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World Economic Situation and Prospects 2002

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This report is a joint product of the Department of Economic and Social Affairs (DESA) and the United Nations Conference on Trade and Development (UNCTAD). It provides an overview of recent performance and short-term prospects for the world economy and of some key global economic policy developments and issues. One of its purposes is to serve as a point of reference for discussions on economic, social and related issues taking place in various United Nations entities in the first half of 2002.

The material contained in this report is based on information available as of 30 November 2001.

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The following symbols have been used in the tables throughout the report

.. **Two dots** indicate that data are not available or are not separately reported.

- **A dash** indicates that the amount is nil or negligible.
- **A hyphen (-)** indicates that the item is not applicable.
- **A minus sign (-)** indicates deficit or decrease, except as indicated.

. **A full stop (.)** is used to indicate decimals.

/ **A slash (/)** between years indicates a crop year or financial year, for example, 1990/91.

- **Use of a hyphen (-)** between years, for example, 1990-1991, signifies the full period involved, including the beginning and end years.

Reference to "dollars" ($) United States dollars, unless otherwise stated.

Annual rates of growth or change, unless otherwise stated, refer to annual compound rates.

In most cases, the growth rate forecasts for 2001 are rounded to the nearest quarter of a percentage point.

Details and percentages in tables do not necessarily add to totals, because of rounding.

The following abbreviations have been used:

ACP	African, Caribbean and Pacific (Group of) States
AGOA	Africa Growth and Opportunity Act
AIDS	acquired immunodeficiency syndrome
ASEAN	Association of Southeast Asian Nations
ATC	Agreement on Textiles and Clothing
bps	basis points
CACM	Central American Common Market
CARICOM	Caribbean Community
CEE	Central and Eastern European (countries)
CEO	Chief Executive Officer (World Bank)
CFA	Communauté financière africaine
CIS	Commonwealth of Independent States
CPC	Caspian Pipeline Consortium
CPI	consumer price index
DAC	Development Assistance Committee (of OECD)
DDO	deferred drawdown option (World Bank)
DME	developed market economy
ECB	European Central Bank
EU	European Union
FATF	Financial Action Task Force on Money Laundering
FDI	foreign direct investment
FIUs	financial intelligence units (IMF)
FSAP	Financial Sector Assessment Programs (IMF)
FTA	free trade agreement (WHO)
FTAA	Free Trade Agreement of the Americas
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNP	gross national product
GWP	gross world product
HICP	Harmonized Index of Consumer Prices
HIPC	heavily indebted poor countries
HIV	human immunodeficiency virus
IBRD	International Bank for Reconstruction and Development
ICT	information and communications technology
IDA	International Development Association
IF	Integrated Framework for Trade-related Technical Assistance to Least Developed Countries (WTO)
IIF	Institute of International Finance
IMF	International Monetary Fund
IMFC	International Monetary and Financial Committee
JETRO	Japan External Trade Organization
LDCs	least developed countries
M&As	mergers and acquisitions
mbd	million barrels per day
MERCOSUR	Southern Cone Common Market
NAFTA	North American Free Trade Agreement
Nasdaq	National Association of Securities Dealers Automated Quotations System
NATO	North Atlantic Treaty Organization
NGO	non-governmental organization
NPL	non-performing loan
ODA	official development assistance
OECD	Organisation for Economic Cooperation and Development
OPEC	Organization of the Petroleum Exporting Countries
pb	per barrel
Project LINK	international collaborative research group for econometric modelling, coordinated jointly by the Development Policy Analysis Division of the United Nations Secretariat, and the University of Toronto
PRSP	Poverty Reduction Strategy Paper (IMF and World Bank)
PSI	private sector involvement
RTAs	regional trade arrangements (WTO)
TMB	Textile Monitoring Body (WTO)
TNC	transnational corporation
TRIMS	Trade-related Investment Measures (Agreement on)
TRIPS	Trade-related Aspects of Intellectual Property Rights (Agreement on)
UNCTAD	United Nations Conference on Trade and Development
UN/DESA	Department of Economic and Social Affairs of the United Nations Secretariat
UNLDC III	Third United Nations Conference on the Least Developed Countries
WTO	World Trade Organization

CHAPTER I: GLOBAL OUTLOOK

A pervasive slowdown in the world economy, aggravated by the terrorist attacks in the United States of America, has led to the lowest growth of gross world product (GWP) in a decade. GWP grew little more than 1 per cent in 2001 and the volume of world trade stagnated (see table I.1). The weakness became more widespread as the year progressed, with three quarters of the world's economies registering lower economic growth than in the previous year. Meanwhile, more than a dozen economies, accounting for more than two-thirds of world output and including the world's three largest economies, were falling into recession.

For the year as a whole, growth in the developed countries was the lowest in a decade. The economies in transition grouping exhibited greater resilience but their average growth also declined. With the exception of the year following the Asian crisis, annual average growth in the developing countries as a group was also the lowest since the beginning of the 1990s. Output registered an absolute decline in several of these countries and output per capita fell in West Asia, East Asia and Latin America and the Caribbean when averaged for the regions as a whole. Africa was less adversely affected, with average growth changing little from the previous year. The largest developing countries—China and, to a lesser extent, India—were among those best able to sustain their growth in the face of the slowdown.

The key concern of economic policy makers at the beginning of 2002 is to ensure a prompt and widespread economic recovery. This report forecasts a gradual recovery beginning in 2002, with GWP expected to grow by only 1½ per cent and world trade by 3 per cent. Such limited growth in 2002 implies no growth in per capita world output for two consecutive years. As in 2001, countries accounting for two-fifths of the population of the developing world are expected to increase output per capita by less than 3 per cent in 2002 (see table I.2), compounding the challenge of reducing the number of people living in poverty in these countries.

The global recovery expected in 2002 depends to a large extent on the anticipated revival of the United States economy, which led the global slowdown in 2001.[1] By the end of 2001, a number of the forces that had contributed to the slowdown in the United States and in the world economy generally had improved, partially because of more accommodative monetary policy and fiscal stimulus in the major developed economies. The global consolidation in the information and communications technology (ICT) sector appeared to be ending; energy prices had fallen considerably; other primary commodity prices had softened; and world equity markets had rebounded, albeit tentatively. These developments presage a halt to the deterioration in the world economy early in 2002. The recovery is then expected to gather momentum gradually during the second half of the year (see chapter III).

The overall strength and the breadth of the economic recovery in 2002 are, however, likely to be limited. In addition, in contrast with the synchronization among economies in the slowdown, diversity is expected in the upturn. First of all, only a slow recovery of business investment is expected in the major developed economies, especially in the ICT sector. Secondly, the lingering trade imbalances within and among the major developed economies are likely to dampen their recovery. Thirdly, the frail international economic environment, including

Table I.1.
GROWTH OF WORLD OUTPUT AND TRADE, 1992-2002

Annual percentage change	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001[a]	2002[b]
World output[c]	1.7	1.4	3.1	2.7	3.2	3.5	2.3	2.9	4.0	1.3	1½
of which:											
Developed economies	1.7	0.9	2.9	2.3	2.7	3.0	2.5	2.7	3.5	0.9	¾
Economies in transition	-11.8	-6.7	-7.2	-0.6	-0.1	2.2	-0.7	3.0	6.0	4.3	3¾
Developing economies	4.8	5.1	5.6	5.0	5.7	5.4	1.6	3.5	5.8	2.3	3½
World trade[d]	5.7	4.6	10.5	8.6	5.5	9.2	3.3	5.2	11.4	0.8	3
World output growth with PPP-based weights[d]	1.9	1.8	3.8	3.5	3.9	4.1	2.6	3.4	4.6	2.2	2½

Sources: UN/DESA.

[a] Partly estimated.
[b] Forecasts.
[c] Calculated as a weighted average of individual country growth rates of gross domestic product (GDP), where weights are based on GDP in 1995 prices and exchange rates
[d] Employing an alternative scheme for weighting national growth rates of GDP, based on purchasing power parity (PPP) conversions of national currency GDP into international dollars (for explanation, see the introduction to the statistical tables in the *World Economic and Social Survey 2001*).

the slow growth of international trade, weak primary commodity prices and restrained external financing conditions, is unlikely to improve until the recovery in the developed economies is well advanced; these factors will delay the recovery of the developing countries and economies in transition.

For their part, a large number of developing countries and economies in transition are constrained in their ability to stimulate domestic demand, either because of their weak fiscal position or because of the implicit restrictions on their policy options imposed by their integration into the world economy. The room for fiscal expansion in many of these countries is limited because budget deficits are already large—either because of diminishing government revenue as a result of lower commodity prices (in many African countries) or because of continued public expenditures relating to the 1997-1998 financial crises (in several Asian and Latin American countries). Commitment to fiscal consolidation, either induced by pressures from global capital markets or required by agreements with the Bretton Woods institutions, has also precluded the use of stimulus measures in some countries. At the same time, monetary policy in many developing countries and economies in transition has been directed exclusively to target either the exchange rate or inflation, leaving little room for counter-cyclical easing. Only a small number of developing countries and economies in transition have been able to undertake monetary easing and to use fiscal stimuli simultaneously. The lack of room for policy manoeuvre will contribute to the slowness of the recovery in many developing countries and economies in transition.

The collapse in the growth of international trade, exacerbated by the disruption caused by the terrorist attacks, was a key feature of the slowdown in 2001 (see chapter II). Only a limited improvement in the growth of world trade is expected for 2002, while the tepid global recovery suggests that international commodity prices, including that of oil, will remain soft during the year.

The modest increase in net financial flows to developing countries and economies in transition in 2001 is not expected to be sustained in 2002. Total flows of foreign direct investment (FDI) to these countries had seemed relatively immune to the crises of the previous few years but fell in 2001 and are expected to drop further in 2002. Meanwhile, other private capital flows to developing countries and economies in transition remain subdued and their costs, having risen in the wake of the terrorist attacks, had not returned to their previous levels by year-end.

The lower exposure of developing countries to short-term capital flows and the adoption of more flexible exchange-rate regimes meant that external shocks through international financial channels in 2001 were smaller than in the 1997-1998 international financial crises. Nevertheless, a few countries, notably Argentina and Turkey, suffered from a combination of, and interaction between, domestic and international financial difficulties in 2001. Despite some large depreciations in 2001, there was a greater degree of stability in the exchange rates of developing countries and economies in transition than in the past few years. However, the adverse developments on both the current and capital accounts mean that a number of developing economies, notably those in Latin America highly dependent on external financing, are fac-

Table I.2.
DEVELOPING COUNTRIES: FREQUENCY OF HIGH AND LOW GROWTH OF PER CAPITA OUTPUT, 1999-2002

	Number of countries monitored	Decline in GDP per capita				Growth of GDP per capita exceeding 3 per cent			
		1999	2000	2001[a]	2002[b]	1999	2000	2001[a]	2002[b]
		Number of countries							
Developing countries	95	39	25	32	16	24	35	21	21
of which:									
Latin America	24	12	6	13	7	6	7	3	1
Africa	38	15	15	9	4	7	8	10	9
Eastern and Southern Asia	18	2	1	5	1	9	13	6	9
Western Asia	15	10	3	5	4	2	7	2	2
Memo items:									
Least developed countries	41	17	17	12	13	8	7	8	9
Sub-Saharan Africa	31	13	14	9	4	4	5	7	9
		Percentage of population							
Developing countries	95	22.5	6.5	11.2	4.2	63.0	74.3	59.3	59.7
of which:									
Latin America	24	69.1	11.8	42.9	13.9	25.2	59.7	4.9	0.2
Africa	38	46.6	28.6	19.7	10.1	19.1	16.7	23.2	20.4
Eastern and Southern Asia	18	6.7	0.2	1.7	0.0	83.4	90.6	80.6	82.7
Western Asia	15	58.1	9.1	41.2	20.1	9.9	71.3	9.9	10.0
Memo items:									
Least developed countries	41	32.8	24.9	18.1	19.7	39.2	38.0	51.0	51.6
Sub-Saharan Africa	31	43.2	38.0	29.6	13.8	13.6	9.7	28.6	33.4

Source: UN/DESA, including population estimates and projections from *World Population Prospects: The 2001 Revision* (United Nations publication, Sales No. E.01.XIII.8).
a Estimates.
b Forecasts.

ing a balance-of-payments shock that is likely to persist in 2002.

Unemployment is on the rise in the overwhelming majority of countries, with little improvement foreseen in 2002. In 2000 and early 2001, unemployment fell in most economies, reflecting not only improved economic growth after the setbacks of 1997-1998, but also structural reforms of labour markets in some cases. Nevertheless, for many developing economies in Asia, the recovery in labour markets was insufficient to reduce unemployment rates to the levels prevailing before the Asian crisis and was short-lived. Since mid-2001, the global economic deterioration has aggravated the high levels of unemployment in this region, as well as in other developing countries. In the developed economies, the improvements in unemployment rates over the past few years also began to be reversed in the second half of the year, with the unemployment rate in the United States rising from its recent historical lows and that in Japan breaking its record highs. One exception to the global trend is the Russian Federation, where unemployment fell in 2001 and real wage rates increased. In addition to the cyclical weakness in most labour markets, structural unemployment remains high in many economies.

Inflation is not an imminent global concern; to the contrary, deflation remains worrisome in a number of countries. After a mild upturn in inflation during the first half of 2001, caused by the pass-through of higher prices of energy in the previous period and increased food prices, the majority of developed countries experienced disinflation as a result of weakening global demand, falling prices of primary commodities, particularly oil, growing excess capacity in manufacturing, rising unemployment and increasing international competition. For most developing countries and economies in transition, restrictive policies were successful in controlling inflation. Relatively stable exchange rates also contributed to the non-inflationary environment; even for the few countries whose currencies depreciated, there was little pass-through to domestic prices, with the exception of Turkey. These factors are expected to sustain global disinflation in 2002. For most developed economies, inflation rates are expected to fall below 2 per cent and many developing countries and economies in transition are expected to achieve a further decline in inflation. In a small but increasing number of economies, notably Japan and a few Asian countries, fighting deflation has become the challenge.

The outlook for 2002 encompasses unusual caveats, particularly in terms of international political or military developments regarding terrorism. On the economic front, the high dependency of the global economy on the recovery of the United States involves risks because of the country's persisting imbalances. For example, equity prices, although somewhat lower, are still above traditional benchmarks; household saving rates are still at an extremely low level; and private sector debt is at historical highs. Internationally, the country's external deficits have diminished somewhat but remain large and the risks of an abrupt adjustment in the trade imbalances among major economies and of a sudden fall in the value of the dollar remain.

There are also downside risks in other economies. The deep recession and the protracted financial difficulties in Japan, the world's second largest economy, create downside risks not only for Japan itself, but also for many Asian developing economies and for the global financial system. The depreciation of the Japanese currency at the end of 2001 has also placed pressure on other currencies in Asia and will create difficulties for their export sectors. Elsewhere, the debt crisis in Argentina had limited financial contagion effects for other developing countries in 2001, but the country's continued recession and the lack of a resolution to the crisis was giving rise to a large amount of uncertainty in financial markets and was having adverse effects on other countries in the region at the end of 2001.

SOME KEY ISSUES ON THE INTERNATIONAL POLICY AGENDA

Developments in 2001 underlined once again the high degree of interdependence between developed and developing countries. The global economic slowdown has become deeper and more widespread than anticipated and has fully enveloped the developing countries, adding to the difficulties that remained from the disruptions of the late 1990s. For the developing countries and economies in transition, global linkages have amplified the impact of the vicissitudes in world economic growth in the past few years. Moreover, the impact has often been asymmetric, with most developing countries tending to benefit less than the leading developed economies in the upturns but suffering equally, or more so, in the downturns. A continuation of this pattern of growth threatens the attainment of the Millennium Development Goals, notably the target of reducing the number of poor by half by 2015.

These developments suggest that the current challenges for policy makers worldwide are not only to extricate the global economy from the current slowdown, but also to seek more balanced and stable global growth in the longer run. Maintaining accommodative macroeconomic policies, particularly in major developed economies, is crucial for securing the recovery. However, it is equally important to also sustain the longer-term agenda that seeks to ensure that developing countries and economies in transition can participate more effectively in the globalized world economy and become less vulnerable to its periodic gyrations. This requires both continued reform in the developing countries and economies in transition themselves and strengthened international economic cooperation. In 2001, there was increasing recognition of the need for further reforms in the international trade and financial systems and for an increase in financial transfers to poor countries. The following are some of the areas where progress needs to be consolidated and carried forward in 2002 and subsequent years.

International Conference on Financing for Development

It is widely accepted that the attainment of the Millennium Development Goals will require additional resources, new approaches and a new partnership among all development stakeholders. The overall objective of the International Conference on Financing for Development, to be held in Monterrey, Mexico, in March 2002, is to identify the common ground on these issues, in particular to promote innovative thinking and initiate consideration of new proposals for financing for development. One broad goal is to agree on a number of national policies and institutional changes that will improve the mobilization of domestic resources for development within developing countries. A necessary complement will be to agree on the policies and institutions necessary to mobilize additional private and public international resources to support developing countries in their development efforts. In addition, the Conference will consider issues related to the international financial architecture, global economic governance and the role of the United Nations and the United Nations system in ensuring general policy coherence and coordination.

Within this agenda, some of the specific issues to be considered include facilitating access to financial services by low-income people, particularly women, in developing countries; building investor confidence in direct and portfolio investment in emerging economies; boosting support for development as a guideline in international trade policy negotiations; significantly raising the volume and efficiency of official development assistance; helping to devise mechanisms to address external debt crises; enhancing international cooperation to combat corruption; addressing various multinational tax matters, including reducing evasion; and raising the participation of developing countries and other relevant stakeholders in the consensus building needed for coherent and consistent international policy on financing for development.

Strengthening the Heavily Indebted Poor Countries (HIPC) Initiative

Despite the progress to date, challenges to expeditiously complete the HIPC Initiative remain. One is to ensure that eligible countries reach the completion point as expeditiously as possible. A second is to help more countries, especially those emerging from conflict situations, to qualify for relief under the Initiative. Another is to ensure sufficient flexibility in the programme so as to assist countries whose debt situation is worsened by shocks, such as natural disasters or a fall in the prices of commodity exports. A fourth is that the low level of funding of the HIPC Trust Fund could impede debt relief: as of November 2001, paid-in contributions totalled only 41 per cent of the pledged amount. Additional efforts are required to mobilize the resources necessary to implement the Initiative fully.

Rethinking the role of private creditors in debt crises

Since the 1997-1998 international financial crises, there has been growing consensus among Governments on the need to improve arrangements for “private sector involvement” (PSI) in the prevention and resolution of such crises. This led to an agreement at the 2000 IMF-World Bank Annual Meetings on a voluntary and non-binding framework that employs a case-by-case approach, based on an assessment of each country’s balance-of-payments situation and prospects for regaining access to international capital markets. The basic principles of the framework are that the use of official financing in resolving crises should be limited and that private investors and creditors should bear the consequences of their decisions.

The application of the framework has brought mixed results thus far.[2] The major lesson after a number of cases is that the present arrangements do not guarantee an orderly and timely solution to debt crises. No accepted mechanism has emerged to treat the sovereign debt of middle-income countries that cannot pay. The lack of a legal infrastructure for changing debt-servicing obligations encourages debtors to postpone necessary restructuring for as long as possible in the hope that their payment capacity will recover. At the same time, uncertainty about how the 2000 framework would be applied has contributed to the widening withdrawal of private creditors from emerging markets.

In the face of the debt crises in Turkey and then in Argentina, there is now increasing support for a systematic, rule-based approach, rather than the present ad hoc arrangements. There is a growing appreciation that an arrangement akin to an international bankruptcy procedure could establish a clear set of rules for how sovereign borrowers with debt problems should negotiate with creditors over debt rescheduling. This would reduce uncertainty and this, in turn, could enhance the sustainability of capital flows to emerging markets.

While many proposals have been made, no specific plan is widely accepted. The First Deputy Managing Director of the International Monetary Fund made a proposal in November 2001.[3] According to this proposal, a Government would be allowed to come to the IMF and request a temporary standstill on the servicing of its debts while it negotiated a rescheduling or restructuring with its creditors. If the Fund agreed, the country would be granted protection from those creditors for a limited period of time in exchange for entering into negotiations with its creditors, while adopting sound economic policies. During this period, it could impose capital controls to stem capital flight. Unlike the present framework, the proposal would create a mandatory process for restructuring. It has been argued that the very existence of the opportunity to invoke this process would create incentives for a debtor and its creditors to reach timely agreement on their own accord without the participation of the official sector.

Other proposals have been made by official authorities, non-governmental organizations, academics and private sector financial professionals. The formulation of policy is thus at an early conceptual stage, with various proposals being critiqued and sharpened. However, the imperative to work on this issue at the international policy level has been recognized and the need is to arrive at a consensus around a workable solution as soon as possible.

Implementing the Doha work programme

International trade can make an important contribution to economic growth and development but many developing countries have confronted difficulties in taking advantage of the opportunities that international trade can offer. Many developing-country concerns regarding the international trading system that were raised in the Third WTO Ministerial Meeting in Seattle and reaffirmed in the Plan of Action adopted by UNCTAD X in Bangkok in February 2000 are included in the new WTO agenda, providing an opportunity to improve developing countries' effective participation in international trade (see chapter II). However, the outcomes of the Doha Meeting constitute only the starting point of a negotiation process and the numerous provisions that reflect the concerns of the developing countries will have to be given substance in the agreed negotiations and other elements of the WTO work programme. Many developing countries will need assistance to engage in these negotiations meaningfully, as well as to implement the agreed conclusions.

Particular attention will need to be given to the long-standing issue of provisions for special and differential treatment that take into account the development perspective of developing countries. At the same time, the WTO agenda is expanding to incorporate so-called 'new' issues brought forward at the 1996 WTO Ministerial Conference in Singapore (investment, competition, government procurement, and trade facilitation). Some believe that further liberalisation in these areas will help developing country participants to attract foreign investment and to improve the operation of their economies, while also improving and securing access to other markets. Others believe that negotiations on these new issues do not necessarily create new opportunities for developing countries, but will impose burdens that these countries are ill-prepared to bear. The challenge will be to strike the right balance and to provide adequate support and safeguards during and after negotiations in these areas.

