

WORLD ECONOMIC SURVEY

IFO WORLD ECONOMIC CLIMATE BRIGHTENS

The Ifo World Economic Climate improved in January 2002 and is now at the same level as in July 2001, i.e. before the terrorist attacks in New York and Washington (84.1 after 70.7 in October 2001 84.1 in July 2001 and 117.2 at the peak in this cycle in April 2000; 1995=100). However, it is too early to interpret this improvement as the onset of a worldwide recovery. For such an assertion experience dictates three consecutive, positive survey results. At this stage it cannot be ruled out that as in the early 1990s, an initial improvement of the indicator will be followed by a renewed setback before finally a longer lasting recovery phase starts. Thus, the next two surveys in April and July will be crucial for predicting the timing and the strength of the recovery.

World economy: Rebound of Economic Climate

After having reached an all-time low in October 2001, the overall indicator bounced back in January 2002, reaching exactly the same value as in July of last year, i.e. the last survey before the terrorist attacks in the United States. Despite the recent pick-up, the indicator is still well below its long-term average (see Fig. 1).

The improvement of the world indicator resulted exclusively from more positive expectations; the assessment of the current economic situation stagnated at its low October level. In most countries it is expected that in coming months the recovery in the hard-hit capital expenditure sector will be somewhat more pronounced than in private consumption, which proved to be quite resilient during the past recession.

United States: Increasing signs of economic recovery

In contrast to most other countries, the current economic situation in the United States is already showing signs of a recovery, though they are still weak. However, the optimism in the expectations regarding economic developments in the next six months has increased sharply. Thus, the new data support our view that the U.S. economy will pull out first from the cyclical trough. As in most other countries the outlook for capital expenditures improved more than that of private consumption. Exports are expected to pick up in the course of the next six months but less than imports, with the result that the trade balance will deteriorate further. The single most important problem remains insufficient demand followed by unemployment (see Fig. 2).

Western Europe: Cautious hopes for economic recovery in the course of the next six months

The assessment of the current situation in most Western European economies deteriorated further, with the exception of Denmark, Sweden and the United Kingdom, where some improvements were noted. Germany again received the lowest marks for the current situation, closely followed by Austria, Belgium and Portugal. Although assessments for

