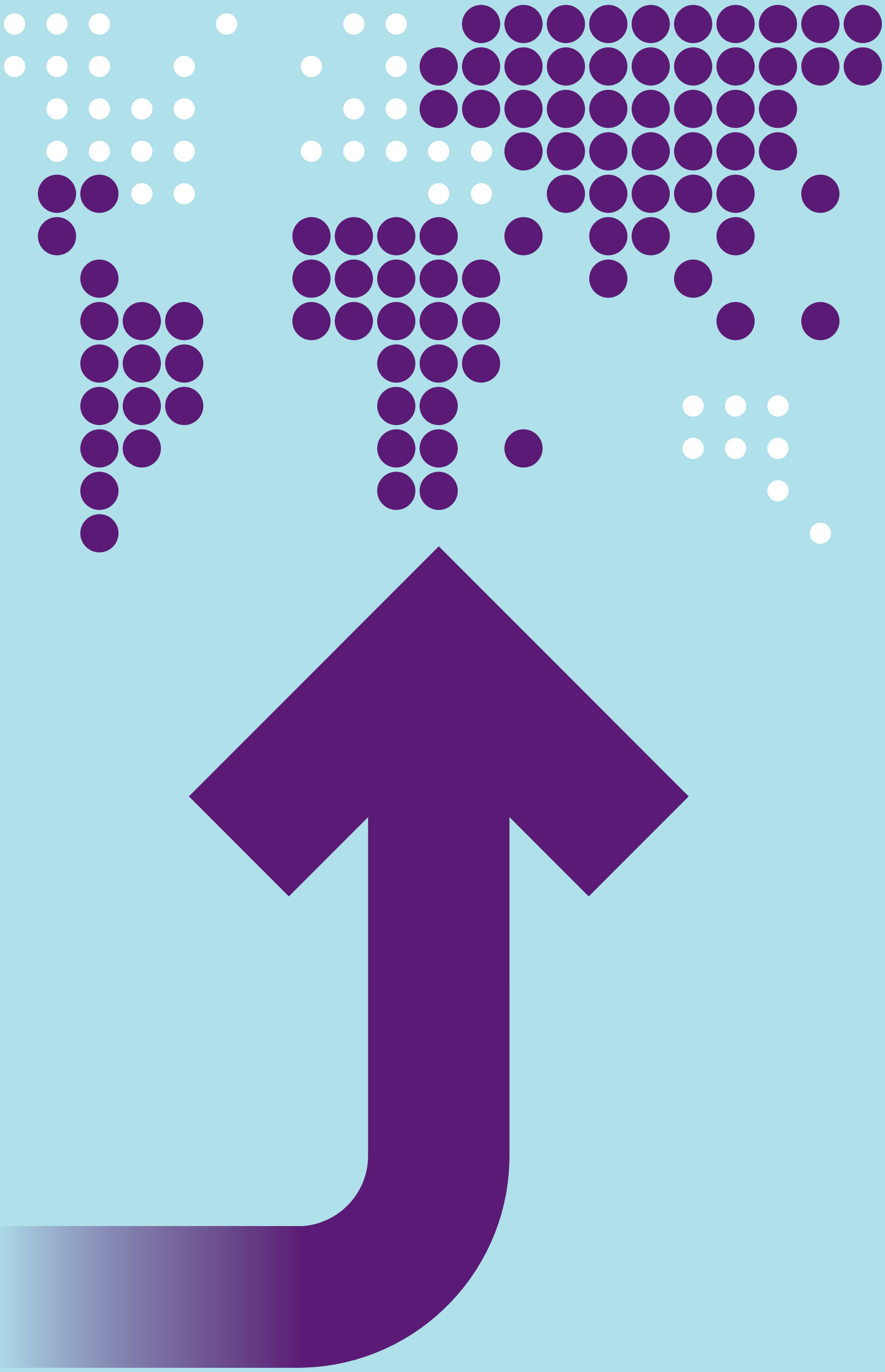

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Successful Macroeconomic Performance: Launching Long-Term Reforms

Discussion Paper

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This Discussion Paper is a draft revised version of Chapter 3, Successful Macroeconomic Performance: Launching Long-Term Reforms from *Latin America 2040—Breaking Away from Complacency: An Agenda for Resurgence*.

Successful Macroeconomic Performance: Launching Long-Term Reforms

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Special thanks to: Harpaul Alberto Kohli and Dana Sleeper

Introduction

Events in the emerging world have been far from predictable since the onset of the global crisis in 2008. At that time, the prospects for the world economy looked good. There were concerns about the effect of a shallow recession in the United States, but the general perception was that Asia and, to a large extent, Latin America and other regions were doing well. Many thought, incorrectly, that the countries in these regions had "decoupled" from the advanced economies, and wealth would grow with few restrictions. Policies in these countries had been conducive to significant improvements in fiscal and external balances, with few exceptions, and international reserves were at record levels. Policymakers felt comfortable. Commodity prices were going up, foreign demand was strong and there was no serious worry about financing, as credit was plentiful and there was little concern about creditworthiness. Problems were only affecting the United States and a few other developed countries.

From then on, the world confronted its worst world-wide financial crisis of the last fifty years, known as the Great Recession. There was a major rebound subsequently, and most emerging economies recovered quickly and continued to expand at a rapid pace until 2011. At that point output growth, while still significant, lost some steam on account of the lingering consequences of the Great Recession on the advanced countries, and particularly on Europe. The crisis continues to affect many advanced economies, and there are signals of a slowdown in China and other Asian countries, as well as in Latin America. Thus, the problems are far from over as of mid-2012, as is clearly and dramatically shown by the public debt and banking sector issues of the Euro-zone. Actions in Europe have been taken late and slowly, with insufficient scope of reform, and therefore there is increasing risk of a full-fledged crisis, if not for the region as a whole, at least for some of its members. In particular, Greece, Spain, and Portugal and to a lesser extent Italy and Ireland, are having mounting problems; these are aggravated by further political and economic issues in other countries in the region, associated with the course of fiscal and monetary policy for the Euro-area.

Some analysts predicted that the intensity of the global financial crisis was equivalent to that of the Great Depression of 1929–33. Now, four years after the onset of the recession, the prospects are more positive but subject to downward risks. The conditions in the financial institutions of the US have improved from the dramatic position of 2008, even though with hesitation, but those in the EU remain weak, as many institutions show large capital shortfalls and considerable declines in deposits. Global GDP has fallen by far less than during the Great Depression, and has recovered in countries like the US—even though economic activity has slowed in recent months—but it has remained depressed in Europe where the debt problem seems to have put a damper into the region's growth prospects. Moreover, unemployment is still high in the US and has been growing in Europe.

While the global financial crisis had serious consequences for the emerging economies, they recovered much faster and stronger than the advanced countries, as the Asian and Latin American countries were able to absorb the impact of the crisis. However, they have been slowing down, in part reflecting the weak advanced countries' demand for their exports. The relative strength of the recovery reflected the timely fiscal and monetary stimulus measures applied by the advanced as well as many emerging economies, as these measures helped ameliorate the impact of the crisis and stabilize economic performance. But, for most countries, the expansionary measures cannot be carried out in the long run without creating a serious debt problem, and thus undermining a sustained recovery.

Since the onset of the Great Recession, markets have been very volatile. From mid-2008 to early-2009, commodity prices declined by more than one half. While they have recovered subsequently, commodity prices remain volatile, as demand for manufactured goods declined sharply. Stock market capitalization also declined by about one half but showed a good recovery subsequently. Currencies in many emerging countries depreciated as capital flows reversed, seeking a safe haven, but in many countries inflows recovered. In fact, the authorities struggled with what some claimed were actions on the part of the advanced economies to devalue their currencies. The latter contend, however, that currency devaluations were part of the need for a loose monetary policy consistent with a stimulus support policy. As of mid-2012, some of these flows had reversed, and the currencies of emerging economies, particularly in South America had depreciated again.

This paper is intended as a background piece that shows the close interaction between emerging markets and the rest of the world, with a particular focus on Latin America and Asia. It highlights the importance of pursuing strong macroeconomic policies. These policies, which had been elusive for long, have become an integral part of economic strategy for most of Latin America with clearly favorable results, even in the context of the turmoil surrounding the world economy. The paper reviews on a world-wide basis the origins of the crisis and how it affected the emerging market economies, mainly in Asia and Latin America. It also discusses what happened subsequently and what can be expected, given that financial volatility and recessionary forces may continue to prevail even during the current recovery.

The Conditions in Asia and Latin America Prior to the Crisis

Both Emerging Asia and Latin America had not reacted in response to the international turbulence that was emerging in 2006–07. The authorities viewed their continued growth as a clear signal of a new resiliency. Without seeking to over-generalize, below are the broad developments that may explain the perceived resiliency.[1]

- For years, Latin America was characterized by high volatility and about the lowest overall growth rate of any emerging region. However, starting in the 1990s, important policy framework and institutional reforms were implemented with a view to improve economic performance, with reductions in poverty. Thus, during 2003-08 there was an acceleration of growth, helped by the favorable conditions in the world. Growth in Asia had persisted for more than two decades, with the exception of the traumatic "Asian Crisis" period, but with a high and steady performance subsequently. Strides in terms of poverty and in quality of life had been impressive.
- Before the 1990s, Latin America had been the worst performer with regards to inflation, but has generally converged to world inflation, helped by these countries' efforts to control both monetary and fiscal policy. Developing Asia was less successful in reducing inflation, but in most cases had not

1 Claudio Loser: The Prospects for Latin America: Risks and Opportunities with a Historical Perspective (Rev. June 2008).

experienced hyperinflation. Monetary policy was generally prudent, particularly after the Asian Crisis, and fiscal policies helped reduce public debt. The NICs had low inflation and generally good fiscal policies as well.

- Both regions saw an increasing role of international trade and FDI. Latin America reduced its trade barriers which had been very high in the past, although with some reversal in reaction to international conditions. To a large extent, exports and investment have focused on natural resources and commodities.[2] With considerably more differences, there was also an emphasis on natural resources in South and South East Asia. However, a major process of incorporation of a large and excluded workforce in China and India, a complex process of industrialization, and a rapid integration in the productive process helped create a sophisticated and highly integrated production process.
- There was a sharp reduction in the previously high dependence on private capital flows, while international reserves rose to record levels throughout the emerging world and the debt burden was reduced. These trends have been strengthened by growing workers' remittances to Asia and Latin America.
- Many of the changes described above were the result of the efforts in the 1990s by many countries to engage in market-friendly reforms, including reforms on taxation, public finances, financial sector, trade, privatization, and labor markets. The impact of these policies was dramatic, even though certain countries went through major crises due to individual or regional circumstances (the Asian Crisis, Argentina, Brazil and Mexico come to mind, although in most cases additional reforms helped improve performance significantly).[3]
- Under these circumstances, with improved productivity, and in the case of Asia, ample markets and large supplies of initially unskilled but increasingly skilled labor, both Asia and Latin America became attractive destinations for FDI, as investors saw an opportunity to share in the new regional prosperity.[4] Moreover, countries like Brazil, China, India and Mexico have become key players in the international cooperation dialogue.

Recent Evolution of the World Economic Environment

Over the last decade, Asian countries were able to emerge from the serious crisis that had brought many of them down in the late 90s. Helped by the consistent growth of China and, to an increasing extent, India, the Asian region witnessed a stellar performance. Concurrently, after a period of low economic growth, persistent crises, and high volatility that extended through the 1990s, Latin America

2 Claudio Loser: "Cross-Border Trade and Investment among Emerging Economies: Lessons from differing experiences in Africa, Asia and Latin America", Emerging Market Forum 2008.

3 The market-friendly reforms of the 1990s have been subject to considerable controversy in political and economic circles in developing countries. For example, some poorly implemented privatizations, and the creation of protected private monopolies instead of public companies gave privatization a bad reputation, well beyond what was warranted. Most privatizations had worked well, but those few that did not, were described as emblematic of what the critics considered the wrong way.

4 Corporacion Andina de Fomento: Reflexiones sobre como retomar el Crecimiento, RED 2004-Corporacion Andina de Fomento; América Latina en el comercio global, RED 2005 CAF; Camino a la Transformación Productiva en América Latina, RED 2006. CAF, Caracas, RED; Oportunidades en América Latina: Hacia una Mejor política social- RED 2007-2008 CAF.

also made a very strong recovery, helped by the emergence of Asia as a major player.

But the global crisis hit hard and the impact on the balance of payments and on domestic activity was very serious. The adverse terms of trade effect aggravated the situation, compounded by a massive loss in financial wealth. Nevertheless, the economies began to recover quickly, in response to the demand-support actions taken by their policy makers as well as by the major countries.

Genesis of the Great Recession

The reasons for the 2008–09 crises are complex and linked to the financial market tensions of previous years. A period of rapid growth was fraught with dangers that were not anticipated by most even a year before. For four years through the summer of 2007, the global economy boomed. Global GDP rose at an average of about 5 percent a year, the highest sustained rate since the early 1970s. About three-fourths of this growth was attributable to a broad-based surge in the emerging and developing economies. Inflation remained generally contained, even if with some upward pressures especially in food and fuel prices.

