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CESifo WORLD ECONOMIC SURVEY

VOLUME 7, No. 3

AUGUST 2008

WORLD ECONOMIC CLIMATE

World Economic Climate deteriorates further

ECONOMIC EXPECTATIONS

Assessments of the current economic situation and economic expectations downgraded

INFLATION

Rising inflation expected in 2008

INTEREST RATES

Interest rates expected to rise

CURRENCIES

US dollar remains undervalued

SPECIAL TOPIC

Energy prices



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Ifo World Economic Survey

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Notes

The World Economic Survey (WES) assesses worldwide economic trends by polling transnational as well as national organizations worldwide on current economic developments in their respective countries. This allows for a rapid, up-to-date assessment of the economic situation prevailing around the world. In July 2008, 1,025 economic experts in 92 countries were polled.

WES is conducted in co-operation with the International Chamber of Commerce (ICC) in Paris.

Methodology and evaluation technique

The survey questionnaire focuses on qualitative information: assessments of a country's general economic situation and expectations regarding important economic indicators. It has proved to be a useful tool, since it reveals economic changes earlier than conventional 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. Overall 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 Maximilian University, Munich. Its research, concentrating on public finance, includes many diverse areas of economics.

Ifo Institute for Economic Research is 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 ECONOMIC CLIMATE INDEX FALLS

The Ifo World Economic Climate Index fell in July 2008 for the fourth time in succession to the lowest level since 2001 (73.4; 1995=100). Both the assessments of the present economic situation as well as economic expectations for the next six months deteriorated further, on a global average (see Figure 1 and 2).

World economy in the downswing

The world economic climate deteriorated for the fourth time in succession. Although the assessments of the present economic situation slipped in July, the present economy is still judged as satisfactory, on a global average. The economic expectations for the next six months, which have been continuously downgraded since the fourth quarter of 2007, point to further global economic cooling in 2008. This contrasts to the pattern of the economic climate observed in 2001, when the present economic situation was assessed as very weak, but the economic expectations were positive. Not all main economic regions are affected by the renewed deterioration of the economic climate, according to the July survey results. The economic climate index deteriorated further only in *Western Europe* and *Asia*. In the *US*, in contrast, the economic climate indicator stabilized in July, after it had fallen to its lowest level since 1991 in the April survey. However, the present economic situation is still assessed as weak. But the economic expectations for the next six months have been up-graded somewhat for the second time in succession since the *US* mortgage crisis.

The business-cycle clock illustrates the cyclical movements of

the business sentiments (see Box 1). The strong decline of the economic climate index began in summer 2007 caused by the *US* mortgage crisis. In autumn 2007 the economic climate index entered the cooling-down area of the business clock and it fell further in the first half of 2008. In the third quarter 2008 the economic climate index entered the cyclical trough area, as the assessments of the present economic situation slipped below the “satisfactory” mark, on a global average. The most important economic problem world-wide at present is the rising inflation that is aggravating the cyclical downturn.

Figure 1

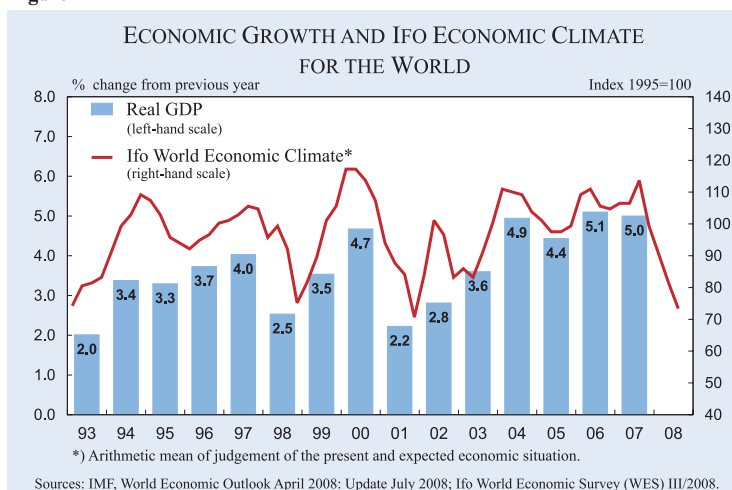
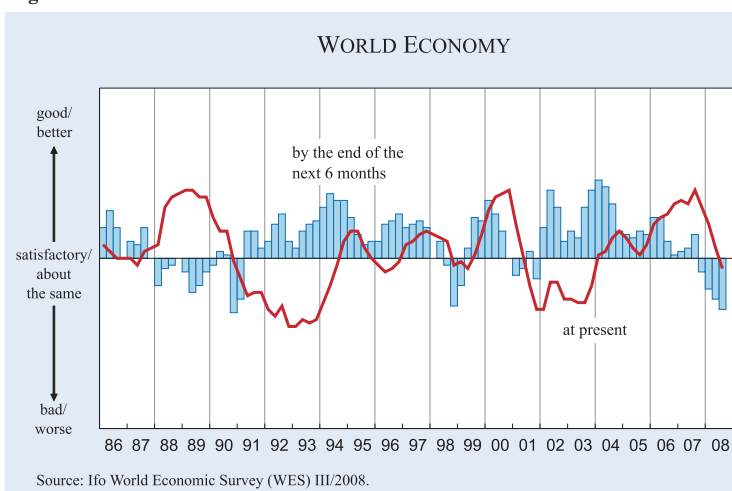


Figure 2

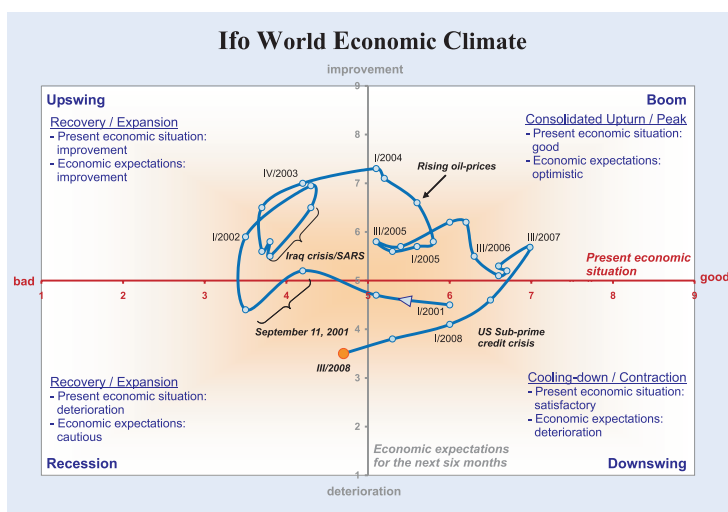


Box 1

Ifo Economic Clock and the World Economic Climate

For a global, medium-term forecast a look at the Ifo Economic Clock showing the development of the two components of the economic climate index over the last seven years visualizes the trend. The business cycle typically goes clockwise in a circle; expectations leading assessments of the present situation.

The strong decline of the economic climate index begun in summer 2007 caused by the US mortgage crisis. In autumn 2007 the economic climate index entered the cooling-down area of the business clock and it fell further in the first half of 2008. In the third quarter 2008 the economic climate index entered the cyclical trough area, as the assessments of the present economic situation slipped below the “satisfactory” mark, on a global average. The economic expectations point to further economic cooling in 2008.



The Ifo World Economic Climate is the arithmetic mean of the assessments of the current situation and economic expectations for the next six months. The correlation of the two climate components can be illustrated in a four-quadrant diagram (“Ifo Konjunkturuhr”). The assessments on the present economic situation are positioned along the abscissa, the responses on the economic expectations on the ordinate. The diagram is divided into four quadrants, defining the four phases of the world business cycle. For example, should the assessments of the interviewed experts on the present situation be negative, but the expectations became positive, the world business cycle is in an upswing phase (top left quadrant).

Greece. However, the present economic performance is still regarded as good or satisfactory in Finland, Austria, Germany and the Netherlands. In France and Belgium, in contrast, the marks of the present economic state slipped below the “satisfactory” level. The present economic situation was assessed as poor in July in Italy, Spain, Portugal and Ireland.

Outside the euro area the economic climate cooled off as well. In Sweden, Norway, Denmark and Switzerland the assessments of the present economic situation deteriorated in July, although the surveyed economists are still judging the economic performance as strong. However, they forecast further economic cooling in the second half of 2008. Economic deterioration is also expected by the surveyed economists in the United Kingdom. The assessments of the present economic performance were strongly downgraded. The present economy in the UK is now assessed as poor, by the WES experts.

Western Europe: Economic cooling

The overall economic climate indicator for Western Europe deteriorated for the fourth time in succession in July. Both the assessments of the present economic situation as well as economic expectations for the next six months have been downgraded somewhat (see Figure 3 and 4 and Box 2). However, as on the world average, the present economic situation is still assessed as satisfactory in the majority of Western European countries, except Italy, Spain, Portugal and Ireland.

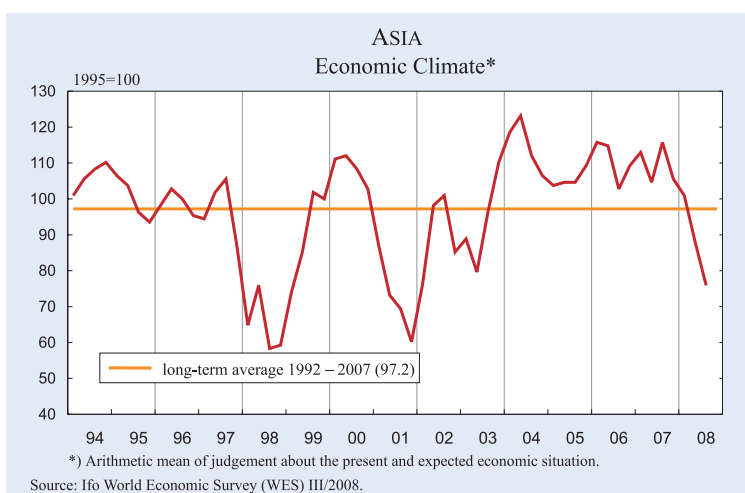
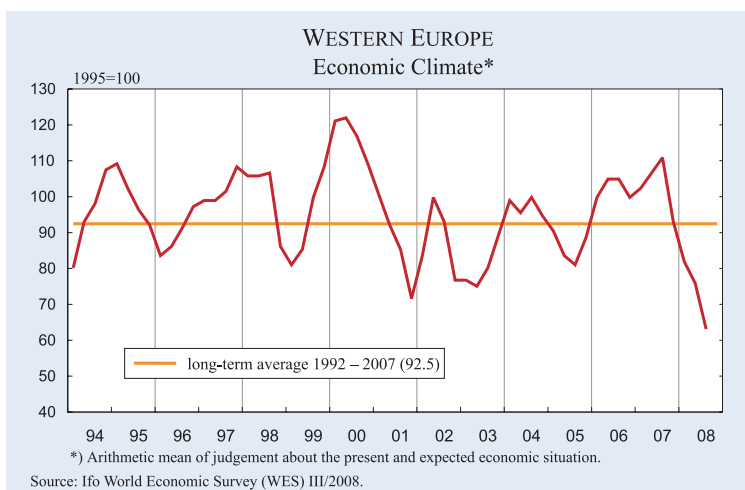
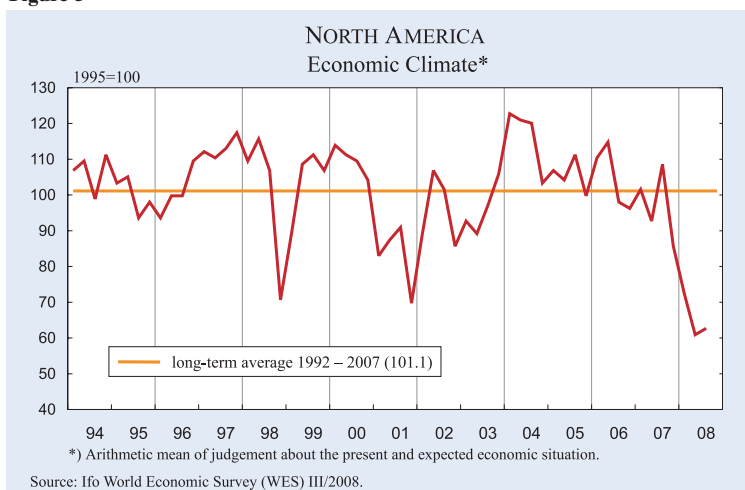
The economic climate index declined in all euro area countries except Slovenia. The economic expectations for the second half of 2008 have been downgraded strongly in almost all countries of the euro area. Also the assessments of the present economic situation were revised downward, except in Slovenia and

North America: Economic climate index stabilizes

Unlike other main economic regions, the economic climate indicator in North America has not further deteriorated in July (see Figure 3). The economic expectations for the next six months even improved somewhat. The present economic situation is still assessed with the lowest marks in a decade, but the WES experts have not downgraded their assessments further (Figure 6).

