

The Impact of the Financial Crisis on Developing Countries

EE 462 Development Macroeconomics

Reference: “Lin, Justin Yifu. 2008. *The Impact of the Financial Crisis on Developing Countries*. World Bank, Washington, DC. © World Bank.
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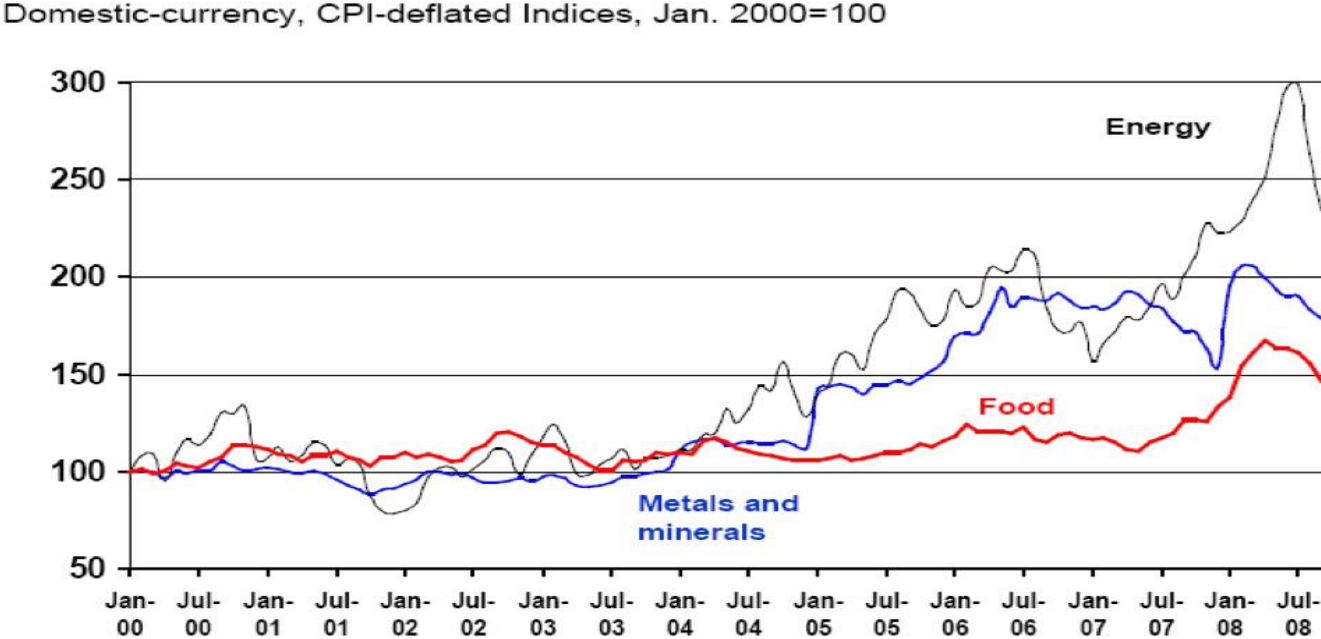
Outline

- Dynamics of global growth in 2002-2007
- Economic downturn in 2007-2008
- Impacts of crisis on developed and developing countries

