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CEI GLOBAL REPORT

CEI Centre for International Economy

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IMF: world economy with high inflation, uncertainty and less growth

The world macroeconomics is suffering the effects of the coexistence of phenomena that had not been recorded for long: a generalised increase of inflation, a conjunction of factors that build up uncertainty over the economic future and a smaller rate of growth.

A rise in inflation…

The IMF projects a global inflation rate of 8.8% for this year –it had been of 4.7% in 2021–, of 6.7% for 2023 and of 4.1% for 2024. Although the increase is generalised, important differences between countries and regions can be observed (for 2022, the projections range from a 4% average for Asian countries to 27.8% for the countries in Eastern Europe).

The rise in retail prices derives from a greater demand originated in the fiscal stimuli of the developed countries to resist the shrinking activity derived from the COVID-19, which met supply constraints, particularly in the provision chains, soon coupled with the effect of the armed conflict between Russia and Ukraine. The higher cost of energy and agricultural raw materials particularly affected the lowest-income population in developing countries.

… and a growing uncertainty, amplifying the risk of committing errors in policy making,…

The uncertainty derives from factors like the pandemic, the war between Russia and Ukraine and the potential effects of governments' policy making.

Although the pandemic has subdued, neither governments nor companies consider this phenomenon to be over –large corporations believe it is more worrying than inflation, recession and war–. The new outbreaks in China have faced measures restricting the movements of goods and people, which have been affecting its level of economic activity and, as a consequence, its demand for imports.

The war between Russia and Ukraine has its own recessive effects on the economies of both countries. To this, the consequences of the economic sanctions to Russia are added, as well as this country's response by restricting the sales of natural gas to Europe, and the fall in its exports. The latter has brought about a rise in the price of foods, energy and products intensive in fossil fuels.

Most of the countries have increased their interest rates responding to inflation. As not all nations did so in the same proportion, the differentials of interest rates resurged, and a greater demand for bonds of the United States and a greater appreciation of the dollar were registered. The rise in the interest rate affects negatively the highly indebted developing economies and the dollar appreciation increases international trade's cost and tends to reduce its growth. Consequently, the restrictive monetary policy aims at reducing inflation but affects growth.

For the IMF, it is necessary to have a highly restrictive and long-lasting monetary policy to stabilise prices and wash away the inflationary expectations that could lead to a spiral of prices and salaries. On the other hand, the fiscal policy should help the most vulnerable groups of the population but it should not have expansive effects. The stabilisation policy is likely to raise unemployment, the IMF suggests governments implement structural reforms so as to improve productivity and allow the elimination of restrictions in supply chains.

… lead to smaller growth

The rate of global growth will shrink from 6% in 2021 to a 3.2% projection for this year and of 2.7% for 2023, as a result of inflation, the uncertainty and the measures adopted.

Developed countries would grow 1.1% on average in 2023 with likely recessions in Germany, -3% and in Italy, -0.2%. In these economies, there would be recession and inflation (stagnation). However, developing countries would grow 3.7% on average. The greatest growth would be in India 6.1% and China 4.4%. The outlook for the growth rate in Argentina is 2%. Our trade partners would have a weak performance, with the exception of China: Brazil and the United States would grow 1%, the European Union 0.7% and Chile's GDP would fall 1%.

For the IMF, these projections are subject to several factors that can make the reduction in growth even more dramatic. In the first place, a highly restrictive monetary policy can prolong the lower growth and lead to recession, but less strict measures may not be enough to redress the inflationary expectations of the economic agents. Likewise, other factors might be negative for economic activity, like a greater dollar appreciation, a rise in energy prices, the risk of a debt crisis due to higher interest rates, a new outbreak of COVID-19 or a greater fragmentation of the political situation at stake. All these would give rise to the fact that, instead of the 2.7% projection for global growth mentioned previously, in a pessimistic scenario, the growth rate anticipated for 2023 would be 0.4%, while in an optimistic scenario it would be 4.2%.

