UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

UNCTAD

DEVELOPMENT AND GLOBALIZATION: Facts and Figures 2012

UNITED NATIONS

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UNCTAD/WEB/GDS/DSI/2012/2

UNITED NATIONS PUBLICATION

April, 2012

Foreword

We have witnessed a remarkable shift in economic trends over the past years. Issues such as current account imbalances, misaligned exchange rates, volatile capital flows and the financialization of commodity markets resulted in a severe crisis that affected all countries. As debate continues to rage about the relevant monetary, fiscal and income policies to address the continuing fallout from the crisis, the international community is falling short on delivering solutions to the long-standing challenges of poverty, food security, debt burden and climate change.

A lesson learned over the past few years is that the only way the world can hope to recover from recession is by ensuring a predictable financial system in line with the rules-based multilateral trading system that strives to meet long-term development goals. That is why UNCTAD is calling for urgent measures to strengthen the shift in the economic paradigm for global governance from a finance-centred one to development-centred one.

This 2012 edition of Development and Globalization: Facts and Figures highlights the latest available statistics depicting the current state of the world economy, with expert comments on their empirical implications. We have focused on pivotal themes that best illustrate the interface of trade and related economic development issues, in particular macroeconomic and financial indicators, as well as those relevant to policymaking in the area of fiscal and incomes policy. Those researchers and policymakers seeking a better understanding of the factors underlying the global slowdown will find the empirical information they need to better appreciate how unrestrained globalization and excessive financialization have overwhelmed the real economy over the past decades.

This quadrennial publication caters to specialists and the general public. Well-designed statistical graphs and tables, and a glossary of the main economic and statistical concepts offer our broad readership practical tools for a better understanding of development trends and their evolution over time.

Supachai Panitchpakdi
Secretary-General of UNCTAD

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Overview

This pdf document is derived from the web version (http://dgff.unctad.org/) of the 2012 edition of the 'Development and Globalization: Fact and Figures' which includes more statistical charts and tables as well as dynamic motion charts that illustrate in an innovative way key findings.

CHAPTER 1

GLOBALIZATION AND THE SHIFTING BALANCE IN THE WORLD ECONOMY

Economically, globalization means closer integration of national economies through trade and financial flows as well as cross-border migration of people. As national economies "open up" and lower their external barriers, they become more exposed – and more vulnerable – to global forces and influences.

With the long-run globalizing trend well established since the end of the Second World War, the pace of globalization accelerated over the past 25 years, resulting in unprecedented levels of economic integration and interdependence in the world, surpassing the pre-First World War peak. After reaching a tentative culmination with the global boom of 2003–2007, globalization reared its ugly head and the world economy ushered in the most severe global economic crisis since the Great Depression – from which recovery remains fragile and incomplete.

CHAPTER 2

GLOBAL IMBALANCES, CRISIS, AND THE LACK OF GLOBAL GOVERNANCE

The era of accelerated globalization that preceded the global crisis saw rising imbalances in international trade and financial flows that starkly contradicted traditional development theory and the conventional wisdom of policymaking of that very era. Seemingly paradoxical capital flows and imbalances were part of the build-up of financial fragilities at the core of global finance in key developed countries that provided the precondition for the global crisis of 2008–2009.

The global crisis had a severe impact on global economic activity, incomes and employment; though more lastingly so in key developed countries than in many developing countries. The legacies of the crisis are posing difficult challenges to designing short-run policies suited for sustaining the global recovery. Unbalanced competitiveness positions provide the background to financial stresses that continue to plague parts of the developed world today, especially in the euro area.

While briefly shrinking during the global crisis, global imbalances in trade and financial flows and their underlying systemic causes have not gone away. Global imbalances are a symptom of existing systemic governance shortcomings. They can only be properly addressed by global governance reform and proper international policy coordination.

CHAPTER 3

DEVELOPMENT CHALLENGES AND POLICIES TO OVERCOME THE CRISIS

This chapter discusses the role of macroeconomic policies to mitigate the effects of the crisis and to reinvigorate economic growth, while reducing unemployment and inequality, and putting the global economy on a sustainable growth path. In that vein, it takes a closer look at the monetary, fiscal and income policies regarding some of the challenges currently faced by both developed and developing nations.

Interest rates have been reduced to provide an incentive to spend and to stimulate the economy. However, monetary policy alone has proven insufficient to put the economy back on track. Fiscal policy, in turn, had been stimulative, but with the collapse of revenues and the increase in public debt, an early turn towards austerity has reduced the chances of a healthy recovery. Incomes policy would be an important complement to stimulative macroeconomic policies. Developing countries also have to cope with volatile commodity prices and pressures to reduced policy space. Last but not least, no recovery could be sustainable without financial re-regulation.

CHAPTER 4

LONG-STANDING CHALLENGES

The relation between the ongoing globalization process and its associated policies is an important element in the evaluation of the progress towards the Millennium Development Goals (MDGs), which has been uneven by countries, regions and goals. While poverty and educational and gender attainment goals have seen significant progress, the other targets, i.e. reduction in child mortality, improvement of maternal health, reducing major diseases, attaining environmental sustainability and improving the conditions for development in particular finance and debt reduction, have seen less marked progress. This has called into question some of the policy proposals that have been used in order to reach the MDGs. Further, hunger reduction, one of the Goals, has been affected by the recent global economic crisis. Food insecurity has increased after the global economic crisis, fundamentally as the result of higher and more volatile prices for food and agricultural commodities. Financial regulation, in the aftermath of the crisis, and increased official development assistance (ODA) flows, and further debt relief for developing countries are also necessary to meet the MDGs deadline in 2015.

Explanatory notes

ECONOMIES, COUNTRIES AND COUNTRY GROUPS

The classifications of countries in this publication have been adopted solely for the purposes of analytical or statistical convenience and do not necessarily imply any judgment concerning the stage of development of a particular country or area. The term “economies" refers to regions, countries and territories.

There is no established convention for the designation of "developed" and "developing" countries or areas in the United Nations system. In common practice, Israel and Japan in Asia, Bermuda, Canada, Greenland, Saint Pierre et Miquelon, and the United States in North America, Australia and New Zealand in Oceania, and Europe are considered "developed" regions or areas. Transition economies refers to South-East Europe and the Commonwealth of Independent States (CIS). Developing countries includes all countries or territories not specified above.

Country groupings follow generally those employed in UNCTADstat and the UNCTAD Handbook of Statistics 2011 (United Nations publication, sales No. E/F.11.II .D.1) unless otherwise stated.

The data for China do not include those for Hong Kong Special Administrative Region (Hong Kong SAR), Macao Special Administrative Region (Macao SAR) and Taiwan Province of China.

EXPLANATION OF SYMBOLS

0 Zero means that the amount is nil or negligible.

_ The symbol underscore indicates that the item is not applicable.

.. Two dots indicate that the data are not available or are not separately reported.

- The use of a hyphen on data area means that data is estimated and included in the aggregation but not to be shown. A hyphen between years (e.g. 1985-1990) signifies the full period involved, including the initial and final years.

The term “billion” signifies 1,000 million.

(e) Estimate
(f) Forecast
(p) Provisional data

Some exceptions are indicated in footnotes.

OTHER NOTES

The term “dollar” ($) refers to United States dollars, unless otherwise stated and data in dollars are expressed in current United States dollars of the year to which they refer.

Decimals and percentages do not necessarily add up to totals because of rounding.
Average annual growth rates are defined as the coefficient b in the exponential trend function $y = ae^{bt}$ where t stands for time. This method takes all observations in a period into account. Therefore, the resulting growth rates reflect trends that are not unduly influenced by exceptional values.

1 GLOBALIZATION AND THE SHIFTING BALANCE IN THE WORLD ECONOMY

GLOBAL TRADE TRENDS

Since the Second World War, global merchandise trade has generally grown faster than global income, but the global crisis has left its mark on trade dynamics: Recovery in global trade remains unfinished and uneven, while the trend toward greater trade openness of economies came to a halt. The global crisis and uneven trade recovery have reinforced the ongoing shift in balance in the world economy, featuring the relative decline of developed countries and rise of developing countries. The shifting global balance is also visible in the changing distribution of exports by destination, marked by the rising importance of trade among developing countries. While developing countries as a whole have become the key driving force behind global trade dynamics in the 2000s, performance varies considerably between regions and countries. Commodity price developments since 2002 came along with sizeable changes to terms of trade.

GLOBAL CAPITAL FLOWS TRENDS

Global capital flows have grown even faster than global trade. While the share of relatively more stable foreign direct investment has increased since the 1990s, private capital flows have proved both highly cyclical and spectacularly fickle over and over again. In many developing countries, financial openness has increased significantly in terms of both capital flows and cross-border holdings, raising countries' exposure to external financial shocks correspondingly. While widely turning towards defensive macroeconomic policies in response to the emerging market crises of the late 1990s and keeping their own house in order, especially financially integrated developing countries at large were caught up brutally in the global crisis of 2008–2009.

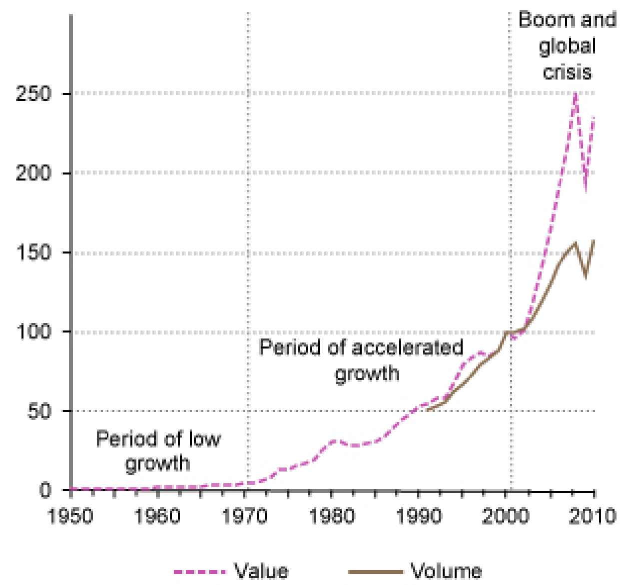
MIGRATIONS AND MIGRANT'S REMITTANCES

While far less advanced than trade and financial integration, migration flows and the cultural intermingling of populations too has increased in many countries and regions. Rising migration flows have come along with a marked increase in the role of private remittances. Remittances have become an important source of foreign exchange earnings for many developing and transition economies. Remittances may serve to support various developmental ends. The global crisis had an immediate and sizeable impact on migration flows and migrant remittances.

1.1 Global trade trends

Long-term trends in value and volume of merchandise exports, 1950-2010

(Index numbers, 2000=100)



Source: UNCTAD secretariat calculations, based on *UNCTADstat* and CPB Netherlands Bureau of Economic Policy Analysis, *World trade database*

In the context of the global crisis international merchandise trade registered its greatest plunge since the Second World War: Between the fall of 2008 and the spring of 2009 global trade collapsed by 20 per cent in volume. Having initially rebounded sharply beginning in mid-2009, growth in international merchandise trade then slowed again in the course of 2010. While regaining its pre-crisis peak level in that year, the global crisis appears to have left a marked impact on the dynamism of global trade, keeping the volume of global trade well below its pre-crisis growth trajectory.

Apart from remaining unfinished, the trade recovery has also been rather uneven. By the end of 2011, in developed countries as well as in South-East Europe and the Commonwealth of Independent States (CIS), where the trade collapse had been sharpest, merchandise trade in volume terms has yet to even reclaim its pre-crisis level. By contrast, the volume of both imports and exports in most groups of developing countries had already exceeded their pre-crisis peak in the course of 2010, with East Asia, China in particular, leading the expansion.

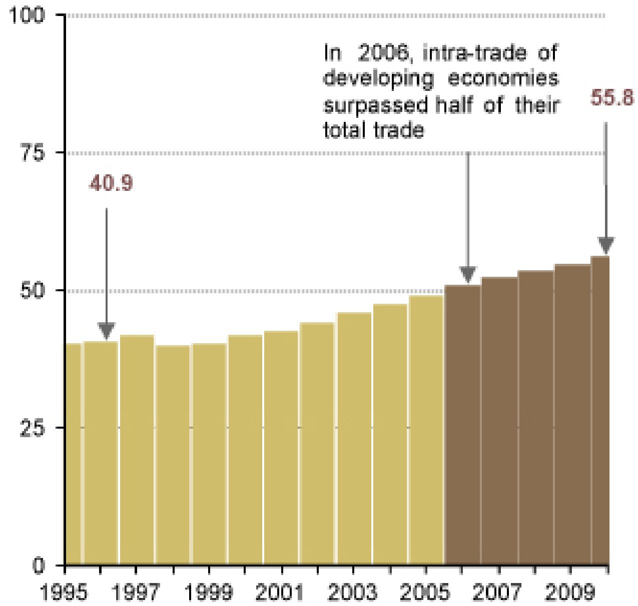
Globalization features the rise in global exports relative to global income, while individual countries see their respective exports and imports rise as shares of national income.

In other words, a rising proportion of global production of goods and services is being traded across borders rather than sold at home. The global crisis has brought the long-run trend of rising global integration through trade to a halt, at least temporarily. The pre-crisis trend toward more openness and ever-deeper trade integration might well firmly reestablish itself in due course. But persistence or trend reversal seem also possible. At a time of high unemployment, fiscal austerity, and complaints of currency wars, the threat of rising trade protectionism is looming large.

The global crisis and uneven trade recovery have reinforced the ongoing shift in balance in the world economy, featuring the relative decline of developed countries. In 2010 the value of total merchandise exports from all countries of the world was $15 trillion (in current United States dollars), of which the share of developed countries was 54 percent, down from 60 percent in 2005. As the world's leading merchandise exporter since 2009, China's share of world exports climbed to 10 per cent in 2010, ahead of the United States (8 per cent), Germany (8 per cent), and Japan (5 per cent). On the import side, the ranking still shows the United States in first place (13 per cent), followed by China (9 per cent), Germany (7 per cent), and Japan (4.5 per cent).

Share of South-South merchandise trade, 1995-2010

(Percentage of total trade in developing economies)



Source: UNCTAD secretariat calculations, based on *UNCTADstat*
Note: South-South trade is also known as intra-trade of developing economies.

The shifting global balance is also visible in the changing distribution of exports by destination, featuring the rising importance of trade among developing countries. The rise in South-South trade has been especially pronounced in East Asia and is linked to the gain in prominence of global supply chains.

While developing countries as a whole have become the key driving force behind global trade dynamics in the 2000s, and especially so since the recovery from the global trade collapse in 2008-2009, contributing 54 per cent to the overall rebound from it, performance varies considerably between regions and countries within the aggregate. Especially successful were developing economies in Asia. In general, progress in least developed countries (LDCs) and other low-income economies, after having fallen behind since the 1960s, has picked up somewhat, as they could recapture some of the lost ground since the mid-2000s. Helped by improvements in commodity prices, the export share of the LDCs, the majority of which are in sub-Saharan Africa and commodity-dependent, rose from 0.6 percent in 2001 to 1.1 percent in 2010. Yet commodity price increases have been a mixed blessing even to LDCs, proving harmful rather than beneficial to some. Especially low-income, food-deficit countries that had suffered severely in the food crisis of 2007-2008 were again affected negatively in 2010-2011.

While an upward trend in world primary commodity prices asserted itself in the 2000s, reversing the prior downward trend that had been in place since 1995, the period surrounding the global crisis witnessed commodity prices taking a roller-coaster ride. The boom years since 2002 ended with a severe nosedive from their peak level of mid-2008, followed by a sharp rebound that took prices back to 2007 levels by early 2011, when a sizeable correction began together with soaring volatility. Heightened market instability and price volatility have become the norm as uncertainty about the global recovery is weighing on market participants' minds.

Commodity price developments since 2002 came along with sizeable changes to terms of trade. In general, countries exporting oil and mining products saw substantial terms-of-trade gains, while those exporting mainly manufactures and importing raw materials, especially oil, experienced losses. Countries with more diversified exports and exporters of agriculture products experienced relative stability while manufactured goods exporters were confronted with a decline trend. Terms of trade changes can have substantial impacts on economies depending on their openness, in particular, either adding or subtracting from real domestic income. In the aggregate, all the developing regions gained, with the exception of East, South and South-East Asia (where manufactures constitute the largest share of exports). Wide differences exist within each region, however.

Highlights

- As trade flows have generally grown faster than income since the Second World War, countries' openness and their exposure to external developments have increased;
- Global trade collapsed in the global crisis of 2008-2009, recovery remains unfinished and uneven; the global crisis appears to have left a marked impact on the dynamism of global trade;
- The global crisis has also brought the long-run trend of rising global integration through trade to a halt, at least temporarily;
- The global crisis and uneven trade recovery have reinforced the ongoing shift in balance in the world economy, featuring the relative decline of developed countries;
- The shifting global balance is also visible in the changing distribution of exports by destination, featuring the rising importance of trade among developing countries;
- The rise in South-South trade has been especially pronounced in East Asia;
- LDCs have generally participated in these trends to a lesser extent but recovered some lost ground in recent years;
- Related to commodity price developments; many countries have experienced sizeable terms-of-trade changes since 2002, with both winners (especially oil and metal exporters) and losers (especially food-deficit countries) among developing countries including LDCs;
- Global governance reform needs to make further progress.

To learn more

UNCTAD Trade and Development Report 2011, Chapter I *Current Trends and Issues in the World Economy*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2007, Chapter III *The "new regionalism" and North-South trade agreements*, UNCTAD/TDR/2007

UNCTAD Trade and Development Report 2007 Chapter IV *Regional cooperation and trade integration among developing countries*, UNCTAD/TDR/2007

New and Traditional Trade Flows and the Economic Crisis, Policy Issues in International Trade and Commodities, Study Series No. 49 UNCTAD/ITCD/TAB/50, 11/12/2011

Evolution of the international trading system and of international trade from a development perspective, UNCTAD/TD/B/58/3, 04/07/2011

Integration of developing countries in global supply chains, including through adding value to their exports, UNCTAD/TD/B/C.I/16, 25/03/2011

1.2 Global capital flow trends

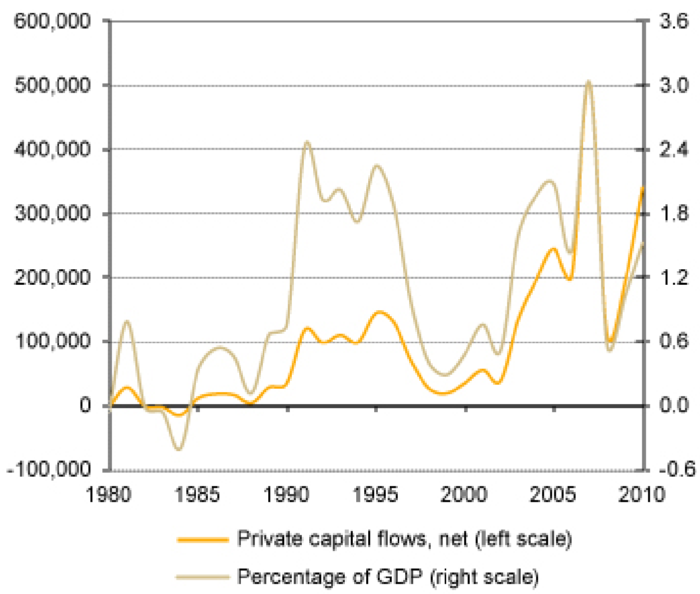
After having surged to unprecedented levels in 2007 and until mid-2008, private capital flows towards developing countries came to a sudden stop or even reversed direction as the system went into cardiac arrest, fleeing back towards the core countries of global finance that were the epicenter of the crisis. Most currencies experienced huge exchange rate gyrations vis-à-vis the United States dollar, functioning as the world's key reserve currency.

Tentative recovery began in the spring of 2009 under continued massive policy support from key central banks in developed countries. But volatility stayed at elevated levels and fresh stresses emerged starting in the winter of 2010, now concentrated in the European countries that share the euro as their currency. Developing countries experienced another surge in capital inflows after mid-2009 followed by yet another reversal in the course of 2011 as the European debt crisis worsened. Renewed disruptive exchange rate swings vis-à-vis the United States dollar broadly mirrored the tidal flows of private capital. Global finance remains in upheaval.

Financial globalization has proceeded at an even more rapid pace than trade globalization over the past few decades. While the developed economies continue to be the most financially integrated, more and more developing countries have meanwhile liberalized and at least partially opened up their financial systems. Since the early 1990s, private capital flows reached the shores of developing countries in two strong waves. The emerging market crises of the late 1990s and the global crisis of 2008–2009 provided the major breaking points that saw sharp reversals. Apart from crises, the monetary policy and business cycle in leading developed countries provide the other key driving force for global capital flows involving the developing.

Net private capital flows towards developing and transition economies, 1980-2010

($ millions and as percentage of recipient countries' GDP)



Source: UNCTAD secretariat calculations, based on IMF, *WEO October 2011*

While more and more developing countries have become prominent destinations of private capital inflows, especially since the 2000s, many have also experienced rising private capital outflows.

Private capital flows consist of three main categories: foreign direct investment (FDI), portfolio investment, and other investment; the latter including international banking flows. A compositional breakdown reveals a rise in the role of FDI and portfolio flows and relative decline in international bank lending flows.

The rise in international capital flows involving developing countries has led to a corresponding rise in cross-border financial holdings and an expansion in their international investment positions, recording foreign assets and liabilities.

The relative rise in developing countries gross foreign assets and liabilities provides further evidence of progressing financial globalization. Increasingly developing countries too are becoming part of globally interconnected balance sheets. In many developing countries, the concomitant rise in foreign assets and liabilities has seen an improvement in their net foreign asset positions, a process mainly driven by improved current account positions. Running a current account surplus position allows a country to either reduce its foreign debt and/or accumulate foreign assets, including international reserves. External debt trends over the last decade brought a continued general improvement of developing countries' debt indicators. External debt expressed as a percentage of gross national income as a percentage of exports of goods and both declined. Helped by declining global interest rates, the debt-servicing burden of developing countries as a group also decreased substantially.

Apart from paying off external debt or reduced overall reliance on foreign debt, many developing countries used improved current account positions to build up their holdings of international reserves. Rising reserves were also sourced from net private capital inflows. While concentrated in China, the unprecedented rise in international reserves has been a widespread phenomenon in the developing world, commonly referred to as self-insurance.

International reserve holdings serve precautionary purposes, and common indicators thus suggest that developing countries markedly increased their precaution in the era of progressing financial globalization, especially in response to the crises of the late 1990s. Recourse to reserve accumulation as self-insurance is part of a broader preference for defensive macroeconomic policies, including avoidance of an overvalued currency.

