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Serious woes on global growth

GLOBAL ECONOMY

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The global economy is not doing well. The International Monetary Fund (IMF) just lowered its forecast for this year to 3.3 percent and to 3.6 percent for 2013. Experts reckon that even those rates may be optimistic. This is not good news. Growth is sorely needed in order to reduce unemployment and debt levels in developed countries and to continue shrinking poverty and expanding the middle class in emerging and developing economies. Europe remains a drag on the recovery.

The twin problems of persistently high unemployment and massive government debt levels in Europe, Japan and the United States are perhaps the most urgent to tackle. After two years of austerity measures, the macroeconomic picture in Europe continues to deteriorate. We have repeatedly called in the past for a shift in emphasis, as has the IMF. Surplus countries need to reactivate their economies to facilitate export-led growth in the heavily indebted peripheral countries. A moderately higher rate of inflation driven by higher wages and spending in the surplus economies would not only give the southern economies an opportunity to grow but also reduce their debt burden in real terms gradually over time. If inflation were to gather speed, the European Central Bank has many tools at its disposal to bring it under control. Price stability is not under threat but growth and employment are. Shifting policymaking to a growth agenda, as the IMF recommends, would also facilitate addressing the problems in the banking sector, saddled as it is with bad loans.

In the United States all eyes and ears are focused on the outcome of the November election. The two competing candidates advocate starkly different ways to cut the deficit and reduce debt. The rest of the world is watching and wondering which of the two strategies will yield faster results and make a greater contribution to global growth. In any event, the United States is no longer the global locomotive that it once was. In fact, it is an economy in dire need of rebalancing when it comes to its economic and financial relationships with the rest of the world. If anything, we should expect lower U.S. imports and higher exports in the medium run.

Given the limited positive growth impact that either Europe or the United States can have on the global economy, our best hopes lie with the emerging economies. China’s plan for a new, if modest, fiscal stimulus program is welcome news, especially for Japan, which benefits from Chinese domestic growth thanks to its exports of capital goods and high value-added components. But the jury is still out as to whether the world’s second-largest economy will manage to reverse the downward trend in its rate of economic growth. Political tensions between the two countries are not facilitating growth in the region.

Another source of uncertainty is India. Reforms have stalled and so has economic growth. While the Indian economy’s impact on global growth is relatively modest, every bit of growth around the world counts. Brazil is perhaps the largest emerging economy that has taken the sharpest turn for the worst. Growth has stalled and the global slowdown threatens commodity prices, which could bring down the country’s stellar economic performance over the last decade and a half.

The global slowdown also creates unwanted problems on the trade front. Countries around the world are reluctant to stimulate their domestic economies and are thus intent on increasing their exports. Volatility in currency markets is high, and many experts expect currency friction, or even wars, to be the norm for the next decade or two. The specter of protectionism looms larger and larger when growth rates slow down.

As we have argued in our book “Global Turning Points,” the global economy is lacking leadership from the largest countries. Coordinated action is required more than ever to lay the foundations for sustained growth. Let us hope that the spirit of global consultation, collaboration and concerted action returns after the U.S. election and the leadership transition in China.

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