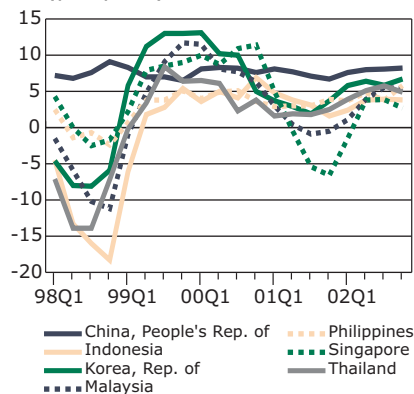


East Asia's Growth, Recovery, and Restructuring—A Regional Update

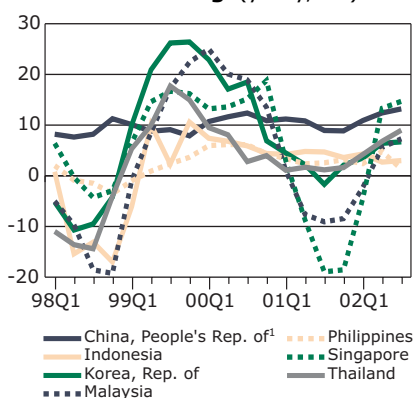
Growth and Recovery in 2002

Figure 1: **Real GDP Growth**
(y-o-y, %)



Note: Fourth quarter data for 2002 are REMU staff estimates based on official 2002 full year GDP estimates, except for the Philippines where official fourth quarter data is available. Source: ARIC Indicators, REMU staff estimates.

Figure 2: **Growth of Manufacturing**
(y-o-y, %)



¹Data for the PRC refer to industrial production. Source: ARIC Indicators.

Real Sector Developments

East Asia¹ posted a modest economic rebound in 2002, reversing the sharp slowdown in growth during the previous year (Figure 1). Reflecting the worsening global economic environment, the growth momentum of East Asia's exports softened in the second half of last year (Box 1). Nevertheless, the region weathered the economic difficulties fairly well. Gross domestic product (GDP) for East Asia is estimated to have grown by 6.1% last year, better than the 5.2% and 5.8% forecast in the April and July 2002 *Asia Economic Monitor* (AEM), respectively, but closer to the 6% forecast in the October 2002 AEM. It was also 1.8 percentage points higher than the region's growth in 2001. Excluding the People's Republic of China (PRC), where GDP grew by an impressive 8%, the region's GDP growth in 2002 was about 5%.

While last year's economic rebound cut across sectors, it was particularly evident in manufacturing among most of the seven economies in the region for which quarterly data are available—PRC, Indonesia, Republic of Korea (Korea), Malaysia, Philippines, Singapore, and Thailand (henceforth referred to as ASEAN5+2). Manufacturing dominated the growth rebound well up to the third quarter of last year—the latest for which such data are available (Figure 2). The exception was the Philippines, where last year's GDP growth was driven primarily by the services sector, with manufacturing and agriculture playing a complementary role.

Last year's regional rebound was supported both by exports and domestic demand (Figures 3 and 4). Despite the loss of growth momentum in the second half of the year (q-o-q data), for the year as a whole, exports of the ASEAN5+2 taken together grew at 11% compared to a decline of 6% in 2001 on a year-on-year (y-o-y) basis.

Both import demand from the G3 countries (US, Europe, and Japan) and intra-regional trade contributed to East Asia's healthy export growth last year. In the second and third quarters of last year, East Asia's exports grew, on average, by 9%. Exports to G3 accounted for 50% of

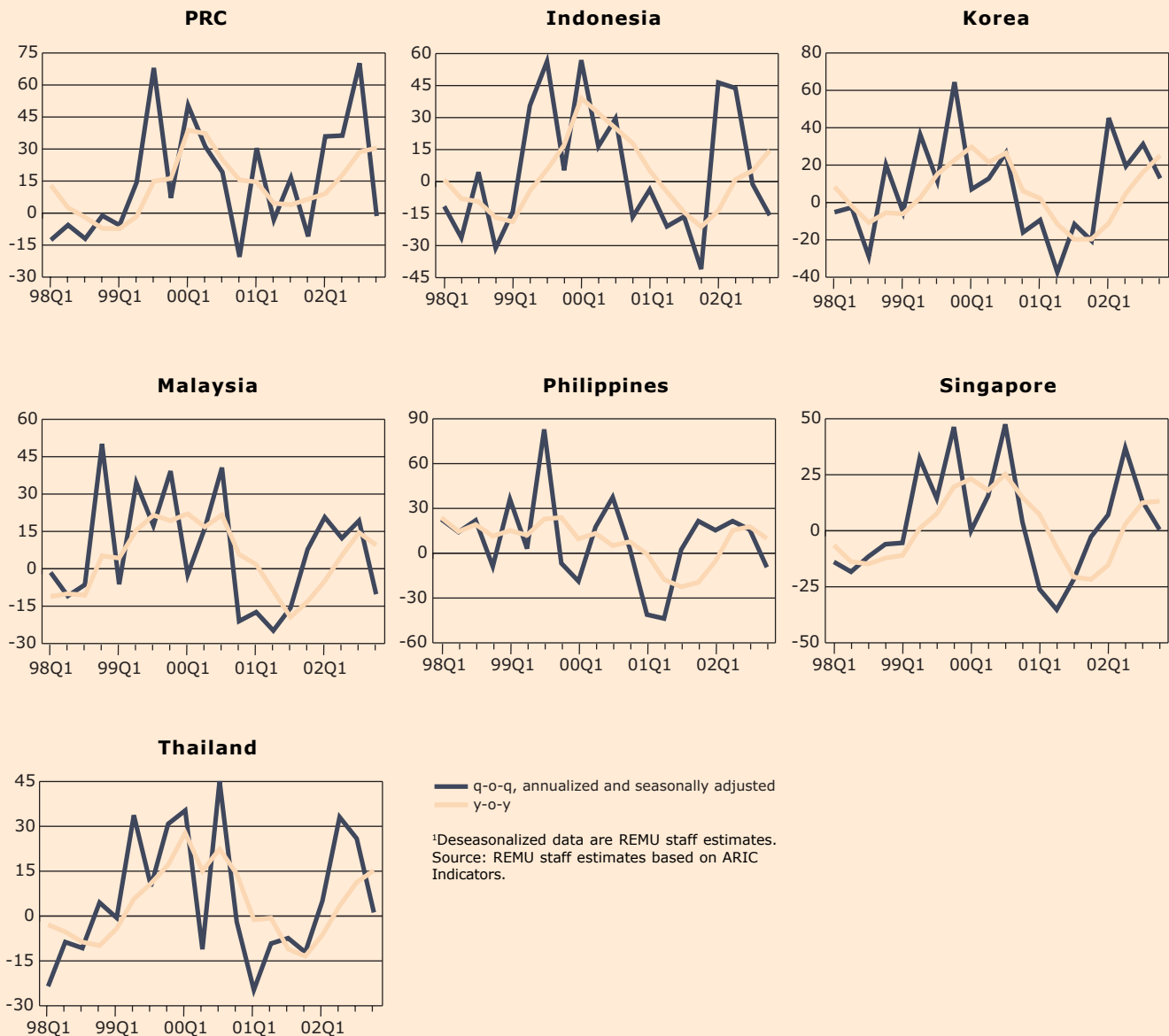
¹Defined here as the 10 Association of Southeast Asian Nations countries (Brunei Darussalam, Cambodia, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Viet Nam) plus the People's Republic of China and Republic of Korea.

Box 1: East Asian Exports: Is the Momentum Slowing?

Driven by the sober external environment, growth momentum of exports slowed somewhat in East Asia during the second half of last year. The loss of export growth momentum is not reflected in the year-on-year (y-o-y) growth in exports (Figure 1.1). These y-o-y data, however, give a misleading picture of the growth momentum, especially since the region had experienced a sharp export slowdown in 2001. Quarter-on-quarter (q-o-q) ex-

port growth rates computed from deseasonalized data series (estimated by the Regional Economic Monitoring Unit [REMU] of the Asian Development Bank), which is a more appropriate measure of the momentum, indicate that there was some moderation of export momentum in the second half of the year in Indonesia, Philippines, Singapore, and Thailand. In PRC, Korea, and Malaysia exports moderated in the fourth quarter of the year.

Figure 1.1: **Growth Rates of Merchandise Exports** (q-o-q, annualized and seasonally adjusted;¹ and y-o-y)



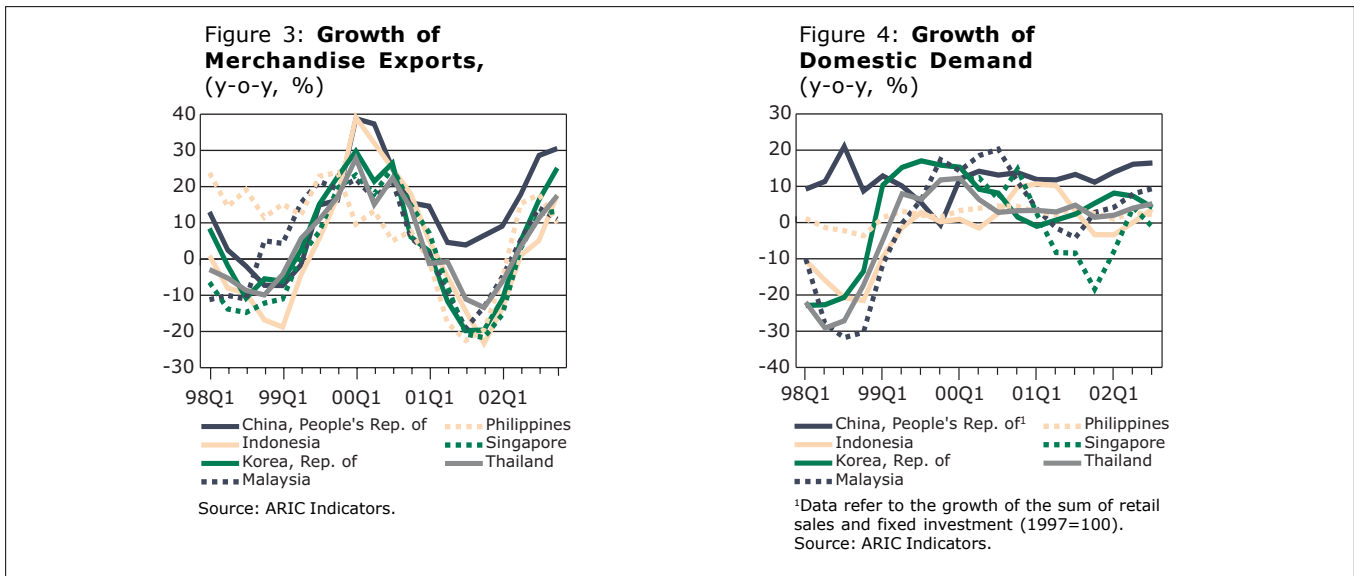
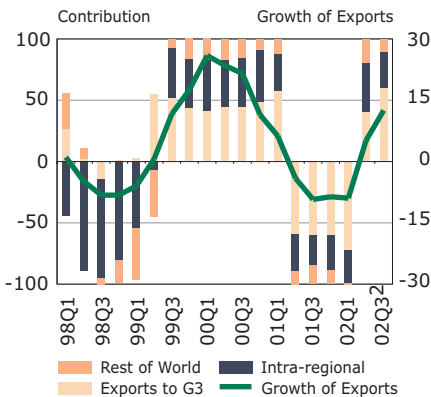