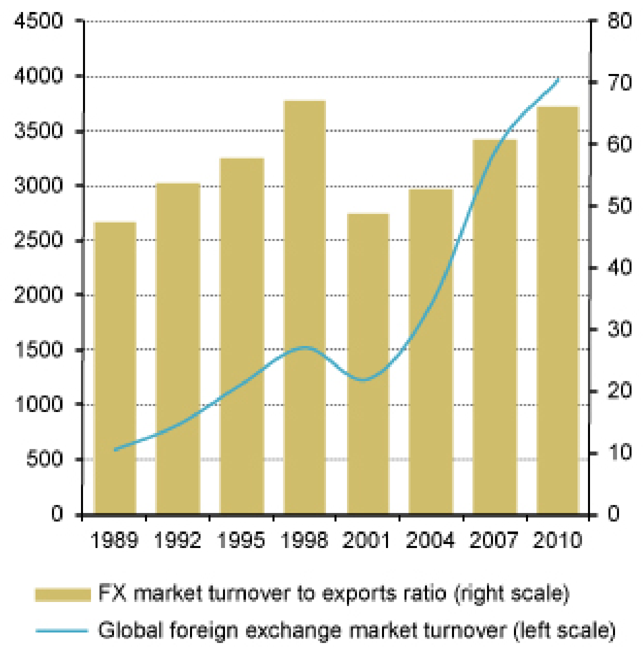
As financial globalization proved hazardous in the experience of many developing countries, maintenance of a competitive exchange rate became a policy focus. If foreign exchange market interventions are used to contain pressures for currency appreciation, a build-up of international reserves arises as a by-product.

The hazards of unfettered global finance were once again illustrated with spectacular vehemence and reach in the global crisis. Even developing countries that had seemed to be in excellent shape and had shored up their defences through large international reserve holdings were caught in the global contagion; albeit generally less so than countries that were running large current account deficit positions prior to the crisis, concentrated in Eastern Europe.

Perhaps the rule of finance over trade in the modern age of accelerated globalization is best illustrated by trading in foreign exchange markets. Daily foreign exchange trading has reached over 4 trillion, including spot and

Ratio of foreign exchange market turnover divided by value of merchandise exports, 1989-2010

(Average daily turnover in April, $ billions (left scale) and ratio (right scale))



Source: UNCTAD secretariat calculations, based on IMF, *DOTS* and BIS, *Triennial Central Bank Survey*

Note: Merchandise exports in April are first converted into daily figures for the ratio calculation.

forward markets and other foreign exchange derivates that feature prominently in carry trades. While still in the teens in the late 1970s, the ratio of yearly foreign exchange market turnover over merchandise exports had reached about 50 in the 1980s, and has doubled again since. The current ratio of around 100 implies that only about 1 percent of foreign exchange trading is actually related to merchandise trade.

The conspicuous rise of derivatives provides another indicator and symptom of the fragility of unfettered global finance, including credit derivatives such as credit default swaps and collateralized debt obligations. Hailed as welcome innovations in an era cherishing beliefs in self-regulation, these products came to prove lethally destructive far beyond their centres of origin in the developed world.

Highlights

- Global capital flows have grown much faster than GDP gross domestic product and trade;
- Capital flows towards developing countries are highly cyclical;
- Despite the relative rise in role of FDI, capital flows are fickle;
- Financial integration and openness of developing countries are on the rise, both in terms of capital flows and cross-border holdings;
- Despite widely improved external positions, developing countries proved vulnerable in the global crisis because of greater integration and interconnectedness in unfettered global finance.

TO LEARN MORE

UNCTAD Trade and Development Report 2008, Chapter III *International capital flows, current-account balances and development finance*, UNCTAD/TDR/2008

Contribution by the UNCTAD Secretariat to G20 Working Group on the Reform of the International Monetary System (Subgroup I: Capital Flow Management), May 2011

Contribution by the UNCTAD Secretariat to G20 Working Group on the Reform of the International Monetary System (Subgroup I: Capital Flow Management), March 2011

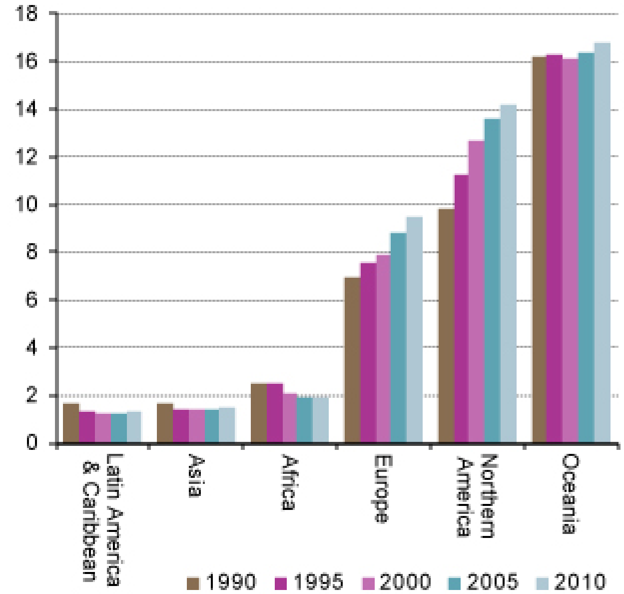
1.3 Migration and migrant's remittances

Cross-border migration has been on the rise since the 1990s in many countries and regions. While traditional immigration countries of the past include the United States, Canada, Australia and New Zealand, some countries in Western Europe that had previously seen net emigration turned into immigration countries. The former Soviet Union and Eastern Europe have been a leading source region since the 1990s. Prominent South–South migration flows occur from South Asia to the Gulf region and in Southern Africa.

Compared with trade and financial integration, cross-border migration plays a lesser role in the globalization process, as immigration remains highly restricted in most countries. This contrasts with an earlier era of globalization from the mid-nineteenth century until the First World War, when world population grew only at about half the rate of the post-Second World War period.

Share of international migrant stock in population by region, 1990-2010

(Percentage of population)



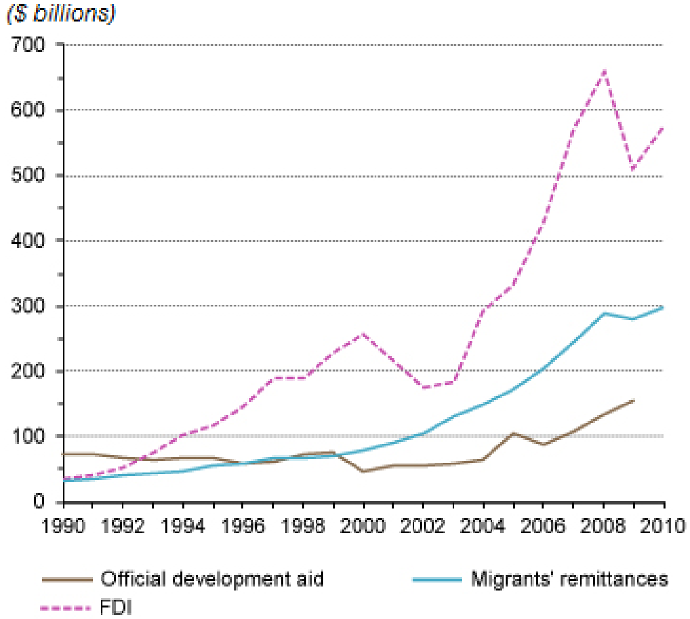
Source: UN DESA Population Division, *Trends in International Migrant Stock: The 2008 Revision*

In the OECD Organization for Economic Cooperation and Development area as a whole, 19.4 per cent of immigrants have a tertiary level of education and the rate is higher for the foreign born than for the native born. This holds for most individual OECD countries. Similarly, the share of people with no or low educational attainment is higher for immigrants than for the native born.

The impact of the global crisis on migration flows remains uncertain. In principle, despite its global reach, countries that were especially hard hit by the crisis may experience heightened pressures for emigration (push). However, sluggish recovery in developed countries that are traditionally prominent destinations of migration flows may fall behind in terms of their relative attractiveness or see the introduction of measures pertaining to the immigration of foreign workers in view of high unemployment (pull). Providing yet another indication of the ongoing shift in global balance, the European crisis has triggered sizeable migration flows from European crisis countries towards fast-growing developing economies.

Migrant remittances and financial flows to developing economies, 1990-2010

($ billions)



Source: UNCTAD secretariat calculations, based on UNCTADstat

It is common for migrants to retain links to their home countries, supporting family members left behind through cash- or in-kind transfers in particular. Migrant remittances to developing countries have seen a more than tenfold increase between 1990 and 2010, reaching $328 billion. The staggering rise may be partly a reflection of improved tracking and recording of such flows. And it may partly reflect a shift from informal to formal channels induced by lower costs of remittance transfer. Even today, however, the proportion of remittances transferred through informal channels or not surpassing minimum thresholds for official recording likely remains large. In any case, migrant remittances have become an important source of foreign exchange earnings for many developing and transition economies. Already by 1996, remittances had eclipsed official development assistance (ODA) in that role, becoming the second-most important source of foreign exchange behind net FDI flows, and a more stable one than the latter.

Migrant remittances are concentrated in a relatively small number of recipient countries: 10 countries account for half of total remittances, and the four largest recipients for more than a third; with India, China, Mexico and Philippines ranking top in terms of dollar volume of remittances.

From a development perspective, it is more instructive to consider remittances relative to recipient countries' income, for remittances have a relatively large weight in many smaller – and mainly low-income – economies. By 2010, the share of inward remittance flows in GDP in excess of 10 per cent included a group of 21 developing and transition economies. These countries are concentrated in Eastern Europe and CIS and among island States in the Caribbean Sea, the Atlantic Ocean and Pacific Ocean.

Remittances may serve to support various developmental ends, ranging from poverty alleviation to the funding of small enterprises. Countries where remittances account for such a considerable share of GDP are particularly vulnerable to recession in the main immigration economies (i.e. countries in the European Union and the Gulf Cooperation Council, the Russian Federation and the United States).

The global crisis had an immediate impact on migrant remittances. A 6 per cent decline was registered for 2009, following years of double-digit growth prior to 2008. Recovery started in 2010

Top fifteen remittance-receiving developing economies in 2010

($ billions and percentage of GDP)

Economy	Total remittances		% of GDP	
	2010	Growth (%) 00-10	2010	Growth (%) 00-10
India	55.00	5.32	3.39	0.79
China	51.00	8.05	0.87	2.21
Mexico	22.57	3.81	2.20	2.07
Philippines	21.31	3.66	11.31	0.09
Bangladesh	11.05	6.30	11.11	3.52
Nigeria	9.97	9.39	4.49	3.16
Pakistan	9.41	6.54	5.32	2.97
Lebanon	8.18	5.02	21.07	2.23
Egypt	7.68	4.37	3.58	1.34
Viet Nam	7.22	4.96	7.27	0.54
Indonesia	7.14	7.97	1.01	2.72
Morocco	6.45	3.71	7.09	0.23
Brazil	4.28	3.51	0.21	-1.31
Guatemala	4.26	6.84	10.36	3.63
Colombia	3.94	3.14	1.40	-1.11

Source: UNCTAD secretariat calculations, based on *UNCTADstat*

Highlights

- Cross-border migration has been on the rise in many countries and regions, though generally lagging other globalization trends;
- Migrant remittances to developing countries witnessed a near tenfold increase between 1990 and 2008;
- Remittances can be an important source of foreign exchange earnings;
- The global crisis impacted migrant remittances too; recovery is under way.

TO LEARN MORE

Report of the Expert Meeting on Maximizing the Development Impact of Remittances, TD/B/C.I/EM.4/3

Impact of remittances on poverty in developing countries, UNCTAD/DITC/TNCD/2010/8

Maximizing the development impact of remittances, TD/B/C.I/EM.4/2

UNCTAD Trade and Development Report 2009, Chapter I *The Impact of the Global Crisis and the Short Term Policy Responses*: C. *The ramification of the spreading crisis: Migrants' remittances*, UNCTAD/TDR/2009

1.4 Policy recommendations

Recent decades saw an acceleration of economic globalization processes that ran well ahead of existing global governance arrangements. The resulting tension, together with an unwarranted faith in the self-regulation of markets, created a hazardous global environment that ultimately ushered in the cataclysmic events of 2008–2009. While the epicentre of the financial meltdown was in the developed world, developing countries, which have increasingly integrated into the global economy, got hit as innocent bystanders as global contagion unfolded. Yet, the crisis also marked an acceleration regarding the secular shift in the balance of the global economy, while the share of developing countries in the global economy increased significantly. The message is clear: Global governance reform needs to catch up with globalization – or risk a backlash. Globalization is at the crossroads: in order to continue in a safe manner, the process needs to be controlled and managed more wisely.

A tension appears when ever-deeper global economic integration is accompanied by insufficient global governance. In a fully closed economy it is within the sovereign government's powers to shape the country's economic performance, though strictly within the boundaries of its economy's own means. Globalization offers many opportunities and the potential for vast mutual gains from interaction. However, globalization also poses daunting challenges and constraints. Openness inevitably involves some loss in national policy space and in scope for deliberate national policies that are well attuned to national conditions and requirements. Global governance needs to ensure a sound balance between national policy space and international policy cooperation as well as overall policy coherence.

As global governance has failed to keep step with accelerated economic globalization, the balance between markets and governments has shifted in favour of the market. Contrary to certain ideological presuppositions, this is not an unquestionably positive development. Markets not only undersupply public goods and fail in the presence of externalities or imperfect information. In reality, markets also rarely meet the ideal form of perfect competition, featuring the absence of market power, from which the famous postulate about the welfare-enhancing powers of the "invisible hand" is derived.

Globally, despite competition being global today in some key industries, a small number of large global corporations–traditionally originating from developed countries–typically dominate in the marketplace. This is also true in the global financial area.

A related asymmetry in economic power exists between larger and smaller countries, with developing countries traditionally falling in the latter category. While the processes of globalization and national policies may mutually codetermine each other, smaller countries are less able to shape globalization trends and global economic governance, while at the same time being more influenced and constrained by the external environment created by globalization.

Both at the global level and within many national economies, globalization has also contributed to a shift in economic power that has increased capital bargaining power at the expense of labour. One of the reasons was that the increased international mobility of products and factors – the core of the whole process – was very uneven, with capital and goods and services having become much more mobile globally than labour. As a result, the threat of delocalization became a powerful argument for wage moderation. In addition, competition among developing countries for foreign direct investment (FDI) can give rise to a race to the bottom through concessions made to transnational corporations, including a relaxation of labour regulations.

All these factors determine whether potential mutual benefits are realized in the first place, and how they are shared, both globally and within nations. Especially in democracies, where governments are accountable to national parliaments and electorates, the loss of national policy space arising with economic integration is a fundamental conflict.

In the past decade, for lack of proper global governance, the unbalanced and hazardous global economic environment encouraged many developing countries to favour defensive macroeconomic policies, featuring the spectacular rise in international reserves (or self-insurance boom).

Other possible unilateral responses to overcoming the above conflicts and rectifying the resulting imbalance between markets and government could include re-erecting or raising protective barriers, be it in the form of tariffs or capital controls, for instance. In a globally integrated economy, the international coordination of policies is essential. Global governance reform needs to catch up with globalization – or risk a backlash.

The global crisis and recent upgrading of the status of the Group of 20 (G20) have given fresh impetus to global governance reform and global cooperation. The inclusion of a group of large developing countries in the inner core of global intergovernmental policy coordination at least partly acknowledges the changing balance in the world economy between developed and developing countries. Some developing countries have grown into large economies and have are home to large global corporations.

Despite these highly welcome recent changes in global governance, the concerns of developing countries remain underrepresented globally. Global governance reform needs to progress further so as to properly reflect the shifting balance in the world economy and enable all developing countries to fully participate in and shape globalization, and fully share in the benefits. While the United Nations should remain the primary forum for discussing global issues, the gravest deficiencies in global governance currently exist in international monetary and financial arrangements. In view of the current hazardous global economic environment, safeguarding national policy place remains vital in steering development.

Highlighting the nature and extent of global interdependence and interconnectedness existing today, the global crisis of 2008–2009 and the economic havoc it wreaked continue to define some key economic challenges that policymakers are struggling with in returning their national – but interdependent – economies to sustainable growth. Globalization is at the crossroads: in order to continue in a safe manner, the process needs to be controlled and managed more wisely.

An inherent tension exists between economic integration and insufficient global governance;

The balance between markets and governments has shifted in favour of the market;

In democracies the loss of national policy space arising with economic integration is a fundamental conflict;

The upgraded status of the G20 has given fresh impetus to global governance reform;

Inclusion of a group of developing countries in the inner core of global intergovernmental policy coordination acknowledges the reality of a changing balance in the world economy;

The concerns of developing countries remain underrepresented;

Safeguarding national policy space remains vital; Global governance reform needs to make further progress.

2 GLOBAL IMBALANCES, CRISIS AND THE LACK OF GLOBAL GOVERNANCE

GROSS DOMESTIC PRODUCT

Vast disparities in per capita income levels continue to exist around the world. The catching-up process of the developing world, which has broadened since 2003, received a boost since the global crisis as key developed countries have struggled to recover from it. These post-crisis developments are not fully benign, since the hesitant and fragile recovery in developed countries risks holding back or even undermining income growth in developing countries. The fast shifting balance in the world economy is reflected in the decline in the share of developed countries in global gross domestic product (GDP).

EMPLOYMENT AND UNEMPLOYMENT

Widespread unemployment and underemployment in the global economy continues to present the most pressing social and economic problem of our time. The situation was made worse by the global crisis. While many developing countries merely suffered a temporary deterioration, the lasting labour market impact in major developed countries poses fresh challenges and risks to the continuation of positive runs in job creation and poverty reduction in the developing world. Ill-guided policies directed at the labour-market legacies of the crisis in developed countries risk global spillovers that could destabilize developing countries.

CURRENT ACCOUNT IMBALANCES

Large current account balances have been at the center of long-standing international economic policy debates regarding global imbalances. The United States has run persistent current account deficits since the early 1990s, with net private capital inflows as well as official inflows (i.e. international reserve accumulation by other countries) as the counterpart. A small and only partly evolving group of developed and developing countries features prominently on the surplus side of global imbalances. Current account imbalances may arise for a number of reasons and are not indicative per se of a systemic problem that needs coordinated intervention. Rather, it is the loss of competitiveness at the national level that causes an unsustainable current account deficit.

MISALIGNED EXCHANGES RATES

Countries' competitiveness positions are primarily shaped by trends in unit-labour costs and exchange rates. Since the end of the multilateral Bretton Woods exchange rate system, non-orderly floating of currencies has prevailed, featuring large exchange rate swings and persistent misalignments. Current account imbalances caused by unbalanced competitiveness positions matter both at the regional and global levels. Unbalanced competitiveness positions are the underlying cause of the ongoing European crisis. In general, exchange rate movements that are persistently inconsistent with achieving balanced global competitiveness positions provide strong evidence for the need to coordinate global currency markets.

INTEREST RATES, VOLATILE CAPITAL FLOWS AND EXCHANGE RATE INSTABILITY

Traditional theory holds that floating exchange rates insulate countries against external shocks and enlarge national policy space. Driven by stabilizing currency market speculation, movements in nominal exchange rates are held to compensate for inflation and/or interest rate differentials, so as to avoid any build-up of unbalanced competitiveness and trade positions. Actual experiences speak another language altogether. In the absence of proper global governance, global finance has become dominated by herd-like short-term risk-reward calculations that may ignore the gradual build-up of economic imbalances and related financial fragilities for a long time. The authorities of target currencies in the developing world are facing difficult choices.

FINANCIAL LIBERALIZATION AND THE FINANCIALIZATION OF COMMODITY MARKETS

Sizeable commodity price volatility can have adverse effects at both the macroeconomic and microeconomic levels. The wide price fluctuations observed over the last decade coincided with major shifts in commodity market fundamentals, as well as with increased trading by financial investors in commodity derivatives markets. The financialization of commodity markets has accelerated significantly since about 2002–2004 and most probably reduced the reliability of price signals emanating from commodity futures exchanges. Greater market transparency and tighter regulatory measures are called for to contain the price impact of financial investors and the associated risk of price bubbles.

GLOBAL REBALANCING AND RECOVERY CONTRIBUTIONS

After briefly shrinking during the global crisis, global imbalances in trade and financial flows have made a comeback during the recovery and remain large as of today. While the balances of the main surplus and deficit countries or regions are below their pre-crisis peak, there has been no fundamental change in the global imbalance constellation. Developing countries at large have contributed disproportionately to global rebalancing and recovery, while an increasing number of them have reached the point where rising current account deficits signal future risks of fragility and crisis.

2.1 Gross domestic product

The per capita level of gross domestic product (GDP) provides a rough summary indicator of the average living standard.

Vast disparities in GDP per levels persist around the world. Average per capita incomes in developed countries exceed average per capita incomes in developing countries by a factor of nearly 11, and disparities are much starker still between the richest and poorest countries.

While the income gap between developed and developing countries has declined in relative terms, it continues to widen in absolute terms, reaching $35,700 in current dollars in 2010.

Convergence of living standards around the world requires that per capita incomes grow faster in poor countries than in rich ones. A comparison of the evolution of growth trends of real GDP thus indicates whether the poor are catching up with the rich or not.

The global boom of 2003–2007 generally reversed trends in place in the prior two decades that saw per capita incomes in the developing countries of Africa, the Americas, Western Asia and Oceania (and transition economies the second half of this period) grow at very low or even negative rates.

Gross domestic product per capita by region, 1992-2010

(Percentage and $)

Region	Real growth (%)		Nominal ($)
	92-00	00 -10	2010
World	**1.7**	**1.6**	**9,178**
Developing economies	*3.0*	*4.6*	*3,703*
Africa	0.7	2.7	1,676
America	1.4	2.3	8,558
Asia	4.3	5.9	3,508
Oceania	-0.4	0.7	3,313
LDCs	1.8	4.8	737
Transition economies	*-1.7*	*5.8*	*6,989*
Developed economies	*2.3*	*1.0*	*39,445*

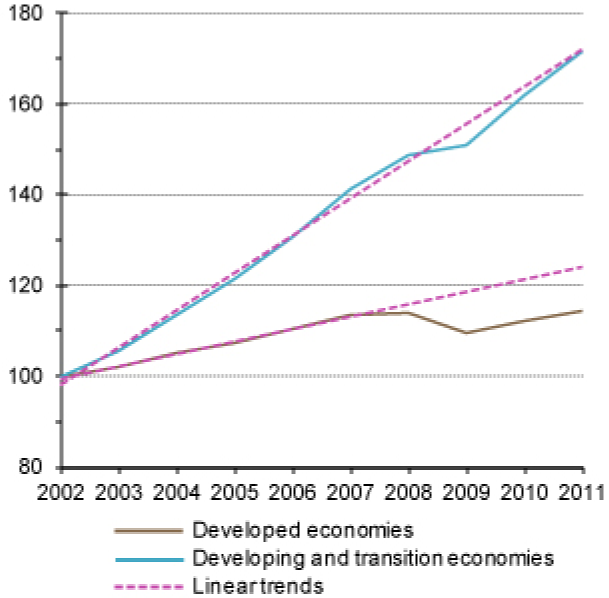
Source: UNCTAD secretariat calculations, based on *UNCTADstat*

In the last 20 years of the twentieth century only Eastern, Southern, and South-Eastern Asia had experienced catching up, and at a fast rate in their cases.

