The global economy is set to expand 5.6 percent in 2021—its strongest post-recession pace in 80 years. This recovery is uneven and largely reflects sharp rebounds in some major economies—most notably the United States, owing to substantial fiscal support—amid highly unequal vaccine access. In many emerging market and developing economies (EMDEs), elevated COVID-19 caseloads, obstacles to vaccination, and a partial withdrawal of macroeconomic support are offsetting some of the benefits of strengthening external demand and elevated commodity prices. By 2022, global output will remain about 2 percent below pre-pandemic projections, and per capita income losses incurred last year will not be fully unwound in about two-thirds of EMDEs. The global outlook remains subject to significant downside risks, which include the possibility of large COVID-19 waves in the context of new virus variants and financial stress amid high EMDE debt levels. Controlling the pandemic at the global level will require more equitable vaccine distribution, especially for low-income countries. The legacies of the pandemic exacerbate the challenges facing policy makers as they balance the need to support the recovery while safeguarding price stability and fiscal sustainability. As the recovery becomes more entrenched, policy makers also need to continue efforts toward promoting growth-enhancing reforms and steering their economies onto a green, resilient, and inclusive development path.

Summary

Following a 3.5 percent contraction caused by the COVID-19 pandemic in 2020, global economic activity has gained significant momentum; however, it remains well below pre-pandemic projections (figure 1.1.A). Moreover, the recovery is uneven, passing over many poorer countries, and there is considerable uncertainty about its durability.

The ongoing pandemic continues to shape the path for global economic activity, with severe outbreaks continuing to weigh on growth in many countries. The most recent wave of COVID-19 is now centered in some emerging market and developing economies (EMDEs), where more transmissible and virulent strains are spreading and where vaccine access remains limited (figure 1.1.B). Vaccination remains especially feeble in low-income countries (LICs). In contrast, advanced economies have generally seen substantial vaccination progress, which has helped limit the spread of COVID-19.

Amid continued vaccination, economic activity is firming across major advanced economies—most notably in the United States, where the recovery is being powered by substantial fiscal support.

Growth in China remains solid but has moderated as authorities have shifted their focus from buttressing activity to reducing financial stability risks. Many other countries, primarily EMDEs, are experiencing subdued pickups alongside surges of COVID-19 cases, even if recent waves of infections appear to be less disruptive to economic activity than previous ones. Recoveries in fragile and conflict-affected LICs are particularly weak, as the pandemic has exacerbated underlying challenges. Whereas global manufacturing activity has firmed, with industrial production surpassing its pre-pandemic level, services activity—especially travel and tourism—remains soft.

Global financial conditions have tightened somewhat, partly reflecting a rise in U.S. bond yields amid increased inflation pressures. Nevertheless, they remain generally supportive, reflecting continued extraordinary policy accommodation by major central banks. Commodity prices have increased markedly, owing to the improving global outlook as well as commodity-specific supply factors. The recovery in global activity and in commodity prices is contributing to an increase in inflation, especially in some EMDEs that have experienced currency depreciation.

Against this backdrop, global output growth is projected to strengthen to 3.6 percent in 2021—its strongest post-recession pace in 80 years (figure 1.1.C). The recovery is underpinned by steady but highly uneven global vaccination and the associated gradual relaxation of pandemic-control
### TABLE 1.1 Real GDP

(Percent change from previous year)

<table>
<thead>
<tr>
<th>Region</th>
<th>2018</th>
<th>2019</th>
<th>2020e</th>
<th>2021f</th>
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Memorandum items:

**Real GDP**

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<th>2020e</th>
<th>2021f</th>
<th>2022f</th>
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**Commodity prices**

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Percentage point differences from January 2021 projections:

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<tr>
<td>Euro area</td>
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<tr>
<td>Japan</td>
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<td>Middle East and North Africa</td>
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<tr>
<td>Argentina</td>
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1. Headline aggregate growth rates are calculated using GDP weights at average 2010-19 prices and market exchange rates. The aggregate growth rates may differ from the previously published numbers that were calculated using GDP weights at average 2010 prices and market exchange rates.

2. GDP growth rates are on a fiscal year basis. Aggregates that include these countries are calculated using data compiled on a calendar year basis. Pakistan’s growth rates are based on GDP at factor cost. The column labeled 2019 refers to FY2018/19.

3. GDP growth rates are on a fiscal year basis. Aggregates that include these countries are calculated using data compiled on a calendar year basis. The column labeled 2019 refers to FY2018/19.

4. World growth rates are calculated using average 2010-19 purchasing power parity (PPP) weights, which attribute a greater share of global GDP to emerging market and developing economies (EMDEs) than market exchange rates.

5. World trade volume of goods and nonfactor services.

6. Oil price is the simple average of Brent, Dubai, and West Texas Intermediate prices. The non-energy index is the weighted average of 39 commodity prices (7 metals, 5 fertilizers, 27 agricultural commodities). For additional details, please see https://www.worldbank.org/commodities.

Note: e = estimate; f = forecast. World Bank forecasts are frequently updated based on new information. Consequently, projections presented here may differ from those contained in other World Bank documents, even if basic assessments of countries’ prospects do not differ at any given date. Country classifications and lists of EMDEs are presented in table 1.2. BRICS includes: Brazil, the Russian Federation, India, China, and South Africa. Due to lack of reliable data of adequate quality, the World Bank is currently not publishing economic output, income, or growth data for Turkmenistan and República Bolivariana de Venezuela. Turkmenistan and República Bolivariana de Venezuela are excluded from cross-country macroeconomic aggregates.
measures in many countries, as well as rising confidence. A substantial share of this rebound is due to major economies, with many EMDEs lagging behind (figure 1.1.D). The United States and China are each expected to contribute over one-quarter of global growth in 2021, with the U.S. contribution nearly triple its 2015-19 average. Vaccination progress is a key determinant of near-term forecast revisions (figure 1.1.E). Despite the strong pickup, the level of global GDP in 2021 is expected to be 3.2 percent below pre-pandemic projections.

The recovery is envisioned to continue into 2022, with global growth moderating to 4.3 percent. Still, by 2022, global GDP is expected to remain 1.8 percent below pre-pandemic projections. Compared to recoveries from previous global recessions, the current cycle is notably uneven, with per capita GDP in many EMDEs remaining below pre-pandemic peaks for an extended period (figure 1.1.F).

In advanced economies, the rebound is expected to accelerate in the second half of 2021 as a broader set of economies pursue widespread vaccination and gradually reopen, with growth forecast to reach 5.4 percent this year—its fastest pace in nearly five decades. Growth is projected to moderate to 4 percent in 2022, partly as fiscal support in the United States begins to recede absent additional legislation.

Aggregate EMDE growth is forecast to reach 6 percent in 2021, as the effects of the pandemic gradually wane and as EMDEs benefit from elevated commodity prices and improving external demand. Nevertheless, the strength of the rebound this year mainly reflects robust pickups in a few large economies. In many other EMDEs, recoveries are expected to be dampened by elevated COVID-19 caseloads and obstacles to vaccine procurement and uptake, as well as by a partial withdrawal of monetary and, especially, fiscal support (figure 1.2.A). Aggregate EMDE growth is projected to moderate to 4.7 percent next year, owing to the continued unwinding of fiscal support and subdued investment, leaving EMDE output 4.1 percent below pre-pandemic projections in 2022. Among LICs, growth is

![FIGURE 1.1 Global prospects](image)

Global output is rebounding but remains below pre-pandemic projections, with more subdued recoveries in poorer countries. Vaccination has helped limit the spread of the virus, but progress is highly unequal and concentrated in advanced economies. Compared to previous global recoveries, the current cycle is strong but uneven, and primarily reflects rebounds in some major economies. With the pandemic and limited vaccination in many emerging market and developing economies (EMDEs) contributing to downward revisions to growth, per capita income in a majority of EMDEs is expected to remain below pre-pandemic peaks for an extended period.
FIGURE 1.2 Global risks and policy challenges

In many emerging market and developing economies (EMDEs), the recovery will be constrained by elevated COVID-19 caseloads, obstacles to vaccination, and a partial withdrawal of macroeconomic support. In many EMDEs, the pandemic has slowed or reversed progress at per capita income catch-up with advanced economies. Inflation is expected to exceed targets in about half of inflation-targeting EMDEs, which could trigger monetary tightening and potentially result in financial stress. Bolstering a green, resilient, and inclusive recovery will necessitate the efficient use of historic increases in debt, the promotion of investments in education and environmental sustainability, and the reduction of trade costs.

A. Fiscal and monetary policy stance in 2021

B. Per capita income growth relative to advanced economies

C. Forecast for EMDE inflation

D. Inefficiencies in public spending

E. Global greenhouse gas emissions

F. Trade costs and tariff rates

Sources: Comtrade (database); Consensus Economics; ESCAP-World Bank Trade Cost Database; Haver Analytics; International Monetary Fund; World Bank; World Resources Institute.

A. The threshold for fiscal loosening/tightening is a fiscal impulse of +/- 0.5 percentage point of potential GDP. Fiscal impulse is the negative change in the cyclically-adjusted primary balance from the previous year. Monetary policy stance shows whether countries have had net policy rate hikes/cuts this year. Sample includes 30 EMDEs for fiscal balance and 70 EMDEs for monetary policy rate.

B. Relative per capita income growth is computed as a difference in per capita GDP growth between respective EMDE groups and advanced economies. For more information on “Small states,” see: https://www.worldbank.org/en/country/smallstates/overview.

C. Based on median inflation in 125 EMDEs and inflation target in 30 inflation-targeting EMDEs. 2021 EMDE inflation forecast described in chapter 4. Vertical line indicates 16-84 confidence bands.

D. Figure shows median efficiency gap: The difference between a country’s spending efficiency and that of best performers. Yellow whiskers show interquartile ranges. Sample includes 34 advanced economies, 139 EMDEs, and 24 LICs. See figure 1.23 E notes for more detail.

E. F. Data are for 2018.

F. Blue bars show average trade costs expressed as ad valorem (tariff) equivalent of the value of traded goods. Red bars show average tariffs for all products. Trade costs aggregated using bilateral country export shares. Yellow whiskers show interquartile ranges.

Notwithstanding these projected recoveries, the pandemic has had a devastating effect on per capita income growth, poverty, and inequality, which will linger for a protracted period. Although per capita income growth in EMDEs is projected to be 4.9 percent this year, it will be essentially zero in LICs. As a result, per capita income catch-up with advanced economies could slow or even reverse in many poorer countries (figure 1.2.B). Moreover, per capita income losses incurred in 2020 will not be fully unwound by 2022 in about two-thirds of EMDEs, including 75 percent of fragile and conflict-affected LICs. By the end of this year, it is expected that about 100 million people across EMDEs will have fallen back into extreme poverty. The pandemic’s impact on poverty could reverberate for a prolonged period due to its scarring effects on long-term growth prospects. The pandemic has also exacerbated inequality as it has disproportionately affected vulnerable groups—including women, children, and unskilled and informal workers.

Moreover, the global outlook is clouded by uncertainty and subject to various risks (box 1.1). The continued spread of COVID-19 shows that repeated outbreaks are still possible, especially in light of the emergence of new variants that are more virulent, deadly, and resistant to vaccines. Elevated debt levels make the financial system vulnerable to a sudden increase in interest rates, which could stem from a rise in risk aversion, inflation, or expectations of faster monetary tightening. A spike in bankruptcies could damage the banking system, restrict the flow of credit, and trigger credit crunches.

The near- and longer-term consequences of the COVID-19 crisis pose enormous policy challenges. The immediate priority continues to be pandemic control, including overcoming obstacles in procuring and distributing vaccines. International cooperation is needed to help ensure timely and equitable vaccine distribution—
particularly in LICs, where inoculation continues to be very slow. As the pandemic is brought under control, policy actions will also be needed to address its adverse legacies, which will require balancing competing priorities.

In many economies, central banks will need to carefully weigh the continued weakness of domestic demand against near-term inflation pressures. Model-based forecasts and inflation expectations point to an increase in inflation in 2021 that will exceed target ranges in about one-half of inflation-targeting EMDEs (chapter 4; figure 1.2.C). Although this may not warrant an aggressive policy response, additional inflation pressure across EMDEs may risk de-anchoring inflation expectations and could trigger monetary tightening despite subdued recoveries, which in some cases could also result in financial stress.

Similarly, many EMDEs will need to be careful to avoid a premature withdrawal of fiscal support, while still keeping a steady eye on medium-term debt sustainability. Given the historic increase in sovereign debt, it will be essential to improve the efficiency of public spending (figure 1.2.D). Strengthening domestic revenue mobilization and medium-term fiscal frameworks can help widen fiscal space and bolster policy credibility. Global cooperation, including private sector participation, is needed to provide debt relief to the world’s poorest countries and fund the investments needed to boost growth and lower greenhouse gas emissions (figure 1.2.E).

Notwithstanding the expected near-term recovery, EMDE output is likely to remain below its pre-pandemic trend for a prolonged period, as many fundamental drivers of growth have been scarred by the pandemic. A comprehensive set of policies will be required to promote a strong recovery that mitigates inequality and enhances environmental sustainability, ultimately putting economies on a path of green, resilient, and inclusive development (GRID). For example, labor market reforms and improved social safety nets can bolster labor productivity by facilitating the movement of labor toward high-growth sectors while protecting vulnerable groups. Productivity can also be boosted by efforts to increase access to digital connectivity and reduce trade costs, which are particularly elevated in EMDEs (figure 1.2.F). Increasing investments in learning infrastructure and education will also be required to boost human capital and arrest recent declines in associated budgets, while expanding green investment can enhance climate resilience.

Global context

COVID-19 continues to spread, particularly in many emerging market and developing economies (EMDEs) amid unequal vaccine deployment. Although world trade is benefiting from the global recovery, it is being constrained by supply bottlenecks and travel restrictions. Financial conditions, while still benign, have tightened somewhat as global yields have risen due in part to higher inflation expectations. Almost all commodity prices have been boosted by the global recovery, with some prices further lifted by supply factors.

Pandemic developments

The pandemic continues to exact a heavy toll, particularly across EMDEs (figure 1.3.A). Since COVID-19 started to spread, it has infected at least 160 million people and caused more than 3 million deaths. Hundreds of thousands of new cases are being reported every day, and the number of unreported cases is estimated to be substantial, particularly in South Asia (figure 1.3.B; Bhattacharyya et al. 2020). Global outbreaks of the virus have come in several waves, each cresting at a higher daily infection rate than the one before. Recent outbreaks have disproportionately affected India and, to a lesser extent, some other large EMDEs such as Brazil.

Vaccination campaigns are gathering pace in many advanced economies and a number of EMDEs, with about 9 percent of the global population having received at least one vaccine dose. Nevertheless, this average conceals enormous regional and income disparities—especially the paltry rate of vaccination in the poorest countries. Countries that have administered vaccines to a greater share of their population are seeing a far slower accumulation of caseloads than the sizable share of EMDEs that have so far administered
FIGURE 1.3 Pandemic developments

The pandemic has continued to spread worldwide, and particularly in emerging market and developing economies (EMDEs). The number of confirmed cases is lower than the estimated number of actual cases, particularly in South Asia. Countries where vaccination campaigns are proceeding quickly have generally seen new cases of COVID-19 fall to a low level. These are mostly advanced economies, as most EMDEs have so far administered only a limited number of shots, and low-income countries have scarcely begun.

