Table A2 East Asia and Pacific country forecasts
(annual percent change unless indicated otherwise)

	1995–2005[a]	2006	2007	2008	2009[c]	2010[d]	2011[d]
Cambodia							
GDP at market prices (2005 US$)[b]	8.3	10.8	10.2	6.7	−2.2	4.2	6.0
Current account balance/GDP (%)	−4.4	−3.6	−6.3	−10.2	−3.5	−4.0	−4.0
China							
GDP at market prices (2005 US$)[b]	9.1	11.6	13.0	9.0	8.4	9.0	9.0
Current account balance/GDP (%)	2.6	9.7	11.0	9.8	5.6	4.1	4.0
Fiji							
GDP at market prices (2005 US$)[b]	2.3	3.6	−6.6	0.2	−0.3	1.8	2.2
Current account balance/GDP (%)	−4.8	−22.5	−14.4	−19.6	−25.4	−24.8	−27.7
Indonesia							
GDP at market prices (2005 US$)[b]	2.7	5.5	6.3	6.1	4.5	5.6	5.8
Current account balance/GDP (%)	1.5	3.0	2.4	0.1	1.4	0.5	0.3
Lao PDR							
GDP at market prices (2005 US$)[b]	6.2	8.4	7.6	7.3	6.4	7.5	7.3
Current account balance/GDP (%)	−9.8	1.4	2.5	−12.5	−8.1	−6.0	−7.0
Malaysia							
GDP at market prices (2005 US$)[b]	4.8	5.8	6.2	4.6	−2.3	4.1	4.8
Current account balance/GDP (%)	6.5	16.3	15.5	17.5	15.3	15.5	15.0
Papua New Guinea							
GDP at market prices (2005 US$)[b]	0.7	2.6	6.5	6.6	3.9	3.7	3.3
Current account balance/GDP (%)	3.0	2.2	1.8	2.8	−6.7	−4.7	−4.3
Philippines							
GDP at market prices (2005 US$)[b]	4.2	5.3	7.1	3.8	1.0	3.5	3.8
Current account balance/GDP (%)	−1.4	4.5	4.9	2.5	3.4	2.8	2.3
Thailand							
GDP at market prices (2005 US$)[b]	2.7	5.3	4.9	2.6	−2.7	3.5	4.0
Current account balance/GDP (%)	1.9	1.1	5.7	−0.1	5.5	3.5	3.0
Vanuatu							
GDP at market prices (2005 US$)[b]	1.5	7.4	6.8	6.6	4.2	4.5	5.5
Current account balance/GDP (%)	−9.8	−4.1	−5.3	−5.9	−4.7	−4.4	−3.4
Vietnam							
GDP at market prices (2005 US$)[b]	7.2	8.2	8.5	6.2	5.5	6.5	7.0
Current account balance/GDP (%)	−2.5	−0.3	−9.8	−11.9	−5.1	−4.5	−4.4

Source: World Bank.

Note: World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not significantly differ at any given moment in time.

American Samoa; Micronesia, Fed. Sts.; Kiribati; Marshall Islands; Myanmar; Mongolia; N. Mariana Islands; Palau; Korea, Dem. Rep.; Solomon Islands; Timor-Leste; and Tonga are not forecast owing to data limitations.

a. Growth rates over intervals are compound average; growth contributions, ratios, and the GDP deflator are averages.
b. GDP measured in constant 2005 U.S. dollars.
c. Estimate.
d. Forecast.

Europe and Central Asia

Recent developments

Among developing regions, the Europe and Central Asia region[4] has been the most negatively affected by the global financial crisis, albeit with large variations across the region in the degree of impact. Aggregate GDP is estimated to have contracted 6.2 percent in 2009, nearly twice as much as the 3.3 percent estimated decline in high-income countries, and sharply more negative than the (2.2 percent) contraction for the remaining developing countries excluding China and India (table A3).

