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Antalya

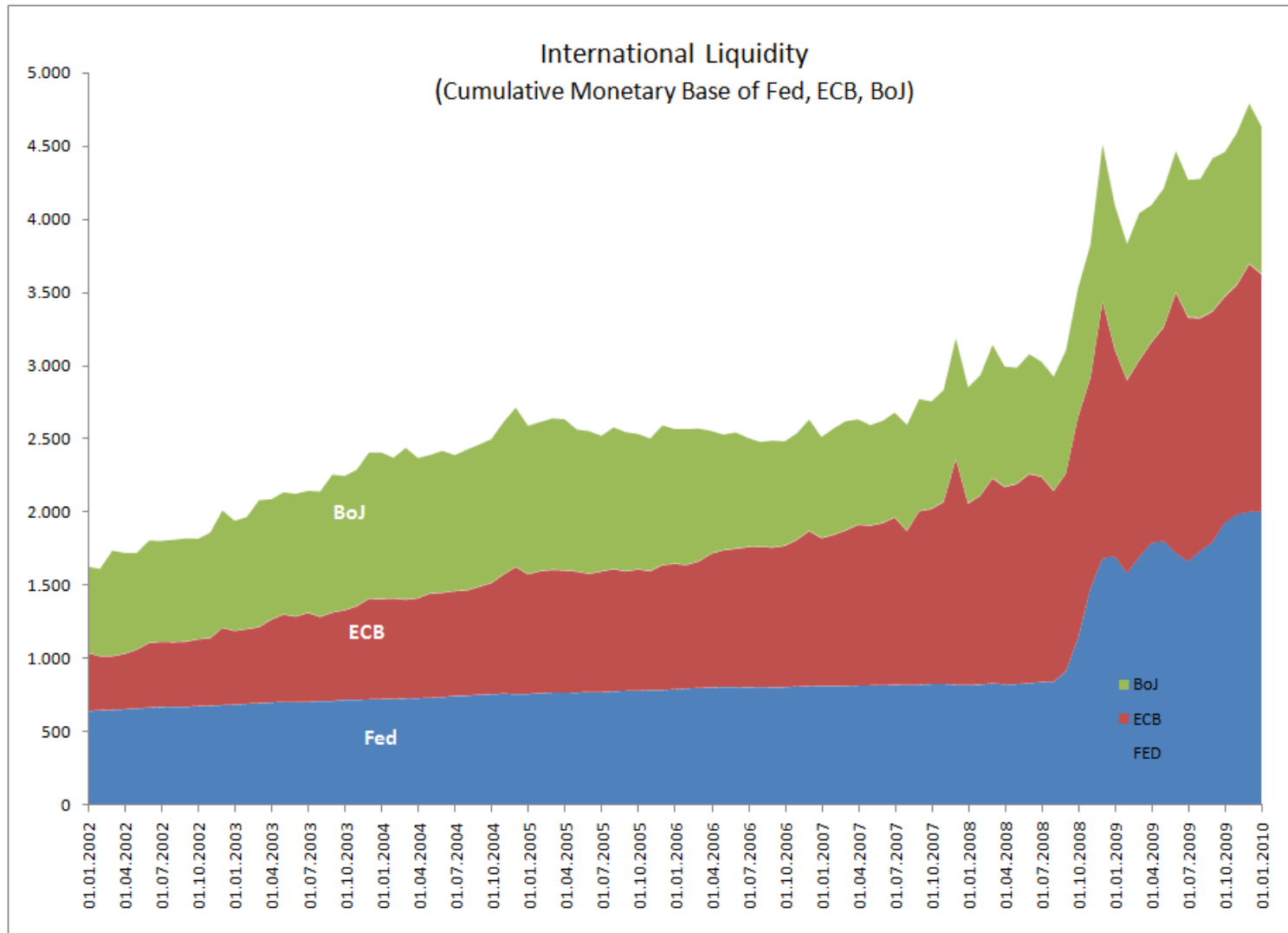
Post-Crises Macroeconomic Trends and Policy Recommendations for Developing Countries

Murat Yulek, Ph.D.
Managing Director
PGlobal Global Advisory and Training Services Ltd.

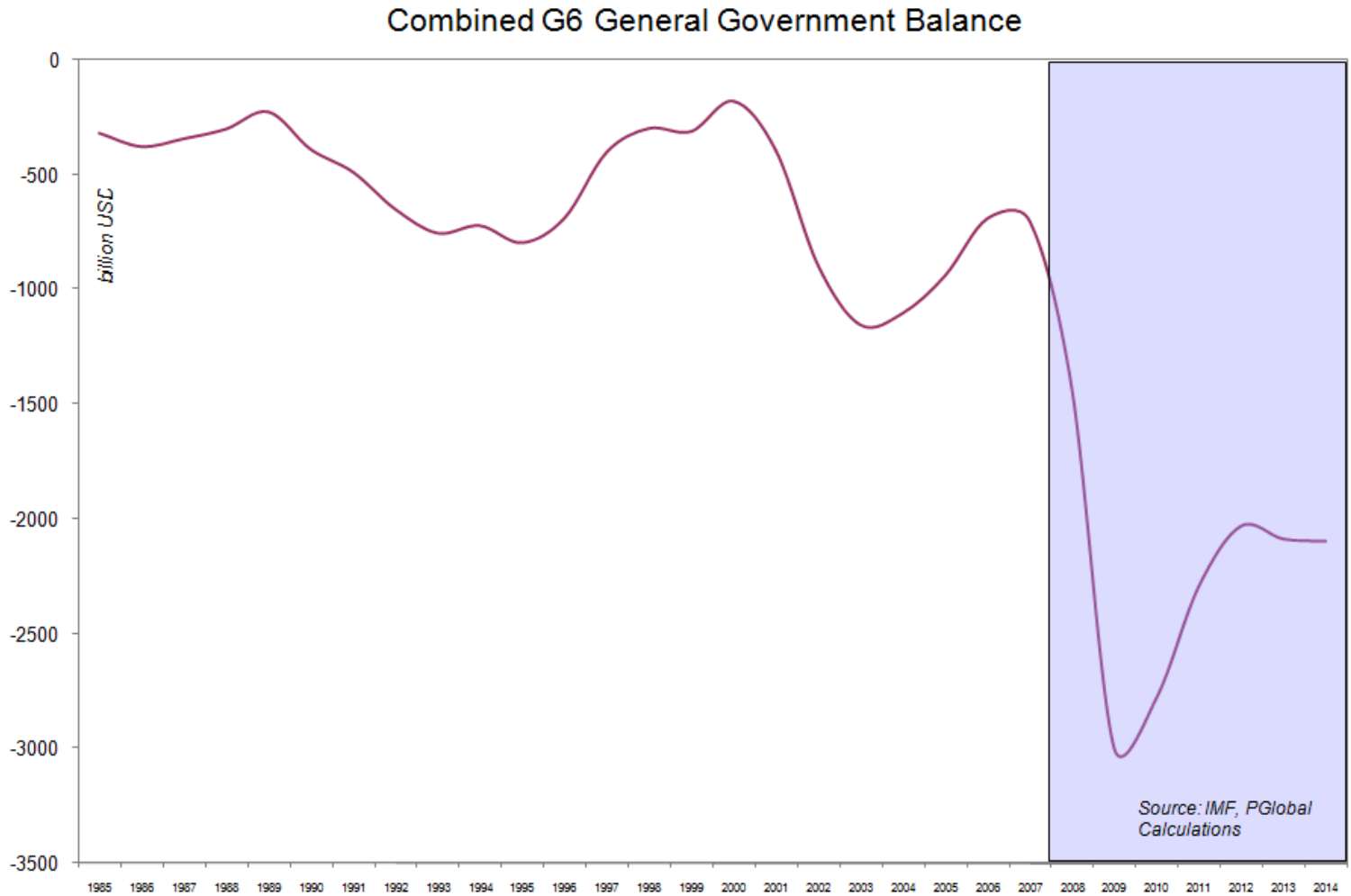
Major trends in the international macroeconomic environment in the next five years: Summary

- *Sustainable recovery in the global economy, especially in G3, will take long time.*
- *Liquidity will have to remain high in spite of*
 - *All the “exit” talk*
 - *Possible sustained uptrend in commodity prices*
- *Fiscal consolidation in the developed economies, is a must; however, there are serious doubts if these economies will be able to produce necessary political will for hard measures.*
- *China’s ascend will continue*
- *So will the commodities*
- *Volatility, uncertainty ... will accompany the global economy for a long time*

International liquidity doubled in less than two years

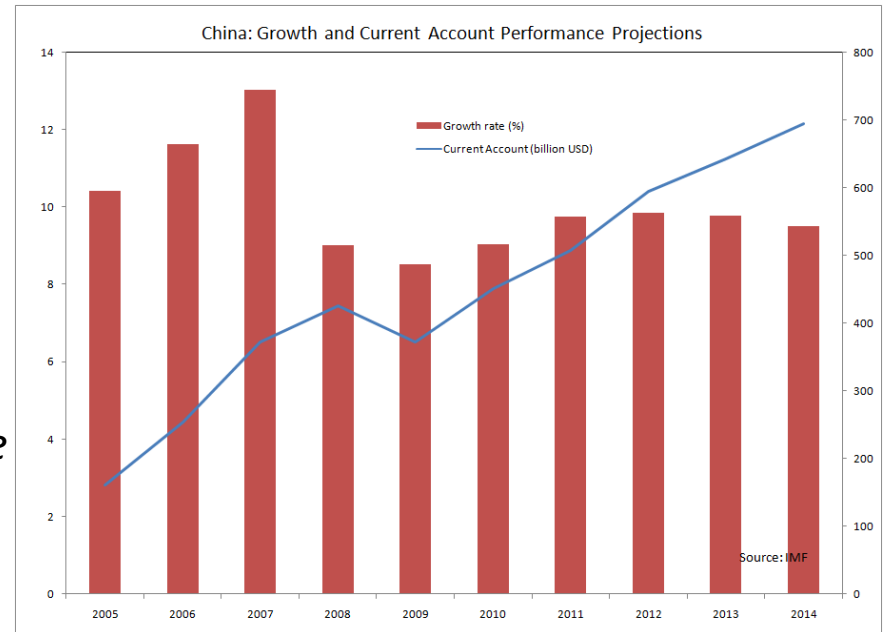


Fiscal expansion recorded unprecedented levels



China and commodities will continue their ascension

China's growth will be enforced with its position as provider of low cost merchandise in the light of weak consumer income and confidence. That is a tough call for competing businesses in other countries and China's market share is likely to increase accompanied by rising commodity prices pushed by demand from China.



What does all this mean for the developing countries?

Liquidity and Investment Flows

Action by Developing Countries

There will be abundant liquidity and low interest rates

Take advantage of the better liquidity environment which may enhance access to funds necessary for the development process

But there will also be high competition for that liquidity

- Western economies: high fiscal deficits and borrowing requirements until fiscal consolidation can be successfully completed
- Developing economies: borrowing needs to complete development cycle

Keep the macroframework sound in order to keep (i) your country attractive for investment; (ii) borrowing costs low

Be selective to incoming investment with a view to (i) keep real exchange rate competitive; while (ii) getting the maximum benefit from imported funds

China's Ascend

China's ascend will continue increasing competitive pressure on companies in developing as well as developed countries

Under weaker international demand, it will be harder and harder for local businesses in industries in the "runway of China" to either (i) sustainably continue their operations; or (ii) produce economically meaningful returns and value.

Action by Developing Countries

"Protection" can only be a short-run solution to the problem.

Medium-to-long term measures
Design and effectively implement policies to (i) support sectoral transformation as well as inter-sectoral migration of local businesses out of the "runway" of China; (ii) invest in human capital; (iii) support design, branding, clustering efforts; (iv) support learning process of local industries; (v) support sectors that have positive spill over effects.

Short term measures
Keep real exchange rates competitive while concentrating on the "real" measures above.

Increasing Commodity and Energy Prices

Action by Developing Countries

The recent rebound of commodity prices is likely to be sustained in the medium run


Resource poor countries will face pressure on their current account balance and their budget, while resource rich ones will continue to have a boon

Resource poor countries will have to increase energy investment to develop in local primary energy sources, especially renewables. They will also have to design cautious and judicious fiscal policy. In some countries, energy importation is a source of fiscal revenue through indirect taxation. That may tempt these governments to keep a blind eye on energy importation bill; that will be a huge mistake as current account deficits are a source of vulnerability.

