THE IMPORTANCE OF CONTINUING GROWTH FOR THE EMERGING AND DEVELOPING COUNTRIES – PRESENT AND PERSPECTIVES

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Abstract

The global economy is facing in the past years diffrent paths of growth in the advanced economies and emerging and developing economies. Slow growth, high global uncertainty and perceptions of a lack of equality of opportunity should prompt policy makers to act in order to revive the global economy. Adressing domestic reforms, as this paper present from the economic outlook analysis of the International Monetary Found and other organisations, is the necessary condition for making the most of megatrends - like globalisation, digitalisation, population ageing and environmental degradation - and requires gouvernments to carrefully select, prepare, prioritise and implement structural reforms.

Keywords: growth, reforms, economic policies, emerging and developing economies

JEL Classification: O, O40, O47

1. A short analysis of the global growth in 2018 and the beginning of 2019

Global growth has fallen sharply over the past year. Between economies the situation has different causes. On one hand, advanced economies had their weakening been broad based, affecting major economies (the United States and especially the euro area) and smaller Asian advanced economies. Even more pronounced was the slowdown in activity across emerging market and developing economies, including Brazil, China, India, Mexico, and Russia.

Over the past year has been a geographically broad-based slowdown in industrial output driven by multiple and interrelated factors, such as:

- A sharp downturn in car production and sales, which saw global vehicle purchases decline by 3 percent in 2018. The automobile industry slump reflects both supply disruptions and demand influences—a drop in demand after the expiration of tax incentives in China; production lines adjusting to comply with new emission standards in the euro area (especially Germany) and China; and possible preference shifts as consumers adopt a wait-and-see attitude with technology and emission standards changing rapidly in many countries, as well as evolving car transportation and sharing options.
- Weak business confidence amid growing tensions between the United States and China on trade and technology. As the reach of US tariffs and retaliation by trading partners has steadily broadened since January 2018, the cost of some intermediate inputs has risen, and uncertainty about future trade relationships has ratcheted up. Manufacturing firms have become more cautious about long-range spending and have held back on equipment and machinery purchases. This trend is most evident in the tradeand global-value-chain-exposed economies of east Asia. In Germany and Japan, industrial production was recently lower than one year ago, while its growth slowed considerably in China and the United Kingdom and, to some extent, in the United States;
- about the production of capital goods, we saw a slowdown in demand in China, driven by needed regulatory efforts to rein in debt and exacerbated by the macroeconomic consequences of increased trade tensions. With the slowdown in industrial production, trade growth has come to a near standstill. In the first half of 2019, the volume of global trade stood just 1 percent above its value one year ago—the slowest pace of

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growth for any six-month period since 2012. From a geographical standpoint, major contributors to the weakening in global imports were China and east Asia (both advanced and emerging) and emerging market economies under stress.

- Downturns in global trade are related to reduced investment spending—as was the case, for instance, in 2015–16. Investment is intensive in intermediate and capital goods that are heavily traded.
- The front-loading of exports, before tariffs were imposed in late 2018, likely also played a role by bringing forward demand for import components. For example, global semiconductor sales declined in 2018, in part related to seeming market saturation in smartphones and fewer launches of new tech products more broadly.
- While manufacturing lost steam, services (a larger share of the economy) broadly held firm. Resilient services activity has meant steady aggregate employment creation, which supported consumer and, in turn, household spending on services. This favorable feedback cycle between service sector output, employment, and consumer confidence has supported domestic demand in several advanced economies.

Weakening growth in the advanced economy group stabilized in the first half of 2019, after a sharp decline in the second half of 2018. The main countries reacted differently:

- The US economy shifted to a somewhat slower pace of expansion (about 2 percent on an annualized basis) in the past few quarters as the boost from the tax cuts of early 2018 faded;
- the UK economy slowed, with investment held back by Brexit-related uncertainty;
- The euro area economy registered stronger growth in the first half of this year than in the second half of 2018, but the German economy contracted in the second quarter as industrial activity slumped. In general, weak exports have been a drag on activity in the euro area since early 2018, while domestic demand has, so far, stayed firm;
- Japan posted strong growth in the first half of this year, driven by robust private and public consumption. Preliminary data suggest a modest pickup in growth in the first half of 2019;

The emerging market and developing economy group were well below its pace in 2017 and early 2018:

- China's growth was lifted by fiscal stimulus and some easing of the pace of financial regulatory strengthening initiated in the second half of 2018;
- India's economy decelerated further in the second quarter, held back by sector-specific weaknesses in the automobile sector and real estate as well as lingering uncertainty about the health of nonbank financial companies;
- In Mexico, growth slowed sharply during the first half of the year owing to elevated policy uncertainty, budget under-execution, and some transitory factors;
- growth resumed in the second quarter in Brazil after a first-quarter contraction driven in part by a mining disaster;
- likewise, growth recovered modestly in the second quarter in South Africa, helped by improved electricity suppl;
- growth recovered in Turkey in the first half of the year following a deep contraction in the second half of 2018, benefiting from more favorable global financial conditions and fiscal and credit support;
- in contrast, the contraction in Argentina continued through the first half of the year, albeit at a slower pace, and risks going forward are clearly to the downside due to the sharp deterioration in market conditions.

