

How to define „Emerging Economies“ and how to distinguish them from „Developed Countries“?

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Agenda

- 1 Problems of definition: „Emerging Economies“ or „Emerging Markets“, „developing countries“, „developed countries“
- 2 Countries in the MSCI portfolio: features and profiles
- 3 Upper middle income countries – the next developed countries?
- 4 Benchmark Korea for middle income countries
- 5 Middle income gap/trap – few newcomers to HIC
- 6 Conclusions
- 7 A simple proposal for a new classification system of countries

1 Problems of definition

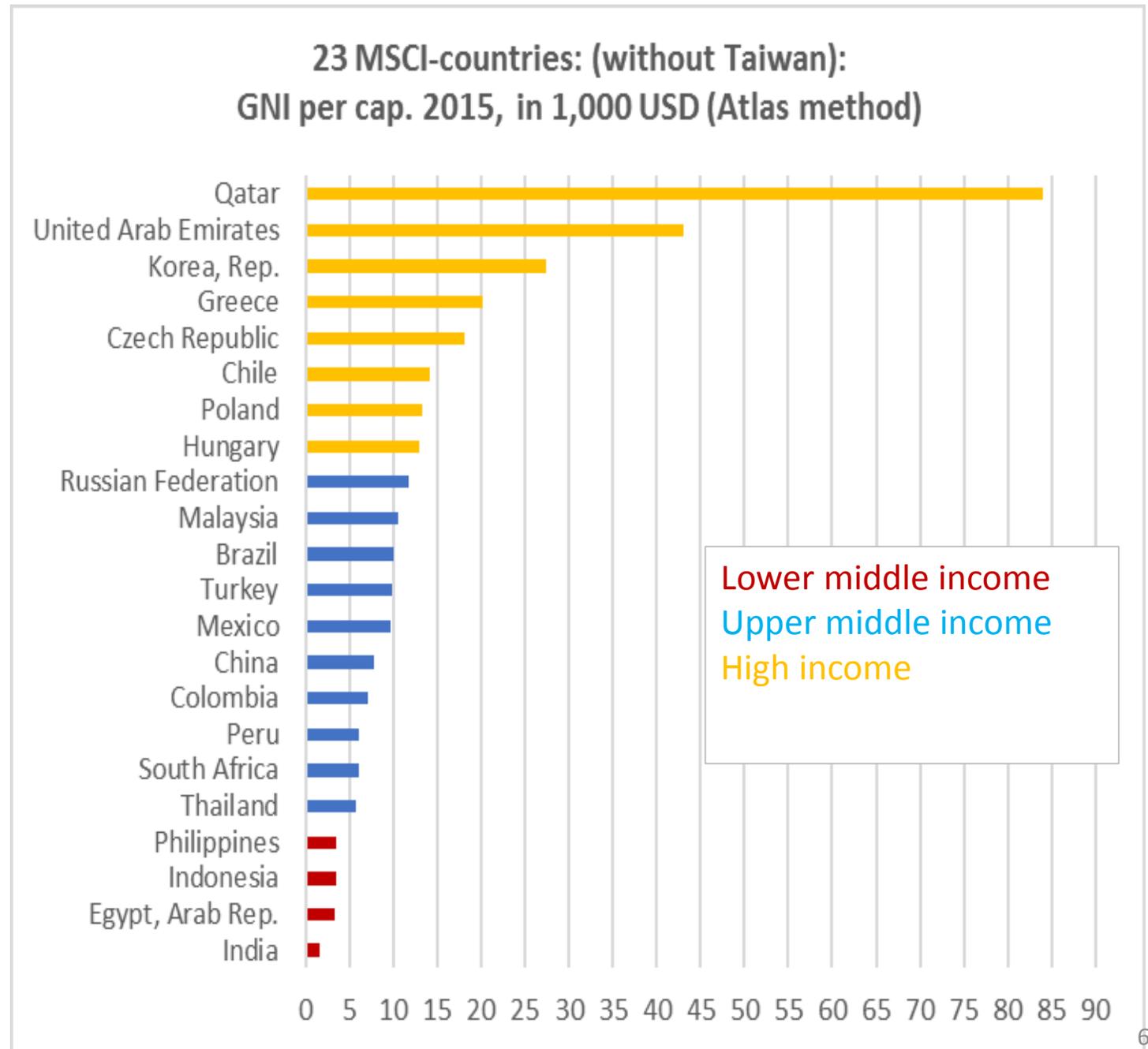
- What are „Emerging Markets“ (EM)? Definition:
- Antoine van Agtmael, formerly IFC, founder of „Emerging Markets Management“ coined „emerging markets“ in the 1981 when trying to establish “Third-World Equity Fund”:
“Racking my brain, at last I came up with a term that sounded more positive and invigorating: emerging markets. ‘Third world’ suggested stagnation; ‘emerging markets’ suggested progress, uplift and dynamism.” (quoted from “The Economist” 2008, Sept. 18)
- Hence: EM is a financial category, meaning developing countries with rising asset markets suitable for portfolio investment and FDI
- EM is not a developmental category
- Terms „emerging economies“ (EE) or „emerging countries“ are undefined
- „Schwellenländer“ or countries close to the level of „developed“ countries is also undefined
- We need to find better classifications for „developing /developed countries“

Problems of definition

- World Bank until 2016: low, lower middle, upper middle, high income countries
- HIC are „developed, beyond threshold of GNI p.c. 12,476 in current USD (Atlas method), other thresholds 1,025, and 4,035 USD
- Hence: „developed countries“ are those $> 12,476$ USD GNI p.c.
- World Bank 2016: no further use of „developing countries“. All countries are developing, all countries addressed in SDG 2015
- IMF uses “developing and emerging economies” as one group
- „Intellectual laziness“? (Bill Gates)
- Basic „development economics“ approach (Chang, Rodrik and others):
overcoming GDP gap, catching-up = convergence, improving production capacity by adopting modern technology, structural change to non-agricultural sectors, industrialisation and high value service sector
- Others: score in HDI, MDGs, or SDGs

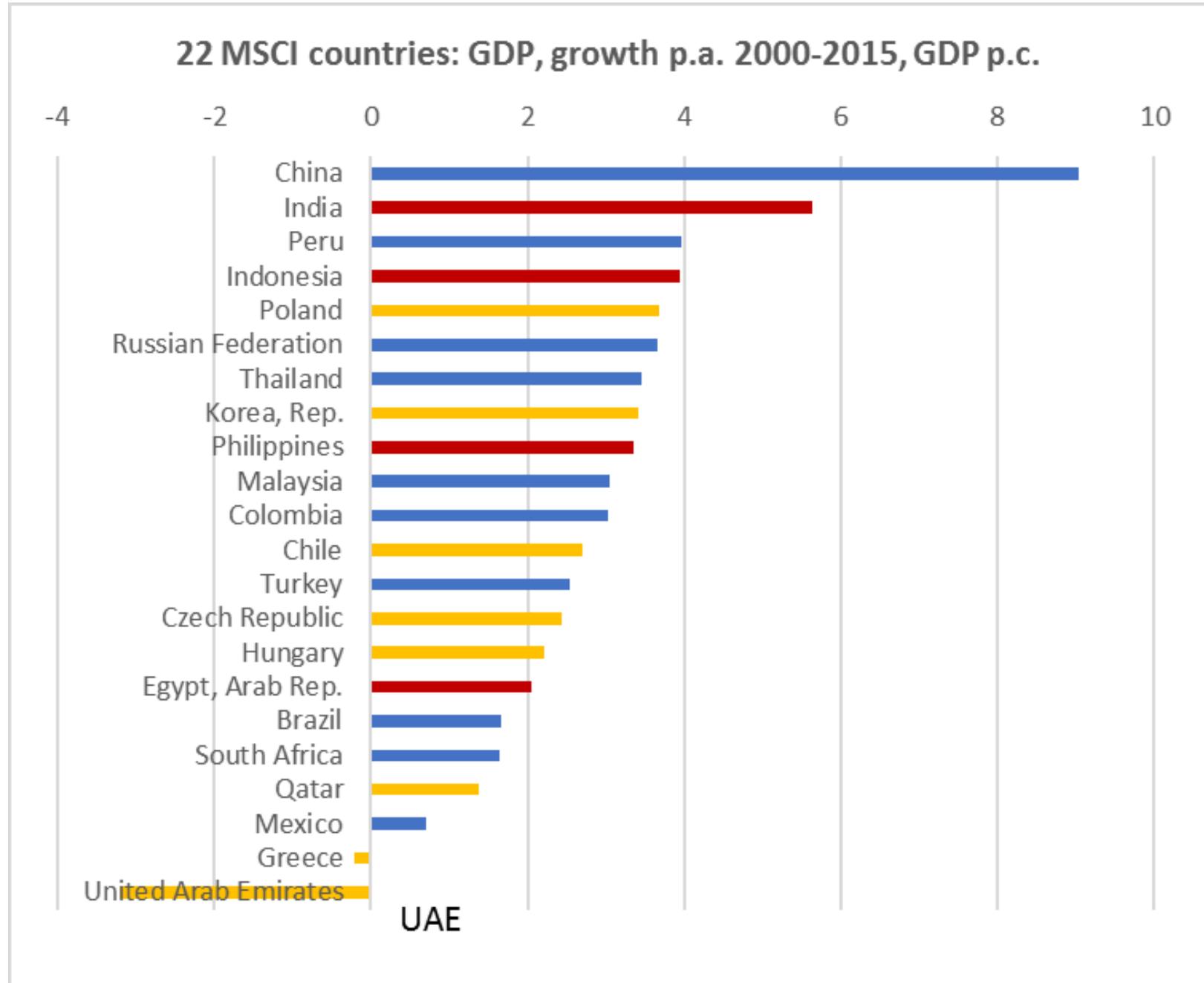
2 Countries in the MSCI portfolio: features and profiles

MSCI group is diverse, includes mainly some UMIC plus newcomers to HIC, plus 2 oil exporters

