GLOBAL ECONOMY IN 2010[1]

The year 2010 was a year of relatively quick growth for the global economy. According to the International Monetary Fund (IMF), the global economy grew by 5% in 2010 after the 0.5% fall in 2009. The rapid growth was achieved in advanced economies due to the overly accommodating monetary and fiscal policy implemented by the central banks and governments to overcome the crisis. Economic activity dropped to some degree in the middle of the year, but began to rise once again in October.

Even though economy grew, several risks threatened the recovery, above all, the weak labour market and, in some countries, the weak housing market. The debt crisis faced by some euro area countries added to the risks, exerting pressure on the stability of public finances and the financial sector in the region, and stoking tensions on the financial markets. Several emerging economies, on the other hand, experienced a rapid capital inflow, facing inflationary pressures and the risk of overheating. Nonetheless, the outlook for global growth improved, with GDP growth of 4.4% forecast for 2011.

Regionally, economic growth was very uneven in 2010, with the advanced economies lagging behind emerging economies. Advanced economies showed GDP growth of approximately 3%, while the growth in emerging economies was over twice as high at 7.3%. The fastest economic growth, 9.5%, was witnessed by the developing Asian industrial countries, while China's economic growth was 8.7%, which was 1.1% higher than in 2009. The Central and Eastern European countries conquered the recession, with the region recording 4.2% growth in GDP year on year. Among major economies, the quickest economic growth was witnessed by Japan at 3.9%, fuelled by strong demand from other Asian countries. GDP grew by 2.8% in the United States of America and by 1.7% in the euro area.

The economic growth in euro area countries still remains uneven, as Germany saw growth of 3.5%, while several other economies came to a standstill or even contracted. The unemployment rate was 9.6% in the USA, 10% in the euro area and 5.1% in Japan.

Inflationary pressures remained modest in most advanced economies, starting to rise in the second half-year, fuelled by energy and food price hikes. With the dollar depreciating against other currencies, US monetary policy had a huge effect on the increase in raw material prices. The inflation rate for advanced economies rose from 0.1% to 1.6%. In emerging economies, the inflation rate rose from 5.2% to 6.2%, forcing several central banks to tighten their monetary policy.

Global financial markets continued to stabilise, with improvement in the outlook for economic growth in 2010. The debt crisis erupting in some euro area countries at the end of April forced Greece and Ireland to request financial aid from the IMF and the EU, and added to the vulnerability of several countries, especially Portugal and Spain. Against the backdrop of economic revival and improvement in the outlook for growth, the stock markets recovered to some degree, with different results seen in different countries. In the United States, for instance, the S&P 500 index advanced by 13%, while the euro area stock market index Eurostoxx more or less retained its previous level, dropping by 0.1%. The prices of raw materials soared. The CRB index, which covers the prices of 22 major raw materials, advanced by 24% during the year. The price of crude oil rose by 22% and there was still strong demand for gold, the price of which rose by 30% and exceeded 1,400 dollars per ounce. Money market interest rates remained at a low level while the long-term interest rates of the United States and the core euro area countries dropped.

[1] IMF "World Economic Outlook", April 2011; Reuters EcoWin.

United States and Japan

The United States recovered from the recession in 2010, with GDP growing by 2.8% year on year. Economic growth was supported by the growth in corporate investments and stock. Due to the weak labour market, the contribution of private consumption remained small, with foreign trade having a negative effect and imports exceeding exports. The annual growth in industrial production was 5.9%.

While the economy recovered, growth in employment remained sluggish. The average monthly growth in non-farm employment was 75,000 people. The unemployment rate dropped from 9.9% at the beginning of the year to 9% at the end of the year, a fall of less than one percentage point. Private consumption grew by 4.1% over the year, but the consumers' sense of security did not improve until the revival of the labour market at the end of the year.

The frailty of the economy could also be seen in the drop in the sale of residential buildings. The external balance of the US economy deteriorated in 2010, with the current account deficit rising to 3.5% of GDP.

The economic decline restored the level of inflation after consumer prices had fallen in 2009. Consumer prices increased by approximately 1.6% in 2010, but excluding energy and food prices, inflation fell to 0.6% by the end of the year.

In order to boost the economy and reduce the risk of deflation, the US Federal Reserve kept the federal funds rate at its historical low (0.0–0.25%) throughout 2010 and resolved to support the economy through the government debt purchase programme for a total of nearly 600 billion dollars. The government also continued to support the economy with an expansionary fiscal policy. Nonetheless, the state budget deficit shrank to some degree from last year.

The Japanese economy saw a rapid recovery in 2010, with GDP growing by 4.3% after the 6.3% drop last year. The economic recovery was mainly fuelled by the rapid growth in export-demand based industrial production as annual growth in industrial production was 4.9%. Economic growth decelerated at the end of the year, and GDP dropped somewhat. However, this is expected to be temporary. Japan's domestic demand has been relatively weak for quite a few years, with the annual growth in the retail trade remaining negative. Unemployment remained between 4.9% and 5.3%, showing no signs of improvement. Despite the recovery of economic activity, deflation persisted in Japan, even though by the end of the year consumer prices reached their level of 12 months ago.

China overtook Japan in GDP in 2010, becoming the second-largest economy in the world.

Euro area

Economic activity in the euro area showed signs of recovery in 2010. According to Eurostat, GDP in the euro area rose by 1.7%. Economic growth was supported by the rise in global economic activity which boosted export revenues. This, in turn, accelerated the growth in GDP.

The pressure exerted by inflation remained modest. The rate of inflation for 2010 was 1.6%, with price increases accelerating at the end of the year and reaching 2.2% in December. The price increase was mostly fuelled by external factors, meaning the increase in the price of food and energy on the global market. Core inflation, which reflects the inflationary pressures within the euro area, remained low, rising from 0.8% to 1.1% over the year. In most Member States, the pressure on prices is eased by huge levels of unemployment.

The lack of greater inflationary pressure allowed the European Central Bank to keep its key interest rate at the low level of 1% in 2010. The European Central Bank continued its main refinancing operations through unlimited fixed rate tenders throughout the year. The low level of the key interest rate and a favourable liquidity environment allowed it to lower loan interest rates and resuscitate the credit supply.

The economic recovery in the euro area has been uneven in the Member States. In some countries, unemployment has dropped to its pre-crisis level or below. In other countries, unemployment remained high in the second half of 2010, or even showed a further increase. The consolidation measures required for ensuring the sustainability of public finances may slow down the economic recovery, especially in countries which fail to generate significant export revenues.

The differences in the economic recovery and the public finance situation caused huge changes in the euro area government bond market. The risk premiums of several Member States increased rapidly, reflecting extreme uncertainty regarding the solvency of these countries in the market. At the beginning of May, the interest rate spread of the government bonds of several euro area countries over the interest rates for German bonds reached a record high since the launch of the euro. Given the significance of government bonds in the monetary policy transfer mechanism, the European Central Bank launched a bond purchase programme, allowing the Eurosystem to purchase government and private sector bonds. This programme helped to tone down the speculation over the sustainability of the public finance of some Member States at the beginning and end of the year.

The quicker-than-expected economic growth in 2010 suggests a further revival of the economy in 2011. The improvement in the labour market situation is expected to boost income, and the improved sense of security to temper the savings rate. In the short term, economic activity will, however, be hampered by the budget consolidation measures. For 2011, the European Central Bank forecasts growth of 0.7–2.1%[2], and the IMF growth of 1.6%[3].

[2] Eurosystem staff macroeconomic projections for the euro area, 2 December 2010.
[3] IMF "World Economic Outlook", April 2011.