

VIII. INTERNATIONAL ECONOMIC DEVELOPMENTS

8.1 Overview of the World

Economy^{1/}

Although the global economic recovery is proceeding, its pace has moderated somewhat as the impact from the inventory cycle and fiscal stimuli have continued to fade. In advanced economies, the combination of weak labour market prospects, ongoing deleveraging and subdued consumer confidence has also contributed to the slowdown in activity. Growth in emerging economies has remained robust, although it has moderated recently.

In the United States, the recovery in economic activity stabilized in the third quarter of 2010, after slowing down in the second quarter. According to the advance estimate by the Bureau of Economic Analysis, annualized quarter-on-quarter real GDP growth stood at 2.0percent in the third quarter driven primarily by robust consumer spending and inventory accumulation. Business investment growth also remained solid,

which more than offset the weakness in residential investment. Meanwhile, growth was dampened by a large negative contribution from net exports, which was nevertheless smaller than in the second quarter. Looking ahead, the recovery is expected to proceed at a less robust pace compared with other post-recession episodes. A renewed deterioration in housing activity and weak labour market conditions may constrain the pace of the recovery.

In Japan, economic activity has been losing momentum recently, with quarter-on-quarter real GDP growth slowing down from 1.2percent in the first quarter of 2010 to 0.4percent in the second quarter. The latest data point to a further weakening in activity. In particular, the annual nominal export growth rate slowed in September for the seventh consecutive month, weighing down the fragile economic recovery. Industrial output fell by 1.9percent on a month-on-month basis in September, following a revised decrease of 0.5percent in August. These developments mainly reflect the moderation in foreign demand

^{1/} Section 9.1 and 9.2 are excerpted from European Central Bank monthly bulletin for Nov 2010 while section 9.3 and 9.4 are taken from Oct 2010.

and the expiry of government incentives for automobile purchases.

In the United Kingdom, the economic recovery has continued. Real GDP growth was 0.8percent quarter on quarter in the third quarter of 2010, after 1.2percent in the second quarter. The recovery has been broad-based across the main economic sectors, with construction, business services and finance being the largest contributors to growth. Quarter-on-quarter basis, house prices declined in the second and third quarters of 2010. Looking ahead, inventory adjustments, monetary stimulus, external demand and the past depreciation of the pound sterling should support economic activity. However, growth in domestic demand is expected to remain restrained by tight credit conditions, household balance sheet adjustment and substantial fiscal tightening.

According to the latest evidence available, economic growth in emerging Asia remained buoyant in the third quarter of 2010. Nevertheless, the pace of expansion had slowed somewhat compared with the preceding quarter as suggested by indicators on industrial

production and exports as well as some early GDP estimates for the third quarter. In a number of countries, domestic private demand has now clearly become the most important driver of economic growth.

In China, annual real GDP growth decelerated further to 9.6percent in the third quarter of 2010 from 10.3percent and 11.9percent in the second and first quarters respectively. Growth is increasingly supported by private investment and net exports, amid the gradual withdrawal of policy stimuli. However, owing to the slowdown in foreign demand, export growth also declined, albeit remaining at an elevated level. The trade surplus, while decelerating in September, was USD 65.6 billion in the third quarter of this year, the largest quarterly surplus since the beginning of 2008.

In Latin America, economic activity has remained buoyant. In Brazil, industrial production grew at an annual rate of 8.9percent in August 2010, after 8.8percent in July. In Argentina, economic activity continued to grow rapidly, with industrial production expanding by 10.1 percent on an annual

basis in September 2010, the same rate as in August. Finally, economic activity in Mexico was robust, with industrial production increasing by 7.9percent year on year in August 2010, after 6.0percent in July.

8.2 Inflation Developments

Overall, inflationary pressures have remained relatively subdued in advanced economies, while they have been somewhat more elevated in dynamic emerging markets. According to the latest available data, in the OECD countries annual consumer price inflation was 1.7percent in September 2010, compared with 1.6percent in August. Excluding food and energy, annual consumer price inflation was 1.2percent in September, unchanged from August.

In the United States, annual CPI inflation was 1.1percent in September 2010, unchanged from August. Headline inflation was boosted by an increase in the energy index, as well as a rise in food prices. Excluding food and energy, the annual rate of inflation declined to 0.8percent in September, the lowest rate

since 1961, reflecting the substantial slack in US product and labour markets.

CPI inflation in Japan stood at -0.6percent year-on-year basis in September 2010, compared with -0.9percent in August. Annual CPI excluding fresh food went down by 1.1percent, whereas excluding fresh food and energy fell by 1.5percent.

