Shockwatch Bulletin: Monitoring the impact of the euro zone crisis, China/India slow-down, and energy price shocks on lower-income countries

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Outline

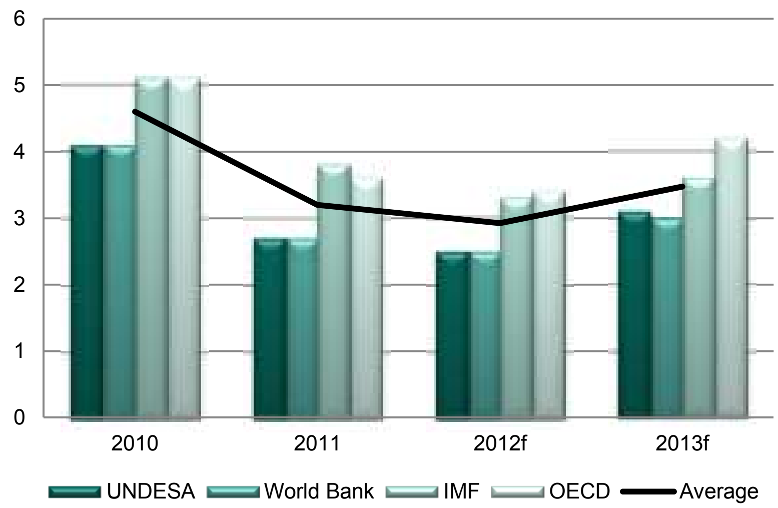
- Global macro-economic and financial situation and outlook
- Vulnerability assessment
- Actual impacts (case studies)
- Policy analyisis

Economic growth trends and forecasts

• Projections of global GDP growth have been revised downwards.

• Global GDP growth is projected to decline from 3.8% in 2011 to 3.3% in 2012, and to recover to 3.6% in 2013 (IMF 2012).

World GDP growth (%)

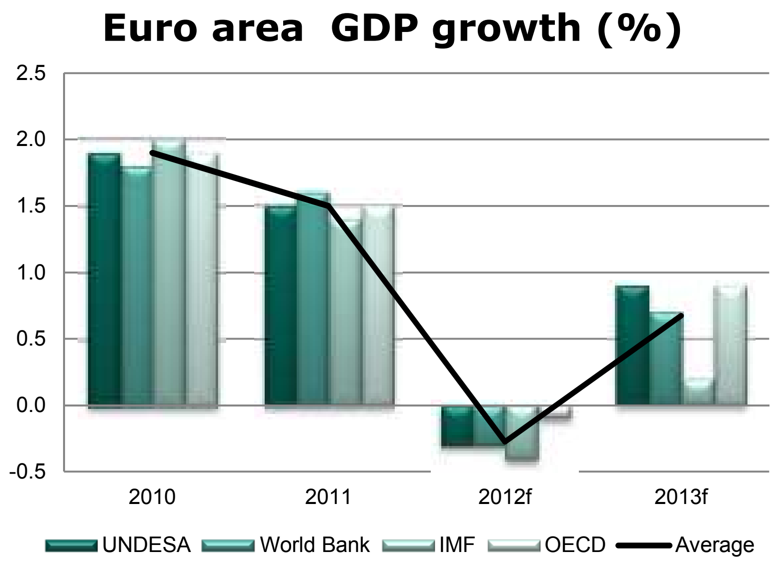


Source: Authors' calculations based on IMF (2012), World Bank (2012), OECD (2012), and UNDESA (2012).

Economic growth trends and forecasts

• Euro zone is slipping into recession and in 2012 is expected to register a –0.4% growth (IMF 2012).

• Italy and Spain are registering the most severe contractions (-2.3% and -1.5% respectively).



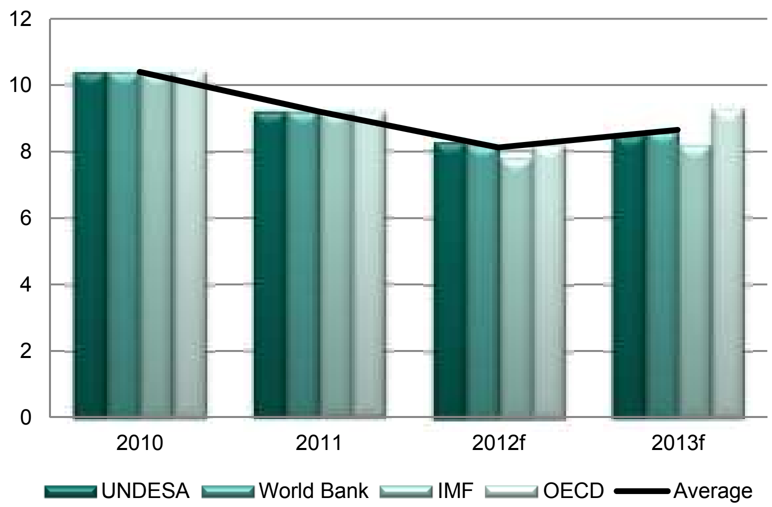
Source: Authors' calculations based on IMF (2012), World Bank (2012), OECD (2012), and UNDESA (2012).

