WORLD BANK GROUP
Equitable Growth, Finance & Institutions
Prospects Group

# Global Monthly

January 2023

## Overview

- Global growth is expected to decelerate sharply to 1.7 percent in 2023—driven by aggressive contractionary monetary policy, tighter financial conditions, and weaker confidence.
- Oil prices have declined from their mid-2022 peak amid demand concerns with Brent prices expected to moderate to an average of $88/bbl in 2023.

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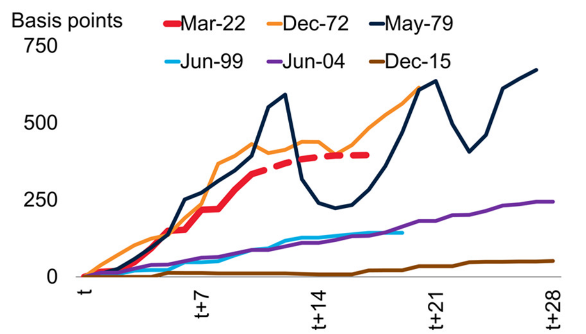
## Chart of the Month

- Very high inflation has triggered unexpectedly rapid and synchronous monetary policy tightening around the world.
- G7 central banks have raised their policy rates at a pace not seen in more than 40 years, with more tightening expected in 2023.
- Higher policy rates led to tighter financial conditions, with rising borrowing spreads for the most vulnerable emerging market and developing economies (EMDEs).

**G7 policy rates**




*Sources*: Haver Analytics; World Bank.
Short-term policy rate weighted by nominal GDP in current U.S. dollars. "t" is the month before the U.S. policy rate increases. March 2022 cycle extended using market-implied interest rate expectations from January 2023 onward, observed on December 16, 2022.

## Special Focus: Overlapping Crises and Challenges in Small States

- Small states were hit particularly hard by the pandemic, and have had a much slower recovery than other EMDEs.
- These countries are particularly vulnerable to global developments, especially climate change, which poses existential risks and increases the frequency and intensity of weather-related natural disasters.
- Domestic reforms can boost growth and resilience, but small states require substantial international support.

The *Global Monthly* is a publication of the Prospects Group. This edition was prepared by Patrick Kirby and Nikita Perevalov under the supervision of Carlos Arteta, based on contributions from Prospects Group staff. The special focus was prepared by Patrick Kirby. This *Global Monthly* reflects data available up to January 18, 2023. For more information, visit: www.worldbank.org/prospects. Back issues of this report are available since 2008.

## Monthly Highlights

**Global activity: persistent weakness.** Global growth is expected to decelerate sharply to 1.7 percent in 2023—the third weakest pace of growth in nearly three decades, overshadowed only by the global recessions of 2020 and 2009 (figure 1.A). To rein in high inflation and bolster credibility, major central banks have tightened policy at the fastest pace in more than 40 years. Aggressive monetary policy tightening to contain high inflation, deteriorating financial conditions, declining confidence, and widespread energy shortages have contributed to a downgrade in global growth by 1.3 percentage points.

**Global trade: softening goods demand.** Global trade growth decelerated in the second half of 2022, as activity in major economies slowed and demand shifted toward its pre-pandemic composition, from goods to services. Despite this moderation, goods trade surpassed pre-pandemic levels last year, while services trade continued to recover. Global trade growth is expected to decelerate further to 1.6 percent in 2023, largely reflecting weakening global demand (figure 1.B).

**Commodity markets: prices down from earlier peaks.** Most commodity prices, including oil, have eased since mid-2022, to varying degrees, due to slowing global growth (figure 1.C). European natural gas prices surged to all-time high in August but have since fallen back toward preinvasion levels as inventories filled and mild weather reduced demand for natural gas for heating. Agricultural prices remain high but have also declined, particularly for wheat and vegetable oils, reflecting higher-than-expected crop yields, as well as a resumption of some exports from Ukraine. Concerns about food availability due to the invasion of Ukraine prompted many countries to impose export bans and other trade restrictions. The extent of these restrictions, in both absolute numbers and as a share of caloric intake, have been comparable with those during the 2008 food price spike. However, they have not affected global markets as much as those imposed in 2008.

