



Charting a Course Through Rough Seas: How Emerging Markets Can Navigate Tougher External Conditions

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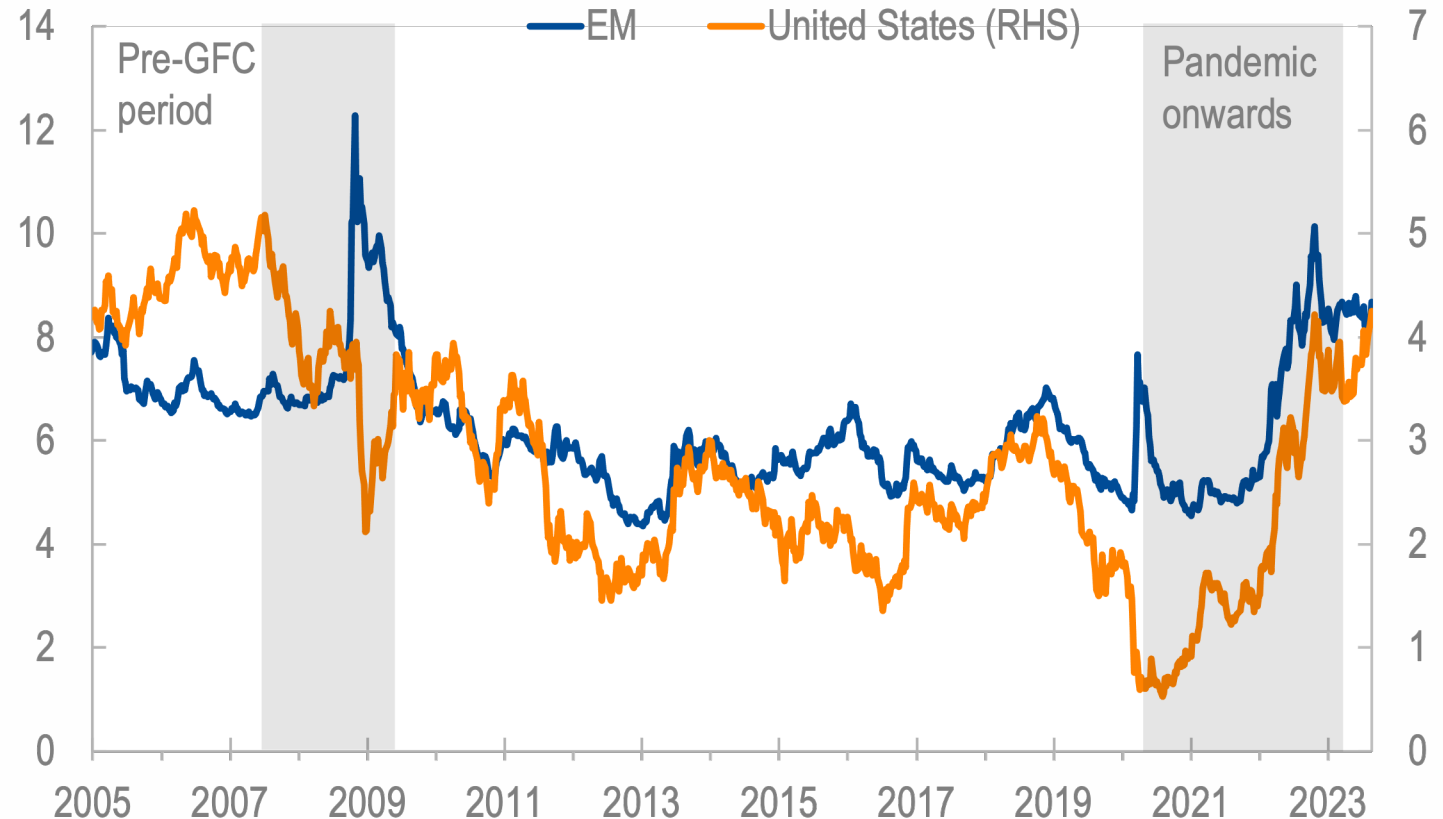
A daunting external landscape for EMs

Global financial conditions are tougher

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10-year US Treasury bond yields have surged to over 4 percent in nominal terms, the highest since the GFC

Sovereign Bond Yields
(In percent, USD denominated)

