

GLOBAL ECONOMIC OUTLOOK – DECEMBER

Monetary and Statistics Department
External Economic Relations Division

2012

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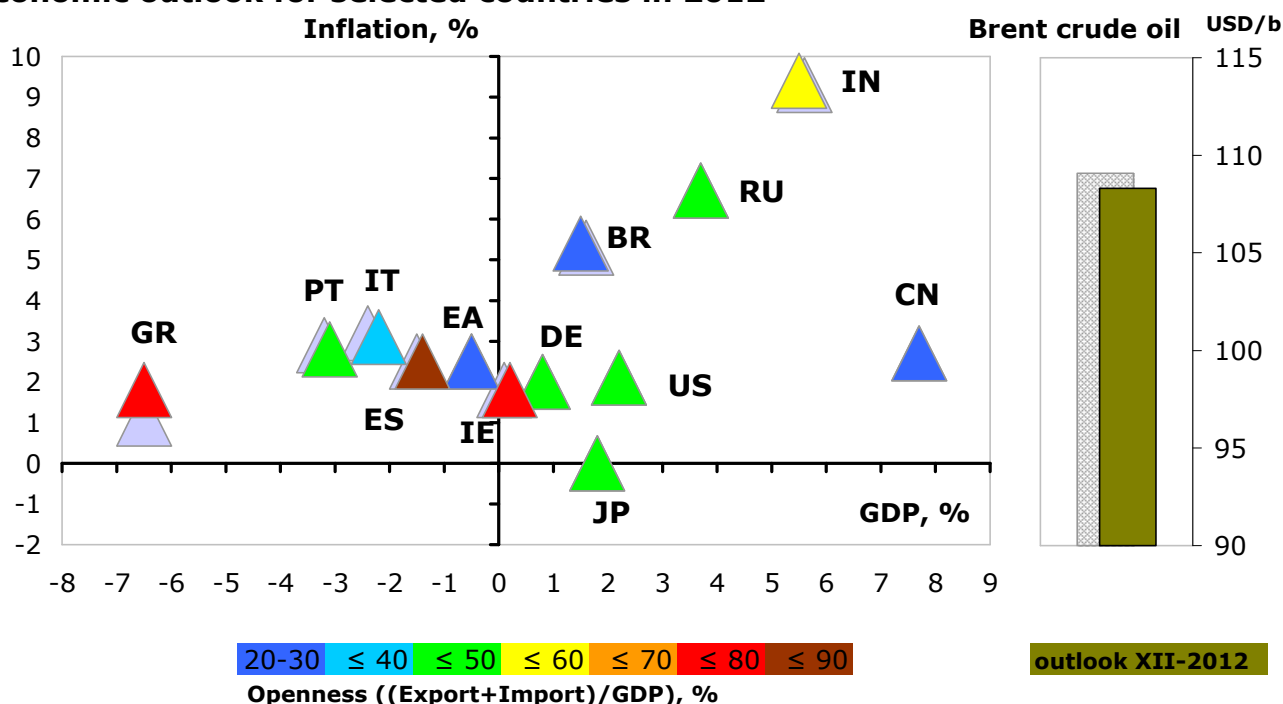
The December issue of Global Economic Outlook presents its regular overview of recent and expected developments in selected territories, focusing on key economic variables such as GDP, inflation, leading indicators, interest rates, exchange rates and commodity prices. Our regular detailed analysis focuses on the global trends in the services balance in 2005–2011, mainly with regard to the peak of the global economic crisis in 2009 and changes in the commodity and geographical breakdown.

From the perspective of the global economy, 2012 was a year of economic slowdown. The world economy recorded growth of just above 2% and inflation close to 4%. The decline in economic performance has been particularly pronounced in the euro area, due to the debt crisis and its gradual spread from the periphery to the core of the monetary union. By contrast, the US economy has performed better in the election year than it did last year.

The outlooks for 2013 suggest that the euro area economy is unlikely to grow. The outlooks for the USA are much more favourable, as confirmed by leading indicators. However, the USA now faces uncertainty in the form of the “fiscal cliff”, which, under current law, would lead to fiscal restrictions (tax increases, government spending cuts and a reduction in the US budget deficit beginning in 2013) with effects undermining current economic growth. Inflation does not represent a real threat (especially to advanced economies) at present or in the outlook for 2013, and is on a downward trend. The question is, however, whether the unconventional policy measures taken by central banks represent a medium-term threat to inflation.

The dollar is expected to continue to appreciate against both the euro and the yen and to remain roughly unchanged against the pound. The current outlooks for market interest rates are rising only slightly at the one-year horizon in both the euro area and the USA. The outlooks for prices of oil, natural gas and food commodities are falling for next year. Industrial metal prices are expected to be flat.

Economic outlook for selected countries in 2012



Note: EA – euro area, DE – Germany, US – United States, JP – Japan, CN – China, IN – India, BR – Brazil, RU – Russia, GR – Greece, IE – Ireland, IT – Italy, PT – Portugal, ES – Spain. The points are coloured according to the degree of openness of the given economy in 2012. The grey colour is the CF forecast (GDP, inflation) or Bloomberg survey (oil price) from the previous month. [Cut-off date for data: 14 December 2012]

Source: CNB calculation using Bloomberg, Consensus Economics and IEA.

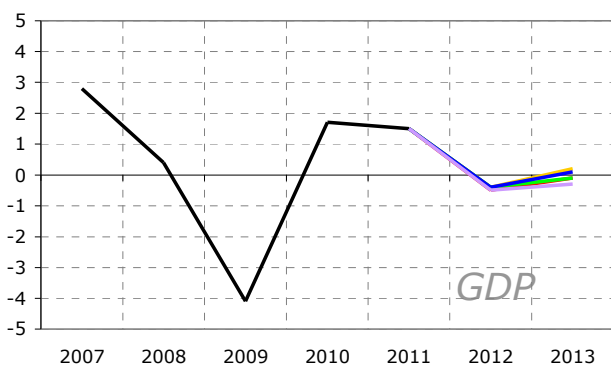
II.1 GDP

This year's final issue of Global Economic Outlook summarises the new CF, ECB, DBB, Fed and OECD outlooks. The ECB, in line with the December CF, expects GDP to fall by 0.5% in **2012** due to weak domestic and external demand. The euro area crisis is hitting Germany increasingly hard, but its impact will be short-lived thanks to sound fundamentals. CF, DBB and the OECD expect the German economy to grow by 0.7%–0.9% this year. Stronger-than-expected GDP growth in the USA in Q3 is outweighed by uncertainty surrounding fiscal policy, and the CF outlook remains at 2.2% overall. By contrast, the Fed and the OECD reduced their outlooks to 1.8% and 2.2% respectively. The CF outlook for China is the same as in September, at 7.7%.

The CF outlook for the euro area in **2013** has worsened gradually over the last 12 months and turned negative at the year-end. However, the ECB expects a gradual return to economic growth, thanks mainly to exports, supported by rising external demand and growing competitiveness of the euro area. Growth will reach 0.4%–0.7% in Germany, 1.9%–2.7% in the USA and 8.1%–8.5% in China.

EURO AREA

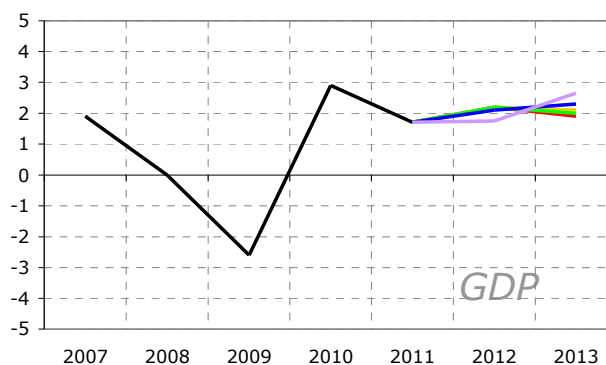
— HIST — CF, 12/12 — IMF, 10/12
 — OECD, 11/12 — EC, 11/12 — ECB, 12/12



	HIST	CF	IMF	OECD	EC	ECB
2011	1.5					
2012		-0.5	-0.4	-0.4	-0.4	-0.5
2013		-0.1	0.2	-0.1	0.1	-0.3

USA

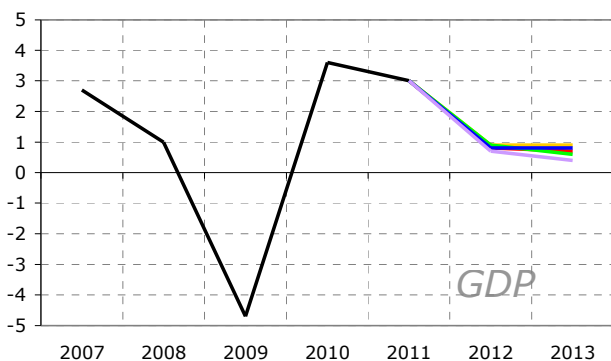
— HIST — CF, 12/12 — IMF, 10/12
 — OECD, 11/12 — EC, 11/12 — Fed, 12/12