Catching up has broadened since 2003 and may have accelerated further since the global crisis, albeit in a less benign way, since it is owing to a falling off in growth in developed countries that also risks holding back income growth in developing countries.

Real gross domestic product at market prices, 2002–2011

(Index numbers, 2002 = 100)



Source: UNCTAD secretariat calculations, based on UN/DESA, *National Accounts Main Aggregates* database and *World Economic Situation and Prospects (WESP) 2011; ECLAC (2011)*; OECD (2011); and national sources.

At its peak, the global crisis severely affected economies around the globe. Its impact has proved more lasting in the case of key developed countries, however.

Led by East Asia, developing countries at large have rebounded more vigorously from the global calamity. To begin with, not all developing countries had experienced the crisis as an absolute decline in income levels but as a slowdown in their rate of growth.

Furthermore, only a small group of transition economies concentrated in Eastern Europe suffered grave declines in absolute income levels.

These economies also seem to find it similarly hard to recoup lost ground, as do the developed countries that were at the heart of the global crisis. Meanwhile, developing countries at large have not only regained and exceeded pre-crisis GDP levels, but also returned to their pre-crisis growth path.

This contrasts with the situation in developed countries. Barely regaining their pre-crisis income levels, as a group, developed countries continue to operate well below their pre-crisis growth trajectory. The situation is most critical today in those European countries that share the euro.

The crisis has not changed the fact that the bulk of global income, as expressed by world GDP, remains in the hands of the developed countries, but their share has shrunk sharply from 70 per cent in 1980 to 64 per cent in 2010. The balance in the global economy is shifting fast.

Highlights

- Catching up of developing countries has broadened since 2003 and accelerated recently;
- Large scope for catching up still exists as vast disparities in per capita income levels persist around the world;
- The global economy experienced high GDP growth rates in the mid-2000s but crisis left a lasting impact, with problems concentrated in key developed countries;
- The global crisis has accentuated the shifting balance in the world economy.

To learn more

UNCTAD Trade and Development Report 2011, Chapter I *Current Trends and Issues in the World Economy*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2010, Chapter I *After the Global Crisis: An Uneven and Fragile Recovery*, UNCTAD/TDR/2010

UNCTAD Trade and Development Report 2009, Chapter I *The Impact of the Global Crisis and the Short-term Policy Response*, UNCTAD/TDR/2009

UNCTAD Trade and Development Report 2008, Chapter I *Current Trends and Issues in the World Economy*, UNCTAD/TDR/2008

UNCTAD Trade and Development Report 2007, Chapter I *Current Issues in the World Economy*, UNCTAD/TDR/2007

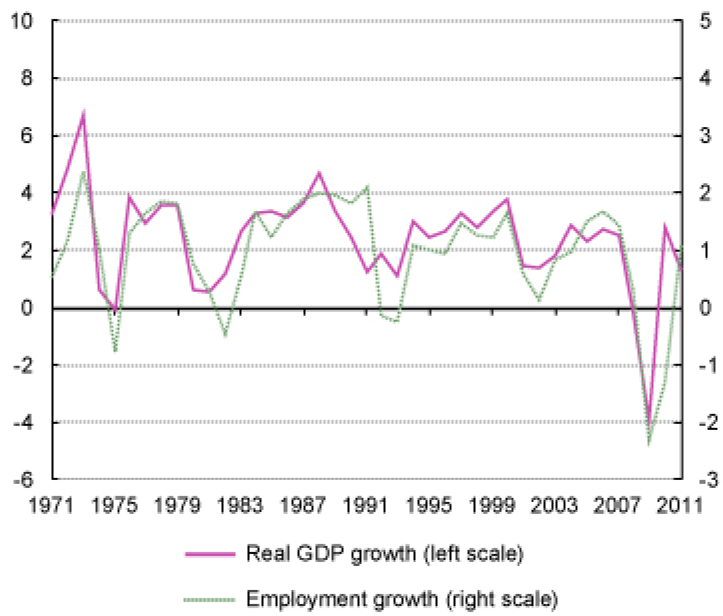
2.2 Employment and unemployment

Work represents – for the majority of the population – the main source of personal income, the other sources being the revenues from capital and social transfers. For working-age populations, employment is also essential for social inclusion. As productivity growth and structural change, featuring job destruction, are inherent aspects of development, the timely creation of jobs in sufficient numbers is a permanent challenge.

Job creation is of even more vital importance when population growth in conjunction with demographic and social factors yield a growing labour force ready for employment – or at risk of raising the reserve of unemployed or underemployed workers. Widespread unemployment and underemployment in the global economy continues to present the most pressing social and economic problem of our time because it is closely related to poverty, on the one hand, and social peace and political stability on the other.

Growth of employment and real gross domestic product in developed economies, 1971–2011

(Percentage)



In developed economies, there is a strong link between GDP growth and employment creation. By contrast, in developing economies, changes in informal employment and self-employment dampen the effects of growth cycles on formal. In the absence of social safety nets fulfilling this role in developed economies, in developing economies movements into and out of informal, low-quality employment is typically cushioning employment in the formal economy as captured in official statistics, if at all.

The segmentation of the labour structure in developing countries reflects the dualism that characterizes their economic structures: The coexistence of a modern sector with relatively high productivity and a sluggish traditional sector with low productivity.

Moreover, the segmentation also highlights the importance of the quality of employment created; above and beyond the sheer quantity of, perhaps, precarious and poorly paid jobs feeding the ranks of the working poor.

While unemployment rates always have to be assessed in conjunction with labour force and employment data in both developed and developing countries. Classification of workers by employment status underlines that the self-employed and contributing family members continue to play a far more prominent role in developing countries.

Given the pivotal importance of GDP growth as contributing force behind job creation and the prevalence of unemployment or underemployment in economies in general, events such as the collapse in GDP growth in the global crisis are bound to have a major impact on the employment and labour market situation too. It turns out that countries that achieved a quick and full recovery from the crisis generally only experienced a temporary deterioration in the employment and labour market situation. Until now, this has proved true for developing countries at large, although regional disparities exist. The global crisis has temporarily dented the favourable trends established during the global boom of 2003–2007, but not derailed the benign developments. In principle, developing countries are thus generally facing the same kinds of challenges regarding job creation and poverty reduction as prior to the crisis, their principal problem being that of deficient productive capacity rather than its underutilization.

Real gross domestic product and employment by region, 2003–2011

(Annual average growth rate)

Region	03-08 GDP	03-08 Employment	09-10 GDP	09-10 Employment	2011 GDP	2011 Employment
Developing economies	**7.0**	**1.9**	**6.4**	**1.4**	**6.0**	**..**
East Asia	8.9	0.6	8.6	0.4	7.6	2.0
South Asia	8.0	2.5	7.5	1.4	6.5	2.2
South-East Asia	6.0	2.0	5.5	2.3	4.8	2.7
West Asia	6.3	2.3	5.2	3.6	6.6	4.3
North Africa [a]	5.1	4.2	4.8	2.3	-0.5	1.3
Sub-Saharan Africa	6.4	3.0	5.4	2.8	4.7	..
Latin America and the Caribbean	4.8	2.8	4.1	1.7	4.3	1.9
Transition economies	**7.4**	**1.2**	**5.4**	**-0.5**	**4.5**	**1.0**
Developed economies	**2.3**	**1.3**	**1.4**	**-2.4**	**1.4**	**2.4**
North America	2.4	1.3	1.5	-2.0	1.7	0.7
Asia	1.6	0.3	0.8	-0.8	-0.7	-2.1
Europe	2.4	1.4	1.5	-1.0	1.6	0.2

Source: UNCTAD, *TDR 2011* (Table 1.1) and *TDR 2010* (Chart 3.3), March 2012 update

Note: [a] North Africa excluding Sudan.

The situation is starkly different in major developed economies, where actual GDP is falling well short of potential output and large negative output persist. In these economies the short-run challenge remains to fully undo the crisis impact on GDP and employment by appropriate macroeconomic policies. In case of failure, crisis-induced unemployment would in due course be classified as structural, which would become true to the extent that a deterioration of human capital (a loss of skills and morale due to long-term unemployment) and lack of physical capital (for lack of investment) artificially creates a state of deficient productive capacity resembling the situation in developing countries. Labour market and welfare system reforms designed to accentuate downward wage pressures would not solve the underlying problem of deficiency of effective demand in these countries, but make them also more similar to developing countries in terms of a widespread prevalence of working poor. It would also tend to make these economies more export reliant and focused on external competitiveness.

The fragile and unfinished recovery of major developed economies affects developing economies as the former represent critical export markets for the latter. Ill-guided policies in developed countries pose new and additional challenges in developing countries.

Highlights

- There is a strong link between GDP growth and employment creation;
- The relative role of social safety nets and informal employment varies in developed vs. developing economies, and stark differences in employment status of the labour force persist;
- The employment impact of the global crisis has proved temporary in many developing economies, but lasting in major developed economies;
- The underlying problem of insufficient effective demand and possible ill-guided policies pursued in developed economies cause spillover effects in the developing world.

To learn more

UNCTAD Trade and Development Report 2010, Chapter II *Potential Employment Effects of a Global Rebalancing,* UNCTAD/TDR/2010

UNCTAD Trade and Development Report 2010, Chapter III *Macroeconomic Aspects of Job Creation and Unemployment*, UNCTAD/TDR/2010

UNCTAD Trade and Development Report 2010, Chapter IV *Structural Change and Employment Creation in Developing Countries*, UNCTAD/TDR/2010

UNCTAD Trade and Development Report 2010, Chapter V *Revising the Policy Framework for Sustained Growth, Employment Creation and Poverty Reduction*, UNCTAD/TDR/2010

Employment Dimension of Trade Liberalization with China: Analysis of the Case of Indonesia with Dynamic Social Accounting Matrix, UNCTAD/DITC/TNCD/2011/4

Trade and Employment: From Myths to Facts, International Labour Office, ISBN: 978-92-2-125320-4

Development Challenges Facing LDCs in the Coming Decade, UNCTAD Policy Briefs, No. 20(f), 10/05/2011

2.3 Current account imbalances

Countries running a current surplus must by necessity either experience net private capital outflows or accumulate international reserves (i.e. official outflows). Similarly, countries running a current account deficit must by necessity either experience net financial inflows or run down its international reserve holdings. The United States provides a special case because the United States dollar serves as the world's key reserve currency. The large and persistent United States current account deficits since the 1990s did not involve any run-down of the country's international reserves. Rather, the equally large net capital inflows into the United States were partly net private inflows and partly official inflows, the latter being other countries' accumulation of international reserves held in United States dollar assets.

When global imbalances and large United States current account deficits first emerged in the 1980s, the main surplus countries or regions were Japan and Western Europe – mainly Germany – also reflecting the fact that the rich industrialized countries represented more than 70 per cent of global trade at the time. In the first half of the decade, the United States recovered more strongly from the second oil price shock and the dollar appreciated strongly. The United States current account deficit then briefly disappeared by 1990 as the dollar depreciated strongly after the Plaza Accord of 1985, and GDP gross domestic product growth in Japan and Western Europe picked up in the second half of the decade.

The (re-) emergence of rising and persistent United States current account deficits since 1991 at first featured mainly the same surplus countries or regions as their counterpart. In both Japan and the European countries preparing to adopt the euro as their currency GDP growth was very sluggish during much of the 1990s while the United States dollar experienced a sizeable appreciation over the course of the decade. Imbalances among these developed countries or regions continued or increased until the global crisis. Apart from Germany, the Netherlands and Switzerland feature prominently among rich European countries with sizeable, persistent surpluses.

The global constellation became more complex at the end of the 1990s.

In reaction to emerging market crises in East Asia in the late 1990s and Latin America in the early 2000s, many developing countries started running current account surpluses; with Eastern Europe as the exception. Mirroring a marked increase in the United States deficit, in the aggregate, the developing world's deficit shifted into surplus. Capital exports from developing countries contradict traditional development theory, which predicts that capital should flow from rich to poor countries.

Current account, net, by region, 1980-2010

(Percentage of GDP)

Region	1980	1990	1995	2000	2005	2010
Developing economies	**1.2**	**0.4**	**-1.6**	**1.4**	**4.6**	**2.4**
Africa	*1.5*	*0.7*	*-2.7*	*2.8*	*6.1*	*0.4*
America	*-4.1*	*-0.4*	*-2.1*	*-2.3*	*1.3*	*-1.1*
Asia	*4.2*	*0.6*	*-1.2*	*3.1*	*5.6*	*3.9*
LDCs	-6.0	-4.0	-4.2	-2.5	-2.5	-4.3
Transition economies	-3.2	-2.8	0.3	11.8	7.6	3.4
Developed economies	-1.0	-0.6	0.1	-1.3	-1.5	-0.6

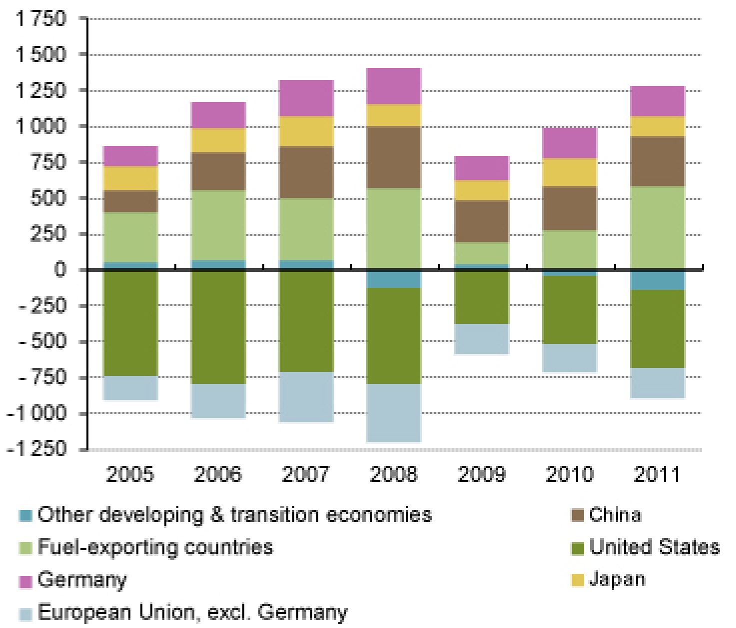
Source: UNCTAD secretariat calculations, based on *UNCTADstat*

While a sizeable Sino-American trade imbalance had built up earlier in the 1990s, China only emerged as a significant contributor to global imbalances in 2003. The commodity price boom of the 2000s then added fuel-exporting economies to the list of surplus countries.

All along, the United States offset the deflationary forces originating in much of the rest of the world through widespread export orientation by encouraging borrowing and spending, particularly by private households. The resulting internal imbalances in the United States household and financial sectors began to implode as the property bubble burst in 2006

Current account balance of selected economies, 2005–2011

($ billions)



Source: UNCTAD secretariat calculations, based on UN DESA, *National Accounts Main Aggregates database*, *WESP 2011: Mid-year update*; and IMF, WEO database

In current dollar terms, global current account imbalances peaked in 2007–2008, shrank in 2009 – when the volume and value of global trade declined sharply – and widened again in 2010–2011. The plunge and renewed surge in commodity prices – especially of oil – was a major factor in this. While the balances of the main surplus and deficit countries or regions are below their pre-crisis peak in both current dollar terms and as a per cent of world GDP, there has been no fundamental change in the imbalance constellation.

Current account imbalances may arise for a number of reasons. Sharp commodity price swings, as witnessed over the last decade, provide one prominent reason, as the spending adjustment in exporting and importing countries typically lags behind changing export revenues or import bills, respectively. Another reason may be that a country begins to serve as a major hub for foreign firms in producing manufactures on a large scale while its population may still lack the earning capacity to consume imports on a scale sufficient to balance out its surging exports (e.g. China). A third reason may arise when a country suffers from protracted domestic demand stagnation and comes to rely on exports for its growth (e.g. Japan and Germany). Finally, current account imbalances may result from the loss of competitiveness at the national level. While international tensions may arise for any of these reasons, current account imbalances per se are not indicative of a systemic problem that needs coordinated intervention. This would be the case, however, in the two last cases, in which changes in domestic demand and in real exchange rates may be needed. Through international cooperation, these changes may be achieved without incurring in a deflationary bias: Surplus countries should expand their domestic demand and cooperate in a smooth adjustment of real exchange rates.

Highlights

- Persistent and large current account imbalances built up prior to the global crisis;
- Imbalances are concentrated in a small group of countries;
- The United States, the world's key reserve currency issuer, is the largest deficit country;
- Initially other developed countries were the main surplus countries;
- Developing countries joined this group in the late 1990s, with China appearing as a globally significant contributor only since 2003;
- Capital exports from developing countries contradict orthodox development theory;
- While the balances of the main surplus and deficit countries or regions are below their pre-crisis peak, there has been no fundamental change in the imbalance constellation;
- Current account imbalances may arise for a number of reasons;
- Current account imbalances caused by insufficient domestic demand in surplus countries and a loss of competitiveness in deficit countries require international coordination for a pro-growth rebalancing.

TO LEARN MORE

UNCTAD Trade and Development Report 2011, Chapter I *Current Trends and Issues in the World Economy*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2008, Chapter III *International Capital Flows, Current-account Balances and Development Finance*, UNCTAD/TDR/2008

Building a global monetary system: the door opens for new ideas, UNCTAD Policy Briefs, No. 17, 17/11/2010

2.4 Misaligned exchange rates

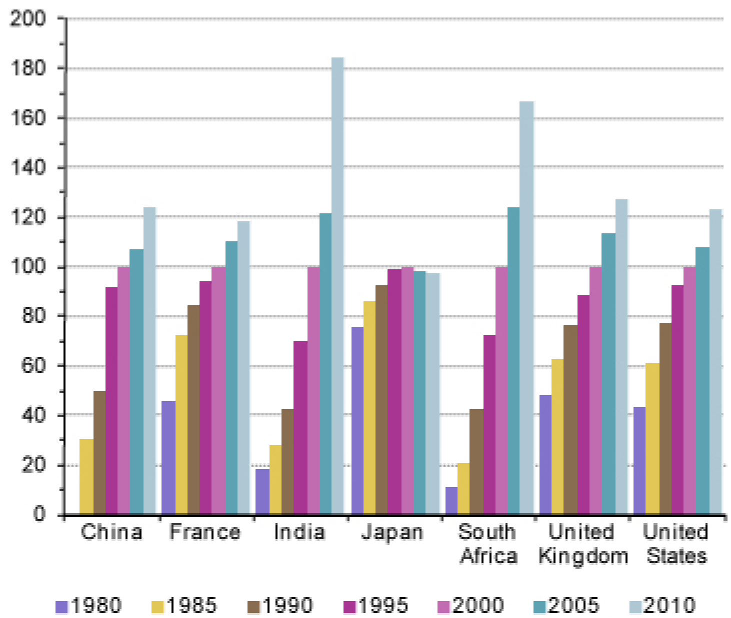
The evolution of competitiveness at the national level is mainly shaped by two factors: first, the rate of increase in wages (and other costs) relative to the rate of productivity growth and, second, the nominal exchange rate. While wage increases per se raise production costs and reduce competitiveness, productivity growth has the opposite effect. If both wages and productivity grow at the same rate, unit-labour costs stay steady; and so would external competitiveness assuming that profit margins, indirect taxes and other related factors remain unchanged too. Exchange rate changes broadly affect the competitiveness of all producers of tradable goods and services in a country relative to producers in trading partners by changing the foreign currency price of home exports and domestic currency price of foreign imports.

Since the breakdown of the multilateral Bretton Woods system of pegged but adjustable exchange rates in the early 1970s, currencies have entered a new era of non-orderly floating exchange rates, leaving it at countries' discretion to choose their particular exchange rate regime. Members of today's European Union established a new regional system of pegged but adjustable exchange rates, and at the end of the 1990s, some of them permanently fixed their exchange rates and adopted the euro as their common currency. Among developing countries, too, many have chosen to peg their currencies to or stabilize them against some anchor currencies, most prominently the United States dollar, at least during some of the time.

Movements in nominal exchange rates may not properly reflect corresponding changes in countries' competitiveness positions, which are also affected by inflation differentials. Except for changes in profit margins and indirect taxes, for example, inflation differentials in turn are mainly driven by trends in relative unit labour costs. Inflation differentials and divergent trends in unit-labour costs have been sizeable since the 1970s.

Trends of consumer price index in selected economies, 1980-2010

(Index numbers, 2000=100)



Source: UNCTAD secretariat calculations, based on ILO, *LABORSTA;* OECD, *OECD.Stat Extracts*; IMF, *IFS*; and national sources

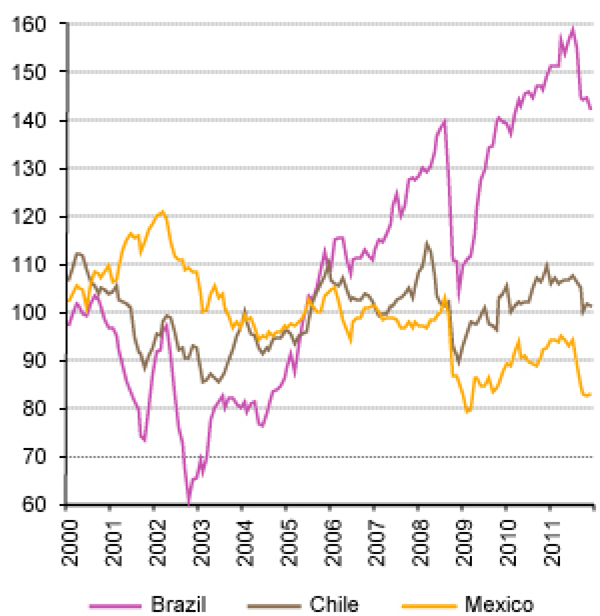
Correcting movements in nominal exchange rates for inflation differentials yields real exchange rates, which are more accurate indicators of changes in competitiveness.

A still superior indicator of the overall competitiveness of a country relies on measures of real effective exchange rates (REER). The term "effective" means that exchange rate changes are not measured against one particular currency, but instead use an average index of a whole basket of currencies, each weighted according to the issuing countries' respective importance as a trade partner.

According to the REER measure, substantial changes in competitiveness positions have occurred since 2000. In principle, if the emergence of unsustainable current account imbalances is to be avoided and benign rebalancing the aim, countries with deficit positions should see their external competitiveness improve – and vice versa. Since 2007, there has been a sizeable depreciation in the REER of two large current account deficit countries, the United Kingdom and the United States, which seems to be in line with rebalancing requirements. The same holds for the marked rise in China's REER since 2005. By contrast, significant improvement in Japan's competitiveness up to 2008, even accelerating in the years 2005–2007, was inconsistent with the country's surplus position. Equally inconsistent with rebalancing requirements, Germany has been awarded a significant improvement in competitiveness in the context of the European crisis. The fact that the euro area's current account position is nearly balanced does not suggest otherwise, but implies that competitiveness positions inside the currency area may be seriously out of kilter.