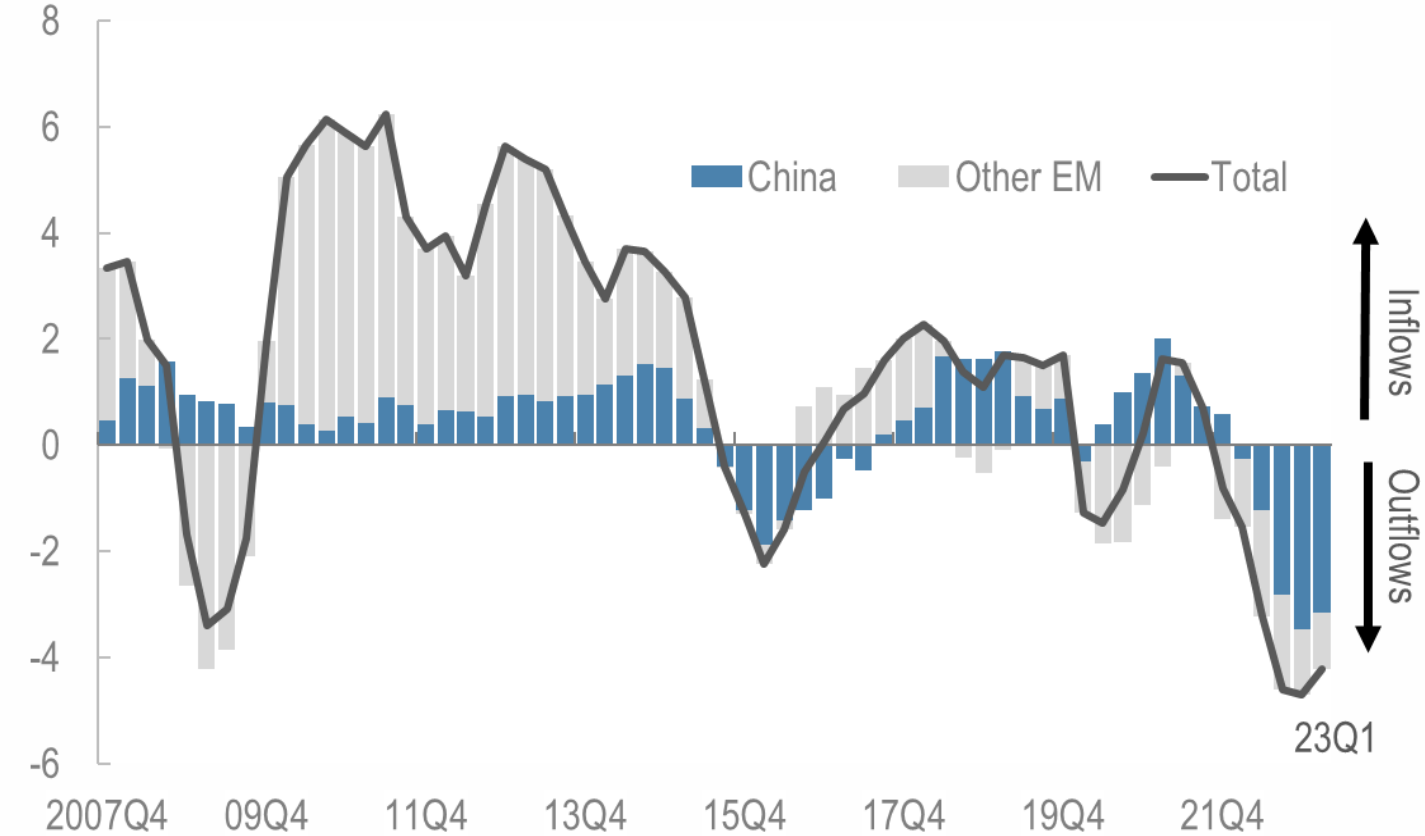


Sources: Bloomberg. Notes: For EMs, JPM Diversified EM Bond Index: blended yields on USD-denominated sovereign debt, with weighted latest maturity of 10.7 years.

Global financial conditions are tougher

EM Net Portfolio Flows
(Percent of GDP, 4 quarter rolling sum)