Resource rich countries should properly replenish their sovereign wealth funds and international aid funds with a view to protect shares of next generations and contribute to international development.

Increasing Volatility and Uncertainty

Action by Developing Countries



Global economics
will face more and
more uncertainty
and volatility

Sound macroframework and fiscal and monetary policies are a must.

Monitor domestic and international money and capital markets closely.

Monitor capital inflows closely to make sure the policies are right to direct them to the “right” sectors under “right” terms.

Monitor current account as it is a critical source of vulnerability.

Monitor real exchange rate closely as its overvaluation will weaken competitiveness and increase pressure on local businesses and employment.

Thank you

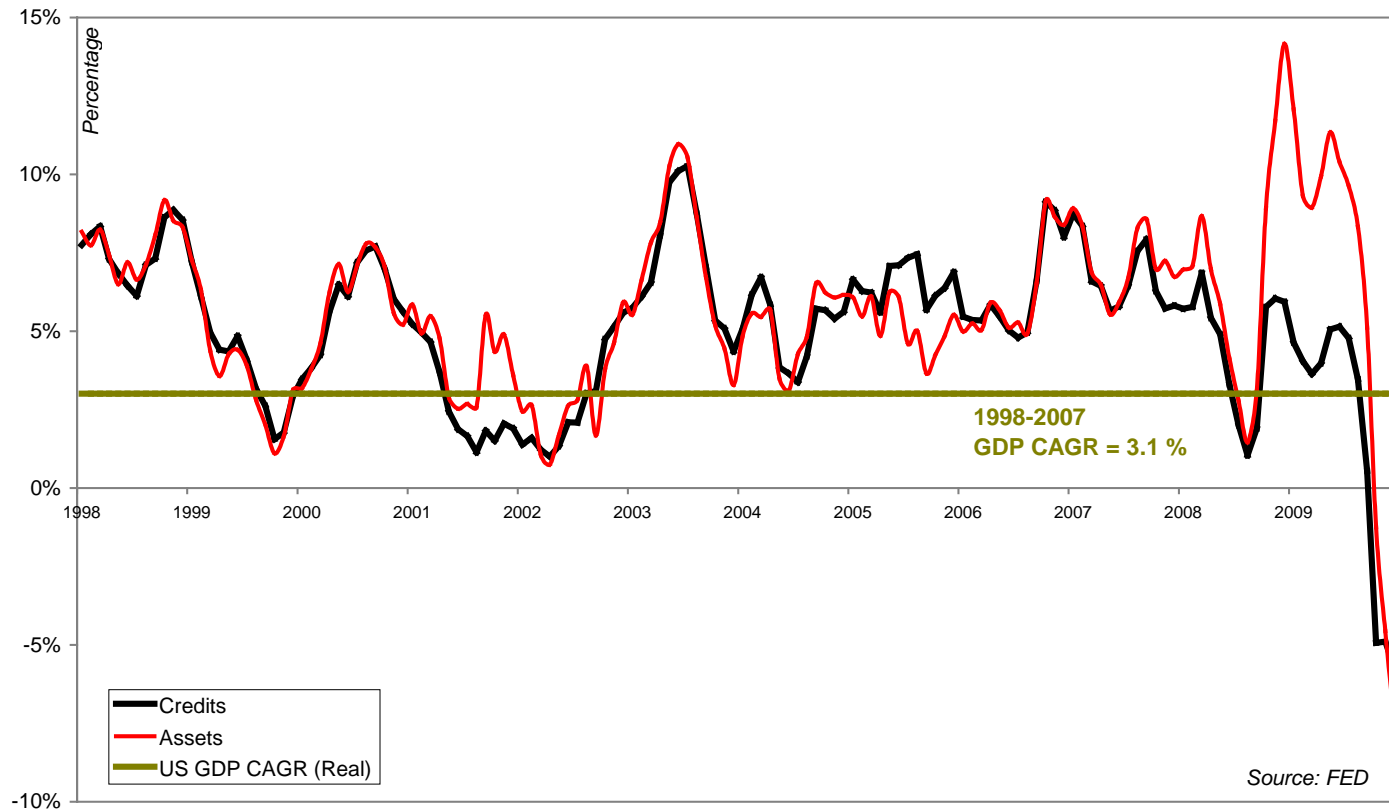
Content

- A Selective Post-crises Stock Taking Exercise
- Post Crises Global Trends
- Policy Recommendations for Developing Countries

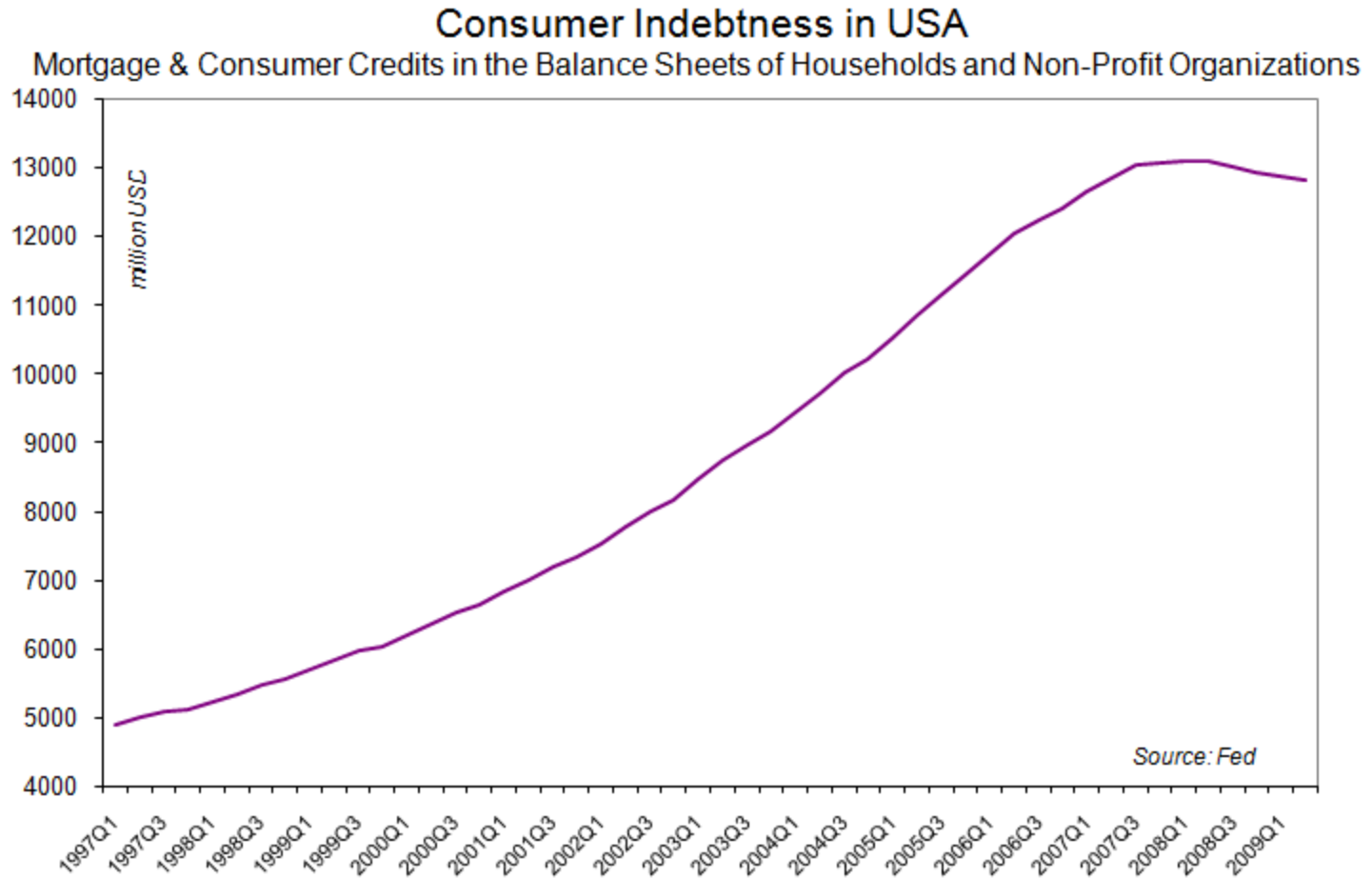
Crises: A Sad Episode

Behind the financial crises in the USA was, among others, the rapid expansion of bank credit ...

US Commercial Bank Credits and Total Assets
YoY Real Growth Rates

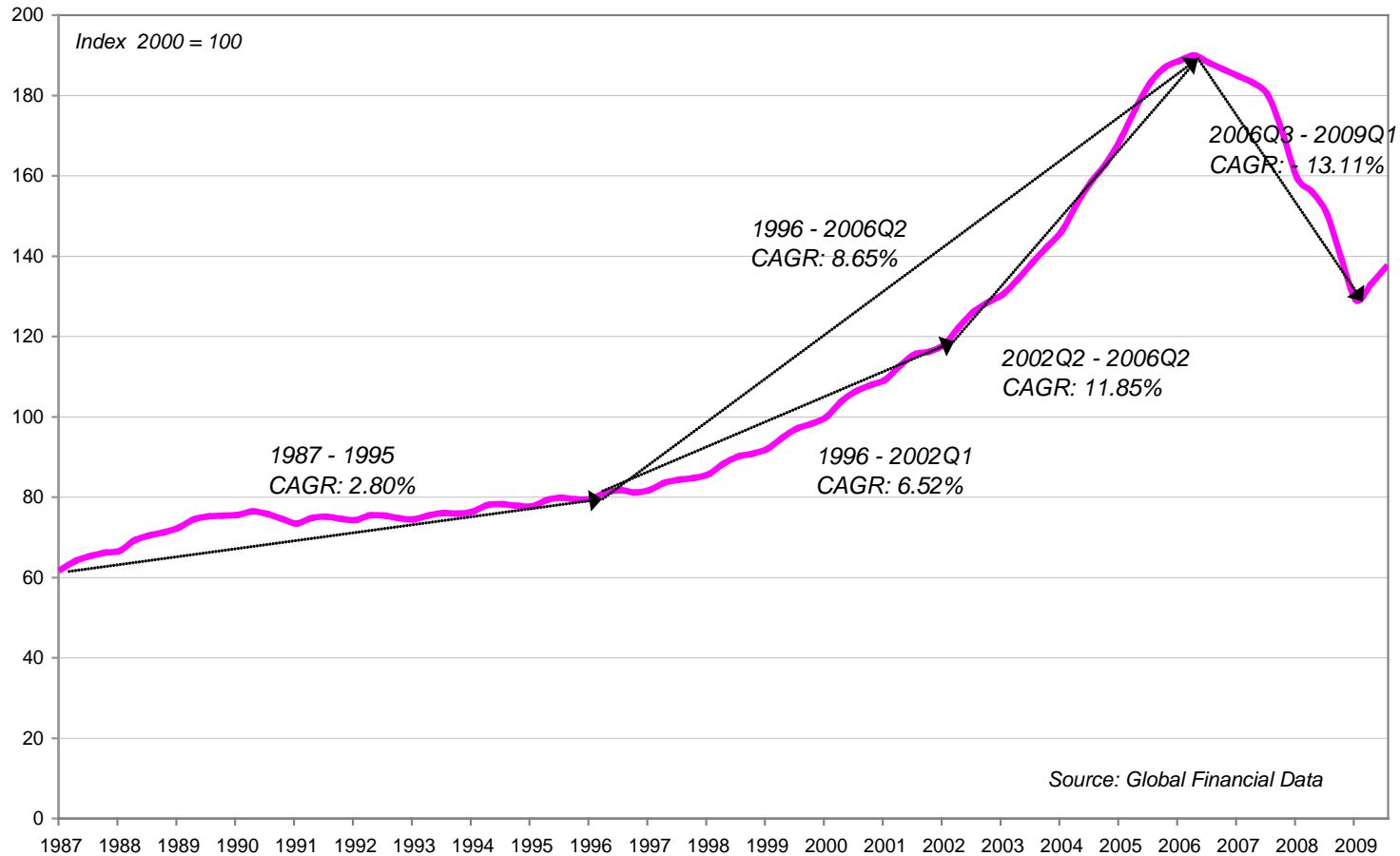


... and increasing leveraging by households ...



