Room at the Top: An Overview of Fiscal Space, Fiscal Policy and Inclusive Growth in Developing Asia

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1. Introduction and Some Analytical Considerations

Fiscal policy, Fiscal space and Inclusive growth: some reflections

The sustainability of policies to create fiscal space is a function of what the fiscal space is used for. The balance of emphasis placed on the stabilization, allocation and distribution and growth functions of fiscal policy would differ according to (Roy, Heuty and Letouze 2009):

- the timeframe of the analytical framework
- political economy context
-

Finding sustainable fiscal space for inclusive growth therefore involves asking what the purpose of public spending is, the timeframe for its implementation, and the political economy context within which it is implemented.

An important question to consider, therefore, in assessing, whether, fiscal space exists for inclusive growth is to examine the extent to which a country's fiscal policies are generally prudent and whether or not there is room to increase fiscal space through expansionary fiscal policies. In this context, it is worth repeating that one of the requirements for inclusive growth is that there must be steady and stable growth. Inclusion, as an objective of fiscal policy is expected to complement, not compromise, the growth potential of an economy. Hence, it is important to examine whether or not there exists fiscal space for inclusive growth in terms of a country's inter-temporal fiscal profile. This involves looking at the potential for securing incremental fiscal space to run such expansionary fiscal policies that may be necessary to improve on inclusion; it also means that the size of the government(G)/GDP ratio, whether tax or debt financed should not increase to an extent and at a pace where it crowds out growth-generating private sector activity.

When inclusive growth is the objective of national development strategies the focus is on securing economic growth through investing in the social and human resources that enable such growth to be resilient. This is a sharp break from the growth mantras of the 1980s and 1990s which focused either on growth driven by an increase in exports based on static comparative advantage or on import substituting industrialization that, for lack of physical and social infrastructure and human capital, faltered in its execution.

This important change in thinking about development strategy is epitomized in the centrality of policy interventions to scale up those investments that secure the achievement of the Millennium Development Goals (MDGs). Considerable progress has been made in many developing countries in designing and implementing supply-side interventions to secure the MDGs. More recently, attention is being paid to ensuring that exposure to economic shocks and to asymmetries in access to the public goods necessary to secure the MDGs do not retard or even derail progress towards those goals (IMF 2011). It is here that specific fiscal measures assume an important role in the overall context of fiscal policy making.

From a fiscal perspective there are two important issues pertinent to this strategic shift (Roy, Heuty and Letouze 2009). Many of the objects of public spending for inclusive growth, including health, education and social welfare, are financed out of current expenditure. Macroeconomic prudence requires a zero current deficit except in times of temporary cyclical stress. However, increases in expenditures on social services are a) largely current expenditures, b) *permanent* in the short to medium term (although, with increased incomes and improved employment performance, they decline as a proportion of total expenditure in the long term). For these reasons, finance ministries worldwide have been skeptical of arguments to enhance outlays on social spending.

The second issue is whether inclusion is expected to happen *ex poste* or *ex ante*. The Second Theorem of Welfare Economics (Hicks 1939, Kaldor 1939) stipulates that the prior and prime objective must be to attain the maximum sustainable rate of steady state growth, irrespective of the extent to which the compensation to different factors of production in the process of traversing to that steady state is consistent with the desired distribution expressed in a given social welfare function. Having achieved steady state growth, a suitable income distribution can then be attained without efficiency losses through distortion neutral lump sum taxes and transfers. In effect, here, the role of fiscal policy is principally distributive, and it is redistributive transfers that secure such an optimal steady state.

An alternative policy stance is to ensure that the process of growth itself is one that maintains or improves inclusion by securing greater participation in the growth process. Essentially this is a question of choice of techniques and relative prices (Roy 2011). The role of fiscal policy here is not to actively intervene to secure a better income distribution but to provide a prudential environment that (1) allows fiscal space to exist for securing increases in economic growth including public investments in economic services that complement private investments without crowding them out (2) provides fiscal space for countercyclical fiscal policies to protect against exogenous shocks (3) delivers merit public goods, significantly health and education, that increase human capabilities and permanently enhance participation in the growth process.

Thus, the headline questions in this overview paper are:

i. **Have countries in Developing Asia chosen to pursue inclusive growth through maximizing progress to a steady state growth path, with Kaldor-Hicks type redistributive income transfers being the main instrument to secure desired *ex-post* inclusion outcomes OR**
ii. **Have countries in Developing Asia tended to use fiscal policy to maintain a prudential environment for economic growth, secure countercyclical stabilization of the growth process and deliver merit and public goods to increase human capabilities and permanently enhance participation in the growth process?**

2. Country Groupings

The analysis of economic trends in Developing Asia is typically undertaken on a sub-regional scale. When assessing fiscal impact, this tends not to be very informative; this is because the structural and other features of the fiscal base of different countries in a sub region can vary immensely. The principal reason for this is differences in the income and consumption base; however, changes in economic structure at different points of the development transformation also matter.

When working with sub regional classifications for this paper, it was difficult to come up with interesting fiscal trends between and across sub regions at a macro level. Different country groupings were therefore experimented with; clustering countries with similar income, consumption patterns together, but also allowing for economic size, special characteristics and geo-political situations. The classification[1] which proved to be the most pertinent across different analytical buckets was

(1) **High income countries** (HIC): HongKong -PRC, Brunei, Singapore, Korea and Malaysia.
These countries continue to be classified as part of Developing Asia and – with the exception of small and resource rich Brunei Darussalam – exhibit trends typical of high income countries globally in terms of their fiscal incidence.

(2) **Middle income countries** MIC (I): Kazakhstan, Maldives, Uzbekistan, Azerbaijan and Turkmenistan. These countries are more or less sub regionally coherent with the exception of the Maldives in their fiscal patterns.

(3) **Middle income countries** MIC (II): Vietnam, Sri Lanka, Philippines, Thailand and Pakistan.
These countries, a mix of countries from South and South East Asia also display distinct middle income country patterns.

(4) **Small countries with special characteristics** (SSC): Armenia, Georgia, Bhutan, Mongolia and Papua New Guinea.

(5) **Least Developed Countries (LDCs) and Low Income Countries (LICs):** Lao PDR, Timor-Leste, Cambodia, Kyrgyz Republic, Bangladesh, Nepal, Tajikistan and Afghanistan.

(6) **Asian mega-emerging economies** (EMEs): China, India and Indonesia.

3. Overview of Fiscal Trends in Developing Asia

On the basis of our revised grouping for comparison and an examination of trends in different fiscal indicators, growth, and savings-investment balance, we are able to draw a number of interesting inferences. The charts for each subsection are presented within each subsection as appropriate.

Section 3.1.Fiscal stance: revenue and expenditure trends
Revenue trends in Developing Asia: How varied or common is the fiscal stance?

Within our country groupings we found that revenue trends -- and the consequent fiscal stance tended to be extremely similar within most groups though with some important outliers. However, there was considerable variation across groups. The emergent patterns were

[1] Data available on request

(1) HICs with the exception of Brunei have an increased convergence in revenue stance since about 2005. (Fig.1)

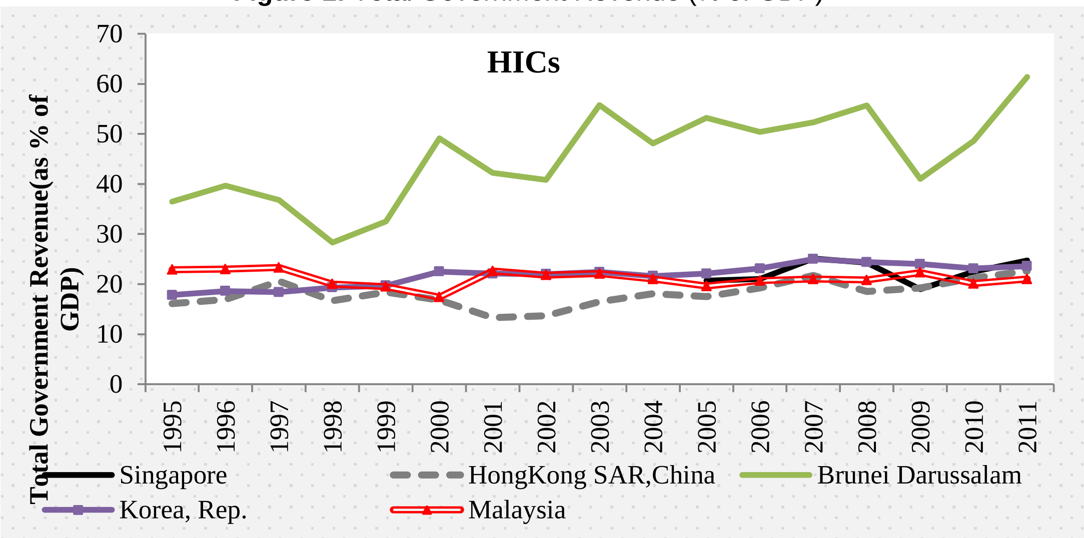
(2) This is also true of MICs (I) and (II) (with the exception of Vietnam) though MICs (I) displays somewhat higher volatility. (Fig. 2 and 3)

(3) There is also some convergence in the LIC group (Fig.5) with trend revenues in all countries increasing over time, though the revenue effort for the Kyrgyz Republic, Tajikistan and more recently, Timor-Leste, is of a much higher order than that of the other LICs, as is to be expected due to the high reliance of these countries on natural resource receipts. Revenue GDP ratios have been rising in LICs since 2006 and, in some cases like Afghanistan Nepal and Lao PDR, this rise is quite dramatic.

(4) The EMEs, as is to be expected, show no such congruence, though trends for each taken individually are stable. China records a secular rise in its revenue GDP ratio. India performs badly on this score with temporary improvements in good years being reversed in bad years.(Fig.6)

On the whole Developing Asia has a ***conservative*** revenue stance No HIC or MIC collects tax revenues in excess of 22 per cent of GDP[2] except Brunei Darussalam and Uzbekistan. Total revenue ratios in excess of that number are only observed in the MIC (I) group chiefly due to high non-tax revenue receipts. These, in turn, tend to be volatile. Vietnam is a possible exception though there, too, revenue GDP ratios appear to have peaked at around 25 per cent since 2004. On an average, compared to for high income and middle income countries in other regions, this is indeed a fairly conservative effort. This is particularly true for the emerging economies where only China exhibits a secular increase in its revenue GDP ratio**.**

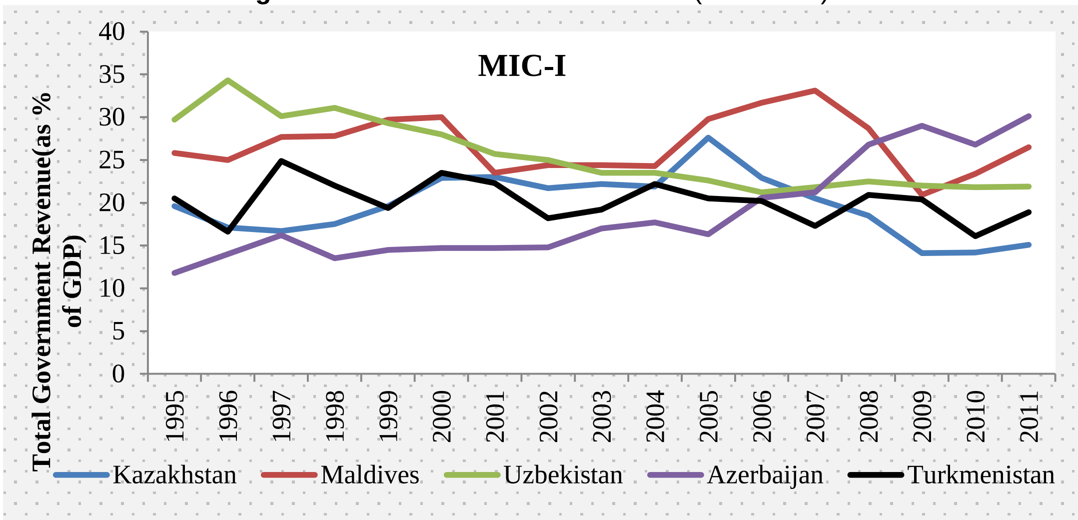
Figure 1: Total Government Revenue (% of GDP)