Net portfolio flows to major EMs turned negative in 2021Q4



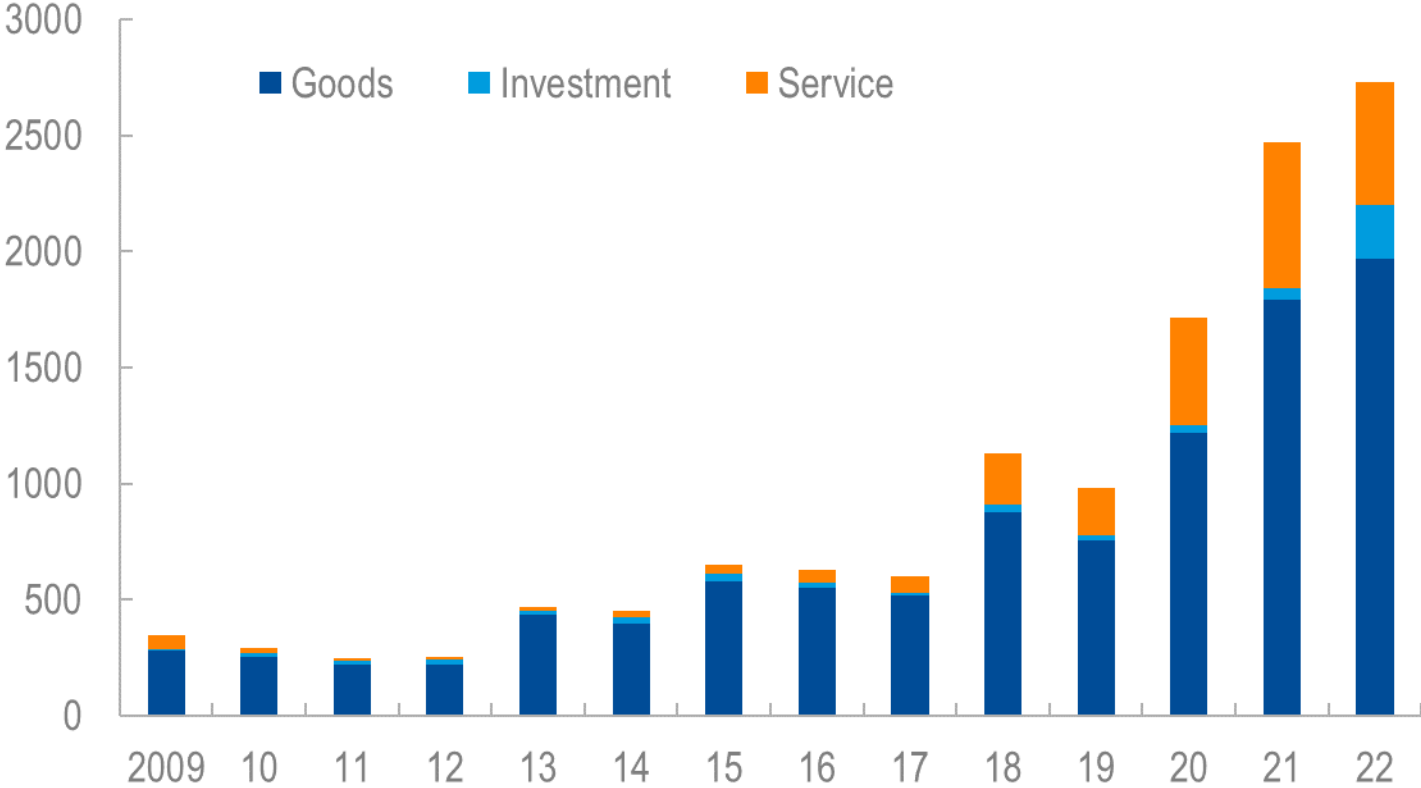
Sources: IMF, 2023 External Sector Report and IMF staff calculations.
Note: Flows include both debt and equity portfolio investment flows.

Geoeconomic fragmentation is rising

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Trade Tension Rising Over Time
(Number of harmful trade restriction measures imposed)

Around **3,000 trade restrictions** were imposed last year—nearly 3 times the number imposed in 2019...

