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GLOBAL ECONOMIC TRENDS AND PROSPECTS

A note by the UNCTAD secretariat

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A. Introduction

After attaining the highest growth rate in 2000 for more than a decade, the world economy experienced a sharp downturn over the last quarter of 2000 and into the new year. The principal factors behind this reversal and near-term economic prospects were examined in *Trade and Development Report, 2001*, issued in April, on the basis of preliminary data available for the first quarter of 2001. Based on an analysis of underlying imbalances and fragilities in the world economy, the UNCTAD secretariat argued that without a coordinated global policy response, the slowdown in the United States would produce a synchronous cyclical downturn in the world economy. Rather than a rapid rebound, the United States economy could experience a prolonged period of sluggish growth which even quick conventional policy actions might be unable to remedy. The *Report* also suggested that even Europe could be much more vulnerable to the slowdown in the United States than was generally expected by policy makers in the region, and without a determined change in economic policy, European growth would fall substantially below the 3 per cent experienced in the previous year. Similarly, without more aggressive measures designed to reverse persistent deflation, Japan's recovery remained highly fragile. If all these risks became reality, there would be a sharp deterioration in the external trading environment of developing countries, many of which were struggling to re-establish conditions for rapid and sustained growth after recent bouts of financial crisis. While some emerging markets were expecting to improve their performance as a result of lower United States interest rates and a weaker dollar, these benefits could be easily wiped out by reassessment of risks, rising risk spreads and falling capital inflows brought about by slowdown in global growth and a further round of uncertainty.

Already on the eve of events of 11 September, global economic conditions had been deteriorating over a year. The decline in the pace of demand in the first half of 2001 had been sharper than expected and for the first time since the late 1970s much of the world economy was simultaneously experiencing slower growth (table 1). The slowdown in the major industrial countries had begun to affect the rest of the world through trade and financial linkages, and many economies in Asia and Latin America were confronting recessionary pressures. Until the events of September 11, however, policy makers in most major industrial countries were reluctant to adopt a coordinated approach to stabilizing and reviving the world economy. But the recent events that have made possible such a coordinated macroeconomic policy response have also made the world economy more fragile and unpredictable.

The aim of this note is twofold. First, to update the analysis of the underlying trends given in *TDR 2001* earlier in the year. Second, to discuss the possible implications of the events of 11 September for the world economy, and to make an assessment of the policy responses in the major industrial countries and what more could be done at the global level in order to alleviate the increased difficulties that are now likely to be faced by a large number of developing countries.

B. Underlying trends

1. Major industrial countries

Before recent events, the slowdown in the United States economy was clearly visible and the hopes of a quick rebound appeared less likely than an extended phase of slow growth. Growth in the second quarter was only 0.3 per cent at an annual rate, and this positive growth was made possible by rising consumer spending and residential investment in the face of a huge drop in gross fixed investment and an inventory drag in the manufacturing sector.

As is usual in a cyclical downturn, much of the adjustment burden has been born by profits. Company earnings that had been boosted to unprecedented levels during the prolonged boom in the late 1990s dropped sharply after the cyclical peak reached in mid-2000. Manufacturing activity slackened from the middle of last year when high interest rates, a sharp stock market sell-off and the overvaluation of the dollar began to reinforce the effects of slowing domestic demand. Investment in machinery and business construction collapsed in the high technology sector that had been the major source of demand expansion. However, the reduction of the employed workforce lagged. Total employment did shrink in the second quarter of 2001, and the unemployment rate rose in August as gains in services and the withdrawal of over half a million from the active labour force no longer compensated for the shedding of labour in manufacturing industry. Real disposable personal income held up well in the first phase of the downturn. Compensation of employees, which had been on a steeply rising trend in the second half of the 1990s resulting in a growth rate of more than 7 per cent in nominal and 5 per cent in real terms in 2000, remained high in the first half of 2001 despite the sudden drop in economic activity. Paradoxically, although unit profits suffered from the stickiness of wages, aggregate profits benefited as consumers continued to spend more than their income.

The United States economy has continued to be affected by disequilibria which threaten the prospect of a speedy return to vigorous expansion. Private savings are low and debt levels high for many households, both factors unfavourable to sustained consumer spending. The excess capacity created by the Schumpeterian wave of "new economy" investments has been largely eliminated through bankruptcy, but despite the declines in asset values the process of balance-sheet restructuring in the rest of the economy is by no means complete. The United States economy is still characterised by a large deficit in the current account of its balance of payments and a rapid accumulation of external liabilities, factors which continue to make the dollar vulnerable.

During the first half of 2001 the Federal Reserve demonstrated its willingness to act aggressively at the first sign of weakening growth. With the headline inflation rate at 3 ½ per cent but few underlying inflationary dangers visible the policy rate of interest was cut in seven steps from 6 ½ per cent in May 2000 to 3 ½ per cent in August 2001. As a result money market rates have fallen almost to the level of the inflation rate, so that real short-term interest rates are close to zero. Moreover, despite some volatility earlier in the year and a budget surplus about $30 billion less than the expected $150 billion, the long-term bond yield had also come down, and in August the 10-year Treasury Bond yield fell below the comparable European rate, even though the expected medium-term inflation and growth rates were higher in the United States.

Growth and employment in the European Union continued to depend heavily on the spillovers from booming world trade and rising market shares due to the undervaluation of the Euro. As export demand faltered and real interest rates rose, growth proved to be much less robust than policy makers in continental Europe were projecting a year ago. GDP growth actually stagnated in the second quarter of 2001 and progress in reducing unemployment, which dropped between 1997 and 2000 from 11.5 per cent to 8.5 per cent, came to a halt. Indeed, conditions in the labour market deteriorated with unemployment rising and vacancies falling in most of the bigger economies.

As of the beginning of 2001 continental Europe enjoyed certain advantages which could have helped avoid a drag on its economy due to the slowdown in the United States. For example, risk premia in financial markets were lower and consumer expenditure was less vulnerable to declines in stock prices owing to lower shares of equities in household wealth. Even the adverse effects on households' purchasing power of the rise in oil prices in 2000 had been partly offset by the additional import demand of oil-exporting countries. However, if continental Europe were to benefit fully from these advantages, forceful action in support of expansion would be required on the fiscal and monetary fronts. Such action was not forthcoming.

