

# Chapter II

Trends in International Markets

## A. INTRODUCTION

The extent to which the global economy is fragmenting and the consequences for its growth and stability are pressing questions for policymakers everywhere – and there are no clear answers. A discernible trend is the emergence of a rigid and fragile global economy after the global financial crisis (GFC). If this trend continues and becomes reinforcing, the damaging consequences for developing countries are likely to be significant.

The vulnerability of developing countries stems from the way the key international markets on which many depend have become both more concentrated and more volatile. This, as discussed in previous United Nations Conference on Trade and Development (UNCTAD) reports, is particularly true of financial markets, but the way innovative financial instruments, in the form of futures and options contracts, swaps, derivative instruments and so on, have allowed a handful of market speculators to influence the price of key commodities, such as food and energy, is clearly apparent in the current context. The vulnerability of developing countries is exacerbated by the lack of global safety nets to cushion the blow and repair the damage from unexpected shocks, such as the Covid-19 pandemic, and by the lack of policy coordination to ensure their vulnerabilities are taken into account when systemically important countries are pursuing their own policy agendas.

Given the unfavourable direction of the global economy outlined in the previous chapter, an immediate concern is the dangerous level of debt distress facing a growing number of developing countries. This is discussed in the next section. Section C explains how the breakdown of supply chains is raising wider concerns about the strength and direction of trade flows, whilst section D turns to the financialization of commodity markets.

## B. GLOBAL FINANCIAL CONDITIONS AND DEVELOPING COUNTRY VULNERABILITIES

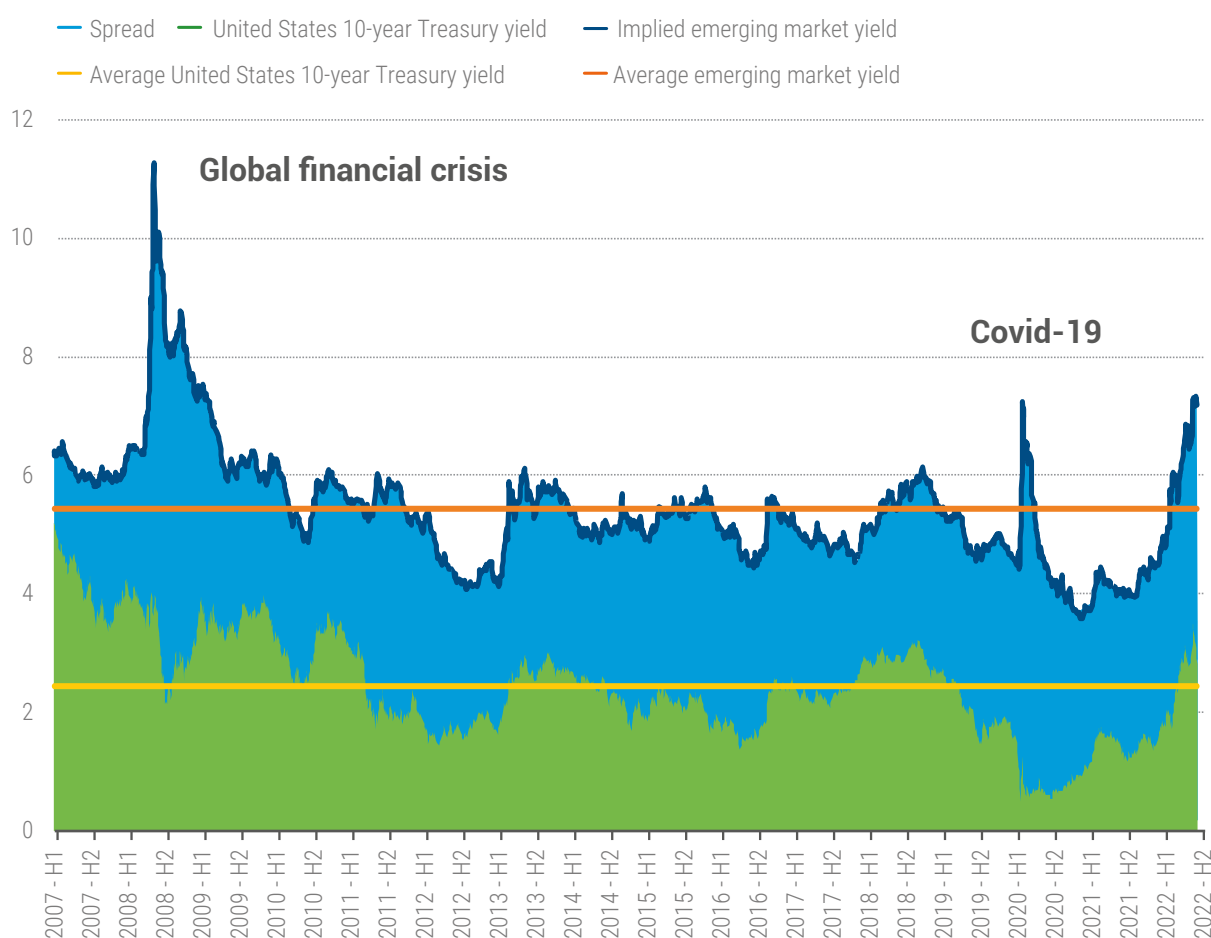
Over the decade and a half since the global financial crisis, many developing countries have seen their external financial positions deteriorate, first gradually and particularly since the Covid-19 shock more precipitously. As of mid-2022, the IMF assessed 55 per cent of Poverty Reduction and Growth (PRGT)-eligible countries<sup>8</sup> to be at high risk of or already in debt distress – compared to fewer than 30 per cent in 2015. Overall, the IMF has warned that around 6 out of 10 low-income countries and 3 out of 10 emerging market economies are at or near debt distress.

Three immediate factors have been critical in pushing these countries further towards the financial precipice. First and foremost, after many perfunctory announcements over the past ten years, United States monetary policy has now embarked on a decisive tightening cycle that has seen the United States 10-year Treasury yield increase almost six-fold between mid-2020 and mid-2022 (figure 2.1). Given the continued dominance of the United States dollar in the world economy, this, as discussed earlier, threatens to reverse the global economic recovery, not least through balance-of-payment crises in the developing world prompted by United States dollar appreciations against their currencies and, therefore, also an increase in the dollar-denominated values of their external debt obligations and higher borrowing costs.

<sup>8</sup> The 69 countries eligible to apply to the IMF Poverty Reduction Trust Fund (PRGT) include 25 low-income, 35 lower-middle income and 9 upper middle-income countries, based on World Bank income classifications. According to the IMF Debt Sustainability Framework, 30 of these 69 countries were deemed to be at high risk of debt distress and eight in debt distress, as of 31 May 2022.

Second, price hikes in some commodity markets add to inflationary pressures on a global scale. This has negatively affected developing country commodity importers but has benefited some developing country commodity exporters. While, for now, commodity prices for gas (United States), wheat and oil have returned to near pre-war levels, uncertainty remains as to the extent to which continuation of the war in Ukraine will affect commodity prices in the future. Third, the Covid-19 pandemic lingers on in many countries. This includes high debt burdens left by the pandemic in developing countries that remain unresolved.

**Figure 2.1** Emerging market yield decomposition, 2007–2022 (percentage points)



**Source:** UNCTAD secretariat calculations based on ICE Bank of America (BofA) Emerging Markets External Sovereign Index.

**Note:** The implied yield for external sovereign emerging market bonds equals the sum of the United States 10-year Treasury yield and the spread as measured by the ICE BofA. The average spread (of around 3 percentage points throughout the period) is measured by the difference between the two average yield lines.

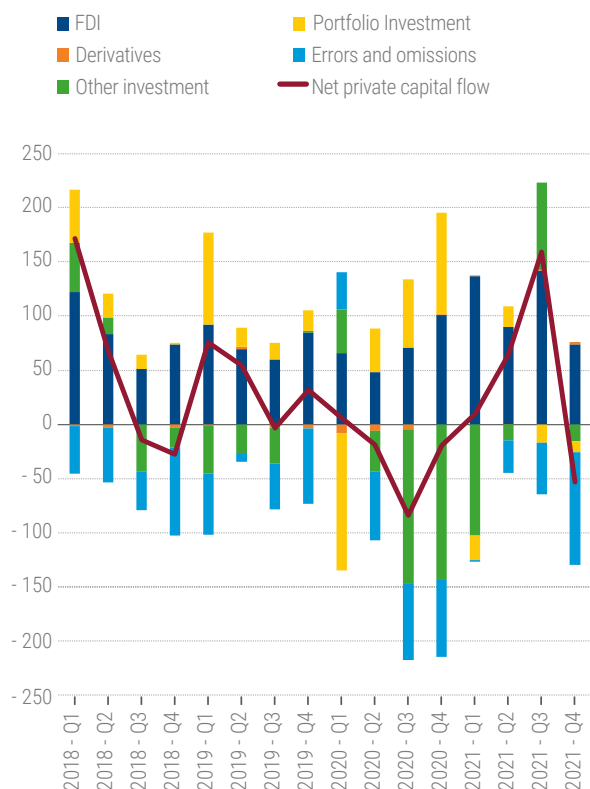
## 1. Net capital flows to developing countries: mounting headwinds

The combination of these factors has resulted in renewed net negative capital flows from developing countries since September 2021, bringing to a halt the rebound of net capital flows to developing countries observed since the last quarter of 2020 (figure 2.2.A).<sup>9</sup>

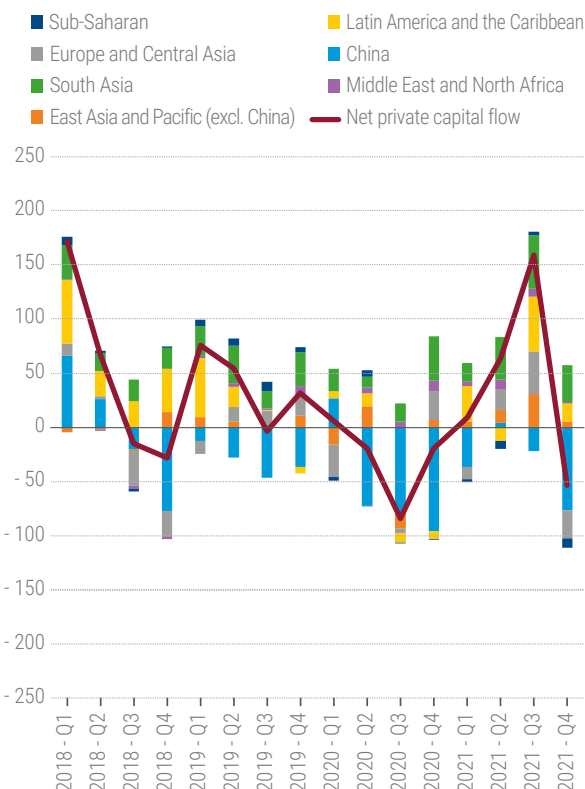
<sup>9</sup> Net capital flows refer to net non-resident inflows minus net resident outflows, including both private and official flows.

Figure 2.2 Net capital flows to developing countries, 2018–2021 (billions of dollars)

A. By type of capital flows



B. By country or country group



Source: UNCTAD secretariat calculations based on national data.

Note: Developing countries are low- and middle-income countries according to the World Bank income group classification. By region, the following countries are included: East Asia and Pacific (excl. China): Cambodia, Fiji, Indonesia, the Lao People’s Democratic Republic, Malaysia, Mongolia, the Philippines, Samoa, Thailand, Timor-Leste, Tonga, Vanuatu, Viet Nam. Europe and Central Asia: Albania, Armenia, Azerbaijan, Belarus, Bosnia and Herzegovina, Georgia, Kazakhstan, Kyrgyzstan, Republic of Moldova, North Macedonia, Russian Federation, Serbia, Tajikistan, Republic of Türkiye, Ukraine, Uzbekistan. Latin America and the Caribbean: Argentina, Belize, Plurinational State of Bolivia, Brazil, Colombia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Suriname. Middle East and Northern Africa: Egypt, Iraq, Jordan, Morocco, State of Palestine. South Asia: Afghanistan, Bangladesh, Bhutan, India, Nepal, Pakistan, Sri Lanka. Sub-Saharan Africa: Angola, Cabo Verde, Eswatini, the Gambia, Guinea, Lesotho, Madagascar, Mauritius, Mozambique, Namibia, Nigeria, Rwanda, São Tomé and Príncipe, South Africa, United Republic of Tanzania, Zambia.

