

**4th Annual OECD - EMF Forum
Virtual Meeting of 30 April 2021
Imagining Emerging Economies in a Post-COVID World Session III :
Rethinking Monetary System and Debt**

Re-thinking Emerging Market Debt and Development Finance

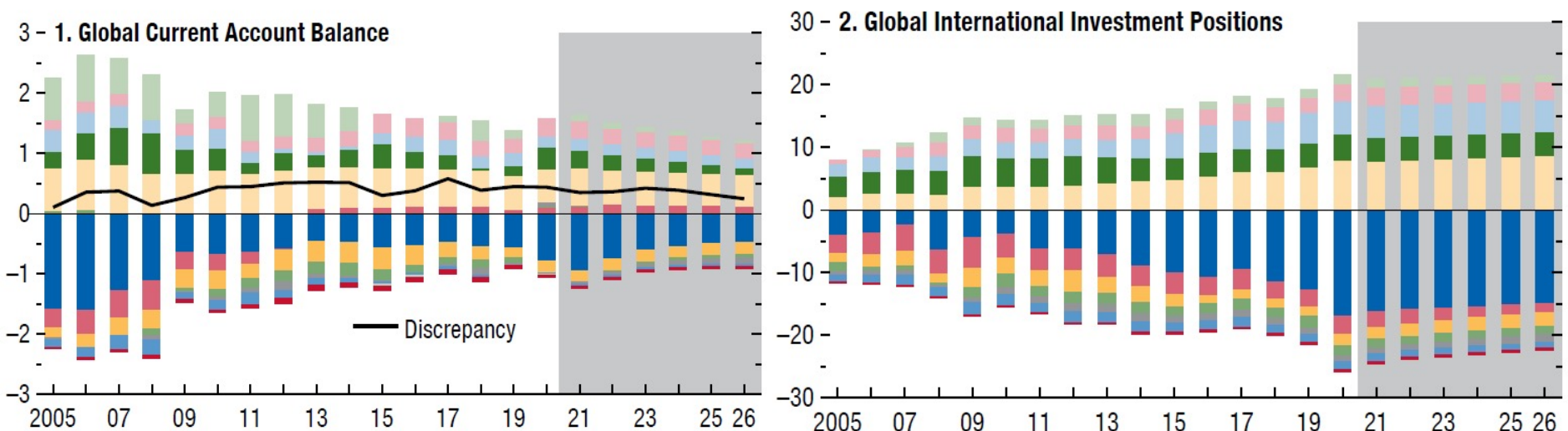
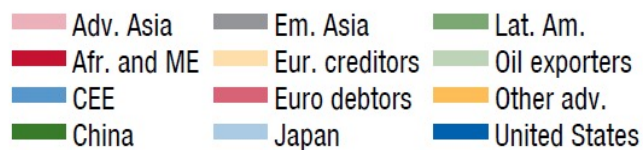
Andrew Sheng
Chairman,
George Town Institute of Open and Advanced Studies
Wawasan Open University, Malaysia.
28 April 2021

Key Points

- Post-pandemic, global and EME debt levels higher than ever, due to IMS
- QE adds debt to solve debt crises, so system has become banker consuming more credit flows, crowding out EME long-term funding
- Global Liquidity Trap with excessive short-term funding and insufficient long-term SDG investments to promote growth, deal with inequities and deal with climate change
- EMEs do not have QE tool, threatened by capital flows, and maintain as high liquid assets (\$10 trn+) as much as their net outstanding USD debt (\$10 trn+) but pay 4% interest margin on difference in income. Revenue enough to cover current account deficits
- SDR500 billion increase welcome first step; some suggestions for use
- EMF can help lead conversation on IMS reforms to help EMEs

Global Current Account Deficits widened to peak in 2006, narrowed since then, but US net liability (NIP) keeps on growing, from 33.3% of global net liability 2005 to 64.8% by 2020 (EME share from 28.8% to 16.7%)

