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World Economic Climate
ifo World Economic Climate Deteriorates Further

Advanced Economies
The Economic Climate in the Advanced Economies Stabilises at a Satisfactory Level

Emerging and Developing Economies
Economic Climate in Emerging Market and Developing Economies Cools Down Further

Special Topic
Collective Memories on the European Debt Crisis

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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 *October 2018, 1,230* economic experts in *119* 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; The individual replies are combined for each country without weighting as an arithmetic mean of all survey responses in the respective country. Thus, 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 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 Deteriorates Further

The ifo World Economic Climate deteriorated for the third time in succession. The indicator dropped from +2.9 points to -2.2 points this quarter. Assessments of the current economic situation deteriorated significantly, but nevertheless remain above their long-term average. Economic expectations were also scaled back considerably (see Figure 1). Growth is waning in the world economy.

The economic climate deteriorated particularly strongly in emerging and developing countries (see Figures 2, 8.1 and 8.2). Except for Latin America, economic expectations declined far more sharply than assessments of the current economic situation. The economic climate in Latin America, by contrast, improved due to more optimistic economic expectations. In advanced economies, the economic climate remained largely unchanged. Here, however, a clear division emerged: while assessments of the current economic situation and expectations improved in the USA, they cooled down in the European Union.

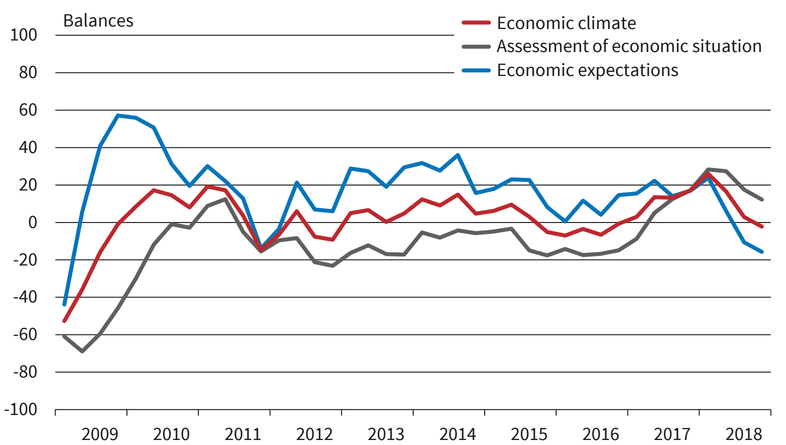
According to experts, the deterioration in worldwide economic expectations was particularly clearly reflected in weaker private consumption, while investment activity did not decline any further. Survey participants also expect far weaker growth in world trade, which is probably because they do not expect existing trade barriers to be dismantled (see Figure 6 and Table 3). Overall, they are expecting world gross domestic product to increase by 3.6 percent on average in the years ahead (see Table 2).

THE ECONOMIC CLIMATE IN THE ADVANCED ECONOMIES STABILISES AT A SATISFACTORY LEVEL

The satisfactory economic climate in the **Advanced Economies** as a group remained stable, at 13.6 points on the balance scale (see Figure 8.1). Assessments of the present economic situation stayed robust at 47.5 points. The expectations for the coming six months, for the second time in a row, remained pessimistic at -15.7 points. Experts reported strong investment and domestic consumption indicators in the fourth quarter of 2018, but both are likely to weaken in the next six months. Respondents report that the main economic problems faced by the advanced economies are the lack of skilled labour and the widening income gap. Taking a closer look at the different regions within the advanced economies a clear division emerged: while assessments of the current economic situation and expectations

Figure 1

ifo World Economic Climate

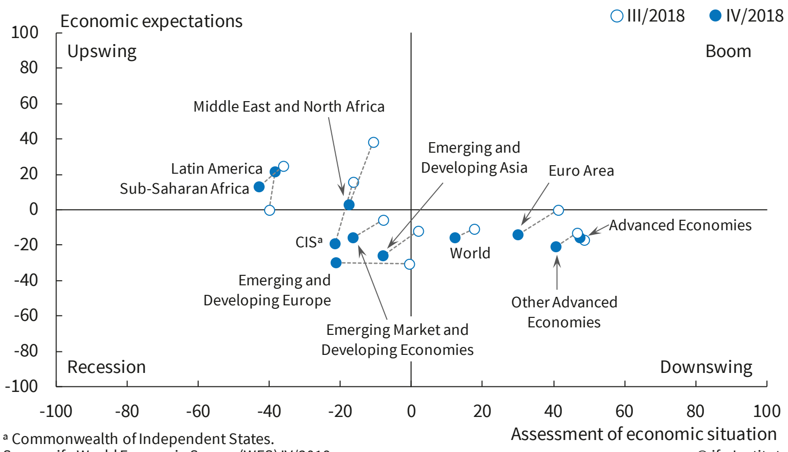


Source: ifo World Economic Survey (WES) IV/2018. © ifo Institute

Figure 2

ifo Business Cycle Clock for Selected Aggregates

Change from III/2018 to IV/2018; balances



[a] Commonwealth of Independent States.
Source: ifo World Economic Survey (WES) IV/2018. © ifo Institute

Box1

IFO BUSINESS CYCLE CLOCK FOR THE WORLD ECONOMY

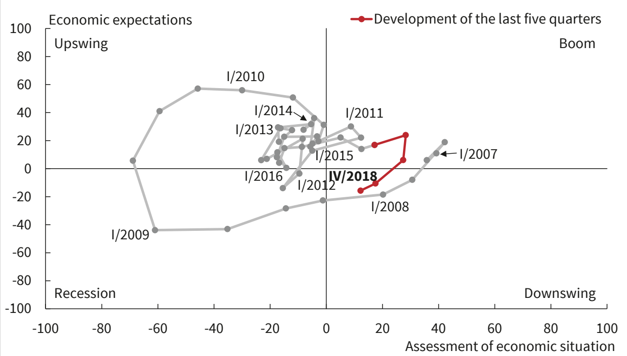
A glance at the ifo Business Cycle Clock, showing the development of the two components of the economic climate in recent years, can provide a useful overview of the global medium-term forecast. The business cycle typically proceeds clockwise in a circular fashion, with expectations leading assessments of the present situation.

According to the October 2018 survey, the ifo Indicator for the world economy moved further into the downswing quadrant (see Figure 3.1). Experts' assessments of both the current economic situation and their economic expectations deteriorated somewhat compared to the previous quarter. Although the indicator is in the downswing quadrant, it remains very close to the middle, indicating only a weak downturn.

Figure 3.1

ifo Business Cycle Clock World Economy

Balances



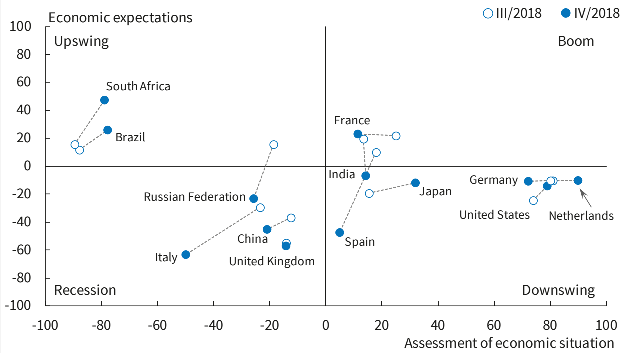
Source: ifo World Economic Survey (WES) IV/2018. © ifo Institute

To further analyse which countries are the main drivers behind this minor downturn, we plotted the main advanced economies and key emerging markets in the Business Cycle Clock below and visualised the change from last quarter to the current quarter (see Figure 3.2). The advanced economies show a very diverse picture. France is the only country that remains in the boom quadrant, while Spain joined the other advanced countries in the downswing quadrant. The Netherlands, Japan and the United States, in the downswing quadrant due to their pessimistic outlook, saw their current economic situation improve. Italy moved even further into the recession quadrant. Out of the key emerging markets, both South Africa and Brazil remain in the upswing quadrant. India's economic outlook clouded over, and the economy suffered a slight downturn. Economic expectations for Russia turned clearly negative, moving its economy back into recession. To sum up, most countries are now either in the downswing or recession quadrants of the ifo business cycle clock. In advanced economies where the current economic situation is still assessed as favorable, it remains to be seen whether there will be any further consolidation of this quarter's somewhat gloomy expectations in the next survey.

Figure 3.2

ifo Business Cycle Clock for Selected Countries

Change from III/2018 to IV/2018; balances



Source: ifo World Economic Survey (WES) IV/2018. © 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).

improved in the USA, they cooled down in the European Union and euro area.

Sentiment in the **Euro Area** continued to weaken for the third quarter in a row. The ifo Economic Climate for the euro area fell significantly from 19.6 points to 6.6 points, plunging to its lowest level since mid-2016. Experts downwardly revised their assessments of both the current economic situation and expectations significantly. The euro area's economy is moving into rough waters.

In **Italy** and **Spain** experts' assessments plummeted. In Spain survey participants were markedly more pessimistic than last quarter about the economic outlook. They downwardly revised their assessments of the current economic situation to a relatively small extent by comparison. Spain's economic climate indicator reached its lowest level since end-2013, with -23.2 on the balance scale. 85.0% of WES-experts reported a lack of confidence in the economic policy of the Spanish government. In addition, more experts stated that there is a current practice of inefficient debt management (47.4 percent of the experts compared to 29.4 percent six months ago). In **Italy** experts' assessments of both the current economic situation and expectations were far more negative, resulting in the lowest score of the economic climate indicator since the end-2011 with -56.7 points on the balance scale. In Italy, 93.3 percent of experts also expressed little confidence in the economic policy of their government. In addition, the climate for foreign investors is assessed as unfavourable, with 91.1 percent of experts indicating this as pressing issue. In **Germany** and **France** economic expectations remained almost unchanged, while assessments of the current economic situation deteriorated somewhat. As a result, the economic indicator dropped in both countries. In Germany, the economic climate remains favourable, and in France it is satisfactory. In the **Netherlands**, by contrast, assessments of the current economic situation improved. However, survey participants did not alter their economic expectations, which are slightly pessimistic at -10.0 points. A clear majority of the experts surveyed indicated that a lack of skilled labour is currently hindering economic performance in the Netherlands. In **Portugal** experts upscaled their expectations of the economic outlook somewhat, but were less favourable about the current situation. As a result, the economic climate remained at the same level as in the previous survey. Current investment was assessed as poor by survey participants. This is also reflected by the fact that 78.9 percent of the experts surveyed reported capital shortage as a pressing issue facing Portugal. In contrast to other countries in the euro area, a relatively low percentage of experts in Portugal (27.8 percent) stated that confidence in their government's economic policy is missing. Experts in the euro area scaled back their export expectations, reflecting beliefs that barriers to trade have grown higher (see Figure 6). At the same time, a larger number of experts now believe that short- and long-term inter-

