

# Monthly Briefing

## World Economic Situation and Prospects

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### Summary

- International oil prices increased further amidst continued unrest in the Middle East.
- Food prices reached new record highs, pushing up inflation worldwide.
- As this went to press, a devastating earthquake in Japan occurred, causing the loss of thousands of human lives and huge economic damages.

### Global issues

#### *G-20 meets to iron out differences and calls for guidelines*

Ministers of Finance and Central Bank Governors of the G-20 met in Paris on 18 and 19 February in preparation for the April G-20 summit. Recently, differences of approach have been surfacing between G-20 members on central issues, such as the re-emergence of global imbalances, escalations in prices of commodities and fiscal and private sector balances. The meeting succeeded in ironing out divergences by postponing concrete coordinating strategies while calling for studies aimed at setting guidelines for policy action, to be enunciated at the April meeting.

#### *Food prices continue to rise*

As G-20 ministers expressed concern at the continuing rise of food and commodity prices, the FAO food price index increased to new record highs in February. Over the last eight months, the index rose 40 per cent and is situated 5 per cent above the peak of June 2008. The index for cereals rose by 68 per cent over the same period and is only 7 per cent below its historic peak of 2008. The sharp price rises are particularly challenging for developing countries with high food import ratios (see table).

#### *Oil surged amid the escalating turmoil in North Africa and Western Asia*

The price of Brent crude oil soared to nearly \$120 per barrel (pb) by the end of February amid the continued political unrest in North Africa and Western Asia, particularly the escalating turmoil in the Libyan Arab Jamahiriya. In the span of less than three business days (between 18 and 24 February), the daily price rose by almost 12 per cent (see figure). The Libyan Arab Jamahiriya produces 1.6 million barrels a day, less than 2 per cent of the global oil supply. The violent uprising in the Libyan Arab Jamahiriya has forced oil companies to cut supply. After Saudi Arabia announced an increase in production to make up for the shortfalls due to unrest in the Libyan Arab Jamahiriya, the prices retreated somewhat, but they continue to fluctuate above \$110 pb.

### Developed economies

#### *Lower growth estimates for the United States and impasse over the budget*

The 2010 fourth quarter growth rate of the United States was revised downwards from 3.2 per cent (annualized quarter over quarter) to 2.8 per cent. Major causes for

**Table: Percentage of food imports to food consumption for selected developing countries<sup>a</sup>**

AFRICA	%	DEVELOPING ASIA	%
Congo	91	Yemen	63
Libyan Arab Jamahiriya	87	Iraq	48
Cape Verde	81	Syrian Arab Republic	39
Gabon	70	Mongolia	31
Equatorial Guinea	68		
Botswana	68	<b>CIS (and Georgia)</b>	
Mauritania	66	Georgia	67
Comoros	65	Armenia	50
Djibouti	61	Tajikistan	35
Swaziland	61	Azerbaijan	33
Lesotho	56		
Tunisia	55	<b>LATIN AMERICA</b>	
Liberia	52	Costa Rica	74
Algeria	49	Haiti	54
Côte d'Ivoire	49	Honduras	52
Somalia	49	Colombia	50
Eritrea	46	Chile	49
Namibia	46	Venezuela (B.R.of)	47
Sao Tome & Principe	38	Guatemala	46
Egypt	36	Peru	40
Morocco	35	El Salvador	39
Guinea-Bissau	35	Ecuador	34
Senegal	35		
Congo, Dem. Rep. of	32		
Cameroon	31		
Burundi	30		

Source: UN Food and Agriculture Organization, Global Food Price Monitor, March 2011.

<sup>a</sup> Countries where imports over consumption represent 30 per cent or higher.

the revision were a higher estimate of imports of goods and lower estimates of private consumption and State and local government expenditures.

The political process for adopting the federal government budgets for fiscal year 2011, which started in October 2010, has been prolonged; the main reason for the impasse is disagreement on the level of government spending. Meanwhile, government operations are sustained by a temporary funding resolution pending the approval of the budget. In Canada, the final estimate of the GDP growth rate for the fourth quarter of 2010 was 3.3 per cent (annualized, quarter over quarter), higher than the 1.8 per cent for the previous quarter. Strong rebounds of exports and private consumption were the main factors behind the improved performance. With this estimate, the GDP growth rate for the year 2010 comes in at 3.1 per cent.

