

East Asia & Pacific

GDF 2003 Summary



Global themes

- Global growth is projected to accelerate steadily from 1.7% in 2002 to 2.3% in 2003 and 3.2% in 2004. Importantly, this view incorporates the effect of a relatively quick military conflict in Iraq. While very much a recovery, the expansion now underway is quite subdued by historic standards, especially given the sizeable stimulus from policy.
- The past few years has seen a fundamental shift in the pattern of private sector financing for developing countries, away from debt flows to equity-related FDI flows. The drop in debt finance has been partly driven by lower demand on the part of many developing countries seeking to lessen their vulnerability to swings in volatile debt finance, as well as a reduced supply of debt from banks and bondholders. The rise in FDI reflects greater optimism about globalization, the spread of FDI in services and heavy privatization.
- While this rotation from debt to equity should continue, the signs are that the low point in the current private debt cycle came in 2002Q3, and that net debt flows to developing countries are likely to turn positive again in 2003 for the first time in three years. While most likely, the overall buoyancy of FDI flows should not be taken for granted, however. Flows are already off their peak; privatization-related revenues have fallen sharply; and FDI in telecom and other areas of infrastructure has slumped. Moreover, rates of return on both FDI and in the corporate sectors of developing countries have generally fallen in recent years.
- Workers remittances have become an increasingly important component of global development finance, having risen to \$80 billion in 2002. They have some very attractive financial features. They are more stable than private debt flows and are less concentrated in the major middle-income countries than FDI flows.
- Aid flows to developing countries probably rose in 2002 and will continue to do so in 2003 and beyond, in line with the commitments made at the Monterrey Conference in March 2002. Emergency financial support (e.g. IMF) is likely to fall in 2003, on the presumption that no new major debt crises are in the offing. In between, official non-concessional lending (which includes the IBRD) is generally quite weak. Note that net IBRD lending was -\$4.1 billion in 2002 and is on track for an even larger decline in 2003.

Regional themes

- Regional GDP growth was 6.7 percent in 2002, up from 5.5 percent in 2001, which is impressive in view of the difficult external environment. Along with policy stimulus in other countries in the region, China's strong GDP growth (8 percent in 2002) boosted regional performance in 2002. Regional growth averaging more than 6.5 percent is expected for 2003-04, with China increasingly the dominant player in the regional economy.
- The external financing pattern of East Asia has been transformed in recent years. There have been sustained repayments of net private debt since 1997, totaling \$118 billion over that five

year period. The bulk of these repayments have been to commercial banks. The pace of debt repayment to private creditors slowed in 2002, however, when there were just \$6 billion of outflows. One reason for this is that borrowers in the region are taking the opportunity to issue newer debt at lower interest rates. In 2002, gross market issuance by East Asian borrowers rose by 61 percent. Net private debt repayments of \$5 billion are seen for 2003.

- FDI inflows to East Asia and the Pacific rose in 2002, growing by 17 percent to \$57 billion, up from \$48.9 billion in 2001. This was a result of the continuing surge in FDI to China. In 2002, China accounted for 92 percent of FDI to the region and for 37 percent of the developing countries' total. China became the largest FDI recipient in 2002, surpassing the United States for the first time, attracting a record high of \$52.7 billion. Buoyant FDI was driven by the new round of market liberalization, strong economic growth, and optimism following China's accession to the WTO. It shows little sign of slowing in 2003-04.
- The region is now entering a phase where it is making significant repayments to official creditors of large loans extended during the 1997-98 crisis. Some of these repayments reflect scheduled maturities; others reflect the desire to prepay. Net official flows debt flows to the region were negative in 2002 and will likely remain so in 2003.
- The combination of a current account surplus and high FDI is balanced by a continued huge accumulation of external assets by East Asian central banks and the private sector.

Other key regional points to note

- East Asia's external debt-equity ratios have declined since the crisis period. The dependence on external FDI-liabilities is highest in East Asia, mainly reflecting the influence of China, where the external debt-equity ratio has fallen below 50 percent. For developing countries as a whole, it is 200 percent.
- The high levels of external assets, especially in the form of foreign exchanges reserves, accumulated by East Asian countries in the wake of the Asian crisis have helped Asian countries shield themselves from the recent global economic downturn unlike other regions (particularly Latin America). With the external financing picture much stronger, East Asia weathered the 2001 global downturn relatively easily.
- Helped by greater domestic financial stability, local currency bond markets have grown considerably in recent years, helping to fill higher budget deficits, as well as to meet the region's needs for long-term infrastructure investment. The development of local bond markets also reflects efforts to reduce dependence on foreign-currency debt.
- China's reinvested earnings accounted for about one-third of net FDI inflows over the period 1996-2001, and its reinvestment rate (the proportion of FDI earnings reinvested) was the highest (81 percent over the period 1997-2000) among developing countries. This helps explain the high level of China's overall net FDI inflows.
- The Asian corporate sector has reduced its external financial vulnerability since the 1997-98 crises. It remains very heavily leveraged, however, and would be especially vulnerable to another sharp rise in domestic interest rates. Also, Asian corporate profitability remains low by international standards.

