



GROUP OF TWENTY

G20 Summit

Toronto, Canada

June 26-27, 2010

G20 AND GLOBAL DEVELOPMENT

Report prepared by Staff of the World Bank for

G20 Growth Framework and Mutual Assessment Process

THE WORLD BANK

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Executive Summary

As requested by G20 Leaders, this report assesses the outlook for developing countries and highlights policy areas for consideration by the G20 to enhance the collective impact of G20 policies on development and poverty reduction as part of the G20 Growth Framework and Mutual Assessment Process (MAP). Key inputs into this report include the G20 submissions, the base case and alternative scenarios for the G20 developed by the IMF, the World Bank's own data and analysis, and inputs from other international organizations, such as the OECD and WTO. The report's analysis serves as one of the inputs under the MAP to help G20 policymakers identify policy options over the course of 2010.

The main findings and messages of the Bank report can be framed under four themes.

Centrality of Global Growth to Development

- Global growth is central to development. The most important thing that the G20 can do for development is to restore strong growth. As the recovery matures, the longer-term growth agenda should increasingly be at the center of G20 policy coordination, with a shift in focus from demand to supply stimulus—fiscal, financial, and structural reforms that enhance medium- to long-term potential growth. The upside scenario presented in a companion report by the IMF illustrates how collective action by the G20 along these lines can boost global growth with benefits for all. Actions on financing for development and trade discussed in the Bank report and summarized below would enhance the development impact of the upside scenario.
- The crisis and recession in advanced economies significantly impacted developing countries. There is considerable heterogeneity across developing countries, but improvements in macroeconomic policies and progress on structural reforms helped them in general navigate the recent crisis with greater resilience than past crises. Nonetheless, the impact was significant. Growth in developing countries fell from an average of about 7 percent in the five years preceding the crisis to 1.6 percent in 2009. There will be an estimated 64 million more people living in extreme poverty (on less than \$1.25/day) in 2010 than would have been the case without the crisis.
- The base case outlook for developing countries, linked to the IMF's G20 base case scenario, is for growth recovering to about 6 percent in 2010, with a relatively strong recovery in the more dynamic emerging markets and a gradual recovery in other developing countries, including low-income countries. This scenario would still leave sizable output gaps in the medium term. Poverty would still be higher by 53 million people in 2015 compared to the pre-crisis path. The ground lost in progress toward the Millennium Development Goals would not be recovered. For example, 1.2 million more children under 5 might die between 2009 and 2015 than under the pre-crisis growth path.
- The output and social losses could be still greater as the base case growth scenario might not be realized, as it is subject to important downside risks. Concerns about fiscal and debt sustainability in advanced economies have intensified with the developments in Greece. Fiscal strains have also increased in many developing countries, especially low-income countries, as they have used up the limited fiscal space they had in responding to the crisis and now face severe constraints in sustaining core social and infrastructure programs important for poverty reduction and growth.
- The package of G20 fiscal and structural reforms envisioned in the IMF's upside scenario would help address current risks in the global economy and increase potential growth. We estimate that the resulting higher growth in the G20 economies would be associated with 2.4 percent higher GDP in developing countries by 2014 and 14 million fewer people living on less than \$1.25/day (33 million fewer people on less than \$2/day) than in the base case. Conversely, the Fund's downside scenario

illustrates well the likely consequences of lack of action to address the risks. GDP in developing countries could be 3.6 percent lower by 2014 and poverty higher by 23 million people based on \$1.25/day poverty line and 58 million higher based on \$2/day poverty line than in the base case.

Multipolarity: A Dynamic Force in Global Growth and Rebalancing

- Growth in developing countries increasingly matters for global growth. Led by the fast-growing emerging markets, developing countries are now contributing about half of global growth. They are leading the recovery in world trade, with their import demand rising at twice the rate of that in high-income countries. Linkages among developing countries, or South-South linkages, also are becoming more important. South-South trade has risen to about one-third of global trade.
- Developing countries offer abundant opportunities for high return/high growth potential investments, such as in critical infrastructure that removes bottlenecks to growth. Many, however, face a binding financing constraint. Promotion of growth in these countries through more support for investment that removes bottlenecks to their growth would be a global win-win. It would support their development and it would contribute to stronger growth at the global level and to the rebalancing of global growth by creating new markets and investment opportunities and more sources of growth in global demand.
- Promotion of stronger, multipolar growth in developing countries should thus be seen as an important and integral element of the G-20 framework to achieve "strong, sustainable, and balanced growth" in the global economy. Rebalancing needs to look beyond a narrow focus on current account balances and macroeconomic policy adjustments to include structural rebalancing—and supporting multiple poles of growth is a key feature of that structural rebalancing.
- Infrastructure investment and maintenance needs in developing countries amount to \$900-plus billion annually. Actual spending is half that level. More financing is not the only answer; improvements in "soft infrastructure"—in governance, regulation, cost recovery—are as much part of the agenda, as are sustained investments in human capital such as health, nutrition, and education.
- The potential to contribute to global growth and rebalancing is not limited to the rapidly growing emerging market growth poles. Better policies have improved growth performance and opportunities in many low-income countries, including in Sub-Saharan Africa (average growth of about 6 percent in the five years preceding the crisis). They offer markets for investment, not just destinations for aid.
- In addition to financing, the G20 can be instrumental in promoting the sharing of development knowledge and support for capacity building in developing countries.

Financing for Development: Challenging Outlook Demands Creativity

- The crisis will have long-lasting implications for financial flows to developing countries. Some emerging markets are seeing a strong rebound in capital inflows, but most developing countries face the prospect of scarcer and costlier capital. The rise in fiscal deficits and debt in advanced economies and concerns about crowding-out, tighter financial sector regulation, and a re-pricing of risk will all likely raise the cost of capital and limit developing countries' access to financing.
- The tighter financial conditions could lower growth in developing countries by up to 0.7 percentage points annually over the next 5 to 7 years, and reduce potential output by up to 8 percent in the long run, compared with the pre-crisis trend. This baseline outlook is subject to further downside risks in view of the increased concerns about sovereign debt in advanced economies.

- Even relatively small declines in growth can have significant effects on poverty. A 0.5 percentage point decline in developing country growth rate, say due to higher capital costs and lower investment, can mean about 80 million additional people in poverty (\$2/day poverty line) in ten years.
- With tighter capital markets, official flows to developing countries take on added importance, both in directly providing development finance and in leveraging private flows. The need for concessional finance has risen as fiscal space in low-income countries has come under pressure while social spending needs, including expansion of social safety nets for poor and vulnerable groups, have increased in the aftermath of the crisis. These developments reinforce the need to ensure adequate ODA, achieve satisfactory replenishments of IDA and the African Development Fund, and follow through on MDB capital increases. They also point to the need to ensure more effective use of resources to achieve development outcomes.
- The tighter outlook for private capital flows and the fiscal stress in donor countries imply the need for supplementing traditional financing with innovative forms of finance. These include, for example: risk-mitigation guarantees; sovereign wealth fund investments (e.g., recent investments in an IFC equity fund); innovations such as the IFFIm and AMCs that support global public goods in health and strengthening of health systems; public-private partnerships in development-linked global programs, such as for food security; carbon finance; and South-South investments. The scale of resource needs calls for both a renewed commitment by G20 members to key global programs and renewed vigor and creativity in exploiting the potential of innovative approaches that leverage private capital.
- The financing outlook also implies the need for stronger domestic resource mobilization by developing countries, including continued efforts to improve public resource management and the climate for private investment. There is a need to strengthen developing countries' own financial systems. Some aspects of financial sector development, such as SME finance, are already the subject of attention in G20 under the theme of inclusive finance. This is important, but there is also a need to develop financial systems more broadly. Expanded technical and capacity building assistance to financial sector reforms in developing countries can be a key area for G20 collective action.
- It is important to ensure that financial system regulatory reforms in advanced economies do not have unintended adverse effects on financial flows to developing countries or their financial sector management. Vigilance is needed to avoid financial protectionism.

Open Trade: Engine of Growth and Facilitator of Rebalancing

- G20 leaders can boost market confidence by renewing their commitment to refrain from protectionist measures. An even stronger signal would be a collective pledge to unwind the protectionist measures that have been put in place since the onset of the crisis.
- Trade rules matter. Areas that are not subject to multilateral discipline or where the coverage is unclear or limited are the ones that have seen more restrictive actions. Strengthening multilateral trade disciplines and moving ahead with the Doha Round therefore are important.
- To improve poor countries' market access, the G20 could consider extending 100 percent duty-free and quota-free access to the Least Developed Countries with liberal rules of origin. Improved market access for poor countries needs to be complemented with a strengthening of trade facilitation and aid-for-trade programs to enhance these countries' trade capacity.

Introduction

As requested by G20 Leaders, this report assesses the outlook for developing countries and highlights policy areas for consideration by the G20 to enhance the collective impact of G20 policies on development and poverty reduction as part of the G20 Growth Framework and Mutual Assessment Process (MAP).¹ The inclusion of development and poverty reduction as part of this framework provides a valuable opportunity to incorporate development issues more systematically and integrally into G20 policy discussions. Key inputs into this report include the G20 submissions that set out each member country's policy plans and provide key data and projections, the base case and alternative scenarios for the G20 developed by the IMF, the World Bank's own data and analysis, and inputs from other international organizations, such as the OECD and WTO. The report's analysis serves as one of the inputs under the MAP to help G20 policymakers identify policy options over the course of 2010.

