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This report presents short-term prospects for the global economy in 2014-2015, including the major risks and policy challenges. The report draws upon inputs from the experts of Project LINK, as well as analysis of staff in the Department of Economic and Social Affairs, the United Nations Conference on Trade and Development and the five United Nation Regional Commissions. The LINK Country Reports, which contain detailed country forecasts and policy analysis submitted by the national LINK centres, are available on the websites of both the United Nations and the University of Toronto.[1]

Under the direction of Pingfan Hong, this report was prepared by the Global Economic Monitoring Unit, which includes Grigor Agabekian, Clive Altshuler, Matthias Kempf, Hung-Yi Li, Ingo Pitterle (who also consolidated the regional outlook), Sergio Vieira and John Winkel. Ann D'Lima and Cordelia Gow provided statistical assistance. Qi Dai and Rui Zhang, two interns, provided valuable support. The views expressed herein do not necessarily represent those of the United Nations or its Member States.

[1] Available from http://www.un.org/esa/analysis/link and http://www.chass.utoronto.ca/link.

Summary

Even after more than five years since the global financial crisis erupted, the world economy has not yet fully recovered. Most developed economies are still toiling up a bumpy path in the aftermath of the financial crisis, struggling, in particular, to find the right policy actions. A number of emerging economies which have already experienced a notable slowdown in the past two years, face more headwinds in the international economic environment including sharp reversals of international capital inflows and large depreciations of their currencies. Meanwhile, the least developed countries have seen a decline in international official development aid.

On the positive side, the euro area seems to have finally come out of a protracted recession, with a growing gross domestic product (GDP) of the region as a whole; and for a few large emerging economies, including China, growth seem to have stabilized and backstopped further slides. In the baseline forecast, the world economy is expected to grow by 2.9 and 3.3 per cent for 2014 and 2015 respectively, compared with an estimated growth of 2.1 per cent in 2013.

The baseline outlook is subject to a number of uncertainties and risks: (1) A key risk is associated with the future unwinding of the unconventional monetary policies by the central banks of major developed countries in the next few years. As indicated by the most recent financial turbulence in mid-2013, when the United States Fed simply mentioned the possibility of tapering its purchases of assets, such a risk could entail substantial instability in the world economy; (2) wWhile the systemic risks in the euro area have abated owing to a number of policy measures adopted in the EU over the past year, considerable banking and fiscal risks remain, and the real economy in the euro area, particularly in those member countries which are under debt distress, remains fragile; (3) tThe United States has just averted a default crisis, however, the risk has not been resolved but merely postponed. The uncertainties about the government budget and the debt ceiling remain, posing significant risks for the world economy; (4) Many large emerging economies saw a significant deceleration in GDP growth in the past two years, owing to a combination of weak external conditions and domestic impediments. Although economic fundamentals and the policy space in these economies are measurably better than they were in the 1990s, some of them, particularly those with significant external imbalances, remain vulnerable to large external shocks, such as tightening in global liquidity and sudden reversals in capital inflows.

Macroeconomic policy stances in the world economy have become more diverse across countries, and some critical transitions are expected in 2014-2015.

While policies in most developed countries, except Japan, will continue to feature a combination of tightened fiscal policy and accommodative monetary policy, the degree of fiscal tightening will be less restrictive and the extent of monetary easing will become less lax. Managing a smooth tapering of the quantitative easing (QE) programmes will be the key challenge for the monetary authorities in major developed countries, as the risks associated with this transition will pose a threat not only for developed economies, but also for the rest of the world. The central banks of major developed countries have the

primary responsibility for providing adequate and stable global liquidity, as they are the issuers of the international reserve currencies.

In developing countries and the economies in transition, policymakers face a more challenging international economic environment and a more demanding domestic economic situation, which requires tough tradeoffs among a confluence of different policy needs. Moreover, some of the challenges facing developing countries and economies in transition may go beyond what standard macroeconomic policies can deal with, and require institutional reforms.

The multiple and complex challenges in the world economy call for strengthening of international policy coordination. While the primary focus of the globally concerted and coherent policy actions should continue to be on a stronger recovery, particularly the recovery of jobs, increasing attention should also be given to mitigating the spillover effects emanating from the large-scaled unconventional monetary policies adopted by major developed countries on developing countries and the economies in transition.

International policy cooperation should ensure that sufficient resources are made available to developing countries, especially the least developed countries (LDCs) and countries that possess limited fiscal space and face large financing needs for sustainable development and poverty reduction. The decline in official development assistance (ODA) flows over the past two years should be reversed. As the target date for the United Nations Millennium Development Goals (MDGs) is approaching, international donors should redouble their efforts to deliver on existing commitments. These resources are badly needed for developing countries to accelerate progress towards the achievement of the MDGs by the end of 2015, and to build a solid foundation for long-run sustainable development beyond 2015.

1. Global macroeconomic prospects

Global growth continues to face headwinds

Once again, the world economy has performed poorly for another year, unable to meet even the modest projections many institutional forecasters made a year ago, including Project LINK. According to the latest information, world gross product (WGP) is estimated to grow by 2.1 per cent in 2013, notably lower than the baseline forecast of 2.5 per cent Project LINK made in October 2012, although still better than the more dire alternative scenario presaged in last year's LINK report.[2]

Underperformance in the world economy during 2013 could be observed across almost all regions and major economic groups. Most developed economies have continued their prolonged struggle in the aftermath of the financial crisis, grappling in particular with the challenges of taking appropriate fiscal and monetary policy actions. A number of emerging economies, which have already experienced a notable slowdown in the past two years, encountered considerable new financial turbulence this summer, featuring sharp reversals of international capital inflows and large depreciations of their currencies.

Nevertheless, some signs of improvements have shown up more recently: the euro area has finally come out of a protracted recession, with GDP for the region as whole growing; and a few large emerging economies, including China, seem to have stabilized their growth and prevented further slides. Premised on a set of assumptions (Box 1), the baseline forecast for global growth is 2.9 per cent and 3.3 per cent for 2014 and 2015 respectively (table 1 and figure 1). Again, this baseline forecast is encompassed by a number of uncertainties and risks, emanating from possible policy missteps and factors beyond the economic domain.

Box 1. Major assumptions for the baseline forecast

This box summarizes key assumptions underlying the baseline forecast, including monetary and fiscal policies for major economies, exchange rates for major currencies, international prices of oil and other primary commodities. Policy assumptions for other countries can be found in the text of the regional outlook.

Monetary policy

The *Federal Reserve of the United States* (Fed) is expected to continue its accommodative stance in the outlook for 2014-2015. In accordance with the forward monetary policy guidance of the Fed, it is assumed that in the forecasting period of 2014-2015 the federal funds interest rate will remain within the range of 0.0 per cent to 0.25 per cent until mid-2015, to be followed by a gradual increase starting in the third quarter of 2015. The Fed will adjust its purchases of long-term assets in three phases: the Fed

[2] LINK Global Economic Outlook, October 2012, available from http://www.un.org/en/development/desa/policy/proj_link/documents/geo201210.pdf.

will start to taper the amount of its purchases in December of 2013, from the current level of $85 billion per month gradually to zero by mid-2014; The Fed will hold the assets on its balance sheet for the period until mid-2015; and will start to unload them gradually in the third quarter of 2015.

The European Central Bank (ECB) is assumed not to cut its policy interest rates further, but to keep policy rates at the current levels through the end of 2015, to be followed by a gradual path of increases. The outright monetary transaction programme (OMT) will remain in place and the existing refinancing operations will continue to meet the banking sector's needs.

The Bank of Japan (BOJ) is assumed to continue its *"Quantitative and Qualitative Monetary Easing" (QQME)* as it was originally designed until the end of 2014. The policy rate for BOJ is also assumed to stay within the range of 0.0 per cent to 0.1 per cent through the end of 2015, to accommodate the second hike of the consumption tax rate that is assumed to be implemented in October 2015.

The People's Bank of China (PBOC) is expected to maintain its prudent monetary policy stance, while making some fine-tuning adjustments to ensure a balance between growth and economic restructuring. Interest rates are likely to remain unchanged over the next few quarters. Money supply growth is expected to moderate slightly in 2014-15. Meanwhile, continued financial reform, especially further liberalization of interest rates, and increased regulations in the shadow banking sector will have significant impacts on the liquidity conditions in the economy, on top of conventional monetary policy.

Fiscal policy

Fiscal policy in the *United States* is expected to remain restrictive in 2014-2015, but less severe than 2013. The sequestration is assumed to be replaced by an agreement on spending cuts that fall on Medicare, Medicaid and Social Security. Emergency unemployment insurance benefits will be phased out gradually. Government spending in real terms will be flat in 2014-2015.

In the *euro area*, 12 out of 17 Economic and Monetary Union (EMU) countries remain under the Excessive Deficit Procedure (EDP) and will continue to pursue consolidation programs, with the crisis countries pursuing even more stringent consolidation programs. The Economic and Financial Affairs (ECOFIN) Council granted a number of countries an extension of the deadline for correction of their excessive deficits: 2014 for the Netherlands and Poland; 2015 for France, Portugal and Slovenia; and 2016 for Spain. They also deemed that Italy has corrected its excessive deficit. Fiscal policy in the region will continue to be focused on reducing fiscal imbalances. The debt crisis countries are assumed to continue their adjustment programs, but the time-table for achieving targets will in some cases be extended, and no countries will ask for formal assistance, under the European Stability Mechanism (ESM).

Japan is assumed to increase the consumption tax rate from the current level of 5.0 per cent to 8.0 per cent in April 2014. An expansionary package of 5 trillion yen will be included into the budget for fiscal year 2014. The package will consist of lower rates for other taxes and higher outlays for certain expenditure categories. The second increase in the consumption tax rate, from 8.0 per cent to 10.0 per cent, will be implemented in October 2015.

China is expected to maintain a proactive, mildly expansionary fiscal policy stance. Public spending will continue to increase in the areas of education, healthcare and other forms of social expenditures. The general government budget deficit is expected to rise to 2.0 per cent of GDP in 2013 and 2014.

Exchange rates among major currencies

The *dollar/euro* exchange rate is forecast to fluctuate around its current level, averaging 1.32 dollar/euro in the rest of 2013, with the dollar appreciating gradually, resulting in a full-year average of 1.27 dollar/euro in 2014, and 1.21 dollar/euro in 2015.

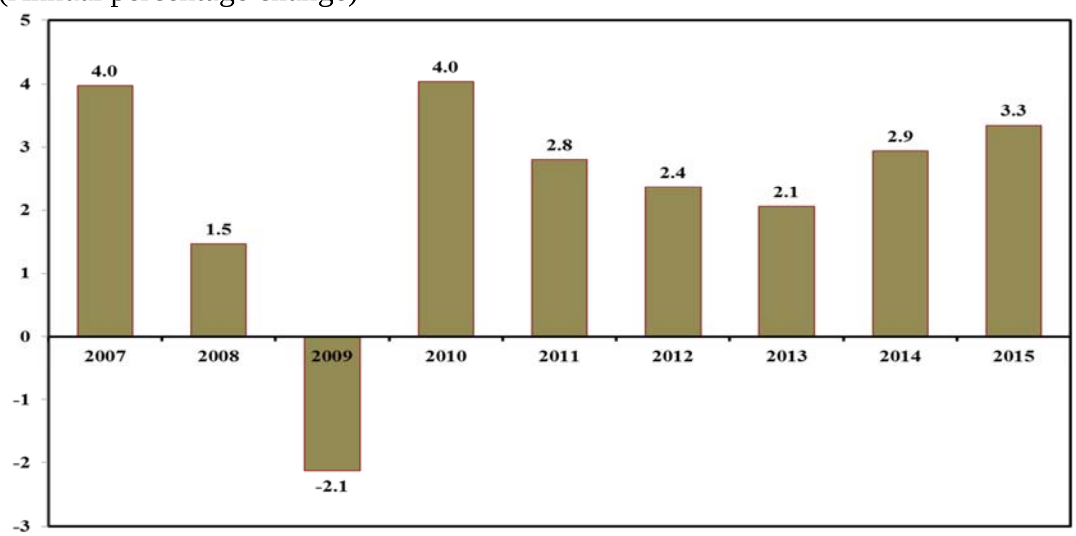
The *yen/dollar* exchange rate will average 102.5 yen/dollar and 104.5 yen/dollar for 2014 and 2015, respectively.

The *renminbi/dollar* exchange rate is expected to be 6.09 CNY/dollar in 2014 and 6.05 CNY/dollar in 2015.

Oil price

Brent is expected to be around $108/bbl for 2014-2015.

Figure 1. Growth of world gross product, 2007-2015 [a]
(Annual percentage change)



Source: UN/DESA.

[a] 2013-2015 are forecast figures, based in part on Project LINK.

Table 1. Gross domestic product and world trade.

						Change from WESP2013	
	2008-2011 [a]	2012 [b]	2013 [c]	2014 [c]	2015 [c]	2013	2014
World	1.5	2.4	2.1	2.9	3.3	-0.3	-0.3
Developed economies	0.1	1.4	1.0	1.9	2.4	-0.1	-0.1
United States of America	0.3	2.8	1.5	2.5	3.2	-0.2	-0.2
Japan	-0.7	2.0	1.9	1.3	0.8	1.3	0.5
European Union	-0.2	-0.4	-0.1	1.4	1.9	-0.7	-0.3
EU-15	-0.3	-0.5	-0.1	1.4	1.8	-0.6	-0.2
New EU members	1.3	0.6	0.6	2.1	2.7	-1.4	-0.8
Euro area	-0.1	-0.7	-0.5	1.1	1.6	-0.8	-0.3
Other European	0.6	1.9	1.7	2.6	2.9	0.2	0.7
Other Developed countries	1.5	2.6	2.1	2.7	3.0	0.1	-0.3
Economies in transition	1.9	3.2	2.4	2.5	3.6	-1.2	-1.7
South-Eastern Europe	1.6	-0.9	1.6	1.9	2.9	0.4	-0.7
CIS and Georgia	1.9	3.4	2.4	2.5	3.6	-1.4	-1.9
Russian Federation	1.4	3.4	2.0	1.8	3.2	-1.6	-2.4
Developing economies	5.3	4.7	4.5	5.1	5.4	-0.6	-0.5
Africa	3.4	5.4	4.0	4.9	5.1	-0.8	-0.2
North Africa	1.7	6.7	2.5	4.2	4.6		
East Africa	6.1	5.6	5.9	6.4	6.3		
Central Africa	4.5	4.4	4.2	4.7	4.0		
West Africa	6.1	6.7	6.6	6.9	6.7		
Southern Africa	2.9	3.5	3.6	4.1	4.4		
East and South Asia	6.8	5.4	5.5	5.8	6.0	-0.5	-0.5
East Asia	7.0	5.9	5.9	6.2	6.2	-0.3	-0.3
China	9.6	7.7	7.6	7.5	7.3	-0.3	-0.5
South Asia	6.3	3.6	3.8	4.6	5.2	-1.2	-1.1
India	7.3	5.1	4.7	5.2	5.7	-1.4	-1.3
Western Asia	3.9	3.5	3.4	4.5	4.5	0.1	0.4
Latin America and the Caribbean	3.1	2.9	2.5	3.6	4.3	-1.4	-0.8
South America	4.0	2.4	3.0	3.4	4.1	-1.0	-1.0
Brazil	3.7	0.9	2.3	3.0	4.2	-1.7	-1.4
Mexico and Central America	1.6	3.9	1.7	4.0	4.8	-2.2	-0.6
Mexico	1.4	3.8	1.5	4.0	4.8	-2.3	-0.6
Caribbean	2.7	2.7	2.4	3.3	3.8	-1.3	-0.5
Least developed countries	5.5	4.3	5.3	5.6	5.6	-0.4	0.1
Memorandum items:							
World trade [d]	2.8	2.9	2.4	4.8	5.3	-1.9	-0.1
World output growth with PPP-based weight	2.6	3.1	2.8	3.6	4.0	-0.5	-0.4

Source: UN/DESA.

a Average percentage change.

b Actual or most recent estimates.
c Forecast, based in part on Project LINK.
d Includes goods and services.

Among *developed countries*, the *United States* is estimated to grow at a meager pace of 1.5 per cent in 2013, significantly lower than the growth of 2.8 per cent in the previous year. Fiscal tightening and a series of political gridlocks on budget issues over the year have weighed heavily on growth. During the writing of this report, the federal government reversed its partial shutdown and raised the debt ceiling, although only for a short period, it will still place significant uncertainties on the economic prospects for 2014-2015. Monetary policy has been extremely accommodative, but the expectations formed in mid-2013 about the possible tapering of the quantitative easing programme has caused some jitters in financial markets, pushing up long-term interest rates and imposing more constraints on consumption and investment. A moderate improvement earlier in 2013, in such areas as housing and employment, lost momentum towards the end of the year. In the outlook, assuming that the debt ceiling would be raised and the future unwinding of the monetary easing will be smooth, GDP is expected to increase 2.5 per cent and 3.2 per cent for 2014 and 2015 respectively. However, risks remain on the downside, particularly because the political wrangling over the budget issues may continue to linger in coming years.

Western Europe emerged from recession in the second quarter of 2013, after six consecutive quarters of declining GDP. Growth was led by net exports, and to a lesser extent, private and public consumption, but investment remained weak. Despite the upturn, the poor performance at the beginning of the year leads to an estimated decline in GDP of the EU-15 by 0.1 per cent in 2013, after a decline of 0.5 per cent in 2012, but afterwards GDP is expected to grow by 1.4 per cent and 1.8 per cent in 2014 and 2015 respectively. Growth remains weak due to a number of factors: fiscal austerity programs remain in force, intra-regional demand is still exceptionally low, while extra-regional demand has slowed. Lending conditions are heterogeneous across the region, with bank credit amply available in some countries while in others conditions remain extremely tight. There remains considerable diversity across countries. In 2013, the United Kingdom is estimated to grow by 1.4 per cent, with Germany and France growing by 0.4 per cent and 0.1 per cent respectively. The countries in debt crisis are showing signs of turning the corner but remain in feeble positions. Italy is estimated to contract by 1.9 per cent and Spain by 1.2 per cent in 2013, but both are expected to return to positive growth in 2014. Cyprus and Greece are expected to continue contracting in 2014.

Many of the *new EU members* in Eastern Europe remained in a sustained recession in the first half of 2013, as they continued to feel the impact of the protracted weakness in their trading partners in the EU-15 and the continuing deleveraging by foreign banks present in the region. The situation has improved in the second half of the year, with business sentiment and household confidence strengthening, in response to the return to growth in Western Europe. For example, the automotive industry in Central Europe shows signs of an upturn and retail sales also increased in the Czech Republic and Poland. The aggregate GDP growth for the region is estimated to be 0.6 per cent in 2013, and is forecast to strengthen moderately to 2.1 per cent in 2014 and further to 2.7 per cent in 2015.

Japan is estimated to grow by 1.9 per cent in 2013, boosted by a set of expansionary policy packages, including fiscal stimulus and large-scale purchases of assets by the central bank. Fixed investment has been a key driver of growth, as a number of public construction projects have been financed by the supplemental budget. The Government is also expected to introduce another package targeting structural reforms soon, but the effects are not certain. Meanwhile, the anticipated increase in the consumption tax rate over the next two years is expected to curb growth. GDP is forecast to moderate to 1.3 per cent in 2014.

In the *other developed countries*, GDP in Canada is estimated to grow at 1.6 per cent in 2013, and by 2.6 per cent and 2.8 per cent for 2014 and 2015 respectively. Residential construction has been a positive contributor to GDP growth in 2013, but the pace of construction is near a maximum. GDP in Australia is estimated to grow by 2.6 per cent in 2013 and is forecast to grow by 2.8 per cent in 2014. While export growth will remain solid, investment in the mining sector is expected to peak in 2014. Growth in government consumption and public investment will decelerate. GDP in New Zealand is estimated to grow by 2.6 per cent in 2013 and is forecast to grow by 3.0 per cent in 2014, driven by growth of exports to Asian markets.

Among *developing countries*, Africa's growth prospects remain relatively robust. After growing by an estimated rate of 4.0 per cent in 2013, GDP is projected to accelerate to 4.9 per cent in 2014. Some of the pick-up in growth will come as a result of expected reversals of slowdowns due to particular circumstances, such as an end to the protests in Libya which decreased oil output and exports by serious measures. Growth prospects are expected to be supported by improvements in the global economic and regional business environment, relatively high commodity prices, easing infrastructural constraints, and increasing trade and investment ties with emerging economies. Other important factors contributing towards Africa's medium-term growth prospects include increasing domestic demand, especially a growing class of new consumers associated with urbanisation and rising incomes and improvements in economic governance and management. A moderate global growth recovery in 2014 underpinned by growth in emerging and developing countries, led by China, and projected improvement in the United States, the European Union and Japan, should also stimulate growth in Africa through increased trade, investment and capital flows.

After a notable slowdown in 2011-2012, economic growth in *East Asia* has stabilized at a moderate level in 2013. The region continues to be adversely affected by relatively weak external demand from developed economies, as well as an adjustment to lower growth in China. Growth of GDP is estimated to average at 5.9 per cent in 2013, the same pace as in 2012. A moderate pick-up in regional growth to 6.2 per cent is forecast for 2014 and 2015, mainly driven by a gradual recovery in export growth amid improving conditions in developed countries. In most East Asian economies, private consumption and investment will continue to expand at a solid pace, supported by stable labour market conditions, low inflation and fairly accommodative monetary policies. Fiscal policies will remain moderately expansionary and continue to provide support for growth.

Growth in *South Asia* remains lackluster as a combination of internal and external factors hamper activity, particularly in the region's largest economies, such as India, the Islamic Republic of Iran and Pakistan. On average, gross domestic product is estimated to expand by 3.8 per cent in 2013, close to the slowest pace in two decades. Growth is forecast to pick up moderately to 4.6 per cent in 2014 and 5.2 per cent in 2015, supported by a gradual recovery in domestic demand in India, an end to the recession in the Islamic Republic of Iran, and an upturn in external demand. However, in most economies, growth will likely remain well below the pre-2008 level. Private consumption and investment are held back by a wide range of factors, including energy and transport constraints, volatile security conditions, macroeconomic imbalances and lack of economic policy reforms.

Western Asia is estimated to grow by 3.4 per cent in 2013, and will accelerate to 4.5 per cent in 2014 and 2015. While the member countries of the Gulf Cooperation Council (GCC) have been on a stable recovery path, continuing political instability, social unrest, security incidents and geopolitical tensions hampered the economies of Iraq, Jordan, Lebanon, Syria and Yemen. The Syrian crisis has been impacting the neighboring countries in a multi-faceted way. The subdued cross-border economic activities between GCC countries and the rest of West Asia, including trade, investment and tourism, continued to fail in bringing intraregional positive spillover effects. The stagnation of private capital inflows put Lebanon, Jordan and Yemen under moderate foreign exchange constraints and was a source of inflationary pressure. For 2013, the growth rate of GCC member countries is expected to taper off mainly due to the moderate decline in oil export revenues. Non-oil sectors, particularly the real estate sector, regained their strength partly owing to active fiscal policy in this sub-region. In Turkey, financial markets have been under pressure since May 2013, with the currency depreciating and interbank interest rates rising as a result of the reversal in international capital inflows, triggered by the anticipated tapering in global liquidity, as well as concerns about the large public debt and the current account deficit in the country.

Economic growth in *Latin America and the Caribbean* has decelerated in 2013, with GDP estimating to grow by 2.5 per cent in 2013. Growth is forecast to pick up to 3.6 per cent and 4.3 per cent in 2014 and 2015 respectively. In South America, Brazil is still expanding below its potential growth rate, curbed by weak external demand, volatility in international capital flows and tightening monetary policy. The expected improvement in the outlook will depend on strengthening global demand. Private consumption has been supportive of growth in many South American economies. Growth in Mexico and Central America is expected to accelerate in 2014-2015, supported by better performance of manufacturing exports and stable domestic demand, as well as structural reforms. Growth in the Caribbean has been hampered by weak external demand, in particular for the tourism sector, and weaker commodity prices. Economic activity is expected to strengthen in 2014 and 2015.

Among economies in transition, growth in most economies of the *Commonwealth of Independent States (CIS)* decelerated in 2013, curbed by weak exports and external financing constants, supply-side bottlenecks, and weak consumer and business confidence. Growth in the Russian Federation weakened further in the first half of 2013, growing by only 1.4 per cent year on year, as industrial output remained weak and investment became a drag on growth. The economic slowdown eventually affected previously resilient consumer confidence and led to weakening retail sales growth. The weakness in the Russian Federation has had a negative impact on its neighbours in the CIS through the trade, investment and remittance channels. In the outlook, structural problems such as sluggish energy sector expansion, capacity constraints and weak investment will prevent an acceleration of growth to pre-crisis levels.

Growth in *South-Eastern Europe* has rebounded in 2013, but growth in the near term is expected to remain marginal, fluctuating between 1.0 per cent and 2.0 per cent, which is insufficient to address the region's long-standing needs for reindustrialization, increased labour force participation and reduction of excessively high unemployment rates. In the outlook, the external environment for those countries is expected to improve, including the terms of access to external finance. With the easing of credit conditions, investment is set to recover gradually in 2014-2015, along with the strengthening of private consumption. GDP growth is projected to accelerate to 1.9 per cent in 2014 and 2.9 per cent in 2015.

A benign global inflation outlook

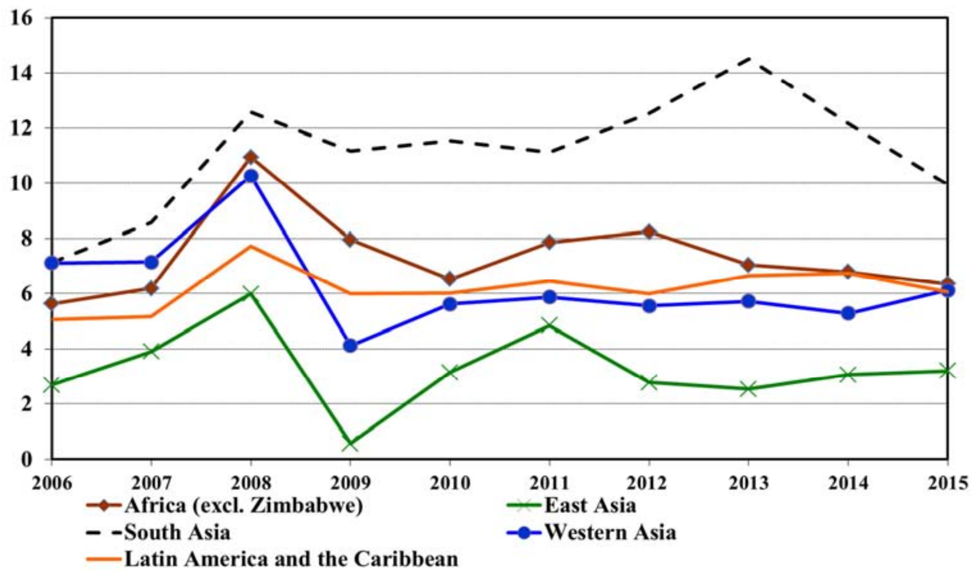
Inflation remains tame worldwide, partly reflecting output gaps, high unemployment and financial deleveraging. Among developed economies, inflation continued to decelerate in the United States and the euro area in 2013 and is expected to remain below 2.0 per cent in 2014 and 2015. In Japan, the large expansionary policies aiming to reflate the economy managed to end the decade-long deflation in 2013, as the CPI is estimated to increase by 0.3 per cent, and is forecast to hit the target of 2.0 per cent in 2014.

Among developing countries and economies in transition, inflation rates are above 10.0 per cent in only about a dozen economies scattered in different regions. Several economies in South Asia and Africa, in addition to a few in the CIS, will continue to face high inflation rates, mainly owing to elevated inflationary expectations, rapid credit growth, localized food price pressures and structural bottlenecks such as energy shortages. On the other hand, most economies in East Asia continue to face benign inflation (figure 2).

Unemployment situation

The global employment situation remains relatively unchanged from the previous year. Long lasting effects from the financial crisis continue to influence the circumstances of many countries and regions. In particular, the downturns and subsequent fiscal tightening have continued to depress demand in the United States and much of the euro zone (figure 3). Unemployment in the United States has continued its slow decline, down to 7.3 per cent in late 2013, from a peak of 10.0 per cent in 2010. A significant portion of this decline is owing to labour force participation rates. Long-term unemployment has declined recently, but rates of workers claiming disability, recourse for those who have had significant trouble in finding new employment, have risen. The unemployment rate is expected to slowly decline and reach the Fed's critical threshold of 6.5 per cent sometime in mid-2015.

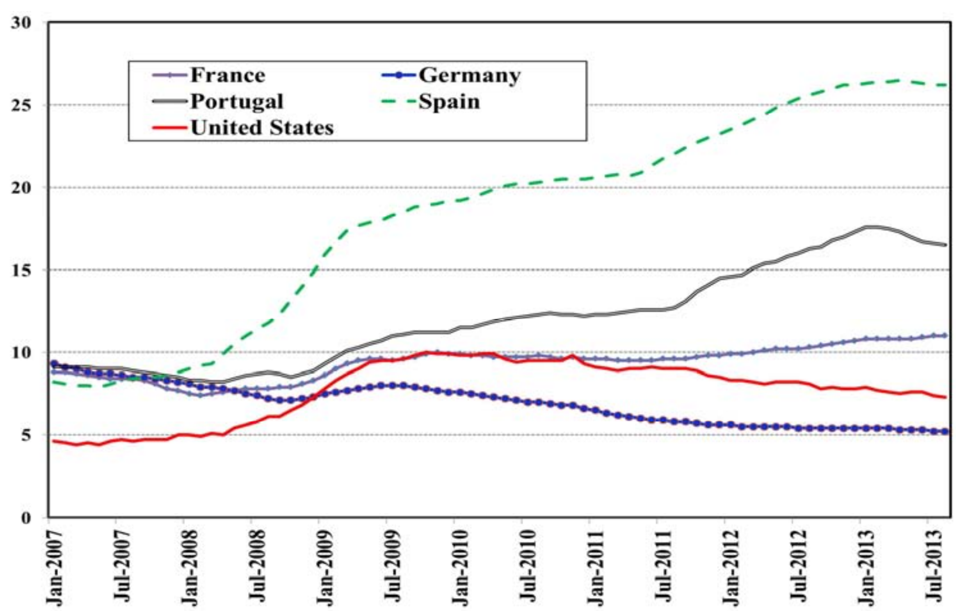
Figure 2. Inflation in developing countries, 2006-2015 [a]
(Annual percentage change)



Source: UN/DESA

[a] 2013-2015 are forecasts.

Figure 3. Unemployment rates in selected countries: January 2007-August 2013
(Percentage of labour force)



Source: EUROSTA and United States Bureau of Labor Statistics.

The persistent rise in unemployment in the euro area appears to have stabilized over the course of the year, at around 12.0 per cent for the past seven months. The unemployment situation in the euro zone masks a wide disparity between some countries, such as Germany, with an unemployment rate near historic lows, 5.2 per cent in September, and other countries such as Spain and Greece with extraordinarily high unemployment rates, 26.6 per cent in July and 27.6 per cent in August, respectively. The youth unemployment rates are double of these. These high rates are expected to gradually come down, but the growth momentum will not be strong enough to make significant progress over the forecast period. In addition, there will be lasting damage to the labour market from discouraged workers who have been unemployed for significant periods of time.

Japan is the only developed country that has moved away from restrictive fiscal policies, though their unemployment rate continued to be low even prior to the enactment of those policies. The labour force participation rate in Japan continues to decline as the working-age population shrinks, which has contributed to maintaining low unemployment rates for many years. Unemployment is expected to decline slowly along with the moderate growth over the forecast period.

The picture is mixed across developing countries with, for example, reasonably steady employment rates across East Asia and problematic rates of unemployment in North Africa and Western Asia, particularly among youth. The slow growth in developed economies has put pressure on labour markets in some developing countries which have more direct economic connections to those economies. Despite slowing economic conditions in many major developing countries, employment in those countries has remained relatively stable. The unemployment rate remains at historic lows in the Russian Federation, between 5.0 per cent and 6.0 per cent, despite a noticeable slowdown and in-migration from surrounding countries in the CIS.

Even as growth faltered in major economies in South America, such as Brazil and Mexico, the unemployment remained around 6.0 per cent or below. Labour market indicators are likely to remain solid over the remainder of the year for the region, but may not see further improvements in the near future, despite improvements in growth.

Unemployment rates remain low across much of East Asia, estimated at below 3 per cent in Malaysia, Singapore, Thailand and Viet Nam. In the outlook period, there is expected to be little change based on the modest growth forecast for the coming two years. In South-East and South Asia, however, the official employment statistics are relatively problematic owing to significant portions of the labour force employed in the informal sector. Slowing growth rate in South Asia appears to have had a considerable adverse impact on employment. Reported unemployment still remains relatively low in India and has deteriorated somewhat over the past fiscal year. Structural issues in some of these economies have aggravated already significant gender gaps with high female unemployment rates in Pakistan and low female participation in Bangladesh. Modest growth in the outlook period combined with population pressures is likely to exacerbate pressures on the labour market.

Positive growth in many African countries has had limited impacts on employment as informality remains rampant and limited opportunities for many of those seeking to enter the labour market. This manifests in high youth unemployment rates and wide gender disparities in earnings. In addition, continual pressure on labour markets from a steady stream of new entrants has meant that even solid GDP growth rates have not been sufficient to make measureable impacts.

2. Trends in international finance and trade

Capital inflows to developing countries reversing along with heightened volatility

Net private capital inflows to emerging markets, a sub-group of developing countries, and the economies in transition, have shown a measurable reversal during 2013. In addition there has been significantly increased volatility in the financial markets of emerging economies, featuring equity markets sell-offs and sharp depreciations of local currencies. The reversal and the volatility intensified especially after May 2013 when the United States Federal Reserve (Fed) announced the possibility of tapering the amount of its monthly purchases of long-term assets later in the year. Waning growth prospects for emerging economies have also played a role in triggering the reversal of capital inflows. Total net private capital inflows to emerging economies are estimated to be $1,050 billion in 2013, down by about 12.0 per cent from the previous year.[3] In the outlook for 2014-2015, downward pressures on capital inflows to emerging economies may continue, with risks of broader and greater turbulence in financial markets, as major central banks in developed countries are expected to start “normalizing” their monetary policy stances from the current crisis-responding mode.

