

The Global Economic Recovery What to Expect in Year 2 (and Beyond)

Philip Suttle
Chief Economist, IIF

Garanti Masters,
Istanbul

October 15, 2010

Three Basic Questions

- How will the global business cycle unfold over the next 24 months?
- Should you be more worried about deflation than inflation?
- What are the financial market implications of this outlook?

How Will the Global Business Cycle Unfold over the Next 24 Months?

A Double Dip in the Making?

Global Industrial Production

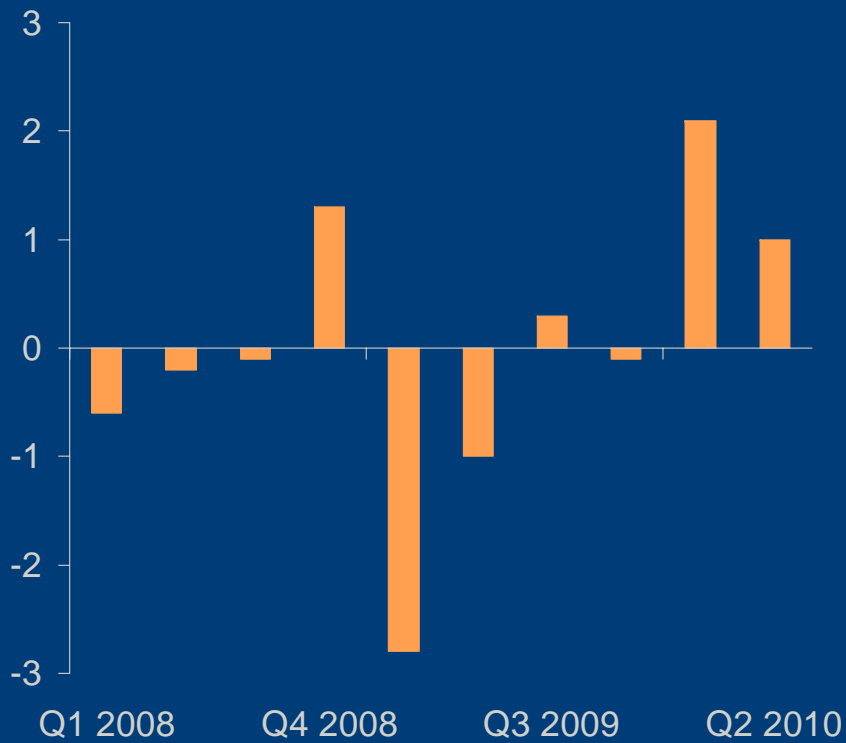
Percent, 3m/3m saar