Dynamics of global economy in 2002-07

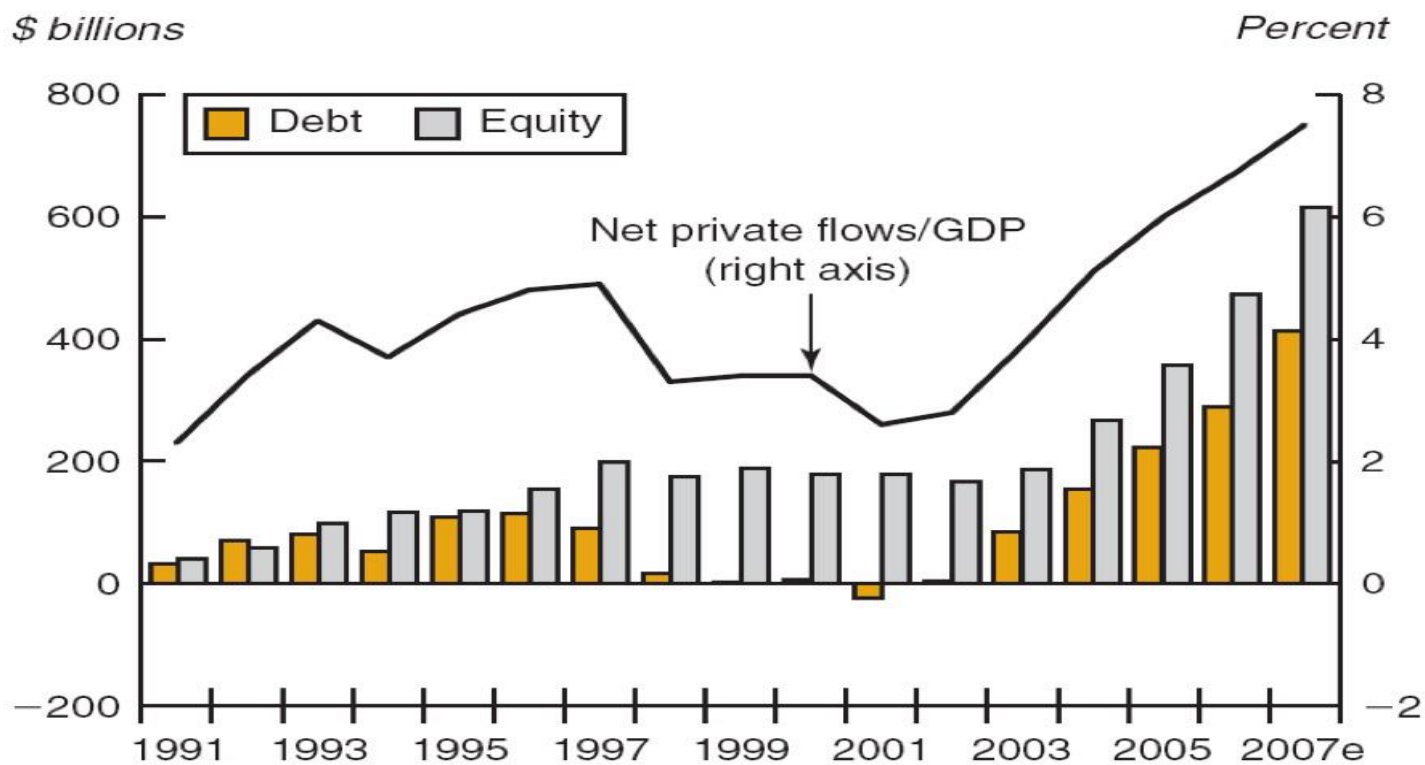
- Developed-country growth fueled by expansionary monetary and fiscal policy
 - US tech-stock and housing bubbles
 - low interest rate
 - Deregulation of financial market
- The investment-led boom in developing world
 - CA surplus
 - Increasing FDI
 - Increasing investment in stock market
 - Rapid growth in BRICs