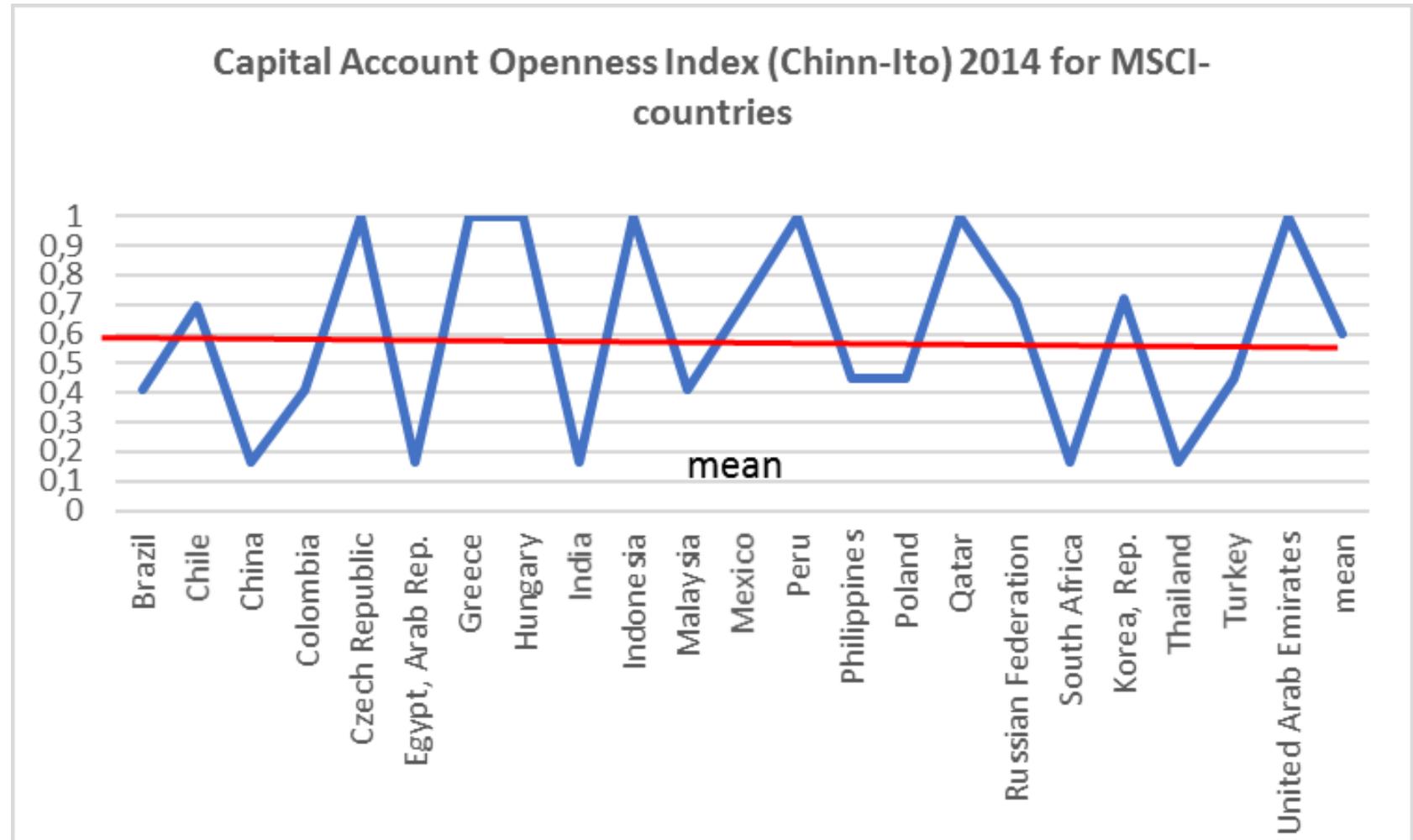


GDP growth is very diverse within MSCI group

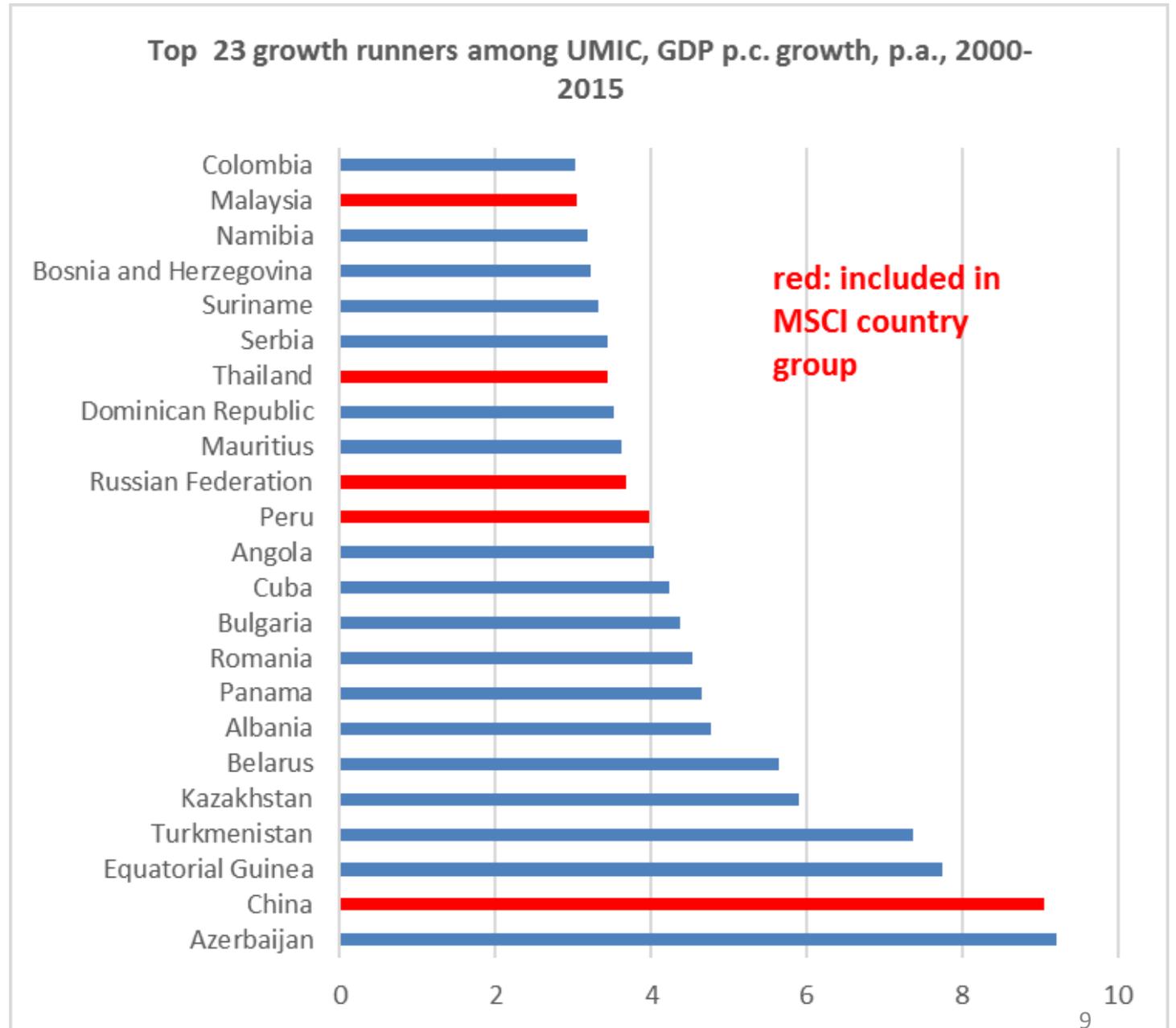
Lower middle income
Upper middle income
High income



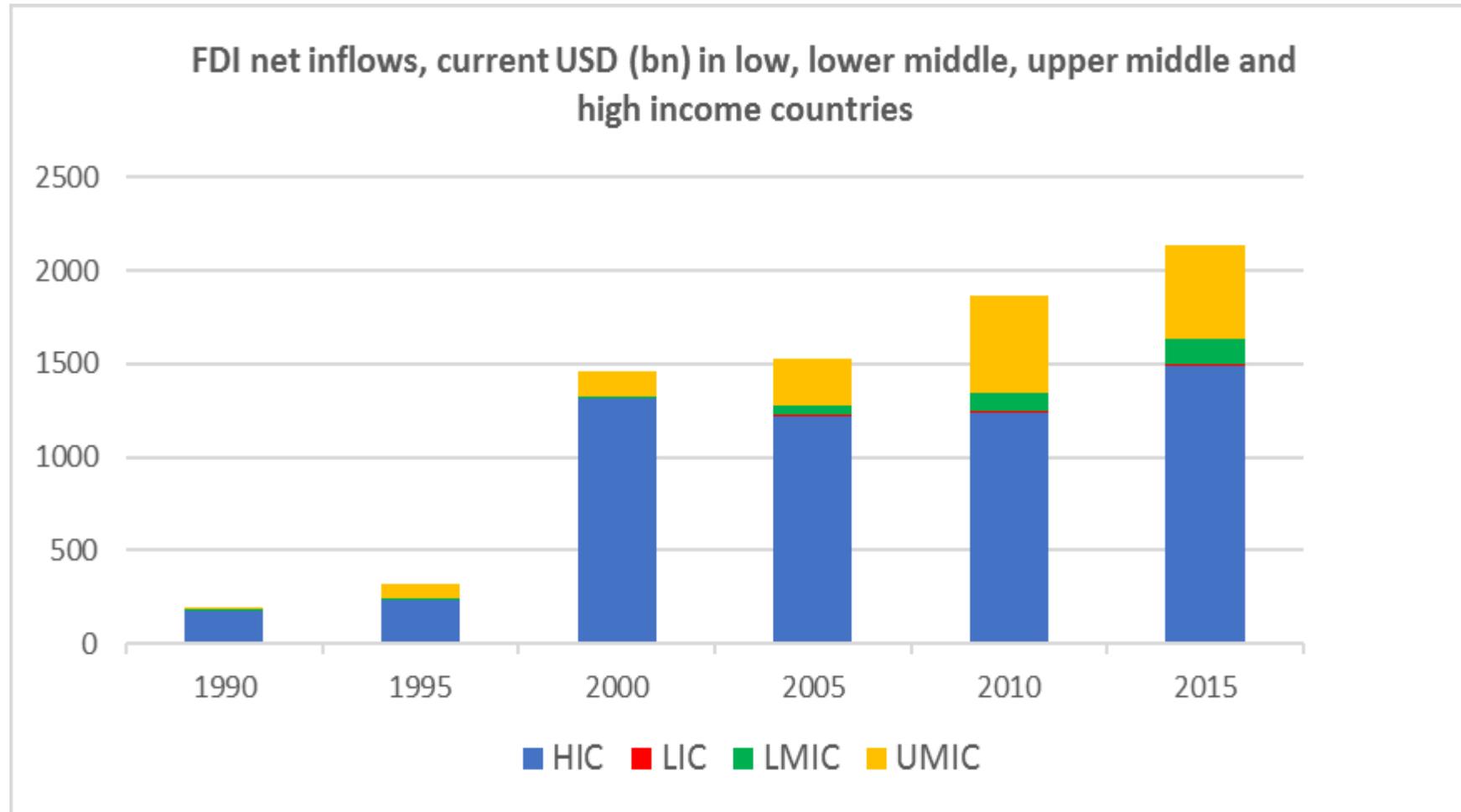
MSCI-countries have no full financial openness, especially China and India. Several country rating below „investment grade“ (junk)



