

# Global Economic Prospects: *A Fragile Recovery*

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Development Economics • Prospects

# Four Questions

1

How is the health of the global economy? *Recovery underway, broadly as expected*

2

How important is the expected acceleration in emerging markets for global growth?  
*Critically important; likely to lead to faster global growth*

3

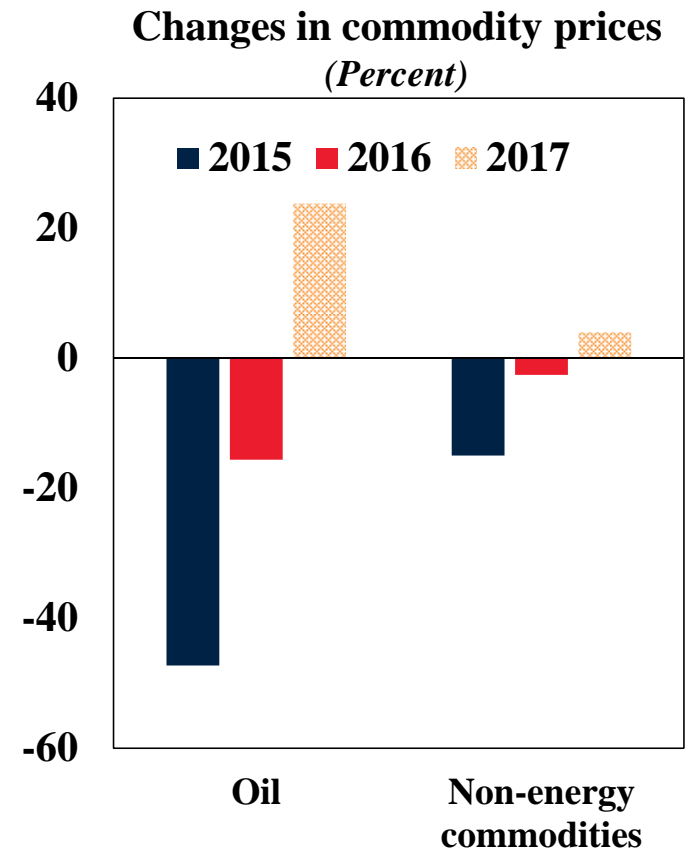
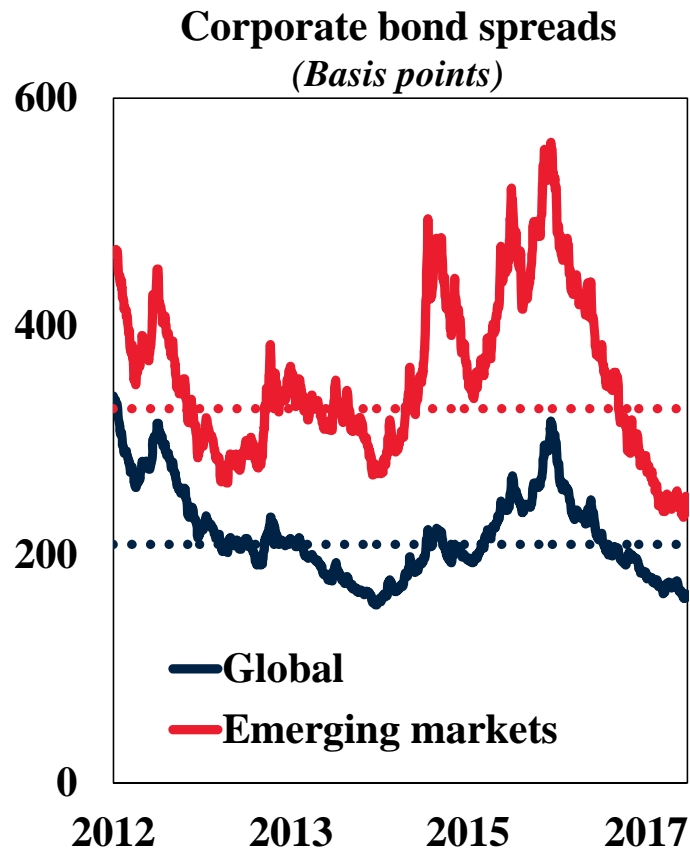
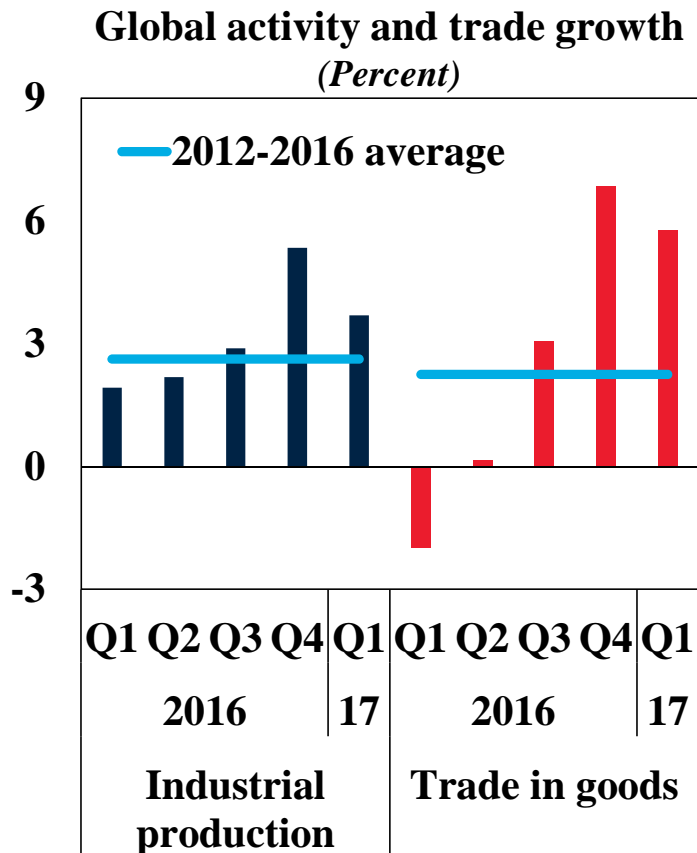
How have fiscal positions evolved in EMDEs since the global financial crisis?  
*Fiscal positions have become weaker in many EMDEs (Emerging Market and Developing Economies)*

4

What are the major risks and what policies could help? *Elevated policy uncertainty, financial stress, protectionism; policy flexibility combined with implementation of reforms*

# Global Backdrop:

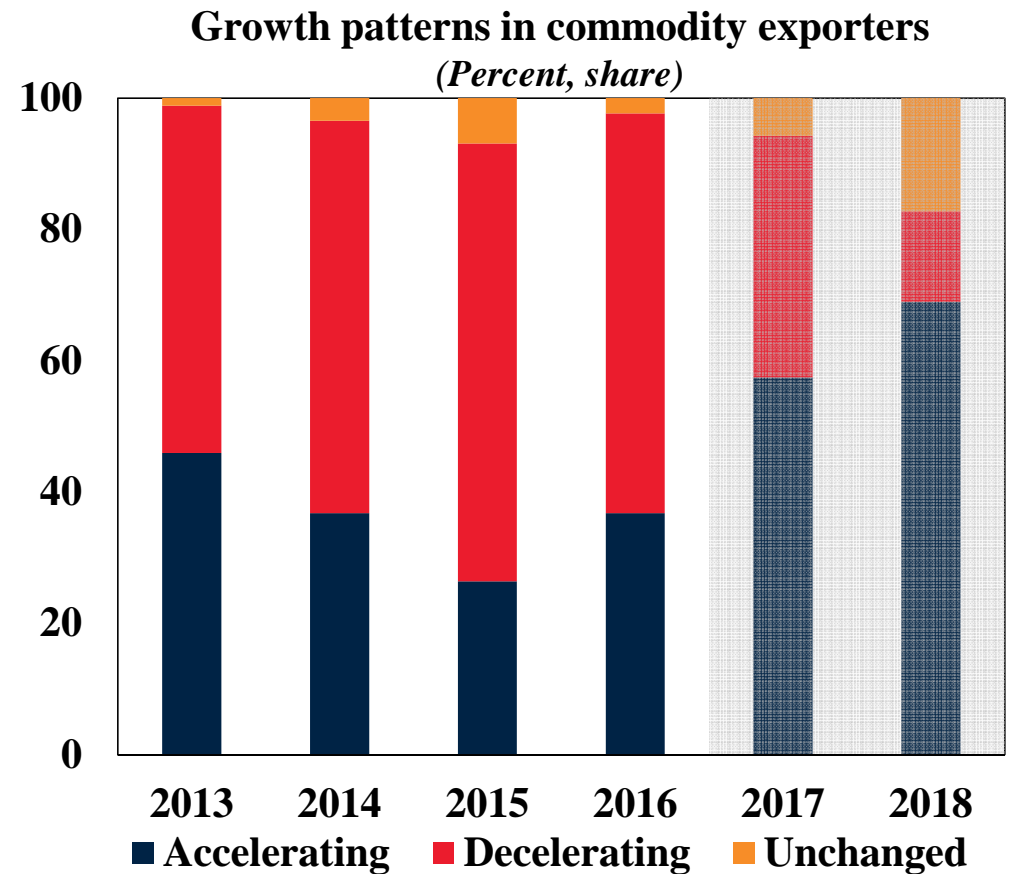
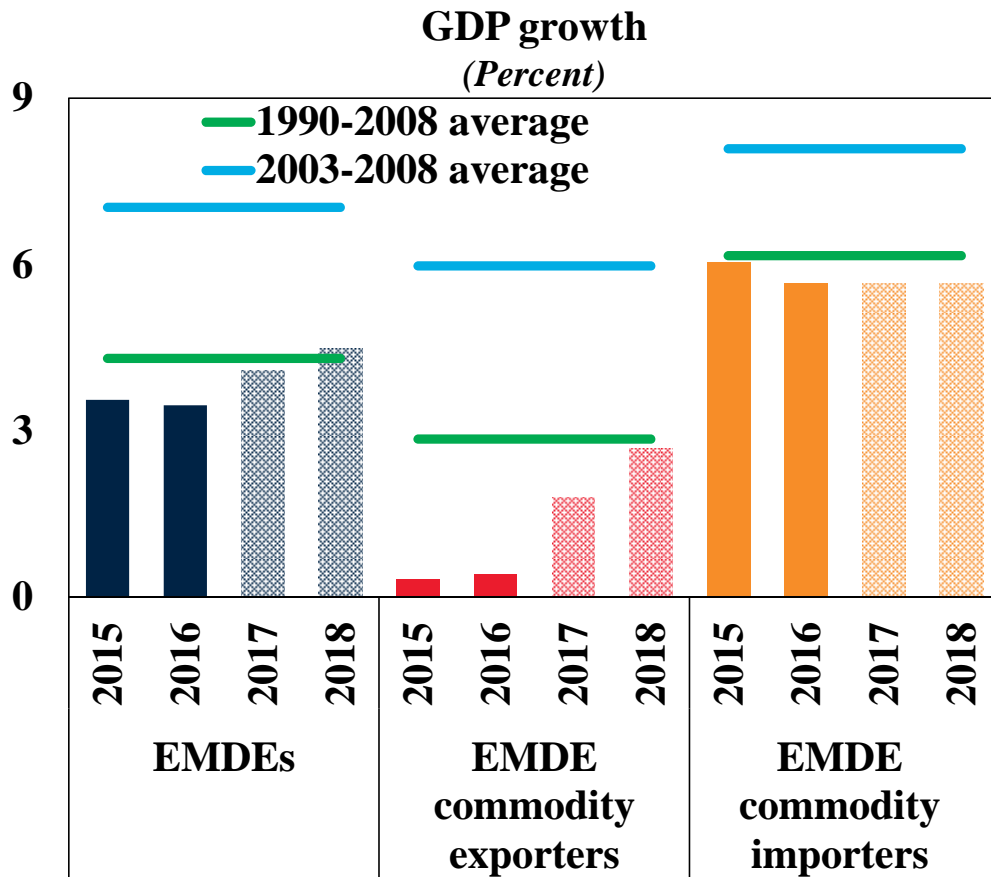
*Robust Trade Growth; Benign Financing Conditions; Increase in Commodity Prices*