In the United States the economic climate stabilized in July. The assessments of the present economic situation remained at the very low level. The economic expectations, however, have been upgraded somewhat for the second time in succession, pointing to an economic stabilization in the second half of 2008. Given the weak US dollar, the export sector is expected to pick up strongly, according to WES experts.

Figure 3



Also in *Canada* the economic climate stabilized in July. The present economy is performing satisfactorily, according to WES experts. But the economic prospects for the next six months remain clouded.

“satisfactory” level was the economic situation judged in *Serbia*. However, also here the surveyed economists remain fairly optimistic. In *Croatia*, in contrast, an economic weakening is foreseen for the second half of 2008, by the WES experts. Although the export sector

Central and Eastern Europe: Moderate cooling

The economic climate cooled only slightly in *Central and Eastern Europe* (see Figure 4). The assessments of the present economic situation remained at a favourable level. The economic expectations for the next six months have been downgraded somewhat, on average for the Central and Eastern European countries (see Figure 8).

The present economic situation is regarded as particularly favourable in the *Czech Republic* and *Slovakia*. The surveyed economists expect the economy to strengthen further in the next six months. Also in *Bulgaria* the present economic situation was assessed as good. The expectations for the next six months point to an economic stabilization. However, in the other countries of the region, the economic prospects have become clouded, although the present economic state was generally assessed as satisfactory. A pronounced decline of economic growth is expected by the surveyed economists in *Estonia*, *Hungary*, *Latvia*, *Lithuania*, *Poland* and *Romania*.

In the countries outside the *European Union* economic trends diverge, according to the July survey. The present economic situation was assessed as “favourable” in *Albania*. The surveyed economists expect further economic strengthening, particularly of the export sector in the next six months. As somewhat below the

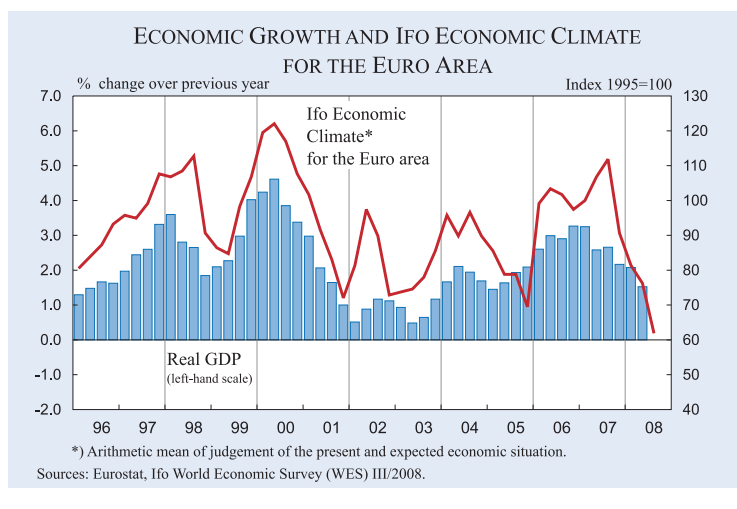
Box 2

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

The Ifo World Economic Climate for the 15 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 July results are based on the responses of 273 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 Ifo Economic Climate in the euro area has worsened again in the third quarter of 2008 for the fourth time in succession. The decline in the Ifo indicator is both the result of less positive assessments of the current economic situation as well as clearly more pessimistic expectations for the coming six months.

The economic climate has further clouded over in nearly all countries of the euro area in the third quarter of 2008. Particularly negative assessments of the current economic situation have come from *Italy, Spain, Portugal, Ireland* and *Belgium*. Favourable assessments of the current situation continue to come from *Finland, Austria, Germany* and the *Netherlands*, however. In the opinion of the WES experts, the slowing in economic activity will continue in all countries of the euro area in the coming six months.



is expected to remain buoyant, capital expenditures and private consumption are expected to weaken strongly in the next six months.

CIS: Favourable economic climate prevails

The overall economic climate index for the CIS countries covered by WES (*Georgia, Russia, Ukraine, Kazakhstan, Kyrgyzstan* and *Uzbekistan*) remained stable at a favourable level in July.

The economic climate continues to be highly favourable in *Russia*, according to WES experts. The present economic situation was again assessed as strong. The economic expectations for the second half of 2008 remain positive. Private consumption and capital expenditures are expected to pick up somewhat in the course of the next six months. A favourable economic climate also prevails in

Georgia, according to WES experts, although this assessment was given by WES experts before the armed conflict started in South Ossetia. In *Kazakhstan* the economic climate index fell. The assessments of the present economic situation have been downgraded somewhat, but the present economic performance is still regarded as “satisfactory”. The economic expectations for the next six months have also been revised downward. Although the export sector is foreseen to remain strong, private consumption and capital expenditures are expected to decline in the second half of 2008. The economic climate strongly deteriorated in the *Ukraine*. The assessments of the present economic situation fell clearly below the “satisfactory” level. The surveyed economists do not expect an economic turnaround in 2008. Also in *Kyrgyzstan* the economic climate strongly deteriorated. The present economic situation is assessed as “bad” by the WES experts. They expect further economic worsening in 2008. Private consumption, capi-

tal expenditures and the export sector are expected to weaken further.

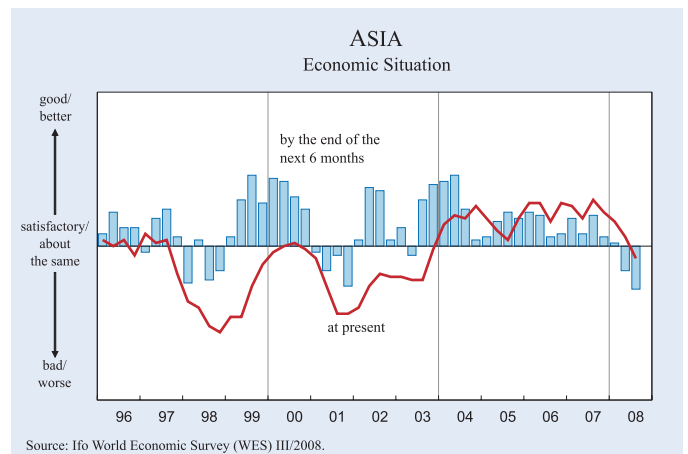
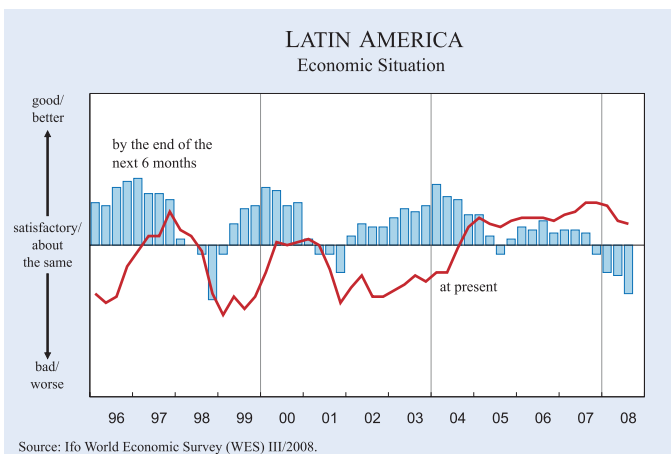
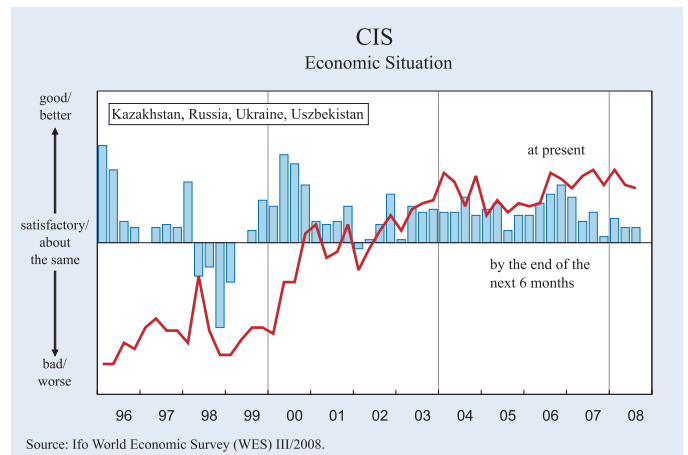
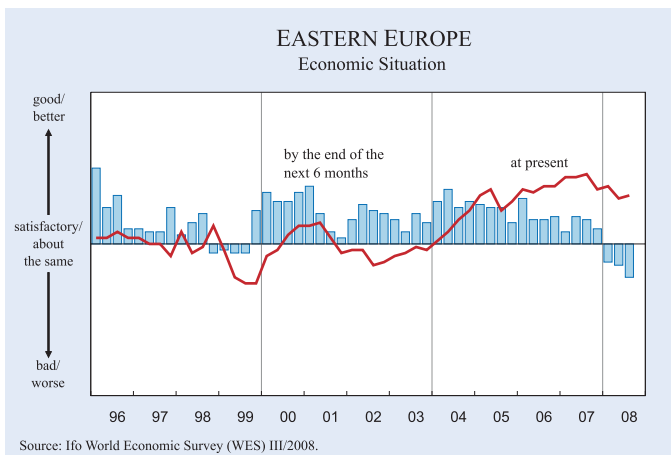
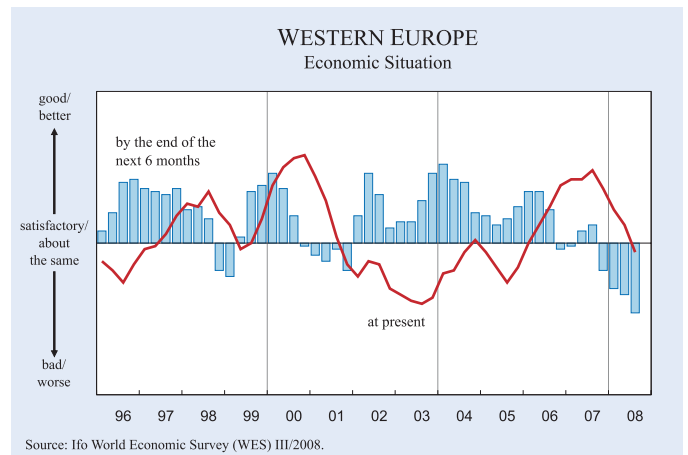
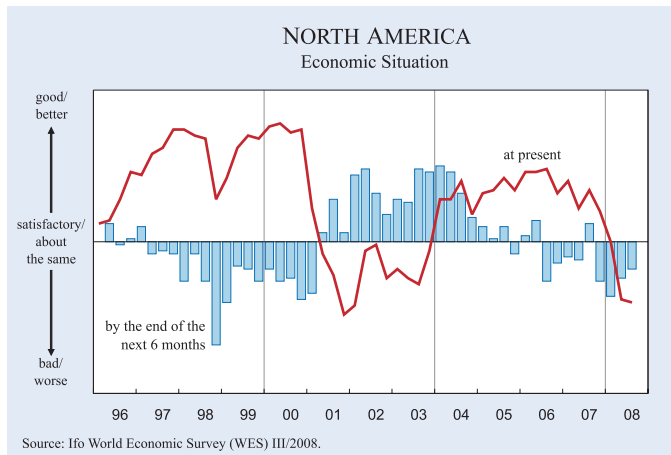
Asia: Economic climate index deteriorates

The economic climate in *Asia* deteriorated for the fourth time in succession and has fallen to the lowest level since 2001 (see Figure 3). Both the assessments of the present economic performance and economic expectations for the next six months have again been downgraded, on average, for the region (see Figure 8).

