

ACCOUNTANTS FOR BUSINESS

Global economic conditions survey report: Q2, 2010

ABOUT ACCA

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

Founded in 1904, ACCA has consistently held unique core values: opportunity, diversity, innovation, integrity and accountability. We believe that accountants bring value to economies at all stages of their development. We seek to develop capacity in the profession and encourage the adoption of global standards. Our values are aligned to the needs of employers in all sectors and we ensure that, through our qualifications, we prepare accountants for business. We seek to open up the profession to people of all backgrounds and remove artificial barriers, innovating our qualifications and their delivery to meet the diverse needs of trainee professionals and their employers.

We support our 140,000 members and 404,000 students in 170 countries, helping them to develop successful careers in accounting and business, based on the skills required by employers. We work through a network of 83 offices and centres and more than 8,000 Approved Employers worldwide, who provide high standards of employee learning and development. Through our public interest remit, we promote appropriate regulation of accounting and conduct relevant research to ensure accountancy continues to grow in reputation and influence.

ABOUT ACCOUNTANTS FOR BUSINESS

ACCA's global programme, Accountants for Business, champions the role of finance professionals in all sectors as true value creators in organisations. Through people, process and professionalism, accountants are central to great performance. They shape business strategy through a deep understanding of financial drivers and seek opportunities for long-term success. By focusing on the critical role professional accountants play in economies at all stages of development around the world, and in diverse organisations, ACCA seeks to highlight and enhance the role the accountancy profession plays in supporting a healthy global economy.

www.accaglobal.com/accountants_business

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ABOUT THE GLOBAL ECONOMIC CONDITIONS SURVEY

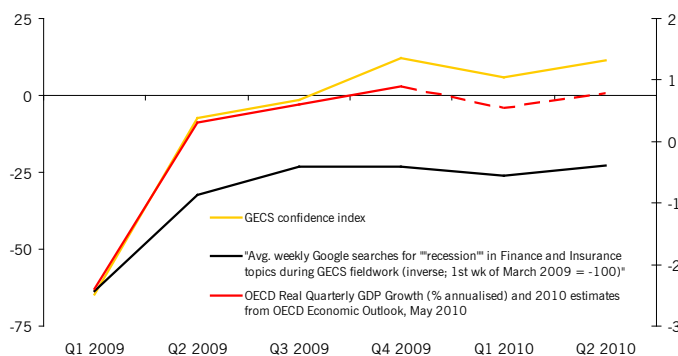
The ACCA Global Economic Conditions Survey (GECS) has been running on a quarterly basis since February 2009 and is now the largest regular survey of professional accountants in the world. The integrated dataset is a powerful and growing record of the global economic downturn and recovery, and helps guide ACCA's thinking on the state and prospects of the global economy.

ACCA believes that the insights of these surveys are of interest not only to the profession but also to the wider public. Whether they work in practice or industry, in the private or public sector, in SMEs or large corporates, accountants have front-row seats to the recovery. Indeed, early evidence suggests that the survey's indicators are reasonably good predictors of some aspects of global economic growth as well as of popular concern for the state of the global economy (Fig 1).

Since the publication of the latest report, the survey has been significantly streamlined in order to encourage responses from time-strapped professionals and focus ACCA's analysis on those indicators that offer the most incremental information. Fieldwork for the latest edition of the survey was carried out between 6 and 24 May 2010 and attracted 2,206 responses from professional accountants in 104 jurisdictions around the world.

The present report also features a new section, 'Views from the Coalface', containing the first set of reports from members of ACCA's panel of correspondents. This small group of professionals in key markets around the world have kindly agreed to share their insights and observations and help bring the survey's findings to life. We are especially grateful for their time and hope they will be the first of many.

Fig 1: GECS as a predictor of OECD growth and popular concern for the global economy



GLOBAL ECONOMY TESTS POSITIVE TERRITORY AS UNCERTAINTY GROWS

Six months after the first concrete improvement in the global economy’s fundamentals, the Global Economic Conditions Survey’s recovery index recorded its first –barely– positive value in the second quarter of 2010. Almost half of our sample (48.2%) now believe that conditions are either improving or about to, up from 46% in early 2010. Almost exactly the same percentage (48.1%) believe conditions are stagnating or deteriorating.