	HIST	CF	IMF	OECD	EC	Fed
2011	1.7					
2012		2.2	2.2	2.2	2.1	1.8
2013		1.9	2.1	2.0	2.3	2.7

GERMANY

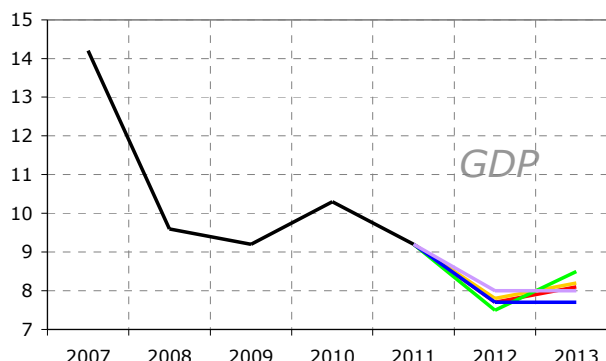
— HIST — CF, 12/12 — IMF, 10/12
 — OECD, 11/12 — EC, 11/12 — DBB, 12/12



	HIST	CF	IMF	OECD	EC	DBB
2011	3.0					
2012		0.8	0.9	0.9	0.8	0.7
2013		0.7	0.9	0.6	0.8	0.4

CHINA

— HIST — CF, 12/12 — IMF, 10/12
 — OECD, 11/12 — EC, 11/12 — BOFIT, 9/12



	HIST	CF	IMF	OECD	EC	BOFIT
2011	9.2					
2012		7.7	7.8	7.5	7.7	8.0
2013		8.1	8.2	8.5	7.7	8.0

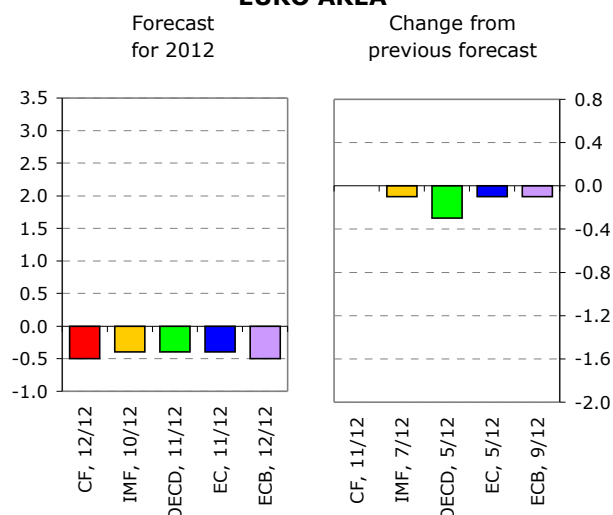
Note: Legend shows latest forecast data in format "Source, month/year of forecast publication". HIST: historical value. ECB and Fed: midpoint of range. [Cut-off date for data: 14 December 2012]

Source: CNB calculation using Eurostat, CF, IMF, OECD, EC, ECB, Fed, DBB and BOFIT databases.

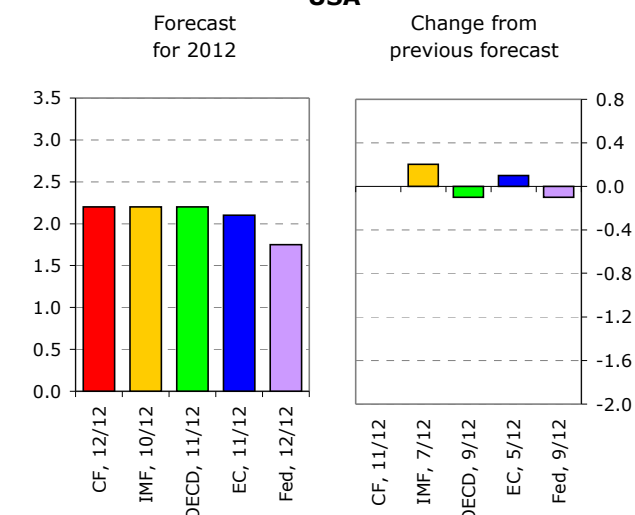
II.2 Current GDP forecast and change from the previous forecast

The December CF outlook for **this year** was unchanged for all the economies under review. The OECD increased its outlook for Germany by 0.1 pp. The other new outlooks were revised towards weaker economic growth. GDP growth will be 0.1 pp lower in the euro area (according to the ECB) and the USA (according to the Fed) compared to the previous forecast. DBB decreased its outlook for German GDP growth by 0.3 pp compared to June. The new OECD outlook is 0.3 pp lower for the euro area, 0.1 pp lower for the USA and 0.7 pp lower for China.

EURO AREA



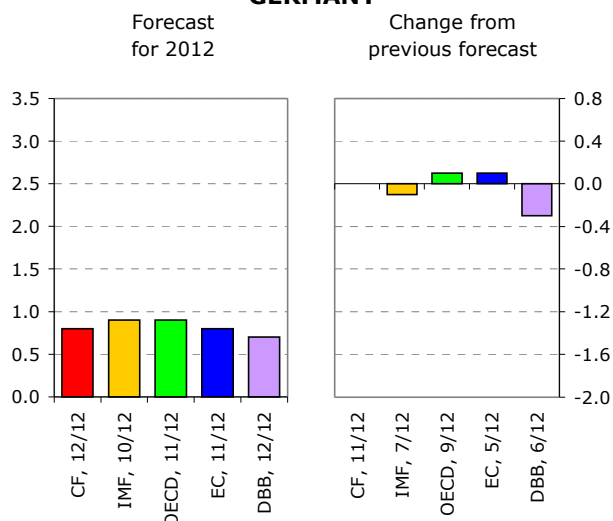
USA



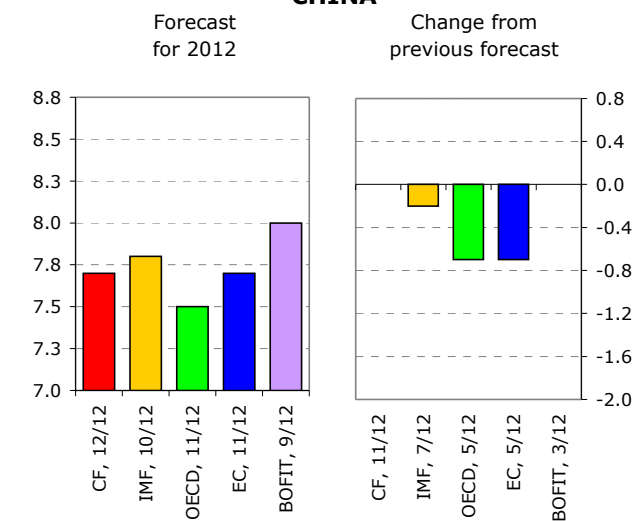
	2011	CF	IMF	OECD	EC	ECB
Forecast	1.5	-0.5	-0.4	-0.4	-0.4	-0.5
Change		0.0	-0.1	-0.3	-0.1	-0.1

	2011	CF	IMF	OECD	EC	Fed
Forecast	1.7	2.2	2.2	2.2	2.1	1.8
Change		0.0	0.2	-0.1	0.1	-0.1

GERMANY



CHINA



	2011	CF	IMF	OECD	EC	DBB
Forecast	3.0	0.8	0.9	0.9	0.8	0.7
Change		0.0	-0.1	0.1	0.1	-0.3

	2011	CF	IMF	OECD	EC	BOFIT
Forecast	9.2	7.7	7.8	7.5	7.7	8.0
Change		0.0	-0.2	-0.7	-0.7	0.0

Note: Horizontal axis of left-hand (right-hand) chart shows latest (previous) forecast data in format "Source, month/year of forecast publication". HIST: historical value. ECB and Fed: midpoint of range.

[Cut-off date for data: 14 December 2012]

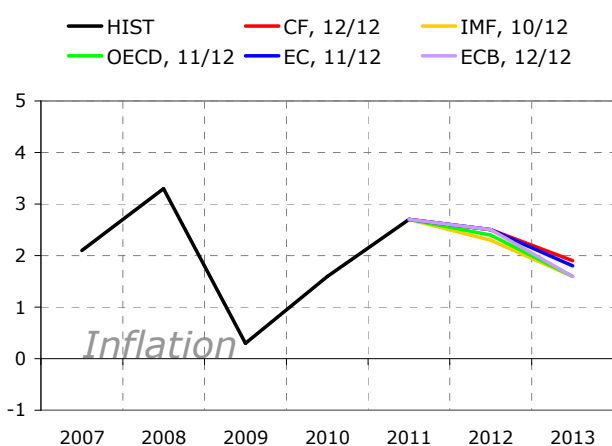
Source: CNB calculation using Eurostat, CF, IMF, OECD, EC, ECB, Fed, DBB and BOFIT databases.

II.3 Inflation

The outlooks published in early December indicate that inflation will not exceed 3% in any of the economies under review **this year**. The lowest inflation will be recorded in Germany (2.0%–2.1%) and the USA (1.7%–2.1%) according to CF, DBB, the Fed and the OECD. Inflation in the euro area will reach 2.4%–2.5% (CF, ECB, OECD). Inflation in China is expected to be about 0.2 pp higher (CF, OECD).

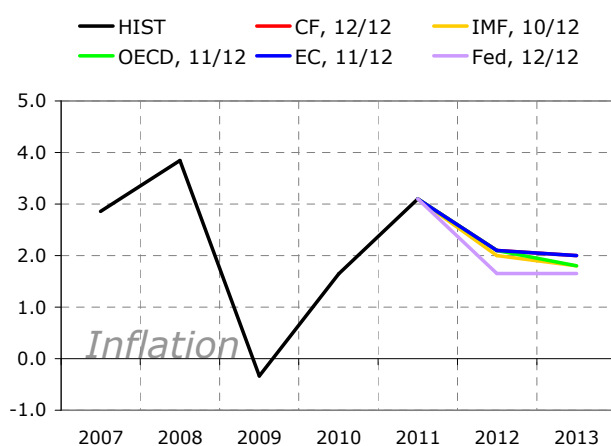
Price growth in the euro area will slow further **next year**. Inflation in the euro area and in Germany will drop to 1.5%–1.9% (CF, ECB, DBB, OECD). Consumer price inflation in the USA will slow slightly according to CF and remain at this year’s level according to the OECD and the Fed. Overall, inflation of 1.7%–2.0% can be expected in the USA in 2013 according to CF, the Fed and the OECD. Inflation in China will pick up to 3.2% according to CF, but moderate to 1.5% according to the OECD.