Real effective exchange rates of selected developing economies, January 2000-December 2011

(Index numbers, 2005=100, CPI based)



Source: UNCTAD secretariat calculations, based on BIS, *Effective Exchange Rate Indices* database

Developing countries have often experienced even greater swings in competitiveness over the last decade. For instance, Brazil's REER rose strongly until mid-2008, plunged at the peak of the crisis, only to resume its rise to new heights until mid-2011, when a new reversal started. Similar exchange rate trends have been observed in other developing countries, a number of which have meanwhile drifted into sizeable current account deficit positions which may herald future instabilities. The currencies of Chile, Mexico, India, the Republic of Korea, the Russian Federation, South Africa and Turkey, for example, underwent a significant appreciation in their REER following the recovery from the crisis; until renewed stresses arose in mid-2011.

Renewed instabilities are mainly related to the European crisis. The euro area provides a special case in which competitiveness positions among members can no longer change owing to exchange rate changes; trends in relative unit-labour costs determine competitiveness positions inside a currency union. To avoid dislocations in intraregional competitiveness positions, national wage trends need to follow an implicit norm that is the sum of national productivity growth and the agreed union-wide inflation rate (defined by the European Central Bank as "below but close to 2 per cent").

Countries in the periphery that are experiencing severe public-debt crises today departed from this norm somewhat in the upward direction, whereas Germany, the economy with the largest trade surplus within the euro area, missed the implicit norm most widely, but in a downward direction. As a result, over time Germany experienced cumulative competitiveness gains over its European partners. Widening current account imbalances inside the euro area by necessity also had their financial counterparts. In some cases, lending flows towards current account deficit countries caused property bubbles. The bursting of those bubbles in the context of the global crisis resulted in private debt overhands that first triggered banking crises and eventually turned into sovereign debt crises. The build-up of unsustainable current account positions fosters financial fragilities that tend to end in tears, whether at the global or regional level, whether in the developing or developed world.

In conclusion, misaligned exchange rates affect competitiveness positions and cause current account imbalances, which matter both at the regional and global levels. Inside currency unions, relative trends in unit-labour costs are the key. In general, exchange rate movements that are persistently inconsistent with achieving balanced global competitiveness positions provide strong evidence for the need to coordinate global currency markets.

Highlights

- Countries' competitiveness positions are shaped by trends in unit-labour costs and exchange rates;
- Since the end of the multilateral Bretton Woods exchange rate system, non-orderly floating has prevailed, featuring large exchange rate swings and persistent misalignments;
- Current account imbalances caused by unbalanced competitiveness positions matter both at the regional and global levels;
- Exchange rate movements that are persistently inconsistent with achieving balanced global competitiveness positions provide strong evidence for the need to coordinate global currency markets.

To learn more

UNCTAD Trade and Development Report 2011, Chapter VI *The Global Monetary Order and the International Trading System*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2009, Chapter IV *Reform of the international monetary and financial system*, UNCTAD/TDR/2009

Global imbalances: The choice of the exchange rate-indicator is key, UNCTAD Policy Briefs, No. 19, 12/01/2011

Will we never learn? UNCTAD Policy Briefs, No. 5, 18/12/2008

2.5 Interest rates, volatile capital flows and exchange rate instability

Movements in nominal exchange rates that compensate for inflation differentials and hence keep real effective exchange rates (REERs) steady over time would also tend to keep international trade balanced and avoid the build-up of unsustainable global imbalances. This is the underlying idea behind the purchasing power parity (PPP) theory, which posits that trade imbalances would tend to correct themselves. High inflation rates would be associated with an expectation of a compensating currency depreciation, and vice versa. If floating exchange rates were behaving according to this script, they would help support stability in the world economy and avoid tensions between nations.

Experience with floating exchange rates has been altogether different. High inflation currencies often experience prolonged periods of sharp appreciation, implying that REERs are driven further and further away from fundamental equilibrium values, while competitiveness positions become seriously and lastingly distorted. In today's world of unfettered global finance, exchange rates are not primarily driven by trade flows, but by capital flows. In the absence of proper global governance, global finance has become dominated by herd-like short-term risk-reward calculations that may ignore the gradual build-up of economic imbalances and related financial fragilities for a long time – until a sudden and highly disruptive reversal eventually occurs, adding to the distortions and damage endured during the build-up phase. Especially in currency markets, the world's largest and most liquid market, financial speculation has proved highly destabilizing.

Financial markets are said to be expectations-driven. Given that the future world is inherently uncertain – uncertain in the profound sense of being non-reducible to objective probability calculations – any idea that asset prices may be firmly anchored by fundamentals at uniquely correct values is untenable. The observed restlessness and volatility of financial asset prices is one reflection of this fact. In this context, interest rates as set by central banks in the conduct of monetary policy provide important fixtures and guidance to financial markets and expectations formation.

As long as domestic policy requirements vary, there may be sizeable disparities between short-term interest rates as set by different national central banks in the world. To a large extent, interest differentials reflect inflation differentials, although interest differentials may also arise for other reasons, so that real interest rates are not uniform across the globe either. Similar differentials are observed for longer-term interest rates, which are generally less closely associated with national monetary policies than short-term rates.

Interest rate differentials invite arbitrage operations, i.e. attempts by actors to profit from price differences across different markets ("buying low, selling high"). There is an incentive to borrow money in a low-interest currency and invest that money in another high-interest currency with the aim of earning the interest differential. Given that different currencies are involved, exchange rates enter the profitability equation of this kind of arbitrage operation. More precisely, what matters are expectations about exchange rate changes over the relevant investment horizon.

Traditional (interest rate parity) theory posits that the market determines exchange rates in such a way that high interest rates are compensated for by an expectation of currency depreciation, and vice versa. In this case, there would be no opportunity to profit from interest differentials, and hence no incentive to borrow in a low-interest currency in order to invest the proceeds in a high-interest currency.

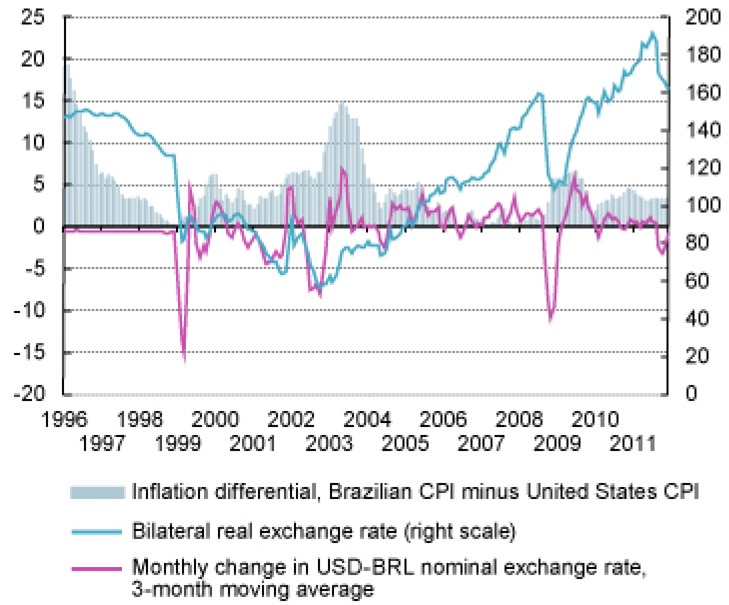
Neither is this traditional theory borne out by the facts. In practice, high-interest currencies often experience prolonged periods of sharp appreciation spurred by capital inflows. Lured by interest differentials, short-term private capital flows can be highly destabilizing.

Currency market carry trade speculation is a key driver behind destabilizing exchange rate movements. Borrowing in a low-yield (funding) currency to invest in another high-yield (target) currency tends to move the exchange rate in favour of the high-yield currency.

Carry trade speculation feeds on itself as the exchange rate movement thereby augments (rather than subtracts from) the arbitrage profit derived from interest differentials alone.

Inflation differential and nominal and real exchange rates in Brazil, January 1996-December 2011

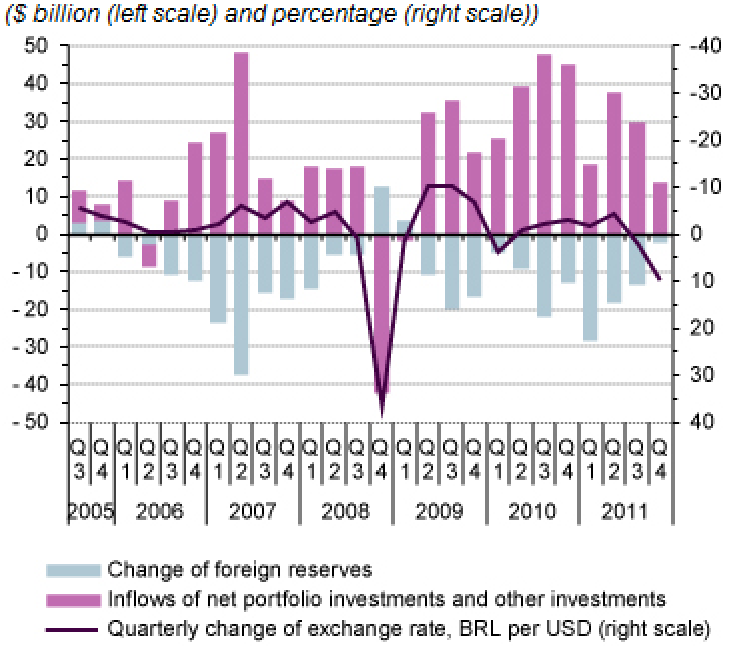
(Percentage (left scale) and index numbers 2005=100 (right scale))



Source: UNCTAD, *TDR 2011* (Chart 6.7), March 2012 update

Changes in exchange rates and reserves, and net portfolio investments of Brazil, third quarter 2005–fourth quarter 2011

($ billion (left scale) and percentage (right scale))



Source: UNCTAD, *TDR 2011* (Chart 6.3), updated March 2012

Note: A negative value of reserves means an increase in reserves (capital outflow).

A positive value of the exchange rate change represents a depreciation of the currency.

In turn, the attraction of even bigger prospective profit further fuels carry-trade speculation and reinforces the trend as more speculators jump on the band wagon (known as herding).

Again, the implication is that REERs may be driven further and further away from fundamental equilibrium values, while competitiveness positions become seriously and lastingly distorted. Volatile and unreliable capital inflows do not support but hinder sustained development and catching up.

If currency markets are left at their own devices, floating exchange rates neither insulate developing countries from external shocks nor do they guarantee sufficient policy space. Financial globalization implies a de facto loss of national policy autonomy.

External financial conditions largely determine the scope for development strategies and domestic macroeconomic policies. Highlighting existing asymmetries in the world economy, these conditions are influenced mainly by monetary policy decisions taken in the key developed countries.

The authorities of target currencies in the developing world are facing difficult choices. If floods of private capital inflows fuel asset prices and inflation expectations, hiking interest rates amounts to adding fuel to the flames. So the widely preferred policy choice features currency market intervention and reserve accumulation to stem the appreciation wind. The net effect of this response is that reserve accumulation offsets net private capital inflows in target countries' international investment positions. This may even be costly for the recipient country of hot money as the authorities effectively act as counterpart to the private carry trade. Capital controls to block undesirable short-term capital inflows provide an alternative unilateral measure. Re-regulation of global finance and the establishment of a multilateral international monetary order remain the order of the day.

Highlights

- Traditional theory posits that currency market speculation would be stabilizing and trade imbalances tend to correct themselves;
- Unfettered global finance has unleashed destabilizing currency market speculation;
- Carry trade speculation is a key driver behind destabilizing exchange rate movements;
- Currency market intervention and reserve accumulation are the preferred defensive response in the developing world subjected to fickle hot money floods and ebbs;
- Capital controls to block undesirable short-term capital inflows provide an alternative unilateral measure;
- Re-regulating global finance and establishing a multilateral international monetary order are needed for global stability.

To learn more

UNCTAD Trade and Development Report 2011, Chapter VI *The Global Monetary Order and the International Trading System*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2010, Chapter I *After the Global Crisis: An Uneven and Fragile Recovery*, UNCTAD/TDR/2010

UNCTAD Trade and Development Report 2009, Chapter IV *Reform of the International Monetary and Financial System*, UNCTAD/TDR/2009

UNCTAD Trade and Development Report 2007, Chapter I *Current Issues in the World Economy*, UNCTAD/TDR/2007

Rebuilding financial multilateralism, UNCTAD Policy Briefs, No. 4, 24/10/2008

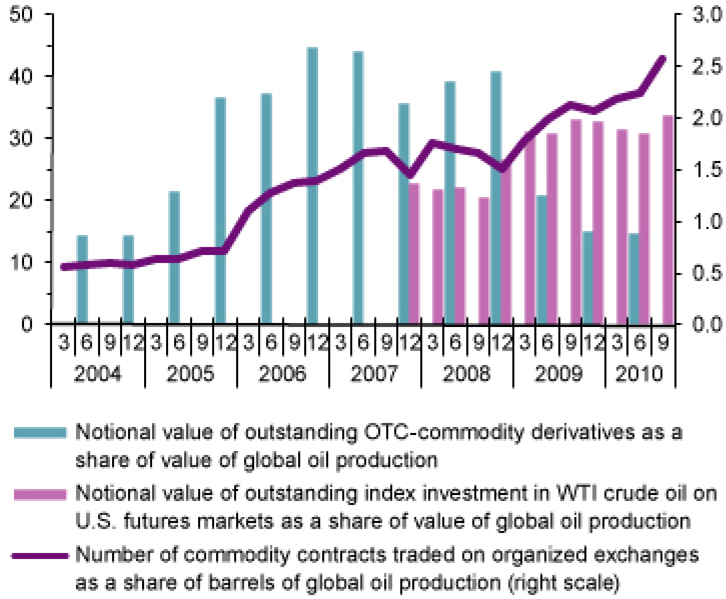
2.6 Financial liberalization and the financialization of commodity markets

Recent developments in primary commodity prices have been exceptional in many ways. The boom between 2002 and mid-2008 was the most pronounced in several decades – in magnitude, duration and breadth.

The price collapse following the eruption of the global crisis in mid-2008 stands out both for its sharpness and for the number of commodities affected. After mid-2009, and especially from mid-2010 onwards, global commodity prices recovered strongly. While the oil price increases up to April 2011 were modest compared with the spike in 2007–2008, food prices reached an all-time high in February 2011. Sizeable corrections occurred in May and August 2011, but since then prices have recovered. Such wide price fluctuations can have adverse effects for both commodity importing and exporting countries, as well as impact the resilience of households and commodity producers.

Financial investment in commodities as a proportion of global oil production, 2004-2010

(Percentage)



Source: UNCTAD, *TDR 2011* (Chart 5.2), based on BIS, *Derivatives Statistics;* CFTC, *Index Investment Data*; Energy Information Administration (EIA), *International Petroleum Monthly*; and *UNCTADstat*

The fundamental factors driving recent commodity price developments include surging demand, especially from rapidly growing developing countries; a relatively sluggish supply response and certain policies encouraging non-food related uses of food commodities. But recent price developments have also coincided with a greater weight on commodity derivatives markets of financial investors that consider commodities as an asset class. This financialization of commodity markets has accelerated significantly since about 2002–2004.

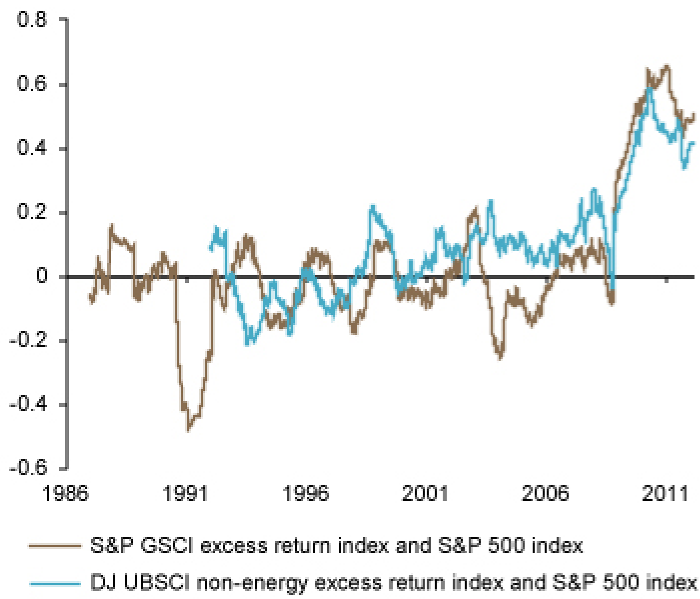
The debate on the price impact of financial investors has pointed to the increasingly close correlation between returns on investment in commodities and equities, as well as those related to the exchange rates of currencies affected by carry trade speculation.

Moreover, recent studies suggest that many financial investors have come to follow more active strategies in commodity markets, compared with the relatively passive investment behaviour of index investors on which much of the debate had focused earlier. Such more active strategies appear to be subject to so-called information-based herding which refers to traders' beliefs that they can glean relevant information by observing the behaviour of others.

In such a situation, position-taking behaviour across market participants converges and price signals emanating from commodity futures exchanges become increasingly less reflective of changes in market fundamentals. As a result, snowballing effects may develop that eventually causes asset price bubbles.

Correlation between commodity and equity indices, 1986–2012

(Coefficient)



Source: UNCTAD secretariat calculations, based on Bloomberg
Note: The data reflect one-year rolling correlations of returns on the respective indices, based on daily data.

These developments have important implications for the traditional roles of commodity futures exchanges in price discovery and risk management, as well as for the associated benefits for commercial market users. Rather than aggregating, discovering and spreading valuable private information from a multitude of independent market participants, commodity futures exchanges will come to follow more closely the logic of asset markets in which price discovery is based on information related to only a few commonly observable events, or even refer to mathematical models that mainly use past information for position-taking decisions. The risk of speculative bubbles and prolonged deviations from fundamental values rises accordingly, with a potential for distorting economic activities and causing financial fragilities.

Moreover, commercial users will fail to benefit from lower transactions costs that would normally be associated with increased market liquidity, and they may well end up shouldering higher hedging costs owing to the greater uncertainty caused by financial investors.

The financialization of commodity markets is but one prominent and more recent aspect of broader financialization trends witnessed in the era of financial liberalization across much of the globe, especially in advanced economies. While financial investors seeking to diversify their portfolios may have viewed commodities as an attractive alternative asset class, the return on which was presumed to be negatively correlated with that on equities and bonds over the business cycle, such strategies have proved ultimately self-defeating as the greater participation of financial investors has caused commodity markets to follow more the logic of financial markets and move in parallel with financial conditions in general.

As a result, financial investors in commodity markets may have come to emphasize the search for higher yields, rather than merely attempting to diversify risk. Important economic risks may arise from these developments, and quite unnecessarily so. There is scope for improving transparency in physical and futures commodity markets and for regulatory measures designed to contain the destabilizing influence of financial investors and risk of bubbles.

Highlights

- Recent developments in primary commodity prices have been exceptional in many ways;
- Sizeable commodity price volatility can adversely affect both commodity importing and exporting countries, as well as affect the resilience of households and commodity producers;
- Commodity price swings coincided with major shifts in market fundamentals but also with a rising presence of financial investors in commodity derivatives markets;
- The financialization of commodity markets has accelerated significantly since about 2002–2004;
- The financialization of commodity markets may cause price signals emanating from commodity futures exchanges to become increasingly less reflective of changes in market fundamentals;
- Further damaging real effects arise from increased hedging costs for commercial traders related to greater price volatility;
- Rising bubble risks raise broader systemic issues;
- Greater market transparency and tighter regulatory measures are called for to contain the price impact of financial investors and the associated risk of bubbles.

TO LEARN MORE

UNCTAD Trade and Development Report 2011, Chapter V *Financialized Commodity Markets: Recent Developments and Policy issues*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2009, Chapter II *The Financialization of Commodity Markets*, UNCTAD/TDR/2009

UNCTAD Trade and Development Report 2008, Chapter II *Commodity Price Hikes and Instability*, UNCTAD/TDR/2008

Price Formation in Financialized Commodity Markets: The Role of Information, Study prepared by the secretariat of UNCTAD, UNCTAD/GDS/2011/1

2.7 Global rebalancing and recovery contributions

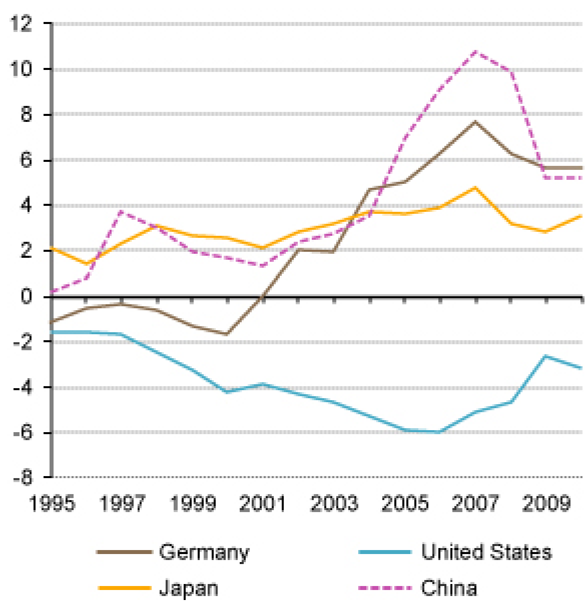
After briefly shrinking during the global crisis, global imbalances in trade and financial flows have made a comeback during the recovery and remain large as of today. While the balances of the main surplus and deficit countries or regions are below their pre-crisis peak in both current dollar terms and as a per cent of World GDP, there has been no fundamental change in the global imbalance constellation. This is despite the fact that the global crisis also triggered prominent initiatives for establishing global policy coordination procedures focused on achieving a benign global rebalancing – as part of joint agenda for sustaining global recovery and avoiding a renewed build-up of imbalances.

In a globally integrated economy, international coordination of economic policies is essential. At their Pittsburgh Summit in September 2009, the G20 Leaders designated the Group as the premier forum for international economic cooperation. The G20 replaced the G8 in this role to better reflect the new realities in the world economy. G20 leaders agreed to launch a new Framework for Strong, Sustainable and Balance Growth as the centrepiece of economic policy coordination among members. Success critically hinges on a certain degree of commonality of policy views among members, which remains problematic. Furthermore, success also hinges on the adoption of policies that are suitable to sustain global recovery and foster rebalancing.

Since mid-2010, there has been a clear shift in the general policy orientation. While the previous position was that fiscal stimulus should be maintained until recovery was assured, fiscal consolidation became established as the new policy priority at that time; although clear policy rifts emerged on the matter, with Europe leading the rush to the exit and shifting towards unconditional continent-wide austerity. There are also conflicting policy views as to how global imbalances could be reduced. Disagreements pertain to which policy adjustments may be best suited for reducing excessive imbalances, and which countries should undertake most of those adjustments.

Current account, net, of Germany, the United States, Japan and China, 1995-2010

(Percentage of GDP)



Source: UNCTAD secretariat calculations, based on UNCTADstat

The extent to which particular economies or groups of economies have actually adjusted since the crisis is reflected in the composition of contributions to their respective GDP growth and their respective domestic demand contributions to global GDP growth. Broadly speaking, global rebalancing requires that surplus countries become less reliant on net exports and more reliant on domestic demand for their growth while deficit countries should do the opposite. The rebalancing process may be partly facilitated through adjustments in international competitiveness positions and partly through macroeconomic policies attuned to either boost or restrain domestic demand growth in particular countries or regions; the ideal mix of policies depending on the nature of imbalances existing at the outset.