This initial rebound was driven by a confluence of developments. Increases in net inflows of foreign direct investment (FDI) to developing countries in the last quarter of 2020, and again in the first and third quarters of 2021, were a main feature of this recovery phase (TDR, 2021). By contrast, net portfolio investment that had led the deterioration of net capital flows in the early phase of the pandemic, remained subdued and volatile throughout 2021, after initial rebounds in the last three quarters of 2020 when global investors in search for yield triggered record net flows of \$93 billion in the final quarter of 2020 alone (TDR, 2021). This pattern is driven mainly by non-resident portfolio flows to developing countries. However, portfolio diversification by residents in emerging-market economies has become an increasingly important component of net portfolio flow dynamics (JP Morgan, 2022). Finally, net official flows, recorded under “other investment”<sup>10</sup> played a significant role in the resurgence of capital

<sup>10</sup> Other investments include currency and deposits, trade credits and advances, private and official loans (including IMF loans and SDRs), guarantee schemes and other equities.

flows to developing countries in this period. Thus, the August 2021 allocation of special drawing rights (SDRs) as well as emergency lending by the IMF and the World Bank were the main driver behind this category's positive contribution in the third quarter of 2021.

However, with the deterioration of global financial conditions from September 2021, net capital flows to developing countries turned negative again in the last quarter of 2021, reaching \$52.3 billion or around 60 per cent of the highest net negative flows in the period of observation at the peak of the Covid-19 pandemic (third quarter of 2020). The first quarter of 2022 saw a slight recovery from this trend, with FDI inflows largely compensating for near record portfolio outflows of \$108.8 billion due to the sell-off of developing countries' bonds and equities, in part triggered by the war in Ukraine. This flight of portfolio capital was surpassed only in the first quarter of 2020 amidst the onset of the Covid-19 pandemic.

Both the initial rebound of capital flows to developing countries as well as the recent negative capital flow shock have affected developing country regions unevenly (figure 2.2.B). As previous reports have stressed, this reflects not only the dynamics of net foreign liabilities, but also the build-up of foreign assets by residents of large emerging market economies, led by China (TDR, 2019; 2021). Chinese "other investment" outflows (linked to overseas deposits, bank loans abroad and trade credit and advances) accounted for the bulk of "other investment" outflows from developing countries in the last quarter of 2020 and the first quarter of 2021.

From end-2020, when the Covid-19 crisis was seen by some to gradually come under control, through to the first quarter of 2022, South Asia was the recipient of the largest cumulative net capital inflows, equivalent to \$179 billion and led by large inflows of other investments. East Asia and the Pacific (excluding China) recorded net inflows of \$70.3 billion, linked mainly to high FDI inflows during this period. Net inflows to the Middle East and North Africa were smaller, amounting to \$36.2 billion, mainly as a result of inflows in other investment.

The remaining regions witnessed more volatile net capital flows over this period, marked by differing patterns. These were positive in Latin America and the Caribbean, a region that benefited from net positive capital inflows of \$121.5 billion since late 2020, with the bulk of these received since the third quarter of 2021. Thus, in the first quarter of 2022 alone, FDI to this region more than compensated for net portfolio outflows, resulting in net capital inflows of \$40.7 billion. These amounted to only \$9.9 billion in East Asia and the Pacific in the first three months of 2022, hovered around zero in other regions, and were strongly negative for China mainly due to portfolio outflows. Sub-Saharan Africa was the only region experiencing net capital outflows throughout the period from end-2020 and into 2022, totaling \$10.9 billion, due to portfolio and other investment outflows overshadowing official and FDI inflows. This is especially concerning given the high degree of external vulnerabilities of the region.

The overall outlook for developing countries remains subdued for now. According to the most recent data available for (selected) developing countries, the flight-to-quality from developing economies continued unabated during the second quarter of 2022, reaching levels comparable to those following the onset of Covid-19 pandemic by end-June (IMF, 2022b; Wheatley, 2022). This is also borne out in the data on emerging market sovereign bond spreads. As figure 2.1 shows, these spreads – an important indicator of sovereign financial risk and distress – have risen sharply between September 2021 and July 2022, following the United States Federal Reserve's more aggressive stance on monetary policy normalization in response to concerns about domestic inflation. Contrary to earlier episodes of steeply rising emerging market sovereign bond spreads in the wake of the global financial crisis and at the height of the Covid-19 pandemic, when 10-year United States Treasury bond yields actually fell, the current episode is clearly driven by emerging market bond spreads moving in tandem with the 10-year United States Treasury yield curve – a clear indicator of the central role played by the tightening monetary policy cycle in the United States in mid-2022.

Worst hit by these deteriorating financial conditions are primarily frontier economies that already suffered from severe balance of payment constraints and high external vulnerabilities from well before

the onset of the Covid-19 pandemic. Thus, for example, low- and middle-income countries, whose external sovereign bonds traded in distressed territory in June 2022 had already seen their bond yields rising to above 10 percentage points relative to the most common benchmark - the yield on 10-year United States Treasury bills – in mid-2019 (including Egypt, Türkiye, Pakistan, Uganda and Zambia). By contrast, for emerging market economies with larger and more liquid markets and with investment grade ratings, sovereign bond spreads have been relatively contained (Curran, 2022). This now seems to be changing to an extent, with external sovereign bonds of other larger emerging economies, such as Brazil and Colombia, seeing their bond spreads on the increase, if not yet in distressed territory (table 2.1). Given growing expectations of a United States (European Union) recession in 2023, the most likely scenario will be one comparable to earlier crisis points, in which further rising sovereign bond spreads with falling yields on 10-year United States Treasury bills.

But this only captures debt and financial distress in those developing countries that issue foreign currency-denominated sovereign bonds above minimum thresholds required for inclusion in relevant indices. Other assessment criteria include the IMF debt sustainability reports for countries eligible to apply to its Poverty Reduction and Growth Fund and, of course, countries already in default or undergoing sovereign debt restructurings as of July 2022. Table 2.1 provides a summary overview of countries meeting one or several of these criteria, at the time of writing.

Predictably, these developments have also resulted in widespread currency depreciations across developing countries in the first half of 2022 (figure 2.3). In addition to widening spreads of developing countries' external sovereign bonds, domestic currency depreciations further increase the servicing costs of debt denominated in foreign exchange. In all, 90 developing countries recorded nominal depreciations of their currencies against the dollar, of which 34 exceed 10 per cent. Countries with major depreciations are either net food importers and/or those with long-standing high external vulnerabilities. Those with only small depreciations are net commodity exporters or countries that have embarked on a monetary tightening cycle ahead of advanced economies (Box 2.1), since the increased interest rate differential created carry-trade opportunities.

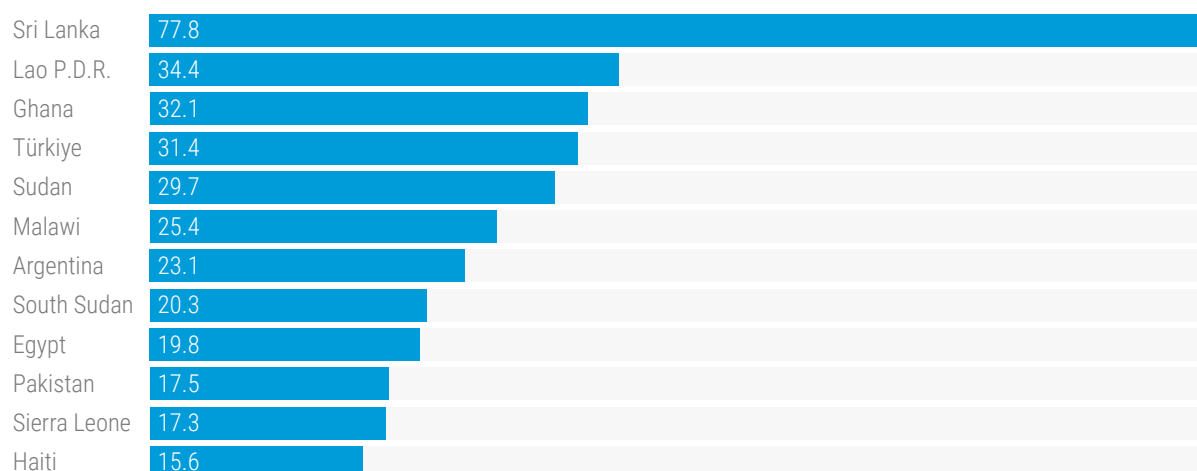
**Table 2.1** Developing countries considered in or close to debt distress, mid-2022

	<b>In default</b> as of 30 June 2022	<b>Undergoing sovereign debt restructuring</b> as of 30 June 2022	<b>Bond yields close to or above 10 percentage points relative to 10-year United States Treasury bills</b> as of 30 June 2022	<b>IMF debt sustainability assessments (in debt distress or at high risk of debt distress) for PRGT-eligible countries</b> as of 31 May 2022
<b>Low-income countries (LICs)</b>	Zambia	Chad, Ethiopia, Mozambique	Uganda, Zambia	Afghanistan, Burundi, Central African Republic, Chad, Republic of Congo, Ethiopia, The Gambia, Guinea-Bissau, Malawi, Mozambique, Sierra Leone, Somalia, South Sudan, Sudan
<b>Lower middle-income countries (LMICs)</b>	Lebanon, Sri Lanka		Egypt, Pakistan	Cameroon, Cabo Verde, Comoros, Djibouti, Ghana, Haiti, Kenya, Kiribati, Lao P.D.R, Mauritania, Micronesia, Papua New Guinea, Samoa, São Tomé and Príncipe, Tajikistan, Zambia, Zimbabwe
<b>Upper middle-income countries (UMICs)</b>	Suriname			Dominica, Grenada, Maldives, Marshall Islands, St. Vincent and the Grenadines, Tonga, Tuvalu
<b>Not classified</b>	Venezuela (Bolivarian Republic of)			

*Source:* UNCTAD secretariat calculations based on IMF Debt Sustainability Framework (as of 31 May 2022), Refinitiv and World Bank income classification 2022–2023.

*Notes:* As of 30 June 2022, Brazilian sovereign bond (10-year maturity to keep comparison with 10-year United States Treasury bills) saw a spread of 9.9 per cent and Colombian bonds of 8.4 per cent (both up from previous year-on-year for date of 30 June).

**Figure 2.3** Nominal exchange rate depreciations against the United States dollar, selected developing countries, January–July 2022 (percentage)



*Source:* UNCTAD secretariat calculations based on Refinitiv.

*Note:* Estimated change in per cent of the nominal exchange rate against the United States dollar between 1 January 2022 and 8 July 2022.

### Box 2.1 Monetary tightening in developing countries

The combination of rising policy rates in advanced economies, higher domestic inflation rates and depreciating currencies is severely limiting the policy space available to monetary authorities in developing countries. This complex background explains the sharp contrast in terms of monetary policy responses in the early stages of the Covid-19 pandemic relative to the situation in 2022. Between June 2019 and May 2020, for a group of 72 developing countries, the median central bank policy rate declined from 5.0 to 4.5 per cent. At least 52 of these countries were able to cut rates during this period to support their response to the pandemic. By contrast, between June 2021 and May 2022, the median policy rate for this group increased from 4.0 to 4.9 per cent. At least 51 countries raised policy rates during this period (figure 2.B1.1A). This widespread tightening of monetary policy in developing countries is acting as a constraint on the efforts of authorities to sustain economic recovery in the aftermath of Covid-19.

