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**Article**

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# CESifo WORLD ECONOMIC SURVEY

VOLUME 4, No. 4

NOVEMBER 2005

## WORLD ECONOMIC CLIMATE

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World Economic Climate brightens up

## ECONOMIC EXPECTATIONS

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Assessments of current economic situation improved, economic expectations somewhat less positive

## INFLATION

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Inflation expectations for 2005 revised upwards

## INTEREST RATES

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Trend of rising rates not yet expected to slow down

## CURRENCIES

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US dollar seen as fairly assessed and the euro to a less degree as overvalued

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## Ifo World Economic Survey

### Regions

- World economy: Stabilization at a favourable level
- Western Europe: Economy remains on recovery course
- North America: Economic climate cools down somewhat
- Eastern Europe: Economic stabilization
- CIS: Economic climate satisfactory
- Asia: Economic climate improves
- Oceania: Economic rebound in Australia
- Latin America: Stabilizing markets
- Near East: Economic climate remains favourable
- Africa: Diverging economic trends predominate

## Notes

The Ifo World Economic Survey (WES) assesses worldwide economic trends by polling transnational as well as national organizations worldwide about current economic developments in the respective country. This allows for a rapid, up-to-date assessment of the economic situation prevailing around the world. In October 2005 1,100 economic experts in 91 countries were polled.

WES is conducted in co-operation with the International Chamber of Commerce (ICC) in Paris and receives financial support from the European Commission.

## Methodology and evaluation technique

The survey questionnaire focuses on qualitative information: on assessment of a country's general economic situation and expectations regarding important economic indicators. It has proved to be a useful tool, since economic changes are revealed earlier than by traditional business statistics.

The individual replies are combined for each country without weighting. The "grading" procedure consists in giving a grade of 9 to positive replies (+), a grade of 5 to indifferent replies (=) and a grade of 1 to negative (-) replies. Grades within the range of 5 to 9 indicate that positive answers prevail or that a majority expects trends to increase, whereas grades within the range of 1 to 5 reveal predominantly negative replies or expectations of decreasing trends.

The survey results are published as aggregated data. The aggregation procedure is based on country classifications. Within each country group or region, the country results are weighted according to the share of the specific country's exports and imports in total world trade.

*CES – Center for Economic Studies* – is an institute within the department of economics of Ludwig-Maximilians-University. Its research concentrates on public finance, aspects of the economy, but also includes many diverging fields of economics.

*Ifo Institute for Economic Research* ist one of the largest economic research institutes in Germany with a three-fold orientation: to conduct economic research, to offer advice to economic policy-makers and to provide services for the research and business communities. The Ifo Institute is internationally renowned for its business surveys.

*CESifo* is the name under which the international service products and research results of both organizations are published.

# WORLD ECONOMY: WORLD ECONOMIC CLIMATE BRIGHTENS

In October 2005 the World Economic Climate slightly improved, after a year of economic cooling (see Figure 1). The climate indicator stands at 99.3 (after 97.5 in July: 1995=100), considerably above its long-term average (1990–2004: 94.0). The improvement of the overall climate index was due to better assessments of the current economic situation. According to the expectations for the coming six months, the global economy is foreseen to stabilize in the first half of 2006 at the current favourable level (see Figure 2).

## World economy: Stabilization at a favourable level

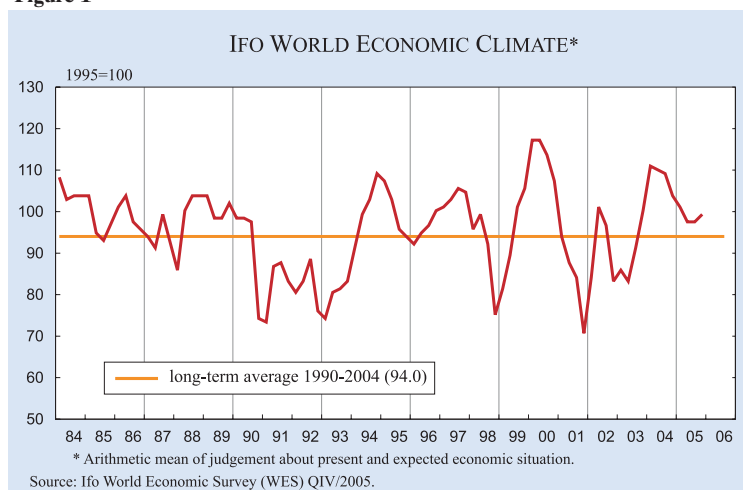
The latest survey results have confirmed the July survey expectations that the global economic slow-down that set in at the beginning of 2004 will level off by the end of 2005. The current economic situation in October was judged somewhat better than in July and again above satisfactory. The economic expectations for the first half of 2006 point to further economic stabilization. However, the interpretation of the recent results must take into consideration that the underlying economic trends strongly differ between the regions (see Figure 3 and 4). The economic climate declined somewhat in October in the *United States*, the world's leading economy. However, in other parts of the world, primarily in *Western Europe* and *Japan* the economic climate improved, pointing to a solid economic stabilization in the first half of 2006. Global GDP is expected to further grow robustly: The IMF in its latest World Economic Outlook has projected global growth of about 4.3 percent for 2005 and the same for 2006. But high oil prices remain a burden on the global economy. Particularly during the winter months in the Northern hemisphere, the recent surge in energy prices, exacerbated by the shutdown of oil platforms and refineries due to the hurricanes in the *United States*, is seen as a constraint to a stronger global economic expansion.

## Western Europe: Economy remains on recovery course

According to the recent survey results, both the assessments of the current economic situation and the economic expectations for the next six months point to an improvement of the economic climate in Western Europe (see Figures 3 and 4).

Although the economic climate improved, on average, in the euro area in October, the vast majority of WES experts surveyed in this region still judged the present economic situation of their countries to be below a “satisfactory” level (see Figure 5a/b). In particular, in *Portugal, Italy, Germany* and *France* the assessments of the present economic situation – despite a reported improvement – remained in the negative territory, indicating that the economic recovery is still hesitant. However, in all these countries the outlook for the first half of 2006 is very optimistic. In other countries of the euro area – in *Belgium, Austria, Spain* and *Greece* – assessments of the present economic performance were more or less at a satisfactory level. A particularly favourable economic climate was again reported for *Ireland* and *Finland*. Though, according to the official figures, unemployment is declining in most Western European countries, for example in *France* and *Germany*, adding to signs that economic growth is gathering pace, it is still considered to be the most

Figure 1

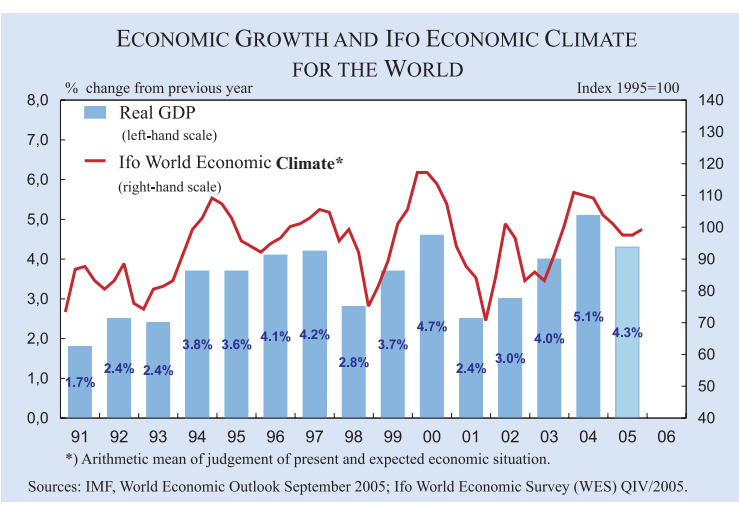


### Box 1

#### World Economic Survey (WES) and GDP Growth in the World Economy

The Ifo World Economic Climate is the arithmetic mean of the assessments of the general economic situation and the expectations for the economic situation in the coming six months. The October results are based on the responses of 1,100 experts. As a rule, the trend of the Ifo Economic Climate indicator correlates well with the actual business-cycle trend measured in annual growth rates of real GDP (see Figure).

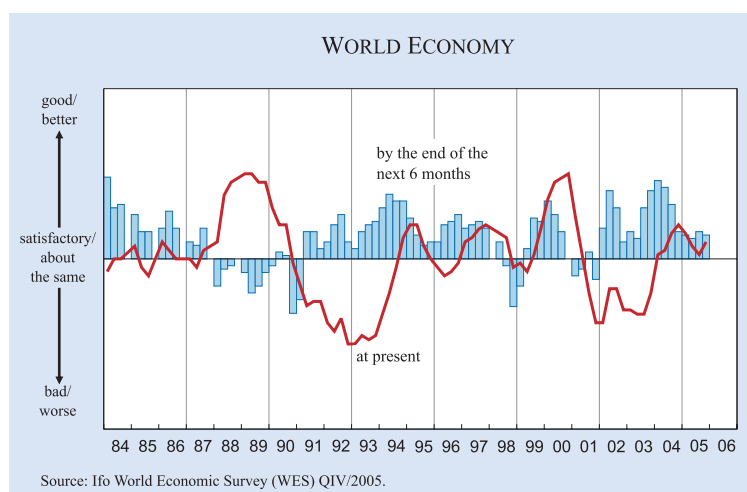
The Ifo World Economic Climate Index rose for the first time since the beginning of 2004, after having stabilized in the previous survey. The improvement, however, applied only to the assessments of the current economic situation. The expectations for the coming six months weakened slightly. The World Economic Survey thus signals a continuingly robust international economy. The weakening in the world economy in 2004 has proved to be only temporary and has now been supplanted by a moderate cyclical upturn.



important economic problem at present. Another important economic problem in the euro area remains insufficient demand. It was considered particularly problematic in *Austria, Germany, Italy* and the *Netherlands*.

In the countries outside the euro area, *Denmark, Norway, Sweden* and *Switzerland*, the present eco-

Figure 2



nomic situation was assessed considerably above satisfactory. The panel's forecast for the coming six months reflects a stabilization of the current positive state. In contrast, in the *United Kingdom* the overall climate index deteriorated strongly in the course of 2005. According to the latest results, business sentiments brightened somewhat in October. However, the survey economists expect a slowdown in consumer spending and corporate investment to remain sluggish into 2006.

#### North America: Economic climate deteriorates

According to the latest survey results, the economic climate indicator in North America deteriorated in October (see Figures 3 and Figure 6). Both components – assessment of the current economic situation as well as the economic expectations – have been

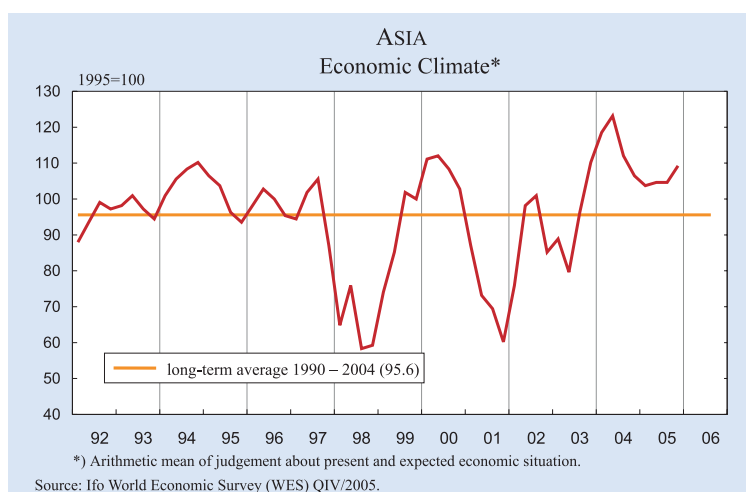
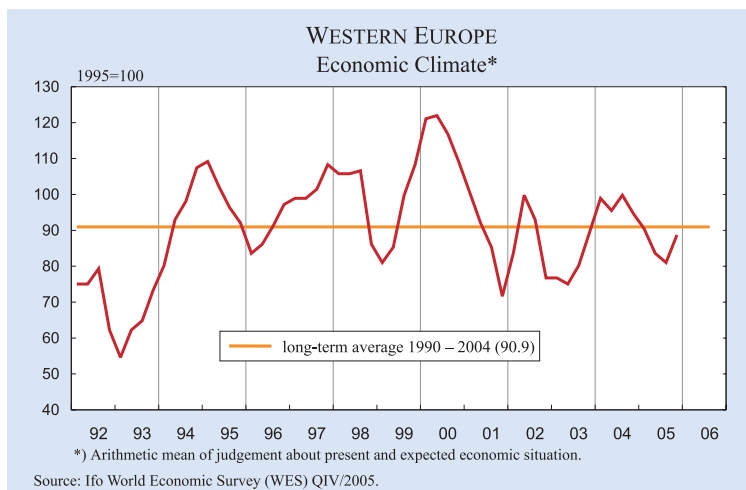
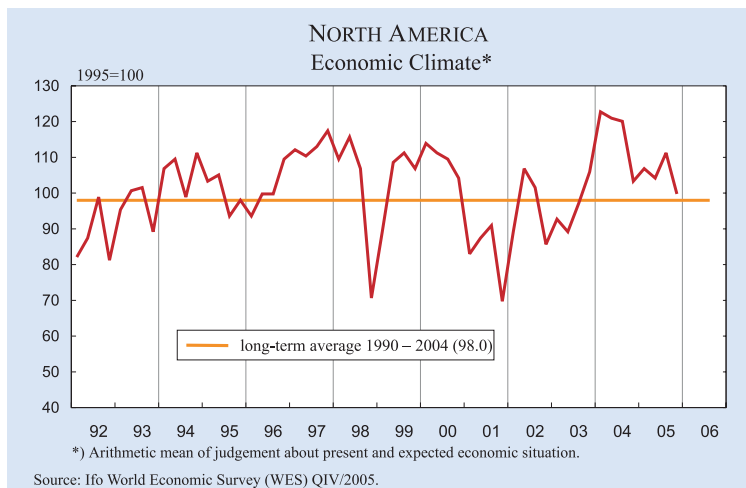
downgraded. Undoubtedly the socio-economic damages caused by the autumn hurricanes have depressed business confidence in the *United States*. However, the current economic situation is still regarded as above satisfactory by the majority of WES experts in the *US*. Both capital expenditures and consumer spending kept momentum, and the outlook for the coming half year is solid. Among the most important economic problems

the surveyed economists again named the public deficits and lack of confidence in the government's economic policy.