Figure 1

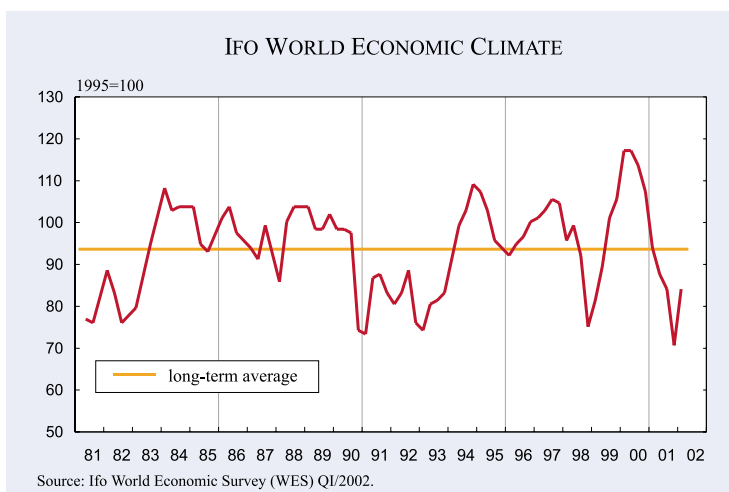
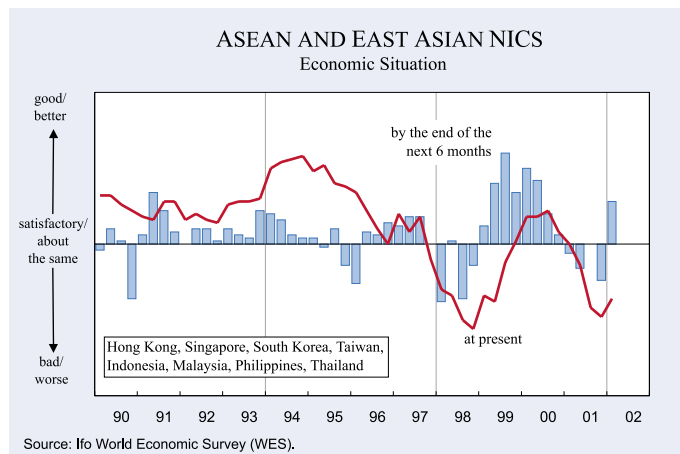
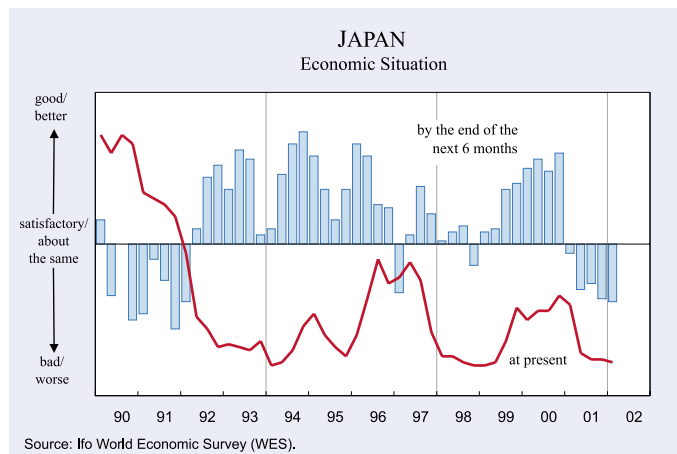
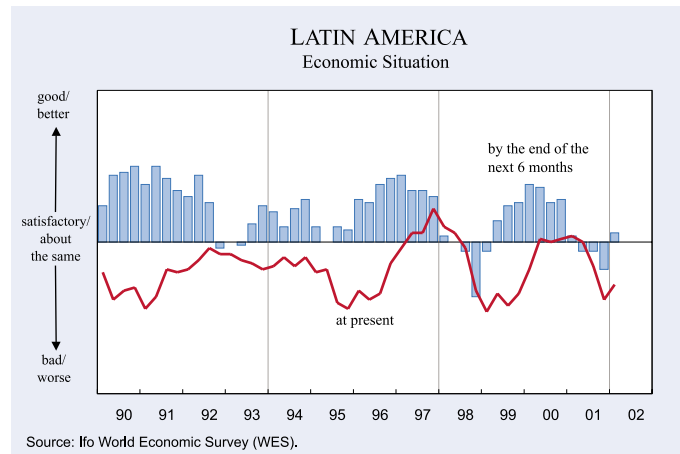
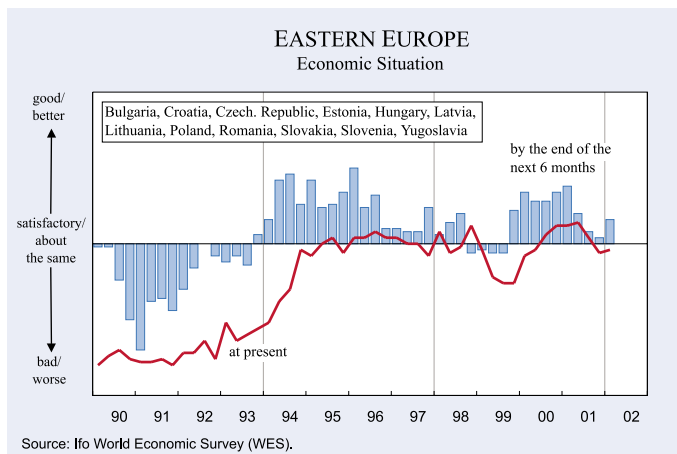
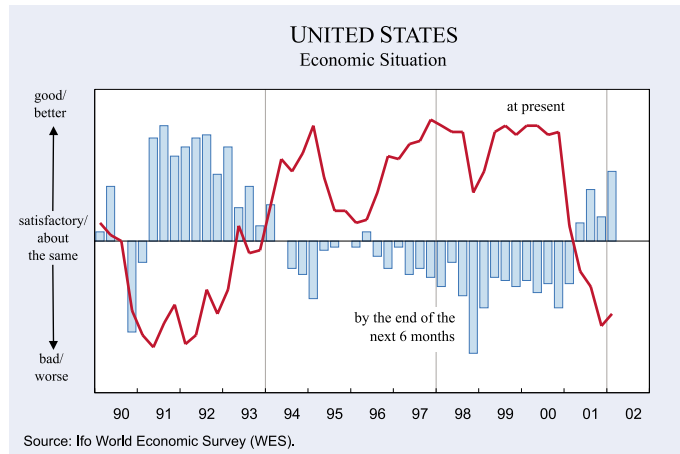
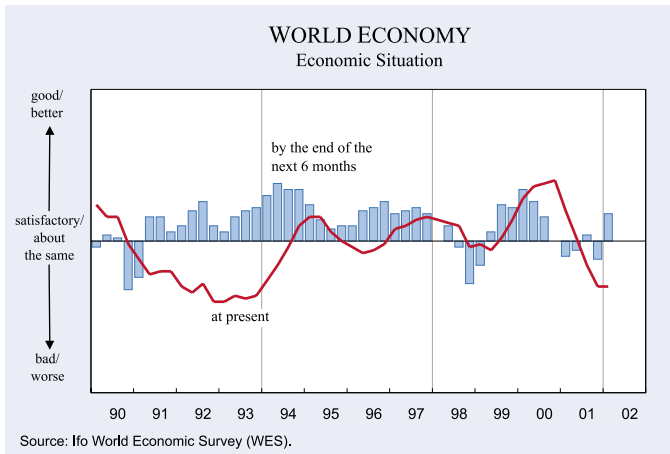