Figure 5: East Asia's¹ Exports—Growth Rate (y-o-y) and Contribution to Export Growth by Trading Partners (%)



¹Includes Hong Kong, China.
²2002Q3 growth and contribution were calculated using July and August 2002 and July and August 2001 data.
 Source: REMU staff calculations based on data from IMF, *Direction of Trade Statistics* (January 2003).

this increase, while exports to countries within the region accounted for 35% (Figure 5). East Asia's intra-regional exports are driven primarily by import demand from the G3 countries, with a substantial part consisting of intermediate and processed goods, which are exported intra-regionally for further processing or assembly before being exported to G3 countries. Preliminary evidence, therefore, suggests that intra-regional trade is providing only limited cushion to any deterioration in the region's export prospects to the G3 (Box 4, October 2002 AEM). The recent buoyancy of domestic demand in several East Asian countries suggests, however, that domestic demand is also contributing somewhat to the increasing importance of East Asia's intra-regional trade.

Growth in domestic demand improved during much of last year in most East Asian countries, helped by the turnaround in exports, generally low interest rates, and expansionary fiscal policies. Another factor is the progress made in restructuring the financial and corporate sectors since the Asian financial crisis. Among the crisis-affected countries, the contribution of domestic demand to the economic rebound has been the most significant in Korea and Malaysia, followed by Indonesia, Thailand, and Philippines. Outside the crisis-affected countries, judging by the strong growth in retail sales (8.8% in nominal terms and 9.7% at constant prices) and fixed investment (15% in nominal terms), domestic demand also played a substantial role in the PRC's continued strong growth last year. In Singapore, too, domestic demand contributed moderately to its pickup in GDP growth.

In several countries, the household sector has spearheaded the turnaround in domestic demand in an environment of low interest rates (and the associated growth in consumer credit and mortgage lending) and the rapid growth of new sources of financing, such as credit cards. However, two other components—domestic investment and public consumption—have also been significant (Figure 6). In Korea, private consumption accounted for about three fourths of the growth in domestic demand since the third quarter of 2001, with the rest attributed to domestic investment. In Indonesia, Philippines, and Thailand, private consumption was the driving force behind growth in domestic demand in recent quarters, although from the second quarter of last year, domestic investment also played a significant role in the latter. Malaysia’s growth in domestic demand since the beginning of 2002 has been more or less equally shared by all the three components of domestic demand—private consumption, public consumption, and domestic investment. In the PRC, retail sales grew by 9% last year, following a 10% rise in the previous year.

Figure 6: Domestic Demand: Growth Rate and Contribution of Components (% , y-o-y, constant prices)

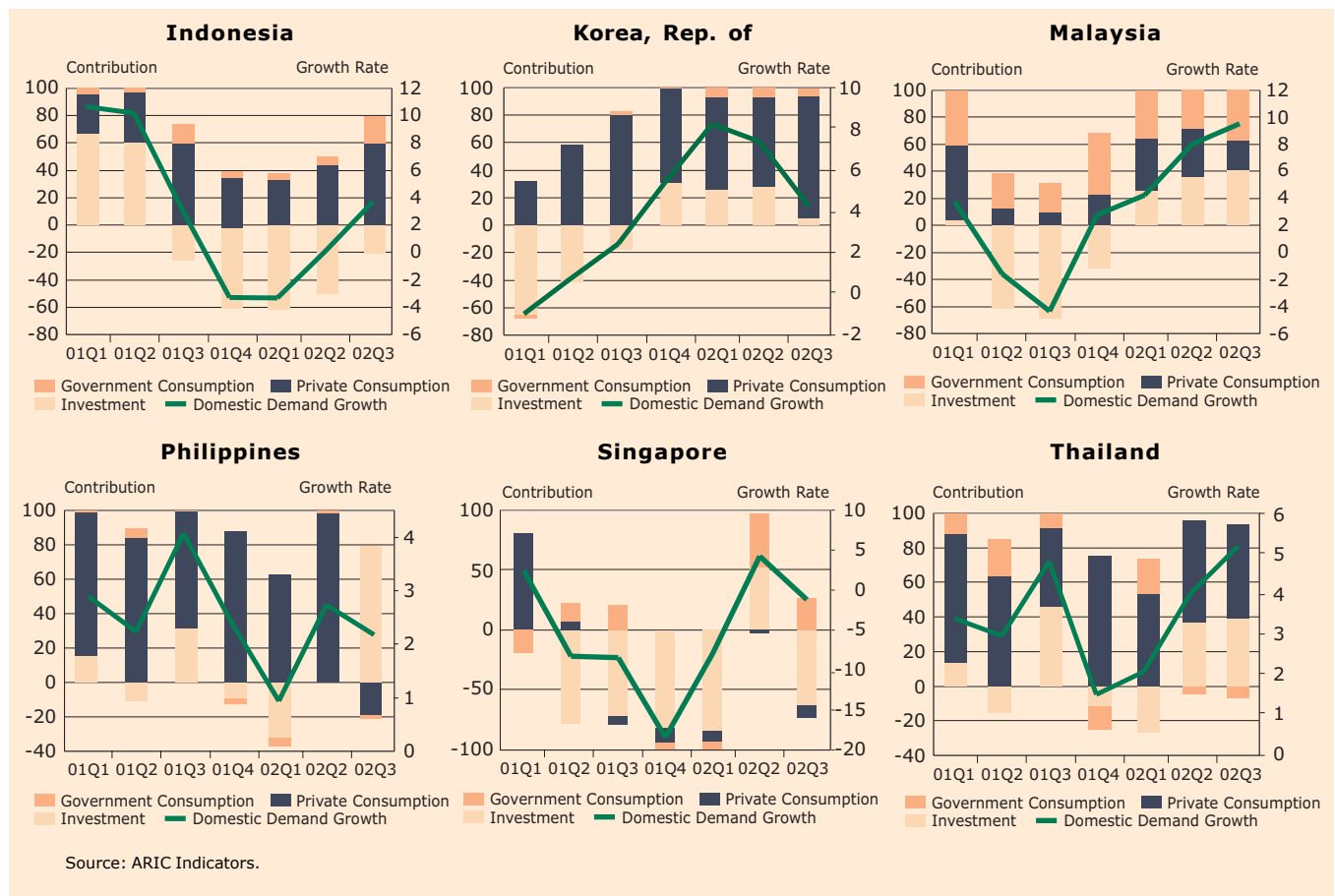


Figure 7: Inflation Rates (%)

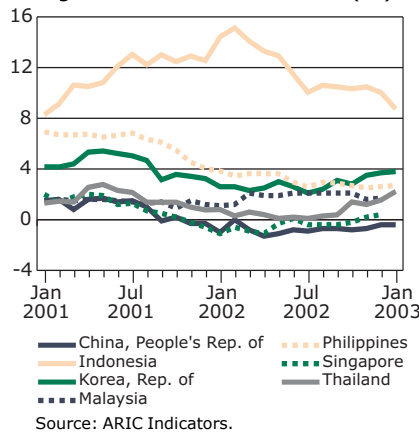


Figure 8: Composite Stock Price Indexes¹ (last week of 2001Dec=100, in local currency)

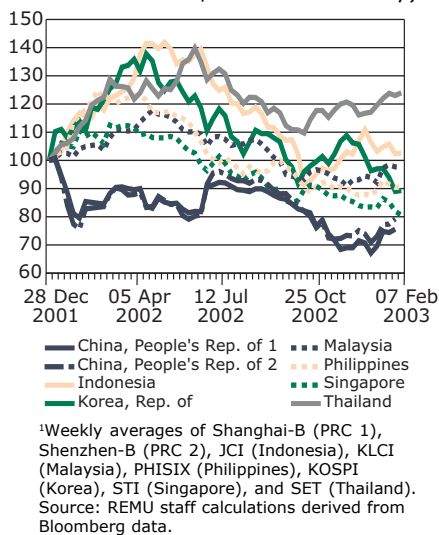
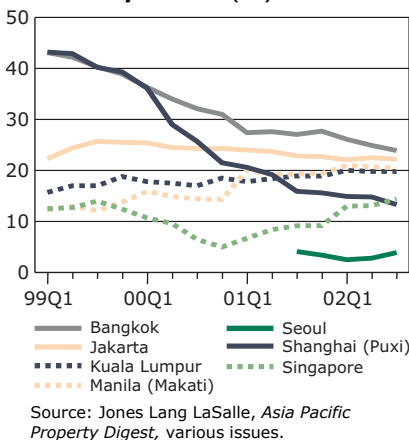


Figure 9: Office Property Vacancy Rates (%)



Despite the improvement in domestic demand and pickup in growth, inflation remains below 4% across the region except in Indonesia where the annual figure hovers around 10% (Figure 7). Inflation has been close to zero in Singapore, while prices have even been falling in the PRC (at an annual rate of about 1%). Although recent months have witnessed a mild uptick in inflation in Korea and Thailand, it is still not a major cause for concern in either of these countries. To some extent, the low inflation environment in the region is structural, in that it is a side effect of the bursting of the precrisis asset price bubbles and credit excesses. The resulting problems of excess capacity and stretched balance sheets are reflected in the decline in the pricing power of firms, leading to a low inflation environment—even as interest rate reductions and fiscal stimulus measures are helping domestic demand to hold up.

