

The Global Financial Crisis: Challenges and Opportunities for Developing ABM

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Workshop on Developing ABM in Financial Crisis:
New Roadmap and Regional Financial Cooperation

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Outline of the Presentation *

I: Global financial crisis: where we are now

II: Developing ABM: challenges and opportunities

* This presentation represents the views of the author and should not be interpreted as reflecting the views of the International Monetary Fund.

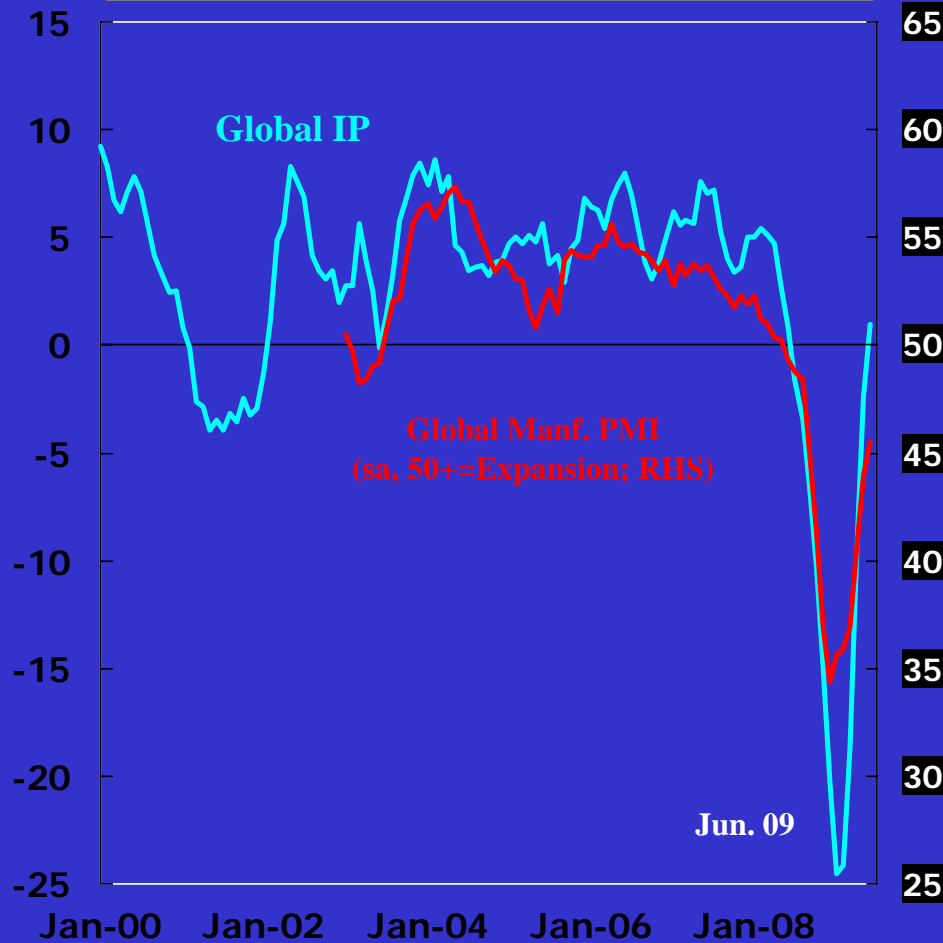
I: Global financial crisis: where we are now

- The global economy is beginning to pull out from the deepest recession in the post-World War II era, but recovery is expected to be sluggish, implying continued rise in unemployment.
- Financial conditions have eased, but remain far from normal and continue to be vulnerable to a renewed deterioration in macroeconomic conditions.
- Emerging economies have benefited from stabilizing external demand, a broad recovery of commodity prices, and improving financial market conditions, but some remain extremely vulnerable.
- The key policy priority remains restoring financial sector health by dealing with impaired assets and the recapitalization of viable but undercapitalized banks.
- Monetary and fiscal policies in major advanced economies should remain supportive until a sustained recovery takes hold.
- As and when market conditions permit and recovery becomes firmly established, credible and coherent exit strategies will be needed to unwind substantial public interventions in an orderly fashion.

The global economy is beginning to stabilize

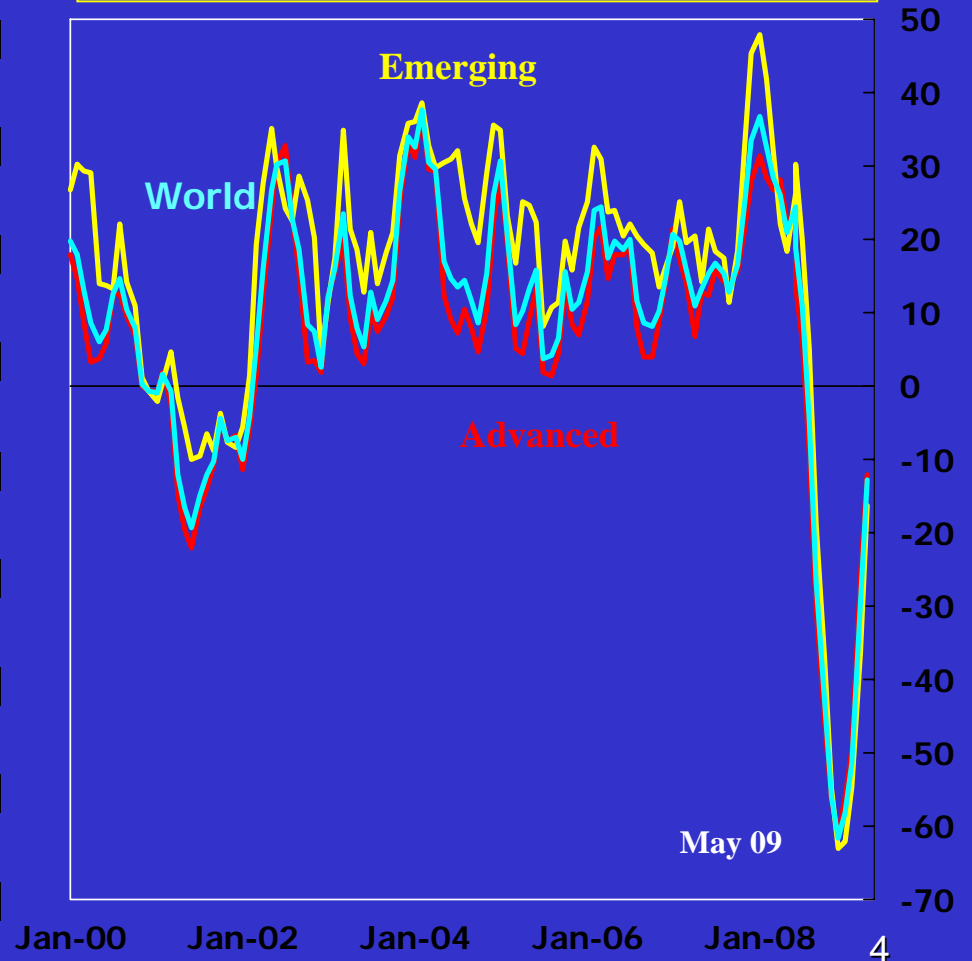
Industrial Production

(Annualized percent change of 3mma over previous 3mma)



Merchandise Exports

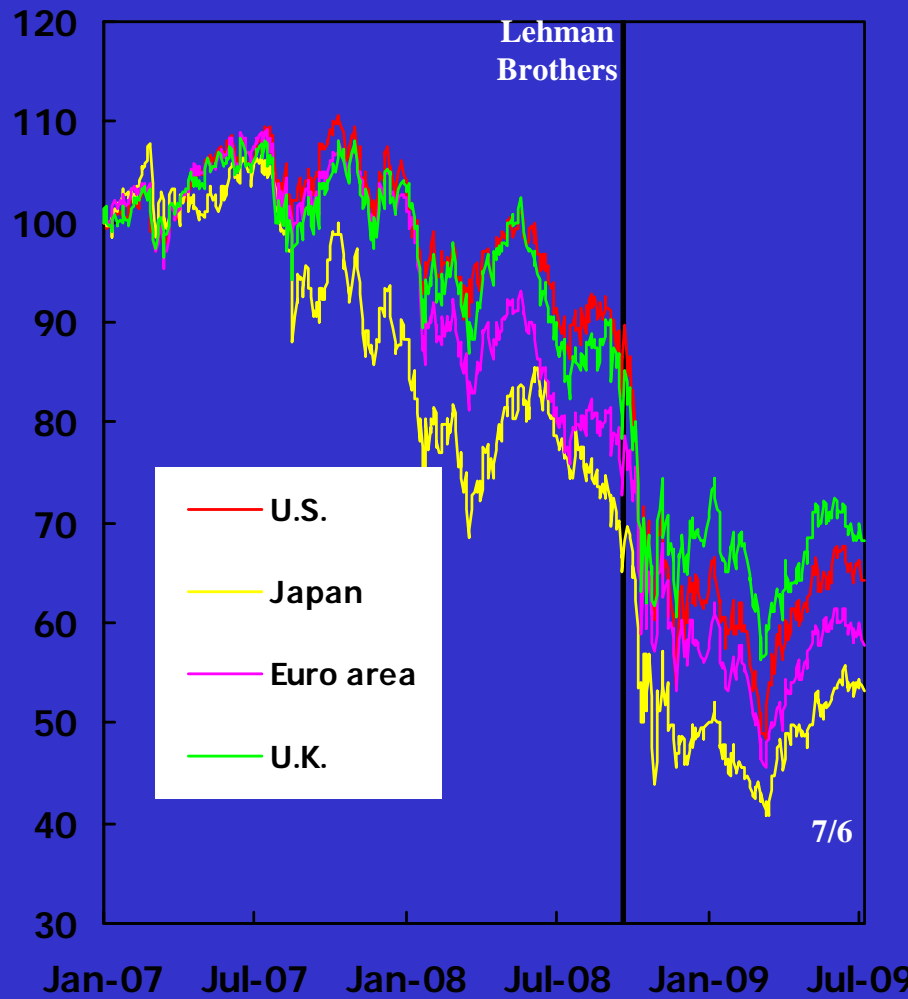
(Annualized percent change of 3mma over previous 3mma)