Slowing Should Have Been Expected

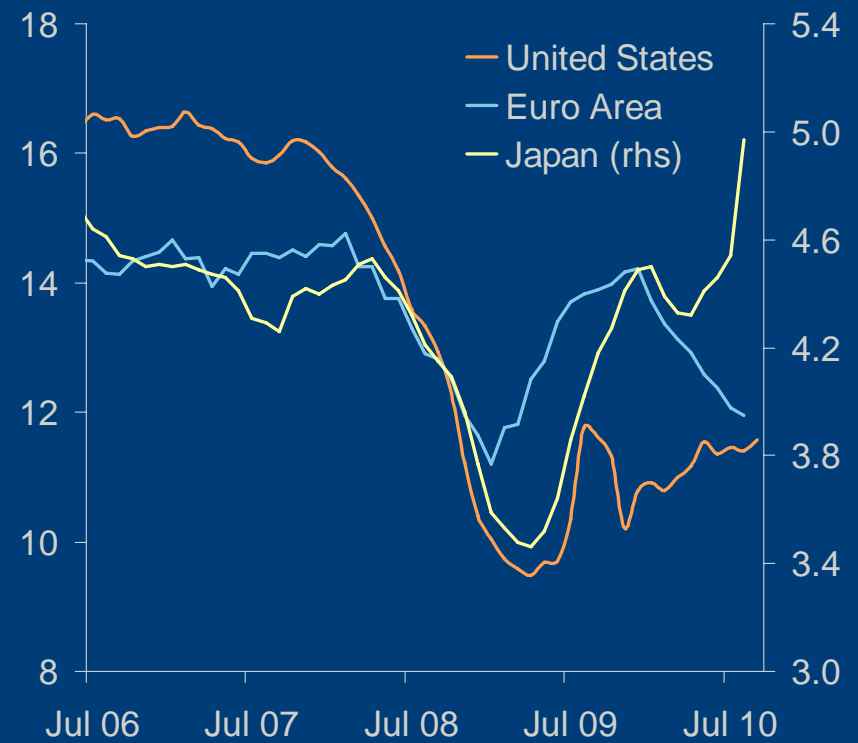
G3 Inventory Contribution to Growth

Percentage points, q/q saar, weighted average



G3 Auto Sales

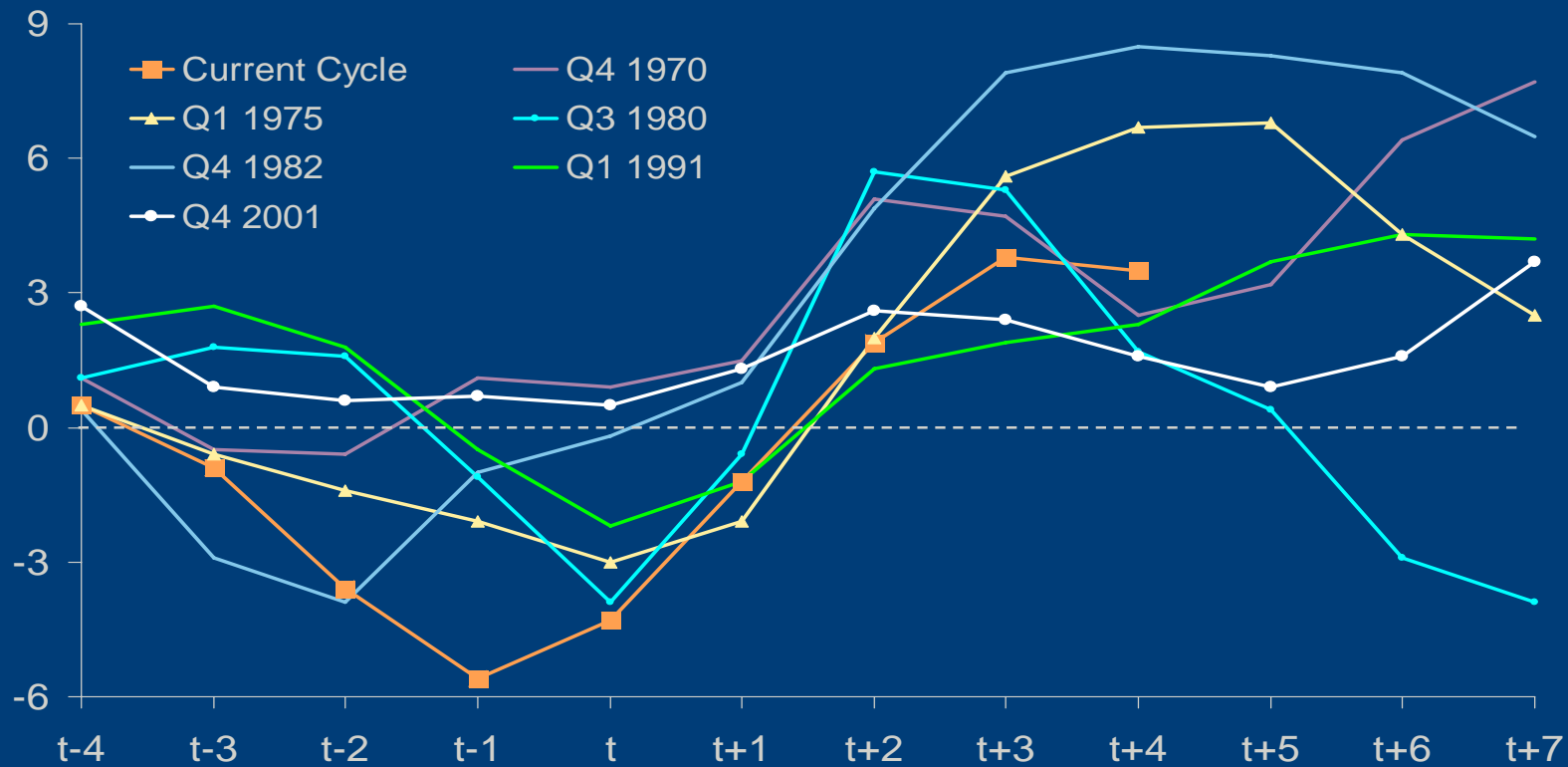
Million units, saar, 3-month MA (both scales)



The “Old Normal”

United States: Cyclical Recoveries

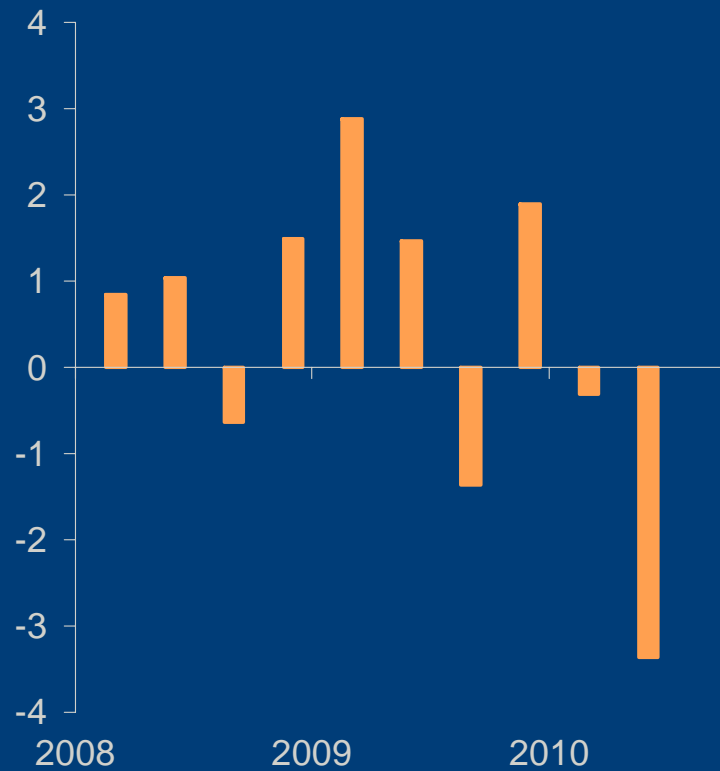
2q/2q percent change, saar, t = NBER end-date of recession



The Near Term

U.S. Upside?

Net trade contribution to growth, percentage points, q/q saar



Euro Area Downside?