While any evidence of a net improvement in economic conditions is encouraging, it is impossible to overstate how marginal a change this quarter’s results actually represent.¹ Perhaps more importantly, the risk outlook for the global economy is deteriorating, with concerns about sovereign debt in Europe weighing down on respondents’ expectations. For the first time since these surveys began, the percentage of respondents saying that the global economy is deteriorating increased, reaching 14%. Additionally, the percentage of those who say they are unsure as to where the global economy is headed reached its highest level yet.

On the other hand, accountants’ confidence in their organisations has risen again in the last quarter, and at a faster pace than in early 2010. While the largest share of respondents (40%) reported no changes in their

confidence levels, the share of those reporting gains in confidence rose from 33% in early 2010 to 36%. Accordingly, ratings of government interventions also continued to improve despite a scaling back of exceptional support, with the government rating index rising higher than it did in mid-2009 in the aftermath of the co-ordinated fiscal and monetary response to the financial crisis. As of May 2010, 26% of respondents rated the response of their governments positively and 38% negatively.

It is important to note that different sectors of the global economy are recovering at very different paces. For the public sector in developed countries, there has simply been no recovery from the financial crisis. Confidence has been falling at an accelerating pace since early 2009, although the latest survey reveals a slightly improved outlook. On the other hand, public sector finance professionals in the developing world have enjoyed a respite during the last 12 months, but are now once again losing confidence.

In the private sector, large corporates and large financials saw conditions bottom out as early as the spring of 2009 and are, despite recent adverse developments, recovering quite fast. Small and medium-sized enterprises (SMEs), on the other hand, have plotted a middle course between the other sectors and their recovery has been slowing since late 2009.

1. The margin of error for the Q2 2010 sample at 95% confidence is ±1.7 percentage points.

Fig 2: Global economic conditions: Main indicators

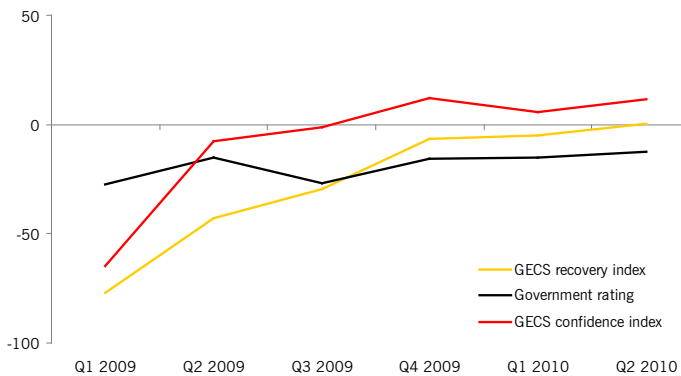


Fig 3: Business confidence by major sector



Key to the indices

Business confidence

The % balance of respondents saying that they have gained confidence in their organisations during the last period, minus those saying they have lost confidence in their organisations.

Distance from recovery

The % balance of respondents saying that the global economy is at the bottom and about to improve or already improving, minus those saying that it is at the bottom and will stay there or getting worse.

Government response

The % balance of respondents rating the response of their governments as 'good' or 'very good' minus those whose rating was 'poor' or 'very poor'.

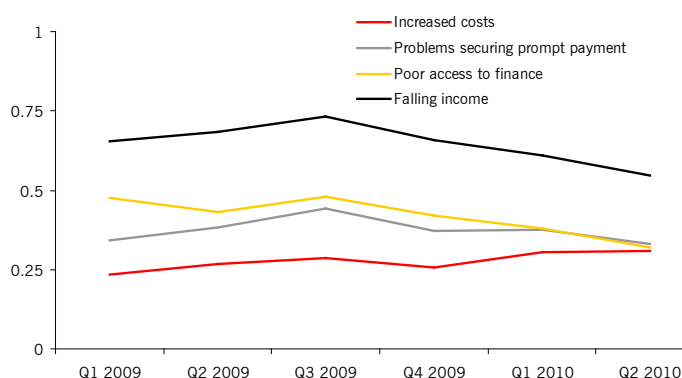
INFLATION WORRIES PERSIST AS TRADING CONDITIONS CONTINUE TO IMPROVE

Consistently with improving expectations and rising confidence, trading conditions continued to improve for accountants and their clients in the second quarter of 2010. Most encouragingly, only about a quarter (25%) of all respondents reported a drop in new orders, down from 36% in early 2010, suggesting that business incomes could recover further in the second half of the year.