The report presents a base case outlook for developing countries and highlights issues and policy implications for consideration by the G20. The analysis of the base case outlook for development is linked to the base case economic scenario for G20 countries developed by the IMF.² The report also assesses the implications for development of the alternative scenarios prepared by the Fund, complemented by some simulations carried out by Bank staff. Based on this analysis, the report identifies areas for attention and options for collective action by the G20 that would enhance the prospects for achievement of the shared growth and development objectives.

The report differentiates between different groups of developing countries to bring out the diversity of impacts, prospects, and challenges across them. There is no simple taxonomy of developing countries. Countries' development prospects depend on a range of factors, for example, the level of development, resource endowments, economic structure, and national policies. Simple definitions and classifications cannot capture these complexities and the interdependencies of today's global economy. The analysis below uses a variety of country categories, including developing countries as a whole, low-income countries, middle-income-countries, middle-income countries that are members of G20, and regional groupings, as appropriate.

The next stage of the MAP will involve identification by the G20 of specific policy measures in the broad policy areas for action identified in the first stage. The next phase of the Bank's analysis will therefore seek to provide more specificity on development policy options and a particular focus on policy options for emerging market members of the G20. However, the coverage of development policies in the first round of G20 submissions was highly variable and in general thin. It will be important that the country templates for the next round of G20 submissions be more specific in terms of the development policies and indicators for which G20 members are expected to provide information.

Four Key Themes

The report is organized around four main themes that emerge from the analysis. First, global development needs robust global growth. As a result, the most important thing that the G20 can do for development is to secure a strong recovery in growth. The G20 provides a very useful forum for policy coordination for that purpose. Second, "reverse linkages" between developing and high-income countries have become increasingly important. Promotion of strong multipolar growth in developing countries would be a global "win-win." It would support development in poorer countries and contribute to strong growth at the

¹ Some of the data presented in the report are preliminary.

² Various IMF staff notes including *Mutual Assessment Process: Analysis and Perspectives*, April 2010; and *G20 Mutual Assessment Process—Alternative Policy Scenarios*, June 2010.

global level. It would also contribute to rebalancing of global growth. Third, the outlook for financing for development will be more challenging in the post-crisis environment and will require creative, innovative approaches. Fourth, keeping trade open will be essential for sustained recovery and enabling the growth rebalancing to work. Trade, together with investment and associated flows of technology, is a key channel for multipolar growth and diversification of global demand.

Theme I: Centrality of Global Growth to Development

The first theme is that global growth is central to development. Through trade and finance linkages, economic outcomes in advanced economies have a significant effect on developing countries. As the recovery matures, the longer-term growth agenda should increasingly be the focus of G20 policy coordination. In advanced economies, this includes fiscal, financial, and structural reforms that enhance long-term growth potential. In developing countries, growth prospects will depend on building on past progress on reforms in macro-fiscal management, investment climate, and governance and achieving requisite investment levels in infrastructure and human capital underpinning growth. Priorities across countries will of course depend on country specific circumstances.

Base Case Outlook for Developing Countries

Economic Growth. Improved macroeconomic policies and structural reforms helped developing countries overall cope with the recent crisis with greater resilience than some past crises. Nonetheless, the impact on their economic growth and progress in poverty reduction and achievement of the Millennium Development Goals (MDGs) was significant. Growth in developing countries fell from an average of about 7 percent in the five years preceding the crisis to 1.6 percent in 2009.³ Behind these general outcomes, there is considerable diversity of experience across countries—both in terms of the impact of the crisis and the policy responses to address it. A lingering impact of the crisis response is that a number of countries face fiscal sustainability concerns that could constrain core, growth-related spending.

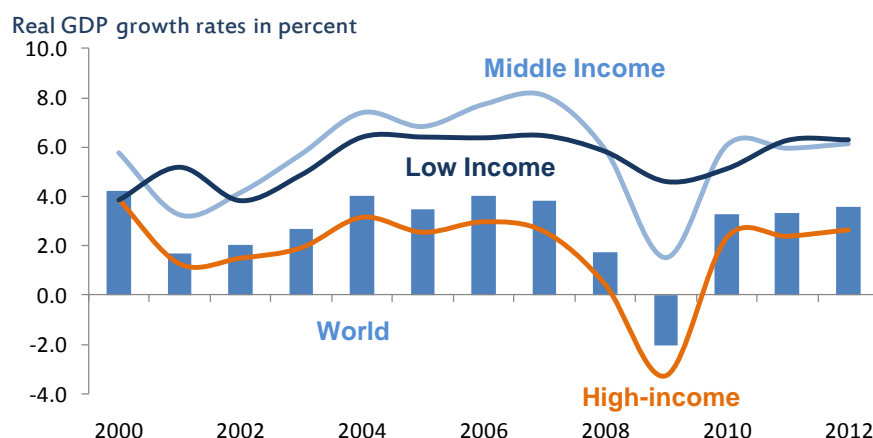
The IMF base case scenario foresees a moderate recovery over the coming five years as economies gradually close output gaps and return to potential growth rates, with the strength of the recovery varying across countries and country groups. From a developing country perspective, there are concerns that the recent recession could impact potential GDP growth rates over the medium-term due to a variety of factors. There is concern that high-income countries' increased public sector financing needs could raise the cost of development finance, and that fiscal stress might also reduce flows of concessional finance.

Linked to the IMF's G20 base case scenario, the outlook for developing countries is for average growth recovering to about 6 percent in 2010-12, with a relatively strong economic recovery in the more dynamic emerging markets and a more gradual recovery in other developing countries, including most low-income countries (Figure 1 and Table 1). Growth in middle-income countries, which were more seriously affected by the financial crisis given their deeper integration with international capital markets, is projected to recover quickly from the low of 1.5 percent in 2009 to around 6 percent, strong but still below average growth of pre-crisis years. Low-income countries were affected by the crisis more through the trade channel. They were initially less impacted by the crisis because of their weaker capital market links but saw their growth drop, though by less than in middle-income countries, as the resulting recession depressed demand for their exports and caused export volumes and commodity prices to decline.

³ Aggregate growth rates in this document are calculated using fixed weights derived from market exchange rates (MER) in 2005. This contrasts with the method employed by the IMF, which uses weights derived from purchasing power parities (PPP). Because developing country GDP measured at PPPs tends to be higher than when measured at market prices and because developing country growth rates are higher than high-income country growth rates, PPP-based global growth rates tend to be higher than MER-based rates.

Countries with a heavier dependence on a few commodity exports were impacted more severely. Low-income country growth could return to about 5 percent in 2010, again with some ground to cover to return to the pre-crisis growth rates. Excluding China and India, developing country growth is projected to be around 4.5 percent in 2010-12.

Figure 1: Growth is recovering but sustainability will depend on supportive policies



Source: World Bank staff calculations.

Table 1: Base case growth outlook for developing countries

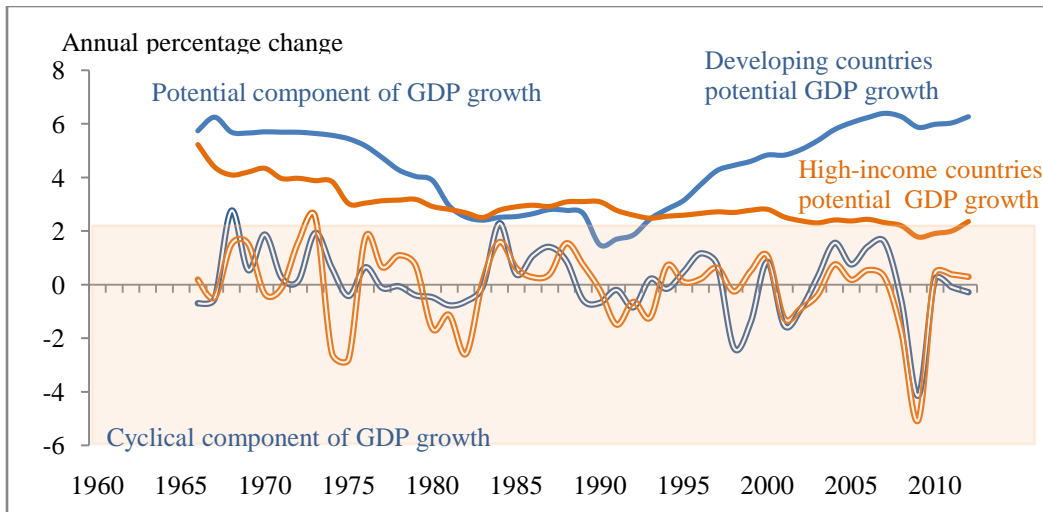
GDP Growth	Avg.					
	2005-2007	2008	2009	2010	2011	2012
Developing Countries	7.5	5.9	1.6	6.1	6.0	6.2
Middle Income Countries	7.5	5.9	1.5	6.1	5.9	6.2
- Of which: G20 Members	8.0	6.3	2.2	7.2	6.6	6.7
Low Income Countries	6.4	5.8	4.6	5.1	6.3	6.3
East Asia & Pacific	10.2	8.5	7.1	8.7	8.0	8.3
Europe & Central Asia	7.0	4.8	-5.3	4.2	4.3	4.3
Latin America & Caribbean	5.1	4.1	-2.4	4.3	3.9	4.2
Middle East & North Africa	5.1	5.8	3.0	3.4	4.2	4.8
South Asia	8.8	4.9	6.3	7.3	7.8	7.5
Sub-Saharan Africa	6.3	5.0	1.6	4.4	5.0	5.3
<i>Memo:</i>						
Developing Countries excl. China & India	5.9	4.6	-1.8	4.3	4.4	4.6

Source: World Bank staff projections linked to IMF G20 base case. As such, they may differ from the Bank's *Global Economic Prospects* projections.