These developments led to the perception that the world economy was entering a new and prosperous stage and, using an abused phrase, entailed a new economic paradigm of uninterrupted strong growth. The value of financial and real assets was growing without a perceptible limit, and commodities were reaching record heights, as described in further detail below. Unfortunately, the most important factor behind these developments was not a change in paradigm. It was the emergence of growing imbalances among the main economies of the world. The US, with low rates of savings at the time, embarked on a private consumption binge—supported by reckless bank lending—and growing fiscal deficits, which translated into growing external current account deficits. These were financed by the surpluses of oil producing countries, China, Japan and, to a lesser extent, surplus countries in Europe and Latin America. These imbalances grew rapidly, but markets did not respond to the mounting dangers on the horizon before 2007. However, the US dollar started to weaken in international markets and there were growing signs of impending problems. These trends were magnified by an increasingly integrated global trading and financial system which accelerated the transmission process; inadequate and weakening regulation and supervision of national financial systems and fragmentation of global regulation; and weak surveillance by the IMF and other multilateral organizations. The problems were aggravated by weak and uncoordinated policy responses to the initial signs of trouble in the financial markets.[5]

In the end, the markets, and the world economy overall, responded strongly to these imbalances. After experiencing a growth rate of about 5 percent a year in the period 2004–07, growth slowed to 3 percent in 2008, and output actually declined by 0.6 percent in 2009—the first such contraction since the Second World War—although with a strong rebound in 2010 and to a lesser extent in 2011. However, the modest global decline in 2009 shows significant differences among countries and regions (Table 1). Economic growth rates in 2009 declined by two thirds among developing and emerging economies. Latin America experienced a GDP decline of 1.6 percent, mainly on account of Mexico and, to a lesser extent, Venezuela. The worst affected regions include the European Union and the CIS countries, with contraction rates of 4.2 percent and 6.6 percent,

5 Jack Boorman: Remarks for the South Asia Forum on the Global Economic and financial Crisis, March 2009.

Table 1 **GDP Growth Rates**

	2002–8	2009	2010	2011	2012	2013
World	4.2	-0.6	5.3	3.9	3.5	4.1
Advanced economies	2.2	-3.6	3.2	1.6	1.4	2.0
United States	2.2	-3.5	3.0	1.7	2.1	2.4
European Union	2.2	-4.2	2.0	1.6	0.0	1.3
Japan	1.2	-5.5	4.4	-0.7	2.0	1.7
China	11.0	9.2	10.4	9.2	8.2	8.8
India	7.7	6.6	10.6	7.2	6.9	7.3
NICs	4.7	-0.7	8.5	4.0	3.4	4.2
Latin America	4.1	-1.6	6.2	4.5	3.7	4.1
Argentina	5.7	0.9	9.2	8.9	4.2	4.0
Brazil	4.0	-0.3	7.5	2.7	3.0	4.2
Chile	4.7	-0.9	6.1	5.9	4.3	4.5
Colombia	4.8	1.7	4.0	5.9	4.7	4.4
Mexico	2.6	-6.3	5.5	4.0	3.6	3.7
Peru	6.8	0.9	8.8	6.9	5.5	6.0
Venezuela	5.1	-3.2	-1.5	4.2	4.7	3.2

Source: International Monetary Fund, World Economic Outlook Database, April 2012 and own estimates

respectively. The advanced economies declined by 3.6 percent. Some other regions did much better, including the emerging market countries of South Asia, Africa and the Middle East, most of which avoided recession. While emerging Asia as a whole grew by some 5 percent, the NICs contracted by 0.7 percent. China and India, the largest emerging economies in the region grew by 9.2 percent and 6.6 percent, respectively. While surprisingly good in the 2009 environment, these growth rates were somewhat below those registered by these countries in earlier years.[6] Under these conditions, policy makers adopted stimulus packages that ameliorated the impact of the crisis and helped their economies recover. In some cases, demand pressures became so strong that they required some withdrawal of the stimulus, as was the case of China in early 2010.

The global contraction gave way to renewed growth in subsequent years, with world GDP increasing by 4.5 percent on average in 2010–11. However, in the face of continuous fiscal policy uncertainty in the US and the protracted difficulties in the Euro area, growth has tended to slow down in the latter part of 2011 and in 2012. The performance in the advanced economies remains considerably weaker than that in the emerging market economies; and growth rates within regions also vary substantially. The advanced economies grew by 3.2 percent

6 The Impact of the Financial Crisis on Emerging Market Economies: The Transmission Mechanism, Policy Response and Lessons-Jack Boorman, Mumbai, India, June 23, 2009.

in 2010, but slowed to 1.6 percent in 2011, and are expected to slow down further in 2012, with only limited recovery subsequently, well below potential. The emerging economies grew by some 7 percent a year in the last two years with a prospective growth of almost 6 percent in 2012–13 (Figure 1). There are significant caveats about future developments, particularly in light of the debt crisis in the Euro zone and the fiscal cliff in the US, weaknesses in Europe's banking system, and the necessary fundamental changes in the Euro area that may entail a further slowdown in growth from current (July 2012) projections.

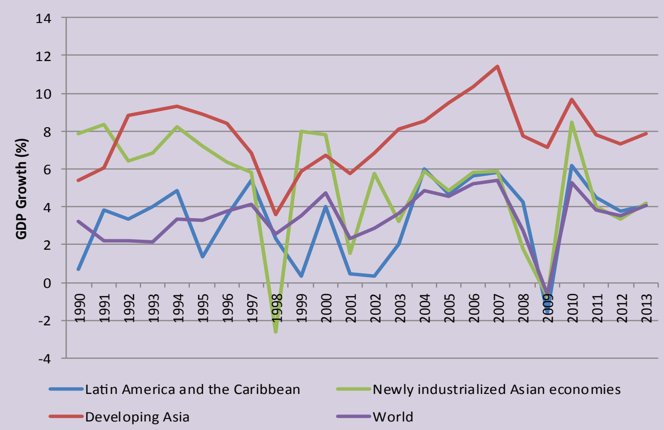
There have been lags in the recovery process—especially in the recovery of employment. This is particularly the case in the advanced economies where employers commit to new hiring only after clear signs of policy direction and a rebound in activity. Thus, unemployment is expected to come down only very slowly, and may be reaching new heights in some of the advanced economies. Renewed global growth will be secured only if the macroeconomic structures of a number of economies—especially the savings balances in the United States and China—continue to improve (in opposite directions), and the required structural changes take place in Europe, particularly in the Euro zone.

Inflationary Pressures

After attaining significant lows, particularly in Latin America, inflation in the emerging and developing economies rose in 2008 in line with commodity prices (particularly food and fuel), and reached 7.7 percent. Inflation declined somewhat in 2009, to 5.6 percent, as price pressures receded with the decline in commodity prices, with 5.3 percent in Developing Asia and 4.8 percent in Latin America, despite significant devaluations (Table 2 and Figure 2).

With the subsequent output recovery and the consequent increase in commodity prices, mainly arising from the continued high demand in Asia, inflation rose in 2010–2011, but to levels below those observed in 2007–08. In the advanced economies,

Figure 1 **Growth of GDP in Developing Asia, Latin America and the World (Annual Percent)**



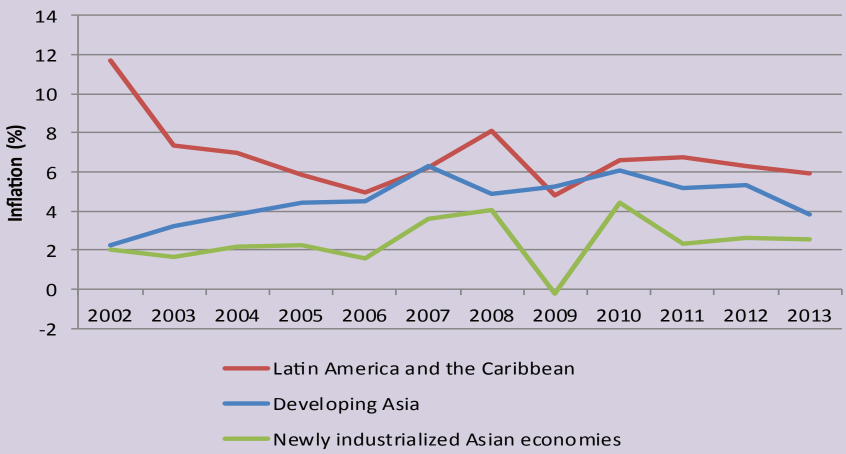
Source: International Monetary Fund, World Economic Outlook Database, April 2012

Table 2 **Inflation (EOP)**

	2002–2007	2008	2009	2010	2011	2012	2013
Advanced economies	2.2	1.6	1.0	1.9	2.5	1.8	1.7
Emerging and Developing Economies	6.4	7.7	5.6	6.7	6.5	6.2	5.1
Latin America	7.2	8.1	4.8	6.6	6.7	6.3	5.9
Argentina	13.6	7.2	7.7	10.9	9.8	10.3	10.3
Brazil	7.1	5.9	4.3	5.9	6.5	5.0	5.0
Chile	3.4	7.1	-1.5	3.0	4.4	3.2	3.0
Colombia	5.7	7.7	2.0	3.2	3.7	3.1	3.1
Mexico	4.3	6.5	3.6	4.4	3.8	3.6	3.1
Peru	2.3	6.7	0.2	2.1	4.7	2.6	2.3
Venezuela	21.9	30.9	25.1	27.2	25.2	33.4	28.7
Developing Asia	4.1	4.9	5.3	6.1	5.2	5.3	3.9
China	2.7	1.2	1.9	4.6	4.1	3.5	2.5
India	4.8	9.7	15.0	9.5	6.6	8.5	6.3

Source: International Monetary Fund, World Economic Outlook Database, April 2010. Argentina- unofficial estimates

Figure 2 **Inflation (in %)**



Source: International Monetary Fund, World Economic Outlook Database, April 2012

even with large oil price increases, underlying inflationary pressures have been contained despite expansionary monetary policies, reflecting continued weak demand and deleveraging. In fact, concerns about inflation are divided between those that are more preoccupied with continued deflation, in response to recent weak world aggregate demand, and those that are more concerned about inflation in the medium-term because of the lagged effects of the expansionary macroeconomic policies.

Concerns about inflation seem to dominate in the emerging world. This was initially partly offset by the appreciation of key countries' currencies, like in Brazil, Chile, and Colombia. However, since early 2012, the currencies of these countries have tended to depreciate as external economic conditions weakened and the US Federal Reserve ended its quantitative easing policy.

Among some of the most traumatic consequences of the global financial crisis was the loss of valuation of financial assets worldwide, which reached well over US$50 trillion, equivalent to about one year of world GDP. The decline reflected the reduced capitalization of stock markets, loss in the value of mortgage-backed securities and other financial and real assets, and the depreciation of many currencies with respect to the US dollar. While this has been reversed in part, the impact of these financial losses continues to weigh upon the world economy. This issue is discussed in detail below.

The Liquidity Crisis of 2008–09 and its Aftermath

Interbank markets virtually locked up in late-2008, as trust in contractual counterparties evaporated. In September, the disintermediation process that had been observed for at least a year led to the worst liquidity crisis of the last thirty years, or perhaps since the Great Depression of 1929. The closing of the long established Lehman Brothers aggravated the panic in the financial markets, as doubts about the stability of the domestic and international payments system increased.[7] The cost of intermediation between financial organizations rose rapidly, together with a generalized paralysis in transactions between financial institutions.[8] In fact, the financial system virtually froze.

To respond to this situation, the authorities of many economies, particularly the European Union and the US, adopted extraordinary measures to stabilize the markets, by providing liquidity and other financial support on a massive scale, extending deposit guarantees and adopting legislation whereby public funds would be used to support problematic assets of banks. In the case of the US, it was done through the TARP program (Troubled Asset Relief Program), with further actions taken subsequently by the new US administration regarding a stimulus to the US economy, and the strengthening of the financial system. Similar actions were announced in other major countries, including programs of bank acquisitions in the United Kingdom and initially poorly-coordinated actions within the Euro zone and in other European Union members and elsewhere.

7 Although subject to debate, part of the financial collapse may have occurred because of actions, or omissions by the authorities. A possible example is the demise of Lehman Brothers, without looking carefully at the consequences, and that many actions were seen as haphazard measures, without a systematic approach.

8 During this period an obscure concept became instantly fashionable, the TED spread. The TEDspread is the differential between US treasury rate and LIBOR (London Interbank Offer Rate), which measures the lending costs among financial intermediaries. This differential, which had been below 1% for most of the last quarter century, showed significant volatility in mid-2007 and rose to a peak of 5% in October. It fell subsequently and now is back to historical levels, helped by key Central Banks.

As described below in more detail, actions were also taken in Latin America and Asia.

The national rescue operations were followed by major swap transactions between the Federal Reserve of the US and a number of other central banks of industrialized economies in order to provide sufficient liquidity in response to a steady demand for US dollars. These swaps were also extended to central banks of some emerging economies, to support their currencies in the face of continued pressures in the foreign exchange markets.