Equity markets and consumer confidence are also recovering

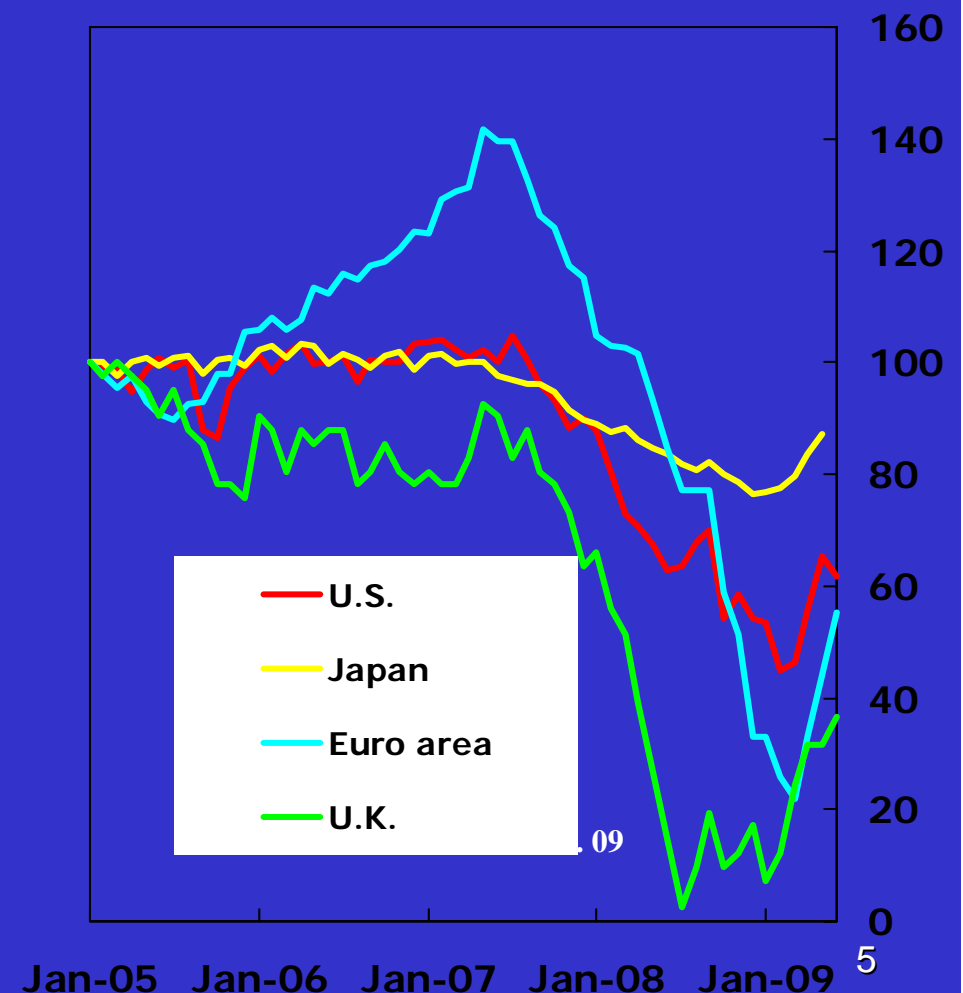
Equities

(1/1/2007=100; FTSE)



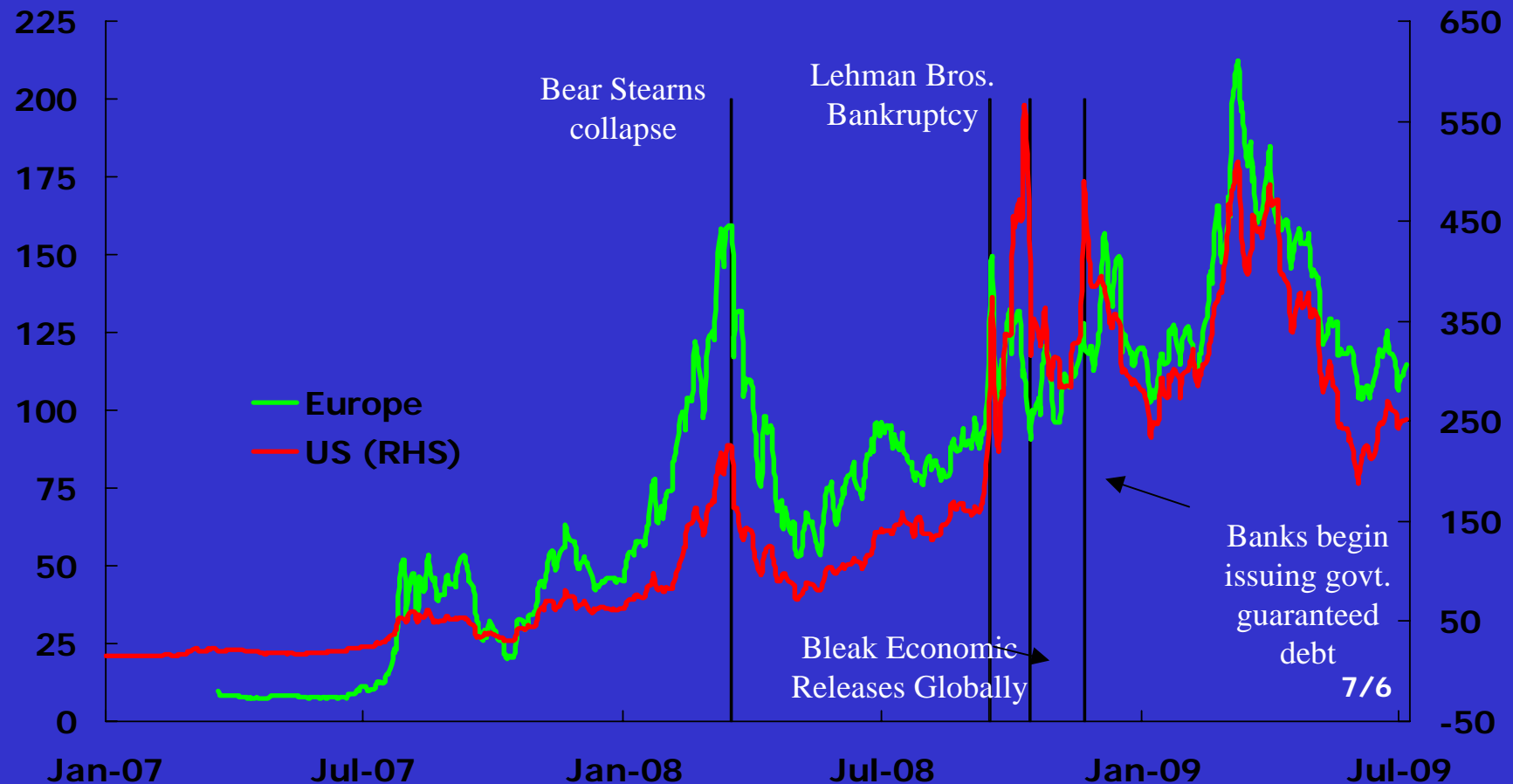
Consumer Confidence

(Jan. 2005=100)



Systemic risks have declined, reflecting wide-ranging policy actions

CDS Spreads for High-Grade Financials (basis points)

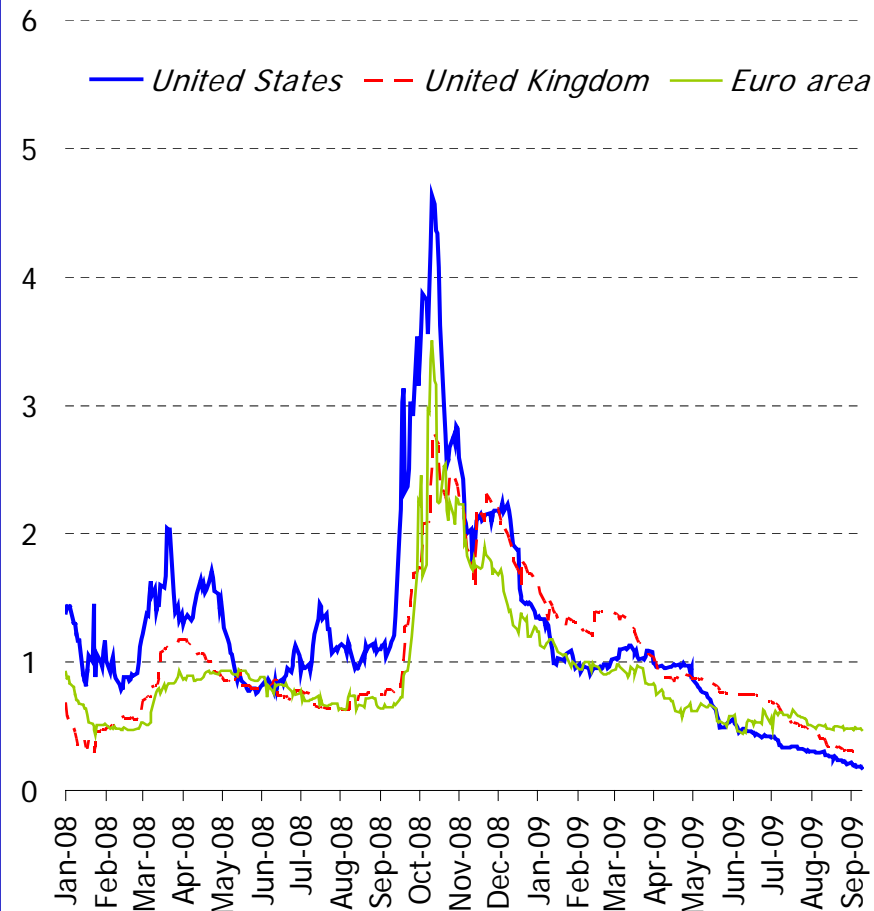


Source: Bloomberg L.P.