### ***A relapse in Japan's recovery***

The latest data show that Japan's GDP fell by 1.3 per cent (seasonally adjusted annual rate) in the final quarter of 2010. The relapse in the recovery of the world's third largest economy was mainly caused by declines in private consumption, public investment and exports. While private investment continued to grow, nominal wages fell for the second consecutive quarter. For 2010 as a whole, GDP rebounded by 3.9 per cent, but the level of real GDP is still about 4 per cent lower than the peak of 2008. What is more, nominal GDP remains about 8 per cent lower than the peak in 1997, due to persistent deflation over the past decade. As a result, measured in United States dollars, Japanese nominal GDP has been surpassed by that of China for the first time in several decades. However, China's per capita income level is still only one tenth of Japan's.

As this went to press, Japan's east coast was hit by an earthquake of unprecedented proportions, followed by a tsunami with devastating effects. It has caused the loss of tens of thousands of human lives. Nuclear power plants have been damaged with consequences that are difficult to gauge as yet. An assessment of the global economic repercussions of the disaster will be given in the next month's Briefing.

### ***New Zealand hit by most severe earthquake in eight decades***

The earthquake of 22 February has caused about 200 casualties in New Zealand, with a tentative estimate of economic loss as high as 16 billion New Zealand dollars (about 9 per cent of its GDP in 2010), more than twice the damage caused by the quake in September 2010.

### ***Western Europe, second half slowdown confirmed, but confidence continues to improve***

Based on initial estimates, GDP of the Euro area grew by 0.3 per cent in the fourth quarter of 2010, maintaining the pace of the third quarter and continuing the significant slowdown in the second half of the year. Economic growth in Germany slowed to 0.4 per cent, in France it was stable at 0.3 per cent, in Italy it barely grew, at only 0.1 per cent, and in the United Kingdom it fell sharply by 0.6 per cent. Among the countries in fiscal crisis, Spain registered positive GDP growth of 0.2 per cent after stalling in the third quarter, while Portugal saw its GDP decline and Greece also remained in serious recession.

Extreme winter events have likely affected economic conditions in parts of Europe, particularly in the UK and Germany, as indicated by the sharp declines in construction and, to a lesser extent, retail sales. Even so, indices of business confidence continued their upward trend, driven by positive expectations about rising activity in manufacturing and services. This indicates that output may pick up slightly in the first quarter of 2011.

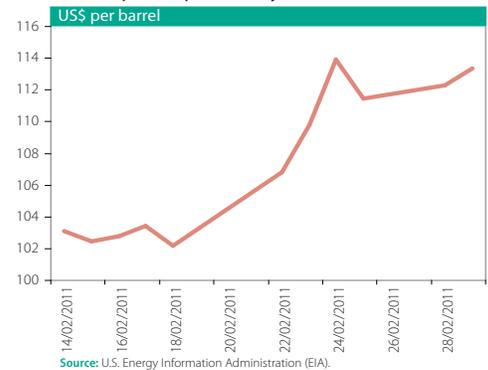
### ***The new EU members: better than expected outcome for 2010***

Flash estimates suggest higher-than-expected GDP growth in several of the new EU member States in the fourth quarter of 2010. Industrial activity has been buoyant thanks to the recovery in import demand in Western Europe. In the Czech Republic, GDP expanded by 2.3 per cent in 2010. Fourth quarter aggregate output levels received a boost from booming exports in automotive and electrical industries. Exports of fuel and fertilizers helped GDP growth in Lithuania to accelerate to 4.8 per cent in the fourth quarter of 2010, and 1.3 per cent for the year. Slovenia's economy grew by 1.2 per cent in 2010. Latvia's economic performance exceeded expectations with a 3.7 per cent GDP growth in the fourth quarter, limiting output decline over 2010 as a whole to only about 0.2 per cent.

Positive trends were also reported in the labour markets at the end of 2010. In Estonia, for instance, the unemployment rate dropped to 13.6 per cent towards the end of December, down from 19.8 per cent in early 2010.

Higher food and energy prices continue to push up inflation. In January, consumer prices increased by 1.3 per cent in Latvia and by 1.2 per cent in Poland.

