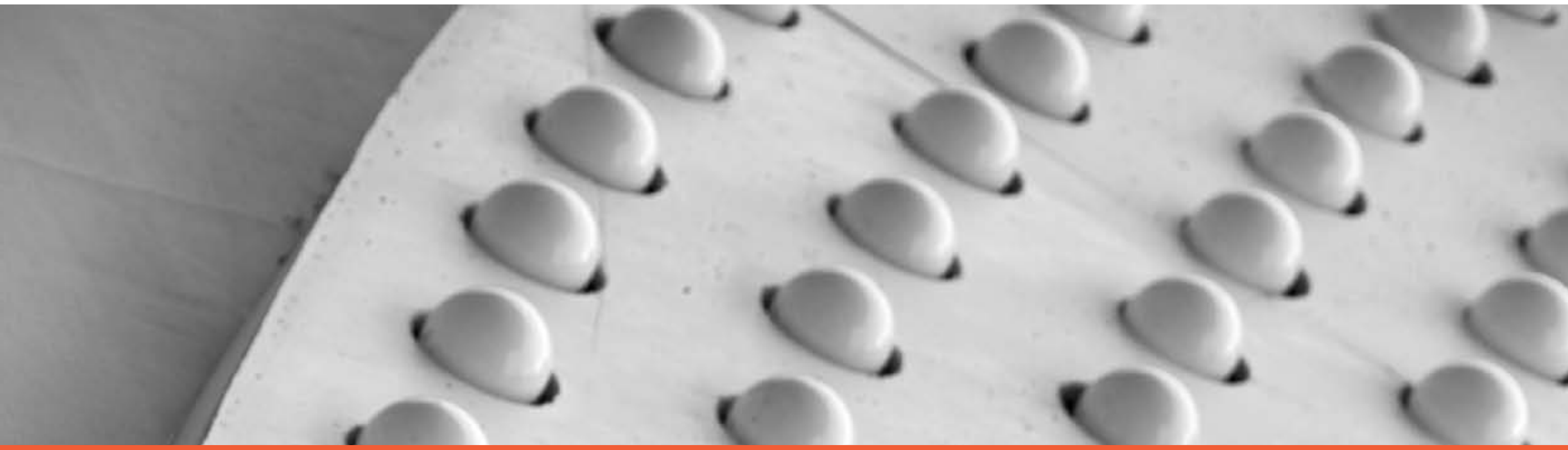
The Association of Accountants and Financial Professionals in Business

The global body for professional accountants



Global economic conditions survey report: Q3, 2013

ACCA AND **IMA**: GLOBAL BODIES EMPOWERING ACCOUNTANTS AND FINANCIAL PROFESSIONALS TO DRIVE BUSINESS PERFORMANCE

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 in all stages of development. We aim to develop capacity in the profession and encourage the adoption of consistent 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 work to open up the profession to people of all backgrounds and remove artificial barriers to entry, ensuring that our qualifications and their delivery meet the diverse needs of trainee professionals and their employers.

We support our 162,000 members and 426,000 students in 170 countries, helping them to develop successful careers in accounting and business, with the skills needed by employers. We work through a network of over 89 offices and centres and more than 8,500 Approved Employers worldwide, who provide high standards of employee learning and development.

About IMA®

IMA® (Institute of Management Accountants), the association for accountants and financial professionals in business, is one of the largest and most respected associations focused exclusively on advancing the management accounting profession. Globally, IMA supports the profession through research, the CMA® (Certified Management Accountant) program, continuing education, networking, and advocacy of the highest ethical business practices. IMA has a global network of more than 65,000 members in 120 countries and 200 local chapter communities. IMA provides localised services through its offices in Montvale, N.J., USA; Zurich, Switzerland; Dubai, UAE; and Beijing, China.

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Global economic conditions survey report: Q3, 2013

About the survey

The Global Economic Conditions Survey (GECS), carried out jointly by ACCA and IMA, is the largest regular economic survey of accountants in the world, in terms of both the number of respondents and the range of economic variables it monitors. Its main indices are good predictors of GDP growth in the OECD countries and daily trend deviations correlate well with the VIX or 'fear' index, which measures expected stock price volatility.

Fieldwork for the Q3, 2013 GECS was carried out between 15 August and 4 September 2013, and drew 2,021 responses from ACCA and IMA members around the world, including 154 from CFOs. Readers should note that fieldwork was concluded before the US government shutdown of October 2013 could become a significant concern.

This is the eighth survey jointly carried out by IMA and ACCA and the nineteenth since the series began in early 2009. As always, we are grateful to all ACCA and IMA members who took the time to share their insights. As finance professionals, they have front-row seats to the recovery, and their collective views can tell a more complete and more accurate story than economic indicators alone.

Perceptions of the recovery are at a 4½–year high in Q3

Business confidence rose again in the third quarter of 2013, with 28% of respondents claiming they were more confident about the prospects of their own businesses than they had been three months earlier, up from 26% in Q2. Nearly a third (32%) reported a loss of confidence, down from 35% in the previous quarter.

While business confidence is still rising modestly, perceptions of the recovery are improving at a very rapid rate. The majority of respondents (53%, up from 47% in Q2) now believe economic conditions are improving or about to do so, while the pessimists' share is down from 50% in Q2 to 43% in the third quarter. Governments around the world are beginning to capitalise on the recovery, with respondents rating their economic policies higher again after a year of intense disapproval.

Putting these findings in perspective, it appears as though faith in the recovery was stronger in the third quarter of 2013 than it's ever been since the GECS began in early 2009 – it is also the first time in the history of the survey that the optimists have outnumbered the pessimists. The same analysis reveals that business confidence has now reached levels last seen in the third quarter of 2010 (see Figure 2).

