

Financial Crisis and Global Recession: At a Turning Point?

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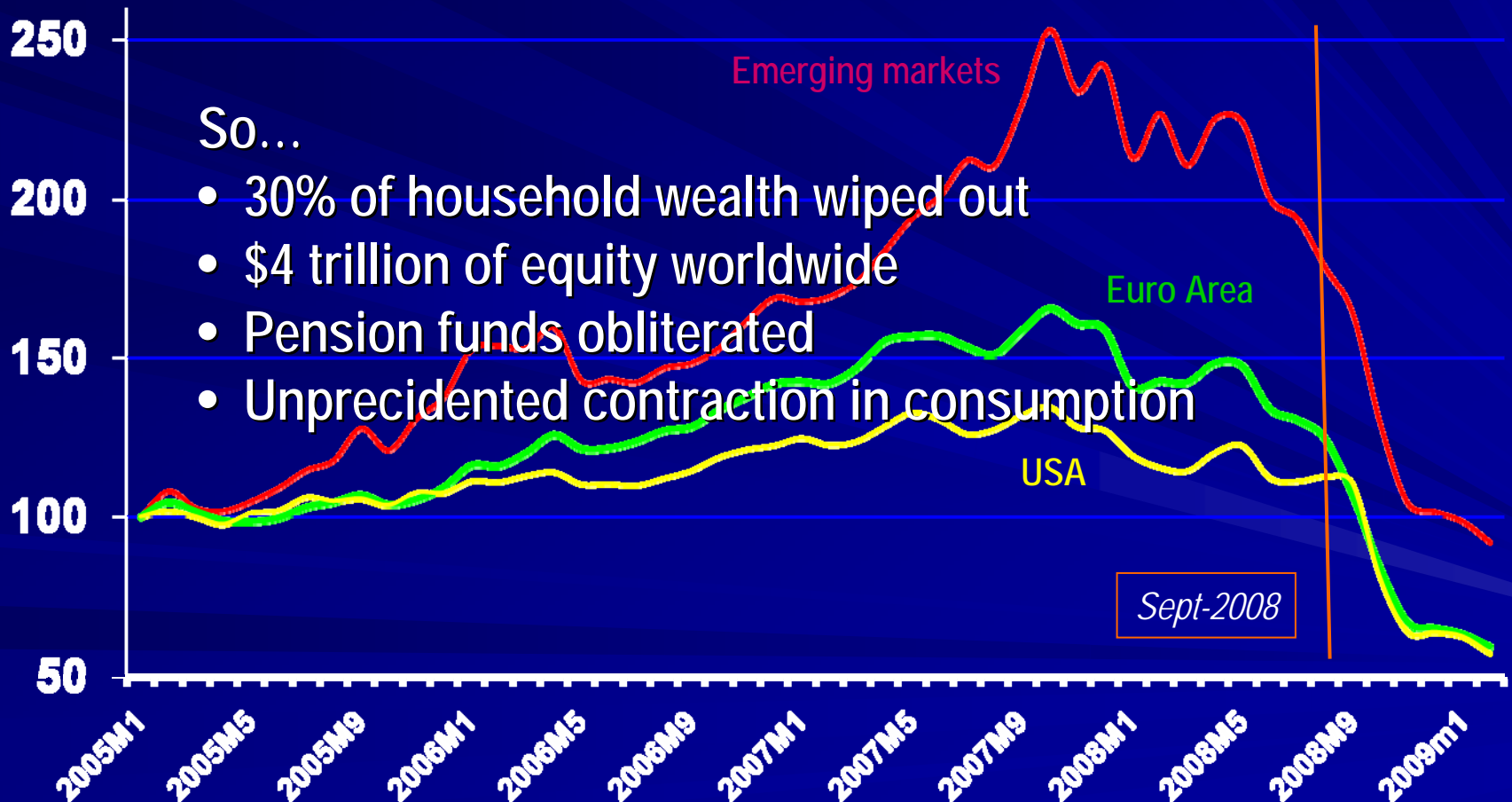
Geneva
June 29, 2009

Main messages

- Recession in the US now appears to be bottoming out, but speed and strength of recovery is uncertain
- Even though recession will eventually end, several daunting challenges remain, particularly for the poorest countries and vulnerable social groups
- Domestic policy is critical, but generating a sustained recovery requires new forms of multilateral collaboration

Crash of Lehman in September...precipitated financial panic that swept through global markets

MSCI equity price indexes, January 2005=100

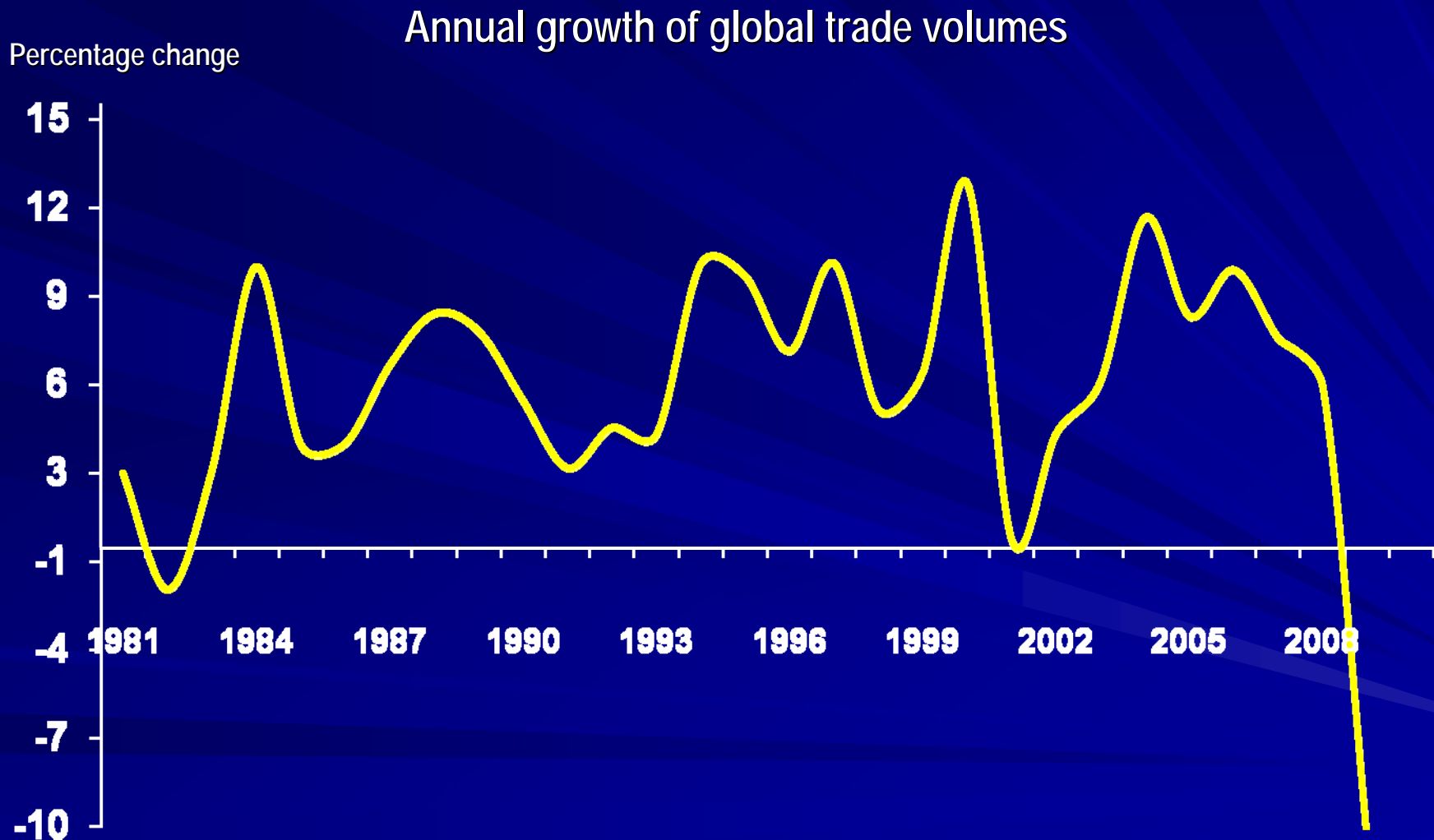


So...

