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WORLD ECONOMIC
SURVEY

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ifo World Economic Climate Remains Positive

NOTES

The World Economic Survey (WES) assesses worldwide economic trends by polling transnational as well as national organisations worldwide on current economic developments in their respective countries. Its results offer a rapid, up-to-date assessment of the economic situation prevailing around the world. In *July 2017, 1,123* economic experts in *121* countries were polled.

METHODOLOGY AND EVALUATION TECHNIQUE

The survey questionnaire focuses on qualitative information: assessments of a country's general economic situation and expectations regarding key economic indicators. It has proven a useful tool, since it reveals economic changes earlier than conventional business statistics.

The qualitative questions in the World Economic Survey have three possible categories: "good / better / higher" (+) for a positive assessment resp. improvement, "satisfactory / about the same / no change" (=) for a neutral assessment, and "bad / worse / lower" (−) for a negative assessment resp. deterioration; For the time t for each qualitative question and for each country the respective percentage shares (+), (=) and (−) are calculated. The balance is the difference between (+)- and (−)-shares. As a result, the balance ranges from -100 points and +100 points. The mid-range lies at 0 points and is reached if the share of positive and negative answers is equal.

The economic climate is a mean of the balances of the present economic situation and the economic expectations.

The survey results are published as aggregated data. For aggregating the country results to country groups or regions, the weighting factors are calculated using the gross domestic product based on purchasing-power-parity of each country.

ifo World Economic Climate Remains Positive

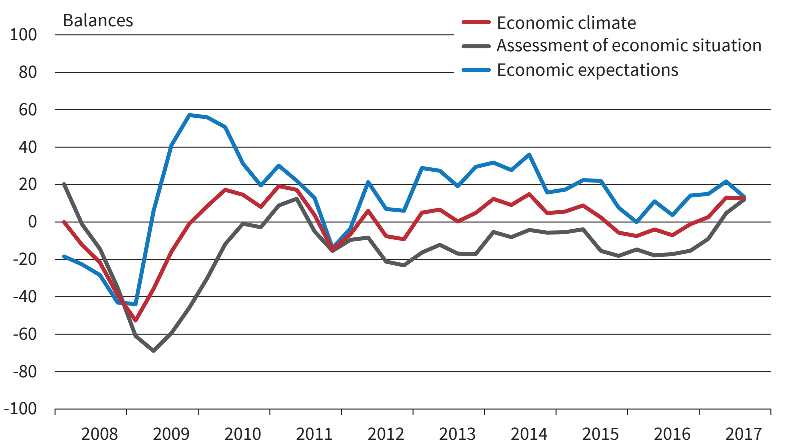
The ifo World Economic Climate remains positive in the third quarter of 2017. Experts assessed the current economic situation far more positively than in April but were slightly less optimistic about the months ahead. The world economy is expected to continue to recover at a slightly slower pace in the coming six months (see Figures 1 and 2).The economic climate improved somewhat primarily in the advanced economies, and especially in the euro area. The United Kingdom was the only country to experience a slump, from plus 4.7 balance points to minus 46.3 points. Emerging and developing economies also had a dampening effect. Economic expectations clouded over in nearly all regions of the world. In the advanced economies, however, the economic situation in the third quarter of 2017 was assessed more favourably than three months ago (see Figure 2). Price increases in the world economy are expected to slow down somewhat in the months ahead. Although most experts still expect short and long-term interest rates to rise, a slightly lower number expect an interest rate increase. Above all, experts expect world trade to pick up considerably over the next six months (See Box 2).

ADVANCED ECONOMIES STABILISE AT A FAVOURABLE LEVEL

The economic climate in advanced economies improved somewhat (see Figure 8). Economic sentiment was assessed far more favourably than last quarter, but the economic expectations clouded over somewhat (see Figure 2). Especially the **Euro Area** contributed to the continuation of the bright economic climate in the advanced economies. The ifo Economic Climate in the Euro Area improved from 26.4 to 35.2 balance points, reaching its highest level since autumn 2000. Assessments of the current economic situation were particularly more favourable than last quarter, but the six-month outlook also brightened. Economic growth is expected to continue in the second half of 2017. The major economies of the Euro area (**Germany**, **France**, **Italy**, and **Spain**) and **Ireland** saw their economic situation and expectations improve. Expectations improved most sharply in France, but differences persist in terms of assessments of the current economic situation. Survey participants almost unanimously assessed the current economic situation in Germany as good. Fairly positive assessments also prevailed in Spain. In France and Italy, experts described the

Figure 1

ifo World Economic Climate

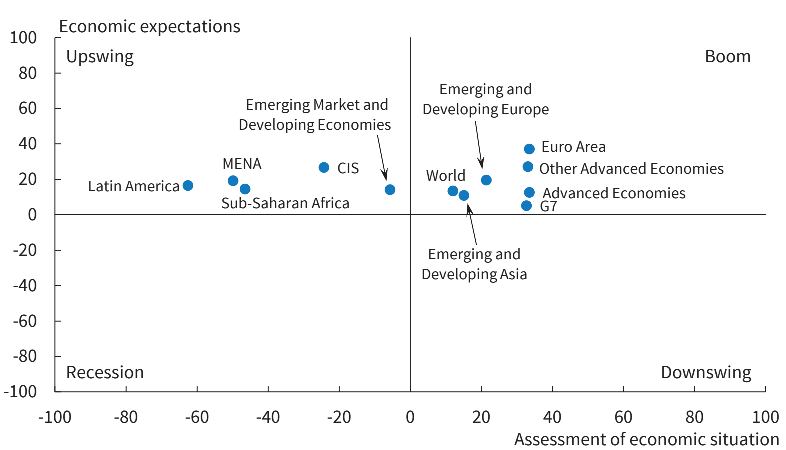


Source: ifo World Economic Survey (WES) III/2017. © ifo Institute

Figure 2

ifo Business Cycle Clock: Snapshot of Selected Aggregates

Balances



Source: ifo World Economic Survey (WES) III/2017. © ifo Institute

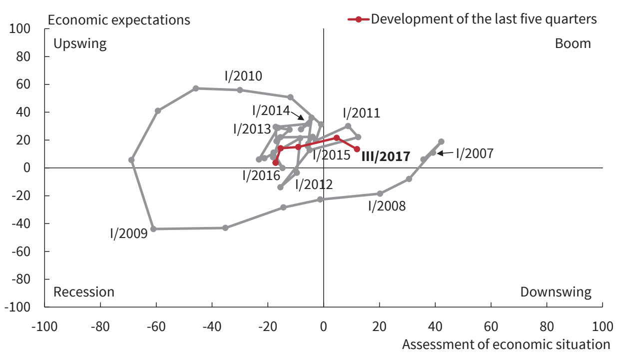
Box 1

IFO BUSINESS CYCLE CLOCK FOR THE WORLD ECONOMY

A glance at the ifo Business Cycle Clock, showing the development of the two components of the economic climate in recent years, can provide a useful overview of the global medium-term forecast. The business cycle typically proceeds clockwise in a circular fashion, with expectations leading assessments of the present situation.
According to the July survey, the ifo Indicator for the world economy deteriorated somewhat. Though the experts assessed the current economic situation as more positive, the economic expectations were downwardly revised. As a result, the indicator moved slightly downward towards the downswing quadrant, but remained in the boom quadrant. The World Climate should continue to recover, albeit at a slower pace.

Figure 3

ifo Business Cycle Clock World Economy
Balances



Source: ifo World Economic Survey (WES) III/2017. © ifo Institute

The ifo World Economic Climate is the arithmetic mean of the assessments of the current situation and economic expectations for the next six months. The correlation of the two components can be illustrated in a four-quadrant diagram ("ifo Business Cycle Clock"). The assessments on the present economic situation are positioned along the abscissa, the responses on the economic expectations on the ordinate. The diagram is divided into four quadrants, defining the four phases of the world business cycle. For example, should the current economic situation be assessed as negative but expectations as positive, the world business cycle is in an upswing phase (top left quadrant).

current economic situation as not yet satisfactory. The **Netherlands**, **Portugal** and **Estonia**, in turn, saw an improvement in their economic climate, as the current situation was assessed more favourably. At the same time, WES experts' economic expectations in these countries, although optimistic, were adjusted slightly downward. The economic climate indicator in **Finland** saw a remarkable jump from 32.1 to 52.3 balance points. This is the highest value since autumn 2007. Assessments of both investment and consumption were higher. In addition, the Finnish experts almost unanimously expect the volume of imports and exports to increase in the coming six months. This signals a further economic recovery in Finland.

