, APEC PSU.

A global cyclical recovery is underway, supported by a turnaround in trade and manufacturing.

Parallel to these key external developments is the economic momentum, which started halfway through 2016 as part of the global cyclical recovery from the 2008–2009 global financial crisis. This synchronized global upswing is supported by a turnaround in manufacturing and trade during the second half of 2016.

Global manufacturing, as measured by the J.P. Morgan Global Manufacturing Purchasing Manager's Index (PMI),⁴⁴ started to firm up its increase in July 2016, ending the year with a 34-month-high index score of 52.7 in December 2016, above the long-run average of 51.4. In terms of world trade, the value of aggregate merchandise exports and imports grew by 3.5 percent in August 2016 after being in negative territory during the first seven months of the year, dipping in September–October 2016, and posting stronger gains in November–December 2016 (Figure 2.1).

The manageable initial impact of major developments worldwide amid firmer signs of a global cyclical recovery, together with China's ongoing economic transformation that is supported by fiscal measures, were factors behind APEC's 3.5 percent GDP growth in 2016 (albeit slightly lower than the year-ago level of 3.6 percent).⁴⁵

APEC GDP grew by 3.5 percent in 2016.

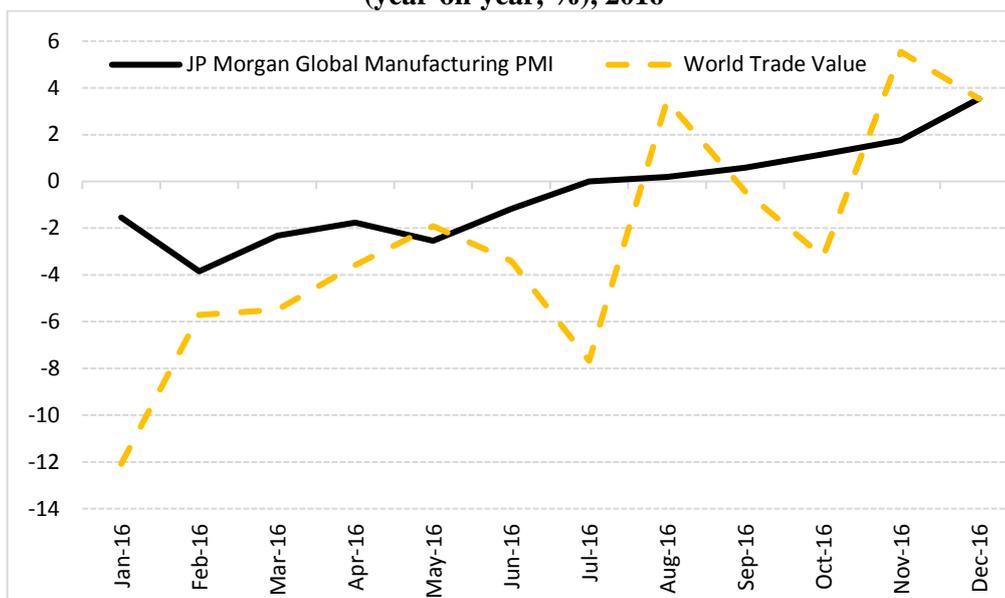
APEC member economies recorded growth in GDP in 2016 ranging from 1.0 to 6.7 percent (Figure 2.2) with two exceptions, namely, Brunei Darussalam and Russia, both of which are commodity exporters that posted contractions in GDP growth in 2016 due to the prolonged downturn in oil prices.

Brunei Darussalam contracted by 2.5 percent in 2016, a further downward adjustment from the 2015 contraction of 0.4 percent even as Russia's economy turned for the better with a smaller contraction of 0.2 percent in 2016 following a 2.8 percent contraction in the previous year.

⁴⁴ The J.P. Morgan Global Manufacturing PMI is produced monthly by J.P. Morgan and IHS Markit in association with the Institute for Supply Management (ISM) and the International Federation of Purchasing and Supply Management (IFPSM). This global indicator is derived from data produced using internationally comparable methodologies covering around 10,000 survey respondents in over 20 economies, which collectively represent 76 percent of global economic output.

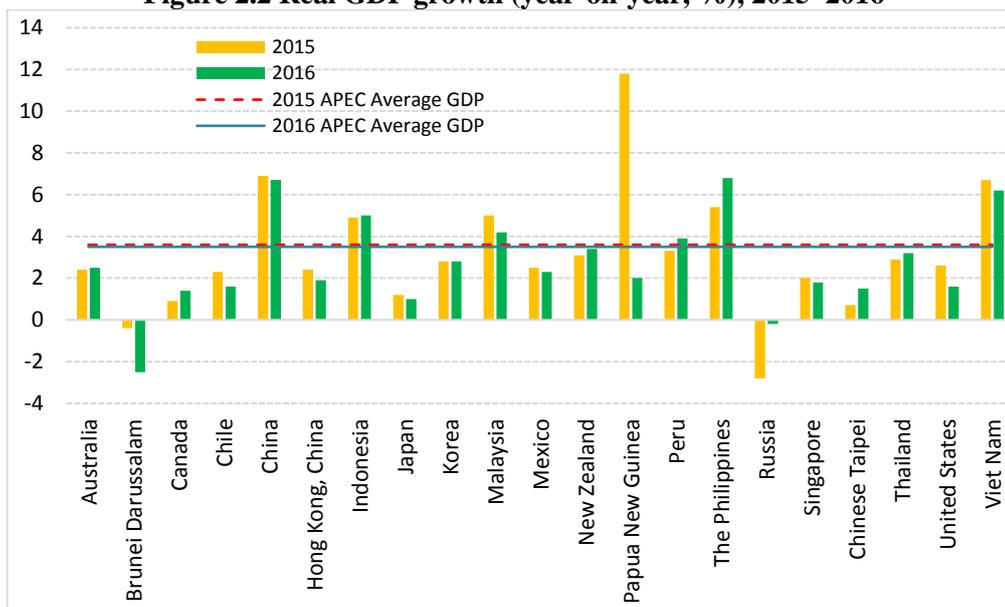
⁴⁵ The GDP growth rate for the APEC region is a weighted average of the growth rates of all 21 member economies.

