



Global Prospects and Policies: Policy Pivot, Rising Threats

WORLD ECONOMIC OUTLOOK OCTOBER 2024

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October 24, 2024 Singapore

Overview

Global Economy: Stable but Low Growth & Continuing Disinflation Elevated Uncertainty

Global real GDP growth (percent; y/y)



Source: IMF staff calculations.

Note: Each shade of blue represents a 5-percentage point probability interval. WEO = World Economic Outlook.

Global inflation

(percent; y/y)



Recent Developments

- Steady disinflation but sticky services
- Tight monetary, loose fiscal policies
- Rising debt burden

Outlook

Risks & Policies

Risks: tilted to the downside

- Larger-than-expected monetary policy impact
- Financial markets repricing
- Sovereign debt distress
- China's property downturn
- Renewed commodity price spikes
- Rising protectionist policies
- Social unrest

Policies:

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- Restoring price stability
- Rebuilding buffers
- Fostering medium-term growth
- Combating climate change

Recent developments

Inflation Declining and Converging across Countries ...

Headline Inflation Distribution

(Percent, year over year)



Sacrifice Ratio for Inflation

(Change in output gap for a change in inflation)



Sources: OECD and IMF staff calculations.

Note: The sample for the headline inflation distribution includes 32 advanced economies and 13 emerging market and developing economies. The sample for estimating the sacrifice ratio includes 37 advanced economies.

... But Services Inflation Still High So Bumps in the Road Still Possible

Core Services and Goods Inflation

(Percent, three month over three month, annualized)



Rising Shipping Costs

(USD per 40 ft. container; index, 2010 = 100, right scale)



Labor Market Pressure Easing amid Higher Wage Growth



Wage Growth

(Percent, year over year)

Contributions to Inflation

(Percent, annualized)



Sources: Eurostat; Haver Analytics; US Bureau of Economic Analysis; and IMF staff calculations.

Policy Mix: Tight Monetary, ...



Sources: Bank for International Settlements; Consensus Economics; European Central Bank; Federal Reserve Board; Haver Analytics; and IMF staff calculations.

... Combined with Loose Fiscal

Fiscal slippage

(Percentage points; 2024 minus 2022 primary balance)



General Government Interest Payments

(Percent of general government revenues)



Global Trade Stable, Fragmentation Starting to Emerge

Globalization and Trade Fragmentation



Sources: Gopinath, Gourinchas, Presbitero, and Topalova (2024); and IMF staff calculations.

Note: The right figure plots the change in global trade between blocs (panel 1) and with nonaligned countries (panel 2) during the Cold War (blue line, with t0 = 1947) and since Russia's invasion of Ukraine (red line, with t0 = 2021:Q4).

Trade Fragmentation: Cold War and Now

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The outlook

Assumptions for the Baseline Forecast



Source: IMF staff calculations.

Note: In the left and middle panels, solid lines denote projections from the October 2024 *World Economic Outlook* and dashed lines from the April 2024 *World Economic Outlook*. Also, the dotted line in panel 1 denotes projections from October 2023 *World Economic Outlook*.

Global Outlook: Stable Growth and Closing Output Gaps

Growth Outlook

(Percent; dashes = April 2024; dots = October 2023)



Cyclical Forces Waning and Output Gaps Closing (Percent)

Growth Projections: Advanced Economies

(percent change from a year earlier)

				*** * * * *			*	
	World	Advanced Economies	U.S.	Euro Area	Japan	U.K.	Canada	Other Advanced Asia
2023	3.3	1.7	2.9	0.4	1.7	0.3	1.2	1.6
Revision from Jul. 2024	0.0	0.1	0.4	-0.1	-0.2	0.2	0.0	0.0
2024	3.2	1.8	2.8	0.8	0.3	1.1	1.3	2.5
Revision from Jul. 2024	0.0	0.1	0.2	-0.1	-0.4	0.4	0.0	0.2
2025	3.2	1.8	2.2	1.2	1.1	1.5	2.4	2.3
Revision from Jul. 2024	-0.1	0.0	0.3	-0.3	0.1	0.0	0.0	0.0

Source: IMF, October 2024 World Economic Outlook.

Growth Projections: Emerging Markets and LIDCs

(percent change from a year earlier)

			*)				\bigcirc	
	World	Emerging Market and Developing Economies	China	India	Brazil	Russia	Commodity Exporting Economies	Low Income Developing Countries
2023	3.3	4.4	5.2	8.2	2.9	3.6	2.9	4.1
Revision from Jul. 2024	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.1
2024	3.2	4.2	4.8	7.0	3.0	3.6	3.1	4.0
Revision from Jul. 2024	0.0	0.0	-0.2	0.0	0.9	0.4	0.3	-0.2
2025	3.2	4.2	4.5	6.5	2.2	1.3	3.3	4.7
Revision from Jul. 2024	-0.1	-0.1	0.0	0.0	-0.2	-0.2	0.0	-0.4

Source: IMF, October 2024 World Economic Outlook.

Medium-Term Outlook

Persistent headwinds to growth over the medium-term

Medium-Term Growth Outlook (Percent)



Inflation: Gradual Decline to Target

Faster Disinflation Expected in AEs

Inflation in AEs and EMDEs (Percent)



Steady Convergence to Target

Inflation Outlook

(Percentage points; deviation from inflation target)



Trade Growth in Line with Output Growth, Narrowing Balances

Global current account balances are expected to continue to decline from 2022 peaks.