**Global financial conditions: tight conditions persist.** Global financial conditions have tightened sharply, with risk appetite dampened by slowing global growth, persistently elevated inflation, and faster-than-expected monetary policy tightening. Long-term government bond yields in the United States and Germany increased at their fastest pace in nearly three decades

**FIGURE 1.A GDP growth**

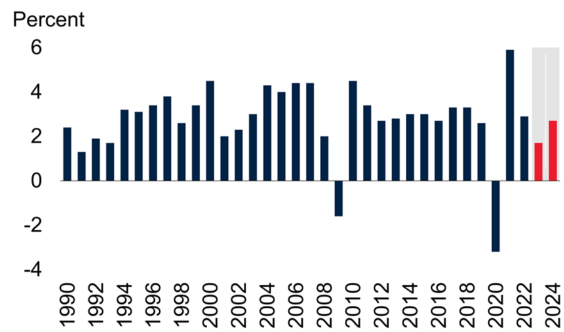



**FIGURE 1.B Global trade**

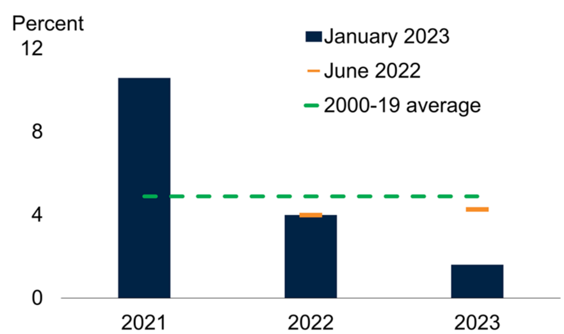
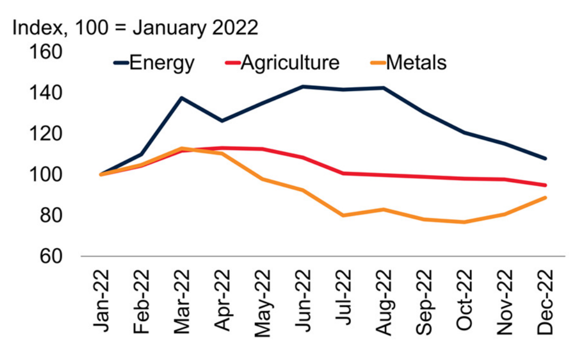



**FIGURE 1.C Commodity prices**




*Sources*: Bloomberg; Haver Analytics; World Bank.
A. Sample includes up to 37 advanced economies and 144 EMDEs. Shaded areas indicate forecasts.
B. Trade is measured as the average of export and import volumes. June 2022 refers to forecasts presented in the June 2022 edition of the Global Economic Prospects report.
C. Last observation is December 2022.

in 2022, reaching their highest levels since 2007 and 2011, respectively, in October. As in past tightening episodes, higher monetary policy rates in advanced economies weighed on EMDE capital inflows, with investors shying away from the debt of the most vulnerable EMDEs before a tentative turnaround in early 2023. The U.S. dollar appreciated markedly in 2022, by about 14 percent on a GDP-weighted basis by October, before moderating somewhat later in the year (figure 2.A). Energy importers with weak credit ratings saw especially sharp increases in sovereign spreads, adding to the difficulty of financing large current account deficits (figure 2.B). Spreads on dollar-denominated debt exceeded 10 percentage points in about one-in-five EMDEs last year, effectively locking them out of global debt markets. This is up from less than one-in-fifteen in 2019.

**United States: avoiding a recession.** In the United States, rising food and energy prices, together with a tight labor market, pushed inflation to multi-decade highs in 2022, before price pressures began easing toward the end of the year (figure 2.C). This has prompted the most rapid monetary policy tightening in more than 40 years. Growth is projected to slow to 0.5 percent in 2023—1.9 percentage points below previous forecasts. Inflation is expected to moderate in 2023 as labor markets soften and wage pressures abate.