Source: ADB Database, Country Profiles

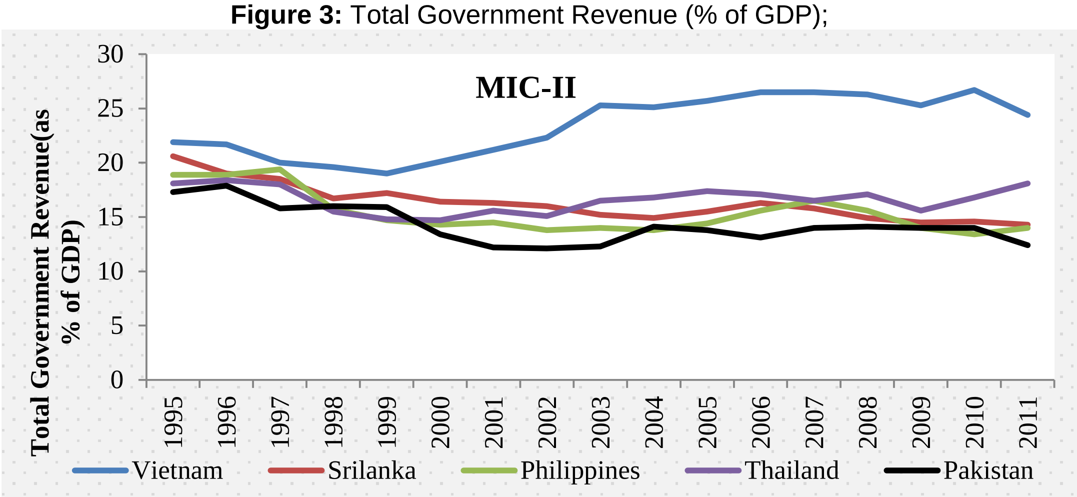
[2] Data available on request

Figure 2: Total Government Revenue (% of GDP)



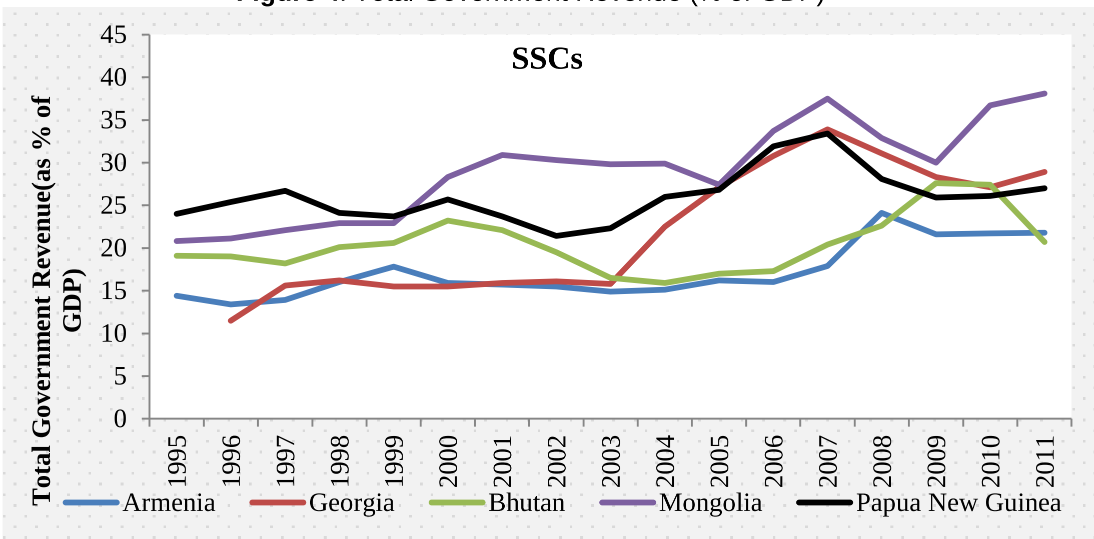
Source: ADB Database, Country Profiles

Figure 3: Total Government Revenue (% of GDP);



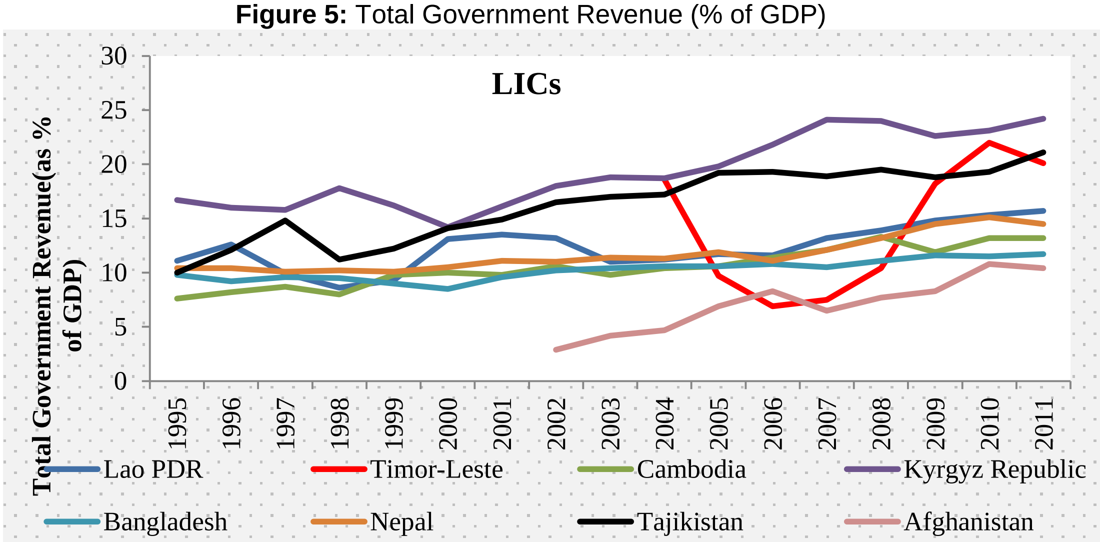
Source: ADB Database, Country Profiles

Figure 4: Total Government Revenue (% of GDP)



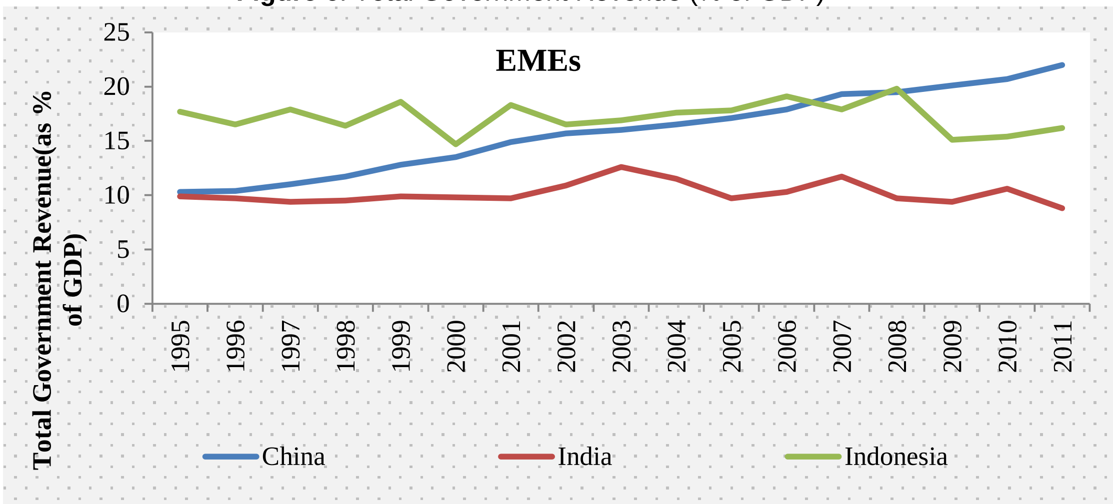
Source: ADB Database, Country Profiles

Figure 5: Total Government Revenue (% of GDP)



Source: ADB Database, Country Profiles

Figure 6: Total Government Revenue (% of GDP)



Source: ADB Database, Country Profiles

Public Expenditure: How varied or common is the fiscal stance?

Total expenditure trends in different groups also display fair convergence. In the case of HICs, again with the exception of Brunei, both Korea and Malaysia spend a stable (around 20 per cent) amount of GDP on public expenditure (Fig.7).

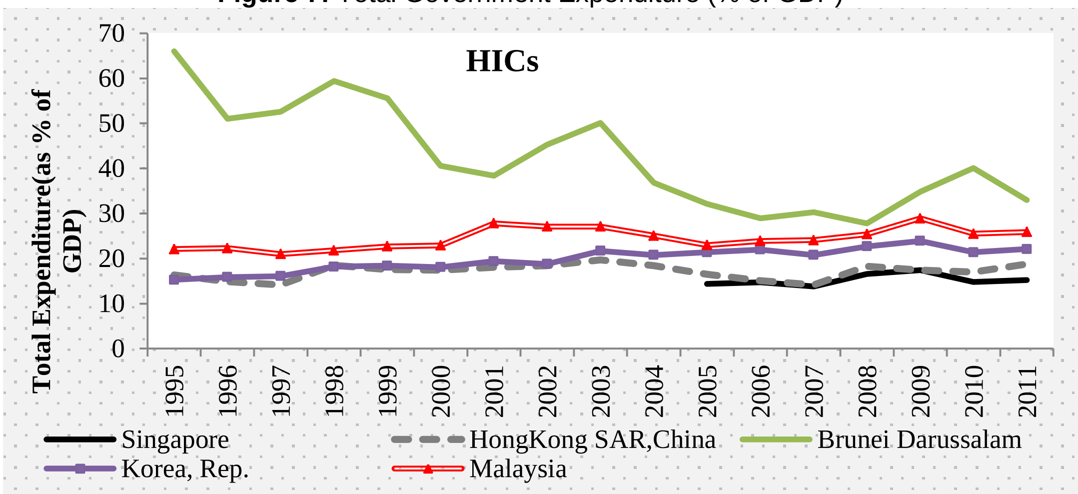
The MIC (I) countries are more heterogeneous. The Maldives upped public expenditure from 35 to more than 40 per cent of GDP in 2005 and has spent about the same proportion since then. Kazakhstan has seen a sharp rise in public expenditure since 2005, while in the case of Uzbekistan, the ratio has steadily fallen since 1997 (Fig.8). The SSC group, on the other hand, displays remarkable convergence in recent times with spending in all cases around 30 per cent of GDP. This convergence has meant both spending cuts (Bhutan) and increases (Georgia and Mongolia) (Fig.10). The LIC countries are again heterogeneous with all countries but Bangladesh showing increases in the total expenditure GDP ratio, with some dramatic increases occurring post 2006 in several countries (Fig.11) In the case of the EMEs, China has matched increased revenue GDP ratios with increases in public spending; the ratio has stayed more or less constant in India and fallen since 2008 in Indonesia (Fig.12).