Global Current Account Balance (Percent of global GDP)



Risks

Downside Risks to Growth Dominates

Risks to growth are tiled to the downside, with elevated uncertainty around the growth and inflation outlook



Source: IMF staff calculations. Note: Each shade of blue represents a 5-percentage point probability interval.

Risks to the Outlook

Downside

- Previous monetary policy tightening bites more than intended
- Financial markets reprice because of monetary policy reassessments
- Sovereign debt stress intensifies in EMDEs
- China's property sector contracts more deeply than expected
- Renewed spikes in commodity prices
- Countries ratchet up protectionist policies
- Social unrest resumes

Upside

- Stronger recovery in investment in advanced economies
- A stronger momentum of structural reforms

Risks Scenarios A: A Downside Alternative

Impact on GDP level

(percent deviation from baseline)





Impact on headline inflation

(percentage point deviation from baseline)

- —— Add global financial conditions
- —— Add lower migration
- Add renewal of US TCJA
- —— Add trade policy uncertainty
 - Tariffs



Risks Scenarios B: Policies to Address Existing Imbalances

Impact on GDP level

(percent deviation from baseline)



Impact on headline inflation

(percentage point deviation from baseline)

Add public investment in Europe
China rebalancing



Policy Priorities: From Restoring Price Stability to Rebuilding Buffers

Monetary and Financial Policies: Smooth Landing and Financial Stability

Anchor short- and long-term inflation expectations

- If inflation elevated and persistent: r>r*; if inflation consistently cooling and in sync with expectations, gradually move r to r* may be warranted; if inflation is consistently below target: r<r*
- Important to communicate consistently a commitment to price stability
- Restoring price stability while supporting growth and employment

Mitigate disruptive foreign exchange volatility

- Less synchronized central bank policies can lead to increased capital flows
- The IMF's Integrated Policy Framework provides guidance on appropriate policy responses
 - Deep FX market and low FX debt: adjust policy rates and allow exchange rate flexibility, provide rapid liquidity support when market stress arises
 - Shallow FX market or high FX debt: temporary FX interventions or capital flow management can be appropriate provided suitable monetary and fiscal policies are maintained
 - Global financial safety nets can provide support to countries vulnerable to external shocks
- Restore macroprudential buffers and ensure financial stability
 - Monitor financial risks in banks, NBFIs and real estate sector, strengthen supervision
 - Gradually rebuild macroprudential buffers deployed during the pandemic
 - Be prepared to deploy necessary financial stability tools when needed

Fiscal Policy: Rebuilding Fiscal Buffers ...

Required Fiscal Consolidation

(Percentage points)



• Urgently plan fiscal consolidation

- Many countries should start tightening to ensure debt sustainability and long-term budgetary flexibility
- The pace of consolidation should be gradual and well communicated
- Front-loaded fiscal adjustments may be needed to alleviate sovereign debt distress
- A credible medium-term plan is essential to achieve lasting consolidation
- A strong institutional framework could support the credibility of medium-term consolidation plans

Source: IMF staff calculations.





The Great Tightening: Insights **From the Recent Inflation Episode**

CHAPTER 2, OCTOBER 2024 WORLD ECONOMIC OUTLOOK **OUTREACH PRESENTATION**

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RESEARCH ASSISTANCE PROVIDED BY CANRAN ZHENG AND WEILI LIN.

Global inflationary pressures in 2021/22 led to a Global tightening cycle

Global Inflation

(Percent, year-over-year, SAAR)



Sources: WEO; and IMF Staff calculations.

Note: Lines are the median of consumer price index (CPI) inflation within each analytical group. The band depicts the 25th to 75th percentiles of data across economies. AEs = advanced economies; EMs = emerging market economies; LICs = low-income countries; SAAR = seasonally adjusted annual rates.

Post-2020 short-term interest rate

(Percent)



Sources: WEO; Haver Analytics; Ari et alii (2023); and IMF staff calculations.

Note: Encompasses 125 inflation episodes centered around 2021 and 2022. Median refers to median outcome across inflation episodes. Shaded areas indicate the 25th and 75th percentiles of data across inflation episodes. Short-term nominal interest rate are normalized at T-1. Real rate is in levels. Gray shaded area indicates the inflation shock identified as in the appendix. Green shaded area indicates projections.

Key Questions

1. What happened?

- What explains the last four years' inflation dynamics in advanced and emerging market economies?
- What was the contribution of shocks and policy settings in accounting for inflationary trends?
- 2. What was the monetary policy reaction and transmission?
 - Is there evidence that monetary policy response and transmission were significantly different this time around?
- 3. What lessons can we draw for monetary policy in a world with more frequent sectoral shocks?
 - Which structural characteristics of the impacted sectors matter for the policy response?
 - Is there a case for modifying monetary policy frameworks?
 - ► Timely question as major central banks are about to review their monetary policy frameworks.

1. What happened?

The inflation surge was global and unexpected

Global Inflation

(Percent, year-over-year, SAAR)



Sources: WEO; and IMF Staff calculations.

Note: Lines are the median of consumer price index (CPI) inflation within each analytical group. The band depicts the 25th to 75th percentiles of data across economies. AEs = advanced economies; EMs = emerging market economies; LICs = low-income countries; SAAR = seasonally adjusted annual rates.

Inflation Forecast Errors

(Median, year-over-year percent change)



Sources: WEO; and IMF staff calculations.

Note: Forecast errors are derived by comparing one-year ahead CPI inflation forecasts to actual figures in each year's April WEO. The actual values for a given year t are taken from the April WEO in the following year (t + 1). The bars represent median inflation rates, and the whiskers extend from the 25th to the 75th percentiles of data across economies. The data for 2024Q1 are annualized year-over-year percent changes, with a limited country sample due to quarterly data availability. AEs = advanced economies; EMs = emerging market economies; LICs = low-income countries..