Financial market conditions have improved albeit remaining far from normal

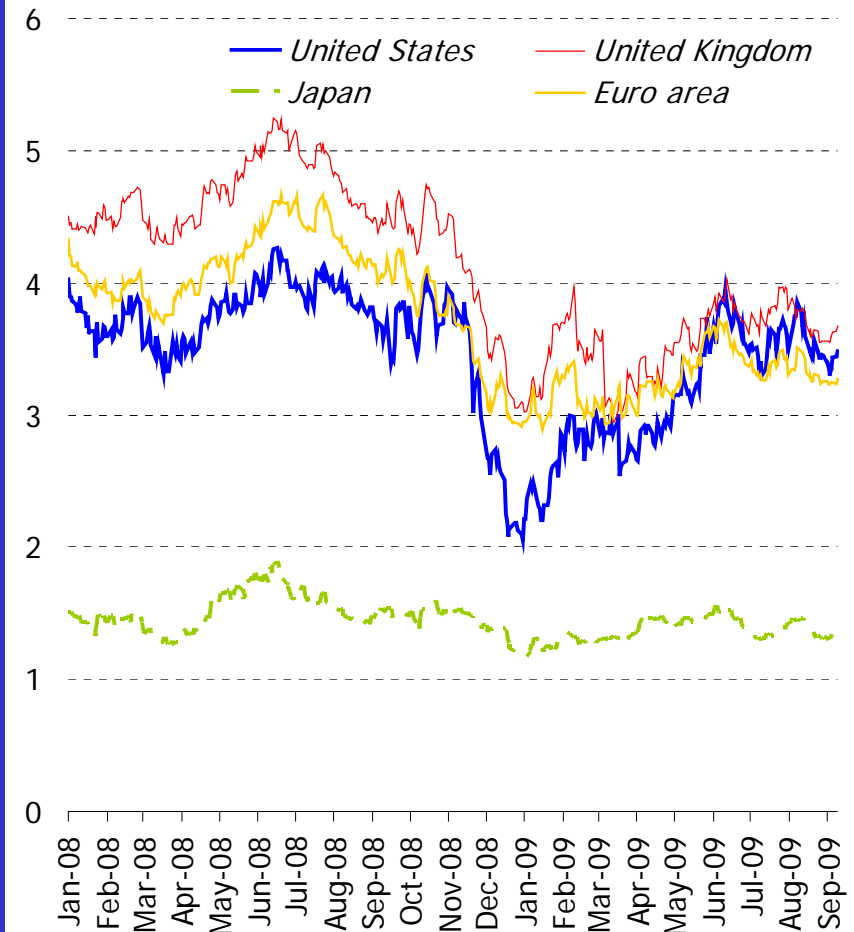
TED Spreads

(3-month LIBOR rate minus 3-month T-bill rate, in percent)



10-Year Government Bond Yield

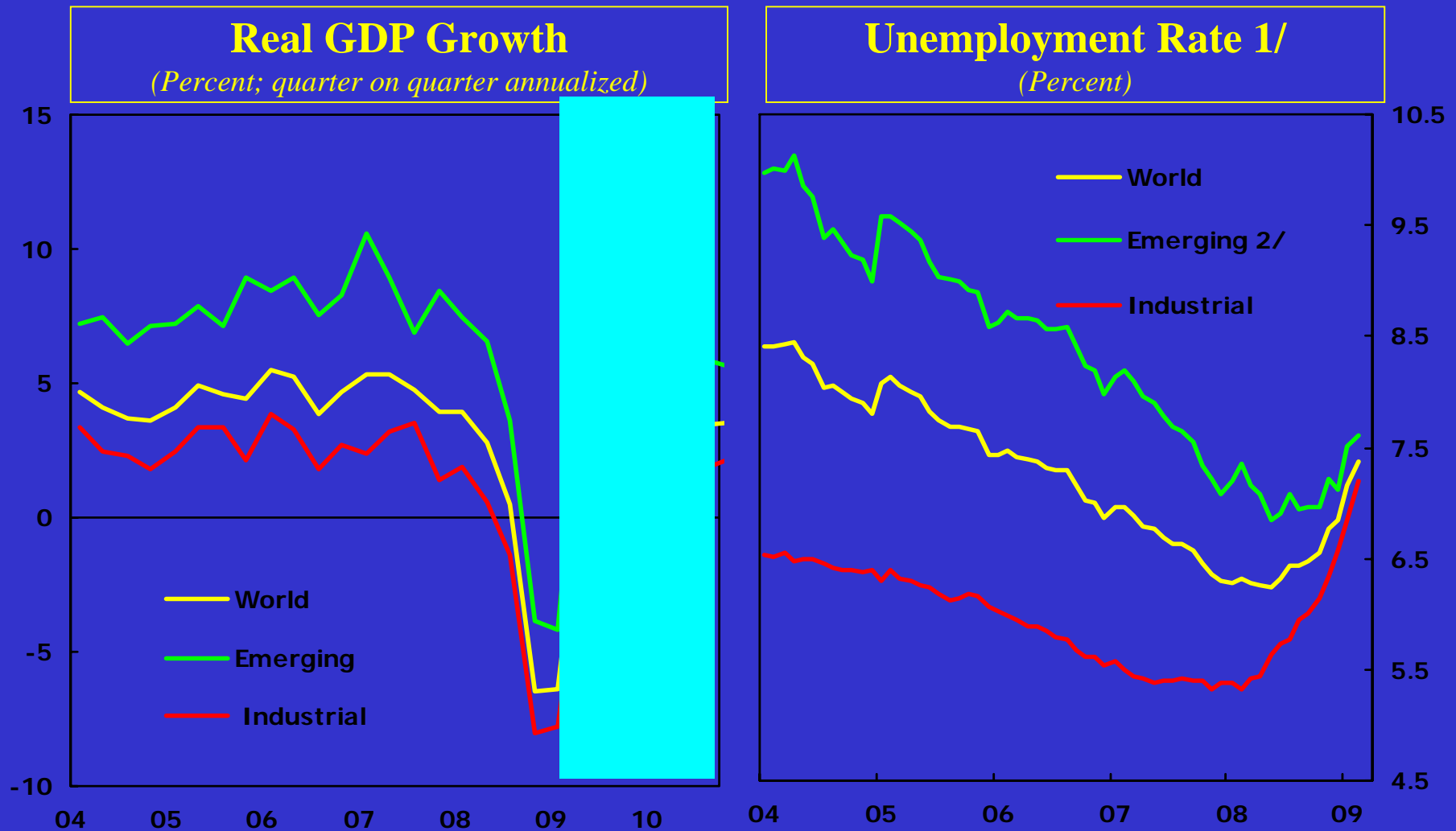
(In percent)



Growth projections vary widely across regions and economies

	2009		2010	
	World Economic Outlook	Difference from April 2009	World Economic Outlook	Difference from April 2009
World	-1.4	-0.1	2.5	0.6
Advanced Economies	-3.8	0.0	0.6	0.6
United States	-2.6	0.2	0.8	0.8
Euro area	-4.8	-0.6	-0.3	0.1
Japan	-6.0	0.2	1.7	1.2
Emerging and Developing Economies	1.5	-0.1	4.7	0.7
China	7.5	1.0	8.5	1.0
India	5.4	0.9	6.5	0.9
Brazil	-1.3	0.0	2.5	0.3
Russia	-6.5	-0.5	1.5	1.0

Across the globe, GDP is bottoming out, although unemployment continues to rise



Source: IMF, Global Data Source and staff calculations.

1/ Unemployment data series were aggregated using total labor force as weights.

2/ Excludes China, India, Indonesia, Hungary, and Pakistan.

Recovery will be sluggish

Recovery in 2010 is predicated on several key assumptions:

- Concerted policy actions to restore financial sector health.
- Continued macroeconomic policy support to bolster demand.
- A gradual improvement in credit conditions.
- Cushioning effect from sharply lower oil and major commodity prices.

Nonetheless, output gaps will continue to widen through 2010, implying rising unemployment.

Widening output gaps should keep inflation in check

Global Headline Inflation
(Percent change from a year earlier)



Risks to the outlook are to the downside

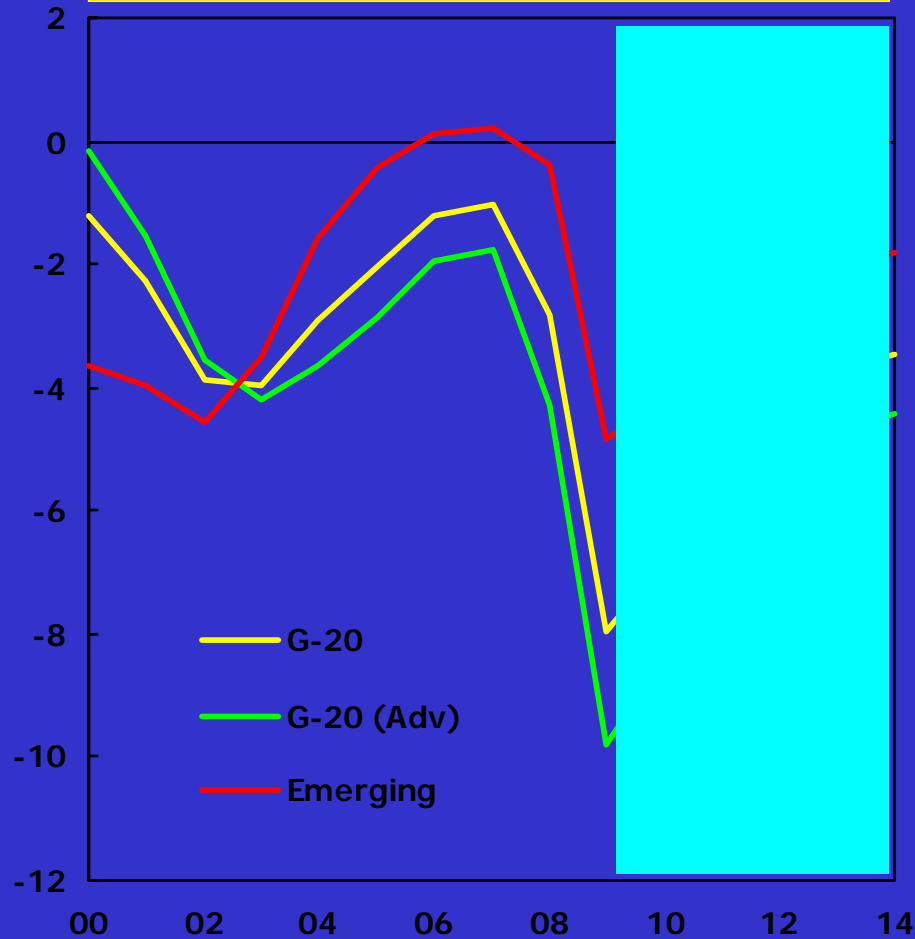
- The overarching risk is that financial strains will persist, particularly if efforts to deal with problem assets and to boost capital are not followed through forcefully.
- Sovereign fiscal sustainability concerns in the face of widening deficits and surging public debt could contribute to rising bond yields and undermine confidence.
- Emerging economies dependent on cross-border bank funding could face increasing financing difficulties if the current pace of global deleveraging continues.