Figure 1: Major GECS indicators for the global economy

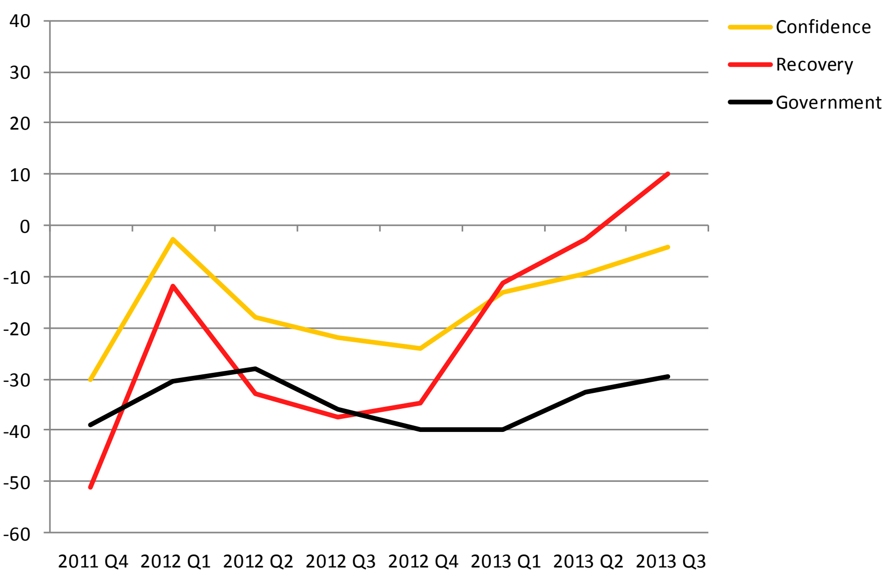
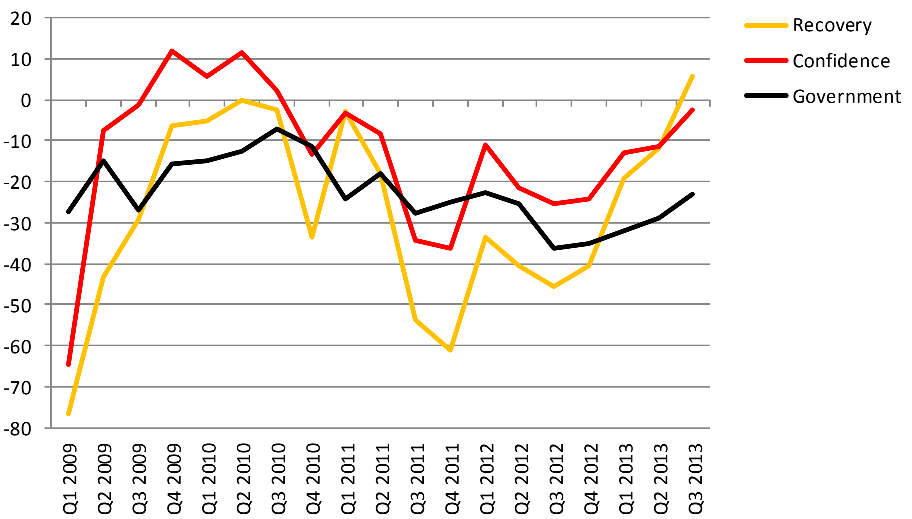
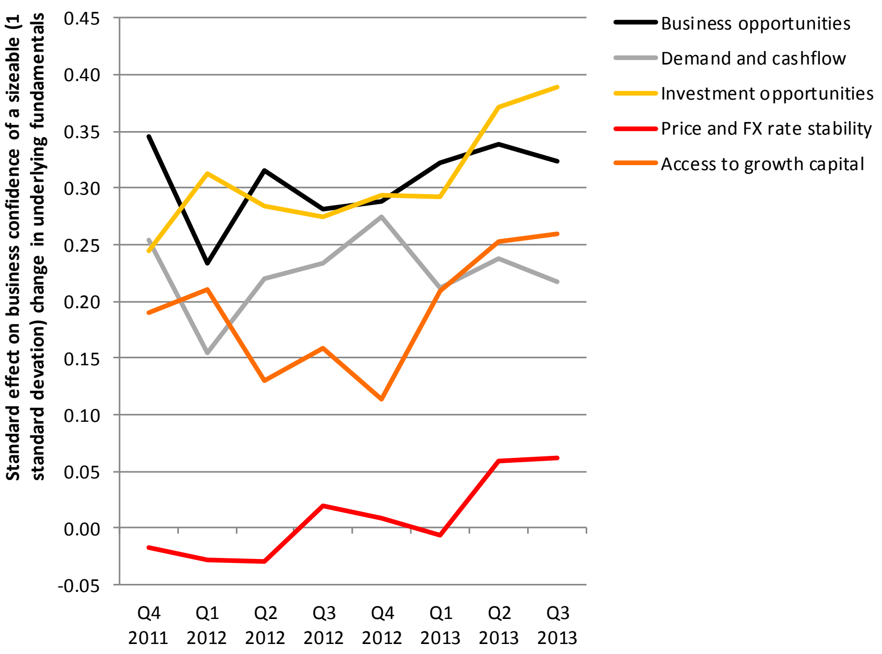


Figure 2: Major GECS indices – complete historical series (ACCA members only)



Business confidence is over-reliant on easy money

Figure 3: How sensitive is global business confidence to the fundamentals?



Once again, perceptions of the recovery improved much faster in Q3 2013 than business confidence, which in turn improved faster than the underlying fundamentals. Our Q2 2013 report warned that much of the growth in business confidence at the global level depended on a surge of monetary stimulus, which was reflected in improved access to growth capital and investment opportunities around the world. This dependence has, if anything, increased in the third quarter, but the flow of capital has, in much of the world, gone into reverse. The reason for this behaviour appears to be a major shift in demand for riskier assets as investors adjust to the prospect of central banks reining in their asset purchases, and monetary policy in general.

As Figure 3 shows, business confidence around the world has become increasingly sensitive to the supply of investment opportunities, access to capital for investment and predictable monetary policy over the last 12 months.[1] On the other hand, the influence of business opportunities has risen only moderately and that of demand and cashflow conditions has fallen. Indeed, both of the latter two factors fell in significance in Q3 2013.

1. The five indices (business opportunities; investment opportunities; demand and cashflow; price and FX rate stability; and access to growth capital) are derived through factor analysis from the full range of 30 GECS questions regarding the state of the business and investment environment. The factors' individual effects on business confidence are determined through ordinal regression analysis, after controlling for business size, complexity, sector and country, as well as respondents' role and gender, and their perceptions of the recovery. The use of varimax rotation ensures that the five indices are uncorrelated, which means that 'investment opportunities' do not include opportunities to invest in organic growth, which are instead summarised under 'business opportunities.'

This picture is not consistent with a healthy global recovery. While it is positive to see confidence respond to investment conditions, these indications paint a picture of a recovery increasingly dependent on current and future monetary stimulus. As the Bank for International Settlements (BIS) explained[2] in its September 2013 outlook:

'Announcements in May that the Federal Reserve envisaged phasing out quantitative easing…triggered a surge in benchmark bond yields that spilled over across asset classes and regions. …The sell-off abated in early July when the Federal Reserve, the ECB and the Bank of England reassured markets that monetary policy would remain accommodative until the domestic recovery was on a solid footing. As the rise in long-term interest rates continued, however, markets effectively precipitated a tightening of financial conditions worldwide.

The policy announcements occurred after a prolonged period of exceptional monetary accommodation in advanced economies, just as the economic outlook there was turning positive. They caught markets by surprise, reminding them that negative term premia cannot last indefinitely.'

Figure 4: GECS Business Dynamism Indices in OECD countries

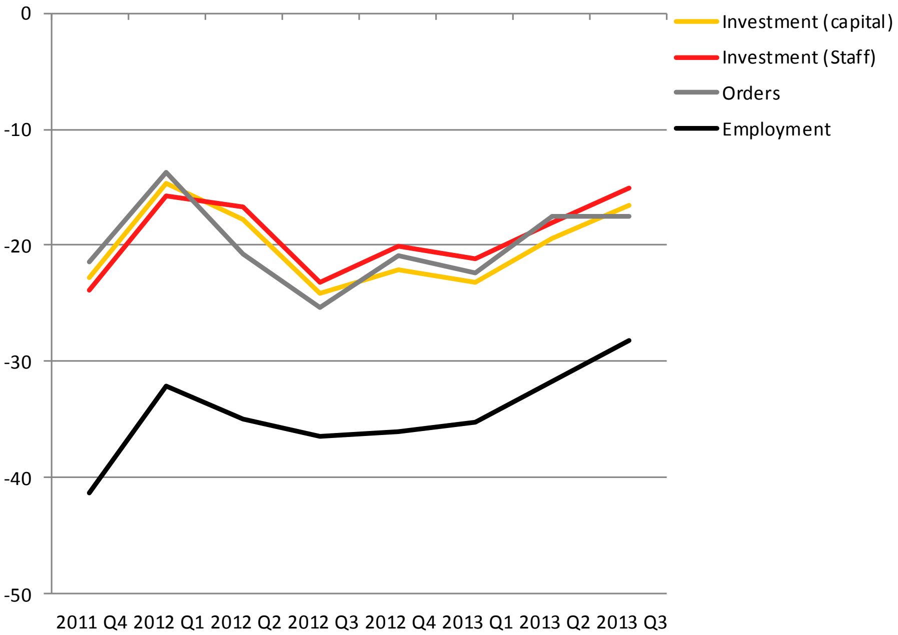
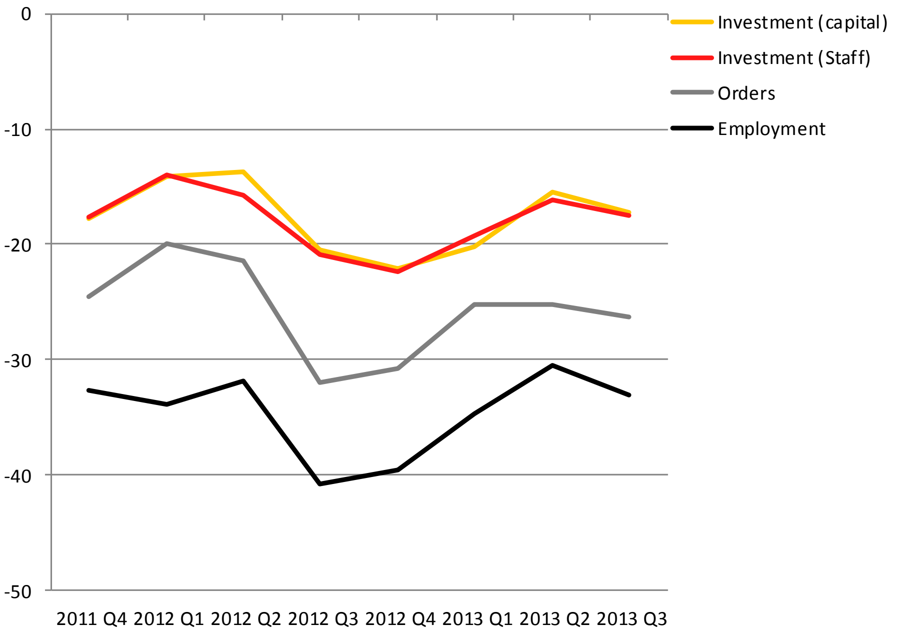