- 30% of household wealth wiped out
- \$4 trillion of equity worldwide
- Pension funds obliterated
- Unprecedented contraction in consumption

Sept-2008

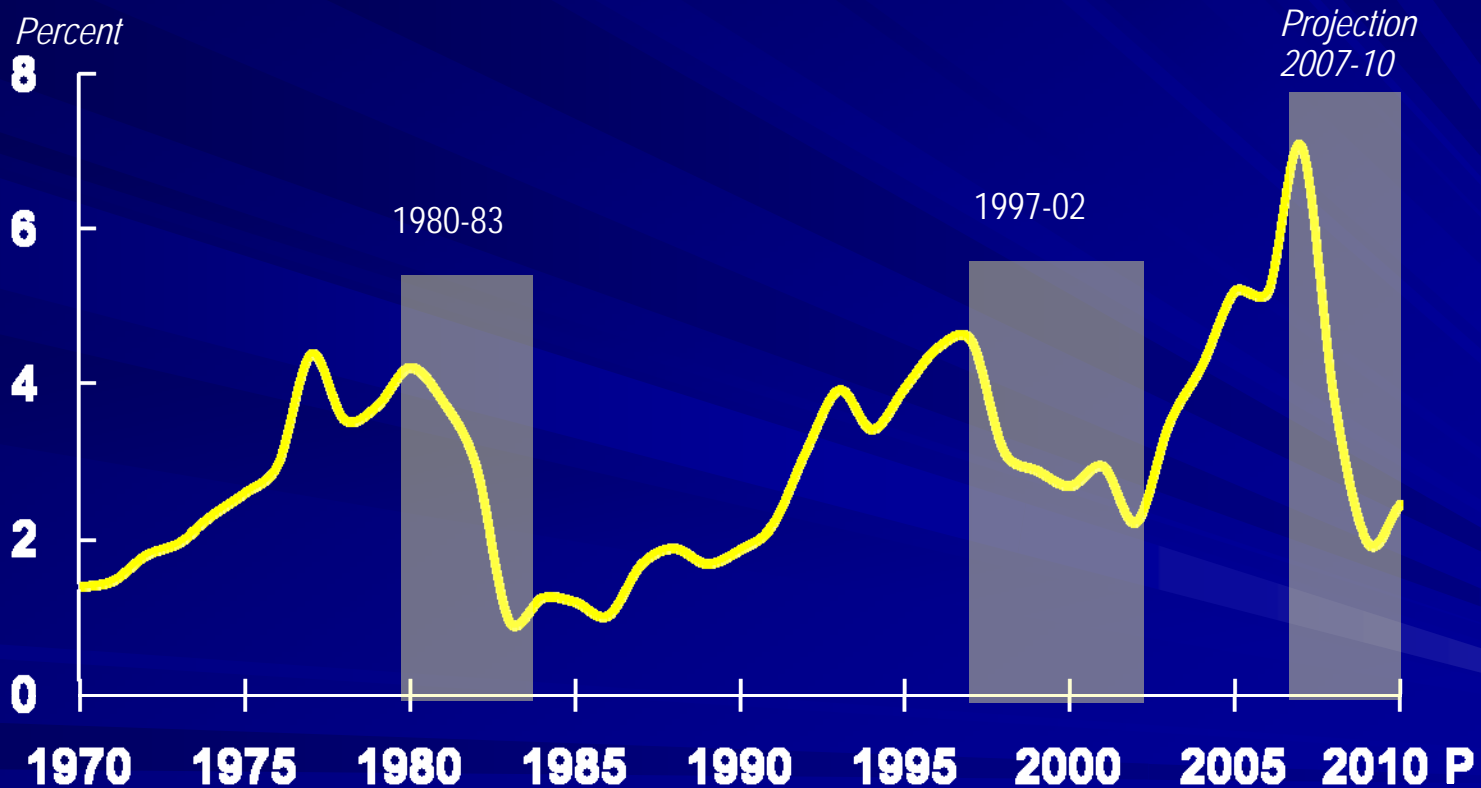
Contracting consumption in rich countries transmits recession to poor countries – as world **trade** collapses



Source: World Bank, *Global Economic Prospects*, 2009

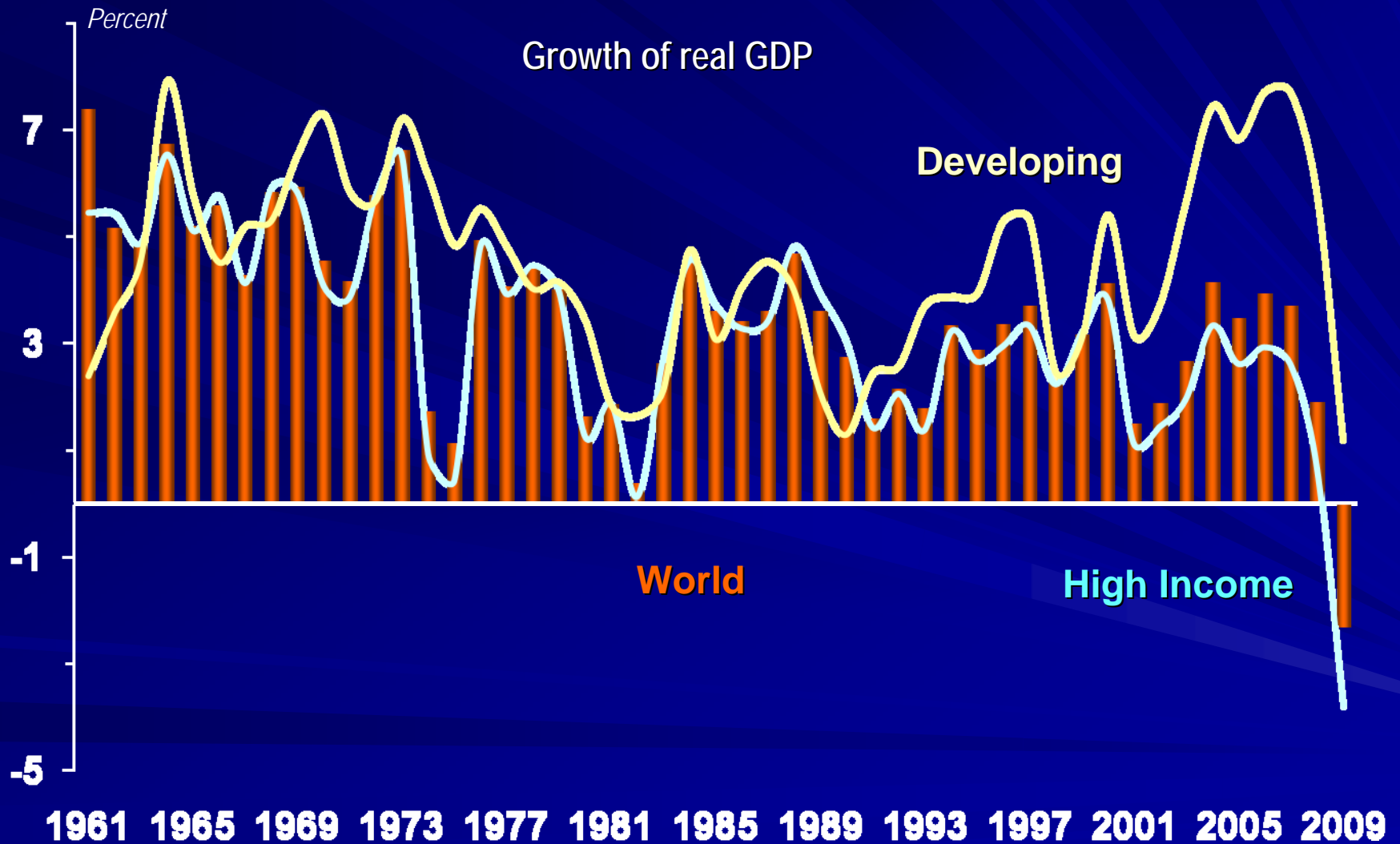
...and diminished **capital flows** have deepened recession in the developing world

Net private capital flows / GDP in developing countries



Source: World Bank, DEC Prospects Group.

