

SECTION TWO: WORLD ECONOMIC DEVELOPMENTS AND OUTLOOK

The World Economy Developments in 2007

General Overview

1. Mr. Speaker, according to the October 2007 issue of the World Economic Outlook (WEO), the world economy has expanded for the fifth consecutive year in 2007, with an estimated overall output growth running above 5 per cent in the first half of 2007, slower than the 5.4 per cent growth in 2006. The moderation in growth can largely be attributed to a slow down in growth in the United States which resulted from deceleration in the housing market.
2. Growth has been widespread, encompassing the advanced, emerging and developing economies. China's economy gained further momentum in 2007, growing at 11.5 per cent, while India, Russia and other resource-rich countries followed closely. Central and Eastern Europe is projected to grow at a slower pace from the 6.3 per cent in 2006, to reach 5.8 per cent in 2007 and further decline to 5.2 per cent in 2008.
3. In many developing countries, including those in Africa, positive trends in the terms of trade since 2003, have contributed to improved external and fiscal balances. This improvement is attributed to the strong demand for primary commodities at the global level, leading to a rise in commodity prices. These have also paved the way for more expansionary policies, and for a widespread recovery in investment rates. Thus, Africa is forecast to continue growing at around 5.7 per cent in 2007, while growth rates in the Western Hemisphere are expected to slow down slightly to about 5 per cent in 2007 and 4.3 per cent in 2008.
4. Data from UNCTAD sources suggest that East and South Asia are expected to continue as the fastest growing regions in the world, as both China and India continue to grow strongly in 2007. This growth pattern will continue for a lot more years to the extent that investment ratios of these Asian giants continue to be high.
5. This expected growth presents a downside risk, being that, the inevitable correction of the imbalances in the global economy does not occur at the expense of a major recession in the United States, which is a very significant market for Asian exports. There are signs that sources of world economic growth are shifting slightly, with the United States economy slowing down, emerging market and developing economies maintaining a strong growth momentum and the domestic demand in Western Europe

increasing. China, India and Russia contributed to about one half of global growth in the last year. Stronger domestic demand growth in emerging market economies is expected to be the main driver to global growth in 2008.

6. Mr. Speaker, the performance of developing countries and their potential for catching up with the developed countries has improved considerably. Although enormous differences in absolute incomes persist, developing countries increased per capita GDP by almost 30 per cent between 2003 and 2007, compared to 10 per cent in the G-7 countries (UNCTAD September, 2007). Real per capita income has picked up in recent years in Latin America, Africa and West Asia after more than two decades of stagnation.
7. In East and South Asia, economic growth accelerated from already high growth rates, which allowed these sub regions to more than double their per capita GDP in only 14 years. The transition economies of South-East Europe and the Commonwealth of Independent States (CIS) have experienced rapid growth in recent years, with an accumulated increase in per capita income of almost 75 per cent.
8. The global output of emerging market economies and developing countries has remained relatively robust and beyond 5 per cent in the past five years. It is projected to remain at the 8.1 per cent in 2007 but slow down to 7.4 per cent in 2008. The expected growth in 2007 is largely attributed to the coming on stream of new production facilities in oil- exporting developing countries.
9. The down side risk to the growth prospects would be the impact of the recent floods which threatens to wipe away large tracts of crop lands in East, Central and West Africa continuing; oil price increase and the regional energy crisis. Also, the terms of trade in the region is expected to deteriorate in 2008 slightly, with further increases in crude oil prices in 2008.

Inflation

10. Global inflation continued to be low in 2007, but has moved up in the emerging markets due to rising oil prices and accelerated food price. However, there are concerns about inflationary pressures emanating from the recent financial market turbulence, rising food prices, dwindling spare capacity, persistent high oil prices and strong exchange inflows, especially, in emerging markets and developing countries.

