



# The Middle-Income Trap

Emerging Markets Forum  
2024 Global Meeting  
Washington D.C.

# Main Messages

WORLD DEVELOPMENT REPORT



1

Middle-income countries—home today to 6 billion people—are in a race against time. But they are getting stuck in middle incomes

2

To escape the “middle-income trap,” countries need to undergo two transitions, not one

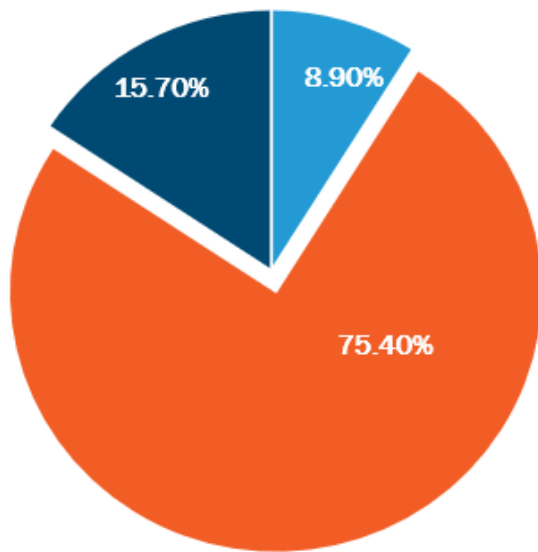
3

To escape being trapped in slower growth, countries require institutions for creative destruction. They must discipline incumbents, reward merit, and capitalize on crises

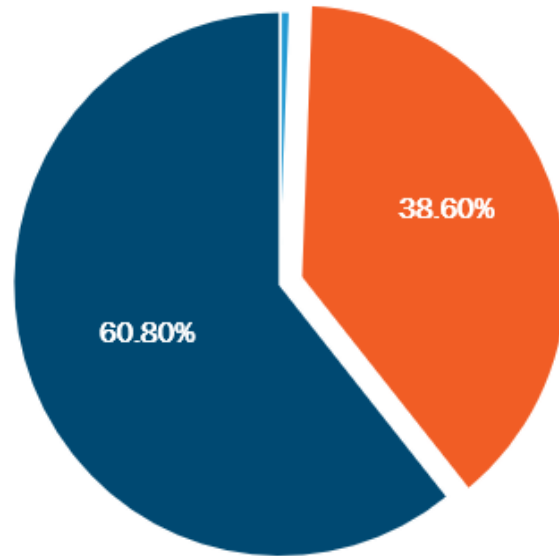
# Middle-income countries—home today to 6 billion people—are in a race against time...but they are getting stuck in middle incomes



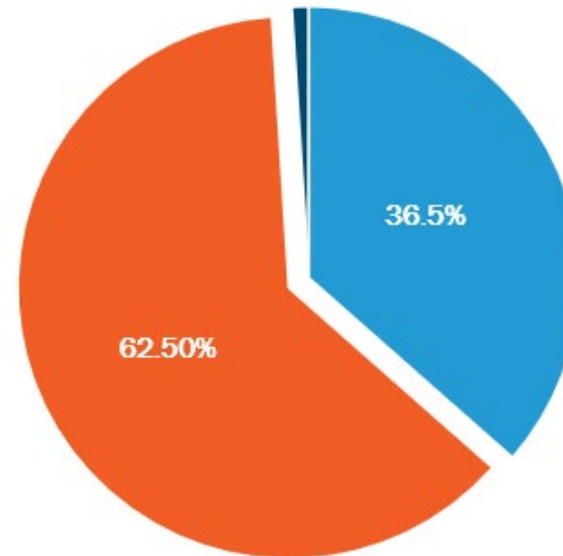
Share of



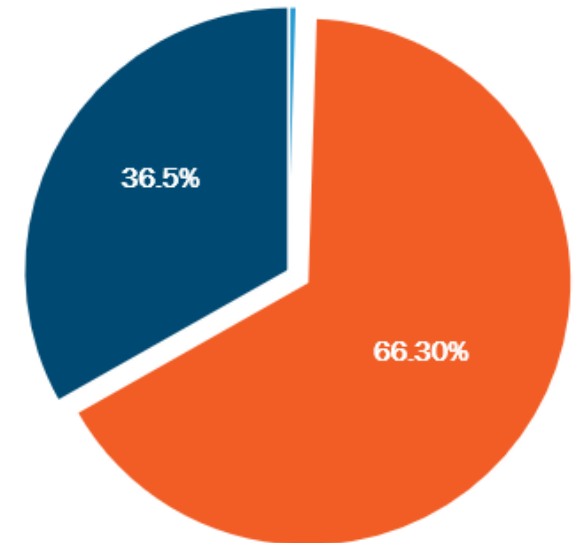
Population



GDP



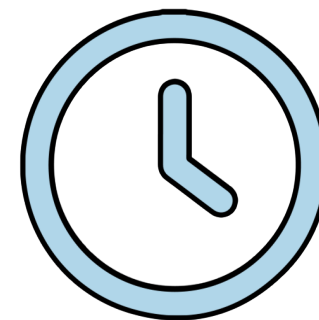
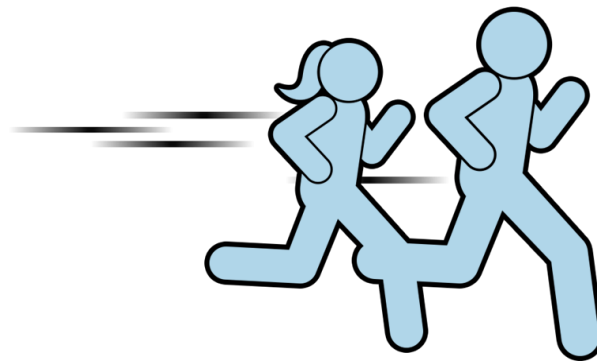
Population living in extreme poverty



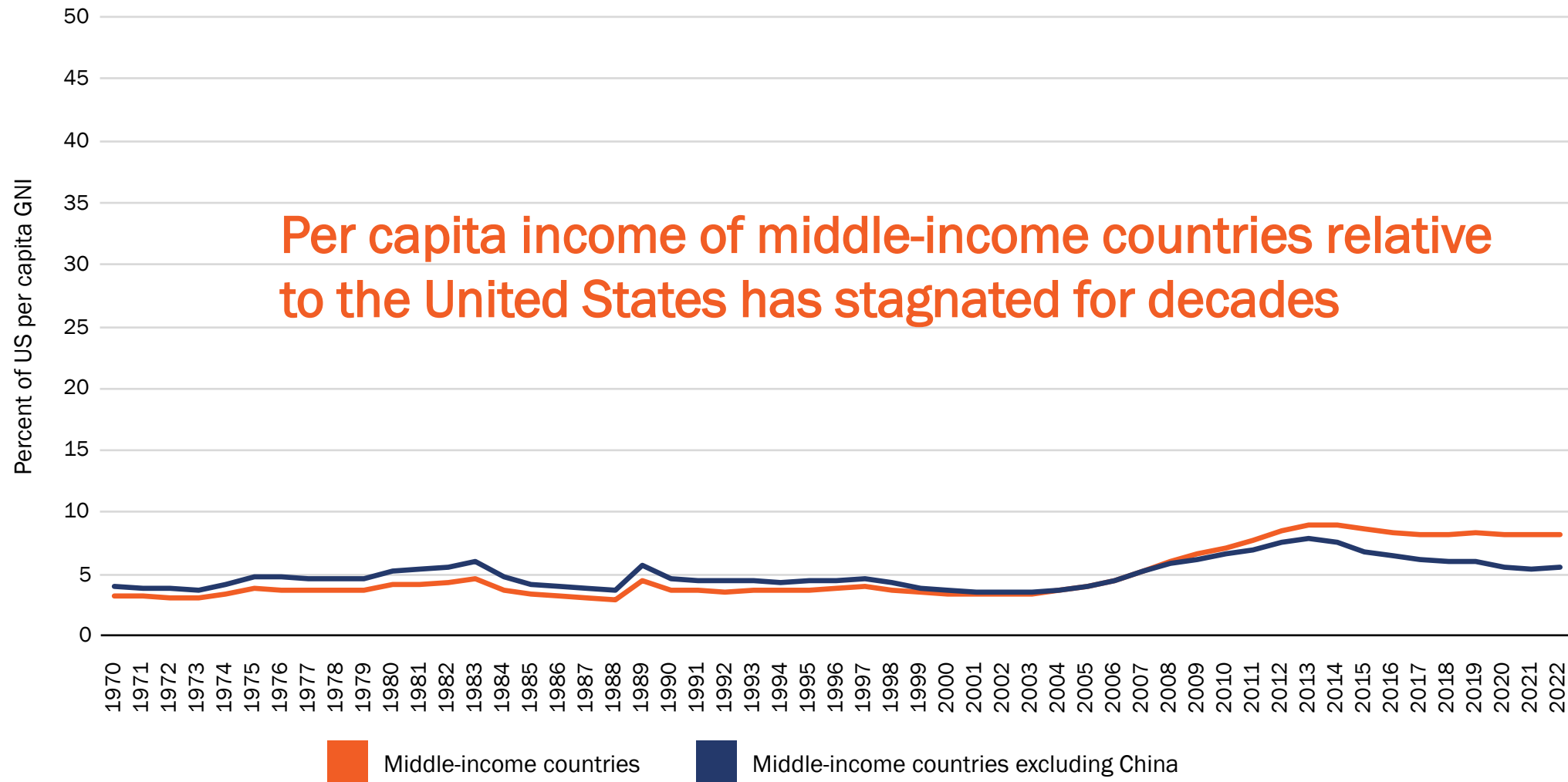
CO<sub>2</sub> Emissions



# Big plans: Middle-income countries have ambitious goals



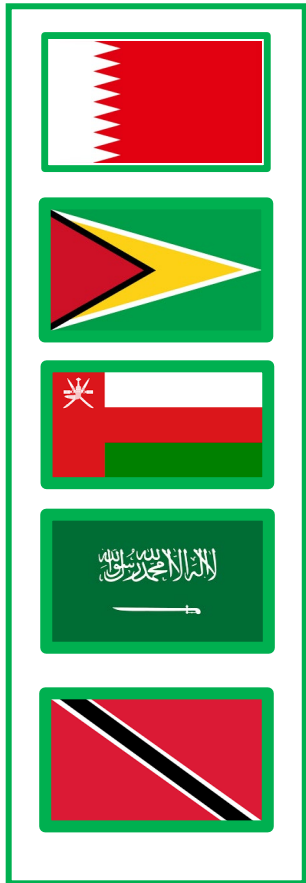
# Big problems: ...but are struggling to achieve those goals