Experts in the Euro Area in general scaled back their inflation expectations for 2017 somewhat to 1.5 percent (see Table 1). Survey participants expect interest rates to rise over the next six months both in the short term and particularly in the long term. After the euro's appreciation against the US dollar last quarter, experts expect little fluctuation in the exchange rate over the next six months. In addition, banks were far more willing to grant companies credit in the quarter under review (especially in France) and survey participants now describe lending as less restrictive (see Table 3).

For the remaining **G7** countries, the **United Kingdom** saw a drastic decline in its economic climate indicator as both the present economic situation and the economic outlook were more negatively assessed than in the previous survey (see Figure 8.2). The prolonged uncertainty about Brexit is resulting in declining confidence in the UK's economy. Experts assess both investment and consumption as very negative without any indication of improvement in the coming six months. Experts scaled back their inflation expectations for 2017 as well as for 2022 to 2.6 and 2.7 respectively (see Table 1). This is the first time since the third quarter of 2016 that the experts lowered their inflation expectations. This can be partly attributed to declining oil prices. A decreasing number of WES experts assess the dollar and the euro as overvalued compared to the British pound. The Japanese yen on the other hand is now assessed as overvalued vis-à-vis the pound. In the **United States** the current economic situation was assessed as more favourable than in the last survey, however it is the first time since the first quarter of 2009 that the expectations turned negative (-6.9 on the balance scale) (see Figure 8.2). Inflation rates for 2017 were downwardly revised to 2.0 from 2.3 in the previous survey (see Table 1). The three main currencies, euro, British pound, and the Japanese yen are currently being assessed as undervalued compared to the dollar. As in the Euro Area, WES experts in the US indicate that banks are far more willing to grant credit to companies. Only 20.7% of the US WES experts describe lending as restrictive (see Table 3). The economic climate in **Japan** remained on its recovery track as WES experts upgraded their assessments of both the current economic situation as well as the economic outlook (see Figure 8.1). Both investment and consumption are reported as more favourable than in the previous survey. According to the results of the quarter under review, fewer WES experts expect the Bank of Japan to increase its low interest rates. However, the supply of bank credit to firms is still constrained according to 37.9% of the WES experts (see Table 3).

Among the **Other Advanced Economies**, the **Czech Republic** saw its climate indicator rise to 68.3 on the balance scale, reaching its highest level since 1996 (see Figure 8.1). All experts in the Czech Republic assessed the current situation as good, reaching 100 on the balance scale. Economic expectations remained also high. All four main currencies are slightly overvalued against the Czech Koruna, which is reflected in the expectations for exports, which are seen to increase in the coming six months. **Switzerland** as well saw its eco-

Table 1

Inflation Rate Expectations for 2017 and in 5 Years (2022)

Aggregate*/Country	2017	2022	Country	2017	2022
Average of countries	**3.4**	**3.5**	Brazil	3.8	3.9
EU 28 countries	1.7	2.3	Bulgaria	2.0	2.5
Euro area a)	1.5	2.1	Cabo Verde	1.4	2.4
			Chile	2.4	3.0
Advanced Economies	**1.7**	**2.3**	China	1.8	2.9
Australia	2.1	2.7	Colombia	4.4	3.5
Austria	1.9	2.3	Croatia	1.6	2.6
Belgium	2.1	2.0	Dem. Rep. of the Congo	42.0	17.0
Canada	1.9	2.3	Ecuador	1.5	3.0
Czech Republic	1.9	2.2	Egypt	27	8.3
Denmark	1.1	1.7	El Salvador	2.9	4.1
Estonia	3.1	2.2	Georgia	5.7	4.3
Finland	1.1	1.8	Guatemala	4.4	4.8
France	1.3	2.0	Hungary	2.4	2.9
Germany	1.6	2.1	India	4.5	4.3
Greece	1.1	1.8	Kazakhstan	7.8	5.1
Hong Kong	2.4	2.7	Kenya	9.5	7.8
Ireland	0.9	1.8	Kosovo	2.4	1.5
Israel	1.9	2.8	Lesotho	5.4	5.3
Italy	1.3	2.1	Malaysia	3.9	4.7
Japan	0.6	1.4	Mexico	5.9	3.7
Latvia	2.4	2.8	Morocco	2.0	2.6
Lithuania	2.7	2.3	Namibia	6.6	7.3
Netherlands	1.4	2.0	Nigeria	16.8	11.3
New Zealand	1.8	2.2	Pakistan	5.9	7.1
Norway	2.1	2.3	Paraguay	3.8	3.9
Portugal	1.4	2.1	Peru	3.0	3.0
Republic of Korea	1.9	3.0	Poland	1.9	2.5
Slovakia	1.3	2.6	Romania	1.6	3.5
Slovenia	1.7	2.6	Russian Federation	5.6	7.7
Spain	1.9	2.3	South Africa	5.7	6.0
Sweden	1.7	3.1	Sri Lanka	6.6	6.0
Switzerland	0.5	1.3	Sudan	27.3	18.0
Taiwan	1.1	1.4	Thailand	1.3	2.4
United Kingdom	2.6	2.7	Togo	1.8	2.5
United States	2.0	2.6	Tunisia	6.0	4.8
			Turkey	9.6	6.0
Emerging market and developing economies	**4.9**	**4.5**	Ukraine	9.0	6.7
Argentina	23.6	8.5	Uruguay	6.9	7.6
Bangladesh	5.7	5.5	Venezuela	---	---
Bolivia	4.7	8.1	Zambia	7.2	6.6
Bosnia and Herzegovina	1.3	3.5	Zimbabwe	4.9	7.0

* To calculate aggregates, country weights are based on gross domestic product based on purchasing-power-parity (PPP) in international dollars (database IMF's World Economic Outlook). – a) Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Portugal, Spain, Slovenia, Slovakia.
Source: ifo World Economic Survey (WES) III/2017.

nomic climate improve, to 54.8 points (see Figure 8.2). Assessments of the current situation as well as economic expectations were very good. The trade balance is expected to improve considerably in the coming six months; this is in line with our aggregated World Trade Volume indicator (see Box 2). Of the four main currencies, the US dollar is assessed to be slightly overvalued and a declining number of experts expect the dollar to rise further. **Israel** saw its economic climate indicator drop by 19.8 points to 8.2 on the balance scale. This still means that trend economic growth is continuing. Economic expectations indicate a similar pattern for the coming months. Expected inflation for the short and long term was upwardly revised to 1.9 and 2.8 respectively (see Table 1). WES experts judged the value of the four main currencies compared to the Israeli shekel as weaker than in the previous survey. This results in the euro, yen and pound being assessed as undervalued and the dollar as at its proper value. **Australia** saw a small uptake in its economic climate as expectations brightened. The current economic situation was less favourably assessed after four consecutive quarters of increasingly positive assessments. A structural problem seems to be a lack of capital expenditures, as

Box 2.1

A COMPARISON OF THE CPB WORLD TRADE MONITOR AND THE IFO WORLD TRADE INDICATOR

The **CPB World Trade Monitor** (WTM) is a well-known monthly indicator that monitors developments in global international trade (trade in goods, also called merchandise trade)*. Calculated by the CPB Netherlands Bureau for Economic Policy Analysis (CPB), the indicator is based on official statistics from, for example, Eurostat, IMF, OECD, UN, and the World Bank. The WTM underlies some revision because of preliminary data and has a delay of two months, as official statistics take longer to be published. This means that the data of June (the last month of the second quarter) will be published at the end of August.

The **ifo World Economic Survey** (WES) asks its experts to evaluate *expected foreign trade volume*, for exports and imports separately. To make this data compatible with the WTM, we calculate the ifo World Trade Indicator, based on the mean of the time series of imports and exports. The delay for the WES is only two weeks, i.e. for the third quarter the survey was conducted in July and the results are published in early August. There are no revisions.

Figure 4

International Trade Volume

a The quarter are calculated by the sum of respective months.
Source: ifo World Economic Survey (WES); CPB Netherlands Bureau for Economic Policy Analysis (CPB). © ifo Institute

To compare the two time series, we decided to convert the monthly WTM series into quarterly frequency data, by adding together the months of the respective quarter. Because the WES experts are asked for their expectations in the change of world trade volume, we calculate the rate of change from quarter to quarter. The calculated data of the WTM and the ifo World Trade Indicator are presented in Figure 4.