Economic growth trends and forecasts

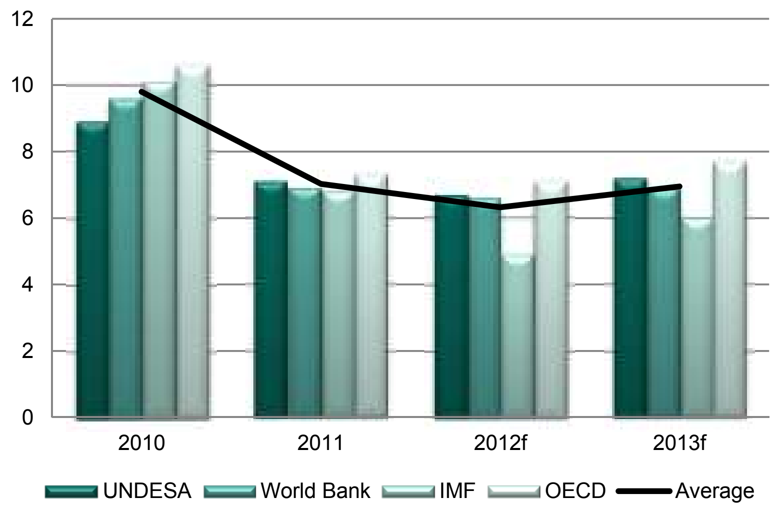
• Emerging economies are experiencing major growth slow-downs.

• China's and India's growth prospects have been revised downwards in both 2012 and 2013.

China GDP growth (%)



India GDP growth (%)



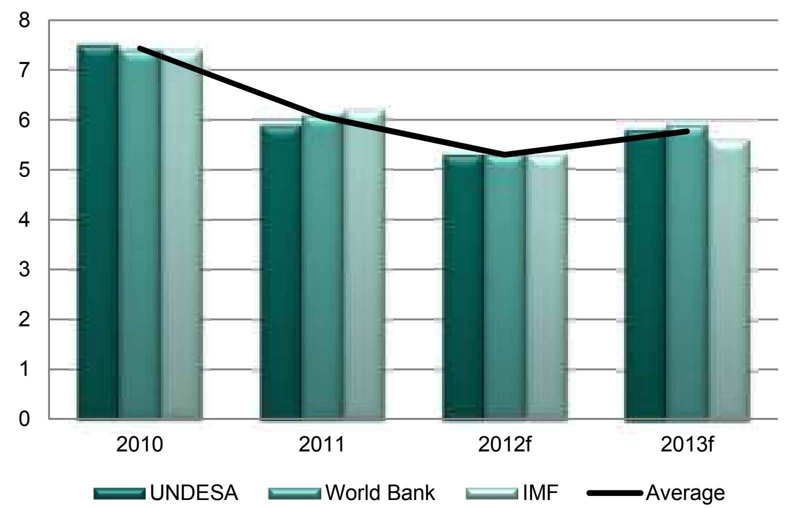
Source: Authors' calculations based on IMF (2012), World Bank (2012), OECD (2012), and UNDESA (2012).

Economic growth trends and forecasts

• Projections of developing countries' GDP growth have been revised downwards.

• Developing countries' GDP growth is projected to decline from 6.2% in 2011 to 5.3% in 2012, and to slightly increase to 5.6% in 2013 (IMF 2012).

GDP growth in developing countries (%)



