

ECONOMIC BULLETIN

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DEVELOPMENTS IN THE WORLD ECONOMY

The recovery in the global economy has become increasingly self-sustained since late 2010, although divergences in growth patterns across countries and regions prevail. At the same time, global inflationary pressures are also picking up, fuelled in particular by higher oil and non-oil commodity prices. While inflation rates so far remain contained in the advanced economies, there has been a gradual increase over the latter half of 2010 and in early 2011. In dynamic and energy-intensive emerging economies, inflation rates have increased substantially, with overheating pressures emerging in some countries.

Europe: Based on its regular economic and monetary analyses, the Governing Council decided at its meeting on 3 March 2011 to leave the key ECB interest rates unchanged. With regard to the economic analysis, following the 0.30% quarter-on-quarter increase in euro area real GDP in both the third and the fourth quarter of 2010, recent statistical releases and survey-based evidence continue to confirm the positive underlying momentum of economic activity in the euro area at the beginning of 2011. This assessment is also reflected in the March 2011 ECB projections for the euro area, which foresee annual real GDP growth in a range between 1.30% and 2.10% in 2011 and between 0.80% and 2.80% in 2012. With regard to price developments, euro area annual HICP inflation was 2.40% in February 2011, according to Eurostat's flash estimate, after 2.30% in January. The increase in inflation rates in early 2011 largely reflects higher commodity prices. Inflation expectations over the medium to longer term must remain firmly anchored in line with the Governing Council's aim of maintaining inflation rates below, but close to, 2% over the medium term. The Governing Council remains prepared to act in a firm and timely manner to ensure that upside risks to price stability over the medium term do not materialise. Turning to fiscal policies, all governments need to fully implement their fiscal consolidation plans in 2011. It is crucial that substantial and far-reaching structural reforms be implemented to strengthen the growth potential, competitiveness and flexibility of the euro area. The current sovereign debt crisis has reinforced the need for an ambitious reform of the economic governance framework, with more stringent requirements and procedures and a clearer focus on the most vulnerable countries with losses in competitiveness in order to ensure that the new framework will indeed be effective in the long run.

Greece: On 11 March the Eurozone heads of state and government met in Brussels. Subject of their negotiations were the corner stones of the "convincing, comprehensive" solution to the debt crisis which has been announced for the summit on 24th/25th March. The leaders decided the extension of the bailout loan maturity period to Greece from five to ten years, and a reduction in the interest rate from 5.20% to 4.20%. In addition, it was decided that the European Financial Stability Facility (EFSF) will be able to purchase bonds of the "rescued" countries on the primary market.

United States: On 15 March the US Federal Open Market Committee (FOMC) decided to keep the target for the policy rate unchanged within a range of 0% to 0.25%. Quarter-on-quarter real GDP growth stood at 0.70% (2.80% in annualised terms) in the fourth quarter, up from 0.60% in the third quarter and 0.40% in the second. The expansion in the fourth quarter of 2010 reflected stronger momentum in consumer spending growth and a positive contribution from trade, as exports continued to grow and imports declined. Price pressures, despite recently having increased somewhat, remain broadly contained. Annual CPI inflation increased from 1.50% in December to 1.60% in January. The increase in consumer prices continued to reflect primarily the impact of higher energy and food prices. On 26 January, the US Federal Open Market Committee (FOMC) noted that the economic recovery is continuing, though at a rate that has been insufficient to bring about a significant improvement in labour market conditions. In the context of elevated unemployment and low measures of underlying inflation, the FOMC continued to anticipate that economic conditions were likely to warrant exceptionally low levels for the federal funds rate for an extended period. In addition, the FOMC kept its plan to purchase USD 600 billion of longer-term Treasury securities by the end of the second quarter of 2011 in order to help support the economic recovery.

United Kingdom: On 10 March the Bank of England's Monetary Policy Committee voted to maintain the official Bank Rate paid on commercial bank reserves at 0.50%. The Committee also continued to vote for maintaining the stock of asset purchases financed by the issuance of central bank reserves at GBP 200 billion. The economic recovery was interrupted in the fourth quarter of 2010. Real GDP decreased by 0.60% in the fourth quarter of 2010 after expanding by 0.70% in the third quarter and 1.10% in the second quarter. Attributed in part to bad weather in December, the decline in output over the fourth quarter was broad-based across expenditure components. House prices

have continued their declining trend in recent quarters against the background of subdued demand in the housing market. Looking ahead, inventory adjustments, monetary stimulus, external demand and the past depreciation of the pound sterling should support economic activity. However, growth in domestic demand is expected to remain constrained by tight credit conditions, household balance sheet adjustment and substantial fiscal tightening. Annual CPI inflation has remained elevated in recent months, increasing to 4.0% in January 2011, up from 3.70% in December, mainly reflecting the lagged effects of the depreciation of the pound sterling, higher commodity prices and the increase in the rate of VAT in January 2011. Looking ahead, these factors are likely to continue to exert upward pressure on annual CPI inflation.

