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World Economic Climate deteriorates

Economic expectations further downgraded but still positive

Inflation pressure remains high despite some softening

Yen and euro are seen as somewhat overvalued

Fewer WES experts expect further increase of short- and long-term interest rates

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Ifo World Economic Survey

Regions

- World Economy: Global upswing is faltering
- Western Europe: Economic climate clouded
- North America: Economic climate deteriorates further
- Eastern Europe: Further improvement of present economic situation
- CIS: Less positive expectations
- Asia: Some economic cooling
- Oceania: Economic expectations upgraded
- Latin America: Unchanged economic climate
- Near East: Economic climate indicator declines somewhat
- Africa: No unified economic trend

The survey is jointly conducted by the Ifo Institute and the Paris-based International Chamber of Commerce (ICC).
Notes

The World Economic Survey (WES) assesses worldwide economic trends by polling transnational as well as national organisations 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 2011, 1,080 economic experts in 117 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 organisations are published.
The Ifo World Economic Climate clouded over in the third quarter (see Figure 1). With this drop the indicator lost all the gains of the first two quarters of this year and now stands at 97.7, after 107.7 in April. The worsening affected both the appraisals of the current situation as well as the expectations for the coming six months (see Figure 2). However, despite the weakening, both components are still in positive territory. The global economic upswing is faltering. This is also illustrated by the business-cycle clock (see Box 1).

Global upswing is faltering

The deterioration results from slowing in various regions. Especially in North America, in Asia and in Western Europe the economic climate has worsened (see Figure 3). Despite the common weakening, these developments have to be classified quite differently. In Asia – apart from a special development in Japan – the economic climate clouded probably because most of the Asian economies are seeking to moderate the growth pace somewhat to reduce inflationary pressure and to reduce the risk of overheating. Hence this slowing might be necessary to avoid crises later and to arrive at a more sustainable growth path. In particular in India, China and Indonesia, the WES experts assess the current situation and the further development more reservedly than so far. Nevertheless, the economic climate indicator for Asia is still slightly above its long-term average, showing that Asia despite the deceleration is still in a lively upswing. The situation in North America is quite different. The US economy is still fragile.

The recovery is weak and by far not strong enough to lead to a substantial improvement in the labour market. According to official data, GDP per capita stagnated in the first half of this year. The survey respondents evaluate the current situation – possibly also in view of debt problems – more unfavourably. Beyond that their expectations regarding the development in the near future are more sceptical than earlier this year. In Western Europe the climate has also worsened. The development within this area is uneven, though. The climate clouded partly because the hitherto strong upswings in Germany, Sweden and Switzerland are losing some momentum, partly
According to the July survey the Ifo indicator for the world economic climate clearly declined. The deterioration of the climate results equally from less positive assessments of the present situation and of less positive economic expectations. The new value of the indicator is still positioned in the “consolidated upturn” quadrant, though closer to the center. This shows that the economic upswing is losing momentum.

The crucial question is in which direction the indicator will move in coming quarters. One scenario could be a development similar to the development in 2004/2006 (see small Figure): Here the climate indicator declined in 2004, as it has now, showed a sideward movement in most parts of 2005 towards the center of the diagram and started to rise again at the end of 2005 and early 2006. Thus, the development in 2005 was a pause and not the end of the upswing. Translated into the actual situation: The most recent development of the softening of the indicator could signal only a break but not the end of the upswing in the world economy. Of course this is only one amongst many other possibilities. A more negative scenario would be a drop of the climate indicator in one of the next survey rounds into the “downswing quadrant” or – even worse – a move directly from the “boom” into the “recession quadrant”, something which however has never before happened in the 30 years of the existence of WES.

The Ifo World Economic Climate is the arithmetic mean of the assessments of the present situation and economic expectations. The new value of the indicator is still positioned from less positive assessments of the present situation.

The economic climate indicator for Western Europe deteriorated for the first time since early 2009 (see Figure 3). Both the present economic situation but mainly the economic expectations for the next six months have been downgraded considerably (see Figure 4). The same pattern applies to

the euro area (see Box 2). While the economic climate indicator of the euro area still lies marginally above its long-term average, the indicator for all of Western Europe has already dipped somewhat below.

Box 1

**Ifo Economic Clock and the Ifo 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 six years can be helpful. The business cycle typically proceeds clockwise in a circular fashion with the expectations leading assessments of the present situation.

The economic upswing is losing momentum because of the problems especially in Italy and Portugal. Also the climate in the United Kingdom worsened. Britain’s GDP figures in the second quarter showed that the economy has grown only very slightly. The WES experts also assess the situation in the third quarter less favourably and their expectations regarding the coming half year are more cautious than in April. So also the recovery in the UK seems to be fragile. In contrast to this, for example, the economic climate in France improved.

Overall, at the moment there are some regions and countries where a strong upswing is slowing somewhat and, on the other hand, there are some countries where the recovery process is uneven. This contributes at the moment to a slowdown of the global economic upswing. Recent official inflation figures in some countries were a little bit lower than before – for example in the US, in the United Kingdom and in the euro zone as a whole – but underlying inflationary pressure remains elevated in most countries. The WES experts expect a world-wide average inflation of 4.0% this year compared to a rise of 3.8% anticipated in the previous quarter. However, the recent strong falls of oil and commodity prices are not included in the survey.