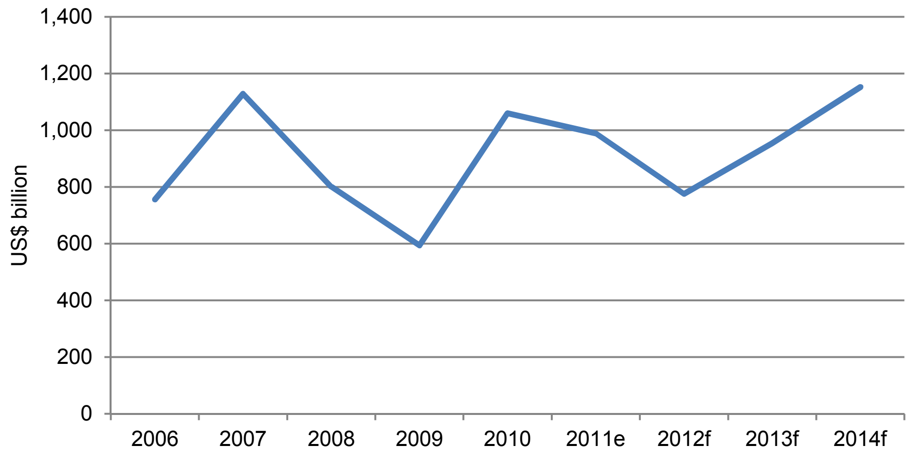
Source: Authors' calculations based on IMF (2012), World Bank (2012), and UNDESA (2012).

Private capital flows trends and forecasts

• Net private capital flows to developing countries remain volatile.

• They declined over the period 2010-12, but medium-term prospects are high.

Net private capital flows to developing countries, 2006-14



• However, there are differences across types of private capital flows.

Source: Adapted from World Bank (2012).

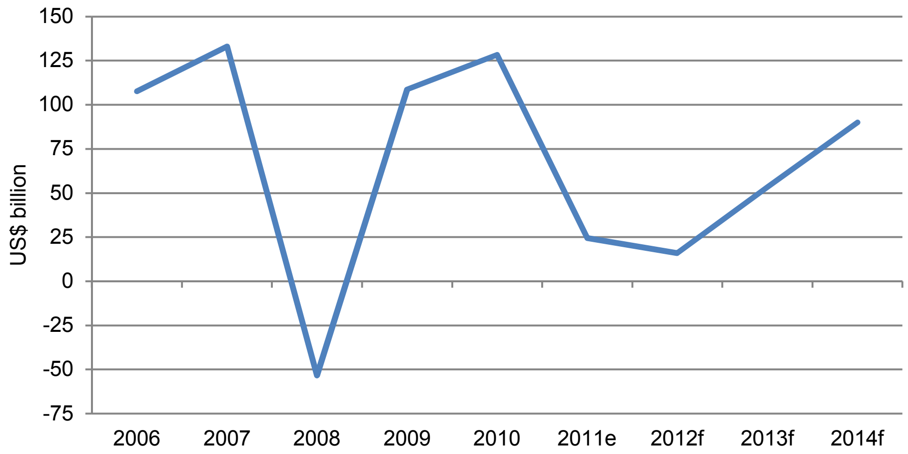
Private capital flows trends and forecasts

• Portfolio equity flows were among the hardest hit.

• They dropped by 80% in 2011, and are expected to decline further in 2012.

• In 2013 and 2014 they are projected to recover but remain below pre-crisis levels in 2010.

Portfolio equity inflows to developing countries, 2006-14



Source: Adapted from World Bank (2012).

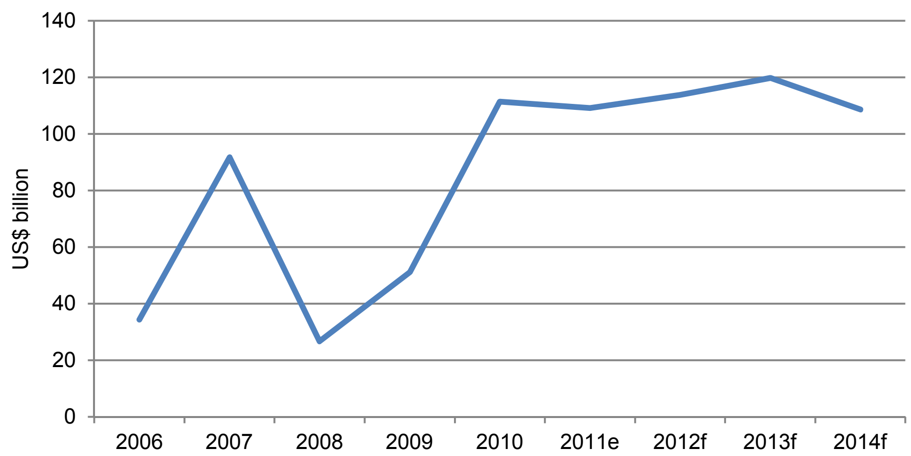
Private capital flows trends and forecasts

• Bond flows were more resilient to external shocks.

• They declined by just 2% between 2010-11.

• They are expected to increase in both 2012 and 2013 before a downturn in 2014 to values close to those of 2010.

