

## CHAPTER 1

# GLOBAL OUTLOOK



*Global growth is slowing due to a substantial rise in trade barriers and the pervasive effects of an uncertain global policy environment. Growth is expected to weaken to 2.3 percent in 2025, with deceleration in most economies relative to last year. This would mark the slowest rate of global growth since 2008, aside from outright global recessions. In 2026-27, a tepid recovery is expected, leaving global output materially below January projections. Progress by emerging market and developing economies (EMDEs) in closing per capita income gaps with advanced economies and reducing extreme poverty is anticipated to remain insufficient. The outlook largely hinges on the evolution of trade policy globally. Growth could turn out to be lower if trade restrictions escalate or if policy uncertainty persists, which could also result in a build-up of financial stress. Other downside risks include weaker-than-expected growth in major economies with adverse global spillovers, worsening conflicts, and extreme weather events. On the upside, uncertainty and trade barriers could diminish if major economies reach lasting agreements that address trade tensions. The ongoing global headwinds underscore the need for determined multilateral policy efforts to foster a more predictable and transparent environment for resolving trade tensions, some of which stem from macroeconomic imbalances. Global policy efforts are also needed to confront the deteriorating circumstances of vulnerable EMDEs amid prevalent conflict and debt distress, while addressing long-standing challenges, including the effects of climate change. National policy makers need to contain risks related to inflation as well as strengthen their fiscal positions by raising additional domestic revenues and re-prioritizing spending. To facilitate job creation and boost long-term growth prospects in EMDEs, reforms are essential to enhance institutional quality, stimulate private investment growth, develop human capital, and improve labor market functioning.*

## Summary

After being buffeted by a series of adverse shocks over 2020-24, the global economy is facing another significant headwind this year, with increased trade barriers and heightened policy uncertainty leading to a notable deterioration of the outlook relative to January (figure 1.1.A). In particular, global output is expected to grow at its weakest pace since 2008, aside from outright global recessions (figure 1.1.B). The sharp increase in tariffs and the ensuing uncertainty are contributing to a broad-based growth slowdown and deteriorating prospects in most of the world's economies (figure 1.1.C). Subdued global growth prospects are unlikely to improve materially without policy actions to address increasing trade restrictions, geopolitical tensions, heightened uncertainty, and limited fiscal space.

The global outlook is predicated on tariff rates close to those of late May prevailing throughout the forecast horizon. Accordingly, pauses to previously announced tariff hikes between the

United States and its trading partners are assumed to persist. This baseline nonetheless entails the highest U.S. average effective tariff rate in nearly a century. In addition, in view of recent rapid shifts in trade policies and the potential for a return to even higher tariffs, consumers and businesses continue to grapple with unusually elevated uncertainty (figure 1.1.D). In this context, a prospective recovery in global trade and investment—two important drivers of long-term development that have been relatively subdued in recent years—has been disrupted.

Commodity prices plunged in early April in response to deteriorating growth prospects. Oil prices posted an especially large decline, with the effects of a notable hike in oil production by OPEC+ nations compounded by a muted outlook for oil demand growth (figure 1.1.E). Base metal prices also dropped as markets priced in substantial headwinds to global manufacturing and industrial activity but have since partially recovered. Overall commodity prices are forecast to decline by 10 percent in 2025, softening further in 2026—mainly due to falling oil prices.

Global headline inflation generally remains elevated relative to central bank targets and pre-pandemic averages and has even risen in some advanced economies since late last year. Slower

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*Note:* This chapter was prepared by Carlos Arteta, Phil Kenworthy, Nikita Perevalov, Peter Selcuk, Garima Vasishtha, and Collette Wheeler, with contributions from Mirco Balatti, Jongrim Ha, Samuel Hill, Gitanjali Kumar, Dawit Mekonnen, Alen Mulabdic, Edoardo Palombo, Shijie Shi, Naotaka Sugawara, and Takuma Tanaka.

**TABLE 1.1 Real GDP<sup>1</sup>**

(Percent change from previous year unless indicated otherwise)

	2022	2023	2024e	2025f	2026f	2027f	Percentage-point differences from January 2025 projections	
							2025f	2026f
<b>World</b>	<b>3.3</b>	<b>2.8</b>	<b>2.8</b>	<b>2.3</b>	<b>2.4</b>	<b>2.6</b>	<b>-0.4</b>	<b>-0.3</b>
<b>Advanced economies</b>	<b>2.9</b>	<b>1.7</b>	<b>1.7</b>	<b>1.2</b>	<b>1.4</b>	<b>1.5</b>	<b>-0.5</b>	<b>-0.4</b>
United States	2.5	2.9	2.8	1.4	1.6	1.9	-0.9	-0.4
Euro area	3.5	0.4	0.9	0.7	0.8	1.0	-0.3	-0.4
Japan	0.9	1.4	0.2	0.7	0.8	0.8	-0.5	-0.1
<b>Emerging market and developing economies</b>	<b>3.8</b>	<b>4.4</b>	<b>4.2</b>	<b>3.8</b>	<b>3.8</b>	<b>3.9</b>	<b>-0.3</b>	<b>-0.2</b>
East Asia and Pacific	3.6	5.2	5.0	4.5	4.0	4.0	-0.1	-0.1
China	3.1	5.4	5.0	4.5	4.0	3.9	0.0	0.0
Indonesia	5.3	5.0	5.0	4.7	4.8	5.0	-0.4	-0.3
Thailand	2.6	2.0	2.5	1.8	1.7	2.3	-1.1	-1.0
Europe and Central Asia	1.5	3.6	3.6	2.4	2.5	2.7	-0.1	-0.2
Russian Federation	-1.4	4.1	4.3	1.4	1.2	1.2	-0.2	0.1
Türkiye	5.5	5.1	3.2	3.1	3.6	4.2	0.5	-0.2
Poland	5.3	0.2	2.9	3.2	3.0	2.9	-0.2	-0.2
Latin America and the Caribbean	4.0	2.4	2.3	2.3	2.4	2.6	-0.2	-0.2
Brazil	3.0	3.2	3.4	2.4	2.2	2.3	0.2	-0.1
Mexico	3.7	3.3	1.5	0.2	1.1	1.8	-1.3	-0.5
Argentina	5.3	-1.6	-1.8	5.5	4.5	4.0	0.5	-0.2
Middle East and North Africa	5.4	1.6	1.9	2.7	3.7	4.1	-0.7	-0.4
Saudi Arabia	7.5	-0.8	1.3	2.8	4.5	4.6	-0.6	-0.9
Iran, Islamic Rep. <sup>2</sup>	3.8	5.0	3.0	-0.5	0.3	1.8	-3.2	-1.9
Egypt, Arab Rep. <sup>2</sup>	6.6	3.8	2.4	3.8	4.2	4.6	0.3	0.0
South Asia	6.0	7.4	6.0	5.8	6.1	6.2	-0.4	-0.1
India <sup>2</sup>	7.6	9.2	6.5	6.3	6.5	6.7	-0.4	-0.2
Bangladesh <sup>2</sup>	7.1	5.8	4.2	3.3	4.9	5.7	-0.8	-0.5
Pakistan <sup>2</sup>	6.2	-0.2	2.5	2.7	3.1	3.4	-0.1	-0.1
Sub-Saharan Africa	3.9	2.9	3.5	3.7	4.1	4.3	-0.4	-0.2
Nigeria	3.3	2.9	3.4	3.6	3.7	3.8	0.1	0.0
South Africa	2.1	0.8	0.5	0.7	1.1	1.3	-1.1	-0.8
Angola	3.0	1.0	4.4	2.7	2.6	3.2	-0.2	-0.3
<b>Memorandum items:</b>								
<b>Real GDP<sup>1</sup></b>								
High-income countries	2.9	1.7	1.9	1.3	1.5	1.7	-0.5	-0.4
Middle-income countries	3.9	4.8	4.4	4.1	4.0	4.0	-0.2	-0.1
Low-income countries	4.4	2.8	4.6	5.3	6.1	6.0	-0.4	0.2
EMDEs excluding China	4.2	3.7	3.6	3.4	3.7	4.0	-0.4	-0.2
Commodity-exporting EMDEs	3.3	2.7	3.1	2.9	3.2	3.4	-0.3	-0.2
Commodity-importing EMDEs	4.0	5.2	4.7	4.3	4.1	4.2	-0.2	-0.1
Commodity-importing EMDEs excluding China	5.4	4.9	4.2	3.9	4.4	4.6	-0.5	-0.2
EM7	3.5	5.4	4.8	4.1	3.9	3.9	-0.1	0.0
World (PPP weights) <sup>3</sup>	3.5	3.4	3.3	2.9	3.0	3.1	-0.3	-0.2
<b>World trade volume<sup>4</sup></b>	<b>5.9</b>	<b>0.8</b>	<b>3.4</b>	<b>1.8</b>	<b>2.4</b>	<b>2.7</b>	<b>-1.3</b>	<b>-0.8</b>
<b>Commodity prices<sup>5</sup></b>								
							Level differences from January 2025 projections	
WBG commodity price index	142.5	108.0	105.1	94.2	89.0	91.9	-4.3	-7.7
Energy index	152.6	106.9	101.5	86.2	80.2	84.4	-7.4	-11.5
Oil (US\$ per barrel)	99.8	82.6	80.7	66.0	61.0	65.0	-6.0	-10.0
Non-energy index	122.1	110.2	112.5	110.3	106.8	107.1	1.8	-0.2

Source: World Bank.

Note: e = estimate; f = forecast. EM7 = Brazil, China, India, Indonesia, Mexico, the Russian Federation, and Türkiye. WBG = World Bank Group. 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. For the definition of EMDEs, developing countries, commodity exporters, and commodity importers, please refer to table 1.2. The World Bank is currently not publishing economic output, income, or growth data for Turkmenistan and República Bolivariana de Venezuela owing to lack of reliable data of adequate quality. Turkmenistan and República Bolivariana de Venezuela are excluded from cross-country macroeconomic aggregates.

1. Headline aggregate growth rates are calculated using GDP weights at average 2010-19 prices and market exchange rates.

2. GDP growth rates are on a fiscal year (FY) basis. Aggregates that include these countries are calculated using data compiled on a calendar year basis. For India and the Islamic Republic of Iran, the column for 2022 refers to FY2022/23. For Bangladesh, the Arab Republic of Egypt, and Pakistan, the column for 2022 refers to FY2021/22. Pakistan's growth rates are based on GDP at factor cost.

3. 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.

4. World trade volume of goods and nonfactor services.

5. Indexes are expressed in nominal U.S. dollars (2010 = 100). Oil refers to the Brent crude oil benchmark. For weights and composition of indexes, see <https://worldbank.org/commodities>.

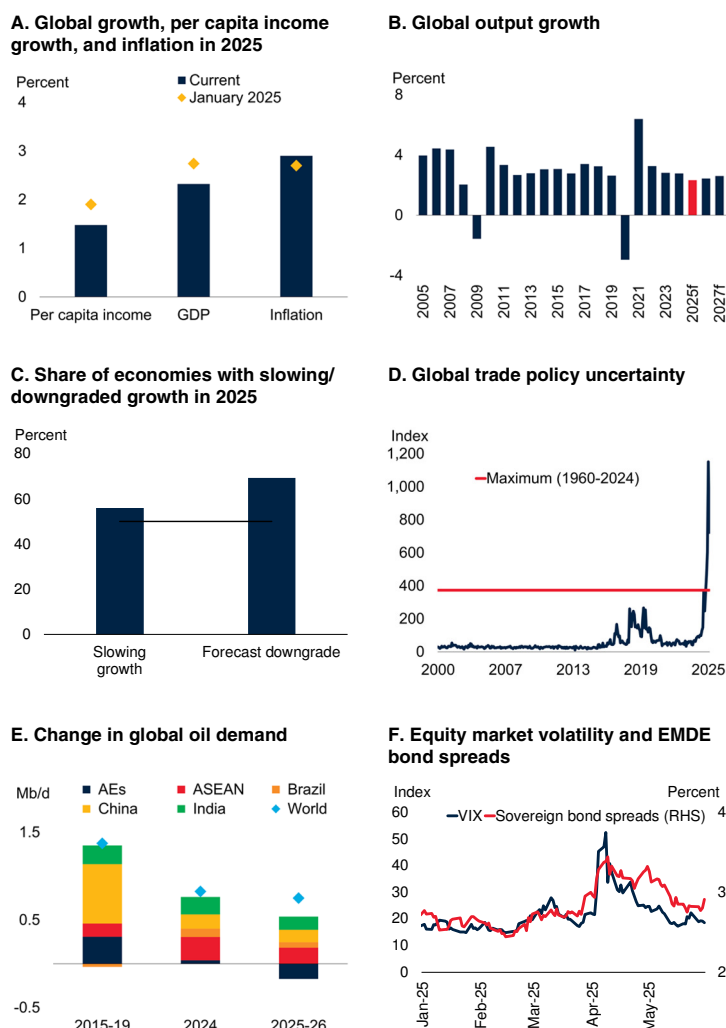
disinflation globally over the last six months has largely reflected continuing inflationary pressures from services prices. The recent rise in consumer inflation expectations has been influenced by the implementation of trade restrictions. In addition, core inflation in some economies is expected to remain high due to persistent services price increases. In all, GDP-weighted global inflation is projected to average 2.9 percent in 2025 and 2026—still a little above the average inflation target—but with notable heterogeneity across economies.

Global financial conditions have been tighter this year, on average, relative to late 2024, principally reflecting trade policy uncertainty. Volatility in financial markets spiked and equity markets plunged globally as trade tensions escalated in early April; however, asset prices largely recovered after an initial 90-day tariff pause was announced and following the rollback in U.S.-China tariffs in May (figure 1.1.F). Long-term government bond yields in major advanced economies have increased since late last year, albeit with pronounced volatility. EMDE financial conditions are also somewhat tighter, on average, relative to late last year. In early April, many EMDEs saw sharp declines in equity markets amid a surge in capital outflows. Sovereign spreads rose, albeit to differing degrees based on economies' exposure to announced trade barriers. Nevertheless, EMDE equity markets regained ground and spreads narrowed again following the partial de-escalation in trade tensions.

Against this backdrop, global growth is set to slow this year, to 2.3 percent—substantially weaker than previously projected amid the impact of higher trade barriers, elevated uncertainty, increased financial volatility, and weakened confidence. Thereafter, growth is forecast to firm to about 2.5 percent over 2026–27, as trade flows continue adjusting to higher tariffs such that global trade edges up, while policy uncertainty moderates from record-high levels. The downgrade to global growth this year is principally driven by advanced economies (figure 1.2.A). This slowdown is projected to be concentrated on investment, including foreign direct investment (FDI) and portfolio flows—which tend to respond

## FIGURE 1.1 Global economic prospects

*The global outlook has deteriorated substantially relative to January, with global growth in 2025 expected to register its weakest pace since 2008, aside from outright global recessions. This deterioration is broad-based across the world's economies and follows sharp increases in trade tensions and policy uncertainty. The slowdown in global growth will erode demand for oil and various other commodities, weighing on the outlook for many EMDE commodity exporters. Following U.S. tariff announcements, financial markets experienced substantial turbulence, with a spike in equity market volatility and a rise in EMDE sovereign bond spreads, although these subsequently subsided.*



Sources: Caldara et al. (2020); Haver Analytics; International Energy Agency (IEA); J.P. Morgan; UN World Population Prospects; World Bank.

Notes: f = forecast. AEs = advanced economies; ASEAN = Association of Southeast Asian Nations; EMDEs = emerging market and developing economies; mb/d = million barrels per day; GDP aggregates calculated using real U.S. dollar GDP weights at average 2010-19 prices and market exchange rates.

A. Blue bars "current" correspond to the current edition of the *Global Economic Prospects* (GEP) report and yellow diamonds "January 2025" correspond to the January 2025 edition of the GEP.

B. Data for 2024 are estimates; data for 2025–27 are forecasts.

C. Panel shows the share of economies with slowing growth and with growth outlook downgraded relative to January 2025 forecasts. Horizontal line shows 50 percent.

D. Trade Policy Uncertainty Index, based on automated text searches of the electronic archives of seven newspapers. A higher value indicates higher trade policy uncertainty. Last observation is May 2025.

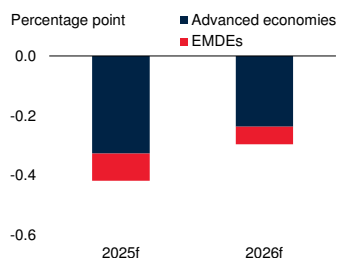
E. Bars indicate the average change in annual oil demand in mb/d for the selected periods. Data based on IEA's Oil Market Report, May 2025 edition. 2025 and 2026 are projections.

F. Blue line represents the daily CBOE Volatility Index, which measures market expectations of near-term volatility conveyed by stock index option prices. Red line represents the median sovereign bond spread for a sample of up to 71 EMDEs. Last observation is May 30, 2025.

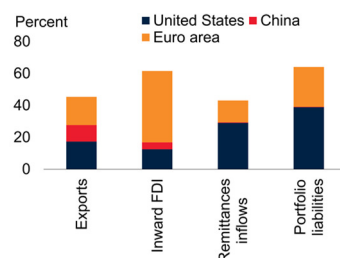
## FIGURE 1.2 Global economic prospects (continued)

The deterioration in the global outlook has largely emanated from trade shocks, with forecasts for advanced economies downgraded markedly. These shocks are set to weigh on EMDEs via trade, financial, and investment flows with major economies. Risks are tilted to the downside. Global growth could be even lower if an escalation of trade tensions and uncertainty further weakens investment, trade, and confidence. Geopolitical fragmentation could accelerate if trade or geopolitical tensions worsen. In EMDEs, a higher incidence of conflict could lead to lasting output losses. A downside scenario of renewed trade tensions could push the world economy into an extended period of anemic growth.

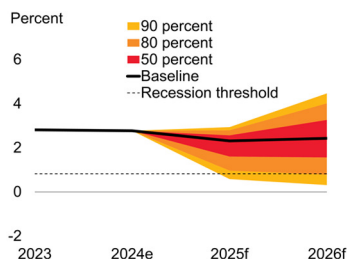
### A. Contributions to global growth downgrades in 2025 and 2026



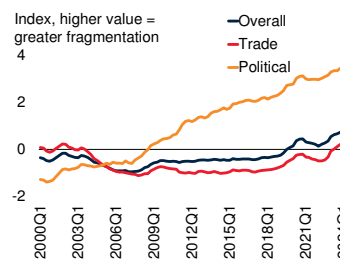
### B. Trade and financial linkages between major economies and EMDEs excluding China



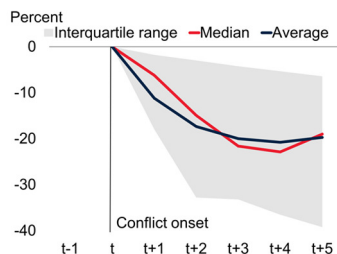
### C. Probability distribution around global growth forecast



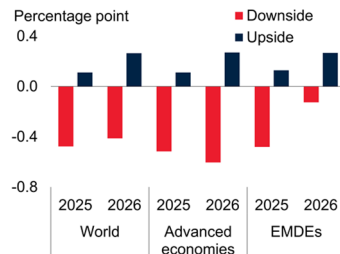
### D. Geopolitical Fragmentation Index



### E. Cumulative loss of per capita GDP following the onset of high-intensity conflicts



### F. Change in global growth in alternative scenarios



Sources: BIS (database); Bloomberg; Consensus Economics; Fernández-Villaverde, Mineyama, and Song (2025); IMF Coordinated Direct Investment Survey (database); Ohnsorge, Stocker, and Some (2016); Uppsala Conflict Data Program; Oxford Economics; World Bank (WITS; KNOMAD).

Note: e = estimate; f = forecast. EMDEs = emerging market and developing economies; FDI = foreign direct investment; GDP aggregates calculated using real U.S. dollar GDP weights at average 2010-19 prices and market exchange rates.

A. Contributions to the global growth downgrade between the current and the January 2025 editions of *Global Economic Prospects*.

B. Bars show, for EMDEs excluding China, the share of total exports (total inward FDI positions, remittance inflows, and portfolio liabilities) that are to (from) China, the euro area, and the United States. See figure 1.11.C for details.

C. The dashed line is the global recession threshold (below zero per capita growth). Probabilities use the range and skewness implied by oil and equity price derivatives, and term spread forecasts. Last observation is May 2025.

D. Last observation is 2024Q1. See figure 1.13.B for details.

E. Lines show the cumulative gap between forecasted and actual per capita GDP following high-intensity conflict. Sample includes 14 conflicts in 14 EMDEs (3 not currently FCS) from 2006-23. See figure 1.12.E for details.

F. Panel shows the deviation of aggregate growth in the upside and downside scenarios, using Oxford Economics' Global Economic Model.

more to demand shifts than aggregate output—and trade, with widespread adverse spillovers to other economies (figure 1.2.B).

Growth in EMDEs is expected to slow in 2025, to 3.8 percent, before edging up a touch over 2026-27, to 3.9 percent. China's economy is projected to decelerate across the forecast horizon, as a near-term boost from fiscal policy fades amid slowing potential growth. Meanwhile, near-term growth in many other EMDEs is anticipated to decelerate amid weakening investment, which is likely to more than offset any possible benefits from trade diversion during the forecast period. Against the backdrop of a deteriorating external environment, progress by EMDEs in closing sizable per capita income gaps with advanced economies, spurring job creation, or reducing extreme poverty rates is anticipated to remain insufficient, leaving poverty rates above pre-pandemic levels in many poorer or fragile EMDEs. At the same time, many of these economies are set to face a looming jobs challenge in the coming decades, especially if employment growth continues to be outstripped by population growth.

Risks to the global outlook remain tilted decidedly to the downside (figure 1.2.C). High and persistent policy uncertainty—particularly related to trade—could lead to greater-than-expected weakening in investment, trade, and confidence. Renewed increases in trade restrictions could push inflation higher in key economies, magnifying real income losses and limiting the scope for major central banks to support flagging growth by lowering policy rates. This backdrop also implies several potential triggers for a souring of financial risk appetite, which could reverberate globally and amplify downside surprises to growth. Even with efforts to resolve some major conflicts, geopolitical tensions and regional conflict risks persist in many parts of the world and could contribute to further geopolitical fragmentation (figure 1.2.D). Moreover, worsening conflict could generate lasting, concentrated output losses, particularly in EMDEs (figure 1.2.E). Natural disasters, the frequency and intensity of which have increased over time, pose another ever-present threat in many economies.

Nonetheless, there are also some notable upside risks to growth. A cooling of trade tensions on the back of recent and ongoing negotiations—for instance, through further trade agreements between large economies that secure lower tariffs—would curb uncertainty, limit trade disruptions, and strengthen business and consumer confidence. A synchronous loosening of fiscal policy in several large economies could mitigate the downward pressures on demand, albeit while also exerting upward pressure on inflation, government debt levels, and interest rates. Efforts to widely employ recent advances in technology—notably artificial intelligence (AI)—could give rise to stronger-than-anticipated global investment growth and start to feed into broad productivity improvements.

To quantify downside risks concerning trade policy, a scenario is modeled in which U.S. weighted average tariffs increase by about 10 percentage points relative to the baseline, with proportional retaliation from trading partners. This sudden escalation in trade barriers results in global trade seizing up in the second half of this year and is accompanied by a widespread collapse in confidence, surging uncertainty, and turmoil in financial markets. The combination of these multiplying shocks reduces global growth, by 0.5 and 0.4 percentage point in 2025 and 2026, relative to the baseline, tipping the world economy into an extended period of anemic growth (figure 1.2.F). In contrast, an upside scenario features further trade agreements that halve tariffs relative to the baseline and reduce trade-related uncertainty. Under these conditions, global growth would be higher compared with the baseline by 0.1 and 0.3 percentage point in the next two years.