In *Canada*, the economic climate remained favourable. The current economic situation has again been rated above the satisfactory level. Economic expectations, though slightly downgraded here as well, point to economic stabilization in the first months of 2006. Lack of international competitiveness was seen by surveyed experts to be the most important problem in the *Canadian* economy.



**Figure 3**



### Eastern Europe: Economic stabilization

The overall economic climate stabilized in October at a satisfactory level, with the assessments of the current economic situation continuing to improve and economic expectations for the coming six months pointing to further economic stabilization (see Figure 7). WES

experts surveyed in the region forecast a marked increase in the foreign trade sector (with rising exports and imports) for the coming six months.

The present economic situation in the eight Eastern European countries that joined the European Union – *Poland, Hungary, Czech Republic, Slovakia, Slovenia, Estonia, Lithuania* and *Latvia* – has been assessed considerably above the satisfactory level, according to economic experts polled by WES in the region. Only in *Hungary* have the marks for the current economic performance again slipped below the satisfactory level. In *Latvia* and *Slovakia*, the economic climate index also declined somewhat, but remained in positive territory. The near-term prospects remained generally positive in all new EU members except *Slovenia*. However, the high unemployment that is substantially above the levels prevailing in the Western countries of the European Union poses the number one economic problem in the Eastern European transition economies, according to WES experts.

In the other Eastern European countries outside the EU, diverging economic trends predominate. In *Albania, Bulgaria* and *Romania*, the present economic situation was assessed as “satisfactory” with prospects for future development remaining highly positive. In contrast, in

*Croatia* and in *Serbia* and *Montenegro* the present economic situation was seen as below the “satisfactory” level. But WES experts are confident of an improvement in the near term. Not so in *Bosnia-Herzegovina*, where no turnaround of the presently unfavourable economic situation is expected in the next six months.



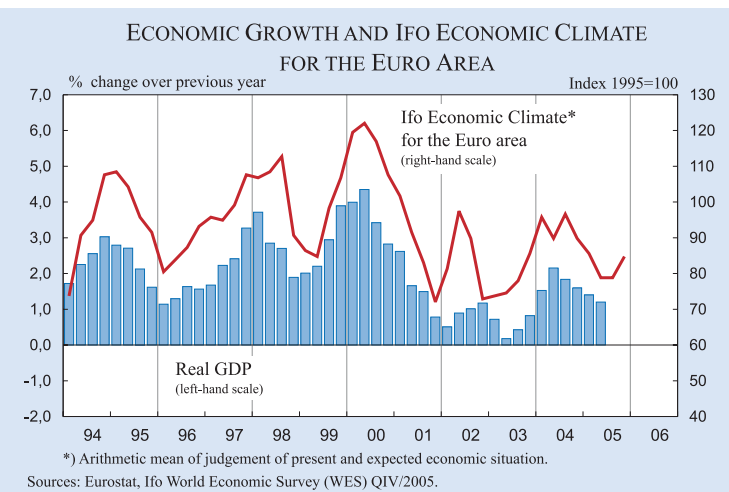
## Box 2

### World Economic Survey (WES) and GDP Growth in the Euro Area

The Ifo World Economic Climate for the 12 member countries of the euro area is the arithmetic mean of the assessments of the general economic situation and the expectations for the economic situation in the coming six months. The October results are based on the responses of 306 experts. As a rule, the trend of the Ifo Economic Climate indicator correlates well with the actual business-cycle trend for the euro area – measured in annual growth rates of real GDP (see Figure).

The economic climate for the euro area brightened in October 2005 for the first time in more than a year. Both the assessments of the current economic situation as well as the expectations for the coming six months improved. Despite this sign of recovery, in the majority of the euro member states the current economic situation is still assessed, on balance, as unfavourable.

The economies of Ireland, Luxembourg and Finland continue to hold the top positions in the appraisals of the WES experts. Whereas further cyclical expansion in the coming six months is expected in Finland, for Ireland and Luxembourg the survey participants see a stabilisation of the economic situation at the present very positive level. With these three exceptions, the current economic situation is assessed positively only in Spain, and in Austria it is still considered to be satisfactory. Nevertheless, in those member states in which the current economic situation is still assessed as unsatisfactory, a slight economic recovery was also apparent. This is especially the case for the Netherlands and Belgium but also for France and Germany. In Italy and Portugal, the current economic laggards in the euro area, an improvement is hardly evident.



### CIS: Economic climate satisfactory

The economic stabilization in *Russia* continues, according to the recent WES results. After a slight deterioration of business confidence during 2004, the economic climate indicator in *Russia* stabilized in 2005, with both the assessment of the current economic situation and economic expectations being in the positive zone (see Figure 6). However, as the world's second largest oil producer after *Saudi Arabia*, *Russia's* economic performance is closely tied to rather volatile oil prices. Whereas the oil sector is currently booming the majority of the other economic sectors is having difficulty competing with products and services from abroad. Thus, as a present economic weak point, WES experts named again “lack of international competitiveness”. Also “lack of confidence in government’s economic policy” was cited as

an important problem. The latter also holds true in *Ukraine*, where the economic climate deteriorated somewhat and also the economic outlook became somewhat clouded. A highly favourable economic climate has been reported again for *Kazakhstan*. With regard to the future economic development, the participants are fairly confident. High inflation has been named as one of the most important present constraints to economic growth in the country though the inflation rate in *Kazakhstan* is significantly lower than in *Russia*.

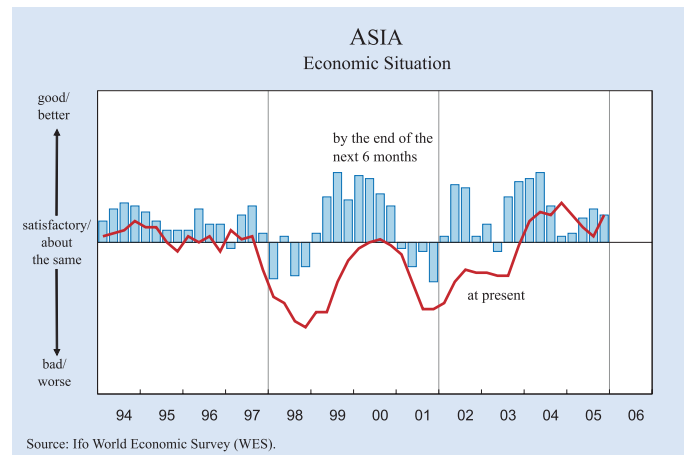
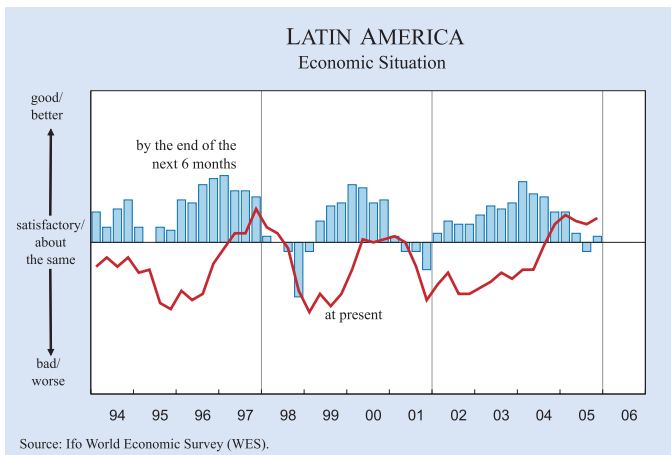
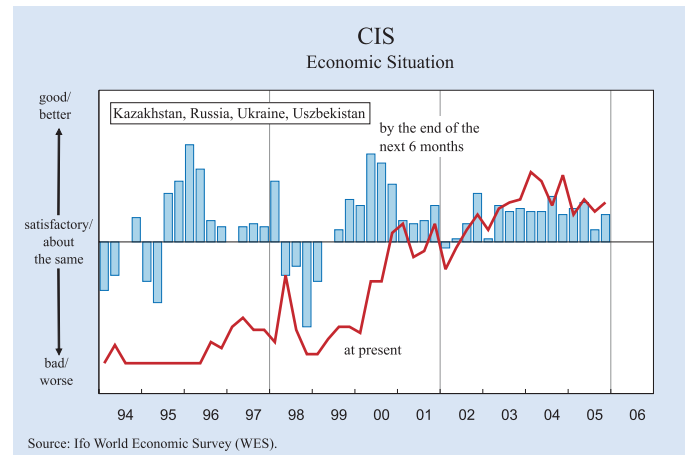
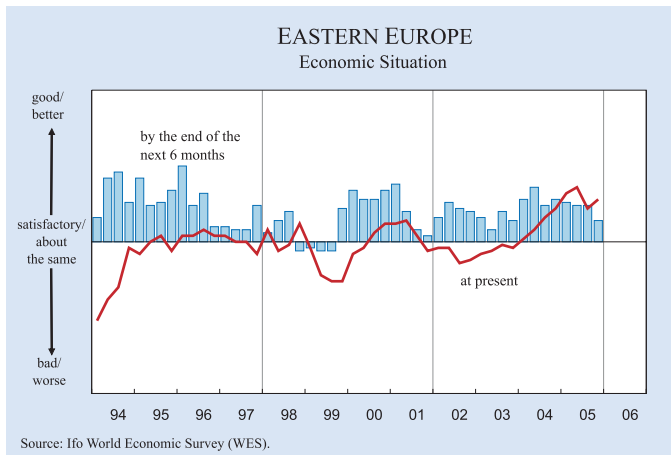
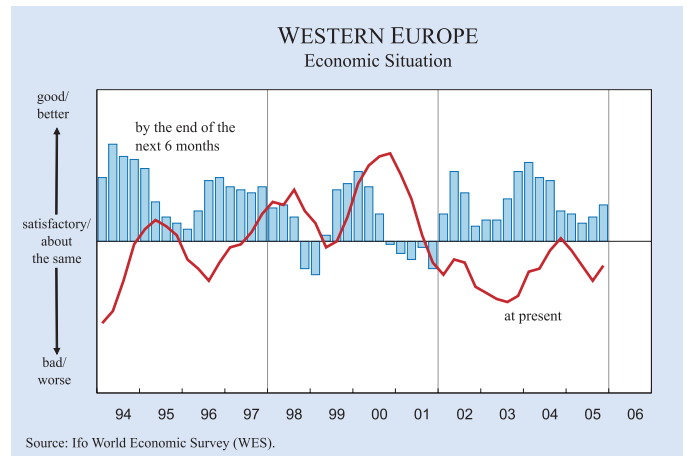
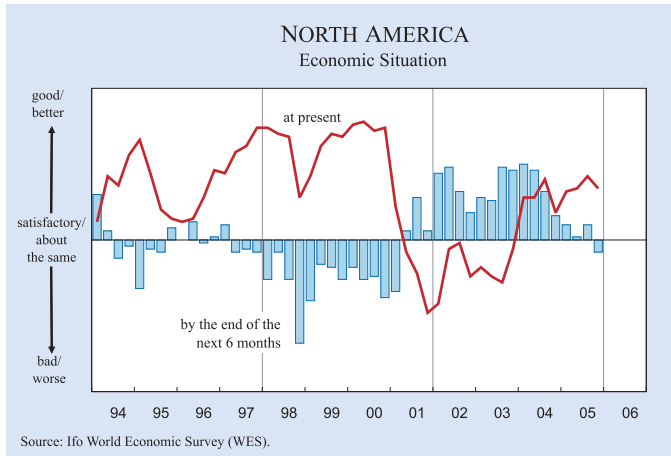
### Asia: Economic climate improves

According to the October survey results, the economic climate in Asia improved slightly, compared to the preceding July survey. For the first time since the end of 2004 the assessments of the present economic situation have been upgraded. The economic expectations for the first half of 2005 point to further stabilization. However, this pattern doesn't apply to all countries surveyed in the region (see Figure 8).