UNCTAD: developing countries negatively affected by developed countries' contractive policies

The UNCTAD states that the policies of monetary and fiscal adjustment of the developed countries, together with the crisis derived from the COVID-19 pandemic and the war in Ukraine tend to curb global growth and generate damage worse than that of the 2008 financial crisis. In the present context of fiscal adjustment, financial uncertainty and problems of multilateral coordination in the economic and political fields, the rise in interest rates to control inflation will generate stagnation in the global economy, a reversion of the capital flows that now return to developed countries, and growing financial difficulties for the indebted developing countries, with the increasing risk of another debt crisis.

This diagnosis is reflected in the projections for growth. The figures are slightly lower than those of the IMF and show declines in almost all the countries. UNCTAD projects a 2.5% rise in GDP for this year (after one of 5.8% last year) and expects a growth rate of 2.2% for 2023. For Latin America, the increase in GDP would turn from 6.6% in 2021 to 2.6% this year, and 1.1% next year.

According to UNCTAD, the post-pandemic recovery was inflationary, a differential feature with respect to the exit from other crises. As a consequence, the rise in the prices of basic products is accounted for by the bottlenecks in supply chains and the higher cost in the use of containers, derived from the transport and distribution difficulties originating during the pandemic and after years of scarce investments, and from the rise in the profit margin of large multinational companies. On the other hand, the increase in the price of cereals, energy and of products intensive in energy stems from the war between Russia and Ukraine.

According to UNCTAD, the present inflation is a costs inflation but not because of the demand for excess in the money supply. For that reason, the body considers it dangerous to face this situation with a contractive monetary policy, as the main tool to change the inflationary expectations. In this situation, it would be advisable to take steps aimed at the sectors with a higher rise in prices: to recover the grain trade, to adopt antimonopoly measures and set stricter regulations on speculation on basic products.

WTO: global trade to show less growth

For the WTO, the international trade will reduce its rate of growth, at the same time that global production does so. The causes vary according to the region: in Europe, the rise in energy prices prevails due to the war between Russia and Ukraine; developing countries face increases in the prices of fuels, fertilisers, agrochemicals and foods, also because of the war; the economy of the United States will be affected by the restrictive monetary policy and the rise in the interest rate; whereas in China, the main factor is the restrictions to the economic activity due to the new outbreak of COVID-19.

Given this scenario, the WTO anticipates that after the 9.7% "rebound" in 2021 following the hardest year of the pandemic, trade will grow 3.5% this year and only 1% in 2023. But given the uncertainty about the war and the monetary policies of the United States and Europe, the projections for next year fluctuate between a 4.6% rise in the optimistic scenario and a 2.8% fall in the pessimistic scenario. At the national level, the greatest descent will be this year in Russia both in exports (-5.8%) and in imports (-24.7%) due to the sanctions applied. With regard to the projections for next year for Argentina's trade partners: South America (-1%) and Europe (-0.7%) would reduce their imports, while Asia's (2.2%) and North America's (0.8%) sales would show a slight growth.

The IMF projects a similar trend for the international trade, except that the estimation includes both goods and services: 4.3% of growth for this year and 2.5% for next year. On the other hand, UNCTAD estimates that trade will grow between 2% and 4% this year, and that in 2023 there would be a weaker increase due to the lower growth of the global economy.

EUROPE

Record inflation and new rise in interest rates

On 27 October, the European Central Bank (ECB) decided to raise the interest rates for the third time in the last three months. On this opportunity, the announced increase was of 75 basis points, for which reason the reference rate reached 2%, its highest value since 2009 (though lower than the rates applicable in the United States and the United Kingdom).

The steps taken by the ECB mainly aim at reducing the current levels of inflation in the European countries and pushes up the risk for the region to head towards a recession. In September, the countries in the euro area recorded an average rise in prices of 9.9% and those of the EU a 10.7% rise, while the first estimation for the month of October anticipates an average inflation of 10.9% for the euro zone (ranging from 7.1% in France to 22.4% in Estonia).

This last register would represent the sixth consecutive month with a record inflation in the region. Especially worrying is the rise in the cost of electricity, with a year-on-year rise of 41.9% in October, very close to the maximum in June (42%).