Thus, countries in Developing Asia exhibit a generally prudent and conservative fiscal stance, whether assessed in terms of the share of revenue in national income or the share of public expenditure. There is considerable convergence within different groups in revenue shares. Non tax revenues do cause some volatility in the MIC (I) group. On expenditure, the HIC countries exhibit stable and, by global standards, conservative public expenditure ratios, indicating that there has been no recourse to “Kaldor- Hicks” type distributional initiatives over the period. The same is true for the MIC groups with the exception of Kazakhstan. Remarkably the SSC group also shows convergence with respect to public spending at around 30 per cent of GDP. The LIC group has recorded increases in expenditure GDP ratios but, with the exception of the

Kyrgyz Republic and Timor-Leste, shares continue to be low at around 20 per cent of GDP

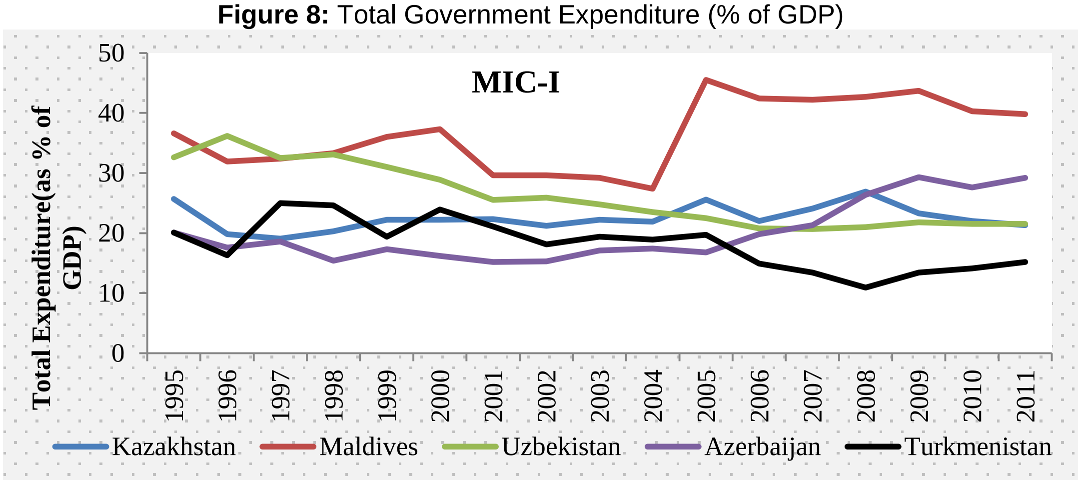
- ***Inference:*** *Revenue and expenditure shares in Developing Asia indicate that the region has not resorted to Kaldor-Hicks type fiscal policy measures in the pursuit of inclusive growth. The endeavor is to pursue inclusion through improving human capabilities and maintaining a prudent macro-fiscal stance.*

Figure 7: Total Government Expenditure (% of GDP)



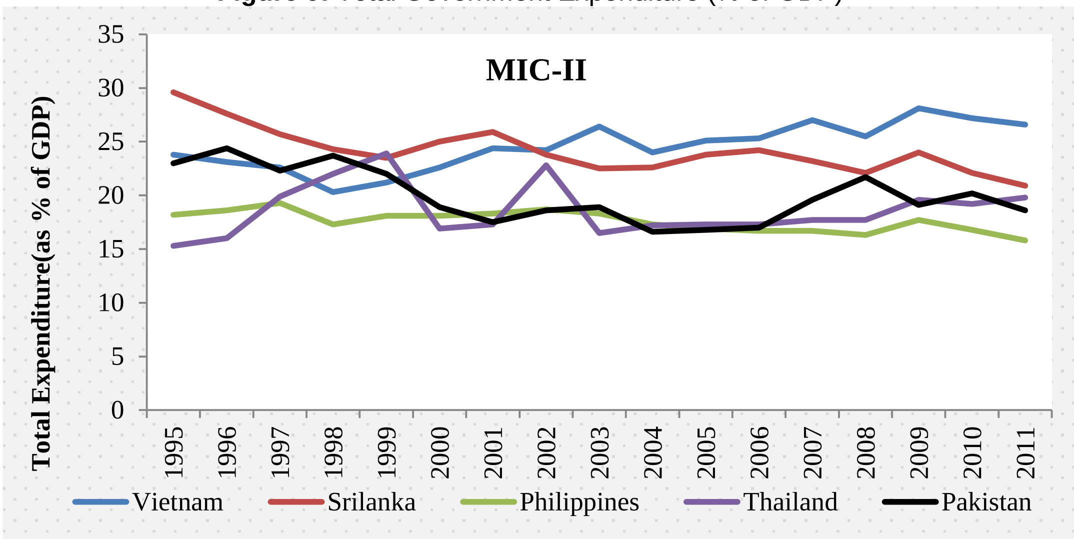
Source: ADB Database, Country Profiles

Figure 8: Total Government Expenditure (% of GDP)



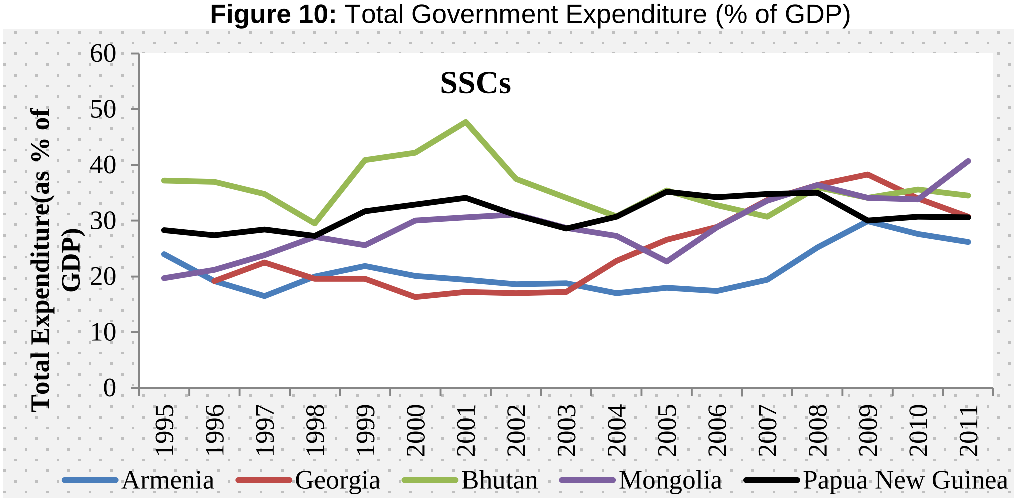
Source: ADB Database, Country Profiles

Figure 9: Total Government Expenditure (% of GDP)



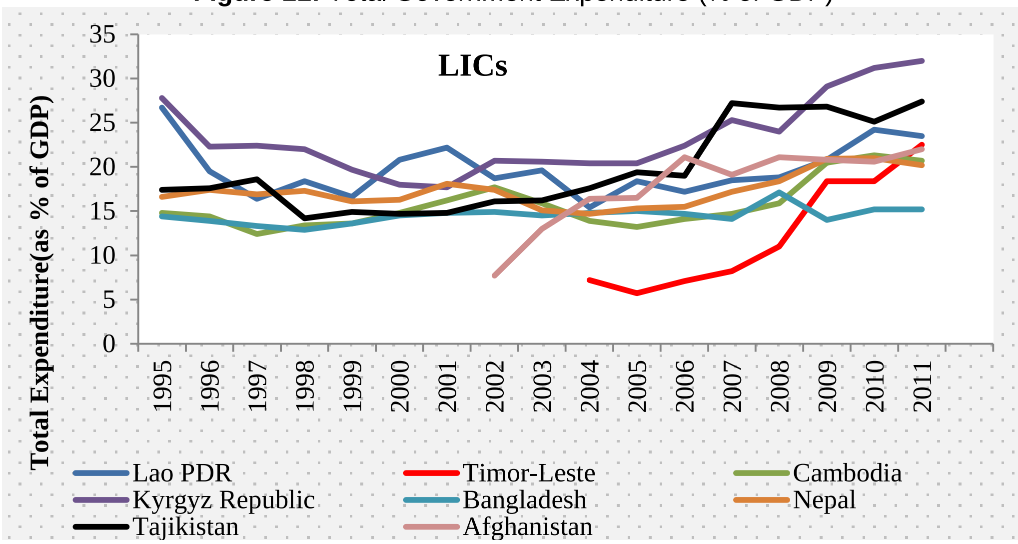
Source: ADB Database, Country Profiles

Figure 10: Total Government Expenditure (% of GDP)



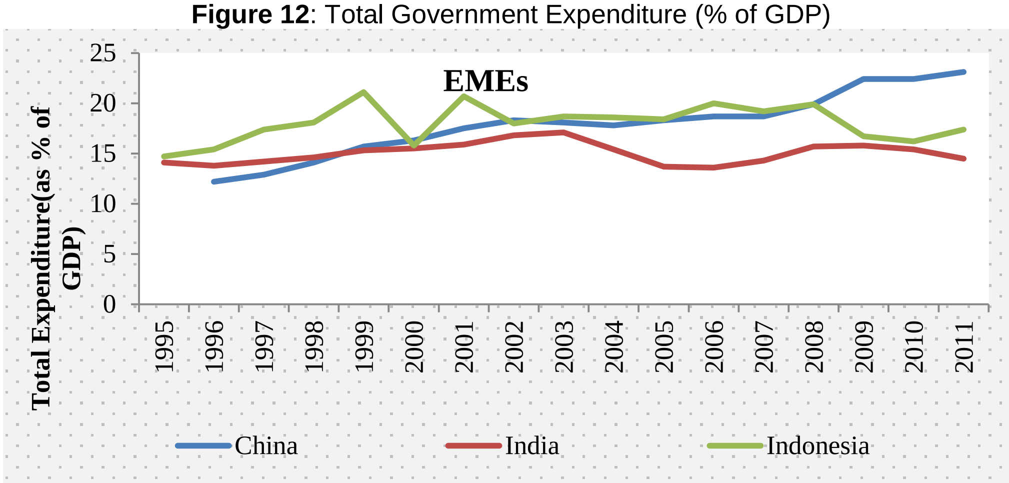
Source: ADB Database, Country Profiles

Figure 11: Total Government Expenditure (% of GDP)



Source: ADB Database, Country Profiles

Figure 12: Total Government Expenditure (% of GDP)



Source: ADB Database, Country Profiles

Section 3.2. Public expenditure trends and spending on inclusive growth

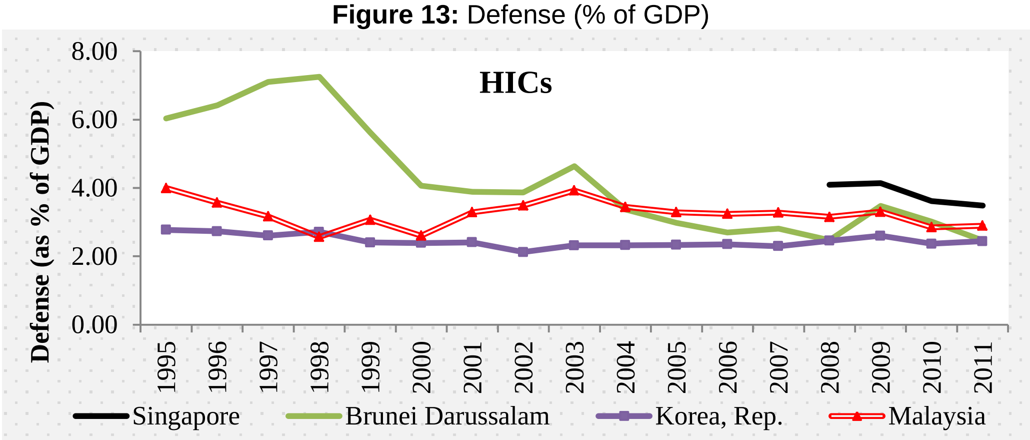
When it comes to the incidence of public expenditure by functional outlay, several interesting trends can be discerned. Malaysia and South Korea have significant outlays on defense (Fig.13). However, Malaysia deploys almost double its GDP on education, compared to Korea. – Its health expenditures are also significantly higher (Fig.14 and 15). Other than defense, Korea has major and increasing outlays on social welfare expenditures, perhaps accounting for its persistent and significantly low levels of inequality (Fig.16).