Asset Market Developments

Most of the region’s stock markets posted strong gains in the first half of the year, only to see these dissipate in the second half, despite the better-than-expected economic growth (Figure 8). As a result, with the exception of Indonesia and Thailand (where the year witnessed gains in stock prices), regional stock markets generally fell compared to the beginning of the year. Stock prices at the end of the year were lower by as much as 30% in the PRC (Shanghai-B share index) from the start of 2002. Stock prices fell by smaller magnitudes in the other countries ranging from 6% in Malaysia to 19% in Singapore. A combination of factors has contributed to this decline. These include sliding stock markets in industrial countries, a decline in net foreign portfolio inflows to the region (Box 2), and domestic economic problems (for example, an overshooting of the fiscal deficit target in the Philippines).

Despite the decline, with the exception of the PRC, regional stock markets managed to outperform many stock markets elsewhere. For example, in the US, last year’s stock market losses ranged from 17% in the Dow Jones index to 33% for NASDAQ. Losses in other major industrial countries ranged from 21% in Japan’s Nikkei 225 to 44% in Germany’s DAX.

In the real estate sector, office vacancy rates experienced mixed fortunes up to the third quarter of last year. During the first three quarters, office vacancy rates remained stable in Indonesia, Malaysia, and Philippines; increased in Korea and Singapore; and declined in the PRC and Thailand (Figure 9). The increases in office vacancy rates were

Box 2: Private Capital Flows: Are Foreign Banks Returning to the Region?

Reflecting continued global economic uncertainties, net private capital flows to the five crisis-affected countries fell to \$4.89 billion in 2002 from \$6.09 in 2001, according to the latest data from the Institute of International Finance (IIF). The reduction was largely caused by a reversal of net portfolio equity investment, from an inflow of \$10.09 billion in 2001 to an outflow of \$4.20 billion last year. Net direct equity investment also fell, from \$8.6 billion in 2001 to \$2.85 billion in 2002.

In contrast, net private credit from commercial banks and other private creditors staged a significant rebound in 2002. After withdrawing from the five countries a total of \$113 billion during 1997–2001, net lending by private

international lenders registered an inflow of \$6.24 billion last year, which offset large outflows of portfolio equity. For the first time since the Asian financial crisis, net lending by foreign commercial banks registered a positive level last year.

In 2003, IIF is projecting a private capital inflow of \$8.43 billion for the five countries. Net equity investment is expected to recover and reach \$6.9 billion, largely in the form of direct investment. Portfolio equity is also expected to return, reaching \$1.7 billion, reflecting a slightly improved outlook for the region's stock markets. On the other hand, net private lending is expected to soften to an inflow of \$1.53 billion.

Table 2.1: **Net Private Capital Flows to the Five Crisis-Affected Countries** (\$ billion)

	1995	1996	1997	1998	1999	2000	2001	2002f	2003f
Net Private Flows	93.31	115.32	3.39	-36.31	-5.75	17.23	6.09	4.89	8.43
Equity investment, net	16.09	16.76	5.18	17.62	30.76	25.44	18.68	-1.35	6.90
Direct equity investment, net	4.14	4.77	6.81	13.30	16.28	13.92	8.60	2.85	5.20
Portfolio equity investment, net	11.95	11.99	-1.62	4.32	14.49	11.53	10.09	-4.20	1.70
Private Creditors, net	77.22	98.57	-1.79	-53.93	-36.51	-8.21	-12.59	6.24	1.53
Commercial Banks, credit flows, net	63.73	69.16	-17.57	-48.39	-32.33	-12.52	-7.12	5.26	0.38
Other private creditors, net	13.49	29.41	15.78	-5.54	-4.19	4.31	-5.47	0.97	1.15

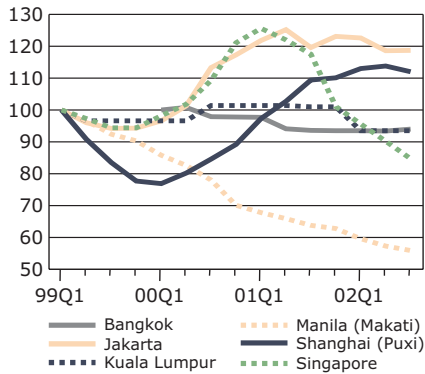
f = forecast

Source: Institute of International Finance.

generally accompanied by a softening of office rentals, whereas the decline in office vacancy rates in the PRC was accompanied by a hardening of rentals. (Figure 10). Indonesia and Thailand were exceptions to this inverse relationship between office vacancy rates and rentals. In both countries, office rentals declined, despite a fall in office vacancy rates in Thailand and more or less unchanged vacancy rates in Indonesia.

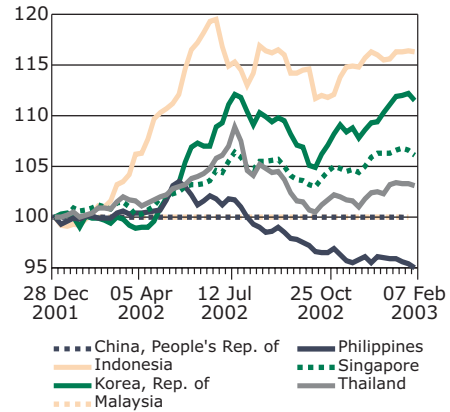
During 2002 (except for a short period during the third quarter), most of the region's currencies appreciated against the US dollar. The exceptions were the Philippines, where the overshooting of the fiscal deficit target steadily dragged the peso down, and the PRC and Malaysia, whose currencies are pegged to the US dollar (Figure 11). The appreciations were largely a reflection of the generalized weakening of the US dollar, although the degree varied, depending on certain factors. They ranged from about 3% in Thailand to about 17% in Indonesia.

Figure 10: **Rents** (per square meter per annum, local currency 1999Q1=100)



Source: Jones Lang LaSalle, *Asia Pacific Property Digest*, various issues.

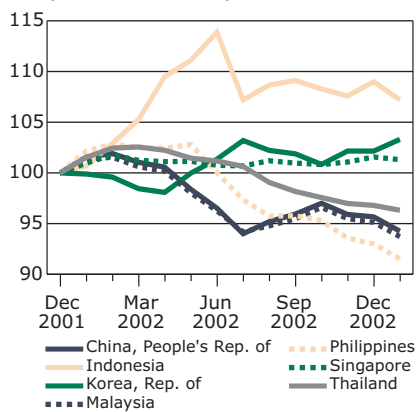
Figure 11: **Exchange Rate Indexes** (weekly average, last week of 2001Dec=100, \$/local currency)



Source: REMU staff calculations derived from Bloomberg data.

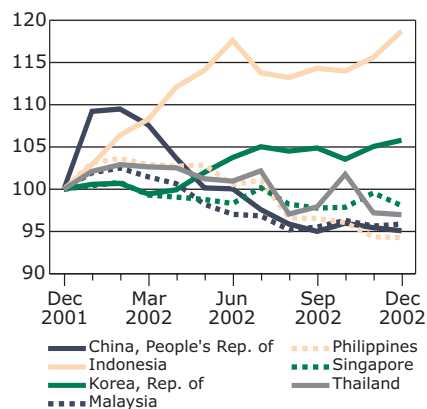
Both the yen and the euro also appreciated against the dollar. Regional currencies, therefore, generally depreciated in nominal effective terms (except in Indonesia and, to a lesser extent, in Korea and Singapore) (Figure 12). Since inflation rates are relatively low in the region, many countries enhanced their export competitiveness last year, apart from Indonesia and, to some degree, Korea, where currencies appreciated in real effective terms (Figure 13).

Figure 12: **Nominal Effective Exchange Rate** (Dec 2001=100)



Note: An increase is an appreciation. Trade weights are total trade from top 10 trading partners.
Source: REMU staff calculations.

Figure 13: **Real Effective Exchange Rate** (Dec 2001=100)



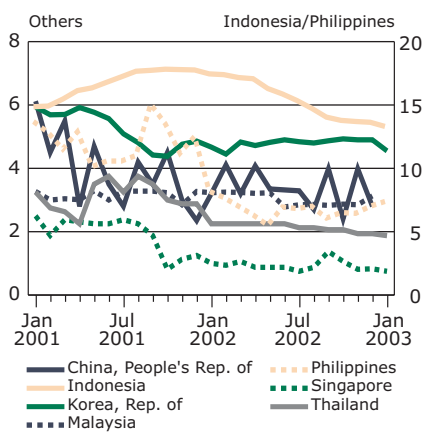
Note: An increase is an appreciation. Trade weights are total trade from top 10 trading partners.
Source: REMU staff calculations.

Fiscal and Monetary Policies

East Asian countries had responded to the 2001 economic slowdown with interest rate reductions and modest fiscal stimulus measures. Most of them continued to maintain this policy stance last year. By the end of 2002, short-term interest rates were below 5% in five of the seven ASEAN5+2 countries, the exceptions being Indonesia and the Philippines (Figure 14). Even in the Philippines, the short-term interest rate fell from about 15% in September 2001 to about 7% by the end of last year. The short-term interest rate also fell in Indonesia, but by much less—mainly because of the continued double-digit inflation last year. Meanwhile, short-term real interest rates are now below 1% in Korea, Singapore, and Thailand, whereas, it is just over 1% in Malaysia (Figure 15).