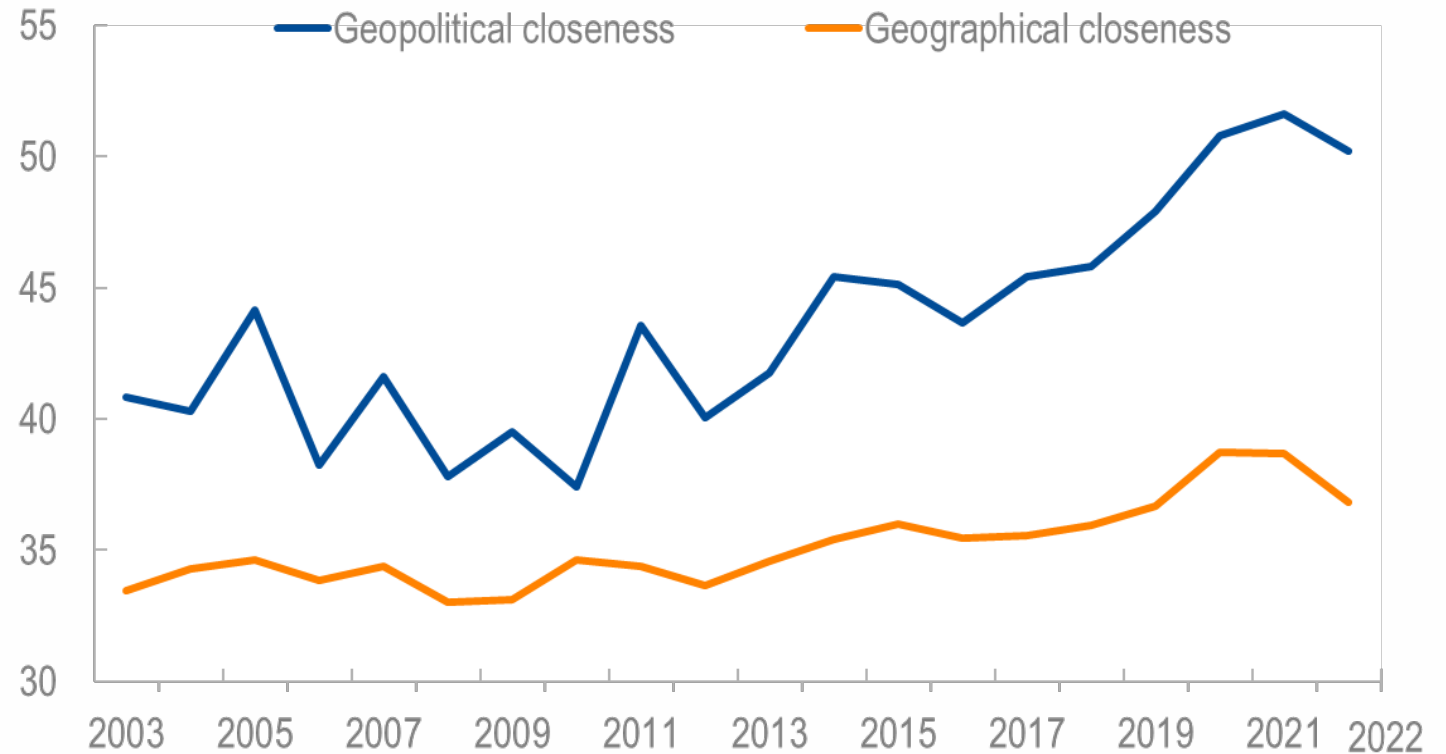


Sources: Global Trade Alert; IMF World Economic Outlook (April 2023).

Geoeconomic fragmentation is rising

... **FDI flows** are increasingly driven by geopolitical closeness.

Foreign Direct Investment between Geographically and Geopolitically Close Countries
(Percent)



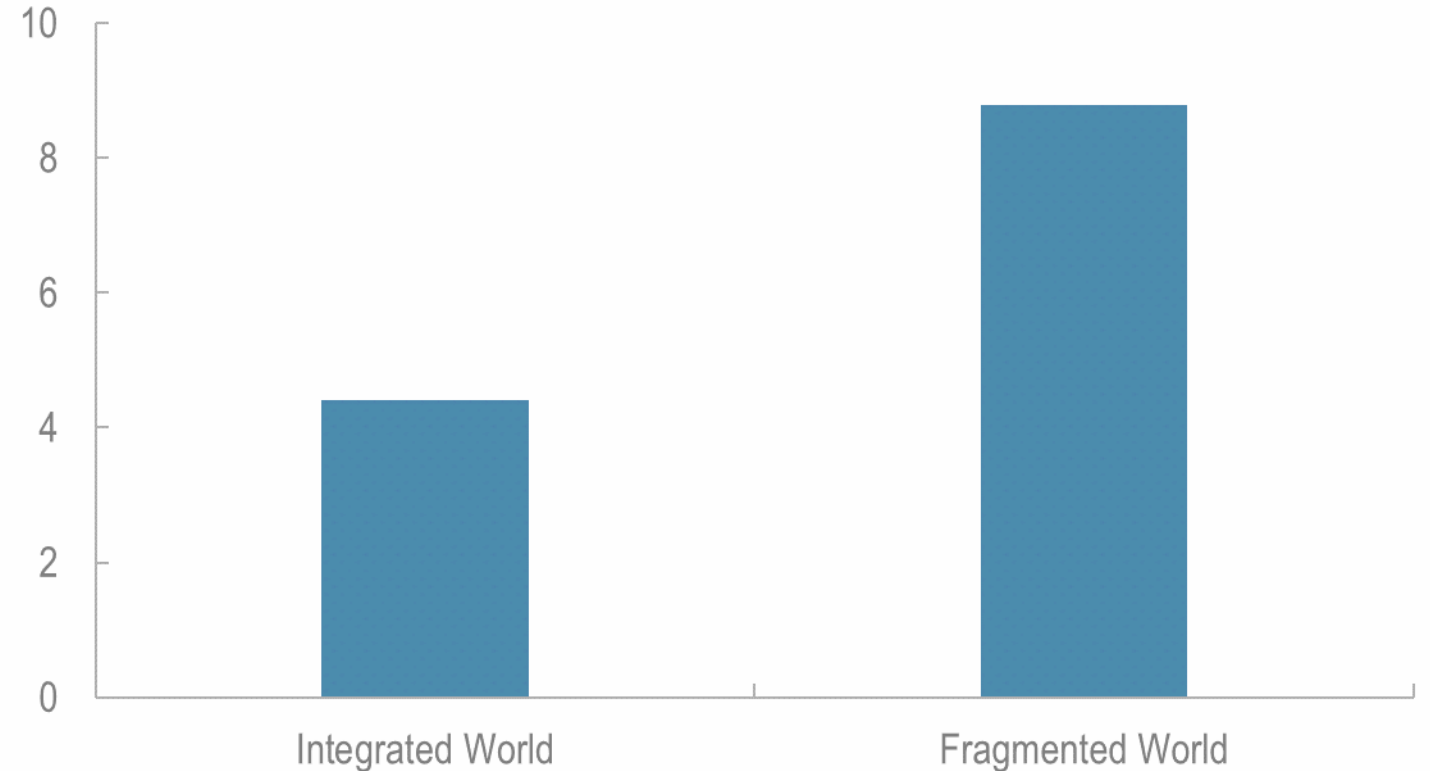
Sources: Bailey, Strezhnev, and Voeten (2017); Centre d'études prospectives et d'informations internationales, Gravity database; fDi Markets; and IMF staff calculations.