The challenging global context highlights the need for policy action at both global and national levels. To mitigate the adverse impact of elevated trade barriers and policy uncertainty on global growth, a key priority is to foster dialogue and cooperation to address global imbalances and restore a more predictable, transparent, and rules-based approach to resolving trade tensions and avoiding escalation. The global community also needs to confront the worsening circumstances of many vulnerable

EMDEs amid debt distress, acute food insecurity, and prevalent conflict. Tackling these severe headwinds to growth and development has become more challenging considering declining aid flows from key donors. Meanwhile, reinvigorating global efforts toward climate change adaptation and mitigation is vital to limit the future economic and social costs of increasingly frequent natural disasters.

Policy action at the domestic level is critical. Some EMDE central banks will face a difficult balancing act between addressing continuing price pressures, on the one hand, and seeking to moderate the contractionary effects of trade restrictions and policy uncertainty, on the other. This will require careful calibration of monetary policy tailored to each economy's circumstances. At the current juncture, some EMDEs may be especially prone to financial volatility and capital outflows, underscoring the importance of central bank credibility. With respect to fiscal policy, many EMDEs are not well positioned for the expected slowdown in growth, with fiscal deficits remaining above pre-pandemic averages and debt levels rising in many economies. To build fiscal space, EMDEs need to raise additional domestic revenues, especially where other sources of financing are drying up, while reprioritizing spending toward growth-enhancing measures and protecting vulnerable populations.

In the long run, the most sustainable solution to the wide range of challenges facing EMDEs—including insufficient job creation, slow poverty reduction, debt-related challenges, and scarce fiscal resources—is to foster stronger environments for private investment and raise potential growth. Reinvigorating FDI deserves particular attention, given its historical role as a vector of technology diffusion and productivity gains. Doing so would require improving institutions and safeguarding political, regulatory, and socioeconomic stability.

To help EMDEs create productive employment for growing working-age populations, measures to strengthen foundational infrastructure, address structural bottlenecks, and enhance private sector dynamism are critical. Priorities could include

policies that encourage upskilling workers, ease access to finance, and promote labor markets that better match workers and employers. Moreover, policy makers need to consider not only aggregate job creation but also the quality of jobs—for instance, by seeking to improve productivity, ensure good working conditions, and reduce barriers to firms expanding and formalizing. For EMDEs recently or currently embroiled in conflict, attaining durable peace and stability is paramount not only for limiting the human toll but also as a prerequisite for raising employment, human capital, and income levels.

## Global context

Against the backdrop of heightened policy uncertainty and increased trade barriers, the global economic context has become more challenging, with the risk of further adverse policy shifts materializing, particularly with respect to trade relations among the largest economies. The rise in trade restrictions clouds the near-term trade outlook—despite solid trade growth earlier this year, which partly reflected the front-loading of imports by some large economies in anticipation of tariff hikes. Beyond the direct impact of higher tariffs, the potential for further rapid shifts in the timelines and magnitudes of trade-restrictive measures is a source of sentiment-sapping policy uncertainty. Commodity prices have fallen substantially, reflecting new headwinds to global manufacturing and broader industrial activity. With re-emerging pressures in core inflation globally, the pace of global disinflation has slowed, while survey-based inflation expectations in key countries have risen alongside tariff-related developments. Trade policy shifts and the associated increase in uncertainty weighed substantially on financial markets earlier this year, although risk appetite has largely recovered in recent weeks.

### Global trade

Global trade conditions experienced a large shock in early April when the United States announced prospective tariffs on most trading partners, with rates proportional to bilateral goods trade deficits, in addition to previously announced tariffs. A sharp escalation of trade barriers between China

and the United States followed. Subsequently, country-specific tariffs were reduced to a universal 10 percent—including in the case of China, with initially prohibitively high tariff rates being rolled back sharply in May. However, other tariff increases remain on China and other large trade partners. As a result, the effective U.S. tariff rate has been brought to levels not seen in almost a century (figure 1.3.A). Tariff rates in effect as of May 27 are assumed to prevail throughout the forecast period, but there is notable uncertainty in this regard. The baseline projections for global trade also incorporate important carve-outs for USMCA-compliant goods, pharmaceuticals, semiconductors, bullion, energy, copper, and other critical minerals, as well as retaliatory measures in place as of late May.

Shifting policy announcements have led to heightened global trade policy uncertainty, measures of which reached historical highs over the past few months (figure 1.3.B). This reflects uncertainty over whether current tariff rates will endure, their implementation, and the scale and timing of potential retaliatory responses. New tariff measures mark an intensification of the upward trend in trade-restrictive measures seen in recent years, with a significant risk of further escalation in trade barriers, as announced policies could generate substantial spillovers to third markets. These markets may respond by adopting protectionist measures to shield domestic industries from a surge in imports.

Prior to the recent tariff announcements, growth in global goods trade had accelerated at the turn of the year, partly reflecting inventory build-ups in anticipation of changes in trade policy in major economies (figure 1.3.C). The growth in goods trade has been relatively widespread, albeit with the pace of expansion in advanced economies exceeding that in EMDEs. Likely driven by the rush to front-load imports before tariffs took effect, the global new export orders manufacturing PMI subindex briefly entered expansionary territory in March, signaling temporary improvements in goods trade, before falling in April to its lowest level in 20 months. Global services trade growth has flattened out after several years of recovery from the pandemic, with travel activity approaching pre-pandemic levels. The

stabilization in services trade is also reflected in the continued softening of the expansion in the global services PMI.

Global trade growth in goods and services is projected to slow sharply in 2025, to 1.8 percent, from 3.4 percent in 2024 (figure 1.3.D). The forecast has been revised down by 1.3 percentage points since January, reflecting changes in trade policies in key economies and higher trade policy uncertainty. Increased tariffs are expected to weigh on global trade over the forecast horizon. In tandem with the projected pickup in global growth, trade growth is nonetheless forecast to firm from a feeble pace this year, reaching 2.4 percent in 2026 and 2.7 percent in 2027—still well below its pre-pandemic average of 4.6 percent. The forecast for global trade growth masks significant heterogeneity. Countries with greater export exposure to EMDE markets are projected to recover more rapidly than those more reliant on advanced economies, though elevated policy uncertainty and weakening demand could weigh on the recovery more broadly.

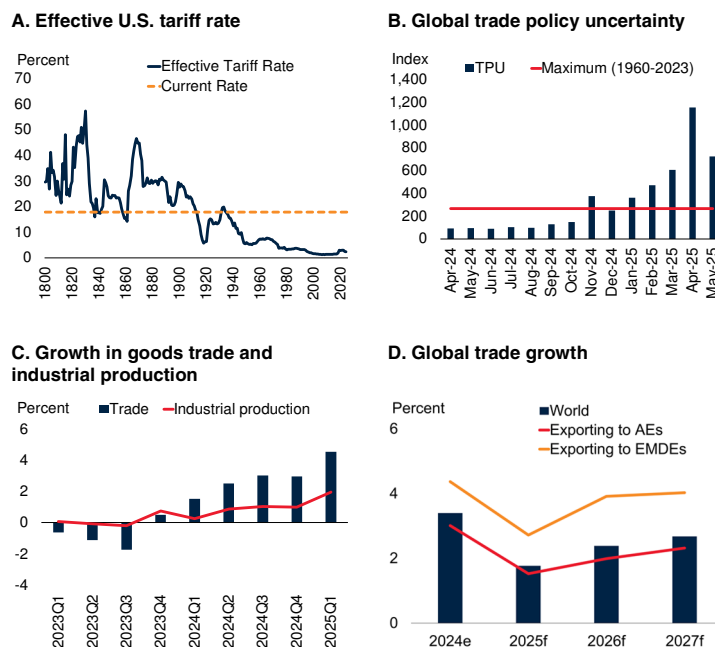
The outlook for global trade is subject to substantial downside risks, notably a renewed escalation of trade restrictions. Even absent further escalation, a related risk is that uncertainty about trade and other policies could slow investment, an import-intensive component of GDP, dampening trade more than anticipated.

## Commodity markets

Commodity prices have fallen since February, largely owing to weaker growth prospects amid increased trade barriers and policy uncertainty (figure 1.4.A). Largely reflecting these movements, annual average commodity prices are expected to decline by 10 percent in 2025 (figure 1.4.B). In 2026, commodity prices are projected to soften further, by 6 percent, as production of some energy and metals commodities expands and supply constraints on several agricultural commodities ease. Thereafter, commodity prices are projected to edge up as global growth continues to recover, supporting commodity consumption. Risks to the commodity price projections are tilted to the downside, as a renewed escalation of trade tensions between

**FIGURE 1.3 Global trade**

*The effective U.S. tariff rate has risen sharply in 2025 to its highest level in almost a century. Trade policy uncertainty, which has reached record-high levels, could further weaken trade prospects. Global goods trade growth had firmed at the turn of the year, partly reflecting inventory build-ups ahead of new tariff announcements. Global trade growth is projected to slow substantially in 2025 and then firm in 2026–27, in line with the projected pickup in global growth.*



Sources: Caldara et al. (2020); CPB Netherlands Bureau of Economic Analysis; IMF; The Budget Lab; World Bank.

Note: e = estimate; f = forecast. AEs = advanced economies; EMDEs = emerging market and developing economies. Trade in goods and services is measured as the average of export and import volumes.

A. Panel shows historical and projected customs duty revenues based on tariffs in force as of May 12, 2025, as a share of goods imports, without accounting for potential shifts in consumer and business purchasing behavior in response to tariff increases.

B. Trade Policy Uncertainty index, based on automated text searches of the electronic archives of seven newspapers: *Boston Globe*, *Chicago Tribune*, *Guardian*, *Los Angeles Times*, *New York Times*, *Wall Street Journal*, and *Washington Post*. A higher value indicates higher trade policy uncertainty. Last observation is May 2025.

C. Panel shows the annual percentage change in goods trade volume and industrial production. Last observation is March 2025.

D. Panel shows the growth of global trade volume in goods and services. "Exporting to AEs" refers to trade growth for countries with over 50 percent of exports to advanced economies during the 2015–19 period; "Exporting to EMDEs" refers to trade growth for countries with over 50 percent of exports to EMDEs during the 2015–19 period.

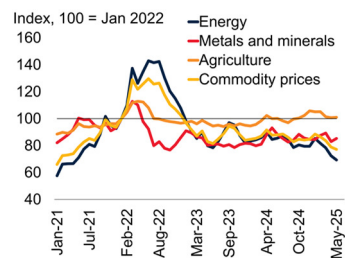
major economies could further weaken global trade and investment, undermining commodity demand.

Oil prices declined precipitously in early April, as worries about the effect of rising trade tensions on demand coincided with OPEC+ pivoting toward relatively rapid increases in oil production. Brent oil prices are projected to average \$66 per barrel this year and \$61 per barrel next year, with demand growth set to remain well below 2015–19

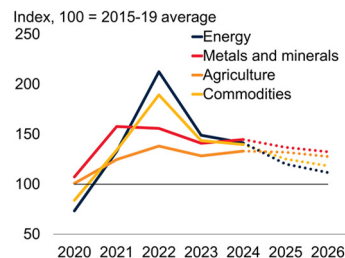
## FIGURE 1.4 Commodity markets

Commodity prices have fallen, partly reflecting deteriorating growth prospects due to increased trade tensions and policy uncertainty. Annual average prices are expected to decline markedly in 2025 and soften further in 2026. Energy prices are forecast to decrease by 15 percent this year, reflecting increases in oil production from OPEC+ and weakening demand growth, which is set to remain well below 2015-19 levels. From early in 2025, the front-running of new trade-restrictive measures buoyed aluminum prices to well above global benchmarks.

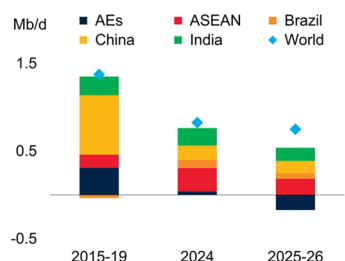
### A. Commodity prices



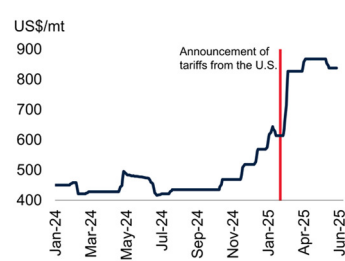
### B. Commodity price forecasts



### C. Change in global oil demand



### D. U.S. Midwest premium for aluminum



Sources: Bloomberg; International Energy Agency (IEA); World Bank.

Note: AEs = advanced economies; ASEAN = Association of Southeast Asian Nations; IEA = International Energy Agency; mb/d = million barrels per day.

A.B. "Commodity prices"/"Commodities" line refers to the World Bank Commodity Price Index, excluding precious metals.

A. Monthly prices. Last observation is May 2025.

B. Dashed lines indicate forecasts.

C. Bars indicate the average change in annual oil demand in mb/d for the selected periods. Data based on IEA's Oil Market Report, May 2025 edition. 2025 and 2026 are projections. ASEAN includes the following members: Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Viet Nam. Data for Lao PDR is excluded from the calculations due to its unavailability.

D. Five-day moving average of July 2025 futures contract for aluminum Midwest premium. Premium reflects the additional cost above the London Metal Exchange price for aluminum delivered to U.S. Midwest. Last observation is June 3, 2025.

levels (figure 1.4.C). In contrast, annual average natural gas prices are set to climb markedly this year, due mainly to a more than 50 percent jump in U.S. natural gas prices. While European natural gas prices have generally fallen in recent months due to mild weather and adequate inventories, U.S. prices have been buoyed by the ongoing structural expansion of LNG exports. In all, energy prices are projected to decrease by 15 percent in 2025 and 7 percent in 2026, before increasing somewhat in 2027 as oil prices firm.

Agricultural commodity prices are forecast to be little changed this year and decrease slightly in 2026-27. In 2025, a surge in beverage prices—reflecting weather-related supply shocks to coffee and cocoa—is expected to be offset by a decline in food commodity prices, partly owing to mounting rice stocks and record-high soybean production. In addition, maize prices are projected to edge down, in part due to lower oil prices reducing demand for maize-derived ethanol. In 2026-27, beverage prices are expected to start normalizing, with food prices broadly holding steady, such that overall agricultural prices are forecast to soften slightly.

Metal prices (excluding precious metals) fell sharply in early April as global growth prospects deteriorated, before partially recovering as trade tensions cooled somewhat. From earlier in the year, copper and aluminum prices were bolstered by the front-running of prospective tariff increases, with U.S. aluminum prices substantially exceeding the global benchmark (figure 1.4.D). In all, the metals index is projected to drop by 5 percent in 2025 and drift lower in 2026 before stabilizing. Prices for most base metals are set to decline this year, reflecting trade-related headwinds to global manufacturing. The precious metals price index—reflecting principally gold but also silver and platinum—is projected to buck the broader trend, increasing by more than 30 percent in 2025. Annual average gold prices are expected to reach a record high this year, supported by safe haven flows, before plateauing in 2026-27.

## Global inflation

Global headline consumer price inflation has remained elevated above pre-pandemic norms over the past year, briefly edging higher in some advanced economies in early 2025 (figure 1.5.A). Continued tightness in labor markets has kept core inflation at a somewhat elevated level in many economies. In EMDEs, monthly headline inflation readings were volatile earlier this year, with a pickup in core inflation partly reflecting rising services prices and wage pressures.

The outlook for global inflation has become more uncertain since last year due to a combination of shocks. Most notably, substantial tariff hikes are

set to exert upward pressure on consumer inflation in key economies by raising prices for imported consumer goods and inputs into production and redirecting demand toward domestic production that is relatively inelastic in the short run (Barbiero and Stein 2025). Indeed, manufacturing purchasing managers in advanced economies have already reported accelerating input and output prices so far this year (figure 1.5.B). Even so, outside economies where import duties have significantly increased, higher trade barriers are likely to be generally deflationary as they weaken external demand. There may nevertheless be other upside risks to inflation in these economies that are indirectly associated with trade restrictions. These include the potential for damage to global supply chains to push up prices in unpredictable ways, and the possibility of sizable currency depreciations.

Inflation expectations, particularly at the shorter horizon, have picked up in 2025, mainly in some major economies (figure 1.5.C). This is likely explained by the expected impact of tariff increases on consumer prices, even as trade tensions weigh on economic activity and commodity prices. Persistent underlying inflationary pressures, coupled with the impact of rising tariffs and trade-protectionist measures, are anticipated to delay the normalization of global inflation to levels broadly consistent with inflation targets. On a GDP-weighted basis, global inflation is projected to average 2.9 percent in both 2025 and 2026, before easing to 2.5 percent in 2027—about in line with the average inflation target. However, there is significant heterogeneity across countries, with inflation projections revised slightly lower in EMDEs in 2025 due to the impact of weaker demand for traded goods, while being revised significantly higher in advanced economies, primarily the United States (figure 1.5.D).

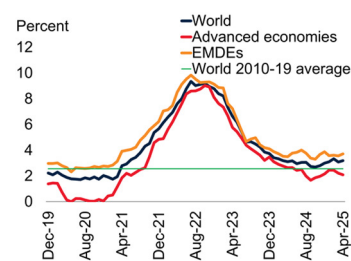
### Global financial developments

Global financial conditions have been tighter this year, on average, compared to late 2024, due to financial market volatility and some decline in risk appetite, fueled by elevated trade policy uncertainty (figure 1.6.A). The surge in and then partial de-escalation of trade tensions in the second quarter led to marked financial market turbulence,

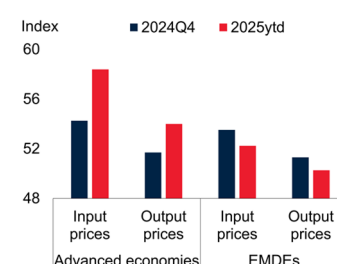
**FIGURE 1.5 Global inflation**

*Global headline inflation has remained somewhat elevated over the past year, briefly edging higher in advanced economies in early 2025. Tariff-induced upward pressure on prices has begun to build along supply chains, particularly in advanced economies, with manufacturing surveys pointing to rising input and output prices. Inflation expectations have picked up in 2025, especially in some major economies. Inflation projections in 2025-26 have been revised slightly lower in EMDEs on account of weaker demand for traded goods, while being revised notably higher in advanced economies, primarily the United States.*

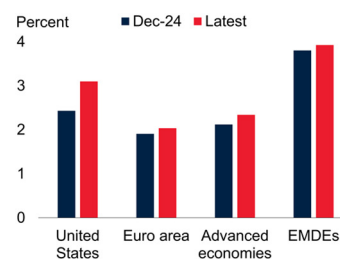
**A. Global headline CPI inflation**



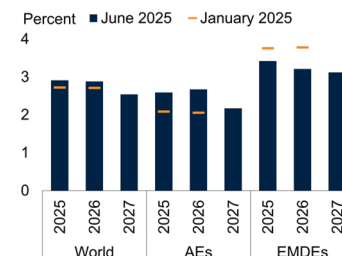
**B. Manufacturing PMIs subcomponents**



**C. CPI inflation expectations for 2025**



**D. Global CPI inflation projections**



Sources: Consensus Economics; Haver Analytics; Oxford Economics; World Bank.

Note: CPI = consumer price index; EMDEs = emerging market and developing economies; PMI = purchasing managers' index; ytd = year to date.

A. Aggregates are calculated as medians. Sample includes up to 36 advanced economies and 99 EMDEs. Last observation is April 2025.

B. Aggregated by source. PMI readings above (below) 50 indicate expansion (contraction). Last observation is April 2025.

C. Panel shows median inflation expectations. Latest survey is May 2025.

D. Model-based GDP-weighted projections of consumer price inflation using Oxford Economics' Global Economic Model. Sample includes 69 countries, out of which 35 are EMDEs, and excludes Argentina and República Bolivariana de Venezuela.

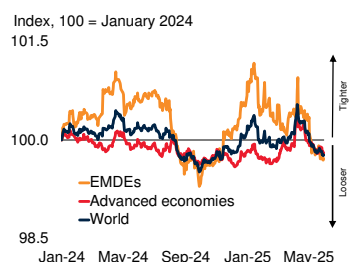
including in core government bond markets. Global equity markets plunged in early April, followed by a recovery driven by the postponement of some tariffs and the partial rollback of tariffs between the United States and China. Risk premia in U.S. equity and corporate credit markets, as gauged by cyclically adjusted equity earnings relative to the risk-free rate and high-yield spreads, have increased this year, albeit from very low levels (figure 1.6.B).

Monetary policy in the United States remains restrictive, with policy rates unchanged so far this

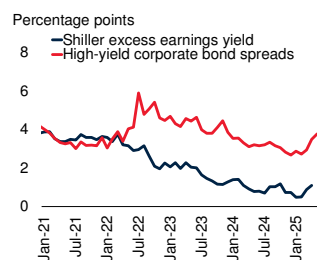
## FIGURE 1.6 Global financial developments

Global financial conditions have been tighter this year, on average, relative to late 2024 amid increased trade barriers, elevated trade policy uncertainty, and concerns of a slowdown in global growth. Risk premia in U.S. equity and high-yield bond markets have edged up, albeit from very low levels. Sovereign spreads have increased overall in EMDEs, although a spike in the spreads of countries exposed to higher U.S. tariffs largely unwound when tariffs were paused. A rise in borrowing costs would put pressure on vulnerable EMDEs with elevated levels of external debt and foreign-currency-denominated government debt, which have increased in recent years.

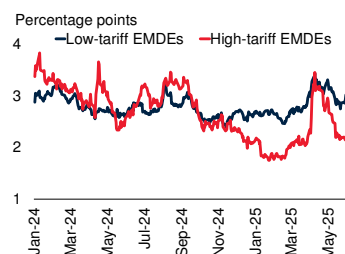
### A. Financial conditions index



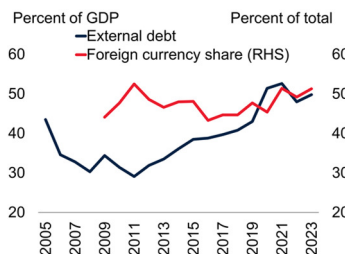
### B. Risk premia in the United States



### C. EMDE sovereign spreads, by announced U.S. tariff rate



### D. EMDE external debt and foreign-currency-denominated debt



Sources: Barclays Investment Bank; Bloomberg; Federal Reserve Bank of St. Louis; Goldman Sachs; J.P. Morgan; Kose et al. (2022); White House; World Bank.

Note: EMDEs = emerging market and developing economies.

A. Higher index values represent tighter financial conditions. Last observation is May 30, 2025.

B. "Shiller excess earnings yield" is the inverse of the cyclically adjusted price-to-earnings ratio minus the yield on 10-year U.S. Treasury inflation-protected securities. "High-yield corporate bond spreads" are measured by ICE BofA Option-Adjusted Spreads (OASs). These represent the calculated differences between a computed OAS index for all bonds rated below Baa/BBB and the spot U.S. Treasury curve. Last observation is April 2025 for the yield and May 2025 for the bond spreads.

C. Median spreads for 6 high-tariff EMDEs and 58 low-tariff EMDEs. "Low tariff" is defined as a tariff rate of up to 30 percent, as announced on April 2. Last observation is May 30, 2025.