In the meantime, there is scope to build further on some recent initiatives. The United States' Africa Growth and Opportunities Act and the European Union's Everything But Arms initiative, whereby Member States agreed to provide duty and quota-free access to most goods from the least developed countries (LDCs), were important steps forward but need to be followed by similar action by all developed countries. In addition, because their overall development and supply-side constraints will limit the LDCs' ability to use these new opportunities in the short term, initiatives such as the Integrated Framework for Trade-related Technical Assistance to Least Developed Countries (IF), which aims to address supply-side and domestic trade policy limitations, should be used in order to ensure that the poorest countries are able to participate effectively in, and benefit from, the global trading system.

Notes

1 See chapter 1 of *World Economic and Social Survey 2001* (United Nations publication, Sales No. E.01.II.C.1).

2 For details, see *World Economic and Social Survey 2001*, pp.51-53.

3 Anne Krueger, "International Financial Architecture for 2002: A New Approach to Sovereign Debt Restructuring", Address to the National Economists' Club Annual Members' Dinner, Washington, D.C., 26 November 2001 (available at http://www.imf.org).

CHAPTER II: INTERNATIONAL TRADE AND FINANCE

International economic linkages increased in the 1990s and were one of the driving forces for economic growth during the decade. In 2001, their role was reversed as they transmitted economic weakness across nations, resulting in a synchronized global slowdown. With these enhanced global linkages, the terrorist attacks of 11 September, physically concentrated in only two cities, were transformed into worldwide economic shocks.

Amidst the global slowdown, the international economic environment deteriorated in 2001, particularly for many developing countries and economies in transition: international trade stagnated at the global level and declined significantly for many countries; the international prices of many commodities on which the exports of a large number of developing countries are still concentrated fell substantially; net capital flows to developing countries remained at a low level; and the external financing conditions for these economies became more stringent. While some improvement is expected, many developing countries and transition economies continue to face a challenging external situation in 2002.

Despite these discouraging short-term developments, some international policy developments augur well for the longer term. The Fourth Ministerial Meeting of the WTO was successful in setting an agenda for international trade negotiations, with the prospect that these might particularly address some of the difficulties confronting developing countries and economies in transition. There were also tentative signs of a strengthening of international financial cooperation, including a possible bottoming out of flows of official development assistance and greater attention to the need for a clear framework for private sector involvement in external debt crises.

SLOWING INTERNATIONAL TRADE

World trade decelerated dramatically over the course of 2001, growing by less than 1 per cent in terms of the volume of world total exports, a significant decline from growth of over 11 per cent in 2000 (see table A.9). This slowdown emanated primarily from the decline in global demand for ICT-related products, particularly in major developed economies. As the weakness in the global economy intensified in the second half of the year, exacerbated by the terrorist attacks, a general reciprocal reduction in import demand across nations led to a sharp dwindling in all trade categories: manufactured goods, primary commodities, and services. With a gradual recovery in global economic activity over the course of 2002, world trade is expected to pick up; however, the uncertain prospects for the ICT sector, the slow recovery of investment and the obstacles to commerce created by enhanced security measures mean that the growth of international trade is likely to be in the region of only 3 per cent.

The **import** demand of *developed economies*, particularly of the United States, remains the key for the dynamics of world trade. The aggregated imports of developed economies as a group registered virtually no growth in 2001. Imports of the United States declined by more than 3 per cent, leading to a negative contribution of about 1 per cent to world trade.[1] The decline in import demand was led mainly by the contraction of investment spending, but the terrorist attacks had also caused severe disruption in trade, with the value of United States' merchandise imports dropping by 14 per cent in September 2001 compared to the same month of the previous year. The growth of European Union imports also decelerated as early as the first quarter of 2001. Despite some cushioning from the appreciation of the euro, the decline accelerated in the second half of 2001. Excluding intra-EU trade, imports of EU from the rest of the world were even weaker. Meanwhile, import demand in Japan weakened continuously during the course of 2001, along with a significant decline in exports and a prolonged contraction in industrial production. The weakness intensified in the second half of the year: the slowdown in the ICT sector resulted in reduced demand for related parts and imports of other goods, and services also decreased.

The prospects for a rebound in import demand from the major developed countries remain lacklustre in 2002. The anticipated economic recovery in most developed economies, at least in the early phase, will be driven mainly by policy stimuli; corporate capital spending is expected to remain weak until late 2002, while private consumption is expected to remain moderate.

Import demand in most *economies in transition* was robust in 2001. Recovery in domestic demand in many economies in this group fuelled imports, with investment goods accounting for a large share. Except Poland, most economies in the group registered double-digit growth of imports in 2001, although a slight deceleration was witnessed compared with 2000. A further moderation in the growth of imports for the group is expected for 2002, as the weakness in the external sector of these economies accumulates.

The deceleration in imports was more significant for *developing countries* than for other groups, a swing from growth of 16 per cent in 2000 to less than one per cent in 2001. A general trend of weakening domestic demand was a common reason for the sharp decline in the growth of imports in many developing countries, with other factors varying from country to country. For many economies in Asia and Latin America, which have large share of intra-industry trade, or so-called "processing trade", a slowdown in the demand from the rest of the world, particularly from major developed countries, led to a slowdown of the same magnitude in the imports of raw materials and intermediate goods. For many commodity-exporting countries, a deterioration in their terms of trade restrained their import demand. Meanwhile, reduced external financial flows (see below) also curbed imports in some developing countries. Only a moderate recovery to about 5 per cent in the growth of imports is expected for developing countries in 2002, as the improvement in both income and the terms of trade for most of these economies will be limited.

Export performance was homogeneously weak across major *developed countries* in 2001. Both North America and Japan registered outright declines in the volume of exports of 3 and 5 per cent respectively, while Western Europe's growth was less than 3 per cent, including intra-regional trade.

Many *economies in transition* maintained a double-digit growth of exports in 2000, partly because of the relatively low exposure of their exports to the markets of major developed countries—more than one third of their exports were within the group. Meanwhile, with improvement in both the quality and the composition of their exports, many economies in Central and Eastern Europe have gained market shares in Western Europe. At the same time, the continued stabilization and recovery of the Russian economy has generated more synergy for international trade among many economies in transition.

The export performance of the *developing countries* varied, but a large number of them suffered a double blow: a decline in the volume of exports combined with a drop in the prices of their exports. For example, both the volume and the value of East Asia's total exports fell in 2001, with export values declining most, largely because of the plunge in both the demand and the prices of ICT products.[2] The export slowdown in the Republic of Korea, Malaysia, the Philippines, Singapore and Taiwan Province of China,[3] was particularly sharp, and the high degree of intraregional industrial linkages exacerbated the set back to trade in East Asia.[4] The situation was not unique to the economies with a large share of ICT products in their exports. Many economies in Latin America and Africa, where exports consist to a greater extent of general manufacturing goods and/or primary commodities, also experienced a decline in both the prices and the volume of their exports, although to a lesser degree. Many oil-exporting countries faced the same situation as they cut the volume of exports when the prices of oil fell, although a few non-OPEC countries managed to maintain, or even to increase, their volume of exports.

As developing countries have increased their share of exports in the global economy,[5] none of them could be immune to such a deep and broad external demand shock, but a number of them have attempted to alleviate the situation by various measures. For example, in Africa, currency depreciation in several countries improved export competitiveness and provided a stimulus for exports. Non-traditional exports (such as horticultural products) increased in several countries, while others benefited from increased exports of textiles and clothing as a result of the improved access to the United

States market provided under the Africa Growth and Opportunity Act (AGOA). Privatization led to efficiency gains and increased exports in some minerals-producing countries. Meanwhile, a few countries were able to take advantage of the weaker international prices of some commodities to increase export volumes and thus sustain export revenues.

Matching the projected mediocre recovery of import demand in major developed economies, the outlook for global export growth remains weak in 2002. The growth of exports of the major developed economies will improve only moderately in 2002, the momentum of the relatively strong exports from the economies in transition is expected to soften, and the pace of exports for many developing countries will remain far below their average performance of the last decade.

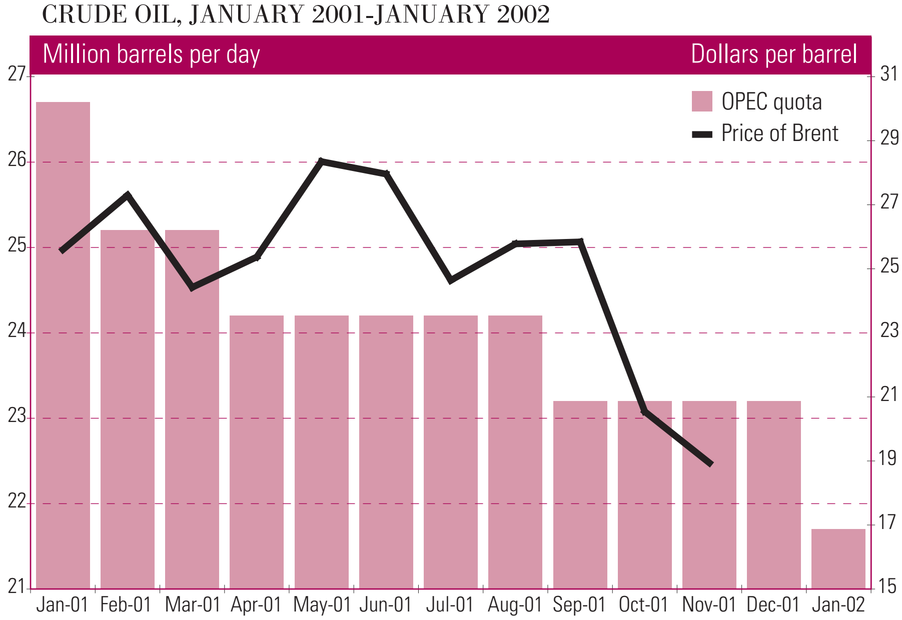
The large fluctuation in international trade has been accompanied, as almost always, by considerable adjustments in external balances across countries. Among the major developed economies, the United States, as expected, reduced its external deficits from $450 billion to about $400 billion in 2001, but the remaining deficit is still large enough to be an unstable factor for the world economy. While Western Europe improved its external balance moderately, Japan's surplus dwindled by more 15 per cent. For a majority of developing countries and economies in transition, the improvement in their external balance in 1999-2000 from the 1997-1998 international crises reversed markedly during 2001. A further deterioration in the external balance for the group of developing countries and economies in transition is likely in 2002, posing a challenge for these economies.

SOFTENING INTERNATIONAL COMMODITY PRICES

The *prices of oil* exhibited considerable volatility in the final months of 2001. For the year as a whole, the price of Brent crude oil averaged $24.5 per barrel (pb) but is expected to decline to about $20 dollars pb in 2002. The decline primarily reflects weak demand, strained cohesion within the Organization of the Petroleum Exporting Countries (OPEC), and increased supply from non-OPEC producers.

Prior to the terrorist attacks of 11 September, oil prices in 2001 fluctuated within the OPEC target range of $22 to $28 pb,[6] partly due to OPEC cutting its production quotas three times by a total of 3.5 million barrels per day (mbd) (see figure II.1). Developments since the terrorist attacks have posed OPEC with a dilemma. Prices far below the target range would constrain spending and aggravate fiscal imbalances in most member countries. Overly aggressive quota policies in the context of a global slowdown and a campaign against international terrorism would alienate major consumers. Furthermore, at the same time as OPEC has cut production, non-OPEC producers have increased their output, undermining OPEC's ability to influence prices. Responding to these challenges, OPEC's ministerial meeting on 14 November 2001 maintained the goals of achieving market stability and minimizing price volatility and called for other oil-exporters to cooperate in order to meet these goals. OPEC announced a further reduction in production of 1.5 mbd, effective 1 January 2002, subject to a firm commitment from key non-OPEC

Figure II.1.
OPEC PRODUCTION QUOTA AND THE PRICE OF BRENT CRUDE OIL, JANUARY 2001-JANUARY 2002



Sources: International Energy Agency, *Middle Eastern Economic Survey* and IMF.

Note: OPEC refers to OPEC-10. It excludes Iraq.

January 2002 quota reflects the proposal at OPEC's ministerial meeting on 14 November 2001.

oil producers to concomitantly reduce their production by a total volume of 0.5 mbd.

The incentive for the non-OPEC producers to avoid a collapse in prices is high. Their production costs generally exceed OPEC's, and they rely heavily on oil for exports and government revenues. For instance, half of Russian export revenues are from sales of oil and gas. As of early December 2001, Mexico, Norway, and Oman had made conditional pledges to cut their production by 100,000 bd between 150,000 bd, and 40,000 bd, respectively. The Russian Federation, which initially had offered to cut exports by 30,000 bd, expanded its offer to 150,000 bd. Subsequent to these announcements, OPEC sought to ensure that the cuts would endure beyond the first quarter of 2002 and at least until mid-2002.

The risks to the price forecast are primarily on the downside and are generally related to potential increases in supply. First, following the reduction in quotas in 2001, OPEC's share of the world oil market shrunk from nearly 40 per cent at the end of 2000 to 34 per cent at the end of 2001, reducing the Organization's leverage in the market. At the same time, OPEC has nearly 5 mbd of spare capacity. Additionally, OPEC was producing significantly in excess of quotas in late 2001 – in October, overproduction was estimated at almost 1 mbd. Secondly, even though a cooperative effort involving non-OPEC producers appeared likely, past history indicates that there might be a difference between commitments and implementation. Although the non-OPEC producers' pledge to curb production in 1999 had a positive effect on market sentiment and prices increased, the implementation of their commitments, particularly in the case of the Russian Federation, was imperfect. In 2002, the market may be more wary of the credibility of the pledges made.

There are also some upside risks to the price forecast. First, the supply of oil from Iraq, which accounts for around 3.5 per cent of global oil production, remains uncertain. The oil-for-food programme was renewed for another six months at the end of November 2001 but, in the event of more discussions in the Security Council in 2002 concerning revisions of the sanctions regime, there is a possibility of further disruptions in the supply of oil from Iraq. Moreover, although events in Afghanistan have had limited effects on oil prices so far, a spillover to other countries could change the situation as demonstrated by the Gulf crisis of 1990/1991.

Non-oil commodity prices fell by about 2.5 per cent, on average, in 2001 (see figure II.2). Prospects for 2002 are for a slight price increase across most categories in the non-fuel commodity index, as world demand and manufacturing activity start to recover gradually, while excess supplies continue to moderate price increases in several markets.

Among the various commodity groups, the prices of *foods and grains* improved after the second quarter of 2000. Nonetheless, this recovery ended towards the end of 2001, as the rate of increase of the price index of food and grains decelerated during the year. Average food and grains prices remain significantly below their level before the Asian crisis.

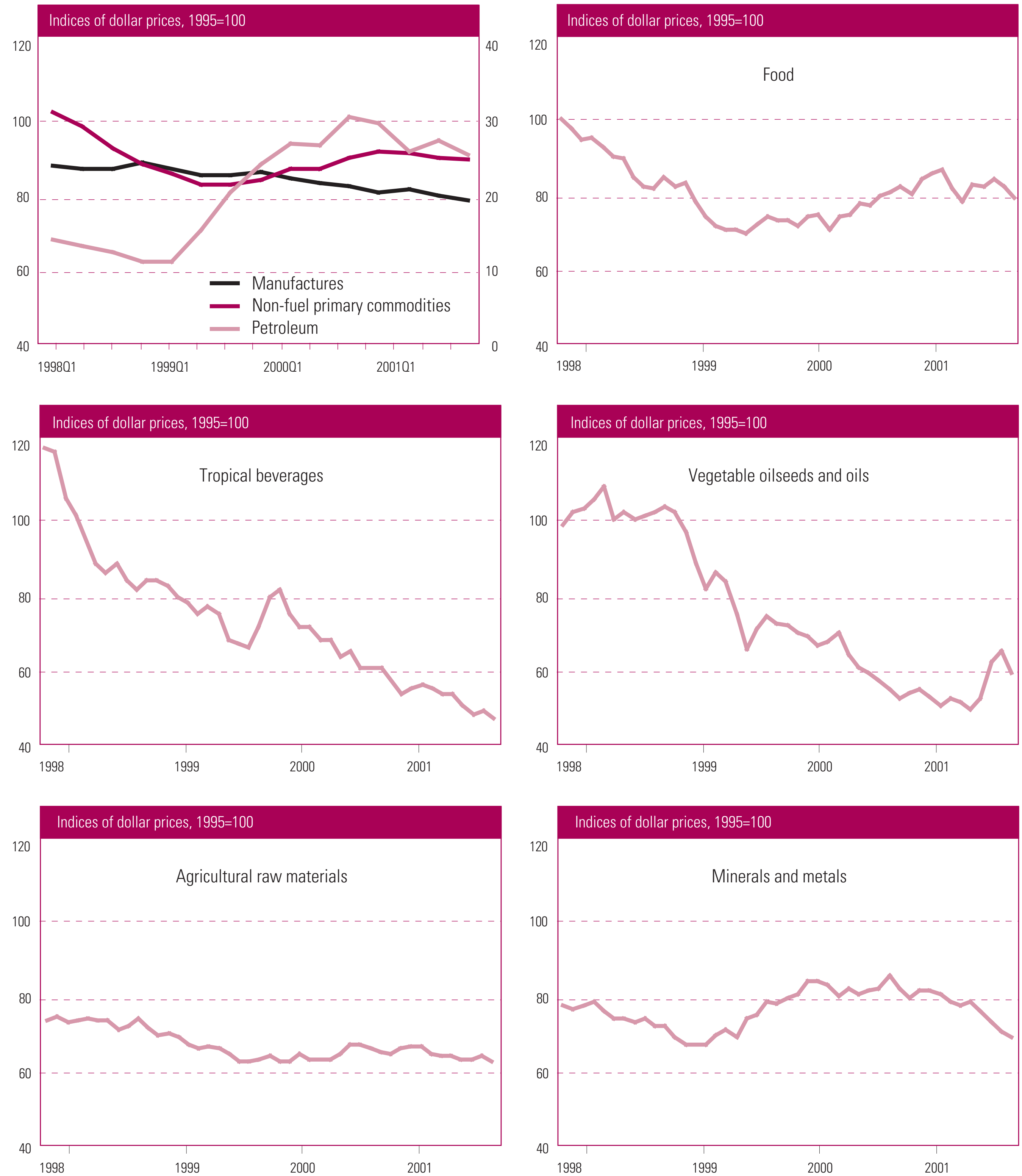
Trends, however, have been divergent among the main components of the *food* category. For instance, the price of s*ugar* was affected throughout the past decade by increasing production, particularly in Brazil, the largest producer. After a strong upturn, which started in 2000 and lasted until the first half of 2001, the price of sugar fell in the third quarter of 2001 due to increased stocks. Conversely, the price of *bananas* benefited from production cuts and growing demand from countries in Asia and Central and Eastern Europe. The price increased by about 45 per cent in 2001, but is expected to moderate significantly in 2002.

Grains have also shown different price trends: the prices of *maize* and *wheat* rose in 2001, whereas the price of *rice* reflected the high level of stocks and continued to decline. All these major grains are forecast to post some increase in prices in 2002 in view of the expected reduction of stocks during the 2001-2002 season. Nonetheless, due to the continued relatively high level of stocks, the price of rice is forecast to advance more moderately than the prices of maize and wheat in 2002.

The prices of *tropical beverages* continued to slide in 2001. As in other commodity categories, trends have been very divergent among the main components of the group. For instance, due to supply restrictions in Côte d'Ivoire and strong demand from the Russian Federation and the Central and Eastern European countries, *cocoa* prices recovered significantly in 2001. This recovery is expected to continue in 2002. Conversely, the prices of tea and coffee were weak in 2001. *Tea* prices suffered from the impact of production increases, as well as the devaluation in Sri Lanka in 2001. *Coffee* prices have continuously fallen since 1998 and declined sharply in 2001, reflecting oversupply due to large crops in major producers, such as Brazil and Viet Nam, as well as the ineffectiveness of supply restriction measures—export retention attempts by the Association of Coffee Producing Countries—in the face of declining world demand. The weakening of the Brazilian currency also contributed to the fall in coffee prices in 2001. The decline is expected to moderate in 2002 if normal weather conditions prevail; prices, however, are not anticipated to recover in the near term.

The prices of *vegetable oilseeds and oils* have been falling since their recovery in 1998. They continued to weaken during the first half of 2001, mainly due to continued production increases, particularly for soybeans and

Figure II.2.
PRICES OF PRIMARY COMMODITIES AND MANUFACTURES, 1998-2001



Sources: UNCTAD, *Monthly Commodity Price Bulletin* and IMF.

palm oil, the two largest components of this group. However, some encouraging signs were recorded towards the end of the year, as prices improved in the third quarter of 2001 (see table A.8). A small increase in production is anticipated for the period 2001-2002, which, along with good demand prospects in China and India, suggests a continued moderate recovery in prices in 2002.

The prices of *agricultural raw materials* did not sustain their limited gains of the second half of 2000 and early 2001. The combined price index recorded a 5 per cent decrease in the third quarter of 2001 when compared with the same period of the previous year, in a path that tends to follow the economic cycle more closely than other agricultural commodity groups. The price of *cotton* is expected to have declined by about 12 per cent in 2001 due to a record crop in the United States and increased stocks. Due to expanded planting and stagnant global demand, prices are not expected to recover in 2002. The price of natural *rubber* also declined significantly in 2001, reversing the gains of 2000. Despite large increases by China, world demand for natural rubber slowed significantly as production kept growing, notably in Viet Nam and Thailand. Nevertheless, a modest upturn in demand and a slower growth of supply are expected to reduce excess stocks and have a positive impact on prices in 2002. A supply management arrangement is being negotiated among the three largest producers of natural rubber—Thailand, Indonesia and Malaysia. The initiative, however, is unlikely to yield major results if the outcomes of similar cooperative arrangements for other agricultural commodities are used as indicator.

Prices of *minerals, ores and metals* declined in 2001 (see table A.8), closely following the downturn in world economic growth and the resulting increases in stocks. The combined price index of this commodity group is expected to have declined by at least 8 per cent in 2001. Demand for *aluminium* and *copper* has been especially hurt by the downturn in key manufacturing activities, such as the automotive sector in the case of aluminium and the electronics sector in the case of copper. Lower demand from stainless steel makers led to a sharp fall in the price of nickel in 2001. During the past few months, producers have been reacting to the lower prices by cutting output; this has brought supply more in line with demand averting steeper price declines. As a result, some recovery in the prices of copper, aluminium and nickel was recorded towards the end of 2001. This notwithstanding, for the year as a whole, the price of c*opper* and *nickel* are expected to have declined by between 14 and 30 per cent, while the price of *aluminium* declined more moderately, partly due to more substantial production cutbacks and partially because of the electricity supply crises in the United States and Brazil. Conversely, the price of *lead* recovered moderately in 2001: the weak demand in developed countries was met by tight supply and stocks declined. The outlook for most metals and minerals is not encouraging, as prices will remain affected by large stocks and the expected slow recovery of world manufacturing activity. Further cutbacks in supply may be required to sustain prices in the near term.

