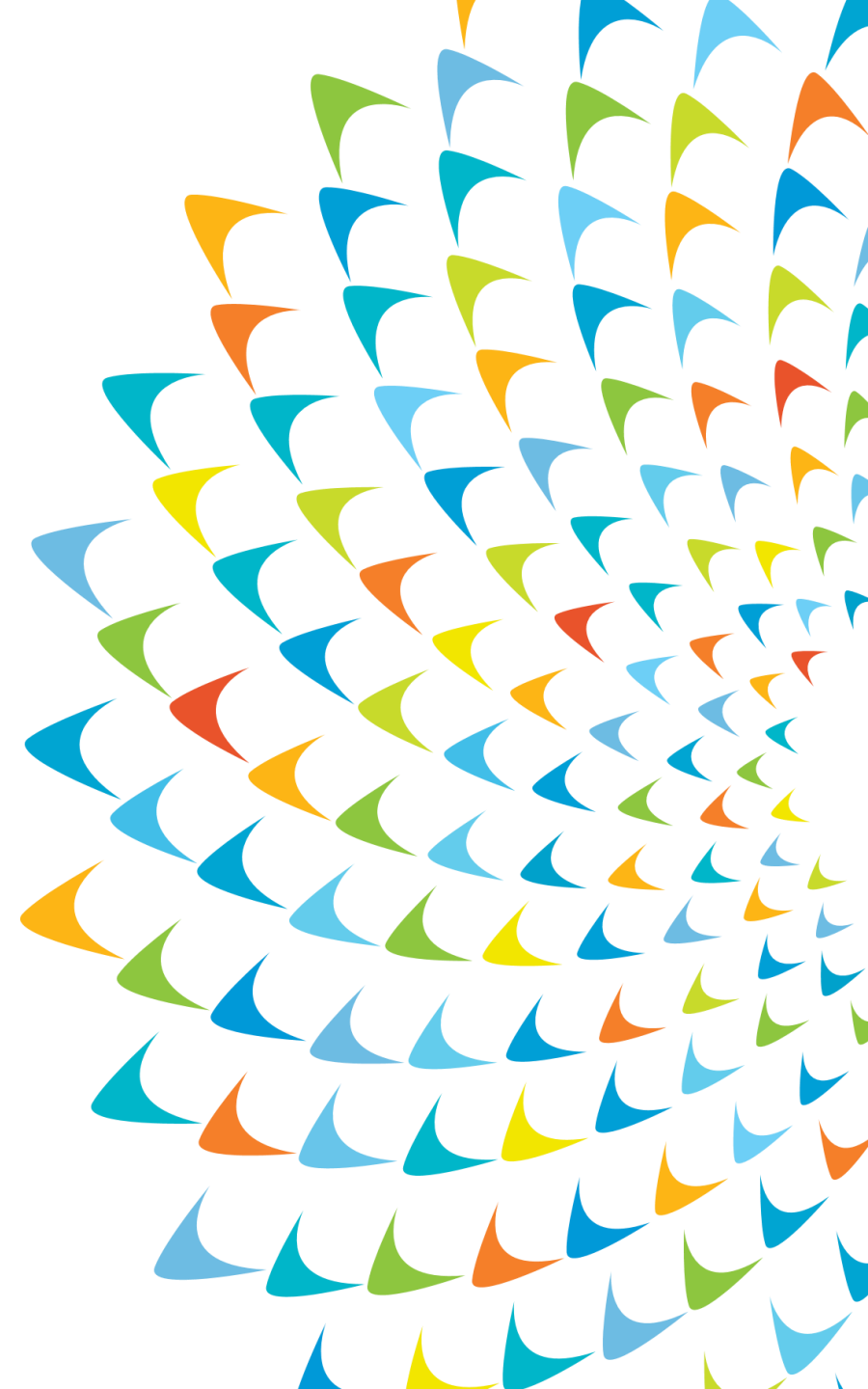




Poverty, Inequality and the Role of Islamic Finance for Inclusive Growth in Asia

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Outline

1. Anatomy of poverty and inequality in Asia
2. Role of governments
3. Infrastructure for inclusive growth
4. Role of Islamic finance

