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- Update of forecasts for the 2014-2024 horizon
- The role of EAGLEs and Nest in the global economy
- Update of middle classes projections
- Inequality concerns
- Balance of risks
Short-term headwinds for emerging economies but long-term gap remains relative to developed markets

Emerging economies lost momentum in 2014, but they will recover its growth’s pace in the long run, maintaining the gap with the developed world.

We expect emerging countries to grow 5.5% YoY in 2024 from 4.2% yoy in 2014.

Developed economies will grow 2.2% YoY in 2024 from 1.8% YoY in 2014.

As a whole, the world economy will grow 4.3% YoY in 2024 from 3.2% YoY in 2014.

Source: BBVA Research, IMF
The recent update of Purchasing Power Parities (PPPs) lifts further the share of the emerging world in world’s GDP.

The new set of PPPs considered by the IMF has supposed a substantial increase in PPP-adjusted GDP levels for most of the emerging economies, while the figures remained almost unchanged in developed economies. Then, with the PPP revision, emerging economies reached developed countries in terms of GDP share 5 years before than previously considered.
Global growth will be concentrated in the Asia-Pacific region, which will account for 76.5% of the increase in GDP between 2014 and 2024.

The role of EAGLEs & Nest in the global economy
BBVA EAGLEs: a reminder of the methodology

Step 1: Estimating GDP level in the next decade

Step 2: Calculating incremental GDP

See the annex for further information.
## BBVA EAGLEs and Nest 2015 membership

<table>
<thead>
<tr>
<th>EAGLEs (14)</th>
<th>G6 average</th>
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<tbody>
<tr>
<td>China, India, Indonesia, Russia, Mexico, <strong>Nigeria</strong>, Saudi Arabia, Brazil, Turkey, <strong>Philippines</strong>, Pakistan, Iraq, Bangladesh, Thailand</td>
<td>Incremental GDP 2014-24 = USD 475bn</td>
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<table>
<thead>
<tr>
<th>Nest (16)</th>
<th>Non-G7 DMs &gt;USD100bn</th>
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<tr>
<td>Malaysia, Egypt, Colombia, Vietnam, Poland, <strong>UAE</strong>, Iran, <strong>Myanmar</strong>, Kazakhstan, Qatar, <strong>Algeria</strong>, Peru, Argentina, South Africa, Chile, <strong>Sri Lanka</strong></td>
<td>Incremental GDP 2014-24 = USD 168bn</td>
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</tbody>
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Rest of emerging economies

See the annex for further information.
BBVA EAGLEs and Nest 2015 membership are balanced across the globe.

Emerging markets will account for 78% of global growth between 2014 and 2024, with EAGLEs contributing up to 62%, the Nest group 9% and other emerging countries another 7%.
**Revision of PPP-adj. 2014 USD GDP (USD bn)**

Saudi Arabia would have become an EAGLE in 2014 regardless of the PPP revision. Thailand, Bangladesh and Iraq also became EAGLEs members in 2014, but they rank at the bottom very close to the EAGLEs threshold.
Evolution of EAGLEs and Nest membership over time

New PPP projections have significantly increased the EAGLEs group in 2014, while the Nest group’s size remains almost unchanged.
**Contribution to world growth 2014-24**

**PPP-adj. 2014 USD GDP (USD trn) % of world growth**

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>China</td>
<td>14.6 (28%)</td>
<td>7.7 (15%)</td>
</tr>
<tr>
<td>EAGLEs-11*</td>
<td>7.4 (14%)</td>
<td>5.1 (10%)</td>
</tr>
<tr>
<td>India</td>
<td>4.7 (9%)</td>
<td>3.7 (7%)</td>
</tr>
<tr>
<td>US</td>
<td>3.6 (7%)</td>
<td>2.9 (6%)</td>
</tr>
<tr>
<td>Nest</td>
<td>15%</td>
<td>14%</td>
</tr>
<tr>
<td>Other EMs</td>
<td>10%</td>
<td>7%</td>
</tr>
<tr>
<td>Non-G7 DMs</td>
<td>4%</td>
<td>6%</td>
</tr>
<tr>
<td>G6</td>
<td>28%</td>
<td>14%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>7%</td>
<td>4%</td>
</tr>
</tbody>
</table>

