Global Economic Prospects

HIGHLIGHTS from CHAPTER 1

GLOBAL OUTLOOK:
SUBDUED GROWTH, SHIFTING POLICIES, HEIGHTENED UNCERTAINTY

Global Economic Prospects January 2017

Key Points

- *Global growth is estimated to have slowed in 2016 to a post-crisis low of 2.3 percent, as global trade stalled, investment decelerated, and policy uncertainty increased.*
- *A moderate recovery is expected in 2017, with global growth forecast to increase to 2.7 percent, mainly driven by improvements in emerging market and developing economies.*
- *With the expected increase in commodity prices, the divergence in growth performance between commodity exporters and importers is on track to narrow in 2017.*
- *Fiscal stimulus measures in major economies—especially in the United States—could lead to stronger-than-expected global growth.*
- *However, downside risks still dominate global economic prospects and are associated with heightened policy uncertainty, protectionist pressures, and risk of financial market disruptions.*

Global growth: moderate recovery expected. Global growth is estimated to have fallen to 2.3 percent in 2016—the weakest performance since the global financial crisis (Figure 1.A). Anemic global investment was accompanied by a further weakening of global trade. Mitigating these headwinds for emerging market and developing economies (EMDEs), commodity prices strengthened. However, the rapid rise in U.S. bond yields and appreciation of U.S. dollar towards the end of the year led to a notable tightening of financing conditions for EMDEs, and in some cases significant portfolio outflows. In 2017, global growth should pick up to 2.7 percent, with the recovery mainly driven by receding obstacles to activity in commodity-exporting EMDEs.

Advanced economies: heightened policy uncertainty. Advanced economies continue to be afflicted by weak underlying growth and low inflation, while uncertainty about future policy direction increased. Growth is projected to recover modestly to 1.8 percent in 2017 (from 1.6 percent in 2016), although the range of possible outcomes has markedly widened after the electoral outcome in the United States and the United Kingdom's decision to leave the European Union. In particular, current forecasts do not incorporate the potential effects of policy proposals suggested by the new U.S. administration, as their scope is still highly uncertain. Fiscal stimulus, if implemented, could result in stronger U.S. growth than currently predicted. However, some other policy changes, or persistent policy uncertainty, could dampen U.S. and international growth prospects.

EMDEs: narrowing divergences. EMDE growth is expected to accelerate to 4.2 percent in 2017 and to an average of 4.7 percent in 2018-19 (Figure 1.B). EMDEs are forecast to contribute 1.6 percentage points to global growth in 2017, accounting for about 60 percent of global growth for the first time since 2013. Given the expected increases in commodity prices, particularly for oil, the divergence in growth outlooks between commodity exporters and importers is on track to narrow. However, the outlook for EMDE regions with large numbers of commodity exporters remain mixed. Growth in Latin

America and the Caribbean, and in Europe and Central Asia, is expected to accelerate in 2017, mainly reflecting a bottoming out in activity in Brazil and Russia. Growth in the Middle East and North Africa will pick up modestly as oil prices recover. While growth should also rebound in Sub-Saharan Africa, the improvement is notably weaker than previously expected, as some commodity exporters struggle to adjust to past deterioration in their terms of trade. EMDE regions with substantial numbers of commodity-importing economies—East Asia and the Pacific, and South Asia—are projected to continue to experience solid growth.

Low-income countries: adjusting. Growth in low-income countries (LICs) remained relatively subdued in 2016 (at 4.7 percent), but their external environment is expected to improve gradually, with commodity prices increasing moderately from low levels and global trade regaining some momentum. Growth in LICs is expected to recover to 5.6 percent in 2017. Growth will be substantially weaker in oil exporters than in metals exporters, while remaining strong in most commodity importers, partly supported by large public investment. However, fragile countries will see a less vigorous recovery over the forecast horizon, as political uncertainty and security challenges continue to hinder private investment.