Inflation had a strong sectoral component due to sectoral shifts, energy and food price shocks

Movements in Sectoral Prices – Average Sectoral Inflation

(Percent; annualized)



Sources: OECD; Haver Analytics; and IMF staff calculations.

Note: Figure displays the average inflation rates for goods (excluding food and energy) and services across a sample of 30 AEs and 13 EMs over time. Data are reported as deviations from 2018–19 average. AEs = advanced economies, EMs = emerging markets.

Inflation Driven by Energy and Food (Percent; annualized)



Sources: IMF, CPI database; and IMF staff calculations.

Note: Chart shows inflation contributions from broad categories. Contributions are computed first by country, annualized over available months where data are partial (e.g. for 2023). The chart shows the median contributions and aggregate inflation rate for each region.

Inflation surge driven by energy-dependent and flexible price sectors

Sectoral Inflation and Energy Dependence

(Percent, annualized rate)



Sources: BEA; Haver Analytics; OECD; WEO; and IMF staff calculations

Note: Energy dependence is computed using sectoral input-output matrices and defined as direct and indirect share of oil, gas, and utilities in sectoral inputs. Sectors are defined as energydependent if their energy dependence is above the median. Remaining sectors have low energy dependence. Sectoral inflation rates are represented by their respective median across high and low energy dependent sectors. Dashed vertical line indicates 2021Q4, the last quarter before the beginning of the war in Ukraine. Sectoral Inflation and Price Flexibility in Europe (Percent, annualized rate)



Sources: OECD; WEO; and IMF staff calculations.

Note: Inflation is measured as HICP inflation across Euro area sectors. Sectoral price flexibility is computed using data from Rubbo (2023). Sectoral data features 12 HICP sectors. Sectors are split along median of price flexibility and then inflation is aggregated across countries using PPP-country weights and within-country HICP weights.

Muted long-term inflation expectations and real wage movements

Stable Long-Term Inflation Expectations (Percent)



Sources: Consensus Economics; and IMF staff calculations.

Note: Figure reports 12-month ahead (solid lines) and long-term 10-year ahead (dashed lines) inflation expectations across advanced economies and emerging markets and developing economies. Each line represents in-group median. AE = advanced economies; EMDE = emerging market and developing economies.

Moderate Real Wage Growth (Percent, annualized rate)



Sources: ILO; OECD; and IMF staff calculations.

Note: Figure reports real wages computed as nominal wages (defined on a per-worker basis) divided by the CPI and then indexed to 100 in each country in 2017Q1. Each line reports group median. AE = advanced economies; EMDE = emerging market and developing economies.

Across the globe, the Phillips curve steepened and shifted up

Core Inflation Deviations vs. Unemployment Gap (*Percent*)



Sources: Haver Analytics; and IMF staff calculations.

Note: The first two quarters of 2020 are excluded. X-axis shows unemployment gap and y-axis denotes core inflation deviation. Inflation measures are residualized on a country fixed effect within each country. Blue and red lines are linear fits with a sample of 29 advanced economies and 15 emerging markets during the period from the first quarter of 2010:Q1 to the first quarter of 2024. "Post-COVID" is defined as 2020:Q1 onward. The unemployment gap is estimated using a univariate Hodrick-Prescott filter. Outliers with deviations of inflation from country average by more than 20 percentage points are excluded.

Steepening of empirical Phillips Curves (Percent for 1ppt change in slack)



Sources: Haver Analytics; WEO; and IMF staff calculations. Note: Figure reports distribution of Phillips curve slope changes across countries from country-level estimations of pre-2020 and post-2020 Phillips curves. The sample starts in 2010 and the first two quarters of 2020 are excluded. Outside values (more than 1.5 interquartile ranges below first quartile or above third quartile) are excluded from boxplots. AEs = advanced economies, EMs = emerging markets.

Headline shocks and subsequent passthrough were key. Labor markets less so.

Inflation Drivers in the US, other AEs, and EMs

(Percent, annualized rate)



Sources: Consensus Economics; Haver Analytics; and IMF staff calculations.

Note: US inflation drivers are estimated on monthly data (following Dao and others 2024) and then converted to quarterly; for other countries, estimation is conducted on quarterly data. "Slack" is measured using the vacancy-to-unemployment ratio for AEs and using the unemployment gap (estimated using a univariate Hodrick-Prescott filter) for EMs. Country-level contributions for AEs and EMs are aggregated across country groups using purchasing-power-parity GDP weights. Fitted values for inflation gap are converted into 12-month rates. AEs = advanced economies; EMs = emerging markets.

2. Monetary policy reaction and transmission: a comparison with pre-2020 episodes
There was a synchronous monetary policy response, with some EMs hiking earlier

Monetary Tightening – Real Policy Rate

(Percent, annualized rate)



Sources: Bank for International Settlements; Consensus Economics; Haver Analytics; and IMF staff calculations.

Note: Real policy rates are computed as nominal policy rates minus 1-year ahead inflation expectations. Sample includes 16 AEs and 65 EMDEs. "Other" aggregates are medians. AEs = advanced economies; EMDEs = emerging market and developing economies. Early hikers=Brazil, Chile, Hungary, New Zealand, Norway, Peru, Poland and South Korea.

