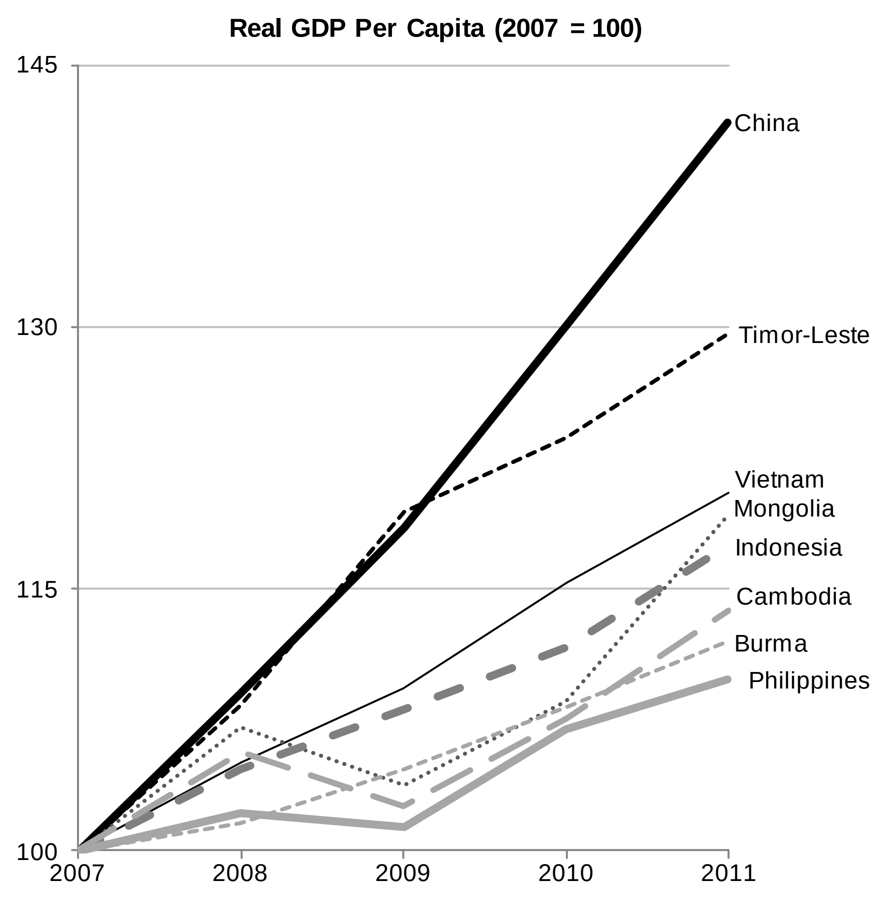
USAID
Economic Analysis
and Data Services

EADS Economic Trends Report
East Asia

October 2011

Economic Overview

Economic growth remains strong in East Asia and retains healthy momentum thanks to strong commodity prices and increases in exports. China leads the region in growth and its GDP is expected to rise 9.5 percent in 2011 and 8 percent in 2012. This growth rate is a slowdown from its 2010 growth of over 10 percent, but still leads the region. Indonesia and Vietnam are also expected to produce strong growth rates about 6 percent for 2010–2012. The rest of the region presents mixed, but generally positive growth around 5 to 6 percent. GDP per capita was slightly lower in 2009 in most countries, but has recovered to its 2008 levels and continues to rise.



SOURCE: IMF, *World Economic Outlook*, September 2011.
NOTE: Data for 2011 are IMF projections.

East Asia managed to weather the global recession by relying on export-oriented growth, particularly strong commodity exports and mining investment, as well as targeted fiscal stimulus by individual countries. These factors were aided by increased regional demand for exports and private domestic demand in each country. Healthy consumer confidence in China has allowed retail sales to grow at double-digits. Fiscal policy remains expansionary, with Vietnam being one of the few countries to begin to remove its fiscal stimulus.

The IMF reports that the prospects of continued growth have increased and for East Asia concerns remain regarding the sustainability of domestic demand and the region's export oriented economy. The export trade has, and will continue to be, the source of the region's economic growth. However, the countries in East Asia are susceptible to overheating, slowdowns in advances economies, unemployment problems and food and commodity price shifts that could hamper the sustainability of growth.

China's Growing Economy

In 2010, China passed Japan to become the second largest economy in the world with a GDP of $3.243 trillion (in constant USD).