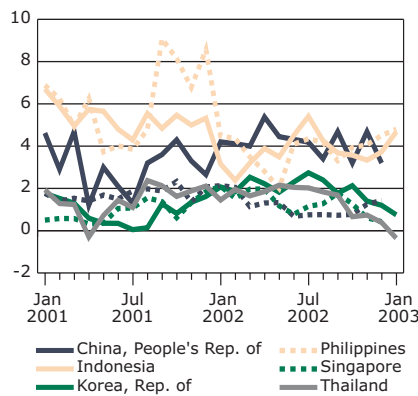
Except for Korea and Singapore, East Asian countries had planned for moderately expansionary fiscal policies in 2002. The budgeted fiscal deficits for 2002 among these countries ranged from 2.5% in Indonesia to 6.9% in Lao People’s Democratic Republic (Lao PDR) (Figure 16). As the year progressed, however, the actual fiscal outcomes have varied from the budgeted fiscal positions in several countries.

Figure 14: Short-Term Interest Rates¹ (nominal, %)



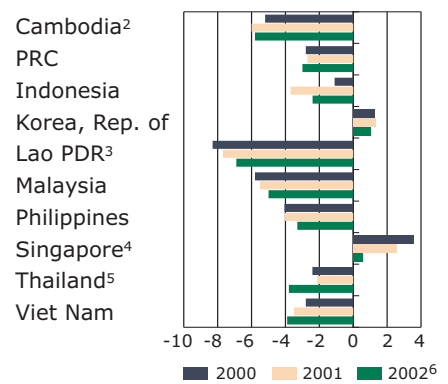
Source: ARIC Indicators.
¹Three-month interbank lending rates—PRC: Average trading rate in interbank borrowing and lending market (People’s Bank of China); Indonesia: Weighted average of banks’ interbank lending rates (Bank Indonesia); Korea: Certificate of deposit (3 months); Malaysia: Average of interbank deposit rates (Bank Negara); Philippines: PHIBOR (Bankers Association of the Philippines); Singapore: SIBOR (Association of Banks in Singapore); Thailand: Bangkok Bank’s interbank offer rate (Bangkok Bank).

Figure 15: Short-Term Interest Rates¹ (real, %)



Source: ARIC Indicators.
¹Three-month interbank lending rates—PRC: Average trading rate in interbank borrowing and lending market (People’s Bank of China); Indonesia: Weighted average of banks’ interbank lending rates (Bank Indonesia); Korea: Certificate of deposit (3 months); Malaysia: Average of interbank deposit rates (Bank Negara); Philippines: PHIBOR (Bankers Association of the Philippines); Singapore: SIBOR (Association of Banks in Singapore); Thailand: Bangkok Bank’s interbank offer rate (Bangkok Bank).

Figure 16: Fiscal Balance¹ (% of GDP)



¹Data refer to central government for Cambodia, PRC, Indonesia, Korea, Myanmar, Philippines, Singapore, Thailand, and Viet Nam; general government for Lao PDR; and federal government for Malaysia.
²Excludes grants.
³Excludes grants and for fiscal year ending September.
⁴Data are for fiscal year April-March. Revenues include Net Investment Income Contribution and the surplus/deficit excludes special transfers.
⁵Data are for fiscal year October-September.
⁶Based on programmed budget.
 Source: ARIC Indicators; IMF country reports (various issues), national web sites.

Actual fiscal developments were more or less on track in Malaysia, with expenditures and revenues roughly in line with budgeted levels. As a result, the actual deficit in 2002 was 4.7% of GDP, quite close to the targeted 5%. But actual fiscal developments diverged significantly from their budgeted levels elsewhere.

In the Philippines, actual expenditures exceeded budgeted levels only marginally but actual revenues fell significantly short. As a result, the fiscal deficit in 2002 turned out to be about P212 billion (5.3% of GDP), compared to P130 billion (3.3%) budgeted in the beginning of the year.

By contrast, actual fiscal developments turned out to be less expansionary than the budgeted stances in Indonesia, PRC, and Thailand. In Indonesia, revenues were on track with the budget, but expenditures were lower than the budgeted level by about 4%. As a result, the fiscal deficit turned out to be 1.7% of GDP, as against the programmed deficit of 2.5% of GDP. Coupled with the appreciation of the rupiah, this has contributed to a large reduction in Indonesia's public debt from about 90% of GDP at the beginning of last year to almost 70% by the end.

In the PRC, in the first 11 months of the fiscal year (January–December), expenditures and revenues both grew faster than planned. However, since revenues grew faster (compared to their expected rates of growth in the budget), the actual fiscal deficit was lower than the planned deficit of CNY310 billion for the full year.

Thailand's experience was similar to that of the PRC. During the fiscal year (October–September), revenues grew much faster than planned, mainly due to an improved economy and better tax collections. As a result, at 2.9% of GDP (or about B155 billion), the actual fiscal deficit for the year turned out to be significantly lower than the budgeted deficit of 3.8% of GDP (B200 billion).

In Korea, in the first 11 months of the fiscal year (January–December), actual expenditures were largely in line with budgeted levels. However, because of a better-than-expected rise in revenues (from value added tax and sale of government stocks in Korea Telecom Corporation), the consolidated budget posted a surplus of W24.4 trillion during the period, which is much higher than the budgeted surplus for the full year (W6 trillion). Similar trends in Singapore in the first six months of the fiscal year (April–March) resulted in a much larger fiscal surplus than was planned in the budget.

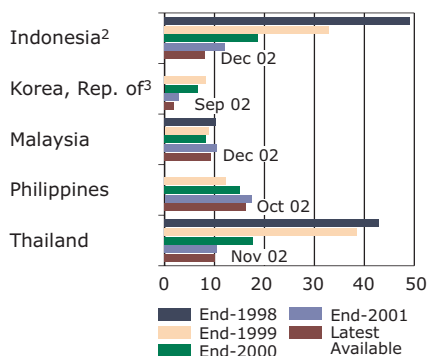
Progress in Financial and Corporate Restructuring and Reforms

Nonperforming Loans, Capital Adequacy, and Bank Profitability

Reflecting improved economic performance and progress in financial restructuring, last year the five crisis-affected countries saw reductions in the ratio of nonperforming loans (NPLs) in commercial banks' balance sheets. The reductions ranged from 4 percentage points in Indonesia, about 1 percentage point in Korea, Malaysia, and Philippines, to 0.5 percentage point in Thailand, with declines in the volume of NPLs being accompanied by increases in the total loan portfolio in many cases. Toward the end of last year, the NPL ratio stood at 16.3% in the Philippines, 10% in Thailand, 9.3% in Malaysia, 8.1% in Indonesia, and a little under 2% in Korea (Figure 17). These figures compare favorably with those at the peak of the Asian financial crisis for most of the countries.

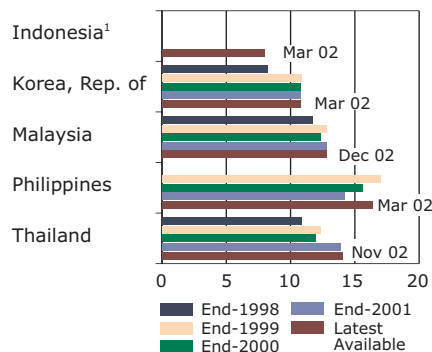
The latest available data for banking sector capital adequacy ratios (CARs) ranged from about 8% (the Basel minimum norm) in Indonesia, more than 11% in Korea, to 13–17% in Malaysia, Thailand, and Philippines (Figure 18). The ratios changed little from those at the beginning of 2002, with the exception of the Philippines where there was a sizable increase.

Figure 17: **NPLs¹ of Commercial Banks** (% of total commercial bank loans)



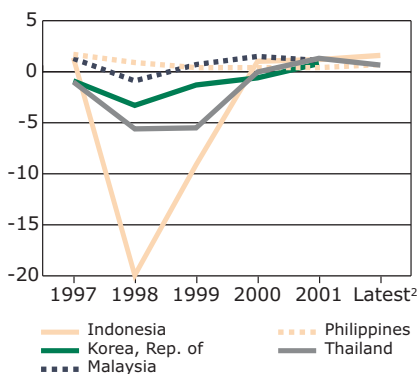
¹Data on NPLs exclude those transferred to AMCs. NPLs are on a three-month accrual basis.
²Refer to NPLs in banking sector.
³NPL criteria were changed in December 1999, so no comparable data are available prior to that date.
 Source: ARIC Indicators.

Figure 18: **Capital Adequacy Ratios of Commercial Banks** (%)



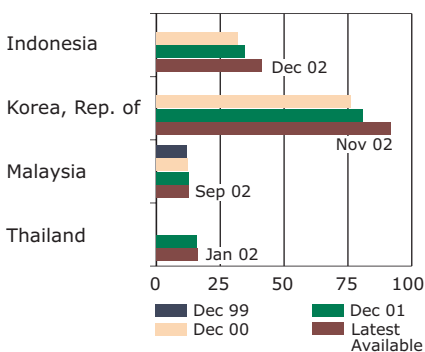
¹Refers to CAR of the banking system.
 Source: ARIC Indicators.

Figure 19: Banking Sector Profitability¹ (%)



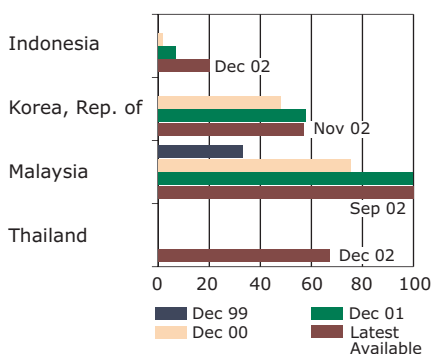
¹Data refer to return on assets of commercial banks, with the exception of Malaysia, which refers to the banking/financial system.
²Latest data refer to annualized estimates: Indonesia (May 2002), Philippines (June 2002), Thailand (September 2002).
 Sources: Web sites of the Bank Negara Malaysia, Bank of Indonesia, Bangko Sentral ng Pilipinas, Bank of Thailand, Financial Supervisory Service Korea.

Figure 20: NPLs Purchased by AMCs (\$ billion)



Source: REMU staff calculations based on data from KAMCO, Danaharta, IBRA, and TAMC.

Figure 21: NPLs Disposed of by AMCs¹ (% of NPLs purchased)



¹Refer to those by IBRA in Indonesia, KAMCO in Korea, Danaharta in Malaysia, and TAMC in Thailand, as of dates indicated.
 Source: ARIC Indicators.