Figure:  
Brent spot oil price, daily



In February, Romania reached a new precautionary two-year standby agreement (at the staff level) with the IMF, worth 3.6 billion euros. The Government, however, decided not to draw the last tranche of the existing standby loan, citing sufficient levels of foreign-exchange reserves.

## Economies in transition

### *Inflation accelerates in the CIS*

Following strong fourth quarter growth, GDP increased by 7.6 per cent in Belarus in 2010 (compared to 0.2 per cent in 2009). In January, the annual rate of inflation continued to accelerate, however, reaching 10.6 per cent, up from 9.9 per cent in December. Monthly food inflation exceeded 2 per cent. In the Russian Federation, monthly inflation accelerated to 2.4 per cent in January. Monetary authorities continued to tighten their monetary stance in response. In January, reserve requirements were increased for the first time since August 2009, and again at the end of February. Also, the benchmark refinancing rate was raised for the first time since 2008. Uzbekistan, in contrast, reduced the refinancing rate by 2 percentage points to 12.0 per cent in January, responding to a relatively low (official) rate of inflation of 7.3 per cent for 2010. Uzbekistan's economy expanded strongly in 2010, as GDP growth reached 8.5 per cent.

Oil exports from the Russian Federation to Belarus were interrupted in January over disagreements about pricing terms. At the same time, on 1 January, the Russian Federation abolished a tax (of \$230 per ton) on fuel exports to Kyrgyzstan as part of efforts to revive the economy.

### *South-Eastern Europe: Serbian economy slows*

The economy of Serbia expanded by 1.8 per cent in the fourth quarter and GDP growth for the year 2010 was recorded at 1.5 per cent. Growth was mainly driven by exports. While economists have positively assessed the ongoing rebalancing of the Serbian economy, the sentiment is not shared by the general public. Private consumption remains depressed, as high inflation has eroded the purchasing power of the population against the backdrop of earlier wage and pension freezes. The annualized rate of inflation increased further, to 11.2 per cent, in January. Most worrisome, the labour market deteriorated notably. The unemployment rate still bordered on 20 per cent in October, as a large number of companies faced bankruptcy.

## Developing economies

### *Africa: Libya conflict evolving into a humanitarian crisis*

The situation in the Libyan Arab Jamahiriya is taking an increasing humanitarian toll. Large numbers of migrant workers are trying to leave the country. The World Food Programme is reporting shortages of food, fuel and medical supplies. As the country was expected to import 1.3 million tons of wheat this year, representing around 80 per cent of its total demand, any prolonged disruption of transportation and distribution networks due to a lack of security is expected to rapidly result in a more serious shortage of food supplies.

In South Africa, the economy grew by 2.8 per cent in 2010, following a contraction of 1.7 per cent in the previous year. Higher commodity prices, generally more favourable external demand conditions and accommodative monetary policy were driving growth, which was dampened by a general sense of reluctance among consumers and businesses to spend in the wake of the recession. Inflation receded to 4.1 per cent in 2010, from 7.2 per cent in 2009, with the central bank projecting an increase to 4.6 per cent this year in the light of higher oil prices. Inflation also remains a concern in other parts of the continent. In Kenya, inflation rose to 6.5 per cent year on year in February from 5.4 per cent in January, mainly because of higher food prices.

### *China steps up efforts to reform its exchange rate system*

Economic activity in East Asia gained further strength in the fourth quarter of 2010, bringing full-year growth to 10.3 per cent in China, 7.8 per cent in Thailand, 7.3 per cent in the Philippines and 6.1 per cent in Indonesia and the Republic of Korea. High-frequency indicators such as trade and industrial production data point to a continuing strong performance in early 2011. Higher international prices for oil and other commodities are pushing up import costs, thereby reducing trade and current-account surpluses. In China, the trade surplus fell from \$13.1 billion in December to \$6.5 billion in January. That of the Republic of Korea dropped from \$3.7 billion to \$1.6 billion.

While China's foreign-exchange reserves reached \$2.8 trillion at the end of 2010, authorities have intensified their efforts to reform the country's exchange-rate system. Measures adopted recently include: promotion of the renminbi as a means of payment in international trade; issuance of off-shore renminbi-denominated corporate bonds; experimentation with the use of renminbi for outward foreign direct investment; and a gradual opening up of the capital and financial accounts. Hong Kong Special Administrative

Region of China, as a global financial centre, acts as the testing ground for the Mainland in the reform, through the massive issuance of renminbi-denominated corporate bonds, among other measures.

