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Briefing Paper

ECONOMIC FORECASTS FOR THE THIRD WORLD

Most of the major international agencies now publish forecasts for developing countries. Policy-makers, public and private, must take decisions and actions whose success depends on future conditions. The economic events of the last ten years have made it both more difficult and more necessary to forecast these correctly, particularly for the third world.

The succession of oil price rises and falls and sharp changes in policies in the major industrial countries have brought much larger movements in the international economy than before 1973. It is no longer possible for developing countries to concentrate on long-term development, ignoring short-term changes in demand and policy in the rest of the world. Even fluctuations which return to normal, if they are on the scale of recent years, may require them to make major and rapid adjustments which seriously affect their medium-term performance.

After ten years of short-term difficulties there is increasing uncertainty about normal growth, for developed or developing countries. Have structural changes shifted them to a permanently lower level of output, or to lower rates of growth? Finally, the increasing participation of the developing countries in trade and in international capital markets has increased their vulnerability to external events.

In the last four years, the forecasts have not correctly identified the major changes in output and trade, although they have been somewhat better on prices; they all failed to predict the sharp decline in developing country growth since 1981. Nevertheless, provided a user takes note of the main points of risk, and is aware of any biases stemming from the objectives or assumptions of individual forecasters, they offer the only guide available through the conflicting indications of the latest economic news. This paper will therefore examine the main forecasts published this year *(see inset for list and for the definitions used in them).*

IS THERE AN ECONOMIC CRISIS?

Most forecasters take a very pessimistic view. Here we indicate, for each forecast, whether it views the situation as critical and which problems are particularly important. **UNCTAD** argues that 'the immediate outlook for the developing countries is grim', citing doubts about the strength of the recovery in the developed countries, the fall in lending to developing countries, and import controls in the industrial countries. It believes the recovery will need government intervention to sustain it. For the **UN**, the 'outlook for developing countries is bleak', with the external environment becoming worse. It fears that falling living standards could disrupt the social and political fabric of several countries, and does not have confidence that the recovery will be sustained. The **EIU** suggests that developing countries risk 'unrest', and that they 'can only react with anger to the performance of the Western economy over the last three to four years'.

The **World Bank** seems the least worried. It sees some problems from import controls but it does not expect them to have a serious effect on manufactured exports. It does not believe that the long term potential for growth has altered fundamentally in either the developed or the developing countries. 'The world debt situation is manageable', and the problems are temporary, not structural, because there have been no changes in basic conditions that would affect the assessments made when the loans were granted. It does admit that, on present trends, even its lowest forecast is optimistic.

The other forecasters do not summarise their views as dramatically. The **IMF,** however, emphasises that policies will be necessary to support the recovery which its forecasts assume, implying that it does not consider this recovery to be self-sustaining. Although it does not spell out in detail the effects of failure to adopt such policies, it emphasises the serious consequences for the developing countries. The **OECD** and **NIESR** also concentrate on specific problems, not broad assessments. Some international organisations do not publish detailed forecasts, but do take positions on these general questions. They support the pessimistic forecasters. **GATT** believes that the recovery is only a cyclical swing,

FORECASTS DISCUSSED AND PRINCIPAL DEFINITIONS

Forecasts by International Organisations

Bank for International Settlements, *Annual Report,* **BIS.**
General Agreement on Tariffs and Trade, *International Trade,* **GATT.**
have International Monetary Fund, *World Economic Outlook,* and revisions announced in September, **IMF.**
Organisation for Economic Cooperation and Development, *OECD Economic Outlook,* July, **OECD.**
have United Nations, *World Economic Survey,* **UN.**
United Nations Conference on Trade and Development, 2 *Trade and Development Report,* and revisions announced in October, **UNCTAD.**
have World Bank, *World Development Report,* **World Bank.**

Forecasts by independent UK forecasters

2 Economist Intelligence Unit, *World Outlook,* **EIU.**
National Institute of Economic and Social Research, have *National Institute Economic Review,* August, **NIESR.** May

Definitions

Oil price: average OPEC official export price; 'real': deflated by price of manufactured exports.

