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MACRO RESEARCH FOR DEVELOPMENT
An IMF-DFID Collaboration

Department for International Development

Modernizing Monetary Policy Frameworks

The IMF-DFID team continues to collaborate closely with selected central banks in sub-Saharan Africa and IMF country teams to modernize the practice and analysis of monetary policy. As part of this initiative, a book titled Monetary Policy in Sub-Saharan Africa was published in April 2018. The book draws on years of DFID-funded research and practice at the IMF and in central banks and explores the challenges and choices faced by the central banks in monetary policymaking, and to provide practical tools and policy guidance. A key feature of the book is the application of dynamic general equilibrium models, suitably adapted to reflect key features of low-income countries, for the analysis of monetary policy in sub-Saharan African countries.

IMF experts participated in and helped facilitate the meeting of the East African Community's Technical Working Group on Forecasting and Policy Analysis System (FPAS), which took place in Uganda in May 2018. The working group initiative is a unique platform for knowledge-sharing and harmonization of FPAS development among the EAC Partner States' central banks. Additionally, the IMF organized customized training missions on modelling and forecasting to Tanzania (February 2018), Malawi (March 2018), and Rwanda (April 2018). These missions assisted forecasting teams in central banks to further develop their quarterly projection model, streamline decision-making process, and modernize communication function, in line with best practices in emerging economies.

Fiscal Policies and Gender Equality

Sound fiscal policies can promote macroeconomic stability, which is essential for boosting growth, jobs, and incomes for all citizens. But fiscal policy can also be actively shaped to achieve gender equality goals, and this is the basic idea behind gender budgeting. The IMF-DFID team conducted a global study of gender budgeting initiatives and the book, Fiscal Policies and Gender Equality, summarizes prominent efforts in more than 80 countries. It also offers lessons learned, good practices, and suggestions for improving current and future gender budgeting initiatives. In addition, the team coordinated with UN Women to offer a TED-style talk on gender budgeting at the IMF Spring Meetings and a panel discussion on transformative gender budgeting practices for rural women at the UN Commission on the Status of Women.

Globalization and Inequality

Globalization stirs a diverse range of sentiments and views: some credit globalization for boosting economic well-being while others blame it for worsening inequality. In a new paper, the authors examine the effect of globalization on income among and within countries in a new panel of 147 countries during 1970-2014.The paper's main finding is that the effect of globalization on average income growth crucially depends on a country's prevailing level of globalization. While globalizing is generally good for growth, there are diminishing marginal returns. The growth gains are substantially positive for countries at early and medium stages of the integration process, notably middle and low-income countries; while for countries at very high stages of globalization, income gains are small or insignificant. The study reveals that globalization is often associated with widening economic inequality. While in the average developing economy the poor also benefit from globalization, in many advanced economies, globalization often has little effect on the incomes of the poor. But government policies matter: the paper shows that investments in education that raise skill levels, as well as taxes and transfers that spread the benefits more broadly, can help globalization to be a more inclusive process generating gains for all. The paper was also a topic of VoxEU column and IMF Blog.

Are Remittances Good for Labor Markets in the LICs, MICs, and Fragile States?

Remittances appear to have a strong impact on both labor supply and labor demand in recipient countries. These effects are highly significant and greater in size than those of foreign direct investment or official development aid. On the supply side, remittances reduce labor force participation and increase informality of the labor market. In addition, male and female labor supply show significantly different sensitivities to remittances. On the demand side, remittances reduce overall unemployment but benefit mostly lower-wage, lower productivity non-tradables industries at the expense of high-productivity, high-wage tradables sectors. As a consequence, even though inequality declines as a result of larger remittances, average wage and productivity growth declines, the latter more strongly than the former leading to an increase in the labor income share. In fragile states, in contrast, remittances impose a positive externality, possibly because the tradables sector tends to be underdeveloped. Our findings indicate that reforms to foster inclusive growth need to account for the role of remittances to be successful.

Domestic Fuel Price Changes and Export Growth in Developing Countries

The team made a presentation on Domestic Fuel Price Changes and Export Growth in Developing Countries at a seminar organized by the Center for Studies and Research on International Development (CERDI, University of Auvergne, France) in May. The findings of the paper point to an adverse but short-lived effect of fuel price hikes on exports. Moreover, this effect is only observed in countries with high energy dependency and where access to an alternative source of energy is constrained. Given the long-standing issue of sizeable fuel subsidies—which have been shown to be fiscally costly, inequitable and bad for the environment—countries seeking to reduce them should not be overly concerned about the impact on export competitiveness. Mitigating measures and structural reforms that focus on reducing energy inefficiencies and enhancing access to other sources of energy should help a long way in minimizing any potential adverse consequences of higher fuel prices for exports.

Dominica and Income Inequality

The team participated in the IMF Article IV mission to Dominica and presented the resilience building tool developed and customized for small states with natural disasters. The key results were illustrated in the Selected Issues Paper and Staff Report for Dominica and presented at the

Ministry of Finance with attendees from the National Resilience Development Committee, the Chamber of Commerce, and the Ministry of Finance in Dominica. The results show that both the long-run economic growth and short-run recovery depend crucially on the level of resilience. The analysis reveals that the return of investing in resilient capital is higher than the cost associated with it and that a more resilient economy leads to higher private investment and lower brain drain.

Economic Fluctuations in Sub-Saharan Africa

The authors compare business cycle fluctuations in Sub-Saharan African (SSA) countries vis-à-vis the rest of the world. The main results are as follows: (i) African economies stand out by their macroeconomic volatility, which is reflected in the volatility of output and other macro variables; (ii) inflation and output tend to be negatively correlated; (iii) unlike advanced economies and emerging markets (EMs), trade balances and current accounts are acyclical in SSA; (iv) the volatility of consumption and investment relative to GDP is larger than in other countries; (v) the cyclicality of consumption and investment is smaller than in advanced economies and EMs; (vi) there is little co-movement between consumption and investment; (vii) consumption and investment are strongly positively correlated with imports.

The Economic Impacts of Revenue Mobilization in Resource-Rich Sub-Saharan Africa

This analysis, focusing on the CEMAC region, provides lessons applicable more broadly to sub-Saharan Africa economies. It shows that revenue mobilization is a particularly powerful means to reduce government indebtedness, but it may also generate undesirable effects on inequality. This highlights the need to adopt mitigating policies, in particular, cash transfer programs targeted to the most vulnerable, especially if the specific revenue mobilization instruments are likely to affect poor households' incomes.

Improving Governance: General Equilibrium Analysis Using a Macroeconomic Model

The Debt, Investment, and Growth model developed by Buffie and others (2012) is extended to capture reforms in the areas of governance. The general equilibrium nature of the DIG model makes it possible to analyze the impact of reforms simultaneously on output, private investment, consumption, and fiscal outcomes. The team analyzed the effects of improvements in three key aspects of governance: (i) a reduction in bribes and other distortions that discourage firms from investing and creating jobs; (ii) an increase in public investment spending efficiency; and (iii) a decline in tax evasion.

For more information, please contact MacroResDev@imf.org or visit the IMF-DFID Macroeconomic Research for Development website.