Global Economic Prospects

Global Economic Prospects:
Spillovers amid Weak Growth

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Select Publications from DECPG

- *Global Economic Prospects* – *January 6, 2016*
  (January and June)
- *Commodity Markets Outlook* – *January 26, 2016*
  (January, April, July, and October)
- *Policy Research Note* – *September 16, 2015*
  The Coming U.S. Interest Rate Tightening Cycle: Smooth Sailing or Stormy Waters
- *Policy Research Note* – *December 8, 2015*
  Slowdown in Emerging Markets: Rough Patch or Prolonged Weakness?
- *Global Monthly*

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Global Economy: The Big Picture

Growth outlook
- **Global growth:** Slowed in 2015, gradually recovering in 2016-17.
- **Emerging and developing countries:** Widespread disappointments in 2015, modest pickup in 2016-17.
- **Backdrop:** Lower commodity prices and capital flows, and weak global trade.
- **Amplifying factors:** Deteriorating potential growth and adverse spillovers from large emerging markets.

Risks
- **Sharper slowdown in large emerging markets**: Substantial effects on others.
- **Financial market turbulence:** Rising borrowing costs, heightened risk aversion, currency pressures and lingering vulnerabilities.
- Secular Stagnation
- **Geopolitical risks:** Terrorist attacks and escalating geopolitical tensions.

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Four Questions

1. How is the health of the global economy?
Remains fragile.

2. Who catches a cold when major emerging markets sneeze?
Other emerging and frontier markets; modest spillovers to major advanced economies

3. What are the major risks?
Slowdown in large emerging markets, financial market turbulence, geopolitical risks

4. What are the main policy challenges?
Limited space for cyclical stimulus; need for structural reforms

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Four Questions

1. How is the health of the global economy?

2. Who catches a cold when major emerging markets sneeze?

3. What are the major risks?

4. What are the main policy challenges?

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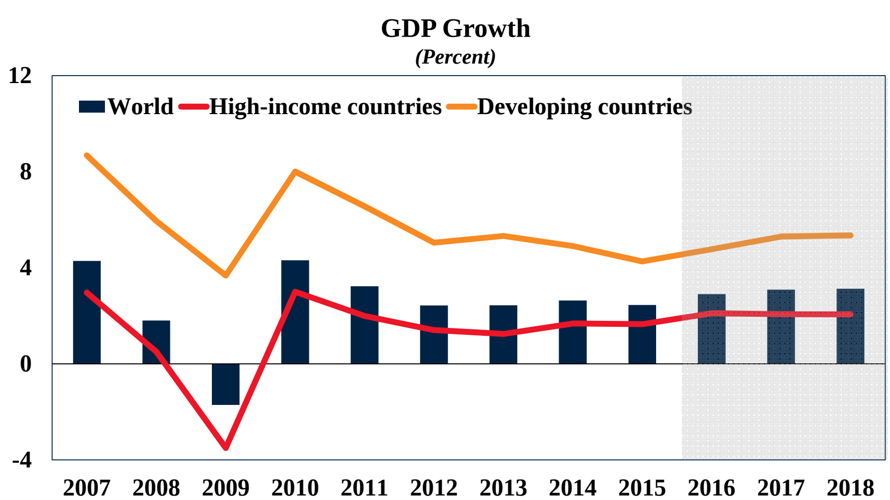
Global Growth: *Slower Growth in 2015*



Source: World Bank.
Note: Several countries were reclassified from middle-income to high-income country status in 2015, including Argentina, Hungary, and Venezuela. All series have been adjusted to ensure a constant sample according to current income status.

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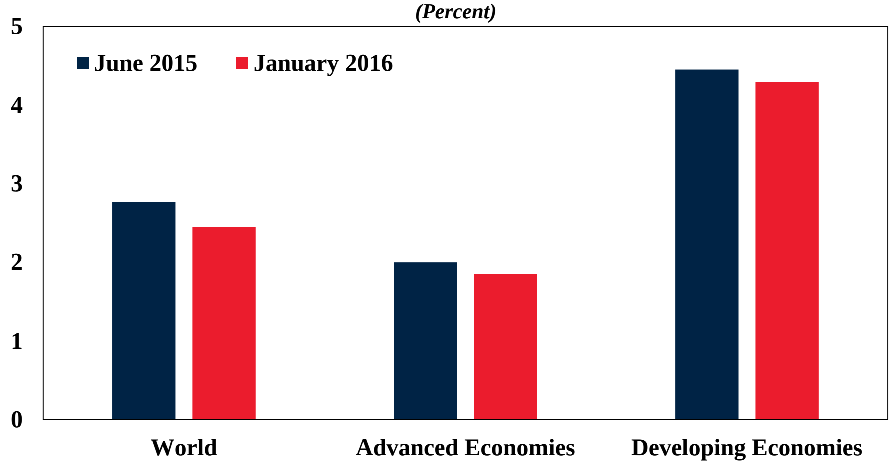
2015: *A Disappointing Year*

Growth in 2015: Forecasts and Outturns
(Percent)



Source: World Bank.
Note: Weighted average growth forecasts for 2015, published in June 2015 and January 2016 Global Economic Prospects.