Sources: Bloomberg, CPB Netherlands Bureau for Economic Policy Analysis, Haver Analytics, World Bank.

Left Panel. Quarter-on-quarter annualized growth rates. Last observation is March 2017. Center Panel. Dotted lines indicate the median values since 2005. Corporate bond spreads refer to spreads between yields on non-sovereign debt with at least 18 months to final maturity and U.S. Treasury yields of equivalent maturity. Individual bonds are weighted by market capitalization. Last observation is May 23, 2017. Right Panel. Percent changes in commodity price indexes. Data for 2017 are forecasts.

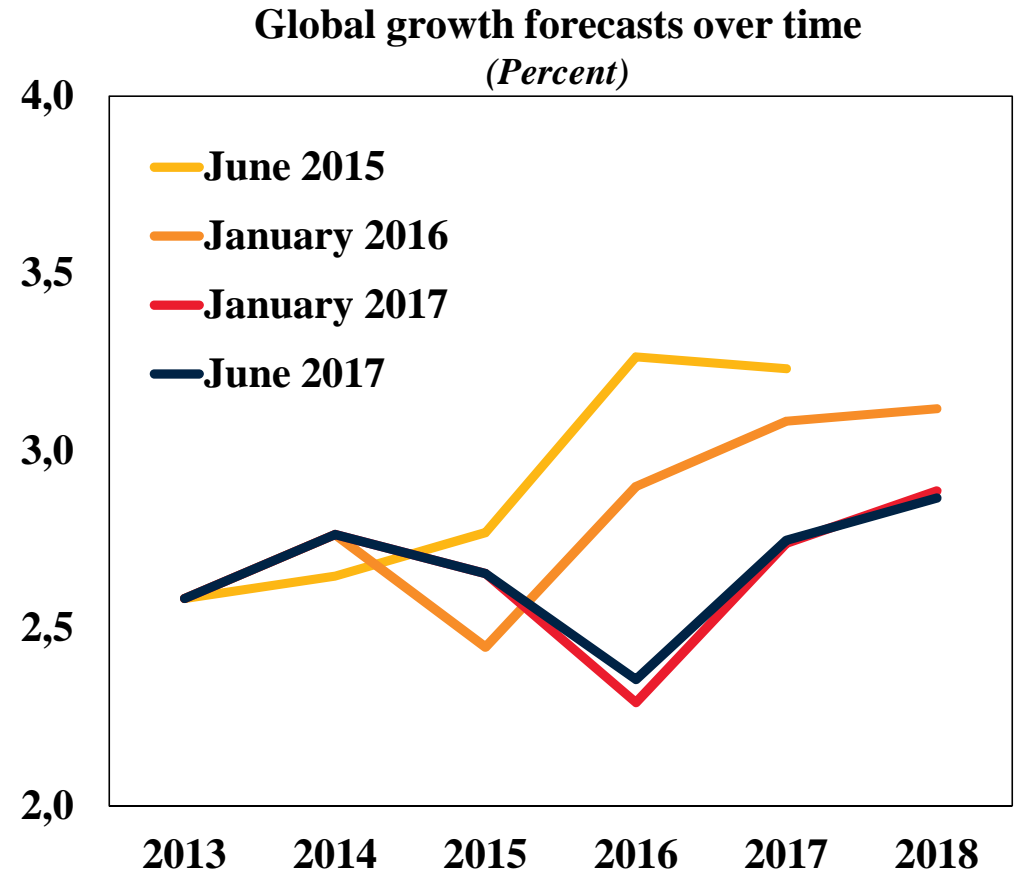
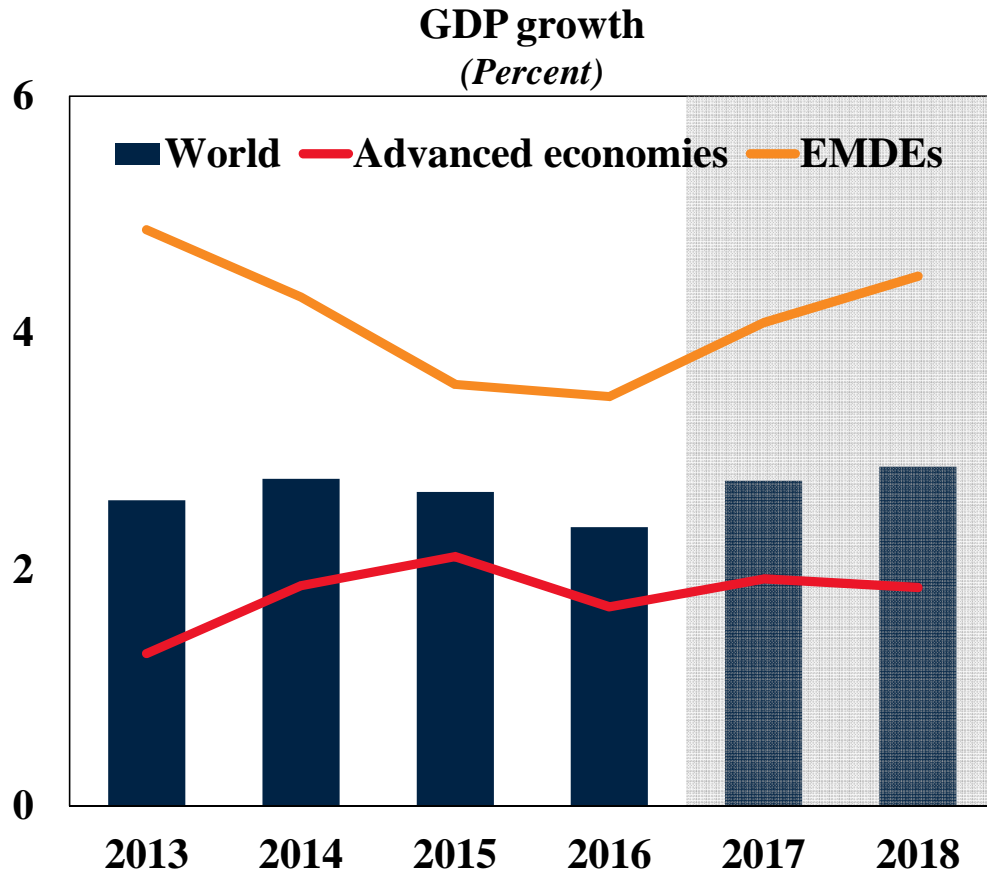
# Growth in EMDEs: *Diminishing Headwinds for Commodity Exporters*



Source: World Bank.

Left Panel. Shaded bars indicate forecasts. Right Panel. Accelerating (decelerating) growth is positive (negative) changes in growth rates from the previous year by at least 0.1 percentage point. Sample includes 87 commodity-exporting EMDEs. Shaded area indicates forecasts.

# Global Growth: *Gaining Momentum as Expected*



Source: World Bank.  
Left Panel. Shaded area indicates forecasts. Right Panel. The dates indicate the editions of *Global Economic Prospects*.

# Global and Regional Forecasts: Still Modest Global Expansion; Differences across Regions

	GDP growth (Percent)				
	2011-15	2015	2016e	2017f	2018f
<b>World</b>	2.7	2.7	2.4	2.7	2.9
<b>Advanced economies</b>	1.6	2.1	1.7	1.9	1.8
<b>EMDEs</b>	4.8	3.6	3.5	4.1	4.5
<b>East Asia and Pacific</b>	7.3	6.5	6.3	6.2	6.1
<b>Europe and Central Asia</b>	3.0	1.0	1.5	2.5	2.7
<b>Latin America and the Caribbean</b>	2.1	-0.8	-1.4	0.8	2.1
<b>Middle East and North Africa</b>	3.4	2.8	3.2	2.1	2.9
<b>South Asia</b>	6.4	6.9	6.7	6.8	7.1
<b>Sub-Saharan Africa</b>	4.2	3.1	1.3	2.6	3.2

Source: World Bank.

Note: e and f refer to estimates and forecasts (as of May 24, 2017), respectively. 2011-15 refers to the period average.