In fact, almost all of our major risk indicators, including access to finance, demand, employment and insolvencies, peaked in the third quarter of 2009 and are now at levels lower than those of early 2009. The only exception is the incidence of late payment, which has been less responsive to improvements in economic conditions. This is because cashflow can come under pressure as undercapitalised businesses seize the opportunities of the recovery, forcing them to tap their own suppliers for liquidity.

Also, as noted in our last Global Economic Conditions Survey report, inflation is quickly establishing itself as a potential risk to the recovery. Nearly one third (31%) of respondents now report problems with rising operating costs, with small businesses (<50 employees) and non-profits hit the hardest. Cost pressures are most acute in the regions leading the recovery, with 39% of respondents in the Asia-Pacific region, 51% in South Asia and 52% in Africa reporting problems with rising operating costs, although only in Asia-Pacific can a clear upward trend be observed.

Fig 4: Risk indicators



AFRICA'S TURN TO PAUSE FOR BREATH; EUROPEAN RECOVERY STALLS

In early 2010, we spoke of Africa powering ahead as the continent was the only region still experiencing consistent and growing net improvements in trading conditions. This contrasted with the two –now three- consecutive cooling-off quarters in the Asia-Pacific region, where expectations were being scaled down by newly-cautious professionals.

It now appears that Africa is following the Far East in reconsidering the pace of recovery – 23% of respondents here (up from 21%) now believe that economic conditions are deteriorating or stagnating. In fact, since the two regions are linked by opposing flows of commodities and investment it is not unlikely that falling expectations in Africa are directly related to the slowdown in Asia. This interpretation may also explain part of the dip in confidence experienced by members in Africa in early 2010.

That said, the Asia-Pacific region is still the undisputed leader in the race out of the downturn: respondents in mainland China, Singapore and Malaysia were almost exactly as likely to report new job creation and hiring as they were to report staff cuts, suggesting a turning point could be at hand for employment and, by implication, demand. Finally, Central and Eastern Europe and the Americas have now moved decisively into positive territory in terms of confidence and trading conditions, with the recovery in both regions appearing increasingly secure.

All of this only serves to bring into sharper relief the problems of Western Europe. Despite emerging into positive territory for the first time in terms of confidence in their own organisations, accountants here still have little faith in the economic recovery in general – 21% of respondents (up from 15% in the last quarter) believe that global economic conditions are deteriorating; another 46% believe the global economy is stagnating. At the heart of pessimism in the region is the increasingly thorny issue of government debt and the prospect of sovereign defaults in the European periphery, but accountants are also aware of problems closer to home. When asked in the last two quarters of 2009, a full 50% of respondents in Western Europe said that they expected government spending to “fall sharply” in the medium term. As country after country announces details of the austerity measures to come, their predictions are set to be fulfilled.

Fig 5: Regional indices, distance from recovery

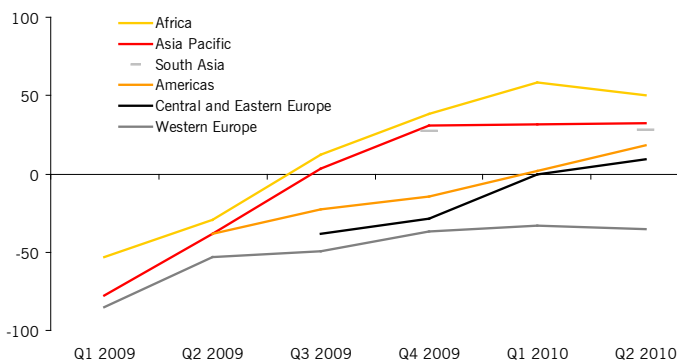
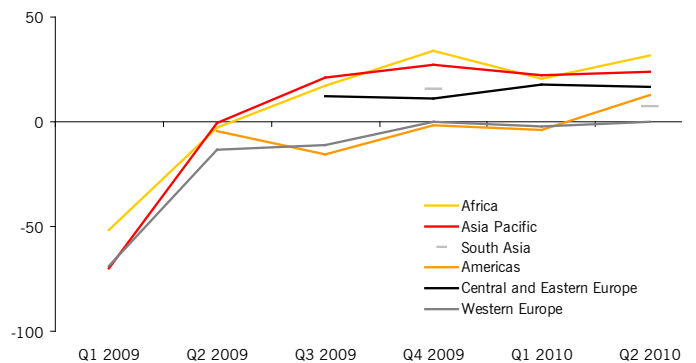