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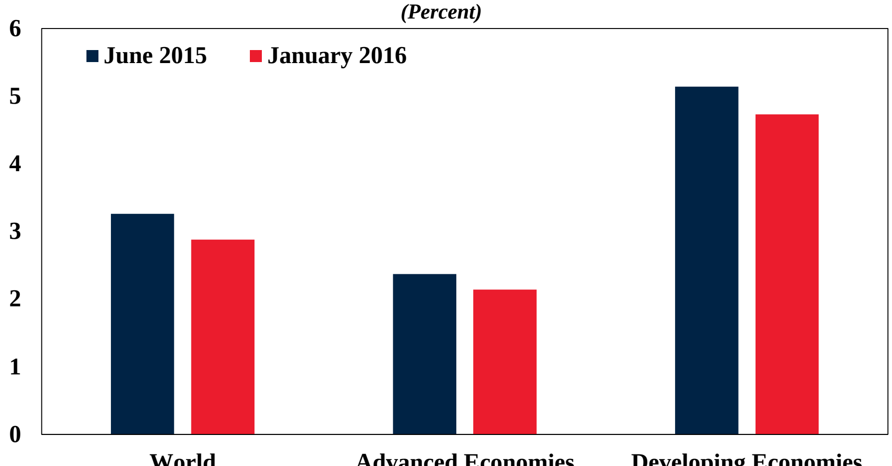
2016: *A Challenging Year*

Growth in 2016: Forecasts
(Percent)



Source: World Bank.
Note: Weighted average growth forecasts for 2016, published in June 2015 and January 2016 Global Economic Prospects.

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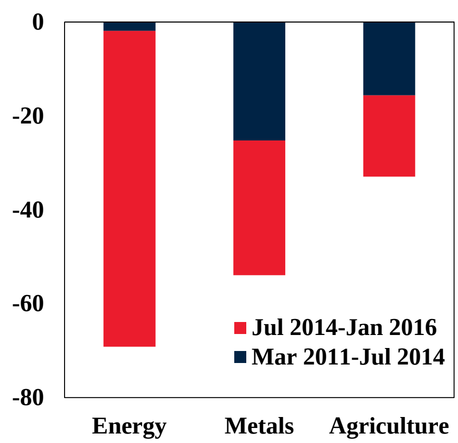
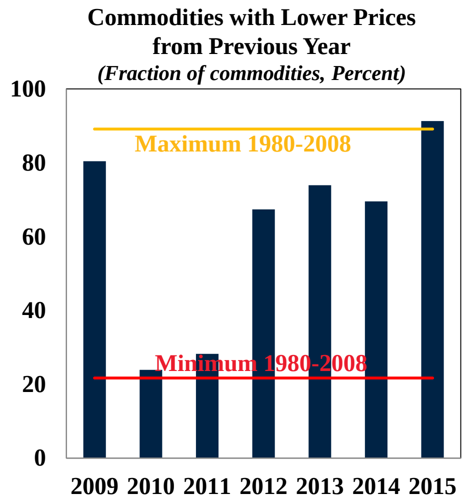
Global Backdrop:
Collapse in Commodity Prices





Source: World Bank, IMF World Economic Outlook.
Right panel: Fraction of commodities (out of a total of almost 50 commodities) for which prices declined from the previous year.

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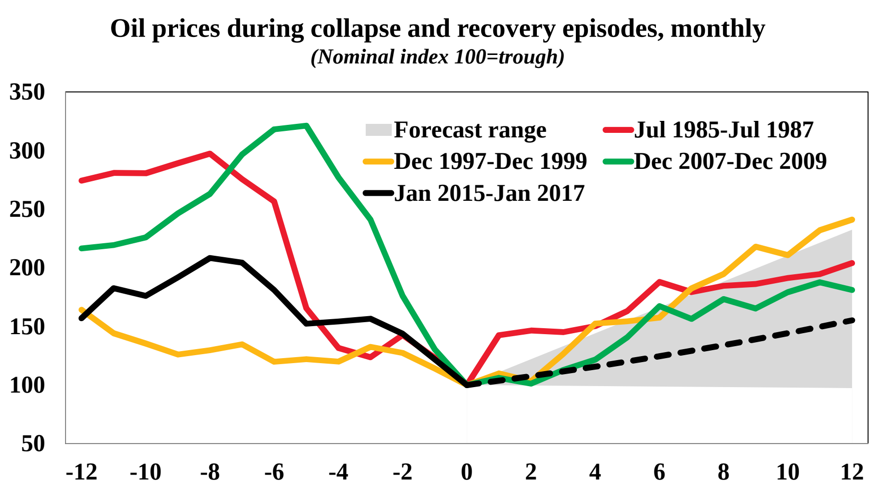
Oil Prices: Weakness Likely Persist…



Source: World Bank.
Note: Lines indicate oil prices for 12 months before and after the trough, indexed to 100 at the trough. Dashed line indicates forecast. Shaded area denotes range of forecasts by 6 major investment banks as of February 2016.

