BBVA | RESEARCH

Economic Outlook

EAGLEs

Annual Report 2012
Economic Analysis

- **The group of emerging countries which compose the EAGLEs and the Nest (our watch list of countries which could eventually become an EAGLE) is expected to create more than two thirds of total global growth in the next ten years.** On the other hand, G7 contribution would be around 16 per cent.
- **China, India, Brazil, Indonesia, Korea, Russia, Turkey, Mexico and Taiwan maintained their EAGLEs membership after BBVA Research updated its forecasts.** Egypt became the first "fallen angel" entering the Nest group. Chile and Ukraine also joined this group, which means that there are now 15 economies in the waiting list to become an EAGLE.
- **Changes in the composition of the EAGLEs and the Nest highlight the advantages of using a dynamic approach** to evaluate which are the key leading economies in the emerging world.
- **Macroeconomic vulnerabilities in the EAGLEs countries remain relatively limited,** at least when compared with the developed world. However, the degree of vulnerability varies widely from country to country. The report offers a map of vulnerability by country.
- **The special topics of the Annual Report pertain to China growing net credit position with the rest of the world,** the growing relevance of the Gulf as a bloc and the decreasing economic importance of Africa within EM.

Index

Summary

Compared with our estimates last year, the group of EAGLEs and their Nest are expected to contribute more than two thirds of global growth in the next 10 years (from 59% estimated last year). G7 contribution slightly rises to around 16% from 14% last year.

- Out of our 10 original EAGLEs, 9 have maintained their status after updating our forecasts. The fallen angel is Egypt, given our sharp downward revision to its growth prospects, especially in the short term.
- The 9 EAGLEs which have been confirmed are China, India, Brazil, Indonesia, Korea, Russia, Turkey, Mexico and Taiwan.
- No country from the Nest has managed to reach the status of an EAGLE yet.

As for the Nest, the revision to our forecasts has brought about a number of changes:

- Egypt is now in the Nest, but also Chile and Ukraine. This increases the list of countries to 15 members. The other Nest economies – from larger to smaller - are Thailand, Argentina, Nigeria, Colombia, Poland, Vietnam, Pakistan, Bangladesh, Malaysia, South Africa, the Philippines and Peru.

This second annual report improves our assessment of vulnerabilities by organizing the risks in six different types. The first are growth related, external demand risks and macroeconomic imbalances. The other three are institutional, social and inclusive growth issues.

- All in all, vulnerabilities are generally found to be limited although some warnings can be found.
- Regarding the growth model, fundamentals for productivity gains could be improved in China, India, Indonesia, Mexico and, to a lesser extent in Brazil and Russia. In addition, the labor force is expected to decline in Russia and to grow only marginally in China and Taiwan.
- On external demand risks, Russia, Turkey and Mexico are exposed to low growth in developed economies, while Brazil, Korea and Taiwan rely much more on China. Indonesia, Russia and Brazil are dependent on commodities.
- India and Brazil present disequilibria in both the fiscal and the external front with also a high public debt, while Turkey has a large current account deficit.
- Russia, as well as Asian EAGLEs with relatively low income per capita (China, India and Indonesia) face challenges on the institutional front as well as potential social unrest. Latin American EAGLEs (Brazil and Mexico) could also face potential brakes to growth stemming from low social inclusion. Thanks to a high income per capita (Korea and Taiwan) record a relative favorable situation.

This annual report also concentrates in a number of special issues:

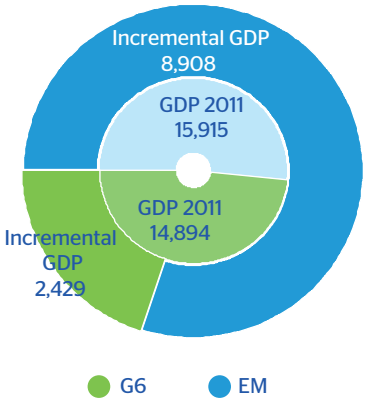
- A new growth-risk pattern is stemming from the crisis, with higher dynamism and less vulnerabilities in emerging economies. Structural twin deficits are concentrated in developed markets, disequilibria that will be corrected at a low pace in the next years.
- The now well known process of shifting wealth from developed to emerging countries is true – in a massive way – for China but not for other EAGLEs. Other than the sheer size, this introduces another key differential characteristic between China and other key emerging economies.
- GCC countries as a block are worth watching since they match the EAGLEs criteria.
- Despite experiencing sound economic progress, Africa is still lagging behind. The only African country in the EAGLEs group, Egypt, has actually fallen from the list and South Africa is still far from getting into the club.

1. The new EAGLEs outlook

In 2011 Emerging Markets outperformed the world economy proving their resilience during the current crisis

World economic growth moderated last year as uncertainty on Europe´s sovereign debt crisis resolution impacted confidence. Industrialized Economies (IE)[1] softened their recovery process initiated in 2010. In spite of the increase in global risk aversion, liquidity tensions and a smaller demand from rich economies, Emerging Markets (EM)[2] maintained a faster growth rate. China kept its role as the economy with the highest contribution to world growth. The EAGLEs countries performance was better than the 45 EM, even after excluding China or the BRIC countries from any of the above group; thus confirming the relevance of this group of economies.

Chart 1
45 EM without BRICs vs G6*: current economic size and incremental GDP 2011-2021 (billion USD, adjusted by PPP)



* G6 Aggregate: Canada, Germany, France, Italy, Japan and the UK
Emerging Markets: other Emerging Markets excluding Brazil, Russia, India and China
Source: BBVA Research and IMF WEO

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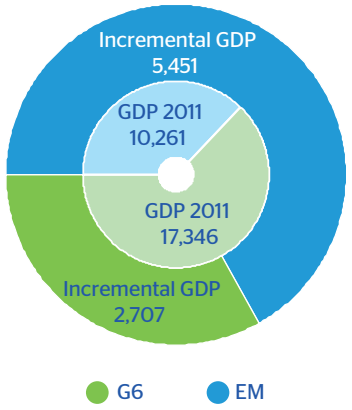
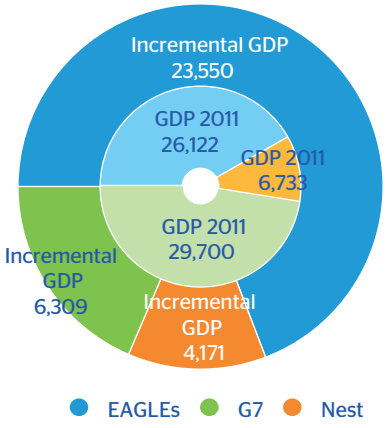
45 EM without BRICs vs G6*:current economic size and incremental GDP 2011-2021 (billion USD)



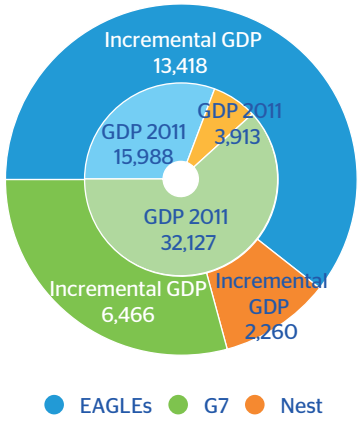
* G6 Aggregate: Canada, Germany, France, Italy, Japan and the UK
Emerging Markets: other Emerging Markets excluding Brazil, Russia, India and China
Source: BBVA Research and IMF WEO

Chart 3
EAGLEs, Nest and G7: current economic size and incremental GDP 2011-2021 (billion USD, adjusted by PPP)



Source: BBVA Research and IMF WEO

Chart 4
EAGLEs, Nest and G7: current economic size and incremental GDP 2011-2021 (billion USD)



Source: BBVA Research and IMF WEO

1: Industrialized economies: Australia, Austria, Belgium, Canada, Cyprus, Denmark, Finland, France, Germany, Greece, Hong Kong, Iceland, Ireland, Israel, Italy, Japan, Luxembourg, Malta, the Netherlands, New Zealand, Norway, Portugal, Singapore, Slovenia, Spain, Sweden, Switzerland, the United Kingdom and the United States.
2: 45 Emerging Markets: Argentina, Bahrain, Bangladesh, Brazil, Bulgaria, Chile, China, Colombia, Czech Rep., Egypt, Estonia, Hungary, India, Indonesia, Iran, Jordan, Korea, Kuwait, Latvia, Lithuania, Malaysia, Mauritius, Mexico, Morocco, Nigeria, Oman, Pakistan, Peru, the Philippines, Poland, Qatar, Romania, Russia, Slovak Rep., South Africa, Sri Lanka, Sudan, Taiwan, Thailand, Tunisia, Turkey, Ukraine, the UAE, Venezuela and Vietnam.

Table 1
Real GDP growth rates adjusted by PPP (%)*

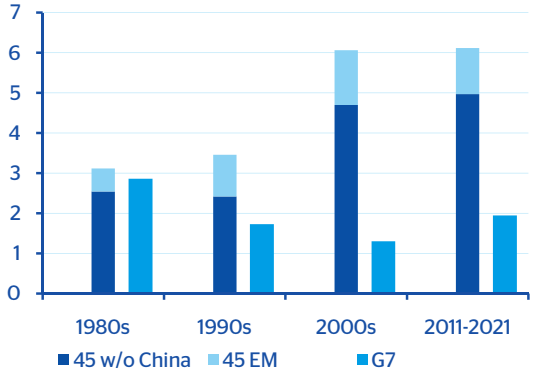
Group	2005	2006	2007	2008	2009	2010	2011
45 EM	7.0	8.4	8.6	5.1	1.2	7.8	6.3
45 EM w/o China	5.8	7.0	6.8	3.8	-1.4	6.6	5.0
45 EM w/o BRICs	5.4	6.5	6.0	3.1	-1.8	6.1	4.8
EAGLEs	7.7	9.0	9.3	5.6	2.2	8.8	7.1
EAGLEs w/o China	6.0	6.9	6.7	3.6	-1.5	7.5	5.4
EAGLEs w/o BRICs	4.9	5.8	4.5	1.4	-3.0	7.9	5.5
Nest	5.2	6.6	6.6	4.3	-0.6	6.3	4.8
BRICs	8.8	10.3	11.1	7.1	4.0	9.3	7.6
BRICs w/o China	6.8	7.8	8.3	5.1	-0.5	7.6	5.5
Industrialized Economies	2.9	3.1	2.3	-0.6	-4.9	3.2	1.6
G7	2.7	2.9	2.0	-0.8	-5.2	3.4	1.5
United States	3.5	2.9	1.7	-0.9	-4.5	3.4	1.9
G6	2.0	2.9	2.3	-0.8	-5.8	3.3	1.1
World	4.0	5.4	5.1	2.1	-2.0	5.4	3.8

*45 EM: Argentina, Bahrain, Bangladesh, Brazil, Bulgaria, Chile, China, Colombia, Czech Rep., Egypt, Estonia, Hungary, India, Indonesia, Iran, Jordan, Korea, Kuwait, Latvia, Lithuania, Malaysia, Mauritius, Mexico, Morocco, Nigeria, Oman, Pakistan, Peru, the Philippines, Poland, Qatar, Romania, Russia, Slovak Rep., South Africa, Sri Lanka, Sudan, Taiwan, Thailand, Tunisia, Turkey, Ukraine, the UAE, Venezuela and Vietnam.
EAGLEs: Brazil, China, India, Indonesia, Korea, Mexico, Russia, Taiwan and Turkey.
BRICs: Brazil, Russia, India and China.
Industrialized Economies: Australia, Austria, Belgium, Canada, Cyprus, Denmark, Finland, France, Germany, Greece, Hong Kong, Iceland, Ireland, Israel, Italy, Japan, Luxembourg, Malta, the Netherlands, New Zealand, Norway, Portugal, Singapore, Slovenia, Spain, Sweden, Switzerland, the United Kingdom and the United States.
G7: Canada, France, Germany, Italy, Japan, the United Kingdom and the United States.
Source: BBVA Research and IMF WEO

The EAGLEs and the Nest: New members show up validating the advantages of a dynamic approach

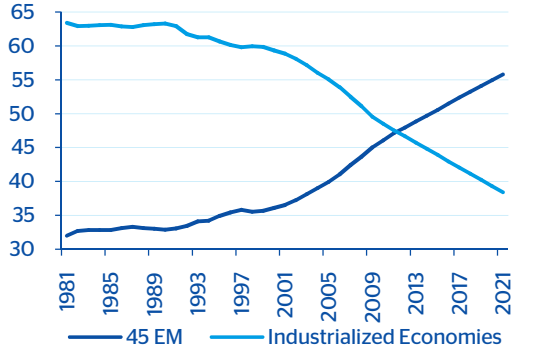
The long term outlook for the world economy is very similar to the one articulated in our previous annual report; it considers a marginal increase in the expected GDP growth rate in the next ten years. The 45 EM will continue driving world economic growth whereas the IE will maintain a slow expansion pace. For the average of the G7, excluding the US, the growth rate forecast remained unchanged whereas for Italy it was marginally revised downwards. These minor changes imply a hardly noticeable increase in the cutoff for becoming an EAGLE but a modest reduction in the threshold for being considered a member of the Nest.

Chart 5
Real GDP growth rates adjusted by PPP (%)



Source: BBVA Research and IMF WEO

Chart 6
Share of World GDP adjusted PPP:
45 Emerging Markets vs Industrialized Economies



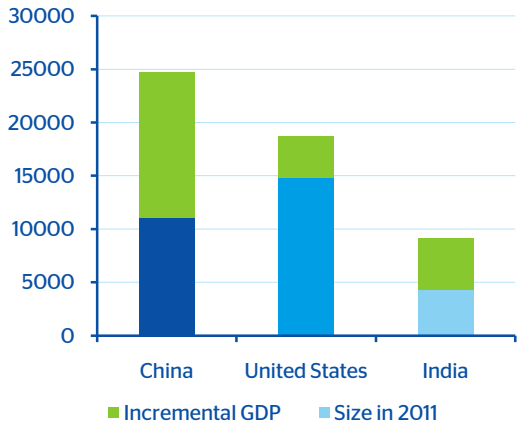
Source: BBVA Research and IMF WEO

The new forecast shows an interesting change in the members of the EAGLEs and also in their contributions within the group. Compared with a year ago, Egypt has become the first "fallen angel". Its forecast for the next ten years has been reduced on average by 0.6 percentage points (pp) given the negative effects in their short run dynamics (2011 and 2012) caused by social unrest during the Arab Spring. Nevertheless, GDP growth is expected to recover towards its long run rate starting from 2013. Given that last year Egypt was slightly above the threshold, the small reduction of its growth outlook was enough to drop it from the EAGLEs league.

Another interesting result is that Iran is meeting the criteria to be considered as an EAGLE. The IMF did a sensitive upward revision to its average growth rate given recent economic reforms cutting subsidies to energy and food prices which are expected to increase the "efficiency and competitiveness of the economy"[3]. Iran's expected incremental GDP is now above the G6 average threshold; however it is not included in the EAGLEs list given the current economic sanctions imposed by the UN. During this year, political tensions may rise if UN resolutions become stricter given the suspicions of nuclear weapons development. The Iranian government has reacted threatening to block the Strait of Hormuz which could have global implications.

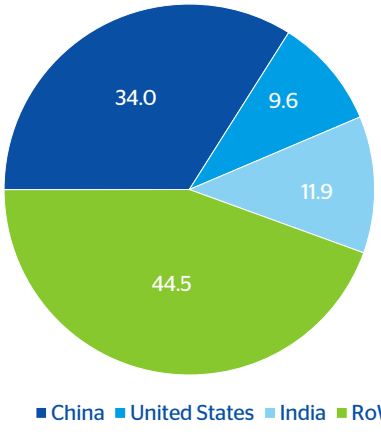
The other EAGLEs members remain but the outlook for India, Russia and Turkey has improved compared to the previous report. In the case of India the forecast was revised upwards due to a shift towards a more investment-led growth pattern, along with productivity gains which are expected to bolster the growth rate towards 8%. As a result, India is expected to have a larger incremental GDP than the US. As for Russia, there is a better short term outlook given a higher forecast for its terms of trade and a higher production of commodities. Nevertheless, its institutional framework and the increase of social unrest are latent risks to the forecast that have to be monitored. Finally, Turkey's forecast has been revised upwards as a faster capital accumulation process and a larger contribution of TFP to long term growth persists.

Chart 7
Global Leaders in the next 10 years: GDP adjusted by PPP (billion USD)



Source: BBVA Research and IMF WEO

Chart 8
Global Leaders in the next 10 years: contribution to World economic growth 2011-2021 (%)

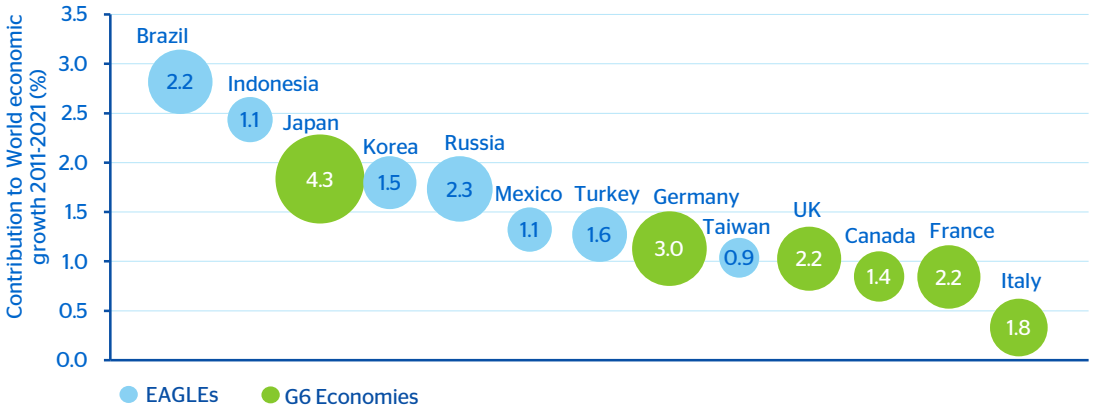


Source: BBVA Research and IMF WEO

The other EAGLEs maintain their relative importance observed in the previous report. Brazil and Indonesia are expected to have a bigger contribution to world growth than Japan, whereas Korea, Russia, Turkey and Mexico could outperform Germany. Finally, we anticipate Taiwan will have a larger incremental GDP than the rest of the G6 economies, including the UK.