Projected growth for 2019, at 3.0 percent, is the weakest since 2009. Except in sub-Saharan Africa, more than half of countries were expected to register per capita growth lower than their median rate during the past 25 years. The marked deceleration reflects carryover from broad-based weakness in the second half of 2018, followed by a mild growth uptick in the first half of 2019 and supported, in some cases, by more accommodative policy stances (such as in China and, to some extent, the United States). With growth estimates for both the second half of 2018 and the first half of this year marked down, the 2019 growth projection is 0.3 percentage point weaker than in the April 2019 WEO.

Continued macroeconomic policy support in major economies and projected stabilization in some stressed emerging market economies are expected to lift global growth modestly over the remainder of 2019 and into 2020, bringing projected global growth to 3.4 percent for 2020. The forecast markdown of 0.2 percentage point for 2020 relative to the April 2019 WEO largely reflects the fact that tariffs have risen and are costing the global economy: following tariff announcements in May and August 2019, the average US tariff on imports from China will rise to just over 24 percent by December 2019 (compared with about 12¼ percent assumed in the April 2019 WEO), while the average China tariff on imports from the United States will increase to about 26 percent (compared with about 16½ percent assumed in the April 2019 WEO).

2. Reforms for growth in the emerging and developing economies

After slowing sharply in the last three quarters of 2018, the pace of global economic activity remains weak. Momentum in manufacturing activity, in particular, has weakened substantially, to levels not seen since the global financial crisis. Rising trade and geopolitical tensions have increased uncertainty about the future of the global trading system and international cooperation more generally, taking a toll on business confidence, investment decisions, and global trade. A notable shift toward increased monetary policy accommodation—through both action and communication—has cushioned the impact of these tensions on financial market sentiment and activity, while a generally resilient service sector has supported employment growth. That said, the outlook remains precarious.

Emerging markets and developing economies have enjoyed good growth over the past two decades. But many countries are still not catching up with the living standards of advanced economies.

At current growth rates, it would take more than 50 years for a typical emerging market economy to close half of its current income gap in living standards, and 90 years for a typical developing economy.

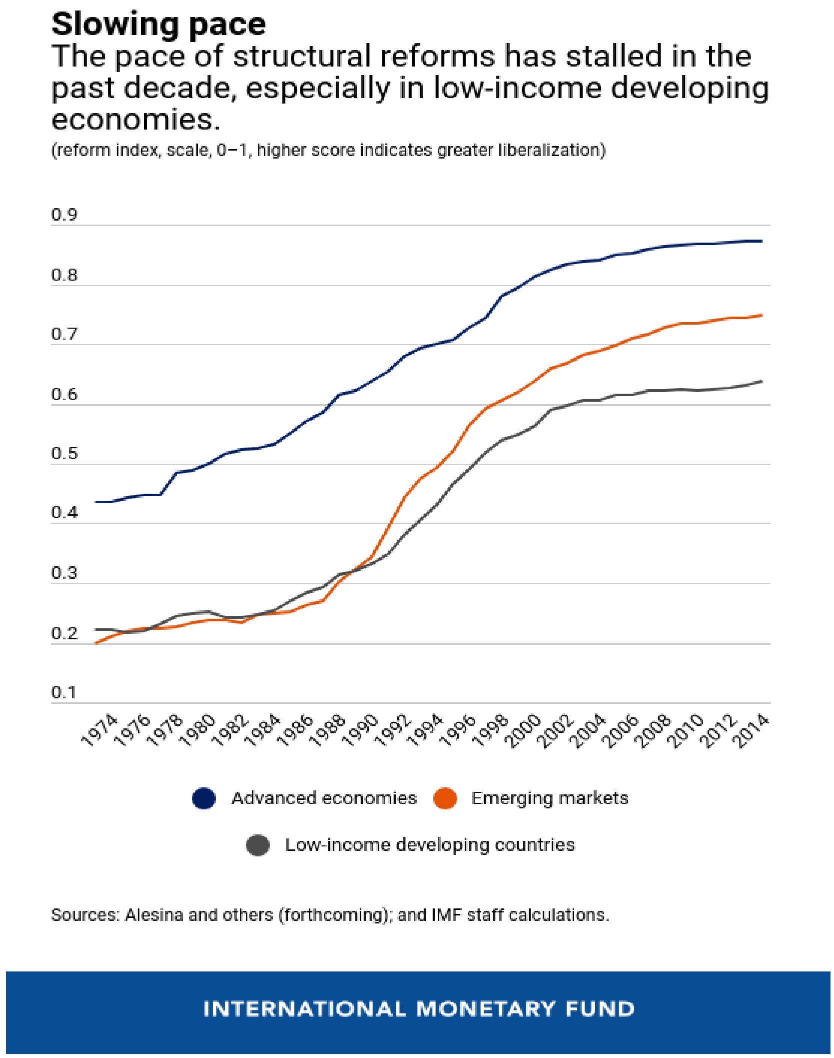
Based on the World Economic Outlook, October 2019, the emerging and developing countries must implement major reforms in six key areas at the same time—domestic finance, external finance, trade, labor markets, product markets, and governance— so they can double the speed of income convergence of the average emerging market and developing economy to the living standards of advanced economies. This could raise output levels by more than 7 percent over a six-year period.