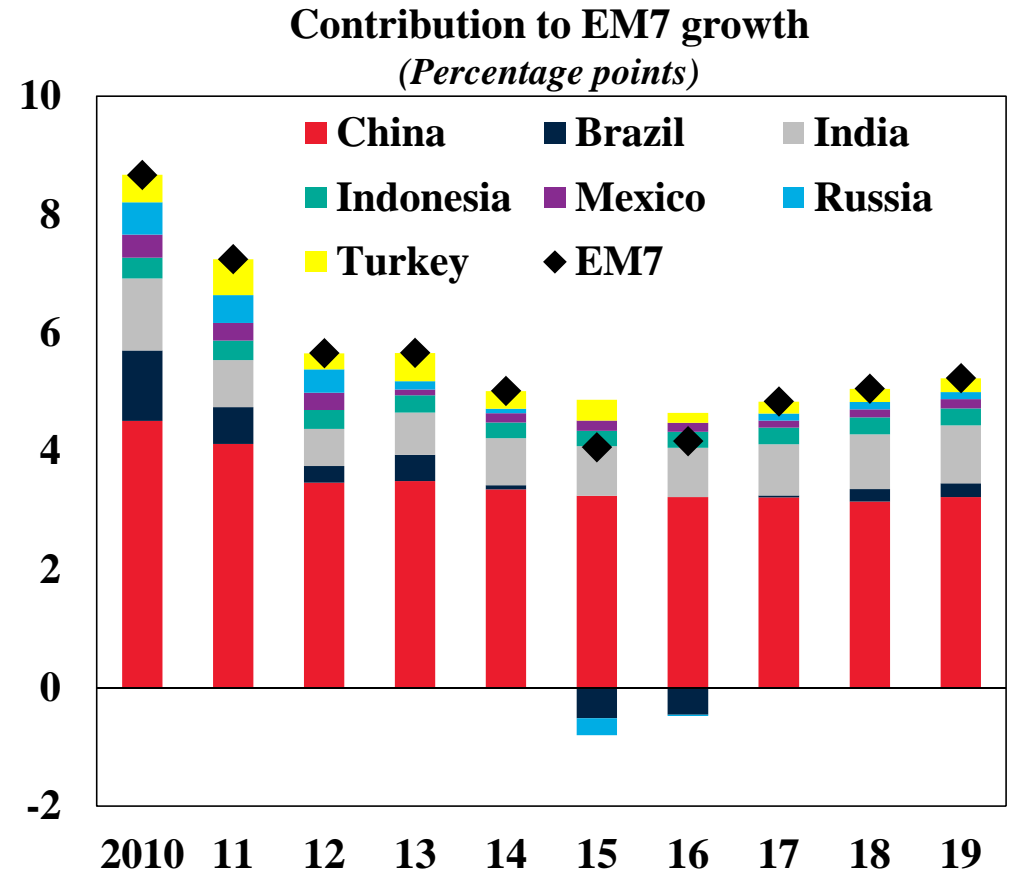
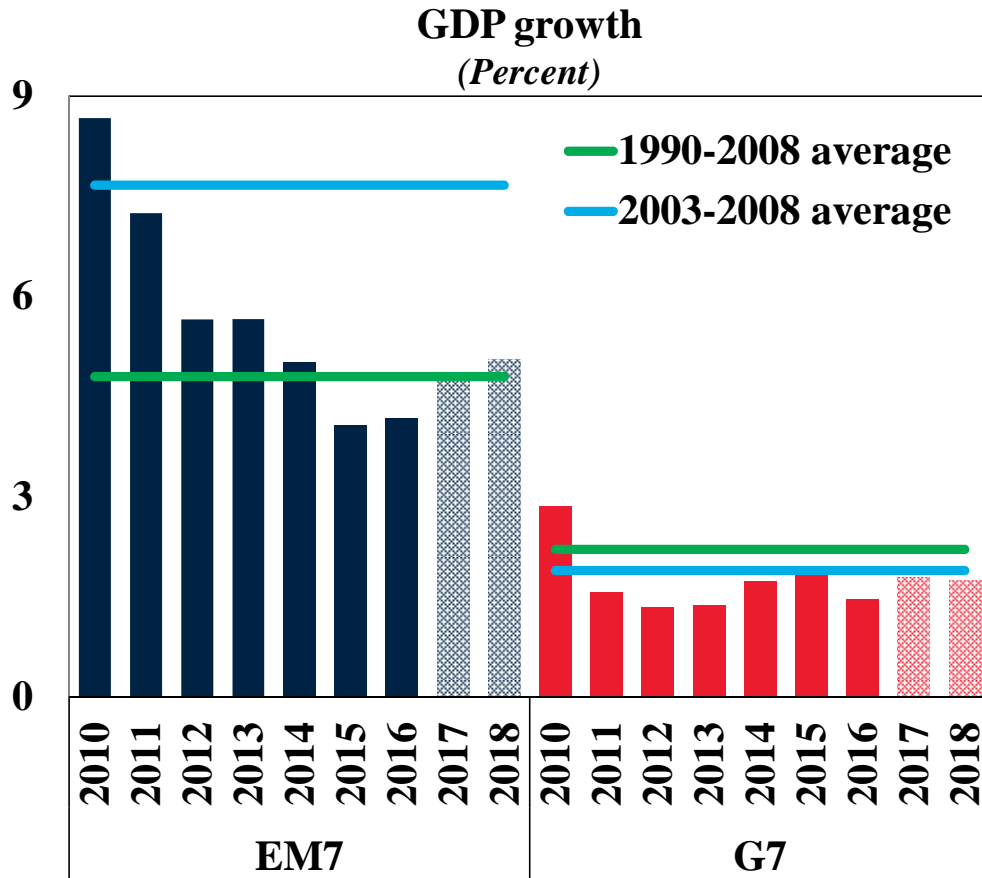
# Four Questions

2

How important is the expected acceleration in emerging markets for global growth?

*Critically important; likely to lead to faster global growth*

# Growth in EM7: *Gathering Momentum after a Prolonged Slowdown*

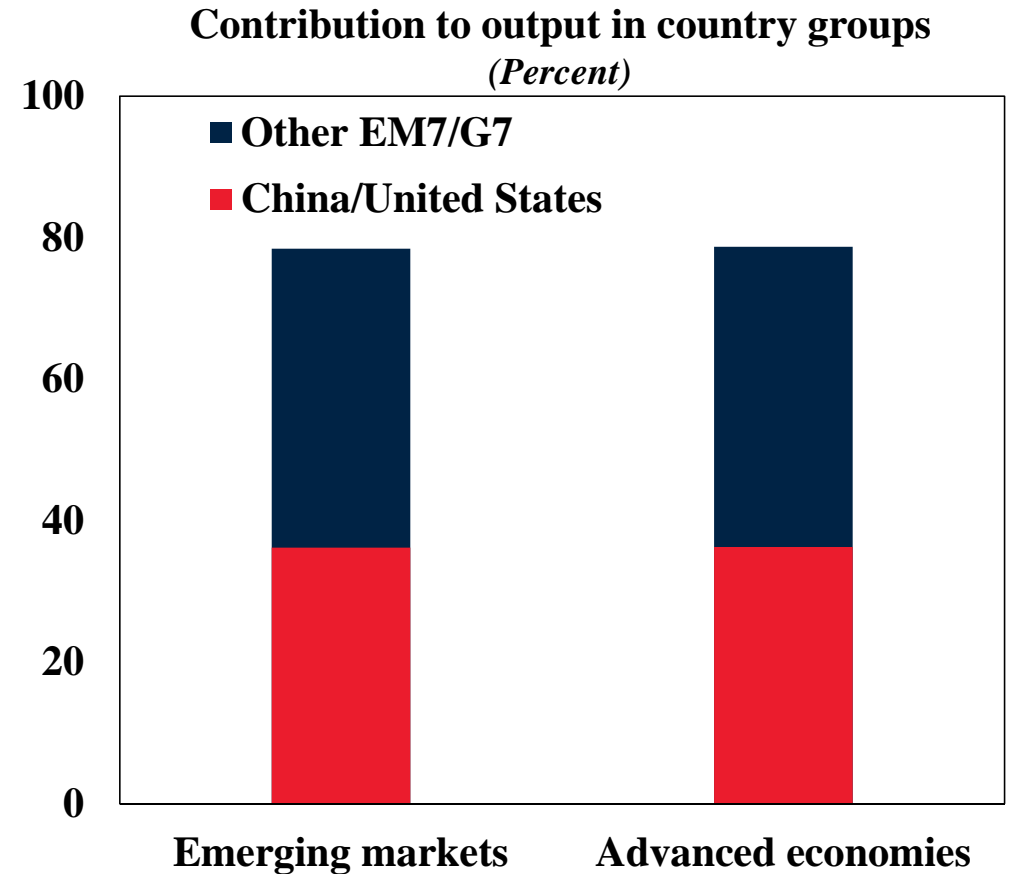
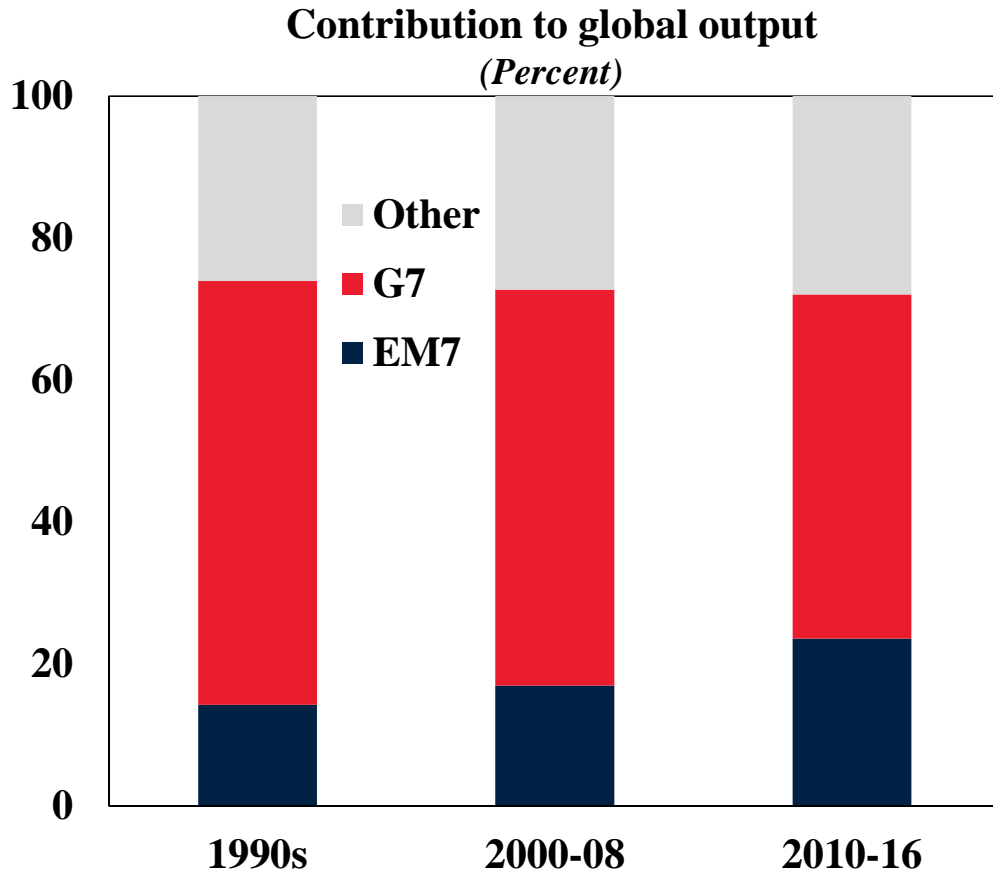


Source: World Bank.