Figure 2.1 Global manufacturing PMI and world trade values (year-on-year, %), 2016

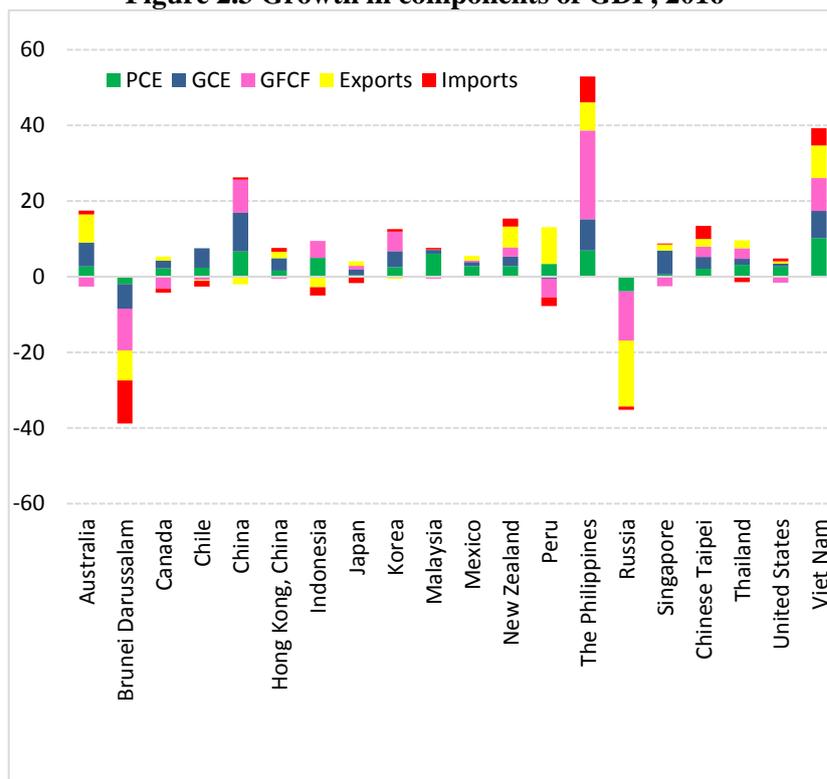


Source: J.P. Morgan Global Manufacturing PMI; WTO for the world trade values.

Figure 2.2 Real GDP growth (year-on-year, %), 2015–2016



Source: ADB; International Financial Statistics (IFS); World Bank; The Economist economic and financial indicators; various economy sources; APEC PSU calculations.

Figure 2.3 Growth in components of GDP, 2016

Notes: PCE = private consumption expenditure; GCE = government consumption expenditure; GFCF = gross fixed capital formation. Data not available for Papua New Guinea. Missing bars denote either nil growth or unavailable data.

Source: ADB; various economy sources; APEC PSU calculations.

The sustained strength in domestic private and government consumption remained the main fuel for APEC's growth amid persistent uncertainty associated with policy shifts and economic transitions occurring worldwide (Figure 2.3). Domestic consumption was

Private and government consumption remained the main fuel for APEC's growth.

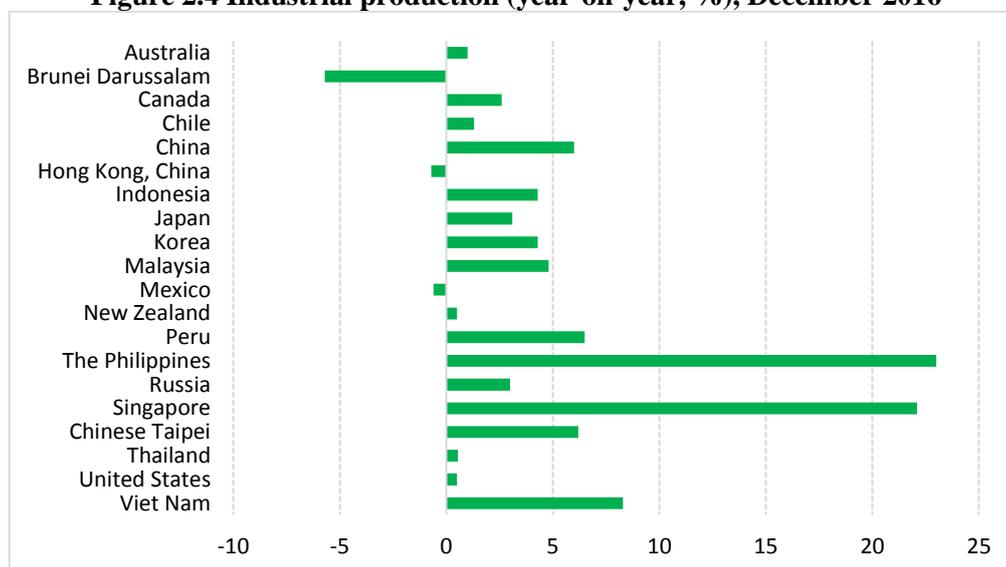
boosted by still-low interest rates and commodity prices as well as government action to pump-prime the economy via fiscal stimulus measures and infrastructure-related expenditures. The generally accommodative environment encouraged continued spending, mitigating the adverse effect of uncertainty on consumer and business confidence.