11. In the Euro area, annual inflation is expected to be 1.7 per cent in 2007, lower than the 2.3 per cent recorded in 2006. Inflation is expected to be more stable in 2008, ranging from 1.7 per cent to 1.9 per cent.
12. Similarly, in the US, consumer price index for 2007 is expected to be 2.7 per cent, lower than the 3.2 per cent achieved in 2006. This is projected to further decline to 2.3 per cent in 2008.
13. In the case of Japan, inflation will continue to be around 0.3 per cent in 2007, just as the 2006 rate, but will increase slightly to 0.5 per cent in 2008.
14. In most of the African region, consumer prices are expected to follow a similar trend with single digit rate in most areas, with the exception of Zimbabwe, Democratic Republic of Congo and Ethiopia. In 2007 the average inflation in sub-Saharan Africa is projected to stay within 6-9 per cent range for the first time.
15. While the annual average inflation is expected to remain at the 2006 rate of 7.5 per cent, inflation in middle income countries in Africa is likely to accelerate from 5 per cent to 6.75 per cent in 2007. Notwithstanding the strong domestic demand in low income countries, the African Region inflation is expected to moderate further due to overall increased food supply, notwithstanding recent floods in some parts of West Africa. Average inflation will remain above 10 per cent in fragile economies.

Risk to Growth Outlook

16. Although the growth prospects are bright for 2008, there still remain some downside risks. They include a deepening in the crisis of the housing sector in the US and upward trend in crude oil prices. Other threats worth considering are: the retrenchment from risky assets should financial markets volatility rise; and inflationary pressures which could heighten as output gaps close.
17. In the long run, any developments that can undermine the current buoyant productivity performance could be a downside risk that could impair global growth. These may include technological progress, open global trading system, cross country capital flows as well as resilient macroeconomic policy framework and financial systems
18. In the medium term, average growth in the WAMZ region is expected to be strong and broadly stable. But the Zone would have to do more to grow sufficiently to achieve the targets of the MDGs. Inflation pressures from the escalating crude oil prices is expected to be a challenge to the

economies, and this would require continued prudent fiscal and monetary policies to control inflation expectations to meet the single digit target.

International Commodity Prices

19. Three global conditions - strong GDP growth, ample liquidity and a weak US dollar – have underpinned the current boom in commodity prices. Even though, these factors still exist, the signals are becoming more mixed. For instance, crude oil prices have reached all-time high, while base and precious metals have experienced some fluctuations in prices hence a safe haven against the dollar. These could further enforce the upward trend of commodity prices on the international market.

Cocoa

20. Cocoa prices on the London International Future and Funds Exchange (LIFFE) assumed an increasing trend from £886 in January, peaking at £1,121.00 in July 2007. However, it has assumed a declining path towards the third and fourth quarter of the year.
21. The high commodity price for cocoa has been driven mainly by low crop yields in West Africa and Indonesia in the 2006/2007 main crop season. Favourable rainfall has improved prospects of cocoa production in the largest producing countries la Cote d'ivoire and Ghana for the 2007/2008 main crop which opened in October, 2007.
22. La Cote d'Ivoire's output is estimated at about 1.3 million tonnes compared to about 1.28 million tonnes for the last cocoa season whiles Ghana's output is projected at 650,000 metric tonnes as against 614,000 metric tonnes in the 2006/07 crop season. There are however concerns about the effect of the black pod disease in West Africa which could also affect the supply fundamentals of cocoa in 2008.

Gold

23. Gold prices have increased steadily from US\$ 650 in the first quarter of the year to US\$ 680 per ounce in the third quarter of 2007. The general weakening of the US dollar has contributed to the increasing commodity prices, most notably gold. The price of gold is projected to hit \$850/oz by end 2007, as investors will continue to increase their holdings in gold and other commodities.

Oil

24. Crude oil prices have far exceeded their projected levels since August 2006, with analysts warning that intense pressures from US reserves and refineries are likely to worsen the situation. Despite the high crude oil

prices, there is little evidence of a slowdown in US gasoline demand. The situation has been compounded by increasing demand in the Euro area and Japan. Demand from China and India continues to be particularly strong growing at about 20 per cent.

25. On the other hand, growth in the supply has been sluggish as Organisation of Petroleum Exporting Countries (OPEC) is keen to keep prices high to preserve the non-dollar value of their exports. Moreover, shortage of refinery capacity is becoming increasingly constrained. OPEC's rising price aspirations are mainly due to the erosion of purchasing power as the US dollar weakens.