But....

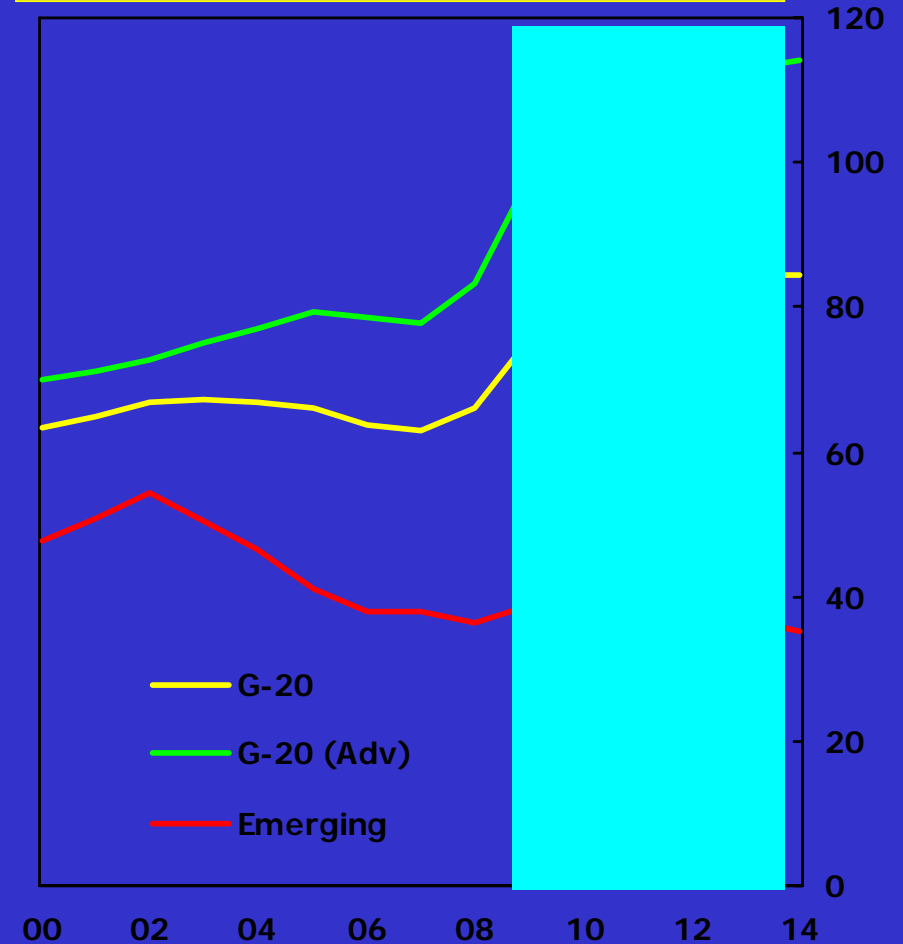
- There is upside potential to the outlook, hinging on bold implementation of policies.

The outlook for public finances remains a concern

Fiscal Balance
(Percent of GDP)



Government Debt
(Percent of GDP)

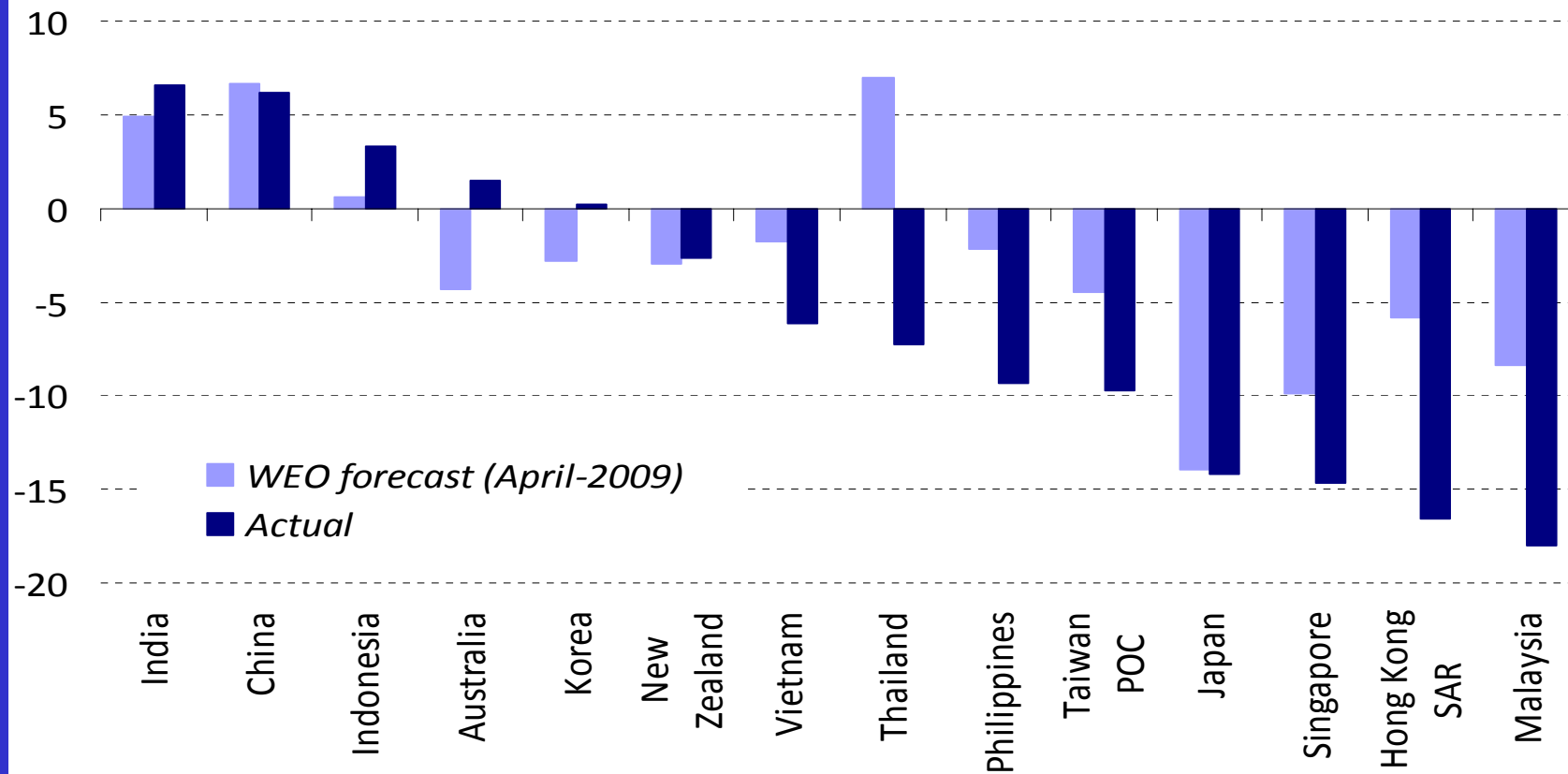


Source: IMF, World Economic Outlook.

