

2.0 General Economic Overview



The majority of respondents believe that despite current difficulties, the Euro will survive.

While economists point to the difficulties of maintaining a monetary union between diverse economies, it is as much a political as an economic question.

All the options to solve the debt crisis in the peripheral economies are unpalatable. Staying in the Euro will require large real wage/price adjustments in these countries to restore competitiveness, on top of austerity measure to correct the public finances; but there would also be severe penalties for a state which sought to solve its problems by leaving the single currency.

The results of the survey reflect the belief that sufficient political will exists to surmount these obstacles.

In terms of Europe's position, most business leaders recognize the reality of an ongoing shift in power to the developing and emerging markets, but this does not necessarily spell doom and gloom for

Europe. The key word in the question is "relative". Global growth is not a zero sum game and there is no reason why Europe should lose out absolutely, just because other countries have superior growth prospects.

In fact, strong growth in the emerging markets should help Europe grow. It's more than likely that Europe could find itself better off economically but with its relative world position still in decline.

On commodity prices, the majority of respondents appear gloomy about any early respite from commodity price inflation. Most participants expect prices to continue to rise and for those rises to hamper the recovery.

In the mid-2000s commodity price run-up, the authorities had scope to offset the negative impact on growth, as overall inflation stayed low but this time the situation is much more difficult. Firstly, inflation rates have gone up sharply in many countries, suggesting that central banks need to tighten policy; and secondly, even if they wanted to, there is little scope for the authorities to implement offsetting measures to support activity. Interest rates are already at rock bottom and the overriding pressures are for budget austerity rather than fiscal expansion.

Regarding the “super-cycle”, half the respondents thought that the commodities bull market could last for an extended period – decades rather than years – on the back of commodity-intensive emerging market growth.

There have been so-called “super-cycles” in the past, but it is incredibly difficult to predict the cycle’s longevity. In the past, at some point, sufficient supply capacity has come on-stream to meet demand – or the spiralling prices have simply killed off growth and prices receded accordingly.

Andrew Smith, Chief Economist

Hypothesis 1

The Euro will cease to exist in its current form within the next five years.

Hypothesis 2

Europe's position as a world economic and political superpower has peaked. Its relative importance will decline over the coming decades as the economies of the emerging markets continue to grow and expand their market share.

Hypothesis 3

The recent appreciation in oil and other commodity prices will continue and curtail the recovery.

Hypothesis 4

Commodity prices are now in a "super cycle" and will continue to rise for a further decade.