Bond flows to developing countries, 2006-14

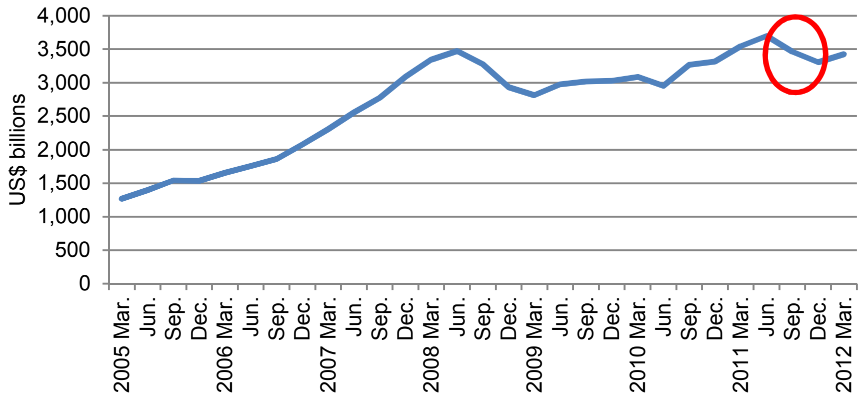


Source: Adapted from World Bank (2012).

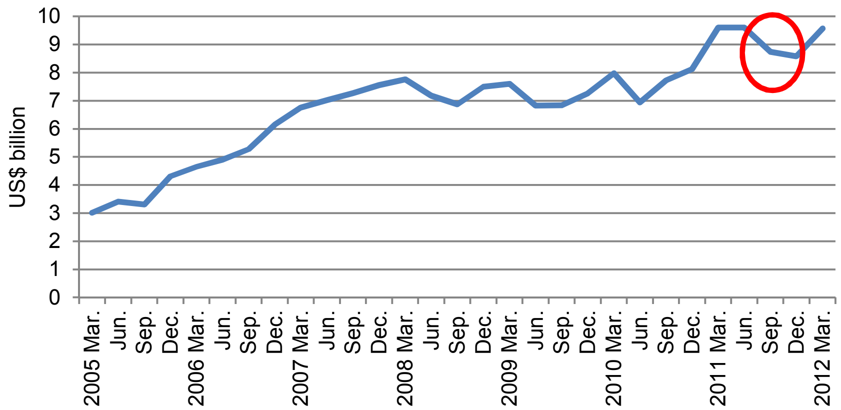
Private capital flows trends and forecasts

• Cross-border bank lending to developing countries from European banks and from some emerging markets experienced important declines between June 2011 and December 2011.

Cross-border bank lending to developing countries from European banks, March 2005-March 2012



Cross-border bank lending to developing countries from Indian banks, March 2005-March 2012



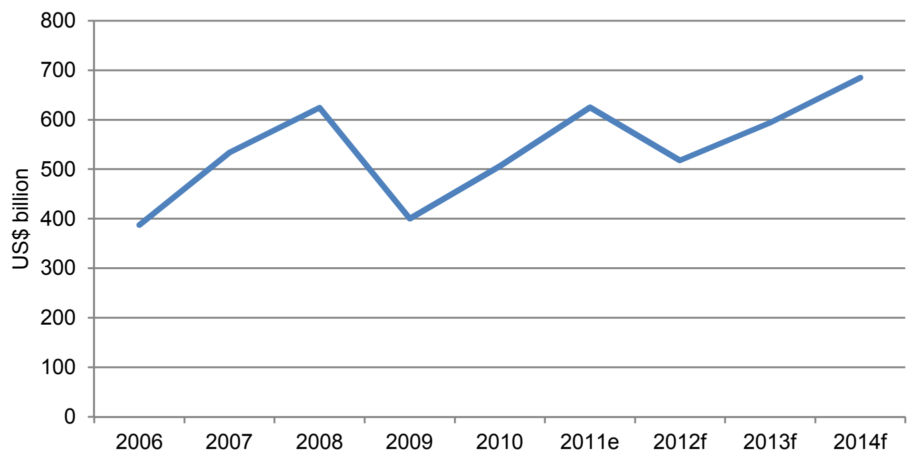
Source: Authors' calculations based on BIS Consolidated Banking Statistics.

Private capital flows trends and forecasts

• FDI inflows to developing countries are projected to decline by 17% in 2012.

• They are expected to recover in 2013 and further increase in 2014 to values above the peak value of 2008.

