06-03-2012 16:33

Emerging no more?

By Mauro F. Guillen and Emilio Ontiveros

For almost 15 years, emerging economies have managed to grow at very high rates, even during times of turmoil and distress. They have weathered financial storms rather successfully, bouncing back much faster than developed economies.

Since the beginning of the crisis, emerging economies have generated three quarters of total growth in the global economy. Based on this spectacular performance, we have come to assume that the emerging economies will continue growing at a fast pace for many years to come, and that their expanding domestic markets would one day become growth engines for the entire global economy.

Recent trends seem to belie such a rosy picture. We are witnessing an economic deceleration around the emerging world, a moderation of growth rates to levels well below those needed to continue lifting people out of poverty, creating a broadly-based middle class of consumers, and providing impetus to the rest of the global economy as a whole.

China’s double-digit growth rates are a thing of the past. Russia and India are also seeing their economies expand at a much slower pace. Brazil’s period of rapid growth seems to have come to an end. Overall, the IMF estimates that emerging and developing economies grew at a rate of 6.2 percent during 2011, down from 7.5 in 2010. The projection for 2012 is a further reduction to 5.7 percent.

Much of the reduction in growth is due to the economic problems in Europe and the United States, which are the emerging world’s most important markets for manufactured goods, commodities and energy. Global trade grew by 12.9 percent in 2010, but only by 5.8 in 2011.

The projection for 2012 is a paltry 4.0 percent, with imports by developed economies growing by as little as 1.8 percent. Although many of the emerging economies now have major domestic consumption markets, it seems as if they are not ready to compensate for the reduction in export-led growth.

The increasingly dire situation of European banks is also a key factor because the play an important role in trade and project finance. The IMF has estimated that its impact on Australia, New Zealand, Hong Kong, South Korea and Taiwan is sizable. European banks often orchestrate complex financing deals for infrastructure projects for which it is hard to find alternatives quickly.

The economic slowdown in emerging economies comes at a bad moment. China and India still have hundreds of millions of people who would like to overcome poverty and enjoy the fruits of development. Russia’s government has ambitious plans to build infrastructure to modernize the economy. Brazil needs continued growth to stay on track with its poverty reduction targets.

The consequences of reduced growth in emerging economies will be first and foremost felt by commodity producers, given the downward pressure on prices. Suppliers of capital goods and industrial components such as Taiwan, South Korea and Taiwan, which run large trade surpluses with China, will also see their exports dwindle.

The global economy cannot afford further reductions in emerging-market growth. At the same time, overheating in some emerging economies mitigate against fiscal stimuli aimed at accelerating growth, especially because they could fuel inflation, which is already high in India, Brazil and other Latin American countries. In China and many other emerging economies banks’ loan portfolios are still reeling from the

excesses of the credit boom.

Emerging economies with a sound fiscal position and little exposure to volatile cross-border capital flows could and should compensate for slackening external demand.

Those lacking such strength should think twice about jumping the gun on stimulus. Let's hope that emerging economies do not make the kinds of fiscal, monetary and banking mistakes that have unnecessarily deepened and prolonged the economic crisis in Europe and the U.S.

Mauro F. Guillen is Director of the Lauder Institute at the Wharton School. Emilio Ontiveros is President of AFI and a Professor at Universidad Autonoma de Madrid.