Figure 5: GECS Business Dynamism Indices in non-OECD countries



2. *Quarterly Review Q3 2013*, BIS, 2013, <http://www.bis.org/publ/qtrpdf/r_qt1309.pdf>.

Emerging markets are getting a taste of the taper

Figure 6: Business opportunities reported by finance professionals, by type

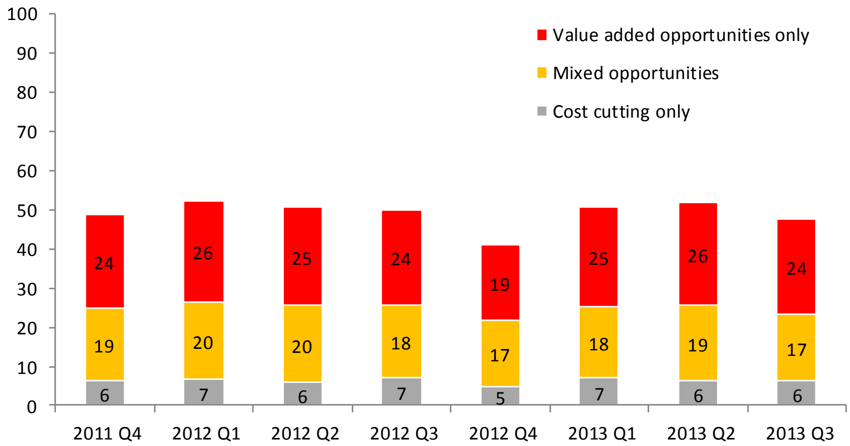
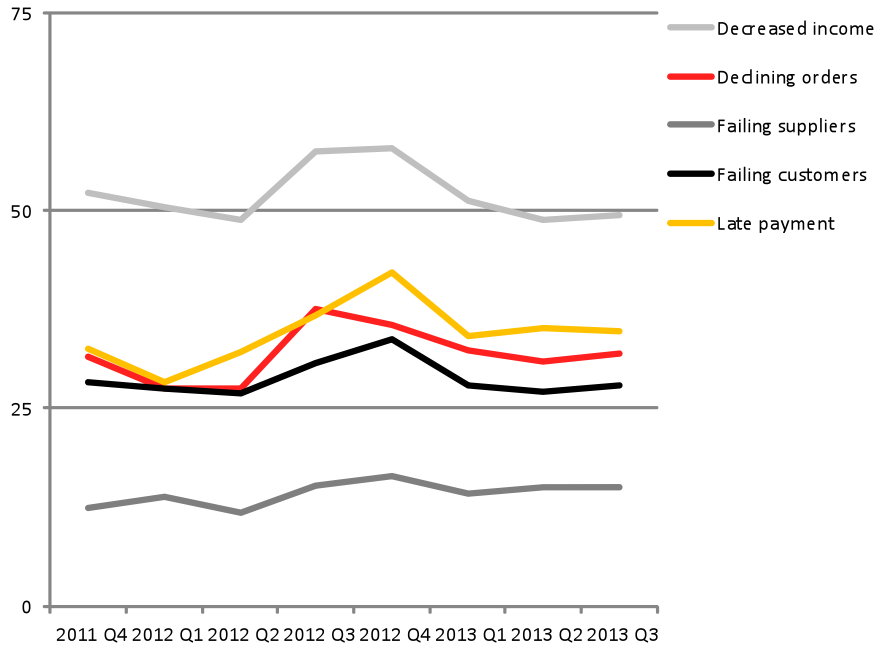


Figure 7: Cashflow and demand challenges in the non-OECD countries



If this stimulus was meant to support capital spending by businesses, there is little doubt of its effectiveness over the last year (see Figures 4 and 5). But it is also clear that, while some major Western economies continued to benefit from stronger investment and employment than at any time in at least eighteen months, emerging markets saw many of the last year's gains compromised in the third quarter of 2013. In those countries, investment, employment and orders all fell over the last three months, even though they were still up significantly year on year.

A final cause for concern is the decline in business opportunities in the third quarter of 2013, which suggests that new orders and investment could continue to weaken (Figure 6). The proportion of finance professionals who saw value-added opportunities of any kind for their organisations fell across almost all of the major regions in the third quarter of 2013; from 43% to 41% in OECD countries, and from 49% to 42% in emerging markets. Professionals in the OECD countries mainly saw a reduction in purely value-added opportunities (ie not including cost cutting), while those in emerging markets mostly saw fewer opportunities to improve efficiency.

Europe turns a corner as emerging markets falter

The Q2 2013 GECS report warned that this is was unlikely to be a recovery for everyone. This remains the case although the tables have turned for some of the leaders of the recovery. As Europe appears to have finally emerged from recession and a severe credit crunch, the exodus from emerging market bonds and assets is threatening to plunge much of emerging Asia, Africa and the Middle East into a credit crunch of their own.

The strongest performers in the third quarter of 2013 have been markets in Europe (both eastern and western) as well as the Caribbean: here business confidence has rebounded following a prolonged credit crunch, and businesses have taken advantage of the renewed access to finance in order to invest in capital and staff. In Europe, these developments have gone hand in hand with improved perceptions of the broader economic recovery, although this has not been the case in the Caribbean.

The Asia Pacific region lies at the other extreme of business fortunes. Here, business confidence is down, access to growth finance has tightened dramatically and business investment is beginning to fall, as a result of an investor exodus and deepening liquidity crisis that is testing the endurance of China's banking sector and the businesses that depend on it. Despite a rising tide of economic sentiment around the globe, respondents in this region felt that economic recovery was further out of reach in the third quarter of 2013.