Fig 6: Regional indices, business confidence



INVESTMENT RECOVERY PICKS UP PACE; RICH NATIONS STIR AFTER HALF-YEAR LAG

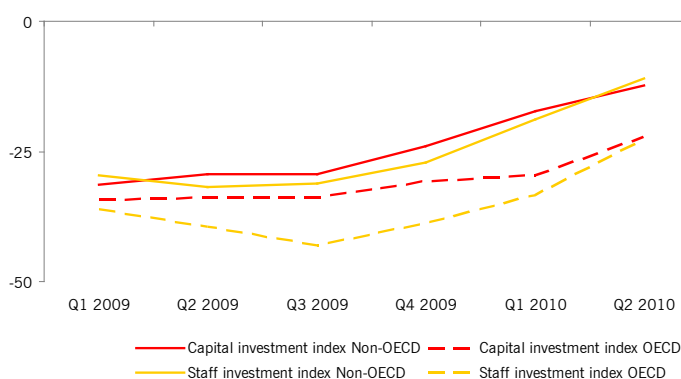
This quarter's GECS data suggest that investment may be closer to bottoming out than previously thought. Although only one in nine respondents reported a rise in investment of any kind, a substantial majority of respondents (70%, up from 66%) said that capital investment had remained constant and another 68% (up from 63%) said the same of investment in staff. This still means that both of ACCA's investment indices (staff and capital) are still in negative territory, but it also suggests that investment could start rising again at the global level between late 2010 to mid-2011.

This is the most substantial improvement recorded by the surveys so far, and part of it should be sustainable in the medium-term. This is because, despite a decline in the amount of government support available, profitable investment opportunities proliferated in the second quarter of 2010, while the availability of capital for investment eased significantly for the second quarter in a row, suggesting an end to the credit crunch might be in sight for businesses willing to take risks.

Respondents reported a net increase in the supply of finance for investment in Central and Eastern Europe as well as the Asia-Pacific region, with Russia, Singapore and Australia leading the recovery in supply. On the other hand, the supply of investment finance in mainland China has fallen for the second quarter in a row as banks continue to rein in excess lending.

On the whole, investment has recovered faster in developing countries, which have consistently led the developed world by around half a year, and investment in staff, which fell further than investment in capital in the early days of the downturn, is now recovering faster across regions.

Fig 7: Investment indices for OECD and non-OECD countries



DECISION TIME FOR BUSINESSES AS WINDOW OF OPPORTUNITY CLOSSES

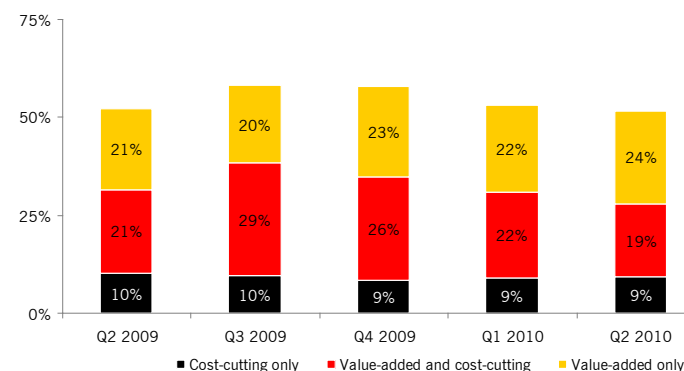
It was often said during the worst of the economic downturn that it would provide opportunities for astute business people. It is also a fact that entrepreneurial activity is a leading indicator of economic recovery.² The GECS data suggest, however, that the window of opportunity for capitalising on the conditions created by the downturn is closing rapidly. Business opportunities in general appear to have peaked in the third quarter of 2009, as the first wave of the recovery was underway, and have been falling since.

Moreover, it appears that businesses are increasingly having to choose between pure cost-cutting and pure value-added opportunities as they exhaust the potential for productivity gains. The incidence of business opportunities combining both approaches also peaked in the third quarter of 2009, and has since fallen consistently. This trend holds equally across most major regions,³ in both the developed and developing world. However, the GECS findings suggest a divergence in how the two have responded to this challenge. Respondents in the developing world are increasingly identifying pure value-added opportunities for their organisations or clients, while their colleagues in OECD countries are increasingly identifying cost-cutting opportunities instead. While it is still too early to interpret these trends, it is likely that they will have major consequences for the shape of the world economy if sustained.

2. P.D. Koellinger and A.R. Thurik, *Entrepreneurship and the Business Cycle*, Timbergen Institute Discussion Paper 2009-032/3, October 2009.