REDUCED FOREIGN INVESTMENT FLOWS

UNCTAD estimates just before the terrorist attacks showed that world foreign direct investment (FDI) flows were likely to decline by 40 per cent in 2001, to $760 billion (see table II.1). This would represent the first drop in FDI flows since 1991 and the largest in three decades.[7] Furthermore, to the extent that the world economy slowed more than anticipated at that time and since FDI flows tend to be pro-cyclical, the decline in world FDI flows in 2001 may be even larger than estimated and may dip to the 1998 level of less than $700 billion.

The decline in FDI flows in 2001 is mainly the result of the decline in world economic growth and, in particular, in cross-border mergers and acquisitions (M&As).

Table II.1.
INFLOWS OF FOREIGN DIRECT INVESTMENT, BY REGION, 1998-2001

Billions of dollars

	1998	1999	2000	2001[a]
World	693	1 075	1 271	760
Developed countries	483	830	1 005	510
Developing countries[b]	188	222	240	225
Africa[c]	8	9	8	10
Latin America and the Caribbean	83	110	86	80
Asia and the Pacific	96	100	144	125
South, East and South-East Asia	86	96	137	120
Central and Eastern Europe	21	23	25	25
including the countries in the former Yugoslavia	22	25	27	27

Sources: UNCTAD, FDI/TNC database.

a Preliminary estimates, made on 3 September 2001, on the basis of 51 countries that accounted for more than 90 per cent of FDI inflows in 2000. The data cover the first two quarters or the first several months of this year. Estimates for 2001 were derived by annualizing these data. See UNCTAD, "World FDI flows to drop this year", Press release, TAD/INF/PR30 (18 September 2001).

b Including the countries in the former Yugoslavia.

c If South Africa is included, the figures are 8 in 1998, 10 in 1999, 9 in 2000 and 11 in 2001.

M&As account for the bulk of FDI and the dramatic increases in cross-border M&As led to unprecedented FDI flows during 1999-2000.[8] A lull in the consolidation processes in certain industries through M&As (e.g. telecommunications, automobiles) also played a role. The value of cross-border M&As completed between January and 10 December 2001 stood at some $533 billion, about one half of the value during the same period of 2000.[9] This dip in cross-border M&As is a reflection of a decline in the overall number of cross-border M&As, in particular of large-scale deals.

During the period of January-10 December, the total number of cross-border M&As declined from some 7,500 in 2000 to 5,500 in 2001. During the same period, the number of cross-border deals worth over $1 billion declined to 100, worth $336 billion, compared to 163 and $812 billion, respectively, the year before. The significant increases in FDI flows in 1999 and 2000 – by some 50 per cent and 18 per cent, respectively – were driven by these mega M&A deals, for example, the $200 billion acquisition of Mannesmann (Germany) by VodafoneAirTouch (United Kingdom) in 2000 and the $60 billion deal of AirTouch Communications (United States) and Vodafone Group (United Kingdom) in 1999. The value of worldwide M&As (both domestic and foreign) in 2001 is expected to be $1.6 trillion, half the value reported for the previous year.[10]

The declining number of cross-border M&As was combined with a lower average value because of lower share prices. The exchange of shares had become important in financing M&A transactions; in 2000, shares were used to finance some 56 per cent of cross-border M&As.[11] Falling share prices in 2001 dampened the ability of firms to use equity as consideration in many potential M&A deals.[12] With the market value of all stocks listed in the six major stock exchanges falling by one-third in the first nine months of 2001(from $29 trillion at the peak in 2000 to $19 trillion at the end of September 2001),[13] the nominal value of a given number of cross-border M&A deals also falls if shares are used to finance M&As, lowering the recorded value of the investment.

Lower share prices also make it difficult for companies to raise funds in financial markets by issuing new stocks. As a part of these funds is used to finance FDI, the more limited availability of funds can lead to a decrease in FDI flows. For example, Japanese TNCs financed some 30 per cent of their capital expenditures in their affiliates in the United States and Europe with funds raised through stocks (as well as corporate bonds) in 1998.[14]

The M&A-led decline in FDI flows in 2001 affected mostly developed countries, with flows to developing countries relatively unchanged. This is because cross-border M&As are particularly important between developed countries, while FDI through greenfield investment is more important for developing countries. Consequently, UNCTAD estimates that FDI flows to developed countries will fall to $510 billion in 2001 from $1 trillion in 2000 (i.e. by about half), while FDI flows to developing countries are expected to decrease by only 6 per cent, from $240 billion to $225 billion, between 2000 and 2001.[15] Decreases in FDI inflows are expected in both Latin America and developing Asia, while FDI flows to Central and Eastern Europe are expected to remain stable in 2001.

Assuming that the basic firm-specific conditions inducing outward FDI will remain the same, the most important economic determinants of FDI flows are market size and market growth in the various countries or regions that are actual or potential investment locations for production activities by transnational corporations (TNCs).[16] Even before the terrorist attacks, a weakening of demand in some of the world's largest economies had already had a dampening effect on FDI. For example, a survey during early 2001 indicated that two-thirds of United States TNCs expected to maintain FDI in 2001 at the level of the previous year, while 13 per cent were expected to cut FDI.[17] This is in sharp contrast to 2000, when nearly 60 per cent of United States TNCs were optimistic about the global environment and their FDI plans.

Despite this immediate dampening impact, the investment plans of TNCs for the coming three years are still promising. Major TNCs plan to sustain the pace of their international expansion.[18] The expansion is likely to focus on production and distribution functions and the preferred mode of expansion continues to be cross-border M&As in developed countries and greenfield investment in developing countries. According to this survey, the most favoured locations for FDI by TNCs for the next three years are the United States, for developed countries as a whole; Germany, the United Kingdom and France, for Europe; China, for Asia; Brazil, for Latin America; Poland, for Eastern Europe; and South Africa, for Africa (see table II.2). This survey gauged the attitudes of major TNCs for the medium term, in light of the fact that direct investment typically is motivated by longer-term considerations. Similarly, as many as 72 per cent of Japanese TNCs said that they will strengthen and expand their foreign operations, a jump of 55 per cent compared to the previous year.[19]

The effects of the terrorist attacks of 11 September on FDI flows are difficult to gauge. Company surveys suggest that they would be limited.[20] In October/November 2001, the UNCTAD *et al.* survey revisited a number of the firms they had surveyed just before 11 September and found that few expected to change their FDI plans in the light of the attacks. Similarly, the Japan External Trade Organization (JETRO) found in October 2001 that nearly half of all firms surveyed did not expect to change their

Table II.2.
MOST-FAVOURED ECONOMIES BY REGION: SHARE OF RESPONSES CITING AN ECONOMY AS A PRIORITY LOCATION IN A REGION

Percentage

Developed economies		Developing Asia		Latin America		Central and Eastern Europe and Commonwealth of Independent States		Africa and West Asia	
Economy	%	Economy	%	Economy	%	Economy	%	Economy	%
United States	27	China	27	Brazil	31	Poland	33	South Africa	17
Germany	16	Indonesia	10	Mexico	20	Hungary	20	Egypt	12
United Kingdom	12	Thailand	10	Argentina	15	Czech Republic	18	Turkey	8
France	10	Malaysia	9	Chile	10	Russian Federation	11	Morocco	8
Italy	6	India	9	Colombia	5	Romania	4	Nigeria	6
Japan	5	Korea, Republic of	7	Peru	4	Bulgaria	4	Saudi Arabia	6
Spain	5	Taiwan Province of China	7	Bolivia	3	Ukraine	2	United Arab Emirates	5
Sweden	3	Viet Nam	5	Venezuela	3	Other	7	Israel	2
Canada	3	Hong Kong, SAR of China	4	Other	8			Angola	2
Ireland	2	Philippines	4					Other	4
Other	13	Singapore	4						
		Other	4						

Source: UNCTAD, "Transnational corporations expected to continue worldwide expansion, but full impact of economic slowdown still unknown", Press Release, TAD/INF/PR27/Rev.1 (5 December 2001). Based on the survey conducted by UNCTAD/AFII/Andersen.

FDI plans, with most of the balance not yet able to make an assessment (figure II.3).[21] These findings are also consistent with a survey undertaken by A.T. Kearney in September/October 2001: two-thirds of corporate executives of the world's 1,000 largest firms said that they still intended to invest abroad at almost the same levels as already planned, while 16 per cent said that their FDI in 2001 would increase and 20 per cent said that it would decline.[22]

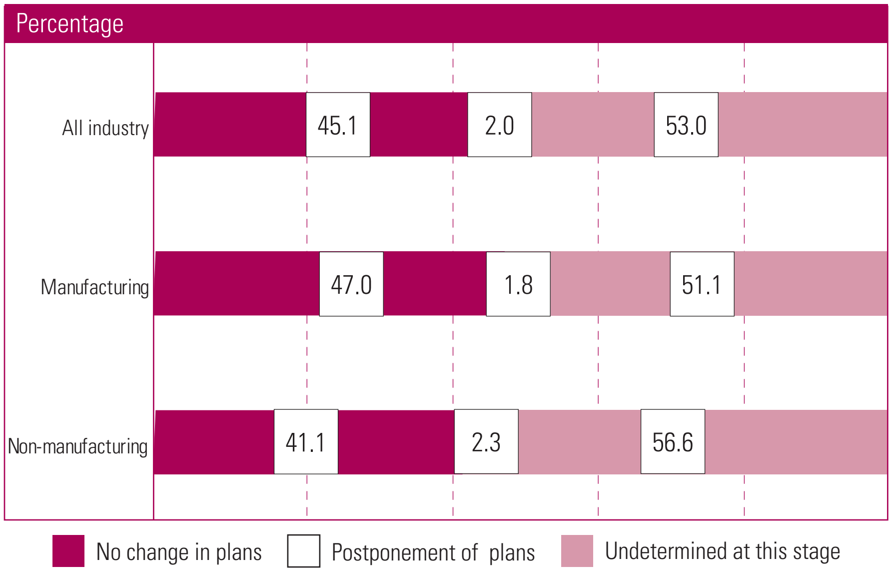
The impact of the terrorist attacks on FDI is likely to be through their effect on economic growth, one of the principal determinants of FDI flows. In particular, if the attacks continue to aggravate the economic slowdown, it is likely that FDI flows will decline further. Such an additional decline could be limited geographically. In particular, companies and countries that rely heavily on United States markets may be affected more. For example, FDI outflows from the United Kingdom – a good part of which are being directed to the United States – are expected to decline considerably in 2001, according to UNCTAD estimates. On the other hand, China will receive record FDI inflows, fueled not only by continued economic growth but also by the impact of China's accession to WTO. Industries in which FDI may be affected negatively include transportation services, financial services and tourism because they were particularly affected by the attacks. A number of companies are restructuring, being acquired or are going bankrupt. Difficulties of this kind reduce the capacity of TNCs in these industries to invest abroad.

More generally, the higher level of uncertainty created by the attacks, including the perception of increased political risk associated with war and terrorism, may induce some companies to adopt a "wait-and-see" position and to delay planned investment until they gain a better comprehension of world economic prospects and the longer-term impact of the attacks on the United States – a possibility reflected in the JETRO survey reported above.[23]

On the other hand, if the economic policy response to the events helps to counteract the economic slowdown, it may also help to stabilize FDI flows. Moreover, the slowdown in the world economy adds to competitive pressures in many industries, forcing companies to enhance their cost-efficiency. Faced by more price-driven competition, some TNCs may expand production facilities in low-cost countries; in this case, there may be some redistribution of FDI flows towards developing countries. This effect could be even stronger if developing countries continue to liberalize their regulatory regimes in order to attract FDI.[24]

On balance, the decline of FDI flows in 2001 is not likely to be recouped in 2002. For developing countries, developments are likely to be uneven, with the overall result difficult to predict. On the positive side, the potential for FDI is far from exhausted in many countries and

Figure II.3.
THE EFFECTS OF THE TERRORIST ATTACKS ON PLANS FOR FDI BY JAPANESE TNCs



Source: Data provided by JETRO, International Economic Research Division.

Note: On the basis of 659 Japanese TNCs that responded to this question in the survey conducted by JETRO in October 2001.

preliminary data for countries such as China, Mexico and South Africa suggest a substantial increase in FDI flows. Many developing countries have only started to allow FDI in utilities and other services, while others that have already done so might benefit from "sequential" investment following the initial privatization phase. Also, as the stock of FDI in developing countries is growing, the potential for FDI through reinvested earnings from prior investments (especially in countries where high profits are realized) is increasing. On the other hand, most developing countries will not be able to de-link themselves from global economic developments and their effects on investment.

In the longer run, the key is economic growth. To the extent that consumer confidence and economic growth can be restored, FDI flows are likely to increase again. This is particularly the case because other basic factors determining FDI flows – such as the quality of infrastructure, the availability of skills and technological capacity in host countries – have not changed. Nor have the factors driving cross-border M&As in the international market for firms.[25] And neither have the principal driving forces of the growth of international production: the combination of the liberalization of FDI regimes (which permits and encourages the growth of FDI, supported further by active efforts to attract investment), developments in information and communication technologies (which make it possible to manage worldwide affiliate networks on an ongoing basis) and competition between firms (which encourages them to seize the possibilities offered by liberalization and technology).

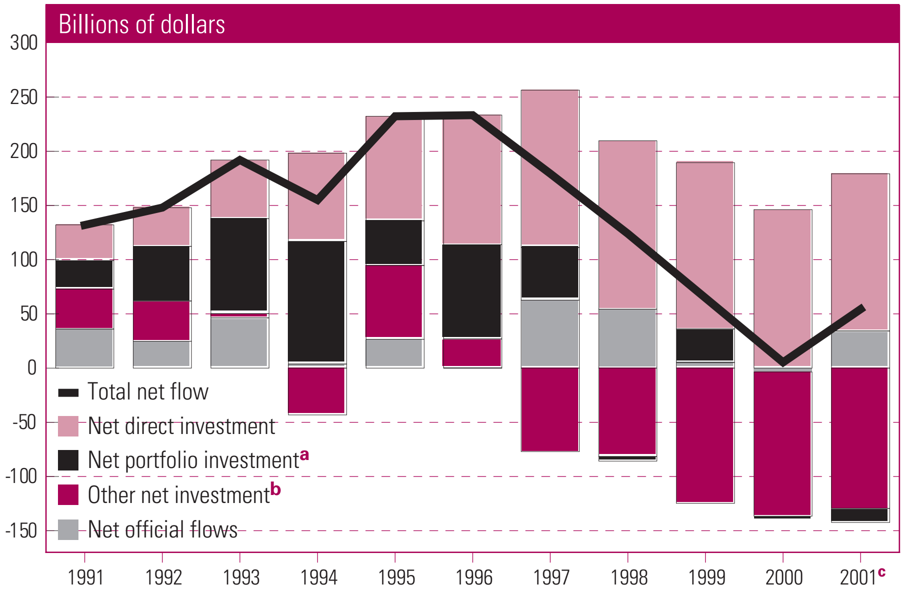
HESITANT FINANCIAL FLOWS TO DEVELOPING COUNTRIES AND ECONOMIES IN TRANSITION

In 2001, there was a net financial flow to developing countries and transition economies of almost $37 billion. This was tiny by the standards of the mid-1990s, but larger than the amount in 2000 (see figure II.4). Almost all of the net inflow in 2001 was accounted for by net official financial flows, mainly because of the rise in assistance to countries in financial difficulties. FDI continued to be the mainstay of net private financial inflows although, as indicated in the previous section, it declined from its level in 2000. Portfolio investment and other investment, mainly bank credit, were the sources of substantial net private financial outflows from developing countries and transition economies in 2001. A recovery in private financial flows to these countries is not expected in 2002, although official financial flows may be further bolstered by an increase in multilateral assistance to economies adversely affected by the global economic slowdown and financial difficulties.

Private financial flows

Investor concern about risk rose in mid-2001 with growing evidence of a global economic slowdown and the consequent deterioration of growth prospects for developing countries and transition economies. The terrorist attacks and the deepening financial difficulties of Argentina towards year-end exacerbated the situation. This was seen in both credit and equity markets and FDI flows.

Figure II.4.
NET FINANCIAL FLOWS TO DEVELOPING AND TRANSITION ECONOMIES, 1991-2001



Sources: International Monetary Fund, World Economic Outlook database (on-line), December 2001 and UN/DESA.

[a] Including portfolio debt and equity flows.

[b] Including short- and long-term bank lending. It may include some official flows owing to data limitations.

[c] Estimate.

In July and August, financial uncertainties in Argentina and Turkey and the strong spillover effect on Brazil increased the perception of investment risk in these markets and, to a lesser extent, in other emerging markets. This was reflected in the widening spreads between the yields on international bonds of Turkey and Latin American countries and the yield on United States Treasury bonds, the risk-free benchmark (see figure II.5). After the terrorist attacks, already-high investor risk aversion rose sharply, raising spreads again and thereby further deterring borrowing. Although there was a subsequent improvement in sentiment towards investment in some emerging markets, creditors largely took defensive positions by selecting investment-grade issues.[26]

Argentina's announcement in November of a proposal to restructure its public debt to avoid default and its subsequent imposition of banking and exchange controls to prevent a collapse of the banking system were additional negative developments for financial flows to emerging markets. The immediate effect on investment risk beyond Argentina and its major trading partner, Brazil, was modest. Nevertheless, uncertainty about the vulnerability of international bonds to forced restructuring by sovereign debtors, such as Argentina, placed a chill on investment in emerging market debt.

A number of emerging market economies faced difficulty in rolling over maturing bonds with new issues in late 2001, and this is expected to persist into 2002. The result was large net outflows from Argentina and Turkey and a decline in net bond financing for Brazil. The overall credit flow from the issuance of bonds by emerging markets as a group was sharply lower in 2001 as a result.

With the outflow of funds to banks exceeding the inflow in 2001, international banks reduced their exposure to emerging market economies, continuing a trend since the Asian financial crisis. Paralleling the bond markets, there were large net repayments by Argentina and Turkey, substantial but declining repayments by Asian economies and only modest net bank lending to other emerging market economies.[27] At the same time, slowing economic growth reduced demand for credit and currency weakness in some developing countries deterred foreign currency borrowing. In addition, high liquidity levels in domestic banks in regions other than Latin America boosted local borrowing. Loan activity was further subdued after the terrorist attacks owing to the postponement of loans and the "flight to quality".[28]

Net portfolio equity investment flows to emerging markets in 2001 were substantially lower than in the previous year, especially following the terrorist attacks. Price declines in emerging equity markets began early in the year in parallel with markets in developed economies and intensified after mid-year as a result of the deteriorating global economic growth prospects followed by the terrorist attacks. This raised the cost of new equity financing while weakening economic conditions soured the outlook for profits. Equity prices in oil-exporting countries, such as Malaysia, Mexico and the Russian Federation, rose because of strong oil prices during most of the year, but prices in countries facing balance-of-payments difficulties and in economies whose exports are most vulnerable to the global economic slowdown suf-

Figure II.5.
YIELD SPREADS ON EMERGING MARKET BONDS,
2 JANUARY 2001-30 NOVEMBER 2001

Source: Data of J.P. Morgan Co., New York.

fered declines. Primary equity issuance by emerging market firms was negligible in late 2001 as many planned issues were delayed or cancelled. Issuance in 2002 is not expected to rebound substantially, given the expected continued weakness of overall economic and financial market conditions.

As elaborated in the preceding section, FDI also declined in 2001, although it remained the main source of net private financial flows to developing countries and transition economies for the fourth consecutive year.

Official financial flows

A new round of financial rescue packages for countries in financial distress spurred the increase in official flows in 2001. Nevertheless, the International Monetary Fund remained a net recipient of funds from the developing countries during the first nine months of 2001, although on a markedly reduced level compared to the same period of 2000 ($2.4 billion versus $7.2 billion). The release of about $4.7 billion of the $15.5 billion stand-by facility to Brazil and sizeable drawings by other countries, such as Turkey, against stand-by facilities approved in previous years were the major disbursements. Loan repayments by previously crisis-affected countries of Asia and by the Russian Federation have begun to wind down. The total net flow of funds to the IMF from the transition economies also declined sharply as disbursements rose in tandem with higher loan commitments.

Net lending by the World Bank rose moderately in 2001, although concessional loans from the Bank's International Development Association (IDA) rose strongly owing to a sharp rise in lending to Africa during the year. The sizeable disbursements to Ethiopia in support of post-conflict rehabilitation and to Kenya in support of its structural adjustment programme contributed to the increase. IDA disbursements included several Africa-wide programmes, such as a concerted response to the HIV/AIDS crisis, and assistance early in the year to countries to adjust to high oil prices.

Net flows from the regional development banks increased as well, led by the European Bank for Reconstruction and Development whose net disbursements nearly doubled during the first three quarters of 2001.

Data on official development assistance (ODA) in 2001 were not available at the time of writing. In the preceding year, ODA declined by 6 per cent in nominal terms to $53 billion.[29] This was equivalent to 0.22 per cent of the GNP of the member countries of the Development Assistance Committee of the OECD, the lowest ratio ever recorded. At the meeting of the Joint Ministerial Committee of the Boards of Governors of the Bank and the Fund (Development Committee) in Ottawa on 18 November 2001, ministers agreed that a substantial increase in ODA levels was needed to enable the low-income countries to take advantage of opportunities arising from their implementation of sound policies. Several ministers pointed to the need to reach the target of 0.7 per cent of GNP called for in various United Nations forums.

The outlook for concessional lending by the World Bank for the fiscal years 2003-2005 improved as negotiators sought to complete agreement on the thirteenth replenishment of IDA resources (IDA-13) by early 2002. For the first time in IDA history, borrower countries as a group participated in the replenishment discussions in an effort to strengthen the development partnership.