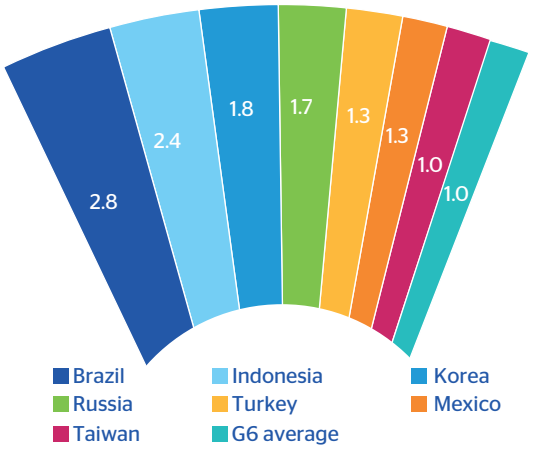
3: Islamic Republic of Iran: 2011 Article IV Consultation - Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Iran. Series: Country Report No. 11/241 August 03, 2011

Chart 9
EAGLEs (excluding China and India)* vs G6 Economies:
current economic size and contribution to World economic growth 2011-2021 (%)**



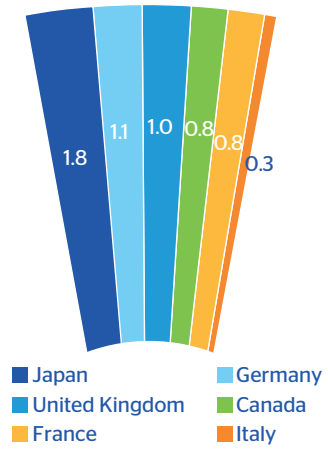
* China and India are off the chart, contributing 34% and 12% with the current size of USD 11 trillion and USD 4.3 trillion respectively.
** Size of the bubble represents the GDP in trillion USD adjusted by PPP in 2011
Source: BBVA Research and IMF WEO

Chart 10
EAGLEs (excluding China and India): contribution to World economic growth 2011-2021 (%)



Source: BBVA Research and IMF WEO

Chart 11
G6 (G7 excluding the US): contribution to World economic growth 2011-2021 (%)



Source: BBVA Research and IMF WEO

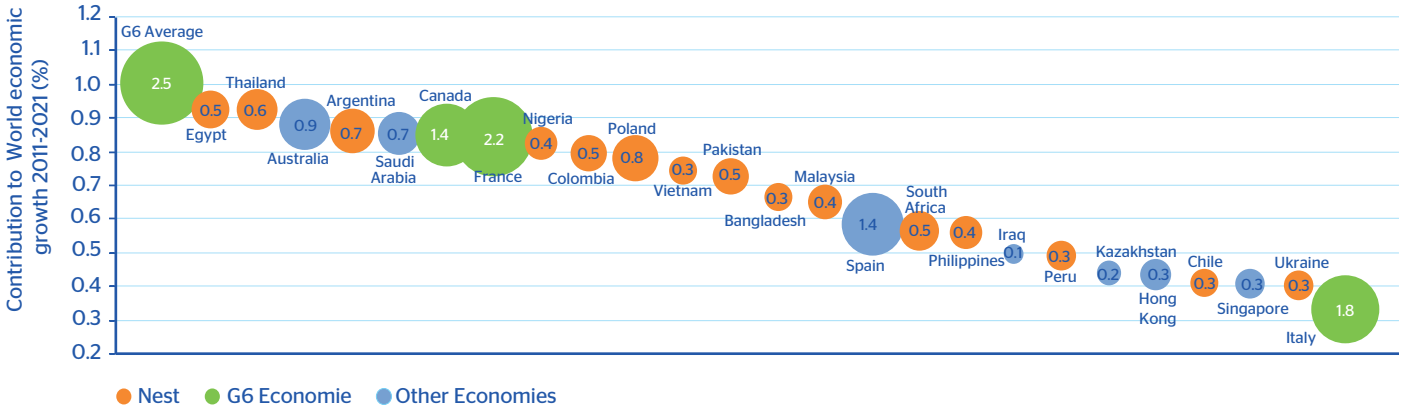
Concerning the Nest, there are three new members, Egypt, Chile and Ukraine; the former relegated from the EAGLEs and the other two advancing from the list of other EM[4]. There has also been a change in the ranking, according to the expected incremental GDP. The outlook for Argentina, the Philippines and Vietnam has been improved markedly, whereas for the case of Peru and South Africa their expected GDP growth rate has been revised downwards. In Argentina's case, the revision is the result of a better than expected performance during 2010 and 2011, and also an anticipated higher capital accumulation process given an improvement in its macroeconomic stability which would foster investors' confidence and cause total factor productivity to soar. The upward revision for the other two Asian economies is explained by an improvement in their macroeconomic policies which should support investment in infrastructure and also an expected process of reallocation of manufacturing from China in the following

4: Saudi Arabia, Iraq and Kazakhstan also meet the threshold criteria to be a member of the Nest. Nevertheless they are excluded since they are considered frontier markets by some investment banks and rating agencies. In the case of Iraq its exclusion also stems from its persistent state of war since 2003.

years. On the other hand, South Africa's forecast reduction by the IMF is explained by two reasons. First of all, a lower demand for its exports (mainly commodities) is expected, given a lower expansion rate of one of its most important trade partners, the European Union. There are also several bottlenecks in the economy which dampen its competitiveness; for instance its labor market regulations maintain a higher unemployment rate, particularly amongst the young population, while it raises real wages[5]. The change in Peru's outlook is also explained by an anticipated loss of momentum of demand for commodities.

Chart 12

Nest, G6 and Other Economies: current economic size and contribution to World economic growth 2011-2021 (%)*



* Size of the bubble represents the GDP in trillion USD adjusted by PPP in 2011
Source: BBVA Research and IMF WEO

The role of the EAGLEs and the Nest in the next ten years

The EAGLEs expected contribution to world economic growth for the next ten years has increased to 58% (compared to 51% a year ago) increasing the relevance of this group of countries. Also the Nest countries are expected to increase their contribution up to 10% (a slight change compared to a year ago). On the other hand, the G7 economies are expected to contribute to the world's incremental GDP less than 16%. BBVA Research anticipates the convergence process between EM and IE will take place during 2012 when considering GDP figures adjusted by PPP.

By regions, world economic growth during the next decade will be concentrated mainly in Emerging Asia, which would be responsible for more than one half. Once again our analysis confirms that this will be the century of Asia and we also expect changes in the balance of global economic power. It is also relevant the increase in incremental GDP by Latin American which will overtake Western Europe in terms of new growth. In addition we envisage a process of strengthening the economic and political ties between China and Latin America, who is not only becoming the most important trade partner but also consolidating Asian giant as the main political influence.

5: South Africa: 2011 Article IV Consultation - Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for South Africa. Series: Country Report No. 11/258 August 25, 2011

Table 2
45 Emerging Markets and G7 Projections

	Country	GDP (billion USD PPP) 2011	2021	Change	Average annual growth (%)
EAGLES	China	11,067	24,785	13,718	8.4
	India	4,314	9,135	4,820	7.8
	Brazil	2,247	3,385	1,137	4.2
	Indonesia	1,100	2,083	983	6.6
	Korea	1,523	2,249	725	4.0
	Russia	2,326	3,026	700	2.7
	Turkey	1,053	1,587	534	4.2
	Mexico	1,628	2,141	514	2.8
	Iran (excluded)	912	1,409	497	4.4
	Taiwan	863	1,281	419	4.0
	G6 average	**2,482**	**2,887**	**405**	**1.5**
Nest	Egypt	506	880	374	5.7
	Thailand	601	974	373	4.9
	Argentina	700	1,048	347	4.1
	Nigeria	407	740	333	6.2
	Colombia	461	783	322	5.4
	Poland	752	1,067	316	3.6
	Vietnam	295	595	300	7.3
	Pakistan	480	774	294	4.9
	Bangladesh	277	545	268	7.0
	Malaysia	436	698	262	4.8
	South Africa	543	772	229	3.6
	Philippines	382	607	225	4.8
	Peru	296	494	198	5.3
	Chile	275	441	165	4.8
	Ukraine	322	485	163	4.2
	G6 minimum	**1,791**	**1,925**	**134**	**0.7**
Groups	EAGLES	26,122	49,672	23,550	6.6
	Nest	6,733	10,904	4,171	4.9
	G6	14,894	17,323	2,429	1.5
	G7	29,700	36,009	6,309	1.9
	World	77,204	117,565	40,361	4.3

	Country	GDP (billion USD PPP) 2011	2021	Change	Average annual growth (%)
Other Emerging Economies	UAE	256	388	131	4.2
	Romania	259	386	126	4.1
	Morocco	160	276	116	5.6
	Qatar	178	286	107	4.8
	Sri Lanka	113	213	100	6.6
	Czech Rep.	268	361	93	3.0
	Kuwait	147	236	88	4.8
	Tunisia	100	186	86	6.4
	Venezuela	366	445	79	2.0
	Hungary	192	261	68	3.1
	Slovak Rep.	125	188	64	4.2
	Sudan	95	149	53	4.5
	Bulgaria	100	145	46	3.8
	Oman	80	115	35	3.7
	Lithuania	60	87	27	3.8
	Jordan	36	56	20	4.5
	Latvia	34	50	16	4.0
	Bahrain	30	46	16	4.3
	Estonia	26	39	12	3.9
	Mauritius	19	29	10	4.5
G7	United States	14,806	18,687	3,881	2.4
	Japan	4,311	5,052	741	1.6
	Germany	3,039	3,495	456	1.4
	UK	2,213	2,628	415	1.7
*G6	Canada	1,367	1,710	343	2.3
	France	2,173	2,513	341	1.5
	Italy	1,791	1,925	134	0.7

*G6 = G7 - US
Source: BBVA Research and IMF WEO

Table 3

Contribution to World economic growth (%)

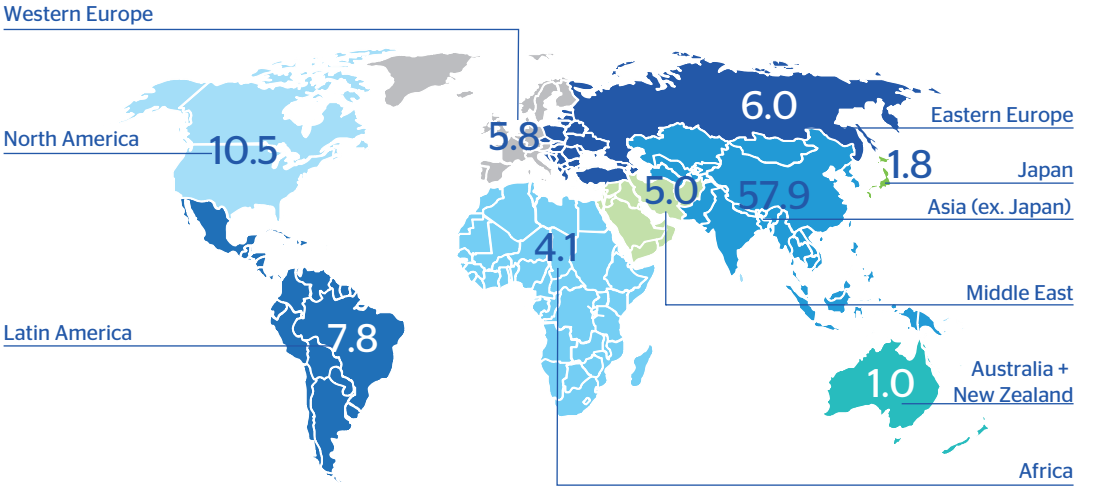
Ranking 2011	Country	Contribution 2011-2021	Ranking 2010	Country	Contribution 2010-2020	Change in ranking
1	China	34.0	1	China	30.2	0
2	India	11.94	3	India	8.55	1
3	United States	9.61	2	United States	8.66	-1
4	Brazil	2.82	4	Brazil	2.68	0
5	Indonesia	2.44	5	Indonesia	2.26	0
6	Japan	1.83	7	Japan	1.74	1
7	Korea	1.80	6	Korea	1.77	-1
8	Russia	1.73	8	Russia	1.42	0
9	Turkey	1.32	14	Turkey	0.99	5
10	Mexico	1.27	9	Mexico	1.20	-1
11	Iran	1.23	22	Iran	0.70	11
12	Germany	1.13	10	Germany	1.05	-2
13	Taiwan	1.04	12	Taiwan	0.99	-1
14	United Kingdom	1.03	13	United Kingdom	0.99	-1
15	Egypt	0.93	11	Egypt	1.00	-4
16	Thailand	0.92	15	Thailand	0.89	-1
17	Australia	0.89	18	Australia	0.82	1
18	Argentina	0.86	30	Argentina	0.58	12
19	Saudi Arabia	0.85	16	Saudi Arabia	0.85	-3
20	Canada	0.85	17	Canada	0.83	-3
21	France	0.84	19	France	0.78	-2
22	Nigeria	0.83	20	Nigeria	0.77	-2
23	Colombia	0.80	24	Colombia	0.67	1
24	Poland	0.78	21	Poland	0.72	-3
25	Vietnam	0.74	27	Vietnam	0.62	2
26	Pakistan	0.73	28	Pakistan	0.60	2
27	Bangladesh	0.66	29	Bangladesh	0.59	2
28	Malaysia	0.65	26	Malaysia	0.64	-2
29	Spain	0.58	23	Spain	0.70	-6
30	South Africa	0.57	25	South Africa	0.66	-5
31	Philippines	0.56	33	Philippines	0.42	2
32	Iraq	0.50	32	Iraq	0.47	0
33	Peru	0.49	31	Peru	0.49	-2
34	Kazakhstan	0.44	35	Kazakhstan	0.39	1
35	Hong Kong	0.44	34	Hong Kong	0.41	-1
36	Chile	0.41	37	Chile	0.37	1
37	Singapore	0.41	39	Singapore	0.35	2
38	Ukraine	0.40	38	Ukraine	0.37	0
39	Italy	0.33	36	Italy	0.37	-3

Legend

- EAGLEs
- Nest
- G7
- Other Economies
- Other EM (not a member of EAGLEs/Nest)
- Excluded

Source: BBVA Research and IMF WEO

Chart 13
Contribution to World economic growth by region between 2011-2021 (%)



Source: BBVA Research and IMF WEO

Box A. Forecasting Methodology

The forecasting methodology used in this project is a combination of short, medium, and long term macroeconomic estimations. Data used in this report has been obtained through analysis done by BBVA Research, which has a presence in many major economies around the world. Analysis of any remaining economies not done by BBVA Research has been contributed by the IMF, which publishes its forecasts semi-annually in its World Economic Outlook. Short and medium term forecasts for the next five years include macroeconomic indicators such as: GDP, inflation, current account and fiscal balances for 184 economies. In conjunction with the data collected by both BBVA Research and the IMF, the long term forecast (for the next ten years) can be derived through combining short and medium term data along with long term potential growth estimations[6].

Box B. Our sample: 45 emerging markets

Semantics: there is no a clear and/or commonly agreed definition, of what exactly constitutes an emerging market[7]. According to BBVA Research terminology, an emerging economy is a nation with high growth expectations and ongoing industrialization process. Its starting point in terms of its level of economic development, income per capita should be lower compared with developed economies; hence they are undergoing a process of convergence towards developing a market-oriented economy. From the point of view of investors, such markets offer great potential investment opportunities but are mostly with a much higher level of risk associated with a weaker institutional framework; however the expected returns of investment are higher than that of developed economies. Nevertheless, their capital markets should offer a minimum set of characteristics such that they are attractive enough for investors; for instance there must be information available about the institutional framework, liquidity and turnover ratios and also equity and bond indexes to track. They should also be clear of any international sanctions to foreign investors imposed by world organizations like the UN, hence excluding countries like Iran.

Currently, BBVA Research has identified 45 Emerging Markets (EM)[8] based on the above principles. These are Argentina, Bahrain, Bangladesh, Brazil, Bulgaria, Chile, China, Colombia, Czech Rep., Egypt, Estonia, Hungary, India, Indonesia, Iran, Jordan, Korea, Kuwait, Latvia, Lithuania, Malaysia, Mauritius, Mexico, Morocco, Nigeria, Oman, Pakistan, Peru, the Philippines, Poland, Qatar, Romania, Russia, Slovak Rep., South Africa, Sri Lanka, Sudan, Taiwan, Thailand, Tunisia, Turkey, Ukraine, the UAE, Venezuela and Vietnam.

Noteworthy is the fact that all the members of the group are subject to a revision as some of them may develop enough to be categorized as developed economies. The reverse may apply when an emerging (or developed) economy could lose its status if its growing prospects worsen sufficiently enough to be dropped from the group if they do not fulfill the required conditions.

In order to narrow the broad number of countries and help investors to concentrate their interests on the key EM, BBVA Research introduced a key list of 24 economies, namely the EAGLEs and the Nest (up from 22 economies in 2010) which are worth watching.

It is important to stress that, when updating the calculations and forecasts to determine the EAGLEs and the Nest members, a sample of 184 countries is considered, including other industrialized economies beyond the G7, frontier markets and other economies with lower income or weaker institutional framework.

6: For a detailed explanation of the potential growth model, please refer to the first issue of the EAGLEs Outlook titled: "Who are the EAGLEs? Driving Global Growth for the Next Ten Years"; 14th February 2011, BBVA Research
7: Ashoka Mody: "What Is an Emerging Market?"; IMF Working Paper, WP/04/177, September 2004.
8: 45 emerging markets: BBVA Research extended its emerging markets selecting process to other definitions offered by other major "think tanks" such as: Goldman Sachs, FTSE, MSCI, S&P, Dow Jones, The Economist, etc.