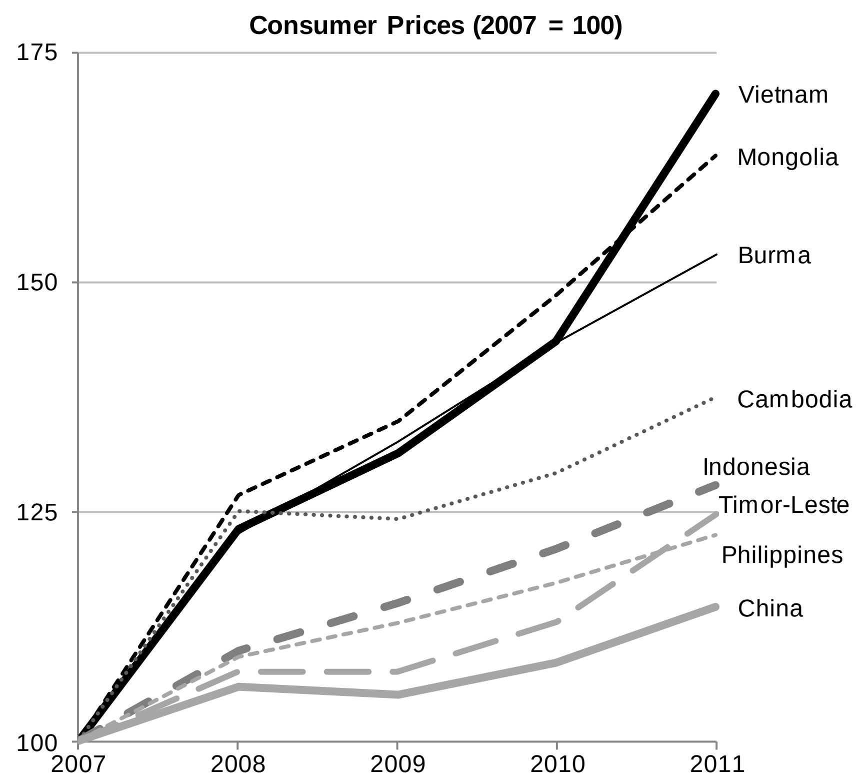
East Asian countries included in this Report are Burma, Cambodia, China, Indonesia, Mongolia, Philippines, Timor-Leste, and Vietnam. Because of limitations on data, not all countries are included in every graph or narrative section.

Unrest in the Middle East could put upward pressure on oil prices and while the effects on East Asia have thus far been minimal, the region could see intense effects if price shocks cause a global slowdown. Additional problems in the euro area could cause growth problems since they are a destination for many of East Asia's exports.

Selected Real GDP Growth Rates, 2010	China 10.3%	Indonesia 6.1%	Vietnam 6.8%

Inflation and Exchange Rates

East Asia's economic growth is threatened by the potential for overheating. One sign of this potential is inflation rates across the region. According to the IMF, inflation in East Asia accelerated in 2010 due to higher commodity prices and inflation is expected to increase in 2011 before declining in 2012. Consumer inflation has been particularly problematic in Vietnam and Mongolia, where inflation has been over 10 percent.



SOURCE: IMF, *World Economic Outlook*, September 2011.
NOTE: Data for 2011 are IMF projections.

Headline inflation has been particularly high in Indonesia and Vietnam. These increases were due primarily to increases in food and energy prices. China is also experiencing inflationary pressures due to food prices and this inflation has raised fears of the economy overheating.

While China's inflation rate was 8 percent for December 2010 and January 2011, the IMF believes it is premature to classify China's economy as overheating. Most of the inflation, roughly 70 percent, is related to pass throughs from food price increases. Inflation is also expected to return to low single digits for China during the second half of 2011.

Exchange rate appreciations can be a method for East Asian economies to deal with potential overheating. According to the IMF, most currency exchange rates remain relatively unchanged from precrisis levels, with Vietnam actually seeing its exchange rate depreciate significantly.