Table 1

Inflation Rate Expectations for 2018 and in 5 Years (2023)

Aggregate*/Country	2018	2023	Country	2018	2023
Average of countries	**3.9**	**3.6**	Bosnia and Herzegovina	1.7	2.7
EU 28 countries	2.1	2.3	Brazil	4.3	4.2
Euro area [a]	1.8	2.2	Bulgaria	3.0.	3.1
			Cabo Verde	1.8	2.5
Advanced Economies	2.1	2.3	Chile	2.7	3.1
Australia	2.2	2.7	China	2.3	3.5
Austria	2.1	2.2	Colombia	3.3	3.0
Belgium	2.0	2.0	Croatia	1.9	2.3
Canada	2.1	2.1	Ecuador	0.4	2.2
Czech Republic	2.4	3.0	Egypt	10.8	8.5
Denmark	1.2	1.7	El Salvador	2.1	2.9
Estonia	3.3	2.2	Georgia	3.7	4.7
Finland	1.3	2.7	Guatemala	3.4	4.0
France	1.8	1.9	Hungary	2.9	3.4
Germany	2.0	2.2	India	5.3	4.6
Greece	1.3	2.2	Kazakhstan	7.6	5.8
Hong Kong	2.4	3.3	Kenya	6.5	7.1
Ireland	1.4	1.8	Kosovo	1.9	2.0
Israel	1.4	2.5	Lesotho	5.2	4.2 5.3
Italy	1.5	2.1	Malaysia	3.2	3.8
Japan	0.9	1.4	Mexico	4.8	4.2
Latvia	2.9	2.9	Morocco	1.9	2.3
Lithuania	2.7	2.8	Namibia	5.1	6.9
Netherlands	1.9	2.2	Nigeria	13.0	11.7
New Zealand	1.8	2.0	Pakistan	7.0	6.9
Norway	2.3	2.2	Paraguay	4.1	4.3
Portugal	1.5	2.0	Peru	2.6	2.7
Republic of Korea	2.4	2.4	Poland	2.2	2.8
Slovakia	2.5	2.5	Romania	4.5	4.8
Slovenia	2.0	3.1	Russian Federation	4.9	5.9
Spain	2.1	2.3	South Africa	5.3	5.4
Sweden	2.0	2.3	Sri Lanka	6.9	4.9
Switzerland	1.0	1.4	Thailand	1.2	1.8
Taiwan	1.6	1.8	Togo	2.4	2.8
United Kingdom	2.6	2.5	Tunisia	7.3	5.2
United States	2.4	2.5	Turkey	22.7	10.4
			Ukraine	10.7	7.0
Emerging market and developing economies	**5.4**	**4.7**	Uruguay	8.1	7.6
Argentina	41.1	11.9	Zambia	8.3	8.2
Bolivia	3.7	5.9	Zimbabwe	40.3	14.7

* 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) IV/2018.

est rates will rise over the next six months (see Figure 7), and that the US dollar will continue to strengthen. The forecast inflation rate for this year was raised from 1.7 percent to 1.8 percent (see Table 1). Experts' confidence in economic policy continued to evaporate.

The economic climate indicator for the **G7** countries overall stabilised at 15.1 points on the balance scale (see Figure 8.1). The European countries in particular saw their economic climate worsen. In the **United States** both climate components were assessed as better by the participating experts, although the economic outlook indicator remained negative at -14.0 points. The assessments of the present economic situation, however, reached their highest level since end-2000 at 78.9 points (see Figure 9.3). 82.5% of experts in the United States reported that widening income inequality is the biggest issue facing the economy again this quarter, which was the highest figure for a high-income group country. A smaller number of experts now believe that the volume of both imports and exports will decrease in the months ahead. Experts downwardly revised their inflation expectations in five years from 2.6 percent to 2.5 percent (see Table 1). The GDP forecast for the next three to five years was downwardly revised by 0.3 percentage points to 2.3 percent (see Table 2). As in the euro area, an increasing number of

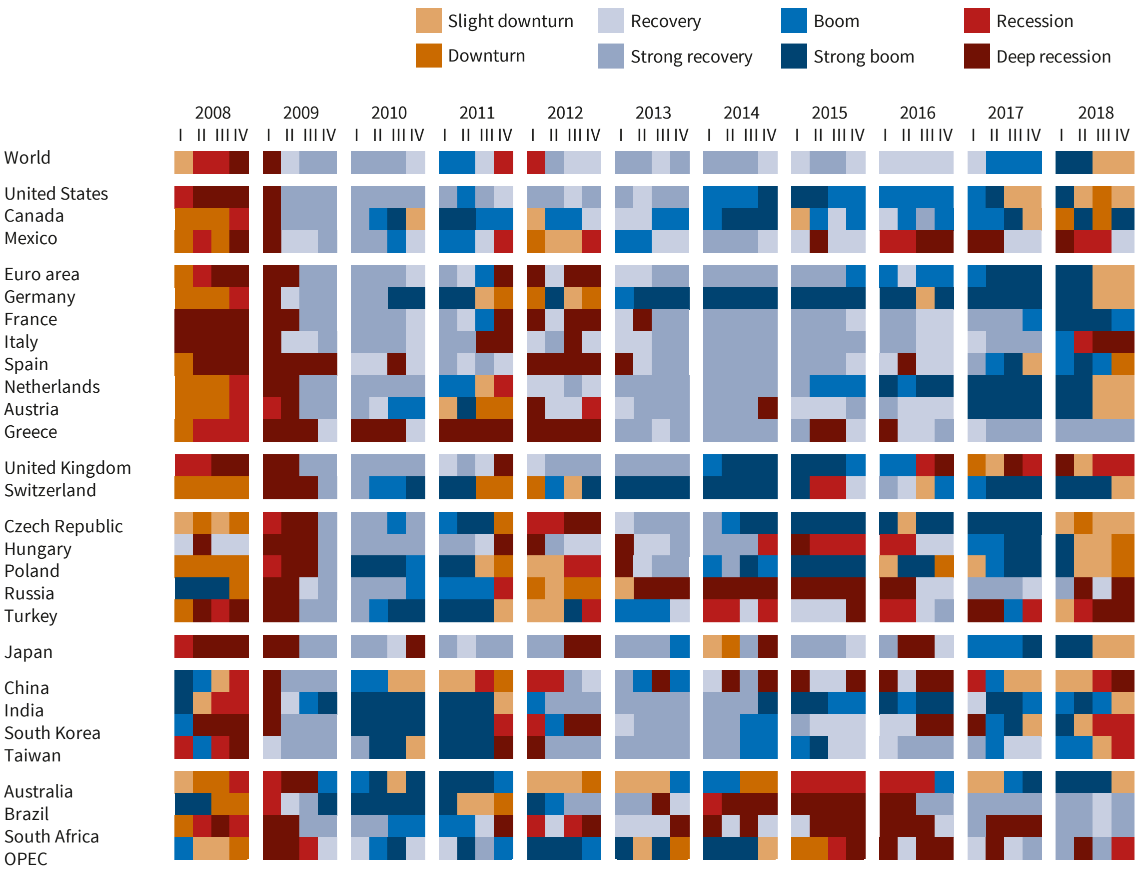
US experts believe that short- and long-term interest rates will rise over the next six months (see Figure 7). The economic climate indicator in **Japan** recovered from its dip in the previous survey and improved from -2.7 to +8.8 points on the balance scale. This was due to improvements in the indicator for the current situation as well as the economic outlook (see Figure 9.2). According to respondents, the two pressing economic problems currently facing Japan are a lack of innovation and a shortage of skilled labour. By contrast, experts believe there is currently a favourable climate for foreign investors in Japan, as this category was only cited by 4 percent of the experts. Inflation expectations did not change compared to the previous survey, and remained at 0.9 percent for 2018 and 1.4 percent for 2023 (see Table 1). However, the three to five-year forecast for GDP was downwardly revised by 0.2 percentage points to 1.2 percent (see Table 2). In **Canada**, the economic climate indicator improved by 21.6 points and now points to 30.3 on the balance scale. This is mainly due to improvements in forecast economic performance, which rebounded and was very optimistic (see Figure 9.1). Both current investment and consumption were more negatively assessed than in the previous survey, but consumption remains favourable. The expected inflation rate for 2018 remained at 2.1 percent, whereas the inflation rate for 2023 was downwardly revised from 2.2 to 2.1 percent (see Table 1). The expected annual growth in real GDP over the next 3 to 5 years was set at 2.3 percent (see Table 2). None of the economic problems listed in the survey were stated by over half of the respondents. Nevertheless, trade barriers to trade, a lack of skilled labour, administrative barriers to businesses and widening income inequality were identified by exactly 50 percent of the surveyed experts as constraining factors on economic performance in Canada.

There was no change in the economic climate of the **United Kingdom** (see Figure 9.3). The uncertainty surrounding Brexit remains a disruptive factor. However, as one expert points out, one should bear in mind this is an acute stress factor for the British economy, rather than a chronic one. The handling of negotiations and the risk of a "no-deal Brexit", as well as adjustment to life outside the EU, will nevertheless be very disruptive. This is clearly shown by the question on economic problems, as 94.3 percent of experts report a lack of confidence in the economic policy of their government and 85.7 percent observe that political instability is hindering the economy. Capital expenditure is very weak, and is not expected to recover in the coming months. Private consumption remains satisfactory, but is expected to weaken in the months ahead. Expected inflation for 2018 was upwardly revised from 2.4 to 2.6 percent (see Table 1). Fewer experts than in the previous survey were certain that short- and long-term interest rates will rise in the coming months (see Figure 7). Out of the three main currencies, the US dollar is slightly overvalued vis à vis sterling, according to the WES experts.