Anatomy of inequality in Asia

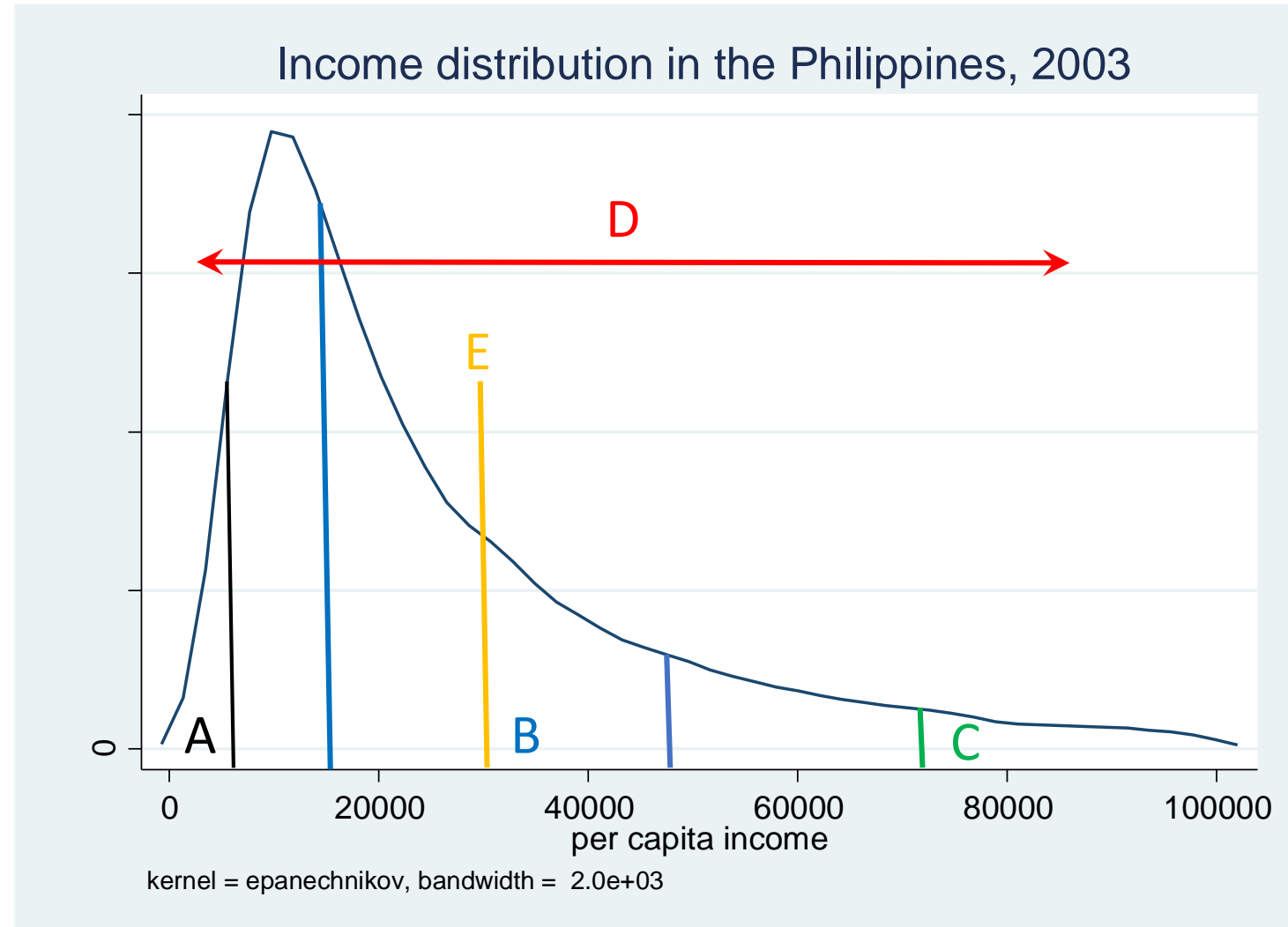
Inequality in Asia

= “within country inequality”

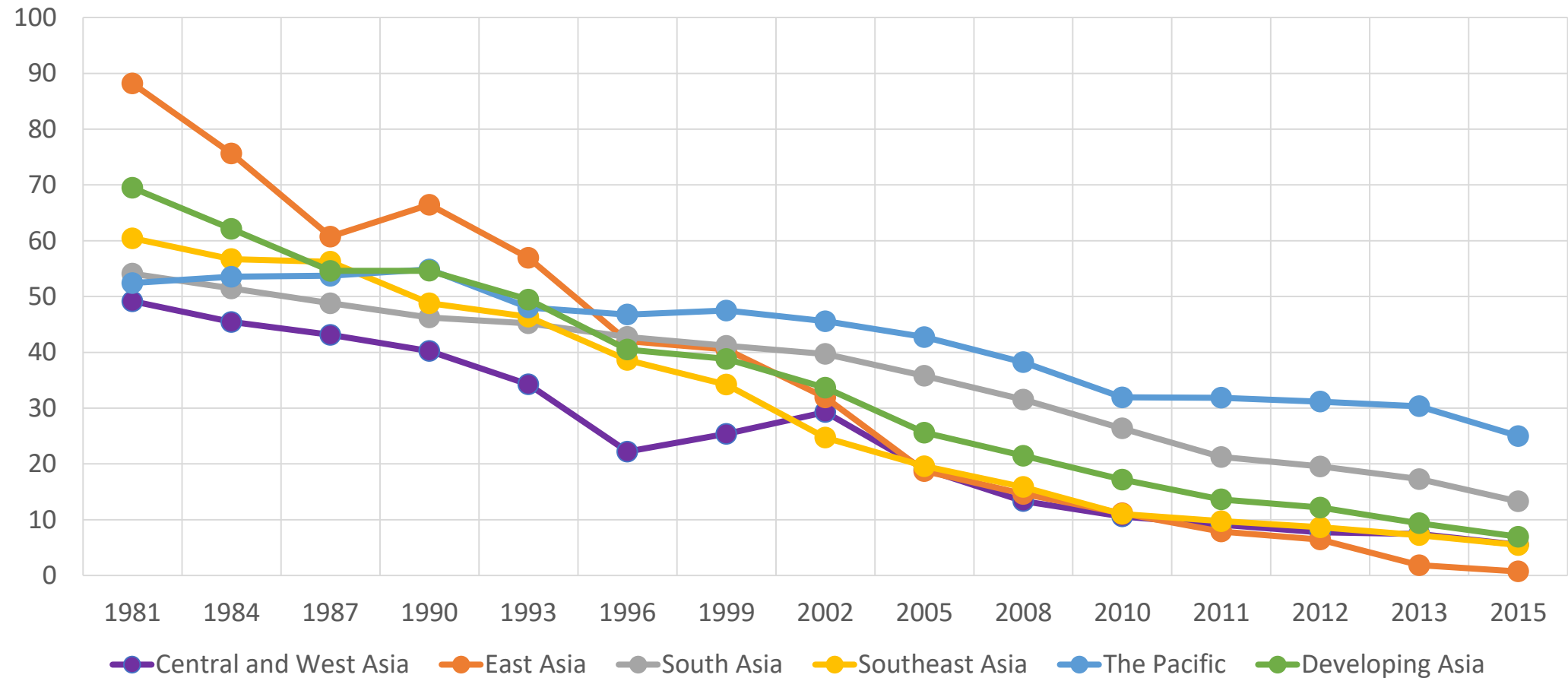
- A. Incidence of poverty (%) ↓
- B. Middle class (%) ↑
- C. Top income share (%) ↑
- D. Overall inequality (Gini) ↑

+ “across country inequality”

- E. Per capita income ?