Japan: On 11 March, a deadly earthquake and subsequent tsunami hit Japan, causing huge losses of human lives and an enormous financial cost. The Bank of Japan tried to support the economy, saying it would inject 15 trillion yen (€132bn) into the banking system. It is expected that the huge cost of rebuilding the affected areas will push up Japan's public debt, which is already the largest among advanced economies. The longer-term real effect of the natural disaster on Japan's economic growth remains to be seen. After strong growth in the first three quarters of 2010, economic activity contracted in the fourth quarter of 2010. Real GDP fell by 0.30% quarter-on-quarter in the fourth quarter of 2010. In addition, exports contracted in the fourth quarter. Overall, real GDP was 3.90% higher in 2010 compared with a year earlier, partly on account of fiscal stimulus measures and increases in external demand. Looking ahead, indicators signal an improvement in the economic climate and point to the gradual strengthening of the economy starting from the beginning of 2011. Annual CPI inflation declined by 0.20% compared with a decline of 0.40% in December. On 15 February 2011 the Bank of Japan decided to leave its target for the uncollateralised overnight rate unchanged at between 0% and 0.10%.

Energy News: Oil prices have increased substantially over the past three months, thereby continuing the upward trend that started in September 2010. Brent crude oil prices stood at USD 111.6 per barrel on 17 March, which is 42% higher than at the beginning of 2010 and 20% higher than at the beginning of 2011. Looking ahead, market participants are expecting slightly lower oil prices in the medium term, with futures contracts for December 2012 trading at USD 111 per barrel. Political unrest in the Middle East and North African region generated concerns that geopolitical factors may threaten supply security, which put additional upward pressure on oil prices. The current situation bears similarities with that of 2008, but the high level of inventories and the possibility to substantially expand production in OPEC countries should provide some buffer against further significant price increases.

CYPRUSECONOMY

The GDP growth rate in real terms during the fourth quarter of 2010 is estimated at 2.50% over the corresponding quarter of 2009. For the whole year 2010, GDP growth rate is estimated at 1.0%. The improvement observed in the economy during 2010 is mainly attributed to the improved performances recorded in the sectors of Tourism, Transport and Trade. The broad Services sector and the Financial Intermediation activities recorded positive results, while Construction and Manufacturing presented negative performances. For 2011 the real GDP growth rate is estimated to range between 1.50% and 2.0%. The rate of inflation for February 2011 rose to 3.10% compared to 3.0% in January 2011 and 2.80% in February 2010. The Consumer Price Index for February 2011 increased by 0.43% compared to January 2011. This is mainly due to increases in the prices of petroleum products. The rate of increase of the Index, and therefore the rate of inflation for February 2011 amounted to 2.80% remaining at the same level as in January 2011 and slightly lower than the inflation rate of 2.90% recorded in February 2010. For the period January-February 2011, the CPI recorded also an increase of 2.80% compared to the corresponding period of 2010. The number of registered unemployed for February 2011 recorded an increase of 2.60% compared to the previous month and reached 25.900 persons. In comparison with February 2010, an increase of 5.857 persons or 24.50% was recorded which was mainly observed in the sectors of trade, accommodation and food service activities, construction, manufacturing, education, transportation and storage, as well as to newcomers in the labour market.

Main Economic Indicators

Period: Fourth Quarter of 2010					
	<i>Europe</i>	<i>United States</i>	<i>United Kingdom</i>	<i>Japan</i>	<i>Cyprus</i>
<i>Real GDP (year on year %)</i>	1.70	2.80	1.55	3.98	1.00
<i>Real GDP (4th quarter 2010 compared to 4th quarter 2009)</i>	2.00	2.80	1.50	-1.30	2.50
<i>Unemployment (%)</i>	10.03	9.63	7.90	5.03	7.40
<i>CPI (year on year %)</i>	2.00	1.27	3.40	0.10	3.10

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