Meanwhile, to respond to the economic dislocations resulting from the terrorist attacks, the World Bank is offering additional long-term financial assistance. Additional credits may be provided to those countries where adverse external factors dampen export demand and weaken commodity prices, on condition that the countries are maintaining sound macroeconomic policies and implementing reform programmes. For other strongly performing countries, the World Bank may accelerate the preparation of new adjustment operations. In addition, beginning on 1 May 2002, borrowing countries with sound macroeconomic policies and good programme implementation will be able to avail themselves of the "deferred drawdown option" (DDO), which is, in effect, a contingent credit line to protect their core structural programmes during times of reduced access to the financial markets.[30] It will be available to countries qualified either to borrow from the World Bank or to use both Bank resources and IDA credits.

TRADE POLICY DEVELOPMENTS

The preparations for the Fourth WTO Ministerial Meeting in Doha, Qatar dominated trade discussions in 2001. Other trade policy developments during the year stemmed from the so-called 'built-in agenda' of the WTO. New negotiations on services and agriculture, envisaged when the WTO Agreement was approved in 1994, were begun in 2000 and continued in 2001. In addition, there were talks within the WTO on other aspects of the implementation of the results of the Uruguay Round. There was also intensive debate inside and outside the WTO on the effects of the Agreement on Trade-related Aspects of Intellectual Property Rights (the "TRIPS Agreement") on access to medicines to treat HIV/AIDS. Other developments included the continuing rapid growth in the number of regional trade agreements and further progress towards enhanced assistance that would enable developing countries to participate more effectively in the international trading system.[31]

The Third United Nations Conference on the Least Developed Countries (UNLDC III), held in Brussels in May 2001, stressed the importance of enhancing market access opportunities for LDCs and concluded with a Programme of Action that praised the efforts of a number of countries to improve market access for LDCs. It noted the EU's decision to extend duty and quota-free access to most goods from the LDCs[32] and encouraged other major developed countries to do likewise. However, it was also noted that, with the exception of a few products, even with such enhanced market access in place, LDCs' capacity to use these new opportunities will remain strongly affected by, and linked to, domestic supply-side and policy constraints, in addition to remaining market access barriers, such as rules of origin and non-tariff measures.

Given these constraints, for a large number of WTO developing-country members the most challenging task in Doha was to make any new trade negotiations a 'development round' by ensuring that their concerns were reflected in the negotiating mandates, i.e., in particular regarding implementation, TRIPS and public health, special and differential treatment, transfer of technology, trade, debt and finance, and technical cooperation.

Developments prior to Doha

Negotiations within the WTO on **agriculture** started in early 2000 and continued during 2001 on the basis of Article 20 of the WTO Agreement on Agriculture. One hundred and twenty one countries submitted various negotiating proposals during this period. The most important issues on the agenda were tariff quota administration, tariffs, export subsidies, export credits, state trading enterprises, export restrictions, food security, food safety, and rural development. A number of proposals referred to the need to eliminate tariff peaks and tariff escalation, particularly for products of export interest to developing countries.

On domestic support, many developing countries called for provisions that were more responsive to those countries' specific needs and special situations, especially with respect to food security, rural development and poverty alleviation. Virtually all developing-country negotiating proposals called for the elimination of export subsidies. There were also proposals for improved measures in favour of least developed and net food-importing developing countries.

The planned negotiations on **services** entered into a next phase, following the adoption of the Negotiating Guidelines and Procedures by the WTO Council for Trade in Services in March 2001. During 2001, negotiations were extended to emergency safeguard measures (Article X); government procurement (Article XIII); and subsidies (Article XV). Unlike trade in goods, countries have maintained their right to introduce new regulations on the services sectors and the need for this flexibility for developing and least developed countries was further emphasised. The Negotiating Guidelines and Procedures stress the need for developing countries to liberalize at a pace consistent with their development situations and emphasize the liberalization of sectors and modes of supply that are of export interest to them. So far, developing countries have been particularly interested in specific services sectors (construction, energy, tourism, and air transport) and specific modes of supply (Mode 4 - temporary movement of natural persons), and have made a number of proposals in these areas.

Liberalization in **textiles** (the "integration of textiles and clothing into the GATT 1994") in 2001 proceeded according to the provisions on the implementation of the Agreement on Textiles and Clothing (ATC). The ATC defines three successive phases for liberalisation: 1995-1997, 1998-2001, and 2002-2004. On 1 January 2005, the textiles and clothing sector should be in full compliance with the rules of GATT 1994. For the end of the second phase, the WTO Textile Monitoring Body (TMB) prepared a report on ATC implementation.[33] The report, while taking note of the progress towards bringing trade in textiles under the GATT 1994 disciplines, concludes that a significant number of restrictions are still in place. This perceived lack of integration of products with potential significance for trade has disappointed a large number of developing countries that are major textile exporters. The slow progress is evident when looking at market access for textiles in major developed markets.[34] For instance, in its 1997 report, the TMB had noted that the products selected for liberalization were mostly low value-added products.[35] Furthermore, while the overall liberalization target of 51 per cent by 1 January 2002 is likely to be met, only about 20 per cent of the imports under specific quota restrictions have been liberalized by the United States and the European Community.[36]

The implementation of the Agreement on Trade-related Investment Measures (**TRIMs Agreement**), which came into force in 1995, required notified policies inconsistent with that agreement to be brought into conformity within two years for developed countries, five years for developing countries and seven for least developed countries. Of the twenty-seven developing countries that notified the WTO, ten requested an extension of their transition period.[37] After nearly one and a half years of negotiation, an agreement was reached on the extension requests from Argentina, Colombia, Malaysia, Mexico, Pakistan, the Philippines and Romania. On 31 July 2001, the WTO Goods Council adopted decisions granting an extension of the transition to 31 December 2001. Thailand was also granted a waiver until 31 December 2001 by the WTO General Council. Almost all cases relate to the use of local content schemes in the automotive industry, where the production of parts is a major source of employment in many developing countries.

During 2001, there was considerable controversy over the implementation of the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (**TRIPS Agreement**). The contentious issues and the slow implementation process are largely related to the distribution of the costs and benefits of the Uruguay Round agreements. More significantly, the conflict between the preservation of intellectual property rights and the interests of developing countries came to a head over access to essential drugs in low-income countries. Developing countries and NGOs in developed countries argued that, by requiring developing countries to enforce pharmaceutical patents, the TRIPS Agreement enables pharmaceutical companies to charge prices for essential drugs that are unaffordable in developing countries; they viewed this as particularly reprehensible with regard to treatments for HIV/AIDS. TRIPS supporters counter-argued that patents are widely acknowledged as providing the incentive for investment in research and development (R&D) to bring new and more effective pharmaceutical products to market.

A World Bank study has estimated that only a handful of developed countries (United States, Germany, Japan, Switzerland, France, Spain, and Australia) will benefit from TRIPS once it is fully implemented.[38] The study shows that virtually all developing countries have to bear significant costs in terms of patent rights, although these might be offset by benefits from higher FDI inflows and technology transfers to countries with WTO-compliant systems of intellectual property rights.

On **other issues,** there was a continuation of the trend towards increased use of anti-dumping and other safeguard measures in 2001. This trend may be exacerbated by the economic slowdown, as indicated by the steel industry in the United States. Sanitary and phytosanitary measures are increasingly being used as trade measures and are at the centre of a number of disputes in the WTO. There is concern among developing countries about their capacity to meet higher standards and fears that such measures may be used as a form of protectionism. There are also concerns about new developments, such as the safety of organically modified organisms.

Regional trade arrangements

The proliferation of regional trade arrangements (RTAs) continued during 2001. One view is that the slow pace of liberalization within the WTO has led countries to move faster within a regional framework, which is sometimes also seen to have the advantages of being a more controlled environment or a learning experience. Another view is that the very existence of RTAs diverts attention from the multilateral process within the WTO system (although the WTO provides for RTAs in goods and for regional integration arrangements in services).

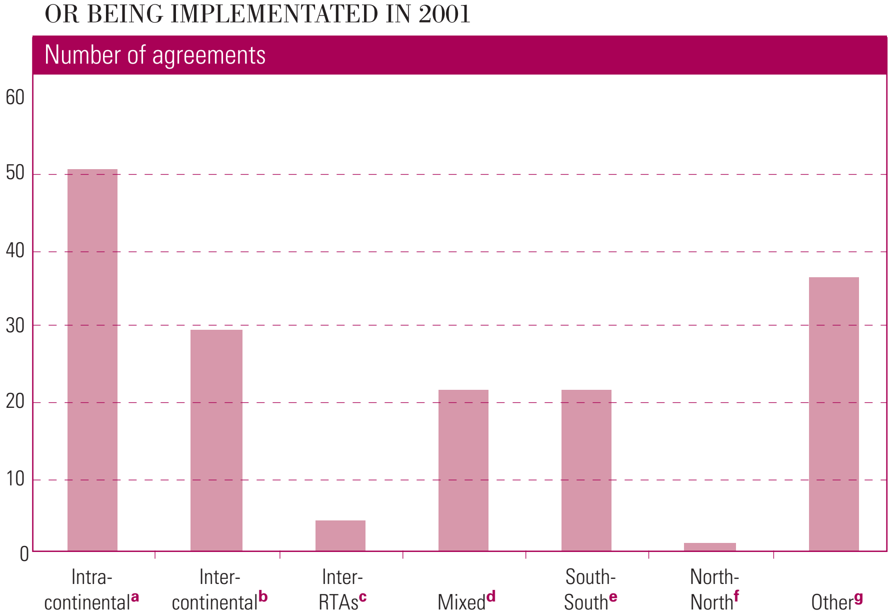
Almost all WTO Members are partners in at least one RTA, and many are partners in two or more. The number of RTAs under negotiation or different stages of implementation during 2001 was estimated at 79[39], compared to 68 in 2000.[40] Most of these are bilateral free trade agreements (FTAs) among countries in the same broad geographical region (see Figure II.6). There is, however, a tendency towards the formation of bilateral FTAs between countries belonging to different continents, especially between countries from Latin America and Asia.

Agreements involving developed and developing countries are a newer phenomenon. Among such mixed agreements, a major development in 2001 was the formal launch of negotiations on a Free Trade Agreement of the Americas (FTAA), linking 34 countries. Other free trade agreements continue to be implemented in the Americas, such as the North American Free Trade Area (NAFTA), sub-regional integration schemes (MERCOSUR, the Andean Community, CARICOM, and CACM) and a dense network of bilateral FTAs. Other interregional and intercontinental trade integration initiatives are also under way or concluded. The most notable are the Chile/Canada and the Mexico/European Union FTAs, the ongoing negotiations on FTAs between the European Union, on the one hand, and Chile and MERCOSUR, respectively, on the other hand, and the almost-concluded negotiations between Chile and the United States. A rising number of RTAs are planned or under negotiation in Asia, in particular involving Japan, which, until 2001, was among the few WTO Members not party to any RTA. Japan, like the Republic of Korea, has shifted its long-standing policy of only liberalizing trade in a multilateral framework in order to initiate negotiations on an FTA with Singapore, and has formed a study group to consider the feasibility of FTAs with the Republic of Korea and Mexico. Singapore is also actively forging preferential bilateral trade links with Australia, Canada, and Mexico. The ASEAN countries are making progress in their sub-regional integration, as well as with their Bangkok agreement that aims at a free trade area.

Strengthening trade-related assistance to developing countries

Improvements in the implementation of the Integrated Framework for Trade-related Technical Assistance to Least Developed Countries (IF) in 2001 transformed the IF into a funded mandate and a viable mechanism for mainstreaming trade into national economic plans and poverty reduction strategies. There are four central elements in the revamped IF: (a) mainstreaming trade priority areas of action into national development plans and poverty reduction strategies; (b) improved governance, with the establishment of the IF Steering Committee and an expanded Inter-agency Working Group for improving coordination and transparency amongst donors, LDCs and the core agencies; (c) the establishment of the IF Trust Fund; and (d) coordination of trade-related technical cooperation within a coherent policy framework. A Pilot Scheme was launched in May 2001 in three countries and subsequently extended to eleven countries. Its objective is to assist LDCs, on a pilot basis, to develop a trade integration strategy through the preparation of a diagnostic study. The findings and policy recommendations of the study will form the basis for incorporating trade policies and priorities into national development strategies, as well as for an action plan for technical assistance to overcome constraints to trade development and integration into the global economy. The Doha Ministerial Declaration draws attention to the pressing need of "addressing supply-side constraints of LDCs and extension of the [IF] model to all LDCs". The renewed collective commitment on the part of the LDCs, donors and the core agencies reflected in the adoption of the new arrangements augurs well for meeting this challenge.

Figure II.6.
REGIONAL TRADE AGREEMENTS UNDER NEGOTIATION OR BEING IMPLEMENTATED IN 2001



Source: Based on Cernat, Lucian (2002) "Assessing regional trade agreements: same issues, many metrics: policy issues" in *International Trade and Commodities,* Geneva: UNCTAD, forthcoming.

a Agreements between countries belonging to the same geographical region.
b Agreements between countries on different continents.
c Trading arrangements between two or more existing RTAs.
d Agreements involving developing and developed countries.
e Agreements involving only developing countries.
f Agreements involving only developed countries.
g Agreements involving one or more economies in transition.

Doha: The new WTO work programme

On 14 November, WTO Members agreed in Doha to launch "a broad and balanced work programme which includes an expanded negotiating agenda and other important decisions and activities necessary to address the challenges facing the multilateral trading system". The agenda contains three types of future actions: topics for immediate negotiations; topics for future negotiations that are subject to 'explicit' consensus among WTO Members on modalities, to be decided at the Fifth Ministerial Meeting (scheduled for 2003); and issues for further examination in relevant WTO bodies.

The first category includes negotiations on agriculture, services, industrial goods, environment, WTO rules regarding anti-dumping, subsidies and countervailing measures, dispute settlement, regional agreements, and fisheries subsidies. The overall conduct of negotiations will be managed by a Trade Negotiations Committee that is to begin work by 31 January 2002. According to the Doha Ministerial Declaration, such negotiations are to be concluded by 1 January 2005. They are also to be covered by a "single undertaking", which means that all Members commit to all elements to be negotiated. Although the term "round" is not used, these procedural arrangements are typical of past GATT negotiating rounds.

Negotiations will continue in agriculture with a view to phasing out all forms of export subsidies and reducing other trade-distorting border measures and domestic support. On services, future negotiations will build on the progress achieved before the Doha meeting (see above). Countries are to submit initial requests for specific commitments by 30 June 2002 and initial offers by 31 March 2003. Immediate negotiations should also start on industrial goods, with the aim of reducing or eliminating tariff peaks and tariff escalation, as well as non-tariff measures affecting all products and, in particular, products of interest to developing countries.

Negotiations on trade-related environmental issues will address the relationships between WTO rules and multilateral environmental agreements. Negotiations should also aim at reducing or eliminating tariff and non-tariff measures on environmental goods and services.

The topics for future negotiations include investment, competition, government procurement and trade facilitation. Negotiations on these issues could be launched if a consensus is reached during the Fifth WTO Ministerial Conference on the modalities of the negotiations. The WTO Committee on Trade and Environment will also continue to work on all issues on its work programme, in particular those related to market access aimed at sustainable development, the relationship to the TRIPs Agreement, and labelling requirements for environmental purposes.

Many of the issues for further examination in WTO bodies are of special interest to developing countries, including the relationship between trade, debt and finance; transfer of technology; and problems faced by small and vulnerable economies. Of particular importance is a paragraph approving work on special and differential treatment of developing countries with a view to making such provisions "more precise, effective and operational". There are also frequent references to taking special account of the needs and capacities of developing countries, and to the provision of technical assistance for capacity building. The Ministerial Declaration also refers to the need for continuing WTO work with the Bretton Woods institutions "for greater coherence in global economic policy-making".

In addition to the Ministerial Declaration, Ministers also adopted the Decision on Implementation-Related Issues and Concerns. This brings further clarification and makes a series of recommendations with regard to provisions contained in GATT 1994, Agreement on Agriculture, Agreement on the Application of Sanitary and Phytosanitary Measures, Agreement on Textiles and Clothing, Agreement on Technical Barriers to Trade, TRIMS, Agreement on Rules of Origin, Agreement on Subsidies and Countervailing Measures, and TRIPS. It includes agreement to encourage accelerated liberalization of the textiles and clothing sector and a commitment to exercise restraint on the use of anti-dumping measures in the sector for two years after the full integration of the sector into the WTO. The mandates on the implementation issues contained in the Ministerial Decision have to be considered together with additional "outstanding" implementation issues identified by Member States and included in the Doha Work Programme.

The separate Ministerial Declaration on the TRIPS Agreement and Public Health acknowledges the right of developing countries to grant compulsory licences to domestic producers of generic drugs and thus to override patent rights in the event of public health crises and national emergencies. However, the issue of compulsory licensing as laid down in the TRIPS Agreement prevents countries from importing cheap medicines in such situations. Since this situation may negatively affect many developing countries, and LDCs in particular, the WTO Council for TRIPS was requested to find a solution before the end of 2002. It was also recommended that the transitional period for LDCs with respect to the treatment of pharmaceutical products under the TRIPS Agreements should be extended until 2016.

There was a separate decision to extend the transition period allowed under the WTO Agreement on Subsidies and Countervailing Measures (i.e., for industrial products) for developing countries to phase out export subsidies from 2003 to the end of 2007. Two further decisions were: (i) agreement on the waiver to allow the European Union to extend until the end of 2007 unilateral preferences under the Cotonou Agreement for African, Caribbean and Pacific (ACP) countries (the "EU-ACP Partnership Agreement"); and (ii) acceptance of EU transitional regime for banana imports.

The accession of China to the WTO was also formally approved during the Conference. WTO accession is expected to have important implications for China, but also for third countries. Overall, the Chinese economy is expected to draw significant benefits from the WTO accession, largely as a result of increased competition and FDI flows, as well as protection under WTO rules from arbitrary actions by other WTO Members. However, as domestic protection is reduced in accordance with the agreement on WTO accession, the Chinese agriculture and automotive sectors are likely to be negatively affected in the short term, because of their low levels of international competitiveness. Another important aspect of liberalization will be the likely positive impact of WTO accession on textile exports from China.

INTERNATIONAL FINANCIAL COOPERATION

International Conference on Financing for Development

Preparations for the International Conference on Financing for Development to be held in Monterrey, Mexico in March 2002 gathered momentum in 2001. In January, the Secretary-General issued a report containing proposals for consideration by the Conference, prepared by an interagency team that included staff of the IMF, the World Bank, WTO and several parts of the United Nations.[41] This report was a main focus of discussion of the Preparatory Committee for the Conference in the first half of 2001. At mid-year, a high-level panel on Financing for Development, appointed by the Secretary-General and chaired by Ernesto Zedillo, former President of Mexico, issued its report.[42] In October, the Preparatory Committee considered a first draft of the "outcome document" for the Conference, a revised version of which is to be discussed by the Committee in January 2002.

Since their inception, the preparations for this Conference have actively involved "all relevant stakeholders". The World Bank, IMF and WTO have cooperated with the United Nations at both the staff and intergovernmental levels throughout. In November 2001, the Development Committee of the International Monetary Fund (IMF) and the World Bank focused its attention on the Conference and issued a statement containing its views on items on the agenda. In addition, the Bureau of the Preparatory Committee met with the Executive Boards of the IMF and the Bank and with the Trade and Development Committee of the WTO. Other intergovernmental organizations, non-governmental organizations and private-sector organizations have also participated intensely in all stages the process.

Implementing the Heavily Indebted Poor Countries (HIPC) Initiative

The enhanced HIPC Initiative is the primary international mechanism for the coordinated reduction of the debt service burden of 42 countries that meet specific debt criteria and have established a track record of reform and sound policies through IMF and World Bank-supported programmes. As of November 2001, 24 countries had reached the "decision point" under the Initiative, but only four countries (Bolivia, Mozambique, Tanzania and Uganda) had reached the "completion point". When the 24 decision-point countries complete the process, they will have received debt service relief amounting to some $36 billion. Already, owing to interim relief, most indicators of the debt burden for the decision-point countries have improved, although they are still high.

Under the HIPC process, Governments of HIPC countries are required to prepare Poverty Reduction Strategy Papers (PRSPs) in cooperation with civil society. The objective of the PRSP is to focus attention on poverty reduction, including ensuring the most effective use of resources freed up in HIPC debt reduction. As of November 2001, 38 countries had completed interim PRSPs and eight countries their first full PRSPs. The World Bank and the IMF are currently reviewing the experience with the PRSPs in consultation with all stakeholders.

Combating the financing of terrorism

The new global policy initiative to stop the flow of financial resources to terrorist organizations may affect the composition of financial flows in and out of developing countries and transition economies. This is because ordinary residents of these countries, as well as terrorists, use informal (and sometimes illegal) mechanisms for transferring funds. The new policies are expected to shift more transactions to the legal, traceable (and thus taxable) channels of the banking sector and this may have a dampening effect on their volume.[43]

On 28 September 2001, the United Nations Security Council adopted Resolution 1373, which requires that all Member States prevent and suppress the financing of terrorism. It also appointed a Committee to receive reports on compliance with the resolution within 90 days. In addition, the Financial Action Task Force on Money Laundering (FATF), on 30 October 2001, adopted eight new recommendations to criminalize the financing of terrorists and their organizations. It has requested all countries to undertake an immediate self-assessment against the new recommendations, which could assist the Security Council in evaluating compliance with Resolution 1373. In addition, FATF has decided to revise its 40 recommendations issued in April 1990 to make the international legal framework for combating the financing of terrorism more operational.

Fighting cross-border money laundering and terrorist financing involves law enforcement, financial supervision, international and inter-agency information sharing and coordination. It requires a collaborative approach, with every partner concentrating on the activities within its mandate and expertise. It was in this spirit that the International Monetary and Financial Committee (IMFC) of the Board of Governors of the IMF endorsed, at its meeting in November 2001, an action plan to intensify IMF involvement in this area. It envisages, among other steps, enhancing the Financial Sector Assessment Programs (FSAP) and Offshore Financial Centre assessments to cover money laundering and terrorist financing. The Committee also called on all countries to set up financial intelligence units (FIUs) for information collection and analysis on related issues and to promote cooperation among these units, building on the work of the Egmont Group, established in 1995 as an informal association of FIUs in the fight against money laundering. Countries were urged to implement these measures as soon as possible, preferably by 1 February 2002. The IMF is also called upon to enhance its collaboration with the FATF to develop a global standard to be applied internationally on a uniform, cooperative and voluntary basis.