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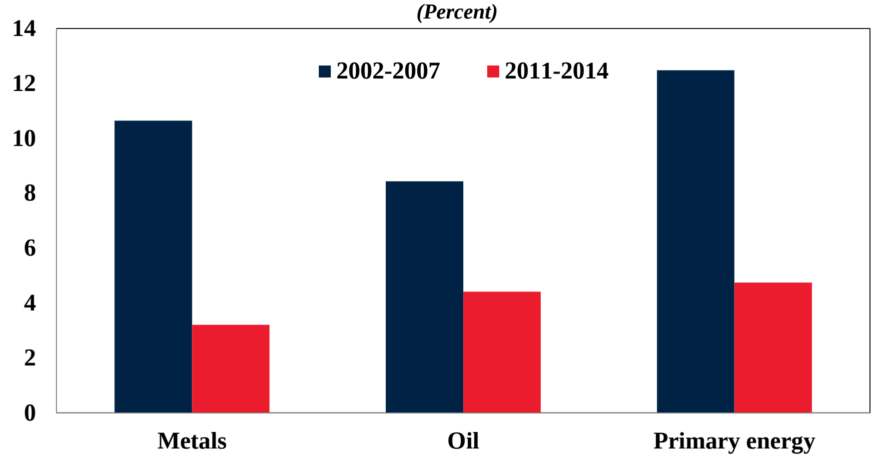
Commodity Demand: Weaker from China

China: Consumption Growth of Industrial Commodities
(Percent)



Sources: BP Statistical Review and World Bureau of Metal Statistics.
Notes: The declines in the growth rate of oil and primary energy are nearly identical because declines in the growth rate of coal have been compensated by corresponding increases in natural gas.

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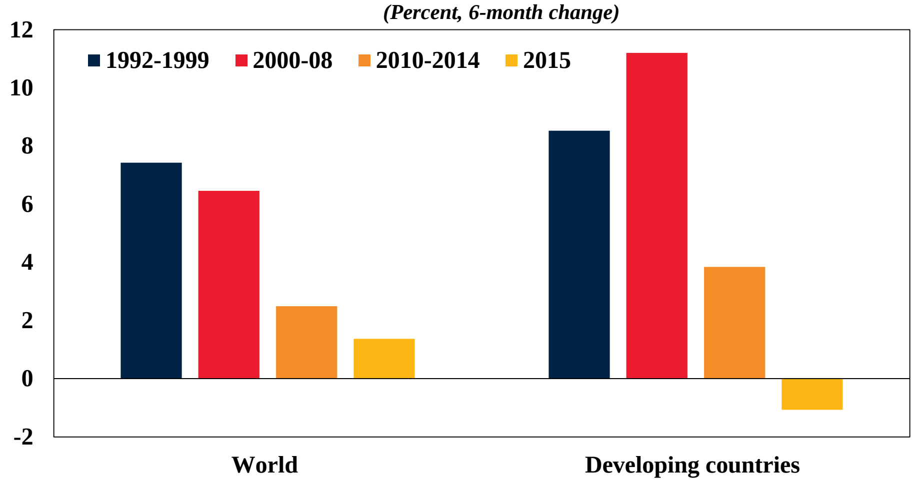
Global Backdrop: *Weak Global Trade*

Merchandise Import Growth
(Percent, 6-month change)



Source: World Bank, CPB.
Note: Merchandise import volumes. Recently-graduated high-income countries (Argentina, Chile, Hungary, and the Russian Federation) are included in the developing country aggregate. Last observation is Nov, 2015.

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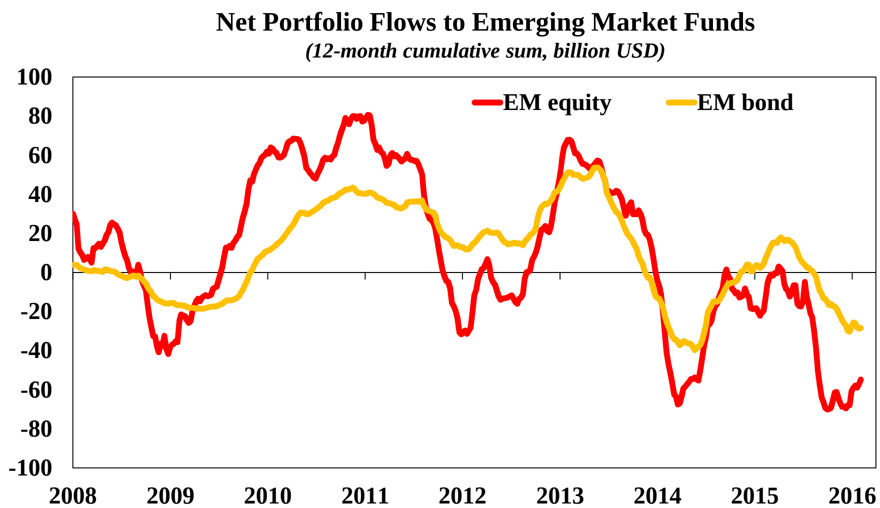
Global Backdrop:
Declining Financial Flows to Emerging Economies



Source: World Bank, EPFR.
Note: 12 months / 48 weeks cumulative sum of net inflows into emerging equity and bond funds.