In the United Kingdom, annual CPI inflation increased markedly at the beginning of 2010, peaking at 3.7percent in April, but has moderated somewhat in recent months, standing at 3.1percent in September 2010. Looking ahead, the lagged effects of the depreciation of the Pound Sterling and the impact of expected increase in the rate of VAT in January 2011 are anticipated to exert upward pressure on consumer prices.

Inflation developments showed a diverse picture in other European countries. In September 2010, annual HICP inflation stood at 2.5percent in Denmark and 1.5percent in Sweden, 1.8percent in the Czech Republic, 2.5percent in Poland and 3.7percent in Hungary. In Romania, it was at a markedly higher level of 7.7percent in September, partly

reflecting the effect of the recent VAT hike.

Average inflation in emerging Asia region increased somewhat in September 2010 compared with the preceding month. Upward pressures on inflation rates resulted mainly from rising food prices and are projected to be temporary in nature. In China, inflationary pressures have increased, but are expected to remain contained by persistent excess capacities in the economy. In September 2010, annual consumer and producer price inflation stood at 3.6percent and 4.3percent respectively.

In Latin America, inflation rates have remained broadly unchanged. In Brazil, annual CPI inflation was 4.6percent in September 2010, up from 4.4percent in the previous month. CPI inflation in Argentina stood at 11.1percent in September 2010. In Mexico, annual inflation was unchanged in September 2010 compared with the preceding month at 3.7percent.

8.3 Commodity Markets

Oil prices recovered during September and early October. Brent crude oil prices stood at USD 83.9 per barrel on 6 October, which is 5.8percent higher than at the beginning of the year. Looking ahead, market participants expect higher oil prices in the medium term, with futures contracts for December 2012 trading at around USD 90 per barrel.

Looking at fundamentals, oil demand is growing robustly in non-OECD countries and recovering steadily in OECD countries, in particular in the United States. According to the International Energy Agency, global oil demand is expected to rise by 1.5percent in 2011. On the supply side, oil production capacity remains ample, partially owing to increases in non-OPEC output. While high levels of inventories have dampened the demand-side pressures on oil prices in recent months, some signs of an inventory drawdown have started to materialize, which may hint at tighter market conditions in the future.

The prices of non-energy commodities increased significantly in September. Food prices continued to increase strongly, driven in particular by maize and sugar. Price increases were due to a combination of robust demand, a reduced supply owing to adverse weather conditions and low inventories. Cotton has also reached record prices, mainly owing to a strong recovery in demand and tight supply. Metal prices have also increased, driven in particular by aluminum, tin and nickel. In aggregate terms, the price index for non-energy commodities (denominated in US dollars) was 20.8percent higher at the end of September than at the beginning of the year.

8.4 Exchange Rate Developments

In the three-month period to 6 October the euro appreciated by 5.5percent in nominal terms at the end of June 2010 but 5.2percent below its average level in 2009. The appreciation of the euro was broad-based and accompanied by a decrease in the implied volatility of the bilateral exchange rates of the euro vis-à-vis other major currencies.

In the same period, the euro strengthened against the US dollar and the euro was traded at USD 1.39 on 6 October, 12.9percent higher than at the end of June and around 0.6percent below its 2009 average. This strong appreciation of the euro against the US dollar was mainly driven by the relative short-term developments in the euro area and the US economies as well as policy-driven expectations in the United States. Over the same three-month period the implied volatility of the USD/EUR exchange rate showed a slight decline at both the short-term and long-term horizons.

Over the three months to the beginning of October 2010, the euro also appreciated vis-à-vis the Japanese yen. Yen/Euro stood at JPY 115 on 6 October, 5.7percent stronger than at the end of June but still 11.8percent below its 2009 average. Over the same three-month period, the implied volatility of the JPY/EUR exchange rate decreased at both the short-term and long-term horizons.

8.5 Impact of Global Economic Developments on the Ethiopian Economy

Ethiopia's external sector has continued to respond positively to the preceding recovery of global economy despite moderation in economic activities in advanced nations in the third quarter of 2010. For instance, earning from export of merchandise goods showed a 64.6 percent growth on yearly basis in the first quarter of 2010/11 largely on account of the increase in volume of exports and improved world prices of major export products.

Likewise, the receipts from services and remittances increased significantly by 31.7 percent year-on-year basis in the first quarter of 2010/11.

In contrary, import bill for petroleum in the period under review went down by 31.7 percent with respect to the preceding quarter. However, world fuel price has been rising, which together with the increase in local demand for fuel due to continuous expansion in economic activities is expected to put pressure on the balance of payments of the country.