The economic climate index fell in all major Asian economies, particularly strongly in *India* and *Malaysia*. However, the present economic performance in these two countries is still judged as “satisfactory” by the surveyed economists. But the economic expectations for the second half of 2008

Figure 4

SELECTED REGIONS



turned clearly negative. Major decline is expected for private consumption and capital expenditures. Rather cautious economic expectations prevail in *China* and *Hong Kong*. Although the present economic state is rated as good in these economies too. In *China* the WES experts expect a pronounced weakening of the export sector in the next six months. The same forecast applies to *Hong Kong*. Furthermore, the increase of private consumption and capital expenditures is expected to slow down in the second half 2008. The economic climate index deteriorated very strongly in *Taiwan*, *Thailand* and the *Philippines*. The assessments of the present economic situation slipped very strongly, although the surveyed economists are still judging the present economy as “satisfactory”. But they forecast a pronounced decline in the second half of 2008, in particular in *Thailand* and the *Philippines*. In *Japan* and *South Korea* the economic climate continues to deteriorate. The assessments of the present economic situation have clearly fallen below the “satisfactory” level. The surveyed economists judge the present economic situation as “bad”. They expect further worsening in the next six months, particularly in *Japan*. In *South Korea* the export sector is expected to strengthen, serving as the driving engine for an economic rebound. In *Pakistan* and *Sri Lanka* the economic climate clearly worsened. In *Sri Lanka* the present economic situation is now assessed with the lowest possible marks on the WES scale. Also in *Pakistan*, WES experts are generally pessimistic regarding an economic turnaround in 2008. The only countries in the *Asian* region where the surveyed economists remained optimistic are *Vietnam*, *Indonesia* and *Bangladesh*. Although the assessments of the present economic situation worsened in these three economies too and have fallen below the “satisfactory” level, the WES experts are optimistic concerning an economic recovery in 2008.

Oceania: Economic slowdown

The economic climate deteriorated further in *Australia* and *New Zealand* (see Figure 6). However, in *Australia* the present economic situation is still assessed rather positively. But the economic outlook for the coming six months remains clouded, pointing to further economic slowdown in the second half of 2008. Capital expenditures and private consumption are expected to weaken in the next six months. The export sector, however, is forecast too strengthen. In *New Zealand* the assessments of the present eco-

nomical performance again strongly deteriorated. The surveyed WES experts regard the present economy as very weak. The economic expectations for the next six months continue to be pessimistic regarding both capital expenditures and private consumption. The export sector, however, is expected to strengthen somewhat, as in *Australia*, and remains the driving engine of the *New Zealand* economy.

Latin America: Diverging economic trends

The economic climate index deteriorated also in *Latin America* as a whole in July. However, there are diverging economic trends in the region (see Figure 9).

A highly favourable economic climate continues to prevail, according to WES experts, in *Paraguay*, *Peru*, *Trinidad and Tobago* and *Uruguay*. The present economic situation in all these economies is assessed with very high marks on the WES scale. The economic expectations for the next six months are very positive. Private consumption, capital expenditures and the export sector are expected to strengthen further in 2008. The economic situation is expected to stabilize in *Guatemala* and *Panama*. In *Brazil*, *Colombia*, *Costa Rica*, *El Salvador* and *Mexico* the present economic performance is assessed as strong by WES experts. The economic expectations in these economies, however, strongly deteriorated, pointing to an economic cooling in the next six months. The increase of private consumption and capital expenditures is forecast to slowdown in the course of the next six months, but the export sector is expected to remain strong in all these countries, except *Mexico*. Growing exports are also forecast by the WES experts in *Chile*, *Ecuador* and *Bolivia*, although the general economic expectations remained rather cautious. In *Chile*, the assessments of the present economic situation slipped below the satisfactory level in July, and in *Bolivia* and *Ecuador* the present economic performance is regarded as unsatisfactory by the surveyed economists. In *Argentina*, the assessments of the present economic situation slipped further and WES experts are now judging the present economy as weak. Except for the export sector, they expect further economic deterioration in 2008. Also in *Venezuela* the WES experts have become pessimistic. The export sector that was driving the business sentiments in *Venezuela* is now expected to weaken.

Near East: Stable economy

The economic climate in the countries surveyed in the *Near East* remains stable (see Figure 10). In the *United Arab Emirates, Kuwait and Saudi Arabia* the present economic situation is assessed as highly favourable. Economic expectations for the first half of 2008 remained optimistic. In *Iran*, in contrast, the economic climate continues to deteriorate. The present economic situation is now assessed as bad. WES experts expect further economic deterioration in 2008. In *Lebanon* the surveyed economists are fairly optimistic regarding an economic recovery in the near-term future. They expect strengthening of capital expenditures, private consumption and the export sector in the next six months. The economic climate also improved somewhat in *Turkey*, according to WES experts, although the present economic performance is still regarded as below the “satisfactory” level. In *Israel*, the present economic situation was assessed as good by the surveyed economists. However, the economic expectations have been further revised downward and are pointing to an economic cooling in 2008.

Africa: Economic downturn in South Africa

The economic climate index deteriorated further in *South Africa* (see Figure 10), due to less positive assessments of the current economic situation. The economic expectations for the next six months have not been further downgraded. However, they are still pointing to further economic deterioration in 2008. An economic deterioration is also expected by the WES experts in the North African countries, *Morocco and Tunisia*, as well as in *Nigeria and Mauritius*. No good news have come from *Zimbabwe*, where disastrous economic circumstances continue to prevail. In *Kenya and Tanzania*, in contrast, the surveyed economists expect an economic stabilization in the second half of 2008.

2008: No halt to higher inflation expectations

For the average of 2008 WES experts expect, on a worldwide scale, an inflation rate of 5.2 percent; this is significantly higher than the 2007 inflation figure (3.2 percent) and the rate reported for this year in April (4.2 percent). The forecasted acceleration of

inflation is a world-wide phenomenon, with hardly any exceptions. Inflation expectations for 2008 picked up particularly in *CIS* countries (from 12.0 in April 2008 to now 14.5 percent) and in *Latin America* (from 7.9 to now 9.7 percent).

It is an open question whether the decline of oil prices and other raw material prices which started in early August and was not covered in this quarter's WES survey may improve the bleak 2008 inflation outlook somewhat.

In the *euro area* the inflation outlook for 2008 has worsened further and now stands at 3.6 percent, which is almost twice as high as the European Central Bank's target of “slightly below 2.0 percent”. The highest inflation rates in the *euro area* in 2008 are expected again in *Slovenia* (5.8 percent) followed by *Spain* (5.0 percent), *Ireland* and *Greece* (each 4.7 percent). The relatively best price performance in 2008 is expected in *Portugal* (2.8 percent), the *Netherlands* (3.0 percent) as well as *Germany* (3.1 percent).

In *Western Europe* outside the *euro area*, expectations for inflation in 2008 are – as in previous years – still relatively low in *Switzerland* (2.4 percent). In the two other former low inflation countries, *Sweden* and *Norway*, inflation is expected to equal more or less the European average of close to 3.5 percent in 2008; the same holds true for the *United Kingdom*.

In the *United States* inflation expectations for 2008 edged up further from 3.5 in April to 3.8 percent in July. Also in *Canada*, where the inflation outlook for this year stood in April at a relatively moderate level of 2.1 percent, the new forecast for 2008 is significantly higher (2.8 percent).

In *Asia* consumer price inflation in 2008 is expected to reach 5.3 percent, almost one and a half percentage points higher than expected in the April survey. The biggest jump of 2008 price expectations between April and July occurred in *Vietnam* (from 15.0 to 23.5 percent), *India* (from 6.5 to 9.6 percent), *Indonesia* (from 7.0 to 11.5 percent) and *Pakistan* (from 10.5 to 14.0 percent). The lowest inflation rates in 2008 will continue to prevail in *Japan* (1.7 percent), in *Singapore* (3.5 percent) and in *Taiwan* (3.7 percent).

In *Central and Eastern Europe*, inflation in 2008 is seen at 6.3 percent, which is significantly higher

Table 1

Inflation Rate Expectations for 2008
(based on WES QIII/2008 and QII/2008)

Region	QIII/2008	QII/2008	Region	QIII/2008	QII/2008
Average of 90 countries*	5.2	4.2	Latin America	9.7	7.9
<i>World Bank classification:</i>			Argentina	22.5	24.5
High-income countries	3.7	3.2	Bolivia	17.5	16.0
Middle-income countries	9.6	7.7	Brazil	6.7	4.8
Upper-middle	9.2	7.8	Chile	7.5	5.5
Lower-middle	10.5	7.5	Colombia	6.3	5.7
Low-income countries	12.0	8.4	Costa-Rica	12.5	12.0
EU 27 countries	3.8	3.2	Ecuador	10.5	6.0
EU countries (old members) ^{a)}	3.6	2.9	El Salvador	6.8	5.1
EU countries (new members) ^{b)}	6.1	5.7	Guatemala	11.5	8.5
Euro area ^{c)}	3.6	2.9	Mexico	5.9	4.4
Western Europe	3.5	2.9	Panama	8.0	6.0
Austria	3.3	2.9	Paraguay	11.0	8.3
Belgium	4.5	3.3	Peru	5.1	3.4
Cyprus	–	4.5	Trinidad and Tobago	11.0	12.0
Denmark	3.6	3.1	Uruguay	8.0	7.4
Finland	3.7	3.3	Venezuela	32.0	27.0
France	3.3	2.7	Asia	5.3	3.9
Germany	3.1	2.7	Bangladesh	10.0	9.3
Greece	4.7	3.7	China	6.6	6.4
Iceland	–	8.0	Hong Kong	5.1	4.6
Ireland	4.7	4.1	India	9.6	6.5
Italy	3.4	3.0	Indonesia	11.5	7.0
Luxembourg	3.4	3.0	Japan	1.7	1.0
Malta	3.5	3.0	Malaysia	5.6	3.4
Netherlands	3.0	2.5	Pakistan	14.0	10.5
Norway	3.3	2.8	Philippines	8.0	5.5
Portugal	2.8	2.6	Singapore	3.5	3.0
Spain	5.0	4.0	South Korea	4.7	4.0
Sweden	3.5	3.0	Sri Lanka	23.5	17.5
Switzerland	2.4	1.8	Taiwan	3.7	2.9
United Kingdom	3.6	3.0	Thailand	7.6	4.7
Eastern Europe	6.3	5.8	Vietnam	23.5	15.0
Albania	5.7	4.1	Near East	10.5	9.3
Bulgaria	10.5	9.6	Iran	26.5	18.0
Croatia	6.0	4.6	Israel	3.9	2.7
Czech Republic	5.9	5.6	Jordan	12.0	5.7
Estonia	8.9	7.1	Kuwait	10.0	8.3
Hungary	6.7	6.3	Lebanon	8.0	–
Latvia	15.5	13.5	Saudi Arabia	6.0	7.6
Lithuania	10.5	8.1	Turkey	10.5	9.3
Poland	4.5	4.4	United Arab Emirate	12.0	11.5
Romania	7.0	7.2	Africa*	n.a.	n.a.
Serbia	12.5	9.3	Kenya	26.5	13.8
Slovakia	3.9	3.4	Mauritius	10.0	9.0
Slovenia	5.8	5.1	Morocco	3.0	–
CIS	14.5	12.0	Nigeria	10.0	8.6
Kazakhstan	14.0	11.0	South Africa	11.3	9.0
Kyrgyzstan	28.0	18.0	Tunisia	10.0	5.3
Russia	13.5	11.5	Zimbabwe	<i>Hyperinflation</i>	
Ukraine	20.0	15.5	Oceania	3.9	3.4
Uzbekistan	18.0	12.0	Australia	3.9	3.4
North America	3.6	3.2	New Zealand	3.9	3.3
Canada	2.8	2.1			
United States	3.8	3.5			

Within each country group or region the country results are weighted according to the share of the specific country's exports and imports in the total world trade (without Zimbabwe).

^{a)} Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, United Kingdom – ^{b)} Czech Rep., Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovenia, Slovakia (from 1. May 2004), Bulgaria and Romania (from 1. January 2007) – ^{c)} Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Slovenia.

Source: Ifo World Economic Survey (WES) III/2008 and II/2008.