Table A3 Europe and Central Asia forecast summary
(annual percent change unless indicated otherwise)

	1995–2005[a]	2006	2007	2008	2009[e]	2010[f]	2011[f]
GDP at market prices (2005 US$)[b]	4.1	7.6	7.1	4.2	−6.2	2.7	3.6
GDP per capita (units in US$)	4.0	7.5	7.1	4.2	−6.2	2.6	3.5
PPP GDP[c]	4.0	7.7	7.4	4.5	−6.5	2.7	3.6
Private consumption	4.8	7.5	9.2	6.4	−4.6	2.2	3.3
Public consumption	2.0	6.0	5.2	4.1	2.3	2.1	2.6
Fixed investment	4.7	16.5	14.2	8.7	−16.5	4.1	4.7
Exports, GNFS[d]	7.9	8.1	7.1	3.9	−13.2	4.3	6.6
Imports, GNFS[d]	8.7	13.9	17.9	9.0	−12.9	3.7	6.0
Net exports, contribution to growth	0.1	−1.5	−3.4	−1.9	0.3	0.1	0.0
Current account balance/GDP (%)	0.9	1.1	−0.6	−0.3	0.5	0.4	−0.2
GDP deflator (median, LCU)	18.8	9.3	7.7	9.5	3.5	6.7	4.0
Fiscal balance/GDP (%)	−5.5	3.0	2.4	0.7	−6.2	−4.5	−3.4
Memo items: GDP							
Transition countries	4.0	6.9	5.7	3.0	−4.1	2.2	3.8
Central and Eastern Europe	3.8	6.8	6.8	5.0	−2.5	1.3	3.5
Commonwealth of Independent States	4.1	8.3	8.4	5.4	−8.1	3.1	3.3
Russian Federation	3.9	7.7	8.1	5.6	−8.7	3.2	3.0
Turkey	4.3	6.9	4.7	0.9	−5.8	3.3	4.2
Poland	4.3	6.2	6.7	4.9	1.6	2.2	3.4

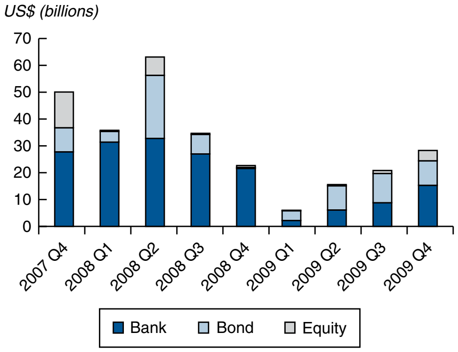
Source: World Bank.
a. Growth rates over intervals are compound average; growth contributions, ratios, and the GDP deflator are averages.
b. GDP measured in constant 2005 U.S. dollars.
c. GDP measured at PPP exchange rates.
d. Exports and imports of goods and nonfactor services.
e. Estimate.
f. Forecast.

The severity of the impact of the crisis in the region reflects significant preexisting vulnerabilities in many countries. Many economies were heavily reliant on foreign finance (a result of excessive credit expansion that had been enabled by foreign banks, large current account deficits, elevated external debt levels, and considerable currency mismatches in both corporate and household debt). As a result, this region was particularly vulnerable to the reversal in capital flows that accompanied the initial phases of the financial crisis.

Sharply reduced external demand for exports, a halving of foreign direct investment inflows, and falling remittances exacerbated the collapse in investor confidence and credit tightening, forcing a sharp contraction of 4.6 percent in regional private consumption, and a decline in gross fixed investment of 16.5 percent in 2009—down from expansions of 6.4 percent and 8.7 percent, respectively, in 2008. The impact of the crisis was most negative in countries where households and corporations held large foreign currency obligations (Armenia, Bulgaria, Croatia, Latvia, Lithuania, Romania, Turkey, and Ukraine), and where pre-crisis growth relied heavily on foreign capital inflows (Bulgaria, Georgia, Latvia, Lithuania, the former Yugoslav Republic of Macedonia, Moldova, Montenegro, and Romania are among the largest, with current account deficits equivalent to 10 percent or more of GDP in 2008). At the same time, petroleum exporters (Kazakhstan, the Russian Federation) were also hit hard by the plunge in international commodity prices.

