



FINANCIAL
TIMES

**Challenges and threats in the
world economy** **Martin Wolf, Associate
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Financial Times

Fundacion Rafael del Pino

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Madrid

Challenges and threats in the world economy

- Glimmering hope
- Uncertain legacy
- What can go right
- What can go wrong
- Conclusion

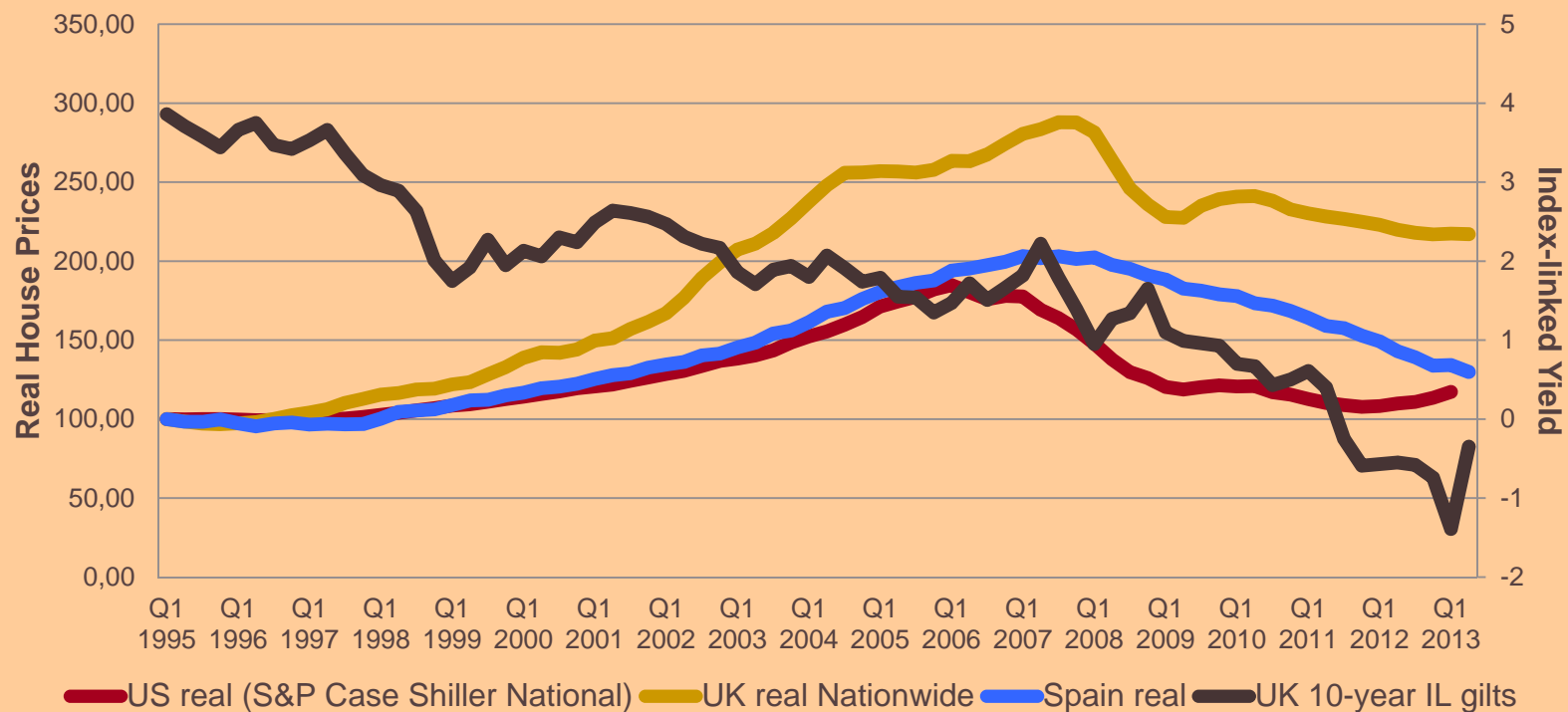
1. Glimmers of hope

- Forecasters imagine recovery
- Stress falls in crisis-hit regions
- Stability re-emerges