*Japan's* economy in particular seems to have strengthened in the second half of 2005: both components of the economic climate indicator bounced back strongly after this year's spring lull. The present economic situation is now rated as above satisfactory and the prospects for the coming year are highly optimistic. An improved economic situation has been reported by WES experts in *Hong Kong*, though the overall climate index slightly slipped due to somewhat less optimistic near-term expectations. *China's* enormous economic growth rates are expected to moderate in the near-term future. However, the business sentiments in the country remained favourable according to the October results. Among common economic problems, unemployment remained the main challenge in the populous country despite its strong economic dynamic. The economy in *India* maintained its expansion

Figure 4

## SELECTED REGIONS



course also in October, according to economists surveyed in the country. Though both components of the economic climate index have been slightly downgraded, the marks for the present economic situation were the highest in the region, and also the expectations for 2006 point to further economic expansion. However, despite real GDP growth rates at about seven percent per annum, the growth in agriculture remains weak, while *India's* farm sector accounts for nearly a quarter of *India's* gross domestic product and employs about two-thirds of the workforce in the country. In *South Korea* business confidence is now at a two-year high, raising hopes that a broad-based recovery is under way in Asia's third-largest economy. Private consumption is still regarded as weak, but exports are expected to strengthen further in the coming months. In *Singapore*, the *Philippines* and *Pakistan* improved assessments of the present economic performance were contrasted with cautious expectations regarding the near-term economic development. Both components of the economic climate index improved in *Thailand* and *Vietnam*. The current economic situation is rated as satisfactory and the economic expectations point to stabilisation in the course of the next six months. An unchanged favourable economic climate was also reported for *Malaysia*. In *Indonesia* the economic climate index slightly deteriorated due to less positive expectations, but remained in a satisfactory zone. In the Asian region only in *Taiwan* did the surveyed experts assess the overall economic situation as below the satisfactory level and the near-term expectations remained cautious.

#### **Oceania: Economic rebound in Australia**

In 2005 the panel's responses for *Australia* and *New Zealand* reflected an economic slow-down, starting from a relatively high level: In the July survey the economic climate index slipped marginally. However, the economic patterns of the two countries of the region seem to show diverging economic trends (see Figure 6). While the assessments of the current economic situation improved considerably in *Australia*, the present economic performance continued to deteriorate in *New Zealand*, according to the polled economists. Also the business outlook in *Australia* for the first half of 2006 brightened. In particular the export sector is expected to regain new strength. For a net gas and coal exporter such as *Australia*, increased export earnings from gas and coal exports partially offset the negative impact of

higher oil prices. In contrast, in *New Zealand* the polled experts remained cautious: According to the panel's forecast, the economic cooling phase will last into the first half of 2006.

#### **Latin America: Stabilizing markets**

The latest survey results confirm economic stabilization in Latin America. Both, the current economic situation and economic expectations have been upgraded, though to a slightly lesser degree than in other WES regions (see Figure 9).

Increasing business confidence was reported by *Brazilian* experts. The assessments of the present economic situation are above satisfactory, and the prospects for the next six months point to further economic growth. The government's economic policy seems to enjoy public confidence in the country. A bright picture of the economic climate has again been drawn by experts in *Chile*. The economic performance in the country is remarkably strong, since all demand aggregates are performing satisfactorily and are expected to stabilize further in the first half of 2006. The October survey results confirmed that *Peru's* economy is one of the most vibrant in Latin America. Economic growth is fuelled by strong capital expenditures and private consumption and a buoyant foreign trade sector. *Uruguay* also counts among the group of buoyant economies. The present economic performance is seen to be above satisfactory and is expected to remain on the upward trend. The economic climate in *Argentina* stabilized at a satisfactory level, though both the current economic situation as well as the near-term expectations have been slightly downgraded, the corporate expenditures are still regarded as weak. However, some strengthening is foreseen by the surveyed economists for the foreign trade sector as well as for private consumption. The present economic situation in *Mexico* also stabilized at a favourable level in the course of 2005, according to the experts polled in the country, but the expectations for 2006 remained cautious.

Although there were no further improvements of the economic climate in *El Salvador* and *Colombia* in October, experts questioned in the survey basically confirmed the favourable results of the preceding July survey. In *Costa Rica* the surveyed experts assessed the present economic situation as somewhat below satisfactory. Also the outlook for the coming six months suggests a rather sluggish eco-

economic development. In contrast, *Venezuela's* economy has a tailwind from record high oil prices and the panel's responses suggest that a recovery from the deep recession caused by the oil strike of 2002-2003 is gaining strength. The assessments of the present economic situation have now reached a satisfactory level and the forecast of the panel points to further economic rebound. Also the economic climate in *Bolivia* remains stable, despite a tense political situation in the country. The assessments of the country's present economic situation have been maintained at the "satisfactory" levels and the expectations for 2006 remained positive.

Among all countries of the region, only in *Ecuador* and *Paraguay* did the present economic performance still receive negative marks from the surveyed experts. However, in *Paraguay*, both – assessments of the present economic situation as well as economic expectations for the coming six months – have been upgraded, promising more dynamic development in 2006.

#### **Near East: Economic climate remains favourable**

According to WES experts the economic climate in the Near East remained favourable. Though the assessments of the present economic situation deteriorated slightly since this year's July poll, the outlook for the coming six months improved somewhat (see Figure 10).

The current economic situation continues to be good particularly in *Saudi Arabia*, *Kuwait* and in the *United Arab Emirates*. Also the expectations for the next six months stayed bright in these countries.

The assessments of the present economic situation in *Turkey* remained above the satisfactory level, according to the October results. The prospects for future development promise further economic strengthening in the coming six months. Over all, the last two years' WES survey results suggest that *Turkey* has entered an era of economic stability. In *Israel* the assessment of the present situation improved considerably. The majority of WES experts polled in *Israel* assessed the current economic situation as "good". Also the outlook for the next six months is optimistic – private consumption and capital expenditures are expected to strengthen and the export sector is also expected to pick up somewhat, signalling that economic recovery is

underway. However, terrorist threats and the security situation in general remain the main constraints to a quicker economic revival.

The economic situation in *Jordan*, *Bahrain*, *Lebanon* and also in *Iran* is now regarded as satisfactory. However, in *Iran* according to WES experts the economic outlook for the coming months appears to be clouded. In the other countries, WES experts are fairly confident concerning a positive economic development in the beginning of 2006.

#### **Africa: Diverging economic trends predominate**

Africa remains a region with very diverging economic trends. Thus, an aggregated climate index for countries surveyed by WES on this continent makes little sense, and the following analysis will focus on particular economic trends in individual countries.

The economic climate index in *South Africa* (see Figure 10) stabilized during 2005 at a highly favourable level, after a decade of economic expansion. According to the October survey, business sentiment concerning the current economic situation remained positive, while the economic expectations have improved further. In contrast, the economic recovery in *Egypt* is still rather sluggish, according to economists surveyed in the country. The present economic situation is still assessed as far below satisfactory. The economic expectations though slightly downgraded, still raise hope for an economic turnaround in 2006. The worst economic situation of all 90 countries covered by WES was again reported from *Zimbabwe* where the outlook also remained very bleak. All the surveyed experts gave the most negative marks that are possible on the WES-scale for both present economic situation and expectations.

#### **2005: Inflation expectations revised up**

Consumer price inflation (CPI) has picked up in recent months and is now expected to stand at the end of the year at 3.3 percent on the world-wide average compared with 2.9 percent in 2004 (see Table 1). Thus, higher oil and other raw material prices left clear traces in the CPI.

This holds true also for the *euro area* where the inflation outlook for 2005 reached now 2.2 percent and is thus markedly higher than the ECB's target of

"slightly below 2.0 percent". The worst inflation performance in the euro area will prevail again in Greece in 2005, where the inflation outlook for 2005 edged up from 3.4 percent in the previous survey to now 3.6 percent, followed by Spain (3.4 percent after a previously expected 3.2 percent). On the other hand, the lowest inflation rates in the euro area in 2005 are again expected in Finland (unchanged from previous survey at 1.4 percent) and with an only marginal upward revision in the Netherlands (1.7 percent). In Germany 2005 inflation expectations climbed up from 1.7 percent in the previous survey to now 2.0 percent.

In *Western Europe* outside the euro area, expectations for low inflation rates in 2005 continue to prevail in Switzerland (1.2 percent after an expected 1.1 percent in the July survey) and Sweden (1.1 percent after a previously expected 1.0 percent). In Norway the 2005 inflation outlook deteriorated significantly from 1.4 percent in July to now 1.9 percent. In the United Kingdom the inflation rate in 2005 will be somewhat higher than in the euro area (2.3 percent compared with 2.0 percent).

In the *United States* inflation in 2005 is expected to come in at 3.4 percent, well above the previously expected figure (2.9 percent). Thus, the US inflation rate in 2005 will lie significantly above the 2.5 percent mark that the Fed considers still acceptable.

In *Asia* the period when deflation appeared to be a serious problem is long gone and consumer price inflation in 2005 is expected to be 2.7 percent, which is markedly higher than projected in the July WES Survey (2.4 percent). In contrast to this general upward trend, inflation in China is expected to slow down further and settle at 2.6 percent at the end of the year after an expected inflation rate of 2.9 percent as seen in the survey in July and even 4.1 percent at the beginning of the year. Such a downward revision of the inflation outlook, though to a lesser degree, holds true also for India (5.0 percent after previously expected 5.2 percent in July and 5.5 percent in April) as well as in South Korea (3.4 percent after a previously expected 3.6 percent in July and 3.9 percent in April). On the other hand, inflation is expected to pick up particularly in Indonesia (9.4 percent after a previously expected 7.5 percent) and in Thailand (5.1 percent after a previously expected 3.5 percent). In Japan, though deflation appears to have come to an end, consumer prices are

seen to remain stable in 2005, unchanged from the estimates of the first two surveys of this year).

In *Central and Eastern Europe* inflation is expected to stabilize in 2005 at 3.8 percent which would be significantly lower than in 2004 (5.1 percent). The relatively highest rate of inflation still prevails in Serbia and Montenegro (15.5 percent after previously expected 13.8 percent and 10.9 percent in the April survey). The lowest rates of inflation are seen in 2005 in the Czech Republic (2.6 percent; unchanged from the previous survey), in Slovenia (2.6 percent, even slightly lower than in the previous survey), in Poland (2.4 percent after an expected 2.8 percent in the previous survey), Croatia (3.2 percent after previously 2.8 percent) and in Lithuania (2.7 percent after a previously expected 2.9 percent).

In the *CIS* countries inflation in 2005 is seen slightly lower than in the previous survey (11.5 percent). The downward revision results both from lower inflation expectations in Russia (11.8 percent after a previously expected 12.2 percent) and in the Ukraine (11.9 percent compared with 12.4 percent in the previous survey). The relatively best inflation performance in the region prevails in Kazakhstan with an expected 7.2 percent in 2005.

In *Central and Latin America* inflation in 2005 appears to be slightly lower than expected in the previous WES surveys of this year (5.8 percent in October compared to 5.9 percent and 6.4 percent at the beginning of the year). Whereas the inflation rate in Argentina is expected to pick up and reach 12.8 percent in 2005 against the previously expected 10.9 percent in the July survey, a contrary trend can be observed in Brazil where the 2005 inflation rate is now seen at 5.3 percent compared with the expected 6.3 percent in the previous two surveys. The lowest 2005 inflation rates in the region prevail in Panama with an expected rate of 1.6 percent and in Peru with an expected rate of 2.1 percent. In contrast, inflation in the region is still highest in Venezuela though the rate is slightly shrinking (17.0 percent after expected 17.7 percent in the previous survey and 19.7 percent in the April survey). The inflation outlook remained high in Costa Rica (14.2 percent after previously expected 13.7 percent and 12.7 percent in the April survey).