Only 34 middle-income economies became high income in 34 years—with a combined population of 250 million

### Oil exporting



### European Union



# Three facts about middle-income economies



**1** Slowing growth

**2** Structural stasis

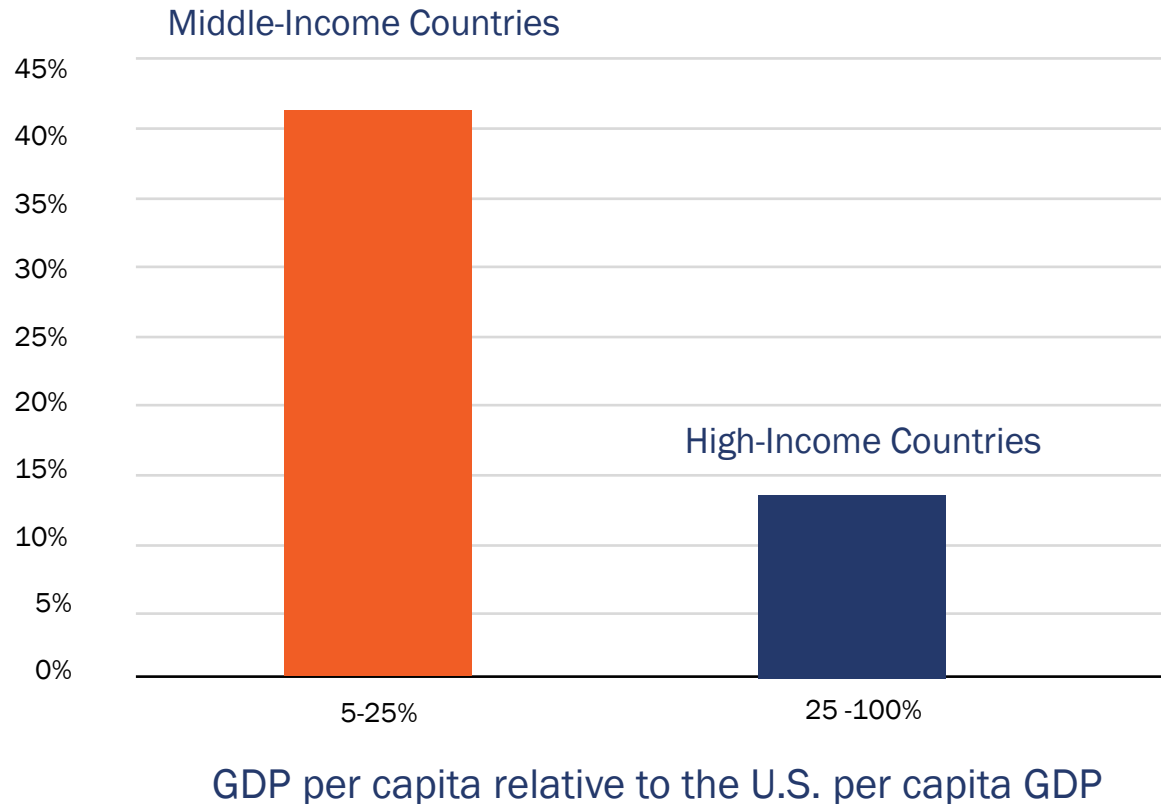
**3** Shrinking spaces

# Slowing growth

## Slowdowns are more likely in middle incomes



Likelihood of growth slowdowns



**A middle-income country is three times more likely to experience a slowdown compared to a high-income country**

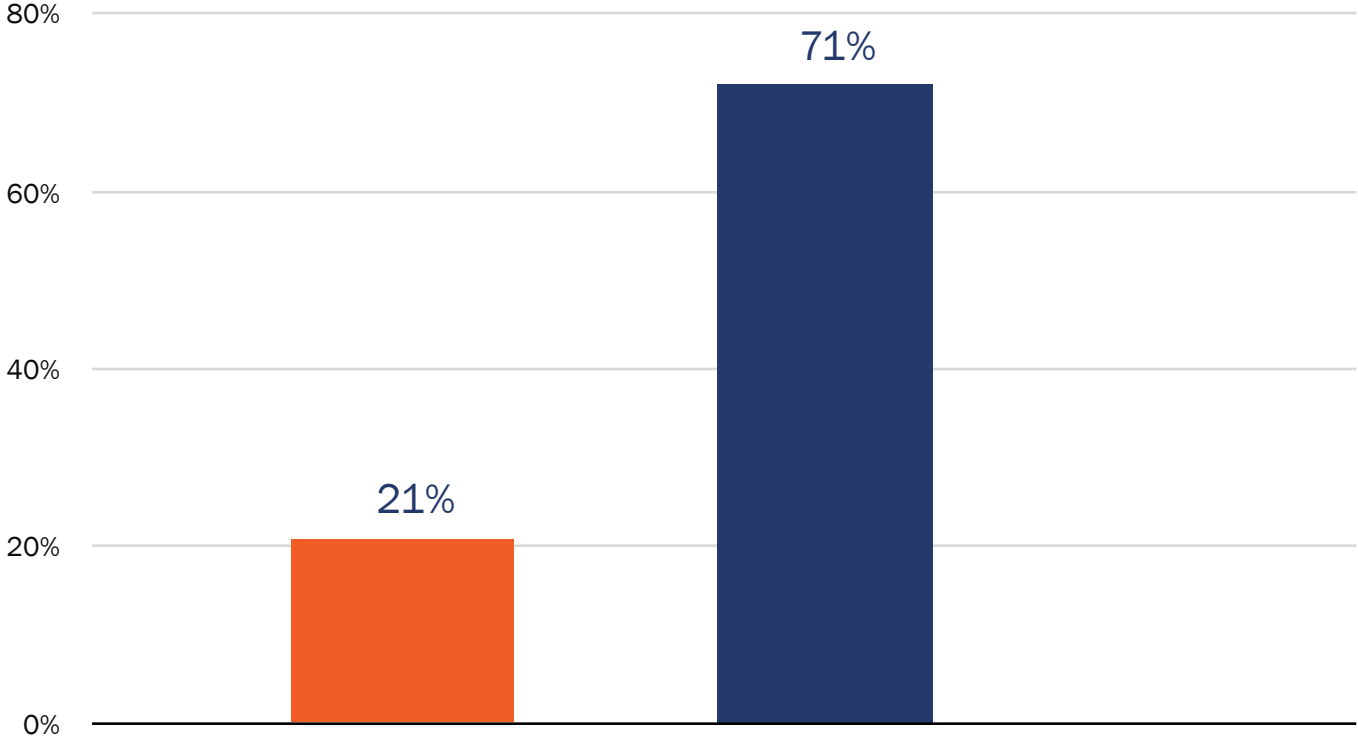


# Structural stasis

Economies become more complex as they get bigger



Middle-Income Countries



- GDP per worker relative to the US GDP per worker
- Physical capital and human capital relative to that in the United States

If capital accumulation were enough...

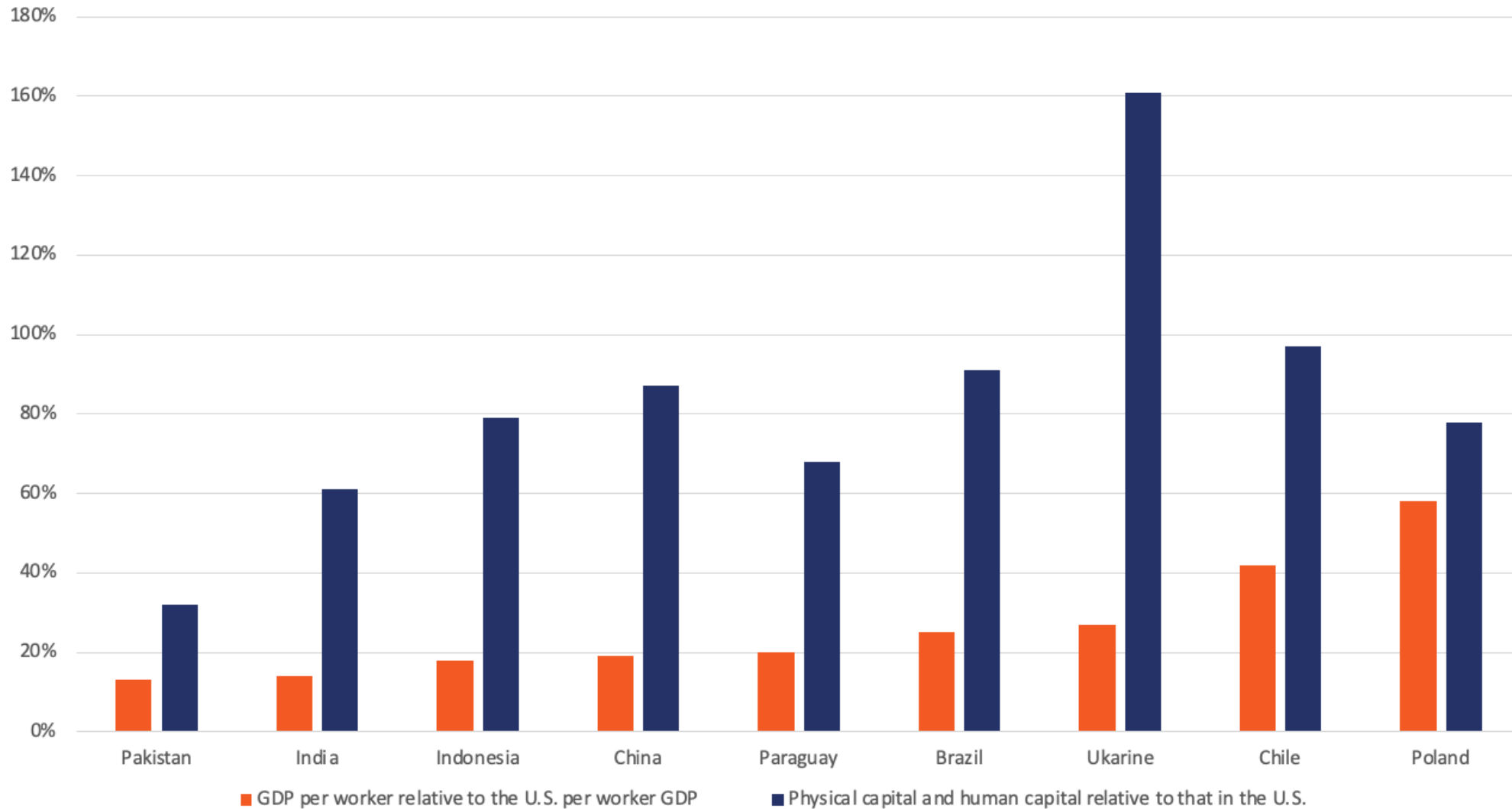
work in middle-income economies would be three-quarters as rewarding as in the US

