ACCOUNTANTS FOR BUSINESS

Global economic conditions survey report: Q4, 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

ACCA's Global Economic Conditions (GEC) Survey has been running on a quarterly basis since February 2009. Since then, more than 10,000 questionnaires have been completed by our members for what is now the largest regular survey of professional accountants in the world. This powerful and growing record of business opinion continues to guide ACCA's thinking on the state of, and prospects for, the global economy.

Whether they work in practice or industry, in the private or public sector, in small businesses or large corporates, accountants have front-row seats to the recovery.

For this reason, ACCA believes that the insights from these surveys are of interest not only to the profession but also to the wider public.

Fieldwork for this latest edition of the survey was carried out between 22 November and 20 December 2010 and attracted 608 responses from professional accountants around the world. Our general findings point to:

- a reversal in the momentum of the recovery, with accountants' confidence in the recovery and the prospects of their own organisations falling back to the lowest levels in some time, possibly the last year and a half
- deterioration in key fundamentals such as business incomes and insolvencies
- continued resilience among small businesses but a strong reversal of fortunes for big financials and even more stress in the public sector
- continued weakness in investment as the supply of finance and government support recede.

As ever, we are grateful to all of the members that responded to the Q4 2010 survey, and especially to our regional commentators whose detailed reports are featured in Views from the Coalface (pages 7–9).

RECOVERY NOW TRULY IN REVERSE

ACCA has warned for some time that the global economic recovery was losing pace, weighed down first by sluggish demand and then by fears about sovereign debt. In our last report, we noted that a shift in the fundamentals could translate to further loss of momentum, and this has now come to pass. Respondents to the survey believe that the recovery is slipping away, with almost twice as many professionals (28%, up from 14% in the previous quarter) saying things are getting worse as three months ago. While nearly a third of the sample (32%, down from 47%) believe that conditions are improving or about to do so, on balance, faith in the recovery is at its lowest level in 18 months.

As a result, business confidence as recorded by our sample has now gone into negative territory for the first time since the third quarter of 2009, with the share of respondents reporting no change in their confidence levels (37%, down from 42%) falling below that of respondents who had lost confidence in their organisations (38%, up from 28%). As Fig. 2 shows, members in the private, non-financial sector are still –barely– reporting rising confidence, with those in small and medium-sized enterprises (SMEs) appearing to be more resilient. It is worth noting, however, the significant change in perceptions among members in large financials, in response to developments such as the looming threat of sovereign defaults in Europe. Finally, as we had feared, confidence among public sector accountants has now reached levels unseen even during the depths of the downturn and the loss of confidence in this sector continues to accelerate.

This quarter's data lend further support to our view that assessments of government policy are decoupling from economic conditions. While 38% of respondents (up from 33%) rate their governments' responses to current economic conditions as 'poor' or 'very poor', a relatively stable 26% (down from 27%) rate them as 'good' or 'very good'.

Fig. 1: Global economic conditions: main indicators

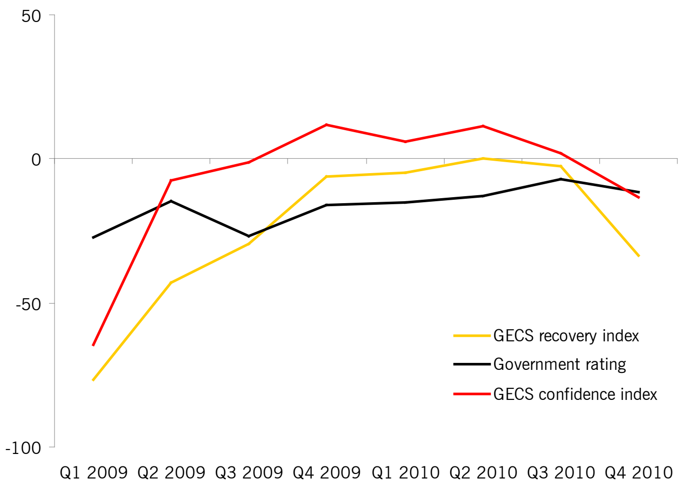
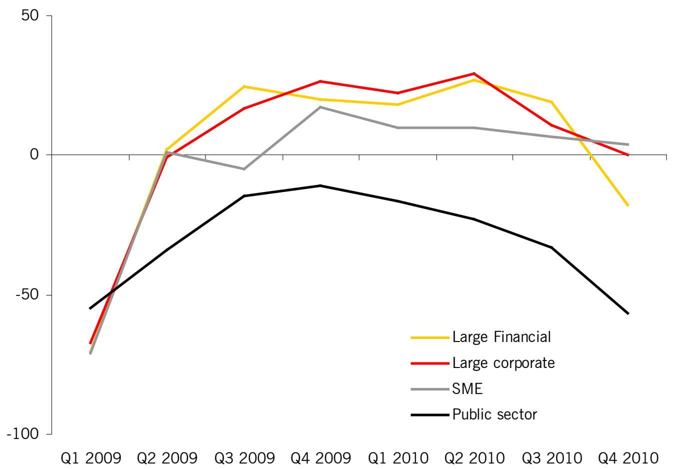