A first visual comparison shows there is a link between the two time series (see Figure 4). This suggests that the WES experts have a good idea of the developments in international trade volume in their respective countries.

To get a more official comparison, we use a cross-correlation to determine the correlation between the two time series. In general, a cross-correlation is a measure of similarity of two time series as a function of the time lag of one relative to the other. The resulting correlation coefficients are located in an interval between -1 and +1. A high coefficient stands for a high statistical

*See Jos Ebregt, The CPB World Trade Monitor: Technical description, CPB Back-ground Document, September 2016.

assessments have remained unfavourable since the second quarter of 2014. Of the four main currencies, the euro and the British pound are assessed to be overvalued, the dollar and the Japanese yen were seen to be at their proper value. No further fluctuation is expected for the dollar. The expected inflation rate for 2017 was slightly upwardly revised from 2.0 to 2.1 in the quarter under review; long-term interest rates stayed the same (see Table 1). The **Asian Tigers**[1] also saw considerable improvements in the two components of the economic climate (see Figure 7.1). Inflation expectations were adjusted only slightly: for 2017 experts now expect an inflation rate of 1.6% or 0.2% lower than the previous survey. In 2022 an inflation rate of 2.3% is foreseen (see Table 1).

EMERGING AND DEVELOPING ECONOMIES PROJECT SLOWER RECOVERY

The climate for Emerging and Developing Economies continues to remain positive for the second quarter in a row. The current situation was judged to have improved compared to the previous survey, but remained negative. The economic outlook on the other hand dropped by 8 points but remained positive (see Figure 2). Trade is also expected to pick up in these countries, as both the volumes of imports and exports are seen to be higher in the coming six months (for a comparison of the ifo World Trade indicator with the World Trade Monitor of the CBP see Box 2). 73% of the WES experts report that banks continue to be restrictive in providing bank credit to firms.

For the main emerging markets (**Brazil**, **Russia**, **India** and **China – the BRICs**) the economic climate remained above the zero line with 4.9 on the balance scale, however economic expectations declined considerably. This decline is mainly due to the worsening of the already unfavourable climate in **Brazil** that dropped by 20 points to -41.0 on the balance scale, as economic outlook clouded over considerably (see Figure 9). This is likely due to the political unrest Brazil is facing at the moment. The current prime minister, who took office in 2016 after impeachment of his predecessor, is now himself facing potential trials from the Supreme Court. But there are sources of optimism: WES experts' assessments of the trade balance have been improving for three quarters in a row. Inflation, in the short and medium term, was downwardly revised to 3.8 and 3.9, respectively (see Table 1). **China's** present economic situation remains satisfactory for the moment. However, its economic climate dipped beneath zero on the balance scale, as economic expectations fell to -10.4 points (see Figure 9). Whereas assessments of capital expenditures declined, private consumption was more positively assessed in the quarter under review.

[1] Hong Kong, Singapore, Korea and Taiwan.

WES experts expect prices to decrease in the coming six months, and inflation rates for 2017 and 2022 were revised accordingly to 1.8 (decline of 0.5) in 2017 and to 2.9 (decline of 0.1) in 2022. Experts reported a downward fluctuation for all four currencies, with especially the euro and the dollar to be slightly undervalued compared to the Chinese yuan. Of the BRIC countries, only in **India** did the economic climate remain very favourable at 46.3 balance points. Both investment and domestic consumption were better assessed than in the previous survey. The trade deficit is expected to increase somewhat, as imports are seen to rise somewhat higher than exports. However, both will increase in volume. India's WES experts downwardly revised their expectations for inflation in 2017 from 5.3% to 4.5% in this survey. Inflation expectations for 2022, however, were set at 4.3% – this being only 0.1% higher than in the previous survey. In **Russia** the hesitant recovery that started at the beginning of 2016 continues (see Figure 9.2). The present situation and economic outlook for the country saw little fluctuation. However, the continued sanctions against Russia from the US and Europe are having an effect on its trade balance. Experts expect the trade deficit to worsen and both the volumes of imports and exports to decrease. The assessments of the four main currencies fluctuated downwards; especially the euro and the dollar were seen to be undervalued.

Other Emerging Markets

Other aggregates of emerging and developing economies showed different contributions to the economic climate (see Figure 2). **Emerging and Developing Europe** saw a 21.3 increase in its economic climate indicator (see Figure 7). Both the current economic situation as well as the economic outlook was more positively assessed than previous survey. **Emerging and Developing Asia** improved considerably in the last survey; now, however, there is a slightly less optimistic view of the coming six months. This caused a small drop in the climate indicator; however, it still sits comfortably at 13.0 on the balance scale. The countries in the **Middle East and North Africa** together have a positive economic outlook for the first time in 10 quarters. The present economic situation, however, remained subdued. **Latin America** saw no improvements in its unfavourable present economic situation and economic outlook.

The drop in the economic climate of **Emerging and Developing Asia** is mainly caused by the **ASEAN-5** countries (see Figure 7). Both the current economic situation and the economic outlook were less favourably assessed than previous survey, causing its economic climate indicator to drop to -20.6 points. The ASEAN-5 group was established in August 1967 and is celebrating its 50th anniversary. The inflation rate in these countries is expected to stay at 4.0% in 2017 and was slightly downwardly revised for the 2022 forecast, namely to 4.1% (see Table 1).

Box 2.2

link between the two time series. A zero identifies non-correlation. We check the cross-correlation between the ifo World Trade Indicator and the rate of change of the quarterly WTM. We first calculate the correlation between the two time series simultaneously, without any time adjustment (i.e. we compare the same quarters of both time series). Second, to identify WES as a leading indicator to the WTM, the cross-correlation coefficient from WES in the current quarter to WTM of next quarter will be calculated. Third, to check if the WES has a delay, the cross-correlation coefficient from WES in the current quarter to WTM of previous quarter will be calculated. The results are presented in Table 2.

Table 2

Cross-correlation coefficients

Simultaneous	0.70
Lead of one quarter	0.28
Delay of one quarter	0.76

Source: ifo World Economic Survey (WES); Netherlands Bureau for Economic Policy Analysis (CPB).

The correlation coefficient, without any time adjustment, is 0.70. This means that WES shows a good correlation with the WTM when testing the time series simultane-ously. The cross-correlation coefficient of lead, if WES is a leading indicator with one quarter, is 0.28 and the lowest coefficient in this comparison. The correlation that tests whether WES will explain the WTM with one quarter delay has a coefficient of 0.76.

The statistical analysis reinforces the insights gained from plotting the two series. WES has a good synchronism with WTM in the same period and the weakest if WES is used as a predictor for the WTM. The correlation is also high when correlating WES with one quarter delay to the WTM. This is a good result for the WES when we con-sider the publication dates of both time series. The current WES, which takes into account the economic developments of Q3, is published in early August with its sur-vey conducted in July. The WTM publishes the data for July at the end of September. This difference will increase even further when one is interested in quarterly data, as the WTM completes its third quarter (September) only at the end of November. In this case the WES survey has an advantage of three months.

In **Emerging and Developing Europe,** the main six countries (**Bulgaria**, **Croatia**, **Hungary**, **Poland**, **Romania**, **and Turkey**) saw an improvement in their economic climate. The biggest difference was seen in **Turkey**, as the climate after two unfavourable quarters turned positive with 7.7 balance points. Volumes in imports and exports are expected to pick up in the coming 6 months and expected inflation rates were downwardly revised. For 2017 WES experts now expect an inflation rate of 9.6% (in previous survey 9.8%) and for 2022 inflation rates have been revised from 7.8% to 6.0% (see Table 1). All the major currencies are now

Table 3

Supply of bank credit to firms

Percentage of experts who report moderately or strongly constraints	
Democratic Republic of the Congo	100.0
Kazakhstan	100.0
Kenya	100.0
Nigeria	100.0
Slovenia	100.0
Sudan	100.0
Tunisia	100.0
Zimbabwe	100.0
Portugal	95.2
Italy	94.6
Greece	93.3
Ireland	90.9
Russian Federation	88.2
Cabo Verde	87.5
Chile	85.7
China	85.7
Togo	85.7
Bolivia	83.3
Latvia	81.8
India	80.0
Malaysia	80.0
Thailand	80.0
Ukraine	80.0
Zambia	80.0
Romania	77.3
Spain	74.4
Netherlands	72.2
Paraguay	71.4
Argentina	68.8
Croatia	66.7
Namibia	66.7
South Africa	66.7
Brazil	64.0
Austria	62.5
New Zealand	62.5
Bulgaria	61.5
Hungary	61.5
Lithuania	60.0
Mexico	58.3
Slovakia	57.1
Georgia	50.0
Lesotho	50.0
Peru	50.0
United Kingdom	47.4
Turkey	46.2
Colombia	45.5
Pakistan	45.5
Belgium	42.9
Germany	39.0
France	38.1
Japan	37.9
Poland	36.8
Australia	35.7
Czech Republic	33.3
Israel	33.3
Sri Lanka	33.3
Finland	31.8
Republic of Korea	30.8
Canada	30.0
Uruguay	25.0
Sweden	22.2
United States	20.7
Norway	20.0
Switzerland	20.0
Taiwan	16.7

