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## 10 YEARS AFTER THE GFC: A LOST DECADE FOR THE EMERGING COUNTRIES?

*The term 'emerging markets' reflects to those countries that are undergoing structural and economic transformation and have the chance of becoming an advanced economy. However many research focus on this group, these countries are heterogeneous and face with different challenges. In the article, after an extensive definition of 'emerging markets' the recent economic, especially macroeconomic and financial trends are presented. The Global Financial Crisis was a turning point, but the path of recovery was far from uniform. As a novelty I present a new categorization in order to present the economic developments of the last decade.*

### 1. INTRODUCTION

Over the past decades many research have focused on the group of countries that are not yet considered as advanced industrialized economies but do have a significant chance of becoming one. These countries are often referred to as **'emerging economies' in the literature, as they are on the path of catching up**. The process of convergence is complex, but economic and political transformation were one of the common points these countries have shared.

In the late 90s and early 2000s several emerging countries fell in crisis proving that financial stability is a necessity for a converging country as one episode of crisis could slow down the growth progress significantly.

The Great Financial Crisis in 2007 was a breakpoint for the global economy too, though. As it is now clear, the crisis started with the subprime crisis in the US and later developed further as the contagion in the globally integrated economy spread. Contrary to the prior currency and bank crises in the developing countries this time the crisis was international, and mainly affected the advanced economies. As such, understanding the last decade of the emerging countries cannot be separated from crisis management of the major central banks and the governments of the industrialized countries.

The main aim of my paper is to **present the post-crisis development of these countries**. In order to illustrate the processes, I first define the group of countries, indicating that a single definition can hardly be assigned to the so-called country group. After doing so, I will briefly present the impact of the 2007-2008 **financial crisis on emerging economies and the economic policy challenges they faced in the post-crisis period** both in macroeconomic and financial extent. The recovery did not follow the same pattern in every cases, so going back to the path of convergence resulted different paths of economic policies. Instead of giving an overall conclusion **I propose a categorization for these countries**, and I am examining the most important macroeconomic and financial indicators for different country groups.

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## 2. EMERGING ECONOMIES – PROBLEMS OF CLASSIFICATION

The group of emerging countries is hard to define, as there is no common international organization of them, and even the criteria for classification depend on research and context. A common definition was given by Kvint in his book: ‘Emerging market country is a society transitioning from a dictatorship to a free-market-oriented-economy, with increasing economic freedom, gradual integration with the Global Marketplace and with other members of the GEM (Global Emerging Market), an expanding middle class, improving standards of living, social stability and tolerance, as well as an increase in cooperation with multilateral institutions’ (Kvint, 2009)

Many authors argue that the term **‘emerging country’ is now an outdated category**, as the countries listed are different in many respects: their level of development and the challenges that they are facing. On the other hand, from a financial point of view, many institutional investors consider emerging markets as a separate asset class those of non-developed countries whose capital markets offer a suitable investment opportunity.

The categorization of the IMF lists emerging and developing countries together, distinguishing them from the developed ones. These categories are used in the ‘World Economic Outlook’, which is an analysis and forecast published every six months, and here the world economy is divided into regions and types of economy. The three aspects are considered as the level of national income over the long-term average, the diversification of exports and the degree of integration into the global financial system. Categorization varies from time to time, for example, in the case of joining the euro area, the country is always classified into an advanced category. Accordingly, Hungary, Poland and Romania are classified in the emerging country group; but they consider Slovakia and Slovenia as developed countries. The World Bank uses a simplified system in its analyses as it classifies the countries into five categories based on the level of national income per capita. (Daniela-Neonila, Mardiros and Dicu, 2014; Ioana-Cristina and Gheorghe, 2014)

The largest countries that are often considered emerging, **are also known as BRICS countries** as Brazil, Russia, India, China and South Africa are counted as the most influential and geopolitically most important countries: all of them are regionally important and large, but not yet advanced. These 5 countries have established an international organization in 2015 (Financial Times, 2015); which is supposed to coordinate these countries’ policies on many level. The world economic weight of the five major regional powers is unquestionable, however, their economic development and structure are extremely diverse. The growth of China’s global economic weight is probably the most striking: thanks to its extremely active foreign trade activity, it has produced the region’s highest growth figures in recent years, although China’s growth is slowing down. The US government bonds, which have been accumulated as a reserve of about 1100 billion US dollars (representing nearly 20 percent of US debt on the market); and the inclusion of the Chinese renminbi into SDR-basket made China’s economy extremely prominent. Brazil, India and South Africa operate in a traditional market economy model with a freely floating foreign exchange policy and an inflation targeting monetary framework, their size and regional power are both in foreign trade and in economic output. Russia has been hit by sanctions and oil prices in recent years, but its size and location have geopolitical significance.

Beside the BRICS countries **we may define a separate category that ‘does not currently play a major role in the region but can become a medium term in the future’**, such as Turkey, Indonesia, or Mexico. In addition, the classification of smaller countries is typically determined

by the investor's view of whether there is a sufficiently large and relatively liquid securities market and whether there are capital restrictions in place.