For most Asian economies, output declines in the first quarter proved larger than anticipated in the Spring 2009 WEO projections

Asia: 2009Q1 Real GDP Growth

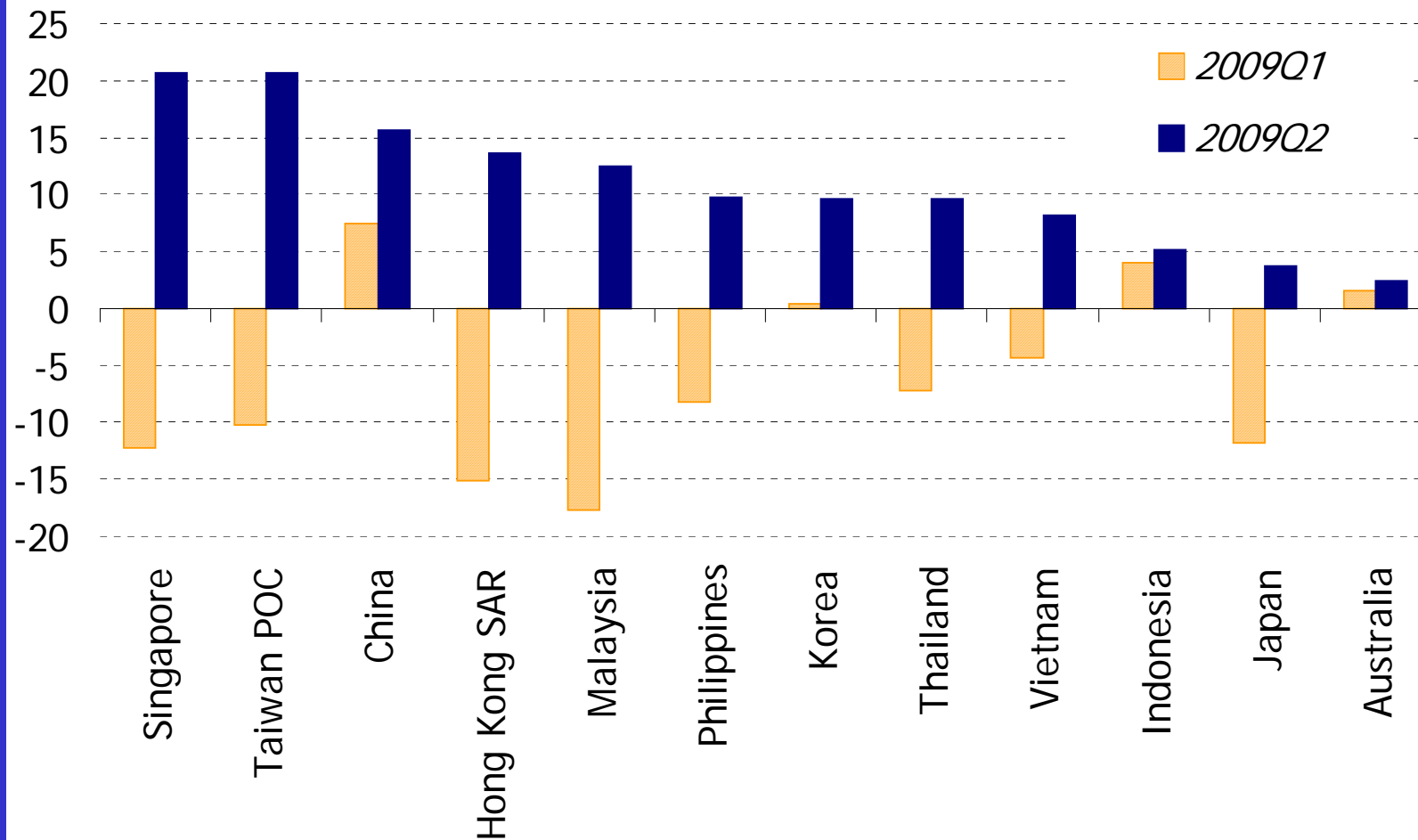
(In percent, quarter-on-quarter, SAAR)



GDP growth rebounded strongly, however, in the second quarter

Selected Asia: 2009 GDP Growth

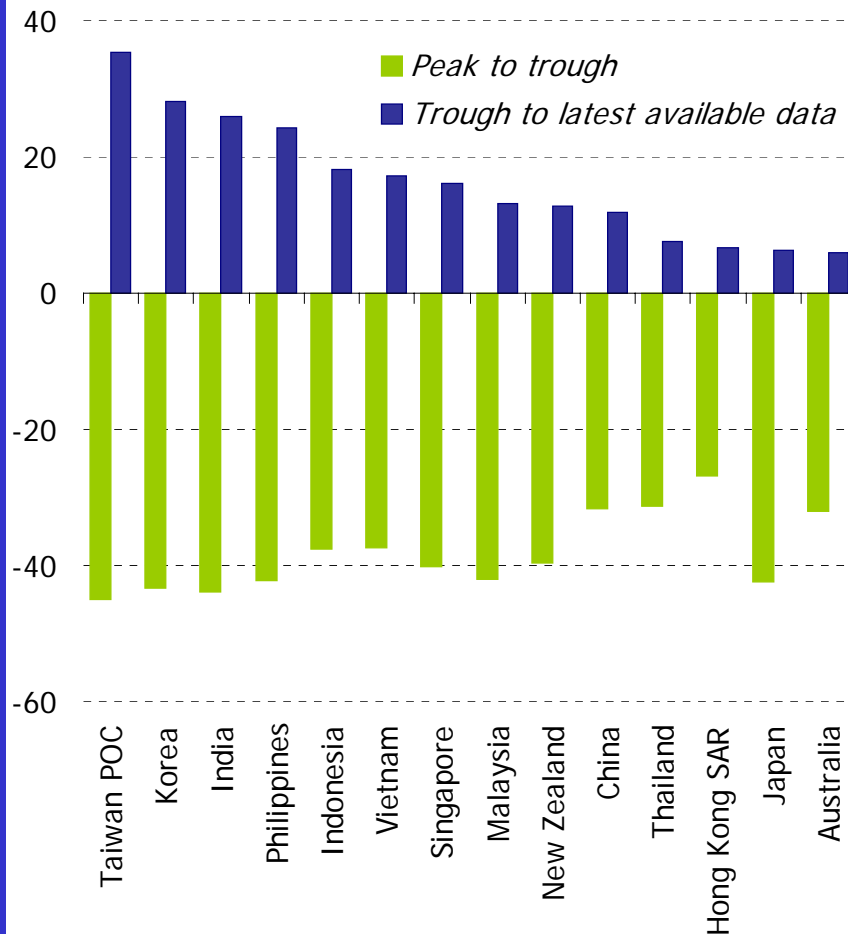
(Quarter-on-quarter percent change, SAAR)



The latest high frequency data suggest that Asian economies are continuing to improve

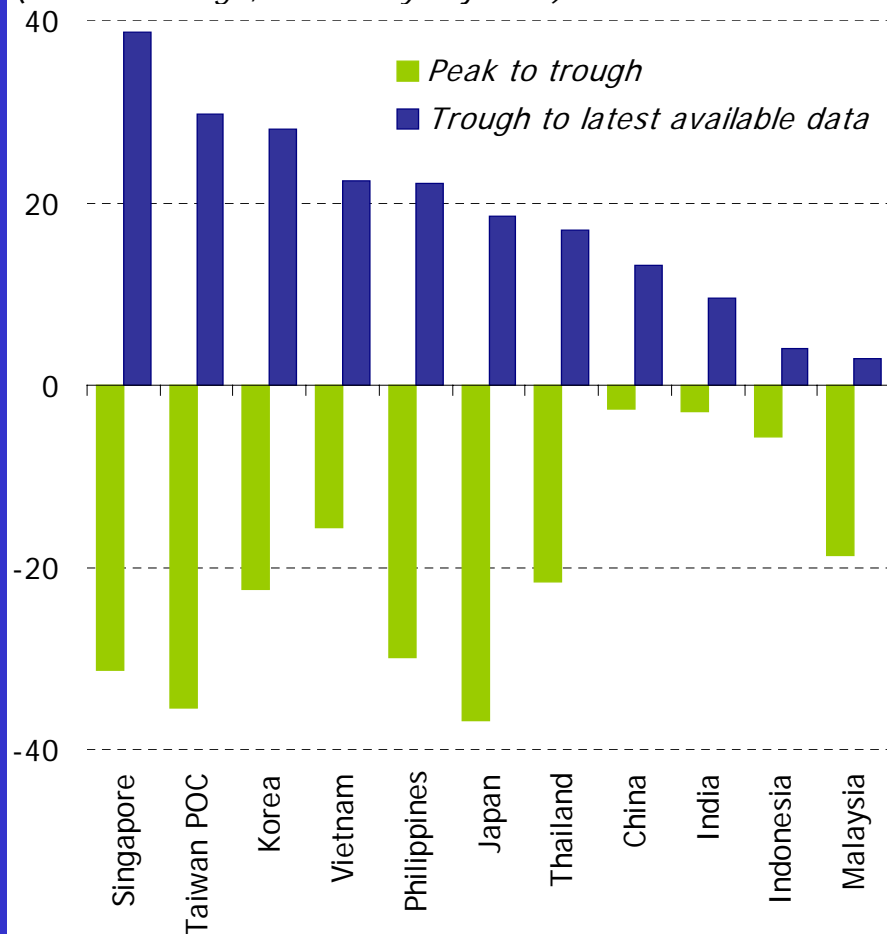
Export Recovery in Asia

(Percent change, seasonally adjusted)