Economic Conditions at lift-off (*Percent*)



Sources: Bank for International Settlements; Haver Analytics; and IMF staff calculations. Note: Figure reports economic conditions at first interest rate hike during current tightening cycle for early hikers (Brazil, Chile, Hungary, New Zealand, Norway, Poland and South Korea), Canada, Euro Area, UK, and US. Countries are sorted by the timing of their first interest rate hike. Headline inflation, output gap, and change in nominal effective exchange rate are all reported in percent.

Post-2020 episodes were associated with looser policy stance than resolved episodes of 1970s





Sources: WEO; Haver Analytics; Ari et alii (2023); and IMF staff calculations.

Note: An inflation episode is categorized as "resolved" if inflation falls to within 1 pp of its pre-shock rate by the end of 5-year window. 1970s resolved includes 13 inflation shock episodes (1973-1979). Post-2020 encompasses 125 inflation episodes centered around 2021 and 2022. Median refers to median outcome across inflation episodes. Dashed lines indicate the 25th and 75th percentiles of data across inflation episodes. Inflation and short-term nominal interest rate are normalized at T-1. Real rate is in levels. Gray shaded area indicates the inflation shock identified as in the appendix. Green shaded area indicates projections.

Post-2020 episodes were associated with tighter policy stance than unresolved episodes of 1970s





T-5 T-4 T-3 T-2 T-1 T T+1 T+2 T+3 T+4 T+5

-6

-8

Sources: WEO; Haver Analytics; Ari et alii (2023); and IMF staff calculations.

Note: An inflation episode is categorized as "resolved" if inflation falls to within 1 pp of its pre-shock rate by the end of 5-year window., otherwise "unresolved." 1970s unresolved includes 12 inflation shock episodes (1973-1979). Post-2020 encompasses 125 inflation episodes centered around 2021 and 2022.. Median refers to median outcome across inflation episodes. Dashed lines indicate the 25th and 75th percentiles of data across inflation and short-term nominal rate are normalized at T-1. Real rate is in levels.

Post-2020 tightening with respect to Taylor-rule-implied tightening is in between resolved and unresolved inflation episodes of 1970s

Deviation from Taylor-Rule-Implied Tightening (*Percent*)



(Variance normalized by its mean) 1.0 0.8 0.6 0.4 0.2 0.0

Unresolved 1970s

Post 2020

Pre-shock inflation volatility

Resolved 1970s

Sources: WEO; Haver Analytics; Ari et alii (2023); and IMF staff calculations.

Note: 1970s unresolved includes 12 inflation shock episodes and 1970s resolved episodes include 13 inflation shock episodes (1973-1979). Post-2020 encompasses 125 inflation episodes centered around 2021 and 2022. Bars refer to averaged pre-shock inflation volatility across inflation episodes, defined as the variance of inflation between T - 5 and T - 1 normalized by its mean over the same period.

3. What lessons can we draw for monetary policy in a world with more frequent sectoral shocks?

A non-linear multi-country and multi-sector new-Keynesian model with sectoral constraints for analyzing the Great Tightening

Example of Supply Constraint



Note: Figure shows an example of a constraint in our model. This shows the output price against the value added of that sector. In the model value added is comprised of labor (which can be constrained) and a fixed factor. A labor constraint thus limits value added and raises the output price of the firm

Model Environment

- Dynamic New Keynesian framework
- Two-country model (USA and ROW)
- Multi-sector production with input-output linkages (11 sectors)
- Occasionally binding labor usage constraints by sector
- <u>Shocks (Scenarios)</u>
 - Aggregate: Monetary policy, Fiscal policy, Aggregate demand, Labor supply
 - Sectoral: Productivity, Preference, Labor constraint

• <u>Two Model Experiments</u>

- Phillips Curve steepens due to arbitrary supply constraints
- Alternative monetary policy experiments, both for 2020-2023 and for specific shocks.

Occasionally binding supply constraints steepen Phillips Curve

US Phillips curve under different constraints (Percent)



US labor response to monetary shocks with constraints (*Percent*)

Sources: IMF staff calculations

Note: The blue line shows the combination of the impact effect of real GDP (x-axis) and inflation (left-scale) on monetary policy shocks of various sizes. The grey bars (right scale) show the share of the economy constrained. The red line shows the same combination without any supply bottlenecks imposed. The Phillips curve shape will depend on the choice of constraints. The right panel shows labor in each sector in the model with monetary policy changes on the x-axis and the change in labor on the y-axis. Dotted lines are the sector-level constraints imposed in each sector.

Occasionally binding supply constraints steepen Phillips Curve

(Percent)

Phillips Curve with constraints plus sectoral demand shocks

Phillips curve with occasionally binding constraints (*Percent*)



Sources: IMF staff calculations

Note: The blue line shows the combination of the impact effect of real GDP (x-axis) and inflation (left-scale) on monetary policy shocks of various sizes with panel 2 also including a relative demand shock. The grey bars (right scale) show the share of the economy constrained. The red line shows the same combination without any supply bottlenecks imposed. The Phillips curve shape will depend on the choice of constraints.

Supply Constraints in 2020-2023 lowered GDP & raised inflation

Contribution of supply constraints to <u>Inflation</u>

(Percent from trend, quarter over quarter, annualized)



Contribution of supply constraints to <u>Real GDP</u> (*Percent deviation from trend*)



Sources: IMF staff calculations

Note: The line in panel 1 shows inflation and the line in panel 2 shows real GDP. The bars show the contributions from different groups of shocks. Note that the sum of all bars will equal the black line in each period.