A. Evolution of the pandemic

New daily cases, thousands

- Advanced economies
- EMDEs
- World

B. Confirmed versus estimated COVID-19 cases

Percent of population

Confirmed
Estimated

C. Daily new COVID-19 cases, by vaccination progress

Index, 100 = January 1, 2021

- Above-average vaccination
- Below-average vaccination

D. Distribution of new COVID-19 cases and vaccine doses from mid-April to mid-May

Percent of population

Estimated COVID-19 cases
Vaccine doses (RHS)

Sources: Johns Hopkins University (database); Our World in Data (database); World Bank.

- AEs = advanced economies; EMDEs = emerging market and developing economies; EAP = East Asia and Pacific, ECA = Europe and Central Asia, LAC = Latin America and the Caribbean, MNA = Middle East and North Africa, SAR = South Asia, SSA = Sub-Saharan Africa.
- A. Figure shows the seven-day moving average of daily new COVID-19 cases. Sample includes 36 advanced economies and 147 EMDEs. Last observation is May 25, 2021.
- B. Bars represent the new COVID-19 confirmed cases, whereas the diamonds represent the COVID-19 cases as estimated by the Institute for Health Metrics and Evaluation (IHME). Data retrieved on May 26, 2021. Last observation available taken for both confirmed and estimated cases. Sample includes 36 advanced economies, 7 EAP, 23 ECA, 26 LAC, 19 MNA, 7 SAR, and 41 SSA economies.
- C. Figure shows the seven-day moving average of daily new COVID-19 cases per million people for 36 advanced economies and 147 EMDEs above and below the global average vaccination rate. Last observation is May 25, 2021.
- D. Figure shows the one-month accumulation of COVID-19 cases in AEs and EMDEs over April 17-May 17, 2021, as estimated by the Institute for Health Metrics and Evaluation (IHME), and vaccinations as a share of the population. Sample size includes 36 advanced economies and 120 EMDEs.

New variants that were originally identified in Brazil, India, South Africa, and the United Kingdom are now circulating globally. There is evidence that these new strains may spread more easily and cause more severe disease (Davies et al. 2021). Some of the strains also appear to be resistant to the immune responses triggered by a previous infection or by the current set of vaccines (Wang et al. 2021). All countries remain vulnerable to renewed outbreaks so long as the virus continues to circulate in some areas amid unequal global vaccine coverage (Çakmaklı et al. 2021).

Despite continued waves of infection, the impact of the virus and associated lockdown measures on economic activity appears to be diminishing in most countries. Over time, firms and households have adjusted their behavior to mitigate disruptions and shift activity to less-affected sectors (ECB 2021). In addition, compliance with lockdown measures appears to have waned somewhat over time (Goldstein, Yeyati, and Sartorio 2021).

Global trade

Global trade has continued to rebound; however, the strength of global trade growth is set to be dampened by shifting activity from manufacturing to the low-trade-intensity domestic services sector in countries where COVID-19 caseloads have been declining. The recovery in global trade started earlier and has been stronger than that of other components of global output, as the pandemic’s impact on activities requiring face-to-face contact initially encouraged a rotation in demand toward the consumption of durable goods, which have a high trade intensity (figure 1.4.A).

Manufacturing trade is currently being constrained by supply bottlenecks and strains in global value chains, which were temporarily exacerbated by the blockage of the Suez Canal in March (Ferrantino et al. 2021). Companies have experienced a sharp rise in freight rates and localized shortages of shipping containers (figure 1.4.B). In order to increase resilience and mitigate logistical problems, companies have increased their use of digital technologies and diversified suppliers and production sites (Saurav et al. 2020).
BOX 1.1 What is next? Growth scenarios beyond 2021

Global growth is set to reach 5.6 percent in 2021—the strongest post-recession pace in 80 years. Nonetheless, the recovery is expected to be highly uneven, and there is substantial uncertainty about the strength and durability of this anticipated upturn beyond 2021. This box explores two alternative scenarios. In a “Faltering Recovery” scenario, the global economy slows in response to the possibility of recurring local COVID-19 outbreaks, mounting inflationary pressures, and a sharp tightening of global financial conditions during the next two years. In contrast, in a “Sustained Expansion” scenario, vaccine-driven COVID-19 containment, re-opening, and ambitious reforms catalyze an even stronger response of private activity and potential output, with positive global spillovers. These scenarios illustrate that the current signs of recovery may be fleeting and underscore the need for policy makers in emerging market and developing economies (EMDEs) to take advantage of present opportunities to put in place growth-enhancing reforms.

Introduction

Global economic activity is accelerating as the world emerges from the deepest global recession since World War II (World Bank 2020a). Barring a protracted global resurgence of COVID-19, the baseline outlook described in the main text envisages the strongest global recovery from any of the five global recession in the past 80 years. However, the recovery is remarkably uneven across countries, as it largely reflects sharp rebounds in some major economies, with poorer countries lagging behind. In addition, there is substantial uncertainty around the baseline growth trajectory, especially beyond 2021. The recovery in global activity may not last, as explored in a “Faltering Recovery” scenario. In this case, growth would slow starting in 2022 as recurring COVID-19 flareups would weigh on risk sentiment, while mounting inflation pressures amid elevated macroeconomic vulnerabilities would trigger a sharp tightening of global financial conditions (Reinhart and Reinhart 2020). Alternatively, in a “Sustained Expansion” scenario, the rebound could broaden and become self-sustaining, anchored by improved confidence, an accelerated pace of technological change, and a renewed push for reforms that boost longer-term productivity in EMDEs (World Bank 2021a; Kose and Ohnsorge 2021). The global implications of these scenarios are assessed using a large-scale global semi-structural projection model. 

Baseline scenario

In the baseline scenario, global output is set to bounce back strongly, expanding 5.6 percent this year—the fastest post-recession pace in 80 years—following a 3.5 percent contraction in 2020. Advanced economies are expected to grow 5.4 percent in 2021, with substantial fiscal support and faster-than-expected vaccinations in the United States adding fuel to the rebound. Growth in EMDEs is also projected to strengthen, reaching 6 percent in 2021 on the back of improving external demand and elevated commodity prices. This baseline outlook is predicated on the assumption that widespread vaccination allows advanced economies to achieve effective containment of the pandemic by the end of the year, while many major EMDEs are envisaged to substantially reduce local transmission rates. In contrast, slow progress of vaccination campaigns would allow COVID-19 to disrupt activity to varying degrees in many other EMDEs, including low-income countries.

The surge in growth envisaged for 2021 reflects, to varying degrees, the combination of ongoing macroeconomic policy support and the release of pent-up demand associated with the easing of the pandemic. In response to the COVID-19 shock, central banks have eased monetary policy forcefully, by cutting policy rates and in many cases committing to keeping them low for an extended period, as well as rolling out unconventional policies (figure B1.1.1.A-B). Fiscal authorities also announced a series of large-scale support packages across advanced economies and, to a lesser extent, EMDEs (figure B1.1.1.C). Moreover, the pandemic and associated lockdown measures forced households to reduce spending on services involving personal contact, leading to a sizable accumulation of personal savings, particularly in advanced economies (figure B1.1.1.D).

Although financial conditions remain benign, they have tightened somewhat as firming activity raises the prospect of stronger inflation and a faster withdrawal of supportive monetary policies. The ebbing of the pandemic is also revealing heightened macroeconomic vulnerabilities in many EMDEs—in particular, high debt burdens and sizable current account and fiscal deficits—leaving many

Note: This box was prepared by Justin-Damien Guénette, with contributions from Alain Kabundi and Takefumi Yamazaki.

a. The scenarios were constructed using the Oxford Economics Global Economy Model (Oxford Economics 2020), which includes 81 individual country blocks (35 advanced economies and 46 EMDEs), most of which are available at a quarterly frequency, with behavioral equations governing domestic economic activity, monetary and fiscal policy, global trade, and commodity prices.
Beyond 2021, the baseline forecast anticipates a moderation of the global recovery with a continued divergence between advanced economies and EMDEs. Advanced economies are expected to continue to recover at a healthy pace, buoyed by reopening amid limited projected scarring of potential output (Das and Wingender 2021). Growth in the United States is forecast to remain strong, in part due to the likelihood that the Federal Reserve will keep policy rates near zero through early 2023, in line with market expectations. In doing so, the Federal Reserve is assumed to permit a modest overshoot of inflation above the 2 percent target over the next three years, consistent with its new Average Inflation Targeting
BOX 1.1 What is next? Growth scenarios beyond 2021 (continued)

regime (Brainard 2021). In contrast, the pace of recovery in EMDEs is expected to be subdued and uneven, with growth in 2022 and 2023 averaging 4.5 percent—only modestly above a declining rate of potential output growth (averaging 4 percent over the same period). The factors weighing on EMDE recoveries include a slow pace of vaccination and reopening, the withdrawal of macroeconomic support, the stabilization of commodity prices, and a sluggish rebound in global tourism.

Comparison with recoveries from previous global recessions

The baseline scenario envisages the fastest recovery from any of the five global recessions in the past 80 years, considerably faster than the initial rebound from the global financial crisis (figure B1.1.2.A-B). The recovery in advanced economies is projected to be particularly robust—their 2021 growth is expected to be nearly twice as fast as that after the 2009 recession (figure B1.1.2.C). In contrast, the recovery in EMDEs is expected to be more modest, with growth in 2021 about one fifth slower than after the 2009 recession.

Nevertheless, this global recovery is expected to be markedly less broad-based than previous ones. Only half of all countries are expected to have regained their pre-pandemic per capita income levels in 2022, two years after the global recession (figure B1.1.2.D). In contrast, by 2011, after the 2009 global recession induced by the global financial crisis, two thirds of countries had regained the pre-recession per capital output levels, a similar share of countries as after the average global recession in the 20th century. The weakness of the recovery is concentrated in EMDEs: Over 90 percent of advanced economies are expected to regain their pre-pandemic per capita income levels in 2022, while only about one third of EMDEs are expected to do so over that time (figure B1.1.2.E-F).

Downside scenario: A Faltering Recovery

The global recovery could falter once policy support is withdrawn and pent-up demand is exhausted, similar to the experience following the global recession of 2009 (Kose and Ohnsorge 2021). A lingering pandemic, with new variants causing recurring local resurgences of infections, would leave households and businesses wary of future prospects (Kozlowski 2020; Ilut and Schneider 2012). This would keep savings elevated and limit the scope for further improvement in private consumption and investment.

At the same time, a rapid demand-driven increase in growth in the United States absent large supply-side improvement would generate sustained inflation pressures and potentially cause a de-anchoring of inflation expectations (Tauber and Van Zandweghe 2020). The Federal Reserve could have no choice but to respond by quickly tightening monetary policy, likely triggering a sharp repricing of risk by financial markets, and exacerbating already heightened macroeconomic vulnerabilities. The macroeconomic effects of a sharp tightening of global financial conditions, as well as weaker consumer and business confidence, would compound the expected unwinding of global fiscal support. Growth in advanced economies would slow sharply from 5.4 percent in 2021 to 2.6 percent in 2022 and 1.4 percent in 2023 (figure B1.1.3.A).

The slowdown would also be sharp in EMDEs as negative spillovers via confidence, trade, and commodity price channels would reduce private sector activity. These countries would experience significant capital outflows in response to heightened investor risk aversion, leading to sharp currency depreciations, which in turn would worsen debt burdens and boost inflation. Domestic credit spreads would significantly widen, triggering a notable rise in defaults, especially in those countries with pre-existing balance sheet vulnerabilities (figure B1.1.3.B; Arteta et al.)

b. Under average inflation targeting, the inflation rate is expected to exceed its target during expansions to compensate for below-target inflation during downturns. The modest overshoot in core PCE inflation envisioned by the Federal Reserve in its March 2021 Summary of Economic Projections would bring average core PCE inflation to 1.9 percent over 2020-23 and to 1.6 percent over 2015-23, still below the 2 percent target. Critically, the projection for U.S. inflation assumes that inflation expectations remain anchored and the Phillips Curve—the relationship between inflation and the level of excess demand—is nearly flat (Hazell et al. 2020).

c. The Federal Reserve is assumed to begin raising rates while rapidly tapering its quantitative easing program starting in 2022Q1.

d. In this scenario, financial market volatility would spike in 2022Q1 and 2022Q2, with the VIX experiencing a rise on par with the COVID-19 crisis due in large part to an unexpected acceleration in the unwinding of U.S. monetary policy stimulus in the face of rising inflation expectations. The sharp rise in global risk aversion is assumed to precipitate a persistent downward shift in global confidence starting in early 2022.

e. Major EMDEs are assumed to face significant adverse domestic confidence shocks in addition to negative spillovers from abroad. These shocks are calibrated to broadly match recent episodes of domestic economic weakness such as what occurred during the Taper Tantrum (2013Q2) and what happened during the global financial crisis for certain EMDEs.
Increased debt servicing costs amid heightened rollover risks would force governments in many EMDEs, particularly in countries with limited fiscal space, to cut consumption and delay investment projects. The domestic credit spread is calculated as a difference between the short-term lending rate and the 10-year government bond yield. Credit spreads in advanced economies are endogenously determined, whereas in EMDEs they are set to be consistent with (1) the levels prevailing during the GFC or (2) the period of rising concerns in anticipation of weaker-than-expected global growth and a no-deal Brexit in 2018. The magnitude of the fiscal consolidation shock is calibrated to match recent historical episodes of rapid fiscal consolidation in major EMDEs. The degree of fiscal consolidation varies across major EMDEs, with EMDEs in 2022 and 2023 would be 1.8 and 1.3 percentage point lower, respectively, and the additional slowdown would cut across all EMDE sub-regions. Growth in China would remain resilient, averaging nearly 5 percent in 2022 and 2023 as policy makers would be according to the size of their fiscal sustainability gap based on Kose et al. (2017). The fiscal sustainability gap widened considerably in most EMDEs in 2020.
expected to roll out additional policy support measures to cushion the effect of adverse spillovers. Excluding China, growth in EMDEs would fall more sharply, from 4.4 percent to 1.4 percent in 2022—2.8 percentage points below the baseline scenario—resulting in nearly zero growth in per capita terms in that year. The pace of activity in EMDEs would barely tick up in 2023 and at 2 percent would still be 1.7 percentage points below the baseline forecast.

In sum, this scenario would mean that global growth would slow sharply, by nearly 3 percentage points from 5.6 percent in 2021 to 2.7 percent in 2022, and further to 2.1 percent in 2023 (figure B1.1.3.D). This would leave the recovery from the COVID-19 pandemic roughly similar to the anemic recovery that followed the global financial crisis.
BOX 1.1 What is next? Growth scenarios beyond 2021 (continued)

Upside scenario: A Sustained Expansion

Alternatively, the global recovery could prove more robust and broad-based than expected. For instance, the policy-supported surge in global growth in 2021, coupled with faster and more equitable global vaccination, could catalyze a self-sustaining period of rapid growth in which the private sector becomes a powerful engine of growth starting in 2022. In effect, strong pro-cyclical policy support would trigger a process of “reverse hysteresis” in which a robust cyclical upturn lifts long-run growth prospects (Reifschneider, Wascher, and Wilcox 2013; Coibion, Gorodnichenko, and Ulate 2017).