The authorities of the ECB said that the institution's greatest concern is to decelerate the pace of the rise in prices to reach the mid-term goal of a 2% annual inflation. In order to meet this expectation, the bank's authorities have shown their willingness to accept the increase in rates, although they have recognised that "considerable progress" has been made and some analysts speculate that the future rises might be slighter.

The crisis of the pound triggers the resignation of United Kingdom Prime Minister

The crisis caused by the package of economic measures announced by former Prime Minister Liz Truss, including a strong depreciation of the pound sterling and British bonds of national debt (see CEI Global Report, October 2022), prompted Finance Minister, Kwasi Kwarteng's quitting and, days later, the exit of the Prime Minister. Ms Truss stepped down only 45 days after she had taken office, which has made hers the shortest tenure of a Prime Minister in the history of the United Kingdom.

Rishi Sunak is the candidate chosen by the Conservative Party to succeed Truss. He had been Boris Johnson's Finance Minister between February 2020 and July 2022. In his first speech as Prime Minister, Sunak recognised that the country is going through an economic crisis and said he had been chosen for the position to mend the errors made by his predecessor.

The recently appointed Prime Minister was one of the British politicians of the ruling party to have expressed his opposition to the package of measures promoted by Truss, and he warned that the tax reduction for the richest sectors had no economic logic at times of high inflation, and that it would only increase public debt. Although there was great expectation by the measures to be implemented by Sunak in economic aspects, the announcement of the plan to organise the public finances in the United Kingdom by 31 October was postponed until 17 November.

Aviation: historical agreement between the EU and the ASEAN

The European Union and the Association of Southeast Asian Nations (ASEAN) signed an agreement on air transport that is expected to promote the connectivity between both regions and upgrade the conditions of the airline companies in both blocs to compete for the existing air routes, in a sector severely affected by the COVID-19 pandemic.

The commitment has been negotiated since 2016 and it is the first of this type to be signed between two economic blocs; it substitutes more than 40 bilateral treaties of air services and provides a legal framework for those countries that do not have any bilateral agreement in this matter with countries from the other bloc.

According to what was signed, all the air companies in the EU will be able to fly direct routes from any European airport to all the airports of the countries in the ASEAN, and vice versa. They will have the possibility of operating up to 14 weekly passenger services and a limitless number of cargo services along the two regions and outside them, to any third country.

SOUTH AND CENTRAL AMERICA

ECLAC's proposals for regional development are approved in Buenos Aires

The authorities of the Economic Commission for Latin America and the Caribbean (ECLAC), a United Nations body that promotes the development in the region, met in the City of Buenos Aires to hold its thirty-ninth period of sessions. With the attendance of UN authorities and representatives of 27 of the member states, the Argentine presidency for a period of two years started, with Costa Rica, Cuba, Jamaica and Peru as vice presidents.

In that context, a series of resolutions were adopted, in which, along with the development of the 2024 working programme, ECLAC's role as collaborator of the States is recognised, for the formulation, follow-up and assessment of public policies. Likewise, the countries reached consensus over the importance for the region to consolidate their efforts and unify their messages in the global scenario and over this body's importance in matters of counsellorship, training and support for the regional and international coordination.

Additionally, the Commission presented the document: “Towards transformation of the development model in Latin America and the Caribbean: production, inclusion and sustainability” that summarises the difficulties facing the region. In the short term, the greatest urgencies are: to reduce inflation and the cost of living, drive growth, mitigate the social effects of unemployment and strengthen public finances; in the long term: to increase productivity, create more and better jobs, to have more sophisticated technology enabling less carbon emission and to eliminate gender gaps, among others. In that sense, it sets out to pay attention to nine sectors with a great boosting potential: energy transition, electromobility, circular economy, bioeconomy, health manufacturing industry, digital transformation, economy of care, sustainable tourism and MSMEs and social and solidarity economy.

