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Global economic conditions survey report: Q1, 2014

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

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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 428,000 students in 173 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.

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Introduction

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.

This is the 21st edition of the survey, and the 10th since ACCA and IMA first joined forces to conduct this research. Using the combined data since 2009, it is now possible to discuss year-on-year trends for five consecutive years.

Fieldwork for the Q1 2014 GECS took place between 27 February and 22 March 2014, which included the escalation of the events in Crimea as well as the early days of the search for flight MH370. The survey attracted 1,772 responses from ACCA and IMA members around the world; 700 of those were senior finance professionals, including 171 CFOs.

As always, ACCA and IMA are deeply grateful to all members who gave up their time to respond to the survey. Finance professionals have front-row seats to the recovery, and it is their first-hand accounts of business conditions on the ground that make the GECS a trusted barometer for the global economy.

Business confidence and sentiment on the rise despite mounting risks

The headline GECS Confidence and Recovery indices both rose in early 2014 (Figure 1), bringing business confidence just short of positive territory for the first time in five years. 30% of respondents were now more confident about the prospects of their organisations than they had been three months earlier, a figure unchanged since late 2013. On the other hand, 31% reported a loss of confidence, down from 34% in late 2013.

Perceptions of macroeconomic conditions improved faster than business confidence, as they have done throughout the past eighteen months. More than half of the global GECS sample (58%, up from 55% in late 2013) were optimistic about the state of their national economies, reporting that recovery was underway or about to begin. The pessimists only made up 38% of the sample, down from 42% in the previous quarter. These are the best business confidence readings since the GECS began in 2009, and the best economic sentiment readings since Q2 2010, while perceptions of government policy have also recovered to their best readings since late 2010 (see Figure A1).

Figure 1: Major GECS Indices, Q4 2011 to Q1 2014

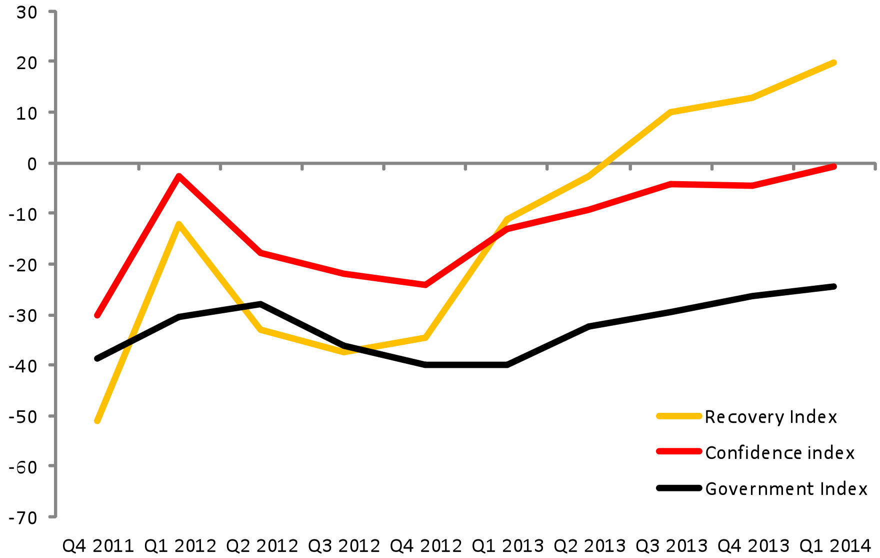
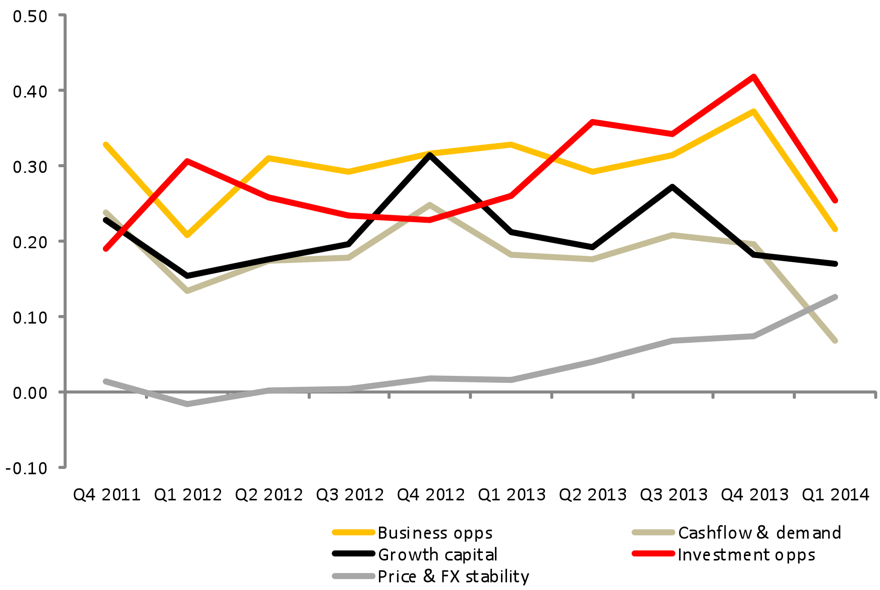


Figure 2: Standardised impact of fundamentals on global business confidence



These should, in theory, be encouraging findings, but ACCA and IMA's analysis of the influence of fundamentals on business confidence suggests that the economic recovery is flawed and has now become much more fragile (see Figure 2).

Since early 2013, global business confidence has become increasingly dependent on price and exchange rate stability. This trend is a sign of building financial turbulence, and has accelerated dramatically in early 2014. Financial stability is now a more significant contributor to business confidence than cashflow and demand (see Figure 2). Similarly, expectations of government spending and ratings of government policy became more significant contributors in early 2014. Finally, the contribution of other fundamentals to business confidence fell sharply, as did that of general economic sentiment. Combined, these developments suggest that the recovery has been hollowed-out in early 2014, and is now over-dependent on policy.

Business investment on the rise again, driven by innovation

Despite mounting downside risks to the recovery, there is no denying the increased dynamism of businesses around the world. As Figure 3 demonstrates, employment and capital spending are on the rise in both developed and emerging economies, while order indices in emerging markets have yet to stabilise.

