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Journal of Policy Modeling 36 (2014) 717–744

Journal of Policy Modeling

www.elsevier.com/locate/jpm

What underlies the recent growth comeback in developing economies?☆

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Received 15 January 2014; received in revised form 15 February 2014; accepted 20 March 2014
Available online 22 May 2014

Abstract

We find that the frequency of growth takeoffs in developing economies has risen markedly in the past two decades, with recent takeoffs lasting longer than those prior to the 1990s. Also, unlike takeoffs prior to the 1990s, developing economies in recent takeoffs experienced an improvement in economic policies, with lower post-takeoff debt and inflation; more competitive real exchange rates; and stronger structural reforms and institutions. These conditions have tended to be associated in the literature as conducive to sustaining strong growth. We also find that the chances of starting a takeoff in the 2000s was triple that before the 1990s, with domestic conditions accounting for most of the increase. Thus, if developing economies improve their economic policies and sustain them forward, they are more likely to jumpstart takeoffs and avoid the reversals in economic fortunes that affected many developing economies in the past.

Keywords: Developing economies; Growth takeoffs; Structural reforms

☆ We thank Andrew Berg, Olivier Blanchard, Jörg Decressin, Romain Duval, Thomas Helbling, Andrew Levin, Chris Papageorgiou, Catherine Pattillo and seminar participants at the 2014 Centre for the Study of African Economies Conference, the 2014 Annual Meeting of the AEA, and the 2013 DEGIT Conference, for many helpful suggestions. Shan Chen and Angela Espiritu provided excellent research assistance and contributed substantially to an earlier version of the research work. The views expressed in this paper are those of the authors and do not represent those of the IMF or IMF policy.
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http://dx.doi.org/10.1016/j.jpolmod.2014.03.008
0161-8938/

1. Introduction

Following a lackluster performance in the 1980s, growth in developing or low-income countries (LICs) rebounded starting in the 1990s (Fig. 1). They have grown at a faster pace than advanced economies since the turn of the 21st century, and have even outpaced other emerging market and developing economies since the Great Recession. This sustained growth comeback in LICs argues for optimism about their future growth prospects.

For skeptics however, LICs' good performance may simply be an artifact of favorable global economic conditions, such as, strong commodity prices, and low interest rates, rather than indicative of a deeper change. LICs also grew at a rapid pace in the 1960s and early 1970s, only to decelerate sharply in the late 1970s and 1980s when global conditions turned sour. In fact, a sense of deep pessimism about LIC prospects pervades much of the literature, given their weak institutions, unimpressive economic reforms, and resource-curse challenges (see Easterly and Levine, 1997; Pritchett, 1997; Rodrik, 1999; Sachs and Warner, 1997; Sachs and Warner, 2001, among others). Thus, understanding whether today's dynamic LICs have truly improved their prospects of strong and sustained growth requires assessing whether their growth today is built on lower economic vulnerabilities than before. Addressing this issue is the main objective of this paper.

We make two small but important contributions to the empirical growth literature in this paper. First, using data from the early 1950s, we exclusively focus on the experiences of nearly 70 LICs to recognize the development challenges that are unique at low income levels and limited finan-

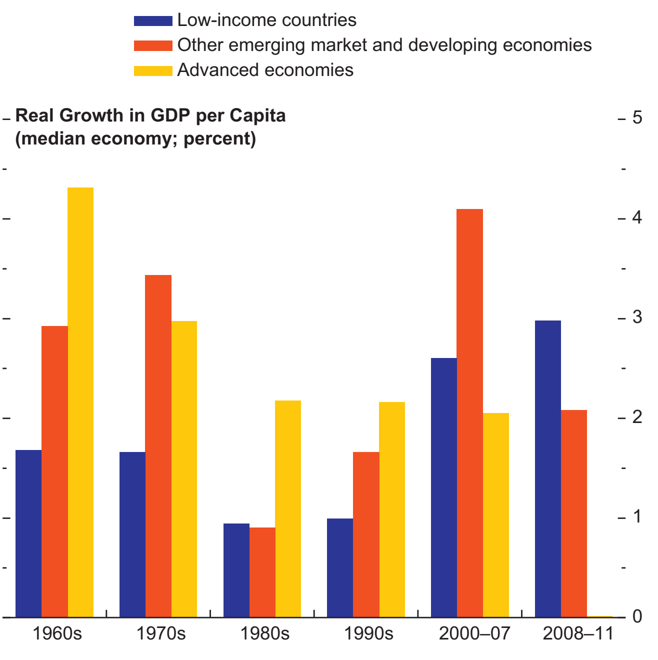

Fig. 1. Economic performance of low-income countries and others. *Note*: Economy groups and indicators are defined in Appendix 1. Real GDP per capita is in purchasing-power-parity terms. The 2008–2011 median of real GDP per capita growth of advanced economies is near zero (0.02 percentage point).
Sources: IMF, World Economic Outlook database (October 2012); Penn World Table 7.1; World Bank, World Development Indicators database; and IMF staff calculations.