**Other advanced economies: weaker growth.** In the euro area, activity in the first half of 2022 exceeded expectations, resulting in annual growth being revised up to 3.3 percent. In the second half of last year, however, activity weakened substantially as a result of soaring energy prices and supply uncertainty, compounded by rising borrowing costs. Inflation rose to record highs as Russia's invasion of Ukraine led to natural gas supply cuts and surging energy prices—which, despite some recent moderation, remain well above pre-invasion levels (figure 3.A). Broad-ranging fiscal measures introduced by European governments, estimated at 1.2 percent of GDP in 2022 and almost 2 percent of GDP in 2023, aimed to cushion the impact of energy price increases on households and businesses. The euro area will likely avoid a recession for the full calendar year. However, there will be no growth (0 percent) in 2023, as the full impact of energy supply shocks and higher monetary policy rates is felt by consumers and businesses. In Japan, growth is expected to slow further to 1 percent in 2023, alongside a slowdown in other advanced economies.

**FIGURE 2.A EMDE currency depreciation against the U.S. dollar in 2022**

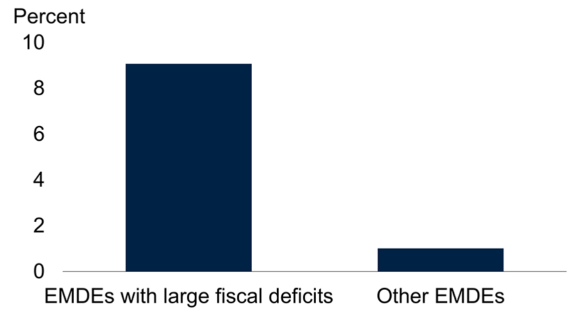



**FIGURE 2.B EMDE sovereign spread changes in 2022, by credit rating and energy exporter status**

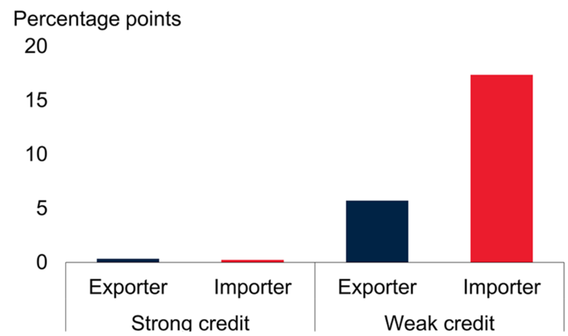
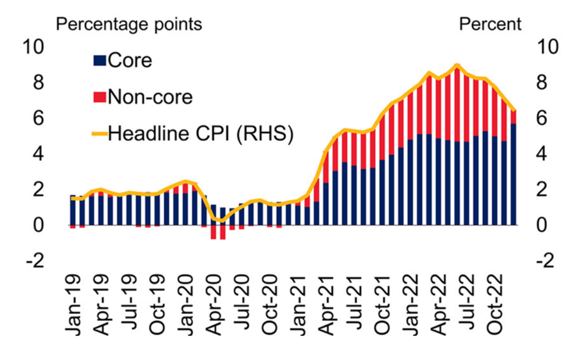



**FIGURE 2.C CPI inflation in the United States**




*Sources*: Bloomberg; Federal Reserve Economic Data; WEO (database); World Bank.

*Note*: EMDE = emerging market and developing economies.

A. Simple average of change in U.S. dollar exchange rates for 114 EMDEs with estimated fiscal deficits greater (less) than 3 percent of GDP in 2022. Last observation is December 16, 2022.

B. Change in EMBI spreads since January 2022, using Moody's sovereign foreign currency ratings. Sample includes 11 EMDE energy exporters and 35 EMDE energy importers. Strong credit defined as ratings from Aaa to Baa3. Weak credit defined as ratings from Caa to Ca. Sample excludes Belarus, the Russian Federation, and Ukraine. Last observation is December 13, 2022.

C. CPI refers to consumer price index. Bars show contributions to year-on-year headline CPI inflation. Last observation is December 2022.

**China: rebounding growth.** Many indicators of economic activity in China deteriorated markedly in 2022 (figure 3.B). COVID-19 related restrictions, unprecedented droughts, and ongoing property sector stress restrained consumption, production, and residential investment. Property sales, housing starts, and new-home prices have continued to decline, and several property developers have defaulted on their debt obligations. Infrastructure-focused fiscal support, policy rate and reserve requirement ratio cuts, and regulatory easing measures have only partially offset these headwinds. In all, growth slowed to 3 percent in 2022, 1.3 percentage points below June 2022 forecasts—and, with the exception of 2020, the weakest pace of growth since the mid-1970s. In 2023 growth is expected to rebound to 4.3 percent, as the lifting of pandemic restrictions releases pent-up consumer spending.