Among developing regions, the recovery is projected to be most robust in Asia. The Europe and Central Asia region is expected to see more moderate growth, as several countries in the region were among the hardest hit by the crisis. Sub-Saharan Africa is expected to return to growth on the order of 5 percent in 2011, with prospects in several countries in the region tied closely to recovery in commodity markets.

Progress in developing country policies over the past decade or so produced an acceleration in their trend growth. There is evidence of some trend decoupling of growth between developing and high-income countries, as the former for a number of years now have achieved appreciably higher average growth than the latter. But this does not necessarily mean cyclical decoupling (Figure 2). As the recent crisis confirmed, the impacts on developing countries of significant cyclical developments in high-income countries remain strong. But the crisis also showed that countries with better policies and economic fundamentals are better positioned than others to withstand shocks.

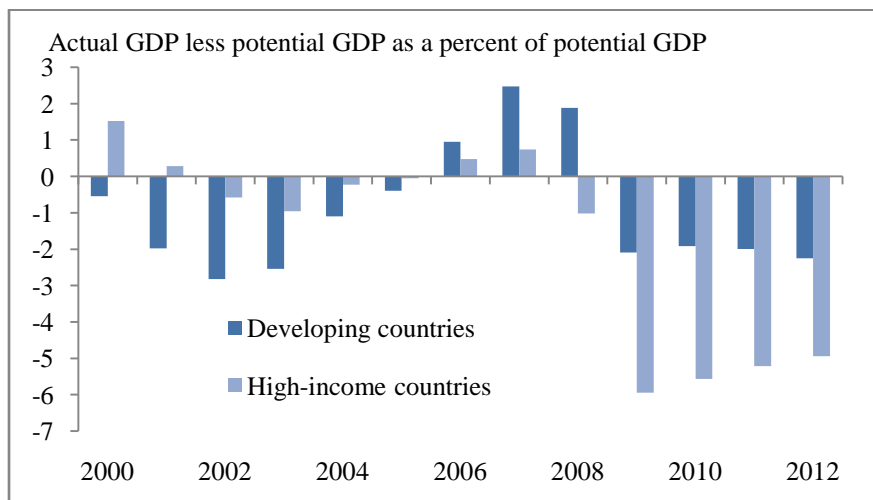
Figure 2: Trend, but not cyclical, decoupling



Source: World Bank staff calculations.

Even as the recovery gathers strength, growth is expected to be insufficient to close output gaps for several years (Figure 3). As a result, progress in raising average incomes in developing countries will remain below the pre-crisis expected levels and poverty will be higher than had been expected pre-crisis. In this sense, there has been a long-lasting impact on the pace of development progress. Only policies to accelerate growth beyond pre-crisis potential growth levels can reverse the negative impact of the crisis.

Figure 3: Output gaps will decline only gradually



Source: World Bank staff calculations.

Poverty and MDGs. There will be an estimated 64 million more people living in developing countries on less than \$1.25/day (76 million more on less than \$2/day) in 2010 than would have been the case without the crisis. Even by 2015, the number of additional poor attributable to the impact of the crisis would be 53 million and 69 million based on these two poverty lines, respectively (Table 2).

Labor market developments have been a driving force behind the increase in poverty. The ILO estimates that, over the 2007-2009 period, unemployment increased globally by 34 million people, of which 21 million were in developing countries (those covered in ILO surveys). In addition, there have been sharp increases in youth unemployment, a troubling development for future employment prospects.

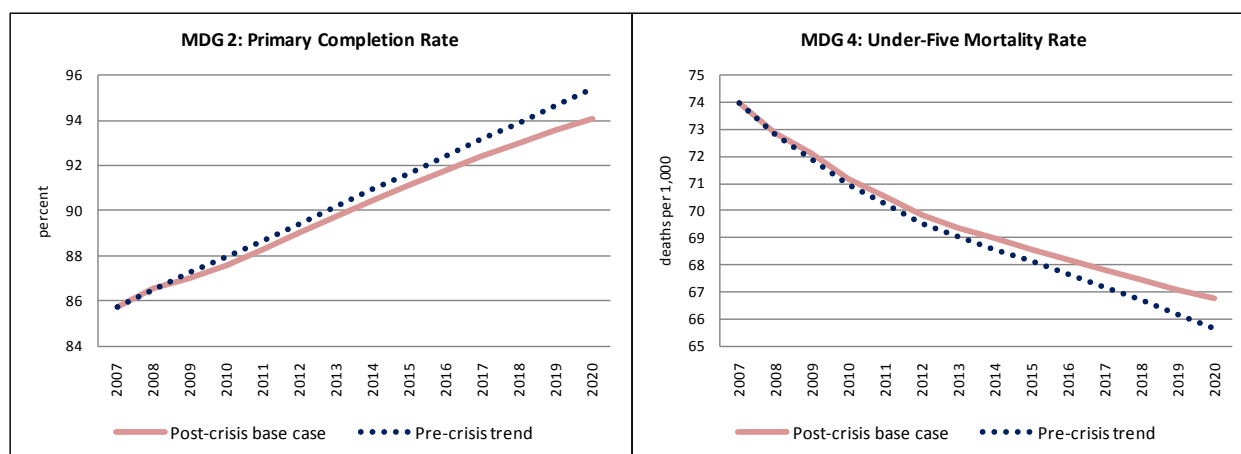
Table 2: Outlook for poverty in developing countries

	1990	2005	2015	2020
Percentage of population living on less than \$1.25 a day				
Post-crisis base case	41.7	25.2	15.0	12.8
Pre-crisis trend	41.7	25.2	14.1	11.7
Number of people living on less than \$1.25 a day (millions)				
Post-crisis base case	1,817	1,371	918	826
Pre-crisis trend	1,817	1,371	865	755

Source: World Bank staff calculations based on PovcalNet.

Growth collapses are particularly damaging for human development outcomes. There is an asymmetric response to the economic cycle, with more severe deterioration during downturns than the improvement during upturns. In addition, the impacts reach full severity with a lag. As a result of the crisis, it is estimated that 1.2 million more children under five may die between 2009 and 2015, and 350,000 more students may not complete primary school in 2015 (Figure 4). With respect to another MDG, it is estimated that about 100 million more people may remain without access to safe water in 2015 as a result of the crisis impact. In brief, the outlook for achieving many of the MDGs was worrisome before the crisis, and the crisis has imposed a further setback.

Figure 4: Impact of slower growth on selected MDGs

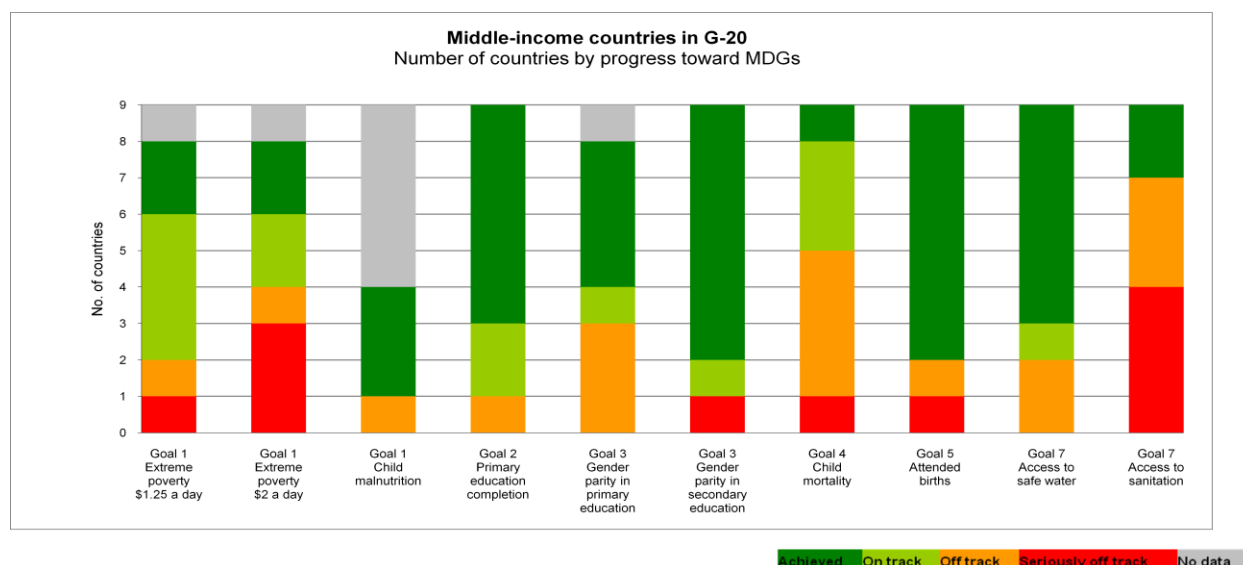


Source: World Bank staff calculations.

The impact of the crisis on poverty and human development outcomes is not confined to low-income countries. A large part of the rise in poverty occurred in middle-income countries, which still account for about two-thirds of the world's poor people. Many of the middle-income countries are still a considerable way from achieving some of the MDGs.

Nine G20 members are middle-income developing countries that continue to face major development challenges, for example, large infrastructure and human development needs, and in some cases large concentrations of poverty. They are home to 54 percent of the world's extreme poor (58 percent based on \$2/day poverty line). These nine countries account for more than half of the estimated increase in global poverty resulting from the crisis. Several of these countries, based on trends to date, are not on track to achieve some of the MDGs (Figure 5).

Figure 5: Progress towards MDGs of developing country G20 members



*Poverty headcount rate at \$2 a day is also included in view of greater relevance for middle income countries.

