HIGHLIGHTS from Chapter 3:

Investment Growth after the Pandemic

Key Points

- *Following a decade-long investment growth slowdown in emerging market and developing economies (EMDEs), the COVID-19 pandemic triggered a sharp investment contraction.*
- *Investment growth is projected to average 3.5 percent in EMDEs in 2022-24, half the long-term average. Weak investment growth has lasting implications for long-term output growth and EMDEs' ability to reach key development and climate-related goals.*
- *A variety of fiscal and structural policies to boost public and private investment, as well as mobilization of sufficient financing, are necessary to promote investment in EMDEs.*

Damage from the pandemic. Emerging market and developing economies (EMDEs) experienced a decade-long investment growth slowdown prior to the COVID-19 pandemic. The slowdown reflected trends in private and public investment, and in commodity-exporting and commodity-importing EMDEs, but slowing investment growth in China made a large contribution to the aggregate EMDE slowdown (figure A). As the pandemic inflicted a global recession in 2020, investment contracted in 70 percent of EMDEs, well above the 55 percent of EMDEs that experienced an investment contraction during the previous global recession, in 2009. Following a robust rebound in 2021, investment growth is projected to average 3.5 percent per year in 2022-24, half the average annual growth rate during 2000-21 (figure B). The sluggish recovery means that in 2024, the level of investment in EMDEs is projected to be about 15 percent above the pre-pandemic level of 2019. By comparison, at a similar point after the 2009 global recession, investment in EMDEs was already nearly 50 percent above the pre-recession level (figure C).

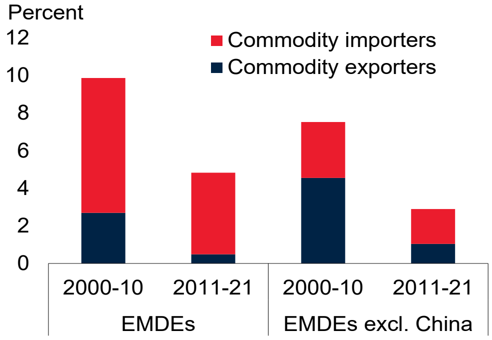
Implications of weak investment growth. Weak investment growth in EMDEs is concerning because it is associated with weak global trade and dampens potential growth through slower capital accumulation and weaker productivity growth, the latter with adverse implications for EMDEs' ability to catch up with advanced economy per capita incomes. Lackluster investment growth will hinder EMDEs' ability to meet the Sustainable Development Goals and fulfill climate commitments under the Paris Agreement.

Reforms to boost investment growth. Constrained fiscal space and uncertain macroeconomic conditions will make boosting investment in EMDEs challenging. A comprehensive set of fiscal and structural policies, tailored to country circumstances, combined with mobilization of additional financing, are necessary to promote investment growth. Spending on public investment can be boosted by reallocating expenditures toward growth-enhancing investment, improving public spending efficiency, or mobilizing domestic resources through, for example, strengthened tax administration or increased revenue collection. In the past, reforms to address a range of investment climate impediments and inefficiencies have been associated with an increase in investment growth (figure D). Establishing frameworks for public-private partnerships for infrastructure investments is also important. Two areas with strong growth potential are investment in digital capabilities and the clean energy transition.

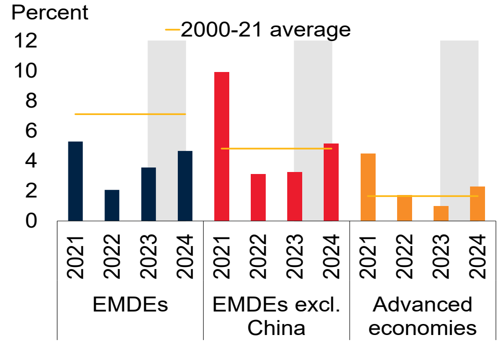
Figure 1. Investment growth after the pandemic

EMDEs experienced a decade-long and geographically widespread investment growth slowdown in the 2010s. Investment growth is expected to remain weak following the COVID-19 pandemic. Due to the large share of EMDEs impacted by the 2020 global recession, the investment recovery is proceeding more slowly than the recovery after the 2009 global recession. Investment growth in EMDEs is projected to be below its 2000-21 average rate in 2023 and 2024. Past reform spurts to improve the investment climate lifted investment growth significantly.

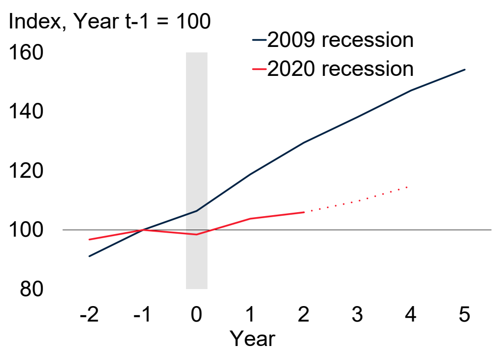
A. Investment growth



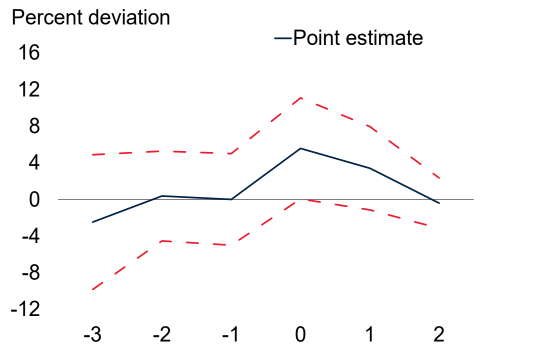
B. Investment growth forecasts



C. Investment in EMDEs



D. Investment growth around reform spurts



Sources: Haver Analytics; World Bank; World Development Indicators.
Note: EMDEs = emerging market and developing economies. Investment refers to gross fixed capital formation. Sample includes 69 EMDEs and 35 advanced economies unless otherwise noted.
A.B. Investment growth is calculated with countries' real annual investment in constant U.S. dollars as weights.
B. Shaded areas are forecasts.
C. On the x-axis, year zero refers to the year of global recessions in 2009 and 2020. Dotted portions of lines are forecasts.
D. Sample includes 60 EMDEs from 1984-2022. Reform spurts are defined in annex 3.2 of chapter 3 of the January 2023 *Global Economic Prospects* report. Solid lines show the increase in investment growth around a reform spurt in year t=0 relative to the countries not experiencing a reform spurt. Dashed lines show the 95 percent confidence interval.