Fig. 2: Business confidence by major sector



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'.

RECOVERY IN INVESTMENT STALLS AS CASHFLOW WORRIES RESURFACE

As we anticipated in our latest report, cashflow appears to be coming under pressure globally, with the incidence of late payment and insolvencies rising. Although part of this trend was already observable three months ago, it was strengthened by the fact that the outlook for business incomes has fallen for the first time since the surveys began (see Fig. 5).

The recent deterioration in the investment outlook was not reversed in the past three months, with businesses apparently putting off decisions until the economic outlook becomes clearer. Only 8% of respondents reported a rise in investment of any kind (down from 14%), but the share of respondents reporting a scaling down of investment also fell marginally (from 38% to 37%). This has pushed both of ACCA's investment indices (staff and capital) slightly deeper into negative territory (Fig. 6).

Fig. 5. Risk indicators

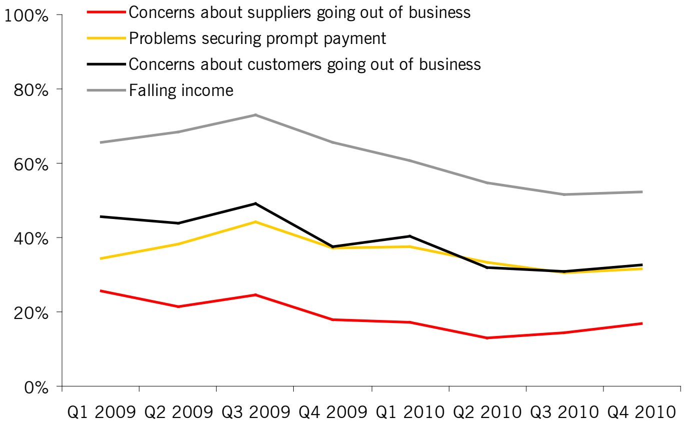
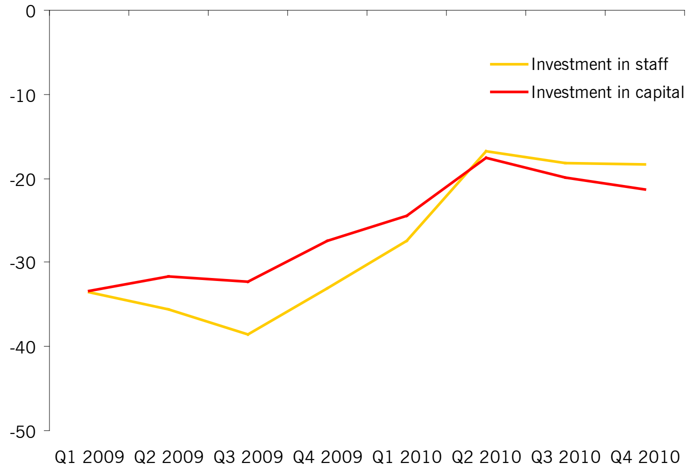


Fig. 6. Investment



As in previous surveys, the main reasons for the poor investment outlook were poor access to finance and a withdrawal of government support (Fig. 7). This time around, however, it appears that the outlook for finance has deteriorated faster than that for government support, while it is encouraging to see that perceptions of investment opportunities held up much better than in previous quarters. This is probably due to a fall in the number of businesses pursuing cost-cutting drives and to the continued attraction of niche markets.[1]

Apart from these developments, however, it is hard to see how investment opportunities have actually proliferated. If anything, analysis of the specific opportunities identified by the accountants taking part in this survey suggests that the ability of businesses to pursue value-adding opportunities or combine them with cost-cutting strategies was reduced further in late 2010 (see Fig. 8).

