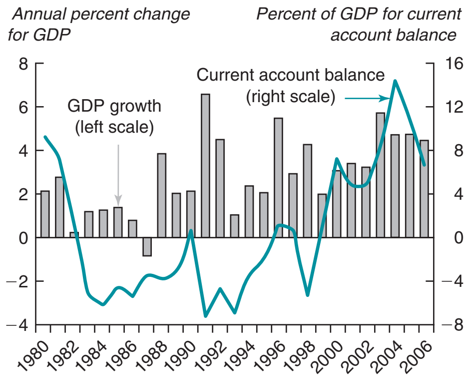
Figure A8 MENA: GDP growth and current account balance



Source: World Bank.

These countries, having signed EU-Mediterranean trade agreements, will benefit from preferential access to that market and can be expected to increase their market shares. However, countries in the region will also likely face increased competition from the new members of the EU, who are now benefiting from almost full market access and strong capital inflows. Meeting this challenge will require reinforced efforts to improve productivity and enhance the quality of regional export products.

In the longer-term, a return to lower oil prices and the need for enhanced reforms across the region will offer substantial challenges. How policymakers manage today's revenue windfalls will have an important long-run impact on the region. Current efforts to allocate surplus revenues to "Oil Funds" and to debt repayment should reduce upward pressure on regional currencies and protect the competitiveness of domestic non-oil firms (the "Dutch disease"). At the same time, such measures should help restrict the expansion of the domestic money supply and help insulate regional economies from overheating.

Longer-term prospects for the region will depend, to a large degree, on the success with which non-oil sectors can develop and flourish. It is important that continuing oil windfalls not delay needed reforms to the "investment climate" across the region, including economic structures and institutions that can promote more balanced growth, employment creation, and the achievement of longer-run poverty reduction goals.[3] Demographic pressures are mounting, and the need for job creation is urgent. At the same time, progress in these areas is complicated by the uncertainties regarding outcomes in the Iraqi conflict, which add an overlay of tension that is a concern for policymakers worldwide.

South Asia

GDP in South Asia is estimated to have slowed considerably in 2004, increasing by 6 percent, down from 7.5 percent in 2003. Much of the slowdown reflects a deceleration in agricultural output (up 3.4 percent) due to poor rainfall, while elsewhere, services, manufacturing, and export demand showed considerable strength. The brunt of the slowdown was felt in India, where the most serious impacts of the delayed onset of the monsoon were felt. In addition to the direct effect on agricultural output, the poor crop had important feed-through effects on rural private consumption, which in India accounts for about a quarter of GDP (over half of the population is dependent on the agricultural sector) (figure A9). India's services sector made strong advances, supported by productivity gains and greater market penetration, and the manufacturing sector continued to post high growth. Overall Indian GDP is estimated to have slowed from an increase of more than 8 percent in 2003 to one of about 6 percent in 2004.

Excluding India, growth in the region is projected to rise to 6 percent in 2004 from 5.6 percent in 2003, supported by robust manufacturing sectors in Bangladesh and Pakistan, and by strengthening services and agricultural sector growth in Nepal and Sri Lanka (table A5). For the subregion as a whole, strong external demand (exports were up 11 percent) and a general rise in remittances from abroad helped boost incomes and

Table A5 South Asia forecast summary

Annual percent change unless indicated otherwise

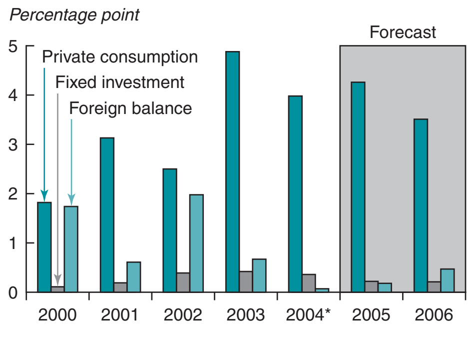
	1990-2000[a]	2002	Est. 2003	Forecast 2004	Forecast 2005	Forecast 2006	2006–15[a]
GDP at market prices (1995 dollars)[b]	5.2	4.6	7.5	6.0	6.3	6.0	5.5
GDP per capita (dollars)	3.3	2.8	5.8	4.3	4.7	4.4	4.1
PPP GDP[c]	5.3	4.6	7.6	6.0	6.3	6.0	. . .
Private consumption	4.2	3.9	7.6	6.2	6.6	5.4	. . .
Public consumption	5.2	3.5	3.8	3.4	2.2	2.1	. . .
Fixed investment	6.0	8.4	8.7	7.1	8.5	8.2	. . .
Exports, GNFS[d]	11.1	18.2	11.4	9.8	14.9	10.9	. . .
Imports, GNFS[d]	10.0	5.5	8.4	10.8	15.7	9.6	. . .
Net exports, contribution to growth	0.0	2.0	0.7	0.1	0.2	0.5	. . .
Current account balance (% of GDP)	−1.5	1.1	1.2	−0.5	−0.5	−0.1	. . .
GDP deflator (median)	7.9	3.6	5.2	3.7	5.3	4.7	. . .
Fiscal balance (% of GDP)	−11.0	−9.6	−8.2	−8.4	−7.8	−7.5	. . .
Memo items: GDP							
South Asia excluding India	4.4	4.5	5.6	6.0	5.6	5.8	5.3