Economic performance continued to slow down further in the **Other Advanced Economies**. The economic climate indicator continued to drop, but remained positive at 7.7 points on the balance scale. Both components were downwardly revised, but experts' assessments of the economic situation remained favourable. The economic outlook by contrast reached its lowest level since early-2012 (see Figure 8.2). The economic slowdown in this aggregate was mainly due to worse assessments in the Asian countries in this group. Both **South Korea** and **Taiwan** saw their economic climate indicator drop below -20.0 points on the balance scale (see Figures 9.2 and 9.3). In South Korea inflation for 2018 was upwardly revised by 0.2 percentage points to 2.4 percent. The inflation rate for 2023, however, was downwardly revised by 0.1 percentage points to 2.4 percent (see Table 1). A rising number of experts expect short- and the long-term interest rates to increase in the coming six months. The US dollar and the British pound were both assessed as being overvalued vis à vis the Korean Won. More experts than in the previous survey expect the value of the US dollar to rise during the next six months. 90 percent of experts cited a lack of confidence in the government's economic policy as the most pressing issue facing the Korean economy at present. In Taiwan, besides a lack of confidence in the economic policy of its government, legal and administrative barriers for business were also reported by WES experts as hindering the economy. The indicator for investment decreased further compared to the previous survey, whereas the indicator for domestic consumption turned negative at -5.3 points for the first time since the third quarter of 2017. The forecast inflation rate for 2023 saw no change, but the inflation rate for 2018 increased slightly to 1.6 percent (see Table 1). There was a clear drop in expectations regarding volumes of trade: imports turned negative for the first time since July 2015, while the volume of exports turned negative for the first time since early-2012, indicating a slowdown in trade in the next six months. Of the remaining other advanced economies, **Norway** boasts the best economic climate, reflected by a marked improvement in assessments of the current economic situation. Although the economic outlook was downwardly revised, it remained positive, indicating further economic expansion in the months ahead, although at a slower pace. The expected annual growth rate for the next 3 to 5 years was forecast as 1.9%. This is considerably lower than the previous year, when experts forecasted an annual growth rate of 2.4% (see Table 2). In **Switzerland** and **Denmark**, the current economic situation was very favourably assessed, with 95.7 and 80.0 balance points respectively. In both countries, this situation is not expected to change soon (see Figures 9.1 and 9.3). The most pressing economic problem reported by respondents from both countries is a lack of skilled labour. This is also a major concern in the **Czech Republic, Sweden** and **New Zealand**. WES experts expect a favourable economic sentiment to continue to prevail

Figure 4

World Economic Survey
Heatmap



Notes: The assessments of the current situation and economic expectations for the next six months are visualised as a Heat Map. The results of the survey are represented by a four colour scheme that illustrates the four phases of a business cycle: boom, downswing, recession, and upswing. These colours are slightly lighter when the values of the assessments of present situation and economic expectations are within a defined range which reflects a transition area between the four phases.

Source: ifo World Economic Survey (WES) IV/2018.

in these countries. They nevertheless expect a slight slowdown as the economic outlook improved compared to previous survey, but still remains slightly pessimistic in the Czech Republic and Sweden. New Zealand's economic outlook indicator did not change. In **Australia**, the present economic situation was assessed as favourable. The economic outlook indicator, by contrast, decreased by 18.4 points to -5.9 points, indicating that the current positive economic situation will continue, but will not improve further. Australia hasn't experienced a single recession in the last 27 years, which The Economist relates back to changes in the country's national pension and health care system that were made after the last recession in 1991. Thanks to these changes, Australia's government now spends just half of the OECD average on pensions as a share of GDP.[1] However, this is not to say that there are no economic problems at present. WES experts indicate a lack of innovation, as well as inadequate infrastructure as pressing economic problems. Political instability was also indicated by 58.8% of the experts as hindering the Australian economy, while six months ago this was only cited by 25% of experts. The inflation rate for 2018 was slightly upwardly revised to be 2.2% and an inflation rate of 2.7 is expected for 2023 (see Table 1).

ECONOMIC CLIMATE IN EMERGING MARKET AND DEVELOPING ECONOMIES COOLS DOWN FURTHER

Economic conditions continued to worsen in the **Emerging markets and developing economies** as a group. Assessments of both the present economic situation and economic expectations were downgraded and both indicators fell to around -16 points on the balance scale (see Figure 8.1). The economic climate remains negative in all sub-groups of this aggregate. This also applies for **Latin America**, despite the fact that the economic outlook brightened and turned positive. In emerging markets corruption was again perceived as the most pressing problem; and to an even greater extent than six months ago (see Table 3).

[1] The Economist- What the world can learn from Australia. Accessed: 8th of November 2018. Source: https://www.economist.com/leaders/2018/10/27/what-the-world-can-learn-from-australia

Table 2

Expected average annual growth rates of real Gross Domestic Product (GDP) over the next 3 to 5 years (based on WES IV/2018 and IV/2017)

Aggregate*/Country	IV/2018	IV/2017	Country	IV/2018	IV/2017
Average of countries	**3.6**	**3.7**	Brazil	2.3	3.1
EU 28 countries	1.9	2.1	Bulgaria	3.2	3.9
Euro area [a)]	1.8	1.9	Cabo Verde	4.4	4.2
			Chile	3.6	3.2
Advanced Economies	**2.0**	**2.2**	China	5.9	5.6
Australia	2.7	2.7	Colombia	3.3	3.4
Austria	2.0	1.9	Croatia	2.6	2.5
Belgium	1.5	1.7	Ecuador	2.3	2.7
Canada	2.3	2.1	Egypt	4.6	5.0
Czech Republic	2.5	2.7	El Salvador	2.7	3.0
Denmark	1.8	1.7	Georgia	4.3	4.7
Estonia	3.3	3.3	Guatemala	3.2	3.8
Finland	1.8	2.2	Hungary	2.7	2.7
France	1.7	1.8	India	7.5	7.6
Germany	1.6	1.7	Kazakhstan	3.7	3.3
Greece	2.3	2.3	Kenya	5.0	5.7
Hong Kong	3.0	3.0	Kosovo	3.8	3.5
Ireland	3.6	3.5	Lesotho	2.0	4.0
Israel	3.4	4.9	Malaysia	4.2	4.8
Italy	1.1	1.5	Mexico	2.4	2.6
Japan	1.2	1.4	Morocco	3.8	3.3
Latvia	2.8	3.5	Namibia	2.4	3.1
Lithuania	2.5	2.8	Nigeria	3.4	4.2
Netherlands	1.9	2.1	Pakistan	5.1	5.5
New Zealand	2.7	2.6	Paraguay	4.4	4.0
Norway	1.9	2.4	Peru	3.9	3.9
Portugal	1.8	2.1	Philippines	5.9	6.5
Republic of Korea	2.2	2.8	Poland	3.3	3.4
Slovakia	3.4	3.3	Romania	3.8	4.0
Slovenia	2.9	3.0	Russian Federation	1.8	2.0
Spain	2.2	2.5	South Africa	2.1	2.7
Sweden	1.9	1.9	Sri Lanka	4.4	5.5
Switzerland	1.8	1.9	Thailand	3.8	4.3
Taiwan	2.3	2.3	Togo	4.0	5.2
United Kingdom	1.4	1.6	Tunisia	2.9	2.8
United States	2.3	2.6	Turkey	3.8	4.7
			Ukraine	3.6	3.8
Emerging market and developing economies	**4.8**	**4.9**	Uruguay	2.4	2.9
Argentina	1.7	2.9	Venezuela	-18.0	0.0
Bolivia	3.9	3.6	Zambia	4.3	5.6
Bosnia and Herzegovina	2.6	2.6	Zimbabwe	2.5	4.2

* 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) IV/2018.

The economic climate for important emerging markets (**Brazil, Russia, India, China** and **South Africa – BRICS**) clouded over further; its aggregated indicator fell from -14.1 to -22.8 points on the balance scale (see Figure 8.1). Out of this group, the sharpest downturn in the economic climate was seen in **Russia** (see Figure 10.3). The outlook for the next six months in particular turned pessimistic. Fewer experts than in the previous survey expect exports to increase in the next six months. Imports, in turn, are likely to decrease, which will lead the trade balance to a surplus in the months ahead. The figures for inflation rates are slightly higher than in the previous survey and are forecast this year at 4.9 and 5.9 percent in five years (see Table 1). According to WES experts, confidence in the government's economic policy is increasingly waning. However, they also see corruption, a lack of innovation, legal and administrative barriers for business and inadequate infrastructure as current prevailing problems for the Russian economy. The experts surveyed see mid-term GDP growth at 1.8 percent (see Table 2). Experts in **China** were more negative regarding the present economic situation and the economic outlook than in the third quarter's survey. This resulted in a downturn in the economic climate indicator from -25.0 to -33.6 balance points (see Figure 10.1). Capital expenditure and private consumption were assessed as weak and are not foreseen to recover in the next six months. In line with current weak economic conditions, short- and long-term interest rates are expected to decrease slightly in the months ahead (see Figure 7). The mid-term GDP growth estimate for China improved from 5.6 percent last year to 5.9 percent, and remains one of the highest growth figures in the emerging markets. However, the WES experts identify **India** as one of the fastest growing economies in Asia with an estimated GDP growth of 7.5 percent over the next three to five years (see Table 2). Assessments of the current economic situation remained satisfactory, while economic expectations continued to deteriorate, resulting in an economic climate indicator pointing to 3.5 on the balance scale (see Figure 10.2). This corresponds to the development in its (GDP) trend rate. The Indian Rupee is considered to be undervalued vis-a-vis the world's main four currencies (the US dollar, the euro, the British pound and the yen). Besides inadequate infrastructure and a widening of income inequality, which were both cited back in the April survey as problematic issues, capital shortages emerged as a new threat to the economy in this quarter. **Brazil** and **South Africa** were the only countries in this block where the present situation and economic expectations improved compared to the previous survey. Despite these improvements, the economic climate indicator remains very negative on balance in both countries (see Figures 10.1 and 10.3). With economic expectations being moderately positive and supposed to lead the present economic situation, both countries are in the recovery quadrant of the ifo Business Cycle Clock (see Figures 3.1 and 4). In both countries, more experts than in the previous survey expect short- and long-term interest rates to rise within the next six months (see Figure 7). While the Brazilian Real seems to have recovered from its recent depreciation against the main four currencies (the US dollar, euro, yen and the British pound), WES experts still deem the South African Rand as undervalued vis à vis the main four currencies. In both countries, mid-term growth perspectives were slightly downwardly revised compared to the survey one year ago to 2.3 percent in Brazil and to 2.1 percent in South Africa (see Table 2). Both countries suffer from corruption and a lack of confidence in the government's economic policy. After the recent presidential election in Brazil with the newly elected president Jair Bolsonaro from the *Partido Social Liberal* (PSL), it remains to be seen whether confidence can be restored.