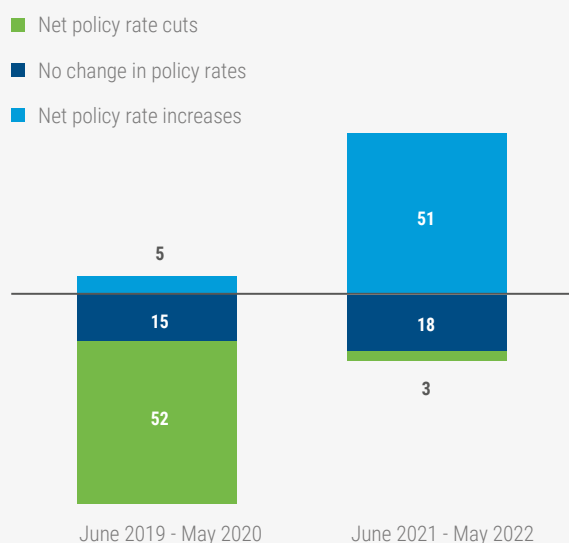
In the current context, one of the most important risks faced by developing country governments is an overshooting of domestic monetary policy tightening. Central banks in these countries have tried to preempt the expected increase of policy rates in the United States by raising their own rates from the second half of 2021 (TDR, 2022). However, with United States monetary tightening transmitting inflationary pressures to developing countries through balance of payment crises and currency depreciations, compounded (until recently) by price hikes in core international commodity markets, monetary authorities in these countries come under pressure to extend the ongoing cycle of tightening, both in terms of rate hikes and duration (World Bank, 2022a). High domestic inflation rates turn policy rates negative in real terms and, therefore, broadly accommodative in many countries. An analysis of the situation for 56 developing countries shows that in at least 35 cases, policy rates have turned negative despite the implementation of nominal rate increases over the last 12 months ending in May 2022 (figure 2.B1.1A). This then calls for further monetary tightening.

This thinking relies heavily on central banks' wariness of the perceived risks of unanchored inflation expectations and wage-price spirals (BIS, 2022). These risk preferences inform their inclination to pursue

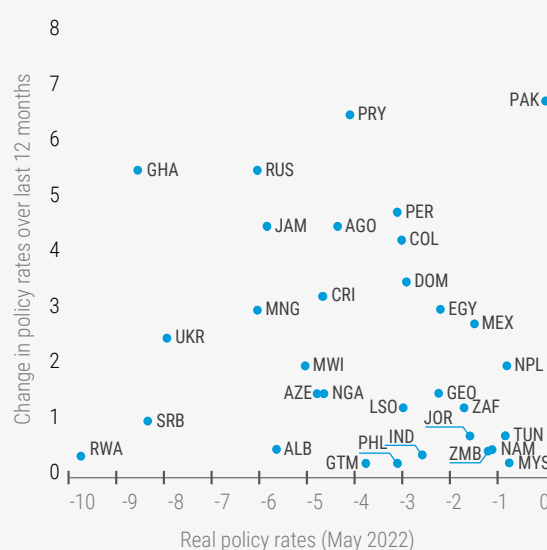
further rate hikes despite both the lack of evidence on systemic build-ups of wage-price spirals and the equally significant danger of triggering sharp domestic economic downturns (Storm, 2022). This dynamic highlights the blunt nature of the use of monetary policy tools to tackle the often divergent causes of domestic inflationary pressures (TDR, 2022).

**Figure 2.B1.1 Monetary policy in developing countries**

**A. Changes in monetary policy, developing countries, 2020-2022 (number of countries)**



**B. Real policy rates and changes in nominal policy rates, developing countries, 2021-2022 (percentage)**



Source: UNCTAD secretariat calculations based on Refinitiv.

Notes: Panel A includes data for 72 countries with available data until May 2022. Panel B includes data for 56 countries with available data until May 2022. The real policy rate is estimated as the difference between the policy rate and national CPI figure for May 2022. Policy rates include reported central bank policy rates, discount rates or repurchase rates.

## 2. External debt sustainability in times of tapering

Clearly, these global financial conditions – and the United States monetary tightening cycle – put already fragile debt sustainability in many, though not all, developing countries in further and acute peril (UNCTAD, 2021). This is evident from the following brief analysis of the evolution of two core indicators of external debt sustainability in developing countries.

The first of these – the ratio of total external debt stocks to exports (of goods and services, including tourism revenues) – provides an indication of countries’ external solvency given the importance of export revenues to service foreign-currency denominated debt obligations. For all income groups (low- and middle- income countries, according to the World Bank income classification and excluding China), this indicator rose from an average of 100 per cent in 2010 to 159 per cent in 2020 (figure 2.4.A). By 2021, this figure had again fallen to 127 per cent, reflecting the much stronger growth in export revenues compared to that of external debt stocks in this year. This is still 18 percentage points above the average value for this indicator at the height of the taper tantrum crisis in 2013 (108 per cent), but below the value for 2016 (142 per cent) when the first cycle of monetary tightening started. A core danger of current tightening financial conditions is precisely that this recent positive development will be reversed.



Disaggregating these data by income groups, low-income countries faced the most severe constraints throughout, with their external debt stocks still exceeding their export revenues by a factor of 2 in 2021. Lower middle-income countries saw their external debt sustainability eroded substantially as their ratio of total external debt-to-exports steeply from a relatively low value in 2013 (compared, for example to upper middle-income countries at this stage) to 118 per cent in 2021 (and a factor of 1.5 in 2020). Unsurprisingly, upper middle-income countries have fared better on average but have also seen their ability to service external foreign-currency denominated debt obligations through export revenues decline over the past decade.

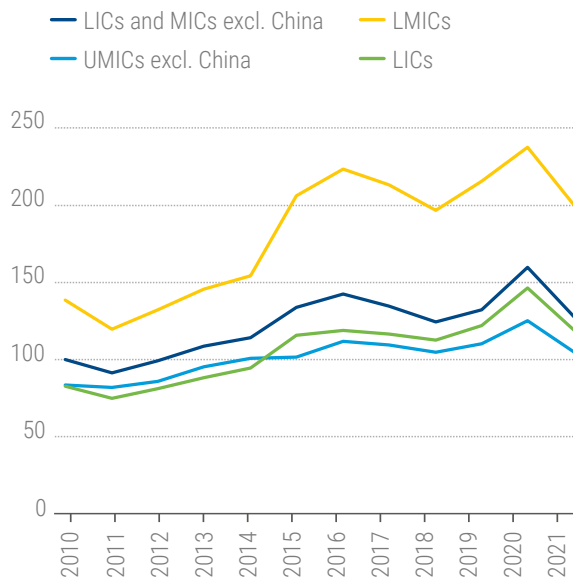
Most importantly, however, such group averages hide the fact that, in each income group, there can be significant “outliers” – that is several often-smaller countries in much more dire straits than the average picture would suggest. This is relevant since assessing the severity of debt distress in the developing world needs to be informed by country experiences. Figure 2.4B-D therefore provides a more detailed picture, at country-level, of changes in their ratio of total external debt stocks to their export revenues between 2016 – when monetary tightening first set in – and 2020, the last available year for country-level data. This shows quite clearly that the number of countries in each income group – with often very different institutional histories, current policy frameworks and operating at different per-capita income levels – whose position deteriorated in regard to this indicator is substantial (i.e. all countries above the 45-degree line in figure 2.4B-D).

The second core indicator is the ratio of debt servicing costs on public and publicly guaranteed debt to government revenues. This approximates the ability of governments to continuously service public (rather than total) external debt obligations, reflecting not only governments’ ability to marshal domestic resources for this purpose but also the changing costs of servicing such debt. As figure 2.5.A shows, a steeply increasing share of government revenues was needed to service external public sector debt obligations in the period 2010 to 2020. This is the case, on average, for all developing countries (low- and middle-income countries according to World Bank income classification), as well as for specific income groups, and is a clear reflection on the cost borne by many developing countries due to their integration into international financial markets. This has proved a double-edged sword for many and, especially, poorer and more vulnerable frontier developing countries: On the one hand, largely private financing provided much-needed immediate relief from external financing constraints, not readily available through multilateral channels. On the other, (re-) financing in international financial markets has arguably worsened external financial constraints in these economies in the longer-term due to their heightened exposure to market risks and associated high and highly volatile debt servicing costs.

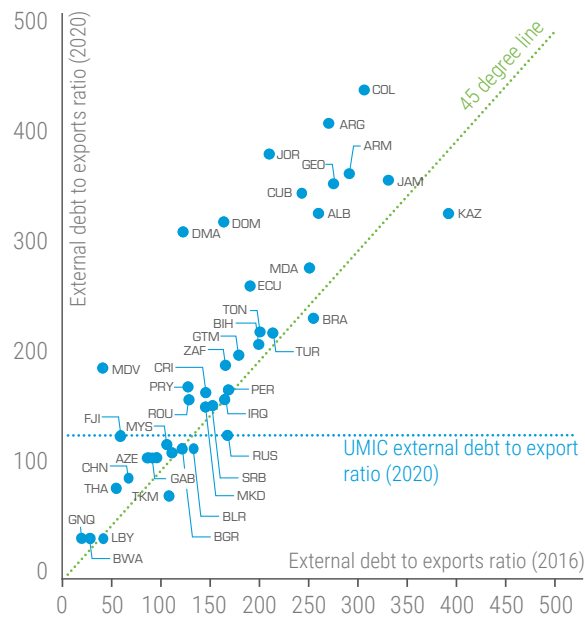
While this situation saw some improvement in upper middle-income countries in 2021 – one that is vulnerable to being reversed soon if adverse global financial conditions persist – there has been little, if any, reprieve in low- and lower-middle income countries. By 2021, these countries’ public sectors remained, on average, under high pressure to dedicate substantive and growing shares of their government revenues to servicing their external debt servicing obligations, compared, for example, to either the 2013 taper tantrum episode or the onset of monetary tightening in 2016. Here again, individual country experiences across income groups are telling and relevant, as depicted in figure 2.5.B for 2020 (the latest data available at country-levels). Clearly, a significant number of both low- and middle-income countries have seen their external public debt servicing costs rise to well above 20 per cent of their government revenue. This is not only not conducive to their own future growth prospects, let alone their ability to respond to higher benchmarks for inclusive and sustainable growth, but it is also destined to negatively rebound on global economic (inclusive and sustainable) growth prospects.

**Figure 2.4** Total external debt stocks to export revenues, developing countries, 2010-2021 (percentage)

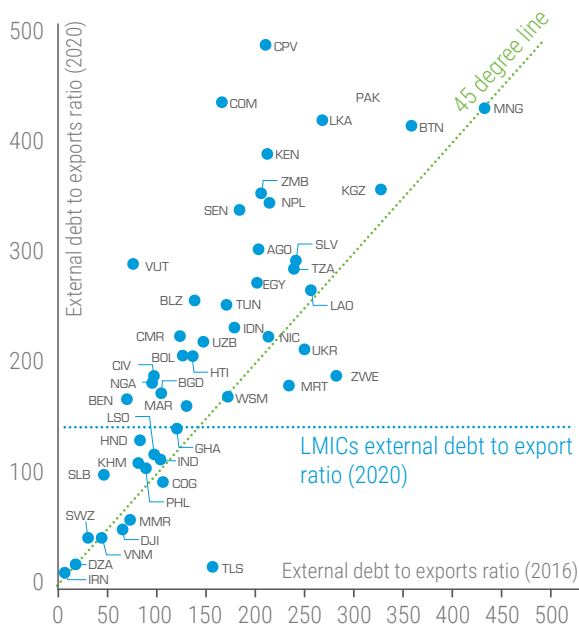
**A. Income group averages**



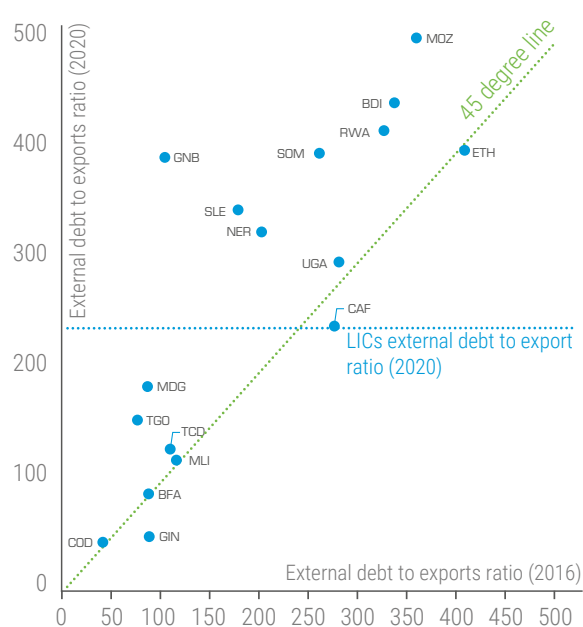
**B. Upper middle-income countries**



**C. Lower middle-income countries**



**D. Low-income countries**



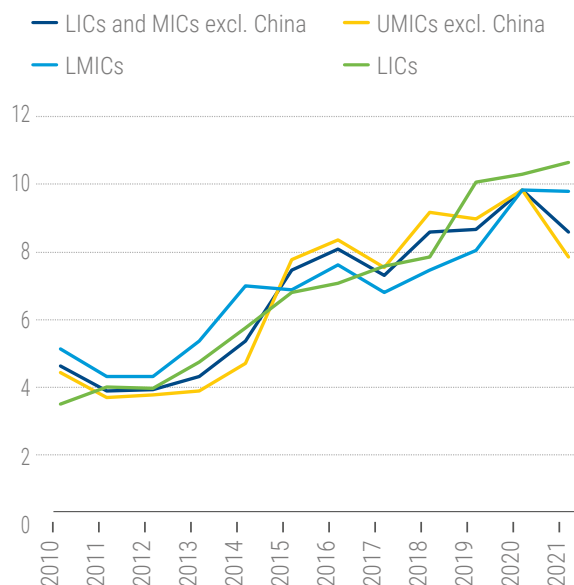
Source: UNCTAD secretariat calculations based on World Bank International Debt Statistics.