After plunging to $658 billion in 2008 from the peak of $1241 billion in 2007, net private capital inflows to emerging economies had been on the road to a rapid recovery until 2012. By the end of 2012, net inflows had almost fully recuperated, to $1215 billion, while portfolio equity inflows and non-bank credit inflows, which are the most volatile components in the capital inflows to emerging economies, surged to surpass the previous peak levels by about 50 per cent and 100 per cent respectively.

The unconventional monetary policies, or so-called quantitative easing (QE), major central banks adopted in the aftermath of the global financial crisis have had a significant influence on the net capital inflows to emerging economies. The QE programmes injected substantial liquidity into global financial markets and at the same time repressed long-term interest rates in developed countries. In a search for higher yields, capital flows were driven to international markets for primary commodities and emerging markets’ equities and bonds over the past few years. In late 2012 and early

[3] Data up to 2012 are based on Institute of International Finance, “Capital flows to emerging market economies”, 7 October 2013, but the outlook is based on Project LINK.

2013, as systemic risks associated with the sovereign debt crisis in the euro area abated and the prospects for economic recovery in the United States and Japan improved, international capital flows started to move away from emerging markets back to developed markets, particularly developed equity markets. More recently, on the expectation that major central banks will taper their purchases of long-term assets and eventually sell their assets back to the markets, international investors have ratcheted up their adjustment in re-pricing assets and rebalancing portfolios, leading to the latest wave of reversals of capital inflows to emerging economies. Given the prodigious size of the assets accumulated by major central banks through QE in the past few years and the challenges for determining the timing and magnitude of unwinding these assets, more volatile movements of capital inflows to emerging economies are expected to occur in the next few years.

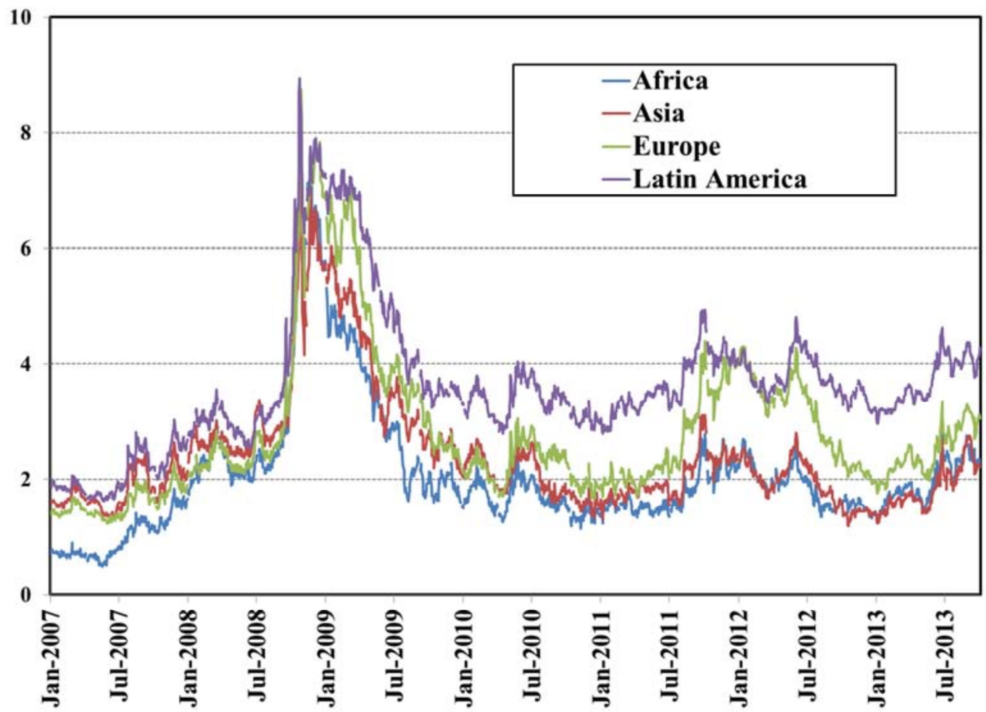
Among emerging economies, reversals and volatility in capital inflows have been most pronounced in Asia. While growth in foreign direct investment inflows to China seems to have resumed lately, portfolio equity inflows to India and Korea and nonbank credit flows to Indonesia have registered significant falls. Latin America has also seen a notable retrenchment of inflows, mostly in portfolio equity. In contrast, Africa, Western Asia and emerging European countries continue to see increases in capital inflows. For example, in the past year Nigeria has registered significant increases in capital inflows to both its equity and bond markets. Egypt has, however, witnessed sharp declines in net private capital inflows due to a continued political instability.

External financing costs for developing countries and transition economies have also risen in the second half of 2013, triggered by the anticipation of QE tapering. The spreads between yields on sovereign bonds issued by emerging economies and the benchmark yields on government bonds of major developed countries surged by more than 100 basis points in the two weeks immediately following the Fed’s announcement in May 2013 of the possibility of reducing the size of its QE purchases (figure 4). By taking into account that the benchmark yields on government bonds in major developed countries also increased by about 100 basis points, the costs of external financing for emerging economies, in terms of the yields, actually increased 200 basis points on average. Among emerging economies, the spreads for Latin America are wider than others, as the risk premia for the region are still perceived to be higher than others due to the more frequent incidences of default in the past.

Outward capital flows from emerging economies have continued to increase. In addition to a continued increase in *official foreign reserves*, which are counted as part of outward capital flows and stood at about $7.5 trillion by mid-2013 for emerging and developing countries as a whole, *private outward capital flows* of emerging economies have increased in the past few years at a robust pace, reaching an estimated amount of about $1000 billion in 2013, almost to the same level as the net capital inflows to these countries. Among emerging economies, China has significantly increased its outward direct investment in recent years, supported by more encouraging government policies promoting its enterprises to “walk abroad”. After registering a total of $88 billion in outward direct investment in 2012, available data have indicated another increase of 18 per cent in the first eight months in 2013. Many economies in Latin America, such as

Mexico, Chile, Brazil, Colombia and Peru, have also increased outward capital flows, mostly in the form of portfolio investments, reflecting the need by companies, banks and pension funds in Latin America to internationally diversify their assets. The overall increases in outward capital flows of emerging economies are considered to be potentially helpful in offsetting the adverse effects of the reversal in capital inflows to these countries, but this argument needs to be tested.

Figure 4. Daily yield spreads on emerging market bonds, January 2007-October 2013 (Percentage points)



Source: JP Morgan Chase.

ODA flows to developing countries contracted in the past two years, falling cumulatively by 4.0 per cent in two years of 2011 and 2012, down to $125.9 billion. Sixteen of the 25 Development Assistance Committee (DAC) members decreased their ODA, owing mainly to fiscal austerity measures. Multilateral ODA and humanitarian aid fell by about 6.0 per cent and 11.0 per cent, respectively. Bilateral ODA increased slightly, by about 1.0 per cent, but bilateral ODA to least developed countries (LDCs) fell by 12.8 per cent in real terms, to about $26 billion in 2012. Preliminary data show that bilateral aid from DAC donors to sub-Saharan Africa fell for the first time since 2007, with assistance totalling $26.2 billion in 2012, a decline of 7.9 per cent in real terms. Aid to landlocked developing countries (LLDCs) and Small Island Developing States (SIDS) also fell in 2011.

In 2012, the combined DAC donors' ODA was equivalent to 0.29 per cent of their combined gross national income (GNI). This widened the delivery gap in reaching the United Nations target—for donor countries to provide 0.7 per cent of GNI annually—from 0.39 per cent of GNI in 2011 to 0.41 per cent in 2012. The gap between DAC donors' ODA to LDCs and the lower bound of the United Nations target of 0.15 per cent has widened to 0.05 per cent of donor GNI. In the outlook, ODA flows in 2013 are estimated to remain at the same level as in 2012, and slight increases are expected for 2014-2015, as more DAC members see improvement in their economies and fiscal situations, along with a strengthening of political commitment in the international community spurred by the United Nations campaign for accelerating progress in the MDGs.

Currencies of developing countries under depreciation pressures

Two distinctive episodes have featured in foreign exchange markets during 2013: the early part of the year was highlighted by a dramatic depreciation of the Japanese yen, and the second notable event has been the sharp devaluation of the currencies in a number of emerging and developing countries since May 2013. In the outlook for 2014-2015, major uncertainties and volatility in foreign exchange markets will still be associated with the currencies of emerging economies, as well as the Japanese yen.

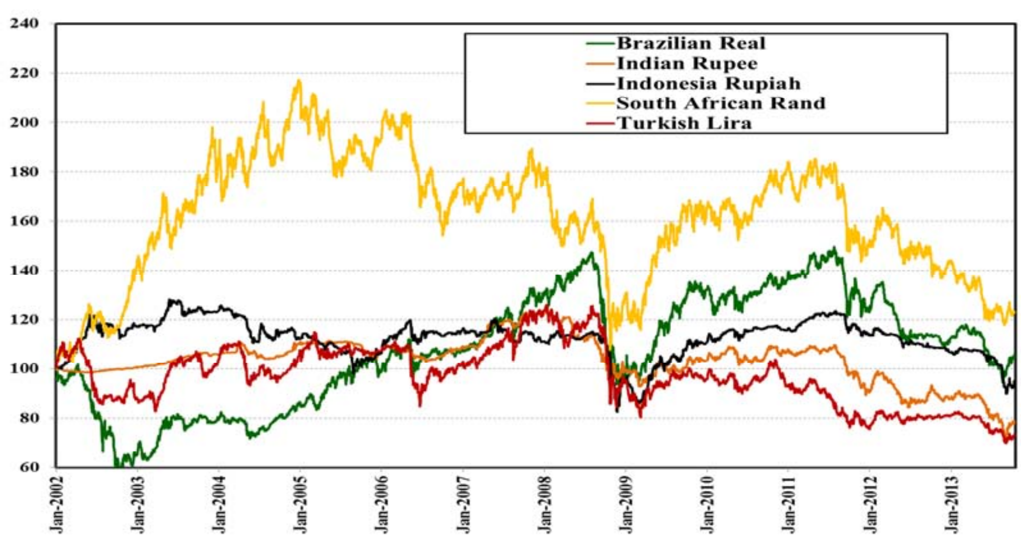
Among major currencies, the decades-long trend of appreciation of the Japanese yen against the dollar seemed to have reached a turning point in late 2012 and early 2013. As the new Japanese Administration initiated a set of drastically expansionary policies, including setting an inflation target of 2.0 per cent and increasing QE and government spending, the yen devalued by about 20 per cent vis-à-vis the United States dollar, from 80 yen/dollar by the end of 2012 to about 100 yen/dollar in March 2013. It has since stabilized within a small range of about 98 yen/dollar. In contrast, the exchange rate between the euro and the dollar has maintained considerable stability during 2013, fluctuating within a very narrow range about 1.3 dollar/euro, as almost no changes have occurred in the bilateral differentials in interest rates and inflation between the United States and the euro area (figure 5). Subdued risks of the European debt crisis which have favoured the euro have been balanced by the better economic growth which has favoured the dollar. In the outlook, the dollar is expected to appreciate moderately against both the yen and the euro, mainly reflecting a stronger growth outlook for the United States versus the other two major economies.

Currencies in many developing countries and economies in transition have depreciated vis-à-vis the United States dollar and other major currencies in 2013. Currencies in a number of emerging economies depreciated the most in May-June 2013, particularly in Brazil, Indian, Indonesia, South Africa and Turkey (figure 6), along with a reversal in capital inflows to these economies. In contrast, the renminbi of China continued to appreciate, gradually, against the United States dollar and other major currencies. The difference between the trends in the exchange rates of China and other large emerging economies lies in a number of factors, including much higher foreign reserves, a less open capital account, higher domestic savings, and more concentration of foreign direct investment in the capital inflows to China, when compared with the other emerging economies. The renminbi is expected to further appreciate slightly against the dollar in 2014-2015, unless China liberalises its capital and financial accounts, which could trigger reminbi depreciation. The currencies of other emerging economies are likely to remain under depreciation pressures.

Figure 5. Exchange rate among major currencies, January 2007-October 2013 (Index [a], 2 January 2002 = 100)

Source: JP Morgan Chase, indexed by UN/DESA.
[a] Higher value of index means appreciation vis-à-vis the United States dollar**.**

Figure 6. Exchange rate of selected emerging economies, January 2007-October 2013 (Index [a], 2 January 2002 = 100)



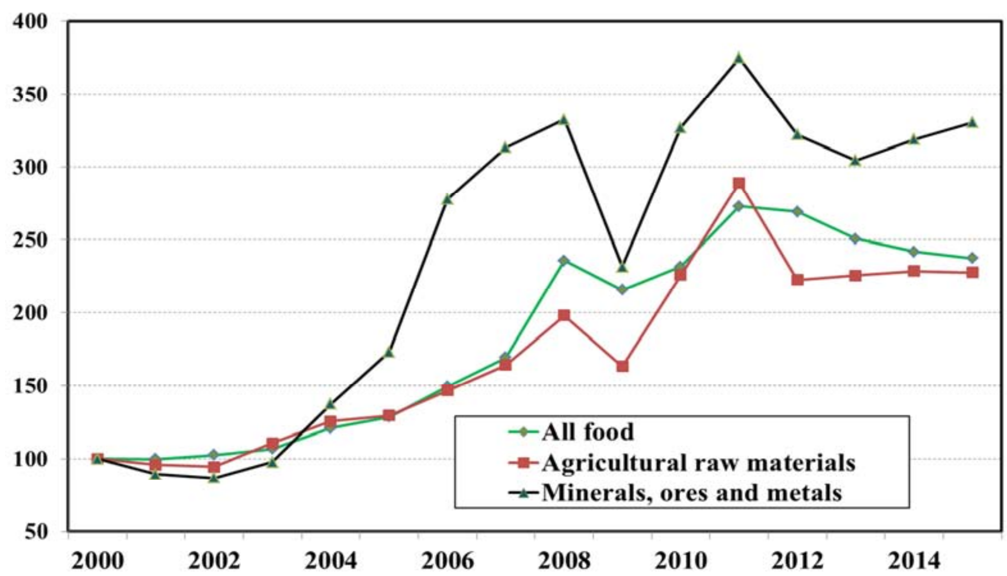
Source: JP Morgan Chase, indexed by UN/DESA.
[a] Higher value of index means appreciation vis-à-vis the United States dollar**.**

Prices of primary commodities continue to moderate

The prices of most primary commodities have declined moderately during 2013 (figure 7), driven mainly by generally weak global demand as the global economic growth remained anaemic. Different patterns continue to be evident across different commodity groups, as they are also determined by various factors on the supply side. In the outlook, as global demand is expected to pick up moderately in 2014-2015, commodity prices are expected to be flat compared with that in 2013, though they are still subject to supply-side factors, such as weather conditions for agricultural commodities and geo-political tensions for oil.

Oil prices were on a downward trend in the first half of 2013, as global demand for oil weakened along with the deceleration in overall world economic growth. A moderation in the growth of emerging economies was particularly notable, as they are the major sources for the incremental increases in global oil demand in recent years. However, oil prices surged in July-August as geopolitical tensions over Syria escalated. Brent increased by about $18/bbl to over $117/bbl within two months. Later, when progress was made in Syria's agreement to surrender its chemical weapons, Brent retreated to $108/bbl in September.

Figure 7. Price indices of commodities, 2000-2015 [a]
(Index, 2000 = 100)



Source: UN/DESA, based on UNCTAD information.
[a] 2013 - 2015 are forecasts by UN/DESA.

Geo-political tensions can entail a large risk premium on oil prices, particular when oil supply is also tight. Most recently, global oil supply has been declining modestly: increased oil supply in North America has been offset by declines in the North Sea, while high Saudi output only partly counterbalanced a collapse in the Libyan production.

In the outlook, global demand for oil is expected to grow above 1.0 per cent for 2014, moderately stronger than 2013. By assuming no further significant eruptions in geopolitical tensions, Brent is expected to be around $108/bbl for 2014-2015, compared with an estimated average of $108.1/bbl for 2013 and $111.6/bbl in 2012.

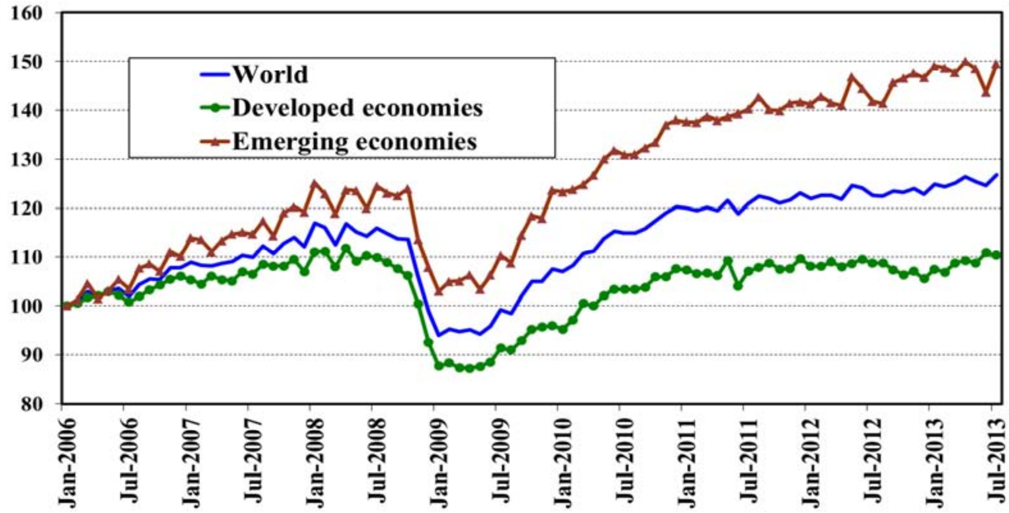
Food prices declined steadily during 2013, with prices for wheat, maize and rice declining by about 5-10 per cent, as production is expected to increase by a large margin in 2013/2014. In the outlook, food prices are projected to moderate further in 2014-2015 based on the assumption of continued increases in the global production of these grains.

Prices of minerals, ores and metals strengthened in early 2013 but fell markedly in the latter part of the year, due to weaker than anticipated global growth, particularly a notable deceleration in the growth of emerging economies, such as China. For example, price indices for aluminium, copper, nickel, and zinc registered a steady decline during 2013, falling by about 10.0 per cent. The price of iron ore also declined significantly. In the outlook for 2014-2015, the prices of minerals, ores and metals are projected to stabilize and register modest gains, as global demand improves.

International trade flows remain sluggish

International trade as the engine for global growth has shifted to a low gear over the past two years. After growing at a sluggish pace of less than 3.0 per cent in 2012, measured by the volume of world exports, international trade flows expanded at 2.4 per cent during 2013 (figure 8). Notably, the ratio between the growth of world trade and the growth of global output is at a historical low. While protracted anaemic import demand from major developed countries can explain part of the cyclical downturn in trade activity, the lack of any progress in multilateral trade negotiations over the past decade may have reduced the momentum in creating new trade flows in the world economy. In addition, certain protectionist measures adopted by a number of economies in the aftermath of the financial crisis, as well as other inward-looking policies, though all on a small scale, may have also added some friction to the engine of the international trade system. The feedback effects of slow international trade growth have in turn dragged down the growth of global output.

Figure 8. Index of world merchandise trade, January 2006-July 2013.
(Index, January 2006 = 100)



Source: CPB Netherlands Bureau for Economic Policy Analysis; re-based by UN/DESA.

In the outlook, international trade is expected to pick up the momentum gradually, growing at 4.8 per cent and 5.3 per cent in 2014 and 2015 respectively.

Impasses in multilateral trade negotiations versus booming regional negotiations

The World Trade Organization (WTO) Doha round of multilateral trade negotiations remains unresolved and there are limited hopes for resolution, though there have been some recent steps towards a pared down "Doha-lite" agreement. There are three areas of possible progress: trade facilitation, though there are divides on customs formalization; some of the agricultural agreements with some progress on exemptions for domestic support for subsistence agriculture, though the administration of tariff rate quotas remains a sticking point; and some development related issues such as special treatment for goods and services exports of LDCs. There are hopes that these issues can be resolved at the upcoming Ninth Ministerial Conference of the WTO taking place in Bali in December. Beyond that there remain a host of other outstanding unsolved issues from the Doha round which has motivated many countries to seek solutions in smaller multilateral agreements or bilateral agreements.

In contrast, regional trade negotiations continue to mushroom. In the coming months there are two large regional trade agreements under negotiation: the Trans-Pacific Partnership (TPP)[4] and the Transatlantic Trade and Investment Partnership (TTIP)[5]. These agreements would cover around two-thirds of global production and a significant

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[4] Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States, and Vietnam.
[5] European Union and United States

portion of world trade. There are still a number of issues that have to be hammered out in the TPP which is likely to delay its conclusion for some time. A recent petition by a bipartisan majority of United States Senators to address “currency manipulation” in these talks also has the potential to derail the process. The negotiations for the TTIP are just beginning and have already experienced some friction around the protection of some domestic industries which could draw out the process.

An important issue with regards to these regional negotiations is the degree to which many developing countries are excluded. It is not clear whether this is voluntarily with some countries continuing to support the WTO processes or whether they have not been invited to participate. This may put them at a disadvantage both economically and politically as they could be excluded from important markets or they could be forced to accept unfavourable future agreements based on their outsider status.

As a counterpoint to the TPP, China has been working to complete the Regional Comprehensive Economic Partnership (RCEP)[6] by 2015. This agreement would create the world’s largest trade bloc and would cover 40.0 per cent of the world trade–a greater fraction than the TPP. The RCEP framework is less comprehensive than that of the TPP and is geared more towards streamlining existing regional trade arrangements. A number of countries are covered by both negotiations so there are possibilities for linking the two arrangements.

There are also on-going talks surrounding a revision of the Trade in Services Agreement (TiSA) involving the European Union, Japan, United States and a number of other countries[7], comprising around 70.0 per cent of world services trade. These countries have opted to negotiate amongst themselves due to mounting frustration with stalled talks within the WTO.

Some previous agreements are fragmenting, which can be observed with Brazil’s overtures to the EU for a trade agreement, outside of Mercosur[8]. In addition, the formation of the Pacific Alliance[9] forms a counterpoint to Mercosur in Latin America, which could complicate the regional trade dynamics. A number of other countries such as Canada and Costa Rica have expressed interest in the Pacific Alliance.

Global imbalances have narrowed to a benign level

Global imbalances, namely, the current account imbalances across major economies, continued to narrow in 2013 (figure 9), to a benign level, which is not considered to be an imminent threat to the stability of the world economy, although

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[6] Australia, Brunei Darussalam, Cambodia, China, Japan, India, Indonesia, Laos, Malaysia, Myanmar, New Zealand, the Philippines, Singapore, South Korea, Thailand and Vietnam.

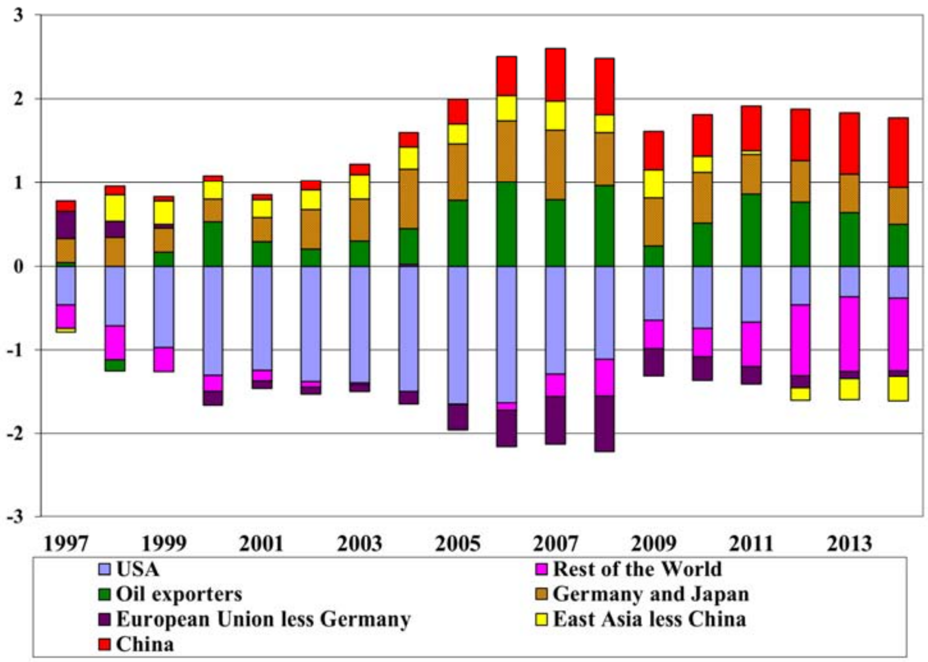
[7] Australia, Canada, Chile, Chinese Taipei, Colombia, Costa Rica, European Union, Hong Kong, Iceland, Israel, Japan, Mexico, New Zealand, Norway, Pakistan, Panama, Paraguay, Peru, the Republic of Korea, Switzerland, Turkey and the United States.

[8] Argentina, Brazil, Uruguay and Venezuela (Paraguay was suspended last year).

[9] Chile, Columbia, Mexico and Peru.

efforts should continue towards strengthening international policy coordination to prevent the imbalances from widening to excessive levels again in the longer run.

Figure 9. Global imbalances, 1997-2014.
(Current account balances in per cent of world gross product, WGP)



Source: IMF *World Economic Outlook* database, October 2013 for historical data, and Project LINK for the forecasts in 2013-2014.

The United States remained the largest deficit economy, with an estimated external deficit of about $410 billion (2.4 per cent of GDP) in 2013, down from $450 billion in 2012 and substantially lower than its peak of $800 billion (6.0 per cent of GDP) registered in 2006. The external surpluses in China, the euro area, Japan and a group of fuel-exporting countries, which form the counterpart to the United States deficit, have narrowed accordingly, albeit to varying degrees. China, for instance, is estimated to register a surplus of just above 2.0 per cent of GDP in 2013, a sharp decline from a high of 10.0 per cent of GDP in 2007. Japan is expected to register a surplus of about 1.0 per cent of GDP in 2013, also a significant reduction from its peak level of 5.0 per cent of GDP reached in 2007. While within the euro area, Germany's surplus remains above 5.0 per cent of GDP, the current account for the euro area as a whole is in surplus of 2.5 per cent of GDP. Large surpluses relative to GDP are still present in oil-exporting countries, reaching 20.0 per cent of GDP or more in some of the oil-exporting countries in Western Asia.

While some of the adjustment of the imbalances in major economies reflects certain improvements in the unbalanced domestic structure of these economies, a large part of the adjustment reflects a cyclical downturn, i.e. a weakening in external demand from the deficit countries, rather than a strengthening of external demand from the surplus countries. In the United States, after exports rebounded for a couple of years in the wake of the crisis, both exports and imports have decelerated markedly in 2012 and 2013. Domestically, a corresponding narrowing of the saving-investment gap reflects a slight decline in the savings rate in 2013 and a large moderation in investment: the household saving rate, which increased from about 2.0 per cent of disposable household income before the financial crisis to above 5.0 per cent in the past few years, has actually declined slightly during 2013, to about 4.5 per cent, but the investment growth slowed down more significantly. The government deficit has improved significantly, by 2.5 percentage points of GDP, dropping from 8.3 of per cent of GDP in 2012 to 5.8 per cent in 2013, with government revenue rising by 2.0 percentages points of GDP and government spending dropping by 0.5 percentage points of GDP. In the outlook for 2014-2015, the current account deficit in the United States is expected remain at the same level relative to GDP.

In the surplus countries, the narrowing in the external surplus of China reflects a confluence of a more flexible exchange rate and the policy measures to move the economy towards greater reliance on domestic demand. The corresponding narrowing of the saving-investment ratio in China came mainly from a notable slowdown in the growth of investment, along with a slight widening of the government deficit. In Japan, the narrowing of its external surplus has, to some extent, reflected the strengthening of its domestic demand, driven by expansionary fiscal and monetary policy. The surpluses in oil-exporting countries are of a quite different nature from other economies, as these countries will need to share the wealth generated by the endowment of oil with future generations via a continued accumulation of surpluses in the foreseeable future, but some studies warn of a slowdown in oil exports for the Russian Federation in the medium run.

Given current trends, global imbalances are not expected to widen by a significant margin in the coming two years to become an imminent threat to the stability of the global economy, although the large net liability position of the United States is a concern for the stability of the exchange rates among major currencies. Should the global economy fall into another recession, the imbalances could narrow further, though in a more counterproductive way.

3. Uncertainties and risks

The baseline outlook presented above is subject to a number of uncertainties and risks, mostly on the downside. In the last LINK meeting of 2012, three major downside risks were delineated for the global outlook of 2013, namely, the risk of a much more detrimental adjustment in the euro area, the risk of a “fiscal cliff” in the United States, and the risk of a hard landing in some large emerging economies. All of these three risks have partially manifested during 2013 and adversely impacted the global economy, although not to the full scale as presented in the downside scenarios. In the outlook for 2014-2015, these risks remain relevant. While the systemic risks in the euro area have abated due to a number of policy measures adopted in the European Union over the past year, the real economy in the euro area, particularly in those member countries under debt distress, remains fragile. The United States has averted a “fiscal cliff” in 2003, but fell into the fiscal sequestration, and the uncertainties remain high about the debt ceiling and the budget for 2014. The slowdown in a number of emerging economies in 2013 has been “hard” enough, and although it may not qualify as a “hard landing”, many of these emerging economies remain vulnerable in the outlook.

In addition to these old risks, new risks are also emerging. One of them is the risk associated with the unwinding of the unconventional monetary policies by the central banks of major developed countries over the course of 2014-2015. As indicated by the mini crisis of mid-2013, when the United States Fed simply mentioned the possibility of tapering its purchases of assets (tapering should have far less impact than unwinding, as the former continues to add liquidity while the latter withdraws liquidity), this risk could cause substantial instability for the world economy. Moreover, beyond economic risks, geopolitical tensions in West Asia and elsewhere in the world might spiral out of control, leading to economic disruptions directly, or indirectly through rising oil prices. These and other risk factors, unfolding unexpectedly, could derail the world economy far away from the projections outlined in the baseline forecast.

Uncertainties and risks associated with the QE

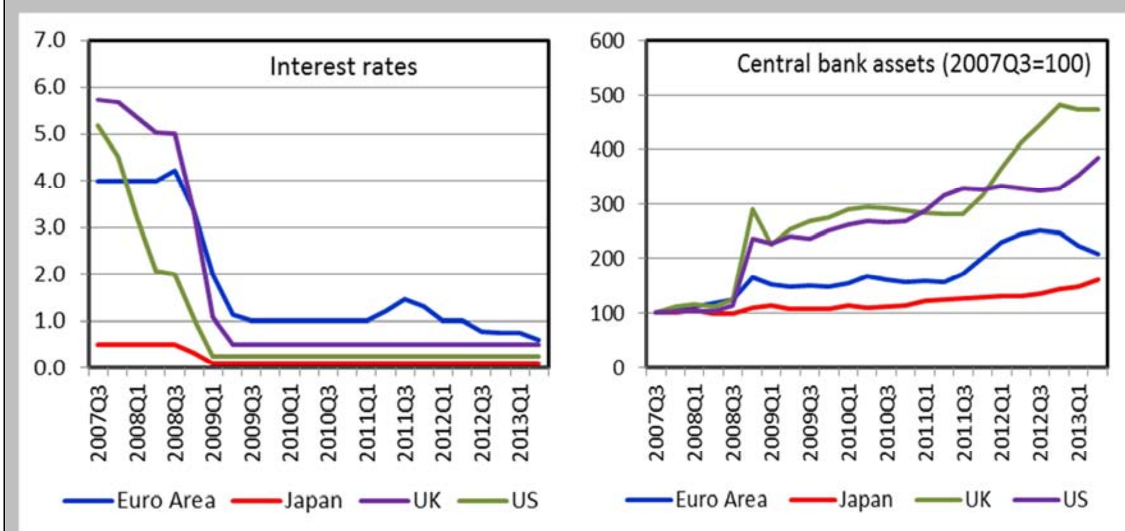
Great uncertainties and risks for global economic growth and the financial stability of the world in the coming years are inextricably associated with the unconventional monetary policies adopted in major developed countries, or more precisely when the central banks of these countries start to change their stances on these policies.

Since the eruption of the global financial crisis in 2008, central banks in major developed countries have implemented the so-called quantitative easing (QE)-a series of programmes to increasingly purchase and hold large amounts of long-terms assets (see Box 2). These policy measures have played a critical role in stabilizing financial markets, injecting liquidity to the beleaguered banks and providing necessary support for economic recovery in general, although the significance of these positive effects is still under debate. However, by moving a prodigious amount of financial assets from financial markets to their own balance sheets, these central banks have also created nontrivial market distortions. This has occurred through repression in the risk premiums for certain classes of financial assets which may have lead to misallocation of certain assets in the portfolios of investors, as well as through the generation of moral hazard for commercial banks by allowing them to delay the clean-up of the balance sheets and necessary other adjustments.

Box 2: Unconventional monetary policy in major developed countries[10]

Following the global financial crisis, in the face of near-zero short term interest rates, central banks in major developed economies have turned to unconventional monetary policies, through purchasing and holding of long-term assets to expand their monetary bases. These policies have been dubbed quantitative easing (QE) by the general public. The United States Federal Reserve (Fed), the Bank of England (BoE), the European Central Bank (ECB) and the Bank of Japan (BoJ) have conducted these policies on a very large scale. Figure 2.1 shows the evolution of short term interest rates in these countries and the size of individual banks' balance sheets (normalised to 100 at the beginning of August 2008), which reflects the scale of unconventional monetary policy actions.

Figure 2.1. Conventional and unconventional monetary policy in major developed countries since the beginning of the crisis



Unconventional monetary policy measures applied by the major central banks included both direct asset purchases and various lending programmes. Initially, the QE programmes enacted by these central banks were implemented to restore the functioning of the dysfunctional financial markets; later the concern shifted to stimulating the economy. The details of QE plans varied across central banks and depended on their specific motivations and the differing structures of the economies in individual countries. For example, the Fed's and BoE's QE programmes differed from those of the BoJ and the ECB in that the former concentrated on bond purchases rather than on direct lending to banks. The differences between the economies, with bond markets playing a relatively more important role in the United States and the United Kingdom and the banks playing a

[10] This box summarizes key findings from Tatiana Fic, "The spillover effects of unconventional monetary policies in major developed countries on developing countries", October 2013, a paper submitted to Project LINK.

relatively more important role in continental Europe and Japan, influenced the choice of tools.