Only countries with more than four responses were included in the analysis

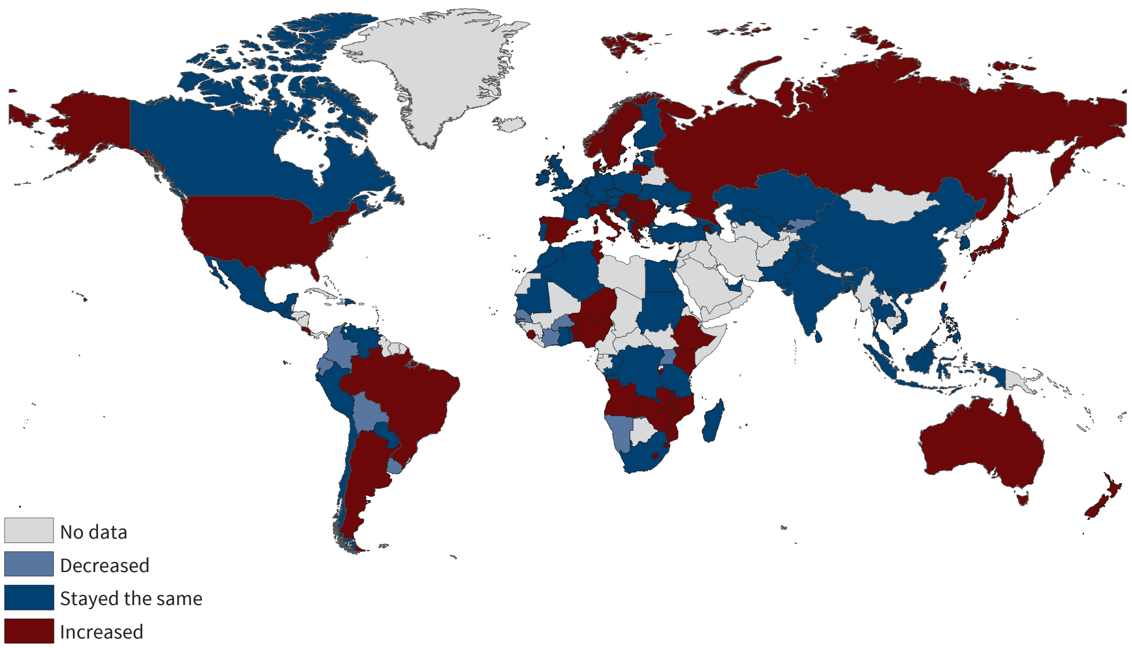
Source: ifo World Economic Survey (WES) III/2017.

assessed as undervalued compared to the Turkish lira. The best economic climate from emerging and developing Europe prevails in **Poland** (see Figure 9.2). The present economic situation is now assessed as very favourable at 52.4 points, and further improvements are expected in the next 6 months. The volume in trade for the coming months is also projected to be favourable. Inflation rates were revised slightly downward (see Table 1). In addition, banks were far more willing to grant companies credit as only 36.8% of the survey participants in Poland, compared to 81% in the first quarter of 2017, now indicate lending as restrictive (see Table 3). The Polish zloty is assessed at about its proper value against the euro, slightly overvalued to the dollar, and slightly undervalued to the Japanese yen and British pound.

For nine quarters in a row, a negative economic climate has prevailed in **Latin America** (see Figure 7.1). However, **Argentina** has had a satisfactory economic climate for four consecutive quarters. The economic outlook for the coming six months is also very bright. This signals that economic recovery, although slow, remains on track this year. The trade deficit is expected to widen, with increasing volume of imports. All major currencies are judged to be undervalued vis-à-vis the Argentine peso. The majority of WES experts (68.8%) assess banks' credit policies to firms as being restrictive (see Table 3). In **Mexico** economic expectations brightened considerably; even though this had a positive impact on the economic climate in Mexico, it still remains unfavourable at -10.0 on the balance scale. There was some considerable fluctuation in the four main currencies compared to the Mexican peso. As the peso recovered, the WES experts now judge the euro, British pound and the yen at their proper value. Only the dollar is still somewhat overvalued, according to the survey participants. As trade policy with the United States remains uncertain, the expected volume of exports was revised slightly downward. The volume of imports jumped considerably. Also in Mexico, banks are reported to be restrictive in their loans to firms (see Table 3).

The climate of the **Commonwealth of Independent States** after one positive quarter turned slightly negative again. Economic expectations remain positive, although they were downwardly adjusted. After a strong recovery from the last survey, the economic climate in **Ukraine** deteriorated as the assessment of the current situation was more negative and the economic outlook was less optimistic. The supply of loans to firms remains restrictive as 80% of the WES Experts judge the supply of credit from banks to firms to be constrained. In **Georgia** only 50% of the experts reported constraints in the willingness of banks to provide companies with credit (see Table 3). Georgia's economic climate deteriorated somewhat as the economic outlook was slightly less optimistic; however it remains positive. Countries from both the **Middle East and North Africa** and **Sub-Saharan Africa** saw an improvement

Figure 5
Changes in Economic Inequality in the last 5 years



Source: ifo World Economic Survey (WES) III/2017.

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of their economic climate, albeit at a low level. The economic outlook for both aggregates was more favourable assessed as in the last quarter. In **Egypt** both components of the economic climate were more negatively assessed, although the economic outlook remained positive. The volume of exports was again seen to be increasing in the coming six months, whereas imports are expected to decline. All experts reported banks to be restrictive in their supply of credit to firms (see Table 3) and experts are expecting increasing interest rates. Although the inflation rate for 2017 at 27% is quite high, inflation expectations for 2022 were downwardly revised to 8.3% (see Table 1). **Nigeria** saw an improvement in its economic climate as economic expectations brightened considerably. The volume of trade, both for imports and exports, was assessed as increasing in the coming six months. Also in this survey, the supply of bank credit to firms was assessed by all experts as being restrictive (see Table 3).

THE WES SPECIAL QUESTION: ECONOMIC INEQUALITY AROUND THE WORLD

Economic Inequality is a pressing international problem. 72.3% of WES experts in the WES Q2 2017 Survey[2] indicated that widening income inequality is one of the major economic problems their country is facing at the moment. To further explore this issue, and shed some light on experts' perceptions of inequality in their countries and preferred possible remedies, the special question of the WES Q3 2017 focuses on economic inequality.

Increasing Economic Inequality

According to a study by the International Monetary Fund (IMF), the gap between the rich and the poor has increased substantially since 1990 in most of the developed world.[3] In emerging markets and developing countries, although higher in absolute terms compared to developed countries, inequality remained stable on average over the same time period. Some emerging markets and developing economies in Asia and Eastern Europe experienced significant increases, while in others, such as countries in Latin America, inequality decreased.

Technological progress and changes in labour market institutions are, according to the IMF, the key drivers of this development. The IMF argues that skill-biased technological advances account for nearly a third of the widening income gap. New technologies increased the ratio of the wages of skilled to unskilled workers by disproportionately raising the demand for skilled labour over low- and unskilled labour. Increasing labour market flexibility posed further challenges. Notably the decline in the union rate is found to be associated with the rise of the top income shares, while the reduction in the minimum wage relative to the median wage is associated with higher inequality in advanced economies.

To determine whether the WES experts concur with the findings of the IMF, the first question asks whether economic inequality has increased in the country of the

[2] Dorine Boumans, "ifo World Economic Survey May 2017 ", ifo World Economic Survey 16 (2), 2017, 1-20

[3] Dabla-Norris, E., Kochhar, K., Suphaphiphat, N., Ricka, F., & Tsounta, E. (2015). Causes and Consequences of Income Inequality: A Global Perspective. IMF Staff Discussion Note.