Growth in gross fixed capital formation was mixed across the APEC region, with more emerging market economies in APEC notably opting to invest in durable equipment and construction compared to other member economies.

In real terms, the contribution of exports to APEC GDP growth was generally stronger in 2016. More economies registered growth in exports, while other members saw smaller contractions.

Meanwhile, APEC's industrial production, a measure of the output of the industrial sector that includes manufacturing, mining and utilities, lent support to observations of a global cyclical recovery as it was generally positive for the APEC region as of December 2016 (Figure 2.4).

Figure 2.4 Industrial production (year-on-year, %), December 2016



Note: Data not available for Papua New Guinea.

Source: The Economist economic and financial indicators.

2.2 TRADE PERFORMANCE

Trade performance in the APEC region, although still contracting, has improved in 2016, with the aggregate value of APEC's merchandise exports experiencing a smaller contraction of 4.1 percent from a contraction of 8.7 percent in 2015; with the same trend observed for imports (Table 2.1). This follows world trade, which also performed better in 2016 compared to a year ago.

Growth in the value of merchandise trade in the APEC region improved in 2016, in line with world trade.

In terms of APEC's share of world trade, the region experienced a slight decrease from 54.7 percent in 2015 to 53.9 percent in 2016.

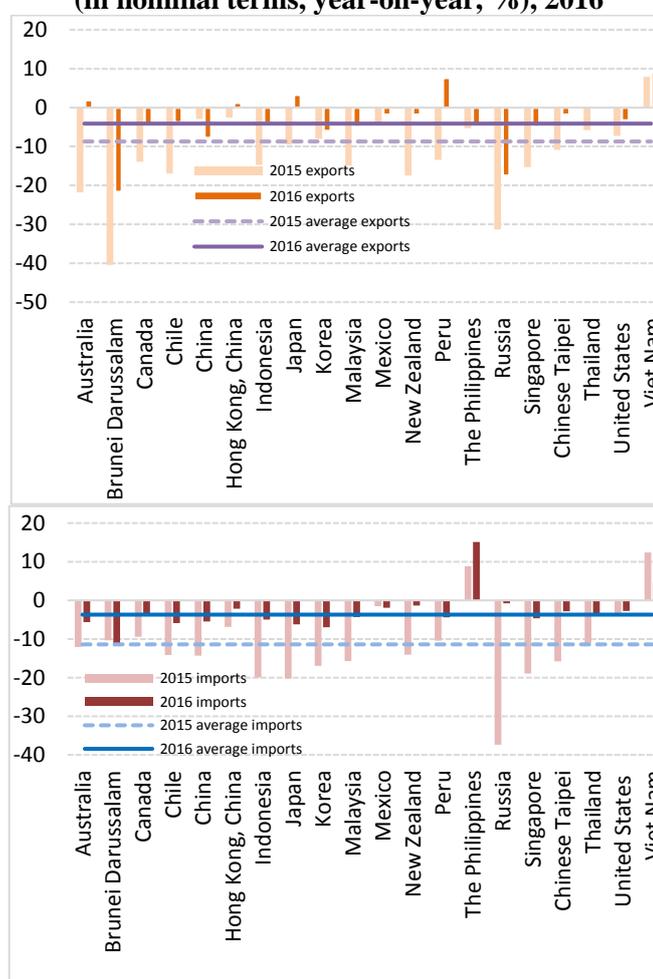
Individually, APEC member economies exhibited lower contraction rates for both export and import values compared to the levels posted in 2015 (Figure 2.5).

Table 2.1 Value and growth in merchandise trade (in nominal terms), 2015–2016

| Merchandise Trade | | | | | |
|--|--------------|--------------|--------------|-------------|------|
| Value in million USD; Growth rate (y-o-y) and share in percent | | | | | |
| | Value | | | Growth rate | |
| | 2014 | 2015 | 2016 | 2015 | 2016 |
| APEC | | | | | |
| Exports | 9,105,213.0 | 8,311,448.6 | 7,974,488.9 | -8.7 | -4.1 |
| Imports | 9,361,369.6 | 8,293,332.1 | 7,987,199.1 | -11.4 | -3.7 |
| Total Trade | 18,466,582.7 | 16,604,780.7 | 15,961,688.0 | -10.1 | -3.9 |
| World | | | | | |
| Exports | 17,083,000.0 | 15,202,000.0 | 14,806,000.0 | -11.0 | -2.6 |
| Imports | 17,560,000.0 | 15,353,000.0 | 14,947,000.0 | -12.6 | -2.6 |
| Total Trade | 34,643,000.0 | 30,555,000.0 | 29,753,000.0 | -11.8 | -2.6 |
| APEC's share of the world | | | | | |
| Exports | 53.3 | 54.7 | 53.9 | | |
| Imports | 53.3 | 54.0 | 53.4 | | |
| Total Trade | 53.3 | 54.3 | 53.6 | | |

Note: Data not available for Papua New Guinea.

Source: WTO; Brunei Darussalam Economic Planning and Development Office; APEC PSU calculations.