Yield to maturity of 10-year government bonds



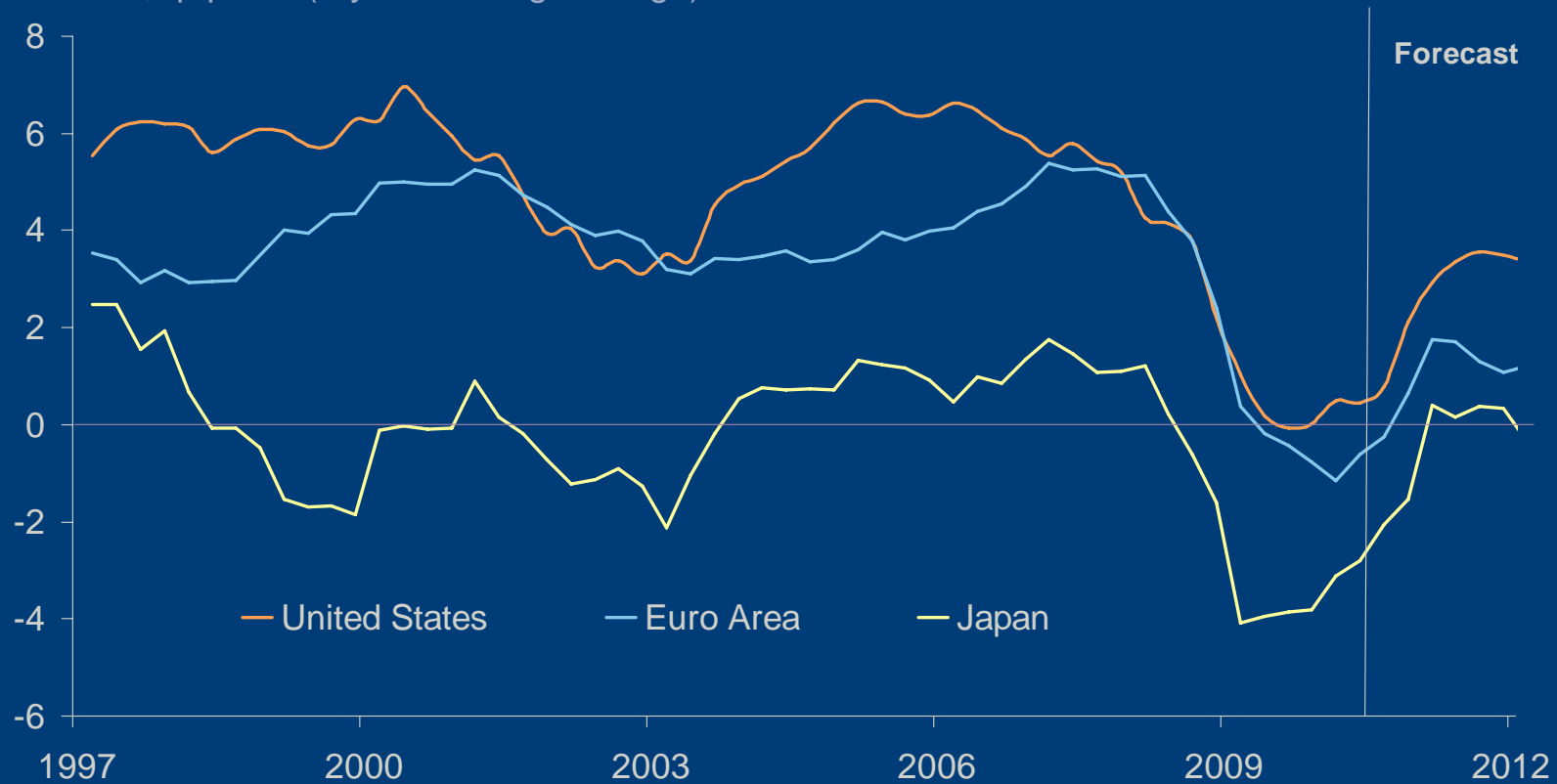
Global Output Growth Forecasts

Percent y/y	2005-07 average	2008	2009	2010	2011	2012
Global	<u>3.6</u>	<u>1.2</u>	<u>-2.5</u>	<u>3.4</u>	<u>2.7</u>	..
Mature Economies	<u>2.5</u>	<u>-0.1</u>	<u>-3.6</u>	<u>2.4</u>	<u>1.7</u>	<u>2.2</u>
United States	2.6	0.0	-2.6	2.8	2.3	2.9
Euro Area	2.6	0.3	-4.0	1.7	1.4	1.6
Japan	2.1	-1.2	-5.2	3.0	1.0	1.6
Emerging Markets (IIF 30)	<u>7.3</u>	<u>5.6</u>	<u>1.4</u>	<u>6.8</u>	<u>6.2</u>	..
Latin America (8)	5.1	4.1	-2.3	5.7	4.3	..
Emerging Europe (8)	6.5	4.0	-5.7	4.0	3.1	..
Turkey	6.7	0.7	-4.7	8.5	5.0	..
Emerging Asia (7)	9.1	7.3	6.6	8.9	8.3	..
Africa/Middle East (7)	5.3	5.1	1.0	3.7	4.3	..

Weak Income Growth

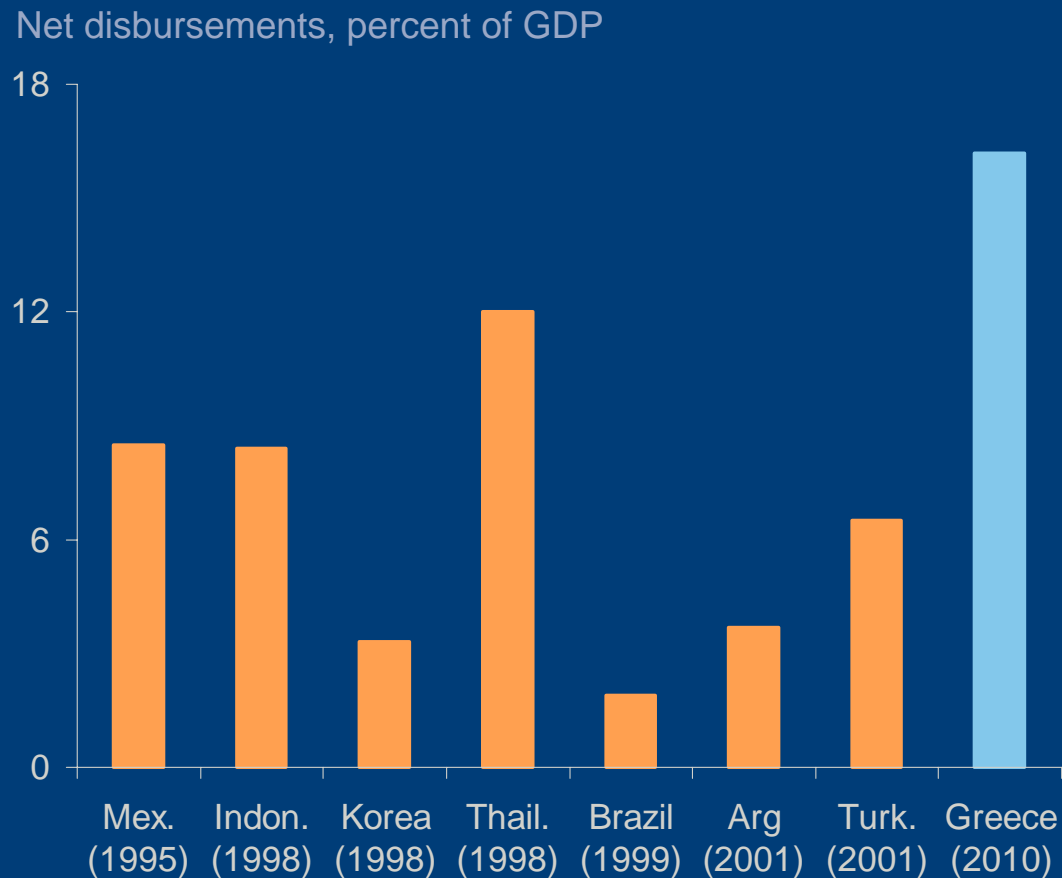
G3: Nominal GDP Growth

Percent, q/q saar (2-year moving average)

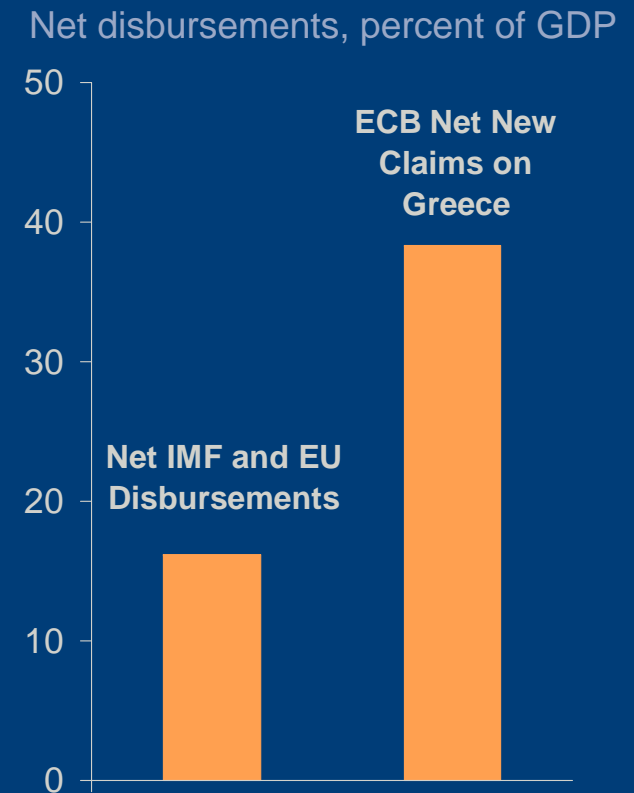


Massive Support for Greece... Ireland Next?