**Western Europe:**

**Economic climate clouded**

The economic climate indicator for Western Europe deteriorated for the first time since early 2009 (see Figure 3). Both the present economic situation but mainly the economic expectations for the next six months have been downgraded considerably (see Figure 4). The same pattern applies to
According to the latest WES results, the current economic situation is judged as good in Germany, Austria, Estonia and Finland (see Figures 5a and 5b). While the assessments in Austria and Estonia have been upgraded over the previous survey, they remain unchanged in Finland and deteriorated marginally in Germany. The economic expectations for the next six months have been downgraded considerably in the WES experts. In Cyprus and Italy no further improvement is expected in the next half year. The economic expectations in the United Kingdom have been downgraded considerably in comparison to the survey in April. However, they remain positive and some strengthening of the export sector in the second half of the year is expected. The situation for the remaining countries of the euro zone – Greece,
Ireland, Portugal and Spain – has hardly changed. The WES experts continue to assess the present situation as very poor. Greece and Portugal even received the lowest mark on the WES scale. For the next six months the surveyed economic experts in Portugal remain very pessimistic and the Greece experts are cautious regarding the economic development. In both countries private consumption and additional capital expenditures are expected to remain subdued. In contrast, the economic expectations in Spain and Ireland are somewhat more positive, even to a higher degree than in the previous survey. In Ireland, Greece and Portugal the WES experts expect a rebound in the export sector.

Outside the euro area, a favourable present economic situation prevails in Norway, Sweden, Switzerland and Monaco. The economic outlook for the next six months remains fairly confident in Norway and Monaco. In contrast, the economic expectations in Switzerland and Sweden have been downgraded considerably over the previous survey and WES experts are now cautious in Sweden and rather pessimistic in Switzerland regarding future economic development. In Denmark, the assessments of the present economic situation have been downgraded and are now seen as unfavourable. However, for the coming six months some improvement with a strengthening of the export sector is anticipated. In Iceland, WES experts assess the present economic situation as still weak. For the coming six months they see no room for improvement.

North America: Economic climate deteriorates further

The economic climate indicator in North America declined further and slipped below its long-term average of 92.2 in the period 1995–2010 (see Figure 3). The assessments of both the present situation and the economic expectations have been downgraded, with the current economic situation even substantially clouded (see Figure 4). This is especially true for the United States. The present economic situation is now rated as weak according to the WES experts. Also the

Box 2
World Economic Survey (WES) and GDP Growth in the Euro Area

The Ifo World Economic Climate for the 17 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 274 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 indicator for the economic climate in the euro area has fallen in the third quarter for the first time since the beginning of 2009 and now stands only slightly above its long-term average. The assessments of the current situation are somewhat less positive compared to the second quarter of 2011. Above all the expectations for the coming six months weakened noticeably. Economic activity in the euro area is entering a difficult phase.

The current economic situation continues to be assessed as “excellent” in Germany, as “good” in Austria, Finland and Estonia and as “favourable” in Belgium. In France, the Netherlands and in Slovakia, the current economic situation has been assessed as “satisfactory” by the WES experts. The general economic situation has worsened all in Cyprus. Here, as in Italy, it is appraised as “unfavourable”. In Ireland, Spain and Portugal, the economic experts have given the present economic situation even worse than in the previous quarter, i.e. it is very weak. Again, Greece received the worst appraisals on the WES scale. The expectations for the coming six months in the euro area are considerably less confident over the previous survey. In many countries a worsening of the economic situation is expected. In contrast, the expectations in Spain, Ireland and France are increasingly pointing upwards. In the Eastern European euro member states (Estonia, Slovakia and Slovenia) the outlook remains confident.

ECONOMIC GROWTH AND IFO ECONOMIC CLIMATE FOR THE EURO AREA

*Arithmetic mean of judgement of the present and expected economic situation.
Figure 4

Selected Regions

North America
Economic Situation

Western Europe
Economic Situation


Eastern Europe
Economic Situation

CIS
Economic Situation


Latin America
Economic Situation

Asia
Economic Situation

expectations have been downgraded somewhat, but remain in positive territory (see Figure 6). The uncertainty regarding the settlement of the debt dispute in the end of July one week before the poll ended, led to a slight stronger downgrade of the economic expectations. In Canada both the present situation and the economic expectations have been downgraded somewhat, but still remain at a favourable level.

**Eastern Europe: Further improvement of present economic situation**

The economic climate indicator in Eastern Europe deteriorated again after the strong rise in the second quarter this year, due to considerably less positive expectations. In contrast, the present economic situation improved somewhat over the previous survey and is still regarded as satisfactory (see Figures 4 and 7).