Figure 2.5 Growth in the value of merchandise exports and imports (in nominal terms, year-on-year, %), 2016

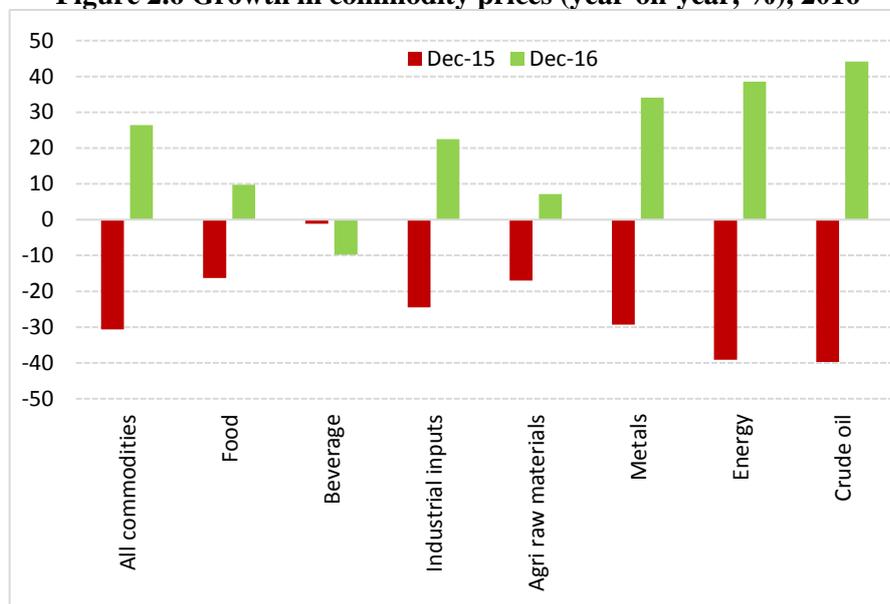
Note: Data not available for Papua New Guinea.

Source: WTO; Brunei Darussalam Economic Planning and Development Office; APEC PSU calculations.

The improvement in APEC trade could be traced to stronger global demand, higher commodity prices, and other trade-related factors.

The enhanced trade in 2016 could be attributed to a confluence of factors. First, stronger global demand in light of the cyclical recovery supported trade. Second, higher commodity prices encouraged production and trade activity while also boosting investments and strengthening the case for higher future demand and inventories. In particular, prices for both oil and non-oil commodity products had gone up in December 2016 compared to the year-ago level. The All Commodities index grew by 26.4 percent in December 2016 from -30.7 percent in December 2015, while crude oil prices jumped by 44.2 percent from -39.8 percent during the same comparable period (Figure 2.6). Third, idiosyncratic factors relating to individual economies' pursuit of more diversified markets, products and partners as well as trade agreements have also contributed to improved trade in the APEC region.

Figure 2.6 Growth in commodity prices (year-on-year, %), 2016



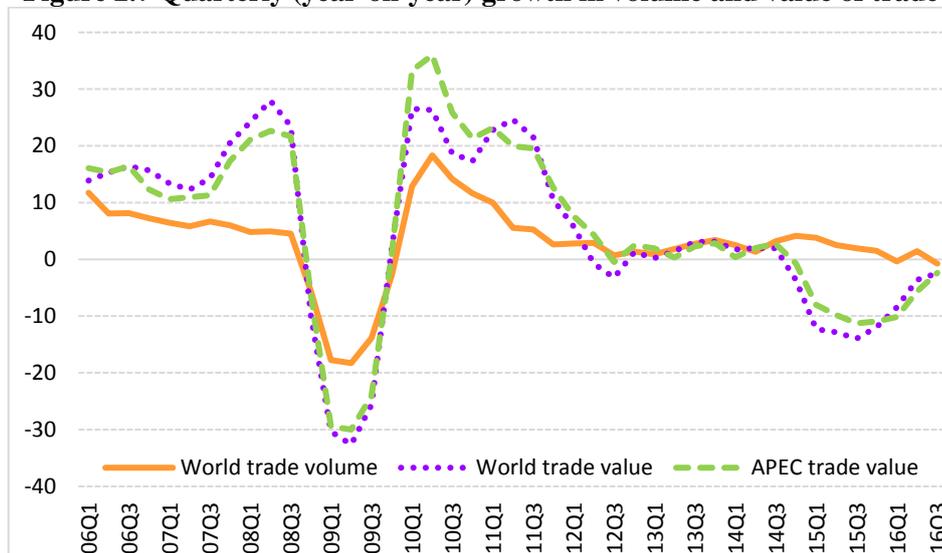
Source: IMF Primary Commodities.

Trade activity in APEC largely mirrored movements in world trade.

Trade activity in the APEC region largely mirrored movements in world trade. Available quarterly data covering the period 2005–2016 show that the trade values of the world and the APEC region generally moved together, marked by the following highlights: reached double-digit levels in the pre-2008 global financial crisis; plunged into negative territory during the 2008–2009 crisis period; recovered strongly in 2010–2011 as monetary authorities worldwide launched coordinated quantitative easing measures to ease credit conditions; weakened significantly in 2012–2014 due to the lingering impact of the crisis; and contracted since the fourth quarter of 2014 up to the third quarter of 2016, with noticeable improvements.

Meanwhile, the volume of world trade has shown consecutive growth since the first quarter of 2010, although a slight dip toward negative territory was seen in the first and third quarters of 2016 (Figure 2.7).