Fiscal policy was designed to avoid any impact from tax cuts on budget deficits, and public expenditure was trimmed accordingly, thereby countering the positive effects of the tax cuts on demand and profits. The Stability and Growth Pact required governments to pursue deficit targets with too little regard to the cyclical position. Discretionary fiscal action to stabilize the economy, such as advancing the introduction of tax cuts, was ruled out by the Commission and the European Council. Monetary policy has also exerted a restrictive influence. With the core inflation rate and unit labour costs low and second round effects on wages from the oil price hike absent, monetary policy in Europe could have acted to counter the negative demand spillovers from global markets. This was the classical case of a common external shock, in response to which a common monetary policy response should have been sufficient to stabilize the economy without violating inflation targets. The European Central Bank (ECB), however, was reluctant to cut policy rates as aggressively as the Federal Reserve, and the current slowdown suggests that its stance was too restrictive.

Europe has been more affected by the global slowdown than generally expected. As pointed out in *TDR 2001*, the weight of sales of affiliates of European firms increased during the 1990s, so that lower sales to the United States have had a direct impact on the profitability of European corporations. Thus the relatively low share of trade in Europe's GDP does not accurately reflect its exposure to the world economy. Moreover, private consumption in the larger European economies has remained flat because employment growth has stalled and the higher inflation rate has eaten into real income per employee. Wage agreements in the second half of the 1990s in the European Monetary Union have led to moderate increases in remuneration. The growth rate of nominal compensation per employee in the 11 founding members of EMU was below 2 per cent between 1996 and 2001, and real compensation has hardly grown at all.

The experience of the United Kingdom in 2001 resembles more closely that of the United States than that of the EMU economies. After an extended boom and a return to high level of employment, the country has managed to limit the slowdown of growth more than any other major industrialized economy. Overall unemployment has been falling, and inflation is low if the one-off effects of oil price rises and soaring house prices are discounted. Nevertheless, the monetary authorities cut official interest rates in four steps, from 6 per cent at the end of 2000 to 5 per cent in August 2001. However, the pound sterling has remained strong and conditions have been characterised as a "twin-speed economy." The latter term is intended to describe recession in the manufacturing sector, hit by an extremely high exchange rate and falling exports, combined with strong domestic demand reflecting unimpaired consumer sentiment. As in the United States, consumer demand had been powered by rising real wages and a low savings rate in the last phase of the boom. Average nominal earnings in the United Kingdom rose by 5 per cent in the first half of 2001, corresponding to an increase in per capita real income of around 3 per cent which, together with rising employment and a rising propensity to consume, pushed retail sales to a growth rate of 6 per cent in volume terms during the first half of 2001.

Japan was the only large industrial economy to experience two recessions and persistently low growth throughout the 1990s. The end of the bubble economy at the beginning of the decade and a huge real appreciation of the yen were accompanied by the first deep and long recession. The Asian crisis and deflationary developments thereafter caused the second. The recovery of 1999 and the first half of 2000 was short-lived. Japan was hit by the slowdown in the United States at exactly the time when it expected to escape the deflationary circle in which it had been trapped for over a decade. With a relatively strong yen, collapsing world markets for technology products, and falling exports the country again faced pressures on companies' sales and profits. Orders for machinery and equipment dropped in the first quarter 2001, and industry sentiment turned sharply negative. Moreover, a rebound of residential investment, another source of hope in 1999 and 2000, has not materialised. Second-quarter growth was negative as all components of aggregate demand were shrinking. With both the corporate and the public sector facing severe financing constraints it was hoped that private consumption would take the lead in the recovery this year, but the outcome did not live up to expectations despite the return of the Japanese central bank to its zero interest-rate policy in March and injection of additional liquidity in the middle of the year in the face of the accelerating downswing of the real economy and worsening balance sheets of companies and banks.

Leading indicators do not point to a quick turnaround in Japan. Stabilization and recovery is likely to depend on shifts in the behaviour of private households, and this in turn may require changes in the Japanese system of remuneration of employees. Japan is the only OECD country where even nominal earnings have been shrinking for a number of years, mainly as a result of the system of profit-related special cash earnings (bonuses, etc), normally paid at the end of the year. These payments fell sharply in 1998 and 1999 at a time when employment was declining and unemployment increasing. In response, private households have cut their expenditure. Other needed changes involve the government budget which is not especially sensitive to overall economic performance, since the tax ratio is relatively low and the automatic stabilizers on the spending side (such as unemployment benefits) are not very effective. This puts a heavy burden on monetary policy whose options for further expansionary action are now limited.

2. International trade, financial flows, and developing countries

The economic slowdown in industrial countries described in section B.1 has been accompanied by widespread downturns in economic activity in developing countries and by a less favourable environment for international trade and financial flows. Decreases in the growth of international trade in 2001 have been pervasive, particularly in the developing world (table 2). Asian countries have been especially severely hit by the decrease in expenditure on information-technology goods in the United States, and decreases in the prices of major categories of primary commodities have unfavourably affected many commodity-dependent developing countries. Even before the events of September 11, current year capital inflows to emerging markets were expected to fall to levels not seen since the beginning of the 1990s. This continuation of the unfavourable conditions prevailing since 1997 has been accompanied by sharply reduced access to international financial markets and sharply higher interest rates for most countries.

So far the global impact of the increasingly unfavourable cyclical performance of the major industrial countries is evident mainly in its direct effects but there is a danger that its indirect effects could worsen the outlook for both output and trade still further. In 1998 falls in commodity prices and flight of capital to safe havens following the Asian crisis helped to stabilize expenditure in the United States and elsewhere in the industrial world. However, in 2001 the primary impulse for more unfavourable macroeconomic conditions is coming from the industrial world itself, in particular the United States, and favourable feedback effects from consequent price declines are absent. Indeed, in 2001 the indirect effects of the economic slowdown, operating through more restrictive fiscal policy in several countries and through secondary effects in financial markets, risk making the downturn more severe. There is also little evidence that financial markets in developing countries are benefiting from capital inflows impelled by investors seeking alternative destinations as the prospects for profits in financial markets in industrial countries deteriorate.

a. Trade impact

According to preliminary estimates, all major developing regions have experienced declines in export volume growth this year. The economic impact of these declines has been reinforced by downward pressure on export prices. In Latin America, this has been due to declines in the prices of primary commodities which constitute substantial proportions of the exports of many countries in the region. In Asia, the most important unfavourable effects have been in the information-technology sector and have involved such products as semiconductors and consumer electronic goods. One result has been that many developing countries, particularly in Latin America, have experienced a weakening of their fiscal and balance-of-payments positions at a time when their attractiveness to external lenders and investors is reduced. In several Asian countries increases in reserves and reductions in foreign indebtedness produced by improved current accounts have come to an end and some economies are now in recession.

