CHAPTER III

Regional developments and outlooks

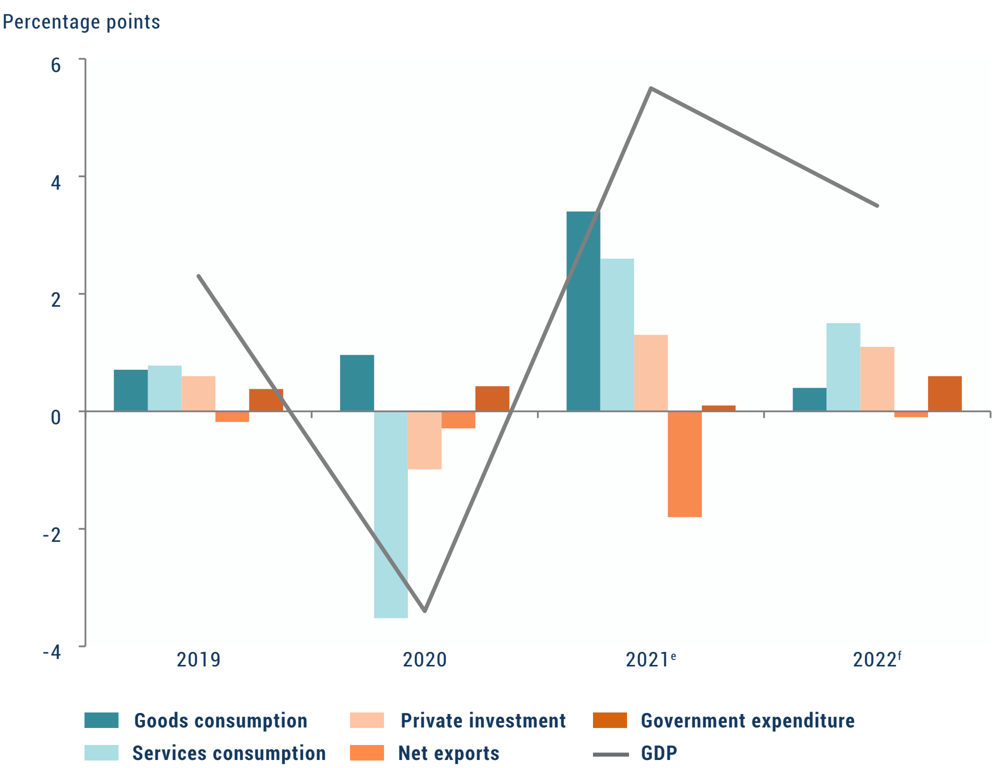
Developed economies

- Economic sentiment has improved as vaccination progresses in major developed economies.
- Employment challenges continue with certain sectors experiencing acute labour shortages.
- Inflationary pressures persist amid prolonged supply-chain disruptions; this may further intensify inflationary expectations in some developed countries.

United States: a robust recovery facing supply-side constraints

The economy in the United States grew by an estimated 5.5 per cent in 2021 after a contraction of 3.4 per cent in 2020. A rapid vaccine roll-out and the relaxation of pandemic control measures substantially improved overall economic sentiment and resulted in a quick recovery of output. The current recovery is imbalanced, however, with consumption of goods driving GDP growth (figure III.1).

Figure III.1
The contribution of demand components to GDP growth in the United States



Sources: United States, Bureau of Economic Analysis, Department of Commerce, and UN DESA estimates and forecasts.
Note: e = estimates, f = forecasts.

An imbalanced recovery is overly dependent on goods consumption

A recovery in services consumption accelerated towards the end of 2021 while recovery in investment expenditure was robust. Expenditure on equipment and intellectual property products such as software and research and development registered a rapid climb. In contrast, expenditure on non-residential structures remained extremely weak. The contribution of external demand to economic recovery was anaemic. Growth in gross exports of goods and services is projected to be only slightly positive in 2021; a jump in demand for imports resulted in a significant drag on net exports.

The economy faces increasing supply-side constraints

The economy in the United States has faced increasing supply-side constraints that initially emerged from global supply-chain disruptions triggered by the pandemic. Rapid domestic demand recovery exacerbated logistics backlogs in incoming freight and domestic transport networks. A shortage of industrial parts, mostly notably semiconductors, has worsened due to continuing supply-chain bottlenecks, production disruptions in East Asian countries and the quick drawdown of inventories. Parts shortages have hit the automotive industry particularly hard.

Figure III.2
Labour market indicators in the United States

Source: United States, Bureau of Labor Statistics.

Another element of supply-side constraints has been a growing labour shortage. The pace of growth in job openings has consistently been higher than the rate of decline in the unemployment rate; the labour market participation rate has remained lower than the pre-pandemic level (figure III.2). The total non-farm job openings rate hit a historic high of 7 per cent in July and is forecast to remain high. The unemployment rate came down to 4.6 per cent in October, still above the pre-pandemic rate of 3.5 per cent in February 2020. While firms have accelerated hiring, the number of workers who quit their jobs reached a historic high in September 2021. The labour market situation suggests a substantial mismatch between job seekers and firms looking to hire in terms of skills, wages, locations and other working conditions (Lubik, 2021).

Inflationary pressures have been mounting

Along with rising energy prices, domestic supply-side constraints have pushed up prices. The producer price index for final demand increased 8.6 per cent in October 2021 from a year earlier, reflecting higher energy prices and the costs of transportation and warehousing. Nominal wages, in terms of average hourly earnings, registered a 4.8 per cent annual increase in October 2021, well above the pre-pandemic average of 2.4 per cent over the last decade. Although the nominal wage increase is still barely over the core inflation rate of 4.6 per cent in the same month, the wage adjustment to inflation has been noticeably quick. Consumer price inflation is estimated to be 4.3 per cent in 2021.

Policies remain expansionary

Highly accommodative fiscal and monetary policies supported quick recovery as stimulus measures wound down during the second half of 2021. With the expiration of enhanced unemployment benefits in September, the focus of fiscal measures shifted to investment promotion under the Build Back Better Framework.[1] The $1 trillion Infrastructure Investment and Jobs Act was passed by the legislature in November 2021, while the Build Back Better Act, intended to pump $1.7 trillion into the social safety net and climate action, is under legislative review. On the monetary side, the Federal Reserve began to taper its asset purchase programme in November.[2] Policy debate continues regarding the timing of the first policy interest rates hike given inflation prospects.

Growth with a rebalanced demand structure is forecast in 2022

The United States economy is forecast to grow by 3.5 per cent in 2022 amid a rebalancing of demand (figure III.1). Consumption growth is expected to slow; exports are predicted to recover. The consumer inflation rate is forecast at 3.2 per cent with substantial supply-side constraints in the first half of the year. The main downside risks stem from uncertainties regarding the pandemic, inflation prospects and associated monetary policy decisions.

Japan: slow recovery in domestic demand while supply-chain disruptions hit exports

The Japanese economy grew an estimated 2.2 per cent in 2021 after a contraction of 4.6 per cent in 2020. COVID-19 outbreaks and measures to control the pandemic weakened household and economic sentiment, which slowed the recovery of domestic demand during the first three quarters of 2021. Unlike other developed economies, which have witnessed a rapid recovery in residential investment

1 See Zandi and Yanos (2021) for detailed discussions on the macroeconomic impact of the Build Back Better Framework.

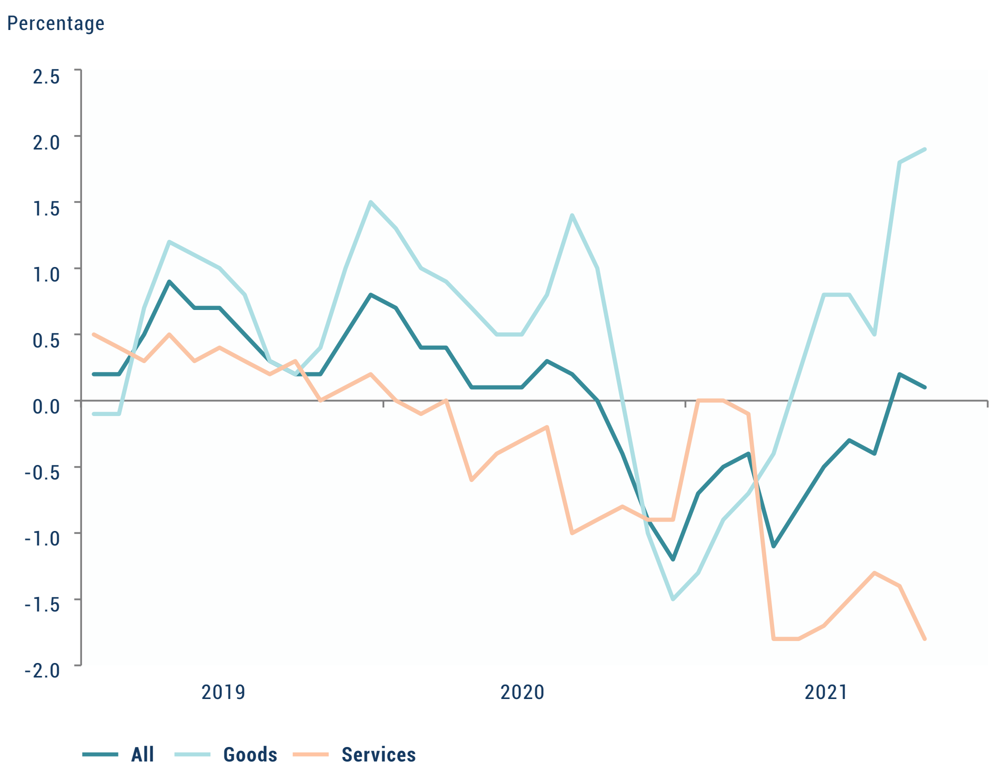
2 See Chapter 2 for details on the asset purchase programmes of central banks during the pandemic.

since mid-2020, residential investment in Japan continued its downward trend since peaking in the third quarter of 2019. In the fourth quarter in 2021, however, a decline in COVID-19 cases and progress on vaccination substantially improved economic sentiment.

Supply-chain disruptions hit the automotive sector

Export growth, the main factor contributing to recovery since the second half of 2020, has lost its momentum. Supply-chain disruptions, particularly semiconductor shortages, compelled the automotive sector to operate under full capacity. Exports of automotive products sharply declined in the second half of 2021. Supply-chain disruptions added inflationary pressure on the prices of goods but this barely offset a persistent deflationary trend, particularly in service prices (figure III.3). Consumer price inflation was an estimated 0 per cent for 2021.

Figure III.3
Inflation trends in Japan



Source: Japan, Ministry of Internal Affairs and Communications.

Expansionary policies contained rising unemployment and bankruptcies

The Government of Japan implemented sizeable fiscal stimulus measures to minimize the impact of the pandemic. The additional stimulus package for the 2021-2022 fiscal year was 40 trillion yen, about 7.5 per cent of GDP. Another package for the 2022-2023 fiscal year amounts to 55.7 trillion yen. Monetary policy continues to be highly expansionary. The Bank of Japan has accelerated its asset purchases along with its existing policy framework for quantitative and qualitative monetary easing with yield curve control. These measures have succeeded in containing rising unemployment and bankruptcies. The unemployment rate peaked at 3 per cent in May 2021 and started declining towards the pre-pandemic rate of 2.4 per cent. Bankruptcy cases have fallen since a peak in July 2020. Policy measures did not induce robust private spending growth in 2021, however.

Robust domestic demand growth is expected in 2022 but downside risks remain

GDP growth is forecast at 3.3 per cent in 2022. Robust domestic demand growth is expected due to increased private consumption reflecting pent-up demand for goods and services. Private investment is also projected to recover along with improving economic sentiment. Both monetary and fiscal policies will likely remain expansionary to support domestic demand recovery. Downside risks stem from uncertainties surrounding the pandemic and supply-chain disruptions. Although the latter have extensively impacted the automotive sector, it is uncertain if they will escalate to broader supply-side constraints.

Australia: strong recovery continues despite a temporary contraction due to Delta variant outbreaks

A strong recovery has resulted in rapid restoration of employment

The Australian economy grew an estimated 3.1 per cent in 2021 after a 2.5 per cent contraction in 2020. A strong recovery in domestic demand promptly led to rapid job recovery in the first half of 2021. The unemployment rate declined to 4.9 per cent in June, below the pre-pandemic level of 5 per cent. During the third quarter, the recovery faced a setback due to outbreaks of the Delta variant of COVID-19, however. The economy shrank on a quarterly basis following stringent lockdown measures in major cities. By the fourth quarter, relaxation of these measures and rapid progress in vaccination restarted economic activities and recovery. Export recovery has gained steam with rising commodity prices.

Robust domestic demand is forecast to continue in 2022

For 2022, the economy is forecast to grow by 4.2 per cent, with robust domestic demand growth. Export growth is projected to accelerate further with a recovery in services trade. Both monetary and fiscal policies are expected to remain expansionary. The Reserve Bank of Australia will probably scale down its bond-buying programme but is not likely to hike its policy rates in 2022 unless rapid wage growth appears. Downside risks stem from uncertainties over the COVID-19 pandemic and global supply-chain disruptions. Compared to other developed countries, however, the impact of the latter is likely to be milder given Australia's service-based domestic demand and commodity-based exports.

Europe: a return to growth but the crisis is not over yet

A strong rebound in the first half of the year, powerful headwinds in the second

The economies of Europe returned to growth in 2021, with the gradual easing of COVID-19 containment measures, continued accommodative macroeconomic policies and a sharp rebound in leading export destinations. Most European economies registered a double-digit year-on-year increase in output in the second quarter; the overall performance of the region in the first half of the year exceeded earlier expectations. Following more than a year of suppression, consumer sentiment improved and private consumption surged as households started to spend savings accumulated due to pandemic-related precautions or limited scope to spend. Amid the reopening of the services sector and lifting of intra-European Union mobility restrictions, economies in countries relatively dependent on tourism, such as Greece, Italy and Spain, saw a sharp increase in tourist arrivals.

In the second half of 2021, however, the region faced serious headwinds. The manufacturing sector, which had recovered to its pre-pandemic level of activity, was severely impacted by supply-chain disruptions in part caused by shortages of shipping containers and lower capacity in Asian ports. Certain industries, in particular the automotive industry – which is of crucial importance for many economies in Europe, including the largest, Germany – have been forced to scale back production because of the global semiconductor shortage. Further, many industries and services have confronted a large-scale lack of workers, especially truck drivers. Supply disruptions and rising costs of input materials brought the construction sector in Europe to a standstill in late 2021. Soaring energy prices, especially for natural gas and LNG,[3] caused a spike in electricity costs and became another hurdle to economic recovery, disrupting output in energy-intensive firms. The Economic Sentiment Indicator for both the euro area and the European Union stabilized at a high level in July after rapidly improving since January 2021 (figure III.4).

The German economy has not regained its pre-crisis size and is expected to expand by only 2.5 per cent in 2021. Growth sharply slowed in the third quarter due to sluggish industrial activity and interruptions in automotive sector output. Disruptions in the supply of intermediate goods were accompanied by rising electricity prices, and in September, producer prices increased by over 14 per cent year on year. Growth should accelerate to 4 per cent in 2022 given an improved outlook for exports and domestic investment, the insourcing of the production of semiconductors and other key inputs, and the gradual shift towards European production chains. An expected increase in the minimum wage should support private consumption. The economy, however, faces medium-term risks associated with slow progress in shifting towards the production of electric vehicles as well as demographic pressures.

Most European countries have accomplished relatively high vaccination rates against COVID-19. Yet, another surge in cases began in the fall of 2021, making the region an epicentre of the pandemic once again. This led to the reintroduction of containment measures in Austria, Denmark, Latvia, the Netherlands and Slovakia. These measures may again disrupt service sectors such as leisure, hospitality and travel. A return to the prolonged full-scale lockdown adopted in 2020 remains unlikely, however.

3 The natural gas price increase in Europe in the second half of 2021 was caused by insufficient domestic storage, declining imports from the Russian Federation, a sharp increase in LNG demand from Asia and the shift from long-term gas purchase contracts to spot markets.

Figure III.4

Economic sentiment indicator for the European Union and the euro area

Source: European Commission, 2021.

The consequences of Brexit weighed on production activities in the United Kingdom, despite the Trade and Cooperation Agreement reached with the European Union in 2020. Numerous non-tariff barriers emerged in trade between the two, while significant uncertainty remains around trade in services. After a double-digit year-on-year expansion in the second quarter of 2021, economic growth in the United Kingdom noticeably slowed amid supply-side and fuel shortages. Difficulties in bringing in migrant workers to meet labour demand, a problem that to a certain extent resulted from Brexit,[4] contributed to persistent supply-side bottlenecks.

A massive recovery plan to improve long-term growth prospects

The outlook for European economies for 2022 is mixed, as the weaknesses of late 2021 will carry on to at least the first quarter. Headline growth may taper somewhat due to the weaker base effect and the start of the gradual unwinding of anti-crisis stimulus measures. On the positive side, the European Union will begin benefiting from the largest stimulus package implemented in decades – the combination of the European Community's long-term multi-annual budget running from 2021 to 2027 and the massive Recovery and Resilience Facility, the NextGenerationEU. The latter, worth over 800

4 Although over 6 million foreign workers applied for residency in the United Kingdom after Brexit, many have left the country. In 2020, the net migration of European Union nationals to the United Kingdom was negative. See ONS, 2021.

billion euros, is financed by joint debt issuance. Implementation of the recovery plan, with spending focused on sectors with high growth multipliers, should facilitate the modernization and digitization of infrastructure, bolster research and innovation, expedite the shift towards a sustainable economy, address social problems such as youth unemployment and improve the efficiency of governance. Actual impacts will of course depend on the ability of national governments to use allocated funds.

The aggregate GDP of the EU-27, after shrinking by 6 per cent in 2020, bounced back by an expected 4.7 per cent in 2021. It may be followed by a further 3.9 per cent expansion in 2022, assuming that prolonged lockdowns are not resumed. European Union member States from Eastern Europe are projected to maintain a positive growth differential with their West European peers. Among European countries not in the European Union, the economy of the United Kingdom expanded by an estimated 6.2 per cent in 2021 and is expected to see further growth of 4.5 per cent in 2022. Despite difficulties in late 2021, the outlook for the economy in the United Kingdom is positive. Most of the corporate sector is in a strong financial position, and a two-year tax deduction incentive should encourage investment.

From battling deflation to dealing with inflation worries

Consumer price inflation turned negative in many European countries in 2020. It remained subdued in early 2021 but accelerated markedly in the second half of the year (see Figure III.5). Even in countries with a long record of price stability, annual inflation exceeded 4 per cent in the final quarter of the year, much above the European Central Bank's (ECB) 2 per cent target. Apart from the base year effect, including from a temporary reduction in the value added tax in Germany, the surge in inflation is explained by various factors. These include higher producer prices caused by skyrocketing costs of raw materials and energy, a sharp rise in food prices and persistent supply-chain disruptions. In Eastern European countries with flexible currencies, depreciation added to inflationary pressure. To mitigate the impact of higher gas and electricity prices on households and businesses, several European countries, including France, Italy and Spain, adopted various measures to curb them. In July 2021, the ECB announced that it will tolerate overshooting the inflation target. Most inflationary factors are believed to be transitory; however, a longer-than-anticipated period of above-target inflation may lead to a second-round effect on labour markets and a wage-price spiral.

Employment is recovering; many countries are facing worker shortages

Labour market conditions notably improved in 2021, with a robust increase in working hours in most countries. In the Czech Republic and Germany, unemployment fell to low single-digit levels, while it remains elevated in Greece and Spain. Phasing out furlough schemes implemented in several countries since the beginning of the pandemic may lead to a modest rise in unemployment, but in general, the European economy should add jobs over the next couple of years. Labour demand is expected to strengthen. Several European countries confront labour shortages causing significant logistical bottlenecks and reflecting persistent mismatches between labour supply and demand and different speeds of recovery across sectors (see Chapter 1). Although immigration remains a politically contentious issue, a long-term, comprehensive immigration strategy for bringing in skilled workers may mitigate labour supply pressures. Removing obstacles to internal mobility that emerged from the pandemic may also address labour shortfalls in some countries. Given that virtually all European Union countries are facing demographic shifts, however, alleviating labour shortages in one country via intra-European Union migration would most likely exacerbate shortages in others.

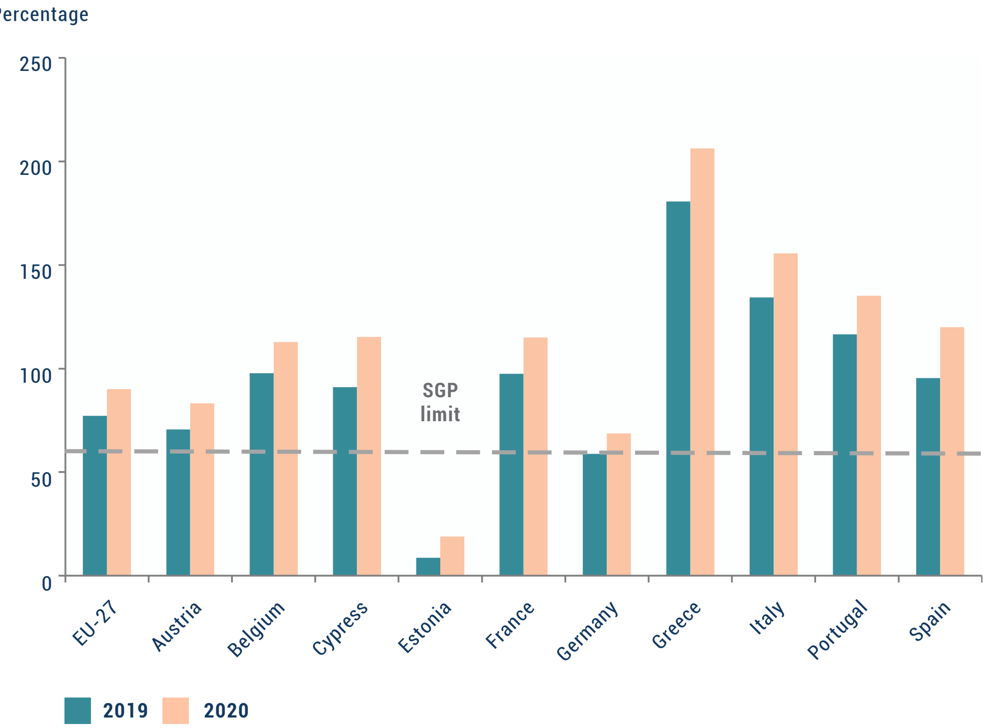
Figure III.5
Annual change in the Harmonized Index of Consumer Prices for select European countries

Source: Eurostat.

A gradual shift to fiscal consolidation

Macroeconomic policies in Europe largely maintained their accommodative stance in 2021, with continuing liquidity and wage support schemes. As an outcome of massive stimulus spending, public debt levels soared in some countries, far exceeding limits set by the Stability and Growth Pact (see figure III.6). Ceilings on the size of budget deficits and public debt were earlier put on hold by the European Commission when it activated the pact's escape clause. Most European countries will nevertheless start putting their public finances in order beginning in 2022. The pace of fiscal consolidation will likely be gradual and decided at a national level. Stronger growth rates will have a modestly positive effect on debt ratios while financing costs should remain low. For the United Kingdom, exiting the European Union allowed greater fiscal flexibility, and the proposed budgetary framework up to 2025 remains accommodative. The ability to borrow in British pounds and the accommodative stance of the Bank of England are expected to provide sufficient fiscal space to support growth.

Figure III.6
Gross public debt-to-GDP ratio for select European countries



Source: Eurostat.
Note: SGP refers to the Stability and Growth Pact.