Annex

Table 4
Real GDP growth rates adjusted by PPP (%)

Country	Forecast Jan 2012	Forecast Nov 2010	Difference
EAGLEs + Nest	**Average annual growth 2011-2021**	**Average annual growth 2010-2020**	
Argentina	4.1	3.3	0.79
Bangladesh	7.0	6.9	0.08
Brazil	4.2	4.2	-0.05
Chile	4.8	4.8	0.02
China	8.4	8.4	-0.05
Colombia	5.4	5.2	0.28
Egypt	5.7	6.3	-0.57
India	7.8	6.6	1.21
Indonesia	6.6	6.7	-0.13
Iran	4.4	3.1	1.37
Korea	4.0	4.2	-0.22
Lithuania	3.8	3.4	0.34
Malaysia	4.8	5.1	-0.32
Mexico	2.8	2.8	-0.07
Nigeria	6.2	6.4	-0.26
Pakistan	4.9	4.4	0.51
Peru	5.3	5.7	-0.47
Philippines	4.8	4.1	0.62
Poland	3.6	3.6	-0.01
Russia	2.7	2.4	0.27
South Africa	3.6	4.3	-0.75
Taiwan	4.0	4.2	-0.18
Thailand	4.9	5.1	-0.10
Turkey	4.2	3.7	0.54
Ukraine	4.2	4.2	-0.01
Venezuela	2.0	1.1	0.87
Vietnam	7.3	6.9	0.41
G7	**Average annual growth 2011-2021**	**Average annual growth 2010-2020**	**Difference**
Canada	2.3	2.3	-0.09
France	1.5	1.4	0.04
Germany	1.4	1.4	0.00
Italy	0.7	0.8	-0.11
Japan	1.6	1.6	0.03
United Kingdom	1.7	1.8	-0.02
United States	2.4	2.2	0.12
Group	**Average annual growth 2011-2021**	**Average annual growth 2010-2020**	**Difference**
EAGLEs	6.6	6.4	0.24
Nest	4.9	4.9	0.01
45 EM	6.1	5.9	0.20
G7	1.9	1.9	0.06
G6	1.5	1.5	-0.01
Industrialized Economies	2.0	2.0	0.02
GCC	4.4	5.1	-0.71
World	4.3	4.1	0.16

Source: BBVA Research and IMF WEO

Table 5
Ranking comparing GDP in USD adjusted by PPP vs GDP in USD

	Country	Ranking GDP PPP in USD	Ranking GDP in USD	Change
EAGLEs	China	1	1	0
	India	2	2	0
	Brazil	3	3	0
	Indonesia	4	4	0
	Korea	5	5	0
	Russia	6	6	0
	Turkey	7	7	0
	Mexico	8	8	0
	Taiwan	9	9	0
Nest	Egypt	10	15	-5
	Thailand	11	12	-1
	Argentina	12	13	-1
	Nigeria	13	14	-1
	Colombia	14	10	4
	Poland	15	11	4
	Vietnam	16	21	-5
	Pakistan	17	22	-5
	Bangladesh	18	24	-6
	Malaysia	19	18	1
	South Africa	20	17	3
	Philippines	21	20	1
	Peru	22	23	-1
	Chile	23	19	4
	Ukraine	24	28	-4

Source: BBVA Research and IMF WEO

2. The map of risks to our outlook

Projections presented in the first section correspond to our baseline scenario for both the short-term horizon (cyclical and policy-driven dynamics) and the long-term perspective (potential growth) for the next decade. However, several factors could eventually affect these numbers, so it is of great interest to test how optimistic forecasts could be for this period, according to macroeconomic risks and potential brakes to growth. It is important to highlight that the following analysis is developed on relative terms, in the sense that comparisons are made on a cross-country basis within the 45 EM considered in this report and conclusions are based on upward or downward deviations from our baseline assumptions. Furthermore, no probability distribution is considered or assessed.

The relevance of certain deviations from the baseline scenario is shown by a simple computing exercise. If performance of other economies remains unchanged, we estimate what annual growth rate is required in the next 10 years for each country to change membership from its current group to the adjacent one. That is, from being an EAGLE to a Nest economy or vice versa. According to this exercise, Taiwan is the country with the highest membership sensitivity to adverse shocks, as a downward revision of only 0.1 percentage points in its annual average growth would imply that it would no longer be considered an EAGLE. Larger deviations are needed for the rest of the EAGLEs, especially in the case of the top four (China, India, Brazil and Indonesia). Among the Nest, Egypt could become an EAGLE again if it is able to accelerate annual growth by 0.4 percentage points, while Thailand could reach that group with 0.3 more, needing more positive shocks in the cases of Argentina, Poland, Nigeria and Colombia.

Table 6

Robustness exercise:
How much less/more growth is needed for an EAGLE /Nest to end up in the Nest/EAGLE group

		Average annual growth in the next 10 years		
		Baseline scenario	**To become a Nest...**	**Difference**
EAGLEs	China	8.4	0.4	-8.0
	India	7.8	0.9	-6.9
	Brazil	4.2	1.7	-2.5
	Indonesia	6.6	3.2	-3.4
	Korea	4.0	2.4	-1.6
	Russia	2.7	1.6	-1.0
	Turkey	4.2	3.3	-0.9
	Mexico	2.8	2.2	-0.5
	Taiwan	4.0	3.9	-0.1
		Baseline scenario	**To become an EAGLE...**	**Difference**
Nest	Egypt	5.7	6.1	0.4
	Thailand	4.9	5.3	0.3
	Argentina	4.1	4.7	0.6
	Nigeria	6.2	7.1	1.0
	Colombia	5.4	6.5	1.1
	Poland	3.6	4.4	0.8
	Vietnam	7.3	9.0	1.8
	Pakistan	4.9	6.3	1.4
	Bangladesh	7.0	9.4	2.4
	Malaysia	4.8	6.8	2.0
	South Africa	3.6	5.7	2.1
	Philippines	4.8	7.5	2.7
	Peru	5.3	9.0	3.7
	Chile	4.8	9.5	4.6
	Ukraine	4.2	8.5	4.3

Source: BBVA Research and IMF WEO

Macroeconomic risks

Three dimensions of risks are considered here: growth model risks, external demand risks and macro disequilibria.

Growth model risks are related to uncertainty about production factors and productivity (the components of our potential growth models). For this we check the following indicators:

- Growth acceleration: it represents a simple approach to forecast optimism, comparing expected growth for the next decade with pre-crisis performance.
- Expected labor force growth: countries around the world are in different stages of demographic transition, conditioning workers availability at the labor market.
- Expected labor force productivity growth: if it is expected to be very high it implies that activity growth will be very capital demanding, needing more financial deepening, and also requires total factor productivity (TFP) to largely increase.
- Quality of infrastructure: this is a key element for domestic and external trade, also affecting TFP.
- R&D expenditure and tertiary education enrolment: these are two of the main factors explaining TFP dynamics and cross-section divergence.

External demand risks cover both the relevance of the external sector for the economy and the concentration of exposure to certain products and markets:

- Trade openness: the ratio between exports and imports to GDP represent risks to a global slowdown.
- Expected trade partners' growth: it focuses on the risks of economic slump in the main trade partners.
- Exports share to China: it particularly captures which countries would be most affected in case of an idiosyncratic shock to the Chinese economy.
- Exports share of commodities: higher ratios imply a larger sensitivity to commodity market dynamics, impacting the current account balance and in some cases the fiscal position

Finally, macro disequilibria describe risks of adjustments stemming from either external or fiscal imbalances (in the case of both we talk about 'twin deficits'), with implications for both domestic and foreign agents behaviour. We focus on flows and stocks disequilibria:

- Flow: expected fiscal and current account balance
- Stock: actual public and external debt-to-GDP ratio

EAGLEs assessment on macroeconomic risks

Overall, EAGLEs present on-average growth risks, with Korea recording the best relative assessment, followed by China and Turkey, while Indonesia, India and Brazil are slightly below average.

Korea shows better fundamentals for TFP growth (infrastructure, R&D expenditure and tertiary education enrolment), a higher expected growth for trade partners (mainly located in growth-leading Asia) and a expected fiscal surplus, offsetting risks stemming mainly from China dependency (25% of exports).

Strong fundamentals for China are concentrated in low macro disequilibria, very low dependency on commodity exports, relatively low trade openness (slightly above 50% of GDP in comparison with 75% for the 45 EM average and with an increasing domestic demand reliance) and R&D expenditure doubling the average (1.4% of GDP). However, some potential weaknesses could emerge from its growth model, particularly from the expected low growth of the labor force (only a 1.9% in the following decade according to UN estimations), making dynamism more reliant on capital accumulation and TFP gains. In this sense, improvements have to be made in tertiary education enrolment.

Turkey shares with China a very low dependency on commodity exports and not very high trade openness (even lower, with around a 40%). It also benefits from relatively good infrastructure (a score of 5 out of 7 according to the World Economic Forum indicator). Concerns are focused in this case on the growth of trade partners, given its external reliance on European demand, as well as on the large current account deficit (expected to average 6.9% of GDP in the 2012-2016 according to IMF estimations).

Mexico, Taiwan and Russia are on the 45 EM average, although with a slightly positive bias.

Regarding exposure to external risks, Mexico shows a very low China dependency (less than 2% of total exports) and a relatively moderate commodity exports dependency (23%, the half of the 45 EM average), although the country's large reliance on the US market conditions a low growth of trade partners. On the positive side, the macroeconomic imbalances are relatively low (with a very low external debt ratio of 19%, half again of the average). However, one of the big challenges is to strengthen factors leading to TFP gains, such as R&D expenditure (0.4% of GDP in 2010 according to WB statistics) and tertiary education enrolment (27% in comparison with a 40% average).

The assessment of Taiwan is very much alike the one for Korea, applied in this case to a smaller economy. In addition to sluggish population dynamics, it shows a high dependency on Chinese demand (28% of total exports), to which it has to add high trade openness (over 120% of GDP), although benefiting from significant trade partners' growth (mainly Asian countries). On the positive side, it lacks macro imbalances and, as in the case of Korea, it presents very good fundamentals for TFP gains.

Russia faces the biggest challenges on the growth model side. From the domestic perspective, it lags behind in terms of infrastructure (rated less than 4 out of 7 in the WEF indicator) and a decline in the labor force is expected over the next decade. Regarding risks on the external side, its reliance on European demand conditions a low expected growth of trade partners and it also concentrates a very large share of exports in commodities (more than a 75%). But good news is also present for Russia's outlook, such as a good base for TFP increases stemming from R&D expenditure and tertiary education enrolment (more than a 75%, only being surpassed by Korea among the EAGLEs) and the absence of macro disequilibria, both in terms of flows and stocks.

Indonesia, India and Brazil show indicators slightly below average.

Indonesia is the only EAGLE that is expected to accelerate growth in the next decade (2011-2021) in comparison to the pre-crisis period (2002-2007), having a potential optimistic forecast bias. Productivity becomes the main concern, as, according to forecasts, it will have a very relevant role in this growth acceleration and all fundamentals for TFP gains are below average (low quality of infrastructure, marginal R&D expenditure and low tertiary education enrolment). On the external side, a relatively high commodity dependency (over 60% of total exports) poses some risks, although the potential impact on the domestic economy is not that large (trade openness is around 40% of GDP) and should benefit from larger trade partners' growth. Finally, macroeconomic imbalances will remain in the low range.

India and Brazil are the EAGLEs with the worst outlook in terms of macro disequilibria, both having high public debt ratios (both over 60% of GDP) and with projections for the next decade of current account deficit (in the 2-3% of GDP range) and fiscal deficit (much larger in the case of India, around 7% in comparison with 2-3% in Brazil). They also share a low quality of infrastructure (a score below 4 out of 7), although Brazil should benefit from hosting big sports events in 2014 and 2016. On the positive side, they have both low external debt ratios, and domestic demand is less exposed to global demand shocks (trade openness below 20% in Brazil and slightly above 30% in India).

In India, a positive performance In the labor force force is challenged by productivity drivers, as infrastructure shortages and low tertiary education enrolment (16%, the lowest ratio for the EAGLEs). In the case of Brazil, main risks stems from the external side, with a high China and commodity exports dependency (16% and 62% of total exports respectively, in comparison with the averages of the 45 EM of 7% and 45%).

Table 7

Macroeconomic risks indicators*

	Dimension	A.Growth model risks						B.External demand risks				C.Macro disequilibria			
								Relevance		Diversification		Flows		Stocks	
	Variable	Growth acceleration	Expected labour force growth	Expected labour force productivity growth	Quality of overall infrastructure	R&D expenditure	Tertiary education enrolment	Trade openness	Expected trade partners growth	China exports dependency	Commodity exports dependency	Expected fiscal balance	Expected external balance	Public debt	External debt
	Definition	Diff. in average annual growth between 2011-21 and 2002-07	Total change in % (next 10 years)	Average annual growth of GDP to labour force (next 10 years)	Score between 1 and 7 (2011)	Expenditure as a % of GDP (last year available)	In % (last year available)	The sum of exports and imports as a % of GDP (2010)	Trade-weighted average annual growth (next 10 years)	As a % of total exports (2010)	As a % of total exports (2010)	Annual average (next 5 years)	Annual average (next 5 years)	As a % of GDP (2010)	As a % of GDP (2010)
	Source	BBVA Research, IMF	UN	BBVA Research, UN, IMF	WEF	WB (World Development Indicators)	WB (World Development Indicators)	WTO, IMF	BBVA Research, IMF	UN (COMTRADE)	WTO	IMF	IMF	IMF	WB (World Development Indicators), IMF
EAGLEs	China	-3.4	1.9	8.3	4.1	1.4	24.3	50.6	3.6	NA	6.3	-0.1	6.5	33.8	9.3
	India	-1.4	16.9	6.1	3.6	0.8	16.2	33.5	4.0	7.9	35.5	-7.1	-2.3	64.1	17.8
	Brazil	0.0	11.3	3.0	3.8	1.1	36.1	18.8	4.1	15.6	61.9	-2.5	-3.0	66.8	16.6
	Indonesia	0.9	12.9	5.3	3.7	0.0	22.4	41.0	4.5	9.9	62.2	-1.2	-0.9	27.4	25.3
	Korea	-0.9	8.5	3.1	6.0	3.2	103.9	87.9	4.7	25.1	11.1	2.7	1.2	33.4	NA
	Russia	-5.2	-7.7	3.8	3.6	1.0	75.9	43.8	3.4	5.1	75.7	-3.1	1.4	11.7	26.0
	Turkey	-3.8	13.2	3.3	5.1	0.7	45.8	40.7	3.2	2.0	19.0	-1.0	-6.9	42.2	40.0
	Mexico	-1.0	14.7	1.5	3.9	0.4	27.0	58.9	2.6	1.4	23.0	-2.4	-0.9	42.9	19.3
	Taiwan	-1.5	NA	NA	5.9	2.3	NA	122.3	5.0	28.0	NA	-1.6	9.7	38.6	NA
Nest	Egypt	0.3	19.1	3.4	4.3	0.2	30.4	36.3	3.7	1.6	53.9	-7.2	-2.1	73.8	15.9
	Thailand	-1.0	4.2	4.2	4.9	0.2	46.2	118.4	4.4	11.0	24.2	-3.1	1.1	44.1	22.3
	Argentina	-5.0	9.2	3.6	3.5	0.5	68.7	33.7	4.1	8.5	62.3	-1.1	-1.1	49.1	34.6
	Nigeria	-1.2	30.3	3.5	2.4	NA	10.3	62.3	3.4	1.7	92.9	0.9	8.2	17.3	3.9
	Colombia	-0.3	14.6	4.0	3.6	0.2	39.1	27.8	3.3	4.9	72.7	-1.1	-2.2	36.0	21.8
	Poland	-1.9	-7.5	4.4	3.4	0.6	70.5	70.2	2.3	1.0	20.7	-3.1	-5.2	55.0	NA
	Vietnam	-1.1	10.0	6.1	3.0	0.2	22.3	151.6	4.0	9.5	30.5	-3.3	-2.7	52.8	33.9
	Pakistan	-1.3	24.9	2.4	3.5	0.7	5.4	34.2	3.8	6.7	25.5	-4.5	-2.5	56.8	32.1
	Bangladesh	0.4	21.9	4.8	2.7	NA	10.6	44.5	2.6	1.3	6.6	-4.2	-0.7	NA	23.6
	Malaysia	-1.5	19.2	3.0	5.5	0.6	37.5	152.8	4.5	12.6	32.3	-4.6	9.6	54.2	34.2
	South Africa	-1.8	6.3	2.9	4.6	0.9	15.0	48.4	4.0	11.4	46.9	-2.6	-4.9	33.8	12.4
	Philippines	-1.0	22.8	2.5	3.2	0.1	28.9	55.0	4.0	11.1	14.2	-2.1	1.3	44.7	36.2
	Peru	-1.5	15.8	3.9	3.6	0.1	35.0	42.7	3.7	15.5	66.2	1.5	-2.7	24.5	23.6
	Chile	-0.3	7.6	4.2	5.7	0.7	59.2	63.9	4.4	24.6	86.0	1.3	-1.9	9.2	42.5
	Ukraine	-3.9	-9.7	5.3	4.1	0.9	79.5	81.5	3.9	2.6	35.6	-2.0	-4.5	40.1	84.7
	Graduation	Above average	On average	Below average											

* A figure is considered to be above average (below) when its value is equal or larger (smaller) than the average for 45 Emerging Markets plus (minus) 0.5 standard deviations
Source: BBVA Research, IMF, United Nations (UN), World Economic Forum (WEF), World Bank (WB) and World Trade Organization (WTO)

Nest countries assessment on macroeconomic risks

With the exception of Vietnam, all the Nest countries are much in line with average for aggregate macroeconomic risks.