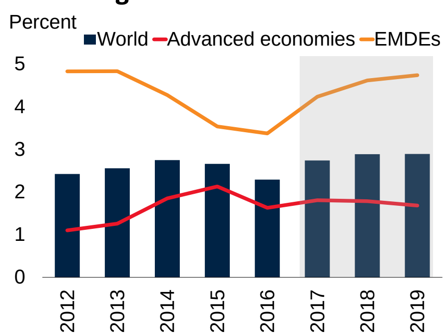
Risks to the forecast: still tilted to the downside. There is substantial uncertainty around baseline projections for global growth, where downside risks still dominate. The heightened level of policy uncertainty has been exacerbated by recent political developments—most notably, electoral outcomes in the United States and the United Kingdom (Figure 1.D). This and other risks—particularly financial market disruptions amid tighter global financing conditions—may be amplified over the medium term by mounting protectionist tendencies, slower potential growth, and lingering vulnerabilities in some EMDEs. In particular, a prolonged period of elevated policy uncertainty could weigh on investment growth in EMDEs (Figure 1.E). In turn, weak investment could adversely affect productivity growth, which has slowed considerably since the global financial crisis (Figure 1.F). However, fiscal stimulus measures in major economies—especially in the United States—could lead to stronger-than-expected global growth, and thus represents a substantial upside risk to the outlook.

Policy priorities: growth-enhancing mix. In advanced economies, low or even negative real equilibrium interest rates constrain the effectiveness of monetary policy and may warrant more supportive fiscal policies. In EMDEs, finding an appropriate balance between fiscal adjustment, measures to reduce vulnerabilities, and growth-oriented reforms aimed at raising human capital and physical infrastructure should be a priority. Policies that boost domestic sources of long-term growth—critically, long-term investment and productivity—need to be pursued. Investing in human and physical capital will help narrow unmet investment gaps in skills and infrastructure. These policies could be reinforced by efforts to further international integration, such as those that support growth in EMDE services trade, and that create an environment to maximize the benefits of foreign direct investment. Measures to support stronger growth and reduce income inequality will have to be undertaken jointly to overcome extreme poverty.

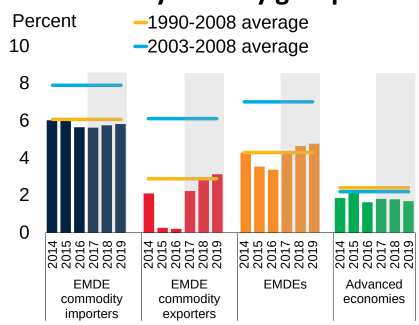
Figure 1: Global Outlook and Risks

After reaching a post-crisis low of 2.3 percent, global growth is expected to recover to 2.7 percent in 2017, mainly supported by stronger growth in EMDEs. Growth in commodity exporters is expected to pick up, while growth in commodity importers is projected to remain robust. Downside risks to global growth still dominate. They are associated with heightened policy uncertainty, protectionist pressures, and risk of financial market disruptions. A prolonged period of elevated policy uncertainty could weigh on EMDE investment growth. In turn, weak investment could adversely affect productivity growth, which has slowed considerably in the post-crisis period.

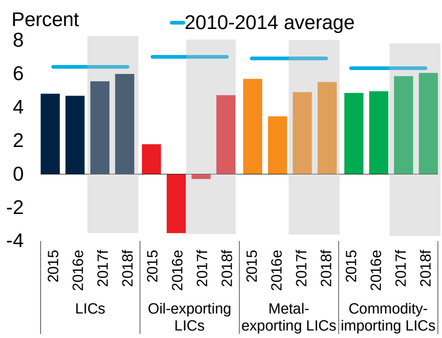
A. Global growth



B. Growth by country groups

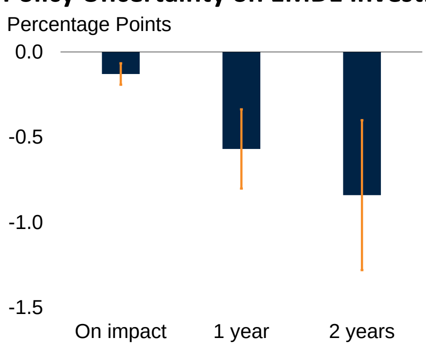


C. GDP growth in LICs

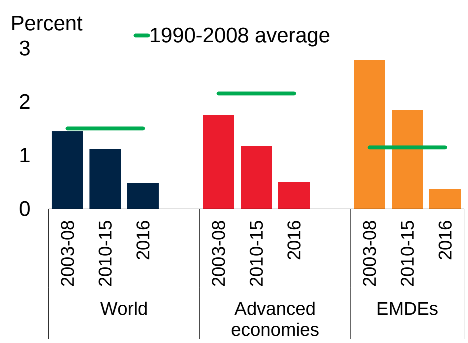


D. Global policy uncertainty

E. Impact of 10-percent rise in U.S. Economic Policy Uncertainty on EMDE investment



F. Labor productivity growth



Sources: Conference Board, Economic Policy Uncertainty, World Bank.