OTHER EMERGING MARKETS

Within the other aggregates of emerging and developing economies, the economic climate indicator worsened and remained negative in **Emerging and Developing Europe, Emerging and Developing Asia**, as well as in **Sub-Saharan Africa.** The slight upturn in the economic climate in the **Middle East and Northern Africa** and in the **Commonwealth of Independent States,** seen in the third quarter, was only of short duration. In this quarter's survey, WES experts strongly curbed their economic expectations in both aggregates. The economic climate improved marginally only for **Latin America,** as the present economic situation was again deemed as weak with only economic expectations turning more positive again (see Figures 2, 8.1 and 8.2).

In **emerging and developing Asia**, the climate indicator fell from -5.1 points in July to -17.1 points this quarter. This figure mainly reflects the economic developments of **China** and **India**, as these are the countries with the highest weights in this aggregate.[2] However, the **ASEAN-5** countries (**Indonesia, Malaysia, Philippines, Thailand,** and **Vietnam**) saw a downturn too, even although both climate components remained slightly above the zero line (see Figure 8.1). Corruption was still mentioned as a threat to the economy in these countries, but a lack of skilled labour was mostly cited as an obstacle to the economy, followed by a lack of international competitiveness and innovation. WES experts in **Pakistan** rated the present economic situation as weak, just as they did in the previous survey. At the same time, they upwardly revised their economic expectations, which are now slightly positive again. One reason might be that after the formation of the new government in Pakistan, the economy is going through a transition phase with the government trying to bring in some economic reforms, according to one of the WES experts. Nevertheless, the resulting economic climate for Pakistan remains negative on the whole. Capital expenditure and private consumption are still regarded as weak, but are likely to strengthen in the months ahead. Imports are foreseen to be lower by the end of the next six months, resulting in an improvement in the trade balance. Inflation rate expectations for 2018 and in five years rank at around 7 percent among the highest in emerging Asia (see Table 1). Besides missing innovation, Pakistan is facing inadequate infrastructure and capital shortages as economic obstacles, according to the experts surveyed.

The economic climate in **emerging and developing Europe** continued to deteriorate from -16.1 to -25.6 points on the balance scale, hitting its lowest level in six years. While experts' economic expectations remain as pessimistic as in the previous survey, assessments of the present economic situation deteriorated markedly (see Figures 2 and 8.1). The deterioration in this aggregate is mainly due to **Turkey**'s poorer economic perfor-

[2] For a more detailed description on China and India, see the BRICS section.

mance. Assessments of the present economic situation deteriorated significantly, with the indicator now pointing to -86.7 points. Economic expectations, in turn, are slightly less negative than in the third quarter. Nevertheless, this resulted in the worst overall economic climate in over 20 years (see Figure 10.3). Both capital expenditure and private consumption are considered to be weak at present, with no recovery expected by the end of the next six months. According to WES experts, the Turkish Lira remains undervalued vis à vis the euro, the British pound and US dollar and is expected to continue to lose value against the latter one over the next six months. Inflation rate expectations for this year and the next five years sharply increased compared to the previous survey to 22.7 percent and 10.4 percent respectively and are among the highest figures in the emerging markets (see Table 1). Capital shortage and a lack of confidence in the government's economic policy gained significance as important constraints on the Turkish economy. In **Romania**, the economic climate improved only marginally from -7.5 points to -4.8 points on the balance scale, due to more favourable assessments of the present economic situation. The economic climate indicator for **Bulgaria** and **Poland** fell slightly, but remained above the zero line. This means an economic development in line with its trend rate. In both countries, the present economic situation was again rated as favourable, but economic expectations fell sharply and turned negative on the balance scale. The GDP growth perspectives over the next three to five years were slightly revised downwards compared to the survey one year ago, with figures of 3.2 percent for Bulgaria and 3.3 percent for Poland cited on average (see Table 2). Both countries suffer from a lack of skilled labour, which also applies to **Hungary**. In addition, WES experts identified corruption and a lack of international competitiveness as a threat to the Hungarian economy. Overall, the economic climate is more positive here than in the other countries of this aggregate. According to WES experts, the present economic situation was more favourable again than in the last survey. However, the economic outlook continued to follow a downward trend, with more experts turning pessimistic about the future. There were no major revisions of inflation figures, which again were set at 2.9 percent in 2018 and at 3.4 percent in 2023. Mid-term growth perspectives also remain at 2.7 percent on average (see Tables 1 and 2). The Hungarian Forint is still seen as overvalued vis à vis the euro, but against the other currencies US dollar, British pound and yen it returned to more or less its proper value, according to experts surveyed.

After slightly improving in the third quarter, the economic climate in the **Commonwealth of Independent States (CIS)** clouded over again. The indicator fell clearly below the zero line to -20.4 balance points. Assessments of the present situation, as well as economic expectations, fell to a similar level within the area, indicating a weak economic performance with no signs of recovery in the months ahead (see Figures 2 and 8.2). This pattern certainly reflects economic developments in **Russia**, whose weight accounts for nearly 80 percent of this aggregate, and where uncertainty over the impact of US sanctions still prevails.[3] In the **Ukraine**, assessments of the present economic situation continued to improve, but remained in unfavourable territory. The economic outlook deteriorated again (see Figure 10.3). At least capital expenditure seems to have recovered, with experts rating it as satisfactory for the first time in a long time. They are now following the development in private consumption, whose performance turned positive in the third quarter of this year. Inflation rate expectations for 2018 and the next five years remained stable at 10.7 and 7.0 percent respectively (see Table 1). While short-term interest rates are expected to rise, more experts than in the previous two surveys expect long-term interest rates to shrink in the months ahead. WES experts see economic growth perspectives at 3.6 percent on average over the next three to five years (see Table 2). The economic climate in **Georgia** and **Kazakhstan** worsened. In Georgia assessments of both the present economic situation and economic expectations are less positive on balance than three months ago. In Kazakhstan, WES experts nevertheless rated the current situation as favourable. The economic outlook, however, turned pessimistic for the first time in nearly three years.

As described previously, **Latin America** is the only aggregate in the emerging and developing markets where the economic climate improved, albeit at a low level (see Figure 8.2). Economic expectations turned positive again. It remains to be seen whether this will prove the turning point towards a recovery (see Figure 2). The economic climate improved in all major countries in this region, **Argentina, Brazil**[4]**, Chile, Mexico, Peru** and **Uruguay,** albeit at different levels (see Figures 10.1 and 10.2). The climate indicator remains very negative for **Argentina** and **Brazil.** Assessments of the present economic situation in both countries remained at a low level. Economic expectations brightened, especially in Argentina, and WES experts turned clearly positive about economic developments ahead of the next six months. The inflation rate for 2018 was further upwardly revised from 29.2 to 41.1 percent this quarter (see Table 1). However, no further increase is expected in the next six months. The Argentine Peso was considered to be undervalued against the four main currencies – the US dollar, the euro, the British pound and the Japanese yen – and WES experts expect it to devalue further against the US dollar. GDP growth estimates of 1.7 percent on average over the next three to five years are considerably lower than the figure projected one year ago (2.9 percent, see Table 2). Confidence in the government's economic policy is increasingly waning. In **Uruguay**, the present economic situation improved markedly, according WES experts. Economic expectations are less negative than three months ago too, shift-

[3] For a more detailed description of the situation in Russia, see the BRICS section.
[4] For a more detailed description on Brazil, see the BRICS section.

ing the economic climate indicator to -17.4 points on the balance scale; and thus into less negative numbers than in July. After having improved in the third quarter, the present economic situation in **Mexico** deteriorated again. The economic outlook, however, brightened considerably and WES experts turned positive for the first time in a year. Nevertheless, the resulting economic climate remains negative at -3.1 points on the balance scale. Mid-term GDP growth perspectives of 2.4 percent are somewhat lower than the figure expected one year ago (2.6 percent, see Table 2). Inflation rate expectations for 2018 and for 2023 increased compared to the survey in July to 4.8 and 4.2 percent respectively (see Table 1). More experts than in the previous survey expect short- and long-term interest rates to rise over the next six months. Growing income inequality is becoming increasingly important in terms of factors constraining the Mexican economy, after corruption, which clearly remains the main problem. **Chile** and **Peru** saw their economic climate indicators improve considerably. In Chile, the economic climate now points to 44.4, marking the highest score within Latin America. Assessments of both the present economic situation and economic expectations are more positive than in July. In Peru, WES experts see the present economic situation less favourably than three months ago, but are considerably more confident about the six-month economic outlook. Chile with 3.6 percent, as well as Peru with 3.9 percent, have the highest growth expectations in this region for the next three to five years (see Table 2). **Colombia** was one of the few countries in Latin America, where the economic climate worsened, albeit only marginally. At 29.1 balance points, the economic climate is the second brightest in this region. Only the economic expectations are slightly less optimistic than three months ago. WES experts see the Colombian Peso as undervalued vis-à-vis the main four currencies – the US dollar, the euro, the British pound and the yen. More experts than in the previous survey expect short- and long-term interest rates to rise in the next six months.

In countries from the **Middle East and North Africa** (MENA) the economic climate deteriorated again. The indicator fell from +12.4 to -7.7 points on the balance scale. The present situation was deemed slightly more unfavourable than three months ago. The economic outlook clouded over (see Figure 8.2). Capital shortage was increasingly cited as a key economic obstacle in MENA countries. Lack of skilled labour and corruption were also identified as key economic problems at present by WES experts (see Table 3). In **Sub-Saharan** countries, besides corruption, a lack of confidence in government economic policy and growing income inequality are posing problems to the economy.