Subsequently, core European countries, after a hesitant beginning, came to the rescue of EU economies that were in serious trouble, particularly over-indebted Greece, Portugal, Ireland, Spain, and Italy. Specifically, they announced the prospective mobilization of Euro 750 billion, or nearly US$1 trillion, two thirds from the European Union itself and the rest from the IMF. This was the first time in thirty years that the IMF has provided support to the western economies of Europe, although it had already done so to other countries in the region. The first step was a Euro 110 billion loan to Greece but lending was extended to Ireland and Portugal, with possible additional loans to Cyprus, Slovenia, and Spain. With such high financing requirements, access to the International Financial Institutions was imperative. The IMF showed great lending flexibility and mobilized significant resources.[9]

The creation of the G-20 Summits was another noteworthy development. Up to 2008, many decisions had been taken at the level of the G-7/G-8, the group formed by the largest advanced economies, and Russia. The G-20 includes the G-8 and the largest emerging economies, such as China, India, Korea, South Africa, and in Latin America, Brazil, Mexico, and Argentina. This forum reflects better the growing importance of the emerging world and may hopefully also open the door to a more representative governance system at the International Financial Institutions (IFIs).

Conditions improved in 2010, with GDP growth recovering from the serious recession of 2008–09. Unfortunately, new tensions emerged in Europe in light of the protracted nature of the fiscal imbalances in some of the countries. Furthermore, the recovery in the US remained weak, as fiscal policy issues were not addressed and public debt continued to mount. Through 2011, growth was moderate. While growth rose in the advanced economies through the third quarter, activity took a sharp turn for the worse during the fourth quarter, mainly in the euro area. The future of the Economic and Monetary Union (EMU) became clouded by uncertainty, as the sovereign debt crisis caused sharp increases in key government bond yields; this was compounded by weaknesses in the financial sector, in turn tightly linked to the performance of the sovereign debt.

Declining confidence and escalating financial stress were major factors in a contraction of the euro area economy, while natural disasters affected Japan and South East Asia. In the United States, by contrast, activity accelerated in 2011, as consumption and investment strengthened. Activity softened in emerging and developing economies. In emerging Asia and in Latin America, production slowed noticeably, due to cyclical factors, including recent policy tightening. Although the recovery was always expected to be weak and vulnerable because of the legacy of the financial crisis, other factors have played important roles. In the euro area, these include design flaws; in the United States, an

9 There have already been several loans with such conditions, including to Mexico, Colombia, and Poland.

acrimonious debate on fiscal consolidation, which undermined confidence within financial markets.

In 2012, conditions have deteriorated further, as the European crisis deepened and activity slowed down in the US. This has had adverse consequences on aggregate demand, with a negative impact on economic activity in the emerging world. As discussed in the IMF's revision of the World Economic Outlook in July 2012, after suffering a major setback in the second half of 2011, global prospects strengthened only to disappoint more recently, as evidenced by the slowdown in the US. Moreover, downside risks remain high.

The Transmission of the Crisis

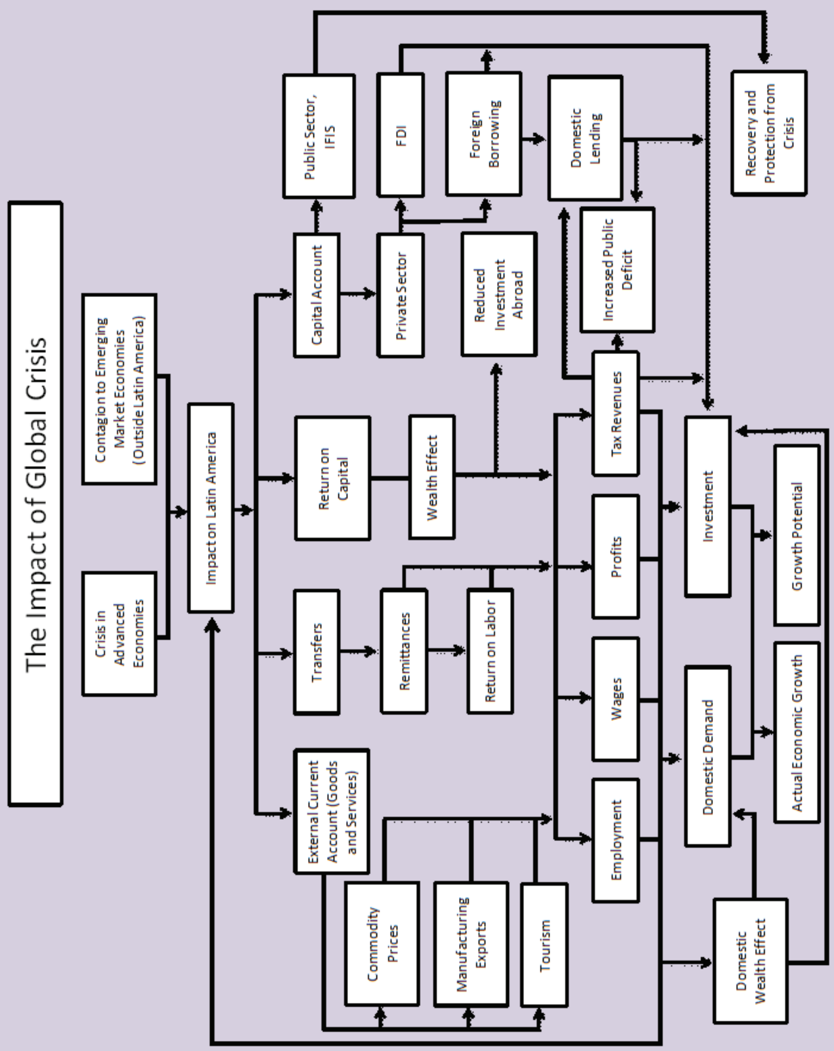
The financial crisis erupted in August 2007 after the collapse of the U.S mortgage market and entered a tumultuous new phase in 2008 following the collapse of Lehman. These developments shook confidence in global financial institutions and markets, and triggered a cascading series of bankruptcies, forced mergers, and public interventions in the United States and Western Europe, which eventually resulted in a drastic reshaping of the financial landscape. When the real estate bubble burst in the US and Europe, investors moved to commodities, where experts expected a continuous increase in prices. The commodity bubble peaked in mid-2008, with a subsequent collapse in 2009. In particular, losses were large in the case of metals and oil. A subsequent strong recovery has reversed these trends.

The transmission of the crisis from the U.S. and Europe to the rest of the world came through a number of channels. The financial institutions in most emerging market economies had not engaged in the kind of practices seen in the major industrial countries. Balance sheets were typically not exposed to toxic assets. Derivatives were employed much less frequently and were generally limited to the more traditional instruments employed to hedge against currency and other risks associated with trade. Financial institutions in the emerging economies either shied away from exotic instruments, or were prevented by regulation from holding or trading such instruments. The impact of the crisis on emerging economies was felt through: (i) the external current account with a large drop in exports and export prices as well as a decline in remittances; (ii) the withdrawal of funds by financial institutions from their subsidiaries; and (iii) a sharp decline in capital inflows. These factors can be seen in a stylized form on the basis of Figure 3, and quantified subsequently.

International Trade

The impact of the crisis on economic activity—in the first instance, in the United States and Europe, and subsequently in Japan—was reflected in a decline in the demand for exports of the emerging market countries that had become the largest exporters to the industrial world. Quite rapidly, the decline in demand for exports affected other emerging economies, i.e., those whose exports consisted of raw and intermediate goods shipped to emerging market countries, particularly China, which had become a key provider of final manufactured goods in the increasingly complex supply chains that came to populate world trade. This fall in exports—at a virtually unprecedented extent and speed—created a feedback whereby the initial reduction in trade weakened the domestic economies of the emerging market countries. This was negatively compounded by the freeze of the domestic financial sectors associated with the uncertainty created by the collapse of the financial sectors in the advanced countries

Figure
3 **World Trade Projections (percentage change, annual)**



Source: Claudio M. Loser.

and the rapid deterioration of the quality of domestic credit portfolios.

During the last quarter century, the volume of world trade had grown at an average rate of 6 percent, or about double the rate of world output. Asian exports had grown at a rate of 10 percent a year and those of Latin America and the Caribbean by some 7 percent, with a marked transformational impact. NICs, which had become highly integrated with the rest of the world, recorded an average ratio of exports to GDP of 71 percent during 2002–07. Developing Asia recorded a ratio of 55 percent, tempered by lower but growing ratios for China (31 percent) and India (12 percent), which were dominated by domestic developments. In Asia, the increased ratio of exports to GDP was due to higher volumes of trade, helped in part by some real depreciation of national currencies. Latin America, which became much more open in the 1990s, registered a stable ratio of exports to GDP of 21 percent, notwithstanding the impact of a strong real appreciation of the currencies, as export volumes increased. World trade volumes contracted by 10.5 percent in 2009 after a peak growth of 9.3 percent in 2006 (Table 3). The impact differed around the world. Latin America experienced declines of 9.7 percent in exports and of 16.8 percent in imports in 2009. The subsequent recovery, aided by continued strong growth in emerging economies and to a lesser degree in the US, has reversed this decline.

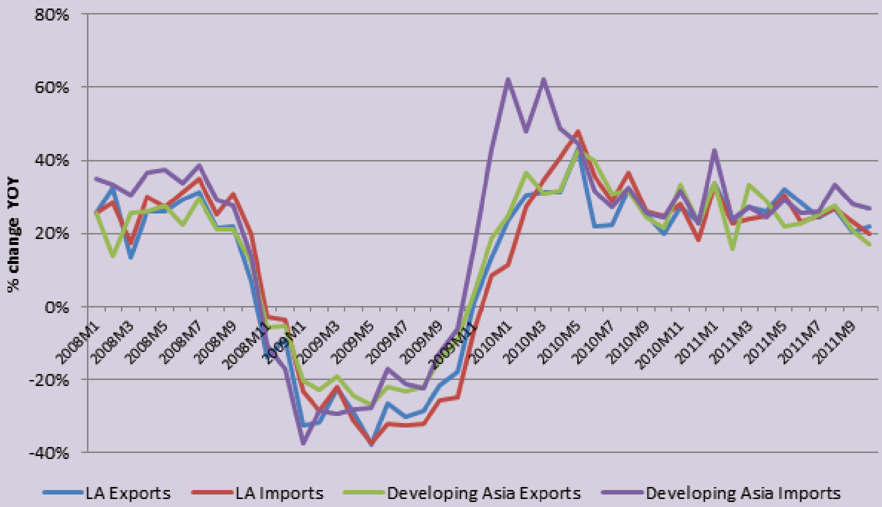
These trends are confirmed by the movements in trade on a monthly 12-months basis, as seen in Figure 4. Because of the composition of exports, half of which are commodities, Latin America was particularly hit by declining prices (Figure 5), thus magnifying the impact of lower export volumes. The slowdown in the US, Europe and the region, which are the main trading areas for Latin America (Figure 6), explain the contraction in exports. The losses in income due to terms of trade effects are also significant, with considerably smaller effects in Asia because of lower net balance in raw materials and

Table 3 **World Trade (% annual change)**

	2006	2007	2008	2009	2010	2011	2012	2013
World trade volume	9.3	7.9	2.9	-10.5	12.9	5.8	4.0	5.6
Imports								
Advanced Economies	7.8	5.2	0.5	-12.2	11.5	4.3	1.8	4.1
Emerging and Developing Economies	11.9	14.9	9.0	-8.1	15.3	8.8	8.4	8.1
Latin America and Caribbean	13.0	13.7	8.7	-16.8	23.9	10.6	6.7	8.0
Exports								
Advanced Economies	8.9	6.8	2.0	-11.5	12.2	5.3	2.3	4.7
Emerging and Developing Economies	11.5	10.5	4.7	-7.7	14.7	6.7	6.6	7.2
Latin America and Caribbean	6.6	4.8	0.8	-9.7	11.6	5.7	6.4	8.4

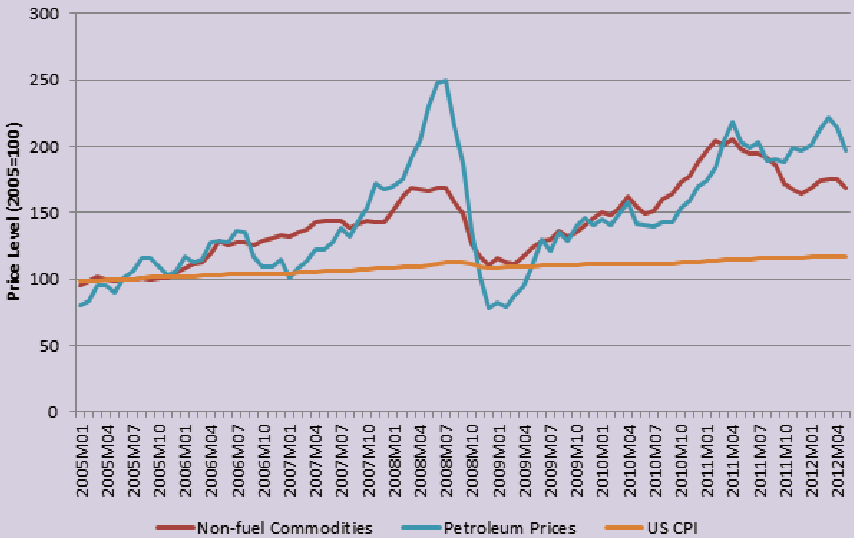
Source: International Monetary Fund, World Economic Outlook Database, April 2012

Figure 4 | **Trade Growth in Latin America and Developing Asia (12-month change)**



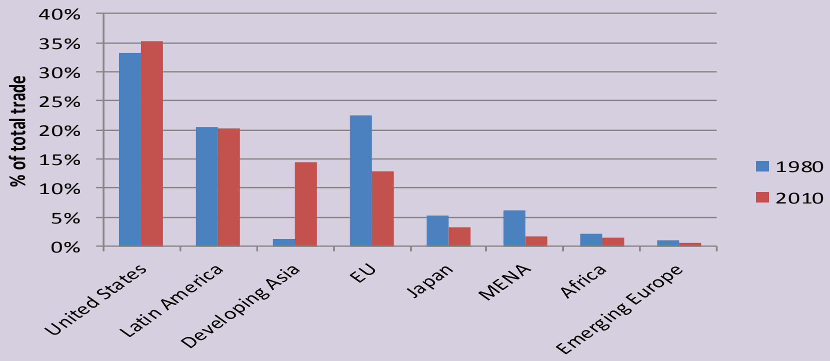
Source: International Monetary Fund, World Economic Outlook Database, April 2012

Figure 5 | **Evolution of commodity prices (2005=100)**



Source: IMF: Commodity Prices; and own estimates

Figure 6 **Latin American Trade Share (% of total)**



Source: IMF, Directions of Trade, 2012 and Author's estimates

intermediate goods, but with considerable differences among countries.