Weak new orders could spell trouble ahead for emerging markets. As Figure 4 demonstrates, it is precisely the promise of new orders, alongside the innovative capacity of businesses, that has driven capital spending over the past three years – and both factors became significantly more influential in the six months to March 2014. At the global level, businesses' capital spending also appears have become more responsive to investment returns and government support.[1]

Figure 3: GECS Dynamism Indices for developed vs emerging markets

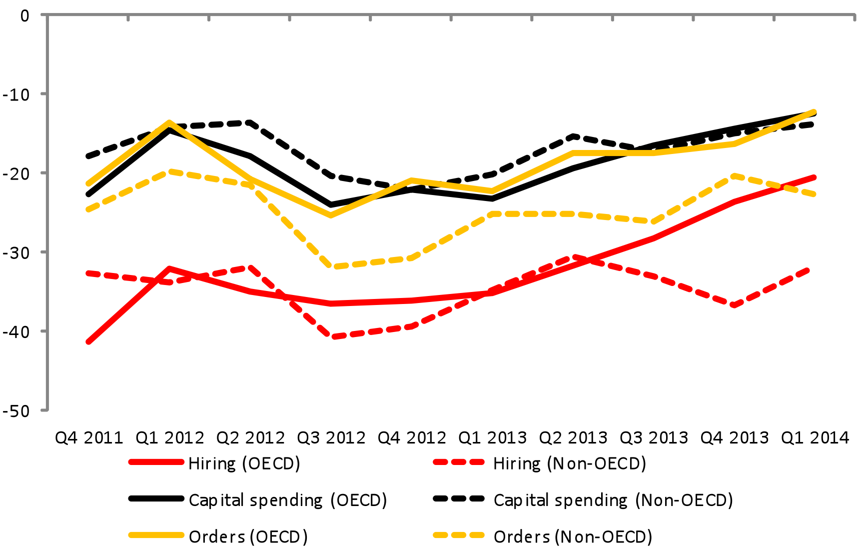
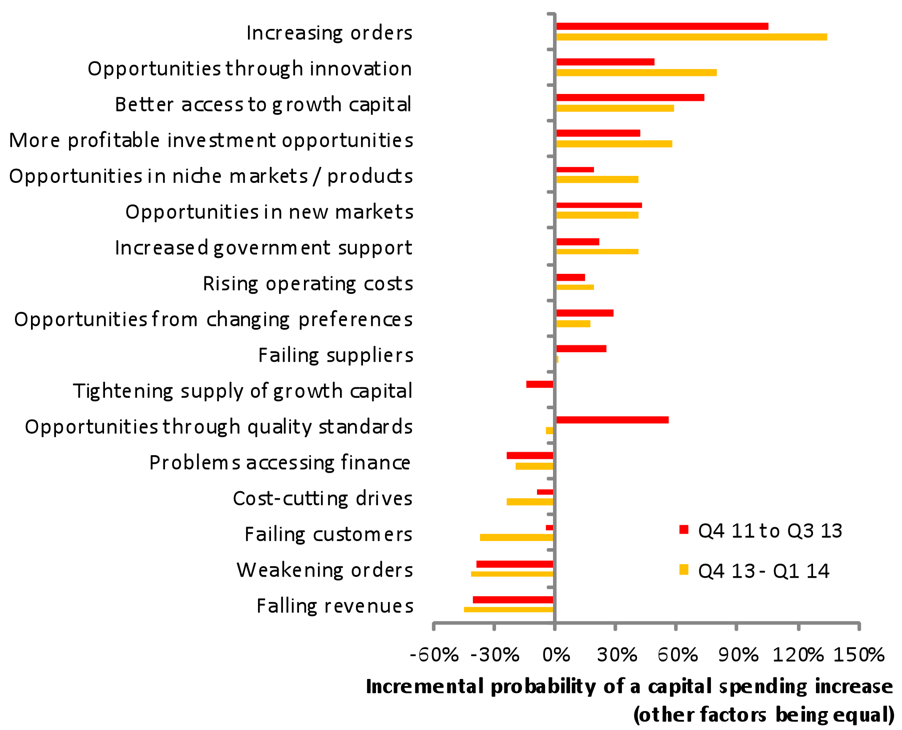


Figure 4: Push and pull factors influencing capital spending



1. This analysis is based on a binomial regression analysis which also controlled for region, size, sector, internationalisation, business confidence, perceptions of the economy and perceptions of government policy, including medium-term spending prospects.

Deeper into the Taper

Figure 5: Business confidence index in developed vs emerging economies

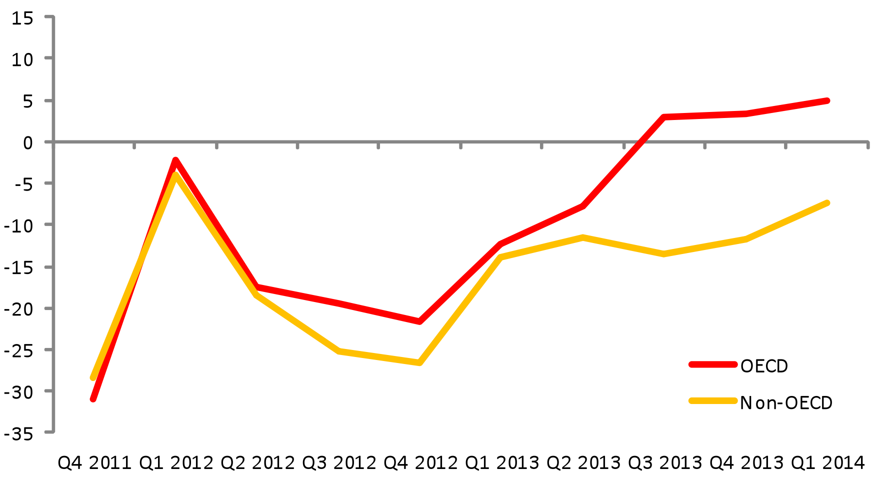
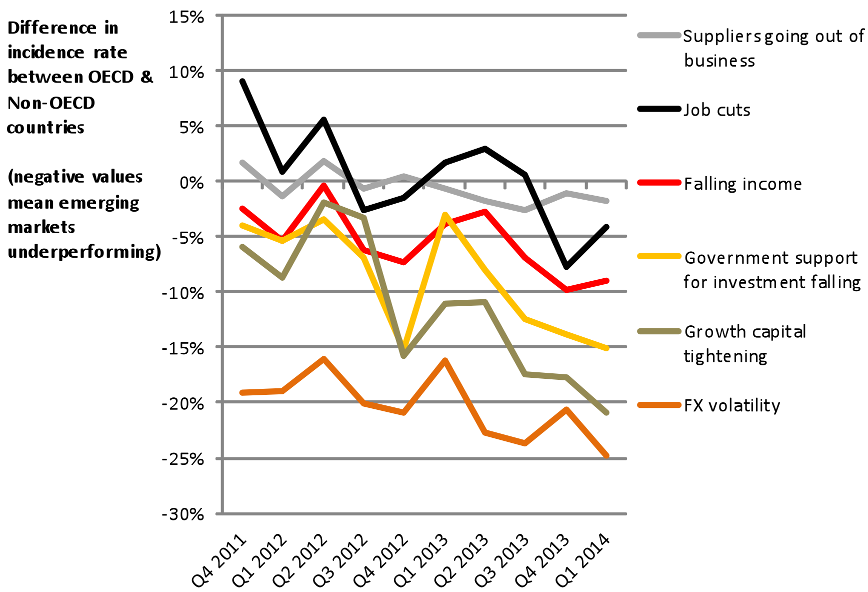