The MICs for which data is available, all seem to spend about the same as the HICs on defense[3]; their outlays on education are comparable to Korea's while their health spending is somewhat higher[4]. Other than Sri Lanka, social welfare spending has always been low in these countries and in Sri Lanka too, it has been consistently falling since 1995 The LICs, with the exception of the Kyrgyz Republic, spend moderately on defense – the other historically high spender- Cambodia has sharply moderated its defense spending. At the same time, spending on social welfare, education and health as a proportion of GDP remains low in all LICs, except the Kyrgyz Republic, notwithstanding a sharp rise in the allocation to social welfare expenditures by Tajikistan in this decade. India and China spend moderately on defense, but India has not managed to significantly increase GDP allocations on health and education[5].

From the above examination of the functional disposition of public expenditure, it appears that by and large, countries in Developing Asia spend moderately on defense in relation to their GDP. However, health and education outlays are low in the SSCs, LICs and the EMEs.

- **Inference:** *While Developing Asia has inter-temporally not been a significant spender on "regrettable necessities" like defense (though data gaps on this indicator mean that this must be interpreted with caution especially for countries like Pakistan and Indonesia), spending on education health and social welfare remains low except in the HIC group. MICs have increased outlays on education in recent years but health and social welfare outlays are still low and there is considerable scope to increase these human capability enhancing expenditures, especially given generally conservative levels of revenue mobilization, should macro fiscal balances be inter-temporally sound.*

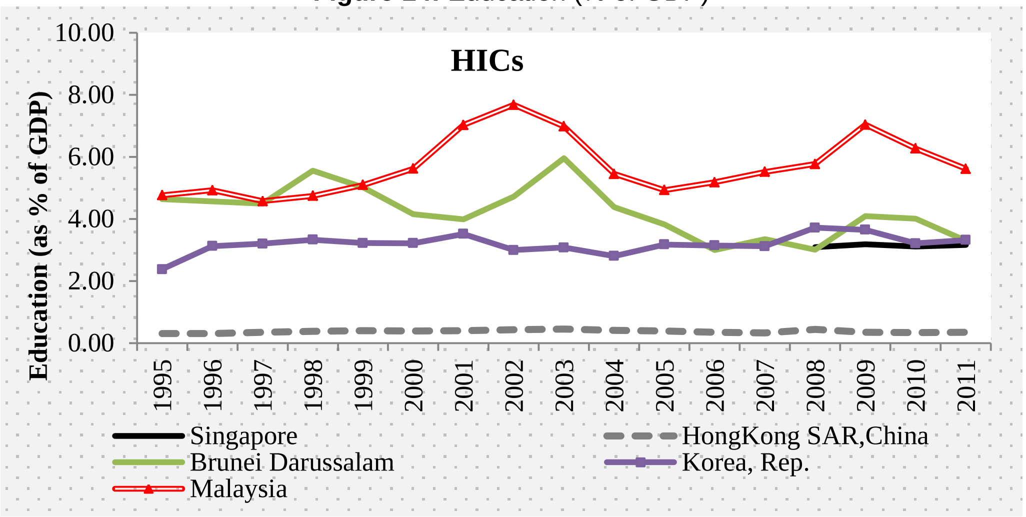
Figure 13: Defense (% of GDP)



Source: ADB Database, Country Profiles

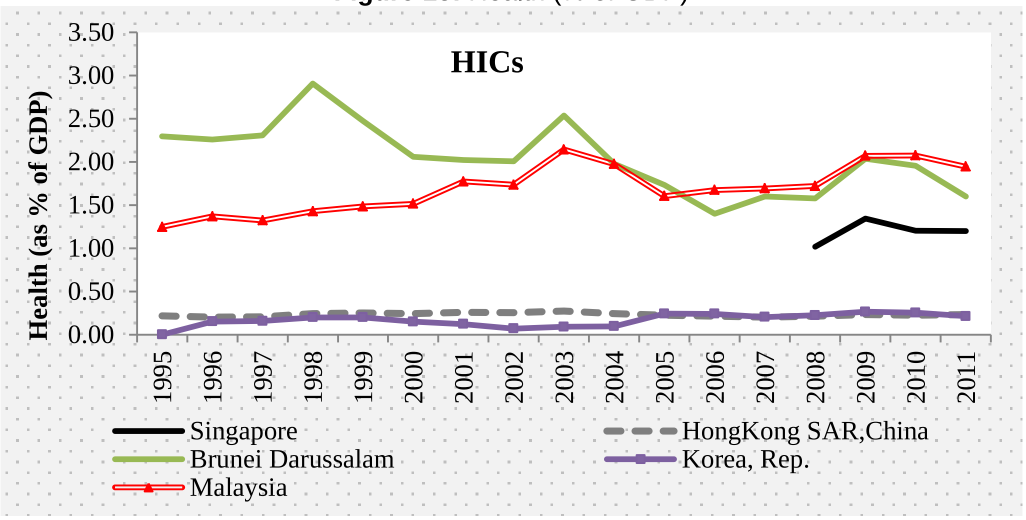
[3] Data available on request
[4] Data available on request
[5] Data available on request

Figure 14: Education (% of GDP)



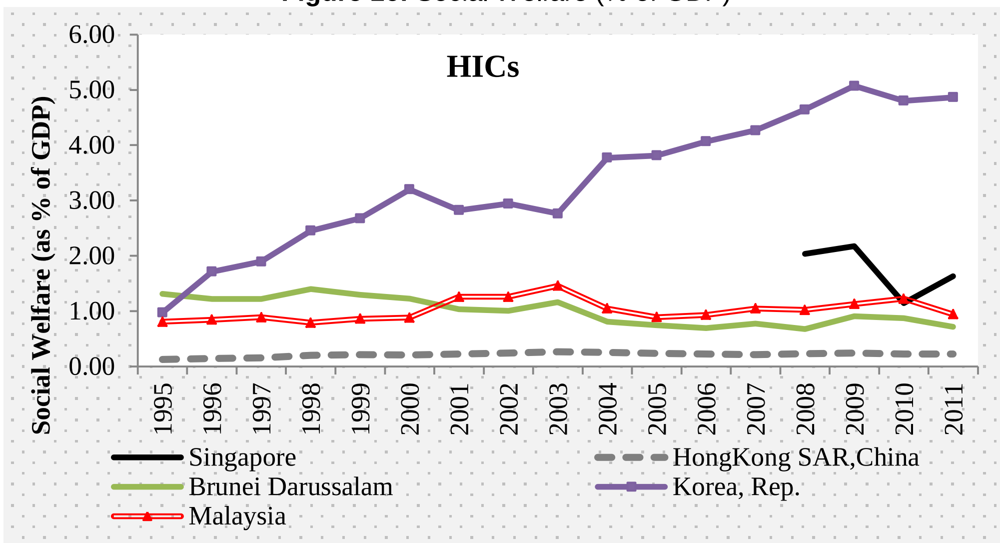
Source: ADB Database, Country Profiles

Figure 15: Health (% of GDP)



Source: ADB Database, Country Profiles

Figure 16: Social Welfare (% of GDP)



Source: ADB Database, Country Profiles

An examination of the shares of health education and social welfare, respectively, in total government expenditure (as opposed to GDP) affords some interesting compositional insights to nuance the above inference. We rank countries according to whether expenditure on social welfare is higher than (a) combined expenditure on health and education (*Table 1*) (b) expenditure on health (*Table 2*) and expenditure on education (*Table 3*) over time.

From *Table 1,* we see that across the recent medium term, Developing Asia continues to prioritise expenditure on human capabilities over expenditure on social welfare, with the exception of Armenia and Georgia, possibly due to transition legacy effects. Korea is the only country which has seen a change in the relative importance of welfare spending which is to be expected as a country approaches steady state. However, when it comes to prioritizing social welfare expenditure over health expenditures, we see that the MICs and the SSCs do indeed prioritize the former; surprisingly several LICs too prioritize the former, as do both China and India. The same is not true for education.

- **Inference:** *While Kaldor-Hicks type expenditures on social welfare are not in general prioritized over expenditures on human capabilities – health and education- within the typical Developing Asian country's expenditure portfolio, it appears that there is some scope to increase the focus of public expenditures on health, either through raising total current expenditures (where this is possible) due to reasonable inter-temporal current fiscal surpluses or, in the case of countries with low or negative current surpluses, through expenditure switching policies that would facilitate such a reprioritization.*

Table 1: Comparison of Expenditure on Social Welfare and Security *vis-a-vis* Health and Education

	1995	2000	2005	2008	2011
HICs					
Singapore	low	low	low	low	low
HongKongSAR,China	low	low	low	low	low
Brunei Darussalam	low	low	low	low	low
Korea, Rep.	low	low	high	high	high
Malaysia	low	low	low	low	low
MIC-I					
Kazakhstan					
Maldives	low	low	low	low	low
Uzbekistan					
Azerbaijan	low	low	low	low	low
Turkmenistan					
MIC-II					
Vietnam					
Srilanka	high	low	low	low	low
Philippines	low	low	low	low	low
Thailand	low	low	low	low	low
Pakistan					
SSCs					
Armenia	low	low	low	high	high
Georgia	high	high	high	low	high
Bhutan			low	low	low
Mongolia	low	low	low	high	high
Papua New Guinea	low	low			
LICs					
Lao PDR					
Timor-Leste			low	low	low
Cambodia	low	low	low	low	low
Kyrgyz Republic	low	low	low	low	low
Bangladesh	low	low	low	low	low
Nepal	low	low	low	low	low
Tajikistan	low	low	low	low	low
Afghanistan					
EMEs					
China	low	low	low	low	low
India		low	low	low	
Indonesia					

Source: Author's calculations using ADB database on Inclusive growth Indicators

Table 2: Comparison of Expenditure on Social Welfare and Security *vis-a-vis*, Health

	1995	2000	2005	2008	2011
HICs					
Singapore	low	low	low	high	high
HongKongSAR,China	low	low	high	high	low
Brunei Darussalam	low	low	low	low	low
Korea, Rep.		high	high	high	high
Malaysia	low	low	low	low	low
MIC-I					
Kazakhstan					
Maldives	low	low	low	low	high
Uzbekistan					
Azerbaijan	high	high	high	high	high
Turkmenistan					
MIC-II					
Vietnam					
Srilanka	high	high	high	high	high
Philippines	low	high	high	high	high
Thailand	low	low	high	low	low
Pakistan					
SSCs					
Armenia	low	high	high	high	high
Georgia	high	high	high	high	high
Bhutan			low	low	low
Mongolia	high	high	high	high	high
Papua New Guinea	low	low			
LICs					
Lao PDR					
Timor-Leste			low	high	high
Cambodia	high	low	low	low	low
Kyrgyz Republic	high	low	high	high	high
Bangladesh	low	low	low	low	low
Nepal	low	low	low	low	low
Tajikistan	low	high	high	high	high
Afghanistan					
EMEs					
China				high	high
India		high	high	high	
Indonesia					

Source: Author's calculations using ADB database on Inclusive growth Indicators

Table 3: Comparison of Expenditure on Social Welfare and Security *vis-a-vis*, Education

	1995	2000	2005	2008	2011
HICs					
Singapore	low	low	low	low	low
HongKongSAR,China	low	low	low	low	low
Brunei Darussalam	low	low	low	low	low
Korea, Rep.	low	low	high	high	high
Malaysia	low	low	low	low	low
MIC-I					
Kazakhstan					
Maldives	low	low	low	low	low
Uzbekistan					
Azerbaijan	low	low	low	low	low
Turkmenistan					
MIC-II					
Vietnam					
Srilanka	high	high	high	low	high
Philippines	low	low	low	low	low
Thailand	low	low	low	low	low
Pakistan					
SSCs					
Armenia	low	low	low	high	high
Georgia	high	high	high	low	high
Bhutan			low	low	low
Mongolia	low	low	high	high	high
Papua New Guinea	low	low			
LICs					
Lao PDR					
Timor-Leste			low	low	high
Cambodia	low	low	low	low	low
Kyrgyz Republic	low	low	low	low	low
Bangladesh	low	low	low	low	low
Nepal	low	low	low	low	low
Tajikistan	low	low	low	low	
Afghanistan					
EMEs					
China	low	low	low	low	low
India		low	low	low	
Indonesia					

Source: Author's calculations using ADB database on Inclusive growth Indicators

Section 3.3. Macro-fiscal stability: Fiscal space for inclusive growth

The story of macro-fiscal stability is, at first cut, told by the extent to which countrys' revenues cover their public expenditures. A golden rule of fiscal policy is that current expenditures should, at least, be covered by current revenues.

