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Crisis in the Eurozone … and what is means for developing countries

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Crisis in the Eurozone … and what is means for developing countries

Bonn, 17 May 2010. It has been clear for some time now that the financial crisis and its consequences are primarily a problem of the OECD countries. The fear that developing countries would thereby be severely affected has not materialized to the extent expected. While many developing countries had to accept cuts in growth in 2009 (GDP growth in developing countries in 2009: Asia + 6.6 %, Latin America - 1.8 %, Middle East + 2.4 %, Sub-Saharan Africa + 2.1 %) and the countries closely interwoven with the OECD area have experienced massive export cuts, as a whole, the developing countries have not been seriously impacted either by the capital markets, which have recovered relatively well, or by world trade beyond the crisis year 2009. They have proven to be remarkably robust, also because many of them have been able to use the financial leeway gained in the "good years" for anti-cyclical policies.

But now comes what has frequently been the case in the history of financial crises: after the crisis of the markets comes the crisis of public budgets and this also first initially affects the OECD countries, which had to prevent the collapse of the financial system and support the economy through the use of public funds. They will need several years to work their way out of the enormous budget deficits again. Above all, the ageing societies of Europe are possibly in store for a long period of higher savings and low growth. This second wave of the crisis will also have structural impacts on the world economy and thus also on the developing countries, which will not be so significant in the short-term, but definitely in the long-term.

The acute crisis in the Eurozone has above all one consequence: the euro is for the time being no longer a safe haven, is thus losing its importance as a reserve currency. The Bank of China, which has for a long time preferred to invest its rising reserves in US dollars, has been cautious in including the euro in its portfolio to a larger extent. This will also stay that way for the time being, because the dissolution of the Eurozone will also be a serious option in the medium term, despite the recent EU rescue package, which for the moment only creates breathing space. The search for a future international monetary system that can guarantee sufficient stability remains on the agenda. Countries that use the euro as an anchor currency and were thus able import stability in the past few years will have to be prepared for times of greater instability. In addition, the euro could gradually lose its role as a second transaction currency after the US dollar again, if for example the Chinese Yuan, the currency of the world's leading exporter, is increasingly used as a transaction currency.

For the advanced developing countries oriented toward global markets, it has become clear once again through the euro crisis that they have to hedge themselves against the risks of fluctuating capital flows on the world financial markets. The Asians have already learnt that in the Asian crisis of 1997/98 and acted accordingly: through the reduction of debts, the built-up of currency reserves and the establishment of reserve swaps and reserve pools (as part of the "Chiang-Mai initiative"). In addition, – by analogy to Europe – a joint monitoring mechanism for the economic policies of the member states is now to be added. However, in Asia they will also know that in crisis situations – like in Europe – there can be no resolution of problems without the IMF because the IMF's possibilities for introducing disciplinary measures and financial volumes are required in an emergency.

For other developing regions that are not so advanced in their regional monetary cooperation such as East Asia, particular caution is recommended: the internal and external debts must be held at bay and the local financial markets be allowed to develop further in order to become more independent of the international capital markets, which however does not mean that they should cut themselves off from these. It is a question of maintaining a cautious management of capital flows and not of insulating markets.

No threatening scenario is on the horizon therefore, since outside of the OECD only a few countries are heavily indebted or threatened by capital flows. Rather, the crisis-related low interest rates in the OECD world will contribute to ensuring that the wandering capital of the financial markets flows to the emerging nations and drives the share and real estate prices upwards there. Investment opportunities in emerging nations and developing countries, which lead to increases in productivity there – above all also to increases in the productivity of resources used for the purpose of resource-saving growth are now being sought therefore. The crisis in the OECD world thus offers emerging nations and developing countries a chance to continue to catch up further.

There is no lack of capital for this, especially now. Already before the crisis, the capital that was invested in ultimately worthless subprime mortgages, Lehman certificates and Greek government bonds by banks, insurance companies and investment funds, can possibly be invested at higher yields in some developing countries. The international development banks have in the meantime all increased their capital and largely spend their additional financial resources as budget support due to the crisis. If it was necessary then for the World Bank to give Nigeria 500 million US dollars as low-interest budget loans in the crisis in order to offset losses in the banking sector and stabilize social security spending, this will be both unnecessary and pointless in the future. This capital must be steered into productive investments and the protection of natural resources. The funds of the development banks are full to bursting for this purpose and private, state and philanthropic investment funds are just waiting for investment opportunities in developing countries.

While Europe is preparing for a difficult consolidation course, whose nexus is still uncertain, the developing countries now have the chance to shift into a higher gear, use the benefit of a lower level of debt and a younger population and make possible investments that signify a more sustainable use of capital than we have experienced in the past few years.

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