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Four Questions

1. How is the health of the global economy?

2. Who catches a cold when major emerging markets sneeze?

3. What are the major risks?

4. What are the main policy challenges?

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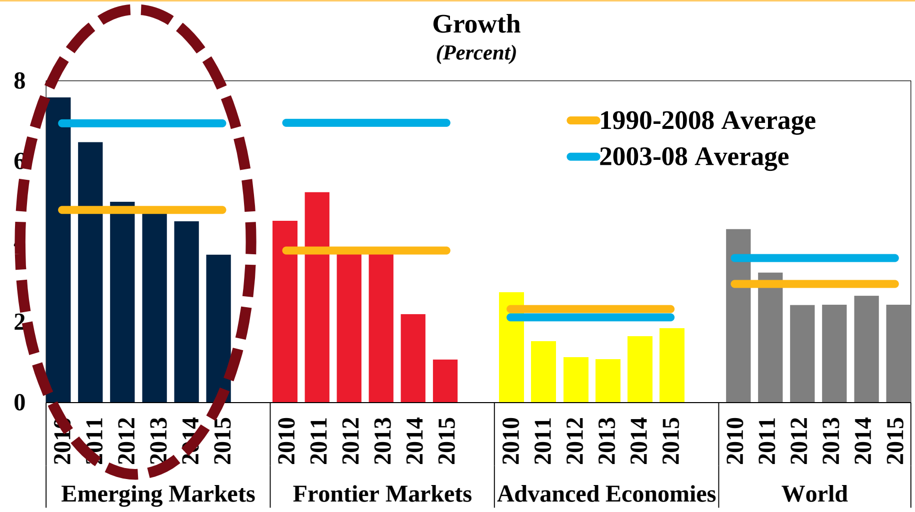
Major Country Groups:
Nostalgic about Growth…



Source: World Bank.
Note: Weighted average growth

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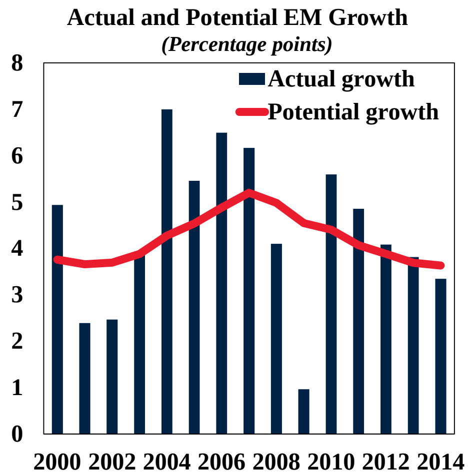
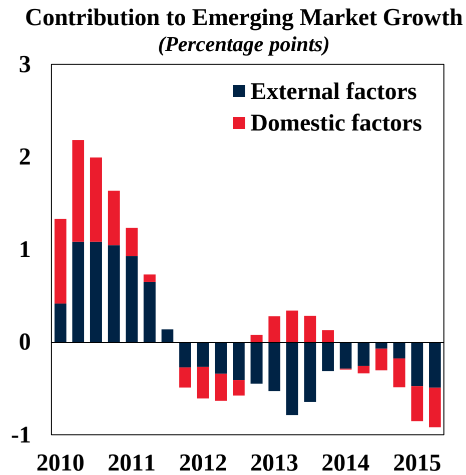
Emerging Market Weakness:
Lower Potential Growth; Larger Role for Domestic Factors





Source: World Bank.
Left panel: Unweighted average of emerging and frontier market economies.
Right panel: Each bar shows the percentage point deviation of growth from the sample mean (1998-2015). Contributions estimated from a Bayesian VAR model for 18 emerging markets. External factors include U.S. growth and 10-year bond yields, Chinese growth, EMBI spreads, and terms of trade. Domestic factors include domestic inflation, the real exchange rate, and short-term interest rates. Unweighted average of emerging markets excluding China.

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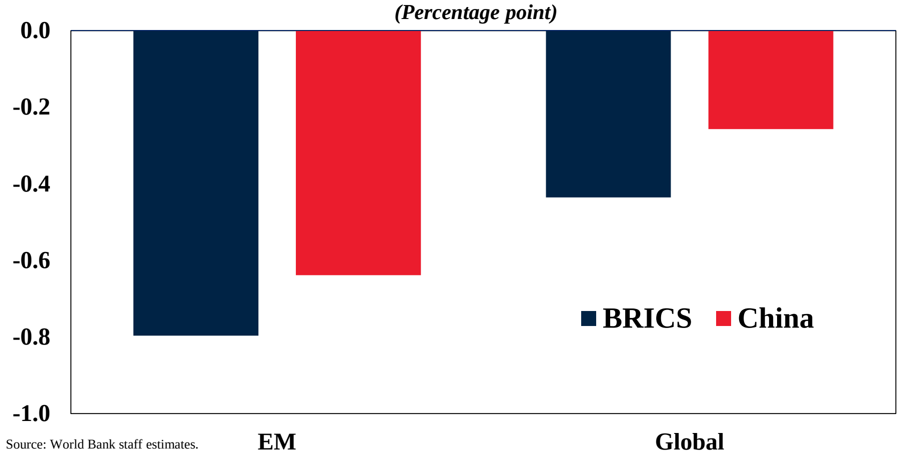
And Large Spillovers from Slowing China

Impact on Growth of 1 Percentage Point Decline in BRICS and China's Growth on Other Emerging Markets and World

(Percentage point)



Source: World Bank staff estimates.
Note: Cumulated impulse responses of EM and global growth at the two-year horizon. The shock size is such that BRICS growth declines by one percentage point on impact. The shock size for China is calibrated such that its growth declines by exactly the same amount as BRICS at the end of two years. Solid bars denote the median and the error bars denote the 33-66 percent confidence bands.