Federal Reserve

The QE in the United States can be categorised into three rounds. The first round, QE1, was announced from November 2008 to March 2009 and its scale oscillated around $1.725 trillion (table 2.1). The QE2 programme worth $600 billion was announced in March 2011; and it was followed by Operation Twist, worth $667 billion, announced in September 2011, and extended in February 2012. The QE3 programme was announced in September 2012, and assumed asset purchases worth $85 billion per month (gradual increases). Due to its open-ended nature, QE3 has sometimes been called “QE-Infinity”. On 19 June 2013, the Fed announced the possibility for tapering of the size of QE3, contingent upon continued positive economic data.

Table 2.1. FED announcements concerning unconventional monetary policy measures

Date	Brief description
28 Nov 2008	QE1: Fed will purchase $100 billion in government-sponsored enterprise (GSE) debt and $500 billion in mortgage backed securities.
18 Mar 2009	QE1 expanded: Fed will purchase $300 billion in long term Treasuries and $750 billion in mortgage-backed security (MBS), and $100 billion in MBS.
11 Mar 2010	QE2: Fed will purchase $600 billion in Treasuries.
21 Sep 2011	Operation TWIST, Fed will purchase $400 billion in Treasuries (with remaining maturities of 6 to 30 years and sell an equal amount with remaining maturities of 3 years or less).
20 Feb 2012	Operation TWIST extended: Fed will continue to purchase long term securities and sell short term securities; at the pace of about $45 billion per month.
13 Sep 2012	QE3: Fed will purchase $40 billion of MBS per month.
12 Dec 2012	QE3 expanded: Fed will continue to purchase $45 billion of long term Treasuries per month without sterilisation.

Bank of England

The BoE asset purchasing announcements can be separated into two distinct periods. In the first period, between January and November 2009, the BoE gradually increased the value of asset purchases (Table 2.2), from £50 billion in January, to £75 billion in March, and then £125 billion, £175 billion and £200 million in May, August, and November, respectively. The second stage of the British QE began in October 2011 with the BoE raising the asset purchase ceiling to £275 billion. The Bank expanded the programme further, in February 2012 and July 2012, setting the ceiling at £325 billion, and £375 billion, respectively.

Table 2.2. BoE announcements concerning unconventional monetary policy measures

Date	Brief description
28 Nov 2008	QE1: Fed will purchase $100 billion in GSE debt and $500 billion in mortgage backed

	securities.
18 Mar 2009	QE1 expanded: Fed will purchase $300 billion in long term Treasuries and $750 billion in MBS, and $100 billion in MBS.
11 Mar 2010	QE2: Fed will purchase $600 billion in Treasuries.
21 Sep 2011	Operation TWIST, Fed will purchase $400 billion in Treasuries (with remaining maturities of 6 to 30 years and sell an equal amount with remaining maturities of 3 years or less).
20 Feb 2012	Operation TWIST extended: Fed will continue to purchase long term securities and sell short term securities; at the pace of about $45 billion per month.
13 Sep 2012	QE3: Fed will purchase $40 billion of MBS per month.
12 Dec 2012	QE3 expanded: Fed will continue to purchase $45 billion of long term Treasuries per month without sterilisation .

European Central Bank

The two covered bond purchase programmes have been relatively moderate in size, though they represent larger purchases of private assets than any other central bank. The ECB announced the purchase of €60 billion in euro denominated covered bonds in 2009 and €40 billion in 2011 (Table 2.3), for a total of €100 billion. The ECB never announced a target for sovereign debt purchases under the securities markets programme. Most of these assets were purchased during two episodes: spring-summer 2010 (with a focus on Greek, Irish, and Portuguese debt), and summer-fall 2011 (with a focus on Italian, Spanish, Portuguese and Irish debt). The ECB asset purchases totalled around €320 billion. Most of them have been sterilised. The path of the ECB's monetary base reflects extensions of the long term refinancing operations (LTRO) programme.

Table 2.3. ECB policy announcements concerning unconventional monetary policy measures

Date	Brief description
28 Nov 2008	QE1: Fed will purchase $100 billion in GSE debt and $500 billion in mortgage backed securities.
18 Mar 2009	QE1 expanded: Fed will purchase $300 billion in long term Treasuries and $750 billion in MBS, and $100 billion in MBS.
11 Mar 2010	QE2: Fed will purchase $600 billion in Treasuries.
21 Sep 2011	Operation TWIST, Fed will purchase $400 billion in Treasuries (with remaining maturities of 6 to 30 years and sell an equal amount with remaining maturities of 3 years or less).
20 Feb 2012	Operation TWIST extended: Fed will continue to purchase long term securities and sell short term securities; at the pace of about $45 billion per month.
13 Sep 2012	QE3: Fed will purchase $40 billion of MBS per month.
12 Dec 2012	QE3 expanded: Fed will continue to purchase $45 billion of long term Treasuries per month without sterilisation.

Bank of Japan

The BoJ has purchased almost ¥187 trillion in total assets over the period January 2009-December 2012 (Table 2.4). However, around 40.0 per cent of this quantity should be attributed to the BoJ QE policy of the early 2000s. The BoJ began purchasing government bonds in 1990 and in 2002 these purchases reached ¥1.2 trillion per month. In 2006 BoJ exited from its QE programme, and reduced its balance sheet by letting short term assets mature without replacement. However, it kept purchasing government bonds at a pace of ¥1.2 trillion per month.

In 2009 the BoJ made plans to purchase ¥115 trillion in assets, on top of their already planned purchases of ¥1.2 trillion per month. In 2010 an asset purchase programme was announced. Subsequently, it was expanded on nine occasions and the composition of assets purchased varied. In total, the BoJ bought around ¥76 trillion in assets, of which ¥44 trillion were government bonds, ¥24.5 trillion were Treasury discount bills, ¥3.2 trillion were corporate bonds, ¥2.2 trillion were commercial paper, ¥2.1 trillion were exchange traded funds, and ¥0.13 trillion were real estate investment trusts.

As the result, the size of asset holdings by the BoE has increased fivefold, the Fed fourfold, and the ECB and BoJ double (Figure.2.2).

Table 2.4. Bank of Japan policy announcements concerning unconventional monetary policy measures

Date	Brief description
28 Nov 2008	QE1: Fed will purchase $100 billion in GSE debt and $500 billion in mortgage backed securities.
18 Mar 2009	QE1 expanded: Fed will purchase $300 billion in long term Treasuries and $750 billion in MBS, and $100 billion in MBS.
11 Mar 2010	QE2: Fed will purchase $600 billion in Treasuries.
21 Sep 2011	Operation TWIST, Fed will purchase $400 billion in Treasuries (with remaining maturities of 6 to 30 years and sell an equal amount with remaining maturities of 3 years or less).
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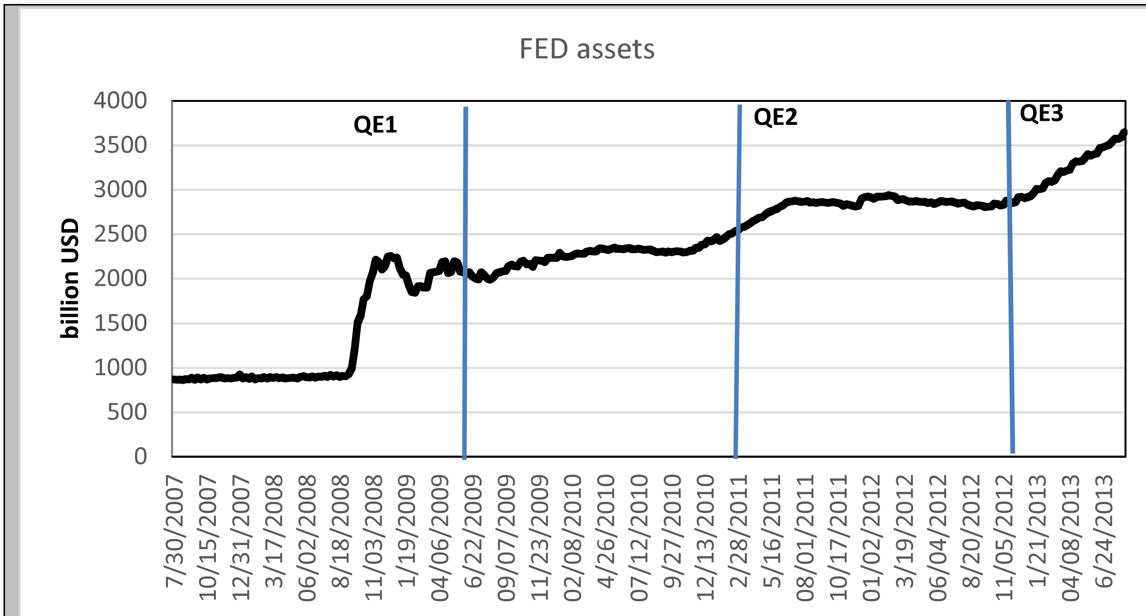
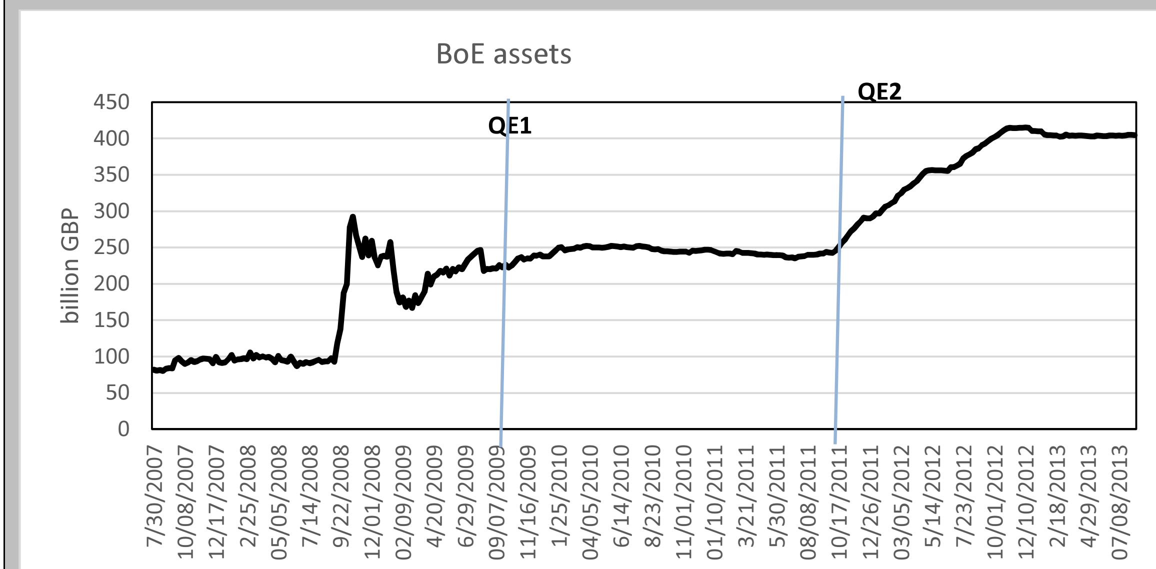
13 Sep 2012	QE3: Fed will purchase $40 billion of MBS per month.
12 Dec 2012	QE3 expanded: Fed will continue to purchase $45 billion of long term Treasuries per month without sterilisation.

Figure 2.2. The size of asset holdings in the balance sheets of Fed, ECB, BoE and BoJ.



FED assets
billion USD
QE1
QE2
QE3
4000
3500
3000
2500
2000
1500
1000
500
0
7/30/2007
10/15/2007
12/31/2007
3/17/2008
06/02/2008
8/18/2008
11/03/2008
1/19/2009
04/06/2009
6/22/2009
09/07/2009
11/23/2009
02/08/2010
4/26/2010
07/12/2010
9/27/2010
12/13/2010
2/28/2011
5/16/2011
08/01/2011
10/17/2011
01/02/2012
3/19/2012
06/04/2012
8/20/2012
11/05/2012
1/21/2013
04/08/2013
6/24/2013



BoE assets
billion GBP
QE1
QE2
450
400
350
300
250
200
150
100
50
0
7/30/2007
10/08/2007
12/17/2007
2/25/2008
05/05/2008
7/14/2008
9/22/2008
12/01/2008
02/09/2009
4/20/2009
6/29/2009
09/07/2009
11/16/2009
1/25/2010
04/05/2010
6/14/2010
8/23/2010
11/01/2010
01/10/2011
3/21/2011
5/30/2011
08/08/2011
10/17/2011
12/26/2011
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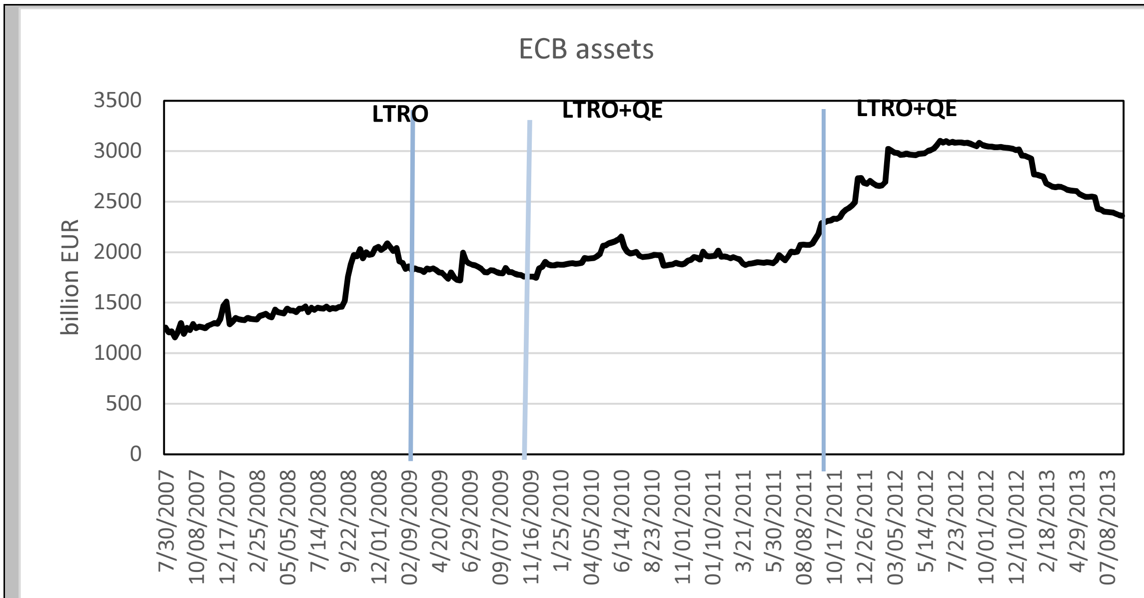
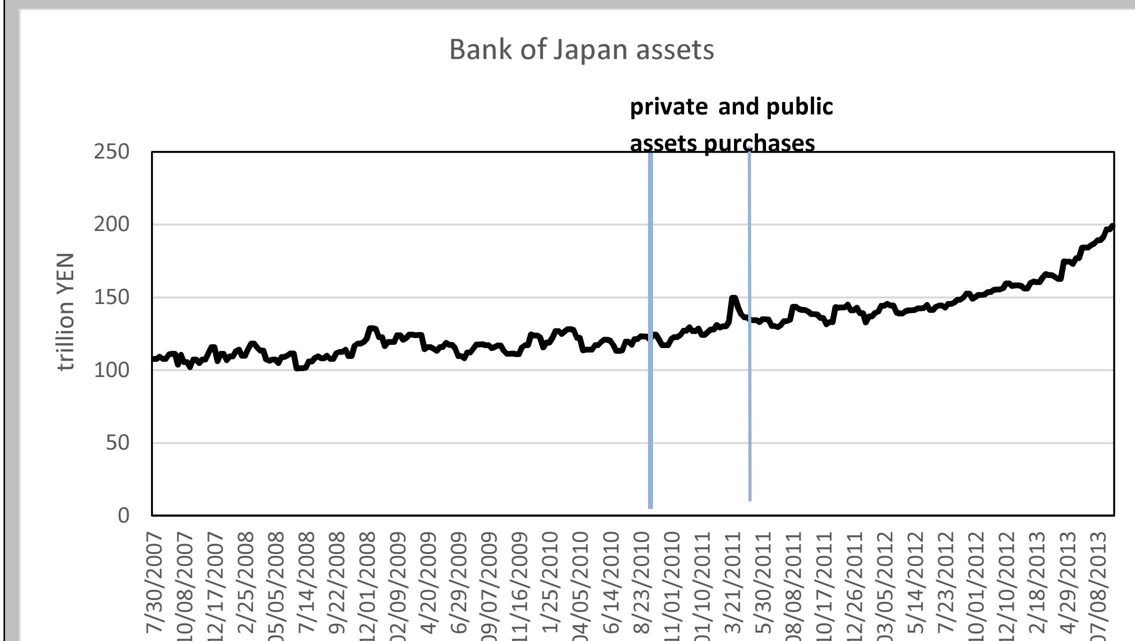
4/29/2013
07/08/2013





Certain side effects generated by QE have already manifested themselves in the past few years. For example, developing countries have repeatedly complained about the spillover effects of QE on their macroeconomic stability as QE led to increase in volatility in capital inflows, prices of primary commodities and the exchange rates of many developing countries. The extra liquidity injected through QE turned out to be beyond the control of the central banks that issued it. The first round of QE occurred in late 2008, immediately after the eruption of the global financial crisis drove global liquidity, in the form of capital flows, away from emerging markets and primary commodities and towards developed markets. QE2 in 2010 resulted in capital flowing in the opposite direction, and QE3 launched in late 2012 has not ushered in capital flows into emerging economies to the degree originally anticipated.

More recently, during the summer of 2013, when the United States Fed signaled the possibility of tapering the size of its monthly purchases of long-term assets, it triggered global financial turmoil. Both equity and bond markets worldwide experienced a sharp sell-off. While equity prices in developed countries recuperated, bond yields remain elevated relative to the level before May 2013. For instance, the yield on the 10-year United States Treasury bond soared by about 100 basis points, reaching the highest level since late 2011. By this measure, all the efforts by the Fed to lower long-term interest rates through QE3 have been undone completely in just two months. The losses in emerging markets have been more pronounced, as emerging economies encountered substantial reversals of capital inflows for the first time since the eruption of the global financial crisis in 2008. Equity prices in emerging markets plummeted by about 20.0 per cent in two months and in the same period, the risk premiums, as measured by the spreads of the bond yields, increased by 30.0 per cent on average. Some African countries have seen their premiums surge by 60.0 per cent, markedly hampering the ability of these countries to borrow affordably. Reversals of capital inflows were found to be more acute in such countries as Brazil and India because of the relatively high degree of liquidity in these markets, accompanied by sharp depreciations of the local currencies. Even in China, a seize-up of inter-bank lending in late June, although rooted in the problems of its own banking system, was to some extent also related to the global financial turmoil.

Both policymakers and financial markets are aware that, in the future, when the central banks start to taper the pace of their asset purchases and eventually unwind the process by selling the assets back to markets, investors will inevitably have to re-price the assets and rebalance their portfolios. It is hoped that by then banks, investors and the economy at large will be in a more robust position to endure such adjustments and the central banks will be able to engineer a smooth exit.

However, the most recent market reaction, or over-reaction, to the possible tapering of the QE in the United States has dimmed this hope and provided a vivid and timely alert to the world of the risks for a bumpy, rather than a smooth exit.

An uneven exit from the QE programmes would lead to a surge in long-term interest rates, not only in developed economies but also in developing countries; a sell-off in global equity markets; a sharp reversal of capital inflows to emerging economies; and a spike in the risk premiums for external financing in emerging economies. Exactly because of the large scale of the assets the major central banks have accumulated in the past few years as a result of QE and the sizeable distortions the QE programmes have brought to financial markets, the magnitude of these shocks from the unwinding could be equally significant. For example, the QE programmes have led to a broad-based shift into fixed-income assets with longer durations. The increased duration has significantly increased the potential losses to the holders of those portfolios when interest rates rise. Moreover, as QE moved a large proportion of the long-term bonds out of the markets, it reduced market liquidity, which in turn could intensify the shocks and lead to an overshooting of long-term interest rates.

More importantly, those first-round shocks in international financial markets could transmit quickly to the domestic sectors of both developed and emerging economies, aggravating the existing weaknesses in the real economy and forming a vicious circle.

For example, in major developed countries, such as the United States, a marked increase in long-term interest rates would be detrimental to not only banks, in terms of funding challenges, but also households and businesses, in terms of higher financial costs. This could stifle the fledgling recovery in private consumption and business investment. In fact, the 100 basis point increase in benchmark long-term interest rates during the financial turmoil of May-June 2013 has already left a measurable imprint on the housing sector in the United States. Mortgage interest rates spiked, leading to a notable weakening in housing starts and permits, at least for a few months.

In emerging economies, higher benchmark interest rates, rising risk premiums on external financing, and the reversal in capital inflows would exacerbate the challenges they are already facing: a slowdown in GDP growth and a further narrowing of policy space, combined with some long-run structural issues, especially for those with twin deficits and elevated inflation (see more discussion below).

Vulnerability in emerging economies

Many large developing countries, including Brazil, China, India and the Russian Federation, saw a significant deceleration in GDP growth in the past two years, owing to a combination of weak external conditions and domestic impediments. In the baseline outlook for 2013-2014, growth in these economies is expected to strengthen in some cases, such as Brazil and India, and to stabilize in others, such as China. For some economies, however, the risk remains for a further considerable slowdown in growth.

The financial turbulence encountered by many emerging economies during 2013 has reminded the world of the Asian financial crisis of 1997-1998. A comparison can be made between the vulnerability facing emerging economies today and the situation in the run-up to the Asian financial crisis in a number of aspects. Specific indicators from three Asian economies involved in the Asian financial crisis - Indonesia, Republic of Korea, and Thailand - were compared to indicators from five economies most affected by the current episode: Brazil, India, Indonesia, South Africa and Turkey. These five economies were selected as they have so far suffered the most from the latest financial turbulence, in terms of currency depreciation.

Volatility of capital inflows

As in the Asian financial crisis, the latest financial turmoil emerging economies have experienced has also been driven by pro-cyclical movements in fickle international capital flows.

In the run-up to the Asian financial crisis, private capital inflows to emerging economies increased from about $180 billion in 1994 to a peak of $320 billion in 1996 (an increase by 90.0 per cent), followed by a sharp reversal to $150 billion in 1998 (a drop by more than 50.0 per cent).

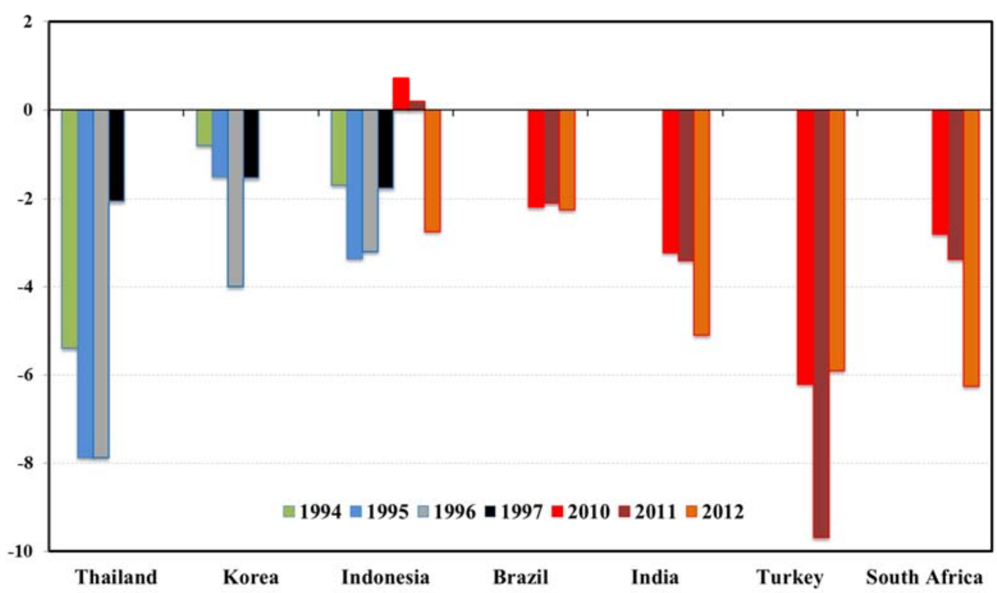
Currently, after plunging in 2008 to $658 billion from the peak of $1241 billion in 2007, net private capital inflows to emerging economies returned rapidly, reaching $1215 billion in 2012 (an increase of 85.0 per cent). This was followed by a reversal to an estimated level of $1,050 billion in 2013 (down by about 12.0 per cent). More importantly, portfolio equity inflows and non-bank credit inflows in 2012 surged to surpass the previous peak levels of 2007 by 50.0 per cent and 100.0 per cent respectively.

Current account balances

As shown in figure 10, in the three years before the Asian financial crisis, the three selected economies all experienced increases in their current account deficits, with Thailand registering the greatest increase, from 5.4 per cent of GDP in 1994 to 8.0 per cent in 1996.

In the current episode, all the five sampled economies have been running current account deficits in the past few years, with the largest deficit in Turkey, at 9.7 per cent of GDP in 2011. India's deficit was also sizeable - more than 5.0 per cent of GDP.

Figure 10. Current account imbalances for selected countries (Percentage of GDP).



Source: UN/DESA.

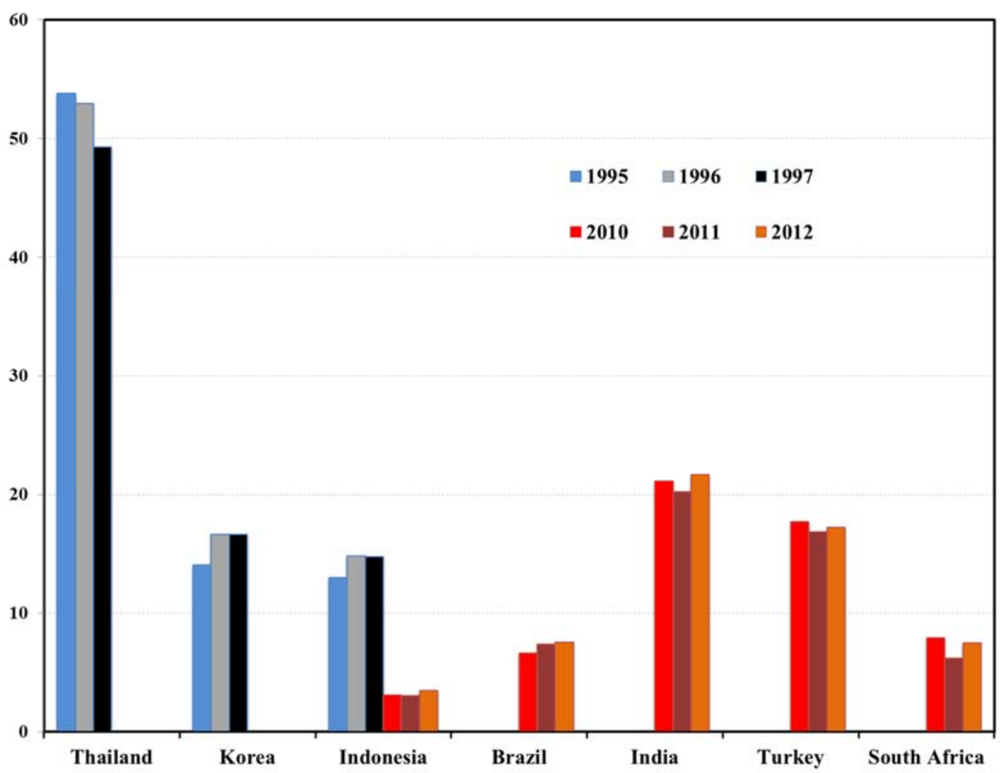
External debt

Measured by the ratio of foreign debt to GDP (figure 11), among the three selected economies for the Asian financial crisis, Thailand had the highest external debt ratio of 50.0 per cent in 1996.

In the current episode, India and Turkey have the highest external debt to GDP ratio of about 20.0 per cent.

In addition, currency and maturity mismatches in emerging markets' balance sheets (particularly of the private sector) played a central role in the Asian financial crisis, but are less pronounced this time. In South Africa, for instance, approximately two thirds of the total external debt is in domestic currency and only about 10.0 per cent of total external debt is short-term debt denominated in foreign currency. Similarly, India's short-term external debt accounts for only about 5.0 per cent of GDP.

Figure 11. External debt for selected countries (Percentage of GDP).



Source: UN/DESA.

Exchange rate regime

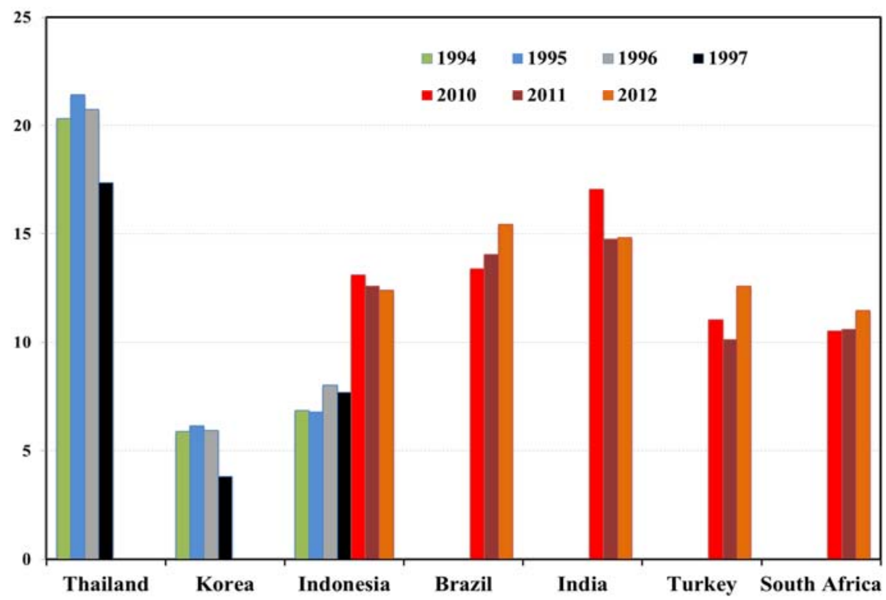
In the 1990s, most emerging economies adopted a fixed exchange rate regime, pegging their currencies to the United States dollar, or other major currencies. The fixed exchange rate regime caused at least two types of problems. First, in the run-up to the financial crisis, the fixed exchange rate regimes tended to lead to over-valuation of the local currencies, when the inflation rates in these countries were notably higher than that in the United States, and/or when they encountered adverse shocks to their exports. Second, when the crisis erupted, the fixed exchange rate regime also obligated these countries to defend their currencies by selling their foreign reserves, only to watch those hard-earned reserves quickly drain away.

In contrast, most emerging economies have recently adopted floating, or managed floating exchange rate regimes. A sharp devaluation of the local currency in a short period is still harmful for emerging economies, in terms of the adverse effects on inflation and losses on the balance sheets of businesses, but a flexible exchange rate regime can to some extent act as a relief valve to offset part of the external demand shocks on the domestic economy, through adjustments to relative prices between the external sector and the domestic sector. Because of the flexible regime, the authorities do not have to vigorously defend their currencies at any pre-set level, avoiding rapid exhaustion of their foreign reserves.

Foreign reserves

Before the Asian financial crisis, foreign reserves in Republic of Korea were at about 5.0 per cent of GDP, in Indonesian about 8.0 per cent of GDP, and in Thailand about 20.0 per cent of GDP (figure 12). When they began defending their currencies from depreciation, foreign reserves were rapidly depleted, forcing these economies to seek aid from international financial institutions.

Figure 12. Foreign reserves for selected countries
(Percentage of GDP)



Source: UN/DESA.

Currently, foreign reserves in most emerging economies are substantially higher. For example, even in the five economies that are under financial pressures, each of them has accumulated foreign reserves above 10.0 per cent of GDP, not to mention a group of other emerging economies with much higher foreign reserves.

Other aspects

Since the Asian financial crisis of the 1990s, as well as a few financial crises in other emerging economies in the late 1990s and the early 2000s, improvements have been made in these economies in such areas as: more transparency in the disclosure of financial information, including data on foreign reserves and non-performing loans; strengthened banking supervision and regulation so as to reduce mismatches in currencies and terms; more flexible policy measures in managing capital inflows; and better macroeconomic positions, in terms of more prudent fiscal and monetary policies and lower government debt to GDP ratios.

In the outlook, as major central banks, particularly the United States Fed, are expected to taper and eventually unwind their quantitative easing programmes, emerging economies are bound to face more external shocks, especially marked reversals of capital inflows. Some of these economies, particularly those with large external imbalances, remain vulnerable. Nevertheless, as a group, economic fundamentals and the policy space in these economies are measurably better than when the Asian financial crisis erupted.

Remaining risks in the euro area

The crisis in the euro area has cooled significantly but remains a significant risk factor for the world economy. The European Central Bank's Outright Monetary Transactions (OMT) program and other policy initiatives since late 2012 have significantly reduced sovereign risks and the risk of a euro area break-up. The OMT, in particular, has acted as a circuit breaker between the eruption of country specific crises and sovereign bond markets. This explains why the political impasse in Italy and the Cypriot bank bail-out have caused only limited disturbances; bond yield differentials have remained contained throughout the year. Despite this progress, considerable banking and fiscal risks remain.

A large number of banks still have weak balance sheets, particularly in the southern region, and could face insolvency. The Cypriot bail-out, in March 2013, actually raised risks in the banking sector by bailing-in additional classes of creditors, thus increasing the possibility of bank runs in the future. This has heightened the urgency to create a region-wide banking union. European Union finance ministers have agreed on the first stage of a banking union, and the ECB will become the top bank supervisor in the euro area. But first the ECB will perform an asset quality review and stress tests on the region's banks later this year, which may lead to further pressure to recapitalize banks either internally, via domestic government assistance or via euro area mechanism.

However in the continuing discussion over the form of the future banking union, the issue of bank resolution is far from resolved, so that the problem of weak banks remains major concern. One side effect of the OMT policy has been that banks have added sovereign debt to their balance sheets and so have become more vulnerable to sovereign instability if it were to return. A major risk, is that no one knows what would happen if the OMT were to actually be deployed.