Table 3

Economic Problems ranked by World Importance*

	World	Advanced Economies	Emerging and Developing Economies	EU	Developing Europe	Developing Asia	Latin America	CIS	MENA	Sub Saharan Africa
Widening income inequality	69.6	65.1	73.3	55.0	59.7	73.0	78.4	75.1	64.2	87.2
Lack of skilled labour	61.4	66.2	57.5	67.9	76.6	52.3	53.9	66.6	77.2	72.7
Corruption	58.3	31.4	80.0	30.8	67.6	76.7	88.2	94.2	77.1	94.6
Lack of confidence in government's econ. policy	56.3	58.4	54.6	64.8	87.0	40.8	76.4	77.2	60.3	79.1
Lack of innovation	55.3	44.0	64.3	55.2	87.4	53.4	85.1	86.2	64.9	75.1
Legal and administrative barriers for business	53.7	38.5	65.9	47.2	53.2	67.6	61.7	72.9	71.5	58.2
Inadequate Infrastructure	51.6	54.5	49.2	49.4	54.4	34.2	87.7	77.1	50.6	74.1
Lack of international competitiveness	43.6	33.4	51.8	39.7	42.4	41.9	71.9	77.8	71.4	71.0
Trade barriers to exports	42.8	32.9	50.7	15.8	21.4	61.0	30.0	49.6	32.8	40.2
Unfavourable climate for foreign investors	40.8	26.3	52.5	34.2	64.3	50.4	44.9	61.7	70.5	52.2
Inefficient debt management	39.8	32.2	46.0	23.7	55.7	48.8	38.6	13.1	59.8	58.4
Insufficient demand	36.6	19.4	50.4	26.4	37.9	44.3	63.5	68.6	51.9	77.0
Political instability	33.5	43.3	25.6	43.7	54.8	14.5	58.8	21.2	35.5	27.6
Capital shortage	29.2	11.4	43.5	24.2	77.3	28.4	49.7	79.1	80.4	78.0
Lack of credible central bank policy	13.3	7.1	18.4	6.8	44.2	12.8	14.9	29.2	45.9	19.4

*Based on percentages of experts indicating their country is facing this problem at the moment. Highlighted problems are the top 3 most important economic problems for each region .

Source: ifo World Economic Survey (WES) IV/2018.

The economic climate worsened in Sub-Saharan countries, with very negative assessments of the current situation, and less positive economic expectations (see Figure 8.2). In **Nigeria** and **Zimbabwe** both components of the climate deteriorated. In **Namibia**, the economic outlook brightened, but with the present economic situation very negative, the economic climate remains extremely poor (see Figure 10.2). Out of these countries, **Kenya** provides the best economic climate at -1.0 points on the balance scale. Economic expectations turned negative for the first time since July 2017. Overall assessments of the present situation remained good.

COLLECTIVE MEMORIES ON THE EUROPEAN DEBT CRISIS

Kai A. Konrad and Niklas Potrafke

Until late 2009, the European Monetary Union was seen by many observers as a great success and an important step towards an even closer Europe. The fears of many economists that the euro could become a soft currency failed to materialise. In the first ten years of the euro, the newly-established European Central Bank geared its monetary policy towards fixing the inflation rate in the common currency area at just under 2 percent. This goal was achieved surprisingly well. The introduction of the single currency was also accompanied by an almost complete convergence of interest rates on government debt of the member states of the European Monetary Union. This has significantly reduced the cost of financing public debt for many member states. Fiscal room for maneuver has arisen, which could be used both for consolidating public finances and for improving infrastructure and other government spending. The financing costs of the private sector also improved significantly in many of the member states. Overall, a majority of the member states experienced economic developments with substantial growth.

The picture clouded over in late 2009. At the beginning of 2010, a crisis became apparent. The conditions under which some member states were able to refinance their government debt deteriorated sharply. The era of convergence in public debt interest rates were over. The situation became particularly acute in Greece. Refinancing on the private capital market in May 2010 would only have been possible at astronomical interest rates, or not at all. The state was threatened with insolvency. As early as May 2010, a fund for possible emergency loans from individual member states was created through intergovernmental agreements. This marked the beginning of a long series of European crisis meetings, the expansion and consolidation of crisis management instruments, and reforms and additions to the European instruments of budgetary surveillance. Several European countries signed a Memorandum of Understanding with the European Commission, European Central Bank (ECB) and the International Monetary Fund (IMF) on a combination of financial aid and economic adjustment. In addition to Greece, the set of countries included Spain, Portugal, Ireland and Cyprus.

Looking back, 2010 can be seen as a watershed. The European Monetary Union switched from a successful course to a crisis mode, from which it did not really recover until 2018.

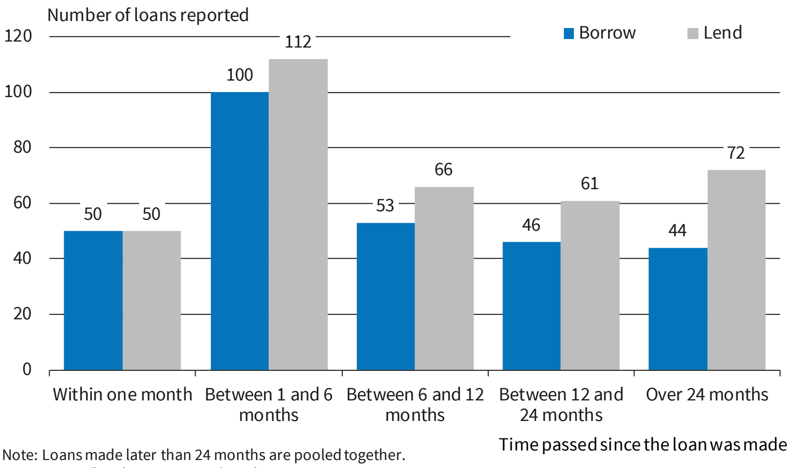
Parallel to these objectively describable courses of action, the process was perceived, interpreted and memorized by experts and the general public. Within the framework of the October survey of the WES, an attempt was made to "measure" this memory. The WES survey of experts within and outside Europe attempts to record how developments in the first two years of the crisis will be remembered in 2018. The questions are primarily aimed at the aid programs. The aim of the survey is to record the memories from some time distance of a few years. We record individual memories, but we are also able to sort these individual memories into collections of memories or collective memories of groups of experts.

More specifically, we asked the WES experts which countries signed a Memorandum of Understanding. Another question dealt with the main reason for how the Memorandum came about. WES experts were asked whether they (dis)agree with these statements: "The lender countries wanted to help the borrower countries", "The lender countries wanted to help themselves to avoid a major crisis at home", "The lender countries wanted to force their desire for institutional change upon the borrower countries". A related question is what are the true motivations and the political processes behind signing the Memorandum of Understanding. We asked experts which of the following three alternatives corresponds most closely to their perceptions: "The borrower countries wanted it, the lender countries were more reluctant", "The lender countries wanted it, the borrower countries were more reluctant", "Both wanted it equally". We also asked the WES experts how the rescue experience influenced the feelings of citizens in the lending and borrowing countries and friendship between the individual countries. Two questions dealt explicitly with Greece.

While the survey generates data on individual memories, various criteria for defining group member-

Figure 5

The Number of Reported Loans by Lenders and Borrowers as a Function of Time



Note: Loans made later than 24 months are pooled together.
Source: Dezső and Loewenstein (2012), p. 1003.

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ship can be used to turn the individual answers into what could be called collective memories. The national affiliation and the affiliation to the group of programme countries are among the possible identifiers defining group membership.

Psychologists and brain researchers provide extensive findings that individual memories can change plastically over time and have developed theories for the processes that determine this plasticity of memory. When measuring crisis memories, it is therefore possible that these memories have changed since the highlights of crisis intervention between 2010 and 2012. Of particular interest is whether these changes are of a systematic nature and can be assigned to specific group membership. Of particular interest is whether the country in which the interviewees work, or their affiliation to the countries that have submitted to a restructuring programme, are related to what the interviewees remember. Differences in memory could arise in terms of the events themselves, how they remember the causes of the crisis programmes, what motivations they attribute to the participants and how they remember the effects of the crisis programmes. The question as to how those persons assess or remember the perception of these events in the individual countries is also an important one.

Studies on the memory of financial relationships and on the divergence of memories of borrowers and lenders to date have dealt with credit between relatives and friends. Dezső and Loewenstein (2012) asked persons about their memories on informal credit relationships between relatives and friends. The results show quite drastic differences in memories that relate to motivations behind the loan, repayment dates, but also to the pure existence of the loan. Borrowers are more likely to forget about the loan than lenders. The differences in the memories of borrowers and lenders increase over time. Figure 5 shows the number of reported loans by lenders and borrowers over time. When the loan was made within one month, both lenders and borrowers report the same number of loans (50 to 50). When the loan was made between 6 and 12 months ago, by contrast, lenders report around 25% more loans than borrowers (53 to 66). The difference in reported loans is large when the loan was made 24 months ago (44 to 72).

The results suggest a self-serving bias: borrowers, in particular, remember to have paid back a larger part of the loan as they actually did; and they were also less likely to report that the repayment date had passed. Moreover, borrowers were less likely to recall that they agreed on an individual repayment date and more often reported that lenders initiated loans than lenders. When borrowers missed the repayment date, lenders often believed that lenders would never pay back the loan. Loans that have not been paid back on time also put a strain on the personal relationship between the lender and borrower. Lenders, in particular, were alienated when borrowers did not pay back the loan on time. Borrowers believed that delinquency would influence the relationship between lenders and borrowers to a smaller extent.

The credit relations between nations within the framework of a Memorandum of Understanding in the Eurozone are naturally of a different nature. For example, a citizen of the country receiving aid has no significant personal influence over the question of repayment or the implementation of agreed reforms. In any event, there could be differences in memories between the groups defined by nationalities, which are similarly self-serving and which make one's own group appear in a better light. Such differences may also influence relations between groups of citizens from different countries. The collected WES data can therefore be used to examine whether the collective memories of events of the European debt crisis diverge between countries and how this affects national identities or the relations between populations in Europe. A study that pursues this research agenda is Konrad and Potrafke (2018) and is currently in preparation. The results are discussed there and will be available soon.

