

Future Macroeconomic Policies in the Making

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Macroeconomic policies implemented during the crisis will inevitably shape the future world economic landscape. Monetary and fiscal policies have provided full support to the Thai economy through the record-low policy interest rate and sizeable fiscal stimulus packages, while on global and national level, some signs of economic recovery are gradually emerging. This is an important turning point for policymakers since a well-navigated next move could lift up economic growth while a policy misstep could lead to a deeper slump.

One of the papers to be presented at the Bank of Thailand's annual Symposium identifies several medium-term macroeconomic challenges arising from the global crisis and subsequent policy responses. With large export contraction and the drops in investment and confidence following the global economic downturn, Thailand's potential output growth has been moderating.

It implies lower expected revenues and greater pressure on the country's fiscal position. Looking forward, large-scale public debts borrowed to finance the stimulus packages need a clear plan for consolidation to ensure fiscal sustainability. Indeed, how the corrective fiscal adjustments could be carried out without disturbing the fragile recovery process will be the real test.

Slower potential growth also adds uncertainty to the monetary consideration. This gap between actual and potential output signals the heat of the economy's demand relative to supply. When the economy operates under its potential, i.e. negative output gap, demand is sluggish and hence the need for stimulus to prevent prices from falling. Nonetheless, the ongoing but unobservable potential growth slowdown makes it difficult to derive the output gap and the appropriate monetary policy response.

As the Thai economy recovers, neither premature nor delayed withdrawal of monetary stimulus seems appealing. Moreover, intensification of financial imbalances, particularly in asset

prices, could translate into higher domestic inflationary pressure should excess global liquidity flow into Asia on account of its stronger recovery than other parts of the world.

The key issues mentioned are intertwined since the medium-term macroeconomic policy framework needs to balance the challengers in growth, stability, and sustainability altogether. Aside from the delicacy and firm disciplines devoted to policy design and execution, chances of success will hinge heavily on policy coordination to compensate for each policy's limitations.

One possibility of a win-win-win solution is to initiate a positive feedback loop by increasing public investment to raise the potential output, thereby lessening the inflation concern of monetary policy in light of a larger negative output gap. In turn, the improved economic conditions and well-anchored inflation expectation would help enhance fiscal position and its sustainability, expanding fiscal space for more gradual consolidation.

Crisis always puts the spot-light on the role of policymakers. The sub-prime financial melt-down proved no exception.

The Bank of Thailand is holding a symposium "Coping With and Looking Beyond the Global Crisis" at Bangkok Convention Hall, Centara Grand Hotel at CentralWorld on September 15-16.

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

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