Figure 8: GECS Recovery Perceptions Index for the major regions

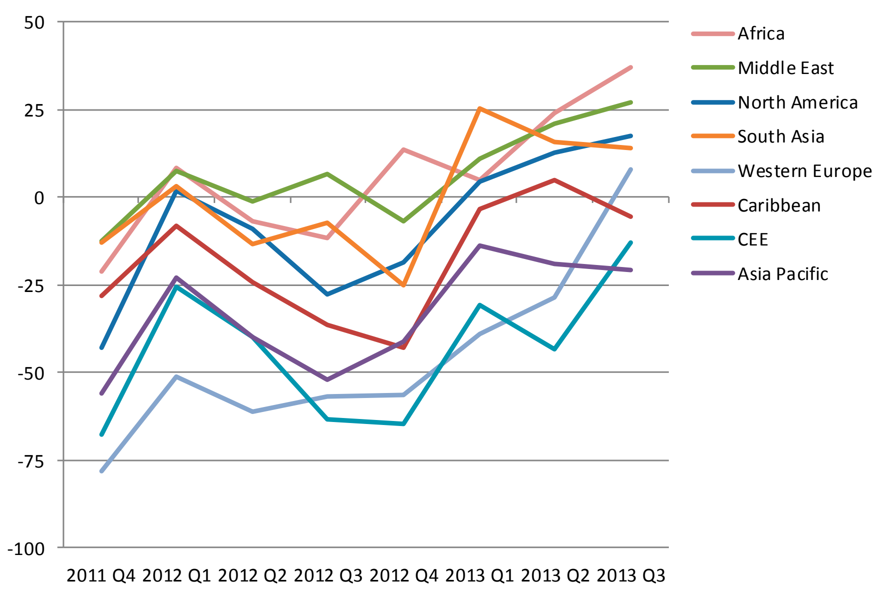


Figure 9: GECS Growth Capital Access Index for the major regions

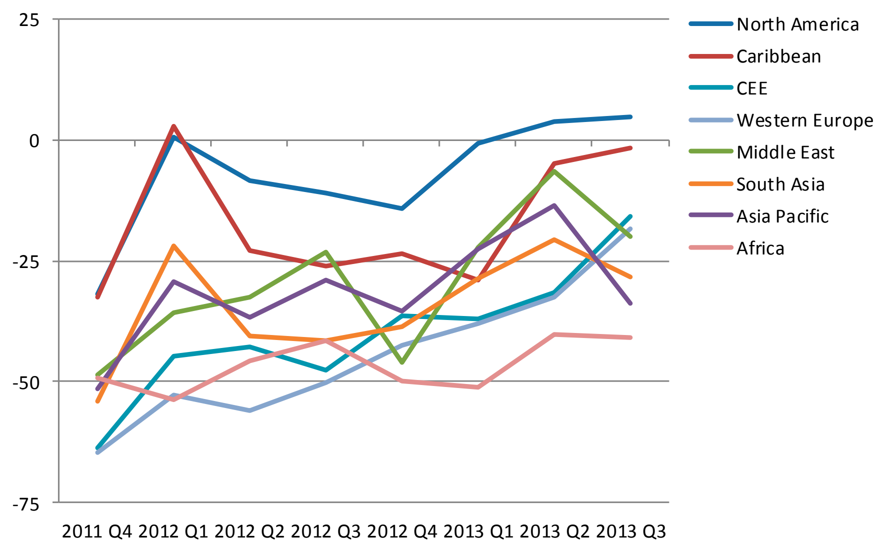
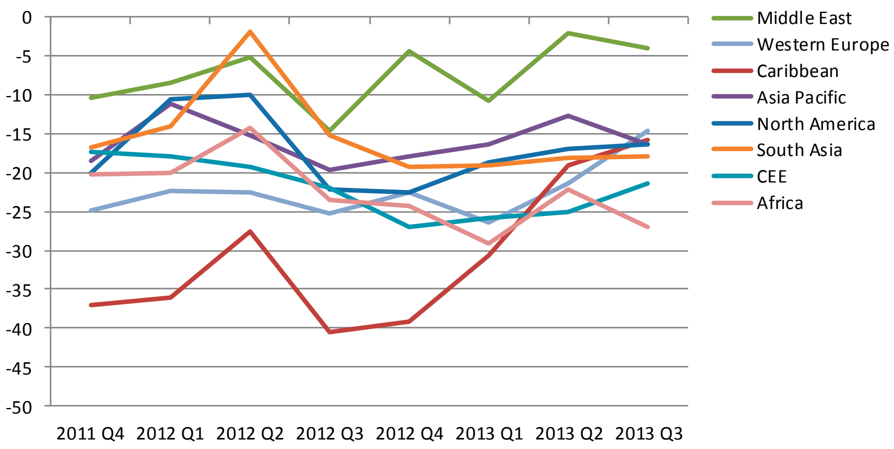


Figure 10: GECS Capital Spending Index for the major regions



A similar shift was evident in South Asia, where respondents were less optimistic about their national economies, but were more or less holding on to past levels of business confidence. Despite a tightening supply of finance, government spending was still propping up capital spending in much of the region, although this dynamic was looking increasingly unsustainable.

Worryingly, and despite increasing optimism about the state of national economies, both business confidence and capital spending were down throughout Africa, reflecting the way in which investment turned away from emerging markets in the third quarter of 2013. Africa remains the most optimistic of the major regions, but lags behind much slower-growing regions for business confidence and access to finance. The latter is a particularly worrying development – some of the world's most promising economies are unlikely now to get the investment they need to realise their promise for years to come.

Spending is back on the menu

The Q2 2013 GECS report noted with some concern that a number of erstwhile 'big spenders', countries with high and growing levels of government spending, were beginning to rein in public spending in response to strengthening domestic economies or poor public finances. This pattern has changed somewhat in the third quarter: for instance, respondents in the US now expect further increases in public spending in the medium-term and Canada is now once again part of the 'spenders' group, while countries such as Ireland and the UK are slowly exiting their fiscal adjustment programmes (see Figure 11). Russia and China remain likely to rein in public spending in the medium term (see Figure 12), but even here changes are now expected to be more modest. It is also worth noting that expectations of government spending in the US are likely to rise further following the resolution of the US shutdown.

Figure 11: GECS Government spending indices in selected markets

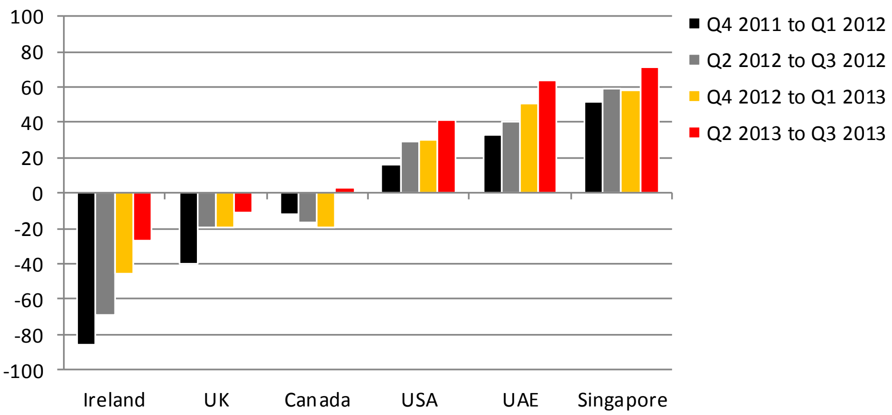
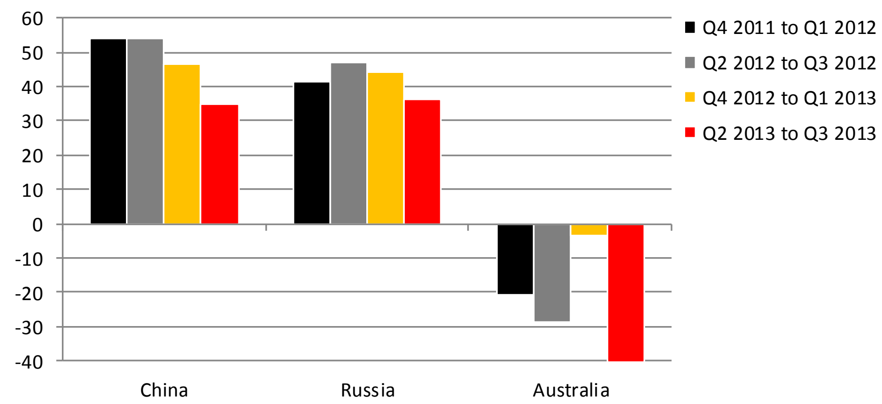


