Overseas Development Institute

Workshop on the

Global Financial Crisis and Developing Countries,

11 February 2009, Overseas Development Institute, London

Introduction to the event

Simon Maxwell, Director, ODI

The global financial crisis poses the biggest risk since the 1930s to the world economy. The first narrative, takes a minimalist view of it. The Chinese are positive that their fiscal stimulus will work; the general narrative posits that the impact on developing countries should be limited so long as aid levels are kept up.

The second narrative being put forward by ODI posits that a tidal wave is coming. Although the major drivers of the crisis are based in the North, the impact in the South will be through transmissions such as trade, FDI and portfolio investment, and remittances. The UK Prime Minister Gordon Brown has predicted a fall in FDI flows to developing countries of 80% during the course of 2009, along with potential falls in remittances. The IMF predicts negative growth in developed countries. Although growth in developing countries will still be positive, it may hardly keep up with population growth.

There is a need to maintain aid flows not only to meet the MDGs but also to buffer developing countries and reduce the impact of the Global Financial Crisis (GFC) and shocks. ODI is identifying vulnerable countries; these include countries without large internal markets; those that are heavily dependent on exports to the North; those that have weak banking systems etc. In short, those countries that might face serious problems as a result of reduced trade, FDI and remittance flows.

In terms of the response to the GFC for developing countries, the UK government still considers the conclusion of the Doha round as important. But others have questioned – how important? There may be a need for new forms of aid flows; these might include new models and financial mechanisms, such as trust funds.

The third narrative posits that developing countries are not part of the problem but are instead part of the solution. The best response to the GFC is to invest in developing countries so as to create a stimulus in global demand. This argument resonates with the debate held in the early 1980's as a result of the oil price shock, stimulated in part by the Brandt report (1981, 1983). At that time people were worried about the price of food; fuels; in addition to the stability of banks. The Brandt report is all about interdependence. One of its key messages was that investing in developing countries could have the same effect of re-inflation in Germany. This argument is similar to calls for between 0.7-0.8 percent of fiscal stimuli to be spent in developing countries now.

However, in order for this argument to be credible – we need to start the dialogue with developing countries; this is the reason for this workshop. The researchers gathered here today represent the experience of developing countries to date. We need to discriminate between the narratives and transmission mechanisms. There is an urgent need to get policy messages out. The G20 communiqué for the 2nd April 2009 meeting is being written as we speak; conversations are on-going between the Treasury and DfID. By the summer there will be a new international architecture - this presents us with a window of opportunity. The country-case studies are expected to draw policy implications and recommendations that we can then put forward to the UK government and others at the G20 meeting.

Alan Winters (AW), Chief Economist, UK Department for International Development

In terms of the response to the GFC there is no 'one size fits all'. Responses are expected to be very country specific. It is clear that the Tsunami is about to come. But at the beginning there were no reports of additional funds being requested from partner countries. There is generally a lack of information as to what is happening on the ground. There is a need for speed in each of the country case-studies: we need to produce answers very quickly. We need to understand both the channels and what is happening now. Which sectors are hurting now? And which ones are likely to hurt? What evidence and recommendations will you put forward to your government and the donor community in order for them to act?

DfID can make general recommendations, but these will need fine-tuning. We need country-specific information in order to devise appropriate responses. There is a lot of discussion about international institutions. But most development is achieved by developing country themselves; responses will need to be local. This is the contribution that the study will make. It will be a unique document. Although the G20 meeting will be held on April 2nd the GFC won't be over by then; there will be a further need for decision making in response to it. The study results are expected to make a major contribution to policy formulation.

Rianne Heijboer (RH), Policy Officer, Dutch Ministry of Foreign Affairs (DGIS)

This study makes an important start to the work that is inevitably ahead. It is very pleasing to see representatives from most of the country case studies present. Currently, there are not a lot of reports from the field about the effects of the GFC in developing countries. Some embassies are reporting about the effects of the crisis, but others are not seeing a lot happening right now. The financial sector is a key area of interest for the Dutch Ministry of Foreign Affairs, we therefore need information on the effects of the crisis. There is a scarcity of country level studies. They do not exist at the moment but are of great importance in our bilateral relations. A much heard argument is that ODA should be a stable capital flow to developing countries. But which countries are hardest hit and what actions are required to mitigate the effects of the crisis?

We are pleased that ODI has drawn our attention to this project and we are pleased to contribute. Thanks also to DfID for their support. The strength of this project is that it will look into the specific effects of the financial crisis within countries. The degree of country openness will determine the potential impact of the crisis and the potential for damage. We are interested in all country case studies (eight out of ten of the country case-studies are in our partner countries); particularly as to what policy response might be necessary.

Dirk Willem te Velde (DW), Project Team Leader and Programme Leader of Growth and Investment, ODI

Thanks to all researchers for your attendance within very short notice. There are three aims of the project, as follows.

1. To monitor the effects of GFC and to feed into G20 process.
2. To feed into country level reports and the growth and development debate. A synthesis of all country case-studies will be prepared by the end of March.
3. To provide an opportunity for research institutes across the world to network.