Note: EM7 includes Brazil, China, India, Indonesia, Mexico, the Russian Federation, and Turkey. G7 includes Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. GDP-weighted averages. Left Panel. Shaded bars indicate forecasts. Right Panel. Growth rates over 2017-19 are forecasts.



# Global Role of EM7: *Increasingly Important*

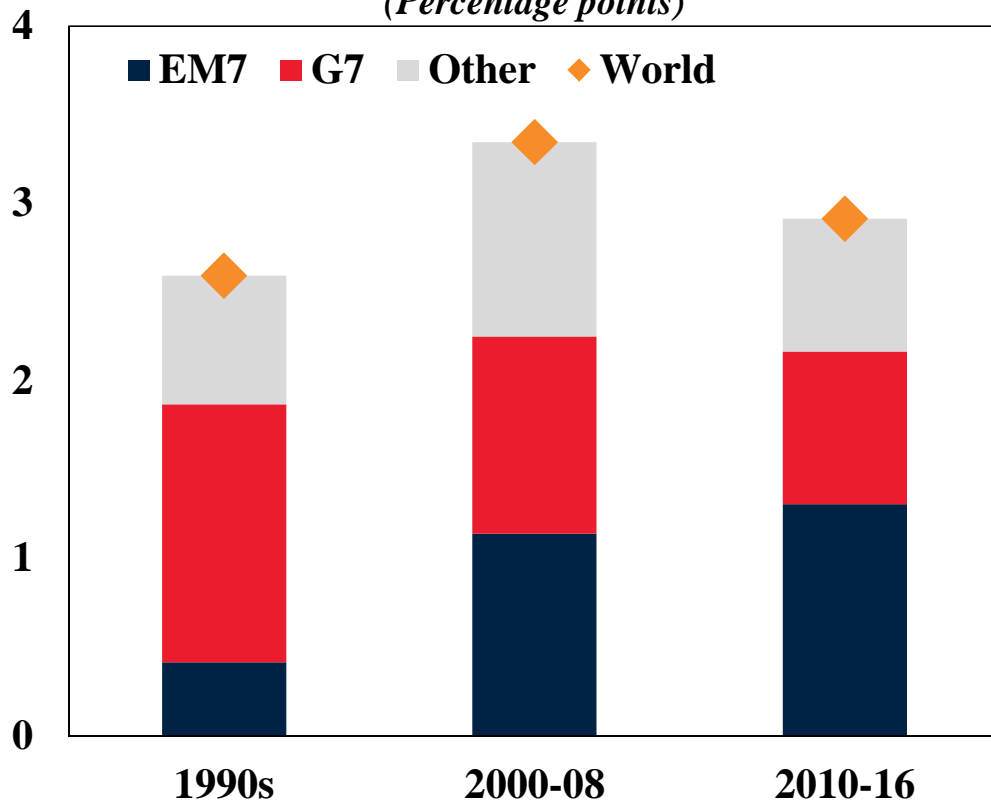


Source: World Bank.

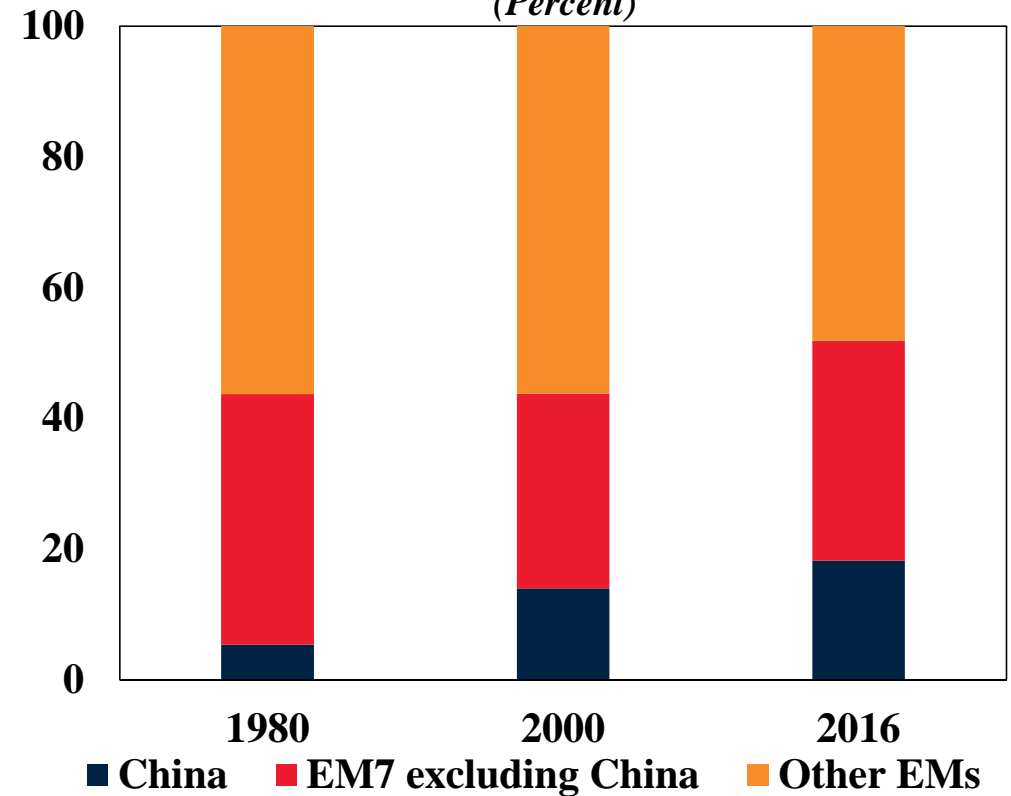
Note: EM7 includes Brazil, China, India, Indonesia, Mexico, the Russian Federation and Turkey. G7 includes Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. Output is measured in U.S. dollars at market exchange rates. Right Panel. Red bars show the share of EM7 (G7) in output in emerging markets (advanced economies). Blue bars show the output share of other EM7 (G7) members. Data refer to averages over 2010-16 and cover 23 emerging markets and 27 advanced economies as defined in Huidrom, Kose, and Ohnsorge (2017).

# EM7 Contribution to Growth and EM Trade: *Getting More Influential*

**Contribution to global growth**  
(Percentage points)



**Intra-emerging market goods exports**  
(Percent)

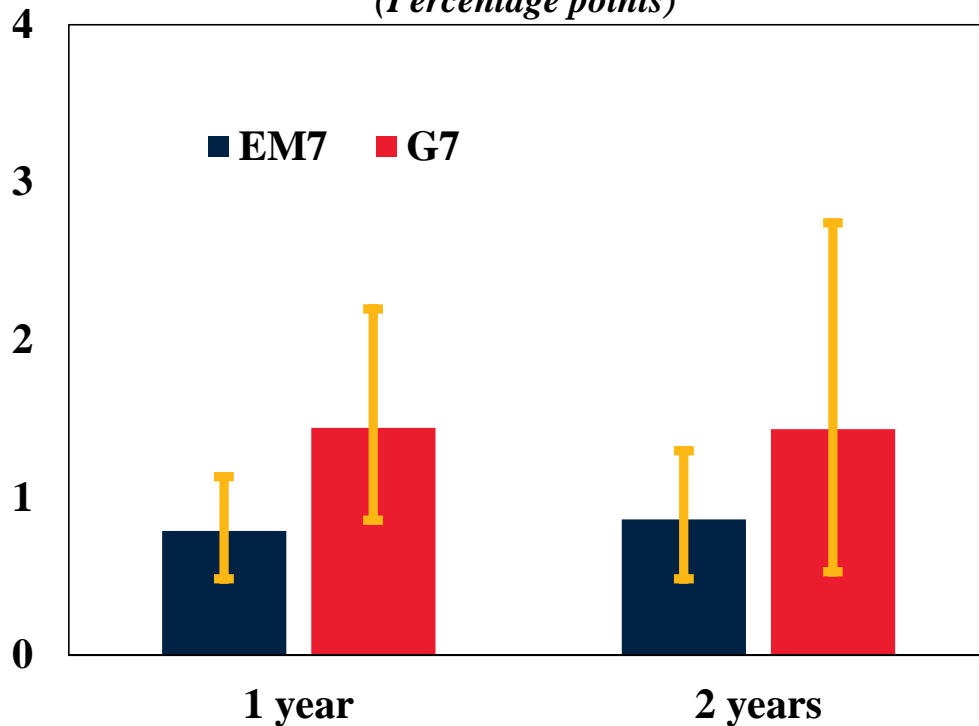


Sources: International Monetary Fund, World Bank.

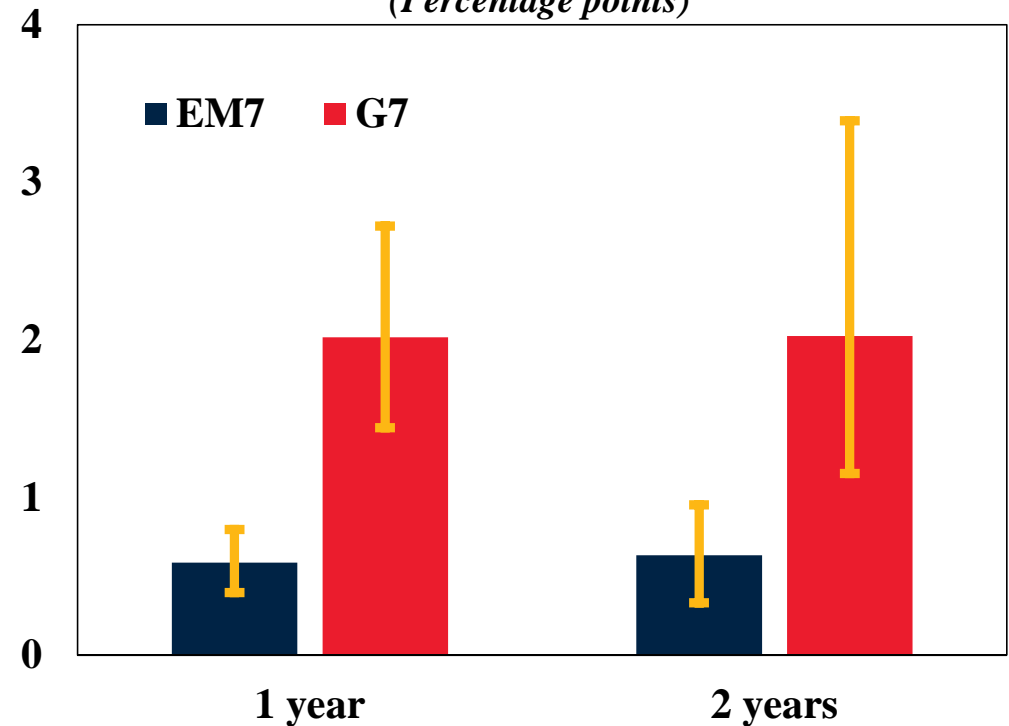
Note: EM7 includes Brazil, China, India, Indonesia, Mexico, the Russian Federation, and Turkey. G7 includes Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. Right Panel. EM refers to emerging market, covering 23 economies (Huidrom, Kose, and Ohnsorge 2017). Percent share of EM exports to other EM countries.