Figure 6: The changing fortunes of emerging markets



The announcement in May 2013 of the Federal Reserve's intention to phase out, or 'taper', its programme of asset purchases sent shockwaves through the world's financial markets. Its impact soon reached the real economy, especially in emerging markets which witnessed an investor exodus from what were seen as risky, high-yield assets. Three quarters into the post-Taper period, the change of fortunes throughout ACCA and IMA's emerging markets is becoming ever more evident. Business confidence readings in OECD and non-OECD have diverged significantly since the third quarter of 2013, and only converged marginally since then (see Figure 5).

Converging confidence, however, can be misleading. As Figure 6 demonstrates, the gap in performance between developed and emerging markets has grown steadily over the past year and a half. The impact of the Taper can be seen clearly, as the performance gap widened dramatically from Q3 2013 onwards, and while business revenues and hiring appear to have resisted the general trend in early 2014, overall the gap between developed and emerging economies has widened.

It is worth noting that during this entire period, and even post-Taper (or Post-Taper-Talk), business opportunities have not been less forthcoming in emerging markets than in developed ones; rather, it is business conditions on the ground, and particularly the lack of growth capital and financial instability, that have held the former down.

The recovery consensus unravels

The comparison between developed and emerging markets becomes even more nuanced when seen at the regional level. As Figure 7 demonstrates, perceptions of the recovery have diverged over the last six months, with respondents in Central and Eastern Europe, Asia-Pacific, Africa and the Caribbean slowly dropping out of the global Recovery Consensus. Both business confidence and capital spending either fell or rose only marginally in each of these regions – though Central and Eastern Europe stood out as the crisis in the Ukraine intensified. Events have had a clear impact on all neighbouring countries and, significantly, on Russia itself.

Even the regions still wedded to the recovery consensus are taking very different trajectories. In South Asia, India's upcoming election and infrastructure improvements in Pakistan strongly supported business confidence and strengthened respondents' faith in the recovery.

The confidence and recovery indices saw a correction in the Middle East in early 2014, following the exuberance of late 2013, when Dubai's EXPO 2020 win was announced. However, capital spending in the region continued surging ahead of the rest of the world and shows no signs of slowing.

Figure 7: GECS Recovery Indices by major region

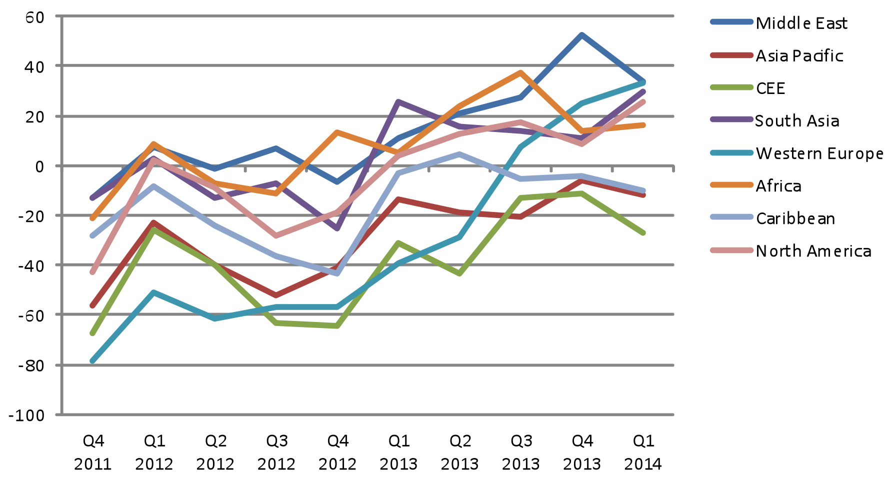
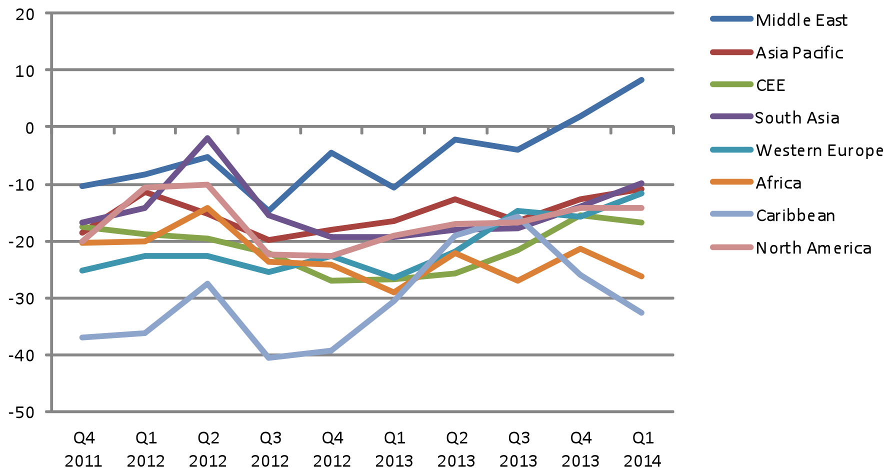


Figure 8: GECS Capital Spending Indices by major region



North America's economies saw confidence and faith in the recovery return across the board on the back of improved financing conditions and a recovering real estate sector, whereas in Africa and Western Europe, economic sentiment was up but business confidence remained more or less flat and capital spending fell.

Appropriately, given the uneven pace of the recovery, mid-market firms (which are dependent on regional economic integration and trade) have lagged behind the rest in terms of business confidence, while the biggest confidence gains were recorded among large, especially multinational, corporates and the public sector.