In East and South Asia, where recovery after 1997 was driven by exports due to the rapid expansion of investment in the information technology sector, the collapse of United States demand has led to a rapid deterioration in current account positions and declining growth rates. Just as in the run-up to the Asian crisis, the sharp fall in the prices of semiconductors (for 64 bit DRAM prices fell from around \$9 to \$1 between the summer of 2000 and that of 2001) has had a sharply negative impact on their terms of trade, while export volumes to the major developed-country markets have continued to fall. The adverse impact of the slowdown in the United States has been reinforced by the return of recession to Japan. Thus economies such as Taiwan Province of China, Singapore and Malaysia with high shares of information technology exports to the United States have entered recession, while others such as Thailand have seen periods when current account surpluses have been replaced by deficits. Despite declining exports, Indonesia has managed to preserve its current account surplus owing to a sharp contraction in imports, and GDP growth has remained at around 3 per cent. While Republic of Korea has resisted the downturn in United States demand better than other producers in the region with GDP growth still above 2 per cent at an annual rate (in the second quarter of 2001), industrial production started to decline as early as the fourth quarter of 2000, and export growth fell sharply in the second quarter of 2001. While the trade balance remained positive, it was sharply lower in the third quarter at a monthly rate of around \$0.5 billion. The fall-off in exports was due to declines in semiconductor and computer sales, while imports were reduced by declining capital-goods imports and lower raw materials prices. Only countries with more diversified exports and a lower dependence on trade, such as India and China, have resisted this trend of recession and declining external surpluses, and managed to maintain relatively stable growth rates of around 5 per cent and 8 per cent respectively.

Prices for some food commodities had risen in 2000 from low levels in 1999 but this recovery ended in 2001, most major categories resuming their decline during the first eight months (table 3). Amongst beverages the prices of coffee and tea have experienced major declines in 2001, and amongst other primary commodities only a few such as vegetable oil seeds and oils have sustained earlier increases. Agricultural raw materials and minerals, ores and metals have been hard hit by declines in global industrial production, declines for several commodities belonging to the latter category being particularly severe. After the increases in 1999 and 2000 petroleum prices have been broadly stable so far in 2001 despite a continued surplus and supply restrictions.

The effects of the declines in the prices of primary commodities have been strongly felt in Latin America whose fiscal revenues as well as export receipts are often sensitive to movements in such prices. In this region major export commodities include petroleum (for Colombia, Ecuador, Mexico and Venezuela), copper (for Chile), and orange juice, coffee and sugar (for Brazil). The unfavourable effects of recent price falls are evident, for example, in Mexico where they have reinforced the impact on GDP growth of a decline in industrial production starting in mid-2000. The decrease in petroleum receipts has produced a shortfall in projected government revenue and, despite the introduction of a programme of subsidies for coffee producers designed to offset declines of market prices below costs, cuts in government expenditures have been announced to meet projected fiscal targets. In Colombia export growth has recently turned negative and in Ecuador economic recovery has been reversed, a major role in both cases being played by weaknesses in the markets for oil and petroleum. But the effects of recent developments in commodity markets on commodity-exporting countries in Latin America and elsewhere have not been uniform. Russia, for example, has avoided stagnation of its exports and economic growth. A sharp recovery in the country's real effective exchange rate, supported by buoyant prices for its exports, has been accompanied by a large current account surplus and has helped maintain the country's growth rate at around 4 per cent, a level nonetheless well below that recorded in 2000.

b. Financial markets and capital flows

Private capital flows are expected to fall sharply in 2001 (table 4).[1] The combination of the slowdown in the United States economy and the rapid relaxation of monetary policy initiated by the Federal Reserve in 2001 had been expected to be favourable to capital flows to emerging markets for reasons similar to those applying in the early 1990s. However, although the decline in interest rates in the United States early in 2001 was much more rapid than during the recession of 1990-1991, the total reduction in rates has not been as great (450 basis points over three years in 1991-1993 compared with 300 basis points in the first eight months of 2001). More importantly, the reduction in rates in the early 1990s followed a decade of historically high rates and many investors sought to preserve these high returns by shifting funds to foreign markets, attracted by the rapid expansion in Asia and the apparent success of adjustment policies in Mexico and Argentina in the early 1990s and then in Brazil from 1994. By contrast the current United States slowdown is taking place in an environment in which international investors have recently experienced a number of liquidity crises which included a particularly severe market disruption in 1998 and massive losses in securities markets in 2000. Furthermore, as a result of increased international economic integration and the greater role of developing countries in international trade, the downturn in the United States has had a direct and rapid negative impact on their growth and export performance. Thus, as distinct from the situation in the early 1990s, developing-country growth today is more directly linked to that of the United States and provides little advantage in terms of diversification to investors seeking higher risk-adjusted rates of return.

Declines of capital flows in 2001 have affected all major regions but have been especially severe for Argentina and Turkey. These developments have been accompanied by higher risk premia for these two countries and for Brazil. Many Asian countries enjoying current account surpluses have continued to repay bank debt and to be a source of increased deposits with international banks. Thus,

1 Differences between the figures of the IIF and IMF in table 4 are partly due to differences in country coverage and in the basis of estimation. Broadly, while the IIF figures only refer to non-resident transactions the Fund figures adjust them for foreign asset acquisition by residents. For further explanation see *Trade and Development Report, 2001*, chap. II, note 10. IIF figures, unlike those of IMF, also attempt to take account of the impact of the events of September 11.

overall the decline in international financial flows has tended to reinforce the negative impact of the slowdown in United States growth on the prospects of most emerging market and developing countries. Investors facing increased uncertainty over international investment prospects have chosen to accept lower rates of return rather than run the risk of increasing or maintaining their exposure to emerging markets.

As a result of the deterioration in their access to international capital markets a number of developing countries facing external constraints have found it necessary to seek increases in official financing. Argentina arranged an IMF package of $40 billion in January 2001, and a further $8 billion of funding was approved in mid-September. Brazil was granted a $15 billion IMF stand-by credit in August, and in May Turkey received additional funding in support of an existing programme arranged in December 2001, bringing the total package to $19 billion. While these programmes provide a substitute for private flows, to the extent that they all carry conditions requiring increases in primary government budget surpluses (and in the cases of Argentina measures to balance the overall budget), they have an impact on demand similar to that of the cessation of private flows and thus tend to reduce global trade and economic growth.