NB: *EAGLEs ex China, India and Indonesia
Source: BBVA Research, IMF

**China and India will lead global growth contributing 28% and 14% respectively between 2014 and 2024. Their rapid growth is behind the boom of the middle classes in the emerging world.**
Russia, Mexico and Nigeria will contribute more than any developed country. Saudi Arabia, Brazil and Turkey will add more to the increase of world GDP than Germany and UK.
Malaysia ranks at the top of the Nest group. Egypt, Colombia, Vietnam and Poland show contributions to global growth comparable to those from large developed economies.
Update of Middle Classes projections
The Emerging Middle Classes revolution will accelerate

There has been a dramatic reshaping of global income distribution since 2000 led by an unprecedented reduction in poverty rates as well as by the rapidly growing middle classes in the emerging economies. This will continue in the coming years.

We expect emerging countries to increase their share of the global medium-high middle classes and affluent segments from 24% in 2000 to 67% by 2025.

NB: Based on PPP-adjusted 2010 USD; Poor and Low Income (<USD5,000), Low Middle Class (USD5,000-15,000), Medium Middle Class (USD15,000-25,000), High Middle Class (USD25,000-40,000), Affluent (>USD40,000).
Source: BBVA Research, UN, WB, IMF

See “Flourishing middle classes in the emerging world to keep driving reductions in global inequality”, BBVA Research. See the annex for further information.
Flourishing middle classes in the emerging world are reducing global inequality

The expansion of the middle classes has contributed to a rapid decline in global inequality, which will reduce further even assuming no changes in domestic income distributions.

However, levels of GINI index will remain high on cross-country standards, with a GINI index similar to those recorded today in Africa and Latin America.

Global GINI index (1980-2025f)

NB: The GINI index is calculated with percentile GDP per capita including data for 90 countries covering over 90% of the world population.
Source: BBVA Research, UN, WB, IMF

See “Flourishing middle classes in the emerging world to keep driving reductions in global inequality”, BBVA Research. See the annex for further information.
Asia leads the reshaping of global income distribution…

Change of population (mn) by GDP per capita and region (2000 to 2025f)

Medium-high middle classes and affluent segments will increase from 24% in 2000 to 67% in 2025 in Emerging Countries.

Emerging Asia is the largest contributor to this reshaping of the world’s income distribution with a new middle class of 2658 mln living there.

The share of the wealthier segments is on the rise in Africa, Latin America and Emerging Europe.

Source: BBVA Research, UN, WB, IMF
...leading creation of the Middle Classes with pro-poor growth. Latam growth has been more inclusive.
As countries develop from low income to middle and high income levels, the relative demand for basic products declines substantially, while the opposite happens with discretionary products.

Korea is a good example of this. The country has developed extraordinarily rapidly, increasing its GDP per capita five-fold between 1980 and 2010 and transitioning from low to high income levels.
Inequality concerns
Inequality as a by-product of the development process (Kuznets Inverted U curve)

Unprecedented growth in emerging economies during the last 15 years has brought an impressive reduction of poverty and a boom in the middle classes.

However, the decline in global inequality has taken place at the expense of more uneven income distributions in large Asian economies and only a slight smoothing of high inequality in Latin America.

Source: BBVA Research, WIID, IMF

Note: see “Tackling excessive inequality as a critical ingredient for sustainable development in the emerging world”, BBVA Research.
The Kuznets curve seems to hold from a historical perspective

The global economy’s development over time shows the inverted-U relationship between economic development and inequality (Kuznets curve) from the Roman Empire to US and China.