Table 1: Detailed Recovery Index for selected markets

	Getting Better	At bottom and will improve	At bottom and will remain	Getting worse	Don't know	Index	QoQ change	YoY change
OECD	45	19	22	10	3	31.6	▲	▲
Non-OECD	32	18	17	26	5	6.4	▲	▲
North America	48	13	22	14	4	25.6	▲	▲
Caribbean	27	16	20	33	4	-10.2	▼	▼
Middle East	44	17	9	19	8	33.1	▼	▲
Asia Pacific	27	12	22	29	9	-11.8	▼	▲
CEE	22	14	21	42	1	-26.9	▼	▲
South Asia	39	23	17	16	5	29.4	▲	▲
W. Europe	41	24	23	8	3	33.5	▲	▲
Africa	34	23	15	25	2	16.4	▲	▲
China (ex HK)	25	13	22	41	0	-25.0	▼	▼
Hong Kong	39	13	16	19	13	16.1	▲	▲
Ireland	36	33	23	5	3	41.0	▲	▲
Malaysia	14	12	20	42	11	-35.4	▼	▼
Pakistan	33	21	19	19	5	15.8	▼	▲
Singapore	37	3	17	23	20	0.0	▼	▼
UK	47	23	20	6	3	44.0	▲	▲
UAE	55	20	7	7	7	60.0	▼	▲
USA	47	12	22	14	3	23.0	▲	▲

Table 2: Detailed Confidence Index for selected markets

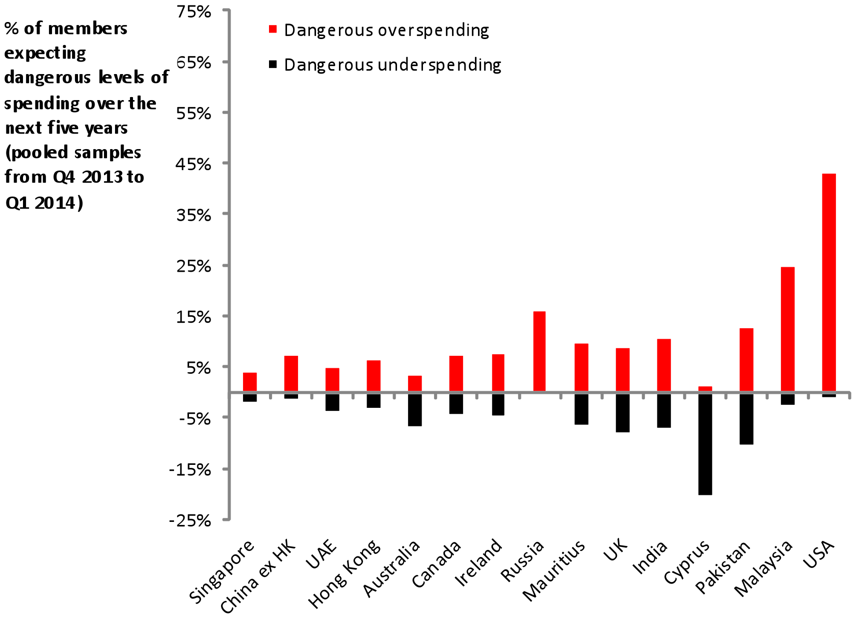
	Much more confident	More confident	No change	Less confident	Much less confident	Index	QoQ change	YoY change
OECD	5	26	43	20	6	4.9	p	p
Non-OECD	6	23	34	25	12	-7.4	p	p
North America	4	21	46	22	7	-3.5	p	p
Caribbean	4	10	47	20	18	-24.5	q	q
Middle East	13	28	32	19	8	14.5	q	p
Asia Pacific	3	16	38	33	10	-23.7	p	p
CEE	3	14	33	31	19	-33.3	q	q
South Asia	7	36	27	17	12	14.7	p	p
W. Europe	5	31	41	17	6	13.0	p	p
Africa	6	26	32	22	14	-3.1	p	p
China (ex HK)	9	16	22	53	0	-28.1	q	q
Hong Kong	3	6	55	26	10	-25.8	p	q
Ireland	5	31	41	21	3	12.8	q	p
Malaysia	0	12	38	32	17	-36.9	q	p
Pakistan	9	33	26	18	12	12.3	p	p
Singapore	3	26	37	29	6	-5.7	p	p
UK	7	33	38	16	6	18.3	p	p
UAE	15	44	25	13	4	41.8	p	p
USA	4	21	46	22	7	-4.3	p	p

The big spenders return

Previous editions of the GECS have noted that governments in major economies including Russia, China and (occasionally) the US were showing signs of reducing public spending. The first quarter of 2014 marks a significant departure from this trend, with spending expectations growing substantially in all three of the above, as well as India.

As Figure 9 demonstrates, however, not all governments have room to manoeuvre: respondents in Malaysia and the US voiced strong concerns about government fiscal policies.[2] At the other end of the spectrum were respondents in China, Singapore and the Emirates, as well as major Western economies such as Canada and Australia, where respondents were more relaxed about government finances.

Figure 9: Expectations of government fiscal responsibility in Q4 2013-Q1 2014, by market



2. 'Dangerous' levels of over- and under-spending, as approximated by GECS, have been previously found to correlate with expectations of a slower recovery.

The fundamentals

NORTH AMERICA

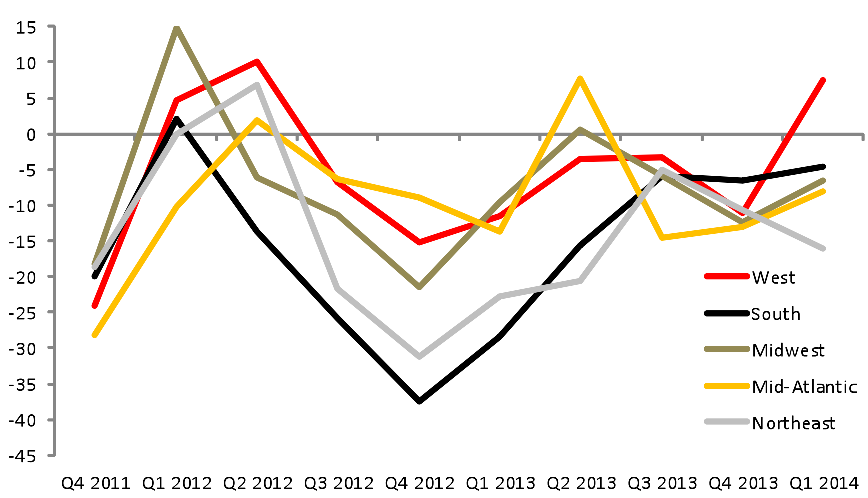
US regions diverge again as industries of the future lead the recovery.
Business confidence and economic sentiment both improved in early 2014, with 60% of respondents optimistic about the state of the economy (up from 50% in late 2013) and 25% reporting rising confidence in their own organisations (up from 23%). US respondents were even marginally more positive about government policy compared to late 2013. This is despite the fact that expectations of public spending growth are now higher than at any time since late 2011, as are fears of over-spending in the medium term: 44% of US respondents in Q1 2014 expected dangerous levels of government over-spending over the next five years.