Figure 12: GECS Government spending indices in selected markets



Fundamentals: an overview of selected markets

US BUSINESS CONFIDENCE UP ONLY MARGINALLY, REGIONS' PERFORMANCE REALIGNED AS FAITH IN THE RECOVERY GROWS

After six months of strong net confidence gains, US respondents appeared only marginally more confident in the prospects of their organisations in Q3. One quarter (25%) of respondents reported confidence gains and 31% reported losses – both figures practically unchanged since the last quarter. After a year of diverging performance, business confidence in the regions converged once again, with continued gains in the South and North-East and losses in the Midwest and particularly the Mid-Atlantic.

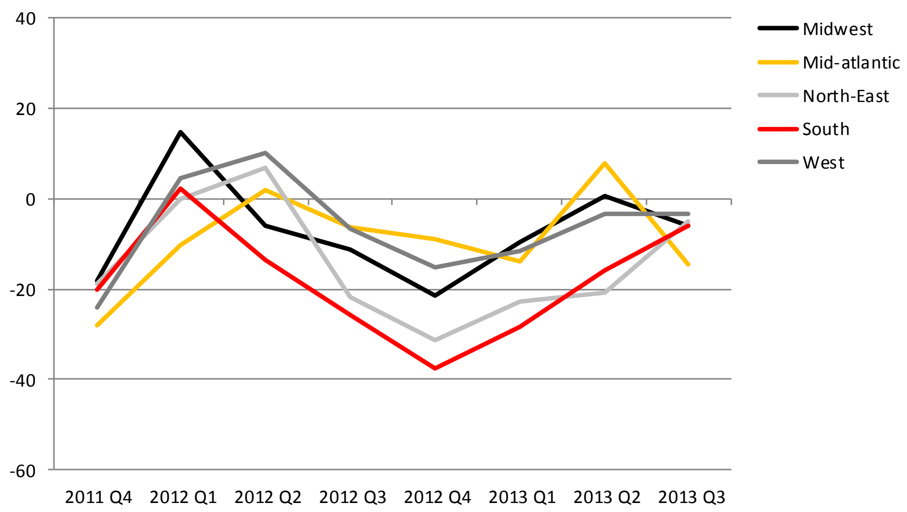
From a macro perspective, the third quarter of 2013 marked a full year of consistently improving perceptions of the economy - 57% of US respondents felt that economic conditions where improving or about to do so, up from 55% in Q2.

Stabilising business confidence should come as no surprise as US respondents reported only marginally more business opportunities in the third quarter. Perceptions of the recovery, on the other hand, were no doubt boosted by a strong improvement in business cashflow and strengthening demand, falling inflation and a substantial improvement in the supply of growth capital – which however appears to have failed to translate into investment in staff or capital.

Respondents expected roughly similar levels of medium-term government spending as in Q2 2013, but their appetite for deficits, traditionally very low, has grown over the last three months – in fact, US respondents have become consistently more dovish over the last three quarters.

Although economic sentiment in the US has been in positive territory since the beginning of 2013, it suffered significantly during the presidential election period, as well as the debt ceiling and fiscal cliff crises. There is reason to believe that the recent Government shutdown (which occurred after fieldwork had ended) will, at least temporarily, have had the same effect. Pre-shutdown, GECS recorded the highest levels of approval for government policies in the US since Q4 2011 – the downside being that this only corresponds to 13% of US respondents approving.

Figure 13: GECS Confidence Index by US region



DESPITE INCREASED DYNAMISM, CANADIAN BUSINESS CONFIDENCE IS HELD BACK BY UNCERTAINTY ABOUT GOVERNMENT POLICY

A steep fall in Canadian business confidence in Q2 was not reversed in the third quarter, although there is now evidence of increased dynamism among businesses. Nearly a quarter (23%) reported confidence gains in Q3, up from 13% previously, but another 44% reported losses, also up from 35% in Q2.

Overall, finance professionals were more optimistic about the state of the economy, with 51% (up from 35%) believing that things were improving or about to do so, while the pessimists made up 47% of the Canadian sample, down from 65% in Q2.

This rise in optimism is despite increasing mistrust of government policies, which a full third of respondents (33%) now considered 'poor' or 'very poor', up from 13% previously. Fiscal policy is part of this change in attitudes, as respondents felt that government spending was now set to increase substantially in the medium-term and about 14% expected dangerous levels of overspending.

Despite this, respondents in Canada reported significantly increased business opportunities in Q3, and the steady deterioration in demand and business cashflow reported in previous quarters has eased. Combined with falling inflation and improving access to growth capital, these developments led to a modest increase in business investment.

SOUTH ASIA

Lack of finance and rising costs are forcing India's businesses to pass up opportunities

Respondents in India were among the very few national panels to report a loss of faith in the recovery in the third quarter of 2013: a surge in optimism at the beginning of the year has now passed, and perceptions are roughly unchanged year on year, with 46% of respondents in the six months to September expecting improvement and 51% expecting deterioration or stagnation.

Business confidence, on the other hand, is clearly down year on year, with 49% reporting a loss of confidence in the last six quarters, up from 24% over the six months to March.

This lack of confidence and optimism reveals increased levels of frustration among respondents, who have pointed to a substantial increase in business opportunities over the last six months, but are unable to exploit them. In fact, business investment in both capital and staff has been falling steadily since its peak in Q3 2012.

This is due partly to a domestic downturn and partly to a loss of foreign investment, which the Indian government has sought to address in the third quarter. Pressures on cashflow and demand rose in the third quarter of 2013 after easing earlier in the year, while the supply of growth capital tightened significantly in the six months to September. Meanwhile, foreign exchange rates have been growing increasingly volatile over the last two years, leading to increased input inflation for India's businesses.

Against this backdrop, respondents from India have become increasingly critical of government economic policies over the last six months, calling for greater fiscal stimulus since the beginning of 2013. These attitudes have intensified over the last quarter.

Soaring business confidence in Pakistan may not be justified by fundamentals

In Pakistan, business confidence has been on the rise for over a year, and this improvement accelerated in the third quarter of 2013. Nearly a third (32%) of respondents reported confidence gains, up from 28% previously, while 36% reported losses, down from 46% in Q2.

Finance professionals have reported growing faith in the recovery over the last nine months, and this trend has been strengthened in the latest quarter. More than half (59%) of the respondents in Pakistan believe the economy is improving or about to do so, up from 57% in Q3, while only 39% believe it is deteriorating or stagnating, down from 41%.

These perceptions may owe more to optimism about the future than any concrete improvement in the recent past. Access to growth capital has been improving over the last year and a half, but tightened somewhat in the third quarter of 2013. Pressures on cashflow and demand remain subdued by the standards of recent years, and business opportunities edged upwards in Q3, even though they are still only marginally higher year on year. Investment is actually down year on year and has neither increased or decreased since the previous quarters. Finally, respondents reported rising inflation and foreign exchange volatility, almost matching the highs of early 2013.

