

## Braving the Storms: The Outlook for East Asia and the Pacific, Illustrated

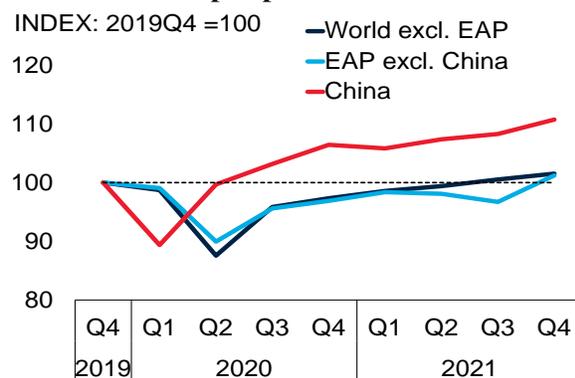
The Russian invasion of Ukraine threatens the uneven recovery of developing East Asia and Pacific (EAP) countries. The invasion comes on top of the economic distress caused by the lingering COVID-19 pandemic, the financial tightening in the United States, and the pandemic resurgence and the economic slowdown in China. While commodity producers and fiscally solid countries in the region may weather these shocks with less difficulty, these events will dampen the growth prospects of most economies in the region. Overall economic growth is projected to slow to 5 percent in 2022— 0.4 of a percentage point less than expected in October. If global conditions worsen and national policy responses are weak, growth could ease further.

The outlook for East Asia and the Pacific can be illustrated in the following charts:

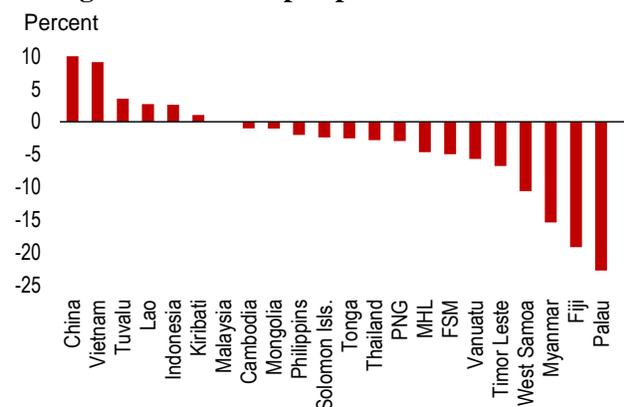
### 1. Economic recovery had resumed in the final quarter of 2021

By end 2021, recovery appeared to be gaining traction, led by China. The rest of the region too posted strong growth in the fourth quarter of 2021, following a dip in the preceding three months due to the Delta COVID-19 variant. However, the recovery was uneven across the region, and output remained below pre-pandemic levels in many economies.