The WES experts in the Czech Republic, Poland and Lithuania rated the current economic situation as favourable. In Lithuania the economic expectations for the next six months have been upgraded considerably and are now regarded as highly optimistic by the surveyed experts. Capital expenditures, private consumption and the export sector are expected to strengthen further in the next half of the year. In contrast, the economic outlook for Poland and the Czech Republic has been downgraded remarkably over the previous survey but still remains in positive territory. In Latvia the assessments of the present economic situation have been upgraded somewhat and are now seen as “satisfactory”. For the coming six months no major changes are anticipated. In Bulgaria, Hungary and Romania the present situation is regarded as unfavourable, but at least the outlook for the coming six months remains in positive territory in all these countries. In Bulgaria, also the export sector is expected to strengthen further according to the surveyed economic experts.

The economic situation in the region outside the EU is assessed as unfavourable in Albania and as still very weak in Croatia and Serbia. However, for the next six months some improvement is expected in all these countries, especially in Croatia, where a strengthening of capital expenditures, private consumption and the export sector is anticipated.

**CIS: Less positive expectations**

The economic climate indicator for CIS countries covered by WES (Russia, Ukraine, Kazakhstan and Kyrgyzstan) deteriorated somewhat. While the present situation improved marginally, retaining its satisfactory level, the economic expectations for the next six months deteriorated, but still remain in positive territory (see Figure 6).

This pattern applies particularly to Russia. The assessments of the present economic situation improved somewhat and have now reached a favourable level. The expectations for the next six months remain positive, although to a lesser degree than in the previous survey (see Figure 6). In Kazakhstan both the present economic situation and the economic expectations improved somewhat over the previous survey and remain on a favourable level. In contrast, in Kyrgyzstan the economic performance seems unimproved and macroeconomic development is expected to remain subdued in the coming months, according to the WES experts. In the Ukraine, the present economic situation improved somewhat, but is still regarded as unfavourable by the surveyed economic experts. However, for the next six months some further improvement is expected.

**Asia: Some economic cooling**

The economic climate indicator in Asia dropped further, but at 94.7 still stands above its long-term average (1995–2010: 90.7). Both the present economic situation and the economic expectations have been similarly downgraded and are pointing to some economic cooling (see Figures 3, 4 and 8).

In Hong Kong, Singapore and Sri Lanka the current economic situation was assessed as particularly favourable. However, the economic expectations have been considerably downgraded over the previous survey, but they remain positive in Singapore and Sri Lanka. In contrast, WES experts in Hong Kong have a more cautious view on the future economic development for the next six months. In the Philippines, Malaysia, South Korea, India, Indonesia and Taiwan, the current economic situation was rated as good by the surveyed economic experts, although in India and Indonesia to a considerably lesser degree than in the previous survey. The economic outlook for the next six months remains positive – despite remarkable
downwards revisions – in all these countries, with the exception of Malaysia, where WES experts have a more cautious view on future economic performance for the next half of the year. The export sector is foreseen to pick up further in India, Indonesia and South Korea. In Bangladesh, China and Thailand the current economic situation has been assessed as satisfactory, although to a lesser degree than earlier this year. The economic expectations in Bangladesh and Thailand have been revised considerably upwards and are now more confident than in the second quarter. In contrast the Chinese WES experts retain their caution regarding the development in the second half of the year. In Vietnam, the situation has not changed. The current economic situation is still regarded as unfavourable and will remain so in the coming six months, according to the WES experts. Japan is still struggling with the aftermath of the earthquake and tsunami. The present situation was assessed as unimproved. Nevertheless, the economic expectations have been revised considerably upwards and are now rather optimistic. Capital expenditures, private consumption and the export sector are expected to rebound in the second half of the year. In Pakistan the present situation is still assessed as very poor, despite some improvement over the previous survey. For the coming six months WES experts see no room for improvement.

**Oceania: Economic expectations upgraded**

Oceania is the only region in which the expectations – compared to the previous quarter – have become more positive. However, the economic climate indicator deteriorated somewhat due to the remarkable downgrade of the present economic situation. This is especially true for Australia (see Figure 6). The current economic situation has been revised considerably downwards, but still remains on a favourable level. The economic outlook continues to be positive – even to a higher degree than earlier this year. In New Zealand the WES experts still assess the present economic situation as unfavourable. However, for the second half of the year the surveyed economic experts are fairly confident and expect mainly capital expenditures and the export sector to strengthen strongly.

**Latin America: Unchanged economic climate**

In Latin America the economic climate indicator has not changed. Both the assessments of the present situation, as well as the economic expectations remain at the same favourable level as in the previous survey (see Figures 4 and 9).