In particular, this scenario envisions that technological adoption would accelerate, along with rising investment and labor force participation, causing potential output to strengthen. Starting in the first quarter of 2022, total factor productivity growth in advanced economies would accelerate to levels similar to those seen during previous episodes of productivity surges, as corporations deepen their use of digital technologies and work from home policies adopted during the pandemic (figure B1.1.3.E; Barrero, Bloom, and Davis 2021; McKinsey 2020). Knowledge spillovers and faster installation of new productive capital would also raise productivity in other countries. At the same time, this scenario assumes that EMDE policy makers, faced with high levels of sovereign debt and slowing long-run growth prospects, implement growth-enhancing reforms, including reforms to strengthen economic governance, diversify economies reliant on commodities or tourism, and facilitate the reallocation of resources towards more productive activities (World Bank 2021a). This comprehensive package of reforms would raise EMDE potential output growth gradually starting in 2022 (figure B1.1.3.F).

Consumer confidence would surge, anchoring strong private consumption growth as consumers rapidly draw down their savings. At the same time, rising potential output and well-anchored inflation expectations would help keep inflationary pressures in check, allowing advanced economy central banks to keep monetary policy accommodative for a prolonged period. In turn, continued monetary accommodation would support investment and consumption by alleviating debt service burdens and supporting asset prices.

Growth in advanced economies would remain near 5 percent in 2022 before slowing to a still strong 3.1 percent in 2023. The investment- and productivity-driven growth in advanced economy growth would have greater spillovers to EMDEs, boosting export demand while ensuring that global financial conditions remain benign (World Bank 2017). As a result, EMDEs would experience a robust expansion, with growth averaging over 5 percent in 2022 and 2023—0.6 percentage point higher on average than in the baseline scenario. Overall, global growth would be notably stronger, averaging 4.4 percent over 2022-23 compared to 3.7 percent in the baseline scenario (figure B1.1.4.A-C).

Policy implications

COVID-19 continues to spread across the world, making pandemic control the top priority for policy makers. Launching durable economic recoveries will not be possible until containment is achieved through widespread and equitable vaccination efforts. Still, there have been encouraging signs of a solid macroeconomic recovery from the deleterious effects of the pandemic in recent months. A supportive external environment has helped buoy activity: strengthened external demand has boosted exports of raw commodities and traded goods, while still-benign global financial conditions have helped ease the burden of heavy debt loads among many EMDE governments and corporates.

Looking beyond 2021, EMDE policy makers can help realize a Sustained Expansion scenario of the global economy by decisively implementing growth-enhancing reforms. The benefits of the ongoing global trade rebound can be leveraged by reforms that lower trade costs (chapter 3), including streamlining trade processes and customs clearance procedures, lowering tariffs, and implementing policies that support trade infrastructure and services. Ambitious reforms to facilitate the transition of labor and capital to high-growth sectors, strengthen social safety nets, and fund environmentally sustainable investments can help entrench a domestically driven green, resilient, and inclusive recovery.
As highlighted by the Faltering Recovery scenario, however, the favorable external environment may not last, and many EMDEs are vulnerable to a sudden shift in external conditions. This underscores the need for policymakers to take full advantage of the currently favorable external environment to implement reforms that increase the resilience of financial systems and improve fiscal sustainability. On the macroprudential front, steps can include enhancing macroprudential supervision, closely monitoring systemic risks in the financial system, and incentivizing domestic banks to rebuild capital buffers. At the same time, fiscal authorities can address investor concerns about long-run debt sustainability by strengthening fiscal frameworks, enhancing debt transparency, and improving debt management by issuing long-duration debt denominated in local currency. If fiscal revenues surprise temporarily on the upside, these can be used to replenish depleted fiscal buffers or to fund critical investment and development needs. When combined, these policies can go a long way in making economies more resilient to external shocks and less susceptible to episodes of financial stress.

Price pressures associated with supply bottlenecks are likely to abate over time as global growth moderates and shippers expand capacity.

High-frequency data point to a pickup in some components of services trade, such as telecommunications and financial services (figure 1.4.C). Tourism remains depressed, however, even in countries that have not experienced major outbreaks, such as small island economies. International travel is expected to be constrained for some time owing to lingering mobility restrictions and reluctance to travel so long as the virus is not completely under control (figure 1.4.D; UNWTO 2021).

Trade growth is hampered by high trade costs, which remain particularly elevated in EMDEs (chapter 3). Trade costs primarily arise from transportation expenses and cumbersome customs procedures, and are likely to have increased further as a result of protectionist measures, such as tariffs on U.S.-China trade and export controls on food and medical products (WTO 2020). In all, global...
Financial markets

Financial conditions have tightened but remain generally supportive. Global borrowing costs have increased as expectations of stronger future growth and higher inflation have pushed up long-term yields on government bonds. Thus far, these developments have been substantially less disruptive to global and EMDE financial conditions than the 2013 taper tantrum, when expectations of tighter U.S. monetary policy triggered volatility in global financial markets.

Global corporate borrowing costs have also risen, but spreads have been stable and stock market valuations in most regions are still close to multi-year highs. Business bankruptcies, which had been limited considering the depth of the global recession, have picked up in some industries and countries but remain below pre-pandemic levels amid easy access to credit and the extension of some COVID-19 relief measures. The extent of post-pandemic credit losses may be limited by the fact that crisis-hit sectors account for a small share of total non-financial-sector debt (Mojon, Rees, and Schmieder 2021).

EMDE sovereign debt yields have risen slightly more than U.S. borrowing costs, particularly for some more-indebted countries, resulting in modest increases in spreads (figure 1.5.A-B). Portfolio flows to EMDEs have lost momentum (figure 1.5.C). Some EMDEs have experienced currency depreciation, contributing to above-target inflation (figure 1.5.D). As has been the case in the past, currency depreciation has led some EMDE central banks to start removing monetary policy accommodation. Large output gaps in many countries may limit the extent of EMDE policy tightening in the near future.

Remittances to many countries have been resilient. Strong activity in the U.S. construction sector, for example, has supported flows to many countries in Latin America and the Caribbean (LAC). The extent of this resilience may be overstated, however, by mobility constraints that encourage a shift from informal methods of transporting money across borders toward wire transfers, which are more easily measured (Dinarte et al. 2021).
The recovery of foreign direct investment (FDI) flows to EMDEs is largely attributable to investors' optimism about prospects in China and a few large foreign acquisitions in India. FDI flows to other EMDEs remain subdued due to concerns about the course of the pandemic and uncertainty about growth prospects.

**Commodity markets**

Commodity prices have seen a sharp rise in 2021, with many now well above their pre-pandemic levels (figure 1.6A; World Bank 2021b). Oil prices have rallied markedly, averaging $60/bbl in 2021 so far. Prices have been supported by a gradual firming in demand and continued production restraint among OPEC+, even if the group is gradually reducing the extent of its production cuts as the market recovers. However, the pickup in oil prices has been partly dampened by uncertainty regarding the evolution of the pandemic and its potential impact on future oil demand.

Oil prices are projected to average $62/bbl in 2021 and 2022. Oil demand is expected to continue to firm in the second half of 2021 but will not regain its pre-pandemic level until next year, with the shortfall mainly due to subdued jet fuel consumption (IEA 2021). A key risk to the forecast is the speed at which OPEC+ increases production—the group currently has spare production capacity of up to 9 million barrels per day, equivalent to 9 percent of global consumption in 2019 (figure 1.6.B). A further increase in drilling activity among U.S. shale oil producers is also a potential risk to the oil price forecast. In the longer term, the outlook for oil and other energy commodities will be dependent on the pace of transition toward renewable energy sources.

Base metal prices have increased sharply this year, supported by continued strong demand from China as well as recovery in the rest of the world (figure 1.6.C). The forecast for metals prices in 2021 has been revised sharply upwards, and prices are now expected to be 36 percent higher in 2021 on average relative to last year, before falling back in 2022 as some supply constraints ease.

**Agricultural prices**

Agricultural prices have also seen a substantial rise, particularly those of food commodities, and concerns about food insecurity persist in some countries, especially those afflicted by conflict or experiencing adverse weather events. While most global agricultural commodity markets remain well supplied, production growth for the main crops has been below trend for the past few years (figure 1.6.D). Agricultural prices are expected to rise by 16 percent in 2021 before plateauing in 2022.
Major economies: Recent developments and outlook

In advanced economies, progress in containing the pandemic, primarily through a ramping up of vaccinations, is expected to unlock significant pent-up demand, allowing a gradual narrowing of the gap between advanced-economy output and its pre-pandemic trend. The recovery is projected to strengthen first in the United States on the back of rapid vaccination and a new round of fiscal support, followed gradually by other advanced economies. The pronounced recovery in China is expected to moderate as macroeconomic policy support is withdrawn.

Activity among advanced economies has been propelled so far this year by a solid recovery in the United States, partly due to the effects of massive fiscal support. Vaccination campaigns are generally proceeding at a faster pace than envisioned in the January baseline forecast, albeit at varying degrees across countries (figure 1.7.A). Still, most advanced economies have maintained some pandemic control measures to dampen COVID-19 caseloads and guard against possible resurgences.

More generally, advanced economies continue to experience a two-track recovery, with sales and production of goods nearing or exceeding their pre-pandemic levels, while services sectors struggle to overcome headwinds from the pandemic and associated lockdown measures (figure 1.7.B). Although labor markets so far are healing at a faster pace than during the global financial crisis, employment in early 2021 remains well below its pre-pandemic level (figure 1.7.C).

Growth in advanced economies is forecast to reach 5.4 percent in 2021—2.1 percentage points higher than envisioned in January, powered by stronger-than-expected momentum leading into 2021, faster vaccination in several countries, additional U.S. fiscal support, and the release of sizable pent-up demand (figure 1.7.D). U.S. growth is expected to outperform that of other major advanced economies due to its more rapid vaccine rollout and larger fiscal support. After this year’s rebound, growth is expected to moderate but remain robust in 2022 as the removal of pandemic control measures continues.

United States

The U.S. economy is recovering more quickly than its peers from the pandemic shock, supported by greater amounts of fiscal relief. Surging personal income has boosted consumption, which is expected to firm as households reduce their savings rate from historically high levels. The signing of the American Rescue Act in March offered $1.9 trillion in additional fiscal support, bringing the cumulative fiscal relief provided since the beginning of the pandemic to over one-quarter of GDP—a level of support that is unprecedented
in peacetime. Vaccination is proceeding at a robust pace and is set to become widespread by mid-2021.

In all, U.S. growth is projected to reach 6.8 percent in 2021—its fastest pace since 1984—reflecting additional large-scale fiscal relief and the ongoing easing of pandemic restrictions. It is then expected to soften to a still-robust 4.2 percent in 2022 as the fiscal impulse begins to fade.

**Euro area**

A slow and inconsistent vaccine rollout and the need to maintain stringent mobility restrictions in the face of more transmissible variants have constrained the pace of recovery in the first half of the year. The euro area is set to experience a strong recovery in the second half of 2021, alongside the expected acceleration of vaccinations and a relaxation of pandemic restrictions.

Growth in 2021 is projected to reach 4.2 percent—0.6 percentage point above January forecasts—and pick up further to 4.4 percent in 2022 as member countries steadily unwind pandemic controls, enabling the continued release of pent-up demand. Disbursement of Next Generation EU grants and loans will also contribute to the recovery over the forecast horizon, helping to finance various growth-enhancing investments, including green and digital infrastructure.

**Japan**

Following a bounce back in the second half of 2020, Japan’s economy again contracted at the start of 2021, weighed down by targeted lockdown measures amid a resurgence of COVID-19. Activity is expected to recover as sharply diminished COVID-19 caseloads allow for a continued relaxation of lockdown measures and fiscal support increasingly feeds through to domestic activity.

Japanese output is projected to expand 2.9 percent in 2021—0.4 percentage point higher than January forecasts, reflecting firming domestic economic activity alongside robust external demand. The 2021 Tokyo Olympic Games are to be held without foreign spectators, limiting its economic benefits. Growth is envisioned to

**FIGURE 1.7 Advanced economies**

Faster-than-expected vaccination in some advanced economies is strengthening the growth outlook. Retail sales, industrial production, and construction have exceeded or are approaching pre-pandemic levels, while consumption of services remains weak. Despite a nascent rebound, employment remains well below pre-pandemic trends, and below levels at a similar time during the recovery that followed the global financial crisis. The eventual containment of the pandemic is expected to unlock sizable pent-up demand as households spend their excess savings.

- A. Effective daily vaccination rate in major advanced economies
- B. Activity indicators for advanced economies
- C. Employment in advanced economies
- D. Household savings rate in advanced economies

Sources: CPB Netherlands Bureau for Economic Policy Analysis; Guénette and Yamazaki (2021); Haver Analytics; Organisation for Economic Co-operation and Development; Our World in Data (database); Oxford Economics; World Bank.

A. Figure shows the average seven-day moving average of effective daily COVID-19 vaccinations administered per hundred people across the Group of Seven (G7) member countries which include Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. As in Guénette and Yamazaki (2021), effective vaccinations are computed by multiplying the total number of vaccinations by 0.5 to account for multi-dose vaccines and by 0.85 to account for imperfect vaccine effectiveness. Baseline and upside assumption as described in box 1.4 of the January 2021 edition of the Global Economic Prospects report (World Bank 2021a). Last observation is May 31, 2021.

B. For industrial production the weights represent country shares in global nominal, dollar-denominated value added in industry. Aggregates for construction, retail sales and services consumption are calculated using 2020 real U.S. dollar GDP weights at 2010-19 prices and market exchange rates. Sample includes 35 advanced economies for the industrial production, 20 advanced economies for the retail sales, 24 advanced economies for construction, and 14 advanced economies for services consumption. Last observation is March 2021 for retail sales and industrial production, and 2021Q1 for construction and services consumption.

C. Figure shows quarterly employment reindexed to equal 100 at t-1 quarters from the onset of respective shocks. “t-1” refers to 2019Q4 for COVID-19, 2008Q4 for the global financial crisis, and 2019Q4 from January 2020 vintage data for pre-pandemic. COVID-19 data for “t+5” are forecasts. Sample includes 20 advanced economies.

D. Figure shows quarterly ratio of personal savings over personal disposable income. “t-1” refers to 2019Q4 for COVID-19, and 2008Q4 for Global financial crisis. Sample includes 27 advanced economies.
Emerging market and developing economies

Although improving external demand and higher commodity prices are lifting aggregate activity in emerging market and developing economies (EMDEs), the recovery in many of them is being constrained by a severe resurgence of new COVID-19 cases and lagging vaccination, as well as a partial withdrawal of macroeconomic policy support. The pandemic continues to have a particularly dampening effect on tourism-reliant economies and is further exacerbating domestic challenges in low-income countries. In all, the pace of recovery in two-thirds of EMDEs will be insufficient to recoup the per capita income losses caused by the pandemic by 2022, and poverty rates are expected to rise further. The long-term outlook has also deteriorated, owing to the pandemic’s lasting impact on potential output.

Recent developments

Aggregate EMDE output in 2020 fell 1.7 percent, less severe than the expected contraction of 2.3 percent. This reflected better-than-expected activity in some large economies, such as China, as well as among industrial commodity exporters, which benefited from rising energy and metals prices toward the end of last year. The upgrade in 2020 was not broad-based, however. Growth estimates were upgraded in just over half of EMDEs, and outturns for most tourism-reliant economies were weaker than expected (figure 1.9.A-B). Excluding China, the contraction in EMDE output was far more severe, at 4.3 percent, as many countries faced continued headwinds from the pandemic.

