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PACIFIC ECONOMIC OUTLOOK 1995-1996

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PECC Pacific Economic Outlook, 1995-1996

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Founded in 1980, PECC now comprises 21 Member Committees representing the economies of Australia, Brunei, Canada, Chile, China, Colombia, Hong Kong, Indonesia, Japan, Korea, Malaysia, Mexico, New Zealand, Peru, The Philippines, Russia, Singapore, Chinese Taipei, Thailand, the United States, and the Pacific Island Nations, and associate member Vietnam. Each committee sends a tripartite delegation to the PECC General Meeting approximately every 18 months. In the interim, policy matters are handled by a Standing Committee, and day-to-day administrative and coordinating functions are carried out by a Secretariat based in Singapore.

In addition, PECC establishes task forces, fora, and working groups to concentrate on particular policy areas. These groups meet periodically, organize seminars and workshops, conduct studies, and publish their conclusions and recommendations for the benefit of the Pacific Community. Currently, task forces are in operation in the areas of Food Policy; Trade and Development; Fisheries Development and Cooperation; Human Resource Development; Pacific Island Nations; Science and Technology; and Transportation, Telecommunications and Tourism. PECC also has a Trade Policy Forum, a Minerals and Energy Forum, and a Pacific Economic Outlook Project.

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PACIFIC ECONOMIC OUTLOOK 1995-1996

BACKGROUND

This report presents the seventh annual Pacific Economic Outlook (PEO). During this time, the PEO has earned a reputation for the accuracy of its predictions of real economic growth in the vast and diverse Pacific region. The first six forecasts have come within a half percentage point of actual growth. This record of accuracy — and the economic understanding that makes it possible — reflects the work of economic forecasters from each of the economies whose data are presented here. Pages 74 and 75 of this report list the names of these forecasters.

This excellent example of pacific economic cooperation began when the Pacific Economic Cooperation Council (PECC) resolved at its Sixth General Meeting, in Osaka in 1988, that an annual forecast for the Pacific Basin be prepared. It assigned the task to the U.S. National Committee and instructed it to work in close cooperation with the Japan National Committee.

That cooperation has been highly productive. The Japan Committee prepares a counterpart document, analyzing longer-term structural issues. For its part, the U.S. Committee prepares this two-year forecast. Under the overall coordination of Professor Lawrence Krause of the University of California, San Diego, leading forecasters from the economies prepare outlooks for the individual economies. Twice during the forecast period they meet as a group to analyze the data and to inform and guide the summary statement written by Professor Krause.

Although the PEO is most often cited for its GDP and price and trade predictions, it has also become a valuable resource on the key elements shaping the economies of the region. The PEO is formally presented to the plenary meetings of the PECC as well as the Ministerial meetings of the Asia Pacific Economic Cooperation (APEC) forum of government officials. Readership surveys reveal that the PEO is now widely used by those in business, academia, and government.

The Asia Foundation's Center for Asian Pacific Affairs (CAPA) is the main sponsor of the Pacific Economic Outlook forecast project. Professor Earl F. Cheit directs The Asia Foundation's work on this project, and Gavin Tritt, Program Officer in CAPA, is the project's manager. The Japan Committee for the Pacific Economic Outlook also supported this year's forecast by hosting a meeting of the forecasters.

SUMMARY

With this forecasting cycle, Vietnam becomes the latest member of the Pacific Economic Outlook (PEO). This is most appropriate in view of Vietnam's impending entry into ASEAN.

ECONOMIC GROWTH SPURTS IN 1994

The economic performance of the Pacific region during 1994 was nothing short of sensational. The weighted average growth rate for the region was 4.7 percent, a full one percent above that achieved in 1993. If we exclude the United States and Japan from the calculation, a remarkable 7 percent rate of growth was recorded. This rivals the extraordinary performance of 1988, and like 1988 may turn out to have been a cyclical peak.

With one exception, every country in the PEO grew faster in 1994 than was forecast one year ago. Our margin of error was 0.5 percent, the greatest miss in our seven year history. Nevertheless, we did get the direction of change correct — we properly forecast an acceleration of growth. In every year we have gotten the direction of change correct, which is of utmost importance. Forecasters just could not believe that the region could grow as fast as it did. The sole exception was Japan, which grew slightly less than forecast. Last year our forecast for Japan was criticized as being too pessimistic. Unfortunately it was not.

The inflation experience in the region was excellent despite the high rate of real growth. The weighted average CPI inflation rate for the region in 1994 was 3.9 percent which was almost the same as for 1993. We had forecast a unique historical event — declining inflation with accelerating growth — which did not occur. Our error was in underestimating real growth, which had the consequence of sustaining inflation. Gains in productivity which were expected to bring lower prices were offset by price increases of raw materials (other than petroleum) which were not fully forecast.

FACTORS PROMOTING GROWTH

By far the most important factor stimulating the economies in the region has been domestic investment. Private business investment has been most evident in Australia, Canada, Colombia, Korea, New Zealand, Singapore, and the United States. In China, Indonesia and Thailand, domestic business investment has been facilitated by significant increases in foreign direct investment. Public utility and infra-structure investment has been particularly strong in Hong Kong and Vietnam. And in Malaysia, the Philippines and Chinese Taipei, investment has been combined with a large rise in domestic consumption.

This is not to suggest that international trade is no longer important for the region. To the contrary, trade remains a strategic factor and is often the catalyst for business investment. In addition, in Canada, Chile, and Singapore growth of export volume was particularly strong and without question was a leading factor in the rise of their GDP in 1994. While export growth was greater than output growth for almost all countries in the region, the growth of import volume was equal or greater than exports. This means that net exports were not a contributor to growth in an accounting sense, but were very important in improving efficiency and productivity, which is the factor promoting growth in per capita income.

THE 1995-96 OUTLOOK

The outlook for the region is for expanding real economic growth as far as the eye can see, but at a moderating pace. With the notable exception of Mexico, no country expects to suffer a recession through the end of 1996. The weighted average rate of growth is forecast to be 4.1 percent in 1995 and 4 percent in 1996. This pattern of moderating growth is seen in fully ten of the nineteen individual forecasts. Only three countries are expecting an acceleration of growth — Chile, Japan, and the Philippines (possibly joined by Chinese Taipei and Vietnam). The story that these numbers are portraying is one of a soft landing for the region as a whole. Achieving a soft landing in 1995-96 would be just as remarkable as the spurt of growth experienced in 1994.

Just like the period immediately following the previous growth peak in 1988, the slowing expected in 1995-96 is self-induced rather than dictated by forces external to the region. The slowing can be attributed to the pre-emptive tightening of monetary policy by the monetary authorities in the region, led by the Federal Reserve of the United States. The Fed was responding to a number of signals implying an impending resurgence of inflation, which included the 28.7 percent actual rise in the weighted index of the prices of 33 commodities (excluding energy) measured in U.S. dollars from December 1993 to December 1994. Over a thirteen month interval, the Fed raised short term interest rates seven times, from 3 percent to 6 percent. Short term interest rates rose as well in many other countries, both because monetary authorities shared the concerns of the Fed and because market forces pushed up rates through international capital movements. Since there is always a delay between when money is tightened by the authorities and it has an impact on real economic activity, the policy actions of 1994 are expected to slow economic activity in 1995 and into 1996.

WHY IS INFLATION SO MODERATE?

Our numbers show that very little if any actual inflation appeared in 1994, and our forecast is for only a moderate rise to 4.6 percent in 1995 followed by a drop back to 4.1 percent in 1996. No doubt the containment of inflation that is forecast can be considered a consequence of the pre-emptive exercise of monetary policy. Nevertheless, there is a question of why more of the sharp rise in raw material prices in 1994 did not get passed along into higher prices for consumers.

A number of factors seem to be responsible. First of all, there seems to have been considerable spare industrial capacity at the start of 1994, which reflects the rather moderate pace of economic expansion from the previous downturn of 1990-91. When an economic recovery is moderate, is led by business investment, and is elongated in time, it permits new capacity to come on line in time to meet an expansion of demand without igniting inflationary fires. Second, international trade continues to be liberalized. While few of the measures agreed to in the Uruguay Round are effective as yet, they are being anticipated and are leading to adjustments within business firms as if they were already in place. Furthermore, regional efforts at trade liberalization such as AFTA and NAFTA have been reducing trade barriers. This added competition contains inflation. Finally, and in a similar vein, there are simply more countries competing for world markets. Former raw material producing countries such as Thailand and Malaysia have become major exporters of manufactured goods. Former NICs such as Korea and Chinese Taipei have moved upscale and are now competing in markets for high tech goods. Moreover, China is now heavily involved in international trade and because of its size is making a huge impact in markets for labor-intensive goods. All of this suggests that it will be harder for business firms to put up prices and make them stick than it has been in the past.

INFLATION CONCERNS REMAIN

While inflation has been contained for the region as a whole, it remains the most serious problem for a large number of economies. China continues to be plagued by inflation and in 1994 suffered its highest rate in sixteen years. This is understandable after three years of double digit growth of real output, but it is very disturbing and cannot be sustained. Monetary policy has gone through several cycles in which tightening leads to a shortage of credit for state enterprises, and when the pressure becomes severe, the policy is relaxed. Policy was tightened again in June 1994 and inflation seems to be ebbing along with a rise of unemployment and stagnation of output in some sectors. Inflation will remain a problem in China as long as the core of the old industrial system remains with state enterprises not being subject to a hard budget constraint.

Inflation in Colombia remained a disappointing 22.6 percent in 1994, missing even the modest improvement targeted by the government. Interest rates were kept too low for too long into 1994. Given the progress that is being made in the Colombian economy, it would be most appropriate for inflation fighting to become a higher priority goal than it has been in the past. The situation in Hong Kong is different in that it imports goods-inflation from China and has its monetary policy set in the United States. However, Hong Kong suffers from a high rate of structural inflation which in time can undermine its competitiveness as a service center.

In order to stimulate output, Indonesia lowered interest rates in 1993 and into 1994. Output did expand substantially, but so did inflation, which reached double digits. After mid-year 1994, interest rates were increased, but large inflows of foreign capital complicated the task of reducing the supply of credit. The monetary authorities are continuing to respond, but inflation momentum in Indonesia is difficult to reverse. The situation in the Philippines is somewhat similar in that the acceleration of growth in 1994 led to a significant rise of inflation. While inflation is expected to moderate in 1995-96, that may not occur if economic growth continues to accelerate.

The inflation experience of Vietnam has been highly variable and is of a rather special character since it is greatly impacted by domestic food prices, which are subject to the vagaries of nature. Indeed, the growth of the economy has been much more stable than inflation (whether measured by the CPI or the GDP deflator). This variability of inflation is expected to continue for some time with occasional double-digit rates.

THE BALANCE OF PAYMENTS PICTURE

The current account of the balance of payments for the Pacific region as a whole (measured on a comparable basis) recorded a sharply increasing deficit in 1994 as compared to 1993 entirely because of the deterioration in the United States. The surplus of Japan in 1994 (measured in U.S. dollars) was slightly reduced as compared to 1993, indicating that much more of the financing of the U.S. deficit must have come from other countries. This same trend, in a much attenuated fashion, is forecast for the U.S. and Japan for 1995. By 1996, the U.S. deficit is expected to decline and the surplus of Japan to increase (again measured in U.S. dollars). For the region as a whole, the deficit is forecast to be reduced in 1995, with Mexico playing a central role, and remain about the same in 1996.

The balance of payments position of several countries must be considered as problematic. Australia's imports have grown significantly more than exports in 1994 and the same is forecast for 1995. This has led to a current account deficit equal to about 5 percent of GDP. While Australia has not had difficulty financing the deficit with commodity prices rising, the situation could be quite different when the inevitable decline of these prices occurs. For Canada the situation is almost the reverse. While high, the current account deficit as a share of GDP has been declining to about 3 percent, but Canada has had difficulty in attracting sufficient capital and the Canadian dollar has been depreciating. While political uncertainties surrounding Quebec may be playing a role, the more direct factor has been rising short-term interest rates in the United States, which have forced Canada to match or even top them in order to help finance its high public sector debt. In this regard, the recent federal budget, by significantly reducing current spending levels, should be a positive development. Nevertheless, a problem might develop if the monetary policy forced upon Canada turns out not to be responsive to the needs of the domestic economy.

There are several developing countries, including Colombia, Indonesia, Malaysia, Peru, the Philippines, Thailand, and Vietnam whose current account deficits are high relative to GDP and may even be rising, but where the balance of payments need not be a problem. It is most appropriate for this situation to occur in the process of economic development, but only if the foreign borrowing leads to increases in domestic investment, and investment of the kind that in time will yield a stream of earnings that can service the foreign debt. This seems to be the case for these countries, but the situation must be reviewed regularly.

THE RECESSION WATCH

Historically, recoveries always end in recessions. For the United States, the average length of recoveries since World War II has been 50 months, and this recovery has already passed that anniversary. Slow and hesitant recoveries such as the one in place in Japan can be interrupted and lead to a double-dip recession. What are the prospects of a recession in either the United States or Japan during 1995-96?

The case for a recession in the United States rests on either a belief that a virulent inflation is about to break out, or that the Federal Reserve will make a serious error in monetary policy. Under both scenarios, the Fed raises short term interest rates to such a high level that a recession becomes inevitable. The countering case embedded in our forecast rests on the belief that the economy is already slowing, which will contain inflation, and that demand for business investment is so strong that it can withstand even a bit more of an increase in short-term interest rates. Furthermore, consumers are likely to continue to spend out of rising disposable income, which will sustain the recovery even if they reduce expenditures on interest-sensitive items such as autos and houses. Finally, U.S. export growth should be sustained or even accelerate with a depreciated dollar and with economies abroad doing reasonably well.

While a soft landing for the American economy is most likely, one can still quarrel with U.S. macro policy. There is no fundamental reason why the economy should be put at risk from higher interest rates. If the budget deficit of the Federal Government, which under current law is expected to stabilize at about $160 billion in 1995-96, was instead headed in a downward direction through more stringent fiscal policy, then the Fed would surely respond by letting the private sector expand to make up the difference. Clearly it is during an extended recovery that the budget should be brought into balance, and that has not yet been faced up to.

The long recession in Japan that was connected to the collapse of the financial bubble is considered to have ended about October 1993. Nevertheless, the recovery has been far from robust. Real growth in 1994 was less than 1 percent and only a minimal rise is forecast for 1995, although stronger growth is expected in 1996. The case for a double-dip recession rests on the belief that even the meager growth achieved in 1994 was due to special factors such as the hot summer and the first traunche of the tax cut, which will abate (or add no further stimulus), and that 1995 faces additional difficulties due the further appreciation of the yen, and because of the undermining of consumer confidence arising from the Kobe earthquake.

Nevertheless, our forecast of continued modest growth is well documented. The inventory overhang that has depressed the economy has been corrected. Business fixed investment will no longer be a drag on the economy and will contribute a modest amount to growth, and consumption will be sustained through the tax cut. All of this is underpinned by record low nominal interest rates and should easily overcome the negative consequence of imports rising more than exports.

HOW MANY ENGINES ARE REQUIRED AND WHAT IS AN ENGINE ANYWAY?

Last year China was recognized as an engine of growth that took its place along with Japan and the United States as an economic leader of the Pacific region. This has raised an important question: what is an engine of growth? As a pragmatic working definition, a country can be considered an engine if most of its economic stimulus comes from internal forces, but because of its economic size has a huge impact on its trading and investing partners. These three countries fit this definition. Is it not possible, however, for a group of smaller, closely-integrated countries collectively to fit the definition? This is certainly a possibility, and if the ASEAN countries, for example, are able to sustain economic progress while the engines are in retreat, then the case will clearly be made.

The current situation will only be a partial test of this proposition. China and the United States are forecast to be slowing, and Japan expects only a modest rise. This should imply slowing throughout the region. Japan, however, may provide more stimulus than its small growth of GDP implies because its imports will react to the appreciated yen, and its business firms may step up their direct investments in the region. Because of this, more than usual attention will be addressed to the forecast of accelerating growth in the Philippines, Thailand, and possibly other countries.

THE STAR PERFORMERS

Almost all countries in the region have recently exhibited outstanding economic performance, but some have done exceptionally well: Chile, Malaysia, and New Zealand in particular. Chile has managed a gradual deceleration of inflation without sacrificing significant amounts of economic growth while maintaining a sustainable balance-of-payments position. The fact that this was achieved while raw material prices were rising is testament to skill in policy management. Malaysia has added yet another to its string of eight consecutive years of rapid growth without inflation. Malaysia has been challenged by huge capital inflows, but has managed to deflect or neutralize them in imaginative ways. While much was experimental and might not be repeatable, its prompt attention to the disturbance is highly commendable. New Zealand has managed several years of above-trend growth without rekindling inflation. It now appears to be benefiting from the series of drastic economic reforms instituted over the last decade, and proving that policy credibility can be sustained even with changes in government leadership.

Four obvious lessons can be drawn from the experiences of these countries. First, economic reforms that encourage markets are the basis for economic prosperity. Second, an outward orientation of policy is essential for small- or medium-sized countries. Third, monetary policy must be recognized as having the critical role for achieving stabilization goals. Finally, government intervention is necessary to manage international capital flows, especially of private portfolio and short-term capital. When capital markets do not have breadth, depth, and resiliency — and they rarely do in developing countries — and freeing of international capital movements is of recent vintage, then governments must act to safeguard the interests of society by countering monetary shocks emanating from abroad.

MEXICO: AN ECONOMY IN TROUBLE

The economic troubles of Mexico escalated into a full blown financial crisis in December 1994 which will take some time to fully contain. The Mexican experience demonstrates that a country may implement many correct policies, but if it emphasizes one goal to the exclusion of others then it is asking for trouble. With hindsight, Mexico can be faulted for trying to tame inflation more quickly than was feasible. The monetary authorities chose to emphasize a stable nominal exchange rate as the monetary anchor to achieve price stability. The problem with that approach (as demonstrated by Chile previously) is that it can translate into an appreciating real exchange rate. While Mexico was prepared to let the peso depreciate in nominal terms to offset its inflation differential with the United States, it did not force that correction. Starting in 1992, if not before, inflows of capital kept the nominal exchange rate stable despite some reserve accumulation by the monetary authorities. This led to growing overvaluation of the peso in real terms. Again, with hindsight it would have been better if even more dollars had been bought to maintain stability in the real exchange rate. Of course inflation would have decelerated at a slower pace, but the current account would not have deteriorated to the extent that it did, and more real growth might have occurred earlier in the 1990s. The growing over-valuation of the peso, combined with the three political shocks of 1994, undermined confidence in the market that the nominal peso exchange rate could be held and massive speculation against the peso followed thereafter.

In response to the crisis, the Mexican monetary authorities have shifted strategy and are now focusing on domestic credit as the monetary anchor while letting the peso float in the foreign exchange market. The task is to bring the exchange rate, the price level and the wage level back onto a sustainable path in relation to one another. That is to say, the authorities on the one hand do not want to permit the inevitable resurgence of inflation to undermine the necessary improvement in Mexico's competitive position engendered by the depreciation of the peso, but on the other hand they do not want to create a greater short run contraction of economic activity than the country can endure. A more or less conventional package of policies have been introduced to accomplish this.

The peso exchange rate must be guided by the market, but not left to the market. Once reasonable stability has been obtained, the monetary authorities should ensure that the real value of the peso is not distorted again. All of this is made more difficult because the crisis itself impacts greatly on the fiscal position of the government — economic contraction reduces receipts and higher interest rates increase payments — which is a reminder to all countries of the dangers of a large public debt in relation to GDP.

The Mexican crisis has had an impact on both sides of the Pacific. It has contributed to the shrinkage of equity values in all so-called emerging markets. Following the depreciation of the peso, the currencies of several developing countries have been questioned by investors and speculators, which has required some countering actions by governments. The value of the U.S. dollar has also declined relative to other major currencies, reflecting the fact that Mexico is a much more important trading partner of the United States than it is of other countries. This points up the lesson that interdependence means just that, and that both desirable as well as undesirable shocks are transmitted in all directions.