EURO AREA



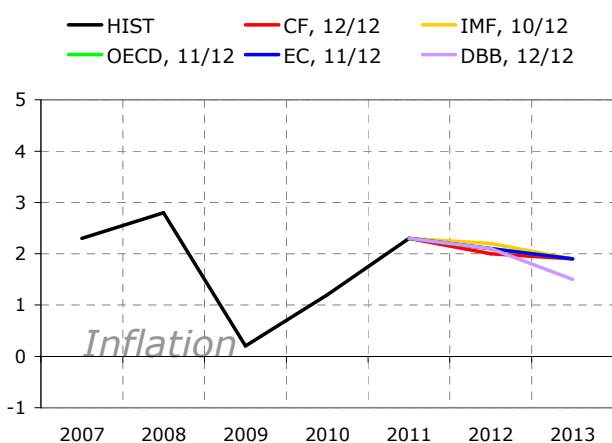
	HIST	CF	IMF	OECD	EC	ECB
2011	2.7					
2012		2.5	2.3	2.4	2.5	2.5
2013		1.9	1.6	1.6	1.8	1.6

USA



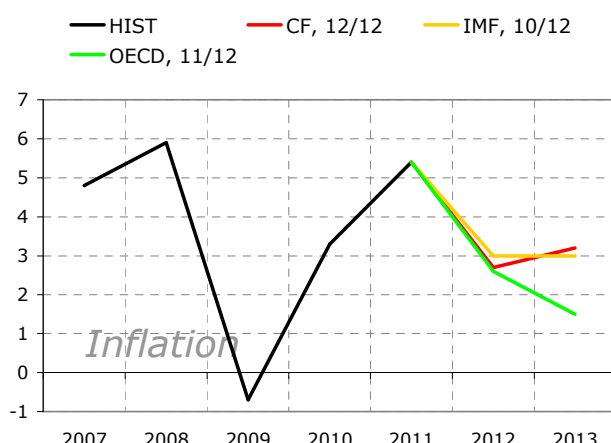
	HIST	CF	IMF	OECD	EC	Fed
2011	3.1					
2012		2.1	2.0	2.1	2.1	1.7
2013		2.0	1.8	1.8	2.0	1.7

GERMANY



	HIST	CF	IMF	OECD	EC	DBB
2011	2.3					
2012		2.0	2.2	2.1	2.1	2.1
2013		1.9	1.9	1.9	1.9	1.5

CHINA



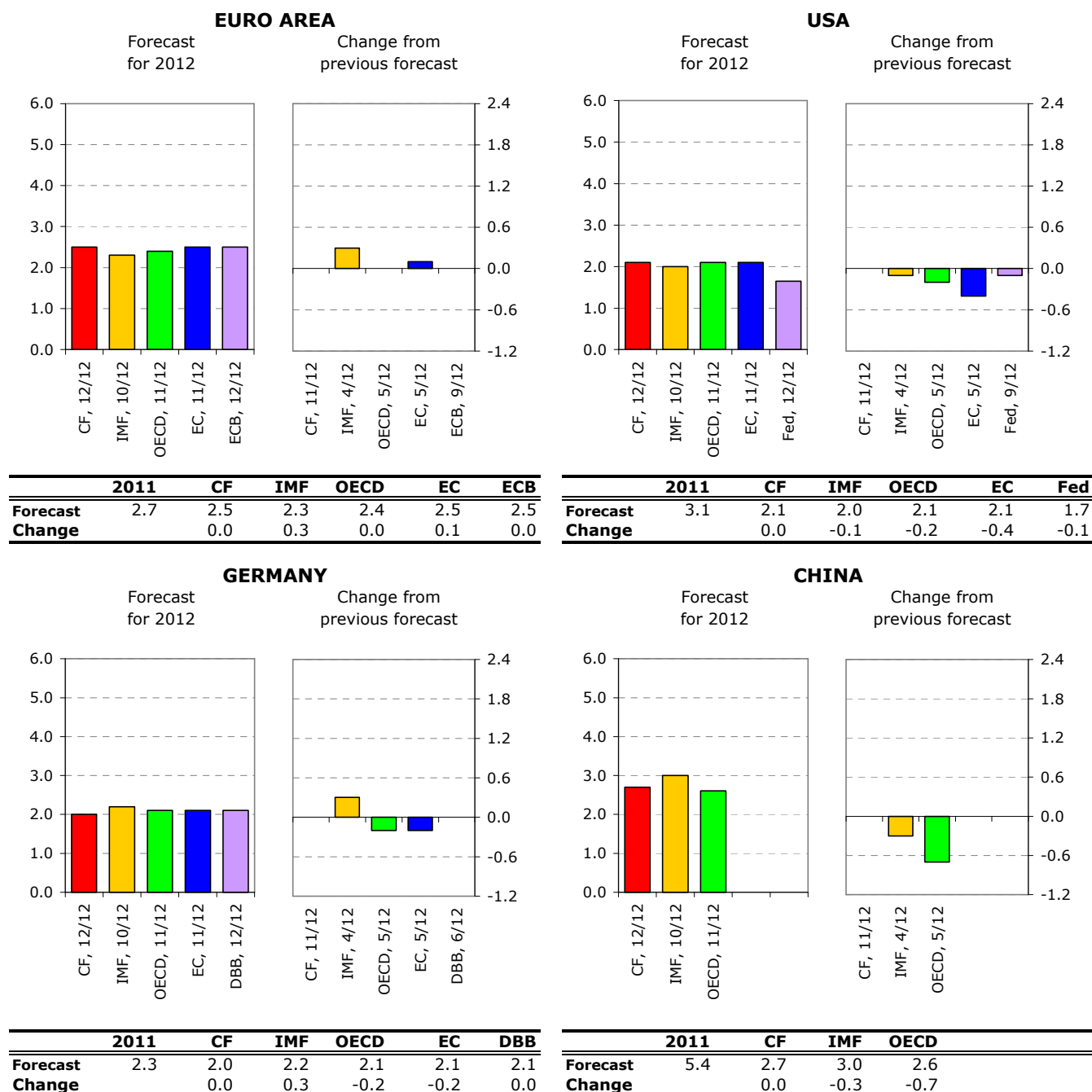
	HIST	CF	IMF	OECD
2011	5.4			
2012		2.7	3.0	2.6
2013		3.2	3.0	1.5

Note: Legend shows latest forecast data in format "Source, month/year of forecast publication". HIST: historical value. ECB and Fed: midpoint of range. [Cut-off date for data: 14 December 2012]

Source: CNB calculation using Eurostat, CF, IMF, OECD, EC, ECB, Fed, DBB and BOFIT databases.

II.4 Inflation forecast and change from the previous forecast

The new inflation outlooks (CF, DBB, ECB) for **this year** confirmed the previous forecasts. The Fed's new outlook, which is 0.1 pp lower than its September forecast, is the exception. The OECD lowered its inflation outlook for Germany, the USA and China.



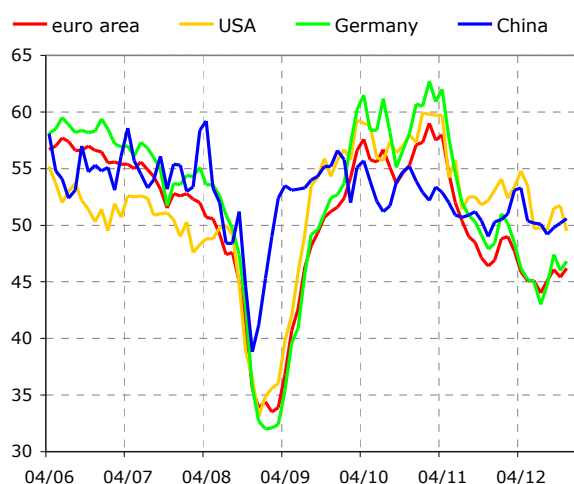
Note: Horizontal axis of left-hand (right-hand) chart shows latest (previous) forecast data in format "Source, month/year of forecast publication". HIST: historical value. ECB and Fed: midpoint of range.

[Cut-off date for data: 14 December 2012]

Source: CNB calculation using Eurostat, CF, IMF, OECD, EC, ECB, Fed, DBB and BOFIT databases.

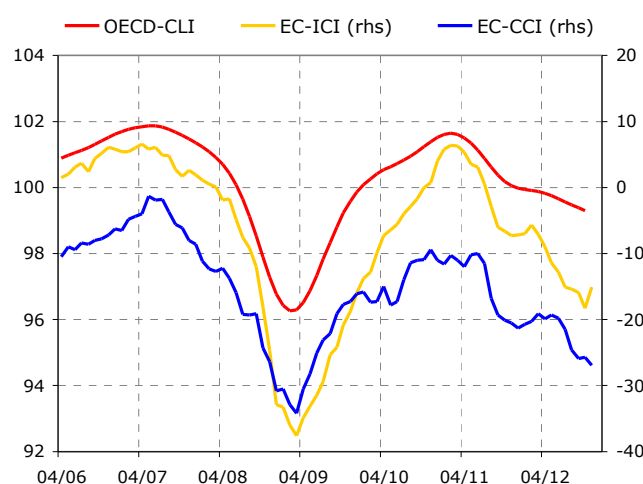
The outlook for the US economy worsened in November. Unlike in the previous two months, when economic expectations had been improving, most of the monitored leading indicators decreased or were flat in November. The PMI (Purchasing Managers' Index) in manufacturing fell below 50 points, the Conference Board and OECD composite leading indicators were flat, and one of the monitored consumer confidence indicators decreased and one increased. It is not easy to say whether economic activity in the euro area including Germany will pick up or slow down at the start of next year. The leading indicators in manufacturing (the PMI and confidence indicators) are indicating an improved outlook, whereas consumer sentiment and expectations have worsened. From the PMI perspective, economic growth in China should increase in the next six months.