Table A.2 East Asia and Pacific outlook in summary, 1981–2003

Real economy (percent change, unless stated)	1981–90	1991–00	1997	1998	1999	2000	2001	2002e	2003f
Real GDP growth	7.4	7.7	6.4	0.6	5.6	7.1	5.5	6.7	6.4
Private consumption per capita	5.6	5.7	2.6	−0.5	4.6	6.0	4.1	6.0	6.0
GDP per capita	5.7	6.4	5.2	−0.5	4.5	6.0	4.6	5.7	5.5
Population	1.6	1.2	1.1	1.1	1.1	1.0	0.9	0.9	0.9
Gross domestic investment/GDP ^a	23.2	28.7	30.7	29.2	28.3	29.2	30.5	33.0	34.0
Inflation ^b	5.5	5.6	4.2	9.2	1.8	5.0	6.6	3.1	2.7
Central government budget balance/GDP	−1.3	−1.2	−0.7	−1.5	−2.3	−3.3	−3.3	−3.4	−3.3
Export market growth ^c	6.7	9.6	7.3	−1.2	7.7	14.1	−2.6	3.4	7.3
Export volume ^d	8.2	11.4	13.7	3.6	3.6	21.5	2.6	16.5	13.8
Terms of trade/GDP ^e	−0.3	−0.2	0.1	−0.3	0.4	0.2	−0.3	−0.4	−0.4
Current account/GDP	−1.4	0.5	1.1	4.4	4.2	3.6	2.6	2.5	2.2
Workers remittances (billions of dollars)	—	—	14.2	8.3	10.6	10.3	10.4	11.0	—
Memorandum items									
GDP growth: East Asia excluding China	5.7	4.6	3.3	−9.5	3.1	5.5	2.3	4.2	4.2
External financing and debt (billions of dollars unless stated)									
	1995	1996	1997	1998	1999	2000	2001	2002e	2003f
Net inward FDI	51.3	58.6	62.2	57.6	48.9	44.0	48.9	57.0	61.0
Net inward portfolio equity flows	9.1	10.1	0.0	−2.8	4.6	19.3	2.9	5.4	7.0
Net inward debt flows	54.2	52.0	44.5	−32.5	−11.6	−18.0	−12.0	−8.3	−13
From public sources	9.1	3.6	17.3	14.7	12.5	7.0	3.5	−2.3	−8.0
From private sources	45.0	48.4	27.2	−47.2	−24.1	−25.0	−15.5	−6.0	−5
Gross market-based capital inflows	60.0	71.5	76.2	27.3	28.2	48.7	20.7	41.0	50.0
Total external debt	462	498	529	535	541	497	504	—	—
Medium- and long-term	352	368	396	449	467	433	411	—	—
Short-term	110	130	133	86	75	64	93	—	—
Owed by public-sector borrowers	263	263	278	295	314	294	289	—	—
Owed by private-sector borrowers	199	235	250	240	227	203	215	—	—
Owed to public-sector creditors	167	160	159	185	206	194	187	—	—
Owed to private-sector creditors	295	338	370	350	335	303	317	—	—
Gross foreign exchange reserves	154.5	199.7	212.5	233.2	262.5	272.6	320.3	377.3	432.3

— Not available.

Note: e = estimate, f = forecast.

a. Fixed investment, measured in real terms.

b. Local currency GDP deflator, median.

c. Weighted average growth of import demand in export markets.

d. Goods and non-factor services.

e. Change in terms of trade, measured as a percentage of GDP.

Table A.23 External financing: East Asia and Pacific, 1997–2003
(billions of dollars)

	1997	1998	1999	2000	2001	2002e	2003f
Current account balance	16.1	58.8	60.4	55.7	42.6	42.8	41.0
as a percentage of GDP	1.1	4.4	4.2	3.6	2.6	2.5	2.2
Financed by:							
Net equity flows	62.2	54.8	53.5	63.3	51.8	62.4	68.0
Net FDI inflows	62.2	57.6	48.9	44.0	48.9	57.0	61.0
Net portfolio equity inflows	0.0	-2.8	4.6	19.3	2.9	5.4	7.0
Net debt flows	44.5	-32.5	-11.6	-18.0	-12.0	-8.3	-13.0
Official creditors	17.3	14.7	12.5	7.0	3.5	-2.3	-8.0
World Bank	2.0	2.8	2.4	1.8	0.9	-1.9	—
IMF	5.9	7.0	1.9	1.2	-2.5	-2.8	—
Others	9.3	4.8	8.2	3.9	5.1	2.4	—
Private creditors	27.2	-47.2	-24.1	-25.0	-15.5	-6.0	-5.0
Net medium- and long-term debt flows	22.8	-3.3	-10.7	-14.8	-15.0	-6.6	—
Bonds	13.3	0.7	0.9	-1.6	-0.4	6.5	—
Banks	3.9	-4.9	-11.5	-11.8	-12.9	-12.0	—
Others	5.6	0.9	-0.2	-1.3	-1.8	-1.1	—
Net short-term debt flows	4.4	-43.9	-13.4	-10.2	-0.4	0.6	—
Balancing item ^a	-110.1	-60.4	-73.0	-90.9	-34.8	-40.0	-41.0
Change in reserves (- = increase)	-12.8	-20.7	-29.3	-10.1	-47.7	-57.0	-55.0
Memo items:							
Bilateral aid grants (ex. technical cooperation grants)	2.4	2.5	2.7	2.6	2.2	2.1	2.0
Net private flows (debt + equity)	89.5	7.6	29.4	38.3	36.4	56.4	63.0
Net official flows (aid + debt)	19.7	17.2	15.3	9.5	5.7	-0.2	-6.0
Workers' remittances	14.2	8.3	10.6	10.3	10.4	11.0	—

— Not available.

Note: e = estimate; f = forecast.

a. Combination of errors and omissions and net acquisition of foreign assets (including FDI) by developing countries.