The categorization used by academics might be interpreted as practical, either. It is a key importance to hold good-quality and available data in order to examine economic issues for example, the long-term government bond yield used as a proxy for long-term macroeconomic expectations and the CDS premium for default risk is a best practice but only works if these data are available from a lively security market. In the literature **it is quite common that emerging markets are defined as constituents of MSCI Emerging Market Index**. Others, for example, combine the World Bank classifications with the countries' accessibility to IBRD loans. (Tatiana Didier *et al.*, 2012)

Many definitions approach these countries from **institutional changes** undergoing, others from **developmental and macroeconomic aspects**, but practical considerations would call for **financial approach as well**. In the article I am going to focus on macroeconomic and financial conditions mostly.

### 3. RECENT TRENDS: WHAT HAPPENED SINCE THE GFC?

In this section I am going to present the economic processes that influenced emerging markets in the post-crisis era. The Global Financial Crisis (GFC) was a breakpoint not only in the history of emerging, but advanced economies as well. The recovery and the new upswing of the business cycle did not happen in the same way though. As the GFC was mainly a financial crisis (Cayon, Thorp and Wu, 2017) looking at **financial and capital market pricing seems to be a good choice in order to understand the general processes after the crisis**. Following this logic the primary focus is on the financial market processes, and in connection with economic policy financial policies, especially monetary policy is discussed. In the rest of the chapter I am going to identify those breakpoints that characterized the post-crisis period then I am going to highlight some of the ongoing processes chronologically.

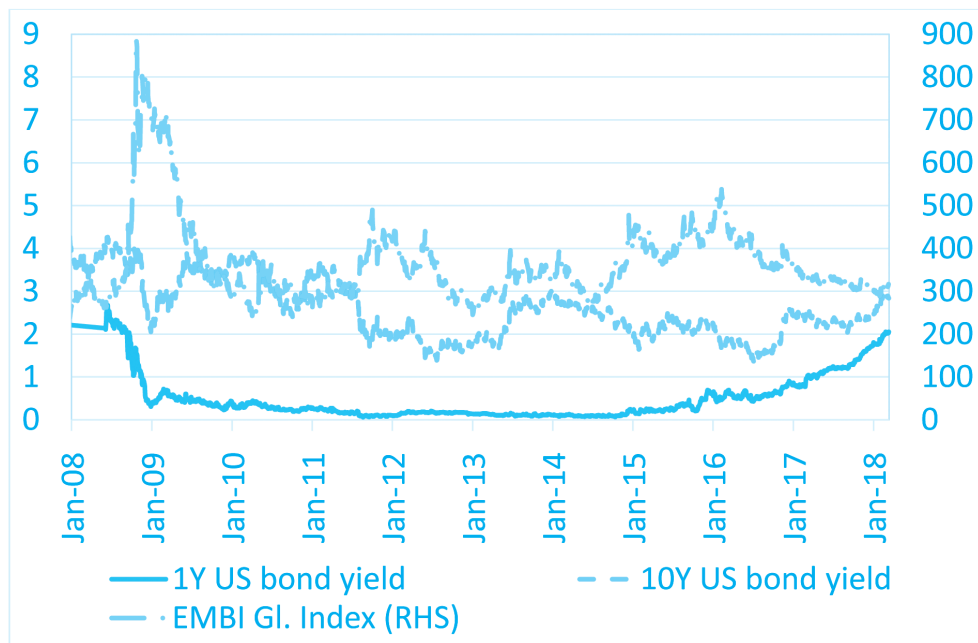
#### 3.1. IDENTIFYING BREAKPOINTS

In order to finding the turning points of the last decade emerging market government bond yields, proxied by EMBI Global Index is used, in light of the short and long-term US. government bond yields. In my view these pricing can shed light on the ongoing processes with special regard to the financing of government budget and investment sentiment.

From the viewpoint of the emerging countries the crisis started in the 2nd half of 2008. As risk of global contagion spread among the financial and capital markets risk premia rose, hence government bond yield rose as well, as it is shown on the composite index of EMBI Global Emerging Index. In the US interest rate cuts by the Fed and the early phase of unconventional tools used by the advanced central banks **risk-free rate decreased**, short-term government bond yields fell significantly. In parallel, growth expectation worsened which led to the decrease in longer segment of the market as well. As a spillover, with the decrease of the **risk-free rate the emerging government bond yields decreased soon**, nearly to the pre-crisis level. Later the low rates persisted, as the major central banks had continued easing, combining with the recovery of the world economy neither emerging nor advanced markets were not under pressure. In 2011

concerns with global growth and European sovereign debt crisis put pressure on EM markets, especially in Europe, while the new phase of Fed easing took place which pressed longer term rates lower. In 2013 as a result of ‘the tapering talk’ yields in emerging countries rose, just like in 2015 when emerging market sell-off took place. As the Fed started to raise its interest rate, first the shorter, then the longer-term US yields started to increase but **this time there was no turbulence on the financial markets**. Beside the global tightening, sharp movements in the oil price and the elevated tension associated to geopolitical risks played important role in the recent years. However, the relative stability of the composite index suggests that only short-living, local effects were typical. In short, after the crisis long period of favourable conditions lasted, but some episode of minor financial turmoil interrupted the post-crisis recovery in some of the cases.