Price of manufactured exports: UN index for developed countries.

Price of Primary Exports: UNCTAD index, market prices of developing country exports.

Major oil exporters: Algeria, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Oman, Qatar, Saudi Arabia, United Arab Emirates, Venezuela.

that 'the capital shortage, international indebtedness and protectionism are problems whose solution will take more time' and refers to 'the payments crisis of the most heavily indebted countries'. The **BIS** believes that to sustain the recovery and 'to keep the international debt situation within manageable bounds' are 'both major, immediate policy challenges'. It also emphasises that the solutions that are found for what it sees as the immediate crisis could have damaging effects on long term prospects.

All the forecasters except the World Bank thus agree that the developing countries face at best moderate growth, with several areas of severe risk. Why do they reach these conclusions?

FORECASTS FOR 1983-1984

At present, most forecasters treat the growth of developing countries as constrained by external conditions. The countries require imports both for consumer necessities (food and fuel) and to supply their investment and production programmes. Their exports are limited more by demand than supply, so this means that their growth is determined by the level of activity in the industrial countries, by the world prices for their imports and exports (their terms of trade), and by the limits on what they can borrow to permit higher imports than exports.

Industrial countries and world trade

All forecasters expect these countries to grow slowly on average in 1983, but more rapidly in the second half than in the first, with this higher rate continuing into 1984 *(see table 1)*. Because they fear that structural changes may have reduced potential output, most think that 1984 growth could be less than the 3-3½% which they forecast, although for a recovery even this is historically low. Their imports are expected to grow at the same rate as total output in 1983. In the past imports generally grew faster than output, but this has not been true recently; this is one area of possible structural change. The forecast for 1984 that they will rise faster than output is thus risky, and the UN explicitly questions this consensus.

Most forecasters expect the volume of imports by the major oil exporters to fall or at best remain flat in 1983, with little recovery next year. These forecasts together imply that total world trade will be static in 1983, and rise by 4- 5% in 1984.

Volume of exports by non-oil developing countries

The improvement which the forecasters expect in 1983 (from 0 in 1982 to 3-6%) is much greater than can be explained simply by the rise for total world trade (from −2% to 0%). It comes mainly from manufactures, where trade fell 2½% in 1982, although exports by primary producers are also expected to improve, from 1-2% to around 5%. The UN takes a cautious view, suggesting that the costs which result from high interest rates will discourage rebuilding of stocks of primary commodities. They also fear increasing trade barriers will slow the increase in market share of developing countries' manufactured exports. Their poor performance in 1982 confirms that it is risky to assume that the increases in market share which have occurred in a few recent years will be repeated. Given stagnant world trade, and forecasts (and some data) for industrial countries' exports suggesting that these will be flat or rise slightly, even if there is a small further fall in oil countries' exports these forecasts leave little room for any rise in exports by the non-oil developing countries.

In contrast to these 1983 predictions, the rises in market share expected in 1984 are at best modest. If the recovery in the developed countries does continue, export growth of around 4-5% may be achievable.

Table 1 **General Forecasts for 1983-1984**

(percentage growth rates)