For most of the period since the 1997 crisis, East and South Asian countries affected have experienced current account surpluses, restoring their foreign currency reserves to record levels. Thus they have been less affected by the fall-off in international capital flows than Latin America. Since many countries in Latin America have to finance substantial debt-service requirements as well as fiscal and current account deficits, the decline in capital flows and its increased costs have compounded the impact of the export declines mentioned earlier.

This has been especially true of Argentina which has successfully implemented a domestic programme to improve external competitiveness and has actually increased its trade surplus, while seeing its current account and fiscal deficits increase and its access to external capital markets fall. Facing rates of interest of 14 per cent on internal borrowing from domestic sources, the country chose to deal with the problem by introducing a balanced overall government budget. This further reduced growth prospects, and despite additional IMF support in September, the risk spread on Argentine debt has remained near its peak levels. Brazil has faced similar conditions, although the decline in growth has been primarily the result of an energy shortage which has required short-time working and caused a collapse in industrial production from an annual average growth of around 6-7 per cent in the first quarter to near stagnation in the third. The real, which had appeared to stabilize at around 1.80 to the dollar, depreciated rapidly and the central bank responded by tightening monetary policy. The resulting deterioration in the external and fiscal balance has brought an increase in risk spreads on borrowing and a sharp fall-off in capital inflows from an average of around $2.5 billion per month in 1999-2000 to an average of only $1.7 billion in July 2001. The deterioration of industrial production, coupled with declining consumer expenditures, a worsening fiscal position and the decline in capital inflows, led Brazil to request a support package from the IMF for the purpose of stabilizing the exchange rate and providing room to reduce interest rates. In Mexico, by contrast, buoyant capital inflows may be adding to the problems created by lower commodity prices and a worsening fiscal position. The country's external balance has deteriorated as export growth has fallen from an annual rate of over 20 per cent in 2000 to near zero in the first quarter of 2001 compared with a fall in imports from a similar rate of growth in 2000 to 1 per cent. However, the peso has remained extremely strong and, in conjunction with falling domestic demand, has contributed to a sharp slowing of inflation. There are indications that an increasing number of firms are again borrowing abroad in dollars, a development which together with the increased foreign investment inflows to Mexico has sustained the level of the exchange rate despite a continued deterioration of the trade balance and a current account deficit in excess of 3 per cent of GDP.

Perhaps because of the failure of the widely expected depreciation of the dollar to materialize, generalized volatility in the exchange rates of developing countries has been absent. However, up to the end of August, countries in Latin America with flexible exchange-rate regimes experienced substantial movements: the Brazilian and Chilean currencies depreciated against the dollar by over 35 per cent and almost 20 per cent respectively, while the Mexican peso appreciated against all major currencies. Argentina by contrast was able to maintain its peg to the dollar but only with continued support from official sources. With more balanced external positions, Asian currencies were broadly stable during the first eight months of 2001: the currencies of Thailand and Taiwan Province of China depreciated by about 2 per cent and 4 per cent respectively and that of the Republic of Korea by about

1 per cent against the dollar, while that of Singapore remained stable and Hong Kong (China), China and Malaysia all maintained their dollar pegs without the need for external support. Since the yen depreciated by more than 10 per cent against the dollar, these currencies in the region appreciated relative to the yen. Turkey was not able to maintain its inflation-targeted peg for the lira: the currency had lost more than 60 per cent of its value against the dollar by the end of August and the economy had entered a deep recession.

The slowdown in international capital flows as well as the falls in prices in United States equity markets, which were accompanied by declines in Japan and Europe, have been accompanied by downward movements in equity prices in developing countries. Countries facing large falls in capital inflows have also had substantive declines in equity prices, those of Argentina falling by almost 25 per cent, and those of Brazil (in local currency) 16 per cent during the year to August. Other markets where capital inflows have been more stable performed better: prices in Mexico, for example, were up slightly in terms of local currency and in Chile the rise was almost 20 per cent. In East and South Asia, where capital inflows have not imposed an external constraint, the markets hardest hit by the decline in United States information-technology and communications investment have had the worst performance. Through the end of August, equity prices in local currency in Hong Kong (China) had fallen by more than 26 per cent and in Singapore by around 16 per cent; prices in Republic of Korea were higher than at the beginning of 2001 but after a substantial fall from the level reached in the spring, and those in Indonesia and Malaysia were also slightly higher. Thailand recorded an increase of about 25 per cent in the first eight months of 2001 but one largely concentrated early in the year.

C. Political uncertainties and economic prospects

Growth forecasts for this year and next had been revised downwards for all regions of the world economy prior to the events of 11 September. The recent downward revision in the IMF's forecast reflects to a large extent a greater than expected impact on the rest of the world from the slowdown in the United States.[2] As discussed in section B.1, the lingering hope that the Euro zone could still avoid the impact of the United States slowdown evaporated during the second quarter of this year and Japan slipped back into negative growth. Among the major industrial economies the sharpest downward revisions in growth forecasts for 2001 have been made for the more export-dependent economies, notably Germany and Japan.

Similarly, without accounting for the impact of recent events, growth of volume of world trade was expected to drop below 4 per cent this year from over 12 per cent last year (table 2). World import and export values were barely to grow because of weaker prices. Developing countries are particularly vulnerable to any sharp slowdown in the growth of world trade. After growing almost 16 per cent last year, exports volumes from developing countries were predicted to grow at just one quarter that figure this year. The expected downturn in export values is even more dramatic because of sharp declines in the prices of commodities as well as for some manufactured exports. As explained in section B.2, both exporters of manufactures (such as the East and South Asian economies dependent on exports of IT goods and many transition economies of Eastern Europe) and commodity-dependent exporters (such as most countries in Latin America and Africa) have already been affected by the sharp decline in world trade.