Table 4

Does Economic Inequality hinder Economic Growth?

	Not at all	Slightly			Moderately		Extremely
Income	Austria Czech Republic Finland Netherlands Norway Slovenia Sweden Switzerland	Australia Belgium Bolivia Bulgaria Canada Chile China Croatia Estonia France Georgia	Germany Ireland Italy Japan Kenya Latvia Lithuania Malaysia New Zealand Poland Portugal Rep. of Korea	Russia Slovakia Spain Taiwan Thailand Tunisia Turkey United Kingdom United States Uruguay	Argentina Brazil Cabo Verde Colombia Dem. Rep. Congo Dominican Rep. Greece Hungary India Israel Kazakhstan Lesotho	Mexico Namibia Nigeria Pakistan Paraguay Peru Romania Serbia Sri Lanka Togo Ukraine Zambia Zimbabwe	South Africa
Wealth	Czech Republic Finland Netherlands Norway Slovenia Sweden Switzerland	Australia Austria Belgium Bolivia Bulgaria Canada Chile China Croatia Estonia France	Georgia Germany Greece Hungary India Ireland Italy Japan Latvia Lithuania Malaysia	New Zealand Poland Republic of Korea Russia Slovakia Spain Thailand Tunisia Turkey United Kingdom United States Urugua	Argentina Brazil Cabo Verde Dem. Rep. Congo Guatemala Israel Kazakhstan Kenya Lesotho Mexico Nigeria	Pakistan Paraguay Peru Portugal, Romania South Africa Sri Lanka Taiwan Togo Ukraine Zambia Zimbabwe	Colombia Namibia

Source: ifo World Economic Survey (WES) III/2017.

respective experts in the last five years.[4] Figure 5 shows the answers aggregated by country. There are indeed some countries in Latin America for which the experts assume that economic inequality has decreased in the last 5 years. However, the majority of the countries either regard inequality to have stayed the same or increased. When looking at the different regions, note that especially in Southern and Eastern Europe and in Sweden and Norway, WES experts report on average an increase in economic inequality. In Asia, in contrast, WES experts on average report that economic inequality has stayed the same these last five years. Also in the United States, Russia and Australia survey participants report increased economic inequality. Comparing these results with the change of Gini coefficients from 2008 to 2013 of disposable incomes[5], indeed Spain, Italy, and Greece saw an increase in their Gini coefficients. For Norway and Sweden Gini's for disposable income actually decreased. According to the Gini Coefficients economic inequality in most Latin America countries decreased, also in Brazil (with -1.0) and Argentina (with -2.0); however WES experts report an increase for these countries. For the Asian countries, for which Gini data is available, inequality declined mostly, only in Indonesia Gini coefficients measure an increase of inequality. In the United States economic inequality also increased according the change in Gini coefficients; however in Russia and Australia Gini's report a decrease of economic inequality in the years from 2008 till 2013.

[4] The exact question was: "How did economic inequality in your country change in the last 5 years?" The WES experts could choose from five different answer categories: significantly decreased, decreased, stayed the same, increased, significantly increased.

[5] Data used from the SWIID version 5.1 accessed from: http://fsolt.org/swiid/

Inequality and Growth

The relationship between inequality and economic growth is currently hotly debated (see e.g. Fuest, 2017; Fratzscher, 2016).[6] There is no consensus whether inequality increases or decreases growth, nor on the strength of the relationship.[7]

Recent empirical studies find that inequality indeed hinders economic growth. The IMF for example argues that a higher net Gini coefficient, a common measure of inequality that nets out taxes and transfers, is associated with lower output growth over the medium term.[8] The Fund identifies several channels through which inequality can have a negative impact.[9] First, it affects the drivers of growth by depriving the ability of lower-income households to accumulate physical and human capital and by reducing aggregate demand. Second, inequality dampens investment by fuelling economic, financial and political instability. Third, inequality can lead to a backlash against growth-enhancing policies (e.g. protectionist policies against globalisation and market-oriented reforms). The Organization for Economic Cooperation and Development (OECD) recently confirmed the negative impact of inequality on growth.[10] They argue in favour of the *opportunities hypothesis*, i.e. that poor households are unable to invest the optimal amount in education,

[6] Fuest, C. (2017). Inequality Reduces Growth. In B. Frey, & D. Iselin, Economic Ideas You Should Forget (pp. 63 - 64). Springer Verlag; Fratzscher, M. (2016). Verteilungskampf. Warum Deutschland immer ungleicher wird. München: Hanser.

[7] Cingano, F. (2014). Trend in Income Inequality and its Impact on Economic Growth. OECD Social, Employment and Migration Working Papers No. 163. A recent meta-analysis of 28 studies on the empirical relationship between inequality and growth finds partly positive and partly negative correlations. Their results suggest that there is no robust empirical relationship, see Neves, P. C., Afonso, Ó., Tavares Silva, S. (2016). A meta-analytic reassessment of the effects of inequality on growth. World Development, S. 386-400.

[8] Ostry, J., Berg, A., & Tsangarides, C. (2014). Redistribution, Inequality, and Growth. IMF Staff Discussion Note.

[9] Dabla-Norris et al., 2015.

[10] See footnote 7.

Table 5

Instruments Governments should use to Tackle Economic Inequality*

Regions	Euro Area and/or G7	Other Advanced Economies	CIS	Developing Asia	Developing Europe	Latin America	MENA	Sub-Saharan Africa
Tax system	64.1	59.3	53	26.8	65.1	57.9	63.2	62
Labour market regulations	33.4	28.5	34.8	34.8	48.1	46	26.3	43
Improving the education system	68.5	57.7	57.6	32	77.4	86.5	42.1	79.3
Introduction of a basic income	12.2	8.9	10.6	13.1	14.2	9.5	21.1	26.6
Increase in the minimum wage	19.8	26	27.3	13.1	33	11.1	36.8	31.4

* The results indicate percentage of experts indicating that their government should use these instruments to tackle economic inequality
Source: ifo World Economic Survey (WES) III/2017.

which harms future incomes and results in slower growth compared to the counterfactual growth with optimal education levels.

However, the validity of these empirical findings is not unchallenged. With respect to the study by the OECD, replications with alternative data sources showed that the results are highly sensitive to model specifications.[11] Considering a sample of developed and developing economies, Kolev and Niehues[12] find a negative effect on growth only for less-developed countries and no significant or rather a positive effect otherwise. This follows in part the arguments of the *incentives hypothesis*; differences in income incentivise people to work harder and study longer (amongst others), which has a positive impact on growth.[13] Without the benefit of financial rewards there is less incentive for risky entrepreneurship or innovation. This is then especially the case for developed countries.

To assess the opinion of WES experts on whether economic growth in their country is hindering their economy, we asked them to judge whether income or wealth inequality is hindering growth in their respective countries. Table 4 shows the average of the WES experts' answers for income inequality for their respective countries. This analysis seems to confirm the findings by Kolev and Niehues, where negative effect of income inequality was found for developing countries only. The averaged assessments of WES experts for most advanced countries are in the "not at all" and "slightly" categories, whereas in the moderately and extremely categories, mostly emerging and developing countries are present. A similar story is found for wealth inequality (see Table 4).

Preferred Instruments to Tackle Inequality

Most advanced economies rely on ex-post redistribution policies to mitigate inequality, notably via progressive taxes and social transfers. Other possibilities include regulating the labour market, increasing the minimum wage, improving the education system and strengthening unions. In some countries, such as Germany, Switzerland or Finland, the introduction of an unconditional basic income is being discussed in the media (Switzerland held a constitutional referendum on the introduction of an unconditional basic income in 2016). While some policies aim to redistribute resources (e.g. taxes and transfers), others try to improve equality of opportunity, e.g. by improving the education system. To get an idea on what is mostly preferred by economic experts, the last question asks the WES experts what instruments the government should use to address economic inequality, if any. Table 5 shows the results of this question. According to the WES experts, governments should use the tax system, labour market regulation and improvements in the education system to tackle economic inequality. Introduction of a basic income, although highest in the Middle East and North Africa as well as Sub-Saharan Africa, is in general the least favourable option.