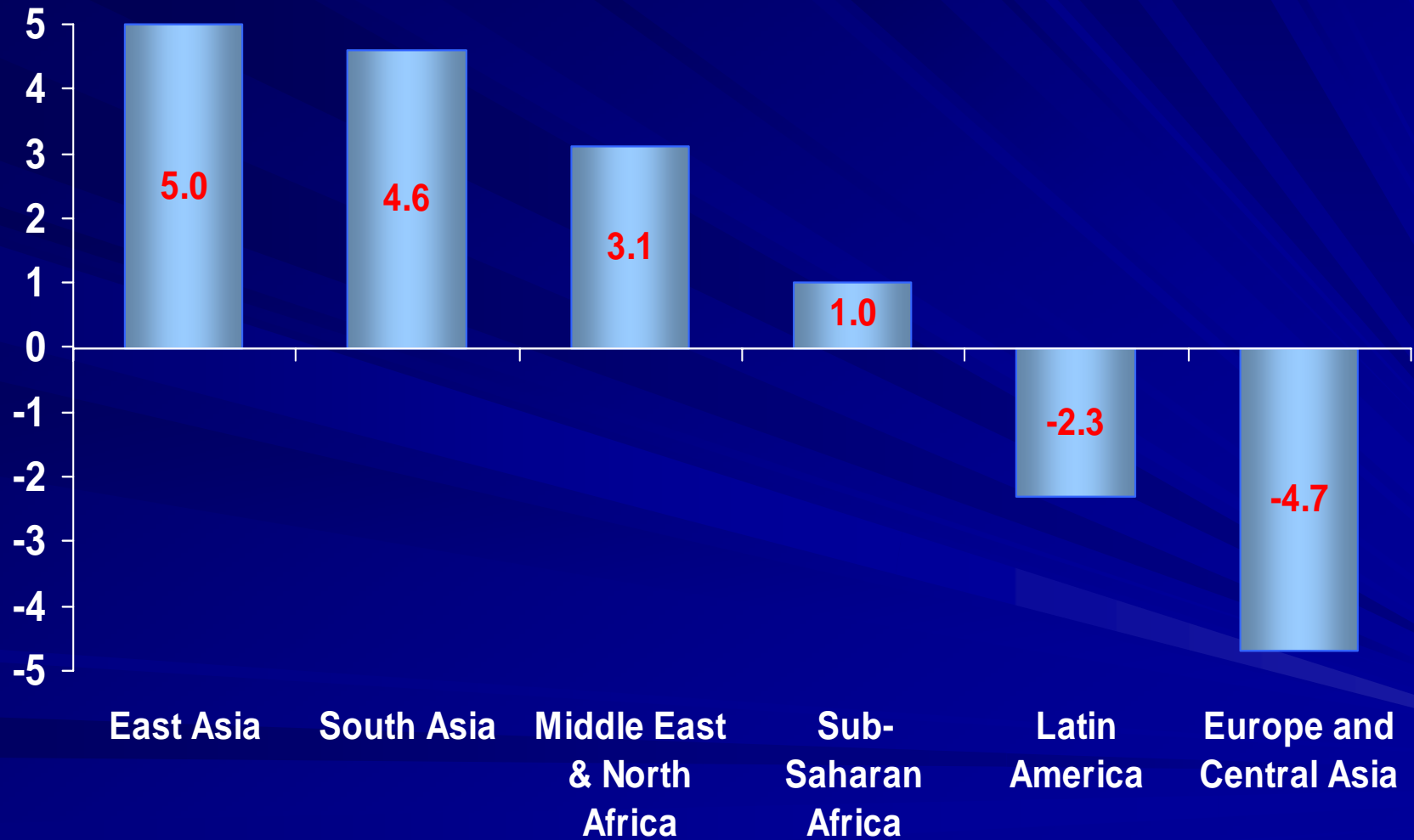
So now the world economy is contracting.... for the first time in the last half-century



Source: World Bank, DEC Prospects Group, Consensus Forecast, May 2009.

Crisis affects regions differently in 2009

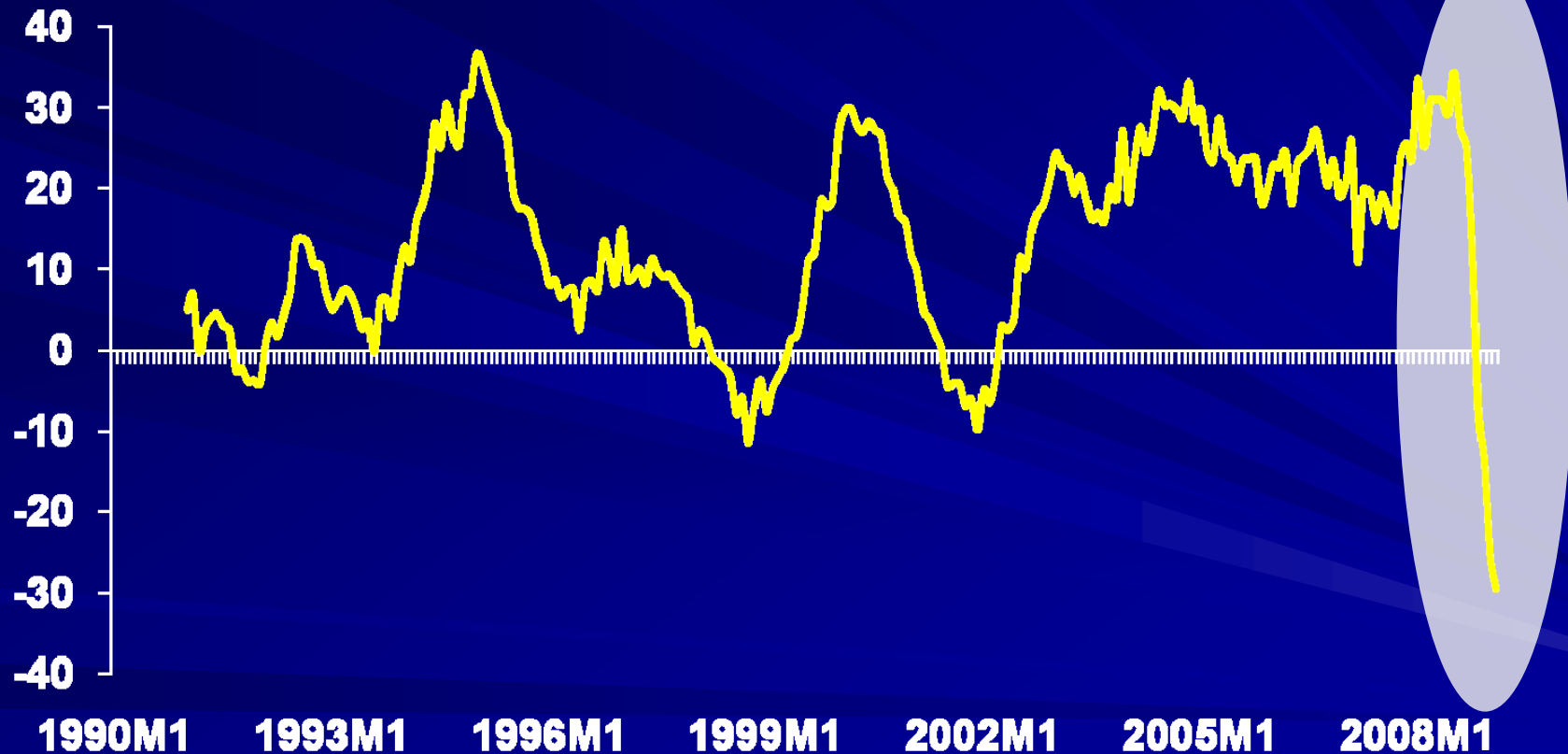
GDP growth, percent



Source: World Bank.