These unfavourable shifts in levels of economic activity have been accompanied by a continuation of the low levels of private capital flows to developing countries that have prevailed since 1997, with particularly marked deteriorations in the access to international capital markets for some countries (as described in section B.2). Prior to the events on 11 September, net private capital inflows to emerging markets (as defined by the IIF, that is without adjustment for resident acquisition of foreign

2 Between May and September the IMF`s *World Economic Outlook* reduced its 2001 forecast for the world economy from 3.2 per cent to 2.6 per cent and for 2002 from 3.9 to 3.5 per cent.

assets) were expected to drop to $140 billion from $167 billion in 2000 (table 4). According to projections made by both the IIF and the IMF, of the major categories of financial flow only FDI was expected to remain relatively buoyant. However, according to the estimates by the UNCTAD Secretariat, made just prior to the events of 11 September and based on a broader coverage, even that was looking optimistic; FDI inflows to all developing countries were predicted to fall by 6 per cent to $225 billion.[3]

Deteriorating prospects in export markets and international capital markets were expected to lead to a markedly slower economic growth in developing countries with only a few managing to sustain relatively vigorous expansion. In Asia only China, where growth forecasts had been revised upwards over the summer due to strong domestic demand, and India, were expected to weather the reversal in the global economy. In Latin America, Mexico, with over 80 per cent of its exports destined for the United States, was expected to be hit particularly hard by a slowdown in trade, and growth forecasts were revised sharply downward, raising the spectre of recession for the first time since the financial crisis of late 1994. Declining capital inflows were expected to hit indebted Latin American countries hardest. As a consequence, growth in the region as a whole had been expected to drop below 2 per cent, down from over 4 per cent in 2000. Eastern European transition economies where strong export growth to Western Europe helped lift growth last year and into this year also looked increasingly vulnerable to slowdown, although relatively buoyant growth in Russia was seen as a possibly offsetting factor for the region. Least developed countries, particularly those in Africa, were expected to suffer from the weakening of commodity prices, with expectations of African growth for this year being pushed back below 4 per cent.

There can be little doubt that since the events of 11 September the world economy has become much more fragile and economic prospects are surrounded by a good deal more uncertainty. It is almost impossible to anticipate with a reasonable degree of accuracy how large the economic effects of these events will be or how long they will last. However, there is an increased concern that their immediate direct effects will be to further weaken the global economy. Despite the difficulties involved

3. UNCTAD *World Investment Report, 2001.*

in making accurate forecasting under current circumstances, a number of institutions have already revised downward their projections for 2001 for economic growth and international capital flows, allowing for the effects of these events on economic performance during the last quarter of the year. JP Morgan is now expecting 1 per cent growth for the year as a whole, down from almost 4 per cent last year (table 1). According to the IIF "economic growth in the G7 industrial countries will be 0.8 per cent this year after rising by 3.2 per cent last year. The U.S. economy is seen slipping into a mild recession for the second half of the year on a further weakening of investor and consumer confidence and the broad impact of the events of September 11."[4] The same institution now puts private capital inflows to emerging markets for 2001 at $106 billion, compared to the earlier forecast of $140 billion, because of heightened risk aversion (table 4). While world exports are expected to rise by 2.5 per cent this year export earnings of emerging markets are projected to decline by 2 per cent. Overall growth in the Latin American and Caribbean region is now expected by SELA to be closer to 1 per cent, than to the 3 per cent it envisaged earlier in the year.[5]

The immediate material and financial damage the events caused in the United States itself can be estimated at some 1 per cent of GDP. This includes loss to insurance companies from the destruction in lower Manhattan, the revenue losses in frontline industries such as financial services, airlines and tourism from the resulting disruption to daily life immediately following the events, the cost of the clean-up process and reconstruction costs. In these terms, the direct economic consequences are not unlike those of a major natural disaster such as an earthquake.

However, the overall impact of these events is likely to be much deeper. Sharp drops in stock prices and substantial job losses in some of the sectors most seriously affected have heightened the sense of economic insecurity and uncertainty. In the first full week after the events initial jobless claims increased by over 50.000 to 450.000 with 11.000 reported in New York alone, indicating that the impact on unemployment may be significant. Increased insecurity and uncertainty in turn can be expected to feed reduced economic spending which is particularly vulnerable to lower confidence.

4 IIF Press Release, 28 September 2001; www.iif.com/press.

5 Sistema Economico Lationoamericano (SELA) America Latina y el Caribe: Tendencias economicas luego del ataque a Estados Unidos del 11 de septiembre de 2001, Caracas, Venezuala, 24 de septiembre de 2001

Indicative of dangers on this front is the exceptionally sharp drop in the Conference Board index of consumer confidence in the United States from 114.3 in August to 97.6 in September, a decline which is likely to reflect only part of the eventual reactions to the events and their effects on jobs, profit performance and equity prices. Corporate earnings are also likely to be further adversely hit by higher security, insurance and travel costs.

Knock-on effects will most certainly dampen economic performance across the world economy. Still lower exports will foreclose any lingering hope that the export-based buoyancy of last year will be quickly revived, and further weakening of the financial performance of European and Japanese affiliates operating in the United States now seems likely to deepen business pessimism in their home countries. On some assessments, the potential size and unpredictability of any and all of these shifts makes calculating the consequences of 11 September less like those of a natural disaster and more like those associated with wartime conditions. By way of a reminder, the damage to consumer confidence and higher oil prices triggered by the Gulf War shaved 5 percentage points from consumer spending pushing the United States into recession. Like then, a shift of this magnitude would push Europe and Japan into recession and postpone recovery until well into 2002.

The threat of contagion to developing countries from a still sharper slowdown in the industrial countries is mainly through weaker export prospects and a worsening of the outlook for private capital flows. Indebted Latin American economies would be particularly vulnerable to such a shift. Although the emergency packages agreed with the IMF have helped bolster the financial positions of Argentina and Brazil, uncertainty in capital markets over the rest of the year is likely to make financing their current account deficits and the rolling-over of their foreign public debt still more difficult. Other emerging-market countries likely to face difficulties in refinancing substantial amounts of maturing debt in the next few months include Turkey, Hungary, and Russia.

The adverse impact of the events of 11 September on transport and insurance costs is likely to have a particularly damaging impact on developing country exporters. Political tensions in certain regions can hurt exports of some poor countries, such as tea exports of Kenya to Afghanistan and

Pakistan.[6] For some producers of strategic commodities, such as oil, favourable price movements could strengthen growth prospects but much will depend on the impact of non-economic factors. The immediate price hike in oil after the attacks to over $30 per barrel has been followed by a sharp drop towards the $22 per barrel lower limit of the OPEC price range and further declines over the remainder of the year cannot be ruled out.