D. External debt (percent of GDP) is the median of up to 137 EMDEs. Foreign-currency share of government debt is the median of up to 36 EMDEs. Last observation is 2023.

year and anticipated to decline only gradually, despite expectations of a slowdown in growth. This partly reflects the Federal Reserve's communications regarding the need to ensure that near-term inflationary pressures do not become persistent and long-term inflation expectations remain anchored. Meanwhile, policy rates have been lowered in the euro area since January, with further cuts expected by the end of the year. Even so, long-term yields have risen, reflecting fiscal announcements earlier in the year.

EMDE financial conditions have been somewhat tighter, on average, relative to late last year. Tariff announcements in April led to portfolio outflows along with broad-based declines in EMDE equity markets, although these moves largely reversed after the pauses in tariffs were announced. Most EMDE currencies have appreciated against the U.S. dollar since the start of the year, except for some economies with pre-existing domestic vulnerabilities. EMDE sovereign spreads have increased overall in recent months, jumping in April among economies that faced higher prospective trade barriers (figure 1.6.C). However, this surge proved short-lived, with spreads generally retreating when trade tensions partially de-escalated. Despite this volatility, from a longer-term perspective, spreads have remained at manageable levels in most economies.

Monetary policy in EMDEs has become more cautious, with many central banks easing or holding their policy rates unchanged as they assess the consequences for inflation and growth of higher trade barriers, elevated uncertainty, and potential shifts in investor appetite for EMDE financial assets. Policy rates may be kept higher for longer to ward off possible capital outflows and currency depreciations that could result from a renewed escalation of trade tensions. As a result, higher borrowing costs and weaker domestic currencies could put pressure on many EMDEs, especially those with weak credit ratings and large debt-refinancing burdens. External debt and the share of foreign-currency-denominated government debt in EMDEs have risen in recent years and are currently at elevated levels (figure 1.6.D).

## Major economies: Recent developments and outlook

### Advanced economies

In advanced economies, growth forecasts for 2025 have declined substantially since January, driven by downgrades in some of the world's largest economies. This reflects the shock dealt by the increases in trade barriers—even with the partial 90-day pause in U.S. tariff increases—and the associated policy uncertainty, financial volatility, and dampening effects on confidence. As a result,

growth is expected to remain below potential growth estimates over the forecast horizon in some advanced economies, including in the United States and the euro area.

In the **United States**, the announcement of trade policy changes did not provide much-needed clarity or reduce policy uncertainty, given the scale and scope of new tariffs, shifting timelines for their implementation, and fluid lists of exemptions. Furthermore, the implications of such large policy shifts, including potential steps that could be taken by other governments in response, remain highly unpredictable.

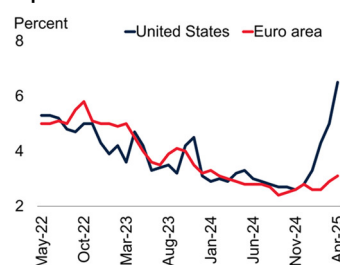
Prior to recent tariffs coming into effect, U.S. activity had already begun to slow in early 2025 as spending on imports surged at the expense of domestically produced goods. Private consumption growth has eased somewhat, despite a brief pickup toward the end of the first quarter in anticipation of new tariffs in categories such as autos. Consumer sentiment has fallen sharply amid declines in equity markets and risk appetite. In addition, U.S. consumer inflation expectations have risen markedly since the start of the year (figure 1.7.A). Treasury yields have increased, and corporate risk spreads have widened, while some corporate sectors faced the risk of disruption to tightly integrated supply chains, particularly in the U.S. auto industry. Policy uncertainty has remained high, with many firms highlighting concerns about the impact of trade policy changes on prices (Federal Reserve Board 2025). In tandem, the resilience in U.S. labor markets has continued to gradually diminish, with nonfarm payroll growth below the 2015-19 average and easing further, and other labor market indicators signaling reduced dynamism (figure 1.7.B).

The outlook for U.S. growth and inflation in 2025 has deteriorated relative to January forecasts. The rise in trade barriers, heightened uncertainty, and the spike in financial market volatility are set to weigh on private consumption, international trade, and investment. As a result, U.S. growth is expected to decelerate sharply in 2025, to 1.4 percent. Investment spending is projected to be particularly hard-hit following the earlier front-loading of imported investment goods. Going

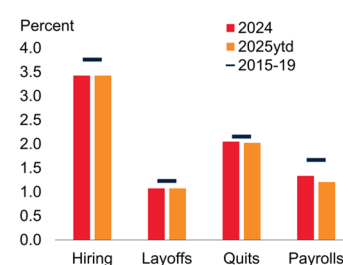
## FIGURE 1.7 Major economies: Recent developments and outlook

*U.S. consumer inflation expectations have risen markedly this year amid escalating trade tensions. Increased trade restrictions, weak confidence, and the resulting slowdown in aggregate demand are expected to contribute to reduced dynamism in the U.S. labor market. In the euro area, activity is expected to remain anemic, particularly given its deep integration in global value chains, which leaves the bloc highly exposed to adverse shifts in trade policy. In China, goods exports expanded in early 2025, reflecting continued front-loading, but are expected to slow as the effects of rising trade restrictions and the associated policy uncertainty are felt.*

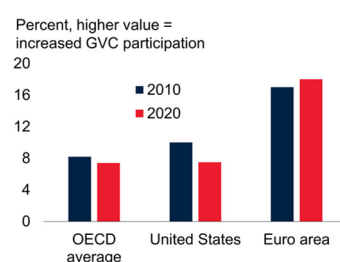
**A. 12-month-ahead inflation expectations**



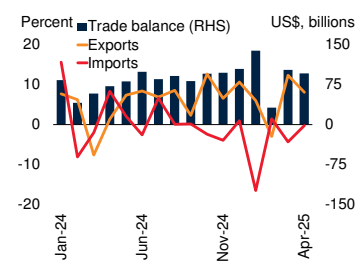
**B. U.S. labor market indicators**



**C. Global value chain exposure: Share of foreign value added in gross exports**



**D. Merchandise trade in China**



Sources: ECB; Federal Reserve Bank of St. Louis; Haver Analytics; Organisation of Economic Co-operation and Development (OECD); University of Michigan; World Bank.

A. Panel shows 12-month-ahead consumer inflation expectations from the Michigan Consumer Sentiment Survey and the European Central Bank (ECB) Consumer Expectations Survey. Last observation is April 2025.

B. Hiring, layoffs, and quits and separations are shown as percent of employment. Payrolls are shown as year-over-year percent change. Panel shows simple averages for the indicated periods. Last observation is April 2025. ytd = year to date.

C. Data measure the extent to which a country is a user of foreign inputs, which is considered as a measure of backward linkages in analyses of global value chains, as computed by the OECD. Euro area aggregates exclude intra-regional trade. Due to data constraints, euro area excludes Croatia.

D. Lines indicate year-on-year percent change in goods exports and imports in U.S. dollars. Last observation is April 2025.

forward, the supply of investment goods is anticipated to be disproportionately impacted by tariffs due to their high import content, at the same time as investment demand cools due to record-high uncertainty, the rise in financing costs, and reduced domestic and external demand. In 2026, growth is anticipated to edge up to 1.6 percent as the economy adjusts to higher trade barriers and policy uncertainty gradually declines.

Growth could prove to be stronger over the next few years if proposals to extend some expiring provisions of the Tax Cuts and Jobs Act and introduce other new fiscal measures clear the legislative process and are implemented. The resulting increase in the federal budget deficit would then be likely to broadly offset the budgetary impact of additional tariff-related revenues, with the latter estimated to reduce the primary deficit by \$2.5 trillion over 10 years (CBO 2025).

In the **euro area**, the recent surge in policy uncertainty and financial volatility, as well as increases in tariffs on the European Union (EU), are set to prolong the bloc's economic weakness, holding back a recovery in investment and trade. The EU is exposed to adverse shifts in trade policies and related uncertainty given its high openness to trade, with extra-EU trade in value terms placing the bloc as the second largest exporter and importer of global goods in 2022 (ECB 2019; Eurostat 2024). The bloc is also vulnerable to these external shocks owing to its deep integration into global value chains (figure 1.7.C; Gunnella and Quaglietti 2019). Together, these developments are set to further dent exports, compounding the losses in competitiveness and global export market shares stemming from high energy prices in the past few years.

Growth in the euro area is projected to slow in 2025, to 0.7 percent, and remain a touch below its trend of about 1 percent, averaging 0.9 percent over 2026-27. Substantial downgrades to growth forecasts relative to January projections reflect a combination of higher U.S. tariffs on imports from the EU, heightened uncertainty and financial market volatility, and weaker external demand, which are expected to more than offset newly legislated fiscal spending on defense and infrastructure—particularly in Germany. Although trade spillovers from higher spending in Germany to other euro area economies are expected to be positive, they are likely to be somewhat muted by the slow implementation of the package given Germany's capacity constraints.

The baseline is also predicated on additional policy rate cuts as inflation is expected to hover near the ECB's medium-term target. Although

possible price pressures could arise from increased trade barriers and additional government spending, they would likely be somewhat countered by weaker demand, softer commodity prices, and the potential redirection of exports from China to the EU (Attinasi et al. 2024; ECB 2025). The baseline assumptions include U.S. tariffs, including those on sectoral goods, as of late May and do not include any potential retaliatory trade measures.

In **Japan**, growth is expected to firm from an estimated 0.2 percent in 2024 to 0.7 percent in 2025, underpinned by a rebound in consumption and the reopening of automobile plants after longer-than-expected shutdowns last year. However, the growth outlook has been downgraded by 0.5 percentage point this year relative to previous projections, largely due to slowing external demand amid increased trade barriers and weaker-than-expected real wage growth owing to elevated food inflation. Over 2026-27, growth is forecast to average 0.8 percent, assuming a slow but continued recovery in consumer spending, as well as modest growth in capital investment, even if it is partly moderated by policy interest rate hikes as the Bank of Japan normalizes its policy stance.

## China

In China, the imposition of tariffs by the United States, the ensuing retaliation, and the subsequent partial rollback will have notable implications for the outlook of trade and broader economic activity. Before these policy actions, China's growth remained resilient in the first quarter of 2025, driven by a front-loading of exports ahead of the implementation of tariffs (figure 1.7.D). In contrast, imports were sluggish, held back by continued tepid domestic demand amid the property sector downturn, now approaching the four-year mark. Resulting soft underlying price pressures, as well as falling food and energy prices, led to decreasing consumer prices earlier in 2025. Producer prices also continued to fall, reflecting declining global commodity prices and competition among firms for market share.

To help strengthen domestic demand and counter headwinds from trade tensions and heightened

trade policy uncertainty, additional fiscal support was announced in early 2025, implying an estimated consolidated fiscal deficit of 8.1 percent of GDP in 2025, wider than the 6.5 percent of GDP in 2024.<sup>1</sup> These measures are aimed at further boosting infrastructure-related spending and, to a much lesser extent, consumer spending. More recently, additional monetary policy easing and financial measures targeted at several sectors were announced to support domestic economic activity.

Going forward, growth is forecast to slow from 5 percent in 2024 to 4.5 percent this year—in line with previous projections, as the impact of higher trade barriers and weaker external demand is assumed to be offset by the boost from additional fiscal policy support. Export growth is expected to slow as the impact of U.S. tariff increases materializes. A soft labor market and a subdued property sector are expected to weigh on consumption. However, announced additional fiscal support will help buoy non-property-related investment, consumption, and industrial activity. Growth is projected to slow to 4 percent in 2026 and edge down to 3.9 percent in 2027, as the growth of potential output decelerates, reflecting the effects of slowing productivity growth, an aging population, and high debt levels.

## Emerging market and developing economies

Against the backdrop of a more challenging external environment, EMDE growth is forecast to slow significantly in 2025, to 3.8 percent, with only a modest projected pickup in 2026-27. The expected rate of growth is well below pre-pandemic averages and the pace that is needed to create sufficient jobs to meet working-age population growth and make progress in closing large per capita income gaps with advanced economies. The deterioration in EMDE growth prospects is driven in large part by economies with a high degree of trade and investment openness. In these economies, large manufacturing sectors,

high global value chain participation, and reliance on global financial markets amplify the negative spillovers from the recent shocks to global trade and confidence and the sharp rises in uncertainty and financial market volatility. However, the softness in the EMDE outlook is anticipated to be broad-based, with growth expected to slow in nearly 60 percent of EMDEs in 2025. More generally, the capacity of many EMDEs to respond to negative shocks has diminished due to sharp pandemic-related increases in debt, elevated poverty rates, and waning official development assistance.

### Recent developments

Prior to the recent deterioration in the external environment this year, activity in EMDEs had generally steadied over 2024, with domestic demand supported by generally benign financial conditions and solid credit growth (figure 1.8.A). Although domestic activity indicators remained relatively resilient over the first quarter of 2025, the rapid rise in uncertainty and slowdown in external demand have begun to act as a drag on activity. Gauges of manufacturing activity, including headline manufacturing PMIs and goods trade indicators, have eased recently. Some trade-exposed EMDEs—such as Malaysia, Mexico, Romania, and Viet Nam—have seen the new export orders component of the manufacturing PMI weaken markedly since November amid increasing global trade policy uncertainty (figure 1.8.B).

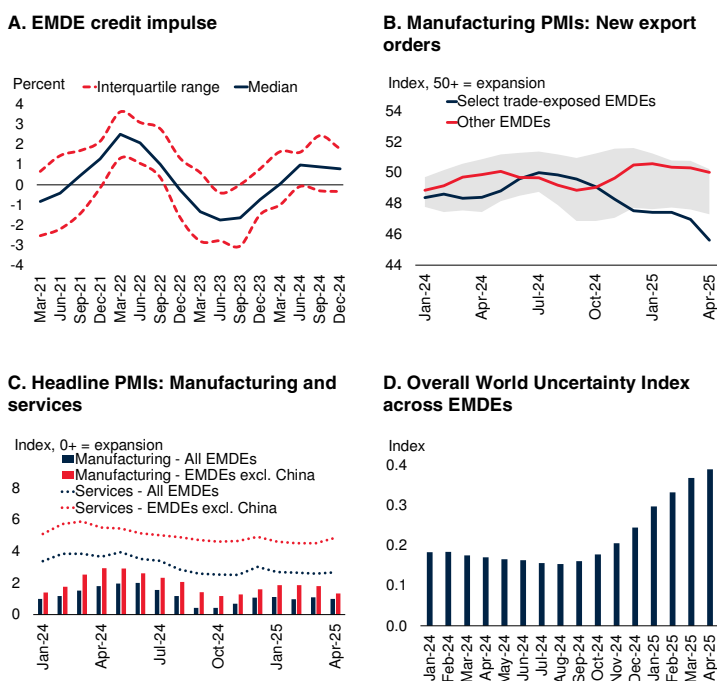
On the services side, PMIs have remained in expansionary territory but nonetheless have trended lower this year (figure 1.8.C). High-frequency consumption indicators also point to a similar dynamic, with both consumer confidence and retail sales losing some momentum in recent months. Nonetheless, the so-far generally resilient trends are expected to lose momentum amid the sharp rise in uncertainty following increases in trade restrictions and other policy shifts (figure 1.8.D).

Growth has continued to diverge across EMDEs so far in 2025, with a slower pace of activity in some commodity-exporting EMDEs and somewhat more solid conditions across other

<sup>1</sup> For China, the World Bank uses a definition of the consolidated fiscal balance that allows for comparisons across countries. See chapter 2 for details.

## FIGURE 1.8 Recent developments in emerging market and developing economies

Before the recent deterioration in the external environment, activity in EMDEs had been supported by solid credit growth, in line with earlier domestic and global monetary policy easing. More recently, some trade-exposed EMDEs have seen a marked decline in new export orders, while services activity and other high-frequency indicators have trended lower. Against the backdrop of a sharp rise in uncertainty, momentum across EMDEs is expected to ease further.



Sources: Ahir, Bloom, and Furceri (2022); Haver Analytics; World Bank.

Note: EMDEs = emerging market and developing economies; PMI = purchasing managers' index.

A. Sample includes up to 36 EMDEs. Last observation is December 2024.

B. Blue line shows a 3-month moving average for a sample of select trade-exposed EMDEs that includes Malaysia, Mexico, Romania and Viet Nam. Red line shows a 3-month moving average for a sample of 12 EMDEs. Last observation is April 2025. Shaded area indicates the interquartile range for all 16 EMDEs.

C. PMI readings above (below) zero indicate expansion (contraction). Monthly readings are centered on 50, the expansionary threshold. Last observation is April 2025.

D. Panel shows the 3-month moving average of the unweighted average of the country-specific measure of overall uncertainty based on the World Uncertainty Index (WUI). All indices have been computed by counting the frequency of the world uncertainty (or its variant) in EIU country reports. The indices are normalized by total number of words and rescaled by multiplying by 1,000. A higher number means higher uncertainty and vice versa. Sample includes 49 EMDEs. Last observation is April 2025.

economies. The weaker performance among the former was mostly concentrated in energy-exporting economies and related to softness in global energy demand; ongoing OPEC+ production cuts; notable declines in commodity prices amid rising trade tensions, which weighed on net exports, revenues, and investment; and new sanctions on some oil-exporting economies. Prior to the deterioration in the external environment, earlier activity readings had modestly surprised to

the upside in some large energy-exporting EMDEs—including Russian Federation, Saudi Arabia, and Nigeria—largely owing to domestic factors outside of the energy sector.

In commodity-importing EMDEs excluding China, activity had remained broadly steady before the sharp rise in trade tensions, supported by a pickup in private consumption and investment, with the latter benefiting from firm manufacturing activity. Despite overall solid performance, some economies have seen a material weakening in activity in recent quarters, largely reflecting an increase in uncertainty related to domestic developments or rising trade barriers.

In LICs, growth is estimated to have firmed to 4.6 percent in 2024, up from 2.8 percent a year earlier. The pickup in activity last year was driven mainly by major LICs facing fragile and conflict-affected situations (FCS)—including the Democratic Republic of Congo, where mining activity surprised on the upside, and in Ethiopia, where mining and agriculture output was better than expected. Such positive momentum hinged on tailwinds from commodity markets and favorable financing conditions prevailing in 2024, which may give way to headwinds as global growth and trade slow, commodity prices weaken, and uncertainty dampens risk appetite. Moreover, pervasive violence and political instability have resulted in persistently challenging economic and humanitarian situations, particularly in the Sahel region and its adjacent countries. Sudan has continued to experience a deep contraction related to ongoing violent conflict, which has also hampered activity in neighboring South Sudan, leading to a steeper-than-anticipated decline in output.

### EMDE outlook

Following the trade shocks that have rippled through the global economy, growth in EMDEs is forecast to slow to 3.8 percent in 2025, then edge up to an average of 3.9 percent over 2026-27, about 1.2 percentage points below the 2010-19 average (figure 1.9.A). In large part, the aggregate EMDE profile continues to be shaped by China's outlook, especially as the ongoing structural deceleration is exacerbated by the escalation in

trade tensions. Nevertheless, the projected slowdown in EMDE growth this year is anticipated to be broad-based, affecting nearly 60 percent of EMDEs.

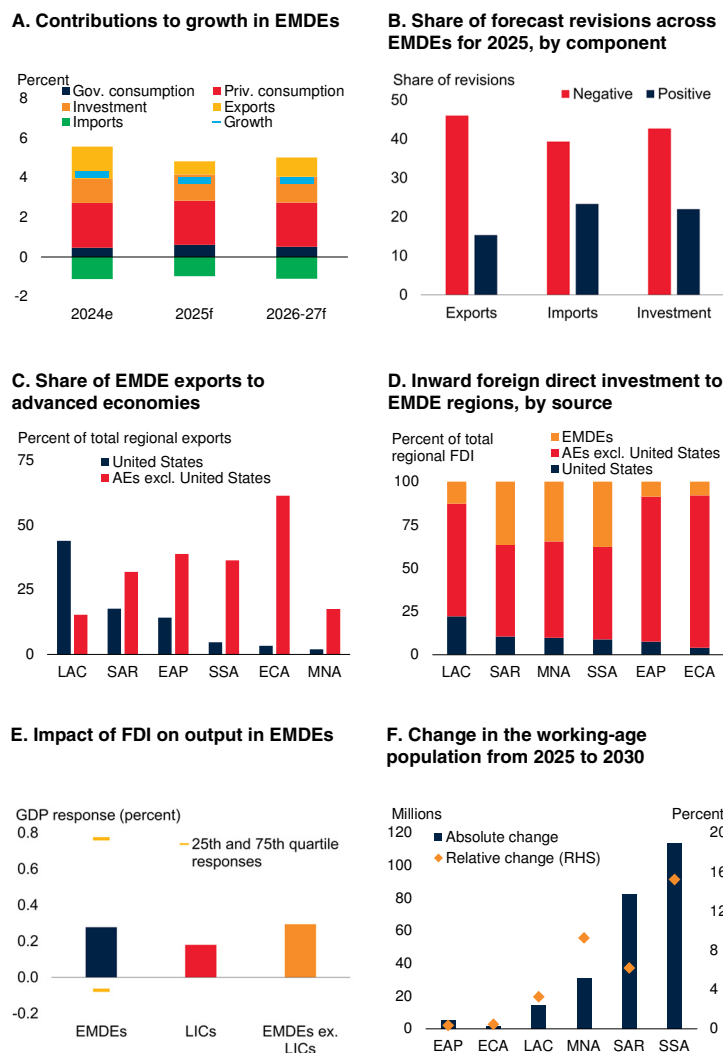
Excluding China, growth in EMDEs is forecast to decelerate from an estimated 3.6 percent in 2024 to 3.4 percent in 2025 and then pick up to about 3.9 percent over 2026-27. EMDE growth this year and next is projected to be notably weaker than expected in January. This reflects a combination of adverse policy shifts at the global level announced since the beginning of 2025—and the limited space to respond to such headwinds in most EMDEs—and weaker external demand related to slowing growth in advanced economies, as well as lower prices for some commodities. These global shocks are propagating to EMDEs through trade, investment, and confidence channels, all of which are being amplified by record-high global policy uncertainty and financial market volatility.

The ability of EMDE governments to respond to these global shocks is constrained by limited fiscal policy space amid elevated debt levels and the tightening of financial conditions. As such, fiscal policy is expected to either dampen or have a neutral effect on growth in about three-quarters of EMDEs, while financial conditions across EMDEs have tightened somewhat since the start of 2025 more broadly.

Over the forecast horizon, domestic demand is expected to continue to anchor growth, despite the substantial downgrade to its outlook since January. Among EMDEs excluding China, investment growth is envisaged to substantially weaken in 2025, with forecasts for investment and trade downgraded relative to January owing to declining business confidence and rising uncertainty—particularly in some trade-exposed EMDEs (figure 1.9.B). The slowdown in investment this year is expected to be broad-based, affecting nearly 60 percent of EMDEs. Private consumption is anticipated to be the principal driver of domestic demand, but it is also expected to decelerate steeply in 2025, in line with declining consumer confidence and rising uncertainty. Over 2026-27, consumption growth

## FIGURE 1.9 Outlook for emerging market and developing economies

EMDE growth is expected to slow this year, with forecasts for trade and investment revised down markedly across many economies. The deterioration of the external environment and ongoing trade policy uncertainty is anticipated to weigh materially on advanced-economy demand for EMDE exports, as well as foreign direct investment (FDI) flows to EMDEs. Against the backdrop of elevated uncertainty and growing protectionism, FDI—which has historically served as a key long-term driver of growth across EMDEs—will likely weaken. This could compound the challenge many EMDEs face to ensure the creation of sufficient employment for swiftly expanding working-age populations.