The dangerous feedback loop between fiscal consolidation and economic weakness remains a risk. The growth performance of the region is improving, but most of the crisis countries remain in recession. The pressure for austerity has been somewhat reduced. In June 2013, the ECOFIN Council granted some countries extensions on the deadlines for hitting their fiscal targets. But the targets remain challenging, and will continue to hinder recovery. There remains considerable risk that these targets will be missed, due to growth shortfalls and/or political difficulties in implementation. This could then lead to a return to crisis, and as was seen during the Cypriot episode, the support for assistance to countries in crisis has weakened.

Uncertainties and risks about the fiscal policy in the United States

Over the course of 2013, the United States has experienced a series of mini fiscal crises caused by political divides on budget issues in Congress. At the beginning of the year, a full-scaled fiscal cliff was averted when an agreement was reached to permanently maintain a large part of the temporary tax cuts after they were due to expire. But Congress failed to agree on a long-term deficit reduction plan, triggering automatic, across-the-board spending cuts (sequestration) worth $1.2 trillion over the next nine years, a cut of $85 billion for 2013. It is estimated that sequestration and the phase-out of the reduction in pay roll tax may have caused a loss of GDP for 2013 by about 1.5 percentage points.

In early October, a failure in Congress to agree on the 2014 budget and to raise the debt ceiling led to a partial shutdown of the federal government and heightened the risk of a default on the United States debt by 17 October. At the last minute, an agreement was reached to fund the government through January 15, 2014 and suspend the debt limit through February 7, 2014.

The latest agreement did not resolve the issues, but merely postponed any resolution, meaning the uncertainties and risks will remain in the outlook. There are two different types of economic costs associated with these uncertainties and risks.

First, the recurrent uncertainties about the government budget, even if no large scale crisis erupts, are detrimental to business investment and hiring, leading to lower growth and higher unemployment in the short run and damaging potential growth in the longer run.

Second, should a crisis occur, for example, if the debt ceiling were not raised, the consequences would be devastating not only for the United States, but also for the world economy. Given that the federal government budget deficit is at more than 4.0 per cent of

GDP, if no more net borrowing were allowed, the government would be forced to take actions which would entail a combination of defaulting on the debt and cutting expenditures. As the United States has never defaulted, and given the fact that the dollar is the major international reserve currency and half of the United States government debt is held by foreigners, including foreign central banks, it is difficult to make a plausible estimate for the costs should the United States default on its debt. On the other hand, the impact of a cut in government spending can be estimated through model simulation. The simulation of the fiscal cliff as reported at the last LINK meeting remains a valid illustration of the potential impact should efforts to raise the debt ceiling fail.

4. Policy challenges

Macroeconomic policy stances in the world economy have become more diverse across countries, and some critical transitions are expected in 2014-2015. While policies in most developed countries, except Japan, will continue to feature a combination of tightening fiscal policy and accommodative monetary policy, the degree of fiscal tightening will be less restrictive and the extent of monetary easing will become less lax. Managing a smooth tapering of the QE will be the key challenge for the monetary authorities in major developed countries, as the risks associated with this transition will pose a threat not only for developed economies, but also for the rest of the world. The central banks of major developed countries have the primary responsibility for providing adequate and stable global liquidity, as they are the issuers of the international reserve currencies. In developing countries and economies in transition, policymakers face a more challenging international economic environment and more demanding domestic economic situations, requiring tough trade-offs among a confluence of different policy needs. Moreover, some of the challenges facing developing countries and economies in transition may go beyond what standard macroeconomic policies can deal with, requiring institutional reforms (see Box 3).

Box 3: Averting a hard landing for the Chinese economy

A continued deceleration in China's GDP during the first half of 2013 has further aggravated global concerns about the risk of a hard landing for the world's second largest economy. While such concerns are not unfounded, China still has policy space to avert a crash.

The moderation of China's growth has been triggered by a confluence of factors.

Persistently sluggish import demand from major developed economies has lowered China's export growth rate to a relatively meager pace of about 6.0 per cent in the past two years, compared with average growth of above 20.0 per cent registered prior to the crisis. This factor alone is estimated to have trimmed China's GDP growth by about 2.0 to 3.0 percentage points from its pre-crisis trend. As manifested by the excess capacity in many industrial sectors, it is impossible for China to turn the capacity that was built for exports to the service of domestic consumption in the short run.

Under such an inauspicious international economic environment, not only China, but also a number of other emerging economies have seen their growth falter markedly. In some of these economies, for example Brazil and India, the slowdown has been more pronounced than in China.

A number of domestic factors are also at play in the case of China's slowdown.

After three decades of rapid growth, which catapulted China from a low-income country to an upper middle-income economy, China is facing a plethora of structural challenges, such as widened inequality, monopoly in certain sectors, environmental degradation, and a reversal of the demographic dividend, all impeding China's growth.

At the same time, financial risks in China have escalated, as characterized by the spawning of shadow-banking activities and the mushrooming of local government debts. These risks were exemplified most recently in June 2013 by the crunch in the inter-bank lending market. The financial risks are largely rooted in the financial system itself, which is overdue for a deep reform as it has significantly distorted the allocation of financial resources in the economy. However, financial risks are also both causes and results of the weakening economic growth, forming a vicious cycle.

The new Administration of China seems to understand well the complex underlying factors for the economic slowdown. Instead of adopting another large-scale package to stimulate aggregate demand as it did during 2008-2009, the government resolved to take a new approach: promoting growth through reforms and structural adjustment.

For instance, the government has undertaken a number of legislative amendments to cut red tape and reduce administrative intervention in business operations. The authorities have also taken one more step in mid-July towards the liberalization of interest rates by removing the lower-bound limit set by the central bank for the interest rates on bank loans.

Indeed, in order to avoid both a hard landing in the short run and overcome the so-called middle-income trap in the medium run, China needs to forge ahead on economic, social and institutional reforms.

Further economic reforms need to focus on improving the efficient allocation of resources, particularly capital, labour and environmental resources, by reducing monopolies in certain sectors, leveling the playing field for small- and medium-size enterprises, and internalizing the externalities associated with environmental degradation and resource depletion.

Reforms of the financial system seem to have come to the fore. In this regard, a successful liberalization of interest rates holds the key for paving the way to a reform of the exchange rate and other financial reforms. At the same time, if carefully executed, a liberalization of the interest rates on deposit could help support household income, although it may heighten the risks for the banks and the state owned enterprises.

Social reforms should be focused on improving equality of both opportunity and outcomes. The Government needs to dismantle barriers between different social groups, such as the *hukou* system that separates the people in the rural areas from the cities, and further increase public spending on education, healthcare and other social services. The basic safety net for the poor should be broadened in line with economic growth.

It also needs to further transform the way the government functions away from direct involvement in business operations towards macroeconomic management and provision of public goods and services.

However, these and other reforms may take time to implement and structural adjustment is a long-term process. These reforms may not generate any immediate effects that will promote GDP growth. On the contrary, they may even entail some adverse impact on growth in the short run.

Therefore, the authorities may have to strike a balance between the supply-side measures for structural adjustment and the demand-side policies for stabilizing growth.

If the cyclical downward pressures persist, such as those emanating from a continued weakening in major developed economies, the authorities may have to be flexible in adopting certain monetary and fiscal stimuli to avert a hard landing. The good news is that both on the monetary and on the fiscal side there is room for targeted stimulus.

Some analysts argue that a hard landing of China's economy can spur the authorities to take more urgent reform measures and expedite structural adjustment. This, however, can hardly be an optimal solution, as a hard landing would likely be extremely costly for the economy and detrimental to social stability, not to mention the potentially grave repercussions it could generate for the global economy. Reforms and structural adjustment are better carried out under stable economic conditions.

Parsing China's latest statistics, one may find a modest silver lining beneath the downward trend. For example, investment growth in the relatively poorer Western and Central Region provinces has been higher than in the advanced East; investment growth in the services sector has been faster than in manufacturing; and incomes of rural families have increased more than that of urban households. All this indicates some improvements in the structure of the economy towards more balanced growth.

If China continues to make progress in reforms, and they are combined with flexible macroeconomic policies, which balance the needs for both structural adjustment and stable growth, a soft landing can still be managed.

The multiple and complex challenges in the world economy call for strengthening of international policy coordination. While the primary focus of the globally concerted and coherent policy actions should continue to be on a stronger recovery, particularly the recovery of jobs, increasing attention should also be given to mitigating the spill-over effects emanating from the large-scaled unconventional monetary policies adopted by major developed countries on developing countries and economies in transition.

Fiscal policy

Most developed economies, with Japan as the exception, have continued fiscal tightening during 2013, by reducing government spending, raising taxes, and, in some case, liquidating public assets. The average budget deficit of developed countries is estimated to have been reduced by 1.4 percentage points of GDP, to 4.5 per cent of GDP by 2013, compared with the peak of 8.9 per cent in 2009 at the height of the financial crisis. The average debt stands at 108.5 per cent of GDP. In the outlook, fiscal tightening will likely continue in most of these economies, but with a notably less acute stance.

In the United States, fiscal policy has tightened markedly in 2013, through increases in taxes and automatic spending cuts (sequestration). As a result, government spending in real terms is estimated to have declined by about 5.0 per cent in 2013 from the previous year. The budget deficit has improved significantly by 2.5 percentage points of GDP, dropping from 8.3 of per cent of GDP in 2012 to 5.8 per cent in 2013, with 2.0 percentage points coming from increased revenue and 0.5 percentage points from cutting in spending. The outlook for fiscal policy in 2014-2015 is clouded by political wrangling, replete with a host of uncertainties. The baseline forecast assumed correctly that the debt ceiling would be raised and the partial government shutdown would be concluded in October 2013, but fiscal policy is still expected to remain restrictive, but less severe than in 2013. The sequestration will end, and emergency unemployment insurance benefits will be phased out gradually. Government spending in real terms is expected to be flat in 2014-2015.

In Western Europe, fiscal policy remains dominated by the need to reduce deficits under the euro zone rules and was reaffirmed by the ratification of the new fiscal compact this year. Progress has been made, with the euro area deficit to GDP ratio coming down from 4.2 per cent of GDP in 2011 to 3.7 per cent in 2012 to close to 3.0 per cent expected for 2013. But twelve out of seventeen euro area countries remain under the Excessive Deficit Procedure of the Stability and Growth Pact. This typically requires consolidation of at least 0.5 per cent per annum and a two year timetable for completion. The pressure remains for further austerity, but with some recognition of the need to ease the terms in the short run. In June 2013, the ECOFIN Council granted some countries extensions of deadlines. The fiscal compact of the euro area entered into force in 2013, adding additional fiscal targets: the structural deficit should now be less than 0.5 per cent of GDP and remedial action will now be required for countries with debt/GDP ratios above 60.0 per cent.

In sharp contrast to other developed economies, Japan, despite facing the largest debt to GDP ratio in the world, has adopted expansionary fiscal policy during 2013, through a supplemental budget to increase government spending by about 2.2 per cent of nominal GDP. On the revenue side, the current Government decided to implement plans to raise the consumption tax rate committed to by the previous Government, with an increase in the tax rate from the current level of 5.0 per cent to 8.0 per cent in April 2014 and further up to 10.0 per cent in October 2015. Subsequently a decision was made to introduce a new complementary package of about 5 trillion yen to compensate the negative impacts of the higher consumption tax. As a result, the overall fiscal policy stance will become neutral to somewhat tighter in 2014-2015.

Compared with developed economies, most developing countries and economies in transition have a better fiscal position, in terms of budget deficits and public debt; however, their fiscal position has deteriorated measurably in 2013, with a number of low income countries experiencing high budget deficits.

The fiscal deficit has deteriorated in much of Africa, as Governments across the continent are under continuous pressure to increase spending on public services, wages in the public sector and provision of subsidies on food and fuel. The deterioration is largely due to lagging revenues in oil-importing countries, while oil-exporting and mineral-rich countries have sizeable fiscal surpluses. In East Asia, fiscal policy has remained generally expansionary, as a number of countries adopted various stimulatory measures, including tax relief, expenditures in support of job creation and infrastructure projects, to counter the slowdown in domestic demand. As a result, fiscal positions have worsened slightly in 2013. A similar stance is expected for 2014. Public finances in South Asia are under pressure, with Governments increasing already large deficits and regularly missing deficit reduction targets by a wide margin. Given the weak growth momentum in the region and the difficulties in raising tax revenues and curbing expenditure growth, fiscal deficits will remain large in the near term. In Western Asia, active fiscal policy in the oil exporters will remain, in contrast to more pronounced fiscal constraints in the non-oil exporters. In Latin America and the Caribbean, the fiscal position has deteriorated slightly in the past two years, mainly due to higher public expenditures in South America, but public revenues are also vulnerable to a softening of the prices of the primary commodities the region exports.

In the CIS, the Russian Federation has maintained a prudent fiscal stance as budget revenue increased less than anticipated. While Ukraine is restrained by high fiscal deficit, a few oil and natural gas exporting countries, such as Azerbaijan, Kazakhstan and Turkmenistan, continued massive fiscal spending on public wages and public infrastructure.

Monetary policy

Major developed countries share a number of common features in their monetary policy. In addition to maintaining policy interest rates at zero or near zero and adopting large scale purchases of long-terms assets (see Box 2 in previous section), central banks in these countries have also increasingly turned to “forward guidance” as a policy tool, to provide additional stimulus through anchoring expectations that interest rates will remain low for an extended period.

The Fed was the first central bank to adopt forward policy guidance, by stating publically that it will keep the target range for the federal funds rate at exceptionally low levels as long as the unemployment rate remains above 6.5 per cent or inflation between one and two years ahead is projected to be no more than a half percentage point above the Committee's 2.0 per cent longer-run target.

The BoE has joined the Fed in framing its guidance as refraining from raising the Bank Rate from its 0.5 per cent level at least until the unemployment rate has fallen to a threshold of 7.0 per cent. The BoE also made it clear that the unemployment threshold is not expected to be breached until at least the second half of 2016. The BoJ has announced that it will continue the Quantitative and Qualitative Monetary Easing (QQME), until the CPI inflation rate reaches the target of 2.0 per cent. In comparison, the forward guidance recently instituted by the ECB is to confirm the nature of their current policy setting rules based on the level of resource utilization and inflation, not on the level of growth.

Enhanced guidance by the central banks is seen as necessary to increase policy transparency and reduce uncertainties, thereby limiting the risk of financial market volatility that diminishes policy effectiveness. In reality, however, confusion can still occur. For example, when the Fed announced in May 2013 the possibility for tapering the amount of its purchases of long-term assets by late 2013, financial markets reacted immediately by pushing up long-term interest rates significantly, and when the Fed did not reduce it purchases in September 2013, markets seemed to be confused again. Managing public expectations, if possible, remains a big challenge for policymakers.

As delineated in Box 1, central banks in major developed countries are expected to maintain the policy interest rates at their current low levels at least until mid-2015, to be followed by a gradual increase in the rates. The Fed is expected to taper QE in 2014.

There is no apparent common trend in monetary policy among central banks in developing countries and economies transition as some of them are tightening while others easing in nature (table 2). In the outlook, the monetary authorities in these countries are expected to adopt appropriate monetary policy stances in accordance with the challenges they are facing: including the responses to the spill-over effects from the changes in the QE of major developed countries, fluctuations in exchange rates, volatility in capital inflows, inflation, unemployment and growth moderation. More details about monetary policy in these countries can be found in the regional economic outlooks.

Policy challenges to manage the risks associated with the unwinding of the QE

The tapering and unwinding of the unconventional monetary policies in major developed economies in the next few years pose significant risks for global growth and the stability of the world economy. It is a challenge for policymakers in these countries to harness a smooth process for this transition. Central banks in these countries should develop a clear communication strategy to articulate the timing and the targets of the policy action, and avoid repeating the episodes, which occurred with the United States Fed in May-June and September of 2013. At the macroeconomic levels the timing and the pace of the unwinding should be decided by taking into account the risks of choking off the economic recovery, destabilizing financial markets and sowing the seeds for high inflation, with a special weight to the recovery. At the technical level, contingency plans are also needed to deal with the over-reaction of financial markets and prevent contagion. Efforts are also needed to enhance supervision, regulation and surveillance of financial markets, in order to be able to identify and mitigate risks and vulnerabilities associated with liquidity of some assets, structure and other problems in advance.

For developing countries and emerging economies, the challenge is to shield themselves from the spill-over effects of the QE unwinding in major developed countries transmitted through international finance and trade. As shown by the financial market turmoil in the summer of 2013, the spill-over shocks to these countries can be consequential and costly, particularly to those emerging economies highly exposed to international capital markets, with large external imbalances financed by short-term external capital flows. Before the next episode of shocks arrives, these economies should address external and internal imbalances and build policy space. Supervision and regulation should also be strengthened to prevent a further build-up of mismatches in foreign currency funding on bank balance sheets. Prudential oversight should be tightened, particularly for shadow banking activity.

Many emerging economies today have gained policy flexibility from adopting a more flexible exchange rate regime, compared with the Asian financial crisis of the 1990s. However, central banks in these economies may still have to defend their currencies from sharp depreciation in case of a significant reversal in capital inflows. How to do it effectively remains a challenge.

During the most recent financial turmoil of mid-2013, a few countries, such as Brazil, India and Indonesia, raised interest rates in an attempt to curb currency depreciation. This orthodox policy is based on two hypotheses: first, higher interest rates would raise the yield differential in favour of these countries, boosting foreign investors' confidence and attracting more capital inflows; and second, higher interest rates would raise the financial costs for those speculators who are borrowing the local currencies to sell short. The similar policy approach was also adopted by a number of Asian economies during the financial crisis of the 1990s. However, as criticized by some economists then, as well as now, this policy could lead to a vicious downward spiral for both the real economy and the currency. These actions might have exacerbated, rather alleviated the Asian financial crisis 15 year ago, and may result in the same outcomes under the current financial distress. In contrast, the central bank of Turkey has adopted an unorthodox policy scheme by creating an interest rate corridor between 6.75 per cent and 7.75 per cent without increasing the policy interest rate.

Table 2. Timeline of policy interest rate action for selected monetary authorities (as of 4 October 2013).

	Official interest rate	Last change		Current (%)	Change since (bp)	
		Date	Change		Trough[b]	Jul-11
Australia	Cash rate	6 August 2013	-25bp	2.50	0	-225
Brazil	SELIC Overnight rate	28 August 2013	+50bp	9.00	175	-350
Canada	Overnight funding rate	8 September 2010	+25bp	1.00	75	0
Chile	Discount rate	12 January 2012	-25bp	5.00	450	-25
China	1-yr working capital	7 July 2012	-31bp	6.00	69	-56
Colombia	Repo rate	22 March 2013	-50bp	3.25	25	-125
Czech Republic	2-week repo rate	1 November 2012	-20bp	0.05	0	-70
Euro area	Refi rate	2 May 2013	-25bp	0.50	0	-100
Hong Kong, SAR[a]	Discount window base	17 December 2008	-100bp	0.50	0	0
Hungary	2-week deposit rate	24 September 2013	-20bp	3.60	0	-240
India	Repo rate	20 September 2013	+25bp	7.50	275	-50
Indonesia	BI rate	12 September 2013	+25bp	7.25	150	50
Israel	Base rate	23 September 2013	-25bp	1.00	50	-225
Japan	Overnight call rate[d]	5 October 2010	-5bp	0.05	0	0
Korea	Base rate	9 May 2013	-25bp	2.50	50	-75
Malaysia	Overnight rate	5 May 2011	+25bp	3.00	100	0
Mexico	Repo rate	6 September 2013	-25bp	3.75	0	-75
New Zealand	Cash rate	10 March 2011	-50bp	2.50	0	0
Peru	Reference rate	12 May 2011	+25bp	4.25	300	0
Philippines	Reverse repo rate	25 October 2012	-25bp	3.50	0	-100
Poland	7-day intervention rate	3 July 2013	-25bp	2.50	0	-200
Romania	Base rate	30 September 2013	-25bp	4.25	0	-200
Russia	Repo rate	13 September 2012	+25bp	5.50	N/A	N/A
South Africa	Repo rate	19 July 2012	-50bp	5.00	0	-50
Taiwan, Province of China	Official discount rate	30 June 2011	+12.5bp	1.875	62.5	0
Thailand	1-day repo rate	29 May 2013	-25bp	2.50	125	-75
Turkey	Effective rate	N/A[c]	N/A[c]	6.22	147	-3
United Kingdom	Bank rate	5 March 2009	-50bp	0.50	0	0
United States	Federal funds rate	16 December 2008	-87.5bp	0.125	0	0

Source: UN/DESA based on data of JPMorgan.

a Special Administrative Region of China.
b Refers to trough end-quarter rate from 2009 to present.
c Effective rate adjusted on daily basis.
d BoJ targets ¥50-60 tn/year expansion in monetary base.

International policy coordination

In order to mitigate the risks and uncertainties for the world economy as discussed above, international policy coordination needs to be enhanced.

Maintaining an open multilateral dialogue about economic policy intentions of all countries, particularly the major economies, is a crucial element in international policy coordination to promote policy coherence and concerted action. Such an economic policy dialogue has so far been frequently held in the context of the Group of Twenty (G20), but it should also be promoted to more broadly representative international forum, such as the United Nations.

Most recently, the G20 at the Saint Petersburg Summit has reaffirmed its framework for strong, sustainable and balanced growth. The G20 members have committed to undertake further policy adjustments toward rebalancing global demand between surplus and deficit countries. The surplus countries will achieve stronger domestic demand while the deficit countries will increase savings, and countries are encouraged to make their exchange rates more flexible. The Summit also called for urgent need to increase the momentum of the global recovery, generate higher growth and better jobs.

International policy coordination is also needed to mitigate the risks associated with the international spill-over effects from the unwinding of the unconventional monetary policies in major developed countries. Excess volatility of both capital flows and international prices of primary commodities should be curbed, as it is particularly detrimental to developing countries because of their small market size and limited capacity to hedge.

International policy cooperation and coordination are needed to advance the reforms of the international financial system on several fronts. Progress in financial regulatory reform has been slow, encountering growing resistance from the financial industry. Some progress has been made in amending the global financial safety standards for the banking sector. A dozen countries have issued final regulations to implement Basel III and more countries have committed to do so during 2013. Progress has also been made in implementing over-the-counter (OTC) derivatives reforms. On the other hand, the question of ending “too big to fail” is still pending, and recommendations from the Financial Stability Board (FSB) for the oversight and regulation of the shadow banking sector have yet to be issued. More forceful efforts are needed to address the issues of international tax avoidance and evasion, particularly through tax havens.

The current phase of reforming both the International Monetary Fund (IMF) and the World Bank needs to be completed to make their governance structure more representative, responsive and accountable. While there has been progress in ratifying the 2010 IMF quota and governance reforms, the process has not been finalized. The new review of the IMF quota formula should be resolved quickly to enhance the voice and participation of developing economies.

International policy cooperation should ensure that sufficient resources are made available to developing countries-especially LDCs and countries that possess limited fiscal space and face large financing needs for sustainable development and poverty reduction. The decline in ODA flows over the past two years should be reversed. As the target date for the United Nations MDGs is approaching, international donors should redouble their efforts to deliver on existing commitments. These resources are badly needed for developing countries to accelerate progress towards the achievement of the MDGs by the end of 2015, and to build a solid foundation for long-run sustainable development beyond 2015.

Regional Prospects

Developed economies

United States

In 2013, the *economy of the United States* is expected to grow at a meagre pace of 1.5 per cent, significantly lower than last year's GDP growth of 2.8 per cent and worse than originally projected in the LINK forecast of October 2012. In 2013, fiscal tightening and a series of political gridlocks, particularly on government budget issues, have weighed on economic growth. As this report is being written, the shutdown of the federal government has recently ended, but uncertainties still loom over the debt ceiling, which was only raised for another four months. Both of these issues caused by the political impasse, remain imminent threats to the economic growth during the forecast period. Although the monetary policy has been extremely accommodative, long-term interest rates started to increase in the second half of 2013, as a consequence of the possible tapering of the quantitative easing programme, adding constraints on private consumption and investment. Given these headwinds, the moderate improvements in earlier 2013, in areas such as housing and employment, have lost momentum towards the year end. Looking ahead, GDP is expected to grow by 2.5 and 3.2 per cent, in 2014 and 2015 respectively, based on the assumption that the debt ceiling will be raised and the future unwinding of the monetary easing will be smooth. However, risks remain on the downside, particularly because the political wrangling over the budget issues may continue to linger in coming years as along as the public finance is not placed on a long-run sustainable path.

Private consumption in real terms is expected to expand by 1.9 per cent in 2013, slightly lower than the previous two years. Positive factors that have supported private consumption include wealth effects, from the recovering housing prices, and rising equity prices. In addition, the modest increase in disposable income generated by a continued, albeit slow, growth in employment has also contributed positively. Nevertheless, consumer confidence has frequently been disturbed this year by uncertainties associated with the political fights over fiscal issues. The fiscal tightening, including higher income taxes (for instance, with the expiration of the 2.0 per cent cut on payroll tax) and the sequestration on government spending, has produced adverse effects on consumer confidence and consumption spending. In addition, many households are still undertaking financial deleverage by reducing mortgage loans relative to income. During the forecast period, real consumer spending is expected to rise 2.5 and 2.7 per cent in 2014 and 2015 respectively.

Business investment has experienced a marked deceleration in 2013, growing only 2.4 per cent, less than half of the 7.3 per cent growth in 2012. Uncertainties associated with fiscal policy have delayed business decision on capital spending and projects planning, but the pace of fixed investment is expected to pick up slightly in 2014-2015.

The *housing sector* has been recovering in 2013, although the recovery pace has been hampered since mid-2013, as mortgage interest rates increased by about 100 basis points, triggered by the expectation of the forthcoming tapering of the monetary easing. In early 2013, the housing sector was growing at an annual pace of about 40.0 per cent, but it decelerated to a pace below 20.0 per cent after May. The number of permits for new construction also declined. The S & P/Case-Shiller National Home Price Index has recovered about 12.0 per cent since 2011, but it is still about 20.0 per cent below the pre-crisis peak registered in 2006. The outlook remains, however, fairly positive: the housing sector is expected to continue its recovery, supported by low inventories and easing lending standards for construction and land development loans.

The *labour market* in the United States is still on a slow recovery. The payroll employment has increased at an average monthly rate of 184 thousand jobs in the past year. The unemployment rate declined to 7.3 per cent in late 2013, from a peak of 10.0 per cent in 2010. Part of the decline is due to a continuous drop in the labour participation rate, which reached the lowest level since 1978. The drop in the participation ratio is the result of several factors, including an aging population, higher school enrolment, but more importantly, because many unemployed workers have also been discouraged and stopped searching for jobs. Going forward, the employment rate is projected to decline slowly, reaching the critical level of 6.5 per cent by mid-2015 (see discussion on monetary policy below).

Inflation has been benign, with the CPI increasing at an average of 1.5 per cent in 2013, and is expected to stay below 2.0 per cent in the period of 2014-2015.

Real exports of goods decelerated notably during 2013, growing merely at bout 2.0 per cent, down from 3.8 per cent of 2012, with exports of food and computer equipment declining, but exports of aircraft and consumer goods increasing solidly. Real imports of goods also moderated, from 2.2 per cent in 2012 to 1.7 per cent in 2013. *Imports* of petroleum products and computers declined, while consumer goods grew at reasonable pace. Looking ahead, real exports and imports are expected to grow at a similar pace, 5.0-6.0 per cent in 2014-2015.

The *trade deficit* is estimated to be about $420 billion in 2013, improving marginally, partly reflecting a decline in the bill for imports of oil, which is likely to continue on a steady downward trend in the next few years. The broad measure of the current account balance is estimated to be in deficit of $410 billion in 2013, or 2.4 per cent of GDP, an improvement from the peak of 6.0 per cent of GDP in 2006. Going forward, both the trade deficit and the current account deficit are expected to stay at their current ratios relative to GDP in 2014-2015.

The Federal Reserve (Fed) has maintained an extremely accommodative *monetary policy* stance in 2013 through two instruments: (1) keeping the federal funds interest rate at zero; and (2) increasing the purchases of long-term government bonds and mortgage-backed securities. The Fed will keep the target range for the federal funds rate at exceptionally low levels, as long as the unemployment rate remains above 6.5 per cent or inflation between one and two years ahead is projected to be no more than a half percentage point above the Committee's 2.0 per cent longer-run goal. Therefore, it is likely that the federal fund interest rate will remain within the range of 0.0 per cent to 0.25 per cent until mid-2015. The Fed will start to raise the interest rates gradually in the third quarter of 2015. The Fed is expected to reduce the amount of its purchases in December of 2013, from the current level of $85 billion per month to zero gradually during 2014, and start to unload them gradually in the third quarter of 2015.

Fiscal policy in the United States has been tightened, during 2013, through two channels: (1) the expiration of the two percentage point reduction in payroll taxes and an increase in the income tax for the top one per cent of high-income households; and (2) the activation of the across-the-board automatic spending cuts (sequestration), worth $85 billion in 2013. As a result, government spending in real term is estimated to decline by about 5 per cent in 2013. During the forecast period 2014-2015, fiscal policy is expected to remain restrictive, but less severe than 2013. The sequestration is assumed to be replaced by an agreement on spending cuts that fall on Medicare, Medicaid and Social Security. Emergency unemployment insurance benefits will be phased out gradually. Government spending in real terms will be flat in 2014-2015.

Major *risks* for the economy of the United States are associated with both monetary policy and fiscal policy. The Fed is facing a dilemma: to keep purchasing long-term assets for too long will risk distorting asset prices, increasing moral hazard for banks and raising future inflation expectation; but to taper the purchases too soon will risk pushing up long-term interest rates too fast, choking the economic recovery and destabilizing financial markets. These risks have already been, to some extent, experienced in the two recent episodes in 2013: when the Fed announced the possibility to taper the purchases in May and when the Fed did not taper in September as markets anticipated. The same incidence of larger scales may recur in the next few years. The risks related to fiscal policy may even be more acute. The baseline outlook as discussed above assumed that the shutdown of the federal government would last only for a few weeks and the debt ceiling would be raised to avert a government default, so that the impact on economic growth will be limited. However, risks remain for a much worse scenario, if the political divide leads to a renewed prolonged government shutdown and a default on the United States government debt during the new budget negotiations in the early part of 2014.

Canada

The *Canadian economy* is estimated to grow at 1.6 per cent during 2013, slightly lower than in 2012. In 2014 and 2015, GDP is expected to grow by 2.6 per cent and 2.8 per cent respectively. The recovery of the Canadian economy from the recession of 2008-2009 is being temporarily held back by a series of factors, both external and domestic.

Residential construction was a positive contributor to GDP growth in early 2003, but the pace of construction is near a maximum. A stalled growth in housing seems inevitable, before a modest pickup forecasted for the second half of 2014. Excess inventory accumulations have apparently worked off, but the contributions of inventory growth to GDP are not expected until the second half of 2014. Meanwhile, recent increases in the personal saving rate, although related to the revisions to the National Accounts, may indicate that households are becoming more anxious about their debt levels and are increasing their savings in response. As a result, the saving rate could rise still further, curbing consumption in the near term.

The *unemployment* rate has improved marginally, dropping to an average of 7.1 per cent in 2013, from 7.3 per cent in 2012, and is expected to improve further to 7.0 and 6.8 in the next two years. Inflation has been running at about 1.1 per cent during 2013 and is expected to remain well below 2.0 per cent in 2014-2015.

Net exports were a negative for growth in early 2013 and are not projected to add significantly to GDP growth for a number of quarters to come. Real exports are estimated to grow by 1.0 per cent in 2013, before increasing gradually by 2.5 per cent to 3.0 per cent in 2014-2015. Real imports are expected to follow a similar pattern.

Government real spending has been growing been less rapidly than real GDP growth, for the past three years. The different levels of government are trying to cut deficits, inevitably affecting GDP growth. Expenditure restraint and low interest rates on government debt permit the federal budget deficit to decline and possibly to turn the fiscal balance to surplus by 2016.

Monetary policy in Canada is largely influenced by the United States monetary policy. Interest rates in Canada will rise with those of the United States, but not before, as Canadian interest rates are already higher by 100 basis points.

Japan

After a contraction of 0.6 per cent in 2011 caused by the earthquake and tsunami in March 2011, *Japanese economic output* managed to increase by 2.0 per cent in 2012. Since late 2012, a new Government has introduced a set of new policy packages to boost economic growth. The recent statistics reveals that the Japanese economy has resumed its expansion. Gross domestic product is projected to grow by 1.9 per cent in 2013 before growth slows down to 1.3 per cent in 2014.

The *new policy packages* announced in early 2013 included both fiscal stimulus and monetary easing. The Japanese Government is also expected to introduce another package targeting structural reform soon, which may have a positive effect on growth, especially in the medium-run. Those three packages form the three “arrows” of the so-called Abenomics.

The *fiscal element* of the stimulus packages is in the form of a supplemental budget for fiscal year 2012 which ended in March 2013. The supplemental budget increased the central government outlay by 10.3 trillion yen (about 2.2 per cent of nominal GDP for 2012), reversing the small-scale tightening introduced by the previous Government. The increased expenditures will be used to improve earthquake-resistance for infrastructure and buildings and to expand growth-inducing initiatives. As a result, real government consumption is projected to continue expanding over the outlook period, although the pace will slow down after 2014. On the revenue side, a law passed during the previous Government will increase the consumption tax rate from the current level of 5.0 per cent to 8.0 per cent in April 2014 and further up to 10.0 per cent in October 2015. In October 2013, the current Government decided to implement the hike as planned. It also decided to introduce a new complementary package of about 5 trillion yen to compensate the negative impacts of the higher consumption tax; the details of this package will only be revealed in December 2013. With this package, the net contribution of the higher consumption tax to the Government’s primary balance will be only around 0.2 per cent of GDP in the 2014. The deficit for 2014 will not change much from the level of 10.0 per cent of GDP for 2013. Even with the second hike in 2015, the deficit will still be about 8.0 per cent of GDP in 2015.

The *monetary element* of the stimulus package is the “Quantitative and Qualitative Monetary Easing” (QQME) announced by the Bank of Japan (BoJ) on 4 April 2013. The “quantitative” part refers to increasing the monetary base—the new operating target for monetary policy—at an annual pace of 60-70 trillion yen via the purchase of Japanese Government bonds (JGB) and other financial securities. The numerical target is to double the monetary base from the end-of-2012 level of 138 trillion yen (about 29.0 per cent of nominal GDP) by the end of 2014. To reach this target, the BOJ plans to increase its net holdings of JGB by 50 trillion yen per year. The “qualitative” part refers to the plan of expanding the target of bond purchases to longer maturity JGB, including 40-year bonds. The average maturity of JGB held by the BoJ will increase to 7 years from the initial level of less than three years. The BoJ also plans to include exchange-traded funds (ETF) and Japanese real-estate investment trusts (REIT) within the asset-purchase programme. Through these actions, the BoJ expects to bring down the yields for longer-term securities and to boost the inflation expectations of consumers, firms, and investors. The ultimate goal is to increase the annual CPI inflation rate to two per cent within two years.