Uneven progress at vaccination has allowed for sharp resurgences of COVID-19 cases, often featuring new variants, which have dampened the recovery in many EMDEs (figure 1.10.A). Services activity remains feeble amid ongoing social-distancing and lockdown measures, while depressed international tourism and travel weigh on services trade (figure 1.10.B). Retail sales are stabilizing below pre-pandemic levels, reflecting renewed softness in countries grappling with high

moderate in 2022, to 2.6 percent, held back by lingering weakness in consumption amid subdued wage growth.

China

After expanding 2.3 percent in 2020, output in China has continued to recover, gradually broadening from public investment and exports to domestic consumption (figure 1.8.A). Policy has been shifting away from buttressing activity and toward reducing financial stability risks (figure 1.8.B). Credit support and infrastructure spending, which initially fueled much of the acceleration in investment, have moderated. Debt defaults, including for state-owned enterprises, have continued to rise (World Bank 2021c).

China’s growth is forecast to rebound to 8.5 percent this year, reflecting the release of pent-up demand. This represents an upward revision of 0.6 percentage point, largely owing to expectations of stronger foreign demand. Amid diminishing fiscal and monetary support and tighter property and macroprudential regulations, growth is expected to moderate in 2022, to 5.4 percent.
COVID-19 caseloads (figure 1.10.C). Private investment has been constrained by an earlier collapse in FDI and, in some cases, escalations in political tensions or heightened policy uncertainty (figure 1.10.D; UNCTAD 2021). Nevertheless, the drag from the pandemic has been offset by a continued recovery in industrial production and goods trade, with both surpassing pre-crisis levels faster than in the aftermath of the global financial crisis (figure 1.10.E). Moreover, robust remittance inflows have partly cushioned household incomes amid widespread unemployment (figure 1.10.F; ILO 2021b).

The pace of recovery has diverged across EMDE regions (box 1.2; chapter 2). A strong rebound in goods exports has underpinned activity in East Asia and Pacific (EAP), helping to offset soft domestic demand. Elsewhere, the recovery in goods trade volumes and industrial production has been more tepid. In Europe and Central Asia (ECA) and Latin America and the Caribbean (LAC), high COVID-19 caseloads continue to constrain growth. In the Middle East and North Africa (MENA), OPEC+ oil production restraint is weighing on extractive activity. In Sub-Saharan Africa (SSA), the continuation of COVID-19 restrictions has curbed business activity, with weakness in some industrial sectors compounded by power outages and subdued oil production. In South Asia (SAR), a robust rebound in services has been interrupted by a sharp worsening of COVID-19 cases and a deterioration in mobility indicators.

Following a sharp slowdown in 2020, activity in LICs has recovered somewhat this year, as some countries benefit from improving industrial commodity exports. Nonetheless, growth continues to be dampened by the effects of the pandemic and the very slow pace of vaccinations, which have delayed the relaxation of control measures and inhibited activity that relies on face-to-face interaction (Afghanistan, Guinea, Madagascar; box 1.3). Some fragile and conflict-affected LICs have also had to contend with floods, droughts, locust infestations, and rising insecurity (Central African Republic, Eritrea, Mali, Sudan).

**FIGURE 1.9 Recent developments in emerging market and developing economies**

The collapse in activity in 2020 was shallower than anticipated for a number of emerging market and developing economies (EMDEs), especially industrial commodity exporters. In contrast, growth forecasts for most tourism-reliant economies were downgraded.

The 2021 forecast is 0.8 percentage point higher than earlier projections; however, this mostly reflects sizable upgrades to some large economies, as well as strong momentum from late 2020 (figure 1.11.A-B). In particular, the projection for China’s growth for 2021 has been revised up due to expectations of more robust external demand.

The recovery in aggregate EMDE activity is anticipated to gather further pace in the second half of 2021 as vaccine deployment, while still uneven, gradually proceeds, particularly in large countries. Aggregate EMDE growth is forecast to reach 6 percent in 2021, supported by improving external demand and elevated commodity prices. The 2021 forecast is 0.8 percentage point higher than earlier projections; however, this mostly reflects sizable upgrades to some large economies, as well as strong momentum from late 2020 (figure 1.11.A-B). In particular, the projection for China’s growth for 2021 has been revised up due to expectations of more robust external demand.

The recovery in EMDEs excluding China is projected to be more modest, at 4.4 percent in 2021, with about 40 percent of countries facing downward revisions to growth this year, reflecting...
continued disruptions from the pandemic and the partial removal of monetary and, especially, fiscal support (figure 1.11.C). Although vaccine procurement and distribution are expected to gradually accelerate over the forecast horizon, it will remain uneven in the near term, with bottlenecks in the equitable distribution of vaccines anticipated to weigh on the recovery in many EMDEs (figure 1.11.D-E).

Aggregate EMDE growth is projected to edge down to 4.7 percent in 2022, as macroeconomic support continues to be withdrawn and commodity prices stabilize. Tourism-dependent economies, such as small island countries, are expected to continue to experience the consequences of subdued international travel next year, which will delay the recovery (UNWTO 2021). More generally, the recovery in EMDEs will not be sufficient to recoup earlier losses, with output in 2022 expected to remain 4.1 percent below pre-pandemic projections (figure 1.11.F).

**EMDE long-term outlook**

In the longer term, the EMDE outlook will likely be dampened by the pandemic’s lasting legacies. EMDE potential output—the activity EMDEs can sustain at full capacity and employment—is expected to remain below pre-pandemic projections over the next decade. Major drivers of growth had been projected to lose momentum even before the COVID-19 crisis, and this trend is likely to be exacerbated by the scarring effects of the pandemic (figure 1.12.A; Kilic Celik, Kose, and Ohnsorge 2020; World Bank 2021a). The pandemic is expected to worsen the slowdown in labor productivity growth, as it has damaged the process of both physical and human capital accumulation (Dieppe 2020). It is possible that the pandemic spurs productivity by accelerating technology adoption, innovation, and a shift in activity toward more productive sectors, but this has not yet been observed on a global scale, whereas the damage to investment and human capital is readily apparent (di Mauro and Syverson 2020).

Investment—both public and private—is expected to remain well below pre-pandemic projections for a prolonged period, which will result in a smaller...
capital stock and lower productivity (figure 1.12.B; World Bank 2018a). Impaired corporate productivity and heightened risk aversion will likely impede private investment, whereas the need to unwind fiscal support in some EMDEs will constrain public investment (Caballero and Simsek 2020; Stiglitz 2020; World Bank 2021a). Sizable investment needs of many EMDEs, and particularly LICs, are likely to go unmet, putting development goals further out of reach (World Bank 2021d).

The pandemic has also eroded earlier gains in human capital through its impact on health outcomes, school closures, and prolonged spells of unemployment. Beyond its direct effects on morbidity and mortality, the pandemic has also delayed essential primary health services and increased food insecurity, which could lead to higher maternal and early childhood deaths (Roberton et al. 2020). These effects are also likely to weigh on longer-term productivity, as malnutrition early in life can permanently impair learning abilities. Education has also been disrupted as partial and full school closures continue to interrupt learning continuity, which could worsen learning outcomes (figure 1.12.C). This, combined with the deskilling associated with prolonged unemployment, could lead to sizable future earnings losses.¹ In EMDEs, COVID-19 triggered a fall in working hours equivalent to the loss of roughly 200 million full-time jobs in 2020, with employment not expected to recover to pre-pandemic levels by 2022, particularly in LICs (figure 1.12.D; ILO 2021b; Khamis et al. 2021). The longer unemployment remains high, the more pronounced will be the loss of human capital.

LIC outlook

In LICs, growth is expected to pick up in 2021, reaching 2.9 percent, aided by firming external demand from LICs’ trading partners and elevated

¹See Azevedo et al. (2021); Bundervoet, Davalos, and Garcia (2021); UNESCO (2021); and UNICEF (2021) for a discussion of the impact of COVID-19 on education. See Azevedo et al. (2020) and Faish, Patrinos, and Shafiq (2020) for a discussion of the impact of COVID-19 on future labor earnings through its disruptions to education and employment.

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**FIGURE 1.11 Prospects for growth in emerging market and developing economies**

The forecast for aggregate growth in emerging market and developing economies (EMDEs) for 2021 has been revised up, to 6 percent; however, this mainly reflects substantial upgrades to some large economies as well as strong carryover from growth in late 2020. Firming external demand and higher commodity prices will help offset macroeconomic policy tightening. The recovery will critically depend on the pace of vaccination. For tourism-reliant economies, activity will continue to be constrained by subdued international travel. In all, the pickup in EMDE growth will be insufficient to restore GDP to pre-pandemic projections.

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**Notes:**

EMDEs = emerging market and developing economies; EM7 = Brazil, China, India, Indonesia, Mexico, the Russian Federation, and Turkey. Aggregate growth rates calculated using GDP weights at average 2010-19 prices and market exchange rates. Shaded area indicates forecasts.

A. Forecast revisions to EMDE growth

B. Contributions to 2021 GDP growth

C. Fiscal and monetary policy stance in 2021

D. Vaccine procurement in 2021

E. Forecast revisions to EMDE growth in 2021, by vaccination progress

F. EMDE growth forecasts and gaps with pre-pandemic projections

**Sources:** Duke Global Health Innovation Center (2021); Haver Analytics; International Monetary Fund; Our World in Data (database); World Bank.

**Note:** EMDEs = emerging market and developing economies; EM7 = Brazil, China, India, Indonesia, Mexico, the Russian Federation, and Turkey. Aggregate growth rates calculated using GDP weights at average 2010-19 prices and market exchange rates. Shaded area indicates forecasts.

A. Figure shows contributions to revision of EMDE growth forecasts relative to World Bank (2021a).

B. Sample includes 147 EMDEs.

C. Fiscal loosening/tightening threshold is a fiscal impulse of ±0.5 percentage point of potential GDP. Fiscal impulse is the negative change in the cyclically-adjusted primary balance from the previous year. Monetary policy stance is measured using year-to-date net policy rate hikes/cuts. Sample includes 30 EMDEs for fiscal balance and 70 EMDEs for monetary policy rate.

D. Figure shows the share of confirmed vaccine doses purchased as a share of total population. Sample includes 16 advanced economies and 67 EMDEs. Data are as of May 27, 2021.

E. GDP-weighted forecast revisions above and below the EMDE median share of population that has received at least one COVID-19 vaccine dose as of June 1, 2021. Sample includes 132 EMDEs.

F. GDP levels are relative to World Bank (2020d) forecasts. Sample includes 144 EMDEs, of which 37 are tourism reliant (defined as having average 2015-19 inbound tourism expenditures as a share of GDP above the fourth quartile).
FIGURE 1.12 Long-term outlook in emerging market and developing economies

The pandemic is likely to lead to a lasting reduction in the level of potential output in emerging market and developing economies (EMDEs) and may cause potential growth to lose further momentum over the next decade. Investment will remain well below pre-pandemic projections for a prolonged period, hindering long-term growth. COVID-related school closures are expected to worsen learning outcomes in EMDEs, while prolonged spells of unemployment may lead to a deterioration in skills.

A. Potential growth estimates based on a production function approach as described in Kilic Celik, Kose, and Ohnsorge (2020). 2010-19 aggregates are calculated using 2009 constant GDP-weighted average for 68 EMDEs. Post-COVID prospects assume that investment grows as expected by forecasts from Consensus Economics and secondary attainment rates decline by 2.5 percentage points. Shaded areas indicate forecasts.

B. Figure shows investment levels relative to January 2020 projections in World Bank (2021a). 2010-19-2029 aggregates are calculated using post-COVID projections and 2019 constant GDP-weighted average for 68 EMDEs. Post-COVID prospects assume that investment grows as expected by forecasts from Consensus Economics and secondary attainment rates decline by 2.5 percentage points. Shaded areas indicate forecasts.

C. The learning-poverty rate is the proportion of 10-year-olds unable to read a short, age-appropriate text, as described in Azevedo et al. (2021). Blue bars show the pre-COVID estimations and red horizontal line denotes the expected impact of COVID-19 on learning poverty due to education disruptions. Orange whiskers show the minimum-maximum ranges for each country group.

D. Working-hour losses, deviation from pre-pandemic levels

With economic activity rebounding this year, EMDE per capita income growth is projected to reach 4.9 percent in 2021 and edge down to 3.6 percent next year (figure 1.13.B). Among LICs, however, per capita income growth is expected to be essentially zero this year and a meager 2 percent in 2022. At this rate, per capita income growth in many EMDEs—especially in fragile and conflict-affected LICs—will fall short of the pace of recovery in advanced economies over the next two years. In many economies, this will slow or even reverse the pace of per capita income catch-up (figure 1.13.C). In all, per capita income losses incurred in 2020 will not be fully unwound by 2022 in about two-thirds of EMDEs—including 75 percent of fragile and conflict-affected LICs—as the lingering effects of job losses and heightened uncertainty continue to dampen domestic demand (figure 1.13.D; Furceri et al. 2021; ILO 2021a).

The per capita income losses incurred due to COVID-19 are anticipated to worsen deprivation along multiple dimensions in health, education, and living standards, with large increases in poverty headcounts, particularly in Sub-Saharan Africa and South Asia (figure 1.13.E; Alkire et al. 2020). In all, it is projected that about 100 million people will have fallen back into extreme poverty by the end of this year due to the pandemic, making the Sustainable Development Goals (SDGs) more elusive (World Bank 2020b).

In addition to reversing gains in global poverty reduction for the first time in a generation last commodity prices. Despite this year’s recovery, the pace of expansion will be the slowest of the past two decades excluding 2020 amid a very slow pace of vaccination. Growth is subsequently projected to firm to 4.7 in 2022, as vaccine distribution bolsters activity. In tourism-reliant countries, a wider administration of the vaccine is also envisioned to support the recovery (Madagascar, Uganda; UNWTO 2021; World Bank 2021a). Nevertheless, the level of aggregate LIC output in 2022 will still be 4.9 percent below pre-pandemic projections.

Furthermore, LIC forecasts for this year and next have been downgraded—especially in fragile and conflict-affected countries, where the outlook is particularly dire (figure 1.13.A). For this subset of LICs, growth is expected to average 2.5 percent in 2021-22—0.7 percentage point below previous forecasts, as an improved external context is more than offset by increased debt burdens, policy uncertainty, social unrest, and rising insecurity.

Per capita income growth and poverty

Sources: Azevedo et al. (2021); International Labour Organization (2021b); Kilic Celik, Kose, and Ohnsorge (2020); World Bank.

Note: EMDEs = emerging market and developing economies; LICs = low-income countries; TFP = total factor productivity.
**BOX 1.2 Regional perspectives: Recent developments and outlook**

The recovery in most EMDE regions is expected to be insufficient to reverse the damage from the pandemic. By 2022, output in all regions is expected to remain below pre-pandemic projections, weighed down by the ongoing pandemic and its legacies, which include higher debt loads and damage to many of the drivers of potential output. The recovery in small, tourism-dependent economies is expected to be particularly weak as some travel restrictions will remain in place until the pandemic is brought under control. The pace of vaccine rollout varies across countries, with low-income countries lagging considerably. The recovery is expected to be strongest in East Asia and the Pacific, primarily due to strength in China. In South Asia, India’s recovery is being hampered by the largest outbreak of any country since the beginning of the pandemic. In the Middle East and North Africa and Latin America and the Caribbean, the pace of growth in 2021 is expected to be less than the magnitude of the contraction in 2020, while the tepid recovery in Sub-Saharan Africa will make little progress in reversing the increase in extreme poverty caused by the pandemic. In most regions, risks to the outlook are tilted to the downside. All regions remain vulnerable to renewed outbreaks of COVID-19, which could feature variant strains of the virus; financial stress amplified by elevated debt levels; deeper-than-expected scarring from the pandemic; and rising social unrest, potentially triggered by rising food prices.

