European Institute for Asian Studies

EU-Asia at a Glance

Notes on the 51st Annual Meeting of the Asian Development Bank (Manila, Philippines)

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The annual meeting of the ADB, Asia's leading development bank, is where you can feel the pulse of Asia. It was quite upbeat this year.

Paying due but sober attention to China's infrastructure focused Belt and Road initiative, the ADB nudges Asia to embrace new technologies to further drive growth in Asia.

Panelists discussed whether Asia should continue to bear dollar dominance, and whether the development banks can reverse the trend towards less multilateral cooperation.

EU-Asia at a Glance is a publication series about the current state of affairs in Asia and EU-Asia relations

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Looking beyond the Silk Roads, Asia eyes technology to keep growing.

ADB meeting discusses 'Dollar - Renminbi tussle' and 'more cooperation among Multilateral Development Banks'.

"Nearly half of Asians now live in middle-income countries and the question now is how to move on?" said the ADB's chief economist **Yasuyuki Sawada**. The Bank sees technology spur a virtuous chain of higher productivity delivering more output, yielding higher income which leads to more demand. The logic is applicable everywhere but Asia counts on a greater positive impact because the potential for a rise in demand for goods and services is still very high compared to the West where consumer demands are largely met and therefore markets often saturated. At the same time, Asia's still abundant cheap labour means that the negative effect of job displacement will be lower since the tech-driven alternatives will need to be more economical.

But *"technology also means that exports of manufactured goods will no more yield the growth"* said **Ms. Junhong Chang**, Director of the 'Asean+3 Macroeconomic Research Office' (AMRO). Innovations such as 3D printing and Artificial Intelligence undermine the foreign investment led manufacturing-for-exports model that Asia used to rely on. The rise in protectionism and the fall in demand following the Great Financial Crisis add to the threat. To overcome the shock, *"Asia's resilience is to be built through the service sector, regional interconnectivity, and the 'in-shoring' of regional demand"*.

The conference's main event started with a colourful presentation by Oxford Professor **Peter Frankopan** of his blockbuster book "The Silk Roads". That was ADB's polite nod towards China's Belt and Road Initiative. The subsequent panel discussion added cool realism with observations such as *"what matters is what the roads connect"* and the Philippine panelist observing *"a third of our exports do not need transport"*.

Host country The Philippines, illustrated the business case for Asia's services sector as a new driver for growth. The country achieved 76 consecutive quarters of GDP growth - consistently close to 7 percent in recent years - largely driven by services which make up 60 percent of GDP, 40 percent of exports and employ more than half of the workforce. Its Business Process Outsourcing (BPO) employs more than one million workers with wages three to five times higher than the national average. The Philippines has broadened its services from call centres to more complex functions such as back-office support, data transcription, animation and software development.[2]

Technology has made services scaleable and tradable. Technology has also led to so-called 'uberization' of services with innovative and disruptive service providers coming into the market. Asia's rapidly increasing number of middle-income consumers make the market grow faster than elsewhere. Tourism in particular is a booming sector. It is acknowledged nevertheless that to make full use of the opportunity, countries should focus on upgrading skills and investment in physical as well as digital infrastructure.

The ADB's **president Takehiko Nakao** left no doubt that whisking the Bank and the Asian governments towards policies that promote new age technologies will be an emphasis in

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[2] Source: AMRO, Asean+3 Regional Economic Outlook 2018

the Bank's "Strategy 2030" plan that is currently being drafted. *"We need to redouble our efforts to pay attention to the most advanced technologies, new ideas. If we are not agile enough to take in new technologies we will lose our relevance"*.[3] Asked for their input, the governors, representatives of the 67 ADB member (shareholding-) countries, are not likely to thwart the new focus, but nuances count. The governor from China alluded to the Belt and Road Initiative and called on the ADB to *"increase financing to support infrastructure interconnectivity in the Asia-Pacific region"*. The governor for India advocated that the *"ADB should become a facilitator of ushering in the digital age in Asia. ADB should invest in innovations, in start-ups and in venture capital to help countries produce goods and services using technologies of digital age. It should invest in fin-tech, health-tech, etc"*

India and China still are the ADB's main recipients of loans and assistance with, respectively 18 percent and 12 percent of 2017 commitments. The Bank's continued lending to China is annoying to some. Yet president Nakao is adamant: *"Engagement with China is so important. Without China as a borrowing country our influence and our relevance in this region is more limited". "It is not the money they care about. It's about finance together with knowledge".*[4]

The weight and clout of China was visible throughout the conference, in particular at one notable side-event, a "High Level Session" discussing "the Potential for CAREC-BRI Collaboration". The meeting brought together the representatives of the eleven countries that make up the 'Central Asia Regional Economic Cooperation', a sub-regional grouping formed by the ADB, and the Chinese vice-president of the ADB. **Mr. Wencai Zhang** described the ambitious scope of the Belt-and-Road Initiative (BRI) and stated *"the six transport corridors initiated by CAREC traverse the BRI space, providing further impetus for close coordination to jointly build resilient and sustainable regional infrastructure, strengthen trade links, and create jobs and greater economic opportunities for all our countries"*. The striking element about this meeting was not so much the message, which is obvious, but the fact that the near full range of the world's multilateral development agencies had been lined up to express in turn their support for the initiative. Among them, we heard the International Monetary Fund (IMF), the World Bank, the European Bank for Reconstruction and Development (EBRD), the United Nations Development Programme (UNDP), the Islamic Development Bank, the AIIB, the New Development Bank (NDB), the International Labour Organisation (ILO), the UN Industrial Development Organisation (UNIDO), the CAREC Institute, and the European Commission. Only subtle recommendations were voiced, such as the World Bank representative calling for CAREC to set guidelines for social and environmental safeguards, and the ILO representative saying the safeguards might as well be more ambitiously set as standards.