... not just a fifth

Source: WDR 2024 team using data from the Penn World Tables 10.01.

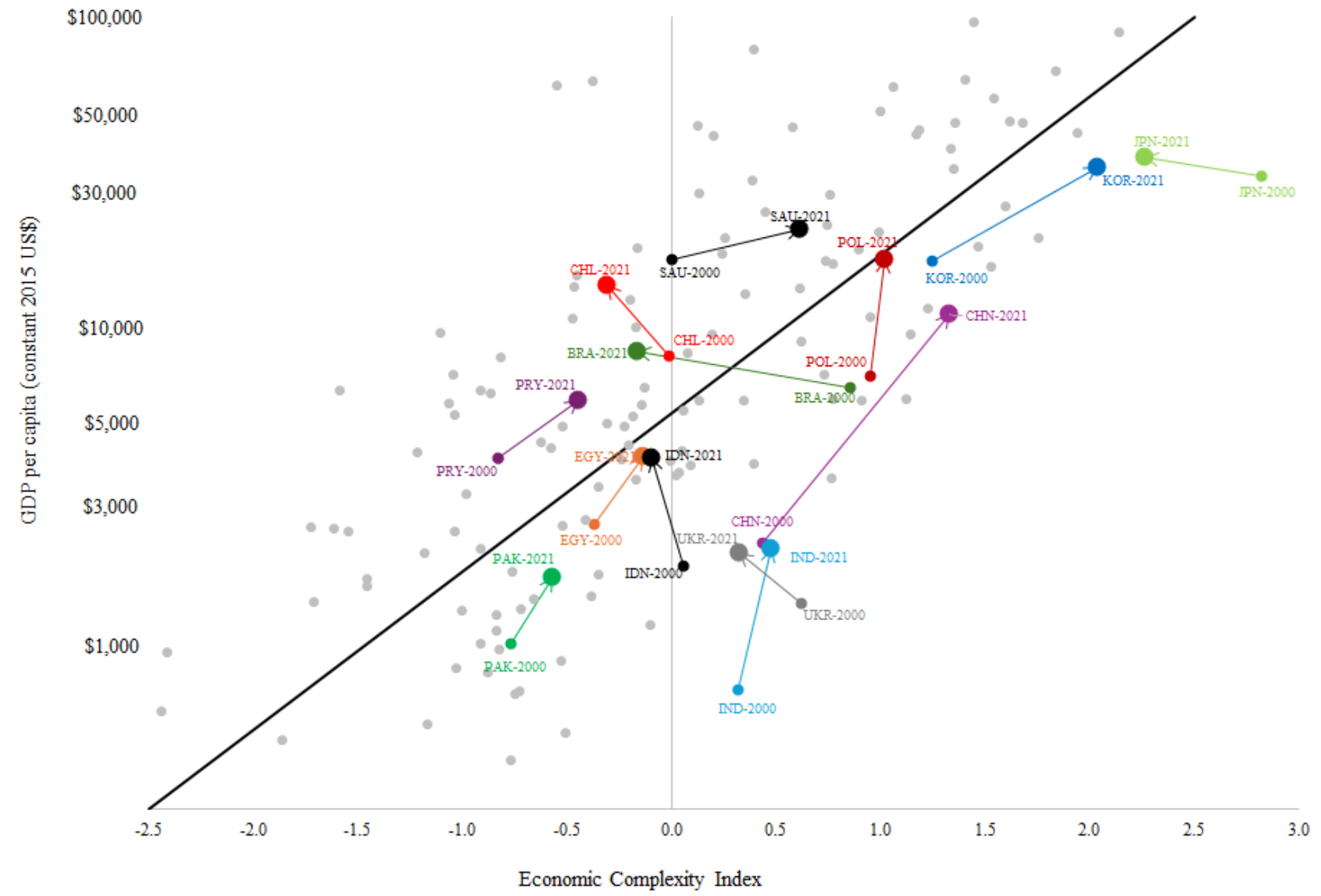
# Structural stasis

Economies become more complex as they get bigger



Source: WDR 2024 team using data from the Penn World Tables 10.01.

# To grow, middle income countries need economic sophistication

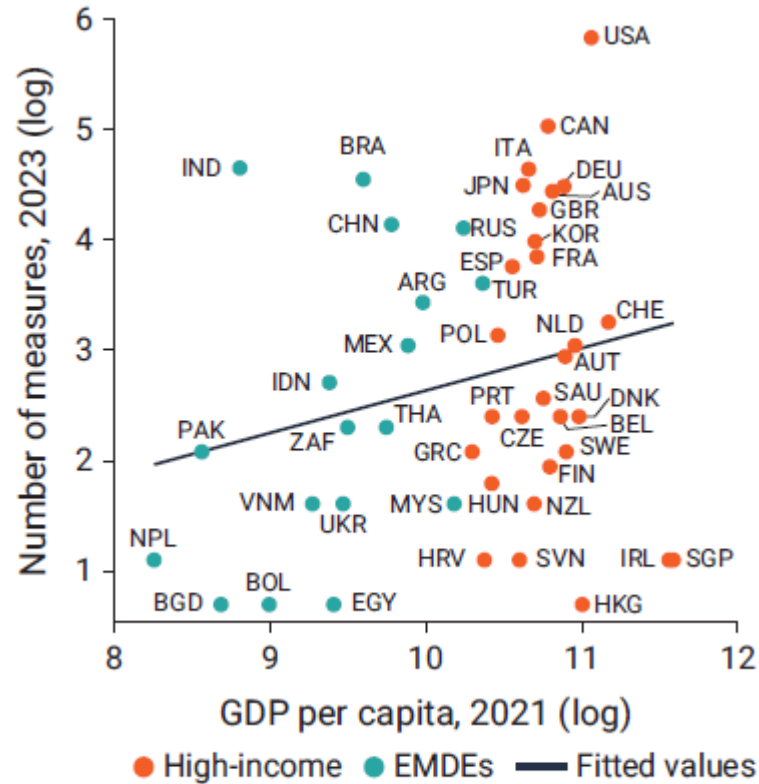


# Shrinking spaces

Today's middle-income countries face stiffer headwinds

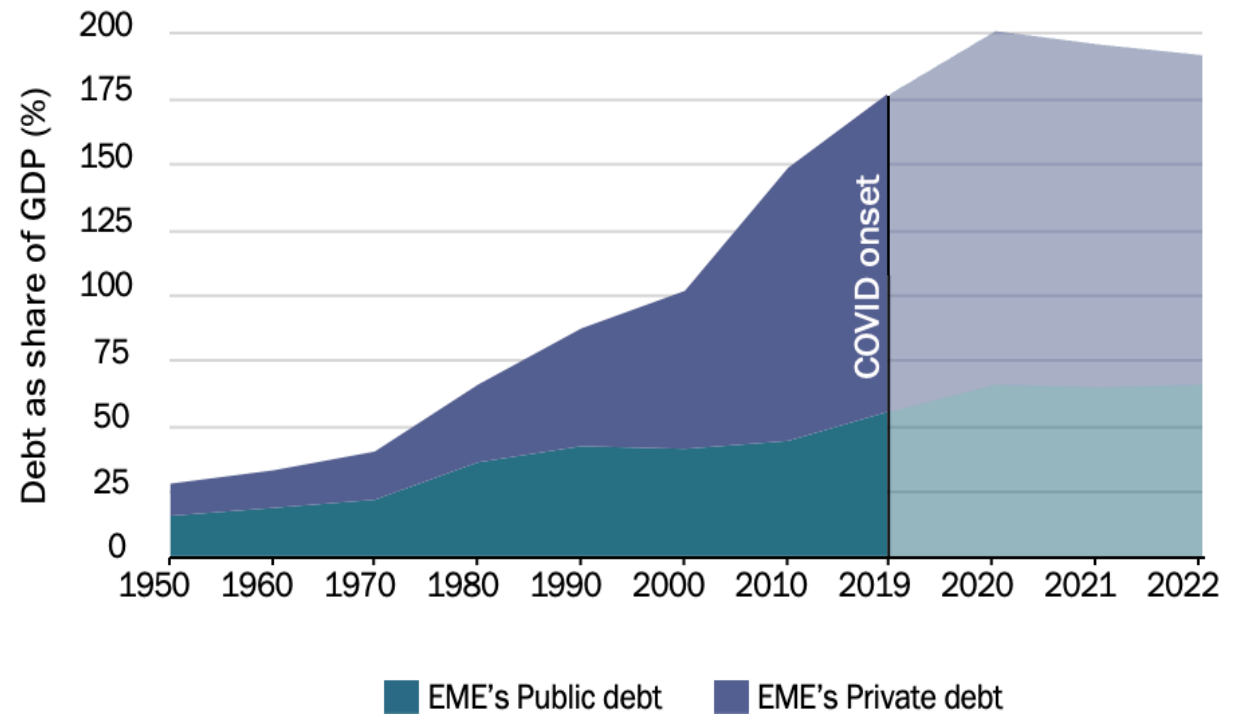


Wealthier nations implement more protectionist policies



Barattieri, Mattoo, and Taglioni 2024

Most developing economies are more severely indebted than ever



Source: WDR 2024 team using the International Monetary Fund's 2023; Global Debt Monitor data and Kose and Ohnsorge (2023).