3. In Central and Eastern Europe, this trend had already begun by Q2 2009, while in Africa it only began in Q1 2010.

Fig 8: Business opportunities reported, by content



Views from the coalface

VIEW FROM JAPAN



Vince Hodgson, consultant, private retail consultancy, Japan

The most important factor for the Japanese economy is deflation, which continues unabated. Add to this the strength of the Yen against most major currencies, and the effects on an export-intensive

economy and natural-resource-light island nation are obvious. Recovery is an uphill battle and government policy lacks the vision and long-term determination to resolve the issues arising from an aging population and the costs associated with it.

The Bank of Japan (BOJ) has launched interbank funding at 0.1 % to try and support loans to business, especially smaller businesses. This is promising, but it will take many months for the effects to work through. Business is cautious in outlook, and banks are wary of lending even the BOJ's cheaper funds – which could defeat the government's intent.

Unemployment remains high and consumer spending remains depressed, both of which contribute to the retail industries' continuing downturn in an economy which, just like that of the US, is up to 65-70% dependent on consumer spending for GDP growth. University graduates are facing the second worst job opportunity statistics ever. The planned new child allowance tax benefit will probably be self-defeating as in most cases it will not be spent but saved during these difficult economic times.

Sustainability policies have had a big economic impact on the car and white goods industries since significant tax relief or points schemes have meant lower costs for consumers. Some of these will end in April 2011 at the latest and many have already concluded.

Although Japan's consumers are still brand-conscious, they are looking elsewhere. Low-price retailers are doing well, while the top end shows no real signs of recovery to pre-downturn levels. Amazingly, rental companies offering designer goods (handbags etc) for hire for special occasions are doing good business! After a period of severe price competition, supermarkets have settled on lower price products and reduced 'special offers'.

VIEW FROM THE STATES



**Robert Fernando, accountant,
public sector, California, US**

As we approach the next fiscal year, the economic devastation has taken its toll on the revenues which finance all levels of government, including my county. As a result, we are looking forward to another

difficult budget year. The current economic crisis and the associated collapse of the real estate market, increases in unemployment and a significant decline in consumer spending have resulted in negative growth in property tax revenue for the first time in forty years and loss of over a decade of sales tax growth. The same forces that have depleted the county's revenue have also caused deficits in the state's budget. The deficit in the state budget has an impact on the county budget too, as County receives part of the State's property tax takings.

While the level of the County's core revenues has declined markedly over the last three years, the purchasing power of the dollar has changed very little. That said, the present day dollar does not purchase the same amount of goods and services as a dollar did in 1999. This has, over time, resulted in a severe strain on the finances of the county and its ability to provide services to the public.

On the employment side, our management was forced, however reluctantly, to lay off some of our employees. In order to prevent the loss of further jobs, both management and general staff decided voluntarily to go on furlough one day of the month. This has reduced employees' take-home pay, which in turn has an influence on the amount of cash circulation in the county's economy.

The current economic atmosphere is not conducive to investment. Investors need a vibrant consumer market to sell their products, and the present atmosphere does not indicate such a market emerging in the near future. Consumers have become more frugal in their spending, focusing more on essentials and deferring purchases of non-essential and luxury items. Their reluctance to spend has affected the county's business environment and forced businesses to close down, which in turn has added to unemployment and the loss of business tax revenue. These, along with a shortage of credit facilities from banks and stringent requirements required by the banks to grant loans, are discouraging investors from embarking on new ventures.

This whole ruinous economic episode could have been avoided if economic pundits had acted prudently instead of relying on high-sounding economic theories beyond their own comprehension. It proves that there is no foolproof way of letting the market regulate itself: this invites unruly behaviour by the powerful and leaves the less powerful at their mercy.

VIEW FROM EUROPE



**Eric Verheijden, finance manager,
Air Products (industrial gasses
– over 1,000 employees)**

Living in Spain and being responsible for The Netherlands, Poland, Czech Republic and Slovakia, I can see different levels of economic recovery in the

different regions. Globally we do see improvements, mainly in Asia and the US with Europe still being behind.

With unemployment now above 20%, Spain is being viewed as one of the high risk countries within the EU and could follow Greece. For our company it remains the poorest region of the regions we operate in. Currently there are issues with the banks as well, and exposure to the property sector remains high.