Some of the improvement in business and economic sentiment can be attributed to better financing conditions: access to growth capital has been improving throughout the past year, and progress accelerated further in early 2014. Otherwise, however, US fundamentals do not support greater optimism. Both business and investment opportunities fell, and respondents reported greater price and exchange rate volatility than at any point in 2013. Business capacity building slowed marginally, breaking a year-long pattern of rising investment, while cashflow and demand conditions remained broadly unchanged for a second quarter running.

From an industry perspective, US business confidence was boosted by strong performance in research- and technology- intensive sectors, but the year-long rally in manufacturers' business confidence appears to have come to an end. More worryingly, confidence in the retail, wholesale and distribution sectors fell for a third consecutive quarter, prompting a steep fall in capital spending.

Meanwhile, the US regions' performance has diverged again (see Figure 10), with respondents in the West reporting significant confidence gains, while the South, mid-Atlantic and Midwest reported marginal gains. By contrast, respondents in the Northeast reported a second consecutive quarter of confidence losses.

Figure 10: GECS business confidence indices by US region



Business confidence bounces back in Canada as two years of stalled growth come to an end
Finance professionals in Canada have been reporting deteriorating demand and cashflow conditions since 2011. Yet, even after accounting for seasonal and other factors, it appears as though the improvement seen in this respect in early 2014 means that conditions have bottomed out and should now begin to recover.

This development follows the bottoming out of growth capital access in mid-2013. Early 2014 saw a significant improvement in this regard, and access is now easier than at any point since 2011. With opportunities for inorganic growth dwindling, capacity building among businesses has bounced back and shows signs of stabilising.

As a result, business confidence among Canadian respondents rose for a second consecutive quarter and crossed over into positive territory for the first time in two years – 29% of respondents (up from 20%) reported confidence gains, while 26% (down from 28%) reported losses of confidence. Perceptions of the recovery have continued to improve for a third consecutive quarter, with 73% (up from 63%) of respondents optimistic about the state of the economy and only 22% (down from 30%) pessimistic. Even assessments of government policy, which had been deteriorating for two years, now appear to have bottomed out in late 2013.

Consistently with a more established recovery, the latest quarter has also seen an end to more than a year of increasing spending expectations by finance professionals.

WESTERN EUROPE

Post-bailout Ireland cheers, but businesses struggle to tap international trade opportunities

The macro-economic outlook in Ireland improved in early 2014. More than two thirds of the Irish sample (69%, up from 65%) were optimistic about the state of the national economy, while only 28% were pessimistic, down from 35% in late 2013.

Following a temporary slowdown in late 2013, cashflow and demand conditions improved substantially in early 2014, and are now stronger than at any time in the last three years. Similarly, prices and foreign exchange rates are at their most stable for years.

For the first time in years, Irish respondents are expecting public spending to increase in the medium-term, and confidence in the sustainability of public spending remains high, practically unchanged since late 2013.

But not all fundamentals are equally healthy. Access to growth capital improved, but remains highly volatile. Business opportunities fell in early 2014, establishing what now appears to be a year-long downward trend. In particular, the combination of fewer opportunities to invest in quality standards and fewer opportunities to explore new markets over the last six months point to weakening access to international supply chains.

These negative developments have meant that businesses aren't yet able to capitalise fully on the improved macro-economic outlook in Ireland. Business confidence fell in early 2014, and is now up only marginally year on year. 36% of respondents reported confidence gains, down from 40% in late 2013, while 23% reported losses, up from 18%.

UK turnaround earns government a thumbs-up but 'budget effect' delays confidence boost

The UK's fortunes have transformed since mid-2013, and this broadly upward trajectory continued in early 2014. Respondents reported a growing number of business opportunities, access to growth capital improved and price levels and exchange rates stabilised further. Meanwhile, opportunities for inorganic growth appeared to reach a plateau, fuelling further business capacity building in the new year. Overall, the recovery consensus was strengthened in early 2014, with 70% of respondents optimistic about the state of the recovery (up marginally from 69%) and only 26% pessimistic (down from 30%).

Despite strong signs of progress, business confidence levels remained essentially unchanged, and a smaller share of the business population accounted for most of the economy's new-found dynamism. 22% of UK respondents reported a loss of confidence, down from 25% in late 2013, while 40% of UK respondents reported confidence gains, down from 43% previously. This is partly due to a 'budget effect', also observed in early 2013. Its effect has been to focus attention overwhelmingly on tax and spending decisions and put investment on hold, which in turn suggests that business confidence should accelerate once again in Q2.

For the first time since the GECS began, UK respondents were, on balance, approving of their government's response to economic conditions, even though they now believed fiscal retrenchment was bound to last a little longer than previously expected. Finance professionals' change of heart is almost certainly related to the improving state of the economy, but respondents also conceded that government support for investment had increased in early 2014.

SOUTH ASIA

Finance professionals upbeat as India works its way out of the FDI slowdown, but a new credit crunch looms.

Indian respondents' macro-economic outlook has improved significantly in the six months to March 2014, and is now more positive than at any time over the last two and a half years. Two thirds (67%) of the India GECS sample between Q4 2013 and Q1 2014 were optimistic about the local economy, up from 46% in the previous six months. Another 33% were pessimistic, down from 51%.

Overall, it appears as though the FDI crunch that endangered the recovery in 2013 is coming to an end. Business opportunities increased significantly in the last six months, suggesting a full recovery from a two-year slump. With a small lag, business capacity building has also started to stabilise after a year-long downturn, and cashflow and demand conditions have also started to recover following a significant tightening in late 2013. Importantly, price and exchange rate volatility is now lower than at any point in almost two years.

In response, business confidence has recovered from a slump in late 2013, and is once again up year-on-year. 43% of respondents in Q4 2013 and Q1 2014 reported confidence gains, up from 29% in the previous six months, while only 30% reported losses, down from 49% previously.

Despite improving fundamentals in many respects, there are also signs that India's economy is facing new headwinds. Respondents report that access to growth capital is still tightening, and deteriorated substantially over the last months, exacerbating an 18-month negative trend.