To escape the “middle-income trap,” countries need to undergo **two transitions, not one**



**1st Transition**

**2nd Transition**



**INVESTMENT**

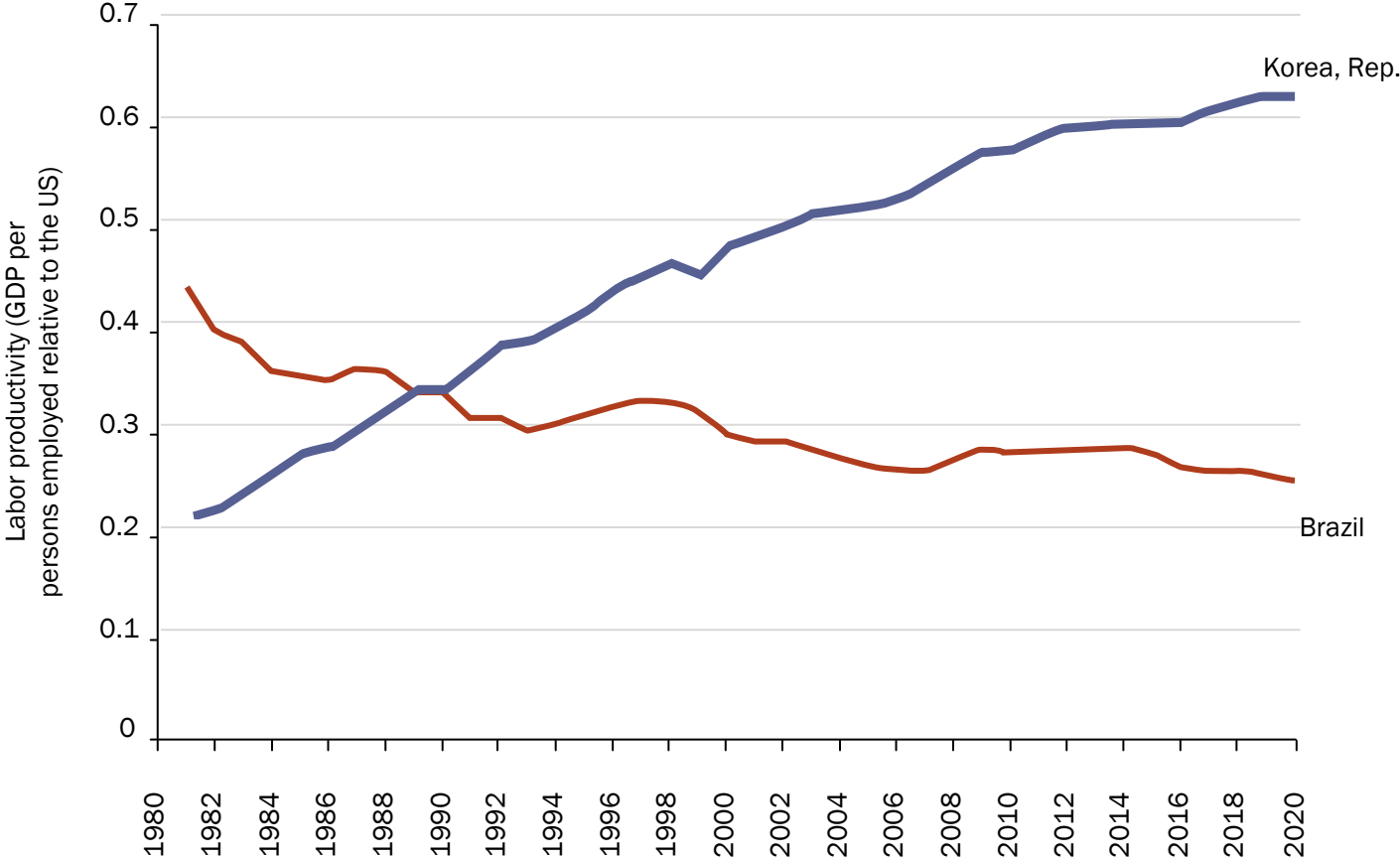


**INVESTMENT  
+ INFUSION**



**INVESTMENT  
+ INFUSION  
+ INNOVATION**

# Bypassing infusion makes it challenging to transition toward innovation

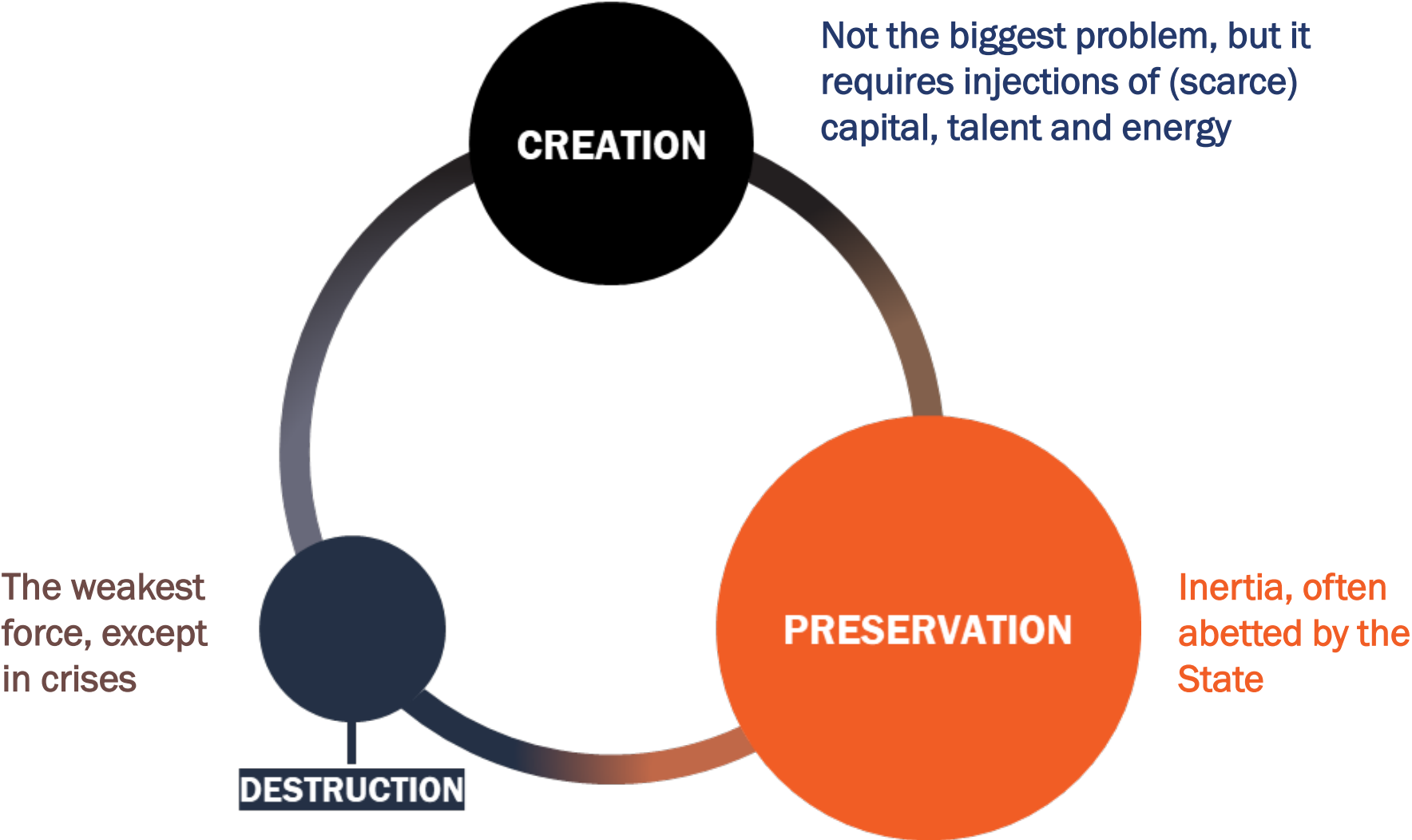


Leapfrogging prematurely into “knowledge economies” hobbles development

Source: WDR 2024 team using data from the Penn World Tables 10.01.