RISKS IN THE FORECAST

Three risks in our forecast have been identified: that monetary policy may be made too tight, that exchange markets may over-shoot, and that a real capital shortage might develop. Our benign forecast could be shaken if any or several of these risks should materialize. First, making monetary policy is not an exact science. If the Fed, the Bundesbank in Germany, and the Ministry of Finance in Japan were all to err on the side of excessive monetary stringency, then a general liquidity shortage could develop which would lead to a credit implosion scenario. The result would be that the soft landing would be converted into a recession.

The second risk is that currency markets under pressure from short term speculative capital movements could lead to extreme values of exchange rates. Under a flexible exchange rate regime, exchange rates from time to time can overshoot and become unrelated to fundamental values. If this should persist for a lengthy period, then real distortions can occur. The Japanese yen-U.S. dollar rate is the one that if distorted can cause serious disruption in the Pacific region. If the yen appreciates excessively, then real growth in Japan in the short run can be undermined and cause another recession. An undervalued dollar would add to inflation in the United States and would also mis-direct investment which in time would also reduce growth. Since many currencies in the Pacific region are linked to the dollar or yen, the potential distortion created thereby would be felt widely.

Finally, the risk of a real capital shortage emerging has been recognized previously, but has not been put to rest. Investors in Japan may be making less savings available to the rest of the world without the United States offsetting them. If the need for capital from abroad in the aggregate is rising — and that case has not been made convincingly — then a real capital shortage could develop. If it did, then real interest rates would rise, which would add to the burden of indebted countries (including the United States) and slow real growth.

THE NON-CRISES

We always focus on dangers and rarely stop to count our blessings. It is probably worth a bit of space to examine the "dogs that are not barking." First, we were warned by the supporters of the bicycle theory that the end of the Uruguay Round would be greeted with a new burst of protectionism (unless a new negotiation was to start immediately). This has not happened. By historic standards, trade relations among countries are remarkably benign because self-restraint is being shown by all countries. Clearly, progress in APEC is promoting this in the Pacific, but it is also true that individual countries are giving attention to disputes that are present and are attempting to reach solutions in good faith.

Second, despite some very severe pressures along the way, market reform policies are not being reversed in places such as China, Vietnam, Korea, or Peru. While the pace of reform may be slowed or not attempted vigorously enough, once announced reform policies are rarely reversed. It appears that the goal of market reform will no longer be seriously contested.

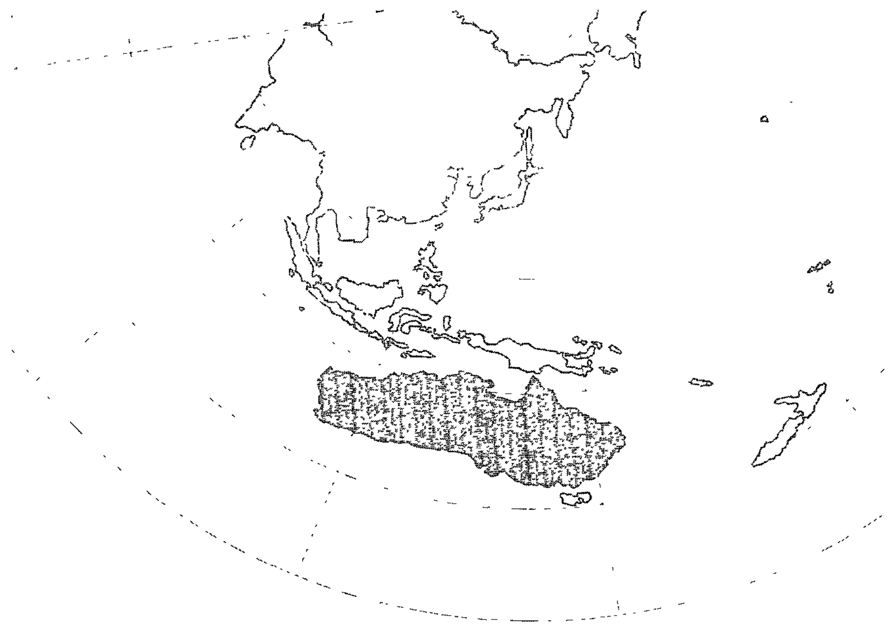
Finally, the Pacific region is blessed by an absence of serious military conflict. While there are danger spots, there is no Bosnia in the region. There is even hope that North Korea might be induced to peacefully engage with the rest of the region.

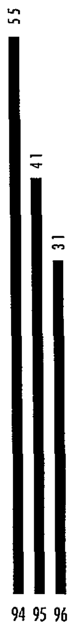
CONCLUSIONS

The Pacific region is expected to effectuate a soft landing in 1995-96 after experiencing a remarkably large spurt of real growth in 1994. The fact that countries recognize that 1994 cannot be replicated in 1995-96, and have already adopted policies to moderate growth, is a very good omen that a soft landing can be accomplished.

Recent experience, however, also points up some challenges that have not been fully comprehended, nor have government policy responses been designed to deal adequately with them. Three things are happening simultaneously which require some analysis: international capital markets are being freed, domestic capital market regulations are being relaxed or lifted, and governments are privatizing state owned enterprises (SOEs) in part by selling them abroad. The threefold challenge that this presents is to have in place effective prudential controls that force both financial and non-financial firms to recognize the unfamiliar risks which their new freedom permits them to assume. Second, that governments recognize that when private portfolio managers gain the benefits of diversification by investing in a newly opened market, they may increase investment into a country at a temporary rate that is much higher than the steady state once portfolio balance is achieved. The task is to estimate the sustainable level of portfolio inflows, and not let the temporary bulge upset domestic monetary stability. Finally, selling off SOEs gives the government a one time increase in revenues. If foreign buyers are involved, then a temporary increase in foreign exchange also results. Again, the challenge is to not let these temporary disturbances affect domestic monetary stability. Governments invariably get into trouble if they fight market trends, but they will also err if they do not recognize that markets at times can be very myopic and need a government-determined frame within which to operate.

AUSTRALIA





REAL GDP/GNP

1994 – STRONG GROWTH WITH LITTLE EFFECT ON INFLATION

Nineteen Ninety-four has been a year of strong economic growth, low inflation and falling unemployment. Strong economic growth has led to a surge in imports and to a deterioration in the balance on the current account. Based on preliminary data for the first three quarters and our estimates for the fourth quarter, real GDP is likely to increase by 5.5 percent in 1994, compared with a rise of 3.7 percent in 1993. This will be the third consecutive year of expansion after the 1990/1991 recession. In 1994, the fastest growing elements of real domestic absorption are expected to be private consumption and private investment expenditure. Consumption expenditure is likely to increase 4.6 percent, with real household disposable income (HDI) likely to rise by about five percent. Growth in real HDI in 1994 was assisted by strong employment growth.

Real private fixed investment is expected to grow by almost 16 percent in 1994, following a 4.9 percent rise in 1993. Within the private investment aggregate, we expect real expenditure increases of 26.6 percent on equipment, 10.4 percent on dwellings, and 5.9 percent on non-dwelling construction. The very strong growth in business investment (about 19 percent) is noteworthy. Real non-dwelling construction had fallen almost continuously from the first quarter of 1990 to early 1994, and equipment expenditure had recovered only marginally. The turnaround in 1994 signals that the excess office space created in the boom building period of the late 1980s has been largely eliminated and that spare industrial capacity has shrunk. Nevertheless, business investment as a share of GDP in 1994 is still low compared with the share in the late 1980s.

Strong growth in real GDP is now being reflected in the labor market. The seasonally-adjusted unemployment rate has fallen to below 9 percent from its peak of 11.4 percent in November 1992. However, the average duration of unemployment is more than 60 weeks and has not yet declined significantly (cf. 53.5 weeks at the end of 1992).

Since March, Australia's current account deficit has been on an upward trend. Import volumes have grown relative to export volumes and this has been offset only partly by improvements in the terms of trade. The major contributor to import growth has been capital goods, with imports rising by over 50 percent in value since the start of the year. The recent subdued performance of exports reflects two main factors: drought, which has seriously cut exports of cereal grains, and real appreciation of the Australian dollar. The dollar rose by 10 percent through 1994, while domestic inflation remained in line with rates overseas. In the short term, the value of Australia's currency is driven principally by world commodity prices and short-term interest rate differentials. The recent appreciation can be attributed mainly to rises in world commodity prices. Nominal short-term interest rates have been increasing, but the increases have been in line with increases in overseas rates.

The nominal appreciation of the currency during 1994 has helped maintain a low rate of consumer-price inflation. The CPI increased by 1.9 percent in 1994, following increases of 1.8 and one percent in 1993 and 1992. Since early 1990, underlying inflation in Australia has averaged little more than two percent. This has been achieved mainly through a combination of wage restraint, tight control over demand administered by the Reserve Bank via interest rates, and structural changes brought about by reforms to public trading enterprises and the opening of Australian industry to greater international competition.

CPI

GROWTH CONTINUES IN 1995, BUT INFLATION AND EXTERNAL-ACCOUNT PROBLEMS SURFACE

Our forecasts suggest that growth in the Australian economy has peaked. Real GDP is forecast to rise by 4.1 percent in 1995, with private consumption up 4.4 percent and private investment 10.8 percent. All of the growth in private investment is expected to come from business investment (non-dwelling construction is forecast to rise 10.1 percent and equipment investment 21.5 percent). Housing industry indicators show that construction growth has started to decline. This reflects, in part, interest rates increases in the second half of 1994. In 1995, we expect a 1.5 percent decline in real dwelling investment.

Strong growth in the import-intensive components of domestic demand in 1995 will continue to place upward pressure on the demand for imports. We are forecasting import volumes will increase by 16.4 percent in 1995. This is not expected to be matched by growth in export volumes, leading to an increase in the current account deficit both in US dollars and as a percent of GDP.

CPI-inflation is expected to rise from 1.9 percent in 1994 to around 3.5 percent in 1995. This is still a moderate outcome given the underlying demand pressures. The greatest risk to inflation is a breakout in wages growth. However, we think that this is unlikely in 1995, as unemployment is expected to remain quite high (i.e., above 8.5 percent).

For 1996, we are forecasting a further fall in real GDP growth to 3.1 percent, an improvement in the current account deficit to 4.8 percent of GDP, and an increase in CPI-inflation to 4.5 percent. The major risk to our 1996 forecasts is the government's ability to manage the labor market. To keep inflation low (say, below 4.5 percent) and unemployment falling, growth in real wages must be restrained. If this does not occur, the government and reserve bank have only one option —high interest rates. This will mean, relative to our current forecasts for 1996, sharply lower growth, higher unemployment and a stronger Australian dollar.

CANADA

REAL GDP/GNP

ANOTHER YEAR OF SOLID PERFORMANCE IN CANADA

There is enough momentum in the Canadian economy to ensure a solid year of growth during 1995 under reasonable economic assumptions. Output is expected to rise 3.7 percent, while growth is forecast to moderate to 3 percent in 1996. However, the shape of Canada's economic dynamics are, to an increasing extent, being determined by external events. The most important pressure comes from a U.S. economy that refuses to slow to sustainable rates of growth despite interest rate increases over the past year.

Canadian interest rates are now expected to be much higher than was projected a year ago. Although the recent federal budget met with the approval of financial markets, the difficult Canadian political climate as the Quebec sovereignty referendum approaches will make it hard for the Bank of Canada to resist further interest rate increases in the U.S.

MONETARY POLICY

The Bank of Canada has attempted to pursue an expansionary monetary policy given relatively weak domestic demand and no immediate inflation threat. However, policy has become more restrictive recently. The devaluation of the peso caused a retreat of investors to more secure economies; selling pressure on the U.S. dollar has exerted further pressure on the Canadian currency; and continued domestic concerns have forced the bank not only to match recent U.S. short term rate increases, but to exceed them.

The Canada-U.S. short-term interest rate spread has widened by about 100 basis points since last November, and is currently at 240 basis points. However, under the assumption that the referendum is defeated, the spread is forecast to be reduced in the neighborhood of 100 basis points by the first quarter of 1996. Nonetheless, given further hikes in U.S. interest rates, by the second quarter of 1996 Canadian three-month treasury bills will average 8.6 percent, about 450 basis points above the lows achieved early in 1994. Throughout the 1995-96 period, the Canadian dollar is forecast to trade between US$0.71 and US$0.73, receiving a boost in 1996 from the failure of the Quebec referendum on sovereignty.

FEDERAL FISCAL POLICY

The fiscal plan tabled in February laid out a framework that will enable the federal government to achieve its deficit target of 3 percent of nominal GDP by fiscal 1996/97. In fiscal 1994/95, the share will be about 5.1 percent, down from about 5.8 percent in the previous two fiscal years.

Significant expenditure cuts were the centerpiece of the austerity budget. Subsidies and capital assistance to business will be sharply reduced, as the government seeks to withdraw from non-essential enterprises. However, by far the largest cost savings will be realized in lower transfers to regional governments. By moving to a system of block funding, the federal government has decoupled itself from the more cyclical elements of regional funding, offering more fiscal autonomy to the provinces in return. Reductions in total cash transfers to the regions will save $2.5 billion by 1996.

One of the key risks to achieving fiscal stability is the response of the regional governments to this package. The current forecast assumes that dollar-for-dollar spending restraint will ensue. This is a likely outcome, given the current success and popularity of fiscal tightness at the provincial level.

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AGGREGATE DEMAND

The outlook for consumer spending over the short term is fair, with real growth at 2.8 percent in 1995 and 2.5 percent in 1996. This growth is generated mainly by improved employment and also by a pick-up in real private sector wages, especially in 1996.

The disposable income created by employment growth should be adequate to sustain consumer spending over the near term. The impact of high interest rates is especially evident in the current housing outlook, which projects a slight decline in housing starts in 1995. Although demographic data suggest that a growing shortage of housing should be emerging, neither the vacancy rates, housing prices nor the resale market give any indication that this is the case. Overall, housing starts are forecast to average 152,000 units in 1995, about 2,000 lower than in 1994.

Energy investment is expected to decline by 2.6 percent in 1996, which is largely attributable to the winding down of the Hibernia project. In addition, we expect total drilling activity to fall through 1995, owing largely to excess supplies of natural gas.

The situation is much brighter for non-energy, non-residential construction investment, with growth expected to average roughly 5.5 percent annually over the 1994-96 period after four years of declines totaling 50 percent. Growth will be concentrated in industrial building and the retail sector, while high vacancy rates should prevent a recovery in commercial office building activity.

Growth in non-energy machinery and equipment investment will slow to about 7.9 percent through 1996, after increasing 10.7 percent in 1994. Higher interest rates, completion of the modernization process in many manufacturing industries, and slower U.S. growth are the major factors expected to cause this slow growth in new equipment spending.

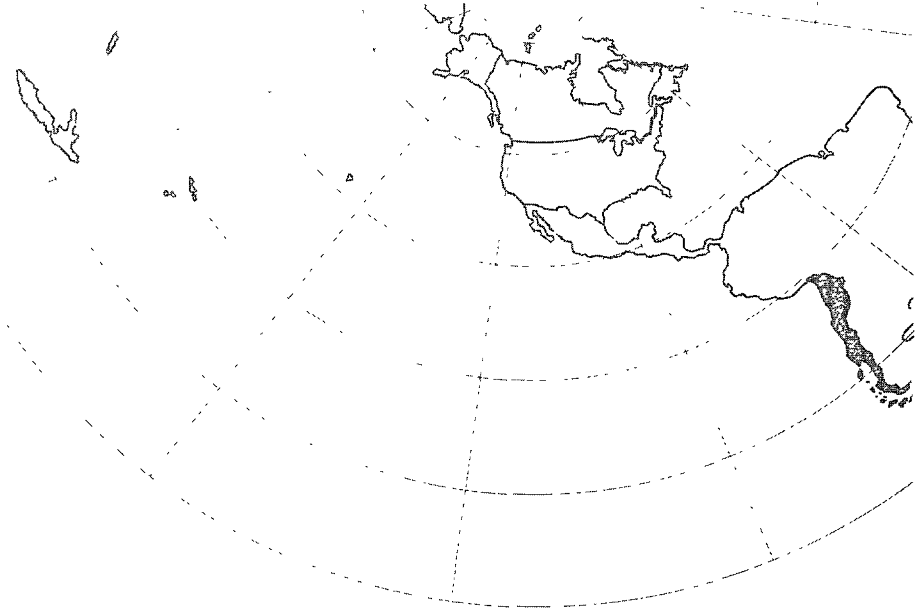
The continued strength in the U.S. economy is good news for Canadian exports, which should also benefit from better economic performances in Europe and Japan. However, recent indicators show signs of a slowdown, particularly in the consumer sector. Overall, real exports are forecast to increase by 12 percent in 1995 before growth slows markedly to a rate of 5.1 percent in 1996.

INFLATION

There should be sufficient slack in the Canadian economy to ensure that inflation does not increase significantly over the short term. Although prices for some commodities have increased sharply over the last six months (especially forest products and metals), there is little sign of these increases being passed on into the CPI.

The same applies to wages, where an acceleration in private sector wage settlements has yet to show up in the CPI. The current outlook assumes that productivity gains and excess capacity overall will combine to hold growth in the CPI to 2 percent in 1995 and 2.2 percent in 1996. This marks an increase over the rate of CPI inflation in 1994 (net of tobacco tax changes) that is largely attributable to the decrease in the value of the dollar.

CHILE



REAL GDP/GNP

THE ECONOMY DURING 1994

Growth and inflation in Chile during 1994 were consistent with the targets made explicit by the government at the end of the previous year. Output expanded by just 4.2 percent, but marked Chile's eleventh year of continuous output expansion. Annual inflation fell to 8.9 percent. Only on the external front was the performance different from the official projections, as the current account deficit was only equivalent to 1.4 percent of GDP.

During 1994 the independent Central Bank actively pursued stabilization goals, keeping the annual real interest rate of 90-day bills at 6.5 percent during most of the year, and reducing it to 6.1 percent in two stages during the last quarter. The Central Bank also continued its exchange rate policy of a managed float within a 20 percent band whose center is anchored to a basket of foreign currencies. The value of the basket is adjusted according to the difference between domestic and foreign inflation. The exchange rate policy remained unchanged throughout most of the year, until the band was adjusted upwards by 10 percent in early December, providing room for a moderate appreciation of the peso.

The slowdown of the economy during 1994 was driven by sluggish domestic demand, owing to a moderation of consumption and investment growth. Inventory accumulation as a percentage of GDP fell from 3.3 percent in 1993 to 2.5 percent in 1994. Private consumption expanded 4.4 percent, while government consumption expanded 2.5 percent. Gross fixed capital formation increased 3.5 percent, and represented 26.3 percent of GDP.

Exports of goods and services resumed their leadership in the growth process, increasing 8.2 percent in volume terms. This reflects the continued dynamism of non-traditional exports, which grew approximately 20 percent in real terms in 1994, and the recovery of some traditional exports that were affected by adverse external conditions in 1993. Imports of goods and services expanded 5.1 percent in real terms.

The terms of trade recovered rapidly in 1994, including an estimated 7 percent increase in export prices. As a result, the trade balance at the end of the year showed a surplus of $0.7 billion, and the external current account closed with a deficit around $0.8 billion.

ECONOMIC OUTLOOK FOR 1995

Government policy will remain the same as in previous years. The independent Central Bank has established a strong reputation since its creation in 1989, and the government has confirmed a conservative fiscal policy. In this context, macroeconomic policy will continue to be aimed at reducing inflation, attaining sustainable current account deficits, and avoiding major internal imbalances.

After two years of economic adjustment, economic growth in 1995 is expected to accelerate to between 5.5 and 6 percent, slightly below the long-term rate. The growth will be spurred by domestic demand, particularly private investment and consumption. The reduction of longterm interest rates, and the end of contractionary cycles in the construction industry, should stimulate a faster increase in gross capital formation. Gross fixed capital formation is expected to grow at a faster rate than GDP, and its ratio to GDP should increase slightly above 26.5 percent. Private consumption is expected to grow 6 percent, and aggregate domestic demand is expected to grow 6.2 percent, somewhat faster than output.