Source: World Bank staff calculations based on most recent data available in World Development Indicators.

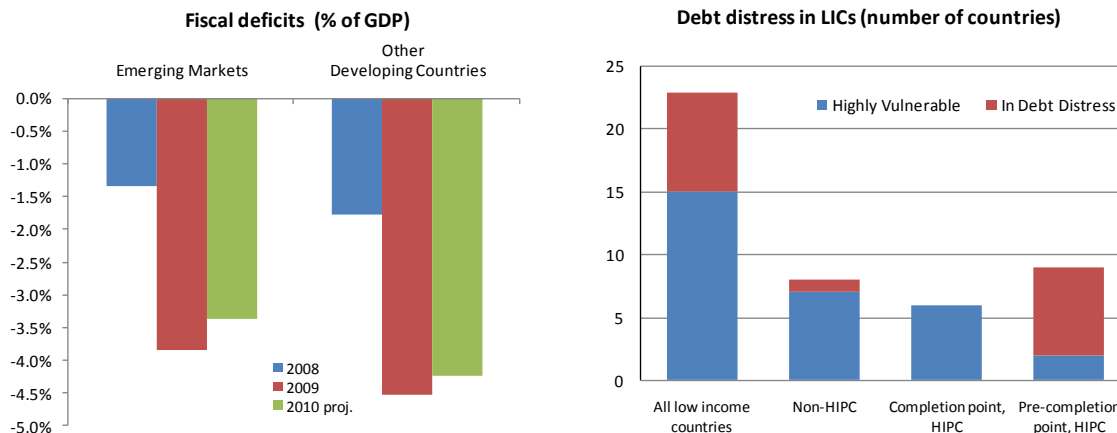
Risks to the base case outlook. The base case growth outlook for developing countries summarized above is subject to risks and uncertainties. Domestically, many countries face increased fiscal strains. Externally, the risks pertain to the prospects for the global economy and financial markets, which face increased uncertainties in view of recent developments in Southern Europe.

Fiscal deficits in developing countries rose by an average of 3 percent of GDP in 2009, and are projected to rise further in 2010 in more than one-third of the countries (Figure 6). While some countries, especially emerging markets, have put stimulus measures in place, in most countries the widening deficit resulted mainly from declining revenues. Although some emerging markets rapidly regained access to international capital, in developing countries with more limited external financing about half of the deficit increases on average were financed domestically, mainly through bank borrowing. This has raised fiscal sustainability concerns in many countries. The risk of debt distress has risen in low-income countries. In the absence of higher concessional flows, many low-income countries will be forced to cut spending.

During the crisis, countries were able to cushion the initial crisis impact on core spending—health and education, social safety nets, infrastructure—even though spending growth slowed. Restoring growth in core spending to pre-crisis levels will be a challenge, especially in infrastructure and in those countries with limited access to capital markets (Figure 7). Core social and infrastructure spending is critical for

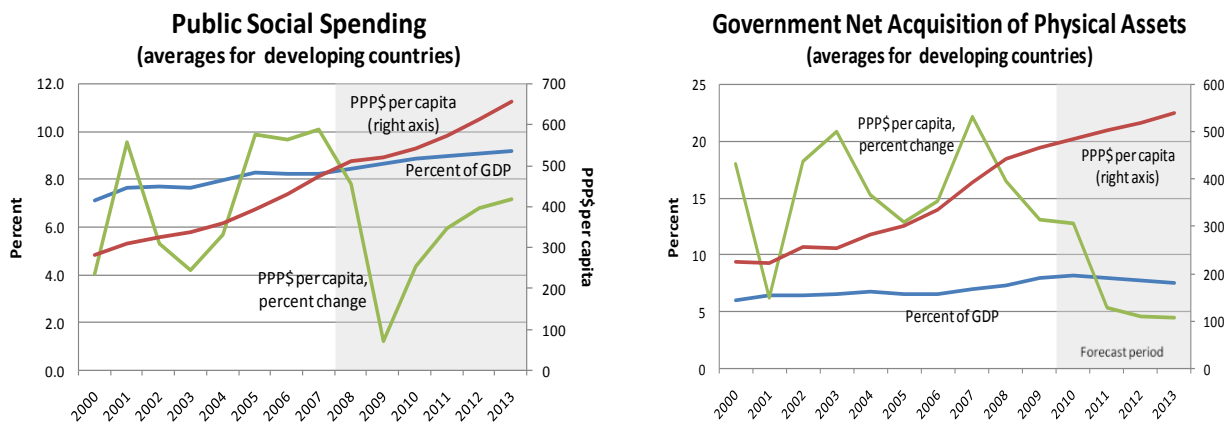
poverty reduction and growth but is likely to face particularly severe constraints in low-income countries. The need for spending on social safety nets will remain elevated in view of the higher unemployment and poverty resulting from the crisis (Box 1).

Figure 6: Fiscal strains have increased in developing countries



Source: IMF and World Bank staff estimates.

Figure 7: Core spending at risk



Source: World Bank staff estimates. “Net acquisition of physical assets” can be interpreted as a measure of government investment spending, of which infrastructure is the largest component.

The debt situation in some European countries poses risks to the base case scenario for developing countries. A crisis of confidence, default or major debt restructuring could have serious consequences for the global economy, because of the recession that the directly affected countries are likely to enter into and the potential knock-on impacts on the financial health of creditor banks elsewhere in the world. The immediate effects of a deepening and spreading of the problems facing Greece are likely to be contained to other highly-indebted high-income countries in Europe. However, the secondary effects of the crisis would have much wider consequences, including impacting developing countries.

Box 1: Social safety nets: a growth perspective

The role of safety nets in preventing people from falling into poverty in the midst of shocks is well known. By reducing inequality, social transfers can mean that a given growth rate has a larger impact in reducing poverty. But the role of safety nets does not stop there.

Productive role of safety nets. There are at least four ways in which safety nets directly contribute to growth.

- First, they are known to stimulate investment activities of the beneficiaries. Examples span a wide array of countries at different income levels: social grants in South Africa, Mexico's *Oportunidades*, Bangladesh's program for the Ultra poor (BRAC), pensions in Lesotho, Zambia's Kalomo Scheme for destitute households, food-for-work program in northern Kenya, cash-for-work program in Ethiopia, Bolivia's *Bonosol (Bono Solidario)* pension program, and Brazil's "social" pension. There is growing evidence that this effect is enhanced by providing money through savings accounts rather than cash handouts, and combining social transfers with microcredit interventions.
- Second, safety nets help the poor to protect and build their main productive asset, labor skills, by reducing the incidence of negative coping strategies, such as school drop-outs. The human capital of the poor is particularly the focus of programs aimed at breaking the intergenerational persistence of poverty, such as *Bolsa Familia* in Brazil, Mexico's Conditional Cash Transfers (CCT) (*Progres/Oportunidades*), Indonesia's scholarship program and waivers for health care, Nicaragua's CCT program, and Bangladesh's food for education program.
- Third, safety nets have also been found to transform the conditions of clientelistic relationships of the poor with lenders. Examples include cash for work transfers in Ethiopia, cash transfers to landless laborers in India, and Zambia's Kalomo program.
- Fourth, cross-country comparisons of growth rates find significant and positive growth effects of 'active' social transfers, those that encourage participation in the labor market by recipients. Mexico's *Progres/Oportunidades* evaluations have demonstrated local growth-enhancing effects.

Safety nets create legitimacy for responsible economic policies. The Growth Commission assembled the lessons of experience of a dozen fast growing countries. Countries included in the report—from Botswana to Ireland—show very different degrees of inequality, but they all share the commitment to the equality of opportunity. The combination of social policies and efficiency enhancing policies for growth can create political support for policy continuity.

Program design is crucial for maximizing the growth impact of social transfers. If transfers are to improve access to credit, they need to be regular and reliable. They must also be of sufficient duration to influence household consumption-investment decisions. Complementary asset accumulation interventions can enhance the growth effect. Transfers should be channeled in such a way as to facilitate improved resource allocation within the household.

Bank staff conducted simulations of the possible impact of a crisis of confidence stemming from Greece that spreads to four other high-income countries in Europe that have been the subject of market concern. The simulations take into account both trade and financial transmission channels. A first simulation examines the potential impacts on GDP of a significant rise in risk premia of heavily indebted countries caused by increased concerns about sovereign default. In this scenario, the yield on 10-year U.S. bonds is assumed to rise by 100 basis points and that of other sovereigns depending upon the degree of their indebtedness. A second simulation combines this with a scenario where credit to these 5 EU countries dries up either following a default or major debt restructuring or due to market expectations of such an outcome. A sharp fiscal adjustment is then forced. GDP in these countries could decline by as much as 15 percent, which would have serious repercussions on exports and activity levels in the rest of the EU and elsewhere in the world. In this simulation, world GDP could be 3.1 and 4.1 percent lower in 2011 and 2012, respectively. For developing countries, the impact is estimated at 2 and 2.9 percent lower GDP in 2011 and 2012, respectively. Because of the stronger financial ties to banks in these EU countries, capital

flows to Europe and Central Asia and Latin America could be particularly affected. These impacts could be much larger if the crisis causes insolvency of some major EU banks.

Implications of Alternative Scenarios for Developing Countries

Bank staff have used the alternative scenarios prepared by IMF staff to assess the potential impact on developing countries. The supportive policies envisioned by the IMF's upside scenario are consistent with the policy discussion above. These policies involve a more rapid fiscal adjustment in high income G20 countries, product and labor market structural reforms, and enhanced social safety nets and improved infrastructure in the developing country members of the G20. The upside scenario produces a cumulative gain in global GDP by 2014 of 2.8 percent relative to the base case.