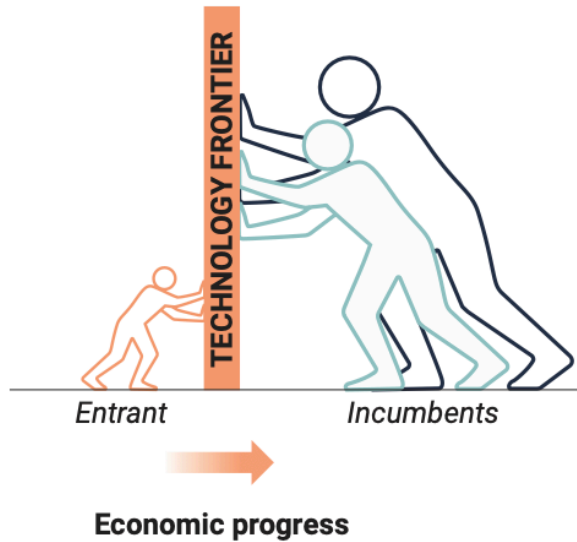
# To escape being trapped in slower growth, middle-income countries need to balance the economic forces of creation, preservation, and destruction



# Who adds value and who stiffens the status quo?

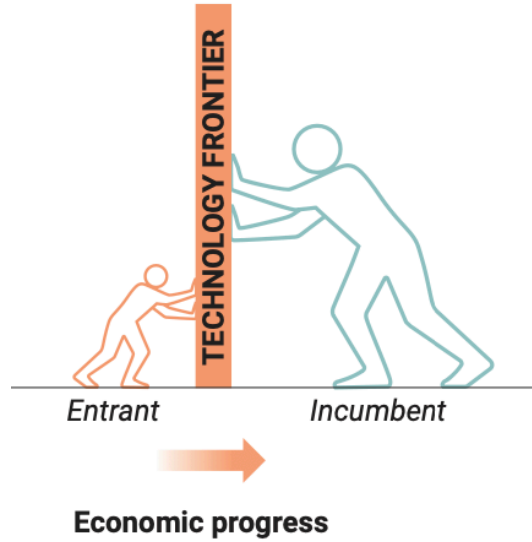


a. Energy  
(Schumpeter)



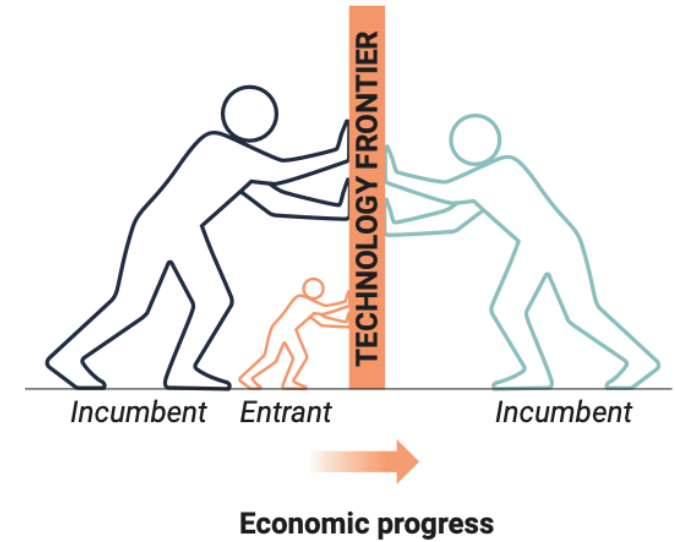
Schumpeter's view: incumbents can collude

b. Talent  
(Aghion and Howitt)



Aghion and Howitt's view: entrants create value and displace incumbents

c. Enterprise  
(Akcigit and Kerr)



Akcigit and Kerr's view: incumbents and entrants add value



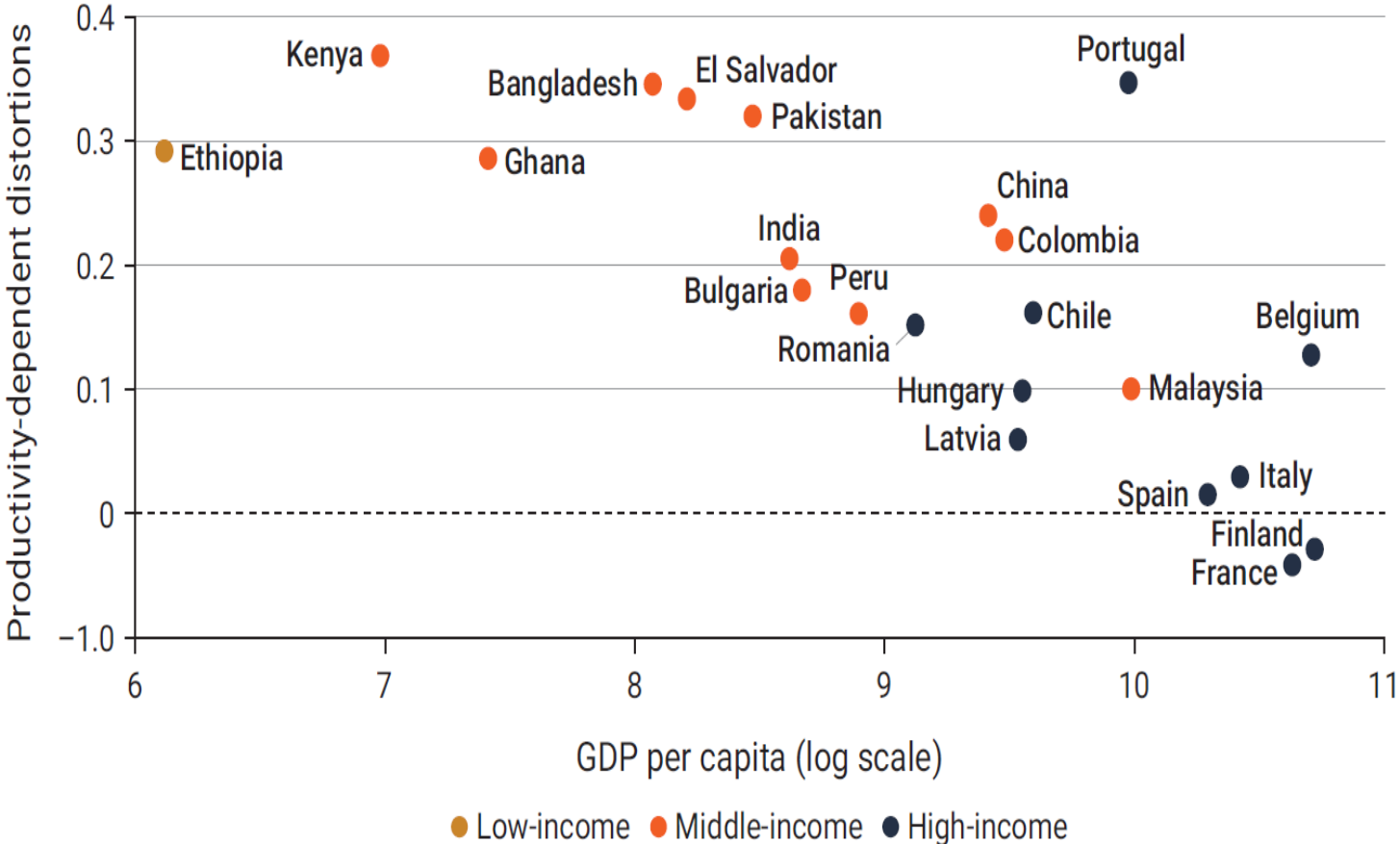
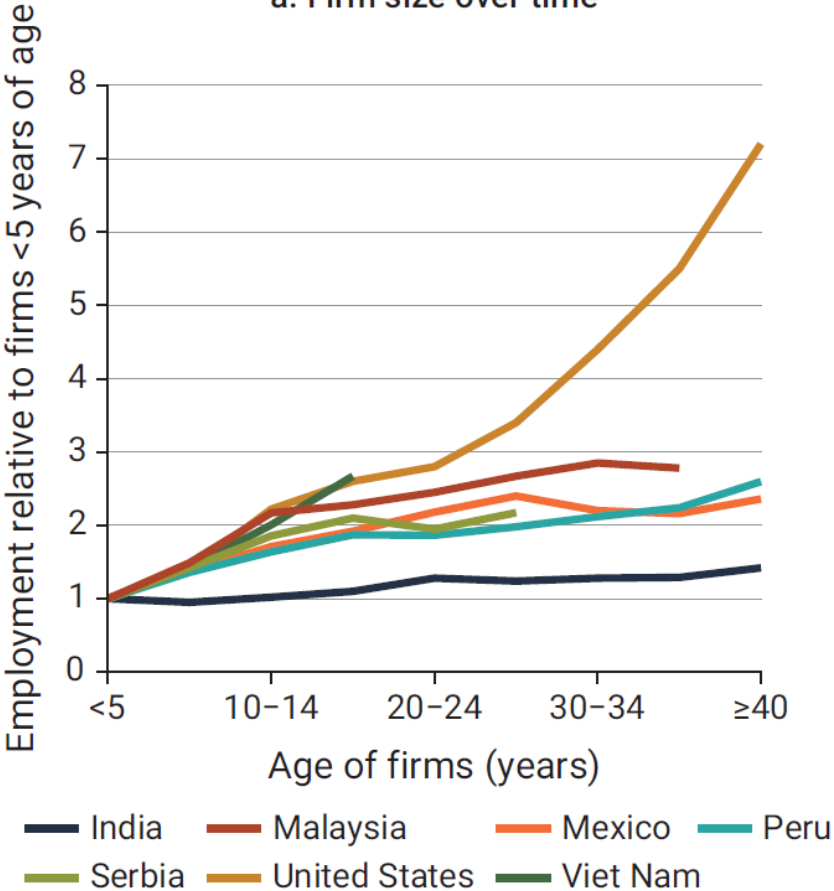
# Creation is held back by strong forces of preservation



