Box 2.2

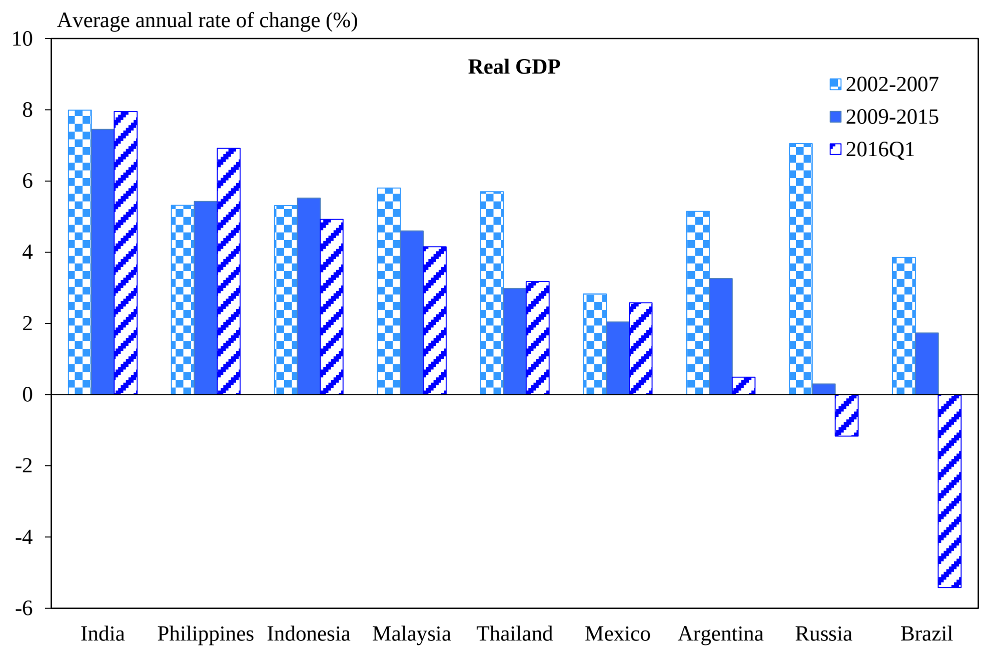
Recent economic performance of emerging market economies

The global economy has been stuck in low gear after the 2008 Global Financial Crisis (GFC), as many advanced economies are still struggling to gain traction. While emerging market economies (EMEs) remain the bright spot, they have also experienced varying degrees of growth slowdown since 2010. This note briefly reviews the recent economic performance of selected EMEs[1]. The performance of the Mainland economy is separately discussed in ***Box 2.3***.

For EMEs as a whole, economic growth, while still notable, averaged 5.1% per annum in 2009-2015, and was visibly slower than the expansion pace of 7.2% per annum in the pre-crisis period (2002-2007). A key drag stemmed from the persistently weak external demand, amid the sluggish growth in the advanced economies. This was evident in the notable moderation in the growth of EMEs' merchandise exports to 3.7% per annum in volume terms in 2009-2015, from 10.8% per annum in 2002-2007. Also, EMEs' investment spending expanded at a much softer pace, as compared to the investment boom in the pre-crisis period. As a percentage share of GDP, investment spending in EMEs increased markedly from 24% in 2001 to 30% in 2008, but had barely changed since then, only edging up to 31% in 2015.

Nevertheless, the economic performance of individual EMEs varied greatly. ***Chart 1*** shows that the slowdown in growth after the GFC was not particularly apparent in some EMEs, with some even expanding at faster paces in the first quarter of 2016. These were mainly Asian EMEs, which generally held up well, thanks to their better fundamentals and resilient domestic demand. Their consumption spending growth was particularly impressive, helping to cushion against the lull in external trade. On the other hand, many EMEs in other regions slackened markedly after the GFC, and showed little improvement in the latest period.

Chart 1 : Asian EMEs fared relatively better as compared to their counterparts



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(1) EMEs covered in this box article include Argentina, Brazil, India, Indonesia, Malaysia, Mexico, the Philippines, Russia and Thailand.

Box 2.2 (Cont'd)

Among Asian EMEs, India saw exceptional growth, expanding briskly by 7.5% per annum in 2009-2015, and its growth picked up further to 7.9% year-on-year in the first quarter of 2016. Meanwhile, Indonesia and the Philippines also performed well, helped by robust investment spending amid higher infrastructure investments.