Growth will continue to be led by exports of goods and non-factor services, which are expected to expand by around 10 percent in real terms. The leading force in export growth in 1995 is expected to be copper. Non-traditional exports are expected to continue to be a dynamic force. It is projected that average annual export prices in 1995 for the main export items will significantly exceed those in 1994, so that the terms of trade will continue to improve. The effect of the Mexican crisis on export demand should be limited to some sectors of industrial exports that will be forced to search for alternative markets. Imports are expected to grow somewhat faster than exports, 11 percent in real terms, but the trade balance should remain in surplus, and be higher than in 1994, owing to the terms of trade improvement.

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The current account deficit is expected to remain around US$0.7 billion, the equivalent of 1.2 percent of GDP. The deficit in financial services is expected to increase as a result of larger profit remittances that may follow the turbulence in international financial markets. This turbulence would most likely result in a significant reduction in the high level of net capital inflows registered in 1994, but not of net foreign direct investment. However, financing will still be more than sufficient to cover the current account deficit, and may even imply a further increase in net international reserves.

The trend of gradual disinflation should continue in 1995. It is expected that annual inflation will fall to 8 percent as a result of the increase in the gap between potential and actual output created by the 1993-94 adjustment. The credibility in the inflation targets set by the Central Bank, as well as the lagged response of wage inflation to the macroeconomic adjustment and the reduction of inflation, should be the driving forces of the 1995 inflation reduction.

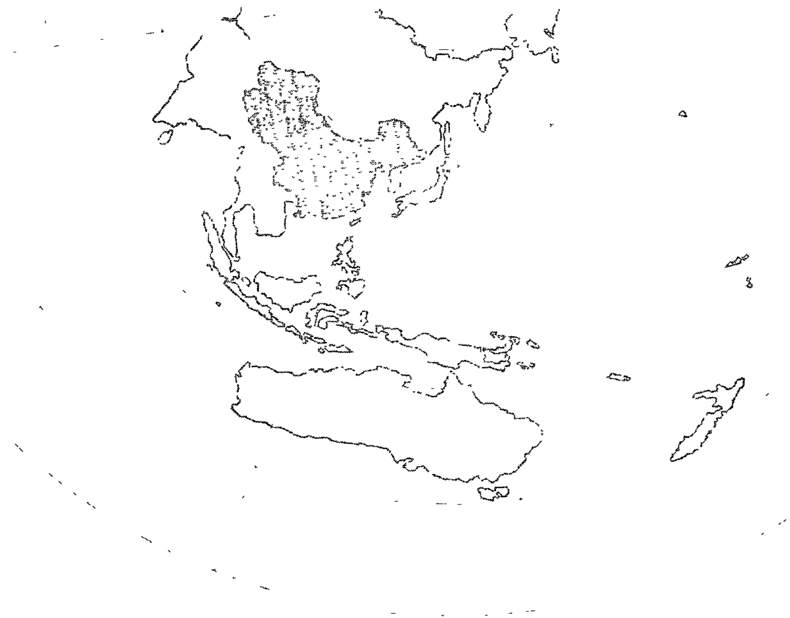
FORECAST FOR 1996

During 1996, economic growth should resume the trend rate of 6 percent, with annual inflation falling an additional one percentage point to 7 percent. The recovery of investment and output growth in 1995 should continue in 1996, keeping domestic demand expansion high. Gross fixed capital formation is expected to grow at 8 percent, and the capital formation to GDP ratio should increase to 27 percent. However, the moderate acceleration of output growth in 1996 will be the result of an increase in net exports.

In 1996, export prices should recede from the high levels of 1994-95, and the terms of trade should deteriorate, albeit still exceeding the 1994 level. Imports are expected to grow at a somewhat lower rate than exports in real terms, and the trade balance should deteriorate slightly.

The current account deficit is expected to increase to around 2 percent of GDP in 1996, still below the lower end of the medium-term target range. The projected increase in the current account deficit results from a deteriorated trade balance and a higher deficit in financial services, owing to higher net interest payments and profit repatriations. It is projected that a resumption in portfolio net inflows in 1996 would increase the availability of foreign exchange, while net direct foreign investment should remain stable at around US$1.4 billion.

CHINA



REAL GDP/GNP

ECONOMIC PERFORMANCE IN 1994

China's real GDP growth was 11.8 percent in 1994, the third consecutive year of high growth. Manufacturing continued to rapidly increase, and industrial value-added is estimated to have increased 18 percent. The major features of the 1994 expansion include a gradual speeding up of the pace of production, rapid growth in the coastal areas and among non-state owned enterprises, and an acceleration of light industrial production. Growth of heavy industry was lower than that of light industry (16 percent versus 19 percent) owing to strict control over fixed investment. The growth of investment decreased and its structure was somewhat improved. Fixed real investment rose 17 percent, and the share of important basic industries and infrastructure accounted for over 50 percent of its growth. Value-added in agriculture is estimated to have increased 3.5 percent in 1994 despite natural disasters in some areas. Tertiary industry developed vigorously, and its value-added increased 8.7 percent in 1994, with transportation and telecommunication growing 13 percent.

Private consumption increased about 30 percent in current prices in 1994, but only 7 percent in real terms. Despite price inflation, the propensity to save of residents was relatively strong. Purchases of treasury bonds and stocks were very large.

Exports increased 31.9 percent in 1994 to US$121 billion, and imports increased 35 percent to US$115.7 billion. At the beginning of 1994, the former double-track exchange rate of the Renminbi was unified. By the end of 1994, the exchange rate against the US dollar had appreciated a bit. Foreign direct investment in China increased greatly, up 35 percent to US$35 billion. Foreign exchange reserves doubled during the year and reached US$51 billion.

The fiscal and taxation reforms of 1994 led to a 18.9 percent increase in revenues during the first eleven months of 1994, compared to the full year 1993. Fiscal expenditures rose 22.1 percent, leading to a larger deficit. Monetary policy was tightened at the beginning of 1994. The monetary issue was lower than the planned target, and credit volume was within its target.

HIGH INFLATION IN 1994

The consumer price index and the retail price index of commodities increased 24.1 and 21.7 percent in 1994, which was the highest price hike over the past 16 years. Inflation was the most serious problem in 1994. However, along with inflation, stagnation was also seen in the rise of both unemployment and inventories. Meanwhile, the number of loss making enterprises remained large.

The most important factor causing inflation is the boom in investment that began in 1992. Much investment is still generated as a result of the combination of state political and economic power under the past planned economic system. This permits state-owned enterprises to freely use investment funds provided by the state. There have been some reforms, but the situation of a soft fiscal constraint on state-owned enterprises has not been fundamentally changed.

Foreign direct investment in China has increased rapidly since 1992, reaching US$25.3 billion in 1993 and US$33 billion in 1994. The foreign exchange coming from these investments are converted into Renminbi, much of which has ended up as foreign reserves in the central bank. This involves a huge rise in high powered money.

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THE POLICY ORIENTATION AND THE OUTLOOK FOR 1995 AND 1996

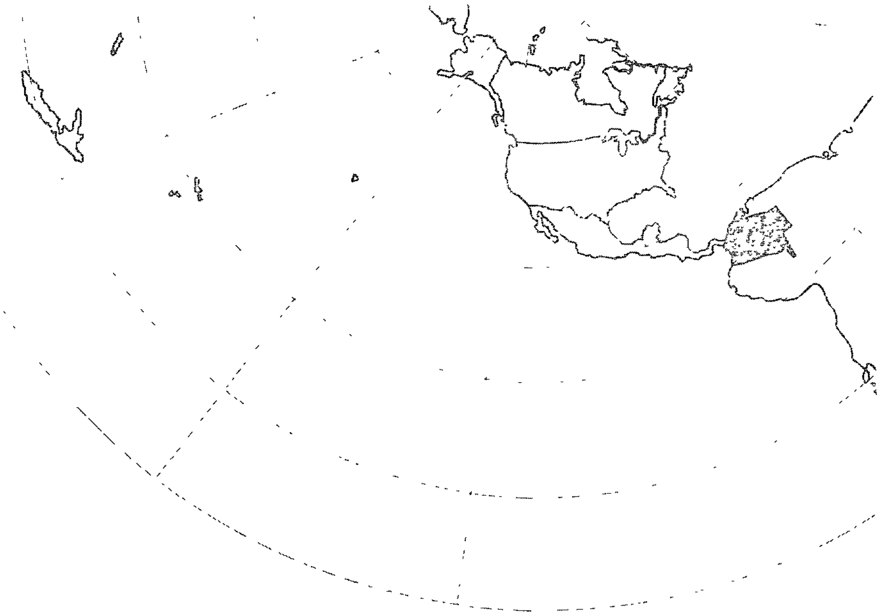
Policy in 1995 will be oriented to reducing inflation while avoiding an economic downturn. Due to the stringent measures taken on June 6, 1994, macro control has been strengthened and retail price inflation has begun to ebb. Fiscal policy is expected to considerably moderate the growth of fixed investment, but the economy will maintain a high rate of growth. Monetary policy should also be tightened. The growth of the money supply (M1) will likely decline to 26 percent from the 37 percent recorded in 1994.

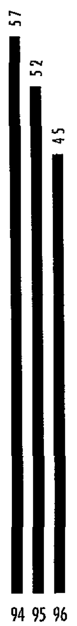
The growth of exports will likely slow in 1995 because of the absence of the exchange rate stimulus experienced in 1994. Imports will increase further, however, especially of grain, cotton, chemical fertilizer, steel, non-ferrous metals, and crude petroleum, for which there are shortages in the domestic market. While commercial loans from abroad will be strictly controlled, the utilization of foreign capital will be effectively encouraged and more attention will be paid to improving the structure of foreign capital. It is expected that foreign direct investment will increase 43 percent.

The economic growth rate for 1995 is expected to be 10.2 percent, with the inflation rate moderating to 17.8 percent. If a bumper harvest should occur and the various reform measures are continued, then inflation could be even lower. In sum, the national economy will approach a soft landing.

For 1996, appropriately tight fiscal and monetary policies are expected to aid in the adjustment of the structure of industry. Inputs into agriculture will be expanded further, and agricultural value-added is expected to increase 4 percent. Increasingly development projects will be extended to the hinterland, especially the northwest and southwest areas. With the resumption of China's status in the GATT, China's trade will adjust further. The economic growth rate in 1996 is expected to be 9.3 percent and inflation is expected to decline further to 14.6 percent.

COLOMBIA





REAL GDP/GNP

THE COLOMBIAN ECONOMY IN 1994

Real GDP grew by 5.7 percent in 1994, up from 5.3 percent in 1993. The increased growth was stimulated by a surge in domestic demand (8.7 percent), and particularly by private sector investment (19.1 percent) and public consumption (17.6 percent). Private investment in proportion to GDP came close to 13 percent, the highest rate in the last 20 years. On the other hand, private consumption grew by only 5.2 percent.

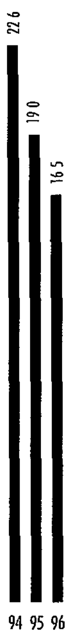
The increase in domestic demand also contributed to a marked rise in imports of goods and services (19 percent). This was encouraged by liberalization of trade controls in 1991 and the appreciation of the real exchange rate. Exports of goods increased by 15 percent and nontraditional exports grew by 10 percent. The favorable performance of exports is even more meaningful if we take into account Venezuela's economic crisis, strong domestic absorption and the real appreciation of the exchange rate. Total import growth was well above export growth, which increased the trade deficit and, coupled with the chronic service balance deficit, led to a current account deficit of US$2.8 billion, equivalent to 4.6 percent of GDP.

The capital account reported net inflows close to US$3 billion, which is well above last year's figure. Direct foreign investment reached US$1.4 billion, and medium- and long-term private external indebtedness US$2.6 billion. Much of the FDI went to the petroleum, financial, and telecommunications sectors. In contrast, public external indebtedness declined by US$190 million because of the government's policy of prepaying and substituting domestic for external debt. In all, capital inflows allowed the current account deficit to be financed, and reserves to increase US$133 million.

MONEY, INFLATION AND THE EXCHANGE RATE

The monetary base grew by 27.3 percent in 1994, down from 34 percent in 1993, and the means of payment (M1) increased by 26.6 percent. This was considered compatible with the central bank's target of a 19 percent rate of inflation and 5 percent real growth. From mid-year, interest rates were increased and more flexibility was given to central bank operators to set the interest rates in open market operations to levels aimed at achieving the monetary targets. Controls on external indebtedness were strengthened and due-date ceilings on import payments were reduced in order to restrain short-term capital inflows and hasten outflows. Nevertheless, private sector credit, including Peso and foreign currency denominated debt, increased by more than 45 percent during the year.

The consumer price index rose 22.6 percent in 1994, indicating no improvement from 1993. Inflationary pressures were mainly caused by low real interest rates in the first part of the year, high government expenditures, and the presence of inertial factors. Even higher inflation would have occurred in the absence of the minimum wage being set according to the inflation target, the limiting of price increases of public services, and the slowing of the nominal currency devaluation. Strong capital inflows and the adoption of an exchange rate sliding band system caused the nominal exchange rate to devalue by 3.4 percent at the end of the year. The real exchange rate, as measured by the producer price index, appreciated by 9.3 percent.



REAL GDP/GNP

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OUTLOOK FOR 1995 AND 1996

Our forecast for 1995 and 1996 rests on the following assumptions: that the average international price for coffee will be US$1.81 per pound in 1995 and US$1.60 in 1996; that growth in world trade will be 5 percent; that a 10 percent decline of Colombian exports to Venezuela will occur this year and in 1996; that there will be an 8 percent reduction in Colombian exports of textiles, leather and leather goods, and clothing to the United States, given the Mexican Peso's devaluation, but that in 1996 they will recover to the same value observed in 1994; and that world capital market conditions will cause Colombians to be more cautious in contracting external debt.

The government has committed itself to attaining a non-financial public surplus equivalent to 0.7 percent of GDP. At the same time, the central bank and the government have announced that they will continue to adopt a restrictive monetary policy this year, which will maintain real borrowing interest rates at levels around 8 percent to 9 percent and lending rates between 17 percent and 19 percent. Furthermore, a new exchange rate bandwidth of 14 percent was established at the end of 1994, with an implicit nominal devaluation of 13.5 percent for 1995. According to the plan, the real exchange rate will devalue two percent in 1996 and during the remaining years of this decade.

Economic activity throughout 1995 will be boosted by private and public investment, and increased revenues from coffee exports will stimulate the economy. In 1996, lower growth of private investment and consumption is expected — the outcome of a slowing in physical infrastructure investments, higher real interest rates, and the ebbing of demand for some consumer durables after three years of rapid increases. Moreover, restrictive monetary policies, smaller capital flows, and Mexico's and Venezuela's present economic difficulties will restrain Colombia's economic growth this year and in 1996. This suggests a slowing of Colombia's growth rate to between 4.7 percent and 5.6 percent in 1995, and between 4 percent and 5 percent in 1996.

Inflationary pressures are likely to be somewhat less than in 1994. Inflation will be sustained by the higher nominal devaluation rate and the using up of spare industrial capacity. The central bank's commitment, however, to achieving its monetary targets and to maintaining high real interest rates, as well as lessening inflationary inertia as a result of the social pact, suggest an inflation rate between 18 percent (the target) and 20 percent. For

1996, lower domestic demand and higher interest rates this year may allow for a reduction of two to three percentage points to between 15 percent and 18 percent.

The current account deficit as a percentage of GDP is forecast to be between 5.5 percent and 6.5 percent. Foreign direct investment will finance between 65 percent and 75 percent of the estimated deficit, particularly investments in petroleum exploitation, gas pipeline construction, and the expansion of the road network. The rest of Colombia's current account deficit will be financed by long-term private external indebtedness. For 1996, the country's current account deficit is estimated to be US$4.7 billion (6.5 percent of GDP), financed largely by FDI. From 1997 and beyond, however, the current account deficit will diminish, and finally reach levels close to 2.5 - 3.5 percent of GDP by 1999, given the 200 percent anticipated upswing in petroleum exports.

HONG KONG

REAL GDP/GNP

1994 - ECONOMIC GROWTH STEADY BUT BUSINESS CONDITIONS BECAME MORE DIFFICULT

Hong Kong's economy was affected by a number of unfavorable factors during 1994. Structural imbalances in China's economy, coupled with a high level of inflation there, have made it necessary for the macroeconomic adjustment program in China to continue, and this has taken a toll on the territory's exports of both goods and services, and the business of Hong Kong investors in China. The gradual rise in interest rates in the U.S., leading to increases in Hong Kong dollar interest rates, also put downward pressure on local property and share prices. On the political front, although the breakdown of Sino-British talks on the territory's 1994-95 electoral arrangements did not have any major impact on investor confidence, it has affected Sino-British cooperation on other issues.

Nevertheless, Hong Kong's economy performed well under these circumstances. The gross domestic product (GDP) is likely to achieve a real growth of 5.5 percent for 1994, as compared with an estimated 5.8 percent for 1993. Inflation as measured by the CPI has eased slightly, from 8.5 percent in 1993 to 8.1 percent in 1994.

Total export growth picked up from 10 percent in value terms in the first half of this year to 13.3 percent in the second half, though the whole-year growth of 11.8 percent was lower than the 13.1 percent registered in 1993. The combined growth of exports to the U.S., the E.U., and Japan improved slightly from 10.4 percent to 10.9 percent, while shipments to China grew slower at 13.6 percent, down from the 23.3 percent registered in 1993. Exports to China for its domestic use, in particular, grew much slower at 13.6 percent in value terms in the first 9 months of 1994 as compared to a 46.3 percent increase recorded during the same period in 1993. Much slower growth in the Chinese market, coupled with increased competition arising from a much higher level of interest in China by many firms, have made business conditions difficult for many companies in Hong Kong.

Another growth impetus came from increased fixed capital investment by both the public and private sectors. Construction work on infrastructure projects has boosted expenditure on building and construction despite a gradual slowdown in property development work in the latter part of the year. A faster rate of growth in retained imports of capital goods also suggested a higher level of investment in plants and machinery, particularly in office equipment.

By contrast, a slowdown in consumer spending was evident since the second quarter, due partly to the negative wealth effect as a result of falling property and share prices. Increased home mortgage payments as a result of the rise in interest rates and the difficult business conditions faced by many firms in China probably also contributed to the decline. Growth in real retail sales slowed from 8.2 percent during the first half of 1994 to 3.2 percent in the second half.

1994 witnessed some interesting developments in the labor market. Following a trend established since late 1993, the local labor force has grown significantly faster than previous years. For the first nine months of 1994, the total labor force grew by about 3.5 percent over that of a year ago. This compares with an average growth rate of 0.8 percent in the previous 5 years. The number of persons employed during the first three quarters of 1994 also grew by 3.6 percent. This phenomenon is due largely to a rapid increase in net in-migration, and appears to be driven by the increase in the level of confidence over the long-term prospects for Hong Kong and China, which has discouraged emigration among working age people, lured more Hong Kong workers who had emigrated to return, and attracted more expatriates to come to work in the territory. As the unemployment rate has remained stable, at around 2.1 percent, the faster rate of growth in the labor force was matched by increases in job opportunities.

CPI

1995 - GROWTH CONTINUES TO BE STEADY WHILE INFLATION RISES

Economic prospects for the G-7 countries as a whole should remain positive in 1995, while in China, the on-going macroeconomic adjustment program is set to continue. Against this background, Hong Kong's exports should experience another year of moderate growth. Total exports are expected to grow 16 percent in value terms, within which re-exports are expected to grow by 19 percent.

On the domestic side, rising interest rates and a weak property market have dampened plans for property development, and hence private-sector spending on building and construction. But this is more than offset by the increase in spending on infrastructural projects so that gross domestic fixed capital formation should grow faster in 1995 as compared to 1994. On the other hand, private sector consumption expenditure is likely to be continually affected by higher interest rates and weak asset prices.

On the whole, Hong Kong's real GDP is likely to grow by 5.5 percent in 1995 as compared with an estimated 5.5 percent in 1994. Inflationary pressure, however, should rise. An acceleration in infrastructural spending should add upward pressures on the domestic wage price structure. The rate of increase for charges on services such as rents for residential premises, school fees and public transport fares is also expected to stay high. Furthermore, import prices have started to rise faster in recent months on the back of a weak Hong Kong dollar (due to the weakness of the U.S. dollar against other major currencies) and this higher rate of imported inflation is expected to continue, given the weakness of the U.S. dollar against the Yen and the Mark in particular. Should the Renminbi continue to stay strong versus the Hong Kong dollar during 1995, and given the high level of inflation in China, import prices from China should also increase in due course. Overall, inflation as measured by the CPI is forecast to rise to 9.3 percent in 1995, as compared with 8.1 percent in 1994.