Chart 1. Emerging vs. US yields<sup>2</sup>



### 3.2. AFTERMATH OF THE CRISIS

As many authors confirm (Dooley and Hutchison, 2009; Chivakul *et al.*, 2010; Kenourgios and Dimitriou, 2014) there were *no obvious warning signs of global crisis outside the US* as the most important indicators, such as CDS premia, government bond yields of emerging (and other advanced countries) remained broadly unchanged until the collapse of Lehman Brothers

<sup>2</sup> Source of data (all charts): Bloomberg

in October 2008. Despite the generally positive view on EM assets, with special regard to the appreciation of currencies and accumulation of foreign reserves in many countries during 2007 (Dooley and Hutchison, 2009) in some countries such as Hungary, Iceland **serious macroeconomic imbalances had been developed** by 2008. (Claessens *et al.*, 2010)

Chronologically before the collapse of Lehmann Brothers we may reflect to a **subprime phase of the crisis**, while after it the global phase began. (Ait-Sahalia *et al.*, 2012) As a reflection of the American processes the international financial markets reacted heavily, especially the interbank, and foreign exchange markets, and the stock exchange. As many contemporary reports confirm the **reaction was obviously negative and immediate** – the fear and distrust among the market participants was a reaction to the American interbank credit freeze. (IMF, 2009) However it is debated whether the reaction of international market was a contagion or just a spillover of negative happenings. A research done by Morales – Andreosso-O’Callaghan (2014) after examining 58, mainly Asian and Latin American markets, found no clear evidence of contagion coming from American stock exchanges, but negative effects were the result of spillover. Although many broader or narrower definitions exist in the literature they argue that the simultaneous negative consequences were not **the result of the same or common problem but the result of high level interconnectedness, so it should not be reflected as ‘contagion’**. In their empirical research they presented the transmitting countries (markets) with the correlation based network model. (Morales and Andreosso-O’Callaghan, 2014)

As IMF (2009) noted in the Global Financial Stability Report during half-a-year the financial market conditions worsened in the emerging countries, especially in Europe. However global liquidity conditions eased somewhat as a result of major central banks intervention emerging countries still faced to serious financing difficulties as risk appetite remained much lower than before. (IMF, 2009)

At least **3 channels worth to consider in the post-crisis recovery of emerging economies**. First, the **adjustment of domestic economy** took place in those countries where it was necessary, it mainly affected the budget deficit, current account, deleveraging of households and further institutional changes. These adjustments were necessary in economies **where resilience was low** and the negative effect of the crisis hit directly.

Secondly, the **slowing down of world economy and international trade** effected negatively those export-oriented countries that could not replace the export with domestic growth. It means that economies with higher degree of openness but lower degree of diversification in output suffered from the slowdown mainly.

Thirdly, **the reaction of financial market participants was crucial** mainly for those countries which were mentioned in the first two channels as investor trust and capital movements were still fragile. Regarding to the financial channels one may consider many factors besides resilience and openness such as political stability, relationship with international institutions and investors, growth prospects, geopolitical issues as well.

On monetary policy level two typical responses were observable in case of the emerging countries. Those who suffered from the turmoil and sharp movement of financial indicators the policy makers maintained **stricter monetary policy in order to avoid capital flights**. While others, those who had better fundamentals, could follow the Federal Reserve in easing policy and reacted counter-cyclically.

It is clear that the Great Financial Crisis was a major turning point in the history of the global economy but it is more difficult to quantify hence more controversial **how it really affected the emerging countries in general**. (Tatiana Didier *et al.*, 2012) On one hand, as it has been presented, the category is not completely homogenous hence **different countries had better or worse resilience against external shocks** which may lead to different paths of crisis management and recovery. On the other hand, between the first warning signs in the US and successful recovery long time had passed. In the beginning of the period we might identify the signs of financial contagion, but as the American crisis management went forward the spillover effects of the central bank decisions should be followed. (Bekiros, 2014) After the American and the advanced economies relatively had cooled down the change in the structure of international trade was threatening for the emerging countries. Cross-border portfolio and FDI-flows must be separated also: investment decision took place after the financial turmoil, but before the adjustment of the real economies.

### 3.3. CRISIS MANAGEMENT AND RECOVERY

As it is extensively analysed in the literature the post-crisis path of world economy is impossible to separate from the **crisis management of the sovereign governments, and central banks**. These measures might be categorized upon many approaches. We may differentiate the direct 'crisis management' from growth-promoting economic decisions; as the former reflects to the frictions of the economy directly related to the ongoing crisis; the latter is a broader category which aims to promote quick and healthy recovery of the economy. Regarding the effects of these economic tools we might reflect to desired domestic effects that are the expected reaction of the respective economy; and – as it is often examined in the literature the spillover effects of these decisions. These spillovers are usually attributed to the larger, more advanced countries as they might have regional or global effect. Finally, we may differentiate policies that are targeting the financial sectors, the government-led expansion in the real economy, and other measures such as export promotion or institutional changes. All these policies aimed to put the economy **back on track after the crisis, with smooth and painless recovery**, however sometimes this aim could not be reached without hurting of some domestic interest groups.

However economic policy has a wider toolkit to have an impact on the economy but mostly politicians considers solely the effective reaction of two major part of the financial policies, **the fiscal expansion, and the reaction of the central bank with an appropriate monetary policy toolkit**. Counter-cyclical fiscal policy would contribute to recovery after a crisis episode, but in many cases, there were no such a place of manoeuvre. In case of the United States the fiscal deficit of 9.8 and 8.65 percent of the GDP in the financial years of 2009 and 2010, respectively, shows an intention of fiscal expansion, but many emerging European countries used relatively strict fiscal policy in order to maintain the trust of foreign financial investors.