Trade in capital- and durable goods hit hard as global investment collapses

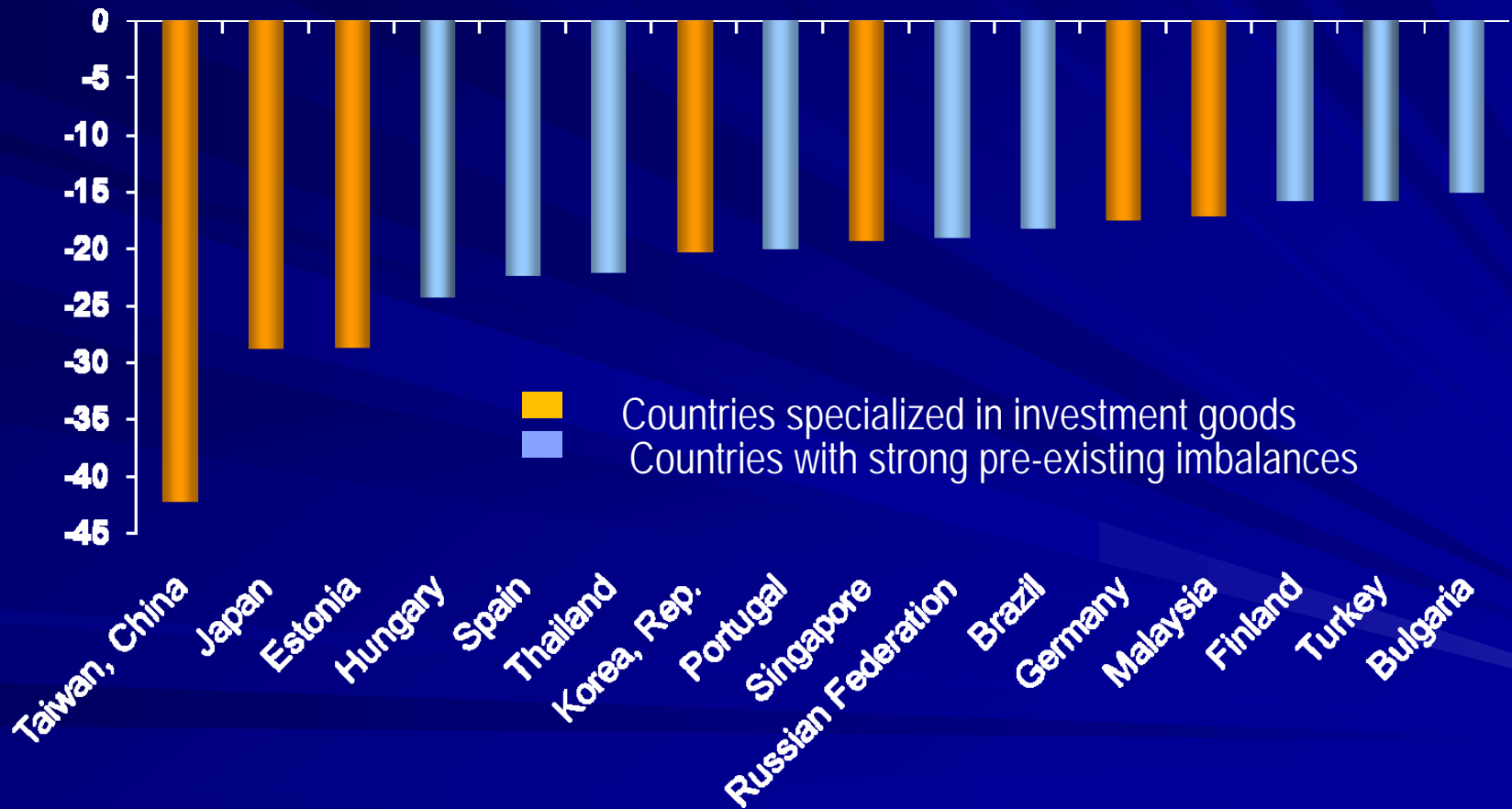
Growth in nominal exports of developing countries, year-over-year



Source: World Bank.

Production declines concentrated among countries specialized in investment goods

Industrial production; %change, January 2009 versus July 2008

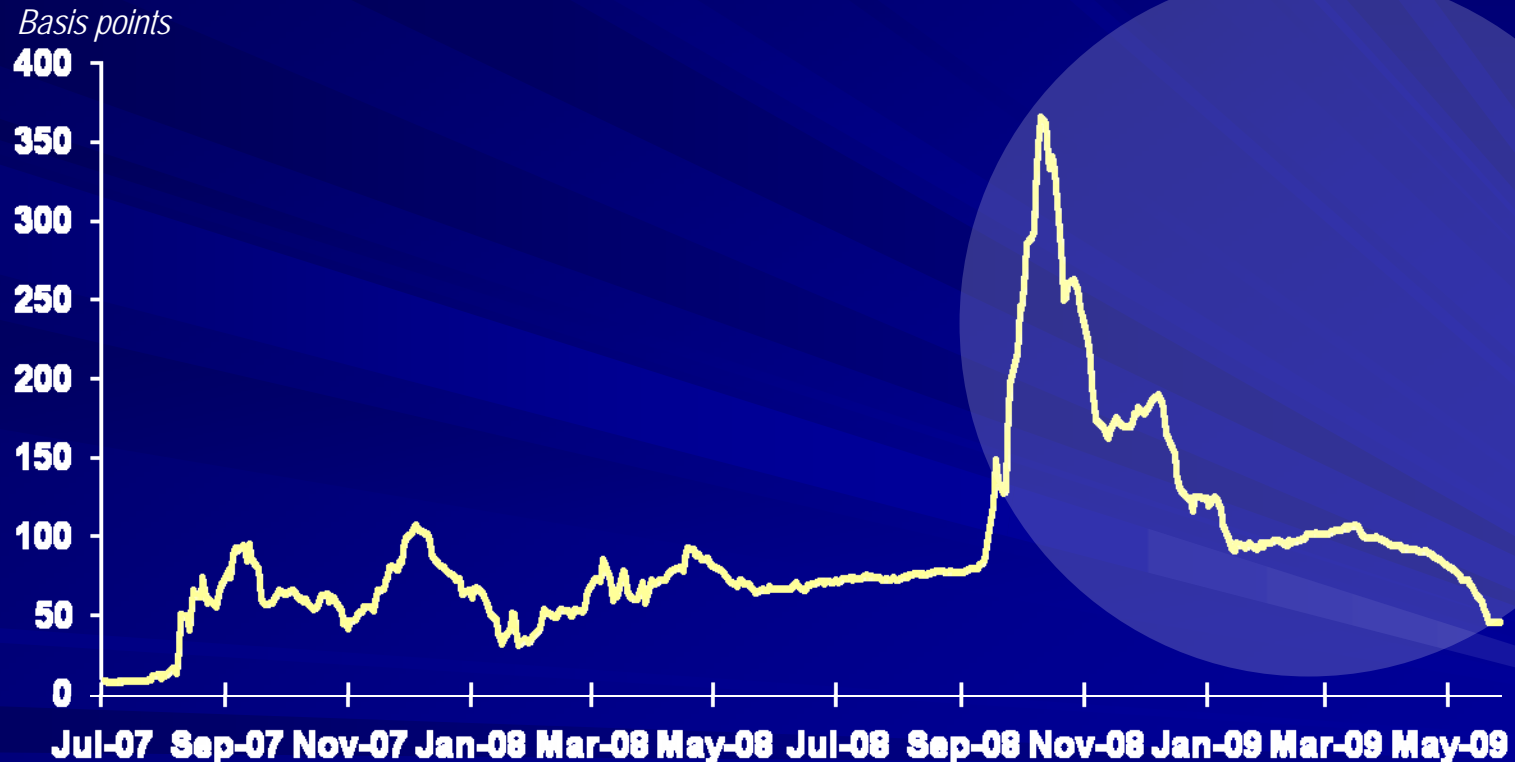


Source: World Bank.