Productive firms do not expand, and inefficient firms do not exit the market

Productive firms are held back from growing in many middle-income countries

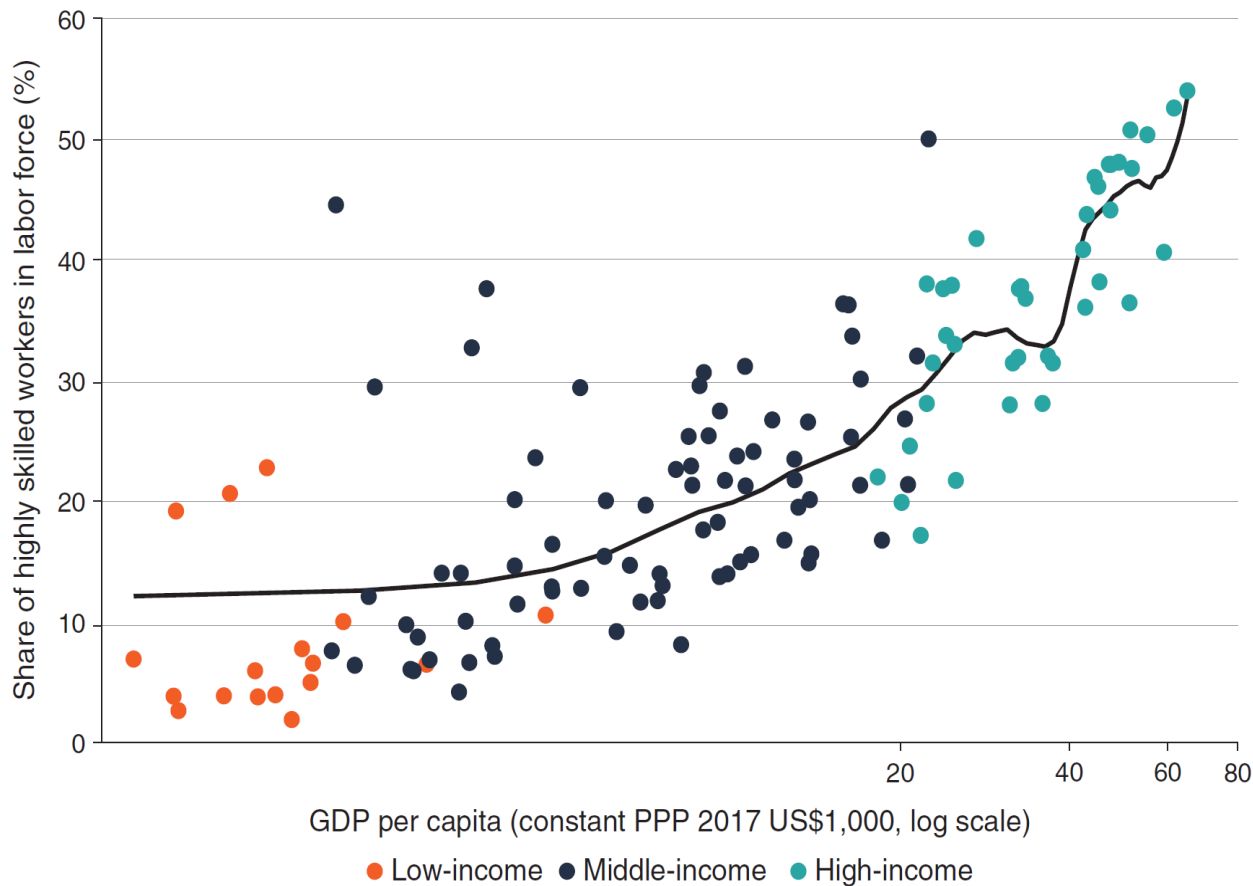
a. Firm size over time



# Creation is held back by strong forces of preservation

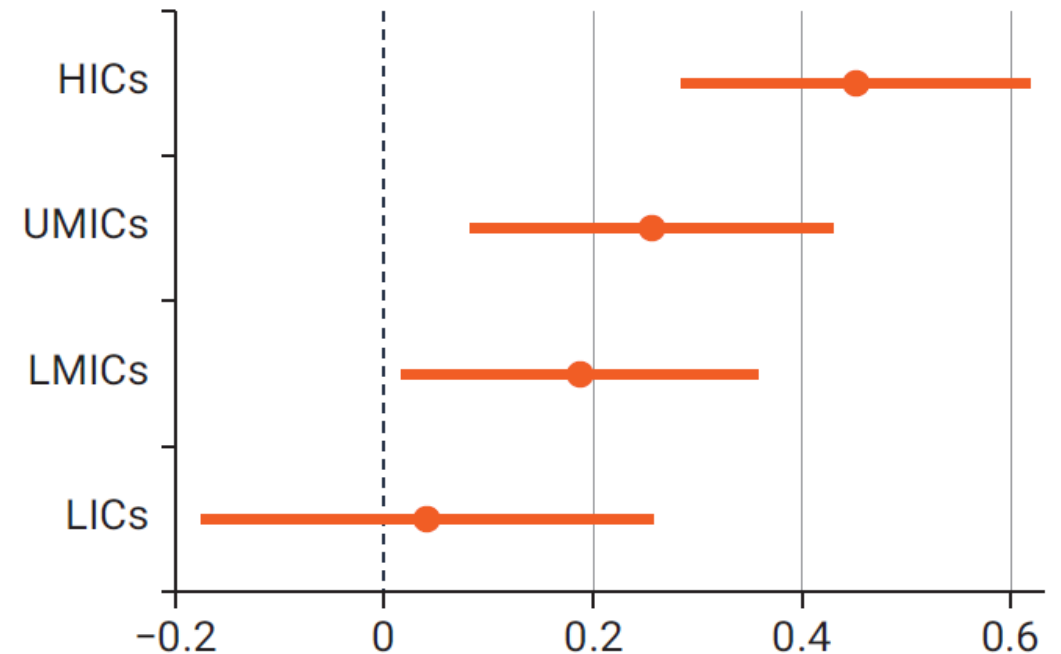


Middle-income countries need diverse skills but are hobbled by low social mobility



The importance of social mobility increases in middle-income countries

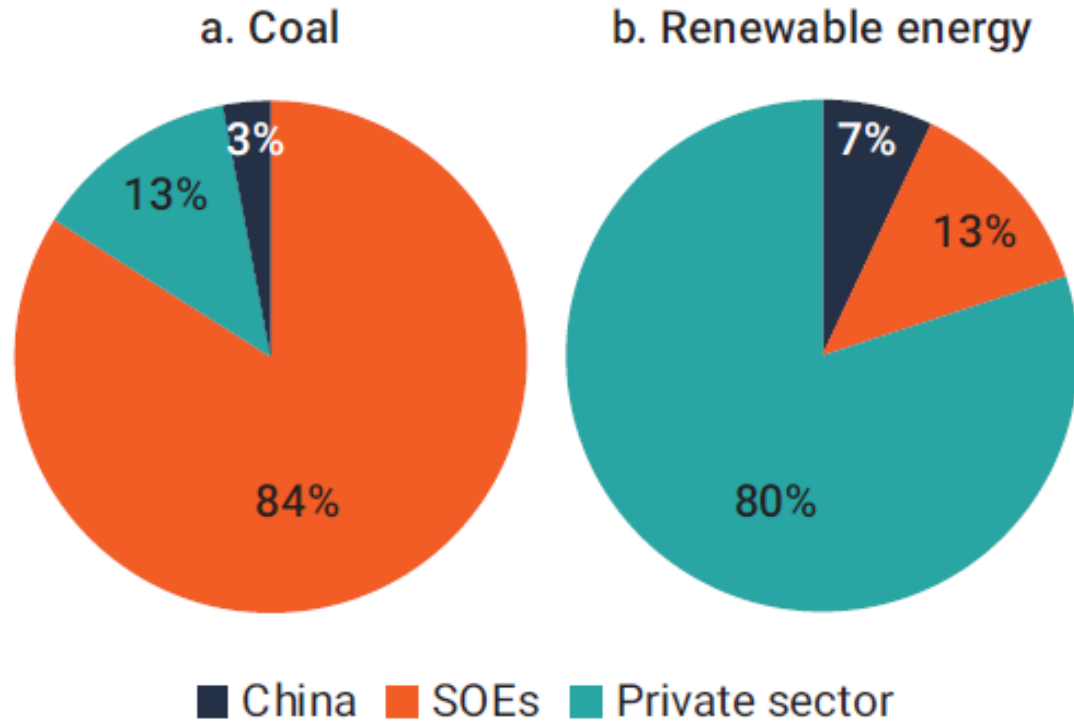
b. Intergenerational mobility matters more for skill development in middle-income countries than in low-income countries



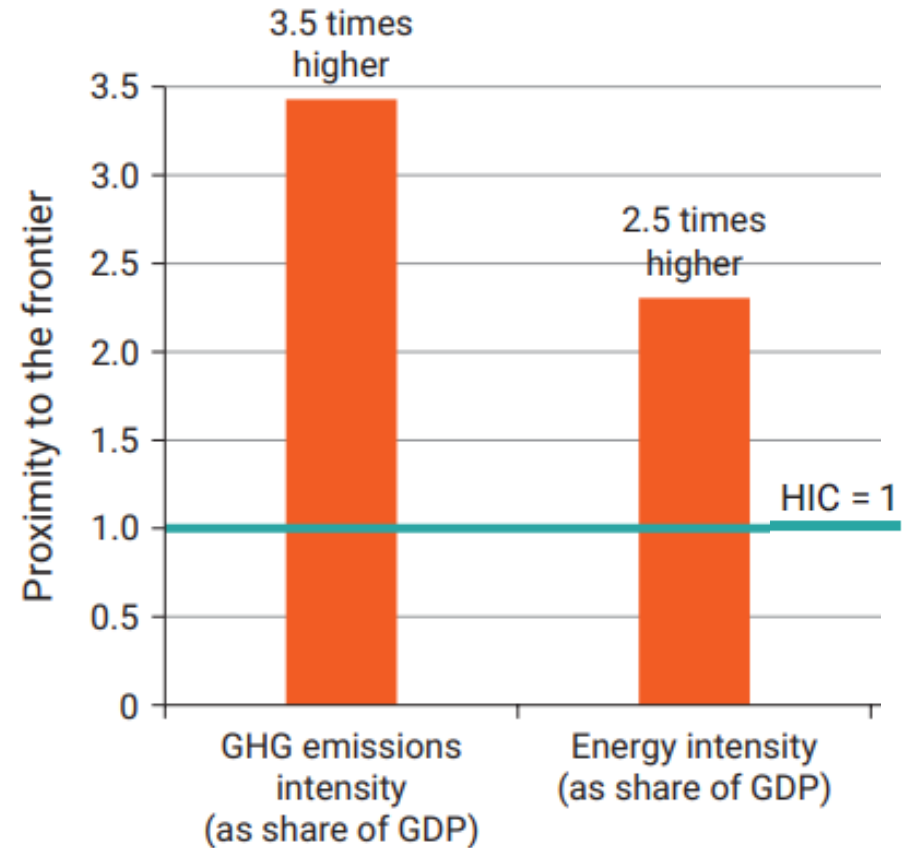
# Cheap, clean, reliable energy fuels economic growth ....but incumbents lock in the status quo