In Argentina, Chile, Paraguay, Peru and Uruguay a highly favourable present economic situation prevails. The economic expectations have been revised downwards in all these countries with the exception of Uruguay. However, the economic outlook in Chile, Paraguay and Uruguay remains positive. In contrast, WES experts in Peru and Argentina have a more cautious view on future economic performance. The surveyed economic experts in Brazil and Colombia continue to assess a favourable present economic situation, including a strong private consumption. The economic expectations for the next six months in Colombia have been upgraded considerably and are now optimistic. In Brazil, the economic expectations continue to point to an economic stabilization at current levels. In Mexico, Costa Rica, the Dominican Republic, Ecuador and Panama, the surveyed experts rate the economic situation again as “satisfactory”. While in nearly all these countries the assessments of the present situation remained unchanged, the situation deteriorated slightly in Mexico, probably due to its strong link to the United States. The outlook for the coming six months remains positive in all these countries – in the Dominican Republic, Ecuador and Panama even to a higher degree than in the second quarter. The current economic situation in El Salvador, Bolivia and Guatemala is regarded as unfavourable by WES experts. The economic performance in the next half year is expected to remain about the same in Bolivia and Guatemala. Only WES experts in El Salvador expect some improvement in coming months. In Cuba, Trinidad and Tobago and Venezuela the present economic situation is assessed as very weak. For the next six months, some improvement is expected in Venezuela and Trinidad and Tobago. In contrast WES experts in Cuba don’t anticipate any substantial changes of the economic situation.

**Near East: Economic climate indicator declines somewhat**

The economic climate indicator in the Near East deteriorated again after its strong rise and reaching its highest peak ever in April 2011. Both the current situation as well as the six-month outlook deteriorated markedly (see Figure 10). However, a
favourable economic climate still prevails. In Israel and Saudi Arabia a highly favourable and in Turkey at least a favourable present economic situation predominates. The expectations for the coming six months in all these countries are positive, in Saudi Arabia even fairly confident. In Bahrain, Kuwait, Lebanon and the United Arab Emirates the current economic situation has been assessed as satisfactory by the surveyed economic experts. The economic outlook for the next six months continues to be fairly confident in all these countries. In Iran a weak economic performance has been observed. Within the next six months WES experts don’t assume any substantial improvement regarding the economic performance.

**Africa: No unified economic trend**

The countries of the African region display a very differing pattern concerning the economic climate. Thus, an aggregated climate index for the countries surveyed by WES on this continent still makes little sense, and the following analysis will focus on particular economic trends in individual countries of Northern and Sub-Saharan Africa.

The current economic situation in the Northern African countries Egypt and Tunisia is still assessed as poor. In Egypt the economic outlook has been revised downwards and WES experts don’t expect major changes of the economic situation in the coming six months. In contrast, the economic expectations in Tunisia have been considerably upgraded and are now optimistic. In Morocco some improvement regarding the present economic situation has been observed and it is now regarded as satisfactory. For the next six months, however, WES experts expect some weakening of the overall economy as well as of private consumption. In Algeria, WES experts continue to assess the current economic situation as favourable. The economic forecasts for the next six months have been downgraded somewhat, but still remain positive. Mainly the export sector is expected to strengthen somewhat.

The economic climate in South Africa cooled somewhat. Both the assessments of the present economic situation and the economic expectations have been downgraded considerably (see Figure 10). The present situation is now regarded as satisfactory and the economic outlook for the second half of the year remains positive, despite of the downwards revisions. In Chad, Rwanda and Zambia the present economic situation is assessed as very good. While in Rwanda the assessments remain unchanged over the previous survey, they have been downgraded somewhat in Zambia. In all these countries the outlook for the coming six months remains positive, and in Rwanda it is even optimistic. Especially the export sector in Rwanda and Zambia is foreseen to strengthen strongly.

In Congo Dem. Republic, Congo-Brazzaville, Mauritius, Niger and Sierra Leone the economic situation is regarded as favourable according to the WES experts. The economic outlook for the next half year has been upgraded considerably in Sierra Leone and Niger and is now even optimistic. In both countries further strengthening mainly of private consumption and the export sector is expected in the coming six months. In Mauritius and Congo-Brazzaville the economic expectations remain in positive territory, despite some downwards revisions in Congo-Brazzaville. Also in Congo Dem. Republic the economic expectations deteriorated considerably and are now rather pessimistic.

In Burundi, Gabon, Liberia, Malawi, Namibia, Nigeria, Senegal, Tanzania and Uganda WES experts rated the present economic situation as “satisfactory”. In nearly all countries it is expected that the economic situation will remain about the same in the next six months. In Namibia and Nigeria, the surveyed economic experts are even more confident regarding future development. Only in Uganda does the economic outlook for the second half of the year remain pessimistic, according to the WES experts.

The present situation in Benin, Kenya, Lesotho and Sudan is now assessed as unfavourable, due to considerable downwards revision in all countries with the exception of Sudan. There, already in the previous survey uncertainty prevailed because WES experts still awaited the official secession, which took effect on 9 July 2011. For the next six months the surveyed economic experts, who are all located in the north of Sudan, remain pessimistic regarding future economic development as it is not clear how the secession will affect both countries — Sudan and the newly founded South Sudan. In Lesotho no further improvement of the economic situation is expected within the next six months. In Kenya, the economic expectations are even pessimistic, according to the surveyed economic experts. Only in Benin
Figure 5a