In the Netherlands, Czech Republic and Slovakia we see a strong recovery compared to previous quarters. In Poland, we are still behind expectations, mainly due to a very strong winter in January that disrupted our services. Some of our customers still have major problems. Construction is slowly picking up, but shipyards are still suffering and we expect this to continue. In the Netherlands, we are investing quite a lot. We expect that we will probably reach pre-crisis levels next year.

We don't expect too much of an impact from the recent appreciation of the Polish zloty against the Euro, since most of our customers are domestic and are invoiced in the domestic currency..

CONCLUSIONS

An important milestone has been cleared in the second quarter of 2010 as the survey's recovery index finally crossed over into positive territory: a majority of respondents now believe that conditions are either improving or about to. However, as with similar thresholds in many other indicators, from GDP growth to PMI or consumer confidence, a positive reading does not necessarily mean the global economy has turned a corner.

Our members around the world continue to doubt the strength of the recovery. In Asia, expectations are now on hold; in Africa, they are being revised downwards; in Western Europe they are increasingly bleak. Where a new downturn is not the main concern (and even in some markets where it is), inflation is rising, with potentially disturbing implications for interest rates and, ultimately, growth.

However, encouraging signals also abound. The continuing improvement in our key indices, from employment and demand to cashflow and access to finance, is evidence of real progress. Investment is recovering faster than at any time in the past year-and-a-half, boosted by the emergence of new opportunities as well as improving access to finance.

These trends are matched by important transformations at the micro-level, as productivity gains level off and businesses are forced to choose the basis on which they will compete going forward. Most, especially in the developing world, are increasingly choosing to add value rather than cut costs.

As finance experts and business advisers, ACCA members will be crucial to helping organisations big and small, public and private, negotiate such choices and implement change. Going forward, this survey will continue to share their experiences with a wide range of stakeholders, shedding more light on the role of the profession not as observers, but as architects of the recovery.

ACCA AND THE GLOBAL ECONOMY

THE GLOBAL ECONOMY – INSIGHT AND ANALYSIS

Global economic conditions continue to dominate business life. They are at the top of the world's political agenda, and updates and debates on economic issues are almost constantly the centre of media attention. Economic downturns now exist in many countries, and it is far from clear how long the downward trends will continue before economic growth is seen again. Nor is it clear what the impact will be in countries and regions around the world, although it is important to recognise that different markets will be affected in different ways.

ACCA is a prominent voice both on the causes of the credit crunch and on what needs to be done to turn round the global economy. It has already published papers outlining its response to the G20's public agenda and analysis of the outlook for regulation of financial markets. It has also considered issues in accounting, such as fair value and the role of international accounting standards in supporting transparent business practices.

ACCA aims to demonstrate how an effective global accountancy profession contributes to sustainable global economic development; to champion the role of accountants as agents of value in business; and to support its members in times of challenge.

ACCA believes that accountants add considerable value to business by driving down costs and identifying drivers of value and profitability – and never more so than in the current environment. They are instrumental in obtaining access to finance and strengthening the balance sheet. Accountants are also essential to supporting the small business sector, estimated by the OECD to represent 95% of all enterprises. SMEs make a positive contribution to economic growth, requiring well-rounded finance managers and advisers to ensure small businesses survive and grow.

RESEARCH

ACCA is conducting a range of research projects to add to understanding of the effect of the economic conditions around the world, and ways in which the impact can be managed. The objectives of the research include:

- understanding trends and developments, including perceptions of changing prospects and opportunities in the current economic climate
- identifying areas of concern to members and assessing support and services which ACCA can offer to assist members in difficult economic circumstances
- championing the role of the accountant in business – especially the CFO – and illuminating areas of best practice which will help the companies where they work to add value to business strategy and operations, and to help their employers grow profitable businesses in difficult trading circumstances
- identifying ways in which accountants can add value as advisors, and
- understanding learning points and indicators for moving towards a refreshed global economy.

THE GLOBAL ECONOMY

Perhaps at the heart of the current debate on the economic environment is: where next for the global economy? As the G20 countries formulate strategy to promote stability and stimulate growth, the interconnectedness of our economies, and how they are managed and regulated, is firmly in the spotlight. The development of the global accountancy profession came out of, and has contributed to, the development of the global economy, with the aim of promoting common standards for accounting and auditing, and transparency in financial reporting. As a key stakeholder in the debate, ACCA will seek to address the challenges posed for the global economy, not least the need to ensure appropriate regulation, which favours fair competition, capital investment and economic growth; and the removal of barriers inhibiting the lifeblood of our economies – entrepreneurship and innovation.

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