In the *Near East* the inflation outlook deteriorated somewhat (5.9 percent after previously expected 5.3 percent). Nevertheless, the inflation rate in 2005

Figure 5a

# EUROPEAN UNION

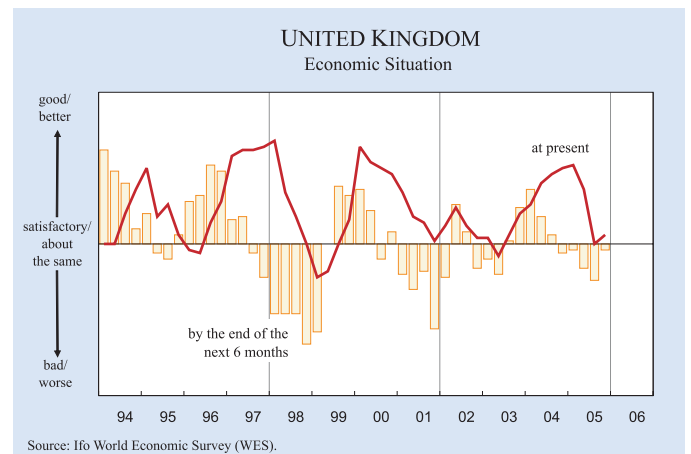
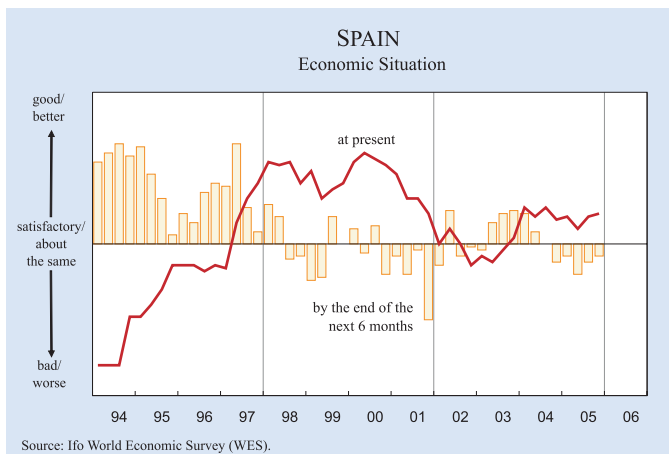
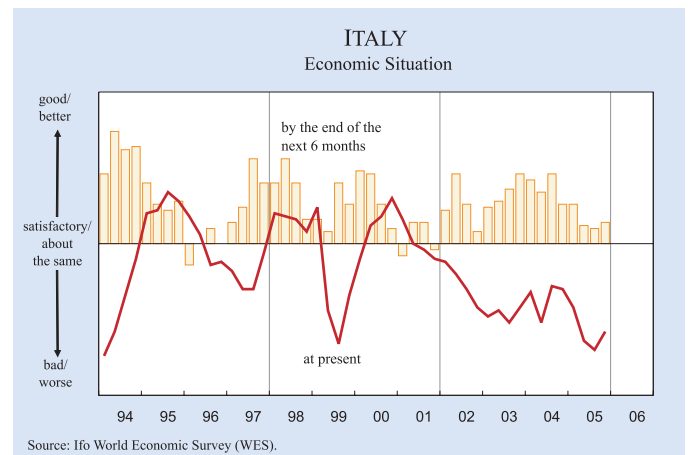
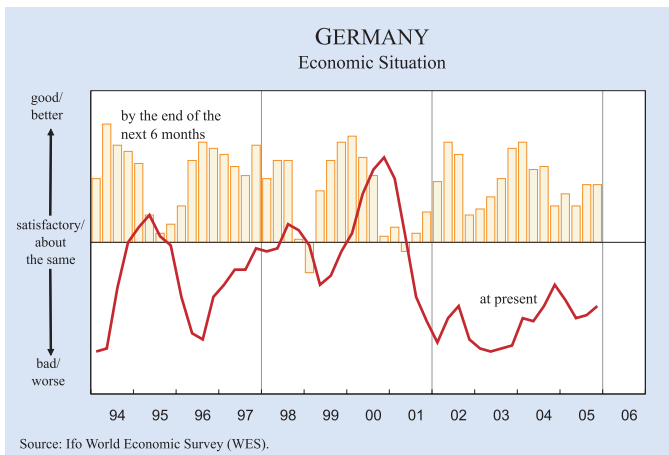
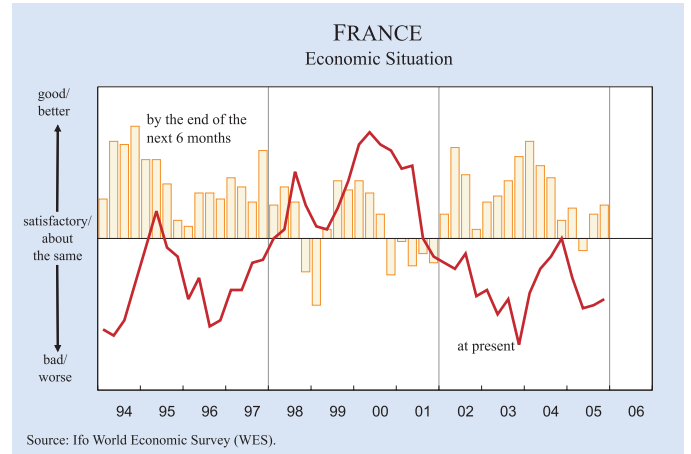
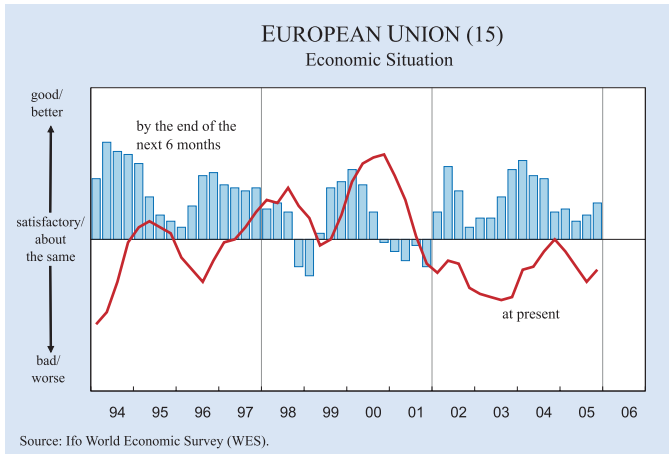
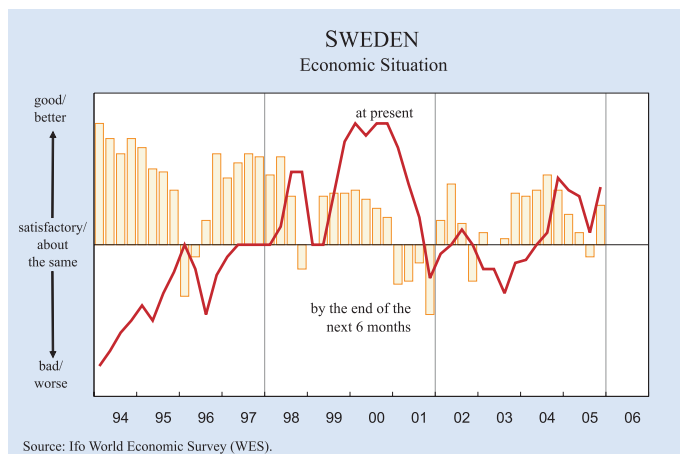
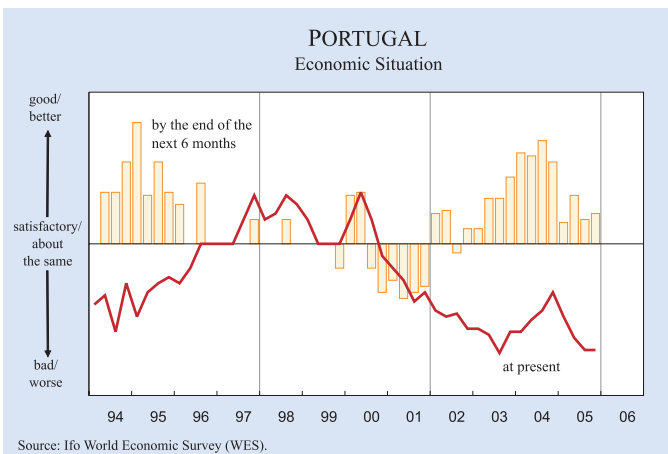
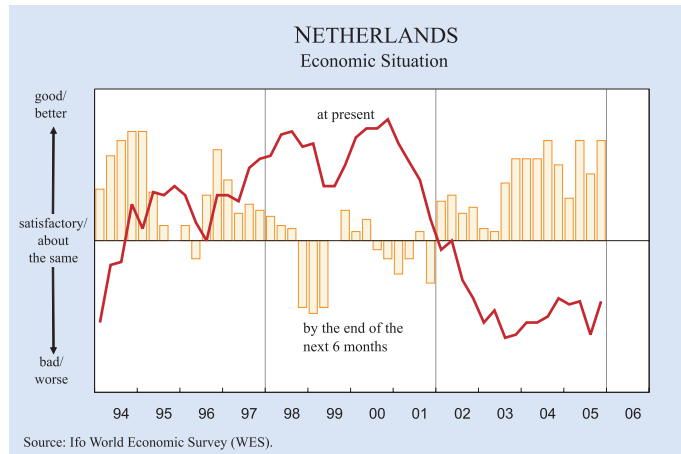
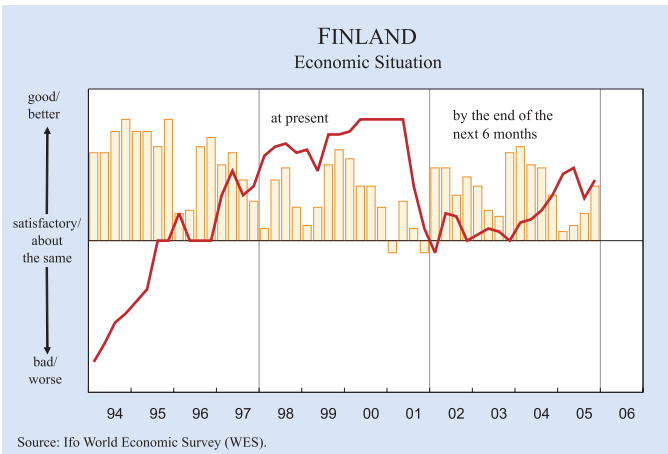
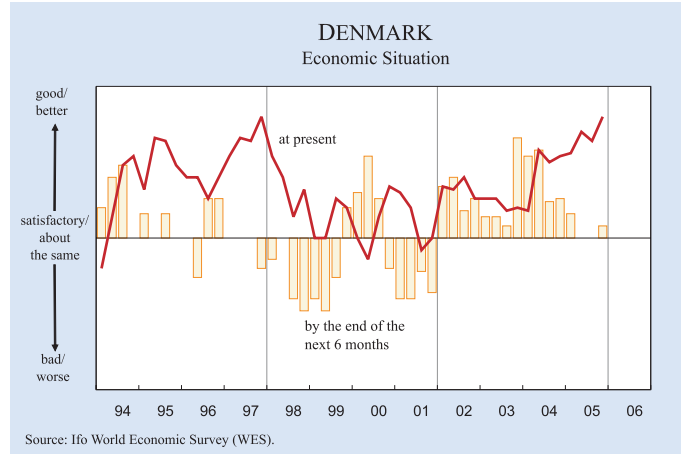
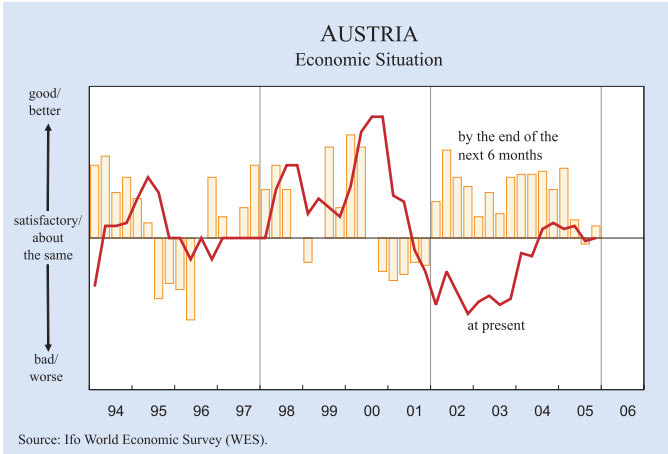