Government is clearly being credited with some of the improvement in business conditions, although respondents in Pakistan are still among the most critical of government among the major ACCA and IMA markets. This points to public spending as one possible explanation for the rising confidence levels. Only 76% of respondents rated Government economic policies as 'poor' or 'very poor', down from 91% in Q2 2013. In terms of fiscal policies, both government and respondents in Pakistan appear to be becoming more dovish, as both expected and preferred medium-term spending levels have been rising over the last two years.

ASIA-PACIFIC

China's credit crunch bites in Q3, but nightmare scenarios have yet to play out

In early 2013, GECS figures indicated that China had avoided the 'hard landing' analysts had predicted for the past two years. Still, the slowdown in China is far from over, as credit rationing and fears about private and public sector debt have continued to damage the Chinese recovery.

While businesses in Hong Kong still appear to have reasonable access to growth capital (down only marginally year on year), in mainland China respondents reported the tightest supply in at least two years, suggesting that the country's official and shadow banking sectors are taking significant damage. In response, business investment in capital and staff has fallen sharply throughout China.

The credit crunch has also put pressure on demand and cashflow, which started to falter in the second quarter of 2013, first in Hong Kong and now in the mainland. Respondents are reporting significantly fewer business opportunities in the mainland (both quarter on quarter and year on year), while Hong Kong has seen a marginal recovery in the third quarter.

These developments coincide with a longer-term trend towards tighter controls over government spending in China. Respondents in the mainland, in particular, now expect spending to grind to a halt in the medium-term, after revising their expectations downwards throughout the last year. Meanwhile, their colleagues in Hong Kong expect the administrative region to have some more room to manoeuvre when it comes to public investment.

As a result of these pressures, business confidence has been falling throughout China over the last six months, with concerns accelerating in the third quarter of 2013. Only 20% of respondents in the mainland and 5% of those in Hong Kong (down from 32% and 18% respectively) reported confidence gains in Q3. Respondents in the mainland have been consistently more confident than their colleagues in Hong Kong, but confidence could soon converge as the credit crunch deepens.

Yet faith in the global recovery and the authorities' ability to respond to challenges is keeping Chinese finance professionals optimistic. Following a sudden deterioration in the second quarter of 2013, perceptions of the recovery are clearly on the rise again in mainland China, while respondents in Hong Kong have recorded a full year of improving perceptions. Overall, 40% felt that the economy was improving or about to do so, up from 36% in the second quarter, and 52% felt that conditions were deteriorating or stagnating, down from 60% previously. This optimism, however, could prove short-lived if China's credit crunch persists beyond the fourth quarter.

Recovery has gone into reverse in Malaysia as election spell is broken

Confidence has fallen back to pre-election levels, and perceptions of the state of the economy have deteriorated: 65% of respondents now believe that conditions are deteriorating or stagnating, up from 55% in the second quarter of 2013. Only 13% reported confidence gains, down from 28% in the previous quarter.

It isn't hard to see why confidence is falling again. After stabilising throughout the first half of 2013, pressures on demand and cashflow have risen once again. A surge in perceived post-election business opportunities has now died down, and with it the temporary increase in capital available for investment. Both economic measures are now down year on year. Business investment in capital and staff has fallen for a second quarter. Meanwhile, inflation and foreign exchange volatility have increased for the third quarter in a row, putting importers under a lot of pressure.

Approval of economic policies is at its lowest for quite some time, with 63% disapproving, up from 51% in Q2 2013. On the other hand, fears of public spending spiralling out of control appear to have died down. Post-election, spending expectations have fallen substantially, and, at 20%, the share of respondents expecting dangerous levels of overspending is at its lowest in eighteen months.

Singapore's finance professionals still believe in the recovery, despite good evidence of the contrary.

Business confidence fell in Singapore during the third quarter of 2013, with only 18% of respondents reporting confidence gains – down from 26% previously.

This loss of confidence is mostly down to reduced prospects for Singapore's businesses. Finance professionals reported fewer business opportunities in Q3 – these have fallen substantially over the last nine months, and are now down year on year. Inflation is close to its Q1 highs once again, while pressures on demand and cashflow are up again, following a year of improvement. Late payment, usually rarer in Singapore than elsewhere in the world, has surged. Meanwhile, growth capital has also become less accessible, after supply peaked in early 2013. It is now down marginally year on year.

Nevertheless, perceptions of the broader economy were stable – 34% of the finance professionals surveyed believe it is improving or about to do so, while 55% believe it is deteriorating or stagnating. These figures have not changed significantly since the second quarter of 2013.

Despite this challenging environment, business capacity building has continued to recover for a third quarter in a row, having bottomed out in late 2012. This trend, however, may be driven by new restrictions placed on foreign labour and the need for new hires. If that is the case, the boost to overall business capacity may be small and short lived.

Australia hit by a new credit crunch in run-up to elections

After peaking at the turn of the year, business confidence in Australia has fallen substantially, and perceptions of the recovery in general have deteriorated, including in the third quarter of 2013.

This particularly gloomy outlook is due partly to financing conditions and partly to underperforming economies elsewhere in the Pacific. Respondents are not reporting fewer business opportunities, but they are reporting a substantial credit crunch, putting both demand and business cashflow under severe pressure. Falling input price inflation, while helpful for some businesses, is actually a symptom of this lack of credit. So is a mild increase in employment, as businesses are finding it easier to increase their headcount than invest in capital.

Meanwhile, in the nine months leading up to the 2013 elections, respondents in Australia have been reporting increasingly negative views of their government's economic policies. Generally, such disapproval tends to give way to a 'honeymoon' effect as the new government settles into office, and it remains to be seen whether that can significantly improve conditions. For now, respondents expect medium-term government spending plans to be revised downwards, which is likely to pile more pressure on a slow recovery.

CENTRAL AND EASTERN EUROPE

Despite improving fundamentals, missing foreign investment is still limiting business dynamism in Poland

Polish business confidence rose marginally in the second and third quarters of 2013, with 26% of respondents reporting confidence gains, up from 20% in the six months to March 2013. These confidence gains, which appeared to stabilise in Q3, reflect both improving fundamentals and a tougher investment environment.

After peaking in late 2012, pressures on cashflow and demand have progressively eased, and continued to do so in the third quarter of 2013. Access to growth capital has also been improving steadily for almost two years, yet business opportunities are flat and unresponsive to improving fundamentals. Worse, capacity building has stalled over the last 12 months. This loss of dynamism appears to be the result of a sharp interruption in the flow of foreign capital into Poland halfway through 2012 that businesses have yet to recover from.

But with most of Europe on the mend, finance professionals in Poland joined their colleagues throughout the continent in expecting recovery – over the last 6 months, 50% believed that the state of the economy was improving or about to do so, up from 20% in the six months to March. As a result, perceptions of government policy have begun to recover, although concerns remain about the level of government spending, which about 19% of respondents over the last six months felt was going to be dangerously high in the medium term.

Russian business stirs from a long winter, greeted by volatile markets

Over the last two quarters, inflation and exchange rate volatility have emerged as significant problems for GECS respondents from Russia, and may well become more so following the Bank of Russia's decision to widen the range within which it will allow the Ruble to trade against the Euro and US dollar.

Despite these pressures, finance professionals reported significantly increased business opportunities for the first time after a very difficult 2012 and a subdued first half of 2013. Pressures on cashflow and demand likewise fell in Q3, and access to growth capital improved, leading to a small but significant increase in investment.

Business confidence also improved as a result, breaking a nine-month streak of negative results. Respondents are now more optimistic about the state of the macro-economy than they were three months ago, and perceptions have also improved year on year.

Expected levels of medium-term government spending have continued to fall, but this trend appears to be coming to an end; on balance, respondents in Russia now believe that spending over the next five years will be at roughly the right levels, and have reported higher levels of approval for government policies than they did three months ago.