Having recovered from negative levels during the crisis years, profitability of banks continued to consolidate in all of the five crisis-affected countries. Latest data suggest that the rate of return on bank assets ranged from 0.5% to 0.8% in Thailand, Philippines, and Korea, and stood at 1.1% in Malaysia and 1.6% in Indonesia (Figure 19).

Asset Resolution by Asset Management Companies

Centralized asset management companies (AMCs) continued to make progress in resolving bad debt under their management in Indonesia, Korea, Malaysia, and Thailand. As of late 2002, the cumulative volume of NPLs transferred from banks and other financial institutions to centralized AMCs ranged from \$12.6 billion in Malaysia to \$91.7 billion in Korea (Figure 20).

The progress in debt resolution by centralized AMCs has varied across the four crisis countries that instituted them. In Malaysia, Danaharta had resolved all NPLs in its portfolio by September 2002, projecting an expected recovery rate of 57%. However, the recent challenges to Danaharta’s immunity from legal actions and a court case against it have clouded an otherwise solid reputation. Meanwhile, as of November 2002, the Korea Asset Management Corporation (KAMCO) had resolved 57.2% of the face value of NPLs purchased from financial institutions since 1997, and it is expecting a recovery rate at about 47%. KAMCO has stopped acquiring distressed loans from the special public fund. In Thailand, debt resolution by the Thai Asset Management Corporation (TAMC) reached the targeted 67% of the total book value of impaired assets under its management by the end of 2002, with an estimated average recovery rate of 45%. TAMC expects to complete the restructuring of all B759 billion in debts in its portfolio by the end of 2003. In contrast, debt resolution by the centralized AMC has proceeded much slower in Indonesia. As of December 2002, the Indonesian Bank Restructuring Agency (IBRA) had disposed of only about 20% of the total assets under its management. In addition, another 19% had reached the stage of signing a memorandum of understanding or implementing restructuring proposals (Figure 21).

Unlike the other crisis-affected countries, the Philippines did not establish a centralized AMC in the aftermath of the crisis, relying instead on banks to work out their own NPLs. Last year, however, in response to the rising level of NPLs, the Government proposed a bill for the creation of specially designed AMCs or special purpose vehicles (SPVs). The SPV law, which lays out the framework for and grants tax perks to SPVs, was signed by the country’s President early this year. The SPVs

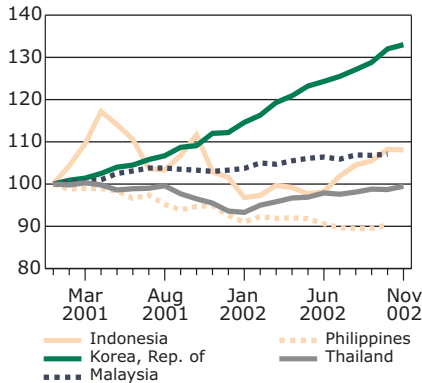
will acquire, turn around, and resell the financial sector's distressed assets, estimated at P600 billion or about 16.9% (as of September 2002) of the total assets of the banking system.

Voluntary Corporate Workouts

Last year, progress was also made in debt restructuring under voluntary workout schemes.

- **Indonesia.** As of December 2002, the Jakarta Initiative Task Force (JITF) had worked out about \$18.9 billion out of the total \$29 billion in distressed corporate debt that it had been tasked to help restructure, meeting the target agreed with the International Monetary Fund (IMF). The amount of debt restructuring reached \$4.7 billion in 2002 alone. JITF now has a year left to complete restructuring of the remaining \$10 billion of distressed debt, as the agency's mandate is scheduled to expire by the end of 2003.
- **Malaysia.** The Corporate Debt Restructuring Committee (CDRC) officially ceased operation in August 2002 after it successfully restructured 47 cases or 98% of those it accepted, worth RM43.97 billion in face value.
- **Thailand.** By the end of November 2002, the Corporate Debt Restructuring Advisory Committee (CDRAC) had approved workout of 15,385 cases of target debtors with credits outstanding of B2,625 billion in face value to enter the CDRAC process. Of these, 10,303 cases worth B1,372 billion had been successfully restructured, while 4,994 cases worth B1,287 billion were still in the process of restructuring or subject to court litigation. In the meantime, from 1998 to October 2002, financial institutions themselves successfully restructured 538,468 cases worth B2,664.6 billion in face value, with 40,142 cases worth B124.8 billion still under the restructuring process.
- **Korea.** Significant progress was made in restructuring the top five *chaebols* in 2002. The latest development was the approval by the creditor financial institutions of Hynix Semiconductor Inc. of a W4.9 trillion (\$4 billion) debt restructuring last December. This was the third debt restructuring in two years led by the Korea Exchange Bank, the main creditor bank, to keep the world's third-largest chipmaker afloat. The rescue package includes a swap of W1.9 trillion of debt into equity and a rollover of W3 trillion of debt by 2006. The restructuring package also includes the sale of assets to pay some of its debt and to generate cash to invest in new technology. The planned debt-equity swap and an associated share consolidation will reduce Hynix's debt-to-equity ratio to 71% from 147%.

Figure 22: Real Bank Credit¹—Five Crisis-Affected Countries
(Jan 2001=100),
seasonally adjusted



¹Claims on the private sector: deposit money banks.
Source: ARIC Indicators.

Trends in Bank Credit

In the post-crisis period, real bank credit recovered fairly quickly in Korea followed by Malaysia. Presently, the stock of real bank credit to the private sector is about 77% higher than pre-crisis levels in Korea and 16% higher in Malaysia. For the first time since the Asian financial crisis, last year saw the stock of real bank credit to the private sector increase in Indonesia and Thailand also (Figure 22), suggesting that reforms are starting to bear fruit. It is only in the Philippines that real bank credit continues to be sluggish.

In the first 11 months of last year, private sector credit in Korea rose by 18.5%, driven largely by lending to the household sector. The rapid growth in household debt has, however, caused some concern and prompted Government tightening. In Malaysia, in the first 10 months of last year, real credit grew by 3.7%. The prevailing low interest rate environment increased the amount of loans approved, most notably for consumer credit and the purchase of automobiles. In Indonesia and Thailand also, bank lending expanded in 2002, with the stock of real bank credit to the private sector growing by over 6% in both countries from January to November 2002. In contrast, there was no sign of a revival in bank lending in the Philippines, with the stock of real bank credit falling by 2.5% in the first 10 months of last year.

Reforms of the Regulatory and Supervisory Framework

- **Indonesia.** In the last few years, the Government’s focus has largely been on restructuring troubled financial institutions. But the country has also introduced measures to improve the financial supervision and regulatory framework. In 2002, Bank Indonesia (BI) took actions to comply with the Basle Core Principles for Effective Banking Supervision, including moving toward consolidated supervision. More recently, in response to the recent expansion of bank lending to small- and medium-sized businesses, BI has taken steps to ensure that credit to this sector follows prudential principles. Following the passage of the money-laundering bill in March 2002, the central bank in December 2002 established the Financial Transaction and Report Analysis Department in an attempt to block financing channels to terrorists. To further enhance its banking supervision, the BI is considering shifting its supervisory function to a new body to be established—the Financial Service Authority.
- **Korea.** There has been significant progress in strengthening financial supervision and regulation in Korea since the 1997 financial crisis, to

bring them in line with international standards. In 2002, the Financial Supervisory Service (FSS) issued new guidelines aimed at lowering the ratio of loans classified as substandard, doubtful, or presumed loss that were held by nonbank financial institutions (NBFIs) to improve overall asset quality. It also instituted new minimum mandatory loan loss provisioning ratios for domestic banks' household loans and credit card services. More recently, FSS announced regulatory changes that will become effective in the first half of this year. The minimum mandatory Bank for International Settlements (BIS) CAR is to be increased from 4% to 5% for mutual saving banks. For new unsecured small loans made after 1 January 2003, the BIS risk weighting will increase from 50% to 75% by the end of March and to 100% in April. Other regulatory changes include those related to online securities trading, credit card services, and automobile insurance. The Government is looking at ways to restructure and improve the financial supervisory system. The incoming administration has promised continued and deeper *chaebol* reform.

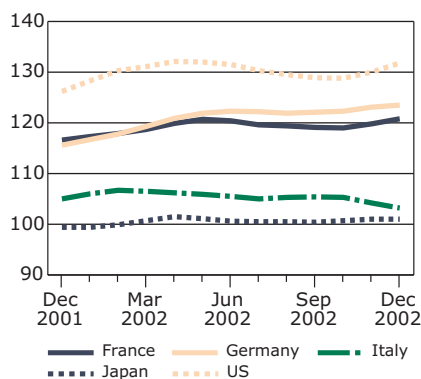
- **Malaysia.** With a view to integrating the domestic financial system with global markets over a 10-year period, the Government adopted the Financial Sector and Capital Market Master Plans two years ago. Under the two plans, the system of financial regulation and supervision is to be brought in line with international standards. The focus of policy in the banking sector has now shifted from addressing balance sheet problems to enhancing operational efficiency and quality of services. Bank Negara Malaysia (BNM) has taken initiatives to develop a quality service index to benchmark and assess the quality of banking service. BNM is to liberalize controls over product approval and encourage banks to develop new products and services. In the meantime, the Government is pressing for further consolidation of the banking industry to raise banks' capital adequacy and enhance profitability.
- **Philippines.** Bangko Sentral ng Pilipinas (BSP), the country's central bank, has continued to introduce various policy initiatives to implement the General Banking Law that was introduced in 2000. The more recent of these initiatives include, among others, amendments to the Manual of Regulations for Banks and Nonbank Financial Institutions concerning the publication of the consolidated statements; guidelines in determining whether a particular business activity is unsafe or unsound; rules and regulations governing the amortization of loans and other credit accommodations; and limits on the equity investments of banks in enterprises. After some delay, the Senate finally passed the SPV bill in October 2002 that would allow the creation of AMCs to help clean out banks' nonperforming

assets. The country's President signed the bill into law in January 2003.