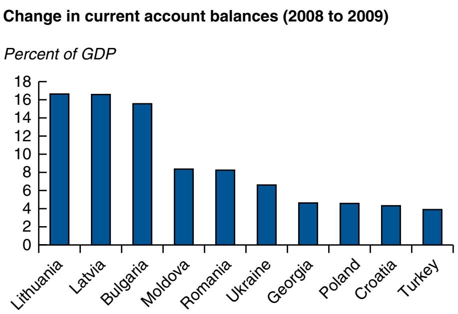
Sharp declines in international financing have forced large adjustments in domestic demand. Gross capital inflows to the region fell 54 percent during 2009, versus the 19 percent increase posted by other developing countries (figure A8). This decline in inflows primarily reflects the drying up of syndicated bank lending, which represented 60 percent of total flows to the region in 2007, before the crisis. Partly

Figure A8 Gross capital flows to Europe and Central Asia picked up in mid-2009



Sources: Dealogic: Bondware, Loanware and World Bank.

Figure A9 Many European and Central Asian economies post sharp current account adjustments



Source: World Bank.

reflecting substantial support from international financial institutions, bond and equity flows to countries in the region began recovering in the third quarter of 2009, although bank lending remains very weak.

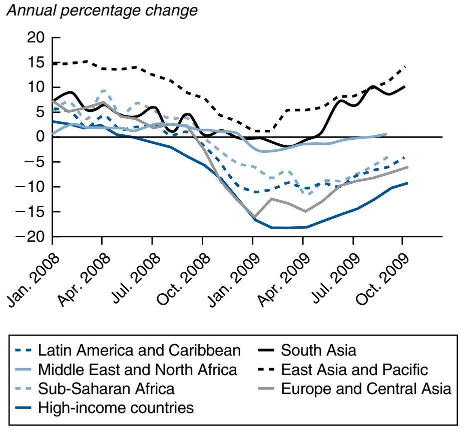
Reflecting the cut in capital inflows (and the associated cuts in domestic demand), regional current account deficits have narrowed, with Bulgaria, Latvia, and Lithuania posting double-digit improvements in current account positions measured as a share of GDP (figure A9). As a result of the cuts in spending, the region's ex post financing needs declined, while at the same time external assistance and moral suasion helped prevent access to external finance from declining as sharply as had been initially expected.

Reflecting these developments, financing conditions have improved. Spreads on sovereign debt, which rose sharply in the third quarter of 2008 and into the first quarter of 2009, have since narrowed. In the case of Ukraine, for example, spreads over U.S. Treasuries jumped by as much as 3,100–3,660 basis points in March 2009 but have since reversed to a spread of 768 points, as of early January. These improved market conditions have also been supported by an easing of inflationary pressures, which has enabled monetary policies to focus on cushioning the downturn. Many governments also implemented countercyclical fiscal policies to support domestic demand. Reflecting these measures, as well as the depth of the recession and much weaker commodity prices, government deficits have increased by about 7 percent of GDP, moving from a surplus of 0.7 percent in 2008 to a 6.2 percent of GDP deficit in 2009.

Although economic activity in Europe and Central Asia remains depressed, the pace of contraction is moderating. Thus, although industrial production in the region began expanding at a 4.8 percent annualized pace in the second quarter of 2009, output in October 2009 remained 6.0 percent below its pre-crisis level in October 2008 (figure A10).

In Russia, the 2009 recession is estimated to have been much sharper than was the one following the 1998 crisis. During the 2009 recession, GDP is estimated to have fallen 8.7 percent, compared with 5.3 percent in the 1998 crisis, and represents the largest decline in growth since the breakup of the Soviet Union.[5] The contraction reflects both external factors (import demand among Russia's main trading partners decreased by an estimated 15 percent in 2009) and domestic factors (an 18 percent decline in investment and a 4.7 percent contraction in private consumption). Reflecting widespread economic slack, inflation

Figure A10 Pace of contraction in industrial production moderates in Europe and Central Asia



Sources: IMF and World Bank.

has fallen below the 10 percent level, and the Russian central bank has repeatedly lowered its refinancing rate, so that it is nearly zero in real terms. The government has also put in place a large fiscal stimulus program, and as a result the fiscal budget is projected to move from a surplus of 4.3 percent of GDP in 2008 to a deficit equivalent to 7 percent of GDP in 2009.