Figure 2.7 Quarterly (year-on-year) growth in volume and value of trade



Source: WTO short-term trade statistics.

2.3 INVESTMENT TRENDS

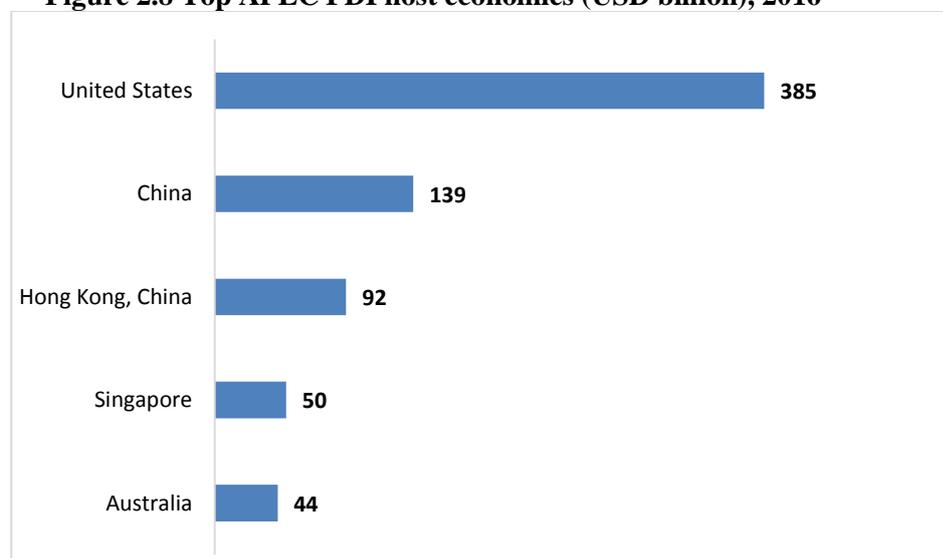
Preliminary data from the United Nations Conference on Trade and Development (UNCTAD) show that global FDI flows declined by 13 percent to USD 1.52 trillion in 2016 from USD 1.75 trillion in 2015, owing to weak global economic growth and the marginal year-on-year increase in world trade volume for the whole year of 2016.⁴⁶

Nonetheless, this decline does not tell the whole story. There exist variations in FDI movements across the globe. For example, while the estimated FDI flows to developed economies dropped by 9 percent to USD 872 billion, led by Europe which fell by 29 percent, a significant increase was noted in other developed economies, particularly Australia and Japan. Also, FDI inflows to developing economies were lower by 20 percent, while transition economies attracted 38 percent more FDI in 2016 at USD 52 billion compared to a year ago.

The top five APEC FDI hosts accounted for 46.7 percent of global FDI flows in 2016.

APEC member economies constituted half of the top 10 FDI recipient economies in 2016. The United States took the largest share of FDI at USD 385 billion with 11 percent growth, maintaining its position as the top FDI host economy. The other APEC economies in the top 10 in 2016 were: China (USD 139 billion); Hong Kong, China (USD 92 billion); Singapore (USD 50 billion); and Australia (USD 44 billion). Taken together, FDI inflows to these APEC host economies reached USD 710 billion, equivalent to 46.7 percent of global FDI flows in 2016 (Figure 2.8).

Figure 2.8 Top APEC FDI host economies (USD billion), 2016



Source: UNCTAD.

The other upward movers in the APEC region in 2016 relative to 2015 FDI levels were: Korea, which posted FDI inflows at USD 9.4 billion from USD 4.0 billion; Russia, which recorded a 62 percent rise in FDI inflows to USD 19 billion from USD 12 billion; Japan,

⁴⁶ UNCTAD, *Global Investment Trends Monitor* no. 25 (1 February 2017).

with inflows of USD16 billion from a net divestment of USD 2 billion; and Australia, whose FDI inflows more than doubled to USD 44 billion.

However, other APEC economies experienced reductions in FDI inflow in 2016 relative to a year ago, including Canada, with inflows settling at USD 29 billion from USD 43 billion; Chile, with inflows down by 31 percent to USD 11 billion in 2016 from USD 16 billion; and Mexico, with a 21 percent reduction in FDI inflows to USD 26 billion from USD 33 billion. Moreover, inflows to Hong Kong, China and Singapore also fell in absolute terms, although they belong to the top 10 FDI recipients in 2016.

2.4 TRADE AND INVESTMENT MEASURES

The period mid-May to mid-October 2016 saw APEC economies implementing a total of 60 trade and trade-related measures (see Table 2.2 for a summary and Annex 1 for the specific measures⁴⁷). Trade-facilitating measures, at 31, outnumbered trade-restrictive measures at 29.

The same period saw a total of seven investment measures implemented by APEC economies, with five measures having the effect of facilitating investments while the other two had the effect of restricting the entry of investments (see Table 2.3 for a summary and Annex 2 for specific measures⁴⁸).

