Appendix
Regional Economic Prospects

East Asia and Pacific

GDP in the East Asia and Pacific Region is estimated to have increased by almost 8 percent in 2004 (for a second year), the strongest performance since the 1997–98 financial crisis. The regional boom has been led by extremely strong domestic demand and trade growth in China.

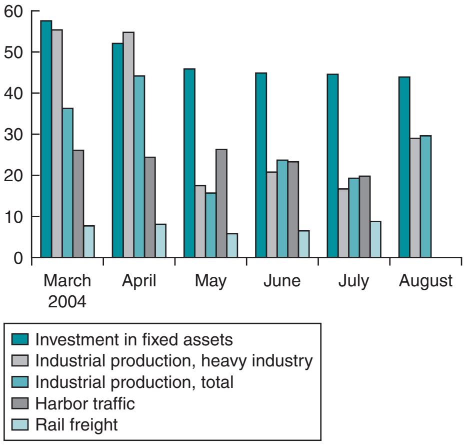
Chinese GDP is estimated to have increased by 8.8 percent, somewhat slower than in 2003. This slowdown reflects China's efforts to stave off an overheating of the economy and prevent an inflationary spiral that could derail long-term growth if recent hikes in food prices are passed through to wages and other consumer prices. Administrative controls on investments and restrictions placed on the issuance of new credits appear to be bringing expansion down to a more sustainable level. Investment growth slowed from over 40 percent to still high 20–30 percent rates between the first and third quarters (figure A1). In addition, the recent moderation in freight rates and the precipitous fall in October of the prices of copper, nickel, zinc, lead, and other commodities that are the building blocks of the Chinese boom appear to reflect perceptions that Chinese demand has been slowing (increases in Chinese demand represented 90 percent of the growth in global steel demand during 2003, and 66 percent of the increased demand for iron ore).

However, the effectiveness of these measures in slowing overall demand is less clear. Investment levels continue to exceed 50 percent of GDP, and retail sales volumes and the dollar value of imports are still expanding very rapidly.

Elsewhere in the region, GDP in 2004 is estimated to have increased by about 7 percent in Malaysia, by between 5.5 and 6.5 percent in the Philippines and Thailand, and by somewhat less than 5 percent in Indonesia. Buoyant consumer spending continues to make an important contribution in all these economies, while fixed investment spending, which has been subdued in the years since the financial crisis, has mounted a substantial recovery since late 2003.

Figure A1 A gradual slowing of China's growth

Selected indicators of activity, annual percent change



Source: National authorities.

Table A1 East Asia and Pacific forecast summary

Annual percent change unless otherwise indicated

	1990–2000[a]	2002	Est. 2003	2004	Forecast 2005	2006	2006–15[a]
GDP at market prices (1995 dollars)[b]	7.7	6.7	7.9	7.8	7.1	6.6	6.1
GDP per capita (dollars)	6.3	5.8	7.0	6.9	6.2	5.7	5.3
PPP GDP[c]	8.4	7.1	8.4	8.1	7.3	6.8	. . .
Private consumption	6.8	5.5	6.5	8.2	7.3	7.0	. . .
Public consumption	7.7	6.8	6.7	5.8	5.4	5.4	. . .
Fixed investment	9.0	13.1	18.6	16.4	9.5	8.1	. . .
Exports, GNFS[d]	11.6	14.8	20.8	20.9	13.2	11.0	. . .
Imports, GNFS[d]	11.6	15.1	23.3	24.4	15.6	12.1	. . .
Net exports, contribution to growth	0.3	0.5	−0.1	−0.7	−0.8	−0.4	. . .
Current account balance (% of GDP)	0.4	3.5	3.1	1.5	1.6	1.6	. . .
GDP deflator (median)	6.8	3.9	3.6	3.9	3.0	3.5	. . .
Fiscal balance (% of GDP)	−1.2	−3.4	−2.8	−2.4	−2.3	−2.2	. . .
Memo items: GDP							
East Asia excluding China	4.6	4.4	5.2	5.8	5.6	5.4	5.0

a. Growth rates over intervals are compound average; growth contributions, ratios, and the GDP deflator are averages.
b. GDP measured in constant 1995 dollars.
c. GDP measured at PPP exchange rates.
d. Exports and imports of goods and nonfactor services.
Source: World Bank.