1. Glimmers of hope: house price corrections

HOUSING CORRECTION

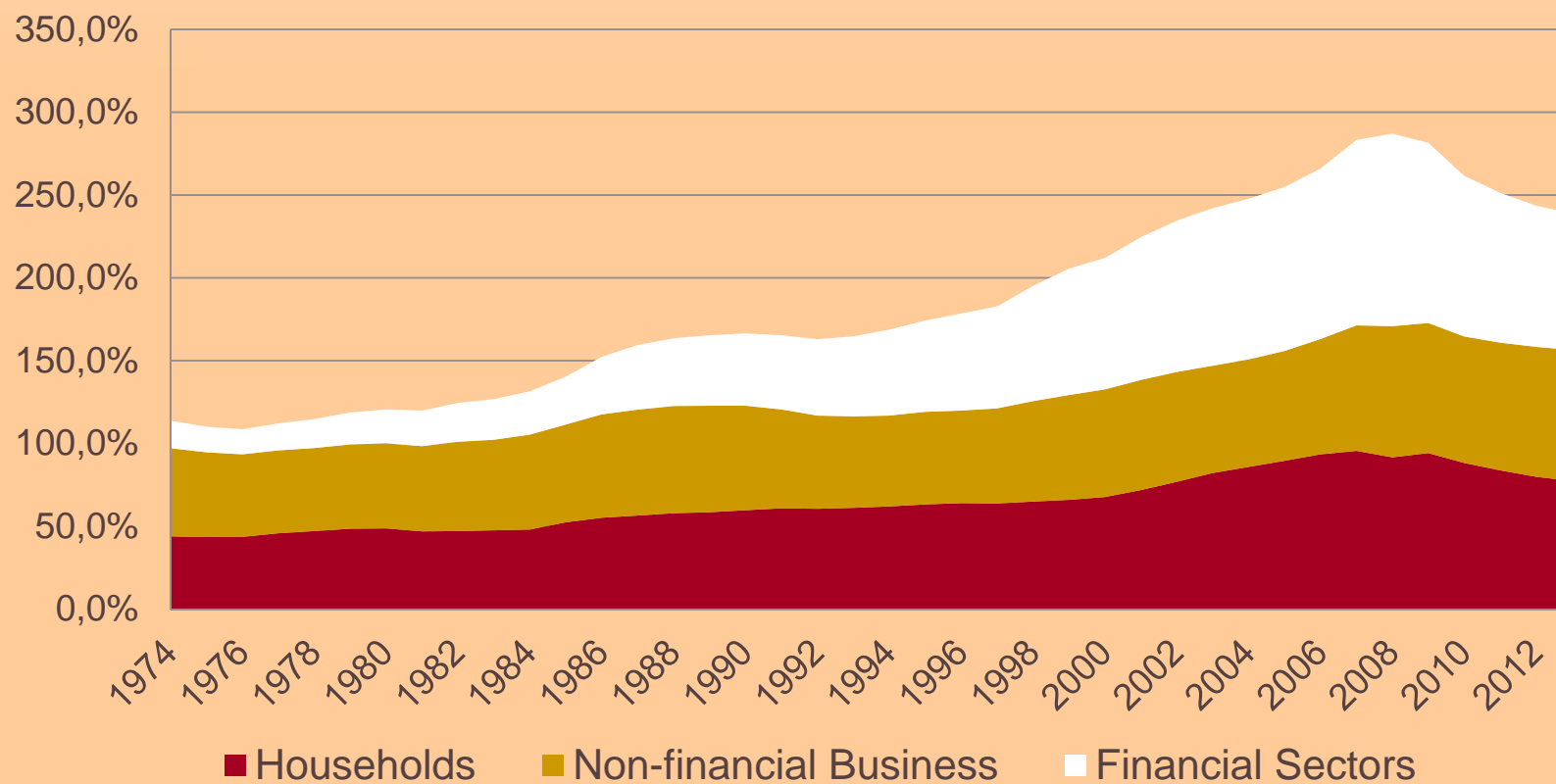
REAL HOUSE PRICES AND REAL INDEX-LINKED YIELDS



1. Glimmers of hope: deleveraging

DELEVERAGING APACE

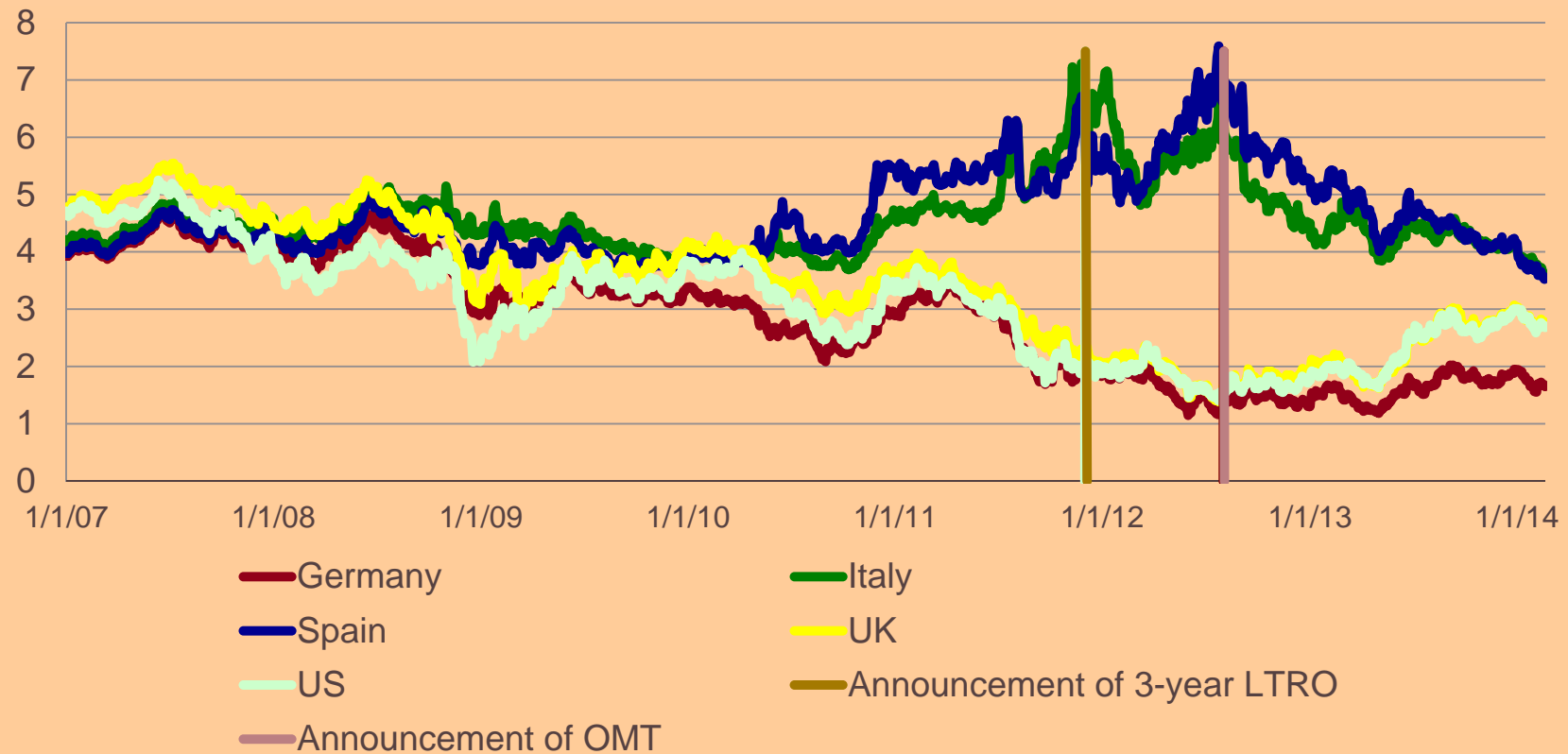
US PRIVATE SECTOR DEBT OVER GDP



1. Glimmers of hope: end of panic

END OF THE PANIC