Policies that change the way governments work—known as structural reforms—are difficult to measure. They often involve policies or issues that are not easy to quantify, such as job protection legislation or the quality of supervision of the domestic banking system.

To address this, the IMF recently developed a comprehensive dataset covering structural regulations in domestic and external finance, trade, and labor and product markets. The data cover a large sample of 90 advanced and developing economies during the past four decades. To the five indicators, we added the quality of governance (for example, how countries control corruption) from the World Governance Indicators.

The new indicators show that, after the major wave of reforms in the late 1980s and—most importantly—the 1990s, the pace slowed in emerging market and developing economies during the 2000s, especially in low-income developing countries (see Figure 1).

Figure 1



While this slowdown reflects the prior generation of reforms, as in advanced economies, there remains ample room for a renewed reform push, particularly in developing economies—notably, across sub-Saharan Africa and, to a lesser extent, in the Middle East and North Africa and the Asia-Pacific region.

For the average emerging market and developing economy, the results imply that major simultaneous reforms across all six areas considered can raise output by more than 7 percent over a six-year period. This would increase annual per capita GDP growth by about 1 percentage point, doubling the average speed of income convergence to advanced-country levels.

One channel through which reforms increase output is by reducing informality. For example, lowering barriers to businesses' entry in the formal sector encourages some informal companies to become formal. In turn, formalization boosts output by increasing companies' productivity and capital investment. For this reason, the payoff from reforms tends to be larger where informality is pervasive.

Some reforms work best when the economy is strong. In good times, reducing layoff costs makes employers more willing to hire new workers, while in bad times it makes them more willing to dismiss existing ones, magnifying the effects of a downturn. Similarly, increasing competition in the financial sector at a time of weak credit demand may push certain financial intermediaries out of business, further weakening the economy.

In countries where the economy is weak, governments may prioritize reforms—such as strengthening product market competition—that pay off regardless of economic conditions, design others to alleviate any short-term costs—such as enacting job protection reforms now with a provision that they will take effect later. These reforms can also be accompanied with monetary or fiscal policy support where possible.

Reforms also work best if properly packaged and sequenced. Importantly, they typically deliver larger gains in countries where governance is stronger. This means that strengthening governance can support economic growth and income convergence not just directly by incentivizing more productive formal enterprises to invest and recruit, but also indirectly by magnifying the payoff from reforms in other areas.

Finally, to fulfill their promise of improving living standards, reforms must be supported by redistributive policies that spread the gains widely across the population—such as strong social safety nets and programs that help workers move across jobs. For reforms to be sustainable and therefore effective, they need to benefit not just some, but all.

3. Growth Forecast for Emerging Market and Developing Economies

Growth in the emerging market and developing economy group is expected to bottom out at 3.9 percent in 2019, rising to 4.6 percent in 2020. The forecasts for 2019 and 2020 are 0.5 percentage point and 0.2 percentage point lower, respectively, than in April, reflecting downward revisions in all major regions except emerging and developing Europe.

