The difference in the impact of the crisis in different areas of the world

Who can win and who can lose?

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This question has not one single answer. It is time to prospect, to weigh risks for the future and act. One can learn from diversity and adversity, in a world that is far from uniformity, where new agglomeration trends become evident as they come together with the increasingly complex role of globalisation and international trade, which have acquired a major relevance with recent events; a world with a scenario of increasing vertical specialisation of tasks, where notable growth has occurred and inequality has increased, where the country gap reveals the role of public policies; a world where the current crisis has a different impact based on activity, population segment and country, and will have differing effects on its competitiveness. The article presents these different impacts in a world and at a time in which there are also opportunities.

Many questions like this one, in a moment like this, with high levels of uncertainty, do not have one single answer for economists nor for the not so much economists. And for those of us who also do prospecting usually comes the fact that the future is not written and depends on individual and collective action on the ground that is taken now but determines the future in the short and long term. Any decision – individual, corporate, social or political – comes along with a vision of the future, whether right or wrong, either immediate or not so immediate. What seems to be beyond any doubt is that the current crisis, though comparable to other periods, also has some distinctive features making it different. In any case, it is time to prospect, weigh risks for the future, act and get prepared with contingency plans.

In times of crisis it is time to prospect, weigh risks for the future and act.

In a world far from uniformity, in which new agglomeration trends become evident, where given activities and talent, creativity, innovation, technology and capital (despite its volatility) concentrate on certain areas and countries, we can learn from diversity and adversity. These new trends come together with the increasingly complex role of globalisation and international trade in a balance between dispersion and concentration forces (*OME*, ACC1Ó, 2008), which have been modified by a knowledge-based economy and progress of ICT. Globalisation and international trade have grown in relevance as the financial crisis that started in the United States spread to emerging economies, which are now experiencing a strong slowdown in their average growth (International Monetary Fund, IMF, 2009).

We are in a world scenario with increasing vertical specialisation of tasks, in which trade of goods is being replaced by trade of tasks (*OME*, COPCA, 2007). In the last decades, this world has been experiencing strong growth, the more so in so-called emerging economies where inequalities also have increased.

The OECD has stated a growth of inequality and poverty in two thirds of countries in the last five years. The Gini coefficient has increased by two points in the last twenty years. It also points out that the degree of affection and the causes leading to such inequalities are explained by numerous factors of several kinds, from different use of technological capacities to diverse sociopolitical change. It points out that the current level of expenditure in social policies is higher than in the past due to ageing population in developed countries, but it also states that the redistribution effect of public expenditure – from the mid-1980s to the mid-1990s – caused a slowdown in the increase of poverty, and positive effects of this expenditure had less effect on the poorest, as it did in the following decade. The relevance of the role of public policies in the different evolution of countries is also explained (OECD, 2008).

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All this indicates that the current recession can have a very different impact according to the activity, population segment, country and area concerned. In fact, in May 2008, Stephan Garelli, from the Institute of Management Development, (IMD), pointed out that the current crisis could affect the leading position of the United States in the competitiveness ranking published by the organisation, stating that no country is immune to collapse, no matter its competitive position. Garelli quoted Benjamin Franklin's words: «Even a small hole can sink a big ship.»

It has also been shown that emerging economies have not been able to escape from recession, which is deeper and larger than expected in developed economies, as opposed to what some analysis said in relation with decoupling (IMD, 2009).

With respect to the degree of interdependence between economies, the study by Kose, Otrok and Prasad (2008), commented in the last *Informe Anual de l'Observatori de Mercats Exteriors* (Observatory of Foreign Markets Annual Report) is worth mentioning. The authors' conclusion is that integration mechanisms and forces interact with each other at both global and regional level.

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At the same time, the authors point out that the current recession can have distinct effects on the pace, the impact and long-term competitiveness of countries according to public and private, individual and collective response.

Different impact in different countries

Countries depending on exports such as Japan, Germany, South Korea and China also suffer from recession in global demand and need to turn to the domestic market. Emerging countries like China, Brazil and India have not been left untouched by the recession in Europe and the United States.

All countries are undergoing credit restriction. Also emerging economies depending on foreign capital (some Central and Eastern European countries, the Baltic states, Turkey and some in Central Asia) will be vulnerable.