10-YEAR BOND YIELDS



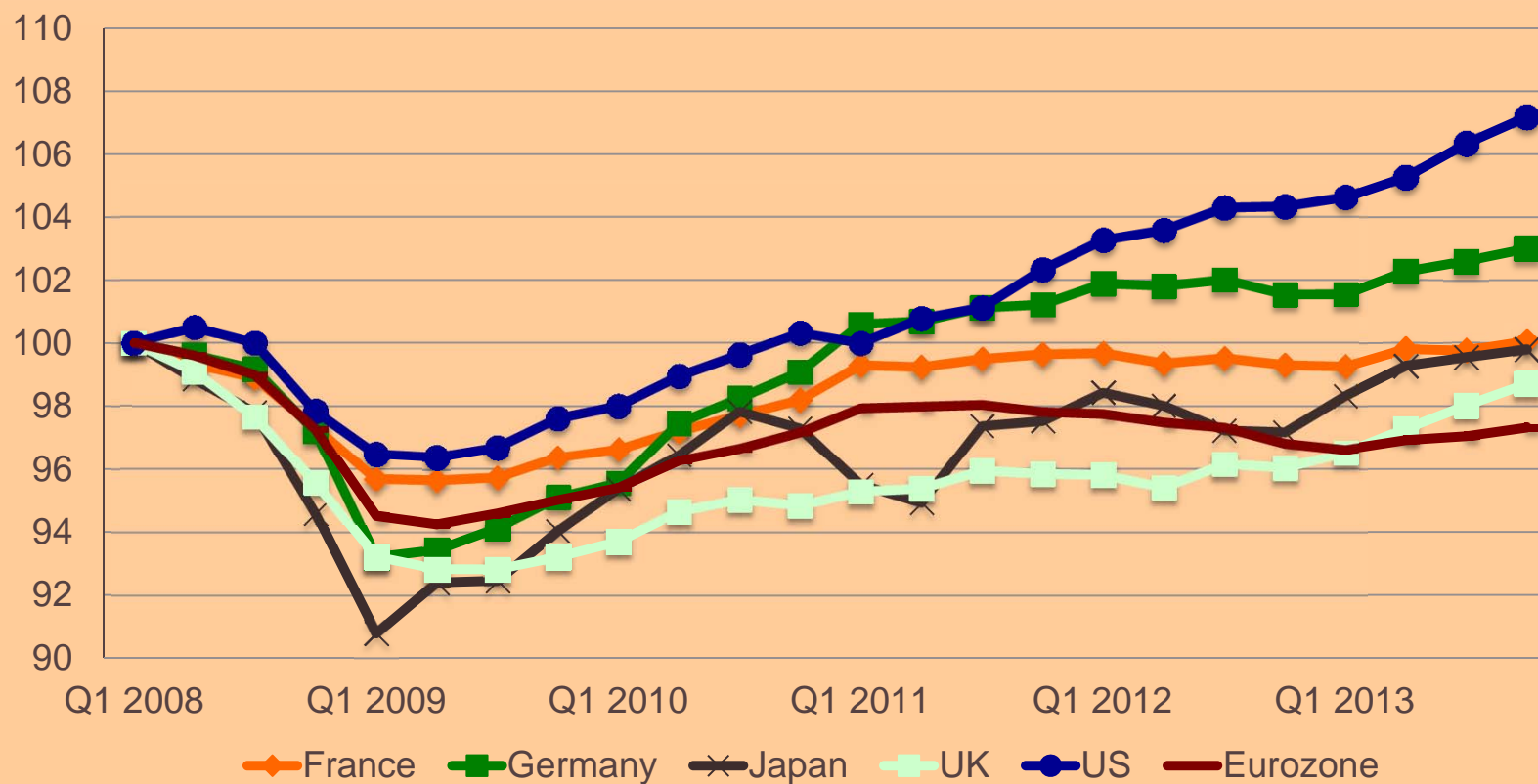
2. Uncertain legacy

- Abnormal policy
- Huge losses
- Deflationary pressure

2. Uncertain legacy: long slump

AND A WEAK RECOVERY FROM A DEEP SLUMP

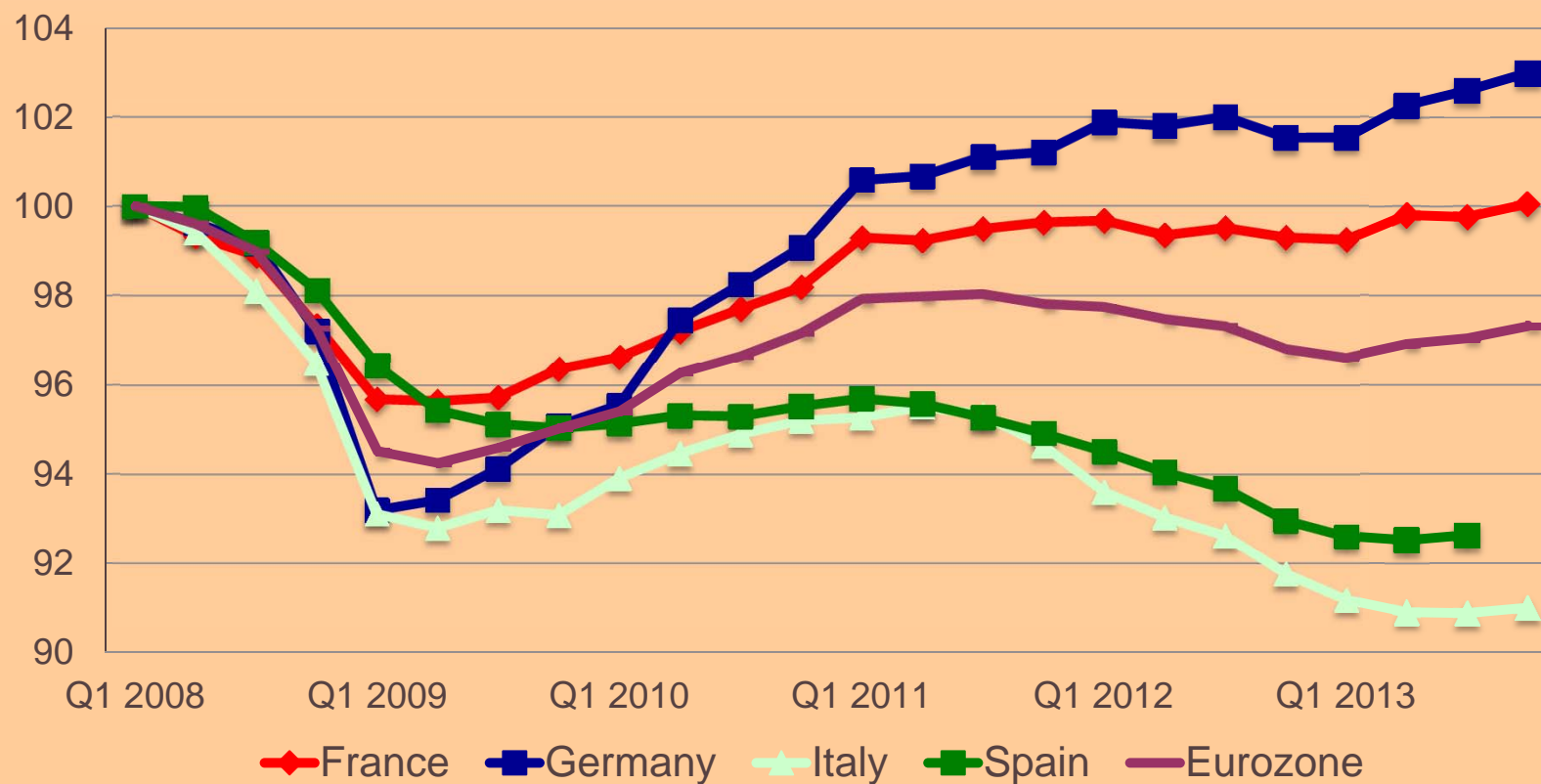
GDP IN THE CRISIS



2. Uncertain legacy: long slump

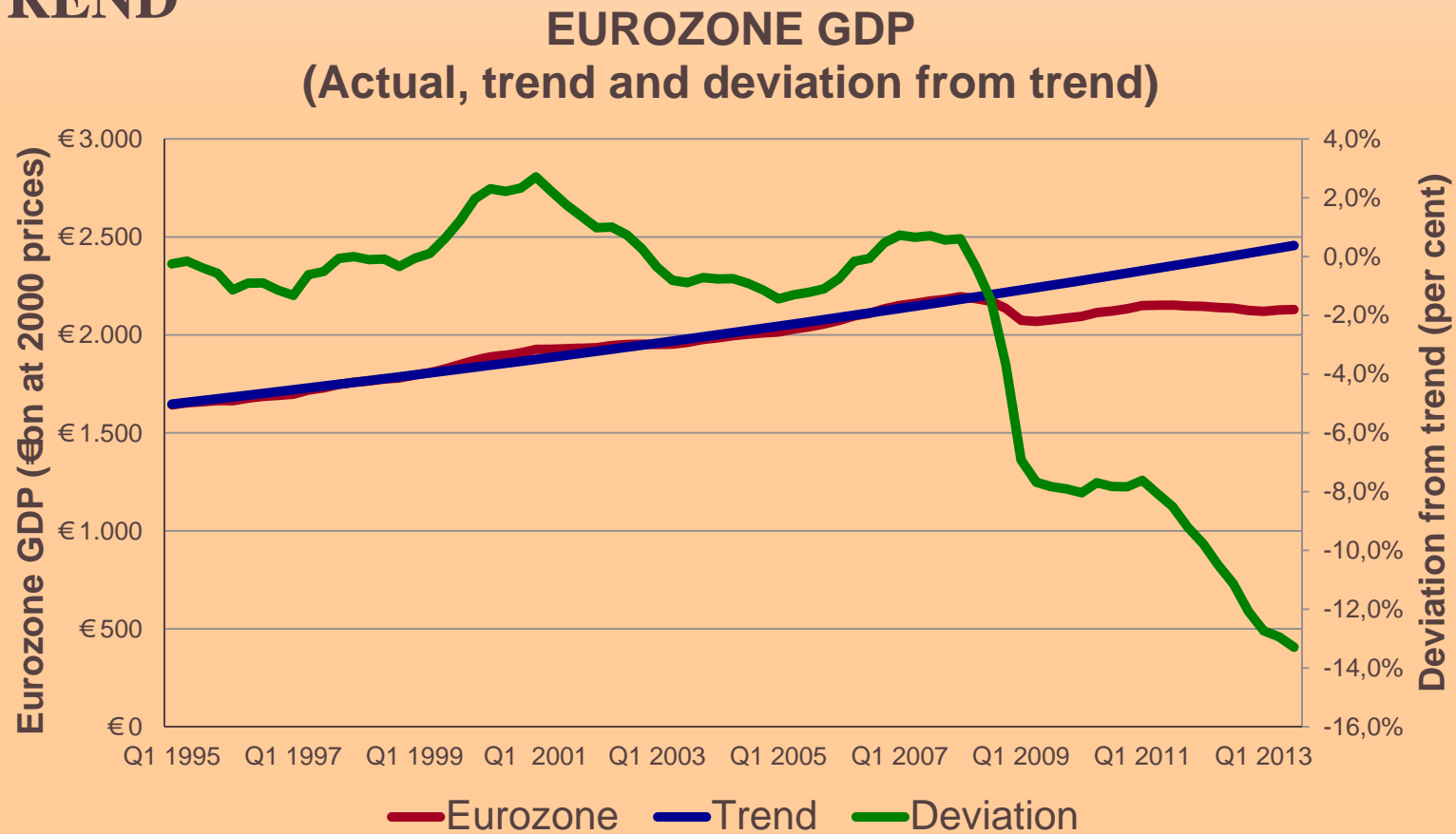