Conclusion

To conclude, economic inequality as assessed by the WES experts has developed differently across the world in the last five years. Only a few countries, according to the WES experts, have seen a decrease in inequality. Interesting is Europe, where especially southern European and Scandinavian countries reported an increase in inequality. This perceived development in Europe is reflects partly actual developments, as measured by the Gini coefficient (with the exception of Sweden and Norway). However, in Latin America economic inequality as measured by the Gini coefficient is decreasing, this is not completely reflected in the WES experts' answers. In addition, in Asia most experts report on average that economic inequality has stayed the same these last five years. However, according to the Gini coefficients there is also a declining trend in this region. Whether economic inequality actually hinders economic growth seems to depend on the level of development. Across all regions, however, the two preferred instruments to tackle economic inequality are the tax system and improving the education system.

[11] Sachverständigenrat. (2015). Jahresgutachten 2015/16; Niehues, J. (2014). Subjective Perceptions of Inequality and Redistributive Preferences: An International Comparison. IW-TRENDS Discussion Papers.
[12] Kolev, G. and J. Niehues (2016), "The Inequality-Growth Relationship: An Empirical Reassessment", IW-Report 7/2016
[13] OECD. (2015). In It Together: Why Less Inequality Benefits All. Paris: OECD Publishing.

Figure 6

Expected Trend for the next 6 Months for Short- and Long-term Interest Rates

Source: ifo World Economic Survey (WES) III/2017.

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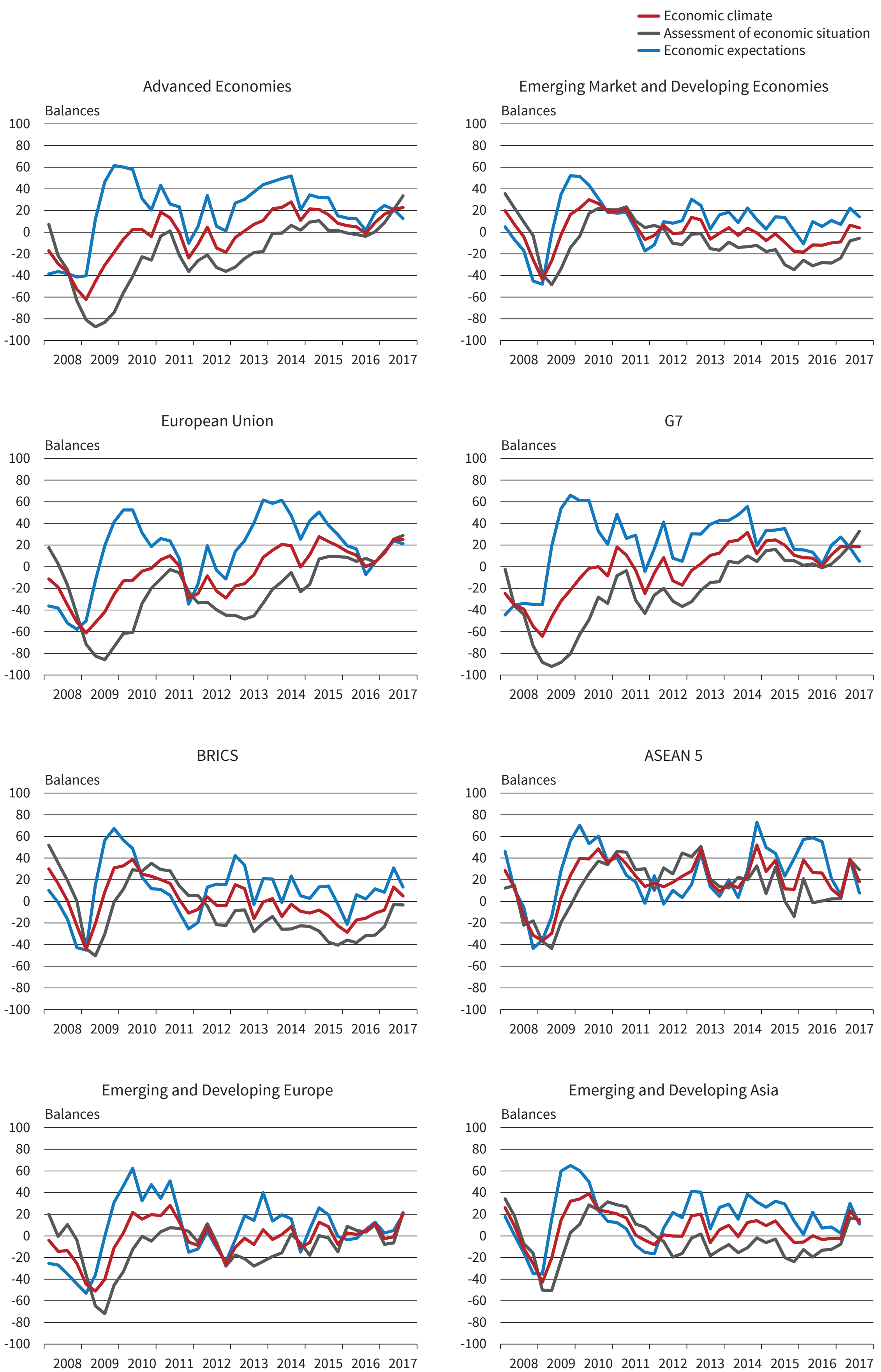
Figure 7.1

Selected Aggregates



Source: ifo World Economic Survey (WES) III/2017.

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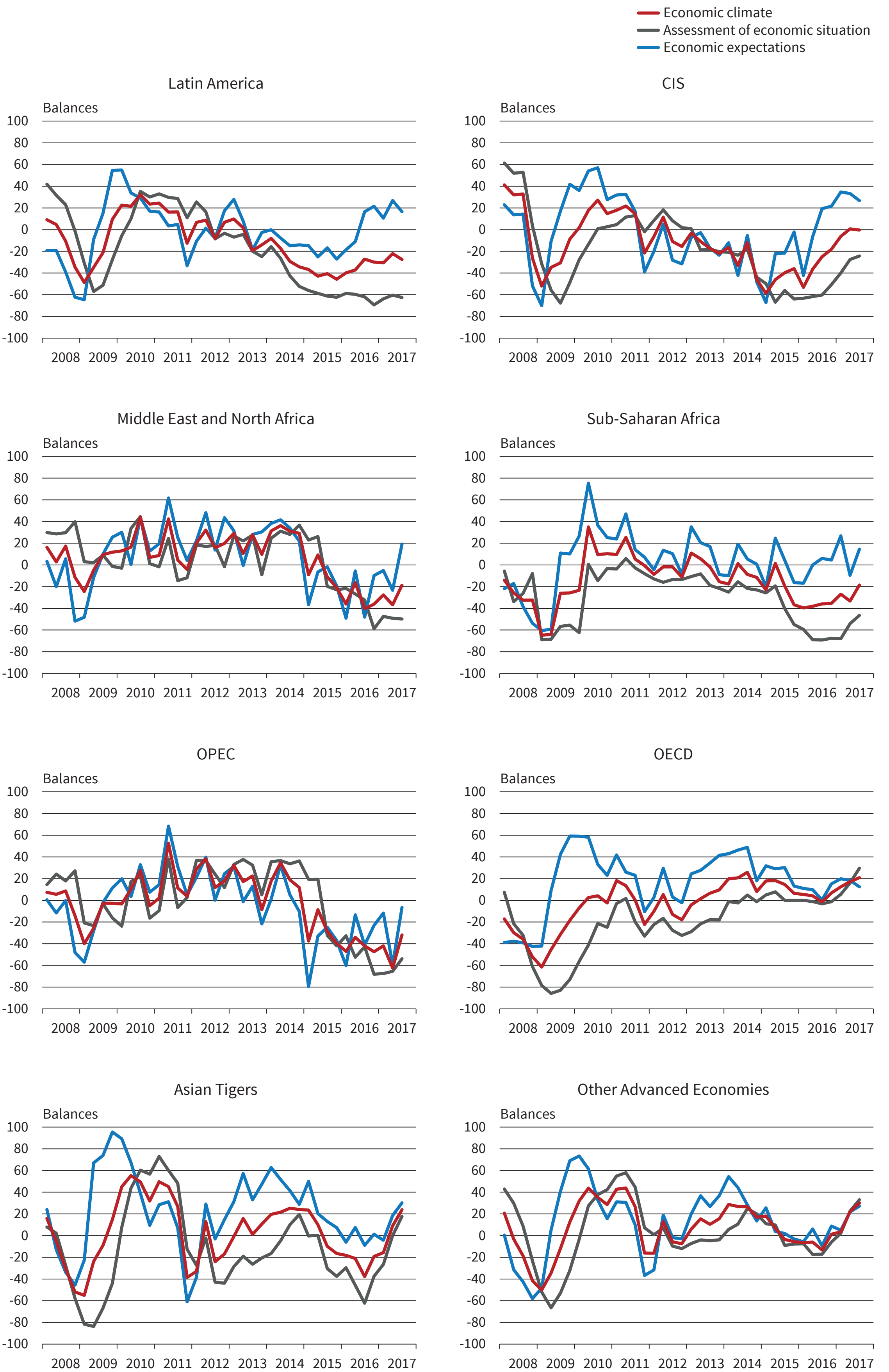
Figure 7.2

Selected Aggregates



Source: ifo World Economic Survey (WES) III/2017.