The United Kingdom is especially vulnerable due to high family debt – 150% of available income – one of the highest in the developed world. It is also one of the countries most dependent on the finance sector, which has contributed to 25% of its growth in the last five years and amounts to more than one fifth of employment, compared to 6% of jobs in the United States.

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Public debt in Japan amounts to more than 170% of its GDP, in Italy it is more than 100% and Greece is not lagging much behind. These countries might soon be limited in their monetary and taxation possibilities.

Countries with a surplus like China, Russia and the Persian Gulf countries may have smaller reserves due to the rescue of banks and companies. They might take less damage from the crisis than those that did not invest enough in their future competitiveness, considering investment as implying more economic diversity in social infrastructure, especially education, institutional quality and sustainable development.

Competitiveness and resilience to crisis in different countries

Globalisation, especially financial one, has reached unprecedented features. Although it is true that from a historic perspective, globalisation and setbacks due to social distress and protectionism have been around for a long time at the current level and in possible scenarios that are being discussed now, some pieces of analysis also point towards several globalisation waves with distinctive features. The globalisation process has played a relevant role in distributing economic activity, tasks and the generation of new agglomeration trends involving change related to income and labour, and it has also had an influence on the different positions of countries in a heterogeneous world.

It is currently obvious that a cooperation and commitment scheme between emerging and advanced countries to stimulate the economy and avoid protectionism is the way to go for the benefit of all. Despite present uncertainty, some countries can find measures to reach more sustainable competitiveness in the long term.

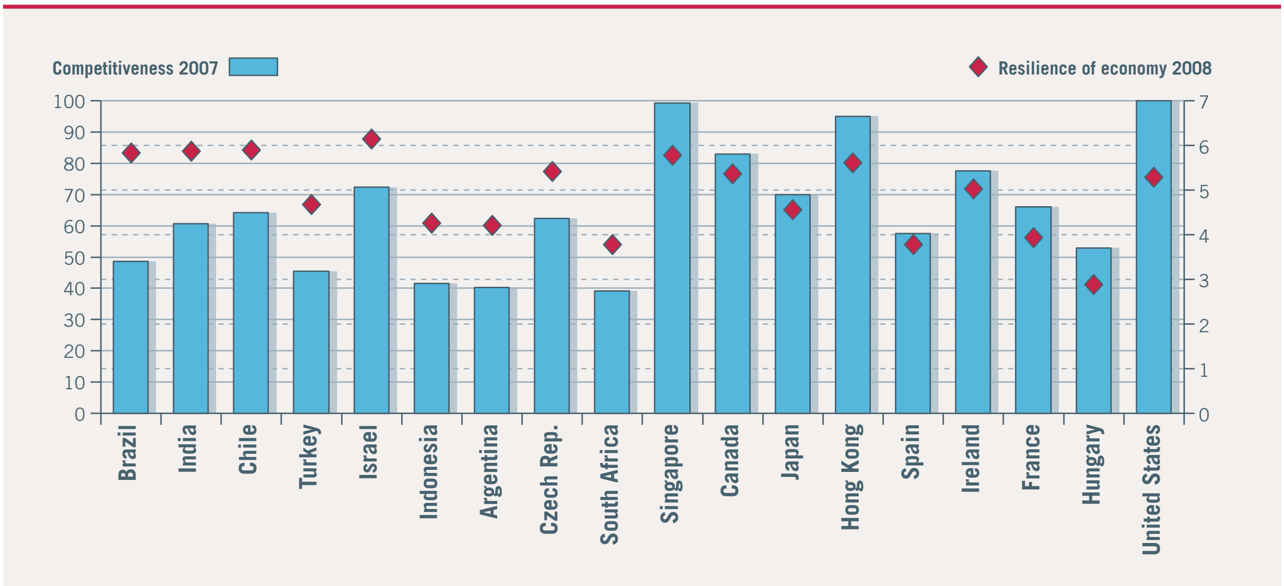
In this respect, it is interesting to compare the IMD 2007-08 competitiveness ranking and that of resilience of different countries to change of economic cycle from the same source, published one year later in its competitiveness report as shown on Chart 1 (C 2007 refers to the competitiveness ranking and R 2008-2009 to that of resilience) and on Graph 1. Among countries with a far worse position in the resilience than the competitiveness ranking are developed ones: the United States (1st in competitiveness and 21st in resilience to change of economic cycle), France (25th and 41st, respectively), Ireland (12th and 25th), Spain (39th and 45th) and Japan (22nd and 32nd).