Finance professionals look to electrifying new prospects as Pakistan shakes off the post-election blues

Business confidence in Pakistan has been on the rise almost steadily for a year and a half and is now higher than at any point in the last three years: 43% of respondents reported confidence gains, up from 36% in late 2013, while only 30% reported losses, down from 41% previously.

For the time being, the fundamentals do not fully support such confidence levels, although they do point to a recovery from the uncertainties of the electoral cycle. The macro-economic outlook is positive, but perceptions of the recovery appear to have reached a ceiling in late 2013. In Q1, a majority of respondents (55%, unchanged from Q4 2013) were optimistic about the state of the economy while 39% were pessimistic (up from 34% in late 2013).

Cashflow and demand conditions, as well as access to growth capital, tightened marginally in the first quarter of 2014, while maintaining the gains made in late 2013 and concluding the recovery from last year's temporary crunch.

Respondents' outlook for business opportunities was unchanged since late 2013, and is still down year-on-year, while opportunities for non-organic growth soared, continuing an upward medium-term trend that has persisted for the last two years.

Finally, respondents reported falling inflation and foreign exchange rate volatility in early 2014. While this is a positive development, the medium-term trend still appears to be towards deterioration in this area.

That said, three quarters into the post-election period, respondents have reported improved energy supply for industry and now expect more prudent fiscal policy in the medium-term. As a result, they have revised their views on government policies dramatically upwards in early 2014, marking a third consecutive quarter of rising approval. Partly as a result of this, business capacity building in Pakistan strengthened significantly for a second consecutive quarter and is now stronger than at any point over the last three years.

ASIA PACIFIC

China's liquidity crunch fades into background as fiscal policy is expected to counter slowing growth

GECS figures suggest that China's liquidity crunch has now abated, with conditions in the mainland slowly returning to normal. Cashflow and demand conditions could take another six months to stabilise, but access to growth capital has strengthened to pre-crunch levels.

Despite some improvements, respondents' macro-economic outlook, which briefly showed signs of recovery in late 2013, has returned to the levels seen earlier that year – 63% of respondents in the mainland are pessimistic about the state of the economy, up from 60% six months earlier, and only 38% are optimistic, a figure unchanged from six months earlier. More ominously, business confidence fell for a third consecutive quarter and is now at a 12-month low, with a majority of respondents in the mainland (53%, up from 43% six months earlier) reporting a loss of confidence in the prospects of their own organisations. One quarter (25%) reported confidence gains, up from 20% six months earlier.

The reason for this further deterioration appears to be a continuing slowdown in China's economy, with both business and inorganic growth opportunities falling marginally in early 2014. This, combined with lingering effects of the crunch and rising financial instability, meant that business capacity building was unable to recover in early 2014. This downturn, however, appears to be coming to an end as business opportunities and capacity building are both showing signs of having bottomed out. Furthermore, respondents in the mainland are reporting increasingly favourable views of government policies and appear to be expecting a very robust fiscal response from the authorities over the medium-term.

Despite improving outlook, regional financial instability holds back investment in Hong Kong

Meanwhile, in Hong Kong, respondents' macro-economic outlook improved for the sixth consecutive quarter. More than half (52%) of the Hong Kong sample are now optimistic about the domestic economy, up from 41% six months earlier, while only 35% are pessimistic, down from 44% in Q3 2013. This is in line with improving fundamentals, as business opportunities grew for a third consecutive quarter, cashflow and demand conditions improved very substantially, and opportunities for non-organic growth also proliferated.

As a result, business confidence recovered significantly in early 2014, ending a nine-month slump, but remains low by global standards. Only 10% of the Hong Kong sample reported confidence gains in Q1 2014 (up from 5% six months earlier), while 38% reported a loss of confidence – down from 54% in Q3 2013. Despite improving sentiment and improved access to growth capital, continued financial instability in the wider region, and growing expectations of fiscal tightening in the medium-term meant that business capacity building fell for a second consecutive quarter.

Post-election blues give way to deepening financial turmoil in Malaysia

In Malaysia, both business confidence levels and respondents' macro-economic outlook deteriorated marginally in early 2014. 63% of respondents were pessimistic about the state of the economy (up from 62%), while only 27% (down from 31%) were optimistic. Nearly half (49%, down from 51%) reported a loss of confidence in the prospects of their own organisations, while only 12% reported confidence gains, down from 21% in late 2013.

The fundamentals point to more trouble ahead. Following a good end to 2013, cashflow and demand conditions weakened again in early 2014 and were virtually unchanged year-on-year.

Business opportunities also fell, and only opportunities for inorganic growth remained resilient. As a result, despite improved access to growth capital for a second consecutive quarter, business capacity building fell. Most importantly, though, price and foreign exchange rate volatility intensified for a fifth consecutive quarter: a record 81.5% of respondents cited rising input costs over the past three months while 46% cited an adverse impact from shifting exchange rates.

Despite increasingly unfavourable business conditions on the ground, respondents' satisfaction with government policy, which had been slipping since the May 2013 elections, now appears to have stabilised. However, respondents in Malaysia had been calling for tighter fiscal policy long before the 2013 elections, and are now more likely to expect the government to overspend in the medium-term than at any point in the past three years.

Uncertainty takes hold in Singapore despite improving fundamentals

Singaporean respondents' macro-economic outlook has changed significantly in the new year: although the broadly upward trend of the past two years has been preserved, an unprecedented 20% were unsure whether conditions were improving or not, up from just 3% in late 2014. 40% of respondents were optimistic (down from 51% previously), while another 40% were pessimistic, down from 46%.

This sense of uncertainty has some basis in the fundamentals of the economy. According to GECS respondents, price and exchange rate volatility moderated in early 2014, but the year-long trend towards further instability seems most likely to continue into the middle of the year.

Accordingly, business confidence was up for a second consecutive quarter, but responses paint a picture of increased volatility. While 29% of respondents reported confidence gains, up from 19% in late 2013, 34% reported losses, also up from 32%.

Both business and investment opportunities grew significantly in early 2014, despite a marginal deterioration in cashflow and demand conditions. Access to growth capital also improved quarter-on-quarter, although it is still on a downward trajectory, having peaked in Q3 2013. The combination of new opportunities and a stronger supply of funding help maintain business capacity building on a strong upward trajectory, although seasonal influences meant that it was down slightly quarter on quarter.

Geopolitical turmoil in Central and Eastern Europe crushes fledgling recovery

In many ways, conditions on the ground in early 2014 were promising. After a long slump between mid-2012 and mid-2103, cashflow and demand conditions were recovering strongly, particularly in early 2014. Business opportunities fell only marginally, while still maintaining a year-long broadly upward trend, and opportunities for inorganic growth completed their recovery from a two year slump. Access to growth capital, which had tightened in mid-2013, stabilised.