	1983						1984				
	UNCTAD	IMF	OECD	UN	EIU	NIESR	UNCTAD	IMF	OECD	UN	NIESR
Developed countries' Output	>2.0	1.9	2	2	1.6	1.9	3.2	3.5	3½	3.0	3
Developed countries' import volume	0.8	2.0	¾	2.5	1.4	2	5.0		5	3.5	4.5
Oil exporters' import volume	0.0	−8.0	−10¼	5	4	−13	0.9		2½	7	
World trade volume[a]	0.2	0.5	−¾	2	1.5	1	4.5	4.5	4¾	4	4
Volume of trade in manufactures			0			1½			4		4
Oil price, US $	−12.4	−13.7	−12.2	−15			5.0	−1	−1.9	5	−1
Oil Price, real	−13.3	−15.4	−12.2	−17.5		−14.5	0		−5	0	−5
Price of manufactured exports	1.0	2.0	0	3		1.5	5.0		3¼	5	4.1
Price of primary products	>0	5	1	1		5	7.2	11	7	7	8
Food	) 5.5		) −1	−6		) 4	) 4.7		) 3½	9	) 7
Tropical beverages	)		)	5		)	)		)	4	)
Vegetable oilseeds & oils	−6.9		−7½	−9		)	14.8		2¾	7	)
Agricultural raw materials	4.7		8	3		7	8.0		8½	8	10
Minerals, ores, metals	3.0		10½	5		3	9.3		7½	10	9
Non-oil developing countries											
Output	1.7	<1.75		2.5			4.2	3.7		4	
Consumer prices		40						25			
Export volume	5.9	4.7	3	4	2		5.4		6	5	
By exporters of manufactures	7.2	4.9	3				6.9		8		
Import volume	2.2	2.3	−1¾	−1.5	−1		4.9		5	5	
Export prices		1.6	−4	0.5					4		
Import prices		0.4	−2	−1.5					3		
Terms of trade	2.7	1.2	−2	2			0.2		1		

[a]*GATT, World Trade 1983: 0*

Source: See inset, page one.

International prices

For 1983, forecasts are close together, with almost all forecasters expecting little change or small rises for manufactures and primary products and no further change in the oil price. For 1984, there is a split between those who expect no change in oil's dollar price, and those who expect it to keep pace with the price of manufactured exports. Roughly unchanged oil market conditions seem a reasonable expectation if end-1983 growth rates in the industrial countries do persist; the difference between the forecasts is small relative to recent movements. Price forecasts for primary commodities and manufactures range from 0 to 5% for 1983, with most forecasters expecting primary prices to rise slightly more. This is plausible, given recovery in the industrial countries. Expectations for 1984 are for a further relative rise. Forecasts for export and import prices of the developing countries follow directly from these; almost all forecasters expect small improvements in their terms of trade in both years.[1] The most recent data on prices support a small improvement in 1983, of the order of 1%.

Financing

The debt problems faced by developing countries have caused most forecasters greatly to increase the attention they give to the availability of all forms of finance. UNCTAD, the IMF and OECD publish detailed forecasts; NIESR, the UN and the BIS consider the question in some detail. All now assume that the quantity will be limited by the industrial countries, not by the amount developing countries want to borrow. Most do not expect any significant change in **development assistance**; the OECD expects a small rise. In 1982, the total is estimated to have fallen slightly despite an apparent rise from OECD countries because of reductions from OPEC. The fall in their income from oil makes further OPEC cuts possible in 1983 and 1984; the cautious forecasts seem reasonable. The UN predicted difficulties in increasing the funding of the multilateral agencies and these have occurred. The IMF was the most optimistic about its own lending, expecting it to double in 1983, to $14 billion. Most also expect little change in **direct investment** from producers in industrial countries. The general reduction in investors' expectations about growth and the debt problems suggest this could be optimistic (the UN expects a fall), but the amounts are small. There appear to be no major disagreements on these types of finance; the net rise could be $3-5 billion.

Private banking flows accounted for most of last year's fall in financing and are much more uncertain than other finance for 1983-1984. Preliminary evidence suggests that lending is contracting sharply. The OECD thinks that there is a risk that it could fall even more than the $8 billion they forecast (giving a range of $5-10 billion) because of 'greater prudence' on the part of lenders. The IMF gave the same range. UNCTAD forecast a fall of over $10 billion. The UN and NIESR also expected falls.

These forecasts of available financing thus suggest that the supply in 1983 will be less than in 1982; although the fall may be less than between 1981 and 1982, it could still be $8-10 billion. The only possible source of recovery in 1984, when a fall in IMF credits is likely to balance any improvement in the other regular inflows, would be a recovery in bank confidence and lending. It is impossible to quantify this; unfortunately, the lower limit may be close to zero. But UNCTAD and OECD argue strongly that the developing countries should or do want to increase their foreign exchange reserves. These were used to finance the 1982 deficits and are now well below levels normally considered prudent. Therefore even an increase in finance might not permit an equal increase in deficits.