The ECB's asset purchases are to be scaled down; Eastern Europe tightens policy

Following the enactment of massive anti-crisis liquidity support schemes, central banks in Europe are expected to start gradual monetary policy normalization. The key policy rates of the ECB, the interest rate on the main refinancing operations and the deposit rate, are likely to be maintained at 0 per cent and minus 0.5 per cent, respectively, at least until early 2023. By contrast, the main policy tool of the ECB since 2020,[5] asset purchases, is expected to be scaled down starting in 2022.[6] The reduction in monthly asset purchases will take place gradually to avoid raising long-term interest rates and prevent disruptions in financial markets. The ECB's balance sheet will likely retain its size in the medium term, with reinvestment of payments from maturing securities.

Outside the euro area, in Sweden, the Riksbank completed its asset purchases by December 2021. In Denmark, where the Government entered the crisis with a large liquidity buffer, the Central Bank, after a series of currency interventions, has reduced the already negative key interest rate further to curb appreciation pressures, defending the peg to the euro. In Eastern Europe, inflation rates not seen for over a decade and concerns about rising inflationary expectations prompted sharp interest rate hikes in the Czech Republic, Hungary, Poland and Romania. In European countries outside the

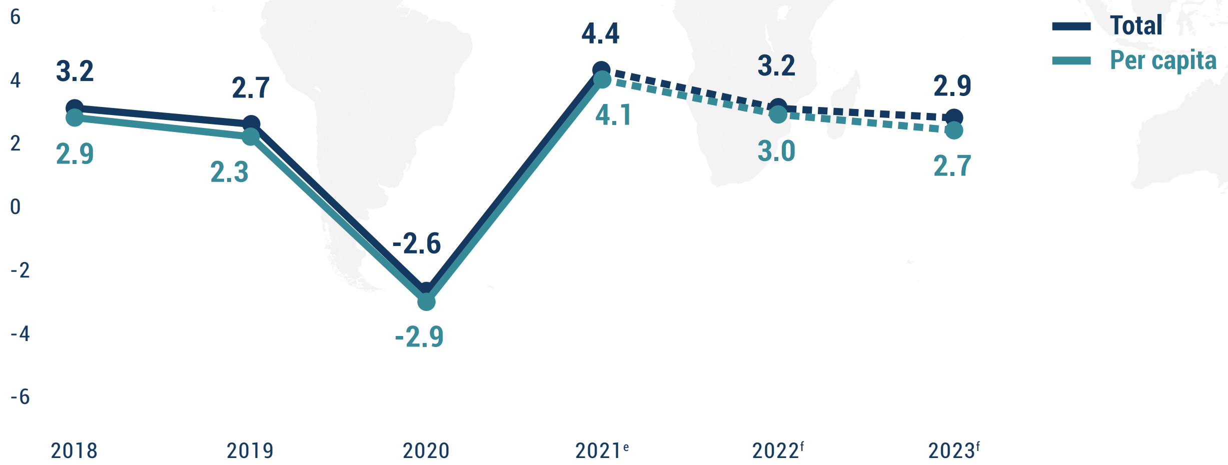
5 The ECB is running two asset purchase programmes: the Pandemic Emergency Purchase Programme to be phased out in March 2022 and the smaller Asset Purchase Programme.
6 The volume of newly issued sovereign bonds is also expected to shrink along with planned reductions in budget deficits.

European Union, the Bank of England has announced that it plans to begin slowing its asset purchases once interest rates reach 0.5 per cent. Continued favourable monetary conditions in Europe will give a respite to the corporate sector, given elevated business indebtedness. On the other hand, monetary authorities should acknowledge the risks from credit misallocation and elevated asset prices, which could produce unanticipated and sharp price corrections.

Economies in transition

GDP growth

Percentage



COVID-19 cases & deaths

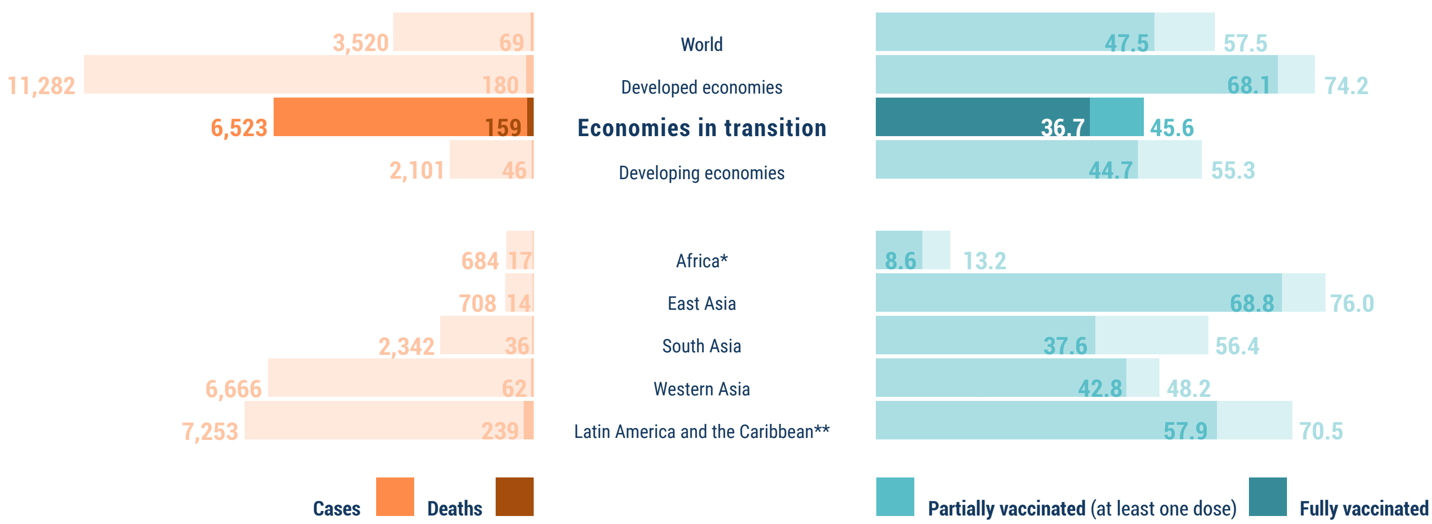
as of 20 December 2021

Per 100,000 people

Vaccination

as of 20 December 2021

Percentage of population



Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. The map represents countries and/or territories or parts thereof for which data is available and/or analysed in World Economic Situation and Prospects 2022. The shaded areas therefore do not necessarily overlap entirely with the delimitation of their frontiers or boundaries. Aggregate data for Africa, excluding Libya.

* Excluding Libya; **Excluding Bolivarian Republic of Venezuela. **e:** 2021 estimates. **f:** 2022-2023 forecasts.

Source for COVID-19 data: UN DESA calculations, based on data from Johns Hopkins University.

Economies in transition

- The Commonwealth of Independent States (CIS) and South-Eastern Europe returned to growth amid the lifting of pandemic containment measures, higher commodity prices and an improved external environment.
- Surging inflation is hurting living standards, prompting monetary tightening in the CIS.
- Official development assistance remains important for parts of the region.

The Commonwealth of Independent States and Georgia: the lifting of restrictions and higher commodity prices underpin an economic rebound

Economic growth in the CIS area, including Georgia, resumed in 2021 following contraction in 2020. The turnaround picked up as mobility and activity restrictions were eased or removed. A more favourable external environment, including sharp rises in commodity prices, boosted export volumes and revenues. Services also bounced back while construction activities benefited from support programmes in the Russian Federation and higher remittances sent to Central Asian countries. Better terms of trade for energy-exporting countries improved their current account positions, despite the recovery of imports. In energy-importing countries, remittance flows and tourism revenues along with rebounding domestic demand mitigated current account pressures from import growth.

Private consumption remains the major driver of growth

Growth in the CIS area in 2021 was largely driven by consumer demand, amid raising employment levels, increased retail lending and higher remittances to smaller CIS countries. Investment generally trailed behind amid high uncertainty and subdued foreign direct investment inflows. The relaxation of oil output restrictions under the OPEC Declaration of Cooperation,[7] along with elevated prices for oil and natural gas in late 2021, accelerated recovery in energy-exporting countries.

In the Russian Federation, the main impetus for growth came from the rebound in household spending, boosted by one-off social payments and wage growth due to tight labour market conditions. Investment activity also picked up. The Government launched multiple stimulus packages in 2020-2021, including tax deferrals and guarantees, equivalent to about 6 per cent of 2020 GDP. Despite higher export revenues, protection of reserve buffers against possible external shocks remains a priority. International reserves rocketed to historically high levels in 2021, virtually eliminating debt service risks.[8] That same year, the United States and the European Union introduced additional economic sanctions against the Russian

7 The Declaration of Cooperation is a coordination mechanism for crude oil production by both OPEC member countries and 11 non-OPEC member countries. It is referred to as “the OPEC Plus agreement”. See OPEC (2021) for details.

8 In late 2021, international reserves of the Russian Federation exceeded total external debt by around one third.

Federation, in particular forbidding banks based in the United States to purchase Russian sovereign debt on the primary bond market. The decline in the share of non-residents in the Russian domestic bond market was rather limited in 2021, however. The Government in any case was able to issue debt denominated in the local currency and borrow from domestic banks. Economic growth is likely to moderate from the estimated 4.2 per cent in 2021 to 2.7 per cent in 2022 as the Government moves towards fiscal consolidation. The ambitious $360 billion National Development Projects Plan, comprising large investments in infrastructure and the social sphere, was postponed.

In Ukraine, a good harvest, higher steel prices and a surge in construction boosted output in 2021. Economic potential is constrained by the conflict in the East, however, as well as a challenging business environment and large-scale emigration. IMF lending will be important for meeting external debt service obligations in 2022. In Belarus, despite the absence of generalized lockdown measures, domestic demand remained weak amid political tensions. Exports performed well, supported by higher prices for refined oil products and fertilizers, despite sanctions imposed on the country in 2021 by several parties, including the European Union.

In Central Asia, the rebound in remittances in 2021 spurred private consumption; most countries registered high growth rates. Poor performance of the gold sector dampened recovery in the Kyrgyz Republic, however. Pandemic-related restrictions introduced by China in 2020 damaged cross-border trade with Kazakhstan, Kyrgyzstan and Tajikistan, affecting many small businesses.

Following the rebound in 2021, output growth in the CIS area is expected to decelerate in 2022, given weaker base effects, the moderation of consumer demand, more restrictive macroeconomic policies and persistent structural constraints. Without more ambitious reforms, growth will settle around moderate pre-pandemic expansion levels. The aggregate GDP of the CIS and Georgia, after a 2.6 per cent contraction in 2020, increased by an estimated 4.3 per cent in 2021 and is forecast to rise by 3.2 per cent in 2022. Integration processes within the framework of the Eurasian Economic Union[9] are expected to continue, including for financial systems.

Vaccination against COVID-19 is progressing slowly

Vaccination rates in the region remain relatively low, rendering it vulnerable to further waves of infection. In late 2021, the situation in the Russian Federation sharply deteriorated, prompting a one-week lockdown. COVID-19 cases also spiked in Georgia and Ukraine.

Labour markets have improved

Unemployment in the CIS area declined through 2021, approaching pre-pandemic levels in the best-performing countries. They include the Russian Federation, where limited inflows of migrants added to the tightness of labour markets, and numerous sectors such as construction saw shortages of workers. The unemployment rate declined to a record low of 4.3 per cent in September. Authorities relaxed some restrictions imposed earlier, such as by lifting entry bans on Tajik and Uzbek citizens who had committed minor violations.

9 Eurasian Economic Union members are Armenia, Belarus, Kazakhstan, Kyrgyzstan and the Russian Federation. Cuba, Moldova and Uzbekistan are observers.

An upsurge in inflation is eroding living standards

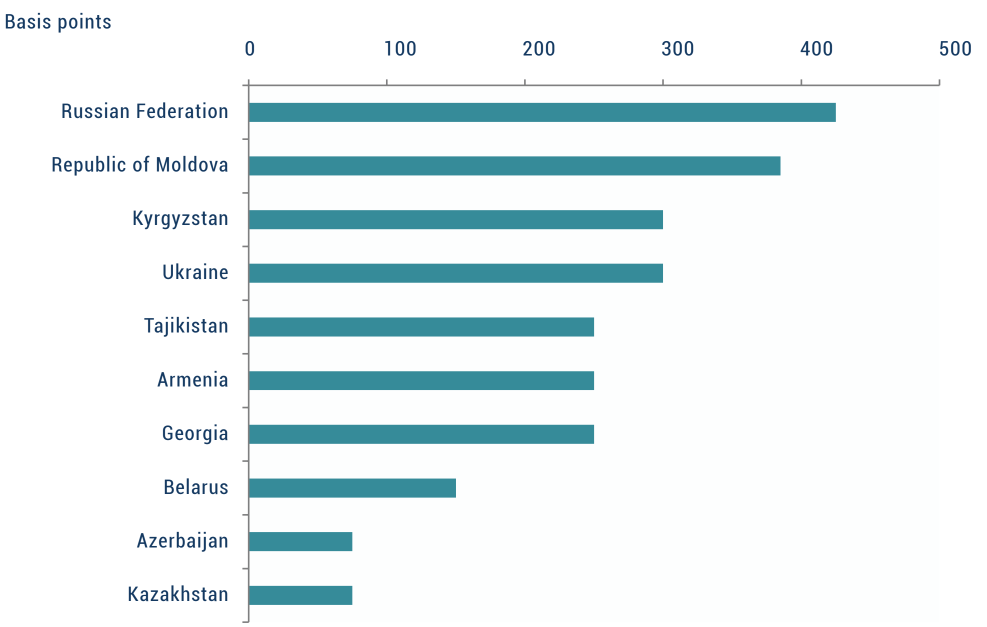
Most of the CIS area experienced a strong upsurge in inflation in 2021, which reached double-digit levels in many countries. The upswing resulted from a combination of supply disruptions, higher food and energy prices, strengthened demand and, in some cases, past exchange rate depreciation. It also came from elevated inflationary expectations and accelerated purchases. Governments responded in various ways. Kazakhstan introduced price controls and export quotas to contain food price pressures. In the Russian Federation, export duties, price controls and agreements with producers were deployed to limit price hikes. In most of the region, inflation is expected to moderate in 2022, except for Moldova, where increases in natural gas tariffs in late 2021 will lead to a double-digit annual consumer price increase.

Monetary policy is significantly tightening

Monetary authorities reacted to the inflationary spike by tightening policies. Interest rate increases in 2021 were substantial, with a series of successive hikes in virtually all countries (see figure III.7). Despite tighter monetary policy, retail lending, in particular mortgage lending, grew rapidly, supporting the recovery of demand. In the Russian Federation, the Central Bank announced plans to curb lending growth in late 2021; a tight monetary policy is expected to continue in 2022 amid concerns about high inflationary expectations.

Figure III.7

Changes in benchmark monetary policy rates in the CIS and Georgia since January 2021



Sources: National central banks data as of 20 December 2021.

The crisis leaves a legacy of public debt

Fiscal policies, although less expansionary than in 2020, have continued to support recovery. Public revenues increased as growth resumed, often exceeding earlier expectations. In the Russian Federation, the deficit fell sharply in 2021 on the back of growing revenues and the return to fiscal consolidation, implying a less supportive fiscal impulse. A tighter fiscal stance is anticipated in 2022, when the fiscal rule is expected to be reinstated. Although public debt in the Russian Federation remains low, at around 20 per cent of GDP, for many other CIS economies, especially energy importers, the crisis has left higher public indebtedness. In Kyrgyzstan, for example, the public debt-to-GDP ratio increased from 54.1 per cent of GDP in 2019 to 68.1 per cent in 2020. The composition of the debt, with a significant share of official financing, represents a mitigating risk factor in the most vulnerable countries. Official financing, critical at the height of the crisis in 2020, remains important, as the recovery of private flows has been limited. Countries from the region have retained good access to international capital markets, however, with a spate of well-received Eurobond issues. The new allocation of the IMF's Special Drawing Rights has alleviated financing needs for many countries, including Ukraine, and helped rebuild reserves.

Looking forward, the region faces multiple downside risks. Volatile commodity prices, especially of oil and natural gas, will remain a major determinant of economic performance. Slow progress in vaccination may lead to a rise in new COVID-19 cases. Mounting geopolitical tensions, internal political strife and the potential for refugee flows from Afghanistan into Central Asia could heighten instability, undermining business and consumer confidence. The banking sector has fared relatively well during the COVID-19 crisis but may come under stress in some countries as temporary forbearance measures are withdrawn and the share of non-performing loans rises, particularly in Ukraine. Persistent price pressures may unleash expectations of rising inflation, leading to quicker policy tightening and domestic tensions.

Box III.1

Sustainable finance in the Commonwealth of Independent States and Georgia

New financial products worldwide are supporting the shift towards sustainable development. This wave of innovation has been accompanied by reflection on the role of financial regulators in both actively contributing to climate change mitigation and adaptation and addressing related risks to the financial system. Sustainable finance is highly relevant for CIS countries, given the importance of hydrocarbons for their economies, including for non-energy-exporting economies through remittances, trade and investment channels, and the related costs of the green energy transition.

Green bonds, where proceeds are used for environmental goals, account for most new offerings. After a slow start compared with other emerging markets, the pace of issuance has picked up. Several financial institutions in Armenia and Kazakhstan and non-financial corporations based in Georgia debuted new products in 2020. Overall issuance in the first nine months of 2021 reached record levels (figure III.1.a). Corporations have pioneered these new financial products and, in line with other emerging markets, financial institutions have been major players. In July 2021, Uzbekistan broke new ground with a sovereign Sustainable Development Goals bond, where proceedings will be allocated to education, water management, health and green transportation, among other ends. The city of Moscow in the Russian Federation issued the first subnational green bond to finance infrastructure projects that reduce air pollution from transport.

New sustainable financial instruments have been accompanied by increased product diversification. For example, some Russian companies in extractive sectors have issued loans linked to sustainability, where interest paid is linked to meeting specified environmental targets. This approach gives issuers more flexibility, as the use of proceeds is not tied to particular projects. Perpetual bonds have been issued by Russian Railways to finance green projects, first in 2020 in the domestic market and then in 2021 in the Eurobond market. While few projects are fully green, the potential pipeline of investable initiatives that could reduce environmental footprints is large. So-called transition bonds, which provide finance for emissions-intensive sectors to meet specific performance criteria, could be of particular interest to the region.

Given the frequent absence of clear comparators, it is difficult to make strong statements on a "greenium" or cost-of-financing advantage. Recent issues have attracted strong investor interest, which has translated into high levels of oversubscription. This has lowered prices and opened access to a broader investor base, which tends to reduce volatility.

From the point of view of issuers, launching a green or sustainable bond has a significance beyond raising revenues at an expected lower financial cost. It allows them to engage with investors and, in the case of corporations, consumers, and to signal their efforts to adopt more sustainable practices and business models. Wide acceptance of these bonds requires alignment with well-established criteria around how proceeds can be used and the existence of suitable monitoring mechanisms, however. According to common practice, issuers have put in place frameworks that detail revenue use and are verified by external parties, but this is a source of additional costs that may deter issuance.

Different forms of financial support have encouraged the development of green finance. For example, under certain conditions, the costs of assessing green bond alignment with globally accepted standards are reimbursed by the Astana International Financial Centre, which aims to become a regional leader in green finance. In the Russian Federation, subsidies to cover part of the cost of the coupon are provided by the national ecology programme. International organizations and multilateral development banks have played roles as anchor investors (European Bank for Reconstruction and Development), helped to identify suitable projects to finance (United Nations Development Programme) or even issued green bonds in domestic markets to raise funding in local currency (Asian Development Bank).

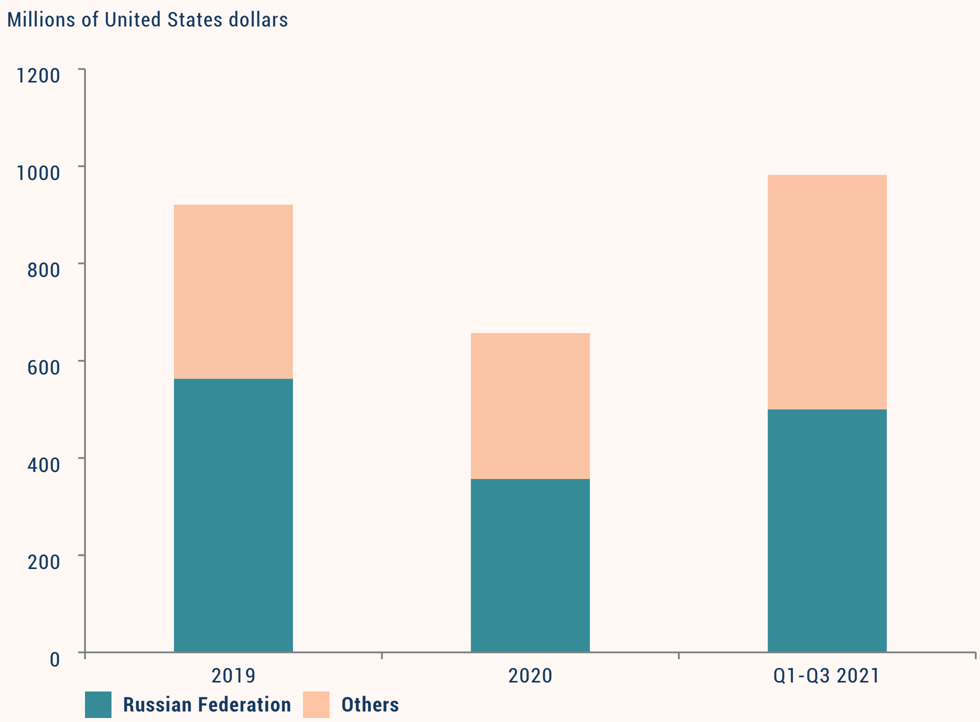
For most countries in the CIS, issuance in external markets is the rule as the investor base for domestic launches remains limited. This relates to the lack of awareness of green instruments among domestic investors but also to shallow domestic capital markets. Judging by developments in other countries and ongoing regulatory initiatives to support demand, green and similar bonds are expected to account for an increased share of total issuance in the future. They still add to the debt burden of issuers,

Author: José Palacin, United Nations Economic Commission for Europe

however, and, in most cases, to their foreign currency exposure. These risks need to be understood and managed, including through regulatory actions to ensure transparency and promote demand. More general initiatives are required to foster domestic capital markets. While sustainable finance carries transformative potential, critical constraints could relate to the appropriate pricing of externalities and regulatory reforms in relevant sectors.

Figure III.1.a

Green bond issuance in the CIS and Georgia



Sources: International Finance Corporation, Amundi, Bloomberg, Climate Bonds Initiative and Environmental Finance.

South-Eastern Europe: growth returns to the region

Economic growth returned to South-Eastern Europe in 2021 after a COVID-19-induced recession in 2020. An improved external environment was a major driver of recovery in these open economies with strong links to the European Union through trade and remittances, and, in the case of Albania and Montenegro, large dependence on the tourism sector. In Serbia, the largest economy in the region, the economy expanded by more than an estimated 6 per cent in 2021 amid soaring private investment and exports. Consumer confidence in South-Eastern Europe has markedly improved; macroeconomic policies have been generally supportive. Investment remained comparatively weak, although in Albania, post-earthquake reconstruction will continue to contribute to recovery. In late 2021, some countries experienced an energy supply crisis induced by the increasing cost of natural gas, leading to more use of coal along with higher prices for it. The pace of economic expansion may slow somewhat in 2022, as fiscal support unwinds to stabilize debt ratios. Aggregate GDP in South-Eastern Europe, after contracting by 3.1 per cent in 2020, is projected to increase by 6.2 per cent in 2021 and a further 4 per cent in 2022.