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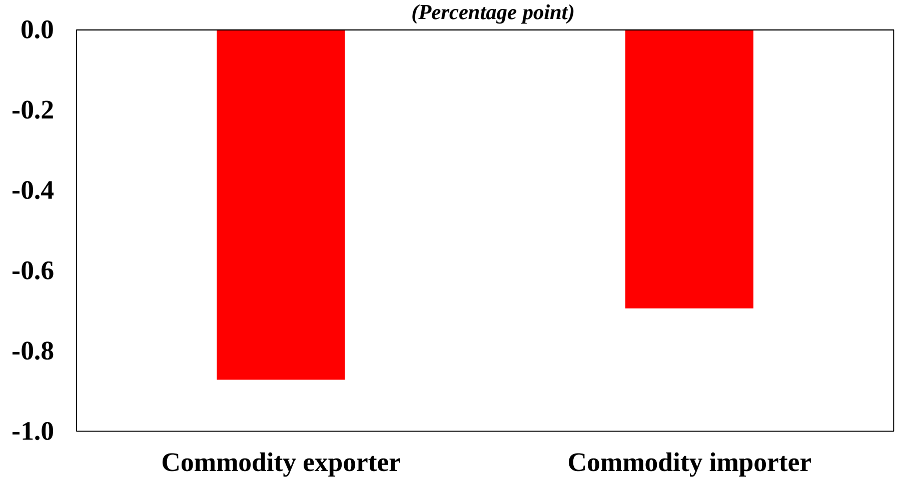
Slowing China Affects Commodity Exporters More

Decline in China Growth (1 pp) on Emerging Markets Growth

(Percentage point)



Source: World Bank staff estimates.
Left: Cumulated impulse responses of GDP growth, at the two year horizon, due to a one percentage point decline in China's growth. For each group, the figures refer to the cross-sectional average response across all the countries in that group.

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2. Who catches a cold when major emerging markets sneeze?

3. What are the major risks?

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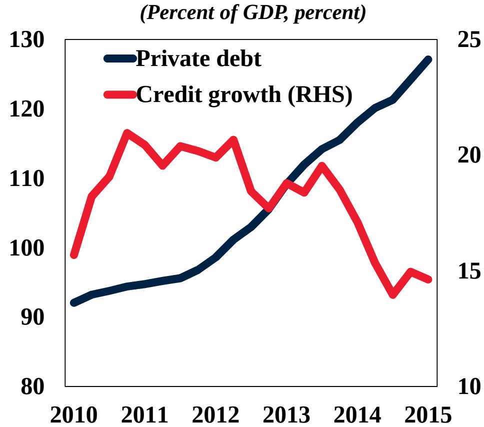
Downside Risks: Old and New

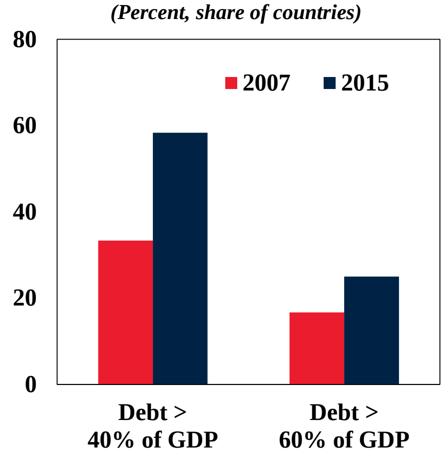
- Sharper slowdown in large emerging markets
- Financial market turbulence: ***Possible triggers:*** *Rising U.S. interest rates / U.S. dollar appreciation, heightened risk aversion, fragile liquidity conditions and deteriorating creditworthiness;* ***Impact:*** *Slowing capital flows and risk of sudden stops.*
- Tail risk *(a perfect storm?)*: *Sharper slowdown in large emerging markets combined with financial turbulence*
- Secular stagnation
- Geopolitical risks: ***Terrorist attacks:*** *Limited effects of isolated events so far but potentially large effects possible;* ***Geopolitical tensions:*** *Regional and global repercussions;* ***Refugee crisis:*** *Regional repercussions.*

Financial Market Turbulence: Elevated Debt

Private Debt and Credit Growth in Emerging Markets
(Percent of GDP, percent)



Number of Emerging Markets with Elevated Government Debt
(Percent, share of countries)



Source: World Bank, International Monetary Fund, Bank for International Settlements.
Left panel: Weighted-average of debt-to-GDP ratios of households and non-financial corporations in Brazil, Russia, India, South Africa, Mexico, Indonesia, Malaysia, and Turkey. Right panel: EM with general government debt above 60 percent of GDP in 2015 include Brazil, Egypt, India, Hungary, Morocco, Pakistan.