Such figures suggest that the deterioration of developing countries' external debt sustainability was more widespread across developing countries than indicated by the IMF LIC Debt Sustainability Framework. However, and as mentioned, the countries with a particularly perilous position in the three country groups are mainly economies which were already facing high pressures on their external debt positions before the Covid-19 pandemic. The pandemic, along with increasing climate-related shocks, the war in Ukraine and the current tightening of global financial conditions, has led them to the brink of debt distress or to default.

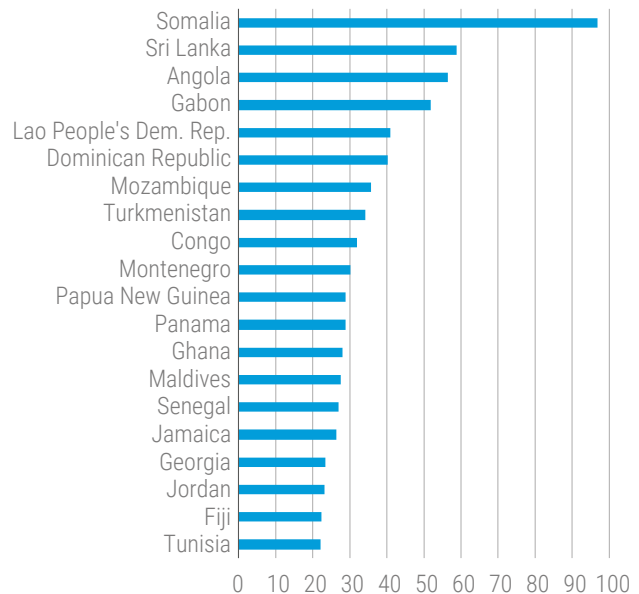
This means that the current situation, although very worrying, is different from the 1980s and 1990s when a few but very large developing countries faced acute financial and debt crises.

**Figure 2.5** Servicing costs on public and publicly guaranteed external debt to government revenues, developing countries and groups, 2010–2021 (percentage)

### A. Income group averages



### B. Top 20 countries in 2020



Source: UNCTAD secretariat calculations based on World Bank data.

## 3. Policy responses by the international community

This analysis reinforces the warnings raised recently by the United Nations Global Crisis Response Group on Food, Energy and Finance. 94 developing economies, home to 1.6 billion people, are severely exposed to at least one of the dimensions of the interlocked crises outline above. The Group has emphasized that there is no way to respond to this challenge, without first addressing the deterioration of financial conditions in developing countries. Unfortunately, policy and financial commitments made by the international community in recent months have fallen short of what is required (United Nations, 2022a).

There are three relevant areas of multilateral action which require the implementation of additional measures based on a renewed sense of urgency. These include the provision of official development assistance (ODA), the allocation and effective deployment of SDRs and policies to effectively address debt distress in developing countries.

First, there is an imperative need for developed countries to meet their ODA commitments while protecting levels of assistance in key areas, including Covid-19 vaccination efforts and climate commitments, and particularly to least developed countries (LDCs). In 2021, ODA reached \$178.9 billion, equivalent to 0.33 per cent of GNI of the members of the Development Assistance Committee (DAC) (OECD, 2022). This figure is problematic for at least two reasons. First, it is less than half of the established commitment of 0.7 per cent of GNI. Over the last 50 years, the systemic failure of DAC members to meet their pledges means that developing countries have lost over \$5.7 trillion in developing financing (OXFAM, 2020). Second, resources allocated to LDCs are under threat because of the declining share of grant financing as well as the expected increase of in-donor country refugee costs (Eurodad, 2022).

Second, developing countries have made active use of their share of resources received through the allocation of \$650 billion in SDRs by the IMF in August 2021. At least 69 developing countries have included SDRs in government budgets or have deployed them for fiscal purposes for a total of \$81 billion since this allocation (CEPR, 2022). Additional resources are required that could be deployed through different mechanisms. These include the operationalization of commitments to reallocate SDRs towards the IMF Poverty Reduction and Growth Trust (PRGT) and the new Resilience and Sustainability Trust (RST), a new emission of SDRs in 2022, and in addition, establishment of an SDR development link in SDR allocations as long advocated by UNCTAD (UNCTAD, 1965).

Third, piecemeal measures to provide short-term debt relief are inconsistent with the magnitude of the challenges faced by debt countries in terms of both existing liabilities and future financing needs. Actions ought to focus on two broad areas. First, establishment a multilateral legal framework for sovereign debt restructuring to facilitate timely and orderly debt crisis resolution with the involvement of all official (bilateral and multilateral) and private creditors (TDR, 2015). The framework would facilitate the provision of debt relief linked to a debt sustainability assessment that incorporates long-term finance needs, including for the achievement of the 2030 Agenda and the Paris Climate Agreement (TDR, 2019). Second, establishing a publicly accessible registry of debt data for developing countries to address debt transparency challenges. Following the UNCTAD Principles for Responsible Sovereign Borrowing and Lending, this registry would allow the integration of debt data by both lenders and borrowers at the level of specific transactions in a way that ensures interoperability of data across direct and indirect sources of reporting (UNCTAD, 2012; Rivetti, 2021; Eurodad, 2019).

### Box 2.2 Developing countries' sovereign defaults and restructurings in 2022

The deterioration in global financial conditions has not triggered a sharp increase in the number of countries that are either in sovereign default or undergoing a debt restructuring during the first half of 2022. In total, there are five countries classified in default – Lebanon, Sri Lanka, Suriname, Bolivarian Republic of Venezuela and Zambia – and a further three undergoing a debt restructuring as of July 2022 – Ethiopia, Chad and Mozambique. Except for Sri Lanka, all the ongoing cases of default and restructuring started in previous years. In the case of defaults, the duration of each open event remains below the average length of a default over the last 50 years, estimated at 58 months (figure 2.B2.1.A). In contrast, in the case of debt restructurings, the duration of each open event is already above the historical average, estimated at 11 months (figure 2.B2.1.B).

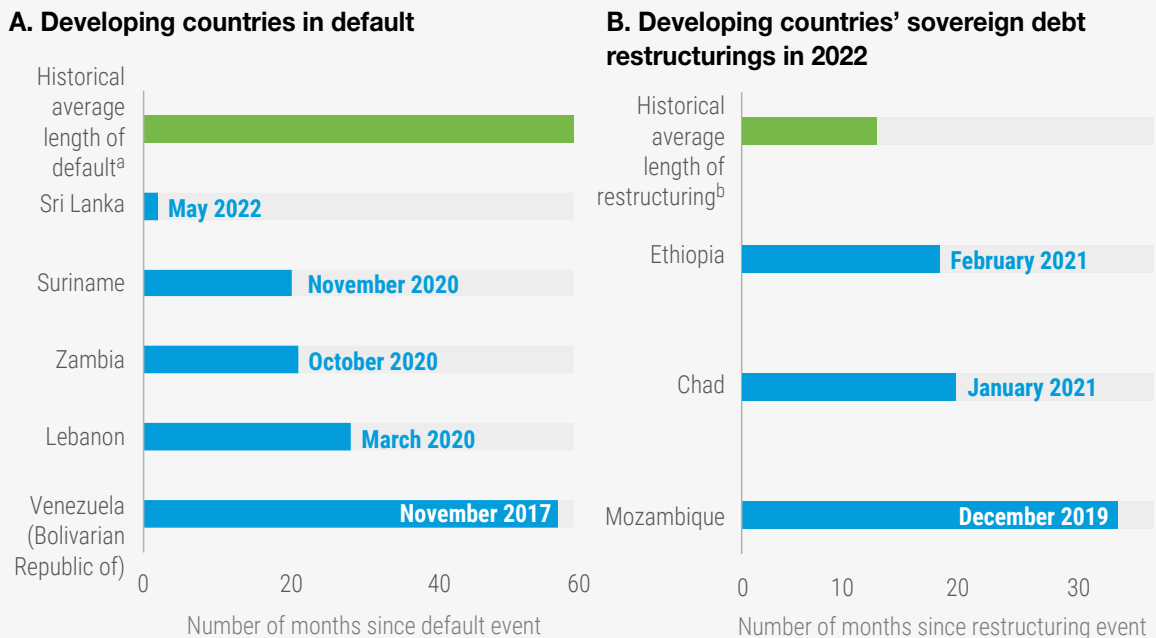
The situation faced by these countries raises three pressing concerns. First, debt distress has already caused a severe degree of economic and social disruption in these countries. Further delays in addressing their debt challenges places them at risk of steeper economic output losses (Asonuma et al., 2019). Second, the combination of elevated debt levels, higher interest rates and the growing likelihood of a global economic slowdown or recession raise the risks of a renewed series of debt crises, as last seen in the 1980s (World Bank, 2022a). As a result, a substantial number of countries might be effectively prevented from mobilizing resources towards achieving the SDGs as they spend most of the rest of the

decade grappling with the consequences of debt distress. Third, the existing “non-system” for sovereign debt resolution is not suited to address these problems (Ocampo, 2017). In the context of an increasingly diverse creditor base, developing countries in debt distress are trapped by strategic creditor choices which are more responsive to repeated inter-creditor disputes across countries than to the economic and developmental considerations of a specific debt restructuring negotiation.

Against this background, efforts to enhance the G20 Common Framework (CF) can be considered a step towards, but not a substitute, for a permanent and comprehensive debt restructuring mechanism (United Nations, 2022a). Of the eight countries that are either in default or undertaking a restructuring in 2022, four are eligible to join the Common Framework. This includes Chad, Ethiopia, Zambia and Mozambique. The first three have opted to participate in the initiative since early 2021. With the exception of Zambia, for which an Official Creditor Committee, including China, was eventually set up under the CF on 16 June 2022 and subsequently moved quickly to help unlock a \$1.3 billion IMF loan to the country (Cotterill and Wheatly, 2022), the CF has achieved little progress so far to accelerate the process of debt crisis resolution for participating countries.

Previous TDR reports have raised concerns over an approach to sovereign debt restructuring that focuses on official bilateral creditor preferences as an effective way to address the manifold external debt challenges faced by developing countries (TDR, 2015). Thus, for example, Zambia still will have to negotiate the exact terms of debt relief under the CF as well as find a way to bring on board private creditors on comparable terms.

**Figure 2.B2.1** Developing countries’ ongoing sovereign defaults and restructurings in 2022



*Source:* S&P Global Ratings (2022); Asonuma and Trebesch (2016).

*Note:* Panel A includes countries classified in default by S&P Global Ratings as of July 2022. Default date as reported by S&P.

<sup>a</sup> Average length of post-default restructurings from default to debt exchange between 1978 and 2020, as defined by Asonuma and Trebesch (2016). Panel B includes countries undergoing a debt restructuring, including participation in the G20 Common Framework (Chad and Ethiopia) or facing ongoing litigation (Mozambique), but which are not classified in default by a rating agency. Restructuring date refers to application to the G20 Common Framework and start of litigation.

