

Economic Commentary

World Economy

In January 2012, the International Monetary Fund (IMF) published an update to their World Economic Outlook projections. The IMF's predictions for the world economy were revised downwards compared to their initial figures (published in September 2011), largely due to the economic problems of the euro area. The IMF now predict that the euro area will contract by 0.5% this year, but that there will be economic growth of 0.8% in 2013. Growth in most other advanced economies is expected to be lower than previously anticipated.

In the US, stronger domestic demand has countered some of these global economic pressures. The US unemployment rate decreased at the start of this year to a three-year low of 8.3%, and industrial production was 3.4% higher in January 2012 compared with the previous year. The US manufacturing sector has led the increase in employment, and this is set to continue in some parts of the sector. For example, the auto industry has recently announced better than expected sales figures, and companies such as Chrysler have announced the creation of 1,800 new jobs at a plant in Illinois. Figure 1 shows that the US economy is expected to have grown by 1.7% in 2011, and that growth will be 2% this year. The IMF predict that US output will grow by around 2.2% in

2013. Despite these relatively healthy predictions, the US and other world economies will take many years to recover from the global financial crisis.

The Economist estimated the number of years lost by each country as a result of the financial crisis (February 25th, 2012). Their overall indicator of economic health comprised three main categories. These were measures of household wealth (including property prices), measures of annual output and private consumption, and then real wages and unemployment. According to the overall index the 'economic clock' in the US has been turned back by 10 years, and for Greece, the clock has gone back over 12 years. Other European countries such as Ireland and Spain have lost over seven years, while Germany has done rather better losing just over two years. Figure 2 shows that Germany is expected to have grown by 3% in 2011, but that growth will be only just positive (0.1%) this year. The slow-down in world trade is expected to hit German exports particularly hard and the euro area debt crisis places a deal of uncertainty over the economy. German public sector investment is expected to fall by over 7% during 2012 (OECD, November 2011). The German labour market has however remained relatively healthy, and this has been attributed to past labour market reforms. The German unemployment rate was 6.7% in January (compared to

an average of over 10% for the euro area). Whilst the short-term economic outlook for this year worsened in recent months, the OECD forecast that the German economy would return to growth in 2013 (OECD Economic Surveys - Germany, February 2012).

The Greek economy is now in its fifth year of recession. The economy is expected to have declined by just under 7% in 2011, and the fall in output will be just over 7% this year. Agreements of new economic support packages, and confirmation by the IMF in March 2012 that it was to recommend a €28 billion arrangement 'to support Greece's ambitious economic programme over the next four years' (IMF, March 9th 2012) should restore some confidence in the economy, however the downside risks remain substantial. The unemployment rate in Greece is around 20%, and this is expected to remain at similar high levels in 2013, although the economy is expected to achieve small but positive growth levels in 2013, supported by increased exports (OECD, November 2011).

The Japanese economy contracted by an estimated 0.7% during 2011, but is expected to return to growth of around 1.6% this year. The earthquake and tsunami in March 2011, and the subsequent nuclear shutdowns resulted in imports of energy into Japan. This, together with falling manufacturing

Figure 1: GDP Forecasts, Selected Economies, annual % change, 2011 and 2012.



Source: *The Economist*, March 5th 2012. *The Economist* Poll or *Economist Intelligence Unit* estimate/forecast.

Table 1: FDI Inflows by Selected Region/Economy, 2007-2010, (US\$m).

Region / economy	2007	2009	2010
World	1,970,940	1,185,030	1,243,671
Developed economies	1,306,818	602,835	601,906
European Union	850,528	346,531	304,689
France	96,221	34,027	33,905
Germany	80,208	37,627	46,134
United Kingdom	196,390	71,140	45,908
North America	330,604	174,298	251,662
Developing economies	573,032	510,578	573,568
South, East and South-East Asia	261,041	241,534	299,653
China	83,521	95,000	105,735
India	25,350	35,649	24,640
South-East Europe and the CIS	91,090	71,618	68,197

Source, UNCTAD, WIR 2011.

exports, led Japan to record its first trade deficit since 1980, and in January 2012 the trade in goods deficit reached an all time high of US\$19.2 billion.

Economic growth in China and India remained exceptionally strong during 2011, in sharp contrast to the other world economies shown in Figure 1. These growth rates are however expected to be lower this year. Exports from China are expected to be hit by problems in Europe, which is China's largest export market, and from lower demand from America. China is the world's largest manufacturing country, accounting for over one fifth of global manufacturing output (The Economist, 10th March 2010).