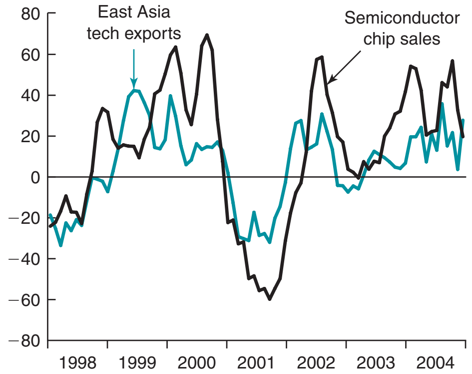
Output in the region is expected to slow through 2006, when it is projected to increase by 6.6 percent. By then Chinese GDP growth is forecast to ease to a more manageable 7 percent pace. It is assumed that administrative controls on investment and credit restrictions are calming the torrid pace of investment. As a result, the overall contribution of investment to GDP growth is projected to decline by more than 3 percentage points, with slower consumer demand also making a contribution as the pace of economic activity moderates.

Excluding China, GDP growth in the region is projected to remain robust, easing somewhat to around 5.5 percent by 2006 (table A1). This mainly reflects the slowing in economic activity among the region's major trading partners (China, Japan, and the United States) and, at the sectoral level, a weakening in world demand for high-tech products (G-3 orders for semiconductors fell 8.5 percent in the three months ending August 2004, as compared with the still robust growth of the second quarter) (figure A2).

This relatively benign outlook is subject to downside risks. In particular, overinvestment and excess capacity in China could lead to a sharp downswing in new investment, which would result in a much more abrupt slowdown than forecast. This slowdown would, in turn, have a significant impact on China's major trading partners in the region. In addition, should rapidly rising headline inflation

Figure A2 The global high-tech cycle may be easing

Selected high-tech indicators, rolling quarterly annualized rates, three month moving average, seasonally adjusted, percent



Sources: Semiconductor Industry Association, National sources, and World Bank.

feed through to core inflation, and the economy overheat, a much sharper policy response may be required. Finally, should oil prices not decline as projected in the baseline, the resulting adverse terms of trade consequences would act as a drag on growth within the region, because most of the larger economies in the region are significant net energy importers.

Over the long term, the East Asia and Pacific region is projected to continue generating strong growth. Since the 1997 financial crisis, GDP growth in the region has averaged 6.8 percent, and real per capita incomes have risen by almost 6 percent a year. While much of this strength reflects China's very rapid growth (8.1 percent on average), the rest of the region still enjoyed robust growth of 4.4 percent. Over the period 2006–15, regional per capita incomes are projected to continue rising rapidly, by about 5.3 percent a year in real terms.

Past reforms auger well for the future. Initiatives such as joining the WTO, the adoption of a much more welcoming attitude toward foreign capital, and efforts to recapitalize and restructure the financial sector in those countries most seriously affected by the 1997 financial crisis have underpinned growth in the recent period. They have done so by expanding markets and increasing the capital stock, which have allowed vast numbers of hitherto underemployed agricultural workers to be productively employed in the manufacturing sector, which increased both demand and output. At the same time, measures to consolidate public finances and reduce debt, including contingent liabilities, have also contributed to improved economic performance.

If real per capita incomes are to continue rising by the projected 5.3 percent a year, the reform agenda will have to be retained and expanded. Given the increased importance of financial markets and external investment, the region's growth prospects could be enhanced through further improvements to financial sector supervision and prudential rules, and by strengthening accounting and auditing standards. By raising investor confidence in regional markets, the domestic repercussions of higher world interest rates as well as the risk of contagion from financial turmoil elsewhere would be limited. Investment levels and growth would be further supported by strengthened insolvency laws, while public-sector governance reforms could significantly improve the state's ability to deliver key public goods and services. In China, clarifying the relations between the largely state-owned banking system and other state-owned enterprises would help reduce the likelihood of accumulating more bad loans.

Europe and Central Asia

Real GDP in Europe and Central Asia is estimated to have increased by 7 percent in 2004, a sharp acceleration from the 5.9 percent outturn in 2003. This strong performance outstrips the 2000 peak in growth of 6.7 percent. It marks a new record since the beginning of the transition period, with the commonwealth of independent states (CIS) showing the most rapid growth (table A2). The acceleration reflects several factors. Domestic consumption and investment in Russia and other CIS oil exporters were boosted by a surge in oil revenues, while the accession of a number of the region's countries to the European Union (EU) provided a further boost to investment demand and foreign direct investment inflows. Industrial production for the region as a whole was up an estimated 8.4 percent (figure A3). Strong domestic demand in Russia spurred increased imports from neighboring countries, mainly in the CIS, and the new EU members continued to increase their share of EU trade, reflecting past foreign direct investment from the EU. Overall, the region increased market share, and its exports grew almost 35 percent faster than world trade (figure A4).

Notwithstanding rapidly expanding production, fiscal deficits remain unsustainably high in a number of countries in central Europe. These deficits along with strong private-sector demand and higher oil prices have