The most drastic adjustments have occurred in China. China's GDP growth had been primarily domestic demand driven even prior to the global crisis, and net exports only made a significant positive contribution in the years 2005–2007 As the crisis struck, domestic demand growth was sustained by means of a large stimulus programme, whereas the growth contribution of net exports has turned negative in the meantime. Expressed as a share of national GDP, China's current account surplus has declined sharply from its peak of over 10 per cent to 2–3 per cent in 2011. The adjustment has involved a gradual, managed appreciation of the renminbi's REER.

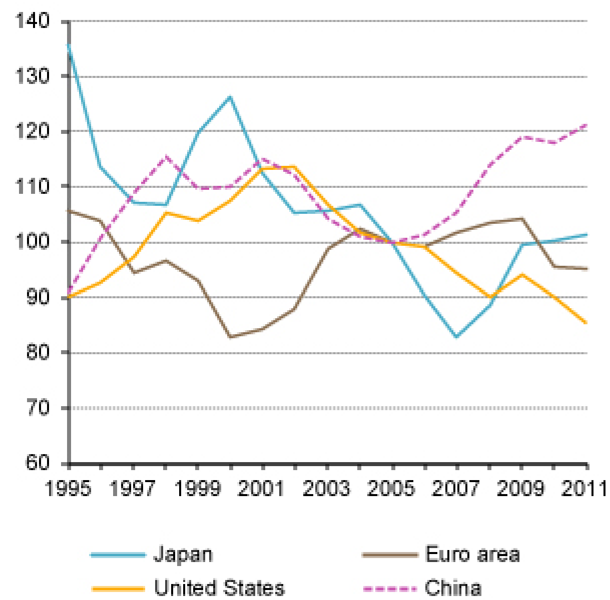
Drastic changes also characterize the situation in the United States. Sizeable negative growth contributions by net exports characterizing the pre-global crisis era have disappeared. While recovery is driven entirely by domestic demand, budget deficits and public debt have replaced earlier private deficit spending and private debts as drivers of domestic demand growth. The United States dollar's REER has moved downwards since the global crisis, as appropriate. The challenge remains to ensure fiscal consolidation by means of sustained recovery. Austerity can only fail to reach that end, as the European example clearly shows.

Among European countries, Germany's GDP growth was spectacularly unbalanced prior to the global crisis, almost exclusively reliant on net exports for the country's meagre growth. After having suffered severely from the trade collapse, Germany again benefited handsomely from trade for its recovery. While net exports again provided outsized positive growth contributions in 2010–2011, domestic demand too revived and contributed somewhat more than prior to the crisis. Owing to stresses inside the euro area, Germany's REER has moved contrary to what is needed for global rebalancing.

With the recovery derailed by unconditional continent-wide austerity, the European Union faces a double-dip recession in 2012 and a highly uncertain economic outlook beyond that year. The world's foremost trader is becoming a rising drag on global GDP growth and poses the foremost threat to sustained recovery.

Real effective exchange rate of euro area, the United States, Japan and China, 1995-2011

(Index numbers, 2005=100, CPI based)



Source: UNCTAD secretariat calculations, based on BIS, *Broad indices*

Note: The weights are based on trade data in 2008-2010.

The picture in Japan was very similar to Germany's prior to the crisis: notorious reliance on net exports for growth. The unwinding of the yen carry trade has partly corrected the yen's misaligned REER since the global crisis. Tragic natural disasters unravelled domestic demand in 2011.

The commodity exporters group's aggregate current account balance has turned from a pre-global crisis surplus position into a growing deficit during the recovery. The growth rebound in these economies was domestic demand driven, with net exports making negative growth contributions. As private capital flows have in some cases pushed up currencies very significantly, current account deficits have grown large in a growing number of developing countries, posing future risks of fragility and crisis.

In conclusion, any notion that developing countries at large, and China in particular, may be assisting the global rebalancing effort insufficiently seems untenable. Strong domestic demand growth in developing countries has made outsized contributions to world gross product growth in recent years. These developments once again highlight the shifting balance in the world economy that was accelerated by the global crisis.

Highlights

- After briefly shrinking during the global crisis, global imbalances in trade and financial flows have made a comeback during the recovery and remain large;
- While the balances of the main surplus and deficit countries or regions are below their pre-crisis peak, there has been no fundamental change in the global constellation;
- Developing countries at large, and China in particular, have experienced a significant rebalancing of their growth towards domestic demand;
- Among developed countries, recovery in the United States is exclusively carried by domestic demand, while Japan and Germany remain primarily export-reliant economies;
- Derailed by unconditional continent-wide austerity, the European Union represents the foremost threat to global rebalancing and sustained recovery.

TO LEARN MORE

UNCTAD Trade and Development Report 2011, Chapter I *Current Trends and Issues in the World Economy*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2010, Chapter I *After the Global Crisis: an Uneven and Fragile Recovery*, UNCTAD/TDR/2010

South-South Integration is Key to Rebalancing the Global Economy, UNCTAD Policy Briefs, No. 22, 22/02/2011

2.8 Policy recommendations

The world is missing an international monetary order allowing for both reasonable exchange rate stability as well as symmetric adjustment pressures on creditor and debtor countries alike. The lack of coherence between the multilateral trading system and the international monetary system has led to persistent current account imbalances. Combined with far-reaching financial deregulation and unfettered global finance, a highly unstable and hazardous global economic environment is nourished, in which democratic national governments are subjected to market whim. Given systemic asymmetries in economic and political power, developing countries are particularly vulnerable.
While global financial reform and national regulatory initiatives remain unfinished business as of today, the G20 process of international policy coordination has so far failed to produce satisfactory results. The crisis has accelerated the shift in economic balance toward the developing world, while global rebalancing remains unresolved, calling for urgent global governance reform.
UNCTAD's proposal towards a greater stability of the real exchange rate rule would directly address the systemic causes behind global imbalances.

While briefly shrinking during the global crisis, global imbalances in trade and financial flows and their underlying systemic causes have not gone away. The current monetary non-order causes developing countries to adopt defensive strategies against fickle markets and allows developed countries to engage in beggar-thy-neighbour strategies, with a reliance on exports serving to offset their failure to manage domestic demand. Global imbalances are a symptom of existing systemic governance shortcomings. They can only be properly addressed by global governance reform and proper international policy coordination.

At the peak of the global crisis, G20 members managed to see eye to eye on the need for coordinated measures to generate a strong demand stimulus. Policymakers mostly agreed that deflation presented the greatest threat. That moment of unanimity in policy views has since passed. However, nothing is gained if cooperating countries agree on strategies for their respective countries that do not represent any departure from the policies that had led to the global imbalances in the first place. Significant policy adjustments have been made in developing countries, to the extent that some have again been pushed into precarious positions by speculative capital flows. Major obstacles to global rebalancing and sustained recovery reside in key developed countries or regions.

Persisting global imbalances indicate a failure of the G20 process of international cooperation. So far that process has fallen short of launching serious reforms of the international monetary and financial system.

Essentially, the world is missing an international monetary order allowing for both reasonable exchange rate stability as well as symmetric adjustment pressures on creditor and debtor countries alike. The lack of coherence between the multilateral trading system and the international monetary system has led to persistent current account imbalances. Combined with far-reaching financial deregulation and unfettered global finance, a highly unstable and hazardous global economic environment is nourished, in which democratic national governments are subject to market whim. Given systemic asymmetries in economic and political power, developing countries are particularly vulnerable.

UNCTAD's proposal of a multilateral agreement centred on a constant real exchange rate rule would directly address the systemic causes behind global imbalances. The proposed multilateral system of rules-based managed floating exchange rates aims at stabilizing real exchange rates at sustainable levels, so as to facilitate international trade and decision-making on fixed investment in the tradable sector, while forestalling destabilizing currency speculation. The proposed system requires symmetric obligations for currency market interventions by members and amounts to a dynamic version of the earlier Bretton Woods system of pegged but adjustable exchange rates.

Instead of allowing discrete adjustments in the face of fundamental balance-of-payments disequilibrium, this alternative system aims at avoiding such disequilibria from arising in the first place, namely through continuous rules-based adjustments.
Rules-based adjustments of nominal exchange rates could follow either of two principles: adjustment according to changes in purchasing power parity; or adjustment according to uncovered interest parity. The first principle addresses more directly the need to avoid imbalances in trade flows, while the second is more directly related to avoiding imbalances in financial flows (i.e. destabilizing carry trade speculation). To the extent that differentials in official interest rates reflect differences in national inflation rates, which is largely the case (while inflation differentials, in turn, very closely correlated with trends in unit-labour costs), the two approaches lead to the same result.

It may seem paradoxical at first that the proposed monetary system should take the traditional theories of purchasing power parity and uncovered interest parity as its key guiding rules, given that these theories were found contradicted by the facts in the era of non-orderly floating exchange rates. Unfettered markets cannot be trusted to determine exchange rates that reflect fundamentals and allow balanced trade. Left to their own devices, currency markets lack an anchor, and exchange rates are rendered inherently restless, inviting destabilizing speculation. Policy intervention following the proposed rule would provide the needed anchor. Intervention by governments and central banks should not be seen as an exception to the rule of free markets, but rather, as a means of making the market function more efficiently.

Establishing a multilateral system of rules-based managed floating exchange rates should go hand in hand with re-regulating global finance, including financialized commodities markets, with a view of safety and stability.

- Lack of coherence between the multilateral trading system and the international monetary system has led to persistent current account imbalances;
- International monetary non-order, financial deregulation and unfettered global finance make for an unstable and hazardous global economy – highly asymmetric for its lack of proper global governance;
- Crisis has accelerated the shift in economic balance toward emerging market economies while global rebalancing remains unresolved;
- Global financial reform and national re-regulatory initiatives remain unfinished business;
- The G20 process of international policy cooperation has failed to produce satisfactory results;
- UNCTAD’s proposal of a multilateral agreement on exchange rates provides a solution to a pressing lack of global governance.

3 DEVELOPMENT CHALLENGES AND POLICIES TO OVERCOME THE CRISIS

MONETARY POLICY AND INTEREST RATES

Before the global economic crisis, monetary policy had been fixated on inflation control, giving only secondary importance to other goals such as full employment. Central banks were seen as the defenders of price stability, and the consensus was that they should remain independent from the pressures of governments. Monetization of debt was seen as a quintessentially inflationary phenomenon that should be avoided at all cost. In addition, the rate of interest controlled by the central bank was the fundamental tool to keep prices under control. In that sense, relatively high interest rates to discourage excessive expansion of demand was key for inflation-targeting strategies that dominated the theoretical debate and the policy practices around the world before the crisis.

FISCAL POLICY

This section discusses the relation between fiscal balances and economic activity. Too often fiscal austerity has been described as a necessary tool for economic growth, in the so-called expansionary fiscal contraction literature. However, the evidence suggests that excessive public spending and debt accumulation did not cause the current situation, and that the further adjustment of government spending, particularly in developed countries, could make things worse. This contrasts with developing countries where the fiscal stance was more stimulative after the crisis, based on expanding spending rather than on tax cuts. Policies to promote growth and employment like investment in infrastructure and in green technologies might be more relevant to promote lower debt-to-GDP ratios than fiscal austerity.

INCOME POLICY

Incomes policy is the suitable complement for expansionary monetary and fiscal policies, in particular under conditions that reduce the space for further macroeconomic expansion. Over the last 30 years, economic growth in developed countries has relied less on consumption booms on the basis of expanding wages than on increasing private indebtedness, or more on export markets, which often rely on compressed wages. This proved to be unsustainable. In some developing countries, wage expansion has proven to be a more reliable source of demand expansion. A policy that maintains real wages expanding in line with productivity would provide a sustainable source of domestic demand expansion.

RE-REGULATION OF THE FINANCIAL SYSTEM

Deregulated financial markets are prone to crisis: Credit supply is by nature pro-cyclical, herd behaviour is dominant and regularly leads to self-fulfilling prophecies. These conditions have been aggravated in the last decades by wider liberalization and financial innovation, which affected transparency and incentives, weakened supervision and expanded leveraging. Following the financial crisis, re-regulation has been dominated by the view that increased reserve requirements, and smaller financial institutions would be sufficient for curbing future crises. Further, the view that financial markets should regulate themselves is still quite predominant. The process of re-regulation has been incomplete, and further measures are needed to reduce the likelihood of financial crises.

SPECIAL CHALLENGES FACING EMERGING MARKET ECONOMIES AND LEAST DEVELOPED COUNTRING OWING TO THE VOLATILITY IN COMMODITIY PRICES

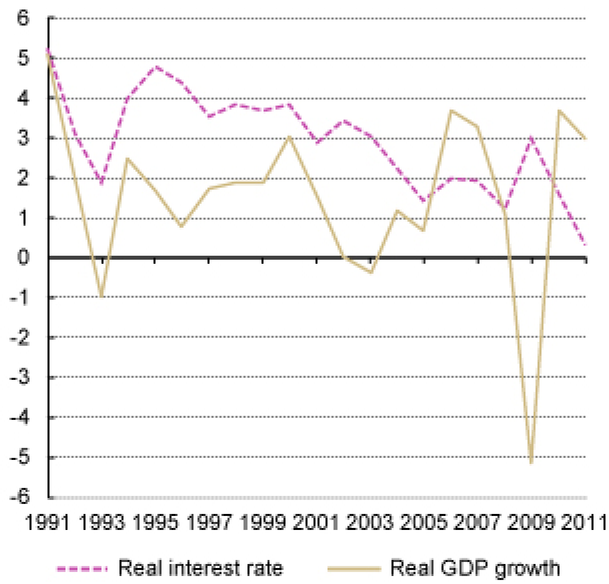
The financialization of commodity markets has come hand in hand with increasing volatility of commodity prices, which are a fundamental component of the exports of several developing countries. Commodity prices rebounded from the crisis incredibly fast, but since the second quarter of 2011 have undergone a negative trend. Volatility in commodity markets is dangerous for developing countries, since it affects growth negatively in exporting countries when they fall precipitously, and it might lead to food and energy shortages in developing import countries when they grow too fast. Regulation of financial markets to reduce volatility of commodity prices would reduce the chance of growth collapses and hunger in the developing world.

3.1 Monetary policy and interest rates

From the mid-1940s to the early 1970s, low interest favoured fiscal expansion for recovery and for the creation of the Welfare State in developed countries, as well as for infrastructure building and sustained growth rates in the developing world. This period is often referred to as the Golden Age of Capitalism. The evolution of interest rates dynamics saw two important breaks. In the first break, starting in the late 1970s and early 1980s, there was a sharp increase in interest rates, when inflationary pressures led to a shift in monetary policy priorities from full employment to price stability. The second break, which took place in the early 2000s, relates to the lower rates of interest, on average, in developed countries, after the collapse the dot-com financial bubble.

Real interest rate and real gross domestic product growth of Germany, 1991-2011

(Percentage)



Source: UNCTAD, *TDR 2011* (Table 1.1 and chart 3.3), updated March 2012

After the first break, for the most part real interest rates were higher than the rate of GDP growth in developed countries (e.g. Germany, Japan and the United States), as well as in Latin America (e.g. Mexico, in Eastern Europe (e.g. Poland, and in sub-Saharan Africa (e.g. South Africa, but not in the Asian developing economies (e.g. China and the Republic of Korea). In the subsequent phase, at least between 2001 and 2003 and the Great Recession, there was a reversal, with real interest rates lower than growth rates in almost all countries. And despite the brief fall in GDP, this trend has continued to the present day.

This is an important result, since low interest rates moderate the growth of debt, while the rate of growth of GDP, which goes hand in hand with government revenue and family income, is a measure of the ability to repay debt. Hence, when the rate of interest is below the rate of growth of the economy, the amount of debt accumulated can normally be paid, and the economy is on a sustainable path.

Quantitative easing, a situation in which the central bank buys long-term government bonds, rather than just short-term bills, in order to maintain long-term interest rates relatively low, has been particularly important in the United States. This contrasts with the limitations of the European Central Bank in buying government bonds from member countries, which has implied that interest rates on government bonds of peripheral European Union countries have risen considerably during a very difficult economic situation.

Although maintaining low interest rates on the public debt is important for avoiding a further deterioration of public finances, it will not restart credit provision to the private sector, as long as de-leveraging is not achieved. Monetary expansion could promote economic growth more effectively if it were linked to the generation of higher domestic demand or to the restructuring of mortgage debts.

The reduction of interest rates after the crisis, and quantitative easing where pursued, has been an essential instrument to preclude a major crisis of the same proportion of the Great Depression, but insufficient to promote a full-fledged recovery. For that additional support from fiscal and income policies is still needed.

Highlights

- When the rate of interest is below the rate of growth of an economy, the amount of debt accumulated can normally be paid, and the economy is on a sustainable path;
- Between 2001 and 2007, real interest rates have been lower than growth rates in almost all countries. This trend has continued from 2010 onwards;
- The reduction of interest rates after the crisis has been an essential instrument to preclude an even bigger crisis, but insufficient to promote a fully fledged recovery;
- Quantitative easing, and other unconventional monetary policy measures used to maintain interest rates relatively low and expand credit, should be used to support the recovery;
- Additional fiscal stimulus and income policies are also needed in order to promote a fully fledged recovery.

TO LEARN MORE

UNCTAD Trade and Development Report 2011, Chapter I *Current Trends and Issues in the World Economy*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2011, Chapter III *Fiscal Space, Debt Sustainability and Economic Growth*, UNCTAD/TDR/2011

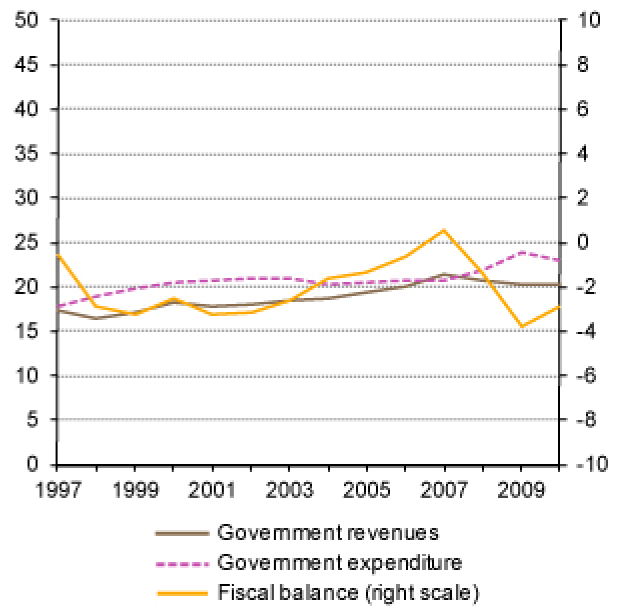
The crisis of a Century, UNCTAD Policy Briefs, No. 3, 06/10/2008

3.2 Fiscal policy

Economic crises and fiscal accounts are closely interrelated, although the nature of that relationship is controversial. It is clear that fiscal balances deteriorated significantly in all regions with the crisis, but this correlation does not reveal causality. As several governments and international institutions are adopting fiscal austerity policies aimed at reducing their public-debt-to-GDP ratios, it is important to examine whether such a policy tackles the roots of the problem.

Government revenues and expenditure and fiscal balance in developing East, South and South-East Asia,1997-2010

(Percentage of current GDP)



Source: UNCTAD, *TDR 2011* (Chart 2.2), based on the European Commission, *AMECO* database; OECD, *Economic Outlook* database

Note: East, South and South-East Asia includes: China, China, Hong Kong SAR, Taiwan Province of China, India, Indonesia, the Islamic Republic of Iran, the Republic of Korea, Malaysia, Nepal, the Philippines, Singapore, Sri Lanka, Thailand and Viet Nam. (Data for China refer to budget revenue and expenditure, they do not include extra-budgetary funds or social security funds.)

Many governments entered the crisis with fiscal surpluses or small deficits and with relatively low debt-to-GDP ratios. It was the fall in revenue caused by the crisis together with the increase in spending to reduce the impact of the crisis that deteriorated fiscal balances, in developing, developed and transition economies alike. However, economic recovery in developing countries and transition economies led to a significant improvement in fiscal accounts, while governments' deficits remained high in developed countries. These trends are mirrored by the evolution of the public-debt-to-GDP ratios: Public debt ratios generally declined before the crisis, and it is only after 2008 that they increased considerably in high-income countries.

The fiscal responses to the crisis varied considerably across regions and countries, not only in terms of the size of their economic stimulus, but also in terms of its composition and timing. A detailed assessment of fiscal stimulus packages is not straightforward, because it is difficult to distinguish policy measures that were adopted in response to the crisis from others that were already planned or that would have been implemented in any case (e.g. public investments for reconstruction following natural disasters).

In addition, official announcements are not always made at the expected time, and they only provide a general idea of the size and composition of the packages. Among developed countries, the United States implemented the largest stimulus package, in both nominal terms and as a percentage of GDP. A relatively large share of the announced fiscal stimulus took the form of tax cuts (about 40 per cent) in developed countries, compared with only 5 per cent in the larger developing and transition economies.

Governments of many natural-resource-rich countries, where public finances had a strongly pro-cyclical bias in the past, were generally able to adopt proactive countercyclical policies, despite the fall in commodity prices. During the commodity boom of the 2000s, several of these countries adopted fairly prudent fiscal policies, resulting in larger reserves. When the crisis erupted, they could increase their spending to moderate its impacts.

In many respects, the fiscal problems have been the result, not the cause, of the financial crisis. For that reason it would be more sensible to reduce debt-to-GDP ratios by boosting growth rather than cutting spending and increasing taxes to reduce debt, which might backfire and reduce growth.

Excessive reliance on fiscal austerity might end up promoting an environment of low spending, reducing the chances of a private spending recovery, in particular in developed countries. Ultimately, it would not result in fiscal consolidation.

The latter can only be achieved in highly indebted countries through a recovery of growth in the medium term, to which fiscal policy can contribute; in cases in which it would be difficult to increase total expenditure or reduce taxation, fiscal stimulus can be provided by changing the composition of spending and revenues. In particular, progressive income redistribution and public investment in infrastructure and alternative energy might be a suitable and simple way to boost demand, while creating the conditions for further growth.

Fiscal stimulus packages, as announced in selected developed economies, 2008-2010

($ Billions and percentage)

	Total amount ($ billions)	GDP (%)	Tax cut share	Spending share
Australia	23	2.4	45.2	54.8
Canada	24	1.8	52.4	47.6
France	21	0.8	6.5	93.5
Germany	47	1.4	68.0	32.0
Italy	6	0.3	33.3	66.7
Japan	117	2.3	30.0	70.0
Spain	35	2.4	58.4	41.6
United Kingdom	35	1.5	56.0	44.0
United States [a]	821	5.7	36.5	63.5
Total	1129	3.3	38.3	61.7
Unweighted average		*2.1*	*42.9*	*57.1*

Source: UNCTAD, *TDR 2011* (Table 2.2), based on European Commission, 2009; ECLAC, 2009; CBO, 2011; OECD, 2009; Hur et al., 2010; Ponomarenko and Vlasov, 2010; Prasad and Sorkin, 2009; and United States Government, 2011

Note: [a] The amount reported for the United States refers only to the stimulus package provided under the American Recovery and Reinvestment Act (ARRA) of 2009; it excludes the cost of industry bailouts and capital infusions that were components of the Troubled Asset Relief Program (TARP).