In addition, the finance ministers and central bank governors of the Group of 20 at its November 2001 meeting adopted a comprehensive action plan to deny terrorists access to their financial systems and to stop abuse of informal banking networks. The plan emphasized, among other measures, the promotion of international standards relevant to terrorist financing, money laundering, and financial sector regulation and supervision, as well as technical assistance to countries that need help in developing and implementing the necessary laws, regulations and policies.

Notes

1 An international multiplier of 1.5 is estimated for the imports of the United States. See "Global implications of the United States trade deficit adjustment", UN/DESA Discussion Paper No. 17, 2001 (available at www.un.org/esa/papers.htm).

2 The price for a 128-megabyte DRAM chip fell by over 50 per cent during the first three quarters of 2001, but began to pick up towards the end of the year.

3 ICT-related goods account for 30-70 per cent of these countries' total exports.

4 The share of the United States and Japan in these countries' total exports exceeds 30 per cent and a significant part is ICT-related. Intraregional exports account for about a third of their total exports.

5 The share of developing countries in world total exports increased from 25 per cent in 1990 to 34 per cent in 2000.

6 The OPEC target range refers to the price of the OPEC basket of oil, which is a calculated average and not a price observed in the markets. The OPEC basket price is usually around $1-1.50 less than the price of Brent oil.

7 In 1991, FDI inflows declined by $47 billion, or 23 per cent. They also declined in 1976, 1982, 1983, 1985 but never by as large an amount or proportion as in 1991.

8 For detailed account of trends and the impact of cross-border M&As on economic development, see UNCTAD, *World Investment Report 2000: Cross-border Mergers and Acquisitions, and Development* (United Nations publication, Sales No. E.00.II.D.20).

9 The data cover completed cross-border M&As deals involving more than 10 per cent equity acquisition only, provided by Thomson Financial Securities Company.

10 "M&A volume down almost a half in 2001", *Financial Times*, 10 December 2001.

11 Data from UNCTAD, cross-border M&A database. This figure represents deals concluded through the exchange of shares.

12 "Barely fast … hardly furious", press release of Thomson Financial, 3 July 2001 (www.tfibcm.com).

13 The six stock exchanges included are those in Frankfurt, London, New York, Paris and Tokyo and the Nasdaq. *Nihon Keizai Shimbun*, 2 October 2001.

14 The other means to finance FDI are loans from parent firms and commercial banks, and own funds. Japan, Ministry of Economy, Trade and Industry, *Dai 29-kai Wagakuni Kigyo no Kaigai Jigyo Katsudo* (Tokyo: Ministry of Finance Printing Bureau, 2001), pp. 166-172.

15 Estimates of FDI flows to developing countries are strongly affected by the geographical coverage of estimates made by different sources. For example, the Institute of International Finance estimates $130.2 billion in 2000 and $124.4 billion in 2001 in direct equity investments for 29 emerging countries, which include seven countries in Central and Eastern Europe (see IIF, "Capital flows to emerging market economies", 20 September 2001). In comparison, UNCTAD's estimate for developing countries is based on data on FDI covering all of Africa (except South Africa), Asia (except Japan and Israel), Latin America and the Caribbean, Oceania (except Australia and New Zealand) and some developing European countries, while that for Central and Eastern Europe is based on all economies of that region.

16 For example, the rank correlation between FDI inflows and GDP during 1998-2000 for 188 countries is 0.78.

17 A.T. Kearney, *FDI Confidence Index*, February 2001. This survey covers the 1,000 largest TNCs in the world, 29 per cent of which are based in North America.

18 Based on a survey of 129 TNCs conducted from May to September 2001 and updated by telephone interviews in November 2001 by UNCTAD, the Agence Française pour les Investissements Internationaux and Andersen Consulting.

19 Japan Bank for International Cooperation, "JBIC FY2001 survey: the outlook of Japanese foreign direct investment", 13 November 2001. The survey covered 501 manufacturing firms surveyed in July/August 2001.

20 This applies to domestic investment as well. According to a survey by the World Economic Forum, 64 per cent of corporate executives do not expect to change their investment (domestic or foreign) plans, while 34 per cent expect a reduction by 10 per cent or more. "Slowdown and uncertainty: international economic networks in the wake of September 11, 2001", 5 October 2001, a survey of 90 Chief Executive Officers (CEOs) by the World Economic Forum.

21 The survey was conducted by JETRO for 667 Japanese TNCs (both manufacturing and services) in October 2001. The results were made available to UNCTAD by the JETRO International Economic Research Division.

22 "New A.T. Kearney survey captures CEO mood on global economic prospects in wake of the September 11 terrorist attacks", press release by A.T. Kearney on 9 October 2001.

23 Some companies are reported to have cancelled previously planned investment after the 11 September events (*Business Latin America* (EIU), 24 September 2001).

24 This is what a number of Asian countries did in partial response to the Asian financial crisis; see UNCTAD, *World Investment Report 1998: Trends and Determinants* (United Nations publication, Sales No. E.98.II.D.5.).

25 For a discussion of the factors driving cross-border M&As, see UNCTAD, *World Investment Report 2000*, op. cit.

26 International Monetary Fund, "Emerging market financing: quarterly report on development and prospects", 14 November 2001, p. 19.

27 Institute of International Finance, "Capital flows to emerging market economies", Washington, D.C., 20 September 2001, p.7.

28 International Monetary Fund, op. cit., 2001, p. 14.

29 If changes in country coverage and exchange rates and the effects of inflation are taken into account, the decline was 0.2 per cent.

30 A DDO gives IBRD borrowers the option of deferring the disbursement of a single-tranche adjustment loan for up to three years, provided that overall programme implementation and the macroeconomic framework remain adequate. See *Proposal to Introduce a Deferred Drawdown Option (DDO) for Use with IBRD Adjustment Loans* [R2001-0174], World Bank, 26 September 2001.

31 See Report of the Secretary-General on International trade and development (A/56/376) for a review of additional developments prior to the Fourth WTO Ministerial Meeting.

32 For a detailed analysis on the impact of the EU's Everything But Arms initiative on LDCs, see UNCTAD (2001) *Duty and Quota Free Market Access for LDCs: An Analysis of Quad Initiatives*, UNCTAD/DITC/TAB/Misc. 7, London and Geneva. See also Ianchovichina, Elena., Aaditya Mattoo, and Marcelo Olarreaga, "Unrestricted market access to sub-Saharan Africa: how much is it worth and who pays?", CEPR Discussion Paper No. 2820, 2001.

33 WTO document G/L/459.

34 An exception is Norway, which has eliminated all the restrictions due under the ATC (see G/L/459).

35 This is mainly because liberalization under the ATC is implemented on the basis of total volume of imports rather than value. This allows countries to fulfil the intermediary liberalization targets by starting with low-value added products, while pushing high-value added products (like clothing) towards the final date of ATC implementation.

36 Report of the Textiles Monitoring Body, WTO document G/L/475.

37 Bora, Bijit (2001), "Trade-related Investment Measures and the WTO: 1995-2001", *Policy Issues in International Trade and Commodities*, No. 17, Geneva: UNCTAD.

38 See also McCalman, Philip (2001), "Reaping what you sow: an empirical analysis of international patent harmonization", *Journal of International Economics* 55: 161–86.

39 Cernat, Lucian (2002), "Assessing regional trade agreements: same issues, many metrics", *Policy Issues in International Trade and Commodities*, Geneva: UNCTAD, forthcoming.

40 See WTO (2000) "Mapping of regional trade agreements: Note by the Secretariat", WT/REG/W/41, 11 October 2000.

41 See Report of the Secretary-General to the Preparatory Committee for the High-level International Intergovernmental Event on Financing for Development (A/AC.257/12).

42 See Letter dated 25 June 2001 from the Secretary-General to the President of the General Assembly (A/55/1000).

43 This notwithstanding, the formal banking systems and nonbank financial institutions that are used for commercial transactions may also be used as channels for terrorist-related transfers.

CHAPTER III: REGIONAL DEVELOPMENTS AND OUTLOOK

After a generally positive year for many of the world's economies in 2000, there was an unexpectedly severe and widespread deterioration in 2001, with prospects of only a limited recovery in 2002. The slowdown began in the developed economies, particularly in North America, but quickly spread around the world through trade, finance and investment links. Most developing countries were affected, some severely, but the transition economies less so. In 2002, most economies are expected to share in the modest improvement in growth, with some of the developing countries rebounding the most.

DEVELOPED ECONOMIES

Most developed economies began to decelerate in mid-2000 and their average GDP growth fell from 3.5 per cent in 2000 to less than 1 per cent in 2001. With Japan sinking further into recession and North America and Western Europe staging only a modest recovery, a further slight weakening is expected for the year 2002 for the group as whole.

The decade-long economic expansion in **North America** came to an end with declines in GDP in both Canada and the United States in the second half of 2001 (see table A.2). The terrorist attacks on the United States in September 2001 aggravated the weakening that had already occurred in both countries but, by the end of the year, there were some signs that the economic slowdown would end in the spring of 2002 and be followed by a recovery. GDP growth for the region is estimated to have fallen to 1 per cent in 2001 (compared to 4 per cent in 2000) and is forecast to be only about 1¼ per cent in 2002.

The terrorist attacks had a substantial economic impact. The consequences included not only the human losses and the destruction of physical capital in the United States but also the widespread disruption of economic activity and the further and steep decline in both consumer and business confidence worldwide (see figure III.1).[1] Growth of GDP in the United States is estimated to have been reduced by over one percentage point in the third and fourth quarters. The economic losses for Canada were also sizeable due to its proximity to and close economic linkages with the United States.

Although the economic repercussions of the incident persist, there were some positive developments by year-end. For example, monetary policy had become aggressively accommodative, expansionary fiscal measures were being implemented, energy and other primary commodity prices had softened considerably and equity markets had rebounded, although tentatively. These factors are likely to stabilize the slowdown in the first quarter of 2002, with consumer and business confidence recovering gradually. Business investment is expected to begin to recover in mid-2002, as adjustment of excess capacity ends and corporate profits start to improve. The policy stimuli are crucial for ending the recession, but a solid recovery will depend largely on both private consumption and business investment regaining their full strength.

Consumer spending is expected to grow only moderately in 2002, as its major underlying determinants –real income, household wealth and labour market conditions– are not expected to fully recover the momentum lost in 2001. Net household wealth declined in 2001, as equity prices, measured on an annual basis, dropped for the second consecutive year. Unemployment rates have increased and are expected to continue rising until mid-2002. Additionally, household saving rates, which were at historical lows in the United States before the recession, are expected to increase during the recovery, further moderating consumption spending.

The recovery of business investment is expected to lag the other components of domestic demand. After a continued decline during 2001, business investment is not foreseen to experience tangible growth until mid-2002.

Figure III.1.
CONSUMER CONFIDENCE IN MAJOR ECONOMIES, 1998-2001[a]

Sources: United States: The Conference Board; Japan: Economic and Social Research Institute; European Union countries: European Economy – Business and Consumer Surveys.

[a] For United States, measure is an index (1985=100); for Japan, measure is a composite index (percentage); for European Union, measure shows percentage of respondents to survey who expect an improvement minus percentage of those who expect a deterioration.

The upturn of the ICT sector from its protracted global consolidation is one key determinant of the growth of business investment and computer-related spending is not expected to regain its pre-recession peak level (in nominal terms) in the next few years. However, just as most analysts failed to anticipate the rapid innovation and diffusion of ICT in the late 1990s, it is difficult to foresee the end of the consolidation and even more challenging to predict the emergence of the next cycle of innovation in the sector. Towards the end of 2001, there were signs of a deceleration in writing off inventory and in shedding excess capacity in the sector, signalling that consolidation may be coming to an end.

The recovery of corporate profits will be another stimulus to increased business investment. Profits have been declining sharply since mid-2000, but are expected to recover in the second half of 2002. Lower prices of energy and other commodities, reduced interest rates, fiscal stimuli, and the shedding of excess labour should all contribute to the revival of corporate profits. The external sector is not likely to make a significant contribution to recovery in the United States, as no major economic region shows any signs of a forthcoming increase in demand for North American exports.

Inflation has been declining in North America since mid-2001, and this trend is expected to continue in 2002. Core inflation in the United States is estimated to have been 2.7 per cent in 2001 and is forecast to fall to 2.2 per cent in 2002. In Canada, inflation is expected to be below 2 per cent in 2002. In contrast, unemployment, which increased to 5.7 per cent in the United States and to 7.5 per cent in Canada towards year-end, is expected to rise in both countries in 2002 (see table A.1).

With the nominal policy-targeted interest rate standing at 1.75 per cent in the United States—the lowest in four decades—and at 2.25 per cent in Canada at year-end, the corresponding real interest rates are around zero. The aggressive monetary easing has already had some effects on the economy, especially in such areas as equity prices, household mortgage refinancing and sales of automobiles; more sectors are expected to benefit from the low interest rates over time. Policy interest rates in both economies are expected to remain at year-end levels until mid-2002. In case of worse-than-expected developments in the region, however, further easing is possible.

Fiscal policies are also expected to remain expansionary in 2002, even though some specific stimulus measures in the United States were still under debate in December 2001. Tax cuts were implemented in both economies during 2001 and an increase in military spending and in other areas has been built into the budget of the United States for the fiscal year 2002. As a result of the recession and the expansionary policies, fiscal balances in both Canada and the United States deteriorated in 2001, and a further worsening is likely in 2002.

In **Western Europe**, many economies, except the United Kingdom, had joined the global contraction by the end of 2001. The manufacturing sector led the weakness, depressed by declines in exports and investment, but a deceleration in the service sector intensified in the last quarter. This weakness is expected to extend into 2002, but growth will begin to rebound in the second quarter and to accelerate as the year progresses. On an annual basis, GDP in the EU is estimated to have grown by 1.6 per cent in 2001 and is forecast to increase at about the same rate in 2002.

The slowdown in Western Europe was evident by the second quarter of 2001. Private consumption, while slowing, provided the main support for growth, despite the negative impact of both higher inflation and the stalling, or reversal, of the gains in employment in most countries. Consumption spending was also held back by the sharp decline in wealth as equity prices declined. Although historically less important in Western Europe than in the United States, wealth effects have increased in significance as share ownership has expanded across the region.

Rapidly decelerating world demand depressed European exports and discouraged investment expenditure more than expected. The relatively small share of Western European trade with the United States proved to be a poor indicator of Europe's insulation from the United States slowdown. Firstly, Europe's exposure was increased as the slowdown rapidly became more widespread. Secondly, if intra-company trade and trade in services are taken into account, the trade linkages are significantly stronger than indicated by merchandise trade data. Thirdly, the global decline in the ICT sector was exacerbated in Europe by the large debt incurred by many of the region's telecommunications companies in financing third generation mobile phone licenses. Additionally, investment by both European firms active in the United States and European subsidiaries of United States' companies was negatively affected by the poor profit prospects in the United States, while the declines in United States equity prices contributed to a substantial fall in prices on European stock exchanges during the year. As indicated above, the resulting wealth effect was one of the factors that depressed consumption expenditure. Finally, the external shock hit some countries particularly hard. This was especially true of Germany which, due to its size and the strength of its regional linkages, subsequently magnified the deceleration by transmitting it to the other economies of the region.

In mid-2001, there were signs of an improvement: industrial production for both the EU and the euro area rose in August and retail sales moved up as well. However, the terrorist attacks in September turned the situation around and led to a sharp deterioration in manufacturing, service sector and in consumer confidence, as well as in business sentiment. Pessimistic assessments following a dramatic event often represent an overreaction, with subsequent moderation in the coming months, but these various measures of confidence all continued to fall until December 2001.

Meanwhile, the improving employment situation came to an end in 2001. As of October 2001, the rate of unemployment for the EU had stalled at 7.7 per cent for several months. At the same time, unemployment had risen in a number of member countries, such as France and Germany. Due to the cyclically lagging nature of unemployment, and the poor economic outlook over the next two to three quarters, it is likely unemployment will rise further during 2002.

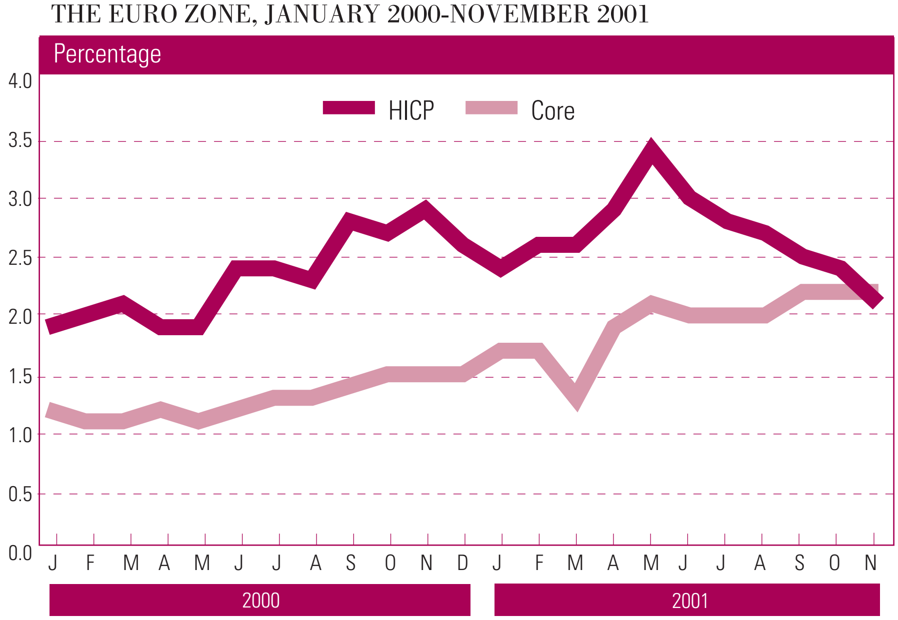
Inflation accelerated in the region during the first half of 2001, with the Harmonized Index of Consumer Prices (HICP) for the EU-12 rising to a peak of 3.4 per cent in May, while core inflation, which excludes energy, food, alcohol and tobacco, rose to 2.1 per cent. As these impulses worked their way through the system, inflationary pressures receded. The feed-through of earlier impulses, however, continued to push core inflation up (see figure III.2). In the outlook, continued economic weakness and the further dissipation of inflationary impulses from past supply shocks, together with the recent weakness in oil prices, should lead to a turnaround in core inflation and a continuation of the downward trend in HICP inflation, with both measures falling below 2 per cent by the beginning of 2002 and projected to remain below 2 per cent during 2002.

During the year, the European Central Bank (ECB) lowered its short-term interest rate four times, bringing the minimum bid rate to 3.25 per cent by the end of 2001 (see figure III.3). Despite this loosening, many observers have argued that the ECB has been too cautious. The policy environment has been highly contentious. On the one hand, both the HICP and core inflation have been above the euro area inflation target, justifying a cautious approach. On the other hand, since inflationary pressures were expected to recede in the near term, a more forward-looking approach might be seen as justifying a loosening of policy.

Policy at the end of 2001was stimulative but not overly so. Nominal short-term rates had not reached the lowest level achieved during the previous slowdown (see figure III.3). On the other hand, real short-term rates had been below 2 per cent since the second quarter of 2001 and fell to about 1.5 per cent by year-end. This is similar to their level during the previous slowdown but still higher than those in the United States. This differential may be appropriate, however, because the United States is at the centre of current economic difficulties. Nonetheless, with inflation expected to decline an additional half a percentage point over the next few quarters, nominal rates in Europe would have to be lowered further in order to maintain the current policy stimulus. The ECB is therefore likely to lower rates by another 50 bps by the end of the first quarter of 2002, which would bring the minimum bid rate to 2.75 per cent. This is expected to be the end of the easing cycle, with rates rising again in the second quarter of 2002

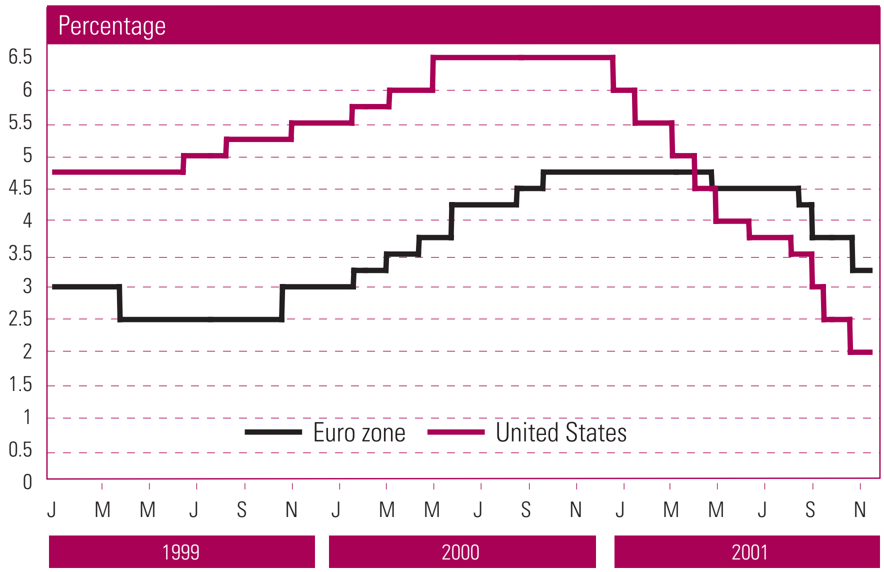
The economic slowdown has affected the fiscal position of most countries in the region. A number of fiscal stimuli were already in the pipeline during early 2001 and the current fiscal position is supportive of growth. There

Figure III.2.
ANNUAL RATE OF CHANGE IN CONSUMER PRICE INDEX IN THE EURO ZONE, JANUARY 2000-NOVEMBER 2001



Source: Eurostat

Figure III.3.
EURO ZONE AND THE UNITED STATES: POLICY INTEREST RATES, JANUARY 1999-NOVEMBER 2001



Sources: United States Federal Reserve Bank and European Central Bank.

seems to be little room for further stimulus but, since 11 September and given the expected further deterioration in growth, counter-cyclical fiscal policy has been actively discussed. Governments are likely to make maximum use of automatic stabilizers and avoid the introduction of new fiscal packages, although there are some exceptions.[2] Fiscal balances are therefore expected to continue to deteriorate into 2002, especially for the large countries but, as the recovery takes hold and, particularly in the medium term, further consolidation is expected.

On balance, the worsening economic conditions in Western Europe are expected to extend into the first quarter of 2002. However, net trade will begin to be less of a drag on growth, while domestic demand, supported by accommodatory fiscal policies and more stimulative monetary policy, will drive a modest rebound in growth in the second half of 2002.