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.

domestic demand, with private consumption accounting for virtually all of the increment to demand. In Pakistan, consumer demand was supported by robust increases in consumer credit and worker remittances. Rising investment rates reflected progress in structural reform and improved investor sentiment. Bangladesh's GDP growth is estimated to have been broadly stable between 2003 and 2004, although a sectoral breakdown indicates that this result reflects a combination of stronger manufacturing production (export-led growth) with some moderation of agricultural output (flooding and lower harvests). Growth in Nepal and Sri Lanka was held back by political tensions, which have cut into both tourism revenues and investor confidence. Meanwhile, donor assistance and relative peace, combined with a recovery in the agricultural sector after a prolonged drought, helped boost real GDP growth in Afghanistan by an estimated 16 percent, excluding the opium sector (which accounts for roughly a third of output).

There has been some building of inflationary pressures in the region. In India, producer prices were up 7.9 percent in September 2004 compared with 5.0 percent a year before, while in Pakistan producer inflation in the same period increased from 3.7 to 8.0 percent. Rising inflationary pressures mainly reflect higher food prices and some transmission of the rapid escalation of oil prices. The region's net current account surplus is expected to slip into a small deficit in 2004, due to the high energy import bill. However, robust external demand and continued market penetration are providing a substantial counterbalance.

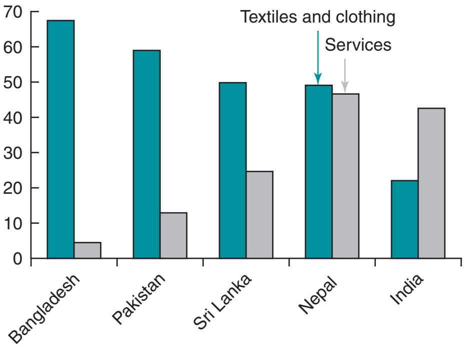
Figure A9 Contributions to growth



Source: World Bank.

Figure A10 Exports of services, and textile and clothing

Percent share of total merchandise exports



Note: Data observations are for 2002, with the exception of Nepal, which is for 2001.

Source: World Trade Organization.

Regional GDP is forecast to accelerate, expanding by 6.3 percent in 2005, before moderating somewhat in 2006. The acceleration is largely driven by an anticipated recovery of agricultural sector growth in 2005; it is forecast despite slower GDP and trade growth elsewhere in the world. The subsequent slowdown in 2006 is connected to a return to trend growth rates in the agricultural sector, which will moderate income and private consumption growth. Nonagricultural sectors are projected to continue expanding at a fast pace. Lower oil prices and better crops (assuming no further weather-related disruptions) should result in an easing of inflationary pressures in the near-term.

The slowdown in world trade growth should be reflected in regional exports, although South Asia is projected to continue increasing its share in both world goods and services markets. The entry of 10 new member countries into the EU should provide a fillip to regional exports. Many of these countries have large textile sectors, which now benefit from a more preferential trading regime and are likely therefore to increase their demand for inputs from South Asia. However, prospects for the South Asian textile sector remain clouded by the impending final phase-out of the Agreement on Textile and Clothing in 2005, which could have significant impacts on the balance of payments, production levels, and employment in a number of smaller countries in the region (figure A10).