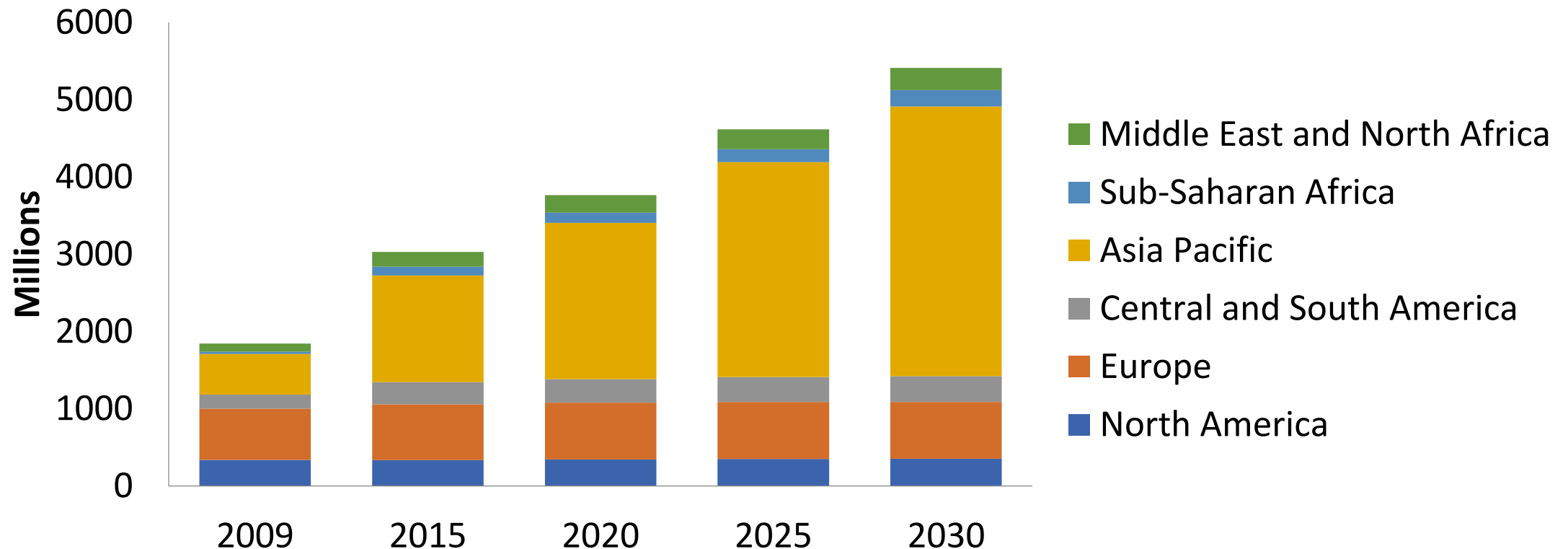


Regional trend of incidence of poverty (in %; 1.9 USD Poverty Line)



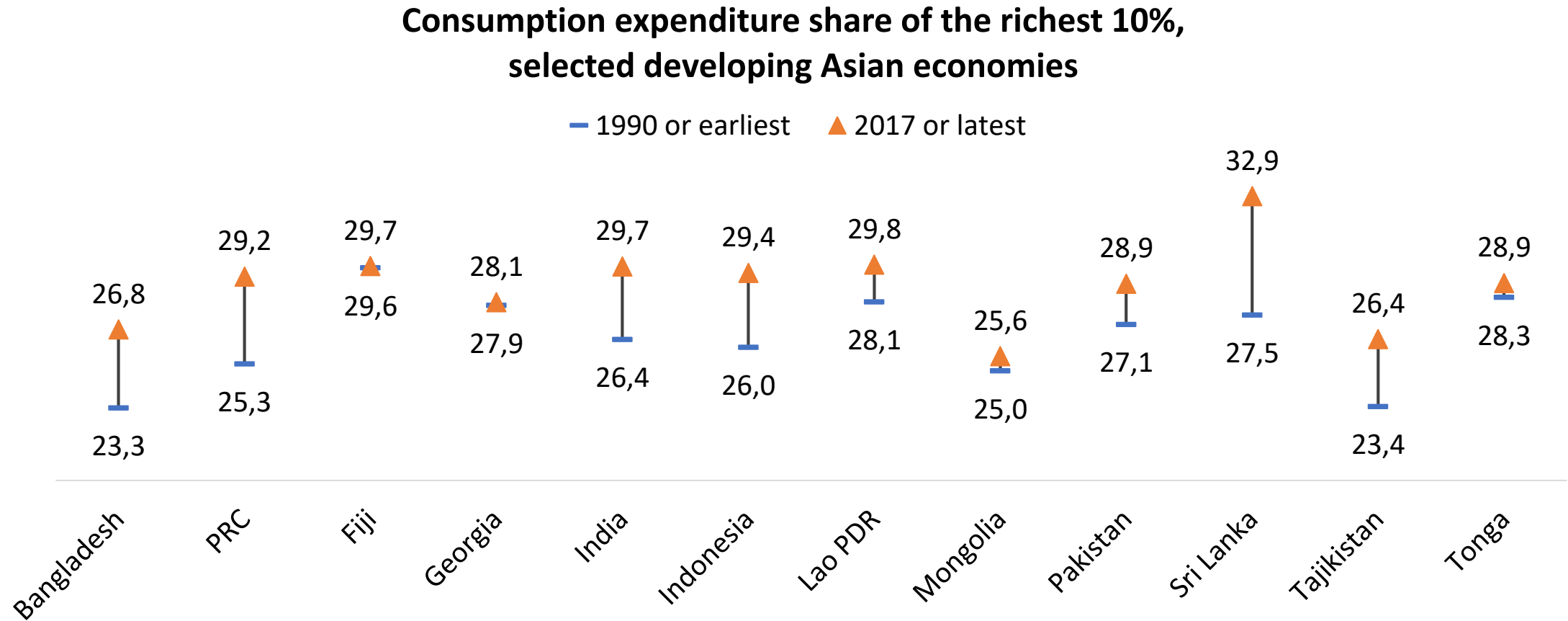
Data: PovcalNet: the on-line tool for poverty measurement developed by the Development Research Group of the World Bank. <<http://iresearch.worldbank.org/PovcalNet/povDuplicateWB.aspx>>

Middle income population



Data: For 2009, Kharas, Homi (2010). "The Emerging Middle Class in Developing Countries." OECD Development Centre Working Paper No. 285. Paris: OECD. For 2015 to 2030, Kharas, Homi (2017), "The Unprecedented Expansion of the Global Middle Class: An Update," GLOBAL ECONOMY & DEVELOPMENT WORKING PAPER 100, Brookings Institution.