World economic growth forecasts have been revised dramatically recently and are likely to be dire in 2009. The GFC represents an enormous shock to the world economy. The research methodology for each of the country case studies will consist of the following three building blocks, which will identify:

1. what is the shock?;
2. what is the effect on growth and development?; and
3. what are the policy responses?

In terms of the first building block, in identifying the shock at the national level the following transmission mechanisms have been selected: Capital Flows, Trade, Remittances, and Aid; these are detailed below.

1. **Private Capital Flows**
2. **Trade**: for Asian countries it may be that as opposed to capital and finance, the primary transmission mechanism may be trade. Recent data are quite horrendous with some countries experiencing drops of 20% in exports, year on year. Other countries may have more of a time-lag before a decline is felt.
3. **Remittances**: some country's will be more affected than others but falls in employment in developed countries are likely to also affect migrant workers.
4. **Aid**: How are donors reacting? Are they scaling up or down their plans? In some countries it may be the case that donors are planning the early disbursement of funds, such as regional development banks.

In terms of the second building block - the effects on growth and development - it may be the case that some country case-studies may use existing CGE model. Others may prefer to undertake causal chain analysis; use may be made of forecasts and estimated output loss. Although there have been major revisions in forecasts – these will vary by country.

Researchers will need to look at changes in investment and consider changes in employment and poverty. In China and Cambodia, due to the closure of factories it may be the case that there are increased urban to rural migration flows. If tourist arrivals decline – how might employment in the industry be affected? Researchers at all times will need to distinguish between the *actual* and *possible* effects of the GFC: what is happening now and what is likely to happen?

In terms of the third policy block and policy responses, actions taken by national governments might include economic policy measures, such as: fiscal stimulus; changes in reserve requirements; easing of monetary policy. Social policies might include: direct cash transfers or other subsidies. It might also be the case that investment climate reforms are sped up (the low hanging-fruit argument). But in all cases, researchers will need to distinguish between the potential and actual policy responses. What is the capacity available to respond? What would be the optimum way to respond?

It is worth bearing in mind that in the 1930s, although growth dramatically reduced, it subsequently rapidly increased. As opposed to countries resorting to protectionist measures instead crises often present opportunities.

We are working to very tight deadlines with the research project. A first draft of the report will be required by 15 March 2009. It is crucial that we stick to this deadline. The country case studies are expected to feed into the G20 process and meeting of 2nd April 2009. But there are also other policy processes that the report may feed into. The first objective of the report is to do with monitoring - it represents the start of thinking about how the can country deal with the crisis; how can it respond and best deal with the crisis?

Questions

Dr BP: In terms of the conceptual framework it is important to look at how the transmission mechanisms fit together. For some countries it is not the GFC that is the shock but the fall in commodity prices. This will result in a decline in public expenditures.

The optimal response is elusive: what is the yardstick? It critically depends on the trajectory of the crisis: will it be L-Shaped or U-Shaped? Also, how do we evaluate the optimality of the policy response? It is budget maximisation or protection of poor people? How do we judge it?

DW: The methodology is broad; it looks at a number of transmission mechanisms. It doesn't specify the details or how to identify the shock and attribute effects to it. It is important that the research methodology allows freedom for individual researchers; the methodological framework has been designed so as not to limit research – but merely to structure thoughts and make it helpful to synthesise all reports. If there is an important aspect that you feel is not included in the methodological framework then by all means include it.

AW: The policy response will depend on the effect of the down-turn, which won't be clear by March. But if in terms of our projections we think the crisis may result in an L-Shaped depression we ought to do X or Y. Clarity and explicitness is required. However, this will not be the definitive work of the 2009 - all will be living documents ready to be updated over the year.

Dr OOF: If the recession turns to depression: what is the policy response? The answer depends not only on developing country responses but also developed. We could declare a scenario, such as - if growth is depressed especially in 2009 and things get better in 2010 how will your country adapt.

DW: We need to distinguish between what is actually happening and what might happen? What have the policy responses already been? Further to this the research teams could specify some scenarios.

Research Teams Country Case Study Presentations

Session 1: Asian Countries

Professor Mustafizur Rahman (Prof MR), Executive Director, Centre for Policy Dialogue, Bangladesh

It is likely that the trade transmission mechanism will be very important for Bangladesh. The presentation covered two areas:

1. The exposure of the Bangladesh economy to the GFC
2. Its current impact and potential transmission mechanisms

Exports constitute 18% of GDP and remittances around 25.8% GNI 25.8%. Bangladesh's degree of openness (X+M as a % of GDP) was around 43% in 2008. 85% exports are destined for developed country markets.

Export growth in the first six months of FY2008-9 (July-December 2008) was robust at 19.6% (yoy). But if we look at the second quarter of FY2008-9 exports were down -2%. This is the first time that negative export growth has been recorded in recent years. Garment exporters are reporting that their cut and make (C&M) charges are being lowered; some orders being deferred; and discounts being requested from buyers.

In terms of remittances, the level is currently stable (there are 6.2million people working abroad at present). However, the number of workers leaving Bangladesh to find work elsewhere fell by 45% in January 2009 (yoy).

Traditionally FDI flows are relatively low. But there has been a net outflow of portfolio investment. However, portfolio investment comprises a very small part of the stock market (2.5% of market capitalisation). There has been no change in ODA yet; the World Bank has agreed to maintain levels. Instead, the challenge is the utilisation capacity of the country.