Many literature could be found regarding the **domestic and international effects of the monetary policy decisions**, though. The standard thinking of monetary policy is delivering an anticyclical policy with the help of financial markets, in order to influence the macroeconomic stance in 18-24 months. In case of negative shock which is likely to cause decrease in growth and inflation over the policy horizon the easing of monetary conditions is needed. In other words the policy response is a rate cut which makes the credit cheaper, the financial assets more expensive,

and the currency to depreciate. (Mishkin, 1996) After the crisis the monetary policy changed, as a result of newly emerged challenges such as the 'zero lower bound' which describes the reaching of minimum of policy rate level. The toolkit widened and among other, large-scale asset purchase programs have been started by the major central banks. The efficiency of these unconventional measures is assessed by many authors, usually in comparison with the conventional tools. In case of programs conducted by the Federal Reserve many research confirm that they were efficient, but in some cases the impact was limited in time or to some maturity. (Gagnon, Raskin and Remache, 2011; Amico *et al.*, 2012; Wright, 2012) However, these policies were mainly implemented by advanced countries, the international impact of them affected emerging central banks as well.

Chen *et al.* enumerated 4 channels where international spillovers might had positive impact on – at least the financial sector – such as the fall of US premium, the confidence channel, trade and bank lending channel. (Chen *et al.*, 2012) Those who assessed this impact quantitatively tried to measure the signalling and portfolio-rebalancing channel of the policies. While many authors find evidence for the former, which means that cross border flows dominated the market ((Joyce *et al.*, 2010; Gagnon, Raskin and Remache, 2011) others argue that latter was more significant. It means the impact of advance central banks did play a measurable role in effecting the conditions in the emerging countries, simply on financial level: both the perception of the investor both cross-border portfolio flows could cause sizeable changes (decrease) in yields of emerging markets.

Using of asset-purchase programs was less prominent though other unconventional measures were actively used by many central banks such as the Hungarian, the MNB. (Ábel *et al.*, 2015) So the extended place for easing in case of EM central banks was largely attributed to the impact of major central banks' policy. Both were in favour of growth, and credit expansion, via the favourable financing environment which helped the economy to recover. However in some growth accelerated slowly, or without any credit expansion. (Bodnár *et al.*, 2015)

**The result of the supporting international financial condition and the upward phase of the business cycle contributed to quick recovery and strong growth cycle in many cases, only few, vulnerable and overheated economies lagged behind as a result of adjustment.** Moreover, as we might have the impression from raw data that EM recovered faster and went back to pre-crisis path of growth empirical researches conducted by Didier *et al.* (Tatiana Didier *et al.*, 2012) Even some analyst called the emerging countries the **new engines of global growth as their speed of recovery** hence growth patterns were much more favourable than of the advanced ones. (Canuto, 2010; Gevorkyan and Otaviano, 2016) These authors mainly discuss whether the recovery of these countries is the result of the business cycle or some of them could gain advantage from the crisis and could reach a higher growth but with still sustainable conditions.

### 3.4. FROM SLOWING DOWN TO 'TAPER TANTRUM'

Divergence between EM countries has started to develop in the beginning of the 2010s. Many of these countries experienced enormous capital inflow as a result of extremely easy global monetary conditions provided by the major central banks. Policymakers' dilemma was finance-related this time: with the capital inflow the domestic currency faced with appreciation pressure, as the participation of foreigners raised on the local capital markets. This has contributed to adjustment in monetary stance, EM central banks cut interest rate in order to avoid appreciation

of the currency. On the other hand, recovery went forward, sometimes faster than expected. With credit-bubble the growth accelerated further causing the overheat of some EM country (Magas, 2018).

We may identify at least 3 different paths after the crisis: 1. in Eastern Europe the macroeconomic adjustment legged behind which was an unfavourable environment for the global investors. 2. some EM recovered and grew in a faster pace, but at the same time the vulnerability to external factors diminished. 3. some large EM grew without accumulating reserve and with serious vulnerabilities.

As the IMF noted in World Economic Outlook, published in September 2011 one of the key downside risks for the **global economy was the overheated credit expansion in some of the emerging economies**, namely in Brazil, Colombia, Hong Kong SAR, India, Indonesia, Peru, and Turkey. (IMF, 2011)

A major turning point was May 2013 when Fed Chair B. Bernanke and other Fed senior officials indicated that **the discussion of ending the asset-purchase programs, is timely**. The event is later called ‘taper tantrum’. As Aizenman et al. found those countries that were considered ‘fragile’ based on current account balance, reserve adequacy and external debt, had experienced bigger depreciation, drop in stock market, and increase in sovereign CDS spreads. They explain that countries received more inflow in the precedent years had stronger response at this time as more capital were subject of repatriating. This later called ‘**in-and-out hypothesis**’. (Aizenman, Binici and Hutchison, 2014)