Although on all accounts global growth will certainly slow still further in the immediate aftermath of the events of 11 September, the extent of the slowdown this year and the speed of any recovery next will very much depend on whether the major industrial economies can collectively moderate deflationary pressures and avoid excessive disruption of international economic relations. Policy actions already taken or projected in major industrial countries on the monetary and fiscal fronts are a reason for some optimism here. In an immediate gesture of international economic solidarity both the ECB and Bank of Japan followed the Federal Reserve and cut interest rates after the events, pushing down nominal interest rates to their lowest levels in some time and providing a degree of calm to foreign exchange markets. Perhaps more remarkably a large number of other industrial and emerging-market economies followed suit in the 10 days following the events of 11 September, including Canada, United Kingdom, Sweden, Denmark, Switzerland, South Africa, New Zealand, Hong Kong (China), Republic of Korea, and Taiwan Province of China. The ECB, the Bank of England and the Federal Reserve have also been co-operating to ensure the smooth functioning of the financial markets and clearance and settlement systems. Despite persistent trade imbalances and exchange rate misalignments among the major reserve-currency countries, foreign exchange markets have avoided major disruptions since the recent events partly thanks to collective monetary action and central bank intervention, and only the Swiss franc, a traditional safe-haven currency in times of crisis, has shown strong gains.

In the United States the Federal Reserve and the Controller of the Currency have urged banks to restructure loans and loosen credit conditions for distressed borrowers. The Federal Reserve has also been supporting banks through its policy on the availability of short-term funds. The Congress has already granted funds to the airline industry, aid to New York for reconstruction and funds for general

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6 See “Kenya: Tea exports hit by US anti-terror campaign”, Office for the Coordination of Humanitarian Affairs (OCHA), Integrated Regional Information Network, 28 September 2001, Nairobi.

security measures. It is also considering a rapid implementation of additional tax reductions. In this respect, Chairman Greenspan's recent suggestion to the Senate Financing Committee that any stimulus package would need to be of the order of $100 billion to be effective is telling in pointing not only to the difficulties facing the United States economy but also to the willingness of policy makers in that country to respond aggressively to ensure that the economy is turned around.

For global prospects a good deal of hope is being pinned on a recovery in the United states beginning in the first half of next year, accelerating towards its long-term potential in the second half.[7] Sound fundamentals and timely use of expansionary monetary and fiscal measures underpin this hope. These measures are expected to jumpstart the United States economy, particularly as they would come on top of planned tax cuts. On some accounts, the combination of a deeper downturn and aggressive expansionary policy measures could even make the recovery more vigorous than expected.[8] While such an outcome cannot be ruled out, it is also possible that the combined impact of these measures, which amount to some 2 per cent of GDP, may do little more than offset the negative overall impact of the events of 11 September, without doing enough to counter the underlying weaknesses in the economy. In any case there now seems a consensus that the positive effects of the expansionary measures will not be felt for some time, and they are unlikely to prevent a contraction in the United States economy over the coming months.

That consensus now includes a recognition that the fate of the world economy cannot be and should not be left to the policy response of the United States to recent events in that country. Policy in Japan and, particularly, continental Europe needs to take a much more aggressive stance in responding to deflationary threats and reviving the global economy. As noted in *TDR 2001*, “business as usual” was not the right mantra for policy makers anywhere even before these events; it is much less so now.

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7 See, for instance, Statement by Treasury Secretary O’Neill and Chairman Greenspan to the Senate Banking Committee; and Statement by Kenneth Rogoff, at the IMF World Economic Outlook Press Conference, September 26, 2001.

8 For instance “the stage is being set for the current down-leg to be sharp, but then to be followed by a strong recovery, which probably will begin to take hold sometime around the middle of next year”, JP Morgan, *Global Data Watch*, 21 September 2001, p.1.

Still, and much like the growing calls for a global response to heightened political vulnerabilities, the economic fall-out from the attacks on the United States cannot be dealt with in isolation. As much as in the political and military spheres, policy coordination and coalition building at a multilateral level is taking on increasing importance in economic matters. On some accounts, launching a new round of trade negotiations in November would also help boost global demand. However, whatever the other merits of launching a round, these should not be confused with the urgent task of coordinating expansionary macroeconomic responses. History shows that economic contraction and rising unemployment are the principal enemies of free trade.

The simultaneous cuts in interest rates by the Central Banks of the major industrial countries immediately following the attacks points in the right direction. However, much more can and should be done, particularly to alleviate the actual and potential problems confronting developing countries. The need for such an approach is also recognized by international financial markets:

> The Institute of International Finance (IIF) called ... for a coordinated policy response 'that lays the basis for renewed global economic expansion, while taking into account of the particular circumstances facing emerging markets. .... [T]he official actions of recent days demonstrated strong leadership and have provided sorely needed confidence. Nevertheless, further actions are necessary to ensure the recovery of the global economy. [T]here is a need to use the current situation to forge new forms of intensified global cooperation not only between policy-makers in the industrial and emerging market economies, but also between public authorities and private financial institutions.[9]

The swift response of the United States authorities to financial instability and economic difficulties in the wake of the attacks highlights the need for global mechanisms to inject international liquidity into the world economy in times of stress. With austerity and import retrenchment now threatening growth across the developing world, provision of such liquidity to these countries would constitute a major source of global expansion and stability. Given the heightened risk aversion in emerging market assets, lower interest rates and liquidity expansion in the major industrial countries do not necessarily revive private capital inflows to developing countries, and direct action may be needed

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9 IIF Press Release, 28 September 2001; www.iif.com/press.

at the global and national level. This calls for mobilization of the full resources of the Bretton Woods institutions, including the facilities established at the IMF for emergency and contingency financing for crisis and contagion in emerging markets. Consideration could also be given to the use of reversible SDR allocation as and when needed.

It is also important that national export credit agencies should fully play their role as facilitators of international trade and investment during a period of heightened uncertainty. For this purpose they should avoid imposing more restrictive conditions on export credit insurance and should as appropriate be prepared to make expanded use of their direct lending powers. If necessary governments should consider raising ceilings on the total amount of insurance which export credit agencies are allowed to provide. Multilateral institutions which provide export credit insurance should consider taking parallel actions to the extent that this is possible within their legal mandates. Provision of international liquidity and export credit facilities to countries facing acute shortage of foreign exchange as a result of declines in their exports earnings and drying up of private capital inflows would be consistent with the current policy advice that the best response to such a crisis is reflation rather than austerity.