Policy tightening costs less output loss when supply bottlenecks are prevalent



Sources: Federal Reserve Economic Data; Organisation for Economic Co-operation and Development; and IMF staff calculations.

Note: "Tighten early" scenario assumes rates rise three quarters earlier. Standard monetary policy counterfactuals assume identified labor constraints remain. "No bottlenecks" assumes the wedge between the marginal product of labor and wages (shadow price of constraint) is kept consistent with the data, but the constraint does not bind.

Coordinated tightening expedites disinflation process

• Sceanrio (red line)

ROW tightens policy later than US

US remain as observed

Bar graphs

Sectoral decomposition of difference between red and black lines

Implications

- Flexible price sectors (blue) act immediately
- Other sectors react through input-output linkages int. with price stickiness

US inflation (QoQ annualized)



Sources: Federal Reserve Economic Data; Organisation for Economic Co-operation and Development; and IMF staff calculations.

Note: "The rest of the world (ROW) delays tightening" scenario assumes ROW hiking is delayed three quarters and US rates remain as observed. Identified labor constraints are assumed to remain. The right-hand y-axis shows percentage point difference in sectoral inflation between the observed data and "ROW delays tightening" scenario.

Targeting inflation in the stickiest-price sectors remains appropriate when supply bottlenecks are sparse



Source: IMF staff calculations.

Note: The Taylor rules are identical except for the inflation measure targeted. "Targeting stickiest prices" targets the five sectors with the steepest Phillips curves. "Inflation forecast targeting" targets the four-quarter moving average of future CPI inflation. "Average inflation targeting" represents average inflation targeting in which the central bank targets the average of the previous four quarters of inflation. "50/50 CPI and constrained sectors" targets CPI inflation and sectoral inflation in agriculture, mining, and energy. "Flexible prices" shows relative prices in a scenario without nominal rigidities in any sector market. In each case the Taylor parameter is 3, the persistence parameter is 0.5, and neither GDP nor the output gap is targeted. CPI = consumer price index.

Conclusions

Conclusions – Looking backward

- To understand the recent global inflation surge, the analysis needs to go beyond tradition macro aggregates
 - Inflation spikes in specific sectors became embedded in core inflation
 - Interaction between soaring demand in some sectors and sector-specific bottlenecks and shocks is crucial
- New Lesson: When supply bottlenecks become widespread and interact with strong demand, the Phillips curve gets steepened
 - Inflation surges as many sectors hit capacity constraints
 - Curbing inflation is possible at a lower cost in terms of lost economic output
- Old lesson: When supply bottlenecks are confined to specific sectors:
 - Focusing on sectors with the stickiest prices remains appropriate (e.g. targeting Core inflation)

Conclusions – Looking forward

- Given these insights, central bank monetary policy frameworks should identify conditions under which frontloaded tightening is appropriate
 - Use of enhanced models with sectoral detail
 - Use of sectoral <u>data</u> to gauge underlying inflationary forces, improve forecasts
 - Escape clauses when using forward guidance to allow central banks to react when the Phillips Curve steepens





World Economic Outlook October 2024

THANK YOU!





UNDERSTANDING THE SOCIAL ACCEPTABILITY OF STRUCTURAL REFORMS

CHAPTER 3 – WORLD ECONOMIC OUTLOOK - OCTOBER 2024

Silvia Albrizio, Hippolyte Balima, Pragyan Deb, Bertrand Gruss, Eric Huang, Colombe Ladreit, and Yu Shi; with support by Yaniv Cohen, Shrihari Ramachandra, and Isaac Warren.

Implementing critical reforms is increasingly challenging amid weak social acceptability

Uneven progress on reforms to ease resource reallocation and boost labor supply.

Regulatory Stance

(Ratio to the highest score across all countries and periods)





Widespread and increasing social resistance increases urgency to understand social acceptability.

Protests by Reform Area (Number of Countries)



Sources: Mass Mobilization Project; and IMF staff calculations. Note: The lines shows the 5-year moving averages of the number of countries facing protests, with x-axis labels indicating the final year of the rolling window. EPL = employment protection legislation; PMR = product market regulation. Social resistance can slow reform progress and/or lead to reform reversals.

Reform Resistance and Likelihood of Reversals

(Percent of reform episodes)



Sources: IMF Structural Reforms Database; Barrett and others (2022); and IMF staff calculations.

Note: The figure displays, for each reform area, the percentage of implemented reforms, both contested and uncontested, that experienced a reversal within 5 years. ***, **, and * denote significance at the 1, 5, and 10 percent levels, respectively, for t-tests comparing reversal rates between resisted and unresisted implemented reforms. LP = labor participation; PMR = product market regulation.

Key questions

- How difficult has it been to implement structural reforms? What are the key factors affecting reform outcomes?
- What drives individuals' attitudes toward reforms? To what extent do individual characteristics and economic self-interest determine support? What is the role of perceptions, information, and other beliefs in driving policy preferences?
- What **tools, strategies, and institutions** can help policymakers forge consensus, improve the policy design process, and ensure that reforms not only are implemented but also endure?

Preview of methodology and findings

Historical analysis: New database that disentangle reforms discussion and implementation

How difficult has it been to implement structural reforms in the past?

- > Pace of reform efforts has more than halved since 2008–09, coinciding with rising discontent
- > Reform strategies are more reliable predictors of reform implementation

Online surveys: Surveys of +12K individuals from 6 countries covering 2 policy areas

What drives people's attitudes toward reforms?

- Individuals' beliefs and perceptions explain about 80 percent of reform support
- Concerns about others and community account for +50 percent of reasons cited for opposing reform

What tools, strategies, and institutions can help policymakers forge consensus and ensure enduing reforms?