FDI inflows to developing countries, 2006-14



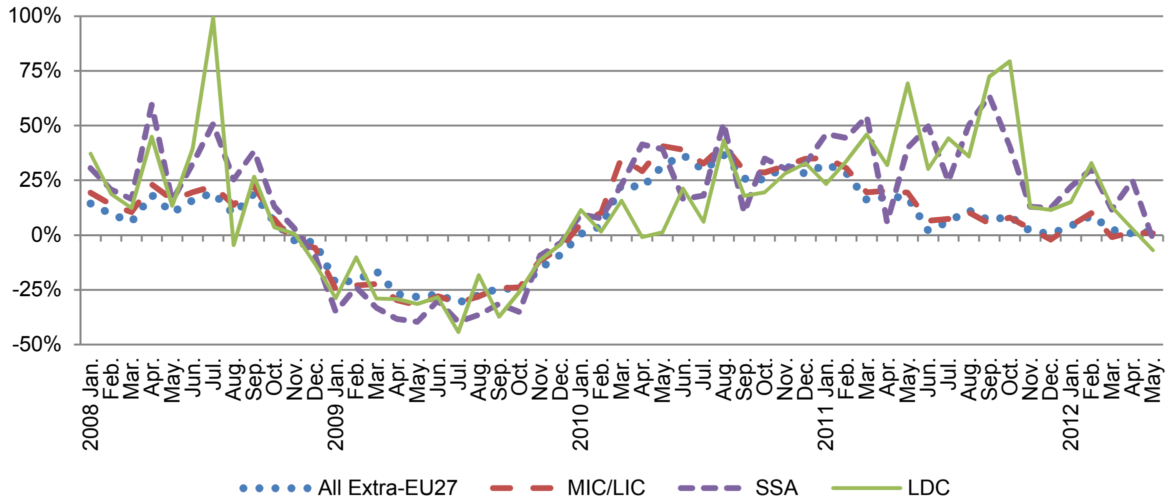
Source: Adapted from World Bank (2012).

Trade trends and forecasts

• Growth in developing countries' exports declined from 6.5% in 2011 to 4% in 2012, and is expected to recover to 5.7% in 2013 (IMF 2012).

• Growth in the value of imports into the euro zone slowed during the first quarter of 2012.

Euro zone imports: monthly year-on-year change, Jan. 2007-May 2012



• Some commodity imports into China began to slow-down in 2012.

Source: Authors' calculations based on data from Eurostat COMEXT database.

Remittance and aid trends and forecasts

• Remittances to developing countries could decline by 5% or more in 2012 (World Bank 2012).

• More restrictive employment conditions are affecting migrant workers.

• Some EU member states have reduced their aid budgets (e.g. Spain, Greece).

• Growth in country programmable aid is expected to decline to an average of 2% between 2011-13, compared to the 5% average growth during 2001-10 (World Bank 2012).

Vulnerability to macro-financial shocks

- We assessed the vulnerability of 57 developing countries (20 LICs and 37 LMICs) to: (i) euro zone crisis; (ii) China/India slow-down

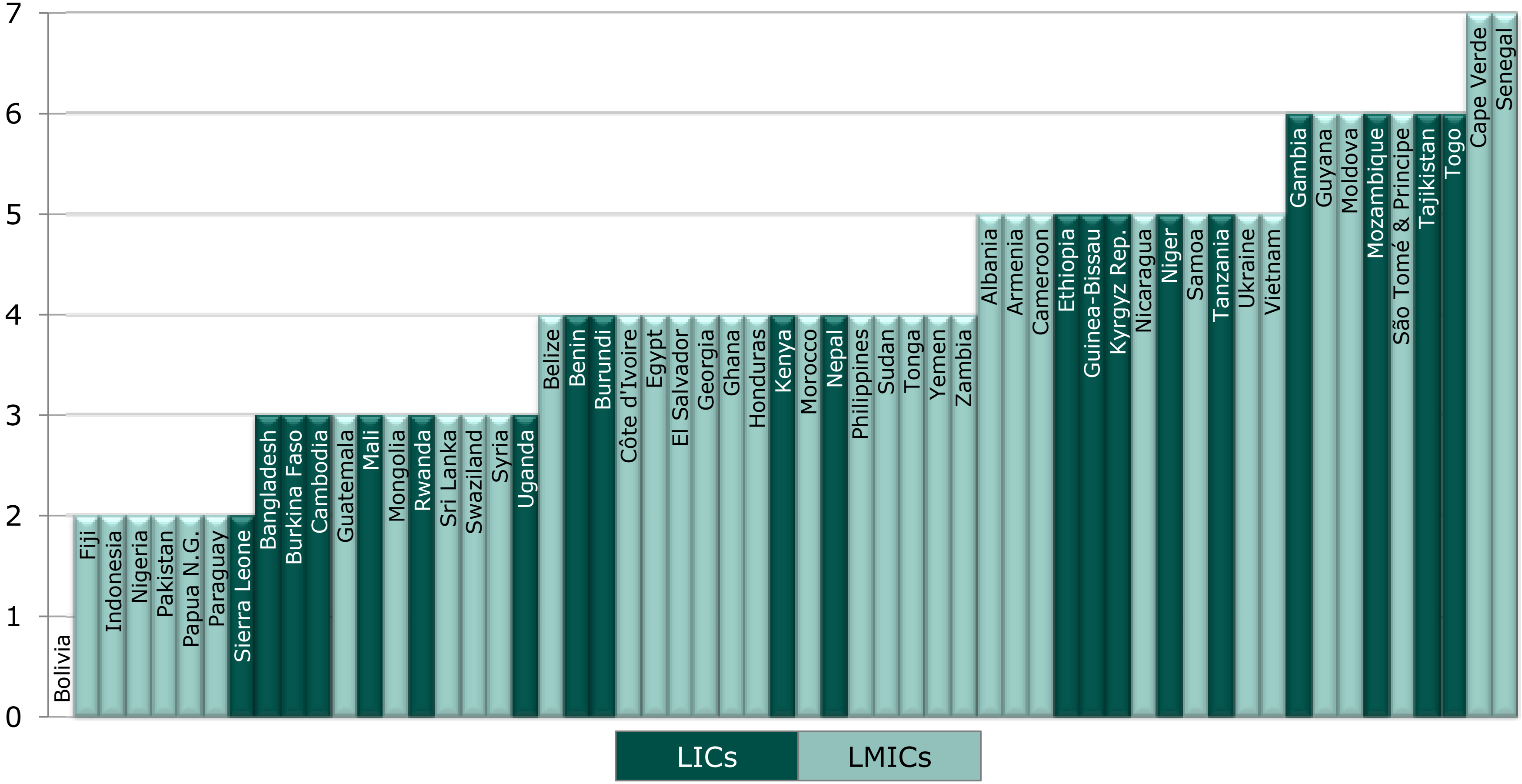
- **Vulnerability = Exposure – Resilience**

