Book

Declining labour share and the challenge of inclusion

Asia-Pacific
Economic Cooperation

Advancing Free Trade
for Asia-Pacific Prosperity

APEC Regional Trends Analysis

Declining Labour Share and the Challenge of Inclusion

APEC Policy Support Unit
November 2017

Prepared by:
Asia-Pacific Economic Cooperation Policy Support Unit
Asia-Pacific Economic Cooperation Secretariat
35 Heng Mui Keng Terrace
Singapore 119616
Tel: (65) 6891-9600 | Fax: (65) 6891-9690
Email: psugroup@apec.org Website: www.apec.org

Produced for:
APEC Ministerial Meeting
Asia-Pacific Economic Cooperation

APEC#217-SE-01.34

TABLE OF CONTENTS

LIST OF FIGURES

LIST OF TABLES

KEY ABBREVIATIONS

AEPR	APEC Economic Policy Report
ALMPs	Active labour market policies
ARTA	APEC Regional Trends Analysis
EC	Economic Committee (APEC)
FDI	Foreign direct investment
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
GFCF	Gross fixed capital formation
GVCs	Global value chains
HRDWG	Human Resources Development Working Group (APEC)
ICT	Information and communications technology
ILO	International Labour Organization
IMF	International Monetary Fund
MSME	Micro, small, and medium enterprises
OECD	Organisation for Economic Co-operation and Development
OPEC	Organization of the Petroleum Exporting Countries
PSU	Policy Support Unit (APEC)
RAASR	Renewed APEC Agenda for Structural Reform
ROW	Rest of the world
UNCTAD	United Nations Conference on Trade and Development
WB	World Bank
WEO	World Economic Outlook (IMF)
WTO	World Trade Organization

KEY MESSAGES

I. Declining Labour Share and the Challenge of Inclusion

- Share of labour compensation in GDP is an indicator of income distribution and inclusiveness. A falling labour share indicates that wages are not rising in step with rising productivity. It also indicates that workers are proportionally benefiting less from economic growth.

- Several studies have noted a downward trend in the labour share of GDP since the 1990s (e.g., ILO and OECD 2015; IMF 2017). Data analysis show that a similar pattern is happening in APEC: overall, the labour share in APEC exhibited a downward trend between 1995 and 2015, chiefly among industrialised APEC economies. Studies show that a falling labour share, along with rising inequality and a perception that the gains of economic growth have not been shared broadly, are contributing to a backlash against globalisation (IMF 2017).

- The story is more nuanced for developing APEC economies. Estimates of labour share focusing on formal sector employees show an increasing share of labour in GDP, which could be pointing to the expanded opportunities in formal sector employment that come with economic development. However, by imputing wages for self-employed workers to include those in informal sector employment, we find that labour share is declining in developing economies as well.

- Apart from domestic circumstances that can lead to falling labour shares (e.g., regressive fiscal policies and weak labour market regulations), studies point to two distinct but intertwined causes for the decline in labour share: (1) technological change and (2) globalisation.

- Technological change lowers the relative cost of accessing and utilising capital goods such as computers and machinery. This makes it easier for firms to automate certain tasks and lessen the demand for labour, particularly for routine jobs. This effect is generally more prominent in industrialised economies compared to developing economies. In addition, improved communication technologies make it easier to monitor and manage global value chains.

- While globalisation has brought many benefits and opened new opportunities, the development of global value chains has led to offshoring of some production activities to more competitive locations with lower cost. Globalisation also helps to facilitate access to capital and, hence, newer technologies.

- The intertwined impacts of technological change and globalisation can lead to skills mismatches and structural unemployment. The 2017 APEC Economic Policy Report (AEPR) on Structural Reform and Human Capital Development discussed this issue in the context of improving labour participation and adaptability. It found that in order to mitigate these impacts and make growth more inclusive, policies

that promote skills development and help affected workers gain access to new opportunities need to be implemented.

- Policy options to promote inclusiveness and reverse the trend of falling labour shares in GDP begin with improving access to and the quality of education and training, especially among disadvantaged groups and workers. This is the bedrock of any skills development and contributes to equalising opportunities for all workers, allowing them to access the new jobs created by technological change and globalisation.

- Economies can also implement active labour market policies (ALMPs) that ensure a timely, coordinated, and holistic approach to responding to skills gaps and mismatches while providing support and protection to workers. ALMPs cover various aspects of skills development, social protection, and employment, from training and apprenticeships and labour market information systems to unemployment benefits and job counselling. Coordinating these policies and activities is key to equitably distributing opportunities and ensuring inclusive growth while also promoting efficiency in the labour market.

- Regional cooperation plays a role in addressing the cross-border impacts of technological change and globalisation. Promoting people-to-people connectivity through cross-border training exchange, labour mobility, and regulatory coherence can help economies address skills mismatches and structural unemployment at a regional level. Sharing timely, accurate, and comparable labour market information, such as through the APEC Labour Market Portal,[1] can provide policymakers with a better picture of labour market challenges and opportunities in the region.

II. APEC Grows Faster amid Global Policy Uncertainty

- Economic growth and trade performance in the APEC region and the world have generally moved in tandem since APEC comprises almost 60 percent of global GDP and trade. However, since the 2008 Global Financial Crisis, the APEC region has grown at a relatively faster pace than the rest of the world. In 2016, the APEC region expanded by 3.4 percent, while the rest of the world grew by 2.9 percent.

- In H1 2017, the APEC region expanded at an average of 3.9 percent, higher than the 3.3 percent GDP growth reached in H1 2016. This expansion can be attributed to both favourable external developments, driven by a firmer global economic recovery, and domestic factors, particularly steady private consumption, relatively strong industrial production, and continued improvement in exports.

- The APEC region recorded a significant improvement in trade growth in terms of both the value and volume of merchandise exports and imports. During the period January-August 2017, the value of merchandise exports expanded at an average of 10.4 percent compared to a contraction of 6.6 percent in January-August 2016, while merchandise imports recorded a similar reversal. In H1 2017, growth in the

[1] Available at http://skillsmap.apec.org/.

volume of merchandise exports and imports grew by 10.6 percent and 8.4 percent, respectively, from their levels in the same period a year ago.

- In terms of investment, the APEC region attracted 53 percent of the world's foreign direct investment (FDI) in 2016, equivalent to USD 926.3 billion. The continued high level of FDI inflows into the region indicates investor optimism about the economic fundamentals and investment opportunities in the APEC region. However, the growth in FDI inflows slowed to 1.4 percent in 2016 from 21.9 percent in 2015, while FDI outflows at 4.1 percent outpaced FDI inflows in 2016.

- The APEC region accumulated around USD 342.8 billion worth of greenfield investments in 2016, equivalent to a 41.4 percent share of the world. Over the period 2003-2016, this is the second lowest APEC share of the world's greenfield investments aside from the 38.8 percent share recorded in 2008 amid the Global Financial Crisis.

- Between mid-October 2016 and mid-May 2017, the number of restrictive measures on trade and investment implemented by G20 APEC members outweighed the number of facilitating measures. Trade-restrictive measures comprised 59 percent of total trade and trade-related measures implemented during the reporting period, while investment-restrictive measures comprised 64 percent.

- The economic outlook for the short-term indicates a surge in APEC GDP growth to 3.9 percent in 2017 from 3.4 percent growth in 2016, outpacing the world economy at 3.6 percent and the rest of the world (ROW) at 3.2 percent. In 2018, the APEC region is projected to continue to outpace the global economy and the ROW at 3.8 percent, before aligning with the world economy in 2019 and 2020.

- Short-term risks are broadly balanced. Downside risks relate mostly to policy uncertainty which could take a toll on consumer and business confidence, pulling domestic spending and demand downwards, effectively halting the current momentum in global economic activity. The upside potential for growth could come from continued strength in global economic activity, which is expected to further boost consumer and business spending as well as provide much needed support to trade and investment activities.

- In the medium-term, risks remain tilted to the downside as uncertainty over the future direction of monetary, fiscal, and trade policies continues to be a crucial determinant of growth going forward. For example, an unexpected magnitude in monetary policy tightening in some developed economies could result in tightened global financial conditions and unmanageable debt levels which could leave some economies vulnerable, while fiscal policy measures that do not support growth could also hold back global economic expansion. Moreover, inward shifts towards protectionist policies could discourage trade and investment, giving pause to the ongoing economic momentum.

- The current period of relatively high growth, which is expected to be sustained into 2020, leaves adequate room for APEC economies to continue along the path of reform. Thus, the APEC region could focus on improving the ease of doing business, implementing structural reforms as embodied in their Renewed APEC

Agenda for Structural Reform (RAASR) individual action plans, and exerting all efforts to achieve the 1994 Bogor Goals of free and open trade and investment by 2020.

- APEC could also exert efforts to ensure that the benefits of free trade and investment are not only measurable, but that those benefits also reach all sectors of society throughout the region, particularly among women, youth, the disabled, and the poor.

1 DECLINING LABOUR SHARE AND THE CHALLENGE OF INCLUSION[2]

1.1 INTRODUCTION

"A rising tide lifts all boats," says the oft-repeated aphorism on the economy. Its appeal comes from its apparentness: just as everything floating in the water will be lifted by the rising tide, so will everyone benefit from economic growth. The image portrayed is also very equitable: if the tide rises half a metre, then all boats lift half a metre and no boat is left behind. Increasingly, however, the assumption that everyone benefits equitably from economic growth, as well as the various policy choices meant to encourage this growth, is being challenged. Who benefits from economic growth and the resulting expansion in incomes, and by how much, is an increasingly important question.

Economic accounting defines an economy's total income as a mirror image of its output: income is the compensation for output (e.g., production of a good or provision of a service) and are therefore two sides of the same coin. This is because total output, measured as gross domestic product (GDP), is the outcome of two broad inputs: (1) labour, which is contributed by workers and compensated through wage income, and (2) capital, which is contributed by owners of capital (e.g., investors, stockholders) and compensated through profits, interest income, dividends, or capital gains.[3] Thus, the sum of workers' wages and capital owners' returns should equal GDP (i.e., the income approach to calculating GDP). The total share of GDP that is paid out to workers as wages is termed the labour share (or wage share) and, by definition, the remainder is the capital share that accrues to the owners of capital.

Since the majority of people in a society are workers and not capital owners,[4] the labour share is often considered as an indicator of distribution of income and inclusiveness of economic growth: a higher share means proportionally more income is accruing to workers and their households. Labour shares in many economies had been stable throughout the second half of the last century (Schneider 2011). This is because real wages have generally grown in step with labour productivity;[5] thus, spending on capital goods like machinery, if it enhances labour productivity, will still contribute to rising real wages for workers. However, this condition can only hold in a situation where exogenous factors such as technology, fiscal policy, or savings rates are fairly constant.

---

[2] Prepared by Emmanuel A. San Andres, Andre Wirjo, and Satvinderjit Kaur Singh, APEC Policy Support Unit (PSU). The authors would like to thank Cyrille Schwellnus, Senior Economist, OECD, for contributing Box 1.1 in this report and for his inputs in calculating adjusted labour share. Research assistance from Kathrina G. Gonzales is gratefully acknowledged.