Figure 5b

# EUROPEAN UNION





**Figure 6**

**NORTH AMERICA, OCEANIA AND CIS**

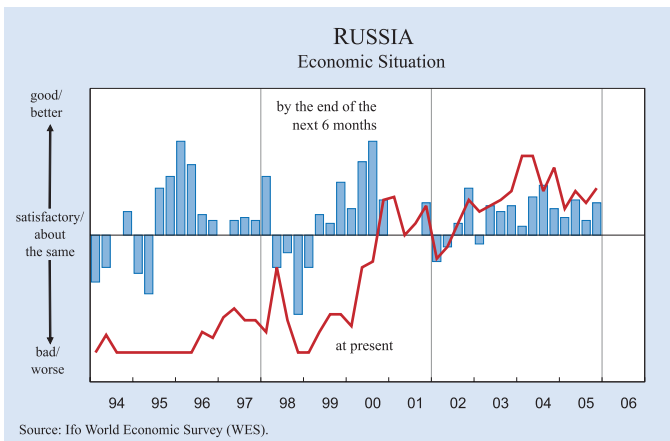
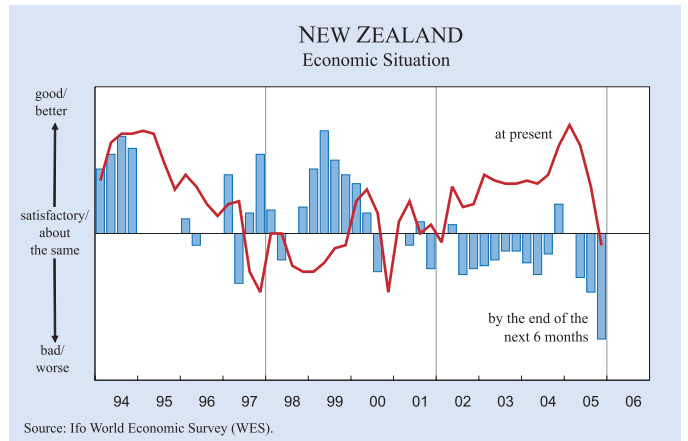
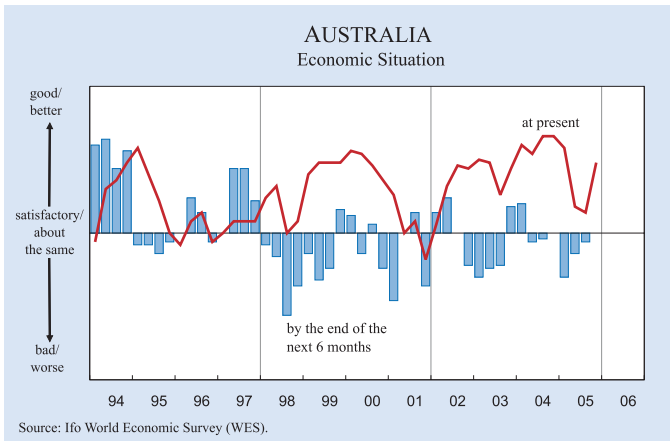
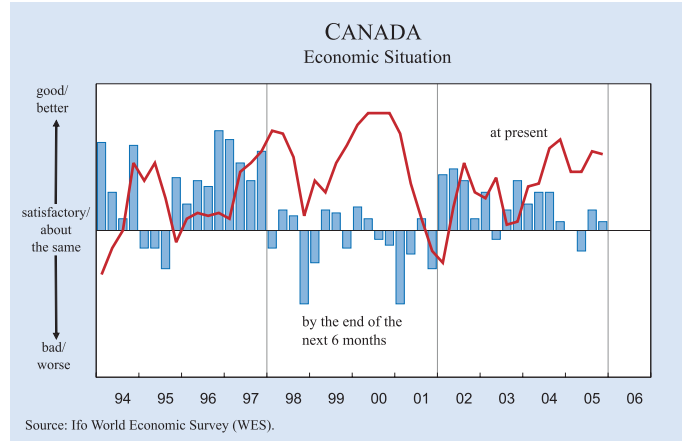
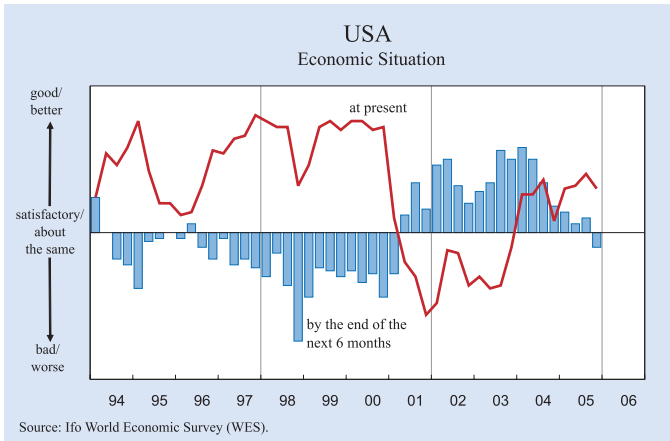
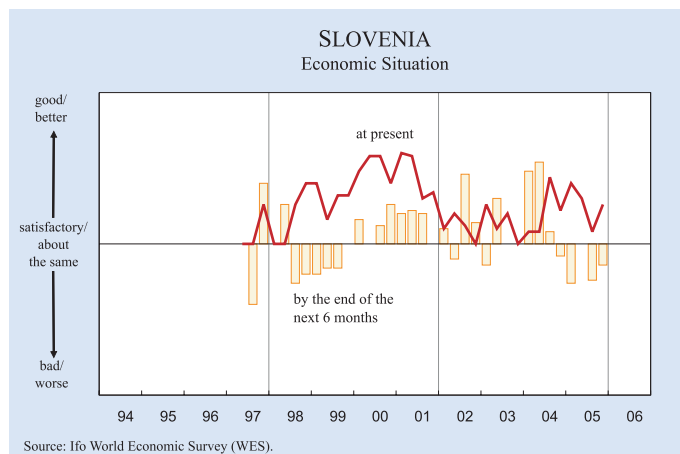
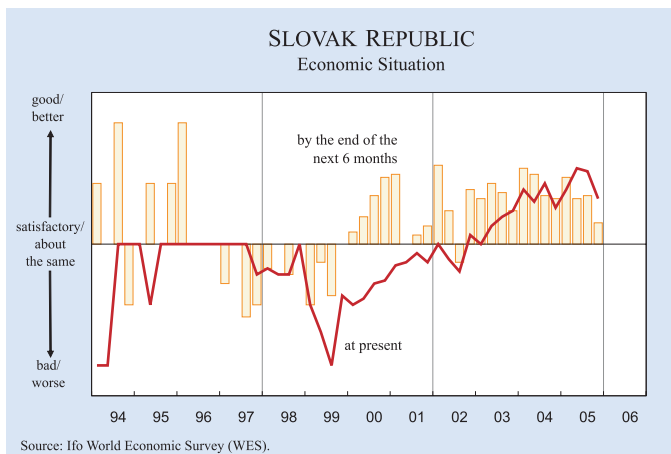
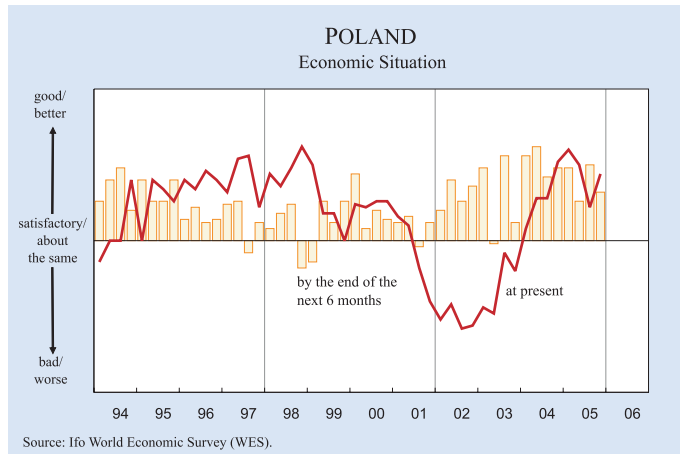
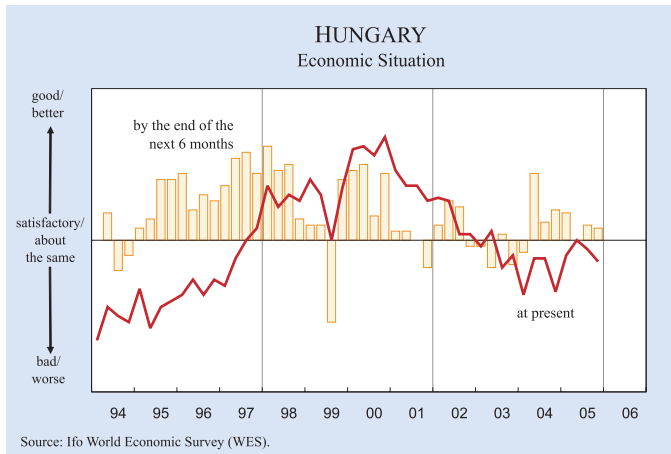
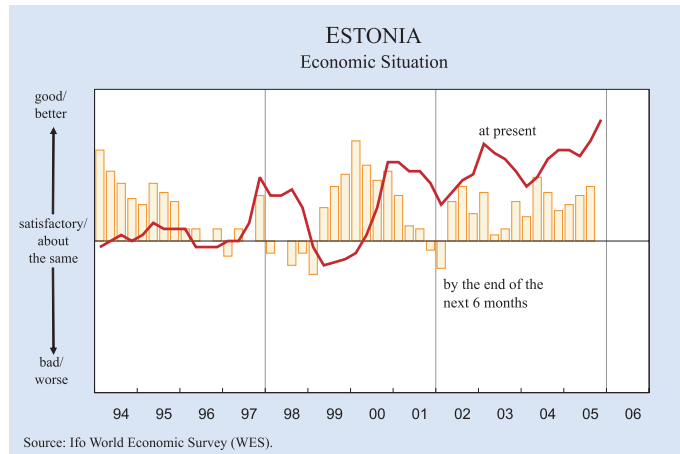
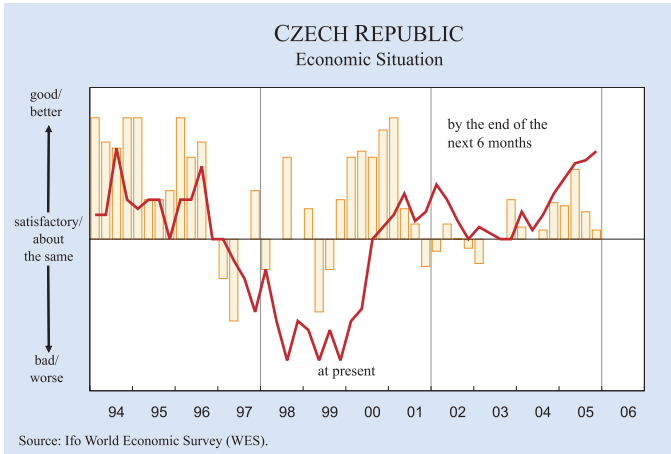


Figure 7

# EASTERN EUROPE



**Figure 8**

**ASIA**

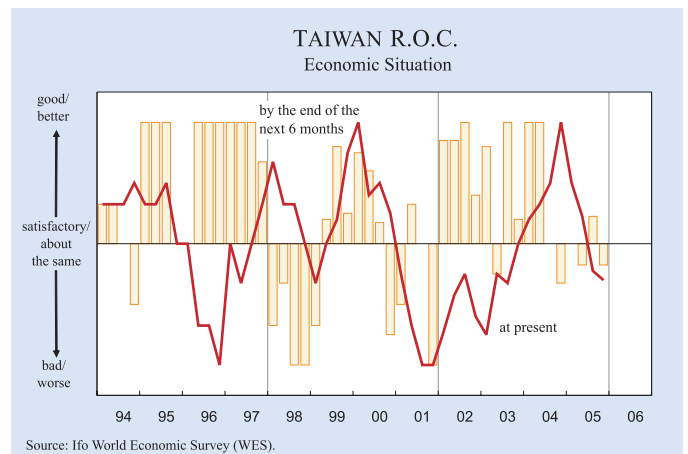
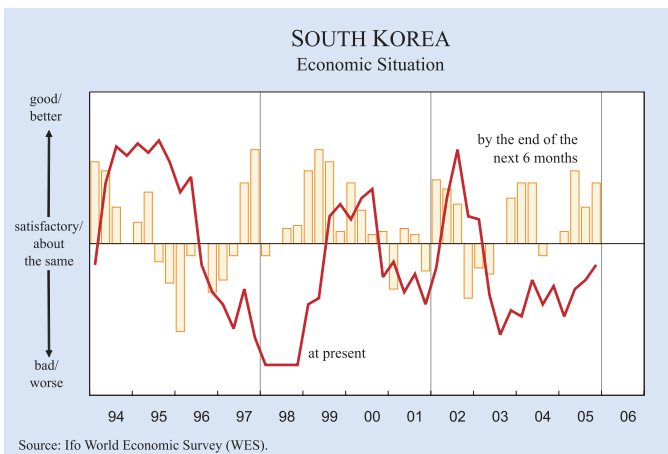
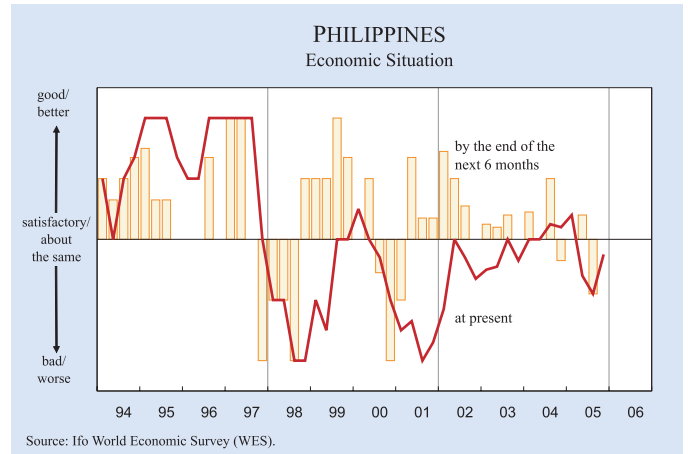
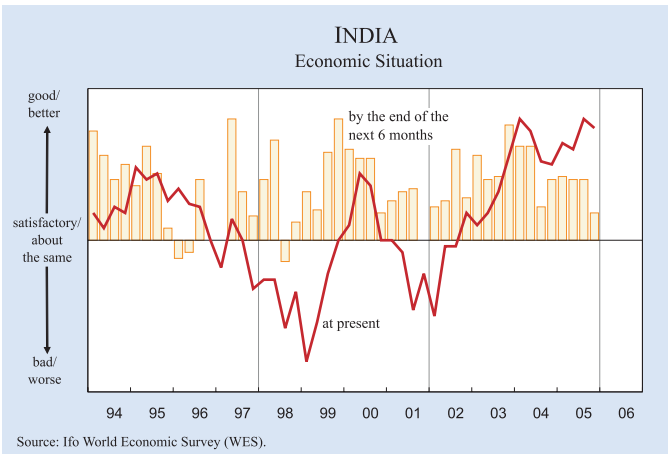
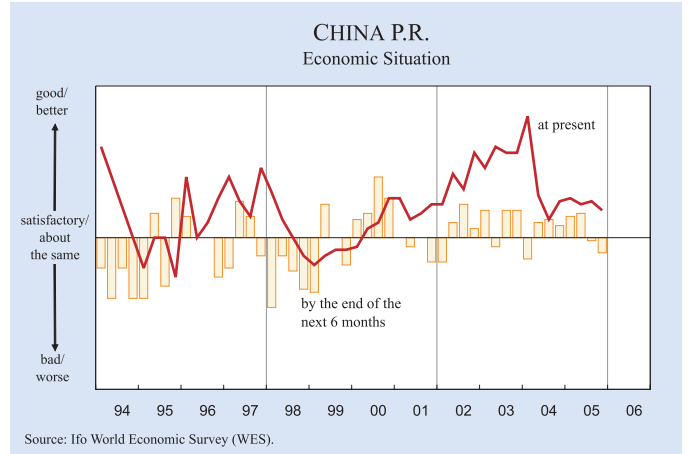
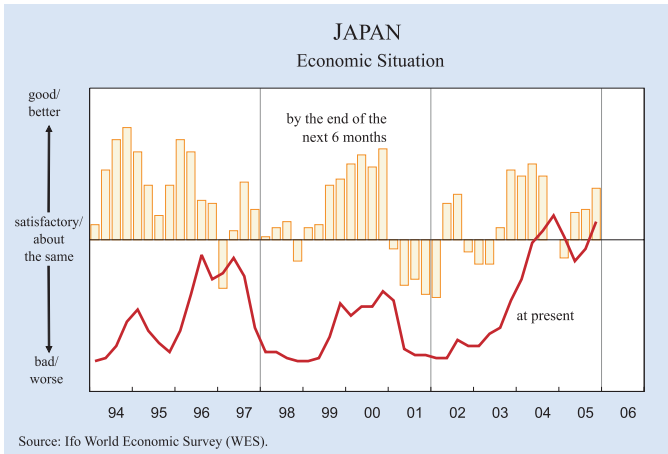