The initial *impact of QQME* on JGB yields was very strong but it has partially faded since then. By the end of third quarter, the yields for 20- and 30-year JGB have declined by 20 and 27 basis points respectively from the end of 2012. This impact seems to be sustainable. The most significant impact of QQME is on the Japanese yen's exchange rate. Until the third quarter of 2012, the yen had appreciated vis-à-vis the United States dollar for many years. But during the fourth quarter of 2012, the perception of a possible extremely loose monetary policy stance was widely formed in the financial market and the yen started to depreciate. By the end of September 2013, the yen had depreciated by about 21.0 per cent vis-à-vis the United States dollar compared to September 2012.

Japan has experienced *deflation* for 15 consecutive years since 1998. Although the extent of the deflation has been declining over the recent years, the consumer price index was still on a downward track in early 2013. The introduction of QQME has changed the inflation expectations of economic agents, as revealed by the surveys conducted around mid-2013 and later. In addition, the sharp depreciation of the Japanese yen has inflated the prices of imported items included in the consumer price index and producer price index basket. The headline inflation rates for the first eight months support the projection that CPI will increase by 0.3 per cent for 2013 as a whole. In 2014, the inflation rate is forecast to increase further to 2.3 per cent, mainly as a consequence of the higher consumption tax rate. However, the core inflation rate may remain negative during 2013 due to the flat wage rate. Stagnant labour compensation was partially a result of increased hiring of part-time and short-term workers.

Since the Great Recession, the *export volume* of Japan has not yet resumed its pre-crisis level. In addition to weakened import demand from other developed countries and the damage to productive capacity caused by the natural disasters, the appreciation of the Japanese yen also hampered export growth. From mid-2007 to the third quarter of 2012, the yen's role as a safe-haven pushed up its value against the United States dollar by 56.0 per cent (52.0 per cent on a trade-weighted basis, according to the IMF). After the recent depreciation, the baseline assumption for the outlook is that the yen will remain close to or slightly above the current level (as of early October 2013) in the coming two years. On this basis, it is projected that real exports will expand by 2.2 and 3.6 per cent 2013 and 2014 respectively.

In both years, *import volume* will still grow but at a pace much lower than in 2012. The balance of trade in merchandise will remain in deficit over the outlook period, but will stop dragging down GDP growth in 2014. Still the investment income generated by Japan's huge holdings of external financial assets is expected to be enough to compensate for the deficit in the balance of trade in goods and services. The current account balance is projected to remain positive, although at a much lower level than prior to the crisis.

In 2013, *private consumption* is predicted to grow by 1.9 per cent. Despite the tepid growth in household incomes, expenditure on durable goods that has been brought forward to avoid the higher consumption tax will also contribute to solid growth. By the same token, private consumption growth will slow down to significantly less than one per cent in later years due to the planned tax hike. Fixed investment expanded by more than 4.0 per cent in 2012 due to reconstruction activity after the 2011 natural disasters. In 2013, fixed investment has continued to grow as public construction projects financed by the supplemental budget are being executed. It is predicted that investment will grow by 2.4 per cent and 2.3 per cent in 2013 and 2014 respectively.

Employment is expected to grow very slowly due to the projection for mild GDP growth. On the other hand, the labour force is expected to continue declining at a slow pace owing to the decline in the working-age population and the almost-flat labour force participation ratio. Assuming no major changes in the structure of the labour market, the average unemployment rate is predicted to decline from 4.4 per cent in 2012 to 3.8 per cent in 2014.

Australia and New Zealand

The *Australian economy* grew by 3.7 per cent in 2012, the best performance since 2007. The resumption of investment in the mining sector and the expansion of exports were the main reasons for this improvement. In the outlook, the pace of export growth is projected to remain solid, but investment in the mining sector is expected to peak in 2014 and then slow gradually, partially due to weakened international prices for Australia's major mining products. Meanwhile, growth in government consumption and public investment will also be lower, due to concerns about the fiscal balance. The GDP growth rate is expected to be 2.6 per cent in 2013 and 2.8 per cent in 2014.

CPI inflation has remained close to the lower bound of the Reserve Bank of Australia's (RBA, the central bank) target range of 2.0 to 3.0 per cent since 2012, and is expected to continue to do so during the outlook period. Against this backdrop, on 6 August 2013, the RBA decided to cut its policy rate further by 25 basis points to 2.5 per cent, the eighth cut since November 2011- a cumulative cut of 225 basis points in total. The statement from the RBA indicated that the expected slowdown of investment in the natural resources sector in the coming years warrants lower interest rates, as lower financing costs could help other sectors to regain their growth momentum.

Since the onset of the Great Recession, the *Australian dollar* has mostly maintained a strong value against the United States dollar until the second quarter of 2013. Capital inflows, mainly in the form of a carry trade, were one of the key reasons for this phenomenon. For the outlook, it is assumed that the Australian dollar will depreciate mildly vis-à-vis the United States dollar.

In *New Zealand*, GDP growth reached 3.2 per cent in 2012, also the best performance since 2007. The reconstruction for the Canterbury region after the earthquakes in 2010 and 2011 has sustained fixed investment at an elevated level which was the most important reason for this improvement. Fixed investment is expected to remain solid, albeit somewhat lower level for the outlook period. Export growth is predicted to remain strong given that half of New Zealand's exports are food products, which have been gaining popularity in the Asian market. Government consumption is expected to grow only mildly due to concerns over maintaining fiscal balance. The GDP growth rate is expected to be 2.6 per cent in 2013 and 3.0 per cent in 2014.

The *Reserve Bank of New Zealand* (RBNZ, the central bank) has kept its policy rate at a historically low level since March 2011. Meanwhile, the exchange rate for the New Zealand dollar has maintained its high level relative to the United States dollar. In addition, housing prices have kept on increasing and more people are taking out mortgages to finance real estate investment. The RBNZ considers the housing market as posing a risk to financial stability. Therefore, the RBNZ has decided to impose a restriction on the mortgage loan-to-value (LVR) ratio starting in October 2013. Under this policy, banks are required to limit the ratio of residential mortgages with LVR ratios higher than 80.0 per cent to less than one tenth of new mortgages in value terms.

Western Europe

Western Europe emerged from recession in the second quarter of 2013, after six consecutive quarters of declining GDP. *Growth* was led by net exports and, to a lesser extent, by private and public consumption, while investment made no contribution. Economic activity is expected to continue its momentum in the second half of the year, but annual growth rates will be affected by the very strong downturn at the end of 2012 and beginning of 2013. Thus, GDP is expected to decline for a second year at the aggregate level. In the EU-15, GDP is expected to decline by -0.1 per cent in 2013, before strengthening to 1.4 and 1.8 per cent in 2014 and 2015 respectively.

There are, however, considerable differences across countries. Among the large countries, the United Kingdom is expected to grow by 1.4 per cent in 2013, while Germany and France are expected to grow by 0.4 and 0.1 per cent respectively. The crisis countries are showing signs of turning the corner, but they remain in delicate positions. Italy is expected to contract by 1.9 per cent and Spain by 1.2 per cent in 2013, before both returning to positive growth in 2014. Among the smaller crisis countries, Cyprus and Greece are expected to continue to contract in 2014.

Growth in the region remains weak due to a number of factors: fiscal austerity programs remain in force, intra-regional demand is still exceptionally low, while extra-regional demand has slowed, and lending conditions are heterogeneous, with bank credit amply available in some countries while in others, conditions remain extremely tight. After weakening at the beginning of 2013, survey data have improved continuously since and are consistent with positive but subdued growth going forward. The European Commission’s Economic Sentiment Indicator (ESI) began increasing in May and is currently just below its long term average. The Markit Eurozone Composite Output Index has increased in every month since March and has been above 50, the point demarking expansion from contraction, throughout the 3rd quarter. Manufacturing has been leading the upturn, but the service sector has now also turned the corner. Industrial production and retail sales have been trending upward since the end of 2012, while construction started to uptrend in April.

Consumption expenditure remains weak and is expected to decline marginally in the euro area in 2013, before picking-up modestly in 2014 and 2015. But a number of countries, Austria, Germany, France, as well as the non-EMU countries are experiencing more robust consumption expenditure. Different degrees of austerity programs and the varying state of labour markets across the region explain these different patterns. The slight rise in inflation earlier in the year, which stemmed from energy price increases, also played a dampening role on consumption via real disposable income. Changes in consumer confidence have tended to follow the changes in uncertainty, stemming from the ebbs and flows of the euro area crisis. But since the easing of tensions in the region, confidence has climbed steadily and rests just below its long term average. Going forward consumption expenditure is expected to strengthen gradually as labour markets stabilize and confidence continues to improve, but will be held back by continuing austerity programs.

Investment expenditure remains a major weak spot, dropping sharply in most countries in 2013. Weak demand, continuing uncertainty, and funding difficulties in the crisis countries were key constraints. Going forward, investment is expected to increase in 2014 and 2015, as demand continues to pick up gradually and funding conditions begin to turn more favourable on aggregate. But the rebound will be weak. Capacity utilization has increased since the beginning of the year, but remains low by historical standards. Industrial confidence has also improved significantly, but it is only at its long term average. Funding conditions vary tremendously across the region; interest rates on loans, particularly to SME's, are much higher in the crisis countries, than elsewhere in the region. This situation will take a long time to normalize. Housing investment has started to turn around, but remains a drag to activity in some countries.

Exports volume growth remains exceedingly low. In the euro area, export volumes are expected to grow by only 1.2 per cent in 2013, as a consequence of extremely weak intra-regional demand, coupled with the slowing of extra-regional demand, particularly from East Asia. The appreciation of the euro in the early part of 2013 further dampened exports. As regional and global demand picks up, exports are expected to follow suit, supported by the assumed depreciation of the euro for the rest of the forecast period. Import volumes are even weaker, expected to decline, albeit marginally, for the second straight year. Some rebound is seen for 2014 and 2015, as regional growth picks up. Although the depreciation of the euro could play negatively on imports, the evolution of demand will be the dominant factor.

The relentless increase in *unemployment* seen across most countries in the region has ended. Since mid 2013 rates of unemployment have been stable or coming down slightly, albeit remaining at historically high levels in most cases. In the euro area, the unemployment rate has been close to 12.0 per cent since mid-year, but there is tremendous diversity in the region. In Spain unemployment was 26.2 per cent (August), in Greece 27.9 per cent (June), in Portugal 16.5 per cent and in Ireland 13.6 per cent. In Italy the unemployment rate is 12.2 per cent, in France 11.0 per cent, in the United Kingdom 7.7 per cent, while in Germany it was only 5.2 per cent. Going forward, the unemployment situation is expected to improve at a glacial pace, since the growth outlook is not strong enough to impart much dynamism to labour markets. Unemployment rates are expected to drift down only very gradually over the forecast period, with the crisis countries continuing to experience very high rates of unemployment at the end of the period. In addition, current rates understate the dimension of the problem, as discouraged workers have dropped out of the labour force and will be difficult to re-integrate.

Headline *inflation* is expected to decelerate from 2.5 per cent in 2012 to 1.8 per cent in 2013. This pattern is mostly due to changes of energy prices over the period. Core inflation (abstracting from energy, food, alcohol & tobacco) has run well below 2.0 per cent since the onset of the great recession and is currently close to 1.0 per cent. Inflation is expected to remain stable at 1.7 per cent in 2014 and to tick up slightly in 2015 to 1.9 per cent. With growth picking up only modestly, the output gap will remain large, while energy and food prices are assumed to remain contained.

Fiscal policy remains dominated by the need to reduce deficits, despite some progress made recently. The euro area deficit to GDP ratio came down from 4.2 per cent in 2011 to 3.7 per cent in 2012, and is expected to come close to 3.0 per cent in 2013. However, twelve out of seventeen euro area countries remain under the Excess Deficit Procedure of the Stability and Growth Pact. Under these circumstances, fiscal consolidations of at least 0.5 per cent per annum and a two-year timetable for completion will be required. Thus, the pressure remains for further austerity, although there is some recognition that its terms will need to ease in the short run. In June 2013, ECOFIN Council granted some countries extensions of deadlines (to 2014 for the Netherlands and Poland, 2015 for France, Portugal and Slovenia, and 2016 for Spain).
At a longer horizon, however, pressure for austerity will remain. The euro area's "fiscal compact" entered into force in 2013. This adds additional fiscal targets: the structural deficit should now be less than 0.5 per cent of GDP (with some caveats) and remedial action will now be required for countries with debt/GDP ratios above 60.0 per cent. In the forecast period it is assumed that fiscal policy continues to be focused on reducing fiscal imbalances and debt crisis countries will continue with their adjustment programs. The time-table for achieving targets will, however, be extended in some cases. In addition, it is assumed that no countries will ask for formal assistance, under the European Stability Mechanism (thus triggering the OMT).

Monetary policy has been dominated by various types of unconventional policies since the great recession. But in May 2013, the ECB returned to conventional measures when it cut both its Main Refinancing Rate and Marginal Lending Rate by 25 basis points, bringing them to 0.5 per cent and 1.0 per cent respectively. The Deposit Facility Rate was left at zero, avoiding the adoption of a negative interest rate and narrowing the corridor bounded by the Deposit and Marginal Lending Rates. Unconventional policies continue to be the key policies utilized to combat the sovereign debt crisis and the slow growth across the region. The ECB has pursued quantitative easing (QE) via a number of different LTRO. Thus, the ECB balance sheet expanded by more than 1 trillion euro to more than 3 trillion euro, particularly through the two 3-year refinancing operations in Dec 2011 and Feb 2012. However, in contrast to the QE programs of the US Fed, BOJ and BOE, the ECB's QE program is endogenous (passive rather than active), with liquidity being provided to banks on demand. Since January 2013, banks have been allowed to repay these loans and the ECB's balance sheet has shrunk to close to two trillion euro.

The other major unconventional policy, introduced in September 2012, was the "Outright Monetary Transactions" (OMT) facility. Under this policy, the ECB can potentially make unlimited purchases of selected country bonds to reduce their yields, but only if a country formally requests assistance and accepts conditionality. These purchases would not be QE, as they would be fully sterilized and have no impact on the ECB's balance sheet. So far the policy has not actually been deployed, but it has acted as a powerful circuit breaker, keeping bond yields contained after a number of crises at the beginning of 2013. In July 2013 a new policy was unveiled, "Forward Guidance", under which the ECB committed itself to maintain policy interest rates at a low level for an extended period of time, following a similar path as that of the United States Fed and the BOE. However, the ECB did not link this policy to the achievement of explicit targets, such as the US Fed did with their unemployment target. During the forecast period, it is assumed that the ECB will not cut its policy interest rates further. Given the outlook for low inflation and weak growth, it is assumed that interest rates will remain at current levels through the end-2015. In addition, it is assumed that the existence of the OMT will keep government bond yields within appropriate bounds. It is also expected that further LTRO's will be introduced to smooth the winding down of the existing three-year LTRO's. However, the ECB's balance sheet will gradually unwind as the banking sector's needs diminish.

Risks to the outlook are more evenly balanced than in the past few years, but remain slightly to the downside. There are ample possibilities for a flair-up of the sovereign debt crisis in the affected countries. This would depress consumer and business confidence across the region, or more seriously, could lead to renewed turmoil in the sovereign debt markets and test the ECB's OMT policy. Vulnerable banks could become insolvent, forcing more government bailouts. On the positive side, external demand may pick up with more vigour than anticipated, giving a boost to exports and investment. In addition, some of the structural policies may begin to bear fruit sooner than anticipated.

The New EU Member States

Many of the new European Union member States from Eastern Europe sustained negative *economic trends* in the first half of 2013. Their output shrank year on year, while consumer and business confidence remained depressed. These economies continued to feel the impact of the protracted weakness in the EU-15 trading partners and the on-going deleveraging by foreign banks present in the region (albeit at a more modest scale). On an annual basis, GDP contracted in the first two quarters in a number of countries, such as the Czech Republic, while the economy of Poland, the largest in the region, grew only marginally during the same period. Net exports provided the only positive contribution to growth in most of these countries in the first half of the year, with the exception of the Baltic States and Hungary. Domestic demand in the region remains suppressed by high unemployment and stagnant real wages, as well as by the on-going fiscal consolidation. Investment is held back by low FDI and stagnant construction sector. The export-oriented manufacturing sector, by contrast, was able to benefit from the slightly improved economic situation in the EU-15, and in case of the Czech Republic, Hungary, Poland and Romania, also the modest depreciation of the respective currencies versus the euro in early 2013.

Nevertheless, the *outlook* for the new European Union members has improved along with the return of the euro area economy to positive growth in the second quarter of 2013, as reflected by more optimistic forward-looking indicators during the summer months. Not only did business sentiment indicators improve, but also household economic confidence strengthened in the third quarter. The automotive industry, which is the backbone of manufacturing in Central Europe, shows signs of an upturn. Retail sales increased year on year in summer months in the Czech Republic and Poland, helped by the low-inflation environment. There is therefore potential for stronger economic performance in the second half of the year. However, while private consumption may pick up, investment is likely to remain subdued in the near-term. Most of those economies still operate below full capacity, which prevents businesses from undertaking risks and investing. In Hungary, nevertheless, public infrastructure projects, supported by European Union funding, helped to mitigate the decline in the investment rate, whose annual figure is expected to be negative. On an annual basis, several economies are expected to register a contraction in GDP in 2013, such as Croatia, which joined the European Union in July and where the economy remains in recession. The initial impact of Croatia's European Union membership is likely to be negative on GDP growth, as the country will face tougher fiscal spending requirements and exports will become subject to tariffs in some of the important trading partners, as the result of leaving the CEFTA[11].

Growth rates in the new European Union countries are expected to pick up only modestly in 2014. In 2013, the aggregate GDP growth for the region is expected to stay at 0.6 per cent, the same marginal level as in 2012. GDP growth is expected to strengthen in 2014 and 2015, in line with the improving external environment and a gradual recovery in domestic demand, by 2.1 per cent and 2.7 per cent respectively. At this pace, these economies will need several years before returning to the path of sustainable convergence with their EU-15 peers' income levels.

Inflationary pressures in the new European Union members continuously weakened in the course of 2013, held back by fragile domestic demand and lower prices for food and energy, as well as by administrative price reductions, such as utility price cuts in Hungary. Annual inflation reached record low levels in a number of countries. In the Czech Republic, for instance, inflation was as low as 1.3 per cent in August, decelerating further to 1.0 per cent in September, while core inflation was estimated to be virtually zero. In Hungary, annual inflation declined to 1.9 per cent by the end of summer. In 2014 and in 2015, a modest acceleration of inflation is possible, in line with the pick-up in economic activity, but it is expected to remain in low single digits in most of those countries.

For the new European Union member States, counter-cyclical fiscal policy actions remain limited, and in 2013 *monetary policy* was the main macroeconomic tool used to

[11] Central European Free Trade Agreement

bolster economic growth. Countries with flexible exchange rates have tried to use both conventional and unconventional monetary policy measures. Policy interest rates have been cut, within the course of the year, to record low levels in the Czech Republic, Hungary, Poland and Romania. In addition, the Hungarian National Bank announced the "Funding for Growth Scheme", offering funds at zero interest rate for commercial lenders, in order to help SME-s to convert their foreign currency loans into the domestic currency. The Czech National Bank announced its readiness to intervene directly into the currency market, in order to weaken the exchange rate and to support exports. The scope for further interest-rate cuts in those countries is now constrained, as portfolio investors became cautious about emerging markets, in anticipation of a tapering of the United States Federal Reserve's bond-buying programme. The large share of foreign currency loans in some of those countries is another hurdle on further monetary easing. In Hungary, in mid-2013, about 57.0 per cent of all retail loans (their total value exceeding $15 billion, and equivalent to 13.0 per cent of GDP) were denominated in foreign currency. Despite accommodative monetary policy, credit growth in the region remains either anaemic or negative. In the first quarter of 2013 credit to private sector contracted in some countries, in particular, in Hungary and in Slovenia. Cross-border deleveraging, by the parent EU-15 banks, continues (with the exception of Poland), but it is of a smaller magnitude than in the previous years. However, as banks increasingly rely on domestic deposit base, credit supply constraints are becoming less prevalent. Low demand for loans is a larger obstacle to recovery in private credit, as households and businesses still continue to rebuild their balance sheets. Credit standards remain tight, as the share of nonperforming loans remains still high. In 2014, a gradual tightening of monetary policy may be expected in the countries with flexible exchange rates (Estonia, Slovakia, and Slovenia are members of the euro area and therefore do not conduct independent monetary policy; Latvia will join the euro area in January 2014; and Bulgaria has a currency board regime, with the currency pegged to the euro).

On the *fiscal policy* side, most governments continued to reduce their budget deficits in 2013, in order to rebuild their public finances and, for a number of countries, to exit the excessive deficit procedure of the European Union. However, the governments are gradually moving away from the tight austerity path of the past few years. In Poland, the Government, facing a breach of the constitutional limit on the size of the public debt, decided to transfer government bonds worth an equivalent of 7.5 per cent of GDP from private pension funds to the state-run pension system. Consequently, the budget deficit in Poland in 2014 will be lower, due to lower interest payments for those bonds that will be cancelled. However, the deficit is still likely to exceed the 3.0 per cent of GDP benchmark. A similar action is possible also in the Czech Republic later in the year, depending on the outcome of the upcoming parliamentary elections. If the revenue intake improves along with economic strengthening, a slightly more expansionary fiscal policy may be expected in the region in 2014 and in 2015, especially in those countries, which reduce their deficits to a level below 3 per cent of GDP.

The region's *labour markets*, which deteriorated in late 2012, have improved somewhat since the second quarter of 2013. Public employment projects, while creating low-skill, low-paid employment, contributed to a reduction in the unemployment rate in

Hungary. In the Baltic States, where the post-crisis labour market improvement was the most noticeable, the reduction in the unemployment rate may be attributed not only to increased employment figures, but also to the shrinking labour force due to the large outward migration, in particular, in case of Lithuania. Although unemployment rates may slightly decline in 2014 and in 2015, a drastic improvement in unlikely, given the structural nature of the unemployment in the region and the continuing skill mismatch (in addition, some countries, such as Slovenia, still have to undertake cuts in public sector employment to meet their fiscal deficit targets).

The recovery is still subject to *risks* from a renewed slowdown in the EU-15, but to certain domestic risks in several countries. In particular, the Slovenian banking system remains a serious risk for macroeconomic stability. Although countercyclical measures are limited, countries should adopt pro-growth policies and, in particular, significantly improve absorption of the available EU finding, especially for public infrastructure.

Economies in transition

Commonwealth of Independent States (CIS) and Georgia

Economic growth in most economies of the CIS noticeably slowed in the first half of 2013. The difficult international environment, which constrained exports and the access to external finance, as well as a number of domestic factors, such as supply-side bottlenecks or weak consumer and business confidence, weighed on economic activity. In most of the CIS economies, annual GDP growth in 2013 is expected to be lower than in 2012, and the official growth targets will not be reached. The aggregate GDP of CIS and Georgia will grow by 2.4 per cent in 2013, a slowdown compared with 3.4 per cent growth accomplished in 2012. Economic activity is expected to strengthen modestly in 2014, with aggregate output of the area expanding by 2.5 per cent, and to recover more solidly in 2015 with a growth rate of 3.6 per cent

In the *Russian Federation,* where GDP growth already slowed to 3.4 per cent in 2012, the economy weakened further in the first half of 2013, growing by only 1.4 per cent year on year and is likely to expand by just 2.0 per cent for the year as a whole. Industrial output remained weak, investment became a drag on growth, and the economic slowdown has eventually affected the earlier resilient consumer confidence, and has led to weaker retail sales growth. The weakness in the Russian Federation, which has a strong influence on the CIS area, will have negative impact on its CIS neighbours through trade, investment and remittance channels. In the outlook, structural problems such as sluggish energy sector expansion, capacity constraints and weak investment will prevent an acceleration of growth to the pre-crisis levels. In 2014, freezing tariffs of the natural monopolies may lead to a squeeze in their investment plans. Growth in the Russian Federation is forecast to remain low in 2014, before it accelerates to around 3.0 per cent in 2015, provided that investment recovers.

In *Ukraine*, GDP contracted by 1.2 per cent year on year in the first half of 2013, despite strong real wage growth and buoyant private consumption, as industrial output and construction shrunk. Although strong agricultural output is expected to provide a boost to the economy in the third quarter, the country is likely to register near-zero GDP growth in 2013. Moreover, the country is facing a large external financing gap and may need to sign a loan agreement with the IMF in order to avert a possible balance-of-payments crisis. The Government, however, refuses to accept the IMF’s conditionality on domestic policies, including increasing tariffs on natural gas. Ukraine faces high cost of external borrowing and in September the country’s foreign exchange reserves dropped to a level covering just two and a half months of imports. The slowdown in the Russian Federation and China has led to weaker demand for steel, one of the main Ukrainian exports. Moreover, the possibility that the Russian Federation introduces barriers on imports of Ukrainian goods in response to the Ukraine signing a free trade agreement with the EU in November, further complicates the prospects for the economy, and low growth rates are expected for the forecast period. The economy of Belarus also performed poorly in the first half of 2013, with growth rates much below the official target.

In the *Caucasus*, growth picked-up in Azerbaijan in the half of 2013, and should accelerate further in 2014. The improved performance reflects success in diversifying the economy away from the energy sector. However, growth slowed year on year in Armenia and Georgia.

The economies of *Central Asia* continued their strong growth in 2013 and this trend should continue in 2014-2015. In Kyrgyzstan, where GDP fell by 0.9 per cent in 2012, growth turned positive, reaching 7.9 per cent in the first half of the year, thanks to a recovery in gold production, and a strong expansion in the other sectors of the economy. The economy of Kazakhstan slowed in the first two quarters of 2013. However, the imminent launch of the major Kashagan offshore oil field, following numerous delays, will push up oil exports for the rest of the year and in 2014.

Similar to 2012, *inflationary trends* in the CIS area diverged in the first half of 2013, with inflation rates close to double-digit figures recorded in Central Asia and a near-zero inflation registered in Georgia and Ukraine. Belarus is likely to register the highest annual inflation rate in the CIS in 2013, at over 20.0 per cent, after the Government increased public sector wages markedly and tried to stimulate private credit growth, and the domestic currency further depreciated. Inflation in Belarus is forecast to decelerate modestly in 2014. In the Russian Federation, inflation remained above the target range of the Central Bank, fuelled by higher food prices, strong nominal wage growth and robust consumer spending in early 2013. As the Government has decided to freeze public sector wages and state-regulated tariffs on transport and utilities in 2014, inflation should significantly weaken to about 4.0 per cent next year. In Ukraine, however, inflation may accelerate in 2014 amid devaluation fears. Higher prices for Russian natural gas have pushed up inflation in Armenia through higher electricity and transport costs, but inflation should slow in 2014. In the countries of Central Asia, rising incomes and strong public and consumer spending fuelled inflation in 2013. This trend is likely to continue in 2014, with annual inflation rates in Turkmenistan and Uzbekistan forecast to be in high single digits.

Although most of the CIS economies experienced a slowdown in 2013, the situation in the CIS *labour markets* did not deteriorate, with the exception of Ukraine. Moreover, some economies, such as Kazakhstan, continued to generate employment. In the Russian Federation, the unemployment rate remains at historically low levels of 5.0-6.0 per cent, despite some contraction of employment in the services sector. For many small economies of the CIS, labour migration, especially to the Russian Federation, remains an important factor alleviating pressure in the domestic labour market.

Fiscal policy in the Russian Federation remained conservative in 2013, as lower-than-projected growth led to a shortfall in budget revenues. Although the country has low public debt (at around 10.0 per cent of GDP), its high non-oil budget deficit (estimated at about 10.0 per cent of GDP in 2012) requires fiscal prudence, and the Government suggested to freeze public sector wages in 2014, and is planning to cut spending excluding pensions, welfare payments and debt servicing by 5.0 per cent in the near term. On the other hand, the Government also announced its plans to spend part of the National Wealth Fund on three major transport projects in a bid to provide a stimulus to the economy. In Ukraine, the fiscal deficit remained high, aggravated by the need of large financial transfers to the loss-making state-owned oil and gas company, as the Government refrained from raising the tariffs on natural gas, and the policy may be tightened over the forecast horizon. Fiscal spending remained modest in Armenia and Georgia, although planned increases in public wages in Armenia should favourably affect growth. By contrast, oil and natural gas exporting countries, such as Azerbaijan, Kazakhstan and Turkmenistan, continued massive fiscal spending on public wages and public infrastructure, and in 2014-2015 their fiscal policy will remain expansionary.

Monetary policy in the Russian Federation remains restrictive, although the stagnant state of the economy invoked calls from businesses to stimulate credit. However, the Central Bank decided to refrain from monetary easing, until inflation returns to its target range. As inflationary pressure eases, rate cuts are possible later in 2013 and in 2014. By contrast, in Ukraine, the Central Bank cut policy rates in order to boost the economy, but has to remain cautious about the possibility of a sudden and uncontrolled devaluation of the currency. More flexible exchange rates would allow more room for monetary easing; however, the large share of foreign currency denominated debt in the economy requires caution about the balance sheet effects. In Armenia, where inflation accelerated beyond the Central Bank’s target range, policy rate was increased to keep price rises in check.

The CIS region is facing a number of *risks*, emanating from the difficult international environment and slow progress in economic diversification in the energy exporting countries. Although the region’s major oil and gas exporters possess sufficient financial resources to shelter themselves from a short-term economic downturn, they still need significant supply-side reforms to increase competitiveness in the non-energy sector to withstand economic pressures in the long run. Among the energy importing countries, those with large external financing requirements, such as Belarus and Ukraine, may become especially vulnerable to a sudden deterioration in financing conditions. Many small CIS economies still rely heavily on remittances, and thus may be affected by an economic downturn or more restrictive conditions for migrant labour in the countries of destination, leading to a contraction in those flows.

South-Eastern Europe

Economic growth in South-Eastern Europe is expected to recover in 2013, after turning negative in 2012[12], as most of the region emerged from recession. However, in the near term, annual growth in those countries is expected to remain very weak, fluctuating between 1.0 and 2.0 per cent. This is clearly insufficient to address the region's long-standing needs of reindustrialization, increase the labour force participation ratio and tackle the excessively high unemployment rates. The aggregate GDP of South-Eastern Europe is expected to increase by 1.6 per cent in 2013, after contracting by 0.9 per cent in 2012. Although the outlook is subject to numerous risks, growth is projected to accelerate to 1.9 per cent in 2014, provided the tentative recovery in the EU strengthens, and 2.9 per cent in 2015, along with gradual recovery in FDI flows and in domestic demand. All economies in the region, with the possible exception of Bosnia and Herzegovina, should register positive GDP growth in 2013.

In Serbia, the economy grew at about 1.5 per cent in the first half of 2013, supported by export-led manufacturing and improved agricultural output. Domestic demand remained lacklustre, and the economy is likely to remain heavily dependent on exports in the near term. By contrast, in Albania the modest growth in the first two quarters was driven both by exports and by a solid recovery in construction output; and in the former Yugoslav Republic of Macedonia, activity was supported by large-scale public investment projects. In the outlook period, the external environment for those countries is expected to improve in 2014-2015, including the terms of access to external finance. As credit conditions ease, investment is set to recover gradually in 2014-2015, along with strengthening private consumption.

Inflationary trends in South-Eastern Europe diverged in 2013. While in most of the countries, annual inflation slowed by about 1 percentage point, it accelerated in Serbia from 7.3 per cent in 2012 to an estimated 9.0 per cent in 2013. This high inflation rate is largely explained by a base year effect (low inflation in early 2012) and a sharp food price rise in late 2012. Serbia's inflation rate, however, declined noticeably in the course of 2013 thanks to good agricultural output and falling food prices, combined with weak domestic demand and tight monetary policy. In the outlook period, average inflation for the region is expected to moderate in 2014 and 2015. This can be mostly attributed to lower inflation in Serbia, while in the rest of the region inflation should stay at about 2.0 per cent.

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[12] Since Croatia joined the European Union in July 2012, it is no more considered as part of this group of countries.

In most of South-Eastern Europe, *unemployment rates* remain precariously high, especially in Bosnia and Herzegovina, the former Yugoslav Republic of Macedonia and Serbia. In all of these countries, labour force surveys estimate unemployment at over 25.0 per cent. Most of the unemployment in the region is structural, caused by the destruction of capital stock during the earlier regional conflicts, and by insufficient investment in education and training and the consequent skill mismatch. However, the situation in the region's labour markets was further aggravated by the cyclical economic downturn. Nevertheless, some positive trends have emerged in the former Yugoslav Republic of Macedonia, where the registered unemployment rate dropped to 28.8 per cent in the second quarter of 2013, from 31.2 per cent a year earlier. The activity rate also increased, in part thanks to publicly financed large scale construction projects. In the outlook, the unemployment rates are expected to remain high, and serious efforts are needed to address them.

Fiscal policies in South-Eastern Europe remain tight, as the countries struggle to reduce their budget deficits or to comply with loan requirements by the IMF. In Serbia, the budget deficit is likely to approach 6.0 per cent of GDP in 2013. Since the Government aims to achieve a balanced budget by 2016, fiscal policy will remain tight in the medium-term. In the former Yugoslav Republic of Macedonia, however, fiscal policy will not be tightened significantly in the near-term, as large scale public investment projects need to be completed. Formal or informal currency pegs, in turn, constrain the conduct of monetary policy in the region. Among the countries with flexible currencies, the National Bank of Serbia repeatedly increased its key policy rate until April 2013 in response to accelerating inflation, before cutting it by a total of 75 basis points as inflationary pressures tapered. Facing increasing risk aversion among investors, the monetary authorities are likely to put further interest rate cuts on hold in the near-term. By contrast, the Central Bank of Albania repeatedly cut its policy rate, bringing it to a record low level in July 2013 amid rapidly falling inflation.

Some of the countries in the region run high *current accounts* deficits, which in 2013 is likely to reach 6.0 per cent of GDP in Serbia, 9.0 per cent of GDP in Albania, and 15 per cent of GDP in Montenegro. Given that those deficits are only partially covered by FDI inflows and that the economies in the region often rely on short-term capital flows, the large deficits may become a source of macroeconomic vulnerability in case of sudden capital outflows.

