A major factor in the impressive performance by the developing countries as a whole in 2000 was the relatively broad-based and strong recovery in the crisis economies of Asia.[10] Preliminary estimates indicate that the ESCAP region should grow by over 7 per cent in 2000. The pattern of growth within the ESCAP region displays some striking differences. Within South-East Asia, for instance, Malaysia and Singapore have grown rapidly; growth has tended to falter somewhat in Indonesia, the Philippines and Thailand, especially in the second half of 2000, a development reflecting political difficulties and uncertainties in all three countries. Three countries in East Asia, China; Hong Kong, China; and the Republic of Korea, have grown impressively. On the positive side, the recovery process has displayed a welcome shift in some countries from being led by net exports and government spending to a more self-sustaining path of higher business investment and private consumption.

Investment levels have generally not yet risen to pre-crisis levels because of excess capacity in several sectors and the need for most companies to restructure and reduce debt. A particular constraint on the recovery process in the crisis economies has been the inability of SMEs to raise finance, whether for working capital, other operational needs, or for restructuring and rationalizing their operations in the medium term.

The higher oil prices in the later part of 2000, and the attendant possibilities of higher interest rates and stock market weaknesses, pose significant downside risks to recovery in 2001. Domestic stock markets remain highly vulnerable to developments elsewhere, particularly in the United States. Recent stock market weakness has undoubtedly affected business and household confidence in the region in an adverse manner, although it is difficult to determine precisely the extent to which greater stock volatility and lower equity prices are likely to affect the real economy.

The economies in transition almost doubled their growth rate in 2000, compared to 1999, as a result of high oil and gas prices, a faster pace of growth in the EU, continued inflows of foreign investment, particularly FDI, and the strong pace of recovery in the Russian Federation where soaring oil prices combined with a strong industrial performance led to a large trade surplus. As a result, foreign exchange reserves were built up from their low levels of 1999, thus giving stability to the rouble exchange rate. Capital flight diminished as a result. On the fiscal front, the significant buoyancy of output and higher oil prices led to a dramatic improvement in the financial position of all levels of government.

Along with the Russian Federation, a number of the Central Asian republics also enjoyed a major boost to their economic activities and recorded improvements in internal and external financial conditions from higher oil prices and firmer commodity markets. Kazakhstan, for instance, was able to repay a significant portion of its external debt, including all obligations to IMF.

Overall, the economies in transition in Central Asia should be able to sustain significantly positive growth in 2001. However, a possible easing of oil prices and a reduction in the pace of expansion in the Russian economy as it comes up against structural constraints are likely to mean that the robust economic performance in 2000 may not be exactly matched a year hence.

TRADE, COMMODITIES AND CAPITAL FLOWS

International trade expanded in 2000 at a strong pace, almost double that of 1999. Measured by changes in export volume, world trade is estimated to have surged by over 10 per cent in 2000, compared to 5.1 per cent in 1999 and 4.3 per cent in 1998. The share of developed countries, at about two thirds of the total, still dominates world trade, with the United States accounting for one fifth of developed country imports and around 12 per cent of world imports.

The crisis and the subsequent rapid recovery in Asia in 1999 gave rise to sharp swings in world trade flows. Trade by the developing countries had declined by a large margin in 1998, especially in value terms; significant discrepancies emerged between trade volumes and trade values as prices of

[10] The GDP performance and macroeconomic developments in the ESCAP member countries are discussed more fully in chapter II.

some commodities and, indeed, certain manufactures, declined precipitately. In 1999, both exports from and imports into the developing countries staged a major recovery. However, the discrepancy between trade volumes and trade values persisted, albeit to a lesser degree, implying that commodity prices, other than oil, had not yet recovered fully to their pre-crisis levels.

A noticeable feature in 2000 was the strong acceleration in import demand from the developing countries, a recovery resting on the strength of growing domestic investment and household consumption from early 2000 onwards. In addition, many export categories from developing countries have a high import content of components and raw materials; higher exports inevitably generated a strong demand for imports. For developing countries as a group, import volumes were estimated to have increased substantially faster than the overall growth in world trade, by 14 per cent in 2000 compared to 6 per cent in 1999. Notably, import demand from the developing countries of the ESCAP region expanded by 15 per cent.

The strong growth of world trade in 2000 embodied a robust export performance in almost all the main regions of the world. First in the list was the Asian and Pacific region where the dynamism of intraregional and intra-industry trade revived almost to pre-crisis levels, with several economies in the ESCAP region registering export growth by 20 per cent or more in 2000. Such dynamism did not, however, have much of a visible impact on the patterns of external imbalance. Developing countries as a group have traditionally run high levels of current account deficits. However, the crisis in Asia led to severe import compression in several economies of the region in 1998, giving rise to substantial current account surpluses. These surpluses have remained largely intact despite the significant rise in imports in 1999 and 2000. This out-turn suggests that the Asian crisis economies, aided by exchange rate depreciations in 1997 and 1998, have maintained and indeed enhanced their international competitiveness.