After years of low inflation, consumer prices have increased

After years of moderate price increases, inflation pressures have returned to the region, driven by the sharp acceleration in food and energy prices and, to a lesser extent, stronger consumer demand. Higher inflation has offset most nominal wage growth and worsened social conditions, with food accounting for up to 30 per cent of consumption spending. Price increases have been steeper in Serbia, while in Bosnia and Herzegovina and Montenegro, a deflationary trend ended. Formal or informal currency pegs constrain monetary policy in the region. While labour markets showed some positive trends in 2021, unemployment remains precariously high in Bosnia and Herzegovina and the Republic of North Macedonia.

Fiscal balances in the region have improved

Fiscal balances in the region improved as revenues increased and spending growth moderated. The fiscal impulse remained positive in 2021 but consolidation is likely in 2022. Countries have retained favourable access to capital markets, despite some deterioration for Montenegro. Several countries issued Eurobonds, including Serbia, which offered its first sovereign green bond. Current account deficits in the region remain high, especially in Albania and Montenegro, and despite a moderate reduction in the latter. Increases in exports and tourism revenues have been offset by stronger domestic demand and higher energy prices.

Structural barriers to growth remain

The outlook for the region is subject to certain risks. Vaccination rates are still relatively low, particularly in Albania and Bosnia and Herzegovina, which could lead to further waves of infection that derail recovery. Structural impediments to growth in South-Eastern Europe remain significant; the pandemic exacerbated already low productivity levels and labour market participation rates. Demographic pressures and outward migration create additional challenges. Geopolitical tensions, while contained, could resurface. Infrastructure deficits, skills shortages and weak governance continue to undermine private investment.

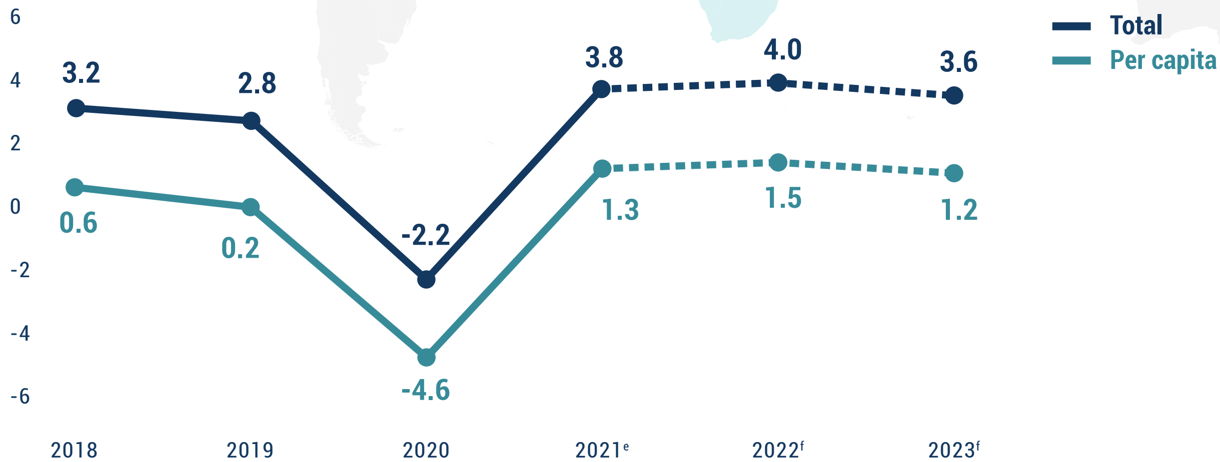
An additional regional cooperation framework was launched

In 2021, Albania, North Macedonia and Serbia agreed to lay the foundation for a single market, including the free movement of labour. This is within the framework of the initial “mini-Schengen” initiative, later renamed “Open Balkans”, which is aimed at removing internal borders by 2023. To some extent, the move reflects frustration with slow progress in accession to the European Union, which should nevertheless continue to provide an anchor for domestic policies and remain a source of financing.

Africa

GDP growth

Percentage



COVID-19 cases & deaths

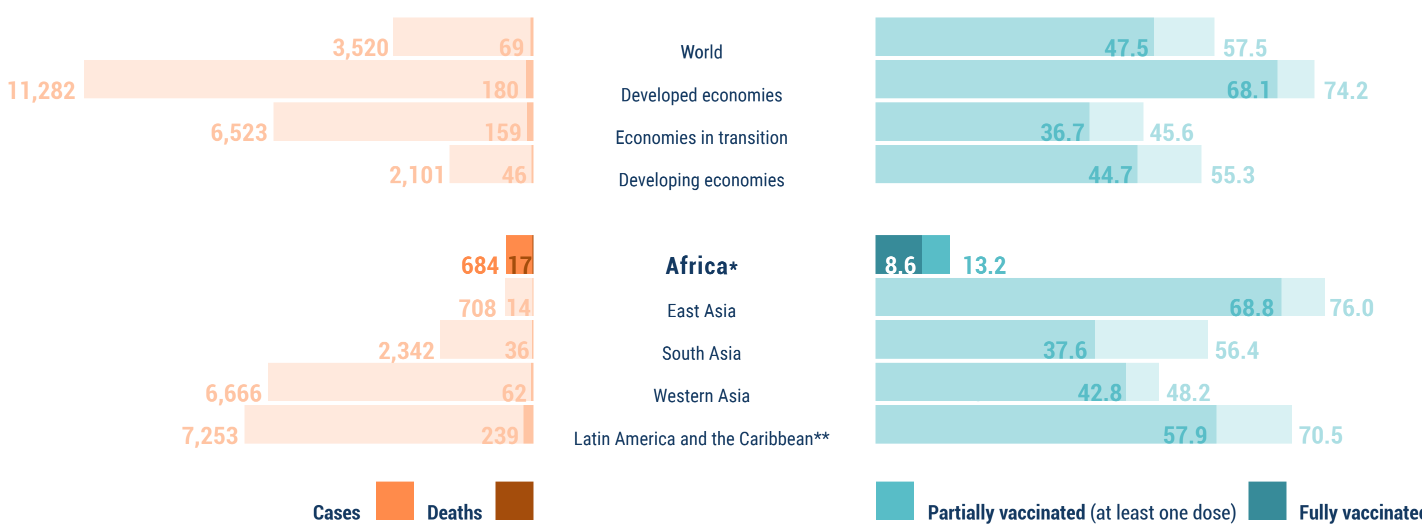
as of 20 December 2021

Per 100,000 people

Vaccination

as of 20 December 2021

Percentage of population



Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. The map represents countries and/or territories or parts thereof for which data is available and/or analysed in World Economic Situation and Prospects 2022. The shaded areas therefore do not necessarily overlap entirely with the delimitation of their frontiers or boundaries. Aggregate data for Africa, excluding Libya.

* Excluding Libya; **Excluding Bolivarian Republic of Venezuela. **e:** 2021 estimates. **f:** 2022-2023 forecasts.

Source for COVID-19 data: UN DESA calculations, based on data from Johns Hopkins University.

Developing economies

Africa: rebound in economic growth amid great downside risks

- Economic output in Africa is projected to rise, but it is subject to risks from recurrent waves of COVID-19 and increased instability.

- A boom in commodity prices is providing much needed fiscal space for commodity exporters but tourism-dependent countries may take longer to bounce back.

- Multilateral support to the region will remain critical for full recovery, including to expedite vaccine distribution and facilitate debt relief.

Returning to normal economic activity has been challenging in Africa

Economic activity in Africa continues recovering from the unprecedented events of 2020 but at a fragile pace. A projected expansion is marked by high uncertainty and exposure to repeated waves of COVID-19 infection, as seen recently with the emergence of the Omicron variant. Mitigation measures, such as lockdowns and travel bans, have been the main tool for stopping the spread of the virus due to low vaccination rates. Resulting disruptions in economic activities make a return to pre-pandemic conditions difficult. Although most African economies are witnessing rising output levels, supported by a more favourable global context, economic recovery has been weaker than in other regions.

Economic growth rates are insufficient for a return to pre-pandemic trends

Aggregate output in Africa is projected to recover gradually against a backdrop of subdued investment and high uncertainty. Economic growth is estimated to firm up in 2022, to 4 per cent from 3.8 per cent in 2021 (figure III.8). This should be driven by the gradual rollback of virus containment measures and rising vaccination rates as well as higher commodity prices and incremental improvements in investment rates. Africa observed one of the slowest recoveries in the world in 2021, lagging average growth rates for the developing countries and the globe, which are estimated at 6.4 per cent and 5.5 per cent, respectively. Projections point to a permanent loss of output in the forecast horizon (figure III.9). To return to its pre-pandemic trajectory of output growth, Africa would need to grow by approximately 6 per cent in 2022-2023, which is as fast as South Asia. In per capita terms, real GDP levels are expected to remain below pre-pandemic levels through 2023, especially in southern Africa, representing a significant setback to development gains achieved before the pandemic.

Figure III.8

Real GDP growth in Africa by subregion

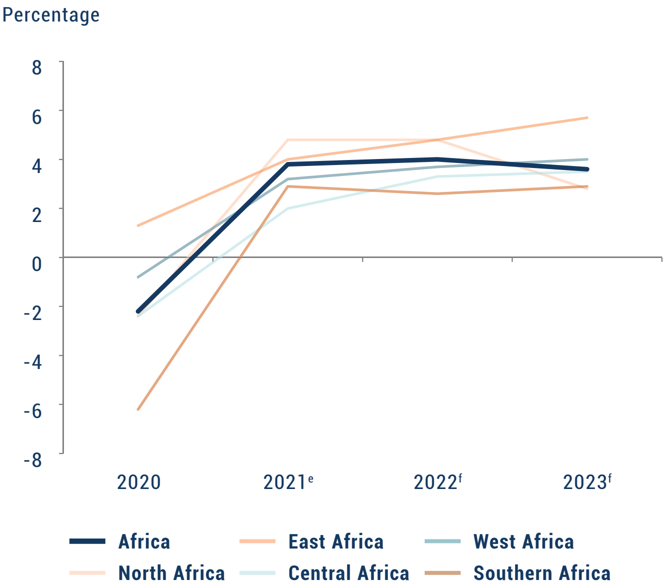
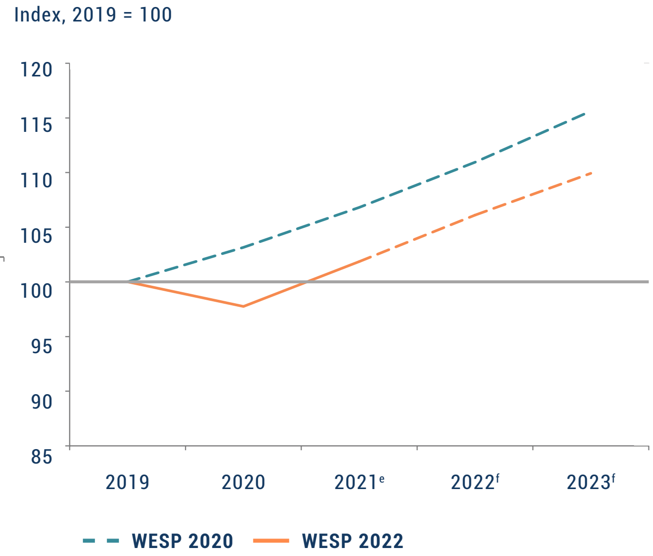


Figure III.9

Real GDP in Africa



Sources: Source: UN DESA, based on projections produced with the World Economic Forecasting Model.
Note: e = partial estimate, f = forecast. Excludes Libya. The dashed line in Figure III.9 indicates pre-crisis projections.

Low vaccination levels are exposing African countries to repeated COVID-19 waves...

Most African economies remain in the grip of the pandemic. While the third wave of the coronavirus has tapered off, at least 12 countries – Algeria, Benin, Burkina Faso, Egypt, Eritrea, Kenya, Mali, Mauritania, Mauritius, Somalia, South Africa and Tunisia – are battling or have battled their fourth wave. In late November 2021, a new variant, Omicron, was detected in Botswana and put the world on edge after South Africa announced a surge in cases. Though the impact of each wave is unknown, the death toll from future waves in Africa would likely be high, given case fatality rates that rank among the highest in the globe (such as in Egypt, Somalia and Sudan). The continent remains the most undervaccinated in the world, with just over 10 per cent of its 1.3 billion people vaccinated with at least one dose (figure III.10). Most countries have vaccinated less than 5 per cent of their populations, failing to meet the World Health Organization (WHO) vaccination goals of 10 per cent coverage by September 2021 and 40 per cent by the end of 2021. Only five African countries have accomplished the latter (Cabo Verde, Mauritius, Morocco, Seychelles and Tunisia). The vaccine roll-out has been hampered by affordability, hesitancy,[10] logistics, global production constraints and vaccine hoarding abroad. Global solidarity around vaccines has proved widely inadequate, with pledges and deliveries to the WHO's COVAX Facility falling short of requirements. Production facilities in Algeria, Egypt, Nigeria, Senegal and South Africa may help boost vaccination in those countries later this year. The vast majority of countries,

10 A survey by the Africa Centres for Disease Control and Prevention on perceptions of COVID-19 vaccination found that misinformation in Africa is rife. Young, male and unemployed people and urban residents are more likely to be sceptical (Africa CDC, 2021).

however, may not reach 60-70 per cent coverage before 2023 and, in some cases, not at all barring significant changes in vaccine production and distribution.

Figure III.10

COVID-19 vaccination rates by world region (as of 20 December 2021)

Sources: UN DESA, based on data from Our World in Data (accessed on 20 December 2021).

...and political instability is undermining the economic recovery

Even promising economies face the challenges of conflict and instability. Four military coups occurred last year, in Chad, Guinea, Mali and Sudan, and attempts were foiled in the Central African Republic, Madagascar and Niger. UN Secretary-General António Guterres has referred to “an epidemic of coup d’états”. In Ethiopia, Africa’s second-most populous nation, civil war in the northern Tigray region since November 2020 is a major source of tension domestically and for countries across the Horn of Africa. A prolonged unsettled dispute will have escalating humanitarian consequences while further destabilizing the region and depressing investment. Tensions are also intensifying among Ethiopia, Egypt and Sudan over the filling of the Grand Ethiopian Renaissance Dam. In the Sahel region, humanitarian and security crises continue to deteriorate, with interethnic violence on the rise in Burkina Faso, Chad, Mali, Mauritania and Niger. Other ongoing conflicts include civil wars in Libya and Somalia, an Islamist insurgency in Mozambique, the “Anglophone crisis” in Cameroon and natural resource-driven conflict in the Democratic Republic of Congo. These crises interact with and aggravate other challenges – such as poverty, unemployment, crime, food insecurity and internal displacement – and undermine the economic potential of the continent.

The main downside risks of the pandemic are elevated food prices and tightening financing conditions

Risks to regional growth skew down due to domestic and external factors. On the domestic front, there is a significant concern that countries will experience recurrent COVID-19 waves with possibly more dangerous variants. Border closures could wreak havoc in African economies, disrupting the flow of medical supplies and tourism. The risks would be aggravated by further delays to vaccination programmes. Vaccine hoarding by developed nations, including for third-dose booster shots, and affordability constraints present serious concerns and may extend the pandemic in the continent. Even as supplies increase, deficient infrastructure, limited access to crucial commodities such as syringes and vaccine hesitancy may continue to slow the roll-out of vaccines. Should COVID-19 become an endemic disease in the region, medium-term prospects would be hampered by lower consumer and investor confidence.

Domestic risks from upsets in crop and livestock production also cloud the outlook. Extreme weather- and conflict-related events may cause these disruptions and increase already elevated food prices, pushing up headline inflation (as in Angola, Egypt, Ethiopia, Guinea and Sierra Leone). Droughts and floods are becoming more frequent as temperatures and sea levels continue to increase faster in Africa than the world average (IPCC, 2021b). Conflict and unrest may escalate given greater instability, poverty and insecurity.

On the external front, rising inflation expectations in advanced economies and other regions threaten financing for the region. A tightening of monetary policy in the United States and global financial conditions would dampen global economic activity and increase risk premiums, especially for more exposed economies in Africa already grappling with elevated debt levels. This situation would decrease access to funds for investment, with dire consequences for social and economic development.

Within the region, prospects remain subdued for the largest economies. Nigerian economic growth is projected to accelerate to 2.8 per cent in 2022 from 2.5 per cent in 2021, as the impact of the health crisis declines and the new oil bill and public infrastructure development boost investment. Nevertheless, there are downside risks from an uncertain evolution of the pandemic given low vaccination rates, high inflation and security threats. South Africa's recovery has faced headwinds due to a sluggish vaccine roll-out and damaging civil unrest during the summer of 2021. Its economy grew by an estimated 3.8 per cent in 2021, not enough to compensate for the 7 per cent drop in 2020. With the outbreak of the Omicron variant spelling dire economic troubles for the country, especially for tourism, prospects are gloomy. Growth is forecast at only 2.3 per cent in 2022. Frequent power outages, high unemployment, inequality and corruption will continue to weigh on productivity growth. In Egypt, after near stagnant economic growth in 2020, a robust recovery is underway with real GDP growth at an estimated 6.1 per cent in 2021 and forecast at 5.7 per cent in 2022. The recovery has been led by solid growth in private consumption, exports and private investment amid easing balance-of-payments constraints due to more favourable external conditions. Both public and external debt are growing at alarming rates, however, posing risks.

Higher commodity prices support some exporters while other countries await the return of tourism

Among commodity exporters, strong global demand and high prices provide a promising outlook. The upturn in global commodity prices is giving some breathing room to energy, metals and agricultural producers after two commodity price crashes in five years. The financial windfall is providing crucial improvements in national income and government spending and investment. The rise in commodity prices will likely be transitory, however, and insufficient to generate robust, sustainable growth. The need for economic reform and diversification will remain high on the development agenda.

Tourism-dependent economies face improving prospects, though from a low base. These are driven by the loosening of travel restrictions and economic recovery in origin markets in Europe and Asia, as well as higher traveller confidence associated with successful containment measures and relatively high vaccination rates (as in Cabo Verde, Comoros, Mauritius, Morocco, Sao Tome and Principe, and Tunisia). Yet global tourist arrivals are not expected to return to 2019 levels before 2023 and quite possibly 2024 (UNWTO, 2021b). Economic recovery in these countries will likely be difficult and vulnerable to renewed shocks to global travel, including from new variants. Tourist-dependent industries, such as wildlife conservation and environmental protection, and informal workers in the sector are expected to face another difficult year, with aggravating long-term effects.

Stagnant working hours and productivity growth contribute to poverty and inequality

Labour markets and social conditions lag economic growth in Africa. Growth in working hours stalled in 2021, remaining 5.3 per cent below levels at the end of 2019 (ILO, 2021d). Labour productivity declined in 2021 with average output per hour worked 1.4 per cent lower than in 2020, except in North Africa. This contrasts with positive productivity growth in developed economies. It follows a medium-term decline in African labour productivity since 2016. With 85.8 per cent of the labour force and 89.7 of the female labour force in informal employment (ILO, 2018), the ability of governments to provide targeted assistance to those in need, especially during the pandemic, proved very limited. The global economic crisis in 2020 increased extreme poverty in Africa by 38.4 million people, and in 2021, another 8.6 million fell below the extreme poverty threshold. Given predicted GDP per capita growth of less than 2 per cent in 2022-2023, the poverty headcount rate in Africa will remain elevated (see box III.2). Women have been disproportionally affected by job losses in hard-hit sectors, increased domestic care, exposure to domestic violence and reduced access to sexual and reproductive care (UN Women, 2020). Young African women are now 60 per cent more likely than men not to be in employment, education or training (ILO, 2020). High unemployment, poverty and inequality afflicting young, increasingly tech-proficient and urbanized populations will present substantial political and policy challenges ahead.

Box III.2

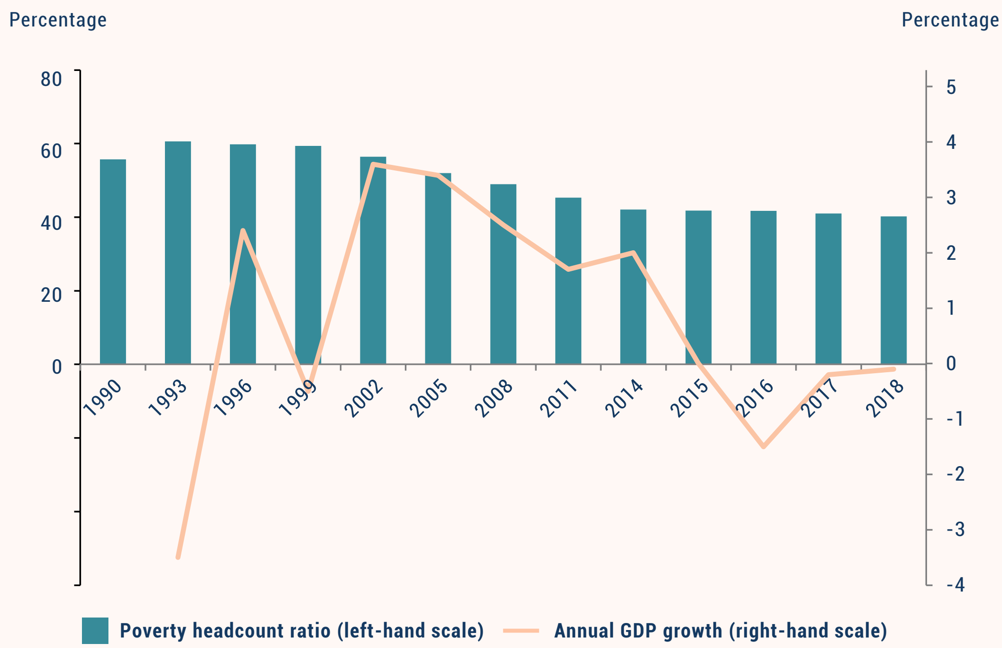
The quantity and quality of economic growth fosters poverty reduction in Africa

Extreme poverty in Africa has dropped from over 50 per cent of the population in 2002 to 41 per cent in 2018 (figure III.2.a). From 2002-2014, the poverty rate fell by 1.2 percentage points per year, mainly due to robust economic growth, with average GDP per capita increasing by 2.6 per cent over this period. Even so, the region added about 13 million poor people due to population growth. Since 2014, reflecting in part the 2014-2015 decline in global commodity prices, annual per capita GDP growth has been negative. Africa's poverty headcount rate decreased by less than 0.5 percentage points per year from 2014-2018.

COVID-19 increased the number of newly poor people in Africa by up to 55 million in one year, more than the combined total since 1999. Achieving the first Sustainable Development Goal, to end extreme poverty by 2030, was unlikely for most African countries even before the pandemic. It is now even further out of reach. Although income growth appears to be the main driver of poverty reduction, its decomposition reveals striking differences across countries in terms of inequality (ECA, 2021).