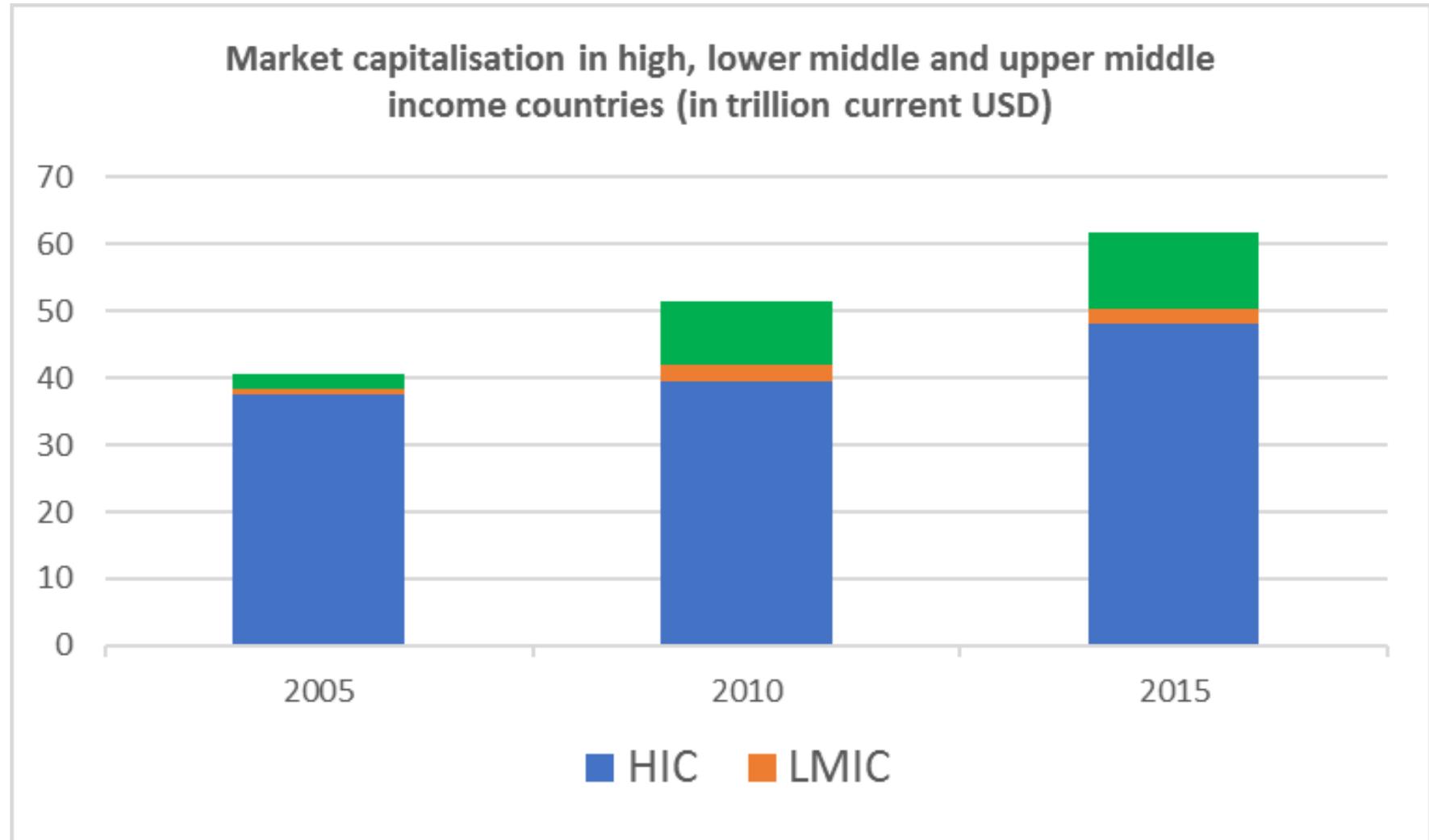
High p.c. growth (> 3,0%) in half of UMIC 2000-2015, not only in MSCI country group



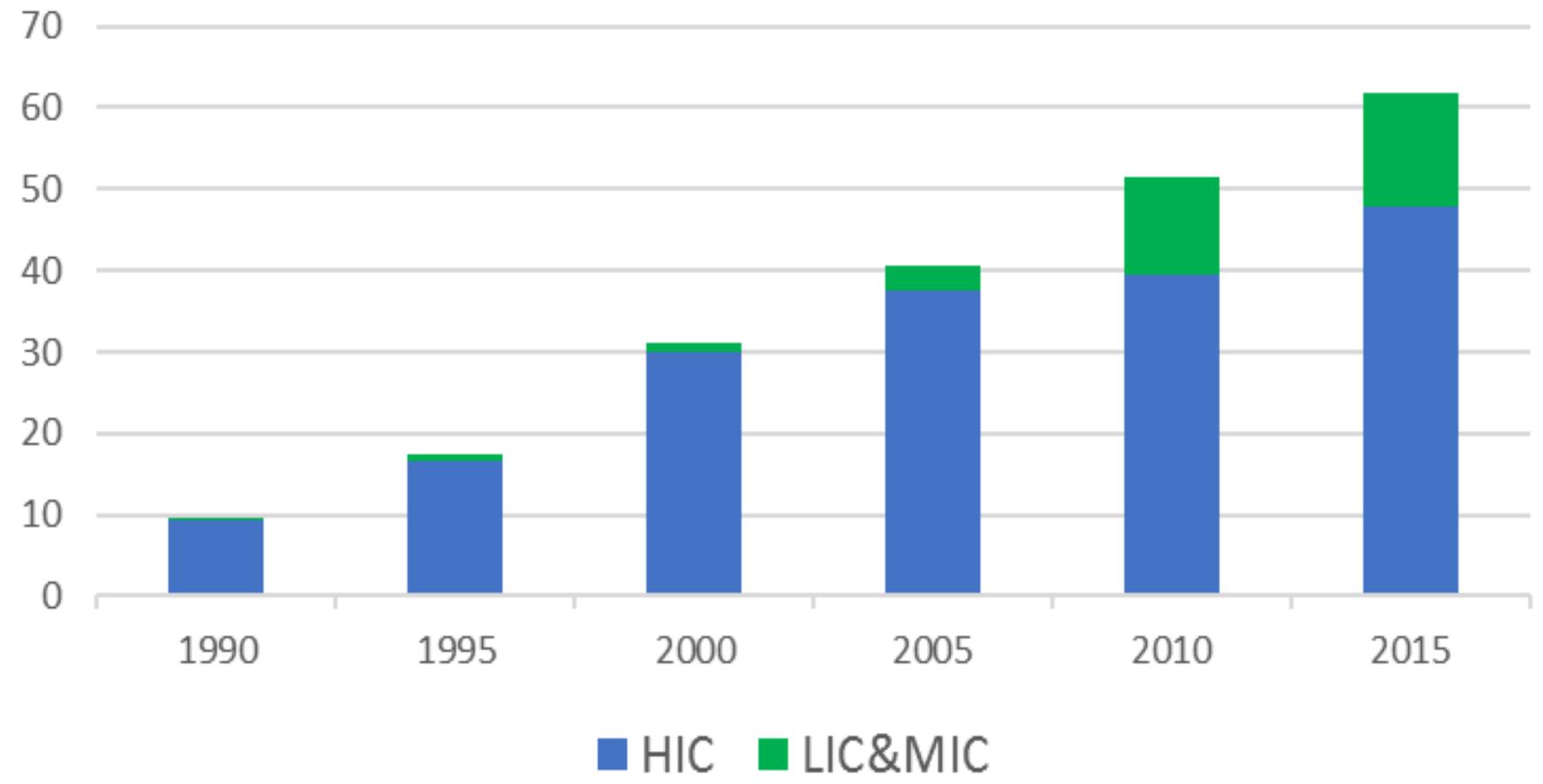
Most FDI inflows remain inside HIC group, but share of middle income countries rises