Relative to the growth model risks, Egypt (formerly an EAGLE) and Bangladesh are the only countries for which GDP increases in the next decade are expected to be higher than in the pre-crisis period, although marginally. The labor forces are expected to shrink in Poland and Ukraine (a new Nest country this year), while labor productivity should increase largely in Vietnam, Bangladesh and Ukraine to reach GDP forecasts. It will be challenging in Vietnam and Bangladesh as TFP fundamentals underperform, as it happens in Nigeria. Both infrastructure and R&D are also lagging in Colombia, the Philippines and Peru, infrastructure and tertiary education enrolment in Pakistan, while another group presents shortages in one of the three categories (Argentina and Poland in infrastructure, although they both outperform in tertiary education enrolment, Thailand and Egypt in R&D expenditure, and South Africa in tertiary education enrolment). Chile is definitively the best positioned in terms of TFP fundamentals.

Regarding the external demand risks, Thailand, Malaysia and Vietnam are the most open economies (close to 120% of GDP in the first case and around 150% in the other two), while Argentina, Colombia, Egypt and Pakistan are the closest ones (less than 40% of GDP). In terms of expected trade partners' growth, the lowest figures correspond to Poland (exposed to Europe) and Bangladesh (with the lowest share of exports to China). With respect to diversification measures, Chile (a new Nest country this year) and Peru are the only countries with exposure to China (15% and 25% respectively), and their commodity exports dependency is high (66% in the case of Peru and 86% for Chile), as it happens in Argentina, Nigeria and Colombia (62%, 93% and 73% respectively).

Finally, regarding macroeconomic disequilibria, Egypt, Pakistan, Malaysia and Bangladesh show the largest risks on the fiscal front, expecting fiscal deficits in the following five years (over 7% of GDP in the first case and in the 4-5% for the other three) and having today a high debt-to-GDP ratios (74% in Egypt). The same happens on the external front for Ukraine, with expected large current account deficits (4-5%) and a high external debt-to-GDP ratio (85%). Poland, South Africa and Bangladesh are also expected to have significant external imbalances, but external debt is not such a concern for the last two. Chile, Peru and Nigeria will present the lowest macro imbalances (with expected fiscal surplus and public debt below 25% in all cases and with a large external surplus and very low external debt in the case of Nigeria).

Potential brakes to growth

Beyond macroeconomic risks, other factors must be considered to draw potential deviations from the baseline scenario. Here we analyze three dimensions of what we call potential brakes to growth: institutional factors, social unrest risks and the challenge of inclusive growth.

Regarding institutional factors, we differentiate those indicators more related to business obstacles from state fragility, which at some point could cause a disruption in economic activity. In the case of the former, we include both from a market and a public perspective, through investment climate and governance indicators respectively.

Social unrest risks have very much to do with growth as the Arab Spring is showing. Social unrest can impact economic performance (business disruption and distrust) and policy decisions (such as the increase or/and extension of subsidies). Events in the MENA countries are rooted in a combination of high youth unemployment rates, rising food prices, income inequality and lack of democracy and civil liberties. Here we include food dependency, measured by imports share and the weight in the consumption basket, and the labor market situation in terms of unemployment rate (with a mention to youth unemployment rate when available) and education (secondary enrolment), as proxies of these social unrest risks.

Finally, inclusive growth considerations are focused on concerns of whether economic dynamism is being unevenly shared by population. Here we present two indicators of this challenge: the GINI index and the share of population below the poverty line.

EAGLEs assessment on potential brakes to growth

In contrary to economic risks, variability among EAGLEs is larger in the case of potential brakes to growth. Korea and Taiwan remain on the positive side, while India, Indonesia and Russia are slightly worse than average.

Korea and Taiwan present the best assessment in the case of institutional factors, from a market and a public perspective. As the stage of development is relatively advanced among the EAGLEs (with a GDP per capita doubling the one of Russia, the next on the ranking), both countries present low food dependency (around 2% of total imports and a weight in the CPI basket lower than 15% in Korea and around 25% in Taiwan, in comparison with a 45 EM average above 30%). Unemployment rates are also low (in the 3-5% range). Finally, the Gini index is the lowest among EAGLEs, slightly above 30% in both cases, almost 10 points lower than the 45 EM average.

Mexico, Brazil, China and Turkey are around average when considering an aggregate view, but some deviations deserve to be mentioned. This is the case of Brazil and Mexico, both showing low social unrest risks stemming either from food dependency (weight in the CPI basket is around 20% in both cases) or from the labor market (relatively low unemployment rate in Mexico and above average secondary education enrolment in Brazil). However, this is partially offset by the challenge coming from inclusive growth. Despite recent improvements, both countries still present the most uneven income distribution among the EAGLEs (a Gini index above 50%, 10 points higher than the 45 EM average) and a very high share of population living under the poverty line (especially in Mexico). In Brazil, the investment climate could also be improved further, according to the WB 2012 Doing Business indicators.

China lags in terms of institutional factors, it presents a high sensitivity of population to food price shocks (a weight in the CPI basket close to 40%) and uneven income distribution (Gini index of 45%). In Turkey, one of the challenges lies in the labor market situation, with the highest unemployment rate among the EAGLEs (above 10%), affecting especially young people (25%, higher than the 20% 45 EM average).

Finally, India, Indonesia and Russia show potential brakes to growth slightly above average. In the three cases, institutional shortages concentrate the explanatory power, especially on the investment climate side, governance and long-term state concerns. Social unrest risks are also a source of concern, with the three countries having, as low per capita income countries, a share of food in the CPI above average (close to 40% in Russia and in the 45-50% range in the other two countries), with both total and youth unemployment rates in line with the high average for Russia and Indonesia (around 8% and 20% respectively) and above average for the aggregate in India (more than 10%). This is reinforced by the fact that India and Indonesia present the lowest secondary education enrolment among the EAGLEs (60% and 75% respectively, below the 45 EM average of 84%).. In terms of inclusive growth, income distribution is not especially relevant (with a Gini index around average in all cases), although poverty is relatively high in Indonesia, Russia and India.

Table 8

Potential brakes to growth indicators*

	Dimension	A.Institutional factors			B.Social unrest risks					C.Inclusive growth challenge	
		Market	Public		Food prices		Labour market				
	Variable	Investment climate	Governance	State fragility	Food imports dependency	Food in the consumption basket	Unemployment rate	Youth unemployment rate	Secondary education enrolment	Income inequality	Poverty
	Definition	Average world ranking for 10 indicators between 1 and 183 (2012)	Average of 6 indicators between-2.5 and +2.5 (2010)	General index between 0 and 25 (2010)	As a % of GDP (2010)	As a % (last year available)	As a % of active population (last year available)	As a % of active population (last year available)	In % (last year available)	GINI index (last year available)	% of population below the poverty line (last year available)
	Source	WB (Doing Business)	WB (Worldwide Governance Indicators)	CSP	WTO, IMF	FAO, national statistics	ILO, national statistics	ILO, national statistics	WB (World Development Indicators)	WB (World Development Indicators), UNU-WIDER	WB (World Development Indicators)
EAGLEs	China	92	-0.6	9	1.0	39.8	4.3	NA	80.1	44.9	NA
	India	119	-0.3	13	0.7	49.7	10.8	NA	60.2	36.8	NA
	Brazil	111	0.1	6	0.4	22.3	8.3	17.8	101.3	53.9	21.4
	Indonesia	113	-0.5	10	1.6	45.4	7.9	22.2	75.1	36.8	13.3
	Korea	28	0.7	0	1.9	14.0	3.6	9.8	97.1	31.6	NA
	Russia	106	-0.7	7	2.3	38.7	8.2	18.3	88.6	42.3	11.1
	Turkey	81	-0.1	10	1.0	27.9	14.0	25.3	77.6	39.8	18.1
	Mexico	76	-0.2	4	1.9	18.9	5.2	10.0	86.9	51.7	47.4
	Taiwan	48	1.0	0	2.2	25.9	5.2	NA	NA	33.9	NA
Nest	Egypt	102	-0.6	13	4.6	42.1	9.4	NA	84.7	34.4	22.0
	Thailand	40	-0.3	7	2.7	33.0	1.2	4.3	77.2	42.0	8.1
	Argentina	107	-0.3	1	0.4	36.2	8.6	21.2	85.8	45.8	NA
	Nigeria	118	-1.2	17	2.2	59.4	21.1	NA	44.0	43.7	NA
	Colombia	69	-0.3	12	1.4	29.5	12.0	23.0	96.4	58.5	37.2
	Poland	82	0.8	0	2.8	24.9	8.2	20.7	97.0	34.2	NA
	Vietnam	93	-0.5	8	5.5	41.6	2.4	NA	77.2	37.6	14.5
	Pakistan	104	-1.1	15	2.8	34.8	5.0	7.7	34.2	32.7	22.3
	Bangladesh	113	-0.9	12	4.6	53.8	5.1	NA	49.3	33.2	NA
	Malaysia	43	0.3	5	5.4	31.4	3.7	10.9	69.1	46.2	3.8
	South Africa	63	0.2	8	1.3	18.3	23.8	48.2	93.8	67.4	23.0
	Philippines	115	-0.6	11	3.2	39.0	7.5	17.4	84.8	44.0	26.5
	Peru	65	-0.2	7	2.0	47.5	6.8	14.0	91.6	48.0	31.3
	Chile	57	1.2	2	2.0	18.6	9.7	22.6	87.9	52.3	15.1
	Ukraine	128	-0.6	6	4.1	53.7	8.8	NA	95.6	27.5	NA
	Graduation	Above average	On average	Below average							

* A figure is considered to be above average (below) when its value is equal or larger (smaller) than the average for 45 Emerging Markets plus (minus) 0.5 standard deviations

Source: BBVA Research, World Bank (WB), Center for Systemic Peace (CSP), World Trade Organization (WTO), Food and Agriculture Organization (FAO), International Labour Organization (ILO), United Nations University-World Institute for Development Economics Reserach (UNU-WIDER) and national statistics

Nest countries assessment on potential brakes to growth

Potential brakes to growth present a larger dispersion within countries in the case of the Nest group. Chile and Poland have lower risks, with Bangladesh, the Philippines, Egypt and Nigeria presenting higher challenges.

Regarding institutional factors, Chile and Malaysia share a better diagnosis, both concerning the investment climate and the public sector indicators, while also Thailand, South Africa and Peru are above average in terms of investment climate and Poland in the case of governance and state strength. The opposite happens in Egypt, Nigeria, Pakistan, Bangladesh and the Philippines, with an assessment worse than average from both private and public approaches.

Some of the Nest countries share both a high proportion of income expenditure in food products and food imports dependency. That is the case for Egypt, Vietnam, Malaysia, Ukraine and Bangladesh, exposed then to both domestic and external food price shocks (they import around 4-5% of GDP in food products with a share of over 40% in the CPI). Nigeria and Peru also have very large shares of food in the CPI basket (close to 60% in the first case), but their import dependency is half (around 2% of GDP). South Africa and Chile are the countries with the lowest exposure to food price shocks according to these criteria.

With respect to potential social unrest stemming from labor market conditions, Nigeria and South Africa face the highest unemployment rates (more than 20%), followed by Colombia (above 10%). Although South Africa and Colombia record high secondary education enrolment (over 90%), both have high youth unemployment rates, being especially worrisome in the first case, with almost half of the active population being jobless. Asian Nest countries have the lowest unemployment rates, also for young people, although they lag behind in terms of education, as in Nigeria. The labor market is not so tight in Latin American economies, with aggregate and youth unemployment rates on average, as well as in terms of secondary education enrolment.

Finally, the challenge of inclusive growth is also present for Nest countries, especially those related to the income distribution in the case of Latin American countries (the four Nest countries average a Gini index around 50%, 10 points over the 45 EM reference), South Africa (with a Gini index value of 67%, the highest among the 45 EM) and Malaysia (46%, the highest among Asian EM). Poverty data is not so prominent, but concern is focused on Colombia (37% of the population below the poverty line) and also in Peru, South Africa, the Philippines, Pakistan and Egypt (all of them with shares over 20% of total population). The case of Malaysia is of interest, with a very uneven income distribution, as mentioned before, but the lowest share of people under the poverty line for the countries with available data (a percentage less than 10% of total population).

3. Ad-hoc issues in the world of EAGLEs

Box 1. Structural disequilibria: how do EAGLE countries fare when compared with developed ones?

During the past years the balance of risks has moved to a more favorable risk-return profile for the emerging markets. Supported by a significant improvement in policy management after the lessons learned during their crises, emerging countries find themselves in a sound position. A first "bird's eye" of public and current account shows that risks are now concentrated mainly in the developed economies. However, part of this bias could be the result of negative cyclical effects of the crisis. This box analyses the structural situation of public and external imbalances and confirms that rather than a cyclical phenomenon the structural twin deficits remain favorable for the emerging markets.

A new growth-risk pattern

One of the salient results of the recent crisis has been the change in the risk-growth profile between developed and emerging economies. Although economic growth has usually favoured EMs, the risk-return trade-off has generally played against.

This paradigm has started to change as a consequence of the global crisis, although the seeds of the change can be found even before. The Asian and Latin American crisis during the nineties acted as a powerful wake-up call for emerging economies to improve their economic policies. First, they contributed to reduce macroeconomic imbalances. Second, and more importantly, they introduced the idea of a prudential approach to avert problems in the future.

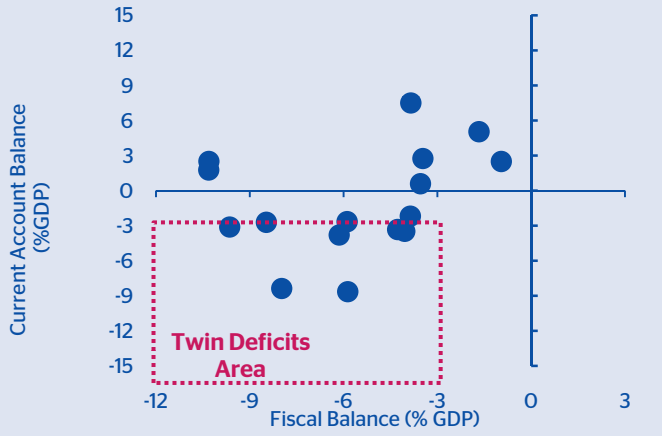
A "bird's eye" on twin deficits in developed and emerging economies

A simple view to account for the change in the risk profile of the world is to check visually the current account and fiscal balances in both emerging and developed economies. Chart 14 shows that developed markets imbalances are now more concentrated in the worrisome quadrant (CA and fiscal deficits) and some of them fall inside of the dangerous limits (delimited by imbalances both above 3%). Contrary, the scatter-plot for emerging economies in Chart 15 shows a more benign situation, with most of the countries lying outside the 3% twin deficits area.

Obviously, some of the divergent patterns are the result of cyclical effects triggered by the impact of recent crisis. Thus, we consider more relevant to assess the situation of the structural twin deficits. To do that we decompose both the current account and fiscal balances in the structural and cyclical component to answer the following questions:

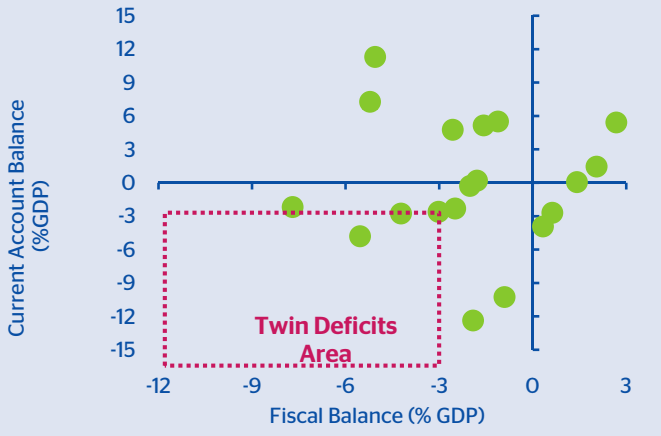
- What is the size of the structural twin deficits?
- Which are the structural drivers of the structural current account deficit?
- How the financial crisis has affected these structural drivers?

Chart 14
Nominal current account and fiscal balance in developed countries (% of GDP, 2011)



Source: BBVA Research and IMF

Chart 15
Nominal current account and fiscal balance in emerging countries (% of GDP, 2011)



Source: BBVA Research and IMF

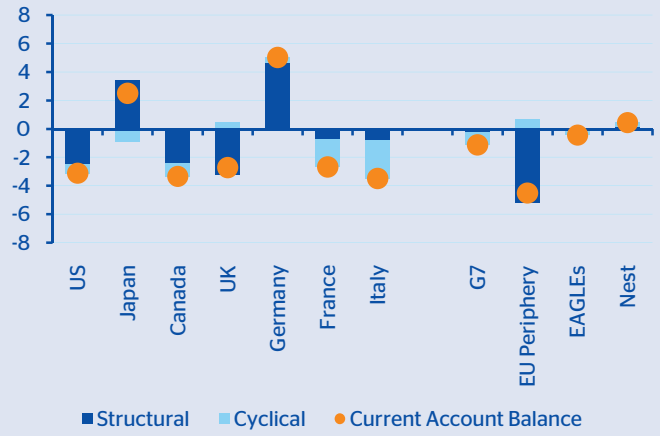
Structural twin deficits concentrated in developed countries but not exclusive

We estimate a panel for the current account balance, covering the period between 1980 and 2010 for 46 economies, which accounts for around a 90% of the world's GDP[9]. The main results from our estimations are in line with economic literature[10]. A negative long-term coefficient is estimated for demographic variables (including dependency ratios and population growth) and for the investment-to-GDP ratio. On the contrary, and a positive elasticity is found for the fiscal balance, terms of trade (especially the oil balance) and trade openness.