Net Official Support for Countries with Financing Difficulties

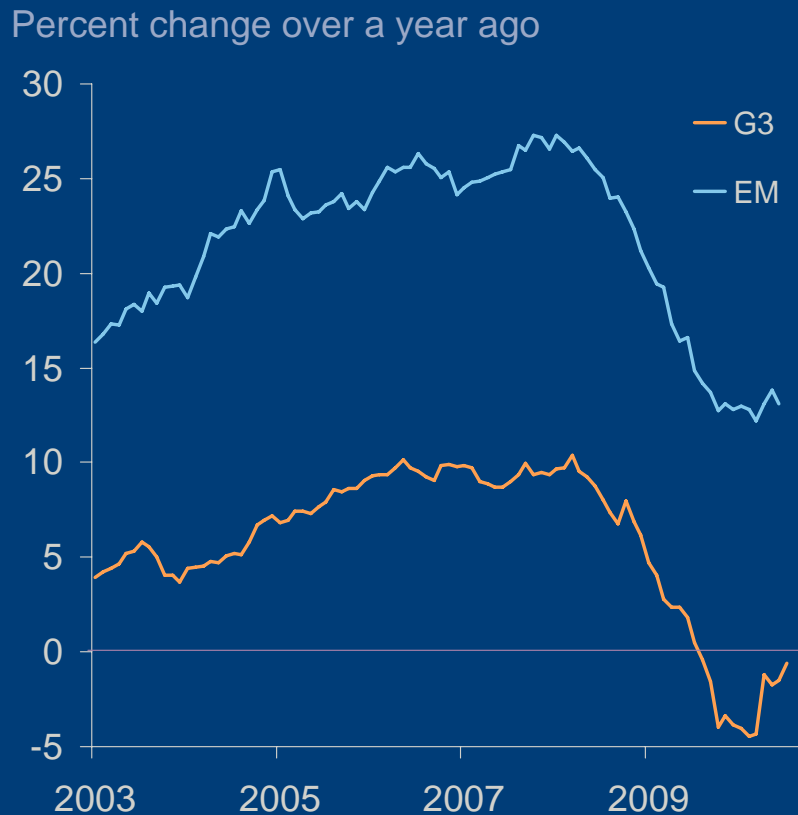


Net External Financing for Greece, 2010

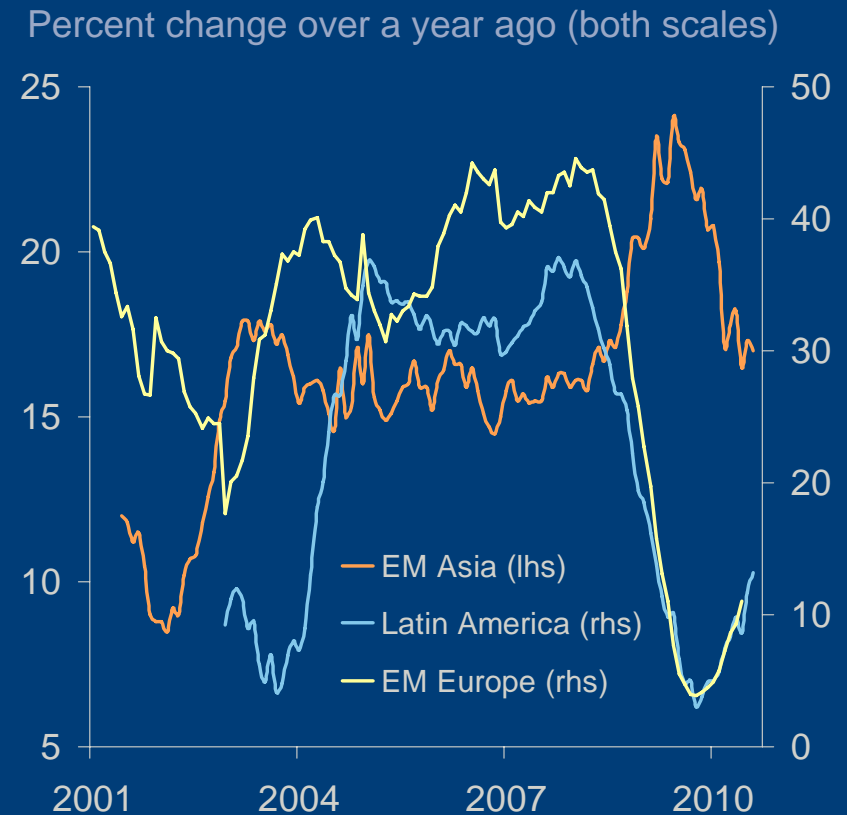


Strong Credit Growth in Emerging Economies

EM vs. Mature Market Credit Growth