Figure 1: Real commodity price indices, 2000-08



Source: World Bank data

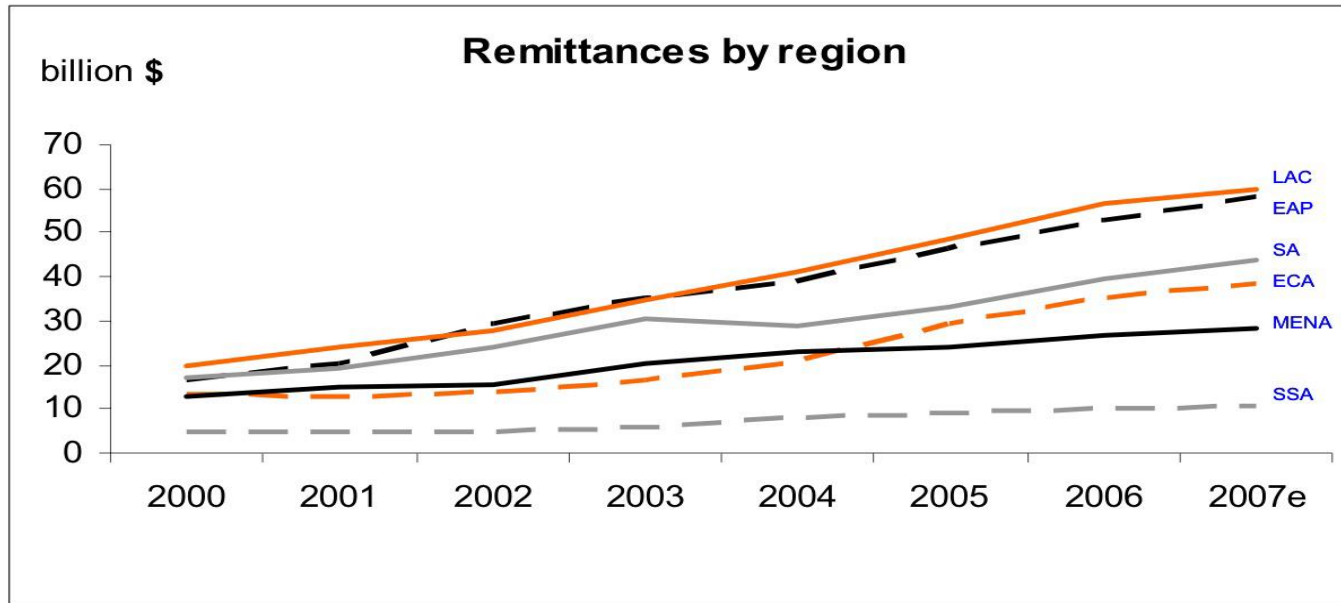
Figure 2: Private capital flows to developing countries, 1990-2007



Note: Equity flows include both foreign direct investment and portfolio investment.

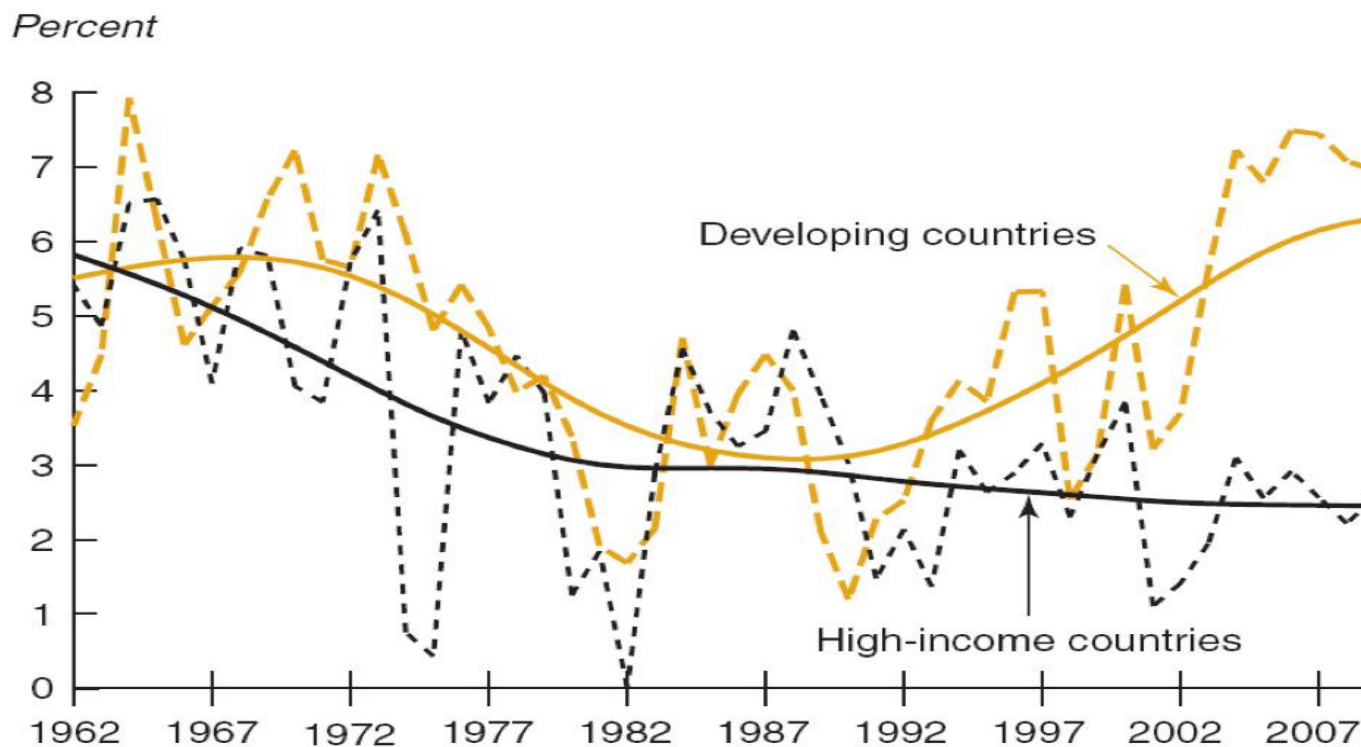
Source: World Bank, *Global Development Finance 2008*