**East Asia and Pacific.** Growth in the region is projected to accelerate to 7.7 percent in 2021, largely reflecting a strong rebound in China. Nevertheless, output in two-thirds of the countries in the region will remain below pre-pandemic levels until 2022. The pandemic is expected to dampen potential growth in many economies, especially those that suffered most from extended outbreaks of COVID-19 and the collapse of global tourism and trade. Downside risks to the forecast include the possibility of repeated and large COVID-19 outbreaks amid delayed vaccinations; heightened financial stress amplified by elevated debt levels; and the possibility of more severe and longer-lasting effects from the pandemic, including subdued investment and eroded human capital. Disruptions from natural disasters are a constant source of severe downside risk for many countries, especially island economies. On the upside, risks include accelerated vaccination rollouts and greater-than-expected spillovers from recoveries in the United States and other major economies.

**Europe and Central Asia.** The regional economy is projected to grow 3.9 percent in 2021, with firming external demand and higher industrial commodity prices offsetting the negative impact of recent resurgences in new COVID-19 cases. Regional growth is forecast to remain at 3.9 percent in 2022 as the recovery in domestic demand gains traction. The outlook remains uncertain, however, with uneven vaccine rollouts and the withdrawal of macroeconomic support measures weighing on the regional recovery. Growth could be weaker than projected if the pandemic takes longer than expected to abate, external financing conditions tighten, or geopolitical tensions rise further. Legacies of the pandemic, including slowdowns in physical and human capital accumulation, loom over the medium-term outlook if left unaddressed.

**Latin America and the Caribbean.** Activity is projected to grow 5.2 percent in 2021—a rebound insufficient to return GDP to 2019 levels this year after a historically deep recession in 2020. The rebound will be supported by moderate progress in vaccine rollouts, relaxation of mobility restrictions, and improved external economic conditions. Per capita income losses will still be deep in 2022, particularly for small island economies in the Caribbean. Although spillovers from robust growth and additional fiscal support in the United States through trade and confidence channels are an upside risk to the baseline forecast, the balance of risks is tilted to the downside. Key downside risks include a slower-than-expected COVID-19 vaccine rollout; further surges in new COVID-19 cases, including from variant strains of the virus; adverse market reactions from social unrest or strained fiscal conditions; and disruptions related to social unrest or to climate change and natural disasters.

**Middle East and North Africa.** Regional output is projected to grow by a subdued 2.4 percent in 2021, only half the pace of the recovery following the 2009 global recession. Higher oil prices have bolstered growth prospects in oil exporters, but the improvement has been limited by new virus outbreaks and mixed progress at vaccine rollout. COVID-19 resurgences have also worsened the outlook for oil importers. By 2022, regional activity is expected to remain 6 percent below pre-pandemic projections. Risks to the regional outlook remain predominantly to the downside. Limited vaccine progress suggests that the pandemic may intensify again, new variants may emerge, and mobility restrictions may be reimposed. The region is also exposed to risks from conflict and social unrest, high debt in some economies,
and unfavorable commodity price developments. These risks could interact and further undermine living standards, increase deprivation for vulnerable communities, and heighten food insecurity.

South Asia. Output in the region is expected to expand 6.8 percent in 2021, a pace on par with average growth over the previous decade. Stronger-than-expected momentum at the beginning of the year has been disrupted by a large surge of COVID-19 cases. Despite continued recovery, output in 2022 is forecast to be 9 percent below pre-pandemic projections. Poverty rates have risen, and by the end of this year more than half the new global poor are expected to live in the region. The outlook could be weaker if vaccination does not proceed as quickly as assumed. Financial sector balance sheets are at risk of deteriorating, as policy measures put in place at the peak of the pandemic are scaled back, which could constrain the provision of credit and investment needed to support the recovery.

Sub-Saharan Africa. Regional activity is expected to expand a modest 2.8 percent in 2021 and 3.3 percent next year. Positive spillovers from strengthening global activity, better international control of COVID-19, and strong domestic activity in agricultural commodity exporters are expected to gradually help lift growth. Nonetheless, the recovery is envisioned to remain fragile, given the legacies of the pandemic and the slow pace of vaccinations in the region. In a region where tens of millions more people are estimated to have slipped into extreme poverty because of COVID-19, per capita income growth is set to remain feeble, averaging 0.4 percent a year in 2021-22, reversing only a small part of last year’s loss. Risks to the outlook are tilted to the downside, and include lingering procurement and logistical impediments to vaccinations, further increases in food prices that could worsen food insecurity, rising internal tensions and conflicts, and deeper-than-expected long-term damage from the pandemic.
Global outlook and risks

Global growth is recovering unevenly. The pickup in many emerging market and developing economies (EMDEs) remains constrained by high COVID-19 caseloads and the partial withdrawal of macroeconomic support, while activity in major economies—particularly the United States—is rebounding markedly. Aggregate global activity is not expected to be strong enough to fully recoup last year’s output losses in the near term. New variants of COVID-19 could extend the duration of the pandemic, and a sudden rise in interest rates or an increase in corporate defaults could trigger financial stress, resulting in weaker-than-expected activity. Conversely, global and EMDE growth could be more robust if the virus is controlled more quickly or if spillovers from rapid growth in major economies catalyze a sustained, broad-based global rebound.

Global outlook

The global economy is recovering, and is expected to expand by 5.6 percent in 2021 and 4.3 percent in 2022 (figure 1.14.A). The strength of the near-term recovery is, to a large extent, attributable to a few major economies, such as the United States and China (figure 1.14.B-C). In many other economies, the pickup is projected to be less robust than previously envisioned, partly due to the continued spread of the virus and slow vaccine distribution (figure 1.14.D). On aggregate, the global forecast has been upgraded as a result of the diminishing economic impact of subsequent waves year, COVID-19 is set to cause lasting damage to the living conditions of the most vulnerable populations. In LICs, this compounds the challenges faced by the 112 million people who are already facing food insecurity and the 223 million who are exposed to significant flood risk (figure 1.13.F; Furerer et al. 2020; WFP and FAO 2021; World Bank 2021e). The pandemic is also bound to worsen income and gender inequality given its outsized negative effect on women, children, and unskilled and informal workers, as well as its adverse effects on education, health, and living standards (Bundervoet, Davalos, and Garcia 2021; Lakner et al. 2020; Ohnsorge and Yu 2021).

Sources: Mahler et al. (2021); Rentschler and Salhab (2020); World Bank (2020b).
Note: EMDEs = emerging market and developing economies; LICs = low-income countries; Fragile LICs = fragile and conflict-affected LICs; Other EMDEs = EMDEs that are not low-income countries; SAR = South Asia; SSA = Sub-Saharan Africa. Shaded areas indicate forecasts.
A. Forecast revisions to LIC growth B. Per capita GDP growth

C. Per capita income growth relative to advanced economies D. Share of countries with lower per capita GDP level in 2022 than 2019

E. Increase in poverty headcounts due to the pandemic by end-2021 F. Number of poor exposed to flood risk

Figure 1.13 Poverty and per capita income in emerging market and developing economies

GDP growth forecasts in low-income countries (LICs) have been downgraded for 2021-22; in per capita terms, LIC growth will be essentially zero this year. Per capita income catch-up with advanced economies could slow or even reverse in many emerging market and developing economies (EMDEs). The pandemic has erased at least three years of per capita income gains in about two-thirds of EMDEs, including 75 percent of fragile and conflict-affected LICs. Poverty headcounts are set to rise sharply, especially in Sub-Saharan Africa and South Asia, leaving millions of the world’s poorest even more vulnerable to future shocks, including adverse weather.

Figure 1.13 Poverty and per capita income in emerging market and developing economies
The global economy is recovering. The faster-than-expected rebound is to a large extent attributable to a few major economies, such as the United States and China. In many emerging market and developing economies, growth forecasts have been downgraded and output is projected to remain well below pre-pandemic trends, weighed down by the effects of the pandemic. Although risks to the outlook have become more balanced, downside risks are significant.

Across most EMDEs, however, the recoveries taking place will not be sufficient to erase the damage from the pandemic, whose legacies are expected to weigh on global activity for a protracted period. Many countries will take a prolonged period to regain their pre-COVID-19 levels of activity, and a return to pre-pandemic output trends may become unattainable in the absence of major reform efforts (World Bank 2020a; World Bank 2021a). The erosion of skills from lost education and employment are likely to reduce productivity, as will the smaller stock of physical capital resulting from last year’s sharp decline in investment. Debt burdens and financial vulnerabilities have risen in many parts of the global economy, which will make the recovery susceptible to financial market stress. This is expected to be accompanied by a gradual withdrawal of macroeconomic policy support.

The evolution of the pandemic and the pace of vaccination will be the most crucial factor driving the outlook. The baseline assumes that progress at vaccination will help to effectively contain COVID-19 in advanced economies by the end of the year, with most major EMDEs also making substantial progress at reducing transmission. This would allow most control measures in these economies to be lifted, with a few—such as restrictions on some international travel—being maintained to minimize possible flare-ups linked to new variants of COVID-19. In many other EMDEs, vaccination campaigns will be ongoing throughout the forecast horizon. The virus will
continue to disrupt activity to varying degrees, but growth will still benefit from vaccine deployment as well as spillovers from the rapid recovery in major economies.

Risks to the outlook

Forecasts of the pace of the global recovery are subject to considerable uncertainty, especially given the volatile nature of the pandemic (figure 1.14.F). Positive surprises to growth since the January forecast suggest that risks to the outlook have become more balanced; however, downside risks to the near-term outlook continue to predominate.

On the downside, the pandemic could prove more persistent than expected, a wave of corporate bankruptcies or financial market stress could derail the recovery, and an unequal pickup in growth could exacerbate social unrest in various parts of the world. On the upside, more rapid vaccine production—along with more equitable distribution—could lead to faster-than-expected control of the pandemic; moreover, the current upturn in growth, currently concentrated in some major economies, could lead to sizable spillovers and trigger a broader and stronger global economic recovery.

Downside risks

Continued COVID-19 flare-ups and new variants

COVID-19 caseloads are likely to remain high in many parts of the world, including in EMDEs where vaccination progress has been slow, or LICs where vaccinations have barely begun. Bottlenecks in production, vaccine hoarding by some countries, and logistical impediments could continue to slow the pace of vaccine rollouts, particularly in EMDEs. Within many countries, a substantial share of the population is hesitant about inoculation (figure 1.15.A). The continued circulation of the virus in these places means that countries risk repeatedly cycling between making progress in reducing COVID-19 caseloads and relaxing restrictions, followed by the re-emergence of the virus, triggering new lockdowns and renewed declines in activity. The effectiveness of pandemic control measures is also likely being progressively eroded by a rising degree of “lockdown fatigue” (figure 1.15.B).

In addition, COVID-19 has a demonstrated ability to mutate. The appearance and spread of new variants that are more transmissible or more severe could significantly set back the fight against the virus, as well as the economic recovery. The emergence of new strains that are able to circulate even within vaccinated or previously infected populations could prove especially damaging. The prevalence of virus variants in foreign countries would encourage policy makers to maintain stringent travel restrictions, and further delay the recovery in economies dependent on international tourism.

Financial market stress

Governments and corporations amassed considerable debt as they weathered last year’s global recession (figure 1.16.A-B). This followed a decade of rapidly accumulating debt after the global financial crisis (Kose et al. 2021). Elevated
Recent developments

In 2020, the COVID-19 pandemic pushed growth in low-income countries (LICs) down to 0.7 percent—the slowest pace in 27 years—with per capita income contracting by 2 percent. Activity has since picked up somewhat, aided by stronger activity in major trading partners and higher commodity prices (figure B1.3.1.A-B). Nonetheless, growth continues to be held back by the ongoing pandemic and its legacies. Continued infections have delayed the resumption of activity in some sectors, particularly in those dependent on face-to-face interactions. The pace of vaccination has been extremely slow in LICs, in part due to procurement hurdles and limited financing. As of late May, only about 0.3 percent of the population in LICs has received at least one dose of vaccine—a mere one-tenth of the share of the population vaccinated in EMDEs and just one-hundredth of the share in advanced economies.

Fragile and conflict-affected LICs have been hit the hardest by the pandemic, with GDP falling by an estimated 1.2 percent in 2020 (Afghanistan, Eritrea, Haiti, Liberia, Sudan). In per capita terms, output in these countries contracted by an estimated 3.8 percent last year, setting back per capita income gains by at least a decade (World Bank 2021a). In some countries, the negative effects of the pandemic were exacerbated by severe floods, droughts, locust infestations, and rising insecurity (Afghanistan, Eritrea, Mali, Sudan).

Activity in other LICs also decelerated sharply last year, with GDP growth falling to a two-decade low of 2.7 percent, equivalent to zero per capita income growth. The adverse effects of COVID-19 and related control measures have disrupted exports, impeded consumption and investments, and eroded tourism revenues (Ethiopia, Guinea, Rwanda).

Outlook

Activity in LICs is forecast to grow by 2.9 percent in 2021—the second slowest growth rate of the past 20 years after that of 2020—and by 4.7 percent in 2022 (figure B1.3.2.A; table B1.3.1). The projected rebound hinges on stronger demand from LICs’ trading partners—notably China and the United States—higher commodity prices, and some progress at vaccination in LICs. Nonetheless, growth forecasts in 2021-22 have been downgraded by an average 0.6 percentage point, reflecting further delays in vaccination campaigns; natural disasters such as floods, droughts, and insect infestations; and rising geopolitical risks and conflicts. The group’s output level in 2022 is projected to be 4.9 percent lower than pre-pandemic projections, as the lingering adverse effects of the pandemic weigh on the recovery. The weakness of the rebound implies that most LICs will make little progress toward recovering to pre-pandemic output levels.

Firmer metals and oil prices and strengthening global activity are projected to support growth in industrial commodity-exporting LICs (Central African Republic, Guinea, Tajikistan) to 3.1 percent a year on average in 2021-22. Nevertheless, this pace will be 1.4 percentage point lower than the 2010-19 average and 1.1 percentage points below previous projections, as policy uncertainty, social tensions, and insecurity are expected to delay some investments in new production capacity in the extractive sector (Chad, Mozambique, Niger). In commodity importers (Eritrea, Haiti), activity is expected to stall, with
**BOX 1.3 Recent developments and outlook for low-income countries (continued)**

**FIGURE B1.3.1 Recent developments**

Despite improved external conditions and relatively low infection rates, the pandemic and the very slow pace of vaccination have inhibited the resumption of activity in low-income countries (LICs). Sovereign borrowing costs have increased in some LICs.