**European Union**

**EUROPEAN UNION (15)**

Economic Situation

- Good/better
- Satisfactory/about the same
- Bad/worse

by the end of the next 6 months
at present


**FRANCE**

Economic Situation

- Good/better
- Satisfactory/about the same
- Bad/worse

by the end of the next 6 months
at present


**GERMANY**

Economic Situation

- Good/better
- Satisfactory/about the same
- Bad/worse

by the end of the next 6 months
at present


**ITALY**

Economic Situation

- Good/better
- Satisfactory/about the same
- Bad/worse

by the end of the next 6 months
at present


**SPAIN**

Economic Situation

- Good/better
- Satisfactory/about the same
- Bad/worse

by the end of the next 6 months
at present


**UNITED KINGDOM**

Economic Situation

- Good/better
- Satisfactory/about the same
- Bad/worse

by the end of the next 6 months
at present

Figure 5b

**EUROPEAN UNION**

![Graphs showing economic situation in Austria, Denmark, Finland, Netherlands, Portugal, and Sweden](image)

Figure 6

**NORTH AMERICA, OCEANIA AND CIS**

Figure 7

**EASTERN EUROPE**

**CZECH REPUBLIC**
Economic Situation

**ESTONIA**
Economic Situation

**HUNGARY**
Economic Situation

**POLAND**
Economic Situation

**SLOVAK REPUBLIC**
Economic Situation

**SLOVENIA**
Economic Situation

Figure 9

LATIN AMERICA

MEXICO
Economic Situation


ARGENTINA
Economic Situation


BRAZIL
Economic Situation


COLOMBIA
Economic Situation


PERU
Economic Situation


VENEZUELA
Economic Situation

Figure 10

NEAR EAST AND AFRICA

do the economic expectations for the second half of the year remain optimistic.

In Comoros, Mauritania and Zimbabwe the present economic situation has been assessed as weak and is expected to remain so in Mauritania. In contrast, in Comoros and Zimbabwe some improvement in the next six months is anticipated. The remaining Sub-Saharan countries Burkina Faso, Ivory Coast, Madagascar, Swaziland and Togo have been assessed by the surveyed economic experts with the lowest mark on the WES scale. The present situation is regarded as very poor. In the next six months in Madagascar and Togo no improvement of the economic performance is expected. The WES experts in Swaziland and Burkina Faso even forecast deterioration. At least in Ivory Coast a bettering of the economic situation in the next six months is anticipated.

**Inflation pressure remains high despite some softening**

**General trends**

On a world-wide average, WES experts forecast for 2011 an annual inflation rate of 4.0% compared with 3.8% in the April survey and 3.4% at the beginning of the year (see Table 1). Thus, the extent of upward revisions in inflation expectations is shrinking. The expected slowdown of the inflation trend is also signalled by the results of another survey question focussing on the expected tendency of consumer prices in the coming six months. Here a significant smaller percentage of WES experts than in the previous survey expect further price increases in the coming six months.

**Price trends by regions and countries**

On average for the euro area, the expected inflation rate will be 2.6% in 2011 which is again clearly above the medium-term inflation objective of the ECB. However, the results of the additional question on the inflation tendency in coming six months point to some deceleration of consumer price inflation. Within the euro area the lowest inflation rates in 2011 are expected in Slovenia (2.1%), France (2.2%), Ireland and the Netherlands (each 2.3%) as well as in Germany (2.4%). Above the average of the euro area lie the expected inflation rates particularly in Greece (3.4%) as well as in Portugal and in Finland (each 3.3%). In the case of Greece and Portugal the increase of taxes and charges as part of the fiscal consolidation programme will lead also in 2011 – as already in 2010 – to the expected still relatively high inflation rate. In Western Europe outside the euro area by far the lowest inflation rate (1.0% in 2011) is again expected in Switzerland, where a strong appreciation of the Swiss franc appears to counterbalance inflationary pressures coming from the outside, mainly from prices for raw materials (including oil) and agricultural products.

In Eastern Europe inflation expectations picked up only moderately in the course of the previous three months. In Serbia inflation expectations (9.6%) remain the highest in the region followed by Romania (5.3%). The lowest inflation in 2011 will prevail, according to the WES experts’ expectations, in the Czech Republic (2.1%) and in Croatia (2.5%).

In North America, the new inflation forecast both for the United States and Canada stands at 2.6% and is thus nearly unchanged over the forecast in the previous survey.

In Asia inflation expectations for 2011 continue their rise and have now reached 4.1% for 2011 after an expected 3.6% at the beginning of the year and 3.9% in the April survey. By far the highest inflation rates in the region prevail again in Vietnam (16.3%) and in Pakistan (14.9%). In China inflation expectations for 2011 picked up strongly from 4.9% to 5.5% despite a relatively restrictive monetary policy for more than a year. However, in the answers to the additional question on the expected price trend in the coming six months some success of the high interest rate policy of the Chinese Central Bank is becoming apparent: The percentage of WES experts in China expecting further price increases in the coming six months is clearly shrinking. In India the inflation outlook remained constant at 8.0% in 2011. The moderate inflation typical for Taiwan is expected to continue also in 2011 (2.0%). In Japan the deflationary process seems to be overcome but the expected price increase in 2011 is still negligible (0.4%).