Nevertheless, there are a number of reasons why the outcome may be less satisfactory. The possibility of continued slow growth in Germany is of particular concern. On the other hand, Germany could provide the key to a pickup in the euro area as a whole. In the past, the German economy proved to be highly responsive to external demand and monetary policy. Unemployment is another area of concern. Much of the improvement in consumer spending in Western Europe over the recent past has been rooted in the substantial and sustained improvement in labour markets. Even a small deterioration in employment could have a large negative impact.

The deepening slowdown in external demand since late 2000 has compounded many domestic structural problems in **Japan** and the economy is not expected to recover soon. Dragged down by a confluence of several adverse factors, GDP is estimated to have contracted by 0.7 per cent in 2001, while another decline of 1¼ per cent is forecast for 2002. Policy makers face a challenge in balancing apparently conflicting goals: economic recovery, a reduction in non-performing loans (NPLs), and structural fiscal reform. Measures for resolving bad loans and improving public finances may exacerbate the cyclical contraction in the short term. Meanwhile, various forms of monetary easing have so far had little effect in lifting the economy out of its deflationary trap.

The sharp decline in external demand has been the leading factor underlying the current contraction. The volume of Japanese exports is estimated to have dropped by 5 per cent in 2001, a marked contrast with the growth of 9.4 per cent registered in 2000. Due to the unfavourable outlook for global demand in the near term, Japanese exports are expected to remain depressed in 2002.

Additional weaknesses have emerged in other sectors of the economy. Business investment, for instance, which had been buoyed by the booming demand for ICT, has faltered. Business surveys in the second half of 2001 indicated that corporate investment plans for 2002 had been revised downwards because of the continuous decline in corporate profits and the consolidation in the ICT sector. Real business investment is expected to decline by 5 per cent in 2002, after an estimate of zero growth in 2001. Meanwhile, already sluggish household demand has weakened further due to the deterioration in both equity and labour markets. Finally, the large decline in government investment spending during the course of 2001 aggravated the situation. Government investment spending in real terms is estimated to have declined by 4 per cent in 2001, and further reductions are expected in the next two years.

The unemployment rate climbed to an historical high of about 5.3 per cent by the end of 2001, while the ratio of job offers to applicants declined steadily. Amid the ongoing corporate restructuring, the employment situation is expected to remain unfavourable in the short run.

A deflationary trend has persisted in Japan for the past three years. With a widening gap between potential output and real demand, the deflationary spiral will remain as the crucial policy challenge. In addition to weak demand, other factors, such as declining prices of imports, market deregulation, technological innovation, and streamlining of distribution channels, are likely to continue exerting downward pressure on prices.

Japanese monetary authorities took various unorthodox measures during 2001. These included shifting the target of monetary policy from the overnight interest rate to the Central Bank's liquidity balance on money market operations; using the CPI as the guideline for monetary easing, at least until a sustainable positive annual CPI rate prevails (although a formal inflation-targeting framework was not adopted); and increasing the Central Bank's outright purchases of long-term government bonds to ensure a smooth supply of liquidity. After 11 September, the Central Bank provided more liquidity by substantially increasing the Bank's outstanding balance and by reducing the discount rate to virtually zero.

While Japanese monetary policy is expected to remain accommodative in the outlook, views are split on how to make monetary policy more effective in reversing the deflationary trend. Some analysts believe that with nominal interest rates close to zero, monetary policy may have reached its limits, and the revival of the economy should rely on structural reforms. Others, however, suggest that the Central Bank still has room to stimulate the economy by resorting to more orthodox measures, such as an increase in outright purchases of long-term government bonds, open market purchases of commercial and corporate loans, and direct inflation targeting.

Since April 2001 (the beginning of fiscal year 2001), Japan has redirected the focus of its fiscal policy away from traditional stimulus spending towards structural reforms.[3] In the latest committed supplementary budget, it includes direct spending of only 2.5 trillion yen (about $20 billion) to be financed by the proceeds from the sales of shares of government-owned enterprises. With a cap of 30 trillion yen imposed on the issuance of government bonds, and a diminution of tax revenue because of a declining economic activity, fiscal policy is likely to remain austere in the near term.

Compared with many other developed economies, the economies of both **Australia** and **New Zealand** have weathered the global slowdown relatively well, but the adverse impact on their external sector and the effects of global contagion on confidence put more downward pressures on these economies towards the end of 2001.

In Australia, a recovery in housing construction supported domestic demand, and the weak Australia dollar partly held up the growth of exports. Nevertheless, because growth in many of its major trading partners was slowing, Australian exports weakened significantly at the end of 2001 and will remain weak in the first half of 2002. The Reserve Bank of Australia has been easing monetary policy and more cuts in interest rates are expected, given declining inflation and the large differentials with interest rates in the United States. GDP growth is estimated to have been about 2 per cent for 2001, and 2¼ per cent is expected for 2002.

New Zealand maintained strong export growth during most of 2001, particularly in value terms. A rise in international prices for its key export commodities (beef and diary products) in the first half of the year was the main reason, but the low value of the New Zealand dollar and the good economic performance of Australia also helped. As it approached year-end, the external environment became more adverse: international prices were falling, and tourism revenue was declining. GDP is estimated to have grown above 2½ per cent in 2001, but a slowdown is forecast for 2002.

ECONOMIES IN TRANSITION

The economies in transition weathered the global slowdown relatively well in 2001, achieving their second best rate of overall growth since transition started. Economic reforms in some Central and Eastern European (CEE) countries and the continued strength of the Russian economy were the major factors behind this outcome. Domestic demand remained robust in most countries and helped to sustain growth. Nonetheless, as export demand faltered and commodity prices dropped, growth decelerated and will likely slide further in 2002.

Economic growth in **Central and Eastern Europe** faltered only slightly in 2001, despite the weakening of economic conditions in the EU, the region's major trading partner. A pick-up in domestic demand—boosted by high export revenues in 2000 as well as by expansionary fiscal policies—supported production in many of these economies. Poland was an exception, with sluggish growth largely due to the stringent policies introduced to correct the macroeconomic imbalances of 1998-1999. Domestic demand will continue to be the main support for growth in the near future, buttressed by domestic macroeconomic policies.

Factors in addition to domestic demand explain the relative resilience of the region in the face of the global slowdown. Exports remained robust for a number of reasons: the dependence of these economies on exports to the United States is minimal and the share of ICT products in exports is also small; most CEE countries have diversified their export markets both within the EU and to CIS countries; and several years of foreign investment, combined with economic reforms, have raised the "quality competitiveness" of the region's products. Foreign capital inflows, particularly FDI, have been attracted by prospects of EU accession. These inflows, especially greenfield investments, continued in 2001 and contributed to the growth in fixed investment, as well as cushioning the region from the volatility of financial markets. Provided growth in the EU picks up by the second half of 2002 and domestic spending strengthens, GDP for the region is expected to grow by 3 per cent, a similar rate to 2001. On the other hand, if the contraction in the EU persists, growth in CEE will be dampened.

The countries of South-eastern Europe, with the exception of the Former Yugoslav Republic of Macedonia, registered positive GDP growth in 2001, despite adverse shocks. Ethnic tension in Macedonia—besides adversely affecting the country's GDP growth—threatened stability in the entire Balkan region. In Albania, energy shortages disrupted industrial production. For this subregion, additional pressure resulted from the drop in Turkish import demand, which particularly affected Bulgarian exports. Some acceleration of consumption and investment spending is expected in Bulgaria in 2002, while Romania is likely to benefit from fresh loans from multilateral creditors. In Yugoslavia, the industrial sector continues to stagnate due to persistent supply-side problems. Nonetheless, the substantial debt relief resulting from the renegotiation with the Paris Club should alleviate some of the country's constraints in the near term.

Inflation in most CEE countries continued to decelerate in 2001. In a few countries, inflation remained at double-digit rates for a number of reasons, including increases in administered prices and continuing relative price adjustments. Further disinflation in the region is expected in 2002.

High rates of unemployment, especially in rural areas, remain a serious problem for Bulgaria, Poland, Slovakia and most of the former Yugoslav states. Continued restructuring of many sectors of these economies (for instance, the energy sector in Poland), the harder budget constraints faced by domestic companies and increased labour productivity in the industrial sector augur poorly for a reduction in unemployment in the near term.

Macroeconomic policies in CEE in 2001 varied. Monetary policy was tightened in the Czech Republic in July 2001, following concerns about inflation, but was eased by the end of 2001. Interest rates were cut in both Hungary and Poland, in the latter by a total of 750 basis points by the end of November. Nonetheless, real interest rates remain high in Poland. In the weaker external environment, these countries would like to loosen monetary policy in 2002 as a stimulatory measure. The expected further moderation in inflation should provide some room for further monetary relaxation, but the extent of the easing will be limited by the continuing fiscal—monetary dilemma in most of these countries, as central banks feel compelled to offset potential inflationary pressures resulting from the expansionary fiscal stance. Romania and Yugoslavia already have stubbornly high inflation rates and are committed to tight monetary policies. Monetary easing will also be constrained by the need to maintain interest rate spreads between the region and the euro zone in order to attract and keep foreign capital. Thus, interest rates may not move much lower than their current levels, with the likely exception of Poland.

Parliamentary elections will take place in some of these countries in 2002, and this may have been one of the reasons for the strong fiscal expansion throughout the region in 2001. Although expansionary fiscal measures are often financed by non-inflationary means (such as privatization receipts in the Czech Republic), such expenditures still pose a threat to macroeconomic stability. The fiscal position, therefore, remains one of the vulnerabilities of these economies.

The economies of the **Commonwealth of Independent States** (CIS) have fared even better than those of CEE in the slowing global economy. The outlook remains positive, but the high dependency on commodity exports, particularly on oil, poses a risk for the region.

The three largest CIS economies (Kazakhstan, the Russian Federation and Ukraine) are expected to slow in 2002 but to maintain relatively high rates of growth (see table A.3). Assisted by favourable oil prices, the state of the Russian economy has improved considerably. Growth has been accompanied by fiscal consolidation, macroeconomic stability and a decline in capital flight. The Ukrainian recovery also looks more sustainable and broadly based, with an increasing contribution from sectors other than steel (in particular food and machinery production, construction and agriculture). Growing domestic consumption—reflecting rising real incomes and an improved employment situation—has driven economic activity, while investment has been strong in both economies. The investment climate in the Russian Federation is likely to improve further in light of increased political stability and further progress in reforms.

Strong growth in Kazakhstan, driven by the oil sector, will continue in 2002. Exports will rise due to the increased capacity provided by the Caspian Pipeline

Consortium (CPC) pipeline, which came on stream in September 2001, and by growing levels of FDI. The two other hydrocarbon-exporting countries of the region, Azerbaijan and Turkmenistan, are also expected to grow at a rapid rate, following strong performances in 2001. Investment in the oil sector will support growth in Azerbaijan, while Turkmenistan will benefit from continued strong demand from its major export partners, the Russian Federation and Ukraine.

Recent performance and prospects in the rest of the region vary. Two other commodity exporters, Kyrgyzstan and Tajikistan, recorded strong growth in 2001 due to recoveries in the production of gold and aluminum, respectively. However, with the drop in the prices of those commodities, growth in these economies will likely slow in 2002. In Georgia, GDP growth remained constrained by energy shortages, as well as insufficient investment and restructuring. Georgian output will be negatively affected in 2002 by the economic crisis and devaluation in Turkey, Georgia's major export market. Growth in Armenia is also expected to moderate in 2002 due to lower exports. Belarus, Uzbekistan and the Republic of Moldova were the poorest performers among the CIS countries in 2001. Falling investment rates and insufficient restructuring dampen the economic outlook for these countries.

Unemployment fell to 8.1 per cent of the labour force in the Russian Federation in September 2001, compared to 10.2 per cent a year previously. Ukraine also reported a significant drop in official unemployment. In other CIS countries, unemployment remains high, and small changes are difficult to interpret due to the limitations of the official data. For the first time since the Russian crisis in 1998, real wage rates increased substantially in most CIS countries in 2001. In the Russian Federation, for example, they rose by almost 18 per cent in the first seven months of the year.

Inflation in the CIS region continued to fall during 2001, as a result of tight monetary policies in most countries (with the exception of Belarus, Uzbekistan and Turkmenistan) and falling energy and food prices, the latter due to exceptionally good harvests in most parts of the region. In Belarus, inflation fell from the three- to the two-digit level. However, further improvement in this country is unlikely because of the Government's continued reliance on extra-budgetary funds to support economic growth. Inflation in the Russian Federation has also fallen but remains relatively high because of the Government's resistance to nominal appreciation of the currency, combined with insufficient sterilization of the large current-account surplus. Inflation in the Russian Federation should fall slightly in 2002 with the narrowing of the current-account surplus.

The relatively tight macroeconomic policies of 2001 are likely to continue in the region. Belarus, Turkmenistan, and Uzbekistan are exceptions to this trend, as they will rely on monetary expansion to finance state-sponsored projects and to subsidize state-owed enterprises.

Fiscal balances deteriorated in most CIS countries in 2001 due to lower oil and commodity prices. The Russian Federation, however, was able to maintain its budget surplus, while also fully servicing its foreign debt, including a $2.7 billion repayment to the IMF ahead of schedule. Its strong fiscal situation suggests that the country will also be able to service its debt in 2003, when payments peak at about $19 billion. In some of the CIS countries, however, debt-servicing continues to be a large burden on the Government's finances and a factor behind their persistently high fiscal deficits.

For several Central Asian countries, in particular Uzbekistan and Tajikistan, adverse developments in Afghanistan are a potential downside risk. Uzbekistan may, on the one hand, face a financial burden related to security spending but, on the other hand, is likely to benefit from increased levels of international assistance.

Economic growth in the **Baltic countries** exceeded 5 per cent in 2001 (see table A.3), with a strong export performance and a sharp increase in industrial output in the first half of the year. Towards the end of 2001, however, the global slowdown affected these countries and economic activity in the region weakened in parallel with the East European countries. As in the case of Eastern Europe, the main channel was weaker import demand from the region's main trading partners.

Growth is expected to decelerate to about 4 per cent in 2002. Lower export revenues will undermine economic performance, but industrial output is expected to continue to grow moderately. Being small open economies, all three Baltic countries have business cycles synchronized with those of the EU, but anticipated inflows of FDI will likely sustain investment and growth in 2002.

The fixed exchange-rate regimes in the Baltic countries require prudent fiscal policies, especially in the light of anticipated weaker budget revenues in 2002 due to lower export earnings and the implementation of some tax reforms, such as the reduction in corporate income tax in Lithuania. This situation will complicate planned spending associated with prospective EU and NATO membership.

DEVELOPING COUNTRIES

Growth in the developing countries fell to 2.3 per cent in 2001 from 5.8 per cent in 2000, abruptly halting their recovery from the crises of 1997-1998. The major reason for this outcome was the deterioration in the external environment; domestic factors had only a minor role in the majority of countries. All regions were affected by the global slowdown in one way or another. Countries that export ICT products suffered from the consolidation in the industry; countries that export commodities saw already low prices falling to even lower levels; and countries dependent on foreign finance experienced reduced inflows and higher costs of capital.

Growth is expected to recover to 3½ per cent in 2002, still well below the rate achieved in 2000 and the mid-1990s. The improvement will largely reflect improved domestic conditions, particularly in countries where agriculture generates a large share of GDP and in those few economies with leeway for policy stimulus. The external environment will provide little impetus because of the developed countries' slow recovery.

In **Africa,** growth in 2001, at 3.3 per cent, was almost unchanged from 2000 (see table A.5). Growth was supported by a recovery of agricultural output in several countries, although some others suffered from adverse weather conditions and lower agricultural output. Relatively high oil revenues supported domestic demand in oil-exporting countries. Meanwhile, the deepening global economic slowdown, reinforced by the terrorist attacks, weakened external demand, depressed foreign investor sentiment, reduced tourist arrivals, and lowered the prices of many commodities that the region exports. Political instability and violence, although reduced, continued to curtail economic activity in the region. In the outlook, another year of modest growth is expected, with GDP increasing by about 3½ per cent in 2002. The improvement primarily reflects domestic factors, such as more stable political conditions and continued increases in agricultural output, as well as sustained growth in oil-exporting countries.

The economies of North Africa are being particularly affected by the slowdown in the EU. Such countries as Egypt, Tunisia, and Morocco depend greatly on export demand, tourism receipts and capital inflows from the EU. In the case of Morocco and Egypt, devaluations in 2001 may partially offset the fall in external demand. The drop in air travel will reduce tourism receipts, while North Africa's status as one of the major recipients of FDI in Africa makes the subregion vulnerable to an expected decline in foreign investment flows. As a result, growth in Morocco and Tunisia is expected to decelerate and output in Egypt to increase only marginally in 2002.

Following two years of expanded spending financed by increased revenues from the oil sector, prospects for the oil-exporting countries in Africa in 2002 are mixed. Although still benefiting from considerable inflows of revenue, lower oil prices, OPEC quotas, and a less favourable foreign investor sentiment are likely to dampen growth in the larger oil-exporting countries. Some of the smaller oil-exporting countries are expected to fare better as they are not bound by OPEC quotas and foreign investment continues to be attracted by these countries' oil potential. For instance, increased output and exports are expected to sustain economic growth in the Sudan, which will also benefit from increased production of refined petroleum products.

In most non-oil commodity-exporting countries, growth is expected to improve in 2002. The decline in oil prices and a modest recovery in the prices of some key commodities, such as cocoa and cotton, should relax the import constraint in several of these countries. In such countries as the Central African Republic, Congo, Côte d'Ivoire, the Democratic Republic of Congo, Eritrea, Ethiopia and Guinea, moderating political instability or the cessation of violence should improve investor and consumer sentiment. Additionally, the resumption of official financial assistance to some countries will support increased public spending. Conversely, civil unrest may result from upcoming presidential and parliamentary elections in Kenya, Zambia and Zimbabwe, while the continuing land reform controversy in Zimbabwe is likely to have a destabilizing effect on travel, tourism and general economic activity in eastern and southern Africa in 2002.

Some countries, such as Benin, Ethiopia, Mali, Niger and Senegal, will benefit from debt relief under the Highly Indebted Poor Country (HIPC) debt initiative in 2002. In 2001, Mozambique and Tanzania became the third and fourth countries, respectively, to reach the HIPC "completion point". Mozambique will benefit from an estimated 73 per cent reduction in its external debt stock and a halving of its external debt servicing obligations. All HIPC beneficiaries will be able to free up budgetary funds for public expenditure and investment in accordance with the commitments undertaken in their Poverty Reduction Strategy Papers. The impact of the HIPC agreements should not, however, be over-estimated because several of these countries were in payment arrears, implying that the cash-flow relief will be less than appears from their original repayment agreements.

Among African oil-exporting countries, fiscal policies will remain relatively loose. In Egypt, financing of large infrastructure projects, pressure to maintain social spending, and payment of domestic debt arrears are expected to increase spending. In Nigeria, an oil-fuelled fiscal expansion is likely to maintain steam, while Algeria, in an effort to address social grievances, plans to increase public spending considerably in 2002.

In contrast, most African oil-importing countries have seen their fiscal positions strained over the past few years due to lower commodity prices and higher energy costs. This has imposed severe limits on public spending and has intensified efforts to increase fiscal revenues. Although no new shock is anticipated for the coming year, their fiscal situations are generally fragile. Many countries will continue to rely on budgetary assistance from external donors, with some relief expected from the implementation of the HIPC initiative in the countries concerned. Conversely, following several years of consolidation, fiscal policy in the Republic of South Africa will remain expansionary as the budget proposal for fiscal year 2002 anticipates increased social spending and infrastructure investment, as well as tax relief and incentive programmes.

Monetary policy is expected to remain tight in Africa, with a few exceptions. Most countries in the region aim their monetary policy towards maintaining a fixed or stable exchange rate against the euro, the dollar or a currency basket. For example, the two regional central banks in the CFA zone are expected to maintain tight monetary policy in order to keep inflation at low levels consistent with the exchange rate peg with the euro.

Economic growth in **East Asia** slowed down significantly in 2001 (see table A.5), with economies with a concentration on the ICT sector and a large exposure to the United States market suffering the most. Singapore and Taiwan Province of China fell into recession, while Malaysia was expected to be in the same situation by the end of the year. High oil revenues and the low value of the rupiah cushioned Indonesia, a more diversified net oil-exporting country, from a further setback. In such countries as the Philippines and Thailand, domestic demand buffered the export decline and provided some support to economic growth (see figure III.4). Across the region, private investment slowed faster than consumption, while increases in public spending in several economies were insufficient to offset the negative external shock. Weakening exports and domestic demand led to a slowdown in virtually all sectors, except for agriculture. The negative repercussions of the terrorist attacks on air transportation and tourism especially affected Malaysia, Singapore and Thailand.

By mid-2002, a rebound in exports and stimulative policies are forecast to lead to a modest recovery in most of these economies. Additional fiscal measures introduced in several economies after the terrorist attacks are providing some support to domestic demand. Towards the end of 2001, the Republic of Korea exhibited signs suggesting that the slowdown was decelerating as policy stimuli started to take effect and the slump in the ICT sector began to ease. More generally, the policy measures that have been adopted will not be, in themselves, sufficient to generate a solid recovery. Due to the region's heavy export dependence, a durable recovery will hinge primarily on a rebound in exports, which, in turn, depends crucially on the recovery in the major industrial countries—the United States, in particular—as well as in the global electronics market. The recovery, therefore, is unlikely to be strong because the upturn in the United States is expected to be modest, with no growth in its import demand forecast for 2002.

Reflecting the slump in the manufacturing sector and corporate consolidation, the unemployment rate surged in most East Asian economies during 2001. In Taiwan Province of China, the unemployment rate rose to record levels (about 5.3 per cent in October 2001) and it also increased in Hong Kong SAR, partially reversing some of the gains registered in 2000. In the case of these two economies, the continuing relocation of manufacturing to mainland China contributed to rising unemployment. In contrast with other Asian countries, unemployment fell in the Republic of Korea, despite the sluggish economy. This decline reflects, on the one hand, growth in the labour-intensive service sector and an increased number of part-time (usually temporary) workers and, on the other hand, some withdrawal of female workers from the labour force.