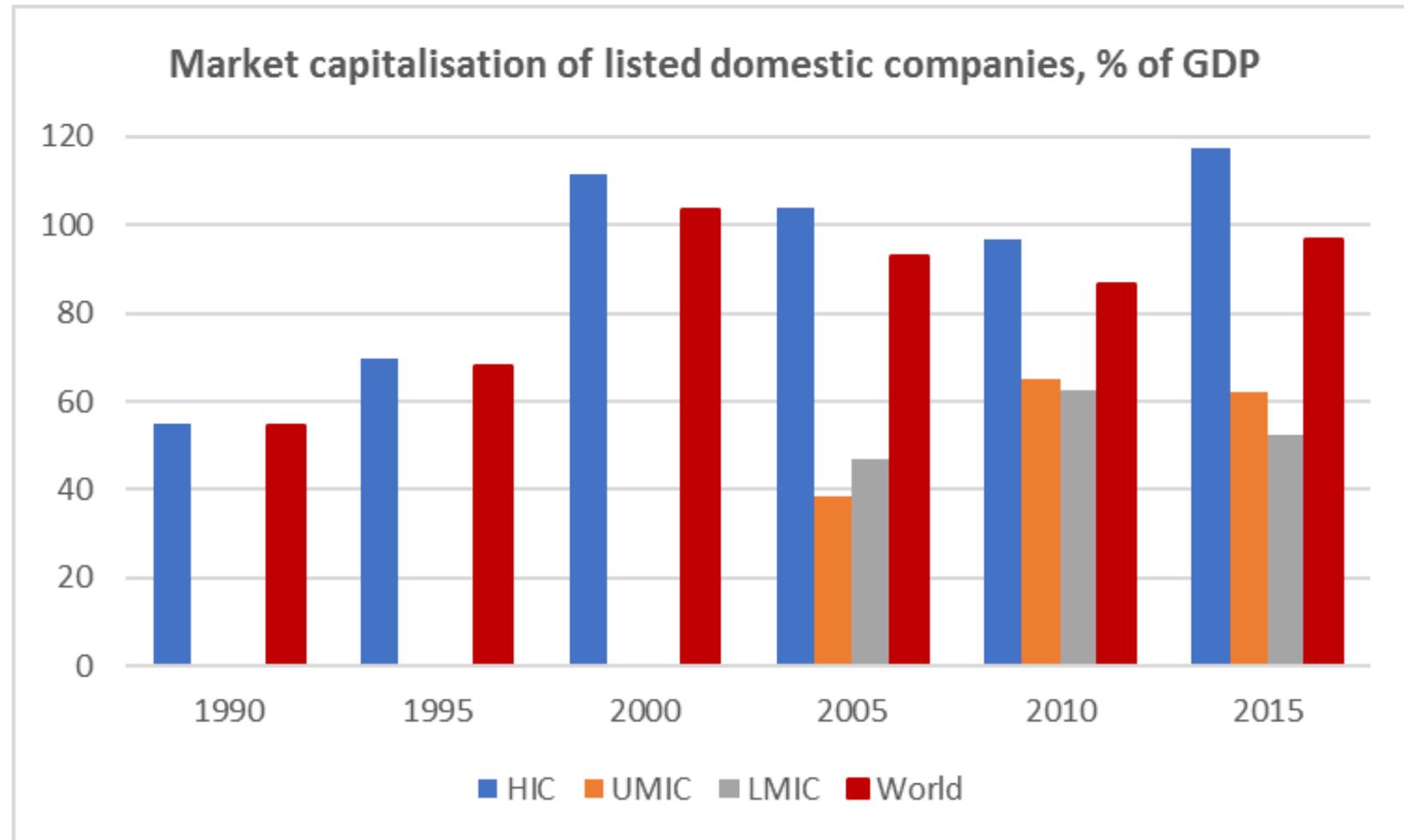
Market capitalisation of UMIC grows quickly, but share remains small



Market capitalisation in high Income and lother countries (in trillion current USD)

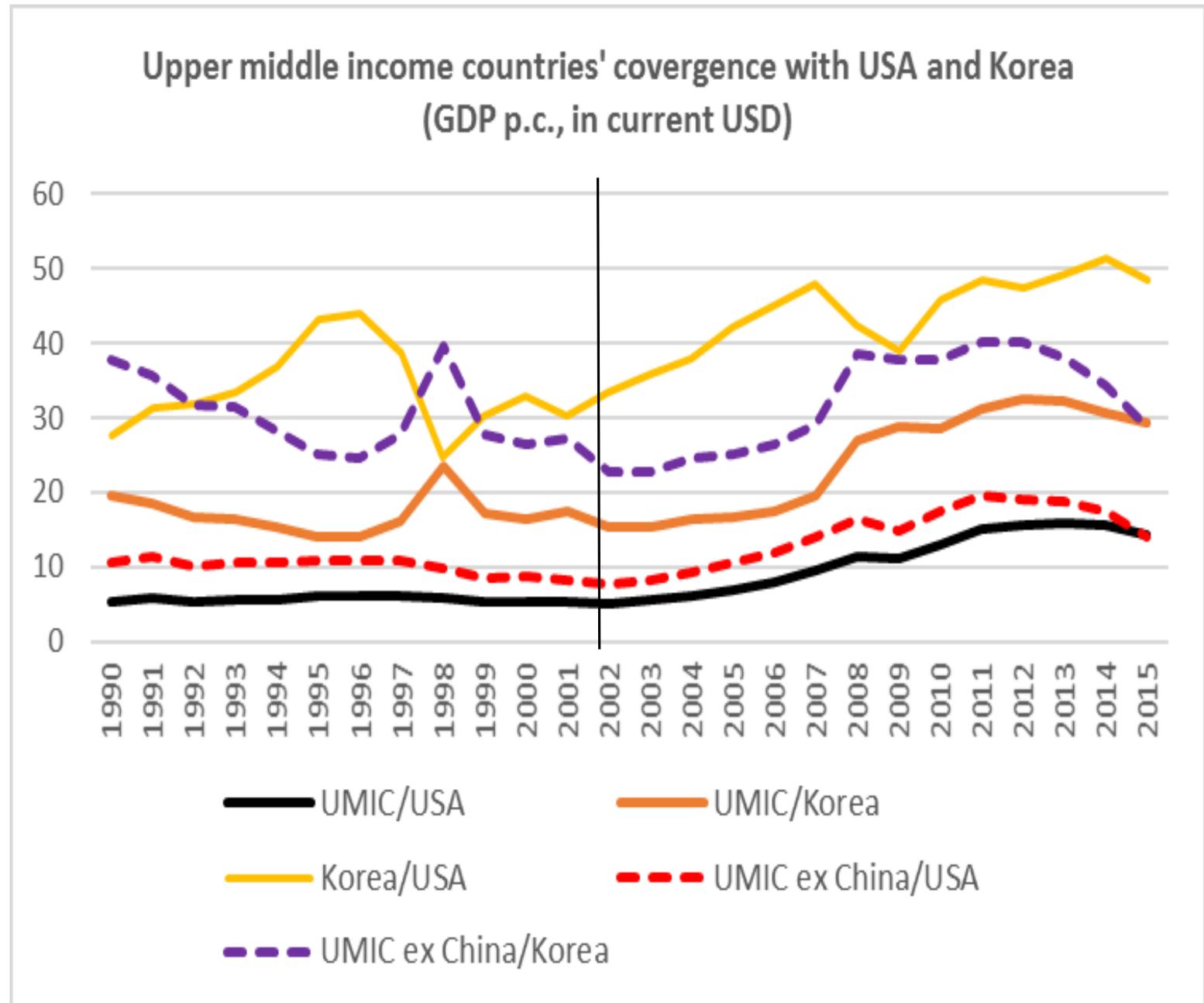


UMIC catch-up with stock market capitalisation, % of GDP, but remain < 50% of HIC



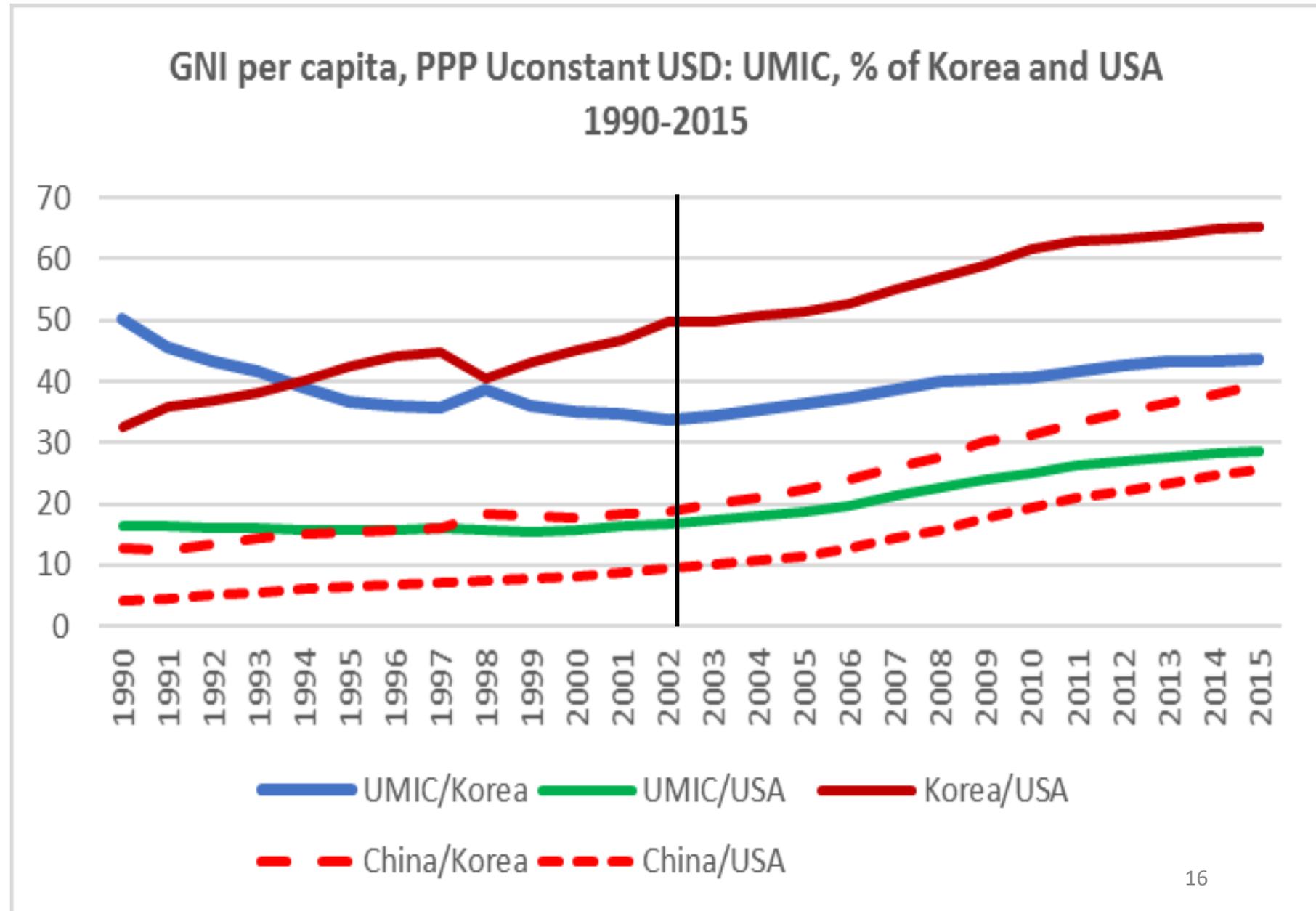
3 Upper middle income countries (UMIC) – the next developed countries?