Fig. 7. Determinants of the investment environment

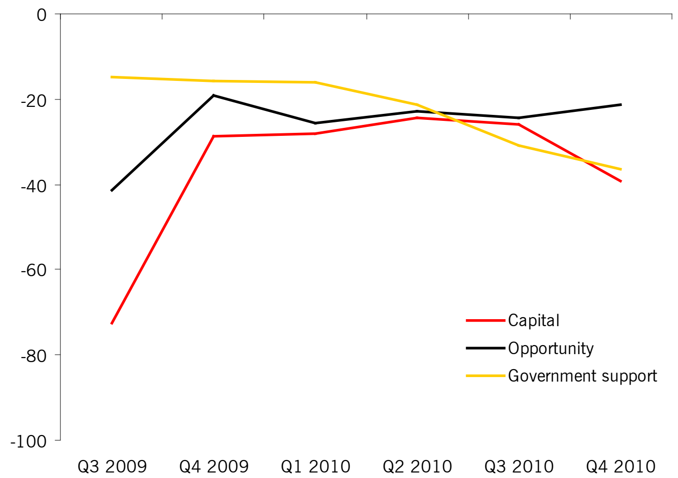
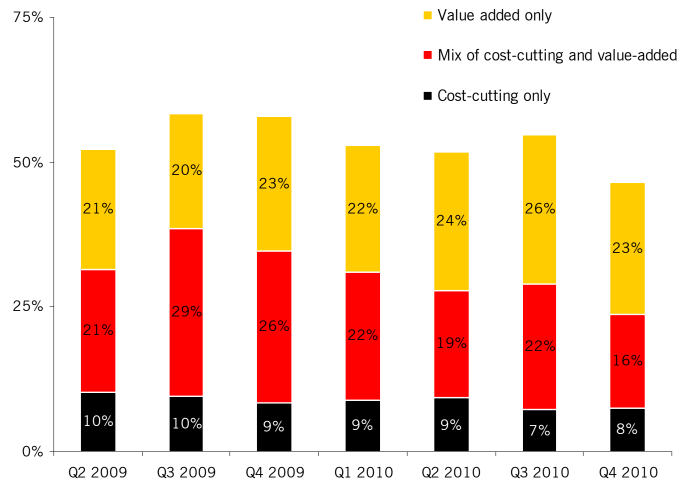


Fig. 8. Respondents reporting business opportunities, by type



1. These two types of opportunities are significantly correlated with the ‘investment opportunities’ index even after other opportunities are taken into account and were more frequent in Q4 2010 than in Q3 2010.

VIEWS FROM THE COALFACE

ROBERT D. PEARCE

CFO, Davis Langdon and Seah Asia Company Ltd[2]

It will come as no surprise to anyone that Asia is a booming market with lots of opportunity. Recent months, however, have produced new challenges for Asian companies. Articles covering the strength of the Chinese Yuan, imports and exports and inflation have introduced a certain feeling of uncertainty looking towards 2011.

Business in Asia has benefited from employing a highly skilled workforce and continues to do so. More people within the Asian region are turning to professional bodies such as ACCA or RICS and demand for skills is at an all time high.

The investment environment appears to be very positive throughout Asia, perhaps with the exception of countries like Japan and Korea. Clients continue to publish articles on a daily basis surrounding capital investment projects such as hotels, commercial buildings, condominiums, shopping malls and leisure facilities. Asia is increasingly becoming a more and more popular choice for tourism. In addition, countries throughout Asia have become a more attractive option for foreign investors since governments have incentivised foreign investment by offering tax incentives. Access to finance in Asia has so far not really been an issue.