#### GDP relative to pre-pandemic



#### Change in GDP from pre-pandemic

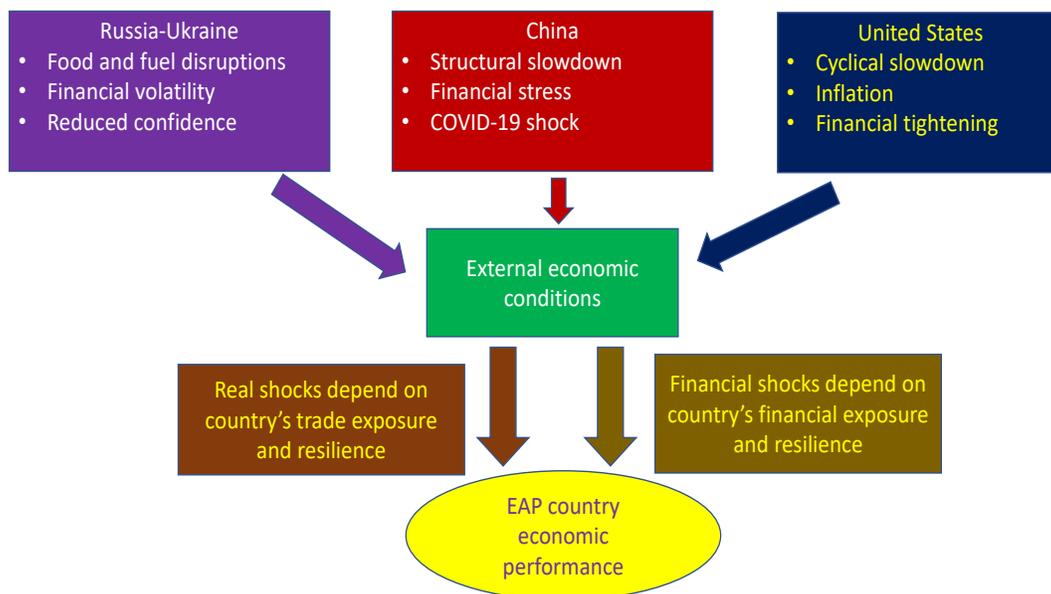


Source: Haver Analytics, World Bank.

Note: The figures show seasonally adjusted real GDP indexed to 2019Q4 (100). B. Latest value is 2021.

### 2. Three emerging shocks will dampen the recovery

Three international developments now threaten the recovery. Most serious is the war in Ukraine, which is leading to a spike in commodity prices, strains in financial markets, and loss of business confidence. This comes on top of a structural slowdown in China, exacerbated by growing COVID infections amid the country's a zero-COVID policy and continuing difficulties in an over-leveraged real estate sector, and financial tightening in the United States as inflation accelerates. These emerging shocks will affect the region through trade and financial channels. How individual countries are affected will depend on their exposure and resilience to these shocks.

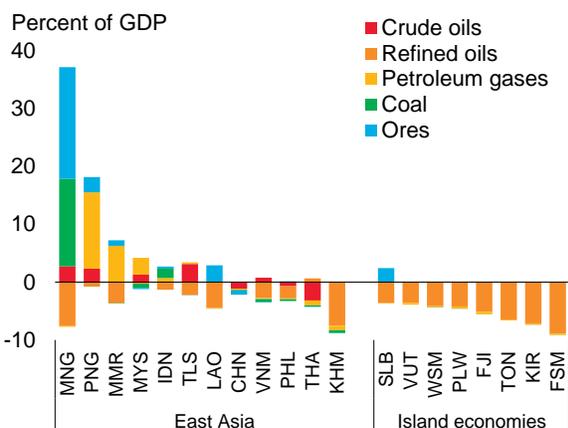


Source: World Bank staff illustration

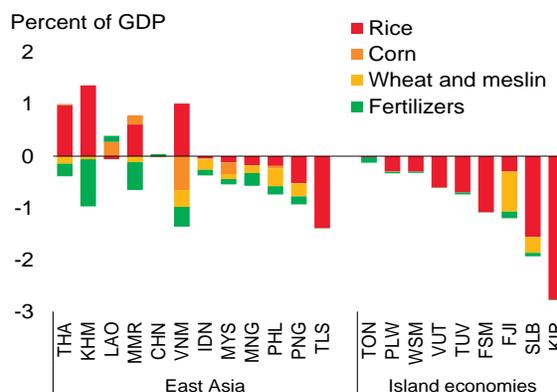
### 3. Fuel and food price spikes will hurt commodity importers

While most East Asia and Pacific countries are not directly exposed to Ukraine or Russia through trade or finance, they will feel the effects of global repercussions, most immediately and significantly because of the spike in fuel and food prices. While some (Indonesia, Malaysia) are less dependent on imported fuels, most other countries are net energy importers. Rice prices too are likely to increase -- rice and wheat are substitutes -- as will the prices of fertilizers and energy, weighing even on rice exporters like Thailand and Vietnam.