Figure 5a

EUROPEAN UNION

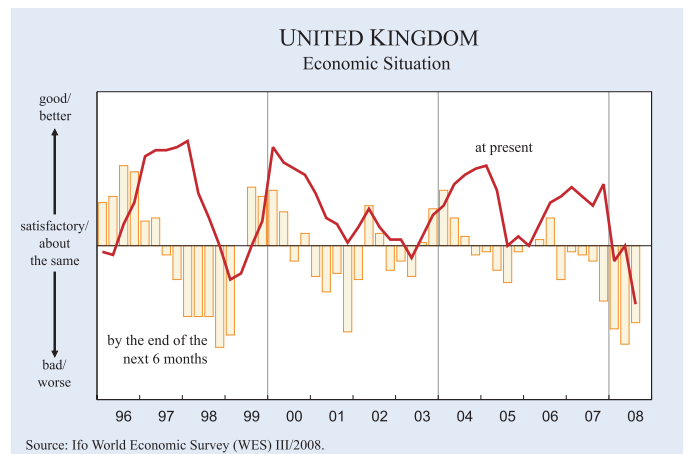
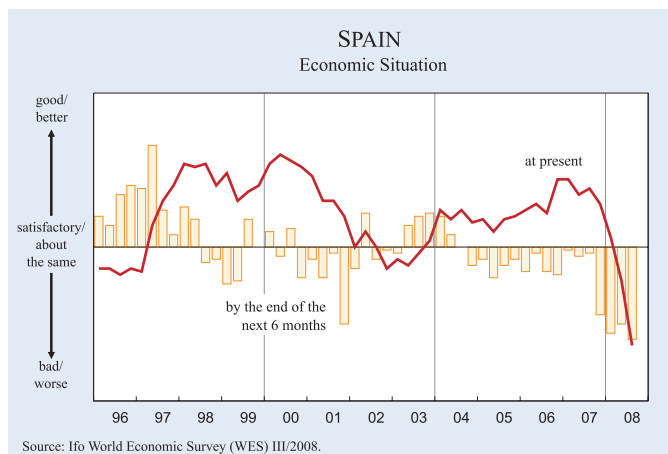
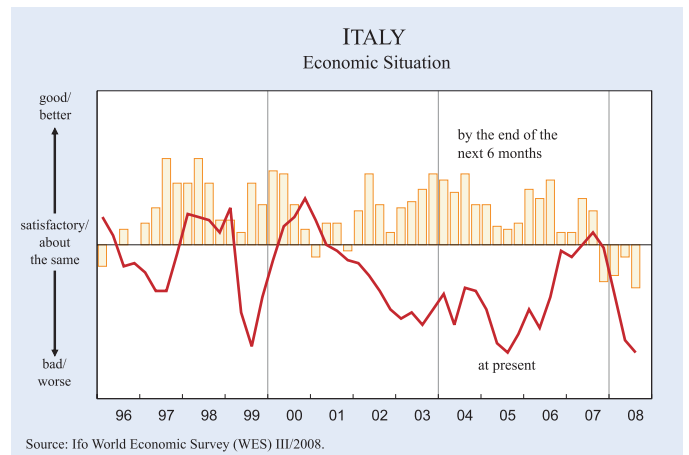
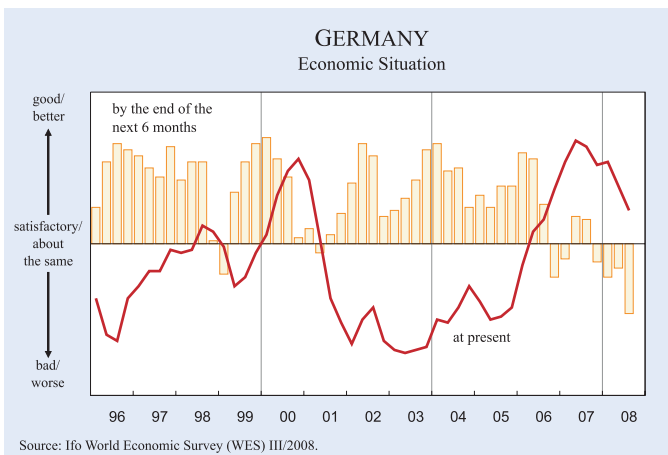
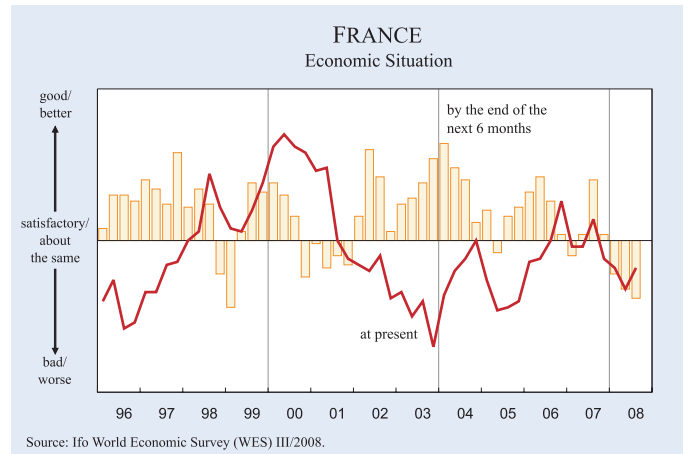
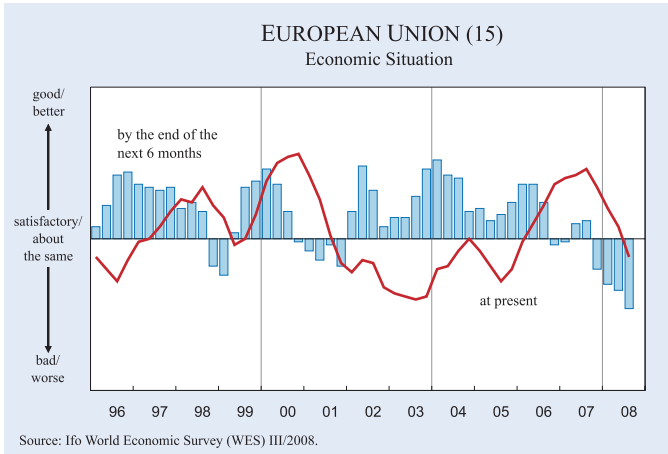
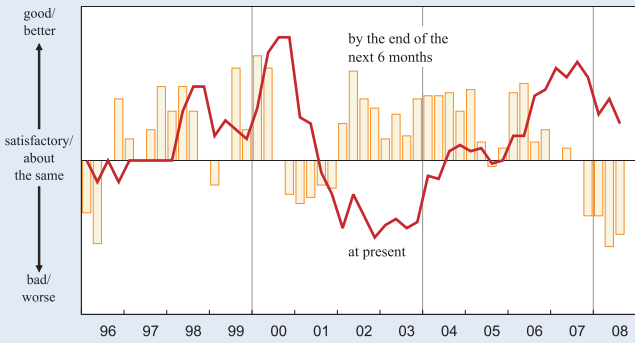


Figure 5b

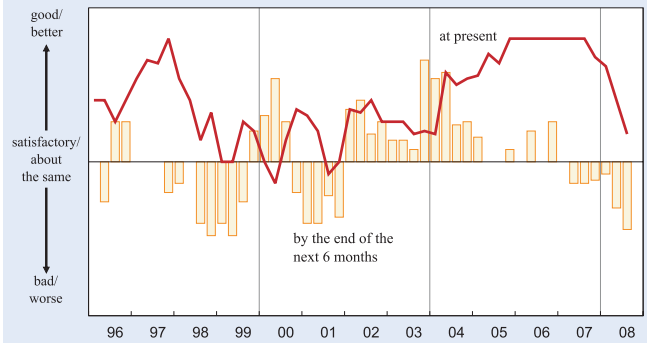
EUROPEAN UNION

AUSTRIA
Economic Situation



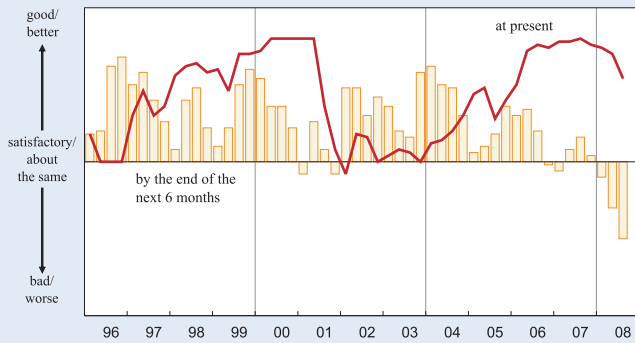
Source: Ifo World Economic Survey (WES) III/2008.

DENMARK
Economic Situation



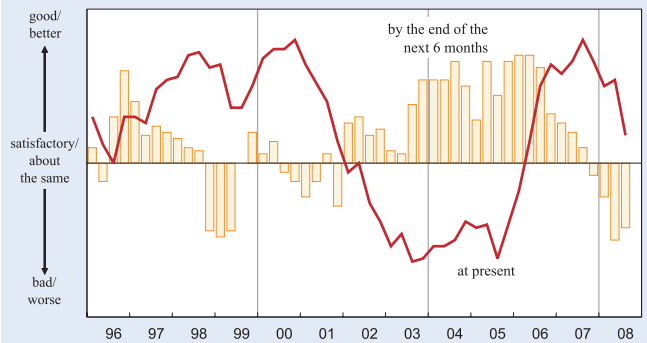
Source: Ifo World Economic Survey (WES) III/2008.

FINLAND
Economic Situation



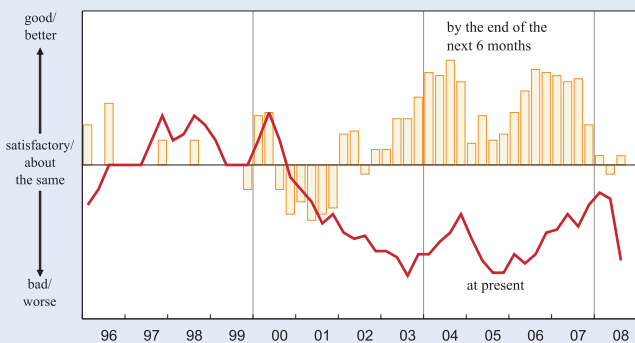
Source: Ifo World Economic Survey (WES) III/2008.

NETHERLANDS
Economic Situation



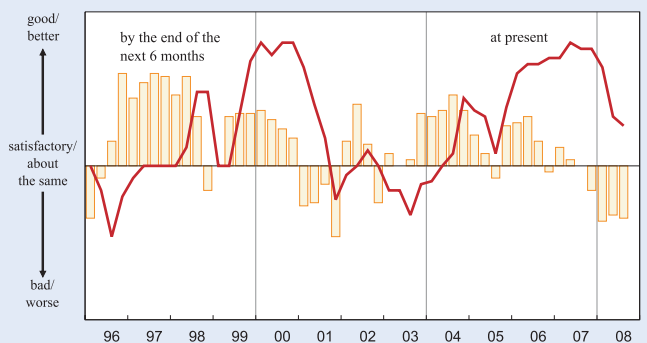
Source: Ifo World Economic Survey (WES) III/2008.

PORTUGAL
Economic Situation



Source: Ifo World Economic Survey (WES) III/2008.

SWEDEN
Economic Situation



Source: Ifo World Economic Survey (WES) III/2008.