Foreign Direct Investment

The World Investment Report 2011 (WIR, produced by the United Nations Conference on Trade and Development, UNCTAD), reports that global foreign direct investment (FDI) flows increased moderately to US\$1.24 trillion in 2010. These flows for 2010 are 15% below pre-economic crisis average levels, and almost 37% below the 2007 peak. UNCTAD estimates that FDI flows will recover to the pre-crisis level (US\$1.4-1.6 trillion) in 2011, and to increase further to US\$1.7 trillion in 2012 and reaching US\$1.9 trillion (2007 levels) in 2013. This forecast is however conditional on the absence of further unexpected global economic shocks. In this difficult and unpredictable economic environment, such forecasts have to be treated very carefully.

FDI flows in the European Union in 2010 were only just over one third of the 2007 flows, whilst in the UK, FDI flows fell from US\$196,390 million in 2007, to US\$45,908 million in 2010.

The UK economy

Figure 1 shows that the UK economy is expected to have grown by 0.9% during 2011, and that this will slow to 0.2% this year. The IMF downgraded their forecast for UK output growth from 1.6% to 0.6% in their January update. The UK economy contracted by 0.2% in the final quarter of 2011, with many predicting a further decline in the opening quarter of this year, and hence a slip back into recession. However labour market data has shown that the

Table 2: GVA Per head Indices¹, UK = 100.

	1997	2000	2008	2009	2010 ²
North East	78.4	77.2	76.6	76.5	76.9
North West	88.6	87.7	84.8	84.4	84.9
Yorkshire and the Humber	89.7	87.6	83.2	82.6	82.6
East Midlands	93.3	90.3	87.8	87.6	88.3
West Midlands	90.5	89.8	83.8	83.0	83.3
East of England	96.4	96.2	94.3	92.7	92.8
London	156.2	159.8	171.0	173.9	171.1
South East	104.8	106.8	106.9	106.3	107.1
South West	92.6	91.7	91.0	90.9	91.2
Wales	78.2	76.3	73.9	73.3	74.0
Scotland	96.2	94.2	97.8	98.8	98.7
Northern Ireland	80.8	80.7	77.9	76.2	76.4

Notes:

1. GVA per head indices at current basic prices on a workplace basis, based on a weighted 5-year moving average.

2. 2010 estimates are provisional.

Source: ONS, December 2011.

Table 3 Forecast Change in Real GVA (%)

	2011	2012
Wales	0.8	0.1

unemployment rate stabilised in January at 8.4%, and public sector job losses slowed. The public sector lost 37,000 jobs in the quarter to December, but this loss was more than offset by growth of 45,000 in the private sector.

Growth in household consumption and exports are expected to contribute to a recovery in the UK economy during the latter part of this year, continuing into 2013. Investment growth in 2013 is expected to further improve the economic outlook. The IMF has forecast that the UK economy will grow by 2% in 2013 (IMF, January 2012).

The Welsh Economy

The Labour Market section of this Review shows that the unemployment rate in Wales is above the UK average, and with considerable variations in rates within Wales. Unemployment rates are well above the Welsh average in Merthyr Tydfil and Blaenau Gwent, and below average in Powys, Ceredigion and Monmouthshire.

The Industrial Activity section of this Review suggests that the economic

outlook in the production industries of the Welsh economy is cautiously positive with output increasing during the latter part of 2011. Recent export figures for the whole of 2011 further reveal that the value of exports from Wales increased by £1.629bn, compared to 2010, and that exports to both EU and non-EU countries increased.

In December 2011, the ONS released data for regional, sub-regional and local gross value added (GVA). Table 2 gives an extract of the regional data provided, showing a time series of GVA per head indices for selected years from 1997 to 2010. The table shows that London and the South East (as would be expected) far outperform other regions of the UK, with London recording GVA per head of over 171 compared to the UK average of 100. At the other end of the scale, Wales has the lowest GVA per head for each of the years shown. The 2010 (provisional) figure suggests that GVA per head in Wales is only 74% of the UK average.

The sub-regional and local data contained in this latest press release

relates to 2009. At the sub-regional level (NUTS2), West Wales and the Valleys is bottom of the UK table, with GDP per head only 62.8% of the UK average. At the local level (NUTS3), the Central Valleys and the Isle of Anglesey are in the bottom five of UK local areas, with Gwent Valleys last in the table with a GDP per head of 53.3% of the UK average.

Eurostat provide data that compares the 27 European Union regions by expressing GDP per capita in terms of purchasing power standards. This data shows that GDP per capita in Wales was 79.8% of the EU 27 average in 2009, with the West Wales and the Valleys region at only 68.4%, below some regions in Eastern Europe and Greece (Eurostat, 13th March 2012).

Table 3 shows Forecasts for the Welsh economy for 2011 and 2012. The Welsh economy is expected to have grown by 0.8% during 2011, and the growth forecast is just positive, at 0.1%, for this year.