Figure III.2.a

Poverty headcount rate and annual GDP growth



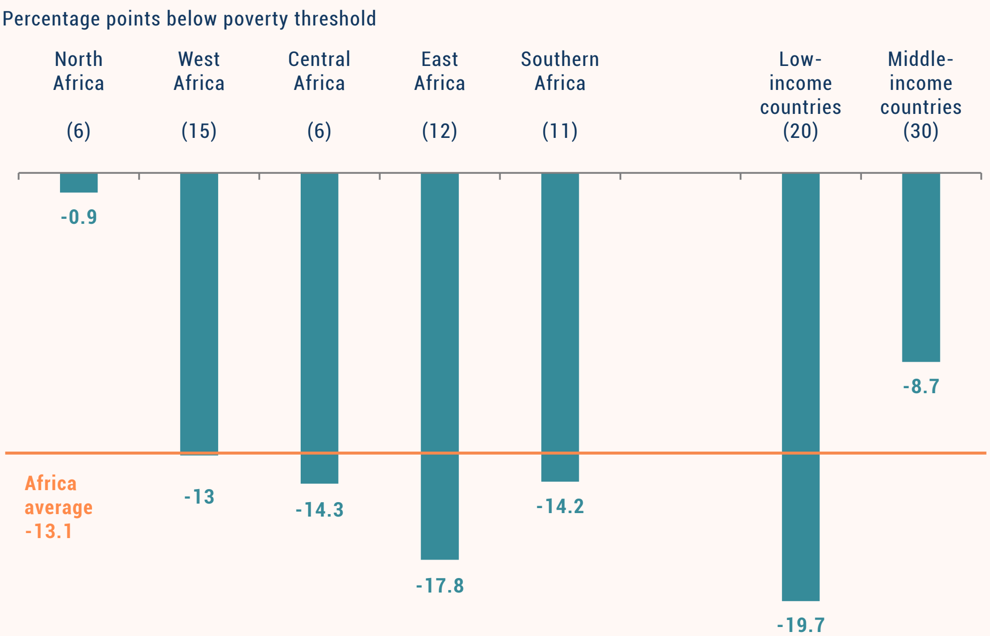
Source: ECA calculations based on data from the World Bank PovcalNet database (accessed in September 2021).

Deep poverty and vulnerability exacerbate poverty reduction challenges

A key challenge to poverty reduction in Africa is how deep poverty remains in many countries. On average, the depth is 13.1 per cent, implying that the average poor person is 13.1 per cent below the poverty threshold (figure III.2.b). There is wide variation, with the poor less than 1 per cent below the poverty line in North Africa, but 13-18 per cent below in the other four subregions. In low-income countries, the average poor person is nearly 20 per cent below the poverty line. The six most-affected countries (Burundi, Democratic Republic of Congo, Central African Republic, Guinea-Bissau, Madagascar and Zambia) have a depth of poverty between 30-39 per cent. The 10 countries in the world with the deepest poverty are all in Africa.

Figure III.2.b

Depth of poverty in Africa



Source: ECA calculations based on data from the World Bank PovcalNet database (accessed in September 2021).
Note: Figures in parantheses are the number of countries in each category.

Another key challenge to ending poverty in Africa is the high proportion of people who live just above the poverty line. About 175 million people have consumption levels about 10-33 per cent above the extreme poverty line. They are not considered poor but remain vulnerable to falling into poverty. About 58 million people are extremely vulnerable as their mean consumption is only 10 per cent above the poverty line. A very small drop in consumption can be enough to push them under the line. This group likely explains the sharp increase in poverty headcount numbers due to COVID-19. West and East Africa have the largest shares of people vulnerable to falling into poverty, with Ethiopia and Nigeria the biggest contributors. East Africa and Southern Africa have the largest proportions of people most vulnerable to staying in poverty (or the chronic poor) at 34.6 and 33.3 per cent, respectively. Unsurprisingly, low-income countries have the largest proportion of people (36.2 per cent) most vulnerable to remaining in poverty after a shock.[a]

Economic performance is key in reducing poverty. The transformation of growth to poverty reduction is mediated by relative contributions of changes in income and inequality. Currently, a return to declining rates of poverty is uncertain given a weak economic recovery with considerable downside risks, such as low vaccine availability and slow roll-outs, the emergence of possible variants, constrained fiscal space and high debt repayment obligations. Those far below the poverty line will require robust targeted income support and other social protection measures.

To revert to the pace of poverty reduction in 2002-2014 and accelerate implementation of the 2030 Agenda and Africa's Agenda 2063, countries need higher growth rates of at least 7 per cent annually. Since high inequality reduces the likelihood that economic growth will translate into poverty reduction, policies must also narrow inequalities in opportunities and set growth on an inclusive path. This could be done through continental initiatives, such as the African Continental Free Trade Area, to stimulate value added intra-Africa trade, structural transformation and job creation. It could build on poverty reduction strategies that hedge against extreme income volatility due to present and future shocks.

With COVID-19 exacerbating economic vulnerabilities, African countries should also emphasize measures including effective debt management, increased expenditure efficiency and greater domestic revenue allocations in sync with the Sustainable Development Goals. They should harness the benefits of international debt relief options, such as the Debt Service Suspension Initiative, the Heavily Indebted Poor Countries Initiative and the Common Framework for Debt Treatment. This would strengthen recovery and eventually diminish the depth of poverty and vulnerability.

a ECA calculations based on data from the World Bank PovcalNet database (accessed in September 2021).

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Fiscal consolidation began during the pandemic

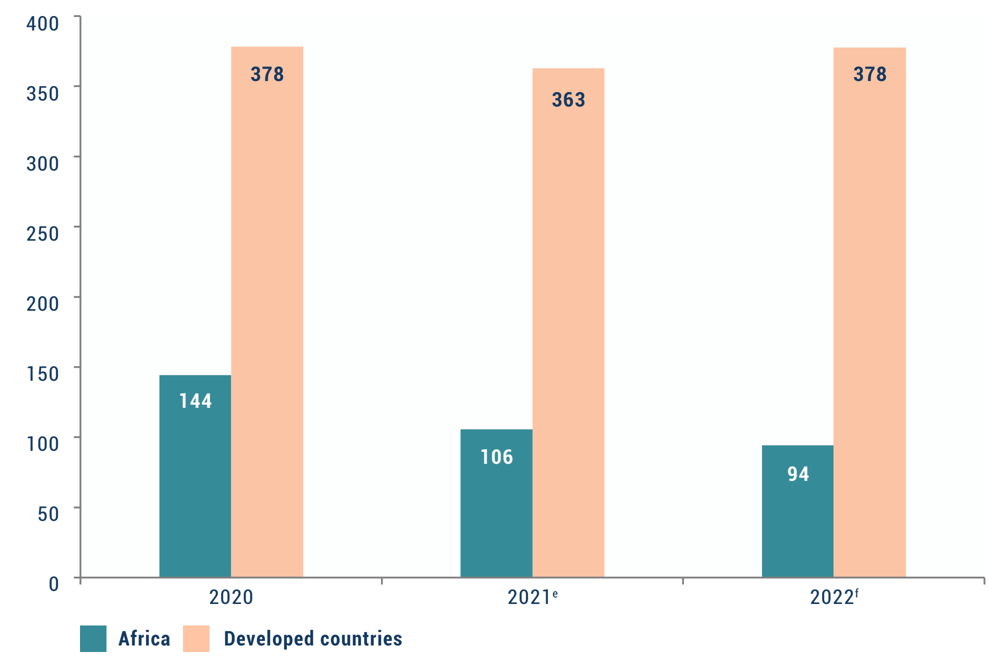
Though African governments initially responded to the crisis by increasing fiscal outlays, fiscal sustainability concerns preceding the pandemic meant a relatively quick return to fiscal consolidation. Governments already had little room to accommodate revenue shortfalls caused by the pandemic and the budgetary costs of response packages. Financing needs were mostly covered by international emergency support, including IMF, World Bank and bilateral assistance, and debt service relief from the G20 Debt Service Suspension Initiative and the IMF Catastrophe Containment and Relief Trust. In 2021, while still fighting second and third waves of COVID-19, governments began fiscal consolidation to maintain sufficient external reserves, protect currency pegs for some and ensure debt servicing capacity, despite weak and fragile economic recoveries. In developed countries, by contrast, greater policy buffers have allowed robust support and a quadrupling of government borrowing since the outbreak of the pandemic (figure III.11). Fiscal balances are expected to continue shrinking across the continent. In August 2021, the $650 billion Special Drawing Rights allocation boosted reserves somewhat and could be amplified by voluntary channelling of allocations elsewhere. China, for instance, announced it would shift $10 billion in its Special Drawing Rights to African nations.

Despite fiscal tightening, debt levels are projected to remain high and rising. Government interest expenditure continues to absorb a rising share of revenues and is already above a third in certain countries in the West African Economic and Monetary Union (IMF, 2021c). This reflects a build-up in debt, persistently weak revenue mobilization and for some countries the end of the Debt Service Suspension Initiative. Rising interest expenditure reduces fiscal space to support economic recovery and the 2030 Agenda for Sustainable Development. Already, several countries spend more on debt servicing than on health care. To this end, a new repo market launched by the United Nations Economic Commission for Africa in November 2021 should trim billions of dollars from government borrowing costs starting in 2022. Still, debt relief as well as emergency assistance may be necessary for countries in higher debt distress.

Figure III.11

Government borrowing as a share of GDP

Index, 2019 = 100



Source: UN DESA, based on projections produced with the World Economic Forecasting Model. Excludes Libya.
Note: e = partial estimate, f = forecast.

Monetary policy stances remain accommodative but global and domestic conditions add pressure

African central banks are mostly maintaining accommodative monetary policy stances but this might change in the short term. In 2021, only a small number of countries changed policy interest rates, either through cuts (as in Ghana, Liberia, the Republic of Congo, Seychelles and Uganda) or hikes (Angola, Ghana, Lesotho, Mozambique, South Africa, Zambia and Zimbabwe). Leniency in developed countries towards rising inflation has allowed crucial policy space for African central banks to prioritize economic growth and narrow output gaps, even if that meant tolerating rising inflationary pressures

(Democratic Republic of the Congo, Nigeria and Sierra Leone). Upside risks to inflation from currency depreciation and planned consumer tax hikes as well as reduced subsidies due to fiscal consolidation may require central bankers to raise interest rates sooner rather than later. Fading monetary stimulus along with fiscal consolidation would complicate already challenging recoveries.

Countries are tasked with fighting the pandemic while boosting growth and development

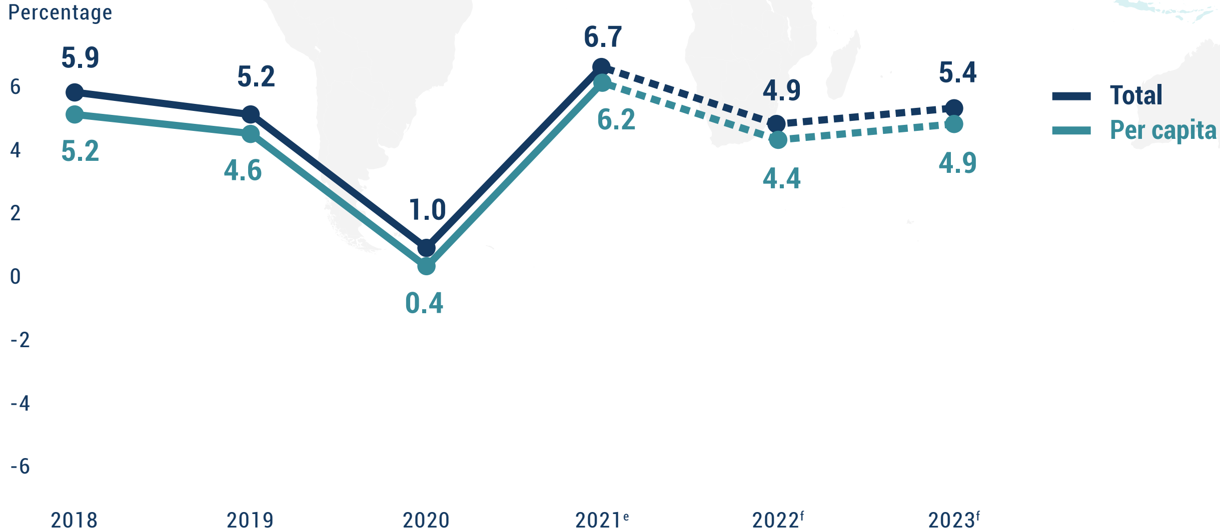
Moving forward, saving lives from COVID-19 must continue to take precedence. Keeping a close watch on the emergence of more transmissible and lethal variants, at home and abroad, and responding with swift action must be a priority. Faster and more fair distribution of global vaccine supplies, expansion of local vaccine manufacturing, improvements in the distribution infrastructure and measures to combat vaccine hesitancy are necessary to control the pandemic in Africa and avoid stop-and-go economic processes.

For the medium term, the single most viable route to inclusive and sustainable development in Africa is through advancing the structural transformation of economies and building productive capacities. A key focus for many countries will be services and manufacturing-driven industrialization with formal and decent employment. The industrialization of agriculture and minerals processing could be avenues for progress, as recognized in several national development plans. Another key area is to speed the digital revolution. This entails deploying new technologies in areas such as revenue collection and anti-corruption efforts, improving 3G and 4G network coverage, and advancing 5G networks, including beyond major cities. Firms stand to profit from new market opportunities, enhanced supply-chain efficiency and resilience as well as productivity increases. Consumers should see more product choices and learning opportunities through digital transformation.

East Asia

GDP growth

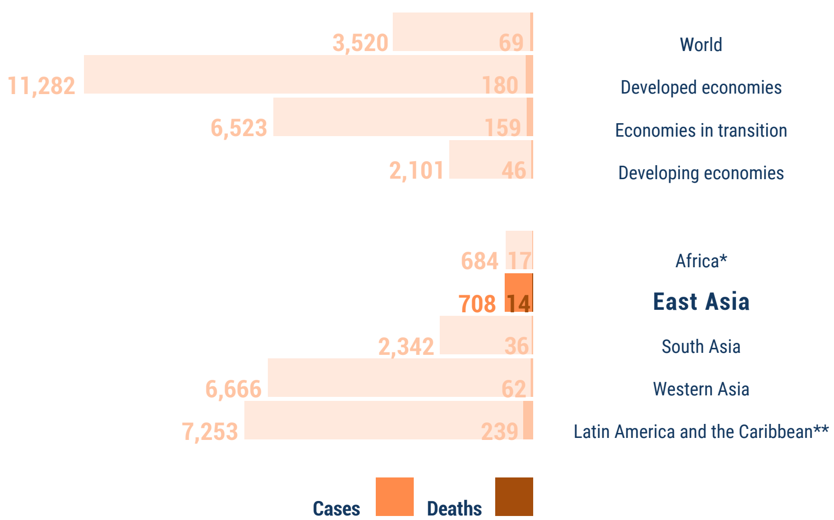
Percentage



COVID-19 cases & deaths

as of 20 December 2021

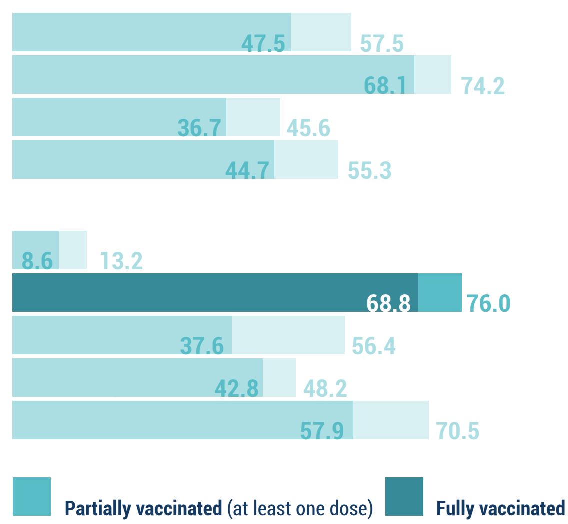
Per 100,000 people



Vaccination

as of 20 December 2021

Percentage of population



Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. The map represents countries and/or territories or parts thereof for which data is available and/or analysed in World Economic Situation and Prospects 2022. The shaded areas therefore do not necessarily overlap entirely with the delimitation of their frontiers or boundaries. Aggregate data for Africa, excluding Libya.

* Excluding Libya; **Excluding Bolivarian Republic of Venezuela. **e:** 2021 estimates. **f:** 2022-2023 forecasts.

Source for COVID-19 data: UN DESA calculations, based on data from Johns Hopkins University.

East Asia: a nascent economic recovery with rising downside risks

- Increasing downside risks and uncertainties cast a shadow on East Asia's nascent economic recovery.
- The lingering pandemic continues to weigh on progress in achieving the 2030 Agenda for Sustainable Development.
- Macroeconomic policies should remain accommodative and targeted to fostering inclusive and sustainable recovery.

East Asia's economies have rebounded from the worst but remain fragile…

East Asia's economic performance largely rebounded in 2021. Headline GDP growth was an estimated 6.7 per cent following the sharp deceleration in 2020. The recovery is nascent, however. A resurgence of COVID-19 has disrupted economic performance supported by strong policy stimulus and a recovery in external demand. Economic growth is forecast to moderate to 4.9 per cent in 2022 as base effects disappear. While countries' reopening could shore up economic activities, the uneven distribution of vaccines, a still low pace of vaccination and unknown vaccine efficacy against new variants of the virus mean that the pandemic will linger and could derail a fragile economic recovery. Additional headwinds come from a possible decline in export demand, prolonged supply-side challenges, rising concerns around financial instability and the possibility of a larger-than-expected slowdown in China's economy amid lingering trade tensions with the United States. Since pandemic control will continue as a policy priority in the near term, macroeconomic policies should remain accommodative and targeted to fostering an inclusive and sustainable recovery.

… and with divergence in economic performance

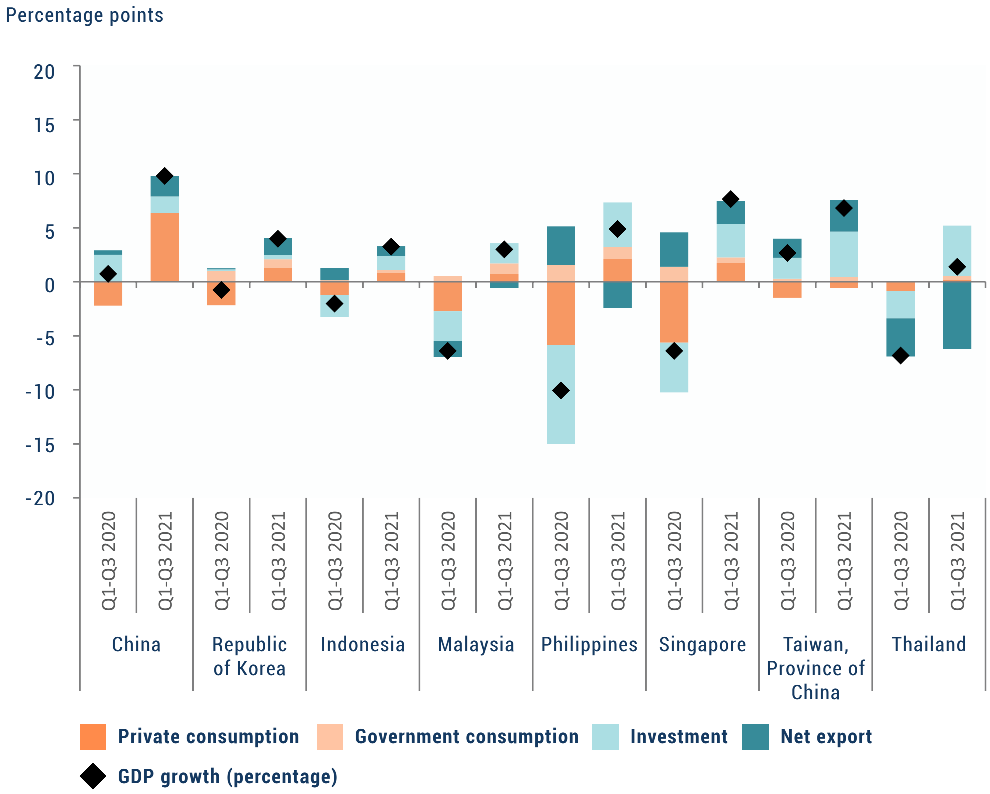
The uptick in East Asia's headline GDP growth masks large divergence in economic performance across countries. Overall, relatively stronger recovery was seen in China, the Republic of Korea and Singapore, due to early COVID-19 containment measures, quick vaccine roll-outs and strong external demand. In contrast, the Delta variant outbreak slowed recovery in many countries in the Association of Southeast Asian Nations (ASEAN), including Indonesia, Malaysia, the Philippines, Thailand and Viet Nam. Tourism-dependent countries, especially the small island developing States in the Pacific, were hit doubly by new waves of COVID-19 and a plunge in tourist arrivals. Ongoing political turmoil has severely weighed on Myanmar's economy.

Trade, the major growth driver during the pandemic, is losing momentum…

Strong global demand for Asian manufacturing and exports has underpinned the region's headline economic growth. A quick rebound in household spending in the developed countries buoyed demand for electronics, electrical and information technology equipment, and automobiles, which particularly benefited China, the Republic of Korea, Singapore and Taiwan, Province of China (figure III.12).[11] Investment was channelled into machinery and equipment, supporting export manufacturing.

11 Improving external demand also benefited several ASEAN economies (such as Indonesia, Malaysia and Thailand) and commodity exporters (Brunei Darussalam and Mongolia). New waves of COVID-19 cases offset economic gains, however.

Figure III.12
Demand-side contributions to growth in select East Asian countries



Source: UN DESA, based on data from CEIC (accessed on 29 November 2021).
Note: For China, the consumption bar covers both the private and government sectors.

Shipment backlogs, surging freight costs and temporary quarantine restrictions in key manufacturing and shipping areas have slowed the region's export growth. Semiconductor shortages due to adverse weather events, COVID-19-induced production disruptions and shipping congestion have significantly extended delivery times.[12] Ongoing technology and trade tensions between China and the United States have further hampered production and exports of semiconductors. Rising energy prices and electricity shortages are also weakening exports. Power rationing in China, for instance, has impeded production at numerous factories, including those that supply components to large manufacturers of consumer electronics and automobiles. Going forward, demand for manufactured goods from Asia is expected to gradually decline as economies elsewhere heal from the pandemic and restore their local supplies.

…while strong domestic demand recovery is subject to the progress and efficacy of vaccine programmes

As export growth begins to moderate in the region, domestic demand should, in principle, play a bigger role in driving economic growth. Many East Asian countries have observed stronger domestic demand (figure III.12) through continued policy stimulus and reopening. Ongoing domestic demand as a driver

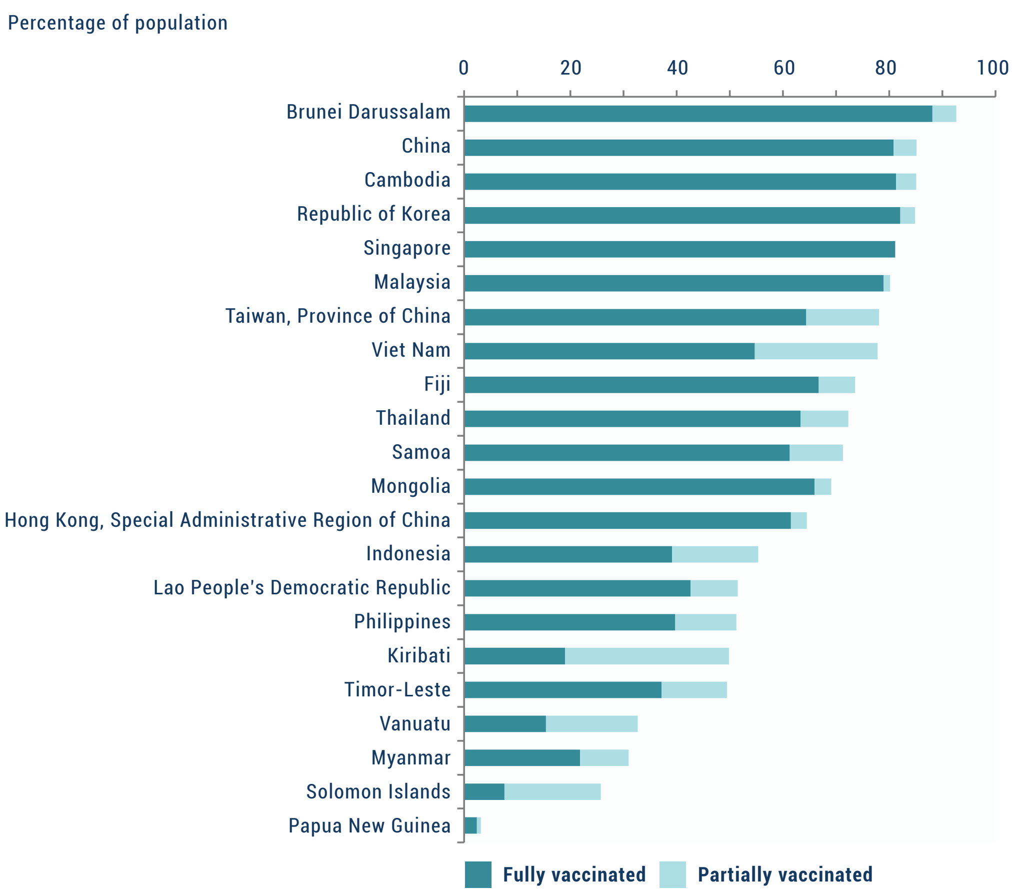
12 Average delivery times for semiconductors increased from 12 weeks in early 2020 to more than 20 weeks in July 2021 (King, 2021).

of growth is contingent on containing the virus, however. New waves of COVID-19 have triggered containment measures over 2021, which heavily weighed on private consumption and investment.