PMI IN MANUFACTURING



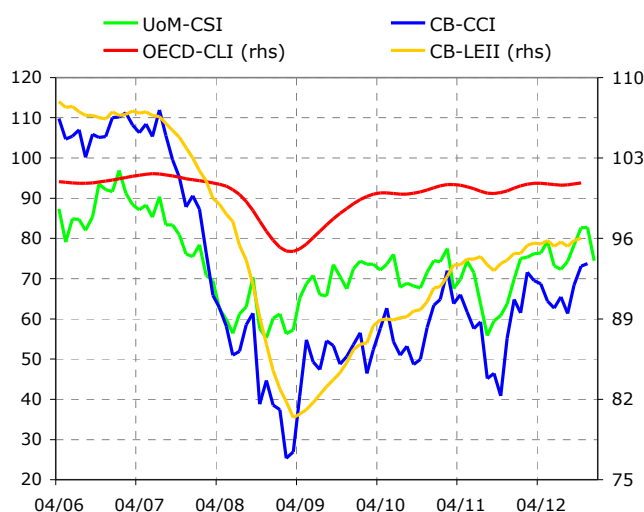
	EA	US	DE	CN
9/12	46.1	51.5	47.4	49.8
10/12	45.4	51.7	46.0	50.2
11/12	46.2	49.5	46.8	50.6

EURO AREA



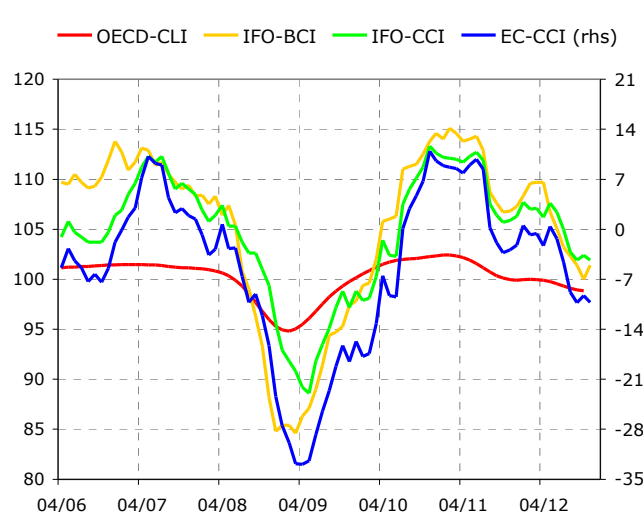
	OECD-CLI	EC-ICI	EC-CCI
9/12	99.4	-15.9	-25.9
10/12	99.3	-18.3	-25.7
11/12		-15.1	-26.9

USA



	OECD-CLI	CB-LEII	UoM-CSI	CB-CCI
9/12	100.7	95.8	78.3	68.4
10/12	100.8	96.0	82.6	73.1
11/12			82.7	73.7

GERMANY



	OECD-CLI	IFO-BCI	IFO-CCI	EC-CCI
9/12	98.9	101.4	101.9	-10.3
10/12	98.8	100.0	102.4	-9.3
11/12		101.4	101.9	-10.2

Note: OECD-CLI stands for OECD Composite Leading Indicator, EC-ICI (right-hand scale) for European Commission Industrial Confidence Indicator, EC-CCI (right-hand scale) for EC Consumer Confidence Indicator, CB-LEII for Conference Board Leading Economic Indicator, CB-CCI for CB Consumer Confidence Index, UoM-CSI for University of Michigan Consumer Sentiment Index, IFO-BCI for Institute for Economic Research – Business Climate Index, and IFO-CCI for IFO Consumer Confidence Index. [Cut-off date for data: 14 December 2012]

Source: CNB calculation using OECD, EC, IFO and UoM databases.

IV.1 Outlook for short-term and long-term interest rates: Euro area

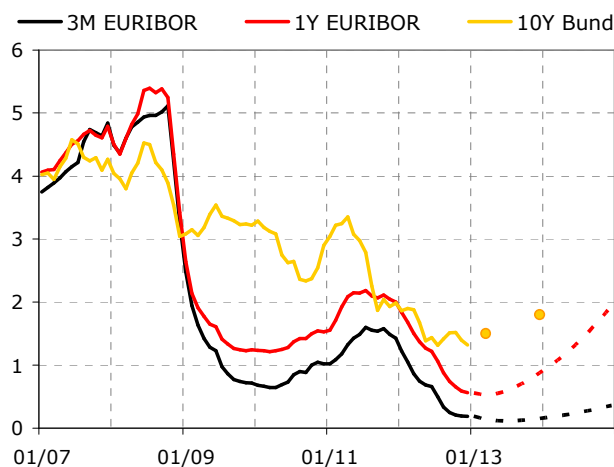
The downward trend in unsecured interest rates was renewed in December and was more pronounced for longer maturities. In early December, EURIBOR rates reached another historical low (0.18% for 3M and 0.54% for 1Y maturity). Euro area money market liquidity remains high and the risk premia for both maturities showed no major changes in the period under review.

At its last meeting, the ECB Governing Council left key rates at the current level, but discussed the possibility of negative deposit rates. Liquidity operations will continue under the current regime.

The outlook based on implied rates shifted slightly downwards again compared to the previous month. The rates are expected to fall somewhat further over the next few months. The Consensus Forecasts outlook for the 3M rate decreased by 0.1 pp at both the 3M and 1Y horizons.

The German 10Y government bond yield stayed at 1.4% in November, but fell again in December. It reacted temporarily to the political situation in Italy, but the publication of improved ZEW sentiment led to a rise in rates.

EURO AREA



	10/12	11/12	06/13	12/13	06/14	12/14
3M EURIBOR	0.21	0.19	0.15	0.22	0.32	0.45
1Y EURIBOR	0.65	0.60	0.72	1.03	1.45	2.03
	10/12	11/12	02/13	11/13		
10Y Bund	1.52	1.38	1.60	1.90		

Note: Forecast for EURIBOR rates is based on implied rates from interbank market yield curve (FRA rates are used from 4M to 15M and adjusted IRS rates for longer horizons). Forecast for German government bond yield (10Y Bund) is taken from CF. Dashed lines and points represent outlook. [Cut-off date for data: 10 December 2012]

Sources: Thomson Reuters (Datastream), Bloomberg, CNB calculations.

IV.2 Outlook for short-term and long-term interest rates: United States

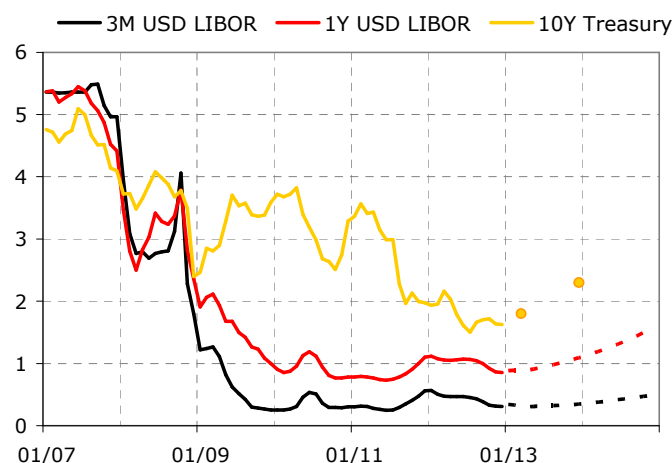
The 3M and 1Y USD LIBOR rates have been flat at around 0.31% since late October. The 1Y rates recorded a very slight decline and stood at 0.84% in early December.

In December, the Fed said it would continue to pursue easy monetary policy. The Twist operation will be replaced by a programme of outright bond purchases. The rates were not changed and the Fed will keep them close to zero as long as the unemployment rate remains above 6.5% and inflation in two year horizon stays below 2.5%.

The outlook based on implied rates also shifted downwards compared to the previous month. The 3M LIBOR will stay below 0.5% for two years. The 1Y rate will rise more slowly, reaching 1.6% at the end of 2014.

In November, the 10Y government bond yield responded to domestic developments. The new CF made no significant change to the outlook, lowering the expected level by 0.1 pp at the 3M horizon only.