Contrarily, among countries featuring the biggest opposite difference between both rankings are some developing ones. This is the case of Brazil, taking the 43rd position in the competitiveness ranking but ranging 9th in resilience to change of economic cycle, as well as India (29th and 8th, respectively), Turkey (48th and 31st) and Indonesia (51st and 38th). Also countries like Denmark, Sweden, Norway and Finland are well positioned in both rankings.

Unequal risks and scenarios for different countries and economic areas

It is interesting to note that the March 2009 *Economist Intelligence Unit* identified three macroeconomic scenarios for the evolution of

Graph 1. **Comparison between the competitiveness and the resilience ranking**



Source: OME, based on IMD data

Among countries with a far worse position in the resilience than in the competitiveness ranking are developed ones like the US, France, Ireland, Spain and Japan.

***Table 1.* Comparison between competitiveness and resilience ranking**

Country	Competitiveness (2007)	Resilience (2008-2009)	Variation
Brazil	43	9	34
India	29	8	21
Chile	26	7	19
Turkey	48	31	17
Israel	20	4	16
Indonesia	51	38	13
Argentina	52	39	13
Czech Rep.	28	17	11
South Africa	53	44	9
Singapore	2	11	-9
Canada	8	18	-10
Japan	22	32	-10
Hong Kong	3	15	-12
Spain	33	45	-12
Ireland	12	25	-13
France	25	41	-16
Hungary	38	54	-16
United States	1	21	-20

Source: OME, based on IMD data

▲ The countries featuring the biggest difference between low competitiveness and high resilience ranking are developing ones.

the crisis and risk assessment. The first, at an estimate likeliness of 60%, is that in which governmental stimuli are able to stabilise the global financial system by 2010 and restore economic growth in countries leading the developed world at a lower level than in recent years.

A second scenario – at a 30% probability rate – are countries with big associated risks and likeliness of deflation and depression in the OECD countries. In this scenario, economic stimuli are not enough and the bigger role of governments in rescuing banks and attempting to stimulate domestic demand leads to protectionist pressure and hampers globalisation.

In this scenario, as has been mentioned earlier, it is not only indebted economies that are vulnerable[1] but also those having a seemingly better position – based on savings rate, trade and current account surplus – can get in serious trouble if global demand and trade collapse.[2] And in the developed world, the eurozone can be struck harder by limitations of monetary policy in some countries, anticipating a stronger impact on those with a weaker position regarding competitiveness and whose sustainability of its public finance is dubious.

The Economist also insists on interdependence of emerging markets, which it classifies according to three types based on their vulnerability:

- Countries where growth has been driven by credit expansion and appreciation of asset prices, i.e. Central and Eastern European countries with a high current account deficit while struggling with high foreign debt (Hungary, Baltic states, Bulgaria and Romania).

- Countries with a strong link to global growth (most Asian countries) depending on growth of their exports, for which a protectionist scenario can lead to export decline in the medium term, with strong effects on the solvency of companies and banks. In such a protectionist scenario, the role of China in the recovery of the world economy is at stake. Aggressive measures by China to stimulate private consumption by improving health and social protection may be insufficient and not make up for the decline in exports. Imbalance may persist in the country and affect the global economy. The increase of bank credits as a reaction to governmental pressure may translate in inefficient capital distribution and create a bigger excess capacity and low return on investment that eventually may require support from the government to restore capital adequacy.