Figure 9

# LATIN AMERICA

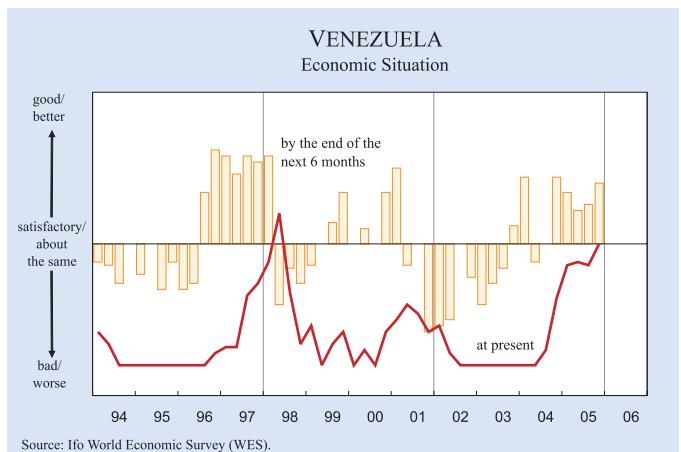
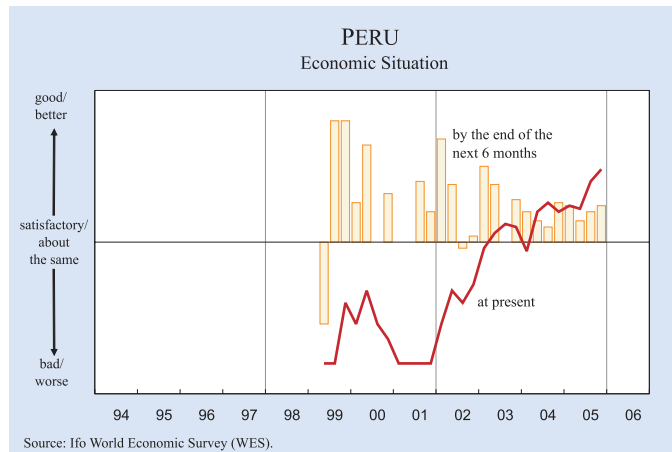
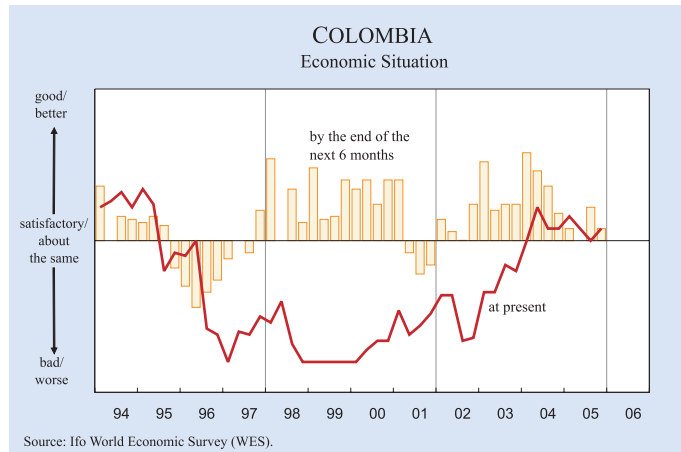
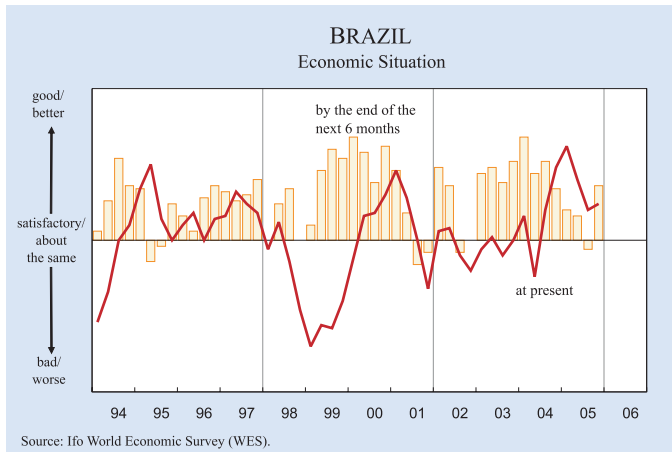
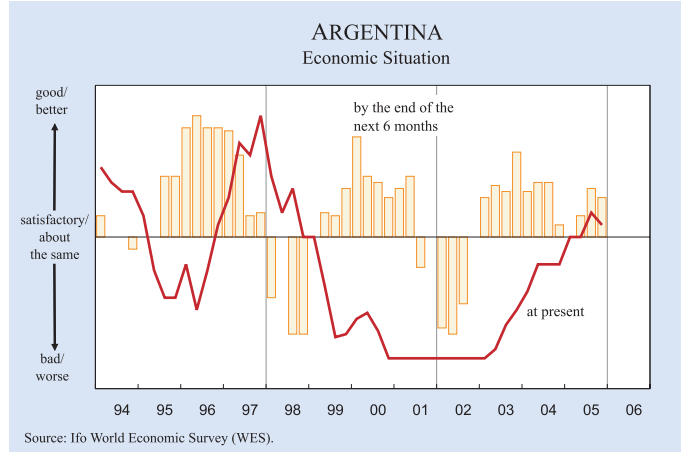
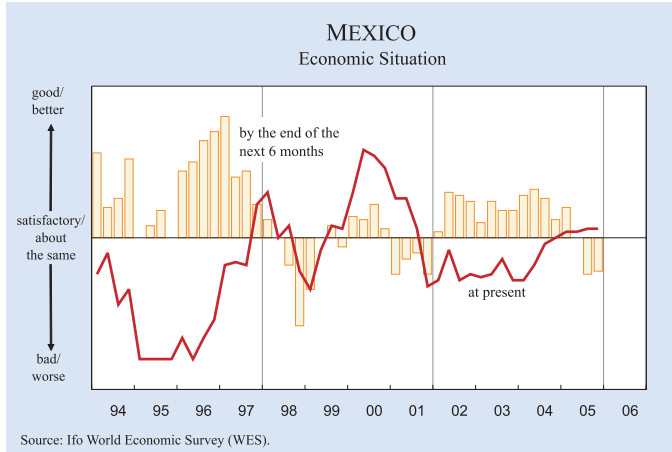


Figure 10

## NEAR EAST AND AFRICA

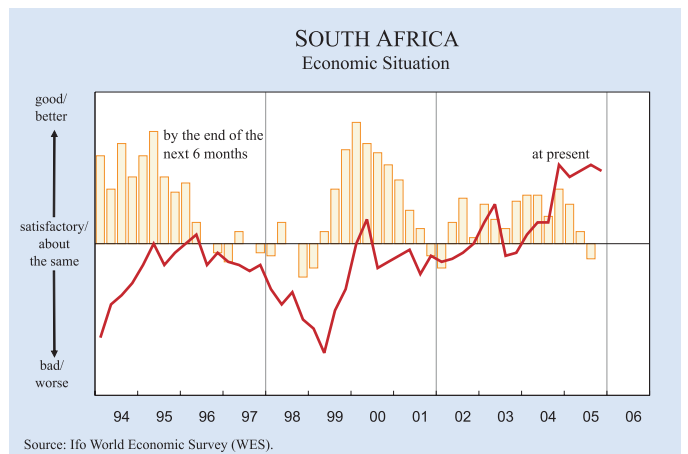
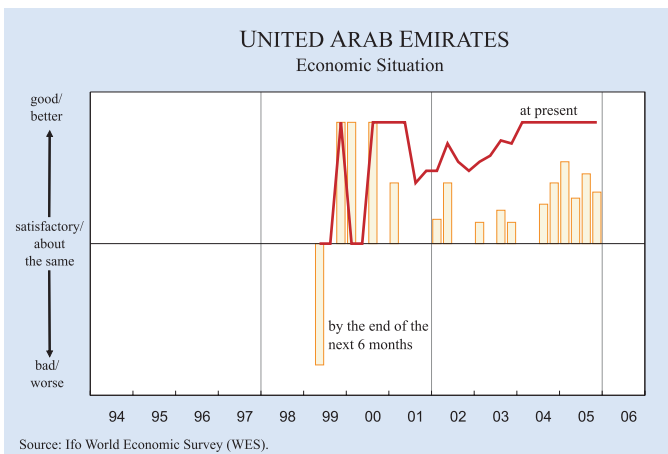
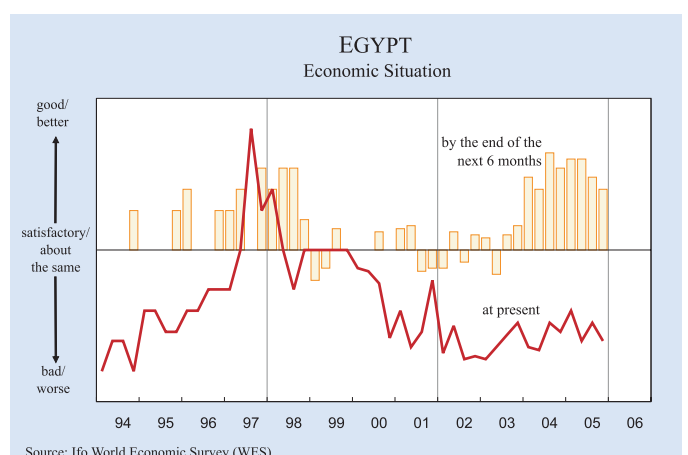
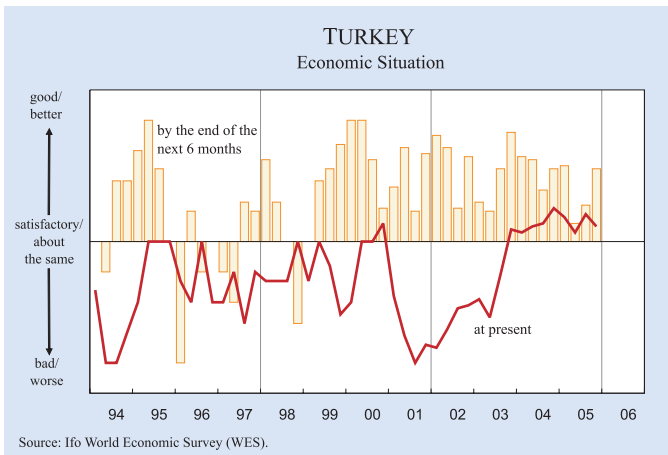
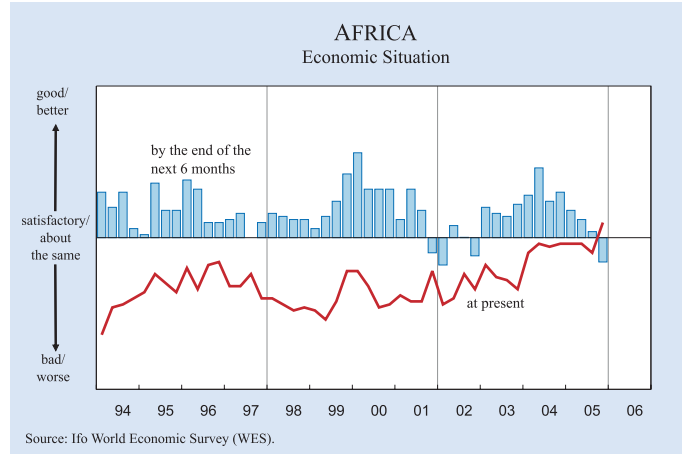
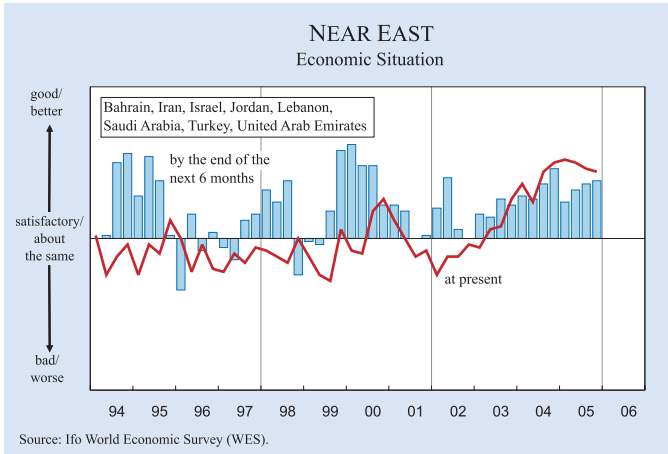