Top income share increased in developing Asia



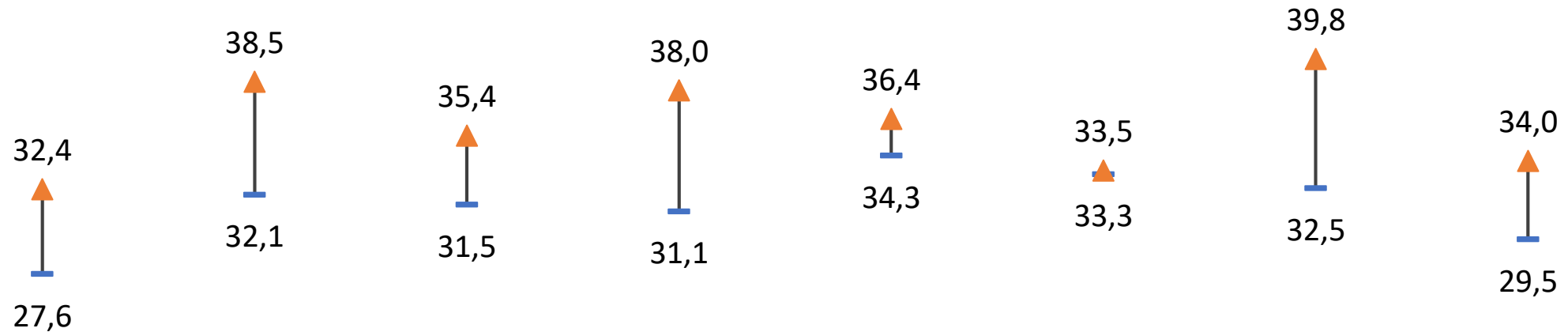
Source: ADB staff estimates based on World Bank PovCal data.

Income inequality has risen in developing Asia:

Asia-wide Gini increased from 38 in the 1990s to 45 in the 2010s, contrasting with “growth with equity” in the 1960s and 1970s

Gini coefficient of per capita household consumption, selected Asian economies

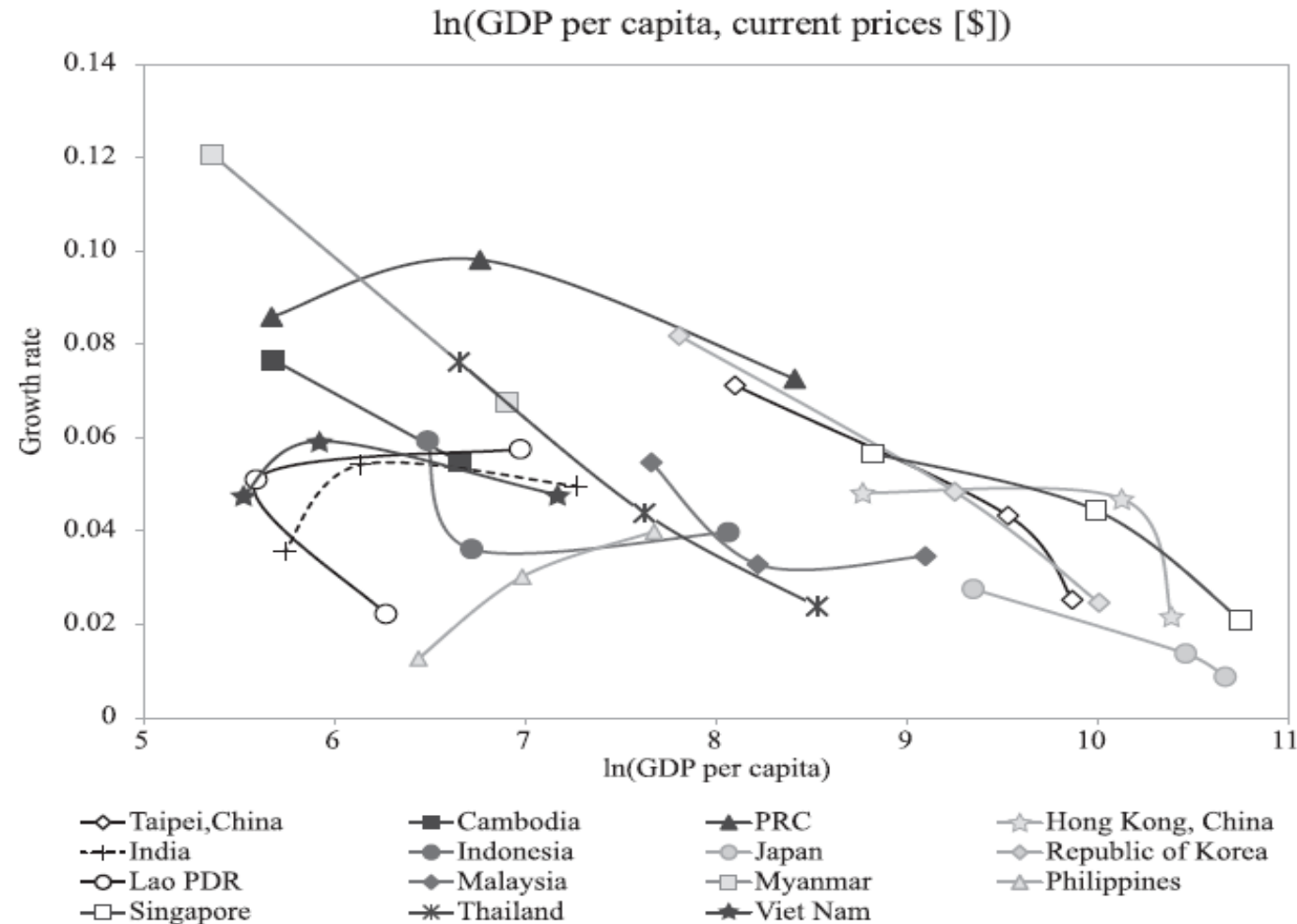
— 1990 or earliest ▲ 2017 or latest



Source: ADB staff estimates based on World Bank PovCal data.

Middle income trap

Figure 6. Growth Convergence in East Asia



GDP = gross domestic product, Lao PDR = Lao People's Democratic Republic, PRC = People's Republic of China.
Source: Author's calculations.



Ito, Takatoshi (2017)
“Growth Convergence and the Middle-Income Trap,”
Asian Development Review
34(1), 1-27.