It would be easy to suggest that the countries that have been most open to international trade may have been subject to the greatest shock on account of reduced world demand, thus justifying protectionism. However, this should be viewed in a broader light. Countries that opened more vigorously to trade grew the fastest, and benefitted more from global prosperity. They may experience a significant short-term loss, as is being observed in Taiwan and Korea, but they recovered quickly as well. More significantly, the more open traders are actually benefitting from a more flexible and diversified productive structure that allows them to adjust more efficiently and faster than most closed economies.

Remittances

Remittances over the last fifteen years have become a major channel of prosperity. The merits of increased mobility of large numbers of workers to better-paying jobs in prosperous destinations (especially the US, Europe, and the Middle East) may be subject to debate. However, the impact of the consequent remittances to their home countries have helped increase prosperity and reduce poverty, particularly in Asia and Latin America, with India, Mexico and the Philippines being the largest recipients of workers' remittances. Remittances to emerging markets amounted to some US$443 billion in 2008 (some 3 percent of GDP of the receiving countries), with nearly US$157 billion to Asia and US$64 billion to Latin America (Table 4). These flows were steadily growing, and were a countercyclical force in the receiving countries.[10] However, they are sensitive to economic conditions in the countries of employment, and as a consequence, remittances started to fall in late-2008 for the first time in a quarter century, and to an estimated decline of nearly US$30 billion in 2009. Subsequently, remittances recovered, partly in response to better economic conditions. However, a new trend has affected these flows, as many emigrants of the region have been going back to their countries, particularly from the US and Europe, because of reduced opportunities in specific areas

10 Claudio Loser, "The Macro-Economic Impact of Remittances in Latin America-Dutch Disease or Latin Cure?" G-24 Technical Papers, 2006 (G-24 website, Technical Meetings).

Table 4 **Workers Remittances (billions US$)**

	2008	2009	2010	2011
World	457	429	453	501
Emerging Asia	85	86	95	107
Emerging South Asia	72	75	82	97
Latin America	64	57	57	62

Source: Migration and Development Brief 12, World Bank

like construction and some services. Furthermore, the US tightened its border controls and many migrants were deported, thus slowing down the inflow of workers, with potentially significant effects in the years to come. The return of workers from abroad to their countries of origin has put additional pressure on the labor markets as those workers seek employment in their own economies.

Tourism

Tourism is another area affected by the global crisis. Receipts from tourists are a significant source of income, particularly for Mexico, Peru, Central America and the Caribbean, and some other countries in South America. Emerging economies, arguably the most dynamic segment of international tourism, show a strong recovery in 2010–12 (Table 5).

Developments in Employment[11]

In 2009, more than a million jobs were lost in the Latin America according to ECLAC. The economies in the region have expanded subsequently, and unemployment rates fell on a sustained basis ever since, although prospects for 2012 are surrounded by considerable uncertainty (Figure 7). In the context of a renewed slowdown in activity, further job losses may take place together with growth in the informal sector. In any event, there has been an increase of 0.6 percentage points in the level of employment from 2007 to 2011. This is the second largest

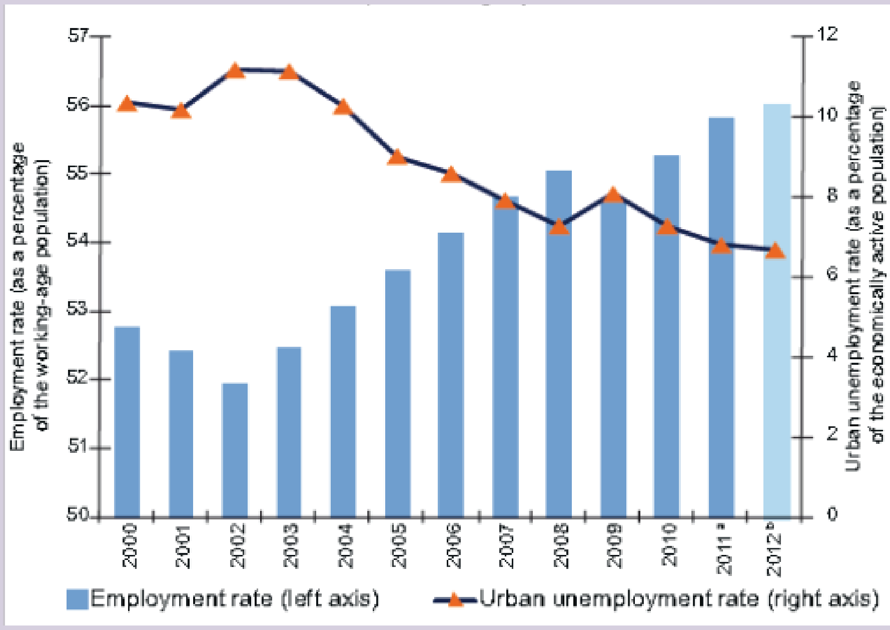
Table 5 **International Tourist Arrivals (millions)**

	2000	2005	2009	2010	2012
World	674	799	883	940	983
Europe	385	440.7	461.7	474.8	504
Asia and Pacific	110.1	153.6	181.1	204.4	217
Americas	128.2	133.3	141.7	150.7	156.6
South America	15.3	18.3	21.4	23.6	25.8

Source: UN World Tourism Organization, World Tourism Barometer April 2012

11 Crisis in the labor Market ECLAC/ILO, June 2009.

Figure 7 **Latin America and the Caribbean: Rates of Employment and Open Unemployment, 2000-2012 (%)**



Source: Economic Comission for Latin America and the Caribbean (ECLAC), on the basis of official figures

increase—after Central and South-Eastern Europe—of all regions during the crisis period.

As discussed by the ILO,[12] however, the employment growth masks two important considerations. First, job quality remains of concern. The share of informal employment remains high in Latin America—close to 50 percent on average—and has increased in over one-third of the countries for which data are available, even though the region as a whole has seen a slight decrease in informal employment. Second, the crisis has led to an increase in income inequalities in one third of the countries. Moreover, economic growth in the region has slowed in 2011–12. As the prospects for growth weaken, and capital flows remain volatile, this may result in slower employment growth in the near future, particularly as investment rates remain unchanged.

Financial and Credit Markets

The impact that the global financial crisis has had in the financial markets can be seen from different points of view. Fundamentally, these include the valuation of companies, particularly those quoted in stock markets; the investments by some economic agents in toxic assets; the general conditions of the banking system in the region; and problems of external financing.

The stock markets of the emerging economies experienced a sharp fall in 2008, exceeding that of the stock markets in the advanced countries. The fall was particularly strong from mid-2008, in contrast with what happened in the US and Europe, where the reduction began in the middle of 2007. Reflecting

12 International Institute for Labor Studies-World of Work 2012: Better jobs for a better economy—April 2012

the wide-ranging effect of the global financial crisis, the S&P 500 index of the United States fell by 36 percent from June to end-2008, the Japan Nikkei index fell by 37 percent, while the stock market indices in Brazil and Mexico fell by 49 percent and 29 percent respectively, and in Korea, India, and China by 36, 41, and 48 percent, respectively (Table 6). Since the end of 2009, there was a significant recovery, as seen in the table, but again in 2011–12 the improvements have been eroded, on account of a weakened world economic outlook.

Initially, it was thought that because of the characteristics of the developing financial markets, there would be no significant presence of “toxic” financial assets in emerging economies. Nevertheless, in some of them, including Korea, India, China, Brazil and Mexico, some companies were invested in derivatives, particularly to hedge against foreign exchange risk, and, to a lesser extent, commodities. The fall in international prices and the depreciation of local currencies had an important impact on the finances of these companies and therefore, their share values suffered. This, together with uncertainty regarding the scope and extent of these derivatives, generated strong temporary pressures on the exchange markets.

There have been significant improvements in the financial conditions from the trough in 2008,

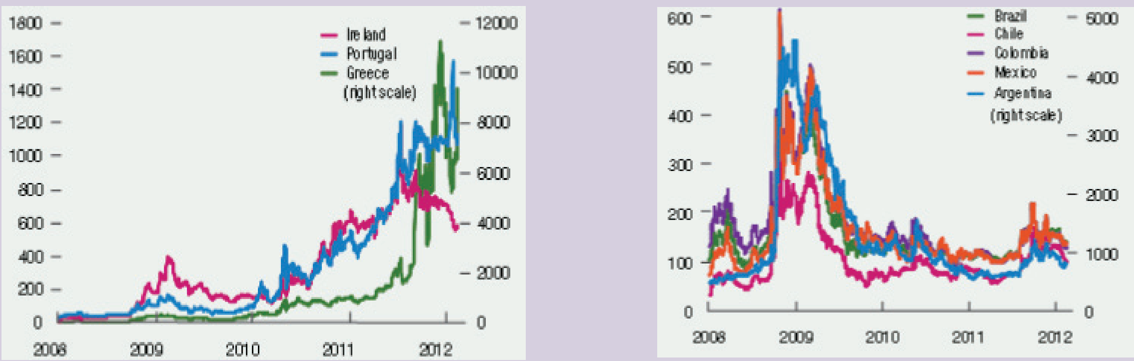
Table 6 **Selected Countries—Stock Market and Exchange Rate Changes**

	Stock Market Changes					Exchange Rate Changes (relative to USD)				
	2008	2009	2010	2011	First half of 2012	2008	2009	2010	2011	First half of 2012
Argentina	-48.9%	103.6%	48.8%	-23.3%	-0.5%	-9.5%	-8.9%	-4.5%	-7.2%	-4.7%
Brazil	-41.2%	82.7%	1.0%	-18.1%	-4.2%	-29.8%	25.2%	1.4%	-10.0%	-9.9%
Chile	-19.6%	46.9%	38.2%	-12.4%	4.7%	-28.2%	20.3%	6.7%	-5.7%	2.3%
Colombia	-29.3%	53.5%	33.6%	-18.3%	5.9%	-11.4%	10.1%	3.6%	-2.0%	8.1%
Mexico	-24.2%	43.5%	20.8%	-2.7%	8.8%	-25.3%	5.9%	3.8%	-11.4%	3.5%
Latin America	-34.6%	68.3%	16.1%	-13.4%	0.7%	-25.0%	14.4%	2.0%	-9.4%	-3.2%
China	-65.4%	80.0%	-14.3%	-21.7%	1.2%	6.0%	20.0%	2.6%	3.8%	0.9%
Hong Kong	-46.9%	42.9%	7.1%	-18.8%	4.8%	4.3%	-10.0%	-0.3%	-0.1%	0.2%
India	-57.1%	90.2%	14.1%	-27.2%	15.9%	-23.8%	6.0%	0.4%	-15.5%	-2.7%
South Korea	-40.7%	49.7%	21.9%	-11.0%	1.5%	-34.6%	8.7%	-1.2%	-2.7%	0.2%
Japan	-30.5%	5.6%	-1.0%	-18.9%	5.7%	20.4%	-2.0%	11.0%	5.7%	-3.1%
Euro Area	-49.6%	23.8%	1.8%	-15.3%	-0.7%	-10.5%	-2.0%	-8.6%	-1.0%	-3.8%
USA (NYSE)	-38.6%	24.8%	10.8%	-6.1%	4.3%	0.0%	0.0%	0.0%	0.0%	0.0%

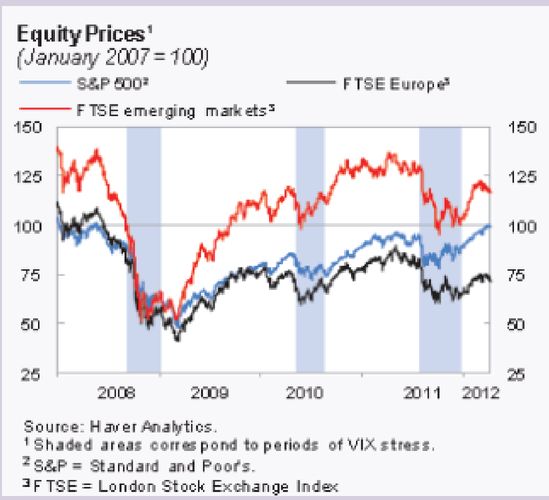
Source: World Federation of Exchanges, OANDA. Official exchange rates as reflected in Figure 8.[13] Nevertheless, financial markets have remained volatile, and the perceived risk of investments resulted in a sharp increase in risk premiums, with particularly marked increases for Argentina, Ecuador and Venezuela. In the case of these countries, the risks caused by the fall in international oil prices were accompanied by macroeconomic and structural policies that can be regarded

Figure 8 | Emerging Market Spreads and Comparison with Selected Markets

Collaterized Debt Security Spreads for Selected Latin American Countries and European Countries



Equity Markets and Interest Rate Spreads



Source: IMF, World Economic Outlook, April 2012, and Regional Economic Outlook, Western Hemisphere, May 2012 as weak or deficient. In the case of Argentina, this was compounded by the impact of the recent expropriation and nationalization of the Oil Company YPF, and increasing trade and exchange controls. In most cases, risk premiums have declined, although they have not yet achieved the levels prior to mid-2008. Interest spreads for Latin American corporations had increased at a much slower pace than for those in Europe, which had been hit hard by the crisis.