A. B. C. Shaded area indicate forecasts. Aggregate growth rates calculated using constant 2010 U.S. dollars GDP weights.

C. Commodity-exporting LICs include oil and metal exporters. Commodity-importing LICs include 22 low-income countries for which data are available. Commodity-importing countries comprise non-resource intensive economies. Shaded grey areas denotes forecast period. Shaded area indicates forecasts.

D. Global policy uncertainty as measured in Davis (2016). Based on the frequency of articles in domestic newspapers mentioning economic policy uncertainty. 6-month moving average. Last observation is November 2016.

E. Vector autoregressions include, in this order, the VIX or the U.S. Economic Policy Uncertainty (EPU) index, MSCI Emerging Markets Index, J.P.Morgan Emerging Markets Bond spreads, aggregate GDP and investment growth in 18 EMDEs, with G7 GDP growth, U.S. 10-year bond yields, and MSCI World Index as exogenous regressors and estimated with two lags. Blue bars indicate the median responses and orange lines indicate 16-84 percent confidence intervals. Models estimated over the period 1998Q1-2016Q2.

F. Labor productivity growth is the annual percent change in the ratio of real GDP to total hours worked. Labor productivity data for 2016 are estimates.

Table 1.1 Real GDP[1]

(percent change from previous year)

			Estimates	Projections			Percentage point differences from June 2016 projections			
	2014	2015	2016	2017	2018	2019	2015	2016	2017	2018
World	**2.7**	**2.7**	**2.3**	**2.7**	**2.9**	**2.9**	**0.3**	**-0.1**	**-0.1**	**-0.1**
Advanced Economies	**1.9**	**2.1**	**1.6**	**1.8**	**1.8**	**1.7**	**0.3**	**-0.1**	**-0.1**	**-0.1**
United States	2.4	2.6	1.6	2.2 *	2.1 *	1.9 *	0.2	-0.3	0.0 *	0.0 *
Euro Area	1.2	2.0	1.6	1.5	1.4	1.4	0.4	0.0	-0.1	-0.1
Japan	0.3	1.2	1.0	0.9	0.8	0.4	0.6	0.5	0.4	0.1
Emerging Market and Developing Economies (EMDE)	**4.3**	**3.5**	**3.4**	**4.2**	**4.6**	**4.7**	**0.1**	**-0.1**	**-0.1**	**0.0**
Commodity-exporting EMDE	2.1	0.4	0.3	2.3	3.0	3.1	0.2	-0.1	0.0	0.0
Other EMDE	6.0	6.0	5.6	5.6	5.7	5.8	0.1	-0.2	-0.2	-0.1
Other EMDE excluding China	4.5	5.0	4.3	4.6	5.0	5.1	0.3	-0.4	-0.3	-0.1
East Asia and Pacific	6.7	6.5	6.3	6.2	6.1	6.1	0.0	0.0	0.0	0.0
China	7.3	6.9	6.7	6.5	6.3	6.3	0.0	0.0	0.0	0.0
Indonesia	5.0	4.8	5.1	5.3	5.5	5.5	0.0	0.0	0.0	0.0
Thailand	0.8	2.8	3.1	3.2	3.3	3.4	0.0	0.6	0.6	0.3
Europe and Central Asia	2.3	0.5	1.2	2.4	2.8	2.9	0.6	0.0	-0.1	0.0
Russia	0.7	-3.7	-0.6	1.5	1.7	1.8	0.0	0.6	0.1	-0.1
Turkey	5.2	6.1	2.5	3.0	3.5	3.7	2.1	-1.0	-0.5	-0.1
Poland	3.3	3.9	2.5	3.1	3.3	3.4	0.3	-1.2	-0.4	-0.2
Latin America and the Caribbean	0.9	-0.6	-1.4	1.2	2.3	2.6	0.1	-0.1	0.0	0.2
Brazil	0.5	-3.8	-3.4	0.5	1.8	2.2	0.0	0.6	0.7	1.0
Mexico	2.3	2.6	2.0	1.8	2.5	2.8	0.1	-0.5	-1.0	-0.5
Argentina	-2.6	2.5	-2.3	2.7	3.2	3.2	0.4	-1.8	-0.4	0.2