Turkey's economy is projected to have contracted by 5.8 percent in 2009, nearly on par with the 5.7 percent decline posted during the 2001 economic crisis and its largest contraction on record since 1969. The economy has been hit by an investor pullback and sharp decline in demand from export markets, notably from western and eastern Europe, where economies have posted some of the sharpest slowdowns globally. The pace of contraction in growth hit the trough in the first quarter of 2009, at 14.7 percent compared with the previous year, but has eased significantly to a 3.3 percent rate of contraction in the third quarter—a relatively rapid turnaround. Unemployment has surged, contributing to the marked decline in private consumption and fixed investment. With import volumes contracting even faster than export volumes, the current account deficit improved to 1.9 percent of GDP in 2009 from an estimated 5.8 percent of GDP in 2008. To support domestic demand, the Central Bank of Turkey has more than halved its key policy interest rate, cutting it by a cumulative 1,025 basis points from 16.75 percent in October 2008 to 6.5 percent as of January 2010.

Economic conditions remained difficult over the first three quarters of 2009 for the five new members of the European Union that are developing countries, although the pace of contraction in real output moderated from 12.6 percent year-over-year in the first quarter to 4.4 in the third quarter. Partly in response to strengthening demand in high-income Europe, industrial production grew at a 6.5 percent annualized rate in the three months ending in October.

Among the five European Union accession members that are developing countries,[6] Poland has best weathered the economic storm and is one of a handful of the 24 developing countries in Europe and Central Asia not to witness a contraction in output. Poland's good performance reflects comparatively resilient service and agricultural sectors, compared with industrial output, which fell by 9 percent in the first half of 2009 over the first half of 2008. Exports were also relatively resilient, and as a result, net exports contributed positively to growth.

Outside of Poland, the other four developing European Union accession economies posted marked contractions in output during 2009, given the bursting of the credit boom and contraction in demand from Western Europe. The economies of Latvia and Lithuania were under significant stress before the onset of the acute phase of the crisis—a situation that was exacerbated by heightened international risk aversion (and concerns about the sustainability of their pegs to the euro given huge accumulated imbalances). GDP in both countries is estimated to have declined by well over 10 percent in 2009. All four countries entered the crisis with very large current account deficits. While the collapse in domestic demand has improved their external positions, substantial external debt obligations remain, further undermining the business and investment environment.

Among the Commonwealth of Independent States, Ukraine is projected to post the deepest contraction in GDP of 15 percent in 2009—indeed one of the sharpest contractions in the world. The plunge in metal prices in 2008 took a toll on the economy, where nonprecious metals represent over 40 percent of goods exports. Further, political strains in the lead-up to the January 2010 presidential elections have delayed the government from meeting the full set of IMF policy measures (such as raising household gas prices) under its $11 billion November 2008 stand-by facility. Thus, while the government has made some progress in meeting its commitments to the IMF, it appears that the release of the latest $3.7 billion tranche will be postponed until after the elections. This uncertainty—along with ongoing political instability—has undermined confidence and contributed to the depreciation and heightened volatility in the hryvnya, which depreciated by 50 percent against the U.S. dollar in 2009.

Economic growth in the five Central Asian countries has been relatively more robust than in the rest of the region.[7] However, this aggregate picture masks wide differences in economic performances at the country level. Turkmenistan and Uzbekistan—among the least open economies in the Commonwealth of Independent States and exporters of natural gas—were only modestly affected by the global crisis. In addition, these economies benefited from the implementation of fiscal stimulus measures and are estimated to have posted the strongest GDP growth outcomes in the Europe and Central Asia region, with 8 percent and 5.5 percent, respectively, in 2009. Growth in Tajikistan and Kyrgyz Republic was buoyed by an upswing in agricultural output stemming from good harvests. In contrast, GDP in Kazakhstan is estimated to have contracted, led by the negative fiscal effects from the collapse in oil prices.

Among the three Caucasus countries,[8] the global crisis has had a particularly pronounced impact on Armenia and to a lesser extent Georgia—with economic conditions in the latter also negatively affected by the conflict with Russia in 2008. In most of the other Central Asian and Caucasus countries, weaker economic conditions—notably a sharp reduction in trade demand from Russia, lower oil and commodity prices, and significant reductions in investment and remittance flows—have been partially offset by sustained economic assistance from Russia.