Sources: IMF Coordinated Direct Investment Survey (IMF-CDIS) (database); UN Population Prospects (database); WITS (database); World Bank.

Note: e = estimate; f = forecast. AEs = advanced economies; EAP = East Asia and Pacific; ECA = Europe and Central Asia; FDI = foreign direct investment; LAC = Latin America and the Caribbean; LICs = low-income countries; MNA = Middle East and North Africa; PVAR = panel vector autoregression; SAR = South Asia; SSA = Sub-Saharan Africa.

A. Discrepancies between GDP growth and the sum of its components reflect inventories and residuals.

B. Forecast revisions relative to the January 2025 *Global Economic Prospects* for up to 150 EMDEs.

C.D. Data is for 2023. Sample includes 169 economies for panel C and 189 for panel D.

E. Impact after 3 years of a 10-percent increase in net FDI inflows on real GDP level (in percent), based on heterogeneous PVAR model estimations. Bars show average country group responses. Horizontal lines show impact in countries at the 75th percentile and 25th percentile responses of GDP to FDI inflows. Sample includes 74 EMDEs, 11 of which are LICs.

F. Panel shows the change in the working-age population over 2025-30.

in EMDEs excluding China is envisioned to remain subdued, as real wage and productivity growth weaken amid adverse policy shifts impacting trade and investment flows to EMDEs, while idiosyncratic factors in several large economies, such as India and Russia, see consumption growth moderate.

In many EMDEs, net exports are expected to be dampened by weaker external demand from key trading partners, especially given tight trade linkages with advanced economies in some EMDE regions (figure 1.9.C; box 1.1). In parallel, ongoing trade policy uncertainty and concern over market access to advanced economies are expected to weigh on foreign investment flows from key trading partners to EMDEs (figures 1.9.D).

With the rise in trade barriers and elevated uncertainty, the recovery in EMDEs from the shocks of the past five years remains incomplete. In EMDEs excluding China, the level of output is anticipated to remain about 4 percent below the pre-pandemic trajectory in 2027. Indeed, if growth were to continue at the pace forecast for 2027, it would take about two decades for output to return to the pre-pandemic path.

Against the backdrop of another delay in the post-pandemic recovery across EMDEs, uncertainty and risks continue to mount, with trade growth in EMDEs set to come under further pressure after weak performance in recent years. These developments will likely place further strain on global value chains and slow the pace of investment—including foreign direct investment, which has been a key driver of economic growth in many EMDEs (figure 1.9.E). Indeed, participation in global value chains linked to advanced economies remains substantial in some EMDE regions, which has historically fostered productivity growth and technological adoption across EMDEs—but also has the potential to amplify the effects of trade fragmentation (World Bank 2021).

Over the longer run, a major jobs challenge—ensuring the creation of sufficient employment opportunities for rapidly growing working-age populations—is looming in many EMDEs, including in the poorest two regions—SSA and

SAR—and MNA (figure 1.9.F). Taken together, SSA, SAR, and MNA are envisaged to add about 1 billion people to their working-age populations between 2025 and 2050. This increase is historically large relative to previous episodes of rapid working-age population expansion, in both numerical and percentage terms. Most of these additional people will need jobs. In almost all SSA countries, the expected average annual growth in the working-age population between 2025 and 2030 is set to exceed the average annual employment growth seen over 2010-19. Absent sufficient new job creation, various economic, social, and political pressures could rise in countries with fast-growing populations.

### LICs outlook

With the backdrop of deteriorating global economic prospects, projected growth across LICs has been downgraded by 0.4 percentage point in 2025, to 5.3 percent. Although this represents an uptick in growth from last year, the rebound hinges on a recovery that is already being hindered by violent conflict in parts of SSA, particularly Sudan (box 1.2).

Growth in LICs is expected to rise to 6.1 percent over 2026-27. Yet the LICs' outlook remains highly uncertain and depends on the evolving circumstances in economies marred by conflict, where substantial improvements in security situations will need to take place. Furthermore, the forecast assumes that no new conflicts or debt crises in LICs emerge, and that inflation continues to broadly abate. Moreover, given LICs' high dependence on commodity exports, weakening external demand and lower global commodity prices could still dampen growth and government revenues in many economies.

Notwithstanding the expected pickup in growth, the level of output across LICs is projected to remain about 3.7 percent below the pre-pandemic trajectory by 2027. Growth prospects of non-FCS economies have deteriorated materially, while the near-term outlook for FCS LICs has been marginally revised up from last January. Nevertheless, many LICs continue to face severe challenges related to conflict, including the destruction of productive capacity and significant

### BOX 1.1 Regional perspectives: Outlook and risks

*All emerging market and developing economy (EMDE) regions face a challenging outlook amid the rise in global trade tensions and heightened uncertainty. In 2025, growth is projected to slow in East Asia and Pacific (EAP) as well as in Europe and Central Asia (ECA)—both regions that are highly reliant on global trade—and, to a lesser extent, in South Asia (SAR). In Latin America and the Caribbean (LAC), growth is projected to be the lowest among EMDE regions over the forecast horizon, as activity is held back by high trade barriers and long-standing structural weaknesses. In regions with a large number of commodity exporters, including in the Middle East and North Africa (MNA) and Sub-Saharan Africa (SSA), growth is anticipated to face drags from the weakening outlook for external commodity demand. Against the backdrop of a deteriorating global environment, growth forecasts for 2025 have been downgraded in all EMDE regions relative to January projections. The looming jobs challenge faced by EMDEs could intensify already weak trends in per capita income catch-up and extreme poverty reduction. Risks to the outlook remain tilted to the downside and stem especially from additional increases in trade restrictions and policy uncertainty, as well as the further weakening in external demand and heightened financial volatility. To varying degrees, EMDE regions also face downside risks from declining global risk appetite, worsening or increasing conflict and violence, and more frequent natural disasters.*

#### Introduction

Emerging market and developing economy (EMDE) regions are being buffeted by a variety of adverse factors—in particular, the wide-ranging repercussions of a rise in trade tensions and the ensuing increase in global policy uncertainty, which are affecting EMDEs through trade, commodity, financial, and confidence channels. In addition to the increase in trade barriers and uncertainty and the subsequent weakening in external demand, the projected deceleration in growth is also related to idiosyncratic factors across regions, including headwinds from elevated levels of violence and conflict, heightened domestic political uncertainty, and the impact of recent natural disasters.

Growth is projected to slow in most EMDE regions this year, particularly in the trade-reliant economies of East Asia and Pacific (EAP) and Europe and Central Asia (ECA), and to a lesser extent in South Asia (SAR). In Latin America and the Caribbean (LAC), growth is expected to be the lowest among the EMDE regions over 2025-27, as structural weaknesses are amplified by softening activity in the United States and China via tight linkages through trade, financial flows (including remittances), and commodity markets (in the case of China). Although growth is set to edge up in the Middle East and North Africa (MNA) and Sub-Saharan Africa (SSA) in 2025, this follows soft activity over the past couple of years, partly related to conflict and, in some economies, oil production cuts. Furthermore, lower global commodity prices are set to weigh on

activity and government revenues in some commodity exporters in MNA and SSA, as well as in LAC and ECA. As a result of this weak outlook, prospects for spurring the job creation that is needed to lift incomes and reduce poverty are subdued.

In this context, this box considers two questions:

- What are the cross-regional differences in the outlook for growth?
- What are the key risks to the outlook for EMDE regions?

#### Outlook

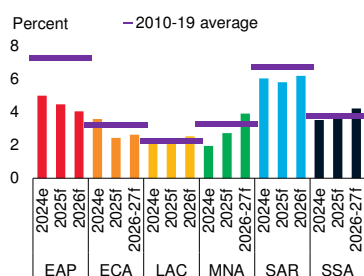
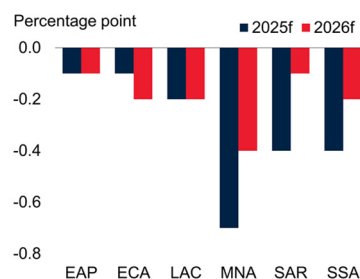
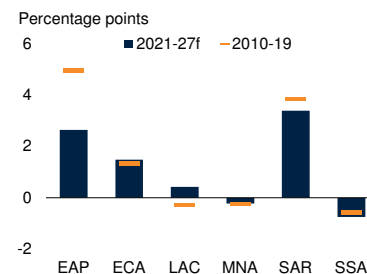
While the economic outlook varies across EMDE regions, it remains challenging for all amid the deterioration in the global economic environment (figure B1.1.1.A; chapter 1). Increases in global trade barriers and uncertainty, as well as the subsequent projected weakening in external demand, have contributed to downgrades to growth forecasts for this year and next in most EMDE regions (figure B1.1.1.B). In some trade-exposed regions, the growth slowdown in 2025 relative to last year is expected to be broad-based, affecting 78 percent of EAP economies and 73 percent of ECA economies. In many commodity-exporting regions—including ECA, LAC, MNA, and SSA—activity and fiscal revenues in some large commodity exporters are expected to come under pressure this year and next from softening global commodity demand. Among the regions, aggregate growth in LAC is expected to be the lowest over 2025-27, followed by ECA, as the weakening in the external environment amplifies domestic challenges and exacerbates the deceleration in growth.

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*Note:* This box was prepared by Samuel Hill and Collette Wheeler.

**BOX 1.1 Regional perspectives: Outlook and risks (continued)****FIGURE B1.1.1 Regional outlooks**

Growth in all EMDE regions is facing considerable headwinds amid a notable deterioration in the external environment, resulting in weaker growth projections this year relative to pre-pandemic trends and previous forecasts. For most regions, increased trade barriers and heightened policy uncertainty at the global level—including the impacts on external demand, financial and commodity markets, and broader sentiment—are offsetting tailwinds to domestic demand from moderating inflation and, in some cases, macroeconomic policy support. The pace of per capita income catch-up with advanced economies is projected to be slower in many EMDE regions than in 2010-19, with income gaps widening in some—notably in Sub-Saharan Africa, the poorest region. The rapid deterioration in the external environment is likely to further weigh on progress in per capita income catchup.

**A. Output growth****B. Growth forecast revisions****C. Differences between per capita income growth in EMDE regions and advanced economies**

Source: World Bank.

Note: e = estimate; f = forecast. EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging market and developing economies; LAC = Latin America and the Caribbean; MNA = Middle East and North Africa; SAR = South Asia; SSA = Sub-Saharan Africa.

A. Aggregated growth rates are calculated using GDP weights at average 2000-18 prices and market exchange rates. "2010-19" refers to period averages of regional growth rates. Data for 2025, 2026, and 2027 are World Bank forecasts.

B. Revisions reflect differences in forecasts presented in the January 2025 edition of the *Global Economic Prospects* report and the current forecasts. Data for 2025 and 2026 are World Bank forecasts.

C. Bars and dashes represent annual average GDP per capita growth in EMDE regions minus the annual average GDP per capita growth in advanced economies, expressed in percentage points.

In EAP, the slowdown this year largely reflects tight trade linkages—both globally and within the region, especially with China, where macroeconomic policy support is expected to counter the adverse impact of recent increases in trade tensions with the United States. In some EAP economies, including Myanmar, Thailand, and Vanuatu, activity has been disrupted by powerful earthquakes in recent months. In ECA, although the deceleration in growth is broad-based, in tandem with the projected weakening of euro area growth—one of ECA's largest export markets—it also reflects the slowdown in activity in the Russian Federation amid the lagged effects of monetary policy tightening.

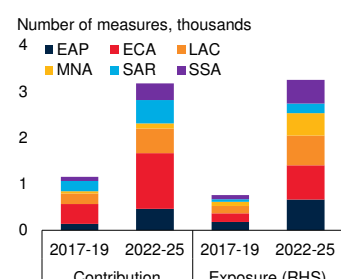
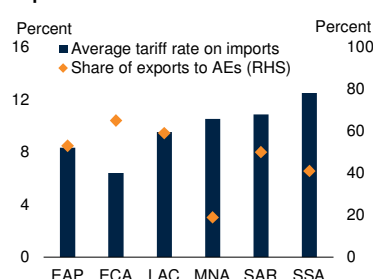
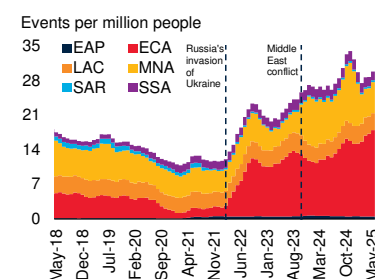
In LAC, although growth is expected to remain at the same pace in 2025 as in 2024, activity in many economies is likely to be impacted by the recent rise in trade barriers and policy uncertainty. Mexico will be

particularly affected, largely through its high integration with the United States via goods' trade—particularly the automotive sector. Other LAC economies, particularly those in Central America and the Caribbean, will also be affected through trade, investment, and remittance flows. These drags on LAC's growth are expected to offset the rebound in Argentina following two years of recession.

In contrast to most other regions, growth is forecast to pick up this year in MNA as activity in oil exporters benefits from rising oil production amid the phase-out of OPEC+ oil production cuts. This improvement is expected to counter the adverse effects of weakening external demand and lower oil prices. Growth is also contingent on expanding activity in MNA's oil importers, assuming that armed conflicts in the region stabilize and inflationary pressures ease. Although growth in SAR is projected to remain the fastest among

**BOX 1.1 Regional perspectives: Outlook and risks (continued)****FIGURE B1.1.2 Regional risks**

Additional increases in global trade barriers and policy uncertainty could further weaken activity in many EMDE regions, particularly in those with tight trade linkages to advanced economies. Import tariffs, which were already elevated in EMDE regions prior to this year, could rise if EMDEs undertake retaliatory measures in response to recent increases in trade restrictions. Heightened conflict and its fallout continue to pose a major risk to activity in all regions, particularly in ECA, MNA, and SSA.

**A. New trade-distorting policy measures****B. Tariff rates on imports into EMDE regions and share of EMDE regional exports to advanced economies****C. Conflicts**

Sources: ACLED (database); WDI (database); World Bank.

Note: AEs = advanced economies; EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging market and developing economies; LAC = Latin America and the Caribbean; MNA = Middle East and North Africa; RHS = right-hand scale; SAR = South Asia; SSA = Sub-Saharan Africa.

A. The number of harmful trade measures implemented by and affecting different EMDE regions. These measures include the sum of "Amber" and "Red" measures classified as harmful in the Global Trade Alert database. Each measure may be implemented by, and target, multiple countries. Data are adjusted for reporting lags as of June 4, 2025.

B. Bars show the most favored nation tariff rate for each EMDE region, based on unweighted average across all products, 2022 or the latest available. Markers show, for EMDE regions, the share of total exports that are directed to advanced economies. Export data refer to 2023. Sample includes 106 EMDEs for exports data.

C. Stacked bars show three-month moving averages of the number of reported individual conflict events per million people in each of the six EMDE regions. Major conflicts involve multiple conflict events, including battles, explosions, riots, and violence against civilians. The date of Russia's invasion of Ukraine is February 24, 2022. The date of the conflict in the Middle East is October 7, 2023. Last observation is May 2025.

the regions, the rise in global trade barriers and elevated uncertainty is set to keep growth below the pre-pandemic average. In some SAR economies, the effect from heightened global uncertainty is expected to be somewhat countered by reduced domestic political uncertainty, which should help support confidence and investment. In SSA, growth is forecast to edge up this year, but the outlook remains highly uncertain and depends on an easing in inflation and de-escalation of conflict in some fragile and conflict-affected situations (FCS; box 1.2). However, lower global commodity prices are expected to weigh on regional activity and revenues. Moreover, elevated government debt, still-high interest rates, and rising debt-servicing costs have further narrowed fiscal space, prompting fiscal consolidation efforts in many countries, while financing needs remain high as international development assistance is cut back.

Inflation has diverged somewhat across EMDE regions so far in 2025. In ECA, inflation edged up in late 2024

and early 2025 on the back of food price increases and robust wage growth in some cases. More recently, it has moderated somewhat alongside easing energy prices in some economies but remains above 4 percent in most ECA subregions. In LAC, price pressures have mostly subsided, with inflation above central bank target ranges in only a couple of large economies. The disinflation process in SSA has stalled, largely owing to rising food prices. Conversely, inflation has softened in MNA and SAR but has remained high in some notable cases. Meanwhile, inflation mostly declined across EAP given falling commodity prices. On average for 2025, inflation is generally expected to remain stable or decline modestly across regions, supported by softening energy prices.

The outlook for trade in all EMDE regions remains challenging due to elevated global policy uncertainty, ratcheting trade tensions between major economies, and an expected slowdown in external demand this year. Although some EMDEs benefited from the front-

**BOX 1.1 Regional perspectives: Outlook and risks (continued)**

loading of exports ahead of anticipated tariffs, additional uncertainty and restrictions are set to dampen investment and dent global value chains, leading to downward revisions to trade growth forecasts for this year in nearly every region. With global tourism near pre-pandemic levels, tailwinds to service exports from the recovery in inbound tourists have also faded. Trade growth is projected to slow markedly in EAP and LAC and, to a lesser extent, in SSA; meanwhile, it is expected to pick up in MNA as oil production cuts unwind, though this is curbed somewhat by weaker external demand. Trade growth in SAR is projected to firm, as robust domestic demand in India supports an improvement in imports.

Investment growth slowed across most regions last year amid high interest rates, subdued global manufacturing and trade activity, and idiosyncratic drivers, including lower extractive production or conflict. Investment growth is anticipated to slow this year in MNA, SAR, and SSA, and remain subdued in ECA and LAC due to the rise in global policy uncertainty and weaker confidence. In EAP, firming investment growth largely reflects additional fiscal support in China; excluding China, it is anticipated to soften owing to global trends. In SAR, investment growth is anticipated firm over 2026-27, partly because of reduced domestic political uncertainty and monetary policy easing in several economies, helping to counter the rise in global uncertainty. In all, most regions are expected to experience weaker investment growth this year relative to their 2010-19 averages.

Private consumption growth, while projected to moderate in many regions, will still underpin activity, assuming that inflation moderates and supports real incomes. However, the outlook for private consumption is expected to be dampened by the rise in global uncertainty and, in some cases, modest fiscal consolidation. In a few regions, private consumption is anticipated to be further contained amid persistent underlying price pressures, which have kept inflation close to the upper end of central bank target ranges in some countries, limiting central banks' scope to reduce policy rates. Central banks many across regions continue to make headway on taming inflation but remain watchful for a resurgence in inflation and the possibility of financial instability stoked by further global policy uncertainty. Uncertainty surrounding the

pace and extent of monetary policy easing in some major economies is adding to caution and restricting room to maneuver.

The stance of fiscal policy is expected to vary across regions and thus has a mixed influence on activity. In LAC, SAR, and SSA, needed—albeit gradual—fiscal consolidation will impose some headwinds to growth but should help address fiscal deficits and stabilize public debt if these efforts are sustained. In ECA, fiscal policy is expected to be somewhat supportive of activity, with deficits set to increase further this year, partly due to rising military expenditures, before a gradual shift toward consolidation. Meanwhile, in EAP, increased government spending is expected to provide notable support to demand in China and, to a lesser extent, in Thailand; in many other large EAP economies, fiscal policy support—including from social spending programs and public investment—is anticipated to be more modest and have a relatively neutral impact on growth.

Over the forecast horizon, catch-up toward advanced-economy per capita GDP levels is anticipated to be limited, particularly in MNA and SSA (figure B1.1.1.C). Absent the sufficient creation of new jobs, EMDE regions with fast-growing populations face especially subdued prospects for per capita income catch-up with advanced economies and poverty reduction (Chrimes, Kose, and Stamm forthcoming). This jobs challenge is concentrated in SSA—which accounts for two-thirds of the world's population living in extreme poverty—but it also looms large in several economies in SAR and MNA. In these regions, job growth has not met the pace of growth of the working-age population in recent years, and this trend of subdued job growth is set to intensify amid the projected slowdown in long-term growth in many cases (Kose and Ohnsorge 2024). For example, in almost all SSA economies, the expected average annual growth in the working-age population between 2025 and 2030 exceeds the average annual employment growth seen over 2010-19. Most countries that face a surge in their working-age populations are not well-placed to cope with the challenge due to limited fiscal space, weak government capacity, pervasive informality, high levels of low-productivity employment, widespread economic inactivity (such as high youth unemployment), and heightened levels of conflict or extreme poverty.

## BOX 1.1 Regional perspectives: Outlook and risks (*continued*)

### Risks

Risks to the outlook remain tilted to the downside across all EMDE regions. Persistently elevated or renewed policy uncertainty and additional trade tensions at the global level pose significant risks, especially for trade-exposed regions with large manufacturing sectors. Further risks relate to a marked deterioration in global risk appetite, which could dampen capital flows to EMDEs, as well as increased conflict and rising frequency and severity of natural disasters.

Global policy uncertainty has increased markedly in recent months and could be persistent, posing a substantial downside risk to all EMDE regions. Abrupt policy changes, particularly relating to trade, could again unnerve financial markets and cause firms to hold off committing to investments or shelve them completely. Regions more dependent on investment-led growth, particularly where it is tied to trade-intensive production, are especially exposed to the cooling effects of heightened policy uncertainty. This includes EAP and ECA, and to a lesser extent LAC, MNA, SAR, and SSA.

A substantial rise in global trade barriers has affected EMDE regions in recent years, and the imposition of new tariffs earlier this year adds to these earlier increases (figure B1.1.2.A). Additional trade policy restrictions beyond those implemented by late May could negatively impact all EMDE regions through various channels. Beyond worsening global trade fragmentation, additional trade barriers could weaken trade growth, suppress economic activity, drive up prices, and reduce purchasing power, causing real wages to decline. Regions could suffer directly if their exports face new restrictive trade measures, and indirectly if external demand weakens owing to slower growth in key trading partners or if mounting policy uncertainty dents investment. Export-reliant regions with substantial manufacturing bases, such as EAP, ECA, and, to a lesser extent, LAC, are particularly vulnerable to the adverse

effects of heightened protectionism and supply chain reorientation. If taken by EMDEs, retaliatory measures could ramp up import tariffs in EMDE regions, which were already high (figure B1.1.2.B). This would magnify risks related to trade and inflation.

Worsening policy uncertainty could also trigger a marked erosion in global risk appetite, which could reduce capital flows to EMDE regions, push up borrowing costs, and lead to currency depreciation and further inflationary pressures. Regions with a preponderance of less-creditworthy borrowers, as well as high levels of external debt with elevated exposure to foreign currency or shorter maturities, are vulnerable to sudden adverse shifts in market sentiment and external financing. This could particularly affect LAC and SSA, but also several economies in ECA, MNA, and SAR.

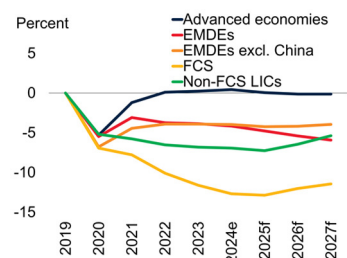
All regions continue to experience varying degrees of violence, including from high insecurity, and conflict (figure B1.1.2.C). A key downside risk to growth is the possibility of conflicts flaring and broadening, especially given that baseline assumptions in several regions, especially in MNA and SSA, hinge on a de-escalation in violence and conflict (chapter 2). Given the loss of life and large economic losses caused by armed conflict, this could substantially set back growth and the catch-up of per capita income with advanced economies. Regions where major armed conflicts continue to be centered, including ECA, MNA, and SSA, are particularly vulnerable to the effects of escalating instability and violence.