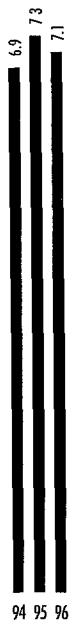
PROSPECTS FOR 1996

The pick-up in economic growth in Japan and Germany is likely to gather momentum in 1996, while the growth in the U.S. and other OECD economies appears likely to decelerate. China, on the other hand, should experience a slightly faster rate of growth in 1996, following a further year of consolidation in 1995. Against this background, Hong Kong's total exports should continue to grow steadily as compared with 1995.

Domestically, investment in infrastructure, particularly the new airport and related projects, is likely to grow faster than in 1995. The commitment of the government to increasing housing supply should also boost building and construction spending. Interest rates in Hong Kong should also have passed the top of the cycle as U.S. interest rates peak in 1995, and this should be conducive to investment and boost asset prices.

Overall, the economy is likely to continue a steady pace of expansion, with the GDP expected to grow 5.8 percent in 1996 as compared with 5.5 percent in 1995. Inflation, on the other hand, would also stay high, at 9 percent in 1996 as compared with a forecast of 9.3 percent in 1995.

INDONESIA



REAL GDP/GNP

RECENT TRENDS

After a good performance in 1993, inflationary pressures began to re-emerge in 1994 as the money supply grew faster than the targeted rate. Higher inflationary expectations caused interest rates to move upward. Ironically, this was the period when international interest rates were in a downward trend. Such a phenomenon, coupled with an open capital account system and improved capital markets, put Indonesia on the list of Asian countries receiving considerable amounts of capital inflows during that period.

The monetary authority faced a classical problem of sterilization. As expected, this put pressure on the exchange rate. During the second half of 1994, the exchange rate appreciated, albeit not at an alarming pace. For the entire year, the real appreciation was about 2 to 3 percent. Such a development only worsened a number of serious problems that have been facing the export sector.

The foreign trade picture was rather bleak in 1993. Export growth, especially of non-oil commodities, dropped markedly. The deceleration continued in 1994. Measured in local currency at constant prices, 1993 export growth was sharply lower than the rate in 1992 (11.6 versus 21.3 percent). The significant drop that occurred in textile and garment exports in 1993 was likely repeated in 1994.

The slow down in exports has raised quite serious concerns. Most of the reasons behind it are actually not new, and include a recession in a major export destination, increased competition from other (emerging) countries, and a number of domestic factors ranging from the long and inefficient procedures in the implementation of the drawback system to the suspected unscrupulous system of quota allocation. In general, domestic rigidities have been the most important determinant, suggesting that much still needs to be done in deregulating the economy.

An important package announced in June 1994 dealt mostly with investment. Basically, its goals are to simplify investment procedures and ease the condition for divestment. For example, in the case of a joint-venture with 95 percent foreign ownership, no divestment is required at all. Even for a wholly owned subsidiary, the divestment requirement is (deliberately) stated very vaguely. Furthermore, no minimum amount of initial investment is now required. With respect to sectors, at least 9 major sectors (especially in infrastructure) previously closed to foreign investment are now opened. Still controversial is the opening of the mass-media sector to foreign investors. No specific mention is made of location, except that in those areas having a bonded-zone and/or an industrial estate, the recommended location for foreign investment is in those zones.

This package was among the important factors taken into account in our forecast. Recent data show that approved foreign investment for 1994 soared to a record $23 billion, tripled from the total approvals in 1993. The restructuring process in Korea, Taiwan, and Japan is an important external factor in this regard. A large increase was also recorded for domestic private investment. Signs of a construction boom began to emerge, raising concerns for an overheated economy. Existing infrastructure simply can not keep up with the surge. The investment upsurge raised the growth rate of GDP in 1994 to an estimated 7.1 percent, which is higher than previously forecast.

The inflation rate in 1994 was around 10 percent. While there have been signs indicating that inflationary pressures will continue in 1995, past history suggests that policy responses are likely to be taken when such pressures arise. The central bank's move to raise key discount rates during the second half of 1994 turned out to be only the beginning of a series of interest rate hikes. By October, the central bank had raised the rate seven times. It should be noted that some of these moves were also meant to adjust to the international trend. Twice in early 1995, key discount rates were also raised following a similar move by the U.S. Federal Reserve, in a bid to limit possible capital flight.

CPI

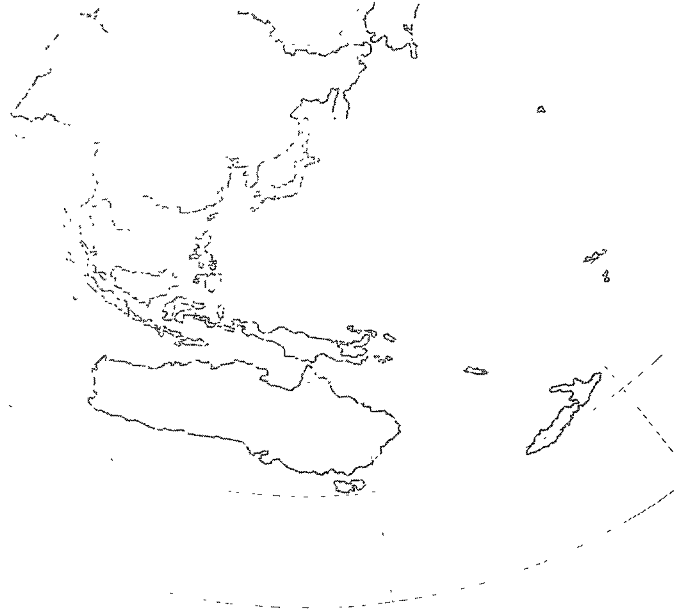
THE FORECAST

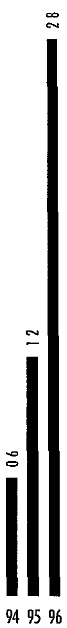
The Mexican financial crisis hit at the end of 1994. In the week following the Mexican devaluation in December, a jitteriness was observed in the foreign exchange and stock markets in a number of Asian countries. Indonesia was no exception. The stock market took a hammering with the composite index finishing at 441.87, which is the lowest level in 15 months. The Indonesian rupiah came under a week-long offshore attack. Concerns over the nation's foreign debt — almost $100 billion — seem to be the prime reason. In response, the central bank made a swift move by intervening in the market, selling some $500 million, and it worked! The rupiah, which had been dumped by foreign banks for a couple of days, was immediately stabilized. Such an incident (some called it mini crisis), along with a strong move by the monetary authority, is expected to raise confidence about the rupiah and on the handling of monetary policy.

On the fiscal side, the 1995/96 budget is once again tight. With a nominal increase of 11.9 percent, in real terms the budget is practically not expanding. An optimistic target was set for non-oil revenues, particularly the value-added tax and sales tax on luxury goods (increased by 26 percent). The targeted oil revenue is based on the oil price assumption of $16.50 per barrel. In announcing the budget, the government also made 6 percent an explicit inflation target for fiscal year 1995/96, despite a salary rise of 10 percent for civil servants, the military and pensioners. Such an inflation rate is lower than our forecast for the calendar year of 1995 (7.3 percent). With the assumption that infrastructure bottlenecks are not expected to be resolved very soon, it is our view that inflationary pressures are likely to persist throughout the rest of the forecast period. However, efforts to control inflation will always be in place, resulting in a one-digit rate each year (around 8 percent) during 1995 - 1998.

With almost 40 percent of expenditure taken up by debt servicing, the 1995/96 budget clearly indicates that the government expects private investment to take a leading role. While the growth of real investment is not much changed compared to the figure in 1994, it is estimated that in 1995, the private sector's share will increase. In our forecast, during 1995-1998 total investment is expected to grow at a fairly stable rate (in the neighborhood of 10 percent). Such a scenario implies that investment's contribution to GDP growth will not change much. The forecast pattern of private consumption growth is also steady — albeit in an ascending trend — between 4.5 and 5.5 percent, suggesting a small increase in its contribution to GDP growth.

JAPAN





REAL GDP/GNP

SLOW RECOVERY WILL BE HAMPERED BY THE LATEST QUAKE IN KOBE

Japan's long recession came to end, but the process of recovery was glacial in the first five months of 1994. In the summer of 1994, Japan was hit by a highly unusual run of hot and dry weather. It boosted sales of goods that hot weather forces people to buy; air-conditioner sales nearly doubled compared to the summer of 1993.

The summer sales were also boosted by an income tax rebate (up to a 20 percent cut of the total tax compared to the previous year), and new car sales picked up. In addition, the world economic situation contributed to Japan's recovery. The expansion of the U.S. economy in particular brought about a substantial increase in exports from Japan, including semiconductors, LCDs, and even fully-assembled autos. This led to an upward revision of investment plans by the electronics and automotive industries.

THE STRONG YEN AND EXPORT GROWTH

Export growth is continuing in spite of a strong yen and decelerating U.S. economic growth. The strong yen seems to undermine the price competitiveness of Japanese products relative to those from Germany, Korea, and Taiwan in machinery exports. But Japan's hi-tech machinery and parts are price-inelastic owing to high quality.

Japan's external balance began to show signs of a reduction — exports are growing, but Japan's imports are showing much greater growth. Japan's import demand for American products is rising. Sales of passenger cars for recreational purposes and CPU chips for personal computers are rising at an extraordinary pace. These phenomena are not the result of the bilateral trade talks between the two countries, but are simply the result of market forces. Substantial drops in the prices of goods imported from the U.S. brought about a surge in demand. Prices of imported goods are coming down as keen competition is taking place in the market for consumer goods and the prospect of high profits is drawing many competitors into the market.

This so-called "Price Destruction" is spreading widely. Not only are the prices of imported goods falling, but so are the retail prices of domestically produced goods such as beer, wine, and other manufactured goods.

Japan's distribution industry is at long last facing a drastic reform generated by market forces. Price destruction is not well represented in the official CPI since it does not fully include prices of imported goods or goods of high import-content. Most economists agree that the "real CPI" is falling even though the official one still maintains an upward trend.

Plant and equipment investment is likely to register a negative rate of growth this year (the fourth in a row), but stock adjustments seem to have come to end in many industrial sectors. The electronics and auto industries are likely to show an increase in investment expenditures.

Lower interest rates and expanded housing loans by the government keep housing investment strong. It appears that price destruction is now going to hit the housing construction market, where the internal/external price differentials are most conspicuous. Expanded housing loans and a drop in the cost of houses will further contribute to expansion of housing investment in the future.

CPI

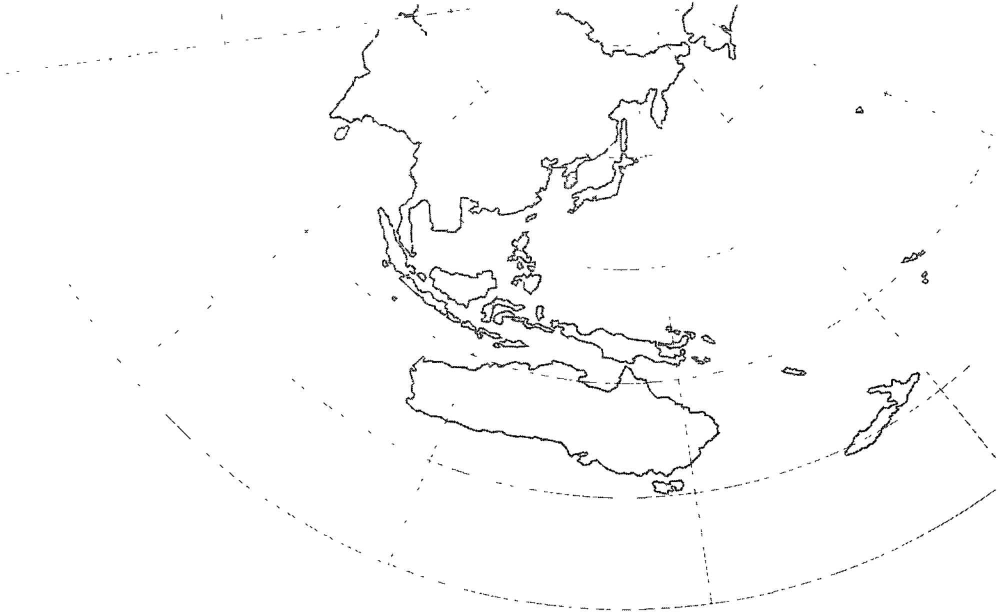
INCOME TAX CUT AND FISCAL EXPENDITURES

The problem with the current income tax cut is that it will have to be compensated for by an increase in the consumption tax in the near future. A new tax reform will combine an income tax cut of 5.5 trillion yen for fiscal 1995 with a VAT increase (from the present 3 percent to 5 percent) to start in fiscal 1997. The two year time-lag before the increase of the VAT has been given much attention, and was achieved by the LDP - JSP coalition government.

IMPACT OF THE KOBE QUAKE

The total loss to physical assets as a result of the earthquake in Kobe is estimated to be around 10 trillion yen. The 1995 forecast is impacted because local production declined and unemployment increased temporarily. It will take a great deal of time to clear up wrecked buildings and highways. A real output increase due to reconstruction work is likely to show up in 1996. Hence, the 1995 growth rate of GDP is revised downward to 1.2 percent, and the 1996 growth rate is likely to rise to 2.8 percent.

KOREA



REAL GDP/GNP

ECONOMIC GROWTH AND SECTOR PERFORMANCE

The recent upswing in the Korean economy is expected to continue until the end of 1995, although the pace will gradually slow down. The current expansionary phase is expected to last longer than the average duration of about two and one-half years mainly because of the continued increase in exports due to the strong yen and the world's economic recovery. Real GNP growth is projected to reach its peak in 1994 at 8.5 percent and to gradually decline to 7.6 percent in 1995 and 6.7 percent in 1996. The economic growth momentum for 1995-96 is expected to come more from private consumption and construction investment, while the contribution of equipment investment and exports should decline.

Private consumption will continue its expansion, increasing 7.9 percent in 1995, although its growth rate is expected to decline to 6.9 percent in 1996. In 1995, private consumption will be affected not only by increased income, but also by a rise in asset prices through wealth effects. Despite the recent decline, stock prices are expected to rebound in the second half of 1995 due to the continued cyclical upswings and additional stock market opening to foreign investors. In addition, the declining trend in real estate prices has recently slowed, and is expected to be reversed in the second half of 1995.

Given the fact that the equipment investment boom began in the second half of 1993, it is likely to continue until the first half of 1995. However, equipment investment is projected to grow by 11.6 percent and 7.8 percent in 1995 and 1996, respectively, down from 21 percent in 1994. Such a decline in investment growth will be partly affected by the expiration of the special investment tax credit and lower export growth rates expected in 1995-96.

Construction investment is projected to increase by more than 9 percent in the 1995-96 period. Residential construction will be stimulated by continued deregulation and the upward realignment of reference prices for apartments. Civil construction will also be active as the demand for SOC investment is expected to be strong given its high priority in government expenditures.

Exports should grow steadily in 1995 as the world economy is expected to show firm growth in output as well as in international trade. In 1995-96, however, the growth of merchandise exports will decline to 8 - 10 percent in real terms and 11 - 13 percent in dollar terms, as the domestic currency is expected to appreciate against the U.S. dollar. To achieve a soft-landing of the economy, the current administration is likely to allow the appreciation of the Korean currency to offset the adverse effect on price stability of the recent strong appreciation of the Japanese yen.

The increase in import demand is expected to slow due to lower economic growth and reduced investment demand in 1995. In addition, if the current trend of a strong yen continues, the expected rise in import prices will decrease the demand for imports. The projected growth rate of imports in dollar terms is 13.2 percent and 12.9 percent in 1995 and 1996, respectively. As imports are expected to grow more rapidly than exports, the trade deficit will widen to US$2.9 billion and US$4.8 billion in 1995 and 1996. In 1995, the current account deficit will remain similar to 1994, but it is expected to worsen to US$6.3 billion in 1996.

FINANCIAL MARKET AND PRICES

CPI

Given the monetary authority's price stability concerns, monetary policy for 1995 is expected to maintain a non-expansionary stance. The M2 growth target range for 1995 was set to 12 - 16 percent, which is 1 - 2 percent lower than last year's target. Reduction in M2 growth will be made largely through tightening the domestic credit supply to offset the increase in liquidity subsequent to the increase in capital inflows. Even though demand for investment will be less expansive in the next year, market interest rates are likely to remain at 14 - 15 percent in 1995 because of the reduction in money growth. The trend appreciation of the Japanese Yen and the DM will add to the increase in import prices, although the appreciation of the domestic currency could partially offset the impact of import prices on inflation. On the demand side, excess demand pressure must be controlled at a proper level for the economy to remain close to its potential growth path. Given these factors, the consumer price index is expected to rise by 6 percent and 5.4 percent in 1995 and 1996, respectively.

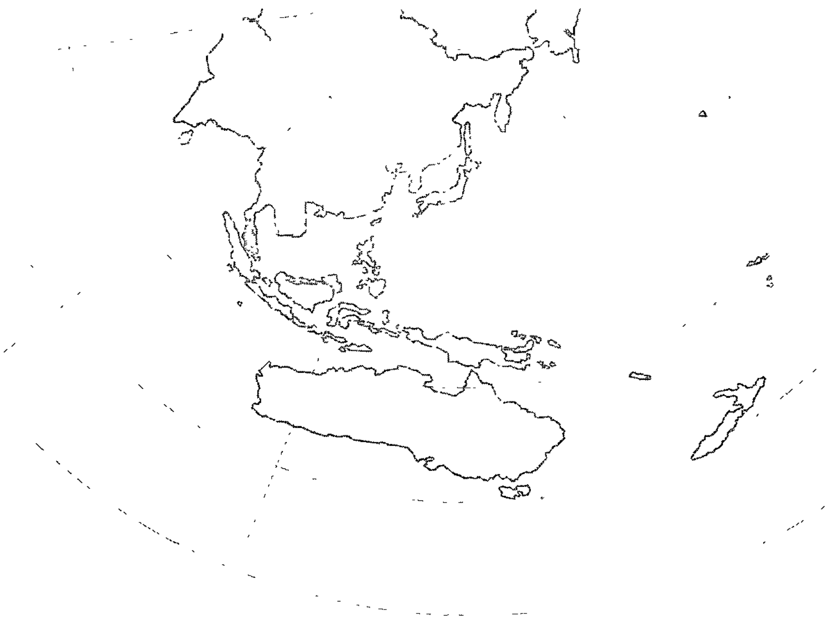
Capital account liberalization will be accelerated over the next several years. Since 1992, the domestic stock market has been open to direct foreign investment, with foreigners allowed to purchase stocks up to 10 percent of the total outstanding volume of listed stocks. The purchase limit was raised to 12 percent on December 1, 1994, and will rise to 15 percent by the end of 1995. The planned capital account liberalization will not be limited to the stock market. Long-term government bonds for primary issues and convertible bonds issued by small and medium-sized firms were made open to foreign investment this year. According to a preliminary plan, which has not yet been fixed, foreign investment in fixed income securities will also be gradually liberalized.

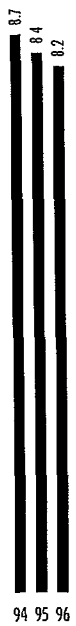
Given the planned capital account liberalization, the Korean economy will be faced with large capital inflows. About US$2-3 billion of additional capital inflows are expected due to the 3 percent increase in the stock purchase limit in 1995. Given the planned liberalization of capital flows, the capital account is expected to have a surplus of US$8 - 10 billion in 1995.

To minimize the adverse effects of excessive capital inflows, the government has introduced various liberalization measures in the foreign exchange market. In particular, regulations on capital outflows and foreign currency holding will be either substantially relaxed or lifted to reduce the expansionary effects of the increased capital inflows on the domestic money supply. During the 1986-88 period, more than 55 percent of the increase in the M2 supply was fueled by a massive current account surplus because foreign currency holdings by domestic residents was prohibited by law.