In Oceania – both in Australia and New Zealand – inflation expectations for 2011 remained slightly above 3%.

In Latin America inflation expectations for 2011 declined somewhat from 7.9% to 7.4%. The coun-
### Table 1

**Inflation Rate Expectations for 2011**

(based on WES QIII/2011 and QII/2011)

<table>
<thead>
<tr>
<th>Region</th>
<th>QII/2011</th>
<th>QI/2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average of countries*</td>
<td>2.6</td>
<td>2.5</td>
</tr>
<tr>
<td>High-income countries</td>
<td>2.6</td>
<td>2.5</td>
</tr>
<tr>
<td>Lower-middle</td>
<td>2.6</td>
<td>2.5</td>
</tr>
<tr>
<td>Low-income countries</td>
<td>2.6</td>
<td>2.5</td>
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*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. – ( ) The data in brackets result from few responses. – *1 Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, United Kingdom. – *2 Czech Rep., Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovenia, Slovakia. – *3 Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, Netherlands, Portugal, Spain, Slovenia, Slovakia. Source: Ifo World Economic Survey (WES) III/2011 and II/2011.
tries with the worst inflation outlook are still Venezuela (29.3%) and Argentina (27.2%). The countries with below-average inflation in 2011 will again be Peru (3.1%), Colombia (3.6%), Chile (4.0%) and Mexico (4.3%). In Brazil, despite a restrictive monetary policy and an appreciation of the currency, inflation expectations remain high for 2011 (6.1%).

In CIS countries inflation expectations for 2011 stabilised at a high level of around 10%. The relatively best inflation performance is seen in 2011 by WES experts in Kazakhstan, though an expected rate of 8.7% is still far from satisfactory. However, compared with this figure the inflation outlook in Russia is somewhat (9.5%) and in Kyrgyzstan by far worse (15.7%).

In the Near East the inflation outlook for 2011 deteriorated from 4.3% to 6.4%. The worsening of the inflation outlook is mainly due to Saudi Arabia where the inflation forecast for 2011 increased from 3.9% in the April survey to now 6.3%. In the United Arab Emirates as well as in Israel inflation is expected to remain moderate in 2011 (3.0% and 3.2% respectively). In Turkey the expected price increase in 2011 at 7.1% is somewhat higher than the average of the region.

In Africa the expected inflation rate for 2011 has slowed down slightly since April (from 7.5% to 7.0%). However, price trends in Africa are still very heterogeneous. Relatively low inflation rates for 2011 are again expected in Niger (3.7%) and Benin (2.5%). In a medium inflation bracket lie Algeria (4.4%), Tunisia (4.8%), South Africa (5.5), Namibia (5.4%) and Swaziland (6.8%). High inflation rates of 10% or more will predominate in 2011 according to WES experts particularly in Kenya (15.3%), Nigeria (12.0%), Congo Dem. Rep. (16.1%), Sierra Leone (14.7%), Egypt (11.7%) and Sudan (19.2%).

Yen and euro are seen as somewhat overvalued

On a world-wide scale the exchange rates of two of the four currencies that constitute the Special Drawing Rights of the IMF – namely the US dollar and the UK pound – appear to be close to their fundamentally appropriate values. The other two lead currencies – the Japanese yen and the euro – are regarded by the majority of WES experts as overvalued (see Figure 11).
However, by countries there are big differences in currency evaluations: WES experts regard their own currency as generally overvalued in Switzerland, Indonesia, Egypt as well as in South Africa; on the other hand, experts assessed their own currencies as generally undervalued particularly again in China but also in Bangladesh as well as in the Philippines, in Russia, in Turkey, in Sierra Leone and also in Venezuela.

The answers to a supplementary survey question on the likely development of the US dollar in the next six months, regardless of how currencies are assessed from a fundamental point of view, signal on a worldwide average a decline in the value of the US dollar in the course of the coming six months. However, behind this average are diverging trends: An expected weakening of the US dollar is expected particularly in some Asian countries (particularly China, Singapore, Thailand and the Philippines), in Canada as well as in Russia. These results contrast with an expected increase of the value of the US dollar in Switzerland, Australia and New Zealand, in Japan, Vietnam and Bangladesh, in some Eastern European countries like Albania, Croatia and Lithuania, in the CIS countries Kyrgyzstan and the Ukraine, in most Near East countries as well as in most African countries including South Africa. In Western Europe as well as in Eastern Europe the value of the US dollar six months from now continues to be seen by the vast majority of WES experts as roughly unchanged or marginally lower.

Fewer WES experts expect further increase of short- and long-term interest rates

The number of WES experts expecting a tightening of monetary policy in the course of the next six months has decreased for the first time since the end of 2010 (see Figure 13). This result is in line with the expected slowdown of inflation in the course of coming six months and the softer patch of world economic development.