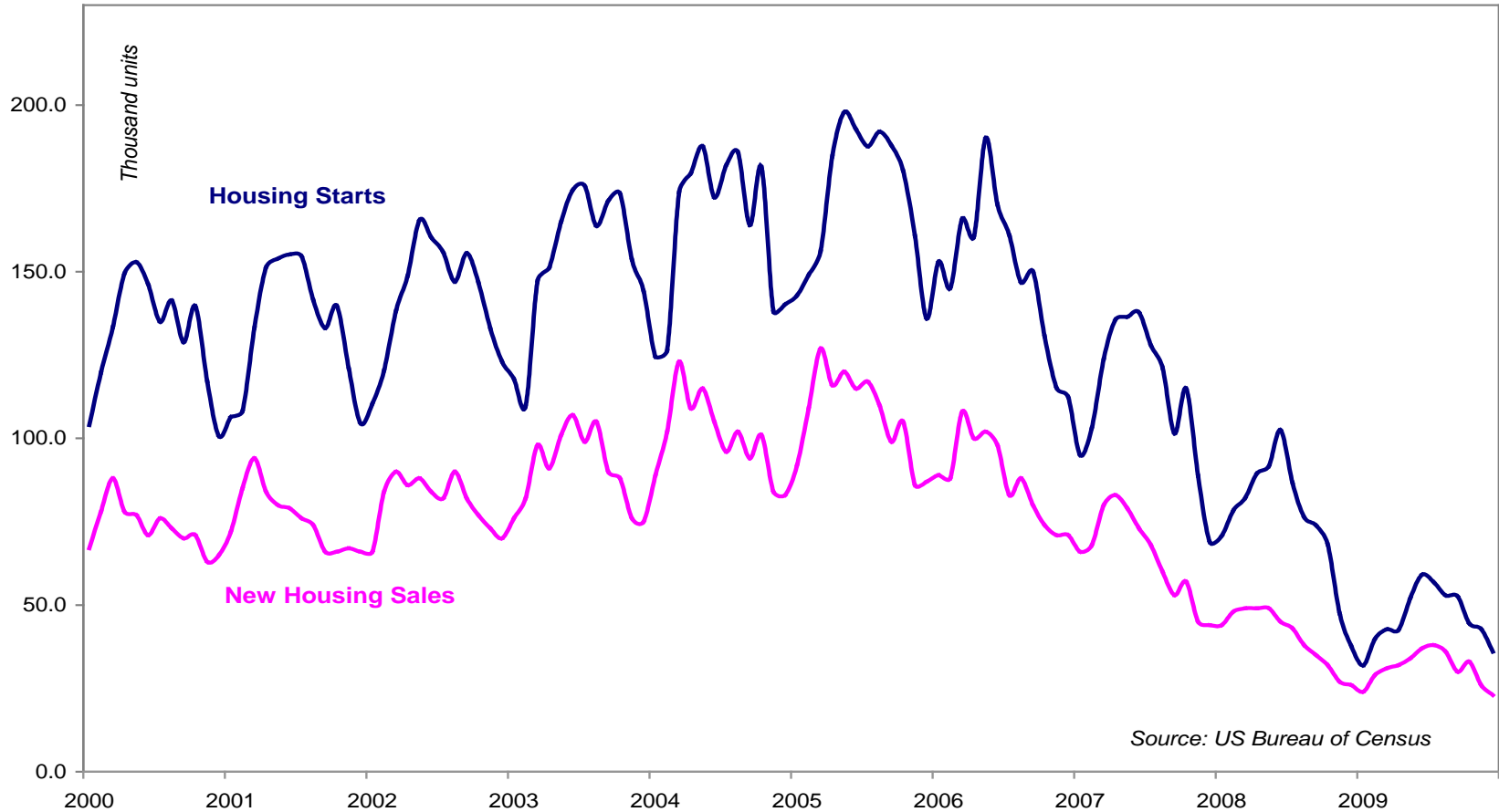
... rapidly heating real estate market

US Residential Real Estate Prices (Case Schiller Index)

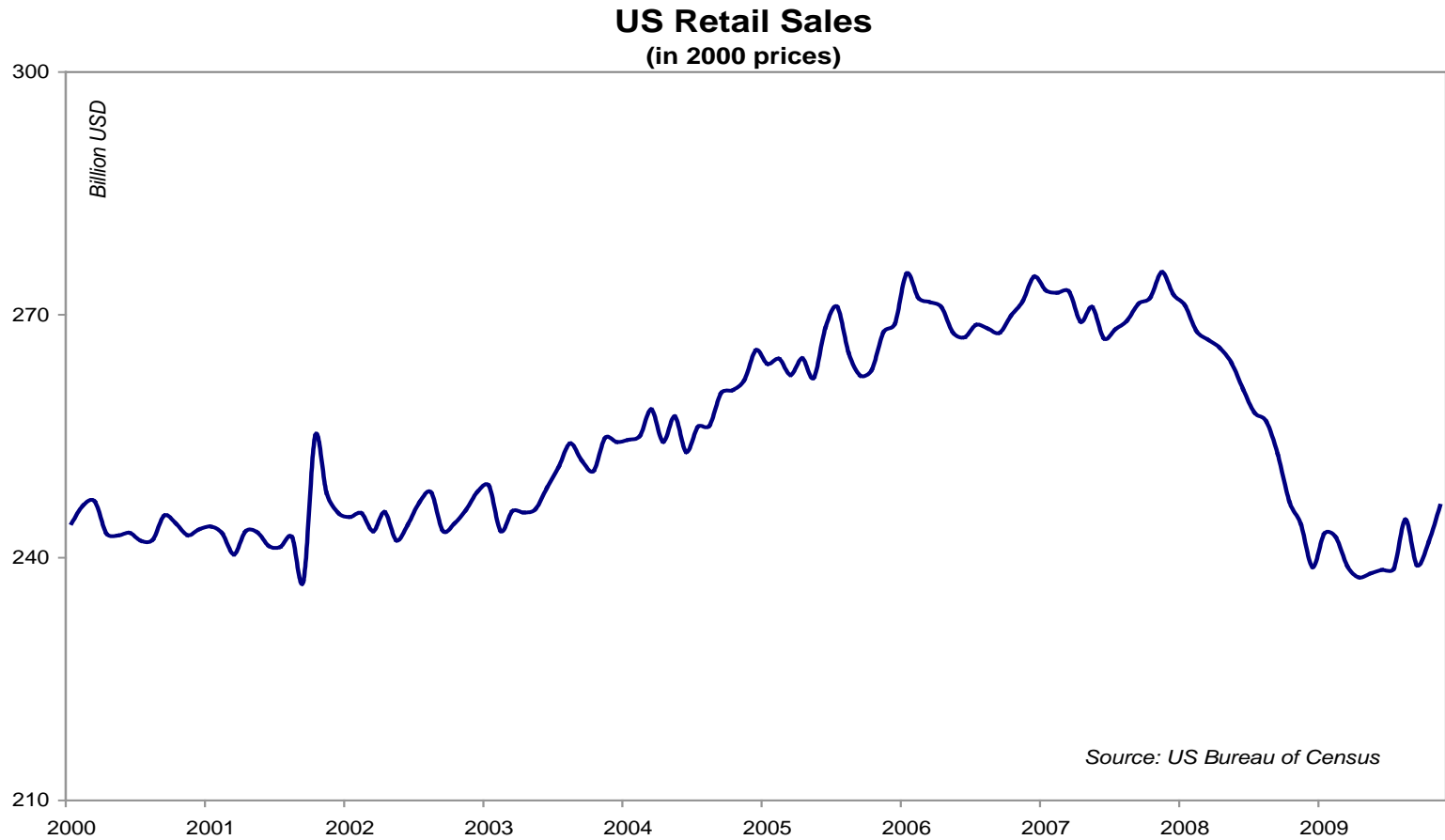


The residential real estate market collapsed causing a large financial sector shake down ...

US Housing Starts and New Home Sales

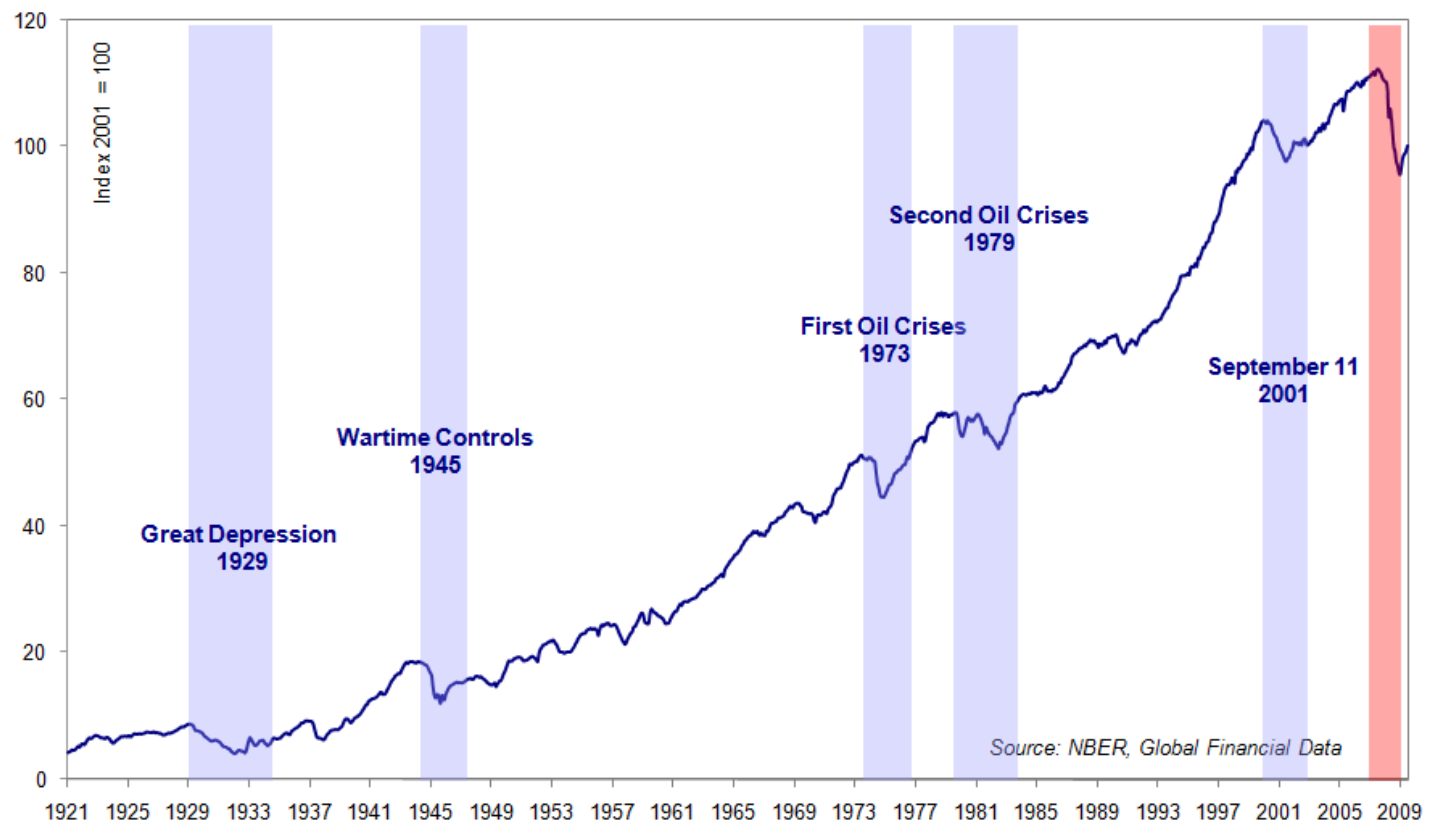


... taking with it the consumption appetite ...