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Figure 8.1

Advanced Economies

Source: ifo World Economic Survey (WES) III/2017.

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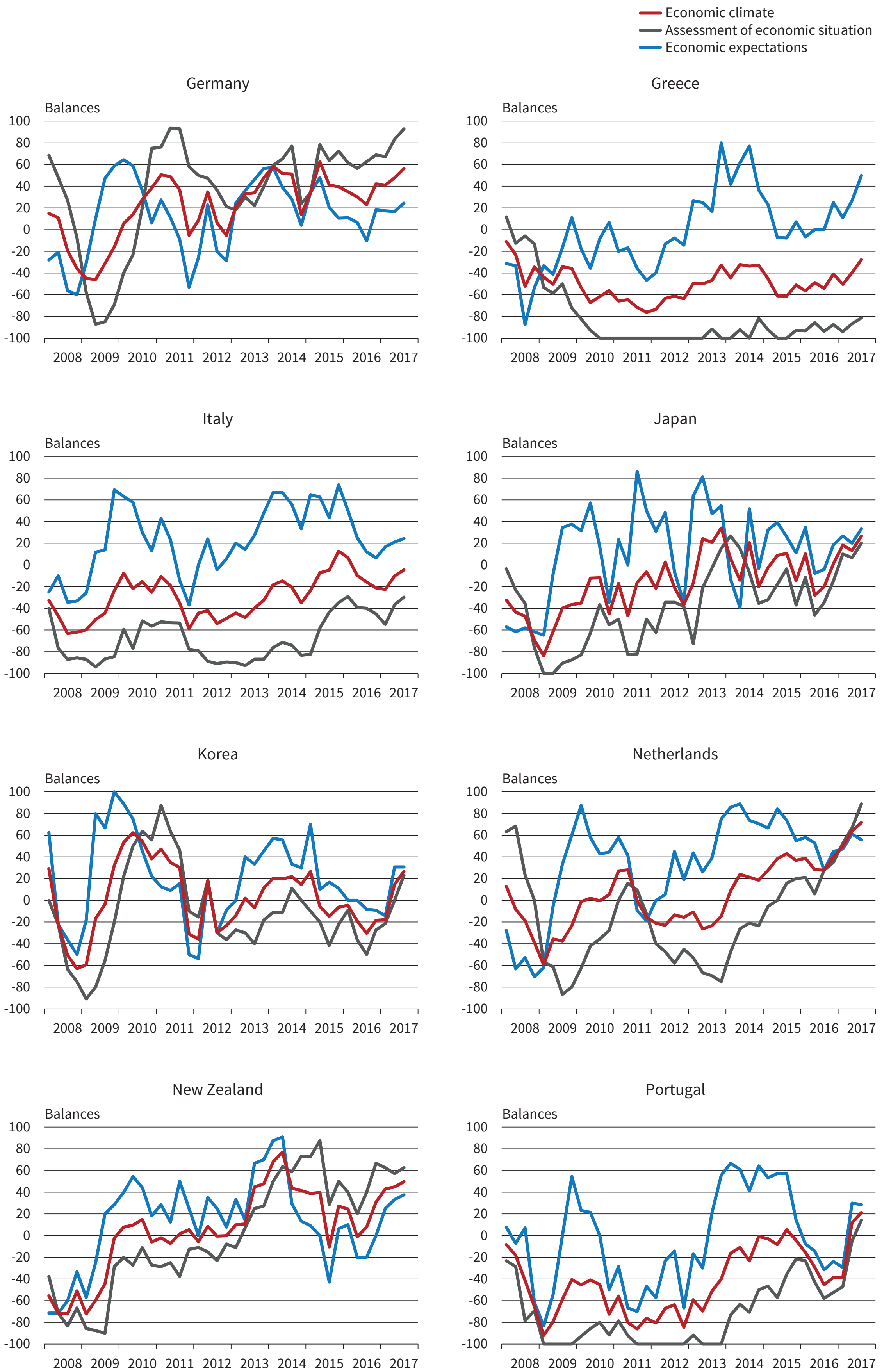
Figure 8.2

Advanced Economies



Source: ifo World Economic Survey (WES) III/2017.

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Figure 8.3

Advanced Economies

Source: ifo World Economic Survey (WES) III/2017.

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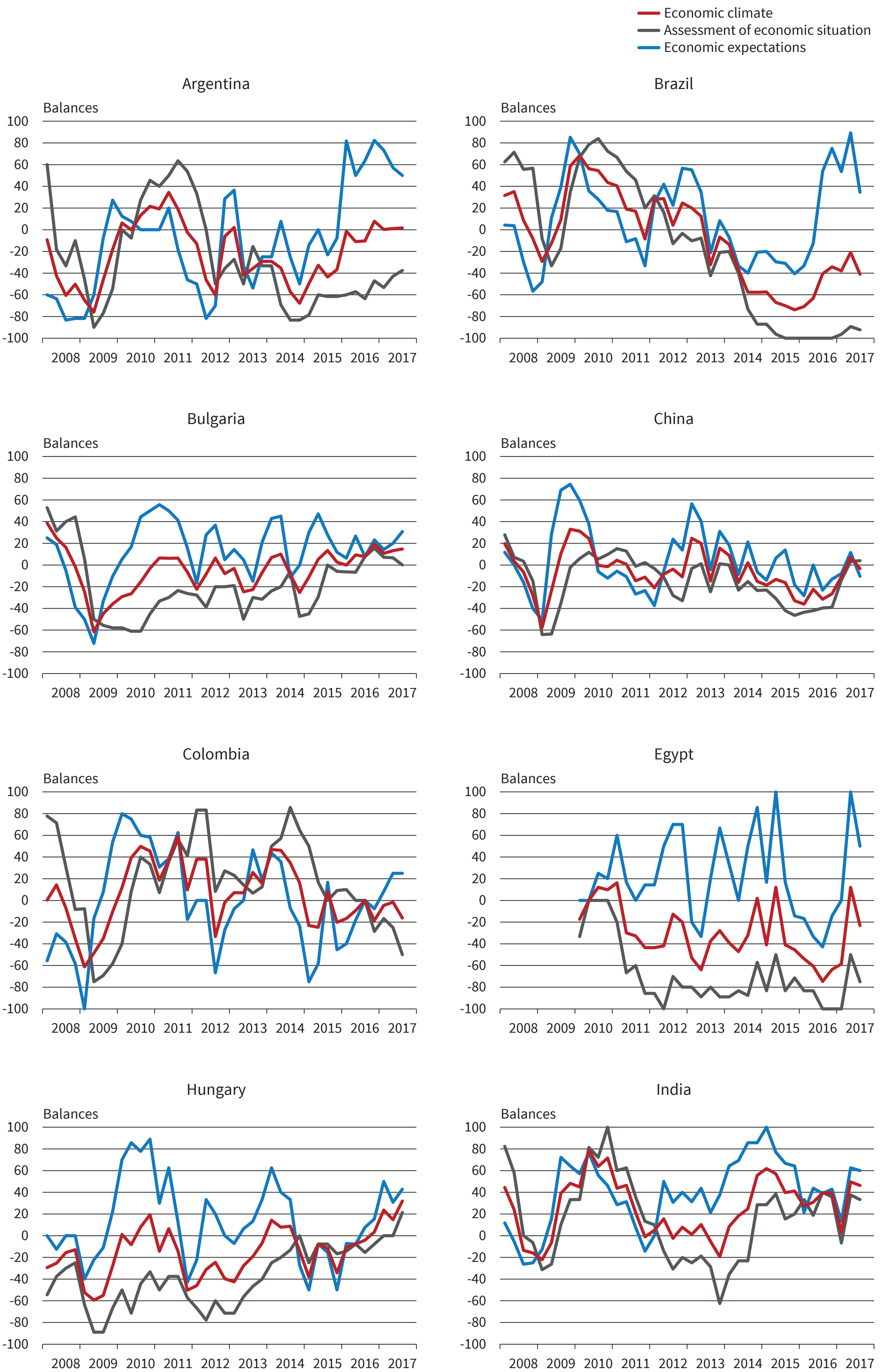
Figure 9.1

Emerging Markets and Developing Economies



Source: ifo World Economic Survey (WES) III/2017.