The real challenge for Asia appears to be inflation. Published articles state that labour workforces in certain areas of China are demanding substantial wage increases (sometimes in the region of 30%). Some say the problem is caused by the soaring price of food. While some argue that pressure surrounding interest rates and inflation might be improved by an appreciation of the Chinese Yuan, it is not clear whether this would force China to become more of a consumer market as opposed to one focused on export trade. It is clear, however that this is a main area of concern.

The real positive item at the moment is that cash flow remains unaffected. Suppliers and clients alike continue to be very co-operative and there appears to be no impact on trade debtor days. However, it is fundamentally important to keep a watchful eye over bank and cash and frequently forecast trading in order to minimize risk.

In times like these I feel it appropriate that businesses establish a clear corporate strategy which is understood by all stakeholders and that basic internal controls are strengthened to the maximum. Staff training and retention appear key to the success of Asian business as more job opportunities become available in the market place.

ONG EE CO

Assistant vice-president, Bank of Tokyo-Mitsubishi UFJ (Malaysia) Berhad

Many have questioned whether the Malaysian economy might be affected by the uncertain global economic conditions and rising fuel prices. Despite these challenges, the Malaysian economic has remained stable, with moderate growth expected during the fourth quarter of 2010. Furthermore, this trend is expected to be sustained until the next quarter. The key lies with strong fundamentals and a vibrant domestic market.

The price of Crude Palm Oil (CPO), one of Malaysia's key exports, is currently at a 30-month high, as unpredictable weather resulting from the La Niña phenomenon has resulted in lower global CPO production and CPO prices rising above RM3,700 per metric tonnes by the middle of December 2010. Market analysts expect the high demand and prices for CPO prices to remain at least until the middle of 2011.

The impact of rising fuel prices may be critical to some industries in Malaysia. However, petroleum and natural gas are also one of the country's main exports. Rising fuel prices will result in higher revenue for the state-owned Petronas, and with oil and gas currently one of the largest sources of tax revenue for the country, this should in turn contribute to a rise in tax revenue.

Malaysia is also recognized as the largest Islamic banking and finance centre in the world. The issuance of *Sukuk*, or Islamic Bonds, in Malaysia totals $83 billion, and accounts for 65% of the total global *Sukuk* outstanding. The stock exchange, Bursa Malaysia is currently the world top exchange for *Sukuk*. On conventional stocks, the sentiment is currently bullish with indices reaching an all-time high in

2. Mr Pearce is based in the Philippines, but Davis Langdon and Seah Asia Company also have a presence in Singapore, Hong Kong, China, Philippines, Indonesia, Vietnam, Thailand, Brunei, Malaysia, Japan, Korea, India and Pakistan.

November 2010. The KLCI index has more than recovered from the pre-1997 financial crisis and exceeded the previous record set in June 2007.

On the real estate and properties front, strong demand and the rapid increase in residential property prices has raised concerns for the possibility of a 'property bubble', focused on selected localities around major cities. Residents complain of property prices appreciating by more than 20 percent annually over the past several years.

The Malaysian Central Bank, Bank Negara Malaysia, keeps a tight rein on the monetary supply and interest rates via the Overnight Policy Rate (OPR). The OPR was increased from 2.0% to 2.75% during the second and third quarter this year but remained unchanged for the fourth quarter of 2010. The inflationary pressure is well managed and expected to be less than 2% for 2010.

The vibrant domestic economy has kept unemployment levels low at 3%. In fact, demand for low-skilled workers, particularly in manufacturing, construction and plantation sectors, is currently being supported by about 1.8 million registered foreign workers - with Indonesia accounting for more than half while the remaining foreign workers are mainly from Bangladesh, Nepal and Myanmar.

In conclusion, the economic outlook of Malaysia has remained stable with moderate growth supported by strong domestic economic fundamentals during the fourth quarter of 2010.

ERIC VERHEIJDEN

Finance manager, Air Products

The last quarter has seen another bailout in Europe by the EU, with Ireland receiving a package of €85 billion. As a consequence Euro stock, bonds and the currency itself have declined. There are still fears that Spain and Portugal will also need to be bailed out against default at some stage, as they continue to come under pressure from the markets.