Note: According to Kuznets curve theory, income inequality would be a by-product of growth in early stages of development as urbanisation and the shift to more productive activities increase the gap with rural areas, and the capital share rises. Thereafter, this upward trend is stabilised and eventually reversed at some point, following transition to medium-high income levels. See "Tackling excessive inequality as a critical ingredient for sustainable development in the emerging world", BBVA Research
Beyond Kuznets curve, redistribution and human capital play key roles

Our cross-country analysis exercise shows that redistribution policies and labour market dynamics are key determinants in tackling inequality. This relationship appears more intense in developed countries, which present lower GINI indices.

Source: BBVA Research
Redistribution requires stable and adequate fiscal revenues

**GINI index in OECD countries before and after taxes and transfers (late 00s)**

**General government revenue (% GDP) (2014)**

**Redistribution policies** in developed countries have proved to be effective in reducing inequality. To use redistribution policies, **emerging countries need to increase fiscal revenues**, especially in South-east Asia, Mexico and the Andean countries in Latin America, where fiscal revenues are around 20% of GDP compared to 40% in G7 economies.
Education is also crucial to guarantee equality of opportunities… Spending on education will discriminate between and within countries.

Educational gaps are crucial determinants to fight inequality. Large gaps remain between countries.

Public expenditure on education in emerging countries is very low compared with developed standards.

Reducing these gaps will be important in tackling inequality.

Source: BBVA Research, WB and IMF
...although it must be accompanied by good infrastructure

Quality of overall infrastructure (1-7)
(2013-14)

Poor quality of infrastructure harms competitiveness and may eventually become a serious bottleneck for further growth.

The challenges to developing infrastructure are huge, given the low fiscal revenues, leading necessarily to consideration of alternative financing sources such as regional banks, private-public partnerships or portfolio diversification by global lenders.

NB: Countries are ranked according to their real PPP-adjusted GDP per capita in 2013
Source: BBVA Research, WEF
Financial inclusion rather than size is a key factor in tackling income inequality…

Average of GINI index for income groups / regions and financial inclusion conditioned on GDP per capita

Financial inclusion contributes significantly to more equal income distribution, having a larger incidence in low and medium-income countries, particularly in Emerging Asia and Africa.

Note: Values above average correspond to residuals of regressions on GDP per capita (level and square values) that are one standard deviation above mean (0). See García-Herrero A., Martínez Turégano D., 2015, “Financial inclusion, rather than size, is the key to tackling income inequality.”
...and there is still plenty of room for improvement in emerging markets

BBVA Research Multidimensional Financial Inclusion Index

Countries ordered by the degree of financial inclusion.
Source: BBVA Research

Note: the degree of financial inclusion is determined by three dimensions: usage, barriers and access. These dimensions are, at the same time, determined by several demand-side individual level indicators for the cases of usage and barrier, and supply-side country level indicators for access. Weights assigned to the dimensions are determined endogenously. See Cámara N., Tuesta D., 2014. “Measuring Financial Inclusion: A Multidimensional Index”, BBVA Research.
Balance of Risks
Geopolitics will dominate Eurasia and Middle East, but more hot spots need to be monitored

BBVA World Conflict Heatmap (from 2H 2014 to Mar 2015)
(Number of conflicts / Total events)

Ukraine-Russia
A new ceasefire agreement was reached, but is still very fragile

Instability in Middle East
Fighting continues in Syria and Iraq and is now spreading to North Africa. Yemen conflict escalates

Some pressure in Asia
The risk of Social unrest in Hong Kong and territorial disputes in South East Asia Sea

Source: www.gdelt.org & BBVA Research
The Global Awakening has spiked after years of calm

World Protest Intensity Map 1979- Mar 2015
(Number of protests / Total events. Dark Blue: high intensity)

There was some revival of instability on the EU but less intensive than during the early 80’s and it’s softening now...

EM Europe and CIS countries are facing increasing social unrest...