[3] A third factor, land, which is owned by landowners and compensated through rental income or capital gains, is often lumped with capital in economic accounting.

[4] Note that it is possible for an individual to be both a worker and owner of capital (e.g., a wage earner who invests savings in the stock market). That said, studies have shown that ownership of capital is inversely related with household income even in economies with well-developed and accessible capital markets (e.g., see Gallup's 2017 survey on stock ownership in the United States: http://news.gallup.com/poll/211052/stock-ownership-down-among-older-higher-income.aspx).

[5] Neoclassical wage theory posits that, in a competitive market, the real wage rate will equal marginal productivity of labour in equilibrium. This implies that, on average, wage growth should be in tandem with labour productivity growth.

Several studies have noted the decline of labour shares in recent years (e.g., IMF 2017; ILO and OECD 2015). A falling labour share indicates increasing income inequality: low-skilled workers bear most of the brunt of lower wages while middle-skilled occupations also experience a decline in real earnings. Meanwhile, a lower labour share translates to a higher capital share and, since the majority of capital owners belong to the top income distribution bracket, a higher compensation to capital often leads to rising income inequality (IMF 2017). Higher income inequality can lead to significant social costs, misallocation of resources and efforts, and lower growth (Dabla-Norris et al. 2015). A falling labour share also indicates slower wage growth compared with the growth of labour productivity (see Box 1.1), which has implications on the ability of markets to fairly compensate workers for their productivity. This decline in labour share, rising inequality, and a perception that the gains of economic growth have not been shared equally has contributed to increasing hostility towards economic integration and shifting preferences towards more inward-looking policies (IMF 2017).

Studies focusing on advanced economies have noted the accelerated advancement of technology and globalisation as the primary causes of declining labour shares. Technological advancement has lowered costs of capital and enabled the replacement of labour through greater automation, causing a decline in wage costs and hence labour share. On the other hand, globalisation has promoted greater competition, encouraging firms to outsource and relocate production. Greater options to save costs and access to global value chains have increased firms' bargaining power and reduced workers' ability to negotiate higher wages (IMF 2017).

The next section of the report examines trends in labour share in APEC economies, finding that there is a general downward trend starting from the mid-1990s. It then discusses some of the reasons behind this trend and focuses on two phenomena that may be driving these global patterns: technological change and globalisation. Box 1.1 of the report, contributed by the OECD, examines the decoupling of real wage growth from labour productivity growth in selected APEC economies. The report concludes with some policy options that could promote inclusive growth and support workers affected by economic changes.

1.2 LABOUR SHARE IN APEC ECONOMIES

Measuring labour share, while theoretically simple, is not straightforward in practical terms (see, for example, Krueger 1999 and Schneider 2011). Getting the sum of wages paid to workers requires a definition of who is a worker and what is a wage—definitions that could be the subject of debate. While wages paid to employed workers are straightforward enough to measure and account for, wages accruing to self-employed workers are more difficult to measure. There is also a debate on whether self-employed workers—such as doctors, lawyers, taxi drivers, and food hawkers—are to be considered workers and their income considered wages.

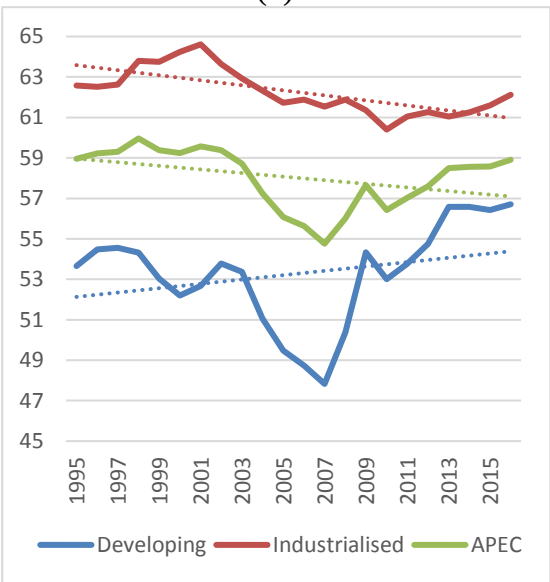
Figure 1.1 shows calculations of labour share using two different sources: (1) The Conference Board's Total Economy Database that harmonises various economy-level sources of data and (2) consolidated GDP, compensation, and employment data from various sources. In both sources only formal sector employees and the wages they receive are considered under labour share. Data for 1995-2015 show that there is a downward trend

in labour share of income in APEC as a whole: this finding holds regardless of data source and measurement method, although there are differences in magnitude.[6]

The data also reveal that the trends for industrialised and developing APEC economies are different.[7] While industrialised economies show a downward trend in labour share, developing economies exhibit an upward trend albeit starting from a lower percentage. Given that labour share in this case considers only those employees in the formal sector, this could point to increased formal sector opportunities for workers in developing APEC economies—a reflection of the economic development in recent decades. On the other hand, the falling share in industrialised economies echoes the observations of previously mentioned studies that focus on the trends in advanced and high-income economies (e.g., G20 or OECD economies).

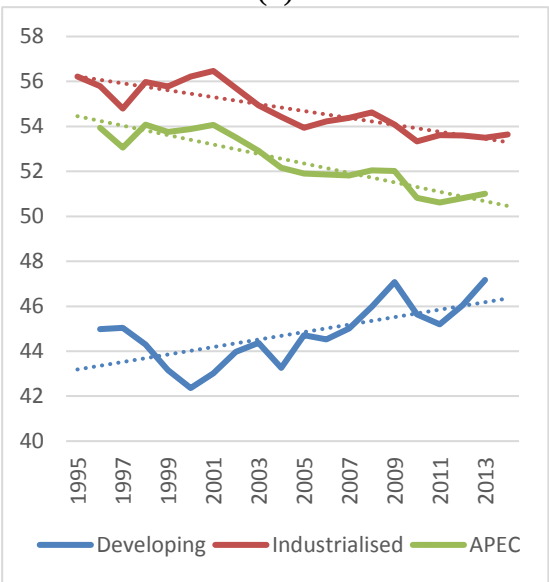
Figure 1.1 Labour share in APEC, 1995-2015 (% of GDP)

(1)



Note: Aggregates are weighted by GDP. Data are not available for Brunei Darussalam and Papua New Guinea. Dotted lines are trendlines.
Source: The Conference Board Total Economy Database and PSU staff calculations.

(2)



Note: Aggregates are weighted by GDP. Compensation data are not available for Indonesia and Viet Nam. Dotted lines are trendlines.
Source: OECD, UN, World Bank, economy sources, and PSU staff calculations.

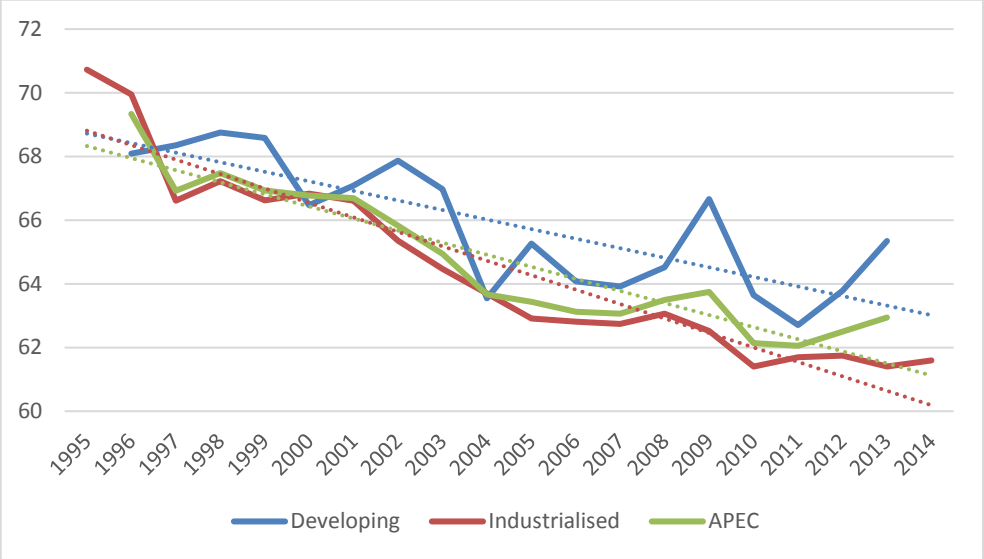
Given the large size of the informal sector in many developing economies, there is a need to take a broader view of workers' compensation to account for workers not in formal employment. To do this, we use ILO employment data to obtain the number of employees and self-employed workers in each economy. Ideally, we would use micro-level data from labour force surveys to calculate income accruing to self-employed workers. However, due to various constraints, we utilise national accounts data on compensation of employees to impute average wages for self-employed workers. We assume that self-employed workers

[6] This is based on analysis of aggregate APEC data. Analysis by OECD (2012) and IMF (2017) have shown that the trend in labour share of income varies depending on the economy, sector and skill level of workers.
[7] Industrialised APEC economies are Australia; Canada; Japan; New Zealand; and the United States. Developing APEC economies are all other APEC economies not classified as industrialised.

receive the same average wage as employees and add their imputed wages to the data on compensation of employees to obtain total labour compensation in an economy.[8]

Figure 1.2 shows labour shares that have been adjusted to include imputed wages for self-employed workers. As can be seen, labour shares of GDP are higher than those shown in the previous figure due to the addition of wage income for these workers. The increase is quite significant in developing economies—despite increasing opportunities in the formal sector, a significant proportion of workers in developing economies still work in the informal sector. Hence, imputing wages for self-employed workers can give a clearer picture of labour share in developing economies.

Figure 1.2 Adjusted labour share in APEC, 1995-2014 (% of GDP)



Note: Aggregates are weighted by GDP. Compensation data are not available for Indonesia and Viet Nam. Dotted lines are trendlines.
Source: ILO, OECD, UN, WB, economy sources, and PSU staff calculations.

Adjusting labour share to account for self-employed workers also gives a more nuanced picture of the trends. As Figure 1.2 illustrates, developing APEC economies now exhibit a trend of declining labour share, which is similar to the trend in industrialised economies. While this trend is more apparent and accelerated in industrialised economies, developing economies are not immune to declining labour shares of GDP. As noted in IMF (2017), the recent decline in labour share shows signs of being a global phenomenon with global causes.

1.3 CAUSES OF FALLING LABOUR SHARE

The causes of the declining labour share of income are complex and multi-layered. Domestic policies and regulations, first and foremost, can have a significant impact on the labour share and inclusive growth. For example, a reduction in corporate income tax rates is likely to increase the relative return to capital and encourage firms to replace labour with

[8] Computationally, we multiply the compensation of employees from national accounts data by the ratio (Employees + Self-employed)/(Employees). Note that income for self-employed workers varies from highly paid professionals like doctors, lawyers, and architects to subsistence earners like food hawkers, street sellers, and day labourers. Similarly, wages for employees covers compensation for bank presidents and engineers as well as for doormen and janitors.

more capital (IMF 2017). Privatisation of firms in certain sectors, especially network industries such as energy and communications, has also led to a declining labour share (OECD 2012). In addition, labour market regulations could result in either an increase or decrease in the labour share of income.[9] For instance, allowing for greater coverage of collective bargaining agreements or strengthening employment protection legislation can raise labour income shares. On the other hand, if such regulations become too strict or onerous, it may lead to firms deciding to employ less labour, substituting labour with more capital and causing labour income shares to decline instead.