Again, in their intervention in the aftermath of the events of 11 September the United States authorities recognized that under such exceptional conditions, distressed debtors may need relief and support in the form of rollover of their maturing debt as well as rapid access to new credits. In any case the United States Bankruptcy Code provides considerable protection to debtors against asset grab race by creditors and support in terms of access to new credit. The UNCTAD Secretariat has long been arguing for the introduction of global mechanisms recognizing the need for protection and support for distressed international debtors in the form of standstills, lending into arrears and debt restructuring, based on the principles of chapter 11 of the United States Bankruptcy Code.[10] It is therefore encouraging to see that serious attention is now being given by the United States Administration to the application of such principles to international debt, as indicated by recent remarks made by the Secretary of Treasury of the United States in his Testimony to the Senate Banking Committee:

10 See *TDR 1998*, pp. 89-93; and *TDR 2001*, chap. VI.

> I think now it is the time that we need to take the action that had been talked about for years that has never been done. We need an agreement on international bankruptcy law so that we can work with governments that, in effect, need to go through chapter 11 reorganization instead of socializing the costs of bad decisions.[11]

Under current conditions, contingency measures needed with respect to the debt of the affected developing countries could include write offs as well as deferral of payments on official debt. Again, private creditors could be encouraged through various mechanisms to provide some breathing space for debtors experiencing serious payments difficulties. More fundamentally, the link from extreme poverty to the global fight against terrorism has already led to calls for a more generous stance on the side of donors and official creditors. As suggested by European Union's external affairs commissioner Chris Patten, policy makers must think beyond hunting down and punishing those behind the attacks, and the prosperous parts of the world should be ready for a significant transfer of resources from rich to poor as part of any fierce and relentless attack against terrorism.[12] It is thus important to ensure that political imperatives should not take precedent over development in the allocation of aid.

Finally, it is perhaps worth recalling that the design of a more stable financial and trading system after the Second World War was preceded by a lengthy process of discussion, albeit among a limited number of parties. The growing realization since the events of September 11 that unregulated financial markets can operate against the wider public interest by channelling resources in support of terror carries a wider message. Developed and developing countries have common cause in finding constructive measures to better manage financial markets in the interest of all countries. In this light, the upcoming United Nations Conference on Financing for Development provides a multilateral setting where progress towards a more balanced and stable pattern of integration can begin to take shape.

11 Transcript from minute 31 of clip 2 of the CSPAN video. See also "U.S. Weighs Aid Boost as Global Slump Worsens" , Washington Post, 21 September 2001.
12 Financial Times, 17 September 2001.

Table 1 (CORRECTED)

WORLD OUTPUT, 1990-2001

(Percentage change over previous year [a])

Region/country	*1990-1995* [b]	*1995-2000* [b]	*1998*	*1999*	*2000*	*2001 estimates*		
						UNCTAD [c]	IMF [c]	JP Morgan
World	2.0	3.1	1.9	2.9	3.8	1.5	2.6	1.1
Developed market-economies countries	1.8	2.8	2.1	2.7	3.3	1.1		
of which:								
United States	2.4	4.1	4.4	4.1	4.1	1.2	1.3	1.0
Japan	1.4	1.3	-2.5	0.8	1.5	-0.6	-0.5	-0.7
Canada	1.7	3.7	3.3	5.1	4.4	1.9	2.0	1.4
European Union	1.5	2.5	2.7	2.5	3.4	1.8	1.8	
of which:								
Euro area	1.6	2.5	2.8	2.5	3.5	1.8	1.8	1.5
Germany	2.0	1.8	2.1	1.4	3.1	0.8	0.8	0.8
France	1.0	2.5	3.2	3.0	3.4	2.0	2.0	1.9
Italy	1.3	1.8	1.5	1.6	2.9	1.8	1.8	2.0
United Kingdom	1.6	2.8	2.6	2.3	3.1	2.0	2.0	1.9
Transition Economies	-6.9	2.2	-0.5	3.3	6.1	4.1	4.0	3.9
of which:								
Russian Federation	-9.1	1.1	-4.9	5.4	8.3	4.5	4.0	4.4
Developing economies	5.0	4.4	1.5	3.6	5.6	3.3		
of which:								
Africa	1.5	3.6	3.2	3.0	3.1	3.7	3.8	
Latin America	3.6	2.9	1.9	0.1	3.7	1.0		
of which:								
Argentina	5.8	2.7	3.9	-3.0	-0.5	-1.5		-1.5
Brazil	3.1	2.2	-0.1	0.8	4.3	0.7	2.2	0.5
Asia	6.2	5.1	1.1	5.4	6.8	3.6		
of which:								
China	12.0	8.3	7.8	7.3	7.8	7.5	7.5	7.3
Developing Asia excluding China	4.9	4.3	-0.8	4.8	6.5	2.6		
of which:								
Malaysia	8.7	4.6	-7.4	5.8	8.5	0.1	1.0	
Republic of Korea	7.4	4.7	-6.7	10.9	8.6	2.5	2.5	1.9
Memo Item								
Developing economies excluding China	4.1	3.8	0.5	3.0	5.3	2.6		

Source: UNCTAD secretariat calculations, based on data in 1995 dollars from national and international sources; IMF, *World Economic Outlook*, September 2001; JP Morgan, *Global Data Watch*, 21 September 2001.

a Based on country weights in terms of purchasing power parity for IMF, and in terms of exchange rates for UNCTAD and JP Morgan.

b Annual average.

c Produced before the events of September 11 in the United States.

Table 2

EXPORTS AND IMPORTS BY REGION AND ECONOMIC GROUPING, 2000-2001:

(Percentage change over previous year)

Region / economic grouping	*Export value* 2000	*2001 estimates* IMF	*2001 estimates* LINK	*Export volume* 2000	*2001 estimates* IMF	*2001 estimates* LINK
World	12.3	0.1 [a]	6.4	11.9	3.6 [a]	6.1
Developed market-economy countries	6.7	.	7.3	9.8	2.7	.
of which:						
Japan	14.3	.	0.7	9.2	-5.5 [b]	.
United States	12.5	.	.	10.7	5.8 [b]	.
European Union	1.9	.	10.7	10.1	4.6 [b]	.
Transition economies	26.0	.	.	17.0	7.1 [b]	.
Developing countries	24.2	1.2	4.6	15.8	4.0	.
of which:						
Africa	27.0	-0.2	0.4	7.3	1.5	.
Latin America	20.8	1.3	5.4	10.4	5.6	.
Asia	20.2	1.7	6.1	18.8	3.6	.
of which:						
China	27.7	.	6.9	28.3	.	.