Highlights

- Before the crisis most governments had fiscal surpluses or small deficits, and debt-to-GDP ratios were relatively low and in several cases declining;
- The fiscal problems have been the result, not the cause, of the financial crisis, which was fundamentally associated with the expansion and collapse of private debt, and consumption;
- Only in developed economies did public debt soar after the crisis;
- Fiscal responses to the crisis, in terms of the size and composition of the economic stimulus, varied considerably across regions and countries;
- Recovering growth is essential for curbing high public debt-to-GDP ratios; fiscal austerity may well be a self-defeating strategy.

TO LEARN MORE

UNCTAD Trade and Development Report 2011, Chapter II *Fiscal Aspects of the Financial Crisis and its Impact on Public Debt*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2011, Chapter III *Fiscal Space, Debt Sustainability and Economic Growth*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2008, Chapter VI *Current issues related to the external debt of developing countries*, UNCTAD/TDR/2008

On the brink: fiscal austerity threatens a global recession, UNCTAD Policy Briefs, No. 24, 19/12/2011

3.3 Incomes policy

The instruments available to policymakers for supporting economic recovery seem to have been limited after the crisis, especially in developed economies. On the one hand, there is little scope for monetary policy to provide additional stimulus, as interest rates has remained at historic lows, and quantitative easing has become more difficult to defend politically. Further, the ongoing deleveraging process associated to falling asset prices, made it extremely hard to revive credit to boost domestic demand. On the other hand, higher public-debt-to-GDP ratios have convinced many governments that they should shift to fiscal tightening.

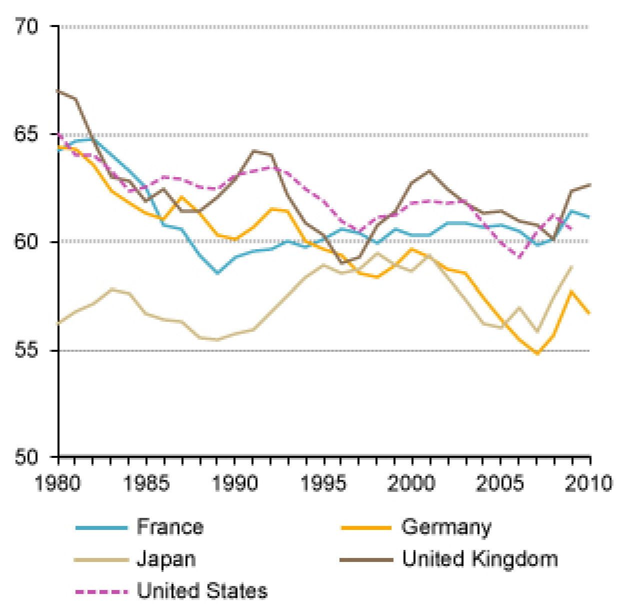
While there is more space for proactive fiscal policies than what is perceived by policymakers, in addition, there are other policy tools, such as incomes policy, that have been largely overlooked. These could play a strategic role in dealing with the present challenges.

In the period of intensified globalization from the early 1980s until the global crisis, the share of national income accruing to labour declined in most developed and developing countries. If real wage growth fails to keep pace with productivity growth, there is a lasting and insurmountable constraint on the expansion of domestic demand and employment creation. To offset insufficient domestic demand, one kind of national response has been an overreliance on external demand. Another kind of response has taken the form of compensatory stimulation of domestic demand through credit easing and increasing asset prices. However, neither of these responses offers sustainable outcomes. These are important lessons to be learned from the global crisis.

Trends in income distribution since the 1980s confirm that inequalities within many developed economies have increased as globalization has accelerated. In particular, wage shares have declined slowly, but steadily over the past 30 years, with short reversals during periods of recession – particularly in 2008–2009 – when profits tend to fall more than wages. After such episodes, however, the declining trend has resumed. This trend is creating hazardous headwinds in the current recovery. As wages have decoupled from productivity growth, wage earners can no longer afford to purchase the growing output, and the resultant stagnating domestic demand is causing further downward pressure on prices and wages, thus threatening to bring about a deflationary spiral.

Share of wages in national income in selected developed economies, 1980-2010

(Percentage)



Source: UNCTAD, *TDR 2011* (Chart 1.5), based on OECD, *Main Economic Indicators* database; and Lindenboim, Kennedy and Graña, 2011

In most developing and transition economies, the share of wages has behaved differently for the period as a whole. That share is generally between 35 and 50 per cent of GDP – compared with approximately 60 per cent of GDP in developed economies – and it tends to oscillate significantly, owing mainly to sudden changes in real wages. In many of these economies, the share of wages in national income tended to fall between the 1980s and early 2000s, but has started to recover since the mid-2000s, though it has not yet reached the levels of the 1990s. The positive evolution of wages and the role played by incomes policies, particularly transfer programmes to the poor, have been significant factors behind the present “two-speed recovery”.

In developed countries, real wages grew on average at less than 1 per cent per annum before the crisis, which is below the rate of productivity gains; they then declined during the crisis, and tended to recover very slowly in 2010. Arguably, the early move to a more contractionary fiscal policy and the relatively high levels of idle capacity and unemployment imply that the pressures for higher wages could remain subdued, thereby reducing the chances of a wages-led recovery.

In contrast, since the mid-2000s, in all developing regions and in CIS, real wages have been growing, in some instances quite rapidly. In some countries, this may represent a recovery from the steep reductions in the 1990s or early 2000s, and in others it is more than a mere recovery, as wages follow the same path as productivity gains. Even during the difficult years of 2008 and 2009, real wages did not fall in most developing countries, as had generally been the case in previous economic crises. This suggests that to some extent, recovery in developing countries was driven by an increase in domestic demand and that real wage growth has been an integral part of the economic revival.

Further, incomes policy could also be used to complement more expansionary fiscal policy in order to control prices, allowing for a more robust recovery with relatively stable prices. Subsidies to reduce the costs of basic consumption baskets for the lower income groups, which have a higher propensity to spend, and direct transfers to the less privileged in society might provide an alternative source of demand growth, helping create jobs and leading to a self-sustaining recovery.

Highlights

- There is little scope for monetary policy to provide additional stimulus, and higher public-debt-to-GDP ratios have convinced many governments that they should shift to fiscal tightening;
- Other policy tools, such as incomes policy, could play a strategic role in dealing with the present challenges;
- Wage shares have declined slowly, but steadily over the past 30 years, in particular in developed countries;
- In developing countries, wage shares tended to fall between the 1980s and early 2000s, but have started to recover since the mid-2000s;
- The positive evolution of wages and the role played by incomes policies in developing countries, in contrast with developed countries, are among the main factors behind the present "two-speed recovery".

TO LEARN MORE

UNCTAD Trade and Development Report 2011, Chapter I *Current Trends and Issues in the World Economy,* UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2010, Chapter III, *Macroeconomic Aspects of Job Creation and Unemployment*, UNCTAD/TDR/2010

UNCTAD contribution to the G20 Framework Working Group: *Incomes Policies as Tools to Promote Strong, Sustainable and Balanced Growth*, September 2011

Social Unrest Paves the Way: A Fresh Start for Economic Growth with Social Equity, UNCTAD Policy Briefs, No. 21, 21/02/2011

3.4 Re-regulation of the financial system

Financial liberalization and deregulation was based on a widespread belief in the greater efficiency of market forces. This led to the creation of increasingly sophisticated financial instruments. Deregulation was in part a response to pressure from the financial sector, but it was also part of a generalized trend towards less government intervention in the economy. New financial instruments and continued liberalization in the financial system allowed speculative activities to expand significantly, so that gambling became an important feature of financial activities. This became a source of instability in many economies, threatening the entire international economic system. By contrast, it is difficult to find any new financial instruments that have improved the efficiency of financial intermediation for the benefit of long-term investment in real productive capacity.

Financial markets do not function in the same way as typical markets for goods and services. While most entrepreneurs participating in goods markets are concerned with the creation of new real assets that have the potential to improve productivity and increase all incomes in the future, many financial market participants are primarily concerned with the effective use of information advantages concerning existing assets. In goods markets, price discovery is based on information from a multitude of independent agents who act according to their own individual preferences, and opportunities for profit arise from individual pioneering actions based on the private, circumstantial information of the market participants. By contrast, in financial markets, especially those for assets which fall in the same broad risk category (such as equities, emerging-market currencies, and more recently, commodities and their derivatives), price discovery is often based on information related to a few, commonly observable events, or even on mathematical models that mainly use past information for making price forecasts.

The fatal flaw in the functioning of financial markets lies in the fact that the most profitable activities are often derived from herd behaviour (i.e. following the trend for some time and disinvesting just before the rest of the crowd does). Acting against the majority, even if justified by accurate information about fundamentals, may result in large losses. Thus prices in financial markets sometimes overshoot, sending the wrong price signals for extended periods of time. As herding dominates the scene, no single participant questions whether the underlying information is correct or can be rationally related to events and developments in the real economy. This phenomenon has been observed not only in securities and financial derivatives markets, but also in currency and commodity futures markets.

The deregulation of financial markets has also allowed an increased concentration of banking activities in a small number of very big institutions, as well as a shift in bank funding, from a reliance on deposits to a greater reliance on capital markets, and from lending to trading. Moreover, it has paved the way for the development of a largely unregulated shadow financial system, particularly in developed economies. By early 2008, the liabilities of this shadow financial system were almost twice those of the traditional banking sector. In addition, banks outsourced a large segment of their credit intermediation functions to associated companies in the shadow system. Some parts of this system (e.g. money market funds) played the same role as that of banks, but with virtually no regulation, while the volume of activities of such groups has always been backed by too little capital.

Much of the systemic risk in the financial system has derived from the systemically important financial institutions. Proposals to address this too-big-to-fail problem have concentrated so far on additional capital requirements and improved supervision rather than on restructuring. A more comprehensive approach should also include a special resolution procedure in case of crises, which should not place the burden on government resources, and the introduction of size caps. Further, much of the impetus for financial re-regulation has stalled in developed countries, and the renewed risks of a financial crisis associated with the ongoing European crisis, suggest that a new global financial crisis cannot be completely discarded.

In the absence of a global solution for financial market volatility, developing countries should promote alternative sources of finance and develop instruments to reduce the effects of external shocks. Capital controls, the accumulation of foreign reserves and the development of a more diversified banking sector with a bigger role for public, development and community banks might be prudent measures to deal with an unreformed global financial sector.

Highlights

- The fatal flaw in the functioning of financial markets lies in the fact that many profitable activities are often derived from herd behaviour;
- Prices in financial and financialized markets sometimes overshoot, which gives rise to the possibility of bubbles;
- The development of a largely unregulated shadow financial system and the rise of the systemically important financial institutions has created systemic risk within financial markets in the sense that the failure of one institution could trigger a global financial crisis;
- Efforts to achieve financial re-regulation, which have stalled, should be pursued at the national level and at the appropriate international forums in order to avoid regulatory arbitrage;
- Developing countries should promote alternative sources of finance and develop instruments to reduce the effects of external shocks.

To learn more

UNCTAD Trade and Development Report 2011, Chapter IV *Financial Re-regulation and Restructuring*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2009, Chapter III *Learning from the Crisis: Policies for Safer and Sounder Financial Systems*, UNCTAD/TDR/2009

UNCTAD Trade and Development Report 2009, Chapter IV *Reform of the International Monetary and Financial System*, UNCTAD/TDR/2009

UNCTAD Trade and Development Report 2007, Chapter V *Regional Financial and Monetary Cooperation*, UNCTAD/TDR/2007

The Global Economic Crisis: Systemic Failures and Multilateral Remedies, Report by the UNCTAD Secretariat Task Force on Systemic Issues and Economic Cooperation, UNCTAD/GDS/2009/1

Global Monetary Chaos: Systemic Failures Need Bold Multilateral Responses, UNCTAD Policy Briefs, No. 12, 19/03/2010

3.5 Special challenges facing emerging market economies and least developed countries owing to the volatility in commodity prices

The fluctuations of commodity prices remain a central issue for developing countries. Often the collapse of commodity prices spells disaster for developing countries, since exports are needed for obtaining essential imports. But also, high commodity prices, particularly of food and energy, may be a significant problem for least developed countries creating food and energy shortages.

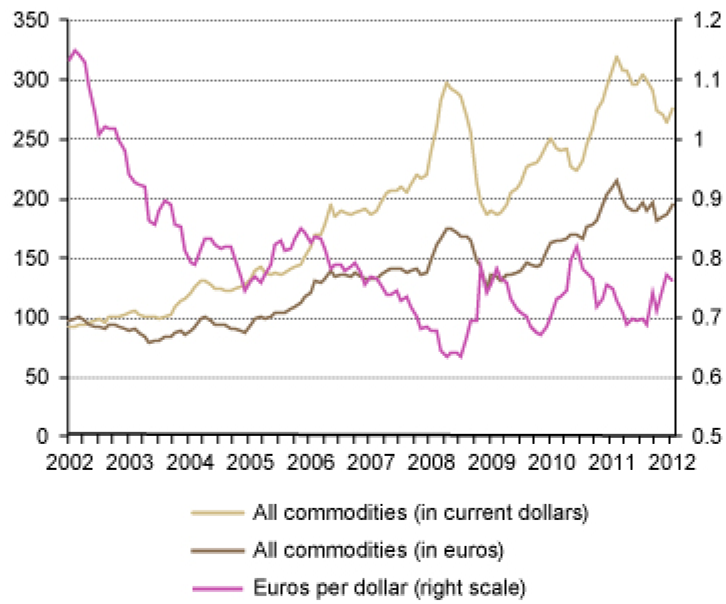
Commodity price developments have traditionally been discussed in terms of changes in fundamental supply and demand relationships. However, there is increasing support for the view that recent commodity price movements have also been influenced by the growing participation of financial investors in commodity trading. Uncertainty and instability were the major distinguishing features of commodity markets in 2010 and 2011.

This is reflected in greater volatility of commodity prices than in the past, similar to the period of the commodity boom prior to the eruption of the global financial and economic crisis in 2008. The prices of commodities and some subcategories (food, metals, and energy) grew significantly starting in the late 1990s, and it is also clear that since 2006, volatility has increased considerably.

After declining in the second quarter of 2010, commodity prices generally surged until early 2011, and then reversed the trend. Price increases were associated with three broad tendencies: (a) rising demand that reflected the recovery in the world economy, and, in particular, robust growth in developing countries; (b) supply shocks; and (c) the increased financialization of commodity markets.

Monthly evolution of non-fuel commodity price indices and exchange rates, January 2002-January 2012

(Index numbers, 2000=100 and exchange rate)



Source: UNCTAD, *TDR 2011* (Chart 1.4), based on *UNCTADstat* Commodity Price Statistics and IMF, *IFS*

The price indices for all commodity groups peaked in February 2011 at levels close to those reached in 2008, except for tropical beverages and agricultural raw materials, which were considerably higher. Although commodity prices generally declined over the second half of 2011, they have remained at relatively high levels. This reversal of the upward trend, particularly in the case of energy commodities and minerals and metals, seems partly due to the slowdown in world industrial production growth. Curbing financial speculation in commodity markets is central to guarantee economic prosperity in developing countries.

Commodity price instability indices, 2001-2010

	2001-2010	Volatility
Non-fuel commodities	**9.8**	**Medium**
All food	7.5	Medium
Food	8.2	Medium
Tropical beverages	6.4	Medium
Vegetable oilseeds and oils	15.3	High
Agricultural raw materials	7.6	Medium
Minerals, ores and metals	20.8	High
Crude petroleum	**20.1**	**High**

Source: UNCTAD secretariat calculations, based on *UNCTADstat*

Commodity exporters can take advantage of these relatively high prices for financing development. Government intervention through taxation or direct involvement in primary activities is essential for capturing a significant share of the generated rent. Instability can be addressed through stabilization funds and countercyclical macroeconomic policies in order to avoid currency overvaluation and the generation of boom-and-burst episodes.

In poor commodity-importing countries, domestic financing and foreign aid should be devoted to the development of food production and new energy sources, and to the provision of contingent finance in case of price hikes.

Highlights

- Commodity exports have a positive effect on economic growth in many developing and emerging markets;
- High commodity prices, particularly of food and energy, may be a significant problem for less developed countries, creating food and energy shortages;
- Recent commodity price movements have been influenced by the growing participation of financial investors in commodity trading;
- Curbing financial speculation in commodity markets is central to guarantee economic prosperity in developing countries.

TO LEARN MORE

The Least Developed Countries Report 2010, Chapter VI *An Agenda for Action: Commodities*, UNCTAD/LDC/2010

Special issue on Cotton in Africa, Commodities at a Glance, UNCTAD N°2 - July 2011

Historical Evolution of Primary Commodity Prices and Indices, Commodities at a Glance, UNCTAD N°1 - March 2011

Global Crises and the Commodity Dependence of the Least Developed Countries: Impacts, Challenges and the Way Forward, UNCTAD/ALDC/MISC/2011/6

Development Impacts of Commodity Exchanges in Emerging Markets, Report of the UNCTAD Study Group on Emerging Commodity Exchanges, UNCTAD/DITC/COM/2008/9

Sustainable Agriculture and Food Security in LDCs, UNCTAD Policy Briefs, No. 20(c), 09/05/2011

LDCs' boom and bust in the 2000s: the turbulent decade, UNCTAD Policy Briefs, No. 20(d), 09/05/2011

3.6 Policy recommendations

The two-speed recovery, fast in the developing world and slow in advanced economies, continues. Developed countries moved back to contractionary fiscal policies for fears of excessive accumulation of public debt.

Those fears are misplaced, and further fiscal and monetary expansion is actually required to avoid further economic slowdown. Financial re-regulation is essential for the stability of the global economy but it remains unfinished. Incomes policy that promotes the adjustment of real wages in line with productivity should also be considered, particularly in developed countries where wages have grown at lower rates. Monetary policy should move beyond inflation targeting and be also concerned with the level of activity.

The economic recovery in developed countries has entered a new phase of fragility. Many developed countries, particularly in Europe, have shifted from stimulus to fiscal retrenchment, even though private spending has not recovered and unemployment has remained high. This creates risks of prolonged stagnation or of double-dip recession in some developed economies. Given the lack of growth in employment and wages in Europe, Japan and the United States, their policies should aim at renewed monetary and fiscal stimulus of their economies instead of trying to regain the confidence of the financial markets by prematurely cutting government spending.

It is important to understand that there is nothing in balancing the budget that would automatically lead to an absorption of excess capacity as long as the private sector does not increase its spending. On the contrary, balancing the budget, by curtailing the disposable incomes of people with high consumption propensity would decrease demand and increase further excess capacity.

The rapid recovery of Asian economies after the crisis, in particular China and India, and the relatively fast recovery of commodity prices have helped developing countries maintain their growth momentum. However, many developing countries continue to face considerable downside risks and the danger of a negative external shock cannot be completely ruled out, given the volatility of commodity prices, the continuous crisis in Europe or their exposure to significant short-term capital flows, which tend to exert an upward pressure on their currencies and damage their export industries. In other words, even though growth in several developing countries has come to rely more on domestic forces rather than on exports, it remains vulnerable. Thus developing countries should aim at maintaining stable macroeconomic conditions domestically and containing external disruptions.

Strict re-regulation of the financial sector in developed countries is essential to reduce the possibilities of a new financial crisis. It is a requirement to reduce herd behaviour and eliminate the problems associated with too-big-to-fail institutions. Meanwhile, it should be more orientated towards investment in fixed capital. In parallel, developing countries should use capital controls, foreign reserve accumulation and foreign exchange management in order to reduce the risks of contagion associated with external financial crises.

Given the importance of private spending for boosting global demand, incomes policies in the biggest economies could contribute significantly to a balanced expansion, especially when the global recovery is still fragile. An essential element of such a policy is the adjustment of real wages in line with productivity, so that domestic consumption can rise in line with supply. This would also help prevent an increase in unit labour costs, and thus keep the main domestic source of inflation under control. Monetary policy could then reduce its focus on price stability and pay greater attention to securing low-cost finance for investment in real productive capacity, which in turn would create new employment opportunities.

Wages rising at a rate that corresponds approximately to the rate of productivity growth, augmented by a target rate of inflation, is the best anchor for inflation expectations.

- Developed countries' policies should aim at renewed monetary and fiscal stimulus instead of trying to regain the confidence of the financial markets;
- Developing countries also face considerable downside risks and should aim at maintaining mildly expansionist macroeconomic conditions domestically, while trying to contain external disruptions;
- Re-regulation of financial markets is a requirement to reduce herd behaviour and eliminate the problems associated with too-big-to-fail institutions;
- Developing countries should use capital controls, foreign reserve accumulation and foreign exchange management to reduce the risk of financial crises;
- Adjustment of real wages in line with productivity to promote domestic consumption is necessary for a sustainable recovery in developed countries;
- Monetary policy could then reduce its focus on price stability and pay greater attention to securing low-cost finance for investment in real productive capacity.

4 LONG-STANDING CHALLENGES

MILLENNIUM DEVELOPMENT GOALS, WHERE WE ARE?

Progress towards the achievement of the Millennium Development Goals (MDGs) has been uneven by countries, regions and goals. Poverty alleviation and gender educational attainment have seen significant progress. By contrast, maternal and child mortality, access to sanitation and water, and hunger eradication have been less promising. Most countries in sub-Saharan Africa have lagged significantly behind other developing regions. The local difficulties in Africa and the more general difficulties encountered in various regions in achieving some MDGs bring into question the policies pursued in order to attain the Goals by 2015.

POVERTY AND FOOD CRISIS

Food insecurity and undernourishment have increased after the global economic crisis, owing to higher and more volatile prices of food and agricultural commodities. Change in demand and supply are responsible for recent price hikes and rising hunger has resulted. On the demand side, financial speculation and fundamental changes associated with economic and population growth are major contributing factors. On the supply side, several shocks, partly related to climate change, aggravated resource scarcities, and in some circumstances, sparked the diversion of resources towards biofuel production. Developing countries suffer the most with food shortages. Moreover, temporary shocks can have permanent effects if they trap people in conditions of extreme poverty. Investment in agricultural productivity and more widespread safety nets are necessary to reduce the impact of undernourishment in the developing world.

OFFICIAL DEVELOPMENT ASSISTANCE AND DEBT RELIEF

Debt relief and official development assistance (ODA) are key for the achievement of the MDGs. ODA flows have increased steadily since the late 1990s, even if the global economic crisis has had a negative effect on absolute levels of ODA in the last few years. The international community has played an important role in pushing for more steady and increasing commitments from donor countries and improved governance and administration of funds in recipient countries. Flows as a share of donor country income, however, have remained constant, and a push to reach the target of 0.7 per cent is still needed. Debt relief is an important instrument for creating additional fiscal space in developing countries.