Despite the deregulation on capital outflows, the increased capital inflow is expected to exert expansionary pressures on the money supply, and appreciate the domestic currency. Therefore, an optimal policy mix will have to be devised to share the burden of macroeconomic adjustment. The importance of the exchange rate in accommodating the adverse effects of the increased capital inflow will be raised to a range that is not excessively harmful to the price competitiveness of exports. The expansionary effects of the increased capital inflow on the domestic money supply need to be offset by a fiscal surplus. To accomplish this, the average tax rate will be raised gradually until 1998.

MALAYSIA





REAL GDP/GNP

GROWTH MOMENTUM SUSTAINED IN 1994

In 1994 real GDP grew by 8.7 percent, marking the eighth consecutive year of greater than 8 percent growth. The major signs of overheating became more apparent, although domestic price inflation recorded a marginal increase of 3.7 percent. Growth was led by domestic demand, with private investment and consumption contributing more than half of the increase, and government spending the balance. Net exports of goods and non-factor services made a negative contribution. Industrial production was up by 12 percent largely because manufacturing, which accounts for one-third of the economy, expanded a strong 14.6 percent, with capacity utilization reaching 84 percent.

TRADE AND WIDENING CURRENT ACCOUNT DEFICIT

The Asia Pacific played a larger role in expanding Malaysia's trade performance, accounting for 80 percent of total trade in 1994. Exports expanded 26.8 percent to US$59 billion, and exports of electronic products alone contributed one-six of total export earnings, effectively transforming Malaysia into an important electronics specialization center in an increasingly globalized economy. Based on customs clearance data, imports rose by an expectedly high rate of 32.9 percent to US$60 billion, yielding a smaller merchandise trade surplus on an FOB basis.

The external account deficit widened to 6.6 percent of GNP, due to large service payments for freight and insurance as well as investment income. This deficit in the balance of payments may not, arguably, be as pressing as it seems because imports, which form a major component in the current account, are primarily investment-driven. About 85 percent of the gross imports bill was for capital and intermediate goods, including big ticket items such as aircraft, ships and offshore oil installations and tankers for the national carriers and oil industry. For the record, 12 years out of the last 15 years registered external current account imbalances.

COMBATING SPECULATIVE CAPITAL INFLOWS

The main focus of monetary policy in 1994 was combating a continued massive surge of capital inflows in search of profits from interest rate arbitrage, a widely-anticipated appreciation of the Malaysian Ringgit, and enormous tax-free capital gains from a booming stock market which saw a 250 percent increase in market capitalization to US$229 billion in the previous year. This was equivalent to 400 percent of GNP, making the Kuala Lumpur Stock Exchange the fourth largest bourse in Asia.

In the first ten months of 1994, gross capital inflows amounted to US$77 billion and outflows US$71 billion, compared with inflows of US$72 billion and outflows of US$62 billion in the previous year. The first response of the monetary authorities was to sterilize the de-stabilizing excess liquidity in the banking system through the sales of Central Bank bills and Treasury bills, but this was found to be inadequate. The second response, undertaken in January and February, took the form of six unprecedented measures: raising the statutory reserve requirement for banks' eligible liabilities by 3 percentage points in three steps to 11.5 percent, a historic high; placing foreign vostro accounts held with commercial banks with the Central Bank; charging a negative interest rate on foreign vostro balances along with the imposition of statutory reserve and liquidity requirements; setting a cap on banks' non trade-related external liabilities, thereby discouraging foreign borrowing; prohibiting the sale of short-term monetary instruments to non-residents; and banning non-trade related swaps and forward transactions with non-residents.

CPI

Except for the first two, these measures were subsequently lifted as monetary conditions stabilized and short-term rates declined. By year-end, the capital account saw a net outflow of short-term capital of US$5.7 billion compared with a net inflow of US$5.4 billion in the previous year, as well as a net inflow of private long-term capital of US$5 billion. The Ringgit showed a slight appreciation against the U.S. dollar but, for different reasons, a 6 percent depreciation against the Yen.

With an unemployment rate estimated at 2.9 percent, a 7.8 percent increase in manufacturing employment added new pressures on the tight labor market. The year also saw some erosion in labor competitiveness and new cost push inflationary pressures as wages in new wage agreements rose by 10 percent, prompting official pronouncements on the need to link wage increases with productivity.

OUTLOOK FOR 1995 AND 1996

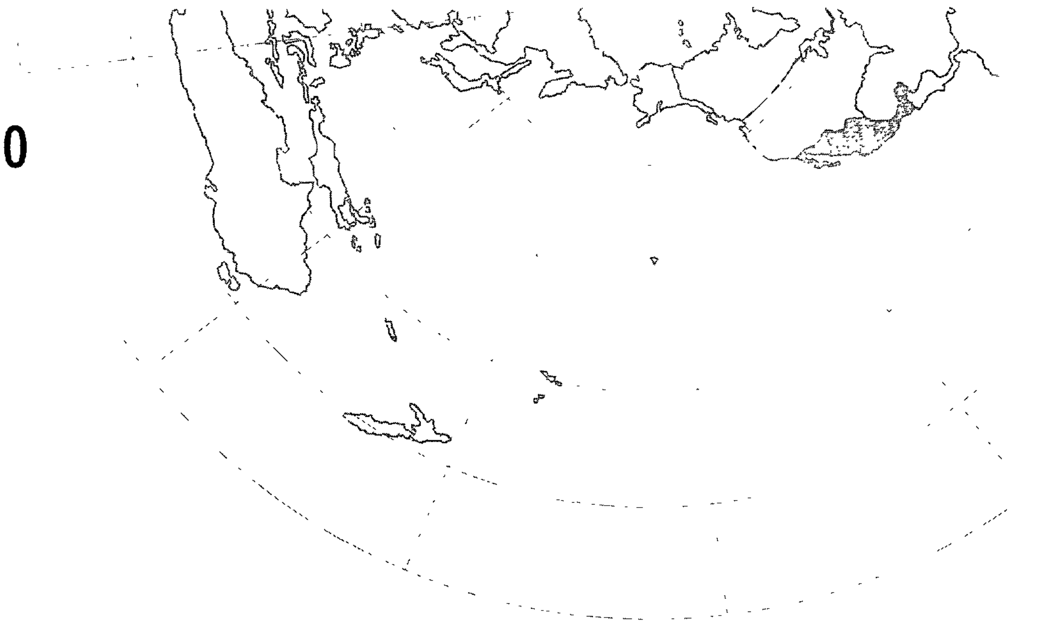
The October 1994 budget announced for 1995 implies a policy of fiscal restraint consistent with the Government's anti-inflationary stance and the country's development objectives. Economic growth in the 8 - 8.5 percent range is strongly expected in 1995 and 1996 as new and large investment projects come on stream.

High public spending can be anticipated, especially for key development projects - expressways, ports, hydro-electric projects and the new US$4 billion Kuala Lumpur International Airport at Sepang, 40 kilometers from Kuala Lumpur.

Confidence in new private investments is strong. In 1994, foreign direct investment showed a sharp upturn, increasing by 77 percent to US$4.3 billion and further enhancing the perception of Malaysia as a profit center.

The external imbalance is likely to continue, albeit at a lower magnitude, as will the reliance on foreign savings to meet the national resource gap.

The challenge remains for public policy to find solutions to high growth without domestic overheating while pursuing outward-oriented strategies.



MEXICO

REAL GDP/GNP

BACKGROUND TO THE CRISIS

Since 1988, the main objective of economic policy in Mexico has been to reduce inflation. In general terms, the economic program has been characterized by restrictive fiscal and monetary policies, a stable exchange rate used to "anchor" the economic program, and structural reforms, especially trade liberalization.

Even though the inflation rate followed a decreasing trend and was substantially reduced during the last year (from 51.7 percent in 1988 to 7.1 percent in 1993), it has been greater than in other countries, generating gradual appreciation of the real exchange rate. When combined with trade liberalization, this has led to increasing current account deficits.

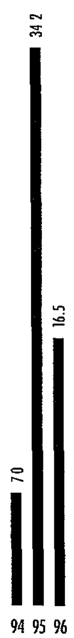
Between 1989 and 1993, foreign capital inflows were substantial, and took the form of both public and private indebtedness. Foreign investment financed both the current account deficit and permitted the accumulation of international reserves which reached $24.5 billion at the end of 1993. However, these inflows were substantially lower in 1994 due mainly to rising interest rates in the United States, larger political risk perceived by foreign investors, and enhanced attractiveness of other emerging markets such as Brazil. Thus Mexico received only about 20 percent of total portfolio foreign investment inflows channeled to Latin American countries in 1994, compared with almost 50 percent of such inflows received between 1989 and 1993. Hence, capital inflows financed only part of the current account deficit in 1994, while the rest was financed out of international reserves. These reserves decreased to $17.2 billion on November 1, 1994.

In order to avoid a deterioration of economic expectations because of political events (such as the military rebellion in the Mexican state of Chiapas, the assassination of the PRI's presidential candidate, uncertainty about the presidential elections, etc.), monetary policy sought to mitigate the impact of the reduction of capital inflows. In particular, policy aimed to avoid a "liquidity crisis", and thereby prevent higher interest rates from obstructing the recovery of economic activity.

One of the goals of monetary policy at that time was to provide enough credit to increase investment (and consumption), and consequently, economic growth. In fact, the rising trend of growth of GDP during the first three quarters of 1994 was in part a result of such monetary policy. The monetary expansion also contributed to increased imports, and thus added to the current account deficit.

Uncertainty increased when the new administration ratified the 1994 economic pact to continue the existing exchange rate policy, and was heightened when the 1995 Economic Program stated that "in 1995 exchange rate policy will maintain the established band." This implicitly assumed that interest rates would be the only available instrument to respond to contingencies, particularly the volatility of foreign capital flows.

In addition, the 1995 program recognized that the current account deficit would likely increase from $27.9 billion in 1994 to $30.3 billion in 1995. International and domestic financial markets perceived that such an economic program would not be feasible, particularly the exchange rate policy, because of the difficulty in obtaining enough foreign resources to finance the projected current account deficit. As a consequence, an exchange rate devaluation became unavoidable.



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THE CRISIS AND THE POLICY RESPONSE

On December 19, 1994, the financial authorities adjusted the fluctuation band of the exchange rate, increasing the ceiling by 15 percent. This action created even greater uncertainty, since it was not coupled with additional supporting measures. Both Mexican and international experience has shown that an exchange rate devaluation is successful only if it is accompanied by several measures dealing with the real sector (absorption adjustment, contraction in public and private expenditures, etc.) and the financial sector (restriction of credit and money supply). Otherwise the exchange rate depreciation only translates into inflationary pressures that nullify its positive effects.

As a consequence, the exchange rate adjustment was ineffective and unsustainable. In addition, financial markets considered the adjustment to be insufficient to correct the current account disequilibrium. An exchange rate crisis ensued with considerable financial market instability. Eventually, the financial authorities chose to let the exchange rate float freely (which depreciated substantially), and it was necessary to formulate a new economic program for 1995: the National Accord to Overcome the Economic Emergency.

The explicit short-term objectives of the program are to prevent the devaluation from creating an inflationary spiral with further exchange rate instability, to reduce the current account deficit, and to stabilize financial markets. The medium-term objective is to deepen structural change in the economy through the privatization of public enterprises and further deregulation of economic activity at both the regional and local levels.

Essentially, the new program substitutes the monetary base and wage restrictions for the exchange rate as the nominal "anchor" of the stabilization process. This requires a "purely orthodox" adjustment program with reduction of consumption, high real and nominal interest rates, contraction of real wages, and severe economic deceleration.

THE FORECAST FOR 1995 AND BEYOND

The economic program is feasible, but will likely yield less favorable results than those stated by the authorities, particularly with respect to economic growth and inflation. Monetary and wage restrictions combined with an average exchange rate of N$5.3 in 1995 would induce a contraction of real GDP of 4.9 percent compared with the rate of growth of 3.5 percent estimated for 1994. After a severe recession in the first quarter, economic activity should recover towards the end of the year. With the exception of exports, a contraction of every component of aggregate demand is expected, particularly private consumption (55 percent of total demand) and public investment.

With respect to inflation, annual growth of at least 34.2 percent is projected (higher than the official estimate of 19 percent). Almost 60 percent of it would be concentrated in the first four months of the year because of the impact of the devaluation — 65 percent of consumption is traded or potentially tradable. A complex pattern of inflationary expectations is anticipated.

The combined effect of the exchange rate devaluation and the monetary and wage contractions will induce a reduction of the trade deficit from $18.5 billion in 1994 to just $1.8 billion in 1995. A current account deficit of $15.3 billion dollars is projected for 1995 (10 percent higher than the official estimate), and economic uncertainty could make financing it a problem. Assuming that there will be no change in international reserves (at about $6 billion), the current account deficit implies that the private sector will need to obtain more than $2.3 billion from abroad in addition to direct foreign investment inflows of $8 billion dollars (official projections) and the public sector external debt placements of $5 billion.

Thus, the projected macroeconomic framework for 1995 is as follows: severe contraction of economic activity, with the resultant deterioration of employment levels; inflation of 35 percent concentrated in the first quarter; and high nominal and real interest rates. This will mean less investment and consumption, a negative but feasible public sector fiscal balance, a contraction of credit among commercial and development banks, and a current account deficit equivalent to 45 percent of that observed in 1994.

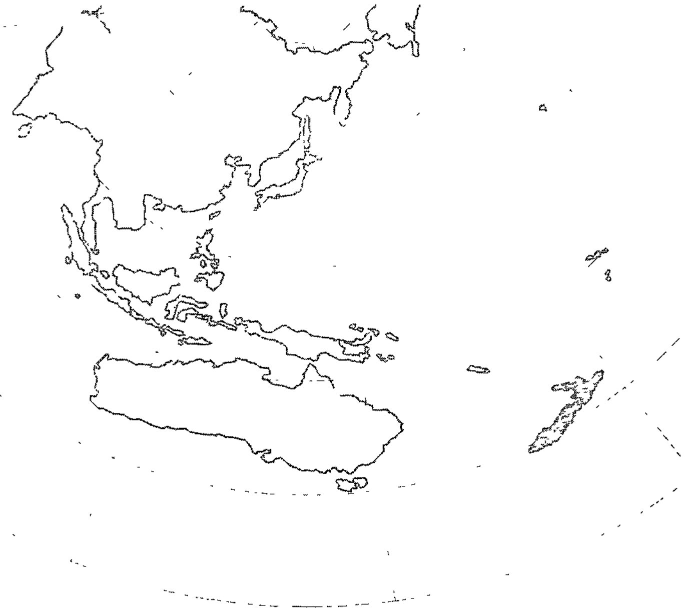
RISKS IN THE FORECAST

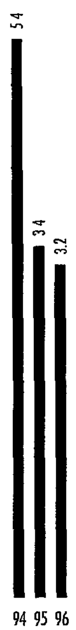
The program is in principle feasible, but it has diverse risks. They include problems in financing the current account deficit, the impossibility of maintaining wage restrictions, and the deterioration of inflationary expectations.

Despite a significant reduction of the current account deficit, the "markets" may not be ready to finance it. On one hand, the contraction of economic activity anticipated for 1995 will pose an important obstacle to direct foreign investment channeled to sectors directly tied to the domestic market, but on the other hand the increasing uncertainty of foreign investors will make it difficult to obtain other resources. If financing is not available, the external deficit would have to be further reduced. This would imply a larger exchange rate depreciation with the resultant effect on inflation and growth.

Another risk is that the authorities will be unable, or unwilling, if they do not consider it convenient because of "social pressure," to establish wage restrictions in the negotiations with unions because of the severity of the recession, increasing unemployment, and accumulated wage deterioration during the last year. Finally, there is the risk that the high rates of inflation in January through March will induce a significant deterioration of expectations so that this rate could be considered "permanent," with the resultant impact on interest rates, the exchange rate, and in general, the feasibility of the program.

NEW ZEALAND





REAL GDP/GNP

MACROECONOMIC FORECASTS

The New Zealand economy grew by 5.1 percent in 1993 and an estimated 5.4 percent in 1994, which was considerably stronger than expected. Until the middle of 1994, spare capacity in the economy allowed growth to occur in the absence of inflationary pressures, and interest rates fell to their lowest level for decades in early 1994. Inflationary pressures began to build in the latter half of 1994 as domestic demand picked up, and domestic interest rates rose sharply as a result of both a tightening in monetary policy and rising international rates.

Economic growth is forecast to slow to between 3 percent and 3.5 percent over the next two years as anti-inflationary policies bite. Nonetheless, this is a much improved performance over an average annual growth rate of only 0.2 percent between 1985 and 1992.

PRIVATE CONSUMPTION

Private consumption rose by 5 percent in 1994, the highest rate of growth since 1984. During 1995, growth in consumer spending will be constrained by higher interest rates, the impact of higher inflation on disposable incomes, and a slowing in new residential construction. In 1996, private consumption should grow by 3.1 percent, supported by growth in household real disposable incomes and employment, and a rising population.

BUSINESS INVESTMENT

Business sector investment rose by 25.5 percent in 1994 as manufacturers, and the transport sector in particular, were faced with growing capacity constraints. In 1995, investment in productive capacity is forecast to grow by nearly 17 percent, but the cycle has passed its peak as the capital stock comes more into line with demand. Growth will slow to 7 percent in 1996, but there will be further expansion of capacity, particularly in the manufacturing and tourist sectors. However, there will be major new investments in the retail sector, factory investment is expected to expand as manufacturing grows, and hotel investment should pick up along with growth in tourism.

EXPORTS

Exports are providing the main source of economic growth, and underpin much of the growth in domestic demand. In 1994, export volumes rose by 8 percent and are forecast to grow by between 5 percent and 5.5 percent annually over the next two years. Exports are dominated by commodity products, which will be constrained by only modest growth in production and limits on available stocks in the medium term. Therefore, this growth is largely coming from non-traditional goods and services.

Tourism has recovered strongly in recent years, and visitor numbers rose by over 14 percent in 1994. Growth from countries in Asia, particularly Korea, Thailand, and Taiwan, has been especially strong. This growth reflects rising incomes in the region, and has been aided by improved air links, the removal of visa requirements, and marketing. New Zealand is a popular holiday destination, and tourism growth of over 10 percent is being forecast to the end of the decade.

The other fast-growing export sector is non-commodity manufacturing products, which have found a ready market in Australia under CER, and around half of the exports are currently sold there. Export volume growth has averaged 17 percent annually in recent years and further growth of over 10 percent is expected in 1995.

CPI

IMPORTS

Recent growth in domestic demand has had a high import content, and import volumes rose by 12.5 percent in 1994. This growth has not been a cause of concern as it is largely made up of capital equipment and inputs into the production process. Strong import growth is forecast to continue in the short term, but in the medium term growth should slow as the investment cycle passes its peak and domestic production meets an increasing share of spending on both consumer and capital goods.

Trade liberalization has left New Zealand with one of the lowest tariff structures in the OECD, and further cuts are planned for coming years. Import penetration is not expected to increase markedly over the next two years, but there remains a risk that import penetration of the consumer good market in particular will be higher than forecast, especially if tariff cuts are combined with a significant appreciation of the exchange rate.

FISCAL AND MONETARY POLICY

Fiscal policy will remain tight during 1995 and 1996. Increasing fiscal surpluses are being forecast, and the government is expected to cut personal taxes in 1996. Tax cuts will be introduced gradually so they have a minimal impact on inflation and the current account. Fiscal surpluses will also be used to repay overseas debt, with the aim of reducing net foreign currency debt to zero within three years.

Monetary policy is also expected to remain tight during 1995 and the first half of 1996 as the Reserve Bank struggles to keep a lid on inflation. As inflation begins to fall from mid-1996, there is expected to be some easing in monetary conditions, although real interest rates will remain high.

INFLATION

The consumer price index rose 2.8 percent in 1994, which is above the upper limit of the central bank's target range of 0 - 2 percent. However, underlying inflation, (which excludes movements in interest rates, terms of trade effects, and government charges) remained well below 2 percent.