- **Thailand.** Over the past few years, loan classification, provisioning, and interest accrual and capital adequacy rules have been tightened in Thailand to bring them up to international standards. To further promote sound corporate governance practices in the banking sector, the Bank of Thailand (BOT) recently announced various policy measures. These cover guidelines on board composition, appointment of independent boards of directors, establishment of board committees, and audit and risk management committees in commercial banks. The BOT also plans to establish a Deposit Guarantee Institute that will protect 100% of bank savings up to a maximum of B1 million. Rules have also been introduced to permit commercial banks to engage in investment advisory services and in arranging, underwriting, and dealing in debt securities. To improve profitability of the sector, the Government recently asked the BOT to consider allowing big banks to acquire smaller unprofitable ones. The central bank announced new regulations on credit card services to control the rapid growth of credit card usage late last year.

Prospects for East Asia's Growth and Recovery

Figure 23: **OECD Leading Indicators**



Source: OECD web site.

External Economic Environment

Since the release of the October 2002 AEM, the external economic environment facing East Asia has turned less favorable for two reasons. First, baseline growth forecasts for industrial countries have been marked down.² Second, downside risks to these baseline forecasts have increased, especially with the mounting tensions over Iraq. The projected turnaround in the global economy has been postponed by one or two quarters. Recent trends in leading indicators for US, Germany, and France suggest that global economic growth could pick up in the latter part of this year (Figure 23).

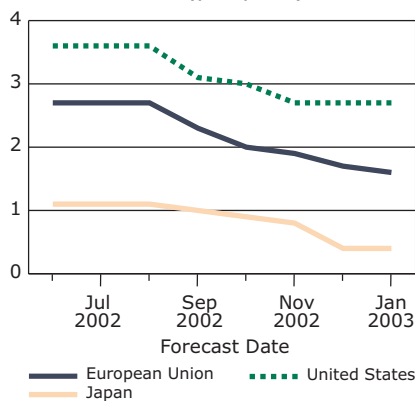
The US economy grew by 2.4% last year and the projected growth rate this year is expected to be only slightly higher. Judging by recent figures on consumer confidence,³ the outlook for personal consumption

²Despite this downward revision, the G3 countries taken together are expected to grow by 1.9% this year compared to 1.4% last year (using 2001 GDP weights).

³In December 2002, the Conference Board's consumer confidence index slipped below the lows it had reached in the immediate aftermath of the attacks of 11 September 2001.

in the US, which has held up well in recent years, appears uncertain. In fact, the threat of possible military action against Iraq and the surge in oil prices have added to consumer caution. In the fourth quarter of last year, consumer spending increased by the lowest level in a decade. Therefore, despite the proposed \$674 billion fiscal stimulus package, growth in personal consumption is forecast to soften this year from the 3.1% increase that it posted last year. Growth in industrial production, after being positive during the first seven months of last year, remained in negative territory in four out of the five remaining months of the year. Moreover, there is no marked indication of an upturn in business sentiment and fresh hiring. The Institute of Supply Management (ISM) services sector survey continues to show that employment in the sector is faltering. Given that services account for more than half of consumer spending and 80% of US employment, this is a cause for concern. Without a significant turnaround in business sentiment, the much-needed pickup in business investment, which shrank by about 5% in 2001 and another 6% in 2002, will perhaps not materialize. In the fourth quarter of last year, business investment increased a little for the first time in two years, but this increase could be difficult to sustain in view of the prevailing uncertainties. Although US factory orders rebounded in December (and the ISM’s factory manufacturing index in January indicated expansion three months in a row), a large part of this rebound has been led by demand for defense equipment. Reflecting these considerations, US GDP is now forecast to grow by 2.7% this year, lower than the October 2002 forecast of 3% (Figure 24). Within the year, growth in the first half is expected to be below 2% (on a y-o-y basis), while it is expected to pick up pace in the second half to about 3%.

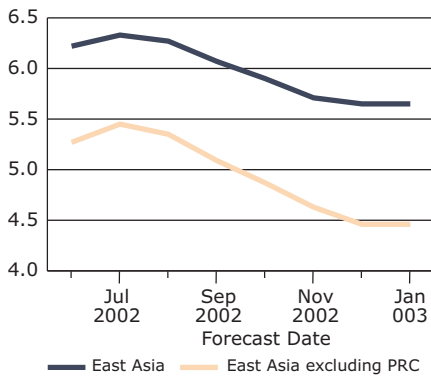
Figure 24: **Consensus Forecasts of 2003 GDP Growth—G3** (y-o-y, %)



Source: Consensus Economics Inc., *Consensus Forecasts*, various issues.

To a large extent, exports enabled the European Union (EU) to post GDP growth last year of about 1%. Since domestic demand in Europe is weak and the US is a major export market for some of the bigger EU economies such as France, Germany, Italy, and UK, the downward revision of the US growth outlook has adverse implications for their growth prospects. Moreover, unlike the US, Germany—the largest economy in the EU—has no fiscal levers to spur growth this year. In fact, Germany has already been warned by the European Commission for breaching the fiscal deficit target under the Stability and Growth Pact, and is now bound to reduce the fiscal deficit significantly this year from last year’s estimated level of 3.8% of GDP. Against this backdrop, European growth prospects for next year have been revised down, close on the heels of the downward revisions to US forecasts. In October 2002, the EU’s GDP was forecast to grow by 2% in 2003, but that has been lowered to 1.6%. Within the EU, the corresponding

Figure 25: **Consensus Forecasts¹ of 2003 GDP Growth—East Asia (y-o-y, %)**



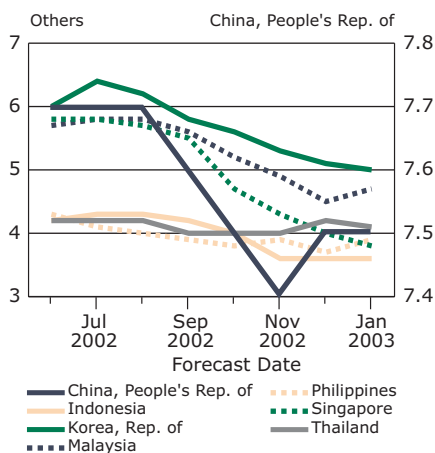
¹Based on Consensus Economics forecasts, except for small countries, which are from the *Asian Development Outlook* and IMF country reports.
²East Asia includes ASEAN countries (except Brunei Darussalam and Myanmar) plus PRC and Korea.

revisions are from 1.5% to 0.9% for Germany; from 1.9% to 1.6% for France; from 1.8% to 1.4% for Italy; and from 2.5% to 2.3% for the UK.

Last year, Japan’s economy contracted by 0.3%. In October 2002, the forecast for this year’s GDP growth was close to 1%, but this has now been trimmed to 0.4%. The Bank of Japan’s quarterly Tankan survey for December 2002 pointed to a weakening of future expectations of business sentiment and capital expenditures. The unemployment rate also increased from 5.3% in November to a post-World War II high of 5.5% in December. Meanwhile, the stock market is at a 20-year low. Although business investment is expected to improve from the 6% contraction it suffered last year, it still is not expected to post positive growth this year. Moreover, anticipation of further job cuts by firms (on top of the 2.6 million jobs shed since 1997), continued deflation (for the fourth consecutive year), and the uncertainty over financial sector restructuring are eroding consumer sentiment. As a result, private consumption, which is estimated to have grown by more than 1% last year, is forecast to rise by just 0.3% in 2003.

Using the 2001 GDP weights, forecast GDP growth in 2003 of the G3 countries now works out to 1.9%, lower than both the October 2002 forecast of 2.2% and the June 2002 forecast of 2.8%. The geopolitical risks arising from the possible US military action against Iraq are causing further uncertainty to consumers and investors around the globe, further exacerbating the weakening external environment confronting East Asia.

Figure 26: **Consensus Forecasts¹ of 2003 GDP Growth—ASEAN5+2 (y-o-y, %)**



Source: Consensus Economics Inc., *Asia Pacific Consensus Forecasts*, various issues.

Regional Economic Outlook

The recent worsening of the external environment will impinge on East Asia’s immediate economic prospects. In a few East Asian countries, such as Korea and Thailand, tighter policies to contain consumer credit will also dampen the growth momentum. As a result, East Asia’s growth is expected to moderate somewhat this year to 5.6% (Table 1), according to the January forecast of Consensus Economics. This is lower than its forecasts of 6.3% in July 2002 and 5.9% in October 2002 (Figure 25). Next year, growth should pick up to about 6%.

Among the ASEAN5+2 countries, the highest downward revisions to this year’s growth forecast from October 2002 are for Singapore, followed by Korea, Malaysia, and Indonesia (Figure 26). Those for PRC, Philippines,

Table 1: Annual GDP Growth Rates (%)

							January 2003 Forecasts		Difference ¹	Average	
	1997	1998	1999	2000	2001	2002	2003	2004	2003	1987-1996	1998-2002
Brunei Darussalam	3.6	-4.0	2.6	2.8	1.5	4.1	...	...	...	1.4	1.4
Cambodia	3.7	1.5	6.9	7.7	6.3	4.5	5.0	6.0	-1.0	6.2	5.4
PRC	8.8	7.8	7.1	8.0	7.3	8.0	7.5	7.6	0.0	10.0	7.6
Indonesia	4.7	-13.1	0.8	4.9	3.3	3.5	3.6	4.1	-0.4	7.6	-0.1
Rep. of Korea	5.0	-6.7	10.9	9.3	3.0	6.2	5.0	5.4	-0.6	8.1	4.6
Lao PDR	6.9	4.0	7.3	5.8	5.7	5.8	5.8	...	0.0	5.2	5.7
Malaysia	7.3	-7.4	6.1	8.3	0.4	4.0	4.7	5.4	-0.5	9.1	2.3
Myanmar	5.7	5.8	10.9	6.2	...	...	...	...	...	2.7	...
Philippines	5.2	-0.6	3.4	4.4	3.2	4.6	3.9	4.2	0.1	3.7	3.0
Singapore	8.5	-0.1	6.9	10.3	-2.0	2.2	3.8	4.9	-0.9	9.1	3.5
Thailand	-1.4	-10.5	4.4	4.6	1.8	4.9	4.1	4.4	0.1	9.5	1.1
Viet Nam	8.2	4.4	4.7	6.1	5.8	6.3	6.7	7.0	0.3	7.0	5.5
East Asia ²	6.2	-1.4	6.9	7.6	4.3	6.1	5.6	6.0	-0.3	8.8	4.7
East Asia exc. PRC ²	4.5	-7.3	6.8	7.4	2.4	4.9	4.5	4.9	-0.4	8.0	2.8
ASEAN ²	4.2	-7.8	3.7	6.0	1.9	4.0	4.1	4.6	-0.3	8.0	1.6
ASEAN5+2	6.2	-1.5	6.9	7.7	4.3	6.1	5.6	6.0	-0.3	1.7	4.7
Five Crisis-Affected	4.1	-8.2	6.8	7.2	2.7	5.1	4.5	4.9	-0.4	8.0	2.7

... = not available

¹Difference from October 2002 AEM.