Figure 2



France, Italy and Spain were worse than in the previous survey, at 4.2, 4.4 and 5 points, respectively, their levels were in the middle of the range. The outlook for the next six months improved markedly for Western Europe as a whole and especially for Finland and Germany. Below the European average were economic expectations for the United Kingdom, Ireland and Spain whereas expectations for France and Italy were just about average. The outlook improved particularly for capital expenditures which had suffered strongly during the past twelve months. The list was topped by Norway, followed by Germany, Italy and Greece (see Fig. 3).

Eastern Europe: Economic Climate still relatively robust

The assessments of the current economic situation remained almost unchanged, being still close to the “satisfactory” level. The expectations for the next six months show growing optimism. The current economic situation continues to be more positive than average particularly in Estonia, Hungary, Latvia Slovenia and the Czech Republic. On the other hand, in Bosnia-Herzegovina, Poland, Bulgaria, Croatia and Yugoslavia the current situation is clearly below the “satisfactory” level, though the expectations point more than in the previous survey to some recovery in the course of the next six months.

In Russia, both the current economic situation and the economic outlook for the next six months deteriorated somewhat and slipped now slightly into negative territory. The lower oil price appears to have been mainly responsible for the more sceptical answers. In Kazakhstan, too, the assessment of the current economic situation and the outlook for the next months deteriorated somewhat but still remained quite positive. In contrast, the economic situation is still unsatisfactory in the Ukraine, though less so than in the previous survey; the expectations for the next six months are now seen much more confidently than in past surveys.

Latin America: Better Economic Climate despite economic chaos in Argentina

The signs of economic recovery in the G7 area – particularly in the United States – are showing spill-over effects in Latin America. Brazil, the lar-

gest economy in this area, appears to have left the doldrums. The assessment of the current economic situation has emerged from negative territory and expectations for the next six months improved even more, largely due to better export prospects. The economic climate is also relatively positive in Chile. By far the most negative assessments concerning the current economic situation came from Argentina, hit by the currency and banking crisis, followed by Uruguay, Paraguay and Bolivia.

Japan: Still in the doldrums

Although the assessment of the current economic situation is low for Asia as a whole, the assessment for Japan is poorest – aside from Sri Lanka – but bottoming out. Capital expenditures and private consumption are both rated near the bottom. Expectations for the performance of the overall economy by the end of the next six months deteriorated slightly compared to the last survey, but expected capital expenditures improved, albeit to a level which is still dismal and the lowest of all Asian economies. The yen is considered at about the right level against the US dollar and pound Sterling, but overvalued against the euro. Not surprisingly, insufficient demand is held to be the most important problem facing Japan, closely followed by unemployment.

