

VIII. International Economic Developments

8.1 Overview of the World Economy⁵

According to European central bank economic bulletin issue 7/2015, global indicators suggest that world real GDP growth remained moderate in the third quarter of 2015, with substantial divergence across major economies. The global composite output Purchasing Managers' Index (PMI) excluding the euro area fell slightly in the third quarter and remained below its long-term average, pointing to continued moderate GDP growth. Developments diverged somewhat across advanced economies, although quarterly composite output PMIs in the United States, United Kingdom and Japan remained close to or above their long-term averages. Meanwhile, PMIs in the emerging market economies (EMEs) continued to weigh on the global index, with notable weakness in the quarterly output PMI in Brazil in the third quarter.

Global trade remains weak. For the first time since 2009 global trade growth turned

negative in the first half of 2015. In the third quarter the volume of world merchandise imports stabilized in July 2015, with flat growth on a three-month-on-three-month basis, up from -0.5 percent in June. The global trade outlook remains weak, however, as suggested by the further decline in the global PMI for new export orders in September, with the index remaining below the threshold of 50 for the third consecutive month.

In United State, growth activity appears to have softened in the third quarter of 2015, following a strong rebound in the second quarter. Real GDP was robust in the second quarter, growing by 1.0 percent quarter on quarter (up from 0.2 percent in the previous quarter). Consumption expenditure continued to be the main engine of growth and is expected to remain strong, supported by rising real incomes, reduced debt service burdens, low interest rates and declining gasoline prices. Meanwhile, weakness in the manufacturing sector appears to have intensified recently, as indicated by the decline in the institute of supply

⁵Sections 8.1 – 8.4 are excerpted from European Central Bank monthly bulletin, issue 7/2015.

management manufacturing index over the past three months. In addition, recent trade data suggest that net exports could act as a drag on activity in the third quarter, against the background of a strong US dollar and relatively weak foreign demand. The labor market continued to improve, but at a slower pace than earlier this year.

In Japan, momentum in the economy remained relatively subdued, following a decline in economic activity in the second quarter of this year. Real GDP fell in the second quarter (-0.3 percent quarter on quarter), partly because of temporary factors such as adverse weather conditions, but also as a result of substantial weakness in private consumption and foreign demand. Available monthly indicators for the third quarter paint a mixed picture. Although the increase in the synthetic consumption index in August suggests a rebound in consumer spending, consumer sentiment remains fragile. Meanwhile, private sector core machinery orders a leading indicator for business investment spending fell considerably in July and August.

In UK, the economy is heading towards a moderate slowdown in the second half of 2015. In the second quarter of 2015 real

GDP growth rebounded, growing by 0.7 percent quarter on quarter. Domestic demand continued to support growth, as low energy prices provided a temporary lift to real disposable income and consumption, while net exports made a significant positive contribution to growth in the second quarter of 2015. Short term indicators, in particular the PMI survey data for services, are trending downwards, suggesting a slowdown in economic growth. The unemployment rate edged down to 5.4 percent in the three months to August 2015, while earnings growth stabilized at around 3 percent.

In China, recent data overall remain consistent with a gradual slowdown of the economy. Real GDP grew by 1.8 percent quarter on quarter in the third quarter of 2015, unchanged from the previous quarter. While some indicators particularly those associated with heavy industries and construction have clearly retreated in recent quarters, the structural changes underway in the economy away from heavy industries and towards services and consumption together with the greater resilience of the other sectors, suggest that, overall, available data remain consistent with an economy undergoing a gradual slowdown. Activity is

supported by past monetary and fiscal stimulus working its way through the economy, thus buffering the Chinese economy from sharper slowdown.

8.2 Inflation Developments

Global headline inflation has stabilized at a low level in recent months. Annual inflation in OECD countries has remained unchanged at 0.6 percent since May 2015. Excluding food and energy, annual inflation in OECD countries also remained stable at 1.7 percent in August. Among major non-OECD economies, inflation fell in China and Brazil, while it increased marginally in Russia. In Russia and Brazil, inflation is still high, reflecting the upward impact of currency depreciation on import prices.

According to Euro stat, euro area annual HICP inflation was -0.1 percent in September 2015, down from 0.1 percent in August. The decline in energy inflation more than offset the small increase in food price inflation, which has increased for two consecutive months. This was mainly a result of larger price increases for the

vegetables component of unprocessed food compared with the previous year.

In United States, inflation remained at low levels, with annual headline CPI inflation flat in September. Excluding food and energy, inflation edged up slightly to 1.9 percent, reflecting an increase in services inflation.

In Japan, annual headline CPI inflation remained low in August, but annual inflation excluding food and energy continued its gradual upward trend.

In United Kingdom, annual headline CPI inflation continues to remain close to zero on the back of low energy and food prices, while inflation excluding food and energy averaged around 1 percent in the third quarter of 2015.

8.3 Commodity price

Underlying world headline inflation has stabilized following the earlier pick-up. HICP inflation excluding energy and food remained unchanged at 0.9 percent in September. While non-energy industrial inflation, which was the main driver of the recent increase in HICP inflation excluding energy and food, declined in September (down to 0.3 percent from 0.4

percent), services inflation remained stable at 1.2 percent. Other underlying inflation indicators for the euro area, such as a diffusion index and a measure based on a dynamic factor model, have not moved up further recently either, although in September 2015 all indicators continued to record higher levels than early this year. The effects of the lower euro exchange rate compared with early this year continue to pass through, but some of the loss of momentum in the pick-up in underlying inflation can be attributed to a recent strengthening in the euro exchange rate and the indirect effects of recent further declines in oil prices.

While growth in import prices remains strong, indicators of domestic pipeline pressures for underlying inflation signal continued weakness ahead. Despite some downward pressure from the recent appreciation of the euro, import price inflation for non-energy consumer goods continues to record solid annual growth rates. On the domestic side, indicators of pipeline pressures for non-energy consumer goods still point to weak dynamics along the price chain. The

annual rate of producer price inflation for domestic sales of non-food consumer goods industries remained subdued in August at 0.1 percent for the second consecutive month. Similarly, survey data for input and output prices up to September point to a continuation of the subdued domestic price pressures at the producer level. Further weakening is likely to be evident in the September data on import and producer prices as the effects of the recent appreciation of the euro and the decline in oil prices continue to filter through.

8.4 Exchange Rate Developments

The effective exchange rate of the euro remained broadly stable. In bilateral terms, the euro appreciated by 0.9 percent against the US dollar, reflecting changes in market expectations about future monetary policy in the United States. The euro also appreciated against the Japanese yen, the currencies of most emerging market economies and the currencies of several central and eastern European countries. By contrast, it depreciated against the pound sterling, the Swedish krona, the Russian rouble and the currencies of commodity exporting countries.

8.5 Impact of Global Economic Development on Ethiopian Economy

Despite the gradual recovery of the global economy, export fell by 6.6 percent. The fall in these export earnings was in turn partly a result of a decrease in international price registered during the report period.

On the other hand, the fall in international oil prices resulted in the decline of fuel import bill by 35.5 percent in the first quarter of 2015/16.

Net services payments stood at USD 61.9 million due to decline in net travel services partly as result of decline in travel from oil producing countries owing to the decline in their income following international fuel price decline. However, official long-term capital and foreign direct investment rose by 62.9 percent and 5.3 percent, respectively.

On the other hand, as a result of low trading partners head-line inflation and relatively

higher domestic price, REERI appreciated by 14.6 during QI of 2015/16 on annual basis.