Green shoots? Incipient signs of recovery....?

- Credit markets have stabilized...secondary markets beginning to reappear

Spread between 3 month \$ LIBOR and \$ OIS

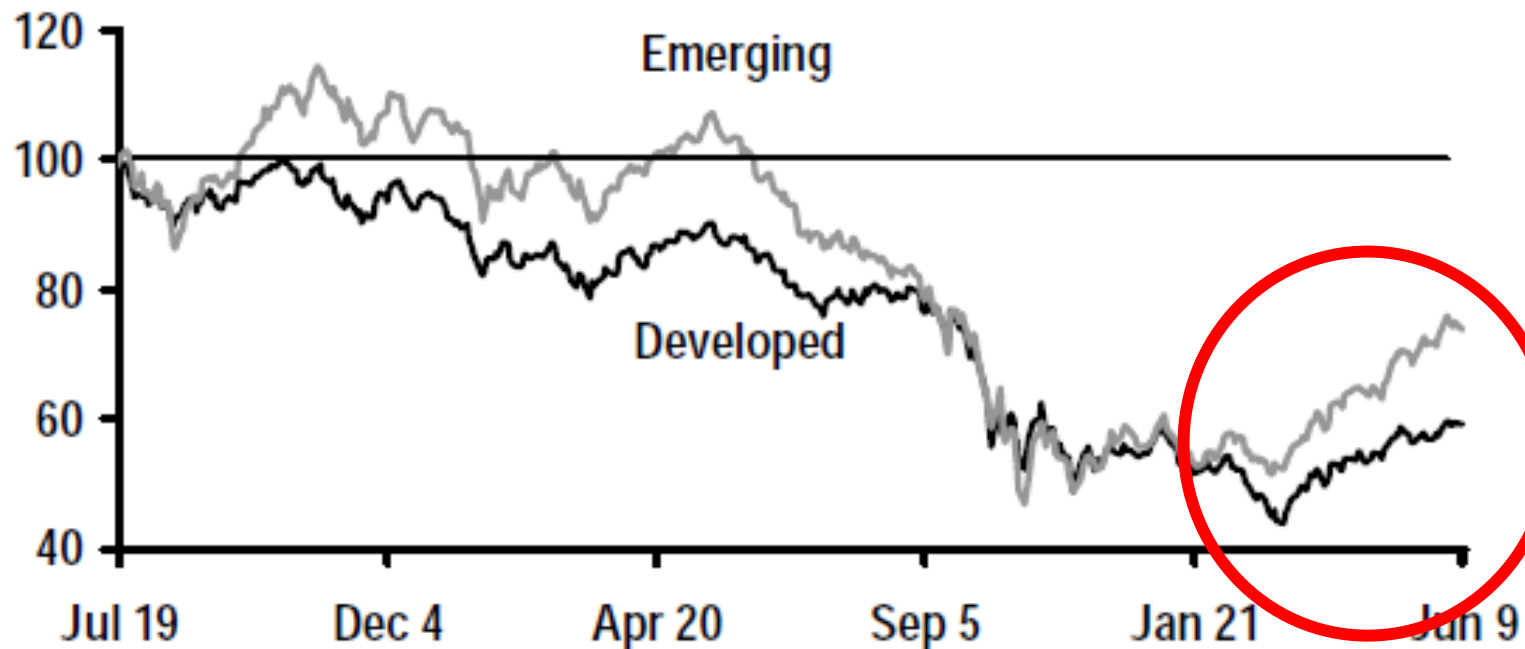


Green shoots? Incipient signs of recovery....

- Credit markets have stabilized...secondary markets beginning to reappear
- Equity markets appear to have established a floor

World equity indexes

Index, July 19 = 100



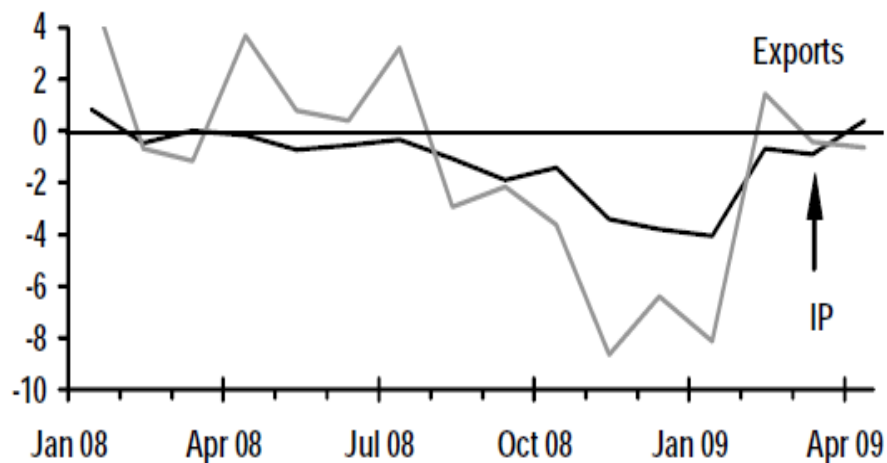
Source: JP Morgan, *World Financial Markets*, June 2009

Green shoots? Incipient signs of recovery....

- Credit markets have stabilized...secondary markets beginning to reappear
- Equity markets appear to have established a floor
- Personal income in US rose 0.4% in April...household savings hit 5.7% of disposable income (highest since 1995)
- Some life in the real sectors...