In general EU members are increasing tax rates to reduce deficits, with a lot of countries seeing VAT rates increase from 1 January 2011. Unemployment in Europe is around 10% (rising to as much as 20% in Spain), which puts pressure on governments' spending commitments.

Our company has had a strong financial year, but Europe lagged behind the US and Asia, and is expected to will grow more slowly than the rest of the world for the near future. Nevertheless, there has been an increase in operating profit due to restructurings carried out in the previous year and other cost-reducing measures. Sales increased considerably, mainly due to higher volumes.

We also saw a reduction in late payments and payment defaults which has improved our cash flow and lowered our bad debt allowances. Severe weather conditions in Europe are an added pressure, as we need to ensure we can supply our customer demand. So far we have dealt with disruptions in France, Belgium, The Netherlands, Germany and the UK.

The company expects increased capital spending, with considerable projects underway in the Netherlands and Belgium. We expect a continued, gradual global economic recovery in 2011 and remain focused on growth of volumes, winning new business and continuing to lower costs.

VINCE HODGSON

Consultant, private retail consultancy, Japan

The basic data and short-term outlook for Japan remain bleak. The latest Tankan survey of business confidence tanked, pointing to a significant slowdown over the next three months. The main economic headlines behind that are increasing national debt, expected to be 184% of GDP at the end of the fiscal year, continuing deflation and nominal GDP growth slowing from 3.1% in 2010 to 1.5 % in 2011. Over 50% of university graduates still have no job offers, the highest this percentage has been in twenty years, and the unemployment level remains stuck at over 5%. This may sound good, but it does not include the part-time (arbeito) unemployed.

Consumer demand, especially for cars and electrical goods, has been propped up in the last three months by government subsidies. These expire soon and already demand in both these areas is in decline. The November consumer confidence indicator showed its 5th consecutive decline and major department stores saw revenues fall 0.5% vs last year. In many cases, even the recently increased child benefit is being saved rather than spent as intended.

The government has recently cut corporate taxes by 5%, in response to a recent trend of outsourcing manufacturing plant and component sourcing to low labour cost countries who also offer tax incentives on the investment. Some electronics companies have backed out of plant construction or merged production facilities and the imposition of a 25% export tariff on rare earths from China is going to be an issue for car makers, battery and electronics manufacturers in the medium term.

Exporters are now feeling the effects of the strong yen on sales, with the major car manufacturers and electronics companies experiencing drops in demand especially in US/Europe as well as locally. The only bright spots on the horizon are exports to China and trade with Singapore, which are growing strongly. Overall Japan's industrial output is trending down.

Prospects for Japan joining the Trans Pacific Partnership (TPP) have unfortunately dimmed considerably, after running up against opposition from the farm lobby. Japan has in place huge duties - rice and butter producers, for instance, are protected with import duties of 700% and 350% plus respectively. It will apparently take ¥918.5 billion of 'farm income compensation' in the 2011 budget, on top of the effective import subsidies, to ensure the price of Japanese rice is competitive.

Opportunities for good business growth across the board are not good at all, except in niche sectors. Stagnation and deflation will unfortunately continue throughout 2011, and the BOJ are running out of options - they are making money available but it's not being taken up.

CONCLUSIONS

In our last report (Q3, October 2010), we noted that the *Global Economic Conditions Survey Report* Q4, 2010 'may be the most important one yet; this quarter [Q3] could prove to have been a temporary pause for breath or the beginning of a second downturn.'

Although it is still too early to draw definitive conclusions, our findings so far suggest that the latter is the more likely scenario.

With an ever-widening array of fundamentals turning against the recovery and governments seen as powerless to prevent a new downturn, expectations have fallen substantially among respondents to the survey. However, it is important to bear in mind that very little of this gloomy forecast has yet translated to falling business confidence – which suggests that some of the most pessimistic scenarios may yet be proven wrong.

Even in that case, however, the return of uncertainty and systemic risk means that a great deal of economic activity will be put on hold while entrepreneurs and managers wait for the dust to settle. Barring another major systemic event this 'wait and see' attitude will most likely persist for most of early 2011, and could test the strength of the recovery severely before it dissipates.

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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