²Exclude Brunei Darussalam and Myanmar for all years and Lao PDR for 2004 since GDP growth for Lao PDR is not available for 2004.

Source: Asian Development Bank, *Asian Development Outlook Update 2002*, October 2002; official sources; Consensus Economics Inc., *Asia Pacific Consensus Forecasts*, October 2002 and January 2003; Department of Economic Planning and Development, *Brunei Economic Bulletin*, October 2002; Council for Social Development (Cambodia), National Poverty Reduction Strategy 2003-2005 (December 2002).

and Thailand have been left largely unchanged. Outside this group, Viet Nam's growth forecast for this year has, in fact, been revised up.

➤ **Singapore.** Singapore's economy was already slowing in the last quarter of 2002, when GDP growth declined to 2.6% from 3.9% in the previous quarter. In October 2002, Singapore's GDP was predicted to grow by 4.7% in 2003, which already represented a major downscaling from the 5.8% forecast of July 2002. Being a highly open economy, the recent weakening of the external environment has forced a further downward revision of the 2003 growth forecast to 3.8%. As for Singapore's export growth forecasts, in October 2002, Consensus Economics saw this reaching more than 9% in 2003, but that figure has now been lowered to 7%. Growth in private consumption and fixed investment has also been revised down—to 2.4% (compared to 3.9% forecast in October 2002) and 1.7% (compared to 4.6% forecast in October 2002), respectively, this year. Singapore's economy is still suffering from the post-bubble trauma of the information technology sector, leaving the country with excess manufacturing capacity, significant commercial property vacancies, and a fragile job market. All these are expected to suppress consumer spending and private investment. Moreover, being a highly open economy, the scope for fiscal pump priming to spur growth is also limited, as the large import-propensity tends to lower the multiplier

effects of such policies on GDP. Against this backdrop, Singapore is more likely to rely on supply-side policy measures to support growth. The Economic Review Committee has already recommended several such measures, including removing barriers to entry, cutting taxes, privatizing public enterprises, enhancing wage and labor market flexibility, and upgrading human capital.

- **Korea.** In October, forecasts put Korea's GDP growth at 5.6% in 2003—already representing a significant downscaling from the 6.4% forecast of July 2002. That figure has been further scaled down to 5%, underpinned by a moderation in exports and domestic demand. Exports are forecast to grow at 7.3% this year (compared to the 7.8% forecast of October 2002). As for domestic demand, consumer spending is expected to recede to a more sustainable pace, after booming through most of 2002 with the help of aggressive bank lending to households that has since been tempered. Household consumption forecasts have been moderated to 4.6% from 5.3% in October 2002, while the forecast for 2003 fixed investment growth has also been scaled down—from 5.6% to 4.1%. Korea's near-term economic prospects would also depend on the policies of the new government, which will take office on 25 February. On a positive note, against a background of subdued inflation and cooling consumer demand, Korea has the flexibility to use fiscal policy to support domestic demand and growth, especially since the fiscal position is comfortable.

- **Malaysia.** In October 2002, Malaysia was forecast to grow by 5.2% in 2003. That has been trimmed to 4.7%, because of lower growth in exports, private consumption, and fixed investment. This year, export growth has been lowered from 9% in October 2002 to 7.7% now. The corresponding downward revisions in forecasts of private consumption and fixed investment are from 5.9% to 5.2% and from 5.8% to 4.5%, respectively. The prospect of US military action against Iraq, along with soft external demand, does not bode well for the Malaysian economy. However, on an encouraging note, the country's tourism industry, which accounts for about 7% of GDP and expanded at an annual rate of 40% during 1999–2001, does not seem to have suffered much in the aftermath of the Bali bombings of October 2002. Moreover, fiscal policy remains expansionary, although the Government has budgeted for a smaller fiscal deficit (3.9% of GDP) for 2003 compared to 2002 (4.7%). Given the comfortable fiscal position, there is also further scope for additional fiscal stimulus through supplementary budgets, and given the low inflation and the stability of the exchange rate, there is also room for interest rate cuts.

- **Indonesia.** Security concerns following the Bali bombings and a deteriorating external environment have led to a downward revision of Indonesia's 2003 GDP growth forecast from 4% in October 2002 to 3.6%. Slowing export growth is becoming a cause for concern. Reflecting this, Consensus Economics now forecasts zero export growth for 2003 (against 7.3% forecast in October 2002), despite rising international oil prices. This partly reflects the expected softening of nonoil commodity prices in the international markets. In addition, private consumption and fixed investment are expected to grow at a slower pace in 2003 than was foreseen in October last year. Private consumption growth has been downscaled from 4.5% to 3.9%, while private investment growth has been slashed from 5.3% to 1.4%. Indonesia is constrained in using either fiscal or monetary policy levers to spur growth: the large public debt constrains fiscal expansion, while the continued double-digit inflation limits the scope for interest rate reduction. It is, however, encouraging that the Government has made significant progress in addressing terrorism issues in the aftermath of the Bali bombings.
- **PRC.** Despite the worsening external environment, the PRC's forecast GDP growth of 7.5% for 2003 remains unchanged from October 2002, for several reasons. First, the effect of any export slowdown on the PRC's growth is likely to be relatively small, given the country's relatively low export-GDP ratio. Second, domestic demand is expected to post strong growth, offsetting any export slowdown: the forecast for 2003 retail sales growth remains unchanged at about 9% whereas growth in fixed investment is now seen to reach 13.5%, up from the 12.8% forecast in October 2002. Third, in preparation for the opening up of the huge domestic market, foreign direct investment in the PRC is expected to continue to be strong in 2003. Last, the PRC could maintain its expansionary fiscal stance this year, given the importance that the Government attaches to the need for the generation of substantial fresh jobs (of about 10 million each year to absorb about 5 million laid-off workers from State enterprises each year and another 5 million new entrants to the urban labor market, not to mention significant excess labor in rural areas).
- **Philippines.** The latest 2003 growth forecasts for the Philippines and Thailand hover around 4% (3.9% for the Philippines and 4.1% for Thailand). These forecasts are a shade higher than those foreseen in October 2002. The Philippines is constrained in using fiscal expansion to spur growth, given the overshooting of the fiscal deficits and the negative market sentiment that it has evoked. Moreover, the Philippine fiscal deficit is relatively structural in nature

Figure 27a: **Composite Leading Indicators—Malaysia, Philippines, and Thailand**

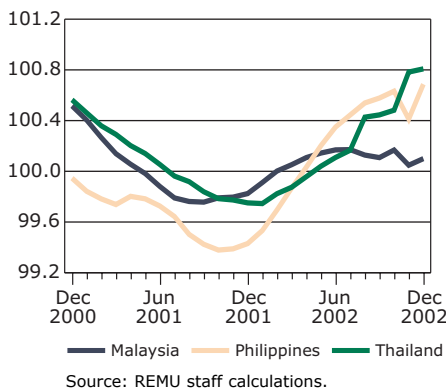


Figure 27b: **Composite Leading Indicators—Korea**



in that it is more due to a continued low tax-GDP ratio (due to inadequate tax compliance/enforcement rather than low statutory tax rates) than expenditure excesses, which makes it difficult to correct over a short period. The country’s public debt is also sizable in relation to GDP.

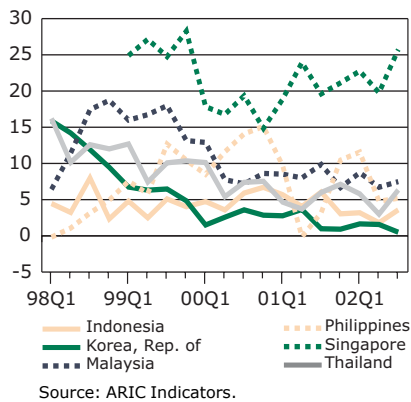
- **Thailand.** Meanwhile, in Thailand, any export slowdown is likely to be offset by improvements in fixed investment. Last year’s buoyancy of corporate tax collections indicate that corporate profits are steadily edging up, and this should induce robust growth in investment. Fixed investment is expected to grow at 5%, somewhat higher than the October 2002 forecast of 4.6%. Private consumption, which is estimated to have grown by around 4% last year, is expected to maintain that momentum. Given the negligible inflation, there is the option of cutting interest rates to spur domestic demand, if necessary. Moreover, unlike Indonesia and the Philippines, Thailand has some scope for fiscal expansion should the need arise, although the budget for 2003 (October 2002 to September 2003) plans for significant fiscal consolidation, with a reduction in the fiscal deficit to less than 1% of GDP from last year’s actual level of 2.9% of GDP.
- **Viet Nam.** Viet Nam’s GDP is forecast to grow by 6.7% this year, representing an improvement from both the October 2002 forecast of 2003 growth (6.4%) and last year’s actual growth (6.3%). Strong domestic demand, driven partly by growth in private investment and partly by expansionary fiscal policy, is expected to underpin this improved outlook.
- **Cambodia and Lao PDR.** Among the other countries in the region, this year Cambodia is expected to improve upon last year’s performance and post GDP growth of about 5%, while Lao PDR is expected to more or less maintain last year’s growth momentum of close to 6%.

Composite leading indicator series calculated by REMU for the Philippines and Thailand, and from official sources for Korea, have been trending up in recent months (Figures 27a and 27b). This suggests some pickup in economic growth in the latter part of the year.