CLIMATE CHANGE AND THE NEED FOR ENVIRONMENTALLY FRIENDLY DEVELOPMENT

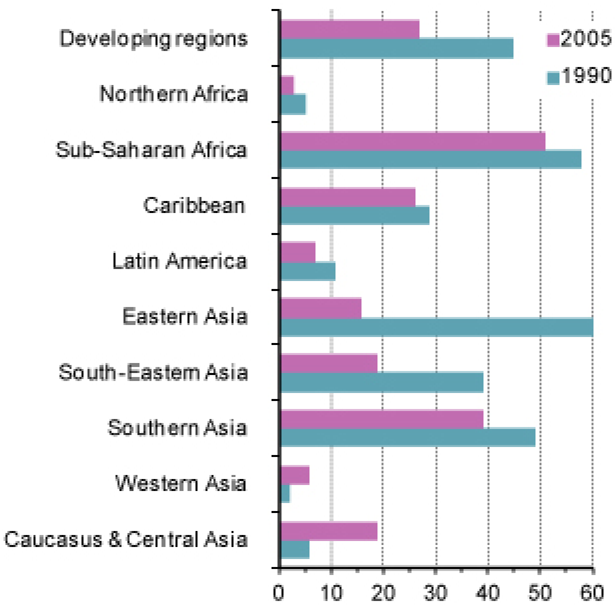
Global warming and a growing population will put a severe strain on non-renewable and agricultural resources, potentially leading to higher prices of food and energy and making it more difficult for developing countries to achieve the MDGs. Strict government regulations on greenhouse gas (GHG) emissions and deforestation are required. Meanwhile, large investment in new green technologies are essential for a more environmentally friendly growth process.

4.1 Millennium development goals, where we are?

The Millennium Development Goals (MDGs) represent the commitment of the international community to reduce poverty and hunger significantly and promote development in a relatively short-term period. Although there has been significant progress towards the achievement of the goals, several countries are off track on most MDGs, and in certain Goals, particularly in sub-Saharan Africa, the MDG achievement gap remains relatively large. Around two thirds of developing countries are on track or close to meeting the Goals. Further, the effects of the recent global economic crisis have had a clear negative impact and will make it even more difficult to achieve the MDG by 2015.

Proportion of population living on less than $1.25 a day in 2005 and 1990

(Percentage)



Source: United Nations, *MDG Report 2011*
Note: The composition of regional groupings follows MDG UN regional classification

The number of people who suffer from hunger remains high in several regions, and in sub-Saharan Africa the level might have increased. Estimates of poverty incidence in sub-Saharan Africa will be 35.8 per cent, essentially the same 36 per cent level achieved before the global economic crisis, and short of the target of 28.8 per cent. In terms of absolute numbers, while 296 million people lived in poverty in the region in 1990, approximately 345 million will be below the extreme poverty line in 2015. Only three low-income countries have currently reached the MDG1 target: Cambodia, Kenya and Mauritania.

Global poverty as a share of total population fell in all regions between 1990 and 2005, with the exception of Caucasus and Central Asia and Western Asia, where levels are very low. It is important to note that the measures are based on a poverty line of $ 1.25 per day, which is considered extreme poverty by the World Bank, and that the results might differ if alternative measures are employed. Most of the progress towards the goal is due to significant reductions in Eastern Asia, while progress in other regions has been less impressive. Latin America and the Caribbean have also progressed significantly towards the goal of halving extreme poverty.

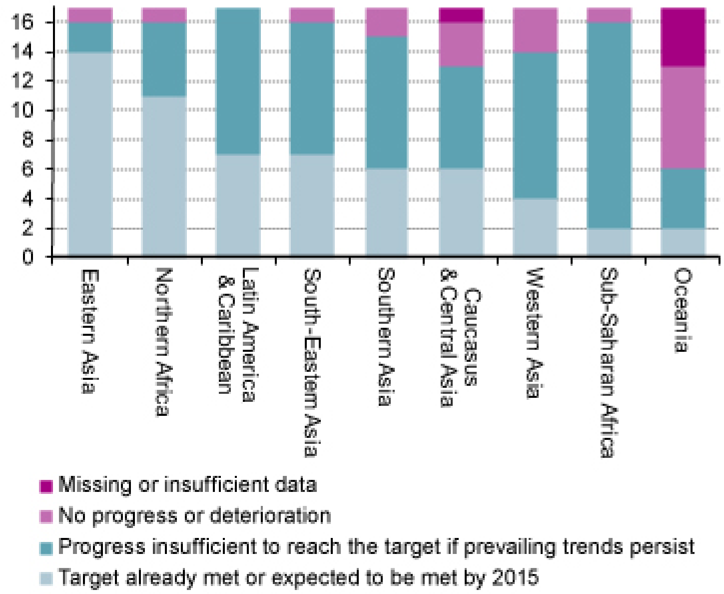
Not only is there significant diversity in the country and regional performance on MDGs achievements, but also there is a high level of variability among different MDGs. While the improvement in gender educational parity has been encouraging, one of the most worrisome developments is represented by the low achievement record in child mortality reduction.

About 70 per cent of developing countries have achieved or are on track to achieve the targets for gender parity in primary and secondary education. However, only around 36 per cent are on target to reducing the mortality of children under five, mostly from preventable and treatable diseases and conditions, including low dietary energy consumption, unsafe drinking water and the lack of basic sanitation. For example, in the case of sub-Saharan Africa, the target is to reach 61 deaths per 1,000 by 2015, but at the end of 2009, the number was still at 129 per 1,000; according to the World Bank, the region will still be considerably off target by 2030. While still off target with respect to child mortality, most Latin American, Asian and Eastern European countries are considerably closer to the goal.

Results are also not particularly promising for maternal mortality reduction, access to sanitation and to a lesser extent, access to clean water and hunger reduction. The percentage of countries on target to achieve the MDGs is uneven by region, and the proportion of developing countries on target to all the goals varies significantly by goal. Unsurprisingly while a significant number of developing countries are on target to achieve the MDGs, sub-Saharan Africa lags in most goals, and only poverty and gender educational parity goals seem to be well within reach.

Progress made towards Millennium Development Goals in selected indicators by region, 2011

(Indicators)



Source: UNCTAD secretariat calculations, based on United Nations, *Millennium Development Goals: 2011 Progress Chart*

Note: The composition of regional groupings follows MDG UN regional classification

It is crucial to understand why some regions are lagging significantly behind, and why particular targets seem less amenable to completion. These are important questions that would allow a more rational way forward for policymakers. The two main forces behind the attainment of MDG-related development outcomes are economic growth and the implementation of sound policies and institutions that allow for targeting effective service delivery to the poor. There has been a significant debate and controversy, however, over the relevant policies that are adequate to promote growth, on the one hand, and the advantages of targeting over universalism in the provision of services on the other.

While some authors have emphasized the need for deregulated and liberalized markets with strong property rights in place, with a relatively reduced role for the State, and sound fiscal and monetary policies as the main drivers for growth, the critics have suggested that the global economic crisis has debunked the main tenets of the market-friendly approach to development. Further, some authors have also been critical of the move towards targeting, suggesting that under universalism, the entire population is the beneficiary of social benefits as a basic right. According to this view, since under targeting eligibility to social benefits involves some kind of means-testing to determine the beneficiaries, a question of fairness arises.

Another important issue in the promotion of a more homogenous and widespread achievement of the MDGs is that several of the alternative goals seem to be intertwined, in the sense that it is easier to achieve one specific target if other targets are already on their way to be achieved. For example, it might be easier to reduce child mortality if access to clean water, access to sanitation and reduced hunger are already dealt with. In order to achieve the MDGs, an emphasis on growth is relevant but it is essential to tackle the issue of income distribution.

Highlights

- The percentage of countries on target to achieve the MDGs is uneven by region;
- The proportion of developing countries on target to all the goals varies significantly by goal;
- Global poverty as a share of total population fell in all regions between 1990 and 2005;
- Sub-Saharan Africa lags in most goals;
- Only the poverty and gender educational parity goals seem to be well within reach by 2015;
- There is significant controversy on the best development strategy in order to achieve the MDGs;
- In order to achieve the MDGs, an emphasis on growth is relevant but it is essential to tackle the issue of income distribution.

TO LEARN MORE

The Millennium Development Goals Report 2011, United Nations, ST/DPI(058)/M646/2011

UNCTAD Trade and Development Report 2008, Chapter V *Official Development Assistance for the MDGs and Economic Growth*, UNCTAD/TDR/2008

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Poverty Reduction and Progress towards MDGs in the LDCs: Encouraging signs but much remains to be done, UNCTAD Policy Briefs, No. 20(e), 10/05/2011

A big public investment push needed in least developed countries to meet Millennium Development Goals, UNCTAD Policy Briefs, No. 16, 20/09/2010

Reconnecting the MDGs to the development agenda: A four-pronged approach, UNCTAD Policy Briefs, No. 14, 16/06/2010

Improving the Odds of Achieving the MDGs, Global Monitoring Report 2011, 2011 The International Bank for Reconstruction and Development / The World Bank, ISBN: 978-0-8213-8700-9

4.2 Poverty and food crisis

Nearly one billion people in the world are now hungry; an additional 115 million people are suffering from hunger as a result of the combined impacts of rising food prices and the global economic recession. Two recent prices spikes have shown the limitations of the global food provisioning system. In 2007–2008, commodity prices doubled, and the estimated number of hungry people topped one billion, while food riots spread through the developing world. In 2010–2011, food prices increased again by 21 per cent.

The absolute number of undernourished people in the world has been on an upward trend since the mid-nineties. While the proportion of undernourished people has been more or less constant, it has risen sharply owing to the food and financial crises. In 2009, undernourished people accounted for 18 per cent of the world population.

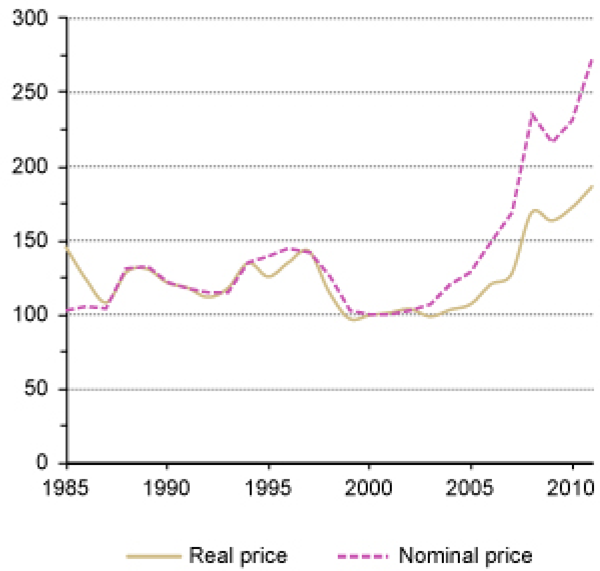
Further, the 2007–2009 crisis has had a different impact on developed and developing countries, with the least developed countries being affected the most. Around 98 per cent of the world's undernourished people live in developing countries According to the Food and Agriculture Organization of the United Nations, two thirds of the undernourished live in seven developing countries: Bangladesh, China, the Democratic Republic of the Congo, Ethiopia, India, Indonesia and Pakistan. The prevalence of undernourishment varies significantly from region to region, with sub-Saharan Africa heading the list with around 30 per cent of the population, followed by Asia with 16 per cent and Latin America and the Caribbean with 10 per cent.

In the developed world, most people were able to deal with the crisis reasonably well as a result of well-functioning safety nets; however, people in many relatively poor import-dependent countries, especially in Africa, experienced large price hikes that had permanent effects on their future income and their ability to escape poverty. Small farmers and poor consumers are extremely vulnerable to poverty as a result of unstable commodity prices. It is important to note that food represents a large share of farmer income and also a significant share of the budget of low-income consumers. As a result, big changes in food prices have a large negative impact on the real incomes of small landholders and poor families. For that reason, even temporary reductions in prices for farmers or price hikes in prices for consumers can cause permanent effects on income, leading to poverty traps.

Food prices have increased at an annual average rate of 12 per cent since 2002, despite the trend shift during 2009. Prices for rice, wheat and maize, traditional food staples, rose substantially during the global economic crisis. Further, climate change, leading to increasingly frequent natural disasters, the growing connections between energy and food markets as a result of the rising demand for biofuels, and the increased financialization of food and agricultural commodities seem to indicate that price volatility will remain an important problem in the near future. In addition, the fundamental causes of relatively high prices seem to persist; in particular, consumer demand in rapidly growing economies will increase, and the population continues to grow. On the supply side, challenges must be met to deal with the increasingly scarce natural resources in some regions, as well as declining rates of yield growth for some commodities.

Real and nominal food price indices, 1985-2011

(Index numbers, 2000=100)



Source: UNCTAD secretariat calculations, based on *UNCTADstat* Commodity Price Statistics and UN Statistics Division, *Monthly Bulletin of Statistics*, various issues

In addition to high and volatile food prices, some countries are more vulnerable than others to undernourishment and recurrent food shortages. People in countries that are in protracted crises are more vulnerable to hunger.

According to FAO, protracted crisis situations are characterized by recurrent natural disasters and/or social conflict, the longevity of food crises, the breakdown of livelihoods and insufficient institutional capacity to react to the crises. One way FAO identifies countries in protracted crises is by the proportion of humanitarian assistance received by the country as a share of total ODA.

If a country has received 10 per cent or more of their ODA as humanitarian aid since 2000, then it is classified as being in a protracted crisis. Somalia, for example, one the 22 countries on FAO's list of countries in protracted crisis has received as much as two thirds of its ODA as humanitarian aid.

Investment in agriculture remains the most decisive instrument to promote sustainable long-term food security. Such investment has the potential to improve the competitiveness of domestic production, increase farmers' profits and make food more affordable for the poor. Safety nets are also crucial for alleviating food insecurity in the short term, as well as for providing the basis for long-term development. Additional measures would include limits to biofuels expansion as it is clear that this was one of the key factors behind rising agricultural commodity prices. The high levels of price volatility must also be addressed, by increasing financial regulation to curb speculation in commodity markets. Finally, food reserves are needed to cushion price swings.

Highlights

- Around one billion people in the world are hungry, and an additional 115 million people suffer from hunger as a result of the combined impacts of rising food prices and the global economic recession;
- The crisis has had a different impact on developed and developing countries, with the least developed countries being affected the most;
- Two thirds of the undernourished live in seven developing countries: Bangladesh, China, the Democratic Republic of the Congo, Ethiopia, India, Indonesia and Pakistan;
- Small farmers and poor consumers in developing countries are more vulnerable to undernourishment as a result of the instability of commodity prices;
- People in countries that are in protracted crisis are more vulnerable to hunger;
- Investment in agriculture remains the most decisive instrument to promote sustainable long-term food security.
- In order to achieve the MDGs, an emphasis on growth is relevant but it is essential to tackle the issue of income distribution.

TO LEARN MORE

The Millennium Development Goals Report 2011, United Nations, ST/DPI(058)/M646/2011

Official Development Assistance for the MDGs and Economic Growth, UNCTAD Trade and Development Report 2008, Chapter V UNCTAD/TDR/2008

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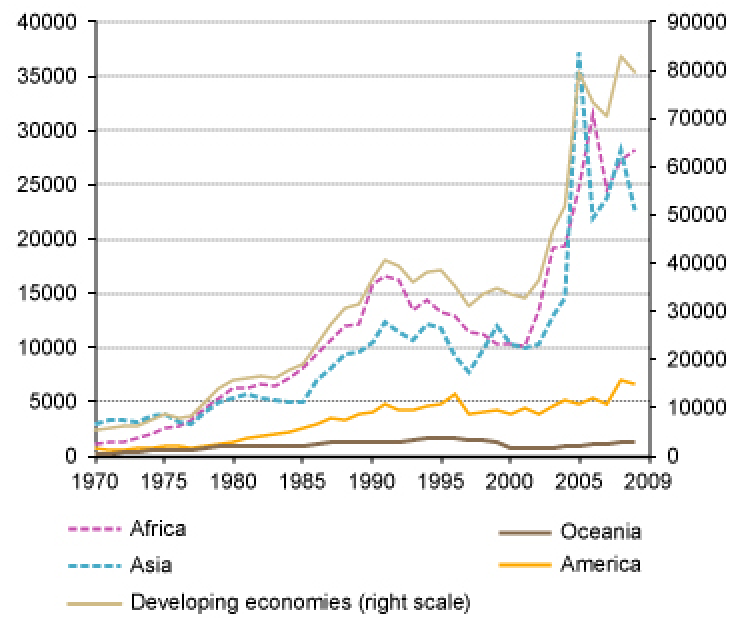
Improving the Odds of Achieving the MDGs, Global Monitoring Report 2011, 2011 The International Bank for Reconstruction and Development / The World Bank, ISBN: 978-0-8213-8700-9

4.3 Official development assistance and debt relief

Debt relief and official development assistance (ODA) are key for the achievement of the MDGs. For that reason, political leaders renewed their commitment during the 2008 G8 meetings to support the achievement of MDGs and acknowledged that ODA from G8 and other donors to developing countries, particularly Africa, should be reassessed and increased significantly beyond 2010, above their previous commitments. The 2008 G8 statement echoed previous commitments that have been made, including the United Nations Millennium Declaration of 2000. Many of the donors had targets for the year 2010 or intermediate targets to achieve by 2010 before achieving a larger target by 2015, e.g. the European Union's 0.7 per cent of ODA to the gross national income (GNI) target for 2015. However, the global economic crisis had a negative effect on absolute levels of ODA, since it also affected GNI levels in donor countries.

Net official development assistance disbursements from Development Assistance Committee donors, 1970-2009

($ millions)



Source: UNCTAD secretariat calculations,based on *UNCTADstat*

The evolution of total ODA in constant dollars and as a share of GNI for Development Assistance Committee (DAC) members from the 1960s to 2010 shows a contrasting picture. From the 1970s to 1990s, and again after the late 1990s, ODA flows from DAC countries to developing countries rose steadily. More importantly, since the late 1990s, a series of high-profile international conferences have boosted ODA flows. By contrast, total ODA as a percentage of DAC countries' combined GNI fell between 1960 and 1970, and then oscillated between 0.27 per cent and 0.36 per cent for a little over 20 years, remaining essentially at the same level after the oscillations related to the more recent global economic crisis. At the current rate of progress, donors will not fully respect their commitments in the near future and will remain far from the long-standing United Nations target of providing 0.7 per cent of GNI by 2015.

Furthermore, not only has total ODA in absolute value increased, but the composition of aid has changed over the past three decades, with large shifts in ODA allocations towards the social sector (health, education, governance), and emergency assistance and reconstruction activities. The share of ODA devoted to the social sector grew, while that for productive sectors (agriculture, industry, mining) and economic and infrastructure sectors (communications, banking, transport, energy) has declined.

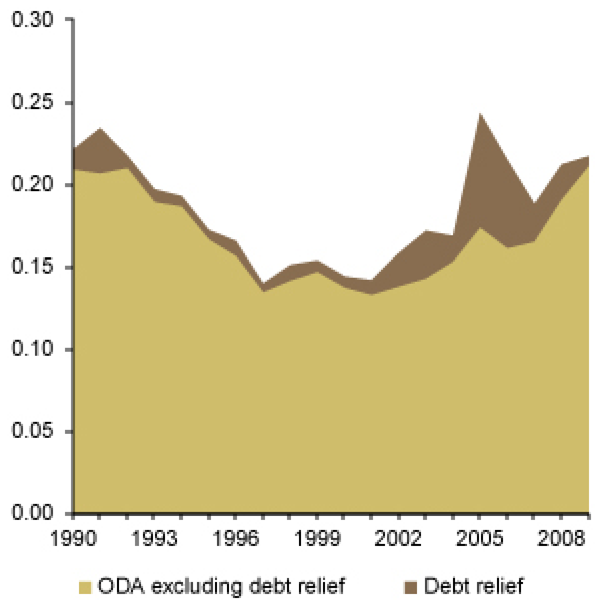
According to the OECD, ODA to agriculture and food security fell from its 1980 high of 17 per cent to under 4 per cent of total bilateral ODA in 2007. In the light of the recent food crisis, this is a particularly problematic development.

Regional patterns of ODA flows have varied significantly with donor countries' changing views of the role of ODA. The overall aid to sub-Saharan Africa has increased significantly over the past 30 years and more so in the past decade in part as a result of the pressure imposed by the MDG agenda. The United States has traditionally justified development cooperation policies in terms of recipient country needs and its own foreign policy objectives. This was true of the Marshall Plan and in the post-9/11 world. In 2005 and 2006, aid peaked because of exceptional debt relief operations in Iraq and Nigeria.

Further, developed and donor countries have more recently tried to tie the question of ODA to trade and investment liberalization. The Aid for Trade Initiative was launched at the 2005 Hong Kong World Trade Organization (WTO) Ministerial Conference, aiming at promoting aid flows for infrastructure assistance. This includes building roads, ports and telecommunications to link domestic and global markets. It also refers to productive capacity assistance related to promoting developing countries exports and to adjustment assistance to facilitate tariff reductions. Several authors have challenged this initiative and pointed out that the links between trade, growth and poverty reduction are more complex that what it is assumed by the Aid for Trade Initiative.

Official development assistance of the Development Assistance Committee and debt relief to developing economies, 1990-2009

(Percentage of GNI)



Source: UNCTAD secretariat calculations, based on *UNCTADstat*

Debt relief might be a more important tool to promote growth in developing countries than aid-for-trade arrangements. The debt relief process was greatly enhanced by the Heavily Indebted Poor Countries Initiative (HIPC) and the Multilateral Debt Relief Initiative. According to the International Monetary Fund, debt reduction packages under the HIPC Initiative have been approved for 36 countries, 30 of them in Africa, providing $76 billion in debt-service relief over time. The MDRI allows for 100 per cent relief on eligible debts by three multilateral institutions—the International Monetary Fund, the World Bank, and the African Development Fund – for countries completing the HIPC Initiative process. According to the Jubilee Debt Campaign, more than 32 of the poorest countries in the world have received over $110 billion in debt cancellation. Debt relief fundamentally frees resources, creating additional fiscal space for social spending, and is essential if the MDGs are to be achieved.

Highlights

- Debt relief and ODA are central to the achievement of the MDGs;
- The global economic crisis had a negative effect on absolute levels of ODA;
- Total ODA as a percentage of GNI fell between 1960 and 1970, and then oscillated between 0.27 per cent and 0.36 per cent until now;
- Overall aid to sub-Saharan Africa has increased significantly over the past 30 years and more so in the past decade in part as a result of the pressure imposed by the MDG agenda;
- The composition of aid has changed over the past three decades with large shifts in ODA allocations towards the social sector, while ODA for the productive sectors and economic and infrastructure sectors has declined;
- Donor countries have more recently attempted to tie ODA to trade and investment liberalization;
- Debt relief is also an important tool to promote growth in developing countries, since it frees resources, creating additional fiscal space for social spending.