Vaccinations offer some hope, yet despite gathering pace in the second half of 2021, vaccination progress remains highly uneven. By mid-December 2021, Brunei Darussalam, Cambodia, China, Malaysia, the Republic of Korea and Singapore had over 70 per cent of their populations fully vaccinated. In contrast, some least developed countries and small island developing States lagged behind. Vaccination rates in Myanmar, Papua New Guinea, the Solomon Islands and Vanuatu were still less than 30 per cent (figure III.13). Limited access to vaccines and inadequate capacity for vaccine roll-outs further increase the vulnerability of these countries.

Figure III.13

Vaccination progress in East Asia (as of 20 December 2021)



Source: UN DESA, based on data from Our World in Data (accessed on 20 December 2021).

As the pandemic lingers, East Asian countries have started considering long-term strategies to deal with the virus. For instance, while China is sticking with its "zero COVID-19" policy, Indonesia, Malaysia, the Republic of Korea, Singapore and Thailand are pursuing approaches to "coexist" with the virus. No matter which path countries choose, policymakers remain cautious about fully reopening economies; the Delta outbreaks showed the high risks of new and more transmissible variants. While vaccines are assumed to generally reduce the severity and duration of COVID-19 symptoms, their efficacy against new variants is still unknown. This means that some restrictive measures will likely remain in place during the forecast period, with targeted lockdowns and mobility restrictions introduced if infection rates surge again. Border openings are likely to be gradual and come with entry requirements. All such measures will likely further increase social and economic costs and delay full recovery.

China's economic slowdown adds additional headwinds to the region's near-term outlook

China's "zero COVID-19" policy constrains the economy's full recovery. Renewed restrictions in response to a surge in infections in the second half of 2021[13] weighed on consumer spending and weakened the pace of initially strong recovery. At the same time, China's policy efforts to stabilize the property market have slowed investment.[14] This will likely sustain China's long-term resilience for several reasons. First, slower growth in property prices could curb rising inequality and support China's pursuit of "common prosperity".[15] Second, reducing household indebtedness from mortgages, which account for 76 per cent of household debt (People's Bank of China, 2020), could advance China's economic restructuring strategy, which prioritizes domestic consumption. Third, limiting the exposure of highly indebted private property developers will likely reduce financial risks. Given that the property sector potentially contributes about a third of China's GDP (Rogoff and Yang, 2020), a sharp price correction would not only adversely affect investment but also impair household consumption and potentially trigger broader financial instability.

In 2021, China's economy grew an estimated 7.8 per cent with an expectation of moderating to 5.2 per cent in 2022. The slowdown could have regional and global spillovers. For instance, sharp declines in new construction could reduce demand for raw materials from the rest of the world. At the same time, reining in the property market could lead to defaults by several large private property developers. A default would have wide repercussions on banks and other financial institutions as well as investors who hold these companies' offshore bonds. While China is cautiously managing the situation, concerns about a spillover are mounting.

A shift in global liquidity conditions raises financial stability worries

Quicker-than-expected tapering of quantitative easing in the United States raises financial stability concerns for East Asia. As the recovery in the region is in the early stages, a sudden change in global financial conditions could trigger capital outflows and increase exchange rate volatility. Over 2021, while foreign direct investment inflows were steady, a few ASEAN economies (including the Philippines and Thailand) experienced capital outflows through portfolio channels amid the Delta wave. Almost all

13 As of early November 2021, at least 19 of 31 provinces in China have reported infections with the Delta variant. Different provinces re-introduced temporary restrictive measures based on local needs, including mobility restrictions, school closures and quarantines.

14 Investment in construction in China contracted by 1.8 per cent in the third quarter of 2021, compared with an average quarterly growth of 6 per cent during 2015-2019.

15 The concept of "common prosperity" was first put forward by Mao Zedong, Chairperson of the Central Committee of the Communist Party of China, in 1953. China is giving a new push to it in 2021.

currencies in the region depreciated against the United States dollar to some extent, except for China's renminbi. With domestic economic conditions still weak, countries will be highly sensitive to changes in the interest rates of major developed countries. Countries with high debt levels, especially external debts, will be particularly vulnerable, such as Indonesia, Malaysia and Thailand, where external debt was around or above 150 per cent of GDP in the first two to three quarters of 2021.[16]

A lingering pandemic shadows progress on the 2030 Agenda for Sustainable Development

The pandemic is threatening to undermine some development progress in East Asia. The adverse impacts are expected to continue and deepen scarring effects. In particular, temporary restrictive measures have disrupted labour market recovery. The ASEAN region may see working-hour losses of an estimated 7.4 per cent in 2021, which implies only limited improvement compared with 2020 (ILO, 2021a). Working-hour and job losses have caused millions of people to lose at least part of their labour income. In the first half of 2021, labour income in the ASEAN region contracted by 5.7 per cent (ILO, 2021a). Job losses are exacerbating already high inequality as women, young workers and informal workers have been affected disproportionately. Around 8.6 million people in East Asia were pushed into extreme poverty in 2019-2021.

The pandemic's contribution to reducing pollution and emissions due to mobility restriction has proven short-lived. Air pollution (measured by PM2.5 emissions) has exceeded pre-pandemic levels. The recent energy crunch risks derailing the transition to low-carbon energy. Some firms may turn to "dirtier" energy such as diesel. This comes as rising climate risks already threaten the region's recovery. For instance, Fiji and Papua New Guinea experienced cyclones and floods in early 2021, adding economic costs to recovery. Taiwan, Province of China experienced its worst drought in 56 years in April 2021, which affected semiconductor production. East Asian countries are taking actions to address climate risks, with China and the Republic of Korea announcing they intend to reach carbon neutrality by 2060 and 2050, respectively. The Philippines and Viet Nam have committed to moving away from coal.

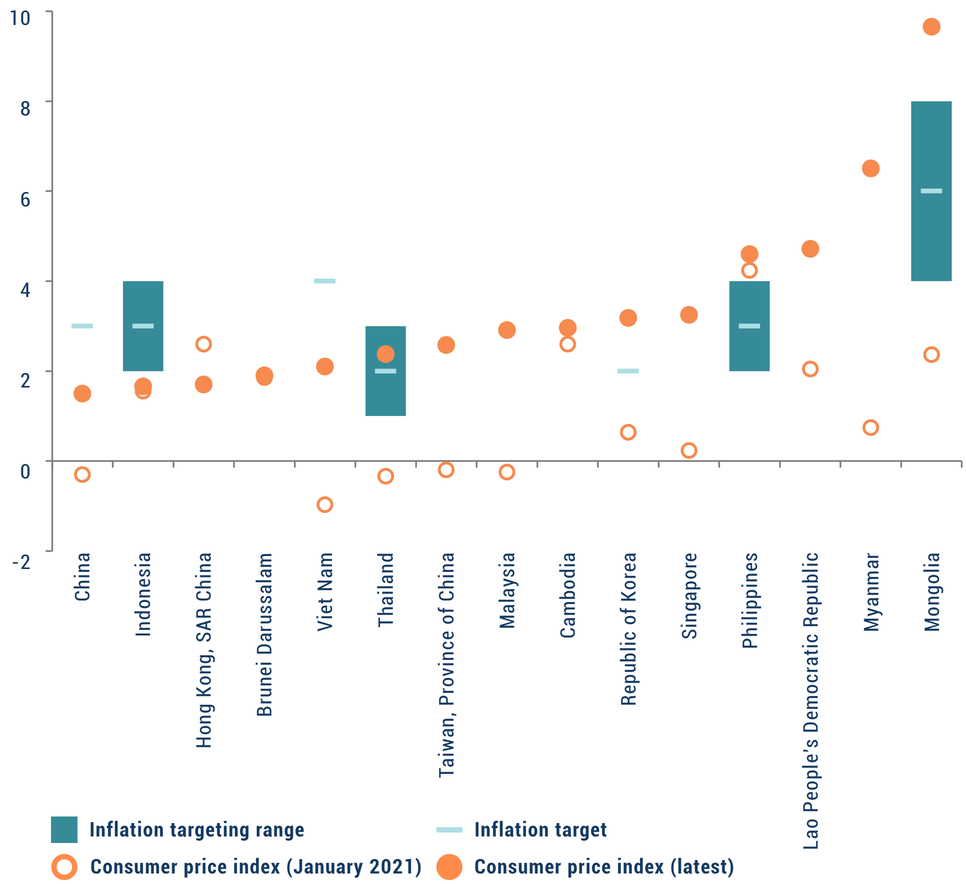
Inflationary pressure is still low

Inflation is expected to remain largely in check in East Asia. In 2021, headline inflation was an estimated 1.5 per cent. Most countries had inflation below or within central bank targets (figure III.14) although it trended upward due to rising food and fuel prices and supply-chain disruptions. Some countries observed above-target inflation related to particular factors, such as the Republic of Korea (higher costs of petroleum, housing rentals and services) and the Philippines (a spike in food inflation caused by adverse weather conditions). Going forward, headline inflation is projected at 2 per cent in 2022. While rebounding commodity prices and supply bottlenecks could increase prices, broader inflationary pressure is unlikely as the reopening of economies will be very cautious. Most economies are expected to operate below pre-crisis levels (figure III.15) with low consumer purchasing power likely keeping a surge in producer prices from passing through to consumer prices. Ongoing supply shortages and network disruptions are anticipated to recede over time as more countries reopen and demand shifts away from goods to services.

16 UN DESA estimate, based on data from CEIC (accessed on 29 November 2021).

Figure III.14
Inflation and inflation targets in East Asia

Percentage



Source: UN DESA, based on data from CEIC and Central Bank News (both accessed on 29 November 2021).

Fiscal policies could be more targeted to support an inclusive and green recovery

Supportive fiscal policies are critical to shore up the region's domestic demand, especially during new waves of COVID-19 and new rounds of restrictive policies. From January to October 2021, total COVID-19 policy responses cost an estimated $266 billion, equivalent to 1.4 per cent of the region's GDP.[17] Countries have extended fiscal stimuli introduced in 2020 (such as Indonesia[18]), implemented new programmes to contain the pandemic and fund social security programmes (Lao People's Democratic Republic and Malaysia[19]) and introduced new tax relief to support small firms (China, Malaysia and the Philippines).

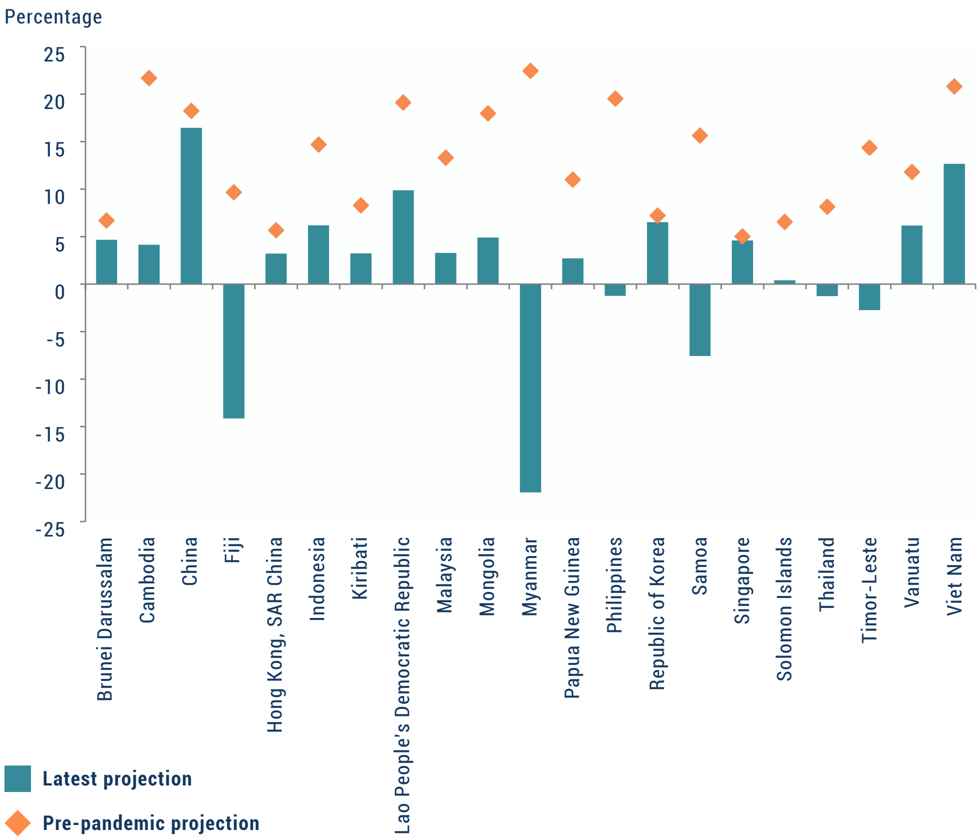
17 In 2020, policy responses totalled about $970 billion in East Asia. The amount of fiscal stimulus is estimated based on the IMF's Policy Responses to COVID-19 and the Asian Development Bank's COVID-19 Policy Database (both accessed on 13 November 2021).

18 Indonesia increased the budgeted amount of a national economic recovery programme from IDR579.8 trillion in 2020 to IDR699.4 trillion in 2021.

19 Lao People's Democratic Republic allocated LAK100 billion in 2021 for prevention, control and treatment of COVID-19 cases; Malaysia accelerated social security payments and provided additional funds for vaccine procurement.

Figure III.15

Growth of real GDP from 2019 to 2022, based on projections made in 2022 and 2020



Source: UN DESA.

Increasing public spending and decreasing tax revenue (due to economic output that is below the pre-pandemic level along with tax cuts) have widened fiscal deficits and increased public debt-to-GDP ratios. The region's median fiscal deficit as a share of GDP increased from 1.7 per cent in 2019 to an estimated 5.8 per cent in 2021. The gross government debt-to-GDP ratio grew from 40.5 to an estimated 47.8 per cent over the same period.[20] While premature fiscal consolidation should be avoided to prevent reversal of recovery gains, shrinking fiscal space requires more targeted public spending that is better aligned with the 2030 Agenda.[21] At the same time, countries could turn to various policy options to better mobilize domestic and international financial resources (box III.3).

20 Calculated based on October 2021 data from the IMF's World Economic Outlook Database (accessed on 14 November 2021).

21 The United Nations Economic and Social Commission for Asia and the Pacific (2021) points out that only a small share of the stimulus in Asia and the Pacific supported gender equality. A large part of the spending encouraged more production and consumption of fossil fuels without green commitments.

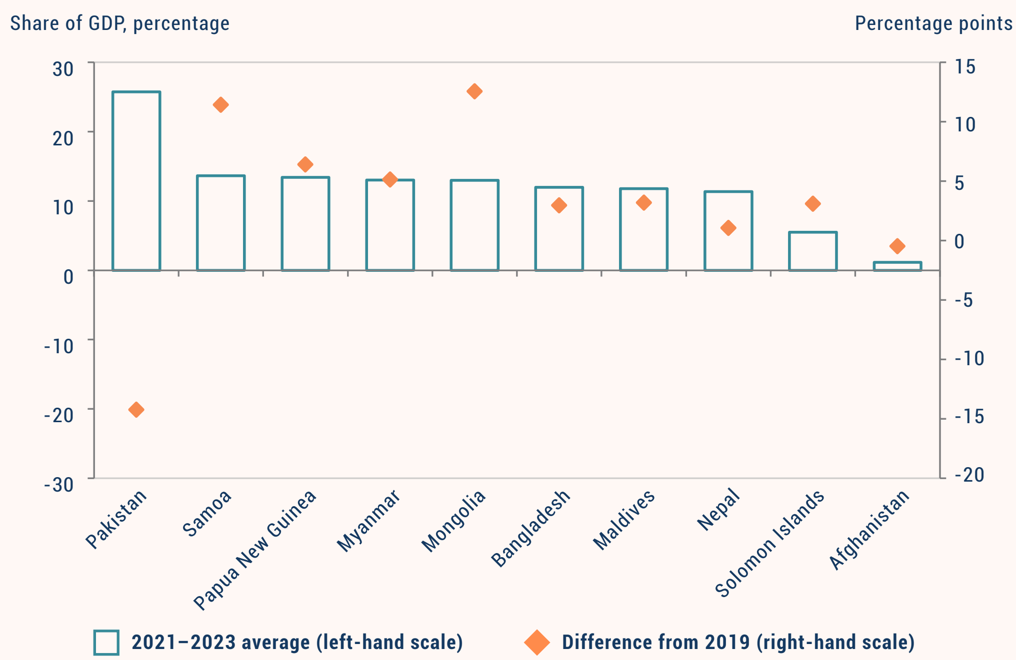
Box III.3

Fiscal policy and financing options to build forward better

The scars of past economic and non-economic shocks could last for a long time in East and South Asia (ESCAP, 2021). The region has high-quality public infrastructure and strong human capital, and even during the pandemic maintained ample fiscal space to help withstand the crisis. Sizeable fiscal stimulus buoyed domestic demand and supported households and companies in need. While accommodative fiscal policies are still required for recovery, however, fiscal space constraints will tighten in some countries. For example, while gross financing needs (the sum of the primary fiscal deficit and maturing debt obligations) in selected East and South Asian economies are expected to fall during 2021-2023 from the level in 2020, projected levels are far higher than in 2019 (figure III.3.a). Public debt sustainability is tenuous in some countries, more so given prospects for tightening global financing conditions and higher borrowing costs.

Figure III.3.a

Gross financing needs in selected East and South Asian countries



Source: ESCAP, based on Munevar, 2020.

Governments are exploring options to mobilize fiscal resources beyond traditional sources of borrowing and to improve public debt management. Tighter fiscal space also means that countries need to consider risk sharing to cope with coming shocks and rely less on fiscal resources. There are several different fiscal and financing policy options in the region.

Offshore sovereign and diaspora bonds: During 2013-2020, the Government of Lao People's Democratic Republic and other public entities issued 43 Thai baht-denominated bonds in Thailand, with an outstanding value of $2.1 billion at the end of 2020. These issuances benefitted from Thailand's relaxation of investment rules and close economic ties with Lao People's Democratic Republic. In a similar vein, smaller countries in Asia and the Pacific could tap domestic savings in neighbouring emerging economies with close economic connections. Examples include China for Mongolia, and India for Bhutan and Nepal. Multilateral development partners could support these initiatives by developing common market practices for cross-border bond issuances. In addition to offshore bonds, governments could also consider diaspora bonds, especially in countries with large remittance flows as a share of GDP, such as Nepal and Tonga. To benefit from this type of bond, issuing countries could conduct demand analysis to gauge the willingness and ability of diaspora communities to invest in bonds, offer diversity in bond structures and launch marketing campaigns.

Debt swaps for development: Bangladesh, Indonesia, Pakistan and the Philippines engaged in debt swaps during the 1980s and early 2000s. While these agreements were broadly consistent with national development policies, strong frontloading of counterpart payments reduced fiscal space in Indonesia in the first few years. The overall impact on public debt reduction was small given the modest scale of debt relief. Learning from past lessons, countries should conduct independent feasibility studies to identify the amount and profile of swappable public debt, beneficiary projects, co-financing sources and the debt discount rate. Relevant stakeholders could seek to reduce the transaction costs of debt swaps, since elements such as a time-consuming negotiation process, feasibility studies and financial and legal fees can add up to 5 per cent of the debt value. Other efforts can be made to scale up debt swaps and minimize fund fungibility.

Emergency financing mechanisms: Many countries in East and South Asia have dedicated reserve funds for natural disasters. But catastrophic risk insurance schemes, based on a risk-transfer modality and especially important during low-frequency, high-impact events, remain uncommon. Some examples of existing schemes include agricultural insurance in Bangladesh, India and Mongolia, earthquake insurance in China and public asset insurance in Indonesia and Viet Nam. Covered losses are mostly small, however. At a subregional level, a catastrophe risk insurance pool for the Pacific islands was set up in 2016 and has so far made three payouts worth $6.7 million to Tonga and Vanuatu. To enhance emergency financing mechanisms, countries need to incorporate sovereign catastrophic risks into government financial planning and explore risk-transfer financial instruments for emergencies. Development partners can help by establishing more regional catastrophic risk-sharing initiatives and coordinating regional emergency funds.