Anatomy of inequality: Philippine Case

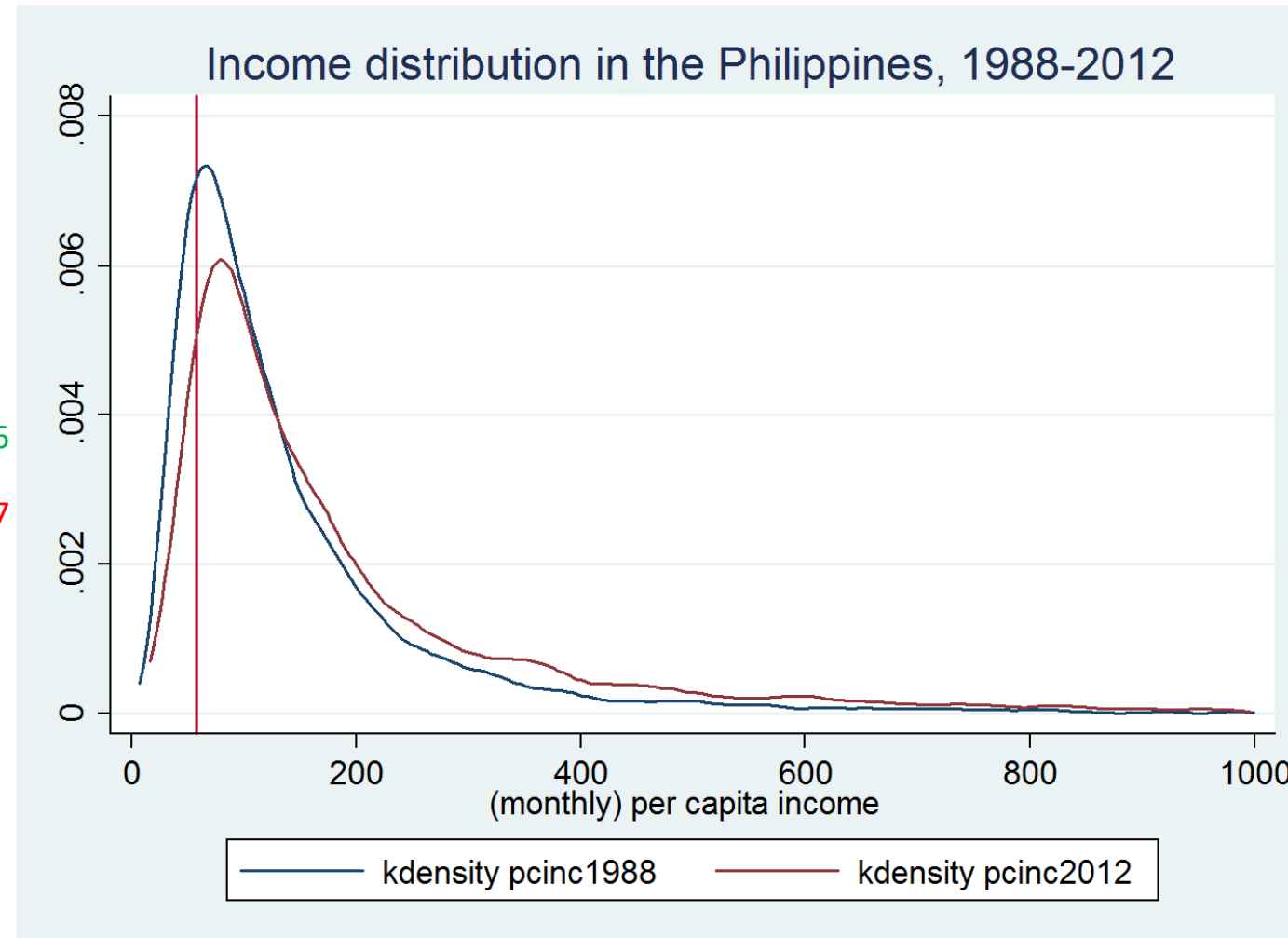
Inequality in Asia

= “within country inequality”

- A. Incidence of poverty (%) ↓ 20.8→11.0
- B. Middle class (%) ↑ 9.7→18.4
- C. Top income share (%) ↑ 36.1→36.6
- D. Overall inequality (Gini) ↑ 0.46→0.47

+ “across country inequality”

- E. Per capita income ↓ 155.0→214.3



Why has inequality risen globally?

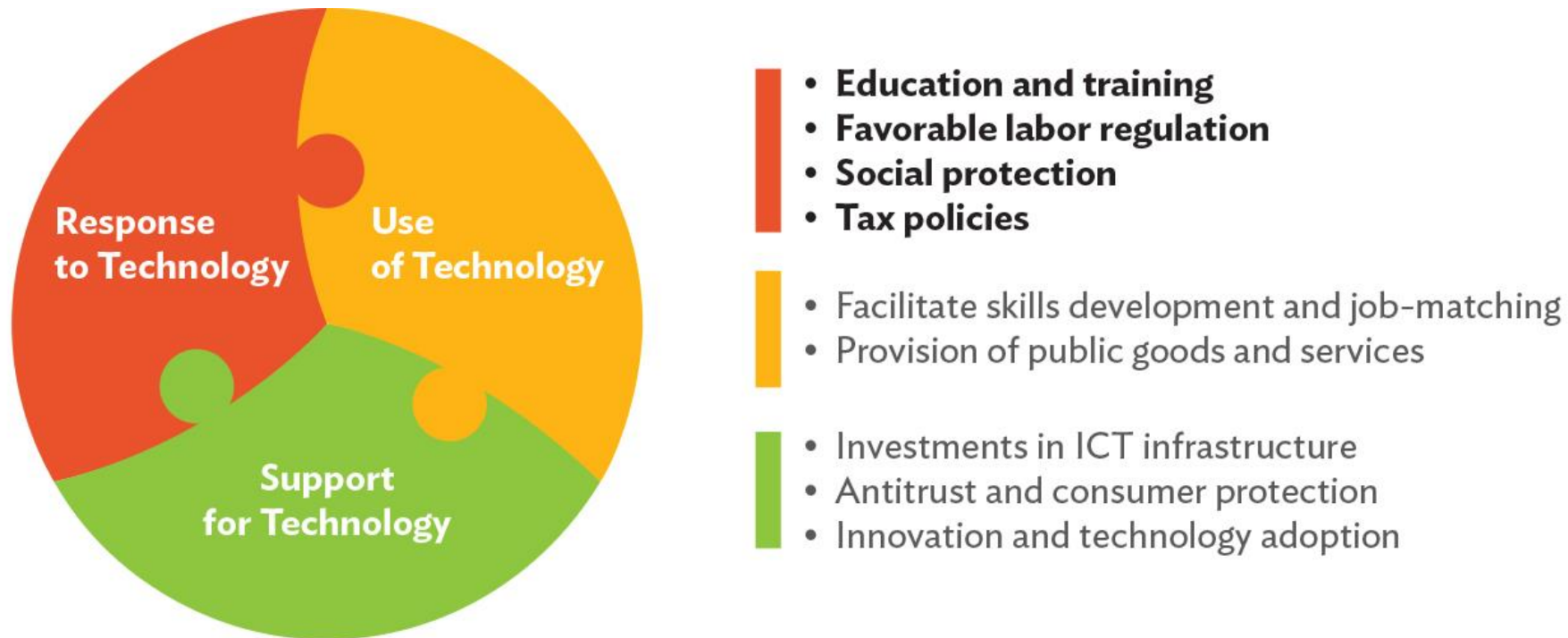
- **Technological progress (4th IR), globalization, and market deregulation** favor:
 - skilled over unskilled labor; capital over labor
 - certain geographical locations (such as urban and coastal areas) over others (such as rural and inland regions)
 - Countries with absorptive capacity over countries with low capacity
- **Aging populations**, since older cohorts have a more unequal income distribution than younger cohorts [Deaton and Paxson (1994) JPE]
- **Inequality of opportunity**
 - **Intergenerational** transmission of inequality: low (high) education → low (high) income → low (high) education
 - **Spatial core-periphery structure** perpetuates rural-urban inequality.