USA



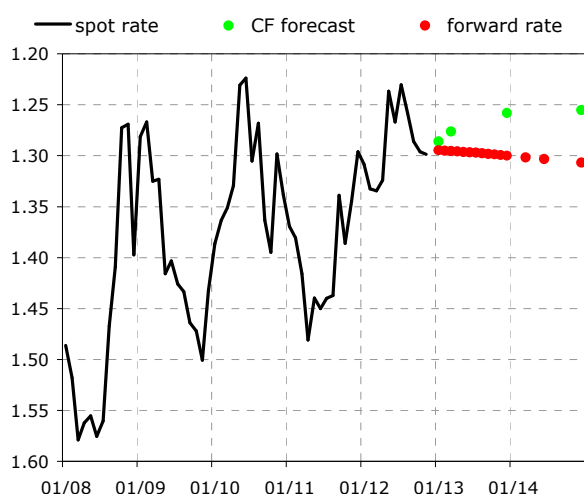
	10/12	11/12	06/13	12/13	06/14	12/14
3M USD LIBOR	0.33	0.31	0.33	0.39	0.46	0.54
1Y USD LIBOR	0.92	0.87	1.00	1.18	1.39	1.70
	10/12	11/12	02/13	11/13		
10Y Treasury	1.72	1.62	1.90	2.30		

Note: Implied LIBOR rates are derived from London interbank market yield curve. Forecast for 10Y Treasury yield is taken from CF. Dashed lines and points represent outlook. [Cut-off date for data: 10 December 2012]

Sources: Thomson Reuters, Bloomberg, CNB calculations.

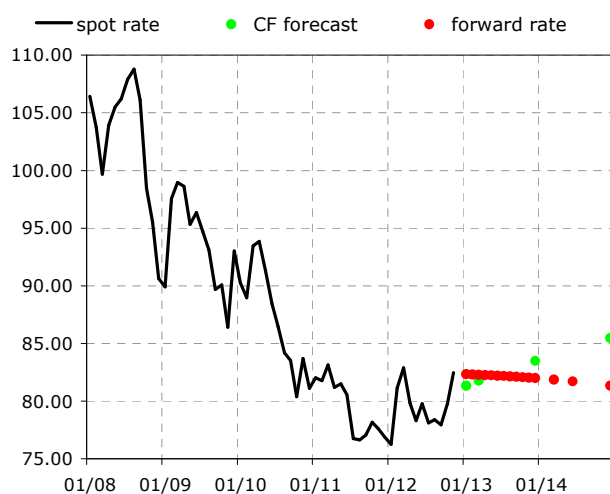
The dollar-euro exchange rate has been affected in recent months not only by the strength of the economic recovery, but also by political uncertainty and actions taken by monetary authorities. The dollar has depreciated under the threat of the fiscal cliff, even though new data, especially from the labour market, look favourable. By contrast, the euro area is in recession, although the debt crisis-related tensions have eased. The announcement of new measures by the Fed led the dollar to depreciate against the euro. The ECB is not ruling out further steps either. The risks are reflected in the new forecast, which expects the euro to depreciate against the dollar by 2.7% at the 1Y horizon. The yen has been depreciating against the dollar since early October amid rising political pressure on the Japanese central bank to take more radical action to promote growth. According to CF12, this trend will last two years. The recovery in the UK is not very robust and public debt poses a threat to the country's credit rating, therefore the forecast for the dollar-pound rate remains stable. The outlook for the Swiss franc-dollar rate is also unchanged.

US\$ per Euro



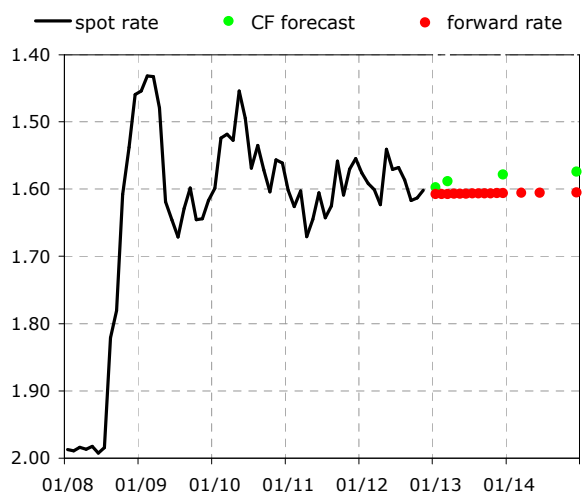
	10/12/12	01/13	03/13	12/13	12/14
spot rate	1.294				
CF forecast		1.286	1.276	1.258	1.255
forward rate		1.295	1.295	1.300	1.307

Yen per US\$



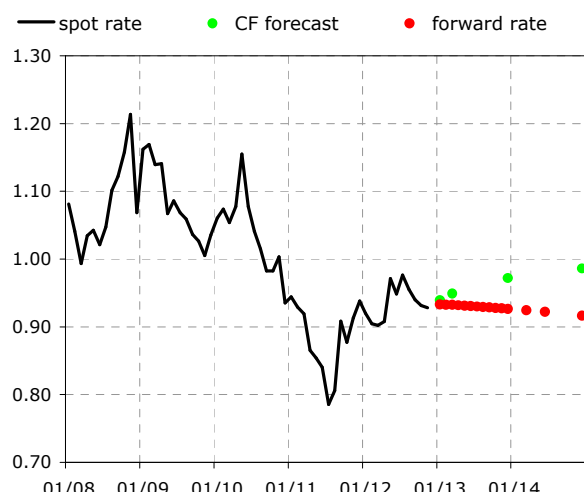
	10/12/12	01/13	03/13	12/13	12/14
spot rate	82.36				
CF forecast		81.33	81.79	83.49	85.47
forward rate		82.33	82.29	82.00	81.35

US\$ per UK£



	10/12/12	01/13	03/13	12/13	12/14
spot rate	1.608				
CF forecast		1.597	1.588	1.578	1.574
forward rate		1.607	1.607	1.606	1.605

Swfr per US\$



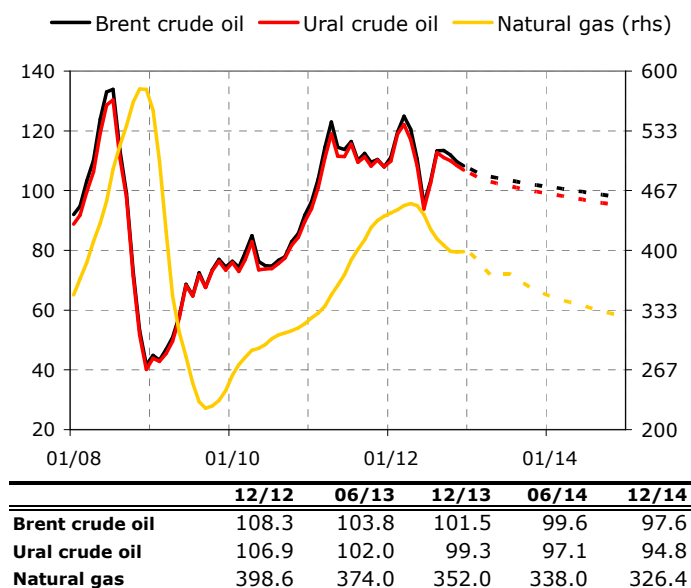
	10/12/12	01/13	03/13	12/13	12/14
spot rate	0.934				
CF forecast		0.939	0.949	0.972	0.986
forward rate		0.933	0.932	0.927	0.916

Note: Increase in currency pair represents appreciation of US dollar; data as of the last day of the month. Forward rate does not represent outlook; it is based on covered interest parity, i.e. currency of country with higher interest rate is depreciating. Forward rate represents current (as of cut-off date) possibilities for securing future exchange rate. [Cut-off date for data: 10 December 2012] CNB calculation using Bloomberg and Consensus Forecasts databases.

VI.1 Oil and natural gas

The price of Brent oil has been fluctuating between USD 106 and USD 116 a barrel since October. From the lows recorded in early November it rose gradually during the month to more than USD 110 a barrel, but fell again in early December. Subdued global demand for oil and uncertainty regarding its outlook related to the situation in the euro area and possible fiscal restriction in the USA are pushing oil prices down. Non-OPEC oil extraction, which rose in November after fields in the North Sea and Brazil came back on line, had a similar effect. Supplies from OPEC countries, primarily Saudi Arabia, Angola and Libya, also rose in November. By contrast, unrest in the Middle East pushed oil prices up in November. In December, declining spot prices were accompanied by falling futures prices. Based on futures prices, the outlook is falling and the price of oil should be below USD 98 a barrel at the two-year horizon. The outlook for natural gas prices also shifted downwards compared to the previous GEO.

OUTLOOK FOR PRICES OF OIL AND NATURAL GAS



Note: Brent oil price in USD/barrel (ICE quotation). Price of Russian natural gas at German border in USD/1,000 cubic m (IMF database). Future oil prices are derived from oil prices. Dashed line represents outlook.

[Cut-off date for data: 14 December 2012]

Source: Bloomberg, IMF, CNB calculations.

VI.2 Other commodities

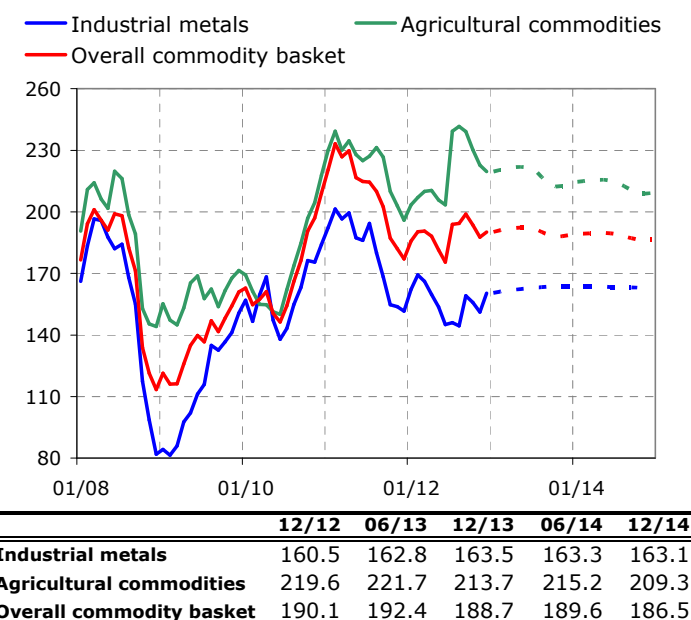
The overall non-energy commodity index was still falling in November, but rebounded slightly in early December.