Sustainable investing by public institutional investors: Financial assets under management by pension funds and sovereign wealth funds in Asia and the Pacific stood at about $8.5 trillion at the end of 2020. Relative to GDP, these assets are particularly large in Brunei Darussalam, Solomon Islands, Timor-Leste and Tuvalu. Yet the extent of sustainable investing by public institutional investors appears limited. Moving forward, one policy option is to relax investment rules in line with a careful review of the impact on portfolio risk. For example, certain pension funds in India, Pakistan and the Republic of

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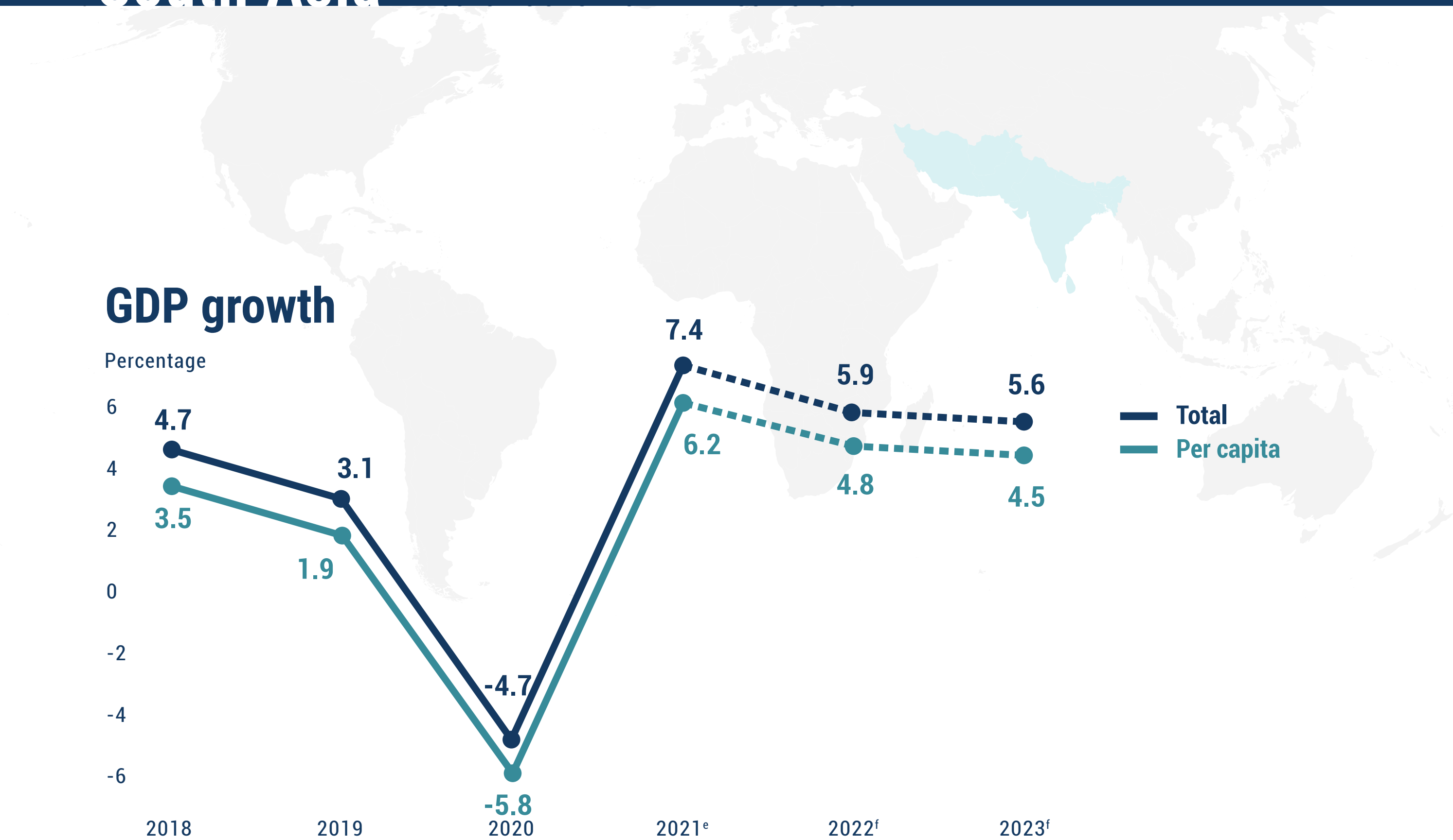
Korea are not allowed to invest in domestic equities or allowed but with maximum limits. Similarly, there are often maximum portfolio limits on investments in sovereign bonds and requirements to invest only in corporate bonds with certain ratings. Pension funds in India and Indonesia are prohibited from investing in foreign equities and bonds.

Still low inflation leaves room to maintain accommodative monetary policies

Low and relatively stable inflation offers some flexibility for central banks. Most kept accommodative monetary policy stances in 2021, maintaining policy rates at historically low levels after massive rate cuts in 2020. Central banks have also used other tools, including lowering reserve requirement ratios, extending lending operations and purchasing assets. Rising inflationary pressure in some countries has prompted central banks to change policy direction. The Bank of Korea raised its policy rate in August 2021, aiming to cool the real estate sector. The Monetary Authority of Singapore unexpectedly tightened policy in October 2021 to counter imported cost pressures. In 2022, overall monetary stances still need to be accommodative to sustain a fledgling recovery, however. While changing monetary policy stances in major developed countries, especially the tapering of quantitative easing in the United States, may pressure East Asian central banks to begin tightening, a cautious approach is warranted if changes in interest rates are not driven by better economic conditions.

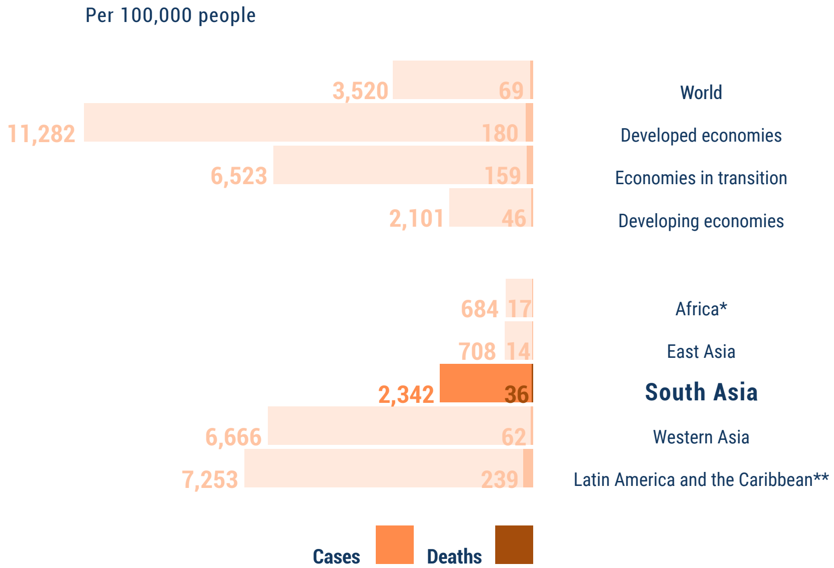
South Asia

GDP growth



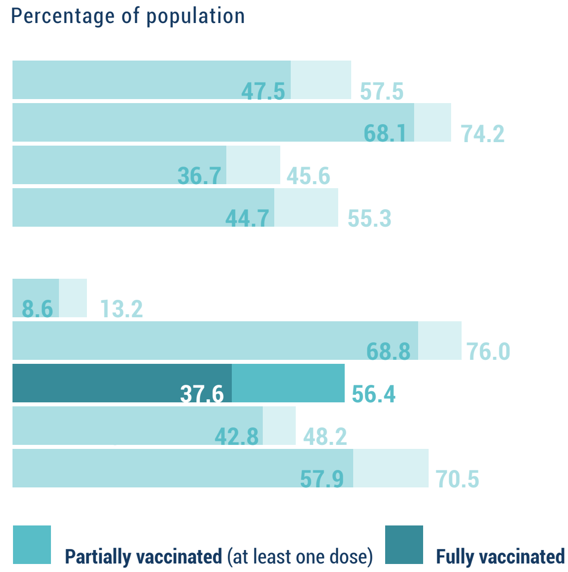
COVID-19 cases & deaths

as of 20 December 2021



Vaccination

as of 20 December 2021



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* Excluding Libya; **Excluding Bolivarian Republic of Venezuela. **e:** 2021 estimates. **f:** 2022-2023 forecasts.

Source for COVID-19 data: UN DESA calculations, based on data from Johns Hopkins University.

South Asia: moderate economic prospects amid large uncertainties and more constrained policy space

- South Asia's recovery is gathering steam but remains fragile and subject to downside risks.
- Revitalizing employment growth is crucial to tackle worsening poverty and inequality.
- Amid higher public debt and prospects for tightening financial conditions, fiscal policy faces increasing constraints.

South Asia confronts challenges to achieving robust and inclusive growth

The economic recovery continues to gain momentum in South Asia amid contained COVID-19 infections and higher mobility, robust remittance inflows and broadly supportive macroeconomic policy stances. After an estimated expansion of 7.4 per cent in 2021, regional GDP is projected to expand at a more moderate pace of 5.9 per cent in 2022 as base effects gradually disappear.[22] The recovery, however, is still fragile, uneven and subject to pandemic-related uncertainties and downside risks. A lagging labour market recovery illustrates the severe socioeconomic difficulties for large segments of the population. Achieving robust, sustained and inclusive growth will be critical in tackling the region's recent rise in poverty and inequality, with the pandemic erasing years of progress on poverty reduction and an estimated 30 million more people in extreme poverty in 2020. A sustained recovery may prove challenging as global financial conditions tighten, however, and monetary and fiscal policy space become more constrained. Policymakers need to maintain essential support for the recovery and job creation, such as by prioritizing public infrastructure and green investments that crowd-in private finance.

The outlook is highly uncertain and subject to downside risks

South Asia faces major downside risks that can strengthen headwinds in achieving the 2030 Agenda. Relatively slow vaccination progress leaves the region vulnerable to new variants and recurrent outbreaks. Financial constraints and an inadequate global vaccine supply continue to drag down full recovery in some countries. As of early December 2021, Bangladesh, Nepal and Pakistan had less than 26 per cent of their populations fully vaccinated (figure III.16). By contrast, the fully vaccinated population is above 64 per cent in Bhutan, Maldives and Sri Lanka. In India, a deadly wave of infection with the Delta variant stole 240,000 lives between April and June and disrupted economic recovery. Similar episodes could take place in the near term.

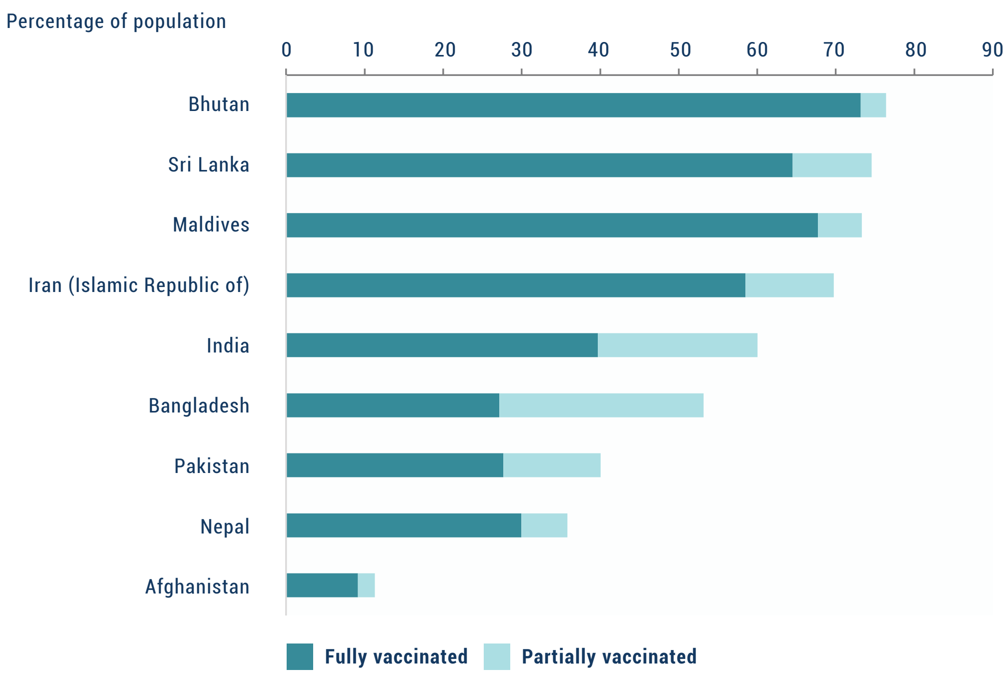
Accelerated global monetary tightening could increase volatility, trigger capital outflows and disrupt credit growth, especially in countries with elevated debt, large financing needs and high levels of foreign-currency-denominated debt. Significant financial distress could emerge as highly leveraged firms face greater refinancing costs, particularly in sectors hit harder by lockdowns, even more so if the removal of forbearance measures uncovers a large deterioration in balance sheets. In Bangladesh and Bhutan, non-performing loans were elevated even before the pandemic. While still vulnerable, India is in a better position to navigate financial turbulence compared to its situation during the "taper tantrum"

22 All growth figures for South Asia are on a calendar year basis. For fiscal year growth figures, please refer to the Statistical Annex.

episode after the 2008-2009 global financial crisis. This is due to a stronger external position and measures to minimize risks to bank balance sheets. In the medium-term, scarring effects from higher public and private debt or permanent impacts on labour markets could reduce potential growth and prospects for poverty reduction.

Figure III.16

South Asia's vaccination progress (as of 20 December 2021)



Source: UN DESA, based on data from Our World in Data (accessed on 20 December 2021).

Economic activity has gathered pace in Bangladesh and India

India's economic recovery is on a solid path, amid rapid vaccination progress, less stringent social restrictions and still supportive fiscal and monetary stances. GDP is projected to expand by 6.7 per cent in 2022 (figure III.17) after a 9 per cent expansion in 2021, as base effects wane. Robust export growth and public investments underpin economic activity, but high oil prices and coal shortages could put the brakes on economic activity in the near term. It will remain crucial to encourage private investment to support inclusive growth beyond the recovery. India has taken an important step by committing to 50 per cent of its energy mix coming from renewable sources by 2030 and to reaching net-zero emissions by 2070. Amid sound macroeconomic policies, Bangladesh has navigated the COVID-19 pandemic relatively well. GDP is projected to expand by 6 per cent in 2022. Economic activity rides on export growth and the rising demand for apparel, robust remittance inflows, and accommodative fiscal and monetary policies. The economy of Pakistan also remains on a relatively robust recovery path. After an economic expansion of 4.5 per cent in 2021, GDP growth is projected at 3.9 per cent in 2022, driven by private consumption, record-high remittances and fiscal support. The outlook for the Islamic Republic of Iran continues to improve after severe difficulties in recent years, supported by rising gas and oil exports. GDP is projected to expand by 3.1 per cent in 2022, following an expansion of 2.9 per cent in 2021.

Figure III.17

GDP growth in select South Asian countries

Source: UN DESA.
Note: e = estimates, f = forecasts.

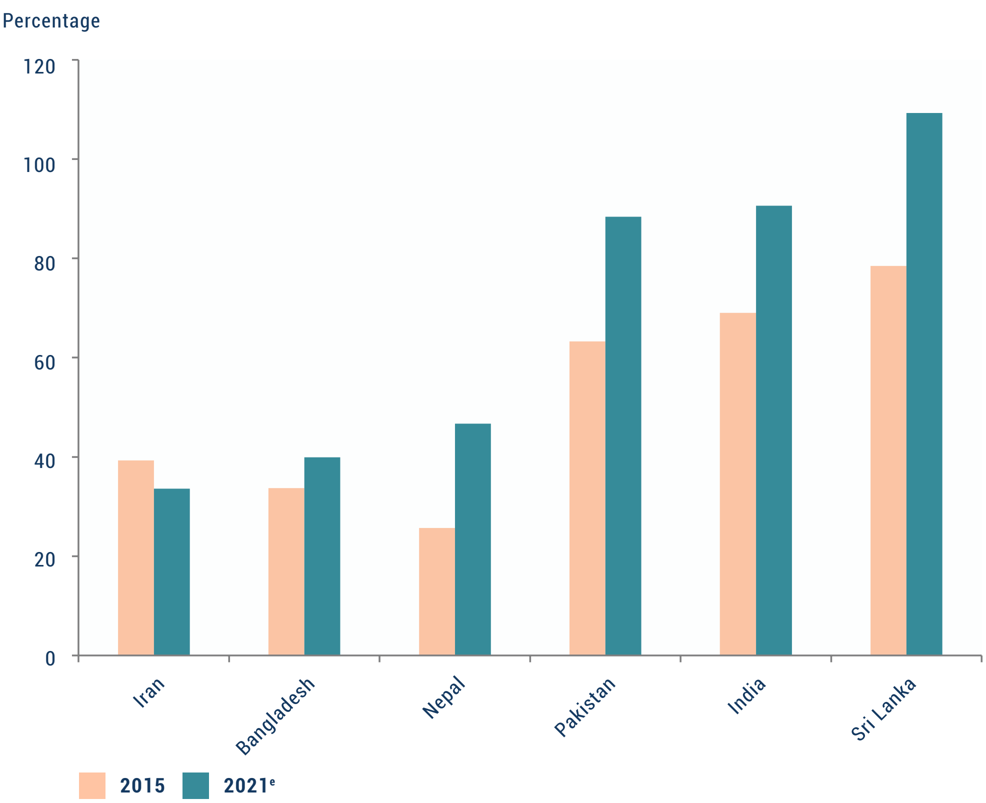
Sri Lanka faces major challenges; Afghanistan is on the brink of economic meltdown

The outlook is more challenging for other countries in South Asia, including those more dependent on tourism. In the Maldives, economic activity is gradually improving partly due to a solid rebound in international tourism. But renewed COVID-19 outbreaks, locally and abroad, could easily derail recovery. GDP may remain well below pre-pandemic levels; the risk of debt distress could be high. In Sri Lanka, GDP growth is projected at 2.6 per cent in 2022. Its major challenges include food shortages, dwindling foreign reserves and sovereign debt risks. Afghanistan's severe downturn has come amid drastic political changes, a decline in international aid and a lack of access to offshore assets. The worsening situation is leading to extreme poverty and food insecurity with the risk of the entire country becoming a humanitarian catastrophe.[23]

More constrained fiscal policy space

In South Asia, fiscal responses to the crisis were relatively restrained compared to other regions, largely due to sovereign credit ratings and debt-to-GDP ratios. Fiscal policies remain moderately supportive as the recovery gathers pace. In India and Pakistan, fiscal deficits are projected to decline gradually. At the same time, policy priorities have shifted towards capital expenditure. Pressures for fiscal consolidation will likely increase from higher public debt and rising borrowing costs (figure III.18). Amid elevated social needs, a still fragile recovery and lagging employment, it is imperative to avoid premature consolidation, however. The weak debt situation emphasizes the need for revenue mobilization (box III.3) as well as further multilateral support, especially for countries with elevated sovereign risks. Yet the G20 Debt Service Suspension Initiative did not provide substantial relief to eligible countries, namely, Afghanistan, Maldives, Nepal and Pakistan. Relief stood at less than 20 per cent of debt service obligations or about 1.6 per cent of GDP, on average.

Figure III.18
Public debt over GDP in select South Asian countries



Source: UN DESA based on IMF, 2021a.
Note: e = estimates.

23 The United Nations estimated that about 23 million people would be at risk of acute hunger, with 3.2 million children expected to suffer from malnutrition (IPC, 2021).

Inflation prospects remain largely stable

Inflation is projected to remain largely stable in most economies in South Asia, which offers flexibility to central banks before they move to more restrictive monetary stances. After inflationary pressures gained momentum in early 2021 due to supply constraints and rising energy prices, consumer price inflation has tended to subside. At the aggregate level, it is projected at 8.4 per cent in 2022. In India, inflation is expected to decelerate throughout 2022, continuing a trend observed since the second half of 2021 when relatively restrained food prices compensated for higher oil prices. A sudden and renewed rise in food inflation, however, due to unpredictable weather, broader supply disruptions and higher agricultural prices, could undermine food security, reduce real incomes and increase hunger across the region. In the Islamic Republic of Iran, inflation remains elevated due to depreciation of the domestic currency and the monetization of fiscal deficits.

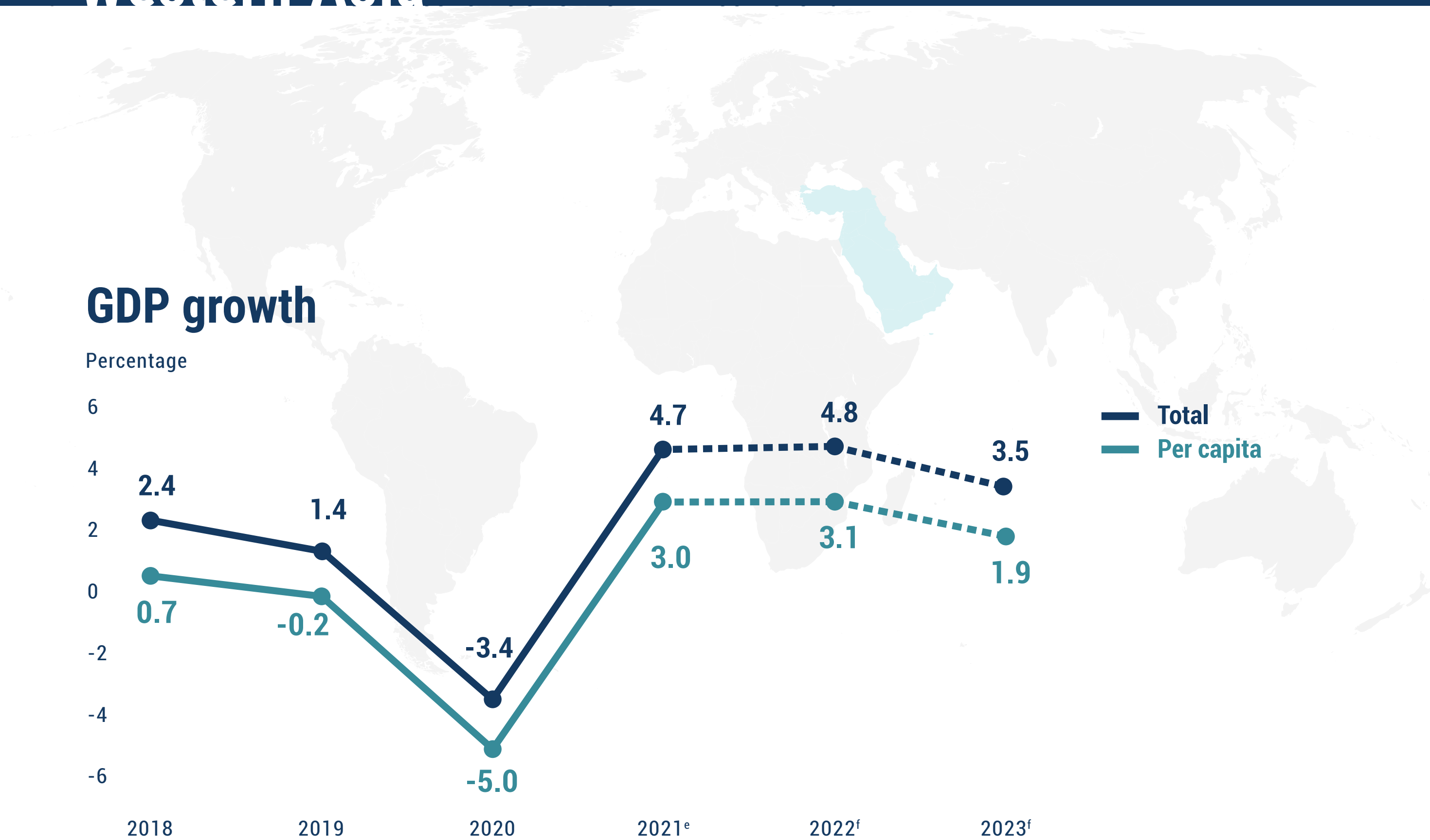
The monetary cycle is gradually shifting towards a less accommodative stance

Monetary policies remain accommodative with interest rates close to record lows and liquidity measures still in place in most economies. Yet the monetary cycle is gradually shifting as global financial conditions tighten and the recovery gains steam. The Reserve Bank of India has begun to taper liquidity by increasing the volume of reverse repo operations and the cash reserve ratio; it is expected to raise interest rates throughout 2022. The central banks of Pakistan and Sri Lanka increased interest rates in the second half of 2021 amid rising inflation and widening current account deficits. Central banks need to assess the magnitude and timing of policy changes to support an inclusive recovery and maintain financial and price stability.