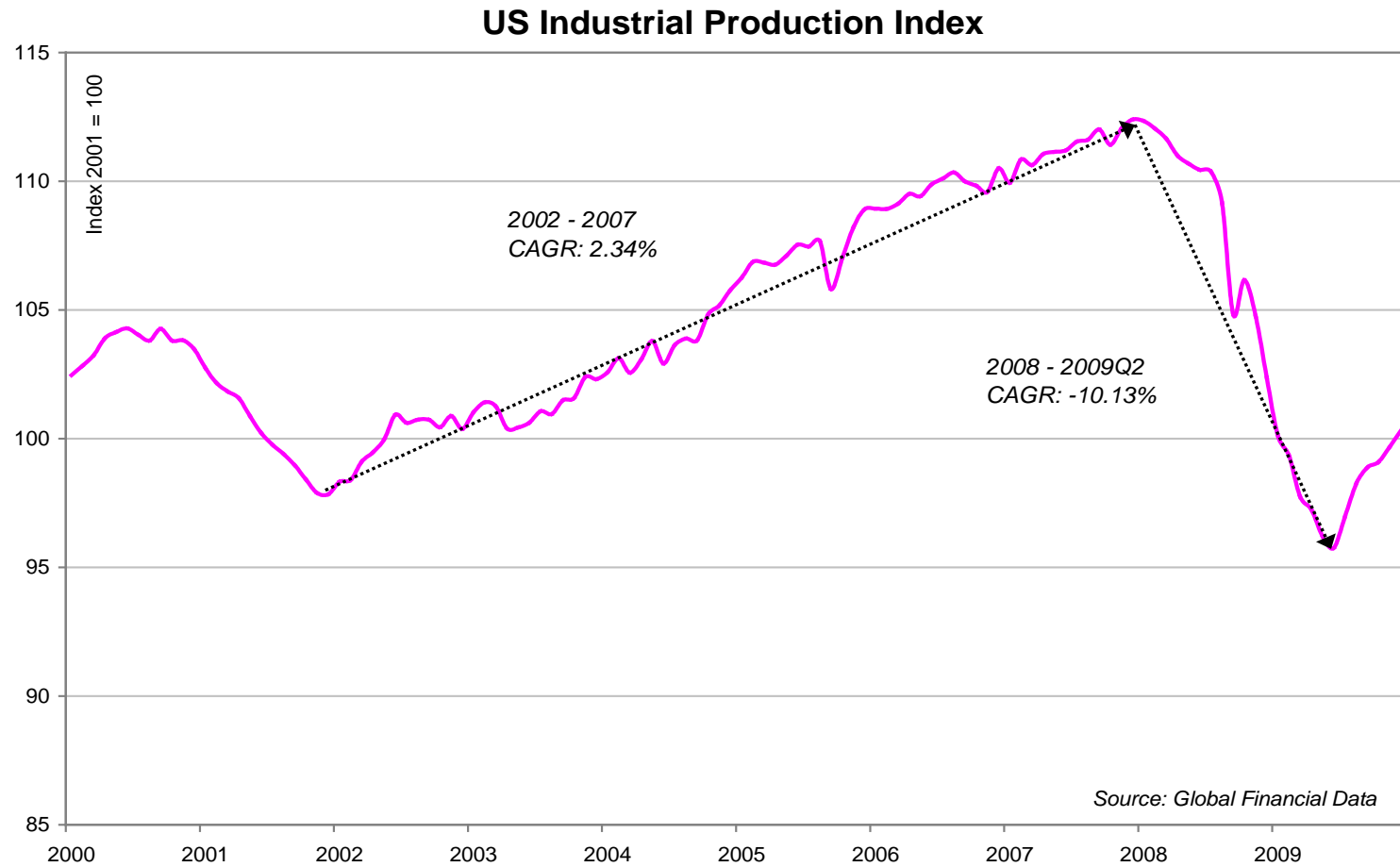


... and the industrial production ...

A Schematic History of US Industrial Production Index
(1921 - 2009)