It is clear that in many countries in Developing Asia the "Golden Rule" is meticulously followed. There are a few clear exceptions; these are clustered mainly in South and Central Asia. Thus Kazakhstan, the Kyrgyz Republic, the Maldives, Sri Lanka, Pakistan and India have been consistently running current deficits across the 1995-2011 period. In the case of the Kyrgyz Republic, the economic downturn seems to have caused a reversion to an earlier trend of current deficits – the country recorded current surpluses from 2003-2008 and deficits before and after that sub-period. Another group of countries – Tajikistan, Armenia Georgia and Thailand recorded current deficits during the 2009-2011 downturn but appear to have reverted to compliance with the golden rule in 2011[6].

As far as overall fiscal balance goes, while a country's fiscal deficit limits are determined by country characteristics and policy limits such as fiscal rules, it is interesting to note that much of Developing Asia in fact operates at reasonable levels of fiscal prudence. The HICs, with the exception of Malaysia, quite routinely incur fiscal surpluses. The MIC (II) group routinely runs fiscal deficits but there is a distinction here between the ASEAN MICs and the South Asian MICs; in the latter case the fiscal deficits are of much higher magnitude. What marks out the SSCs is high volatility in fiscal balances with countries running large deficits and also significant surpluses in different phases since 2003-04. The LIC group tends to be prudent as a whole – in recent times only Tajikistan has consistently faced fiscal deficits of any significant magnitude. With the EMEs, again China and Indonesia run moderate fiscal deficits with India being unable to reduce its deficits to its own FRBM targets over the last 16 years[7].

The EMEs and LICs, at opposite ends of the economic size spectrum, tend to finance their deficits domestically thus, limiting concerns regarding spillovers. This is also true of the MICs, excepting Kazakhstan and the Maldives, with the MIC (II) group having significantly reduced external debt over the past 8 years to less than 50 per cent of GNI. The opposite is true of the SSCs which have witnessed a spike in external debt since the 2008 crisis, with Mongolia being the only exception[8] .

Remarkably, across all of Developing Asia, most debt is long term in nature, which bodes well for fiscal prudence. The two exceptions are China and Thailand - in both these countries, there appears to have been a deliberate policy initiative to switch to short term debt. With these overall debt patterns, general government gross debt is also low enough to be called prudent in most of Developing Asia, the exceptions being Singapore, the Maldives, and Sri Lanka (where it has, however, fallen consistently until 2008).

[6] Data available on request
[7] Data available on request
[8] Data available on request

- **Inference:** *There is fiscal space to invest in inclusive growth in Developing Asia. However, there are some important exceptions, especially in South and Central Asia, where the "golden rule" is being consistently violated. In these countries, until the tax effort improves, there is extremely limited room to increase spending on human capabilities. The inter-temporal debt patterns, both in terms of size and composition, are remarkably stable and low across most of Developing Asia. This is not a constraint to inclusive growth.*

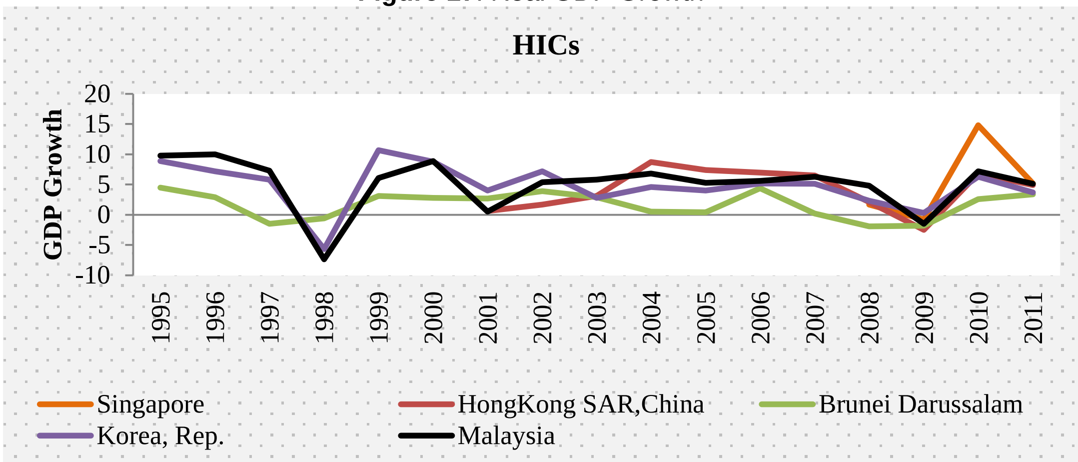
Section 3.4. The Asia growth story and the inclusive growth story

As highlighted in the introduction, for growth to be inclusive, an *a priori* condition is that it must be sustained and of a magnitude sufficient to allow for targeted public spending to improve human capabilities and provide the necessary economic and social infrastructure to improve inclusivity. Prudent fiscal policies may act as a constraint on growth if they do not sufficiently stimulate economic activity. Further, if growth is volatile then scarce fiscal resources can be diverted to stabilization, acting as a constraint on fiscal space for inclusive growth

The Asian region has been known across the past thirty years as one which records growth rates that are phenomenal by the standards of other regions. Whether or not such growth has been inclusive, it would be instructive to first discern what the "Asia growth story" is in recent times. Other than the well-known rise of India and China and the continued importance of countries like South Korea and Singapore as growth poles, what else can be seen from a comparative look at the numbers?

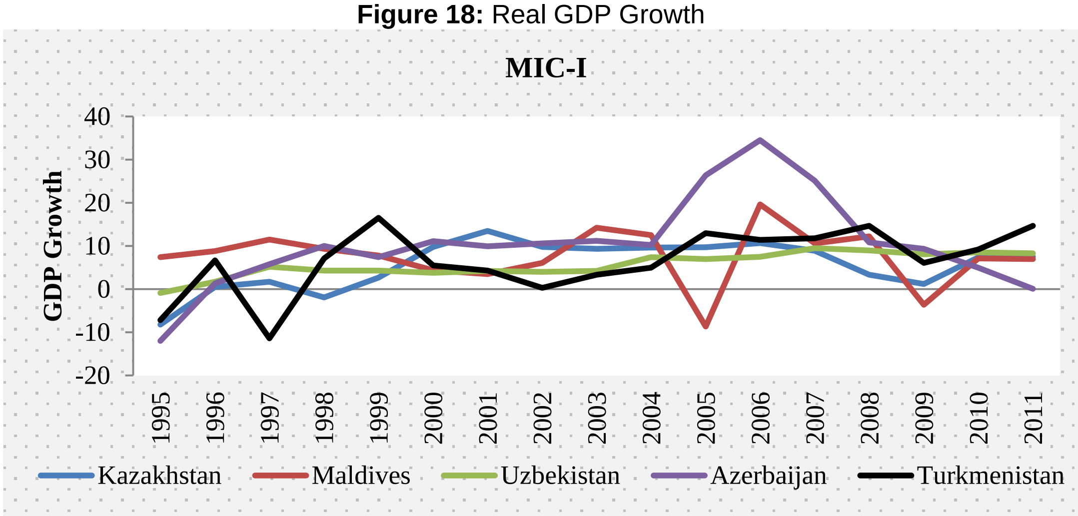
(1) In the two major HICs, i.e. South Korea and Malaysia growth appears to be cyclical. It is difficult to judge whether indeed the recent growth story approximates a scenario of steady state growth. Yet, even if this were to be the case, the steady state level would be somewhere between 4 and 5 per cent for both countries, a level significantly higher than reported for similar countries in other regions. (Fig.17)
(2) The MIC (I) countries display volatile growth trends with pronounced cyclical features. The exception in this group is Uzbekistan which has recorded steady and high growth over the past eight years.(Fig.18)
(3) The MIC (II) countries present a mixed picture. Other than Vietnam, growth in these countries is volatile with the last economic slowdown having caused a pronounced drop in growth in all of them.(Fig.19)
(4) 2008-09 was a year of growth adversity also for all the SSC countries except Papua New Guinea.(Fig.20)
(5) The EME group on the other hand displayed remarkable resilience in growth in the same period though India and Indonesia both faced slowdowns in 2011.(Fig.21)