MIDDLE EAST

Confidence stalls in the Emirates as financial flows reverse and government spending is reined in

The Emirates have traditionally been one of the most confident of the ACCA and IMA markets, but finance professionals are reporting a distinct loss of confidence both in their own businesses and in the economy as a whole in the third quarter of 2013.

Over two thirds (67%) of respondents still believe conditions are improving or about to do so, down from 68% in Q2, but another third (33%) now believe the economy is deteriorating or stagnating, up from 30% previously. Only 30% of respondents from the Emirates reported confidence gains, down from 40% in the previous quarter.

It is not hard to understand why. After a year of consistent increases in the supply of growth capital, the third quarter of 2013 saw financing conditions tighten for businesses in the Emirates, cutting short what was shaping up to be a slightly delayed increase in business investment.

Moreover, although pressures on demand and cashflow continued to ease, and are now clearly stabilising, inflation and foreign exchange volatility continued to increase, in what appears to be a longer-term upward trend.

Uncharacteristically for the UAE, some of the blame for this is directed towards government policy, with only 30% of respondents now approving of their governments' economic policies, down from 52% previously. Fiscal policies are perhaps more popular: the number of respondents who fear dangerous levels of over- or under- spending is at an historical low. Even so, Q3 2013 marked a turning point in expectations, as the Emirates are now expected to join a long list of erstwhile Big Spenders that are slowly tightening their medium-term fiscal policies.

WESTERN EUROPE

Buoyant Britain leads the European recovery due to a surge of funding; but businesses could struggle to find suitable investment opportunities

Once consistently pessimistic, UK respondents were willing to call the recovery in the third quarter of 2013 - 62% believe the economy is improving or about to do so, up from 42% in Q2 2013. With regards to their own organisations, more than two in five (42%) respondents reported confidence gains in Q3 2013, up from 26% previously, while only 20% reported losses, down from 30% in the previous quarter.

These figures suggest that the UK economy has substantially outperformed most major ACCA and IMA markets in the third quarter of 2013. The reason behind this is a dramatic improvement in access to growth capital over the last six months, which has prompted an equally impressive increase in investment and employment. Meanwhile, pressures on cashflow and demand are falling, adding to the sense that conditions on the ground are easing. Importantly, however, business opportunities did not increase in the third quarter of 2013, which suggests there is a limit to how much investment can be sustainably funded through the UK's new-found liquidity.

Government has been given some of the credit for these developments – 25% of UK respondents approved of the Government's economic policies in Q3 2013, up from barely 11% on year ago. As with other European countries, austerity in the UK is increasingly seen as having run its course: respondents are expecting less fiscal retrenchment over the next five years than they expected previously. Only about 10% of respondents felt that the government was likely to cut too much over the next five years.

Investment up but confidence stable as Scotland pursues a more balanced recovery

In terms of business confidence, Scotland entered positive territory half a year ahead of the rest of the UK and has seen more balanced confidence gains since. In fact, business confidence was largely unchanged between Q2 and Q3 (26% reporting gains and 21% reporting losses, against 24% and 17% respectively in Q2). While this does mean that business confidence is now lagging behind the rest of the UK, it is likely to be much more sustainable in the long run.

A key reason behind this divergence in business confidence is the fact that respondents in Scotland are more reserved in their expectations of economic recovery than their colleagues elsewhere in the UK – 50% (up from 38%) believe the economy is improving or about to do so, compared to 63% across the four nations. This still represents a significant improvement in perception and the first move into positive territory since the survey began.

Respondents in Scotland have reported a marginal fall in the availability of business opportunities, following a surge in early 2013. Pressures on cashflow and demand have increased, although they are still at reasonably low levels by global standards and still down year on year. But following a full year of improvements in the supply of growth capital, business investment in both capital and staff has surged in 2013, rising modestly in the third quarter as well. As a result, input prices have risen for a second quarter, after bottoming out in early 2013.

Government is getting some of the credit for improved conditions on the ground, although respondents in Scotland have been consistently more critical of economic policy. At 18.4% (up from 10%), approval ratings for economic policy are higher than they've been in a year and a half, despite respondents increasingly expecting fiscal policy to tighten again in the medium-term.

Hopes of bailout exit boosting Irish business confidence despite poor fundamentals

GECS respondents in Ireland are treating the country's recovery with caution as fundamentals are recovering slowly and unevenly. They reported fewer business opportunities for a second quarter in a row in Q3, while pressures on cashflow and demand increased significantly, driven to some extent by the rising cost of foreign inputs.

Despite these developments, business investment in capital and, to a lesser extent, staff, grew substantially in the third quarter. This is partly due to continued access to growth capital, as the tightening in Q2 has since proven to be transitory. But it is also due to businesses releasing reserves for investment as Ireland looked set to exit not only its latest recession but also the fiscal adjustment programme agreed with the IMF, EU and ECB – the first country to do so since the Eurozone crisis began.

In response, expectations of government spending have risen significantly, with only 8% of respondents now believing that the Irish government is likely to keep spending at dangerously low levels in the medium term – down from 20% a year ago.

As a result, business confidence recovered from an unexpected fall in the second quarter of 2013, with 28% of respondents (up from 24%) reporting confidence gains in the three months to September. Similarly, perceptions of the recovery recovered to the levels seen in the first quarter of the year, with 47% of respondents believing that conditions were improving or about to do so (up from 30%). Both indices are up substantially year on year, indicating a healthier recovery.

Caribbean credit crunch may be over as region sees the return of domestic demand, financial stability and investment

Business confidence and economic sentiment in the Caribbean reached a low point in late 2012 as the region was weighed down by a substantial credit crunch, weakness in demand and uncertainty about Jamaica's public finances in particular. But finance professionals in the region grew much more optimistic in the New Year and were in broadly similar territory in the third quarter of 2013.

Business confidence was up in net terms in the third quarter, mostly due to a larger share of respondents reporting that confidence was unchanged. About one in five (19%) reported confidence gains, down from 24% in the second quarter of 2013, while one third (33%) reported a loss of confidence, down from 45% previously.

Meanwhile, respondents were slightly more cautious than previously about the state of their national economies. 45% of respondents in the Caribbean believed economic conditions were improving or about to do so in Q3, down from 50% in the previous quarter. Despite this, faith in the region's governments has registered the first year on year gains in a while, after reaching a low point in the first quarter of 2013.

The resolution of the region's financial troubles finally filtered through to improved domestic demand and business cashflow in the third quarter of 2013, marking the beginning of a more solid recovery in the region. Input prices continued to fall and respondents reported less volatile exchange rates, marking a significant improvement since a year ago. Not surprisingly, business opportunities are up substantially year on year and well ahead of the global average, despite a small seasonal fall in the third quarter.

The combination of more opportunities and better access to finance has boosted business investment in capital and staff, both of which bottomed out at the end of 2012. Employment grew more strongly that capital spending in the third quarter, but the recovery in capital spending has been much stronger and more consistent over the last nine months, suggesting that the region is slowly gearing up to produce more and better jobs.

Investment grinds to a halt in Africa as accountants see fewer opportunities ahead

A long-term trend of increasing business capacity building in Africa appears to have come to a halt in the third quarter of 2013. Capital spending fell in Q3, although the trend appears to have started improving since the beginning of the year. Investment in staff development, on the other hand, has been on a downward slope for the last year and a half, and the fall accelerated in Q3, with businesses also cutting down significantly on headcount.