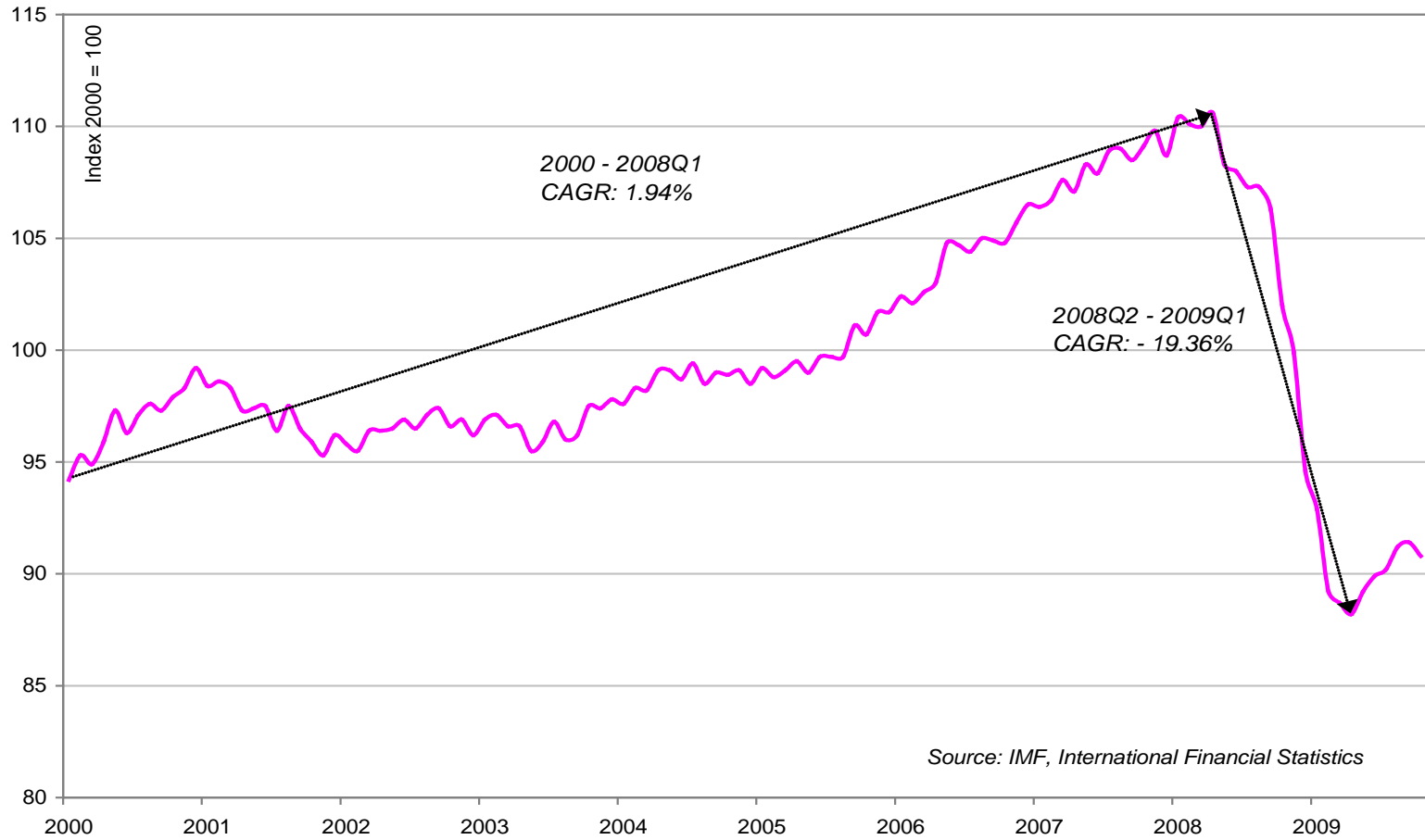


... wiping out all the gains since 2001

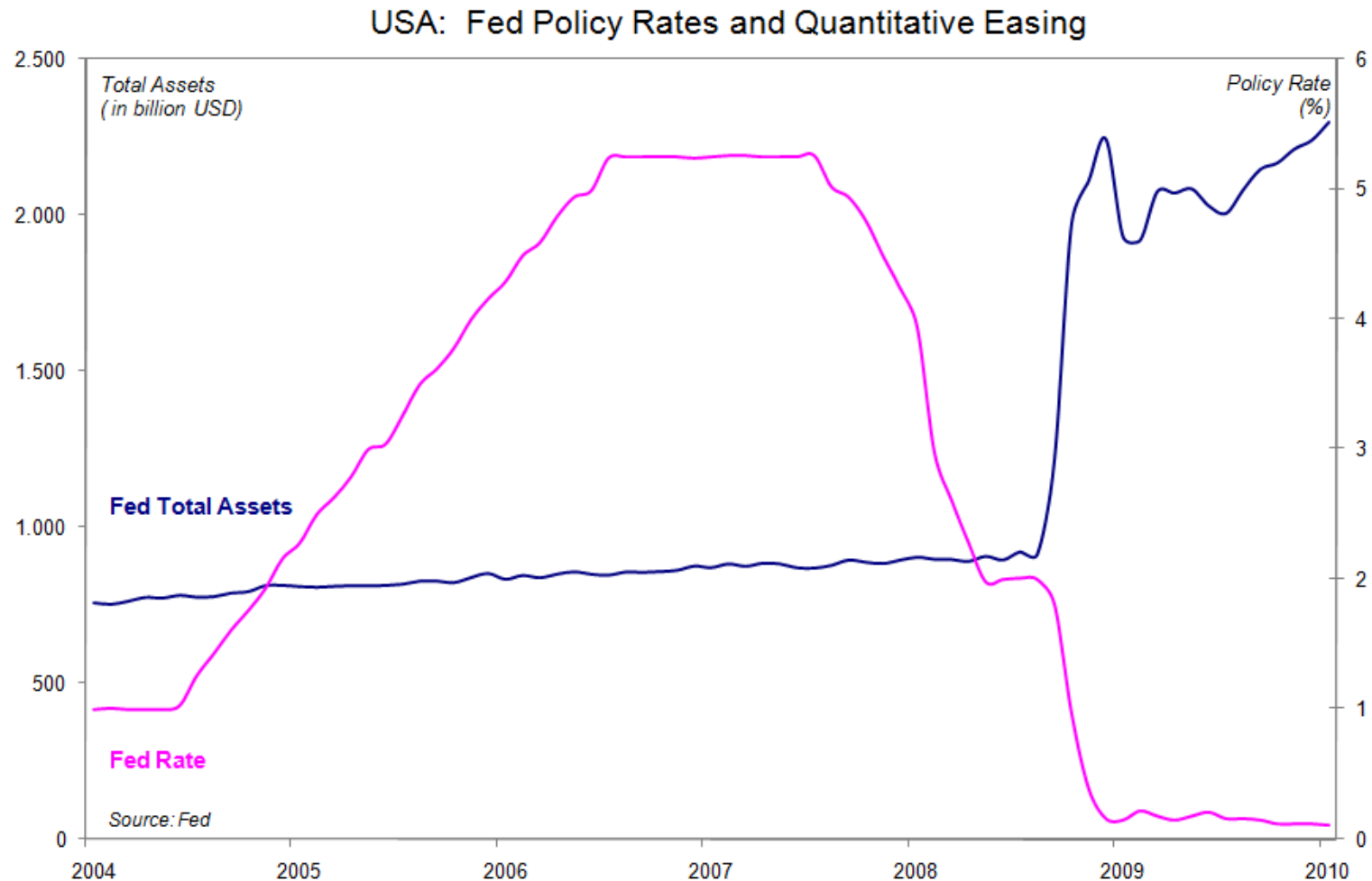


Slow down in the real activity was not limited to USA

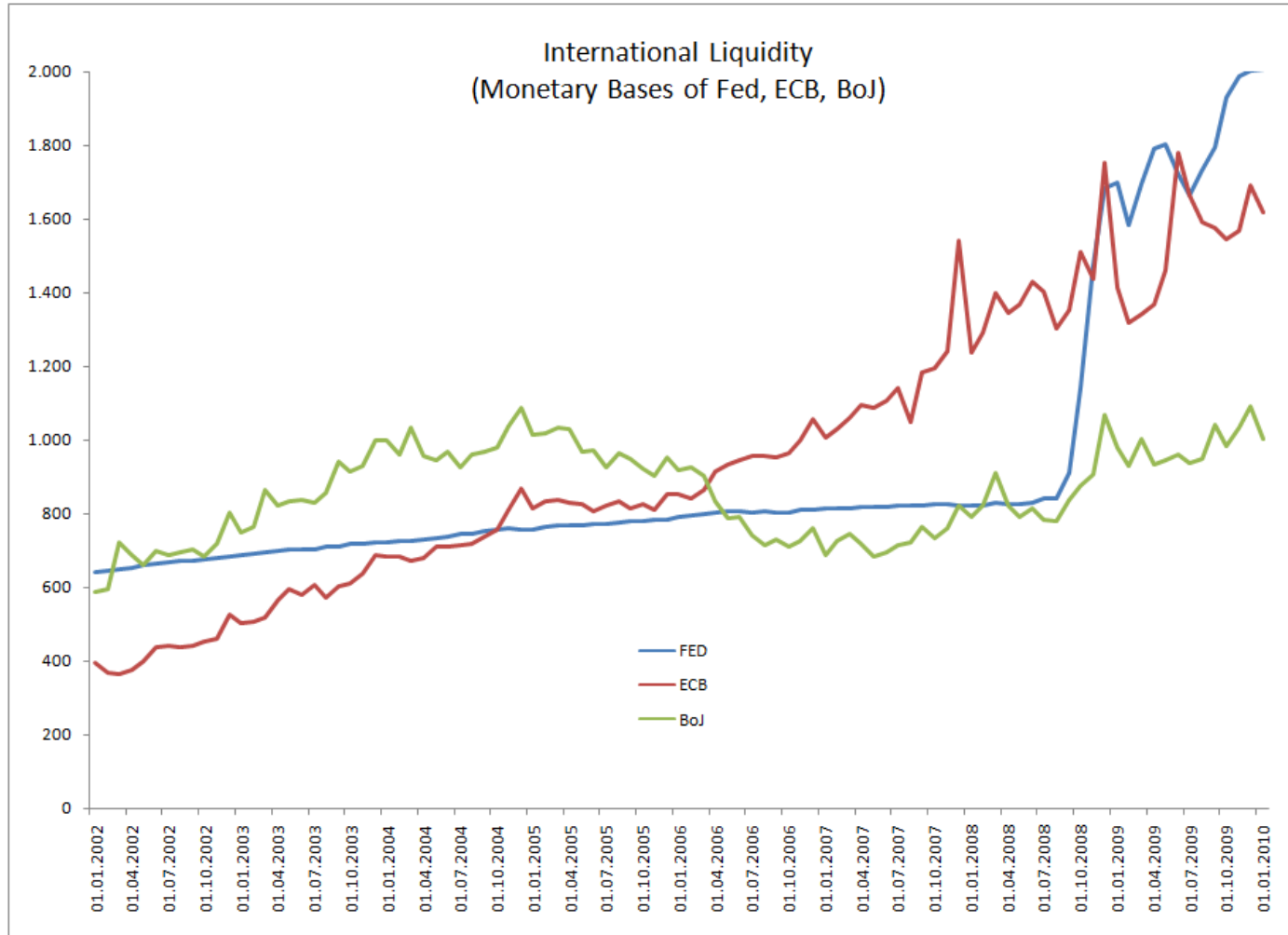
EU Industrial Production Index



The perceived magnitude of the problem triggered a monetary expansion of unprecedented size not only in the USA ...

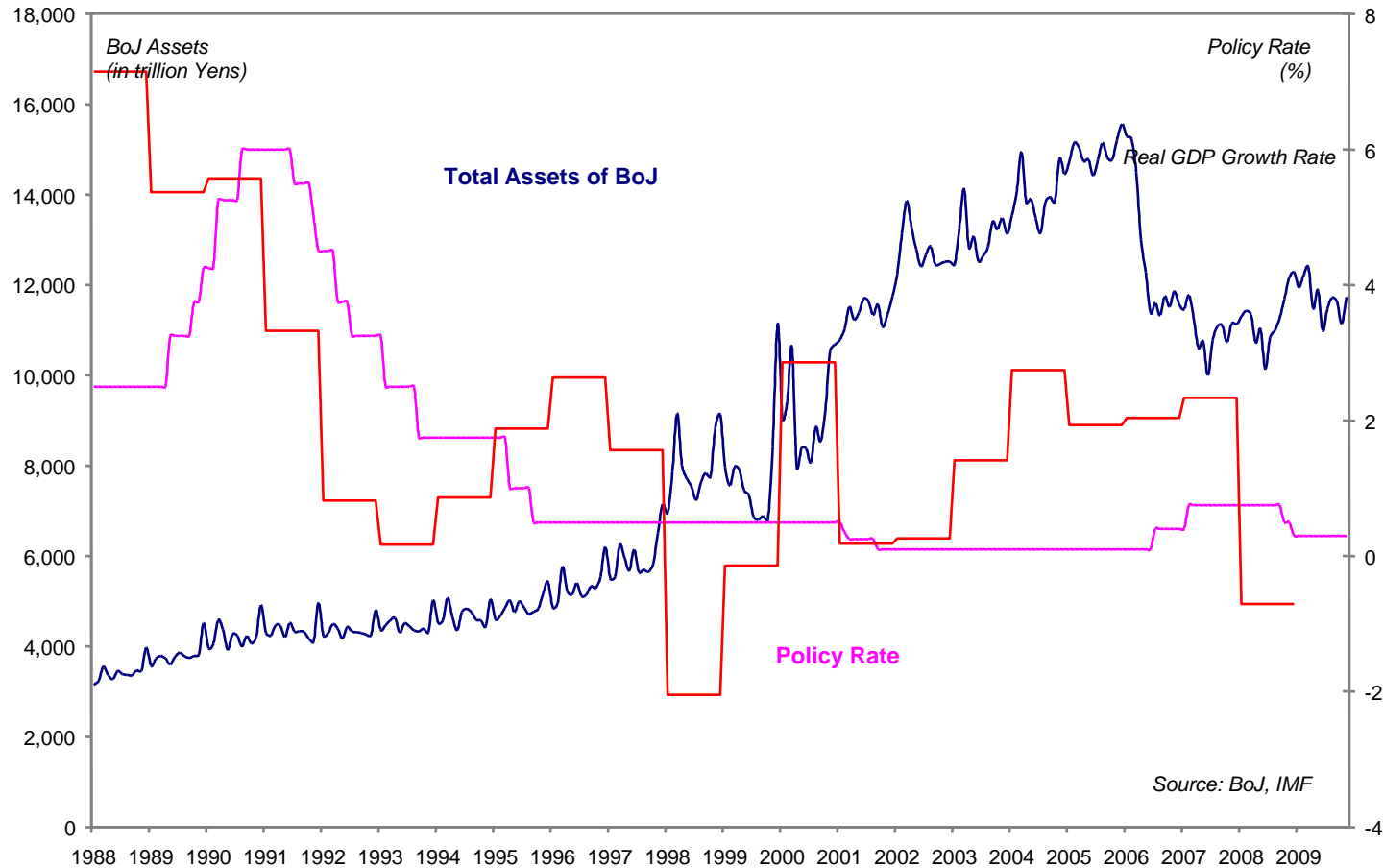


... but also in Europe and Japan

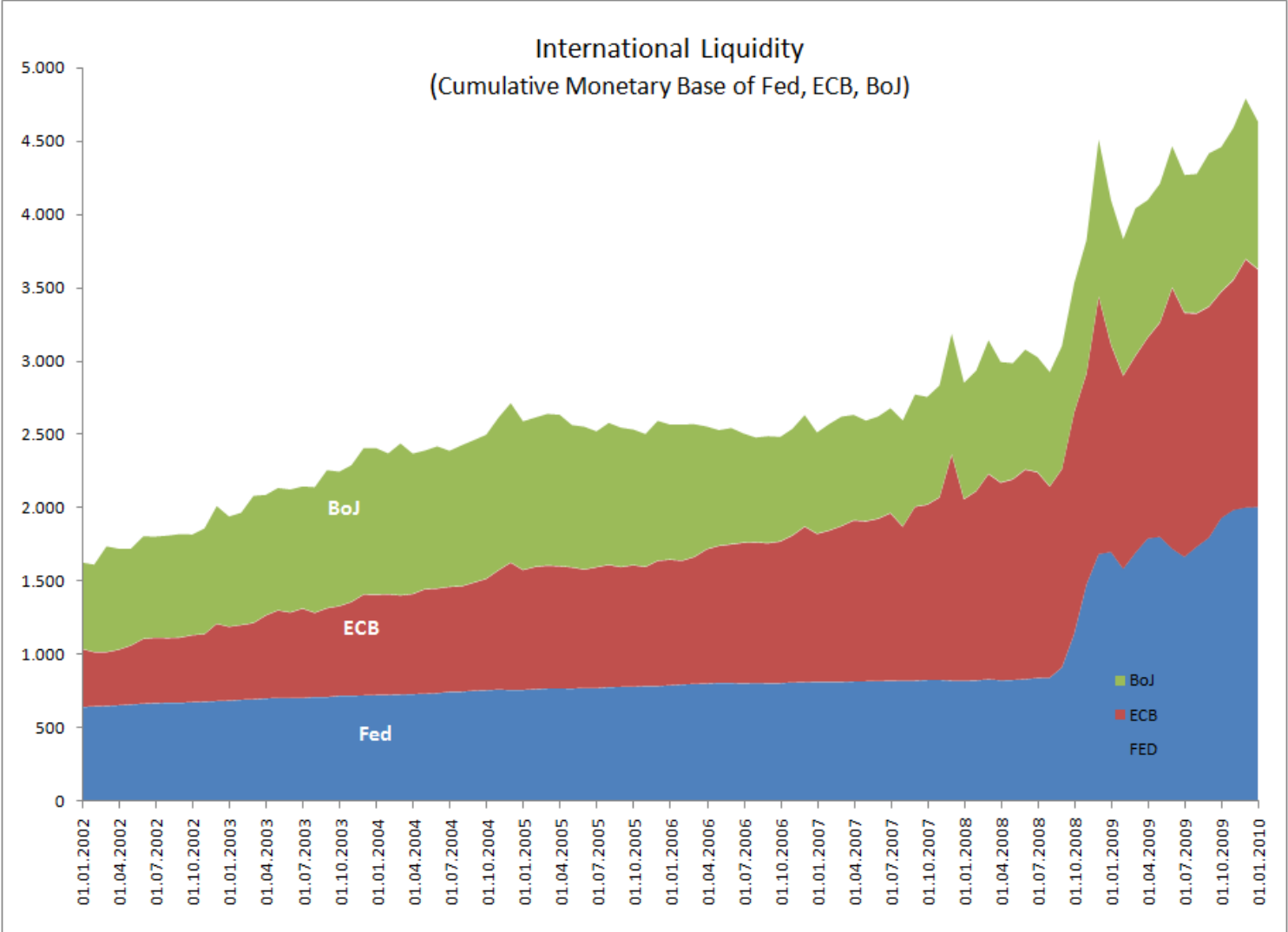


In fact, Japan's monetary expansion has been ongoing since end-1990s to stimulate growth