However, domestic characteristics are not the only cause of falling labour shares in an economy. Studies have shown that this decline is being experienced by both developed and developing economies. This indicates that aside from domestic factors that may be causing the decline, there may also be underlying reasons that are more global in nature.

Two main causes of falling labour shares have been identified in the literature: technological change and globalisation (e.g., Autor et al. 2017; ILO and OECD 2015; IMF 2017). Although technological change and globalisation are distinct and separate causes, they are intertwined and tend to reinforce one another. For example, improvements in technology have lowered ICT and logistics costs and, in doing so, help to facilitate globalisation. Likewise, globalisation has made it easier for technology and knowledge to be transferred from one economy to another.

Technological change

Technology, particularly digital technology, has improved by leaps and bounds in recent decades. Technological advancements have not only made machines, robots, and computers more effective in performing tasks, enhanced production methods (and global value chains) have also made them more affordable. Consequently, the relative cost of accessing production capital has fallen to the point that it is often more efficient for firms to automate certain tasks (i.e., replace labour with machines), particularly routine ones (OECD 2012; Driver and Muñoz-Bugarin 2010; Karabarbounis and Neiman 2013). This degree of substitution is high enough that despite the lower cost of capital, labour share of income can still decline.

Analysis conducted by IMF (2017) which looked at changes in labour shares over the long term (i.e., focusing on economies that have at least 10 years of data between 1991 and 2014) showed that technological advancement along with "routinisation" (i.e., the ability to automate certain job tasks) are the largest contributors to the declining labour income shares in developed economies[10]. They found that economies with high exposure to routinisation were shown to have approximately four times more decline in labour income share than those with low exposure, for a given change in the relative cost of accessing investment goods. Specifically, for a 15 percent decrease in the relative price of investment

[9] Labour market regulations cover a wide range of labour market institutions, such as the unemployment benefit system and labour unions, as well as various aspects of labour legislation, such as statutory minimum wage rates and employment protection legislation.

[10] IMF indicated two main reasons for looking at long-term changes: 1) changes caused by technological improvements take some time to be observed, and 2) it minimises the probability that observed changes are contributed by cyclical or temporary occurrences. Technology improvements and hence firms' incentive to substitute labour with capital were proxied by the change in the relative price of investment to consumption goods, while routine task intensity was used as a measure of the initial exposure to routinisation of a task (i.e., its ease of being automated).

goods, labour share in an economy with high initial exposure to routinisation decreased by 1.5 percentage points, while that of an economy with low initial exposure decreased by 0.4 percentage points. Examples of sectors with high exposure to routinisation include manufacturing, mining and quarrying, and transportation.

The effect of technological change on declining labour income shares is also observed in developing economies, in part due to the falling price-performance ratio[11] of new technologies. The increasing efficiency and cost-effectiveness of new technologies could tilt production capital-labour ratios in favour of capital even in labour-abundant developing economies. Substitutability between capital and labour, which will be further elaborated below, could also lead to a significant decline in labour income shares in developing economies.

Globalisation

The benefits of globalisation are well-cited (e.g., Fajgelbaum and Khandelwal 2014; Wacziarg and Welch 2003). Besides enabling access to a greater variety of goods and services, trade and financial integration have been shown to promote convergence, raise incomes, and contribute to poverty reduction.

At the same time, however, globalisation through participation in global value chains (GVCs) has led to more imports and offshoring (Amiti and Wei 2005; Hummels et al. 2011), activities which have been associated with job losses, particularly at the middle-skill level. In the case of developed economies, competition from imports makes it imperative that lower-skill, labour-intensive stages of production are relocated to developing economies where wages are relatively cheaper. Imports also lead to access to cheaper capital goods (e.g., machines and computers), making labour relatively more expensive and hence encouraging firms to automate. Essentially, by facilitating factor reallocation (or the threat of doing so), globalisation has lowered the bargaining power for labour to negotiate for higher wages (Harrison 2005).

Given the differences in factor endowments between developed and developing economies (i.e., developed economies are capital-abundant, while developing economies are labour-abundant), participation in GVCs should lead to an increase in labour shares of income in developing economies. The reality is, however, quite different from the theory. At the heart of the issue is the substitutability between capital and labour. If capital cannot be easily replaced by labour for the offshored tasks from developed to developing economies, then it is possible that the receiving developing economy would experience a declining labour share of income.[12]

[11] Price-performance ratio refers to the ability of an equipment to perform a task given its price. A lower ratio means greater performance at a lower price (i.e., higher cost-efficiency).

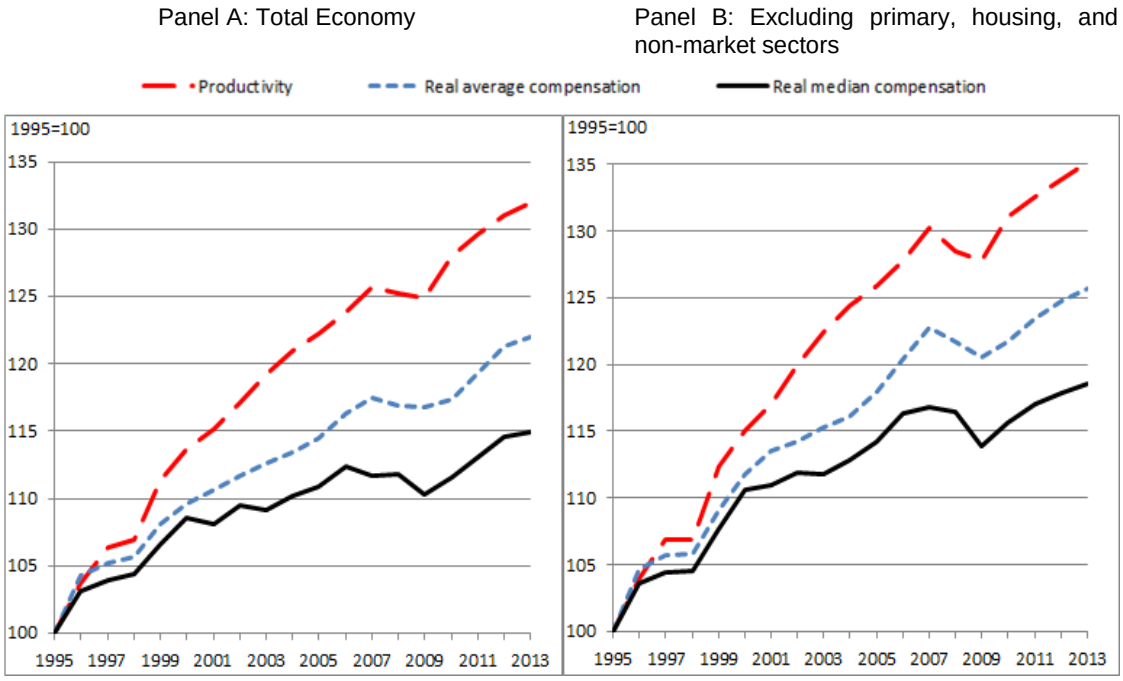
[12] One way to understand this is that labour-intensive activities in developed economies are still capital-intensive relative to existing tasks in the receiving developing economies (Cho 2016).

Box 1.1 Decoupling of real median wages from productivity: Evidence from covered APEC economies*

In the long run, raising productivity is the only way to raise living standards, with real wages being the most direct mechanism through which the benefits of productivity growth are transmitted to workers. Over the past two decades, however, aggregate labour productivity growth in a number of APEC economies has decoupled from real median compensation growth. Raising productivity no longer appears to be sufficient to raise real wages for the typical worker, suggesting that there is a role for public policies to support a broader sharing of the benefits of productivity gains in the economy.

In the covered APEC economies as a whole, there has been significant decoupling of real median wages from productivity over the past two decades as real median wages have grown at a lower average rate than labour productivity (Figure B1.1.1). Both in the total economy and in a narrower aggregate excluding the primary, housing and non-market sectors, median compensation would have been around 13 percent higher than observed in 2013 if it had perfectly tracked labour productivity since 1995.

Figure B1.1.1 Macro-level decoupling in covered APEC economies, 1995-2013



Note: Unweighted average of Australia; Canada; Japan; Korea; New Zealand; and the United States. 1995-2013 for Japan and Korea; 1995-2012 for Australia; 1997-2012 for Canada and New Zealand; 1997-2013 for the United States. In Panel A, all series are deflated by the total economy value added price index. In Panel B, all series are deflated by the value added price index excluding the primary, housing and non-market sectors. The sectors excluded in panel B are the following (ISIC rev. 4 classification): (1) Agriculture, Forestry and Fishing; (2) Mining and quarrying; (3) Real estate activities; (4) Public administration and defence, compulsory social security; (5) Education; (6) Human health and social work activities; (7) Activities of households as employers; and (8) Activities of extraterritorial organisations and bodies.

Source: OECD National Accounts Database, OECD Earnings Database, and OECD staff calculations.

The decoupling of real median wages from labour productivity for the covered APEC economies as a whole reflects both declines in labour shares (decoupling of average compensation from productivity) and increases in wage inequality (decoupling of median compensation from average compensation). In line with previous studies on decoupling (Bivens and Mishel 2015; Uguccioni and Sharpe 2017), this box uses as a starting point compensation and value added in the total economy. The total economy includes sectors for which labour shares are largely determined by fluctuations in commodity and asset prices, such as the primary and housing sectors, or for which labour shares are driven by imputation choices, such as the non-market sector. Labour share fluctuations in these sectors may have different distributional implications from those in the production sector. However, both measures of decoupling suggest that the contributions of declines in labour shares and increases in wage inequality to overall decoupling have been approximately equal.

While real median wages have decoupled from labour productivity in the covered APEC economies as a whole, there have been large cross-economy differences, both in the extent of decoupling and the relative contributions of labour shares and wage inequality. All but one of the covered APEC economies have experienced significant decoupling, with the annual growth differential between real median compensation and labour productivity ranging from -½ to -1.5 percentage point. In the covered Asian APEC economies, decoupling mainly reflects declines in labour shares whereas increases in wage inequality have played a significant role in the remaining economies.

[*] This box was contributed by Cyrille Schwellnus, Senior Economist, OECD. It is based on Schwellnus et al. (2017) and covers Australia; Canada; Japan; Korea; New Zealand; and the United States.

1.4 POLICY IMPLICATIONS AND THE ROLE OF APEC

An important link between technological change and globalisation, on one hand, and declining labour shares and rising inequality, on the other, is structural unemployment.[13] While structural unemployment has many causes, technological change and globalisation contribute to skills mismatches and economic realignments that can displace workers in affected sectors. Not only does this lead to declining labour shares and greater inequality, but it is also economically inefficient to have workers unemployed or underemployed while new opportunities from technological change (e.g., the digital economy) and continued globalisation are opening up.