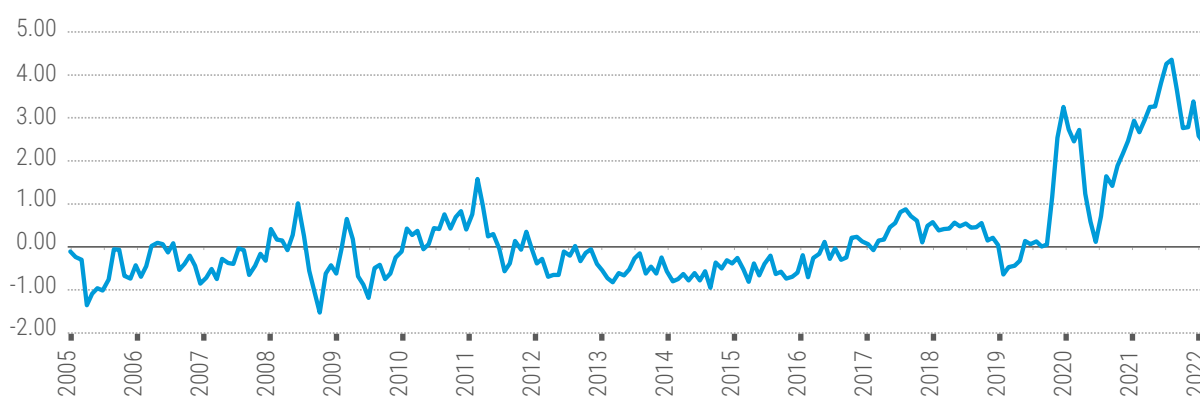
<sup>b</sup> Average length of strictly and weakly preemptive debt restructurings between 1978 and 2020 as defined by Asonuma and Trebesch (2016).

## C. TRENDS IN INTERNATIONAL TRADE

Despite the outbreak of war in Ukraine and subsequent sanctions imposed against the Russian Federation, as well as continued lockdowns in China, affecting particularly Shanghai, world trade has shown resilience in the first half of 2022.

Before the emergence of these new headwinds, there was a sense that other difficulties that had hampered the movement of goods around the world since 2020 would gradually ease. Freight rates started to decline after the third quarter of 2021 while the disruptions in international supply chains and other logistical eased after it peaked in late 2021 (figure 2.6).

**Figure 2.6** Global supply chain pressure index (GSCPI), January 2005–June 2022  
(standard deviations from average value)



Source: Benigno et al. (2022).

Note: The index is normalized such that a zero indicates the index is at its average value, with positive values representing how many standard deviations the index is above this average value (and negative values representing the opposite).

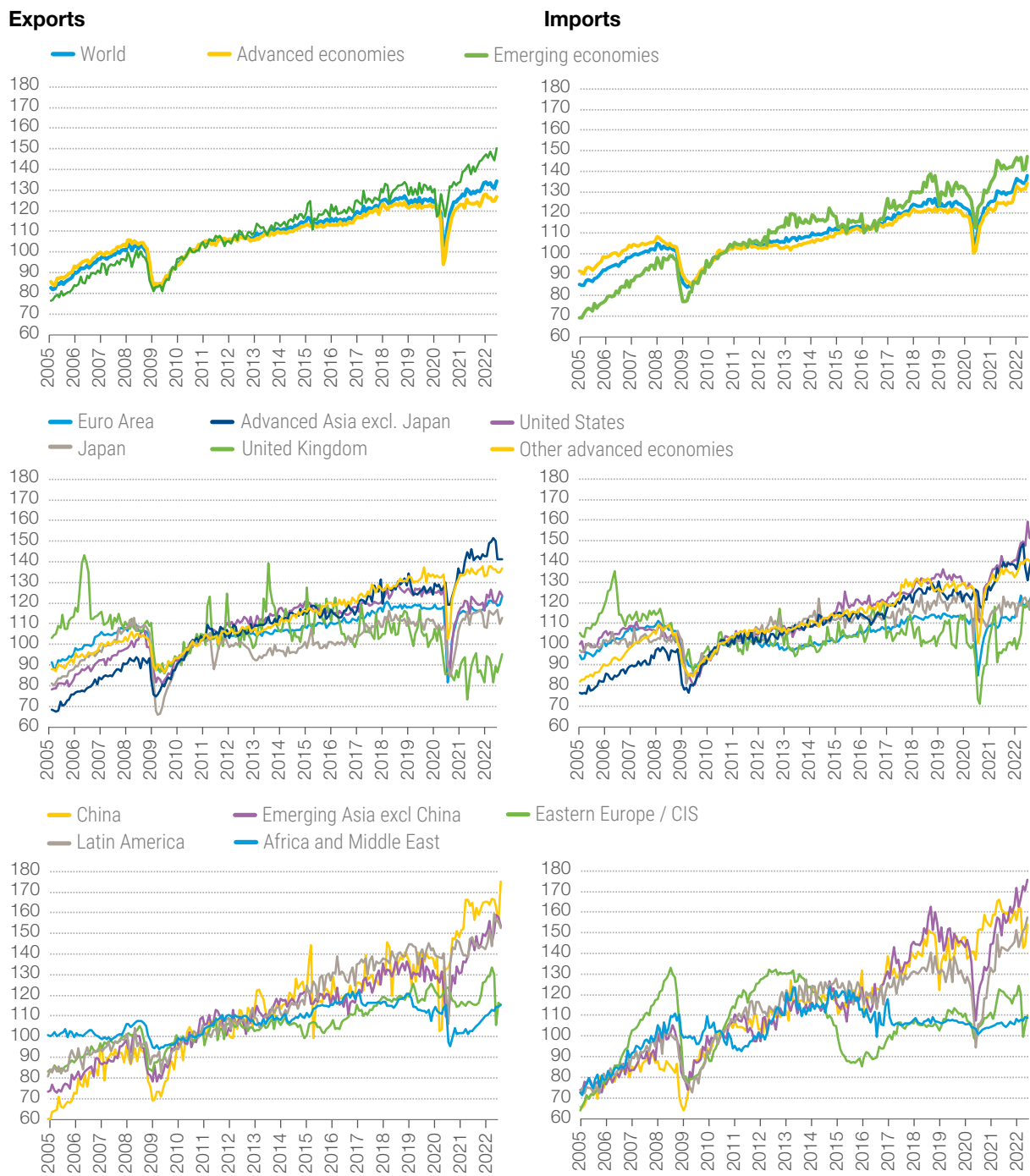
Robust merchandise imports – emanating primarily from Europe, the United States and parts of the developing world, like “Emerging Asia excl. China” and “Latin America” – supported the growth of merchandise trade in the first half of 2022 (figure 2.7). This partially reflected pent-up demand relating to the legacy of the pandemic-driven spending shift from services towards goods that could not be satisfied earlier because of the supply bottlenecks. It also resulted from other positive factors such as the appreciation of the dollar in the case of the United States, the relative dynamism of intra-regional trade in Europe, and favourable terms-of-trade effects in some large emerging economies due to elevated energy prices.

Elsewhere, demand for foreign goods has been more muted. One notable case is China, where monthly data show merchandise imports between January to May 2022 5.6 per cent below their average during the same period last year. Meanwhile, CPB estimates also pointed to a significant contraction in the imports of the “Eastern Europe / CIS” group, following the outbreak of the war in Ukraine.

In terms of exports, patterns since the Covid-19 outbreak have varied. Within advanced economies, by mid-2022, Asian exports stood way above their pre-Covid-19 levels. This contrasts with the United States and especially the United Kingdom, where exports remain significantly below their historical peaks. In between these two extremes stand Europe and the “other advanced economies”, laying slightly above their pre-Covid-19 heights. Within the emerging economies, the picture is also mixed. In China, “other developing Asian economies” and Latin America, the V-shaped recovery was extremely

rapid, while exports continued to grow afterwards. This led to average levels for the first five months of 2022 that were between 6 and 14 per cent above their pre-Covid-19 maxima. Meanwhile, in “Africa and Middle East” and in “Eastern Europe / CIS”, similar figures remained about 5 per cent lower than their pre-Covid-19 peaks.

**Figure 2.7** World merchandise trade, January 2005–May 2022 (index numbers, average 2010=100)



*Source:* CPB Netherlands Bureau for Economic Policy Analysis, World Trade Monitor database.

*Note:* Country group classification relies on Ebregt (2020).



Altogether, these developments contributed to an averaged year-on-year growth of 4.3 per cent in real terms for world trade during the first five months of 2022, if one takes the simple average between the growth of exports (3.0 per cent) and imports (5.5 per cent).

Turning to the components of exports allows a better grasp of the underlying patterns behind these aggregates. For goods, estimates of world seaborne exports from Cerdeiro et al. (2020), which track maritime merchandise trade by their respective vessels in real time, show the following. For the three main types of vessels, containers, bulk and oil/chemicals,<sup>11</sup> data show a significant synchronized rebound taking place in the second quarter of 2022 (figure 2.8.A). Besides these three main vessel types, gas shipments and vehicles also registered an upturn during the first half of the year. This contrasts with foodstuff, the only vessel type that did not perform well during this period (figure 2.8.B). This results mostly from the blockaded grain exports in the Black Sea, which affected net food-importing countries in Africa and parts of Asia, since some of them are highly dependent on cereals coming from the two countries currently at war (United Nations, 2022a). In late July, however, grain shipments from Ukraine started again after an agreement with the Russian Federation was signed. At present, it is still unclear how long it will take for exports to normalize but prices of key grains, including wheat and corn, saw immediate falls and have already returned to pre-war levels.

Turning to trade in services, recent patterns from the subcomponents of this catch-all aggregate depict a rather favourable picture after many of these sectors were hard hit by the pandemic. Starting with tourism, the sector continues to recover at a strong pace. This is a boon for the largest component of trade in services, which accounted for one fourth of this aggregate in 2019 before dropping to one tenth in 2020 and 2021 during Covid-19. More precisely, international tourism saw a strong rebound in the first five months of 2022, with arrivals reaching almost half the levels of the same period of 2019. By regions, Europe and the Americas continued to lead the recovery. Europe welcomed more than four times as many international arrivals as in the first five months of 2021. In the Americas, arrivals more than doubled over the same period. Despite the strong rebound, arrivals remained 36 per cent and 40 per cent below 2019 levels in Europe and the Americas, respectively. The Middle East and Africa also saw strong growth of about 150 per cent in January-May 2022 over 2021 but remained about 50 per cent below 2019 levels. Asia and the Pacific saw arrivals almost double, though numbers were still 90 per cent below 2019, as some borders remained closed to non-essential travel (UNWTO, 2022a). In this context UNWTO has revised upwards its forecast for 2022 due to stronger-than-expected results in the first quarter of 2022. It expects international tourist arrivals to reach 55–70 per cent of 2019 levels in 2022 depending on the scenarios it considers for the rest of the year. In parallel, the percentage of experts seeing a potential return of international arrivals to 2019 levels in 2023 has increased from 32 per cent in January 2022 to 48 per cent in May, reflecting rising optimism among tourism experts worldwide, building on strong pent-up demand, in particular intra-European travel and travel from the United States to Europe (UNWTO, 2022b).

Turning to transport, which accounts for about one sixth of the total trade in services, the recovery has continued over the course of 2021 and in early 2022. For air passenger transport services, IATA data show that the seasonally-adjusted international revenue passenger kilometres (RPK) – an airline industry metric reflecting the number of kilometres travelled by paying passengers – had exceeded the 2019 levels for almost all main routes by the end of second quarter of 2022, after growing steadily since the beginning of 2022. Two key segments differ strongly from this encouraging development: “Asia-Europe” and “Asia-North America”. For these two routes, international RPKs were still severely depressed (May 2022) at about 65 per cent below the 2019 level, despite progressing since January 2022 when this figure stood at 80 per cent.<sup>12</sup> Meanwhile, trends in air cargo has shown an almost opposite evolution. This specific service declined almost 10 per cent year on year in late 2021, early

<sup>11</sup> Containers represent roughly half of the world maritime transport in terms of metric tons of cargo, while bulk and oil/chemicals account for slightly less than one fifth of the total each.