Others, such as Misha et al. confirmed that better fundamentals were associated with less outflow from government bond, and less turbulent money market reactions but notes that stock market reactions were less differentiated. (Mishra *et al.*, 2014) Regarding the effect of liquidity of these markets two articles finds that markets with better liquidity suffered greater outflows, but while Eichengreen and Gupta finds it as a result of easier rebalancing of foreign investors, Karolyi and McLaren did not do so. (Eichengreen and Gupta, 2015; Karolyi and McLaren, 2017). Those countries that suffered the biggest depreciation and remained sensitive to the change of international sentiment were named ‘fragile five’ after this event. (India, Brazil, South Africa, Indonesia and Turkey)

### 3.5. MUTED EFFECTS OF US. RATE HIKES, OIL PRICES, TRADE WAR

After the ‘taper tantrum’ the focus of the investors and policy makers turned to the future rate path of the Federal Reserve, as it was clear that sensitivity to American happenings are still on the menu and it was far from sure whether tightening policy of the American central bank will lead to general emerging market shock with wide depreciation of currencies and tightening of liquidity conditions, or ‘fragile’ countries have to fear only.

In case of US. tightening the opposite effects are expected then it was observed in the recent global easing cycle. As risk-free rate rise not only the financing of external debt will be more expensive but the capital flows could reverse as well. Empirical findings suggest that a reverse-way is more sudden, and could cause sharper movements in economic indicators. (Forbes and Warnock, 2012) **All in all, the expected movements in the emerging countries were depreciation of the currency and rise in yields, on longer term slow-down of the economy and FDI-inflow, but the result of rebalancing are only observable ex-post.** (Almansour et al., 2015)



At the end of 2015 the Federal Reserve hiked the interest rates first time since the GFC. **Market reactions were weak, immediate spillover to other advanced and emerging countries were muted as the decision was widely expected by market participants.** Many authors argue that this outcome can be attributed to communication strategy conducted by the Fed, the anticipation of the decision and the timing – as it was near to the year end. In the next months there were no evidence for market panic or sudden reverse of capital flows, however some oil exporting countries experienced the consequence of persistently low oil prices. However, the global tightening is still in progress, with the oncoming tapering and rate increase by the European Central Bank, for example; there was no sign of general shock in the countries examined.

While in July 2014 the price of the Brent oil was over 110 USD per barrel, nearly 7 months later in February 2015 it was around 60 USD, and in February 2016 it reached its lowest with 30 USD. **However, oil is a very important input for the economy this shock did not mean the same for every of them.** Oil-importer countries experienced lower input costs, and lower inflation which could further boost the economic growth. Oil-exporters received less for the same amount of oil on the world market, so some of them experienced currency pressure and the policy makers had to address questions about the sustainability of the government budget as usually the revenue from the oil is one of the most important of all. In case of Russia lower oil-price threatened the fiscal stability seriously, and political concerns related to Russian foreign policy challenged the stability of ruble occasionally. In case of Venezuela, inflation accelerated, and society-wild negative consequences appeared as a result of disappearing state revenue. After many rounds of negotiation oil price is increasing slowly now since the second half of 2017.

As we go further from the crisis it is even **more difficult to discuss the emerging countries uniformly.** Some countries experienced shocks, and sudden capital movements, but it is mainly attributed to local factors. However some points should be left for further research. As it seems after a decade, the studies about vulnerability in case of countries are still valid at some points. The general overheatedness of the country might be a concern domestically, but the international position i.e. reserves, current account balance is more important. After the crisis years it was out-of-focus what policy makers did in the economy, but the global business cycle is approaching to the end, the global liquidity is about to decrease, and the resilience will become more important than it was. In other words, sustainable growth for emerging country is still a receipt to be found, and resilience is a tool to use in order to avoid crises.

#### **4. HETEROGENEOUS COUNTRIES – DIFFERENT PATHS**

As it has been emphasized many times these processes could be fit in a broader perspective and the results substantially relies on sentiment and country grouping. At this point of the research following authors in the literature we may differentiate the countries in order to present quantitatively the post crisis era. Doing so we may follow two different research methodologies.

On one hand, we may do a **'bottom-up' selection** which means developing a methodology to make categories of countries upon existing data, such as (Sensoy et al., 2016) did in their research. They used **correlation matrix** to find those groups which fit the best. Other possibility to employ a **principal component analysis**: as it was done by Stolbov and Schepeleva the extension to financial stress indicator could work as a base of the categorization. (Stolbov and Shchepeleva, 2016)

On the other hand, we may **categorize the countries intuitively**, upon common sense and perception. This is a **'top-down approach'** that I am going to develop further. Choosing this way, we collect the data for selected countries, then with aggregating the changes we have the opportunity to conclude general ideas. However, this methodology is **less robust and leaves more possibility for false categorizing** the results are more likely to be interpreted smoothly. Regarding to the method of aggregation our choices are rather limited due to the availability of comparable data. From those, the five chosen are widely used variables and subject of the analysis conducted.

In order to present overall growth pattern real GDP yearly change, for internal balance CPI yearly change, for external balance BoP will be presented; regarding to financial markets the presentation of government bond yields will be done. In the calculations simple average of data is considered as group average and analysed further. The logic behind the presentation of the variables is the following. First, the financial indicators will be discussed, because the **main channel of international effects are likely to be found in these series**, as a reflection of external impact of advanced countries' policies. At this time short-term (3M) and long term (10-year) government bond yields will be presented. For further discussion of international factors current accounts will be presented. Finally, the average of domestic factors namely the growth patterns and CPI will be discussed. Assessing the overall status of the economies we need to present the cyclical position of the respective countries, with identifying the deviation from potential output: although many models and calculations were published on this topic, this time growth will be presented as output and inflation figures will be used as a proxy of heatedness: the growing pace of the inflation is associated with the possibility of overheatedness.