Western Asia

GDP growth

Percentage



COVID-19 cases & deaths

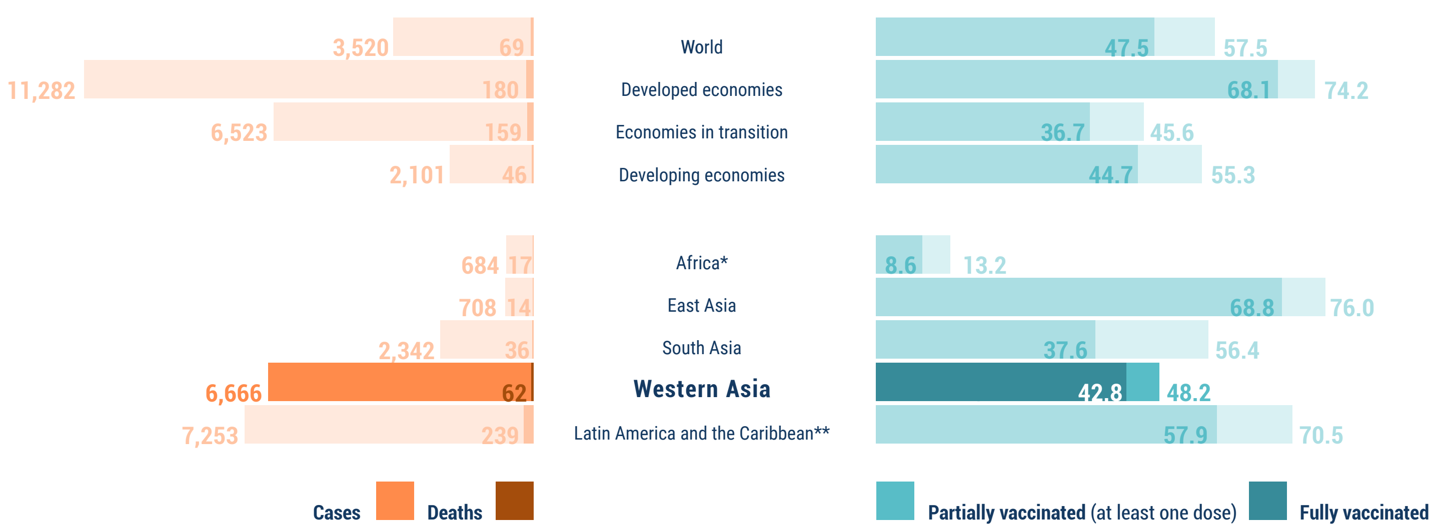
as of 20 December 2021

Per 100,000 people

Vaccination

as of 20 December 2021

Percentage of population



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* Excluding Libya; **Excluding Bolivarian Republic of Venezuela. **e:** 2021 estimates. **f:** 2022-2023 forecasts.

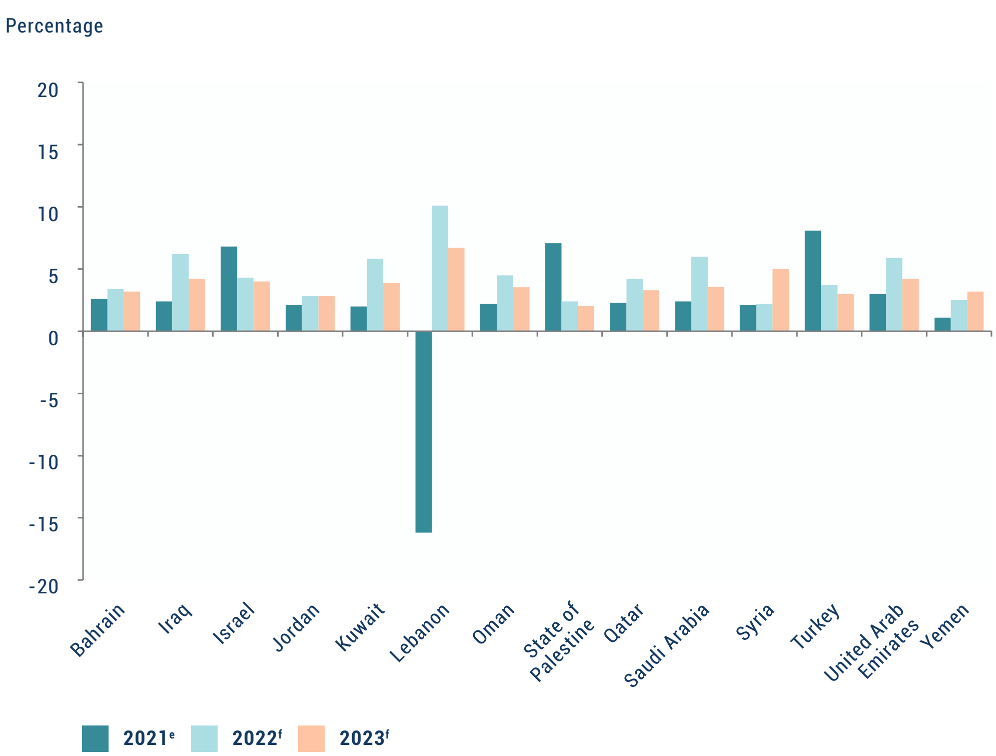
Source for COVID-19 data: UN DESA calculations, based on data from Johns Hopkins University.

Western Asia: recovery to continue in 2022

- The slow recovery of crude oil production countered the rapid recovery of domestic demand.
- Economic sentiment improved in the second half of 2021 with progress on vaccination.
- A robust recovery is forecast to continue in 2022 with an expected increase in crude oil production.

The Western Asian economies grew an estimated 4.7 per cent in 2021. With the relaxation of pandemic control measures and the progress of vaccination, economic activities recovered rapidly particularly in the second half of the year. Strong domestic demand was seen after the substantial plunge in the previous year, leading recovery in Israel and Turkey. While the unemployment rate declined towards pre-pandemic trends in Israel, Saudi Arabia and Turkey, the speed of employment recovery has been slower in other countries. The employment situation is dire in Iraq, Lebanon, the State of Palestine, the Syrian Arab Republic and Yemen.

Figure III.19
Recovery forecast for Western Asia



Source: UN DESA, based on projections produced with the World Economic Forecasting Model.
Note: e = estimates, f = forecasts.

GDP growth is modest in Gulf Cooperation Council countries due to little expansion in crude oil production

Estimated GDP growth in 2021 was modest in major crude oil producers, namely the member countries of the Gulf Cooperation Council (GCC): Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. Strongly recovering energy prices contributed to overall improved economic sentiment but production coordination under OPEC[24] meant that crude oil production in the GCC countries likely increased only slightly from 2020. In real terms, the oil sector's contribution to GDP growth is estimated as extremely modest relative to the contribution from the rapidly recovering non-oil sector. Iraq is following a similar recovery path although the recovery of its non-oil sector has been more modest.

Recovery has stagnated in other countries in the region

Despite resilience in 2020, Jordan has seen a slow recovery due to the stagnation of service exports, namely tourism. The economic situation in Lebanon further deteriorated against a deepening financial crisis (see box III.4). Ongoing armed conflict has hampered economic recovery in the Syrian Arab Republic and Yemen.

Box III.4

The anatomy of the Lebanese financial crisis

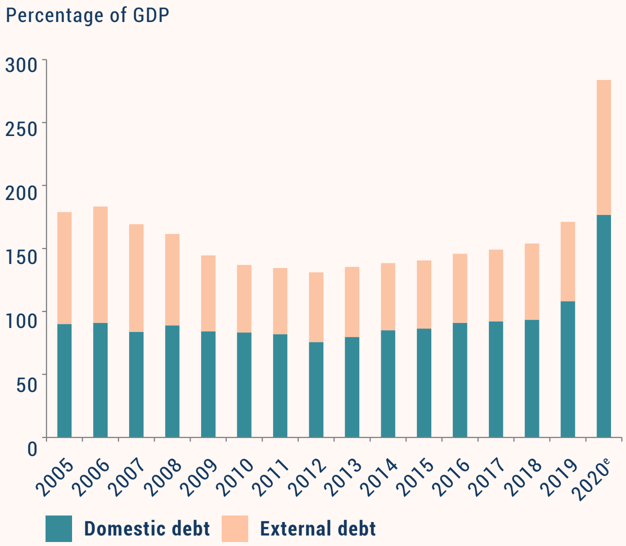
Lebanon faces an unprecedented economic and financial crisis, with GDP growth contracting by 7.2 per cent in 2019 and 37.1 per cent in 2020. While COVID-19, the subsequent loss of tourism revenues and the devastating Beirut port explosion were major drivers of the downturn, an unravelling financial crisis is also a significant factor. In March 2020, Prime Minister Hassan Diab announced that Lebanon would not be able to pay a Eurobond of $1.2 billion. As of November 2021, a new Government, formed after a year-long political vacuum, is about to restart difficult negotiations with the IMF on debt restructuring and default.

For almost two decades, Lebanon received huge foreign currency inflows. These primarily comprised remittances from the very large Lebanese diaspora, which may total 15.4 million people, greatly outstripping an internal population of 6 million (Pukas, 2018). Lebanon also benefited from its reputation as a safe haven for savings from war-torn Syria. Inflows were directed to domestic banks, which bought Eurobonds issued by the Government. In 2019, as the supply of foreign currency significantly decreased, the Government faced difficulties in financing the debt and maintaining the official exchange rate. It announced measures to improve liquidity, including taxes on gasoline, tobacco and VoIP applications. These plans triggered massive social protests dubbed the 17 October Revolution. The unrest combined with a worsening economic situation to propel a bank run with depositors rushing to withdraw foreign currency deposits from Lebanese banks. Facing shortages of cash, banks froze foreign currency deposits on 17 October 2019 and began limiting withdrawals to $1,000 per month. Withdrawals were halted completely a few months later without any official capital control measure.

24 See OPEC (2021) for details.

Figure III.4.a

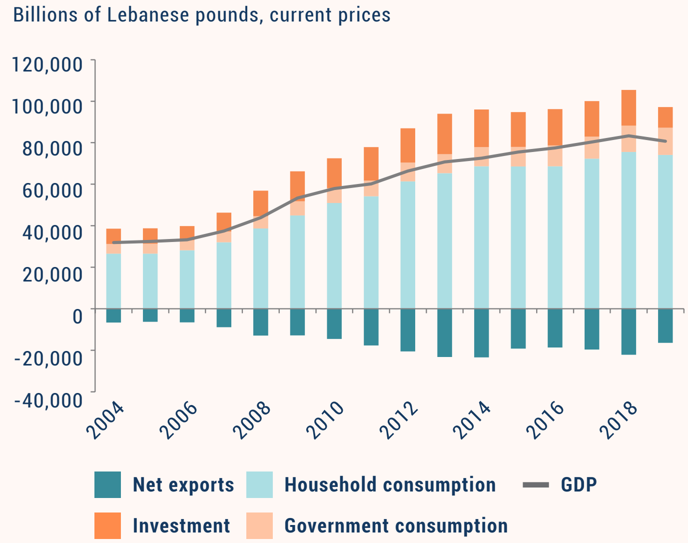
The structure of Lebanese public debt



Source: Lebanon, Ministry of Finance and Central Administration of Statistics.
Note: e = estimation.

Figure III.4.b

The composition of Lebanese GDP



Source: Lebanon, Central Administration of Statistics.

The freeze on foreign currency deposits led to the immediate birth of a black market for cash dollars. Initially, the Central Bank provided importers with currency to finance the huge Lebanese current account deficit. This meant the black market rate hovered around LBP2,000-2,500 per dollar, with the official peg maintained at LBP1,507 per dollar. With dwindling foreign reserves, however, the portfolio of products financed at the official rate began shrinking. By the beginning of 2021, only medicines, essential food products, medical equipment and fuel imports were financed at the official rate in ever smaller amounts, leading to huge shortages in Lebanese pharmacies and petrol stations. As of September 2021, the Central Bank announced that it will no longer finance these imports, which caused massive price increases. At the same time, the black market exchange rate had risen to almost LBP21,000 per dollar, meaning the Lebanese pound had lost 93 per cent of its value even as the official peg was maintained.[a] These developments spurred inflation to enormous levels of 85 per cent in 2020 and an estimated 128 per cent in 2021.

This situation has several consequences for negotiations on debt restructuring. First, pound-denominated debt has become less of a concern because a default has effectively taken place through inflation, even though the debt is still officially being repaid. Second, a significant share of Lebanese market-issued Eurobonds, which constitute 94 per cent of total foreign debt, is held by local banks and the Central Bank ($11 billion and $5 billion out of $31.3 billion in outstanding debt, respectively). This means that a significant haircut in dollar-denominated deposits is inevitable. A question hangs over whether such a solution will be accepted by depositors, even though these deposits have been effectively frozen for more than two years despite some measures to allow small withdrawals in pounds at unfavourable rates (Banque du Liban, 2021).

Another element is that two decades of massive foreign inflows financed huge current account deficits (figure III.4.2), leading to the overvaluation of the pound and dampening export competitiveness. Amid minimal investment in public infrastructure and productive sectors and the lack of a 24-hour electricity supply, restoring the current account balance will be painful, requiring a major wage adjustment. This problem is especially acute given that the main Lebanese export sectors – tourism and knowledge-intensive services – were severely damaged by the pandemic, on top of the brain drain triggered by the economic situation.

Due to the toxic combination of the financial crisis, the COVID-19 pandemic and the Beirut blast, Lebanon's poverty rate has shot up from 42 per cent in 2019 to 82 per cent in 2021. Among the poor, 40 per cent suffer extreme multidimensional poverty (ESCWA, 2021b). Safeguarding them against further deterioration in dignity and well-being is of primary importance and needs to be taken seriously in further negotiations with international donors.

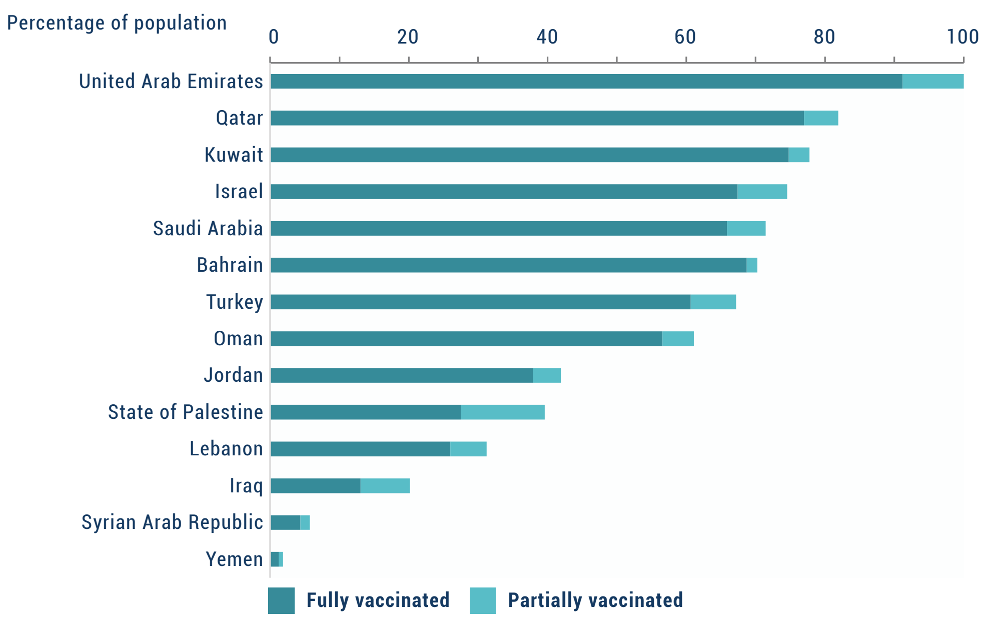
a As of November 2021, the official exchange rate stood at LBP1,507 per dollar. Three other officially designated exchange rates were in place serving different purposes, including LBP3,900 per dollar and LBP12,000 per dollar for bank withdrawals under different conditions. The Central Bank's Sayrafa platform supplied dollars for importers at a rate that reached LBP19,000 per dollar.

Authors: Ahmed Moummi and Jan Gaska, United Nations Economic and Social Commission for Western Asia

In Western Asia, COVID-19 outbreaks were generally contained by the end of 2021, after multiple surges in cases. Israel and Turkey went through Delta variant outbreaks in the second half of 2021. Further outbreaks in all countries remain a possibility.

Figure III.20

Vaccination progress in Western Asia (as of 20 December 2021)



Source: UN DESA, based on data from Our World in Data (accessed on 20 December 2021).

Vaccination programmes progressed quickly in the GCC countries, Israel and Turkey, with more than half of the population having received two shots by October 2021 (figure III.20). In Israel, Turkey and the United Arab Emirates, additional booster shots were administered in the second half of the year. Other countries struggled to raise the vaccination rate amid supply constraints and vaccine hesitancy. Despite these difficulties, vaccination has steadily progressed in Iraq, Jordan, Lebanon and the State of Palestine. The vaccination rate is likely extremely low for Syria and Yemen.

Pandemic control measures eased in the second half of 2021

In the first half of 2021, COVID-19 outbreaks compelled governments to introduce lockdowns, curfews, social distancing and mask requirements. Stringent lockdowns of various duration were implemented in most countries. These measures were eased in the second half of the year, replaced by vaccination promotion, including booster shots, and with softer social distancing measures. Border entry restrictions have also gradually lifted, replaced by COVID-19 test and vaccination requirements, although Israel temporarily closed its borders due to the emergence of the Omicron variant.

Fiscal balances improved with recovering energy export prices and tax revenues

In 2021, recovering energy export prices and tax revenues improved fiscal balances after a sharp deterioration in the previous fiscal year. Fiscal expenditure growth in 2021 was estimated as moderate, however, focusing on public health and other essential areas. Governments were obliged to step up fiscal consolidation in the face of rapidly growing public debt (ESCWA, 2021a). Fiscal expenditure in real terms significantly declined in Lebanon and Syria amid high inflation rates.

Efforts to diversify fiscal revenue sources in the GCC countries continued. Oman introduced a value added tax with a 5 per cent rate in April 2021, with Kuwait and Qatar expected to follow in the near future. Bahrain, Saudi Arabia and the United Arab Emirates had already introduced a 5 per cent value added tax in 2016, in accordance with the GCC Common Value Added Tax Agreement. Saudi Arabia raised the rate to 15 per cent in 2020, and Bahrain is scheduled to raise it to 10 per cent in 2022.

Monetary policy has remained expansionary for most countries

Monetary policy has remained expansionary in the GCC countries, Iraq, Israel, Jordan and Turkey. For Lebanon and Syria, the monetary stance has resulted in extremely tight financial conditions through a substantial devaluation of the national currency.

Despite global supply-chain disruptions, inflation pressures generally remain weak

Inflationary pressures have remained weak except in Lebanon, Syria, Turkey and Yemen. The main factor contributing to high inflation in these countries has been a tight balance-of-payments condition that resulted in a substantial devaluation of the national currency. Inflation in Lebanon reached an estimated 128 per cent in 2021 due to an exchange rate pass through. Inflationary pressure from global supply-chain disruptions remained weak in Western Asia in 2021 although supply-chain disruptions remain a risk into 2022.

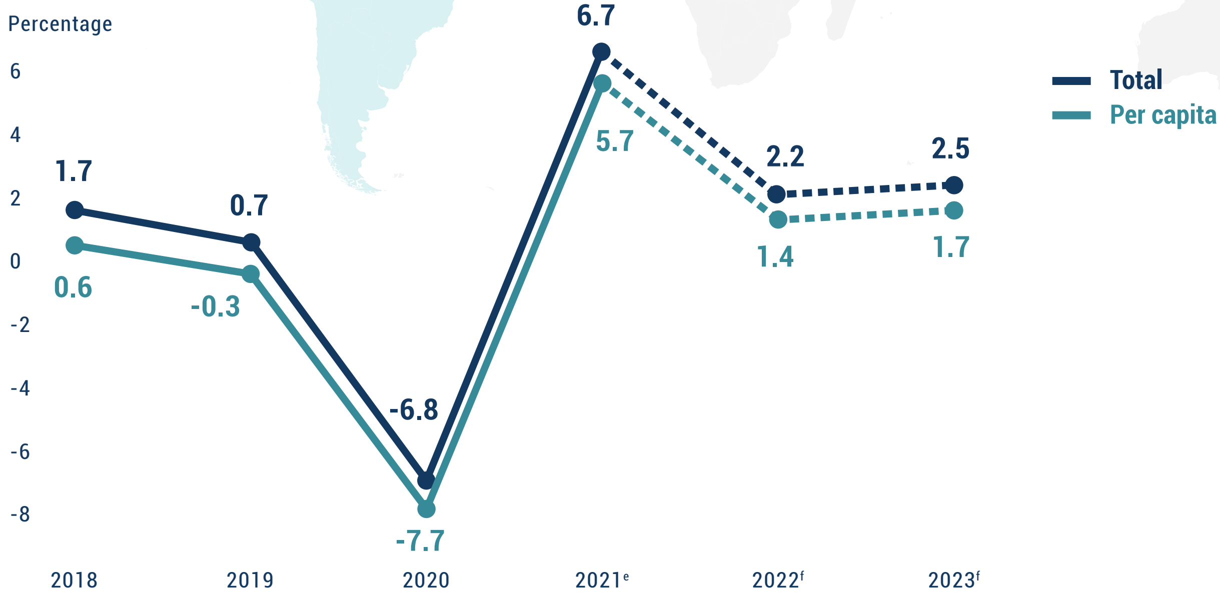
A robust recovery is forecast to continue in 2022 amid downside risks

The region's economy is projected to grow by 4.8 per cent in 2022. The expected expiration of the OPEC+ crude production coordination in 2022 will allow oil-exporting countries to increase crude oil production towards pre-pandemic levels. The resumption of international tourism will support further recovery. Significant downside risks remain from geopolitical tensions and high unemployment, however. Prolonged conflict in the State of Palestine, Syria and Yemen largely explains uneven recovery in the region, especially where the economic situation was dire even before the pandemic. High unemployment rates remain among the region's most important socioeconomic concerns and need to be resolved.

Latin America and the Caribbean

GDP growth

Percentage



COVID-19 cases & deaths

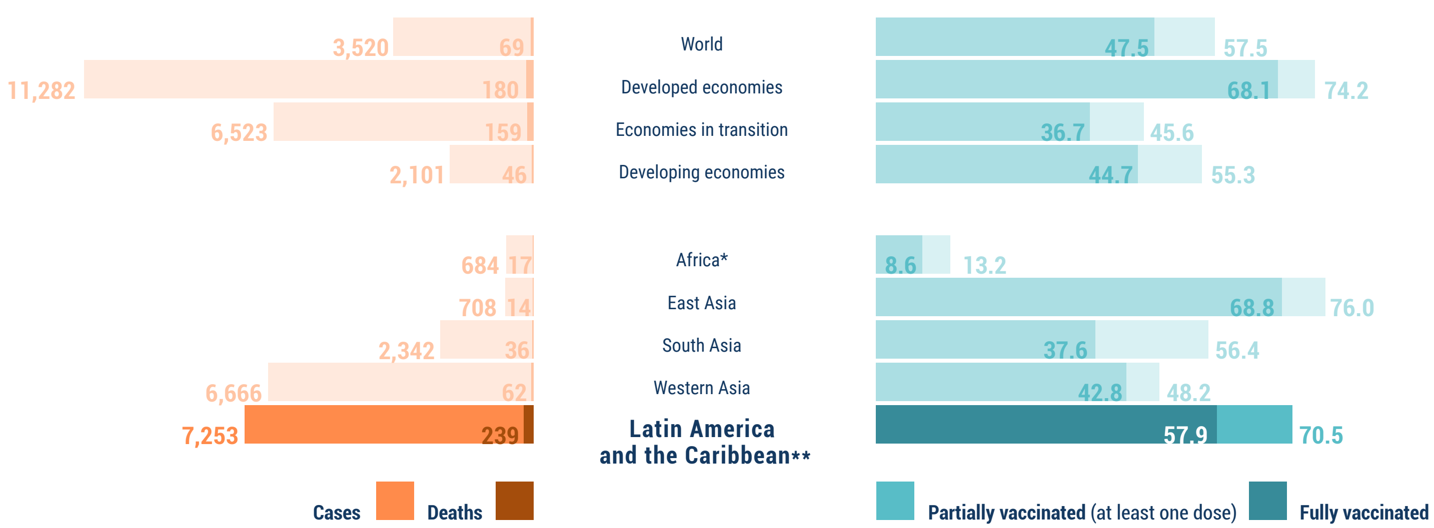
as of 20 December 2021

Per 100,000 people

Vaccination

as of 20 December 2021

Percentage of population



Note: The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations. The map represents countries and/or territories or parts thereof for which data is available and/or analysed in World Economic Situation and Prospects 2022. The shaded areas therefore do not necessarily overlap entirely with the delimitation of their frontiers or boundaries. Aggregate data for Africa, excluding Libya.