In 2017, the Economic Committee (EC) published its APEC Economic Policy Report (AEPR) on Structural Reform and Human Capital Development, which discussed policy responses to the challenges of structural unemployment due to technological change and globalisation. While many policy responses to these challenges are domestic and unilateral in nature, the AEPR explored opportunities for regional cooperation in addressing skills mismatches and structural unemployment in APEC, particularly for EC and the APEC Human Resources Development Working Group (HRDWG).

[13] Structural unemployment is defined as unemployment caused by fundamental changes in an economy, such as shifting demand patterns (e.g., due to globalisation, capital accumulation, urbanisation, or affluence) or changes in technology, leading to a mismatch between the skills of workers looking for work and the skills required by job opportunities.

Promoting inclusiveness and reversing the trend of declining labour shares of GDP begins with improving access to and the quality of education and training, especially among disadvantaged groups and workers. Primary and secondary education is the bedrock of any future skills development and contributes to equalising opportunities for all workers and allows them to access the new jobs created by technological change and globalisation.

In order to assist workers displaced by various economic forces, economies need to implement active labour market policies (ALMPs) that ensure a timely, coordinated, and holistic approach to responding to skills gaps and mismatches while providing support and protection to workers. ALMPs cover various aspects of skills development, social protection, and employment. These include policies and programmes on skills training and apprenticeships, gathering and disseminating labour market information, providing unemployment benefits, and job counselling (Figure 1.3). Coordinating these policies and activities is crucial to equitably distributing opportunities and ensuring inclusive growth while assisting displaced workers and promoting efficiency in the labour market.

Figure 1.3 Active Labour Market Policies

Source: APEC Economic Policy Report 2017 Factsheet.

Key to developing well-coordinated ALMPs is gathering, analysing, and utilising accurate and timely labour market information. Most economies already gather supply-side data from workers and households through regular labour force surveys covering information on employment status, occupation, and educational attainment. APEC economies could initiate regular efforts to gather demand-side data from employers to inform on job vacancies and redundancies as well as skills needs and hiring expectations. It is also important to develop skills definitions and certification mechanisms to help workers and employers better understand what skills are needed and available in the market. These

definitions and certifications can also be important inputs in the development of responsive curricula and pedagogies and are crucial inputs for retraining and employment counselling.

Social protection and safety net programmes contribute to providing assistance and security to workers and households. If designed as part of a set of coordinated ALMPs, they can also help unemployed workers find appropriate jobs and provide them with opportunities for skills development. Where appropriate, linking social protection (e.g., unemployment benefits) with job search or skills training efforts could help workers adapt to the impacts of technological change and globalisation while minimising skills gaps and mismatches in the labour market. Agencies that distribute social protection benefits could work in tandem with employment centres to help match unemployed workers with potential employers as well as disseminate opportunities for skills retraining or apprenticeships.

Regional cooperation also plays a role in addressing the cross-border impacts of technological change and globalisation. The 2017 AEPR lists several activities and opportunities for APEC to work on these issues, particularly for EC and HRDWG. For example, promoting people-to-people connectivity through cross-border training exchange, labour mobility, and regulatory coherence can help economies address skills mismatches and structural unemployment at a regional level. Likewise, sharing timely, accurate, and comparable labour market information, such as through the APEC Labour Market Portal,[14] can provide policymakers with a better picture of labour market challenges in the region and potential opportunities for cooperation.

[14] Available at http://skillsmap.apec.org/.

1.5 REFERENCES

Amiti, M. and S.J. Wei. 2005. "Service Offshoring, Productivity, and Employment: Evidence from the United States", IMF Working Paper WP/05/238, International Monetary Fund, Washington, DC.

Autor, D., D. Dorn, L.F. Katz, C. Patterson, and J. Van Reenen. 2017. "The Fall of Labor Share and the Rise of Superstar Firms", NBER Working Paper No. 23396, National Bureau of Economic Research NBER, Cambridge, MA.

Berg, A.G. and J.D. Ostry. 2011. "Inequality and Unsustainable Growth: Two Sides of the Same Coin?", IMF Staff Discussion Note 11/08, International Monetary Fund, Washington, DC.

Bivens J. and L. Mishel. 2015. "Understanding the Historic Divergence Between Productivity and a Typical Worker's Pay", EPI Briefing Papers No. 406, Economic Policy Institute, Washington, DC.

Cho, I. 2016. "Offshoring and Labour Share in Manufacturing Industries in Developed Countries", Job Market Paper, University of California, Davis.

Dabla-Norris, E., K. Kochhar, N. Suphaphiphat, F. Ricka, and E. Tsounta. 2015. "*Causes and Consequences of Income Inequality: A Global Perspective*", Washington, D.C.: International Monetary Fund.

Driver, C. and J. Muñoz-Bugarin. 2010. "Capital Investment and Unemployment in Europe: Neutrality or not?", *Journal of Macroeconomics*, Vol. 32 (1), 492-496.

Fajgelbaum, P.D. and A.K. Khandelwal. 2014. "Measuring the Unequal Gains from Trade", NBER Working Paper No. 20331, National Bureau of Economic Research, Cambridge, MA.

Harrison, A. 2005. "Has Globalization Eroded Labor's Share? Some Cross-Country Evidence", Munich Personal RePEc Archive Paper No. 39649, University of California, Berkeley.

Hummels, D., R. Jørgensen, J.R. Munch and C. Xiang. 2011. "The Wage Effects of Offshoring: Evidence from Danish Matched Worker-Firm Data", NBER Working Paper No. 17496, National Bureau of Economic Research, Cambridge, MA.

ILO and OECD. 2015. "The Labour Share in G20 Economies", G20 Employment Working Group, Antalya, Turkey, 26-27 February 2015.

IMF. 2017. "Understanding the Downward Trend in Labour Income Shares", Chapter 3 in *World Economic Outlook April 2017*, Washington, DC.

Karabarbounis, L. and B. Neiman. 2013. "The Global Decline of the Labour Share", NBER Working Paper No. 19136, National Bureau of Economic Research, Cambridge, MA.

Krueger, A. 1999. “Measuring Labor’s Share”, NBER Working Paper No. 7006, National Bureau of Economic Research, Cambridge, MA.

OECD. 2012. “Labour Losing to Capital: What Explains the Declining Labour Share?”, Chapter 3 in *OECD Employment Outlook*, Paris.

Schneider, D. 2011. “The Labor Share: A Review of Theory and Evidence”, Collaborative Research Center 649, SFB 649 Discussion Paper 2011-069, Humboldt University of Berlin.

Schwellnus, C., A. Kappeler, P.A. Pionnier. 2017. “The Decoupling of Median Wages from Productivity in OECD Countries”, International Productivity Monitor 32.

Uguccioni J. and A. Sharpe. 2017. “Decomposing the Productivity-Wage Nexus in Selected OECD Countries, 1986-2013”, International Productivity Monitor 32.

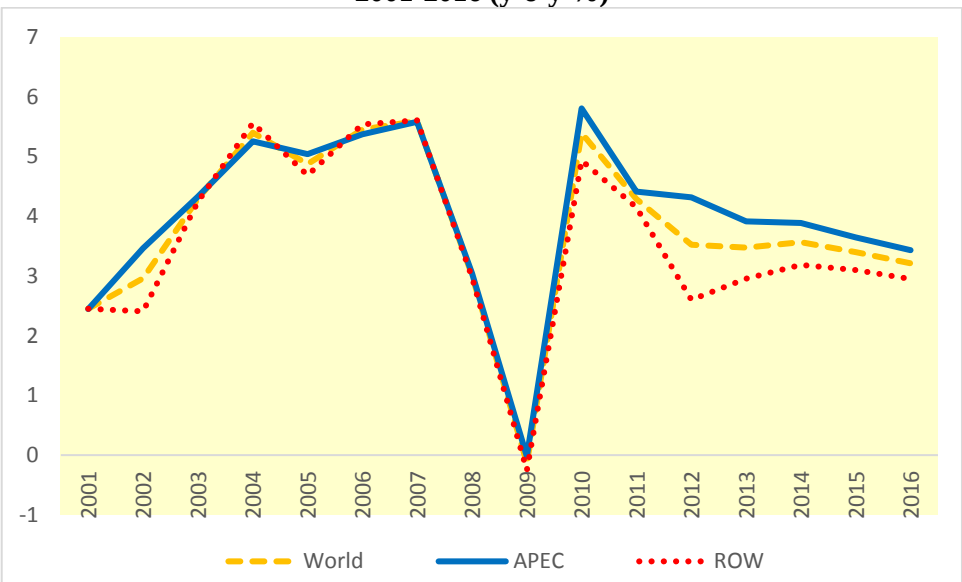
Wacziarg, R. and K.H. Welch. 2003. “Trade Liberalization and Growth: New Evidence”, NBER Working Paper No. 10152, National Bureau of Economic Research, Cambridge, MA.

2 APEC GROWS FASTER AMID GLOBAL POLICY UNCERTAINTY[15]

2.1 APEC GDP GROWTH

Growth in the APEC region generally moves in tandem with world growth since APEC comprises about 60 percent of world GDP. Up until the 2008 Global Financial Crisis (GFC), the GDP growth of APEC and the rest of the world (ROW) tracked a similar path (Figure 2.1). However, as global economic activity began to recover following the GFC, the APEC region has grown at a relatively faster pace than the rest of the world, marked by significant improvements in trade and industrial production.

Figure 2.1 Real GDP Growth: World, APEC, and Rest of the World (ROW) 2001-2016 (y-o-y %)

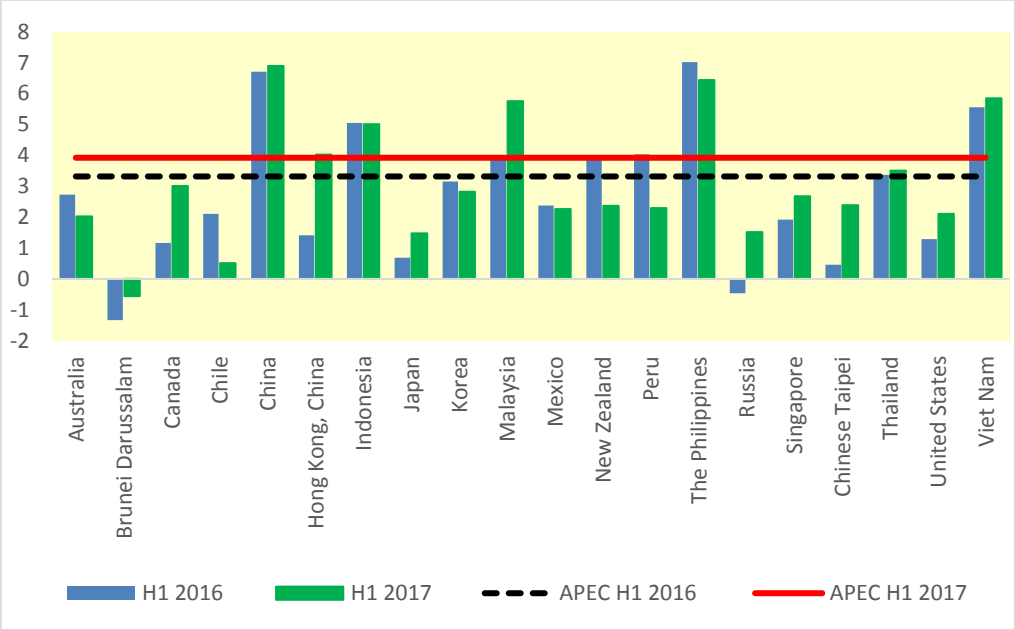


Source: IMF World Economic Outlook (WEO) Database (October 2017) and PSU staff calculations.