**Other EMDEs: subdued growth.** Activity in EMDEs other than China decelerated sharply in 2022 to an estimated 3.8 percent from 5.8 percent in the previous year, as global financial conditions tightened, high inflation weighed on consumer spending, weakness in the world's largest economies dampened external demand, and spillovers from the Russian Federation's invasion of Ukraine persisted. On average, growth in 2023 is expected to weaken further, averaging 2.7 percent and leaving output in EMDEs other than China 5.7 percent below the pre-pandemic trends in 2023. This is considerably worse than the output loss in advanced economies (figure 3.C).

**FIGURE 3.A Euro area electricity prices**

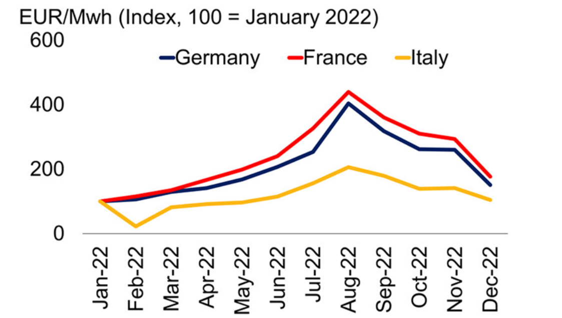



**FIGURE 3.B Industrial production, retail sales, export, and import growth in China**

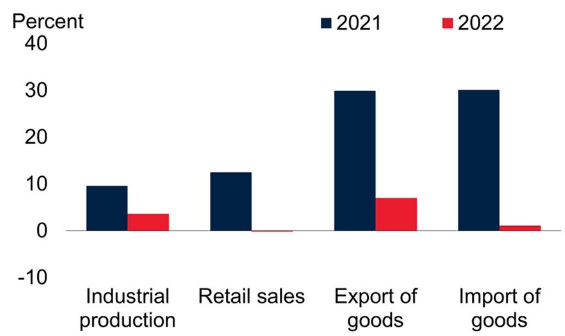
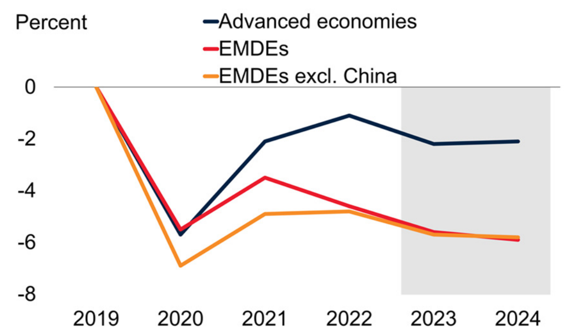



**FIGURE 3.C Deviation of output from pre-pandemic trends**




*Sources*: Bloomberg; Haver Analytics: World Bank.
*Note*: EMDEs = emerging market and developing economies.
A. Figure shows one-year-forward baseload electricity prices. Last observation is December 2022.
B. Bars denote the year-to-date real growth of industrial production from January to November and year-to-date nominal growth of retail sales and goods exports and imports from January to November. Last observation is December 2022.
C. Figure shows the percent deviation between the current estimates and forecasts released in the January 2020 edition of Global Economic Prospects. For 2023 and 2024, the January 2020 baseline is extended using projected growth for 2022.

## Special Focus: Overlapping Crises and Challenges in Small States

Small states—countries with a population of 1.5 million or less—were hit particularly hard by the COVID-19 pandemic, and have had a much slower recovery than other emerging market and developing economies (EMDEs; figure 4.A). These countries are particularly vulnerable to global developments, especially climate change. Policy makers in small states have limited tools at their disposal but, with the support of the global community, they can nonetheless take steps to reverse pandemic-related losses and reduce vulnerability to future crises.

**Small state economies shrank drastically during the pandemic.** Small states tend to concentrate output and exports in a limited set of industries, most commonly tourism—tourism expenditures were equivalent to an average of 18 percent of economic activity in small states prior to the pandemic, and substantially more in some countries (figure 4.B). Tourism fell precipitously in 2020, with arrivals falling 70 percent compared to only about 4 percent during the 2009 global recession. This pushed small states into an especially deep recession, with aggregate output contracting by more than 11 percent in 2020, about seven times as much as in other EMDEs.