UMIC catch-up slowly with US and Korea, but level reached is 15% and 30%, resp., starting from 5 and 20%, resp.

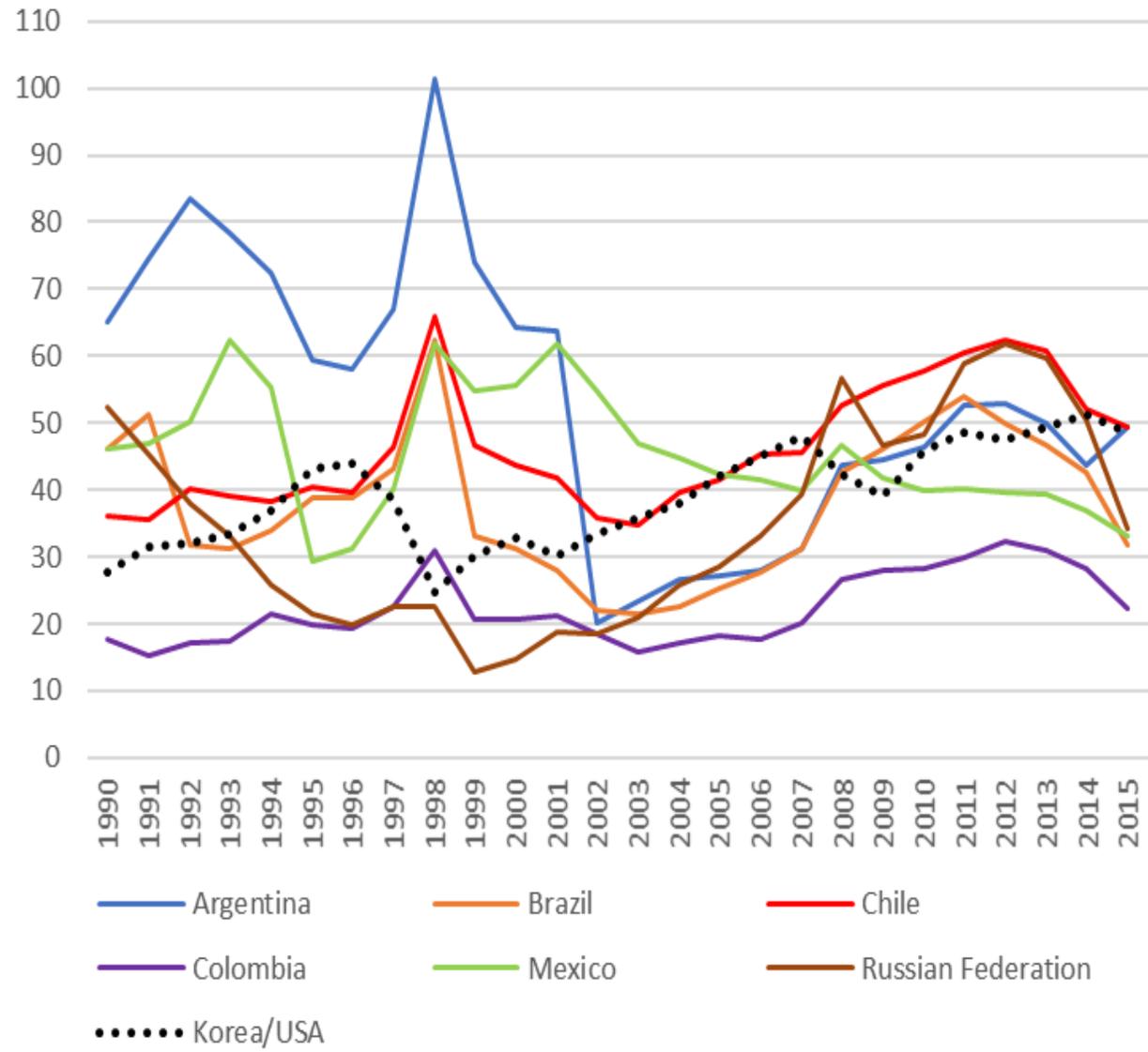


Does income p.c.
in PPP USD
matter?
Convergence of
UMIC since early
2000s

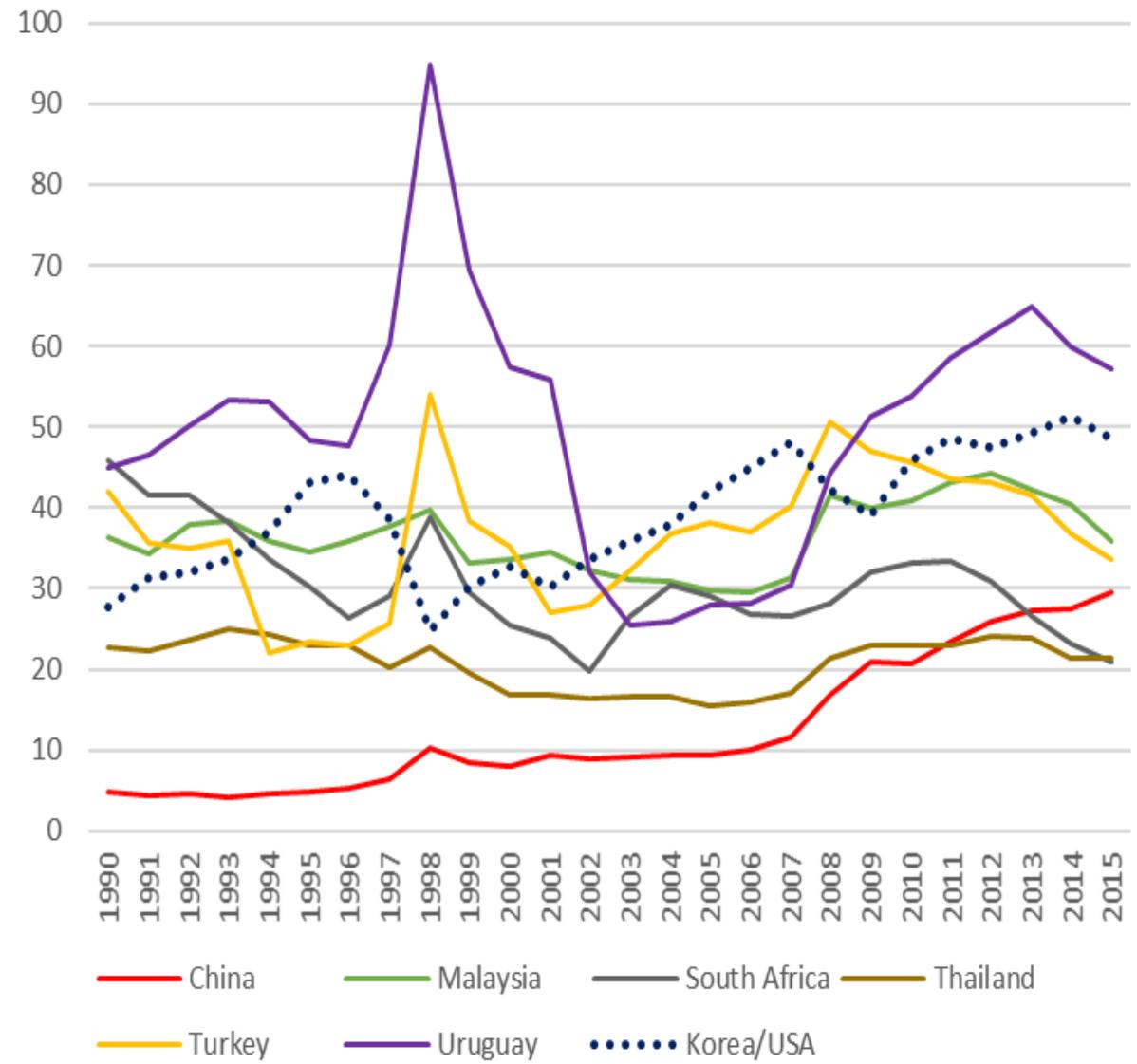
Note: China is 53%
of UMICs'
population (2015)