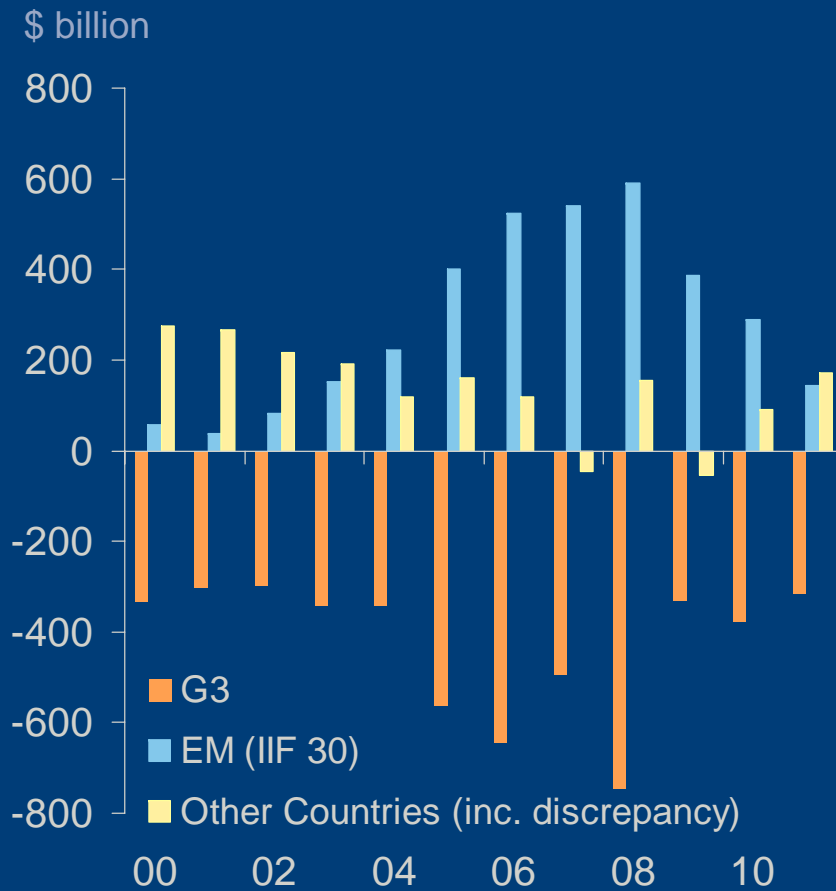


EM Credit Growth by Region

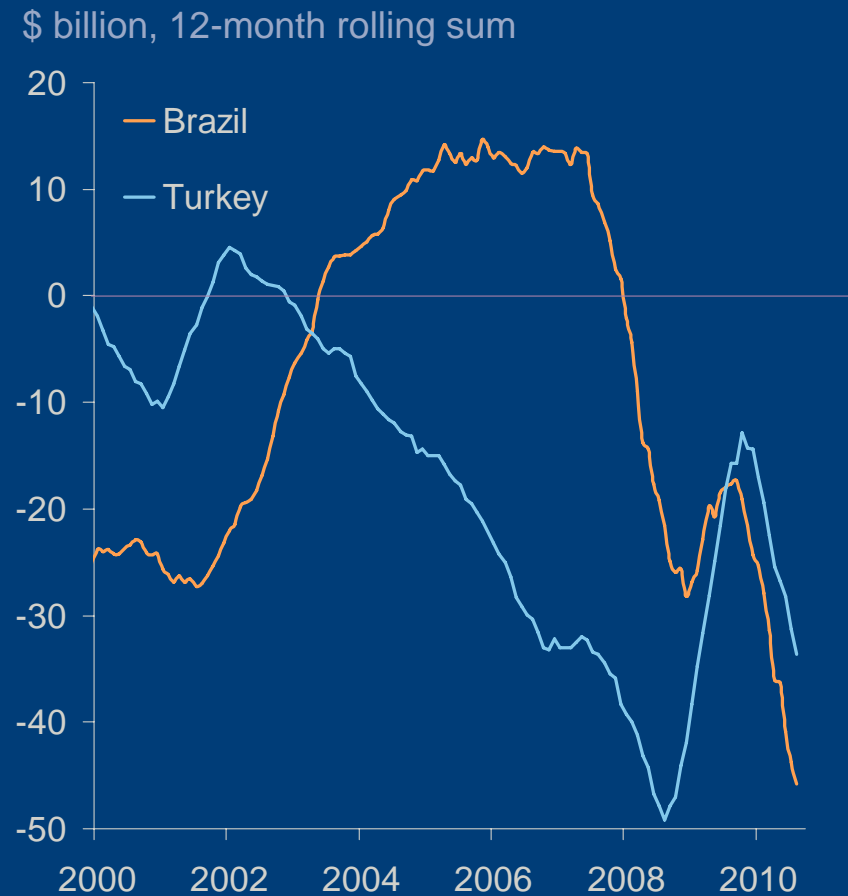


Current Account Shifts Ahead

Global Current Account Imbalances



Current Account Balances

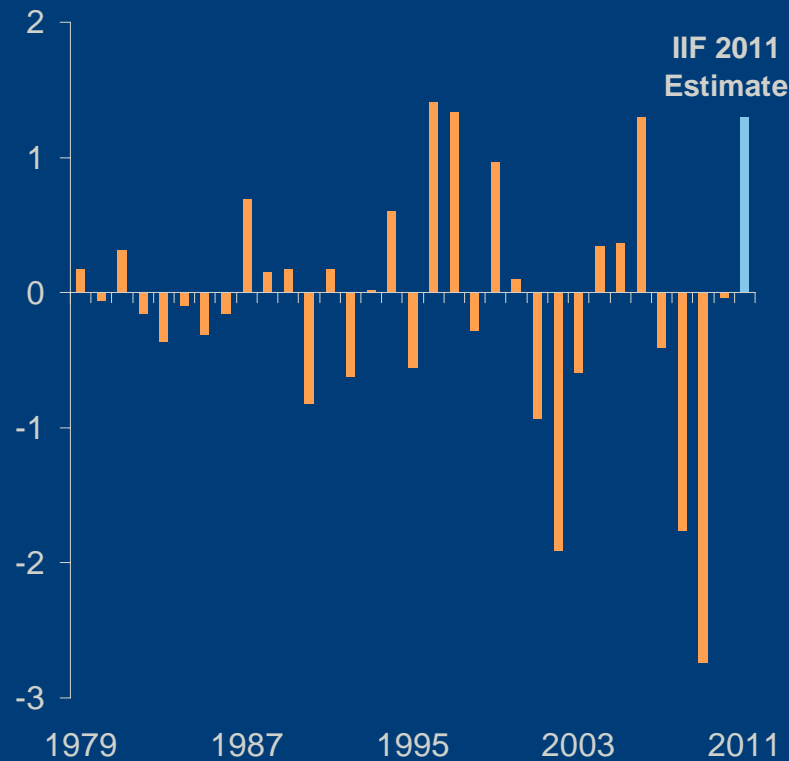


Should You Be More Worried about Deflation than Inflation?