Applying coefficients to the 5-year moving average of explanatory variables, and adding country effects accounting for omitted factors, we can now estimate an approximation for the structural component of the current account. The main findings are the following:

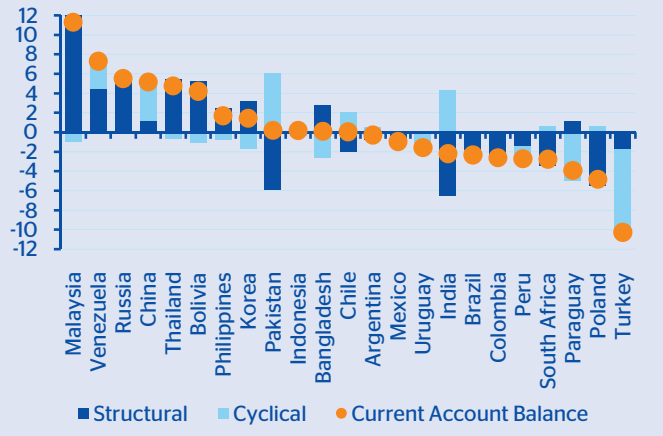
- Developed economies (Chart 16): Except Germany and Japan, the rest of the G7 countries has structural current account deficits. The US, Canada and the UK present structural imbalances higher than 2% of GDP. Although relatively high, this is significantly lower than the EU periphery, which in average has a structural deficit of nearly 5% of GDP.
- Emerging economies (Chart 17): Taking BBVA's own grouping of key emerging economies (the EAGLEs and their Nest), their structural position is close to equilibrium, namely zero. The largest structural surplus is recorded for Malaysia (near12% of GDP). The structural surplus is also significant in the case of Thailand and Korea (above 5%), the oil and gas exporters (Venezuela and Russia over 4%) and, to a lesser extent, China (1.5%). Contrary, the largest external disequilibria are found in India and Pakistan (over 6%), followed by South Africa (around 3.5%). Finally, Brazil, Colombia, Peru and Turkey present moderate structural CA deficits (around 2%).

Chart 16
Decomposition of current account in developed countries (in percentage points, 2011)



Source: BBVA Research

Chart 17
Decomposition of current account balance in emerging countries (in percentage points, 2011)



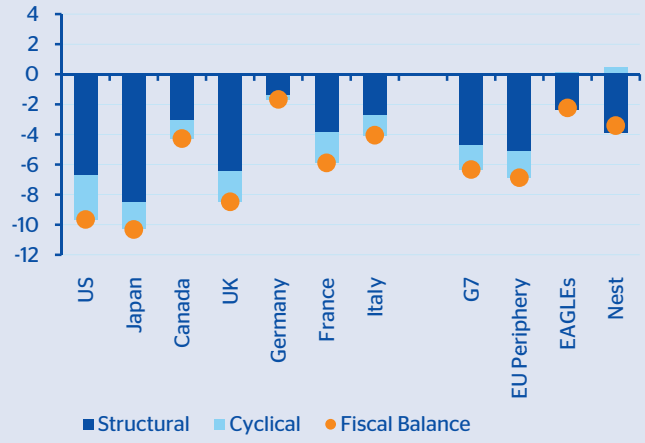
Source: BBVA Research

9: Argentina, Australia, Austria, Bangladesh, Belgium, Bolivia, Brazil, Canada, Chile, China, Colombia, Egypt, Finland, France, Germany, Greece, Hong Kong, India, Indonesia, Ireland, Italy, Japan, Korea, Malaysia, Mexico, Netherlands, Nigeria, Pakistan, Panama, Paraguay, Peru, Philippines, Poland, Portugal, Russia, Singapore, South Africa, Spain, Taiwan, Thailand, Turkey, the United Kingdom, the United States, Uruguay, Venezuela and Vietnam.
10: For details on methodology see Economic Watch "Structural Twin Deficits: A problem of the developed world rather than the emerging one" at www.bbvaresearch.com/KETD/ketd/ing/nav/geograficas/economiasemergentes/index.jsp.

With respect to fiscal imbalances, the relative position of developed and emerging economies is also different:

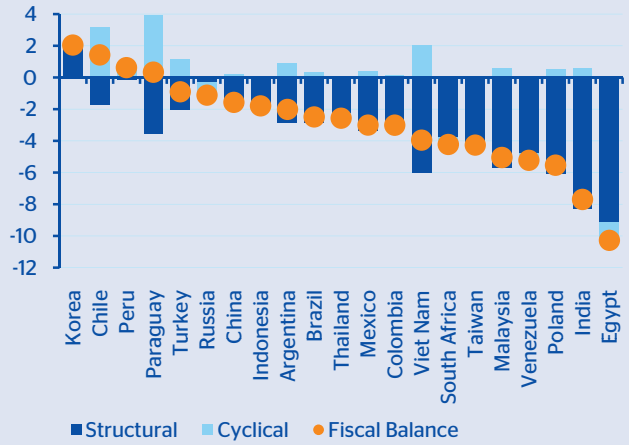
- Developed economies (Chart 18): Most of the G7 (except Germany) present worrisome cyclically adjusted deficits positions. This is especially the case for Japan (8%), the US and the UK (both with near 6.5% structural deficit), but France (4%) and Italy(3%) are also in this situation despite the recent fiscal consolidation adjustments. On average, and after the fiscal consolidation process, the situation of the EU periphery (average of near 5%) is now similar to the G7.
- Emerging economies (Chart 19): Although in a better position, many of the EAGLEs and particularly the Nest have also cyclically adjusted deficits. The highest structural deficit would correspond to Egypt (9% of GDP), India (8%), Poland, Vietnam and Malaysia (6%), Venezuela (close to 5%), Taiwan, South Africa and Paraguay (around 4% in both cases). Colombia, Argentina and Brazil have lower structural fiscal deficits of around 3% of GDP. These are even lower (2%) for Thailand, Turkey, China, Indonesia and Chile Finally, Russia and Peru record an almost neutral structural fiscal position.

Chart 18
Decomposition of fiscal balance in developed countries (in percentage points, 2011)



Source: BBVA Research

Chart 19
Decomposition of fiscal balance in emerging countries (in percentage points, 2011)



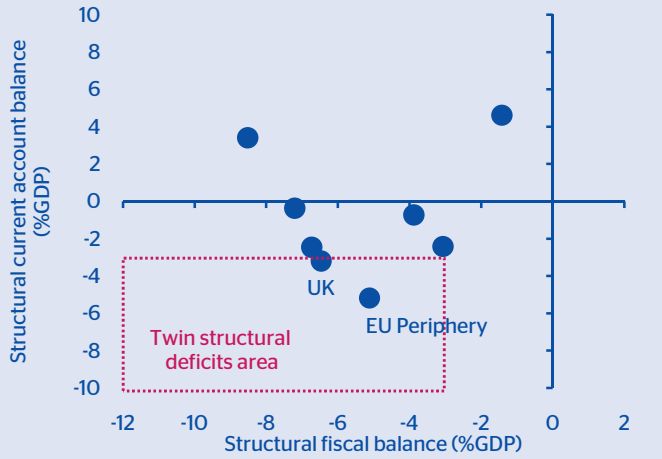
Source: BBVA Research

Who are the kings of twin structural deficits?

Once we have decomposed both the current account and fiscal balance between structural and cyclical components, we can determine which countries present higher vulnerability position in terms of twin structural imbalances. For this, we identify which countries lay on the structural twin deficits area defined as structural deficits higher than 3%. The main results are the following:

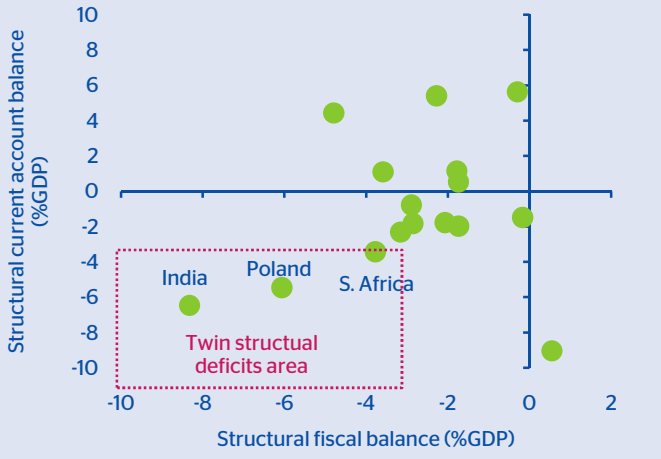
- Developed economies (Chart 20): EU peripheral countries are the ones with higher structural deficits, but the UK position is far from comfortable.
- Emerging economies (Chart 21): Only three countries of our EAGLEs and Nest are inside the vulnerability region. India is the most worrisome case. Poland and South Africa, although inside the vulnerability area, have structural imbalances close to our 3% benchmarks. There are other countries outside the structural twin deficits but with no room, such as Brazil, Turkey, Chile and Argentina.

Chart 20
Structural current account
and fiscal balance in developed countries (% of GDP, 2011)



Source: BBVA Research and IMF

Chart 21
Structural current account
and fiscal balance in emerging countries (% of GDP, 2011)



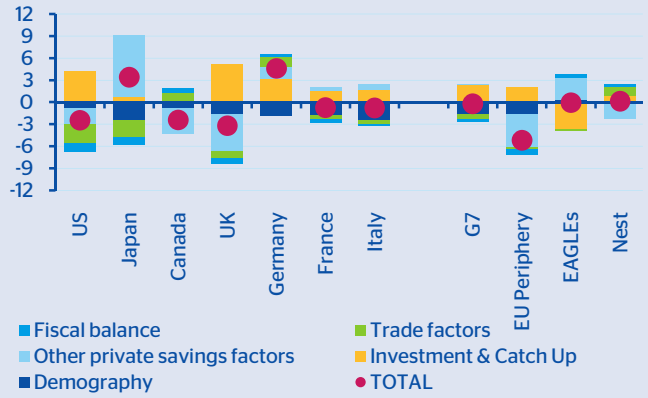
Source: BBVA Research and IMF

The drivers of the structural current account balance

Once the model is estimated we can assess for the factors determining the structural current account position. We have grouped the savings related variables in fiscal position, demography (dependency ratios and population growth), other private savings factors (including financial deepening) and trade-related variables. Finally we also account for investment. The main results of the analysis for 2011 are the following:

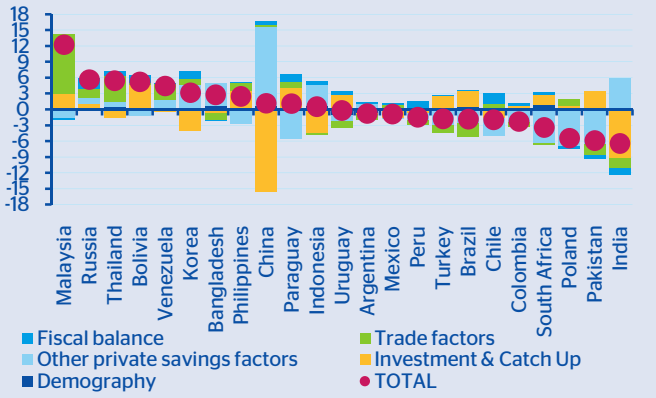
- Developed economies (Chart 22): In general terms saving related factors are responsible for the structural current account positions in 2011 as investment ratios have been reduced during the crisis. This is particularly the case of demographic factors, whose negative contribution is uniform across the countries. The twin deficits argument is not homogeneous for the 2011 structural position. There is evidence for the twin deficits argument in the EU peripheral countries, US, UK and Japan but not in Canada and Germany. Trade related factors are also responsible for the structural current account balance, weighting negatively in relatively close countries as the US and Japan and, to a lesser extent, in France and Italy, while the effect is positive in Germany and Canada. Other private sector savings determinants, mostly related to financing considerations, are also driving structural deficits in most, but not all, the countries (the main exception being Japan and Germany). Finally, an investment rate below world average is contributing positively to the current account balance for nearly all developed countries.
- Emerging economies (Chart 23): In contrary to the developed economies savings related factors are normally supporting structural balances in the EAGLEs countries. Demographic factors are neutral or slightly positive contributors to structural balances as population is more dynamic and young dependency ratios are higher, offsetting their condition of less-aged economies. The fiscal impact has been also positive except for Pakistan and India. The contribution of other private savings factors, which add for these economies social protection considerations, is not uniform across the countries. It contributes positively in China, India, Russia and Korea. But, on the other hand, it is pressuring structural deficits in South Africa, Pakistan, Brazil, Chile and Turkey among others. There is also asymmetry in the investment driver. There are countries where still low investment rates are supporting structural current account balances (Brazil, Turkey, Philippines and Malaysia) in contrast with very high investment rates pressuring on structural deficits (China, India, Indonesia and Korea).

Chart 22
Decomposition of structural current account in developed countries (in percentage points, 2011)



Source: BBVA Research

Chart 23
Decomposition of structural current account balance in emerging countries (in percentage points, 2011)



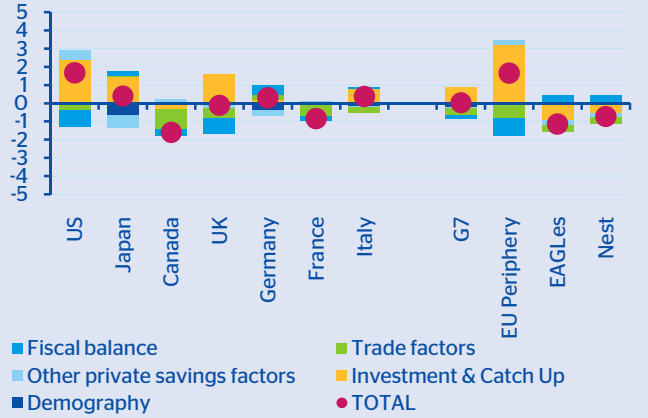
Source: BBVA Research

The effects of the recent financial crisis in the structural current account balance

The current financial crisis has triggered important current account adjustments in some of the countries, driving a partial correction of structural imbalances. Analysis from the contribution of the different factors brings the following conclusions:

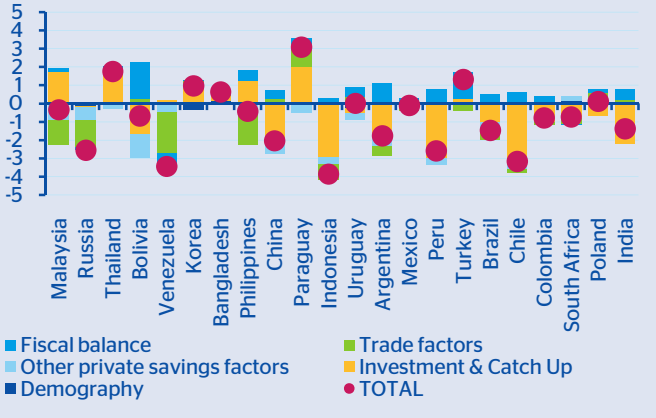
- Developed economies (Chart 24): Previously overheated economies (US, EU periphery) have experienced a positive change in their structural positions (an average improvement of 2 percentage points), mainly due to dramatic changes in the structural component of investment and, to a lesser extent, by the group of other private savings factors caused by the de-leveraging process and the increase in precautionary savings. However, fiscal structural deterioration has limited the potential adjustment in these countries. Thus it looks that besides cyclical effects, the de-leveraging process is also improving the structural positions of these economies. Contrary, Japan and Germany did not change significantly their structural positions.
- Emerging economies (Chart 25): Most of the emerging markets have experienced a deterioration of their structural position, contributing therefore to the global imbalance adjustment. The main driver for the adjustment has been the investment component, followed by the trade related factors. The commodity exporters suffered from the big slump of the terms of trade after the crisis. The fiscal factor has contributed to support structural positions as the structural fiscal balances improved relative to the world during the period 2007-2011.

Chart 24
Change of structural current account balance in developed countries (in percentage points, 2007-2011)



Source: BBVA Research

Chart 25
Change of structural current account balance in emerging countries (in percentage points, 2007-2011)



Source: BBVA Research

Box 2. Shifting Wealth: China is the only global creditor within BBVA EAGLEs

International Investment Position, the easiest way to measure external wealth

International investment position (IIP) is the balance sheet of an economy. It summarizes the international assets and liabilities an economy holds with the rest of the world. They are grouped into five categories: direct investment, portfolio investment, financial derivatives, other investment (mainly short term credits) and reserve assets. The net position of it is called net IIP, which is the difference between assets and liabilities. Thus, an economy can be either a net creditor or debtor with the rest of the world. Creditor economies can use their net assets to fund current account deficits in the future without increasing their external vulnerabilities. On the other hand, debtor countries must implement policies such that their current account deficit path is "sustainable", in order to avoid reaching a negative IIP that is unbearable. Special attention should be taken on the deficit in the net portfolio investment flows, since this means an economy is more dependent on external savings to fund their excessive expending.

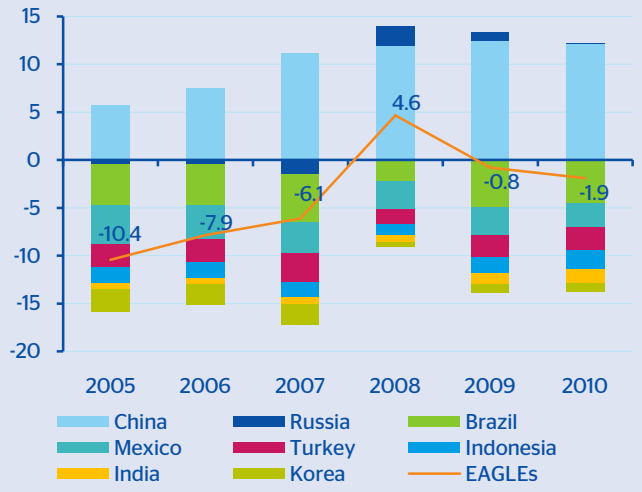
Is wealth shifting to Emerging Markets? Only China is a huge creditor within our EAGLEs[11]

Within the EAGLEs , China is the biggest supplier of credit whereas Brazil, Mexico, Turkey and Indonesia are the biggest debtors. The net position of the EAGLEs is negative, which is not surprising considering they are developing economies which require external funding to finance their current investment projects (charts 26 & 27).