**EAP countries' net exports of ores and mineral fuels**



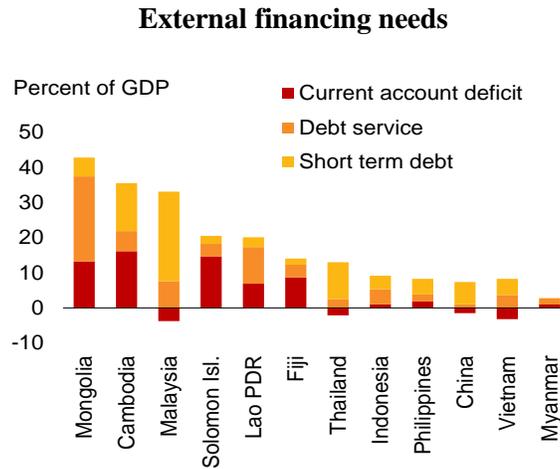
**EAP countries net exports of rice, corn, wheat, and fertilizers**



Sources: UN Comtrade, Consensus Economics, Haver Analytics, World Bank.  
Notes: Net export of selected commodities as a share of GDP, average 2015-19.

#### 4. Interest rate hikes will pinch countries with large deficits or debt obligations

Tightening financial conditions will affect most countries that have large external financing needs, including those holding large external debt (Lao PDR, Mongolia), and countries that rely on short-term capital flows (Cambodia, Malaysia, Thailand).

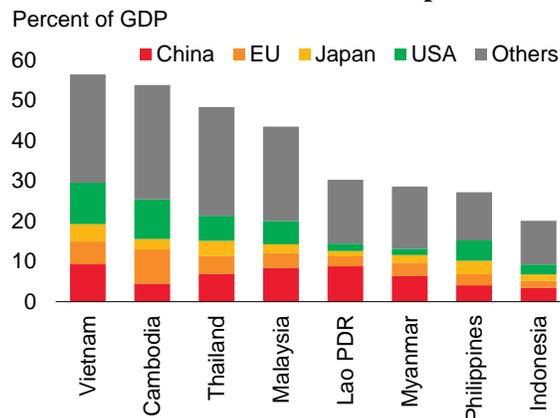


Source. International Monetary Fund. World Development Indicators. World Bank. Fitch Solutions  
 Note: The figure shows decomposition of external financing needs in 2022 estimates. EMDE shows the unweighted average of EMDEs.

#### 5. Slowing global growth will weigh on exporters

As global growth slows, so will demand, weighing most on export-oriented economies (Cambodia, Malaysia, Thailand, Vietnam) for whom half or more of domestic value-added is destined for foreign markets. China now matches the United States in significance as a destination for exports of several countries in the region.

#### Relative importance of ultimate destination for value-added produced in EAP countries



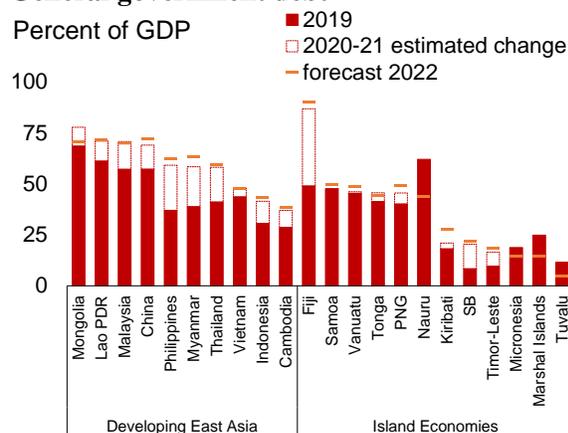
Source: OECD Trade in Value Added database.

Note: The chart plots the share of EAP countries' total value added absorbed in major economies during 2015-2019.

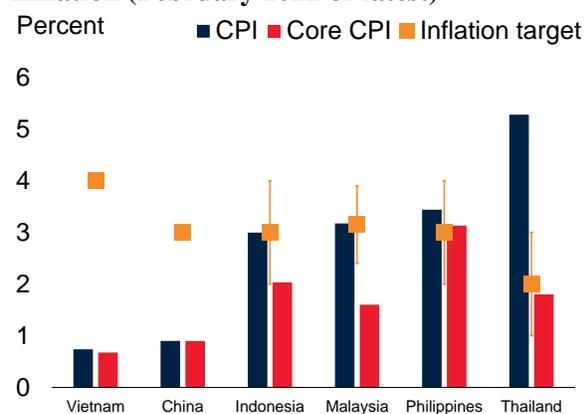
## 6. Government support capacity is constrained, and inflation further limits options

Government support capacity has been stretched thin by the pandemic. The scope for supportive fiscal policy in most countries is constrained by debt that has increased by 10 percentage points of GDP on average. While core inflation remains low, rising consumer prices combined with global financial tightening are beginning to limit options for supportive monetary policy in some countries.