Risks to Regional Growth and Recovery

The New Year started on a less-than-optimistic note, with a worsening external environment forcing a modest downward revision to East Asia’s growth prospects in 2003. Going forward, the key question is, as the year progresses, whether there are likely to be more risks to further dampen the region’s outlook.

Figure 28: **Current Account Balance** (% of GDP)



Both the July and October 2002 issues of AEM noted that in the face of improved political stability and prudential indicators around the region, domestic risks to East Asia’s rebound had been receding. Although the October 2002 bombings in Bali added a note of caution, by and large, that assessment still largely holds. Prudential indicators suggest a more stable outlook, with (i) all the major countries in the region continuing to run current account surpluses (Figure 28); (ii) foreign exchange reserves improving significantly and more than covering the entire short-term external debt (Figure 29); (iii) the short-term to total external debt and total external debt to GDP ratios lower than those at the height of the 1997 crisis (Figures 30 and 31); and (iv) banking sectors in the region slowly returning to health, although the agenda of restructuring and reforms is far from complete. Reflecting many of these improvements, international credit rating agencies have improved their assessments for several countries in the region, except for the Philippines whose outlook has recently been changed from “stable” to “negative” mainly due to fiscal concerns (Table 2). Overall, therefore, there are no major domestic risks on the horizon that could significantly upset the economic outlook for East Asia.

Figure 29: **Short-Term External Debt** (% of Gross International Reserves)

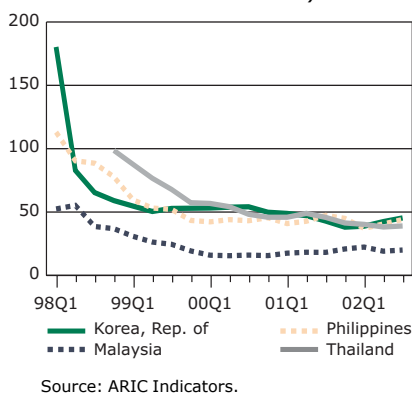


Figure 30: **Short-Term External Debt** (% of Total External Debt)

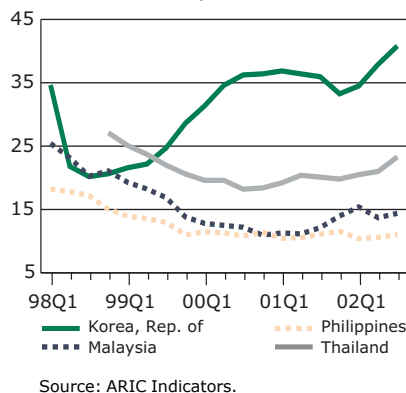
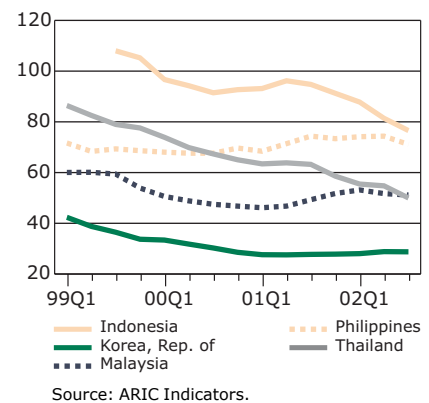


Figure 31: **Total External Debt** (% of GDP)



On the external front, however, the tensions over Iraq have already led to rising economic uncertainty, decreases in business and consumer confidence, and higher oil prices, which since mid-June 2002 have risen by about 30%. These tensions were partly responsible for the lower East Asian growth forecasts for 2003.

If the tensions escalate into a war, the impact would depend on its scale and duration. A short military operation could lead to only a temporary spike in oil prices, followed by a sharp decline. Under this scenario, the average price of oil this year could be more or less the same as last year (about \$25 per barrel), and the baseline growth forecast for East Asia would not be affected substantially. On the other hand, a long drawn-out war that inflicts extensive damage to the Middle East's oil fields would have a more adverse impact on the global economy and East Asia's growth prospects. Oil prices could even spike up to \$100 per barrel and remain at this high level for a long period, although the likelihood of this scenario appears low.

The deteriorating external environment, weakening growth prospects, and excess capacities across sectors pose major challenges for policymakers in East Asia. As the October 2002 AEM noted, appropriate policy responses in such a situation would be to cut interest rates and further ease the fiscal policy stance. Countries in the region should, therefore, closely monitor the emerging economic situation and stand ready to initiate such policy responses. The case for interest rate reductions is especially strong, as the spread between short-term interest rates in most East Asian countries and US rates has widened because most central banks in the region have not fully followed the latest rate cuts by the US Federal Reserve. As for fiscal policy, except for Indonesia, Philippines, the smaller economies such as Cambodia and Lao PDR, and—to a lesser extent—Thailand, there is reasonable scope for easing, should the need arise.

Fiscal and monetary easing should, however, be reinforced by pursuit of the remaining agenda of financial and corporate sector restructuring and reforms. This is crucial, as the low inflation being seen in the region is not entirely cyclical. At least partly, the region's low inflation environment is a result of structural factors that usually characterize a postcrisis economic environment—excess capacities; depressed profits; subdued private investment; and lack of credit growth, which is due to corporate sector reluctance to borrow as well as banking sector reluctance to lend. In such situations, the growth-enhancing effects of fiscal and—more important—monetary easing would be vastly reduced. This underscores the need for reinvigorating profits and private investment through efficiency-enhancing structural measures, not only for sustaining growth over the medium to long term, but also to maximize the growth-enhancing effects of fiscal and monetary easing over the short term.

Table 2: Foreign Currency LT Sovereign Credit Ratings¹

Item	PRC	Indonesia	Korea	Malaysia	Philippines	Singapore	Thailand	Viet Nam									
Moody's	Current Outlook	↑ Positive 22-Nov-02		↑ Positive 15-Nov-02		Stable 24-Sep-02		Stable 9-Jan-03		Stable 14-Jun-02		↑ Positive 15-Nov-02		Positive 17-Jun-02			
	Ratings	A 3	10-Sep-93	B 3	20-Mar-98	A 3	28-Mar-02	Baa1	24-Sep-02	Ba 1	18-May-97	Aaa	14-Jun-02	Baa3	22-Jun-00	B 1	9-Jul-98
		Baa1	8-Nov-89	B 2	9-Jan-98	Baa2	16-Dec-99	Baa2	17-Oct-00	Ba 2	12-May-95	Aa1	18-Jan-96	Ba 1	21-Dec-97	Ba 3	17-Apr-97
		A 3	18-May-88	Ba 1	21-Dec-97	Baa3	12-Feb-99	Baa3	14-Sep-98	Ba 3	1-Jul-93	Aa2	24-May-94	Baa3	27-Nov-97		
				Baa3	14-Mar-94	Ba 1	21-Dec-97	Baa2	23-Jul-98			Aa3	20-Sep-89	Baa1	1-Oct-97		
Standard & Poor's	Current Outlook	Stable 9-Oct-01		Stable 5-Sep-02		Stable 24-Jul-02		Stable 20-Aug-02		↓ Negative 29-Oct-02		Stable 16-Mar-01		Positive 20-Aug-02		Stable 28-May-02	
	Ratings	BBB	20-Jul-99	CCC+	5-Sep-02	A -	24-Jul-02	BBB+	20-Aug-02	BB+	21-Feb-97	AAA	6-Mar-95	BBB-	8-Jan-98	BB-	28-May-02
		BBB+	14-May-97	SD	23-Apr-02	BBB+	13-Nov-01	BBB	11-Nov-99	BB-	2-Jul-93	AA+	6-Sep-91	BBB	24-Oct-97		
		BBB	20-Feb-92	CCC	2-Nov-01	BBB	11-Nov-99	BBB-	15-Sep-98			AA	24-May-89	A -	3-Sep-97		
				CCC+	21-May-01	BBB-	25-Jan-99	BBB+	24-Jul-98					A	29-Dec-94		
				B -	2-Oct-00	BB+	18-Feb-98	A -	17-Apr-97					A -	26-Jun-89		
				SD	17-Apr-00	B+	22-Dec-97	A	23-Dec-97								
				CCC+	31-Mar-99	BBB-	11-Dec-97	A+	29-Dec-94								
				SD	30-Mar-99	A -	25-Nov-97										
				CCC+	15-May-98	A+	24-Oct-97										
				B -	11-Mar-98	AA -	3-May-95										
				B	27-Jan-98	A+	1-Oct-88										
				BB	9-Jan-98												
				BB+	31-Dec-97												
				BBB-	10-Oct-97												
			BBB	18-Apr-95													
Fitch IBCA	Current Outlook	Stable 6-Dec-01		Stable 09-Dec-02		Stable 27-Jun-02		Stable 7-Aug-02		↓ Negative 25-Nov-02		Stable 17-Jan-02		Positive 10-Oct-02		Positive 12-Jun-02	
	Ratings	A -	11-Dec-97	B	01-Aug-02	A	27-Jun-02	BBB+	7-Aug-02	BB+	8-Jul-99	AA+	18-Nov-98	BBB-	24-Jun-99	BB-	12-Jun-02
				B -	16-Mar-98	BBB+	30-Mar-00	BBB	7-Dec-99					BB+	14-May-98		
				B+	21-Jan-98	BBB	24-Jun-99	BBB-	26-Apr-99								
				BB -	8-Jan-98	BBB-	19-Jan-99	BB	9-Sep-98								
			BB+	22-Dec-97	BB+	2-Feb-98	BBB-	13-Aug-98									
			BBB-	4-Jun-97	B -	23-Dec-97											

Notes:
 A positive/negative outlook suggests that a long/intermediate-term movement (i.e., an upgrade/downgrade) is likely. A stable outlook means that the rating is not currently subject to change.
 Those in **bold italics** refer to ratings/outlooks that have changed since the last AEM.
 ↑ refers to an improvement over a previous rating or outlook since the last AEM while ↓ refers to a deterioration over a previous rating or outlook.
¹Please refer to Annex in Regional Overview of the *Asia Recovery Report*, March 2001, for a description of ratings.
 SD = selective default
 Sources: Web sites of Moody's, Standard and Poor's, and Fitch.