The Arab Spring spread protests across the Middle East region. Some countries remain under tensions...

Source: www.gdelt.org & BBVA Research
Portfolio flows to EM adjust as policy normalisation in the West is becoming closer...  

The monetary policy reactions in developed economies after the financial distress and favorable conditions in terms of economic growth and lower risk premia triggered supporting global push and pull factors for flow dynamics across Ems, leading to strong and sustained flows into them (phase 2).  

However, the announcement of the normalisation of monetary stimuli, the recovery of Developed economies and lower appeal of Ems is triggering a portfolio rebalancing in favor of DM. (phase 3).
…but still global factors dominate the correction of flows so far. However, some local strains have emerged.

Emerging Markets flows
(Median Emerging Market portfolio flow breakdown as per BoP, monthly change in %)

Emerging Markets flows’ drivers
(Median Emerging Market portfolio flow decomposition, in % change MoM)

Global Factors dominated the reallocation at the end of 2014 and the beginning of the first quarter of 2015. However, high frequency data reveal that idiosyncratic elements are also emerging.
The Fed will dominate and the ECB’s push will only partially compensate

Monetary policy in the north and flows in the south (alternative QE, Fed and ECB scenarios)
Cumulative response of portfolio flows in USD bn, forecast made at end 2Q14

EM Flows will continue to be challenged by Monetary Policy normalisation by key Central Banks…

… but part of the adjustment have already been materialised

Source: IMF, BBVA Research
Beyond flows adjustments, commodity exporters will have to adapt to lower prices…

Commodity prices, especially the oil price, have experienced a declining trend since 2011, introducing important challenges and potential risks for exporting countries.
Emerging Markets asymmetry in oil dependence…

Trade balance (% of GDP) (2013)

Average fuel deficit of 6% of GDP

Oil-producing countries suffer the sharp drop of oil prices, but some other emerging countries from Asia, such as India and Phillipines, and also Turkey benefit from cheaper energy.
...explains the different sentiment to the sharp fall in oil prices across countries

The world sentiment to the drop in oil prices

Source: BBVA Research and www.gdelt.org
See “Very low energy prices and geopolitical risks”, BBVA Research.
The contribution of the Emerging World to global growth is bound to be even bigger than we had initially projected, due to recent updates in purchasing power parity estimates across the globe. In fact, in 2024 they will have an almost two-thirds share of the global economy.

There are now more countries included in our EAGLEs list. The new additions come mainly from Asia and the Middle East.

The creation of a new middle class is well underway and this will continue to push consumption.

A flourishing middle class in emerging markets, fiscal redistribution, equality of opportunities and financial inclusion will all be instrumental in reducing income inequality.

Geopolitical risk in Emerging Markets has become one of the main risks of 2015. The single-polar word is changing towards more multipolar geopolitics. Instability’s spots appear in several geographies at the same time.
Methodological issues: BBVA EAGLEs and Nest membership definition

The *reference variable* in our calculations is the *incremental GDP*, i.e. the increase of real GDP in PPP-adjusted terms during the following ten years. To compute it, we add growth forecasts to the estimate of PPP-adjusted for the starting year provided by the IMF. Our approach is therefore a mixture of size and growth.

**We update growth forecasts for the following ten years on an annual basis.** We use BBVA Research projections for those countries that we cover in depth, and IMF projections in the latest World Economic Outlook (and updates) for the remainder. In the latter case, we extend the available forecast horizon by assuming as constant the growth rate available for the last year.

After updating the growth forecasts we compute the incremental GDP for all countries in the world and then rank them from largest GDP to smallest, defining membership of BBVA EAGLEs and Nest as follows:

- The **BBVA EAGLEs** are defined as those emerging economies contributing to world growth more than the average of the G6 countries in the next ten years.

