

6. Inflation

After a year marked by deflation in the main advanced countries, inflationary pressure reappeared in 2010, notably in the second half, affected by soaring world prices for commodities, particularly energy and foodstuffs. Thus consumer prices went up by 1.6% on average in **developed countries** after virtual stagnation in 2009.

Similarly, inflation increased somewhat in **emerging and developing countries**, up from 5.2% in 2009 to 6.1% in 2010 on average, leading some countries (like China) to tighten monetary policy to reduce the risk of overheating their economies.

Over the first half of 2011, and in light of disruptions in supply but still high demand, notably in emerging countries, the increase of international prices for commodities (especially energy and foodstuffs) exerted higher pressure on consumer prices in both advanced and emerging/developing countries, fanning thus inflation.

SECTION 2 - CAPITAL MARKETS

2010 was marked by volatility of the main international stock exchanges indexes, with globally an upward trend. The MSCI¹ world index rose by 9.55% for the year.

In the United States, stock exchanges posted major gains: S&P-500 +19.85%, Dow Jones +11%, and Nasdaq Composite +16.9%. Such performance reflects renewed interest in risky assets, helped in particular by the Fed's active policy of quantitative easing.

Stock exchanges in Europe posted differing performance. The CAC 40 fell by 3.34%, due to high exposure of French banks to Greek credit risk. German and British stock exchanges went up over the year, in line with sound economic performance : Dax 30 +16.06% and FTSE 100 +9%. The markets of southern Europe, deeply involved in the debt crisis, had a bad year, with the Greek stock market falling by more than 35% and the Spanish IBEX 35 down by 17.43%.

In Japan, the Tokyo stock exchange closed for 2010 with a drop of 2.26%. The NIKKEI 225 suffered from a strong yen and its adverse impact on export value performance.

As for stock exchanges in emerging countries, the MSCI world index for emerging stocks rose by 16% in 2010, far lower than the previous year's growth rate of 74%.

Globally, the main stock exchange markets pursued over the **first half of 2011** an upward trend in the wake of regain of confidence in the economic recovery of the western countries. The US stock indexes recorded some 7% in gains for Dow Jones and 4.5% for Nasdaq Composite. As for the European markets, and over the considered period, Dax progressed by 6.6%, Cac 40 by some 4.7%, while FTSE posted a virtual standstill. Nikkei was the only index to post a decrease (some 9.6%) over the first quarter of 2011 in the wake of the natural disaster that ravaged the Japanese Archipelago.

The international bond market, after a short period of loss, posted higher yields as economic prospects improved in the United States, with a rate for ten-year US bonds reaching a peak for the year of 3.99% on 5 April for the first time since June 2009, compared to 3.61% in February.

This trend reversed in the second half of the year, with the ten-year rate for US bonds hitting a low for the year of 2.38%, influenced by a series of negative economic indicators in the United States and announcement by the Fed of a new programme to purchase \$ 600 billion in long term Treasury securities. Still, the yield for ten-year US bonds managed to check its losses to close for the year at 3.30%, in line with optimistic outlook of the world economic growth.

¹ MSCI : Morgan Stanley Capital Index.

German bond yields also dropped for most of the year, taking advantage of rising aversion to risk in the wake of the European debt crisis. The yield for ten-year German bonds came to a low for the year of 2.11% on 31 August (compared to more than 3.30% at the beginning of January), before rising to close for the year at 2.96%, boosted by the overall climate of optimism reigning at the end of the year.

Trend in yield rate over the **first half of 2011** went through two different periods. In effect, the upward trend in 10-year bond rates in the main developed economies was pursued in the first quarter of 2011 in the wake of an increase in inflationary anticipations. In the second quarter of the same year, bond yield regressed following weak recovery and anticipated pursuit of accommodating monetary policies in the wake of worries with respect to sovereign debt in the USA and in the Euro Zone countries. US and German yields closed for the first half of 2011 at 3.16% and 3% respectively.

SECTION 3 - INTERNATIONAL FOREIGN EXCHANGE AND GOLD MARKETS

International foreign exchange markets in 2010 were marked by considerable depreciation of the euro against the US dollar, due mainly to escalation of the sovereign debt crisis in the euro zone. This drop was however curbed by adoption of a wide-ranging European bail-out plan and new quantitative easing plan in the United States.

The USD continued to climb against the euro until the beginning of June, on the strength of better growth prospects in the United States as well as uncertainty about growth in the euro zone as financial conditions deteriorated in peripheral countries of the euro zone facing a debt crisis. A record high of \$1.1875 to the euro was posted on 7 June 2011, vs. \$1.4285 at the beginning of the year.

However a series of disappointing economic indicators were published in the United States, casting doubt on the sustainability of US recovery, causing a reversal of the US dollar's upward trend. The euro also profited from sound economic performance in Germany and less concern about financing issues in certain euro zone countries. This change in the attitude of investors was due in particular to release on 23 July of globally positive results for the «stress tests» to which the European Union and Switzerland subjected their banks, along with successful mobilisation of funds by a number of peripheral countries of the euro zone on the international market.

The dollar then took off on a virtually continuous downward spiral starting in June, which closed for the year at \$1.3377 to the euro.

Against the yen, the dollar depreciated by more than 12% for the year, going from 92.90 to 81.50. Japan's currency regained its status as a safe investment in a climate marked by growing fears about the debt crisis in certain euro zone countries. The risk of slowing world growth was also favourable to the yen.

Over the first half of 2011, deterioration of growth outlook in the United States, with disclosure of deceiving US economic indicators and soaring oil prices in the wake of intensified political pressure in North Africa and the Middle East, maintained pressure on the dollar which pursued its downward trend against the euro, reaching its lowest level for 17 months (1.4939) on 4 May. Concurrently, the euro took advantage from anticipations that came to guarantee an imminent return to normal conditions with respect to ECB monetary policy. The single currency enjoyed also relatively less worries about spreading of the debt crisis in certain countries of the Euro Zone to the rest of the region. EUR/USD parity closed for the first half-year period at 1.4522.

Over the first six months of the year, the dollar oscillated within a wide range against the yen (between 76.99 and 85.54). The disastrous earthquake of 11 March in Japan, then tsunami and the ensuing nuclear crisis increased volatility of the Japanese currency which closed for the first quarter at 80.52 yens to the dollar.