Among the developed countries, the United States has run a significant current account deficit for a number of years with the shortfall widening considerably as imports grew faster than exports in both 1999 and 2000. In fact, the deficit reached, on a year-on-year basis, nearly $400 billion by the second quarter of 2000, compared to $275 billion for the same period in 1999. Against this backdrop, the current account surpluses of the EU, except those of Japan and the United Kingdom declined only marginally. The main factors driving trade and current account imbalances in 2000 were essentially the same as those that had operated for much of the 1990s, namely the strong pace of growth in the United States and the strong US dollar, the latter being due in part to the positive interest rate differentials in favour of the United States.

A special factor operating in 2000 was the oil price, its surge during the year and, contrary to expectations, its apparent stabilization at a relatively high level. Certain other commodity prices, principally those of base metals, also rose although the overall commodity price index in dollar terms stood only marginally higher in 2000 compared to 1999. This was due largely to the offsetting weaknesses in the prices of agricultural raw materials.

The rise in oil prices was the result of strong demand driven by the robust pace of global growth superimposed upon a mismatch of inventories. There is little doubt, however, that it is the pace of global economic recovery that has been behind the recent upsurge in oil prices. The 1997-1998 crisis had caused plummeting prices and high inventories with many oil production and refining facilities being mothballed in the process. When recovery gathered pace from 1999, producers first ran down inventories with a view to gauging the sustainability of any increase in demand. Few idle production rigs, platforms or refineries were brought back into operation. Consumers, for their part, scrambled to rebuild inventories over most of 2000, especially for distillates in the summer and then for winter heating oil.

With political tensions rising in West Asia, oil prices came under unusual pressure in the autumn of 2000 and this necessitated a release by the United States Government of some of its Strategic Petroleum Reserve to alleviate market pressures. Prices began to ease thereafter but only marginally so.[11] Oil prices are expected to fluctuate within a band of $28-$33 a barrel until the spring of 2001, and then decline gently.

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11 On 10 November 2000, the price of Brent crude stood at $32 a barrel, still $10 a barrel more than a year ago.

Table I.2. Net long-term flows[a] to developing countries, 1990-1999

(Billions of US dollars)

	1990	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999[b]*
Total	98.5	124.0	153.7	219.2	220.4	257.2	313.1	343.7	318.3	290.7
Official flows	55.9	62.3	54.0	53.4	45.9	53.9	31.0	39.9	50.9	52.0
Private flows	42.6	61.6	99.7	165.8	174.5	203.3	282.1	303.9	267.7	238.7
International capital markets	18.5	25.4	52.2	99.8	85.7	98.3	151.3	133.6	96.8	46.7
Debt flows	15.7	18.8	38.1	48.8	50.5	62.2	102.1	103.4	81.2	19.1
Bank lending	3.2	5.0	16.4	3.5	8.8	30.4	37.5	51.6	44.6	–11.4
Bond financing	1.2	10.9	11.1	36.6	38.2	30.8	62.4	48.9	39.7	25.0
Other	11.3	2.8	10.7	8.7	3.5	1.0	2.2	3.0	–3.1	5.5
Equity flows	2.8	7.6	14.1	51.0	35.2	36.1	49.2	30.2	15.6	27.6
Foreign direct investment	24.1	35.3	47.5	66.0	88.8	105.0	130.8	170.3	170.9	192.0

Source: World Bank, *Global Development Finance 2000* (Washington DC, 2000).

[a] Net long-term resource flows are defined as net liability transactions or original maturity of greater than one year.

[b] Preliminary.

Base metal prices rebounded in the second half of 2000 after having declined to historical lows in the early part of 1999. Here again, the pace of global growth compounded by low inventories has led to unexpected firmness in prices in 2000. However, a wide range of other commodities remained largely unaffected by these developments because their stock-to-consumption ratios are less amenable to changes in the short term, especially rice, coffee, cocoa, tobacco and tropical logs. As such, their outlook is for continuing weakness in prices, not least on account of persistent excess production and/or stock overhang for a number of years.