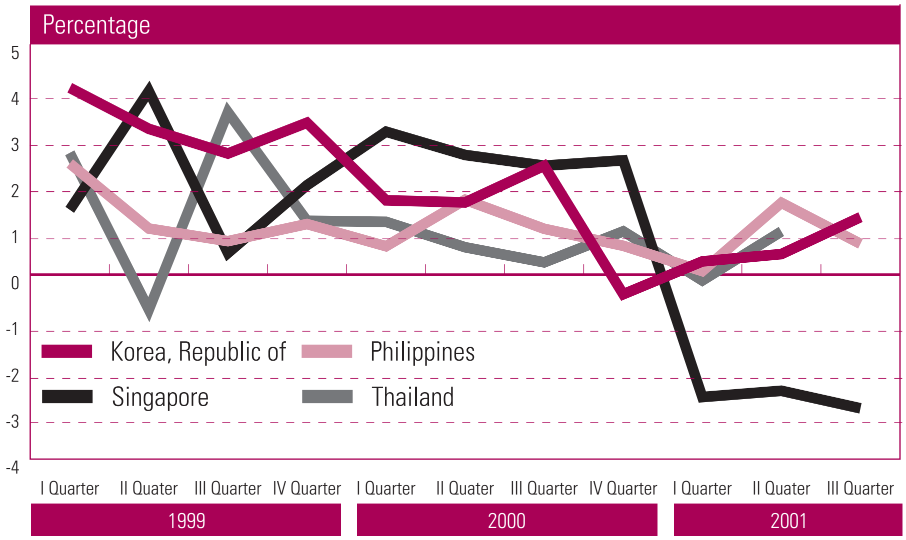
Economic policy in East Asia turned increasingly pro-growth during 2001 to cushion the effects of plunging exports: the Republic of Korea, Malaysia, Singapore, Taiwan Province of China, and Thailand introduced various stimulative fiscal measures during the year. As long as the slowdown continues and inflation remains benign, these economies are expected to maintain their expansionary policy stance.

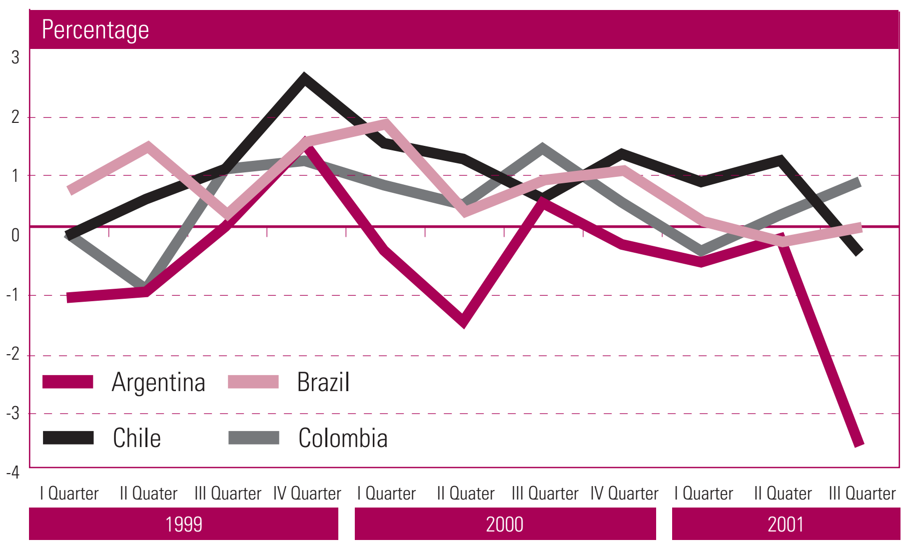
Among East Asian economies, interest rate cuts were particularly sharp in the Philippines, as the country could not use fiscal stimulus due to its large fiscal deficit. Most other economies gradually lowered interest rates or kept them low. After 11 September, in line with the cuts in the United States, some countries lowered interest rates further. In the near term, most East Asian economies are likely to maintain their accommodative monetary policy stance. There are, however, two exceptions. Indonesia kept monetary policy tight and raised interest rates in 2001 due to concerns about inflation and pressures on its currency. Thailand also raised its benchmark interest rate in an attempt to stabilize its currency. Both countries are expected to maintain these policy stances in 2002.

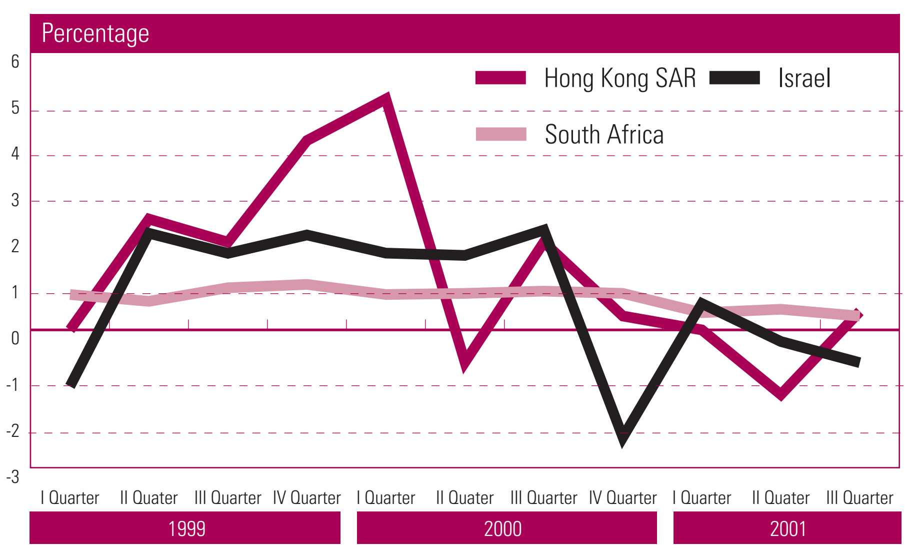
In contrast with East Asia**, China** grew by 7.3 per cent in 2001. Domestic demand, particularly public investment, buttressed economic growth, offsetting a negative contribution to GDP from net exports. Capital spending on technological innovations, infrastructure and housing were the leading sub-components. The outlook for the Chinese economy remains robust, with GDP expected to grow by 7¼ per cent in 2002.

The poor prospects for global trade in the near future imply that growth in China in 2002 will have to rely heavily on domestic demand, and policy measures in the short run are likely to continue to stress boosting domestic demand. Meanwhile solid growth of consumer spending is expected to continue, even though it remains subject to a few potential weaknesses. The disposable income of rural residents—accounting for more than 60 per cent of

Figure III.4.
SELECTED DEVELOPING COUNTRIES: SEASONALLY ADJUSTED QUARTERLY RATE OF GROWTH OF REAL GDP, FIRST QUARTER 1999-THIRD QUARTER 2001







Sources: Asian Development Bank and national statistical offices.

total population—has increased more slowly than that of urban residents, with negative consequences for income distribution and demand. Additionally, the restructuring of the state sector has put pressure on the labour market, further reducing demand. In the longer term, however, the policy focus is expected to be on efficiency, or the quality of growth. Accession to the World Trade Organization (WTO), the staging of the Olympics in 2008, and the accelerating development of the inland areas in the west of China are expected to sustain strong growth of investment during the coming years.

Despite increased government spending over the past few years, China's fiscal position remains sound. Fiscal policy is expected to remain expansionary in 2002. Meanwhile, monetary policy has been accommodative, with interest rates having been maintained at low levels since mid-1999. Further monetary easing is expected, but the challenge will be to continue reforming the financial sector so that the effects of monetary easing can be fully channelled into the real sectors.

Growth in **South Asia** slowed—albeit less dramatically than in East Asia—to 4.6 per cent in 2001. While the main drag on growth during the year was the deteriorating external environment, domestic factors, such as political uncertainties, an increased oil bill, the fiscal debt burden, infrastructure bottlenecks and other structural problems also hampered growth. Additionally, poor weather hurt a number of countries, depressing agricultural output and constraining consumption early in the year. Barring further major exogenous shocks, GDP growth is expected to recover to around 5½ per cent in the region in 2002 (see table A.5).

Pakistan will continue to be vulnerable to the possibility of disruptions of economic activity and additional risks brought about by any persisting instability in neighbouring Afghanistan. Export orders have fallen, in part because of rising insurance costs. Moreover, any further need to host large populations of refugees or to maintain increased security costs will aggravate the country's already fragile fiscal position. For the region as a whole, workers' remittances, an important source of foreign exchange, may also be adversely affected. Additionally, weaker investor confidence will depress both FDI and other inflows of private external finance and create additional incentives for capital flight, leading to further pressures on the balance of payments.

There are, however, some offsetting factors. A number of countries that suffered a setback from adverse weather in early 2001 reaped more favourable harvests during the second half of 2001 and this will increase rural incomes and consumption. In some of these countries, growth will be supported by policy stimuli and increased foreign assistance—including preferential trade treatment, concessional finance and debt relief, this will be the case particularly in Pakistan. By reducing the import bill and inflation, lower oil prices will also be conducive to growth. Nonetheless, these external factors are likely to have only a modest positive impact on most of these countries in the near term and are unlikely to be sufficient to set the region on a sustainable recovery; strong export growth is also necessary, but is likely to prove difficult to achieve.

Fiscal policy in most South Asian countries has been expansionary, despite their large fiscal deficits and the need to improve their fiscal positions. Due to their slowing economies and the increased security requirements in the region, however, these countries are under pressure to increase public spending. The fiscal situations in India and Sri Lanka remain precarious, notwithstanding their reform efforts. They are aiming to reduce their budget deficits through increased revenues, but this is a difficult task in a slowing economy. Pakistan has been complying with IMF-agreed targets and is likely to receive substantial external support, including some debt forgiveness and concessional loans; this may ease the tightness in its budget and enable it to increase development spending, although not immediately.

Monetary policy in South Asia has responded to both inflationary and currency pressures as necessary. Several countries cut interest rates in the second half of 2001. Further monetary easing is possible if inflation and exchange rates remain stable.

Western Asia confronted three major adverse events in 2001, two of them home-grown. First, Turkey plunged into profound financial and currency crises, which took the economy into a deep economic recession (see table A.6). Second, the increased violence between Israel and Palestine continued unabated throughout 2001. It caused growth in Israel to decelerate sharply and the Palestinian economy to collapse. The human toll was high, physical infrastructure and housing were destroyed and the number of displaced persons rose. Third, oil output declined and oil prices weakened due to sluggish global demand. As a result, growth in the region decelerated from 6.3 per cent in 2000 to 0.8 per cent in 2001. The economic outlook for 2002 seems more favourable and growth is expected to accelerate to about 3½ per cent (see table A.5).

Much of this expected upturn reflects the recovery in Israel and Turkey. In Turkey, after a large devaluation of its currency, high interest rates, and a sharp contraction in credit provision due to the banking crisis, growth is expected to return in 2002.[4] Domestic demand will support the recovery, but investment will remain subdued. The sharp devaluation of the lira makes Turkish products very competitive in external markets so that exports should contribute to growth, despite the sluggish import demand from the EU—the country's largest export market. Tourism earnings, which grew strongly in 2001, are expected to decline in 2002 due to concerns generated by the terrorist attacks.

The increased violence and political unrest in Israel has had devastating effects on tourism and on unskilled-labour intensive sectors, such as agriculture and construction. The growth of exports (particularly of high technology products) decelerated and the economy entered a recession (see figure III.4). Growth is expected to pick up modestly in 2002, supported by expansionary macroeconomic policies, but this forecast is subject to considerable downside risks. Meanwhile, Palestine's economic prospects for 2002 remain bleak. With poverty rates having increased dramatically in 2001, domestic demand will continue to decline in 2002 as private and public consumption contract. As a result, the economic recession is expected to deepen, causing social conditions in the territories to worsen further.

Growth in the oil-exporting countries will depend on developments in both oil prices and quotas. Due to revised OPEC quotas, these countries' oil output is expected to be lower in 2002 and oil prices are forecast to decline further (see chapter II). Reduced oil revenues will constrain the growth prospects of the oil-exporting countries in the region. Nevertheless, growth in some of these countries will accelerate marginally due to the renewed vigour of the non-oil sector.

These countries are expected to increase public outlays marginally in 2002. Capital expenditures on infrastructure and industrial projects will expand, which in turn may crowd-in private investment. Monetary policy in most of these countries will remain unchanged in 2002, with the currency peg against the dollar supported by current-account surpluses and abundant foreign reserves and assets. Because of these pegs, interest rates in most of those countries have declined along with those in the United States and will continue to follow United States rates.

In **Latin America**, the sharp deceleration of the region's major economies and a deepening recession in Argentina reduced GDP growth to 0.5 per cent in 2001. Growth is expected to improve in 2002, but only to 1¼ per cent.

In 2001, the region suffered the impact of weakened external demand, a poorer external financial environment, including more costly finance and reduced capital inflows, and worsened terms of trade, as commodity prices fell. GDP growth decelerated sharply in Mexico, the Dominican Republic and other economies in Central America and the Caribbean, which have a large exposure to the United States market. Chile and Colombia were hard hit by the lower prices of copper and coffee, respectively (see figure III.4). Additionally, tight macroeconomic policies in some key economies of the region and a severe energy crisis in Brazil constrained domestic demand and contributed to the low growth. Among the larger economies, only Ecuador and Venezuela maintained or improved growth in 2001, in both cases supported by internal demand and relatively strong oil revenues.

The terrorist attacks adversely affected the region's economies, both by accentuating negative trends already present in the external environment and by further reducing opportunities for growth in the near term. For instance, the sharp decline in tourism is damaging Caribbean economies substantially. Such factors will continue to affect the region's economies well into 2002 when it is expected that the external environment will become more conducive to growth. Internal demand in most countries is likely to either grow only moderately or remain constrained due to conservative monetary and fiscal policies.

The outcome of the crisis in Argentina, which is now entering its fourth year of recession, is an important source of uncertainty for Latin America in 2002. The country fell into a vicious cycle of depressed internal demand, deflation and deep fiscal crisis, coupled with an unsustainable external debt and reduced international competitiveness. However, there were limited policy options under the existing monetary framework. Persistent declines in tax revenues amid a deepening recession meant that the zero-deficit budget target agreed with the IMF could not be met. This prompted the IMF and other international financial institutions to suspend disbursements to Argentina. Bank controls were imposed in order to safeguard the domestic banking system as deposits were withdrawn. A major reduction of the country's debt burden seems to be a necessary condition for Argentina to resume growth.

The Argentinean crisis has also resulted in rising sovereign debt spreads and exchange rate volatility across the entire region, with the Brazilian economy in particular feeling the effects of contagion, as the real depreciated sharply and financing costs increased. Nonetheless, as the crisis unfolded, the contagion in financial markets seemed to be contained. The Brazilian currency regained some of its value in November, while other countries in the region, Chile and Mexico for instance, were able to access capital markets successfully even as the Argentinean crisis intensified.[5] Nonetheless, the management and eventual solution of the Argentinean crisis will influence external financing conditions—and therefore growth prospects, given the region's dependence on foreign savings—for all of Latin America in 2002.

Lower economic growth brought to a halt any improvement in employment in the region in 2001. High unemployment remains a key factor behind weak internal demand in countries across the region. In countries such as Argentina, Colombia, and Chile, open urban unemployment is at least 15 per cent. Job losses have taken place in the Mexican export-oriented manufacturing sector, particularly during the second half of 2001, and have already started to spread to other sectors of the economy.

With the exceptions of Argentina and Brazil and, to a lesser extent, Mexico, monetary policies in Latin America were flexible in 2001. In the absence of internal inflationary pressures, they aimed to support more vigorous growth. While a tight monetary stance is likely to remain in place in Argentina and in Brazil for most of 2002, other countries are likely to take a more accommodative stance.

A number of economies in the region have adopted restrictive fiscal policies and these are expected to continue in 2002. Brazilian authorities, for instance, increased the primary deficit target to compensate for the negative impacts of the depreciation of the currency and of higher domestic interest rates on the cost of debt-servicing obligations. Argentina adopted a zero-deficit fiscal policy in July 2001, but it proved difficult to implement. The outbreak of the economic crisis in the country at the end of 2001 suggests that its fiscal policy will have to remain restrictive for some time to come.

Notes

1 For a United Nations assessment of the economic consequences of the attacks, see "Global economic slowdown aggravated by attacks on the United States", 11 October 2001 (available at www.un.org/esa/analysis)

2 For instance, France has already announced an employment programme.

3 For details, see *World Economic and Social Survey 2001* (United Nations publication, Sales No. E.01.II.C.1), p. 79.

4 Ibid., pp. 113-115, for an analysis of the Turkish crisis.

5 Chile's bonds were priced at 256 bps over 10-year United States' Treasury bonds, slightly above the rate for the country's previous 10-year bond sold in 1999. Mexico's bonds were priced at 347 bps over Treasuries that have a similar maturity date.

LIST OF TABLES

Table A.1.
DEVELOPED MARKET ECONOMIES: RATES OF GROWTH OF REAL GDP AND RATES OF INFLATION AND UNEMPLOYMENT, 2000-2002

Annual percentage change

	Growth[a]			Inflation[b]			Unemployment[c,d,e]		
	2000	2001[f]	2002[g]	2000	2001[f]	2002[g]	2000	2001[f]	2002[g]
Developed economies	3.5	0.9	¾	2.0	2.1	1½	6.0	4.5	5
United States	4.1	1.0	1¼	3.4	3.1	2	4.0	4.8	6¼
Canada	4.4	1.5	1½	2.7	2.7	1¾	6.8	7.0	8
Japan	2.4	-0.7	-1¼	-0.7	-0.4	0	4.7	5.0	6
Australia	3.3	1.9	2¼	4.5	3.5	2¼	6.3	6.7	6½
New Zealand	3.8	2.5	2	2.7	2.7	2¼	6.0	5.3	5¾
EU-15	3.4	1.6	1½	2.3	2.6	1¾	8.2	7.8	8
EU-12	3.5	1.6	1½	2.3	2.7	1¾	8.9	8.5	8¾
Austria	3.3	1.4	1¾	2.4	2.6	1½	3.7	3.9	4
Belgium	4.0	1.2	1½	2.5	2.6	1½	7.0	6.9	7
Finland	5.9	1.0	2	3.4	2.6	1¾	9.7	9.2	9½
France	3.4	2.0	1½	1.7	1.9	1½	9.5	8.9	9½
Germany	3.1	0.8	1	1.9	2.5	1½	7.9	7.8	8¼
Greece	4.1	4.0	4	3.2	3.5	3	11.4	11.2	11
Ireland	11.5	6.0	3½	5.6	5.2	3¾	4.2	3.8	4¾
Italy	2.9	1.8	1¼	2.5	2.8	1¾	10.5	9.6	9¾
Luxembourg	4.5	3.4	3¾	3.1	2.7	2¼	2.4	2.4	2¾
Netherlands	3.5	1.5	1½	2.5	4.5	2¼	2.9	2.5	2¾
Portugal	2.8	1.7	1½	2.9	4.3	2¾	4.1	4.2	4½
Spain	4.1	2.5	2	3.4	3.7	2½	14.1	13.2	13½
Other EU	3.0	1.9	2	2.6	2.1	1¾	5.5	5.1	5¼
Denmark	2.9	0.7	2¼	2.9	2.3	2	4.7	4.6	4¾
Sweden	3.6	1.2	1½	1.0	2.7	2¾	5.9	5.2	5½
United Kingdom	2.9	2.2	2	2.9	1.9	1½	5.5	5.1	5¼
Other Europe	3.2	1.4	1¾	2.1	2.4	2½	2.7	2.5	2¾
Iceland	5.0	1.5	-½	5.2	7.2	6	1.4	1.5	2½
Malta	4.7	3.0	2¼	2.4	2.5	2½	4.5	4.5	5
Norway	2.7	1.6	2½	3.1	3.2	3¾	3.5	3.5	3½
Switzerland	3.4	1.2	1½	1.6	1.9	1¾	2.2	2.0	2
Memo item:									
Major developed economies	3.4	0.8	¾	1.9	1.9	1¼	5.7	6.2	7

Source: UN/DESA, based on IMF, *International Financial Statistics* and OECD.

a Data for country groups are weighted averages, where weights for each year are the previous year's GDP valued at 1995 prices and exchange rates in United States dollars.
b Data for country groups are weighted averages, where weights for each year are 1995 GDP in United States dollars.
c Unemployment data are standardized by OECD for comparability among countries and over time in conformity with the definitions of the International Labour Office (see OECD, Standardized Unemployment Rates: Sources and Methods (Paris, 1985)).
d Data for country groups are weighted averages, where labour force is used for weights.
e Greece and Malta are not standardized.
f Partly estimated.
g Forecasts.