Figure 1. Current Account and International Investment Positions (per cent of world GDP)



EMEs (ex-East Asian surplus countries) slightly negative CA deficits, but roughly 4% of world GDP in net debt

US Net liability growth 2005-2020 85% due to Capital Inflows and Valuation Effects, 15% due to cumulative Current Account Deficits

Table 1: US Current Account Balance & Net Investment Position 2005-2019 (USD billion)

Year	CA Balance (USD bn)	NIP (USD bn)
2005	-209.6	-2,238.4
2006	-193.7	-1,807.8
2007	-167.1	-1,278.8
2008	-156.2	-3,994.6
2009	-101.9	-2,626.9
2010	-100.6	-2,511.1
2011	-109.8	-4,454.6
2012	-95.4	-4,517.1
2013	-73.4	-5,367.6
2014	-102.4	-6,944.2
2015	-99.4	-7,460.2
2016	-93.7	-8,129.3
2017	-92.8	-7,622.2
2018	-132.5	-9,674.4
2019	-104.3	-11,050.5
2020	-188.5	-14,092.1
Total CA (2006-2020) USD bn	NIP 2020 less 2005 (USD bn)	Change in NIP (USD bn)
-1,811.6	-11,853.7	-10,042.1

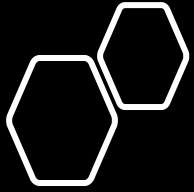
NIIP of Major Surplus and Deficit Countries, 2020

Appendix Table A2: Net Investment Position, Major Surplus and Deficit Countries, June 2020

Surplus Country	NIIP Surplus (US\$ bn)	% of GDP	Deficit Country	NIIP Deficit (US\$ bn)	% of GDP
Japan	3,721.0	69.2%	United States	-14,092.1	-62.1%
Germany	2,870.0	66.4%	Spain	-1,060.5	-72.6%
Hong Kong^[2]	2,150.3	583.3%	Ireland	-752.1	-157.8%
China^[2]	2,150.3	12.9%	Brazil^[2]	-731.2	-49.0%
Taiwan^[1]	1,342.8	176.9%	Australia	-729.5	-45.1%
Norway^[2]	1,175.4	264.4%	France	-698.5	-23.8%
Canada^[2]	1,095.8	58.2%	United Kingdom	-668.0	-21.4%
Netherlands	1,047.3	103.4%	Mexico^[2]	-590.1	-49.5%
Singapore^[2]	1,043.1	278.2%	Turkey	-403.1	-50.7%
Switzerland^[2]	721.7	87.5%	India	-340.5	-13.1%
Saudi Arabia^[2]	622.7	77.4%	Greece	-335.4	-159.8%
Total	17,940.3	54.7%		-20,401.1	-52.9%

Notes: [1] 2019 data. [2] NIP data as of 1 Dec 2020.

Sources: IMF Data, IMF Report for Selected Countries and Subjects and national NIP data.



Risks to current IMS and for EMEs

Return of inflation, initially in EMEs, rise in interest rates → asset bubbles burst, debt distress

Secular Stagnation in HDC as global productivity slows and insufficient resources to deal with climate change, natural disasters, social unrests

Bretton Wood Institutions + MDBs (\$1.6 trn assets) underfunded to deal with scale of liquidity and long-term development gap (\$2.5 trn annually for SDG goals).