In contrast, economic activities in Russia and Brazil have slowed sharply and experienced contraction since 2015, mainly dampened by the sharply lower energy and commodity prices. In the case of Russia, economic sanctions from the West, which have been extended till January 2017, posed an additional downward pressure on its exports. As for Brazil, the increasing political instability and worries about the sustainability of its public finances have eroded consumption and investment confidence. In addition, the currencies of these two economies weakened significantly against the US dollar alongside capital outflows, leading to a surge in imported inflation. Russia's central bank increased policy rates sharply in late 2014, while Brazil's central bank raised interest rates successively since end-October 2014. But monetary tightening dealt a further blow to their economic activities.

Looking ahead, while the sustained growth of EMEs in Asia would continue to help shift the gravity of the global economy towards the East, we still need to be mindful of any sudden increase in risk aversion under the still-challenging external environment, as this could trigger abrupt shifts in capital flows and exert downward pressures on those EMEs with weaker economic fundamentals and less resilient financial systems. Therefore, it is useful to examine the latest state of fiscal and financial health of these economies. ***Charts 2a and b*** present an update to ***Box 1.1 in the Half-yearly Economic Report 2015***.

Chart 2a : Current account and fiscal balances are important indicators of an economy's financial health

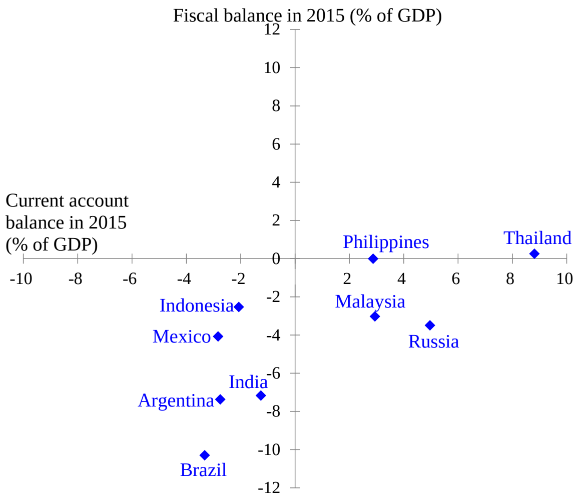
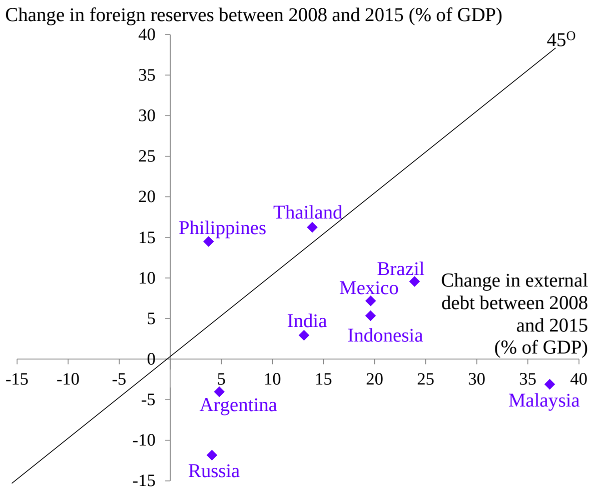


Chart 2b : Sudden shifts in capital flows would exert more pressure on economies with a visible build-up of external debt



It can be seen from the two charts that some of the EMEs are still faced with external and/or internal imbalances, i.e. current account and/or fiscal deficits. Hence, they may be more prone to sudden capital reversals and sharp currency fluctuations, especially if they have also accumulated sizeable external debts, as already experienced during mid-2013 and August 2015. Nonetheless, should these EMEs have an ample amount of foreign reserves, it would hopefully help stabilise their currencies against a sharp rise in capital outflows.

Box 2.2 (Cont'd)

In July, the IMF maintained its GDP growth projection for EMEs as a whole at 4.1% in 2016, which if attained, would contribute around three-quarters of the world's economic growth. In particular, EMEs in Asia were projected to grow by 6.4% in 2016, faster than EMEs in other regions. These projections, however, were made under the benign assumption of a gradual reduction in the uncertainties related to the UK vote to leave the EU.

In view of the various downside risks to the global economy, the IMF warned that the scope for short-run demand support may be limited in some EMEs during periods of heightened global risk aversion and policymakers in EMEs should strengthen defences against increased global financial volatility for an extended period of time, while continuing to bolster medium-term growth prospects through structural reforms. Hence, we will need to keep a close watch on the economic situation in EMEs and stay vigilant to any potential adverse impacts on Hong Kong's near-term economic growth and prospects.