Falling commodity prices have helped Bangladesh. The government budget has improved because of reduced subsidies because of price declines – this has given the government budget some cushion. But import duties - 40% of domestic resource utilisation – have been falling. Previously 30% duties were levied on fuel that cost \$150; this cost has now fallen to around \$40; as a result the duties levied and therefore government revenue has declined.

Bangladesh may suffer an adverse impact of the stimulus packages offered by competing countries such as India and China. India has already put in place a stimulus package; China has also implemented targeted measures for the garment sector (these include a technology upgrading fund and buy-back scheme). Bangladesh has not yet put in place measures. The currencies of Pakistan and India have recently depreciated. But Bangladesh's currency so far has held. This has had a reduced competiveness effect. At present the government's growth projections are more optimistic than other multilateral institutions (6.5-6.3% compared to 5.6% from the IMF; and between 5.4-4.8% projected by the World Bank).

In terms of policy response, the government of Bangladesh has taken steps to safeguard reserves. But as yet no stimulus package or support programmes has been initiated. However, exporters and backward linkage industries (spinners) are calling for action (cash compensation, devaluation etc.). Apparel exports have so far held up although other exports have experienced a decline.

Some banks are reporting difficulties about importers paying; others are having difficulty selling at higher prices. In relation to trade policy, things are moving slowly at the WTO. The US Trade Act and proposed duty free quota free access for less developed developing countries may be further delayed as a result of the crisis; this may further negatively impact Bangladeshi exporters.

Hossein Jalilian (HJ), Director of Research, Cambodia Development Policy Research Institute (CDRI), Cambodia

The Cambodia Economic Forum (CEF) was held in Phnom Penh last week. There lots of people discussing the impact of the crisis and relatively good amounts of data on the actual and potential impact on Cambodia. Exports are the key challenge: garments comprise around 90% of total exports from Cambodia; there is a high dependence on a limited number of products which are likely to be severely affected by the GFC and slowdown in demand in developed country markets.

Around 80% of garment exports are destined for the US; 20% EU. There are different viewpoints on the potential impact of the GFC. Some posit that garment exports might decline. But others posit that there could be increased substitution for lower priced products (such as Cambodian products). However, in recent months there has been a slowdown in garment exports.

Although the tourism industry has expanded year on year (around 2million tourists visit Cambodia each year), there is likely to be a 10% reduction in arrivals in 2009. Most tourists arrive via Thailand. It is difficult to distinguish between the effects of the Thai political crisis and the impact of the financial crisis in terms of reduced tourist arrivals.

Around 300,000 migrants work in Thailand, many illegally. Because of the GFC, the Thai authorities have banned illegal migrants (who are mostly from Cambodia). CDRI is running monthly vulnerable worker surveys in Phnom Penh and other areas to better determine the impacts of the crisis on labourers.

Due to recent prices rises for cassava and rubber there has been a lot of cultivation and production. But as a result of recent declines, many farmers are now left with products they cannot sell. The recent decline in prices of some products has negatively affected farmer welfare.

Most FDI is destined for the garment and construction industry. However, there has recently been factory closures and reduced investment, including some flight of investors. Most investment in construction comes from Korea. Most investment in the mining sector comes from the Chinese mainland. However, for both the mining and agricultural sectors information on investment (and investors) is scare and difficult to come by.

Cambodia has been a high growth performer recently. But the impact of growth on poverty reduction has not been fast (1% reduction in poverty p.a.). The poverty elasticity of growth in Cambodia is around less than half of the minimum average of other recent high growth performers; this is because of the sectoral composition of growth. Agriculture has not been a high growth sector – it produces well below its export potential. The impact of the GFC is likely to be through reduced employment and remittance flows, as opposed to agriculture –poverty is not likely to be much affected (because of the weak poverty elasticity of growth).

The government has a relatively strong grip on fiscal and monetary policy tools. It has also recently emphasised the need to invest in agriculture: lack of finance is a serous constraint to this sector. Around $1billion of donor support has been pledged for 2009. In Cambodia, it is difficult to disentangle the effects of the food, fuel and political crisis in Thailand on the economy.

Ira Setiati Titheruw (IST), Centre for Strategic and International Studies, Indonesia (CSIS)

The debate about decoupling surfaced one year ago. But it is true to say that now nobody is under an illusion that they will be untouched from this financial crisis; the worst is yet to come. The most recent data available for Indonesia is for the third quarter of 2008; this is better than expected.

Private and public consumption expenditure accounted for around 65% of GDP in Indonesia. Between 2008Q2 and 2008Q3 there was a high growth in consumption expenditure; this may reflect religious celebrations or government spending (most budgetary disbursements occur towards the end of the year). An increase in government expenditure in the last quarters of 2008 is not as a response to the crisis – but business as usual. In December and January deflation was reported, this is unusual as it is more common to have inflationary pressures towards the end of the year.

Fourth quarter growth data are available across sectors. Domestic orientated industries are reporting strong growth still. But for manufacturing industries growth has slowed. Commodity prices started to fall from June 2008 onwards; exports have been hard hit since Nov 2008. Up to the end of 2008 the trade balance recorded a surplus. But this overlooks that the non-oil and gas trade balance has worsened and experienced a larger export decline compared to imports.