Middle East and North Africa	3.3	3.2	2.7	3.1	3.3	3.4	0.4	-0.1	0.0	-0.1
Saudi Arabia	3.6	3.5	1.0	1.6	2.5	2.6	0.1	-0.9	-0.4	0.2
Iran, Islamic Rep.	4.3	1.7	4.6	5.2	4.8	4.5	0.1	0.2	0.3	0.1
Egypt, Arab Rep.[2]	2.9	4.4	4.3	4.0	4.7	5.4	0.2	1.0	-0.2	0.1
South Asia	6.7	6.8	6.8	7.1	7.3	7.4	-0.2	-0.3	-0.1	0.0
India[3]	7.2	7.6	7.0	7.6	7.8	7.8	0.0	-0.6	-0.1	0.1
Pakistan[2]	4.0	4.0	4.7	5.2	5.5	5.8	0.0	0.5	0.7	0.7
Bangladesh[2]	6.1	6.6	7.1	6.8	6.5	6.7	0.5	0.6	0.5	-0.3
Sub-Saharan Africa	4.7	3.1	1.5	2.9	3.6	3.7	0.1	-1.0	-1.0	-0.7
South Africa	1.6	1.3	0.4	1.1	1.8	1.8	0.0	-0.2	0.0	-0.2
Nigeria	6.3	2.7	-1.7	1.0	2.5	2.5	0.0	-2.5	-2.5	-1.5
Angola	5.4	3.0	0.4	1.2	0.9	0.9	0.2	-0.5	-1.9	-2.5
Memorandum items:										
Real GDP[1]										
High-income Countries	1.9	2.2	1.6	1.8	1.8	1.7	0.3	-0.1	-0.1	-0.1
Developing Countries	4.4	3.6	3.5	4.4	4.8	4.9	0.1	-0.1	-0.1	0.0
Low-income Countries	6.2	4.8	4.7	5.6	6.0	6.1	0.0	-0.6	-0.7	-0.6
BRICS	5.1	3.8	4.3	5.1	5.4	5.5	0.0	0.1	0.0	0.1
World (2010 PPP weights)	3.5	3.3	3.0	3.5	3.7	3.7	0.2	-0.1	-0.1	0.0
World trade volume[4]	3.7	2.8	2.5	3.6	4.0	3.9	0.0	-0.5	-0.3	-0.2
Commodity prices										
Oil price[5]	-7.5	-47.3	-15.1	28.2	8.4	4.6	0.0	4.1	6.3	1.9
Non-energy commodity price index	-4.6	-15.0	-2.6	1.4	2.2	2.1	0.0	2.5	-0.9	-0.1

Source: World Bank.

Notes: PPP = purchasing power parity. World Bank forecasts are frequently updated based on new information. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not differ at any given moment in time. Country classifications and lists of Emerging Market and Developing Economies (EMDEs) are presented in Annex Table 1. BRICS include: Brazil, Russia, India, China and South Africa.

1. Aggregate growth rates calculated using constant 2010 U.S. dollars GDP weights.
2. GDP growth values are on a fiscal year basis. Aggregates that include these countries are calculated using data compiled on a calendar year basis. Pakistan's growth rates are based on GDP at factor cost. The column labeled 2017 refers to FY2016/17.
3. The column labeled 2016 refers to FY2016/17.
4. World trade volume for goods and non-factor services.
5. Simple average of Dubai, Brent, and West Texas Intermediate.

For additional information, please see www.worldbank.org/gep

* The U.S. forecasts do not incorporate the effect of policy proposals by the new U.S. administration, as their overall scope and ultimate form are still uncertain. However, simulations indicate that the large reductions in corporate and personal income taxes suggested by the new administration could—if fully implemented and without consideration of any other policy changes—increase both U.S. GDP growth and global growth above baseline projections in 2017 and 2018. See the "Risks to the outlook" section of Chapter 1 for further details.