Note: Figure shows the annual share of total foreign direct investments between country pairs that are similarly distant (that is, in same quintile of distance distribution), geopolitically and geographically, from the United States.

Fragmentation makes the world more vulnerable to shocks

In a fragmented world, a negative supply shock in the U.S. production of wheat would raise its price by about **twice as much** as it would in an integrated world.

Wheat Price Increase in the USA-Europe+ Bloc from Wheat Harvesting Shocks in an Integrated versus Fragmented World
(Percent)

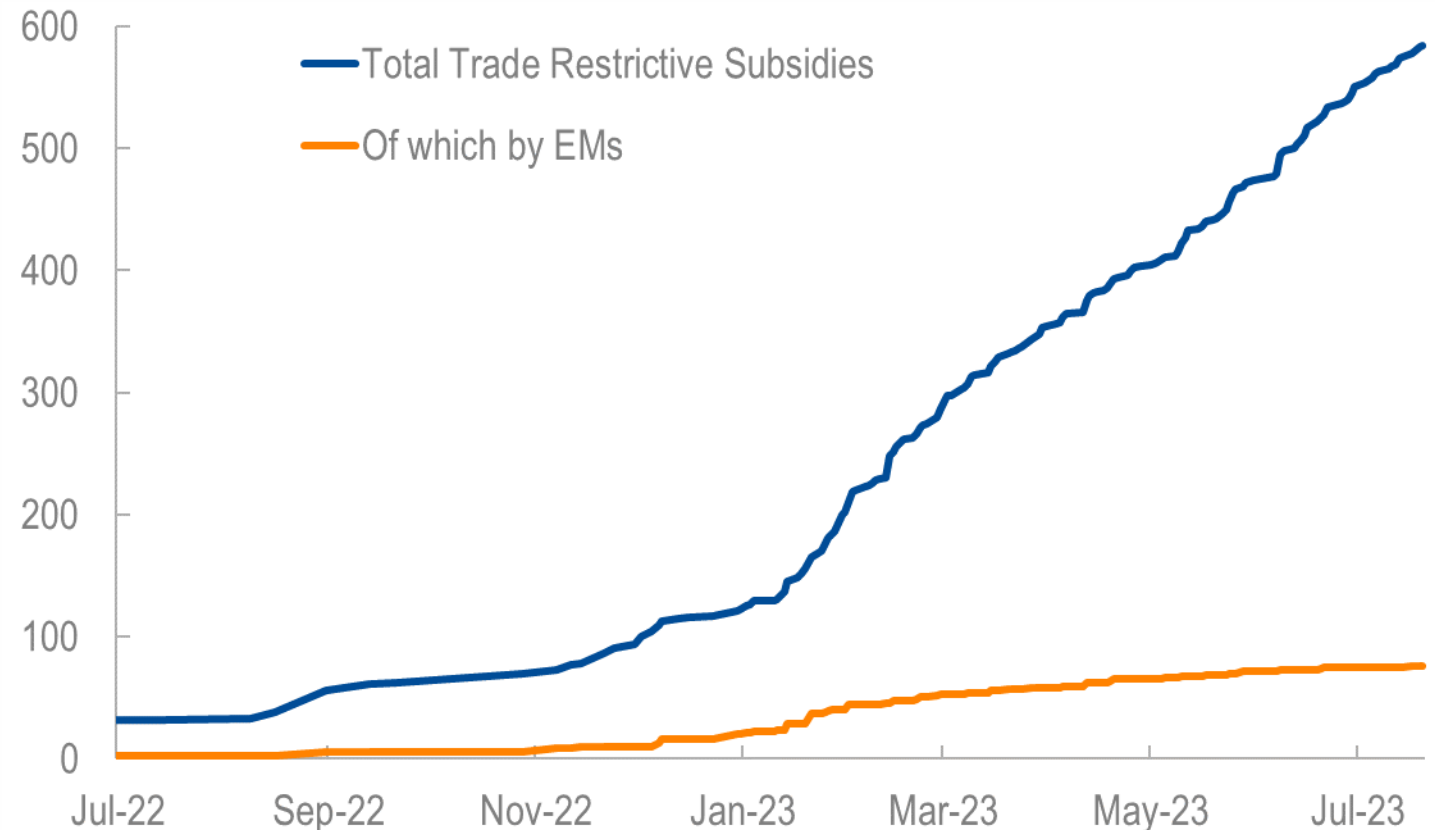


Sources: Food and Agriculture Organization of the United Nations; and IMF Staff calculations.