Remittances remain relatively unchanged. A slight increase in net remittances is reported in 2008Q3 compared to 2008Q3. The Indonesian rupiah has been depreciating since 2007; in fact it is at a level vis-à-vis the US$ last seen during the last financial crisis. The Indonesian stock exchange dropped 51.17% during 2008; the equity market capitalisation was down 46.4% during 2008. Net foreign equity purchases have always been volatile, so it is not possible at this stage to decipher any impact from the GFC. Foreign ownership of government securities has declined since Sept 2008. Although capital and financial accounts show a surplus, it is lower in 2008 than in 2007.

The Indonesian banking sector has no direct exposure to toxic assets. Lessons from the last financial crisis meant strict regulations have been put in place. Banks are not allowed to take any investments in unrelated assets such as property; there is no direct ownership of sub-prime mortgages in Indonesia.

The current GFC is expected not to be as severe as the previous Asian financial crisis. For example, the rice harvest has been good for 2008. The previous financial crisis occurred at the same time as a poor harvest and El Nino effect. Consumption expenditure is also expected to remain high in 2009 due to it being an election year.

Government policy has consisted mostly of measures to maintain financial market stability. In an effort to increase liquidity reserve requirement ratios were lowered from 9.08% to 7.5% to provide more liquidity in the banking sector; FOREX swaps have been lengthened. The Ministry of Trade is acting to reduce illegal imports; the Bank of Indonesia is providing export finance facilities and reducing interest rates. In terms of fiscal stimulus, the government is providing direct and indirect subsidies through the provision of free health and education facilities for low-income households. The government's budget deficit is healthy and remains low. But the unspent budget surplus is now expected to be used for responding to the GFC.

Questions and Answers

Q: How is the Indian stimulus affecting Bangladesh?

Prof MR: It has provided a technology upgrading package which consists of subsidised credit to backward linkage industries (yarn producers). The devaluation of the rupee also means that Indian yarn costs around 60 cents less than Bangladesh. Manufacturers are now purchasing from India; backward linkage industries that produce yarn are now having problem selling their products and paying back banks. In terms of the demands of Bangladeshi spinners they are as follows: 1. Ban import of Indian yarn; 2. Cash compensation (moratorium on payment of credit for two years); and 3. Devaluation.

Q: How are the respective governments' debt positions?

HJ: The government (Cambodia) is in a relatively good position in terms of its deficit – it looks healthy and has improved. But official statistics overlook the fact that there is a lot of foreign debt. The government is borrowing at concessional rates – but putting in into commercial banks to get the premium difference. Official statistics do not reflect this.

Dr DP: Government deficit in Bangladesh is mostly related to the recent commodity price boom and cost of subsidies. It is not high but is around 5.4% GDP (according to the IMF a level of 3% is considered safer). The government's budget deficit may fall in Bangladesh due to falls in commodity prices. But if fiscal measures and stimulus are undertaken, the composition of the deficit will change.

Q: Is trade finance a problem for exporters?

PM/DP: It is not an issue in Bangladesh: banks still have liquidity. However, liquidity within the system may be sucked up by the government if fiscal measures are undertaken. The major challenge for the government is macroeconomic management of both the internal and external balance. Gross national savings are high, similarly investment. The challenge is posed by the high interest rates in Bangladesh (there has recently been an increase).

IST: Trade finance has not been reported as a problem in Indonesia; the government undertakes some provision of trade finance as part of its management of foreign capital flows and exchange. For example, state oil companies must purchase foreign exchange from domestic banks. These measures have been devised so as to limit the volatility of foreign exchange markets.

Q: What is the role of social safety nets within the country?

HJ: In Cambodia there are hardly any official social safety nets. But NGOs and Donors are raising the issue.

DP/MR: Social safety nets in Bangladesh include food and employment guarantees.

IS: Efforts to maintain levels of social protection and poverty reduction in Indonesia include cash transfers and the provision of free education and healthcare. The government has set aside 20% of its budget in 2009 for education expenditure on education; this is double the level in 2008 and is expected to provide some degree of fiscal stimulus.

Comments

KB: Interesting and robust presentations but backwards and forward linkages need to be strongly articulated in these studies. We need to identify micro and macro linkages. We need a clear understanding of the structure of the economy and structure of society etc. This will assist in ensuring that social protection is not considered as an add-on.

DW: Linkages issues: ODI is available to provide support and clarification.

NR: By definition a fiscal stimulus must be countercyclical. It is not about policies for social support, but policies the government is willing to do to increase expenditure – knowing that GDP will decline.

Dr DP: The resources and time available for the studies are limited. But the attribution issue needs to be made clear. Attributing macro performance is a challenge. If we can get an idea of this in the 30 days, then more in-depth analysis of the social impacts may be the second phase; this may entail analysis of specific sectors and employment structures and how they might change etc.

Session Two: sub-Saharan Africa countries (Commodity Exporters)

Dr Oluwatayo Oni Fakiyesi (OFF), Head of Economics Department, University of Lagos, Nigeria

Data constraints in Nigeria are in part due to the federal nature of government. More than 50% of total government revenue is earmarked for lower chairs; this means it is more difficult to track government revenue.