State-owned enterprises dominate coal power generation, while the private sector leads in modern renewable energy



Middle-income countries have much higher emissions and energy intensity



# Total efficiency – economic, social and ecological- requires shifts in thinking



From firm size



To value added



From inequality



To social mobility

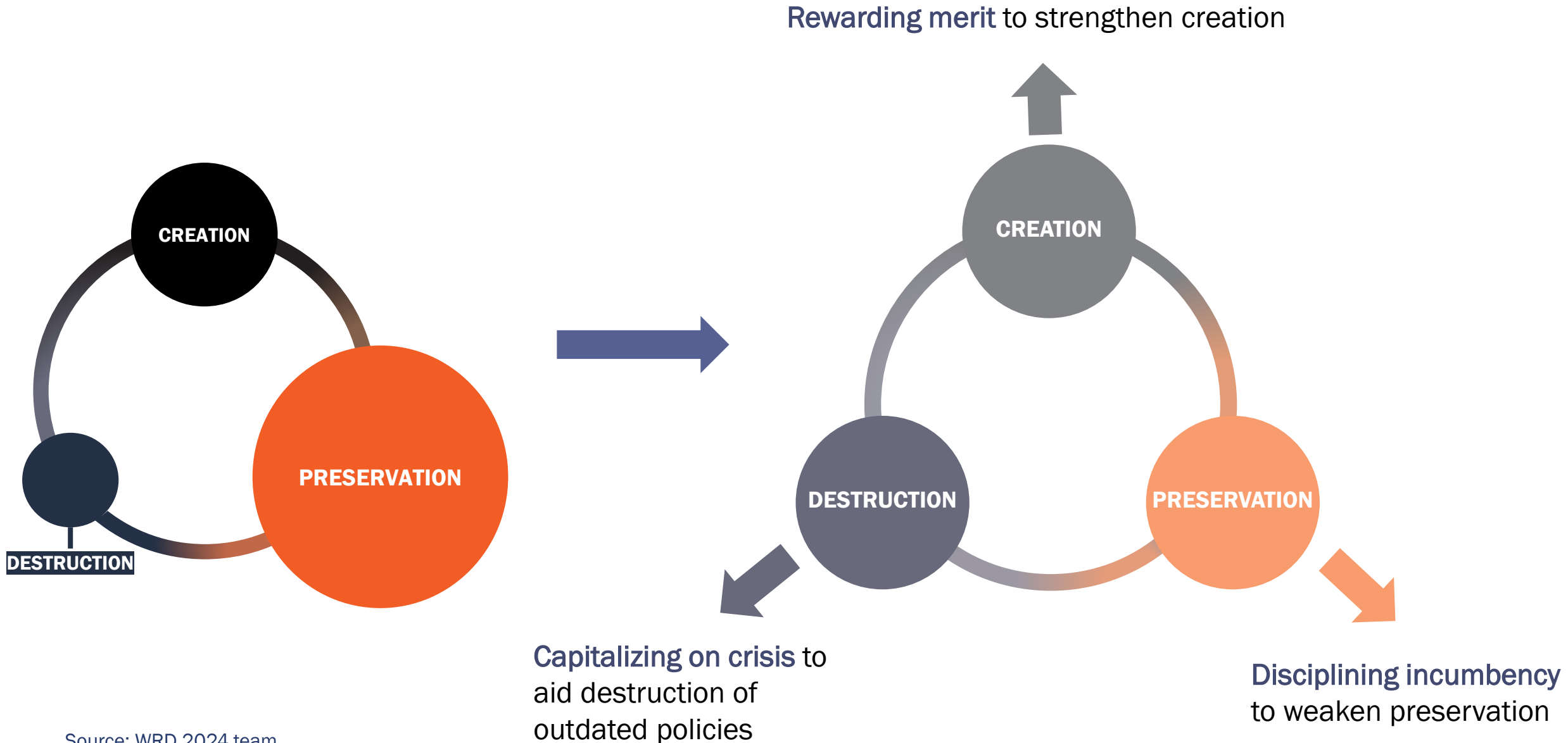


From sources of energy



To emissions intensity

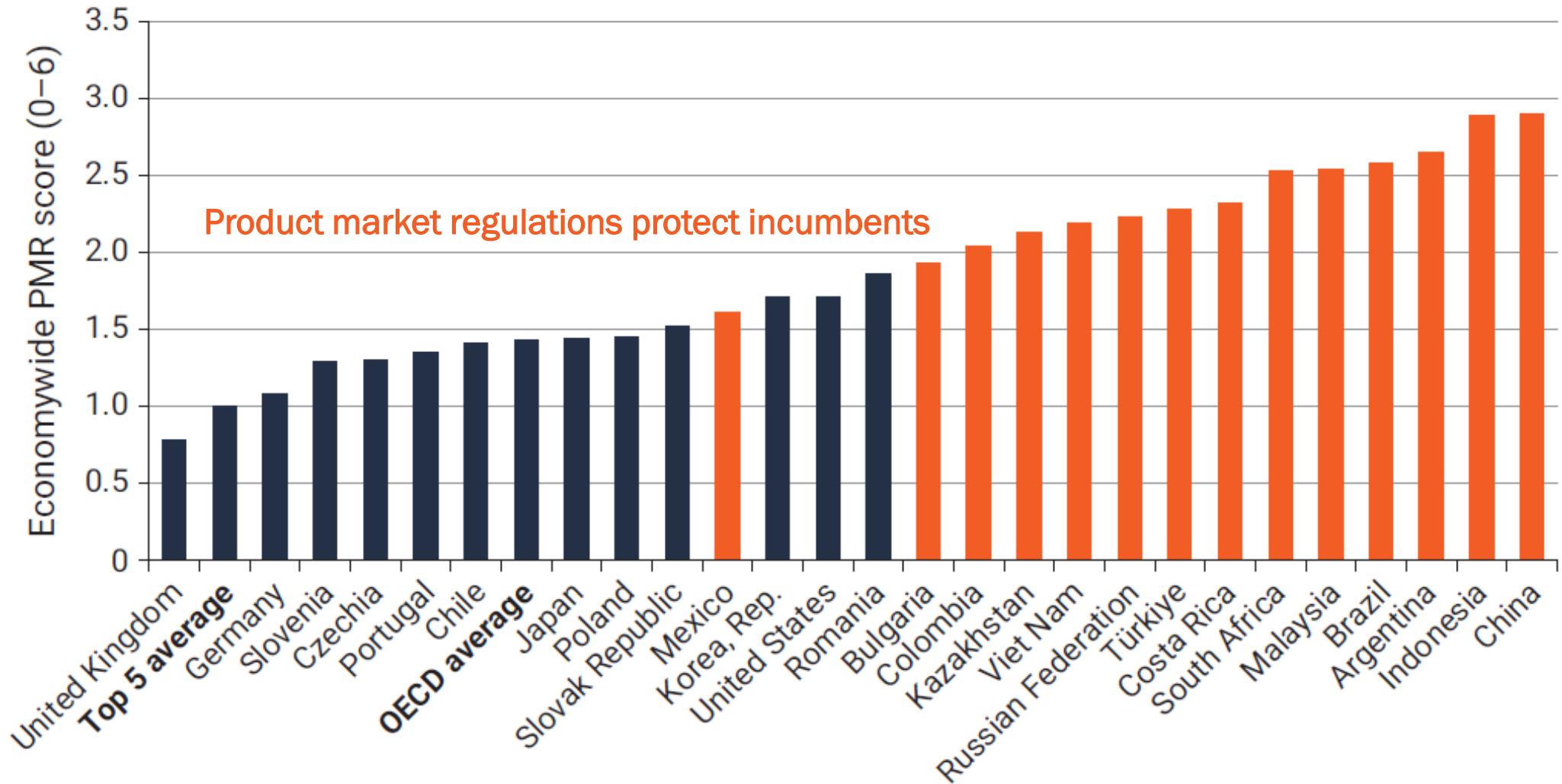
# Maintain a healthy balance between the three forces