Global IP and merchandise exports

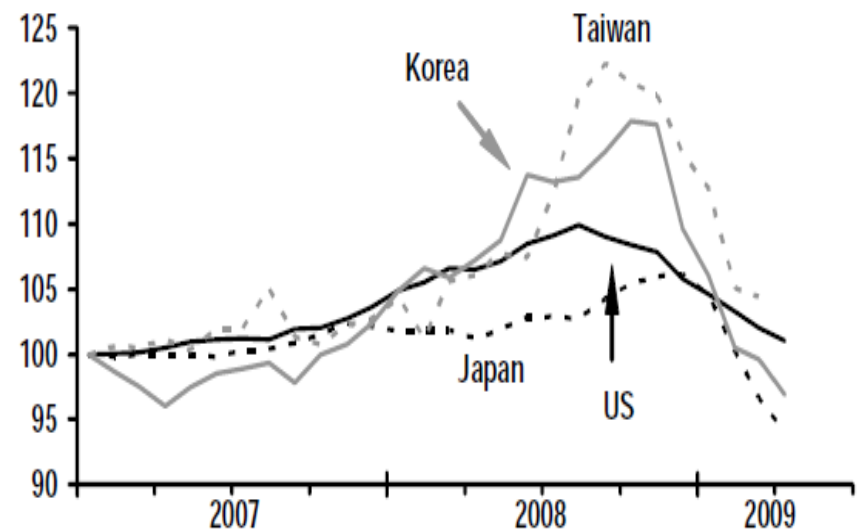
%m/m, samr



Source: JP Morgan, *World Financial Markets*, June 2009

Level of manufacturing inventories

Index, Jan07=100

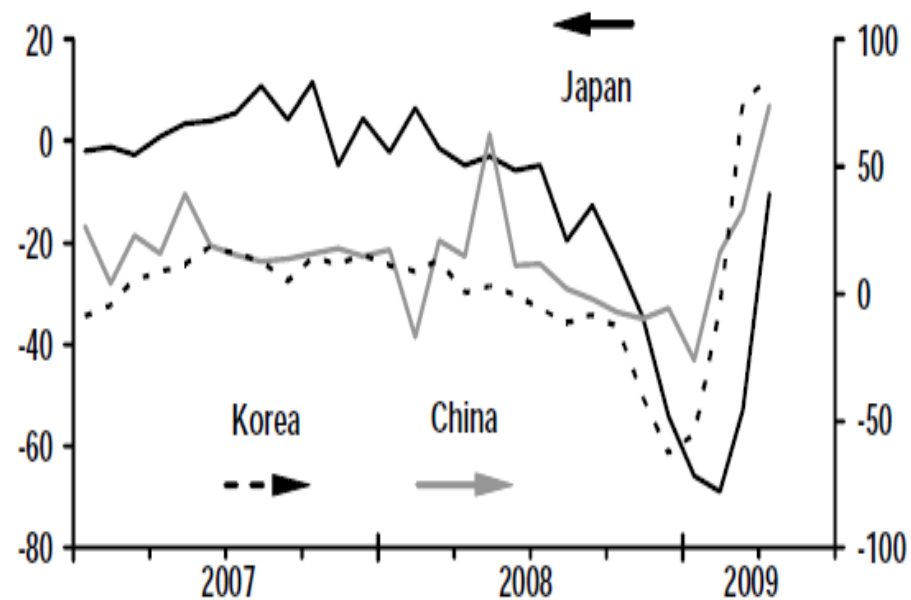


Green shoots? Incipient signs of recovery....