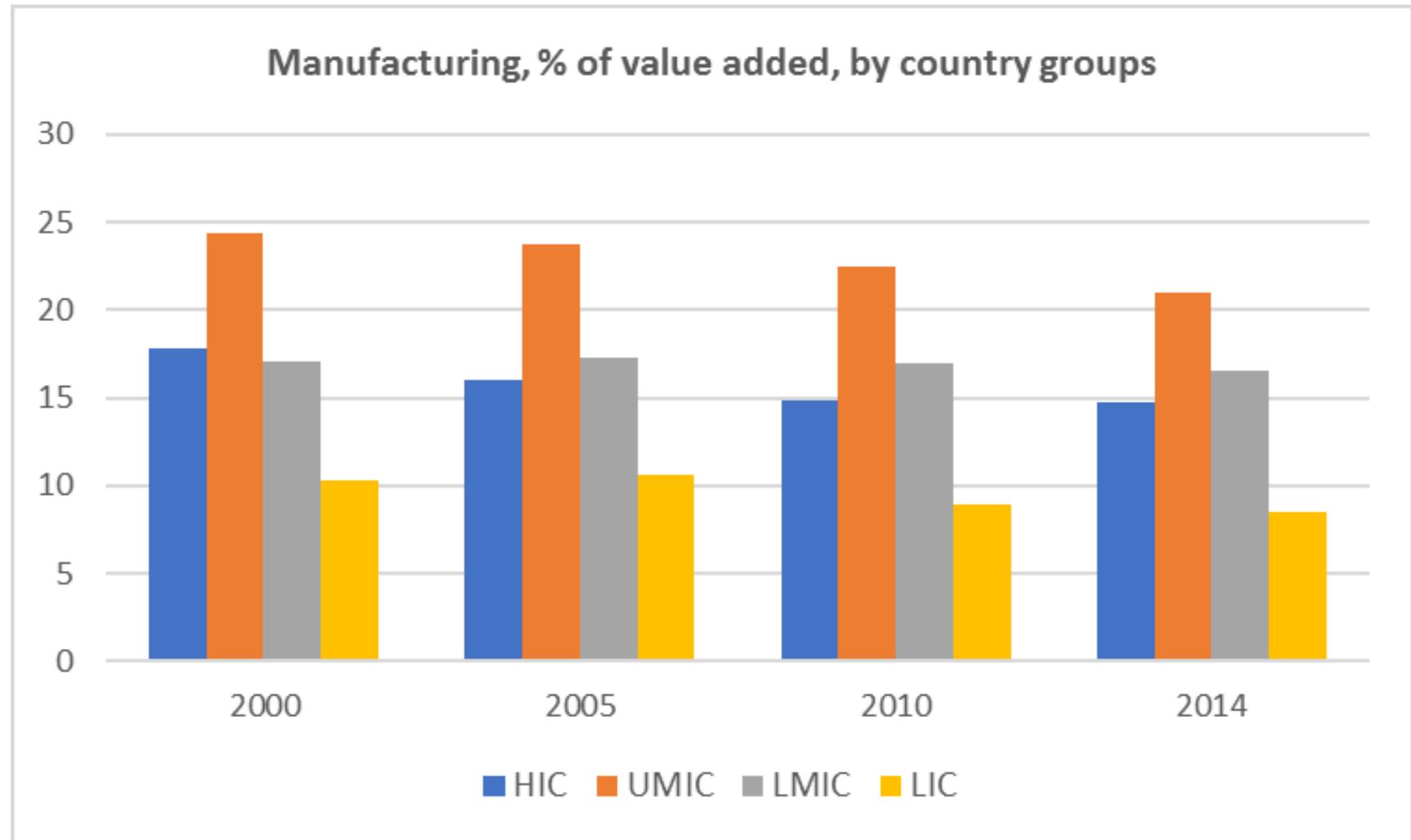
12 UMIC candidates for catching-up with Korea? GDP p.c. in % of Korea's GDP p.c. - batch 1



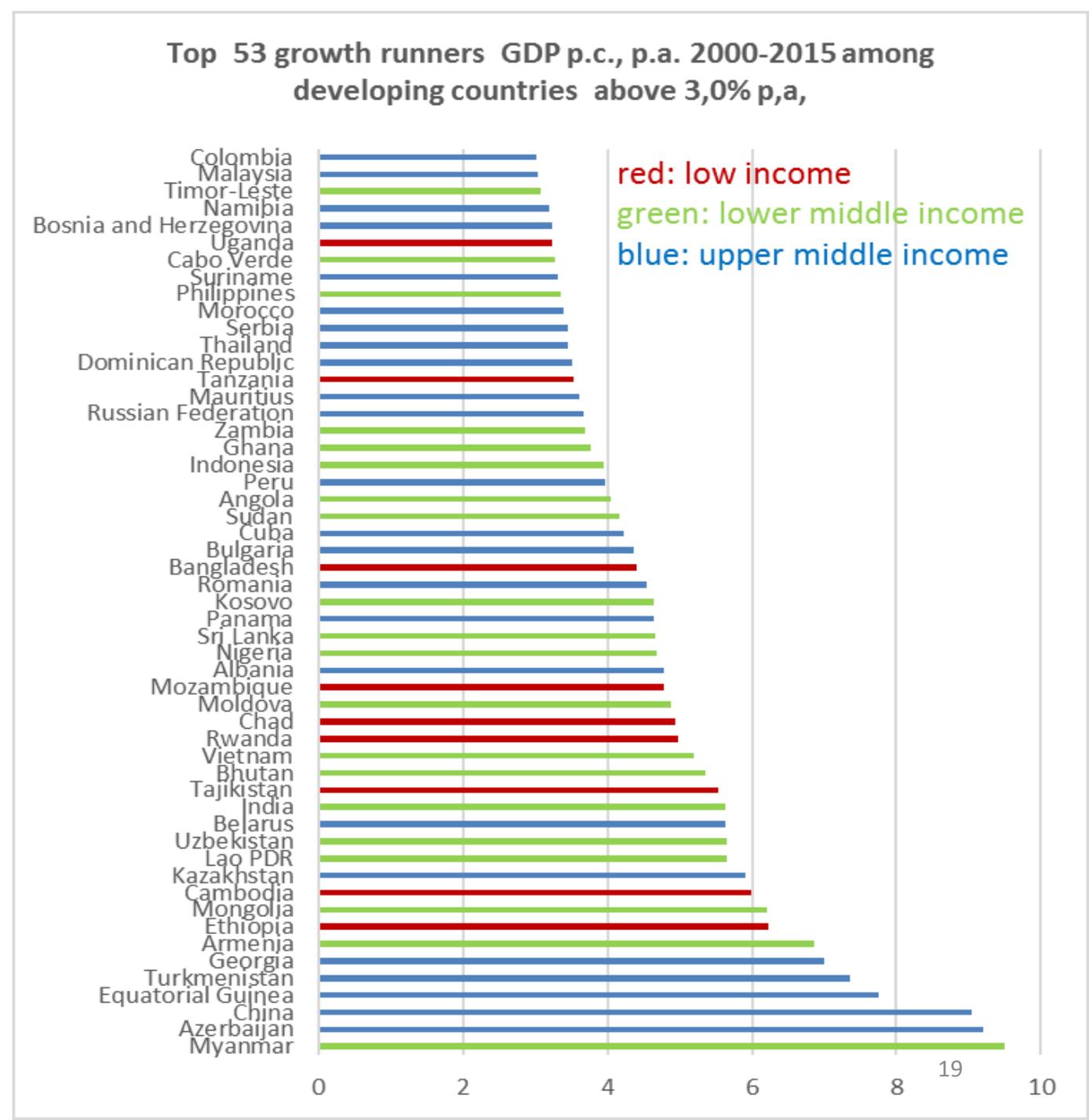
12 UMIC candidates for catching-up with Korea? GDP p.c. in % of Korea's GDP p.c. - batch 2



Middle income countries are more industrialised than HIC, regarding manufacturing



High growth occurred in low, lower middle and upper middle developing countries 2000-2015, not only in some „emerging market“ economies



4 Benchmark Korea for middle income countries

Are EEs “developing countries”?

Korea used as benchmark

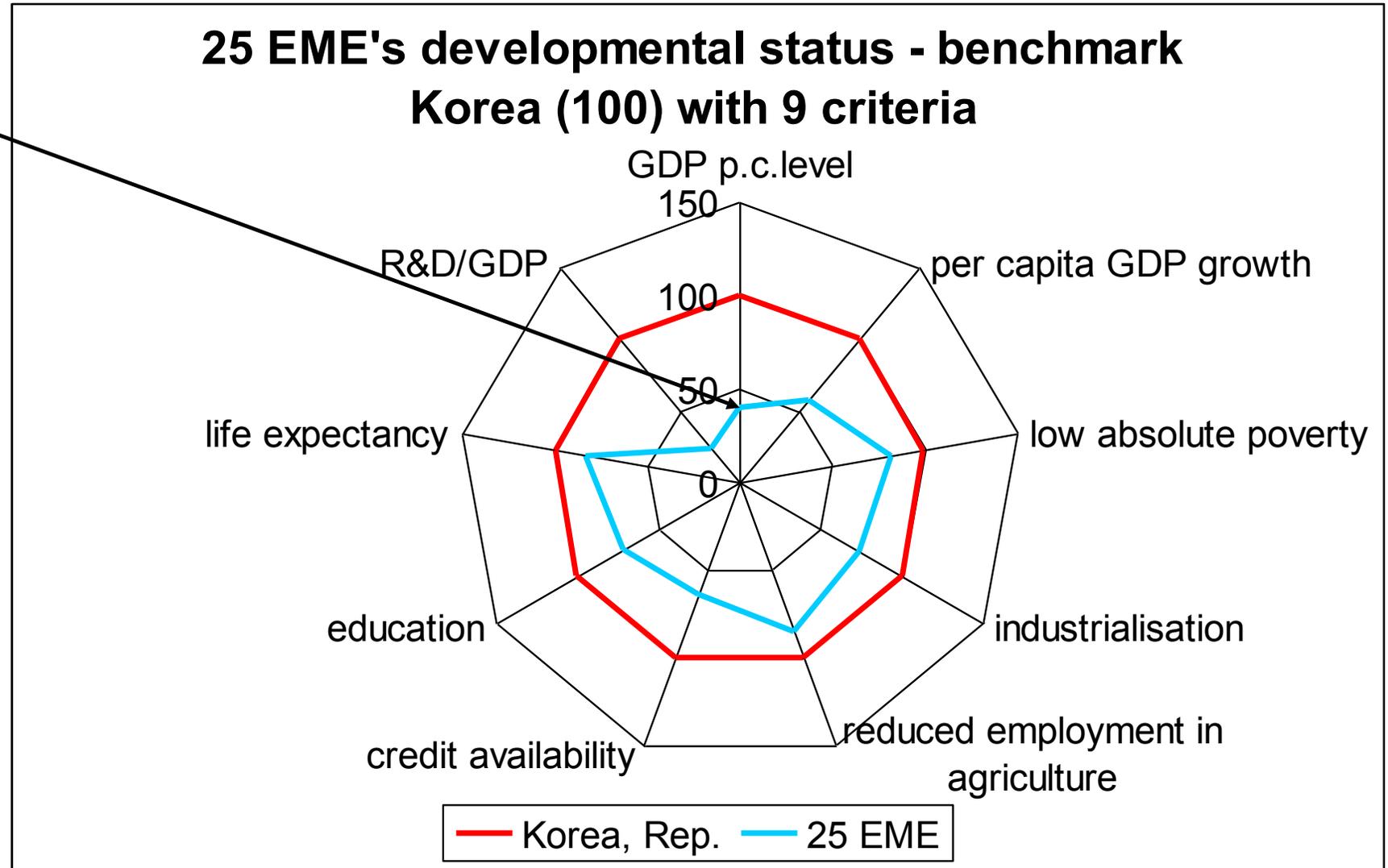
9 criteria used, benchmark is Korea [data red]