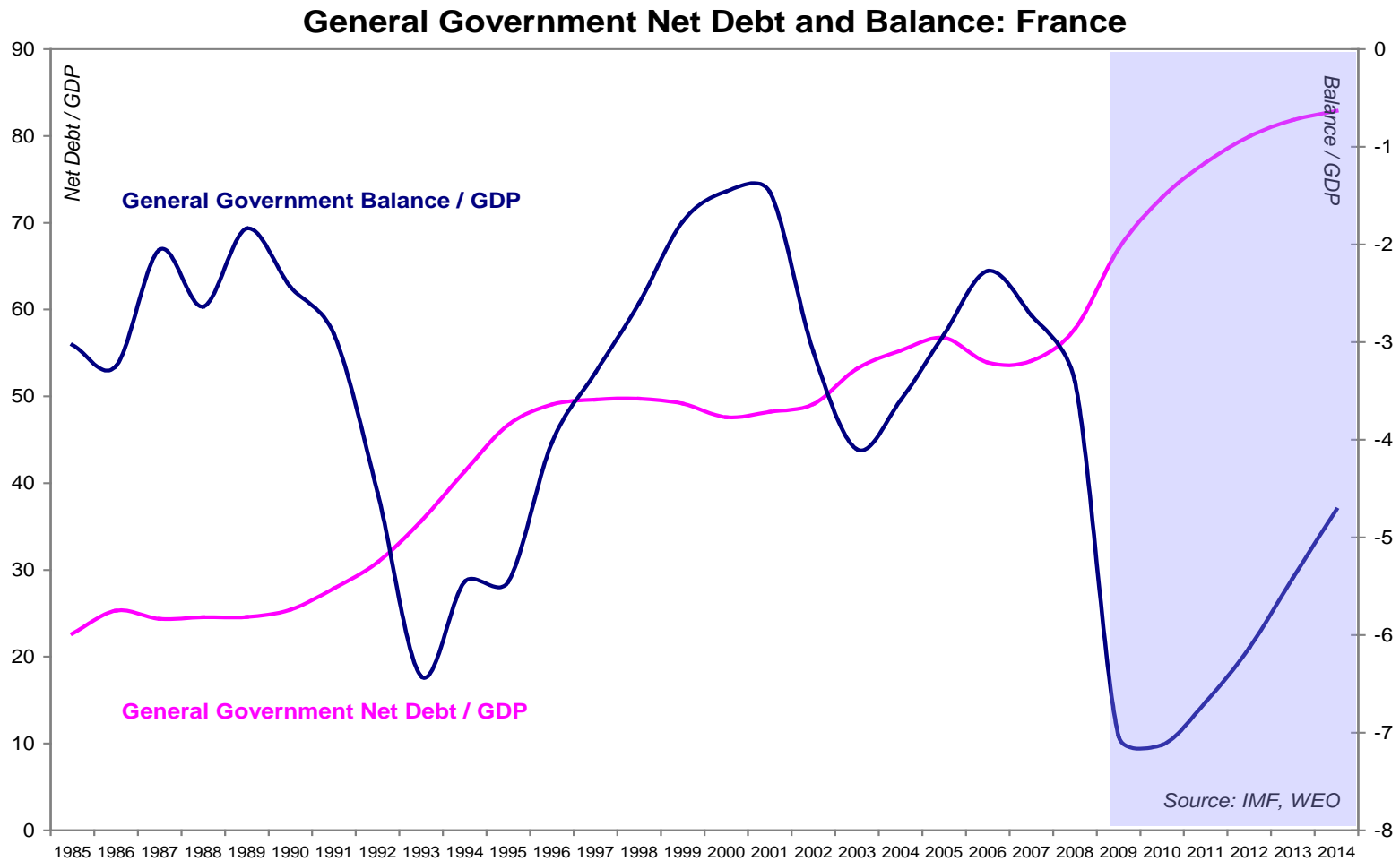
Japan Monetary Policy and GDP Growth



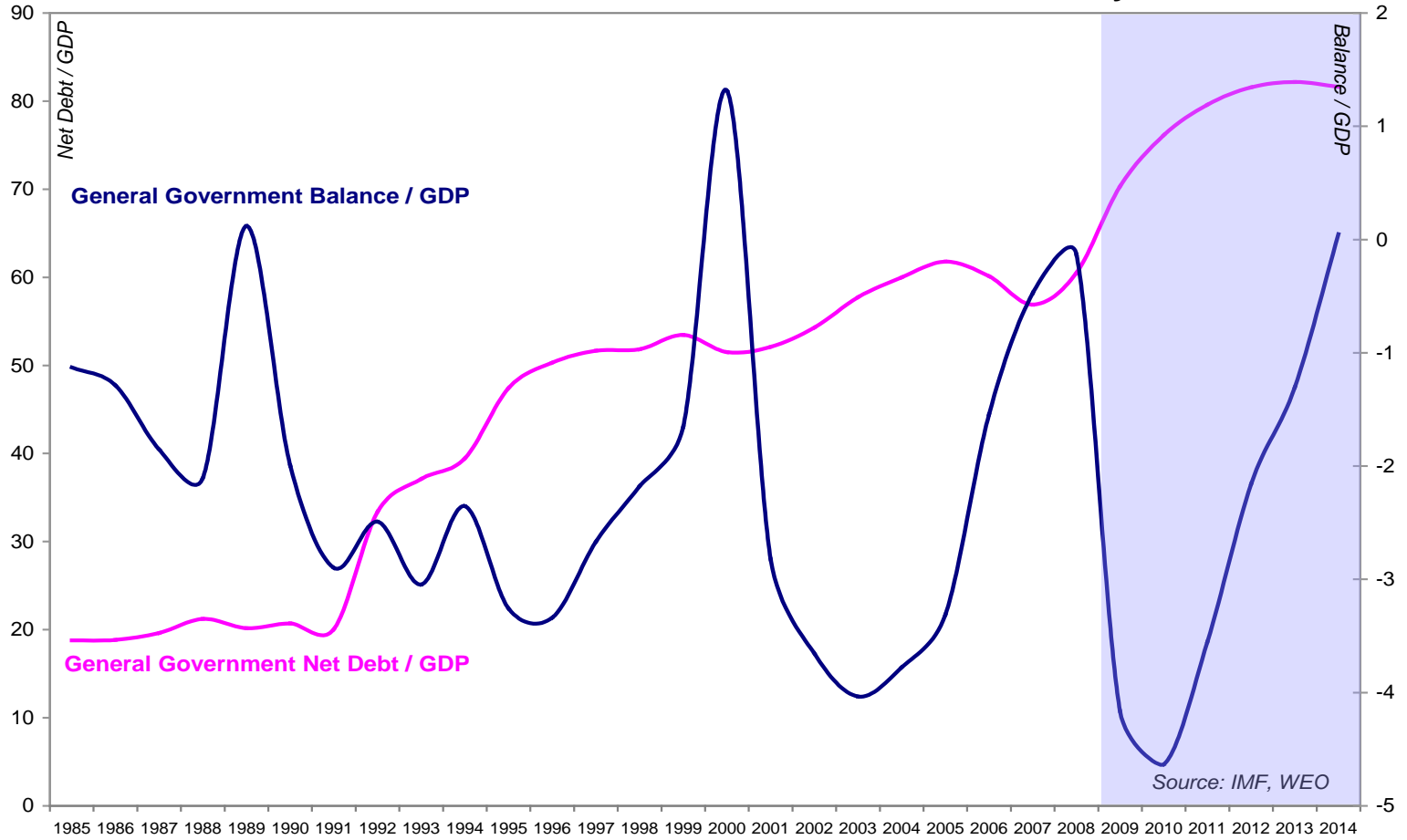
...doubling international liquidity in less than two years



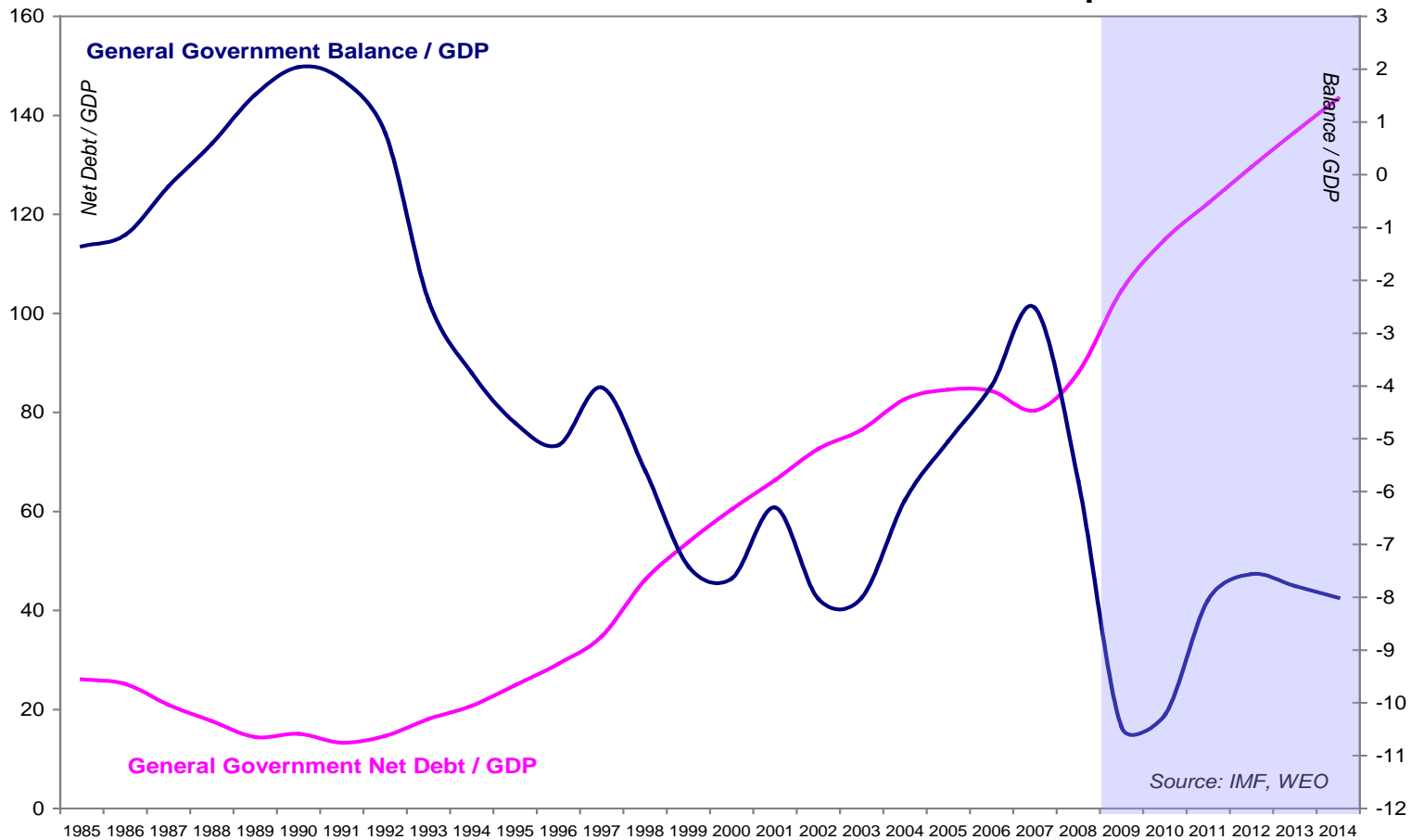
Fiscal stimulus in almost all major economies accompanied monetary expansion...



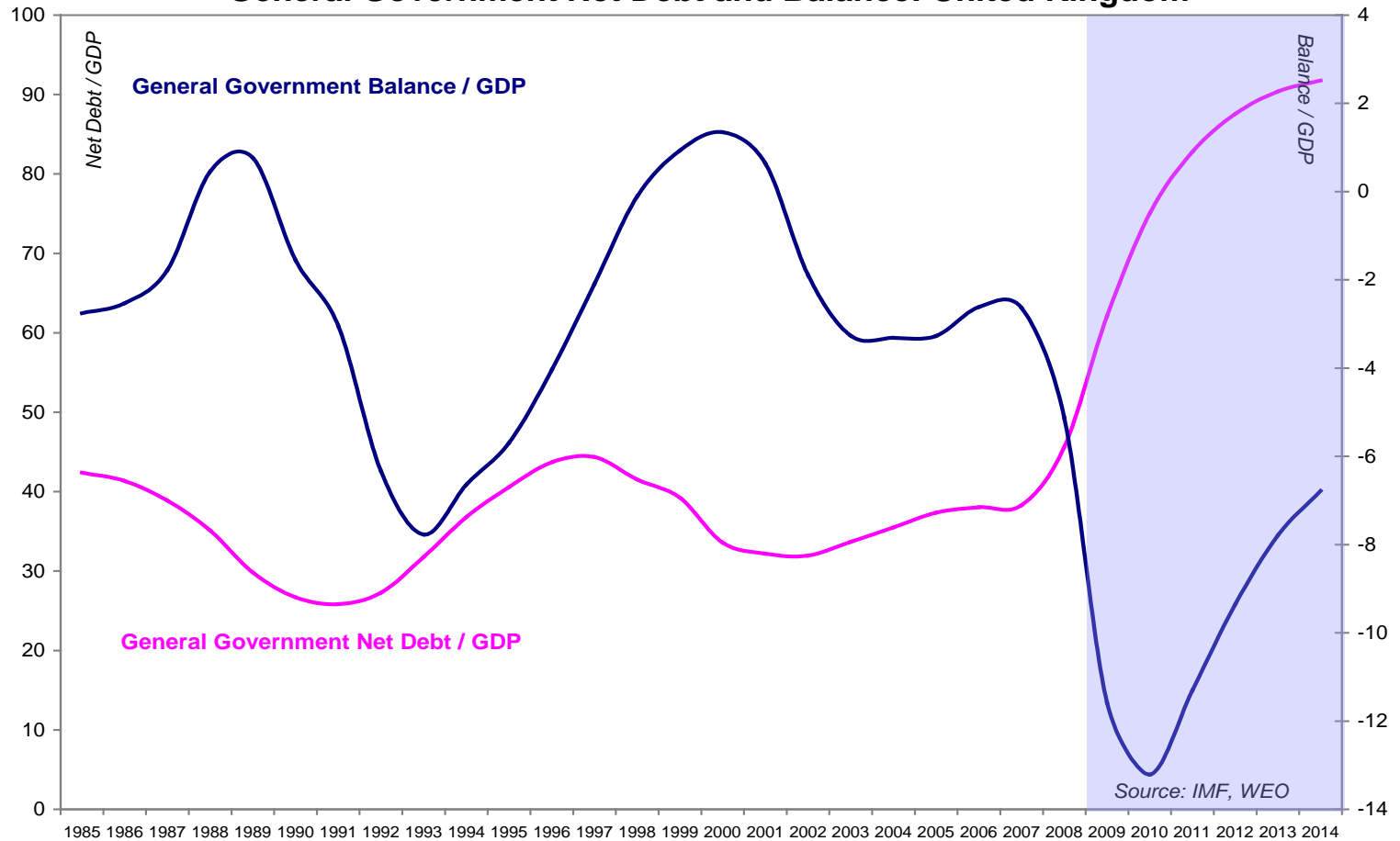
General Government Net Debt and Balance: Germany