PARTICULARLY IN THE EUROZONE

GDP IN THE EUROZONE CRISIS



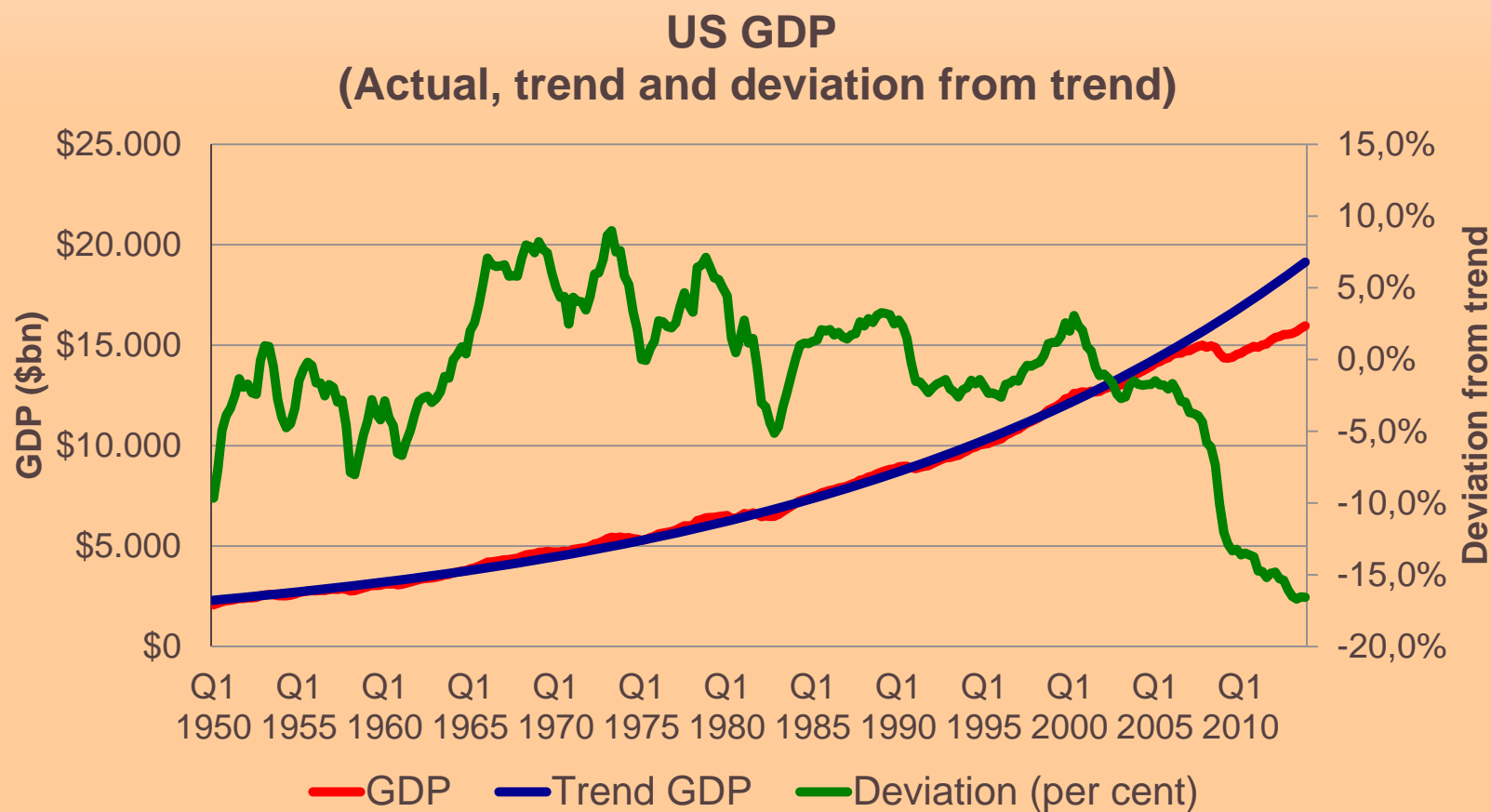
2. Uncertain legacy: lost growth

OUTPUT IS VASTLY BELOW THE PRE-CRISIS TREND



2. Uncertain legacy: lost growth

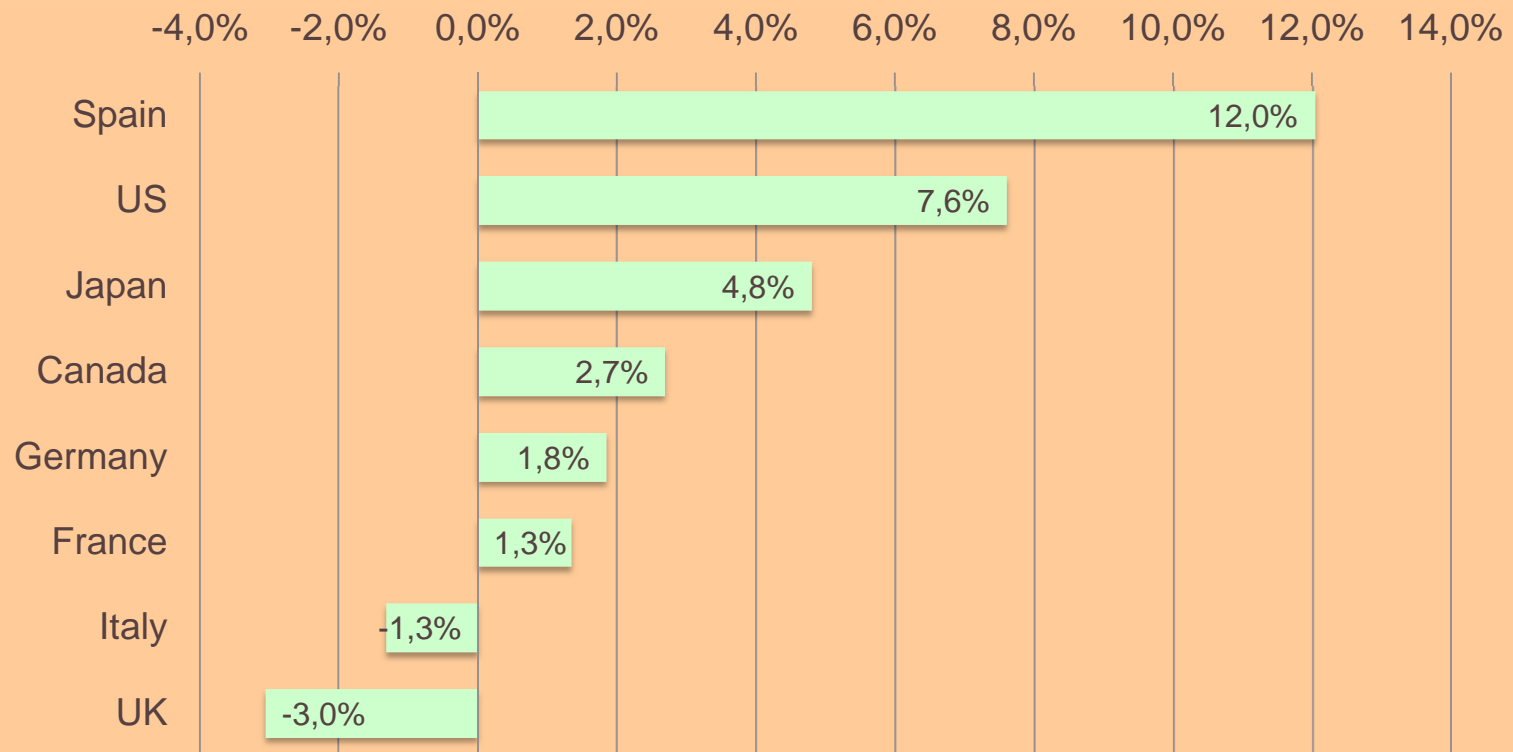
IN THE US IT IS LOOKING LIKE A NEW ERA



2. Uncertain legacy: lost growth