The combined effect of a firmer global economic recovery, robust domestic consumption, and generally strong industrial production boosted APEC's overall GDP growth in the first half of 2017. During H1 2017, the APEC region expanded at an average of 3.9 percent, higher than the 3.3 percent GDP growth reached in H1 2016 (Figure 2.2). This expansion can be attributed to both external developments and domestic factors. With the global economy on a more solid footing, global demand also strengthened, resulting in a firmer pick-up in trade and manufacturing, as well as a more upbeat sentiment which has buoyed consumer and business spending.

[15] Prepared by Rhea C. Hernando, APEC Policy Support Unit (PSU).

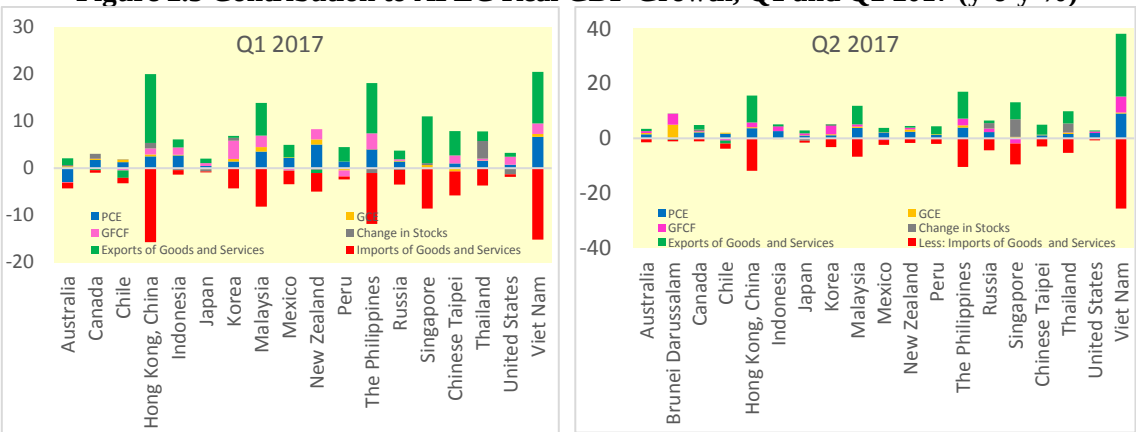
Figure 2.2 APEC Real GDP Growth, H1 2016 and H1 2017 (y-o-y %)



Note: Quarterly data are not available for Papua New Guinea.
Source: Economy sources; *The Economist* Economic and Financial Indicators; IMF WEO Database (October 2017); and PSU staff calculations.

Private consumption expenditures remained as the major contributor to growth among APEC economies (Figure 2.3). It is worthwhile to note that exports have continued their recovery in line with strengthening global demand, thereby contributing positively to GDP growth. The contribution from gross fixed capital formation (GFCF), a measure of the value of new acquisitions or existing fixed assets intended for production use, was also generally positive across APEC economies. Meanwhile, government consumption continued to contribute to APEC growth, although in a more subdued manner compared to private consumption and GFCF.

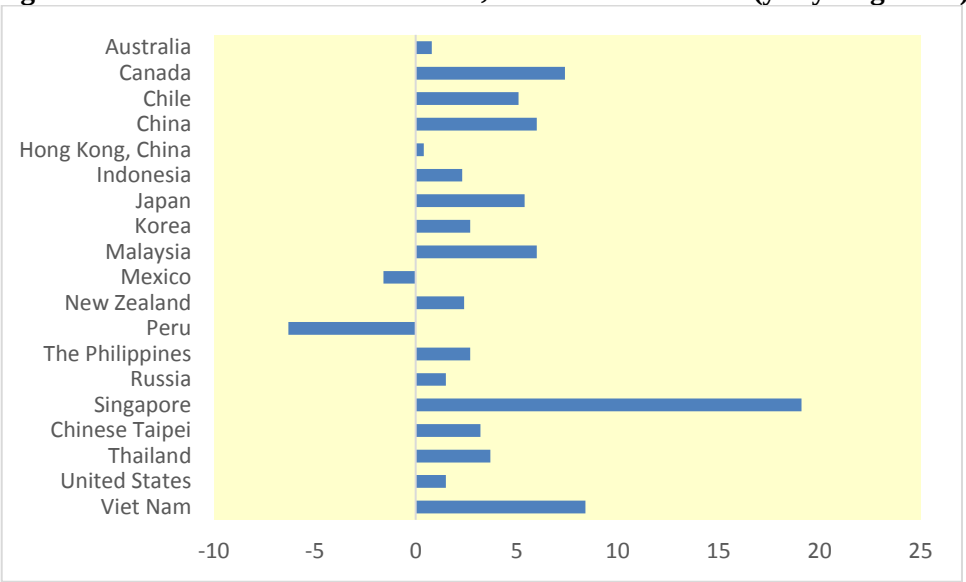
Figure 2.3 Contribution to APEC Real GDP Growth, Q1 and Q2 2017 (y-o-y %)



Legend: PCE = private consumption expenditure; GCE = government consumption expenditure; and GFCF = gross fixed capital formation.
Note: Breakdown of contribution to GDP growth is not available for Brunei Darussalam; China and Papua New Guinea for Q1 2017; and China and Papua New Guinea for Q2 2017.
A missing bar denotes an almost nil to nil contribution to GDP growth.
Source: Economy sources and PSU staff calculations.

Industrial production in the region was also relatively strong as the overall output growth of industrial sectors was positive for most APEC economies (Figure 2.4), except for Peru and Mexico which contracted due to a slowdown in their mining sectors. The high growth exhibited by Singapore is notable, attributed to a year-on-year increase in almost all manufacturing clusters, led by the electronics cluster (38.7 percent), followed by biomedical manufacturing (25.1 percent), and precision engineering (10.7 percent).

Figure 2.4 Industrial Production Index, latest available data (y-o-y % growth)



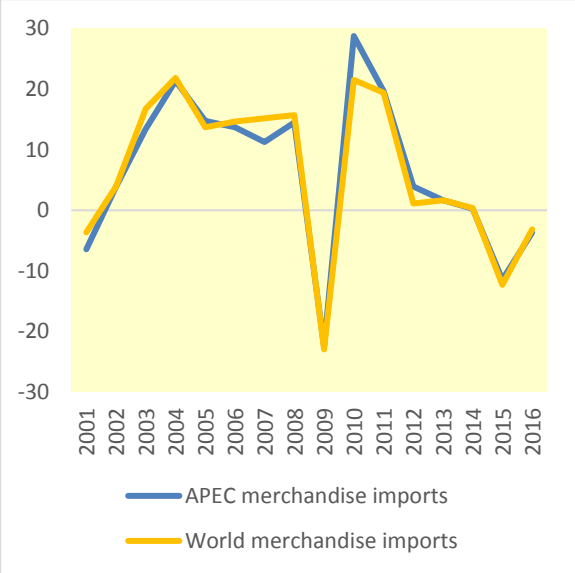
Note: Data for August 2017 include Chile; China; Indonesia; Japan; Korea; The Philippines; Russia; Singapore; Chinese Taipei; Thailand; United States; and Viet Nam. Data for July 2017 include Canada; Malaysia; Mexico; and Peru. Data for Q2 2017 include Australia; Hong Kong, China; and New Zealand. Data for Brunei Darussalam and Papua New Guinea are not available.
Source: *The Economist* Economic and Financial Indicators, accessed 17 October 2017.

2.2 TRADE PERFORMANCE

The ongoing global cyclical recovery is also reflected in the upturn in merchandise trade across economies. A comparison of APEC trade growth vis-à-vis world trade growth reveals synchronized peaks and troughs for the years 2001-2016 for both exports and imports (Figures 2.5 and 2.6), reflecting APEC's 54 percent share in world trade (Table 2.1).

Figure 2.5 APEC and World Exports 2001-2016 (y-o-y %)

Figure 2.6 APEC and World Imports 2001-2016 (y-o-y %)



Source: UNCTADstat online database.

Table 2.1 APEC Merchandise Trade Value and Growth

	Value (billion USD)			Growth (y-o-y %)	
	Jan-Aug 2015	Jan-Aug 2016	Jan-Aug 2017	Jan-Aug 2016	Jan-Aug 2017
Merchandise Exports					
World	10,073.0	9,627.0	10,491.0	-4.4	9.0
APEC	5,492.2	5,127.9	5,663.5	-6.6	10.4
Rest of the World (ROW)	4,580.8	4,499.1	4,827.5	-1.8	7.3
Merchandise Imports					
World	10,222.0	9,752.0	10,722.0	-4.6	9.9
APEC	5,515.0	5,154.1	5,765.5	-6.5	11.9
ROW	4,707.0	4,597.9	4,956.5	-2.3	7.8
APEC's share of the World (%)					
Merchandise Exports	54.5	53.3	54.0		
Merchandise Imports	54.0	52.9	53.8		

Source: UNCTADstat online database.

Latest available data show that the APEC region recorded a significant improvement in trade growth, in terms of both the value and volume of merchandise exports and imports. During the period January-August 2017, the value of merchandise exports in the APEC region expanded at an average of 10.4 percent compared to a contraction of 6.6 percent in January-August 2016 (Figure 2.7). The same positive reversal is also observed for merchandise imports. In H1 2017, growth in the volume of merchandise exports and imports grew by 10.6 percent and 8.4 percent, respectively, up from 3.2 percent and 0.9 percent in the same semester a year ago (Figure 2.8).