Implementation of trade and investment measures by APEC economies in the period mid-May to mid-October 2016:

- *More trade-facilitating measures than trade-restrictive measures*
- *More investment-friendly measures than measures that discourage investments.*

⁴⁷ Annex 1 can be downloaded at:

http://www.apec.org/~media/Files/AboutUs/PolicySupportUnit/2017/Annex%201_Trade%20and%20Trade-Related%20Measures_May%202016%20to%20October%202016.docx

⁴⁸ Annex 2 can be downloaded at:

http://www.apec.org/~media/Files/AboutUs/PolicySupportUnit/2017/Annex%202_Investment%20Measures_May%202016%20to%20October%202016.docx

Table 2.2 Trade and trade-related measures, mid-May 2016 to mid-October 2016

| | Number of Measures |
|--|--------------------|
| <i>Trade-restrictive measures</i> | |
| Initiation of anti-dumping investigation | 17 |
| Initiation of countervailing investigation | 7 |
| Initiation of safeguard investigation | 1 |
| Increase/Imposition of import tariffs and export duties | 0 |
| Imposition of export/import requirements/quotas/restrictions | 4 |
| Imposition/Extension of import/export ban | 0 |
| Sub-total: Trade-restrictive measures | 29 |
| <i>Trade-facilitating measures</i> | |
| Termination of anti-dumping investigation/duties | 16 |
| Termination of countervailing investigation/duties | 6 |
| Termination of safeguard investigation | 0 |
| Reduction/elimination of exportduties/import tariffs | 8 |
| Elimination of import/export ban and other restrictions | 1 |
| Sub-total: Trade-facilitating measures | 31 |
| Total: Trade and trade-related measures | 60 |

Source: UNCTAD, OECD and WTO, *Reports on G20 Trade and Investment Measures (mid-May to mid-October 2016)*, 10 November 2016.

Table 2.3 Investment measures, mid-May 2016 to mid-October 2016

| | Number of measures |
|--|--------------------|
| <i>Facilitating the entry of foreign investment</i> | |
| Increasing transparency in the investment environment | 1 |
| Clarifying and simplifying rules and processes | 2 |
| Relaxing rules on foreign exchange quota | 2 |
| <i>Restricting the entry of foreign investment</i> | |
| Imposing additional requirements and/or fees | 2 |
| Total: Investment measures | 7 |

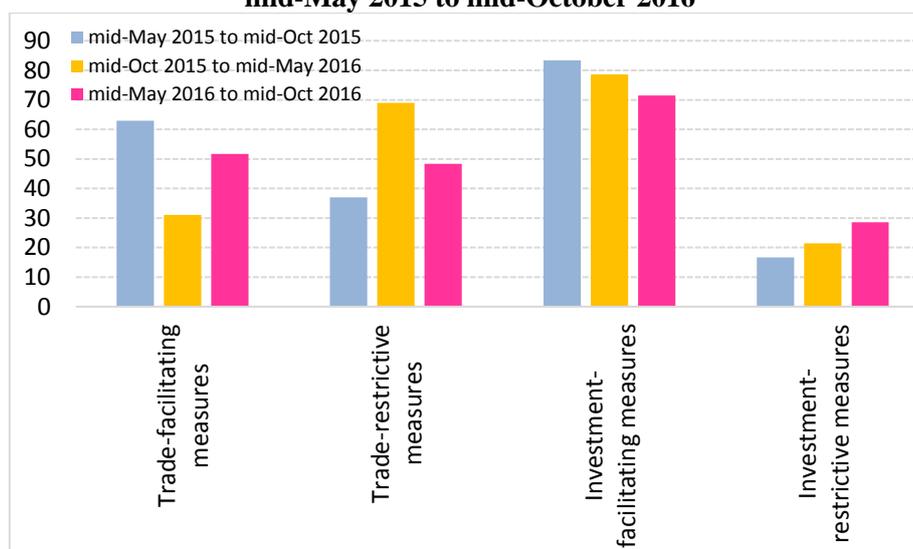
Source: UNCTAD, OECD and WTO, *Reports on G20 Trade and Investment Measures (mid-May to mid-October 2016)*, 10 November 2016.

As a percentage of the total, trade-facilitating measures outweighed trade-restrictive measures for the reporting period mid-May to mid-October 2016. This development was a turnaround from the mid-October 2015 to mid-May 2016 period wherein the trade measures implemented by APEC economies leaned toward trade-restrictive measures at 69 percent of the total compared to 31 percent of trade-facilitating measures (Figure 2.9).⁴⁹

Meanwhile, APEC economies have been consistent in implementing more investment-friendly measures compared to investment-restrictive measures across reporting periods. However, although measures that facilitate investments remained significant, they have been declining as a percentage of total measures implemented. In contrast, investment-restrictive measures are on an uptrend, from 16.7 percent of the total in mid-May to mid-October 2015 to 21.4 percent in mid-October 2015 to mid-May 2016, and 28.6 percent as of the latest reporting period covering mid-May to mid-October 2016 (Figure 2.9).

Although investment-friendly measures remained significant, investment-restrictive measures are on an uptrend.

**Figure 2.9 Trade and investment measures in APEC (as % of total)
mid-May 2015 to mid-October 2016**



Source: UNCTAD, OECD and WTO, *Reports on G20 Trade and Investment Measures (mid-May 2015 to mid-October 2016)*.

⁴⁹ It is instructive to note that only 9 of the 21 APEC member economies belong to the G20, namely: Australia; Canada; China; Indonesia; Japan; Korea; Mexico; Russia; and the United States.

The latest available data from the WTO up to October 2016 covering all WTO members show that APEC member economies who are not G20 members have also implemented trade-facilitating measures, including the elimination of import and export licensing requirements on certain products; the termination of anti-dumping duties on selected imports; and the reduction of import tariffs and port charges. However, the same period also saw other APEC economies implementing trade-restrictive measures such as anti-dumping investigations and safeguard investigations on certain imports.