THE PRODUCTIVITY DIVERGENCE

CHANGE IN GDP PER HOUR WORKED 2007-13
(Source: Conference Board)



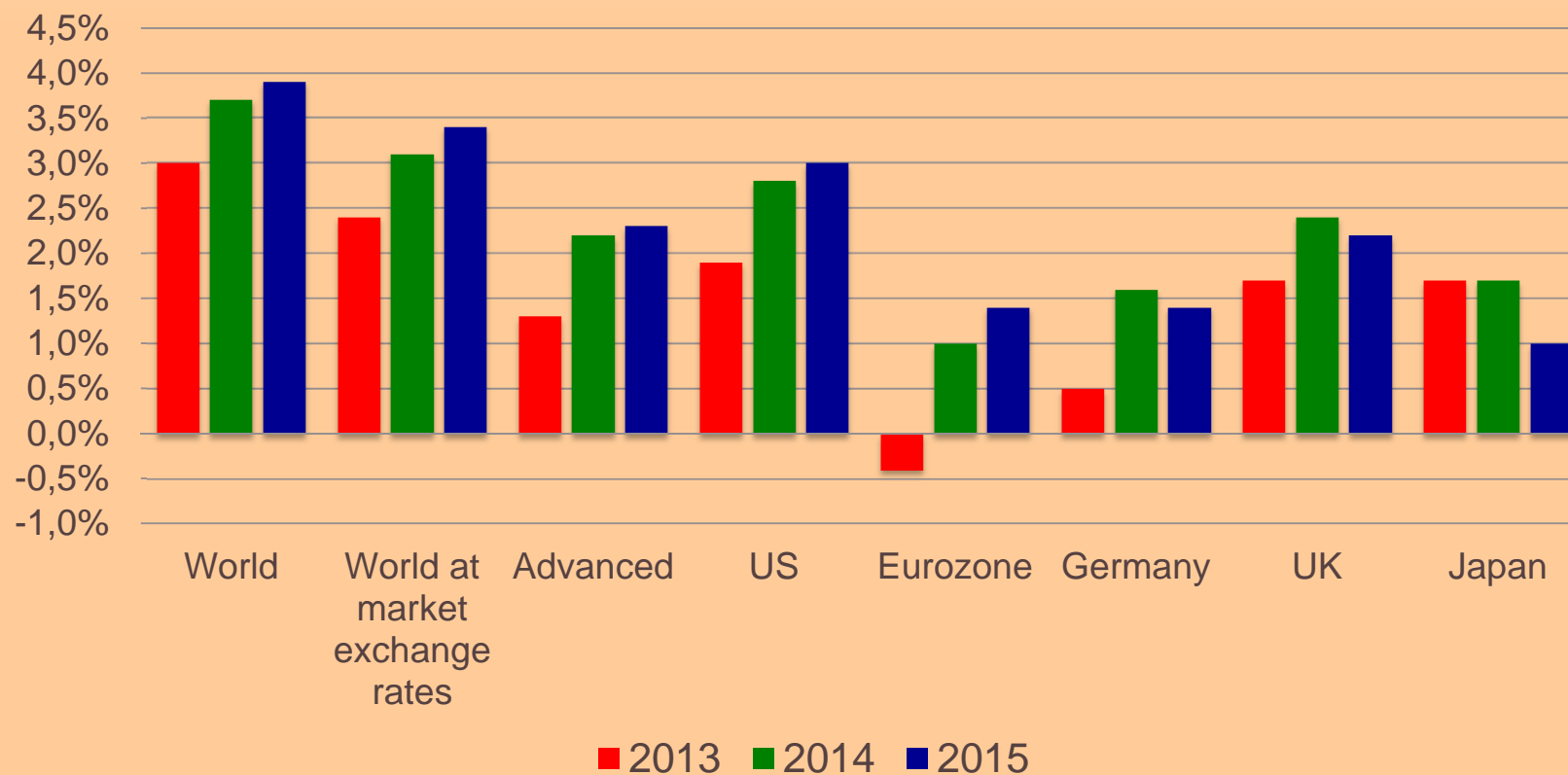
3. What can go right

- Post-crisis healing is well under way
- Globalisation continues.
- Emerging economies still have potential.
- New technologies are unfolding.
- US energy revolution is under way.