With the BRI China has set a plan to reshape the world's physical financial structure. In contrast, China's ability to reconfigure the global monetary system is much more limited, said **Dr. Paola Subbachi** from Chatham House. *"As long as the dollar remains the dominant currency in trade and capital markets, the US will continue to be the main player in world economic governance"*. At the basis is the provision of financial stability, liquidity, and safety net that supports the smooth settlement of global trade and investment. Currently the US Federal Reserve Bank is providing that support, even if it is more and

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[3] Quoted in the IFR Asia, April 2018.

[4] Ibid.

more reluctant to do so. The Renminbi, for all its efforts to internationalise, remains *"a constrained currency"* with limited liquidity and usability. As a result China has to lend in dollars and is therefore *"an immature creditor"*. Nor is China really willing to put its resources on the line to support the global financial system. In the opinion of **Sri Mulyani Indrawati**, the Minister of Finance of Indonesia, China should not do so anyway: *"With the US backing up the international order, it also advocates its own interests". "The RMB replacing the USD is no solution. There is an inherent incompatibility in a system with multiple countries having their own sovereignty, fiscal policy, and currency, but all using another country's single currency internationally."* A multi-currency system is the likely outcome but its adoption is not imminent.

Unperturbed by the views of the two eminent female leaders in, respectively, the academic and policy making field, **Mr. Thierry de Longuemar**, the Chief Financial Officer of the Asian Infrastructure Investment Bank (AIIB), defended his recommendation to the Board of the AIIB to use the IMF's 'Special Drawing Right (SDR)' as the operating currency of the Bank (The AIIB, just like the ADB, uses the Dollar as working currency; the African Development Bank, the Islamic Development Bank, and of course the IMF use the SDR.) *"But who is the controlling sovereign behind?"* asked Indrawati. *"It will not really untie from the USD"* said Subacchi, as the SDR is a basket of currencies with the USD the biggest constituent. That may be so, countered de Longuemar, but we have seen a recent first dilution of the USD weighting when the RMB was admitted into the SDR. He acknowledged nevertheless that for the SDR to become transactional, it should have a liquid capital market and also get used in commodity trade. The AIIB CFO ended the discussion with spice: *"Avoiding currency wars means having less national currencies, for national currencies are a weapon for countries to defend themselves and attack. That is why again I propose use of the SDR"*.

The inclusion of the Renminbi into the IMF's SDR, the Belt and Road Initiative, and the creation of the AIIB and the NDB, are all signs of China grinding its path onto co-governance of the global order. In particular the two new Multilateral Development Banks with their significant impact on the emerging markets ruffle up the established post-war institutional set-up. It is a paradox at a time of reversing globalisation, that the birth of new NDB's may lead to more multilateral cooperation. The AIIB's projects so far have all been co-financed by peers, incl. the ADB. In the ADB Governors' Session, the Canadian delegate encouraged the ADB *"to increasingly approach its operations in the context of multilateral development banks operating as a system. By working together and coordinating their interventions, MDBs have the potential to achieve a transformational development impact that is beyond the reach of a single institution"*.

The ADB may well do so, even if on its own the Bank is well funded to increase its commitments. It did so in 2017 for an amount of USD 20 billion. The ADB's outstanding loans now amount to USD 101 billion with supporting equity of USD 50.3 billion. External co-financing in 2017 generated USD 6 billion, about half of that through its Trade Finance Program. Large as these amounts may seem, they are a drip in the ocean compared to what is required. The ADB estimates that, taking into account the costs of climate change mitigation and adaptation, developing Asia needs to invest every year USD 1,700 billion. Furthermore, looking beyond the commitments to finance new projects, the annual report highlights that *"disbursements and co-financing fell short of the targets. Disbursements are essential to make a difference on the ground, while mobilising co-financing is critical to realising the Sustainable Development Goals"*.

Therefore, how to engage the private sector and make finance greener should be focus matters in the ADB's 2030 strategy, stress the Benelux countries in their statements to the Board. Belgium *"would like to see an elaboration on how the Private Sector Operations Department will operate, which instruments it will use and how it can show a bigger risk appetite and stronger focus on frontier markets"*[5] and repeated Belgium's suggestion to spin off the department. The ADB's governor for Luxembourg said that as 'sustainability' has become a global priority, his country can greatly contribute to the development of 'green finance': *"the Luxembourg Green Exchange provides issuers and investors with a regulatory and rules-based environment that guarantees that securities issued and listed are truly green, social and sustainable"*. [6]

The development of Asia, which the ADB during its 50 years of operations has helped make such a success, leaves the ADB with an ever more complex but exciting task. Half the world's citizens of middle and upper income countries are now Asian but, the ADB notes, "some areas of Asia are still home to the poorest of the poor". Juggling the priorities is just one of the considerations when finalising the 'Strategy 2030'.

[5] Full statement by Ronald De Swert, Alternate Governor, at https://www.adb.org/sites/default/files/page/419241/BELGIUM.PDF

[6] Full statement by Arsène Jacoby, Alternate Governor, at https://www.adb.org/sites/default/files/page/419241/LUXEMBOURG.pdf

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