- ...and China's fiscal stimulus is beginning to take hold

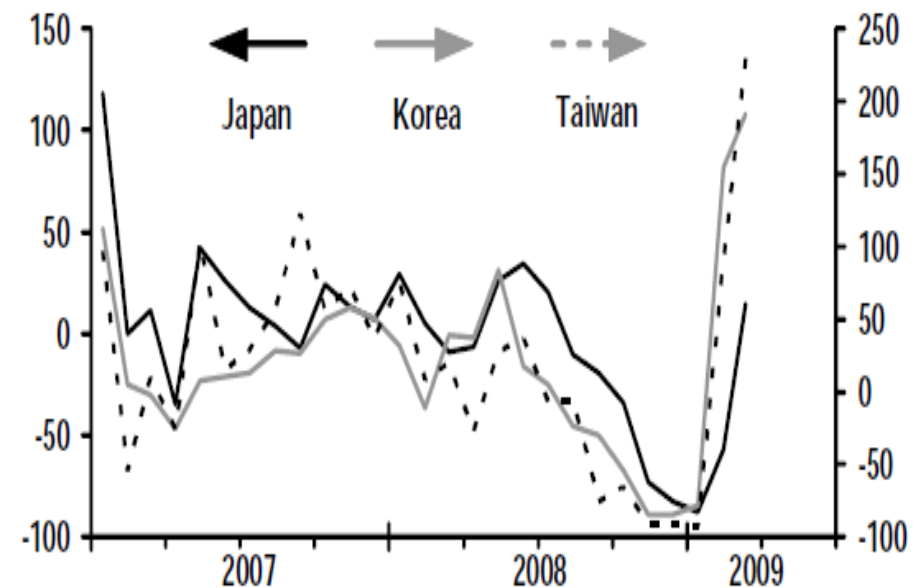
Asia manufacturing production

%3m saar, both axes



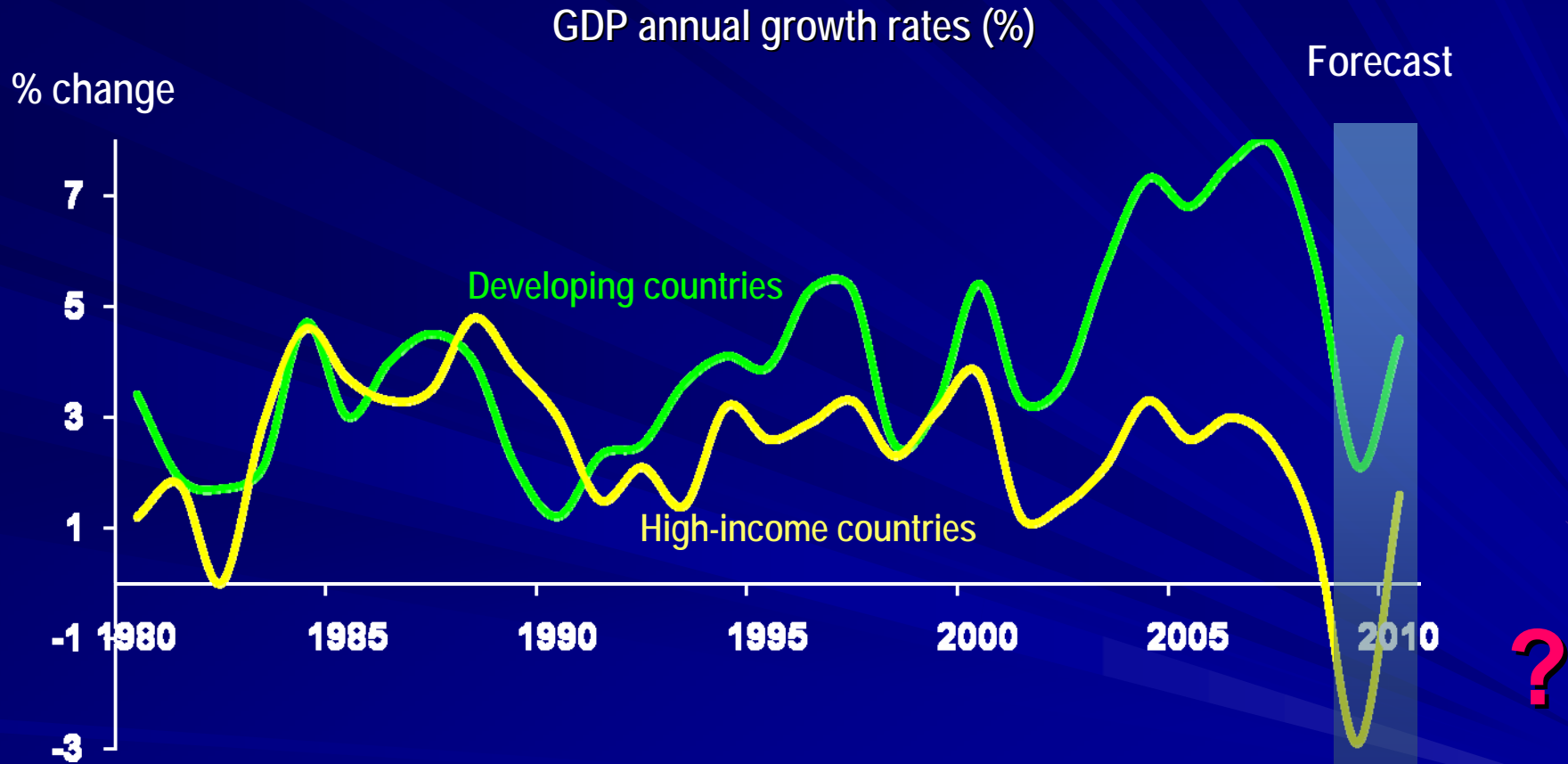
Asia exports to China

%3m saar, both axes



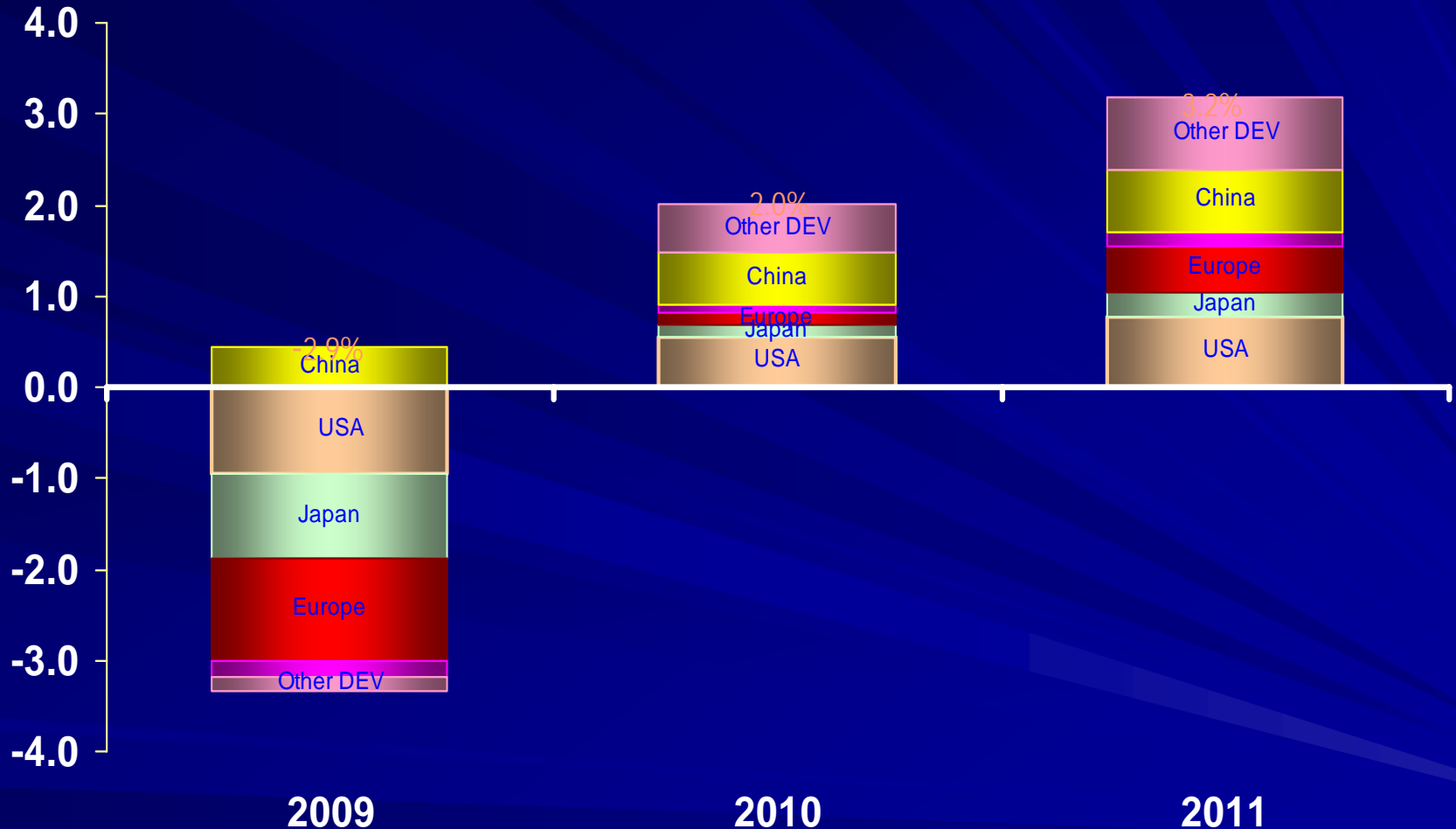
Source: JP Morgan, *World Financial Markets*, June 2009

Outlook? Recovery will probably begin later this year or early next year ... but strength is uncertain



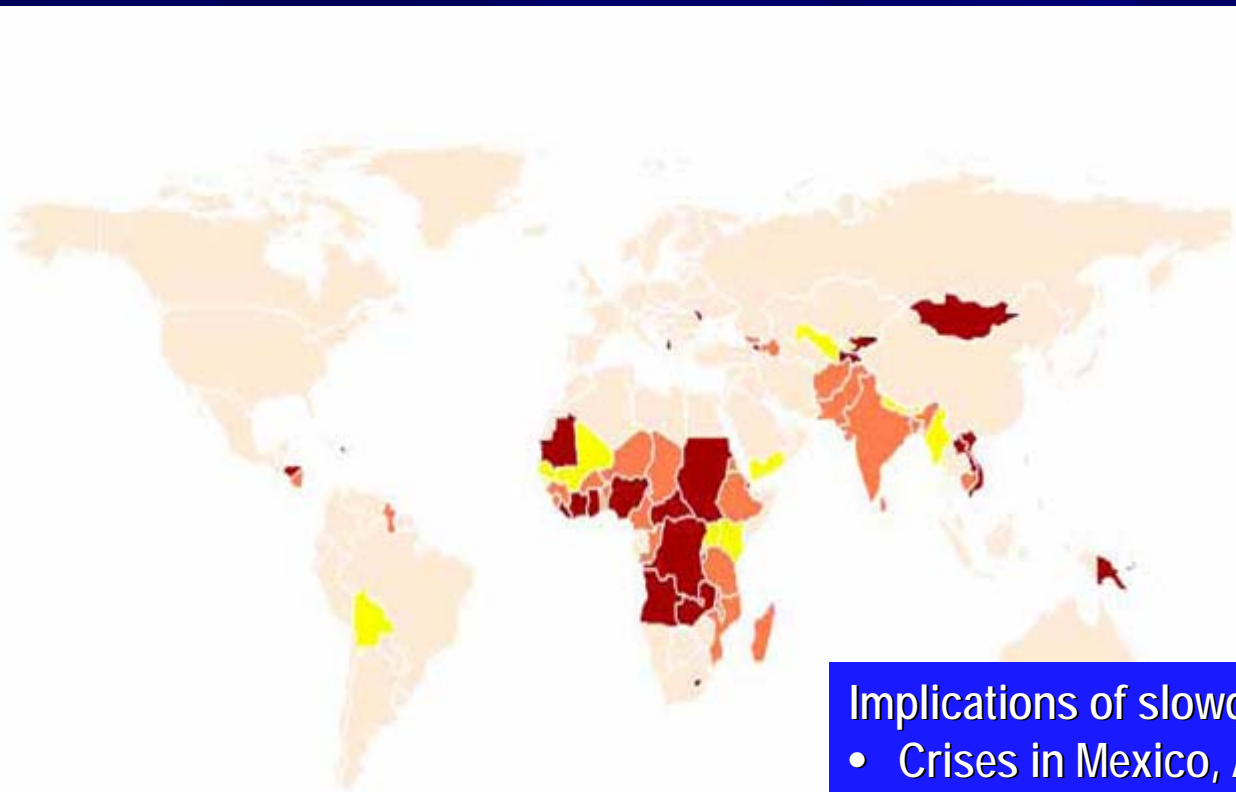
U.S., China and other developing countries lead upturn

contributions to global growth (percentage points)

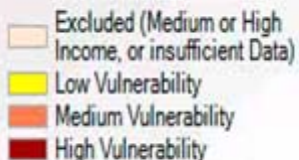


Shape of the coming recession depends on responding to several **daunting challenges...**

Daunting challenges: At-risk countries...