Overall, the number of poor or vulnerable people in the Europe and Central Asia region is estimated to have increased by some 10 million in 2009—compared with what might have been had the crisis not arisen (based on a $5-a-day poverty line). The contraction in economic activity has led to a 2.5 percentage point jump in the median unemployment rate of the 10 countries reporting data (compared with August 2008). Unemployment is expected to remain high for some time, curtailing household expenditures and contributing to higher poverty rates. Partly as a result of higher unemployment in destination countries (notably the European Union and Russia) for migrants, remittances are projected to decline by 15 percent in 2009—placing additional pressure on poor households. The macroeconomic impact from the decline in remittances will be largest in countries such as Albania, Armenia, Moldova, and Tajikistan, where remittances represent between 9 percent of GDP (Armenia) and as much as 50 percent of GDP (Tajikistan). In Tajikistan an estimated 30 percent contraction in remittances may cause an additional 5 percent of the population to move into poverty.[9]

Medium-term outlook

The recovery in economic growth in the region is expected to be slow and marked by a rise in poverty. GDP is projected to rise a modest 2.7 percent and 3.6 percent in 2010 and 2011, respectively. This growth path contrasts sharply with the average growth rate for the region of 7 percent from 2003 through 2007, and with the aggregate growth of 5.6 percent and 6.1 percent projected for other developing countries in 2010 and 2011, respectively. While resurgent demand in parts of Europe and Asia—combined with stable and/or modestly rising commodity prices—should support a turnaround in the region's exports, the projected weak recovery for developed Europe will result in relatively muted overall export growth. Similarly, foreign direct investment—which correlates strongly with trade activity—and credit inflows are expected to remain significantly lower than the levels observed before the crisis.

Given the region's overleveraged private sector, weakness in the banking sector, and household indebtedness, the recovery in domestic demand is expected to be muted. Higher tax rates, cuts in public spending, higher unemployment, and lower wages will curb private consumption, which is projected to firm to 2.2 percent in 2010 and 3.3 percent in 2011—half the unsustainable 8.4 percent pace recorded in 2006–07. Excess capacity and crowding-out from increased government borrowing will constrain investment, which is projected to grow by 4.1 percent in 2010 and by 4.7 percent in 2011—well below the double-digit growth rates recorded in the pre-crisis years.

Because of weak domestic demand and relatively tight financial conditions, the regional current account balance is forecast to remain close to zero over the forecast horizon. Across the region, however, there is greater variety (table A4). For instance, hydrocarbon exporting economies are expected to record rising surpluses or reductions in deficits resulting from somewhat higher petroleum prices and increased production (Azerbaijan, Kazakhstan, Russia, Turkmenistan, and Uzbekistan). This improvement is projected to be offset by an expansion in the current account deficits—given a more rapid recovery in domestic demand leading to import volumes that exceed exports—in Moldova, Poland, Romania, Ukraine, and Turkey. For developing European countries with important automotive industries, sales are expected to decelerate as cash-for-clunkers programs in high-income European countries unwind.

Most countries have little room for further fiscal expansion. Indeed, government spending is projected to moderate as a result of planned structural fiscal consolidation. Combined with a projected firming of growth, which should support stronger revenues, fiscal consolidation is projected to progressively reduce the regional fiscal deficit from 6.2 percent of GDP in 2009 to 4.5 percent in 2010 and to 3.4 percent in 2011. However, the adjustment in an environment characterized by large negative output gaps and low growth will be difficult, particularly as the recovery in tax revenues may initially underperform, and that recovery will be exacerbated by additional pressure in the medium term emanating from extensive social assistance and pension regimes to support the aging population.

Monetary policy is expected to remain accommodative in most regional economies over much of the forecast horizon. Inflationary pressures should remain subdued, given large excess capacity, weak domestic demand, and a relatively open economy. In countries facing continued adjustment in demand to reduce external and internal imbalances, monetary policy is expected to remain relatively restrictive to help dampen activity. Monetary policy in countries with IMF programs will be guided by the framework defined by the ongoing Stand-by Arrangements. For those economies that are moving toward adoption of the euro, or whose currencies are pegged to the euro (Bosnia and Herzegovina, Bulgaria, Latvia, and Lithuania), monetary policy will be influenced by the European Central Bank's policy stance—which is expected to remain supportive of growth over the forecast horizon, but incrementally withdraw stimulus measures (including reversal of policy interest rate cuts) as demand conditions permit. A moderate uptick in median regional headline inflation is projected for 2010, as the downward pressure from the fall in oil prices in the second half of 2008 ceases and the recent uptick in commodity prices starts to work through the system. These pressures should be partly neutralized by the strong appreciation in currencies since March 2009 (particularly the Russian ruble and the Turkish lira), which will help to reduce import costs. However, core inflation will continue to be subject to disinflationary