The Policy Response

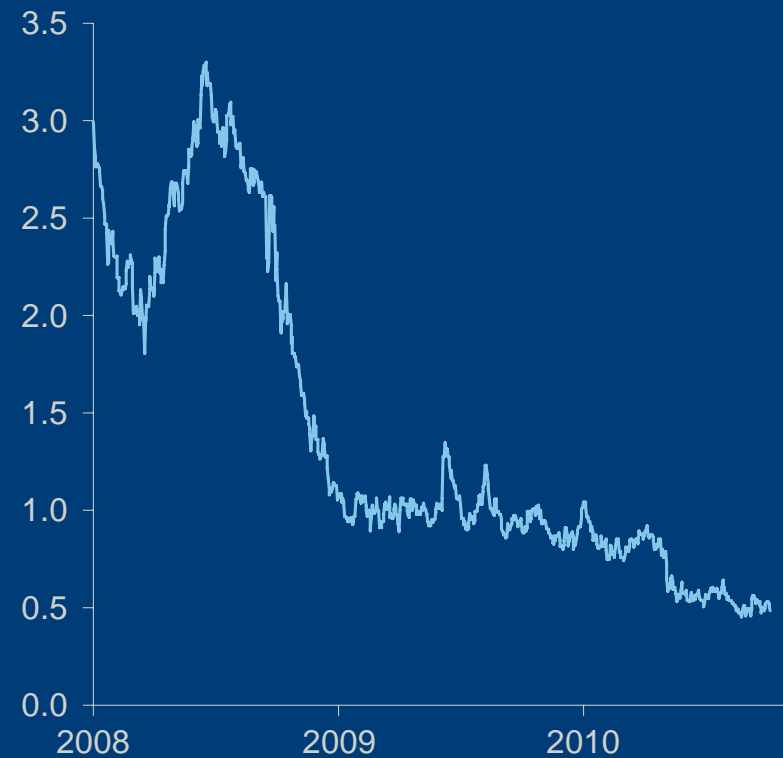
G7: Changes in Cyclically-Adjusted Fiscal Balance

Annual change in percent of potential GDP, OECD



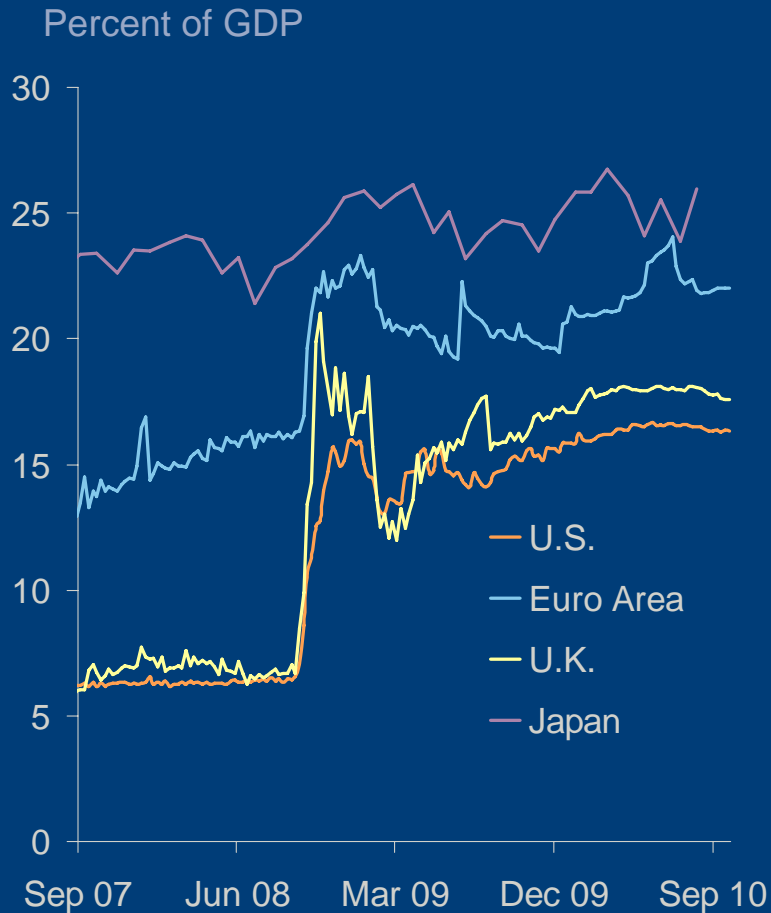
G3 Sovereign Bond Yields

Percent per annum, 2-year notes

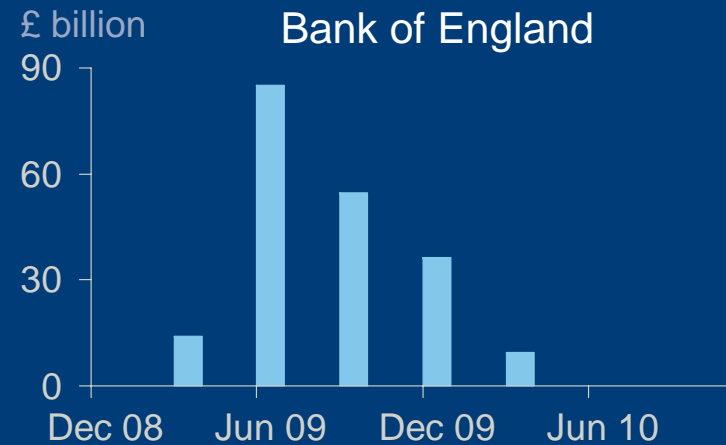
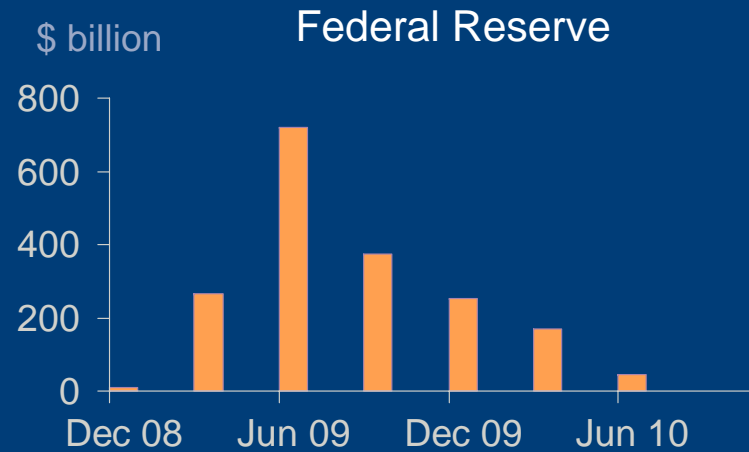