All other EAGLEs are net debtors, except for Russia whose surplus is negligible. They have all followed the same strategy of accumulating reserve assets, but it has not been enough to offset the increasing debtor position in FDI and portfolio investment (chart 28). However, this trend confirms the interest in these economies given their expected high growth rates. At the end their revenues will increase remarkably, reducing their current debts.

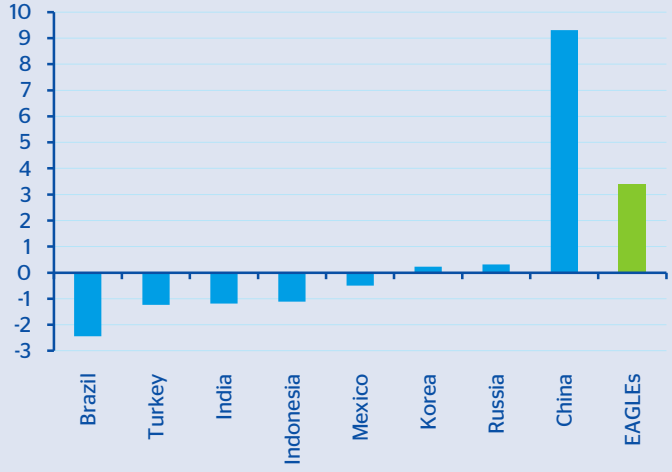
One interesting case is Korea who is the only EAGLE holding an FDI positive net position. This is a consequence of the reallocation of the manufacturing production process which has happened in recent years. It is also evident that Korean corporations are in a new stage of developmental process, becoming transnational world players.

Chart 26
EAGLEs: net IIP (as % of EAGLEs' GDP)



* No data for Taiwan
Source: BBVA Research and IMF

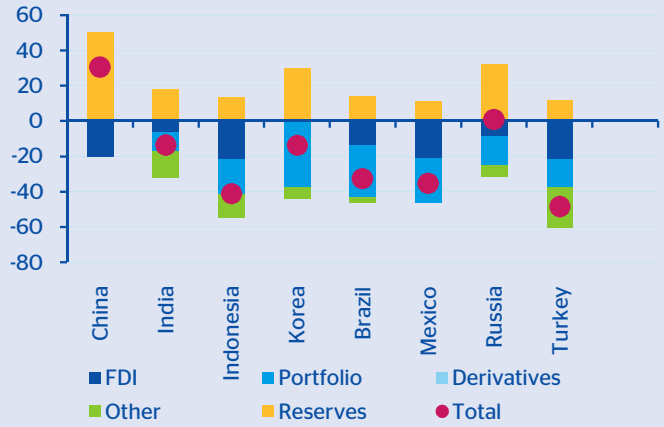
Chart 27
EAGLEs: change in net IIP
(between 2005-2010, as % of EAGLEs' GDP in 2010)



* No data for Taiwan
Source: BBVA Research and IMF

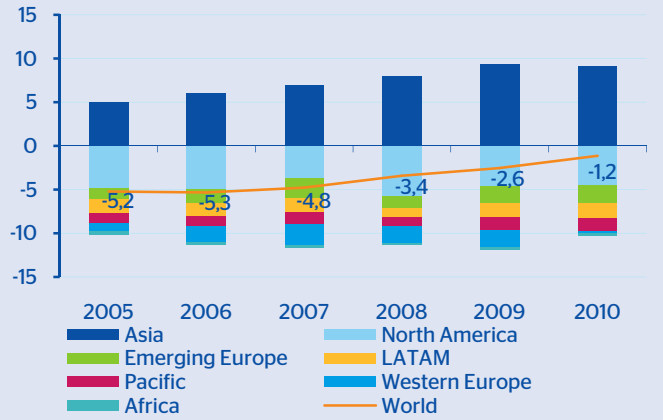
11: EAGLEs is a grouping acronym created by BBVA Research to identify all emerging economies, whose expected contribution to world gross domestic product (GDP) in the next ten years is expected to be larger than the average of the G7 economies, excluding the United States..

Chart 28
EAGLEs: net IIP in 2010 (as % of GDP)



Source: BBVA Research and IMF

Chart 29
World*: net IIP (as % of World's GDP)



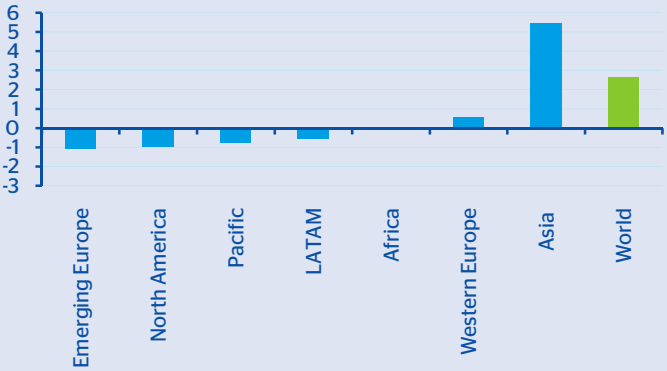
* World: is a sample of 62 economies whose aggregated GDP represents almost 93% of Word GDP in US dollars according to IMF database. Given the lack of data on IIP, GCC
Source: BBVA Research and IMF

Several Asian economies[12] are net creditors

The highest increase in IIP from 2005 up to 2010 was observed in the Asian economies as they generally maintained high savings rates. In terms of world GDP[13], the net IIP of the region almost doubled (charts 29 & 30). In addition to China, Japan, Singapore and Hong Kong have increased their net IIP the most either by augmenting their net portfolio holdings (equity or debt) or by raising their reserve assets (chart 31). As a consequence, this situation has created an interesting paradox:, while some of the Asian economies (China, Hong Kong and Singapore) are main recipients of FDI inflows, they are also massive savings exporters. It is also worth highlighting the fact that Japan holds the largest net FDI surplus in the region and the second highest within the sample of 62 economies, which is also a result of its own reallocation of manufacturing strategy in Southeast Asian economies.

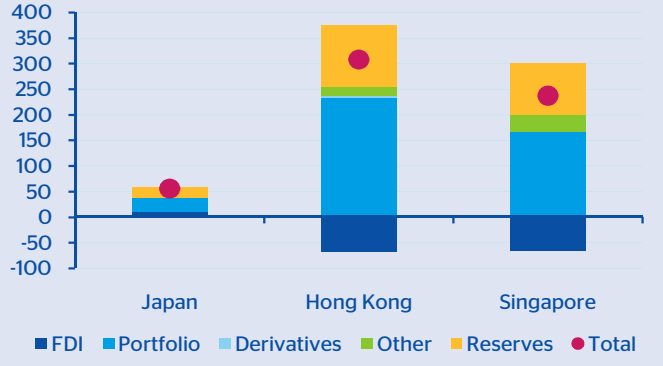
The reasons behind the increase in net IIP are different. In the case of China, huge savings rate is the cause. State Own Enterprises (SOEs) hold large reserves to fund their investment projects; households have been advised to hold precautionary savings given income inequality and lack of safety; hence consumption rates still remain low in China. In the case of Japan, the already high private savings rate has increased further, raising the Ricardian equivalence hypothesis among households and corporations given the inconvenient public debt and deficit.

Chart 30
World*: change in net IIP
(between 2005-2010, as % of World's GDP in 2010)



* World: is a sample of 62 economies whose aggregated GDP represents almost 93% of Word GDP in US dollars according to IMF database. Given the lack of data on IIP, GCC
Source: BBVA Research and IMF

Chart 31
Asian economies: net IPP in 2010 (as % of GDP)



Source: BBVA Research and IMF

12: Asian economies included are: Japan, China, Singapore, Hong Kong, India, Indonesia, Korea, the Philippines, Malaysia, Thailand, Pakistan and Bangladesh.
13: A sample of 62 economies whose aggregated GDP represents almost 93% of Word GDP in US dollars according to IMF database. Given the lack of data on IIP for GCC economies are not considered.

Globally, other than Asia, only Germany stands out as a large net creditor

Emerging Europe[14] and North America have the largest increase in negative IIP position. In Emerging Europe, high investment rates financed by credit inflows explain the large negative position. In the US, although big efforts have been made to reduce external deficit, the de-leveraging process of the private sector has been offset by a sensitive increase of the public deficit that explains the higher holdings of debt by foreign investors.

Western Europe[15] has improved significantly their net IIP, almost reaching equilibrium in 2010; however the situation in Europe is asymmetric. Most of the peripheral countries are debtors as a result of the increase in private and public debts during the pre-crisis years, while core economies (i.e. Germany, Switzerland, Belgium, Norway and the Netherlands) kept a strong positive position due to their low consumption rates in the pre-crisis period. When looking at G7, Japan and Germany are the biggest creditors, making the G7 a global creditor as a block, regardless of the huge negative position of the US (charts 32 & 33).

What are the main determinants of a net creditor position?

Several variables have been identified as the main determinants of the net creditor position, defined as the international investment position (IIP) in the economic literature[16]. The key variables are the GDP per-capita, the public debt level as percentage of GDP and the old-age dependency ratio (population above 65 years old). The use of the latter is justified on the basis of the life cycle hypothesis, which characterizes age groups according to their consumption, investment and saving patterns. People at retirement age should have the highest net asset position, with both real and financial assets and marginal liabilities, in contrast to younger people at the start of their working life. However, an aging society could eventually reduce its aggregate net foreign assets position as people will tend to use their savings and also be less able to leave inheritance.

Other variables including terms of trade, reallocation of manufacture production and precautionary savings, should also be considered.

When considering the change in the net IIP between 2005 and 2010, it is clear Asian economies and also Germany have become the most important savings exporters worldwide. However, regional aggregations hide other important results. Japan, China and Germany were the economies which increased the most their net IIP during these years, as a consequence of their impressive current account surpluses (charts 34 & 35), which are part of what is known as the global imbalances. Germany is similar to Japan in the sense it has increased its net FDI, but has also become the largest supplier of short term credits.

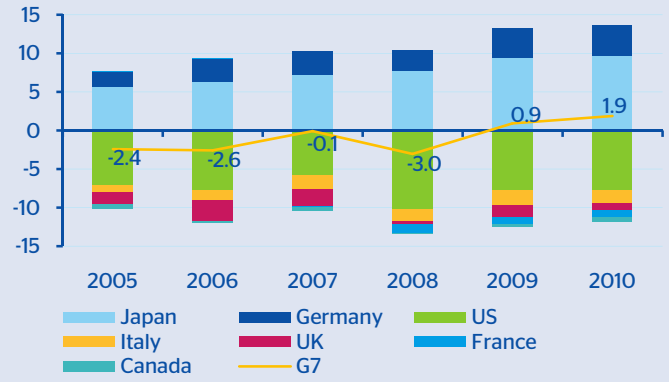
The reallocation process of manufactures production does not seem to be the main driver when trying to explain the change in net IIP. All G7 economies, except Germany, have reduced their share of manufacture exports in the last decade (chart 36). On the other hand for the case of China this process is clearly behind its huge trade surplus which ended with the impressive growth of its international reserves (chart 37).

The savings rate of the economy seems to be one of the most relevant determinants. When comparing the G7 and the EAGLEs (charts 38 & 39), China, Japan and Germany have the highest rates. Nevertheless, other circumstances should be considered, for instance the current stage of development and the quality of social protection networks which may stimulate a higher rate of precautionary savings. Excluding China, all EAGLEs have larger saving rates than Japan and Germany (bar Mexico, Brazil and Turkey), the resources required to finance their current growing process is larger and thus the change in their IIP is negligible or even negative.

Concerning the rise of commodity prices, in particular for energy like oil (chart 40), there is a sensitive income transfer from households living in net import to export economies; this shock has been more than offset in the case of Japan and Germany.

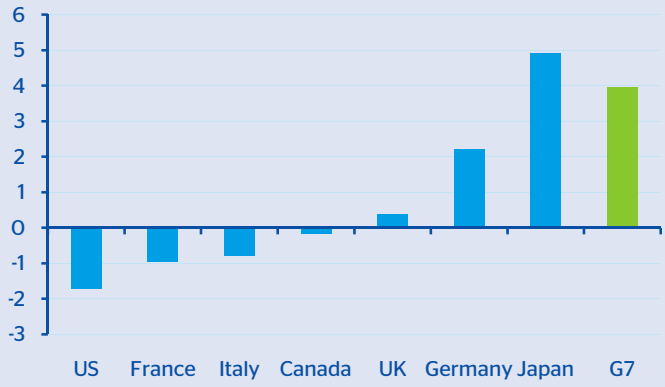
14: Emerging Europe includes: Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Poland, Romania, Russia, Slovak Republic, Slovenia, Turkey and Ukraine. North America includes: Canada and the US.
15: Western Europe includes: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland and the UK..
16: Philip R. Lane and Gian Maria Milesi-Ferretti, (2001) Long-Term Capital Movements. NBER Macroeconomics Annual 2001, Volume 16
Philip R. Lane and Gian Maria Milesi-Ferretti, (2000) External Capital Structure-Theory and Evidence, IMF Working Paper No. 00/152.

Chart 32
G7: net IIP (as % of G7's GDP)



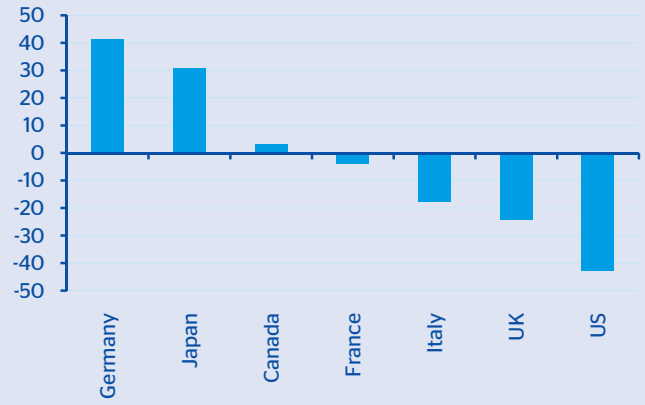
Source: BBVA Research and IMF

Chart 33
G7: change in net IIP
(between 2005-2010, as % of G7's GDP in 2010)



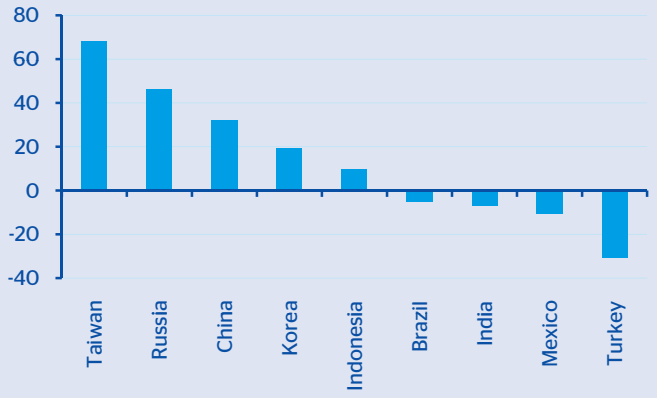
Source: BBVA Research and IMF

Chart 34
G7: accumulated current
account balance 2000-2010 (as % of 2010's GDP)



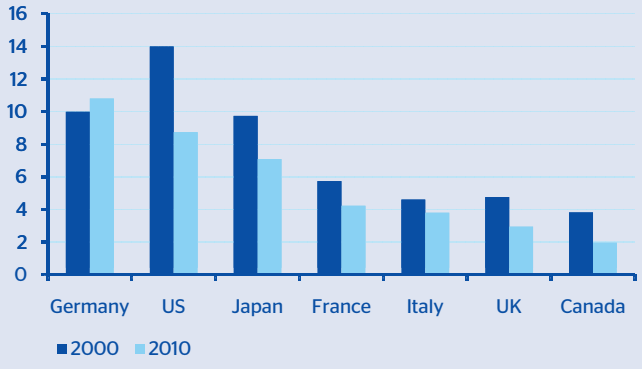
Source: BBVA Research and IMF

Chart 35
EAGLEs: accumulated current
account balance 2000-2010 (as % of 2010's GDP)



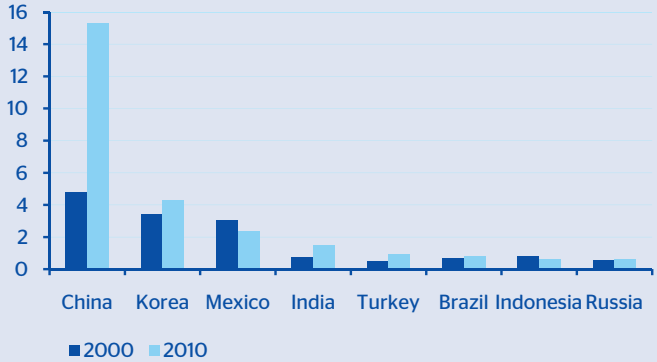
Source: BBVA Research and IMF

Chart 36
G7: share in world manufactured exports (%)



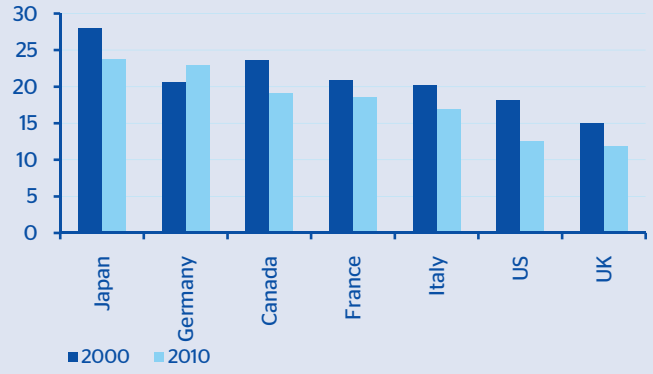
Source: BBVA Research and WDI

Chart 37
EAGLEs: share in world manufactured exports (%)