Inflationary pressures are expected to remain strong throughout 1995. Inflation is forecast to be between 2 percent and 4 percent throughout the year as a result of the sharp rise in mortgage interest rates at the end of 1994, pressure on wages as skill shortages develop, declining labor productivity and a slight rise in unit labor costs in the short term, and stronger international commodity prices. However, the tightening in monetary conditions that occurred in the latter half of 1994, and possible further tightening in the first half of 1995, aided by a strong currency, means this is temporary, and inflation should return to below 2 percent in the first half of 1996.

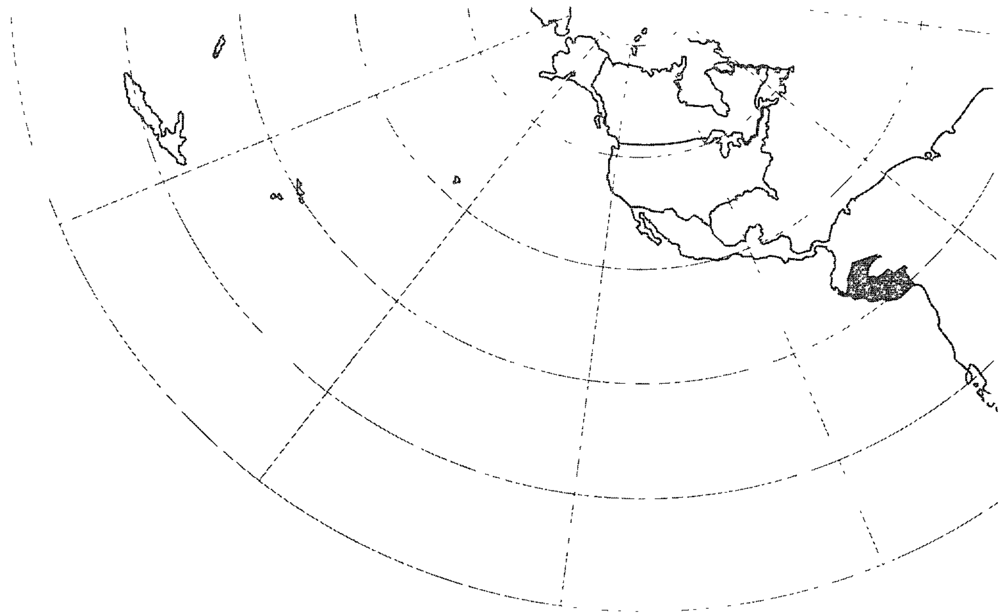
BALANCE OF PAYMENTS

New Zealand's current account deteriorated in the latter half of 1994 as imports eroded the trade surplus and high domestic company profits saw strong growth in dividend payments to overseas investors. This was partly offset by growth in tourism receipts. In 1995 and 1996, the current account deficit is forecast to improve to around 1.5 percent of GDP as import growth slows, the terms of trade rise, and tourism continues its strong expansion.

REAL INCOME GROWTH

Household average real disposable incomes are forecast to rise over the next two years. However, there will be further divergence in income growth between the higher and lower income groups. In particular, low skilled workers and households relying on government transfer payments are likely to see their incomes fall relative to growth in average wages and investment income. Business gross profits are estimated to have risen by around 13 percent in 1994, and are forecast to increase steadily as a percentage of nominal GDP over the next two years.

PERU



REAL GDP/GNP

PERU'S ECONOMIC PERFORMANCE

Peru's economic performance during the last three years has been exceptionally good. Inflation has come down from 7,649 percent in 1990 to 15.4 percent in 1994, GDP growth surged to 6.5 percent and 12.9 percent in 1993 and 1994, respectively, and GDP per capita is beginning to increase again. As good as these statistics are, however, they are just moving Peru from its lowest floor in the last 35 years. Peru is still far away from its GDP peak of 1985-1986.

At the same time, basic economic fundamentals look right. Government current and capital expenditures are entirely financed by current revenues and privatization of public enterprises. Net international reserves have grown 100 percent, totaling 6 billion dollars at the end of 1994 (about 11 months of imports). Monetary accounts, however, look relatively tight; money supply accounts for only 5.8 percent of GDP and if foreign currency is added, total liquidity reaches about 16.5 percent of GDP, meaning that dollarization is a major phenomena in the country.

This impressive economic performance has been accompanied by a decline in terrorism, increased foreign capital flows, and an upsurge of capital markets and net credit to the private sector from the banking system. Interest rates are declining, but are still high in comparison with international standards. The real lending interest rate for domestic currency came down from 41 percent in 1993 to 32.9 percent in 1994, while its real equivalent dollar rate was 11 percent in 1993 and 0 percent in 1994. The latter figure is basically a consequence of the real appreciation of the sol vis a vis the dollar (in 1994 exchange rate devaluation was -1.4 percent while the inflation rate was 15.4 percent), one of the major reasons for the dollarization of banking assets in the economy.

FORECAST FOR MAJOR ECONOMIC VARIABLES IN 1995-1996

To run ESAN's forecasting model for the Peruvian economy we made the following assumptions: higher government expenses are expected to arise from internal infrastructure development programs and external debt pressures; the government will use its funds from the privatization of public companies and the selling of treasury bonds to finance its larger budget; the central bank will continue to follow a monetary target instead of an exchange rate target, thus restraining money supply and monetary policies; foreign capital inflows will remain at the relatively high current level of 1993-1994; and no major increases in export prices are expected.

Given these assumptions, we expect GDP to grow 7.7 percent and 6.8 percent in 1995 and 1996, respectively. The real exchange rate will appreciate some more because of a nominal devaluation of only 5.6 percent and 4.3 percent in 1995 and 1996. At the same time domestic interest rates will continue to drive downward to 18.1 percent and 16.2 percent in 1995 and 1996, but those rates will still be far above the real equivalent dollar rates of 12.9 percent and 13 percent, respectively.

These major GDP and price projections in spite of real exchange appreciation will bring a positive balance of payment result of about 1.6 and 1.1 billion dollars and a superavit in public accounts of about 0.3 and 0.8 per cent of GDP in 1995 and 1996.

However, the balance of payments and the fiscal superavit could change to deficits if expected privatization fund goals are not achieved. Major sectoral macroeconomic balances are temporary due to the privatization process and, once it is finished, external and public macroeconomic imbalances may emerge again. Therefore, there are major inconsistencies between projected price figures and medium and long-term sectoral equilibria.

CPI

This appears relatively far in the distance (1997-1998), so there is still time to prevent a major macroeconomic crisis. A key issue is to redirect economic policy as to not allow the real exchange rate to further appreciate. This could perhaps lead to about one or two additional points in inflation and lower GDP growth, but much more consistent external and public accounts in the future. At the same time, policy should be addressed to increasing domestic savings, which is still only 15-16 percent of GDP, and not allowing accelerating increases in private or public sector demand. Peru's actual growth is very fragile in the face of an abrupt capital outflow of funds and an exchange rate crisis, as is occurring in Mexico and Argentina, and it needs to ameliorate the impact of those circumstances.

We must conclude that Peru's inflationary threat has finally dimmed and that the stabilization process is about to be completed. The major problem ahead is how to create employment and solve basic problems of poverty. GDP growth in the last two years has led to increased rather than decreased unemployment. Peru needs new economic investment that generates employment, not only the conversion of public into private enterprises. Encouraging long term and direct foreign investment in new economic activities, together with increasing domestic savings, are two related objectives.

One final additional point should, however, be considered. Peru's external debt problem has not yet been resolved. Those figures, without major reductions and forgiveness, will anticipate macroeconomic imbalances (in the public, savings and external accounts) and create major misallocations and inefficiencies. A major reduction of the external debt is a necessary condition for Peru to successfully face the challenge of increasing employment cum growth with celerity and efficiency.

PHILIPPINES

REAL GDP/GNP

THE 1994 RECOVERY

Gross Domestic Product (GDP) grew by 4.3 percent in 1994, up from the 2.1 percent growth rate a year earlier. And the Gross National Product (GNP) increased by 5.1 percent compared to the 1993 growth rate of 2.6 percent.

The momentum of the turnaround in 1993 was carried into a 1994 recovery, although the difference between GNP and GDP widened, which indicates the continuing importance of net foreign income from abroad (mainly remittances from Filipino workers) in maintaining the growth process.

On the expenditure side, exports and consumption expenditures showed increases of 19.5 and 3.7 percent, respectively. In fact, government expenditures even declined marginally from a 6.2 percent expansion in 1993. Although investment expenditures did increase, the growth rate of 10.1 percent was lower than the 1993 growth rate of 11.2 percent. Worrisome has been the import surge of 19.5 percent, which is more than the 6.2 percent growth rate in 1993.

The 1994 recovery, therefore, was mostly paced by exports and consumption spending. The actual (marginal) decline in government spending meant social capital formation did not really take place in 1994, implying a serious deterioration of infrastructure necessary for long-term growth. Exports also declined in the fourth quarter of 1994 (from 28.4 percent in the third quarter to 13.8 percent in the fourth quarter) while consumption expenditure continued apace. Imports, on the other hand, increased in the fourth quarter to 18 percent from the third quarter's 13 percent.

Looking at economic performance by sector, industry paced the recovery with an overall 6.1 percent growth rate in 1994 (it was 1.6 percent in 1993) while agriculture improved slightly on its 1993 performance. Within industry, manufacturing expanded by 5.1 percent (from 1993's 0.7 percent growth rate), construction growth almost doubled, and utilities surged forward.

1995 – LEVELING THE GROWTH

With the recovery in place in 1994, GDP is projected to grow by 5.2 percent in 1995, driven by a government expenditure turnaround of 3 percent. Investments will continue to keep the same pace as 1994, while consumption will see a slight increase from the 1994 level. Exports are expected to taper off, with a growth rate slightly lower than 1994.

Both agriculture and industry will increase their growth rates, the former to 3.1 percent (from the 1994 growth rate of 2.4 percent) and the latter to 8.2 percent. Again, both manufacturing and construction will lead the surge in industrial growth. Mining is expected to recover while utilities will slow down from the fast pace in 1994.

The 5.2 percent projected GDP increase in 1995 maintains the growth momentum but is leveling off from the sharp rise in 1994. In part, this is because government expenditures are expected to pick up (more so because of the May elections) from zero growth in 1994. On the other hand, exports will slow down, partly due to the continued appreciation of the currency and the problem of regaining markets as exchange rates increase.

A more feasible forecast is a leveling in the growth rate for 1995 dictated by the government budgetary conservatism in 1994, and by the market forces that effectively drown potential export expansion. The operational problems of the economy in 1993 have effectively been replaced by events which put a drag on a higher growth rate. Unfortunately, these were unnecessary and avoidable.

CPI

THE MEDIUM AND LONG RUN: A SHAKY FOUNDATION

The economy could surge forward to a higher growth rate of 6.1 percent in 1996 that would be pushed by investments. But it would depend on a foundation whose structure had been strengthened during the economy's turnaround and recovery.

The trade sector remains weak and unable to adjust because dramatic reforms have been slow and there have been surges of short term capital to rely on as well as remittances. Consequently, the country's trade deficit rose in the first three quarters of 1994 (13.7 percent of GNP from 11.1 percent in the full year of 1993), and was pushed further by a real currency appreciation.

National savings has remained at a constant low rate for the last several years (19 percent is low relative to the Asian averages and relative to investment requirements for sustained growth), and needs policy attention.

The government's fiscal prudence in 1994 is clearly a noteworthy point. But too much fiscal restraint during a recovery may have serious long run costs as social overhead deteriorates at the expense of productive investments. On the other hand, this did not induce private savings to increase either. Indeed, private consumption took up the slack. In the end, basic public investments have to be beefed up anyway, the sooner the better.

All these imply that both the recovery of 1994 and the expected growth leveling in 1995 rest on shaky foundations. They continue to reflect the kind of growth cycles the Philippines has experienced in the past and not a move towards sustainable high growth.

If the growth directions in the next 2 years materialize and do not fizzle out from a short-run shock (which the country is still quite vulnerable to), these foundations have to be addressed before they are further eroded.

SINGAPORE

REAL GDP/GNP

A BRIEF SURVEY OF THE SINGAPORE ECONOMY

The Singapore economy has repeated the high growth performance of 1993. A preliminary projection from available data indicates a GDP growth rate of 10.1 percent for 1994. The overall broad based growth was boosted by the buoyant growth in trade, recovery in the U.S. economy, and continued expansion of the regional ASEAN economies. The manufacturing sector improved upon its growth performance of 9.8 percent in 1993 to 12.9 percent in 1994. The electronics industry, greatly boosted by the export demand to the U.S., is once again the main contributor to the rapid growth in the manufacturing sector. The transportation and telecommunication sectors, as well as the construction sector, also posted double digit growth. The financial and business service sectors grew less rapidly than the previous year. In general, it is a reflection of the much subdued mood in the stock exchanges as a result of the rise in U.S. interest rates and the depreciation pressure of the U.S. dollar. It is also due to the consolidation and adjustment to the frenzied growth of 21 percent in the financial sector during 1993.

THE OUTLOOK FOR 1995-96

The growth prospects for the Singapore economy continue to be good for the next two years, given no adverse developments in the American and Japanese economies. The 10 percent growth rate of GDP is admirable but puts severe strain on the limited labor and land resources in the Singapore economy. International events, such as the Mexican currency crisis, lower U.S. growth, the Kobe earthquake, the uncertainty surrounding a Japanese fiscal stimulus, the announced intention to cool the Chinese economy, and apparent domestic constraints will dampen Singapore's GDP growth for the next two years. External trade is expected to grow at a lower rate of 14 percent. Productivity growth is expected to be a major contributor to GDP growth as corporations review and fine tune their manpower policies to accommodate the regionalization drive. The forecast growth rate of GDP for the economy in 1995 is 8 percent. The growth momentum is expected to be maintained in 1996 at 7 percent.

Inflationary pressure has been relatively suppressed in Singapore by the strong currency and weak import prices of commodities and raw materials. The imposition of a 3 percent goods and services tax (GST) in April 1994 is expected to have a one-time effect of raising the inflation rate from the average of 2.8 percent to 4 percent in 1994. In 1995 and 1996, inflation is expected to slide back to the pre-GST level of around 3 percent.

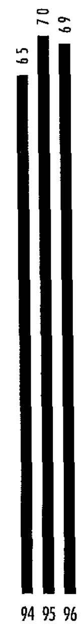
THE IMPACT OF REGIONALIZATION

An active regionalization policy has been pursued by the government to encourage local entrepreneurs and foreign investors based in Singapore to relocate production activities, become involved in joint ventures, and use the more abundant resources in the Asia Pacific region, particularly, China and Southeast Asia. The overseas investments will likely lead to capital outflow and a deficit in the capital account of the balance of payments. But in the longer term, the yields (profits, dividends, and interest) from such overseas investments will improve Singapore's current account. In the near future, the measurement of national income by the GNP definition will be more appropriate for the Singapore economy.

CPI

The movement of capital and production facilities overseas help to ameliorate the shortage of labor and land in Singapore. There is a perceptible gain in productivity as more labor intensive and standardized production activities have been shifted to neighboring countries. For two consecutive years, 1993 and 1994, the manufacturing sector registered productivity growth of 12.2 percent and 11.4 percent respectively, compared with the mere 3 percent recorded in 1992. Active participation in the regionalization drive by the government is a deliberate effort to ensure that it will not lead to a "hollowing out" or "de-industrialization" in Singapore. Retention of overseas headquarters and more technologically-advanced production functions in Singapore are actively encouraged and fostered. Liberalization of regional economies and the continued expansion of foreign investment in the region will allow the Singapore economy to grow at a rate near its potential for the next five years.

CHINESE TAIPEI



REAL GDP/GNP

ECONOMIC SITUATION IN 1994

Chinese Taipei's real GDP exhibited a moderate growth rate of 6.5 percent for 1994, a step up from the 6.3 percent recorded in 1993. Private consumption continued to grow rapidly at 8.2 percent. As in the past, its contribution to real GDP was the most conspicuous among various components of expenditure. It reached 57.8 percent of real GDP in 1994, up from 55.9 percent in 1993. The rise in private consumption was mainly due to the visible recovery of the global economy and stable growth of income.

Because of the heavy burden on the government budget from the simultaneous implementation of many major infrastructure and public construction projects, the government made its best effort to reduce its consumption and reign in its budget deficit. Consequently, real growth in government consumption in 1994 was negative, at -1.2 percent in 1994. The proportion of government consumption was 15 percent of real GDP, as compared to 15.8 percent in 1993.

With total consumption increasing at a higher rate than the GNP, the national saving ratio is estimated to have fallen slightly, from 27.7 percent in 1993 to 26.5 percent in 1994, the lowest recorded since 1970.

Real fixed capital formation grew 7.1 percent in 1994, reaching 24.3 percent of GDP as compared to 23.8 percent in 1993. As a result, the combination of the government's economic revitalization program to improve the domestic investment environment and its major infrastructure projects, the real annual growth rate of private investment was boosted to 10.4 percent in 1994, falling within the targeted range of 10-15 percent. As a consequence of the implementation of the Six Year National Development Plan, the government's investment maintained a nominal growth rate of 11.2 percent in 1994.

On the public enterprise side, after being delayed by weak stock market prices during 1990-93, the government decided to resume the State Owned Enterprise (SOE) privatization in order to ease its public debt. The combination of privatization and the completion of major investment projects led to a negative nominal growth rate of 9.3 percent for public enterprise investment in 1994.

Merchandise exports in 1994 reached US$93.1 billion (current prices), growing 9.4 percent relative to 1993. At the same time, imports increased 10.8 percent to US$85.4 billion. The resulting merchandise trade surplus was US$7.7 billion, down 4.1 percent from 1993.

Exports to the United States were sluggish, but the U.S. still accounted for 26.2 percent of the total value of exports. Instead, export growth was due to higher demand within Asia, especially Hong Kong and Japan. In 1994, exports to Hong Kong and Japan accounted for 22.8 percent and 11 percent of the total value of exports respectively, a 1.1 percent and 0.4 percent increase over last year. Hong Kong still plays a very important role as Chinese Taipei's major transit port for trade with China. Chinese Taipei's trade deficit with Japan did not show a substantial decrease in 1994. Furthermore, because tariffs on most imported goods will be reduced to 10 percent to meet GATT requirements, and the ban on some Japanese imports will be relaxed, the trade deficit will likely increase during 1995-96 unless exports to Japan benefit from the appreciation of the Japanese yen and increase proportionally.

The CPI inflation rate was 4.1 percent in 1994, higher than the 2.9 percent recorded for 1993. The CPI grew sharply in August, reaching 7.1 percent, the largest increase for a single month in more than 13 years. The rise in August resulted from a huge increase in food prices throughout Taiwan following four typhoons which caused serious floods. Furthermore, a combination of other factors suggested that inflationary pressures were continuing. Hence the Central Bank began to soak up excess liquidity in July 1994, and the annual growth rate of M2 has been back within the targeted range of 10-15 percent since September 1994.

CPI

ECONOMIC OUTLOOK FOR 1995-96

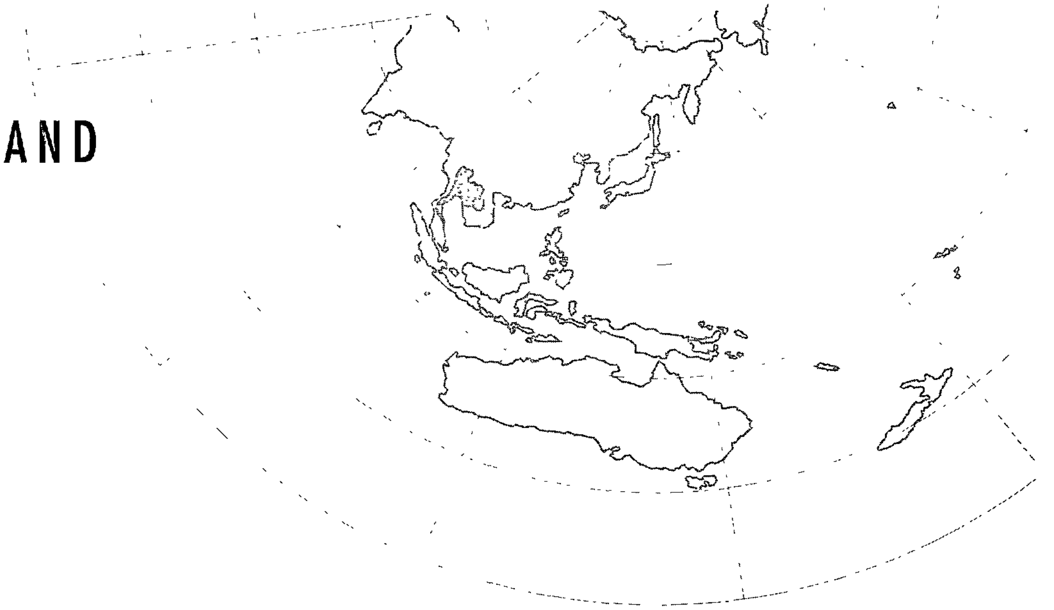
Real GDP is forecast to grow by 7 percent in 1995 and 6.9 percent in 1996, supported by greater private consumption and investment, stable growth of exports and imports, and continued recovery of the global economy.