- > Effective information is key to correct biased beliefs on the need for reforms and the benefits of reforms
- > Mitigating measures addressing respondents' concerns are pivotal, although trust deficit is the ultimate challenge

Case studies: In-depth review of 11 labor market reform episodes

Employ a multi-faceted strategy to enable a more participative policy design process, engage in a two-way dialogue, provide mitigation measures and reinforce trust in public institutions

Historical analysis

Historical overview: How difficult has it been to implement structural reforms?

Novel narrative database (EIU reports; 26 AE, 36 EMMIEs, 14 LIDCs; 1996-2023):

Status (discussion, adoption, implementation); policy measures; resistance and adjustments; communication; compensation.

Reform areas: *PMR reforms* to foster private participation & competition in the electricity sector; *Migrant integration reforms* to aid the labor market integration of foreign-born workers; *Elder Labor Participation reforms* to boost older workers' labor supply.



Sources: Economist Intelligence Unit, World Economic Outlook (WEO) Database; and IMF staff calculations.

Note: The figure shows the shares of reform episodes across reform areas by implementation outcome: implemented (not resisted); implemented but resisted; implemented but resisted and diluted; and not implemented. AEs = advanced economies; EMEs = emerging market economies; LICs = low-income countries; LP = labor participation; PMR = product market regulation.

INTERNATIONAL MONETARY FUND

Determinants of implementation outcomes: analytical framework

Multinomial logistic regression with three reform outcomes:

- Discussed & not implemented (0)
- Implemented and resisted and/or diluted (1)
- Implemented (without being resisted or diluted) (2)

$$\log\left(\frac{\Pr(outcome_{it} = j)}{\Pr(outcome_{it} = 0)}\right) = \gamma_j Z_{it} + \beta_j X_{it} + \alpha_{g(i)} \text{ for } j = 1,2$$

- Z_{it} : vector of determinants
- X_{it}: vector of controls capturing country-specific economic, political & demographic characteristics
- $\alpha_{g(i)}$: country income group fixed-effects

How did the context and strategies influence implementation outcomes?

Macroeconomic and **political contexts** matter for implementation, but the role and significance varies across reform areas.

Reform strategies jointly explain 28 percent of implementation likelihood.

 By comparison, macroeconomic and political contexts explain 16 and 22 percent.

Consultation, communication, and mitigating strategies appear to be more robust predictors of implementation. **Relative Importance of Reform Strategies for Predicting Reform Implementation** (Share of implementation likelihood explained, percent)

Consensus-building strategies significantly boost chances of implementing reforms.



Note: The figure shows the relative predictive power of each set of factors for the implementation of reform proposals across different areas. Estimates are obtained through dominance analysis based on a multinomial logistic regression (Online Annex 3.2.). PMR = product market regulation; LP = labor participation. Sources: World Economic Outlook (WEO) Database, Economist Intelligence Unit, Kose and others (2022), Nguyen and others (2022), Monitoring of Fund Arrangements (MONA) Database, Database of Political Institutions, Global Leader Ideology dataset, the Standardized World Income Inequality Database, Our World in Data, IMF Structural Reform Database; and IMF Staff Calculations.

Survey analysis: Individual characteristics, beliefs, and (mis)perceptions

Surveys of individuals: Understanding people's attitudes towards reforms

Objective 1: Uncover drivers of people's attitudes toward reforms.

Objective 2: Test whether informing people about the cost of the status quo and/or the effects of policies correct people's misperceptions and increase their support for reform.

Objective 3: Assess whether addressing their concerns towards the reforms through the provision of hypothetical complementary and compensatory measures improve reforms support.

Advantage of surveys:

- Randomized control trial (RCT): causal identification
- Capture behavioral aspects
- Direct link between individual concerns and complementary policy options

Applications:

- EMDEs: Reforms to increase private participation in electricity and telecommunication sectors (MA, MX, ZA)
- > AEs: Policies to integrate foreign-born workers in the labor market (CA, IT, UK)

Survey I – Attitudes towards reforms

Measuring support for reforms

PMR survey:

Some countries have adopted reforms allowing private companies to compete among themselves and with public companies to produce and sell **electricity** to the population. In some cases, the government also sold its own electricity business to private companies.

Do you support or oppose allowing private companies to produce and sell electricity in South Africa?

- O Strongly oppose
- O Somewhat oppose
- O Neither oppose nor support
- O Somewhat support
- O Strongly support

Migrant integration survey:

Would you support or oppose the following policies to help immigrants find jobs in the UK? Please select one option for each of the policies proposed:

	Strongly oppose	Somewhat oppose	Neither support nor oppose	Somewhat support	Strongly support
Supporting immigrants in creating new businesses (through access to financing, mentoring, and networking).	0	0	0	0	0
Giving immigrants work authorization as soon as they arrive.	\bigcirc	\bigcirc	0	\bigcirc	\bigcirc
Providing job training and job search assistance for immigrants.	\bigcirc	\bigcirc	0	\bigcirc	\bigcirc
Making it quicker and easier to recognize immigrants' work experience and qualifications from other countries.	0	\bigcirc	0	0	0

Testing for policy support

$$y_{ic} = \beta_1 T_{i,c} + \beta_2 Soc_{i,c} + \beta_3 Bel_{i,c} + \theta_c + \varepsilon_{i,c}$$

- *y_{ic}* captures the policy support for the individual *i* of country *c*
- $T_{i,c}$ is the treatment indicators
- **Soc**_{*i*,*c*} a vector of socioeconomic characteristics
- **Bel**_{*i*,*c*} a vector of beliefs and perceptions
- θ_c country fixed effects
- Robust standard error

Who supports product market reforms?