The major *risks* the region is facing are emanating from its strong trade and financial linkages with the euro area, as well as the region's strong dependence on remittances and on external finance. Therefore, a renewed slowdown in the European Union (especially in Greece and Italy), or a reversal in capital flows caused by stress on the parent EU banks or a quick unwinding of the monetary stimulus in developed economies, may have a profoundly detrimental impact on the South-Eastern European region.

Developing countries

Africa

Africa's *growth prospects* remain relatively robust with the average GDP growth rate projected to accelerate from 4.0 per cent in 2013 to 4.9 per cent in 2014, slightly lower than the developing countries' average of 5.1 per cent. Some of the pick-up in growth will come as a result of expected reversals of slowdowns due to country-specific circumstances, such as an end to protests in Libya that have seriously decreased oil output and exports. Medium-term growth prospects are expected to be supported by improvements in the global economic and regional business environment, relatively high commodity prices, easing infrastructural constraints, and increasing trade and investment ties with emerging economies. Other important factors for Africa's medium-term growth prospects include increasing domestic demand, especially a growing class of new consumers associated with urbanisation and rising incomes and improvements in economic governance and management. A moderate global growth recovery in 2014 underpinned by growth in emerging and developing countries, and projected improvements in the United States, European Union and Japan should also stimulate growth in Africa through increased trade, investment and capital flows.

Disruptions in oil production and political unrest in parts of North and West Africa (Central African Republic, Libya and Mali), slowed growth in Africa's oil-producing economies to 3.8 per cent in 2013. Growth is expected to rise to 5.2 per cent in 2014 as stability returns. Growth in mineral-rich economies is also expected to accelerate from 3.6 per cent in 2013 to 4.1 per cent in 2014, thanks mainly to increased investments and new mineral discoveries in countries such as Sierra Leone (in iron ore and diamond production), Zambia (in copper mining), Botswana (in copper, coal and diamonds), Namibia (in uranium and diamonds), Angola (in coal mining) and Ghana and Liberia (in gold mining). Growth in Africa's non-oil and non-mineral rich economies' is forecast to rise from 5.1 per cent in 2013 to 5.3 per cent in 2014, mostly driven by strong expansion in services and agriculture in countries such as Ethiopia.

At the *sub-regional* level, growth in West and East Africa is expected to increase from 6.6 per cent and 5.9 per cent in 2013 to 6.9 per cent and 6.4 per cent in 2014, respectively. Growth is also projected to increase in North Africa from 2.5 per cent in 2013 to 4.2 per cent in 2014 and in Southern Africa from 3.6 per cent to 4.1 per cent. Central Africa' growth is expected to recover moderately in 2014 to 4.7 per cent from a slight decrease to 4.2 per cent in 2013, which was mainly caused by political instability and violence in the Central African Republic, deceleration in oil production in Congo (Brazzaville) and Equatorial Guinea, and reduction in oil exports from Gabon.

West Africa will continue to attract investments in the oil and minerals sector, a key source of growth in the sub-region, especially in countries such as Burkina Faso, Ghana, Guinea, Liberia, Niger, Nigeria, and Sierra Leone. Real GDP growth in East Africa will benefit from several positive factors including for example increased consumer spending in Kenya, increased consumption and investment in the natural gas sector in Tanzania, increased activity in construction, transport, telecommunications, financial services, exploration and construction in the burgeoning oil industry in Uganda, and improved agricultural and service sector growth spearheaded by the wholesale and retail trade sector performance in Ethiopia. Growth in Kenya will also benefit from an expected rebound in 2014 after a cut in growth in 2013 due to after-effects of the Westgate Mall attacks on key sectors such as tourism.

Growth in the *Central Africa* sub-region is expected to remain reasonably solid despite decelerating as a result of political instability and violence and an expected fall in oil production in the absence of new discoveries in the Central African Republic (CAR), where growth is projected to decline to 1.2 per cent in 2014. Gabon's growth is also expected to decelerate from 5.5 per cent in 2013 to 5.4 per cent in 2014, as the country's oil fields are maturing, leading to a decline in output.

Political instability and disruptions in oil output continue to weaken growth prospects in *North Africa* especially in Egypt, Libya and Tunisia. Growth in the sub-region is expected to improve from 2.5 per cent in 2013 to 4.2 per cent in 2014 contingent on the assumption that some stability returns to the affected economies. Growth prospects in Southern Africa are improving largely due to projected increases in South Africa's growth rate from 2.7 per cent in 2013 to 3.3 per cent in 2014 with declining labour market unrest, increased investments and rising mineral output. The sub-region is likely to attract increased foreign investment due to huge coal deposits and offshore gas discoveries in Mozambique, increased oil output in Angola, and the increased investment in the copper sector in Zambia and uranium mining in Namibia.

Africa's recent relatively robust growth, heavily driven by commodity production and exports, remains far below the continent's potential and continues to fail to translate into meaningful *job creation* and broad-based economic and social development needed to reduce high poverty and rising inequality rates seen in many countries. It is therefore essential that African countries embark on strategies to transform their economies through increased value addition in the primary commodity sector and diversification into higher productivity sectors especially manufacturing and modern services.

Inflation across Africa is expected to decelerate slightly from an average of 7.0 per cent in 2013 to 6.8 per cent in 2014, owing to a variety of factors including subdued global demand and moderating international food and fuel prices and tighter monetary policy in most African countries coupled with increased investment in infrastructure. For example, in Central Africa, monetary policy in most of the countries is managed by the regional central bank, Banque des Etats de l'Afrique Centrale (BEAC), and will remain focused on controlling inflation and maintaining the CFA franc's peg to the euro. South Africa is expected to tighten its monetary policy in 2014 in order to control inflation and to ensure that real interest rates return to a positive territory. Exchange rate depreciation and falling foreign reserves will be major concerns for monetary policy in a number of countries such as Burundi, Egypt, Kenya, Malawi, Sudan, Tanzaniaand Uganda, although the gravity of the situation varies from country to country. In some of the countries in East and Southern Africa, loose monetary policy, high fiscal deficits, domestic currency depreciation and relatively high energy costs are among the factors that are expected to strengthen inflationary pressure in 2014. In North Africa, efforts to rein in rising costs for subsidies, particularly fuel subsidies, will put some pressure on inflation and is likely to increase social tensions.

Africa's average *fiscal deficit* deteriorated from 1.35 per cent in 2012 to 1.80 per cent of GDP in 2013 as a number of governments across the continent are under continuous pressure to increase spending on public services, including education, health, infrastructure besides increasing wages in the public sector and provision of subsidies on food and fuel. However, this deterioration was largely due to lagging revenues in oil-importing countries. Oil-exporting and mineral-rich countries recorded fiscal surpluses of 4.72 per cent and 4.97 per cent, respectively, in 2013. The fiscal outlook is brighter for the region's large economies of Equatorial Guinea, Ghana, Kenya, Libya, Morocco, Nigeria and South Africa as considerable improvements are expected in their respective fiscal balances in 2014. Among these countries Angola, Equatorial Guinea, Gabon and Libya continue experiencing relatively large fiscal surpluses, thanks to sustained increases in oil production and exports. Other countries such as Egypt and Morocco have taken steps this year to address significantly rising deficits, owing to the rising costs of subsidies.

Africa's overall *current account* deficit is expected to slightly decline from 1.8 per cent in 2013 down to 1.7 per cent of GDP in 2014. External balances will remain positive, albeit lower, in oil-exporting African countries. In oil-importing countries, mineral-rich countries, and non-mineral-non-oil rich countries external balances will continue to be negative, but are expected to improve over the forecast period.

Africa's total *exports* are expected to decline in 2014 to 29.6 per cent of GDP from 30.9 per cent in 2013, mainly due to the weakening global commodity markets, although oil and other commodity exports will continue to dominate. At a sub-regional level, exports are expected to decline in all the regions except in East Africa where exports will slightly increase from 15.5 per cent of GDP in 2013 to 15.7 per cent in 2014 due to increasing non-traditional exports such as floriculture and trade services. In Ethiopia, for example, exports are expected to grow rapidly as the country begins selling the electricity from its massive Grand Renaissance Dam to neighbouring countries. The country's trade deficit will remain negative though, with significant capital goods imports. Along with exports, total imports are expected to decline as a percentage of GDP across all sub-regions with the lowest decline in East Africa, from 33.0 per cent in 2013 to 32.5 per cent in 2014. Lower oil prices will keep growth in import bills lower, but necessary imports to fuel the nascent oil sectors in many East African countries will maintain pressure on trade deficits.

Foreign Direct Investment (FDI) flows to Africa are projected to increase in 2014 to 6.3 per cent of GDP, up from 6.1 per cent in 2013. Southern Africa will remain the highest recipient of FDI flows in 2014 (4.7 per cent of GDP), followed by Central Africa. In terms of economic groupings, the highest recipient of FDI flows in 2014 will be the non-mineral-non-oil rich countries, followed by the oil-importing countries. But mineral-rich African countries are expected to experience a slight decline in FDI flows from 4.11

per cent of GDP in 2013 to 4.05 per cent in 2014, mainly because of sluggish growth especially in the EU and some emerging economies as well as the declining commodity prices.

Despite the positive growth picture for many countries, the *employment* situation remains a major problem across the region, both in terms of the level of employment as well as the quality of jobs that are generated, especially in North Africa. High youth unemployment remains a concern for the region and continues to contribute to social pressures. Wide gender disparities in employment and earnings are also a significant issue. Women face unemployment rates at least double that of men in countries such as Algeria and Egypt. With the labour force growing at a rapid pace, the solid rates of GDP growth have proven far from sufficient to absorb all new labour market entrants, given the current pattern of production and employment generation. The lack of economic diversification away from the heavy dependence on resource extraction or agriculture is a key reason why labour demand is not more dynamic. Continued growth in other sectors such as telecommunications, financial services, transport and construction in countries such as Ghana, Kenya and Nigeria is helping to change this situation though.

Despite the expected robust medium-term growth prospects, some significant internal and external *downside risks* and uncertainties exist in the region. On the external front, a global economic slowdown encompassing the euro area, the US and the emerging economies would have a significant negative impact on Africa's performance through its impact on trade, FDI and ODA flows, tourism, and remittances to the region. Changes in global commodity prices and terms of trade are among the key risk factors Africa will face in the medium-term. The projected decline in global oil prices, will have a significant positive impact on current-account balances in oil-importing countries. In turn, it is expected to further reduce current account surpluses in oil-exporting countries, exerting pressure on their fiscal balances as their export revenues and government income decline. Political, civil and labour unrests still pose a significant threat to production in several African countries (such as Somalia, Congo DRC, South Africa, Central African Republic, Mali, Tunisia, Libya, Egypt, etc), especially through their negative effects on investment, trade and tourism. Developments in these countries continue to pose a significant downside risk to Africa's overall economic outlook. Furthermore, since most of the economies in the region are agriculture-based, weather-related shocks are the key downside risks for agricultural production and key upside risks for agricultural prices in Africa.

East Asia

After slowing considerably in 2011-12, *economic growth* in East Asia has stabilized at a moderate level in 2013. The region continues to be adversely affected by relatively weak external demand from developed economies and an adjustment to lower growth in China. Growth of GDP is projected to average 5.9 per cent in 2013, the same pace as in 2012. A mild pick-up in average regional growth to 6.2 per cent is forecast for 2014 and 2015, mainly driven by a gradual export recovery amid improving conditions in developed countries. In most East Asian economies, private consumption and investment will continue to expand at a solid pace, supported by stable labour market conditions, low inflation and fairly accommodative monetary policies. Fiscal policies will remain moderately expansionary and continue to provide support for growth.

China's economic growth decelerated further in the first half of 2013 as both domestic and external demand weakened. Recent data indicate that the economy has picked up mildly in the third quarter on the back of stronger industrial production and higher export growth. Full-year growth for 2013 is estimated at 7.6 per cent, down only slightly from 7.7 per cent in 2012. Looking ahead, a further gradual decline in growth to 7.5 per cent in 2014 and 7.3 per cent in 2015 is projected, in line with the Government's target to put the economy on a more sustainable path. The region's higher-income and strongly export-oriented economies have seen a moderate recovery in growth, which is expected to continue in 2014 and 2015. This follows a sharp slowdown in 2012 that was mainly caused by slowing external demand from China and weaker capital spending. The strength of the current recovery depends, however, heavily on the global economic environment as well as on specific domestic factors. Household debt, for example, has steadily increased since the global financial crisis and could weigh on growth if credit conditions are tightened. After a strong performance in 2012, the economies of Indonesia, Malaysia and Thailand are expected to see growth decelerate markedly in 2013, with a moderate pick-up projected for 2014 and 2015. In Indonesia, exports were negatively affected by lower commodity prices; while domestic consumption held up relatively well during the first half of 2013, the recent monetary tightening by the Bank Indonesia (BI) – introduced in response to rising inflation and large capital outflows - will lead to slower domestic demand. In Malaysia, exports have remained fairly weak in the first half of 2013 and fixed investment growth slowed considerably from a year ago. This was only partially offset by robust growth in government and household consumption. Thailand's economy slowed as consumption and investment demand weakened in connection with the phase out of stimulus programmes such as tax rebates and post-flood reconstruction activities. Bucking the trend of slowing regional growth was the Philippines whose economy is expected to expand by almost 7.0 per cent in 2013, supported by rapidly expanding consumption and a boom in construction.

In spite of the recent slowdown in economic growth, East Asia's *labour markets* have remained broadly stable. Unemployment rates are generally low, although considerable differences between countries and within countries exist. In the region's higher-income economies, the unemployment rate ranges from about 2.0 per cent in Singapore to 4.2 per cent in Taiwan Province of China. Unemployment is estimated to be below 3.0 per cent in Malaysia, Thailand and Viet Nam. In the Philippines, by contrast, the unemployment rate stood at 7.3 per cent in July 2013, up from 7.0 per cent a year ago. Despite growing strongly at about 7.0 per cent over the past year, the economy failed to create sufficient full-time jobs to keep pace with the rapidly growing labour force. The underemployment rate in the Philippines, however, declined during the same period from 22.8 per cent to 19.2 per cent. In Indonesia, the positive trend of the past few years has continued as strong domestic demand was associated with robust employment growth in the manufacturing sector, construction and services. The unemployment rate in Indonesia dropped to 5.9 per cent in the first quarter of 2013, down from 6.3 per cent a year ago and about half the level of 2005. In 2014 and 2015, unemployment rates across East Asia are expected to show little change given the expected moderate pace of economic growth in most countries. In most of the region's economies, a more pressing concern than unemployment is wide-spread informal employment, which in some cases in South-East Asia accounts for a significant part of total employment. Informal employment tends to suffer from low wages, weak productivity, and lack of benefits and job security.

Consumer and producer price *inflation* is generally mild across East Asia, not least owing to reduced pressure from international commodity prices and weakening demand pressures. Food prices remained fairly stable in 2013 on the back of favourable weather conditions and robust agricultural production. Average consumer price inflation in the region is projected at 2.5 per cent in 2013, slightly down from 2.8 per cent in 2012. In most countries, upward price pressures are likely to remain muted in the outlook period. In line with a gradual pick-up in economic growth, average inflation is forecast to accelerate only slightly to 2.7 per cent in 2014, ranging from 1.8 per cent in Taiwan Province of China to 6.7 per cent in Viet Nam. In China, consumer price inflation continues to be below 3.0 per cent despite relatively strong rises in food prices (particularly pork and vegetables); producer prices have remained in deflationary territory, weighed down by falling commodity prices, overcapacity, and weakening demand. Conversely, inflation accelerated sharply in Indonesia in the third quarter of 2013 after the Government hiked the administered price of gasoline by 44.0 per cent and of diesel by 22.0 per cent. The sharp depreciation of the rupee since June is likely to add to inflationary pressures. Average consumer price inflation is estimated to rise to 6.9 per cent in 2013, before easing slightly to 6.3 per cent in 2014.

Monetary policy remains generally supportive of economic growth across East Asia, in line with stable prices and weak external demand. Several Central Banks (Papua New Guinea, Republic of Korea, Thailand and Viet Nam) lowered their policy interest rates during the first half of 2013 in response to slowing domestic demand and reduced inflationary pressures. Further easing is, however, unlikely, and some central banks could tighten monetary conditions in 2014, provided that growth picks up and the Federal Reserve Bank tapers its large-scale asset purchase programs. The Bank of Indonesia already hiked interest rates three times by a total of 150 basis points from June to September 2013, while also strengthening macro-prudential measures. These policies were implemented to keep inflation under control, maintain stability in the financial system, halt the depreciation of the rupiah and reduce the current account deficit. Financial stability has also gained increased attention in other East Asian economies over the past few months. In June, China's interbank market experienced a temporary liquidity squeeze, which led to a spike in interbank rates. The People's Bank of China (PBOC) responded by providing additional liquidity to financial institutions that were facing funding shortages and were complying with macro-prudential requirements. Going forward, the PBOC will likely maintain its focus on adjusting liquidity in the banking system and ensuring steady credit growth. Continued financial reform, especially further liberalization of interest rates, and increased regulation of the shadow banking sector will have significant impacts on the liquidity conditions in the economy. In addition to national measures, East Asian countries are also increasingly looking to regional monetary and financial cooperation, such as the extension of bilateral swap arrangements, in response to financial market volatility.

Fiscal policy has also remained generally supportive of growth across East Asia as Governments are trying to counter the slowdown in domestic demand. Since late 2012, the Chinese government has announced a series of targeted measures including scrapping taxes for small firms and boosting investment in urban infrastructure and railways. The Republic of Korea passed a supplementary budget in May 2013, which includes spending on public sector jobs, business start-ups, mortgage subsidies and trade financing for small exporters. Malaysia, the Philippines and Thailand are pushing for large infrastructure projects, although delays in implementation have so far limited their impact. These expansionary fiscal policies, combined with costly subsidy schemes in some countries, are projected to lead to a slight deterioration in fiscal positions in 2013. In most economies–other than Malaysia and Viet Nam, budget deficits and government debt levels as a percentage of GDP remain still low. However, debt levels of local governments and state-owned enterprises, which are not recorded in the government's official balance sheet, have been rising rapidly in some cases, most notably in China. As a consequence, total debt might be greater than official government statistics indicate and vulnerability to international monetary conditions is likely to be somewhat higher. Given the expected slight pick-up in growth in 2014, fiscal balances are likely to improve slightly. In some countries, such as Indonesia and Malaysia, a gradual reduction of fuel subsidies will help narrow the budget shortfall. Several Governments are also looking into reforming the current tax system with a view to widening the tax base and diversifying revenue sources.

East Asia's *trade and current account* surpluses are much smaller than before the global financial crisis. In 2012, the combined current surplus of the region stood at 3.1 per cent of GDP, compared with a high of 8.3 per cent in 2007. This significant decline can be attributed to the protracted weakness of demand in developed economies and the robust growth in domestic demand (for both consumption and investment) across East Asia during the initial recovery from the crisis. In the first half of 2013, export growth in most East Asian economies remained fairly weak owing to on-going sluggish import demand in the key destination markets, notably Europe and the United States. Import growth, in turn, decelerated sharply during 2012 as activity across East Asia lost momentum, and has failed to recover in the first half of 2013. Looking ahead, both exports and imports are projected to pick up in 2014 and 2015 in line with a gradual improvement in the global economy, but growth rates will remain much lower than before the 2008-09 crisis. In some economies, such as Indonesia and Malaysia, exports may benefit from the recent depreciation of the national currency. Current account balances as a share of GDP are expected to remain relatively stable in most countries. China's current account surplus is forecast to further narrow gradually from about 2.0 per cent in 2013 to 1.6 per cent in 2014 and 1.2 per cent in 2015. This can be attributed to a steady decline in the trade surplus and a widening service balance deficit as the number of Chinese tourists travelling overseas rises.

While the baseline forecast projects a slight pick-up in East Asia's growth in 2014 in line with improved global conditions, there are still considerable *downside risks* for the region. The upcoming tapering of the Fed's massive asset purchase program could trigger sharp capital outflows from some East Asian economies. Monetary authorities may be pressured to raise interest rates to support their currencies, thereby dampening economic growth. Tighter liquidity conditions and higher global and regional interest rates could pose challenges for countries with high levels of household debt, such as the Republic of Korea, Malaysia and Thailand. At the regional level, a sharper-than-expected slowdown in China, for instance triggered by measures to address financial instability, could have a severe impact on East Asia's growth.

South Asia

South Asia's *growth* momentum remains lacklustre as a combination of internal and external factors hamper activity, particularly in the region's largest economies (India, the Islamic Republic of Iran and Pakistan). On average, gross domestic product is estimated to expand by 3.8 per cent in 2013, after growing by 3.6 per cent in 2012, the slowest pace in almost two decades. Going forward, growth is forecast to pick up moderately to 4.6 per cent in 2014 and 5.2 per cent in 2015, supported by a gradual recovery in domestic demand in India, an end to the recession in the Islamic Republic of Iran, and an upturn in external demand. However, in most economies, growth will likely remain well below the pre-2008 level. Private consumption and investment are held back by a wide range of factors, including energy and transport constraints, volatile security conditions, macroeconomic imbalances and lack of economic policy reforms. At the same time, the room for monetary and fiscal policies to stimulate domestic demand is limited by elevated inflation, large fiscal and current account deficits, and volatile global financial conditions.

India's economic woes continued in the first three quarters of 2013 and the short-term outlook remains subdued. Gross domestic product growth decelerated to 4.6 per cent in the first half of the year, the slowest pace of expansion since the 2008/09 crisis. Consumption growth fell to 2.7 per cent and gross fixed capital formation expanded by a meagre 1.2 per cent from the previous year, despite the fact that the Reserve Bank of India (RBI) had eased monetary policy significantly in 2012 and early 2013. Full-year growth in India is projected at 4.7 per cent in 2013, down from 5.1 per cent in 2012. India's economy also experienced massive capital outflows between June and August 2013, which led to a sharp depreciation of the rupee. These outflows had been triggered by expectations of an upcoming tapering of the Federal Reserve's bond-buying program, combined with concerns over India's large current account deficit. While India's slowdown may have bottomed out, the recovery is likely to be much slower than previously expected. Economic activity is forecast to expand by 5.2 per cent in 2013 and 5.7 per cent in 2014, on the back of a good monsoon, a new round of government reform measures, and stronger investment activity. In the Islamic Republic of Iran, economic activity is expected to further contract in 2013, although less severely than in 2012, before recovering slightly in 2014 and 2015. The prolonged recession reflects the impact of Western sanctions, which have caused a sharp drop in oil exports and serious supply shortages. The recent surge in inflation and the depreciation of the local currency hamper private consumption and investment. Nepal and Pakistan also continue to face significant macroeconomic challenges, with growth in both countries expected to remain fairly weak in 2013 and 2014. Pakistan recently entered into a loan agreement with the IMF that aims at stabilizing macroeconomic conditions and solving the balance of payments problems. The program comes with a number of strict conditions attached, particularly with regard to fiscal consolidation. In combination with some monetary tightening by the State Bank of Pakistan, this is likely to weigh on activity in the short run. A moderate recovery is forecast for 2015 as supply conditions improve and investment strengthens. The economic outlook is more favourable in Bangladesh, where growth is projected to remain fairly robust at about 6.0 per cent in 2013 and 2014, and especially in Sri Lanka, the region's fastest growing economy in recent years. Growth in Sri Lanka is expected to further strengthen to about 7.0 per cent in the outlook period, on the back of on-going reconstruction efforts and strong consumption growth, which is fuelled by rising incomes and remittance inflows.

Recent *employment* surveys in South Asian countries suggest that the economic slowdown has taken its toll on the region's labour markets. Available data provide, however, only an incomplete picture of the actual situation, as the majority of South Asian workers are employed in the informal sector. The latest figures for India, the Islamic Republic of Iran and Pakistan indicate that unemployment increased in the past year and the labour force participation declined slightly. According to India's Employment-Unemployment Survey, the average unemployment rate rose from 3.8 per cent in the fiscal year 2011-12 to 4.7 per cent in 2012/13, with large differences by region, gender and age group. Unemployment is estimated to be higher among women (7.2 per cent) than men (4.0 per cent), higher in urban areas (5.7 per cent) than rural areas (4.4 per cent) and much higher for the age group 15-29 years (13.3 per cent) than for those 30 years and above (1.0 per cent). Similar unemployment patterns prevail in other South Asian countries. In Pakistan, the structural weakness of the economy seems to have exacerbated the employment gaps. In the second quarter of 2013, an estimated 18.7 per cent of women living in urban areas were unemployed compared to only 6.3 per cent of men. Moreover, the female labour force participation rate in urban areas was only 7.3 per cent, down from 8.4 per cent two years earlier. In Bangladesh, a factory building collapse in April 2013 that killed more than 1,100 garment workers sparked a debate over employment conditions. This has led to an adoption of a new labour law in July that strengthens worker rights, including the formation of trade unions. Given that economic growth in South Asia is expected to remain below potential and the labour force will increase rapidly, the labour market pressures are likely to further intensify in the years ahead.

In most South Asian countries, consumer price *inflation* rates moderated slightly over the past year as aggregate demand pressures declined and international commodity prices eased. Inflation remains, however, significantly higher than in other world regions and, in most cases, well above the central bank's comfort zone. The continued strong upward pressures on prices can be attributed to several factors, including persistent supply bottlenecks, entrenched inflationary expectations, on-going weakness of local currencies (particularly in India, the Islamic Republic of Iran and Pakistan), and the attempts by several Governments (for example in India and Pakistan) to reduce their food and fuel subsidy bills. Because of a surge in inflation in the Islamic Republic of Iran, average annual consumer price inflation in South Asia is estimated to increase from 12.5 per cent in 2012 to 14.5 per cent in 2013, before slowing to 12.2 per cent in 2014. Severe supply shortages and a sharp devaluation of the rial pushed Iranian consumer prices sharply up in 2013, with year-on-year inflation reaching a high of 45.0 per cent in June. Since the sanctions are likely to remain in place in the outlook period, inflation is projected to ease only gradually, averaging about 30 per cent in 2014 and 20.0 per cent in 2015. In India, consumer price inflation has remained stubbornly high at close to 10.0 per cent even as domestic demand weakened further in 2013. By contrast, inflation decelerated moderately in Bangladesh, Nepal, Pakistan and Sri Lanka during 2013, ranging between 6.0 per cent and 8.0 per cent in the third quarter of the year. While the baseline scenario foresees a gradual decline in inflation across South Asia in 2014 and 2015, significant upside risks remain, including a significant reduction of subsidies (particularly in India, Pakistan, and Sri Lanka) and poor harvests.

Recent *monetary policy* actions in South Asia reflect the considerable differences in macroeconomic conditions between countries. On the one hand, the monetary authorities in India and Pakistan have recently hiked their benchmark interest rates. By doing so, they have shifted the policy focus towards bringing down inflation and easing external pressures amid volatile global financial conditions, rather than trying to support economic growth. The Reserve Bank of India (RBI) raised the repo rate by 25 basis points in September, which marks a turnaround from the first half of the year, when policy rates were cut three times. The RBI also recently rolled back the exceptional liquidity tightening measures that were introduced in July and August when India experienced massive capital outflows and a sharp drop in the value of the rupee amid expectations of an imminent tapering of the Fed’s large asset-purchase program. While the RBI is expected to maintain its focus on inflation, it is unlikely to raise policy rates considerably given the on-going weakness in investment and growth. Should inflationary pressures ease in the course of 2014 and the external financial environment stabilizes, the RBI will likely loosen monetary conditions. In Pakistan, the Central Bank also raised its benchmark interest rates in September 2013, the first hike in almost three years. This move is in line with recommendations from the IMF to tighten monetary policy and comes shortly after the IMF approved a 6.6 billion dollar loan for Pakistan. The path of Pakistan’s monetary policy in the quarters ahead will be mainly determined by the trend in inflation; a further gradual decline in inflation could give the State Bank of Pakistan room to resume monetary easing. The Central Banks in Bangladesh and Sri Lanka, by contrast, have maintained their accommodative monetary policy stances as consumer price inflation moderated and exchange rates were fairly stable. In both countries, monetary conditions are expected to remain unchanged over the next few quarters, with the possibility of some tightening later in the forecast period.

The current economic slowdown in South Asia has put further pressure on *government finances*, which were already strained by very low tax bases and rising expenditure. Over the past few years, the Governments have regularly missed their deficit reduction targets by a wide margin. Growth projections proved too optimistic and expenditures on food, fuel and fertilizer subsidies were significantly higher than anticipated. For the past fiscal year (2012 or 2012-13), the budget deficit is estimated at nearly 5.0 per cent of GDP in Bangladesh, India and the Islamic Republic of Iran, at 6.7 per cent in Sri Lanka and at 8.0 per cent in Pakistan. Given the weak growth momentum in the region and the difficulties in raising tax revenues and curbing expenditure growth, fiscal deficits will remain large in the near term. In India, the Government is unlikely to meet its target of reducing the deficit to 4.8 per cent of GDP in the current fiscal year 2013-14 since GDP growth is well below the projected rate of 6.5 per cent and the sharp depreciation of the rupee pushes up the subsidy bill. During the first five months of 2013-14, the budget deficit reached 75.0 per cent of the full-year target. In Pakistan, which faces the most severe fiscal challenges in the region, the recently approved $6.6 billion IMF loan comes with strict conditions to consolidate the public finances. The program envisages a gradual decline in the deficit from about 8.0 per cent of GDP in 2012-13 to 5.8 per cent in 2013-2014 and 3.5 per cent in 2015-2016. While these targets will be difficult to achieve, the deficit is expected to narrow gradually.

South Asia's *merchandise exports* continue to be weighed down by relatively weak demand in key destination markets, including the European Union and the United States. However, some South Asian countries, notably Bangladesh and India, have seen a moderate improvement in export performance in recent quarters. In India, the value of merchandise exports grew by 4.2 per cent year on year in the first nine months of 2013, after declining slightly in 2012. This positive trend is likely to persist in the quarters ahead as demand in developed economies strengthens and export industries benefit from a weak rupee. In Bangladesh, garment exports rose rapidly in the second and third quarter of 2013 despite several deadly industrial accidents over the past year and international concerns over the rights of workers. Exports from the Islamic Republic of Iran, by contrast, contracted further over the past year due to the on-going international sanctions. South Asia's *imports* have been weighed down by slowing domestic demand, depreciating national currencies and lower international commodity prices. Accordingly, trade and current account balances, as a percentage of GDP, are projected to improve moderately in 2013. Workers' remittance flows, particularly to Bangladesh, Pakistan and Sri Lanka, have continued to grow strongly and help support current account balances.

Downside risks to the economic outlook for South Asia are related to the expected tightening in global liquidity conditions in 2014-2015 and to regional or domestic vulnerabilities. The upcoming tapering of the Fed's massive asset-purchase program could lead to significant capital outflows, particularly for India. This, in turn, could require further monetary tightening and emergency measures that would weigh on economic growth. Protracted sluggish growth in India would likely have a negative impact on some of its neighbour countries. In Pakistan, the conditions attached to the IMF loan program, such as a considerable fiscal consolidation, entail the risk of further depressing the economy in the short run.

Western Asia

Western Asia will see relatively stable aggregate *growth* of 3.4 per cent in 2013 that will accelerate to 4.5 per cent in 2014 and 2015. However, Arab countries in Western Asia (Western Asia excluding Israel and Turkey) exhibited further polarization in their economic performances. While the member countries of the Gulf Cooperation Council (GCC), namely Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates, have been on a stable recovery path, the economies of Iraq, Jordan, Lebanon, Syria and Yemen have been hampered by continuing political instability, social unrest, security incidents and geopolitical tensions. The Syrian crisis has been impacting the neighboring countries in a multi-faceted way. Most importantly, the influx of refugees into Lebanon and Jordan resulted in a considerable change in the demographic structure and the composition of production factors in both countries. Lebanon and Jordan were thrown off their balanced growth paths when adjusting the projected growth rates in 2013 and 2014 with population increases of 25.0 percent in Lebanon and 15 percent in Jordan. The subdued cross-border economic activities between GCC countries and the rest of Western Asia, including trade, investment and tourism, continued to fail in bringing positive intraregional spillover effects. The stagnation of private capital inflows put Lebanon, Jordan and Yemen under moderate foreign exchange constraints as a source of inflationary pressure. The depletion of capital inflows and foreign reserves, combined with severe supply shortages, led to hyper-inflation in Syria. For 2013, the growth rate of GCC member countries is expected to taper off mainly owing to the moderate decline in oil export revenues, which marked a historical high in 2012. Non-oil sectors, particularly the real estate sector, regained their strength, partly owing to active fiscal policy in this sub-region. Iraq’s growth is also expected to decline moderately in line with its oil export revenues, while growth in Jordan, Lebanon and Yemen remains relatively weak, ranging from 1.3 per cent to 4.8 per cent during 2013-2014.

In *Turkey*, financial markets have been under pressure since May 2013, with the currency depreciating and interbank interest rates rising as a result of a reversal in international capital inflows. This was triggered by the anticipated tapering in global liquidity, as well as concerns about the large public debt and the current account deficit in the country. The devaluation of the currency has in turn added to inflation pressures, with CPI inflation running at about 8.0 per cent. These unfavourable factors are expected to weigh on real economic growth in the near term. GDP is estimated to grow by 3.2 per cent in 2013 and by 5.0 per cent in 2014, before decelerating slightly to 4.6 per cent in 2015. The GDP of *Israel* is estimated to grow at a pace of 3.2 per cent in 2013, driven mainly by consumer demand and net exports. In the outlook, GDP is forecast to grow by 2.2 per cent in 2014 and 3.3 per cent in 2015.

The GCC countries have seen a recovery in *employment* in line with the consistent growth of non-oil sectors, while employment creation was subdued in other economies in the region. However, the issue of employment has remained one of the most important policy challenges in the region, including in GCC countries given high chronic unemployment among nationals. Several GCC countries, most notably Saudi Arabia, shifted to a more stringent labour nationalization policy, rigorously promoting employment of nationals in the private sector where the labor force consists mostly of foreign expatriates. Since March 2013, the Saudi government has encouraged foreign expatriates to rectify their sponsorship status or to voluntarily leave the country. A significant number of foreign workers have left Saudi Arabia voluntarily, which affected especially the parts of the private sector with low skill requirements. In Iraq, Jordan, Lebanon, Palestine and Yemen, chronic high unemployment was exacerbated by low domestic demand growth. Where official statistics are available, the unemployment rate stood at 12.6 per cent in Jordan in the second quarter of 2013, compared to 12.5 per cent in 2012. In the same period, the unemployment rate of Palestine was 20.6 per cent, compared to 23.0 per cent in 2012. Although no official statistics were released, a large portion of the labor force in Syria is estimated to have become unemployed, underemployed or economically inactive. Most Syrian refugees competed for a job in the informal sector with low-skilled labor in host countries.