In putting off investment and losing capacity, businesses are responding to signs of further trouble ahead: business opportunities plummeted throughout Africa in the third quarter of 2013, falling far from their peak at the end of 2012 as the slowdown in Asia continued to bite into economic activity in Africa. Access to growth capital tightened marginally and pressures on cashflow and demand also increased, though they remain lower than a year ago. Against this backdrop, a fall in input price inflation and more stable foreign exchange rates have been unable to decisively boost business prospects.

As a result of these challenging conditions on the ground, African business confidence dipped slightly in the third quarter, but remains on a slow upward trend over the last 9 months. Only 36% of respondents reported confidence gains in Q3, down from 41% in the second quarter.

Despite concerns for their own businesses, respondents' faith in the prospects of their national economies is up very substantially year on year, and grew further in the third quarter of 2013. In Q3, two thirds of respondents in Africa (66%) felt that the state of their national economies was improving or about to do so, up from 60% in the previous quarter.

Views from the coalface

IMPRESSIONS AND COMMENTARY FROM SELECTED MARKETS

The pent up demand is there, but the Government spending is not. In the private sector, financing from banks seems to be freeing up a little but the market is very sensitive to interest rate movements and negative press.
Director, large construction company, US (northeast)

The payroll tax increase this year has had a significant impact on our top line growth. Our consumers' discretionary income in small to medium markets in the southeast, which make up the largest segment of our customer base, saw more of the impact which directly tied to our missing targets in the Spring.
Manager, large retailer, US (South)

Easier access to investment capital at lower interest rates as banks actually bid against each other for the opportunity to loan the money.
CFO, medium-sized wholesaler/retailer, US (midwest)

We rely on export business. Federal Reserve's QE3 policy possibly winding-down has caused our overseas customers [to be] affected significantly, probably due to Forex volatility.
CFO, small wholesaler, US (west)

We're an export-driven company, more susceptible to economic conditions in mainland EU, US and APAC. [We're seeing a] weak recovery in the EU and lower than expected results from APAC, while the US is showing some signs of recovery. A new internship scheme has provided us with an opportunity to inject new blood/skills into the business at a reasonable cost.
Director, large corporate, Ireland

New regulations for Hedge Funds have meant trustee departments now have more work and can command a bigger fee.
Senior fund accountants, large financial, Ireland

[The possibility] of the Fed tapering QE3 resulted in a sell-off of Asian shares by foreign funds managers. Customers have less budget in professional services after losing money in shares market.
Accountant, small practice, Malaysia

High housing costs have resulted in high operating costs everywhere. Investment in housing has reduced the capital in other operations; cash flow shortage is spreading.
Controller, large corporate, China (Shanghai)

Due to tighter restrictions on the hiring of foreigners, the operating expenses of the company have increased significantly, resulting in thinner operating margins. Our employee income has been affected and life has become tougher.
Senior Manager, larger corporate, Singapore

Weak non-oil exports over the past three months have impacted the manufacturing and electronics sectors. We have seen a decline in orders from customers in both sectors.
Controller, small business, Singapore

Approval of the Finance Act 2013–14 in Pakistan has made a substantial difference to the financial performance of the organisation, with increased taxation across almost all sectors.
Internal auditor, large corporate, Pakistan (Lahore)

Bad economic policies from the newly elected Government. Salary taxes were increased, which will result in a brain drain. Indirect taxes (VAT) were also increased, which has resulted in double-digit inflation.
CFO, small business, Pakistan (Islamabad)

Relatively higher exchange rates have resulted in decreased financial performance for our export driven organisation. On the other hand the low interest rates increases financial performance due to the relatively lower finance costs incurred.
Internal auditor, large corporate, Canada

Russia suffered from joining the WTO and has started creating non-tariff [trade] barriers to protect local production. These bring additional costs.
Consultant, large corporate, Russia

The collapse of the banking system prompted by the downgrading of the economy and haircut of deposits meant that the company had to move its funds abroad and this increased the cost for the company and the speed and ease by which transactions are done.
Newly qualified accountant, large corporate, Cyprus

Since my organization runs a refinery, the availability of capital expenditures have increased because of the crucial need to expand and modernize. There is increased infrastructure activity, but only because the refining margins are positive.
Supervisor, larger refinery, Bahrain

[An improving] airline network has helped the company I work for manage travel costs, which are a big part of our operating costs. Also the advancement in the country's IT infrastructure has boosted our company's confidence in investing more resources within the country for meeting client requirements.
Supervisory, large oil and gas company, United Arab Emirates

Low liquidity has caused serious challenges: no deposits, no borrowing, high foreign exchange rates, a drought in agriculture hence steadily low food production, to mention but a few.
Director, large financial, Uganda

China has just agreed on a US$5 billion basket of aid for infrastructure, a sum that is substantial for Kenya. Due to high government spending, credit from local markets is slowly being squeezed and the effects are telling on some businesses. We are hoping that with external development aid/borrowing and a new sovereign bond of US$1 billion together with the Chinese aid Kenya can achieve its MDGs [Millennium Development Goals] and Vision 2030.
Director, mid-tier accountancy firm, Kenya

Due to the global crisis, top management has been forced to cut down on the company's expenses. To compensate and keep the colleagues motivated, there has been a change in company values, objectives and ways of working. There is a lot more focus on building future leaders.
Supervisor, larger retailer, India

Conclusions

The third quarter of 2013 has been a time of marked contrasts in the performance of different regions. While many Western countries returned to growth and their damaged banking sectors began to heal, emerging markets were reeling from a mass exodus of investors from riskier assets. In both cases, the global economy's dependence on cheap credit and abundant liquidity has become painfully obvious, and now threatens to destabilise the global recovery.

China's continuing credit crunch is showing signs of infecting the wider Asia-Pacific region, but respondents on the ground appear confident that this does not yet present as much of a threat to the national and regional economies as western commentators have claimed. The way the Chinese authorities choose to resolve this issue will determine much of the region's prospects going forward.

In the US, the government shutdown promises to damage investment just as credit-starved businesses begin to make plans for the future once more; the precedent of previous political showdowns of this kind suggests that the impact of uncertainty can be severe.

Nevertheless, it is important not to downplay the best economic sentiment readings in four and a half years. Even if this quarter's good news are disproportionately weighted towards Europe, it is worth celebrating the fact that European businesses have managed to see a long period of austerity through with some of their appetite for investment intact. And while much of the positive sentiment regarding the global economy's fortunes may be artificial, it's clear that a consensus is emerging that the worst is truly behind us. When it comes to economic matters, a global consensus is a very powerful thing.

ACCA, IMA and the global economy

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 focus of media attention. While most national economies are now growing once again, it is far from clear how sustainable this growth is or how long it will be before a sense of normalcy returns to the global economy.

ACCA and IMA have been prominent voices on what the accounting profession can do to help turn the global economy around. Both bodies have published extensively on a range of topics from the regulation of financial markets or the prevention of fraud and money laundering, to fair value or the role of international accounting standards, to talent management and the development of an ethical business culture.

ACCA and IMA aim 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 their members in challenging times. Both professional bodies believe that accountants add considerable value to business, and never more so than in the current environment.

Accountants are particularly instrumental in supporting the small business sector. Small and medium-sized enterprises (SMEs) account for more than half of the world's private sector output and about two thirds of all employment. Both ACCA and IMA focus much of their research and advocacy efforts on articulating the benefits to SMEs of solid financial management and reliable financial information.

WHERE NEXT?

As countries around the world once again consider strategies to promote stability and stimulate growth, the interconnectedness of our economies, and how they are managed and regulated, is now firmly in the spotlight. The development of the global accountancy profession has benefited from, and in turn contributed greatly to, the development of this interconnected global economy. The fortunes of the two are tied. ACCA and IMA will, therefore, continue to consider the challenges ahead for the global economy, and focus on equipping professional accountants for the uncertain future.

To find out more visit

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