Global issues

Global economic growth remains heavily carbon-intensive

The baseline outlook presented in the latest World Economic Situation and Prospects (WESP) 2019 report projects steady economic growth in 2019–2020 at the global level, although risks to that outlook have continued to build. The report also notes that economic activity remains excessively dependent on carbon-intensive fossil fuels. Growth in gross domestic product (GDP) and carbon dioxide (CO₂) emissions remain closely linked. CO₂ emissions continue to rise but must start to decline well before 2030 to avert substantial changes to our natural and human systems. This requires a fundamental and more rapid shift in the way the world powers economic growth.

Economic growth and emissions

Continued global economic and population growth have driven a persistent rise in greenhouse gases (GHG) and other gases stemming from human activities. Between 1990 and 2015, as the global level of production doubled, anthropogenic GHG emissions increased by 45 per cent (International Energy Agency, 2018). CO₂ emissions constitute most of these emissions. CO₂ emissions from fuel combustion represented over two thirds of total GHG emissions in 2015. The primary use of fuel combustion is to generate energy, making the energy sector the largest contributor to global anthropogenic GHG emissions.

After three years of remaining flat, global energy-related CO₂ emissions increased 1.5 per cent in 2017, reaching a historical high. This resulted from the acceleration of global economic growth, supported by the relatively low cost of fossil fuels and weaker energy efficiency efforts, according to the International Energy Agency (IEA). Preliminary evidence of global energy-related CO₂ emissions suggests a further increase in 2018. At this rate, the IEA warns, current efforts to combat climate change are insufficient to meet the objectives of the Paris Agreement.

Growth in GDP and emissions remain closely linked (figure 1). In 2017, a 1.0 per cent increase in world gross product was associated with a 0.5 per cent increase in global CO₂ emissions. This shows that the energy transition is not happening fast enough. While the share of renewables in energy production has risen, global consumption of coal remains essentially unchanged, and absolute levels of oil and gas consumption continue to rise. Without a significant step up in the use of cleaner sources of energy and much faster energy efficiency gains, global CO₂ emissions are likely to continue to rise.

Emissions and climate change

The Intergovernmental Panel on Climate Change (IPCC) assesses that human activities, such as GHG emissions and land-cover changes, have already caused approximately 1.0°C of global warming above pre-industrial levels (1850–1900) (IPCC, 2018). Global warming is likely to reach 1.5°C between 2030 and 2052 if it continues to increase at the current rate—about 0.2°C per decade—due to past and ongoing emissions. By 2100, warming...
Climate change already poses serious threats to communities. In 2017, there were 18 million new internal displacements in 135 countries due to weather disasters (Internal Displacement Monitoring Centre, 2018). Estimates of financial losses related to relevant natural events reached $335 billion globally, of which less than half were insured ($140 billion) according to Munich Re’s NatCatSERVICE database. In 2018, while receding from the extreme levels in the previous year, natural catastrophes again reached above-average levels, causing more than 10,000 deaths. However, these figures may underestimate actual losses, as data is not available for many disasters in low-income countries.

Developing economies in the tropics and Southern Hemisphere sub tropics are projected to experience the largest economic losses due to climate change. Small island developing States (SIDS) and least developed countries (LDCs) are among those facing the highest risks of adverse consequences from climate change, as they are exposed to multiple interrelated climate risks. For example, drought is found to significantly increase the likelihood of sustained conflict, particularly for vulnerable countries or groups dependent on agriculture. Additionally, many SIDS and LDCs derive a substantial proportion of national income (more than 15 per cent of GDP) and foreign exchange from tourism, which is threatened by climatic change.

**Climate change and policy**

Dramatic economic and technological transformations are required in order to deal with the climate challenge at hand. This includes, in particular, the accelerated decoupling of economic growth from energy demand and CO₂ emissions. Central for achieving this is internalizing the costs of the negative externalities caused by CO₂ emissions into economic decision-making. This can be achieved through tools such as carbon pricing measures, which in turn can take the form of an emissions tax or an emissions rights trading mechanism. Carbon pricing can serve as an incentive for low-carbon technology innovation. It can also generate an additional source of government revenue, which could be redistributed in the form of social transfers to ease the transition to the low-carbon economy or used to subsidize the development of low-emissions technology and infrastructure. Carbon pricing would also incentivize deployment of carbon removal practices such as natural climate solutions (reforestation, land-use change and other ecosystem-based approaches). These measures could also accelerate efforts towards economic diversification in countries that remain highly reliant on fossil-fuel production.