Table 1

**Expected Inflation Rate on Average of 2005**  
(based on WES QIV and QIII 2005)

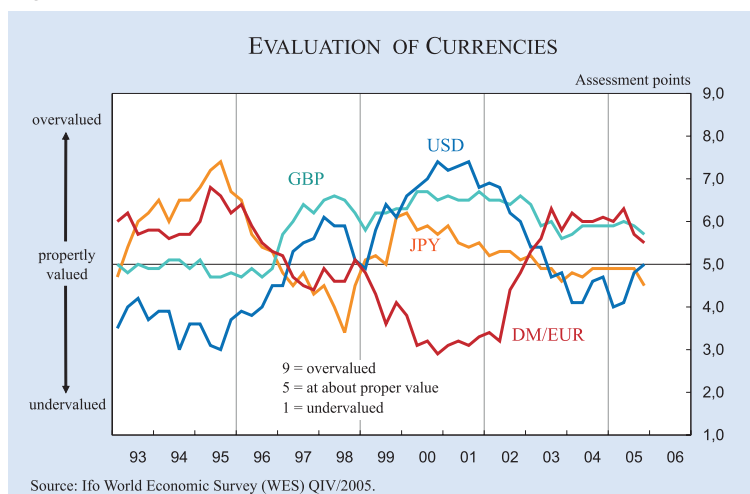
Region	QIV/2005	QIII/2005	Region	QIV/2005	QIII/2005
<b>Average of countries</b>	<b>3.3</b>	<b>2.9</b>	<b>Central a. Latin America</b>	<b>5.8</b>	<b>5.9</b>
<i>World Bank classification:</i>			Argentina	12.8	10.9
High-income countries	2.3	2.1	Bolivia	3.9	4.4
Middle-income countries	5.9	5.6	Brazil	5.3	6.3
Upper-middle	5.8	4.2	Chile	3.8	2.8
Lower-middle	6.2	7.1	Colombia	5.2	5.0
Low-income countries	12.8	10.1	Costa Rica	14.2	13.7
EU countries (old members)	2.2	2.0	Ecuador	2.5	2.4
EU countries (new members) <sup>1</sup>	3.1	3.1	El Salvador	5.2	3.8
Euro area <sup>2</sup>	2.2	2.0	Mexico	4.0	4.3
Asian Pacific Rim <sup>3</sup>	3.4	3.1	Panama	1.6	1.3
			Paraguay	8.9	9.0
<b>Western Europe</b>	<b>2.1</b>	<b>1.9</b>	Peru	2.1	2.5
Austria	2.2	2.2	Trinidad and Tobago	5.0	5.0
Belgium	2.6	2.1	Uruguay	6.0	6.6
Cyprus	2.5	2.5	Venezuela	17.0	17.7
Denmark	1.9	1.6			
Finland	1.4	1.4	<b>Asia</b>	<b>2.7</b>	<b>2.4</b>
France	1.9	1.9	Bangladesh	6.6	6.5
Germany	2.0	1.7	China P.R.	2.6	2.9
Greece	3.6	3.4	Hong Kong	2.2	1.5
Iceland	4.0	-	India	5.0	5.2
Ireland	2.5	2.4	Indonesia	9.4	7.5
Italy	2.2	2.2	Japan	0.0	0.1
Luxembourg	3.2	2.3	Korea	3.4	3.6
Malta	2.7	2.6	Malaysia	3.0	2.9
Netherlands	1.7	1.6	Pakistan	9.0	8.9
Norway	1.9	1.4	Philippines	7.7	8.0
Portugal	2.4	2.5	Singapore	1.6	2.5
Spain	3.4	3.2	Sri Lanka	12.2	12.0
Sweden	1.1	1.0	Taiwan	2.4	1.9
Switzerland	1.2	1.1	Thailand	5.1	3.5
United Kingdom	2.3	2.0	Vietnam	8.1	7.7
<b>Central a. Eastern Europe</b>	<b>3.8</b>	<b>3.7</b>	<b>Near East</b>	<b>5.9</b>	<b>5.3</b>
Albania	3.4	3.2	Bahrain	-	3.0
Bosnia Herzegovina	-	2.0	Iran	17.0	16.6
Bulgaria	5.1	4.5	Israel	2.5	2.6
Croatia	3.2	2.8	Jordan	3.5	3.9
Czech Republic	2.6	2.6	Lebanon	1.5	3.5
Estonia	3.6	3.3	Qatar	-	6.0
Hungary	3.8	3.9	Saudi Arabia	1.2	1.3
Latvia	6.8	5.6	Turkey	7.8	7.7
Lithuania	2.7	2.9	United Arab Emirates	6.5	5.3
Poland	2.4	2.8			
Romania	7.8	7.8	<b>Africa</b>	<b>n.a.</b>	<b>n.a.</b>
Serbia a. Montenegro	15.5	13.8	Algeria	-	5.3
Slovenia	2.6	2.7	Egypt	8.0	7.3
Slovakia	3.6	3.2	Kenya	-	10.7
			Mauritius	5.2	5.5
<b>CIS</b>	<b>11.5</b>	<b>12.5</b>	Morocco	-	1.9
Kazakhstan	7.2	-	Nigeria	23.0	14.0
Russia	11.8	12.2	South Africa	4.4	4.3
Ukraine	11.9	12.4	Tanzania	-	4.0
			Tunisia	2.8	2.7
<b>North America</b>	<b>3.2</b>	<b>2.8</b>	Zimbabwe	400.0	190.0
Canada	2.8	2.1			
USA	3.4	2.9	<b>Oceania</b>	<b>3.1</b>	<b>2.6</b>
			Australia	3.1	2.6
			New Zealand	3.2	2.6

\* Within each country group the results are weighted according to the share of the specific country's exports and imports in the total world trade.

<sup>1</sup> Czech Rep., Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovenia, Slovakia (from 1. May 2004) – <sup>2</sup> EU countries without Denmark, Sweden, United Kingdom. – <sup>3</sup> Australia, China P.R., Hong Kong, Indonesia, Korea, Malaysia, New Zealand, Philippines, Singapore Taiwan, Thailand, Vietnam.

Source: Ifo World Economic Survey (WES), QIV/2005.

**Figure 11**



will still be somewhat lower than in 2004 when it stood at 6.2 percent. In Turkey the inflation outlook for 2005 remained practically unchanged at 7.8 percent. On the other hand inflation is expected to pick up further in the United Arab Emirates where CPI in 2005 is now expected to be 6.5 percent after 5.3 percent and even 3.7 percent at the beginning of the year. The highest rate of inflation in the region prevails still in Iran with an expected consumer price increase of 17.0 percent in 2005.

In *Oceania*, in 2005 an inflation rate of 3.1 percent is now expected; this is half a percentage point lower than in the previous surveys of the year. The 2005 inflation figure will be almost identical in Australia and New Zealand according to WES experts' estimates.

**US dollar seen as fairly assessed and the euro to a lesser degree as overvalued**

For the first time in more than two years the *US dollar* was not longer regarded as undervalued vis-à-vis the average of the other currencies covered in the WES panel but as appropriately valued. On the other hand the *euro* and the *British pound* continue to appear to be overvalued, but – particularly in the case of the *euro* – to a significantly lesser degree than in the past two and a half years. In contrast to the previous four survey rounds the *Japanese yen* is seen as somewhat undervalued (see Figure 11).

This overall picture characterizes the assessments in most countries. Noticeable exceptions from this general view in *Western Europe* are again Norway and Switzerland where the main world currencies (*US dollar*, *euro*, *British pound* and *Japanese yen*)

were seen as overvalued vis-à-vis the own currency (in the case of Switzerland however with the exception of the *US dollar* which was here even seen as slightly undervalued). Outside *Western Europe* the own currency is judged as generally undervalued in Russia, Kazakhstan and to a lesser degree also in Latvia, Romania and Slovakia. Also regarded as undervalued are currencies in some Latin American countries (Argentina, Brazil, Mexico, Peru and Uruguay and in some *Asian* countries (particularly

China, Japan, Indonesia, Malaysia, the Philippines and Thailand).

The own currency is regarded as generally overvalued compared to the four main currencies particularly in New Zealand, South Africa, Egypt, Turkey, Croatia, Venezuela, Colombia, South Korea, Vietnam, Sri Lanka and also Zimbabwe.

According to the responses to the supplementary survey question on the development of currencies, the *US dollar* is expected to remain stable or decrease slightly in value in the course of the next six months in most countries. In contrast to this general trend the *US dollar* is expected to increase in the course of the next six months vis-à-vis the currencies of Denmark. New Zealand, most Eastern European countries (except Slovakia) most Latin American countries with the exception of Chile, Colombia, Peru und Uruguay and in practically all African countries covered in the survey. On the other hand, the *US dollar* is expected to lose in value in the course of the next six months in most Asian countries with only a few exceptions like Pakistan, Sri Lanka and Vietnam, where the value of the *US dollar* is expected to increase.

**Interest rates: Trend of rising rates not expected to slow down**

According to the previous survey in July the expectations of further rising **short- and long-term interest rates** in the next six months were fading. However, according to this new survey this trend has not continued but was replaced by somewhat increasing interest rate expectations.