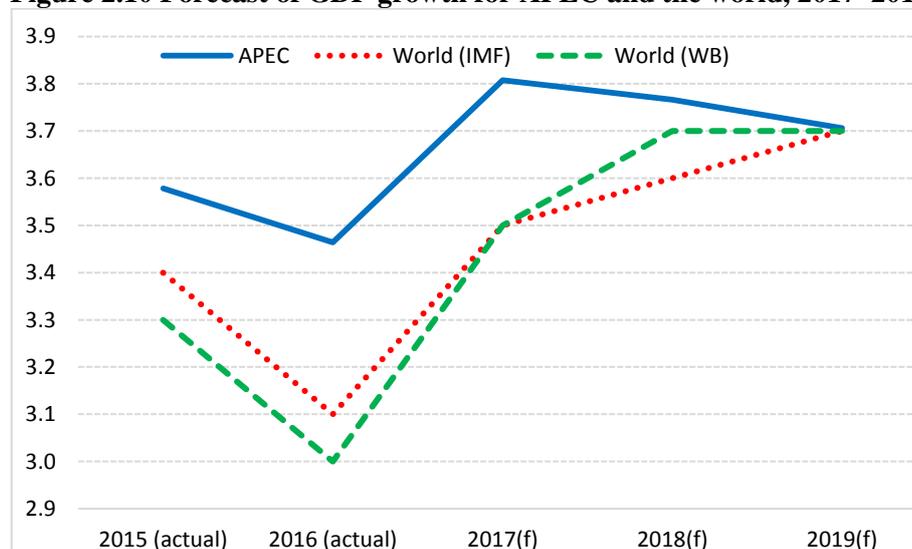
2.5 NEAR-TERM OUTLOOK, RISKS AND OPPORTUNITIES

The APEC region is expected to post a higher GDP growth rate in the near term, generally apace with world economic activity.

Near-term GDP projections point to higher APEC growth for the period 2017–2019, generally apace with world economic activity.

Following a GDP growth rate of 3.5 percent in 2016, which was higher than the estimated world GDP of 3.0–3.1 percent, the APEC region is expected to accelerate to a growth of 3.8 percent for the period 2017–2018, before tapering to 3.7 percent by 2019. The upward trend in APEC’s GDP growth mirrors the expected trajectory of world growth, at 3.5 percent in 2017; 3.6–3.7 percent in 2018; and settling at around 3.7 percent in 2019 (Figure 2.10).

Figure 2.10 Forecast of GDP growth for APEC and the world, 2017–2019



Notes: IMF GDP figures in PPP, constant 2011 international dollar; World Bank GDP figures in constant 2010 PPP weights.

Source: IMF, World Economic Outlook Database, April 2017; World Bank, *Global Economic Prospects, January 2017 – Weak Investment in Uncertain Times* (Washington, DC: World Bank, 2017); APEC PSU calculations.

Trade and investment activity will continue to have an impact on economic growth. In its April 2017 trade outlook, the WTO expects trade to recover via a 2.4 percent growth in world merchandise trade volume in 2017 from a lacklustre increase of 1.3 percent in 2016.⁵⁰ This optimistic projection rests primarily on a near-term global expansion that is expected to create positive effects on global demand and overall trade.

Trade volume and FDI are expected to grow stronger in the near term, in line with the global cyclical recovery.

However, uncertainty looms. The lack of clarity on near-term policy directions encompassing trade, monetary and fiscal policies translates to higher risks. Thus, the forecast range for world trade volume in 2017 is wider at 1.8–3.6 percent. For 2018, the WTO forecasts higher trade growth as world merchandise trade volume is expected to increase to a range of 2.1–4.0 percent.

IMF projections of world trade volume track the WTO forecasts as the IMF also expects a higher growth of 3.8 percent in 2017 and 3.9 percent in 2018.⁵¹ The IMF's forecast is supported by expectations of increased demand and capital spending, bolstered by the observed synchronised upswing of economies across the globe and the gradual recovery in commodity prices.

Trade and trade-related measures, particularly relating to the movement of goods and supply of services across borders, continue to be a key factor in determining the level of trade activity and resulting gains.

Pressures to turn inward and implement policies that lean toward protectionism amid discussions on income inequality and low productivity, combined with anti-globalisation sentiments, could affect the free flow of trade and investments across economies, threatening not only the global recovery in the short term, but also the move toward greater economic integration that has the potential to significantly benefit economies in the medium term.

Clear and consistent trade, monetary and fiscal policies could determine the magnitude and direction of global growth in the short term.

Clear and consistent policy directions could help create an environment conducive to trade activity, which, at the same time, could encourage greater investments. Unclear and conflicting policies, conversely, could hold back trade and investments.

⁵⁰ WTO, 'Trade recovery expected in 2017 and 2018, amid policy uncertainty', press release, *World Trade Organization*, 12 April 2017, https://www.wto.org/english/news_e/pres17_e/pr791_e.htm (accessed 5 May 2017)

⁵¹ IMF, *World Economic Outlook April 2017: Gaining Momentum?* (Washington, DC: IMF, 2017).

Along with prevailing uncertainties, particularly relating to trade policy and its consequence for trade and investment, short-term monetary and fiscal policies could also affect economic growth.

Monetary surprises could generate volatility and affect economies via capital flows and capital costs. A larger-than-expected mark-up in US interest rates could trigger capital flight from economies that are perceived as fundamentally weak, further raising foreign debt burdens and potentially introducing credit constraints. In addition, an increase in US interest rates leads to a stronger US dollar, which could create currency mismatches that could weigh down foreign debt borrowers. Furthermore, higher interest rates translate to higher capital costs, which could deter investment opportunities.