World financial leverage: 2010-2019

Crude leverage showed decline, but equity base very narrow with number of listed companies shrinking and concentrated

Table 2: World Financial Assets/Liability (2010-2019)

Year	World GDP A	Stock Mkt Cap B	Bond Mkt Cap C	Bank Assets D	Total B+C+D	Crude Leverage (C+D)/B
		\$ trillion			\$ trn	
2010	75.5	58.0	82.2	129.8	270.0	365.5%
2019	86.6	94.0	105.9	155.3	355.2	277.9%
		% of World GDP				
2010	100.0	76.8	108.9	171.9	357.6	
2019	100.0	108.5	122.3	179.3	410.1	

Listed company base very concentrated (tech valuations) and numbers dropping to 41,000 relative to millions of SMEs requiring capital

Structural Mismatches

- Maturity Mismatch – borrow short, lend long
- FX Mismatch – borrow FX, invest in local currency, insufficient reserves
- Debt/Equity – leverage growth leads to insufficient equity cushion to absorb shock losses
- Not solved after AFC97 nor GFC2008, as QE enabled debt funding through low interest rates

Asset Size of Multilateral Banks is \$1.6 trn, Mere 1% Of Global Banking System (\$155 trn as at End-2019)

Table 3: Share of Country's GDP in the World in 2035, Versus Current Vote Share at IMF.

Positive numbers indicate the country will be overrepresented at IMF based on its economy

Country	GDP share (%)	Voting share (%)	Difference (%)
Australia	1.35	1.34	-0.92
Brazil	2.87	2.22	-22.66
Canada	1.62	2.22	36.99
China	24.31	6.09	-74.95
France	2.50	4.04	61.29
Germany	2.85	5.32	86.89
India	11.33	2.64	-76.70
Indonesia	2.69	0.95	-64.69
Italy	1.85	3.02	63.12
Japan	4.06	6.16	51.84
Mexico	2.43	1.80	-26.00
Russia	3.48	2.59	-25.54
South Africa	1.06	0.64	-39.71
South Korea	2.22	1.74	-21.63
Turkey	2.01	0.96	-52.31
United Kingdom	2.94	4.04	37.62
United States	19.52	16.53	-15.32

Majority shareholders unwilling to increase capital due to dilution and loss of control.

Global Liquidity Trap - short-term funding from QE, inadequate long-term funding for infrastructure, climate change and addressing inequality.

- With reserve currency countries using QE, IMS has high liquidity, but has long-term infrastructure funding gap to address climate change and social inequalities
- This arises from short-term focus of central banks and policy agencies, whilst EMEs and MDB lack institutional expertise and capacity to design, manage and operate complex engineering infrastructure projects.
- Due to volatile gross capital flows, EMEs maintain high FX reserves and also constrained in borrowing long-term, paying 4% p.a. premium
- Result is lower long-term growth and productivity, which is also afflicting rich countries.

MDB resources currently \$1.6 Trn and under-funded due to Unwillingness of Major Shareholders' to Increase Equity

Appendix Table A1: Multilateral Development Banks Total Assets (USD bn)

#	Development Bank	Assets (USD bn)
1	European Investment Bank	606.5
2	International Bank for Reconstruction and Development, World Bank Group	283.0
3	Asian Development Bank	191.9
4	International Development Association, World Bank Group	188.5
5	Inter-American Development Bank	129.5
6	European Bank for Reconstruction and Development	67.7
7	African Development Bank	48.3
8	Asian Infrastructure Investment Bank	19.6
9	Islamic Development Bank	18.5
10	Central American Bank for Economic Integration	10.9
11	New Development Bank	10.4
	Total	\$1,574.8

Possible reform options

SDR500 (\$650) billion increase add only to liquidity, but can be used if SDR surplus countries willing to convert/donate to special funding to address urgent issues:

1. \$15 bn used by low income countries and \$60 bn used by medium income countries for own liquidity needs (managing capital flows)
2. \$100 bn Trade Finance Facility to help SMEs and global trade finance liquidity (ICC)
3. \$575 bn increase in MDB capital, with leverage of 9:1, will increase MDB long-term funding by \$4.275 trillion for SDG needs

But, must improve long-term project design, operation, management at country and MDB levels.

4. Avinash Persaud proposal for middle-income debt reduction scheme to address natural disasters and post-covid rebuilding

Thank you

**Q&A to
altsheng8@gmail.com
and www.andrewsheng.net**