The November decline was chiefly driven by food prices, which have been returning to lower levels since September. In the food index, the biggest declines were recorded for prices of wheat, maize and soy, i.e. the crops whose harvest was hit hardest by the drought in the USA this summer. By contrast, beef prices are still close to historical highs and their outlook is still rising.

Prices of industrial metals also decreased in November, but grew significantly in December, generating a rise in the overall non-energy commodity index. The price of aluminium rose the most. By contrast, the decline in prices of carbon steel deepened significantly, with prices reaching their lowest level since the start of 2010. The outlook for industrial metals is broadly flat, except for aluminium, whose price is expected to rise strongly.

Prices of electricity and coal edged up in November and December and their outlook is flat and rising respectively.

OUTLOOK FOR OTHER COMMODITY PRICES



Note: Chart shows price indices, year 2005 = 100. Dashed line represents outlook based on futures.

[Cut-off date for data: 14 December 2012]

Source: Bloomberg, outlooks based on futures.

GLOBAL TRENDS IN THE SERVICES BALANCE 2005–2011¹

The services balance on the current account of the balance of payments does not enjoy such interest as its more robust sister, the trade balance, but as a traded component of aggregate output it has a strong position in the output balance² and the current account. Services have gained in importance as a foreign trade commodity in the last quarter of a century. Although it used to be assumed that they were a typical example of a non-tradable item, services trade is currently rising rapidly. This article aims to map the main international services trade flows over the medium-term horizon of 2005–2011, focusing mainly on the peak of the global economic crisis in 2009, and to evaluate changes in the commodity and geographical breakdown. It also examines the Czech Republic's services balance and its evolution vis-à-vis major trading partners, especially Germany. With regard to data source consistency, the global analysis is based on the IMF database in USD (BPM6 methodology) and the analysis of the Czech Republic is based on the CNB's balance of payments database in CZK (BPM5 methodology).³

Introduction

The turnover of the global balance of services, representing the sum of transactions in the five sub-balances,⁴ reached USD 7.4 trillion in 2010, rising by almost one-half in 2005–2010. However, it accounted for only about one-quarter of the global trade balance turnover. Despite the considerably higher value of goods exports and imports compared to services in 2006–2010 (excluding 2009), goods trade turnover increased faster on average than services trade turnover. By contrast, the decline in goods trade in 2009 – a year of global economic contraction – was almost 12 percentage points deeper than in the case of the services balance. This was probably due to a higher share of fixed credits and debits in the services balance, which are less sensitive to the phase of the business cycle, or may even increase in a recession (e.g. legal services), while goods trade in general decreased considerably when the crisis escalated as a result of a downturn in production and distribution chains. As in the case of goods trade, however, the crucial determinants of services trade from the point of view of individual countries were external demand, aggregate domestic demand and the real exchange rate.

Global exports of goods and services should theoretically always equal global imports. In reality, however, this does not always hold, as a result of the various thresholds relevant to the reporting of transactions in the goods and services balance, the various methods used at the national level to comply with the methodologies laid down by international institutions (IMF, OECD), revisions and errors, as well as potential time mismatches. These mismatches relate not only to statistical data publication schedules, as the records on commodities in transport can also be a substantial source of statistical

¹ Written by Ladislav Prokop (Ladislav.Prokop@cnb.cz). The opinions expressed in this article are those of the author and do not necessarily reflect the official position of the Czech National Bank.

² The output balance is the sum of the trade balance (goods balance) and the services balance.

³ Within the services balance, BPM6 (Balance of Payments and International Investment Position Manual) now also monitors processing operations (imports of goods for processing, e.g. completion, assembly and subsequent exports) as well as maintenance and repair, which in BPM5 were included in the trade balance. By contrast, merchanting, which was included in other services under BPM5, is reported in the trade balance under BPM6. As shown below, the value and evolution of these items are very important for the changes in the balance of services of the Czech Republic and other countries (e.g. Germany). However, they change nothing from the perspective of the output balance as the sum of the trade balance and the services balance.

⁴ Under BPM6, these include the balances on transport, travel, other services, processing, and maintenance and repair.

differences. The global balances of goods and services therefore end up not as fully balanced, but with certain statistical residuals called discrepancies. As in the case of the trade balance, the statistical discrepancy of the services balance was positive with an upward tendency (see Figure VII-1).⁵

1. Regions

1.1 USA

Notwithstanding the financial and economic crisis, the USA recorded the fastest services surplus growth (more than USD 100 billion) in 2005–2011. Surpluses on other services and travel were the biggest contributors to the total surplus throughout this period (see Figure VII-2). The economic downturn in 2009 was associated with an only modest decrease in total turnover in the USA, leading to a negligible decline in the total surplus. The surplus continued to rise apace in the following two years, mainly because of an increase in credits from other services (especially charges for the use of intellectual property). The moderation of the total surplus in 2009 was due mainly to a decline in the travel and other services surpluses.⁶ The services balance thus contributed to a moderation of the US output balance deficit – caused by a high trade deficit – throughout the period under review. At the same time, it testified to strong competition in services as a whole in the USA, especially in highly sophisticated industries.

Figure VII-1

Global services balance and global trade balance (USD billions)

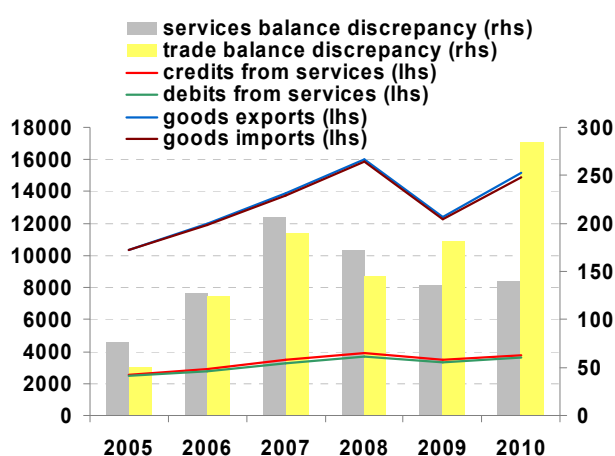
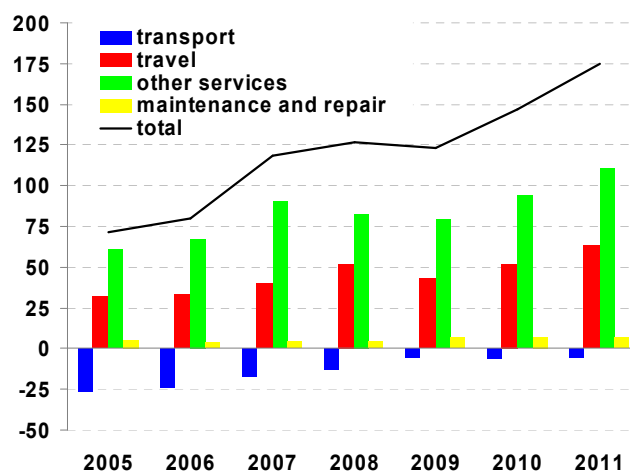


Figure VII-2

US services balance (USD billions)



Source: IMF, author's calculations.

1.2 Euro area

The euro area's balance of services followed a similar path as in the case of the USA. However, the impact of the crisis year 2009 was more pronounced. Sizeable decreases in the surplus and above all in the trade turnover were recorded that year. However, both variables then started rising rapidly again. The aggregate balance for the euro area – including intra-regional turnover – showed a similar pattern (see Figure VII-3). As

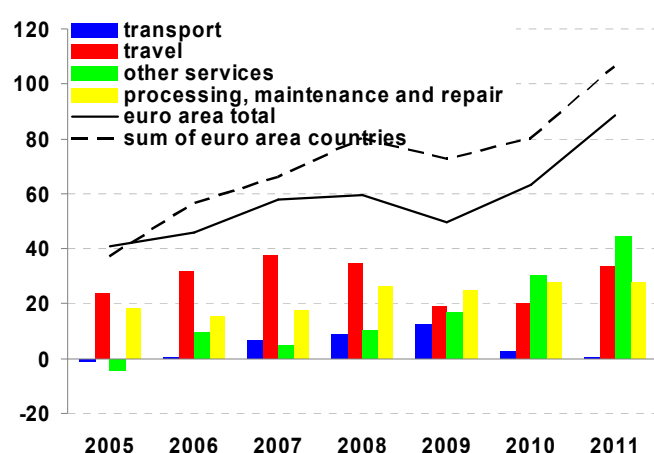
⁵ A positive discrepancy was recorded for other services and travel over the entire period under review, while a negative global discrepancy was visible in transport.

⁶ However, credits from almost all items of other services continued to rise even in 2009.