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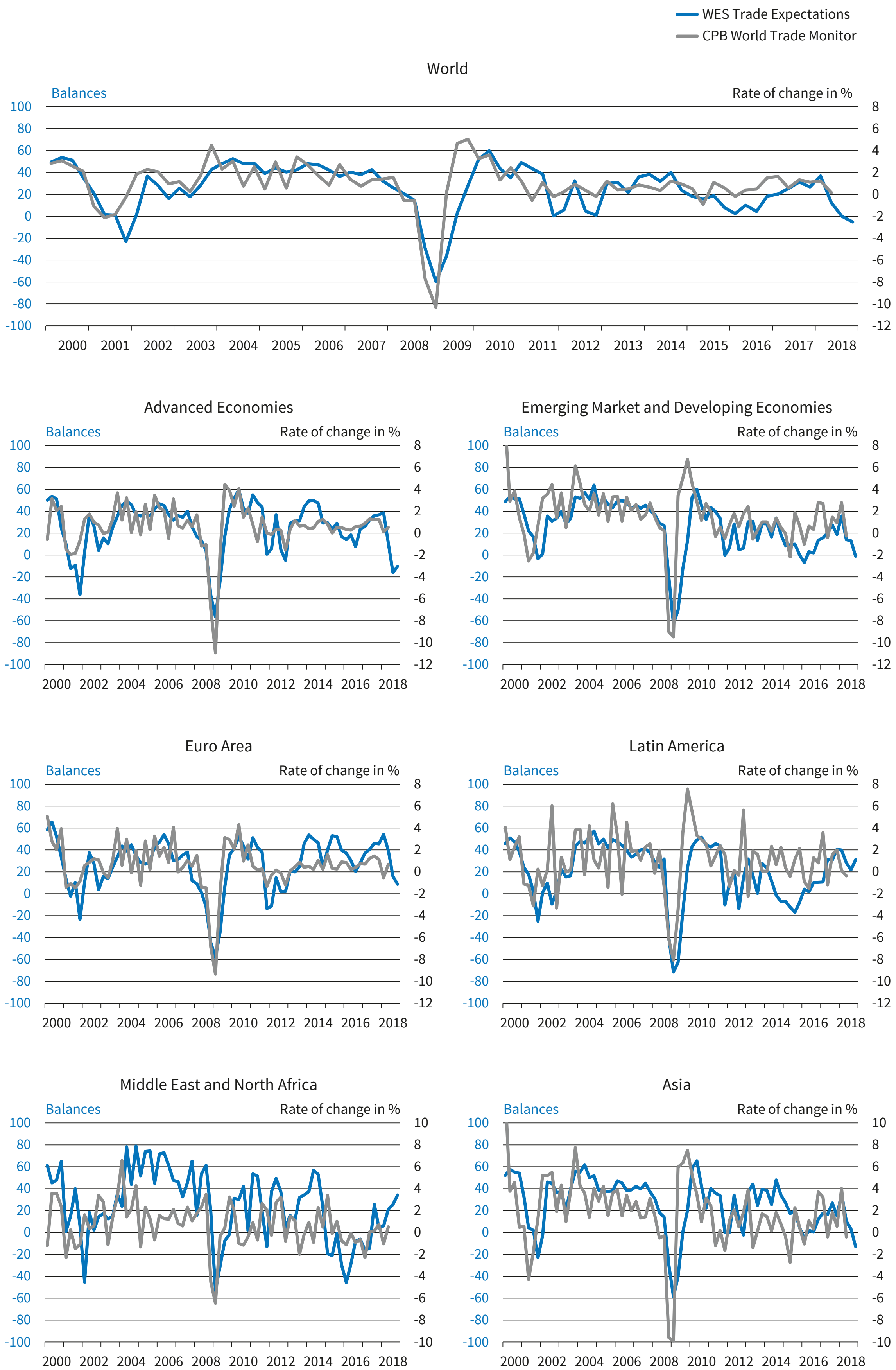
Konrad, K.A. and N. Potrafke (2018). Divergence of collective memory on European Financial Retrenchment – Implications of the European Union. *Working Paper*.

Figure 6

Comparison of WES Experts Trade Expectations and the CPB World Trade Monitor in Selected Aggregates



Source: ifo World Economic Survey (WES) IV/2018; CPB Netherlands Bureau for Economic Policy Analysis (CPB).

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Figure 7

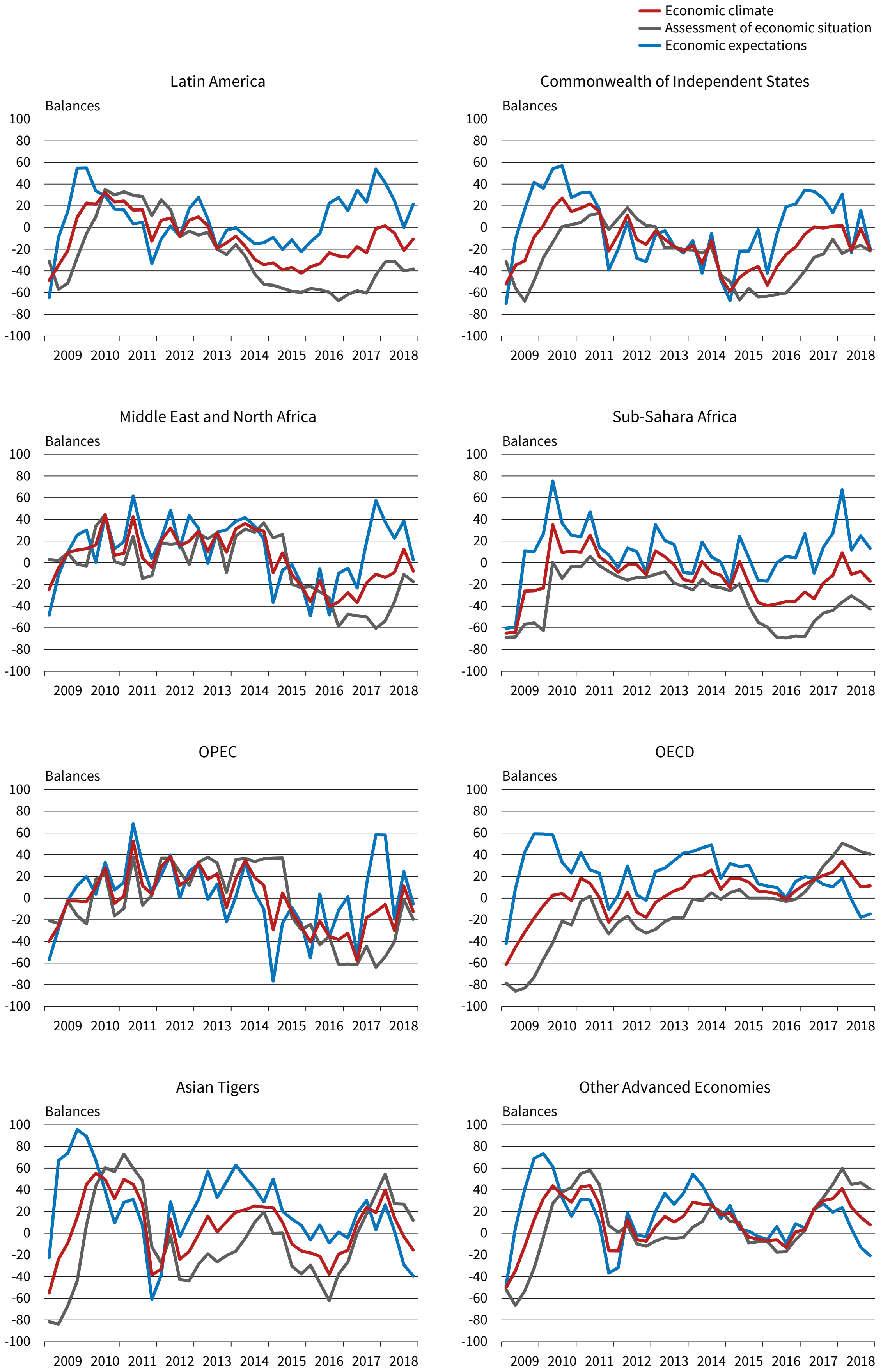
Expected Trend for the next 6 Months for Short- and Long-term Interest Rates

Source: ifo World Economic Survey (WES) IV/2018.

Figure 8.1
Selected Aggregates

Source: ifo World Economic Survey (WES) IV/2018.

Figure 8.2
Selected Aggregates



Source: ifo World Economic Survey (WES) IV/2018.

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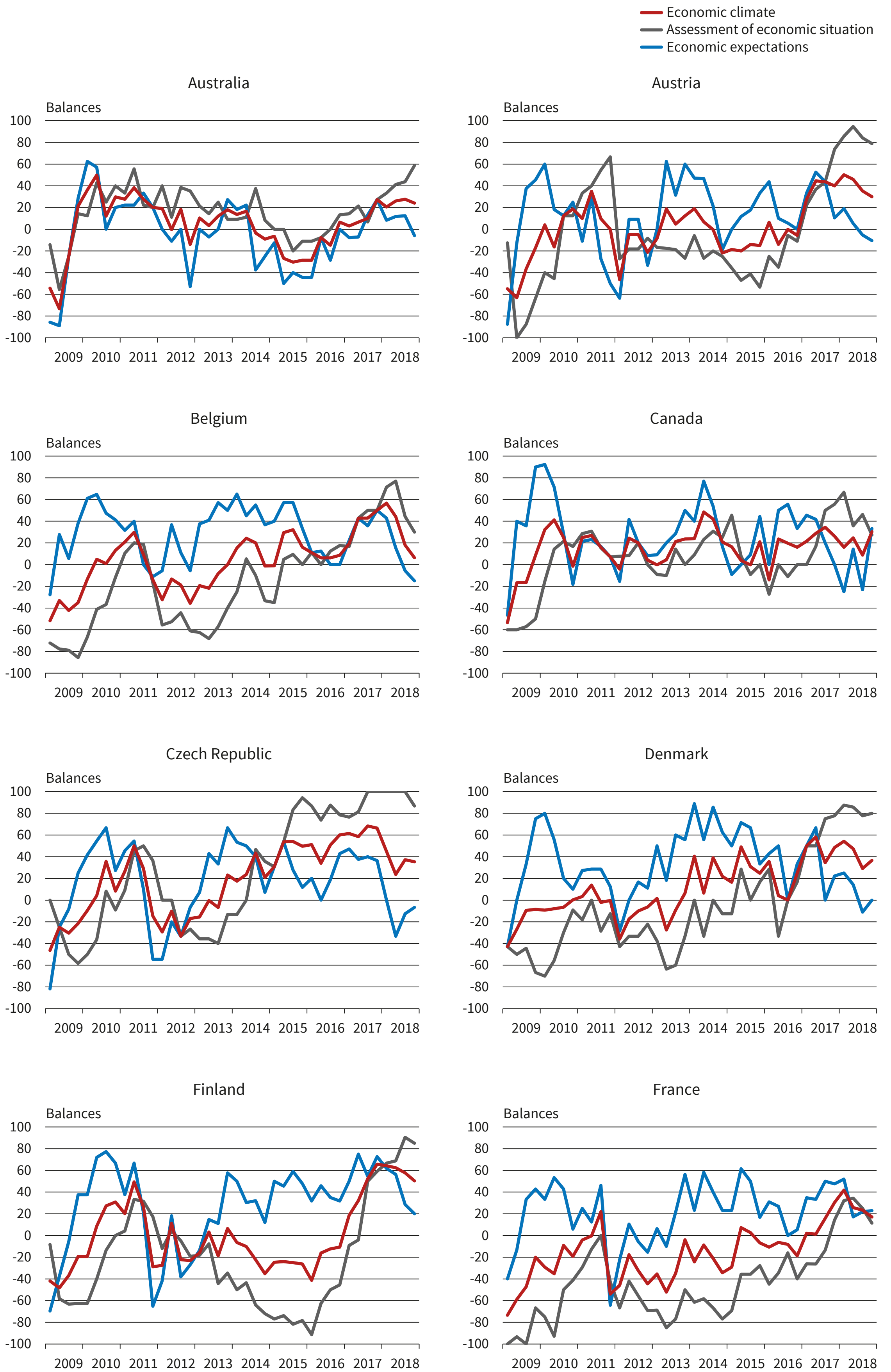
Figure 9.1

Advanced Economies



Source: ifo World Economic Survey (WES) IV/2018.