**Developed economies**

*United States: GDP growth to moderate as fiscal stimulus wanes, confidence levels drop, and capacity constraints build*

The United States economy is estimated to have expanded by a buoyant 2.8 per cent in 2018. The impact of ongoing trade disputes was offset by major fiscal stimulus measures, including a two-percentage-point drop in income tax rates, a steep decline in the corporate tax rate and a rise in federal government consumption spending, especially on defence. Economic confidence and sentiment indicators in the United States rose towards historical highs in 2018, despite the wide range of tariff hikes and the build-up of trade tensions that intensified over the course of the year. However, confidence levels dropped sharply in January 2019, largely in response to the federal government shutdown which started on 21 December 2018 and ended on 25 January 2019—the longest in history. The shutdown impacted 800,000 federal employees, or 0.5 per cent of the national workforce.

Firms in the United States are facing capacity constraints, which will also restrain growth in 2019. Internal freight transportation costs have risen sharply, reflecting labour shortages in the trucking sector and capacity limits in rail transport. The unemployment rate is at its lowest level since 1969, and the ratio of job seekers to job openings is also at historical lows. GDP growth is expected to slow to 2.5 per cent in 2019 and will revert towards 2 per cent in 2020, as the temporary impact of fiscal stimulus measures dissipates. Downside risks to this forecast include a further rise in import tariffs and a failure of confidence to rebound even after the federal government has been restored to full operation.

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Japan: Economy is at capacity despite a slower expansion

In Japan, real GDP growth slowed to 1.0 per cent in 2018 from 1.7 per cent in 2017. Rising corporate profits have contributed to robust growth in corporate capital investments, particularly in R&D. Solid growth of the world economy and a stable exchange rate resulted in resilient growth in external demand. However, a rapid decline in private housing investments has weighed on aggregate investment. Private consumption growth has decelerated as consumer confidence weakened over the year. Despite continued tight labour markets, real wage growth remains stubbornly weak.

Europe: Robust growth ahead, but risks are shifting

Europe will continue to see robust growth of 2.0 per cent in both 2019 and 2020. The main drivers of this performance remain intact, notably solid household consumption propelled by lower unemployment, rising wages and the continued accommodative monetary policy stance. On the business side, companies, especially in the construction sector, also continue to benefit from the expansionary monetary policy stance. However, the risk profile of the outlook has markedly changed for a number of reasons. Firstly, numerous countries in the region find themselves on a decelerating growth trend, which is one symptom of the uncertainty created by the increase in global trade tensions. Second, the European Central Bank (ECB) faces the challenge of exiting its accommodative policy stance, which holds the potential for major ramifications along the way, such as heightened financial market volatility. In the area of fiscal policy, the euro area will be faced with the unresolved problem of how to achieve and maintain a common policy stance in the absence, at least so far, of a more institutionalized policy framework. Uncertainty over the credibility of the European Union’s (EU) fiscal framework has the potential to lead to sharp financial market reactions. Finally, the uncertainty created by Brexit has already led to increased tangible economic consequences, such as companies moving assets or diverting investment from the United Kingdom to the EU. In the case of a disorderly exit from the EU, the British economy runs the risk of even more domestic disruptions because of the lack of a broad legal framework for its future trade relations with the EU, while the European financial sector could face severe disruption.

Economies in transition

CIS: A mild growth slowdown in the CIS is possible

Most economies of the Commonwealth of Independent States (CIS) saw favourable economic outcomes in 2018, with accelerating growth and slowing inflation, as external conditions were generally supportive. The recovery in the Russian Federation has supported activity across the region via trade and remittance channels. However, the dynamics in the terms of trade are likely to be less favourable in 2019. Aggregate CIS growth may decelerate modestly in 2019, as the strong expansion recorded by some of the smaller economies in 2018 may not be sustainable, fiscal policies are growth-neutral at best and monetary tightening is expected in several countries. The Russian economy is expected to remain on a low-growth trajectory, facing constraints such as insufficient business lending; weak investment; banking sector vulnerabilities and moderately conservative fiscal policy. Lifting the value added tax rate in January 2019 may add to inflationary pressures and curb consumer spending. Building-up protective buffers remains a priority, as international sanctions remain a source of uncertainty.