Geopolitical uncertainties were already being reflected in soaring price and FX volatility, and a second consecutive quarter of falling business capacity-building. But respondents clearly felt that the worst was yet to come.

Business confidence, which had already fallen in late 2013, plummeted: 50% of respondents in the region (up from 39% in Q4 2013) reported a loss of confidence in the prospects of their organisations. Only 17% reported confidence gains, up from 19% previously. Faith in the recovery also receded. The pessimists made up 63% of the CEE sample in early 2014, up from 54%, while the optimists made up 36%, down from 43% previously.

In the Middle East, an increasingly dynamic regional economy runs into financing headwinds.

Following a temporary burst of exuberance driven by the Expo 2020 boost in the Emirates, business indicators in the Middle East have suffered an adjustment, and returned to a more normal (and still upward) trajectory.

Business confidence is still up significantly year on year but fell slightly in Q1 2014, with 41% of respondents reporting confidence gains, down from 47% in late 2013. Another 27% reported losses, down from 29% earlier. Similarly, finance professionals' macro-economic outlook was more cautious in early 2014 compared to late 2013. 63% of respondents in the region felt optimistic about the state of their national economies, down from 74% in late 2013, while 29% were pessimistic, up from 22% previously.

But some of the latest surge in confidence is slowly being reflected in business conditions on the ground. Cashflow and demand conditions improved substantially, rising above the global average for the first time in nearly three years. Business opportunities also grew substantially, and are now finally up year-on-year. Finally, although price and exchange rate volatility increased in the first quarter of 2014, it is down substantially year on year and the general trend suggests the journey to financial stability is almost complete.

These three trends have added to an almost unbroken three-year trend of rising capacity building by businesses continued in early 2014, and promise a much more dynamic regional economy in 2014. However, it is worth noting that access to growth capital is still highly volatile: despite a strong improvement in Q1 2014, current trends point towards further deterioration.

Business confidence falls in the Caribbean as financial turbulence returns

In the Caribbean, both business confidence and economic sentiment deteriorated in early 2014. 43% of respondents were optimistic about the state of their national economies, down from 45% in late 2013. Over half (53%) were pessimistic, up from 49%

previously. Only 14% of respondents reported rising confidence in the prospects of their own organisations, down from 34% in late 2013, while 39% reported a loss of confidence, down from 48% previously.

The shift in confidence is strongly supported by deteriorating fundamentals. Business opportunities in the region fell sharply for a second consecutive quarter, back to levels last seen in the third quarter of 2012. Investment opportunities also fell, and are now scarcer than at any time during the last three years. Cashflow and demand conditions tightened, although they remain close to average levels for 2013. Most importantly, a year-long trend towards increasing price and exchange rate stability was broken in early 2014, and the tentative recovery in access to growth capital was interrupted. As a result capacity building by businesses fell for a second consecutive quarter, to the lowest levels observed in the last three years.

Perhaps not surprisingly, support for government policies in the region has reached a new low, continuing a trend that has persisted over the past three years. Government spending is still expected to grow in the medium-term, but expectations have become much more moderate than last year.

Post-Taper financial instability in Africa scuppers hard-won trust in governments

Cashflow and demand conditions among businesses in sub-Saharan Africa improved significantly in early 2014, but this was not enough to boost confidence among the region's finance professionals.

Access to growth capital tightened further compared to late 2013, and a pattern of medium-term deterioration is now emerging. Price and exchange rate volatility increased for a second consecutive quarter, and with it opportunities for inorganic growth – at least for cash-rich businesses.

As a result, and although business opportunities fell only marginally, capacity building fell sharply to the lowest level in almost two years. Business confidence remained constant, with 33% of respondents (up from 32%) reporting confidence gains and 36% (up from 35%) reporting losses. Similarly, faith in the recovery remained broadly constant: the optimists made up 57% (up from 56%) of the African GECS sample, while the pessimists made up 41% (down from 42%). A substantial loss of faith did occur elsewhere though. In early 2014, respondents throughout Africa were much more critical of policymakers, who, up until the Taper, were doing a good job of winning back trust.

Views from the coalface

IMPRESSIONS AND COMMENTARY FROM SELECTED MARKETS

'We have definitely experienced a slow-down in orders. We service the manufacturing industry, and orders consist of parts, repair/rebuild services and installation of new equipment. The installation of new equipment services has suffered the most in the last 4 to 5 months ...and looks the same going forward.'

Controller, medium-sized manufacturer, US (Midwest)

'Stimulus programs are running out of steam, while at the same time, senior management is so risk-averse that needed investment is not occurring. This seems to be creating a downward spiral. For example, one company lost several major customers because they couldn't produce the product needed; senior management's response was to close two factories.'

Manager, Big Four, US (Northeast)

'It is hard to meet higher utility bills when pay is frozen. As a result, people haven't got enough to give and charities find it very difficult to raise funds. This has led to spending cuts and training internal staff to do financial processes that were once outsourced.'

Senior finance officer, medium-sized charity, UK (Scotland)

'Foreign currency exchange rates are moving so fast, and so predictably, it is not possible to forecast in foreign currency as previously. We're having problems doing business between Russia and the Ukraine.'

Controller, small IT/communications business, Russia

'The government's decision to join the [Eurasian Economic Community] Customs Union was followed by foreign exchange rate fluctuations, economic obstacles raised by the European Union, and a significant reduction in the financial aid injected into the Armenian economy. We've also seen changes in the legal environment, namely the adoption of a new compulsory pension scheme and a corresponding decrease in salaries.'

External auditor, small financial, Armenia

'The laying off of more than 3,000 workers in the public sector and an increase in income tax deductions have meant that disposable income has decreased and consumers are spending less. This has had a significant impact on the beverage industry. Manufacturing costs are already high and it's difficult to drop our prices without eroding margins significantly.'

Supervisor, large beverages manufacturer, Barbados

'The withdrawal of Bangladesh' GSP [Generalised System of Preferences] status in the US and a similar outlook among other major garments importing countries, combined with ongoing political unrest, have caused significant harm to the country's economy.'

Accountant, large financial, Bangladesh

'Energy crises have been the most critical issue for all manufacturing concerns in Pakistan over the last few years. Control on lead shedding of electricity and committed supply of natural gas by the Government has enabled my organization to improve its financial results in the current year. In addition to that, holding interest rates constant over the last four to six months has also reduced the financing cost for capital projects.'