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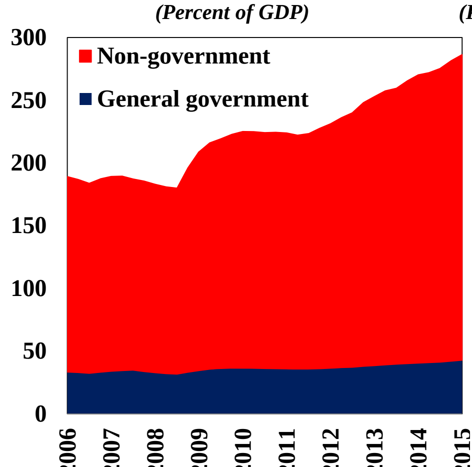
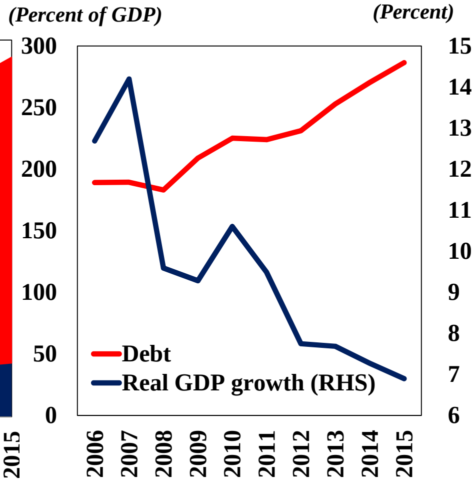
China's Debt and Growth: Soft Landing?

Stock of Debt
(Percent of GDP)



Debt and Growth
(Percent of GDP) *(Percent)*



Source: BIS, IMF, WB.
Note: A. Consolidated figures for the general government sector.

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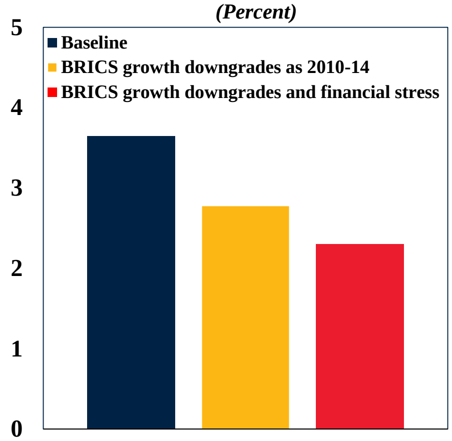
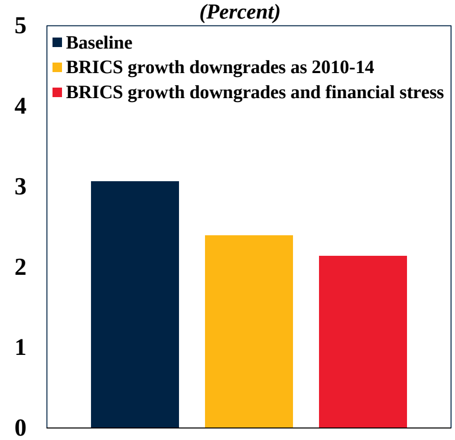
Tail Risk:
Sharp Slowdown in BRICS and Rising Risk Aversion

Emerging Market Growth Excl. BRICS, 2016
(Percent)



Global Growth, 2016
(Percent)



Source: World Bank staff estimates.
Note: Conditional forecasts of emerging markets excluding BRICS and global growth, with conditions imposed on future BRICS growth and EMBI. The conditions are: (i) BRICS growing at the current rate in 2015: BRICS continue to grow at its current 2015 level (annualized rate of 3.2 percent) during the forecast horizon; (ii) BRICS growth with forecast downgrades as during 2010-14: BRICS continue to grow during the forecast horizon at its current 2015 level minus the average forecast downgrades it saw during 2010-14. The forecast downgrades are based on the World Bank forecasts; (iii) BRICS growth with forecast downgrades and financial stress: The second scenario is combined with EMBI rising by 100bp during the forecast horizon. Global growth is the GDP-weighted average of BRICS, emerging markets excl. BRICS, frontier markets, and G7 growth.