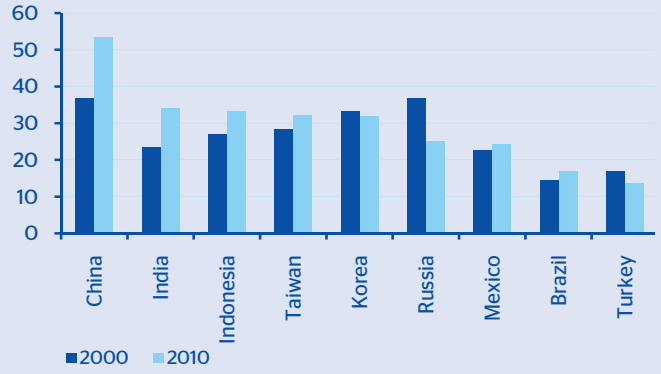
Note: No data for Taiwan
Source: BBVA Research and WDI

Chart 38
G7: gross national savings rate (as % of GDP)



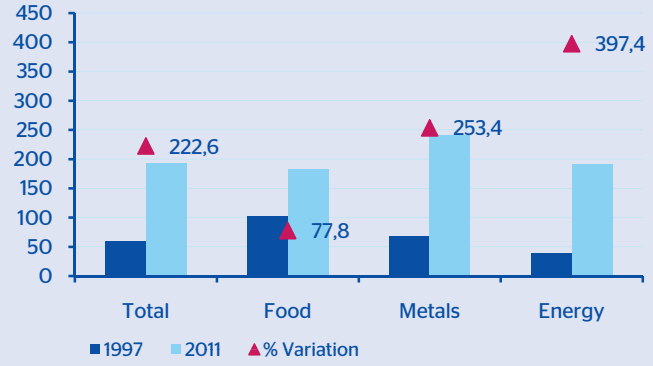
Source: BBVA Research and IMF WEO

Chart 39
EAGLEs: gross national savings rate (as % of GDP)



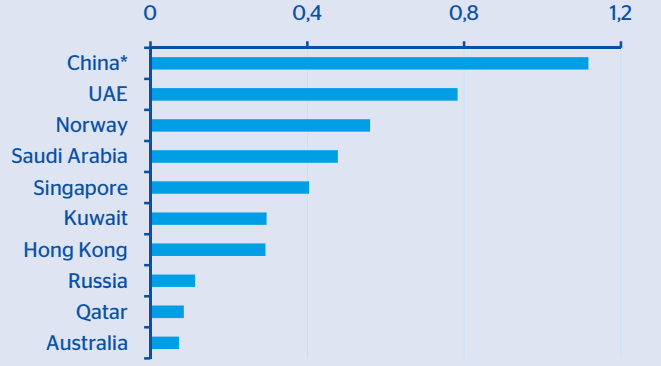
Source: BBVA Research and IMF WEO

Chart 40
Commodities price index (2005 = 100, accumulated % variation)



Source: BBVA Research and IMF

Chart 41
Sovereign Wealth Funds (Assets 2011, trillion USD)



* 2011 Estimate
Source: BBVA Research and Sovereign Wealth Fund Institute

Rebalancing the global economy: China will further increase its influence over EM

One solution to the global imbalance is to lower the high savings rate for current big creditors, which implies increasing their consumption. On the other hand, current debtors will need to raise their savings rates, thus de-leveraging their private and public sectors.

For the US, it needs to shift the economy from debt and consumption to savings and exports in order to become rebalanced. This idea is also being shared by some European peripheral economies which are implementing an adjustment process based on private de-leveraging and fiscal consolidation.

In the case of China, it is expected a portfolio rebalancing towards higher FDI at the expense of a decline in their reserve assets. Also change can not be ruled out in the currency composition of those reserves. In addition, their household consumption may rise faster if the ongoing pension reform has the desired effects of creating an efficient social protection network. Concerning EM, the Chinese portfolio reallocation should benefit them by increasing the funding available to finance investment projects, in particular infrastructure, in order to consolidate their development process through higher FDI and also portfolio investment.

Other EM will also rebalance their pattern of savings and investments. Emerging Europe will intensify the adjustment towards a more sustainable growth path with lower investment rates. Turkey's rebalancing should cause a correction of the current account deficit through higher saving rates and FDI financing should replace the current short term flows (especially credit flows). In Latin America, Brazil and Mexico are expected to maintain their strong fundamentals, for instance fiscal and external balances. It is anticipated their net IIP will start to increase as long as their transnational companies accelerate their expansion strategies, thus increasing their FDI outflows.

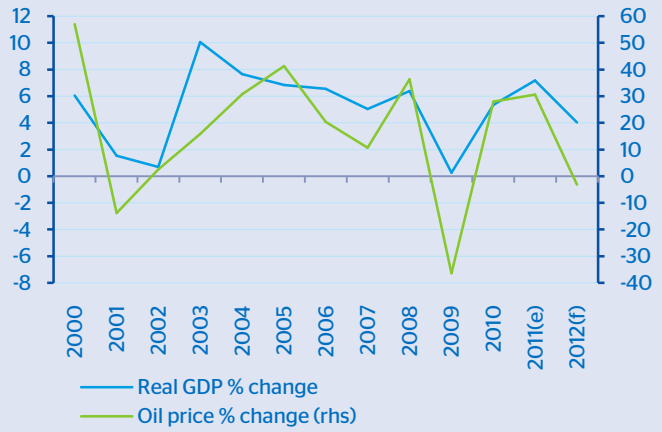
As long as EM continue their development process it is unlikely they will become the world's creditors, with the exception of China which will continue playing in a league of its own. For the moment, Asian economies and oil exporter countries have the largest investment pools in the world (Chart 41).

Box 3. What about the Gulf countries? An EAGLE in the making

The Gulf Cooperation Council (GCC) countries (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates) account for around a 20% of world oil production and 45% of proven oil reserves, reflecting the importance of developments in the oil market for their economies. As oil price is today around 4 times the value in the early 00s (it averaged USD 100 per barrel in 2011 against around USD 25 in 2002), the GCC countries have enjoyed an outstanding growth cycle for a long period.

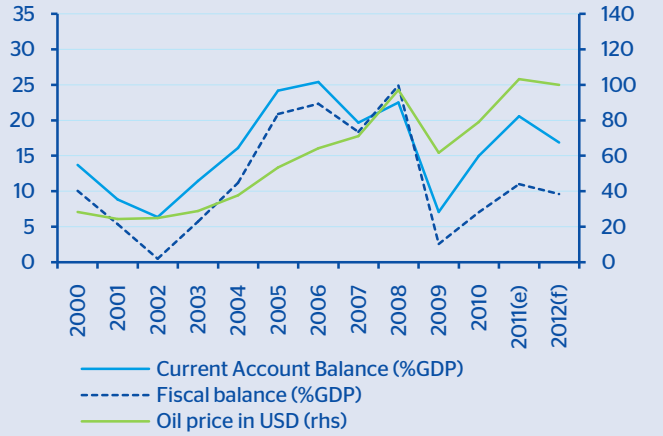
Real GDP annual growth averaged 6.1% between 2002 and 2011, well above the world's average (3.8%). At the same time, with the exception of Bahrain, the Arab Spring, has not spread into the GCC countries as it has happened in other places in the Middle East (e.g. Egypt, downgraded from the EAGLEs to the Nest as a result of short-term effects on growth stemming from social unrest and uncertainty about political transition).

Chart 42
GCC countries: real GDP LCU growth rates (%)



(e) estimation; (f) forecast
Source: BBVA Research and IMF

Chart 43
GCC countries: current account and fiscal balance



(e) estimation; (f) forecast
Source: BBVA Research and IMF

Spillovers from oil price boom

Income from hydrocarbons (oil and natural gas) constitutes a very large share of both fiscal and external revenues. For the 2007-2011 period[17], Saudi Arabia showed the highest fiscal dependency (an average of 89% of total revenues), followed by Oman, Bahrain and Kuwait, all of them also above 80%, and the UAE, slightly below this figure (76%). Qatar is an outlier here, with an estimated 55% of total fiscal revenues.

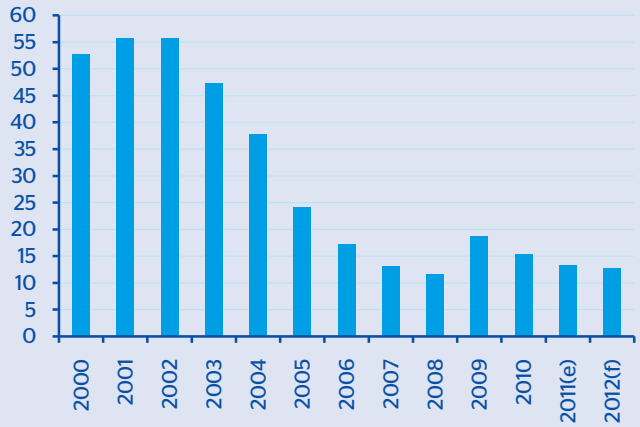
Qatar is, however, one of the most dependent countries in terms of exports revenue, with an average of 86%, similar to the share in Saudi Arabia (87%) and slightly below the highest figure, Kuwait, with a 93%, Bahrain and Oman show percentages between 70% and 80%, while in this case is the UAE the outlier, with "only" a 39%, although this share is downward biased due to significant re-export activity in this country. Excluding these figures, dependency raises to 57%, a percentage that is still, in any case, the lowest among the GCC countries.

As a result of increasing oil prices, the GCC countries have been enjoying very comfortable fiscal and external positions in the last decade. The simple average for the six countries over the 2000-2011 period is a fiscal surplus of more than 10% of GDP and a current account surplus of 16% of GDP. Continuous fiscal surpluses have resulted into a significant public debt reduction of more than 30pp over this period (from a figure close to 50% of GDP in the late 90s) , while current account surpluses have substantially increased international reserves. According to IMF data, total reserves for the six GCC countries were up to

17: Figures for hydrocarbons share in fiscal and external revenues are taken from the corresponding latest information of the IMF under the Article IV Consultation, December 2011 for Oman, September 2011 for Saudi Arabia, July 2011 for Kuwait, May 2011 for UAE, March 2011 for Qatar and December 2010 for Bahrain. Averages are then computed using available data, estimations or projections over the 2007-2011 period.

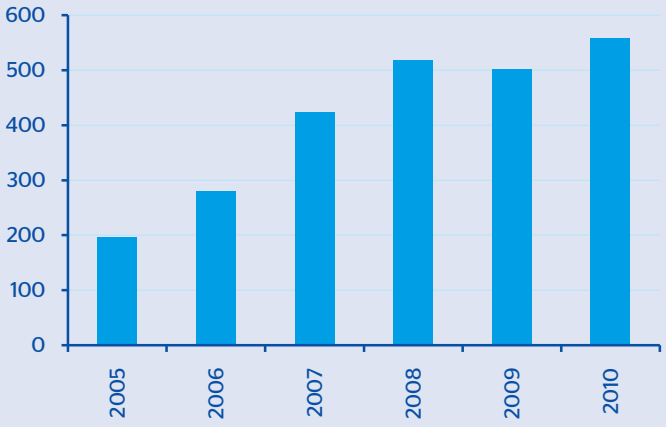
USD 553 billion at the end of 2010, most of them corresponding to Saudi Arabia (USD 445 billion), which is also the country with the highest amount in relative terms, with almost 100% of GDP in comparison with an average around 20% for the rest of the GCC members. As a result of current account surpluses, sovereign wealth funds of these countries are at the world top ranking in terms of assets under management. This is the case for example of Abu Dhabi Investment Authority (USD 627 billion as of December 2011, being the 1st in the ranking), SAMA Foreign Holdings from Saudi Arabia (USD 473 billion and in 4th position) and Kuwait Investment Authority (USD 296 billion and 6th in the ranking)[18].

Chart 44
GCC countries: public debt (% of GDP)



(e) estimation; (f) forecast
Source: BBVA Research and IMF

Chart 45
GCC countries: total reserves (billion USD)



Source: BBVA Research and IMF

However, these developments have been uneven within countries. Kuwait have shown the best performance both in the fiscal and the external front, with an average surplus of 30% of GDP in both cases, as well as a reduction of more than 40pp in public debt-to-GDP ratio. Oman, Qatar and the UAE kept a fiscal surplus around 9% and Saudi Arabia over 12%, while Bahrain was the only country averaging a fiscal deficit, resulting into public debt increase (the highest among GCC countries with an estimated 32% of GDP in 2011). It is worth noting that, although figures remain under control, also the UAE have shown an increase in public debt, especially in 2009, climbing from 13% to 23% of GDP as a result of Dubai World (DW) bailout. In July 2009 the government established the Dubai Financial Support Fund (DFSF) in order to provide financial assistance to Government-Related Entities (GRE). On the opposite side, Saudi Arabia underwent a very strong deleveraging in the public sector, reducing public debt from more than 100% of GDP in the late 90s to less than 10% in 2010 and 2011. Regarding the current account, coming after Kuwait, Qatar averaged a surplus of around 25% of GDP, followed by Saudi Arabia (slightly less than 20%), while the other three countries showed similar figures around 8%.

Other variables have to be considered in order to analyze spillovers from the oil price boom. Regarding the non-hydrocarbon sectors[19], real GDP has shown a remarkable growth, with an annual average of 18% for Qatar in the 2007-2011 period and around 5% for the rest of the countries. This growth has outperformed in all cases real GDP change of the hydrocarbon sector, which in fact was negative in the cases of the UAE and Kuwait and almost plain for Saudi Arabia. Some of the drivers of dynamism outside of the hydrocarbon sectors have to be with liquidity expansion stemming from strong external revenues. Credit to the private sector has increased by a simple annual average of 18% between 2002 and 2011, with Qatar (27%) and the UAE (21%) outperforming, Bahrain

18: A complete list is available at the Sovereign Wealth Fund Institute (SWFI): www.swfinstitute.org/fund-rankings/.
19: Figures commented here are also taken from IMF information under the Article IV Consultation (see Note 1 for the latest publication date for each country).

on average, Saudi Arabia and Kuwait slightly below (16% in both cases) and with the lowest increase in Oman (13%). The construction and the real estate sectors were among the most benefited of this credit expansion, paving also the way to the generation of bubbles in some areas. For example, urban real estate prices tripled in real terms in Dubai between 2004 and 2008, while initial levels were almost recovered in 2009 after a considerable collapse.

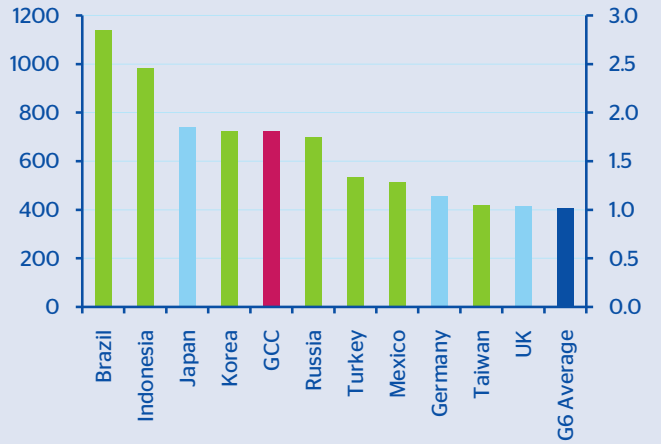
Dynamics in both the oil sector (much more in nominal terms) and in the rest of the economy should have translated into employment generation and a reduction of unemployment rates. Data for these countries is not always reliable and available, but anecdotal evidence show a general positive evolution of labor market in the last years. The IMF estimates that approximately 7 million new jobs were created in the GCC countries between 2000 and 2010[20], which represents around a 50% increase. The aggregate unemployment rate is low in Kuwait and the UAE, under 5% in both cases, although higher in Saudi Arabia, above 10%, and Oman. One of the most remarkable issues is the very wide difference between the performance of labor market for national workers and for foreign workers. The IMF estimates that out of the 7 million jobs created in the last decade, only 2 million went to nationals. This asymmetry happens for example in the case of the UAE, with an aggregate unemployment rate around 4% in 2009, but a figure of 14% for national workers and 3% for foreigners, or Oman, with a rate of 24% among nationals. From a sector approach, construction, real estate and finance activities have shown a significant dynamism in job creation. For example, in Qatar, employment share of construction raised from less than 20% in 2001 to almost 40% in 2007. In the UAE, employment annual increase between 2001 and 2008 averaged 13% in the construction sector and 10% in finance and insurance services and in real estate services, above the 8% average.

The GCC countries would be the sixth EAGLE

According to estimations by the IMF for 2011, Saudi Arabia is the biggest GCC country, with a GDP of USD 665 billion (in PPP-adjusted terms), followed by the United Arab Emirates (256bn), Qatar (178bn), Kuwait (147bn), Oman (80bn) and, finally, Bahrain (30bn). The six countries sum to USD 1,356 billion, which around 1.8% of world's incremental GDP.

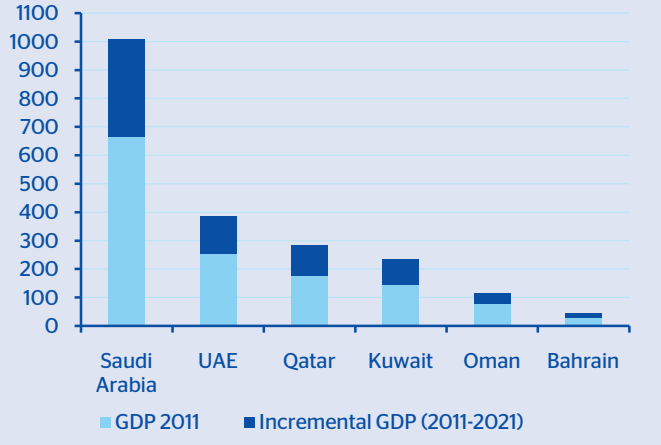
The latest forecasts from the IMF (September 2011 WEO), extended to 2021 with the 2016 figures, anticipate an annual growth rate of 4.4% for the GCC countries, ranging from 3.7% for Oman to 4.8% for Kuwait and Qatar. With this growth, the six members will add USD 723 billion to world incremental GDP in the next 10 years, around 1.8% of the total. As expected growth rates are relatively homogenous, no major deviations are forecasted between current and forecasted incremental GDP share.