With a declining propensity to save and an inflation rate well below 4 percent, real private consumption will grow by more than 7 percent per year in 1995 and 1996, maintaining its role as the leading sector in the GDP. Private consumption may also rise because of the legislative and presidential elections being held in late 1995 and March 1996, and because of the likely lowering of import prices due to tariff reductions resulting from joining the GATT and the possible appreciation of the New Taiwan Dollar. Government consumption, on the other hand, will be maintained at a zero or even negative growth rate, reflecting the government's policy of reducing expenditures. Also, the implementation of the National Health Insurance Plan will bring a rise in the government's debt-service ratio and further limit government spending in 1995-96.

Real gross fixed private investment may continue to grow in 1995-1996 as there are still enough incentives, such as establishing Chinese Taipei as an Asia Pacific Operational Center, designed to encourage private firms to invest in high-technology industries and establish operational headquarters at home rather than overseas. Conversely, investment in public enterprises will continue at a negative growth rate in 1995-1996, affected in part by the implementation of the SOE privatization program. As for government investment, a lack of funds, under-estimation of project costs, plus inefficient government administration have limited its rapid expansion.

Real growth of exports of goods and services is forecast to rise 8.1 percent in 1995 and 7.1 percent in 1996. Imports of capital goods will continue to expand rapidly in 1995-96 as the government may hasten to complete some projects and develop Chinese Taipei as an Asia Pacific Operational Center. Therefore, the import of goods and services is projected to grow by 7 percent in 1995 and 1996. The real trade surplus of goods and services may remain in the area of 2 percent of GNP during 1995-96, compared with 1.3 percent in 1993 and a preliminary 2.1 percent in 1994. Furthermore, inflation will remain stable during the next two years. Consumer price inflation is forecast to grow by 3.9 percent in 1995 and 3.5 percent in 1996, and the Central Bank is likely to implement a tight monetary policy in 1995 to ensure it.

THAILAND



REAL GDP/GNP

The Thai economy is forecast to continue to grow by 8.6 percent in 1995, up from 8.4 percent in 1994. Underpinning these high growth rates has been a surge in exports, increasing levels of domestic consumption and a dramatic rise in the level of foreign investment.

Inflation rose from 3.3 to 5 percent over the course of 1994, primarily due to increases in food prices. The current account deficit also widened as larger volumes of capital goods were imported to supply the investment boom. Increased imports of consumer goods and growing numbers of Thai tourists traveling overseas also contributed to the higher current account deficit. Interest rates are expected to continue their rising trend over 1995 in order to maintain positive capital flows.

The Thai government has taken steps towards liberalizing the economy. In February 1995, the government released the Financial Master Plan (the blueprint for the deregulation of financial markets), which seeks to expand the number of institutions in the financial sector, enhance competition in the banking industry, and improve regulation of the financial sector. The legal reform will be implemented in parallel with substantial tariff reforms flowing from the outcome of the Uruguay Round and the ASEAN Free Trade Area.

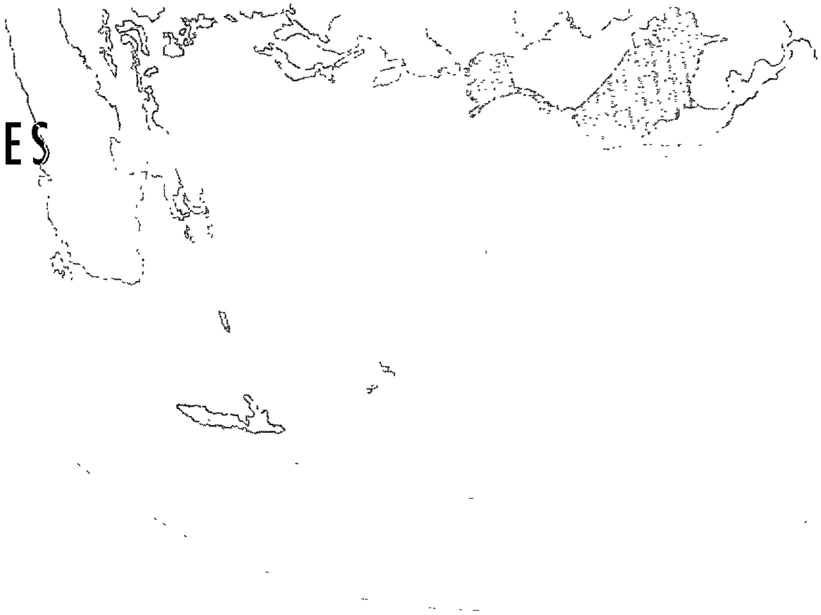
The government continued the use of conservative monetary policies aimed at ensuring that credit expansion keeps pace with macroeconomic developments. The government has set in place a program of privatization and concessions to maximize private sector involvement in infrastructure projects.

The FY 1995 budget contains expenditure of Bt 715 billion, representing an increase of 14.1 percent over FY 1994. Of this expenditure, 51 percent is for support of the government's key policies of regional and provincial development. The preliminary allocations in the FY 1996 budget direct increasing spending to the promotion of the role of local government.

Net revenue earned by the Thai government in the first half of 1994 was Bt 332 billion, an increase of 45 percent over the same period in 1993. For FY 1995, total government revenue is estimated to be Bt 768.3 billion, a 17.2 percent increase over FY 1994.

The Bank of Thailand revised its end of 1994 current account estimate upwards from Bt 180 billion to Bt 203 billion, an increase of 12.7 percent to 5.7 percent of GDP. At the end of 1994, Thailand's international reserves stood at US$30 billion.

UNITED STATES



REAL GDP/GNP

A SLOW DOWN, COURTESY OF THE FEDERAL RESERVE

In the thirteen months since February of 1994, the Federal Reserve has boosted the federal funds rate from 3 percent to 6 percent and most long term interest rates have gone up by about 1 1/2 percentage points over the same period. The evidence is now accumulating that the U.S. economy — on a tear during most of 1994 — is indeed responding to the Federal Reserve's disinflationary policy.

And that response is pretty much as expected, with the most interest-sensitive sectors cooling off first. For example, the January-February 1995 sales pace for new cars has slipped to an annual rate of 8.75 million units, compared with 9.25 million in the final quarter of 1994, and 9.4 million back in the opening quarter of last year. Similarly, existing home sales slid from an annual rate in excess of 4 million units in the first half of last year to a 3.8 million unit pace in the last quarter of 1994, and to a 3.6 million unit pace in January of this year. In addition, housing starts slipped to a 1.38 million unit annual rate in January, after reaching a pace in excess of 1.5 million units during the final three months of 1994.

A slowing in the pace of sales, if sustained, will also produce a moderating pace of production and employment; and evidence of that is also beginning to accumulate in the form of smaller monthly gains in industrial production, the count of jobs, and the number of persons employed.

BUT NOT A MELT DOWN

It does *NOT*, however, appear that the Fed has clamped down so hard as to send the economy into a 1995 recession. Rather, the economy is expected to continue to expand throughout 1995, but at a slower pace than during 1994.

In fact, it appears highly likely that the Federal Reserve will conclude that the upside inflationary risks are still too strong and that the economy can take even more disinflationary policy without sliding into recession. In other words, at this writing in mid-March, the Federal Reserve is not yet done raising interest rates. It is only mostly done.

THE U.S. DOLLAR AND FEDERAL RESERVE POLICY

It doesn't always work out this way, but at the moment international currency considerations are pointing the Fed in the same direction it was already facing in its focus on domestic policy. The dollar has been sinking in value against a number of major currencies for the past year, and that process accelerated in late-February/early-March.

The recent increase in downward pressure on the dollar hardly seems to have been the result of any change in U.S. economic fundamentals or in any basic relationship between the U.S. economy and its major trading partners. Rather, it was probably much more an animal-spirits over-reaction to a number of concurrent developments (including the collapse of the Mexican Peso, the likelihood that U.S. interest rates may soon stop rising relative to foreign rates, and the failure of the balanced budget amendment to pass in the Congress) and, as such, is not likely to last. But a weakening dollar does feed the inflationary potential that the Fed is aiming to minimize and is yet another reason for the Fed to be attracted to somewhat higher interest rates in the near term.

In consequence, the Fed is expected to raise short term interest rates by another 50-100 basis points between this writing and mid-year, and that should leave an upside inflation risk that is acceptably low for Chairman Greenspan and his colleagues at the Fed – *without producing a near term recession in the U.S. economy.*

CPI

THE SOURCES OF CONTINUED STRENGTH IN 1995

The incentives for American industry to cut costs and become ever more competitive in the world economy are extraordinarily strong — one of those crucial lessons learned the hard way. And that means continued strength in capital investment, in industrial equipment generally, and most especially in the kind of capital that reflects the latest in computer technology.

In total, real business fixed investment increased by 13 1/2 percent in 1994 and contributed more than 1 1/2 percentage points to that year's 4 percent gain in real GDP; even more than the 1.3 percentage points business fixed investment contributed to 1993's 3.1 percent gain in real GDP. The investment sector is forecast to continue to be strong and to contribute nearly 1.2 percentage points to 1995's growth rate, despite higher interest rates.

Total consumer purchases won't contribute as much to economic growth in 1995 as in 1994 as higher interest rates slice into the pace of spending on most big-ticket consumer durables. But purchases of nondurables and services — which alone comprise 57 percent of real GDP — are expected to rise about as much in 1995 as in 1993 and 1994 in response to job market stability and continued growth of household purchasing power. And this expected gain in consumer purchases of nondurables and services is enough to account for 1 1/2 percentage points of growth in real GDP.

In addition, the solid and sustainable expansion now being experienced by most of America's major trading partners will combine with the recent weakening of the U.S. dollar to contribute to a healthy pace of U.S. export growth during 1995 and 1996.

THE BOTTOM LINE: GROWTH AND INFLATION DURING 1995-96

Compared with the 4 percent growth rate now estimated for the economy for calendar 1994, the current forecast anticipates 3.3 percent growth of real GDP for 1995 to be followed by growth of just over 2 percent for 1996. This growth path is consistent with an aggregate unemployment rate holding steady at or near 5.6 percent during most of 1995 and then edging up to just under 6 percent during 1996.

The rate of industrial inflation, as measured by the private nonfarm output deflator, amounted to only 2 1/4 percent during 1994, and is forecast to edge up during the next two years, but to reach barely 3 percent during 1996. Consumer price increases will be moderate as well, running at about 3 1/2 percent by 1996, or a normal half point or so ahead of the pace of industrial inflation.

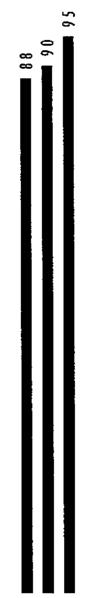
MAJOR UNCERTAINTIES IN THE OUTLOOK

The risks inherent in a persistently tight monetary policy are well known, and this analysis has argued that the private sector of the U.S. economy is strong enough to absorb the expected dimension of the disinflationary policy without going into recession.

There may well be even greater uncertainty connected with fiscal policy in 1995-96 than with monetary policy. The Clinton Administration managed to put in place a multi-year deficit-reducing fiscal policy in the summer of 1993. That policy has made a significant contribution, along with the strength of the economy, to the decline of the federal budget deficit from a rate near $300 billion (NIPA basis) when President Clinton took office, to about $165 billion at the end of 1994.

The political victory of the Republican Party in the November 1994 elections, however, gave the Republicans majority control of both Houses of the U.S. Congress and has placed fiscal policy under a cloud of uncertainty. It is certainly possible that a Republican-dominated fiscal policy could have major macroeconomic implications for the near- or intermediate-term economic outlook, but no such policy has been built into this forecast. Rather, the 1993 budget policy, amended only to include somewhat more spending on national defense approximately offset by somewhat less spending on entitlements and other transfer payments, has formed the fiscal policy basis of the current forecast. This may have microeconomic distributional implications, but it is a policy perturbation that is virtually neutral in macro terms. What develops on the fiscal front in the next year or two may very well be of this sort, but it need not be.

VIETNAM



94 95 96

REAL GDP/GNP

THE ECONOMY IN 1994

Despite the 14.4 percent rise of the CPI in 1994, the Vietnamese economy achieved high real growth with significant increases in investment, and the incremental capital-output ratio (ICOR) remained low. Even though the flood in the Mekong delta led to heavy losses in agriculture, the GDP of Vietnam in 1994 increased by 8.8 percent.

The GDP deflator was estimated to be 19.1 percent due to the variance of agricultural production. The State budget for 1994 accounted for 25.2 percent of GDP. Taxes and fees amounted to 22.9 percent of GDP, and the budget deficit was 3.6 percent of GDP. Exports increased by 21.1 percent in 1994, up from 15.1 percent in 1993.

THE FORECAST FOR 1995 AND 1996

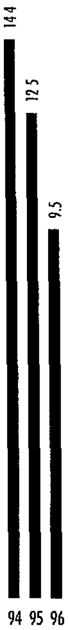
For 1995-1996, it is expected that investment will continue to rise sharply (especially for infrastructure development) and that inflation will be controlled. The growth of GDP is forecast to be 9 percent for 1995 and 9.5 percent for 1996. This rather good growth in GDP is largely attributable to the current payoff from previous investment in expanded capacity in the oil industry and in hydro-power generation. Total investment in 1995-1996 will be further enhanced by the state budget, ODA, and FDI, and by the rise of domestic savings resulting from incentives and encouragement provided by the government. Foreign trade should expand even faster, with annual growth in excess of 23 percent, export growth of 22-24 percent, and import growth of 24-25 percent. The GDP deflators for 1995 and 1996 will likely be lower than that of 1994, specifically 17.9 percent and 16.1 percent respectively. Associated with the decline of the GDP deflator will be changes in the structure of spending, and in the costs of investment inputs and consumer products.

Given the GDP growth rate and the infrastructure-oriented investment policy, the ICOR of the economy will likely rise rather rapidly during 1995-1996. For the period 1989-1994, the recorded ICOR was between 2.3 and 2.5. This low value was the result of three key factors. First, there were gains in efficiency brought about by previous investment in the oil industry, in hydro-power generation, and in cement production before 1989. Second, private investment was not yet fully counted. Finally, there was the expansion of labor intensive and service sectors. It is forecast that the ICOR will be 2.8 in 1995 and 2.9 in 1996. Investment is forecast to reach 25.2 percent of GDP in 1995 and 27.4 percent in 1996.

THE IMPACT OF TRADE

The growth of Vietnam's exports is mainly the result of the expansion of crude oil and rice. In 1994 Vietnam exported 2.3 million tons of rice, of which 300,000 tons were exported through border trade. However, the export of rice across the border will be controlled to stabilize its price in the domestic market. Expansion in textile and garment production will also contribute to Vietnamese exports. Tax exemptions applied to almost all export items will act as another stimulant to exports.

Import policies have been designed to permit imports of materials for investment. Also some liberalization will occur through the scrapping of quotas on most imports, encouraging the importation of materials for export production. The trade deficit is about US$700 million annually, and made possible by financing from ODA and FDI. The amount of ODA in 1995 is estimated at about US$800 million, which is part of the loan program from international financial organizations and institutions for investment in infrastructure.



CPI

The State budget is forecast to reach 25.2 percent of GDP in 1995 and 25.5 percent in 1996. Taxes and fees will also rise to 24.3 percent of GDP in 1995 and 24.7 percent in 1996. Recurrent expenditures will account for 17 percent and 17.3 percent of GDP, and the budget deficit 4.2 percent and 4.5 percent of GDP in 1995 and 1996, respectively. Financing the deficits depends mainly on borrowing. Domestic borrowing is forecast to be 1.5 percent of GDP in 1995 and 2.6 percent of GDP in 1996, and the remainder will come from foreign borrowing. Foreign borrowing is devoted entirely to investment.

During 1993-1994 the population increased slightly, and the population growth rate is forecast to be 2.2 percent in 1995 and 2.1 percent in 1996. This is in keeping with the target of containing the growth of population to under 2 percent early in the 21st century. With economic expansion in excess of 8 percent, and an annual increase of nearly 1 million people of working age, the total labor force in 1995 and 1996 will be 42.9 and 44 million people. The determination of an accurate unemployment rate is a matter of debate because a considerable part of Vietnamese labor is under-employed, and the labor market is unorganized (labor markets are now spontaneously formed in big cities).

TABLES

Table 1

FORECAST OF REAL ECONOMIC GROWTH AND INCREASE OF CONSUMER PRICES OF NINETEEN ECONOMIES, 1994-1996
(Percent)

	Real GDP/GNP			CPI		
	1994	1995	1996	1994	1995	1996
Australia	5.5	4.1	3.1	1.9	3.5	4.5
Canada	4.5	3.7	3.0	0.2	2.0	2.2
Chile	4.2	5.7	6.0	8.9	8.0	7.0
China	11.8	10.2	9.3	21.7	17.8	14.6
Colombia	5.7	5.2	4.5	22.6	18.0	15.8
Hong Kong	5.5	5.5	5.8	8.1	9.3	9.0
Indonesia	6.9	7.3	7.1	9.2	10.0	7.6
Japan	0.6	1.2	2.8	0.7	0.8	0.9
Korea	8.5	7.6	6.7	6.3	6.1	5.4
Malaysia	8.7	8.4	8.2	3.7	4.0	4.0
Mexico	3.5	-4.9	2.4	7.0	34.2	16.5
New Zealand	5.4	3.4	3.2	2.8	4.1	1.5
Peru	12.9	7.7	6.8	15.4	8.6	7.0
Philippines	4.3	5.2	6.1	9.2	6.5	5.0
Singapore	10.1	8.0	7.0	4.0	3.1	2.8
Chinese Taipei	6.5	7.0	6.9	4.1	3.9	3.5
Thailand	8.4	8.6	8.2	5.0	4.8	4.2
United States	4.0	3.3	2.0	2.1	2.5	3.2
Vietnam	8.8	9.0	9.5	14.4	12.5	9.5
Weighted Average ('89-'91)	4.7	4.1	4.0	3.9	4.6	4.1
Wt. Ave. Excl. U.S. and Japan	7.0	6.0	5.8	6.4	7.5	6.2
Wt. Ave. Excl. Latin America	4.7	4.3	4.0	3.6	3.9	3.8

The weighted average is based on the respective economies' exports during the period indicated.