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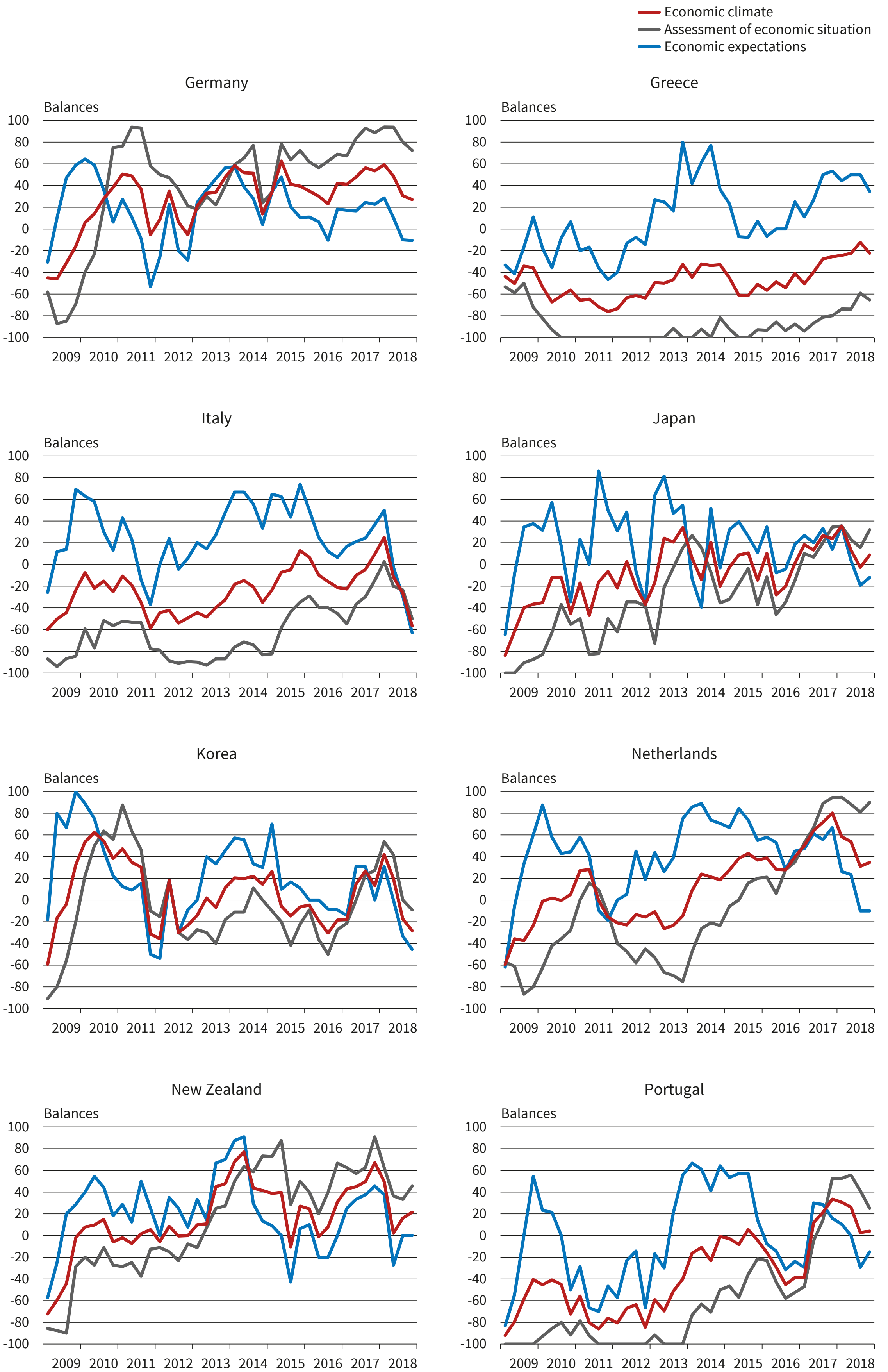
Figure 9.2

Advanced Economies



Source: ifo World Economic Survey (WES) IV/2018.

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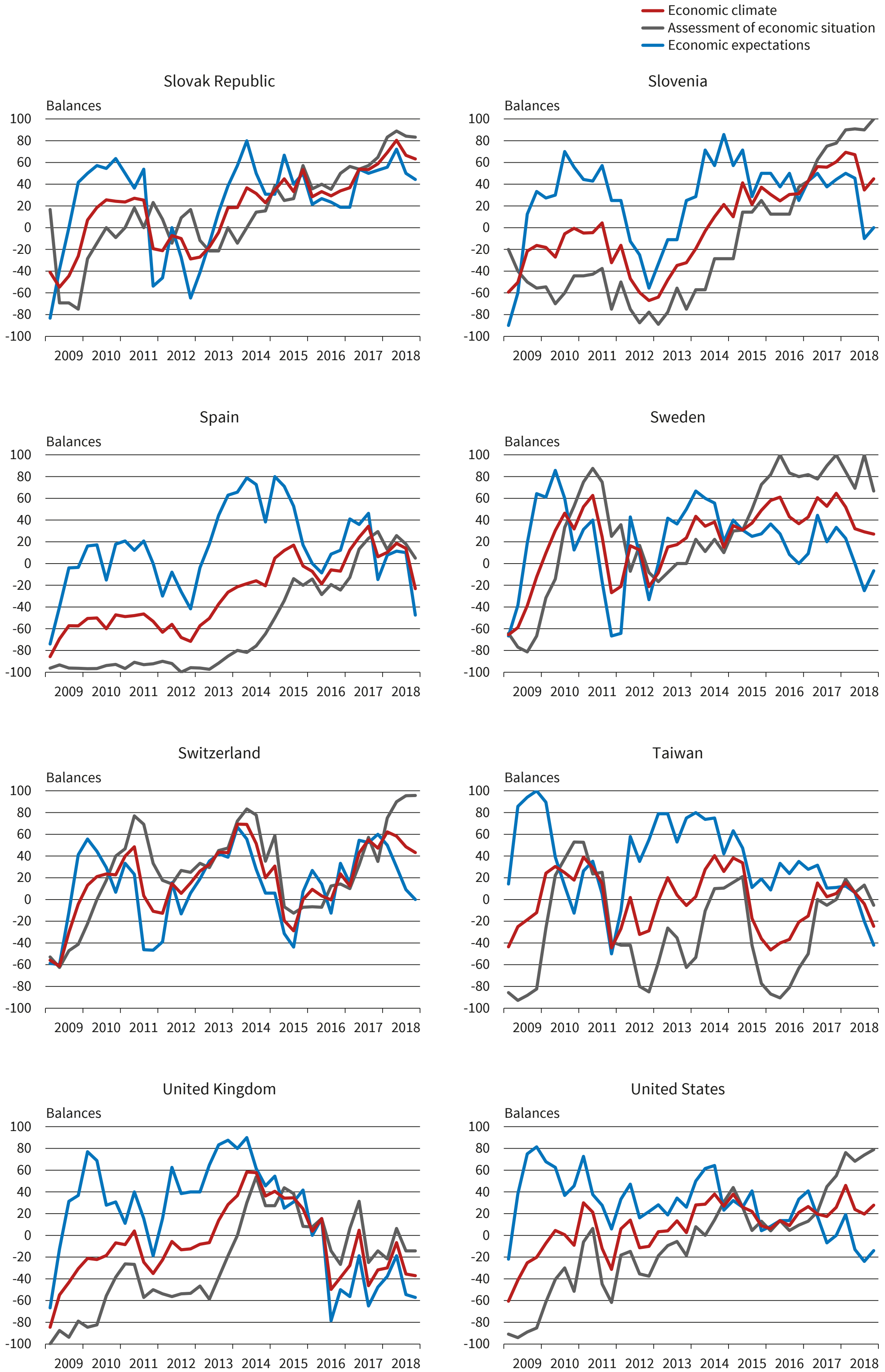
Figure 9.3