Volumes of imports by non-oil developing countries

The implication of these financing forecasts is that imports will probably have to grow by less than is implied by the forecasts for exports and prices in 1983, and by no more in 1984. All forecasters do expect the developing countries' imports to rise more slowly than exports in 1983, but they may underestimate the difference. Even the lowest forecasts are above the level implied by the available financing. Combining the more pessimistic financing forecasts with the forecasts for export volume and prices implies that imports could fall by about 5% (they fell by 5-8% in 1982).

This is consistent with preliminary data for 1983. The Latin American countries in particular have cut their imports severely. Mexico reduced imports by 50% in the first six months, and Brazil reduced its non-oil imports by 30%. Other countries have also reduced their imports, including even some Asian exporters of manufactures. The IMF forecast assumed a rise of 6½% for Asia and a fall of only 5½% for Latin America. The countries that have borrowed from the IMF in 1982 or 1983, which must therefore be assumed to be in financial difficulties and following programmes aimed at reducing imports, accounted for over 40% of all imports by the non-oil developing countries in 1982. Even with a strong recovery for Mexico and Brazil in the second half of 1983 (on which there is, as yet, no evidence), the fall could be about 4% if the other non-oil developing countries fail to increase their imports. (This is consistent with 0 to −1% for world trade as a whole).

For 1984, most forecasters predict a much closer relationship between imports and export growth, in spite of their misgivings over finance and reserves. Given the general expectation of inflation around 5%, this may be high, as even an unchanged deficit requires a lower import growth, as the OECD forecasts. Five per cent may be at the optimistic end of what is possible for import growth.

Output in the developing countries

A low forecast for imports means that output is unlikely to be able to grow much faster in 1983 than in 1982, when it grew by 1-2%, although some recovery in 1984 is possible. In addition to the direct constraints which shortages of essential imports impose on output, the same stabilisation programmes that restrain imports operate directly on output. The most recent 1983 output forecasts for the developing countries are under 2%. The recovery to 4% expected in 1984 seems modest in relation to the rises suggested in imports, but the forecast for 1983 may prove optimistic: the second year of falling imports may have more serious effects than the first. The forecasts are lowest for the Latin

Table 2 **Output Forecasts by area or type of developing country** *(percentage growth rates)* **1983-84**

	1983 UNCTAD	1983 IMF[a]	1984 UNCTAD
Western hemisphere	−1.6	−0.2	3.3
Africa	1.5	2.3	3.7
South Asia	3.6	)	3.8
		)5	
East Asia	4.7	)	5.8
Secondary oil exporters	3.9	1.1	4.4
Least developed	3.0	4.6	3.5
Exporters of manufactures	0.0	0.4	4.7

Source: See inset, page one.

a These are consistent with an earlier forecast of 2.3% for the total.

[1]Part of the wide spread in these forecasts can be explained by the exclusion of some secondary oil exporters from the UN and UNCTAD figures

American countries as would be expected from their import figures *(see table 2)*.

FORECASTS FOR 1985 and AFTER

For the **industrial countries**, the IMF and the NIESR, supported by unquantified indications from the UN, UNCTAD, GATT and BIS, agree that further recession on the scale of the early 1980s is not probable, but that growth is unlikely to increase from the present rate, and might fall back towards the 2½% observed between 1973 and 1980 *(see table 3)*. They also appear to agree that capacity has risen at less than normal rates, because investment has been low, which limits the duration of a high recovery period growth rate. Some also suggest that changes in industrial technology or labour forces have reduced normal growth rates permanently, or at least made them more difficult to achieve. Only the World Bank rejects all these arguments. It expects high and rising growth to 1985, during the recovery, and then resumption of the pre-1973 rate.[2] The level of potential output is assumed to have continued to increase throughout the recession at the pre-recession rate. The possibility that the ratio of import growth to output growth may be lower than in the past, discussed above in relation to 1983-4, has not yet affected medium-term forecasts. A forecast of 4% therefore seems to be at the upper end of the possible, given the most common output forecasts for imports of 2½-3%.