Figure 17: Real GDP Growth



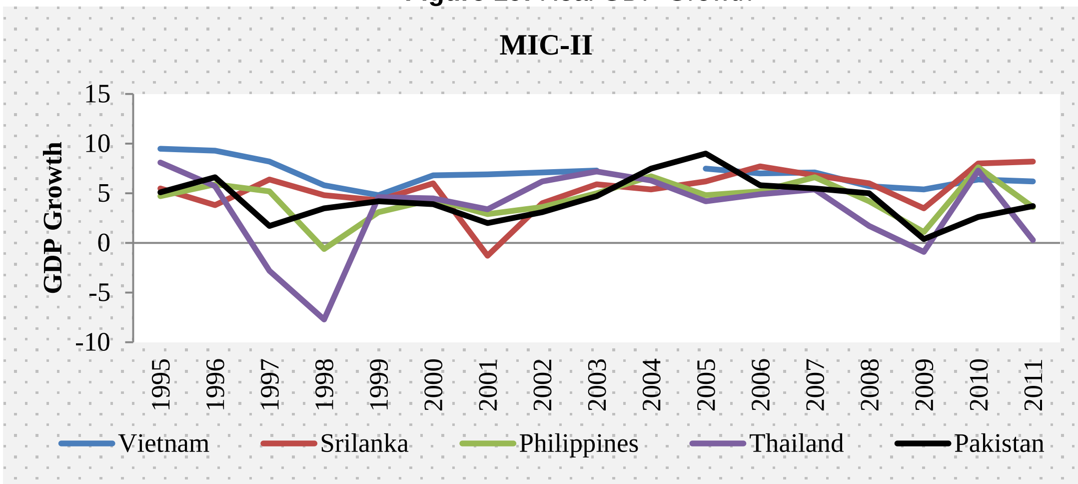
Source: ADB Database, Country Profiles

Figure 18: Real GDP Growth



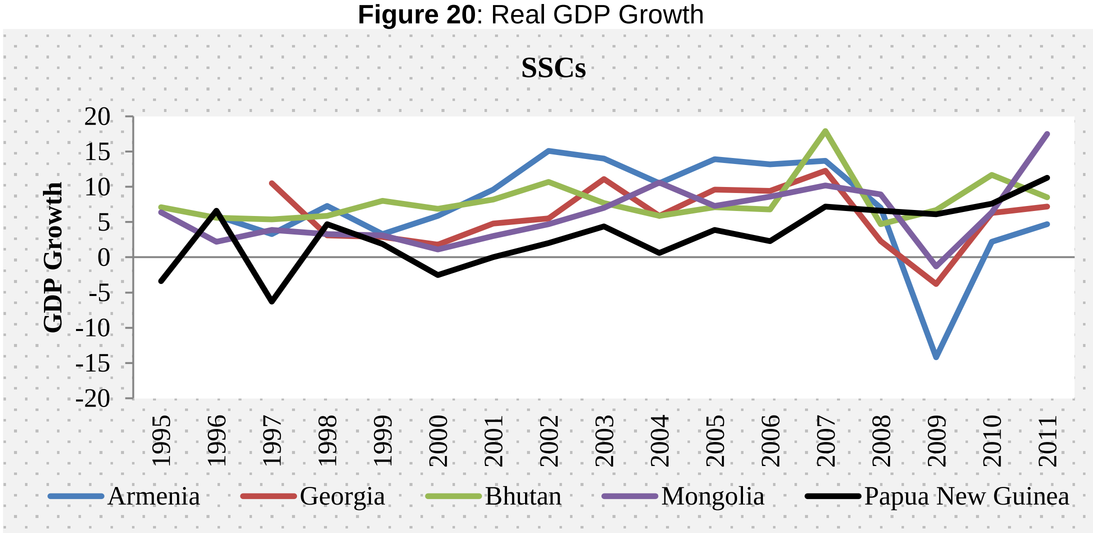
Source: ADB Database, Country Profiles

Figure 19: Real GDP Growth



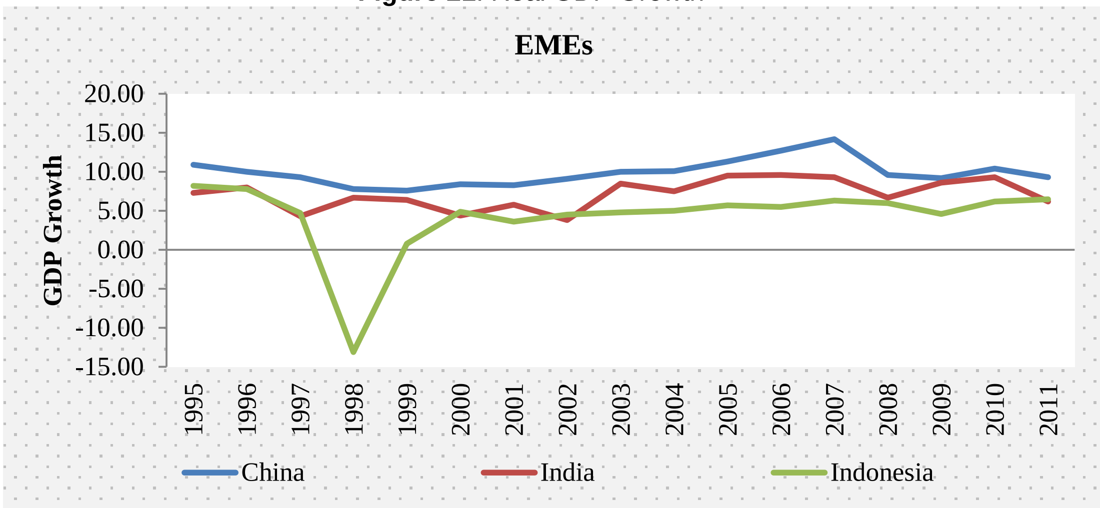
Source: ADB Database, Country Profiles

Figure 20: Real GDP Growth



Source: ADB Database, Country Profiles

Figure 21: Real GDP Growth



Source: ADB Database, Country Profiles

- **Inference:** *We can see both from an examination of inter-temporal trends and from looking at median growth figures across the groupings that growth across the region has not been inter-temporally low in the medium term notwithstanding a prudent fiscal stance. Prudent fiscal policies have not obviously retarded growth in Developing Asia. However, the MICs and the SSCs face a challenge from the volatility of growth, requiring greater attention in these countries to using fiscal policy as a stabilization instrument.*

Turning to the "inclusion story", our main interest here is to see whether there are any sharp changes in inclusion within and across different countries in Developing Asia that can in any reasonable way to be linked to the design and articulation of fiscal policies. Here, we are confounded primarily by the lack of adequate comparable inter-temporal data.

One of the critical indicators of inclusive growth that is of the *ex-ante* variety discussed in the introduction (Section I) is the extent to which people are participating in the business of delivering growth. The obvious indicator to use for this is employment and indeed there has been a lot of emphasis placed on this by many authors (see, for example, Felipe 2009). However, it is difficult to see how employment can be influenced by fiscal stance unless governments decide to provide incentives to enhance wage shares and/or labour intensity of output through the provision of selective tax and subsidy incentives. This would be both inefficient – in the sense that other policy instruments would achieve this with far greater efficacy – and highly distortionary.

However, one can take a call on how well Developing Asia is doing on this score by examining employment-population ratios. While this is an imperfect measure as country demographics vary widely, it is the only measure for which some inter temporal data is available[9] . These indicate that median employment population ratios tend to be fairly stable. The median employment-population ratio has tended to be fairly stable across all country groupings except the MIC (I) countries where it has risen, possibly due to the stabilization of economic transition.

In the case of the infant mortality ratio, the trends are largely downward stable for most of the countries across Developing Asia[10]. The countries for which data is available on health spending, it would appear that there is no clear correlation between countries that have stepped up health spending (or reduced it) and infant mortality results. Such declines appear to be linked, if anything, with the growth effect.

Income and consumption inequality is another popular measure of the extent to which growth is inclusive. The Gini coefficient is a measure of ex poste inequality – ex ante inclusion is better measured by changes in income shares of the highest versus the lowest quintiles, on the assumption that, given the virtual absence of redistributive welfare measures in the fiscal policies of most countries in Developing Asia, changes in this ratio would be influenced by changes in the intensity of use of factor endowment and/or factor prices of those factor endowments that belong to populations in the lowest quintiles (See Roy 2011 for an explanation). Again (*Table 4*), this ratio appears to have been inter-temporally quite stable across the medium term. Many countries have recorded mild improvements in this ratio; the most striking cases of worsening ratios are the countries in the emerging economies group i.e. China, India and Indonesia. These are also the fastest growing and most dynamic economies in Asia and it would be imprudent to draw any conclusion about the link between this rise in the ratio and the conduct of fiscal policy in these countries. More detailed research would be required at country level to draw any correlations.

- **Inference:** *For the bulk of Developing Asia trends in the limited variables of inclusive growth that we have examined do not indicate any dramatic first order link between performance in individual measures of inclusion and the conduct of fiscal policy. In the case of the emerging economies, it is clear that there is a prima facie case for redistributive measures to address the increase in top-bottom inequity in consumption; in the case of India, there is limited fiscal space to undertake such an exercise, though some room may exist for enhancing the magnitude of redistributive policies in the case of China and Indonesia, consistent with fiscal prudence. Otherwise, it appears that inclusion is best served by making fiscal policy an instrument to secure rapid progress to steady state growth rather than to attempt a break with the extant model by resorting to redistributive Kaldor Hicks type measures.*

[9] Data available on request
[10] Data available on request

Table 4 : Ratio of Income or Consumption Share of the Highest Quintile to Lowest Quintile

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
HICs																	
Singapore#				12.3					12.0					14.5			
HongKongSAR,China#		9.6															
Brunei Darussalam																	
Korea, Rep. $												5.4	5.4			5.7	5.7
Malaysia#	12.0		12.4							6.9			11.0		11.3		
MIC-I																	
Kazakhstan		6.2					8.5	5.9	5.6	5.1		4.5	4.6	4.2	4.2		
Maldives				46.6						6.8							
Uzbekistan				12.7				5.5	6.2								
Azerbaijan	6.1						5.9							5.3			
Turkmenistan				7.7													
MIC-II																	
Vietnam				5.5				6.1		6.2		6.0		5.9			
Srilanka		5.5						7.2					6.9			5.8	
Philippines			9.8			9.7			9.3			9.0			8.3		
Thailand		8.1		7.6	8.2	8.0		7.7				8.1		7.2		6.9	
Pakistan			3.9		4.8			4.3			4.4	4.7		4.2			
SSCs																	
Armenia		9.2			5.8		5.8	5.5	5.0	6.1	5.6	4.9	4.5	4.5		4.6	
Georgia		7.1	9.4	7.1	8.8	8.9	8.4	8.2	8.4		8.7	8.5	7.6	8.9	8.8	9.5	
Bhutan									9.9				6.8				
Mongolia	5.5			4.9				5.4						6.2			
Papua New Guinea		12.5															

LICs																
Lao PDR		5.4					4.9						5.9			
Timor-Leste						7.0						4.6				
Cambodia									7.2			7.9	6.1	5.6		
Kyrgyz Republic			6.1				4.8		5.6	7.7	6.1	4.8	6.9	6.4	6.5	5.4
Bangladesh	4.9				4.9					4.8					4.7	
Nepal	5.5							7.8							5.0	
Tajikistan				4.5				5.2	5.4			5.5		4.7		
Afghanistan													4.0			
EMEs																
China*	6.0			7.2			8.9			9.6			10.0	10.1		
India*										4.9					5.0	
Indonesia*	4.5			4.1			4.2			5.1			5.3		5.7	

Notes:
* Data for these countries is derived from the consumption share of the highest quintile to lowest quintile. Combines the urban and rural distributions, weighted by share of urban and rural population to total population
# Data for these countries is derived from income share of the highest quintile to lowest quintile
$ Data for Korea, Rep. is derived from income share of the highest quintile to lowest quintile. Income is defined as disposable household income
Data for all other countries is derived from consumption share of the highest quintile to lowest quintile

Source: ADB Database on Financial Inclusion Indicators

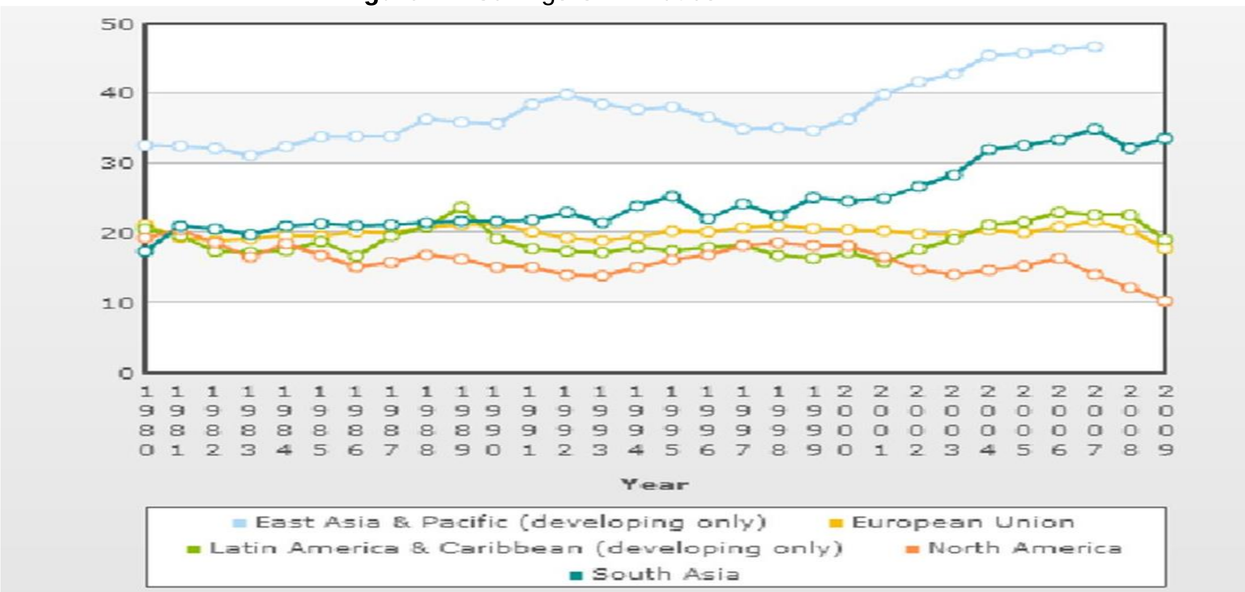
4. Fiscal Space, Savings and Inclusive Growth

The Asia Pacific region has historically been thought of as a high savings region and the traditional story of development transformation in the region is tied not to aid or to large financial transfers from other regions (with the exception of US aid to Japan and the early underwriting of defense budgets in South Korea, PRC Taiwan and Hong Kong) but of success in mobilizing savings – both domestic and cross border – to accelerate investment. There are two dimensions to this story that are of specific interest in the context of this paper.