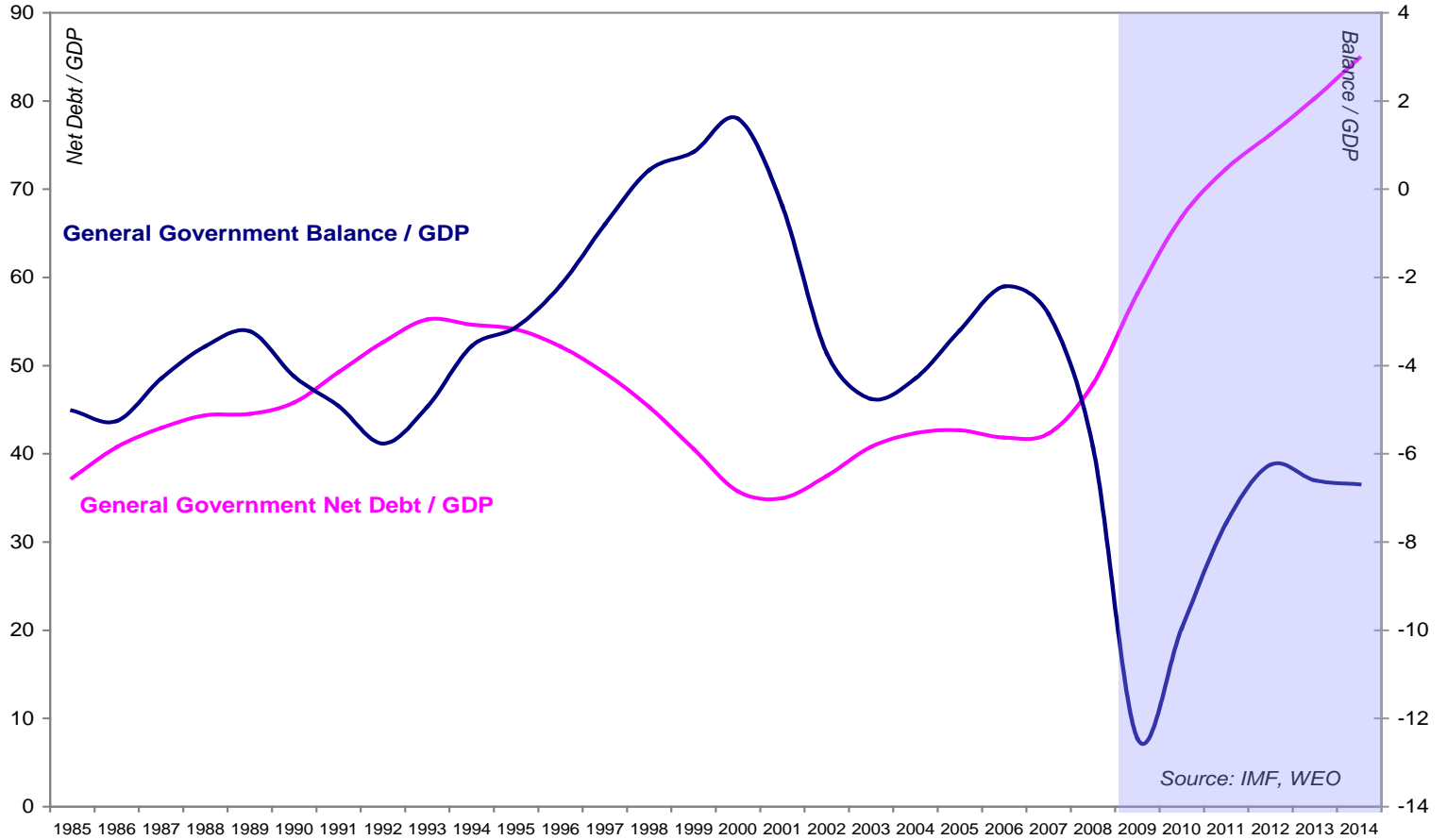
General Government Net Debt and Balance: Japan



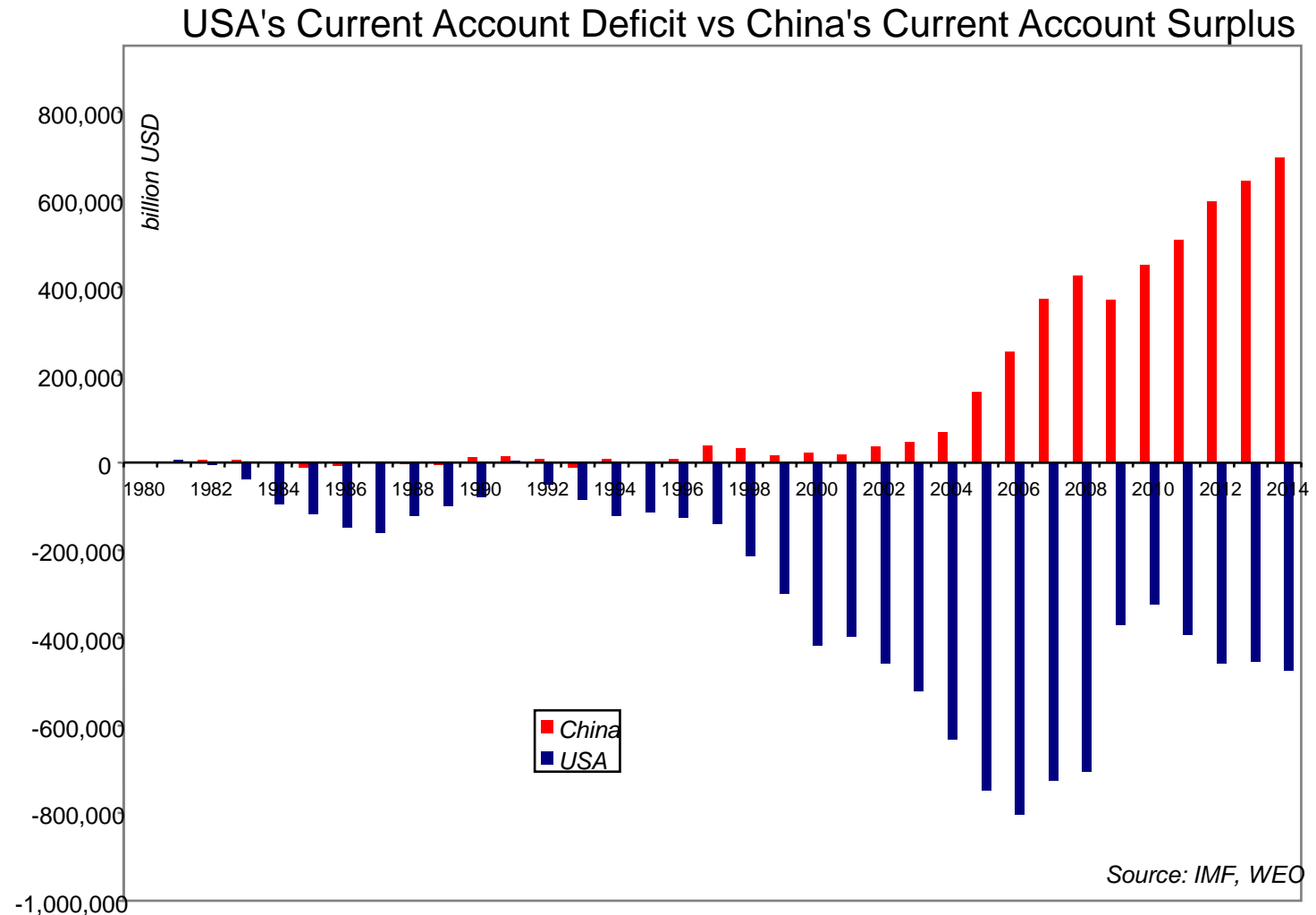
General Government Net Debt and Balance: United Kingdom



General Government Net Debt and Balance: USA

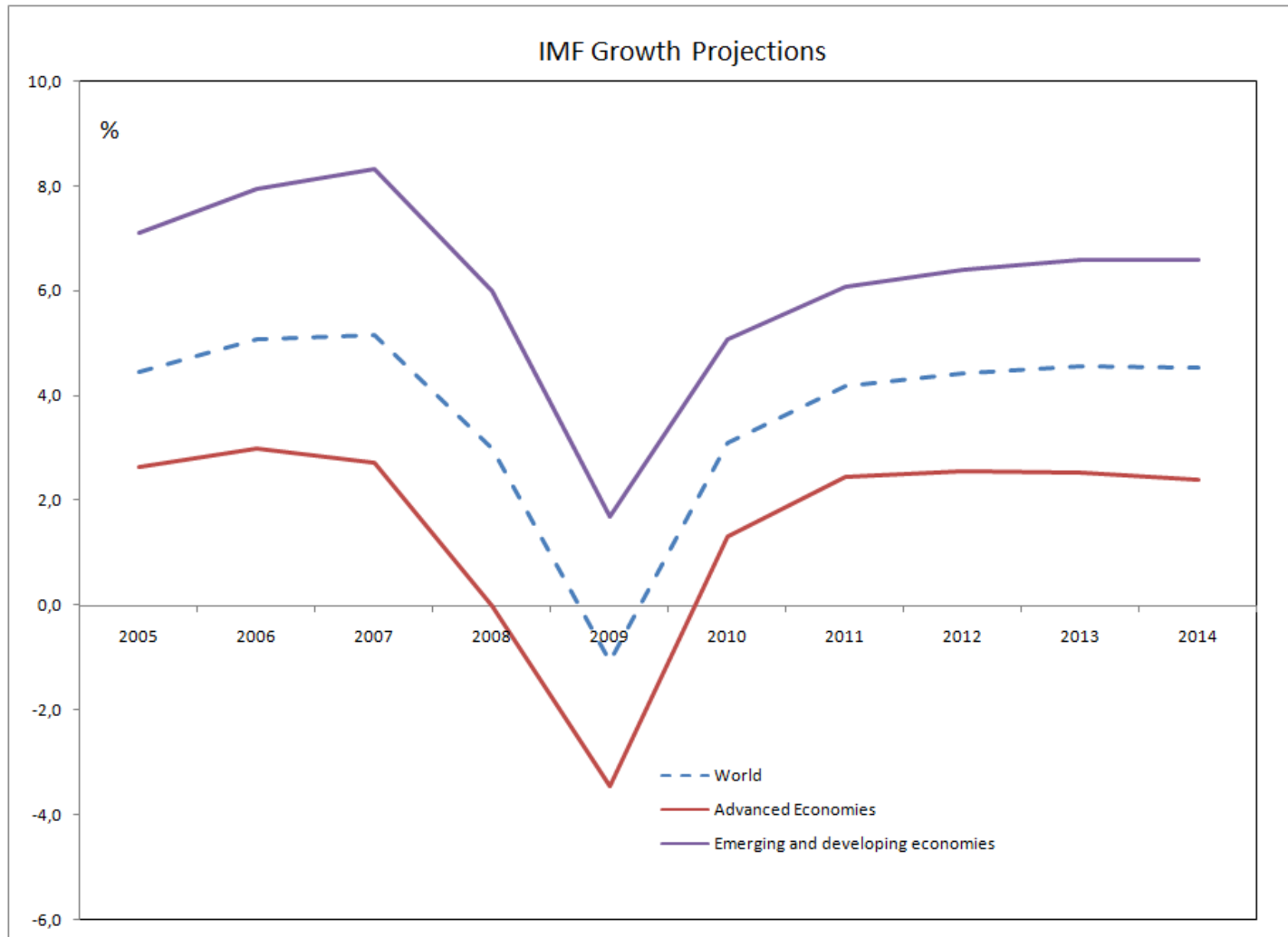


... and the infamous “Global Imbalances” have survived comfortably



A Likely Post-Crises Scenario: Major Trends

Growth: official projections of the IMF imply assumptions of recovery of growth back to somewhere close to the pre-crises levels by 2011 ...



IMF's (and some others') "back to the beginning" optimistic scenario hides a number of issues especially around households and states

- All balance sheets in the USA are quite weak simultaneously:
 - Households
 - Corporates
 - Banks
 - and the government!
 - Moreover, international economic pace is not helping the USA
- Long term structural problems in the USA, Japan and Europe are abundant:
 - Cost of crises
 - Cost of war, among others in Iraq and Afghanistan
 - Social security
 - Demographic burden
 - Institutional and governance issues

... and questions ...