Figure 6

NORTH AMERICA, OCEANIA AND CIS

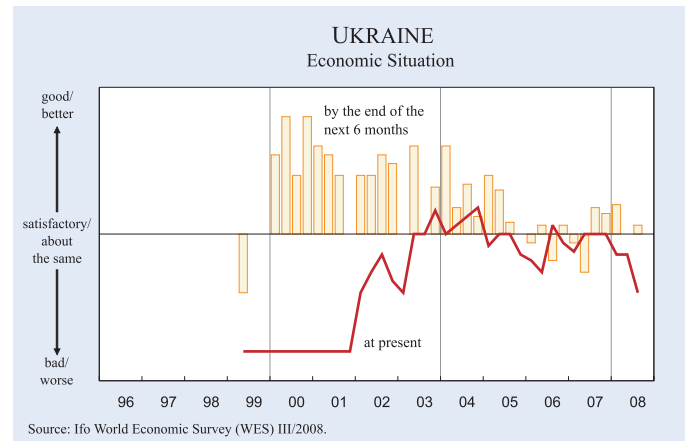
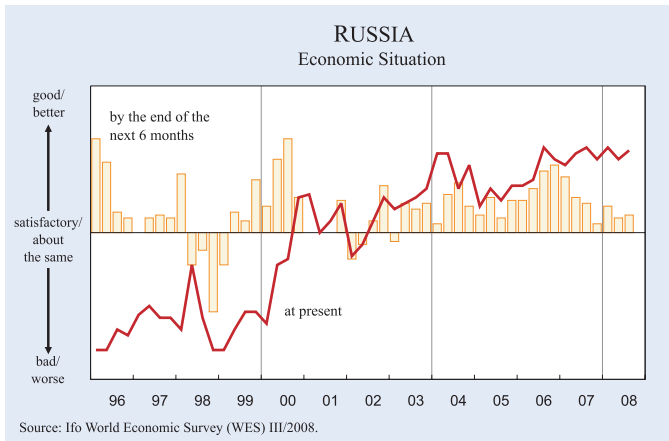
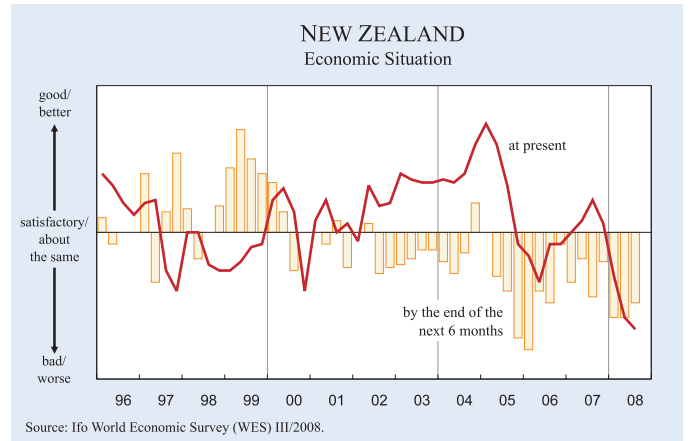
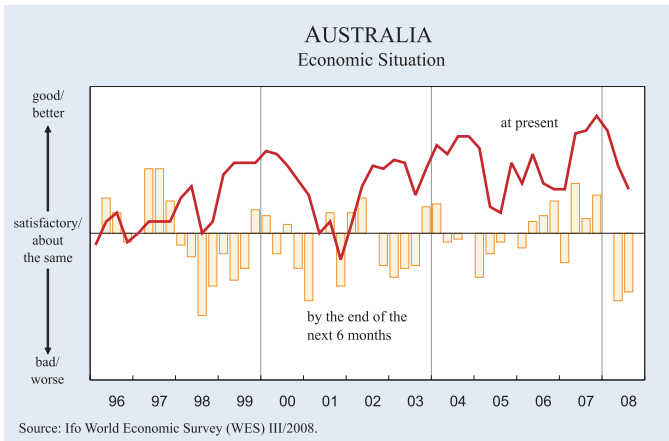
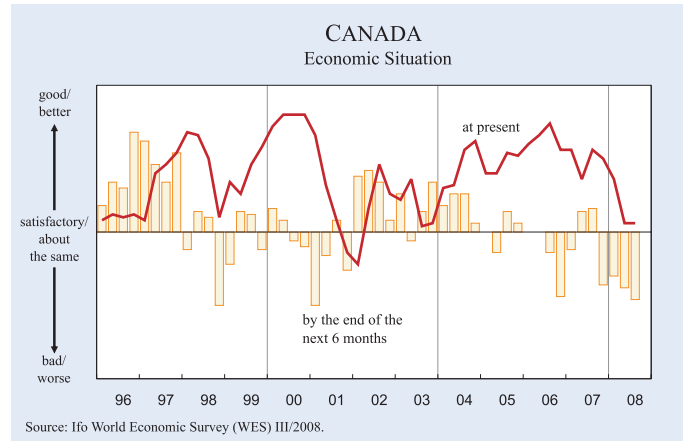
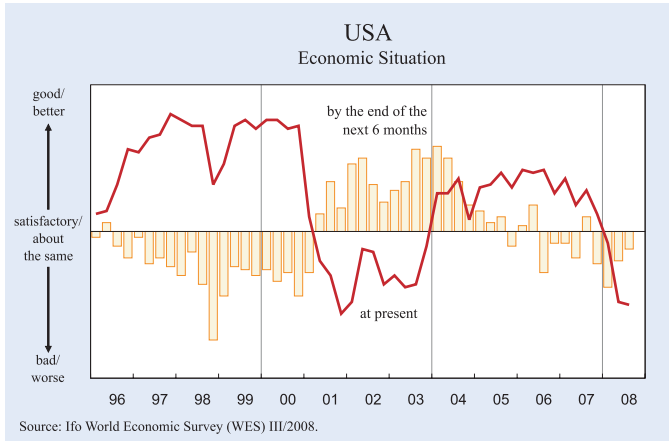


Figure 7

EASTERN EUROPE

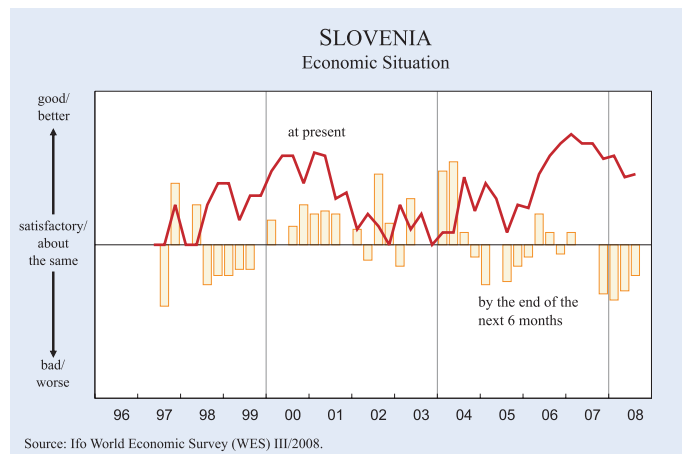
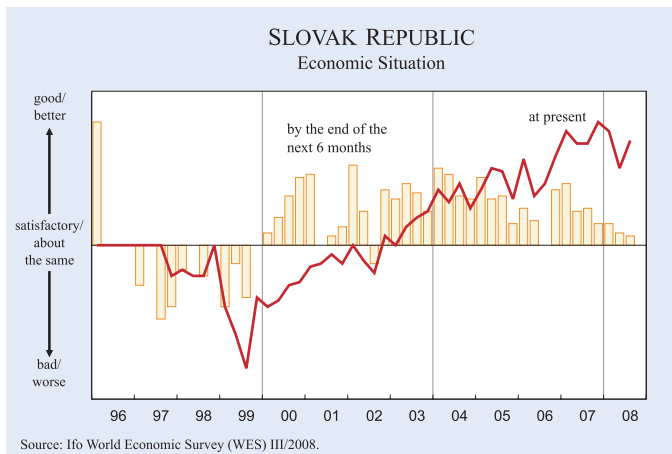
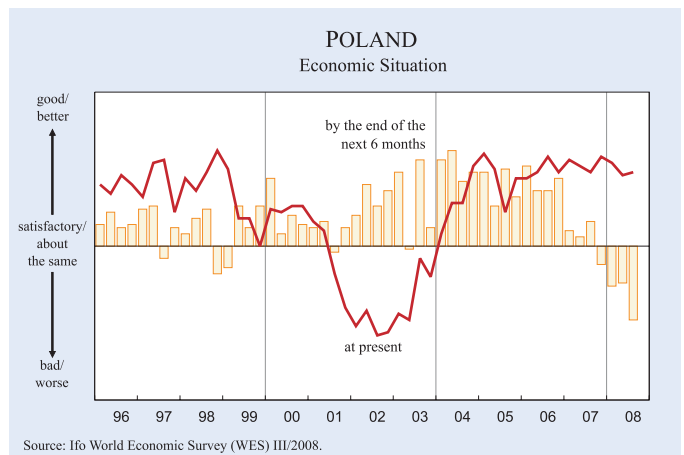
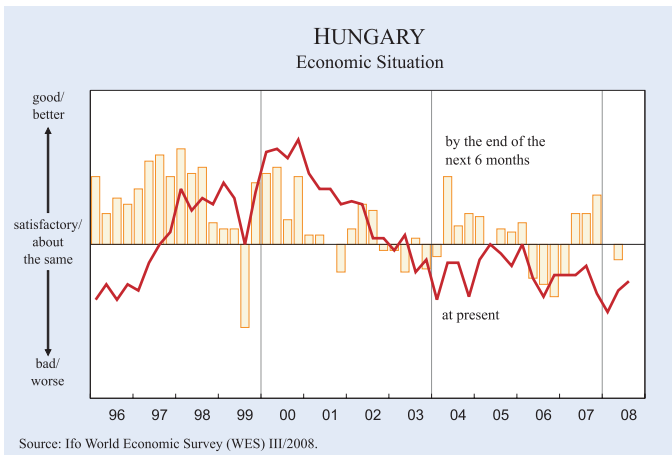
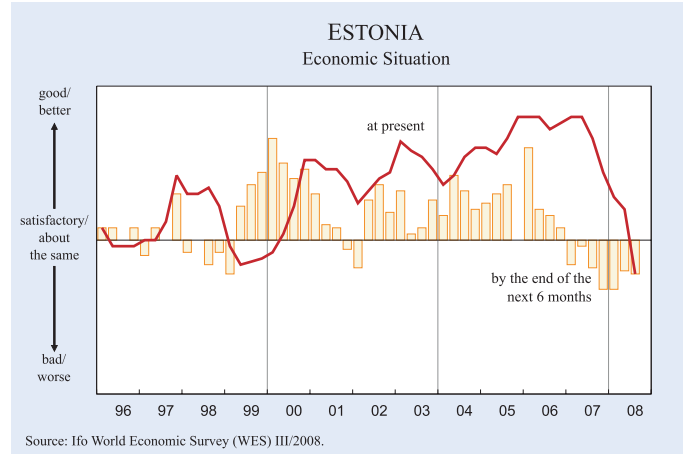
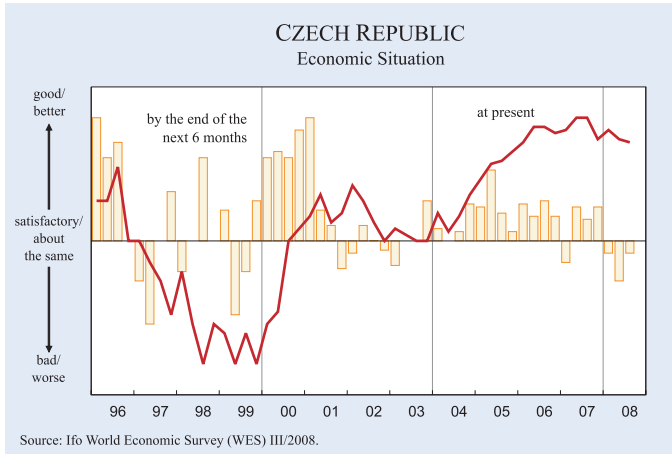