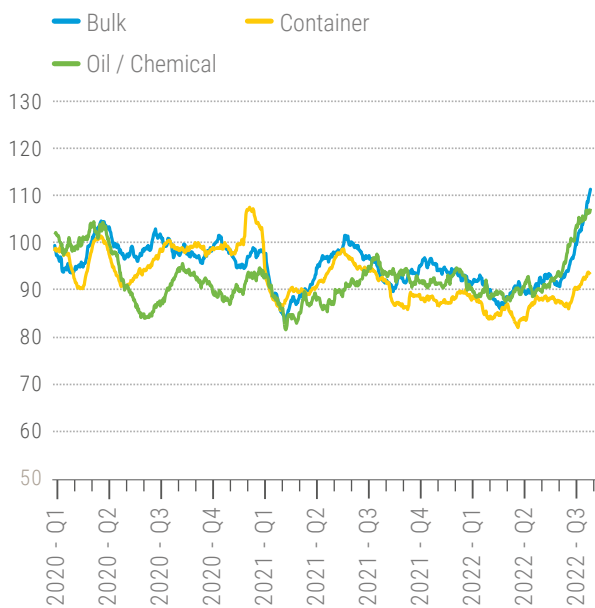
<sup>12</sup> IATA (2022). Air Passenger Market Analysis - May. 7 July. Available at <https://www.iata.org/en/iata-repository/publications/economic-reports/air-passenger-monthly-analysis--may-2022/>



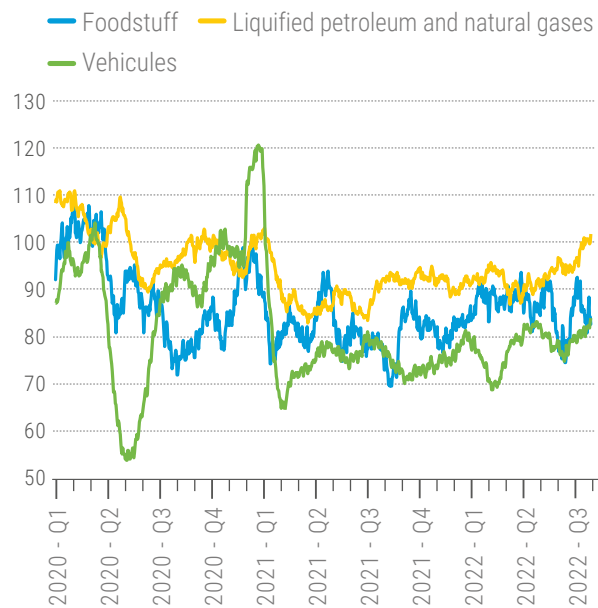
2022, after an intense activity during the first three quarters of 2021, which lay way above pre-pandemic trends. Overall, under the current conditions, the revenues of the commercial airlines for passengers are expected to reach \$498 billion in 2022, compared to \$607 billion in 2019, while for cargo, revenues are forecast to \$191 billion in 2022 from \$100 billion in 2019.<sup>13</sup>

**Figure 2.8** Metric tons of world exports by vessel type, 1 January 2020–7 June 2022  
(index numbers, average 2019 = 100; 31-day centred moving averages)

### A. Three main types of vessels



### B. Other selected types of vessels



*Source:* UNCTAD secretariat calculations based on Cerdeiro et al. (2020) and AIS data collected by MarineTraffic (available at UN COMTRADE Monitor).

*Note:* Underlying data behind the 31-day centred moving average go until 22 June 2022.

In the other broad categories of trade in services, the recovery has continued across the board, with export revenues in 2021 exceeding the 2019 figures, except for construction which remained 8 per cent below its pre-pandemic level. Trade in “ICT” and “insurance and pensions services” registered the largest growth over these two years, about 30 per cent. During the same period, “financial services”, “personal, cultural, and recreational services” and “other business services” grew between 12 and 18 per cent.

Despite such positive development in the first half of 2022, the outlook for international trade is rather grim as the global economy reached an important crossroad around midyear. In the second half of 2022, risks remain mostly tilted to the downside and trade growth is expected to weaken. This results from a combination of different factors including, inter alia, continued supply chain disruptions, weakened demand tapering demand for consumer durables, unduly aggressive monetary policy, and elevated freight charges. Such worries seem already visible in inventories and new export orders, both leading indicators for trade, which were subdued in July 2022. Except for China’s new order figure, which has rebounded in the aftermath of the recent lockdown, those of other major economies have declined or stabilized below the 50-threshold, marking the difference between improvement and deterioration. As a result, and despite the broad uncertainties that lie ahead, it is expected that global

<sup>13</sup> IATA (2022). Industry Statistics Fact Sheet June 2022. 20 June. Available at <https://www.iata.org/en/iata-repository/publications/economic-reports/airline-industry-economic-performance---june-2022---data-tables/>

trade will grow almost at par with the global economy in 2022, namely in the range of 2 to 4 per cent. This would represent a sharp deceleration from the 2021 figure, whose current estimates point to a range of 7 to 10 per cent in constant prices, depending on whether one considers world exports or imports, given the challenges that trade statisticians are facing to get reliable price indices for these variables since many countries still have to provide their final numbers for 2021.

Beyond 2022, the prospects for trade remain relatively weak, mirroring the expected deceleration of economic growth discussed in the previous chapter and suggesting a return to the subdued long-term trend prior to Covid-19.

Certainly, the Declaration at the conclusion of the 12th Ministerial Conference (MC12) of World Trade Organization provided some positive elements and the reaching of an agreement suggested the multilateral trading system remains relevant in difficult, as well as in good, times. However, many of the elements were indecisive with the details still pending and it remains to be seen to what extent they can boost international trade in the near future. The outcomes of value to developing countries are mainly concerned with the emergency responses to food insecurity and the Covid-19 pandemic, notwithstanding the resistance of some advanced economies to agree to waiving the TRIPS legislation that could help developing countries combat the pandemic. Moreover, not being able to resolve the issues around fully and well-functioning dispute settlement system poses an ongoing challenge to multilateralism.

In this context, there is still a long way to achieve an inclusive, transparent, and development-friendly multilateral trading system that serves the three pillars of sustainable development and allows developing countries to have sufficient policy space to pursue pragmatic development policies adapted to local conditions. In the pursuit of this objective, chapter IV of this Report argues that, while a constructive and cooperative approach to multilateralism must remain paramount, open developmental regionalism could support this transition.

## D. COMMODITY MARKETS

While the market for commodities has been historically characterized by sharp movements in international prices, the fluctuations observed since the onset of the pandemic in early 2020 have been startling not only in terms of their magnitude but also in the sudden reversals in trajectories. It is important to bear in mind that the effects of these abrupt price movements are not limited to the returns to international investors, for whom commodities are just another form of financial asset. Rather these swings in international prices are having a heavy and real impact on economies and individuals, particularly in the developing world.

Not only are developing countries seeing an outsized impact of these price movements on their current account balances – complicated further by the fact that any deterioration in these balances necessitates financing precisely at a time of increasingly scarce and costly international financing conditions – they are also experiencing a disproportionately large knock-on effect on domestic inflationary pressures as these raw materials account for a far larger share of their consumer baskets than those of developed countries. Ultimately, these sudden price swings are having a direct impact on the welfare and livelihoods of some of the most vulnerable populations across the globe, both as small-scale producers and as consumers of these basic goods.

Even before the outbreak of Covid-19, the last decade had seen a period of elevated volatility in commodity markets, with multiple shocks causing both steep declines and rises in international prices. This is in stark contrast to the first decade of the twenty-first century, during which a turbocharged demand for commodities from a rapidly growing and industrializing Chinese economy produced a

considerable and sustained increase in commodity prices across the board. The heightened volatility in commodity markets since the global financial crisis in 2008 has only been exacerbated in the last two years by severe and largely unprecedented shocks on both the demand and supply side.

The outbreak of the Covid-19 pandemic in early 2020 precipitated an abrupt drop in commodity prices as lockdowns were imposed and economic activity slowed to a crawl across the globe. The aggregate commodity price index fell by 25 per cent from January to April (figure 2.9). While the fall in prices was broad-based, energy commodities registered the largest drop (54 per cent), followed by metals (16 per cent) and food (9 per cent). Thereafter, a rapid bounce-back in activity, particularly in China, coupled with severe disruptions to supply, transport and logistics produced a sharp recovery in commodity prices. The aggregate index rose by just over 50 per cent between April and December 2020, finishing the year over 10 per cent above the level observed at the end of 2019.

The same factors driving the upward movement in prices in the latter half of 2020 continued into 2021. The aggregate index posted an annual increase of 54.7 per cent over the course of 2021 (table 2.2), with energy commodities again registering the largest change (85.8 per cent), followed by food (29.9 per cent) and metals (20.7 per cent). These upward price pressures remained through the first two months of 2022, as all commodity groups registered further increases.

**Table 2.2** World primary commodity prices, 2008–2022 (percentage change over previous year)

Commodity groups	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022 <sup>a</sup>
All commodities <sup>b</sup>	33.4	-31.6	24.3	28.6	-3.0	-3.7	-7.9	-36.2	-9.4	17.4	16.0	-7.4	-15.8	54.7	55.7
Non fuel commodities <sup>c</sup>	22.2	-17.8	26.1	18.9	-12.7	-6.5	-8.0	-18.9	2.3	9.1	-2.2	0.1	4.2	33.9	14.3
Non fuel commodities (in SDRs) <sup>c</sup>	18.3	-15.6	26.9	15.1	-9.8	-5.9	-8.0	-11.9	3.0	9.1	-4.2	3.0	3.5	31.1	19.2
All food	32.6	-10.4	12.0	24.0	-6.5	-9.6	-0.8	-15.6	3.6	-1.3	-6.5	-2.0	6.6	29.9	23.9
Food and tropical beverages	31.1	-2.2	11.6	23.6	-9.9	-9.1	3.8	-14.2	2.2	-1.6	-6.7	0.3	3.6	21.0	22.3
Tropical beverages	19.2	1.1	19.8	31.2	-22.4	-19.8	24.1	-10.3	-3.3	-3.1	-8.5	-5.1	4.8	28.3	49.8
Food	34.9	-3.2	9.1	21.1	-5.6	-6.0	-1.2	-15.4	4.0	-1.2	-6.1	1.9	3.3	19.0	15.1
Vegetable oilseeds and oils	35.2	-24.1	13.0	24.8	0.7	-10.5	-9.6	-18.8	7.0	-0.5	-6.2	-6.9	13.7	49.0	26.5
Agricultural raw materials	8.4	-16.4	37.0	24.5	-19.2	-8.8	-11.8	-13.3	-0.4	5.3	-1.8	-3.9	-2.1	13.5	5.5
Minerals, ores and metals	19.7	-12.9	33.6	20.5	-6.9	-9.5	-12.8	-17.2	4.6	11.3	1.3	6.2	15.5	20.7	5.3
Minerals, ores and non-precious metals	17.5	-25.4	39.0	12.2	-16.8	-2.0	-14.6	-24.8	1.4	25.7	2.6	3.4	3.7	43.6	7.9
Precious metals	23.4	7.5	27.5	30.8	3.4	-15.8	-11.0	-9.9	7.1	0.4	0.0	8.9	26.3	3.6	2.5
Fuel commodities	37.9	-38.6	23.1	32.0	-0.5	-1.2	-7.5	-44.4	-17.5	25.9	27.5	-12.6	-32.0	85.8	91.2
<b>Memo item:</b>															
Unit value of exports <sup>d</sup>	10.9	-9.4	4.4	11.9	-2.3	0.8	-1.2	-11.9	-4.0	5.1	6.7	-2.6	-0.5	15.0	n.a

*Source:* UNCTAD secretariat calculations, based on UNCTAD, Commodity Price Statistics Online; and UNCTADstat

*Note:* In current dollars unless otherwise specified.