• Emerging and Developing Asia remains the main engine of the world economy, but growth is softening gradually with the structural slowdown in China. Output in the region is expected to grow at 5.9 percent this year and at 6.0 percent in 2020 (0.4 and 0.3 percentage point lower, respectively, than in the April 2019 WEO forecast). In China, the effects of escalating tariffs and weakening external demand have exacerbated the slowdown associated with needed regulatory strengthening to rein in the accumulation of debt. With policy stimulus expected to continue supporting activity in the face of the adverse external shock, growth is forecast at 6.1 percent in 2019 and 5.8 percent in 2020—0.2 and 0.3 percentage point lower than in the April 2019 WEO projection. India's economy is set to grow at 6.1 percent in 2019, picking up to 7 percent in 2020. The downward revision relative to the April 2019 WEO of 1.2 percentage points for 2019 and 0.5 percentage point for 2020 reflects a weaker-than-expected outlook for domestic demand. Growth will be supported by the lagged effects of monetary policy easing, a reduction in corporate income tax rates, recent measures to address corporate and environmental regulatory uncertainty, and government programs to support rural consumption.

• Subdued growth in emerging and developing Europe in 2019 largely reflects a slowdown in Russia and flat activity in Turkey. The region is expected to grow at 1.8 percent in 2019 and 2.5 percent in 2020. The upward revision to 2019 growth relative to the April 2019 forecast reflects a shallower-than-expected downturn in Turkey in the first half of the year as a result of fiscal support. In Russia, by contrast, growth has been weaker this year than forecast in April, but is projected to recover next year, contributing to the upward revision to projected 2020 growth for the region. Several countries in central and eastern Europe, including Hungary and Poland, are experiencing solid growth on the back of resilient domestic demand and rising wages.

• In Latin America, activity slowed notably at the start of the year across the larger economies, mostly reflecting idiosyncratic factors. Growth in the region is now expected at 0.2 percent this year (1.2 percentage point lower than in the April 2019 WEO). The sizable downward revision for 2019 reflects downgrades to Brazil (where mining supply disruptions have hurt activity) and Mexico (where investment remains weak and private consumption has slowed, reflecting policy uncertainty, weakening confidence, and higher borrowing costs). Argentina's economy is expected to contract further in 2019 on lower confidence and tighter external financing conditions. Chile's growth projection is revised down, following weaker-than-expected performance at the start of the year. The deep humanitarian crisis and economic implosion in Venezuela continue to have a devastating impact, with the economy expected to shrink by about one-third in 2019. For the region as a whole, growth is expected to firm up to 1.8 percent in 2020 (0.6 percentage point lower than in the April forecast). The projected strengthening reflects expected recovery in Brazil (on the back of accommodative monetary policy) and in Mexico (as uncertainty gradually subsides), together with less severe contractions for 2020 compared to this year in Argentina and Venezuela.

• Growth in the Middle East and Central Asia region is expected to be 0.9 percent in 2019, rising to 2.9 percent in 2020. The forecast is 0.9 and 0.4 percentage point lower, respectively, than in the April 2019 WEO, largely due to the downward forecast revision for Iran (owing to the effect of tighter US sanctions) and Saudi Arabia. While non-oil growth is expected to strengthen in 2019 on higher government spending and confidence, oil GDP in Saudi Arabia is projected to decline against the backdrop of the extension of the OPEC+ agreement and a generally weak global oil market. The impact on growth of the recent attacks on Saudi Arabia's oil facilities is difficult to gauge at this stage but adds uncertainty to the near-term outlook. Growth is projected to pick up in 2020 as oil GDP stabilizes and solid momentum in the non-oil sector continues. Civil strife in some other economies, including Libya, Syria, and Yemen, weigh on the region's outlook.

• In sub-Saharan Africa, growth is expected at 3.2 percent in 2019 and 3.6 percent in 2020, slightly lower for both years than in the April 2019 WEO. Higher, albeit volatile, oil prices earlier in the year have supported the subdued outlook for Nigeria and some other oil-exporting countries in the region, but Angola's economy—because of a decline in oil production—is expected to contract this year and recover only mildly next year. In South Africa, despite a moderate rebound in the second quarter, growth is expected to be weaker in 2019 than projected in the April 2019 WEO following a very weak first quarter, reflecting a larger-than-anticipated impact of labor strikes and energy supply issues in mining, together with weak agricultural production. While the three largest economies of the region are projected to continue their lackluster performance, many other economies—typically more diversified ones—are experiencing solid growth. About 20 economies in the region, accounting for about 45 percent of the sub-Saharan African population and 34 percent of the region's GDP (1 percent of global GDP), are estimated to be growing faster than 5 percent this year while growth in a somewhat larger set of countries, in per capita terms, is faster than in advanced economies.

Over the medium term, growth for the emerging market and developing economies group is projected to stabilize at about 4.8 percent, but with important differences across regions. In emerging and developing Asia, it is expected to remain at about 6 percent through the forecast horizon. This smooth growth profile rests on a gradual slowdown in China to 5.5 percent by 2024.

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