Why inequality matters?

- Impede trickle-down poverty reduction effect of growth
- May undermine economic growth itself
 - e.g., leading to a misallocation of human capital, creating intergenerational inequality
- Can damage society and institutions – it can strain social cohesion and lead to conflicts that discourage investment (where an institution can be defined as a self-sustaining system of shared beliefs *a la* Masahiko Aoki)
- Cause political backlash – public pressure to enact populist policies may benefit the poor in the short term, but hold back efficiency and growth in the long run

Government's role for inclusive growth in the era of 4th Industrial Revolution

The new industrial revolution and the role of government

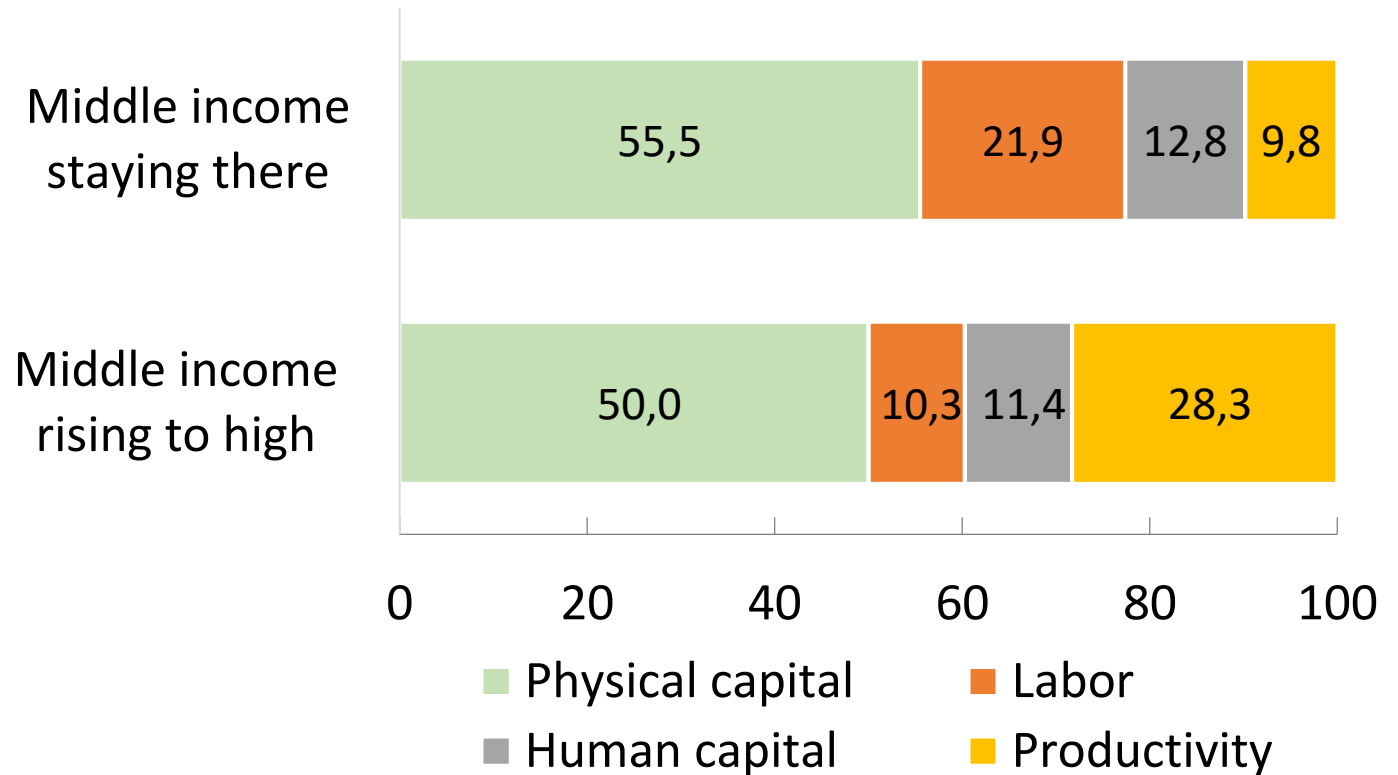


Role of infrastructure in making growth more “inclusive”

- Infrastructure sets “enabling” environment of inclusive growth
- RCT on infrastructure is challenging by nature but recent micro IE study of infrastructure shows its important re-distributional role:
 - Enable the poor to gain welfare through better information [Jensen (2007) QJE]
 - Reduce poverty by increasing the property value [Gonzalez-Navarro and Quintana-Domeque (2016) REStat]
 - Eliminate barriers to (female) job participation [Dinkelman (2011) AER]
 - Improve regional connectivity to reduce regional disparity [Donaldson (2017) AER]
 - Improve access to education & labor markets for the poor [Duflo (2001) AER]
- Right infrastructure is also critical to overcome middle income trap

Productivity is the key to transcend middle income challenge: Innovation, human capital investments, and (advanced) infrastructure investments

Contributions to Growth, 1960–2014 (%)