- Economy: GDP p.c. level, current USD (2009) [17,110]
- Economy, dynamics: GDP p.c. growth, constant 2000 USD (1990-2010) [4.4%]
- Economy, dynamics: R&D expenditure/GDP [3.4 %, 2008]
- Economy, dynamics: Education (source: HDI) [0.934]
- Finance, money: Credit/GDP [109.4]
- Structural change: Low share of agriculture in labour force [7.2%]
- Structural change: High value added in industry/GDP [27.3]
- [Economy: small differential GDP in USD and in PPP USD] data unreliable
- Social target: Life expectancy at birth [80.8 yrs]
- Social target: Low absolute poverty (<2 USD/day) [0]

Set of 25 middle income countries used for 2010

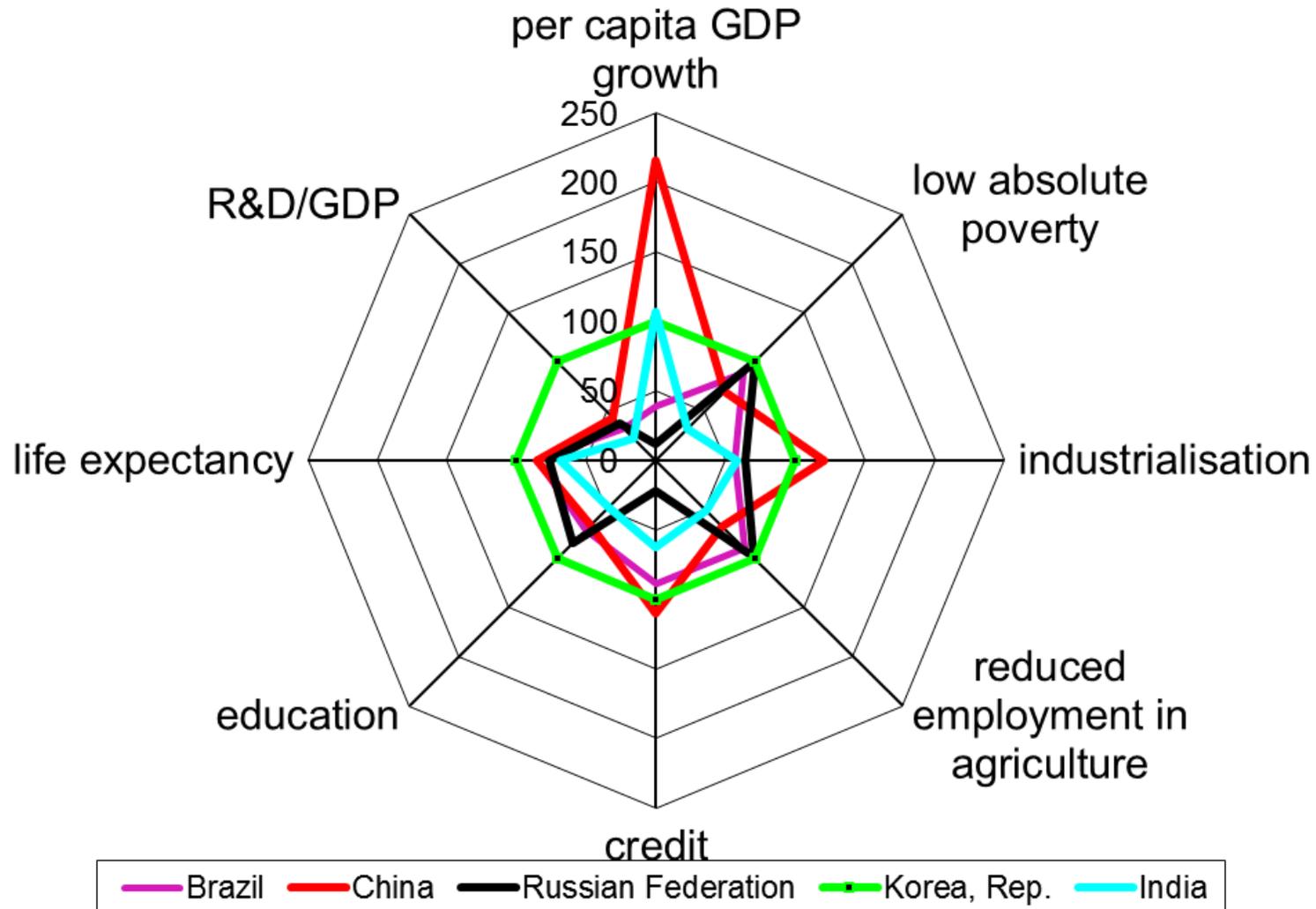
Low GDP p.c. in 25 EE compared to Korea indicates lower level of productivity

Set of 25 countries was taken from various definitions of „emerging countries“ (based on an analysis in Priewe 2013)



Are BRIC developing countries?

BRICS' developmental status - benchmark Korea (100) with 9 criteria (2010)



5 Middle income gap – few newcomers to HIC-group

Only 13 newcomers to „developed countries“ 1990-2015

From 1990-2015 13 newcomers to HIC group (threshold ca 12,000 GNI per capita)

- Korea, Chile, Antigua, Uruguay
- 8 transition countries: Czech R., Slovak R., Estonia, Lithuania, Latvia, Poland, Hungary, Croatia
- 1 oil exporter: Trinidad & Tobago

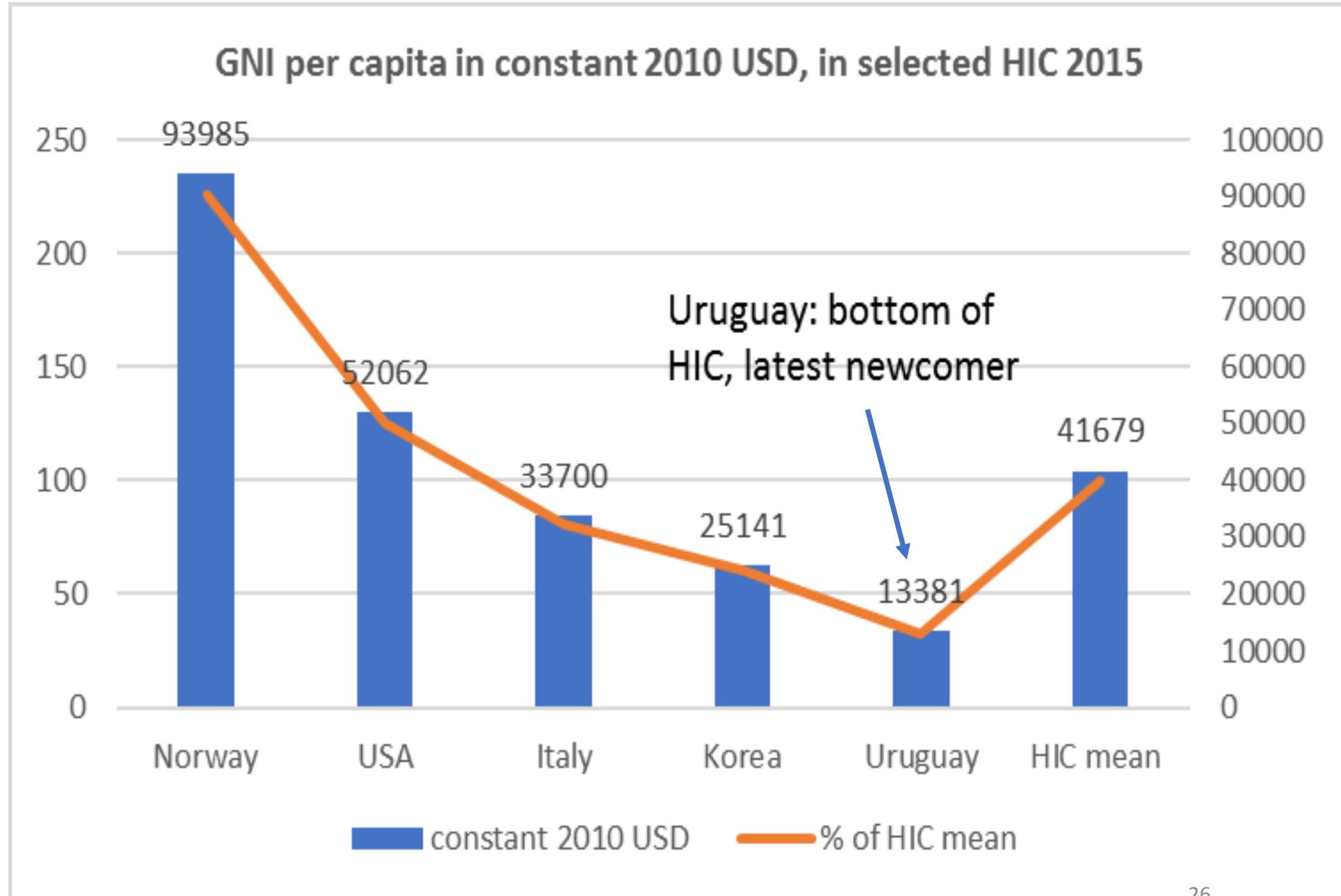
Total population 148 mn, besides Korea & Poland, small countries

13 newcomers add 14% to population of HIC-group and only 5,8% to GDP

Bottom line:

- hardly any upgrading of UMIC to HIC over 25 years
- Strong hierarchy within HIC group
- Newcomers have not finished „development“

Income hierarchy within high income countries (HIC)



6 First conclusions

- We must distinguish „Emerging Market“-Economies and „Emerging Economies“
- Few countries have managed in the last 25 years to access the class of developed countries, i.e. reach the 12,475USD threshold
- Since the early 2000s, a dozen or so UMIC grew faster than HIC, i.e. converged toward the high income group, but the performance is not robust
- There is likely no group of countries that will be capable to reach the high-income-status in the near future, such as the „Asian Tigers“ long time ago.
- If Korea is the benchmark for being a „developed country“, these countries are still far behind and do not catch up
- Development should not only target SDGs 2030, but also target at climbing up the productivity ladder, including catching-up (production approach to development)
- Many of these countries struggle with a variety of middle income traps.