Figure 3: Remittances to developing countries, 2000-2007



Source: World Bank, *Global Development Finance 2008*

Figure 4: GDP growth in developed and developing countries, 1962-2007



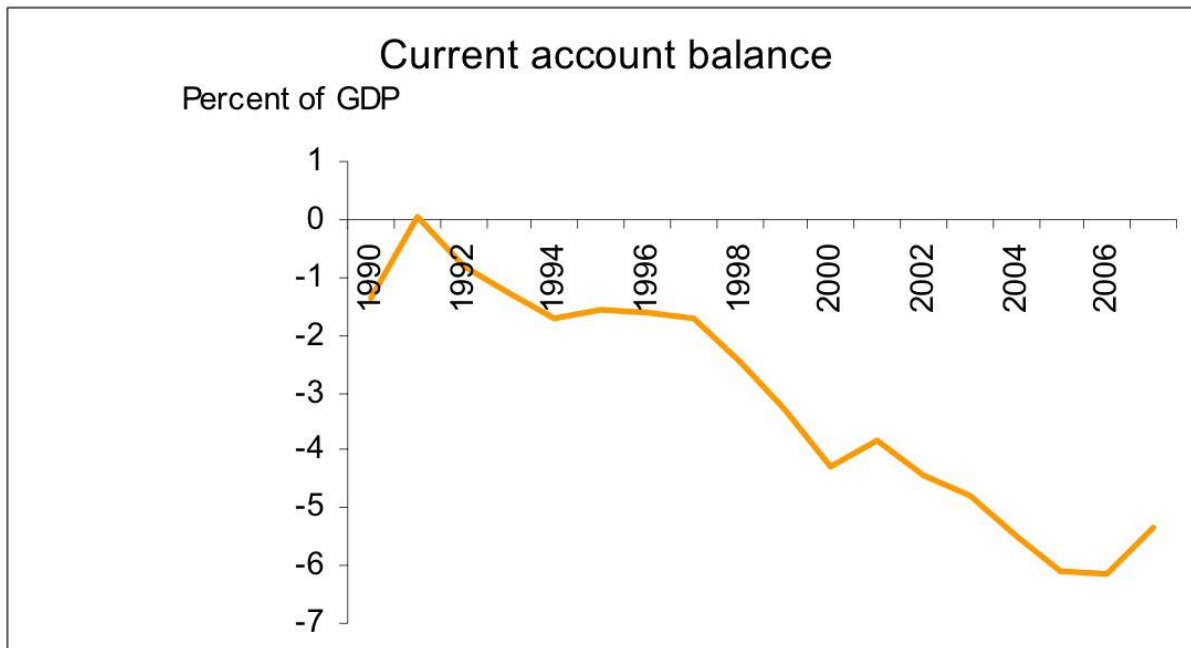
Source: World Bank, *Global Development Finance 2008*