Among the CIS energy importers, the economy of Ukraine expanded by over 3 per cent in 2018. Growth may slightly weaken in 2019; further progress is hampered by noticeable emigration. In Central Asia, growth was robust in Tajikistan, thanks to larger aluminium and gold exports and Chinese investment in metals processing. A series of economic reforms in Uzbekistan attracted foreign investment and spurred interregional trade. Growth in these countries may slightly decelerate in 2019 if higher inflation erodes purchasing power.

The Central Asian region should benefit from the implementation of the Belt and Road Initiative, through infrastructure upgrades, improved connections with China and Europe, and better market access. Aggregate GDP of the CIS and Georgia is expected to increase by 2.0 per cent in 2019 and 2.5 per cent in 2020.

South-Eastern Europe saw faster economic growth in 2018, reflecting robust consumption and investment, amid a favourable external environment. Serbia, the largest economy, bounced back strongly, bolstered by the agricultural and construction sectors, amid double-digit growth in investment. Regional GDP is expected to expand by 3.7 per cent in both 2019 and 2020, supported mostly by investment and exports. Stronger growth is needed to address the region’s multiple challenges, including the need for reindustrialization.

Developing economies

Africa: Improving outlook falls short of needs

Economic growth in Africa is projected to increase to 3.4 per cent in 2019 and 3.7 per cent in 2020. Inflation is estimated to have declined in 2018 and should fall further in 2019, as exchange rates stabilize and agricultural production improves. These seemingly optimistic headline figures, however, mask uneven growth patterns across the continent. Importantly, Africa’s economic growth remains well below what is needed to reach many Sustainable Development Goals and keep pace with rapid population growth. Per capita income growth for the continent has only modestly improved from the contraction in 2016. At 0.6 per cent in 2018 and 0.9 per cent projected in 2019, it remains insufficient to significantly improve living standards. In Southern and Central Africa, GDP per capita declined in 2018, and will likely continue to do so in 2019. Two of Africa’s largest economies, Nigeria and South Africa, struggle to deliver economic progress to their citizens. Only East Africa remained on a steady GDP growth path of 3.3 per cent per capita in 2018. According to WESP 2019 estimates, reducing the level of extreme poverty to below 5 per cent by 2030 will require a combination of double-digit GDP growth and dramatic declines in inequality—well-outside the realms of historical precedence.

Inequality levels remain high. Only a few African economies have achieved significant improvements in income distribution over the last 10–15 years. Out of 25 economies for which data are available, just four West African countries have seen the income share of those in the bottom 20 per cent of income distribution increase by 2 percentage points or more. By contrast, the income share held by...
those in the top 20 per cent of income distribution has risen by at least 2 percentage points in seven economies.

**East Asia: Solid growth outlook but downside risks are high**

The short-term growth outlook for East Asia remains solid, bolstered by resilient domestic demand and accommodative policies. On the external front, however, export growth is likely to slow, amid elevated trade tensions between China and the United States. Against this backdrop, regional GDP growth is projected to moderate from 5.8 per cent in 2018 to 5.6 per cent in 2019 and 5.5 per cent in 2020.

In China, growth is projected to moderate gradually. The imposition of tariffs by the United States will dampen exports, while ongoing economic rebalancing measures will weigh on industrial sectors with excess capacity. Nevertheless, the recent easing of monetary policy and the introduction of several other pro-growth measures will support domestic demand in 2019–20. In several other East Asian economies, including Indonesia, the Republic of Korea, Malaysia, the Philippines and Thailand, domestic demand is expected to remain resilient. Consumer spending will be supported by favourable labour market conditions and increased welfare spending in a few of these countries. In the Philippines and Thailand, public investment growth will be driven by the implementation of large infrastructure projects.