Note: The bars describe the change in the price of wheat in the USA-Europe+ bloc from a three-standard deviation negative shock to USA wheat production. The graph compares the price increases in the bloc in a free-trade world versus a fragmented world.

Countries are turning inwards and engaging in large-scale industrial policies

Over the past year, there has been a **fivefold increase in new trade-restrictive subsidies** in AEs.

New Industrial Policies in EMs and AEs
(Number of measures)



Sources: Global Trade Alert - New Industrial Policy Observer, August 2023
Note: EU-wide measures counted only once.

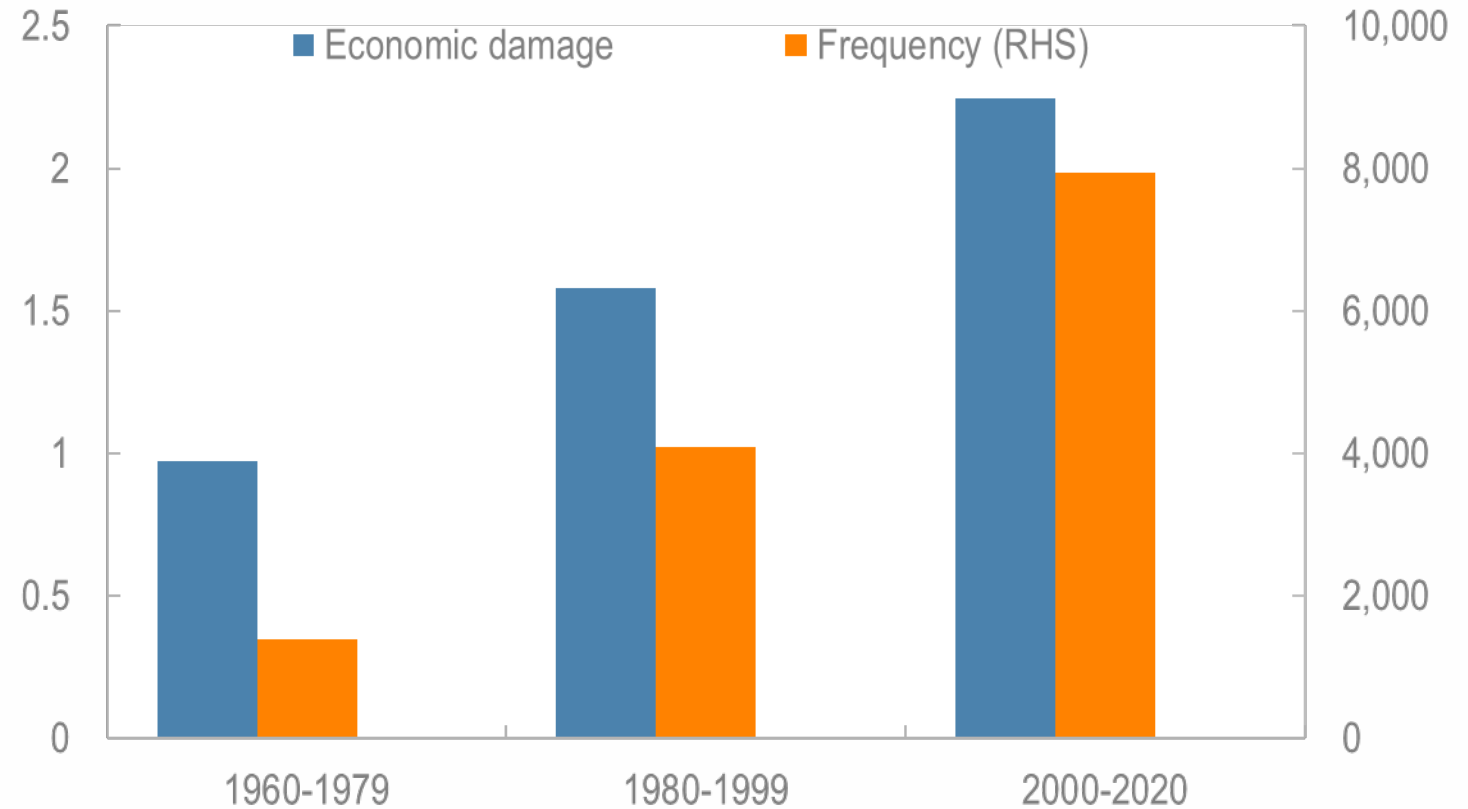
Climate change is inflicting growing economic costs