Region / economic grouping	*Import value* 2000	*2001 estimates* IMF	*2001 estimates* LINK	*Import volume* 2000	*2001 estimates* IMF	*2001 estimates* JP Morgan
World	12.7	0.1 [a]	.	11.3	3.6 [a]	6.4
Developed market-economy countries	9.7	.	6.5	9.6	3.5	4.8
of which:						
Japan	21.9	.	1.7	10.9	0.2 [b]	3.4
United States	18.7	.	3.4	11.5	7.2 [b]	4.4
European Union	4.0	.	9.6	8.5	3.8 [b]	5.6 [c]
Transition economies	13.5	.	.	13.0	10.1 [b]	9.5 [d]
Developing countries	20.7	4.2	7.5	15.3	6.5	9.7 [d]
of which:						
Africa	5.4	6.7	5.2	5.4	6.8	.
Latin America	16.0	4.0	9.9	11.1	5.8	10.3 [d]
Asia	26.6	5.4	7.1	18.7	8.7	10.0 [d]
of which:						
China	35.8	.	8.9	33.1	.	.

Source: UNCTAD secretariat calculations, based on statistics of WTO;
IMF, *World Economic Outlook* , October 2001(preliminary version), Washington DC;
Project LINK, *World Economic Outlook* , April 2001 (www.chass.utoronto.ca/link);
JP Morgan, *World financial markets* , Third Quarter 2001, New York, 16 July 2001.

a Average of annual percentage change for world exports and imports.
b Including services.
c Euro area.
d Emerging economies.

Table 3

WORLD PRIMARY COMMODITY PRICES, 1997-2001

(Percentage change over previous year)

Commodity group	*1997*	*1998*	*1999*	*2000*	*August 2001* [a]
All commodities [b]	**0.0**	**-13.0**	**-14.2**	**1.9**	**-4.7**
Food and tropical beverages	**2.8**	**-14.3**	**-18.3**	**1.0**	**-2.8**
Tropical beverages	33.3	-17.3	-20.9	-13.2	-8.2
Coffee	54.7	-28.5	-23.2	-16.2	-9.7
Cocoa	11.2	3.7	-32.1	-22.2	28.7
Tea	35.1	4.3	-7.0	6.8	-19.2
Food	-3.5	-13.8	-18.1	5.9	-2.2
Sugar	-4.9	-21.2	-30.0	30.5	-19.1
Beef	4.0	-7.0	6.1	5.7	15.0
Maize	-25.3	-13.4	-5.5	-1.0	-1.4
Wheat	-22.6	-19.9	-10.9	3.5	-3.1
Rice	-10.7	1.3	-18.6	-18.1	-8.7
Bananas	4.3	-3.1	-9.9	-2.3	53.8
Vegetable oilseeds and oils	**-0.9**	**7.1**	**-23.3**	**-22.8**	**18.8**
Agricultural raw materials	**-10.3**	**-10.8**	**-10.3**	**-1.0**	**-2.9**
Hides and skins	-19.8	-22.7	-27.6	73.8	27.8
Cotton	-8.9	-8.3	-22.9	3.5	-29.7
Tobacco	15.6	-5.5	-7.0	-3.3	4.8
Rubber	-28.3	-29.8	-12.6	7.9	-5.2
Tropical logs	-5.5	-1.2	-7.2	-4.3	0.3
Minerals, ores and metals	**0.0**	**-16.0**	**-1.8**	**12.0**	**-13.3**
Aluminium	6.2	-15.1	0.3	13.8	-12.0
Phosphate rock	7.9	2.4	4.6	0.2	-6.8
Iron ore	1.1	2.8	-9.2	2.6	4.5
Tin	-8.4	-1.9	-2.5	0.6	-25.6
Copper	-0.8	-27.3	-4.9	15.3	-20.9
Nickel	-7.6	-33.2	29.8	43.7	-24.5
Tungsten ore	-9.3	-6.4	-9.3	12.1	29.6
Lead	-19.4	-15.3	-5.0	-9.7	4.4
Zinc	28.4	-22.2	5.1	4.8	-21.9
Crude petroleum	**-6.0**	**-31.8**	**38.7**	**55.6**	**1.6**

Source *:* UNCTAD, *Monthly Commodity Price Bulletin,* various issues.

a Change from December 2000.

b Excluding crude petroleum.

Table 4

NET CAPITAL FLOWS TO DEVELOPING AND TRANSITION ECONOMIES, 1998-2001: ESTIMATES OF THE INSTITUTE FOR INTERNATIONAL FINANCE AND THE IMF

(Billions of dollars)

Type of flow/region	*1998*	*1999*	*2000*	*2001* [a]
	Estimates of the Institute for International Finance			
Net private capital inflows				
Total	143	141	167	106
by category:				
Private creditors				
Commercial banks	-55	-46	6	-23
Non-bank private creditors	64	26	26	0
Equity investment				
Direct equity	121	146	130	124
Portfolio equity	14	16	16	4
by region:				
Africa/Middle East	7	11	5	9
Asia/Pacific	0	31	61	38
Europe	38	35	40	14
Latin America	99	65	61	45
Memo item: [b]				
Resident lending/other, net				
Total	-146	-120	-143	-99
Africa/Middle East	1	-6	-8	-8
Asia/Pacific	-76	-61	-86	-36
Europe	-27	-24	-38	-32
Latin America	-43	-31	-11	-24
	Estimates of the International Monetary Fund			
Net private capital inflows				
Total	69	59	1	-1
Net direct investment	156	153	147	163
Net portfolio investment	-2	32	2	0
Other net flows [c]	-85	-126	-148	-164
Africa	10	11	4	11
Net direct investment	7	8	8	12
Net portfolio investment	4	9	-2	3
Other net flows [c]	-1	-6	-2	-4
Asia	-46	-9	-16	-22
Net direct investment	60	52	47	51
Net portfolio investment	-15	14	4	-11
Other net flows [c]	-91	-75	-66	-63
Middle East and Europe	12	-1	-26	-34
Net direct investment	7	6	7	6
Net portfolio investment	-12	-4	-10	-4
Other net flows [c]	17	-2	-24	-36
Western hemisphere	73	45	37	39
Net direct investment	61	63	63	67
Net portfolio investment	18	11	5	7
Other net flows [c]	-6	-30	-31	-35
Transition economies	21	14	2	5
New direct investment	22	24	23	27
Net portfolio investment	4	3	4	5
Other net flows [c]	5	-13	-25	-27

Source: IIF, *Capital Flows to Emerging Market Economies* , 30 Sept. 2001; IMF, *World Economic Outlook* , Sept. 2001.

a Estimates of the IIF allow for the impact of the events of September 11 in the United States.

b For explanation of this term, see *TDR 2001* , Part One, chap. II, note 10.

c Other net flows comprises other long-term net investment flows, including official and private borrowing.