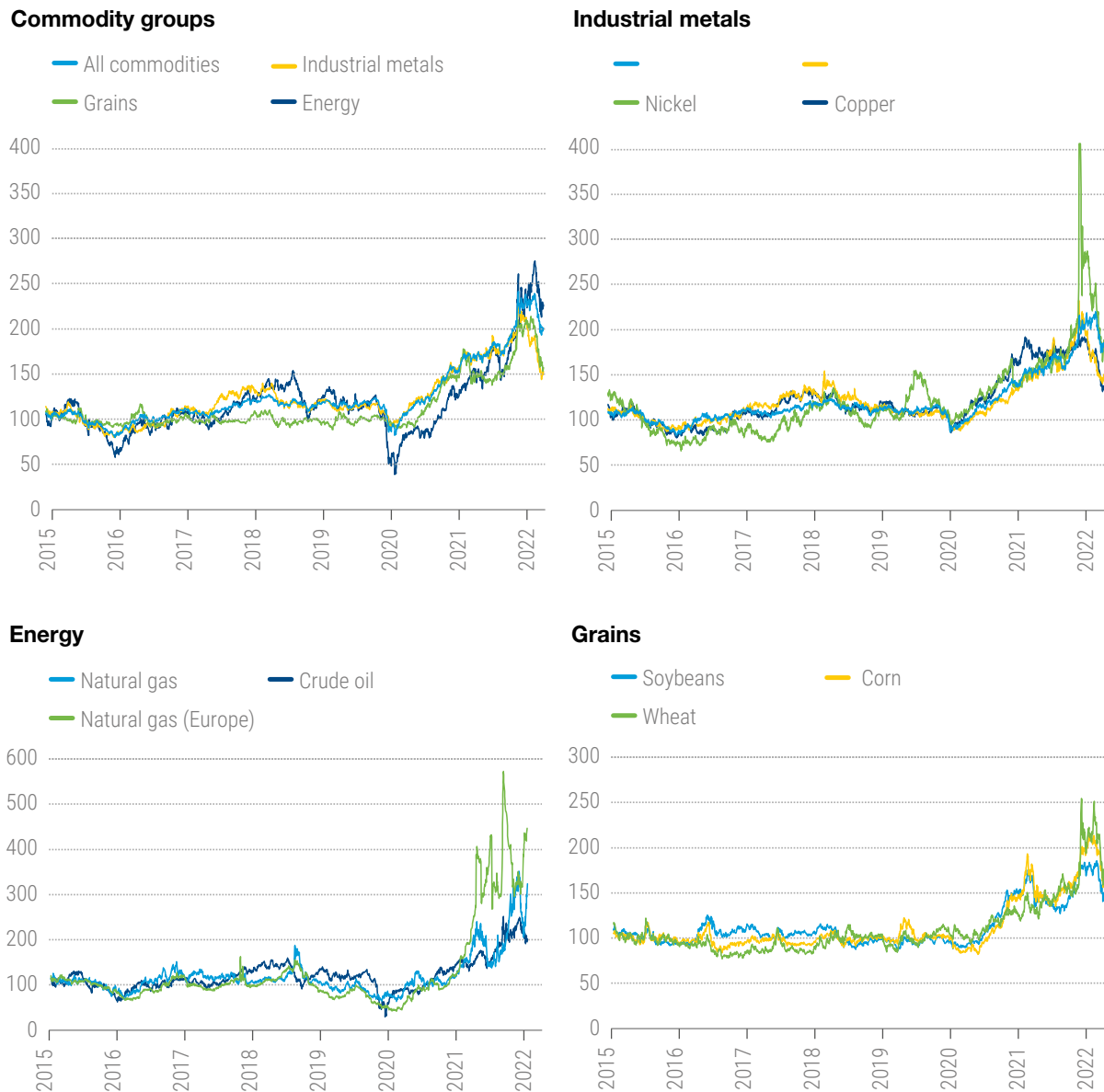
<sup>a</sup> Percentage change between the average for the period January to May 2022 and January to May 2021.

<sup>b</sup> Including fuel commodities and precious metals. Average 2014–2016 weights are used for aggregation.

<sup>c</sup> Excluding fuel commodities and precious metals. SDRs = special drawing rights.

<sup>d</sup> Unit value of merchandise exports of developed countries (M49).

**Figure 2.9** Daily commodity price indices by commodity group and product, Jan. 2015–July 2022  
(index numbers, 2015=100)



Source: UNCTAD secretariat calculations based on Refinitiv data.

Note: Price indices correspond to Dow Jones Commodity Index, except “Natural Gas (Europe)” which corresponds to Hamburg Institute of International Economics (HWWI) Natural Gas Europe price index and “Iron Ore” which corresponds to Credit Suisse Commodity Benchmark (CSCB) iron ore TR index.

The outbreak of war in Ukraine therefore came at a time of already historically high prices across the various commodity categories, and it only exacerbated these upward price pressures. Moreover, the war has had a truly global impact on commodity markets due to the key role played by the Russian Federation and Ukraine in international food, mineral and energy supplies. The Russian Federation is not only the world’s largest natural gas exporter, but also the second largest oil exporter, as well as a leading supplier of aluminum and nickel. Likewise, both the Russian Federation and Ukraine are key

global suppliers of various grains. Between them, the two countries provide approximately 30 per cent of world exports of wheat, as well as 20 per cent of maize and over 50 per cent of sunflower oil (United Nations, 2022b). Perhaps even more crucially, the Russian Federation and neighboring Belarus account for approximately 20 per cent of global fertilizer exports. A combination of factors generated by the war, including production disruptions, interruptions to transportation links – particularly the shutting down of Ukraine’s ports on the Black Sea – and the imposition of sanctions on Belarus (before the war) and on the Russian Federation, have put a severe constraint on the supply of these materials from these countries to the world. Though sanctions to the Russian Federation explicitly excluded food and fertilizers, exports of these suffered declines due to a ‘chilling effect’ in the private sector (foreign insurers, lenders, traders, and shippers) which, afraid of reputational risks, further retaliatory action, often over-complied and ‘self-sanctioned’; a clear result of this was a noted increase in trade transaction costs, in the form of higher interest rates, insurance premiums, and shipping rates for goods coming from the Russian Federation, including grains and fertilizers. Speculation and financialization of the markets have also played an important role as explained before (see Box 1.3). The result of which has been international supply shortages and acute spikes in prices, reflected in an increase of 15 per cent in the aggregate commodity price index in the 2 months following the outbreak of the war (figure 2.9).

While the increase in prices has been broad-based, certain commodities have been more affected than others. As is customary, and consistent with the Russian Federation’s key role in global energy supply, the most drastic spike in prices was observed in energy commodities, which rose by 25 per cent in the two months following the war in Ukraine. Initial sanctions against the country did not target the Russian Federation’s oil and gas exports, precisely for fear of unsettling global energy markets. However, the potential for disruptions to Russian supply as well as avoidance of Russian crude by oil traders owing to concerns of possibly violating financial sanctions imposed on the Russian Federation economy alarmed oil markets, particularly as tight global oil supply – largely due to the very gradual relaxing of output restrictions introduced by OPEC+ members as per the agreement reached in April 2020 despite a faster than anticipated surge in global oil demand since then – was already applying significant upward pressure on prices. As a result, the price of the Brent crude oil benchmark rose rapidly from just under 100 dollars on the eve of the war to over 120 dollars only two weeks later.

Subsequent announcements by the United States banning oil imports from the Russian Federation, by the United Kingdom to phase out Russian oil imports by the end of the year, and by the European Union to ban seaborne oil imports from the Russian Federation by the end of 2022, as well as prohibiting shipping insurance for oil exports from the country, exerted further pressure on oil markets. However, the release of 180 million barrels from the United States’ strategic petroleum reserves as well as the readiness of both China and India to receive Russian oil exports – and thus take advantage of the significant discount at which the country’s Urals brand of crude oil trades compared to other benchmark prices – proved sufficient to ensure that global oil supplies did not tighten further.

For its part, the natural gas market has been particularly sensitive to the war given the dependence of numerous European countries on natural gas supplies from the Russian Federation. Given the fixed distribution systems (i.e. pipelines) required to deliver gas, ready substitutes for these energy products are not easy to come by. There still exist different types of gas pricing: fixed, regulated or cost-related mechanisms; prices linked to crude oil or oil products; market, spot or hub-based prices. In the United States and the United Kingdom, privatization and market-based pricing was already well underway by the end of the 1980s. In the European Union, the process started later: in 2005, nearly 80 per cent of its gas was sold on an oil-linked basis, by 2018 that figure had fallen to around 25 per cent with 75 per cent of gas sold at spot or hub prices (and regulated prices had virtually disappeared) (Stern and Imrisovic, 2020). Basically, even long-term contracts price the entire purchase based on the price of the last barrel exchanged on the spot market. On the contrary, Asian markets, which used to import 70–75 per cent of LNG before the war in Ukraine, remain largely dominated by oil-linked or fixed pricing (Stern and Imrisovic, 2020). Globally, spot prices dropped in 2019 due to large LNG supply. In the

European Union, that affected pricing of pipeline gas from Gazprom to the considerable advantage of member states. Then, ahead of winter 2021/22, Asian economies rushed for new long-term contracts securing greater volumes ahead of time and rely less on spot cargoes. So, what determined a good deal for Europe in 2019 turned bad in 2021/22, well before the war in Ukraine and despite gas supply based on long term contracts being fully guaranteed (Stern and Imsirovic, 2020; Sharples, 2021).

Hence, the liberalization of the gas market and the choice of market-based pricing rather than based on cost-based agreements with producers has proved problematic for Europe, a move which Asian countries have not yet made. As gas spot prices in Europe skyrocket, with the main beneficiaries the Russian Federation and the United States, the region just became the first world importer of United States LNG but still cannot avoid dependence on Gazprom supply (Celi et al., 2022). On the contrary, countries which have been able to establish fairer long-term relationship with producers are now enjoying lower energy prices and reliable delivery. Those who have maintained control of domestic energy companies and/or their retail price formation have also been able to keep the distributive implications of domestic inflation in check (Storm, 2022) as shown by the difference between the GDP and the private final consumption expenditure deflator in Indonesia and China. The decision by Germany to halt the Nord Stream-2 Baltic Sea gas pipeline project, as well as the European Union's pledge to reduce Russian gas imports by two-thirds by the end of the year and the intermittent shutting off of gas flows to the continent by the Authorities of the Russian Federation has provoked a surge in European natural gas prices, increasing by more than four-fold in April compared to levels a year earlier (figure 2.9). Moreover, since the European Union's commitment to reduce its reliance on Russian natural gas supplies depends on the bloc increasing its imports of Liquefied Natural Gas (LNG) from other countries, LNG prices have also registered increasing upward pressures since the outbreak of the war. LNG prices stood almost 30 per cent higher in June compared to January, and over double the level registered a year earlier in June of 2021 (UNCTAD secretariat calculations based on data from Japan Import Price Index for LNG). These price movements are further increasing the import bills of LNG-importing developing countries, and could even potentially price out some developing countries from the LNG supplies on which they depend to meet their energy needs.

Perhaps the area in which the impact of the war has been most damaging to developing nations has been in the precipitous rise in food prices. Even before the war broke out, however, food prices were already approaching historic highs, with the subsequent adverse consequences for the most vulnerable populations across the globe. Before the war, it was estimated that food insecurity touched the lives of an estimated 800 million people around the world (FAO, 2022).

Since the Russian Federation and Ukraine are, respectively, ranked the third and seventh largest producers of agricultural goods, the repercussions of the conflict on global food supplies and prices have been widespread and considerable. While some countries, particularly in the case of the European Union, have been able to make up for the shortfall on certain agricultural imports by tapping regional producers or alternative sources, this has not been the case for most developing nations who lack the regional partners and global presence to ensure the provision of additional agricultural stocks in times of global supply squeezes.

The outsized impact of the war in international food markets is reflected in the sharp jump in the aggregate price index of grains between February and April, at just over 16 per cent (figure 2.9). The two countries' key role in global wheat supplies translated into a surge of over 30 per cent in international wheat prices during this period. Moreover, the shortfall in wheat supplies coming from the Russian Federation and Ukraine has hit Africa and the Middle East particularly hard as these regions rely on these two countries for an outsized share of their wheat imports. For its part, maize prices also saw precipitous increases in the aftermath of the war, rising by more than 20 per cent in the following two months. Largely unrelated to the war, soybean prices have also remained at elevated levels since the beginning of the year due to adverse weather conditions in producing countries, namely Argentina, Brazil and the United States.



In reaction to growing domestic price pressures on staple food items, a number of countries instituted food export restrictions in an effort to bring down prices. While such measures may have provided some relief in the short-term domestically, they have exacerbated upward price pressures internationally.

An important additional factor weighing on current and future food prices has been the disruption to worldwide fertilizer supply from the war. As mentioned earlier, together the Russian Federation and neighbouring Belarus account for a substantial chunk of worldwide fertilizer exports. The 2021 sanctions on Belarus international sales of potash – a key ingredient in fertilizers – have intensified the already sharp upward trend in prices observed since mid-2020. According to data from the World Bank, while the aggregated price of food rose by almost 80 per cent from May 2020 to June 2022, that of fertilizers increased by just shy of 230 per cent over this same period (World Bank, 2022b).

Moreover, the introduction of a fertilizer export ban by China in an attempt to alleviate domestic price pressures has only added to the tight supply conditions internationally. The scarcity and steep price increases of fertilizers has important implications for food markets, as these factors will inevitably translate into a reduction in their usage by farmers, thereby lowering crop yields and provoking a further increase in food prices. The situation is even more dire for many small-scale producers in developing countries, for whom the lack of access to or prohibitively high prices of fertilizers will translate directly into increased hunger and poverty rates.