The global pool of savings (not the Savings/GDP ratio which is the stock-flow counterpart that measures the size of the savings flow compared to GDP) is pertinent in assessing Asia's role and contribution to the future of global development process. The fact that the global pool of savings is *prima facie* sufficient to address post 2015 development challenges is well recognized by those tasked to think about the development finance in the context of the post 2015 process (e.g. Sheng 2013). UN (2013) too asserts that "The money is there—world savings this year will likely be over USD 18 trillion"

As we can see from Fig.22 the high-saving regions of the world have, for the past 30 years been the same i.e. East Asia and South Asia. From this picture, one could quite legitimately conclude that Asia has always dominated global savings mobilisation.

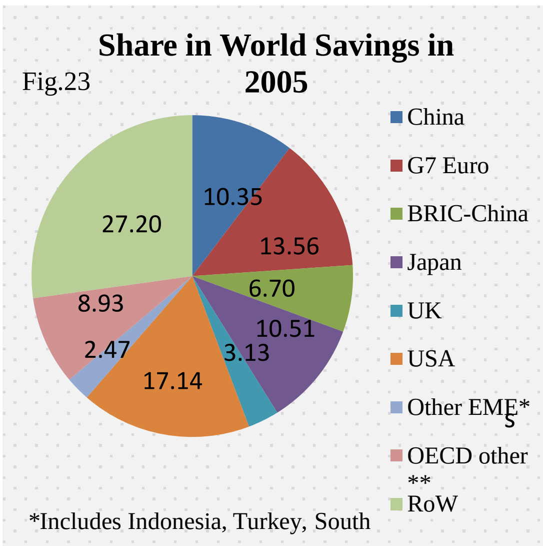
Figure 22: Savings GDP Ratios

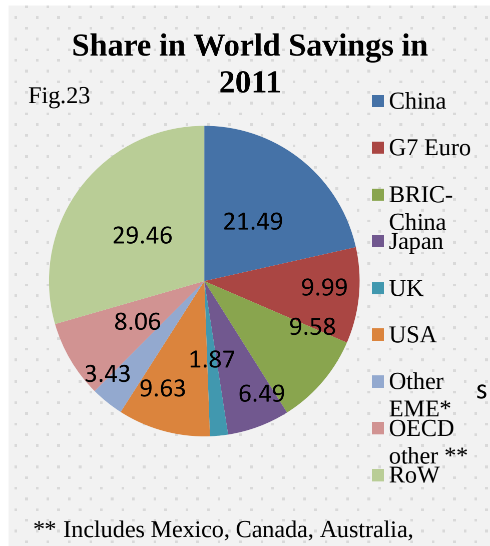


Source: World Development Indicators

This, of course, is not true. The reason is that historically the *share* of developed country savings in total savings has been of a far higher magnitude than that of developing countries. Thus, International Public Finance was an instrument to re-assign these savings from being deployed in developed countries to developing countries through a public sector process when markets failed to do so (or failed to do so in a magnitude sufficient to address public good needs).

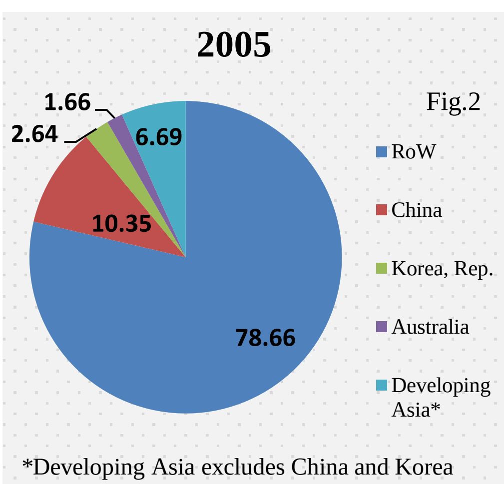
This logic held well until at least 2005. From Fig. 23a and 23b, we see that the United States, followed by the G7 Eurozone, collectively generated more than 30 per cent of global saving. With Japan and other G7 countries more than half of global saving was generated within the G7as recently as 2005, *despite the rise of China and more recently the BRICS*. (Fig.23a)

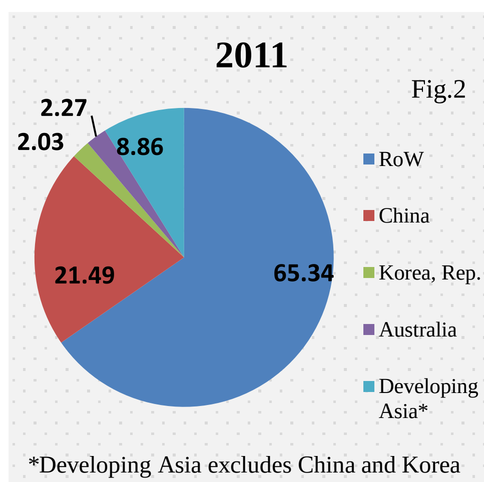




Source: World Development Indicators

This picture has changed dramatically in recent years (Fig.23b). Today China accounts for the highest share in world savings of any country, followed by the United States. The other BRIC countries contribute savings comparable to the G7 Eurozone and exceeding Japan.





Source: World Development Indicators

This affects Developing Asia quite dramatically.(Fig.23c and 23d)While the bulk of the rise in the share of Developing Asia in global savings is accounted for by China, there has also been a non-trivial increase in the share of the rest of Developing Asia as well. Further, Australia, alone among developed countries has seen an increase in its share of global savings.

If private sector and World Bank research is credible, then this reversal is likely to continue over the next five years. However existing institutions for mobilization of savings for International Public Finance continue to operate as if the World is what it was in 2005.

This new trend presents perhaps the greatest challenge to the International Public Finance Architecture. The Asia Pacific region has ample use for savings for domestic investment purposes as most countries in Developing Asia are not (with the possible exception of the HICs) anywhere near their maximum possible steady-state growth path. At the same time, these countries have proactively sought to engage with their partners in the global South, to explore ways in which their savings could be deployed to build development partnerships that reinforce mutual gains through growth in South-South development relationships. Looking at Asia as a region, the available pool of domestic savings is now of an order of magnitude that is highly conducive to regional arrangements to mobilise these resources for investments in key economic services and other capital expenditures, transitively relaxing the fiscal constraint on countries in Developing Asia to raise current expenditures on health education and other outlays conducive to inclusive growth.

In other words, with the appropriate institutional arrangements in place; Asia has enough savings to finance the growth requirements of the region. Regional co-operation to maximize the disposition of these savings for public and private investment then opens up fiscal space for countries to prudently utilize their current revenues for spending on merit and public goods for inclusive growth that require increases in current expenditure.

- **Inference:** *The phenomenon of what one can term, " Asian savings dominance", has two important implications for Developing Asia:*

    - ✓ *The scope for Pan-Asian coordination to channel resources for public and private investments across Developing Asia is now no longer reliant on savings from other regions.*
    - ✓ *This provides a significant pool of resources for public and private investments in inclusive growth. Co-ordinated fiscal (and monetary actions) across Developing Asia could be key to optimizing the pool of available resources for such investments.*

The rapid increase in the share of Developing Asia in global savings is already having a beneficial impact on fiscal stability. Thus even in HICs in Developing Asia, Investment-GDP ratios are high and stable at between 25 and 30 per cent. The MIC (I) group traditionally considered low savers in the 1990s have seen very sharp increases in their Savings-GDP ratios and in total Investment-GDP ratios over the past decade. In the MIC (II) group low savings continues to constrain the investment outlays of Pakistan and the Philippines. In the SSCs too, high Savings-GDP ratios have led to increased Investment-GDP ratios, in Bhutan's case marking a shift from aid financed investments to domestically resourced investments in some significant measure. The LICs exhibit higher investment ratios notwithstanding low savings ratios, chiefly due to access to highly concessional investment finance – yet the fact that savings are higher than in other LICs means, in turn that the overall Investment-GDP ratios for most Asian LICs is higher than that for LICs in other regions[11]. Given the fact that the regions as a whole follows sound public finance principles the only countries where the "draft" of public sector spending on domestic savings is high are India, Sri Lanka and Pakistan; these three countries are also remarkable for the extent and magnitude of borrowing financed government consumption, measured by the current fiscal deficit, a phenomenon they have failed to address in current years.

- **Inferences**

  - ✓ *There have been important recent changes in the incidence of global savings, favoring Developing Asia.*
  - ✓ *An examination of savings behavior and debt deficit patterns indicates that fiscal space exists both for public investment and for expansion of current expenditure in the majority of Developing Asia.*
  - ✓ *These two trends in conjunction indicate that there is scope for enhancing fiscal space for public investment, though tax effort would need to increase if merit good provisioning is to be enhanced.*

5. The Impact of Countercyclical Fiscal Policy on Growth and Inclusion

There is a constant tension for governments between securing fiscal prudence and maintaining predictability in the course of fiscal policy and the pressure to expand spending on public goods and moderate tax burdens, so as to secure inclusive growth. Such pressure is particularly pronounced in times of fiscal stress. When there is an exogenous shock that threatens a recession, there is pressure on governments to run expansionary counter cyclical fiscal policies and to suspend fiscal rules and other prudential commitments until the crisis is weathered.

All governments in Developing Asia face such pressures but, in particular, the emerging economies of Developing Asia have to craft fiscal policies very carefully when expansionary demands arise. The argument for such expansionary countercyclical fiscal policies has become more forceful after the 1997 Asian crisis when it was felt that countries that followed fiscal compression suffered in contrast with countries that took active steps to counter the recessionary impact of the crisis using fiscal instruments.

Analysis by Adams *et.al* (2010) in an early finding on countercyclical fiscal stimuli across Asia indicated that Asia's public finances were in relatively good shape prior to the crisis and, therefore, fiscal stimuli were *prima facie* sustainable. They, however, warned that failure to unwind the anti-crisis stimulus would erode the region's fiscal stability. This would seriously restrict medium term fiscal space for inclusive growth.

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[11] Data available on request

From the vantage of the present, the experience of four emerging Developing Asia economies with countercyclical policies following the 2008 crisis provides interesting insights on this issue.

In the case of *India*, the economic crisis elided with the national elections, and so there was a fiscal expansion already undertaken just prior to the onset of the global crisis. A fiscal stimulus equivalent to 4 per cent of GDP was introduced in the central government 2008 budget. The crisis also impacted State finances, with the result that the combined fiscal deficit grew to 11.4 per cent of GDP in that year. While this had serious implications in future years for India's sovereign ratings, given its high and rising current account deficit, and poor growth performance, the immediate fiscal sustainability implications in terms of debt dynamics were not negative as feared by some commentators at the time (Kumar and Vashisht 2009). Thus, India's public debt GDP ratio actually declined from 73 per cent in 2008-09 to 66.36 percent in 2011-12.