The softening of the upward trend affects both long-term and short-term interest rates on a world-wide average. However, particularly in Australia and in Canada as well as in the majority of Eastern European countries, the weaker upward trend is restricted to the short-term interest rates whereas the

### Table 3: Assessment of the Following Factors Influencing the Climate for Foreign Investors in the Next Six Months

<table>
<thead>
<tr>
<th>Climate due to</th>
<th>Change for the next six months*</th>
<th>Deterioration</th>
<th>Improvement</th>
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</thead>
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<tr>
<td>Legal/administrative restrictions to invest and/or to repatriate profits</td>
<td>Benin</td>
<td>Greece, Kenya, Romania, Saudi Arabia, Serbia, Sierra Leone</td>
<td></td>
</tr>
<tr>
<td>Political stability</td>
<td>Bulgaria, Congo Dem. Rep., El Salvador, Mexico, Paraguay, Serbia, Taiwan, Venezuela, Zimbabwe</td>
<td>Namibia, Nigeria, Saudi Arabia</td>
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</tr>
</tbody>
</table>

For the countries that are not mentioned in the table, no major changes relating to the climate for foreign investors are expected during the next six months. Only countries with more than four responses were included in the analysis.

Criteria for selection of countries:

- Deterioration: WES grade between 1.0 and 3.5
- Improvement: WES grade between 6.0 and 9.0

Box 3  
**Adjustment processes in the GIIPS countries**

Since the outbreak of the financial and economic crisis investors have been sceptical about the sustainability of the public finances of Greece, Ireland, Portugal, and – to a lesser extent – Spain and Italy (GIIPS). This loss of confidence of the financial markets is reflected in strongly increased risk premia of some of the government bonds since early 2010.

In addition to country-specific structural problems, the high levels of private and public debts result from massive capital inflows and low interest rates from the mid-1990s on that were due to an inappropriate risk assessment of investors. Consequently, in most of these countries a construction and consumption boom emerged that boosted wages and prices. This, in turn, undermined their competitiveness and led to considerable current account deficits.

In order for the GIIPS countries to be granted more favorable conditions when incurring new debts, the investors have to regain confidence. This is only possible if, in addition to fiscal consolidation, the GIIPS increase their price and cost competitiveness in order to improve their mid-term growth perspectives.

One indicator for the change in competitiveness is the relative consumer price inflation. Ireland succeeded in enhancing its competitive position within the euro area; it even experienced deflation from early 2009 on. Although it recently realised positive inflation rates again, they are still far below the euro area average (Figure 12, 1). Inflation rates in Greece, Italy, Portugal and Spain, however, are markedly above average. Yet, these are biased upwards because of the effects of indirect taxes and administered prices that have risen as a result of fiscal consolidation. Since these effects are temporary, the prospects for their price competitiveness are (at least slightly) more favourable.

Other competitiveness indicators are the nominal unit labour costs relative to the euro area average (Figure 12, 2). In contrast to Germany, where they have evolved similarly to the euro area since the onset of the financial crisis in mid-2008, they have fallen more strongly especially in Ireland, but also in Spain and Portugal, so that these countries have been able to improve their competitiveness. In Italy, however, unit labour costs are currently even higher than before the financial crisis. In Greece, they declined recently, although the data are seen to be quite volatile.

For analysing changes in the competitive situation of the GIIPS countries relative to their trading partners in the euro area, several relative cost and price indicators can be consulted. The real effective exchange rate on the basis of the GDP deflator (Figure 12, 3) has the advantage that it reflects the price dynamics of the domestic economy, excluding import price effects. It can be seen that Ireland has strongly depreciated in real terms and thus gained competitiveness since the beginning of the financial crisis. Spain also improved its competitiveness, while the Portuguese real terms of trade have remained broadly unchanged. The deterioration indicated for Greece is partly due to the tax effects mentioned above. But its real effective exchange rate on the basis of unit labour costs has also only stagnated in the same period. Thus, the Greek consolidation measures seem not to have affected the competitiveness of the private sector yet.

The different adjustment processes and changes in the competitiveness positions are reflected in the current account balances. While Italy has enlarged its current account deficit since 2008, Greece, Ireland, Portugal and Spain were able to reduce the deficits they had built up over the years – even though to different degrees (Figure 12, 4). Due to its flexible labour market, Ireland managed to strengthen its competitiveness to such an extent that in 2010 its current account deficit only amounted to 0.7% in relation to the gross domestic product. In Spain, the structural labour market reforms have also shown first effects. In Portugal, Greece and Italy, however, much greater efforts are required for the adjustment process to gain momentum. Greece, in particular, will not be able to service its foreign credits without a massive increase in competitiveness.

expected further rise of long-term interest rates remained unchanged or even increased slightly. In CIS countries as well as in most Latin American countries, the current upward trend of short- and long-term interest rates remained unchanged.