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Large natural disasters are becoming more frequent and costly

Climate-related Disasters

(Economic damage in percent of countries GDP (simple average), frequency in total number recorded)

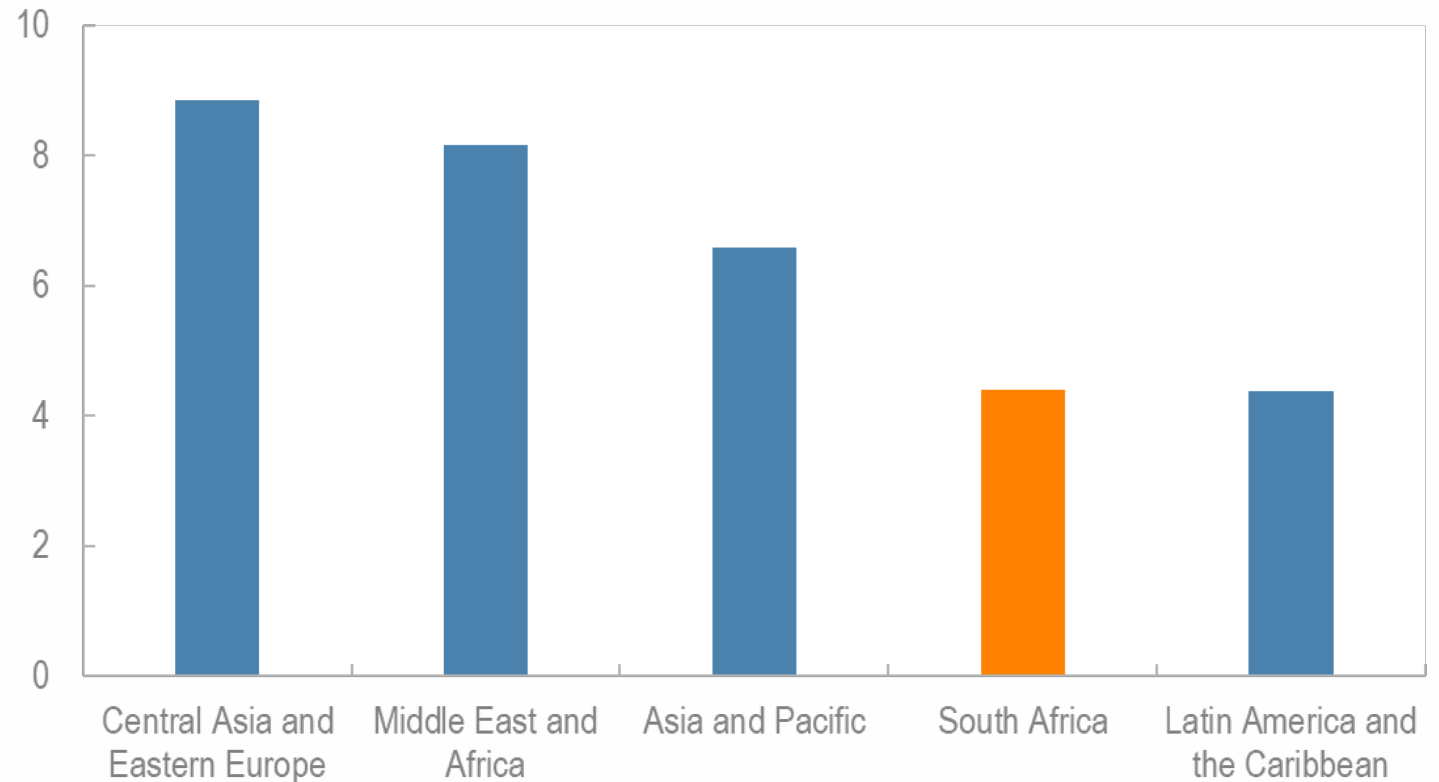


Sources: Our World in Data based on raw disaster data published by EM-DAT, CRED / UCLouvain, Brussels, Belgium – www.emdat.be (D. Guha-Sapir).

Addressing climate change will be very costly

Climate infrastructure investment needs for South Africa are estimated at **4.4 percent of GDP** per year between 2022 and 2050

EMDE Annual Climate Infrastructure Investment Needs, 2021-50
(Percent of GDP, 2022-50 for South Africa)



Sources: IMF GFSR (2022); Climate Policy Initiative (2021); Emissions Database for Global Atmospheric Research; Emissions Database for Paris Reality Check; Era Global Supply Chain Database; Notre Dame Global Adaptation Index; World Bank (2019); World Bank Carbon Pricing database; World Economic Outlook database; and IMF staff calculations.