Figure 8

ASIA

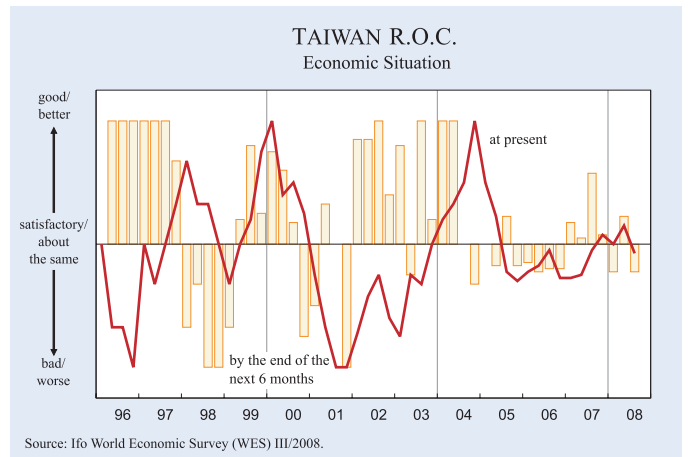
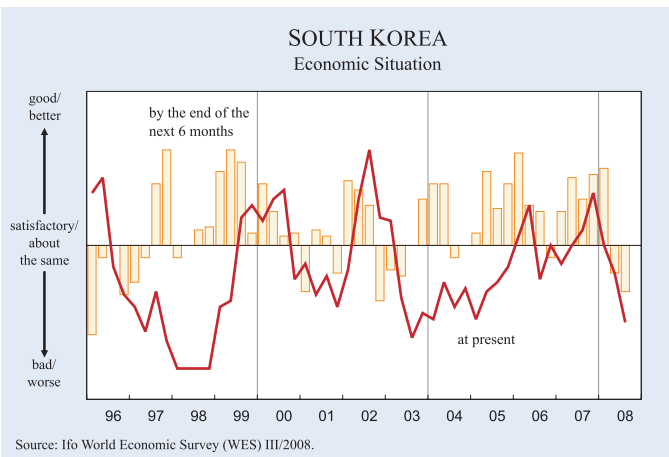
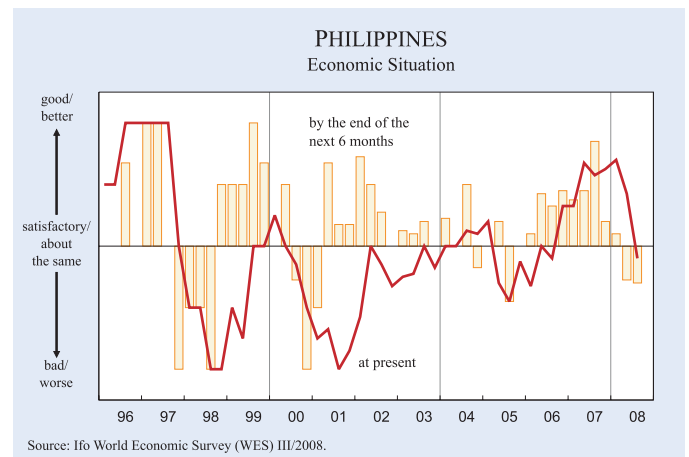
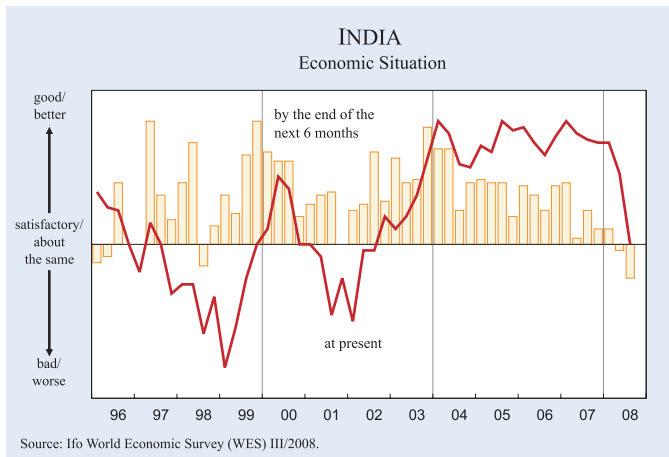
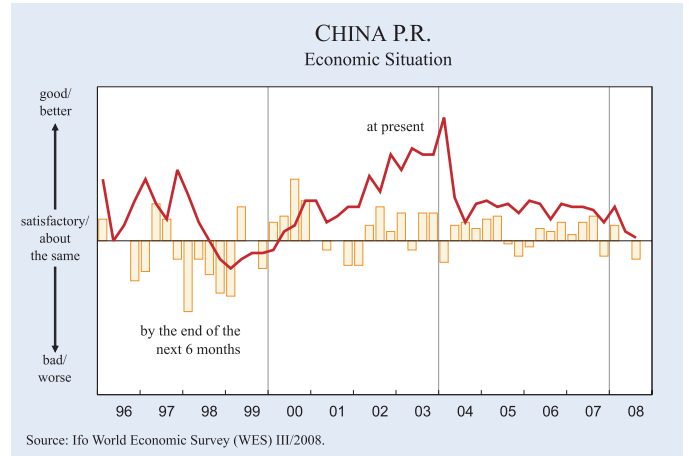
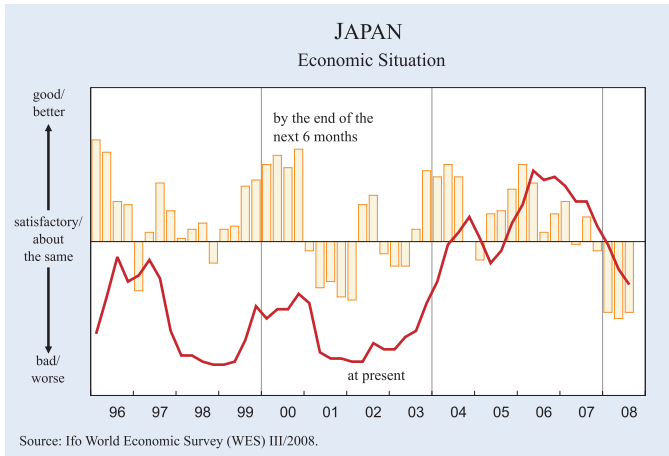


Figure 9

LATIN AMERICA

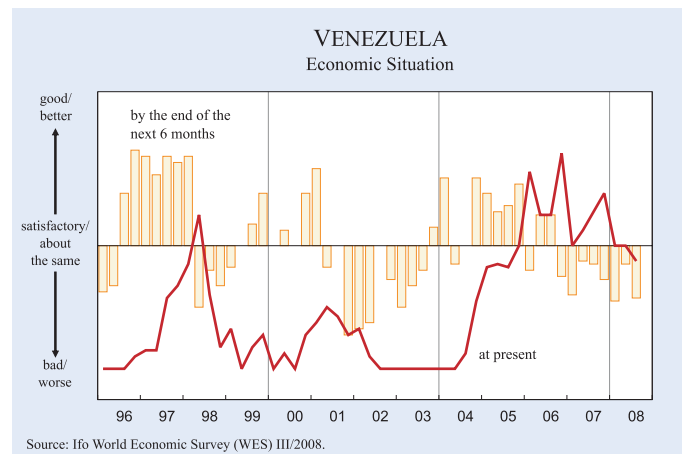
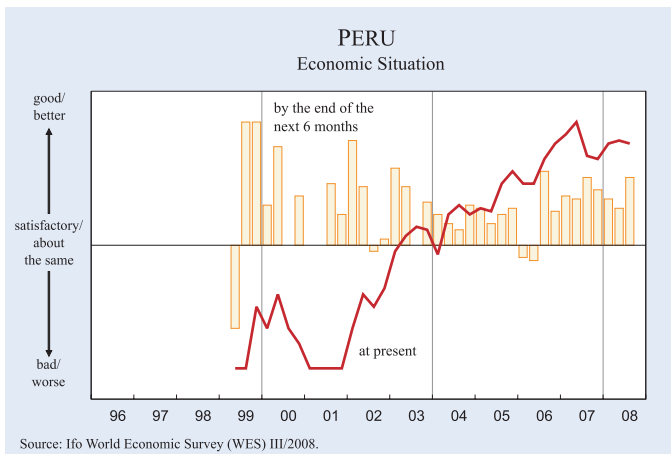
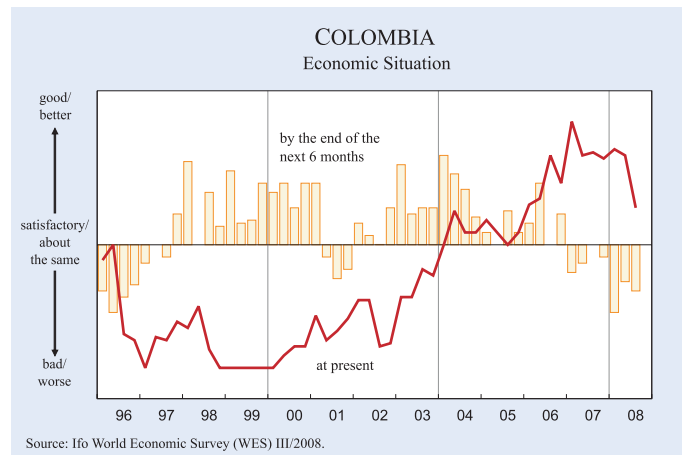
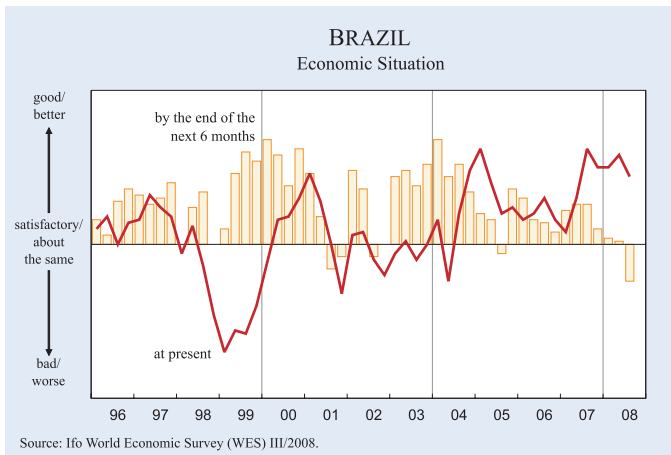
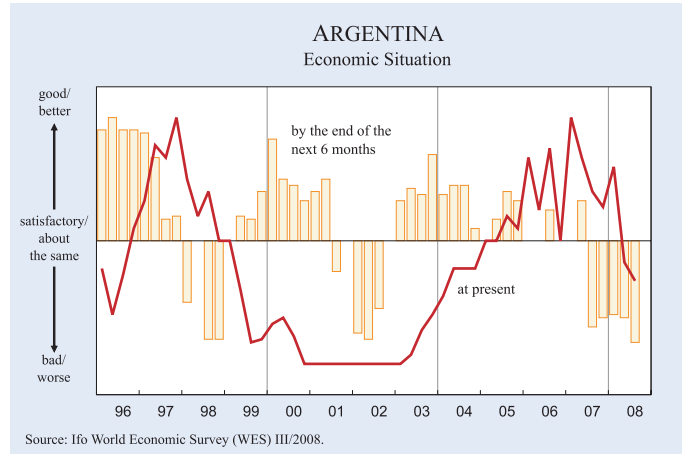
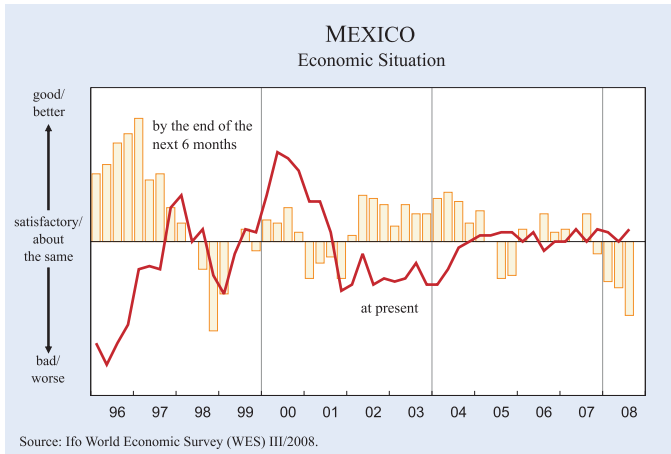
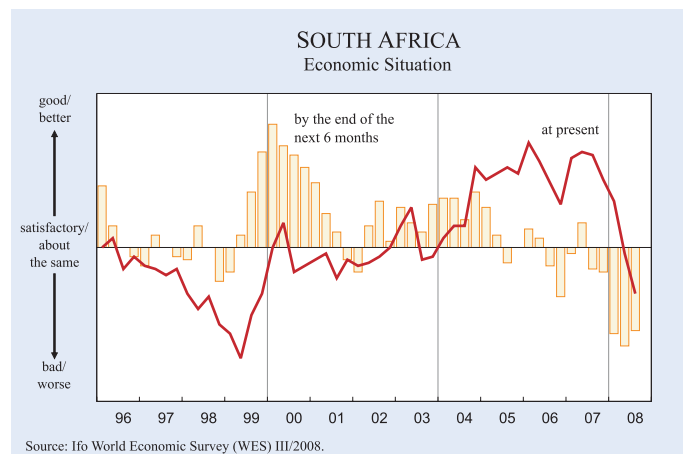
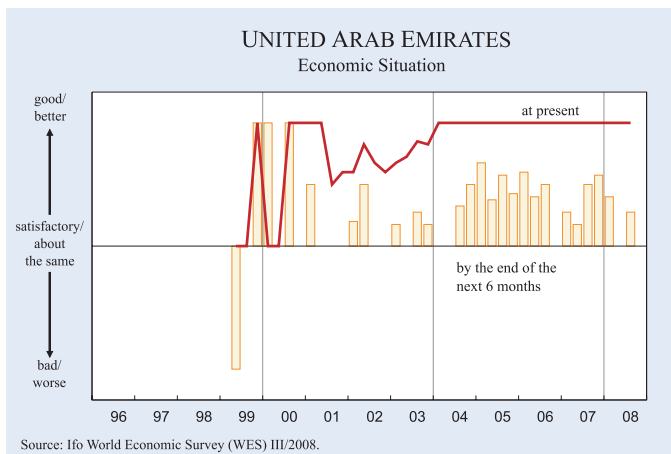
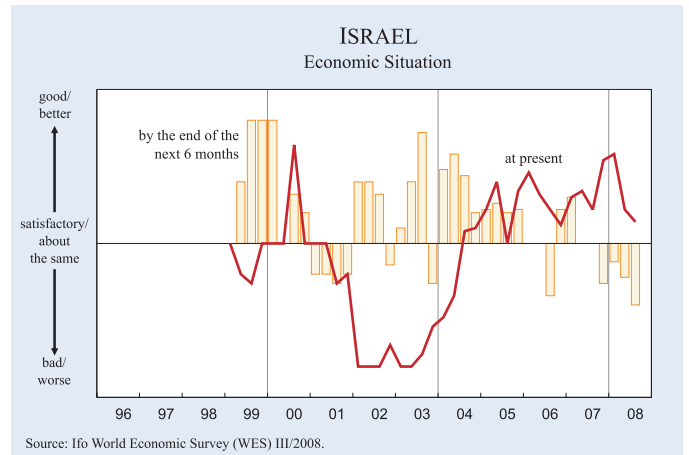
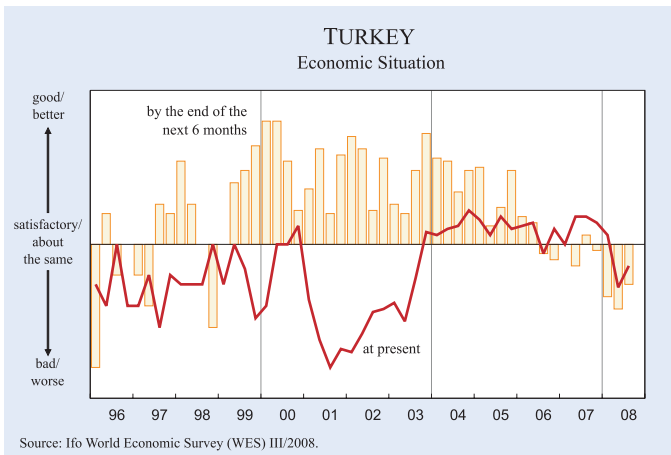
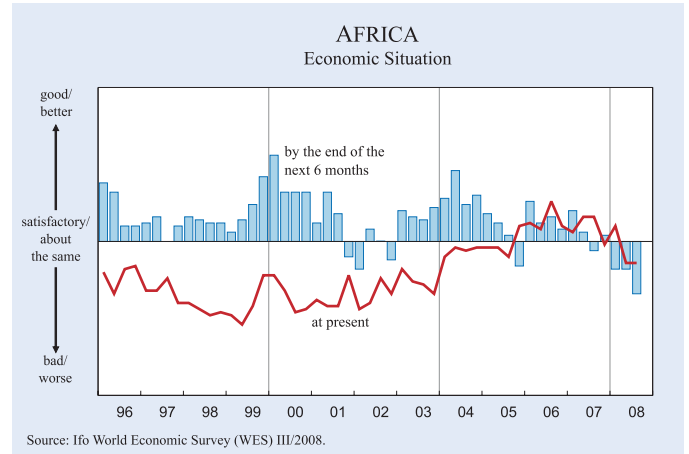
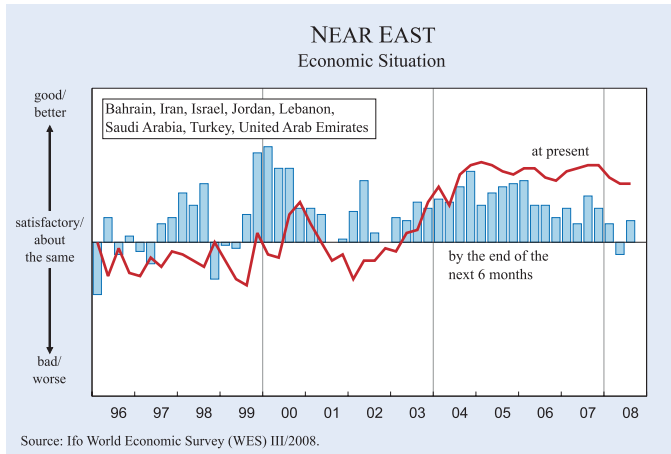