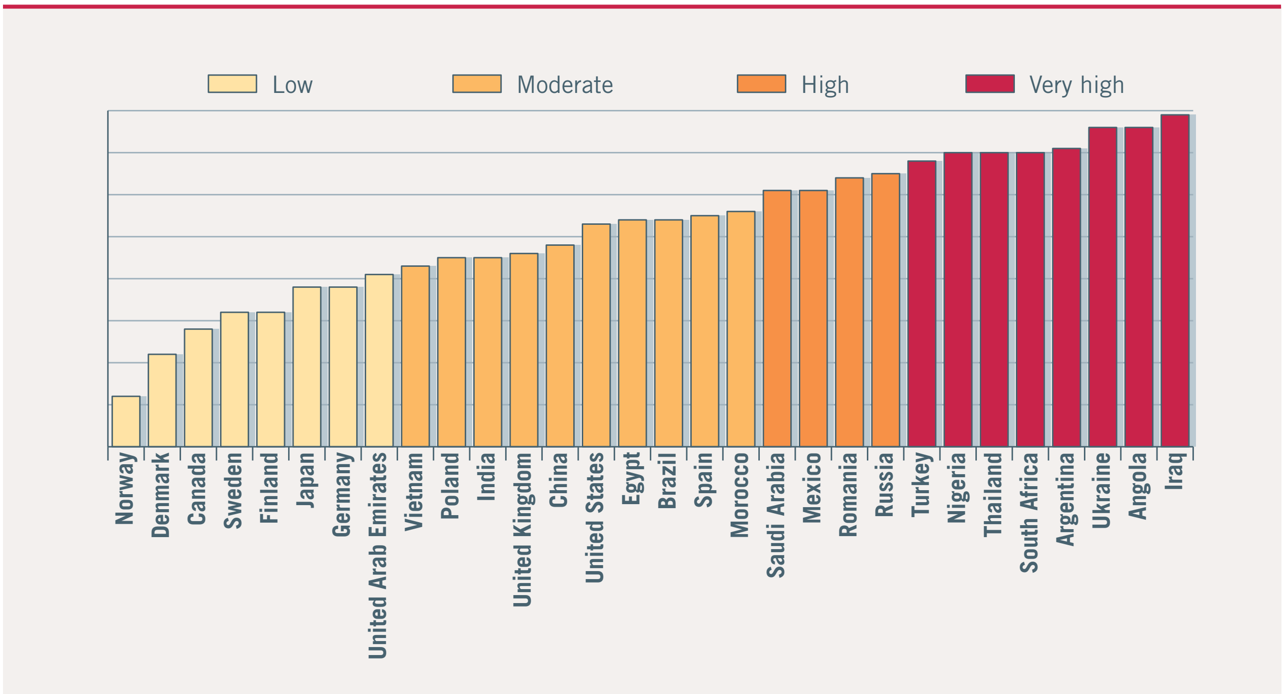
- Countries dependent on commodities. They include such in Latin America, the Middle East, Africa and Russia, which are struggling with price falls[3] as a reaction to persistent decline in global demand. Some countries may undergo financial restrictions, such as the economies managed more carefully that invested in productive capacity. Sovereign wealth funds will become less important as their value is persistently declining.

Finally, a strong decline in economic activity according to the third alternative risk scenario[4] may cause an increase of the risk of social distress and, as Graph 2 shows, a different degree of vulnerability of social and political stability in those countries.[5]

A time for opportunities to improve competitiveness

As can be inferred from this article, given the current situation, some stakeholders could lose or win more than others and have a different impact on the immediate future as well as in the longer term, based on the individual and collective action they take now. In situations as the present one, people and companies resort to the most economical alternatives. Low-cost competitors are gaining ground in many industries while others are losing. Also new competitors appear with different, innovative business models allowing lower costs and prices.

Graph 2. Risk of social and political instability



Source: Economist Intelligence Unit.

A strong decline in economic activity may cause an increase of the risk of social distress.

Some companies also take advantage of situations like the present one to launch new products: it is easier and more economical to draw the attention of the customer when competitors are forced to cut costs and customers are under strong pressure, so they may be more open towards trying new products, especially if they are cost-saving. Hence a crisis can also be a time for opportunities to improve competitiveness.

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Notes

1. United States, United Kingdom, Spain and Ireland.
2. Germany, Japan and China.
3. The oil price is decreasing $20 a barrel.
4. Estimated to be likely at a 10%.
5. The resulting indicator has a scale going from 0 (non-vulnerability) to 10 (highest vulnerability). It has two components measuring vulnerability itself, with indicators such as inequality level, history of political instability, corruption, ethnical fragmentation, trust in institutions, situation of minorities, level of social policies or political systems. The other component measures economic malfunction, with indicators such as income growth, unemployment or living standard.