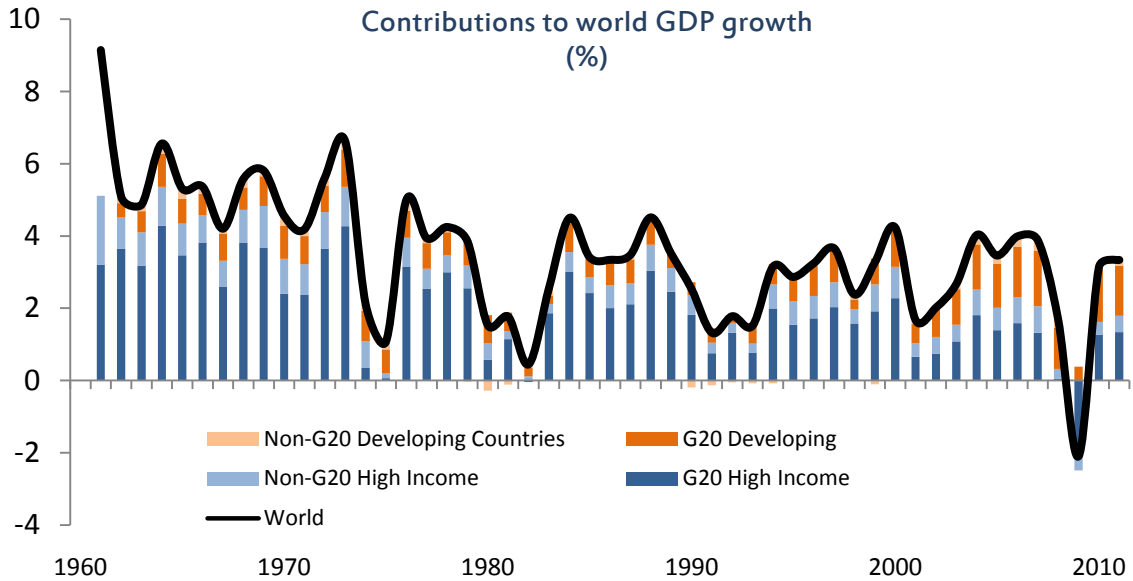
Applying the IMF's upside scenario to the Bank staff model for developing countries, the results show an increase in GDP of 2.4 percent for developing countries as a whole, with middle-income countries benefiting to the tune of about 2.3 percent and low-income countries about 3.1 percent. This could be associated with a decline in global poverty by 2014 of 14 million people at the \$1.25/day level and 33 million at the \$2/day level compared to the base case. These simulations take into account mainly the impacts on developing countries through trade flows. Additional benefits could be expected, especially for middle-income countries, from the lower interest rates that would accompany such a scenario. Some Bank simulations presented later in this report, in the section on financing for development, illustrate the potential benefits for developing countries from stronger fiscal consolidation in advanced economies that leads to a lower cost of capital.

The IMF's "downside scenario" is focused on fiscal sustainability risks and the credibility of fiscal adjustment. Inability to adjust the fiscal accounts would lead to market skepticism over reform and additional difficulties in enacting growth enhancing reforms in a stressed political environment. Global GDP would be 3.7 percent lower by 2014 than in the base case. Applying this scenario to the Bank staff models for developing countries results in a GDP decline relative to the base case of 3.6 percent for developing countries as a whole, with middle-income countries experiencing a decline of 3.5 percent and low-income countries 4.7 percent. The corresponding increase in global poverty is estimated at 23 million people at the \$1.25/day level and 58 million at the \$2/day level compared to the base case. Again, the transmission mechanism in these simulations is mainly through the trade channel. The higher interest rates that would be associated with such a scenario would exacerbate the impact on developing countries, especially middle-income countries.

Theme II: Multipolarity – A Dynamic Force in Global Growth and Rebalancing

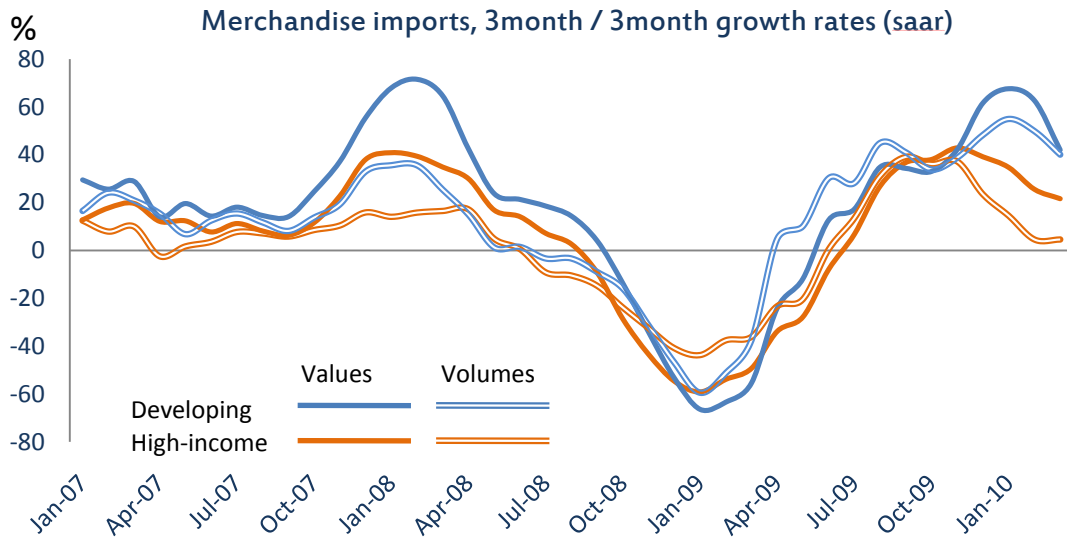
The second theme that emerges from the analysis is that reverse linkages—that is, how developing country outcomes in turn affect the global economy—also are becoming more important. As noted above, developing countries have been growing at a much faster average rate than high-income countries, and their weight in the global economy is rising. Whereas their GDP represented about 18 percent of global GDP in 1980, as of 2009 their share had increased to 28 percent of world GDP when measured at market exchange rates (close to 45 percent if purchasing power parity weights are used). Their weight in global trade has grown even quicker, rising from 20 percent in 1995 to an estimated nearly 30 percent in 2010. Not only has their share in activity increased, their faster growth rates mean that their overall contribution to global growth is larger still. Developing countries contributed around 40 percent of global growth in the past decade. In 2010, their projected contribution will approach 50 percent (Figure 8). Since the year 2000, developing countries have accounted for more than 40 percent of the increase in world import demand. They are leading the recovery in global trade, with their import demand rising at twice the rate of that in high-income countries (Figure 9).

Figure 8: Almost half of global growth now comes from developing countries



Source: World Bank staff calculations.

Figure 9: Developing countries are leading recovery in trade



Source: World Bank staff calculations.

Linkages among developing countries, or South-South linkages, also are becoming more important. South-South trade has risen to a third of world merchandise trade. Within regions, trade among developing economies has increased substantially, further strengthening regional growth poles. For example, the share of imports originating from other developing countries within their own regions (in 2008) was 29 percent, 20 percent, and 15 percent in Europe and Central Asia, Latin America and the Caribbean, and East Asia and the Pacific, respectively. South-South foreign direct investment has

accounted for a third or more of total such investment going to developing countries in recent years. South-South migration is larger than South-North migration.

Developing countries possess a large potential for future growth. They offer abundant opportunities for high return/high growth potential investments (such as in critical infrastructure and human capital that remove bottlenecks to growth) and they have undertaken important reforms in recent years to improve the development effectiveness of their programs and investments. Many, however, face a financing constraint in fully exploiting these growth opportunities. Promotion of growth in these countries through more support for investment that removes bottlenecks to their growth would be a global win-win. It would support their development and it would contribute to stronger growth at the global level and to the post-crisis rebalancing of global growth by creating new markets and investment opportunities and hence more sources of growth in global demand.

Rebalancing needs to look beyond a narrow focus on external balances and macroeconomic policy adjustments to include structural rebalancing, and supporting multiple growth poles is a key element of structural rebalancing. Promotion of growth in developing countries should be seen as an integral element of the G20 framework for “strong, sustainable, and balanced growth.”

The potential to contribute to global growth and rebalancing is not limited to the rapidly growing emerging market growth poles. Better policies have improved growth performance and opportunities in many low-income countries, including in Sub-Saharan Africa (average regional growth of about 6 percent in the five years preceding the crisis). They offer markets for investment, not just destinations for aid. Net foreign direct investment to the region more than doubled from \$14 billion in 2001 to \$34 billion in 2008. There is much potential for further growth in these investment flows.

Box 2: Infrastructure investment needs in Africa

Africa’s infrastructure investment needs relative to GDP are particularly large, at 15 percent. But more financing is not the only answer. Improvements in “soft infrastructure” (such as improvements in governance, regulation, and cost recovery) can yield significant efficiency gains. Even with such efficiency gains, however, the region’s annual funding gap would remain sizable at about 5 percent of GDP, or about \$30 billion.