- Exposure indicators:
  - *dependence on trade with Euro zone*
  - *dependence on trade with China*
  - *dependence on trade with India*
  - *FDI dependence*
  - *dependence on cross-border bank lending from European banks*
  - *aid dependence*
  - *dependence on remittances*
  - *pegged to euro (yes/no)*

- Resilience indicators:
  - *fiscal balance*
  - *current account balance*
  - *foreign currency reserves*
  - *external debt burden*

Vulnerability to macro-financial shocks

Selected LICs/LMICs: 0 to 3 = low; 4 = intermediate; 5 to 7 = high



Source: Authors' elaboration from various sources.

Vulnerability to macro-financial shocks: high

Country	Exposure indicators									Resilience indicators				Overall degree of vulner-ability
	Dependence on trade with:				*FDI depend-ence*	*Depend-ence on cross-border bank lending from European banks*	*Aid depend-ence*	*Depend-ence on remit-tances*	*Pegged to euro (yes / no)*	*Fiscal balance (surplus / deficit)*	*Current account balance (surplus / deficit)*	*Foreign currency reserves*	*External debt burden*	
	Euro zone	*China*	*India*	*China and India*										
Cape Verde	high	low	low	low	medium	high	high	medium	yes	deficit	deficit	healthy	heavy	high
Senegal	high	low	high	high	low	high	medium	high	yes	deficit	deficit	healthy	manageable	high
Gambia	high	high	high	high	medium	medium	medium	high	no	deficit	deficit	healthy	manageable	high
Mozambique	high	medium	low	medium	high	high	high	low	no	deficit	deficit	healthy	manageable	high
Tajikistan	high	low	low	low	low	low	medium	high	no	deficit	deficit	unhealthy	heavy	high
Togo	medium	low	medium	medium	low	high	medium	high	yes	deficit	deficit	healthy	heavy	high
Guyana	high	low	low	low	medium	low	high	high	no	deficit*	deficit	healthy	heavy	high
Moldova	high	low	low	low	medium	high	medium	high	no	deficit*	deficit	healthy	heavy	high
São Tomé/Principe	high	low	low	low	medium	high	high	low	no	deficit	deficit	healthy	heavy	high
Ethiopia	high	high	low	high	low	low	medium	low	no	deficit*	deficit	unhealthy	manageable	high
Guinea-Bissau	low	low	high	high	low	low	medium	medium	yes	deficit*	deficit	healthy	heavy	high
Kyrgyz Republic	low	low	low	medium	high	medium	medium	high	no	deficit	deficit	healthy	heavy	high
Niger	high	low	low	low	high	low	medium	low	yes	deficit*	deficit	healthy	manageable	high
Tanzania	high	high	medium	high	medium	high	medium	low	no	deficit	deficit	healthy	manageable	high
Albania	high	medium	low	medium	medium	high	medium	high	no	deficit	deficit	healthy	manageable	high
Armenia	high	low	low	low	medium	medium	medium	high	no	deficit	deficit	healthy	heavy	high
Cameroon	high	medium	medium	high	Low	high	low	low	yes	deficit*	deficit	healthy	manageable	high
Nicaragua	medium	low	low	low	high	medium	medium	high	no	deficit*	deficit	healthy	heavy	high
Samoa	low	low	low	low	low	high	medium	high	no	deficit	deficit	healthy	heavy	high
Ukraine	high	medium	medium	medium	medium	high	low	medium	no	deficit	deficit	healthy	heavy	high
Vietnam	high	high	low	high	medium	medium	low	medium	no	deficit	deficit	unhealthy	manageable	high