1. **Capital inflows**: The first impact of the crisis was felt by Nigeria's financial markets. Market capitalisation fell by some 45% in 2008 compared to 2007.

Capital market (share index and market cap) peaked in March 2008. Credit crunch felt by banks loaning to investors. There has been a dramatic reduction in the all share index.

In terms of policy, the initial response of the government was to state that Nigeria would be insulated. However, dramatic capital outflows have eroded confidence. A reduction in liquidity has constrained firms' ability to raise funds. The government has increased interest rates. In addition, bad banking debt is hidden; borrowers are unable to pay back loans.

Foreign reserves have declined from N64billion in 2008 to N56 billion at present. There has been a reduction in expenditure on capital projects. Some foreign commitments have been scaled back or withdrawn.

2. **Trade (oil)**: Crude oil comprises around 85% exports and 90% of government revenue. The price of oil has fallen from a high of $147 per barrel in July 2008 to $47 per barrel in January 2009.

3. **Remittances and ODA**: No impact on remittances has been observed yet; similarly ODA flows.

4. **Growth, poverty and the response of the government**: Donor agencies are very active in the promotion of MDGs and provision of health and education in Nigeria. However, most expect prior donor commitments to be revised in 2009.

The financial sector in Nigeria is integrated. The most pressing policy questions are: how can the government maintain stability? How can it minimise the risks of financial contagion? What banking sector regulations need to be put in place? What might be appropriate policy responses: diversification into other non-oil sectors? What if recession turns into depression? Most investors are multinational enterprises; how might oil companies react?

Professor Manenga Ndulo (Prof MN), Department of Economics, University of Zambia

Preliminary work to establish baseline data includes analysis of transmission mechanisms 2000-2008. Before discussing impacts it is considered important to firstly understand the transmission mechanisms: Capital flows; Trade; ODA; and Remittances. It is also important to understand where Zambia has come from. Pre-1995 Zambia experienced negative growth, had a low standard of living and was a controlled economy. Market reforms have provided for the recent growth performance of Uganda. Poverty levels have been reduced from. The global financial crisis threatens these gains. Zambia has achieved growth and control of inflation; savings and investment have increased. But projected growth for 2009 has been reduced from 5.8% to 5%.

In terms of capital flows, most FDI is targeted at the mining and financial sector. The top investors are: Australia, Switzerland, Canada, South Africa, India and China. The major investors do not originate from the most crisis affected countries: UK or US. However, most portfolio investment originates from the UK and Kenya. Australia and South Africa are equity investors

Trade data show that in the final period of 2008, the trade balance worsened (imports were more than exports). Changes in the terms of trade index for Zambia suggest that the impact may yet be coming. The Stock market index fell by 29% in 2008. Although single digit inflation has been achieved in recent years, it has now returned to double digit figures.

Mining products account for around 80% of Zambia's exports. The Kwacha has depreciated against the US$. The copper price (US$/pound) fell in 2008, from just over US$3/pound to just over $US2/pound by December 2008 (although it is expected to return to $3/pound in 2009).

Copper mines are already closing. Around 32,611 workers have lost their jobs - 15% of the total workforce of the copper industry. New projects have been put on hold; exploration projects have been affected due to difficulty in obtaining bank loans for financing.

Remittance data do not yet show a decline, but monthly flows will be investigated. ODA accounts for around 30-40% of the Zambia's government budget and is mostly spent on health and education. At present no change is expected in ODA.

In terms of policy, the government is adopting prudent fiscal policies. However, infrastructure development is planned for the agricultural sector. A tight monetary policy is being used to target inflation; in addition, the government is negotiating with mining companies for a potential suspension of windfall tax.

Sarah Ssewanyana (SS), Executive Director/Principal Research Fellow, Economic Policy Research Centre (EPRC), Uganda

The results of the study are expected to feed into Uganda's National Development Plan. Although services and construction are important, Uganda is a predominantly agricultural economy. Around 35% of the government's budget is supported by ODA which is spent mostly on education and health. Poverty has been reduced from around 56% in 1992 to 31% in 2002, although inequality has increased. The MDGs are expected to be met in Uganda by 2015 so long as 'everything remains as it is'.

Monthly trade data show a decline in value since September 2008 into 2009. Uganda's key export is coffee. At the beginning of 2008 the value of exports were high ($/kg) but fell towards the end of 2008; although Uganda's export pattern across the years, 2005, 2006, and 2007 remained broadly similar.

Uganda's exchange rate is pegged to the US$ and has depreciated by 20% since October 2008. Government tax revenue has recently declined. Inflation had previously fallen but since May 2008 has increased and is around 14% at present - much of it is imported. There has been a slowdown in remittances during 2008.

Aid disbursements have declined between 2007 and 2008 (yoy), although development partners have pledged that levels will not decline. There have been anecdotal reports of Barclays bank Uganda closing, but these have yet to be substantiated. There are some reports of NGO activities in Northern Uganda falling and operations closing.

Uganda's growth projections have fallen. The IMF predicts growth will be around 6-7% in 2009 from 8.9% in 2008. The ADB predicts 5.6% in 2009, but the basis of such projections is less clear.