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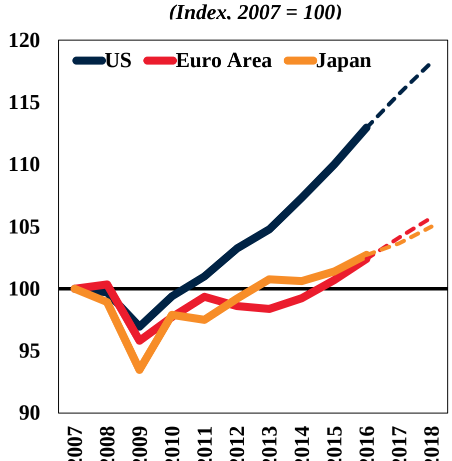
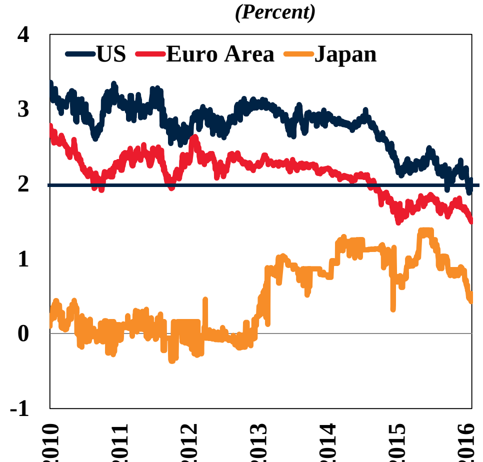
Advanced Economies:
Paces of Recovery Different; Low Inflation Common

GDP
(Index, 2007 = 100)



10-Year Inflation Expectations
(Percent)



Source: World Bank, Bloomberg.
Note: 10-year inflation expectations derived from 5-year forward contract on 5-year interest rate swaps. Last observation is Feb 4, 2016.

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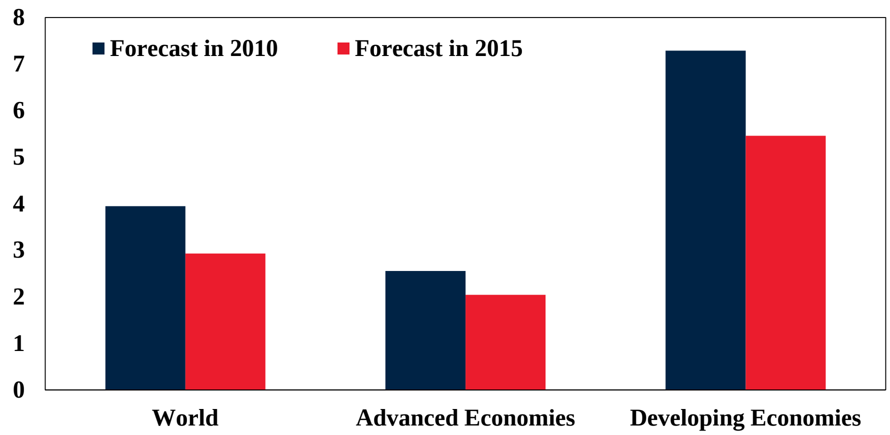
Secular Stagnation?
Long-Term Forecast Downgrades

Growth in 2020: Forecasts in 2010 and 2015
(Percent)



Source: World Bank.
Note: Weighted average growth October forecasts for 46 countries for which long-term consensus forecasts are available.

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Four Questions

1. How is the health of the global economy?
2. Who catches a cold when major emerging markets sneeze?
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4. What are the main policy challenges?

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What Are the Main Policy Challenges?

Monetary policy, exchange rate and capital flows

- Capital flow and currency pressures: *Complicate the attainment of domestic policy objectives.*
- Priority: *Credible commitment to price and financial stability.*
- Challenge: *Limited space. Decoupling monetary policy from the U.S. Fed?*

Fiscal policy

- Commodity importers: *Depleted fiscal buffers.*
- Commodity exporters: *Significant pressure on revenues.*
- Challenge: *Limited space. Availability and effectiveness of fiscal policy?*

Structural policy

- Reforms: *Key priority in slow growth environment.*
- Challenge: *Appetite for reforms?*

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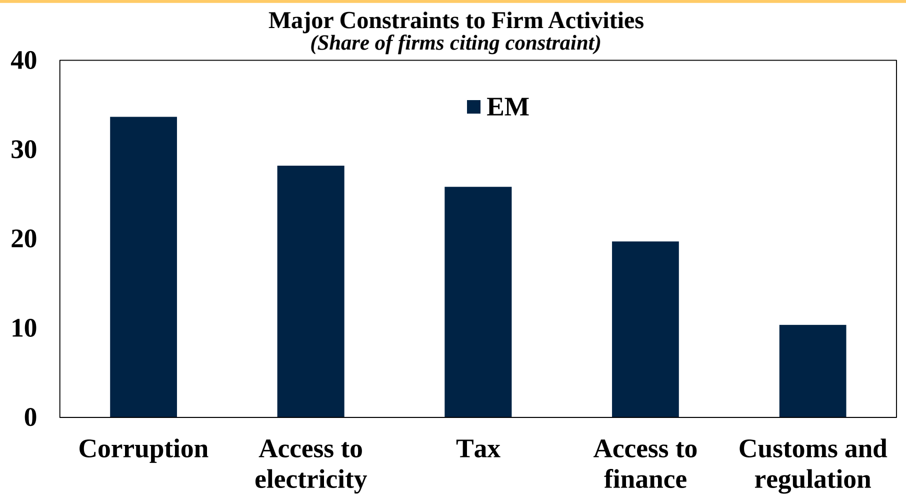
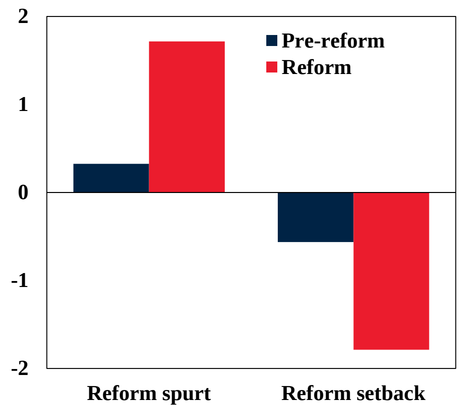
Widespread Growth Bottlenecks: *Need for Structural Reforms*