### ***Growth in India moderates but outlook remains favourable***

Growth in India decelerated slightly in the final quarter of 2010 amid tighter monetary and fiscal conditions, but the prospects for 2011 remain favourable. Economic activity expanded by 8.2 per cent year on year, down from 8.9 per cent in each of the previous two quarters. Private consumption growth accelerated to 9 per cent, largely offsetting a slower growth of fixed capital formation and a contraction of government consumption. Fixed capital formation, which had been a major growth driver during the recovery, expanded by only 6.0 per cent following several interest rate hikes by the Reserve Bank of India in 2010. At the sector level, agricultural output rose by 8.9 per cent—the fastest rate in several years—owing to healthy monsoon rains, whereas manufacturing output growth softened.

The IMF has released the sixth tranche of the standby agreement with Sri Lanka, bringing total disbursements to \$1.5 billion. In combination with strong inflows of workers' remittances and of portfolio and direct investments, these disbursements have allowed foreign reserves to recover. Total gross official reserves currently account for about 6 months of imports, compared to only 1.2 months in the first quarter of 2009.

### ***Political unrest continued in a few countries in Western Asia***

Massive protests continued in Bahrain, Jordan and Yemen, and have recently spread to Oman, and, to a lesser degree, Saudi Arabia, along with a number of countries in neighbouring North Africa. While social discontent from food inflation, unemployment and corruption was a catalyst for the unrest in some of these countries, the focus of the protests is now on calling for greater political representation. The political turmoil in the region has added significant uncertainty to the economic outlook of the region, as well as to the world.

### ***Fiscal position in Turkey improves***

The central government budget of Turkey posted a surplus of TRY 1.0 billion in January 2011, a remarkable improvement compared with the deficit of TRY 3.2 billion in January of last year. The cyclical improvement in tax revenues was the main factor behind the strong fiscal outcome, as they were up by 14 per cent in January, along with robust domestic demand. The target of keeping the budget deficit below 2.8 per cent of GDP in 2011 seems reachable.

### ***Attempts to contain inflation may weaken growth prospects in Latin America***

Recent data confirm that most countries in Latin America experienced robust output growth rates in 2010, though they tapered off towards the end of the year. The exceptions are the Bolivarian Republic of Venezuela and Haiti, which continued in recession. In the near outlook, however, these countries may also see positive growth.

The economic landscape in 2011 is complicated by escalations in international prices of food and commodities. Five countries in the region which suffered natural disasters affecting current food supplies are at particular risk as they have rather high shares of food imports (relative to total food consumption): Costa Rica (74 per cent), Haiti (54 per cent), Colombia (50 per cent), Chile (49 per cent) and the Bolivarian Republic of Venezuela (47 per cent). The rise of international prices, attenuated by exchange-rate appreciations, is adding pressure to tighten monetary policy in Chile and Colombia, while in Costa Rica and the Bolivarian Republic of Venezuela food subsidies and regulation are cushioning the effects for consumers. In the Bolivarian Republic of Venezuela, monthly consumer price inflation remains high but decelerated from 2.7 per cent in January to 1.7 per cent in February. An urgent challenge to containing inflationary pressures due to shortages of supply is the expansion of electricity generation, which is affecting production in all sectors.

Brazil, Chile and Colombia have shifted to monetary tightening and moderating the expansionary fiscal stance in order to stem the overheating of their economies.

### ***Least-developed countries: adverse weather conditions compound power shortage in the United Republic of Tanzania***

In the United Republic of Tanzania, prolonged droughts have led to low water levels at hydropower stations. This has compounded the existing power shortages and the electricity supply has been rationed further. The country is currently producing only 470 megawatts of electricity, well short of the peak demand of 830 megawatts. Only 14 per cent of the population has access to the national grid. To deal with the current shortfall and the projected demand growth rates, the Government has moved closer to securing the loans for the construction of a new 200 megawatt coal-fired power plant, with the more immediate focus being the installation of emergency power plants.

Meanwhile, Zambia registered consumer price inflation at 9.0 per cent year on year in February, which is unchanged from the previous month but does not yet take into account the 11 per cent fuel price increase announced in the middle of the month. ■