Natural disasters—including those related to climate change, which are becoming more frequent and severe—pose further downside risks to all regions. These can amplify other challenges, notably food insecurity and population displacement, particularly in regions with concentrations of fragile and conflict affected situations, notably MNA and SSA. The ability to respond to such events is hampered by narrow fiscal space, still elevated borrowing costs, and weak institutional capacity in some cases.

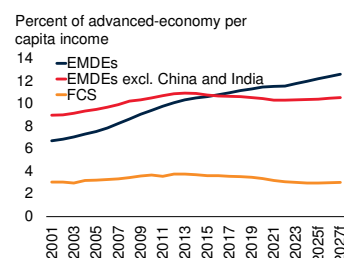
## FIGURE 1.10 Per capita income growth

Relative to pre-pandemic trends, per capita income losses in EMDEs are expected to remain large. Excluding China and India, income levels relative to advanced economies are envisaged to remain stagnant. Conflict-related casualties have risen since the 2000s, with conflict having become an increasingly important driver of per capita output losses across FCS. Following steady progress before the pandemic, the extreme poverty rate in EMDEs excluding China and India, and especially LICs, remains higher than in 2019, driven in large part by rising poverty across FCS.

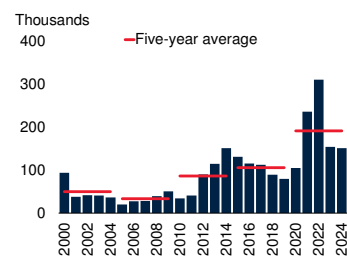
### A. Per capita output losses relative to pre-pandemic trends



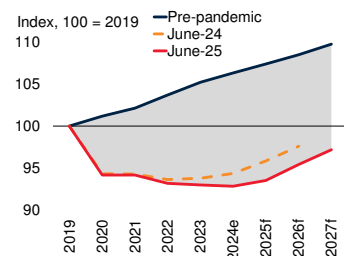
### B. EMDE per capita GDP relative to advanced economies



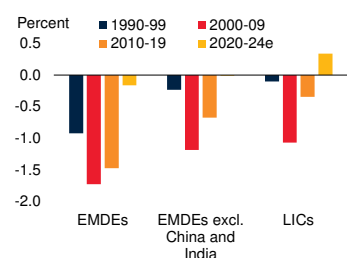
### C. Conflict-related fatalities



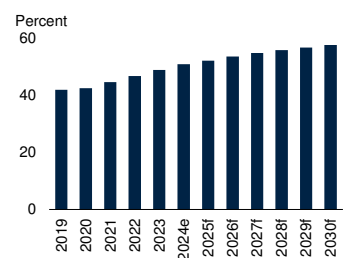
### D. Per capita income forecast revisions and output losses among FCS economies



### E. Average annual reduction in extreme poverty rates



### F. Share of global extreme poor living in FCS economies



Sources: Mahler, Yonzan, and Lakner (2022); UN World Population Prospects; Uppsala Conflict Data Program; World Bank Poverty and Inequality Platform (database); World Bank.

Note: e = estimate; f = forecast. EMDEs = emerging market and developing economies; FCS = fragile and conflict-affected situations; LICs = low-income countries; PPP = purchasing power parity. FCS country group based on current World Bank FCS classification.

A.C. Sample includes 179 economies, of which 37 are advanced economies and 142 are EMDEs.

A.D. For 2023 and beyond, the pre-pandemic trend is the January 2020 baseline projection extended using the projected growth rate for 2022.

A. Panel shows the percent deviation between the latest forecast and the January 2020 *Global Economic Prospects* report.

C. Bars show the number of fatalities per year; lines show the simple average for the period indicated. Last observation is December 2024. Sample includes up to 82 economies. The Uppsala Conflict Data Program defines a conflict "event" as an incident in which armed force was used by an organized actor against another organized actor, or against civilians, resulting in at least one direct death.

D. "June-24" and "June-25" refer to the forecasts presented in the corresponding editions of the *Global Economic Prospects* report. For 2023 and beyond, the pre-pandemic trend is the January 2020 baseline projection extended using the projected growth rate for 2022. Shaded area indicates the output loss since 2019.

E.F. "Extreme poverty" is defined as living on less than \$3 per day in 2021 PPP. Estimates after 2023 are nowcasts. Sample includes 192 countries, of which 39 are currently classified as FCS economies.

population displacement, with adverse effects on poverty reduction efforts (Wu et al. 2024). Severely constrained fiscal space, high levels of indebtedness, slow progress in debt restructuring, and limited access to new external financing continue to pose headwinds to the outlook. Progress in poverty reduction, conflict prevention, infant mortality, and institutional capacity may be further damaged as major international donors reduce their support to LICs, and especially to FCS.

## Per capita income growth

Per capita GDP in many EMDEs is on a trajectory that implies a very slow pace of convergence with advanced-economy incomes, with the recent deterioration in external conditions hindering progress. This comes on top of an incomplete recovery from the pandemic, combined with an escalation of conflict in some economies, all of which have slowed the pace of poverty reduction and hampered per capita income catch-up. Per capita income growth in EMDEs over 2025-27 is projected to be 2.9 percent—about 1.1 percentage point below its 2000-19 average. Excluding China and India, both key drivers of income convergence over the forecast horizon, per capita income growth is expected to be even slower, at 1.8 percent over 2025-27. Across numerous LICs and FCS—many of which have large gaps in per capita income with other EMDEs and advanced economies—per capita income growth is projected to be lower still, contributing to slowing progress in poverty reduction. Moreover, absent the rapid economic growth and supportive policies needed to spur job creation, many EMDEs will continue to struggle to lift incomes and thus reduce poverty in the coming years.

In level terms, per capita income in EMDEs is estimated to remain nearly 5 percent below pre-pandemic trends in 2025, compared to marginally above for advanced economies, with the gap on track to widen through 2027 (figure 1.10.A). Indeed, most EMDEs are in a notably worse position in terms of output losses relative to the pre-pandemic trend, compared to advanced economies, given their weaker initial recoveries. This has been exacerbated further by the

## BOX 1.2 Low-income countries: Recent developments and outlook

*In low-income countries (LICs), growth is projected to rise to 5.3 percent in 2025 and average 6.1 percent in 2026-27, yet this outlook hinges on a de-escalation of conflict in some countries and a moderation in inflation. Crucially, the weaker global environment has led to a significant downward revision of LICs' growth this year. Although per capita income is set to increase by an average of 3 percent annually during the forecast period, this pace remains too weak to fully recover pandemic-related losses or foster the rapid expansion of jobs needed to lift incomes and reduce extreme poverty. In this context, extreme poverty will remain high, exacerbated in many cases by the effects of violent conflict. A weaker global environment amid the rise in trade tensions and uncertainty weighs on the outlook for LICs, especially those that rely heavily on commodity exports. Reduced fiscal space, arising partly from increased debt-servicing costs and exacerbated by falling donor support, has heightened the challenges many countries face in addressing their development needs and confronting recent global shocks. Risks to the growth outlook are tilted to the downside. They include intensifying insecurity and violent conflict, which could result in negative spillovers for many LICs, including increased food insecurity. Other downside risks include weaker external demand due to heightened trade tensions and related policy uncertainty, more persistent inflation, increased risk of government debt distress, further withdrawals of donor support, and more frequent or intense extreme weather events.*

### Introduction

Last year, output in low-income countries (LICs) grew by an estimated 4.6 percent—still below the 2010-19 average of 5 percent. While growth in LICs is expected to strengthen further, to 5.3 percent in 2025 and to an average of 6.1 percent in 2026-27, such a forecast is contingent on substantial improvements in security in several LICs in fragile and conflict situations (FCS; figure B1.2.1.A). Notwithstanding such a rebound, the projections for this year represent a significant downgrade in LICs' growth prospects compared to January forecasts, in line with the deterioration of the global economic environment. Indeed, at these projected rates, per capita income growth will remain too weak to fully unwind losses in per capita income from the pandemic and spur the rapid growth in jobs needed to lift millions from extreme poverty.

In many LICs, the outlook is clouded due to the worsening in the external environment—including rising trade tensions and uncertainty, tighter global financing conditions, and lower demand and prices for commodities—even if their exposure is somewhat contained by more limited trade in manufactured goods than in other EMDEs. Growth in LICs also remains hindered by lingering structural constraints, including pervasive violence. In several LICs, elevated violence has increased extreme poverty, food insecurity, and the number of displaced people (figure B1.2.1.B). Additionally, increased debt-servicing payments, in part reflecting higher borrowing costs, have required budgetary tightening and constrained the ability of

governments to support the poor and promote development. To this end, many LICs have reduced their capital spending, which constrains their ability to address wide infrastructure gaps, weighing on longer-term growth prospects.

Risks to the growth outlook are skewed to the downside. Growth in LICs could fall short of current projections if the global environment deteriorates further. Intensification of global trade tensions and uncertainty could weigh on activity, especially in commodity-exporting LICs. Weaker external demand could exacerbate other risks in LICs, including further increases in domestic political instability and violent conflict, as well as more persistent inflation than projected, which could delay the easing of financial conditions. Greater frequency or intensity of adverse weather events could also dampen economic activity, as could further reductions in donor support.

Against this backdrop, this box addresses the following questions:

- What have been the main recent economic developments in LICs?
- What is the outlook for LICs?
- What are the risks to the outlook?

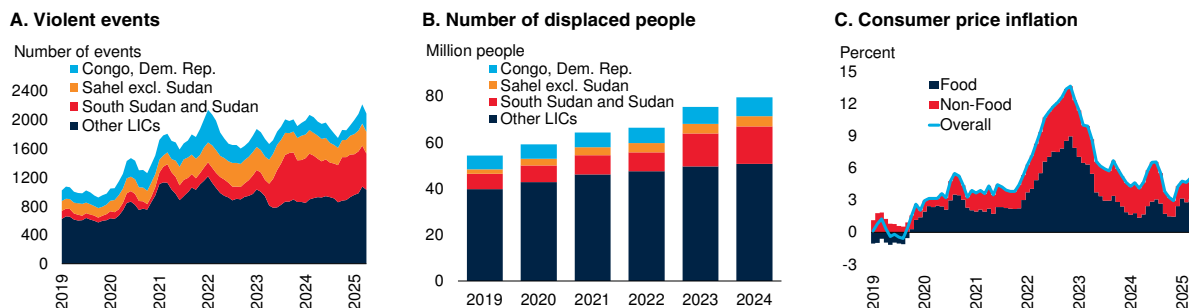
### Recent developments

Growth in LICs strengthened to 4.6 percent in 2024 but remained below pre-pandemic average rates. The growth momentum was driven by accelerated activity in agricultural exporters, including Ethiopia; solid invest-

*Note:* This box was prepared by Edoardo Palombo and Dominik Peschel.

**BOX 1.2 Low-income countries: Recent developments and outlook (continued)****FIGURE B1.2.1 LICs: Recent developments**

Despite growth in LICs strengthening to 4.6 percent in 2024, domestic factors—such as violent conflict, displacement, and inflationary pressures—continue to hinder economic and humanitarian development. The incidence of violence has remained high in LICs, mainly reflecting violent conflicts in East Africa and the Sahel. Consequently, the number of displaced people has increased, driven by conflicts in Sub-Saharan Africa. Median consumer price inflation in LICs has been on a downward trend since early 2023, but a resurgence in food inflation caused it to spike in mid-2024, and it has edged up again more recently.



Sources: ACLED (database); Haver Analytics; UNHCR Refugee Population Statistics Database; World Bank.

Note: excl. = excluding; LICs = low-income countries.

A. Three-month moving average. Violent events include battles, explosions, violence against civilians, and riots. Last observation is April 2025.

B. Statistics cover forcibly displaced persons by country of origin, including refugees under UNHCR's mandate, asylum-seekers, and internally displaced persons of concern to UNHCR. Sample includes 26 LICs, of which 6 are in the Sahel.

C. Change in prices from 12 months earlier. Unweighted average for the sample of seven LICs. Last observation is March 2025.

ment growth in Uganda; and still-above-average growth in the Democratic Republic of Congo, spurred by mining activity. Part of the improvement in aggregate growth also reflects a smaller-than-anticipated economic contraction in Sudan's economy. In 2024, growth picked up in 15 of the 25 LICs for which data are available, and it has been revised up since January for nearly two-thirds of them, including the two largest LICs—the Democratic Republic of Congo and Ethiopia. For LICs as a group, growth in 2024 has been revised up by 1.0 percentage point since the January forecast.

Fragility and conflict have been key differentiators of growth performance. Among non-FCS LICs, activity expanded by 5.7 percent in 2024, helped in part by the oil-related construction boom in Uganda. However, output grew by only 0.5 percent in FCS LICs when the Democratic Republic of Congo and Ethiopia are excluded. The conflict-related contraction in Sudan contributed markedly to this weak performance, with government institutions collapsing and a sizable portion of the population displaced. In Ethiopia, growth accelerated to 8.1 percent last year, boosted by good agricultural output, increased mining, and higher electricity generation activity. In the Democratic

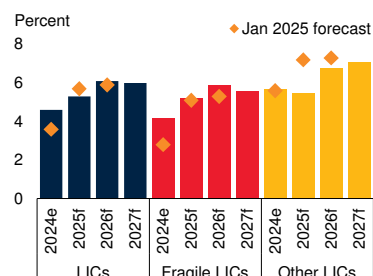
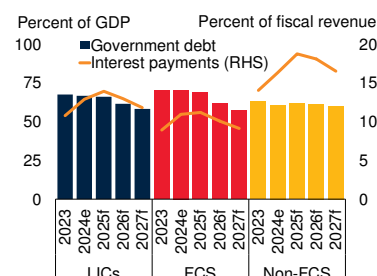
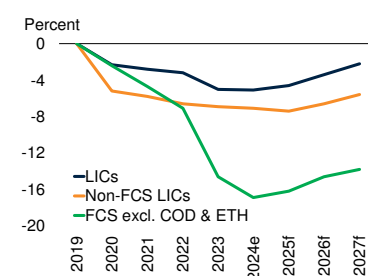
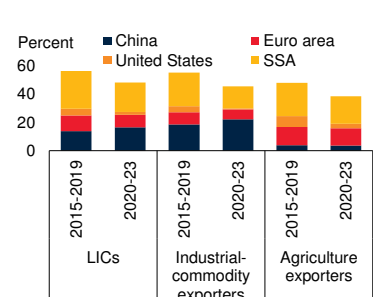
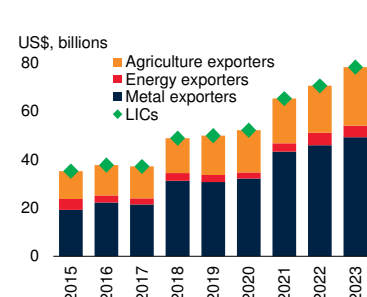
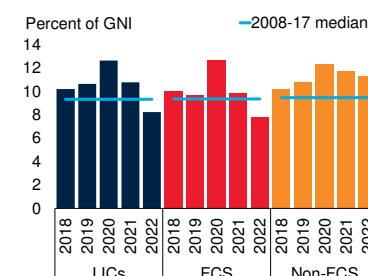
Republic of Congo, output grew by 6.5 percent, despite intensifying conflict in the eastern part of the country, which has further increased the number of internally displaced persons, already in the millions, as a result of ongoing violence.

In early 2025, improved weather conditions helped agricultural output recover in some LICs affected by severe climate-related shocks last year, such as Malawi, which experienced droughts, and Mozambique, which experienced heavy rains and floods. In South Sudan, returning households have resumed agricultural activities, which has increased farming production and helped prevent an even more severe economic downturn.

While annual consumer price inflation in the median LIC has come down from its mid-2022 peaks, food prices temporarily edged up in many LICs in mid-2024 (figure B1.2.1.C). In 2024, floods in East Africa and the Sahel and droughts in Southern Africa adversely affected some harvests, raising local food prices. However, recent satellite data show that, since the start of 2025, drought conditions have worsened in East Africa, with Rwanda and Uganda particularly affected. In early 2025, food price inflation remained very high in some LICs

**BOX 1.2 Low-income countries: Recent developments and outlook (continued)****FIGURE B1.2.2 LICs: Outlook and risks**

Although growth in LICs is expected to firm in 2025, it will be weaker than previously expected, reflecting a more challenging external environment. Debt-to-GDP ratios in LICs are set to decline, but interest payments are set to remain elevated relative to fiscal revenues. Despite recoveries in FCS economies, LIC per capita incomes are not set to reach pre-pandemic trends by 2027. LICs export a small share to the United States, with a greater share directed to China, the euro area, and other SSA economies. Metal exporters drove the doubling in LIC exports from 2015 to 2023. Growing dependence on development assistance (2018-22) makes LICs vulnerable to aid withdrawal, which would worsen fiscal pressures, growth, and humanitarian conditions.

**A. Growth forecast and comparison to January 2025 projections****B. Government debt and interest payments****C. Per capita income losses relative to pre-pandemic projections****D. LICs' exports by destination****E. LICs' exports by country grouping****F. Official Development Assistance inflows as a share of GNI**

Sources: International Monetary Fund; World Bank.

Note: e = estimate; excl. = excluding; f = forecast. COD = Democratic Republic of Congo; ETH = Ethiopia; FCS = fragile and conflict-affected situations; GDP = gross domestic product; GNI = gross national income; LICs = low-income countries; SSA = Sub-Saharan Africa.

A. Data are GDP growth forecasts, as reported respectively in the June 2025 and January 2025 editions of the *Global Economic Prospects*. Sample comprises 22 LICs.

B. Simple averages of country groupings. Sample includes 21 LIC economies.

C. Panel shows percent deviation from the 2020 January *Global Economic Prospects* baseline projections for GDP per capita.

D.-E. Subgroupings include LICs only. The sample contains 22 LICs.

D. The figure shows the share in total exports.

E. Countries are categorized according to their main export items.

F. Sample includes up to 23 LIC economies. The blue line represents the median from 2008 to 2017 for each grouping.

(Burundi and Malawi), while conflict has kept food prices elevated in other LICs (South Sudan and Sudan).

**Outlook**

Growth in LICs is projected to firm to 5.3 percent in 2025 and strengthen further to an average of 6.1 percent a year in 2026-27 (figure B1.2.2.A). Compared to previous projections, the forecast has been trimmed by 0.4 percentage point for 2025. This largely reflects slower global growth amid increases in trade barriers,

heightened trade policy uncertainty, and waning investor sentiment. While weaker growth prospects in 2025 have also been driven by a large downward revision for conflict-affected South Sudan, the deterioration in prospects is broad-based. Specifically, growth forecasts have been downgraded for nearly 60 percent of LICs in 2025 and in 2026. Although the growth forecast in LICs has been upgraded by 0.2 percentage point for 2026, this is driven by the large upward revisions for South Sudan and Sudan, where

**BOX 1.2 Low-income countries: Recent developments and outlook (continued)****TABLE B1.2.1 Low-income country forecasts<sup>a</sup>**

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

Percentage-point  
differences from January  
2025 projections

	2022	2023	2024e	2025f	2026f	2027f	2025f	2026f
<b>Low-Income Countries, GDP<sup>b</sup></b>	<b>4.4</b>	<b>2.8</b>	<b>4.6</b>	<b>5.3</b>	<b>6.1</b>	<b>6.0</b>	<b>-0.4</b>	<b>0.2</b>
GDP per capita (U.S. dollars)	1.6	0.1	1.8	2.5	3.3	3.2	-0.4	0.2
Afghanistan <sup>c,d</sup>	-6.2	2.3	2.5	2.2	2.4	2.5	..	..
Burkina Faso	1.5	3.0	4.9	4.3	4.7	5.0	0.4	0.6
Burundi	1.8	2.7	3.5	3.5	3.7	4.0	0.0	-0.5
Central African Republic	0.5	0.7	1.5	2.1	2.2	2.8	1.0	0.2
Chad	13.0	4.1	3.7	3.5	4.5	4.4	1.4	1.0
Congo, Dem. Rep.	8.9	8.6	6.5	4.8	5.0	5.3	-0.2	0.4
Eritrea	2.5	2.6	2.9	3.1	3.4	3.5	0.1	0.1
Ethiopia <sup>d</sup>	6.4	7.2	8.1	6.4	6.5	7.2	-0.1	-0.6
Gambia, The	5.5	4.8	5.7	5.6	5.3	5.5	-0.2	-0.1
Guinea-Bissau	5.6	4.4	4.8	5.1	5.2	5.2	0.1	0.2
Liberia	4.8	4.7	4.8	5.1	5.5	5.7	-0.6	-0.3
Madagascar	4.2	4.2	4.2	3.7	3.9	4.4	-0.9	-0.8
Malawi	0.9	1.9	1.8	2.0	2.4	3.2	-2.2	-0.9
Mali	3.5	3.5	4.0	4.8	4.8	4.7	0.8	0.3
Mozambique	4.4	5.4	1.8	3.0	3.5	3.5	-1.0	-0.5
Niger	11.5	2.0	8.4	7.1	5.1	4.5	-1.4	0.5
Rwanda	8.2	8.2	8.9	7.0	7.3	7.3	-0.8	-0.2
Sierra Leone	5.3	5.7	4.0	4.1	4.2	4.2	-0.6	-0.5
Somalia, Fed. Rep.	2.7	4.2	4.0	3.0	3.5	3.5	-1.5	-1.0
South Sudan <sup>d</sup>	-2.3	-1.3	-7.2	-34.7	41.1	21.2	-23.3	35.0
Sudan	-1.0	-29.4	-13.5	5.0	9.3	4.1	3.7	6.4
Syrian Arab Republic <sup>c</sup>	0.7	-1.2	-1.5	1.0	..	..	2.0	..
Togo	5.8	6.4	5.3	5.0	5.4	5.5	-0.4	-0.4
Uganda <sup>d</sup>	4.7	5.3	6.1	6.2	6.2	10.4	0.0	-4.6
Yemen, Rep. <sup>c</sup>	1.5	-2.0	-1.5	-1.5	0.5	..	-3.0	..

Source: World Bank.

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 is not projected due to data limitations.

b. Aggregate growth rates are calculated using GDP weights at average 2010-19 prices and market exchange rates. Data for the Syrian Arab Republic and the Republic of Yemen are excluded.

c. Forecasts for the Syrian Arab Republic (beyond 2025) and the Republic of Yemen (beyond 2026) are excluded because of a high degree of uncertainty. Forecasts for Afghanistan (2024-26) and the Republic of Yemen (2026) were not included in January 2025 *Global Economic Prospects*; therefore, the differences from January 2025 projection are not computed.

d. GDP growth rates are on a fiscal year basis. For example, the column for 2022 refers to FY2021/22.

conflict is assumed to de-escalate and oil exports resume in the latter, outweighing the impact of lower global growth on other LICs.

Activity in LICs will continue to face multiple challenges arising from domestic factors, including high public debt, limited access to financing, and external factors, such as a slowdown in global growth, fragmented trade, and falling donor support. Against

this backdrop, the outlook remains highly uncertain and hinges on a substantial improvement in the security situation in a number of LICs, no new violent conflicts breaking out, inflation abating, debt crises being avoided, donor support not retrenching further, and the absence of major adverse weather events.