Note: Solid lines show smoothed trend

Why dynamism collapsed in developed countries, and effects on emerging markets

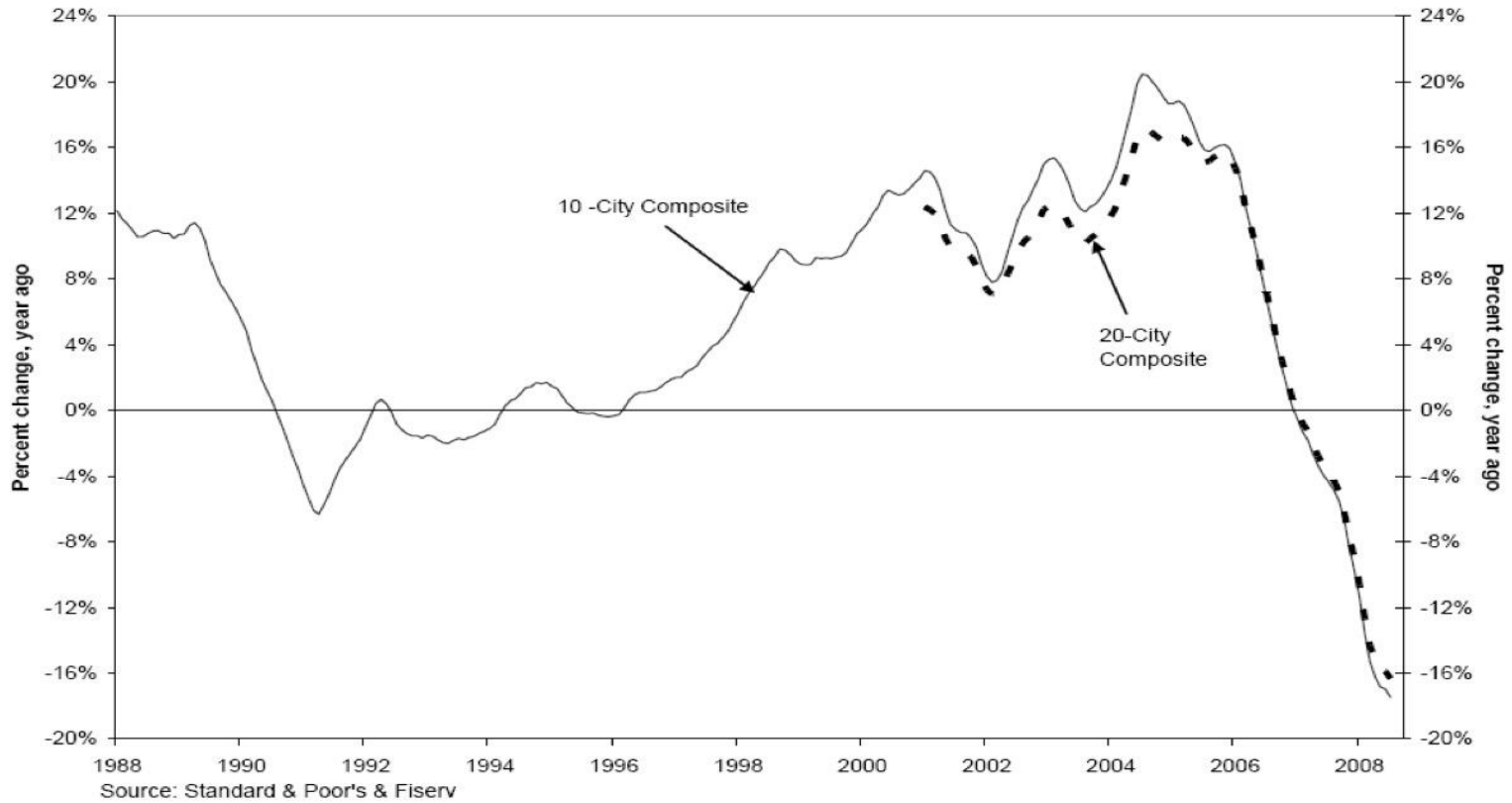
- The collapse in the US and other advanced economies
 - Burst of housing bubbles
 - Sub-prime crisis
 - High inflation
 - Fall in consumption and increasing in saving
- Effects on developing countries
 - Negative shocks on investment
 - CA deficits
 - GDP growth declined
- Global recession