Role of Islamic Finance in Achieving Inclusive Growth

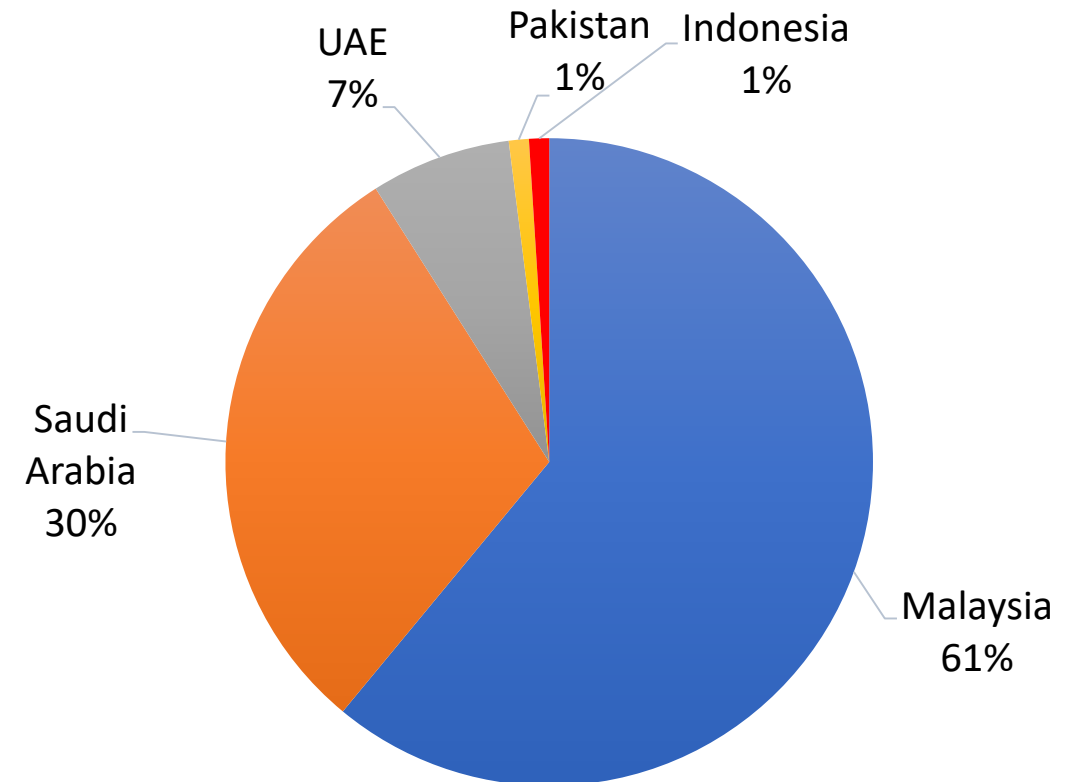
1. **The lack of proper infrastructure** is one of the major obstacles to development to achieve inclusive growth.

✓ The infrastructure financing needs of Asia at **\$26 trillion for the 25 years** from 2016 to 2030.

2. To achieve inclusive growth:

- a) **Islamic finance such as Infra-Sukuk** can be particularly instrumental in bridging the infrastructure gap.
- b) Islamic finance can also support **trade financing** for sustainable growth.
- c) **Specialized poverty focused Islamic FIs** can provide services to the poor using Shariah compliant modes and instruments.

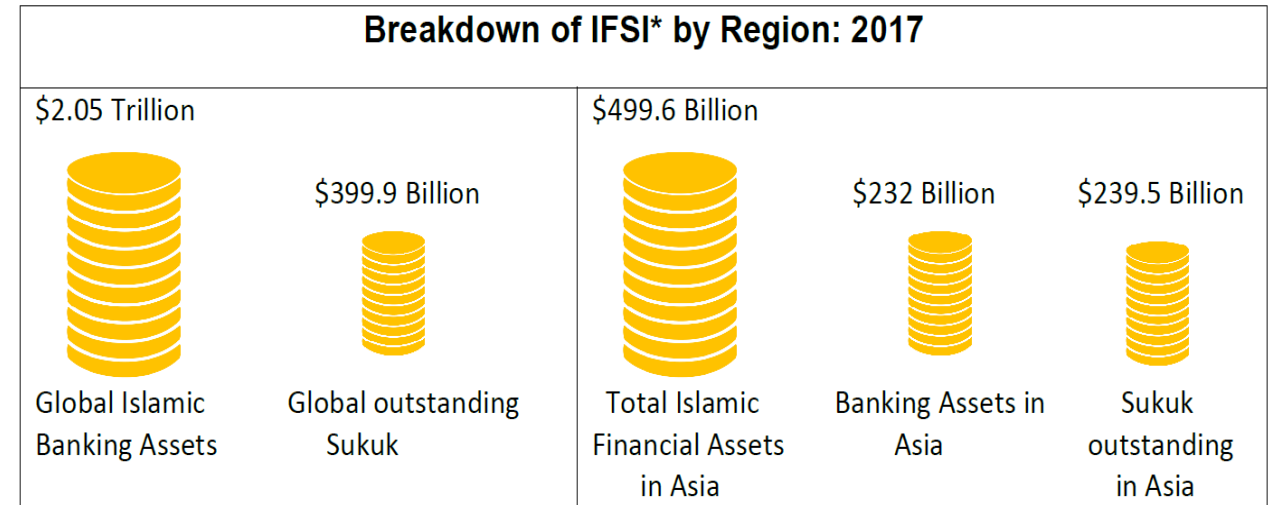
Infra-Sukuk Issued (% share): 2012 Q1 – 2015 Q3



Source: An Overview of Islamic Banking and Finance in Asia, ADBI. 2018.

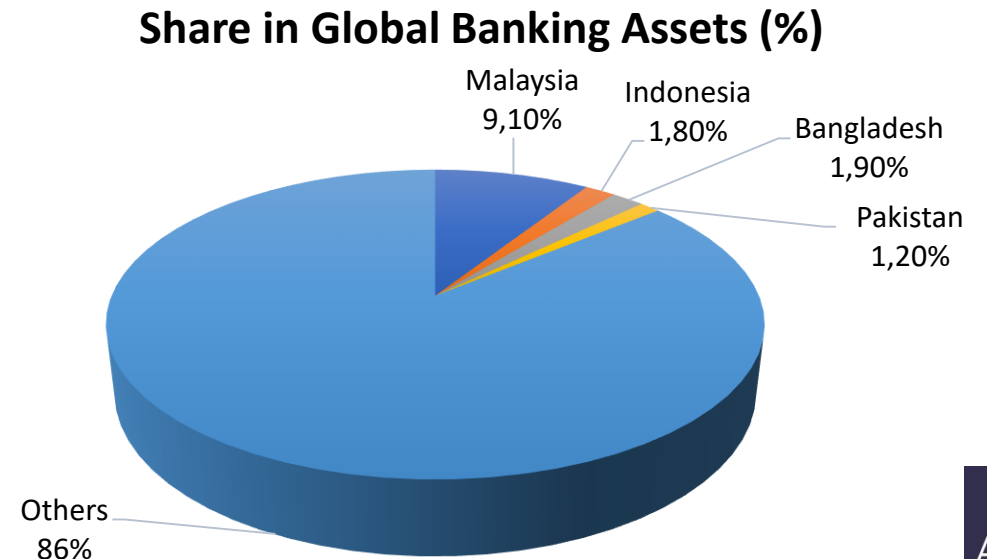
Indeed, Islamic Finance has Shown Robust Growth