Although international commodity prices were stable, the average *inflation* rate crept up in the region. For GCC countries, the upward trend in the inflation rate is due to recovering domestic demand. The price of housing-related items, including property rents, showed a robust recovery. Wage increases were observed in several high-skill sectors in GCC countries, but its impact on the general price level is projected to be limited. For Iraq, Jordan and Lebanon, upward creeping inflation stems from modestly binding foreign exchange constraints and a significantly increased number of residents, including Syrian refugees. The depletion of foreign reserves and a substantial devaluation of the national currency caused a state of hyper-inflation in Syria. According to estimates, the consumer inflation rate went beyond the 100.0 per cent mark in August 2013.

Arab countries in Western Asia utilize stable exchange rates as their main monetary anchor. Therefore, *monetary policy* is rather passive as it follows that of the US Federal Reserve. Policy interest rates of GCC countries had already stayed at a very low level and monetary policy focused on liquidity management and on regulating private banks' lending practices. However, having kept the value of their national currency fixed to the dollar, Jordan and Yemen had to maintain a higher policy interest rate to defend the value of their national currency by early 2012. After a recovery in the level of foreign exchange reserves, the Central Bank of Yemen lowered its policy interest rate to 15 percent in February 2013 and the Central Bank of Jordan cut its main policy rates by 25 basis points in August 2013. Jordan cut its policy interest rates for the first time since 2011 after a series of interest rate hikes. The growth of money stock has been on a recovery path in GCC countries due to the improving liquidity supply and increasing demand for credit. Reflecting the improving liquidity, funding rates, represented by 3-month money market rates, further converged among GCC countries in the range between 0.75 percent and 1.26 percent. The three-month EIBOR of the United Arab Emirates, which had been the highest among the equivalent interest rates in GCC countries since 2008, came down below Saudi Arabia's equivalent interest rate in May 2013 and reached 0.8613 percent in August. Reflecting further improvement in liquidity supply, the funding cost of the United Arab Emirates became again competitive among other GCC countries.

Despite depreciation pressure on the currency, the Central Bank of Turkey has refrained from raising interest rates. Instead, it recently adopted an unorthodox policy scheme by creating an interest rate corridor between 6.75 per cent and 7.75 per cent without increasing the policy interest rate. In Israel, with inflation subdued, the central bank has been cutting interest rates during 2013, but monetary policy is expected to tighten in late 2014.

The GCC countries and Iraq remained active in *fiscal policy* on the back of growing oil export revenues in the fiscal year covering 2013 and this trend is projected to continue in 2014. The focus has been on a shift to capital expenditure and large public-sector led infrastructure projects, although the actual fiscal impact on respective economies depends heavily on the implementation rate of budgeted fiscal items. A case in point is Kuwait, where the postponement of planned large public-sector led projects negatively affected overall economic growth. A tightened fiscal policy stance continued in Jordan, Lebanon and Yemen due to decreasing revenues and increasing deficits.

In Turkey, fiscal policy has been somewhat restrictive, with government expenditure growing at a pace much slower than government revenue. In Israel, fiscal policy is neutral, with the budget deficit standing at above 3.0 per cent of GDP. Government spending is expected to grow only moderately in 2014-2015 to curb the deficit further.

The *current account* surpluses of GCC countries and Iraq are estimated to have declined moderately in 2013. Oil export revenues edged down, while imports increased because of robust domestic demand growth. Meanwhile, the current account deficits of Jordan, Lebanon and Yemen are estimated to have narrowed. Without any sign of improvement in export performances, the level of imports declined due to weak domestic demand. The amount of foreign reserves has been on a recovery path in Jordan and Yemen, where the level dipped in the previous year. Lebanon’s foreign reserves growth has stagnated at a sufficiently high level. Syria faced severe foreign exchange constraints as its national currency continuously came under devaluation pressure against foreign currencies. After oil exports ceased in the previous year, Syria’s increasing need to import essential goods puts pressure on already depleted foreign reserves. The Syrian Pound dived in the parallel market to SYP340/$, before recovering to SYP210/$ at the end of September 2013. The exchange rate once stood at SYP48/$ two years ago.

In Turkey, real exports decelerated significantly in 2013, to a growth rate of about 3.0 per cent compared with growth of 16.7 per cent in 2012. Export growth is expected to improve in the outlook, as external demand from Europe starts to recover. Real imports have accelerated from zero growth in 2012 to 8.0 per cent growth in 2013, but the pace of growth is projected to moderate in the outlook, partly due to the recent depreciation. In Israel, both exports and imports declined in 2013, but the drop in the former was less than in the latter, leaving the current account in moderate surplus. The start of natural gas output is expected to boost exports further.

A rise in geopolitical tensions is a *major risk* for the region's economic prospects. Nevertheless, as the region's geopolitical tensions are projected to stay around Syria, GCC countries are projected to be less affected. The division is well reflected in the region's share price performances: in dollar-adjusted terms, stock price indices rose significantly in all GCC countries over the first three quarters of 2013, while those of Syria and its neighbouring countries declined. For GCC countries, the risk lies more in a sudden plunge in oil prices, as happened in 2008. Oil prices are crucial not only for export revenues but also for economic sentiment and confidence of non-oil sectors in GCC countries. If oil prices fell below $80 per barrel in Brent, it would dent the growth of domestic demand. As the source of revenues depends on oil, counter-cyclical fiscal measures may not be sufficient for such contingency. With exchange rates mostly pegged to the US dollar, the region will be impacted by any change in the Federal Reserve's monetary policy stance. The looming reduction of bond purchases by the Federal Reserve will affect the yields of United States Treasury bonds; any rise in yields will affect the borrowing costs in the region, particularly in GCC countries.

Latin America and the Caribbean

Economic growth in Latin America and the Caribbean[13] is expected to decelerate in 2013, reflecting a sluggish global economy, including slightly slower economic growth in China, and domestic constraints in the region's bigger economies. GDP growth will slow to 2.5 per cent in 2013, from 2.9 per cent in 2012. In 2014 and 2015, GDP growth is expected to pick up, 3.6 per cent and 4.3 per cent respectively, sustained mainly by a gradual recovery in developed economies, sound macroeconomic policies, and resilient domestic demand.

In South America, economic growth will accelerate in 2013 to 3.0 per cent, up from 2.4 per cent in 2012, mainly due to a rebound of the Brazilian economy, supported by growing domestic demand, which has only partially compensated for the bleak external environment. In 2014 and 2015, GDP growth in the sub-region is expected to accelerate, to 3.4 per cent and 4.1 per cent respectively. Brazil is expected to recover from the anaemic growth of 0.9 per cent recorded in 2012, but will still perform below potential. In 2013, the economy is expected to expand by 2.3 per cent during the whole year, driven by higher private demand, which has been stimulated by lower interest rates in 2012 and early 2013. Manufacturing output picked up in the second quarter of 2013, but given the relatively low business confidence and tighter monetary policy initiated in April, economic growth will stay on a moderate path. In 2014 and 2015, the Brazilian economy will benefit from a stronger external demand, along with the economic recovery in the US and Europe. However, despite anticipated improvement for the external sector in the coming years, the deceleration of the economic activity in China – the main commodity importer for the region – may reduce annual trade gains as experienced in previous years. In most countries in the sub-region, the dynamism of private consumption has been a relatively common pattern, compensating for the softening of external demand and commodity prices. In 2013, private consumption in Chile and Peru continued on a

[13] The economic forecast was prepared based partially on figures provided by LINK experts.

strong trajectory, while it is growing more moderately in Argentina and Colombia. The outperformers in the South American corner in 2013 will be Paraguay and Peru, which will register GDP growth 12.0 per cent and 6.0 per cent respectively. Paraguay's agricultural sector has been particularly dynamic, in part benefiting from expanding external demand from other South American countries. Despite lower metal prices in 2013, the Peruvian economy is expected to continue to benefit from external demand for their commodities, while foreign investment in the mining sector is expected to remain strong.

In *Mexico and Central America*, economic activity in 2013 is projected to slow down to 1.7 per cent from 3.9 per cent in 2012. This year, the Mexican economy has faced structural constraints and GDP growth decelerated significantly in the first half of 2013 (1.0 per cent year on year), partly due to the change of political administration, which delayed the execution of the federal budget and private decisions on investment. In 2013, the economy is expected to expand only by 1.5 per cent, but the economic outlook is relatively positive for the period covering 2014-2015. The Mexican government has announced a set of reforms, which should solve part of the current structural weaknesses, including inefficient technology in the energy sector, and should potentially stimulate private investment. Mexico, but also Central America, will also benefit from anticipated higher growth rates in the US economy, their main economic partner. The Mexican economy is expected to expand by 4.0 per cent in 2014 and 4.8 per cent in 2015, on the back of better performance of manufacturing exports and stable domestic demand, but also due to the low base effect from 2013. Panama will register the strongest GDP growth in this sub-region in 2013, 7.5 per cent, driven by large scale infrastructural investments, including the expansion of the Canal.

The Caribbean region is still struggling to recover from the impact of the global financial crisis in 2008, experiencing relatively low GDP growth and large current account deficits. There are several factors hampering economic growth in the Caribbean. External demand has been subdued, in particular for the tourism sector, given the relatively slow economic recovery in the United States and in Europe. Weaker commodity prices have also affected net-exporters of commodities in the region. Domestic demand has also been relatively weak on the back of fiscal austerity measures, which are limiting government spending, high levels of unemployment, and limited credit access. In 2013, the Caribbean economy is expected to expand by 2.6 per cent, relatively similar to 2011 and 2012. However, the anticipated economic recovery in developed economies is expected to boost the tourism sector, with indirect spill-overs into other sectors, bringing the Caribbean GDP growth to 3.3 per cent and 3.9 per cent in 2014 and 2015 respectively. Private consumption is also expected to improve, supported by higher level of remittances, considering better employment prospects in the United States in the next two years. Among commodity exporters, Guyana is expected to experience robust economic growth in 2013 and 2014 (4.6 per cent and 4.5 per cent respectively), on the back of strong investment in the mining and energy industries. After weak economic expansion in 2012, Trinidad and Tobago will also post higher GDP growth in 2013 and 2014, 2.0 per cent and 2.5 per cent respectively, although these figures are still lower than previous energy boom years (before 2008).

The regional *unemployment* rate (weighted average) reached a record low of 6.4 per cent in 2012. In early 2013, the unemployment rate was about 6.0 per cent or lower in several South American countries Brazil, Chile, Ecuador, Panama and Uruguay, and Mexico. Regional labour market indicators are likely to remain robust this year, but further improvements, such as additional reductions in unemployment or faster job creation, will be difficult to achieve. However, in several Central American and Caribbean countries, unemployment is relatively higher and is constraining private consumption. In Costa Rica, for instance, the unemployment rate was 9.6 per cent in the first quarter of 2013, while in Jamaica the unemployment rate reached more than 16.0 per cent in April 2013 and is expected to remain high in the near future.

The *inflation* outlook is fairly stable, though it is expected to increase slightly in 2013, as a result of accommodative monetary policies in some countries since the second half of 2012. In Brazil, the inflation rate is expected to reach 6.0 per cent in 2013, which is higher than in 2012 and well above the 4.5 per cent central bank target. However, during the rest of the outlook period, inflation should decline, as a result of the gradual monetary tightening policy initiated in April 2013, by the Banco Central do Brasil. The main risk will come from a weaker currency that could exert price pressures due to imported inflation. In Mexico, inflation has fluctuated throughout the year, but it is expected to remain slightly below the 2012 level of 4.1 per cent. Amid concerns of economic growth, further cuts in the interest rate are possible and could reignite inflationary pressures. Despite the relatively stable consumer price prospects during the forecast period for the region as whole, inflation will remain high in a number of countries. The Bolivarian Republic of Venezuela displays the highest inflation rate in the region (year-on-year consumer price inflation reached 49.0 per cent in September 2013) and the massive depreciation of the local currency in early 2013 is adding to price pressures. The Caribbean sub-region is managing inflation relatively well, helped by lower commodity prices. However, as domestic demand improves in 2014, inflation rates are expected to increase. In addition, these economies are highly vulnerable to supply-side inflationary pressures, in particular from international food price shocks, which could create additional challenges.

In general, *monetary policy* is expected to continue to be relatively expansionary in 2013, but it will be gradually reversed throughout 2014, as inflationary pressures mount. In 2012, several countries modified their monetary stance with the goal of promoting economic activity, given the output gap. Brazil adopted the most aggressive expansionary monetary policy in the region, maintaining the interest rate (Selic) at a 7.25 per cent historical low, between October 2012 and March 2013. Consequently, inflationary pressures increased, compelling the Banco Central do Brasil to initiate a monetary tightening cycle in April, despite slow economic growth. During the forecast period, Brazil will have relatively less monetary policy room to support the economy, given the current inflationary pressures. Conversely, the Banco de Mexico decided to cut its reference interest rate in March 2013 for the first time in four years, amid concerns over low economic growth. As inflationary pressures subsided in the summer, there is still room for additional cuts in the interest rate, if economic growth remains sluggish.

Nevertheless, the Banco de Mexico is expected to cautiously manage its monetary policy during the forecast period. In the Caribbean, as well as in several Central American countries, central banks are expected to maintain their accommodative monetary policies in 2013, before a gradual tightening in the forecast period, as price pressures are expected to rise. In some countries, such as Jamaica and Honduras, further currency depreciation could spark inflation and force central banks to adopt monetary tightening measures sooner than expected.

In the aftermath of the global financial crisis, the region enjoyed the benefits of sounder macroeconomic fundamentals, including lower public debt ratios, which helped governments adopting stimulus measures. However, the *fiscal position* deteriorated slightly in 2012, mainly because of higher public expenditures in South America. Brazil's primary fiscal surplus, for instance, is expected to deteriorate in 2013, as social unrest has forced the government to adopt an expansionary fiscal policy. At the same time, the global slowdown and the decline in regional terms of trade generated contractions of public revenues in several commodity exporter countries. The structural dependency of public revenues on commodity exports results in fiscal balances vulnerable to external shocks. Tax revenues, which are more closely linked to domestic demand, showed more robust behaviour recently. In 2012, Argentina, Chile, the Dominican Republic, Ecuador, El Salvador, Guatemala, Panama, and Peru have implemented fiscal reforms in an attempt to broaden the tax base. These reforms were crucial, but not yet sufficient. Overall, in South America, the fiscal position is not as strong as prior to the financial crisis, and Governments may find it more difficult to provide stimulus if global economic conditions deteriorate further. However, in countries, such as Bolivia, Chile and Peru, governments have preserved some space for countercyclical policies. In Mexico, a moderate the fiscal deficit is expected to continue in 2013, as the government will favour the expansion of the economy in the short term, rather than focusing strictly on macroeconomic discipline. In 2014-2015, as economic activity gains momentum, the government is expected to establish fiscal discipline, while reforming the tax system in order to increase tax revenues. In the Caribbean, public debt-to-GDP ratios are traditionally high and fiscal deficits are expected to increase in several countries, given weak revenues and, for example, large public investments in Guyana. However, in 2014 and 2015, fiscal deficits should shrink, as serious efforts have been made to reduce spending, for instance in Jamaica, and tax revenues should increase along with a better economic outlook.

The *external sector* has been affected by the sluggish global economy and strong currencies, which should lead to a wider current account deficit in 2013. Throughout 2013, export performance has been affected by lower demand from China, one of the major economic partners for the region, and lower commodity prices. The current situation contrasts with the previous cycle of surpluses, when commodity prices were relatively high. In the region as a whole, the still feeble global recovery will limit major export expansions before the end of the year. The current account deficit in the region is also aggravated by robust domestic demand and stronger currencies, which have kept the import bill growing faster than export gains. However, current account deficits will be manageable in a great number of countries. In 2014 and 2015, an improvement is expected on the back of the economic recovery in developed economies. The US economy in particular, but the euro area as well, is expected to pick up next year, increasing demand for Latin American and Caribbean exports. In addition, a price recovery of key commodities is anticipated for the region’s exports, as international demand is expected to improve in 2014. However, despite anticipating improvement for the external sector in the near future, the deceleration of the economic activity in China–the main commodity importer for the region–may reduce annual trade gains as experienced in previous years. This could particularly affect several countries in South America. In the Caribbean economies, such as Barbados, Haiti, and Jamaica current account deficits are expected to remain high in 2013, owing to traditionally high import levels, while services’ revenues from the tourism sector are still lower than prior to the crisis of 2008-2009. In 2014 and 2015, as developed economies are expected to perform better economically, the tourism sector should generate higher revenues, narrowing current account deficits in this region. In a number of countries, such as Guyana, massive investments in the mining and energy sectors are expected to drive imports higher and consequently widen the current deficit during the forecast period. Part of the current account deficit will be covered by higher FDI inflows.

In many cases, financing requirements have been covered by *FDI and capital inflows*. In 2012, global financial liquidity, relatively high interest rate differentials with respect to developed countries and moderately good regional economic prospects encouraged capital flows to the region. However, in 2013, this picture changed considerably, as economic prospects for the region started to deteriorate, but also after the US Fed announced in June 2013 that it would gradually taper its QE programme. As a result, investors changed their financial positions in emerging markets, reversing capital inflows and leading to instability in major currencies and financial markets in the region. During the third quarter of 2013, many Latin American currencies depreciated against the US dollar, which may increase inflationary pressures and constrain domestic investment, as imports become more expensive. On a positive note, the region has accumulated abundant international reserves, which should give monetary authorities room to deal with currency volatility. In addition, currency depreciations could support the manufacturing sector in the medium term, in particular for Mexico and other Central American economies. However, structural constraints would need to be addressed in order to take advantage of more competitive exchange rates. Infrastructural investments, including in commodity sectors, should continue to attract FDI in the region during the forecast period, particularly in Brazil, Chile, Colombia, Peru, and Guyana. Solid macroeconomic fundamentals and an expanding middle class should also reinforce the attractiveness of Latin America for international investors, in particular from the US – the largest foreign investor in the region in 2012. However, FDI would need to be channelled towards non-commodity sectors in order to diversify their economies. In the current context of high volatility of capital inflows and significant uncertainties in developed countries, the region will face the challenge of coordinating fiscal, monetary, and exchange rate policies in order to preserve financial stability and stimulate economic growth.

There are *risks* to this forecast on the downside, related to economic uncertainties in the euro area and the United States, but also in China, which is now accepting slower growth than in previous years. Tighter monetary policy in the US would present challenges to the region, through limited financing of investment, in particular for the economies that have accumulated fiscal and external imbalances. In addition to external risks, domestic policies to support the economy face a number of challenges. A major issue will be for economies to find the right balance between controlling

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Statistics Annex Table

Table A.1
World and regions: rates of growth of real GDP, 2008-2015
(Annual percentage change[a])

	2008	2009	2010	2011	2012 [b]	2013 [c]	2014 [c]	2015 [c]
World	1.5	-2.1	4.0	2.8	2.4	2.1	2.9	3.3
Developed economies	0.0	-3.7	2.6	1.5	1.4	1.0	1.9	2.4
North America	-0.2	-2.8	2.6	1.9	2.7	1.5	2.5	3.2
Asia and Oceania	-0.5	-4.4	4.2	-0.1	2.3	2.0	1.6	1.2
Europe	0.4	-4.4	2.0	1.7	-0.3	0.0	1.5	1.9
European Union	0.4	-4.5	2.0	1.7	-0.4	-0.1	1.4	1.9
EU-15	0.1	-4.6	2.0	1.5	-0.5	-0.1	1.4	1.8
New EU Members	4.0	-3.8	2.1	3.1	0.6	0.6	2.1	2.7
Other Europe	1.2	-1.9	1.7	1.6	1.9	1.7	2.6	2.9
Memorandum items:								
Euro area	0.4	-4.4	2.0	1.6	-0.7	-0.5	1.1	1.6
Major developed economies (G7)	-0.3	-3.9	2.9	1.5	1.6	1.1	2.0	2.4
OECD	0.1	-3.6	2.9	1.7	1.5	1.1	2.1	2.5
Economies in transition	5.4	-6.6	4.6	4.7	3.2	2.4	2.5	3.6
South-Eastern Europe	5.1	-2.1	1.6	1.9	-0.9	1.6	1.9	2.9
Commonwealth of Independent States and Georgia	5.4	-6.8	4.8	4.8	3.4	2.4	2.5	3.6
Developing countries	5.2	2.7	7.6	5.8	4.7	4.5	5.1	5.4
Africa	5.2	2.7	4.7	1.0	5.4	4.0	4.9	5.1
North Africa	4.9	3.6	4.1	-5.6	6.7	2.5	4.2	4.6
East Africa	6.7	4.4	7.0	6.3	5.6	5.9	6.4	6.3
Central Africa	5.0	3.0	4.8	5.1	4.4	4.2	4.7	4.0
West Africa	5.9	5.5	6.7	6.1	6.7	6.6	6.9	6.7
Southern Africa	4.9	-0.4	3.5	3.9	3.5	3.6	4.1	4.4
East and South Asia	6.1	5.3	9.0	6.9	5.4	5.5	5.8	6.0
East Asia	6.4	5.2	9.2	7.1	5.9	5.9	6.2	6.2
South Asia	4.6	6.1	8.0	6.4	3.6	3.8	4.6	5.2
Western Asia	3.9	-1.5	6.7	6.8	3.5	3.4	4.5	4.5
Latin America and the Caribbean	4.0	-1.5	5.8	4.3	2.9	2.5	3.6	4.3
South America	5.4	-0.2	6.5	4.5	2.4	3.0	3.4	4.1
Mexico and Central America	1.7	-4.2	4.9	4.1	3.9	1.7	4.0	4.8
Caribbean	3.6	0.9	3.5	2.7	2.7	2.4	3.3	3.8
Memorandum items:								
Least developed countries	7.7	5.1	5.8	3.4	4.3	5.3	5.6	5.6
East Asia (excluding China)	2.8	0.2	7.7	4.2	3.3	3.4	4.1	4.4
South Asia (excluding India)	3.1	3.8	5.2	3.9	-0.1	1.5	2.9	3.7
Western Asia (excluding Israel and Turkey)	5.7	0.0	5.8	6.1	4.4	3.5	4.5	4.7

Source : UN/DESA

[a] Calculated as a weighted average of individual country growth rates of gross domestic product (GDP), where weights are based on GDP in 2005 prices and exchange rates.

[b] Actual or the most recent estimate.

[c] Forecasts, based in part on Project LINK.

Table A.2
Rates of growth of real GDP, 2008-2015
(Annual percentage change)

	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
Developed Economies								
North America								
Canada	1.2	-2.7	3.4	2.5	1.7	1.6	2.6	2.8
United States	-0.3	-2.8	2.5	1.8	2.8	1.5	2.5	3.2
Asia and Oceania								
Australia	2.4	1.5	2.6	2.4	3.7	2.6	2.8	3.1
Japan	-1.0	-5.5	4.7	-0.6	2.0	1.9	1.3	0.8
New Zealand	-0.6	0.3	0.9	1.3	3.2	2.6	3.0	3.0
European Union								
EU-15								
Austria	1.4	-3.8	1.8	2.8	0.9	0.7	1.8	2.2
Belgium	1.0	-2.8	2.4	1.8	-0.3	-0.4	0.5	1.3
Denmark	-0.8	-5.7	1.6	1.1	-0.4	0.7	1.8	2.8
Finland	0.3	-8.5	3.4	2.7	-0.8	-0.8	0.7	1.4
France	-0.1	-3.1	1.7	2.0	0.0	0.1	0.8	1.1
Germany	1.1	-5.1	4.0	3.3	0.7	0.4	1.9	1.9
Greece	-0.2	-3.1	-4.9	-7.1	-6.4	-4.5	-1.0	1.3
Ireland	-2.2	-6.4	-1.1	2.2	0.2	-0.3	1.2	2.2
Italy	-1.2	-5.5	1.7	0.5	-2.5	-1.9	0.7	1.3
Luxembourg	-0.7	-5.6	3.1	1.9	-0.2	0.9	3.0	2.0
Netherlands	1.8	-3.7	1.5	0.9	-1.2	-1.2	0.5	1.2
Portugal	0.0	-2.9	1.9	-1.3	-3.2	-2.1	0.1	1.3
Spain	0.9	-3.8	-0.2	0.1	-1.6	-1.2	0.9	2.1
Sweden	-0.6	-5.0	6.6	2.9	1.0	1.1	2.6	3.3
United Kingdom	-0.8	-5.2	1.7	1.1	0.1	1.4	2.2	2.4
New EU Member								
Bulgaria	6.2	-5.5	0.4	1.8	0.8	1.0	1.6	2.1
Croatia	2.1	-6.9	-2.3	0.0	-2.0	-0.9	1.0	2.0
Cyprus	3.6	-1.9	1.3	0.4	-2.4	-13.9	-4.2	-1.4
Czech Republic	3.1	-4.5	2.5	1.8	-1.0	-0.5	1.5	3.0
Estonia	-4.2	-14.1	2.6	9.6	3.9	2.5	2.9	3.0
Hungary	0.9	-6.8	1.3	1.6	-1.7	0.2	2.0	2.3
Latvia	-2.8	-17.7	-1.3	5.3	5.0	4.0	4.0	4.0
Lithuania	2.9	-14.8	1.6	6.0	3.7	3.0	3.0	3.5
Malta	3.9	-2.8	4.0	1.6	0.8	0.7	1.1	2.5
Poland	5.1	1.6	3.9	4.5	1.9	1.2	2.5	3.0
Romania	7.3	-6.6	-1.1	2.2	0.7	2.6	3.0	3.1
Slovak Republic	5.8	-4.9	4.4	3.2	2.0	0.9	1.6	2.2
Slovenia	3.4	-7.9	1.3	0.7	-2.5	-2.4	-0.2	1.0
Other European								
Iceland	1.2	-6.6	-4.1	2.7	1.4	2.0	2.4	2.5
Norway	0.1	-1.6	0.5	1.2	3.1	1.7	2.7	2.7
Switzerland	2.2	-1.9	3.0	1.8	1.0	1.6	2.5	3.0
Economies in transition								
South-Eastern Europe								
Albania	7.6	3.3	3.9	2.0	1.6	1.9	2.6	4.0
Bosnia and Herzegovina	5.6	-2.9	0.7	1.7	-1.0	1.2	2.0	2.5
Montenegro	6.9	-5.7	2.5	3.2	-2.5	2.3	2.5	3.0
Serbia	3.8	-3.5	1.0	1.6	-1.7	1.5	1.5	2.8
The former Yugoslav Republic of Macedonia	5.0	-0.9	1.8	3.0	-0.3	2.0	2.0	2.0
Commonwealth of Independent States								
Armenia	6.9	-14.2	2.2	4.7	7.1	5.4	6.0	5.0
Azerbaijan	10.9	9.2	5.0	0.1	2.2	4.5	5.0	4.2
Belarus	10.3	0.1	7.7	5.3	1.5	1.5	2.5	3.0
Kazakhstan	3.4	1.2	7.2	7.5	4.9	5.2	6.0	6.0
Kyrgyzstan	8.4	2.9	-0.5	5.7	-0.9	7.0	6.0	5.5
Republic of Moldova	7.9	-6.0	7.1	6.4	-0.8	3.0	4.0	4.0
Russian Federation	5.3	-7.9	4.3	4.3	3.4	2.0	1.8	3.2
Tajikistan	7.6	4.0	6.5	7.4	7.5	6.0	6.0	5.0
Turkmenistan	14.8	6.1	9.2	14.6	11.1	9.0	9.5	9.5
Ukraine	2.3	-14.8	4.1	5.2	0.2	0.3	2.1	3.0
Uzbekistan	9.1	8.0	8.5	8.3	8.2	7.0	6.9	6.1
Georgia	2.3	-3.8	6.3	7.0	6.1	3.0	4.0	4.5

	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
Developing Economies								
Africa								
Algeria	2.4	2.4	3.3	2.8	2.9	3.1	3.7	3.6
Angola	13.8	2.4	3.7	3.9	6.8	6.8	6.9	6.7
Benin	5.0	2.6	2.5	3.2	3.6	4.2	4.1	4.0
Botswana	3.0	-4.8	7.0	3.7	3.7	4.1	4.0	3.9
Burkina Faso	5.8	2.9	7.9	-7.9	9.2	6.9	7.1	6.8
Burundi	13.6	3.5	3.9	4.2	4.0	4.4	4.6	4.9
Cameroon	2.9	1.9	3.2	5.6	4.7	5.0	5.2	5.3
Cape Verde	6.2	3.5	5.4	5.4	4.6	3.0	3.4	3.9
Central African Republic	2.0	1.7	3.0	1.9	4.1	-8.9	1.2	1.8
Chad	0.3	4.1	14.6	0.7	5.0	4.5	7.2	4.8
Comoros	1.0	1.8	2.0	2.2	2.5	3.4	3.8	4.1
Congo	6.0	7.5	8.7	4.5	3.8	6.0	6.2	5.9
Côte d'Ivoire	2.3	3.8	3.0	-4.7	9.5	8.8	7.2	6.7
Democratic Republic of the Congo	6.2	2.7	7.2	6.9	7.2	7.3	8.0	6.9
Djibouti	5.8	5.0	3.5	4.4	4.8	5.3	5.8	6.4
Egypt	7.2	4.6	5.2	1.8	2.2	1.9	2.1	3.3
Equatorial Guinea	15.3	4.6	-0.8	7.1	2.5	1.8	1.1	-1.3
Eritrea	-9.8	3.9	2.2	8.7	5.5	6.0	6.6	5.0
Ethiopia	10.8	8.8	12.5	11.2	7.8	6.9	6.5	6.4
Gabon	1.8	-0.4	5.6	5.8	5.9	5.5	5.4	5.4
Gambia	5.5	6.3	6.0	5.5	5.2	8.0	7.5	6.4
Ghana	8.4	4.6	6.7	14.4	7.9	8.0	8.6	8.9
Guinea	4.7	0.9	2.1	2.7	3.9	3.5	5.0	5.1
Guinea-Bissau	4.0	12.7	6.0	4.1	-1.5	1.9	3.8	3.5
Kenya	1.5	2.7	5.7	4.4	4.6	4.5	5.5	5.8
Lesotho	5.5	2.8	5.6	5.8	3.8	4.6	5.7	5.2
Liberia	8.1	7.8	7.3	8.2	8.4	7.5	7.3	7.0
Libya	2.7	-0.8	4.2	-62.0	104.1	-2.0	15.1	12.2
Madagascar	7.1	-4.2	0.4	1.6	1.9	2.6	3.6	4.0
Malawi	8.3	8.9	6.7	4.5	1.9	4.5	4.4	4.2
Mali	5.0	3.4	4.1	2.7	-1.2	4.5	6.1	5.9
Mauritania	-0.7	0.1	5.6	5.1	5.4	6.1	5.9	5.6
Mauritius	5.5	3.3	4.1	3.5	3.3	3.1	3.7	3.9
Morocco	5.6	4.7	3.7	4.1	2.7	4.6	4.0	4.9
Mozambique	6.9	6.3	6.8	7.1	7.4	6.5	7.3	7.1
Namibia	4.3	-0.7	6.6	4.9	5.0	4.2	6.1	5.9
Niger	9.6	-1.8	5.6	2.3	11.2	5.7	6.4	6.1
Nigeria	6.3	6.9	7.8	7.4	6.6	6.5	6.9	6.7
Rwanda	11.1	6.2	7.2	8.6	8.0	7.4	7.6	6.7
Sao Tome and Principe	9.4	4.8	4.5	4.9	5.0	3.9	4.2	4.5
Senegal	3.7	2.0	4.1	2.8	3.6	4.3	4.7	4.4
Sierra Leone	5.2	-1.2	2.2	6.5	15.2	14.5	11.2	9.5
South Africa	3.6	-1.7	2.9	3.5	2.6	2.7	3.3	3.7
Togo	2.4	3.3	4.0	3.9	5.6	5.8	6.1	6.2
Tunisia	4.5	3.1	3.5	-1.5	3.6	2.9	3.8	4.3
Uganda	10.4	4.2	6.3	4.1	2.8	5.8	6.6	6.9
United Republic of Tanzania	7.5	6.0	7.0	6.4	6.9	7.2	7.3	6.9
Zambia	5.7	6.7	6.5	6.6	6.1	7.7	7.9	7.4
Zimbabwe	-4.7	16.9	9.6	10.3	3.1	2.2	2.4	2.5
East and South Asia								
Bangladesh	6.0	5.9	6.3	6.5	6.2	5.9	6.0	6.4
Brunei Darussalam	-1.9	-1.8	2.6	2.2	0.9	1.7	2.1	2.0
China	9.6	9.2	10.3	9.2	7.7	7.6	7.5	7.3
Hong Kong, Special Administrative Region of China	2.4	-2.7	7.0	5.0	1.5	2.8	3.5	3.3
India	5.2	7.2	9.2	7.5	5.1	4.7	5.2	5.7
Indonesia	6.0	4.6	6.2	6.5	6.2	5.6	5.7	6.0
Iran, Islamic Republic of	2.1	3.2	5.5	2.8	-5.1	-2.0	0.8	1.7
Korea, Republic of	2.3	0.3	6.3	3.7	2.0	2.6	3.3	3.6
Malaysia	4.9	-1.5	7.1	5.1	5.6	4.4	4.9	5.2
Myanmar	10.2	10.6	10.4	5.4	5.0	5.3	6.1	6.4
Nepal	5.6	4.6	4.5	4.1	3.9	4.0	4.2	4.3
Pakistan	2.6	3.5	3.2	3.4	4.0	3.6	3.3	4.3
Papua New Guinea	6.7	6.2	7.6	8.8	9.2	5.4	5.7	13.5
Philippines	4.2	1.1	7.6	3.7	6.8	6.9	6.2	6.3
Singapore	1.8	-1.0	14.7	4.9	1.3	2.6	3.6	4.0
Sri Lanka	6.0	3.5	8.0	8.3	6.4	6.8	7.0	6.8
Taiwan, Province of China	0.8	-1.9	10.9	4.1	1.3	2.2	3.3	3.6
Thailand	1.7	-1.1	7.5	0.1	6.5	3.4	4.3	4.7
Vietnam	6.3	5.3	6.8	5.9	5.0	5.3	5.7	6.0

	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
Western Asia								
Bahrain	6.3	3.1	4.5	2.2	3.4	3.7	3.7	3.7
Iraq	6.6	5.8	5.9	8.6	9.3	6.1	6.8	7.9
Israel	5.2	1.1	3.9	4.6	3.3	3.2	2.2	3.3
Jordan	7.3	5.5	2.3	2.6	2.7	3.2	3.9	4.4
Kuwait	4.2	-7.8	7.9	8.2	7.9	4.1	3.8	4.4
Lebanon	8.6	9.0	7.0	1.5	1.7	1.3	2.4	4.8
Oman	12.9	1.1	8.1	5.5	5.5	5.1	3.9	3.8
Qatar	17.7	12.0	16.7	13.5	6.2	5.2	5.2	5.5
Saudi Arabia	4.2	0.1	5.1	7.1	5.1	3.5	5.1	5.0
Syrian Arab Republic	4.5	5.9	3.4	-2.0	-18.8	-11.3	4.2	4.1
Turkey	0.7	-4.8	9.2	8.8	2.2	3.2	5.0	4.6
United Arab Emirates	3.2	-4.8	1.3	4.2	4.4	3.7	3.9	4.1
Yemen	4.0	4.3	7.8	-10.5	1.3	4.1	2.6	2.5
Latin America and the Caribbean								
Argentina	6.8	0.8	9.2	8.9	1.9	3.5	3.0	3.0
Barbados	0.4	-4.1	0.2	0.6	0.2	0.0	1.0	2.0
Bolivia, Plurinational State of	6.1	3.4	4.1	5.2	5.2	4.9	5.0	5.1
Brazil	5.1	-0.3	7.6	2.8	0.9	2.3	3.0	4.2
Chile	3.3	-1.0	5.8	5.9	5.6	4.3	4.4	4.6
Colombia	3.6	1.7	4.0	5.9	4.0	3.7	4.2	4.5
Costa Rica	2.8	-1.0	4.7	4.2	5.1	3.0	4.2	4.3
Cuba	4.1	1.4	2.4	2.7	3.0	2.9	3.9	4.0
Dominican Republic	5.3	3.4	7.7	4.5	3.9	2.5	3.5	4.4
Ecuador	7.3	0.4	3.6	7.8	5.1	4.2	4.2	4.4
El Salvador	1.3	-3.2	1.3	1.5	1.6	1.5	1.8	2.0
Guatemala	3.3	0.5	2.9	3.9	3.0	2.8	3.5	3.8
Guyana	2.1	3.3	3.6	4.6	4.8	4.6	4.5	4.0
Haiti	0.9	2.9	-5.4	5.6	2.8	3.5	4.5	4.8
Honduras	4.2	-2.1	2.8	3.6	3.3	3.0	3.2	3.4
Jamaica	-0.8	-3.1	-1.4	1.5	-0.3	0.2	1.2	1.9
Mexico	1.4	-4.7	5.1	4.0	3.8	1.5	4.0	4.8
Nicaragua	2.9	-1.5	4.5	4.7	5.2	4.2	4.1	4.3
Panama	10.2	3.8	7.6	10.6	10.6	7.5	6.9	6.6
Paraguay	5.9	-3.9	15.0	3.8	-1.2	12.0	4.6	4.7
Peru	9.8	0.8	8.7	6.9	5.4	6.0	6.1	6.3
Trinidad and Tobago	2.4	-3.5	2.5	-1.4	0.4	2.0	2.5	2.7
Uruguay	7.2	2.4	8.9	5.7	3.9	3.5	4.1	4.2
Venezuela, Bolivarian Republic of	5.3	-3.2	-1.5	3.9	5.6	1.2	2.5	2.9

Source: Project LINK

a Actual or most recent estimate.
b Forecasts, based in part on Project LINK.