Overall Vulnerability Scores



Source: IMF, 2009

Those are at risk:

- export only a few commodities
- have large % in poverty
- have weak fiscal positions
- have low reserves/ high debt

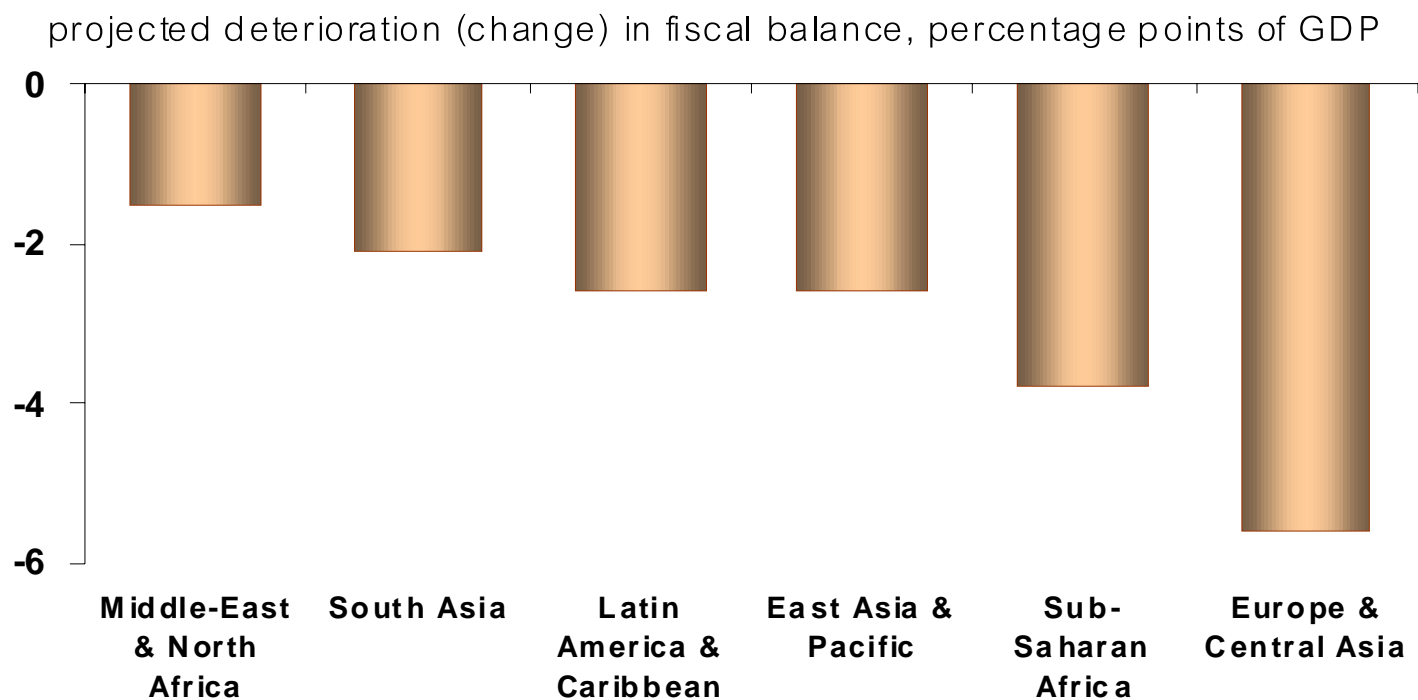
Implications of slowdown...

- Crises in Mexico, Argentina, and East Asia increased poverty dramatically
- 200 million likely to be trapped in poverty
- Infant mortality and child mortality rises – 200,000- 400,000 infants annually
- Cutbacks in health services

Daunting challenges: Providing support to workers and the poor

- Widening fiscal deficits will put pressures on **social safety nets**

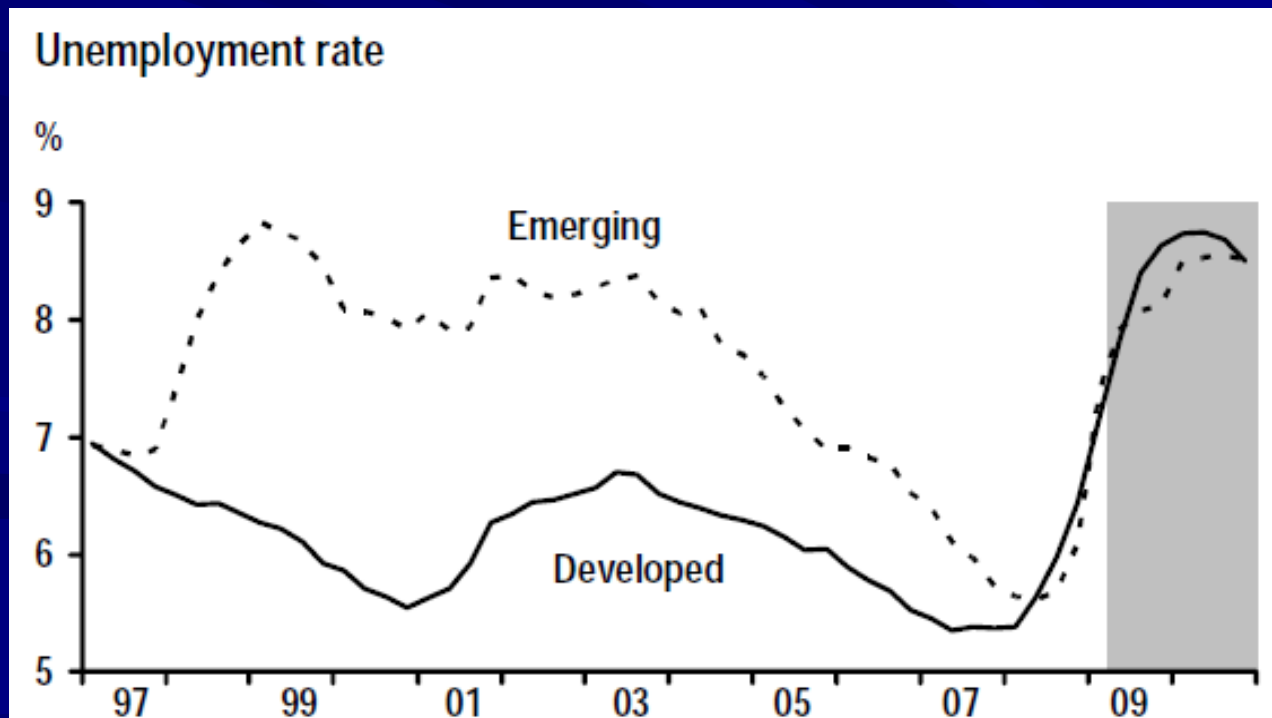
Fiscal deficits will widen sharply in 2009



Source: World Bank, DEC Prospects Group.

Daunting challenges: Providing support to workers and the poor

- Widening fiscal deficits will put pressures on **social safety nets**
- Poor households suffer declines in **remittances**
- ...and continued **higher food and fuel prices**
- Firms will face **tighter credit** conditions and weaker demand, so they will be slow to create new jobs... and **unemployment will rise**



Source: JP Morgan, *World Financial Markets*, June 2009

Multilateral collaboration is crucial... and the G20 leaders have begun the process...

G20 Summit
April 2



Agreed:

- Accelerated restructuring of banks and increased regulation
- Pledge to avoid protection
- Fiscal stimulus and expansive monetary policy
- Mobilization of more capital for developing countries
 - IMF – \$700- b. New arrangement to borrow (NAB)
 - World Bank MDBs – Capital increase for ADB
- Reform of the IMF and World Bank – Increased capital , new voting, merit selection of leaders

... but improving the multilateral response requires...

- Fulfilling pledges for development assistance
- Keeping global markets open and resisting pressures for trade protection – and renewing a commitment to the Doha Development agenda
- Improving regulation of financial markets will require careful balancing of national regulatory authorities with international cooperation
- Developing multilateral governance mechanisms to be more inclusive

Conclusion...

- Recovery is near, but its strength is in doubt and it will take many quarters to have full effect on incomes
- Meantime, assertive policy interventions are needed to protect core social spending and support households – and invest in reforms that will revive growth
- The G20 process has helped but much remains to be done – in keeping markets open, financial regulation, and providing adequate development assistance

Acknowledgements and Selected References

This presentation was prepared with inputs from Mansoor Dailami of DECPG , Pierella Paci of PREM, and Margaret Grosh of HDN

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