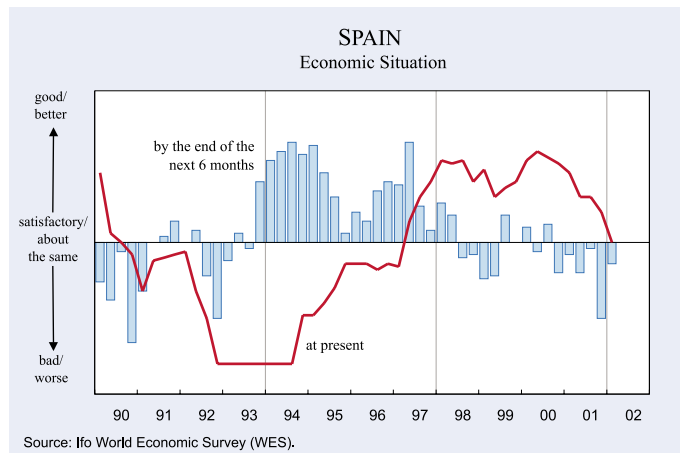
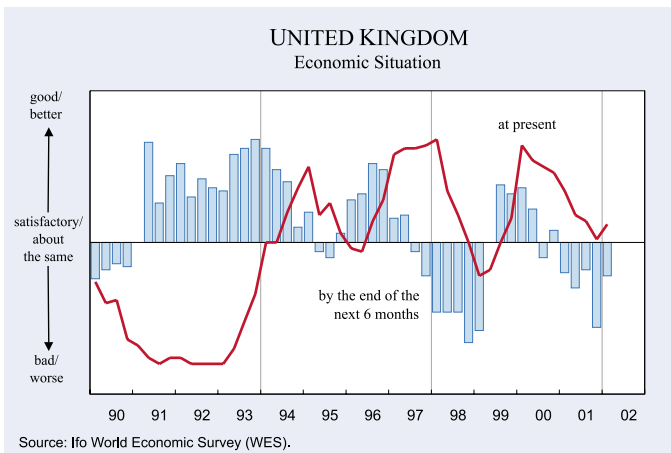
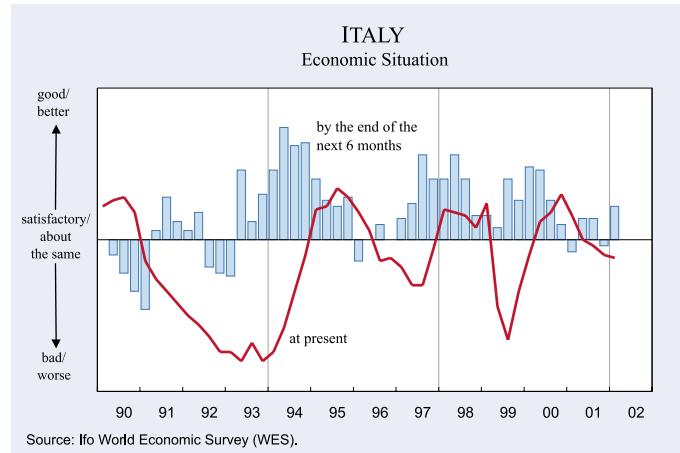
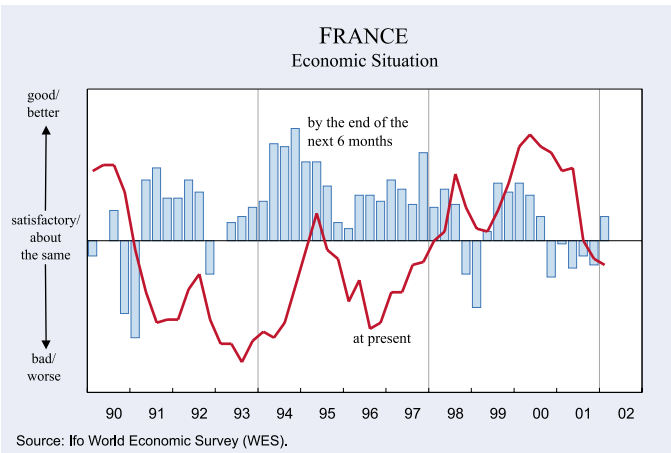
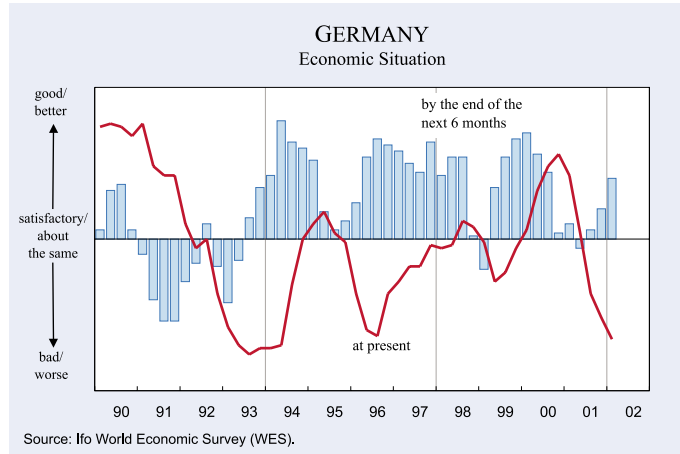
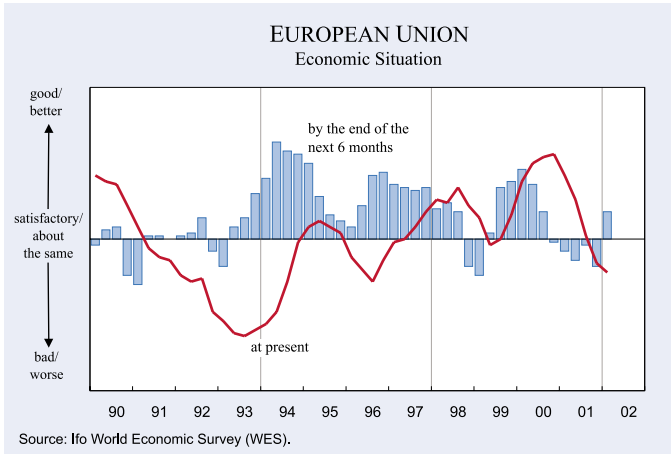
ASEAN and East Asian NICs: Economic Climate recovers from low reached last autumn