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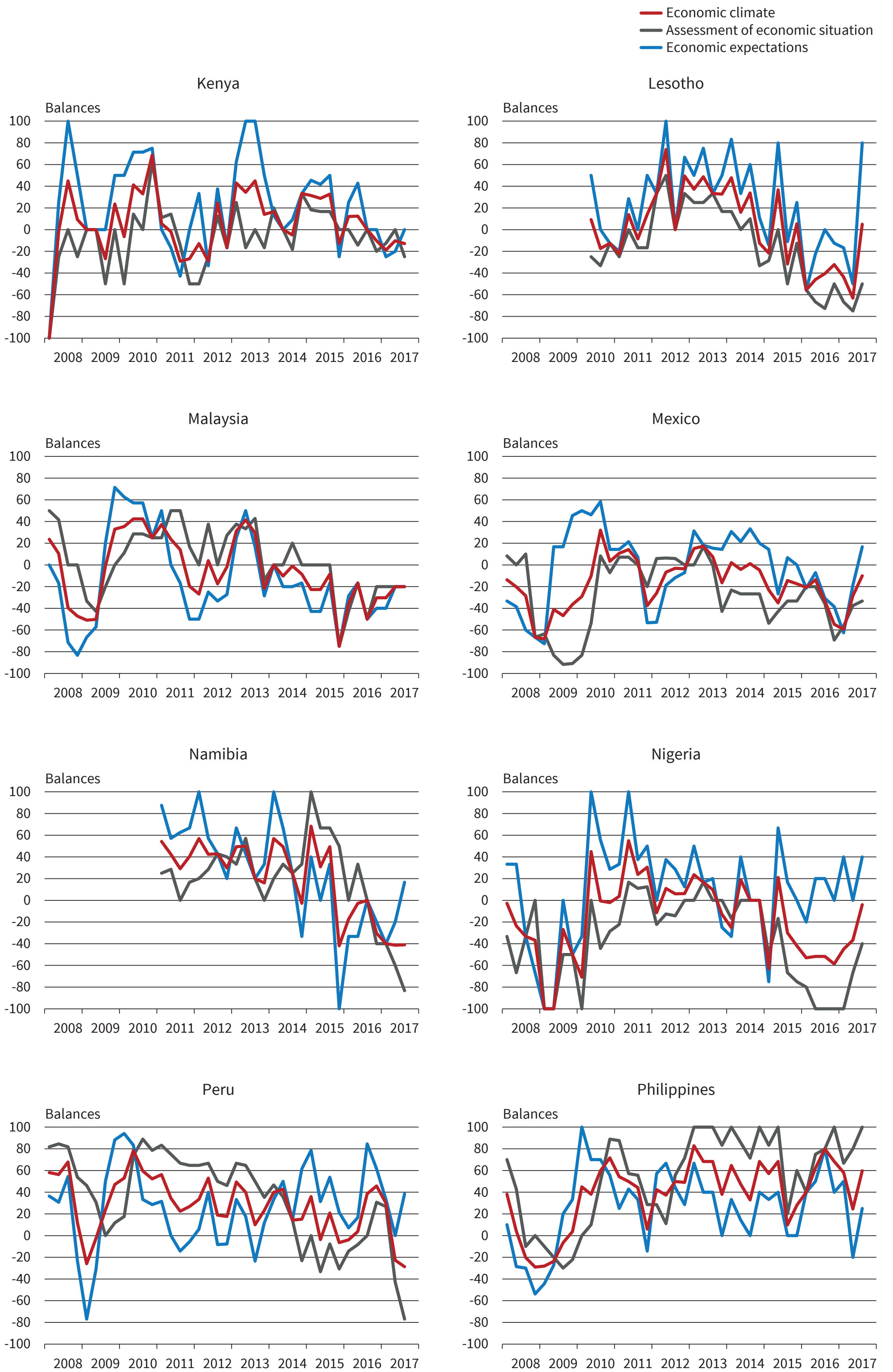
Figure 9.2

Emerging Markets and Developing Economies



Source: ifo World Economic Survey (WES) III/2017.

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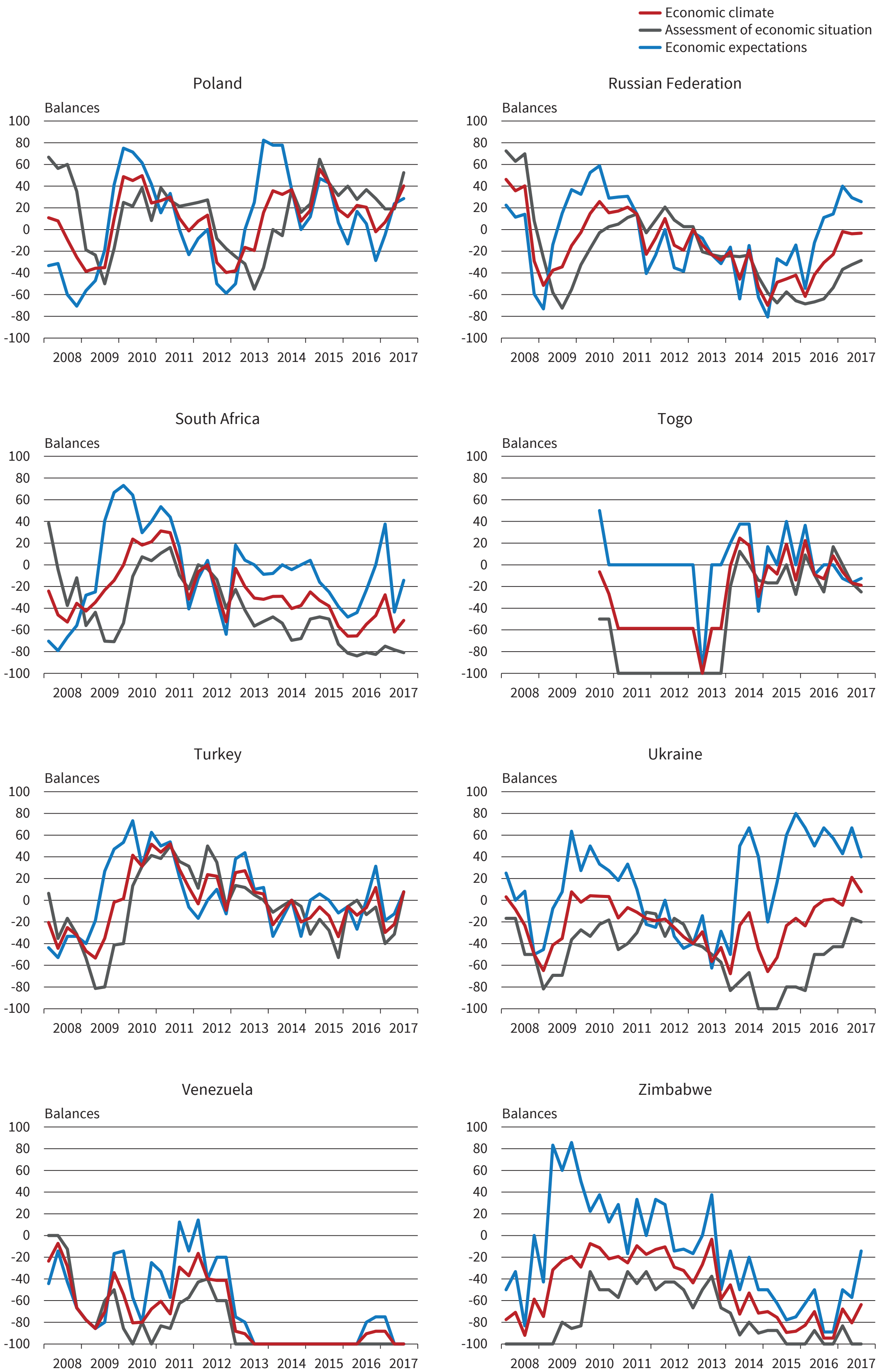
Figure 9.3

Emerging Markets and Developing Economies



Source: ifo World Economic Survey (WES) III/2017.

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