	Infrastructure Investment and Maintenance (% of GDP)			
	Needs	Spending	Efficiency gap	Funding gap
Middle income	10	6	2	2
Resource rich	12	5	3	4
Low income	22	10	3	9
Fragile states	36	6	5	25
All of Africa	15	7	3	5
<i>In dollars (billions)</i>	93	43	19	31

Source: Africa Infrastructure Country Diagnostic, 2009

Infrastructure is a key area for investment, due to its high potential for spurring growth—in agriculture, manufacturing, services. For example, research shows that raising infrastructure services in Africa to Korea’s level could raise the region’s growth rate by up to 2.6 percentage points. Infrastructure investment and maintenance needs in developing countries amount to over \$900 billion (6-8 percent of

GDP) annually. Actual spending reaches only about half that level (Box 2). Alleviating the financing constraint can boost local growth and support global demand. It could be a high return investment in a win-win global growth outcome. Research also shows high returns on sound investments in human capital—education, health and nutrition.

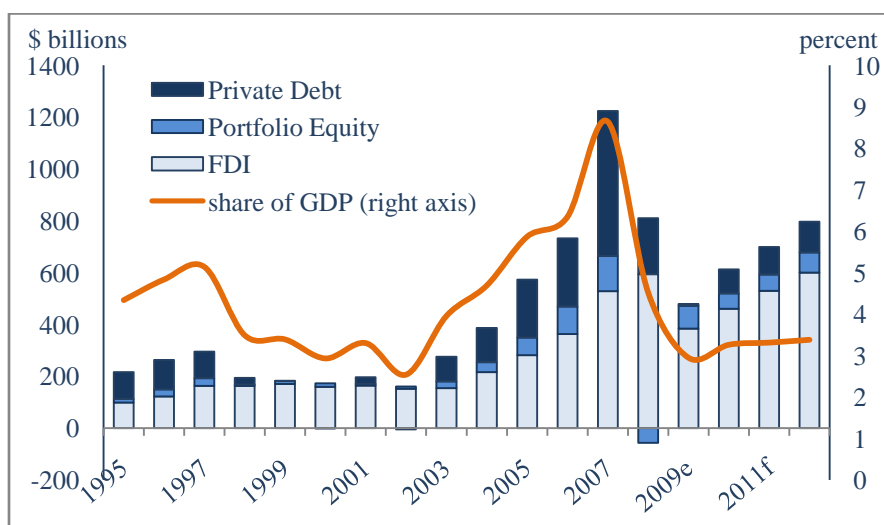
In addition to financing, the G20 can be instrumental in promoting the sharing of development knowledge and support for capacity building in developing countries. The accumulated richness of national development experiences offers considerable opportunities for sharing development knowledge and expertise—not just North-South but increasingly also South-South and South-North.

Theme III: Financing for Development – Challenging Outlook Demands Creativity

Outlook for financing for development. A third theme that emerges from the analysis is that the outlook for financing will be more challenging and will demand creativity. Although the global financial markets are recovering, the recent crisis will have longer lasting implications for financial flows to developing countries. While some major emerging market countries are now seeing a strong rebound in capital inflows, especially non-debt flows, most developing countries face the prospect of scarcer and more expensive capital. The rise in fiscal deficits and debt in advanced economies and related concerns about crowding-out, tighter financial sector regulation and banking system consolidation, and a re-pricing of risk are all likely to limit developing countries’ access to financing and raise the cost of capital.

Net private capital flows to developing countries fell precipitously in 2008-09 as a result of the financial crisis, falling from a peak of about \$1.2 trillion (8.7 percent of developing countries’ GDP) in 2007 to \$480 billion (3 percent of GDP) in 2009. They are likely to recover only slowly, reaching a projected level of about \$770 billion (3.3 percent of GDP) by 2011 (Figure 10).

Figure 10: Net private capital flows to developing countries: only a modest recovery

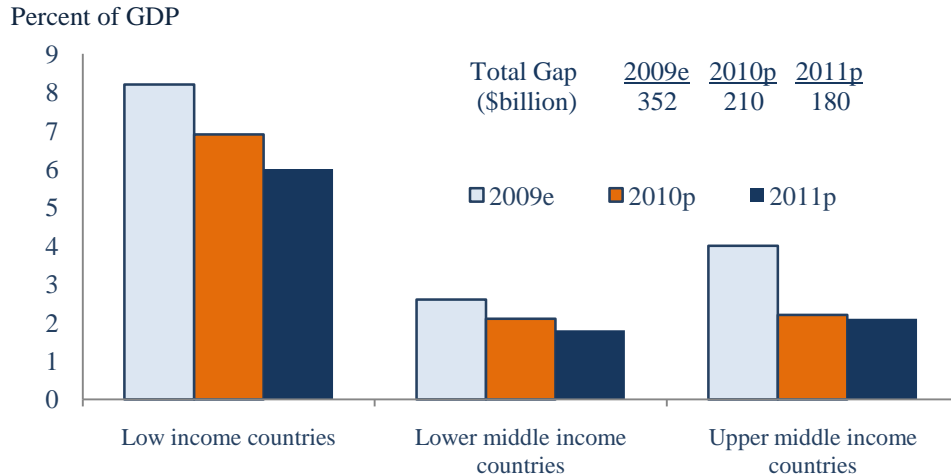


Source: World Bank Staff estimates.

While developing countries’ access to capital markets is projected to decline in the post-crisis period, their financing needs are likely to be larger. Developing countries’ external financing needs rose sharply during the crisis and are expected to decline only gradually. Even by 2011, the projected ex ante external financing gap (current account deficit plus amortization minus expected private capital inflows) will be

high at about \$180 billion (Figure 11). Relative to GDP, the projected financing gap is particularly large in low-income countries.

Figure 11: Developing country financing gaps will remain large

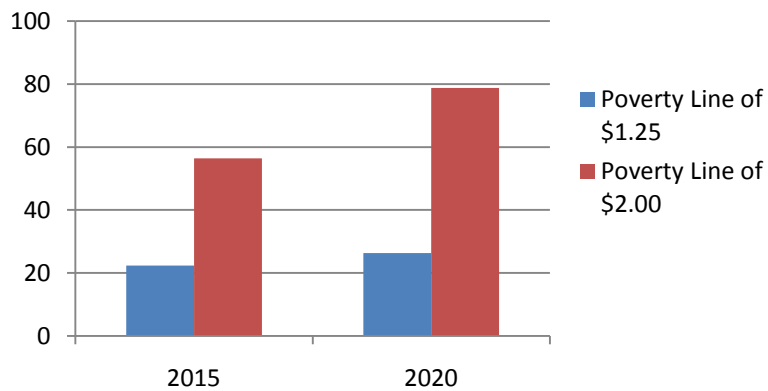


Source: World Bank staff estimates.

Bank staff estimate that the tighter conditions in international financial markets reflected in scarcer and costlier capital could depress investment and lower economic growth in developing countries by up to 0.7 percentage points annually over the next 5 to 7 years compared with the pre-crisis trend. Potential output in developing countries could be reduced by up to 8 percent in the long run relative to its pre-crisis path. This baseline outlook is subject to further downside risks, in view of the situation in Greece and increased concerns about sovereign debt in advanced economies.

The stakes are high. Even relatively small declines in growth can have cumulatively large impacts on poverty. Our simulations suggest that a 0.5 percentage point decline in developing country growth rate, say due to higher capital costs and lower investment, can mean nearly 80 million additional people living on less than \$2/day in ten years (Figure 12).

Figure 12: Impact on developing country poverty headcount of a 0.5 percentage point decline in GDP growth rate (in millions)



Source: World Bank GIDD Model simulations

Fiscal consolidation, financing for development, growth and rebalancing. With high and rising public debt, fiscal consolidation is a key priority for the advanced economies. It would also benefit developing countries. Debt-GDP ratios in advanced economies are expected by the IMF to exceed 100 percent of GDP in the next 2-3 years, some 35 percentage points higher than before the crisis. Sovereign debt issuance by the G-3 alone exceeded \$2.5 trillion in 2009, more than 7 times total net capital flows to developing countries. Simulations show that a stronger, quicker fiscal consolidation in advanced economies would produce a win-win outcome. Two scenarios were constructed to explore the impact of fiscal consolidation in advanced economies. In the first, the improvement in primary balances is calibrated such that if applied gradually between 2011 and 2020 and then held there through 2030, the debt to GDP ratio would fall to 60 percent by 2030. In the second scenario, the same improvement in primary balances is achieved in the first four years and then held at that level through 2030. The results were then compared with a scenario that assumes no proactive fiscal consolidation. The results show gains in growth for developing countries in both fiscal consolidation scenarios but larger gains in the scenario with quicker adjustment; in the latter scenario, the gain in GDP in the medium- to long-term reaches about 6 percent. The loss for developing countries through weaker demand for their exports is more than offset by benefits from lower real interest rates and higher investment. Long-run growth outcomes also improve in the advanced economies, though the fiscal adjustment implies a loss of output in the short run. The simulations suggest that the fiscal consolidation would also go a long way in helping to reduce global trade imbalances.

Rebalancing of global growth and financing for development can be linked in a virtuous circle. Three quarters of developing countries are net importers of capital. However, as an aggregate, developing countries, including emerging markets, have in recent years run a surplus, mainly reflecting large surpluses of saving over investment in a few countries—notably China and developing oil and mineral exporters. So, considered as a whole, developing countries have recently been net exporters of capital to high income countries—a phenomenon sometimes referred to as capital flowing uphill. Capital inflows from the BRIC countries financed about 75 percent of the US current account deficit in 2008, up from 13 percent in 2001. Success in rebalancing in advanced deficit economies, thereby reducing their borrowing requirements, would allow more of the surplus global savings to flow to support investment and growth in developing countries which in turn would generate more import demand (and from multiple sources) to reinforce rebalancing.