The Chilean Senate approves the Comprehensive and Progressive Agreement for Trans-Pacific Partnership

After its undersigning in March 2018 and its approval by the Chamber of Deputies in April 2019, the Chilean Senate approved the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in October. This trade agreement involves other 10 nations (Australia, Brunei, Canada, Malaysia, Mexico, Japan, New Zealand, Peru, Singapore and Vietnam) and it is the third largest in the world, with a market with almost 500 million people (13% of global GDP).

So far, its entry into force in Brunei and Malaysia, and also in Chile is still pending. In the case of the Andean country, the remaining step is its ratification by President Boric, who assured that although contrary to his preference, he would comply with the willingness expressed in Congress. In fact, the Chilean Minister of Foreign Affairs, Antonia Urrejola, confirmed that its ratification would take place by the end of the year, regardless of whether the negotiation of the specific regulatory agreements or “bilateral charters” is achieved or not (exceptions to the treaty that are bilaterally dealt with between the States).

Economic proposals of the President-elect in Brazil

Luiz Inácio Lula da Silva was elected President of Brazil on 30 October and will take office for the third time on 1 January, 2023. Among the measures of economic and foreign policy announced during his electoral campaign the following stand out: the strengthening of companies and public banks; the rise in the minimal salary above the inflation rate; the transfer of additional incomes for the families with children up to six years of age; a higher investment in infrastructure and sanitation; and the derogation of the ceiling on public expenditures.

Also, the winning candidate promised a tax reform that includes the simplification of taxes, the reduction of burdens to consumption, the fight against fiscal evasion and increases in taxes to the revenue of people with higher income, among other measures.

Lula was also committed to promoting the industries associated to knowledge and new technologies, and, regarding foreign relationships, he expressed his intent to prioritise and promote regional integration policies, as well as the dialogue with the members of the BRICS group, countries in Africa, the European Union and the United States.

NORTH AMERICA

The US and the EU try to settle dispute over electric car credits

US Deputy National Security Advisor Mike Pyle, and Bjoern Seibert, Chief of Staff of the President of the European Commission, launched on Tuesday the "US-EU Working Group on the Inflation Reduction Act." The group –which will hold its first meeting in early November– is set to address the bloc's trade concerns about the US Inflation Reduction Act. In this regard, the Executive Vice President of the European Commission, Valdis Dombrovskis, stated that the bloc intends to achieve a negotiated agreement before having to reach more complex instances.

It should be recalled that EU as well as South Korean and Japanese officials have expressed their concern about the assembly and local content requirements underpinning the law's incentives to support clean energy technologies, in particular the tax relief for US-made electric vehicles (see CEI Global Report, September 2022).

On the other hand, the Alliance for Automotive Innovation (representing manufacturers that produce nearly 98% of the cars and light trucks sold in the US) warned that none of the electric vehicle models currently available to the US consumer will remain eligible for tax credit when the battery requirements come fully into effect. This is because China plays a key role in refining most of the key minerals needed for its manufacture and is also responsible for most of the world's production of mineral-rich components for battery cells. The development of electric vehicle supply chains in North America capable of supporting demand will take considerable time.

Potential options to address these concerns include the possibilities of delaying the phasing-in of requirements, broadening the definition of eligible countries which can supply batteries, their components and critical minerals, and reaching specific bilateral agreements with the trading partners.

US GDP recovers in the third quarter of the year

US GDP grew 0.6% in the third quarter of the year compared to the same period in 2021, and thus reached an annualised growth rate of 2.6%, according to provisional estimates published by the Bureau of Economic Analysis (BEA). The figure represents the first positive rate of the year, after two consecutive quarters of decline, of 0.4% in the first three months of 2022 and 0.1% in the second quarter.

The increase in GDP was made possible by an improvement in exports and consumer spending, as well as of non-residential investment and public expenditure, which offset the decline in residential investment and other investments.

The return to positive growth rates comes in a context marked by high inflation and the consequent interest rate hikes (the Federal Reserve continues adjusting the monetary policy and raised the reference rate once again by 75 basis points at its last meeting), but also by low unemployment and a strengthening of the dollar.