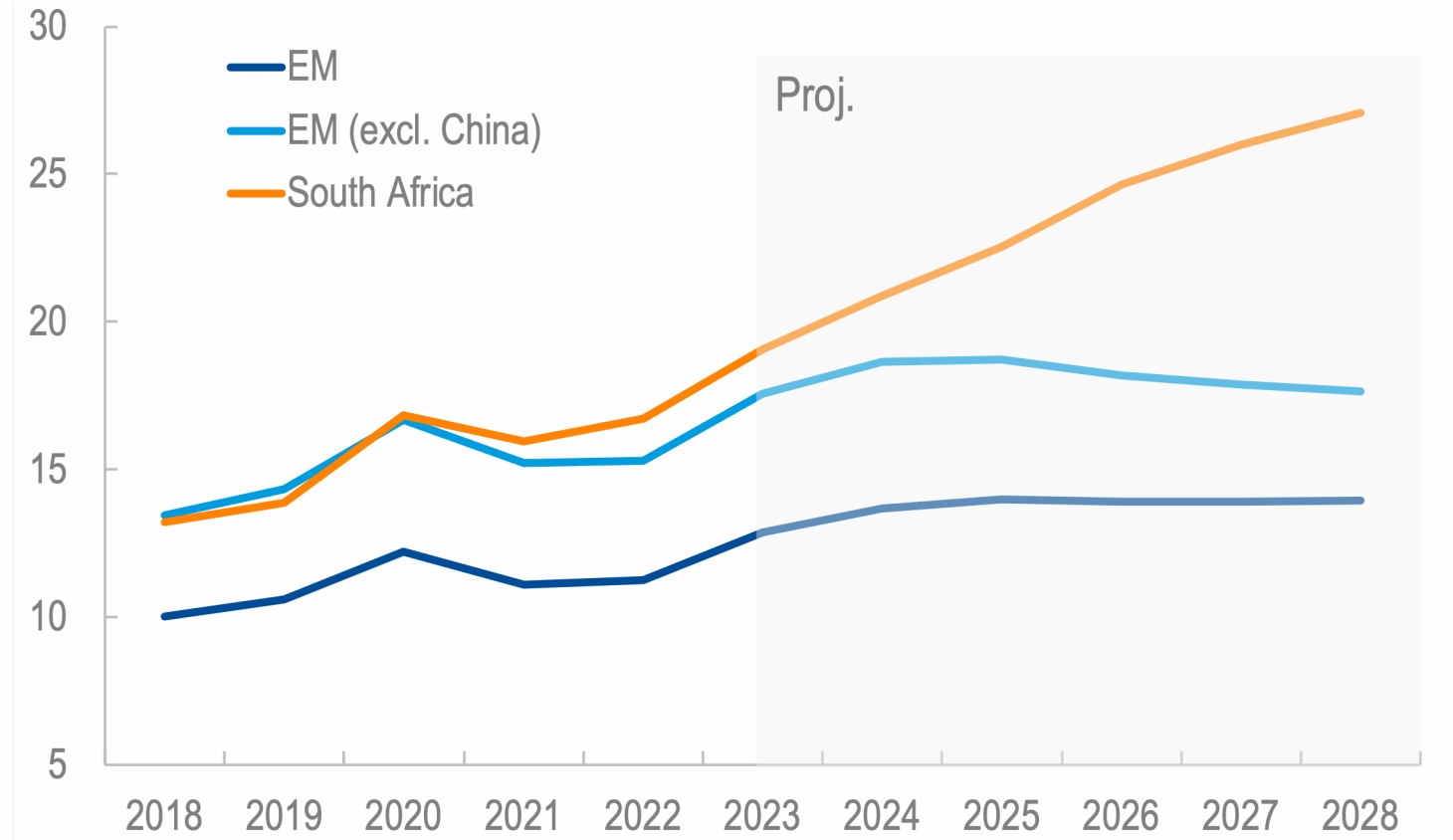
Note: Investment needs for both mitigation and adaptation.

How can EMs succeed in this difficult new environment?

#1 Accelerate domestic resource mobilization and rebuild fiscal buffers

Interest payments on public debt owed by EMs are set to rise significantly, from **11% of revenue in 2019** to **14% in 2028**

Government Interest Expense to Revenue
(Percent, weighted by GDP in PPP)



Sources: IMF World Economic Outlook, IMF staff calculations.

#2 Enhance resilience to fragmentation through diversification and reforms

#2 Implement a fiscally and socially sustainable climate strategy