- Many countries above the WB threshold of 12,475 USD are only semi-developed; this threshold is arbitrary.
- The category „developing country“ is multi-dimensional and should be measured with a number of indicators beyond income.
- Yet, the income hierarchy of countries is important and should be extended to the heterogeneous group of HIC (low, middle, top HIC)
- Indeed, all countries do develop, but the meaning of „development“ differs strongly. Abandoning the term developing countries is not the way forward.

7 A simple proposal for a new classification system of countries

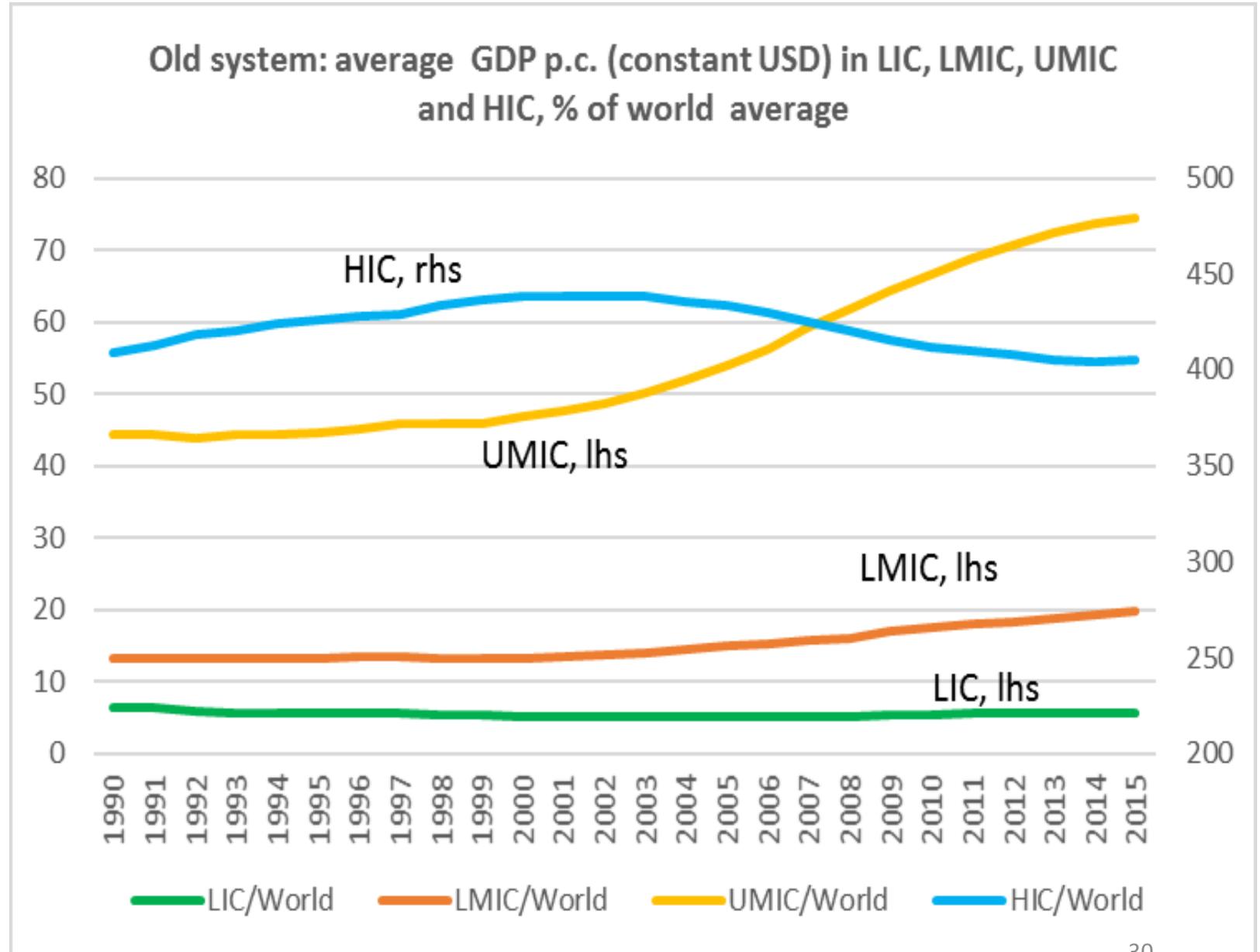
World Bank's old classification system

4 classes

- LIC (<1025 USD)
- LMIC (<4035 USD)
- UMIC < 12475 USD
- HIC > 12475 USD, „developed countries“

Threshold for HIC is arbitrary. Convergence of countries is not addressed.

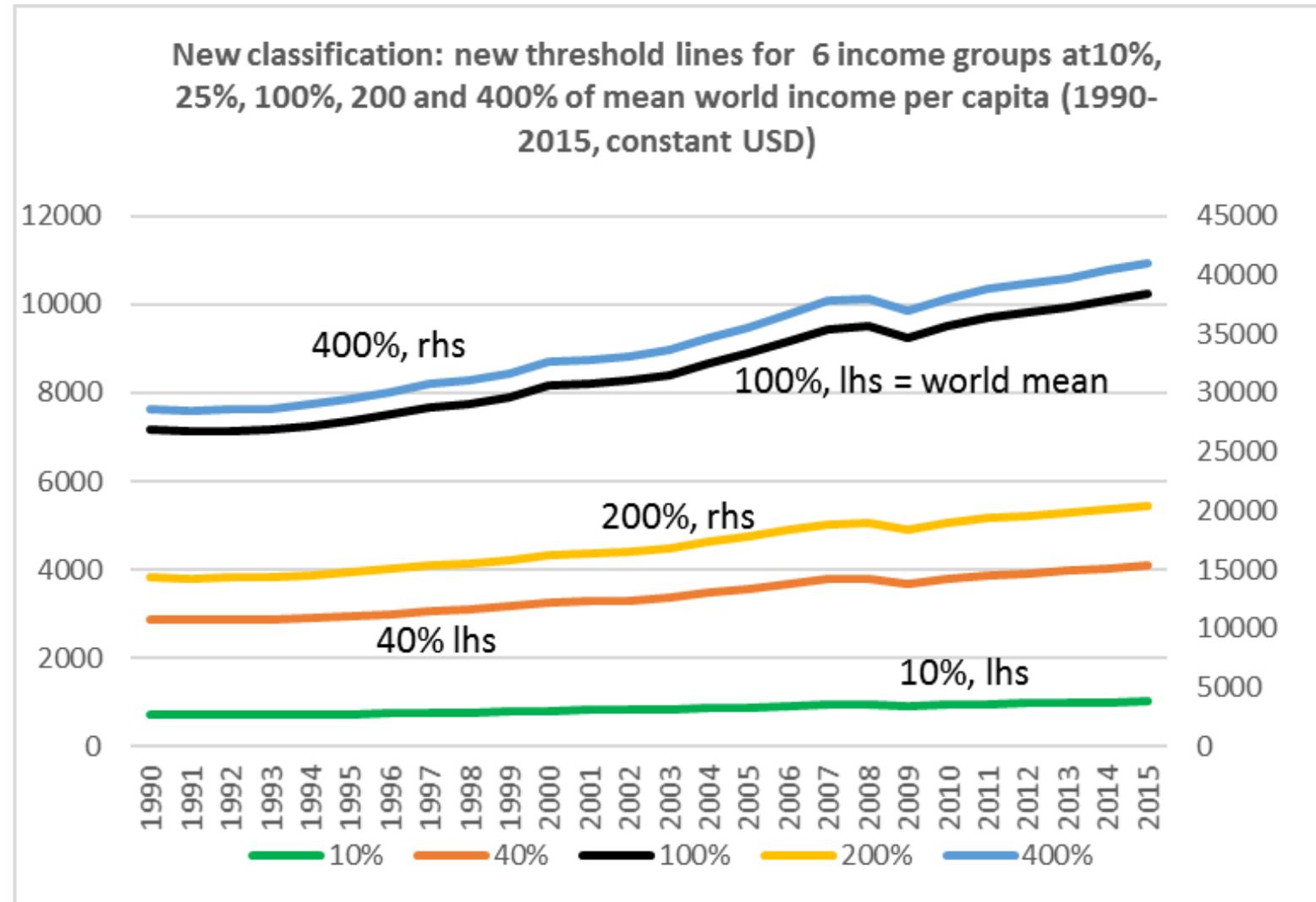
Developing/developed countries criteria must not only be based on income p.c.



Proposal for new system of classification:

- 6 classes
- related to benchmark **mean world income p.c.**
- low < 10%
- lower middle < 40%
- middle < 100%
- low high > 200%
- high < 400%
- top > 400%

„Emergence“ could be used as a category indicating whether or not convergence relative to the benchmark HIC-mean (or some other) takes place.



Developmental criteria

- In addition to income criteria, a set of developmental criteria should be used to assess whether countries have emerged out of the category of developing countries
- Such criteria should focus on the production system and the capacity to generate technical progress either at the world frontier or by continuous absorption of more advanced technology originating in other countries
- This is based on the stock of accumulated knowledge and on having advanced sectors like full industrialisation (manufacturing) or equivalent sectors producing nontraditional tradables
- Korea may serve as a proxy, a set of criteria independent from one country should be developed
- HDI indicators are too rough to assess the full meaning of development and the determinants of the rank in the global hierarchy of economies

All countries should develop, but developmental issues differ greatly

- Low (< 10), e.g. Tanzania: absolute poverty, basic needs, upgrading agriculture, move out of subsistence agriculture
- Low middle (>10, < 40), e.g. India: early industrialisation, education
- Middle: (>40, < 100), e.g. China, Brazil: diversification, upgrading of industries, overcoming middle income traps

The first three classes are developing countries in the traditional understanding of development economics

- Low high (>100, <200), e.g. Korea: technology upgrading, diversification; global environmental issues
- High (>200, < 400), e.g. Italy: reduce distance to technology frontier, welfare state, inequality, global environmental issues
- Top (> 400), e.g. USA: technology frontier, climate change, inequality, financialisation, quality of life, inequality, global environmental issues

- Lower 3 classes similar to World Bank
- Dynamic benchmark: the rank in the global hierarchy is important
- Global development/emergence is flattening the hierarchy
- Low income countries should move out of their class, soon
- Reducing gaps between countries is a way to reduce global inequality (see Target 10 of SDG)
- The gaping income differentials within the HIC group need more attention.