On the other hand, fiscal stimulus measures, especially from the US and China as they support their economies' growth requirements amid economic transitions, could have positive spillover effects for the global economy via increased demand, which, in turn, could boost trade and investments across the globe, realising projections of higher world growth in the near term.

Aside from expectations of fiscal support, another factor that could lead to accelerated global growth is a projected 10 percent increase in FDI in 2017 on the back of a stronger global economic recovery as well as a rosier trade picture in the short term. However, UNCTAD is also mindful about the role that uncertainty plays in a global setting, particularly relating to the magnitude and frequency of changes in US monetary policy rates as well as near-term economic policy directions which could influence the path of investments going forward.⁵²

There is substantial upside potential for increased growth as trade and investment are expected to gather pace in tandem with the global recovery. However, there is also significant uncertainty on near-term trade, monetary and fiscal policies; and this could pause trade and investment activity, weighing down overall economic growth. Therefore, the clarity, transparency and consistency of economic policies could determine the magnitude and direction of economic growth in the near term.

⁵² UNCTAD, *Global Investment Trends Monitor* no. 25.

2.6 CONCLUSION

The cyclical global recovery affords economies a level of optimism not seen since the 2008 global financial crisis. This optimism is supported by improvements in trade growth along with manufacturing observed in the second half of 2016. In the near-term period covering 2017–2019, the economic picture points to higher global growth, marked by more buoyant trade and investment activity. In the APEC region, economic growth is expected to surpass world GDP in 2017–2018, converging in 2019.

It is important to sustain, and benefit from, the global upswing by implementing measures that continue to fuel demand.

It is important to sustain the global upswing and benefit from stronger consumer and business confidence by implementing macroeconomic measures that continue to prop up demand. At the same time, economies need to be mindful that the risks are substantial, and uncertainty, particularly on the direction of economic policies, remains a significant downside risk that could put a brake on the economic momentum if not addressed in an appropriate and timely manner.

Macroeconomic management differs across economies, depending on domestic conditions and vulnerabilities. The aim is to continue to support growth requirements via the demand channel to be able to derive the full benefits from the ongoing global economic momentum.

Economies with enough elbow room to apply fiscal support measures could consider building infrastructure; supporting the labour market with programmes for those displaced by globalisation and technological change; and implementing social safety nets and other initiatives to help the vulnerable and marginalized, including women, the young and the disabled. Economies with fiscal constraints could lean toward easing interest rates as well as streamlining requirements and procedures to boost credit growth, and thereby, encourage consumer and business consumption.

Macroeconomic management needs to be supported by structural reforms that promote innovation, lead to more competitive markets, facilitate participation of all segments of society, and enhance economic resilience, allowing for a significant contribution toward the goal of sustainable and inclusive growth. In concrete terms, these reforms entail reducing the cost of doing business, unlocking productivity gains, increasing labour force participation across gender and skill levels, and ensuring that a wider set of opportunities is available and accessible to all.

Macroeconomic management needs to be supported by structural reforms.

APEC continues to push forward its structural reform agenda. APEC's work on this front began in earnest in 2004 with the Leaders' Agenda to Implement Structural Reform (LAISR). It forged on with the APEC New Strategy for Structural Reform (ANSSR) in 2010; and strengthened the agenda anew through the Renewed APEC Agenda on Structural Reform (RAASR) which has a 5-year implementation period covering 2015–2020. APEC member economies have come up with individual action plans to implement the RAASR

and have agreed on 17 APEC-wide external indicators to monitor their progress.⁵³ A mid-term review is due in 2018, with a final review in 2020.

Parallel to these efforts to respond to structural transformations through reforms, economies could also allocate resources for infrastructure to improve connectivity and help facilitate trade and investment flows. Also, investing in human capital could bridge gaps in skills and education while also addressing vulnerabilities.

The APEC region envisions free and open trade and investment in the Asia-Pacific; by 2010 for industrialised economies, and by 2020 for developing economies.⁵⁴ Commitments and subsequent actions toward achieving the APEC vision by member economies are voluntary as APEC operates on the basis of non-binding commitments, open dialogue, and equal respect for the views of all participants.

In 2015, the APEC region accounted for around 59 percent of the world's nominal GDP and almost half of the world's total trade at 48 percent.⁵⁵ This combination of a non-binding, consensus-based process and significant influence puts APEC in a unique position to move forward policy discussions to respond to prevailing issues that pose challenges to its vision. As such, APEC needs to refocus so that its members collectively work toward the goal of a free flow of trade and investment across the Asia-Pacific region, while, at the

APEC's short- and medium-term actions could help cement the path toward higher, more sustainable and more inclusive growth, both for the region and the world.

same time, being mindful of the impact of its actions on vulnerable groups by instituting social programmes to ensure that the benefits are shared by all members of society. APEC's decisions and actions, both in the short term and the medium term, could help cement the path toward higher, more sustainable, more equitable and more inclusive growth, both for the region and the world.

⁵³ The APEC-wide external indicators are discussed at length in: A. Wirjo, *Exploring Quantitative Indicators for Effective Monitoring of APEC-wide Progress on Structural Reform under RAASR 2016–2020* (APEC PSU, Singapore: APEC Secretariat, 2016).

⁵⁴ These goals for APEC member economies, known as the Bogor Goals, were agreed on by the APEC Economic Leaders in Bogor, Indonesia in 1994.

⁵⁵ APEC PSU, *APEC in Charts 2016* (Singapore: APEC Secretariat, 2016).