**The recovery in small states has been slow.** Following the unprecedented economic contraction in 2020, the return to the level of output prevailing before the pandemic has been slow. Small states are forecast to grow 3.5 percent in 2023, slowing from an estimated 5.2 percent in 2022. The 2023 growth forecasts for about two-thirds of small states have been downgraded relative to the June forecast. The recovery in small states has been delayed by elevated energy and food prices, which represent a large proportion of imports in these economies (figure 4.C). Slowing external demand and rising borrowing costs pose further challenges for small states, particularly those with sizeable stocks of government debt at variable interest rates or heavily indebted private sectors. As a result of these headwinds, aggregate GDP in small states is forecast to surpass its 2019 level of GDP only in 2023, two years later than other EMDEs.

**Small states are vulnerable to shocks.** Small states share many characteristics that magnify their sensitivity to external shocks

**FIGURE 4.A GDP compared to pre-pandemic levels**

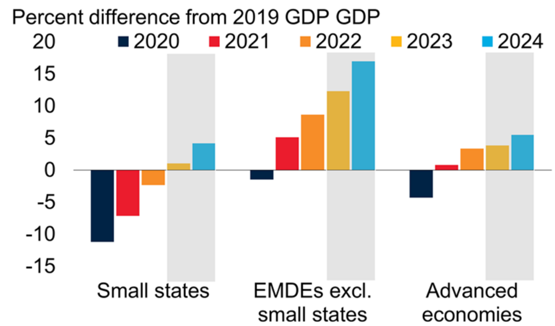



**FIGURE 4.B Inbound tourism expenditure**

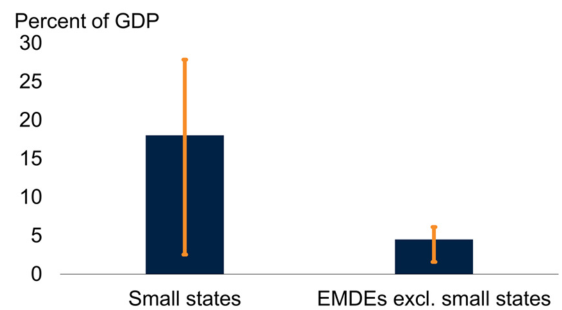
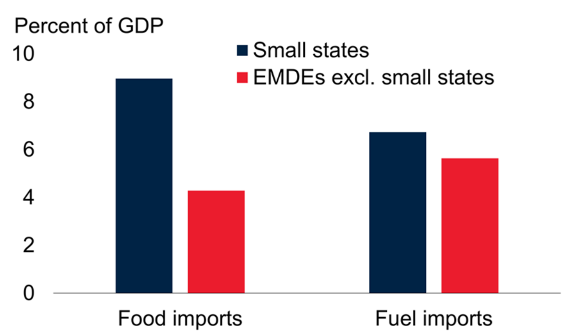



**FIGURE 4.C Food and fuel imports**




*Source*: Haver Analytics; International Monetary Fund; UN World Tourism Organization; World Bank.
Note: EMDEs = emerging market and developing economies.
A. Growth rates are calculated using GDP weights at average 2010-19 prices and market exchange rates.
B. Bars show averages of indicated country groups. Vertical lines show interquartile ranges within groups. Data for 2019. Sample includes 22 EMDE small states and 81 EMDEs excluding small states.
C. Bars show simple averages. Data for 2019. Food imports sample includes 22 EMDE small states and 95 EMDEs excluding small states. Fuel imports sample includes 18 EMDE small states and 78 EMDEs excluding small states. Energy exporting EMDEs were dropped from the fuel imports sample.

and contribute to greater growth volatility (figure 5.A). These include remoteness, economic concentration, and very high levels of openness to trade. As a group, small states tend to run fiscal deficits and depend on a mixture of aid and foreign direct investment to finance large current account deficits. On average, small states have higher public debt levels than other EMDEs. These vulnerabilities are further magnified by the fact that most small states lack two important mechanisms for buffering shocks: floating exchange rates and independent monetary policy. Small state governments are large as a share of GDP, but often too small to achieve economies of scale and effectively provide many public services.