Data on capital flows by IIF show a dramatic picture. Private flows to emerging market countries (net of equity investment abroad) declined from US$1252 billion in 2007 to about one half of that level in 2008–09, but rose sharply, to more than US$1 trillion in 2010–11; a decline of some US$100 billion is estimated for 2012 reflecting weakened risk appetite of private creditors (Table 7). Within these totals, Latin America saw a decline in net private flows from US$229 billion in 2007 to US$130 billion in 2008, with a sharp recovery through 2011, reaching flows that exceed those of 2007. However, as is generally the case, the lower private flows were only offset in small part by the increase in official flows during the period, mainly on account of the greater availability of financing from the IMF.

Foreign Direct Investment

Foreign Direct Investment (FDI) also suffered in the short run. FDI stocks and flows grew at a very fast rate in recent years, reflecting both the emergence of new countries as origins and destinations of capital flows, and rapidly evolving capital markets. This allowed for a sharp increase in available capital within the private sector, and resulted in a decline in lending by International Financial Institutions. Most interesting was the change in the composition of these flows. While total FDI directed to developed countries retained the lion's share of the total inflows (70 percent of the total), both Asia and Latin America became increasingly important, even with some volatility in the case of Latin America (Table 8).[14] Flows in the next years will remain low, as credit and financial market conditions remain weak but should come up from the crisis levels of 2009.

Commercial Banks

Commercial banks in Latin America did not invest to any significant degree in "toxic" financial instruments, but were hit by the sharp contraction in external credit. These institutions, not being strongly exposed to external risks, and focusing mainly on domestic markets, are not incurring risks similar to financial institutions in the advanced countries. In Asia, where the banking system is much larger than in Latin America, banks have tended to be more invested in troubled assets, with the possible exception of India among the larger countries. Latin America has been helped by the relatively small size of the region's national financial systems and the strong supervision and prudential regulations that has followed the crises of the last ten to fifteen years.[15] [16] Thus, the risks have tended to be concentrated in possible disruptions in the traditional flows

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14 UNCTAD, World Investment Report, 2006–2012. Also see: Loser, Claudio, Cross-Border Trade and Investment among Emerging Economies: Lessons from differing experiences in Africa, Asia and Latin America", Emerging Market Forum 2008.

15 The index of Financial development and Stability, developed by the Centennial Group, and presented in Emerging markets in October of 2008 show that the countries in Latin America have developed considerable institutional strength, with index levels that exceed what could be expected in light of their levels of income. In turn the development indices (reflecting the depth and structure) are below what is expected in light of the region's per capita income. This is the opposite of what was observed in the case of Asian countries, where the development indicators tend to run ahead of their relative institutional strength, with the exception of the NICs.

16 "Financial Markets in Latin America, Claudio Loser, in "Growth and Development in Emerging market Economies", Harinder Kohli, Ed. Sage Publications, 2008.

Table 7 **Emerging Market Economies' External Financing**

	2007	2008	2009	2010	2011	2012
Emerging Economies						
Private Flows, net	1252.2	588.2	530.8	1088	1030	912
Equity Investment, net	601.9	420.8	465.8	607	545	560
Private Creditors, net	650.2	167.5	65.0	481	485	353
Official	42.9	61.4	62.4	69	63	46
Resident Lending/Other	-482.6	-535.4	-211.6	-607	-715	-663
Reserves (Increase -)	-1056.7	-477.2	-549.8	-802	-669	-630
Latin America						
Private Flows, net	228.9	129.6	156.6	265.6	253.7	252.9
Equity Investment, net	134.3	89.4	114.9	138.1	133.5	145.4
Private Creditors, net	94.5	40.3	41.7	127.5	120.2	107.4
Official	6.3	14.0	23.7	24	29.3	21.2
Resident Lending/Other, net	-79.4	-68.8	-61.8	-168	-137.2	-120.9
Reserves (Increase -)	-127.8	-43.5	-42.4	-80.2	-98.9	-78.1
Developing Asia						
Private Flows, net	422.2	107.4	282.9	532.1	533.9	452.1
Equity Investment, net	240.7	158.7	231.0	330.1	310.7	287.7
Private Creditors, net	181.5	-51.3	51.9	202	223.2	164.4
Official	28.6	22.5	10.4	18.2	17.7	16.5
Resident Lending/Other, net	-148.7	-122.0	-65.6	-232.5	-267.6	-291.7
Reserves (Increase -)	-587.8	-347.8	-518.1	-595.7	-443.9	-398.4

Source: IIF, Capital Flows to Emerging Market Economies, October 2010; Septemeber 2011, and June 2012

related to international trade and foreign investment; and the contraction in international economic activity.

A separate issue is that the banking system is highly concentrated, and has a large presence of foreign banks. In the case of Mexico, the latter may still create pressures on the system, to the extent that the US, Spanish and other foreign-owned banks may withdraw lines of credit from Mexico to preserve the health of their home operations, as detected in a 2009 IMF study, even in the presence of intervention of Central Banks to offset these outflows.[17]

Cross Border Flows and the Impact of the Crisis

With significant levels of assets abroad, either in the form of investments by companies or in the hands of individuals that have taken money out in response to poor domestic policies, the international crisis has had an additional impact on emerging

17 IMF, World Economic Outlook, Chapter 4, April 2009.

Table 8 **Foreign Direct Investment, Recipient Regions Flows and Stocks (billions US$)**

	Flows						
	1980	1990	2000	2006	2007	2009	2010
World	55.3	201.6	1411.4	1970.4	1185	1185	1243.7
Developed economies	47.6	165.6	1146.2	1306.8	602.8	602.8	601.9
Developing economies	7.7	35.9	256.1	573	510.6	510.6	573.6
of which:							
Africa	0.4	39.8	9.7	63.1	60.1	60.1	55
Latin America	6.5	35.1	97.8	126.1	81	81	115.8
South, East and South-East Asia	3.9	49.8	144.8	284.1	241.5	241.5	299.7
Southeast Europe and CIS	0	0	9	91.1	71.6	71.6	68.2
	Stocks						
World	551.2	2081.3	7445.6				19140.6
Developed Economies	410.9	1563.9	5653.2				12501.6
Share in total	74.5	75.1	75.9				65.3
Developing economies	140.4	517.3	1731.6				5951.2
Share in total	25.5	24.9	23.3				*31.1*
of which:							
Latin America	35.1	101.5	444.3				1376.2
Share in total	6.4	4.9	6.0				7.2
South, East and South-East Asia	49.8	311.7	1012.2				3087.8
Share in total	9.0	15.0	13.6				16.1
World FDI stock (real terms)1/	5.1	9.4	23.1				30.3

1/ Adjusted by world export prices
2/ 2007 values for Asia are estimates
Source: World Investment Report 2011, UNCTAD

economies due to the reductions in returns on those investments abroad, and financing difficulties in connection with these investments. This problem did not exist when the main emerging economies were fundamentally on the receiving end and were not capital exporters as is the case at present.

Table 9 provides data for the net external financial position in Asia and Latin America through 2010. The net position tends to be small. Latin America has a net (negative) position, equivalent of 12 percent of total assets. Even under these circumstances, the financial impact of external events can be considerable, due to the differential behavior of gross assets and liabilities.

Medium Term Prospects

While dramatic and painful, the recent deterioration of global economic performance follows a sustained expansion built on the increasing integration of emerging and developing economies into the global economy that is likely to persist and grow. Over the last quarter century, trade, remittances, and capital flows to and among emerging regions have risen significantly. Without question, their economic and trade growth have constituted the most dynamic aspect of globalization in recent years.

The Great Recession only slowed the process, as evidenced by the subsequent strong recovery despite the slowdown of late-2011 and the first half of 2012. The mechanisms of recovery have been as complex as those of crisis transmission (Figure 9). The sources of recovery can be divided into exogenous forces, domestic efforts, and sources of financing, in particular from regional and international financial organizations where CAF would play a major role. The external current account of Latin America deteriorated by one percent of GDP between 2007 and 2008, and recorded a deficit for the first time since 2002. In 2009, the deficit declined somewhat because of much lower imports, but has widened significantly since then, and the deficit may reach 2 percent of GDP in 2012 (Figure 10). Even under these conditions, after a sharp deterioration in the public finances in 2009, the fiscal position has improved by some 1.5 percent of GDP, as terms of trade strengthened. No further improvements from this source are

Table 9 **Net Investment Positions**

	2002	2007	2008	2009	2010
Advanced Economies					
Net Asset Position (US$ billions)	-1,115	-1,176	-1,876	-547	300
as % of total assets	-1.2%	-0.6%	-1.0%	-0.3%	0.1%
Total international assets	33,845	90,053	86,916	88,929	94,672
as % of total assets	35.9%	46.4%	48.5%	43.3%	44.5%
Developing Asia					
Net Asset Position (US$ billions)	-304	784	1160	1100	1150
as % of total assets	-3.6%	2.6%	4.8%	5.1%	4.4%
Total international assets	307	3,342	3,866	4,530	5,372
as % of total assets	-33.8%	-14.0%	-10.9%	-13.2%	-12.2%
Latin America					
Net Asset Position (US$ billions)	-584	-927	-650	-965	-1075
as % of total assets	-3.6%	-14.0%	-10.9%	-13.2%	12.2%
Total international assets	593	1,399	1,513	1,688	1,973
as % of total assets	34.4%	21.1%	25.4%	23.0%	22.4%

Source: IMF- Int. Financial Statistics and own estimates expected, as the gain in terms of trade may have come to an end in 2012.

In the case of Asia, the impact of lower export prices is minimal because of the trade composition of developing and emerging Asia, although there is a significant divergence among countries. The initial impact of the recession on exports was significant, but this was offset by the sharp decline in the volume of imports and an improvement in the terms of trade. Since 2009, however, the terms of trade have tended to deteriorate, and even with a strong performance of exports, the current account surplus has narrowed, even as the fiscal position has tended to improve markedly.