**Figure 12**

**ACTUAL SHORT-TERM INTEREST RATES AND EXPECTED TREND FOR THE NEXT 6 MONTHS (QUARTERLY DATA)**

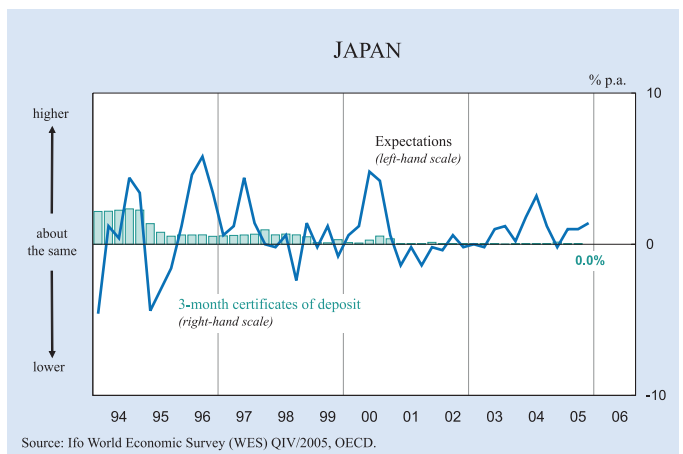
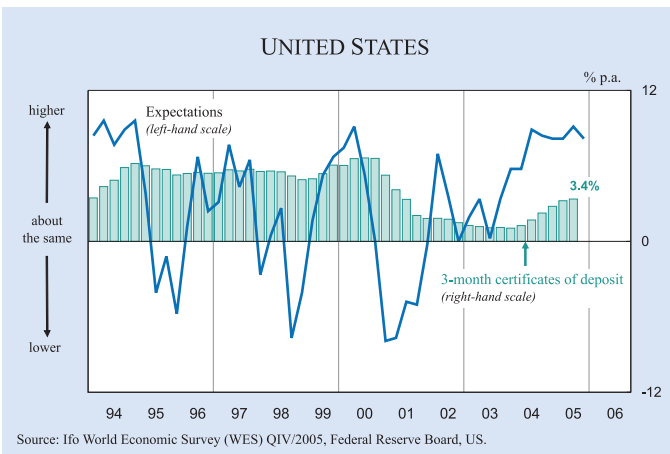
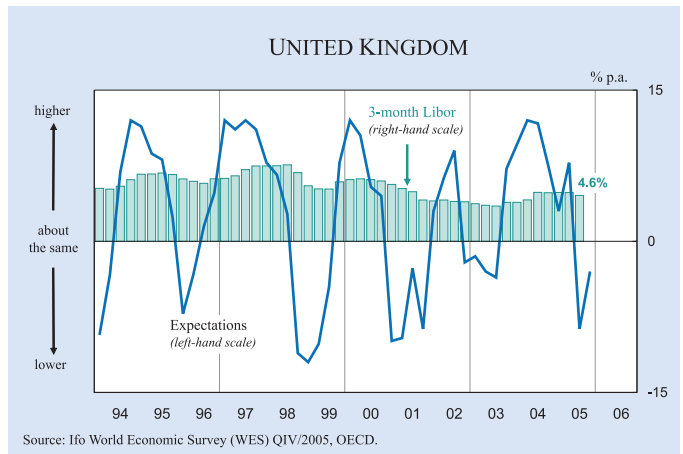
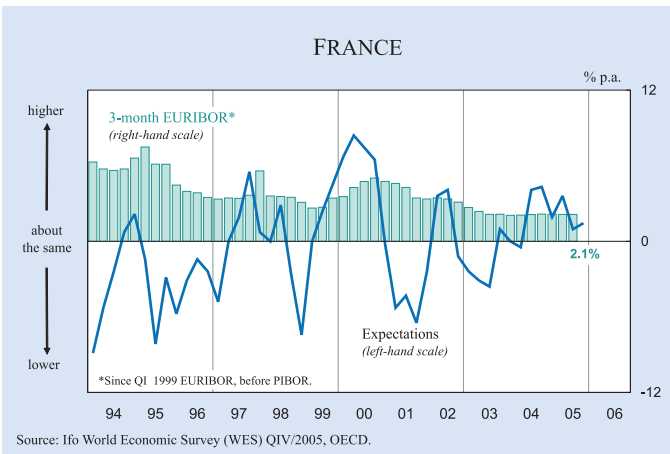
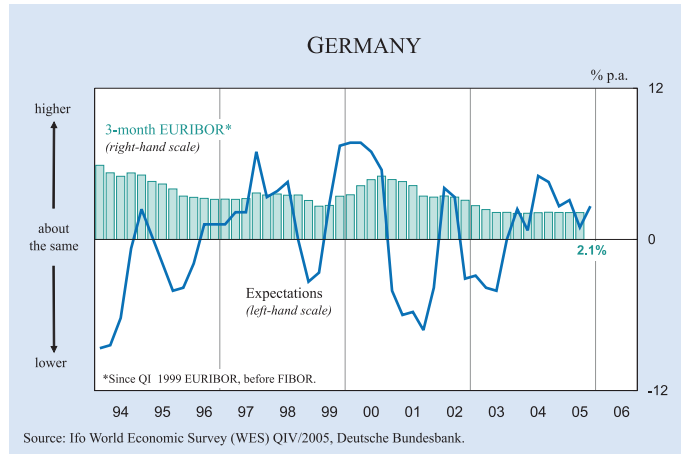
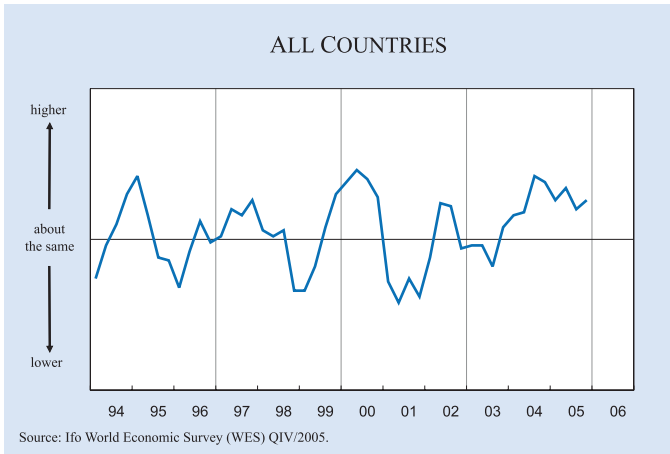


Table 2

**Expected Average Annual Growth Rates of Real Gross Domestic Product (GDP)  
Over the Next 3 to 5 Years\***

(based on WES QIV/2005 and QIV/2004)

	QIV/2005	QIV/2004		QIV/2005	QIV/2004
<b>Average of Countries</b>	<b>3.0</b>	<b>3.1</b>	<b>Latin America</b>	<b>3.4</b>	<b>3.6</b>
			Argentina	3.8	3.7
			Bolivia	3.8	2.6
<b>Western Europe</b>	<b>2.0</b>	<b>2.2</b>	Brazil	3.7	3.7
Austria	1.7	2.1	Chile	4.8	5.0
Belgium	1.4	1.7	Colombia	3.0	3.8
Cyprus	1.5	3.8	Costa Rica	3.8	3.2
Denmark	3.0	2.3	Ecuador	3.8	3.7
Finland	3.5	3.2	El Salvador	1.5	2.6
France	2.0	2.4	Mexico	3.0	3.3
Germany	1.5	1.6	Panama	3.0	3.8
Greece	3.8	3.3	Paraguay	3.3	2.8
Iceland	3.8	3.8	Peru	4.6	3.8
Ireland	3.9	4.6	Trinidad and Tobago	7.0	6.0
Italy	1.1	1.4	Uruguay	3.8	5.6
Luxembourg	3.8	3.8	Venezuela	2.3	3.3
Netherlands	2.0	1.7			
Norway	3.5	3.5	<b>Africa</b>	<b>3.3</b>	<b>4.2</b>
Portugal	1.4	2.4	Algeria	-	6.3
Spain	3.3	3.2	Egypt	3.2	3.8
Sweden	2.5	2.9	Mauritius	3.8	3.8
Switzerland	1.5	1.5	Morocco	-	3.8
United Kingdom	2.6	3.0	Nigeria	3.8	5.5
			South Africa	3.8	3.6
<b>North America</b>	<b>3.3</b>	<b>3.2</b>	Tanzania	-	6.0
Canada	3.3	3.5	Tunisia	3.8	3.8
United States	3.2	3.2	Zimbabwe	-4.0	-4.0
<b>Oceania</b>	<b>3.6</b>	<b>3.5</b>	<b>Eastern Europe</b>	<b>3.8</b>	<b>4.0</b>
Australia	3.8	3.5	Albania	5.4	4.6
New Zealand	3.0	3.5	Bosnia Herzegovina	6.0	3.8
			Bulgaria	4.2	4.3
<b>CIS</b>	<b>5.3</b>	<b>6.1</b>	Croatia	3.8	3.3
Kazakhstan	7.9	8.1	Czech Republic	3.8	3.6
Russia	5.4	6.0	Estonia	6.5	4.6
Ukraine	3.8	5.7	Hungary	3.5	3.6
			Latvia	6.3	6.0
<b>Asia</b>	<b>3.9</b>	<b>4.0</b>	Lithuania	5.6	6.0
Bangladesh	3.8	4.6	Poland	2.7	4.0
China	7.8	7.2	Romania	4.8	4.9
Hong Kong	4.7	4.2	Slovenia	3.8	3.5
India	7.2	6.2	Slovakia	5.0	4.1
Indonesia	5.2	4.1	Serbia and Montenegro	4.3	5.0
Japan	1.6	2.1			
Korea Rep.	4.1	3.3	<b>Near East</b>	<b>5.7</b>	<b>4.9</b>
Malaysia	4.1	4.7	Iran	3.2	3.2
Nepal	3.8	3.8	Israel	3.8	3.8
Pakistan	6.1	5.3	Jordan	6.3	5.7
Philippines	4.0	4.3	Kuwait	3.8	5.5
Singapore	3.8	5.9	Lebanon	3.8	3.8
Sri Lanka	5.5	4.9	Saudi Arabia	9.6	5.2
Taiwan	3.1	3.8	Turkey	4.7	5.3
Thailand	5.1	4.6	United Arab Emirates	7.4	5.8
Vietnam	7.3	6.8			

\* Within each country group or region, the country results are weighted according to the share of the specific country's exports and imports in total world trade.

Source: Ifo World Economic Survey (WES), QIV/2005.

This shift in expectations was particularly pronounced in the euro area and in the majority of the other *Western European* countries outside the euro area. An exception is Switzerland where experts expect a further slowing down in the upward trend of the interest rate cycle in the course of the next

six months. Another exception is the United Kingdom where the trend of shrinking **short-term interest rates** is expected to continue in coming months but at a slower rate than previously assumed (see Figure 12). The most pronounced increase of interest rates in coming months

amongst the *Western European* countries is expected in Norway. In *North America* the hike of interest rates appears to be still in full swing in the coming six months, in Canada even more pronounced than in the USA. In *Oceania*, both in Australia and New Zealand, short-term interest rates are no longer expected to stabilize soon at the current level or even to start shrinking but point for the time being to a renewed slight pickup. In *Eastern Europe* the trend of shrinking short-term interest rates is seen to continue but at a slightly lower rate. In contrast, the average expectations in the Czech Republic signal a moderate increase of interest rates in coming months. In *CIS* countries, particularly in Russia, the trend of shrinking interest rates will continue in the coming months according to the WES experts'. In *Latin America* interest rates will remain stable in the coming months. However, there are significant differences from country to country: Whereas the interest rate trend in Chile is still clearly up, the contrary is true in Brazil and to a lesser degree also in Mexico where the declining trend of interest rates will continue. Also in *Africa* the trends of interest rates are diverging: Whereas in South Africa and Zimbabwe the upward trend of interest rates is expected to go on, the **long-term interest rate's** tendencies in Egypt are seen to be clearly down in coming months. In *Asia* no end of the upward trend of interest rates is in sight in the coming months. Particularly in Hong Kong, Thailand, Korea Republic and also Singapore as well as Taiwan interest rates are expected to climb up further in coming months. On the other hand, in China interest rates are seen as relatively flat in the course of the next six months. In Japan and India only a rather slight increase of interest rates is forecasted by WES experts for the coming six months. In the *Near East* rather stable interest rates are expected; an exception of this overall trend is mainly Turkey where the trend of sinking interest rates prevail.

### **Stable medium-term growth trend expected**

World economic growth is expected to reach 3.0 percent p.a. in the next 3 to 5 years<sup>1</sup> (see Table 2). This figure is only marginally lower than the one given one year ago and corresponds to the average of the estimates collected in WES surveys in the years 1990 to 2000 (in both cases 3.1 percent). However, by region and country the changes are sometimes dramatic: In *Western Europe* the current

medium-term growth outlook at a 2.0 percent is by far not only the lowest one among big regions in the world but is also significantly lower than the average of past WES growth estimates in the period 1990 to 2000 (2.6 percent).

The highest medium term growth rates were expected this time in the *Near East* countries (5.7 percent); this average figure is mainly driven up by oil rich countries like Saudi Arabia and the United Arab Emirates. In the other world regions (*North America, Latin America, Asia, Oceania, Eastern Europe* and *CIS* countries and *Africa*) the expected annual growth rate in the next 3 to 5 years lies in the range of 3 percent to 5 percent.

Within the world regions there are significant differences by country: In *Western Europe* growth estimates are particularly low in Italy, Portugal, Belgium, Germany and Switzerland (1.5 percent p.a. or lower); on the upper side of the scale are Denmark, Spain, Norway, Finland, Greece, Luxembourg and Ireland (3.0 percent p.a. and more). In *Eastern Europe* the growth outlook is the lowest in Poland (2.7 percent) compared with growth figures of at least 3.5 percent in all the other countries of the region. In *Asia* the expected fastest growing countries in a medium-term perspective are China, Vietnam, India and Pakistan (more than 6 percent p.a.). The lowest medium-term growth estimate in *Asia* is reported from Japan (1.6 percent). In *Latin America* with the exception of El Salvador (1.5 percent p.a.) and Venezuela (2.3 percent p.a.), the medium-term growth rate in all other countries covered in the survey it is at least 3.0 percent p.a.

<sup>1</sup> The growth rates refer to increases and/or decreases of real GDP (gross domestic product in constant prices) in the individual countries covered in the WES panel weighted with the country share in world trade. These figures are not directly comparable with growth figures of world GDP based on purchasing power parities as is the case in the estimates presented by the IMF in its World Economic Outlook. The comparable purchasing power GDP figures are between 1.0 and 1.5 percentage points higher than the figures calculated on the price adjusted national GDP figures.

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