Distribution and equity Market economy Trust and corruption Views and satisfaction with sector Knowledge and effect of policies Government role in economic activity Government role in regulating the economy Government role in price setting Perception of foreign companies Perception of foreign companies in utilities Fairness Standard of living Government role in ensuring access to utilities Utility companies' role in ensuring equity Trust in people Trust in government Trust in institutions Corruption in the country Corruption in utilities Perception of private participation in utilities Satisfaction with utility services Lack of access to utility services Knowledge about the utility service's regulator Perception of the effect of competition on price Perception of the effect of competition on quality Perception of the effect of competition on access -0.1 0.0 0.1

Source: Source: YouGov online survey conducted in Mexico, Morocco, and South Africa, with 2,100 respondents per country. IMF Staff calculations.

Note: The figure shows the coefficients from an OLS regression of Support on individual beliefs, controlling for individual characteristics, treatment indicators, and country fixed effects. Support and beliefs are transformed into z-scores. A positive coefficient indicates an increase in Support for policies. Bars represent 90% confidence intervals.

Support for product market reforms correlates with:

- 1. Individual Characteristics (not shown):
 - Employment in utilities a.
 - Demographics b.
 - Income C.
 - d. Political leaning
- 2. Individual Beliefs:
 - Pro-market beliefs а.
 - Fairness b.
 - Trust and corruption C.
 - PMR-related beliefs d.
 - Perceptions on the effect of policies e.

0.3

0.2

Correlation Between Policy Support and Individual Beliefs (Coefficients)

Who supports policies for the integration of migrant workers?

Support for policies to help immigrants find jobs correlates with:

- 1. Individual characteristics (not shown) :
 - a. Socioeconomic status
 - b. Race and immigrant background
 - c. Voluntary contact with immigrants
- 2. Beliefs:
 - a. Trust, Universalism and Life Satisfaction
 - b. Political Leaning
 - c. Beliefs and Knowledge of Immigration Policies
 - d. Stereotypes of Immigrants

Correlation Between Policy Support and Individual Beliefs *(Coefficients)*



Source: YouGov online survey conducted in Canada, Italy, and the United Kingdom, with 2100 respondents by country. IMF Staff calculations.

Note: The figure shows the coefficients from an OLS regression of *Support* on individual beliefs, controlling for individual characteristics, treatment indicators, and country-region fixed effects. All the covariates are dummy variables, except knowledge variables that are z-scores with respect to the control group of the corresponding country. Stereotypes variables are dummies constructed from frequency counts from open-ended questions. Stereotype –Positive(Negative) consider both positive (negative) immigrants' traits and their effect on the economy. A positive coefficient indicates an increase in *Support* for policies. Bars represent 90% confidence intervals.

What matter the most? Beliefs versus socioeconomic characteristics

Support for reforms is largely driven by beliefs and perceptions about effects of policy (Share of support explained, percent)



Source: IMF staff calculations based on IMF-YouGov survey.

Note: The figure shows the results of a dominance analysis that quantifies the share of variance in support for reforms or policies explained by individuals' socioeconomic characteristics and different sets of beliefs and perceptions based on an ordinary least squares regression (Online Annex 3.3.1). The regression controls for country fixed effects and treatment indicators, whose contributions are not shown. PMR = product market regulation.

Survey II – Information Strategies to Boost Reform Acceptability

Information strategies to boost reform acceptability

Hypotheses to Boost Policy Support				
Survey	Treatment: Information provided	Hypothesis		
PMR Reform	<i>Status quo:</i> Cross-country evidence on the cost, quality, and access to electricity or telecommunication services.			
	Status quo + effects of policies: Research-based evidence on the effect of policies to foster competition in network sectors on cost, quality, and access to electricity and telecommunications services.			
Migrant Integration Policies	<i>Effect of policies:</i> Research-based evidence on the effect of policies to integrate foreign workers on labor market outcomes for native workers, public finances, and immigrants' crime rates. <i>Effect of policies + mechanisms:</i> Adds detailed information explaining the mechanisms through which immigration policies lead to those outcomes.	Effect of policies		
	<i>Immigrants' stories:</i> Three stories sourced from newspaper articles about immigrants' struggles in the labor market, their perseverance, and their success.	Empathy		
Courses IME	staff som nilstion			

Source: IMF staff compilation.

Note: PMR = product market regulation.

Can information provision foster support reforms? – Treatment snapshots

Example of the *Information Treatment 1* slide for South Africa



*Source: Prices in national currency from the International Energy Agency (IEA) are adjusted by the purchasing power of the South African Rand vis-à-vis the US dollar.

Electricity is also less reliable in South Africa than in richer countries. About 92% of the companies in South Africa report that they face electricity power cuts, for about 2 hours and 20 minutes each time.*



Example of the *Information Treatment 1* slide for United Kingdom

Finally, in many countries, studies* have found that having more immigrants come in does not make crime rates go up. And when immigrants are allowed to work legally, their involvement in crime goes down by 50%. (*studies by Bocconi University, McGill University, and Stanford University)



*Source: World Bank.

United States*.

Effect of information strategies on reform support

Effect of Information Strategies on Reform Support

(Additional support relative to the control group, percentage points)



Most effective treatments:

PMR reforms:

Status quo + effect of policies. The share of respondents who would support *PMR reforms* increases by almost 16 percentage points w.r.t. control, on average, across sectors.