Figure 9 **Recovery and Growth Support in Latin America**

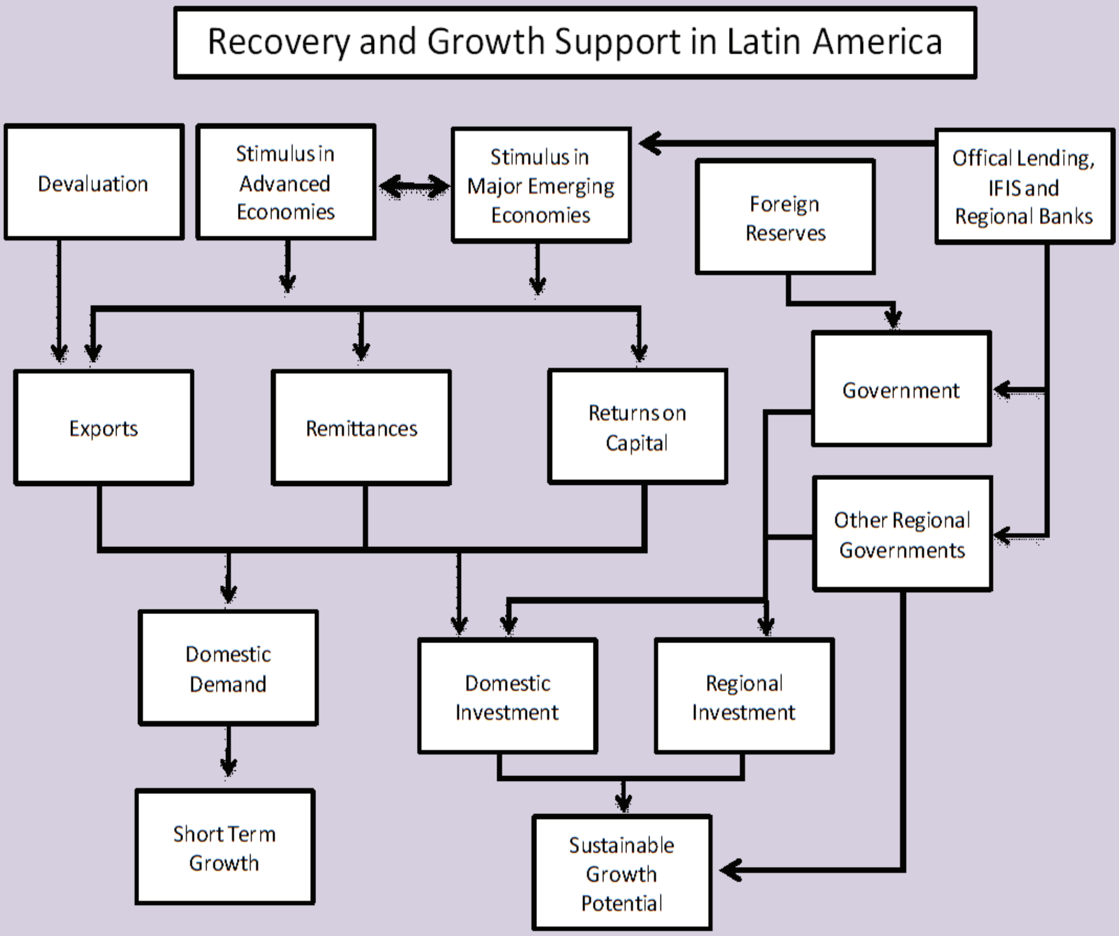
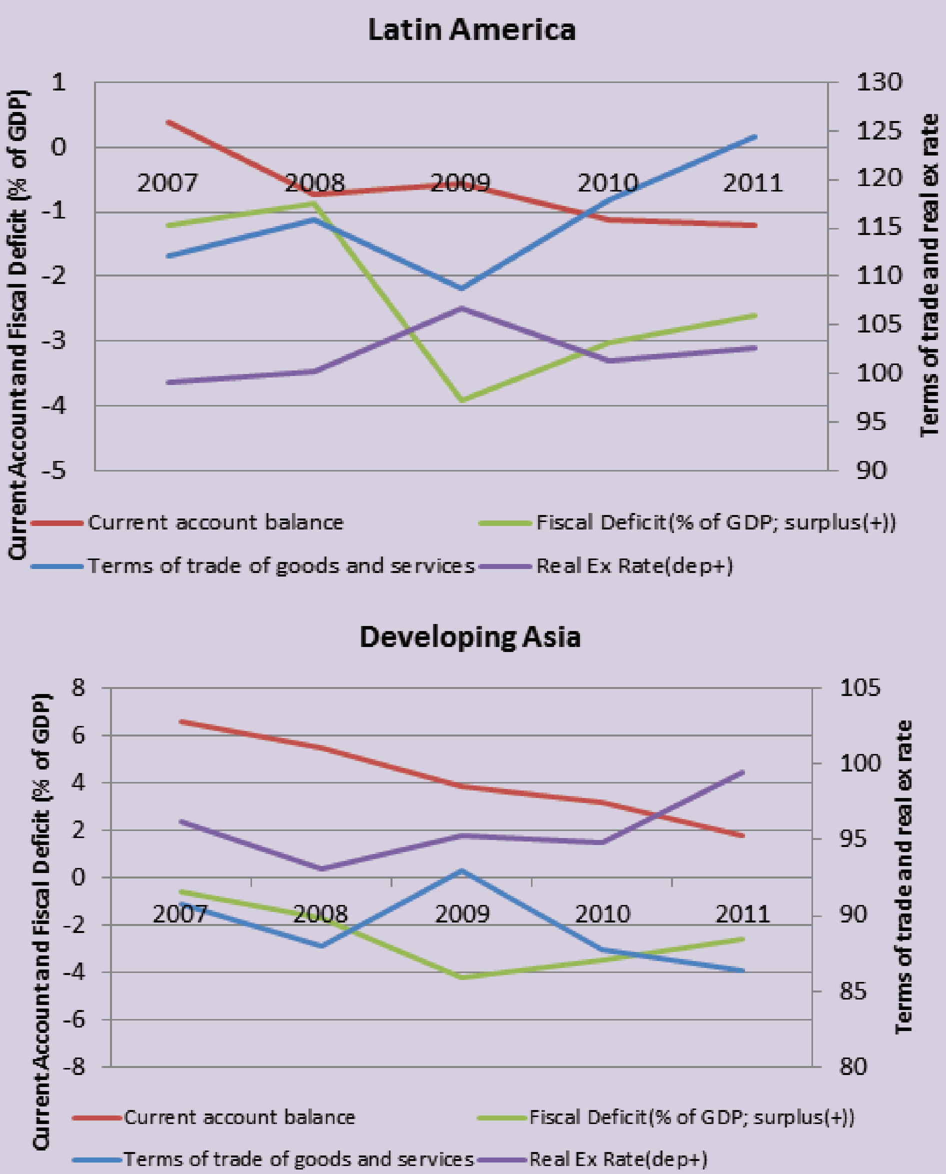


Figure 10 **External Current Account, Fiscal Balance, Exchange Rates and Terms of Trade**



Source: International Monetary Fund, World Economic Outlook Database, April 2010, and International Monetary Fund, International Financial Statistics

External Prospects[18]

The recovery from the Great Recession has been uneven: very weak in many advanced economies but strong in many emerging and developing economies. Initially, the trajectory of the recovery in advanced economies displayed some similarities with the sluggish recovery following the much shallower 1991 global recession. More recently, however, this recovery has weakened, raising serious concern about the pace and durability of the global recovery.

Global growth is projected to drop in 2012 because of the weakening in activity that started in 2011, mainly on account of the deteriorating sovereign debt and banking sector developments in the euro area. For most economies, there is an expectation of recovery in 2013, but subject to risks, particularly in the euro area. Even so, policy has played an important role in lowering systemic risk, but this needs to continue. The European Central Bank's three-year refinancing operations, a strong European firewall, and ambitious fiscal adjustment programs, helped stabilize conditions but only in a tentative fashion. A number of advanced economies have made good progress in designing and implementing strong medium-term fiscal consolidation programs. At the same time, emerging and developing economies continue to benefit from past policy improvements. With no further action, however, downside risks remain. In particular, the concerns remain about a possible generalized flight from risk in some European countries. There are tensions between the need to sustain growth and reduce fiscal pressures, and the concerns about mounting levels of debt are taking increasing importance in the policy debate, although interest levels remain at record lows.

Policies should be strengthened to solidify the weak recovery and contain the many downside risks. In the short term, this will require more efforts to address the euro area crisis, cautious fiscal policies in response to weaker activity, a continuation of countercyclical monetary policies, and ensuring liquidity in the financial sector. However, there is an urgent need for strong, sustainable fiscal consolidation paths over the medium term.

Looking further ahead, the challenge is to improve the weak medium-term growth outlook for the major advanced economies. The most important priorities remain fundamental reform of the financial sector; more progress with fiscal consolidation, including an ambitious reform of entitlement programs; and structural reforms to boost potential output, particularly in the labor markets.

Many emerging and developing economies continue to reap the benefits of strong macroeconomic and structural policies, but domestic vulnerabilities have been gradually building. Many of these economies have had a good run over the past decade, supported by rapid credit growth and/or high commodity prices. Financial deepening may explain this trend. However, liquidity injections cannot continue to expand at their present pace without raising serious concerns about future inflation and the quality of bank lending. Moreover, commodity prices have decelerated. This means that fiscal and other policies may well have to adapt to lower demand.

For economies that have largely normalized macroeconomic policies, the near-term focus should be on responding to lower external demand from advanced economies. At the same time, these economies need to cope with emerging adverse spillovers and volatile capital flows, while strengthening prudential policies.

The recovery is fragile. Flexible exchange rates have helped mitigate the effect of a changing economic reality more focused on Asia, and with greater

18 This section closely follows the World Economic Outlook, IMF, April 2010.

risks in some advanced areas of the world. But the dangers of recurring imbalances remain in place, and policies will need to be exceedingly cautious.

Financial Wealth: An Estimate of the Buildup and Destruction of Wealth 2002–2009

Financial Wealth over the last decade became the clearest sign of economic advancement and well-being. The collapse of financial markets that became evident in 2008 has been a cataclysmic event. Conditions under which financial markets had operated for many decades are unlikely to be replicated in the next few years. The enormous generation of wealth witnessed in previous years may come back, but in the context of a much more controlled financial system, and subject to stricter rules. Even though a recovery has already taken place, it has been at best modest, and with relapses, as was witnessed in 2010 and 2011. Furthermore, the road ahead is difficult. The loss of financial wealth that occurred in 2008 has been enormous, and the consequences for the economies of the world are commensurate. The loss of capital value of financial assets world-wide reached the equivalent of about one year of world GDP in 2008. The discussion below provides an estimation of the changes in financial wealth since 2002, and the possible causes for the changes. The study is based on a more detailed study prepared in 2010 and updated to 2011.[19]

Available data shows that the value of financial assets more than doubled between 2002 and 2007 (125 percent), at a time that GDP grew by 70 percent, entailing an increase in the ratio of financial assets to GDP of 330 percent, to 440 percent by end-2007 (Table 10). During the period under review, the ratio of financial assets to GDP in Advanced Economies rose by 35 percent. In Developing Asia, the ratio rose by 60 percent, and in Latin America it was an impressive 75 percent.

The pace of financial asset accumulation came to an abrupt halt in 2008, when the ratio to GDP declined by 18 percent, in response to the crisis, and 10 percent in nominal terms, notwithstanding the massive injection of liquidity by central banks and governments alike. When only the market-related changes are included, the loss of financial wealth at a world-wide level may have amounted to an astounding US$46 trillion (Figure 11) and a likely additional loss of US$10 trillion before a trough was reached in early 2009, as discussed below. Moreover, while assets have increased since then and have reached the levels observed before the crisis, the increases due to changes in market conditions in the subsequent three years, and most likely in the first half of 2012, have not been able to compensate the losses incurred during the Great Recession. Thus, to a significant extent, the observed increases in financial assets were the result of a massive injection of liquidity by central banks, and a process of deleveraging and increased savings by the private sector, after years of unsustainable borrowing and massive over-expansion in financial wealth. The exact implications for aggregate demand, including for investment, have not been quantified, but clearly explain the decline in GDP in 2009 and the modest pace of the recovery that the world has experienced subsequently. The rebuilding of private savings, the concerns of the private sector about the pace of the recovery, and the fears resulting from the increase in central bank liquidity and government debt have had a major effect on aggregate demand, only offset in part by

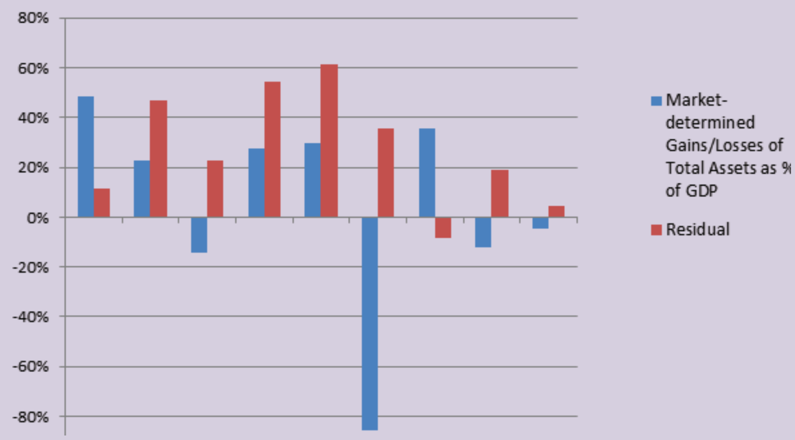
19 The basis for this paper are the calculations presented in the Global Financial Stability Report, of the International Monetary Fund, for the period 2002–07, with additional estimates specifically prepared for this paper for 2008. These do not include the complex set of financial derivatives like CDS (Credit Default Swaps) that further multiplied the size of the financial market.