Table A4 Europe and Central Asia country forecasts
(annual percent change unless indicated otherwise)

	1995–2005[a]	2006	2007	2008	2009[c]	2010[d]	2011[d]
Albania							
GDP at market prices (2005 US$)[b]	5.4	5.0	6.0	6.5	2.2	3.0	4.5
Current account balance/GDP (%)	−5.5	−5.9	−8.6	−13.4	−12.8	−7.6	−6.7
Armenia							
GDP at market prices (2005 US$)[b]	8.6	13.2	13.8	6.8	−13.0	1.5	3.5
Current account balance/GDP (%)	−11.7	−1.8	−2.6	−4.9	−2.8	−0.6	3.7
Azerbaijan							
GDP at market prices (2005 US$)[b]	10.2	34.5	25.0	10.8	3.1	5.2	8.5
Current account balance/GDP (%)	−16.6	17.7	28.5	37.6	19.5	27.2	26.2
Belarus							
GDP at market prices (2005 US$)[b]	6.9	10.0	8.6	10.0	−1.0	2.0	4.0
Current account balance/GDP (%)	−3.2	−4.0	−6.8	−8.4	−9.2	−6.3	−5.1
Bulgaria							
GDP at market prices (2005 US$)[b]	2.2	6.7	6.2	6.0	−6.5	−2.0	3.6
Current account balance/GDP (%)	−3.6	−18.4	−25.2	−25.4	−9.8	−5.2	−4.9
Georgia							
GDP at market prices (2005 US$)[b]	6.6	9.4	12.3	2.2	−4.0	2.0	3.5
Current account balance/GDP (%)	−10.0	−16.2	−16.9	−22.8	−18.2	−15.8	−16.7
Kazakhstan							
GDP at market prices (2005 US$)[b]	6.4	10.7	8.2	3.0	−1.9	1.8	3.5
Current account balance/GDP (%)	−2.3	−2.5	−7.0	9.5	−1.3	2.2	1.4
Kyrgyz Republic							
GDP at market prices (2005 US$)[b]	4.7	3.1	8.5	7.6	0.6	2.4	2.8
Current account balance/GDP (%)	−10.2	−10.6	0.6	4.6	5.2	2.4	4.9
Latvia							
GDP at market prices (2005 US$)[b]	6.9	12.2	10.3	−4.6	−17.5	−3.9	2.4
Current account balance/GDP (%)	−7.5	−22.7	−21.5	−11.3	5.3	6.0	7.0
Lithuania							
GDP at market prices (2005 US$)[b]	6.0	7.8	8.9	3.0	−17.5	−3.5	2.2
Current account balance/GDP (%)	−7.9	−10.7	−14.6	−16.1	0.5	0.3	−0.5
Macedonia, FYR							
GDP at market prices (2005 US$)[b]	2.2	4.0	5.9	5.0	−1.3	1.9	3.8
Current account balance/GDP (%)	−5.9	−0.5	−4.4	−12.5	−9.4	−8.3	−7.3
Moldova							
GDP at market prices (2005 US$)[b]	2.3	4.8	3.0	7.2	−9.0	1.4	2.8
Current account balance/GDP (%)	−7.9	−11.3	−16.5	−17.4	−9.0	−10.2	−11.1
Poland							
GDP at market prices (2005 US$)[b]	4.3	6.2	6.7	4.9	1.6	2.2	3.4
Current account balance/GDP (%)	−3.3	−2.7	−4.7	−5.5	−0.9	−2.6	−2.5
Romania							
GDP at market prices (2005 US$)[b]	2.2	7.9	6.2	7.1	−7.8	0.5	4.2
Current account balance/GDP (%)	−5.8	−10.4	−13.5	−12.4	−4.2	−4.9	−5.5
Russian Federation							
GDP at market prices (2005 US$)[b]	3.9	7.7	8.1	5.6	−8.7	3.2	3.0
Current account balance/GDP (%)	7.6	9.6	5.9	6.2	3.1	2.5	1.7
Tajikistan							
GDP at market prices (2005 US$)[b]	4.6	7.0	7.8	7.9	2.0	5.0	5.0
Current account balance/GDP (%)	−4.5	−2.8	−8.6	−7.9	−10.9	−11.1	−10.2
Turkey							
GDP at market prices (2005 US$)[b]	4.3	6.9	4.7	0.9	−5.8	3.3	4.2
Current account balance/GDP (%)	−1.5	−6.0	−6.1	−5.8	−1.9	−2.5	−2.8
Ukraine							
GDP at market prices (2005 US$)[b]	2.7	7.3	7.9	2.1	−15.0	2.2	3.0
Current account balance/GDP (%)	2.7	−1.5	−3.7	−7.2	−0.6	0.1	−2.1
Uzbekistan							
GDP at market prices (2005 US$)[b]	4.6	7.3	9.5	9.0	5.5	6.5	6.5
Current account balance/GDP (%)	3.3	14.4	19.5	26.3	16.9	20.4	19.2