Capital flows to developing countries from the international capital markets fell by 14 per cent in 1999 on a gross basis. The decline was considerably larger on a net basis with many countries seeking to reduce their external indebtedness or being unable to roll over short-term loans (table I.2). The share of developing countries in the global capital market fell to 4.5 per cent in 1999, compared to 6.4 per cent in 1998 and 11 per cent in 1997.[12] Within the group of developing countries, those of the ESCAP region increased their share significantly to about 36 per cent in 1999, from 23 per cent in 1998. Preliminary estimates suggest that the group of developing countries of the ESCAP region has again raised its relative share in global capital flows to over 40 per cent for 2000.

Gross private capital flows to developing countries are expected to recover moderately in 2000 on the basis of initial estimates up to mid-2000. At this level they would represent a return to the levels of 1995 but still below the levels seen in 1996 and 1997, just prior to the crisis in Asia. After rising strongly in 1999, FDI flows are also expected to level off as foreign investors, already wary of greenfield investments in the developing countries, find fewer opportunities for the acquisition or merger of existing facilities in these countries. Similar trends in resource flows are also in evidence with respect to official assistance. After their visible, crisis-induced rise over the years 1997-1999, official flows are expected to move downwards to their pre-crisis levels. With regard to official assistance, the most notable recent development has been the enhanced initiative for heavily indebted poor countries. Under the enhanced initiative, the qualifying period for debt relief would be reduced, qualifying thresholds for

[12] World Bank, *Global Development Finance 2000* (Washington DC, 2000), pp. 21-23.

certain indicators such as the debt-to-export ratio and the export-to-GDP ratio would be lowered and a link would be established between debt relief and poverty reduction.

While the overall matrix of factors and determinants of capital flows to developing countries remains broadly unchanged, some new features emerged in 2000. The tightening of monetary policy in the developed countries and volatility in the stock markets have considerably restricted access to external finance for developing countries. Not only did interest rates go up but also yield spreads for developing countries tended to widen as stock market volatility induced investors to be more risk-averse. So strong is the flight to quality that even spreads between United States treasury bonds and corporate bonds reached levels last seen only in the early 1990s, as noted earlier.

A related feature of the capital markets in the second half of 2000 was the major downward correction of many ICT-related shares, in both the developed and developing countries. In 1997, the ICT sector accounted for 10 per cent of private capital raised in the developed countries and 12 per cent in the developing countries. Its relative share was estimated to have risen to 44 per cent, and 77 per cent of new equity issues in the developing countries for the first half of 2000.[13] Thus, as the weight of ICT firms had rapidly reached a very high level in a number of developing country stock price indices through rising share values, their vulnerability to downside risks and sharper declines intensified.

IMPLICATIONS FOR THE ESCAP REGION

The external conditions for sustained growth in the ESCAP region appear to be mixed for 2001. Economic growth in the developed countries should continue to be positive. On present evidence the likely slowdown in the United States, starting in the latter part of 2000, is unlikely to be prolonged. Given existing patterns of productivity growth, the United States economy will most likely continue to enjoy above-trend output expansion despite the currently low level of unemployment. A modest slowdown is also forecast for the EU. Japanese economic growth could be higher in the coming year, although signs are somewhat discouraging at this stage.

In aggregate terms, the growth rate of developed country imports from all sources is expected to slow from over 10 per cent in 2000 to just below 8 per cent in 2001. As some two thirds of such trade is with other developed countries, the impact of a slowdown of this magnitude is likely to be modest for the developing countries. Exports by developing countries are estimated to slow from 8.8 per cent to just over 7 per cent in 2001. As such, the likely adverse impact of external demand on output growth in the region should be manageable in the coming year. Nevertheless, the countries of the region need to strengthen domestic impulses for growth.

An imponderable factor, however, is the possibility of a sharp slowdown in the United States economy in 2001, a development which could dampen further export growth from both developed and developing economies. Among other major unfavourable knock-on effects from such an adverse development could be: lower commodity and manufactured goods prices, weakening import demand from various interdependent countries; and possibly a sharp slowdown of world trade in value terms. However, an offsetting factor is the growing importance of intraregional trade within the ESCAP region; chances of the entire region experiencing a simultaneous slowdown in trade and growth, though possible, are not very likely.

On the other hand, the prognosis for capital flows to developing countries is more uncertain when account is taken of their recent levelling off. The slowdown appeared to persist in the second half of 2000. A brighter note is that the Asian and Pacific region increased its share in private capital flows in 1999 as most crisis economies rebounded strongly from the recession. In the first half of 2000, the upward trend continued (figure I.1). It is worth noting here that a major portion of equity capital was directed as investments in ICT firms. Easier financing conditions meant that the boom in ICT investments so visible in the United States in the early part of 2000 was also partially replicated in the region.

[13] *The Economist,* 28 October 2000, p. 113.