Table A.2.
MAJOR INDUSTRIALIZED COUNTRIES: QUARTERLY INDICATORS, 1999-2001

Annual percentage change

	1999 quarters				2000 quarters				2001 quarters		
	I	II	III	IV	I	II	III	IV	I	II	III
	Growth of gross domestic product[a] (percentage change in seasonally adjusted data from preceding quarter)										
Canada	4.8	3.3	6.5	5.1	5.1	4.7	4.9	2.6	2.5	0.4	-0.8
France	2.8	3.6	4.1	4.6	2.6	2.9	3.6	3.0	1.6	0.8	2.0
Germany	3.2	-0.4	3.6	3.6	4.1	4.9	1.2	0.8	1.6	-0.1	-0.4
Italy	1.9	2.3	3.0	3.8	4.1	1.1	1.9	3.3	2.7	0.0	0.8
Japan	1.9	6.3	-0.3	-5.8	10.0	0.5	-2.7	2.6	4.1	-4.8	-2.2
United Kingdom	0.4	2.3	5.1	3.2	1.6	3.4	2.8	2.0	2.8	1.7	2.4
United States	3.5	2.5	5.7	8.3	4.8	5.6	2.2	1.0	1.3	0.2	-1.3
Memo items:											
Major developed economies	2.8	3.2	3.7	3.4	5.6	3.6	1.1	1.8	2.2	-0.9	-0.8
Euro zone	3.2	2.0	4.1	4.1	3.6	2.8	2.4	2.4	2.0	0.4	0.4
	Unemployment rate[b] (percentage of total labour force)										
Canada	7.9	7.8	7.6	7.0	6.8	6.7	6.9	6.9	7.0	7.0	7.1
France	11.7	11.5	11.2	10.8	10.2	9.7	9.4	8.9	8.7	8.5	8.6
Germany	8.8	8.7	8.8	8.7	8.1	8.0	7.8	7.7	7.8	7.8	7.9
Italy	11.6	11.4	11.3	11.1	11.0	10.6	10.3	10.0	9.7	9.5	9.4
Japan	4.6	4.7	4.7	4.6	4.8	4.7	4.6	4.8	4.7	4.9	5.1
United Kingdom	6.4	6.1	6.0	5.9	5.8	5.6	5.4	5.3	5.1	5.0	5.1
United States	4.3	4.3	4.2	4.1	4.1	4.0	4.0	4.0	4.2	4.5	4.8
Memo items:											
Major developed economies	6.3	6.2	6.2	6.0	5.9	5.8	5.7	5.6	5.6	5.8	6.0
Euro zone	10.3	10.0	9.9	9.7	9.3	9.0	8.8	8.6	8.4	8.4	8.3
	Growth of consumer prices[c] (percentage change from preceding quarter)										
Canada	0.8	4.4	2.9	1.3	2.2	3.5	3.9	2.7	0.9	6.9	0.5
France	0.1	2.4	-0.3	1.7	2.3	2.3	1.3	1.7	-0.1	5.3	0.4
Germany	0.1	2.2	1.7	-0.1	3.5	1.5	3.4	0.9	4.3	4.1	0.6
Italy	1.4	2.3	1.8	2.7	2.5	2.9	2.4	2.9	3.4	3.5	1.4
Japan	-3.9	1.3	-1.2	0.0	-2.7	1.1	-1.0	0.7	-1.2	-0.3	-1.1
United Kingdom	-1.7	4.3	0.3	3.0	1.6	7.7	0.6	2.5	-0.5	5.1	0.1
United States	1.6	3.9	2.5	2.5	4.0	4.3	3.2	2.2	3.9	4.2	0.7
Memo items:											
Major developed economies	-0.3	2.9	1.1	1.5	1.8	3.1	1.8	1.7	2.0	3.2	0.2
Euro zone	1.2	2.7	1.2	1.2	2.7	1.9	4.2	2.3	2.6	5.3	0.7

Source: UN/DESA, based on data of IMF, *International Finacial Statistics;* Organisation for Economic Cooperation and Development (OECD) and national authorities.

a Expressed at annual rate (total is weighted average with weights being annual GDP valued at 1995 prices and exchange rates).
b Seasonally adjusted data as standardized by OECD.
c Expressed at annual rate.

Table A.3.
ECONOMIES IN TRANSITION: RATES OF GROWTH OF REAL GDP AND RATES OF INFLATION AND UNEMPLOYMENT, 2000-2002

Annual percentage change

	Growth[a]			Inflation[b]			Unemployment[c]		
	2000	2001[d]	2002[e]	2000	2001[d]	2002[e]	2000	2001[d]	2002[e]
Economies in transition	6.0	4.3	3¾	19.2	14.8	12¾	..	..	..
Central and Eastern Europe and Baltic States	4.0	2.9	3	12.2	9.1	7¼	..	..	..
Central and Eastern Europe	3.9	2.8	3	12.7	9.3	7½	..	..	..
Albania	7.8	6.8	6	0.0	3.0	3½	16.9	15.1	15
Bulgaria	5.8	3.5	4	10.4	7.3	5½	16.9	16.8	15¾
Croatia[f]	3.7	3.9	2¾	6.2	5.4	4½	22.6	21.5	20
Czech Republic	2.9	3.6	4	3.9	4.8	4¼	8.8	8.5	8¼
Hungary	5.2	3.7	3¾	9.8	8.3	6	6.4	6.5	6¾
Poland	4.0	1.7	2	10.1	5.6	4½	16.1	18.1	18½
Romania	1.6	4.3	3	45.6	35.0	26½	10.5	9.2	9
Slovakia	2.2	2.7	3½	12.0	7.4	6½	18.6	18.3	18¼
Slovenia	4.6	3.3	3¾	8.9	8.3	6½	12.0	11.1	11
The former Yugoslav Republic of Macedonia[f]	5.1	-4.0	2	10.6	5.8	6¾	44.9	43.0	42
Federal Republic of Yugoslavia	7.0	4.0	6	75.7	90.0	30	26.6	27.8	26
Baltic States	5.4	5.1	4	2.3	2.8	3	..	..	..
Estonia	6.4	4.3	4	4.0	5.6	4½	7.3	7.4	7¼
Latvia	6.6	6.5	4¾	2.6	2.6	3	7.8	7.7	7½
Lithuania	3.9	4.6	3½	1.0	1.4	2½	12.6	12.1	12
Commonwealth of Independent States	7.9	5.5	4¼	24.1	18.8	16¾	..	..	..
Armenia	6.0	5.5	6	-0.8	4.1	4	..	..	..
Azerbaijan	11.1	8.5	7½	2.0	1.6	2½	..	..	..
Belarus	5.8	2.5	2½	169.0	70.0	80	..	..	..
Georgia	1.8	3.5	4	4.0	5.5	4½	..	..	..
Kazakhstan	9.6	10.0	7	13.0	9.0	7	..	..	..
Kyrgyzstan	5.0	6.0	4	19.0	8.0	7	..	..	..
Republic of Moldova	1.9	5.0	3½	31.0	12.0	10	..	..	..
Russian Federation	8.3	5.2	4	20.0	18.5	16	..	..	..
Tajikistan	8.3	7.0	7½	24.0	40.0	12	..	..	..
Turkmenistan	17.6	16.0	12	7.0	11.0	15	..	..	..
Ukraine	5.8	8.0	5	28.0	12.3	11	..	..	..
Uzbekistan	4.0	4.0	3	25.0	26.0	22	..	..	..

Sources: UN/DESA and Economic Commision for Europe.

a Data for country groups are weighted averages, where weights for each year are the previous year's GDP valued at 1995 prices and exchange rates in United States dollars.
b Data for country groups are weighted averages, where weights for each year are 1995 GDP in United States dollars.
c Because of comparability problems, data for the Commonwealth of Independent States are not given.
d Partly estimated.
e Forecasts.
f For Croatia and The former Yugoslav Republic of Macedonia: retail prices are used for inflation.

Table A.4.
ECONOMIES IN TRANSITION: QUARTERLY INDICATORS, 1999-2001

Annual percentage change

	1999 quarters				2000 quarters				2001 quarters		
	I	II	III	IV	I	II	III	IV	I	II	III
	Rates of growth of gross domestic product[a]										
Belarus	0.7	3.1	2.2	7.2	6.5	2.3	6.4	7.9	2.2	4.2	..
Czech Republic	-2.0	-1.1	0.4	1.1	3.2	2.4	2.4	3.8	4.1	3.9	..
Hungary	3.2	3.3	4.2	5.9	6.5	5.6	4.5	4.2	4.4	4.0	..
Kazakhstan	-7.4	-3.9	6.3	15.3	9.4	11.8	11.0	6.5	11.2	16.6	..
Poland	1.6	2.9	5.0	6.2	5.9	5.0	3.1	2.4	2.3	0.9	..
Romania	-4.2	-3.0	-1.3	-1.5	1.2	2.0	2.2	1.3	4.8	5.1	..
Russian Federation	-2.7	2.2	10.8	10.5	9.0	8.6	8.8	6.8	4.9	5.3	..
Ukraine	-4.7	-1.6	0.2	3.1	5.5	4.5	5.7	6.5	7.7	9.1	..
	Growth of consumer prices[a]										
Belarus	248.2	311.5	345.1	275.6	227.4	196.1	175.8	124.0	83.3	70.6	..
Czech Republic	2.9	2.3	1.2	1.9	3.6	3.8	4.1	4.3	4.2	5.1	5.4
Hungary	9.6	9.3	10.8	10.9	10.0	9.2	9.9	10.5	10.4	10.6	8.7
Kazakhstan	-0.2	5.5	12.1	16.4	20.4	13.7	10.1	10.4	9.1	9.7	8.1
Poland	6.1	6.4	7.5	9.4	10.4	10.1	10.9	9.2	6.8	6.6	4.8
Romania	35.5	43.3	49.6	53.2	53.8	44.6	44.9	41.6	40.1	36.9	31.8
Russian Federation	102.7	116.8	98.1	47.5	25.4	19.9	18.8	19.8	22.3	24.5	21.1
Ukraine	21.2	25.4	26.0	18.7	25.1	27.4	31.1	28.9	19.4	14.5	8.9

Sources: UN/DESA and ECE.

[a] Percentage change from the corresponding period of the preceding year.

Table A.5.
DEVELOPING COUNTRIES: RATES OF GROWTH OF REAL GDP AND RATES OF INFLATION, 2000-2002

Annual percentage change

	Growth[a]			Inflation[b,c]		
	2000	2001[d]	2002[e]	2000	2001[d]	2002[e]
Developing countries[f]	5.8	2.3	3½	5.7	5.9	4
of which:						
Latin America and the Caribbean	3.9	0.5	1¼	7.4	5.6	4
Net fuel exporter	5.5	0.9	2	..	..	..
Net fuel importer	3.3	0.3	1	..	..	..
Africa	3.4	3.3	3½	5.6	7.2	7
Net fuel exporter	3.5	3.4	3½	..	..	..
Net fuel importer	2.9	3.2	3½	..	..	..
Western Asia	6.3	0.8	3½	18.3	18.3	19
Net fuel exporter	6.3	4.3	4	..	..	..
Net fuel importer	6.3	-4.4	2¾	..	..	..
Eastern and Southern Asia	7.2	3.5	5	1.7	3.0	0
Region excluding China	6.9	1.8	3¾	2.2	3.8	3½
of which:						
East Asia	7.3	0.9	3¼	1.7	3.6	3
South Asia	5.7	4.6	5½	4.0	4.3	4¾
Memo items:						
Sub-Saharan Africa (excluding Nigeria and South Africa)	2.6	3.3	4¼	10.5	11.0	10½
Least developed countries	4.7	4.8	5	5.6	6.8	7¼
Major developing economies						
Argentina	-0.5	-4.0	-4½	-0.9	-1.0	-1½
Brazil	4.5	1.5	2	7.0	6.5	4½
Chile	5.4	3.0	3¼	3.8	3.6	4
China	8.0	7.3	7¼	0.3	1.0	¾
Colombia	2.8	2.0	2½	9.5	8.0	7¾
Egypt	5.1	2.5	3	2.7	2.8	5
Hong Kong SAR[g]	12.1	0.0	1½	-3.7	-1.5	-1
India	6.0	4.7	5½	4.0	4.1	4½
Indonesia	4.8	3.0	3½	3.7	11.1	9½
Iran (Islamic Republic of)	6.1	4.2	3½	14.5	13.4	16
Israel	6.0	0.2	1¾	1.1	1.6	2½
Korea, Republic of	8.8	2.5	4	2.3	4.4	3
Malaysia	8.3	0.3	2¾	1.5	2.0	1¾
Mexico	6.9	0.0	1½	9.5	6.4	4¾
Nigeria	3.8	3.0	3	6.9	21.1	17
Pakistan	3.9	3.4	4¼	4.4	5.2	6
Peru	3.6	-0.5	3½	3.8	1.0	2
Philippines	4.0	3.0	4¼	4.4	6.1	5¼
Saudi Arabia	4.5	1.3	2½	-0.8	0.0	1
Singapore	9.9	-3.2	2	1.4	1.2	¾
South Africa	3.4	2.6	2¾	5.3	6.0	5¾
Taiwan Province of China	5.9	-2.5	3	1.3	0.3	1
Thailand	4.4	1.4	2¼	1.5	1.9	2¾
Turkey	7.1	-8.5	3¼	54.9	54.2	53
Venezuela	3.2	3.0	2½	16.2	12.0	12

Source: UN/DESA, based on IMF, *International Financial Statistics.*

a Data for country groups are weighted averages, where weights for each year are the previous year's GDP valued at 1995 prices and exchange rates in United States dollars.
b Data for country groups are weighted averages, where weights for each year are 1995 GDP in United States dollars.
c For Africa and sub-Saharan Africa, the Democratic Republic of the Congo is excluded.
d Partly estimated.
e Forecasts.
f Covering countries that account for 98 per cent of the population of all developing countries.
g Special Administrative Region of China.

Table A.6.
MAJOR DEVELOPING COUNTRIES: QUARTERLY INDICATORS, 1999-2001

Annual percentage change

	1999 quarters				2000 quarters				2001 quarters		
	I	II	III	IV	I	II	III	IV	I	II	III
	Rates of growth of gross domestic product[a]										
Argentina	-2.5	-4.9	-5.1	-0.9	-0.2	-0.4	-0.6	-1.9	-2.0	-0.2	-4.9
Brazil	0.7	-0.4	-0.4	3.5	5.3	4.4	4.2	3.7	4.3	2.1	0.5
Chile	-2.8	-3.7	-1.8	4.0	5.5	6.0	5.6	4.5	3.5	3.4	..
China	8.3	7.6	7.4	7.1	8.1	8.2	8.2	8.0	8.1	7.9	7.6
Colombia	-5.7	-6.8	-3.6	-1.0	2.4	3.4	3.1	2.1	1.8	1.6	..
Ecuador	-5.4	-7.2	-8.0	-8.5	-2.2	2.0	3.6	6.0	7.8	6.8	..
Hong Kong SAR[b]	-2.9	1.2	4.1	9.2	14.1	10.7	10.8	7.0	2.3	0.5	..
India	5.9	7.3	6.2	6.1	6.0	6.1	6.2	5.0	3.8	4.4	..
Indonesia	-4.1	3.5	2.4	5.0	4.2	5.2	4.4	5.2	3.2	3.5	3.6
Israel	1.7	2.7	3.4	4.7	7.7	7.2	7.7	3.1	2.4	0.5	..
Korea, Republic of	5.8	11.2	13.0	13.0	12.6	9.7	9.2	4.6	3.7	2.7	..
Malaysia	-0.9	5.1	8.8	11.2	11.7	8.0	7.6	6.3	3.1	0.5	-1.3
Mexico	1.8	3.1	4.3	5.2	7.7	7.6	7.3	5.1	1.9	0.0	-1.6
Philippines	1.6	5.0	3.0	4.6	3.5	3.2	4.7	4.0	3.2	3.2	2.9
Singapore	1.3	6.9	7.4	7.7	9.8	8.4	10.3	11.0	4.7	-0.9	-5.6
South Africa	1.1	1.5	2.6	3.3	3.3	3.5	3.4	3.2	2.8	2.5	1.9
Taiwan Province of China	4.2	6.4	4.7	6.4	7.9	5.1	6.7	3.8	0.9	-2.4	-4.2
Thailand	0.1	2.7	7.8	6.5	5.3	6.4	2.9	3.2	1.8	1.9	..
Turkey	-9.1	-1.7	-6.0	-3.4	5.6	6.4	7.8	8.3	-2.1	-8.9	-7.1
Venezuela	-8.5	-7.4	-4.3	-4.1	1.1	2.7	3.4	5.6	3.8	2.9	..
	Growth of consumer prices[a]										
Argentina	0.0	-1.1	-1.8	-1.8	-1.3	-1.1	-0.8	-0.6	-1.4	-0.1	..
Brazil	2.3	3.3	5.5	8.4	7.9	6.6	7.6	6.2	6.2	7.1	6.6
Chile	3.8	3.9	3.2	2.5	3.2	3.6	4.0	4.6	4.0	3.6	3.6
China	-1.4	-2.2	-1.2	-0.8	0.1	0.1	0.3	0.9	1.4	0.5	-1.0
Colombia	16.7	9.9	9.1	9.6	9.0	10.6	9.4	8.9	8.6	8.3	8.9
Ecuador	45.6	54.6	54.0	53.8	83.2	96.5	104.8	97.3	67.6	39.6	28.9
Hong Kong SAR[b]	-1.8	-4.0	-5.9	-4.2	-5.0	-4.5	-2.9	-2.5	-2.0	-1.4	..
India	9.0	7.1	2.8	0.5	3.7	5.3	4.1	3.0	2.9	2.7	..
Indonesia	55.9	30.9	6.6	1.7	-0.6	1.1	5.7	8.8	9.3	11.1	..
Israel	7.3	5.9	6.0	1.9	1.5	2.0	1.0	0.0	-5.7	-5.2	..
Korea, Republic of	0.7	0.6	0.7	1.3	1.5	1.4	3.2	2.9	4.2	5.3	4.3
Malaysia	4.0	2.7	2.3	2.1	1.6	1.4	1.5	1.7	1.5	1.6	..
Mexico	18.6	17.9	16.5	13.7	10.5	9.5	9.0	8.9	7.4	6.9	..
Philippines	10.0	6.8	5.5	4.5	3.0	3.9	4.5	5.9	6.8	6.6	6.4
Singapore	-0.7	0.0	0.3	0.5	1.1	0.8	1.5	2.0	1.7	1.7	..
South Africa	8.5	7.3	3.3	2.0	2.8	4.9	6.6	7.0	7.5	6.3	..
Taiwan Province of China	0.7	-0.1	0.3	0.0	0.9	1.4	1.1	1.5	0.6	0.0	0.0
Thailand	2.7	-0.4	-1.0	0.1	0.8	1.6	2.2	1.6	1.4	2.5	1.6
Turkey	64.4	63.7	64.9	66.1	68.8	61.7	52.7	42.3	35.6	52.3	..
Venezuela	29.1	23.9	22.2	20.1	18.2	17.1	15.6	14.2	12.6	12.4	12.7

Source: IMF, *International Financial Statistics* and national authorities.

a Percentage change from the corresponding quarter of the previous year.
b Special Administrative Region of China.

Table A.7.
WORLD TRADE: RATES OF GROWTH OF VOLUMES, 2000-2002

Annual percentage change

	Volume of exports[a]			Volume of imports[a]		
	2000	2001[b]	2002[c]	2000	2001[b]	2002[c]
World	11.5	0.8	2¾	11.3	0.9	3¼
Developed economies	10.3	0.4	1½	9.1	0.3	2
of which :						
North America	9.9	-2.7	½	11.8	-3.8	-½
Western Europe	10.6	2.8	2½	7.6	2.7	3½
Japan	9.4	-5.0	-2	10.9	0.3	-¼
Economies in transition	16.1	8.4	7¾	15.0	11.3	9½
Central and Eastern Europe	20.5	11.2	10½	15.2	11.3	10
Commonwealth of Independent States	10.0	5.0	4	15.0	12.0	8
Developing Countries	13.7	0.5	5	16.8	0.8	5¼
Latin America and the Caribbean	11.0	2.5	5	14.0	3.0	6½
Africa	7.3	2.5	3¾	7.5	4.6	4
Western Asia	-19.9	-4.0	½	20.2	0.3	4
Eastern and Southern Asia	21.5	0.3	5½	18.3	-0.4	5¼
China	31.0	5.0	8	31.0	11.3	10

Sources: United Nations and IMF.

a Growth of country groups are weighted average, where weights for each year are the previous year's trade valued at 1995 prices and exchange rates in United States dollars.
b Partly estimated.
c Forecast, partly based on Project LINK..

Table A.8.
COMMODITY PRICES, 1999-2001

Annual percentage change

	1999	2000 quarters				2001 quarters		
		I	II	III	IV	I	II	III
Combined index, non-fuel commodities								
Dollar	-14.2	-1.9	2.6	5.3	1.9	1.6	-1.3	-4.7
SDR	-14.4	-0.4	3.9	8.8	9.2	8.6	4.2	-1.6
Food and tropical beverages	-18.3	-7.3	2.3	6.8	4.6	7.9	2.3	-1.3
Tropical beverages	-20.9	-9.2	-11.7	-7.7	-26.1	-23.7	-20.9	-21.9
Cocoa	-32.1	-35.1	-19.0	-16.5	-13.3	19.9	13.4	12.0
Coffee	-23.2	-2.6	-14.1	-11.3	-35.4	-36.7	-27.6	-26.5
Food	-18.1	-6.9	6.1	10.1	12.8	15.6	7.4	3.1
Bananas	-9.9	1.3	-2.1	-11.7	2.9	20.7	35.9	81.6
Maize	-5.5	1.5	3.2	-9.9	1.1	3.9	-0.9	12.2
Rice	-18.6	-14.2	-16.5	-24.9	-17.8	-24.1	-19.5	-7.9
Sugar	-30.0	-23.5	23.8	69.1	59.2	83.7	28.5	-18.5
Wheat	-10.9	-7.2	0.6	2.9	18.8	18.1	15.0	7.6
Vegetable oilseeds and oils	-23.3	-24.2	-20.6	-19.0	-25.1	-23.5	-21.5	9.0
Palm oil	-35.0	-39.1	-26.5	-14.6	-29.7	-27.3	-26.8	10.6
Soybeans	-16.9	1.9	11.5	2.5	4.3	-5.9	-16.6	3.0
Agricultural raw materials	-10.3	-7.6	-3.5	5.3	3.0	3.6	0.0	-5.0
Cotton	-18.6	-5.8	1.3	16.9	39.7	12.8	-16.9	-28.1
Rubber	-12.6	6.3	14.7	17.7	-4.7	-14.2	-12.4	-10.3
Tropical logs	-7.2	-12.1	-9.8	4.2	1.1	12.8	10.6	-1.6
Minerals, ores and metals	-1.8	24.6	15.5	9.2	2.0	-4.1	-4.5	-14.4
Aluminium	0.3	37.4	13.1	8.4	0.8	-4.0	1.6	-11.8
Copper	-4.9	27.6	18.6	11.5	6.3	-1.7	-5.0	-21.4
Iron ore	-9.2	2.6	2.6	2.6	2.6	4.5	4.5	4.5
Lead	-5.0	-9.8	-19.5	-6.3	-2.6	8.2	10.8	-0.2
Nickel	29.8	103.1	80.1	29.4	-4.4	-30.4	-29.1	-33.6
Phosphate rock	4.6	0.8	0.0	0.0	0.0	0.0	-2.3	-6.8
Tin	-2.5	8.2	-0.1	2.1	-7.1	-9.9	-9.6	-26.0
Zinc	5.1	13.8	11.2	3.9	-7.6	-9.8	-17.6	-29.8
Memo items:								
Manufactured export prices of DME	-3.1	-3.2	-2.2	-3.2	-6.4	-3.3	-4.4	-4.4
Real prices, non-fuel commodities	-11.4	1.3	4.9	8.8	8.9	5.0	3.3	-0.3
Crude oil (Brent)	39.2	141.4	73.2	49.2	23.0	-3.6	2.6	-16.8

Sources: UNCTAD, *Monthly Commodity Price Bulletin* and IMF.