The assessment of the current economic situation of this country group has deteriorated further. The situation is again considered worst for Taiwan, followed by Hong Kong and the Philippines. The economic situation of South Korea, Malaysia and Thailand is considered to have improved, their ratings edging toward the middle of the scale. Expectations for the economic situation by the end of the next six months have improved sharply, however, giving hope for a cyclical turnaround, especially in Taiwan and the Philippines.

Interest Rates: Not much scope left for further cuts

Significantly fewer experts than in the previous survey expect the downward trend of short-term

Figure 3



interest rates to continue in the coming months. A spectacular swing from expected rate cuts to possible rate hikes can be observed in the United Kingdom, in Taiwan and in New Zealand. In the United States, where after 11 cuts short-term rates have reached low levels (1.75%), a stable development is expected in the course of the next six months. On the other hand, in Latin America expectations switched from an increase of short-term interest rates to a decrease; this swing is particularly pronounced in Brazil. In Venezuela, Costa Rica and Uruguay the trend of short-term interest rates will remain upward, however. Further cuts of short-term rates are particularly expected in Eastern Europe and to a lesser degree in the Euro area.

With regard to the long-term interest rates, a stabilisation or even a slight increase is expected in the course of the next six months. Thus, the downward trend which started in early in 2000 appears to have come to an end. Long-term interest rates are expected to increase in the next six months particularly in the United Kingdom, Canada, the United States, Australia, Venezuela, Taiwan and also Japan, though here from a very low level.

Inflation: Slowdown in coming months

On a world-wide scale consumer price inflation in 2002 is now seen to be 3.2% compared with 3.6% in the previous year. In the Euro area the inflation rate is expected to reach 2.1% in 2002 after 2.8% in the previous year. Similar figures prevail for the United States. Here a reduction of the inflation rate from 2.8% in 2001 to 2.2% this year appears likely. Asia will again show the highest degree of price stability (1.5% after 1.6% in 2001), influenced heavily by deflationary trends in Japan and Hong Kong (in both cases consumer prices will decline again by almost 1%) and continuing low inflation in China (1.3% after 1.6% last year). But also in other parts of the world a downward trend of inflation – though from a higher level – is expected, e.g. in Eastern Europe from 8.9% last year to 6.7% this year and from in the Near East 17.6% to presumably 12.2% this year. Exceptions from the falling inflation trend are Latin America, and here particularly Argentina and to a lesser degree Venezuela and Uruguay. The increasing price trend in Africa is widespread, though particularly pronounced

in Zimbabwe where inflation is expected to surpass the 100% threshold this year.

Euro: Still regarded as undervalued

The euro was still seen as undervalued against practically all currencies, though again somewhat less strongly than in the previous surveys. Conversely, the US dollar and the British pound continue to appear overvalued according to the majority of experts polled. After marked devaluations in recent months, the Japanese yen is now close to an appropriate level according to the majority of the WES experts. Particularly in the Euro area and in Oceania (Australia and New Zealand), a decline of the value of the dollar appears likely, though this expectation was in both cases even more pronounced in the previous survey. On the other hand, in Asia as well as in Eastern Europe and even more pronounced in Latin America and Africa the dollar is expected to strengthen further in the course of the next six months.

Economic Problems: Unemployment and insufficient demand maintain their top position

The ranking of economic problems remained widely unchanged with unemployment and insufficient demand still seen as the currently most urgent economic problems in most regions of the world. Changes worth mentioning are in the United States the growing importance of public deficits (rank 4 after rank 10 in the previous survey) and of lack of confidence in government's economic policy (rank 3 after rank 6). In Africa higher public deficits (rank 4 after rank 6) and increasing inflation (rank 6 after rank 8) are starting to cause growing concern among the WES correspondents. Apart from these changes, there remained striking differences: In CIS countries the lack of international competitiveness still tops the list of problems, whereas in Eastern Europe this rank is occupied by public deficits and in Oceania (particularly Australia) by trade barriers to exports.