- When will/can the “exit” from current monetary and fiscal policy actually start?
- How will that affect the already fragile growth?
- How will the everlasting “Global Imbalances” issue be resolved?

... as well as uncertainties...

- What if western governments can not afford to exit under growth pressures?
- Ramping up commodity prices (especially energy) and their inherent volatility?
- China's integration into the world economy that is pleasant for some (consumers) and painful for the others (local industries that can not adopt)

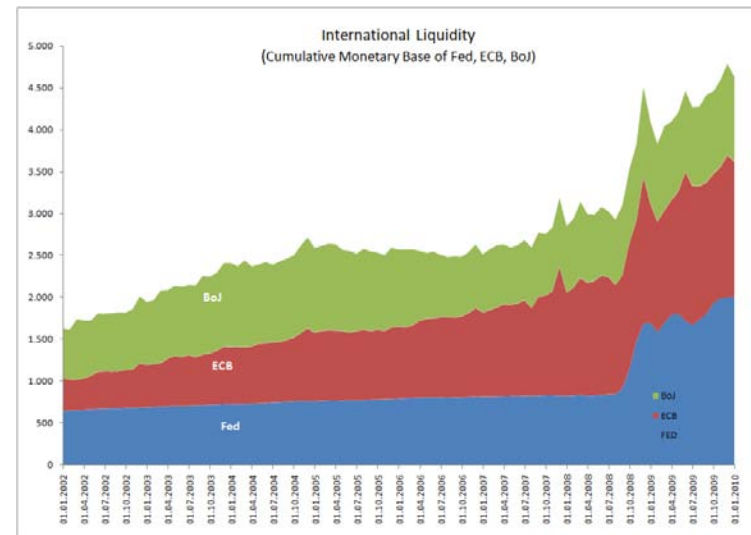
Our working assumption, on the other hand is weak and fragile growth

- *a weak and fragile global growth;*
- *mostly to stem from weaker developed economies dotted with structural, demographic and fiscal problems...*
- *while many developing countries with solid policies may have the opportunity to continue “decoupling”*
- *with China maintaining its rapid growth rates...*
- *threatening the survival of the traditional industries which can not adopt in developing as well as developed economies ..*

Major trends in the international macroeconomic environment in the next five years: Liquidity

- From one to “triple” cash fountains: No strong exit from monetary expansion

Abundant liquidity will survive with growing carry trade possibilities under fragile growth prospects



Major trends in the international macroeconomic environment in the next five years: Investment Flows

- Along with liquidity, we will likely witness increasing international investment, especially towards developing countries

Developing countries' share in total international investment has been on the up. That trend is likely to continue both because of return differentials and better performance of the emerging and developing countries in general. Moreover, developing countries that are resource rich or large exporters such as Saudi Arabia and China will become major investors globally.

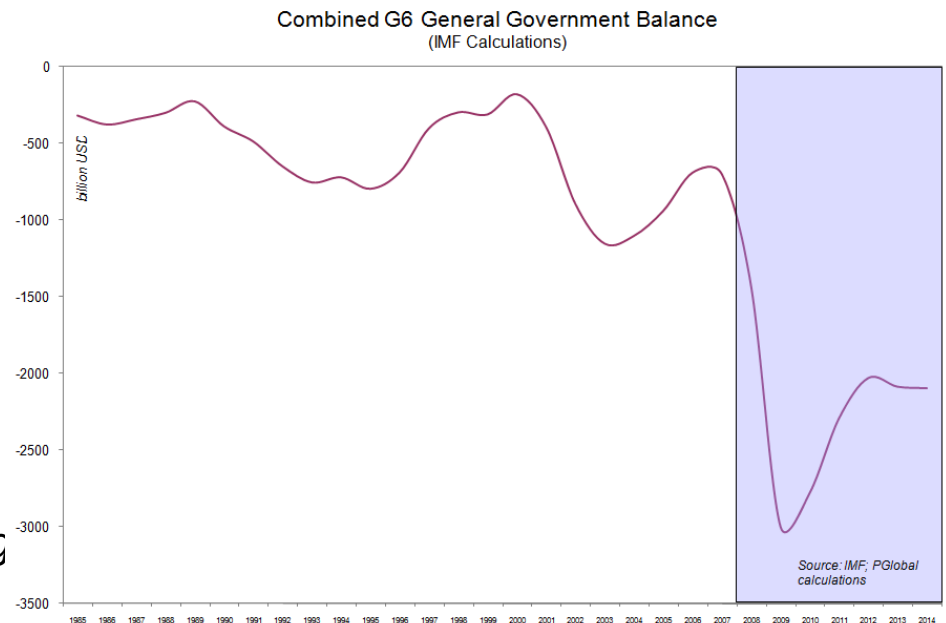
The IIF estimates that investment flows (equity and debt) to emerging and developing countries fell to USD 435 billion in 2009 from USD 667 billion in 2008. Based on the recovery in the second half of 2009, the same institution projects the inflows to recover to USD 721 billion in 2010 and USD 797 billion in 2011.

We believe the outturn can be significantly higher than IIF's expectations.

Major trends in the international macroeconomic environment in the next five years: Fiscal Consolidation

- Fiscal consolidation effort in large economies will mostly mean budgetary tightening but pressure on the borrowing markets is likely to be maintained

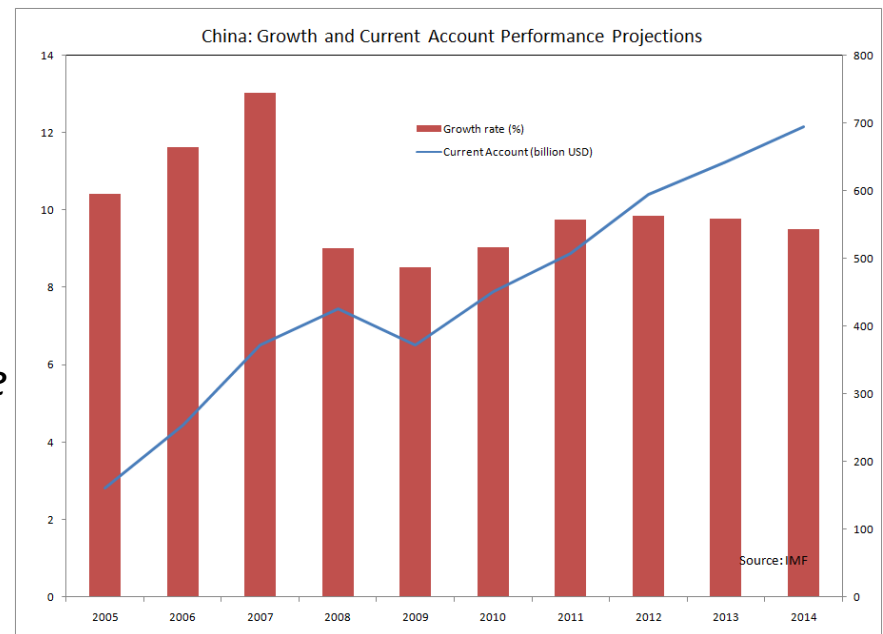
Structural and political issues, as well as fragile growth prospects will make it very difficult for large western economies to enforce fiscal consolidation. That means they will have to continue tapping capital markets.



Major trends in the international macroeconomic environment in the next five years: China and Commodities

- China is likely to continue ascending ...

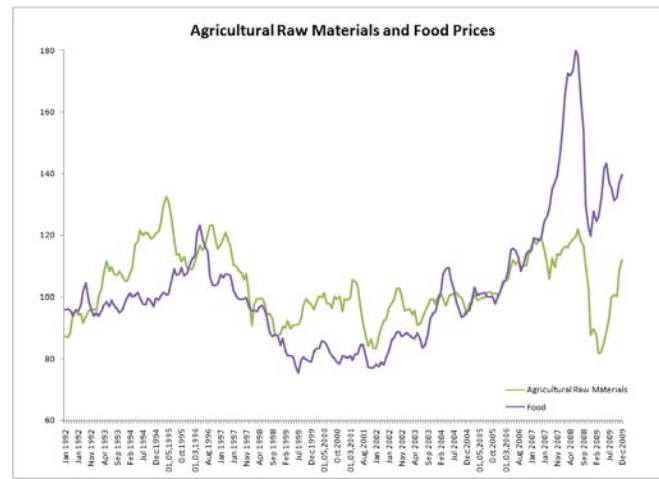
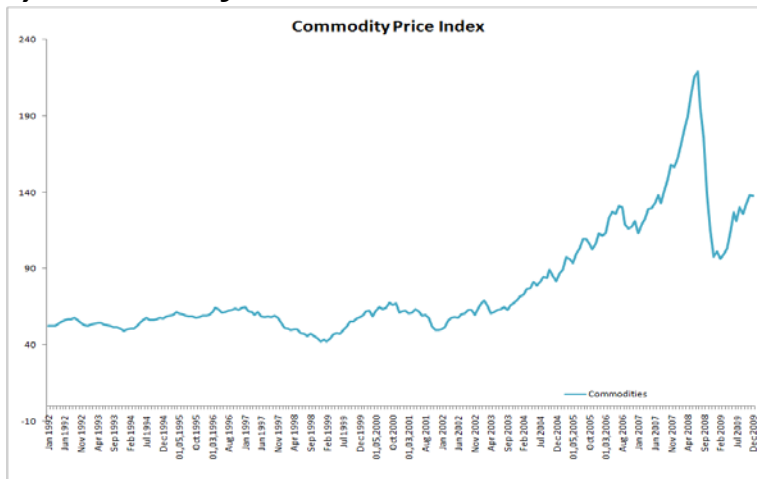
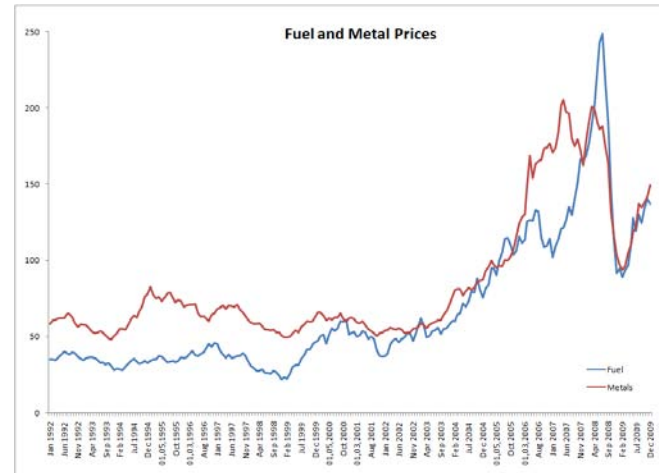
China's growth will be enforced with its position as provider of low cost merchandise in the light of weak consumer income and confidence. That is a tough call for competing businesses in other countries and China's market share is likely to increase accompanied by rising commodity prices pushed by demand from China



Major trends in the international macroeconomic environment in the next five years: China and Commodities

- ... accompanied by rising commodity prices which trended upwards following the initial collapse

China's market share is likely to increase, in spite of weak overall consumption accompanied by rising commodity prices pushed by demand from China.



Major trends in the international macroeconomic environment in the next five years: Volatility & Uncertainty

- Heading towards a volatile world economy dotted with many uncertainties and rising commodity prices

Euro/USD parity, gold prices, ballooning (again) stock exchanges, commodities, all facilitated by the likely maintenance of easy liquidity will make the global economy a very risky place



Major trends in the international macroeconomic environment in the next five years: “Decoupling”

- “Decoupling” in favor of developing countries may continue

Developing economies have performed Better during the crises. That may continue into the medium run. A number of western and eastern European countries collapsed during the crises European economies with substandart governance quality; e.g. Greece, show that those “developed” economies may have unexpected performance revealed at times.

European Commission’s Recent Report on Greece (EUROPEAN COMMISSION (Brussels, 8.1.2010 COM(2010) 1 final **REPORT ON GREEK GOVERNMENT DEFICIT AND DEBT STATISTICS**)

“The reliability of Greek government deficit and debt statistics has been the subject of continuous and unique attention for several years. In 2004, Eurostat produced a comprehensive report on the revision of the Greek government deficit and debt figures, showing how the Greek statistical authorities had misreported figures on deficit and debt in the years between 1997 and 2003.”

“The most recent revisions are an illustration of the lack of quality of the Greek fiscal statistics (and of Greek macroeconomic statistics in general) and show that the progress in the compilation of fiscal statistics in the country, and the intense scrutiny by Eurostat since 2004, have not sufficed to bring the quality of Greek fiscal data to the level reached by other EU Member States.”