Figure 2.7 APEC Trade Value, Jan-Aug 2016 and Jan-Aug 2017 (y-o-y % growth)

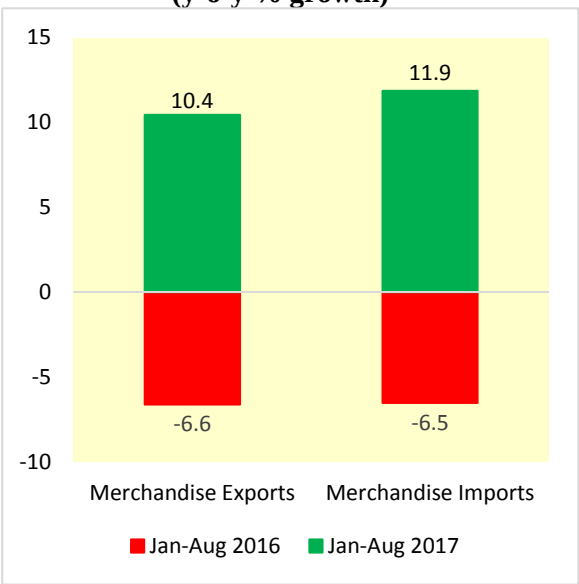
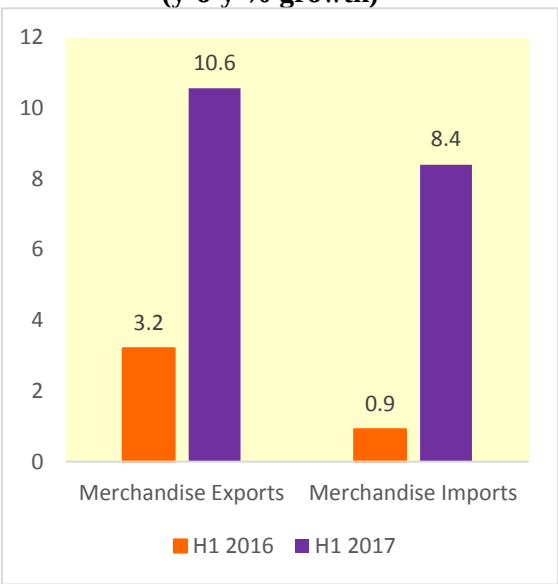


Figure 2.8 APEC Trade Volume, H1 2016 and H1 2017 (y-o-y % growth)



Note: APEC average growth rate does not include Brunei Darussalam and Papua New Guinea due to unavailability of data.
Source: WTO for trade values; UNCTAD Statistics for trade volume growth rates; and APEC PSU staff calculations.

Figure 2.9 Value of Merchandise Exports in APEC Economies, Jan-Aug 2016 and Jan-Aug 2017 (y-o-y % growth)

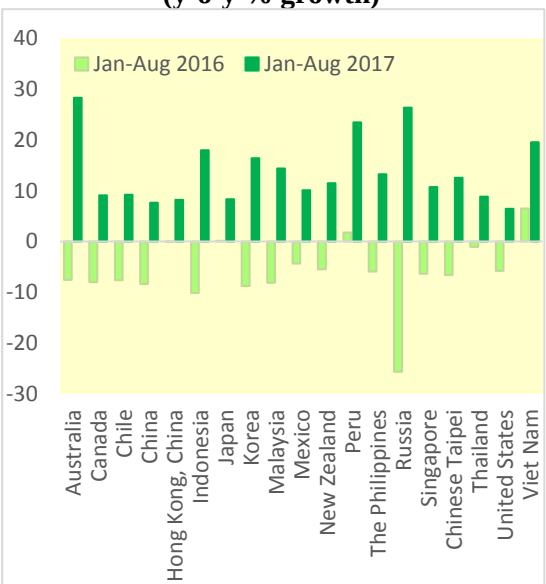
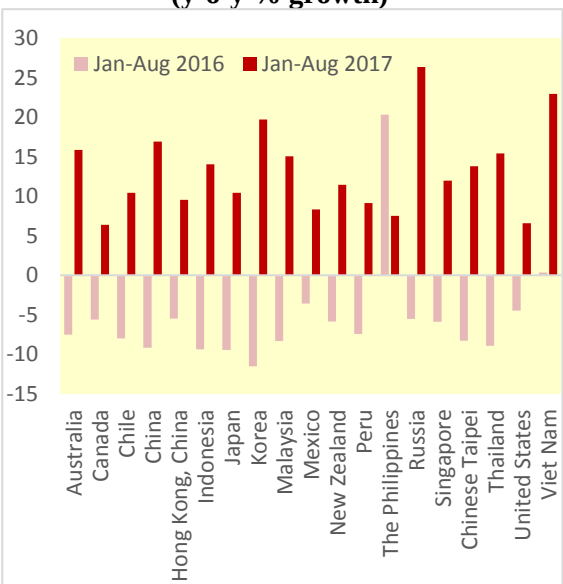


Figure 2.10 Value of Merchandise Imports in APEC Economies, Jan-Aug 2016 and Jan-Aug 2017 (y-o-y % growth)

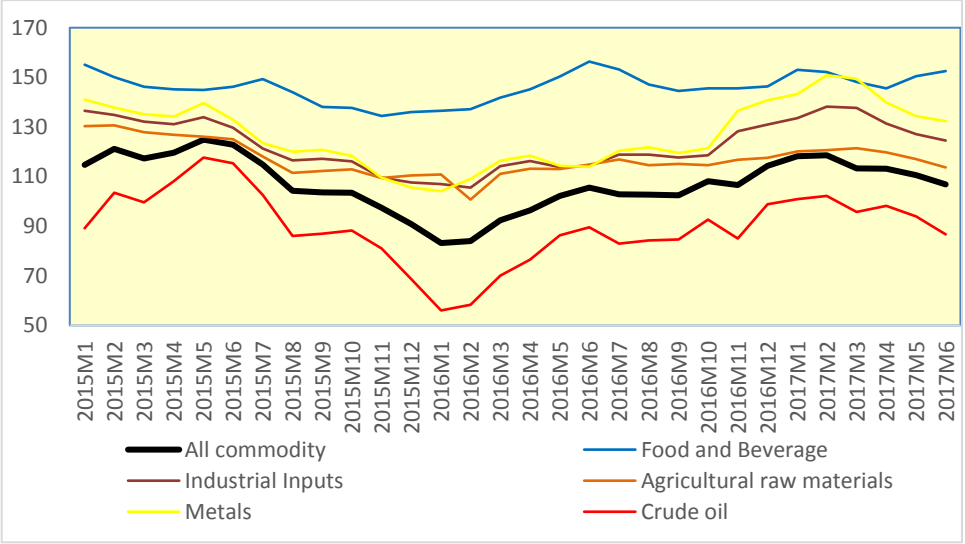


Note: Data are not available for Brunei Darussalam and Papua New Guinea.
Source: WTO; economy sources; and APEC PSU staff calculations.

This positive turnaround is reflected in the trade activity of individual APEC economies (Figures 2.9 and 2.10), wherein exports and imports of goods generally went up in the first eight months of 2017 compared to the same period in 2016. Aside from benefiting from higher global demand, another factor contributing to the reversal to trade growth could be the slight recovery in commodity prices, particularly in Q4 2016 up to Q1 2017 (Figure

2.11). Beginning in October 2016, the all-commodity price index had been on an upward trend until Q1 2017, resulting in an average value of 113.5 in H1 2017 or a year-on-year growth of 20.7 percent compared to the 94.0 index average recorded during the same period in 2016. Similarly, the price index for crude oil trended upwards starting October 2016 until Q1 2017. Prices for metals, industrial inputs, agricultural raw materials, and food and beverage also exhibited higher growth in Q1 2017 compared to Q1 2016. However, with the exception of food and beverage, commodity prices began to moderate in Q2 2017, although their levels were still higher than in Q2 2016.

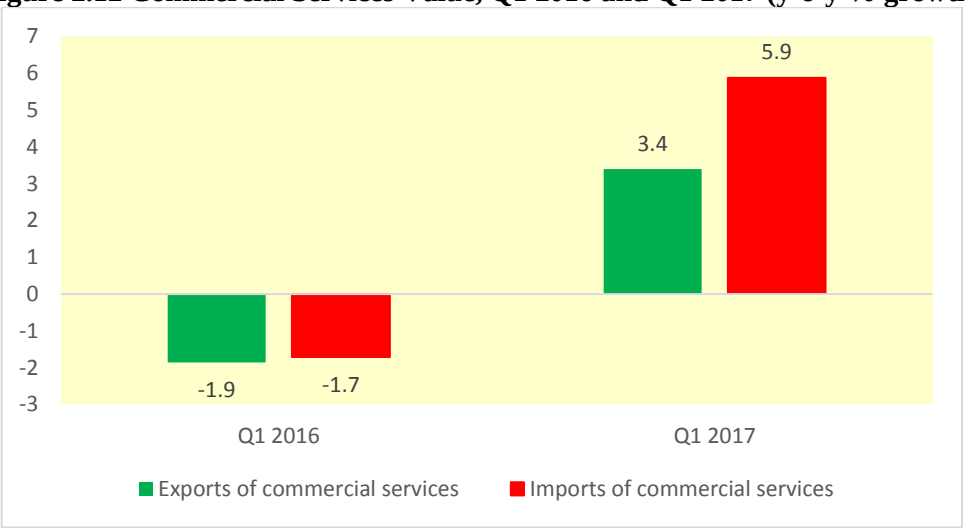
Figure 2.11 Commodity Prices, January 2015-June 2017 (index)



Source: IMF Primary Commodity Prices.

APEC trade in commercial services also exhibited a turnaround in growth similar to that of merchandise trade (Figure 2.12). The region's exports of commercial services increased by 3.4 percent in Q1 2017 compared to a contraction of 1.9 percent in Q1 2016, while imports of commercial services expanded by 5.9 percent in the first quarter of 2017 after falling by 1.7 percent in the comparable quarter in 2016.

Figure 2.12 Commercial Services Value, Q1 2016 and Q1 2017 (y-o-y % growth)



Note: Quarterly data are not available for Papua New Guinea.
Source: WTO; economy sources; and APEC PSU staff calculations.

2.3 INVESTMENT TRENDS

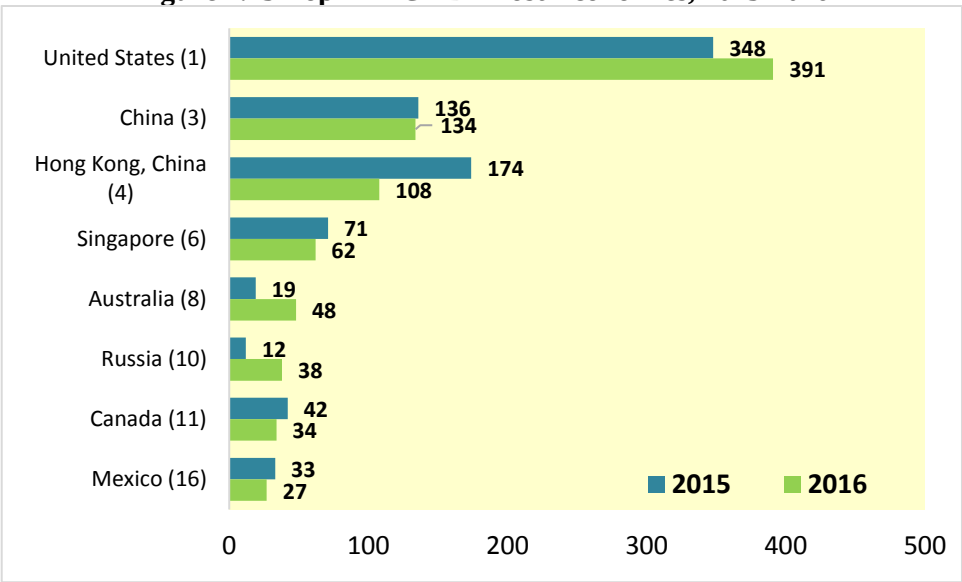
The APEC region attracted 53 percent of the world's foreign direct investment (FDI) in 2016, equivalent to USD 926.3 billion (Table 2.2). The continued high level of FDI inflows into the region indicates investor optimism about the economic fundamentals and investment opportunities in the APEC region. There were eight APEC economies in the top 20 FDI hosts for 2016 (Figure 2.13). Taken together, these top recipients of FDI received USD 842 billion in 2016, equivalent to about 91 percent of total FDI inflows into the APEC region during that year. However, the growth in FDI inflows slowed to 1.4 percent in 2016 from 21.9 percent in 2015, while FDI outflows at 4.1 percent outpaced FDI inflows in 2016.