Consumer Price Inflation for Selected Countries (IMF Projections for 2011)	China 3.3%	Mongolia 10.2%	Vietnam 9.2%

Fiscal and Monetary Policy

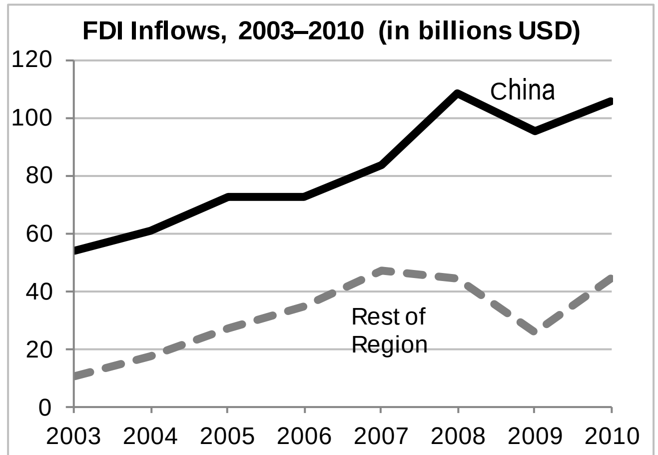
Pro-cyclical monetary policy was also a source for inflationary concerns in the region. Looser monetary policy has led the IMF to recommend tighter policies to address inflation and as a preventative against overheating.

The stabilization of global commodity prices and concurrent tightening of monetary policy are expected to forestall increased problems from inflation. However, risks remain if countries do not seek to end temporary measures from the global economic crisis. Vietnam responded to the global recession by cutting its prime interest rate and with fiscal stimulus. While the fiscal stimulus has been removed, Vietnam continues to practice a looser monetary policy that could have negative effects on its currency and increase inflation in the future.

Real policy rates are negative in China and lower than normal in Indonesia and the IMF is concerned that allowing rates to remain negative could lead to fiscal instability. Changes to real interest rates should be combined with measures such as fiscal tightening in Cambodia and Mongolia as well as exchange rate appreciation in Vietnam.

Foreign Investment

East Asia remains a popular destination for foreign direct investment. 2010 saw an increase in FDI, effectively bringing it back to 2008 levels in the region. FDI inflows to the region are expected to continue their growth in the future. However, not all countries saw returns to pre-crisis levels of FDI and FDI is unevenly distributed throughout East Asia.



SOURCE: UNCTAD, *Foreign Direct Investment*, 2011.

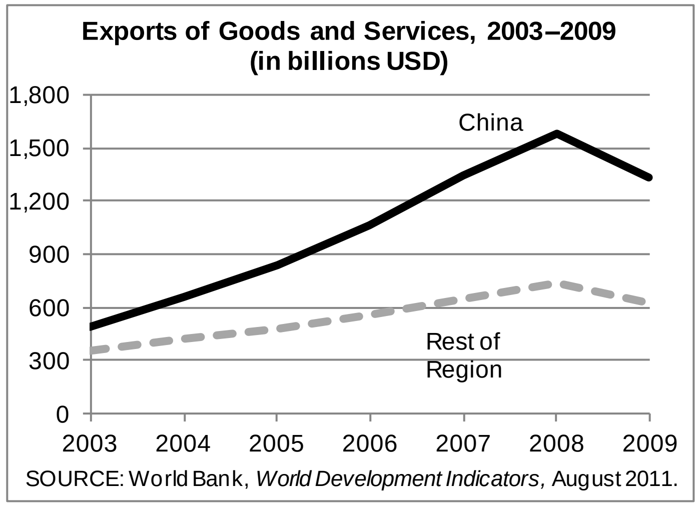
China remains the top FDI recipient in the region and received more than twice the total FDI of the next five recipients combined. China also received twice as much FDI as all countries in East Asia that received USAID assistance in 2009 combined. Despite this continued increase, the entire region did see a decline in FDI in 2008 and 2009 from the global recession and is just beginning to recover its 2007 levels of investment.

Cambodia, Indonesia, and the Philippines all pursued policies to increase the favorability of FDI. All three liberalized industries, Indonesia improved its FDI administrative procedures and the Philippines strengthened support for public private partnerships. Vietnam increased its competiveness in low-cost productions and manufacturing to lure more FDI.

The region is also increasing its FDI outflows, primarily focusing on other East Asian countries and resource rich countries outside the region. According to UNCTAD, in 2010 China surpassed Japan for the first time in outward FDI. Outflows from the region have been increasing and only suffered minor setbacks in 2008. China's demand for energy has been a major factor in its continued increase in outward FDI flows.