Source: World Bank.

Note: World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not significantly differ at any given moment in time.

Bosnia and Herzegovina, Turkmenistan, and Yugoslavia, FR (Serbia/Montenegro) are not forecast owing to data limitations.

a. Growth rates over intervals are compound average; growth contributions, ratios, and the GDP deflator are averages.
b. GDP measured in constant 2005 U.S. dollars.
c. Estimate.
d. Forecast.

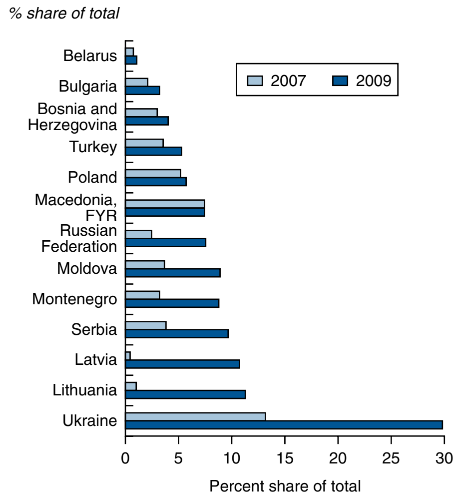
tendencies and headline inflation is expected to ease into 2011.

Risks

Despite the weak baseline forecasts for the region, risks remain tilted toward the downside, a result of financing constraints, the limited scope for supportive fiscal policy, large and rising banking sector vulnerabilities, and a lack of economic diversification. If the domestic recovery is slow and subdued with continued high interest rates stifling investment growth, potential output could suffer—leading to a rise in structural unemployment. A more protracted and deeper-than-projected recession could place further pressure on banking systems and on currencies in those countries with relatively inflexible exchange rate regimes. Balance-sheet consolidation by parent banks of foreign subsidiaries may manifest as further cuts in financial flows to the region in the months ahead. Rising domestic nonperforming loans and inadequate provisioning thereof pose significant risks to regional growth by restricting capital availability or, in a worst case scenario, leading to a freezing of banking systems (figure A11). This already somber scenario may be further darkened if it coincides with a global double-dip scenario, particularly if the region's major export markets (such as Germany) are severely affected.

A related and enduring risk for the region derives from the high level of household and corporate foreign-currency-denominated debt. Exposure to foreign exchange loans exceeds 50 percent of total lending in Hungary, Kazakhstan, Latvia, Lithuania, Romania, and Ukraine for both corporate and household borrowers. For households in particular, high levels of foreign exchange debt post significant risks, because unlike corporations, households are unlikely to have hedged against exchange rate movement.[10] For countries with relatively inflexible exchange rate regimes, outturns could find these regimes under assault, which in turn would limit the ability of regional central banks to conduct accommodative monetary policy.

Figure A11 Nonperforming loans rise across much of developing Europe and Central Asia



Sources: IMF Global Stability Report, October 2009; World Bank.

Note: Ranked by 2009 median for all reporting countries. Median was 2.7 percent for 2007; 4.4 percent for 2009.