#### 4.1. GROUPS OF COUNTRIES

Without repeating the challenges of finding a correct country grouping elaborated in the 2nd chapter, emerging countries will **be divided into four groups**. First, the largest and most influential countries to be considered: the 'BRICS' as we earlier mentioned, not only the biggest in population and in territory among the countries but these countries have the greatest chance of evolving to global power centre in the near future: not only economically but politically as well. However averaging these 5 countries might be misleading if we are looking at possibility of becoming the global growth engine (as (Gevorkyan and Otaviano, 2016) noted) but the **relative positions of these countries are fairly close** to each other on regional level.

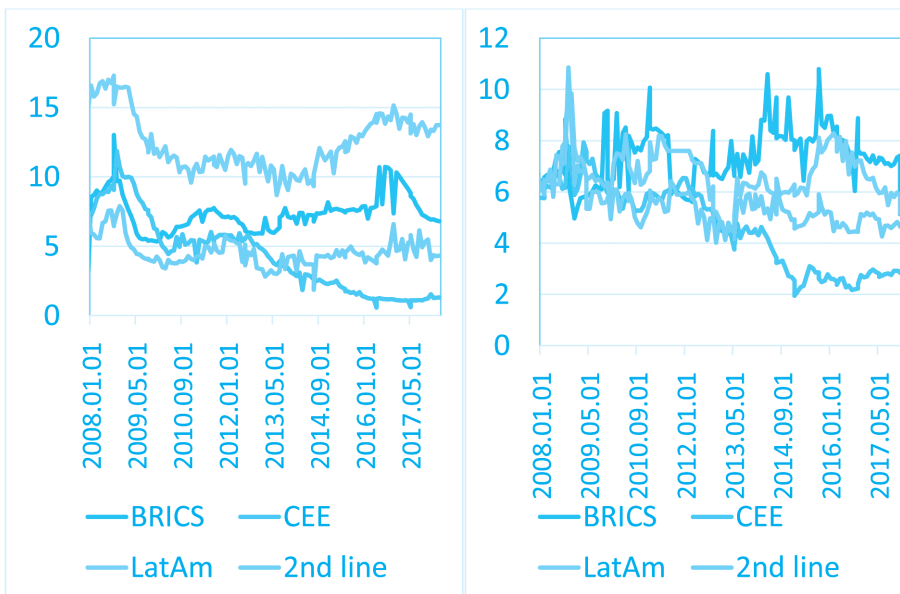
Following this logic, **we may identify countries that might be local hegemon** in the near future, or those countries that still have such an economic and political power that provides indispensable status for them. This category might be the most debated, but the previous definition broadly applicable for Turkey in Europe; South Korea, Indonesia, Thailand, Vietnam in Asia, Mexico in Latin America; and for Nigeria, Egypt, UAE, and Qatar in Africa.

The remaining two categories consist **smaller, but open and liberalised economies with broadly open financial market**. The two groups are defined upon the geographical position of the respective countries. **In LatAm group** the following have been classified: Argentina, Columbia, Venezuela, Uruguay, Costa Rica, Peru, Paraguay, Jamaica, Panama, and Bolivia. In the **Central-Eastern European category** is now defined as the group of Hungary, Romania, Poland, Croatia, Czech Republic and Serbia.

## 4.2. FINANCIAL FACTORS

As it was earlier discussed **the financial conditions were dominant in the last decade**. Short term yields are mainly driven by expectations about near change in policy rate, while long term yields are reflections of longer horizon developments, such as expectations of real economy and uncertainty. (Horváth et al., 2014) Looking at government bond yields we may conclude that there are differences between groups and the two maturities chosen. Regarding to the short term yields the short-living upswing in 2008 might be attributed to rise of short term yields and rate hikes conducted by central banks as a crisis response. Later, there is a **sharp decrease and short-term yields stabilized for long**, except in the **CEE region where eurozone sovereign debt crisis induced rate hikes** and worsening of financing conditions. Since 2014-2015 the CEE yields decreased further as a result of monetary easing conducted by the ECB. In Latin-America, and in the BRICS countries short term rates rose, but in case of BRICS it was temporarily. Regarding the long-term government bond yields, prior the crisis the **average bond yield was broadly the same in all of the four categories**. As a result of the crisis, yields in the ‘2nd biggest’ category and in Latin America rose suddenly while in Europe, and in the BRICS countries the rise was less prominent. However, we need to add that in the former group some extreme outlier = case of Latin America some extreme outliers drove the figures that time. **By 2010 long term yield reached the pre-crisis level on average**. It is interesting to highlight that after the ‘tapering tantrum’ yields in Central Europe did not jump as much as in the other two categories, and since 2014 spectacular decrease took place as ECB began a new phase of easing, and local central banks had further room. In the last two years no sharp change to be found, despite the rate hikes by the Federal Reserve but the divergence between country groups is worth to consider.