### General government debt



### Inflation (February 2022 or latest)



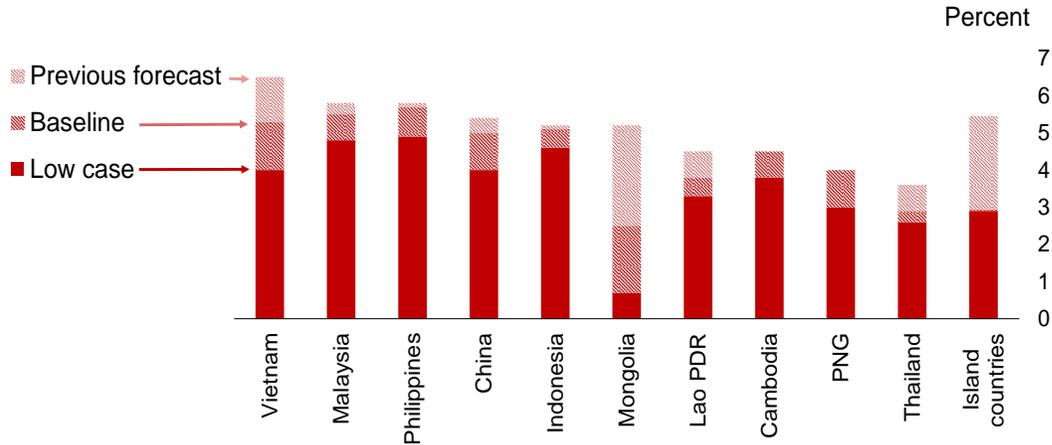
Source: International Monetary Fund, Fitch Solutions, World Bank, national sources.

Notes: A. Refers to 2021 data. B. CPI refers to consumer price index. Core CPI inflation excludes food and energy from CPI inflation.

## 7. The upshot: growth projection downgrades

The triad of shocks and the limited capacity for government support, suggest an outlook that falls short of previous expectations. Projections for regional growth in 2022 have been reduced from 5.4 percent to 5 percent, and if global conditions worsen the national policy response is meager, growth could slow further to just 4 percent. Some larger and commodity-producing countries may be better positioned to weather these shocks, but the repercussions could be harsh for some other countries. Mongolia produces commodities, but its coal exports have been hit by COVID-related Chinese border controls, and its significant imports from and through Russia have been affected by the war and sanctions. The countries in the Pacific, who were struggling with recurrent natural disasters and the decline of tourism, must now confront their first COVID-19 infections, and big food and fuel import bills.

### Revised growth forecasts

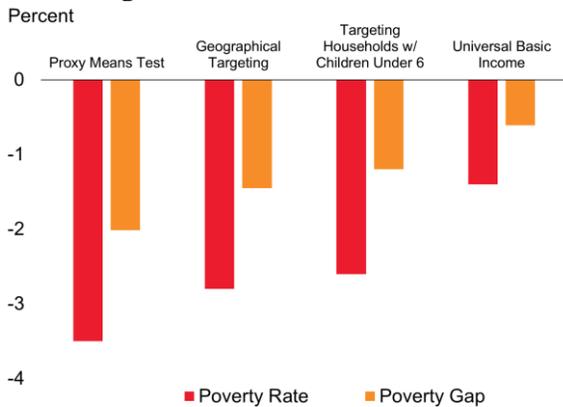


Source: World Bank staff projections.  
Notes: Percent growth of GDP at market prices.