US sanctions against Nicaragua could include trade exchanges

President Biden issued an executive order extending the sanctions against Nicaragua (both against individuals or entities), and holding the Ortega government responsible for "human rights violations, the dismantling of democratic institutions, attacks on civil society, and growing security cooperation with Russia".

The order amended on 24 October extends US sanctions against Nicaragua and the administration's authority to identify which sectors may be eligible for future sanctions –specifically mentioning the gold sector, while leaving open the possibility of incorporating others– and authorises certain restrictions on new US investments in the Nicaraguan economy. In turn, it enables the possibility of limiting or prohibiting imports and exports to and from that country, as determined by the Secretary of the Treasury, in consultation with the Secretary of State and the Secretary of Commerce.

ASIA AND OCEANIA

Asia and the risks arising from the economic fragmentation

A recent IMF news report points out that the current geopolitical tensions raise the possibility that strategic competition and national security concerns could be outweighing the shared benefits of global trade. This scenario would be very costly for Asia and the Pacific, since half of the imports from the United States and a third of those from Europe come from that region. Likewise, in its latest report "Regional Economic Outlook for Asia and the Pacific", the body warns of early signs of fragmentation and the possible weakening of global trade links.

The document mentions as signs of fragmentation the trade policy measures implemented since 2018 due to the trade tensions between the United States and China and the sanctions against Russia because of the invasion of Ukraine, which create renewed uncertainty about future trade relations.

The IMF proposes an exercise that includes a fragmentation scenario in which trade between trading blocs is suspended in sectors recently affected by increased restrictions, such as energy and technology, and where non-tariff barriers in other sectors rise to levels similar to those applied during the Cold War.

In the analysis, the IMF divided the groups of countries into blocs according to the vote of the United Nations General Assembly in March 2022, in which Russia was demanded to end the invasion of Ukraine. In a first scenario, if Russia alone was isolated from the countries that voted for it in the UN, the production losses for the world economy would be small. However, these would become significantly greater if the world was divided into two blocs, with trade restricted between those countries that voted in favour and those that are against or those that abstained in March of this year. Annual permanent global losses are estimated at 1.5% of GDP, with higher losses in Asia-Pacific countries (more than 3% of GDP).

China's economy expands and exceeds expectations

After registering a 0.4% increase in the second quarter of the year –its worst economic performance since 2020–, the Chinese economy exceeded expectations in the third quarter with a year-on-year expansion of 3.9%, according to data published by the National Bureau of Statistics (NBS).

Between July and September, the Chinese economy showed significant improvements in the main indicators, compared to the second quarter. In the first nine months of the year, the country's GDP accumulated a 3% year-on-year growth, the primary sector grew 4.2%, industry increased 3.9% and the services sector expanded 2.3%. Likewise, in September, there were significant improvements in industrial performance and investment, retail sales and exports.

According to the NBS, this expansion did not come easily, and it is the result of a series of support policies to underpin the economy. On 19 August, the State Council launched 19 monitoring policies, in addition to the package of measures to stabilise the economy launched in May. However, the NBS warned that the global situation remains complex and bleak, that the fundamentals of economic recovery are not sound, and stressed the importance of the full implementation of support measures.

Chinese President presents report at the 20th National Congress of CCP

Between 16 and 22 October, the 20th Congress of the Communist Party of China (CCP) took place in Beijing, in the framework of which Xi Jinping was re-elected as Secretary General with a view to obtaining a third presidential term for five more years in March 2023. The meeting, which is held every ten years, is the framework within which the future policies of the People's Republic of China are adopted.

In the opening speech, Xi Jinping highlighted the major events of the last decade, with reference to the increase in China's economic weight and its influence in the world, the increase in people's income, and life expectancy, achievements that would mark the chosen path, and that in turn outline the larger objectives of the future five-year plans. He said that in the past ten years, the country had had historic economic growth, to now account for 18.5% of the world economy (an increase of 7.2 percentage points in its share). China ranks first in the world in terms of cereal production, and its manufacturing sector is the largest in the world, along with its foreign currency reserves.