- The **BBVA Nest** is formed of those emerging economies contributing to world growth more than the average of the non-G7 developed economies, which have a PPP-adjusted GDP of over USD100bn but below the EAGLEs threshold.
Methodological issues: new PPP valuations

The IMF updated its WEO database at the end of 2014, including a new set of Purchasing Power Parities (PPPs) computed in the 2011 round by the International Comparison Program (ICP), which imply significant revisions to those computed in 2005*. In particular, among emerging economies the PPP-adjusted GDP levels have increased substantially for African and Asian countries and to a lesser extent in Latin America and Europe, while the figures have remained almost unchanged in developed economies.

* A thorough analysis on methodology changes between the 2005 and 2011 rounds is available at Deaton, A., and Aten, B., 2014, “Trying to understand the PPPs in ICP 2011: why are the results so different?”
Methodological issues: population projections

We use PPP-adjusted real GDP per capita measured in 2010 dollars. GDP values and projections correspond to the October 2014 edition of the IMF/WEO database, while population estimates and forecasts are from the 2012 revision of the UN World Population Prospects. Regarding income distributions, our starting point is the information available in the WDI/World Bank, which includes the two top and bottom deciles and all quintiles. As data are not continuous we interpolate missing data. Projections until 2025 keep distributions constant from the latest observation.

We group population according to the following five income ranges: 1/ poor and low-income (up to USD5,000), 2/ low middle class (USD5,000-15,000), 3/ medium middle class (USD15,000-25,000), 4/ high middle class (USD25,000-40,000), and 5/ affluent (over USD40,000).

The number of countries included has been extended to 90 and the current coverage accounts for over 90% of the world population:

- **Developed economies**: United States, Japan, Germany, France, United Kingdom, Italy, Korea, Spain, Canada, Australia, Netherlands, Belgium, Greece, Czech Republic, Portugal, Sweden, Austria, Denmark, Finland, Slovak Republic, Ireland, Slovenia, Estonia and Luxembourg.
- **Emerging economies**: China, India, Indonesia, Brazil, Pakistan, Nigeria, Bangladesh, Russia, Mexico, Philippines, Ethiopia, Vietnam, Egypt, Iran, Turkey, DR Congo, Thailand, South Africa, Tanzania, Colombia, Kenya, Ukraine, Argentina, Algeria, Uganda, Poland, Iraq, Sudan, Morocco, Afghanistan, Venezuela, Peru, Malaysia, Uzbekistan, Nepal, Mozambique, Ghana, Yemen, Angola, Madagascar, Cameroon, Syria, Sri Lanka, Romania, Côte d'Ivoire, Niger, Chile, Burkina Faso, Malawi, Paraguay, Mali, Kazakhstan, Guatemala, Ecuador, Cambodia, Zambia, Zimbabwe, Senegal, Hungary, Bulgaria, Croatia, Panama, Qatar, Uruguay, Lithuania and Latvia.
To measure inequality, we use the UNU WIDER World Income Inequality Database that provides more than 7,000 observations. Why we focus on it?

- Data availability with a fair geographical and time balance
- High ratio of observations adjusted by household composition
- Much better data quality
- Better approach to inequality among income measures

Period of analysis:

- Panel data
- Cross-section
- Annual observations
- 10-year average for seven periods
This report has been produced by Emerging Markets Unit, Cross-Country Analysis Team

Chief Economist for Emerging Markets
Alicia García-Herrero
+852 2582 3281
alicia.garcia-herrero@bbva.com.hk

Chief Economist,
Cross-Country Emerging Markets Analysis
Álvaro Ortiz Vidal-Abarca
+34 630 144 485
alvaro.ortiz@bbva.com

Gonzalo de Cadenas
+34 606 001 949
gonzalo.decadenas@bbva.com

David Martínez Turégano
+34 690 845 429
dmartinezt@bbva.com

Alfonso Ugarte Ruiz
+ 34 91 537 37 35
alfonso.ugarte@bbva.com

Tomasa Rodrigo
+3491 537 8840
Tomasa.rodrigo@bbva.com
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