In response to the financial crisis, no concrete measures have been announced by the government on either monetary or fiscal policy. The government is likely to continue with its tight monetary policy, it wants inflation below 10%. One reason for the delay in the government's response to the GFC is the formulation of Uganda's National Development Plan: as they are currently in the process of formulating the plan, they may be able to include potential scenarios/responses to the GFC within it.

Although exports in general have experienced a decline, demand for food products in Kenya and Sudan remains strong. That is, export demand within the region is strong. However, much of the demand from Sudan is a result of donor activities and expenditures. If donor activities decline in Sudan, demand for food products from Uganda might decline.

Questions and Comments

AMc: In terms of evaluating the social impact of the macro data may be easier to obtain than micro. But an exception to this may be labour market statistics such as employment and wages. Such data may provide the link from the macro to the micro. It may also provide more insight as to how countries may adjust to the GFC.

PM: The attribution problem is now coming through very clearly. How do you distinguish between the impact of falling commodity prices on countries such as Bangladesh (net-food importers) as opposed to the GFC and falling demand?

AW: The financial crisis is around one year old; it didn't start when Lehman Brothers collapsed. In the UK the start can be traced back to the Northern Rock bank run. If it possible, countries should try with attribution.

JK: The distinction between the commodity price shocks and financial markets is not so clear. It is important to consider how products are traded. Often commodities are traded with links to financial markets through the use of instruments such as hedges and futures etc.

Q: The Nigerian country case study is most likely to have the most developed financial system. But what was the role of lending to real estate? This was not clear in the presentation.

Nigeria: The capital market in Nigeria has recently grown fast. This includes both FDI and portfolio investment. Due to outflows of capital since the GFC, there have been reported difficulties in paying back loans. Some debts have become bad; the government has had to step-in and rescue some banks.

KB: Most of the case studies are following fiscal prudence and tight monetary policy advice. But the US and EU are obviously not following this advice; this includes inflation targeting. Why have governments chose to follow fiscal prudence and tight monetary polices?

Q: What are the governments' narratives on their policy? What is their priority?

SS: In Uganda fiscal and monetary policies are very much driven by the IMF. Government expenditure is very high; they have been advised to reduce expenditures and tax revenues are expected to decline. Some NGOs are already closing down, such as the Northern Ugandan Social Action Fund (NUSAF).

PM: Policy in Zambia is very much influenced both by the WB and IMF. But you have to also remember where Zambia is coming from. Due to high level of inflation in the 1990s the government is willing to do whatever it takes to control inflation. In comparison, the financial sector in Zambia is overregulated. The government is not willing to reduce regulation. In terms of budget cuts there are areas within which the government has scope to do so.

HJ: Cambodia: In Cambodia, the IMF's office is located within the National Bank (the same in Uganda). The IMF has been pushing for the government to spend more – they have been advocating the government to take a more interventionist approach, increase public good expenditure etc.

Session 3: Bolivia, Benin and Kenya

Dr Luis Carlos Jemio (Dr LCJ), Director of Group Integral S.R.L. INESAD, Bolivia

The Bolivian economy has benefited in recent years from an extremely favourable external environment. Favourable conditions have been driven by:

1. Export prices; and
2. Remittances.

The mining sector is the first that has started to feel the impact of the financial crisis. Since December 2007 to June 2008 there has been a decline in exports. Remittances grew dramatically in 2007 but almost halved in 2008. The government is still awaiting monthly remittance data for 2009.

Due to previously strong growth the Bolivian economy is better equipped to take counter-cyclical measures. The government has at its disposal foreign exchange reserves which will provide it with some cushion. The fiscal balance and surplus are expected to be at around 5-6% GDP. But the government budget is highly dependent on hydrocarbon revenues.

Bolivia's external debt has reduced; it has benefited from the HIPC initiative. However, the exchange rate has appreciated recently. But this is mostly as a result of measures taken by other trading partners (that have devalued) and real exchange appreciation that is affecting Bolivian competitiveness. The import to GDP ratio has increased recently.

Monetary policy has been aimed at stabilising the excess of liquidity. The amount of currency in circulation has experienced a three-fold increase. If the central bank had not sterilised these monetary flows the currency appreciation could have been even higher in recent years.

The gross domestic saving rate stood at 30% of GDP in 2007. However, despite the large supply of domestic savings, investment rates have remained low in terms of enabling Bolivia's growth capacity.

Tradable drivers of growth have been the mining sector. Non-tradable drivers of growth such as construction are expected to experience a recession. There is expected pressure on foreign exchange reserves in the near future. The research team will use a multi-sector CGE model to explore the impact of different scenarios on the Bolivian economy. The research may also entail the use of an RMSM macro-consistency model; this will enable the marginal analysis of external shocks and policies through a macro-consistency model. In addition, enable analysis of the different trade-offs of shocks and the exploration of the appropriate combination of policy responses.

Prof Fulbert Amoussouga Gero (Prof FAG), Universite d'Abomey-Calavi, Benin

Benin is a member of the CFA region. The region has pursued a convergence policy that includes: budgetary, fiscal and monetary policy. So Benin's response to the crisis must be considered within the context of the response of the community. Recently, private capital inflows have grown considerably; FDI accounts for half of all investment in Benin. The GFC is expected to result in a decline in investment and increased risk and vulnerability.