1. Islamic financing has enjoyed a **robust growth of 10%** during 2007-2017.
2. Total assets have increased from \$150 billion in 1990s to **\$2 trillion by 2017**.
3. Total Islamic financial assets in **Asia are estimated to be \$499.6 billion** by 2017.
4. Meanwhile, **global Sukuk** outstanding surged by 25.6% to \$399.9 billion by 2017.



*Islamic Financial Services Industry

Source: Islamic Financial Services Industry Stability Report (2018).



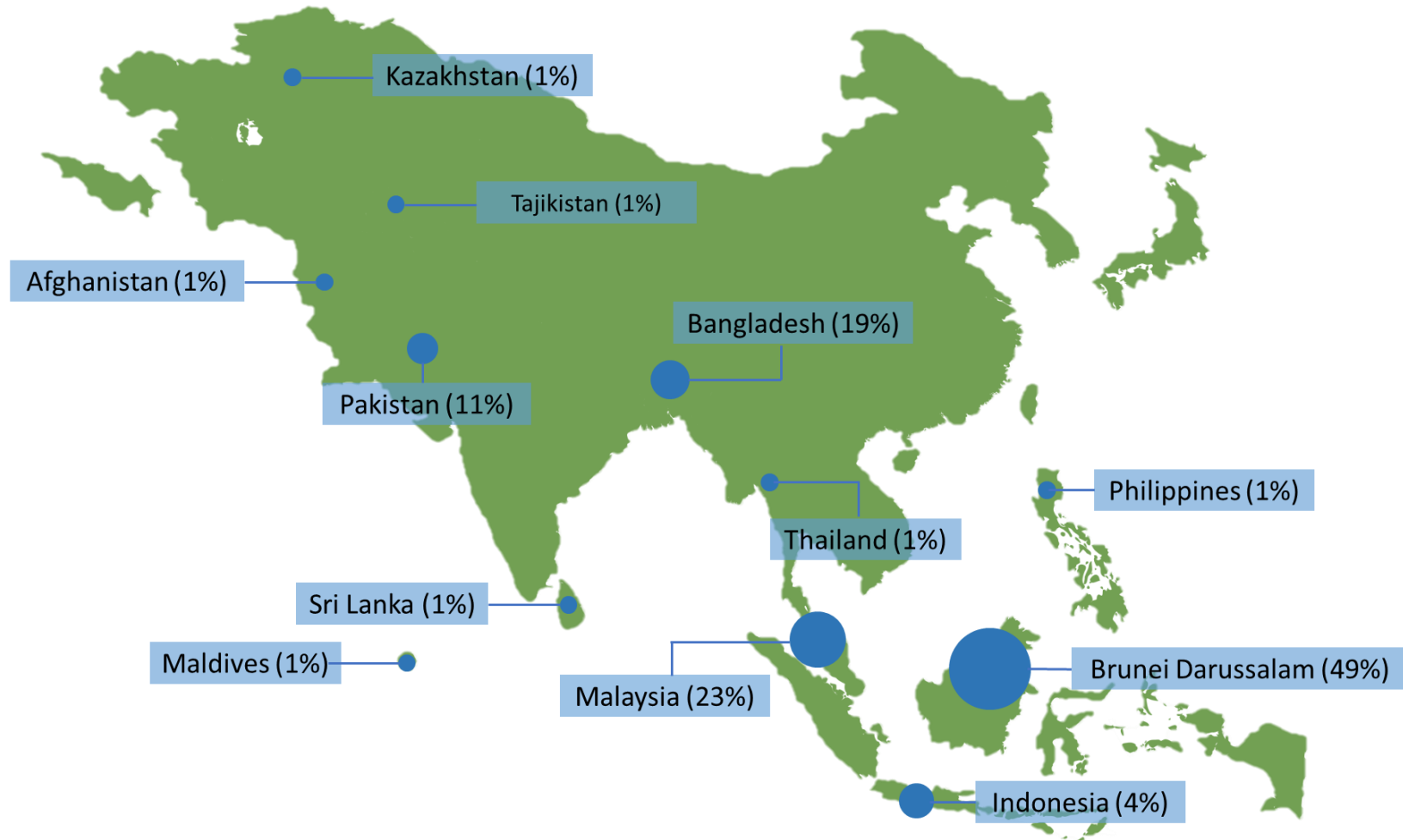
Source: Islamic Financial Services Industry Stability Report 2018



Islamic Finance and ADB's DMCs

1. ADB's **DMCs** represents a sizable portion of Islamic financial assets, increasingly regarding Islamic financial tools as an alternative source of financing investments.
✓ It is also seen as an opportunity to attract liquidity from Gulf Cooperation Council states.
2. ADB recognizes the potential role of the Islamic financial sector in supporting inclusive and sustainable growth.
3. ADB is encouraging the development of Islamic finance by introducing international best standards to DMCs.

Domestic Market Share of Islamic Finance



Source: Islamic Financial Services Industry Stability Report 2018



Remarks

1. Asia and the Pacific region has achieved **substantial poverty reduction**, but **rising inequality** is one of the major challenges
2. The governments in the region will play a key role in tackling this challenge, especially **supporting infrastructure development** to continue sustainable growth, maintain poverty reduction trend, and achieve global climate goals
3. **Islamic finance** has emerged as an alternative source of financing. Islamic finance such as Infra-Sukuk can be particularly instrumental in **bridging the infrastructure gap**.
4. However, there is still a need to build a strong **regulatory framework** in DMCs.



Thank you.