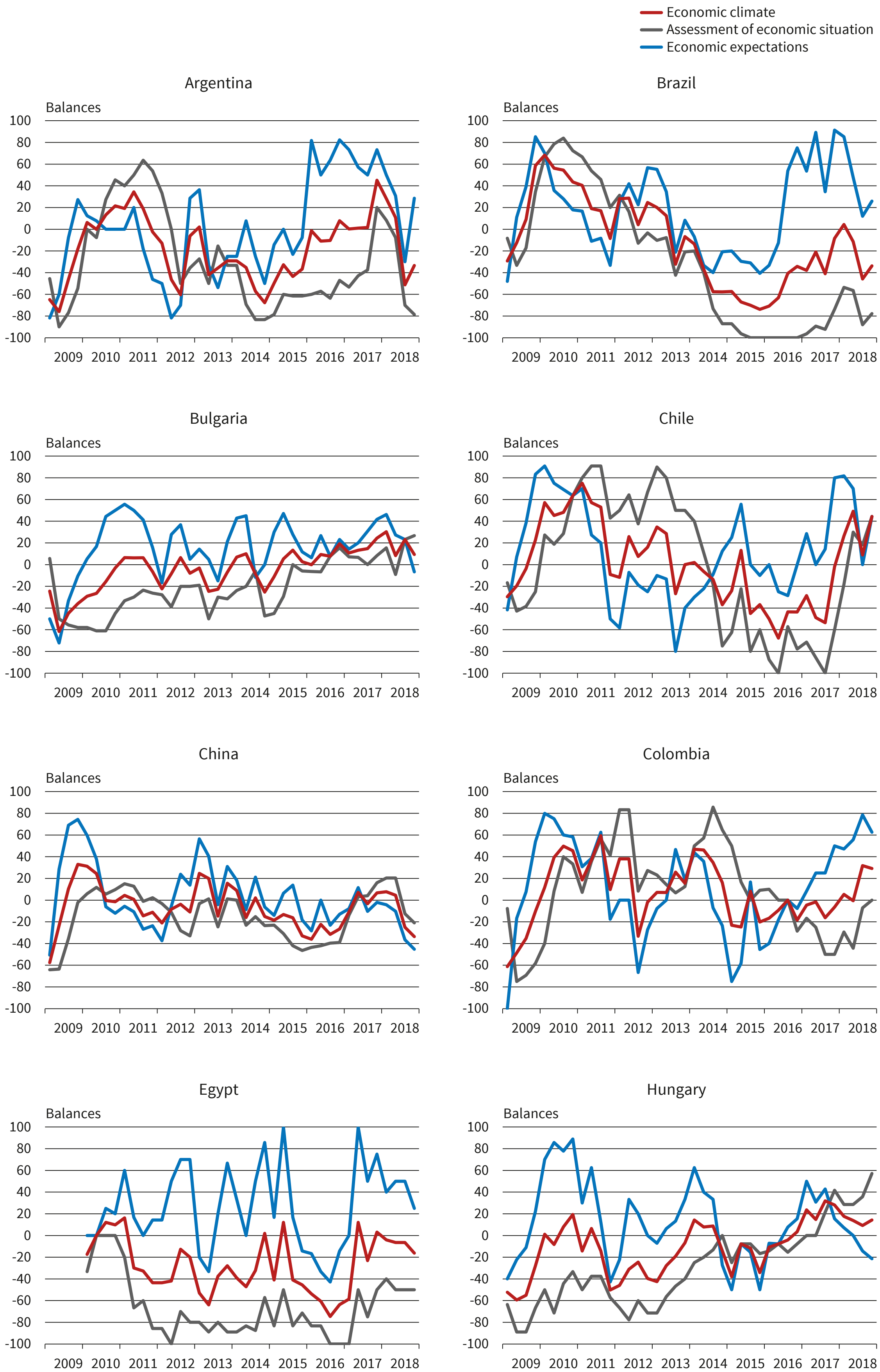
Advanced Economies



Source: ifo World Economic Survey (WES) IV/2018.

Figure 10.1

Emerging Markets and Developing Economies



Source: ifo World Economic Survey (WES) IV/2018.

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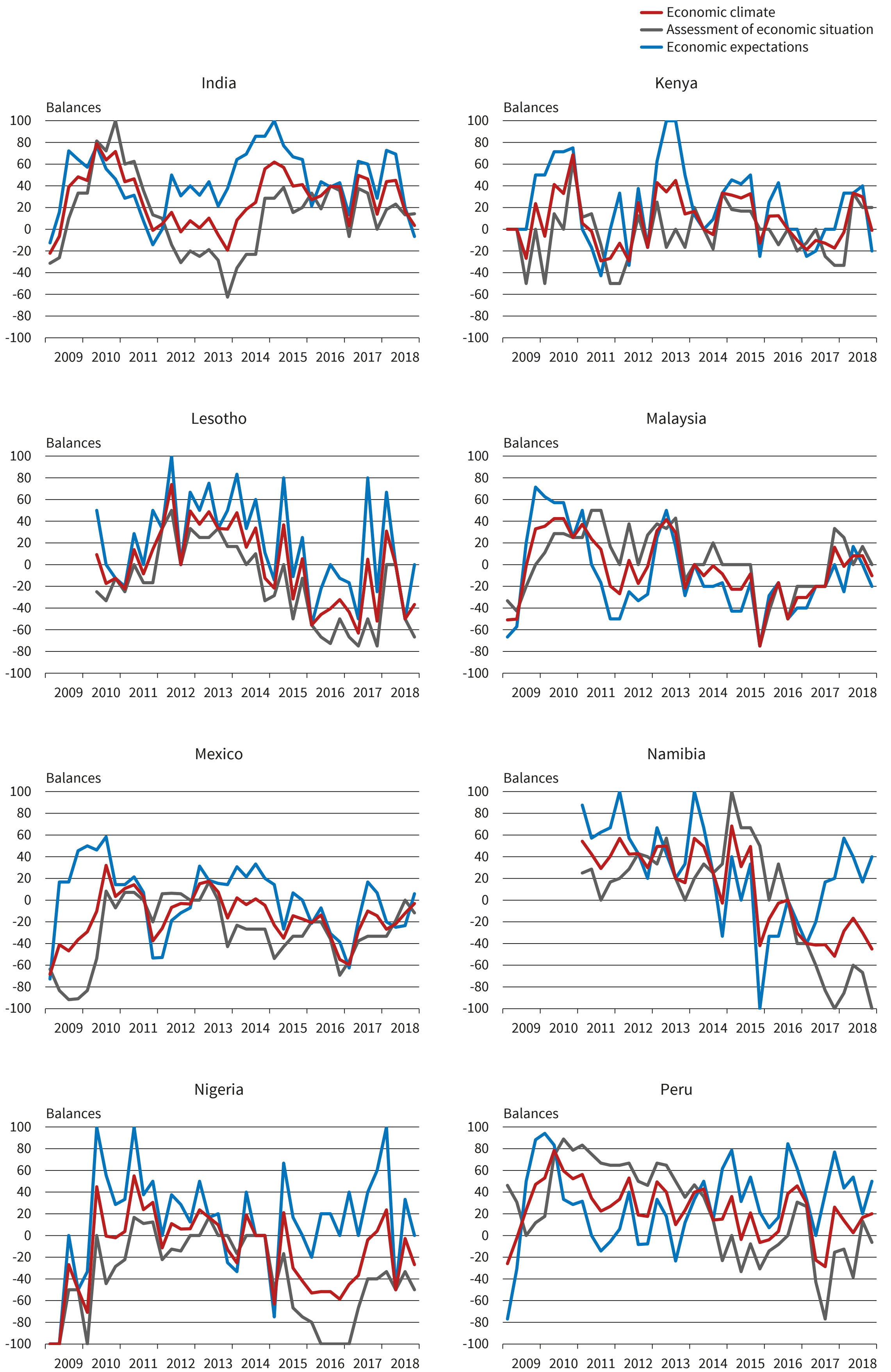
Figure 10.2

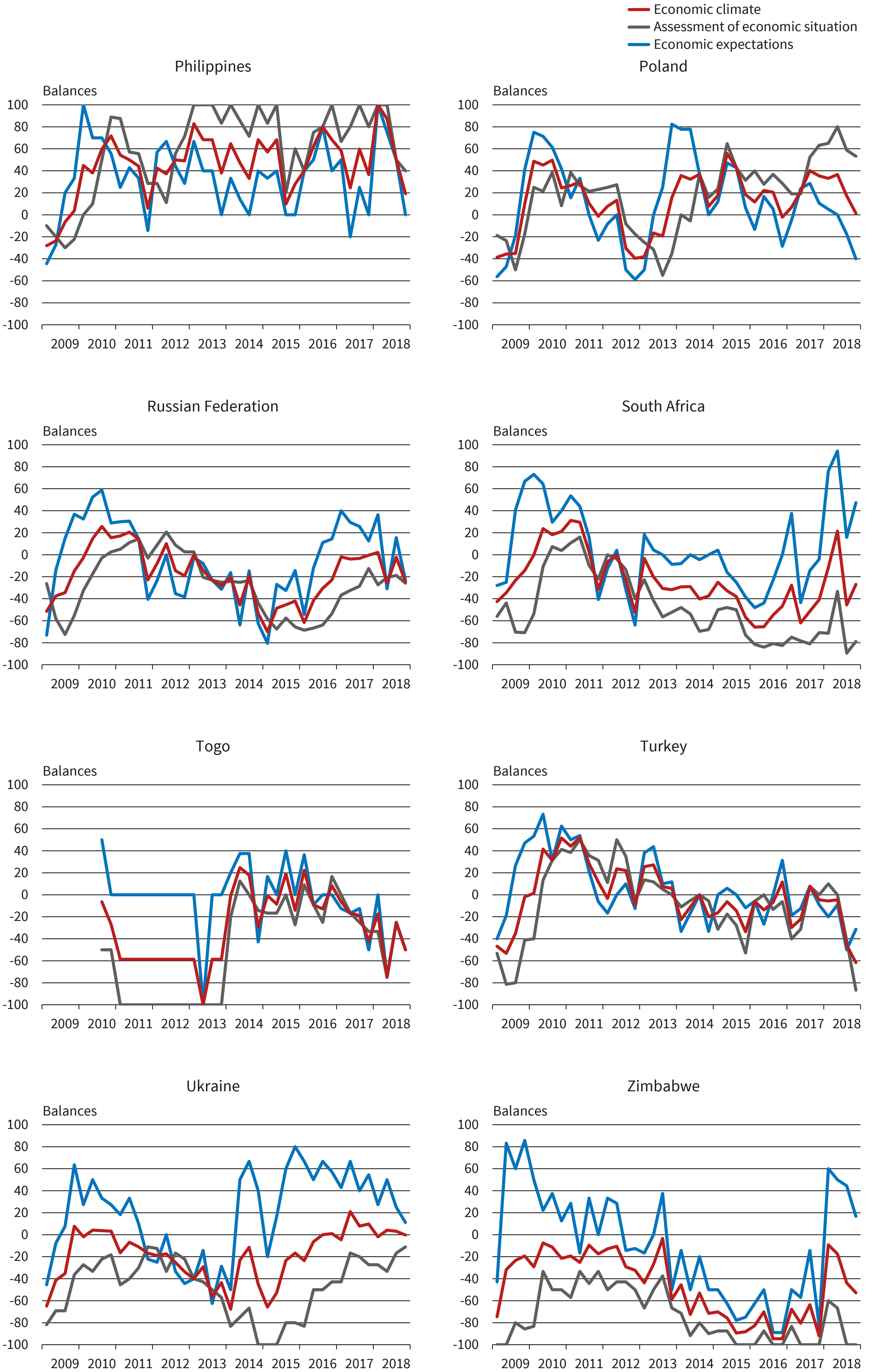
Emerging Markets and Developing Economies



Source: ifo World Economic Survey (WES) IV/2018.

Figure 10.3

Emerging Markets and Developing Economies



Source: ifo World Economic Survey (WES) IV/2018.