Small states face growing risks from climate change. The frequency and intensity of weather-related natural disasters in these countries has increased in recent decades, and small states face severe, in some cases existential, threats from rising sea levels and coastal erosion. Small states, many of which are islands, suffer disaster-related damages and losses of close to 5 percent of GDP per year, on average (figure 5.B). In extreme cases, damages from a single disaster can be several multiples of the country's total GDP. Estimated damages and losses from Hurricane Maria in 2017 in Dominica and Hurricane Ivan in Grenada in 2004, for example, amounted to more than 200 percent of GDP.

**Domestic reforms and international support can boost growth and resilience.** Accelerating growth while building resilience to future shocks will require extensive domestic efforts, but these are unlikely to be sufficient without support from the global community. Small states can diversify their economies and better integrate with global markets by improving private sector business environments and enhancing both digital and physical connectivity. They can also limit vulnerability to shocks by investing in climate adaptation, enhancing disaster risk management, lessening dependence on imported fossil fuels, and rebuilding fiscal buffers. Where feasible, small states can collaborate with major trading partners and each other to achieve economies of scale and reduce trade costs (figure 5.C).

The international community can help through various forms of financing and helping small states deal with excessive debt. It can also assist by providing technical assistance to build institutional capacity; enhancing pandemic preparedness; delivering on commitments to tackle climate change; and promoting open, rules-based global trade and investment networks.

**FIGURE 5.A Volatility of growth in small states, 2000-21**

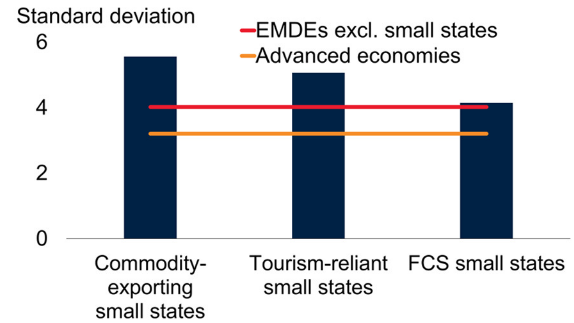



**FIGURE 5.B Damages and losses from natural disasters, 1990-2021**

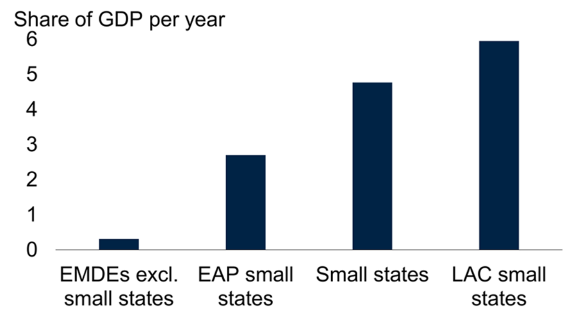
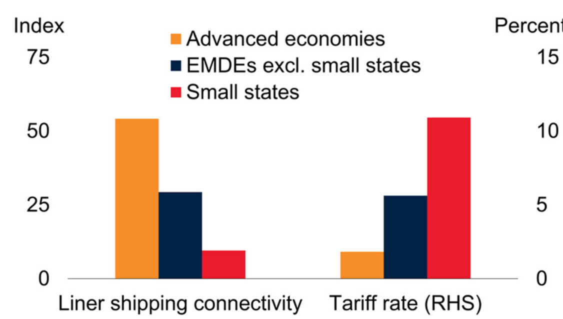



**FIGURE 5.C Trade connectivity and costs**




Source: EM-DAT; World Bank; World Development Indicators.
*Note*: EMDEs = emerging market and developing economies.
A. Average of standard deviations of growth from 2000-21 for countries in each group. Sample contains 12 commodity-exporting, 22 tourism-reliant, and 6 FCS small states. Sample contains 113 EMDEs excluding small states. Extreme outliers are excluded.
B. Bars show the sum of damages in each group of countries in each year divided by the sum of nominal GDP in each group of countries, weighted by country-level nominal GDP.
C. Simple averages of countries in each group. Liner shipping connectivity is an index based on number of ships, their container-carrying capacity, maximum vessel size, number of services, and number of companies that deploy container ships in a country's ports; data for 2020. Tariff rate is the weighted mean import tariff on all products. Data for 2018.

