

Global Recovery hinges on the Right Timing of Exit Strategies

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Last week, the International Monetary Fund revised its forecast for global growth this year to 3.9 per cent - up 0.8 percentage point from its October forecast - but the challenges remain. This revision was based on a stronger-than-expected rebound in the second half of last year, thanks to sizeable stimulus packages globally and a faster-than-expected recovery in emerging and developing economies.

The IMF forecasts that emerging and developing economies will grow at 6.0 per cent, given strong macroeconomic frameworks and sound financial fundamentals.

Meanwhile, growth in advanced economies is expected to return to positive territory of 2.1 per cent, led by the US with 2.7 per cent, whose forecast has been revised upward significantly by 1.2 percentage points.

In the immediate future, US consumers will likely remain on a tightrope given the sharp drop in household net worth, tight credit, a sluggish housing market and high unemployment.

Coming from weak growth, Japan continues to struggle with its deflationary problem.

The excess economic slack as well as an outright fall in unit labour costs will likely exert heavy downward pressure on inflation over the year.

In addition, private consumption and investment are likely to remain weak as corporate profits are falling and business sentiment remains depressed.

In the euro zone, poor credit conditions coupled with the relatively weak financial position in the corporate sector will pose ongoing challenges for policymakers.

In addition to differences in growth expectations for individual economies, diverse challenges are also confronting these groups of economies. Pressures have started to be observed

in asset values and surges in capital inflows have led to currency appreciation in emerging and developing economies.

As for advanced economies, the common challenges are to tackle mounting unemployment and ballooning public debt.

At this juncture, the policy rates in advanced economies are widely anticipated to be kept on hold on account of their relatively weaker growth outlook and fragile recoveries.

On the other hand, given growing concerns over asset price bubbles and foreign-exchange pressure arising from capital inflows and inflation, the focus of monetary policy in emerging and developing economies would possibly shift from managing the recovery to maintaining price and financial stability for sustainable growth.

Raising interest rates - to curb inflationary pressures and swelling asset prices - ahead of developed economies may invite more capital flows into emerging economies.

In turn, this would lead to greater exchange-rate volatility in global financial markets, posing risks to business adjustment, and could make the recovery path less firm.

On the whole, since the global economy will continue to improve but unevenly this year, it is imperative that the unwinding of monetary policy be part of well thought out exit strategies across major advanced and emerging countries.

Appropriate timing and sequencing of policy exits will ensure a sustainable path to recovery while maintaining confidence and stability in international financial markets.

(The views expressed are the author's own.)

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