### A. GDP growth in major LIC trading partners

- **Quarterly GDP growth**
- **GDP growth in 2021**
- **Share of LIC exports (RHS)**

### B. COVID-19 infections in LICs

- **New cases (per 100,000)**
- **Total cases (per 100,000)**

### C. Sovereign borrowing costs in selected LICs

**Sources:** Bloomberg; Haver Analytics; International Monetary Fund; Johns Hopkins University (database); World Bank

**Note:** EMDEs = emerging market and developing economies; Fragile LICs = fragile and conflict-affected LICs; LICs = low-income countries.

*A. “Share of LIC exports” reflects goods exports.*

*B. Shows the seven-day moving average of daily new infections in Fragile LICs and LICs. Seven-day moving average of total number of infections in EMDEs and LICs are on the right-hand side axis. Sample includes 147 EMDEs, 28 LICs, and 19 Fragile LICs. Last observation is May 25, 2021.*

*C. Data for Ethiopia, Mozambique, and Rwanda reflect the yields on 2024, 2031, and 2023 Eurobonds, respectively. Last observation is May 26, 2021.*

Essentially zero growth this year followed by 2.4 percent growth in 2022.

In fragile and conflict-affected LICs (Afghanistan, Eritrea, Sudan), the recovery is also expected to be subdued, with GDP growth reaching 1.7 percent in 2021 and firming to 3.4 percent in 2022. For this subset of LICs, the growth forecasts for 2021-22 will be 1.1 percentage point below the 2010-19 average and 0.7 percentage point lower than January forecasts. Persistently weak growth reflects the ongoing effects of COVID-19 compounded by the limited administrative capacity of some governments, the high prevalence of extreme poverty, and exposure to frequent natural disasters and violence (Corral et al. 2020).

In other LICs, the recovery is projected to be less subdued, with growth averaging 5 percent a year in 2021-22—still 0.4 percentage point below previous projections. Activity in Ethiopia, the largest LIC, is forecast to expand by 4.2 percent a year in the near term amid geopolitical tensions. In some countries, more stable political and business environments are expected to support growth, including by boosting private sector investment and reinvigorating entrepreneurship (Rwanda, Togo).

Per capita GDP growth in LICs is expected to tick up modestly, averaging 1 percent a year in 2021-22, after falling by 2 percent last year (figure B1.3.2.B). As a result of limited gains in per capita incomes, many of the tens of millions of people projected to fall into extreme poverty due to the pandemic will struggle to escape, as per capita incomes in 2022 will be marginally lower, by 0.1 percent, than in 2019 (figure B1.3.2.C; World Bank 2020b). Among LICs affected by fragility, conflict, and violence—which already have a higher incidence of extreme poverty—per capita income growth is forecast to contract by 0.2 percent a year, on average, in 2021-22. In about three-fifths of LICs and three-quarters of fragile and conflict-affected LICs, last year’s per capita income losses will not be fully recouped by 2022. The weak recovery is also unlikely to reverse the increase in inequality caused by the outsized negative effects of the pandemic on women, children, and unskilled and informal workers (IMF 2021a).

After a steep increase last year, government debt in LICs is projected to stabilize at 65 percent of GDP by 2022. As the pandemic recedes and economic activity picks up, a gradual unwinding of fiscal support could help slow
somewhat the build-up of government debt in some LICs (The Gambia, Togo).

Risks

Downside risks to the outlook predominate. More contagious variants of COVID-19 could spread to populous LICs and weaken the recovery if not quickly contained (Democratic Republic of Congo, Ethiopia, Uganda). Chronic impediments to vaccine delivery and administration, alongside vaccine hesitancy could put widescale vaccination out of reach for some time. The COVAX facility could fail to receive adequate multilateral and bilateral financial and logistical support, causing further delays in LIC vaccination campaigns, with particularly outsized negative effects in tourism-reliant countries (Ethiopia, Madagascar, Uganda)\(^a\).

The pandemic has caused a deterioration in public finances and sharply increased debt service costs in some LICs, especially those that were already in financial stress (figure B1.3.3.A). Heightened sovereign debt sustainability concerns may further raise borrowing costs, increase debt burdens, exacerbate debt distress, and dampen the recovery in some countries (World Bank 2020c).

Oil-exporting LICs are set to benefit from stronger oil prices (Chad, South Sudan). However, higher oil prices could prompt a rise in global oil supply—in particular from U.S. shale fields. The current OPEC+ production cut agreement could fail, possibly leading to a sharp increase in supply and weaker oil prices. If this happens, oil-exporting LICs could experience revenue shortfalls and, as a result, be forced to decide between growth-damaging fiscal consolidation and risking financial stress. Lower-than-assumed oil prices would, however, benefit net oil importers.

Food insecurity continues to weigh on the livelihoods of more than 112 million people in LICs (figure B1.3.3.B; FSIN 2021). Currency depreciations, localized supply disruptions, and natural disasters have pushed food price inflation well above pre-pandemic rates in some LICs, and many households are set to suffer real income losses and lower food consumption (Afghanistan, Ethiopia, 

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\(^a\) The COVAX facility is a multilateral initiative that aims at assisting the poorest countries to secure equitable access to about 2 billion vaccine doses by the end of 2021. It provides demand guarantees to vaccine manufacturers to encourage them to expand and accelerate the production of vaccine doses.
**BOX 1.3 Recent developments and outlook for low-income countries (continued)**

**TABLE B1.3.1 Low-income country forecasts**

(Real GDP growth at market prices in percent, unless indicated otherwise)

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Note: e = estimate; f = forecast. World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries’ prospects do not significantly differ at any given moment in time.

a. The Democratic People’s Republic of Korea, Somalia, the Syrian Arab Republic, and the Republic of Yemen are not forecast due to data limitations.
b. Aggregate growth rates are calculated using GDP weights at average 2010-19 prices and market exchange rates.
c. GDP growth based on fiscal year data. For South Sudan, the year 2019 refers to FY2018/19.
d. For Togo, growth figures in 2018 and 2019 are based on pre-2020 rebasing GDP estimates.

Mozambique, Rwanda, Tajikistan, chapter 4). Absent additional aid, acute hunger and poverty could soar in countries where the prevalence of extreme poverty is already highest, particularly in those grappling with fragility or conflict situations (UNFAO 2021; World Bank 2021e).

Rising violence against civilians threatens growth prospects in some LICs (figure B1.3.3.C). Insurgencies in the Sahel and political tensions in some countries are taking a heavy humanitarian and economic toll on the most vulnerable populations and exacerbating the negative effects of COVID-19.
especially for those countries that have borrowed heavily in foreign currency, that have substantial upcoming redemptions that need to be rolled over, or that have limited foreign exchange reserves, a sustained pickup in inflation would drive further depreciation, exacerbating currency mismatches, and could result in significant outflows of the volatile portfolio flows that are often used to finance current account deficits (Chapter 4). As has been shown in the past, several vulnerabilities in a country can interact to become severe conglomerate crises, and financing difficulties in one country can cause contagion and trigger broad-based financial crises as investors move capital to safe havens (Devereux and Changhua 2020; Reinhart 2021).

Corporate defaults and deleveraging

In many countries, government support programs were successful in limiting the number of companies that failed during the pandemic. A combination of loan guarantees, payment moratoria, monetary easing, and regulatory
forbearance helped maintain liquidity during a period of plunging sales revenues. It also helped lower the number of bankruptcies below those seen during the global financial crisis (figure 1.17.A; Banerjee, Noss, and Vidal Pastor 2021). As these programs are gradually withdrawn, major corporate solvency crises may emerge, especially in those countries where corporate indebtedness is high and weak recoveries reduce profits, or in those with a high proportion of “zombie” firms dependent on low interest rates (Helmersson et al. 2021).

The global banking system entered the pandemic with substantial capital buffers and has proved resilient during the downturn (IMF 2021b). Many indicators of banking health appear robust—for example, the average share of non-performing loans (NPLs) in many countries’ financial systems has declined during the pandemic (figure 1.17.B). Nonetheless, the apparent strength of many banks may be overstated by pandemic-related relaxations of the regulations surrounding loan classification and provisioning (Alonso Gispert et al. 2020). If bankruptcies rise as support policies are phased out, bank balance sheets could quickly become impaired.

A wave of corporate defaults could trigger banking crises, particularly in countries where recapitalization by the government may not be possible because of already-strained fiscal positions. The interlinkages between public and private balance sheets have tightened in many countries as a result of pandemic relief programs, suggesting that banking crises could also be triggered by sovereign weakness. Even if a full-fledged banking crisis is averted, a persistently weak banking system would reduce credit availability, hindering the ability of firms to finance investment once demand picks up. This would be particularly damaging for small- and medium-sized enterprises, which have been disproportionately damaged by the pandemic and rely heavily on the banking system for credit (Diez et al. 2021; Gourinchas et al. 2021). At the aggregate level, attempts at deleveraging can fail to gain traction as efforts to reduce debt are hampered by weak nominal output growth.

**FIGURE 1.16 Downside risk: Financial market stress**

Governments and corporations amassed considerable debt as they weathered last year’s global recession. In the past, large currency depreciation in emerging market and developing economies (EMDEs) has often led central banks to tighten monetary policy, regardless of the strength of the domestic economy. Currency depreciation and the recent rise in energy and input prices could also de-anchor inflation expectations and trigger destabilizing capital outflows in some countries.

A.B. Figures show the cumulative change in debt since the start of the episode, which is 2008Q3 for GFC and 2020Q1 for COVID-19. Sample includes 25 EMDEs, excluding China.

C. Bars show estimated impact of a 10-percent monthly currency depreciation at t = 0 on EMDE policy rates at t+1, t+3, and t+6 months horizons using a local projections model. Orange whiskers indicate 90 percent confidence intervals. Sample includes 33 EMDEs with floating or free-floating exchange rates.

D. Figure shows the composite Purchasing Managers’ Index (PMI) for input and output prices. PMI readings above 50 indicate expansion in economic activity; readings below 50 indicate contraction. Last observation is April 2021.

**Region-specific downside risks**

The global recession impacted some regions and groups harder than others, and the global recovery is leaving many behind. Weak and unequal growth or policy missteps could worsen the social discontent already seen in some countries in regions such as EAP, ECA, and LAC. Some governments may address fiscal deficits through austerity measures that reduce support to vulnerable groups. Climate-related events can cause large economic losses (Fernando, Liu, and
Many countries are experiencing a sharp rise in food prices, which account for about one-third of the consumption basket in EMDEs, on average, and close to half in some countries. A sustained rise in food prices would exacerbate food insecurity, erode real incomes, and potentially contribute to more widespread malnutrition. Oil supplies may increase suddenly if OPEC+ changes course, or if U.S. shale operators ramp up production. This could lead to a sharp fall in oil prices that could cause difficulties in many oil-exporting countries, including those concentrated in MENA and SSA.

**Upside risks**

Rapid end of the pandemic at the global level

Vaccine rollouts at the global level, while unequal, have proceeded somewhat more quickly than anticipated at the beginning of the year (figure 1.18.A). At least 10 separate manufacturers have set production targets of more than 1 billion vaccines each by the end of the year (Wouters et al. 2021). If vaccine-makers’ projections prove accurate, the world will have almost 13 billion doses available by December, more than enough to fully inoculate about 80 percent of the world’s population (figure 1.18.B; Duke Global Health Innovation Center 2021). Temporary waivers on intellectual property protections for COVID-19 vaccines could allow for additional manufacturers to enter the market, further accelerating production.

As domestic supplies exceed demand in countries where vaccination is proceeding rapidly, some excess vaccines will be channeled abroad, accelerating progress in lagging countries. Unless distribution and demand challenges hinder progress, increased vaccine production could result in more rapid and globally equitable vaccination distribution and remove the need for stringent control measures. Accelerated COVID-19 vaccination is likely to have economic benefits that heavily outweigh its costs (Gagnon, Kamin, and Kearns 2021). A rapid, effective, and global containment of COVID-19 would strengthen the medium-term global recovery and make it subject to fewer setbacks.
Sustained, broad-based global upturn

The global recovery is now being driven by the United States and a few other major economies. It is possible that spillovers from activity in these economies help to undam a large reserve of pent-up demand, bolster confidence, and catalyze a synchronized and self-sustaining boom that pushes global activity above baseline forecasts, even if outbreaks persist in some EMDEs (figure 1.19.A-B; box 1.1).

A stronger, more durable, and more broad-based global upturn would reduce the scarring caused by the pandemic. A more robust labor market would attract a greater share of discouraged workers back to the labor force. Faster growth would propel the recovery in investment above the baseline forecast. The need to meet surging demand could also encourage faster adoption of new technologies, particularly in the services sector as companies invest in the digital remote service practices pioneered during the pandemic (McKinsey Global Institute 2021). Stronger potential output growth would help keep inflation pressures in check and help reduce debt ratios. A more broad-based recovery would also likely be more inclusive, with a greater reach to those vulnerable groups that have been most affected by the crisis, and thus help move a larger number of people out of poverty.

Policy challenges

Globally-coordinated efforts are essential to secure equitable vaccine distribution and far-reaching debt relief, particularly for low-income countries. As the health crisis abates, policy actions will be needed to address the adverse legacies of the pandemic, including high debt and weak productivity growth. This will require a difficult balancing act as policy makers seek to nurture the recovery while safeguarding macroeconomic stability. Policies to facilitate employment in high-growth sectors, protect vulnerable groups, and reduce trade costs—combined with increased investments in education, connectivity, and green infrastructure—will be needed to bolster growth prospects and steer the recovery onto a green, resilient, and inclusive development path.

FIGURE 1.18 Upside risk: Rapid end of the pandemic at the global level

The pace of vaccine rollout at the global level, while highly unequal, has exceeded expectations. Vaccine makers have committed to producing almost 13 billion doses by the end of the year, enough to fully inoculate most of the world if distribution issues can be resolved and vaccine access becomes more equitable.

FIGURE 1.19 Upside risk: Sustained, broad-based global upturn

A stronger, more durable, and more broad-based global upturn would help reduce the scarring caused by the pandemic. Spillovers from faster growth in major economies would increase growth elsewhere.

Sources: Duke Global Health Innovation Center (2021); Guénette and Yamazaki (2021); Our World in Data (database); World Bank.
A. Figure shows the average seven-day moving average of effective daily COVID-19 vaccinations administered per hundred people across the Group of Seven (G7) member countries which include Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States and the Emerging Seven (EM7) member countries including China, India, Brazil, Mexico, the Russian Federation, Indonesia, and Turkey. As in Guénette and Yamazaki (2021), effective vaccinations are computed by multiplying the total number of vaccinations by 0.5 to account for multi-dose vaccines and by 0.85 to account for imperfect vaccine effectiveness. Baseline assumption is for advanced economies and major EMDEs as described in box 1.4 of the January 2021 edition of the Global Economic Prospects report (World Bank 2021a). Last observation is May 25, 2021.

Sources: Oxford Economics; World Bank.
Note: EMDEs = emerging market and developing economies.
A. Figure shows impulse response of growth in EMDEs excluding China after one year to a 1-percentage-point higher growth in major economies.
Key global challenges

Ending the COVID-19 pandemic will require a global deployment of vaccines. Accelerating the pace of vaccinations will require policy makers to bolster public trust in vaccine safety and work with the private sector to improve the production and distribution of vaccines. International support is also critical to hastening global control of the virus by providing vaccines to EMDEs and LICs where availability is limited. Global initiatives, including COVAX, can redistribute excess vaccine doses and ensure more equitable access to vaccine supplies (Gavi 2021). Until widespread vaccination is achieved, growth-friendly control measures—including universal masking, social distancing, and test and trace strategies—are needed to help contain domestic flare-ups, including those resulting from the spread of new virus strains (Prettner et al. 2021).