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Commodity Markets: Evolution, Challenges, and Policies
Commodity Markets Outlook – October 2022
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Africa's Pulse
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Middle East and North Africa Economic Update
South Asia Economic Focus

## TABLE: Major Data Releases

(Percent change, y/y)

| Recent releases: December 19, 2022 - January 18, 2023 | | | | | |
|---|---|---|---|---|---|
| **Country** | **Date** | **Indicator** | **Period** | **Actual** | **Previous** |
| Japan | 12/22/22 | CPI | NOV | 3.8% | 3.8% |
| United Kingdom | 12/22/22 | GDP | Q3 | 1.9% | 4.0% |
| United States | 12/22/22 | GDP | Q3 | 1.9% | 1.8% |
| Netherlands | 12/23/22 | GDP | Q3 | 3.1% | 5.2% |
| South Korea | 12/29/22 | CPI | DEC | 5.0% | 5.0% |
| Indonesia | 1/1/23 | CPI | DEC | 5.5% | 5.4% |
| Germany | 1/3/23 | CPI | DEC | 8.5% | 10.1% |
| Türkiye | 1/3/23 | CPI | DEC | 64.3% | 84.4% |
| Italy | 1/5/23 | CPI | DEC | 11.6% | 11.8% |
| Mexico | 1/9/23 | CPI | DEC | 7.8% | 7.8% |
| Brazil | 1/10/23 | CPI | DEC | 5.8% | 5.9% |
| Argentina | 1/12/23 | CPI | DEC | 94.8% | 92.4% |
| India | 1/12/23 | CPI | DEC | 5.7% | 5.9% |
| United States | 1/12/23 | CPI | DEC | 6.4% | 7.1% |
| Euro area | 1/13/23 | IP | NOV | 1.9% | 2.7% |
| France | 1/13/23 | CPI | DEC | 5.8% | 6.1% |
| Russian Federation | 1/13/23 | CPI | DEC | 11.9% | 12.0% |
| Saudi Arabia | 1/15/23 | CPI | DEC | 3.3% | 2.9% |
| China | 1/16/23 | GDP | Q4 | 2.9% | 3.9% |
| Nigeria | 1/16/23 | CPI | DEC | 21.3% | 21.5% |
| Canada | 1/17/23 | CPI | DEC | 6.5% | 6.9% |

(Percent change, y/y)

| Upcoming releases: January 19, 2023 - February 18, 2023 | | | | |
|---|---|---|---|---|
| **Country** | **Date** | **Indicator** | **Period** | **Previous** |
| Japan | 1/19/23 | CPI | DEC | 3.8% |
| South Korea | 1/23/23 | GDP | Q4 | 3.1% |
| Australia | 1/25/23 | CPI | Q4 | 7.3% |
| United States | 1/26/23 | GDP | Q4 | 1.9% |
| Spain | 1/27/23 | GDP | Q4 | 4.4% |
| Euro area | 1/31/23 | GDP | Q4 | 2.3% |
| Germany | 1/31/23 | CPI | JAN | 8.5% |
| Italy | 1/31/23 | GDP | Q4 | 2.6% |
| Mexico | 1/31/23 | GDP | Q4 | 4.3% |
| Indonesia | 2/1/23 | GDP | Q4 | 5.7% |
| Italy | 2/1/23 | CPI | DEC | 11.6% |
| France | 2/3/23 | IP | DEC | 0.7% |
| Germany | 2/7/23 | IP | DEC | -0.5% |
| India | 2/10/23 | IP | DEC | 7.1% |
| Italy | 2/10/23 | IP | DEC | -3.5% |
| Mexico | 2/10/23 | IP | DEC | 3.2% |
| United Kingdom | 2/10/23 | IP | DEC | -5.2% |
| Japan | 2/13/23 | GDP | Q4 | 1.7% |
| Netherlands | 2/14/23 | GDP | Q4 | 3.1% |
| United States | 2/14/23 | CPI | JAN | 6.4% |
| Poland | 2/15/23 | GDP | Q4 | 4.5% |