Table 3 Medium-Term Forecasts
(percentage growth rates)

	World Bank	World Bank 1985-95			IMF	NIESR: (Nov.82)
	1984-5[a]	Low	Central	High	1984-6	1983-7
Developed countries Output	3.5	2.5	3.7	5.0	3	2.8
World trade volume			5.1	7.0		4.0
Oil price, real			3.7	2	0	0
Non-oil developing countries						
Output	5.5	4.7	5.5	6.2	4.4	
Western hemisphere					5¼	
Asia, low income		4.5	4.9	5.3		
Africa, low income		2.7	3.3	3.9		
Secondary oil exporters		5.3	5.6	5.8	5.0	
Least developed					3.5	
Exporters of manufactures		4.4	5.7	6.9	4.0	
Export volume	5/6		6.8		5.7	
Secondary oil exporters					5.0	
Least developed					4.0	
Exporters of manufactures					6.5	
Exports of manufactures		12.0				
Import volume			7.2		7.5	
Terms of trade					0.2	

a Derived from 1980-85 forecast
Source: See inset, page 1.

If the real **oil price** falls slightly next year and then remains flat, the average annual change for 1980-5 will have been -1%. The World Bank now forecasts a 20% real rise from the 1981 prices by 1995. This implies about 3½-4% a year from 1985 to 1995. The other forecasters, with their lower output forecasts, expect no real change. The World Bank forecasts seem to imply falling terms of trade for developing countries while the others suggest little change or a small rise.

The relationship between **developing countries' exports** and total world trade has been changing. Unlike the total, their exports had grown more rapidly after 1973 than before, at 7% (and even 9½% between 1975 and 1980).

Between 1980 and 1985, this good relative performance appears to be continuing: the average growth may be around 3%, 2 points higher than the total. The World Bank forecast suggests developing countries' exports may again grow about 2 points faster than the total between 1985 and 1995. This continuing increase in market share is at odds with the fears of some other forecasters about the effects of protection. The World Bank forecast is based on manufactures exports growing three times as fast as developed country output. The IMF forecast implies a similar relationship. With only 2½% growth, these ratios suggest that exports by developing countries could grow at about 4½%, slightly higher than expected next year, but below the late 1970s figures.

Only the World Bank gives a full account of its medium-term **financing** forecast. It expects aid, official loans, private borrowing and direct investment all to rise at about 10% a year (which is 4% in real terms). Except for private lending (which grew at a real rate of 5-10%), these are substantially higher than the real growth rates estimated by the Bank for 1970-1982. All the other forecasters express considerable doubt over whether financing will continue to be available at past levels, and suggest that its costs may be higher.

Because of the possibility of changes in the structure of industry and demand, the relationship between external constraints and **growth** can be less mechanical in the medium term. Between 1973 and 1980, output in the developing countries grew at about 5% a year. This was only slightly below the pre-1973 rate of 6%. The average for 1980-85 may be under 3% even if there is recovery to around 4% in the next two years. The World Bank expects growth to return to 5½% after 1985, or possibly 6.2% if there is a period of rapid recovery, although this rate requires their imports to grow more rapidly than exports. The IMF has expressed concern that prolonged low growth and low investment could lower potential output in the 1980s and its forecast is substantially lower, although it also implies high import growth.

CONCLUSION

Past experience strongly suggests that all these forecasts will be wrong, in terms of predicting exact numbers. But forecasters are becoming better able to identify the weak points of a particular forecast. Most agree that the crucial questions at present are:

* Has the recession or structural change lowered rates of growth?
* Will trade continue to grow much faster than output?
* Can the developing countries continue to increase their share of trade?
* Will they be able to finance deficits that are as large as in the past?

Given these uncertainties, most forecasters agree that the outcome could be even worse than the figures they give. Most also agree, however, that even if future performance cannot be as good as in the best period of the past, it could be better than they predict. They all believe that it is possible for economic policy to improve the outcome in both developed and developing countries, although they would disagree about the most effective mix of policies. These desperately poor prospects for the third world cannot therefore be accepted as completely predetermined.

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[2]This is its 'central forecast'. It also gives low and high forecasts.