

Path to Global Recovery Reaches Critical Crossroads

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LAST WEEK, the International Monetary Fund (IMF) revised its forecast for world GDP growth for 2010 to 4.2 per cent. This is not the first time that the IMF has upped the growth forecast for 2010. It adjusted the forecast to 3.9 per cent in January, 0.8 of a percentage point higher than last October's forecast, reflecting the better-than-expected recovery momentum.

The other main message has remained that the global outlook is proceeding at a multi-speed recovery led by emerging Asian economies. This multi-speed recovery is obvious not only among different groups of economies but also within those groups, as different countries entered the crisis with different fundamentals.

For the advanced economies, the US is expected to lead the recovery with 3.1 per cent growth, on account of its healthier non-bank position and more effective fiscal stimulus measures. The recovery in the euro zone and Japan remains fragile and sluggish with less than 2.0 per cent growth.

Substantial fiscal stimulus measures in these advanced economies have translated to rising public debt and fiscal deficits. In particular, fiscal burdens are more severe in the euro zone, where sovereign ratings have already been downgraded in Greece, Portugal and Spain.

This poses new challenges for policy-makers in maintaining growth linked to the fiscal sustainability concern. While credible medium-term fiscal consolidation strategies are urgently required in countries with high sovereign risk premium to shore up confidence, these efforts will adversely affect the recovery in the near term.

As for emerging and developing economies, the recovery is being led by Asian economies, owing to their strong economic fundamentals-especially China. On the stability front, inflation has been rising in Asia due mainly to higher food and fuel prices. While it remains contained and unlikely to peak in the coming months, checks on inflation should be maintained or it could rise following the upward trend in commodity prices.

Better growth prospects for the region, coupled with the return of risk appetite, have resulted in the resurgence of capital inflows into the Asia. But these flows, as noted by Oliver Blanchard of the IMF, are "gifts" that emerging countries have to handle well. Otherwise, they risk creating financial imbalances that turn into boom-bust cycles in the recipient countries.

Going forward, the sustainability of overall global economic recovery will require clear sustainable recovery paths for both advanced and emerging economies. While policymakers are facing diverse situations in different countries, they share the common challenge of sustaining the growth momentum while safeguarding macroeconomic and financial stability.

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

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