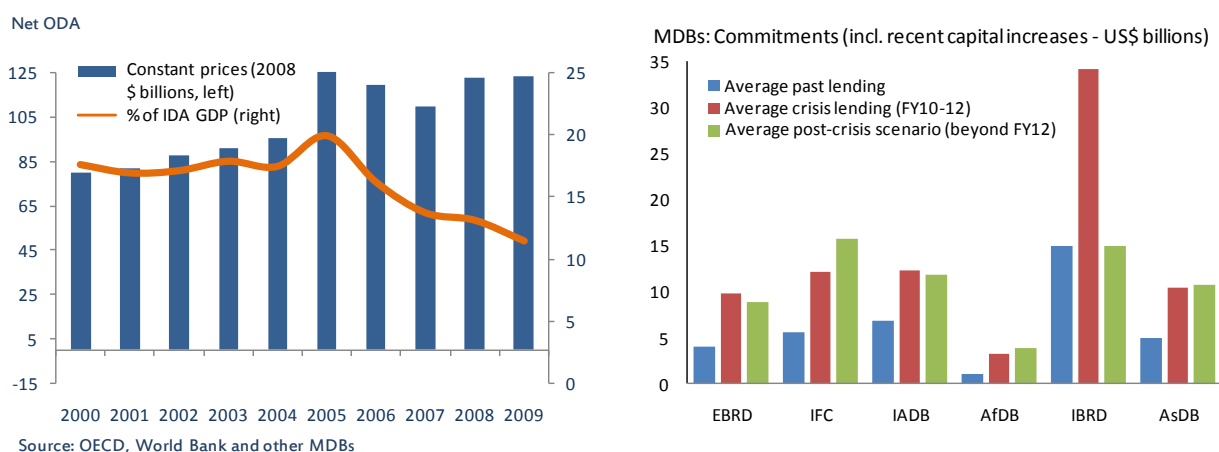
Implications of financial sector reforms in advanced economies. It is important to ensure that ongoing and planned financial sector reforms in advanced economies do not have unintended adverse effects on financial flows to developing countries or their financial sector management. There is a need for a mechanism to assess the implications of these reforms for countries that are not members of the Financial Stability Board and Basel Committee on Banking Supervision. A number of countries have embarked on national reform initiatives which, if not well coordinated, risk creating financial protectionism, regulatory arbitrage, and inconsistency across jurisdictions. Some of the proposed liquidity reforms that require compliance with liquidity requirements at the branch level as opposed to a consolidated group level might constrain global banks in funding operations in emerging markets and vice versa. Proposed reform of securitization and derivatives should not choke off financial innovation that has been beneficial for development, e.g., use of these innovations to hedge crop and weather risks. On trade finance, the Basel Committee could review the appropriateness of a 100 percent credit conversion factor in its proposed leverage ratio for off balance sheet trade finance items with a maturity of less than a year, taking into account the largely self-liquidating, low-risk and short-maturity characteristics of such trade finance products. Regulations designed for banks in advanced economies may not be appropriate for banks in low-income countries, especially smaller banks that cater to smaller enterprises, or may require a longer period to phase them in.

Official financing for development. With tighter capital markets, official flows take on added importance, both in directly providing development finance and in leveraging private capital. This includes ensuring adequate official development assistance (ODA) and supporting multilateral lending with enough capital. While ODA rose modestly in real terms in 2009, overall it is falling short of commitments and declining relative to the GDP of low-income countries for which it constitutes an especially important source of financing (Figure 13). It would be desirable to have a coordinated position among the G20 to maintain or increase aid levels as fiscal consolidation strategies are designed and implemented. At the same time, more can be done, by donors and partner countries working together, to further progress on the Accra Agenda for Action to improve aid effectiveness—better aid alignment and harmonization, improved aid predictability, and a stronger focus on results.

Multilateral development bank (MDB) financing rose appreciably in response to the crisis, complementing IMF financing in providing countercyclical support to developing countries. Between July 2008 and December 2009, MDBs committed \$158 billion (about \$50 billion above pre-crisis trend), of which \$88 billion came from the World Bank Group. Thanks to recent agreements on MDB capital increases, average post-crisis commitments could reach about \$65 billion a year, compared to the average pre-crisis level of about \$38 billion a year (Figure 13). In terms of net flows, however, MDB lending will remain small compared to developing country needs for long-term capital.

Much of the increase in MDB financing during the crisis was in non-concessional financing. Concessional financing rose more modestly. Adequate replenishment of the MDB concessional windows, especially IDA and the African Development Fund, would enable them to meet the increased needs of low-income countries responding to the financial crisis, as well as the aftermath of the food and fuel crises that preceded it. The need for concessional finance has risen as fiscal space in low-income countries has come under pressure while social spending needs, including expansion of social safety nets for poor and vulnerable groups, have increased as a result of higher poverty and unemployment. Innovations such as the IDA crisis-response facility have improved the responsiveness of concessional financing to crises.

Figure 13: Official development financing: ODA and multilateral lending



Supplementing traditional financing with innovative forms of finance. The conjuncture of tighter capital markets and fiscal stress in donor countries implies the need for supplementing traditional modes of financing with innovative forms of finance. Ensuring adequate financing for development in these circumstances will require innovations in leveraging private capital. With a rise in market perception of risks, there will be more demand for guarantees and insurance mechanisms (multilateral and bilateral) to

mitigate the risk faced by long-term private investors in developing countries. Such instruments can provide significant leverage. For example, the World Bank Group issued about \$7.7 billion in guarantees between 2000 and 2008 to support investments in financial and productive sectors of developing countries. These guarantees leveraged total investments of about \$20 billion, a leverage ratio of roughly 2.6. Public-private partnerships offer much potential and a variety of possibilities. A potentially important source of development financing is the multitrillion-strong sovereign wealth funds (SWFs). An innovative example that offers scale-up possibilities is the recent investment by several SWFs in an IFC equity fund. A complementary element is the strengthening of international financial safety nets to reduce the demand for reserves as a form of self-insurance against risks of economic volatility and capital flow reversals. This could free up more of developing countries' own resources for investment.

There are increasing possibilities for South-South financing and investment, from SWFs, corporations, and governments. Some countries, such as China, are trying to improve the standards governing these flows. For example, China has outsourced several environmental assessments to European firms to gain experience with global best practice in this area. It has also worked with the IFC to introduce Equator Principles into its operations. China and the World Bank are collaborating on investments in infrastructure, industrial zones, and health in Africa.

At about \$330 billion annually, officially recorded remittance flows to developing countries are almost three times as large as ODA. The 5x5 initiative that followed from the 2008 G8 summit in Hokkaido and that aims to reduce remittance fees by 5 percentage points in 5 years can increase remittance flows by an estimated \$15 billion annually. Diaspora bonds are another innovation that seeks to tap into the wealth of the stock of migrants from developing countries.

Financing of global public goods and programs. Innovation and partnerships will be particularly important in the financing of global public goods and development-linked global programs. Private aid, which on some estimates approached \$50 billion in 2007 (close to one-half of ODA in that year), has been playing an increasingly important role in partnership with public funding in programs to combat communicable diseases (e.g. Global Fund to Fight AIDS, Tuberculosis, and Malaria and Global Alliance for Vaccines and Immunizations). Other important innovations include the International Finance Facility for Immunization that frontloads financing needed for immunization programs in poor countries, the Advance Market Commitment mechanism that subsidizes private costs of vaccine production for developing countries, and voluntary solidarity contributions such as the UNITAID international solidarity levy on air travel. There are good examples of innovation and public-private partnerships in other areas as well, such as the Global Agriculture and Food Security Program. Carbon markets are emerging as a potentially important source of development finance, especially in helping to meet the large investment needs to increase developing countries' access to affordable and clean energy.

Estimated financing needs in some of these areas are large. For example, the High Level Task Force on Innovative Financing for Health Systems estimates that in addition to current domestic and external health financing, about \$36 billion annually would be required to achieve the health MDG and support national health systems to address communicable diseases in the 49 poorest countries. The International Food Policy Research Institute estimates the incremental public agricultural investment needed to reach the MDG on reducing hunger to be about \$14 billion a year. The World Development Report 2010 estimates that current climate-dedicated financial flows to developing countries cover less than 5 percent of what these countries will need to spend on climate change mitigation and adaptation in coming years. The scale of the resource needs, especially in the post-crisis environment for financing, calls for both a renewed commitment of support by the G20 to such key global programs and for renewed vigor and creativity in exploiting the potential of innovative approaches in development financing and partnerships that leverage private capital.

Domestic resource mobilization and financial sector development. The financing outlook also implies the need for stronger domestic resource mobilization by developing countries themselves, including continued progress on reforms to improve public resource management and the environment for private investment, domestic and foreign. Tighter and costlier access to external finance enhances the need to strengthen developing countries' own financial systems. Strong financial systems are important both for effective engagement with globalized finance and for better mobilization and allocation of domestic resources for development. Inefficiency of domestic financial sectors can make borrowing costs in developing countries as much as 1,000 basis points higher than in advanced economies. Simulations suggest that if developing countries can improve domestic financial intermediation to lower interest rate spreads by an average of 25 basis points a year, they can raise their long-run potential output by 7.5 percent, with the largest gains accruing to countries and regions currently facing the highest spreads.

Some aspects of financial sector development, such as improving access of the poor to financial services and strengthening SME finance, have already been the subject of attention in G20 under the theme of inclusive finance. This is important: almost 70 percent of the adult population in developing countries or 2.7 billion people lack access to basic financial services, and surveys show that SMEs are at least 30 percent more likely than large firms to rate financing constraints as a major obstacle to growth. But there is also the need to strengthen financial systems in developing countries more broadly. Expanded technical and capacity building assistance to financial sector reforms in developing countries can be a key area for G20 collective action in support of development—including, for example, expanding participation in and contributions to The Financial Sector Reform and Strengthening (FIRST) Initiative.

