Key points

• The world economy remains stuck in the doldrums.

• The rise of inequality and persistent financial instability that has accompanied market liberalism continues to hinder sustained growth. Inconsistent policies risk a repetition of past mistakes.

• Alternatives exist potentially boosting global GDP by at least 1-2 per cent, but greater policy ambition and multilateral coordination is needed.

• Developing countries need sufficient policy space to advance post-2015 development agenda.

• Greater policy ambition also needs greater public resources - lost from tax havens, tax competition and transfer mispricing.
The world economy in 2014 still in the doldrums

Output growth, selected country groups, annual percentage change, 2010–2014

[Graph showing output growth for world, developed countries, South-East Europe and CIS, and developing countries with data for 2010, 2011, 2012, 2013, and 2014.]
Weakest recovery since Great Depression

Constant GDP in developed economies
index numbers, crisis year=100

Employment in developed economies
index numbers, crisis year=100
Trade winds won’t blow the global economy back on course

- Trade will grow more slowly than output this year
- Problem is on the demand, not the supply, side…
- Increased competitiveness not the solution
- Seeking growth through higher net exports cannot work for all, and if it involves “internal devaluation” and lower wages, it could even be self-defeating

World trade by volume, 2010–2014
(Exports of goods)
Developed countries: insufficient demand and danger of pre-crisis patterns

• Advanced countries avoided a great depression, stabilized their financial markets and gained back most of the output lost to 2008-2009 crisis

• But the current policy mix, combining monetary expansion with fiscal austerity and wage restraint is ineffective and inconsistent:
  - it dampens aggregate demand,
  - produces slow growth,
  - weak employment,
  - asset price bubbles,
  - financial instability and
  - adverse international spillovers
Déjà-vu

Labour income share in GDP, 1990–2013

House price and stock market indices, 1990–2013
Total Assets of G5 Central Banks, G5 GDP, Global Stock Market (Jan 2009-Dec 2013)

Note: G5 includes China, Eurozone area, Japan, United Kingdom and United States
Developing regions will maintain growth … but there are risks on the horizon

Output growth, selected developing regions, annual percentage change, 2010–2014
Export-oriented strategies becoming less effective

GDP and import volume growth in developed economies
Annual average percentage change

UNCTAD bilateral concentration indices of merchandise exports
Financial instability still a real threat

The global financial cycle is driven mainly by developed countries’ policy decisions guided by the needs of their own domestic economies.

Given their volume and instability, international capital flows frequently have disruptive effects on developing countries’ macroeconomic variables and financial systems.

They should be managed according to prudential and developmental goals.
A better alternative…

Breaking with the protracted period of low economic growth requires stronger aggregate demand, especially in surplus economies, through:

- **Reflation** (government spending and credit policies)
- **Regulation** (ring fence bank activities and manage capital flows)
- **Redistribution** (from profits to wages, incomes policies, progressive taxation, improved debt restructuring)

### GDP growth in selected regions, 1990-2024

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*Data refer to PPP, constant 2005 international dollars.*
Developing countries need new growth drivers, which will require greater policy ambition

• Addressing structural weaknesses and ensuring inclusive growth, in a less favourable external economic environment, will need:

• Rebalancing growth strategies with less emphasis on exports to developed countries, greater role for domestic and regional demand
• Industrial policies – supported by macroeconomic policies – to stimulate productive investment, develop local markets and diversify.
• Public investment in infrastructure and human capital
• Stable and long-term capital inflows
• Greater fiscal space in which to finance a more ambitious policy agenda
Stability of capital flows requires managing the capital account

- Capital account management measures are needed for managing the amount, composition and direction of foreign capital flows
- They should be considered normal instruments in the policymakers’ toolkit, not exceptional devices to be employed only in critical times
- Multilateral rules allow governments to manage their capital accounts, but some bilateral trade and investment agreements introduce commitments to financial liberalisation that may impede using such measures
Fiscal space needs to match policy ambitions

- Governments need to finance the investment and other public spending required for development: fiscal space and economic development evolved hand in hand.

- But “tax optimisation” (now part of “normal” business practice,) and tax competition circumvents fiscal responsibilities and constrains fiscal revenues;

- Magnitude of revenues foregone is difficult to assess but wide agreement it is very big number: estimates - 8–15 per cent of the net financial wealth of households estimated held in tax havens, resulting in a loss of public revenue amounting to $190–$290 billion per year ($66–$84 billion in developing countries);

- The main vehicle for corporates’ tax avoidance or evasion is the misuse of “transfer pricing” and “thin capitalization” for shifting accounting profits to low-(or no-) tax jurisdictions; developing countries may lose over $160 bn annually.

- Tax competition and privatisations in the 1990s reduced the share of natural rents captured by many resource-based economies. Between 2004-2014, 17-34% of rents generated in extractive industries dominated by private firms, much higher where public firms dominate.
Government revenues and per capita GDP (2012) - developing countries still have much to gain.
Tax challenges must be addressed at both national and international levels

- Rising commodity prices allowed governments – from developed and developing countries – to renegotiate or cancel existing contracts, increased tax or royalty rates and changed the degree of State ownership of extractive projects.

- Recent efforts for improving transparency are positive steps, but a bigger role for developing countries and better surveillance of private companies is needed.

- A possible multilateral framework (the UN): (i) an international convention against tax avoidance and evasion; (ii) International initiatives such as the Transparency Initiative in Extractive Industries should be made mandatory and extended.

- Yet, governments can also apply measures at the national level, for instance against the misuse of transfer pricing.
Developing countries can aim at the widest possible policy space

- Skilful use of policy space that remains under existing trade and investment agreements to pursue proactive policies with a view to fostering structural transformation and rebalancing growth strategy
  - Refocus on multilateral agreements which recognize the legitimate concerns of developing countries
  - Eliminate pro-investor-biased mechanisms embedded in International Investment Agreements that reduce policy space
  - Carefully consider loss of policy space when engaging in bilateral and regional trade and investment agreements
  - Joining global value chains should not mean aligning policies simply to interests of lead firms, follow development interests also