Like the developments in energy and food markets, industrial metals also registered sharp increases since the war broke out in late February. The industrial metals index rose by 9 per cent between April and February, with the price of aluminum and nickel (for both of which the Russian Federation is an important global supplier) registering substantial increases.

However, true to the sudden reversals observed in the last two years, talk of a sustained upward trend in commodity prices – with some analysts even prognosing another super-cycle similar to that seen in the first decade of this century – was quickly quashed as substantial declines were observed in the price of a range of commodities from April onwards. The aggregate commodity price index dipped by 12 per cent between April and July, with the prices of industrial metals and grains registering declines of 28 per cent and 21 per cent, respectively. Grain prices by mid-year had returned to the levels observed prior to the war, while in the case of industrial metals the downward movement in prices brought price levels close to those prevailing at the beginning of 2020, prior to the pandemic. With regards to energy commodities, the decline between April and July was more moderate, at just 1 per cent. However, comparing energy prices from their peak in early June to their value at the end of July, we observe a sharp decline of 18 per cent, with the notable exception of European natural gas prices which have remained near historical highs (figure 2.9).

A confluence of factors lies behind this generalized retreat in commodity prices, chief among which is a steeper than anticipated tightening of monetary policy in developed economies and a subsequent deceleration in economic growth, thereby softening the global demand for these raw materials. Similarly, a sharp slowdown of expansion of the Chinese economy, partly explained by strict lockdowns in response to new Covid-19 outbreaks but also by more long-term challenges and weaknesses in certain key economic sectors (see section D, chapter I), has dampened demand for commodities. This is particularly so in the case of industrial metals for which Chinese demand is an outsized component of global demand. On the supply side, two United Nations-brokered agreements with the Russian Federation, Türkiye and Ukraine – the Black Sea Grain Initiative to get grains out of Ukrainian ports, and the *Memorandum of Understanding between the Russian Federation and the Secretariat of the United Nations on promoting Russian food products and fertilizers to the world markets*, managed to ease upward price pressures on these products, and led to a 5-month streak of declines in the FAO Food Price Index.

However, as important as these physical demand factors on recent price dynamics are the financial factors lying behind price movements. The recent drop in prices points to the ever more financialized nature of commodity markets. As commodities have increasingly become a financial asset, huge

quantities of money are traded daily on commodity futures throughout global markets, with investors' decisions having an outsized impact on prices. In fact, part of the recent downturn in prices is crucially linked to the impact of the tightening of monetary policy in the developed world on investors' decision calculus (see box 2.3). Successive rate hikes by the United States Federal Reserve between March and July, totaling 225 basis points, have precipitated a significant increase in real interest rates. As a result, in April real yields on United States Treasury securities moved back into positive territory for the first time since March of 2020 and continued their upward trajectory, motivating investors to shift financial investments away from commodities towards such positive yield-bearing assets. These financial developments have played an important role in the recent retreat observed in commodity prices.

Although the prices of various commodity groups had by mid-year returned to levels similar to those observed before the outbreak of the war, it is important to remember that such prices do still represent historically high levels. Moreover, the recent drop in dollar-denominated international commodity prices has not translated into a significant easing of domestic inflationary pressures on these products in many developing countries as rapidly depreciating local currencies – an inevitable consequence of the abrupt tightening of monetary policy in developed economies – have kept local prices of many energy and staple food products at exorbitantly, and often prohibitively, high levels. As a result, poorer households in the developing world continue to suffer difficulties in covering their basic needs, while governments in numerous developing countries see their already limited fiscal resources eaten into due to the substantial energy and food subsidies they provide.

Looking to the latter part of 2022 and into 2023, heightened uncertainty on both the demand and supply side will translate into continued volatility in commodity markets, further complicating the picture for developing economies who are particularly vulnerable to such price swings. Broadly speaking, commodity prices are expected to remain elevated through 2022 and 2023 due to a combination of slowing growth and dampening demand that will be offset by continued supply and transportation constraints, as disruptions resulting from the war are expected to have a long-term impact on the supply of raw materials from both the Russian Federation and Ukraine.

### **Box 2.3 The war in Ukraine: a shock too far for global food systems?**

The war in Ukraine has served as a powerful reminder that local disturbances can carry global consequences. Between them, the Russian Federation and Ukraine are major exporters of vital agricultural commodities, including wheat, maize and sunflower oil, as well as fertilizers (United Nations, 2022a). The disruption to these markets has increased the pressure on international food supply chains, with demand, purchasing power, distribution, and production already under stress even before the war began.

The war comes on the heels of over a decade of turbulence in global food markets. This period started with several episodes of high and volatile food prices between 2007 and 2013. After 2015, the incidence of hunger started to rise, despite remarkable progress in China (FAO, 2020). Then Covid-19 struck at livelihoods, disrupting global and local food systems, although food workers were quickly dubbed “essential” and some local systems could adapt quickly to the changed conditions and were able to continue supplying food. Many governments in the world also helped food distribution systems by providing pandemic relief to their citizens in the immediate aftermath of the economic lockdowns.

The war represented a distributional shock. Ukrainian grains, for example, were still there, ready to be exported, but the primary export route via the Black Sea was abruptly closed. Initial uncertainty over how long the war would last inevitably sent prices higher. Existing contracts lapsed and buyers and traders scrambled to find new suppliers. The immediate implications of the supply shock were especially severe for the Middle East and



North Africa, a region that imports most of its grain from the Russian Federation and Ukraine. Behind that abrupt change, longer-term threats to agricultural production and storage in the region loomed large. The war also sent energy prices soaring, affecting fertilizer production costs even as both Belarus (before the war) and the Russian Federation' fertilizer exports were cut off. High energy prices also make the whole value chain more expensive, including the costs of food storage, processing and distribution.

The importance of exports from the region and uncertainty of how long the war would drag on also fueled speculation. Excessive speculation on commodity markets likely amplified the price increases for grains that followed the start of the war in Ukraine (Russell, 2022). Changes in futures prices for wheat were even more extreme, increasing by 50 per cent in the globally price influential Chicago futures market in February 2022, subsequently falling by 18 per cent in March.

Futures and forward contracts are normal market instruments, improving liquidity conditions by helping participants involved in producing, trading or consuming those goods to arrange a set price at a determined point in the future. Speculators have different objectives, betting on the direction of price movements. When many speculators enter into trades on agricultural markets with the same assumptions around crop, climatic and political conditions, they can amplify price movements in ways that are delinked from actual and anticipated supply and demand.

The German research institute ZEF (2022) found that the share of non-commercial traders (speculators) holding long positions (buying) in hard wheat and corn rose sharply to 50 per cent in early 2022, a situation that often corresponds to price spikes. Lighthouse Reports, an investigative journalism NGO, reported that in April 2022, investors pumped \$1.2 billion into two major agricultural Exchange Trade Funds (ETFs track market prices for a basket of commodities), compared to just \$197 million for the whole of 2021. Agricultural price indices are often a small share of the total ETF price index, but when energy prices are weighted more heavily in the ETF index formula, agricultural prices follow energy price trends. The United States and the European Union instituted some controls on financial speculation in physical commodity futures contracts in the wake of the 2009 financial crisis, but the controls have been weakened since.

For people who live in low-income, import dependent countries, even short-lived exaggerated price swings can have long term effects on food prices, increasing the incidence of food insecurity. Price swings delinked from supplies, especially when amplified by investors' expectations, disrupt planning for future crops and food supplies. In addition, the opacity and high levels of concentration in supply chains create the real risk that consumer prices will continue at historically high levels, even as farmgate and export prices have started to fall. New approaches to diversifying risk, including the establishment of grain reserves and encouraging planting of a broader variety of cereals suited to local climate and cultural conditions, would increase the stability of food supplies and prices.

More comprehensive information about supply chains could aid that process. The Agricultural Markets Information System (AMIS) was set up by the G20 after the 2007–2008 food price crisis to increase transparency in markets. For the most part, countries utilize reserves to smooth out supplies to national markets, although there are some important experiences with regional grain reserves in Asia, under the auspices of ASEAN, and in West Africa. While exact information on food stocks is difficult to gather, AMIS reports that “[l]ed by traditional holders of large public reserves such as China and India, grain stocks in developing countries more than doubled between the mid-2000s and today (FAOSTAT, 2020).” Of course, the existence of food stocks is not enough. They must also be available to stabilize markets. IPES-Food reports that the greatest knowledge of how much grain is at any given place in the world at any given time is knowledge held by private companies, in particular the “ABCD” of grain traders: Archer-Daniels Midland, Bunge, Cargill and Louis Dreyfus (Farchy and Blas, 2021). With those firms accounting for 70-90 per cent of global grain trade, their reserves are likely to be sizable. And with commodity speculation mounting, they have a clear incentive to hold stocks back until prices are perceived to have peaked (IPES Food, 2022).

On the demand side, financial speculators rushed into wheat futures, commodity swaps and agriculture-linked exchange traded funds (ETFs), immediately following the start of the war in Ukraine. The share of speculators in buy-side wheat futures contracts has increased from 23 per cent of open interest in May 2018 to 72 per cent in April 2022 (Agarwal et al., 2022). By April 2022, seven in ten buyers of futures wheat contract were investment firms, investment funds, other financial institutions and commercial non-hedgers whose aim was to profit from the rise in prices; Agarwal et al. (2022) find that investment firms increased their presence in the buy side of the wheat futures market in Paris from 4 per cent of open interest in 2018 to 25 per cent in April 2022, and investment funds increased their presence from 1 per cent to 21 per cent of open interest. Data from the CFTC also show increased speculative activity in wheat in the Chicago Board of Trade (CBOT), as is clear from the strong growth in Exchange Traded Funds (ETFs) linked to agricultural commodities in 2022. Financial investors are cashing in on rising food prices.

Public food stocks could play a role to stabilize markets and offset the concentrated power of the big private traders. Debates on international food security and stockholding often pit arguments to use free trade and global markets as the ultimate reserve against the long history of national public stocks as a tried and trusted food security mechanism. In fact, stocks and trade can usefully be seen as complementary strategies. If under perfect free trade conditions, public stocks create a market distortion, under actual open trade conditions—a context rife with market failures and distortions, including highly concentrated market power—public stockholding can be seen to offer important benefits. Ideally, public stocks will be thoughtfully integrated into commercial markets, to limit the power of either government or the private sector creating a widespread price shock. Note that stocks occupy a difficult terrain in economic policy where commercial and public interests meet and to some extent collide. Neither a purely private sector nor a purely government-controlled response is likely to prove as effective as policies that recognize the need for co-existence. Public stocks can provide a form of collateral in open markets, protecting against supply shocks that may curtail imports unexpectedly by bridging the gap before imports resume.

Some progress along those lines was made when countries at the WTO agreed in 2013 to refrain from challenging the way India procured food for its public stocks program until the rules of the Agreement on Agriculture could be revised to the satisfaction of all WTO members. The eventual negotiation of such a solution is a necessary first step. Those rules should include safeguards to ensure that public stocks are not dumped on international markets, where they could undermine farmers and food production in other countries.

The Ukraine crisis also showed a new wave of export bans and restrictions on foodstuffs from exporting countries. Things have eased a little since the spring of 2022 but the WTO rules in this regard remain inadequate, deepening the qualms net food importers already experience in trusting their food security to international markets (Espitia et al., 2022).

Other factors deepening the effects of higher food and fuel prices include the deepening debt crisis, a problem that has never really gone away, but that has risen again sharply due to the pandemic and the continued failure to force creditors to do something about the crippling effects public indebtedness has across developing countries. An estimated 60 per cent of least developed and other low-income countries were at high risk of or already suffering in debt distress, spending an average of 16 per cent of their export earnings simply to service their external debt—and Small Island Developing States averaged more than 32 per cent (see section B above). In 2022, these countries have seen the cost of their food imports rise, while their ability to pay has been eroded by the cost of servicing their debt, which has risen with rising interest rates, a higher valuation of the dollar, and higher risk premiums due to increased volatility in commodity futures and bond markets.

The crisis sparked by the war in Ukraine and the subsequent shocks to global supplies of grains and fertilizers drives home the imperative for diversification in which countries grow critical food crops. The unfolding climate catastrophe illustrates the need to diversify which crops are grown, both to respond to an increasingly erratic climate and to improve nutritional diversity. Global cooperation on those issues, as well as enhanced coordination on the regulation of markets, trade and reserves, could help to build resilience against the future shocks that are certain to arise.

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