Four-Syllable Monetary Easing

Central Bank Balance Sheets:
Total Assets



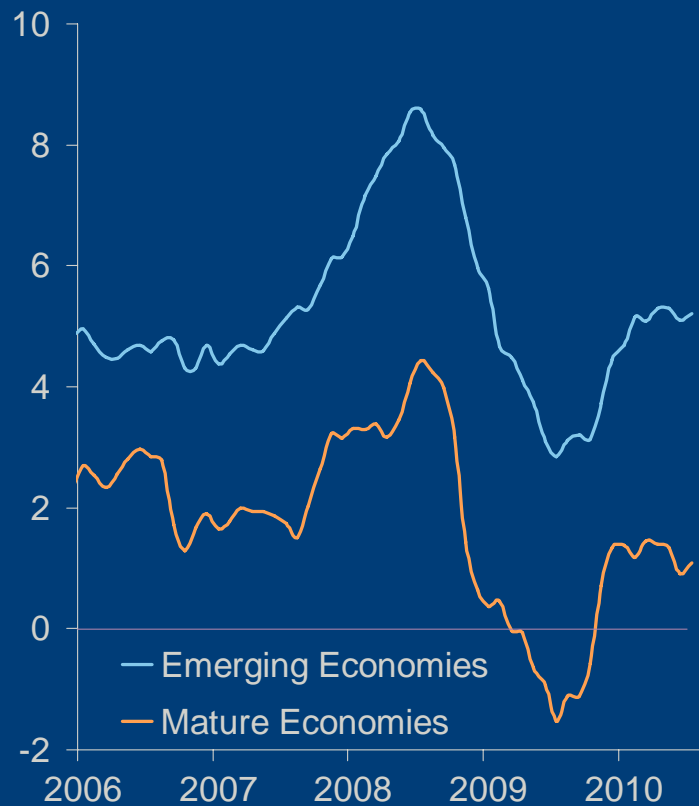
Central Bank Asset Purchases



Inflation or Deflation Risk? –Depends Where You Sit

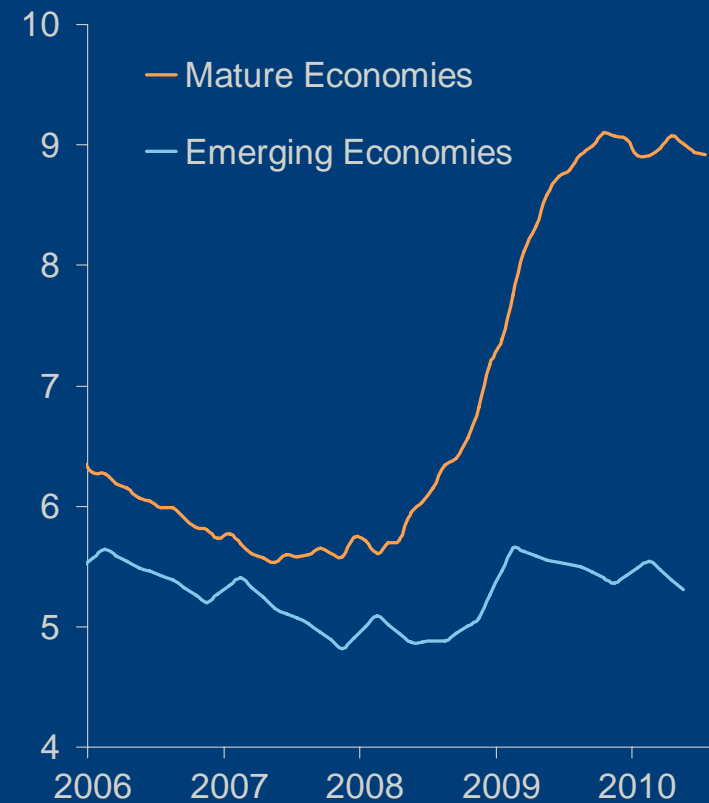
Consumer Prices

Percent change over a year ago



Unemployment Rates

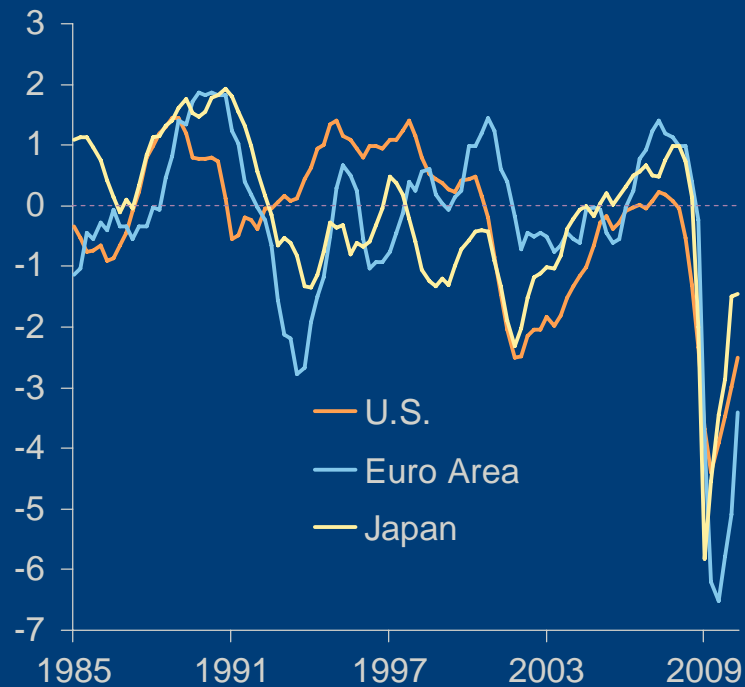
Percent of labor force



How Valid is the Slack Model?

G3: Manufacturing Capacity Utilization

Number of standard deviations from 1985-2007 average



U.S. Beveridge Curve (Stylized and 2001-2010)