3. What can go right

RECOVERY EXPECTED

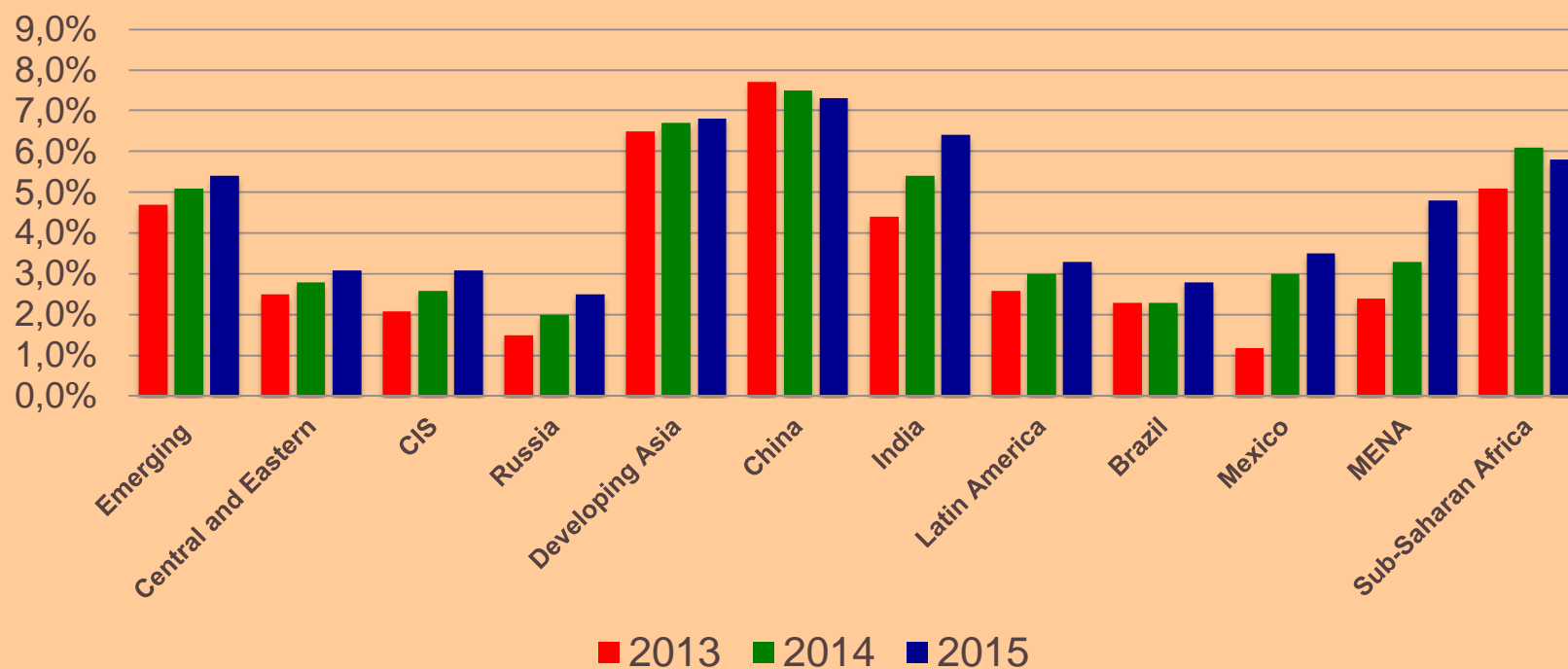
IMF FORECASTS (January 2014)



3. What can go right

RECOVERY EXPECTED

IMF FORECASTS FOR EMERGING AND DEVELOPING COUNTRIES (January 2014)



3. What can go right: US energy

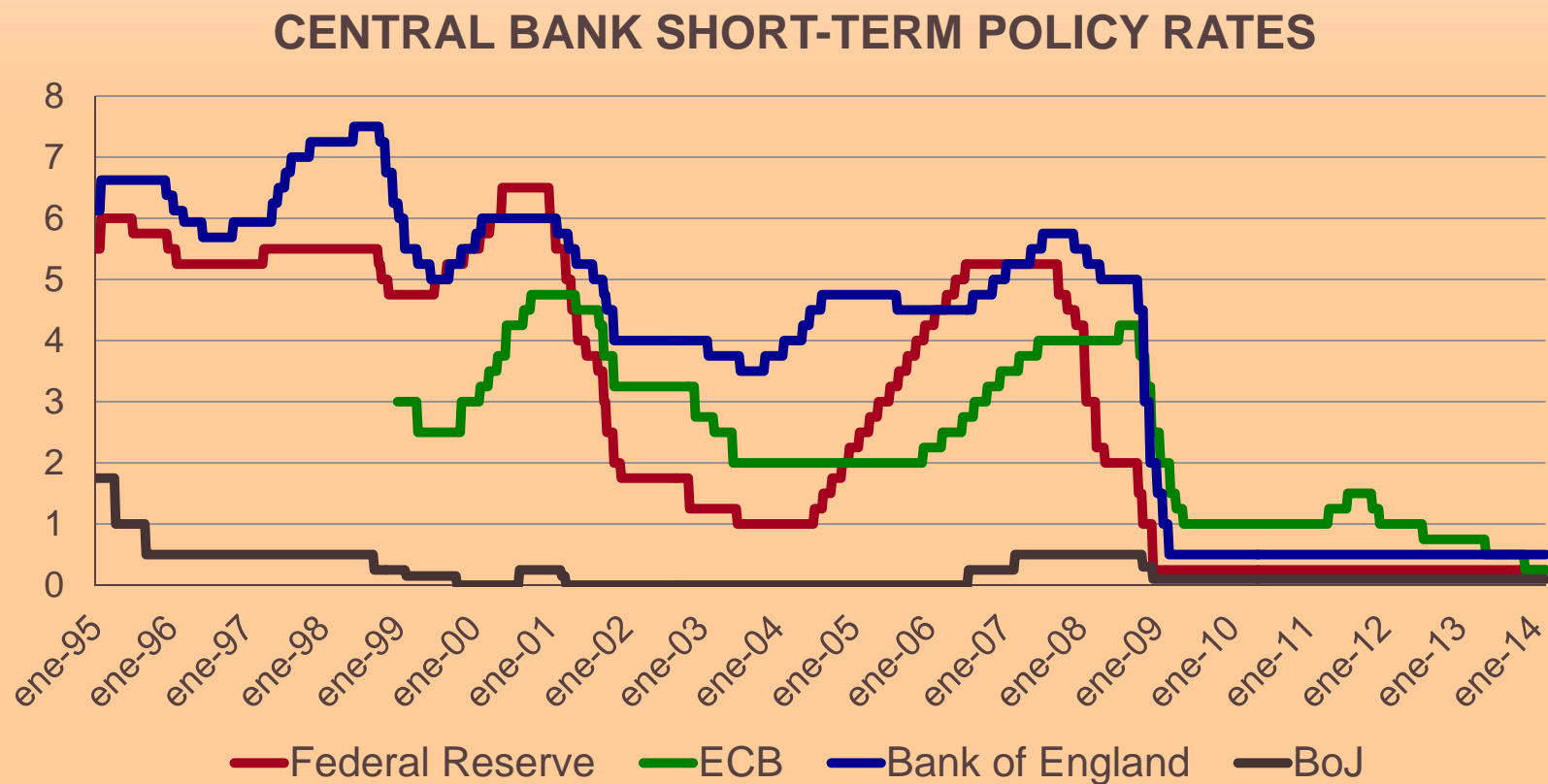
- US energy revolution:
- “European gas import prices are currently around three times higher than in the US while industrial electricity prices are about twice as high, creating an energy price gap Dr Fatih Birol (chief economist of the International Energy Agency) said would last “at least 20 years”. Financial Times, 29th January 2014.

4. What can go wrong

- Secular stagnation continues.
- Technology is a squib.
- Normalisation shock worsens.
- China's growth collapses
- Geo-political risk turns into actuality.