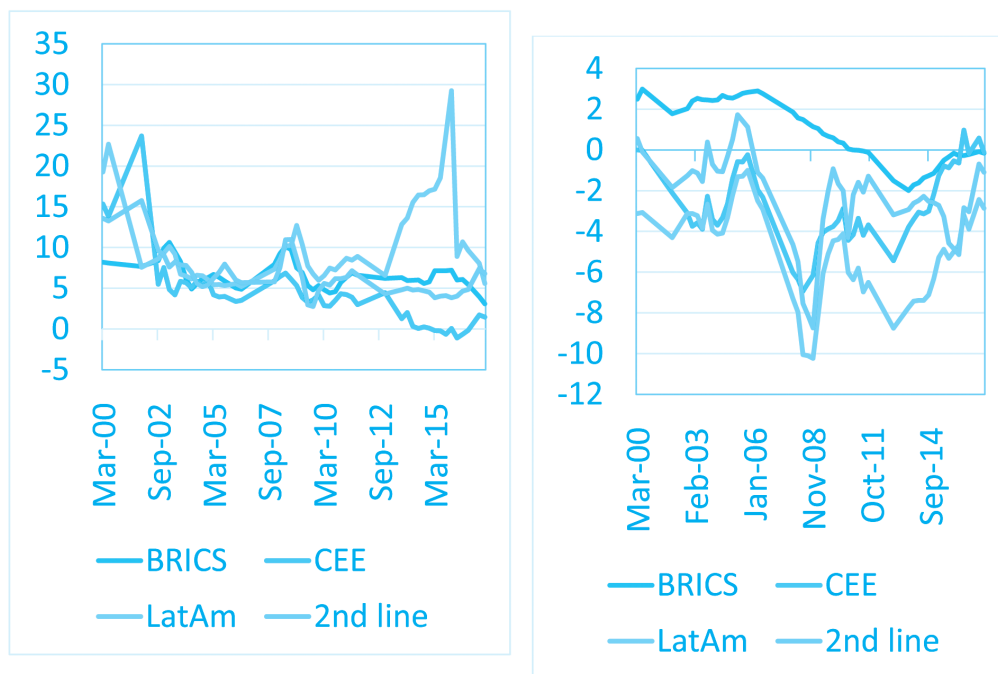
Chart 2. Short-term (3m, left) and long-term (10y, right) government bond yields (percent per annum)



### 4.3. EXTERNAL AND INTERNAL BALANCE

We reflect to CPI as a proxy of heatedness of the economy and current account balance as a proxy of the external position of the respective countries. At this point, one should note that while the overall heatedness is possible to handle directly via monetary policy decision, the external adjustment is usually out of scope of the economic policies. As it was earlier noted the general decline in **inflation in the beginning of 2000s was attributed to technical factors**: as more and more emerging country chose to introduce inflation targeting framework as a monetary policy regime the CPI did significantly changed in these countries. (Mishkin and Schmidt-Hebbel, 2006) While in the Central European region the inflation fell to relatively low, in the bigger countries and the smaller open economies in Latin America still had higher figures; and the inflation accelerated further as the low-yield environment of the mid 2000s stimulated these countries. During the crisis strong depreciation lead to the **temporarily rise of inflation**, specially the price of imported goods, later the slowdown moved along with slowing inflation.

Chart 3. CPI yearly change (left); current account balance as a percent of domestic GDP (right)



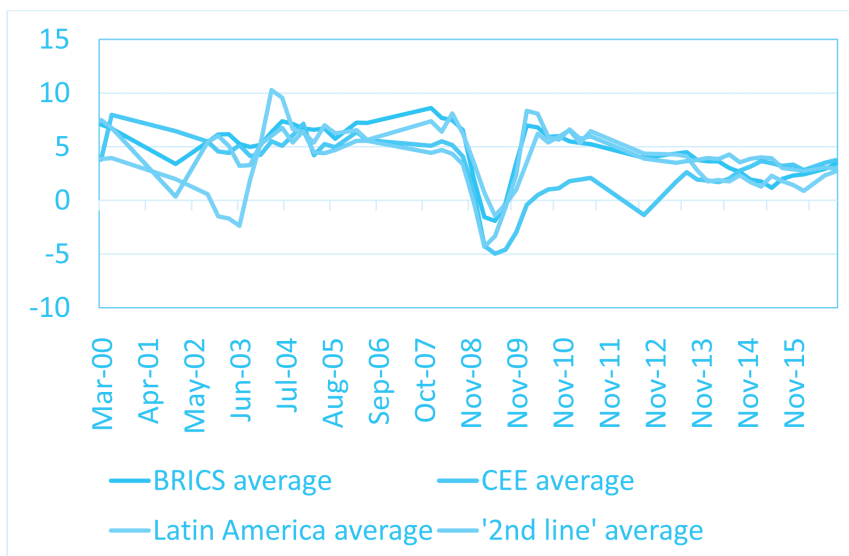
In the recent decade inflation patterns differed slightly among the groups presented. As a result of the European slowdown and extremely low inflation in the Central European region the fall of CPI is spectacular. **In Latin America the inflation accelerated rapidly since 2013 as a result of rapid growth and depreciation against USD.** Regarding to the largest, and 'second largest' country group we may observe a relatively stable pattern: while the rates in BRICS decelerated somewhat, in the 'second largest' group accelerated in the last years.