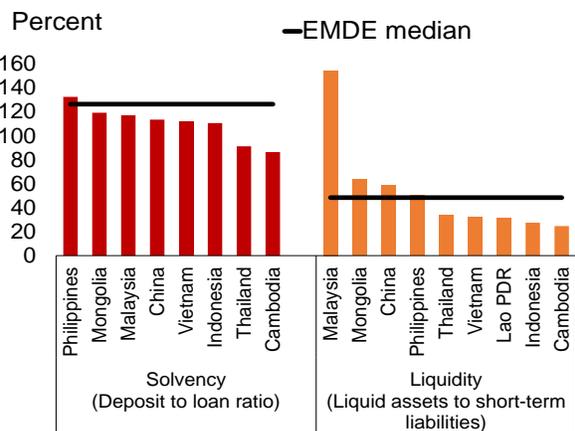
### 8. To brave the storms: target fiscal assistance, identify financial vulnerabilities

To mitigate risks, revive growth, and reduce poverty, first steps should include increasing the efficiency of fiscal policy and strengthening macroprudential policies. Targeted support to households, rather than unselective transfers and price regulations, would deliver gains while creating space for productivity-enhancing investments. While banks in most East Asia and Pacific countries are generally well-capitalized, identifying and addressing vulnerabilities that may have arisen during the pandemic could mitigate the risks from financial tightening.

#### Simulated poverty impacts of cash transfers using different targeting approaches, given a fixed budget



#### Banking sector solvency and liquidity indicators

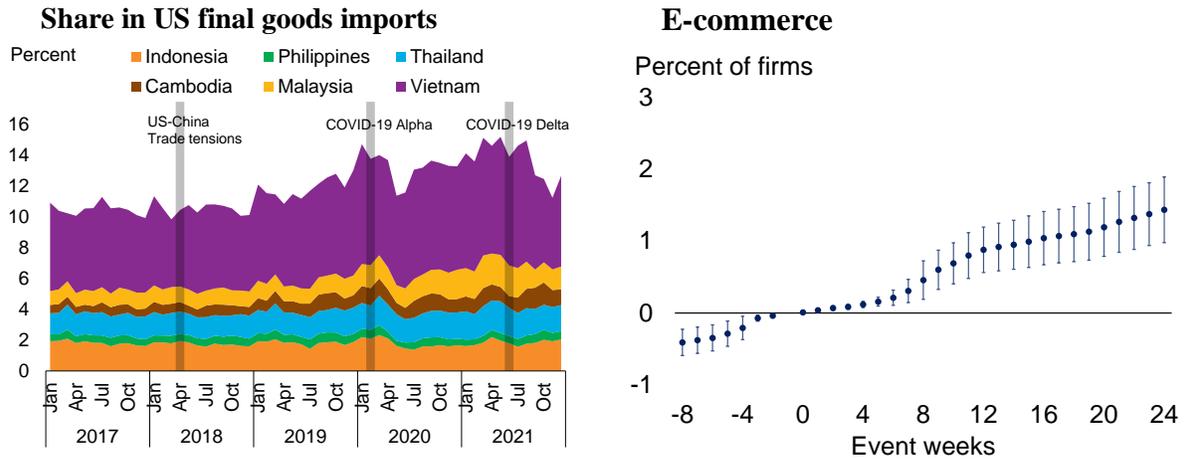


Source: World Bank EAP Economic Update April 2022, IMF Investment and Capital Stock Database 2021, Government Financial Statistics, International Monetary Fund, Haver Analytics, Fitch Solutions, World Bank, national sources.

Note: A. Simulations illustrate the poverty impacts of better targeting social assistance resources in a large middle-income country. B. Shows 2021 data.

## 9. To regain momentum: seize new export opportunities, expand new technology use

Comprehensive trade-related reforms would enable more EAP countries to take advantage of shifts in the global and regional trade landscape, as Vietnam is doing. Improved access to skills and finance could help firms adopt productivity-enhancing technologies. Exposing firms to greater domestic and international competition would strengthen their incentives for doing so.



Source: China, EU, Japan and US customs trade data and World Bank staff estimations.

Note: A. The figure shows the share in US final goods imports. B. Event study plot where the x axis shows event time in weeks – relative to the first COVID-19 cases. Unweighted averages Includes country fixed effects and standard errors are clustered at country-level. Bars reflect 95% confidence intervals. Coefficients are normalized relative to the omitted category at week t-1, the week before the first COVID-19 cases. Simulations using Computable General Equilibrium modeling.