4. What can go wrong: secular stagnation

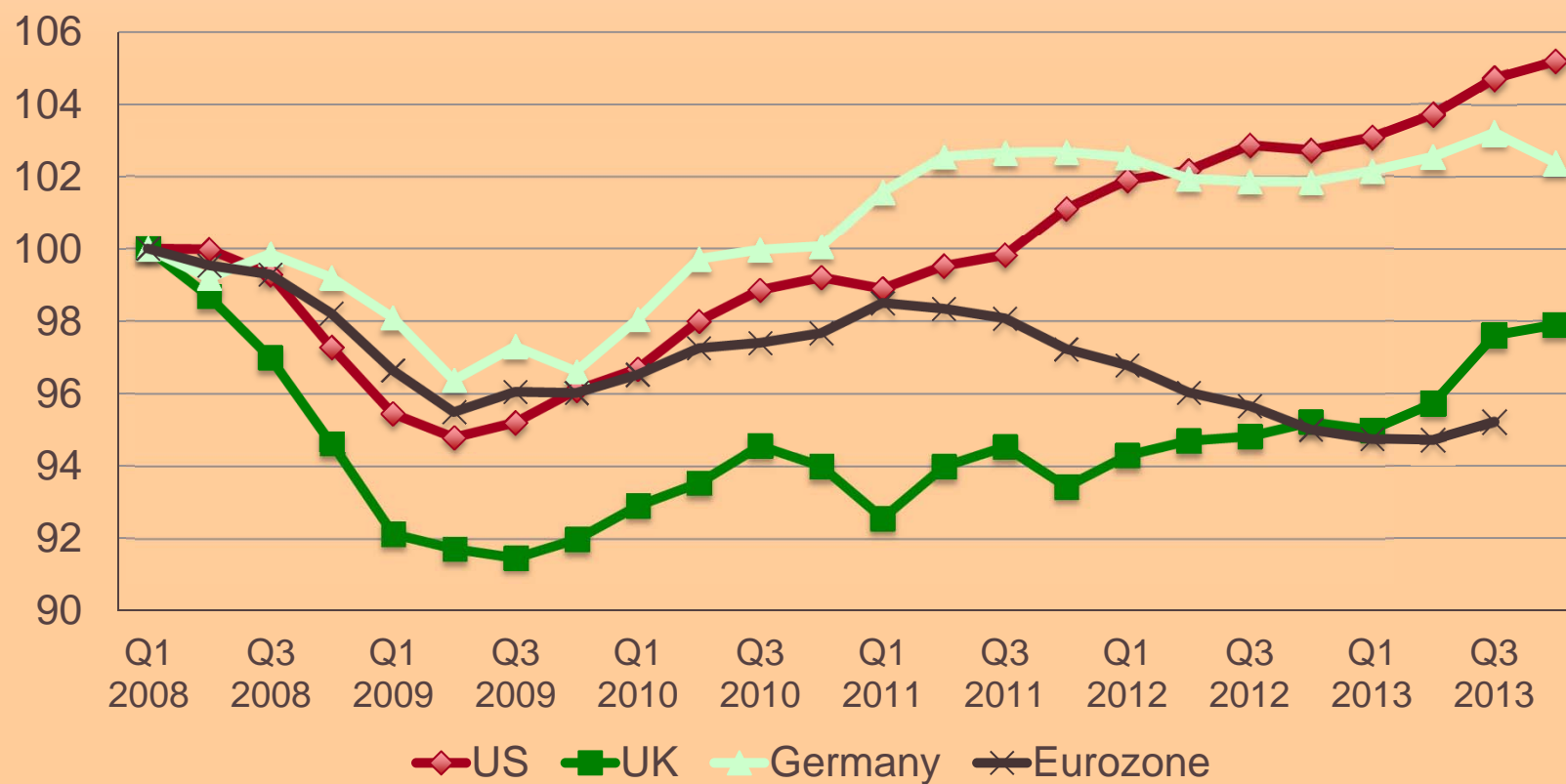
BUT IT IS STILL A WORLD OF FREE MONEY



4. What can go wrong: secular stagnation

WEAK DEMAND

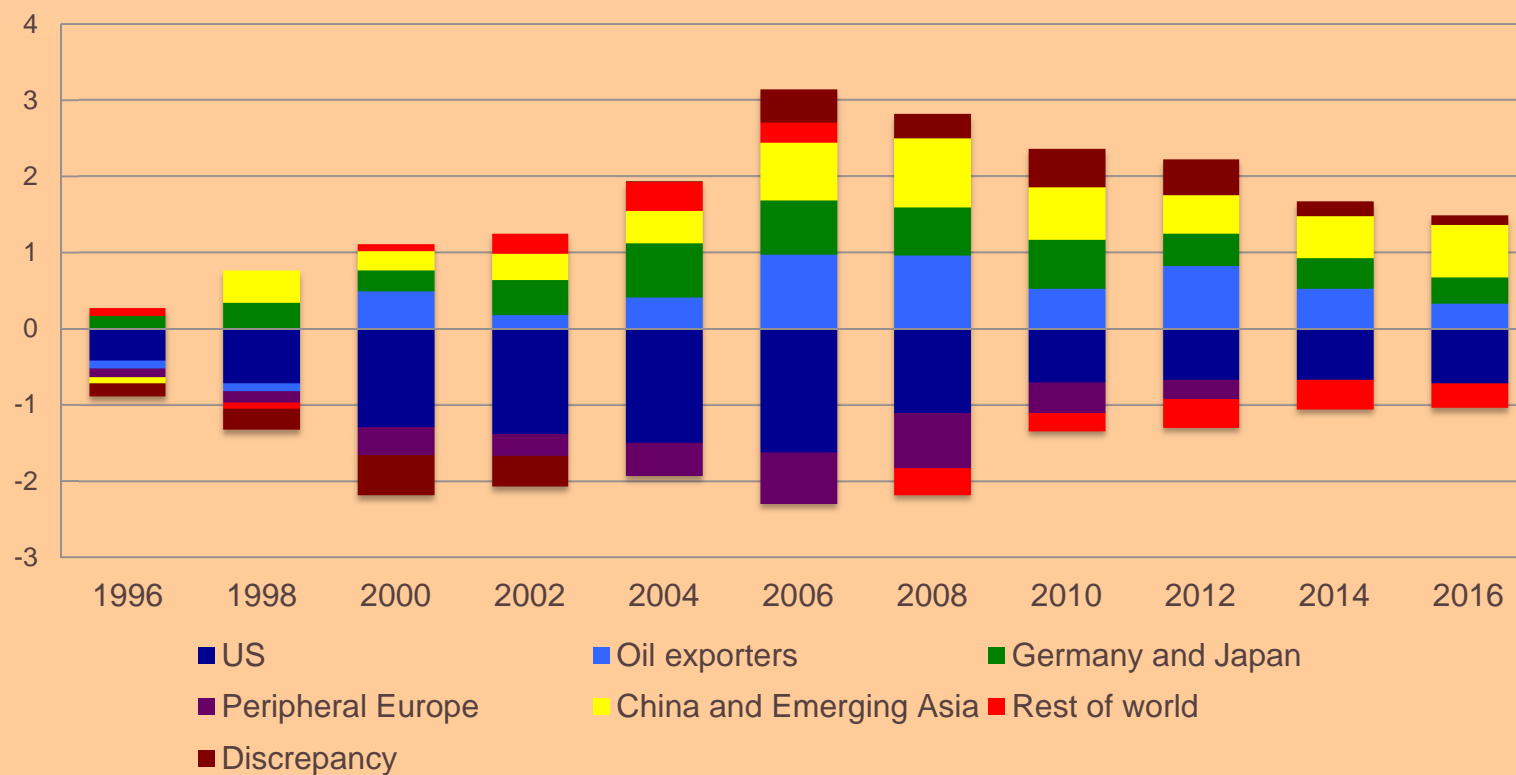
REAL DOMESTIC DEMAND IN THE CRISIS



4. What can go wrong: imbalances