Migrant integration policies:

Effect of policies + mechanism. The 11pp treatment effect is equivalent to about 42% of the share opposed in the control.

Source: IMF staff calculations based on IMF-YouGov survey.

Note: The figure shows the difference in support shares between each treatment group and the control group. Dark blue bars denote that the difference is statistically significant at the 90 percent confidence level according to the regression analyses in Online Annex 3.3.1 and 3.3.2. PMR = product market regulation.
Effect of information strategies on beliefs about policy effects

PMR: "How do you think private companies competing to provide [electricity/telecommunication services] change things? Think about the service cost, quality and access?"

Migrant Integration: "Imagine that the government implemented measures to integrate immigrants in the labour market. How do you think this would affect the following elements in the UK?" Natives Job / Money the gov't gets form taxes / Crime immigrants commit



Treatment Effects on Beliefs about Policy Effects

Source: IMF-YouGov online survey with 6,300 respondents per survey. IMF Staff calculations.

Note: The charts show the coefficients from OLS regressions of post-treatments *Beliefs* (PMR survey right-hand chart, *Migrant Integration* left-hand chart) indicators on dummy variable indicators for each treatment, controlling for a set of individual characteristics and beliefs, as well as country fixed effects. Bars represent 90% confidence intervals. In the case on Migrant integration policies, Post-treatment beliefs variables are z-scores with respect to the country-level control group.

Correcting biased beliefs by explaining the mechanisms

Effect of Information Strategies on Reform Support (*Coefficients, average and marginal effect*)



Source: IMF staff calculations based on IMF-YouGov survey.

Note: The figure presents the treatment average effect on policy support and marginal effects for respondents with pre-treatment negative stereotyped views about immigrants and right leaning respondents, respectively. The dots indicate the point estimates, and the spikes represent the 90% confidence intervals.

Survey III – Mitigation strategies and ultimate reasons for opposition

Mitigation strategies: complementary and compensatory measures

Reasons for Nonsupport and the Role of Compensatory and Complementary Measures

(Share of responses, percent)



Source: IMF staff calculations based on IMF-YouGov survey.

Note: The blue bars show the distribution of respondents' reasons for not supporting the reform (control group only). The yellow (red) bars display the proportion of these respondents that would opt to support (remain against) policies if offered mitigating measures (Online Annex 3.3.3.). PMR = product market regulation.

Understanding ultimate social resistance: trust deficit

Ultimate Reason for Non-Support (Percent)

1. PMR Reform

Don't want the private sector or foreign investors to control the provision of services	43.83
Don't trust the private sector	35.86
Don't trust the government's willingness or ability to implement good reforms	18.19
Other reasons	2.12

2. Migrant Integration Policies

Don't trust the government's willingness or ability to implement good reforms	53.94
Don't want foreign workers in the country	14.90
Doubt effectiveness or feasibility of policies or mitigating measures	10.97
Concerns about jobs	7.28
Fiscal constraints	6.86
Other reasons	6.05
Source: IME staff calculations based on IME You Cov survey	

Source: IMF staff calculations based on IMF-YouGov survey.

Note: PMR = product market regulation.

Lesson from country case studies

Country cases – EPL reforms

Country cases	Country Classification at Reform	EPL change	Other Policy Focus	Implementation Status
Bolivia, 1986	LIDC	Major	Wage bargaining	Reverted in 2006
Denmark, 1990s	AE	Minor	ALMP, Unemployment benefits	Implemented and sustained
Georgia, 2006	LIDC	Major	Working hours and leaves	Reverted in 2013
Germany, 2003-05	AE	Minor	ALMP, unemployment benefits, temporary work	Implemented with some resistance
France, 2015-17	AE	Minor	Collective bargaining, temporary work	Implemented and sustained; further planned reforms in the area slightly delayed
Brazil, 2017	EMMIE	Minor	Labor litigation, collective bargaining, outsourcing	Implemented with some resistance
India, 2014-2020	EMMIE	N/A	Minimim wage, working conditions	Legislated in 2020 but not yet fully implemented
Mexico, 2012	EMMIE	Minor	Collective bargaining	Implemented and sustained
Peru, 2008	EMMIE	Minor	Flexible working hours and easing regulation	Implemented with adjustments
Vietnam, 2012	LIDC	Minor	Regulations on labour contracts and labor protection	New Labor Code enacted in 2012
South Korea, 2016	AE	Minor	Ehance flexibility and stability in the labor market	Largely withdrawn due to resistence

Source: IMF Staff.

Lessons from case studies



Summary and policy implications

- 1. Passing structural reforms has historically been challenging. Context of reform attempts can help but is not determinant; active use of strategies to build consensus matters more.
- 2. Beliefs and perceptions can matter more than individual characteristics and economic self-interest for the social acceptability of policies.
- 3. Effective communication can influence beliefs, correct misperceptions, and ultimately drive policy preferences.
 - ▶ Providing information on the need for reform can help. Explaining the effect of policies is critical.
- 4. Building consensus and ensuring that reforms can be sustained requires an expanded toolkit and strong institutions that foster trust.
 - ▶ Information Trustworthy communication on why reform is needed and how policies affect people.
 - **Engagement** Dialogue with public needs to work in both directions and start early, when reform is designed.
 - ▶ **Mitigation** Careful design, with adequate measures to mitigate impact on most vulnerable.
 - **Trust** Backed by institutions and mechanisms that inspire trust.





World Economic Outlook October 2024

THANK YOU!