Table 2.2 APEC FDI Inflows and Outflows, Growth Rates, and Share of World, 2011-2016

	2011	2012	2013	2014	2015	2016
FDI (billion USD)						
Inflows	737.7	706.6	799.1	749.6	913.4	926.3
Outflows	911.3	844.2	903.5	943.8	841.0	875.5
Growth in FDI (%)						
Inflows	14.2	-4.2	13.1	-6.2	21.9	1.4
Outflows	27.7	-7.4	7.0	4.5	-10.9	4.1
APEC share of world FDI (%)						
Inflows	46.4	44.4	55.4	56.6	51.5	53.0
Outflows	57.8	60.8	64.6	75.3	52.8	60.3

Source: UNCTAD World Investment Report 2017.

Figure 2.13 Top APEC FDI Host Economies, 2015-2016



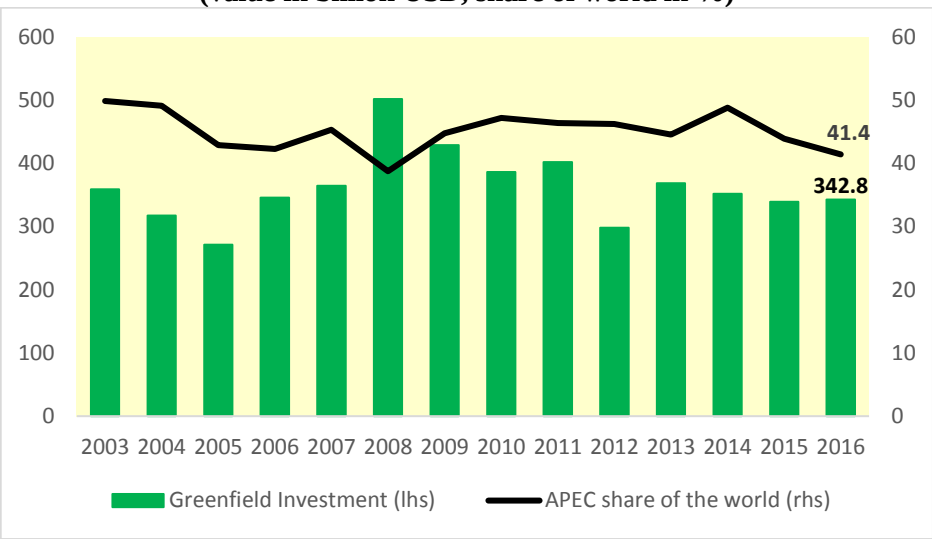
Note: The value of FDI inflows is shown in billion USD. Rankings of the top 20 global FDI host economies are based on 2016 inflows and are shown in parenthesis.
Source: UNCTAD World Investment Report 2017.

In terms of greenfield investments,[16] the APEC region accumulated around USD 342.8 billion worth of investments in 2016, equivalent to a 41.4 percent share of global greenfield

[16] Greenfield investment is a type of FDI where a parent economy begins a new venture and builds operations in a foreign economy, including activities such as the construction of new production facilities and the building of new distribution hubs, offices, and living quarters. Greenfield investment is an important

investments. Over the period 2003-2016, this is the second lowest APEC share of the world's greenfield investments aside from the 38.8 percent share recorded in 2008 amid the GFC.

Figure 2.14 Greenfield Investment Value in the APEC Region, 2003-2016 (value in billion USD, share of world in %)



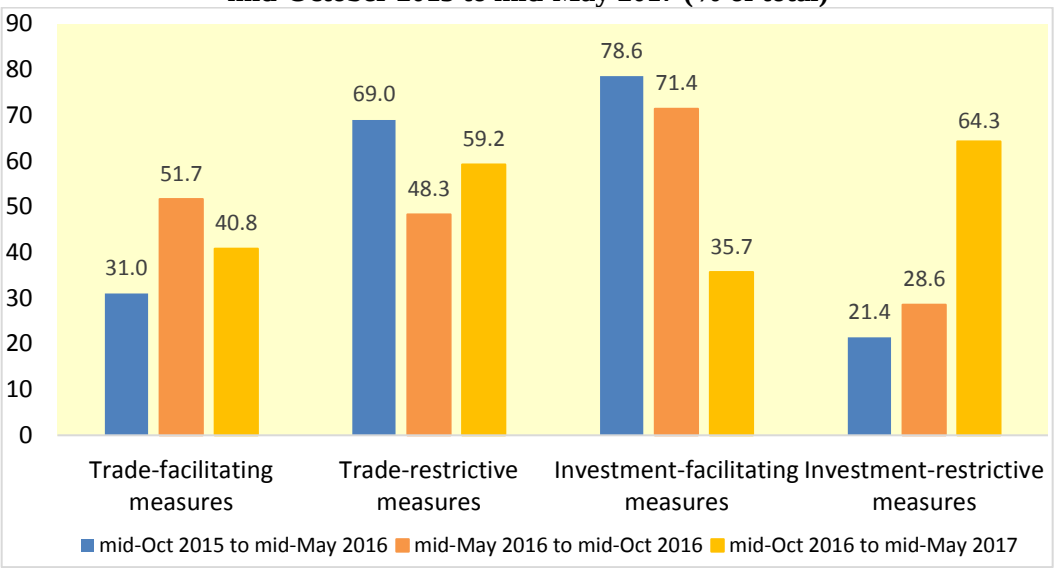
Source: UNCTAD World Investment Report 2017.

2.4 TRADE AND INVESTMENT MEASURES

Based on information contained in the WTO Report on G20 Trade Measures and the WTO-OECD-UNCTAD 17th Report on G20 Investment Measures dated 30 June 2017, the number of restrictive measures on trade and investment implemented by G20 APEC members outweighed the facilitating measures during the reporting period of mid-October 2016 to mid-May 2017. Trade-restrictive measures comprised 59 percent of total trade and trade-related measures implemented over the reporting period, while the share of investment-restrictive measures was higher relative to previous periods at 64 percent of the total investment measures implemented (Figure 2.15).

indicator because it gauges investors' willingness to put up new ventures following its assessment of a foreign economy's growth potential, business environment, and other considerations including political stability.

Figure 2.15 Trade and Investment Measures in Selected APEC Economies, mid-October 2015 to mid-May 2017 (% of total)



Note: Only nine of the 21 APEC economies belong to the G20, including Australia; Canada; China; Indonesia; Japan; Korea; Mexico; Russia; and the United States.
Source: WTO Report on G20 Measures (30 June 2017) and WTO-OECD-UNCTAD 17th Report on G20 Investment Measures (30 June 2017).

Trade-restrictive measures implemented during the most recent reporting period were dominated by anti-dumping and countervailing investigations (see Table 2.3 for a summary and Annex 1 for the specific measures[17]). The WTO defines "dumping" as a situation involving international price discrimination, wherein the price of a particular product is lower when sold in the importing economy compared to the price of the same product that is sold in the exporting economy. Article VI of the 1994 General Agreement on Tariffs and Trade (GATT) elaborates on the basic principles that cover the governance of anti-dumping actions including the investigation, determination, and imposition of anti-dumping duties. Parallel to anti-dumping duties are "countervailing measures" that are meant to level the playing field between local and foreign producers of the same product in cases where the latter can afford to sell at a lower price because of government subsidies. Other trade-restrictive measures imposed during the period covered were in the form of additional import/export documentation requirements, quotas, duties, and bans.

[17] Annex 1 can be downloaded at https://www.apec.org/-/media/Files/AboutUs/PolicySupportUnit/2017/Annex-1_Trade-and-Trade-Related-Measures_-October-2016-to-May-2017.docx.

Table 2.3 Trade and Trade-related Measures Implemented by APEC G20 Members, mid-October 2016 to mid-May 2017

	Number of Measures
Trade-restrictive measures	
Initiation of anti-dumping investigation	25
Initiation of countervailing investigation	10
Initiation of safeguard investigation	0
Increase/Imposition of import tariffs and export duties	1
Imposition of export/import requirements/quotas/restrictions	8
Imposition/Extension of import/export ban	1
Sub-total: Trade-restrictive measures	**45**
Trade-facilitating measures	
Termination of anti-dumping investigation/duties	13
Termination of countervailing investigation/duties	6
Termination of safeguard investigation	0
Reduction/elimination of exportduties/import tariffs	7
Elimination of import/export ban and other restrictions	1
Other trade-facilitating administrative measures	4
Sub-total: Trade-facilitating measures	**31**
Total: Trade and trade-related measures	**76**

Source: WTO Report on G20 Measures (30 June 2017).

The number of restrictive investment measures was also higher than the number of investment-friendly measures implemented during the reporting period in review (see Table 2.4 for a summary and Annex 2 for the specific measures[18]). The imposition of additional requirements and prohibitions against the entry of foreign investment outnumbered all other restrictive measures such as increasing or imposing taxes/fees/surcharges and introducing a ceiling on foreign ownership. Nevertheless, some APEC economies also implemented measures that aim to facilitate the entry of foreign investment, foremost of which was the issuance of guidelines that clarify or simplify existing rules and processes.

Table 2.4 Investment Measures Implemented by APEC G20 Members, mid-October 2016 to mid-May 2017

	Number of measures
Facilitating measures	**5**
Increasing transparency in the investment environment	1
Clarifying and simplifying rules and processes	2
Relaxing rules on foreign exchange quota and settlement	0
Increasing threshold for foreign investments	1
Lifting investment restrictions in certain sectors	1
Restrictive measures	**9**
Imposing additional requirements/prohibitions	5
Increasing/Imposing taxes/fees/surcharges	3
Introducing foreign ownership ceiling	1
Total: Investment measures	**14**

Source: WTO-OECD-UNCTAD 17th Report on G20 Investment Measures (30 June 2017).

[18] Annex 2 can be downloaded at https://www.apec.org/-/media/Files/AboutUs/PolicySupportUnit/2017/Annex-2_Investment-Measures_Oct-2016-to-May-2017.docx.

The increase in trade-restrictive measures implemented over the recent period combined with the upward trend in investment-restrictive measures is a cause for concern. An inward shift towards protectionist policies could significantly reduce cross-border trade and investment flows, which, in turn, could put a brake to the ongoing economic momentum, potentially restraining growth in the APEC region.