Theme IV: Open Trade – Engine of Growth and Facilitator of Rebalancing

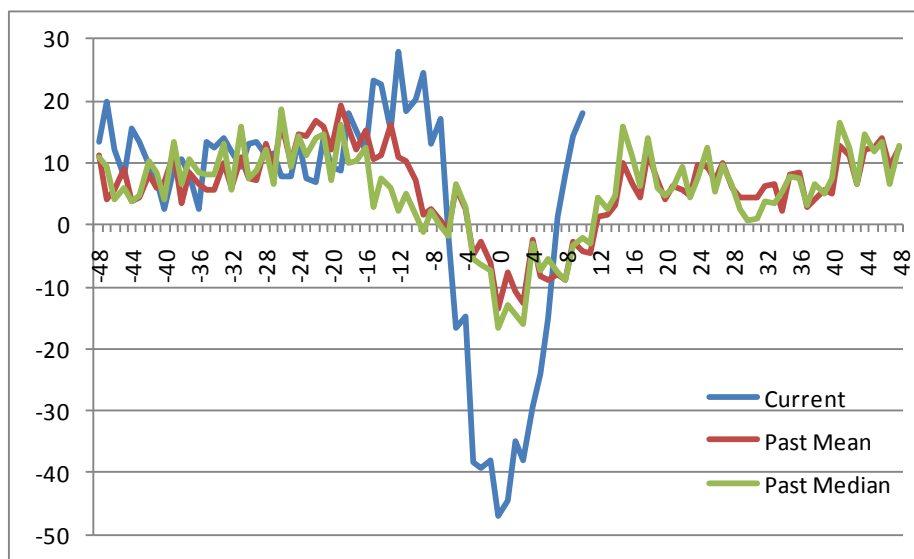
Finally, the fourth theme is that an open trade environment is essential for a sustained economic recovery and for enabling the growth rebalancing to work. Keeping trade open will be important for sustaining the recovery as the fiscal and monetary stimuli are withdrawn. Trade, supported by investment and associated technology flows, is a key channel for multipolar growth and diversification of global demand.

Trade flows: changing patterns, collapse and recovery. The recent crisis made it clear how the evolution of international trade patterns has created more economic interdependence. Parts and components are now one-third of all manufacturing trade, and this share rises to nearly one-half in East Asia. These more integrated supply chains imply that trade shocks in one country transmit more rapidly and strongly across countries. Trade fell fast after the onset of the financial crisis. The low point was in the first quarter of 2009, when the value of global trade was down about 30 percent from the same quarter in the previous year. To place the collapse in historical context, Figure 14 compares trade growth (month over same month in the previous year in constant US\$) in this crisis with previous downturns in 1975, 1982, 1991, and 2001. Data are matched so that year zero is the lowest point of the contraction. Growth leading up to the crisis was higher and the fall deeper in this episode than in previous downturns. The recovery also appears to be much steeper in this crisis than in previous episodes. The graph shows a V-shaped recovery is well underway, though the global trade value still remains below its pre-crisis level.

The trade collapse was primarily the result of a large demand shock, which affected trade to a greater extent than GDP. The bulk of traded goods are manufactures (80 percent of non-oil trade), where inventories can be cut and consumption can be postponed. Global supply chains and lean retailing contributed to spreading the shock rapidly across countries. While the drop in trade was synchronized across countries, the recovery has been less balanced. The recovery in Europe is particularly fragile, as worries over increasing debt in the Euro area have raised uncertainty about future growth. The rest of the world shows strong and steady growth. A number of Asian countries, including China, India, and

Indonesia, have demonstrated remarkable resilience, with imports now above pre-crisis levels. These large and growing emerging markets may be the future engine of trade growth.

Figure 14: Collapse and recovery of world trade: current versus past crises (percent)



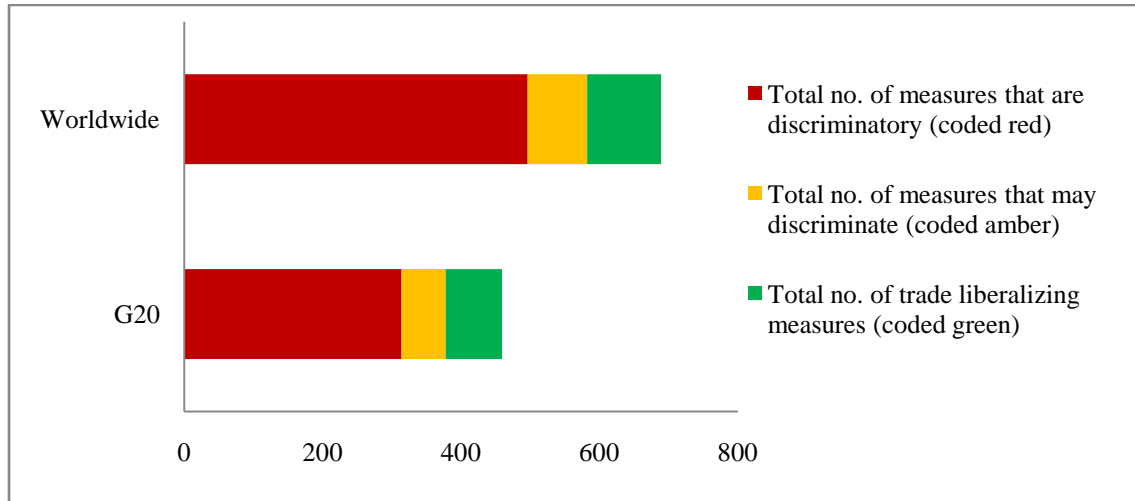
Source: World Bank staff calculations.

The financial crisis and resulting trade collapse have brought about a reversal in the large global trade imbalances that characterized trade patterns in recent years. In part this is purely mechanical. If both imports and exports decline by a given percentage then the difference must also shrink by the same percentage. The value of global trade declined by about 15 percent in 2009, suggesting there should be a similar drop in imbalances. In fact, the global trade imbalance—measured as the sum across countries of the absolute value of the trade balance—plunged 30 percent (this is calculated using data from 58 countries that report data through 2009 and that make up over 75 percent of world trade). This implies that in addition to the drop in trade, net rebalancing of exports and imports accounted for half of the improvement in trade imbalances. In other words, deficit countries tended to experience relatively larger declines in imports, and surplus countries larger declines in exports. This is important because as trade recovers, improvement in imbalances due to the trade drop alone is likely to disappear, while adjustment due to rebalancing is likely to be sustainable.

Trade policy response. Notwithstanding the difficult circumstances of the recession and rise in unemployment, the G20 have by and large adhered to the commitment made at the outset of the crisis to avoid protectionism. Although restrictive actions have been taken by practically all G20 countries, the trade coverage of these actions has been small. However, while open protectionism has been resisted relatively well, there is concern that opaque or murky protectionism has been on the rise.

Between November 2008 and May 2010, governments worldwide have implemented close to 700 trade measures, including about 500 discriminatory measures. G20 members have imposed close to two-thirds of the discriminatory measures (Figure 15). More recently, quarterly data show a declining trend in the imposition of discriminatory measures: in the first quarter of 2009 a total of 120 measures were taken; in the same quarter of 2010 the number had declined to 63 measures.

Figure 15: Trade measures implemented worldwide and by G20, November 2008-May 2010



Source: Global Trade Alert

Among the trade measures implemented, there has been a sharp rise in the incidence of antidumping actions, use of safeguards, preferential treatment of domestic firms in bailouts, and discriminatory procurement. The major G20 users of antidumping, countervailing duties, and safeguards combined to have 25 percent more import product lines subject to these trade barriers than they did in 2007 (Figure 16). Such actions are not just North-South. About half of such barriers in 2009 were South-South in nature. Another risk to watch out for is that as fiscal retrenchment occurs, there might be a temptation to replace subsidies and preferential treatments granted in bailout programs with new trade barriers.

Figure 16: Combined G20 use of antidumping, countervailing duties, and safeguards



Source: Compiled from the World Bank's *Temporary Trade Barriers Database*.

Priorities in trade agenda. G20 leaders recognized early on the potential systemic risks stemming from protectionist policy responses. They can boost market confidence by renewing their commitment to refrain from protectionist measures. An even stronger signal would be a collective pledge to unwind the protectionist measures that have been put in place since the onset of the crisis in August 2008.

Trade rules matter. Areas that are not subject to multilateral discipline or where the coverage is unclear or limited are the ones that have seen more restrictive actions. Strengthening multilateral trade disciplines and moving ahead with the Doha Round therefore are important. Conservative estimates put the global real income gains from a successful Doha agreement at \$160 billion.

Harmonizing the programs of trade preferences granted by developed and emerging countries to the Least Developed Countries (LDCs) would help increase their overall usefulness. Currently, trade preference programs provide high levels of product coverage but with important exceptions, mostly related to agricultural products and apparel. The G20 could consider extending 100 percent duty-free and quota-free access to LDCs, with liberal rules of origin.

For less developed countries, building trade capacity can be at least as important as improved market access in boosting trade. So a complementary priority is the strengthening of support for trade facilitation to address behind-the-border constraints to trade—improvement of trade-related infrastructure, regulations, and logistics such as customs services and standards compliance. Research shows that raising logistics performance in low-income countries to the middle-income average can boost trade by 15 percent or more. In support of trade facilitation, aid for trade should be scaled up substantially. Aid for trade public-private partnerships can make the resources go further by leveraging the dynamism of the private sector in strengthening trade capacity.