Government debt-to-GDP ratios in LICs are expected to decline gradually from recent highs but remain above

**BOX 1.2 Low-income countries: Recent developments and outlook (*continued*)**

60 percent, on average, by the end of 2027 (figure B1.2.2.B). The projected decline in debt ratios partly reflects primary fiscal surpluses amid consolidation efforts. Interest payments are expected to stay elevated across LICs and to remain above 10 percent of fiscal revenues by 2027, partially offsetting the improvements in the projected primary fiscal balance.

Anticipating improvements in the security situation in some countries, growth in FCS LICs is forecast to increase to 5.2 percent in 2025 and average 5.8 percent a year in 2026-27. The pick-up reflects a projected return to growth in Sudan and recovery of oil production in South Sudan. Growth is projected to remain solid in both the Democratic Republic of Congo and Ethiopia, albeit at a lower rate than in the last two years.

Growth in non-FCS LICs, which include 8 economies out of a total of 22 LICs, is forecast to weaken marginally from 5.7 percent in 2024 to 5.5 percent in 2025, before picking up to an average of 7.0 percent a year in 2026-27. This acceleration partly reflects stronger growth in Uganda due to oil-related capital investment and the anticipated start of oil production in 2027.

Per capita income growth in LICs is expected to increase from 1.8 percent in 2024 to an average of 3.0 percent a year in 2025-27, with per capita income growth in non-FCS LICs averaging 3.9 percent a year. However, these growth rates in average per capita incomes are not enough to close the gap with their pre-pandemic trend by the end of 2027 (figure B1.2.2.C). Indeed, per capita incomes growth in FCS LICs, excluding the Democratic Republic of Congo and Ethiopia—the two countries driving growth in this group—is expected to be only 1.7 percent a year in 2025-27. Per capita incomes in more than one-third of 24 LICs are expected to be below pre-pandemic projections by the end of 2027, down from half in 2024.

Despite gains in per capita income, many LICs will likely see limited progress in reducing poverty. One contributing factor is that SSA—home to most LICs—has a high growth inelasticity of poverty, requiring stronger economic growth rates than other regions to achieve similar poverty reduction results (Wu et al. 2024). The high inelasticity reflects a lower pass-

through between growth in GDP per capita and growth in private consumption. Moreover, populations in several countries continue to suffer from violent conflicts, political instability, and their repercussions, including displacement and food shortages, exacerbating the often-dire conditions in FCS LICs.

Without sufficient job creation in LICs, however, these countries' economic and humanitarian challenges will not be resolved. Indeed, the challenge to spur jobs remains large, given growth headwinds and a further doubling of populations over the next 25 years in many LICs. This is likely to exacerbate pre-existing employment constraints, such as pervasive informality and widespread economic inactivity, including large-scale youth unemployment. In many cases, labor productivity remains subdued, notably in the agricultural sector, which accounts for a larger share of employment in LICs than in other EMDEs.

**Risks**

Risks to the growth outlook remain tilted to the downside, especially for FCS LICs, as projections are predicated on positive regional developments, which may fail to materialize. Should the intensity of ongoing conflicts not ease as assumed or escalate further—especially in the Democratic Republic of Congo, South Sudan, and Sudan—it could lead to extended humanitarian crises and exacerbate already severe food insecurity across LICs in the region, as many of these countries rely heavily on food imports.

Growth in LICs could prove weaker than projected if global economic conditions deteriorate. Specifically, unexpected adverse changes in trade policies among major economies and persistently high policy uncertainty could negatively impact LICs' growth prospects. While the direct effect of tariff increases by major economies would likely be relatively moderate for LICs given their limited export exposure to advanced economies, indirect effects could be substantial (figure B1.2.2.D). A primary concern is the potential for trade barriers to escalate and trigger a larger-than-expected global slowdown, which would particularly affect metal exporters, given their reliance on world export markets (figure B1.2.2.E). Overall, LICs remain vulnerable to global commodity price fluctuations and shifts in investor sentiment that could result from heightened international trade tensions.

**BOX 1.2 Low-income countries: Recent developments and outlook (continued)**

Lower-than-expected official development assistance (ODA) inflows to LICs pose another important downside risk to the growth outlook, as well as fiscal burdens and humanitarian challenges. The loss of aid financing for various projects, such as infrastructure development, education, and healthcare, could lead to a deterioration in economic activity and the drivers of long-term growth. Moreover, withdrawal of donor support may exacerbate the fiscal challenges of LICs as governments may have to substitute the missing ODA inflows, representing a median of 8 percent of GNI in 2022 (figure B1.2.2.F). Although, on average, there is not a significant difference in exposure to donor support between FCS and non-FCS LICs, three FCS economies—Afghanistan, Central African Republic and the Syrian Arab Republic—are among the most exposed LICs to a sharp decline in ODA inflows, given their high reliance on donor support.

Domestic inflationary pressures in LICs could intensify due to several factors, including further debt monetization, exchange rate depreciations, regional conflicts disrupting supply chains, and adverse weather conditions affecting food prices. This may push central banks in SSA to slow the pace of monetary policy easing, resulting in a slower-than-expected improvement in LICs' financial conditions. While high debt-servicing costs remain a burden for many LICs, liquidity concerns and foreign reserve adequacy are also pressing challenges. These challenges, which often

disproportionately impact vulnerable populations, may be compounded by global developments, especially should global inflation prove more persistent than expected and global interest rates remain high.

A deterioration in financing conditions facing LICs could further heighten the risk of government debt distress in some countries. Despite the efforts of several LICs to reduce vulnerabilities to external shocks—through an increased share of domestic debt and the extension of its maturity—15 out of 25 LICs were in or at high risk of government debt distress in 2024. Indeed, sizable primary deficits have driven the debt buildup in LICs, reflecting expenditure pressures amid persistent revenue weakness (Chuku et al. 2023). In the forecast horizon, government debt-to-GDP ratios in LICs are expected to improve (IMF 2025). However, overall debt burdens are set to remain elevated, and fiscal consolidation efforts are expected to be slower and more uncertain than anticipated in January, given the challenging external environment.

If the adverse effects of climate change intensify, the pace of poverty reduction in LICs could be markedly slower (Jafino et al. 2020). Extreme weather events, such as droughts and floods, have frequently had catastrophic consequences in LICs. Such experiences could be repeated, as these countries have limited institutional capacity to cope with natural disasters and generally lack the financial resources needed to help mitigate their adverse effects.

deteriorating outlook for global growth amid increasing uncertainty and rising trade restrictions, as well as by limited policy space. Excluding China and India, progress in closing the gap in income levels with advanced economies has stalled since the early 2010s and is envisaged to remain stagnant (figure 1.10.B).

In LICs, per capita growth is expected to pick up over the forecast horizon but remain too slow to make up for ground lost since the pandemic. Indeed, despite LICs' comparatively lesser exposure to increased trade tensions, their recovery in per capita income is projected to be slower than was anticipated in January's forecasts, with softer

global commodity demand and subdued investor confidence weighing on the outlook this year and next. FCS countries continue to fare much worse than was foreseen in the 2010s, as conflict has become an increasingly prominent driver of per capita output losses. Since the early 2000s, the number of conflicts and conflict-related deaths has risen substantially (figure 1.10.C). As a result, by 2027, per capita incomes in FCS are projected to remain over 11 percent lower than the pre-pandemic trend, compared to about 4 percent for LICs as a whole (figure 1.10.D).

After considerable headway in reducing extreme poverty rates until the 2010s, moderating per

capita income growth across EMDEs has slowed progress on poverty reduction (figure 1.10.E). While some regions, such as SAR, have made notable reductions in extreme poverty, the extreme poverty rates in EMDEs excluding China and India, and especially across LICs—many of which are FCS economies—are expected to remain higher than prior to the pandemic through 2026. Slowing progress on poverty reduction has coincided with an intensification in conflict since the mid-2010s. As of 2025, FCS, which are home to nearly 1.1 billion people, account for nearly half of the global population living in extreme poverty, up from about 40 percent in 2019. By 2030, almost 60 percent of the world's poor, or 365 million people, are expected to reside in FCS (figure 1.10.F).

## Global outlook and risks

### Summary of global outlook

In all, global growth prospects have substantially weakened since January, with some of the downside risks related to trade having materialized in recent months—most notably, a significant increase in trade barriers and policy uncertainty. In view of these developments, the forecasts assume that tariff rates in place as of late May prevail throughout the forecast horizon. Accordingly, previously announced pauses to tariff hikes between the United States and its trading partners are assumed to be extended with at most limited modifications. In this context, global growth is projected to slow markedly to 2.3 percent in 2025—the slowest pace since 2008, aside from two years of outright global recession in 2009 and 2020. Over 2026–27, a pickup in domestic demand is expected to lift global growth to a still-subdued 2.5 percent—far below the pre-pandemic decadal average of 3.1 percent (figure 1.11.A). The expected deterioration in growth is broad-based, with many of the world's economies likely to experience slower growth relative to last year as well as previous forecasts (figure 1.11.B). EMDEs with tight trade and investment linkages with the three largest economies—the United States, euro area, and China—are expected to be adversely impacted by the spillovers from a concurrent slowdown in these economies this year (figures 1.11.C and 1.11.D).

Although central banks are anticipated to continue lowering monetary policy rates, the future path of interest rates is uncertain considering the potential risks that higher tariffs pose for the disinflation process, particularly in the United States. Fiscal policy is assumed to be broadly neutral in many economies, excluding some European countries where increased defense and infrastructure spending is included in the baseline. In some major economies, aggregate fiscal policy shifts could prove materially more expansionary than the baseline assumptions.

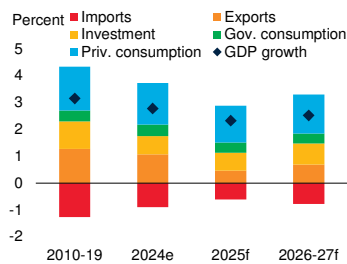
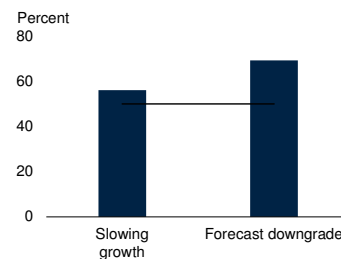
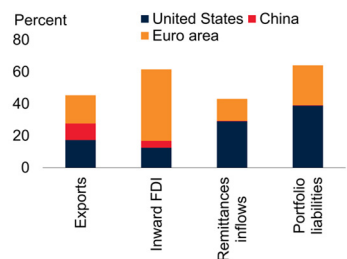
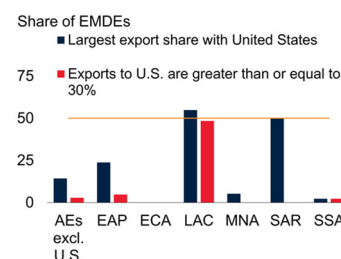
Against this backdrop, global trade and investment growth are also expected to be notably lower relative to previous projections, mostly owing to a sharp deterioration in business and consumer confidence. Uncertainty about future trade policies is likely to amplify the negative effect of increased trade barriers on near-term investment and activity, especially as firms delay or reconsider capital spending, which tends to be trade-intensive (IMF 2018; Kose, Ohnsorge et al. 2017). As global trade and investment weaken, labor demand and private consumption growth in key advanced economies are also set to slow. Although some countries may benefit from trade diversion in the short run depending on the distribution of tariffs across U.S. trading partners, mounting trade restrictions could disrupt global value chains, contributing to higher prices in some sectors. Protectionism, if it becomes entrenched, is also likely to stifle cross-border flows of commerce, capital, and technology in the longer term, weighing on productivity and global potential growth.

### Risks to the outlook

Downside risks to the outlook continue to dominate (figure 1.12.A). Higher or more persistent trade policy uncertainty presents a major risk to global trade, investment, and overall activity. Renewed increases in trade tensions and barriers could further weigh on consumer and business confidence, weakening demand. A reappraisal of risk appetite and deleveraging in financial markets could generate financial stress that curbs economic activity globally, with large capital outflows from vulnerable EMDEs. Some

**FIGURE 1.11 Global outlook**

Global growth is anticipated to weaken in the near term, reflecting a sharp increase in trade barriers and heightened uncertainty. The deterioration in growth prospects is expected to be broad-based, affecting most of the world's economies. The slowdown this year in the three major engines of global growth—the United States, euro area, and China—is expected to dampen activity in other EMDEs, especially those with tight trade and investment linkages to these economies.

**A. Contributions to global growth****B. Share of economies with slowing/downgraded growth in 2025****C. Trade and financial linkages between major economies and EMDEs excluding China****D. Share of economies for which the United States is a major goods export destination, 2010-23**

Sources: BIS (database); IMF Coordinated Direct Investment Survey (database); World Bank; World Integrated Trade Solution (database); WBG-KNOMAD.

Note: e = estimate; f = forecast. AEs = advanced economies; EAP = East Asia and the Pacific; ECA = Eastern Europe and Central Asia; EMDEs = emerging market and developing economies; LAC = Latin America and the Caribbean; MNA = the Middle East and North Africa; SAR = South Asia; SSA = Sub-Saharan Africa; U.S. = United States.

A. Aggregates are calculated using real U.S. dollar GDP weights at average 2010-19 prices and market exchange rates. Discrepancies between GDP growth and the sum of its components reflect inventories and residuals.

B. Panel shows the share of economies with slowing growth and with growth outlook downgraded relative to January 2025 forecasts. Horizontal line shows 50 percent.

C. Bars show, for EMDEs excluding China, the share of total exports that are directed to China, the euro area, and the United States, and the shares of total inward FDI positions, remittance inflows, and portfolio liabilities that originate from China, the euro area, and the United States. Data refer to 2023 apart from remittance inflows, which refer to 2021. Sample includes 106 EMDEs for exports, 144 EMDEs for FDI, 153 EMDEs for remittances, and 81 EMDEs for portfolio liabilities.

D. Share of EMDEs in each region for which exports to the United States account for the single largest share of total exports or for which exports to the United States account for at least 30 percent of total exports.

reductions between major economies. In addition, global growth could be stronger than projected due to a technology-led investment boost and additional fiscal spending in major economies—though the latter could also generate inflationary pressures and undermine efforts to restore medium-term fiscal sustainability.

**Downside risks****Persistently elevated policy uncertainty**

Policy uncertainty—especially about trade policy—remains very high. The imposition of higher trade barriers has already unsettled financial markets and dampened business and consumer sentiment. Despite recent trade negotiations, concerns remain that global trade tensions could escalate in unpredictable ways. The speed and scope of policy shifts have also made it challenging for firms to plan, leading to reduced capital investment and hiring plans.

The duration of this period of acute uncertainty could be a key determinant of global growth, on top of the direct impacts of policies that are enacted. In the baseline, uncertainty is expected to wane as tariff rates stabilize and trade patterns adjust. If, however, elevated uncertainty persists for longer or rises further over the forecast period, the adverse implications for economic activity could compound, pushing global growth notably below expectations.

An unexpected rise in trade policy uncertainty could weigh more on the sentiment of consumers, investors, and businesses, which, in turn, would have adverse impacts on output and employment globally, especially in export-intensive industries. A sharp further increase in uncertainty, particularly for an extended period, would likely drive EMDE investment and growth markedly lower (figure 1.12.B). It could, for example, delay investments in productive capacity in exporting countries, speed up exit of firms from exporting industries most likely to be affected by tariffs, and lead to costly trade diversion (Crowley, Exton, and Han 2020; Douch, Du, and Vanino 2019; Handley and Limão 2019). Weaker investor sentiment and a lack of clarity over future trading arrangements could particularly curtail the flow of

major economies may experience a mutually reinforcing combination of downside risks, resulting in notably weaker growth with adverse global spillovers. Increased conflict and geopolitical stress, as well as more frequent and intense natural disasters, could also push growth below expectations. On the upside, the drag from uncertainty and increased trade barriers could be attenuated if negotiations give rise to tariff

FDI linked to establishing supply chains, which has historically been a major driver of economic development.

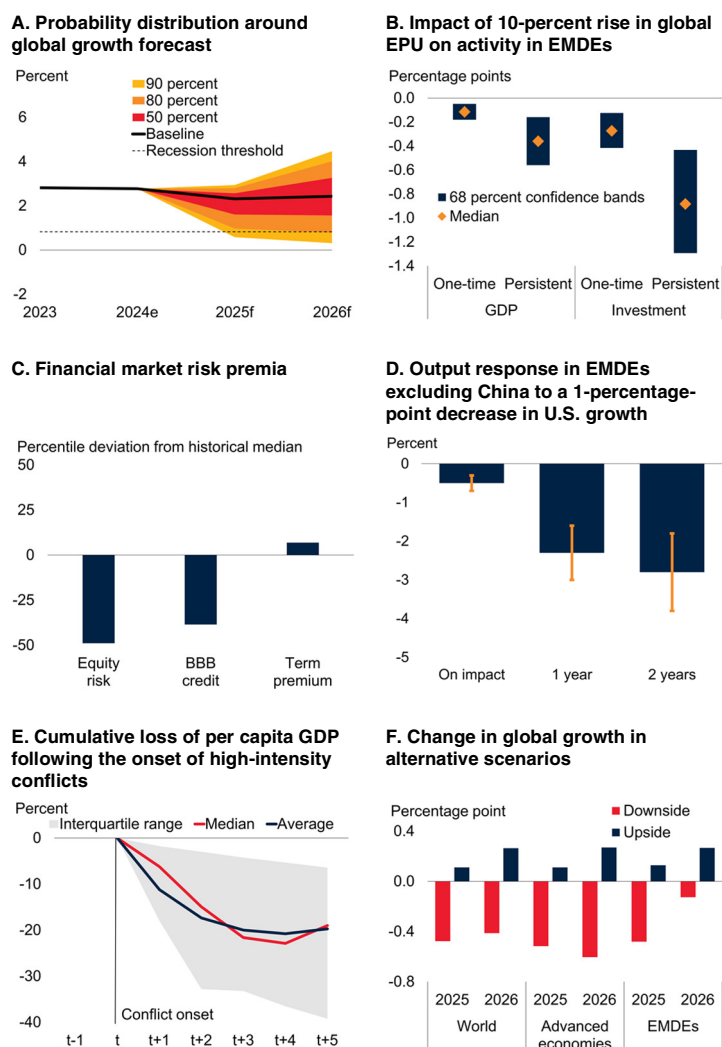
### Escalation of trade tensions

Although the baseline encompasses a significant increase in trade barriers, there remains a substantial risk that the trend of rising trade protectionism and inward-looking policies in major economies intensifies further. This could include a reversion to previously announced higher tariffs and the reintroduction and expansion of retaliatory measures. A renewed escalation in trade tensions and trade costs would amplify their negative consequences for the global economy. Such an outcome might become more likely if tariffs and ongoing shifts in trading relations put downward pressure on export prices in large goods exporters, such that domestic producers in economies that have not increased import levies face suddenly intensifying competition.

Further increases in tariffs would likely lead to higher inflation in the implementing jurisdictions (Amiti, Redding, and Weinstein 2019). Prices for imported consumer and intermediate goods would rise directly, with at least a sizable portion of tariffs likely to be passed on to domestic buyers. In the near term, substitution toward domestic alternatives would not be feasible for every product affected—such adjustments would take time and be costly. This would further push up prices—including on domestically assembled products as already suggested by high-frequency data—raising consumer inflation generally (Cavallo, Llamas, and Vazquez 2025). Higher prices would reduce real income and consumption further, which, in turn, could dampen private investment. These effects could be especially pronounced in export-intensive economies, as importers move parts of the supply chain onshore. Consumer and business confidence would also decline in the context of escalating trade conflicts, further reducing economic activity. In the long run, sustained high trade barriers and reduced trade would dampen productivity growth, including by impeding the diffusion of technology across borders.

### FIGURE 1.12 Risks to the outlook

*Downside risks continue to dominate. Further uncertainty would lower EMDE investment and growth. Despite recent market turmoil, risk premia in key markets remain relatively narrow, leaving asset prices vulnerable to large negative adjustments. A marked slowdown in major economies, especially the United States, would have sizable adverse spillovers. A rising number of EMDEs face acute risks from armed conflicts, which have proliferated in recent years, often culminating in deep recessions. Globally, a downside scenario of renewed trade tensions could push global growth sharply lower. In contrast, an upside scenario of trade negotiations that de-escalate tensions could mitigate the expected slowdown in global growth.*



Sources: Barclays; Bloomberg; Consensus Economics; Federal Reserve Banks of New York and St. Louis; Haver Analytics; Oxford Economics; Uppsala Conflict Data Program; World Bank.

Note: BVAR = Bayesian vector autoregression; EPU = economic policy uncertainty.

A. Dashed line indicates global recession (below zero per capita growth). Probabilities use range and skewness implied by oil and equity options, and term spread forecasts. Values for 2025-26 use 6-month- and 18-month-ahead forecast distributions. Last observation is May 2025.

B. GDP-weighted cumulative impulse responses of growth to a 10-percent increase ("one-time") or ongoing 4-quarter 10-percent increase ("persistent") in global EPU (Davis 2016), one year after the first shock. BVAR estimated over 1998Q1-2023Q4 for 39 EMDEs, with four lags.

C. Equity risk proxied by the U.S. Shiller excess earnings yield. BBB credit spread is for the U.S. Term premium is an average of Kim and Wright, and Adrian, Crump, and Moench models of the U.S. 10-year premium. Data from 2003 for equities; 2000 for other variables. Last observation May 2025.

D. Median cumulative responses from BVAR covering 2000Q1-23Q4. Whiskers show 16-84 percent confidence bands. For details, see Annex 3.2 in the Jan 2025 *Global Economic Prospects*.

E. High-intensity conflict means 150+ deaths per million at onset, with that threshold not exceeded in four prior years. Lines show the cumulative gap between World Bank forecast one year before onset and actual per capita GDP. Sample of 14 conflicts in 14 EMDEs from 2006-23.

F. Growth deviation in upside/downside scenarios, using Oxford Economics' Global Economic Model.

Damage to global supply could, over time, push up prices even in countries that do not raise their own tariffs and are not significantly affected by rising tariffs elsewhere. A bout of higher inflation and weaker growth would pose substantial challenges to central banks in affected economies, especially if inflation expectations showed signs of de-anchoring following several years of above-target price gains.

### **Disorderly asset price corrections and financial stress**

Heightened volatility in financial markets and the potential for large asset price adjustments pose additional risks to global economic activity and could amplify the effects of other risks materializing. Despite recent volatility spikes, risk premia in key equity and credit markets remain narrow compared with historical norms (figure 1.12.C). In this context, a material reappraisal of risk appetite could lead to sharp asset price corrections in advanced economies, which would reverberate through global markets and might become disorderly if synchronous deleveraging by market participants leads to liquidity strains. The resulting repricing of equities in both advanced economies and EMDEs could lower consumption through wealth and confidence effects, whereas widening corporate spreads would weigh on investment globally. Banks might also retrench from riskier lending, slowing credit growth and curbing some cross-border intermediation. For example, with heightened trade policy uncertainty, tighter lending conditions could see the availability of trade credit decline, exacerbating the slowdown in global trade and EMDE exports.

It is also possible that weakening risk sentiment might coincide with a rise in the term premium on advanced-economy government bonds, given uncertainty about the outlook for inflation and policy rates in key economies. This would further tighten global financial conditions. Against a backdrop of reduced global risk appetite and still-elevated benchmark interest rates, EMDEs with heightened domestic vulnerabilities would be prone to large capital outflows. Shifting interest rate differentials could constrain some EMDE central banks from supporting domestic activity,

as they might slow or delay policy easing to mitigate capital outflows and inflationary pressures resulting from currency depreciation. In EMDEs with weak credit ratings and high debt levels, market access for refinancing maturing debts could be disrupted, necessitating sudden fiscal adjustments. More broadly, higher borrowing costs would raise debt-servicing burdens over time, worsening fiscal pressures in many EMDEs.