# Growth Impact of EM7: Quite Sizable but Smaller than G7

**Impact of 1-percentage-point increase in EM7 and G7 growth on growth in other EMDEs**  
(Percentage points)



**Impact of 1-percentage-point increase in EM7 and G7 growth on global growth**  
(Percentage points)



Source: World Bank.

Note: EM7 includes Brazil, China, India, Indonesia, Mexico, the Russian Federation, and Turkey. G7 includes Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. The model includes, in this order, G7 growth, the U.S. interest rate, Emerging Market Bond Index (EMBI), EM7 growth, oil prices, and growth in other EMDEs. Other EMDEs consist of 15 countries. Left Panel. Cumulative impulse responses of growth in other EMDEs, at different horizons, due to a 1-percentage-point increase on impact in EM7 and G7 growth. Right Panel. Cumulative impulse responses at different horizons due to a 1-percentage-point increase in EM7 and G7 growth on impact. Global impact is the GDP-weighted average of the responses of EM7, other EMDEs, and G7 countries. Solid bars represent medians, and error bars represent 16-84 percent confidence bands.

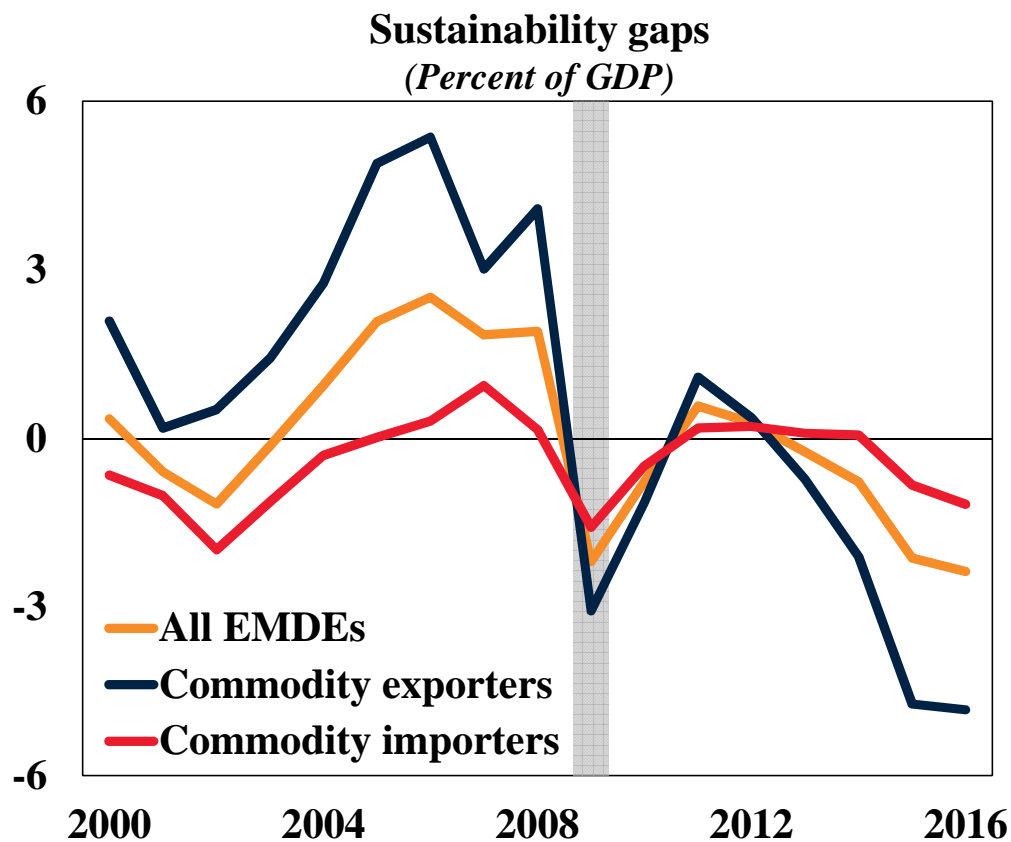
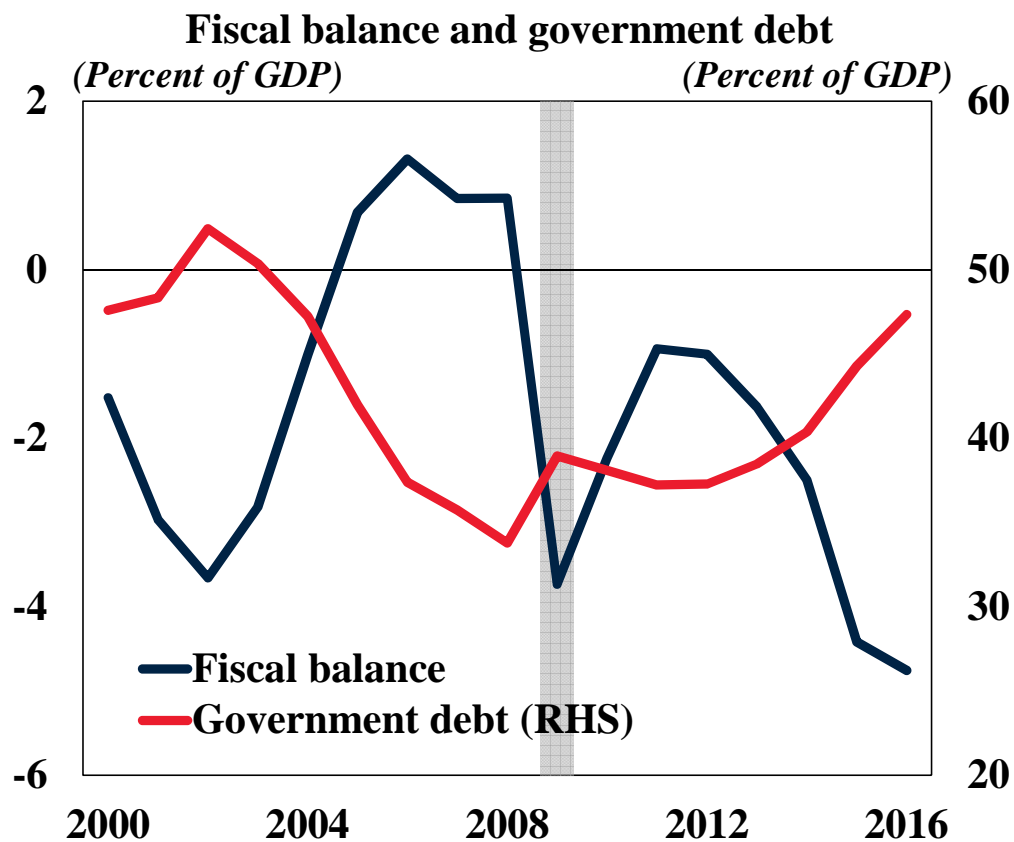
# Four Questions

3

How have fiscal positions evolved in EMDEs since the global financial crisis?

*Fiscal positions have become weaker in many EMDEs (Emerging Market and Developing Economies)*