Table 2

FORECAST OF REAL EXPORT AND IMPORT GROWTH OF PECC ECONOMIES, 1994-1996

(Percent)

	Export Growth			Import Growth		
	1994	1995	1996	1994	1995	1996
Australia	9.1	10.9	9.9	14.0	16.4	8.9
Canada	14.4	13.1	4.3	9.6	9.6	3.9
Chile	8.2	9.7	9.1	5.1	10.6	8.3
China	31.8	19.5	17.5	13.8	15.9	15.2
Colombia	3.3	12.0	4.3	14.6	12.7	5.0
Hong Kong	10.4	14.1	14.5	14.1	14.2	15.4
Indonesia	9.9	8.0	12.6	8.6	12.4	10.4
Japan	8.9	7.8	7.7	13.8	9.5	8.2
Korea	15.7	12.8	11.4	21.3	13.2	12.9
Malaysia	24.0	22.0	20.0	27.9	19.0	19.0
Mexico	17.2	16.0	15.1	21.4	-27.8	12.8
New Zealand	8.0	3.2	3.5	12.5	5.1	4.4
Peru	30.0	12.1	17.0	39.0	28.0	23.0
Philippines	19.5	18.5	18.0	17.9	15.8	15.5
Singapore	23.3	14.5	12.0	14.0	13.8	11.5
Chinese Taipei	9.4	8.1	7.1	10.8	7.0	7.0
Thailand	20.5	16.6	NA	16.5	15.0	NA
United States	9.0	12.7	9.0	13.5	11.4	8.2
Vietnam	21.1	22.2	23.5	31.2	24.5	25.0
Weighted Average	12.4	12.1	9.5	14.0	10.8	9.2
Wt. Ave. excl. U.S. and Japan	16.0	13.6	10.6	14.5	11.1	10.3
Wt. Ave. excl. Latin America	12.3	12.0	9.4	13.9	11.6	9.1

The weighted average is based on the respective economies' exports from 1989-1991.

Table 3

1994-1996 FORECAST OF CURRENT ACCOUNT BALANCE OF PAYMENTS

($US Billions and % of GNP)

	1994	% OF GNP	1995	% OF GNP	1996	% OF GNP
Australia	-14.8	-4.8	-18.5	-5.5	-16.9	-4.8
Canada	-24.8	-0.04	-16.9	-0.03	-12.2	-0.02
Chile	-0.8	-1.4	-0.7	-1.1	-1.2	-2.0
China	5.7	0.0	8.4	0.0	7.8	0.0
Colombia	-2.8	-4.6	-4.2	-6.2	-4.7	-6.4
Hong Kong	2.9	2.2	2.1	1.4	2.1	1.2
Indonesia	-3.8	-2.3	-4.6	-2.5	-4.4	-2.1
Japan	128.0	2.7	124.5	2.4	130.2	2.5
Korea	-0.05	0.0	-0.05	0.0	-0.06	0.0
Malaysia	-4.5	-6.6	-3.5	-4.4	-2.4	-2.8
Mexico	-29.6	-7.8	-0.2	0.0	-17.1	-5.4
New Zealand	-1.3	-2.6	-0.9	-1.5	-0.9	-1.5
Peru	-2.3	-4.6	-3.8	-6.3	-4.7	-6.8
Philippines	-2.4	-5.2	-3.0	-3.8	-2.7	-3.2
Singapore	2.9	3.9	2.5	3.3	2.2	2.6
Chinese Taipei	6.0	2.6	5.7	2.1	5.4	1.8
Thailand*	-8.1	-6.0	-8.8	-5.6	-8.8	NA
United States	-140.4	-2.1	-145.4	-2.0	-139.1	-1.9
Vietnam	-0.5	NA	-0.6	NA	-0.65	NA
Total	-90.5		-67.4		-67.5	
Total excl. U.S. and Japan	-78.2		-46.5		-58.6	
Total excluding Latin America	-55.1		-58.5		-39.8	
Weighted Average		-0.3		-0.2		-0.2
Wt. Ave. Excl. U.S. and Japan		-0.5		-0.4		-0.4
Wt. Ave. Excl. Latin America		-0.1		-0.2		0.0

** The figure for 1996 is not a forecast. It has been inserted to permit consistency.*

The weighted average is based on the respective economies' exports from 1989-1991.

Table 4

FORECAST OF CONTRIBUTIONS TO REAL GDP/GNP GROWTH RATE, 1994-1995

(Percent per year)

		GDP Growth Rate	Personal Con. Exp.	Gross Pte Dom. Invt.	Govt. Purch.	Net Exports
Australia	1995	4.1	2.6	1.8	0.6	-0.9
	1996	3.1	2.2	-0.2	0.8	0.2
Canada	1995	3.4	1.8	0.8	-0.2	1.1
	1996	3.3	1.8	1.2	-0.1	0.4
Chile	1995	5.7	3.8	2.3	0.4	-0.8
	1996	6.0	3.5	2.2	0.4	-0.1
China	1995	10.2	NA	NA	NA	NA
	1996	9.3	NA	NA	NA	NA
Colombia	1995	5.2	2.5	1.5	1.1	0.1
	1996	4.5	3.3	1.0	1.5	-1.4
Hong Kong	1995	5.5	3.6	2.4	0.4	-0.8
	1996	5.8	4.2	3.5	0.4	-2.3
Indonesia	1995	7.3	2.8	2.9	0.0	1.6
	1996	7.1	3.0	3.2	0.0	0.9
Japan	1995	1.2	1.0	0.0	0.2	0.0
	1996	2.8	1.7	0.5	0.6	0.0
Korea	1995	7.6	NA	NA	NA	NA
	1996	6.7	NA	NA	NA	NA
Malaysia	1995	8.4	2.0	2.8	1.9	1.7
	1996	8.2	2.0	2.8	1.7	1.7
Mexico	1995	-4.9	NA	NA	NA	NA
	1996	2.4	NA	NA	NA	NA
New Zealand	1995	3.4	1.7	2.3	0.1	-0.1
	1996	3.2	1.8	0.9	0.1	0.2
Peru	1995	7.7	3.0	4.6	0.5	-0.4
	1996	6.8	2.7	3.8	0.4	-0.1
Philippines	1995	6.0	NA	NA	NA	NA
	1996	6.5	NA	NA	NA	NA
Singapore	1995	8.0	1.5	2.3	0.1	4.1
	1996	7.0	1.3	2.0	0.1	3.6
Chinese Taipei	1995	7.0	4.4	2.2	-0.2	0.7
	1996	6.9	4.8	2.0	-0.1	0.2
Thailand	1995	8.6	NA	NA	NA	NA
	1996	8.2	NA	NA	NA	NA

(Continues next page)

Table 4 (Continued)

FORECAST OF CONTRIBUTIONS TO REAL GDP/GNP GROWTH RATE, 1994-1995

(Percent per year)

		GDP Growth Rate	Personal Con. Exp.	Gross Pte Dom. Invt.	Govt. Purch.	Net Exports
United States	1995	2.6	1.4	1.0	0.1	0.2
	1996	2.0	NA	NA	NA	NA
Vietnam	1995	9.0	5.9	1.6	2.6	-0.8
	1996	9.5	5.9	1.8	2.7	-0.9

For China, private consumption and investment statistics net of government are not available.

Some figures may not add up exactly because of rounding errors and statistical discrepancies.

Appendix Table 1

SHARE OF EXPORTS AND IMPORTS WITH PECC ECONOMIES

(As a % of Total)

	Exports to PECC Economies			Imports from PECC Economies		
	1970	1992	1993	1970	1992	1993
World	33.0	40.9	34.1	36.2	42.9	32.6
PECC	57.0	69.7	72.4	62.0	70.4	72.0
Australia	61.1	73.1	73.9	50.0	66.2	69.5
Brunei Darussalam	99.5	90.6	78.5	85.5	72.1	67.9
Canada	71.0	87.9	90.6	76.1	79.1	82.0
Chile	28.6	50.4	51.8	46.0	44.4	45.3
China	55.3	76.8	73.1	51.8	66.9	70.6
Colombia	44.7	50.7	51.1	60.2	62.0	54.3
Hong Kong	61.1	73.0	75.0	68.5	85.1	84.9
Indonesia	80.5	79.0	77.2	66.7	68.4	65.9
Japan	62.6	67.8	71.7	60.6	64.5	66.9
Korea	85.5	71.4	69.1	81.8	69.6	68.2
Malaysia	68.8	77.4	78.2	65.2	79.9	81.5
Mexico	66.8	87.1	88.9	69.5	81.9	81.3
New Zealand	43.5	70.7	69.0	51.1	70.9	70.6
Peru	50.7	56.3	55.2	55.7	59.6	60.9
Philippines	89.8	77.6	76.6	75.0	72.9	75.0
Singapore	59.9	71.9	75.6	69.2	74.4	79.6
Chinese Taipei	77.0	75.2	93.2	81.9	73.6	77.8
Thailand	67.7	65.8	67.8	64.4	71.8	70.1
United States	46.1	59.5	61.1	56.7	66.2	67.5
Vietnam	NA	73.6	72.6	NA	86.2	85.8

NA not available

Source: Compiled by the East-West Center (Honolulu) 1970, 1992;

Direction of Trade Statistics Yearbook 1994;

The Central Bank of China, Balance of Payments Taiwan District, Republic of China, December 1994.

Appendix Table 2

DIRECT INVESTMENT FROM AND INTO PECC ECONOMIES

(Millions of US dollars)

		1988	1989	1990	1991	1992	1993
Australia	*Outflow*	5,072	3,319	931	2,512	-81	668
	Inflow	8,013	7,770	6,884	4,772	5,299	2,708
Canada	*Outflow*	3,855	4,587	4,725	5,857	3,650	7,155
	Inflow	6,426	5,029	7,855	2,906	4,637	5,923
Chile	*Outflow*	NA	10	8	123	378	431
	Inflow	141	1,289	590	523	699	841
China	*Outflow*	850	780	830	913	4,000	-4,400
	Inflow	3,194	3,393	3,487	4,366	11,156	27,515
Colombia	*Outflow*	44	29	16	24	50	240
	Inflow	203	576	500	457	790	994
Indonesia	*Outflow*	*	*	*	*	*	*
	Inflow	576	682	1,093	1,482	1,777	2,004
Japan	*Outflow*	34,210	44,160	48,050	30,740	17,240	13,740
	Inflow	-520	-1,060	1,760	1,370	2,720	100
Korea	*Outflow*	151	305	820	1,357	1,047	1,056
	Inflow	871	758	715	1,116	550	516
Malaysia	*Outflow*	*	*	*	254	420	969
	Inflow	719	1,668	2,332	3,998	5,183	5,206
Mexico	*Outflow*	*	*	*	*	*	*
	Inflow	2,011	2,785	2,549	4,742	4,393	4,901
New Zealand	*Outflow*	152	1,791	588	44	22	NA
	Inflow	441	1,365	419	682	70	NA
Peru	*Outflow*	*	*	*	*	*	*
	Inflow	26	59	41	-7	127	349
Philippines	*Outflow*	*	*	*	*	*	*
	Inflow	936	563	530	544	228	763
Singapore	*Outflow*	117	882	1,570	444	748	767
	Inflow	3,655	2,887	5,575	4,888	6,730	6,829
Chinese Taipei	*Outflow*	4,120	6,951	5,243	1,854	1,869	2,451
	Inflow	959	1,604	1,330	1,271	879	917
Thailand	*Outflow*	24	50	140	167	-147	-221
	Inflow	1,105	1,775	2,444	2,014	2,116	1,715
United States	*Outflow*	15,450	36,832	29,951	31,295	41,005	57,871
	Inflow	57,270	67,730	47,918	26,089	9,888	21,366
Vietnam	*Outflow*	*	*	*	*	*	*
	Inflow	366	539	596	1,288	1,939	2,928
Total	*Outflow*	64,045	99,696	92,872	75,584	70,201	80,727
	Inflow	86,392	99,412	86,618	62,501	59,181	85,575

* *indicates less than US$ 1 M.*

NA data not available; Hong Kong does not provide figures for direct investment.

Sources: International Monetary Fund (New York), Balance of Payments Statistics Yearbook, 1994; Council for Economic Policy Development (Taipei), Taiwan Statistical Data Book, 1992; Bank of China, Economic Review, country reports.

Appendix Table 3

NUMBER OF TOURIST ARRIVALS IN PECC ECONOMIES

Thousand Persons

	1989	1990	1991	1992	1993	1994
Australia	2,080	2,215	2,227	2,520	2,996	3,359
Canada	15,111	15,258	15,291	14,741	15,038	NA
Chile	797	933	1,330	1,052	1,357	1,544
China*	1,461	1,747	2,710	4,006	4,753	5,013
Colombia	829	733	813	887	1,017	1,096
Hong Kong	5,985	6,581	6,795	8,011	8,938	9,331
Indonesia	1,134	2,178	2,558	3,004	3,363	4,006
Japan	2,835	3,236	3,533	3,926	3,747	3,785
Korea	2,407	2,959	3,196	3,244	3,300	NA
Malaysia	3,954	7,477(v)	5,543	6,010	6,503	7,200
Mexico**	66,898	69,789	82,755	84,060	83,016	NA
New Zealand	901	976	964	1,056	1,157	1,323
Peru	334	317	232	201	296	NA
Philippine	1,076	893	961	1,372	1,562	NA
Singapore	4,830	5,323	5,415	5,990	6,426	6,899
Chinese Taipei	2,004	1,934	1,855	1,873	1,850	2,127
Thailand	4,810	5,299	5,087	5,136	5,761	NA
United States	30,673	28,688	42,723	45,405	45,650	NA
Vietnam	NA	250	300	440	720	1,018

* *Figures for China do not include overseas Chinese visitors due to the high volume of Hong Kong residents making frequent cross-border trips.*

** *Including visitors to the border zone with the U.S. who stayed less than 72 hours.*

(v) *"Visit Malaysia" year.*

Sources: World Tourism Organization (New York); various country reports.

Appendix Table 4

EXPORT WEIGHTS 1989-1991 AVERAGE

	All Countries	Excluding U.S. & Japan	Excluding Latin America	Excluding U.S., Japan & Latin America
Australia	2.96%	6.13%	3.06%	6.58%
Canada	9.38%	19.40%	9.70%	20.84%
Chile	0.65%	1.35%		
China	4.72%	9.76%	4.88%	10.48%
Colombia	0.50%	1.03%		
Hong Kong	6.38%	13.19%	6.60%	14.17%
Indonesia	1.93%	3.99%	2.00%	4.29%
Japan	22.04%		22.80%	
Korea	4.94%	10.23%	5.12%	10.99%
Malaysia	2.23%	4.62%	2.31%	4.96%
Mexico	1.94%	4.01%		
New Zealand	0.70%	1.45%	0.72%	1.56%
Peru	0.25%	0.52%		
Philippines	0.62%	1.29%	0.64%	1.38%
Singapore	3.94%	8.15%	4.07%	8.75%
Chinese Taipei	5.23%	10.82%	5.41%	11.63%
Thailand	1.81%	3.75%	1.87%	4.02%
United States	29.62%		30.64%	
Vietnam	0.15%	0.31%	0.16%	0.33%
Total	100.00%	100.00%	100.00%	100.00%

Appendix Table 5

HUMAN RESOURCES

	1992				1993			
	Population Growth Rate	Fertility Rate*	Labor Supply Growth Rate	Female Particip. Rate**	Population Growth Rate	Fertility Rate	Labor Supply	Female Particip. Rate
Australia	1.4	1.8	1.1	51.9	1.4	1.8	0.7	51.8
Canada	1.2	1.7	0.3	57.6	1.1	1.71	1.1	57.5
Chile	1.6	2.6	4.1	31.8	1.6	2.6	4.6	33.8
China	1.2	1.8	1.6	47.8	1.2	1.8	1.3	48.7
Colombia	1.7	2.7	-0.2	38.0				
Hong Kong	1.0	1.3	0.2	46.2	1.8	1.2	2.9	46.5
Indonesia	1.6	2.9	3.1	40.0	1.66	2.91	3.05	40.2
Japan	0.3	1.8	1.1	50.7	0.32	1.78		42.6
Korea	0.9	1.6	2.0	47.3				
Malaysia	2.4	3.3	2.3	47.6	2.3	3.4	3.5	46.1
Mexico				21.6				
New Zealand	1.0	2.1	0.9	54.6	1.1	2.1	1.7	54.5
Peru			0.4	43.5				
Philippines			6.4	47.8				
Singapore	1.9	1.6	1.0	51.3	2.0	1.8	1.0	50.6
Chinese Taipei	1.0	1.7	2.3	44.8	0.9	1.76	1.24	44.9
Thailand	1.5	2.2	2.4	71.6				
United States	1.1		1.3	56.0				
Vietnam	2.4	3.1	2.7	51.3	2.3	2.9	2.8	51.3

* *total fertility rate (births per woman)*

** *adult females aged 18-64, except Colombia where it is females aged 15-64*

Sources: Social Indicators of Development, 1993 (New York: World Bank); Yearbook of Labor Statistics, various years, Taiwan Statistical Data Book.

Appendix Table 6

FINANCIAL MARKETS

Country (Stock Index)	Short-term Interest Rates (a) 1993	Short-term Interest Rates (a) 1994	Long-term Interest Rates (b) 1993	Long-term Interest Rates (b) 1994	Stock Index (year-end) 1993	Stock Index (year-end) 1994	% Change	Exchange Rates (year-end, US$ in local currency) 1992	Exchange Rates 1993	Exchange Rates 1994
Australia (All Ords.)	4.8	7.9	6.6	10.10	2,173.60	1,912.7	-12	1.45	1.47	1.288
Canada (Composite)	4.1 (c)	6.1 (c)	8.2 (c)	10.0 (c)	4,321.43	4,213.61	-2.5	1.26	1.32	1.4042
Chile (40-Share)	6.5	6.1	6.4	5.9	168.73	256.98	52.3	370.50	418.11	420.3
China (Shanghai, Standard)	10.4	9.5 (d)	11.2	13.4 (d)	86.81	NA	NA	5.84	5.81	8.4462
Colombia (Closing)	24.0	29.5 (m)	27.8	30.5 (n)	749.44	889.91	18.74	618.80	682.30	829.95
Hong Kong (Hang Seng)	3.6	6.31	4.7	8.0	11,888.39	8,191.04	-31.1	7.74	7.73	7.7385
Indonesia (Composite)	10.7 (e)	NA	11.5 (f)	NA	588.77	469.64	-20.23	2063.50	2103.01	2190.5
Japan (Nikkei)	2.2	2.3	4.4	NA	17,417.24	19,723.06	13.24	124.80	111.60	99.8
Korea (Composite)	12.0 (g)	14.5 (h)	12.2 (i)	13.5 (j)	866.18	1,027.37	18.61	786.40	808.40	789.6
Malaysia (Composite)	5.2	4.5	7.0	7.5	1,275.32	971.21	-23.85	2.61	2.62	2.563
Mexico (IPC)	11.7	17.5 (h)	NA	NA	2,602.63	2,375.66	-8.72	3.12	3.11	4.875
New Zealand (NZSE-40)	5.0	9.0	5.8	8.9 (j)	2,188.07	1,914.24	-12.51	1.95	1.79	1.557
Peru (IGBUL)	28.6	16.1 (k)	NA	NA	898.00	NA	NA	1.56	2.06	2.195
Philippines (Composite)	15.9	10.7	NA	NA	3,196.08	2,785.81	-12.84	25.51	27.68	24.4
Singapore (STII)	3.7	4.4 (h)	NA	NA	2,425.68	2,239.56	-7.67	1.64	1.60	1.465
Chinese Taipei (Weighted)	5.6	NA	6.9	NA	6,070.56	7,111.10	17.14	25.40	26.36	26.33
Thailand (SET)	4.4 (l)	NA	10.8	NA	1,682.85	1,360.09	-19.18	25.49	25.48	25.1
U.S. (Dow Jones Indust.)	3.1	5.6	6.3	7.7	3,754.07	3,834.44	2.14	NA	NA	NA
Vietnam	0.8	0.7	1.7	1.7	NA	NA	NA	NA	5.60	3.50

PEO Equity Portfolio of PECC Stocks (weighted by 1989-91 share of exports)

NA indicates data not available.

(a) Short-term interest rates refer to 90-day/3-month Treasury Bills; year-end.

(b) Long-term interest rates refer to secondary market yields on bonds of seven years or longer; year-end.

(c) Fourth quarter averages. (d) Annual average, short-term rates, less than one year; long-term rates more than one year. (e) 3 month time deposit rate. (f) 12 month time deposit rate. (g) One year monetary stabilization bond. (h) Money market rate. (i) Three year corporate bond. (j) Government bond. (k) Discount rate. (l) Weighted average for December. (m) 90-day CDT, annual average. (n) 360 day CDT, annual average.

Sources: Barron's National Business and Financial Weekly (New York), Jan. 2, 1995; Wall Street Journal, Jan. 3, 1995; Yearbook of Financial Statistics; various country reports.

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