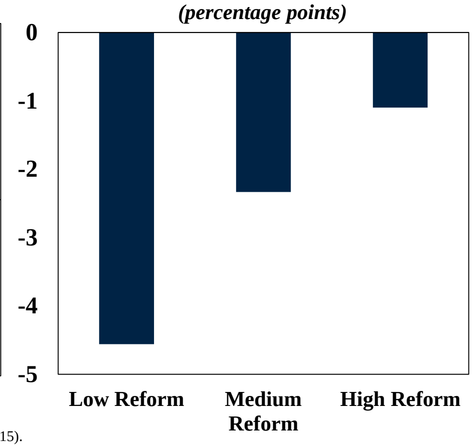
Sources: World Bank Enterprise Surveys, OECD Product Market Regulations index.
Note: Left panel: for each indicator, bars show the EM/FM average of the country-specific percentage of firms citing that indicator as a major constraint. Each diamond shows that indicator for high-income OECD economies. EM: Malaysia, Thailand, Qatar, Saudi Arabia, South Africa, and the United Arab Emirates are not available. Right panel: restrictiveness of product market regulations measured by surveys on barriers to entrepreneurship, barriers to trade and investment, and state control. The index ranges from 1 to 6, where 1=least restrictive and 6=most restrictive. Among AE, data are not available for Hong Kong, Malta, Singapore, and the U.S. The latest available data is for the year 2013.

Structural Reforms:
Key Priority in a Slow Growth Environment

Growth During Reforms and Setbacks
(Percentage point differential)



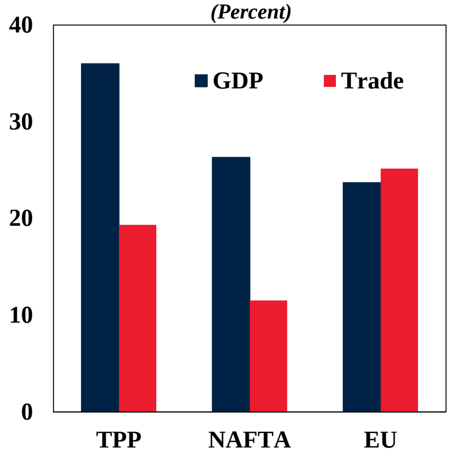
Change in Growth and Governance Quality: 2010-14
(percentage points)



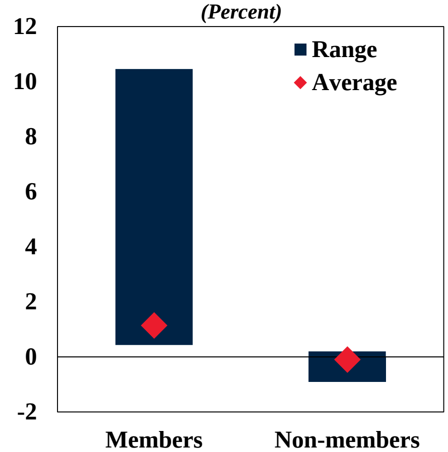
Source: World Bank's World Governance Indicators (WGI); Didier et al. (2015).
Left panel: Methodology as in Didier et al. (2015). Right panel: magnitude of slowdown is the change in growth during 2010-14. Low, medium, and high reform refer to the 25th, 25th-75th, and 75th percentiles of the distribution in EMs and FMs' change in average governance from 2010-2014. Average governance is defined as the unweighted average of the percentile score of each economy's regulatory quality, government effectiveness, rule of law, and control of corruption in the WGI Index. The WGI indicators are principal components of a wide range of survey-based and other indicators.

Trans-Pacific Partnership:
Positive Impact for Members; Limited Effects for Non Members

Major Regional Trade Agreements: Share of Global GDP and Trade
(Percent)



Output Impact of TPP: Change in GDP by 2030
(Percent)



Source: Source: World Trade Organization's Regional Trade Agreement database; World Development Indicators; World Integrated Trade Solution (WITS) database.
Note: EU = European Union; NAFTA = North American Free Trade Agreement; TPP = Trans-Pacific Partnership.

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Four Questions

1. How is the health of the global economy?
Gradually healing but still fragile. Growth slowed in 2015, moderate acceleration in 2016

2. Who catches a cold when major emerging markets sneeze?
Other emerging and frontier markets; modest spillovers to major advanced economies

3. What are the major risks?
Slowdown in large emerging markets, financial market turbulence, geopolitical risks

4. What are the main policy challenges?
Limited space for cyclical stimulus; need for structural reforms

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Questions & Comments
Thanks!

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