### **Weaker-than-expected growth in major economies**

In some major economies, downside risks could become mutually reinforcing or interact with pre-existing vulnerabilities. In the United States, business investment, hiring, and consumer spending could retrench markedly due to pessimism about future economic activity and job prospects, increases in trade barriers, and resurgent financial market volatility. Household spending may be further curtailed by weaker disposable income growth. Reduced private spending could precipitate a sharp deceleration in U.S. economic activity or even a recession. A confluence of factors such as weaker external demand, heightened uncertainty, supply chain disruptions, and tighter financial conditions could also challenge large economies seeking to overcome domestic headwinds. In China, for example, robust export performance in recent years has helped attenuate the drag on growth from the property sector slowdown.

Markedly weaker-than-expected growth in major economies could have considerable negative global spillovers. For EMDEs, external demand could soften, with exports of manufactured goods and traded services such as travel likely to weaken. Commodity prices would fall below the baseline projections, weighing on terms of trade and curbing export earnings in many commodity-exporting EMDEs, some of which might tighten fiscal policy pro-cyclically given diminishing commodity-linked revenues. Additionally, deteriorating labor markets in large economies could curtail remittance flows to some EMDEs. In general, the spillovers to EMDEs from weak growth in the United States are particularly sizable—a one percentage point decrease in U.S.

growth is estimated to lower output in EMDEs excluding China by about 3 percent after 2 years (figure 1.12.D).

### **Increased conflict and geopolitical stress**

The incidence of armed conflicts has risen substantially in recent years. While the baseline assumes a partial resolution of some major conflicts, the risk of continued or escalating conflict remains high—both at the interstate and intrastate level—against a backdrop of elevated geopolitical tensions globally. Armed conflicts result in the destruction of physical and human capital and can lead to sharp increases in poverty and food insecurity. They often culminate in deep recessions, reduced private investment, and persistent output losses in the countries involved (figure 1.12.E). Neighboring countries can also experience weaker private investment, as they often become less stable and more susceptible to conflict themselves. In addition, some large conflicts can have global consequences, as they can lead to large waves of refugees and disrupt trade networks and international commodity and financial markets.

In countries directly involved in conflict, elevated military spending can squeeze public resources for economic capacity-building spending, such as that on education, health, and civilian infrastructure. More broadly, conflict-induced declines in productive capacity lower future expected incomes, raising risk premia and increasing the probability of debt default.

Among current major episodes, a re-intensification of conflict in the Middle East could disrupt oil and natural gas supplies, causing energy prices to rise, exerting upward pressure on inflation. Uncertainty around Russia's ongoing invasion of Ukraine and its future economic implications also remains elevated, although a negotiated end of active hostilities could be reached at some point. More generally, EMDEs can be particularly vulnerable to various knock-on consequences of conflicts, including from the impact of sanctions on trade or through weaker global investor confidence impacting capital flows.

### **Increasing frequency and severity of natural disasters**

The growing incidence of natural disasters poses significant risks to lives, livelihoods, and the global economy. It is likely that the frequency and severity of extreme weather events, including natural disasters, will continue to escalate with global warming (IPCC 2014; 2022). As these events become more prevalent and intense, their future impacts are likely to be more significant. The immediate impacts of extreme weather events can materialize through various channels: loss of life, destruction of physical and infrastructure capital, displacement or migration of the labor force, and disruption of economic activity. Although empirical estimates of the economic costs of extreme weather events vary widely, such events have been shown to have major impacts on economic activity (Dell, Jones, and Olken 2014; Burke, Hsiang, and Miguel 2015). In the longer term, climate-change-related natural disasters can weaken investment and trend productivity growth as well as impede human capital development, with long-lasting impacts on vulnerable households (Angeli et al. 2022; World Bank 2025a; Zhang and Borja-Vega 2024).

Natural disaster risks are more acute for EMDEs given their higher vulnerability to such events, including typhoons, extreme heat, and severe precipitation (Hsiang and Jina 2018). Small island developing states are among the most vulnerable, owing to narrow production bases and undiversified economies, with estimated annual average losses from natural disasters ranging between 1 and 9 percent of their GDP over 2000-15 (OECD 2018). Moreover, the impacts of natural disasters across EMDEs may be amplified by weak institutional capacity, including those related to governance, and constrained fiscal space.

Extreme weather events can also lead to upward price pressures in the short run, with inflation becoming more volatile in areas subject to more frequent occurrence of such events (Angeli et al. 2022). Droughts have been found to increase food price volatility, with disproportionate impacts on poorer households.

## *Upside risks*

### **Dissipating trade policy uncertainty and reduced trade tensions**

A partial resolution of trade tensions between the United States and its trading partners—for example, through further trade negotiations or unilateral tariff reductions—could help stabilize the global trade policy environment and reduce uncertainty. These measures would enable firms to plan better and, where necessary, reorganize supply chains over a longer horizon, mitigating the adjustment costs and limiting trade disruptions (Grossman, Helpman, and Redding 2024). Such measures could also lower effective tariff rates between the United States and its major trading partners compared to the assumptions embedded in the baseline.

Relative to the baseline, lower tariffs would ease upward pressure on consumer prices and raise profit margins for both importing and exporting firms (Amiti, Redding, and Weinstein 2019). These disinflationary impacts would likely be most pronounced in the United States and any countries rolling back retaliatory measures. Diminishing trade policy uncertainty would have wider beneficial impacts, raising business and consumer confidence and thereby partially reversing the widespread drag on investment and consumption assumed in the baseline (Caldara et al. 2020). It is likely that tailwinds to global activity would also be reinforced by further easing of financial conditions, with risky asset prices incorporating a lower possibility of weak growth or debt-related strains.

### **Fiscal expansion in major economies**

In major economies, fiscal policy may become more supportive of growth relative to baseline assumptions. In the United States, fiscal policy may prove expansionary over the forecast horizon, in contrast to the slightly contractionary stance embedded in the baseline. This could result from a renewal of expiring individual and business tax provisions of the Tax Cuts and Jobs Act or other tax reductions, potentially partly offset by federal spending cuts. In the near term, this could reduce personal and corporate taxes and boost disposable

incomes, supporting consumption and business investment.

In the euro area, the outlook is subject to some upside risk following announced plans to relax fiscal rules rather than slightly tighten policy as assumed in the baseline. The EU has paved the way for allowing member states to significantly increase spending by exempting defense categories from its existing clauses in debt and deficit rules, with some economies already approving additional spending. In China, additional fiscal policy stimulus could result in higher-than-expected growth.

A combination of fiscal support in major economies would lift domestic demand in the near term and trigger positive spillovers via trade, despite the relatively low import content of defense spending and the ongoing trend toward greater trade fragmentation. However, the boost from additional fiscal support would likely be dampened somewhat by the crowding out of private investment due to higher government borrowing rates, and with wider fiscal deficits and increases in government debt worsening fiscal sustainability in some key economies.

### **Technology-led investment growth and productivity gains**

Heightened optimism about the growth potential of new technologies—including generative AI—has become widespread in recent years. Already, many large public companies are drastically increasing capital expenditures to ramp-up their technological capabilities, while many governments are also dedicating increased resources to supporting burgeoning industries. If this optimism broadens or intensifies—perhaps fueled by further technological breakthroughs—a large wave of technology-led investment could follow. This could manifest in increased global investment in energy infrastructure, data centers, and research and development, as well as foster more trade in ICT components and services.

Even if centered mostly in advanced economies and wealthier EMDEs, the benefits of such investments could spill over to EMDEs more broadly in the form of stronger external demand.

Moreover, as applications of new technologies proliferate and mature, a greater number of firms across EMDEs may make investments to enable adoption. Over the longer term, new technologies could potentially support a pickup in productivity growth in both advanced economies and EMDEs. However, this remains contingent on many broader factors, such as institutional arrangements, and whether commercially successful applications tend to be labor augmenting or labor replacing.

### *Growth outcomes under alternative scenarios*

If some of the risks discussed above were to materialize, global growth could deviate materially from the baseline projection. The risks around key trade policy assumptions are particularly notable, and their implications are examined below using a global macroeconomic model.<sup>2</sup>

#### **Downside scenario: Renewed increases in trade barriers**

This scenario assumes the weighted average U.S. tariff increases by about an additional 10 percentage points, resulting in significantly higher U.S. tariffs compared to those incorporated in the baseline. These developments are assumed to spark retaliation from trading partners. The renewed rise in trade tensions also leads to a more persistent increase in uncertainty and rising financial market volatility, accompanied by a sizable and widespread shock to confidence.

The resulting seizing up of global trade, elevated uncertainty, declines in confidence, and falling asset prices tip the global economy into an extended period of anemic expansion, reducing global growth by 0.5 and 0.4 percentage point in 2025 and 2026 relative to the baseline (figure 1.12.F). Under this scenario, the impact on growth in advanced and developing economies in 2025 is broadly similar, as the global shock to financial markets and confidence leads to a widespread reduction in activity. Compared with the baseline, advanced-economy growth is weaker

by 0.5 and 0.6 percentage point in 2025 and 2026, whereas EMDE growth is reduced by 0.5 and 0.1 percentage point.<sup>3</sup>

Much of the softness in global growth is attributable to weaker global demand amid sharply higher trade barriers and souring sentiment, which also leads to lower energy prices. This combination initially reduces global inflation by 0.4 percentage point compared with the baseline in 2025, before the upward pressure on prices from higher tariffs begins to dominate, raising inflation to 0.5 percentage point above the baseline in 2026. In this context, central banks in many advanced economies and EMDEs are constrained from significantly easing monetary policy over the next two years.

#### **Upside scenario: Faster resolution of trade tensions**

Under an upside scenario, the U.S. effective tariff rate, while still remaining above 2024 levels, is assumed to be reduced by roughly half compared to the baseline, with all retaliatory tariffs receding. Such an outcome might occur following negotiations between the United States and its main trading partners, resulting in a series of bilateral trade agreements and a general cooling of trade tensions. The lower tariffs are assumed to be accompanied by a reduction in uncertainty and an increase in confidence starting in the second half of 2025.

The more benign global trade backdrop and widespread improvement in confidence would raise global growth by 0.1 and 0.3 percentage point in 2025 and 2026 relative to the baseline. The impact is anticipated to be generally uniform across economies, with growth in both advanced economies and EMDEs boosted by 0.1 and 0.3 percentage point in 2025 and 2026 compared with the baseline. Across major economies,

<sup>2</sup>These simulations are conducted using the Oxford Economics Global Economic Model, a semi-structural macroeconomic projection model that includes 188 individual country blocks in its extended version, available at quarterly or annual frequencies (Oxford Economics 2019).

<sup>3</sup>These results are consistent with other studies that analyze the impact of comparable increases in U.S. tariffs. For instance, without retaliation from trading partners, higher tariffs are found to have a larger effect on U.S. growth compared to other economies. Furthermore, in line with the simulation results, recent studies also suggest that retaliation by trading partners would amplify the negative impact of higher tariffs on U.S. output (McKibbin, Hogan, and Noland 2024; The Budget Lab 2025).

tailwinds from stronger real income growth and better sentiment are reinforced by gradual monetary easing and rising asset prices.

## Policy challenges

With increased trade barriers, heightened policy uncertainty, and multiple downside risks weighing on the outlook, revitalizing and re-energizing global dialogue and cooperation are paramount. Global policy efforts are needed to safeguard international trade by fostering the resolution of trade disputes and mitigating the adverse impacts of geopolitical tensions on trade networks. Collective action is also needed to tackle the myriad of overlapping challenges, including widespread conflict, decline in official development assistance, and severe food insecurity, facing many vulnerable EMDEs. Furthermore, revitalizing global efforts toward climate change mitigation and adaptation is essential to limit future costs from increasingly frequent climate-related natural disasters. At the national level, shoring up economic stability requires focusing on sound monetary and financial policies to contain risks related to inflation and capital flow volatility. Amid narrow fiscal space and substantial development needs, it is critical for EMDE fiscal policy makers to adopt measures to mobilize domestic revenues, reprioritize fiscal spending, and strengthen fiscal frameworks. To bolster long-term growth prospects in EMDEs, structural reforms are needed to strengthen institutional quality, accelerate investment growth, develop human capital, and improve the functioning of labor markets. For EMDEs affected by conflict, achieving lasting peace and stability is crucial to reducing human suffering and improving economic well-being.

### Key global challenges

#### *Confronting rising trade barriers and fragmentation*

The recent rise in trade barriers and ongoing trade fragmentation are critical challenges that require appropriate policy action. These developments come against the backdrop of already sluggish global trade, where the once-rapid increase in

trade openness has stalled since the early 2010s, as the maturation of global supply networks has limited the scope for further gains from specialization (figure 1.13.A). Supply-chain disruptions associated with the pandemic and elevated geopolitical tensions have highlighted the vulnerabilities of the global trade system, prompting some countries to pursue reshoring strategies through increased use of trade restrictions and industrial policies. As a result, the momentum for trade globalization has slowed while geopolitical fragmentation has intensified (figure 1.13.B).

From a longer-term perspective, EMDEs have become increasingly integrated into the global economy since the early 2000s. This integration helped their economic development but also made them more vulnerable to rising protectionism, value chain disruptions, and trade policy uncertainty. The recent increase in trade barriers imposed by key economies, and possible ensuing retaliation, pose a significant threat to the global trading system. The international community has a role in fostering dialogue and cooperation to address global trade imbalances in an orderly and transparent manner. EMDEs, in particular, would benefit more by liberalizing broadly rather than imposing retaliatory tariffs. Across-the-board liberalization lowers trade costs and promotes investment, supporting long-term growth.

In tandem, countries need to design other policies to mitigate the adverse consequences of higher trade restrictions while taking advantage of opportunities for cross-border cooperation and improvements in domestic conditions. In EMDEs, such an approach can involve seeking strategic trade and investment partnerships with other EMDEs, reducing regulatory and trade barriers, and pursuing opportunities to diversify trade, including through regional trade agreements (World Bank 2025a). The negative consequences of rising trade barriers in certain markets can be partially offset by fostering deeper integration with other countries, including intra-regional partners, and by expanding the liberalization of current trade agreements. For example, deepening all existing preferential trade agreements to their highest level of ambition could increase GDP by

an estimated 0.8 percent in Sub-Saharan Africa and by 1.7 percent in South Asia (Fernandes et al. 2021). Deeper trade agreements can also limit the negative spillovers on excluded countries and reduce trade policy uncertainty (Handley and Limão 2015; Lee, Mulabdic, and Ruta 2023; Mattoo, Mulabdic, and Ruta 2022). Additionally, priority needs to be placed on reforming the multilateral trading system to address emerging challenges. Estimates indicate that trade cost reductions between 1995 and 2020, including those related to WTO accession commitments, boosted global real GDP by nearly 7 percent over the period, with low-income countries growing by over 30 percent (WTO 2024).

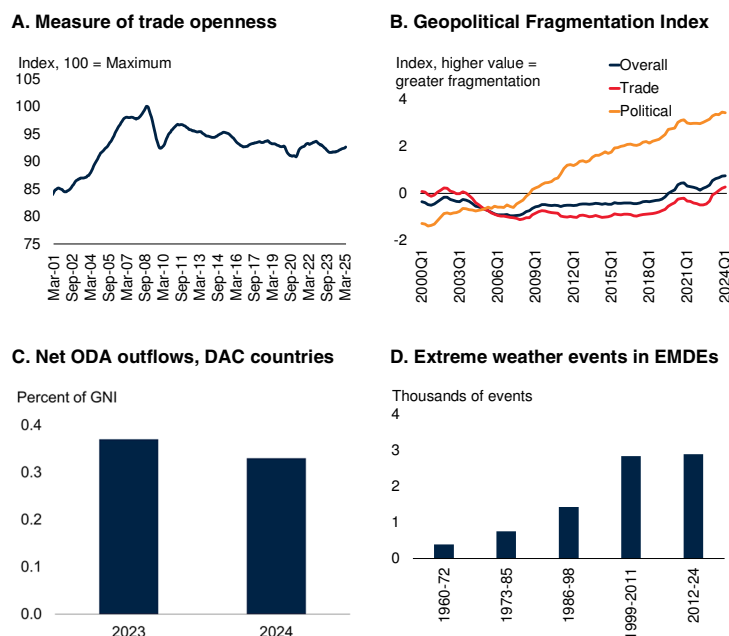
### *Insufficient support for vulnerable EMDEs*

A range of adverse trends—including the rise in global trade-restrictive measures, the incidence of conflict, the increase in displaced populations, and acute food insecurity—point to escalating challenges in many of the most vulnerable EMDEs. At the same time, many of these countries are facing extraordinary financial pressures with elevated public debt, fiscal constraints, and obstacles in mobilizing private finance. These financing challenges are compounded by declining aid flows from the international community (figure 1.13.C). Cross-border and domestic crises have led to increased humanitarian needs that necessitate swift financial responses, with governments often redirecting official development assistance (ODA) funds from other priorities to meet emergent needs (Ahmed, Calleja, and Jacquet 2025).

In a global economy susceptible to additional adverse shocks, collective action is needed to help vulnerable EMDEs make progress on key development goals and avert potentially adverse spillovers to other economies, including pressures for outward migration. Vulnerable EMDEs will need international support to mobilize additional resources and strengthen institutions for lasting reforms. Multilateral institutions can also help ensure the availability of vital goods, such as food and medical equipment, that are urgently needed during crises—as was evident during the COVID-19 pandemic (World Bank 2025a).

## **FIGURE 1.13 Global policy challenges**

*The global economic environment has shifted significantly, with increased trade barriers and ensuing policy uncertainty coming on the heels of already sluggish global trade. The once-rapid advance in goods trade openness has stalled since the early 2010s, partly due to the maturation of global supply networks. This, together with pandemic-related supply chain disruptions and escalating geopolitical tensions, has slowed the momentum for trade globalization and exacerbated geopolitical fragmentation. Meanwhile, declining official development assistance flows are compounding the financing hurdles facing many vulnerable EMDEs. Climate change remains a major challenge, with EMDEs increasingly exposed to extreme weather events.*



Sources: CPB Netherlands Bureau for Economic Policy Analysis; EM-DAT (database); Fernández-Villaverde, Mineyama, and Song (2025); OECD (2025); WDI (database); World Bank.

Note: DAC = Development Assistance Committee; EMDEs = emerging market and developing economies; GNI = gross national income; LICs = low-income countries; ODA = Official Development Assistance.

A. Trade openness is measured as the 12-month moving average of the ratio of global merchandise export volumes to global industrial production volumes (excluding construction). Last observation is March 2025.

B. The Geopolitical Fragmentation Index extracts the common factor across various indicators relating to trade, finance, mobility of people and ideas, and geopolitical instability and misalignment (Fernández-Villaverde, Mineyama, and Song 2025). Lines show the common factor derived from standardized variables with zero mean and unit standard deviation. A higher value implies greater fragmentation. Last observation is 2024Q1.

C. Panel shows ODA flows and grant equivalents as a share of GNI by Development Assistance Committee (DAC) countries.

D. Extreme weather events include droughts, floods, and storms. Sample includes 122 economies for droughts, 144 for floods, and 127 for storms.

In the case of LICs and FCS, given their substantial financing needs and limited state capacity, coordinated efforts from the global community can help these countries expand fiscal space. Measures include concessional financing and debt relief, where appropriate, as well as technical assistance to strengthen fiscal policies and build resilient macroeconomic frameworks. Countries in active conflicts will continue to

depend on the global community for emergency relief and peace-building support.

### *Natural disasters and biodiversity loss*

Natural disasters and the concomitant economic impacts are a growing concern for policy makers. EMDEs are particularly exposed to the adverse effects of climate-related natural disasters, with a steady increase in the frequency and intensity of storms, floods, and droughts over the past decades (figure 1.13.D). At the same time, loss of biodiversity—defined as the variety of plant and animal life in habitats or ecosystems—is proceeding at an unprecedented rate and scale, with dire implications for economies and livelihoods. Biodiversity and climate change are inextricably linked, with climate change being a key driver of biodiversity loss. Biodiversity can also provide protection against natural disasters and promote ecosystem resilience (Seymour, Wolosin, and Gray 2022).

As with natural disasters, the loss and degradation of biodiversity impacts low income and lower middle-income countries disproportionately. Renewable natural capital, including agricultural land and forests, and blue assets, such as fisheries and mangroves, account for 23 percent of the wealth in low-income and 10 percent in lower-middle income countries (Kemper and Pathak 2021). Estimates indicate that about \$44 trillion of global value added is generated in industries that depend moderately or heavily on nature and, consequently, exposed to risks from biodiversity loss (World Economic Forum 2020). Loss of biodiversity also presents a major risk to global food security by undermining the resilience of agricultural systems to climate change and other factors, such as pests and pathogens.

Comprehensive policies are needed to support climate change mitigation and adaptation and address biodiversity loss. These include incentivizing green investments and technologies; strengthening environmental standards and regulations; promoting debt-for-climate swaps; and reducing environmentally harmful subsidies to agriculture, fisheries, and fossil fuels (Damanian et al. 2023; World Bank 2021). Well-targeted

social benefit systems can help reduce the damage done by adverse shocks. Furthermore, facilitating trade and investment in green technologies will enhance green investments in EMDEs and promote knowledge spillovers to these economies.

Reversing global trends in biodiversity loss will require efforts to reduce global pressures on food systems, including practices such as sustainable intensification and reducing food losses and waste (Leclère et al. 2020). Better allocation and management of land, water, and other inputs could boost income from agriculture and forestry as well as increase food production to meet the caloric needs of growing global populations (Damanian et al. 2023). Additionally, applying rigorous safeguards and standards for development finance in line with best practices can help minimize and manage the impact of land use, infrastructure development, and energy and extractive sectors on biodiversity at the global scale (Narain et al. 2023; WEF 2020).

### *EMDE monetary and financial policy challenges*

With core inflation across EMDEs plateauing since mid-2024 about half a percentage point above the pre-pandemic pace, risks to inflation persist (figure 1.14.A). As trade policies shift, the economic impacts that follow should determine the appropriate monetary policy response. Elevated policy uncertainty and increased global trade barriers may have notable negative impacts on economic activity that could require some central banks to ease policy, particularly if inflation falls in response to such shocks (Baker et al. 2016; Caldara et al. 2020). Yet, given challenges in foreseeing these effects with precision, it may be best for central banks to delay taking action until incoming data clarify the state of economic activity. In other cases, central banks may need to proactively respond to emerging inflationary pressures, even at the cost of some softening of economic activity to avoid de-anchoring of inflation expectations (Mendes, Murchison, and Wilkins 2017).

With capital inflows to EMDEs declining since late 2024, some EMDEs may be particularly

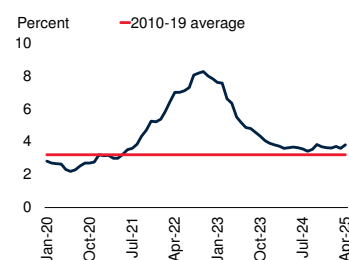
prone to destabilizing capital outflows amid increased uncertainty, ongoing inflation risks, and currency volatility (figure 1.14.B). To reduce the likelihood of such sudden shifts, EMDE policy makers can reaffirm their commitments to price stability (Kalemli-Özcan and Unsal 2024). EMDE monetary policy credibility can be reinforced through clear communications, robust monetary frameworks, and the safeguarding of central bank independence, which has steadily improved over the last two decades but nevertheless remains below advanced economy levels, on average (figure 1.14.C). To bolster credibility some EMDE central banks may need to tighten monetary policy in the face of potential capital outflows and financial volatility. Doing so could help anchor inflation expectations, reinforce investor confidence, and reduce domestic market volatility. Indeed, a proactive tightening of monetary policy by many EMDE central banks during the post-pandemic inflationary surge helped create conditions for a sustained decline in inflation, in addition to bolstering financial stability amid the rise in global interest rates at the time (Evdokimova et al. 2024).