Table 10 **Total Financial Assets (as percentage of GDP)**

Country/Region	2002	2003	2004	2005	2006	2007	2008	2009	2010
World	330.8	342.3	369.2	341.5	401.5	439.6	358.6	418.3	407.3
EU	418.4	405.4	457.8	433.6	541.7	580.7	488.5	580.8	570.5
United States	344.6	373	401.6	402.9	430.6	445	373.6	431.2	440.6
Japan	381.9	454.2	467.2	450.5	459.4	546.6	467.8	523.7	536.1
Emerging Asia	242.2	232.9	251.3	246.8	306.6	389	331.6	274.1	274.7
Emerging Latin America	105.2	129.1	144.1	148.5	155.1	182.3	141.6	183.7	179.6
Emerging Africa, Middle East, Europe	83.7	85.1	99.1	86	142.8	176.3	118.1	106.7	127.4

Source: IMF, Global Financial Stability Report, various issues, Centennial database, and own estimates

Figure 11 **Global Gains/Losses of Total Assets as % of GDP**



Source: IMF, Global Financial Stability Report, various issues, Centennial Group, database, and own estimates

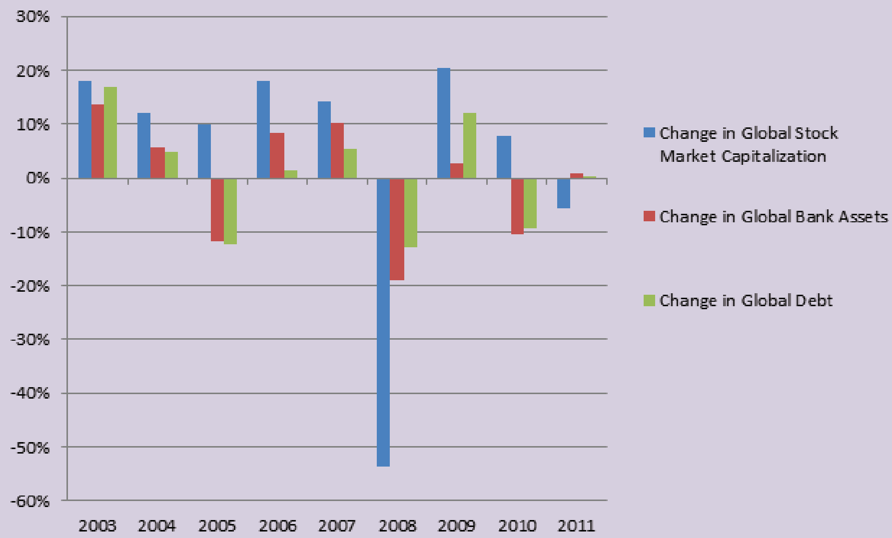
the direct effect of government expenditure and the direct effect of central bank credit expansion. On that basis, the recovery from the current traumatic events can be expected to take considerable time and cannot be expected to lead to the previous rapid but unsustainable path of growth, particularly experienced over the period 2003–07.

Figure 12 provides data on the main sources of explained market changes during the period under study. Clearly, during the period, the main source of change was the stock market, with more limited changes in the area of debt and bank assets. Only in 2003, at a time when financial markets were recovering, and in 2008, when financial markets collapsed, were other items affected in a significant way. What is noticeable, however, is that the sharp decline in bank assets observed in 2008 and 2009 was not reversed, particularly reflecting the difficulties in Europe, and to a lesser extent in the US and Japan.

The impact of the current crisis has been overwhelming in terms of the geographic coverage. All regions of the world suffered the consequences of the crisis, proving again that the decoupling theory that had been prevalent during earlier years was misplaced. Figure 13 shows the magnitude of the fall in 2008, with particularly large declines in the case of Developing Asia, Latin America, and the European Union. This is explained by a combination of the impact of the crisis on the stock market, the large financial system, and the effect of a depreciation of the currencies. In the case of Asia, it is mostly explained by the stock market and the losses in the banking system, while in Latin America, the losses occurred mainly in the stock market.

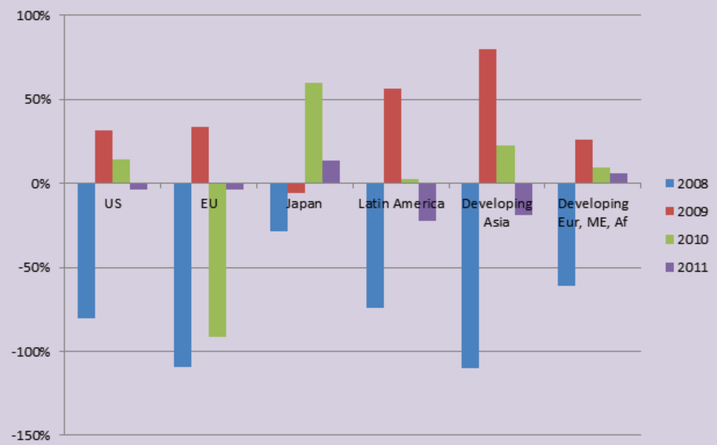
The dramatic nature of the collapse is outlined by the quarterly performance of financial wealth, as shown in Figure 14. Notwithstanding the large governmental packages that were offered in 2008, the financial losses continued unabated until early-2009, when commodity prices bottomed, and coordination among the main economies of the world, embodied in the G-20, started to be implemented. Among the various regions of the world, the one showing the lowest decline and best rebound relative to the end of 2006 was Latin America, helped by reasonable macro-policies after decades of mismanagement.

Figure 12 | **Market-determined Explanations of Global Assets Losses 2003-2011 (% of GDP)**



Source: IMF, Global Financial Stability Report, various issues, Centennial Group, database, and own estimates

Figure 13 **Market-determined Asset gains/losses by region 2008-2011**



Source: IMF, Global Financial Stability Report, various issues, Centennial Group, database, and own estimates

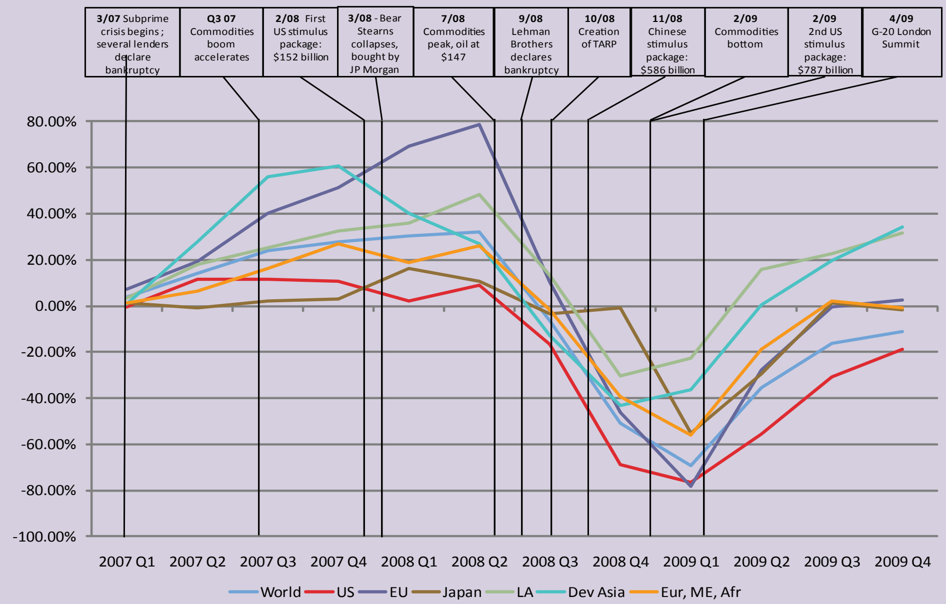
Developing Asia, reflecting the strength of China and India and the appreciation of national currencies vis-à-vis the US dollar, also recovered but remained further away from its maximum.

The recovery from the 2008 shock in the subsequent three years has been significant, but very uneven among regions. In particular, the European Union has experienced a continued loss of its financial wealth, except for the initial recovery in 2009. This is explained by a lack of coordinated fiscal and monetary policies, which had not been seriously addressed until 2012. The US has recovered in part, but still had not reached the previous levels of financial wealth. The weak recovery in the level of assets due to market conditions was offset in part by government action. However, the process of deleveraging by the private sector and the concerns about mounting liquidity and government debt has reduced further the pace of the recovery. While the emerging economies have seen a much stronger recovery in assets, this has not been sufficient to offset the drag in the advanced economies, and particularly in Europe.

The impact of a decline in stock market values and the subsequent slow recovery are having a direct effect on the performance of economies world-wide. Different estimates show wealth-elasticities of consumption to financial wealth in the order of up to .05, and of .06 in the case of housing equity for increases in wealth. However, the association seems to be stronger in the case of declines in wealth.[20] On that basis, a decline in financial wealth in the order of 20 percent could have an impact on consumption of 2 percent. In addition, the effect on investment is significant on account of the perceived reduced prospects for growth in the near future because of significant existing excess capacity and the need to deleverage. Thus, the decline in activity in 2009 and the slow subsequent recovery are consistent with

20 Raphael Bostic Stuart Gabriel and Gary Painter, University of Southern California, and Ziman Center for Real Estate, University of California, Los Angeles, (2008).

Figure 14 **Asset Losses by Region (quarterly as % of GDP)**



Source: IMF, Global Financial Stability Report, various issues, Centennial Group, database, and own estimates

the loss of wealth described here. This has taken place notwithstanding the significant efforts among major countries to reactivate their economies, which in practice came to a halt in 2010, particularly on account of the serious difficulties confronted by the European financial system, because of lack of clear and unified action by the various governments in the European Union, and particularly within the Euro area. Looking forward, the path for recovery is likely but far from easy.

The Future Access to International Financial Organizations

With the advent of the Great Recession, authorities in many emerging economies announced fiscal and credit packages aimed at softening the impact of lower commodity prices and reduced external demand. These measures were being taken on top of the currency devaluations in many larger countries. Questions arose about the size of these packages in emerging economies, and how they compared with those in the more advanced economies of the world. With the exception of those announced by China and Singapore, the packages among emerging economies were considerably smaller than those implemented in the US and Japan (6 percent of GDP) and Germany (3 percent). In these countries, even with high levels of debt to GDP, their size and the depth of capital markets allowed them to increase spending. In China and Singapore, a very low level of net debt and high reserves allowed for the proposed effort. In Latin America, the two countries that were more successful in terms of their stabilization policies were Chile and Peru, with low levels of net debt, and in the case of Chile, a successful stabilization fund. All other countries announced packages amounting to about one percent of GDP, in line with what they could afford, either because of the level of their debt or the size of their financial markets. Subsequently, as (mainly emerging) countries recovered from the recession, commodity prices rose, and private financing became available again, the need for stimulus receded (see Figure 5 and Table 8) for most of these economies.

Thus, to the extent they are to need more stimulus, they will have to rely on the effect of the external packages, more than on their own actions, particularly in the area of fiscal policy. Still, an important additional component of recovery for many of these countries is the ability to raise funds and use reserves. Latin America holds about US$800 billion in reserves as of mid-2012, mostly held by Brazil, and Mexico, and to a lesser degree by Argentina and Peru. Thus, the region has had the ability to withstand well the pressures with respect to lower financing. Furthermore, the relatively small number of outstanding arrangements, even after the extension of contingent credits to Mexico, Colombia and stand-by arrangements to a number of smaller countries in Latin America by the IMF, suggests a capacity to raise official funds that had not been taken fully into account so far.

The international financial community, including the G-20, has made a major commitment to a massive mobilization of resources. The eventual approval of the IMF quota increase will further enhance the prospects for the region, but the money is far from certain as the US has not even submitted the prospective increase for consideration by Congress. Still, Latin America and the Caribbean could have the potential to obtain US$200 billion in loans, or about 5 percent of GDP on the basis of: (1) increases in the amount of SDRs, assigned proportionally on the basis of IMF quotas or shares; (2) possible new lending by the IMF and other International Financial Institutions, assuming that China, India and Saudi Arabia will not be borrowing from them; (3) trade related financing by trading partners (Table 11).

These amounts are substantial, but there a number of constraining factors: the funds may not be available for several years; debt service payments for the region are in the order of US$200 billion, of which more than half are official obligations; and private capital inflows have tended to fluctuate considerably in the recent past, even as foreign direct investment recovered. With the pace of exports declining again, the financial outlook for the region is problematic. In any event, if financial flows fall and the terms of trade remain weak, Latin America can withstand the problems if it strengthens its fiscal policy, maintains a prudent approach in terms of the use of reserves, and considers the possible access to financial resources from the international organizations as a useful tool, and not as a political stigma, particularly on the basis of modified access to IMF resources. This type of package reflects the right policy approach, with the official sector acting as a countercyclical force at a time of financial catastrophe. Within the total borrowing that the region can obtain from multilateral organizations, CAF can play a significant role and it has already indicated its intention to grant loans for a total of US$20 billion to help the region deal with a possible decline in private financing.