Source: Authors' elaboration from various sources.

Vulnerability to macro-financial shocks: intermediate

Country	Exposure indicators									Resilience indicators				Overall degree of vulner-ability
	Dependence on trade with:				*FDI depend-ence*	*Depend-ence on cross-border bank lending from European banks*	*Aid depend-ence*	*Depend-ence on remit-tances*	*Pegged to euro (yes / no)*	*Fiscal balance (surplus / deficit)*	*Current account balance (surplus / deficit)*	*Foreign currency reserves*	*External debt burden*	
	Euro zone	*China*	*India*	*China and India*										
Benin	medium	**high**	medium	**high**	low	low	medium	medium	**yes**	**deficit***	**deficit**	healthy	manageable	intermediate
Burundi	**high**	low	low	low	low	low	**high**	low	no	**deficit**	**deficit**	healthy	manageable	intermediate
Kenya	**high**	low	low	low	low	**high**	medium	medium	no	**deficit**	**deficit**	healthy	manageable	intermediate
Nepal	medium	low	**high**	**high**	low	low	medium	**high**	no	**deficit***	**deficit**	healthy	manageable	intermediate
Belize	medium	low	low	low	medium	**high**	low	medium	no	**deficit***	**deficit****	healthy	**heavy**	intermediate
Côte d'Ivoire	**high**	low	low	low	Low	**high**	low	low	**yes**	**deficit**	surplus	healthy	manageable	intermediate
Egypt	**high**	low	medium	**high**	Low	**high**	low	medium	no	**deficit**	**deficit****	healthy	manageable	intermediate
El Salvador	medium	low	low	low	Low	medium	low	**high**	no	**deficit**	**deficit**	healthy	**heavy**	intermediate
Georgia	**high**	low	low	medium	medium	medium	medium	medium	no	**deficit***	**deficit**	healthy	**heavy**	intermediate
Ghana	**high**	low	medium	medium	medium	**high**	medium	low	no	**deficit**	**deficit**	healthy	manageable	intermediate
Honduras	**high**	low	low	low	medium	medium	low	**high**	no	**deficit**	**deficit**	healthy	manageable	intermediate
Morocco	**high**	low	medium	medium	low	**high**	low	medium	no	**deficit**	**deficit**	healthy	manageable	intermediate
Philippines	**high**	**high**	low	**high**	low	medium	low	**high**	no	**deficit**	surplus	healthy	manageable	intermediate
Sudan	low	**high**	low	**high**	low	low	low	medium	no	**deficit**	**deficit**	**unhealthy**	manageable	intermediate
Tonga	low	low	low	low	low	low	**high**	**high**	no	**deficit**	**deficit**	healthy	manageable	intermediate
Yemen	medium	**high**	**high**	**high**	low	medium	low	medium	no	**deficit**	**deficit**	healthy	manageable	intermediate
Zambia	low	**high**	low	**high**	**high**	**high**	medium	low	no	**deficit**	surplus	healthy	manageable	intermediate

Source: Authors’ elaboration from various sources.