FDI for Selected Countries, 2009–2010 (percent change)	China +11.3%	Indonesia +172.8%	Philippines -12.7%

Trade

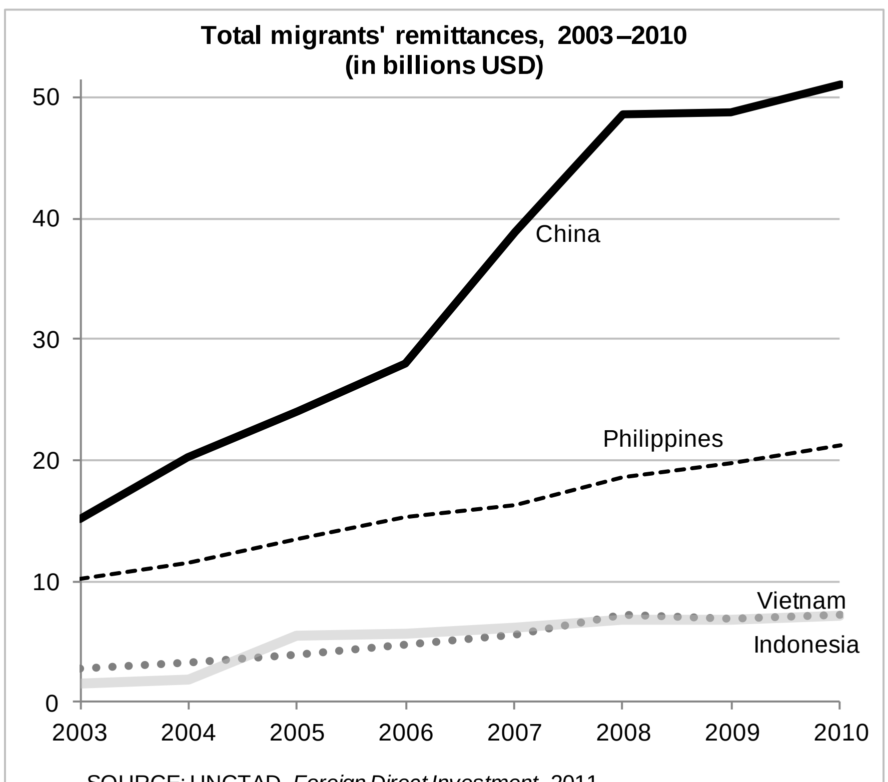


Many of the economies of East Asia are export oriented. China still dominates the region for exports, but there was a slight downturn due to the global recession. Previously, the region's exports were aimed toward developed economies, but that trend is changing.

Developing and emerging economies are becoming more of a destination for East Asian goods. China is also become a recipient of more of the region's exports. The IMF states that these changes represent recovery in both the trade in intermediate goods and the emergence of China as a source of demand.

Exports in East Asia are expected to be boosted by demand for intermediate goods and foreign investment in advanced and emerging economies. However, continued growth in exports for the region is threatened by a potential global slowdown from higher oil prices and dangers in the euro area. China has become a hub for the assembly of final goods and is a large market for the region's exports. The increase in inter-regional trade could insulate East Asia from downturns in advanced economies, but increases in oil and commodity prices still pose risks to growth.

Poverty Reduction



While East Asia has managed to produce impressive growth and continued to increase its exports and FDI, poverty and rising inequality remain an issue. One positive source of poverty reduction comes from remittances. Even with the global recession, remittances to many East Asian countries remained strong and the Philippines did not see the leveling off or slight decline that occurred in Vietnam or China.

While employment for many citizens in foreign countries has contributed to economic growth and poverty reduction, employment in East Asian countries remains tenuous. Employment has grown in the region, but youth unemployment remains high. The number of workers in vulnerable employment, such as unpaid family or casual workers, grew in Indonesia in 2009 and only partially declined in 2010. This trend combined with rising income inequality and social exclusion can make the benefits of economic growth fragile and remains a concern for East Asia.

The reduction of the number of people in East Asia in poverty has been impressive, but it has been paired with an increase in income inequality, particularly in China. Inequality has also risen in Vietnam, Cambodia and Indonesia. Gini coefficients for China and the Philippines are the highest in the region, at 48.2 and 45 percent, respectively. The poor in Vietnam, Indonesia, Cambodia and the Philippines also have less access to basic health services and education.

Large income disparities in the Philippines and Cambodia, where the wealthiest 20 percent out earn and out spend the poorest 20 percent by more than five times. These disparities can be a source of a decline in social cohesion and fuel social unrest. The rise in income inequality in China has already started to dampen poverty reduction efforts and could lead to conflict between the poor and non-poor.

Additional Information

For country-specific data and additional information about the countries covered in this report, please visit the EADS Country Portal at http://esdb.eads.usaidallnet.gov/query/do?_program=/eads/esdb/countryPortal.

Sources used in compiling this report include the semi-annual World Economic Outlook from the International Monetary Fund (http://www.imf.org/) and the Global Economic Prospects from the World Bank (http://www.worldbank.org/).