Reinvigorating the reform programs that have stalled with the global crisis could help deliver stronger growth outturns than projected.[11] Regional governments have space to introduce institutional reforms to improve the regulatory framework and reduce red tape, tighten legal standards and further adopt international contract and property rights norms, and clamp down on corruption to improve competition and efficiency, among other reforms. Failure to reform the pension systems poses a long-term threat to growth, given high social security financing burdens. Successful implementation of these reforms may lower precautionary savings, with positive spin-offs for private consumption and growth. Higher private consumption in the region is indeed identified as a possible upside risk and incorporated in the global "more buoyant private-sector reaction" scenario (see chapter 1).

Finally, given the degree of dislocation engendered by the crisis, black market activity is expected to rise, posing challenges for policy makers and undermining greater fiscal consolidation. In the Commonwealth of Independent States, a lack of economic diversification outside of mineral-export-led activities is a common structural weakness and remains a key vulnerability.

Latin America and the Caribbean

Recent developments

Thanks to sound macroeconomic fundamentals in place before the onset of the crisis, the Latin America and Caribbean region has been able to weather the global financial crisis much better than previous external shocks. Nevertheless, economic activity in the region decelerated sharply in the aftermath of the crisis. For the 2009 calendar year, GDP is estimated to have fallen 2.6 percent, following an expansion of 3.9 percent in 2008 (table A5). This aggregate result masks a high degree of heterogeneity among countries in the region with respect to the timing and magnitude of the contraction in domestic output. Central American economies (including Mexico) were the worst affected, with output contracting a sharp 6.4 percent, while growth in the Caribbean economies stagnated.

In the immediate aftermath of the crisis, the region was hit by a sharp slowdown in private capital inflows, while increased uncertainty and credit tightening led to a marked contraction in private consumption and private investment. The capital outflows induced a sharp depreciation of currencies in the region, a decline in equity markets, and much higher borrowing costs. Nevertheless, the region managed to avoid falling into a balance of payments and/or financial crisis.

Private consumption contracted by nearly 2 percent, while fixed investment declined sharply by 13.6 percent, after growing at double-digit rates in the previous years. The region was also affected by the collapse in external demand for commodity exports, falling

Table A5 Latin America and the Caribbean forecast summary
(annual percent change unless indicated otherwise)

	1995–2005[a]	2006	2007	2008	2009[e]	2010[f]	2011[f]
GDP at market prices (2005 US$)[b]	2.9	5.4	5.5	3.9	−2.6	3.1	3.6
GDP per capita (units in US$)	1.4	4.0	4.1	2.6	−3.8	1.8	2.3
PPP GDP[c]	2.9	5.5	5.7	4.2	−2.3	3.0	3.5
Private consumption	3.4	6.1	3.5	4.2	−1.9	3.2	3.4
Public consumption	2.2	2.8	2.9	4.1	2.9	2.8	2.6
Fixed investment	3.3	13.4	20.7	11.7	−13.6	6.1	5.8
Exports, GNFS[d]	6.0	6.7	4.9	1.6	−11.2	7.8	5.0
Imports, GNFS[d]	6.2	14.0	11.9	9.2	−15.8	10.3	5.6
Net exports, contribution to growth	0.2	−1.5	−1.7	−2.0	1.6	−0.7	−0.3
Current account balance/GDP (%)	−1.6	1.4	0.4	−0.6	−0.9	−1.0	−1.0
GDP deflator (median, LCU)	7.1	7.2	5.4	8.4	7.2	3.0	4.0
Fiscal balance/GDP (%)	−3.5	−1.1	−1.1	−0.9	−3.3	−2.8	−2.5
Memo items: GDP							
Latin America excluding Argentina	3.0	5.2	5.2	3.7	−2.6	3.2	3.7
Central America	3.6	5.0	3.7	1.7	−6.4	3.3	3.6
Caribbean	4.2	9.0	6.1	3.6	−0.1	2.3	3.3
Brazil	2.4	4.0	5.7	5.1	0.1	3.6	3.9
Mexico	3.6	4.8	3.3	1.4	−7.1	3.5	3.6
Argentina	2.3	8.5	8.7	6.8	−2.2	2.3	2.4

Source: World Bank.

a. Growth rates over intervals are compound average; growth contributions, ratios, and the GDP deflator are averages.
b. GDP measured in constant 2005 U.S. dollars.
c. GDP measured at PPP exchange rates.
d. Exports and imports of goods and nonfactor services.
e. Estimate.
f. Forecast.