Asian economies risk being trapped as middle-income countries, held back from sustainable and equitable growth, unless policy action is taken to galvanise green finance, speed up digitalisation and deliver more comprehensive regional policy coordination.

As in the rest of the world, policies in Asia have so far failed to provide the levels of real investment spending capable of securing a sustainable recovery from the COVID-19 pandemic. Low interest rates and injections of liquidity have created financial wealth and spurred consumption—but they have only had a limited impact on real investment.

Investment, as well as cross-border trade, may well decelerate further in 2022 as the global economy stages an uneven recovery at best. The World Trade Organization (WTO) sees Asian exports growing at just 2.3 per cent this year, below pre-pandemic levels.

Many central banks, meanwhile, are not able to respond to the 2022 recovery challenge, having largely exhausted their monetary policy options by reducing interest rates significantly.

Indeed, against a backdrop of gradually rising consumer price inflation, the next moves in monetary policy in developed economies may well be tightening—the Bank of England has already moved that way—which could lead to significant declines in asset prices.

A shift is needed towards policies that specifically address both the immediate economic scarring of the pandemic and secure longer-term resilience and prosperity.

For the 21st century to become the Asian Century, with Asia’s economies set to take a share of over half of global GDP by 2050, only a determined effort by the authorities to fill an evident policy gap will enable growth to continue at the required levels. Adopting a trio of priorities now will enable a robust economic tomorrow: green finance, digitalisation and enhanced regional cooperation.

For green finance, unprecedented levels of coordinated public and private investment are required to meet the Paris Climate Agreement commitments supporting the transition to a low-carbon world.

In Asia, however, access to and the distribution of green finance remains profoundly uneven; this is a partial reflection of the variable depth and breadth of the region’s financial markets, as well as an inability to mitigate and underwrite the risks attached to inward investment.

Only by addressing these obstacles to green finance will policymakers be able to create ecosystems within which green investment can flourish and be mainstreamed. Supporting green finance allows steps to be taken towards combatting climate change, while at the same time avoiding investments that raise the risk of cascading environmental crises.

Prioritising wider digitalisation will boost economic resilience and productivity in a region that is already a leader in digital innovation. Asia can build further on digital success stories that are supporting its drive to tackle climate change and where digitalisation is increasingly being applied in agricultural, financial and energy markets.
KEY MESSAGES:

Asian economies need green finance, broader digitalisation and greater regional coordination to avoid being caught in a middle-income trap that holds them back from greater development.

Achieving this triple-policy objective will promote sustainable, productivity-driven and equitable growth, delivering the trade and investment needed to secure long-term recovery.

The newly launched Asia House economic readiness indices suggest that China leads in both green finance and digital transformation. Within Southeast Asia, Vietnam leads in green finance while Malaysia leads in digital responsiveness.

Unprecedented investment is required for energy transition: fast-tracking green finance will redirect investments away from cascading environmental crises.

Prioritising wider and more diversified digitalisation in Asia will boost climate resilience and productivity in a region that already leads in digital innovation.

Despite their varying size and stage of development, Asian economies must cooperate more comprehensively on policies that will help to achieve shared objectives.

KEY POLICY RECOMMENDATIONS:

Asian economic policymakers should elevate the use of institutionally mobilised finance, including blended finance, to de-risk and catalyse investment flows.

Private and public sector coordination to promote and incentivise green finance must be prioritised to combat the climate crisis.

Asia’s central banks should include sustainability objectives in their monetary policy mandates and explicitly incorporate climate risks into their assessments.

The promotion of Industry 4.0 – the integration of automation, artificial intelligence (AI), cloud computing etc. in manufacturing – coupled with digital reskilling and knowledge diffusion is needed to secure the Asian Century and avoid the middle-income trap.

Currency reserves should be pooled and their management coordinated, while the foundation for a common digital currency in Asia needs to be laid.
COUNTRY OUTLOOKS: KEY MESSAGES

China is likely to see economic growth decelerate. Its consumer sector will recover, and underpin e-commerce, but trade and investment growth could slow.

Japan is likely to experience a moderate acceleration in growth, spurred by the policies of the new administration and Japan’s broad financial ecosystem. But authorities must speed up digitalisation efforts.

India is expected to be the world’s fastest-growing economy in 2022, with GDP up some 8.5 per cent. But building economic resilience and closing its digital divide will be essential for its sustainability.

Indonesia’s 2022 growth is likely to be one of the strongest in ASEAN. Trade growth could see a turnaround if Indonesia’s connectivity gap is addressed. Its inward foreign direct investment (FDI) and portfolio investment suggest momentum ahead.

HOW READY ARE ASIA’S ECONOMIES FOR A GREEN AND DIGITAL FUTURE?

Asia House unveils new Economic Readiness indices

Asia finds itself at an important crossroads with its constituent economies poised to transition to higher levels of income, innovation, and resilience. To gauge progress in the region’s core economies — the notable greenhouse gas emitters and those most vulnerable to the climate crisis — the Asia House Annual Outlook introduces new economic readiness indices for green finance and digitalisation in eight countries.¹

The indices measure progress in macroeconomic readiness to foster green finance and digitalisation, scoring each country out of 100. China is projected to continue to lead in both its promotion of green finance and digitalisation in 2022, with both of its scores of 72 in the top quartile. Japan follows close behind. Thailand and the Philippines, however, bring up the rear (Figures 1 to 3).

The detailed components and construction of the indices can be found in Appendix 1.

¹The eight countries are China, Japan, India, Indonesia, Vietnam, Malaysia, Thailand and the Philippines.
FIGURE 1. ASIA HOUSE ECONOMIC READINESS INDEX SCORES FOR GREEN FINANCE

<table>
<thead>
<tr>
<th></th>
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<th>Japan</th>
<th>India</th>
<th>Indonesia</th>
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<td>73</td>
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FIGURE 2. ASIA HOUSE ECONOMIC READINESS INDEX SCORES FOR DIGITALISATION

<table>
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FIGURE 3. ASIA HOUSE ECONOMIC READINESS SCORES FOR ASIA-8

Source: Asia House Research

Note: Asia 8 denotes China, Japan, India, Indonesia, Vietnam, Malaysia, Thailand and the Philippines.