The return of the IFIs to the international scene, particularly with a crucial role in the current European crisis, has been difficult to accept for many of the possible clients in the region, which had made a point of breaking their previous close financial ties to the IMF, the World Bank and the Inter-American Development Bank. Argentina, Bolivia, Ecuador, Venezuela, and to a lesser extent Brazil and Colombia, had considered that their improved

Table 11 **Estimated Availability of New Funds to Latin America (US$ billions)**

	IMF Quotas (% of total)	SDR Allocation 1/	Additional Lending IMF 2/	Multilat. Dev. Banks 3/	Trade Related Lending 4/	Total Financing
Total World	100.0	250	500	100	250	1100
Advanced Economies	59.6	149	-	-	172	321
Emerging and NICS, Excluding LATAM	32.6	82	378	77	60	596
Latin America and Caribbean	7.8	19	123	23	18	183

Sources: IMF, G-20 Declaration- April 2009, and own estimates.
1/SDR Allocation on the basis of Existing IMF Quotas
2/Additional Lending by IMF on the basis of existing quotas, excluding advanced economies
3/Multilateral Development Bank lending on the basis of GDP, excluding advanced economies
4/Trade related lending on the basis of GDP, including Advanced Economies

circumstances meant that they no longer needed the IFIs now that they had strong trade performance, robust international reserves, and a much easier access to international financial markets. These assumptions are, however, subject to considerable volatility.

While financing requirements have declined, access to the IFIs may well become a necessity for many countries in the region if the advanced economies remain weak. Such access, even if difficult from the countries' point of view, will be eased by the fact that these organizations are showing greater lending flexibility. The initial actions of the G-20 gave some hope in this regard. The G-20 includes the G-8 and China, India, Indonesia, Korea, South Africa, Brazil, Mexico and Argentina, among others. This forum should have reflected the growing importance of the emerging world and opened the door to a more representative governance system at the world financial level, but in more recent years the push for reform has lost its initial strength, and has fallen disappointingly short of its initial objectives.

The trend toward more flexible lending mechanisms by the IFIs also helps. The most controversial lending organization remains the IMF. According to its own information, the IMF has increased its lending capacity to some US$800 billion, in addition to any SDR allocation that has been agreed. The IMF had played a major role in financing Latin America in the past. However, after lending to Latin America reached about US$50 billion at the beginning of the 2000 decade, it had fallen to less than US$1 billion in late 2008. After the announcements of increased flexibility, Mexico has benefited from the new approach of the multilateral organizations, and particularly from the less conditional approach embodied in the Flexible Credit Line (FCL). Specifically, Mexico has been granted US$47 billion, and Colombia US$21 billion, on the basis of their track records, and with the right to draw on the credit line at any time, as long as policies continue to satisfy the established standards in light of existing circumstances. The IMF also remains ready to deal with requests for assistance under what it defines as fast-track emergency financing procedures. The FCL is available for countries that are seen as having carried out reasonable policies and are willing to take the necessary measures to put their economics on track. Once agreement with the authorities has been reached on a lending program, the IMF Executive Board, which is kept informed of the negotiations, considers the request for a loan within up to 72 hours. This is in contrast to the six weeks to two months required under normal lending circumstances. If policy failures are significant, then the IMF would follow more traditional lending procedures. Countries that need financing most urgently in the region may be unwilling to engage in negotiations. They will, however, be attracted by the fact that the IMF will emphasize only a few basic macro economic conditions, as opposed to a wide array of issues, as had been the practice in the past.

The World Bank also launched the Debt Management Facility to help developing countries prevent future debt problems. It also called on donor countries to meet their debt relief commitments. According to the World Bank, the new facility will accelerate the implementation of debt management programs in partnership with several other organizations, with the objective of strengthening debt management capacity and institutions in developing countries. This supplements the Bank's financial assistance for poor countries, but with only very few qualifying members in the region, this has limited impact on Latin America. However, countries will make increased use of World Bank resources to finance their programs of reform, as well as the public expenditure/investment programs that many of them are putting in place to deal with the current slowdown.

The Inter-American Development Bank also approved a record volume of loans since 2009 and has set up a new fast-disbursing US$6 billion liquidity facility to help Latin American and Caribbean economies. The IADB's US$6 billion Liquidity Program for Growth Sustainability is available to domestic firms via commercial banks that may face temporary difficulties in accessing foreign and inter-bank credit lines as a result of the financial crisis.

These efforts on the part of the IFIs are very significant, but they will work only to the extent that the countries themselves are willing to draw down these funds and use them effectively. Many recognize the advantages of these loans, as they are contracted on a longer-term basis and with relatively low interest rates. However, some countries may choose not to use these funds on ideological grounds. They may actually harm themselves, since they may end up having to make more drastic adjustments, or declare a default on outstanding obligations with even worse consequences than availing themselves of help from the IFIs. The number of such countries is small, without major contagion to the other more responsible countries in the region.

Lessons from the Current Financial Turmoil[21]

There are a number of important lessons in relation to the Financial Crisis of the last years:

1. Globalization and the increase in the size of international financial markets have

21 This discussion reflects the presentation of Global Governance and Reform of the International Monetary Fund: An Update, by Jack Boorman, Advisor Emerging market forum, 2009.

dramatically raised the mutual dependence of economies around the world.

2. Large financial institutions are increasingly global in their operations, which link together financial markets worldwide, but without effective global regulation or supervision.
3. Financial instruments created and regulated in one country are bought and sold throughout the world, but the failure of regulation of many of those instruments, the issuing institutions, and the rating processes left the system highly vulnerable to the kind of crisis that developed.
4. Capital markets and capital flows now exceed commercial lending operations in their size and profitability as well as in their influence on the performance of overall financial markets.
5. Financial crises emerge with great regularity, but their origin and nature have been impossible to predict; increasingly such crises develop suddenly and quickly spill over beyond national boundaries, posing threats to the global system itself. Their resolution requires considerable actions on the part of the economic authorities, as it happened in the US, even if imperfectly. The authorities in Europe, however, have clearly failed so far to develop an equivalent set of rules and regulations, consistent with the requirements of their monetary union.
6. In the wake of the financial crisis, financial institutions have merged or consolidated further. In these circumstances, rather than solving the problems of the existence of large institutions, the recent trends have aggravated the problem of institutions that are "too big to fail" and thus generate further risks of moral hazard to the system. This is particularly the experience observed in major advance economies, where banks and creditors have been protected at the expense of tax-payers.

While the financial system has evolved rapidly, its monitoring and regulation have lagged behind:

- The institutional architecture and governance of the global financial system, as well as its governance structure, does not yet reflect the massive changes that have taken place in global financial markets and in the position of the most rapidly growing economies in that system.
- The current system relies on regulation and supervision at the national level, while many major financial institutions and their instruments are global in their reach and influence.
- At the country level, there are important differences in the approach to regulation and supervision; some very profitable and dynamic parts of the system were virtually unregulated (hedge funds, private equity, derivatives) and the lack of transparency—both of markets and of individual institutions—remains an issue.
- In some critical areas, including the analysis and oversight of capital markets and capital flows, no international body currently has a clear mandate.
- There are serious gaps in the codes and standards that guide transparency at national and global levels.
- There has been no effective "early warning system" regarding some of the risks that can develop at the global level.
- There is an asymmetric, albeit improving, willingness of institutions, including the

IMF, to comment candidly on the policy weaknesses and risks being taken by the key players in world financial markets.

Principles for Reform

- The current gaps, disparities, and fragmentation in the setting and monitoring of standards, and in the regulation and supervision of different parts of the financial system, should be eliminated
- Future responsibilities should be based on a three-tier system: national, regional and global institutions.
- The setting of standards and information reporting should be coordinated and monitored at the global level.
- However, the primary responsibility for regulation and supervision should rest at the national level, or at a regional level like the case of the European Union.
- Early warning systems must be developed at the national and global levels.
- Periodic discussions on the stability and vulnerabilities of national and regional financial systems, and peer review of financial systems and the sharing of experience should rest at the regional level.
- To ensure its legitimacy and credibility, the new global financial architecture should reflect the current economic realities and provide for a larger role for the major emerging market economies.
- The IFIs must have the tools and authority to address weaknesses in the economic and financial policies of all their members, including the largest economies and the most important financial systems in the world, and must be independent in using that authority.

Financial Sector Regulation[22]

In light of the above developments, the world's main economies have embarked on a serious effort to reform the financial system operations. The ongoing financial regulatory reform process is aimed at addressing the inadequacies in the regulatory framework that the crisis has revealed. The process is gradually yielding recommendations at both the national level and internationally, which is generating some uncertainty for the financial sector. Proposals are most advanced in the area of strengthening bank capital. Enhancements to the Basel II capital framework—specifying higher capital requirements for banks' trading books and some securitizations—have been implemented since 2010. Other reform proposals (announced in December 2009) focusing on bank capital and liquidity, with the final calibration for capital requirements, will be implemented by end-2012.

The proposals target:

- Improving the quality of bank capital (by increasing the share of common equity in Tier 1 capital; harmonizing the definition of Tier 2 capital internationally; and enhancing the risk coverage of the capital framework).
- Supplementing risk-based capital requirements with a leverage ratio, with details yet to be worked out.
- Dampening pro-cyclicality (by conservative adjustments to capital adequacy to reflect stressed periods; forward-looking provisioning; building up target capital buffers; and

22 This discussion reflects "Recent Developments in Financial Regulation Reforms" by Aditya Narain and Kornélia Krajnyák in World Economic and Financial Surveys: Regional Economic Outlook; Western Hemisphere-Taking Advantage of Tailwinds- Washington DC May 2010.

upward adjustment of capital buffers after a period of rapid credit growth). Work on the details of the proposals is ongoing.

- Addressing systemic risk and interconnectedness (through a better-calibrated asset value correlation factor in internal ratings that would imply higher capital requirements for exposures to large regulated financial firms or to unregulated leveraged entities such as hedge funds).
- Reducing the reliance on external ratings in the capital adequacy framework.
- Introducing internationally common standards of minimum high-quality liquidity buffers, with the dual aim of (i) being able to meet liquidity outflows over a 30-day stress period; and (ii) matching liability and asset profiles over a 1-year horizon.

Recommendations in other areas are less advanced. The framework for macro-prudential supervision is still evolving, with a view to alleviating credit cycles and contagion risks. Discussions on issues related to systemic risk and systemically important institutions are complicated by, among other things, political and legal issues. On the agenda are extending the regulatory scope, introducing differential prudential regulations for systemically important institutions, possibly creating a systemic risk regulator, setting up a resolution framework for systemically important institutions, and rethinking regulatory issues in the OTC derivative and securitization market. Of course, these proposals do not cover all areas where improvements would be needed to strengthen financial stability. Ensuring adequate supervisory responses, improving risk management and governance in the financial sector, and leveling the playing field internationally (by proper and consistent implementation of prudential standards) and across sectors (by stepping up lagging reforms in the insurance sector and securities markets), as well as dealing with the "too big to fail" concept, remain outstanding tasks.

Concluding remarks

Most emerging market economies, including those in Developing Asia and Latin America have come out of the Great Recession, but the next twelve months will remain very difficult, particularly in light of the European crisis. The perception that they had broken the links with the larger economies has been refuted by the hard facts of the last years. Financial markets of the world are closely interconnected; the impact of the world financial collapse and more recently the European debt crisis on emerging economies are witnesses to this fact.

Even as Asia and Latin America diversified their investment and trading partners, the effect of the slowdown on exports, finance, and investment is significant. Growth fell sharply, and the external accounts are reflecting the consequences of the fall in prices, economic activity, and wealth, with capital flows increasing slowly and with some short-term reversals.

In hindsight, poor macroeconomic and regulatory policies allowed the global economy to exceed its capacity to grow and contributed to a buildup of imbalances across asset and commodity markets. Policy and market shortcomings prevented equilibrating mechanisms from operating effectively and market stresses rose. These errors occurred mainly in the US and some European countries, but there has been some slippage in emerging economies, so that the blame cannot be fully shifted to others. However, economic conditions suggest that a recovery may be sustainable, after the adjustments in the financial markets have worked through.

The situation is serious and the effect on output, wealth, and poverty is critical. In Latin America and other emerging economies, particularly in Asia, national authorities now see the situation with a greater degree of realism. The main countries of the world reacted well initially to the crisis, but they lost momentum subsequently. Accordingly, uncertainty has persisted, and the ability to react has been narrowed in the advanced economies, particularly in the face of mounting public debt.

emerging economies are better prepared to deal with external shocks today than at any time in the last quarter century or so. Unfortunately, the shocks were greater than in the past, and defenses have been effective in the short run but may not be sufficient in the medium term to protect these countries. Each country will have to follow a difficult path, and populist and protectionist temptations will remain a major threat. These tendencies carry a high cost. Even with better defenses, the world faces a serious economic challenge. Countries are now confronted with the need to find a balance between economic stimuli on the one hand, and financial stability on the other. Such a task is not simple, and will require effort and clarity of vision.

The Emerging Markets Forum was created by the Centennial Group as a not-for-profit initiative to bring together high-level government and corporate leaders from around the world to engage in dialogue on the key economic, financial and social issues facing emerging market countries (EMCs). The Forum was granted the coveted 501(c) status by the U.S. Internal Revenue Service.

The Forum is focused on some 70 emerging market economies in East and South Asia, Eurasia, Latin America and Africa that share prospects of superior economic performance, already have or seek to create a conducive business environment and are of near-term interest to private investors, both domestic and international. We expect our current list of EMCs to evolve over time, as countries' policies and prospects change.

Further details on the Forum and its meetings may be seen on our website at http://www.emergingmarketsforum.org

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