Selected Asia: Recovery in Industrial Production

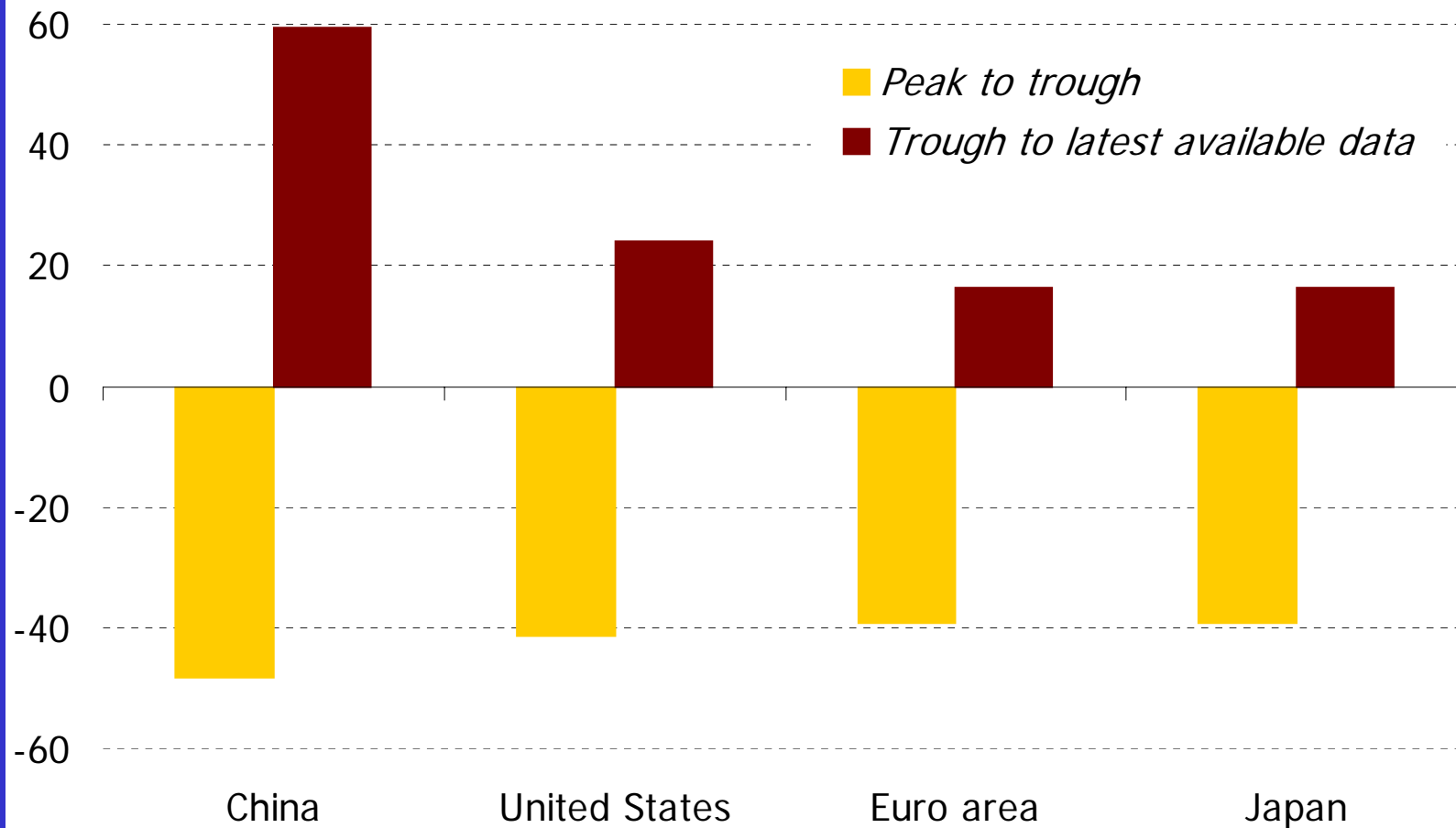
(Percent change, seasonally adjusted)



A potentially strong contribution to regional growth could come from China

Non-China Emerging Asia : Exports by Destination

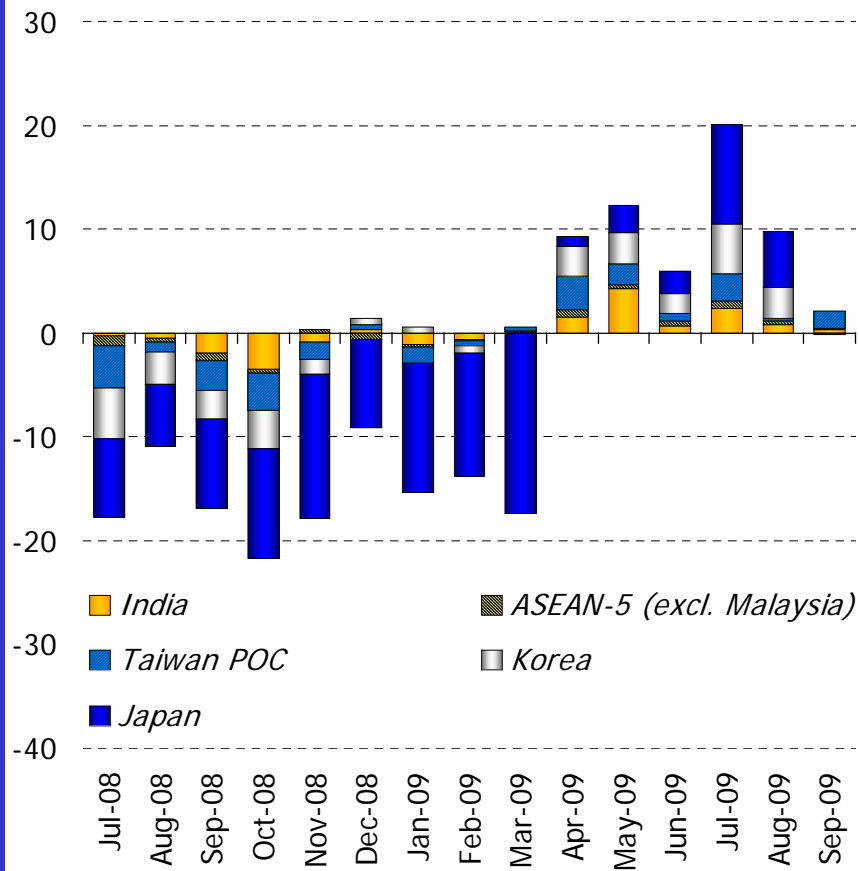
(Percent change)



Meanwhile, financial indicators indicate a broad-based recovery in investor confidence and a return of portfolio inflows

Selected Asia: Net Equity Inflows¹

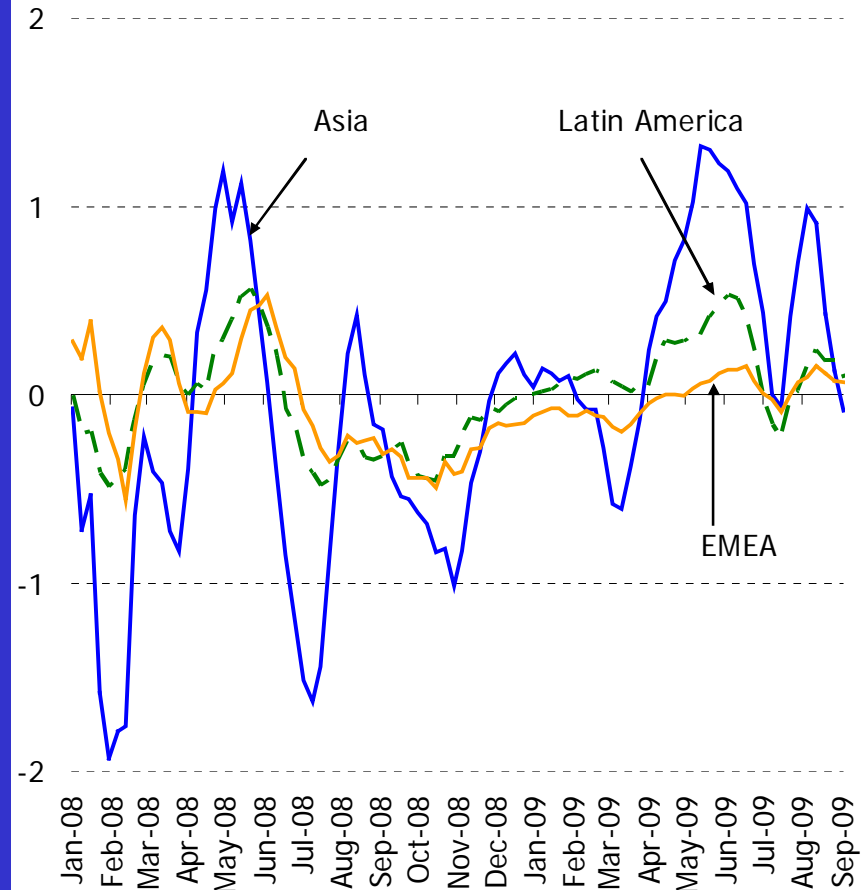
(In billions of U.S. dollars)



¹ Japan's data for September 2009 not yet available.

Net Flows to Emerging Market Equity Funds since 2008

(In billions of U.S. dollars, 4-week moving average)



Against this background, growth projections for Asian economies have been generally revised upward

The upward revision for 2009 reflects a **greater-than-anticipated resilience in domestic demand** on account of the aggressive policy response, and a boost to production from stock building.

But some of the recent improvements may reflect **one-time corrections**, rather than the beginning of a sustained improvement in demand.

There are also other downside risks

- Much of Asia's domestic demand has come from **macroeconomic stimulus**, notably in China, Korea, India and Indonesia. What happens next ? Also from car incentives in advanced economies.
- Moreover, **continued weakness in wage and labor income**—despite relatively minor job losses so far— and increases in commodity prices may compress household disposable income, and weaken private consumption.

Continued policy action may thus be needed to sustain domestic demand and insure against downside risks

- The **monetary stance** should remain supportive until a sustained recovery takes hold.
- With the recovery likely to be weak and output gaps likely to remain large, **fiscal stimulus** would need to be sustained into 2010.
- Authorities will need to remain vigilant about **financial sector** soundness.

At the same time, countries will need to begin preparing frameworks that allow an orderly exit from the extraordinary public interventions of the past few years

- In terms of **monetary policy**, they will need to develop exit strategies for the withdrawal of the exceptional liquidity support, so as to ensure a smooth return to normal market functioning.
- Meanwhile, **medium-term fiscal plans** should be put in place to reverse the deterioration of fiscal balances and ensure sustainable debt trajectories after growth is firmly re-established.