In case of the current account balance (measured as a percent of GDP) **sharp worsening is worth to be observed prior to the crisis**. However, the current account surplus of the BRICS countries remained, the surplus decreased. **While Central European countries adjusted smoothly and closed the average balance to nearly zero; in case of the LatAm and 'second largest' group took more time.** As the current account deficit of EMs slightly disappeared since the crisis one of the structural vulnerability improved notably.

#### 4.4. ECONOMIC GROWTH

Looking at the growth patterns in the country groups we note that all groups had stable growth before the GFC, however the Latin American figure lagged behind as a result of the currency crises at the end of 90s. During the GFC all groups perceived **a great downturn in GDP: the hardest hit was received by the CEE region** while in BRICS countries and in Latin America the average drawback was as low as 2 percent. In the recovery phase emerging countries grew notably, however the **CEE region lagged**. In the other regions the rebound of real activity followed something similar pattern. However the slowdown was common in all groups, the **European figure shows a 'W'-like recession as a result of European debt crisis, perhaps**. Despite the slowdown until 2014 most of the countries showed an impressive growth. This shift is a breakpoint here: while BRICS and Latin American economies slowed down notably, the 2nd group have experienced only smaller negative move. The relatively strong performance of the CEE region might be attributed to the relative isolation of global processes as the positive European progress and the easing of ECB effected the countries in a positive way. In 2017, however, all the country groups delivered some growth despite the negative shocks predicted earlier as a result of tighter financial conditions.

Chart 4. Real GDP yearly change



#### 4.5. ARE THERE DIFFERENT PATHS?

However this comparison allows us to get premature intentions about the underlying processes, we may conclude the research as follows. While the above compared economies has much in common, it seems that they eventually reflect differently. Though our categorisation is a primary approach, we have the possibility to distinguish common and group-specific factors. After the crisis most of the emerging economies recovered quickly, but the small open economies of the CEE region suffered from a setback as European sovereign debt crisis developed. In the recent years, while the bigger states lost their steam, Europe showed significant acceleration. While the level of inflation is widespread the historically low level of the Central European countries are interesting, and could be interpreted as a result of struggling European growth. At the same time external balance is the strongest in this region as well, which is in line with the extra loose financial conditions despite of the global tightening. As a comparison in Latin America wage and exchange rate depreciation boosted the CPI with a less balanced external position. In terms of government bond yields, short yields reflected to monetary policy, while longer term yields diverged in the sample. In case of smaller open economies we may identify notable differences as a result of many reasons, such as different sensitivity to Federal Reserve movements which significantly differs in the case of the two regions. (Kocsis and Tóth, 2017)

### 5. CONCLUSION

Those countries which were transforming into ‘market economy’ provided many aspects for researchers. However those countries used to be called ‘emerging economies’ this category should be reevaluated, as these countries went on different path. Some of them are large, with big population and playing a relatively important role politically as well. There are some followers which have the chance of achieving local importance, beside the first group. And finally there are small open economies, which have totally different challenges to face with.

As it was widely discussed in the last decade the global financial crisis was worldwide so hit nearly all the countries, and was mainly financial related. Following this logic, the article discussed the financial and macroeconomic situation of those countries, which are not yet considered ‘advanced’ but do have economic system which let us examining the evolution of the economy. After the financial crisis the effects of the financial crisis was mainly attributed to the former resilience and macroeconomic stability, as those countries that were imbalanced suffered from deeper recession. After the crisis the economies went back to the track of growth, partly due to the nature of the ‘business cycle’, partly due to the crisis management of the local governments and central banks. Regarding financial conditions cross-border effects of advanced central banks’ policies also played a significant role, as the global liquidity boom provided favourable financial conditions. Monetary authorities in the emerging markets considered this environment and reacted with easing which boosted the growth further. In some countries the credit expansion overheated the economy and led to internal or external imbalance. In the recent years tightening policy of the Federal Reserve and oil-price movements were in focus but they did not really affect the emerging countries as such.

Looking the empirical parts, we may also reflect to different paths that these countries went through. However it was recession in the emerging countries, as well in the advanced, as the

literature confirms, the recovery was more robust and the growth pattern reached the pre-crisis level more quickly. The growth was strong especially in the larger economies, possibly as a result of the credit expansion mentioned before. The European small economies lagged behind, though. In some countries the pre-crisis imbalance resulted in external and internal adjustment, and later the impact of Eurozone sovereign crisis also could play a significant role in the pattern. In the recent years, this region outperformed, partly as a more sustainable growth structure, partly as a result of the European easing policies which provided better environment for investment and growth compared to the other regions. The other indicators mostly confirms these findings. The CPI, here interpreted as a proxy of internal balance, showed more buoyant economic environment in the larger countries, and in the Latin American region. However this should be regarded cautiously as currency movement, hence imported inflation, Balassa-Samuelson effect and many factors could effect it at the same time. The current account figures showed serious adjustment in the case of the Central European states, and in some larger countries which could contribute to a more resilient outcome, a more sustainable growth. From the financial viewpoint the government bond yields have been presented. The decrease in yields persisted long after the crisis as a result of the favourable liquidity conditions. Interesting to note, that the long-term yield diverged in the recent years. In Europe both ECB contributed positively, both the inflation figures.

Further discussion of these circumstances is left for further research. At this point the questions regarding to the economic closeness of any major central bank, the channels of influence and the question of asymmetry are still open.

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