Benin's exports are limited to a few products with relatively low-value added. Cotton accounts for 34% of all exports. Cotton prices on the international market have fallen recently by around 37.4% yoy. Oil prices have fallen by 60.6% yoy. The US$ has appreciated by almost 30% against the Euro in the last year. This combination will most likely result in a dramatic reduction in exports (including re-exports from within the region).

Agricultural producers will be affected by falls in cotton prices. Exports are expected to slow. The global financial crisis has accentuated the food and energy price crisis; this could lead to a social crisis in Benin in the absence of economic vision.

In terms of the policy response to the crisis, the West African Monetary Union has reinforced coordination and dialogue across agencies; increased monitoring of various departments (banks, insurance, inspection, governance, regulation etc.); and enhanced surveillance/supervision etc. But the real problem for the region relates to exchange rate management. What should the policy been for the CFA region when the Euro appreciates? The CFA is pegged to the Euro, when it appreciates this is not good for investment and competitiveness in Benin.

Professor Francis Mwega (Prof FM), School of Economics, University of Nairobi, Kenya

There have been some conflicting messages about the impact of the GFC in Kenya. For example, the Prime Minister is reported as saying that the impact will be large. But the Ministry of Finance and the Central Bank have both reported that the impact with be small. Kenya is predominantly a rural agro-based economy without many direct links to the GFC. However, tourism and commercially orientated agriculture will be affected. Other effects are likely to be macroeconomic and related to the exchange rate and foreign exchange volatility.

Kenya is largely insulated from foreign finance; there are no derivatives or asset based securities. Although there is some foreign bank ownership, it is a very small % of total banking sector. However, since July 2008 the NSE-20 Index has fallen by 25%; portfolio flows have been adversely affected. Although some posit that the worst is now over, the Kenyan stock market is still going down. The decline in the stock market index has made it more difficult to borrow from the capital market; this affected the availability of funds.

There is expected to be a strong regional impact of the GFC in Kenya: Nairobi accounts for 60% of all output and GDP. The city therefore needs to be well managed.

Around 75% of international tourists are from North America and Europe (although just 6% come from the US 6%). If tourist arrivals were to fall by 50% this would result in a loss of revenue of around $316million. However, it is difficult to attribute the impact of the GFC on tourist arrivals from the effect of the post-election crisis.

The value of Kenyan tea exports has declined by 60% since September 2008. But this may also be the result of a free trade agreement between Pakistan and Sri Lanka (around 28% of Kenyan tea is destined for Pakistan; followed by Egypt and the UK).

Cut flowers are a luxury good. Total export volumes increased in 2008 compared to 2007 (93,000 tonnes in 2008 compared to 91,000 tonnes in 2007). These exports may be affected by the GFC and reduced consumer expenditure on luxury goods.

It is important to point out that most of Kenya's exports go to the COMESA region (31.4% in 2007).The EU accounts for around 25% of exports, mostly agricultural goods; the US market accounts for less than 5% of exports. Kenya's depreciating currency is currently promoting exports.

There is an expected reduction in remittances. But data for 2008 still show an increase in remittances compared to 2007 (from US$573.6million to $611.2million in 2008), although they are very volatile. Kenya is not highly dependent on aid; it accounts for around 3-4% of GDP; down from 15% of GDP in the 1990s. In fact, aid flows are not included in the Kenyan budget due to the volatility of flows.

The major effects of the crisis are expected to be macro. Government plans for a sovereign debt board have been shelved. Macro imbalances could cause the Kenyan shilling to fall dramatically: already it has depreciated by 22.6% against the US$ since September 2008.

In light of the commodity price and fuel crises of 2008, fuel prices have fallen but there are still food shortages in Kenya because of the political crisis. The government is subsiding corn meal. In 2007, Kenya achieved the highest growth rate in over two decades. But the IMF predicts growth for 2009 will be only 4%. Growth and poverty have an elasticity of around 1 in Kenya: reduced growth will impact poverty reduction efforts.

In terms of the policy responses to the crisis, the government has reduced bank cash ratio's from 6% to 5%; the Central Bank has reduced ratios from 9% to 8.5%. But is this enough to reduce interest rates in Kenya? There is policy uncertainty in Kenya because the effects of the GFC crisis are not yet clear.

Questions and comments

Q: Does the Bolivian team consider shock dynamics, which by definition CGE models do not? Is the GFC considered to be temporary or will it have dynamic implications?

Dr LCJ: The CGE model is just a tool. It is a static model that is not about dynamic variables. However, it can be used to test the likely impacts of the crisis, for example, a fall in remittances (which account for around 5% of GDP). Household survey data are collected each year in Bolivia; the model can assist with estimating the likely impact on poverty distribution and inequality.

DW: If country's can get household survey – it is useful to work through first-order effects. CGE models can provide a useful way of thinking about shocks and to work through first-order effects.

AW: Yes, for example if there is a 10% drop in exports, how might this affect employment? CGE models have their uses but in all cases, don't take them literally.

Q: How frequent are household surveys? When was the last survey undertaken? When will be the next survey? The speakers did not talk much about poverty impacts.

Prof MR: In Bangladesh, the last household expenditure survey was undertaken in 2005.