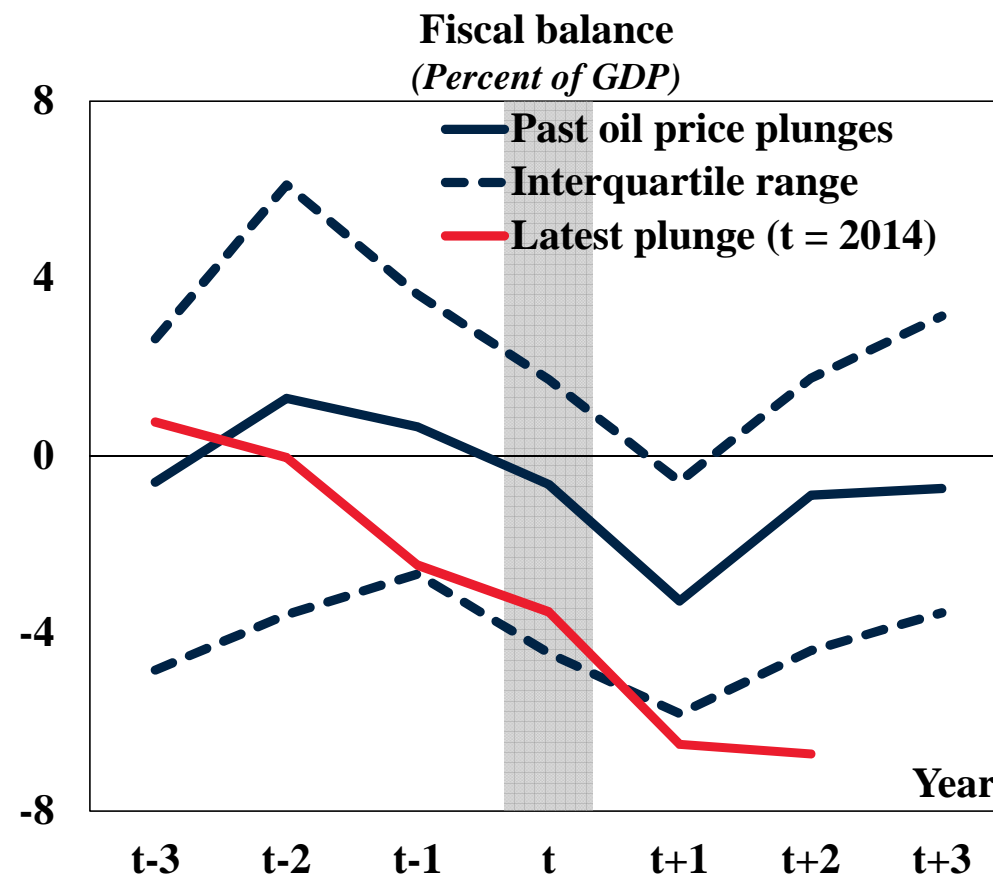
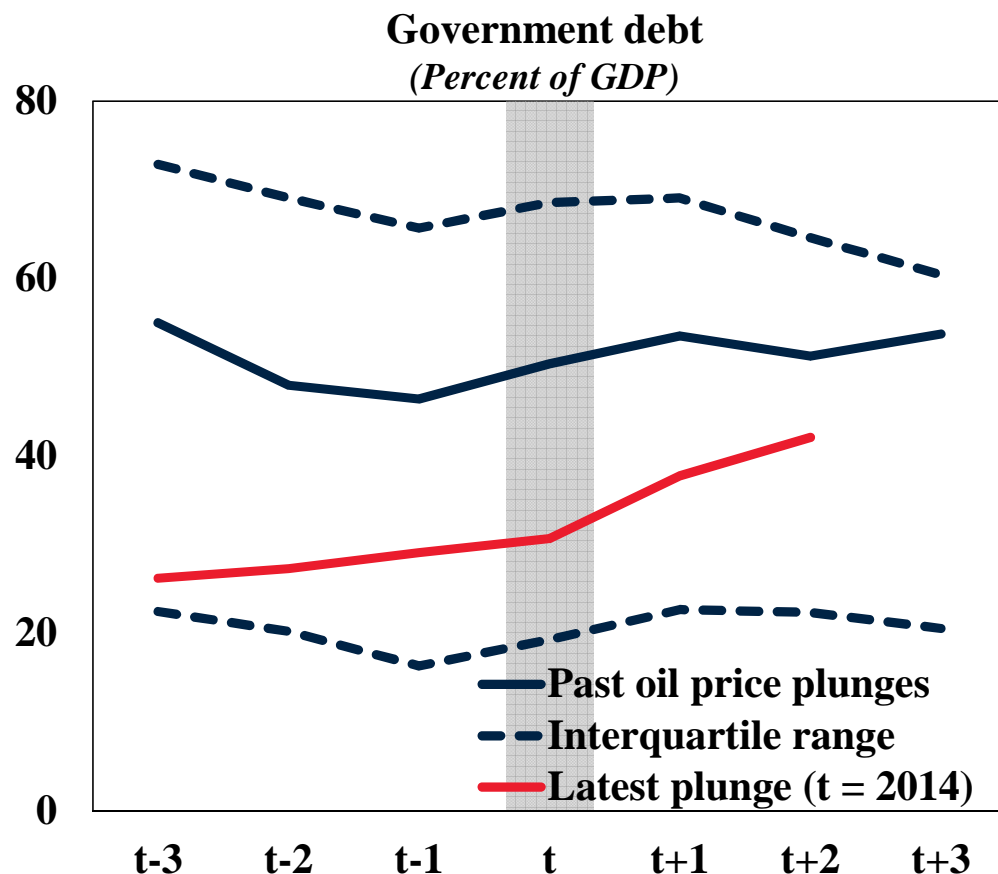
# Evolution of Fiscal Positions in EMDEs: *Becoming Weaker...*



Sources: International Monetary Fund, World Bank.

Note: GDP-weighted averages. The year of global recession (2009) is shaded in gray. Left Panel. Government debt refers to liabilities that require payments of interest and principal by governments and includes, for example, debt liabilities in the form of currency and deposits, debt securities, and loans. It is for general government; therefore, all transactions among government entities are consolidated. Right Panel. Sustainability gap is defined as the difference between the actual fiscal balance and the debt-stabilizing balance. The debt-stabilizing balance captures cumulative impact of sustained fiscal balances on debt stocks and computed with country-specific long-term average nominal interest rate and GDP growth and the historical median government debt levels. Sample includes 72 EMDEs, consisting of 44 commodity-exporting economies and 28 commodity-importing economies.

# Fiscal Positions in EMDE Oil Exporters: *Sharper Deterioration Now than Previous Oil Price Plunges*



Sources: International Monetary Fund, World Bank.

Note: Past oil price plunges include collapses in global oil prices in 1991, 1998, 2001, and 2008, as identified in the June 2015 *Global Economic Prospects*. Simple averages, based on 36 EMDE oil exporters. Government debt refers to liabilities that require payments of interest and principal by governments and includes, for example, debt liabilities in the form of currency and deposits, debt securities, and loans. It is for general government; therefore, all transactions among government entities are consolidated.

# Four Questions

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What are the major risks and what policies could help? *Elevated policy uncertainty, financial stress, protectionism; policy flexibility combined with implementation of reforms*

# Risks:

## *Tilted to Downside; An Upside Risk?*

### Downside risks

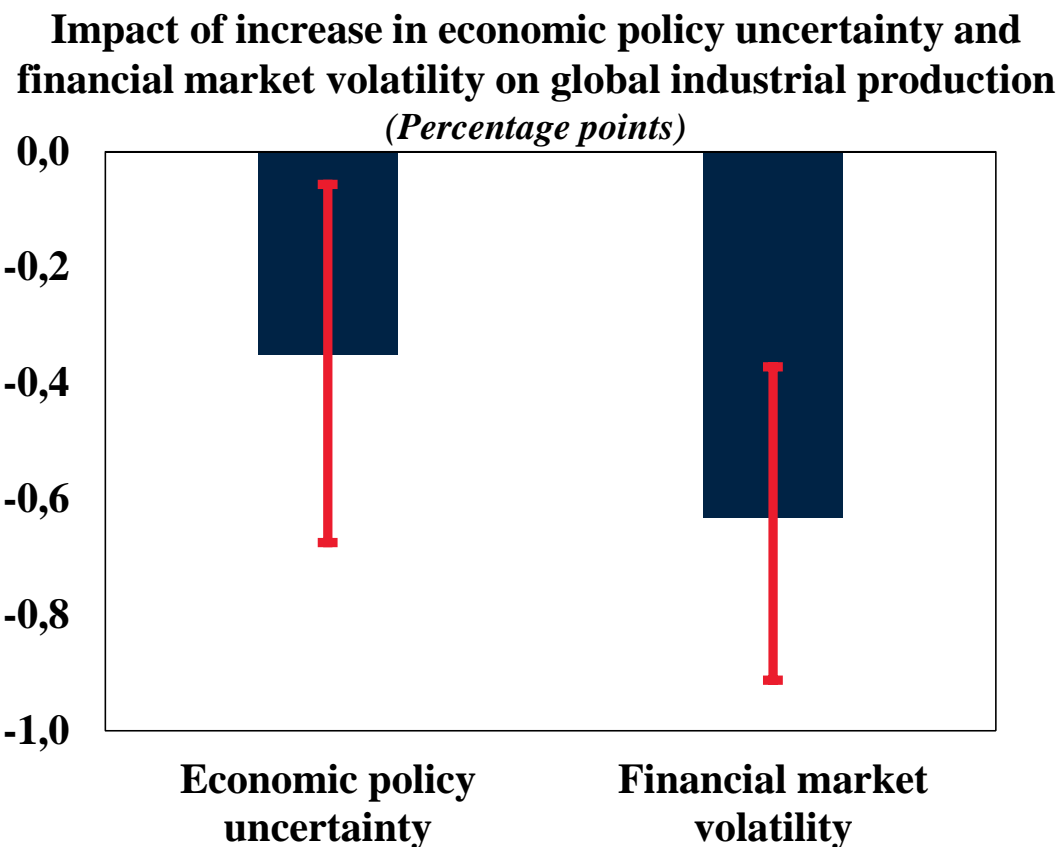
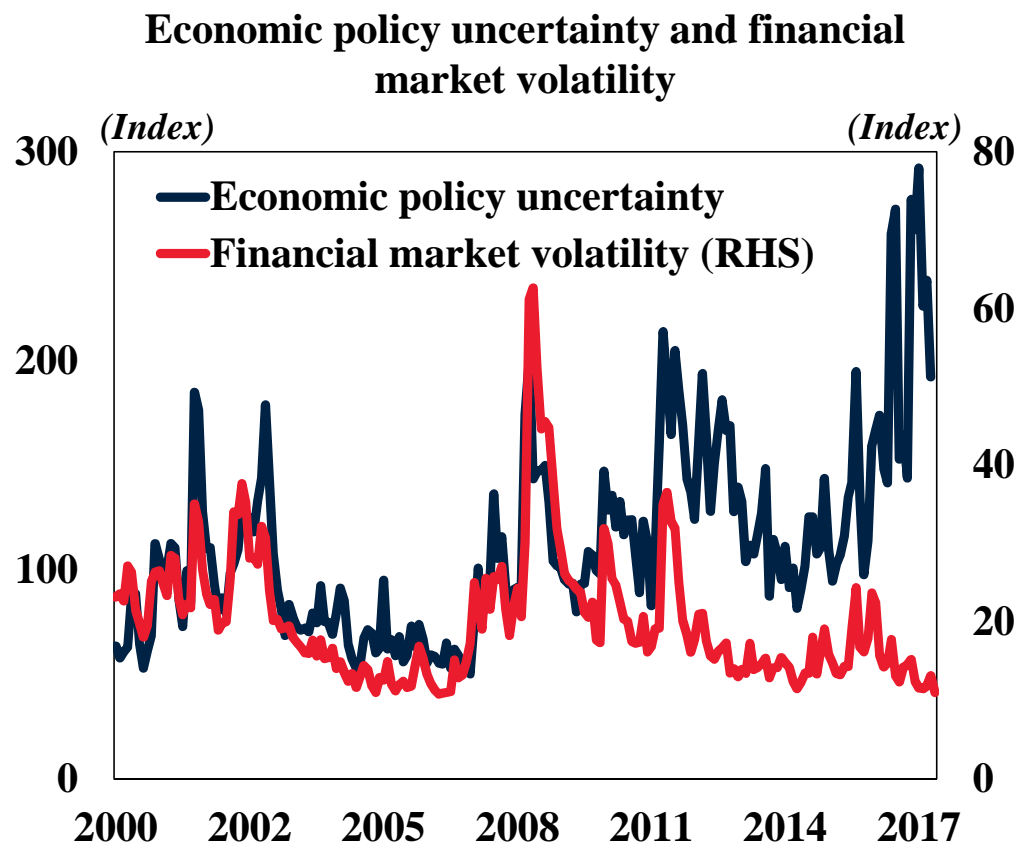
- **Elevated policy uncertainty**
- **Financial market stress**
- **Escalation of protectionist measures**
- **Geopolitical tensions**
- **Heightened volatility in oil markets (*especially for oil exporters*)**
- **Slowdown in potential growth**