Figure 5: US current account deficit, 1990-2007



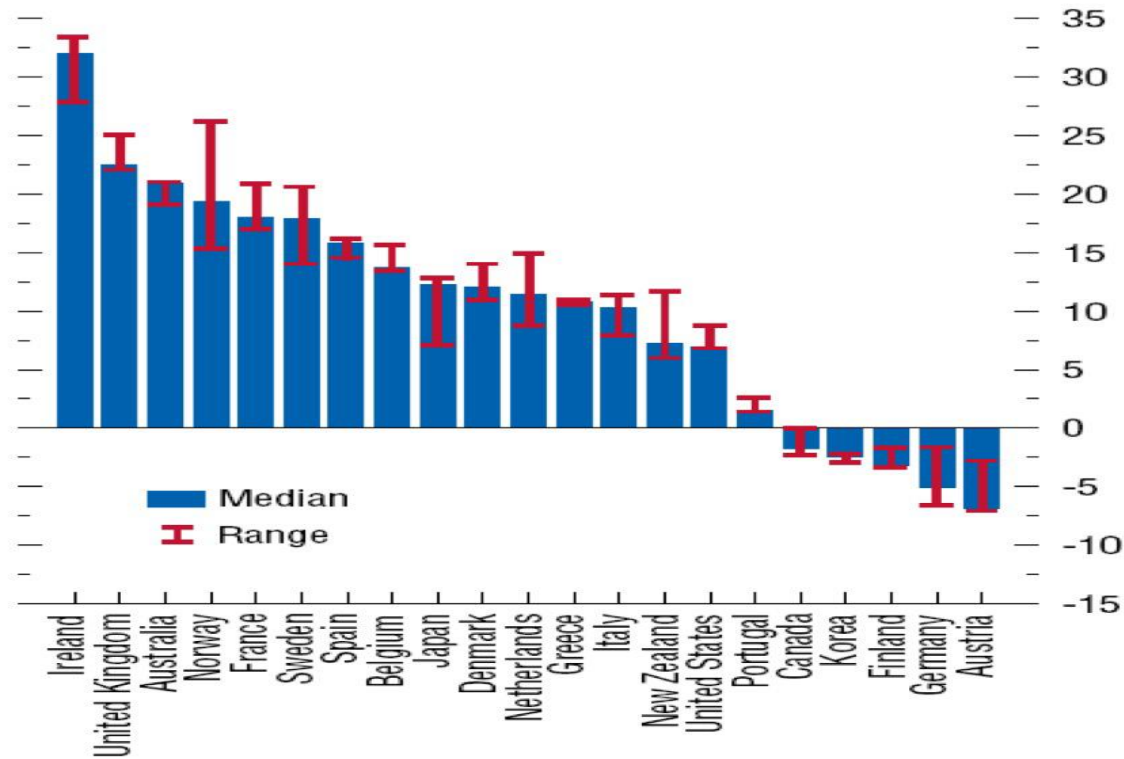
Source: World Bank, World Development Indicators

Figure 6: Changes in US housing prices by the S&P/Case-Shiller Indices, 1988-2008



Note: Data from standardandpoors.com as of September 30, 2008

Figure 7: Housing price gaps in 21 countries as of end-2007 (in percent)



Source: IMF, *World Economic Outlook 2008*, based on IMF staff calculations

Note: Figure shows an estimate of the percentage increase in house prices between 1997 and the end of 2007 that is not accounted for by fundamentals in their model