In addition, health systems must be strengthened to confront the lingering health consequences of the pandemic, including chronic COVID-19 symptoms and delayed treatment of other conditions. Increasing global pandemic preparedness can also help reduce the risk of future global health crises. Moreover, it is essential to avoid the lure of protectionism in favor of a rules-based international trade regime that safeguards global supply chains for vaccines and other essential traded goods.

Sustaining the global recovery and tackling the many legacies from the pandemic will necessitate close cooperation across governments, multilateral organizations, and the private sector. For instance, the collective benefits of exceptional fiscal and monetary policy support measures are more likely to be sustained if their eventual withdrawal is carefully coordinated (Yoshino et al. 2020). International cooperation can play an important role in helping poorer countries address liquidity and solvency issues through interventions that mobilize development finance, as well as spur the design of government credit guarantees, helping to alleviate financing constraints in EMDEs with fragile banking systems. For LICs facing very large debt burdens, far-reaching and globally-coordinated debt relief efforts involving all creditors will be needed to address long-term debt sustainability challenges (Malpass 2021). At the same time, global cooperation can be instrumental in facilitating the transformational investments in agriculture, transportation, and energy systems needed to entrench a green recovery, reduce global emissions, and ultimately tackle the long-term challenge of climate change.

Challenges in advanced economies

Continued support from monetary and fiscal policy will be needed to ensure a durable recovery in the short term. As the pandemic abates, a gradual normalization of macroeconomic policy will be required to achieve price stability and public debt sustainability. Reforms will be also needed to foster green, resilient, and inclusive growth. These include facilitating the reallocation of labor across sectors and harnessing the accelerated pace of technological adoption brought on by the pandemic. They also include expanded green infrastructure and proper carbon tax policy, which would accelerate a low-carbon transition.

Monetary and financial policies

Inflation pressures are appearing earlier than was the case following the global financial crisis, due to an increase in commodity prices and global supply bottlenecks (figure 1.20.A; chapter 4). Still, most advanced economies are in the early stages of recovery and face the prospect of sizable excess supply (figure 1.20.B). A continued high degree of monetary accommodation will therefore be essential to cementing a strong recovery. In the United States, however, the Federal Reserve’s intention to keep policy rates near zero for a prolonged period may be tested by a rapidly narrowing negative output gap and the possibility that additional fiscal support, coupled with continued reopening, leads to unexpectedly strong domestic demand. Effective communication with market participants will continue to be crucial to ensure that the eventual withdrawal of monetary policy support does not trigger undue volatility in financial markets.

In most advanced economies, authorities will need to carefully manage the unwinding of debt and payment moratoria, especially given elevated nonfinancial corporate debt levels (figure 1.20.C).
Although the level of nonperforming bank loans is much lower than it was during the global financial crisis, it will likely rise once forbearance policies are allowed to expire. The risk of insolvency has also increased for small- and medium-sized enterprises with limited means to raise new capital (Gourinchas et al. 2021). Therefore, it would be important to proactively improve a menu of policies to safeguard the health of the banking system, including debt restructuring, asset separation, and recapitalization that could be used to facilitate an early resolution of corporate and household insolvencies (Beck, Carletti, and Bruno 2021; Boot et al. 2021; Díez et al. 2021).

**Fiscal policy**

The historically sharp and ongoing rise of sovereign debt levels highlights the need to use fiscal support wisely and efficiently (figure 1.20.D). Providing continued support to the nascent recovery remains the near-term priority of advanced-economy fiscal authorities, although at this stage in the crisis fiscal support can be more narrowly targeted. For example, focusing support on hard-hit vulnerable populations, such as the unemployed and lower-income families with children, would have a greater macroeconomic impact given their higher marginal propensities to consume (Klein and Smith 2021; Wilson 2020).

In economies already experiencing a rapid recovery, such as the United States, additional fiscal support, over and above historically large increases in spending, would need to be employed efficiently and weighed carefully against its potential consequences for inflation and long-term debt sustainability (figure 1.20.E-F; Furman and Summers 2020). Although the near-term growth impacts of infrastructure investments may be limited, they can be particularly useful in generating long-run economic benefits (Ramey limited, they can be particularly useful in facilitating an early resolution of corporate and household insolvencies (Beck, Carletti, and Bruno 2021; Boot et al. 2021; Díez et al. 2021).

Although record-high public debt and fiscal deficit ratios among advanced economies do not pose an imminent threat given currently low interest rates, there will soon be a need to rebuild fiscal space

**FIGURE 1.20 Monetary, financial, and fiscal policies in advanced economies**

Inflation pressures are appearing earlier than at a similar time during the recovery that followed the global financial crisis. Nonetheless, they may not persist outside of the United States, as most advanced economies face substantial excess supply. Nonfinancial corporate debt levels have risen above their global financial crisis average. Moreover, the historically large increase in sovereign debt levels highlights the need to use fiscal support efficiently.

A. Inflation pressures in advanced economies

B. Output gaps and deviations of output from pre-pandemic projections

C. Nonfinancial corporate leverage

D. Gross government debt to GDP

E. Fiscal support in the United States and euro area

F. General government balance in the United States and euro area

Sources: Congressional Budget Office; Haver Analytics; International Monetary Fund; Oxford Economics; World Bank.

Note: AE = advanced economies; GFC = global financial crisis.

A. Solid lines show 3-month moving average of the Purchasing Managers’ Index (PMI) composite input price index for Developed Markets. PMI readings above (below) 50 indicate expansion (contraction) in economic activity. Dotted lines show median year-over-year core inflation rate for 29 advanced economies. “t” refers to November 2008 for GFC and March 2020 for COVID-19. Last observation is April 2021.

B. Deviation is percent change in real GDP levels between current projections and January 2020 observation is April 2021. C. **“t”** refers to 2009Q4 for COVID-19 and 2009Q3 for global financial crisis.

D. Average of 25 advanced economies. Recent data are estimates by Oxford Economics. Shaded areas are global financial crisis and COVID-19 pandemic. Last observation is 2021Q1.

E. COVID-19 fiscal support is “above the line” measures compiled by the International Monetary Fund. COVID-19 fiscal support in euro area includes measures announced by euro area member countries and the European Commission.

F. Figure shows percent of nominal GDP. Shaded area over 2021-2025 indicates projections from the Congressional Budget Office (for the United States) and the International Monetary Fund (for euro area).
Education systems can also be improved to counter pandemic-related learning losses, particularly in vulnerable populations (Rose et al. 2021).

In contrast to the global financial crisis, productivity and output growth are likely to rebound in the near term, at least temporarily, as pandemic restrictions on activity and mobility are lifted (Bloom et al. 2021). Policy efforts will be needed to sustain this recovery, especially through cementing rapid gains in digitalization. For instance, providing a secure and fast digital communications environment, coupled with regulatory reforms, can harness the flexibility and productivity inherent in allowing workers to work remotely (Barrero, Bloom, and Davis 2021; Morikawa 2021). Behavioral change in favor of digital services and telecommuting stemming from the pandemic may exacerbate inequalities across firms and households. Policies that enhance the accessibility of financial and public services, support small- and medium-sized enterprises, and promote research and development are essential (OECD 2021a).

Fostering green, resilient, and inclusive growth is also a key policy priority. Government authorities can engage the private sector to increase the economy’s resilience to climate change, working together to accelerate a low-carbon transition, strengthen biodiversity, and enhance environmental health (Disparte 2021; OECD 2021b). Implementing carbon taxes can help reduce harmful emissions and better align incentives with economic objectives, while raising the revenues required to fund green investments, strengthen social safety nets, and improve long-run debt sustainability (IMF 2019; OECD 2020).

Challenges in emerging market and developing economies

As the health emergency abates, EMDE policy makers need to cement a durable, resilient, and inclusive recovery while tackling the pandemic’s longer-lasting and harmful legacies. Millions of lives and livelihoods have been lost, progress at poverty reduction has been reversed, and the policy space available to support growth has been eroded. Emerging inflation pressures mean that and ensure medium-term debt sustainability (Bartsch et al. 2020). Achieving these goals will be more likely if early action is taken to establish credible medium-term fiscal plans and develop carefully calibrated consolidation strategies. These efforts can be complemented with comprehensive reform of tax and social security systems (Orszag, Rubin and Stiglitz 2021).

Structural policies

In advanced economies, the pandemic has caused far greater disruption to output and employment in services sectors than the global financial crisis (figure 1.21.A). A comprehensive set of labor market policies can strengthen the recovery and accelerate an appropriate reallocation of labor across sectors. In particular, policies to facilitate employment of displaced workers—notably women and young workers—are crucial given that many of the occupations in the hardest-hit sectors are highly susceptible to automation (figure 1.21.B; Albanesi and Kim 2021; Hallward-Driemeier and Nayyar 2018). Policy makers can consider expanding worker retraining opportunities and increasing social protection funded by a broader and more progressive tax structure (Sedik and Yoo 2021). Education systems can also be improved to counter pandemic-related learning losses, particularly in vulnerable populations (Rose et al. 2021).
some central banks will have to balance the need to support the economic recovery against risks to price stability (chapter 4). The deterioration of fiscal positions and record-high levels of debt in many countries have heightened financial vulnerabilities and may force a premature removal of fiscal support.

These challenges highlight the need to pursue policies that help rebuild fiscal space without unduly weighing on growth. Such policies include efforts to improve spending efficiency and to better target social protection measures. As the recovery gains traction, these policies can be complemented with those that bolster domestic revenue mobilization. Over the longer term, entrenching a green, resilient, and inclusive recovery amid reduced fiscal space will require policies that prioritize raising long-run growth prospects. These include helping workers transition to high-growth sectors while protecting vulnerable groups, raising human capital, increasing access to digital connectivity, reducing trade costs, and spurring green investments.

Policy challenges in China

Although China’s recovery from COVID-19 is becoming more broad-based, the public investment-led support measures to confront the pandemic-induced downturn have disrupted progress at rebalancing aggregate demand toward domestic consumption. Corporate and household debt levels, which were already high before the pandemic, have risen further, eroding previous deleveraging gains and increasing financial stability risks.

As authorities resume de-risking and deleveraging, they may need to avoid premature policy tightening until private domestic demand strengthens further. Improving insolvency and bank resolution frameworks would facilitate an orderly exit of weak or failing corporates and banks and free up resources for more productive activities.

After this year’s cyclical rebound, China’s economy is projected to slow over the medium term, reflecting the legacies of excessive borrowing as well as structural trends, including declining labor supply and softening productivity growth. To bolster potential growth, China needs to pursue structural reforms that boost market-based resource allocation toward more productive activities (World Bank 2020d; World Bank 2021f).

EMDE monetary and financial policies

Average core inflation in EMDEs has ticked up to slightly above pre-pandemic levels, with a more pronounced increase in countries that experienced depreciations (figure 1.22.A-B). Headline inflation has also increased due to rising energy prices and, particularly in LICs, food prices. Model-based forecasts and inflation expectations point to an increase in inflation in 2021 that will exceed target ranges in about one-half of inflation-targeting EMDEs (chapter 4; figure 1.22.C).

EMDEs have generally maintained their expansionary monetary stance, supported by continued benign global financial conditions. Amid some tightening in financial conditions, average EMDE 10-year bond yields have increased by slightly more than those in the United States (BIS 2021). However, further increases in advanced-economy yields may result in larger transmissions into EMDE yields and financial conditions, which could weigh on the recovery.

Some EMDE central banks are already facing difficult policy trade-offs in ensuring that inflation pressures remain contained, particularly after large currency depreciations, in the presence of substantial output gaps. EMDEs with larger current account deficits and higher external debt-to-GDP ratios experienced larger depreciations, on average, over the past year. Countries with weakly-anchored inflation expectations face a higher and more persistent pass-through from currency depreciations to inflation; accordingly, larger increases in interest rates may be required in these economies to prevent a persistent rise in inflation (Ha, Stocker, and Yilmazkuday 2019).

On average, capital adequacy ratios remain high and NPLs low in EMDEs, reflecting forbearance measures, government guarantees, and a delay in loan defaults that has also been typical in previous recessions (World Bank 2021g). Some EMDE banking sectors are likely to face significant challenges as government support measures for
credit provision are withdrawn and regulatory guidance is tightened on loan classifications. Measures to assess credit quality need to be strengthened to identify the scale of potential loan losses and insolvency frameworks improved to maximize recovery rates as government guarantees and forbearance measures are reviewed (figure 1.22.D; World Bank 2021h).

EMDE fiscal policy

EMDE fiscal support packages announced last year were sizable, with discretionary measures averaging 4 percent of GDP. They were also broad based, with nearly all countries easing their fiscal stance. Relative to advanced economies, EMDE fiscal support was largely front-loaded, with announced COVID-19 revenue and spending measures mostly deployed in 2020 (figure 1.23.A; Gaspar et al. 2021). In addition to this discretionary fiscal support, sharp declines in revenues contributed to rapidly widening fiscal deficits in EMDEs, whereas in advanced economies, widening deficits reflected a surge in spending.

This year, many EMDEs, including some large economies, are expected to pivot toward fiscal tightening to improve the sustainability of public finances, despite large spending needs and sizable output losses relative to pre-pandemic projections (figure 1.23.B-C). For about one-third of those EMDEs with fiscal rules, this will be aided by a gradual transition back to rules-based frameworks after invoking escape clauses in response to the pandemic. These efforts notwithstanding, government debt is anticipated to continue to rise over the forecast horizon, which will further limit fiscal space. Moreover, fiscal sustainability gaps are expected to remain negative, even under current benign financing conditions; in this context, a sudden tightening of financing conditions or worse-than-expected growth could result in higher adjustment needs to stabilize government debt.

Policy makers continue to face the challenge of balancing the need to support the incipient recovery with that of ensuring fiscal sustainability and containing vulnerabilities to financial market stress. Although many EMDEs are still able to tap international capital markets, a sudden shift in investor sentiment could result in a jump in borrowing costs, worsen fiscal positions, and increase debt rollover and currency mismatch risks (Blanchard, Felman, and Subramanian 2021; Kalemli-Özcan, Shim, and Liu 2021). To address these challenges, authorities can prioritize and streamline spending, including by targeting social expenditures more effectively.
For smaller EMDEs and LICs, many of which currently face liquidity or solvency issues, international debt relief and financing support have been critical in providing fiscal space. These include the Debt Service Suspension Initiative and the G20 Common Framework, with the latter also helping to facilitate coordination among creditors. Other initiatives, such as the World Bank Group’s Sustainable Development Financing Policy, can help some countries address debt vulnerabilities and achieve more sustainable debt, including through the provision of technical assistance. However, additional resources are likely to be needed, including grants and highly concessional funding, as well as increased private sector participation. Measures to further strengthen the debt restructuring framework could also help increase the efficiency and effectiveness of restructuring in circumstances where it proves necessary (Group of Thirty 2021).