II: Developing ABM: challenges and opportunities

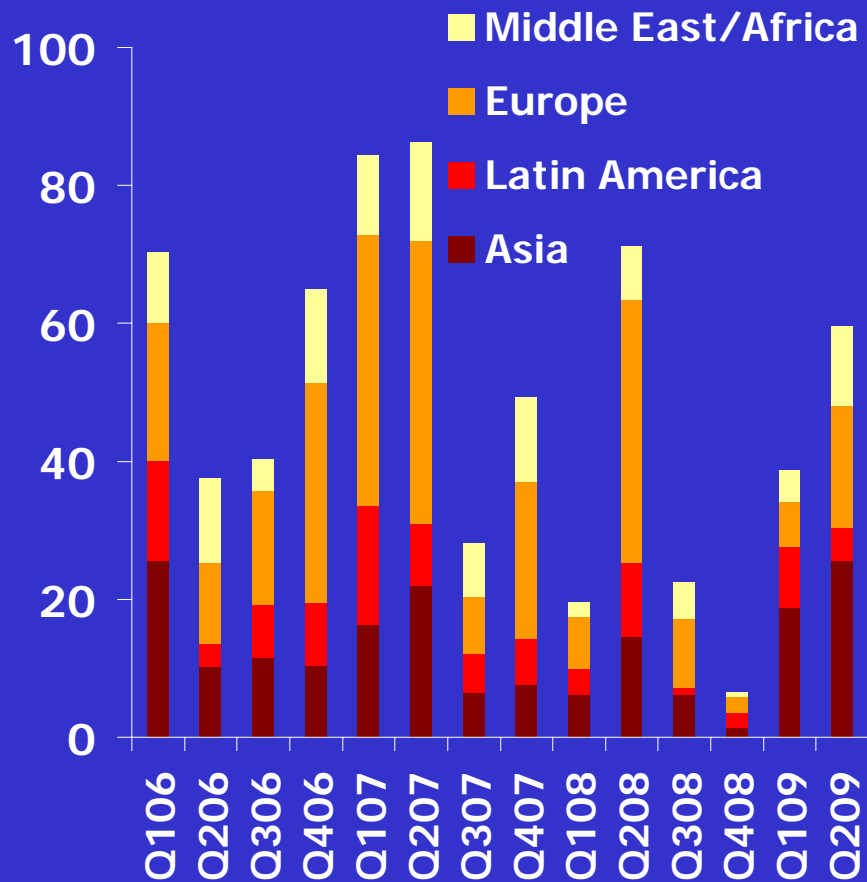
- Global financial crisis highlighted the need for a well-developed ABM.
- Compare with 1997 Asia financial crisis, Asian economies are in stronger position. Asia, as an engine for recovery in global economy, exhibited its abilities/potential for further developing ABM.
- Enhanced regional cooperation has helped countries meet the challenges for further developing ABM.

Global financial crisis highlighted the need for a well- developed ABM

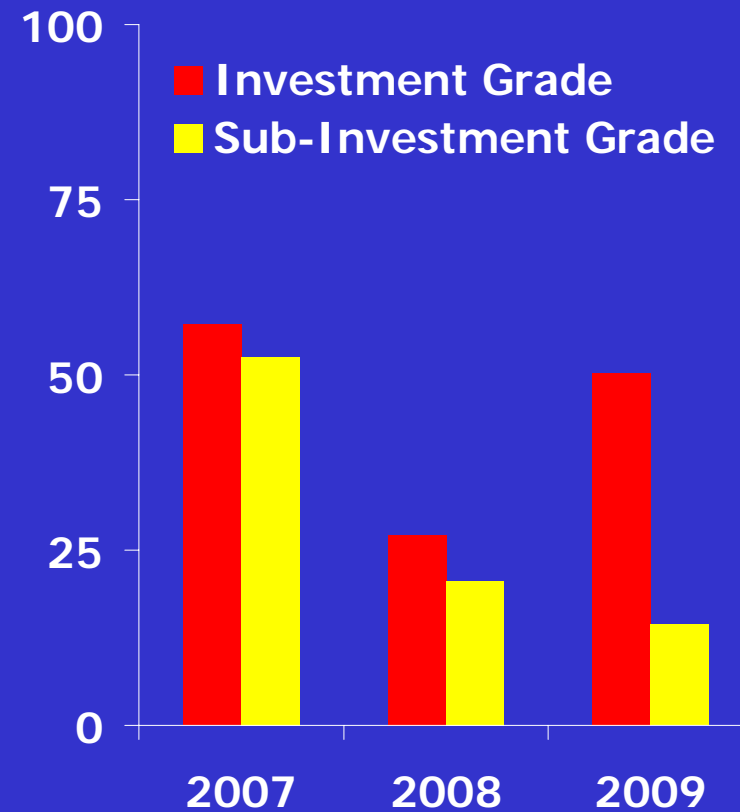
- Financial conditions have eased, but remain far from normal and continue to be vulnerable to a renewed deterioration in macroeconomic conditions.
- Portfolio flows into emerging market began to pick up, but remain a challenge.
- Emerging economies dependent on cross-border bank funding could face increasing financing difficulties if the current pace of global deleveraging continues.

Portfolio flows into emerging markets have picked up, albeit only to higher quality borrowers

Emerging Market External Bond and Equity Issuance (billions of U.S. dollars)

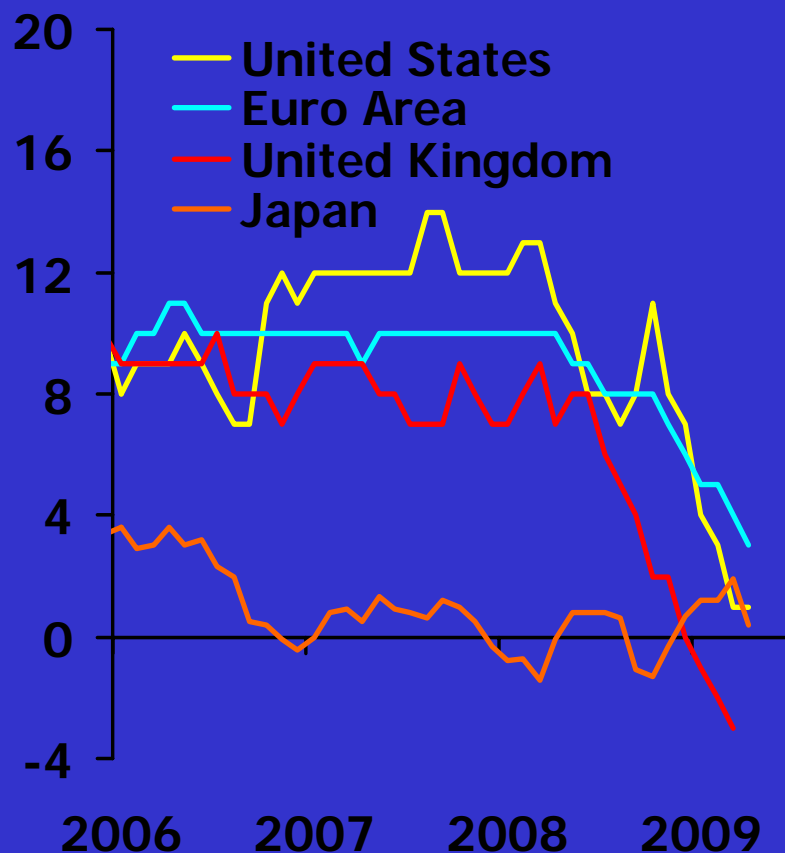


Emerging Market External Bond Issuance by Borrower Quality (Jan-May, billions of U.S. dollars)

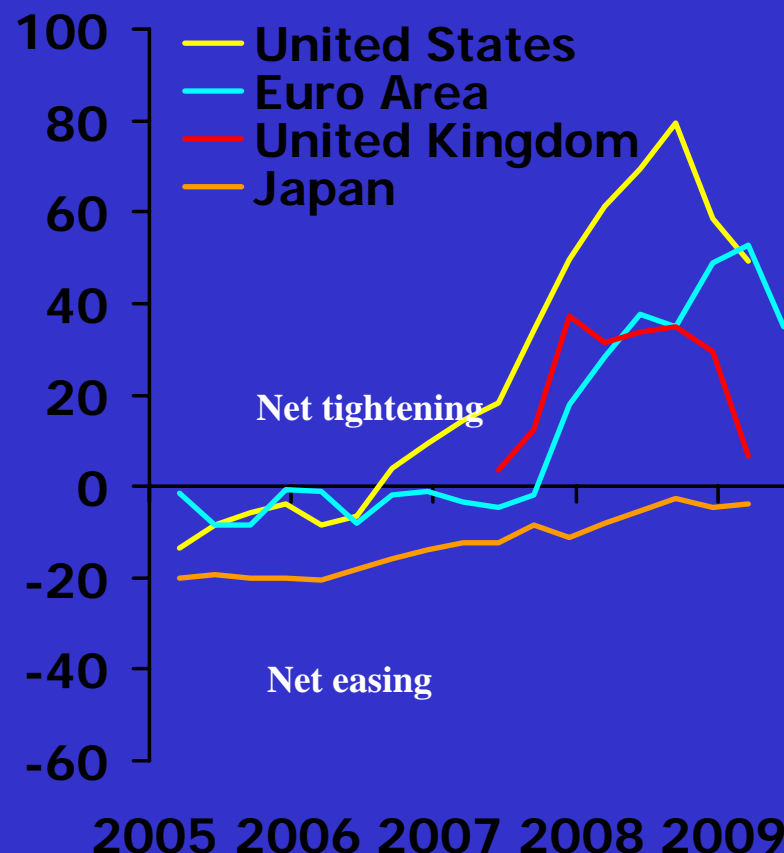


Banks continue to deleverage...