EMDEs policy makers also need to be prepared to deploy tools that manage risks to financial stability, arising, for example, from reduced international investor risk appetite, capital outflows, and rising bond yields—all of which might stem from heightened trade tensions and policy uncertainty. Weakening growth in EMDEs—especially if downside risks materialize—could imperil financial sector balance sheets, increase corporate borrowing costs, and curtail funding access in the nonfinancial sector, particularly among trade-exposed EMDEs. Such strains could also worsen extant financial sector vulnerabilities in some countries, such as overreliance on domestic banks for sovereign financing. To promote financial sector resilience, precautionary steps can include comprehensive stress tests for financial institutions and the scrutiny of bank credit quality and capital levels, as well as enhanced liquidity and liability management, among other sound macroprudential rules. Building on progress in recent years, continued efforts to ensure adequate foreign reserves are also important (figure 1.14.D).

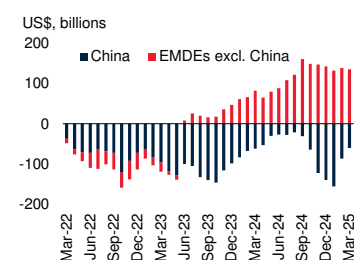
## FIGURE 1.14 EMDE monetary and financial policy challenges

*EMDE core inflation has plateaued above the pre-pandemic average. Cumulative capital inflows to EMDEs have been declining since late 2024 and could come under further strain amid heightened uncertainty, currency volatility, and inflationary pressures. EMDE central banks can make use of clear communications and credible monetary frameworks that reinforce confidence in policy independence, which remains below advanced-economy levels, on average. Additionally, foreign reserves could help protect against sudden shifts in sentiment and deterioration in financing conditions.*

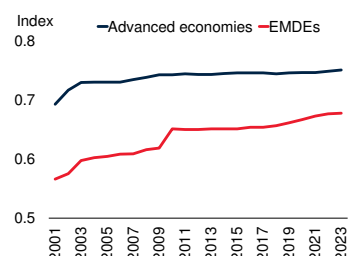
**A. Core inflation in EMDEs**



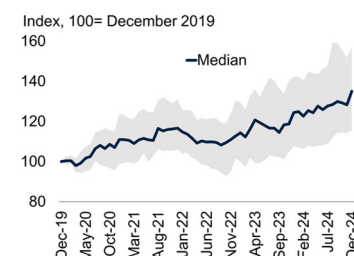
**B. Cumulative capital inflows to EMDEs**



**C. Central Bank Independence Index, by country group**



**D. Change in official reserves relative to December 2019**



Sources: Haver Analytics; Romelli (2022, 2024); World Bank.

Note: EMDEs = emerging market and developing economies.

A. Panel shows year-over-year core inflation for up to 46 EMDEs. Last observation is April 2025.

B. Panel shows the cumulative capital inflows from March 2022, using monthly data. Sample includes up to 32 EMDEs. Last observation is March 2025.

C. Lines represent the average Central Bank Independence Index score by country group, ranging from 0 to 1, with higher scores indicating greater independence. Sample includes up to 37 advanced economies and 117 EMDEs. Last observation is 2023.

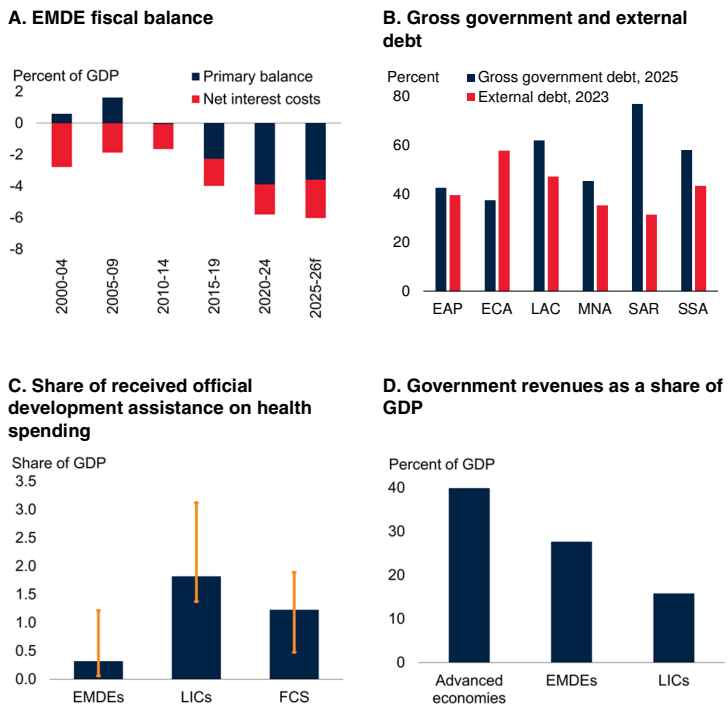
D. Official reserves and other foreign currency assets, presented as an index compared to December 2019 levels. Shaded area indicates the interquartile range. Last observation is December 2024.

## EMDE fiscal policy challenges

EMDEs require considerable fiscal resources to tackle development challenges, but the space to do so has been constrained by overlapping shocks in the last few years, which have increased government debt and widened fiscal deficits (figure 1.15.A). As a result, governments continue to face the difficult task of meeting critical public spending needs and supporting vulnerable households while shoring up fiscal sustainability. Despite progress in extending the maturity of

### FIGURE 1.15 EMDE fiscal policy challenges

*Fiscal space has narrowed in recent years, with fiscal deficits remaining wider than pre-pandemic averages in EMDEs, pointing to the need for these economies to mobilize domestic revenues and reprioritize spending. High government and external debt levels leave some EMDE regions vulnerable to sudden rises in borrowing costs. In LICs and FCS, retrenchment in official development assistance could reduce the spending envelope for critical categories, including health care. Revenue collection continues to substantially lag in EMDEs, especially in LICs, relative to advanced economies.*



Sources: Center for Global Development; IMF; Kose et al. (2022); World Bank.

Note: f = forecast. EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging market and developing economies; FCS = fragile and conflict-affected situations; LAC = Latin America and the Caribbean; LICs = low-income countries; MNA = Middle East and North Africa; SAR = South Asia; SSA = Sub-Saharan Africa.

A. Panel shows GDP-weighted aggregate fiscal balance for 154 EMDEs. Bars represent simple averages for each time period.

B. Bars show the median debt-to-GDP ratio for each EMDE region. Gross government debt includes domestic and external debt; external debt includes government and private debt.

C. Panel shows median official development assistance (gross disbursements) for health spending received in 2023 as a share of GDP. Sample includes 133 EMDEs, of which 38 are FCS and 25 are LICs. Orange whiskers indicate interquartile range.

D. Panel shows average general government revenue as a share of GDP in 2024. Sample includes 38 advanced economies and 149 EMDEs, of which 22 are LICs.

domestic debt in recent years, some EMDE regions remain vulnerable to further rises in borrowing costs and adverse shifts in market sentiment amid already high debt-servicing costs and sizable debt levels (figure 1.15.B).

Although many EMDEs have undertaken measures to strengthen fiscal positions in recent years, including the unwinding of pandemic-era spending, fiscal deficits remain above pre-pandemic averages and debt levels continue to rise

in about half of EMDEs and, in some cases, to levels that appear unsustainable. It will be critical for EMDEs, particularly those with fiscal space constraints, to raise additional domestic revenues, especially as debt-servicing costs grow and some external sources of financing, including development assistance, dwindle. LICs have become more vulnerable to rising debt-servicing costs, as their debt has increasingly shifted from concessional to market-based financing. Nearly half of LICs are either in debt distress or at high risk of it—double the share in 2015—and no LIC is at low risk. This inhibits their ability to repair the economic damage generated by recent shocks. Moreover, in LICs and FCS, since official development assistance represents a large share of critical spending, including in health, the partial loss of these flows could put further pressure on budgets (figure 1.15.C).

EMDEs, especially LICs, continue to substantially lag advanced economies in revenue collection (figure 1.15.D). Building tax capacity is a crucial step toward mobilizing domestic resources, maintaining sustainable debt dynamics, providing essential public services, supporting vulnerable populations, and rebuilding fiscal buffers (Choudhary, Ruch, and Skrok 2024). This can include measures that broaden revenue bases, including the introduction of new tax instruments (De Mooij et al. 2020). Additionally, to balance the tradeoff between generating revenue and economic growth, reducing costly loopholes—such as incentives, deductions, and exemptions—can be complemented with reforms that reinforce tax administration and collection to curb avoidance, base erosion, and profit shifting (Bachas et al. 2025). These reforms can also be combined with those that strengthen institutions and legal systems, which would help unlock tax potential in EMDEs (Benitez et al. 2023). Careful sequencing of various reform elements is also required to harness their mutually reinforcing effects for maximizing the boost to fiscal revenue (World Bank 2025b).

Reprioritizing fiscal spending away from broad, untargeted support and costly subsidies can free up resources that can be redirected to low-income households. In particular, governments can provide vulnerable households with means-tested

cash transfers, which tend to be less costly than food and fuel subsidies. Over the longer term, EMDEs can enhance internet connectivity and leverage digital tools to better identify vulnerable households, especially in countries where registries are outdated, and surveys are costly (Chowdhury et al. 2022). Protecting spending in growth-enhancing categories, such as health and education, is critical given setbacks from the pandemic, increased spending pressures due to rapid price increases in recent years, and persistently large investment gaps—all of which are likely to reduce the space for spending in these critical categories in future years (Kurowski et al. 2024).

Improvements to the expenditure review process—such as strengthening mechanisms that prioritize and evaluate the efficacy of public projects—can enhance the quality and efficiency of public spending. Policies that aim at strengthening public procurement practices, administrative capacity, and transparency can also bolster public investment efficiency, foster a more favorable business climate for private investment, and help reinvigorate productivity.

More broadly, fiscal sustainability can be enhanced by credible and well-designed frameworks, including fiscal rules, stabilization funds, and medium-term expenditure frameworks. Such measures can help reduce the procyclicality of fiscal policy, build fiscal space, and improve fiscal policy outcomes—particularly in the context of fiscal challenges posed by commodity price volatility in commodity-exporting EMDEs (Arroyo Marioli and Vasishta 2025). In the case of fiscal rules, a supportive institutional environment and broad political consensus are key for sustained fiscal discipline (Fatas, Gootjes, and Mawejje 2025).

## EMDE structural policy challenges

### *Boosting long-term growth and investment*

The ongoing headwinds to the global economy exacerbate the broad-based and sustained slowdown in growth that EMDEs have experienced since the global financial crisis. This has reflected a slowdown in underlying potential growth, mirroring trends in investment, labor

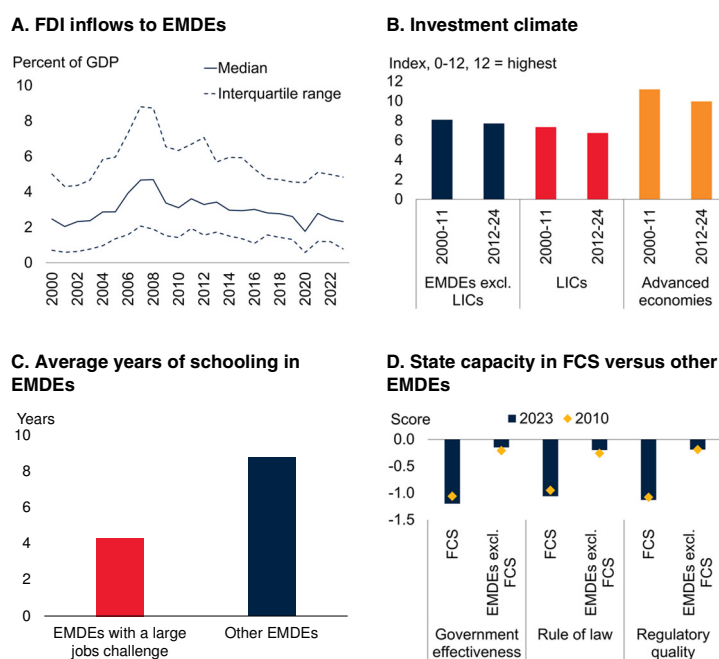
productivity, and labor supply growth. Policies that advance R&D, innovation, and adoption of technology can boost the growth of productivity and potential output (Cirera and Maloney 2017; Kose and Ohnsorge 2024). Reversing the prolonged, widespread slowdown in investment growth is critical for addressing large investment gaps and making progress toward development goals. FDI can help boost domestic investment, generate employment, spread technological innovation, and spur productivity (Amighini, McMillan, and Sanfilippo 2017; Javorcik 2015; Kose, Prasad, and Terrones 2009). Thus, FDI can be a key driver of growth, particularly in countries with sufficiently well-developed financial markets or high levels of human capital (Benetrix, Pallan, and Panizza 2023). Yet, FDI flows to EMDEs as a share of their GDP have also trended down, reflecting a combination of global and country-specific factors (figure 1.16.A). Globally, macroeconomic shocks, elevated uncertainty, and escalating geopolitical tensions have dampened FDI. In many EMDEs, progress with institutional reforms has stalled since the 2000s, weakening the investment climate and discouraging FDI inflows (World Bank 2025a).

To bolster long-term growth prospects, EMDEs need to reinvigorate key policy reforms to accelerate investment growth, including by improving the institutional and business environment. Regulatory reforms can enable innovation by lowering barriers to entry, reducing bureaucratic hurdles, and stimulating competition (World Bank 2025a). In the medium to long term, such reforms can also promote economic diversification. In addition, enhancing competition policy is vital for creating a fair and dynamic market landscape. By curbing monopolistic practices and enabling a level playing field, and by effectively regulating markets that lack competitiveness, such policies can boost innovation and improve economic efficiency (World Bank 2020, 2024a).

Supportive structural conditions are also essential for attracting FDI inflows. These include solid macroeconomic fundamentals; high-quality institutions; political, regulatory, and socioeconomic stability; strong human capital and productivity growth; financial development; and trade and

## FIGURE 1.16 EMDE structural policy challenges

FDI inflows to EMDEs, as a share of their GDP, have trended down since the 2010s. Institutional quality in EMDEs, especially in LICs, generally lags advanced economies, with no progress seen in investment climate indicators over the past decade. To confront the jobs challenge, EMDEs need to enhance human capital, including by boosting spending on education to increase the average years and quality of schooling. FCS face persistent risks of violence and instability, often fueled by weak state capacity, as indicated by measures of government effectiveness, rule of law, and regulatory quality.



Sources: PRS Group's International Country Risk Guide (ICRG); UN Population Prospects (database); WDI (database); World Bank; Worldwide Governance Indicators (database).

Note: EMDEs = emerging market and developing economies; FCS = fragile and conflict-affected situations; FDI = foreign direct investment; LICs = low-income countries. The FCS group is based on the current World Bank classification.

A. Annual medians and interquartile ranges of FDI-to-GDP ratios. Balanced sample of 134 EMDEs.

B. Medians of ICRG Investment Profile Index. Sample includes 36 advanced economies and 102 EMDEs, of which 18 are LICs.

C. Panel shows the unweighted average years of schooling by EMDE group at the latest years of observations. EMDEs facing a large jobs challenge are those with a projected working-age population increase of 50 percent or more between 2025 and 2050.

D. Panel shows simple averages. Higher values reflect better outcomes across each indicator, which range from a minimum of -2.5 to a maximum of 2.5. Sample includes 148 EMDEs, of which 34 are FCS.

investment openness. EMDEs, especially LICs, generally lag advanced economies in terms of the quality of institutions, having made no progress over the past decade in improving features such as the investment climate (figure 1.16.B). Given the significance of institutional quality for both encouraging FDI and enhancing its macroeconomic benefits, it is imperative for EMDEs, particularly LICs, to intensify reform efforts in this area.

## Meeting the jobs challenge amid structural change

The challenge of creating sufficient employment opportunities for growing working-age populations is looming in many EMDEs, particularly in the poorest regions (Chrimes, Kose, and Stamm forthcoming). Between 2025 and 2030, over 600 million young people are expected to join the ranks of the working-age population in EMDEs, with the net working-age population increasing by around 250 million over the same period. SSA, especially FCS economies in the region, and SAR will account for four-fifths of this net increase. In addition, in some regions, such as SAR, the jobs challenge reflects low employment prospects for the female labor force (World Bank 2024b). The challenge also extends over the longer term in some regions: the projected increase in the working-age population over the next quarter-century in SSA is larger than any region has experienced over a 25-year period in the past.

The task of creating sufficient employment opportunities is complicated by the challenging global context, especially as key drivers of growth—notably, trade integration—have weakened significantly over recent decades and now face an even more extreme disruption (Kose and Ohnsorge 2024). Overlapping crises that have hit the global economy since 2020 have damaged fiscal positions, including in many of the countries most affected by the jobs challenge (Mawejje 2024). Evolving structural shifts, including shifts in trade relations and uncertainty about new technologies such as AI, as well as the need to manage the energy transition, add to uncertainty around employment prospects (Cazzaniga et al. 2024; Feriga et al. 2024; IMF 2022a).

Job creation strategies should focus on three pillars: foundational infrastructure for jobs; strengthening governance and supporting business-enabling policies; and mobilizing private capital. These broad pillars include measures to accelerate economic growth, upskill workers, and improve the functioning of labor markets to better match potential workers and firms (Chrimes, Kose, and Stamm forthcoming). Policies to promote macroeconomic stability and robust, effective institutions are crucial. These need to be

complemented with targeted interventions to encourage a more flexible and responsive labor market (including by reducing labor barriers to the formal sector), improve access to finance, address structural bottlenecks (such as barriers to competition, trade, and investment), and support a facilitative business regulatory environment (Kose and Ohnsorge 2024). Investments in key physical and digital infrastructure are also vital. To enhance human capital, EMDEs need to boost spending on education to increase the average years of schooling and the quality of education (figure 1.16.C). Moreover, aggregate job creation is not the only employment-related consideration for policy makers: the quality of jobs is also critically important. Job quality can be enhanced by boosting productivity, in part through the upskilling of existing, including younger, workers; addressing informality; and ensuring adequate working conditions. Strategies can also pay particular attention to sectors with high job-creation potential.

### *Tackling rising conflicts and associated damage*

Addressing the rising incidence of conflict in EMDEs is essential for fostering peace and promoting growth and development in some of the most vulnerable countries. Intense armed conflicts lead to destruction of human and physical capital, often culminating in deep recessions and large output losses (Dieppe, Kilic Celik, and Okou 2020; Federle et al. 2024). Conflicts can also have adverse spillovers, decreasing trade flows and reducing private investment in neighboring states (Abdel-Latif et al. 2024; Rauschendorfer and Shepherd 2022). FCS face persistent risks of violence and instability,

often fueled by deep-seated grievances, exclusion, inequality, and weak governance (World Bank 2020). For instance, state capacity in FCS, as indicated by measures of government effectiveness, rule of law, and regulatory quality, lags other EMDEs (figure 1.16.D).

Although the roots of armed conflicts and instability are complex and context-specific, addressing these challenges requires a proactive approach—tailored to each country’s needs—that prioritizes conflict prevention, fosters inclusive development, and strengthens resilience to adverse shocks (United Nations and World Bank 2018). Investing in early-warning systems and conflict prediction mechanisms enables proactive interventions, which are more cost-effective than post-violence responses (Mueller et al. 2024). For example, counter-cyclical macroeconomic policies and job creation programs can help reduce the risk of violent conflict (Akanbi et al. 2021; Blattman and Annan 2016). During active conflicts, protecting civilians, providing humanitarian relief, and preserving critical institutions—such as central banks, legal systems, and public service infrastructure—can lessen the costs of violence while supporting faster, more inclusive recoveries (Gillard 2024). Effective disarmament, demobilization, and reintegration programs are also crucial for stabilizing post-conflict societies, alongside policies that strengthen institutions, including electoral and justice systems (Ayissi 2020). Sustaining recovery requires investments in basic infrastructure, education, healthcare, and social protection, while expanding financial inclusion and leveraging the private sector to drive inclusive growth.

**TABLE 1.2 Emerging market and developing economies<sup>1</sup>**

Commodity exporters <sup>2</sup>		Commodity importers <sup>3</sup>	
Algeria*	Lao PDR	Afghanistan	Serbia
Angola*	Liberia	Albania	Somalia, Fed. Rep.
Argentina	Libya*	Antigua and Barbuda	Sri Lanka
Armenia	Madagascar	Bahamas, The	St. Kitts and Nevis
Azerbaijan*	Malawi	Bangladesh	St. Lucia
Bahrain*	Mali	Barbados	St. Vincent and the Grenadines
Belize	Mauritania	Belarus	Syrian Arab Republic
Benin	Mongolia	Bosnia and Herzegovina	Thailand
Bhutan*	Mozambique	Bulgaria	Tonga
Bolivia*	Myanmar*	Cambodia	Tunisia
Botswana	Namibia	China	Türkiye
Brazil	Nicaragua	Djibouti	Tuvalu
Burkina Faso	Niger	Dominica	Vanuatu
Burundi	Nigeria*	Dominican Republic	Viet Nam
Cabo Verde	Oman*	Egypt, Arab Rep.	
Cameroon*	Papua New Guinea	El Salvador	
Central African Republic	Paraguay	Eswatini	
Chad*	Peru	Georgia	
Chile	Qatar*	Grenada	
Colombia*	Russian Federation*	Haiti	
Comoros	Rwanda	Hungary	
Congo, Dem. Rep.	São Tomé and Príncipe	India	
Congo, Rep.*	Saudi Arabia*	Jamaica	
Costa Rica	Senegal	Jordan	
Côte d'Ivoire	Seychelles	Kiribati	
Ecuador*	Sierra Leone	Lebanon	
Equatorial Guinea*	Solomon Islands	Lesotho	
Eritrea	South Africa	Malaysia	
Ethiopia	South Sudan*	Maldives	
Fiji	Sudan	Marshall Islands	
Gabon*	Suriname	Mauritius	
Gambia, The	Tajikistan	Mexico	
Ghana*	Tanzania	Micronesia, Fed. Sts.	
Guatemala	Timor-Leste*	Moldova	
Guinea	Togo	Montenegro	
Guinea-Bissau	Trinidad and Tobago*	Morocco	
Guyana*	Uganda	Nauru	
Honduras	Ukraine	Nepal	
Indonesia*	United Arab Emirates*	North Macedonia	
Iran, Islamic Rep.*	Uruguay	Pakistan	
Iraq*	Uzbekistan	Palau	
Kazakhstan*	West Bank and Gaza	Panama	
Kenya	Yemen, Rep.*	Philippines	
Kosovo	Zambia	Poland	
Kuwait*	Zimbabwe	Romania	
Kyrgyz Republic		Samoa	

\* 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; Czechia; 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. Since Croatia became a member of the euro area on January 1, 2023, it has been removed from the list of EMDEs, and related growth aggregates, to avoid double counting.

2. An economy is defined as commodity exporter when, on average in 2017-19, either (1) total commodities exports accounted for 30 percent or more of total exports or (2) 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 EMDEs not classified as commodity exporters.

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