* Excluding Libya; **Excluding Bolivarian Republic of Venezuela. **e:** 2021 estimates. **f:** 2022-2023 forecasts.

Source for COVID-19 data: UN DESA calculations, based on data from Johns Hopkins University.

Latin America and the Caribbean: recovery to lose steam amid fading external tailwinds and policy tightening

- Despite a faster-than-expected rebound in economic activity, the region faces lasting damage from the pandemic.
- Governments and central banks are expected to withdraw policy support to address fiscal pressures and combat rapidly rising inflation.
- The spread of new COVID-19 variants, a sharp tightening of global financial conditions, and social and political instability pose significant downside risks.

After a strong recovery from COVID-19, a slowdown is looming

Economies in Latin America and the Caribbean have largely rebounded from the COVID-19-induced recession, amid favourable external conditions, successful vaccine roll-outs and strong domestic policy support. But recovery has been insufficient to reverse damage from the pandemic, which has pushed millions out of work and into poverty. As global tailwinds recede and structural weaknesses exacerbated by the pandemic resurface, the region faces the prospect of a sharp economic slowdown, with growth returning to its weak pre-crisis trend. Real GDP expanded by an estimated 6.5 per cent in 2021 following the 7.4 per cent contraction in 2020, the region's deepest pull back in 120 years (Maddison Project Database, 2020). Growth is projected to average only 2.2 per cent in 2022 and 2.5 per cent in 2023. Uncertainties surrounding these forecasts remain exceptionally large as the region confronts significant downside risks, including the spread of more contagious or deadly COVID-19 variants, a sharp tightening of global financial conditions, and mounting social and political instability.

The region has experienced faster-than-expected but uneven recovery in economic activity over the past year. The growth rebound in 2021 was partly due to strong base effects, stemming from the output collapse at the beginning of the pandemic, but also reflected improved domestic conditions and supportive external factors. Many countries in Central America and South America recorded high growth rates, with annual GDP expanding at double-digit rates in Chile, Panama and Peru. The Caribbean small island developing States recovered more slowly as fiscal policy was less supportive, due to high levels of debt, and because they depend on international travel, which resumed only gradually.

The pandemic has loosened its grip on the region's economy

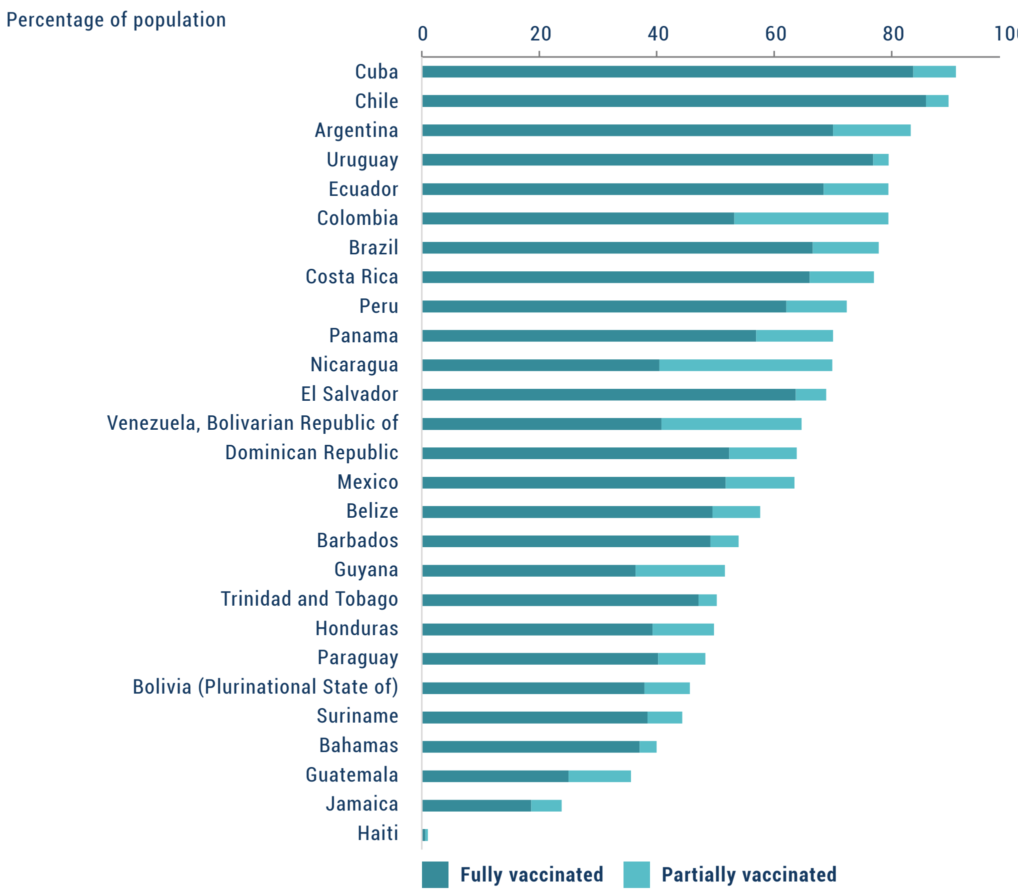
The pandemic has loosened its grip as governments, businesses and households have adapted to restrictions, which are having much less of an impact on output than in the early stages of the crisis (Oliveros-Rosen, 2021). The release of pent-up demand has driven higher private consumption and investment. With the numbers of daily COVID-19 cases and deaths declining sharply since mid-2021 amid significant progress on vaccination, governments have also more assertively eased restrictions and reopened economies.[25] In about half of the countries, more than 50 per cent of people were fully

25 Latin America and the Caribbean's share of the death toll from COVID-19 is the highest in the world. In mid-November 2021, the region accounted for 30.1 per cent of global deaths from the pandemic while having only 8.4 per cent of the world's population.

vaccinated by the end of November 2021 (figure III.21). Disparities in vaccination rates remain large, however. In Bermuda, Chile, Cuba and Uruguay, more than 75 per cent of people are fully vaccinated compared to less than 20 per cent in Jamaica and under 1 per cent in Haiti.

Figure III.21

Vaccination progress in Latin America and the Caribbean (as of 20 December 2021)



Source: UN DESA, based on data from Our World in Data (accessed on 20 December 2021).

Favourable external conditions supported economic recovery

The region has benefited from supportive external conditions. Strong demand from its main trading partners, notably China, the European Union and the United States, has boosted export growth. The global recovery has also led to sharp increases in the prices of oil, metals and agricultural goods, with South America's commodity exporters recording significant improvements in their terms of trade (ECLAC, 2021a).[26] At the same time, rapid growth in remittance inflows, driven by a recovering economy in the United States, has supported private demand in Mexico, Central America and parts of

26 By contrast, Mexico, Central America and the Caribbean experienced a slight worsening in the terms of trade in 2021.

the Caribbean.[27] Total remittance flows to the region reached an estimated record high of $126 billion in 2021, up 21.6 per cent over 2020 (World Bank, 2021c). Exceptionally accommodative global financial conditions have allowed governments and businesses across the region to access international financing on favourable terms.

Fading external tailwinds and policy tightening weigh on growth

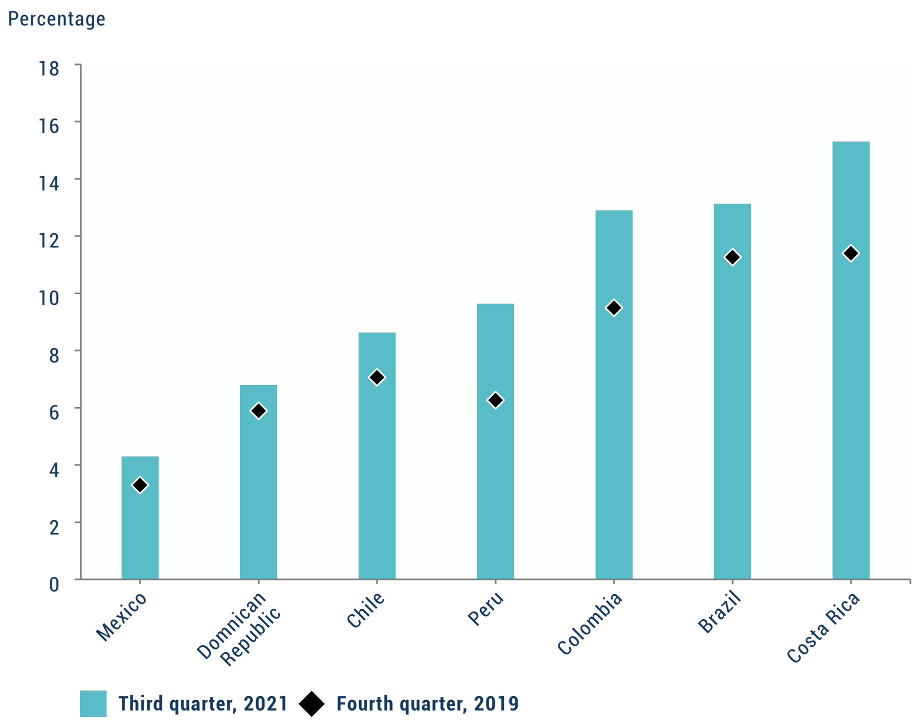
While South America's commodity exporters have led the region's pandemic recovery, their growth prospects for 2022 and 2023 are subdued. Tailwinds from higher commodity prices, buoyant demand from China and the United States and favourable global financial conditions will gradually fade. At the same time, central banks are expected to tighten monetary policy to combat rapidly rising inflationary pressures. Governments will increasingly move away from fiscal stimulus and towards the consolidation of public finances. Altogether, these factors are expected to lower GDP growth in South America to only 1.6 per cent in 2022. Short-term growth prospects are more favourable for Central America and especially the Caribbean, where the continued resumption of tourism will stimulate economic activities.

Labour market recovery has been slow and uneven

The region's labour markets have seen only a partial and uneven recovery after suffering an unprecedented shock during the early stages of the COVID-19 crisis. While economic activity rebounded, job creation has been insufficient in terms of quantity and quality. In most countries, unemployment rates have remained significantly higher and participation rates lower than before the pandemic (figure III.22). In addition, informal employment has accounted for a large portion of the jobs created during the recovery (ILO, 2021b). ECLAC (2021a) warns that unemployment rates may increase even further in the coming years as people re-enter the labour market. Risks of long-term unemployment are greatest for groups hit particularly hard by the pandemic, including young people, women and less educated workers. Box III.5 examines the pandemic's disproportionate impact on the employment of vulnerable groups, underscoring the need to adopt comprehensive macroeconomic and labour market policy packages.

27 In El Salvador, Guatemala, Honduras and Jamaica, the value of remittances exceeded 18 per cent of GDP in 2021.

Figure III.22
Unemployment rates in select Latin American countries



Source: CEIC, national data.

Box III.5

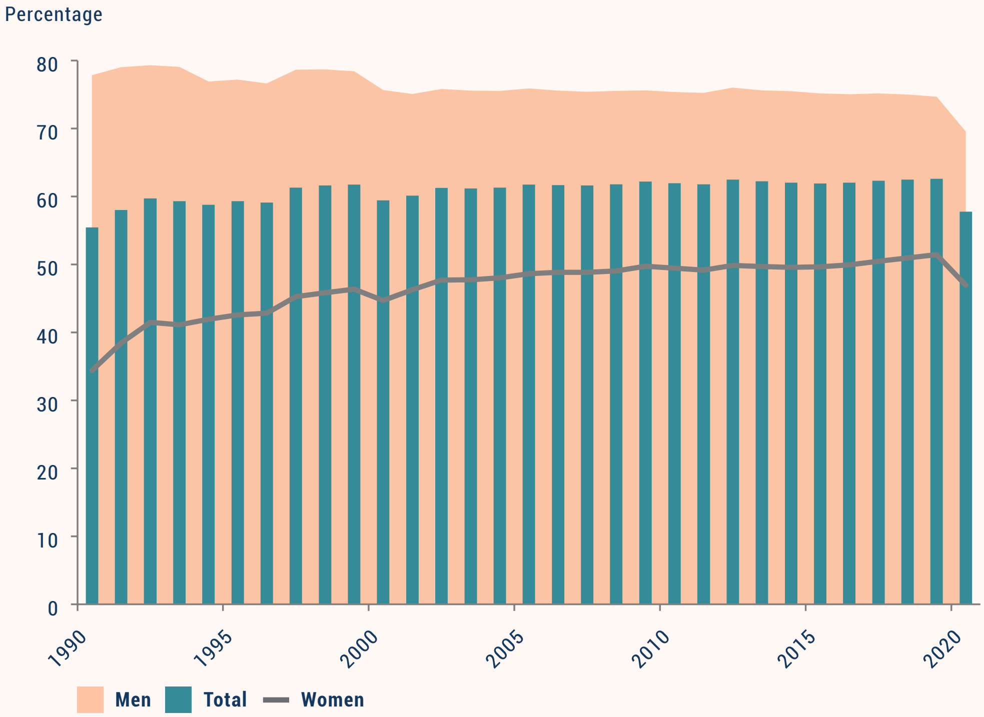
Healing from the pandemic: the impact of COVID-19 on labour markets in Latin America and the Caribbean and policies to promote a transformative recovery

The pandemic triggered an unprecedented crisis in labour markets across Latin American and the Caribbean. Although the entire global economy was affected in 2020, countries in this region saw the largest contraction in employment. It declined 3.5 per cent on average around the world but 9 per cent in Latin America and the Caribbean. Before the crisis, the region's pace of employment growth was already slowing, with 2010-2019 producing the most sluggish growth in the number of employed people since 1950.

For various reasons, the crisis weighed most heavily on employed women and the most vulnerable social groups, such as young people, migrants and less-educated workers. Between 2019 and 2020, the number of people in employment fell by almost 25 million, including about 13 million women. This resulted in a female unemployment rate of 11.9 per cent, up from 9.3 per cent in 2019. The unemployment rate for men in 2020 was 9.3 per cent compared with 6.9 per cent in 2019. These unemployment levels would have been higher (15.3 per cent for men and 22.2 per cent for women) if many workers had not withdrawn from the labour market altogether.

Figure III.5.a

Latin America and the Caribbean's labour force participation rate by gender



Source: ECLAC, based on official national data.

The crisis prompted a marked decline in labour force participation, especially among women, bringing an end to more than 30 years of continuous growth. By the close of 2020, women's participation rate was similar to that of 2001 (see figure III.5.a). This noticeable impact stems from women's strong presence in activities that were highly restricted during the pandemic, such as commerce and tourism, but also from the greater burden of unpaid work linked to household care for children, older persons and the sick that typically falls on women and in many cases grew worse during pandemic-related lockdowns.

Informal employment was heavily affected by the COVID-19 crisis, even as it provided work for nearly half of the people employed in Latin America and the Caribbean. In contrast to previous crises, informal employment did not act as a buffer in the labour market but actually fluctuated more than formal employment, as shown in figure III.5.b.

Figure III.5.b

People in formal and informal employment and total employed, first quarter of 2019 to fourth quarter of 2020

Source: ECLAC, based on official national data.
Note: Percentage change from the same quarter of the previous year.

The 2021 economic recovery boosted employment in the region but for most countries, neither economic activity nor employment returned to pre-crisis levels. In fact, in 2020, the number of employed persons fell by 25.3 million, of whom 17.3 million (68 per cent) returned to the labour force in 2021. This means the number of employed persons in the region was 2.8 per cent lower in 2021 than in 2019.

The total unemployment rate rose to 11 per cent, a rate worse for women at 12.7 per cent, 3 percentage points higher than the rate for men at 9.7 per cent.

Beyond the rebound in 2021, economic growth is likely to remain sluggish, which will not support rapid recovery in employment or improvements in the quality of jobs. Policies to drive the creation of high-quality jobs will be essential. These should focus on strengthening employment among groups most affected during the crisis, including women, young people and migrants. It is also necessary to support productive sectors with the greatest potential for job creation and labour market formalization, and to advance care systems that modify the traditional gender-based division of labour. Such systems should enshrine the right to care and the right to be cared for under conditions of quality and equality. All these steps should be taken in the medium term as the challenges will only grow if the region fails to break the pattern of weak growth seen before the COVID-19 crisis.

Fiscal stimulus packages to respond to COVID-19, particularly job support measures, have played a crucial role in protecting households and businesses and boosting aggregate demand. This support must be maintained in coming years to halt rising inequalities in the region. Furthermore, comprehensive short-term policies should support jobs and productivity and protect the incomes of the most disadvantaged groups, aiming for productive transformation capable of creating and maintaining high-quality jobs.

This comprehensive vision requires training, public employment programmes, employment subsidies, self-employment and microentrepreneurship programmes, employment services and infrastructure for labour intermediation, among other core measures.[a]

a See United Nations Economic Commission for Latin America and the Caribbean (2021a) for the strategies followed by Latin American economies to mitigate the impacts of the crisis and promote job creation during the recovery. UN Women and United Nations Economic Commission for Latin America and the Caribbean (2021) show the importance of comprehensive national care systems to foster growth and gender equality in the region.

Author: United Nations Economic Commission for Latin America and the Caribbean

Soaring food and energy prices have pushed inflation higher

The strong rebound in economic growth in Latin America and the Caribbean has been accompanied by rapidly rising inflationary pressures. Excluding the Bolivarian Republic of Venezuela, average consumer price inflation accelerated to an estimated 11.3 per cent in 2021, the fastest annual pace in more than two decades. In October, year-on-year inflation exceeded the central bank target range in all large economies (Argentina, Brazil, Chile, Colombia, Mexico and Peru). In contrast, upward pressures on prices have been more limited in most Central American countries. The recent surge in inflation reflects several factors, which vary in importance by country: the release of pent-up demand as pandemic-related restrictions have eased; supply shortages, for example, in the electronics, automotive and agricultural industries; higher prices of imported goods and services due to exchange rate depreciation; and, most importantly, soaring food and energy prices, which make up a larger share of consumer price indices in Latin America and the Caribbean than in developed countries. The spike in food prices has particularly affected low-income households, many of which are still reeling from the pandemic.

Inflation expectations have so far remained well anchored

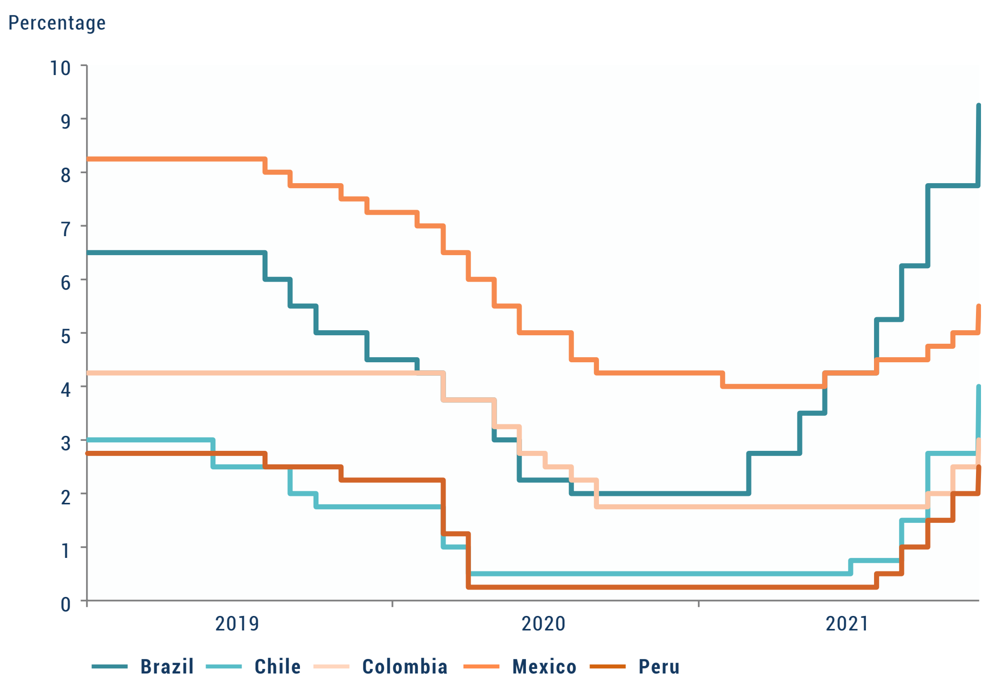
Medium-term inflation expectations have so far remained well anchored, reflecting improved monetary policy frameworks and greater central bank credibility in much of the region, even though the growth outlook for major economies remains weak. In August 2021, three-year-ahead inflation expectations were below 4 per cent in Brazil, Chile, Colombia, Mexico and Peru (IMF, 2021b). Although core inflation, which excludes volatile food and energy prices, has accelerated, most factors pushing prices up are likely temporary. Food and energy prices are expected to plateau in 2022, while demand pressures and supply-chain bottlenecks will likely ease gradually in the coming year. A baseline forecast projects average consumer price inflation in the region to moderate to 9.6 per cent in 2022 and 7.2 per cent in 2023. But large uncertainties surrounding the inflation outlook and concerns over deteriorating growth prospects present monetary policymakers with a challenging environment to navigate.

Several central banks have tightened monetary policy

After providing unprecedented monetary policy support in response to the pandemic, central banks started to withdraw monetary stimulus in 2021. Many have raised their policy rates, aiming to rein in inflationary pressures and prevent de-anchoring of inflation expectations (figure III.23). The Central Bank of Brazil has embarked on the most aggressive tightening cycle in the region, lifting its main policy rate from 2 per cent at the start of the year to 7.75 per cent in late October and projecting the rate will reach 9.75 per cent in 2022. Several other central banks, for example, in Chile, Colombia and Peru, accelerated tightening in late 2021. While the monetary tightening cycle is set to continue in 2022, the question is how aggressively central banks will raise borrowing costs. Since current upward pressure is partly due to global and supply-side factors, sharp tightening of monetary policy may not be effective in reducing inflation and could undermine a fragile and incomplete recovery. If it leads to increased capital inflows and exchange rate appreciations, it could hurt exports.

Figure III.23

Central bank policy rates in select Latin American countries



Source: Bank for International Settlements.

Pressures to consolidate public finances are likely to rise

Large-scale fiscal stimulus measures were vital in cushioning social fallout from the pandemic and supporting economic recovery in the region. Most governments, with major exceptions being Chile and Peru, started scaling back their extraordinary policy support in 2021 but spending levels remained significantly higher than before the crisis. At the same time, public revenues recovered through higher economic growth and rising commodity prices. This temporary cyclical improvement, however, should not obscure a still challenging fiscal outlook. With global financial conditions expected to tighten, pressures to consolidate public finances are likely to increase, especially for countries with large dollar-denominated debt (for example, Argentina and the Dominican Republic). In many countries, fiscal space will further shrink as the debt-servicing burden continues to rise. Given large and increasing demands for greater spending, including to strengthen health and education systems, expand social protection coverage, facilitate energy transition and carry forward policies to support industry and technology, additional resource mobilization will remain critical. Above all, this requires increasing contributions from direct taxes. More progressive taxation, coupled with increased efforts to close loopholes and combat tax evasion, can put public finances on a more solid footing while reducing income inequalities (Hanni and others, 2015; Martorano, 2018).