Internal auditor, large corporate, Pakistan (Lahore)

'The Government's property market cooling measures, e.g. Total Debt Servicing Ratio (TDSR) and increased stamp duty have dampened demand for apartments and impacted developers in Singapore. Shortage of construction workers has always been an issue, but tightening foreign worker quotas and stringent rules for contract renewal make this cost component even higher now.

Controller, large corporate, Singapore

'Central government has issued a law allowing the financial sector to set interest rates based on supply and demand. This act, however, has significantly increased the market borrowing rate from around 6.5% to nearly 8% pa. This has added to a developing liquidity problem on market funds. Consequently, banks are tightening loans issuance and SMEs are seriously impacted by this situation.'

CFO, small business, China (Anhui)

'The constant depreciation of the Ghanaian cedi against foreign currencies has affected economic activity. The worst of it is the Bank of Ghana's directive to close all foreign accounts as well as order for all transactions to be conducted in the local currency. This directive has led to many businesses and investors losing huge sums of money in converting dollar accounts to Ghanaian cedi accounts. Other policies such as the increase in VAT to 17.5%, have affected businesses generally. On the positive side, several micro-finance companies are granting credit facilities for business expansion.'

Accountant, small financial, Ghana

'Several telecommunication companies have emerged and introduced the business concept of mobile money. People have embraced it en mass; and some traditional banks are being affected as more and more confidence is being transferred to the Mobile Money sector.'

Manager, large financial, Uganda

Conclusions

'The economy is generally illiquid as imports far exceed exports. This means that organisations which require audits may defer the engagement as they struggle to raise finance in order to pay for them. When audit assignments are secured, our fees are negotiated down significantly due to the lack of liquidity. Our economy is also mainly informal and the informal sector has no need for our services.'

Senior manager, small practice, Zimbabwe

'The UAE has been awarded the hosting of 2020 EXPO in Dubai. The overall economy will undergo a massive transformation based on the projected government spending of around USD 20 billion. The retail and hospitality industries are going to benefit tremendously though it won't have a significant positive impact on the BoPP [film] manufacturing sector, where we operate.'

Senior manager, large corporate, UAE

'Recent changes in the labour laws of Saudi Arabia have impacted almost all businesses in the region, including professional firms. The attempt to regularize the labour market will yield long-term benefits, but the transition from an unregulated labour market to a more structured one has resulted in an increase in labour-related costs and a related reduction in profits for various companies, especially those where the number of non-Saudi employees is significant. Further, businesses that have not or were not able to comply with the regulations have faced penalties and delays in receiving critical government services.'

Senior auditor, Big Four, Saudi Arabia

The first quarter of 2014 has given finance professionals around the world a lot to think about. With business confidence now in positive territory for the first time in three and a half years, there is little doubt that official quarterly GDP figures will be encouraging across many of the world's major economies, but the underlying strength of the recovery is about to come into question.

The standoff between Russia and the Ukraine is damaging business prospects throughout the broader region and risks contagion beyond. Elsewhere, partly due to the influence of the Taper, the gap in performance between developed and emerging economies is widening. Although global business confidence is on the rise, it is becoming increasingly divorced from fundamentals and confined to a few pockets of financial stability or stimulus-based growth.

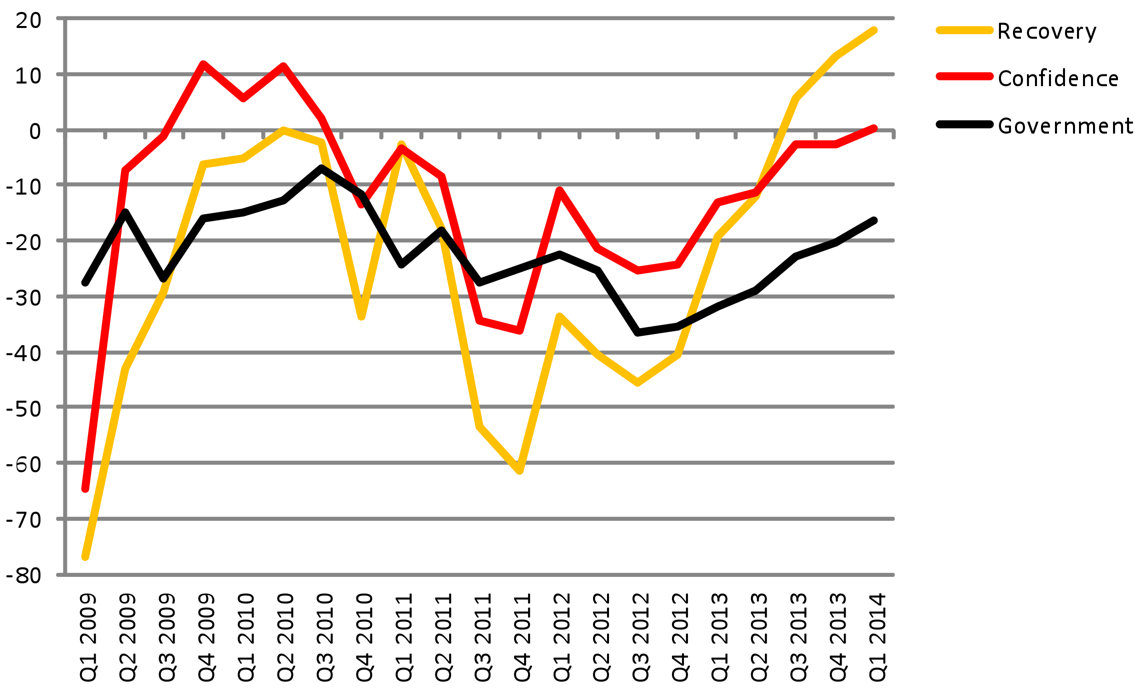
Already, the major emerging economies of Asia and Africa are diverging from the rest of the world and slowing down decisively. As more and more major economies fall off the Recovery Consensus that gained strength throughout 2013, it remains to be seen whether the rest are strong enough to carry the recovery.

That said, it is undeniable that, at the global level, business investment is still picking up and capital spending is increasingly being directed towards more innovative, higher-return projects. A new surge of public spending in Russia, India and China will no doubt add to the momentum. And in further good news, China's liquidity crunch is almost certainly under control and the country's real economy is recovering.

Overall, we expect the rest of the year to be a challenging time, with long-overdue corporate investment propping up a weakening recovery in the short term. But if policymakers around the world can remain committed to financial stability, encourage long-term investment and weather the last of the Taper, the recovery can still take root in 2014.

Annex

Figure A1: Five years of the major GECS Indices



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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