Job openings, million



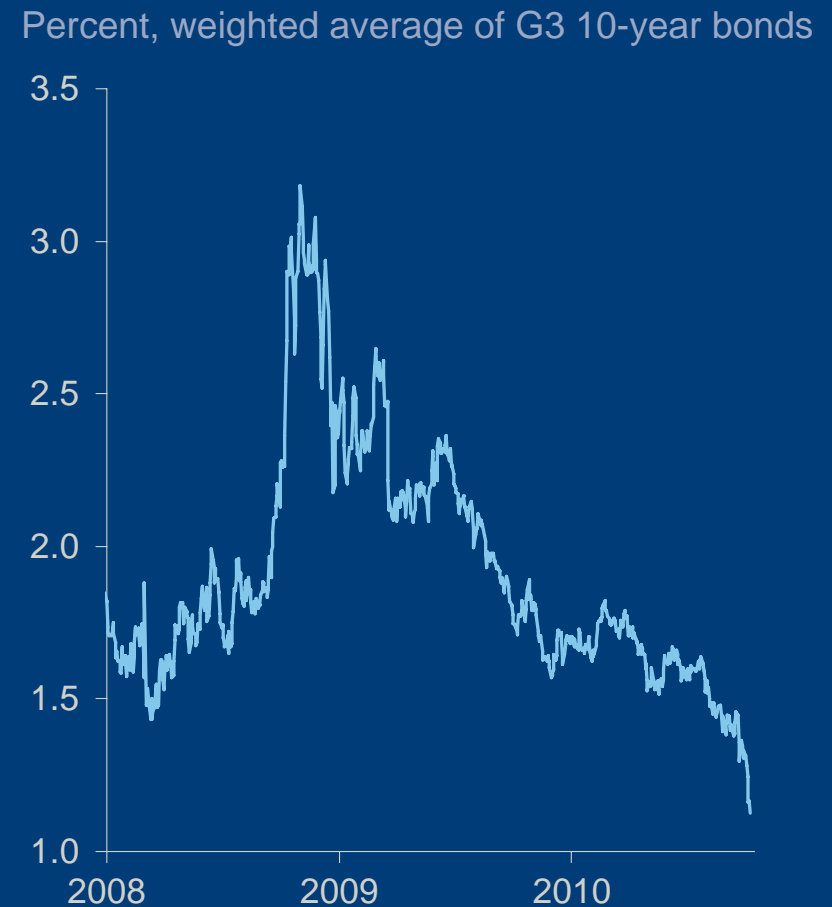
What Are the Financial Market Implications of this Outlook?

The Price of Inflation Insurance is on the Rise

Gold Price

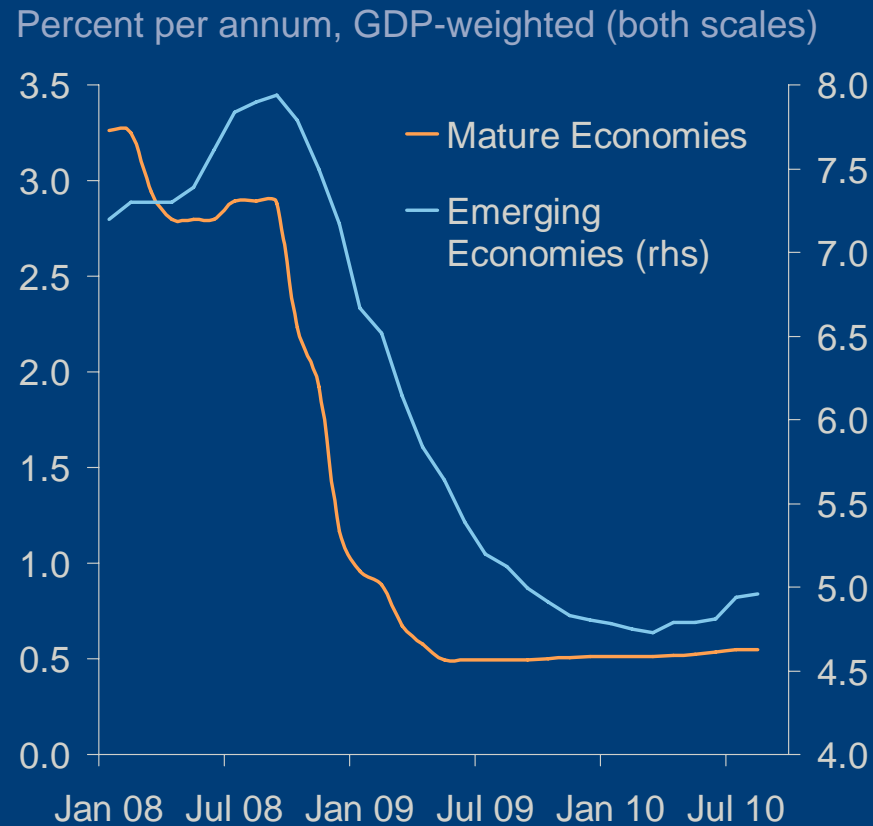


G3 Real Yields

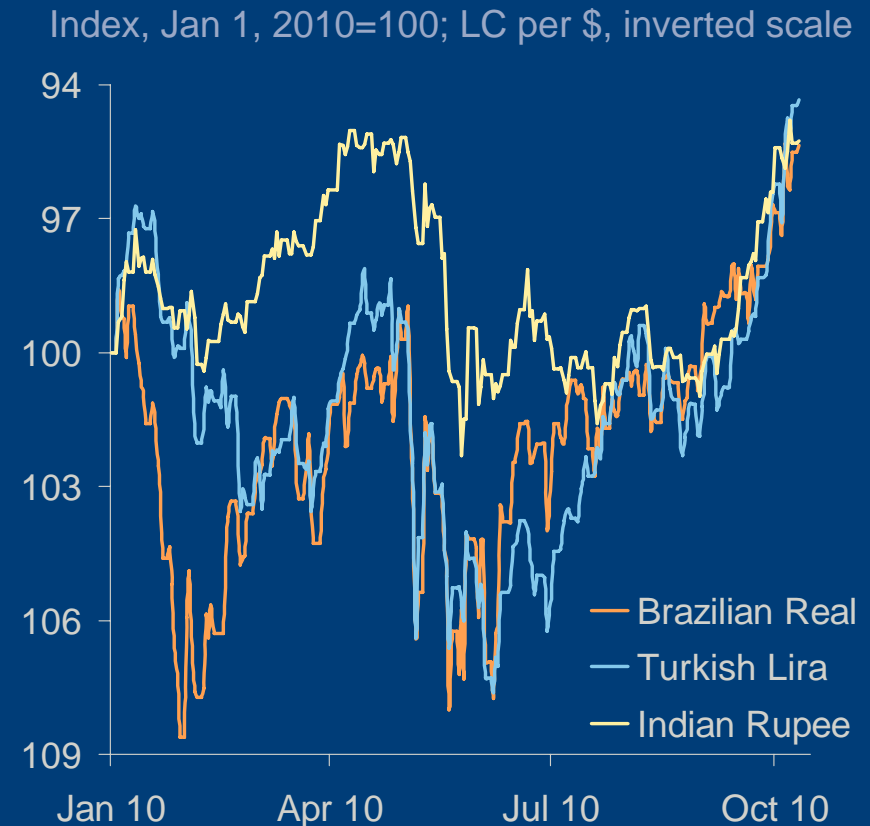


Easy Money Globally... Upward Pressure on EM Asset Prices

Trends in Official Interest Rates



Emerging Economies: FX Rates



Key Financial Market Implications of the Outlook

- Low rates in G3, downward pressure on high-grade spreads
- Continued upward pressure on equities, especially in EM
- More commodity price inflation, especially where supply is inelastic
- Upward pressure on EM FX: currency skirmishes
- Narrowing in EM-Mature credit spreads
- Eventually, inevitably higher G3 bond yields

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