**ICC Special Question: How should the G20 prioritize selected policy issues during their next summit?**

This quarter’s ICC special question asked the surveyed economic experts to assign the priority that the G20 should give to selected policy issues during this year’s summit in Cannes, France. Among the selection, the topics “improving financial regulation” and “reforming the international monetary system” were identified as the most important through all surveyed countries and regions (see Figure 14). In Western Europe, North America, Latin America, Near East and Africa the issue “fighting unemployment by creating productive jobs” also received a high priority. For the surveyed economic experts in Asia and Oceania, “fighting protectionism and concluding the Doha Round trade negotiations” was considered as important, whereas in Africa it was: “the framework for encouraging direct investment across frontiers should be improved”. The WES experts in Eastern Europe, CIS and Africa also selected “strengthening international cooperation against corruption in business transactions” as an important issue for the G20.
However, within the regions, some more aspects were emphasized, depending on the countries. The WES experts in Serbia, Slovenia, India, the Philippines, Thailand, Saudi Arabia, Lesotho and Nigeria also considered promoting green growth as important (see Table 4). The economic experts in India, Pakistan, Thailand, Saudi Arabia and in some African countries (Kenya, Zimbabwe and Nigeria) in addition asserted that combating climate change should be prioritized by the G20. “Improving coordination to reduce large imbalances in countries’ external payments” is an important issue to be
Figure 13

**Actual short-term interest rates and expected trend for the next 6 months (quarterly data)**

**ALL COUNTRIES**

**GERMANY**

**FRANCE**

**UNITED KINGDOM**

**UNITED STATES**

**JAPAN**

*Source: Ifo World Economic Survey (WES) III/2011, OECD.*

Table 4

<table>
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<tr>
<th>Region</th>
<th>Policy Issues</th>
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<tr>
<td></td>
<td>Existing protectionism and countering the Doha Round trade negotiations</td>
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<tr>
<td></td>
<td>Promoting growth and convergence of economies, reducing poverty, and improving financial regulations</td>
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<td></td>
<td>Strengthening financial systems, reducing corruption in business transactions</td>
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<td></td>
<td>Promoting UN and UN-led efforts to combat climate change</td>
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<td></td>
<td>Improving price volatility in commodities</td>
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<td></td>
<td>Improving coordination to reduce large imbalances and avoid external imbalances</td>
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<tr>
<td></td>
<td>Fighting unemployment by creating productive jobs</td>
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<td>Improving the framework for ensuring direct investment across countries</td>
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solved by the G20, according to the WES experts in Romania, Chile, Israel and Sudan. According to the surveyed economic experts in Kazakhstan, Serbia, China, Pakistan, the Philippines, Israel, Saudi Arabia and several African countries (Kenya, Nigeria, Sudan and Zimbabwe), “reducing price volatility in commodities” should receive a high priority.

In summary, among the ten stated policy issues, the vast majority of the surveyed WES experts in all countries and regions gave priority to the issues “improving financial regulation”, “reforming the international monetary system” and “fighting unemployment”. Among other policy issues, which the surveyed WES experts specified themselves, several economic experts asserted that solving the debt problem and the euro crisis should receive priority by the G20.

\[\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|}
\hline
\textbf{What priority should the G20 give to the following policy issues? – Aggregated to regions*} & World & Western Europe & North America & Latin America & Oceania & Asia & Near East & Africa & Eastern Europe & CIS \\
\hline
Fighting protectionism and concluding the Doha Round trade negotiations & 5.5 & 5.5 & 5.0 & 5.4 & 6.4 & 5.8 & 6.0 & 5.3 & 4.7 & 4.2 \\
Reforming the international monetary system & 6.1 & 6.2 & 5.3 & 6.3 & 6.2 & 6.0 & 6.9 & 4.6 & 6.5 & 7.3 \\
Improving financial regulation & 6.6 & 7.0 & 6.4 & 7.2 & 6.9 & 6.0 & 7.0 & 6.3 & 6.6 & 7.9 \\
Promoting green growth & 4.7 & 4.5 & 3.8 & 5.2 & 4.8 & 5.3 & 5.7 & 4.7 & 4.1 & 4.3 \\
Pushing ahead with UN-led efforts to combat climate change & 4.7 & 4.7 & 4.1 & 5.6 & 4.3 & 5.1 & 5.5 & 4.8 & 3.8 & 3.8 \\
Strengthening international cooperation against corruption in business transactions & 5.1 & 4.8 & 4.7 & 5.6 & 5.0 & 5.0 & 6.4 & 6.8 & 6.2 & 5.8 \\
Reducing price volatility in commodities & 4.7 & 4.6 & 3.3 & 5.1 & 2.7 & 5.7 & 5.5 & 6.1 & 4.5 & 4.4 \\
Improving coordination to reduce large imbalances in countries’ external payments & 4.9 & 5.2 & 4.5 & 5.1 & 4.8 & 4.6 & 5.7 & 5.7 & 4.8 & 5.4 \\
Fighting unemployment by creating productive jobs & 5.9 & 5.8 & 6.4 & 6.0 & 6.0 & 5.6 & 6.6 & 7.6 & 6.1 & 4.9 \\
Improving the framework for encouraging direct investment across frontiers & 4.7 & 4.4 & 4.8 & 4.6 & 4.7 & 4.8 & 5.5 & 6.3 & 4.5 & 5.0 \\
\hline
\end{tabular}\]

* 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. WES scale: 9 - most important, 5 - important, 1 - less important. The three most important aspects are shaded.

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