Bank Credit Growth to Private Sector (percent change year-on-year)



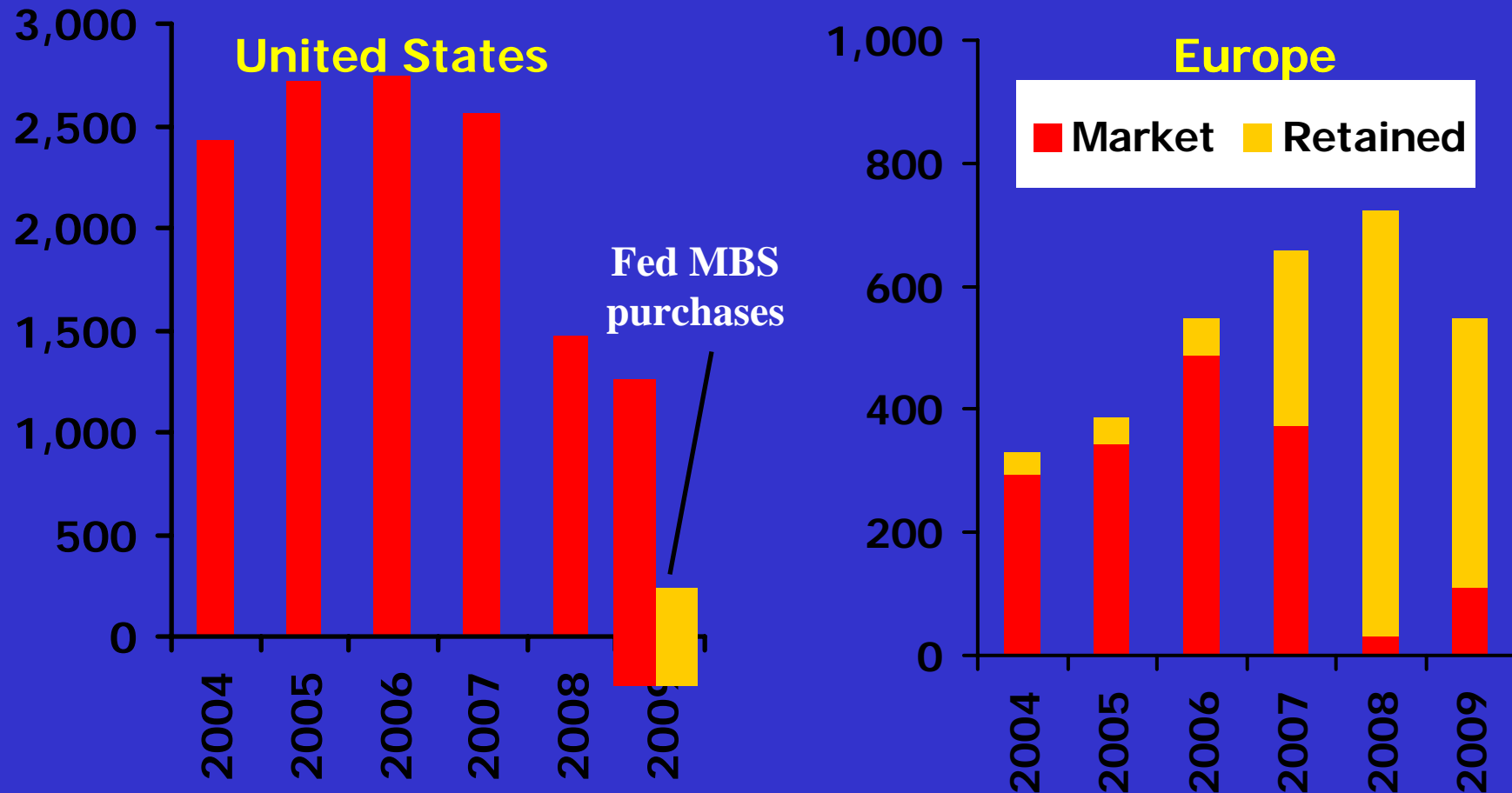
Lending Officer Surveys



Lending surveys represent weighted average of conditions for households and corporate.

... securitization remains impaired

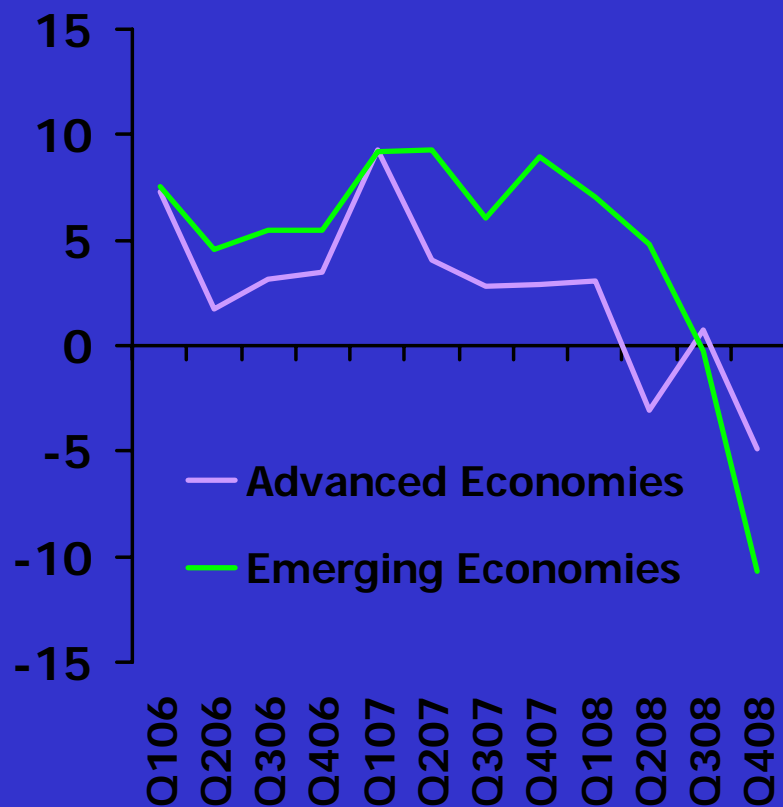
Securitization Issuance (billions of U.S. dollars)



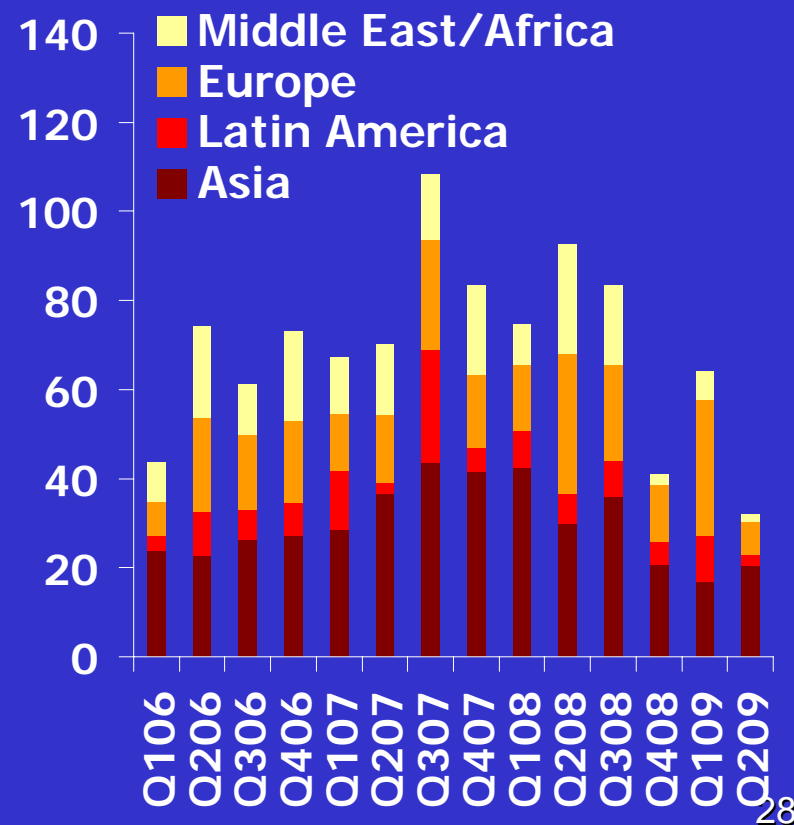
Issuance data annualized for 2009 and include mortgage-related and asset-backed securities. Purchasing data through end-June.

... and cross-border bank flows have suffered from continued deleveraging

BIS Banks: External Claims
(percent change, exchange rate adjusted)



Emerging Market External Loan Issuance
(billions of U.S. dollars)



Compare with 1997 Asia financial crisis, Asian economies are in stronger condition

- Many Asian economies still maintains positive growth, and the region remains as an engine for recovery in global economy.
- Asian economies have accumulated huge foreign exchange reserves. Currently, over half of world's foreign exchange reserves converged in the region, and in top 10 economies with largest foreign reserves, 7 of them are in Asia.
- The governments in the region are in much stronger condition to implement ABM initiatives.

Given its dynamism, Asia remains an engine for recovery in global economy

	2007	2008	2009	2010
World Output	5.1	3.1	-1.4	2.5
Advanced Economies	2.7	0.8	-3.8	0.6
United States	2.0	1.1	-2.6	0.8
Euro Area	2.7	0.8	-4.8	-0.3
Japan	2.3	-0.7	-6.0	1.7
Africa	6.2	5.2	1.8	4.1
Central & East Europe	5.4	3.0	-5.0	1.0
Developing Asia	10.6	7.6	5.5	7.0
China	13.0	9.0	7.5	8.5
India	9.4	7.3	5.4	6.5
ASEAN-5	6.3	4.8	-0.3	3.7
Middle East	6.3	5.2	2.0	3.7
Western Hemisphere	5.7	4.2	-2.6	2.3

Source: IMF's World Economic Outlook, July, 2009

Emerging Asian Bond Markets

- Under great variety of regional financial cooperation initiatives, such as those led by APEC, ASEAN+3 and EMEAP*, the Asian bond markets (including local currency and foreign currency), both public debt market and private debt market have advanced considerably since Asian financial crisis ended.
- For example, total domestic debt securities of the EMEAP markets have more than tripled.
- A noticeable development to further advance the Asian bond market is EMEAP's Asian Bond Fund (ABF) initiatives (ABF1 and ABF 2).

* Executives' meeting of East Asia and Pacific Central Bank (EMEAP) is a regional central bank forum with 11 members, It is mainly focus on financial cooperation in the region.

Opportunities/potential for further developing ABM

- High saving rates
- Large foreign reserves
- Needs for direct financing from borrower's point of view, and
- Needs for a new class of investment instruments from investor's point of view
- Government in the region aggressively prompt the developing of local debt securities market

Challenges to further development of ABM

- Financial reform and liberalization of capital controls
- Regulatory issues – market accessibility
- Tax and accounting, auditing, and disclosure issues
- Under developed bond market infrastructures
- Specific issues for each economy in the region?

Thank You!