### Upside risk

- **Fiscal stimulus in advanced economies**



# High Policy Uncertainty; Low Financial Market Volatility: *Complacency as a Source of Risk?*

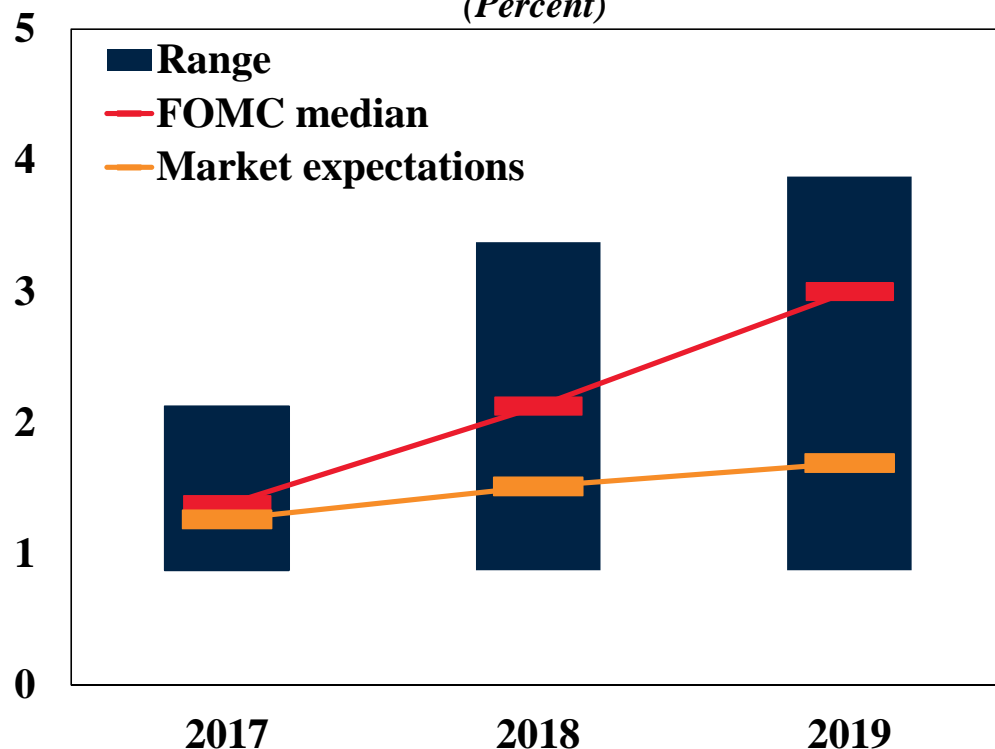


Sources: Bloomberg, Davis (2016), Haver Analytics, World Bank.

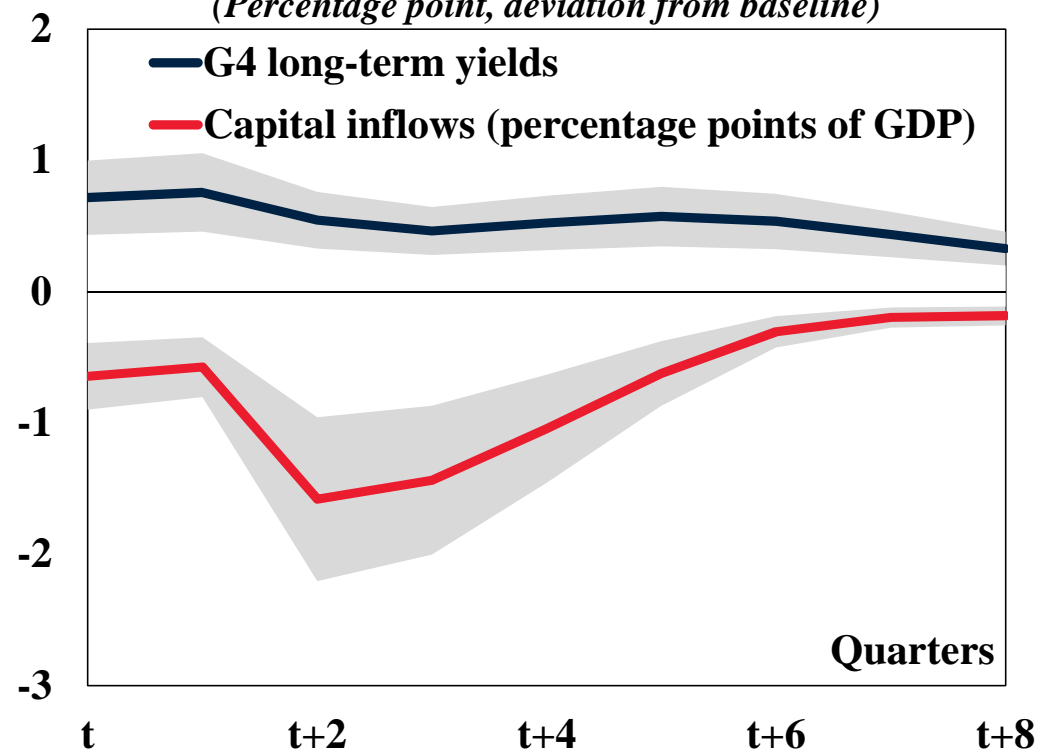
Left Panel. Economic policy uncertainty is the Economic Policy Uncertainty (EPU) index computed by Davis (2016). Financial market volatility is measured by VIX, which is the implied volatility of option prices on the U.S. S&P 500. Last observation is April 2017 for Economic policy uncertainty and May 2017 for financial market volatility. Right Panel. Cumulative impulse response of global industrial production growth after 12 months to a one-standard-deviation shock in global EPU and financial market volatility (VIX). Data are standardized for comparison. Estimation based on a Bayesian vector autoregression of global EPU, VIX, and global industrial production growth rate. Blue bars denote median responses and lines denote 16th-84th percentile confidence intervals. The sample period is from January 2000 to February 2017.

# U.S. Interest Rate Expectations and EMDE Capital Flows: *Gap in Rate Hike Expectations; Risk of Disruptions in Capital Flows*

**U.S. Fed policy interest rate expectations**  
(Percent)



**Impact of long-term yield shock in the U.S.**  
(Percentage point, deviation from baseline)

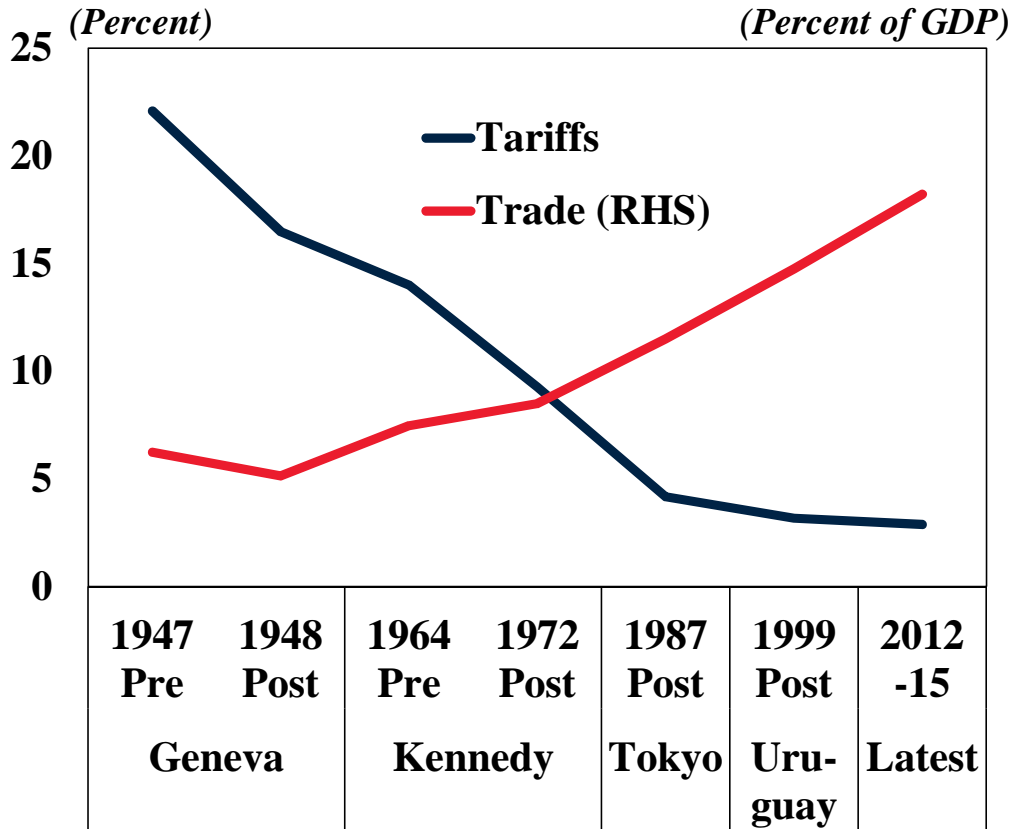


Sources: Federal Reserve Board of Governors, World Bank.