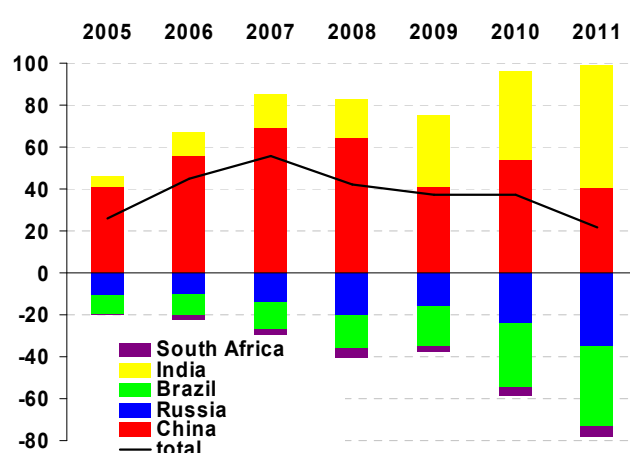
regards the individual items, the travel surplus was the biggest contributor to the euro area aggregate services surplus until 2008. In the following three years, however, the role of the other services surplus strengthened considerably. The surplus on processing and maintenance and repair services was more significant compared to the USA throughout the period. Most euro area countries (12) recorded a services surplus throughout the whole period. The largest surpluses were recorded by Spain (due to a high surplus on travel), Luxembourg (due to a high surplus on financial services) and Greece (due to surpluses on transport and travel). Given their high economic potential, the biggest services turnovers were associated with Germany and France. Germany also showed the largest deficit, caused – unlike in France – by a deep deficit on travel. Ireland also ended in large deficits (owing to an overall deficit on other services).

Figure VII-3

Euro area services balance (USD billions)

**Figure VII-4**

BRICS services balance (USD billions)



Source: IMF, author's calculations.

1.3 BRICS⁷

The five countries of the BRICS group, which have strong growth potential but are geographically very diverse, have recently been under close scrutiny. As in the case of the USA and the euro area, the aggregate services balance of these countries recorded a surplus, which, however, decreased after peaking in 2007 (see Figure VII-4). Its largest items were the overall services surplus of China and the rising services surplus of India. The deficits of the other three economies, which increased substantially during the period, partly offset the overall surplus of the group. China's overall surplus⁸ initially increased mainly as a result of a rise in the processing surplus. However, it was also significantly supported – especially in the last two years – by surpluses on other services (above all business services) and travel. In India, the services surplus increased steadily in the period under review, recording the largest change in balance within the group (almost USD 54 billion). This change was due to a sharp increase in the surplus on other services, more specifically growth in credits from computer services. By

⁷ A group of countries comprising Brazil, Russia, India, China and South Africa.

⁸ China's services balance is monitored for three geographically and above all economically different territories: continental China, the services city of Hong Kong and the gambling island of Macau. It is therefore natural that trends in the three Chinese sub-balances differed. Continental China recorded a surplus until 2008, switching to a rapidly rising deficit in 2009 (due mainly to higher debits from travel and transport). However, the adverse evolution of continental China's services balance was outweighed by growing surpluses in Hong Kong (due to faster growth in credits than debits from all three sub-items) and Macau (due to surging credits from travel).

contrast, the widening of the overall deficits of Brazil and Russia was connected mainly with a rise in deficits on travel and other services. The links between the BRICS countries and advanced market economies manifested themselves clearly in a year-on-year decline in services exports and imports in all the countries under review as the financial crisis peaked in 2009.

1.4 Visegrad Four

Before we map the Czech Republic's services balance, let us examine the developments in the narrow Central European region of the Visegrad Four (the Czech Republic, Slovakia, Hungary and Poland – hereinafter the "V4"). In contrast to the emerging economies of the BRICS group, the aggregate surplus of the V4 countries mirrored the path of the services surpluses of the euro area and the USA (see Figure VII-5). In the crisis year 2009, exports and imports of services declined and the balances of the countries under review (except Hungary) deteriorated, but 2010 saw renewed growth in overall turnover and a slight rise in the aggregate surplus. The deterioration in 2009 was due mainly to lower surpluses on processing and travel. As Figure VII-6 shows, some common features can be observed in the structure of the services balance of the countries under review. On average, all four economies recorded surpluses on transport and travel in the period under review, while other services ended in a deficit. The activities of foreign-controlled corporations specialising in importing services from their home countries may be an important factor associated with the other services deficit. In Hungary and above all the Czech Republic, the travel surplus is basically the determining item of the overall balance. In terms of absolute value and ratio to GDP, the services balance of the Czech Republic recorded the highest average surplus in the period under review.

Figure VII-5

V4 services balance (USD billions)

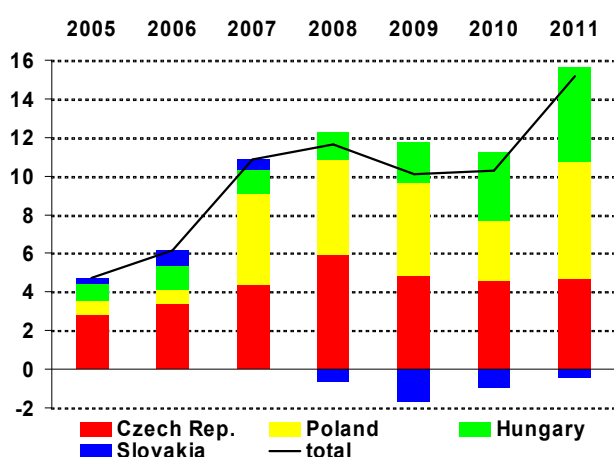
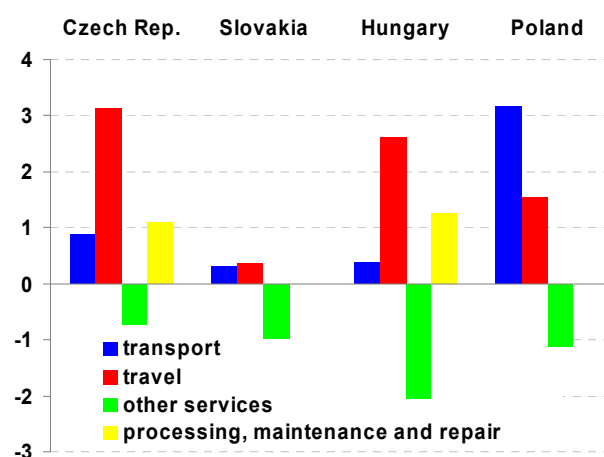


Figure VII-6

Average services sub-balances in V4 countries in 2005–2011 (USD billions)



Source: IMF, author's calculations.

2. The Czech Republic and the world

2.1 Geographical breakdown

In 2005–2011, credits from exports to the EU – influenced by a favourable geographical position and foreign investment in the Czech Republic, including the transfer of activities from other countries to the Czech Republic – dominated the Czech Republic's total credits from services trade. The share of services exports to the EU and the euro area⁹ was largely determined by exports to Germany, which was – as in the case of goods trade – the Czech Republic's largest trading partner. By contrast with goods exports, diversification of services exports in favour of non-EU countries did not occur and the share of exports to countries outside the EU followed a falling trend (see Figure VII-7).¹⁰ Similarly, the overall services balance was most strongly affected by the surplus with the EU, especially Germany (see Figure VII-8), which accounted for roughly 61% of the total surplus in the period under review despite substantial swings. In the final two years, however, the value of the surplus with other euro area members rose significantly. A deficit in trade with non-EU countries, especially China, was observed for most of the period under review. As mentioned below, the shift of this group of countries from deficit to surplus in 2009 was linked chiefly with rapid growth in credits.

Figure VII-7

Geographical breakdown of credits from the Czech Republic's services exports (shares in %, sum = 100)

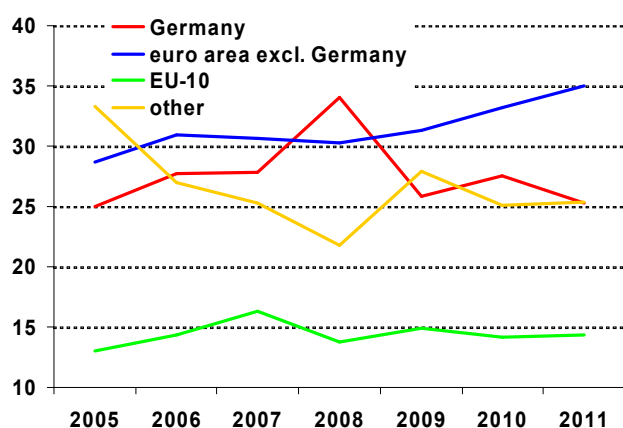
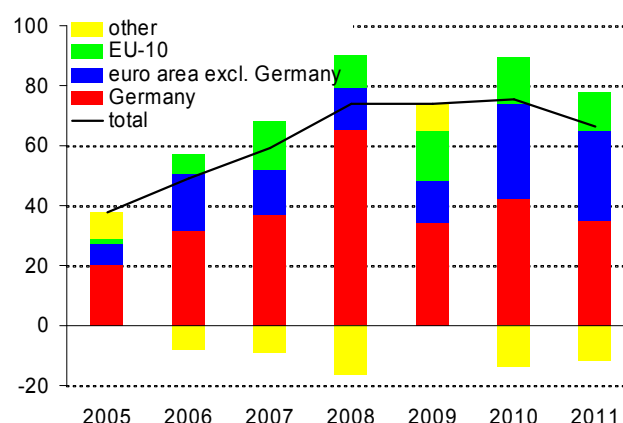


Figure VII-8

Geographical breakdown of the Czech Republic's services balance (CZK billion)



Source: CNB, author's calculations.