TO LEARN MORE

UNCTAD Trade and Development Report 2011, Chapter II *Fiscal Aspect of the Financial Crisis and its Impact on Public Debt*, UNCTAD/TDR/2011

UNCTAD Trade and Development Report 2008, Chapter V *Official Development Assistance for the MDGs and Economic Growth*, UNCTAD/TDR/2008

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4.4 Climate change and the need for environmentally friendly development

Global warming due to increasing greenhouse gas (GHG) concentrations in the atmosphere has become a major concern worldwide. Climate change is manifest in higher average global temperatures, rising global mean sea levels, melting ice caps and an increased intensity and frequency of extreme weather events. Most scientific research suggests that the social and economic consequences of unabated climate change could be dramatic.

At the same time, a growing population will put additional strain on non-renewable and agricultural resources. Rising demand for food, water, and modern energy will put pressure on scarce natural resources. This is likely to further increase the prices of food and energy, with particularly dire effects on poor people located in sub-Saharan Africa and South Asian importing countries, whose Governments often lack the policy space to guarantee affordable prices when global prices increase.

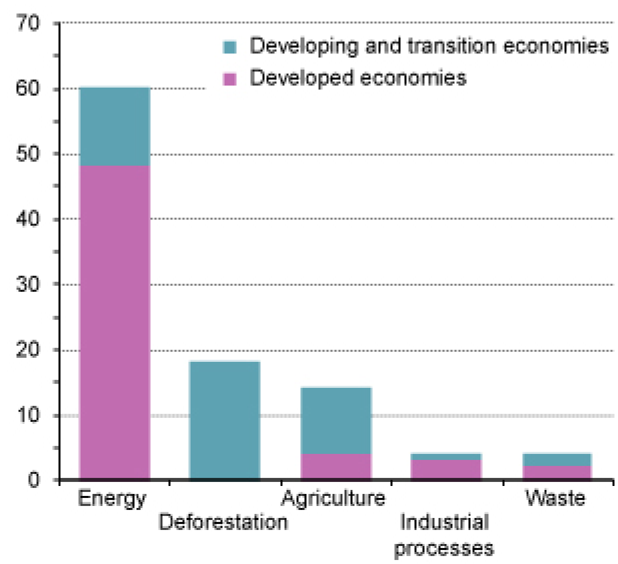
Provision of food, water, and energy becomes more difficult when natural resources are not properly managed or when external conditions deteriorate as a result of global environmental changes. For example, climate change modifies rainfall and temperature patterns. This increases the likelihood of short-term crop failures, and long-term production declines with the deterioration in water quality. The most vulnerable are poor and food-insecure countries at lower latitudes, especially in seasonally dry and tropical regions, that largely depend on rain fed farming, again in sub-Saharan Africa and South Asia. Most of these pressures are moving slowly, but they cannot be stopped easily because of major inertia, including the pressures of fertility transition and GHG accumulation. Moreover, they will become fully apparent only in the long term, after 2015 or even after 2030, trapping people in their poverty and reversing progress. In that sense, global warming might become an important restriction to the efforts to achieve the MDGs.

The rise in GHG concentrations is mainly due to carbon dioxide (CO2) resulting from the use of fossil fuels, especially for power generation and transport in developed countries. Another important source of CO2 emissions is change in land use, mainly deforestation. Together with emissions of methane and nitrous oxides that originate primarily in the agricultural sector, CO2 accounts for nearly 99 per cent of global GHG emissions. CO2 emissions per GDP and energy consumption have decreased, yet emissions relative to population have increased globally since 1980, with the minor reduction in developed countries more than compensated by the increase in developing countries.

Developed countries account for most of the historical GHG emissions, especially the energy-related ones since 1900, and they are therefore largely responsible for the global warming. They also have much higher current per capita emissions than developing countries. However, most of the growth in total GHG emissions over

Sources of current greenhouse gas emissions, 2008

(Percentage of total GHG emissions)



Source: UNCTAD, *TDR 2009* (Chart 5.1) based on Von Braun, 2008

Note: Agriculture excludes land use changes.

the past four decades has taken place outside developed countries.

Carbon dioxide emissions per capita, 1980-2006
(Tons of CO_2 equivalent)

	1980	1990	2000	2006	% change 80-06
World	**4.2**	**4.1**	**3.9**	**4.4**	**3.6**
Developing economies	*1.1*	*1.4*	*1.7*	*2.3*	*105.3*
Africa	0.9	1.0	0.9	1.0	17.6
Latin America	2.0	1.8	2.1	2.2	8.6
West Asia	3.8	4.4	5.9	6.8	78.9
China	1.5	2.1	2.4	4.3	185.5
Other Asia, excl. China	0.6	0.8	1.1	1.3	133.3
India	0.4	0.7	1.0	1.1	165.1
Transition economies	*11.2*	*12.0*	*7.3*	*8.1*	*-28.3*
Developed economies	*11.1*	*10.6*	*11.1*	*10.9*	*-1.2*
Europe	8.7	7.9	7.6	7.6	-12.6
Japan	7.5	8.7	9.4	9.5	26.7
United States	20.5	15.6	16.0	15.2	-25.7

Source:UNCTAD, *TDR 2009* (Table 5.1) based on IPCC reference approach

Note: CO_2 emissions based on IPCC reference approach.

In addition to changes in the incentive structure through market mechanisms, direct government intervention by introducing emission performance standards and strict regulations that prescribe specific modes of GHG abatement appears to be indispensable for achieving ambitious targets within the envisaged time horizon.

Climate change mitigation is an imperative that also requires faster creation and application of new technology. Carbon prices may provide a stimulus for accelerating the creation and application of appropriate cutting-edge technologies for carbon reduction compared with past decades, but significant public investment might be needed. Certain groups have called for a green New Deal to provide funds for the development of new technologies. In that sense, the austerity policies that have been pursued as a result of the recent international financial crisis pose not only a danger from a short-term, employment-generation angle, but also from a long-term perspective that aims at environmentally friendly development strategies.

Highlights

- Global warming and higher levels of population will put a severe strain on non-renewable and agricultural resources, leading to increases in the prices of food and energy;
- Higher food and energy prices will hurt people in those importing countries whose governments are unable to guarantee affordable prices;
- Climate change induces changes in rainfall and temperature patterns, potentially increasing the likelihood of short-term crop failures and increasing the likelihood of undernourishment and persistent poverty;
- Changes in the incentive structure through market mechanisms and direct government intervention by introducing emission performance standards are essential to reduce GHG emissions;
- Climate change mitigation is an imperative that also requires faster creation and application of new technologies;
- A green New Deal to provide funds for the development of new technologies is necessary, and austerity policies may have a negative impact on green investment.

TO LEARN MORE

UNCTAD Trade and Development Report 2009, Chapter V *Climate Change Mitigation and Development*, UNCTAD/TDR/2009

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Sustaining African Agriculture - Organic Production, UNCTAD Policy Briefs, No. 6, 10/02/2009

4.5 Policy recommendations

A broader perspective on the policy tools for achieving the Millennium Development Goals (MDGs) is fundamental. Macroeconomic policies should be geared to promoting full employment and a reduction of income inequality, instead of concentrating solely on price stability. Incomes policy to raise wages in line with the expansion of productivity is also a necessary complement to pro-growth macroeconomic policies. Further, official development assistance (ODA) flows should increase in a balanced way that takes into consideration the synergy between the various MDGs. Debt relief should become a more central element of the policy tool box to achieve the MDGs. Finally, reduction of greenhouse gas (GHG) emissions and the development of new renewable energy technologies should be a high priority.

The MDG agenda has been a bold attempt to improve the life of people in the developing world. The conventional wisdom is that the main hurdles to the achievement of the goals are low economic growth and insufficient economic aid. According to this view, trade and investment liberalization, coupled with an increase in aid, would suffice to promote a faster convergence towards the MDGs. In contrast, some authors suggest that in order to achieve the MDGs, a preoccupation with income distribution, on the one hand, and a bigger emphasis on how aid is spent and further debt relief, on the other hand, are necessary.
In that sense, income policies, such as the creation or extension of transfer programmes for the poorest in society, extension of welfare coverage to broader spectrum of society, and policies to promote job security and decent pay, would also encourage achievement of the MDGs. These income policies might necessitate the appropriate support from macroeconomic policies. A reorientation of macroeconomic policies, aimed at strengthening domestic demand and fostering full employment, is appropriate. In addition, incomes policies must ensure that mass incomes rise in line with average productivity growth.

Further, it is essential that ODA increases not just in absolute level, but more importantly as a share of the GNI of donor countries. Further, ODA must be distributed in a balanced way, taking into consideration that the MDGs are integrated and synergetic in nature. Part of the idea of the MDG agenda was to change the nature of economic and social policies so as to put human well-being at the centre of the policy priorities. However, it is important to understand that the process of development depends to a great extent on the capabilities of the people in developing countries, and for that not only ODA flows are important, but debt relief as well, which frees resources for alternative uses other than the service of debt helping to break the circle of indebtedness and poverty.

The interrelation between the various goals and the need for a comprehensive understanding of the difficulties of the process of development are brought to the fore by the question of global warming. The process of economic growth itself, which remains carbon intensive, has had significant impact on climate and this has created a feedback that affects development. Not only markets incentives and government regulation to reduce emissions of GHG are necessary, but also significant investment for the development of green technologies and new renewable and cleaner energy sources.

- A reorientation of macroeconomic policies aimed at strengthening domestic demand and fostering full employment, rather than just stabilizing price, is key;
- Incomes policies that ensure that mass incomes rise in line with average productivity growth should complement this reorientation;
- A significant increase in absolute ODA flows, but also relative to GNI with a balanced distribution between targets, remains necessary;
- Debt relief should be at the centre of the MDG agenda;
- Markets incentives and government regulation to reduce emissions of GHG are essential to reduce the effects of global warming;
- A major increase in investment for the development of new energy technologies is needed to reduce the environmental impact of economic development.

ANNEXES

Abbreviations

AUD	Australian dollar	**KES**	Kenyan shilling
BRL	Brazilian real	**KRW**	Republic of Kore won
CBO	Congressional Budget Office	**LBP**	Lebanese pound
CHF	Swiss franc	**LDCs**	least developed countries
CIS	Commonwealth of Independent States	**MDGs**	Millennium Development Goals
CLP	Chilean peso	**MXN**	Mexican peso
CNY	Chinese yuan	**MYR**	Malaysian ringgit
DAC	Development Assistance Committee (of OECD)	**ODA**	official development assistance
DEM	Deutsche mark	**OECD**	Organization for Economic Cooperation and Development
DJ	UBSCI Dow Jones-UBS Commodity Index	**OTC**	over the counter
ECLAC	Economic Commission for Latin America and the Caribbean	**REER**	real effective exchange rate
EUR	Euro	**RUB**	Russian rouble
FAO	Food and Agriculture Organization of the United Nations	**S&P**	500 Standard and Poor's Index of 500 stocks
FDI	Foreign Direct Investment	**S&P**	GSCI Standard and Poor's Goldman Sachs Commodity Index
FX	Foreign exchange	**SAR**	Special Administrative Region
GBP	Pound sterling	**SGD**	Singapore dollar
GDP	gross domestic product	**TDR**	Trade and Development Report
GHG	Greenhouse gas	**TRY**	Turkish lira
GNI	gross national income	**UK**	United Kingdom
ILO	International Labour Organization	**UNDESA**	United Nations Department of Economic and Social Affairs
IMF	International Monetary Fund	**USD**	United States dollar
INR	Indian rupee	**WEO**	World Economic Outlook
ISK	Icelandic Króna	**WTI**	West Texas Intermediate
JPY	Janapnese Yen	**WTO**	World Trade Organization

Definitions

Carry-trade
Carry-trade speculation is a strategy whereby an investor sells a currency that yields a relatively low interest rate (i.e. the so-called "funding currency") and uses those funds to purchase short-term assets denominated in a different currency that yields a higher interest rate.

Commodities
Commodities include food products, agricultural raw materials, minerals, ores and metals, and petroleum.

Commodity derivatives
Commodity derivatives include futures and options contracts traded on organized exchanges, as well as forward, options and swaps contracts traded on OTC markets. A derivative is a financial asset, generally a contract between two or more parties, whose value is dependent upon or derived from one or more underlying assets, such as a commodity futures contract or a commodity index.

Competitiveness
Competitiveness is a measure of a country's advantage or disadvantage in selling its products in international markets. Different measures of competitiveness can be calculated based on the differential between domestic and competitors' unit labour costs in manufacturing and consumer prices both expressed in a common currency. Unit labour cost stands for labour cost per unit of output.

Contribution of a component (net exports, domestic demand etc.) to GDP growth
Contribution of a component (net exports, domestic demand etc.) to GDP growth is usually calculated as the real growth rate of this component weighted by the share of this component in the GDP in the previous period. Thus, contributions reflect two effects: the speed with which a component changes and the relative importance of the component in total GDP.

Current account
Current account includes all the transactions recorded in the balance of payments (other than those in financial items) that involve economic values and occur between resident and non- residents entities. Specifically, the major classifications are: goods and services; income and current transfers.

Debt relief
Debt relief is any form of debt reorganisation which relieves the overall burden of debt.

Emerging Market Economies (EMEs)
Emerging Market Economies (EMEs) include include Argentina, Brazil, Chile, Malaysia, Mexico, Peru, the Republic of Korea, Singapore, Taiwan Province of China and Thailand.

Employment
Employment should include full- and part-time employees on the payroll, but not contract and temporary employees. Ideally, figures for part-time employees should be reported on a full-time equivalent basis.

Exports
Exports of merchandise are goods leaving the statistical territory of a country. It is recommended that merchandise exports be reported f.o.b. (free on board) i.e. not included transportation costs and insurance charges between the customs frontier of the exporting country and that of the importing country.

Fiscal balance
Fiscal balance is the balance of a government's tax revenues, plus any proceeds from asset sales, minus

government spending. If the balance is positive the government has a fiscal surplus, if negative a fiscal deficit.

Foreign direct investment (FDI)
Foreign direct investment (FDI) is investment involving a long-term relationship and lasting interest in and control by a resident entity in one economy in an enterprise resident in another economy. In FDI, the investor exerts significant influence on the management of the enterprise resident in the other economy. The ownership level required in order for a direct investment to exist is 10% of the voting shares. Such investment involves both the initial transaction between the two entities and all subsequent transactions between them and among foreign affiliates, both incorporated and unincorporated. FDI may be undertaken by individuals or by business.

G20
The Group of Twenty is a forum for international cooperation between the world's major advanced and emerging economies (19 countries members plus the European Union) on the most important aspects of the international economic and financial agenda.

G8
The Group of eight countries includes Canada, France, Germany, Italy, Japan, the Russian Federation, the United Kingdom, and the United States

Greenhouse gases (GHG)
Greenhouse gases (GHG) refer to carbon dioxide, nitrous oxide, methane, ozone and chloro—fluorocarbons occurring naturally and resulting from human (production and consumption) activities, and contributing to the greenhouse effect (global warming).

Gross domestic product (GDP) per capita
Gross domestic product (GDP) per capita is gross domestic product divided by population.

Gross domestic product (GDP)
Gross domestic product (GDP) is an aggregate measure of production equal to the sum of the gross value added of all resident institutional units engaged in production (plus any taxes, and minus any subsidies on products not included in the value of their outputs). It is the sum of the final uses of goods and services (all uses except intermediate consumption) measured in purchasers' prices, less the value of imports of goods and services, or the sum of primary incomes distributed by resident producer units.

Gross national income (GNI)
Gross national income (GNI) is gross domestic product (GDP) less net taxes on production and imports, less compensation of employees and property income payable to the rest of the world plus the corresponding items receivable from the rest of the world. In other words, GNI is GDP less primary incomes payable to non-resident units plus primary incomes receivable from non-resident units.

HIPC Initiative
The HIPC Initiative was launched by the World Bank and the International Monetary Fund in 1996 to coordinate and harmonize official debt relief by the multilateral financial institutions and bilateral creditors for heavily indebted poor countries (HIPC).The HIPC initiative constituted a radical departure from previous initiatives because it included cancellation of debt owed to multilateral institutions, a first in the history of debt relief. At the G7 meeting held in Cologne, Germany, in the fall of 1999, donors and multilaterals agreed that debt relief was moving slowly and decided on a major expansion of the HIPC initiative. The enhanced HIPC initiative more than doubled the amount of debt relief provided under the original HIPC, reduced the debt ratios that qualified a country's debt as unsustainable, and adopted

procedures for faster and easier debt relief.

Imports
Imports of merchandise are goods that add to a country's stock of material resources by entering its statistical territory. It is recommended that merchandise imports be reported c.i.f. (cost, insurance and freight) i.e. at the price of merchandise delivered at the frontier of the importing country, including any insurance and freight charges incurred up to that point.

Income
Total income refers to regular receipts by individuals and/or household,s such as wages and salaries, income from self-employment, interest and dividends from invested funds, pensions or other benefits from social insurance and other current transfers receivable.

Inflation
Inflation is the loss of purchasing power of currency, expressed through a general and lasting increase in prices. It must be distinguished from the increase in the cost of living. Most of the time, the rate of inflation is evaluated with the consumer price index. This measurement is not complete since the inflationary phenomenon covers a field wider than household consumption.

Instability
Instability is measured as the percentage deviation of the prices from their exponential trend levels for the period.

Interest rate
Interest rate is the cost or price of borrowing, or the gain from lending, normally expressed as an annual percentage amount.

International merchandise trade
International merchandise trade includes goods which add or subtract from the stock of material resources of a country by entering (imports) or leaving (exports) its economic territory.

Least developed countries (LDCs)
Least developed countries (LDCs) are identified on the basis of low income, human assets and economic vulnerability. In the 2009 triennial review by the United Nations, the criteria were: (a) low income, based on a three-year average estimate of the gross national income per capita (eligibility for addition to the list: under $905; qualification for graduation from LDC status: above $1,086); (b) human assets, involving a composite Human Assets Index (HAI); and (c), involving a composite Economic Vulnerability Index (EVI).

Migrant
A migrant is a person who comes to an economy and stays, or is expected to stay, for a year or more.

Migrant remittances
Migrant remittances cover current transfers by migrants: workers' remittances, compensation of employees and migrants' transfers.

Millennium Development Goals (MDGs)
The Millennium Development Goals (MDGs) are eight international development goals that all United Nations Member States and many international organizations have agreed to achieve by the year 2015. The goals are eradicating extreme poverty and hunger, achieving universal primary education, promoting gender equality and empowering women, reducing child mortality rates, improving maternal health, combating HIV/AIDS, malaria, and other diseases, ensuring environmental sustainability, and developing a global partnership for development. Each of the eight goals has specific stated time-bound targets to be

met.

Multilateral Debt Relief Initiative (MDRI)
Multilateral Debt Relief Initiative (MDRI) was launched at the July 2005 G8 summit held in Gleneagles, Scotland. MDRI implies the cancellation of all the debt owed to the IMF, the International Development Association, and the African Development Fund by all countries that reached or will reach the completion point of the HIPC initiative. Unlike the HIPC initiative, the MDRI does not propose any contemporaneous debt relief by other creditors beyond the IMF, IDA, and AfDF.

Nominal exchanges rate
Nominal exchanges rate is the price of one currency in terms of another.

Official development assistance (ODA)
Official development assistance (ODA) as reported by the OECD, includes concessional loans (with a grant element of at least 25%) and grants by members of the OECD Development Assistance Committee. The main objective of such aid is to promote the economic development of developing countries (official development assistance) or of countries in Central and Eastern Europe (official aid).

Other investment
Other investment flows is a residual category that includes all financial transactions not covered under direct investment, portfolio investment or reserve assets.

Output gap
Output gap refers to the difference between actual and potential gross domestic product (GDP) as a per cent of potential GDP.

Portfolio investment
Portfolio investment flows cover equity and debt securities, such as bonds, notes, money market instruments and financial derivatives (options etc.).

Prevalence of undernourishment
The FAO measure of food deprivation, which is referred to as the Prevalence of undernourishment, is based on a comparison of usual food consumption expressed in terms of dietary energy (kcal) with certain energy requirement norms. The part of the population with food consumption below the energy requirement norm is considered undernourished ("underfed").

Private capital flows
Private capital flows cover direct investment, portfolio investment and other investment.

Public debt
Public debt are the external obligations of the government and public sector agencies.

Purchasing power parity (PPP)
Purchasing power parity (PPP) is the rate of currency conversion that equalizes the purchasing power of different currencies by eliminating the differences in price levels between countries. In its simplest form, PPP is simply price relatives which show the ratio of the prices in national currencies of the same good or service in different countries.

Real effective exchange rates (REERs)
Real effective exchange rates (REERs) take account of price level differences between trading partners.

Movements in real effective exchange rates provide an indication of the evolution of a country's aggregate external price competitiveness.

Real interest rate
Real interest rate is nominal interest rate compensated for inflation.

Reserves
Reserves consist of those external assets that are readily available to and controlled by a country's authorities for direct financing of international payments imbalances, for indirect regulation of the magnitude of such imbalances through intervention in foreign exchange markets to affect their currency's exchange rate, and for other purposes. The category of reserve assets comprises monetary gold, special drawing rights (SDRs), reserve position in the IMF, foreign exchange assets (consisting of currency, and deposits and securities), and other claims.

Terms of trade
Terms of trade or "net barter" terms of trade are defined as the ratio of the export unit value index to the import unit value index. Export and import unit value indices reflect changes in price levels of exports and imports during the reporting period in comparison with the base period.

Unemployment
Unemployment exits when a person above a specified age who during the reference period were without work, that is, were not in paid employment or self employment; currently available for work; and seeking work, that is, had taken specific steps in a specified recent period to seek paid employment or self-employment. The specific steps may include registration at a public or private employment exchange; application to employers; checking at worksites, farms, factory gates, market or other assembly places; placing or answering newspaper advertisements; seeking assistance of friends or relatives; looking for land, building, machinery or equipment to establish own enterprise; arranging for financial resources; applying for permits and licences, etc.

Underemployment
Underemployment exists when a person's employment is inadequate in relation to specified norms of alternative employment, account being taken of his or her occupational skill.

Volume
Reference to Volume disregards changes in prices and exchange rates. Volume movements are determined by holding the price constant.

Wages
Wages and salaries are defined as "the total remuneration, in cash or in kind, payable to all persons counted on the payroll (including home workers), in return for work done during the accounting period" regardless of whether it is paid on the basis of working time, output or piecework and whether it is paid regularly or not.

Contacts

Data enquiries

All enquiries about the data presented in the publication should be addressed to:

statistics@unctad.org or by fax: +41 22 917 0389

Address:

Development Statistics and Information Branch (DSIB)
UNCTAD
Palais des Nations
1211 Geneva 10, Switzerland

Textual part

Enquiries about the textual part of the publication should be addressed to:

gdsinfo@unctad.org or by fax: +41 22 917 0389

Address:

Division on Globalization and Development Strategies
UNCTAD
Palais des Nations
1211 Geneva 10, Switzerland

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