Long-term growth in South Asia is forecast to average about 5.5 percent during 2006–15 as the contribution to growth from the private sector continues to rise. Buoyed by an ongoing consolidation of fiscal deficits (diminishing crowding out) and by rising private savings as dependency ratios decline, private investment is expected to play an increasingly large role in the region. The pursuit of trade reforms, banking-sector liberalization and re-regulation, privatization, and infrastructure development should all contribute to improving the investment climate, productivity growth, and ultimately, incomes. These product market reforms are being complemented by progress in raising education and skill levels and reducing infant mortality rates—factors that should further boost productivity. Moreover, demographics should help boost incomes, because despite declining infant mortality rates, falling birth rates mean that South Asian population growth is projected to decelerate and dependency ratios to decline over the forecast horizon. All of these factors suggest that per capita incomes will advance significantly in the coming decades, expanding by an average of 4.1 percent per year for the period 2006–15.

Policymakers in the region face a number of challenges to realize these high rates of growth. Substantial segments of the region's population remain vulnerable to weather patterns and natural disasters. Building capacity to mitigate their impacts without distorting economic incentives should be a priority. Recent peace agreements have eased regional tensions and are contributing to enhanced regional stability, which improves business confidence and increases intraregional trade. However, some international and domestic tensions remain, and the possibility of a deterioration in relations continues to present downside risks to growth outcomes and poverty reduction.

Sub-Saharan Africa

GDP in Sub-Saharan Africa grew by an estimated 3.2 percent in 2004, much faster than in the 1990s, but slower than almost everywhere else in the world. As a result, per capita incomes increased by only 1.1 percent in real terms, and rather than catching up, the region fell further behind both developed and other developing economies (table A6). Performance within the region was varied. Growth in oil-exporting countries was strong at 4.4 percent but was down substantially from the 7.9 percent pace recorded in 2003 as spare oilproduction capacity dried up. Nevertheless, high oil revenues helped fuel a 6 percent increase in personal consumption and investment demand in oil-exporting countries, factors that contributed to strong import demand and an overall negative contribution to growth from the external sector.

In South Africa, which accounts for almost 50 percent of area GDP, but only 11 percent of the population, growth continued to be dampened by the 40 percent effective appreciation of the rand (since 2002). As a result, exports were weak and imports strong so that despite robust domestic demand (up some 5 percent), GDP increased by only an estimated 2.7 percent. Most of the remaining countries in the region are oil-importers and are impoverished. These poor countries represent more than two-thirds of the population of the subcontinent but less than one-third of GDP; their output rose by an estimated 3 percent, up sharply from 1.7 percent in 2003. Strong agricultural and metal prices helped boost incomes in several countries and are reflected in a surge in consumption, investment activity, and imports. Overall, however, oil-importing Sub-Saharan countries suffered a 0.5 percent of

Table A6 Sub-Saharan Africa forecast summary

Annual percent change unless indicated otherwise

	1990–2000[a]	2002	Est. 2003	Forecast 2004	2005	2006	2006–15[a]
GDP at market prices (1995 dollars)[b]	2.3	3.1	3.0	3.2	3.6	3.7	3.5
GDP per capita (dollars)	−0.4	0.9	0.9	1.1	1.6	1.7	1.6
PPP GDP[c]	2.6	3.6	3.9	3.6	3.8	3.7	. . .
Private consumption	2.1	2.6	3.3	4.0	3.8	4.0	. . .
Public consumption	3.5	4.6	3.5	4.1	2.9	2.9	. . .
Fixed investment	3.4	5.3	7.3	7.2	5.0	5.0	. . .
Exports, GNFS[d]	5.1	0.0	2.3	2.0	6.5	6.4	. . .
Imports, GNFS[d]	5.8	3.5	5.3	6.9	6.6	6.4	. . .
Net exports, contribution to growth	−0.3	−1.3	−1.2	−1.9	−0.4	−0.4	. . .
Current account balance (% of GDP)	−1.6	0.4	−0.2	1.3	0.9	−0.3	. . .
GDP deflator (median)	12.8	5.9	4.2	4.1	4.0	4.0	. . .
Fiscal balance (% of GDP)	−4.4	−2.6	−2.7	−3.0	−2.9	−2.7	. . .
Memo items: GDP							
SSA excluding South Africa	2.9	2.7	4.3	3.6	4.0	4.0	. . .
Oil exporters	2.6	4.2	7.9	4.4	3.9	3.7	. . .
CFA countries	2.2	1.4	1.8	2.7	3.2	3.5	. . .

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.