Why was this the case? To some extent, this was because the tradition of fiscal prudence for both the Centre and the States set in place by the 12th Finance Commission (2004) and reinforced by the 13th Finance Commission (2010) led to increased fiscal discipline at the State level. State deficits thus declined to more manageable levels shortly after the crisis. On the other hand, with inflation at around 10 per cent, the nominal value of GDP continued to rise faster than the nominal value of debt. Thus, debt sustainability ratios stayed under control. In addition the low ratio of external debt to total debt in India and the extremely high proportion of long-term debt in total debt meant that debt management was relatively easy. So debt sustainability did not threaten India's macroeconomic fundamentals; rather the fact that the fiscal stimulus did not result in the expected growth response – as explained earlier, India underperformed on growth compared to other Asian EMEs and indeed compared to the other BRIC nations – led to increasing macroeconomic difficulties for India and the consequent pressure to reduce deficits and therefore fiscal space.

In the case of *China*, the government provided a massive fiscal stimulus equivalent to 14 per cent of GDP for FY 2008 and 2009 (Yongdin 2010). This included a fiscal stimulus that is expected to result in a fiscal deficit of 3 per cent of GDP in 2009. However, China had plenty of fiscal space to begin with; fiscal deficits had fallen to below 2 per cent of GDP by 2004 and to less than 0.5 per cent of GDP in 2008; the highest fiscal deficit incurred by China was therefore just 2.3 per cent of GDP in 2009. Since that date China's growth rate reverted to its 9.6 per cent median growth rate for the period 1995-2011, thus, fiscal expansion in China was accompanied by the requisite growth payback, thus ensuring fiscal sustainability.

In the case of *Malaysia,* there was an extremely short term fiscal response to the crisis, equivalent to an increase in the fiscal deficit from 4.6 per cent of GDP in 2007 to 6.7 per cent of GDP in 2009. But this was a one year expansion—deficits then reduced down to 4.8 per cent of GDP in 2011 equivalent to the median fiscal deficit of Malaysia for the 1995-2011 period. To some extent this was necessitated by worsening debt dynamics, both an increase in the debt/GDP ratio to over 50 per cent of GDP in the post crisis period, well above the 1995-2011 median, and an increase in the ratio of relatively more expensive external debt to total debt. This limited stimulus had little impact on growth, or medium term macro-fiscal policy (Lim and Goh 2012).

Indonesia went through a fairly long process of fiscal reforms, which included reforms in public financial management as well as significant structural changes in intergovernmental fiscal relations following the 1998 Asian financial crisis. The fiscal deficit-GDP ratio declined continuously. The median fiscal deficit in the 1995-2011 period was therefore a very low 1.1 per cent of GDP, with a concomitant decline in the debt/GDP ratio over time. Indonesia also had in place a fiscal rule which limits the fiscal deficit to 3 per cent of GDP and the ceiling debt-GDP ratio at 60 per cent of GDP (Basri and Rahardja 2011).

Indonesia's 2009 fiscal stimulus package involved an expansionary fiscal policy as well as tax cuts. Over two thirds of the stimulus came from tax cuts and the rest through increased public spending and subsidies (Hur *et.al* 2010). However, this increase in stimulus did not result in breaching of the fiscal rules. Chiefly due to inability in increasing public spending, the 2010 fiscal deficit was 0.7 per cent of GDP, as against a target of 1.3 per cent. (Basri and Rahardja 2011) As a consequence, both revenues and expenditures fell as a percentage of GDP from 2008. Thus in Indonesia's case the fiscal stimulus was not expansionary but rather involved stimulating the private sector through tax cuts and a fall in the government(G)/GDP ratio.

Thus, we see that the four emerging economies of Developing Asia followed very different strategies – with very different outcomes – post the 2008 financial crisis. The chief impact on inclusive growth seems to have been driven by the impact of the fiscal stimulus on growth. There was little impact on the disposition of public spending with no marked increase (relative to trend) in functional outlays on health, education and social welfare post crisis. All the countries maintained fiscally prudent policies in administering the fiscal stimulus; even in the case of India, it was the failure of the fiscal stimulus to maintain growth that resulted in concomitant pressures on economic activity, chiefly through inflation, high nominal interest rates and rising current account deficits; debt sustainability was not impaired by fiscal expansion.

6. Other Issues

Section 6.1.Subsidies

Apart from the Kaldor-Hicks compensation principle; there are other transfers that detract from fiscal space for inclusive growth. Interest on debt is one obvious example; on this score it would appear that most of the countries of Developing Asia have adequate debt sustainability indicators and while inflationary pressures in countries like India raise mark to market pressures on the public finances by raising interest costs on public debt; the problem is not in general one of serious magnitude across Developing Asia. However, fuel subsidies in the region are a cause of special concern in many countries.

Our examination of data available on subsidies in different countries in Developing Asia indicates[12] that fuel and food subsidies take on a significant proportion of total expenditure in an important subset of countries. Fuel subsidies are known to be regressive; their horizontal and vertical incidence is high, and they are difficult to target

[12] Data available on request

when the volume of subsidy provided – as in the case of the PRC, India Indonesia and Malaysia – is high. Food subsidies are more difficult to judge, but it is fair to say that targeted "Kaldor-Hicks" type income transfers are by an large more efficient than direct food subsidies. Thus, on both counts three important emerging economies in the region – Malaysia, Indonesia and the Philippines – have some scope for improving the inclusivity stance of fiscal policy through expenditure switching away from fuel and food subsidies towards the provision of merit goods – especially health in view of the very low incidence of public expenditures on, especially, health, in all these countries. This would be complimentary to the capabilities based overall strategy to inclusion that these countries have adopted. In the case of China, the volume of subsidies is not of an order of magnitude to cause concern given the ample fiscal space available to that country.

Section 6.2. Changes in tax structure

Inclusive growth can be hindered if tax structures are regressive. Measuring changes in the progressivity of overall tax structures is beyond the scope of this paper. However, an examination of trends in the share of different types of taxation over the past 13 years across Developing Asia reveals a distinct maturing of the distribution which can be said, *prima facie*, to be in a relatively progressive direction. This is particularly so for the emerging economies - China, India, and Indonesia, where the share of direct taxes has risen quite dramatically relative to that of indirect taxes across the past decade[13]. Equally impressive is the fact that many low income countries – Cambodia and Bangladesh being striking examples, have recorded an appreciable increase in direct tax shares over the past decade. Some transition economies, like Armenia and Kazakhstan have also managed to stabilize their tax systems reflected in the fact that the share of direct taxes in these countries is now in line with what would be expected given their per capita income levels.

Concluding Observations

Developing Asia is a diverse region; however, there are several common inter-temporal trends that can be observed when countries in similar economic circumstances are looked at together. In general, it can be said that given the exigencies of economic structure and history most countries in Developing Asia have elected to maintain a prudent, rather than activist fiscal stance. Taxation and revenue mobilization instruments have not been used, in general, to alter the economic structure such that the tax burden is relatively high. Public spending, too, tends to be of an order of magnitude that generates an inter-temporally stable G/GDP ratio.

Given this fiscal stance what has been the approach to ensuring that there is inclusive growth?

In the introduction we posed a headline question namely;

(1) *Have countries in Developing Asia chosen to pursue inclusive growth through maximizing progress to a steady State growth path, with Kaldor-Hicks type*

[13] Data available on request

redistributive income transfers being the main instrument to secure desired ex-poste inclusion outcomes?
OR

(2) *Have countries in Developing Asia tended to use fiscal policy to maintain a prudential environment for economic growth, secure countercyclical stabilization of the growth process and deliver merit and public goods to increase human capabilities and permanently enhance participation in the growth process?*

Our overall finding is that upon an examination of inter-temporal trends, Developing Asia in general has opted to go for the second policy option. Developing Asia has not resorted to Kaldor-Hicks type *ex poste* redistributive measures in the pursuit of inclusive growth. At the same time the macro-fiscal structure and the composition of revenue are not overall regressive and there is evidence of appreciable spending when required on protecting growth against external shocks. This is found to be largely the case with high income and middle income countries, as well as countries in special situations and the emerging economies. The share of spending on "regrettable necessities" like defense is controlled in most cases, and in some important instances, like Cambodia, has even declined over time.

Given that this conclusion emerges from an examination of inter-temporal trends, it marks a significant departure from historical stories in other regions that have undergone a development transformation. The "welfare State" model of Western Europe, to which many middle income and fast growing countries in Latin America and the Middle East aspired, is one which Developing Asia has eschewed to date. Growth and productive inclusion have been at the centre of the development transformation story. A prudent fiscal stance, macroeconomic stability and protecting growth from external shocks have been typical features of fiscal policy for the region.

The prudential environment for economic growth has been secured through the maintenance of the "Golden Rule" of fiscal policy, which is to finance current expenditure out of current revenues. In such countries, there is scope to increase spending on the delivery of merit and public goods to increase human capabilities and we find that countries have elected to prioritise such expenditures – on health and education—to secure such capabilities. However, there are important exceptions to this in South Asia, namely India, Pakistan, the Maldives and Sri Lanka. In these countries there is limited incremental room to invest in human capabilities without considerable attention being paid to improving either the tax effort, or reducing expenditures on subsidies and regrettable necessities.

There is some scope to increase public expenditure on health consistent with the overall fiscal stance, by raising current expenditures where the scope to do so is afforded by medium term positive fiscal balances together with mild efforts to increase the tax effort in most countries in Developing Asia. In countries with low or negative current surpluses, expenditure switching policies to increase the share of health spending relative to that on food subsidies and social welfare (subject to the maintenance of a safety net) and on fuel subsidies affords scope for a reprioritization that would be consistent with the overall fiscal stance.

A prudent fiscal stance has not impeded growth which has progressed reasonably and at a stable pace across the country groupings (though the levels obviously vary) and fluctuations do impact growth when there are global shocks such as in 1998 and 2008. However many MICs and the SSC group of countries continue to be challenged by the volatility of growth relative to the rest of the region necessitating the need for more attention to be paid to use fiscal policy as a stabilization instrument.

The case of the emerging economies shows that countercyclical fiscal policies have been deployed, tailored to individual country circumstances and mindful of country prudential limitations, thus, alleviating the fear that persistence with such policies would jeopardise fiscal prudence. Even in the case of India, which has been going through some recent macroeconomic difficulties, it is supply side constraints and balance of payments difficulties that have caused difficulties in macroeconomic management, rather than the inability to speedily tone down countercyclical fiscal policies.

As far as inclusion goes, in this overview, we do not find any dramatic first order link between performance in individual measures of inclusion and the conduct of fiscal policy. In the case of the EMEs, there is a *prima facie* case for redistributive measures to address the increase in top-bottom inequity in consumption, and this may be feasible consistent with fiscal prudence for China and Indonesia, though not for India. Otherwise, in the absence of a first order link, inclusion is best served by using fiscal policy as an instrument to maximize public spending on merit goods and to secure a growth maximizing macro-fiscal environment rather than resort to *ex-poste* Kaldor-Hicks measures.

There is considerable fiscal room for increasing public or publicly funded investment to remove infrastructural barriers to growth. This is especially so, if we look at two factors in conjunction; (1) The important recent changes in the incidence of global savings, favoring Developing Asia, and (2) Our inter-temporal examination of country savings behavior and debt-deficit patterns. These two trends in conjunction indicate that there is scope for enhancing fiscal space for public investment. There is an increased scope for pan Asian coordination to channel resources for public and private investment since Developing Asia is now no longer reliant on savings from other regions. This provides a significant pool of resources for public and private investments in inclusive growth. Co-ordinated fiscal (and monetary) actions across Developing Asia could be key to optimizing the pool of available resources for such investment, if renewed attention is paid to the fostering of a regional institutional architecture and improved fiscal co – ordination.

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