Figure 10

NEAR EAST AND AFRICA



than the rate reported for 2007 (4.4 percent) and that expected for 2008 in April (5.8 percent). The highest rate of inflation is expected again in *Latvia* (15.5 percent). Also in *Serbia* (12.5 percent), *Bulgaria* and *Lithuania*, inflation will remain relatively high (in each case 10.5 percent). Also in *Estonia* (8.9 percent) inflation expectations remain clearly above the average of the region. The relatively lowest inflation rates will prevail in 2008, according to WES experts, in *Slovakia* (3.9 percent) and *Poland* (4.5 percent).

In the *CIS* countries inflation rates in 2008 will be amongst the highest in the world. Inflation expectations shot up particularly in *Kyrgyzstan* (from 18.0 to 28.0 percent), in *Uzbekistan* from 12.0 to 18.0 percent and in the *Ukraine* from 15.5 to 20.0 percent. Not quite as dramatic was the upward correction of inflation expectations in *Russia* (from 11.5 to 13.5 percent) and in *Kazakhstan* (from 11.0 to 14.0 percent).

Also in *Latin America* 2008 inflation expectations continue to be on the rise (from 7.9 in April to now 9.7 percent). The upward revision of inflation expectations was widespread but particularly pronounced in *Ecuador* (from 6.0 to 10.5 percent), in *Guatemala* (from 8.5 to 11.5 percent), in *Paraguay* (from 8.3 to 11.0 percent) and last but not least in *Venezuela* (from 27.0 to 32.0 percent). In *Brazil* inflation expectations increased from 4.8 in April to now 6.7 percent and in *Mexico* from 4.4 to now 5.9 percent. In *Argentina* the inflation outlook for 2008 remained very bleak but at least did not deteriorate further (22.5 after 24.5 percent in April).

In the *Near East* the inflation outlook for 2008 worsened from an expected 9.3 in April to now 10.5 percent. The only exception in the region where inflation expectations came down somewhat was *Saudi Arabia* (from 7.6 to 6.0 percent). By far the strongest increase in 2008 inflation is expected in *Iran* (26.5 after expected 18.0 percent in April). The relatively lowest inflation rate in the region still prevails in *Israel* despite a significant upward revision (3.9 after 2.7 percent in April).

In *Oceania* inflation expectations for 2008, which had been stable in the spring survey, were now revised upwards to 3.9 percent both in *Australia* and in *New Zealand*.

In *Africa* an overall average continues to make no sense due to the even growing hyperinflation in *Zimbabwe*. But also in most other countries covered in the region, inflation expectations were revised further upwards: in *Tunisia* from 5.3 to 10.0 percent, in *South Africa* from 9.0 to 11.3 percent and in *Nigeria* from 8.6 to 10.0 percent. The relatively lowest inflation amongst the *African* countries is expected in 2008 in *Morocco* with 3.0 percent.

Euro seen as clearly overvalued

A growing majority of WES experts regard the *euro* as overvalued. On the other hand the *US dollar* continues to be seen by the majority of respondents to be undervalued. The *British pound* and the *Japanese yen* are – according to WES experts – not far away from their fair value.

The supplementary survey question on the likely development of the *US dollar* in the next six months, regardless of how currencies have been assessed from a fundamental point of view, brought some surprise. For the first time in many months, a moderate upward trend of the value of the *US dollar* is expected in the course of the next six months. A strengthening of the *US dollar* is expected particularly in *Western Europe*, *Latin America* (with the exception of *Peru*) and *Africa*. However, in *CIS* countries the *US dollar* will continue to lose in

Figure 11

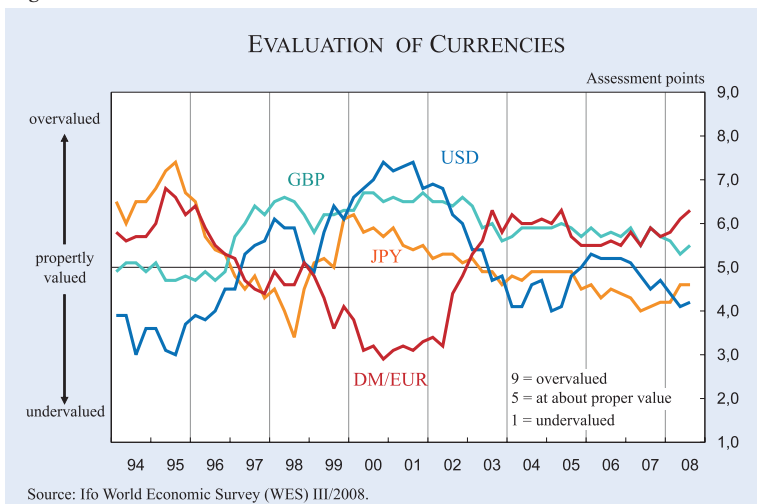
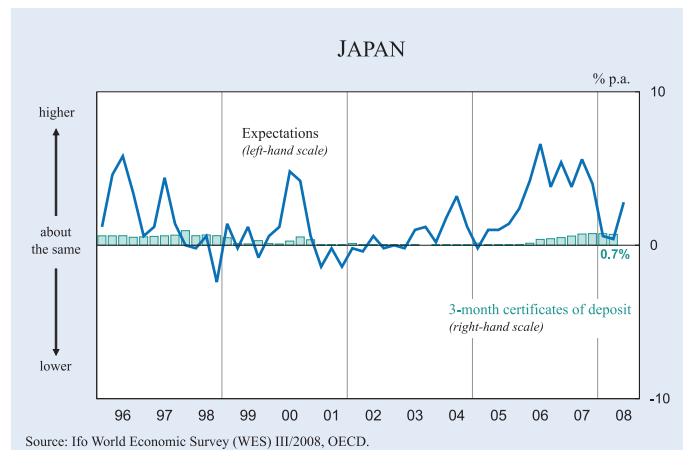
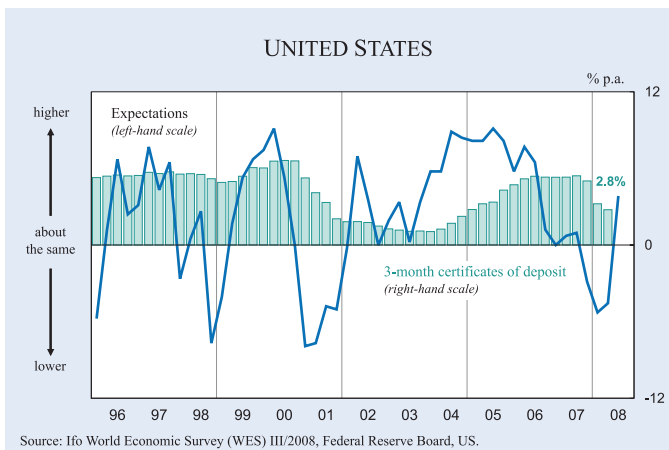
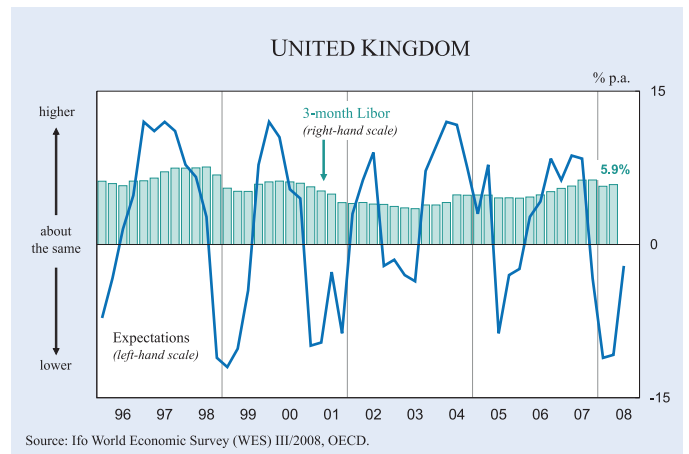
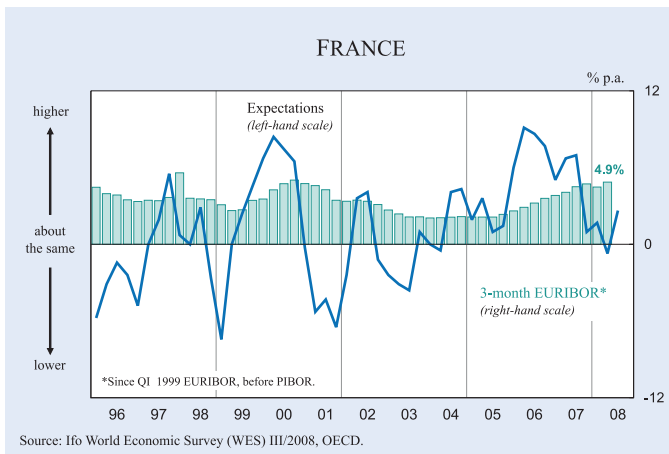
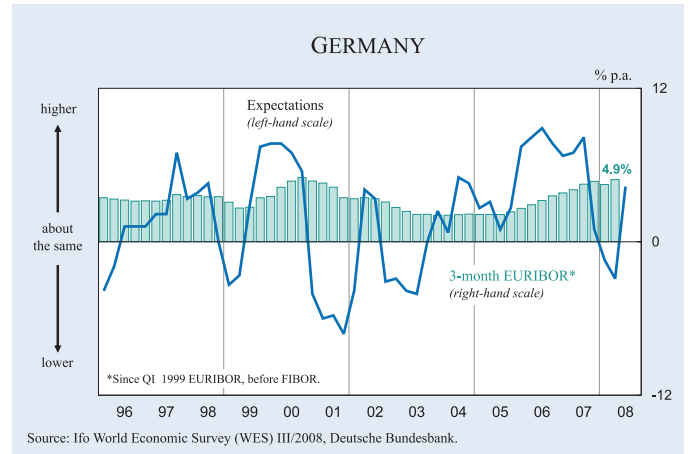
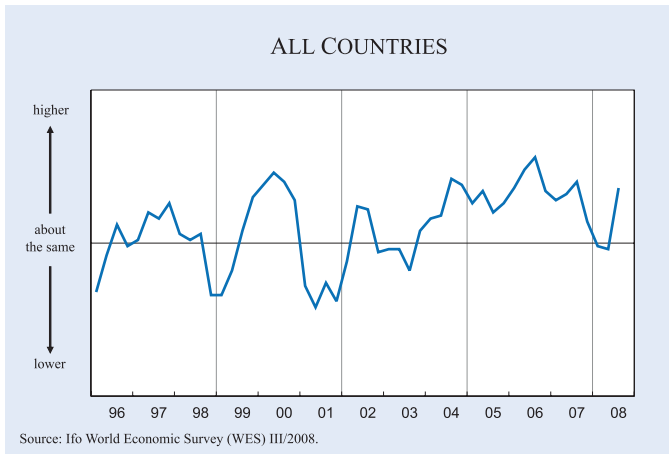