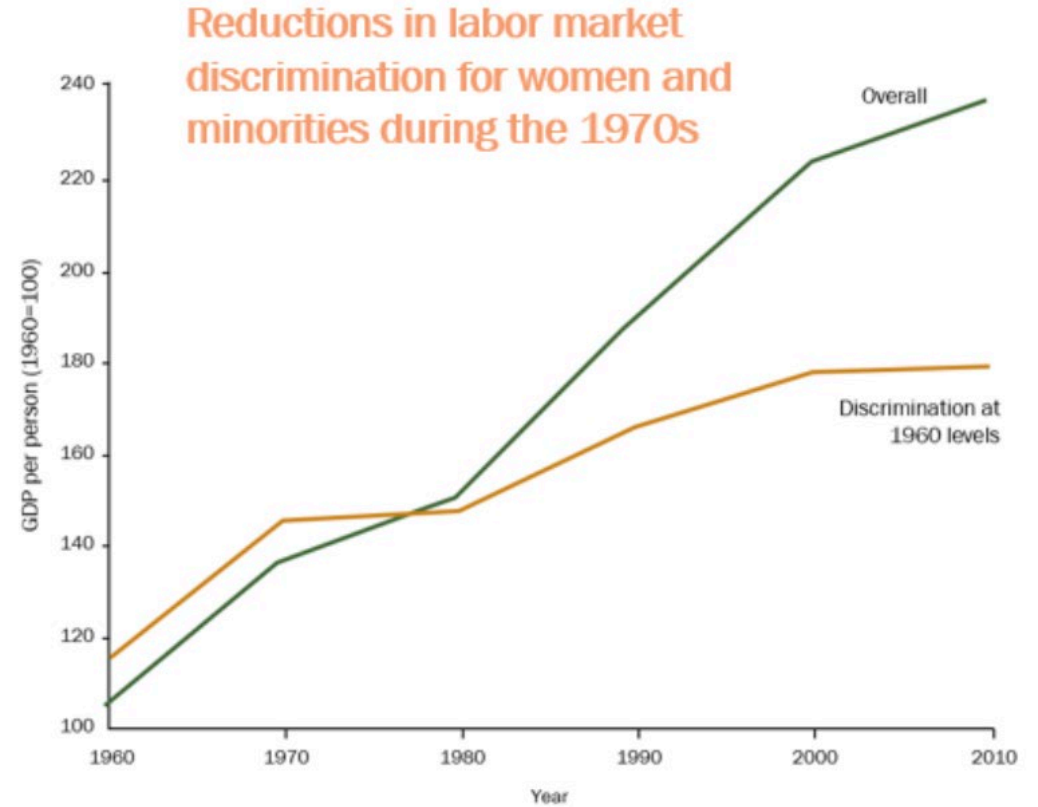
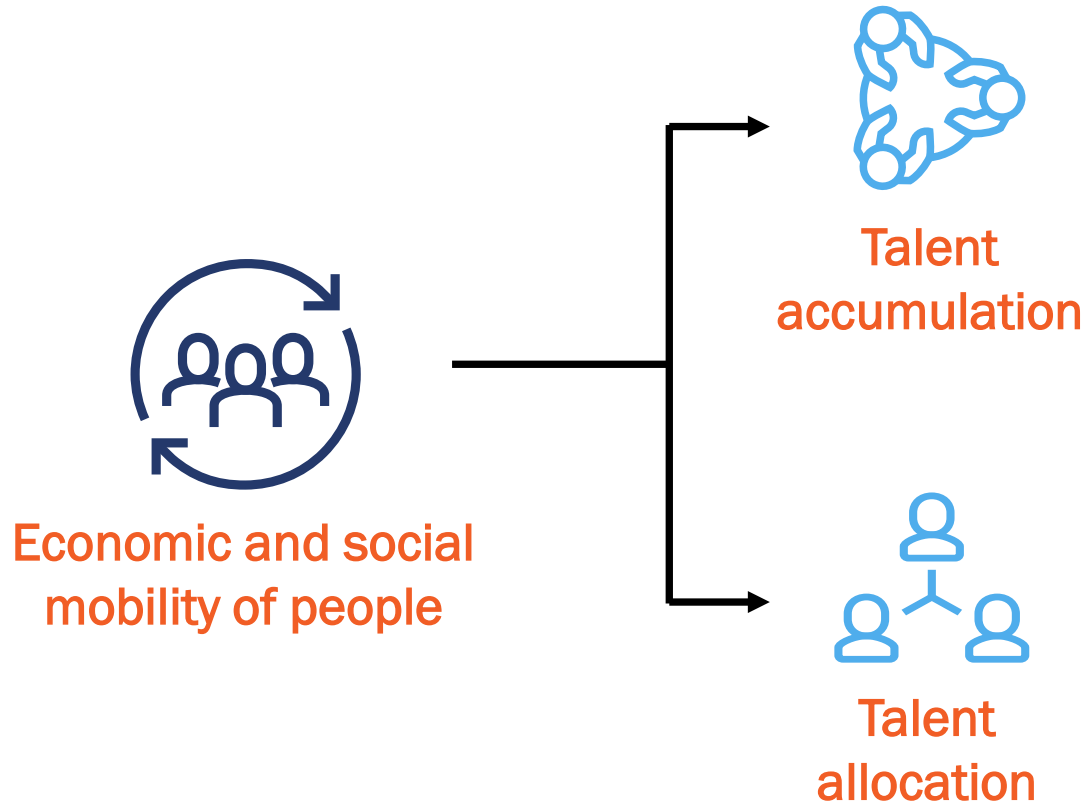
# Disciplining Incumbency



- ✓ Make markets contestable by opening up
- ✓ Reduce factor and product market over-regulation



# Rewarding Merit

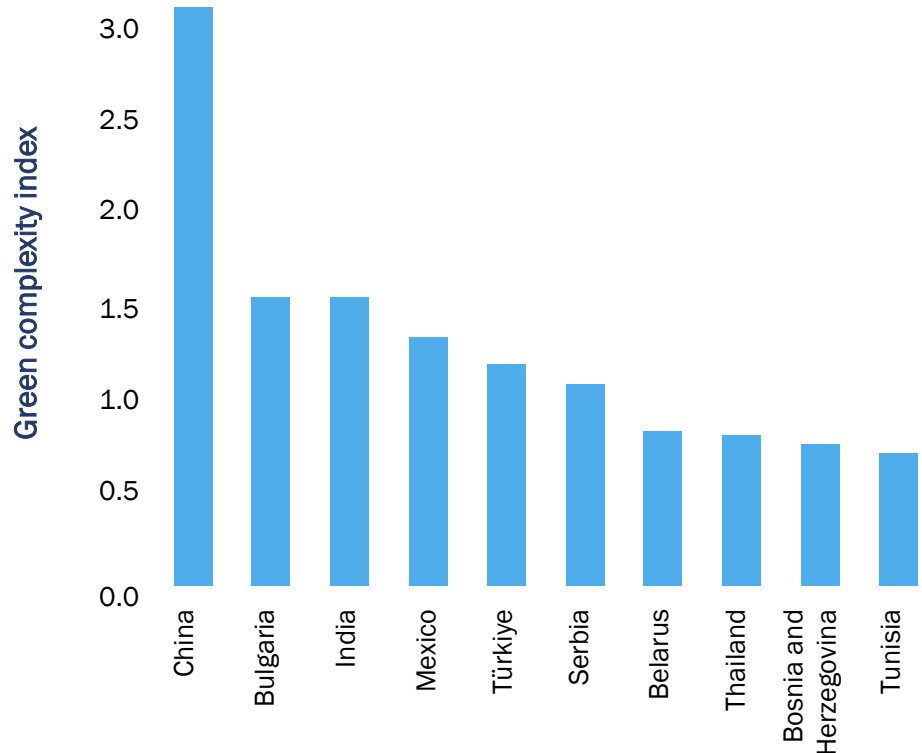


- Higher education, MICs to HICs
- - Higher education, MICs' current average
- Upper-secondary, MICs to HICs
- - Upper-secondary, MICs' current average

# Capitalizing on crises – the global energy crunch and climate change

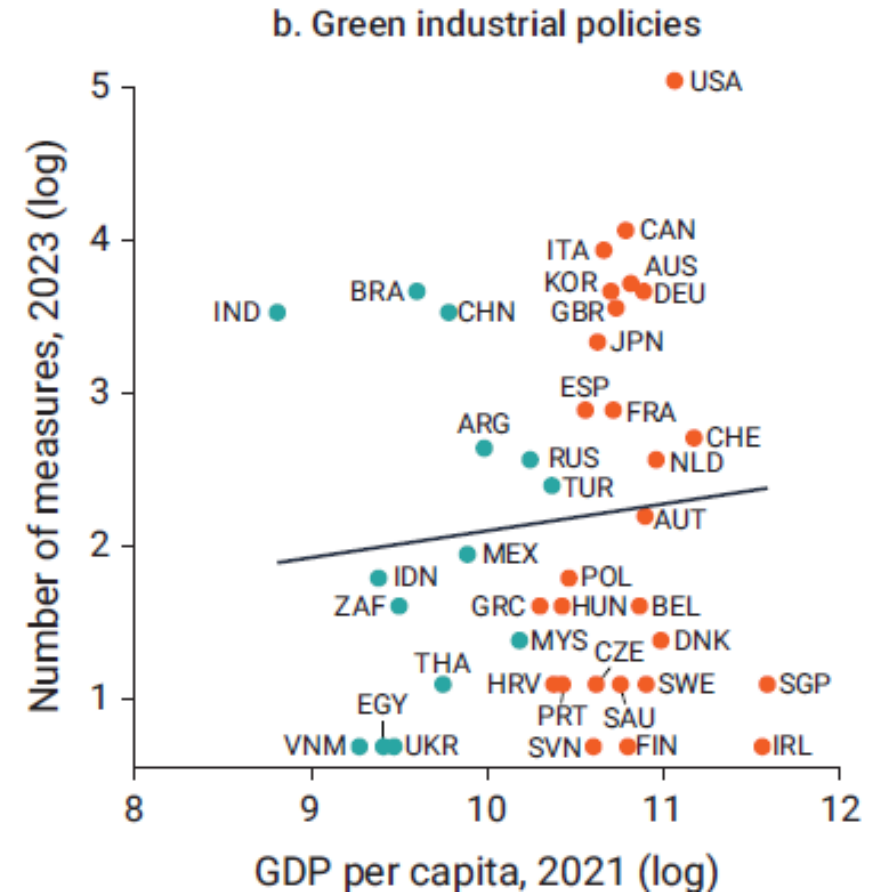


Middle-income countries can competitively export low-carbon intermediates



Source: WDR2024 team, using the Global Trade Alerts database.

The globalization of industrial policy is slowing down global decarbonization







**Making miracles**