Prof FM: The likely impact on poverty is likely to be substantive due to the fall in tea prices. In terms of social safety nets, the government is subsidising maize meal for consumers. But this is bad economics; it involves selected producers and distributers. The government is ready to put in place price controls if they rise too much.

Q: How do we determine changes in ODA given that this year pledges have already been made?

AW: DfID within county offices may already have started to reallocate priority areas themselves.

AMc: Some donors may already have identified cuts. One strategy may be to identify important donors and carry out targeted interviews. They may be already discussions within country about reallocation of aid etc.

Summary and Close

Mirco Goudriaan (MG), Senior Policy Officer, Ministry of Foreign Affairs (DGIS)

Everyday there is a new story about the scale and scope of the financial crisis. This is a new step forward in trying to get knowledge about the effects of the financial crisis within specific countries.

It is part of the assignment to look at the developmental effects (plausible backward and forward linkages) of the financial crisis and poverty impacts; we should probably go a bit further in the analysis of how reduced financial flows might affect certain sectors in the real economy, and employment in the short, medium or long-term. In addition, to consider how structural reforms that might improve poverty reduction efforts in the longer-term: this might be an opportunity to do so.

It is important to get facts and figures on evidence-based information and provide detailed policy recommendations where possible: this includes structural reforms as well as different channels for financing, including ODA. There are many potential avenues in the international (financial and economic) arena that this research may feed into.

Alan Winters (AW), Chief Economist, UK Department for International Development

We are here with a unique chance to provide a really good contribution to the debate on the impact of the GFC on developing countries. There is a need maintain the speed at which the project takes place; this study has got to be manageable. You need to know clearly the path that you are expected to follow – this project cannot grow out of hand. Some presentation comments:

- It would be very useful to present price and volume trade data, as well as information on the terms of trade; how much is a price hit and how much is a quantity hit? Just get the very latest data.

- It is important to use high frequency data. In some cases only annual data might be available. But monthly and quarterly data is much more direct and compelling. If high frequency data are presented it should include year on year changes.

- In relation to employment, one should consider what to do if most employment is within the informal sector. What do you do in this situation/circumstance?

- In relation to stimulus packages, it is not only national packages – but also those of other countries that are relevant. But as part of national packages the distinction should be made between those that focus on production or producers, as well as the extent to which they are aimed at consumption. It might not make that much difference in Keynesian terms but will do in terms of the spillover effects on other countries. We are not asking for judgements, but if it is possible to provide information on trade barriers (tariffs, export subsidies etc.) this will be an area that will generate quite a lot of discussion. They are likely to have an implicit bias and be relatively covert etc.

- Each of the studies should include information on what is happening to monetary policy within country. Where it is possible to identify 'core' interest rates this should be done.

- There are consequences of tracing the shock and disaggregating into first and second order shock etc. We should remember that the really core requirement is to answer the macro questions: this is where the debate is at the present.

- If you can, detail the plausible casual chain. But remember there are around 30 days available. So budget your time carefully; macro is the core; cover micro aspects if possible, but not at the extent of reducing the coverage of macro aspects.

- Labour markets and employment: if you have access to this information – use it. But if it is not clear where this comes from or what it means, exclude it. The relevance of unemployment data in a low-income country is questionable.

- If there is an interesting story - provide this information. One example, in Uganda was the withdrawal of the Northern Uganda Social Action Fund (NUSAF).

- As opposed to trying to attribute effects to a crisis, the teams should detail the shocks that are being dealt with at the moment. We are interested in finding out what is going on now. Attribution is less important than a clear understanding of inputs and outputs.

- There will be differences between urban and rural environment. To the extent that you think the spatial dimension is important – include it. For example, in Indonesia during the last financial crisis rural areas did pretty well due to exchange rate effects benefiting agricultural producers. In Kenya the point has already been made that cities are more connected than rural areas.

- In relation to domestic politics, the whole virtue of the country case-study approach is that these aspects are internalised. It may be the case that countries face similar challenges but take different policy responses, the question then is: why? Country case studies have been selected because research teams are the experts: you tell us what is important and why certain policy has or has not been adopted within your country context etc. However, these are not essays on local political systems and activities. The aim is to understand economic policy.

- If it is more plausible to select a scenario and trajectory, do so and define it; we might also be able to define a core scenario.

Dirk Willem te Velde (DW), Project Team Leader and Programme Leader of Growth and Investment, ODI

It is very important to think about the shock variable. We are not talking just about financial flows, but a range of issues, trade, remittances, private flows, aid etc. In many cases, correct attribution is important as the shock might be more related to political events as opposed to the financial crisis. The first part of the methodology is to identify the shock and the immediate impact. The second part is to think through how this feeds through to the economy? This will include analysis of what has already happened; use of high frequency data; interviews; telephone conversations and/or visits with various associations; obtaining information on bookings and orders; we need to know what is already ongoing. The second building block requires information on the effects going through the transmissions mechanisms, broadly defined.

The third building block consists of analysis of the policy responses so far. Separate out what has happened and what might happen; what would be the most appropriate response? In terms of scenarios, there are no easy answers. Most expect 2009 to be a bad year, which might pick up in 2010. However, we are happy to discuss possible scenarios further with the research teams as necessary.