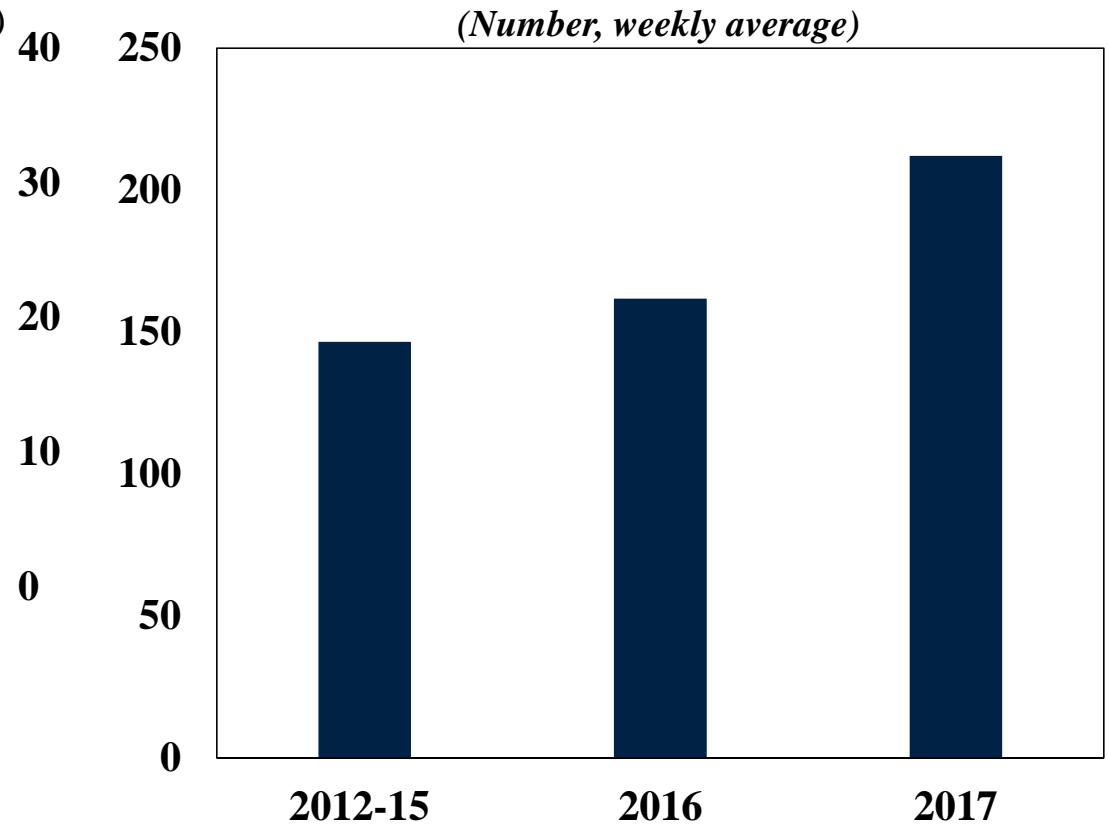
Left Panel. FOMC medians are for the end of the given year. Market expectations are based on overnight indexed swap rates (as of May 31, 2017). Right Panel. Impulse response of long-term yields of G4 countries (United States, Euro Area, Japan, and United Kingdom) and capital flows to EMDEs to a 100 basis-point increase in the U.S. term spread. The results are based on a six-variable VAR model that includes capital flows to EMDEs (including foreign direct investment, portfolio investment, and other investment as a share of GDP), quarterly real GDP growth in EMDEs and G4 countries, real G4 short-term interest rates (three-month money market rates minus annual inflation measured as changes in GDP deflator), G4 term spread (10-year government bond yields minus three month money market rates), and the VIX index of implied volatility of S&P 500 options. Gray area shows the range of estimates for different pass-through rates to bond yields in Euro Area, Japan and United Kingdom.

# Protectionist Sentiment: *Is the Clock Turning Back on Trade Liberalization?*

**Global trade and tariffs**



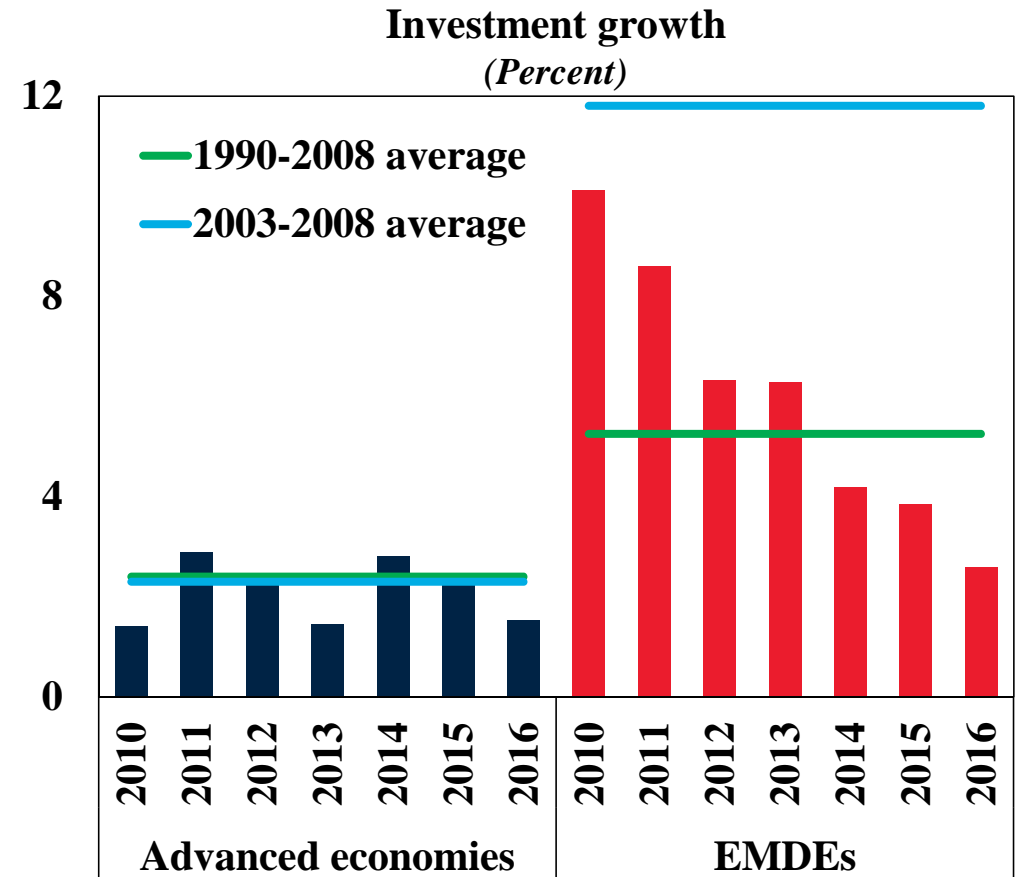
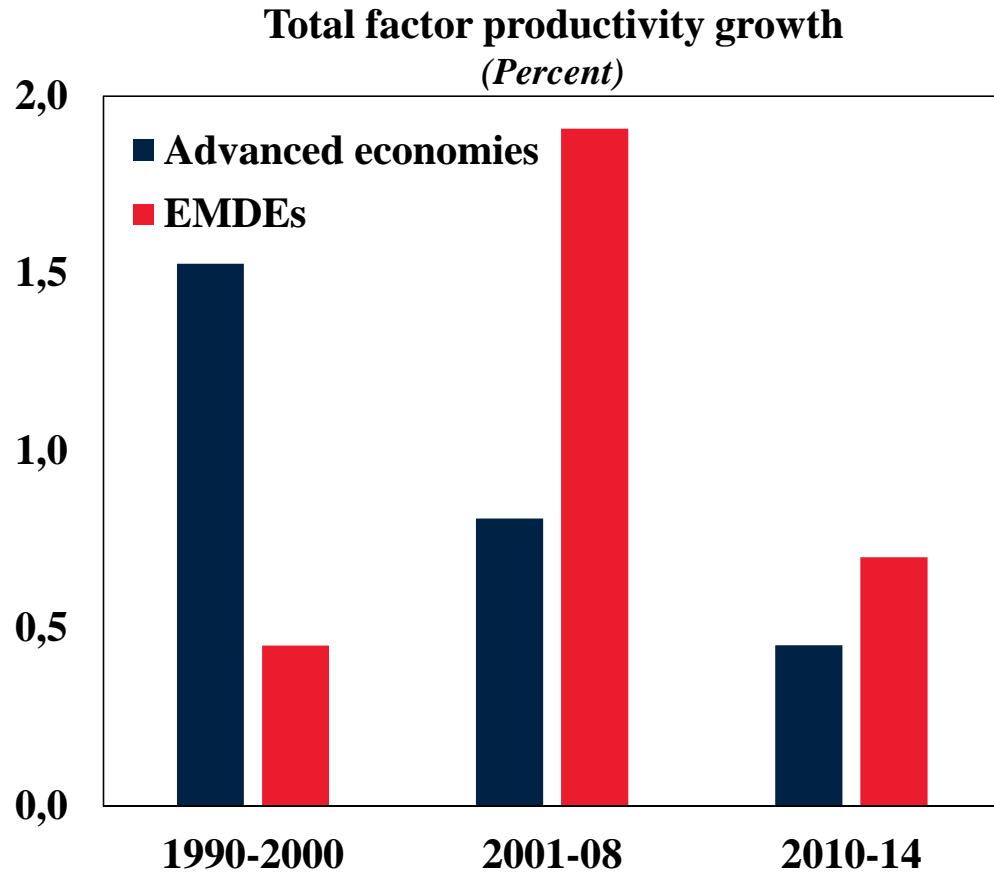
**Discussion of protectionism**



Sources: Bown and Irwin (2015), Google Trends, World Bank.

Left Panel. Global trade is defined as the sum of exports and imports in percent of global GDP. Applied tariff rates based on weighted average for all products. Right Panel. Weekly average Google Trend search for “protectionism,” “trade restrictions,” “trade war,” and “import tariffs.” Average for 2017 is year-to-date. Last observation is the third week of May, 2017.

# Serious Medium-Term Challenges: *Deteriorating Growth of TFP and Investment*



Sources: Feenstra, Inklaar, and Timmer (2015); Haver Analytics; International Monetary Fund; Oxford Economics; World Bank.

Left Panel. Average TFP growth, measured at constant national prices and weighted by GDP in constant 2011 prices. Sample includes 28 advanced economies and 68 EMDEs. Right Panel. Weighted average of gross fixed investment growth, measured in constant U.S. dollars, based on 36 advanced economies and 87 EMDEs. Long-term average for EMDEs starts in 1991 due to the data availability.

# Policy Responses:

## *Depends on Country Context; Implementation is Key*

### **Monetary and financial sector policies**

- Objective: Strike a balance between growth, inflation, and financial market stability
- *Challenge: How to institute a credible policy framework? How to decouple policy from the U.S. Fed?*

### **Fiscal policy**

- Objective: Strike a balance between fiscal stimulus and fiscal sustainability
- *Challenge: How to undertake broad revenue and expenditure reforms?*

### **Structural policy**

- Objective: Implement comprehensive medium-term plans
- *Challenge: How to accelerate the pace of policy implementation?*

### **Global policy coordination**

- Objective: Facilitate responsible integration of trade and finance; Address global challenges
- *Challenge: How to build consensus?*

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- 4 What are the major risks and what policies could help? *Elevated policy uncertainty, financial stress, protectionism; policy flexibility combined with implementation of reforms*

# Lifting Clouds?

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# Select Publications on Global Economy

- *Global Economic Prospects* – *June 2017*
- *Commodity Markets Outlook* – *April 2017*
- *Global Monthly and Global Weekly*
- *A Cross-Country Database of Fiscal Space*  
*Policy Research Working Paper* – *Forthcoming*
- *Weakness in Investment Growth: Causes, Implications and Policy Responses*,  
*Policy Research Working Paper* – *March 2017*
- *Regional Dimensions of Recent Weakness in Investment: Drivers, Investment Needs and Policy Responses*,  
*Policy Research Working Paper* – *March 2017*
- *The Global Role of the U.S. Economy: Linkages, Policies and Spillovers*,  
*Policy Research Working Paper* – *February 2017*

# ***Questions & Comments***

## ***Thanks!***

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