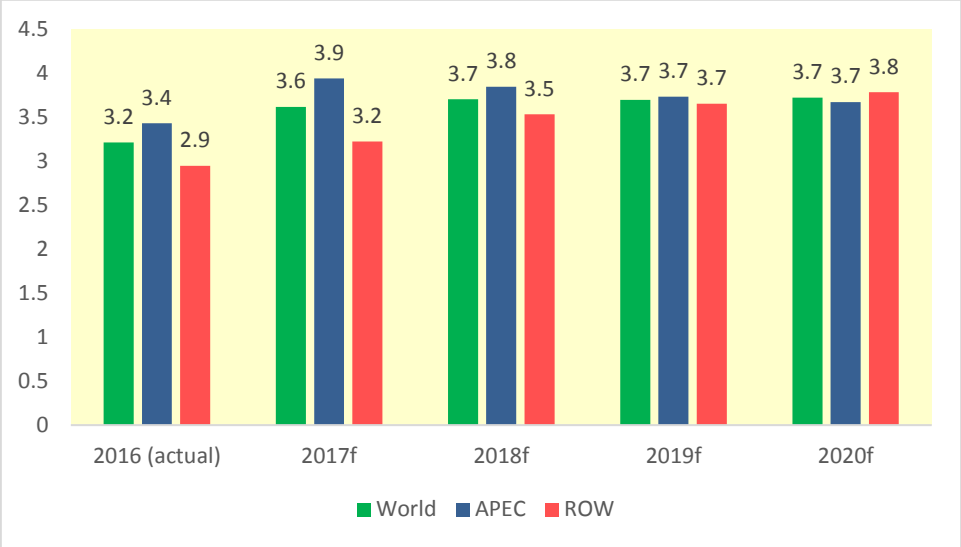
2.5 NEAR-TERM OUTLOOK, RISKS, AND OPPORTUNITIES

The economic outlook for the short-term indicates an improvement in APEC GDP growth to 3.9 percent in 2017 from a 3.4 percent growth in 2016, outpacing the world economy at 3.6 percent and the ROW at 3.2 percent (Figure 2.16). The 0.1 percentage point increase in the 2017 growth projection for APEC from the forecast in the May 2017 APEC Regional Trends Analysis (ARTA) takes into account the ongoing momentum prevailing among APEC economies, derived largely from the global cyclical recovery (Table 2.5). In 2018, growth in the APEC region is projected to outpace the global economy and the ROW at 3.8 percent, before aligning with the world economy in 2019 and 2020. The APEC region benefits from the positive feedback loop of continued strength in global economic activity that translates into higher demand and significant improvements in consumer and business confidence, further feeding into consumption, investment, and trade activity.

Furthermore, economies that are commodity exporters are expected to post relatively stronger GDP growth in 2017 in line with the anticipated continued rebound in the prices of oil, food, and other commodities. Oil prices are expected to trend upward in 2017, with a projected increase of around 14.4 percent[19] compared to the levels in 2016 due to a combination of increased demand and supply uncertainties. In particular, supply uncertainties could stem from involuntary outages due to a variety of reasons such as labour disputes, wildfires, and geo-political unrest in oil-rich economies; production cut targets set by the Organization of the Petroleum Exporting Countries (OPEC); and limited investments in new and unconventional fields due to the fragile recovery observed in overall investment activity. Meanwhile, the International Energy Agency expects global demand for oil to be robust in 2017 at 1.6 million barrels per day.[20]

[19] Based on the IMF Primary Commodity Prices data projections as of July 2017.
[20] International Energy Agency, Oil Market Report dated 12 October 2017.

Figure 2.16 Near-term Real GDP Growth Forecasts, 2016-2020 (y-o-y % growth)



Note: ROW = Rest of the World; f = forecast.
Source: IMF WEO (October 2017) and PSU staff calculations.

Table 2.5 Comparison of APEC Real GDP Growth Forecasts, May 2017 and November 2017

APEC Real GDP Growth Forecast (in %)	2017	2018	2019	2020
May 2017 ARTA	3.8	3.8	3.7	N.A.
November 2017 ARTA	3.9	3.8	3.7	3.7

Note: Weighted aggregates for APEC GDP growth are based on the IMF's growth forecasts.
Source: IMF WEO (October 2017) and PSU staff calculations.

Short-term risks are broadly balanced. Downside risks relate mostly to policy uncertainty and missteps which could take a toll on consumer and business confidence, pulling domestic spending and demand downwards, effectively halting the current momentum in global economic activity. Non-economic factors such as geo-political tensions, terrorist attacks, extreme weather conditions, and localised political discord could also introduce instability, which could, in turn, adversely affect consumption and investment, thereby dampening growth prospects. The upside potential for growth could come from continued strength in global economic activity, which is expected to further boost consumer and business spending as well as provide much needed support to trade and investment activities.

The WTO forecasts global trade volume to expand by 2.4 percent in 2017 from sluggish growth of 1.3 percent in 2016. Due to significant uncertainty surrounding near-term economic and policy developments, the 2017 forecast is placed on a wider range at 1.8-3.6 percent. For 2018, the WTO projects a higher trade volume growth of between 2.1-4.0 percent. The IMF's world trade volume forecasts are higher at 4.2 percent in 2017 and 4.0 percent in 2018, reflecting an expected stronger recovery in global demand and capital spending.

In the medium-term, risks remain tilted to the downside as uncertainty continues to be a crucial determinant of growth going forward. Uncertainty could come from the magnitude and frequency of a monetary policy hike, particularly as higher long-term interest rates could translate into a global tightening of financial conditions and unmanageable debt levels, with adverse effects for vulnerable economies. Fiscal policy remains difficult to

ascertain, which is important at a time when growth-friendly fiscal measures are needed to sustain the economic recovery. In terms of trade and investment policies, protectionism continues to be a concern, both in the short-term and medium-term, since it could give pause to the ongoing global economic recovery. In addition, risks could come from a range of other factors such as the UK-EU relationship post-Brexit, potential corrections in asset valuations and financial market volatilities, as well as ongoing geo-political conflicts and adverse impact of weather disturbances.

2.6 CONCLUSION

The recent expansion in economic growth experienced by the APEC region hinged largely on the global cyclical recovery. This synchronised movement between APEC and the world economy is not surprising, given that the APEC region comprises more than half of global trade and GDP. The APEC region is expected to track a higher growth trajectory in 2017 from the 3.4 percent GDP growth reached in 2016 due to the combined effects of favourable external conditions and strong domestic consumption along with an increased contribution from trade.

Trade growth continues to be an important factor in economic growth. In the APEC region, the continued recovery in trade, marked by a positive reversal in the first eight months of 2017 following a contraction in the comparable period in 2016, has translated into higher GDP growth in the first half of 2017. Growth in global trade volume is expected to continue throughout 2017 and 2018, in line with stronger global demand from a firmer global economic recovery. To support continued trade growth, trade policies that facilitate the free flow of trade and investment across borders remain essential.

However, restrictive measures in trade and investment are on the rise, giving credence to concerns about an increasingly protectionist policy trend worldwide. It is recognised that trade affects labour market outcomes via the demand for skills, available employment opportunities, and disparities in wage levels across sectors, genders and economies. Nonetheless, shifting policies inward to protect jobs could be counterproductive as severe restrictions on trade could have negative repercussions on an economy's growth potential, affecting household incomes as a result. Governments are therefore encouraged to continue facilitating trade and investment on the one hand, while implementing a mix of adjustment programs, skills and education upgrading, and social protection initiatives on the other hand, in order to support workers and households negatively affected by economic changes.

APEC continues to push for a more conducive trading environment. In a statement issued in August 2017 by the Third Senior Officials' Meeting in Ho Chi Minh City, Viet Nam, senior officials from the 21 APEC economies are moving towards restructuring their policy regimes to better align the region's markets by easing structural bottlenecks and limiting barriers to trade. These trade policy reforms are to be implemented with the aim of increasing job creation and productivity, especially in the digital age, and ensuring continued growth for the APEC region.[21]

In a similar vein, APEC Small and Medium Enterprises Ministers, in their September 2017 statement, emphasised the importance of enhancing competitiveness and innovation of the

[21] The full statement is available at https://www.apec.org/Press/News-Releases/2017/0830_som3.

region's micro, small, and medium enterprises (MSMEs) in the digital era. Ministers enumerated joint actions to be taken forward by APEC economies over the next year in order to facilitate increased participation of small businesses in digital-driven trade with the objective of improving livelihoods and economic welfare. In the area of innovation, Ministers endorsed an initiative to be undertaken by APEC economies to foster robust and sustainable growth of innovative startups. They also supported an APEC Strategy for Green, Sustainable and Innovative MSMEs.[22]

The recent interim assessment of APEC's ease of doing business covering the years 2015 and 2016 support these statements and endorsements for a better trading and business environment in the APEC region. The results show that APEC's combined progress in creating a more conducive regulatory environment for starting or operating businesses at 3.6 percent exceeded the pro-rata target of 3.3 percent in 2016. Among the identified priority areas of (1) starting a business; (2) dealing with construction permits; (3) getting credit; (4) trading across borders; and (5) enforcing contracts, the indicator on getting credit posted the greatest progress, owing to improvements in the strength of legal rights and the depth of credit information in the APEC region. Specifically, the average coverage of the adult population with credit information available in public or private credit registries/bureaus increased from 74.3 percent in 2015 to 75.3 percent in 2016. Starting a business in the APEC region also recorded notable progress, with the average time declining from 15.3 days to 14 days between 2015 and 2016.[23]

The current period of relatively high growth, which is expected to be sustained well into 2020, leaves adequate room for APEC economies to continue along the path of reform. Thus, beyond marked progress in ease of doing business in the region, APEC members could focus on implementing their commitment to structural reforms as documented in the Renewed APEC Agenda for Structural Reform (RAASR) Individual Action Plans. The RAASR 2016-2020 encourages reforms along the following three pillars: (1) more open, well-functioning, transparent and competitive markets; (2) deeper participation in those markets by all segments of society, including MSMEs, women, youth, older workers and people with disabilities; and (3) sustainable social policies that promote these objectives, enhance economic resiliency, and are well-targeted, effective and non-discriminatory.

APEC economies will have different approaches and strategies to fulfil their commitments, given their varying stages of development as well as other domestic challenges. The overarching goal of APEC is the 1994 Bogor Goals of free and open trade and investment by 2020 through the reduction of trade barriers in the region and promotion of the free flow of goods, services, and capital among APEC economies. APEC, operating in a voluntary, non-legally binding process, continues to cooperate in all levels of policy discussions to arrive at a consensus that ensures the promotion of the Bogor Goals. As the 2020 deadline for the achievement of the Bogor Goals approaches, APEC could exert all efforts to ensure that the benefits of free trade and investment are not only measurable, but also felt equitably by all sectors of society in the region, particularly the vulnerable or disadvantaged groups such as women, youth, the disabled, and the poor.

---

[22] The full statement is available at https://www.apec.org/Press/News-Releases/2017/0915_SMEMM-statement.

[23] The full report is available at http://publications.apec.org/Publications/2017/09/APECs-Ease-of-Doing-Business--Interim-Assessment-20152016.