Figure 12

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



value in the coming six months, according to WES experts. In *Eastern Europe, Oceania, the Near East* and also *Canada* the *US dollar* parity will remain almost unchanged.

Interest rates: Hikes expected as a consequence of worsened inflation outlook

In contrast to the spring survey, there is now a clear majority of WES respondents that expect rising interest rates in the course of the next six months despite the expected weakening of the real economy. The main reason for this lies probably in the fear of further rising inflation expectations which may lead central banks almost worldwide to hike interest rates despite the growing slack in most economies.

To what extent the decline of oil prices and other raw material prices which set in early August and was not covered by the July WES survey gives room for a more accommodating monetary policy remains to be seen.

Roughly the same picture as in the world-wide average also characterises the *euro area*: expected increase of short-term interest rates and to a lesser degree also of long-term interest rates. In *Western Europe* outside the *euro area* a further decline of short-term interest rates is expected only in the *United Kingdom*.

In the rest of the world declining interest rates in the course of the next six months are only expected by WES experts in *New Zealand*.

ICC Special Question: Energy prices

Oil prices started climbing in 2003 with the beginning of the Iraq war. In 2006 and 2007 the world economy had expanded at its fastest pace in decades, resulting in substantial increases in the demand for oil, while the oil production grew sluggishly, compounded by production shortfalls in oil-exporting countries. As a result of the imbalance and low price elasticity, very large price increases occurred particularly in 2007 and 2008. In July 2008 oil prices hovered above US\$130 a barrel (see Figure 13).

This quarter's ICC special question dealt with the impact of rising oil prices on the global economy and the ability of companies and countries to meet their energy needs.

The vast majority of surveyed economists worldwide stated that oil prices over \$130 will negatively affect company earnings in their country. On the other hand, in *Western European* countries, *North America, Australia*, and also in several *Central- and Latin America* countries (*Brazil, Chile, Costa-Rica* and *Peru*) and *Asian* countries (*Japan, South Korea, China, Taiwan, Thailand* and the *Philippines*) rising oil prices will encourage companies to invest in cleaner and more efficient technologies, according to the surveyed economists.

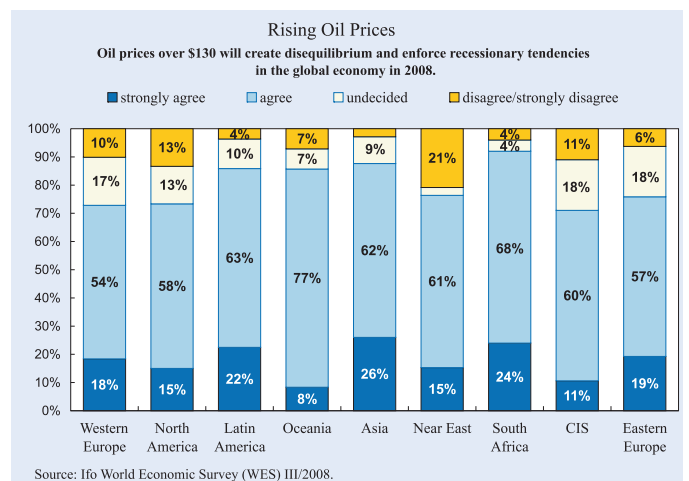
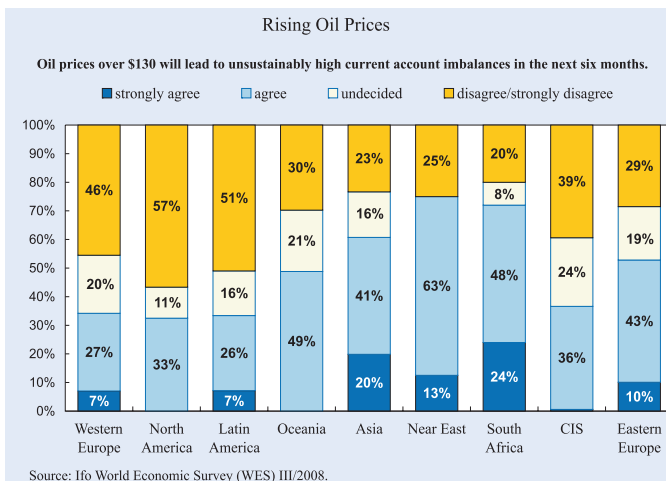
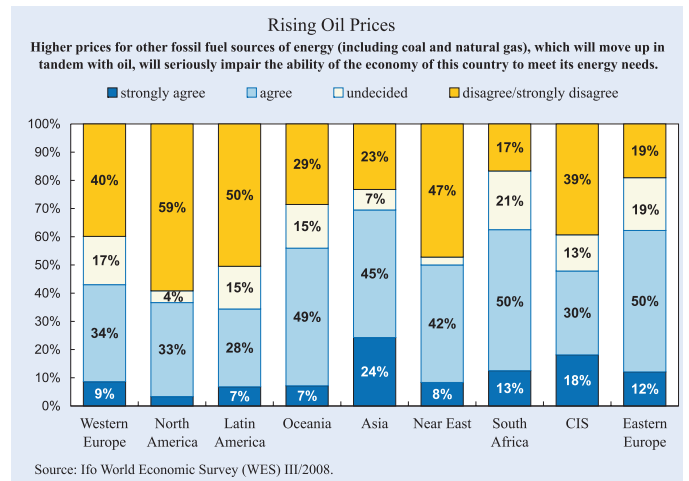
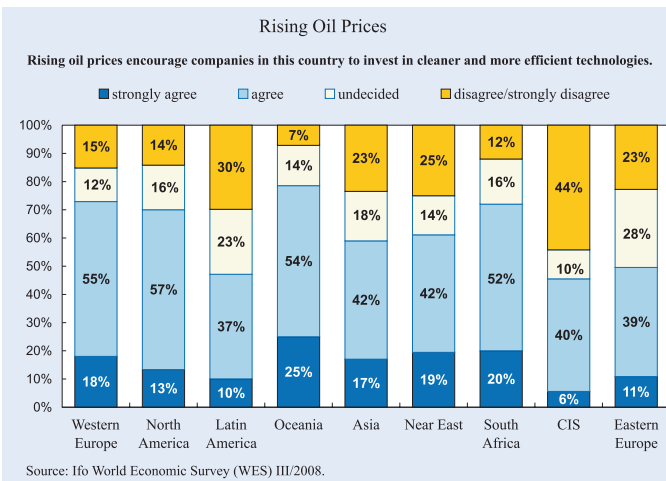
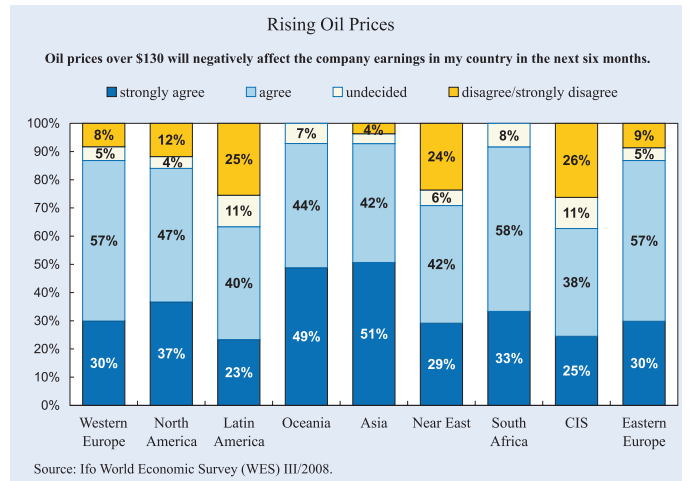
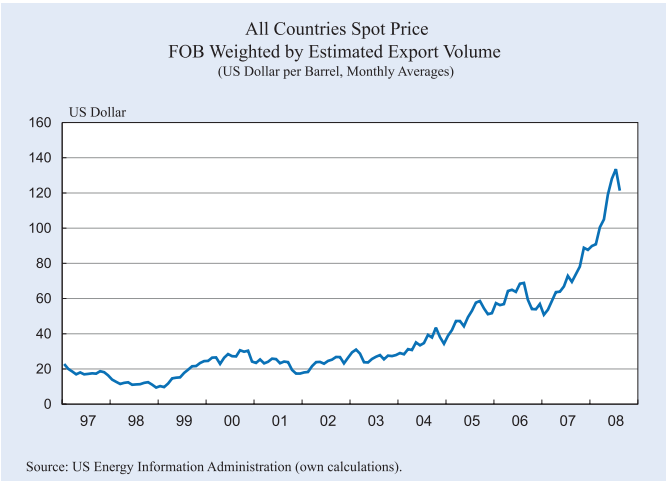
Higher prices for other fossil fuel sources of energy (including coal and natural gas), which will move up in tandem with oil, will seriously impair the ability of many economies to meet their energy needs, according to WES experts. The proportion of economists who see this risk for their country is particularly high in *Asia* (*Japan, South Korea, Taiwan, Indonesia, Thailand, India, Bangladesh* and *Pakistan*), in *Turkey, South Africa* and *Israel*, and also in many *Western European* (*Spain, Italy, Portugal, Greece* and *Ireland*) and *Eastern European* countries (*Latvia, Serbia-Montenegro, Slovakia, Lithuania, Hungary* and *Romania*).

According to WES experts, oil prices above \$130 will lead to unsustainably high current account imbalances in the next six months in many *Asian* countries (*Bangladesh, Pakistan, South Korea, India, Thailand* and *Taiwan*), in *South Africa, Israel* and *Turkey*, as well as in several *European* countries (*Portugal, Greece, Spain, Latvia, Romania, Bulgaria, Serbia-Montenegro* and *Croatia*).

The vast majority of surveyed economists think that oil prices above \$130 will create disequilibrium and enforce recessionary tendencies in the global economy in 2008.

Figure 13

OIL PRICES



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