Vulnerability to macro-financial shocks: low

Country	Exposure indicators									Resilience indicators				Overall degree of vulner-ability
	Dependence on trade with:				*FDI depend-ence*	*Depend-ence on cross-border bank lending from European banks*	*Aid depend-ence*	*Depend-ence on remit-tances*	*Pegged to euro (yes / no)*	*Fiscal balance (surplus / deficit)*	*Current account balance (surplus / deficit)*	*Foreign currency reserves*	*External debt burden*	
	Euro zone	*China*	*India*	*China and India*										
Bangladesh	**high**	low	medium	medium	low	medium	low	**high**	no	**deficit**	surplus	healthy	manageable	low
Burkina Faso	medium	low	low	low	low	medium	medium	low	**yes**	**deficit**	**deficit****	healthy	manageable	low
Cambodia	**high**	low	low	low	medium	low	medium	medium	no	**deficit***	**deficit**	healthy	manageable	low
Mali	medium	low	low	low	low	Medium	medium	medium	**yes**	**deficit***	**deficit**	healthy	manageable	low
Rwanda	**high**	medium	low	medium	low	medium	medium	low	no	**deficit***	**deficit**	healthy	manageable	low
Uganda	**high**	low	low	medium	medium	medium	medium	medium	no	**deficit**	**deficit**	healthy	manageable	low
Guatemala	medium	low	low	low	Low	low	low	**high**	no	**deficit**	**deficit****	healthy	manageable	low
Mongolia	medium	**high**	low	**high**	**high**	medium	medium	medium	no	surplus	**deficit**	healthy	manageable	low
Sri Lanka	**high**	low	medium	medium	low	medium	low	medium	no	**deficit**	**deficit****	healthy	manageable	low
Swaziland	**high**	low	low	low	low	low	low	medium	no	**deficit**	**deficit**	healthy	manageable	low
Syria	**high**	low	low	low	low	low	low	medium	no	**deficit**	**deficit**	healthy	manageable	low
Sierra Leone	low	low	low	low	low	medium	medium	medium	no	**deficit**	**deficit**	healthy	manageable	low
Fiji	low	low	low	low	medium	low	low	medium	no	**deficit**	**deficit**	healthy	manageable	low
Indonesia	medium	**high**	medium	**high**	low	medium	low	low	no	**deficit***	surplus	healthy	manageable	low
Nigeria	**high**	low	**high**	**high**	medium	low	low	medium	no	surplus	surplus	healthy	manageable	low
Pakistan	**high**	medium	low	medium	low	medium	low	medium	no	**deficit**	surplus	healthy	manageable	low
Papua New Guinea	medium	medium	low	medium	low	medium	medium	low	no	surplus	**deficit**	healthy	**heavy**	low
Paraguay	medium	low	low	low	low	**high**	low	medium	no	surplus	**deficit**	healthy	manageable	low
Bolivia	medium	medium	low	medium	medium	low	medium	medium	no	surplus	surplus	healthy	manageable	low

Source: Authors' elaboration from various sources.

Vulnerability to macro-financial shocks

• Poorest countries are more vulnerable to macro-financial shocks: 45% of LICs are highly vulnerable versus 32% of LMICs.

• Most important transmission channels of shocks appear to be (i) trade and financial linkages with European economies; (ii) dependence on remittances; (iii) trade linkages with China and (mainly in the case of LMICs) India.

• Almost all countries have high fiscal and current account deficits.

• The most highly vulnerable countries are Senegal and Cape Verde.

• Several countries with an intermediate degree of vulnerability have weak trade linkages with emerging powers.

• Some countries with a low degree of vulnerability are particularly resilient.

Case studies: actual impacts

- Actual impacts of the euro zone crisis and China/India slow-down are becoming increasingly apparent, with more expected.

- in *Kenya*:
  - horticultural and tea exports declined by about 10% and 3% respectively in the first six months of 2012

- in *Zambia*:
  - copper exports increased at a slower pace in 2011 and 2012 (in estimates) than in 2009
  - exports to European partners declined in 2011
  - exports to China increased at a lower rate in 2011 (42%) than in 2010 (137%)
  - Lusaka Stock Exchange All Share Index dropped in May 2012

- in *Cambodia*:
  - ODA declined by more than 50% between 2010-12

Policy analysis

- *Developing countries (LICs) should be concerned since:*

→ they have become more open
→ global shocks have become more frequent with significant effects on growth and development outcomes
→ links with emerging powers have increased
→ buffers have deteriorated after 2008-09 crisis

- *However, we need to qualify these concerns:*

→ LICs are still growing, and faster than developed economies
→ so far effects of the combined global shocks are smaller than those of the 2008-09 crisis
→ better policies have created more fiscal space and slightly more diversified economies in this decade than previously
→ not all countries are vulnerable to all shocks
→ many shocks are interdependent with some cancelling each other out

Policy analysis

- *What should developing countries do?*

  → need to monitor external shocks and their possible effects more than was the case in the past
  → introduce appropriate policy responses, especially targeted measures to raise productivity

- *How can donors help?*

  → safeguarding the future of shock facilities
  → enhancing coordination and coherence amongst shock facilities
  → encouraging the monitoring of effects of external shocks on developing countries

Thank you!

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This material has been funded by UK aid from the UK Government, however the views expressed do not necessarily reflect the UK Government's official policies.