As the pandemic is contained and the recovery firms, governments will need to shore up medium-term fiscal sustainability by realigning expenditures with revenues. This can include measures to improve domestic revenue mobilization, such as broadening revenue bases with new tax instruments to help close sizable gaps with advanced economies (figure 1.23.D; De Mooij et al. 2020; Kose et al. 2021). On the spending side, strengthening the efficiency of public expenditures could help ensure that additional spending yields dividends to growth (figure 1.23.E; Mathai et al. 2020; Schwartz et al. 2020). Such measures would also help restore the fiscal space that is needed to address sizable investment gaps and broaden social safety net coverage, which could build resilience against future shocks. These efforts can be supported by confidence-enhancing measures to strengthen fiscal credibility, such as fortifying medium-term fiscal frameworks, providing clear policy direction, and increasing debt transparency (Reinhart et al. 2021).

The pandemic has also created additional fiscal challenges for EMDEs with less diversified economies, including energy exporters. For these economies, earlier oil price declines and the subsequent need for fiscal adjustment highlight
the urgency of diversifying sources of fiscal revenue (Stocker et al. 2018). Although global oil prices in the near term have been revised up, broadening the fiscal revenue base could help reduce the vulnerability of EMDE energy exporters to adverse external shocks, particularly as other countries shift toward greener energy (figure 1.23.F). These efforts can be further complemented by other reforms that promote diversification, including those that bolster competition and improve the business environment, as well as fiscal measures that reduce costly energy subsidies and strengthen macroeconomic policy frameworks (Wheeler et al. 2020).

**EMDE structural policies**

The pandemic is expected to exacerbate the slowdown in EMDE potential growth that had already been projected over the next decade. The accumulated scars on human capital will be slow to heal, while the pace of accumulation of physical capital is likely to remain subdued for a prolonged period (World Bank 2021a). Productivity may have also been impaired by disruptions to organizational effectiveness, increased transaction costs, and reduced dynamism, even if some firms have taken the opportunity to increase technological adoption (di Mauro and Syverson 2020; Apedo-Amah et al. 2020).

The policy response to the crisis provides an opportunity to bolster a green, resilient, and inclusive recovery that addresses both the scars brought about by COVID-19 and the longer-term challenges of climate change (World Bank 2021d). To this end, authorities can carefully sequence a package of growth-enhancing reforms, prioritizing policies aimed at alleviating the damage caused to human capital, investment, and productivity by the pandemic, while better aligning private sector incentives with broader economic policy objectives. These include policies that would facilitate the transition of labor across sectors while protecting vulnerable groups, deepen human capital, expand access to digital connectivity, reduce trade costs, and boost green investments.

**Reinvigorating human capital**

The COVID-19 recession caused a severe yet uneven collapse in employment across sectors, and some of those jobs are at risk of automation. EMDEs suffered particularly large declines in working hours (figure 1.24.A; ILO 2021a). Policy action needs to underpin a resilient and inclusive recovery in employment and limit the damage to human capital originating from long spells of unemployment. Active labor market policies—such as providing employment services, entrepreneurship support, and worker retraining programs—can be pursued to encourage employment in sectors experiencing higher growth (Card, Kluve, and Weber 2018; Schmillen 2020; Trebilcock 2014). Coupled with income support programs geared toward vulnerable populations, such as targeted cash transfers, active labor market policies can facilitate the movement of labor across sectors and enhance employment prospects in low-income countries (Escudero and Liepermann 2020).

Investing in education is also needed to mitigate the disruptions to human capital brought about by the pandemic, including learning losses and youth disengagement. About 60 percent of low- and lower-middle-income countries have cut their public education budgets since the onset of the crisis, reversing a decade-long trend of increased funding (figure 1.24.B; UNESCO 2021). Education budgets can be bolstered with additional financing deployed to incentivize attendance and educational attainment, improve school facilities, and reform incentive structures for teachers, which can also increase the efficiency of existing education spending (Hui, La-Bhus, and Baoping 2019; World Bank 2018b; World Bank 2021i). Investment in learning infrastructure leads to improved educational outcomes and higher incomes in the long term (Akresh, Halim, and Kleemans 2021). Moreover, governments can facilitate access to existing free and open-source education technologies in a way that favors the inclusion of disadvantaged groups (Burns et al. 2019; UNESCO 2020).

**Expanding access to digital connectivity**

Policies aimed at expanding access to digital connectivity can also be pursued to accelerate digital transformation and support higher productivity and potential output. In many EMDEs, this requires liberalizing telecom-
munications sectors while expanding investment in communications infrastructure. Properly liberalized telecommunications, coupled with regulatory independence and efficient taxation of digital services, can catalyze private sector investment that lowers the cost of access and increases internet adoption and access to digital services, with significant spillovers to the rest of the economy (Arezki et al. 2021; Rodriguez-Castelan et al. 2021; World Bank 2019).

Policy makers can also play a key role in accelerating the pace of adoption of digital technologies by firms (World Bank 2016). Efforts to foster equitable internet access for distance learning can help avoid the widening of a digital divide across income levels. In addition, policies that enhance data transparency and security can strengthen institutions, including by holding governments more accountable, which in the long run is associated with higher levels of per capita income (Islam and Lederman 2020). Fostering data transparency is important to guarantee an efficient allocation of resources, and it can also help reduce borrowing costs by instilling market discipline and reducing uncertainty (Kubota and Zeufack 2020).

Reducing trade costs

Trade integration can yield significant productivity gains, especially when it involves participation in global value chains (Constantinescu, Mattoo, and Ruta 2017; World Bank 2020e). Trade openness can raise incomes across sectors, lower poverty, and reduce gender bias in wages (World Bank and WTO 2020). Conversely, high trade costs hinder competitiveness, limit participation in global value chains, and erode consumer welfare by reducing the availability of goods and services for consumption (Diakantoni et al. 2017).

Trade costs have declined steadily in EMDEs since the mid-1990s. Still, in many countries, they remain well in excess of 100 percent of the value of traded goods and substantially higher than in advanced economies (figure 1.24.C-D). Trade costs are particularly elevated in small island states. Poor communication and transportation infrastructure, a lack of logistics services, lengthy

![Figure 1.24 Structural policies in emerging market and developing economies](image)

The pandemic severely reduced working hours in emerging market and developing economies (EMDEs). Disruptions to education have been particularly large in lower-income countries, a majority of which have cut education budgets since the pandemic began. In order to sustain the nascent recovery, authorities can prioritize policies to boost productivity, including measures that reduce trade costs. There remains significant scope to improve environmental performance in EMDEs, including by reducing greenhouse gas emissions and accelerating investments in green infrastructure.

![Table A. Changes in working hours in 2020](image)

<table>
<thead>
<tr>
<th>Category</th>
<th>Unemployment</th>
<th>Inactivity</th>
<th>Reduced or zero working hours</th>
<th>Percent</th>
</tr>
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<td>LICs</td>
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<td>30</td>
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![Table B. Share of countries with recent declines in education budgets](image)

<table>
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<tr>
<th>Category</th>
<th>Percent</th>
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</thead>
<tbody>
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<td>High- and upper-middle-income</td>
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<td>Low- and lower-middle-income</td>
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![Table C. Trade costs and tariff rates](image)

<table>
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<th>Category</th>
<th>Trade costs</th>
<th>Tariffs (RHS)</th>
<th>Percent</th>
</tr>
</thead>
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<td>5</td>
</tr>
<tr>
<td>EMDEs</td>
<td>120</td>
<td>10</td>
<td>0</td>
</tr>
<tr>
<td>LICs</td>
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<td>0</td>
</tr>
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</table>

![Table D. EMDE trade costs and tariff rates](image)

<table>
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<th>Category</th>
<th>Trade costs</th>
<th>Tariffs (RHS)</th>
<th>Percent</th>
</tr>
</thead>
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<tr>
<td>ECA</td>
<td>80</td>
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<tr>
<td>LAC</td>
<td>150</td>
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<tr>
<td>MNA</td>
<td>120</td>
<td>5</td>
<td>5</td>
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<tr>
<td>SAR</td>
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</tr>
<tr>
<td>SSA</td>
<td>100</td>
<td>10</td>
<td>0</td>
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![Table E. Environmental performance](image)

<table>
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<th>Category</th>
<th>Score</th>
<th>Percent</th>
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</thead>
<tbody>
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<td>EMDEs</td>
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<td>LICs</td>
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![Table F. Global greenhouse gas emissions](image)

<table>
<thead>
<tr>
<th>Category</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
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<td>Electricity and heat</td>
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</tr>
<tr>
<td>Transport</td>
<td>40</td>
</tr>
<tr>
<td>Other energy</td>
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<td>Agriculture</td>
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<td>Industry</td>
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</tr>
<tr>
<td>Waste</td>
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</tr>
</tbody>
</table>

Sources: Al-Samarrai et al. (2021); Comtrade (database); Environmental Performance Index, Yale University (database); ESCAP-World Bank Trade Cost Database; International Labour Organization (2021a); World Bank; World Resources Institute.

Note: EMDEs = emerging market and developing economies; EPI = Environmental Performance Index; LICs = low-income countries; EAP = East Asia and Pacific; ECA = Europe and Central Asia, LAC = Latin America and the Caribbean, MNA = Middle East and North Africa, SAR = South Asia, SSA = Sub-Saharan Africa.

A. Unemployment and inactivity converted into working-hour equivalents. EMDE aggregate calculated as the unweighted average of lower-middle-income countries and upper-middle-income countries. Advanced economies refers to ILO’s classification of high-income countries.

B. Figure shows share of countries with declines in education budgets between March 2020 and February 2021. Budget changes extracted from country documents for 29 EMDEs.

C.D. Data are for 2018. Blue bars show average trade costs expressed as ad valorem (tariff) equivalent of the value of traded goods. Red bars show average tariffs. Bilateral trade costs aggregated using 2018 bilateral country export shares. Yellow whiskers show interquartile ranges.

E. EPI is a proxy measure of environmental health calculated by Yale University for 180 countries based on 35 performance indicators. Countries ranked according to their relative performance across all categories. Orange whiskers show interquartile range.

F. Data are for 2018. “Other energy” includes energy used by industry, construction, and other emissions from energy production.
border processes, and elevated tariff barriers all contribute to high trade costs (chapter 3).

Authorities can facilitate trade integration by implementing policies that reduce the cost of trading, including streamlining border procedures and reducing border fees through simplification of border clearance procedures, automation, and digitalization of border processes. Adoption of digital technologies can also enhance information flows between exporters and shippers, supporting global value chains. In addition, enhancing transparency in the provision of customs information can reduce corruption and uncertainty. In lower-income countries, investments can improve connectivity by modernizing communications and road, railway, and port infrastructure, while trade liberalization can reduce tariff barriers. Swift implementation of reforms included in the WTO Trade Facilitation Agreement—such as provisions for expediting the movement, release, and clearance of goods in transit—can also be encouraged, including through close cooperation between customs authorities. Trade and global value chain integration could also be promoted through policies aimed at attracting FDI and fostering interactions of domestic firms with multinational corporations (Qiang, Zhenwei, and Steenbergen 2021).

Deploying and financing green infrastructure

The post-pandemic recovery represents an opportunity to pursue long-term strategies to put countries on a greener development path. Investments in green infrastructure, climate-smart agricultural technologies, and climate resilience, combined with sustainable energy policies, can play a pivotal role to this end. There is tremendous scope to improve environmental performance through green investments in EMDEs, including retrofitting buildings for energy efficiency and increasing the use of renewable energy sources to lower greenhouse gas emissions (figure 1.24.E-F). Enhancing environmental clean-up activities and monitoring and deterring the illicit extraction of natural resources can also bolster growth prospects (Strand and Toman 2010).

Attracting private investment is essential to realizing ambitious green investment goals. This requires a supportive domestic environment, with reduced risks, strong competition, and measures to promote capital flows. Providing an effective regulatory environment, while enforcing environmental standards, is paramount to this endeavor (Ambec et al. 2011). Authorities can also buttress the capacity of domestic financial sectors to attract capital to fund green investments in collaboration with international financial institutions, including by strengthening regulation and supervision of local financial institutions. Moreover, concessional finance can play a key role in supporting climate-smart investments. Authorities can also introduce regulations that “green” the financial sector, such as reporting requirements that highlight environmental, social, and governance risks to financial institutions.

As governments adopt policy measures to reinvigorate growth, they can further prioritize objectives related to climate change adaptation and resilience, including enhancing climate risk information systems (Tall et al. 2021). Infrastructures in EMDEs remain particularly vulnerable to climate risks (Miller and Swann 2016). In this regard, ensuring adequate infrastructure maintenance can promote resilience against climate disasters, which is particularly important for small island states (Rozenberg and Fay 2019). Moreover, promoting the issuance of green bonds can also increase investments in climate change mitigation and adaptation, especially if combined with carbon pricing policies (Heine et al. 2019).
<table>
<thead>
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<th>Commodity exporters</th>
<th>Commodity importers</th>
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<td>Liberia</td>
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<td>Libya*</td>
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<td>Armenia</td>
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<td>Azerbaijian*</td>
<td>Mali</td>
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<td>Mozambique</td>
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<td>Zimbabwe</td>
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| Albania             | Romania             |
| Antigua and Barbuda | Samoa               |
| Bahamas, The        | Serbia              |
| Bangladesh          | Sri Lanka           |
| Barbados            | St. Kitts and Nevis |
| Belarus             | St. Lucia           |
| Bhutan              | St. Vincent and the Grenadines |
| Bosnia and Herzegovina | Thailand         |
| Bulgaria            | Tonga               |
| Cambodia            | Tunisia             |
| China               | Turkey              |
| Croatia             | Tuvalu              |
| Djibouti            | Vanuatu             |
| Dominica            | Vietnam             |
| Egypt, Arab Rep.    |                     |
| El Salvador         |                     |
| Entrea              |                     |
| Eswatini            |                     |
| Georgia             |                     |
| Grenada             |                     |
| Haiti               |                     |
| Hungary             |                     |
| India               |                     |
| Jamaica             |                     |
| Jordan              |                     |
| Kiribati            |                     |
| Lebanon             |                     |
| Lesotho             |                     |
| Malaysia            |                     |
| Maldives            |                     |
| Marshall Islands    |                     |
| Mauritius           |                     |
| Mexico              |                     |
| Moldova             |                     |
| Montenegro          |                     |
| Nauru               |                     |
| North Macedonia     |                     |
| Pakistan            |                     |
| Palau               |                     |
| Panama              |                     |
| Philippines         |                     |
| Poland              |                     |

* Energy exporters.

1. Emerging market and developing economies (EMDEs) include all those that are not classified as advanced economies and for which a forecast is published for this report. Dependent territories are excluded. Advanced economies include Australia; Austria; Belgium; Canada; Cyprus; the Czech Republic; Denmark; Estonia; Finland; France; Germany; Greece; Hong Kong SAR; China; Iceland; Ireland; Israel; Italy; Japan; the Republic of Korea; Latvia; Lithuania; Luxembourg; Malta; the Netherlands; New Zealand; Norway; Portugal; Singapore; the Slovak Republic; Slovenia; Spain; Sweden; Switzerland; the United Kingdom; and the United States.

2. An economy is defined as commodity exporter when, on average in 2017-19, either (i) total commodities exports accounted for 30 percent or more of total exports or (ii) exports of any single commodity accounted for 20 percent or more of total exports. Economies for which these thresholds were met as a result of re-exports were excluded. When data were not available, judgment was used. This taxonomy results in the classification of some well-diversified economies as importers, even if they are exporters of certain commodities (for example, Mexico).

3. Commodity importers are all EMDEs that are not classified as commodity exporters.
References