Table A.3
World and regions: consumer price inflation, 2008-2015
(Annual percentage change[a])

	2008	2009	2010	2011	2012 [b]	2013 [c]	2014 [c]	2015 [c]
World	4.9	1.2	2.8	3.6	2.9	2.6	2.8	2.7
Developed economies	3.5	-0.1	1.8	2.5	1.9	1.4	1.8	1.8
North America	4.2	-0.7	2.4	2.9	2.1	1.5	1.7	1.6
Asia and Oceania	1.8	-0.8	-0.1	0.3	0.2	0.6	2.2	2.0
Europe	3.5	0.8	1.9	2.9	2.4	1.7	1.7	1.9
European Union	3.5	0.8	1.9	3.0	2.6	1.8	1.8	1.9
EU-15	3.3	0.7	1.9	3.0	2.5	1.8	1.7	1.9
New EU Members	6.1	3.1	2.8	3.7	3.7	2.0	2.1	2.4
Other Europe	3.1	0.9	1.5	0.7	-0.1	0.7	1.1	1.4
Memorandum items:								
Euro area	3.3	0.3	1.6	2.7	2.5	1.7	1.8	1.9
Major developed economies (G7)	3.4	-0.3	1.7	2.4	1.9	1.4	1.8	1.8
OECD	3.7	0.2	2.0	2.6	2.1	1.6	1.9	2.0
Economies in transition	14.7	11.2	7.0	9.8	6.9	6.6	6.8	6.7
South-Eastern Europe	9.3	4.3	4.1	7.2	4.8	5.3	5.1	4.3
Commonwealth of Independent States and Georgia	15.0	11.5	7.1	9.9	7.0	6.7	6.8	6.8
Developing countries [d]	8.2	4.2	5.4	6.4	5.5	5.7	5.6	5.3
Africa [d]	11.0	8.0	6.5	7.9	8.2	7.0	6.8	6.3
North Africa	9.7	6.4	6.2	7.8	9.1	8.1	7.4	6.3
East Africa	21.7	14.4	7.3	16.6	12.6	6.9	6.7	6.9
Central Africa	6.6	4.3	2.4	2.0	4.4	3.9	3.3	3.3
West Africa	11.2	9.4	10.2	8.9	9.4	7.3	7.5	7.6
Southern Africa [d]	10.4	7.9	5.3	6.1	6.1	6.1	6.2	6.0
East and South Asia	7.4	2.8	4.9	6.2	4.9	5.1	5.0	4.6
East Asia	6.0	0.6	3.2	4.8	2.8	2.5	3.1	3.2
South Asia	12.6	11.2	11.5	11.1	12.5	14.5	12.2	9.9
Western Asia	10.3	4.1	5.6	5.9	5.6	5.7	5.3	6.1
Latin America and the Caribbean	7.7	6.0	6.0	6.5	6.0	6.7	6.7	6.1
South America	8.7	6.6	7.0	8.0	7.1	8.2	8.2	7.1
Mexico and Central America	5.7	5.1	4.1	3.6	4.1	4.0	4.4	4.3
Caribbean	12.9	4.1	8.2	7.5	5.7	5.6	4.6	5.1
Memorandum items:								
Least developed countries	13.8	8.8	8.9	11.7	12.6	10.3	8.8	7.9
East Asia (excluding China)	6.1	1.8	3.0	4.2	2.9	2.6	3.0	3.1
South Asia (excluding India)	21.3	11.7	10.6	15.8	18.4	24.5	18.7	13.8
Western Asia (excluding Israel and Turkey)	11.2	2.9	4.3	5.9	4.1	5.3	4.0	4.3

Source : UN/DESA

[a] Calculated as a weighted average of individual country growth rates of consumer price index (CPI), where weights are based on GDP in 2005, in the United States dollar.

[b] Actual or the most recent estimate.

[c] Forecasts, based in part on Project LINK.

Table A.4
Consumer price inflation, 2008-2015
(Annual percentage change)

	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
Developed Economies								
North America								
Canada	2.4	0.3	1.8	2.9	1.5	1.1	1.8	2.0
United States	4.3	-0.8	2.5	2.9	2.1	1.5	1.7	1.6
Asia and Oceania								
Australia	4.4	1.8	2.9	3.3	1.8	1.9	2.0	2.2
Japan	1.4	-1.3	-0.7	-0.3	0.0	0.3	2.2	2.0
New Zealand	4.0	2.1	2.3	4.0	1.1	1.3	2.1	2.0
European Union								
EU-15								
Austria	3.2	0.4	1.7	3.5	2.6	2.0	2.0	2.0
Belgium	4.5	0.0	2.3	3.4	2.6	1.2	2.3	2.3
Denmark	3.6	1.1	2.2	2.7	2.4	1.3	1.6	1.9
Finland	3.9	1.6	1.7	3.3	3.2	2.3	1.9	2.0
France	3.2	0.1	1.7	2.3	2.2	1.1	1.8	1.8
Germany	2.8	0.2	1.1	2.5	2.1	2.4	2.1	2.2
Greece	4.2	1.4	4.7	3.1	1.0	-0.5	0.1	0.3
Ireland	3.1	-1.7	-1.6	1.2	1.9	1.1	0.5	1.2
Italy	3.5	0.8	1.6	2.9	3.3	1.5	1.8	1.8
Luxembourg	3.4	0.4	2.3	3.4	2.7	2.0	2.2	2.0
Netherlands	2.2	1.0	0.9	2.5	2.8	3.0	1.7	2.0
Portugal	2.7	-0.9	1.4	3.6	2.8	0.6	1.4	1.5
Spain	4.1	-0.2	2.0	3.1	2.4	1.3	1.1	2.1
Sweden	3.4	1.9	1.9	1.4	0.9	0.1	0.8	2.0
United Kingdom	3.6	2.2	3.3	4.5	2.8	2.6	1.8	1.7
New EU members								
Bulgaria	12.3	2.8	2.5	4.2	3.0	1.4	2.6	3.9
Croatia	6.0	2.4	1.0	2.3	3.4	2.7	2.0	2.3
Cyprus	4.7	0.4	2.4	3.3	2.4	0.5	1.9	2.2
Czech Republic	6.3	0.6	1.2	2.1	3.5	2.0	2.0	2.0
Estonia	10.6	0.2	2.7	5.1	4.2	3.5	3.5	3.5
Hungary	6.0	4.0	4.7	3.9	5.7	2.3	3.0	3.0
Latvia	15.4	3.5	-1.1	4.4	2.5	0.8	1.5	2.5
Lithuania	10.9	4.4	1.3	4.1	3.1	1.5	2.5	2.7
Malta	4.2	2.1	1.4	2.8	2.4	1.7	2.2	2.0
Poland	4.2	4.0	2.7	3.9	3.7	1.1	1.5	2.0
Romania	7.9	5.6	6.1	5.8	3.3	4.8	3.0	3.0
Slovak Republic	3.9	0.9	0.7	4.1	3.7	1.8	2.5	2.2
Slovenia	5.5	0.9	2.1	2.1	2.8	1.7	1.9	1.5
Other Europe								
Iceland	12.7	12.0	5.4	4.0	5.2	3.5	2.7	3.4
Norway	3.4	2.3	2.3	1.2	0.4	1.8	1.9	2.1
Switzerland	2.3	-0.7	0.6	0.1	-0.7	-0.3	0.3	0.8
Economies in Transition								
South-eastern Europe								
Albania	3.3	2.3	3.6	3.4	2.1	2.1	2.7	2.7
Bosnia and Herzegovina	7.4	-0.3	2.2	3.7	2.1	1.0	2.0	2.9
Montenegro	9.0	3.8	0.6	3.2	4.1	3.0	3.0	2.7
Serbia	12.4	8.2	6.1	11.2	7.3	9.0	8.0	6.0
The former Yugoslav Republic of Macedonia	8.4	-0.8	1.5	3.9	3.2	3.0	3.0	2.5
Commonwealth of Independent States								
Armenia	8.9	3.4	8.2	7.7	2.5	5.5	4.0	3.0
Azerbaijan	20.6	4.5	-0.9	8.0	1.8	3.0	7.5	4.5
Belarus	14.5	12.6	7.9	51.4	60.0	21.0	12.0	8.3
Kazakhstan	17.1	7.3	7.1	8.3	5.1	6.0	6.4	6.1
Kyrgyzstan	24.5	6.9	8.0	16.4	2.7	7.4	6.0	5.0
Republic of Moldova	10.8	0.6	13.3	8.6	8.8	4.5	5.2	5.0
Russian Federation	14.0	11.7	6.9	8.4	5.0	6.8	6.7	6.7
Tajikistan	32.9	6.5	6.4	27.3	6.0	5.5	5.5	6.0
Turkmenistan	14.5	-2.7	4.4	12.0	8.2	10.2	10.0	8.0
Ukraine	21.6	17.4	10.1	8.7	8.2	1.4	5.9	8.0
Uzbekistan	12.7	14.1	9.4	12.8	11.5	10.0	11.0	8.8
Georgia	10.1	1.7	7.1	8.6	-1.0	-0.5	2.5	3.0

	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
Developing Economies								
Africa								
Algeria	4.9	5.7	3.9	4.5	8.9	4.8	4.4	4.1
Angola	12.5	13.7	14.5	13.5	10.3	9.0	8.5	8.2
Benin	7.9	2.2	2.3	2.7	6.5	3.6	3.2	3.3
Botswana	12.7	8.0	5.6	7.8	7.5	5.5	5.6	5.4
Burkina Faso	10.7	2.6	-0.8	2.8	3.8	2.1	2.0	2.2
Burundi	24.1	11.0	6.4	9.7	18.0	9.7	6.8	7.2
Cameroon	5.3	3.0	1.3	2.9	2.9	2.6	2.5	2.6
Cape Verde	6.8	1.0	2.1	4.5	2.5	1.8	2.2	2.3
Central African Republic	9.3	3.5	1.3	1.3	5.7	7.0	3.5	3.5
Chad	10.3	10.0	-2.1	-4.9	9.8	4.5	4.9	4.6
Comoros	4.8	4.8	4.6	6.8	6.0	4.5	3.8	3.7
Congo	7.3	5.3	5.0	1.3	3.9	7.6	4.0	4.1
Côte d'Ivoire	6.3	1.0	1.7	4.9	1.3	2.9	2.6	2.5
Democratic Republic of the Congo	17.3	46.0	23.0	15.5	6.5	5.8	6.5	6.0
Djibouti	12.0	1.7	4.0	11.5	5.0	2.5	2.2	2.5
Egypt	18.3	11.8	11.3	10.1	7.1	9.1	10.2	8.5
Equatorial Guinea	6.6	4.7	7.8	6.9	6.1	6.0	5.6	5.3
Eritrea	19.9	33.0	12.7	14.0	14.0	12.8	12.5	12.0
Ethiopia	44.4	8.5	8.1	33.0	22.2	9.1	9.5	8.8
Gabon	5.3	1.9	1.5	1.3	2.7	1.2	1.6	1.6
Gambia	4.5	4.6	5.0	4.8	4.6	5.5	4.2	4.4
Ghana	16.5	19.3	10.7	8.7	8.8	9.0	8.7	8.5
Guinea	18.4	4.7	13.7	17.9	15.2	11.9	9.0	8.5
Guinea-Bissau	10.5	-1.7	2.5	5.0	2.1	1.9	1.8	2.0
Kenya	26.2	9.2	4.0	14.0	9.4	5.7	6.0	6.3
Lesotho	10.7	7.4	3.6	5.0	6.1	5.0	4.4	4.1
Liberia	17.5	7.4	7.3	7.4	5.5	5.2	6.0	6.1
Libya	10.4	2.5	2.8	15.5	6.1	3.1	5.0	6.2
Madagascar	9.2	9.0	9.2	9.5	6.0	7.0	6.3	6.0
Malawi	8.7	8.4	7.4	7.6	31.0	18.0	9.1	9.1
Mali	9.2	2.5	1.1	2.9	5.4	0.4	3.1	2.9
Mauritania	7.3	2.2	6.3	5.6	4.9	4.6	5.0	5.2
Mauritius	9.7	2.5	2.9	6.5	3.3	5.4	3.3	3.8
Morocco	3.7	1.0	1.0	0.9	1.3	2.3	2.4	2.5
Mozambique	10.3	3.3	12.7	10.2	2.2	-0.1	8.0	7.8
Namibia	10.4	8.8	0.1	4.1	6.3	4.8	4.4	4.5
Niger	11.3	0.6	0.8	2.9	0.6	1.9	2.1	2.0
Nigeria	11.6	11.5	13.7	10.8	12.2	9.1	9.5	9.6
Rwanda	15.4	10.4	2.3	5.7	6.3	5.7	6.3	5.8
Sao Tome and Principe	26.1	17.0	13.3	12.0	8.0	8.7	6.9	6.6
Senegal	5.8	-1.1	1.3	3.4	1.2	1.5	1.6	1.6
Sierra Leone	14.8	9.3	16.8	17.3	12.9	11.1	10.2	9.4
Somalia	30.0	25.0	2.1	2.2	2.0	2.0	4.0	5.0
South Africa	10.0	7.3	4.0	5.1	5.8	5.8	5.9	5.7
Togo	8.7	3.3	1.8	3.6	2.6	2.2	2.4	2.8
Tunisia	4.9	3.5	4.4	3.6	5.5	6.0	5.2	4.5
Uganda	12.1	13.0	4.0	18.7	14.0	5.4	5.8	6.5
United Republic of Tanzania	10.3	12.1	6.2	12.7	16.0	8.6	6.5	7.3
Zambia	12.4	13.4	8.5	6.4	-8.0	8.0	10.3	10.7
Zimbabwe			5.9	5.4	8.3	8.5	6.6	6.1
East and South Asia								
Bangladesh	8.9	5.4	8.1	10.7	8.7	7.7	7.2	6.7
Brunei Darussalam	2.1	1.0	0.4	2.0	0.5	0.9	1.0	1.2
China	5.9	-0.7	3.3	5.5	2.6	2.5	3.1	3.3
Hong Kong, Special Administrative Region	4.3	0.6	2.3	5.3	4.1	4.3	3.9	3.8
India	8.3	10.9	12.0	8.9	9.7	9.7	9.0	8.1
Indonesia	10.2	4.4	5.1	5.4	4.3	6.9	6.3	5.5
Iran, Islamic Republic of	25.5	13.5	10.1	20.6	27.3	41.1	29.8	20.6
Korea, Republic of	4.7	2.8	2.9	4.0	2.2	1.3	2.1	2.5
Malaysia	5.4	0.6	1.7	3.2	1.7	1.9	2.6	2.8
Myanmar	26.8	1.5	7.7	5.1	6.0	5.9	6.8	6.3
Nepal	10.9	11.6	10.0	9.5	9.5	8.8	8.3	7.9
Pakistan	20.3	13.6	13.9	11.9	9.7	7.2	7.5	6.9
Papua New Guinea	10.8	6.9	6.0	8.4	2.2	3.4	4.5	5.1
Philippines	8.3	4.1	3.9	4.6	3.2	2.9	3.5	3.7
Singapore	6.5	0.6	2.8	5.3	4.5	2.5	2.9	2.7
Sri Lanka	22.6	3.5	6.2	6.7	7.5	7.0	5.9	5.5
Taiwan, Province of China	3.5	-0.9	1.0	1.4	1.9	1.0	1.8	1.8
Thailand	5.5	-0.8	3.3	3.8	3.0	2.2	2.6	3.0
Viet Nam	23.1	7.1	8.9	18.7	9.1	6.9	7.1	7.3

	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
Western Asia								
Bahrain	3.5	2.8	2.0	-0.4	2.8	3.0	3.1	3.0
Israel	4.6	3.3	2.7	3.5	1.7	1.6	1.3	1.7
Jordan	14.9	-0.7	5.0	4.4	4.8	3.8	5.9	5.4
Kuwait	10.6	4.0	4.0	4.7	2.9	3.0	3.2	3.7
Oman	12.1	3.9	3.2	4.1	2.9	1.6	3.1	2.9
Qatar	15.1	-4.9	-2.4	1.9	1.9	3.1	4.2	4.6
Saudi Arabia	9.9	5.1	5.3	5.8	2.9	3.8	3.3	4.3
Syrian Arab Republic	15.7	2.9	4.4	4.8	36.7	59.1	17.8	12.0
Turkey	10.4	6.3	8.6	6.5	8.9	7.5	8.5	10.2
Yemen	19.0	5.4	11.2	16.4	17.3	11.8	11.7	12.6
Latin America and the Caribbean								
Argentina	8.6	6.3	10.8	9.5	10.0	10.5	11.4	10.8
Barbados	8.1	3.6	5.8	9.4	4.8	2.1	4.2	2.2
Bolivia, Plurinational State of	14.0	3.3	2.5	9.8	4.5	4.5	4.0	4.0
Brazil	5.6	4.9	5.0	6.7	5.8	5.7	5.4	4.8
Chile	8.7	0.3	1.4	3.3	3.0	1.8	2.5	3.1
Colombia	7.0	4.2	2.3	3.4	3.2	2.5	4.3	3.9
Costa Rica	13.4	7.8	5.7	4.9	4.5	5.6	4.7	5.5
Dominican Republic	10.6	1.4	6.3	8.5	3.7	4.8	3.6	4.1
Ecuador	8.4	5.2	3.6	4.5	5.1	2.7	3.9	4.0
El Salvador	6.7	1.1	1.2	5.1	1.8	1.2	2.7	3.1
Guatemala	11.4	1.9	3.9	6.2	3.8	4.3	4.4	4.5
Guyana	8.1	2.9	2.1	5.0	2.4	3.9	4.0	5.0
Haiti	15.5	0.0	5.7	8.4	6.3	4.7	4.8	5.1
Honduras	11.4	5.5	4.7	6.8	5.2	5.4	5.4	5.8
Jamaica	22.0	9.6	12.6	7.5	6.9	8.5	6.2	6.6
Mexico	5.1	5.3	4.2	3.4	4.1	4.0	4.4	4.2
Nicaragua	19.8	3.7	5.5	8.1	7.2	7.4	6.1	6.9
Panama	8.8	2.4	3.5	5.9	5.7	4.2	4.0	3.8
Paraguay	10.2	2.6	4.7	8.3	3.7	3.2	4.6	4.8
Peru	5.8	2.9	1.5	3.4	3.7	2.8	2.5	2.0
Trinidad and Tobago	12.0	7.0	10.5	5.1	9.2	6.4	5.8	6.8
Uruguay	7.9	7.1	6.7	8.1	8.1	8.5	8.6	8.1
Venezuela, Bolivarian Republic of	29.8	27.1	28.2	26.1	21.1	36.4	34.4	27.1

Source: Project LINK

a Actual or most recent estimate.
b Forecasts, based in part on Project LINK.

Table A.5
World trade: growth in trade value of goods and non-factor services, by major country group, 2008-2015
(Annual percentage change)

Region	Flow	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
World	Exports	14.1	-19.7	19.5	18.1	2.6	2.2	5.9	7.4
	Imports	14.4	-20.1	19.0	18.0	2.0	1.9	6.3	7.6
Developed economies	Exports	11.1	-19.7	13.8	15.2	-1.7	1.8	4.0	5.4
	Imports	11.4	-22.0	14.4	15.8	-1.9	-0.1	4.3	5.7
North America	Exports	9.6	-16.9	17.2	14.5	3.6	1.9	5.5	6.5
	Imports	7.6	-22.1	19.9	13.2	2.7	1.8	6.5	7.4
Asia and Oceania	Exports	13.9	-23.4	30.9	11.5	-1.9	-5.0	10.3	12.0
	Imports	20.7	-24.8	23.9	23.1	6.2	-5.4	7.3	7.6
Europe	Exports	11.2	-20.0	10.5	16.0	-3.4	2.8	2.5	4.0
	Imports	11.6	-21.6	11.0	15.7	-5.1	0.1	2.8	4.5
European Union	Exports	10.7	-20.2	10.4	15.8	-3.5	3.1	2.6	3.9
	Imports	11.6	-21.9	10.8	15.6	-5.3	0.1	2.8	4.5
EU-15	Exports	9.9	-20.1	9.9	15.3	-3.6	2.9	2.6	3.9
	Imports	10.7	-21.1	10.4	15.1	-5.4	-0.1	2.9	4.6
New EU Members	Exports	18.1	-21.3	14.4	19.5	-3.3	5.0	2.6	4.5
	Imports	19.0	-27.7	14.1	19.0	-4.2	2.0	1.7	4.1
Other Europe	Exports	18.5	-17.8	11.3	19.0	-1.4	-0.8	2.4	4.8
	Imports	11.8	-15.6	12.9	18.2	-1.4	-1.2	2.9	4.6
Euro area	Exports	9.3	-20.0	14.9	14.1	-0.6	1.2	5.1	6.5
	Imports	10.0	-21.8	16.1	15.5	-0.8	-0.1	5.6	6.8
Economies in transition	Exports	31.6	-33.0	27.8	31.6	10.7	3.5	-0.5	4.6
	Imports	29.1	-29.9	22.0	28.2	8.9	8.5	4.0	5.2
South-eastern Europe	Exports	22.2	-20.3	12.8	21.3	-1.4	10.5	5.2	5.5
	Imports	26.3	-27.6	3.0	19.3	0.1	7.8	5.9	7.1
Commonwealth of Independent States	Exports	32.0	-33.5	28.5	32.1	11.1	3.3	-0.7	4.6
	Imports	29.4	-30.1	23.9	28.9	9.6	8.5	3.8	5.1
Developing countries	Exports	17.3	-18.3	27.7	20.9	7.6	2.4	8.8	10.0
	Imports	19.1	-15.4	26.7	20.8	7.2	4.1	9.0	10.3
Africa	Exports	27.6	-26.4	28.5	20.4	21.0	-3.6	3.6	6.0
	Imports	25.0	-11.7	10.7	16.6	5.0	7.3	10.7	11.9
North Africa	Exports	29.8	-27.8	15.2	5.6	39.3	-13.2	4.0	2.6
	Imports	36.7	-12.1	4.5	3.0	11.3	8.0	11.0	13.2
East Africa	Exports	18.4	-12.5	29.2	19.2	13.4	9.3	12.1	11.3
	Imports	27.2	-8.1	15.4	14.9	14.8	10.7	12.3	12.3
Central Africa	Exports	40.5	-31.7	26.3	13.3	10.6	4.5	-6.5	2.1
	Imports	34.8	-5.3	13.6	20.7	18.1	11.1	6.2	5.2
West Africa	Exports	38.3	-26.6	45.7	37.9	17.4	1.2	0.0	4.7
	Imports	10.0	-4.4	16.9	30.5	-14.7	9.7	13.2	12.7
Southern Africa	Exports	18.3	-25.3	35.9	27.1	9.8	0.3	6.2	9.8
	Imports	19.9	-17.0	12.6	23.3	7.4	3.5	9.1	11.1
East and South Asia	Exports	13.8	-14.5	28.5	20.0	6.7	3.9	10.4	11.2
	Imports	17.3	-14.3	31.2	21.9	7.9	3.0	8.9	10.1
East Asia	Exports	13.6	-15.4	28.7	19.6	7.2	5.1	11.0	10.7
	Imports	16.9	-16.0	32.6	21.4	8.8	3.3	8.9	9.7
South Asia	Exports	16.0	-6.0	27.2	23.1	2.8	-6.3	5.2	15.7
	Imports	20.0	-2.7	23.0	25.4	2.4	0.9	8.7	13.0
Western Asia	Exports	28.7	-26.3	20.8	29.1	6.5	1.2	5.0	6.4
	Imports	21.8	-17.5	14.9	18.9	7.4	9.5	10.5	12.0
Latin America and the Caribbean	Exports	15.3	-20.7	31.0	17.8	5.1	0.7	8.3	10.0
	Imports	20.8	-20.2	28.3	19.3	4.7	2.9	7.3	8.3
South America	Exports	21.1	-21.6	35.6	18.2	6.2	-2.4	9.5	11.6
	Imports	30.6	-18.5	31.5	20.7	4.5	1.1	6.6	8.4
Mexico and Central America	Exports	7.2	-18.4	25.5	17.2	3.1	6.0	6.5	7.6
	Imports	9.6	-22.0	25.5	17.7	5.0	4.8	7.9	8.0
Caribbean	Exports	12.0	-27.9	12.4	15.9	6.4	3.7	5.0	6.6
	Imports	19.7	-24.1	12.6	15.3	3.6	13.1	11.5	10.3
Least developed countries	Exports	28.0	-22.0	24.4	28.7	77.6	-28.9	7.8	10.2
	Imports	31.7	-4.2	9.5	21.8	75.7	-27.2	9.7	11.6

Source: UN/DESA

a Actual or the most recent estimate.
b Forecast, based in part on Project LINK.

Table A.6
World trade: growth in trade volume of goods and non-factor services, by major country group, 2008-2015
(annual percentage change)

Region	Flow	2008	2009	2010	2011	2012 [a]	2013 [b]	2014 [b]	2015 [b]
World	Exports	2.8	-9.3	12.7	6.5	3.1	2.3	4.7	5.3
	Imports	2.8	-10.5	13.6	6.9	2.6	2.5	4.9	5.2
Developed economies	Exports	1.9	-11.7	11.3	5.5	2.4	1.6	4.2	5.1
	Imports	0.4	-12.2	10.8	4.7	1.0	0.5	4.1	4.7
North America	Exports	3.2	-10.0	10.5	6.6	3.1	2.0	4.3	4.8
	Imports	-2.1	-13.4	12.9	5.0	2.4	1.4	4.8	5.0
Asia and Oceania	Exports	1.8	-17.1	18.0	-0.4	1.6	3.8	7.3	8.4
	Imports	2.5	-14.2	11.8	7.0	5.5	1.6	7.2	5.3
Europe	Exports	1.6	-11.4	10.6	6.0	2.2	1.2	3.6	4.6
	Imports	1.1	-11.4	9.9	4.1	-0.2	0.0	3.3	4.4
European Union	Exports	1.5	-11.8	11.0	6.4	2.2	1.3	3.7	4.7
	Imports	1.1	-11.6	9.9	4.1	-0.4	0.0	3.4	4.4
EU-15	Exports	1.1	-11.9	10.7	6.0	2.1	1.1	3.6	4.7
	Imports	0.7	-10.9	9.6	3.7	-0.5	-0.2	3.4	4.5
New EU Members	Exports	5.2	-10.7	13.6	9.0	3.1	3.1	4.1	4.7
	Imports	4.9	-16.8	12.6	7.4	0.4	0.8	2.9	3.9
Other Europe	Exports	1.8	-6.1	4.7	1.6	2.2	-0.7	2.9	4.1
	Imports	0.6	-8.2	8.5	4.1	2.8	0.0	2.9	3.7
Euro area	Exports	1.7	-13.3	12.7	5.6	2.4	1.4	4.6	5.6
	Imports	-0.5	-12.0	11.6	4.7	1.4	0.8	4.9	5.3
Economies in transition	Exports	1.8	-7.4	6.6	3.0	1.1	1.5	2.1	2.4
	Imports	11.7	-26.1	16.6	16.2	7.3	7.4	3.8	2.4
South-eastern Europe	Exports	4.4	-10.3	19.6	6.6	3.4	6.8	6.2	5.3
	Imports	7.1	-19.0	8.8	5.1	1.7	4.8	5.4	6.0
Commonwealth of Independent States	Exports	1.7	-7.3	6.2	2.9	1.0	1.2	1.9	2.3
	Imports	12.1	-26.7	17.3	17.1	7.7	7.6	3.7	2.1
Developing countries	Exports	4.2	-6.0	15.4	8.4	4.2	3.2	5.5	5.7
	Imports	6.4	-5.8	18.1	9.7	4.5	4.9	6.0	6.3
Africa	Exports	7.9	-14.4	9.1	-3.4	11.4	-0.8	5.9	5.0
	Imports	9.1	-5.7	7.5	7.3	3.9	5.6	6.7	6.9
North Africa	Exports	5.6	-7.8	2.2	-25.7	29.3	-7.1	9.6	6.3
	Imports	16.7	-5.2	1.6	2.6	11.0	6.9	7.2	8.0
East Africa	Exports	12.2	-4.1	18.5	13.0	5.9	5.0	5.6	4.9
	Imports	11.5	4.4	14.9	8.0	7.5	6.8	6.5	6.8
Central Africa	Exports	3.3	-3.7	0.7	8.6	3.6	-1.1	0.0	1.6
	Imports	11.4	7.3	2.0	4.5	11.6	2.6	2.1	2.0
West Africa	Exports	21.8	-20.9	40.9	23.0	4.0	2.5	3.3	2.9
	Imports	-4.1	5.5	16.0	14.4	-15.5	6.0	9.2	7.6
Southern Africa	Exports	5.5	-21.9	4.4	5.2	2.6	3.1	5.0	5.7
	Imports	8.7	-15.5	7.6	7.8	7.9	4.4	5.5	6.2
East and South Asia	Exports	4.4	-2.9	20.0	10.7	3.6	4.6	6.0	6.3
	Imports	5.3	-1.6	20.7	10.0	4.6	5.1	6.2	6.6
East Asia	Exports	4.1	-3.4	20.8	10.6	3.8	4.9	6.1	6.3
	Imports	4.1	-2.1	22.5	9.4	4.9	5.5	6.4	6.7
South Asia	Exports	7.5	0.9	13.6	11.7	1.9	1.7	5.3	6.9
	Imports	13.3	1.5	10.0	13.9	2.7	1.9	4.9	6.2
Western Asia	Exports	3.5	-8.3	6.7	7.6	5.0	-0.4	4.1	4.0
	Imports	7.7	-13.8	8.8	9.0	4.1	4.6	4.8	6.0
Latin America and the Caribbean	Exports	1.6	-9.6	9.6	6.5	2.4	2.9	4.5	5.1
	Imports	8.1	-14.8	21.6	10.5	4.9	3.9	5.4	4.7
South America	Exports	1.3	-7.9	5.4	6.0	0.3	2.4	4.6	5.1
	Imports	12.6	-12.3	25.7	12.7	3.7	3.2	4.9	4.3
Mexico and Central America	Exports	1.4	-12.1	18.6	8.0	5.7	3.5	4.3	5.0
	Imports	2.9	-18.0	18.2	8.0	7.1	4.2	5.8	5.0
Caribbean	Exports	9.0	-15.3	3.7	0.2	5.1	5.6	5.6	4.8
	Imports	7.2	-15.9	1.2	3.9	1.8	11.5	7.9	5.8
Least developed countries	Exports	7.1	-17.3	7.1	6.4	6.0	5.3	6.0	5.6
	Imports	11.4	-4.8	10.2	5.5	8.0	5.1	6.6	6.7

Source: UN/DESA

a Actual or the most recent estimate.
b Forecast, based in part on Project LINK.