2.2 Trade between the Czech Republic and Germany

The Czech Republic's credits from services exports to Germany accounted for almost 28% of total credits and, together with credits from exports to Slovakia, were clearly the highest of all countries. From 2007 onwards, they were fundamentally affected by other services: other business services and, specifically, merchanting and other trade-

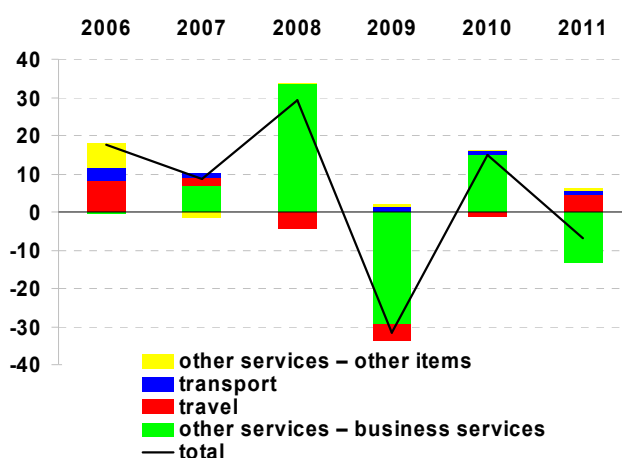
⁹ In 2011, services exports to the EU-27 and the euro area accounted for 74.6% and 60.3% of total credits respectively.

¹⁰ The euro area excluding Germany recorded the highest average annual absolute increase in services exports of the groups of countries presented in Figure VII-7. Its increases after 2008 also most strongly offset the considerably lower credits from exports to Germany. The decrease in total credits in 2009 was due solely to a sharp drop in credits from Germany, while services exports to the other groups of countries continued to rise.

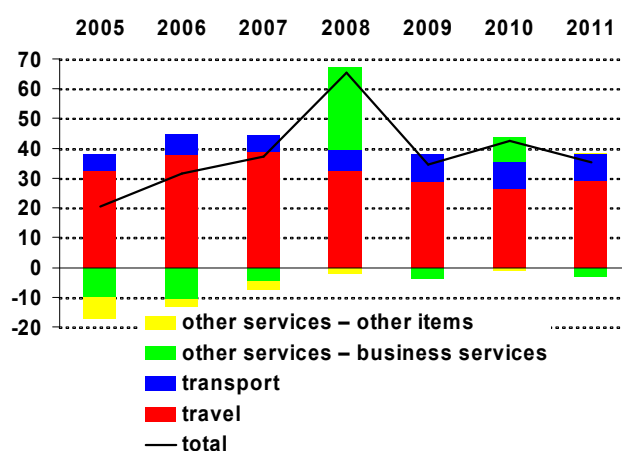
related services.¹¹ The huge rise in credits in 2008 and their sharp decline in 2009 were related to this sub-item. As Figure VII-9 shows, other business services/merchancing also significantly affected total credits in the subsequent two years. From this perspective, the moderation in surplus in 2009 does not appear to be a general trend, but is basically a correction of previous excessive growth in a single sub-item.¹² Thus, the crisis is most visibly reflected in credits from, and the balance of, miscellaneous business, professional and technical services, as well as travel, which is the crucial balance (surplus) in services trade between the Czech Republic and Germany (see Figure VII-10).

Figure VII-9

Annual changes in the Czech Republic's credits from services exports to Germany (CZK billions)

**Figure VII-10**

The Czech Republic's services balance with Germany (CZK billions)



Source: CNB, author's calculations.

2.3 Trade with BRICS

Although services trade turnover with the BRICS group accounted for only 5.4% of total services trade turnover, the overall balance with the BRICS countries has been contributing significantly to the decline in the Czech Republic's overall services surplus in recent years. In 2006, the balance with BRICS switched to a deficit, which quickly widened. As with the trade balance, the overall deficit was determined by the deficit with China, which was linked with a rise in debits from transport connected with growing imports of goods from China. The overall deficit was also significantly affected by the balance with Russia (see Figure VII-11). On the credit side, the most important item was credits from Russia, especially travel credits. However, overall credits from Russia were very volatile as a result of fluctuations in the value of merchancing within other services, probably due mainly to oil and natural gas transactions. After 2007, this item was also the largest factor affecting the overall services balance with Russia, and its evolution was closely connected with the switch of the balance from deficit to surplus in 2009. On the debit side, the main items were debits vis-à-vis China (mainly road

¹¹ These are basically payments and credits for goods purchased by a resident from a non-resident and then sold to another non-resident. During these operations, the goods do not enter internal circulation in the Czech Republic.

¹² Following the transfer of merchancing to the trade balance under the new BPM6 methodology, movements in the credits and surplus of the Czech Republic's services balance with Germany will become very trivial (unless they are significantly influenced by the inclusion of processing).

transport) and Russia (mainly pipeline transport), which were of about the same size and followed a visible upward trend from 2006 onwards (see Figure VII-12).

Figure VII-11

The Czech Republic's services balance with BRICS (CZK billions)

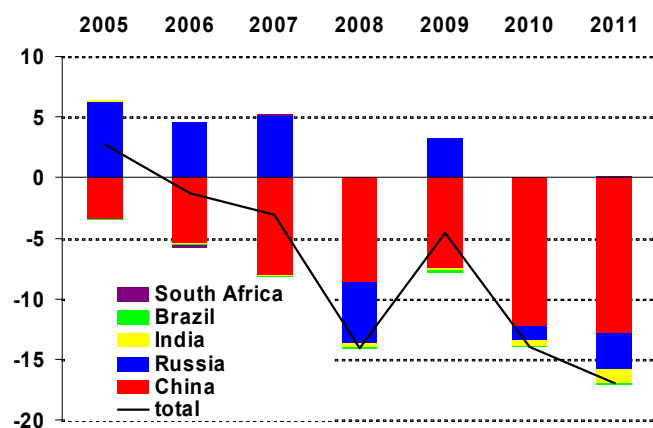
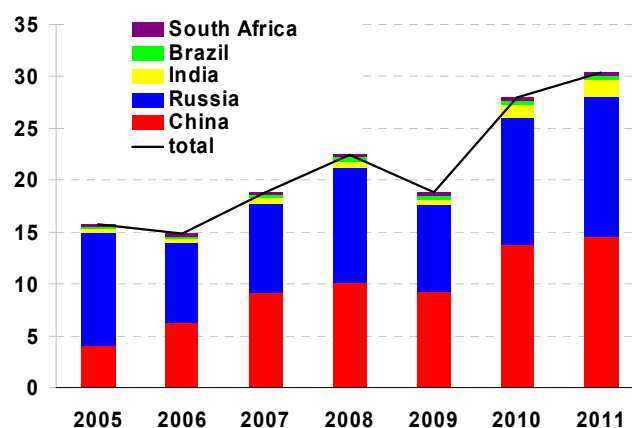


Figure VII-12

The Czech Republic's services debits vis-à-vis BRICS (CZK billions)



Source: CNB, author's calculations.

Conclusion

Despite the often very different trends in the services balances of the countries and regions presented, some common features can be identified in the period analysed. First, a general decrease in the services turnover did indeed occur during the global economic contraction in 2009, affecting both credits and debits. In absolute terms, this decrease was the largest in the case of the euro area. The decline in total credits and the deterioration of the balance (surplus) in absolute terms was linked to the largest extent with the travel balance, specifically private travel. Compared to the pre-crisis period, the movements in the services balance after 2009 were more mixed with regard to both regions and individual countries. This was due to uncertainty surrounding future economic developments (especially the relatively slow recovery in travel surplus growth in advanced economies) and to differences in the scope and impacts of fiscal stimuli (above all improvements in the other services balances of advanced market economies). Developments in the euro area and the USA were broadly similar owing to their strong mutual links and close economic levels, while the individual and aggregate services balances of the BRICS countries showed very different trends after 2009. However, rapid growth in private travel debits and an increase in other services debits point to sizeable growth potential of these countries, indicating modernisation and restructuring of their economies and simultaneously supporting growth in credits in advanced market economies. In 2011, the global services balance probably exceeded its pre-crisis turnover, as suggested by available partial data. The services balance of the USA exceeded its pre-crisis turnover in 2010, and the services balance of the euro area did likewise a year later.

BOFIT	Bank of Finland Institute for Economies in Transition
BR	Brazil
BRIC	Brazil, Russia, India and China
CB-CCI	Conference Board Consumer Confidence Index
CB-LEII	Conference Board Leading Economic Indicator Index
CBOT	Chicago Board of Trade
CF	Consensus Forecasts
CN	China
CNB	Czech National Bank
DBB	Deutsche Bundesbank
DE	Germany
EA	euro area
EC	European Commission
ECB	European Central Bank
EC-CCI	European Commission Consumer Confidence Indicator
EC-ICI	European Commission Industrial Confidence Indicator
EIU	The Economist Intelligence Unit database
ES	Spain
EU	European Union
EUR	euro
EURIBOR	Euro Interbank Offered Rate
Fed	Federal Reserve System (the US central bank)
FRA	forward rate agreement
GBP	pound sterling
GDP	gross domestic product
GR	Greece
CHF	Swiss franc
ICE	Intercontinental Exchange
IE	Ireland
IFO	Institute for Economic Research
IFO-BCI	IFO – Business Climate Index
IFO-CCI	IFO – Consumer Confidence Index
IMF	International Monetary Fund
IN	India
IRS	Interest rate swap
IT	Italy
JP	Japan
JPY	Japanese yen
LIBOR	London Interbank Offered Rate
N/A	not available
OECD	Organisation for Economic Co-operation and Development
OECD-CLI	OECD Composite Leading Indicator
PT	Portugal
RU	Russia
UoM	University of Michigan
UoM-CSI	University of Michigan Consumer Sentiment Index
US	United States
USD	US dollar

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