Downside risks to East Asia’s growth outlook have increased considerably. A further intensification of trade frictions will have adverse spillovers on regional growth through trade, investment, and financial channels. An abrupt tightening of monetary policy in the United States may trigger large capital outflows from the region, posing a risk to financial stability. On the domestic front, financial sector vulnerabilities, particularly high corporate and household debt, will continue to weigh on investment prospects in several countries.

**South Asia: Economic outlook remains favourable, but some countries are facing significant turbulences**

The regional outlook for South Asia is moderately positive. Regional GDP is expected to expand by 5.4 per cent in 2019 and 5.9 per cent in 2020, after an estimated expansion of 5.6 per cent in 2018. However, the outlook is highly divergent across countries. Economic growth in a few countries, including Bangladesh, Bhutan and India, is projected to remain robust in the near term. In contrast, the Islamic Republic of Iran is entering into a recession, while Pakistan’s economy is slowing visibly. Downside risks have increased across the region. On the domestic side, political uncertainties, setbacks to the reforms and security problems, may affect investment prospects. This is a crucial issue as the region needs to tackle infrastructure bottlenecks to promote productivity growth, encourage further poverty reductions and adjust to climate change. On the external side, an abrupt tightening of global financial conditions, coupled with a further escalation of ongoing trade disputes, could expose vulnerabilities associated with rising fiscal and current account deficits and elevated levels of debt.

Beyond the short-term outlook, South Asia also needs to tackle several structural challenges that constrain its medium-term prospects. A key issue is to strengthen its international competitiveness, as the region is lagging in attracting foreign investments, penetrating new markets and diversifying and upgrading its export products. The expansion of technological capabilities—as reflected in R&D investments and innovation activities—has also been disappointing. Given limited trade openness and regional integration, South Asia has a vast potential to gain market share in foreign markets and to participate more in global value chains.

**Western Asia: Gradual recovery as oil markets improve**

The Western Asian economies saw a gradual recovery in economic growth in 2018 as the higher oil price positively impacted the region’s major crude oil producers. However, the high reliance on hydrocarbon exports and geopolitical tensions continue to weigh heavily on the region’s growth prospects.

Higher average oil prices in 2018 not only contributed to fiscal balance improvements but also positively influenced economic sentiment in the region’s major crude oil producers, namely, the member countries of the Cooperation Council for the Arab States of the Gulf (GCC): Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. On the other hand, growth in the energy-importing countries in the region—Jordan, Lebanon, and Turkey—has been mostly subdued, partly because of deteriorating terms of trade. Geopolitical uncertainty and high levels of public debt have also negatively impacted these countries.

**Latin America and the Caribbean: Growth is projected to gradually pick up, but major downside risks remain**

Amid a challenging external environment, the region is projected to see a modest pickup in growth in 2019–20. This follows a sluggish performance in 2018, when weakness in several large economies—including Argentina, Brazil and the Bolivarian Republic of Venezuela—weighed heavily on average growth. Aggregate GDP is forecast to expand by 1.7 per cent in 2019 and 2.3 per cent in 2020, up from an estimated 1.0 per cent in 2018. The recovery will likely be driven by strengthening activity in South America, with economic conditions in Argentina and Brazil expected to improve gradually. Mexico, Central America and the Caribbean will likely see steady but modest average growth, as economic activity is often held back by political uncertainty and structural impediments.

In per capita terms, the region’s annual GDP stagnated in 2018 and has not grown since 2013. This underscores the difficulty the region faces in returning to a robust growth path following the 2014–16 commodity price collapse. While the poor aggregate growth performance reflects a high degree of vulnerability to external and domestic shocks in parts of the region, it is also indicative of a long-standing and deep-rooted weakness in productivity.

Amid a relatively bleak economic picture, a positive development has been the mild recovery of aggregate investment in 2018. The improvement has been fairly broad based across countries, supported by low inflation and accommodative monetary policy. Investment and consumption growth are projected to strengthen gradually in 2019 and 2020, but tighter financing conditions and declining commodity prices could act as a brake. The near-term outlook for trade is generally positive, but the ongoing international trade tensions pose a substantial risk as many countries have strong ties with China and the United States. The region’s prospects are hampered by a lack of macroeconomic policy space, with several countries facing fiscal adjustment pressures going forward.