Chart 46
Incremental GDP adjusted by PPP (billion USD) and contribution to World economic growth 2011-2021 (%)*



* The graph excludes China (USD 13,718 billion, 34%), US (USD 3,881 billion, 9.6%) and India (USD 4,820 billion, 11.9%)
Source: BBVA Research and IMF

Chart 47
GCC countries: current economic size and incremental GDP 2011-2021 (billion USD)



Source: BBVA Research and IMF

20: IMF Regional Economic Outlook for Middle East and Central Asia (October 2011), www.imf.org/external/pubs/ft/reo/2011/mcd/eng/pdf/mreo1011.pdf

If the GCC countries were considered a whole economy, they would be placed sixth in the EAGLEs ranking, slightly surpassed by Korea (1.8%) and marginally over Russia (1.7%), while they contribute more than Turkey (1.3%), Mexico (1.3%) or Taiwan (1.0%). The GCC countries contribution to world's growth is clearly above the G6 average (USD 405 billion), so their membership of the EAGLEs would be primarily robust. In addition, it should be highlighted that incremental GDP for the 2011-2021 period is expected to be higher than contribution for any of the members of the G6 bar Japan (USD 741 bn). However, even in this case, they would only need 0.1pp more of annual growth to reach Japanese incremental GDP.

Risks and brakes to growth in the future

As mentioned before, the GCC has benefited from an extended and very dynamic period of growth since the early 00s due to oil price increase. However, its average annual rate (6.1%) has been underperforming the aggregate of 45 emerging markets (6.6%), and especially the EAGLEs (7.2%). The exception was Qatar, which, as a result of a sizeable enhancement of liquefied natural gas capacity, recorded an outstanding 16.3% annual growth rate, tripling its size in only 8 years time and doubling the GDP of Oman, which shared similar numbers in 2002. In the next 10 years, things are not rather different, with expected annual growth of 4.4% for the GCC countries and a 6.1% forecast for the 45 EM as a whole and 6.6% for the EAGLEs.

The question is then, why is it that GCC countries have not benefited more (and will probably not benefit more) from the historical-high oil prices?

To analyze this, we will rely on the macroeconomic risks and potential growth brakes presented in Section 2[21]. Regarding macroeconomic risks, two issues raise especial concern. The first one is obvious and has to do with commodity exports dependency, amplified in the case of the UAE, Bahrain and Oman due to its relatively high trade openness. The second one is related to the growth model. On one side, labor force is expected to increase at a very high rate in the next ten years (more than a 20% on average), contributing to the bulk of expected growth, but, on the other side, some fundamentals for TFP gains are not very strong. It is true that quality of infrastructure is better than average (a score of 5.5 out of 7 and versus a 4.3 for the 45 EM), boosted by oil revenues boom, but GCC countries lag in terms of R&D expenditure and tertiary education enrolment. It has to be reminded that it has been ample liquidity the base of dynamism in the non-oil sector, with not a significant share of resources channeled to sectors that could lead diversification and future production capacity out of hydrocarbons.

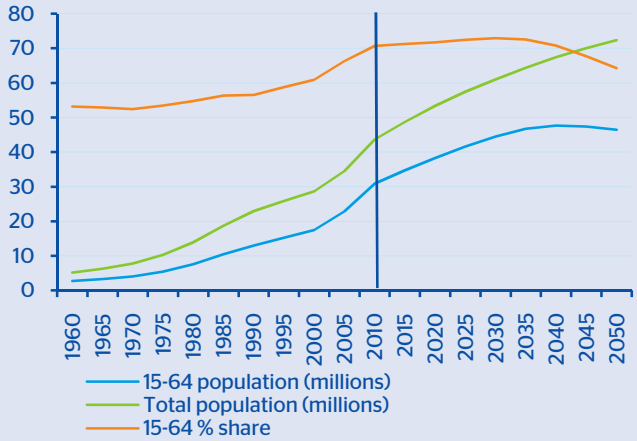
On the positive side, as mentioned before, no significant macroeconomic disequilibria are present thanks to oil revenues, reminding the exception of Bahrain, which is expected to keep a significant fiscal deficit in following years (an average of 9% for the 2012-2016 period according to IMF forecasts). Besides, in the external sector, although product concentrated, geographic diversification is higher, with less exposure than average also to China (less than 5% except Kuwait, with around 10% of total exports).

With respect to obstacles to growth, institutional considerations are good, both in terms of investment climate and public issues, outperforming in most of the cases the 45 EM average. Not enough data is available to analyze inclusive growth challenges, but income distribution is for sure a concern in the GCC countries, less likely to generate a middle class out of their dynamism in comparison with much more diversified emerging economies. More important, however, are those concerns related to social unrest risks, especially considering what is going on in other countries of the Middle East. In terms of food prices shocks, all countries show on or below average import dependency and relatively low shares of food in the CPI basket (around 15%), except for the case of Saudi Arabia and Oman (more than 25%). Regarding the labor market, information is not as good as desired, but not a general bad picture could be hiding potential problems. In addition to the difference between unemployment rate for national and foreign workers, youth unemployment is a concern, especially when a large increase of labor force is on the horizon. The UN estimates that people between 15 and 64 years will continue growing in the GCC countries until 2040 and the share in total population will not reach a peak until 2030. Therefore, inability to create enough jobs for the new labour force could eventually lead to spread of social unrest, under control until now.

21: See Section 2 for definition of variables and information sources.

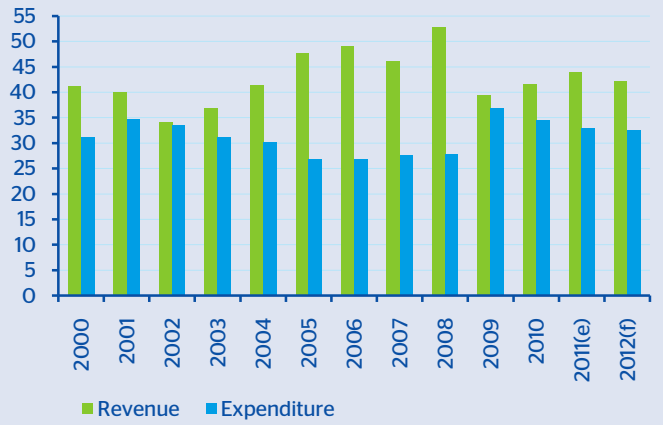
Perspectives for the oil price are a key element for economic and social dynamics in the GCC countries. In this respect, Asian development process is here to remain, and it will keep being a commodity intensive growth model. Energy consumption ratios are still very low and in closing the gap with developed countries they will require large amounts of oil. In this context, prices are not expected to experience significant corrections (and therefore GCC countries fiscal and external revenues). Moreover, domestic supply and geopolitical risks are very present at these moments, increasing upward pressure on prices. Only a world double-dip recession will alter this scenario, but long term trends will however remain.

Chart 48
GCC countries: labor force dynamics (1960-2050)



Source: BBVA Research and IMF

Chart 49
GCC countries:
general government revenue and expenditure (% of GDP)



Source: BBVA Research and IMF

In any case, in this unlikely very adverse scenario, the GCC countries could face very high economic and social pressure. On the economic side, even though the fiscal position has been outstanding and public debt has been reduced, according to IMF estimations[22], the fiscal break-even oil prices have jumped for all the GCC countries in the last years; around USD 20 per barrel between 2008 and 2011 in the case of Bahrain, Saudi Arabia, Kuwait and Qatar, and around USD 60 in the UAE. The exception is Oman, with no significant change, although it remains as one of the countries with the highest break-even prices, close to USD 80 per barrel, as in the case of Saudi Arabia and the UAE. Bahrain shows the highest figure (around 100 USD/barrel) and Qatar and Kuwait the lowest (40 and 50 USD/barrel respectively).

This increase in the break-even oil prices is the result of expansionary fiscal policies to weather the financial crisis and to derail potential social unrest. Evidence is found in this respect in the increase of public expenditure between 2006-2008 and 2009-2011, an average of 6pp from 28% to 34% of GDP, with the largest growth in Saudi Arabia and the UAE (around 10pp, being the former the highest among the GCC countries, 43%, and the latter the lowest, 24%) and the lowest one in Qatar (only a 1 percentage point increase).

Therefore, if global economic outlook worsens significantly, eventually causing a sharp decline of oil prices, governments in the GCC countries will face problems to keep balance between macroeconomic disequilibria and social discontent, as the loss of oil revenues could dampen current welfare policies. The outcome of this negative scenario should reinforce policy efforts to improve global competitiveness and foster sector diversification, while the social agenda should be aimed to shift from often generous (and regressive) oil-related subsidies (on fuel, electricity and water prices) to some kind of conditional transfers program inside a more broad-based development of safety nets.

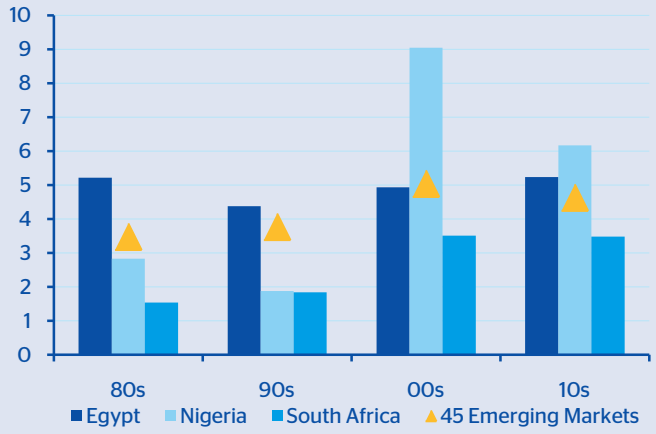
22: IMF Regional Economic Outlook for Middle East and Central Asia (October 2011), www.imf.org/external/pubs/ft/reo/2011/mcd/eng/pdf/mreo1011.pdf

Box 4. EAGLEs in Africa? Not for the time being

The concept of EAGLEs incorporates emerging markets which contribute to the world growth as measured by incremental GDP larger than that of the average G6 economies (i.e. the G7 excluding the US) in the next 10 years. The only African economy that matched this criterion last year was Egypt, which however, has fallen out in the revised group due to an expected grim performance in the short run as a consequence of the political turmoil. It is now one of the African members of the Nest, which is the watch list of economies that could join the EAGLEs club if their growth prospects improve in the coming years, along with South Africa and Nigeria.

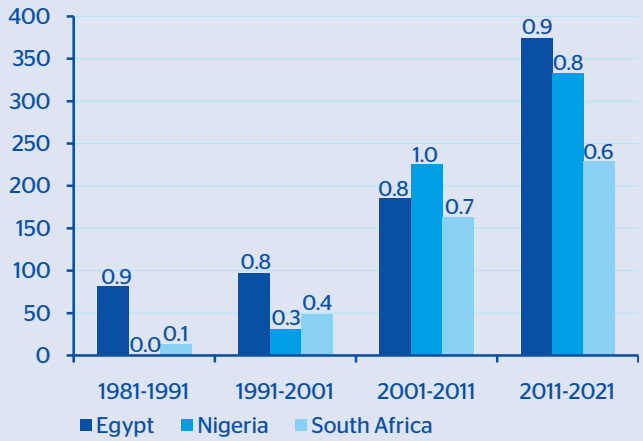
South Africa is the largest economy in the region. In our projection, it will grow at around 3.6% annually and contribute USD 229 billion to the world incremental GDP over the next ten years, a figure much higher than the threshold required for the Nest country classification. Nevertheless, South Africa needs a growth rate of 5.7% in the next ten years in order to enter into the EAGLEs group. It will not be an easy task to achieve this growth rate in view of their external and internal positions. Domestically, the poor demographic prospects and the structural difficulties in improving the functioning of the labor market continue to act as obstacles to further development[23]. Externally, the gloomy European outlook has added main risk to its short-term growth prospects given that European countries have long been the major trading partners, investors and aid donors of South Africa.

Chart 50
Nest members in Africa: real GDP LCU growth rates (%)



Source: BBVA Research and IMF WEO

Chart 51
Nest members in Africa: contribution to World economic growth and incremental GDP PPP (billion USD)

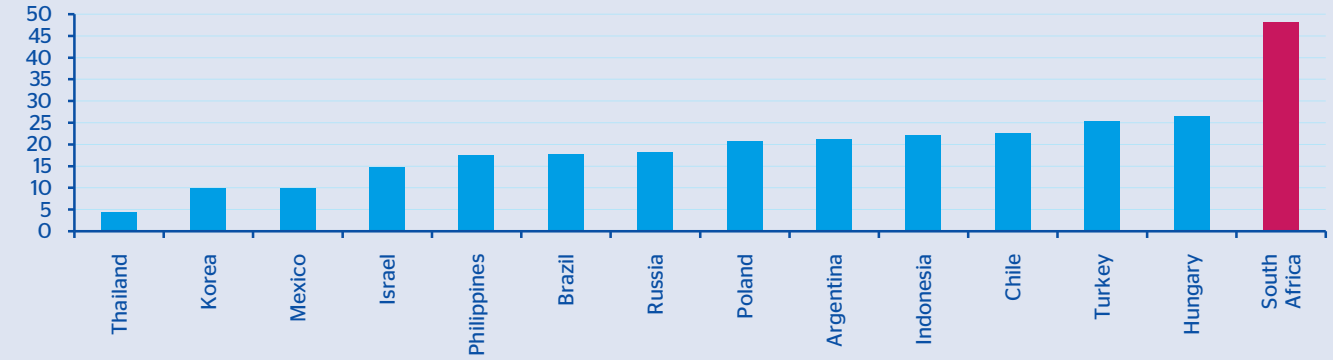


Note: Figures above columns indicate the contribution to World economic growth (%)
Source: BBVA Research and IMF WEO

The political turmoil and social unrest in the first quarter of 2011 seriously hit Egypt's economy, dragging down its output. The country became the first one dropping out of EAGLEs. In Economic Watch in March 2011 "Can Egypt continue to be an EAGLE?" we portrayed two scenarios about how the crisis would affect the country's growth prospects. The current situation is almost consistent with our benign scenario in which we expected growth to barely reach the minimum incremental demand to retain its EAGLEs status. Although was unsuccessful in retaining its position, its incremental GDP between 2011 and 2021 is slightly below the threshold to be an EAGLE (USD 374 billion for Egypt versus USD 405 billion for G6 average). From our analysis, Egypt will experience a drop in its GDP growth rate in 2011 and 2012, but then is expected to quickly recover back to its long-term growth path. Meanwhile, we expect that Egypt will still outperform South Africa in the coming ten years and overtake its position as the largest African economy as early as 2016 which is longer than our last year projection of 2013, measured in PPP terms.

23: South Africa: 2011 Article IV Consultation - Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for South Africa. Series: Country Report No. 11/258 August 25, 2011.

Chart 52
Unemployment rate of the youth: percent of total labor force ages 15-24 (2009)

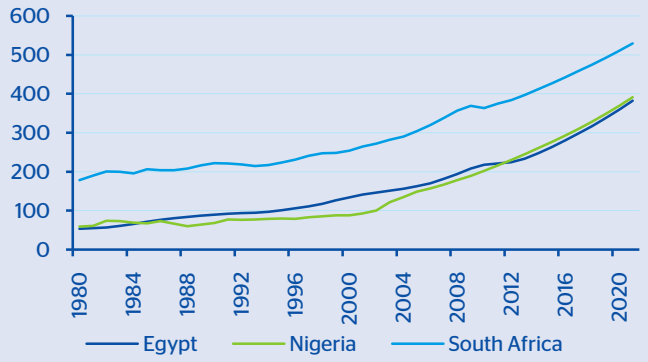


Source: BBVA Research and World Bank (WDI)

The transition to a new, more democratic political system also offers an opportunity to Egypt. Rich writing has focused on the link between democratization and growth, but without shedding much light over its sign or causality. Relying on Polity IV Project[24], a database on political transition, we confirmed the hypothesis that the democratization process can be a window of opportunity. As long as the country can improve its institutional factors, from stringing the rule of law, to controlling corruption more efficiently, or reducing bureaucratic hurdles, we could expect positive externalities over entrepreneurial activity, and ultimately over investment.

The third African economy having the Nest status, Nigeria, has a relatively smaller size compared to South Africa or Egypt, but the highest growth rate over the next ten years (6.2%). It has advantages in agricultural, mineral, and hydrocarbons endowment with a large population and is expected to contribute more to world output than South Africa between 2011 and 2021.

Chart 53
Nest members in Africa: real GDP (billion USD)



Source: BBVA Research and IMF WEO

Chart 54
Nest members in Africa: real GDP PPP (billion USD)

Source: BBVA Research and IMF WEO

Table 9
Estimated and Required growth rate in order to become an EAGLE between 2011-2021 (%)

	Estimated rate	Required rate	Difference
Egypt	5.7	6.1	0.4
Nigeria	6.2	7.1	1.0
South Africa	3.6	5.7	2.1

Souce: BBVA Research and IMF WEO

With the discussion above and a comparison between their estimated growth rate and the rate required to become an EAGLE, we can draw some conclusions for these African economies. Egypt's falling behind will only be temporary and it is set to regain its EAGLEs' status back. Nigeria needs to advance one more percentage point in order to join the EAGLEs club as a result of its smaller size. It is not impossible to achieve this rate considering its spectacular real GDP growth rate of 9.1% during the last decade. South Africa is hampered by both internal and external factors and requires a rate of 5.7% which it has never reached in past decades.

24: The data base includes a variable (regtran) that allows singling out those cases where there is a substantive, normative change in political authority towards democratization. For the detail explanation of methodology we employed, please refer to Economic Watch: "Can Egypt continue to be an EAGLE?" March 2011.

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