Recent Economic Performance

- Economic growth in emerging East Asia continued to slow in the second half of 2008, as the global financial crisis deepened and economic activity contracted in major industrial countries.
- Inflation peaked across most of emerging East Asia during the third quarter as sharp declines in oil and other commodity prices followed tightening credit conditions.
- The balance of payments remained in surplus across much of the region through the third quarter, even as current account balances narrowed and net capital flows declined.
- Stock markets across the region continued their downward slide in the second half of 2008 as the global crisis triggered massive sell-offs.
- Most emerging East Asian currencies depreciated against the US dollar on flight-to-safety, particularly since mid-September, while local currency bond market yield curves shifted downward.

Outlook, Risks, and Policy Issues

- The external economic environment for developing Asia is likely to worsen, as major industrial economies contract further, global financial conditions remain constricted, and world trade growth slows sharply.
- The deteriorating external environment will hurt developing Asia’s immediate growth prospects—aggregate GDP growth is forecast to fall to 5.8% in 2009 from this year’s estimated 6.9%.
- Economies in emerging East Asia will grow at 5.7% in 2009, down from 6.9% this year.
- Major risks to the outlook include (i) a sharper or prolonged global recession, (ii) persistent financial stress with volatile capital flows, (iii) further tightening of external and domestic funding conditions, and (iv) excessively volatile conditions in foreign exchange markets.
- The coming year will be a difficult one for developing Asia but it will be manageable if countries respond decisively to restore confidence in the financial system and real economy, and collectively to avoid the effects of contagion.
With the balance of risks shifting from rising inflation to slowing growth, monetary policy must remain flexible enough to allow growth stimulus where appropriate while keeping inflation expectations firmly anchored.

Fiscal policy could hold center stage for many emerging East Asian economies in mitigating/minimizing effects of deteriorating external economic conditions on growth prospects.

Policy makers in many emerging East Asian economies need to deepen and broaden structural reforms to rebalance the sources of growth from an over-reliance on exports to domestic demand.

Global Economic Crisis: Impact and Challenges for Emerging East Asia’s Financial Systems

In recent months, the ripple effects of the global financial crisis have reached Asian shores, and the region’s financial systems have come under increased pressure as a result.

The region’s policy makers still have the opportunity to be proactive rather than reactive, and to forestall emerging threats to financial stability.

Three sets of short-term policy responses are needed to bolster the foundations of financial stability:

- close monitoring of the region’s financial systems and the identification of both weak financial institutions and systemic vulnerabilities;
- provision of adequate foreign currency as well as domestic liquidity to systemically critical financial institutions so that credit continues to flow into the economy; and
- prevention of the effects of slowing economic growth from spilling over onto the region’s banking systems.

In the longer-term, reforms of regulation and oversight of financial systems should aim to

- strengthen transparency and accountability;
- enhance sound regulation and prudential oversight;
- mitigate the procyclicality of financial markets;
- broaden and deepen financial markets to enhance resilience; and
- reinforce cross-border cooperation.
About the Asian Development Bank

ADB, based in Manila, is dedicated to reducing poverty in the Asia and Pacific region through inclusive economic growth, environmentally sustainable growth, and regional integration. Established in 1966, it is owned by 67 members – 48 from the region. In 2007, it approved $10.1 billion of loans, $673 million of grant projects, and technical assistance amounting to $243 million.