AFRICA

Inflation in Africa, among the most urgent challenges in the region

In its latest report "Regional Economic Outlook for Sub-Saharan Africa", the IMF noted that the region faces one of the most difficult economic scenarios in years, marked by a slow recovery from the pandemic, rising food and energy prices, and high levels of public debt. One of the direst challenges facing the region is the need to address the high levels of inflation, which are devastating incomes and food security. Although there are large differences between countries, the average rate of inflation in the region was about 9% per year in August.

The consequences of the pandemic keep the domestic economic activity in sub-Saharan Africa relatively stagnant, so the IMF expects growth in the region to slow down, and only increase by 3.6% in 2022, more than one percentage point below the 2021 growth rate.

Regarding food, the prices of key commodities such as maize and wheat have been rising since 2019, contributing two-thirds of the overall inflation in fragile states and half in the rest of the region. Higher global energy prices and the strength of the dollar have also been indirectly reflected in inflation, through transport and tradable goods, such as household goods.

On the contrary, there have been only modest increases in the prices of non-tradable services and goods, which include all locally produced services, such as hotel, health or education.

As food and energy account for half of household consumption in sub-Saharan Africa, the cost of living throughout the region has skyrocketed. The IMF estimates that 12% of the region's population will face acute food insecurity by the end of 2022.

Central banks in the region (mainly in Ghana, Malawi, Mozambique, Nigeria, Uganda and the Central and West African Economic and Monetary Unions) began to raise the interest rates in response to rising inflation, capital outflows and currency depreciation as a result of tightening monetary policy in the advanced economies.

Participation of the African Development Bank in the World Health Summit

During the World Health Summit in Berlin, the President of the African Development Bank (AfDB) regretted the adverse situation faced by African countries which failed to have the tools to stop the spread of the pandemic, while in other regions COVID-19 vaccines abounded.

The lack of health resources since the beginning of the pandemic led the AfDB to take innovative measures to address both the impact of COVID-19 in Africa and the health care financing for the region in a more comprehensive manner, including the issuance of a historic US$ 3 billion social bond in 2020. The President of the AfDB requested the use of mechanisms similar to those developed by the bank to other international organisations, and put as an example the distribution of special drawing rights of the International Monetary Fund.

The AfDB recently established a system to defend health care in the region based on three pillars: renewal of the African pharmaceutical industry, promotion of vaccine manufacturing capacity on the continent and development of quality health care infrastructure. The AfDB is investing in the pharmaceutical industry and established the "African Pharmaceutical Technology Foundation", which will address intellectual property rights and access to patented technology to enable Africa to manufacture its medicines and build its own ecosystem to generate capacity in this area.

WTO analyses the lack of financing for foreign trade in West Africa

According to a report from the WTO and the International Finance Corporation (IFC), reducing the costs of foreign trade financing could generate up to US$ 26 billion in economic benefits in four West African countries. The report examines the main barriers faced by the four largest economies in the region (Côte d'Ivoire, Ghana, Nigeria and Senegal), which have a shortage of trade finance of up to US$ 14 billion per year.

The report found that most banks provide financing for consumer goods, but sectors such as agriculture and infrastructure are neglected. While trade finance supports 40% of Africa's imports and exports, and up to 80% at the global level, the trade finance market in the four countries surveyed supports only 25% of goods trade. This low coverage is mainly due to expensive offers and high rejection rates by banks, which disproportionately affect small and medium-sized enterprises, particularly those owned by women. Meanwhile, financial institutions perceive many applicants as high risk and unsecured, and report difficulties in meeting the requirements of foreign correspondent banks and a shortage of low-cost financing.

The IFC and the WTO identified opportunities that can increase the provision of trade finance, including expanding the range of companies that can access trade finance through proposals such as the IFC's "African Trade Recovery Initiative". Other opportunities include integrating trade finance into the implementation of the "African Continental Free Trade Area", strengthening foreign correspondent banking relationships, and supporting decision-making through better data and analysis.

CEI GLOBAL REPORT

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