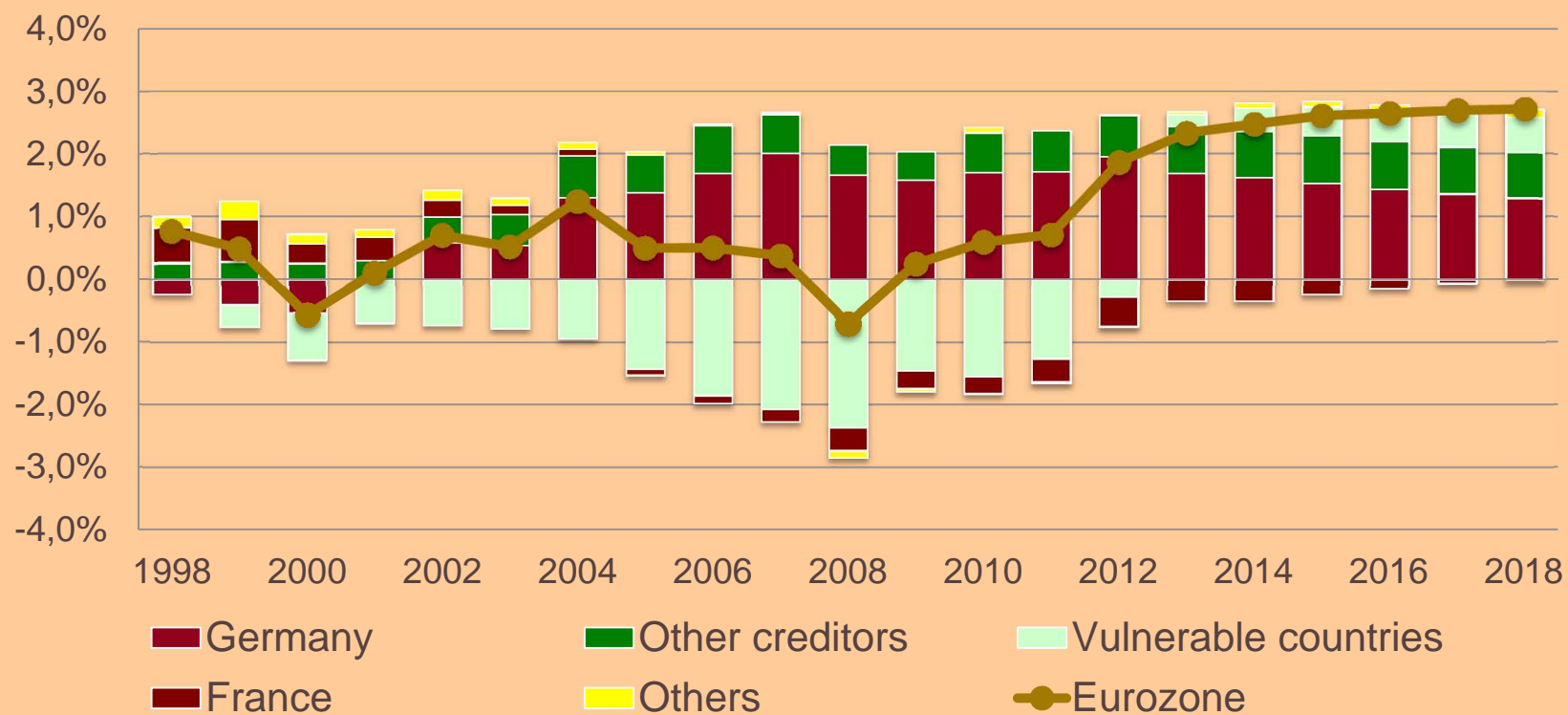
WHERE EXCESS SAVINGS CAME FROM

GLOBAL IMBALANCES (as per cent of world GDP)



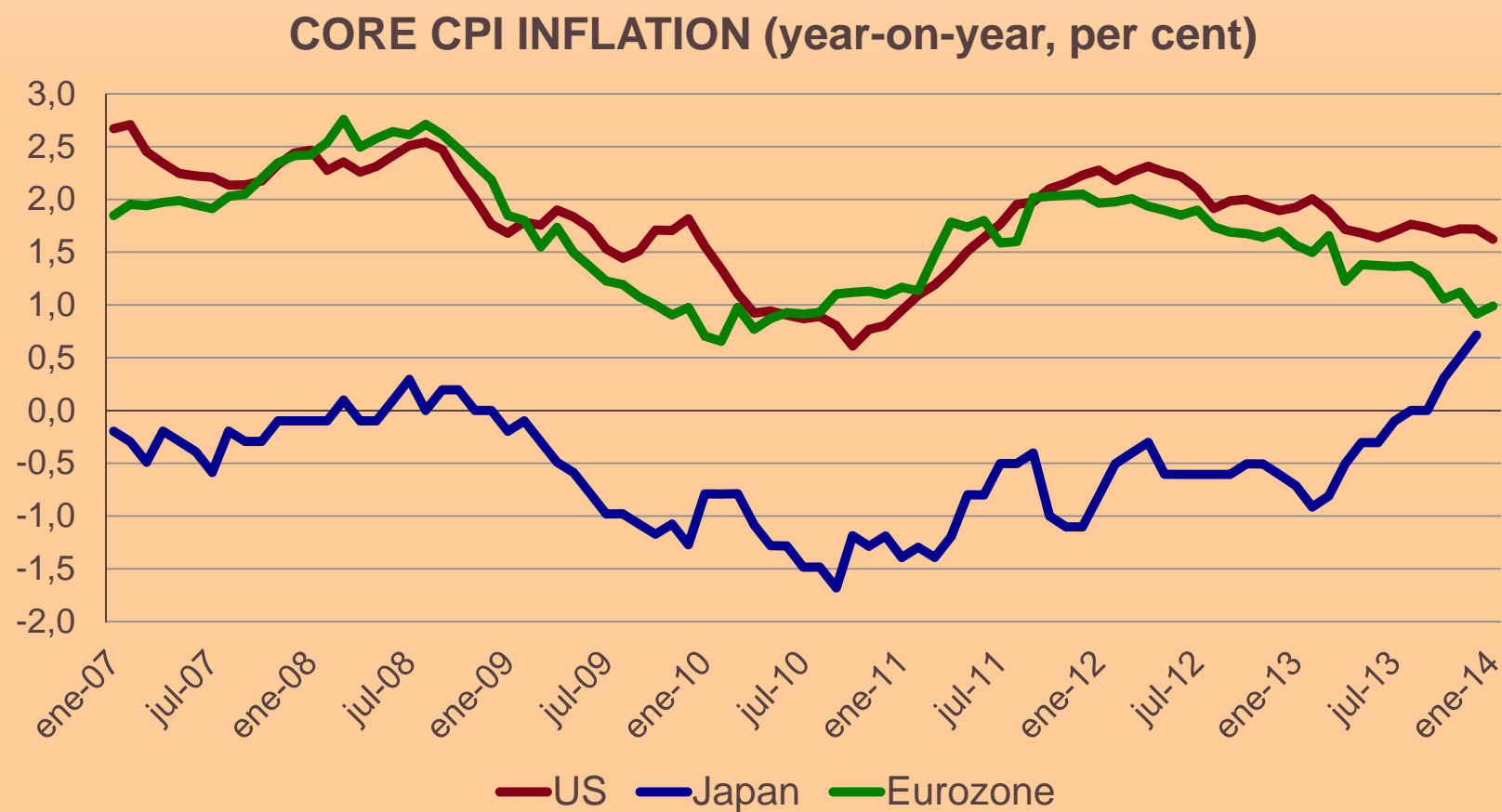
1. Glimmers of hope: imbalances

WHERE EXCESS SAVINGS CAME FROM EUROZONE IMBALANCES ON CURRENT ACCOUNT (as per cent of Eurozone GDP)



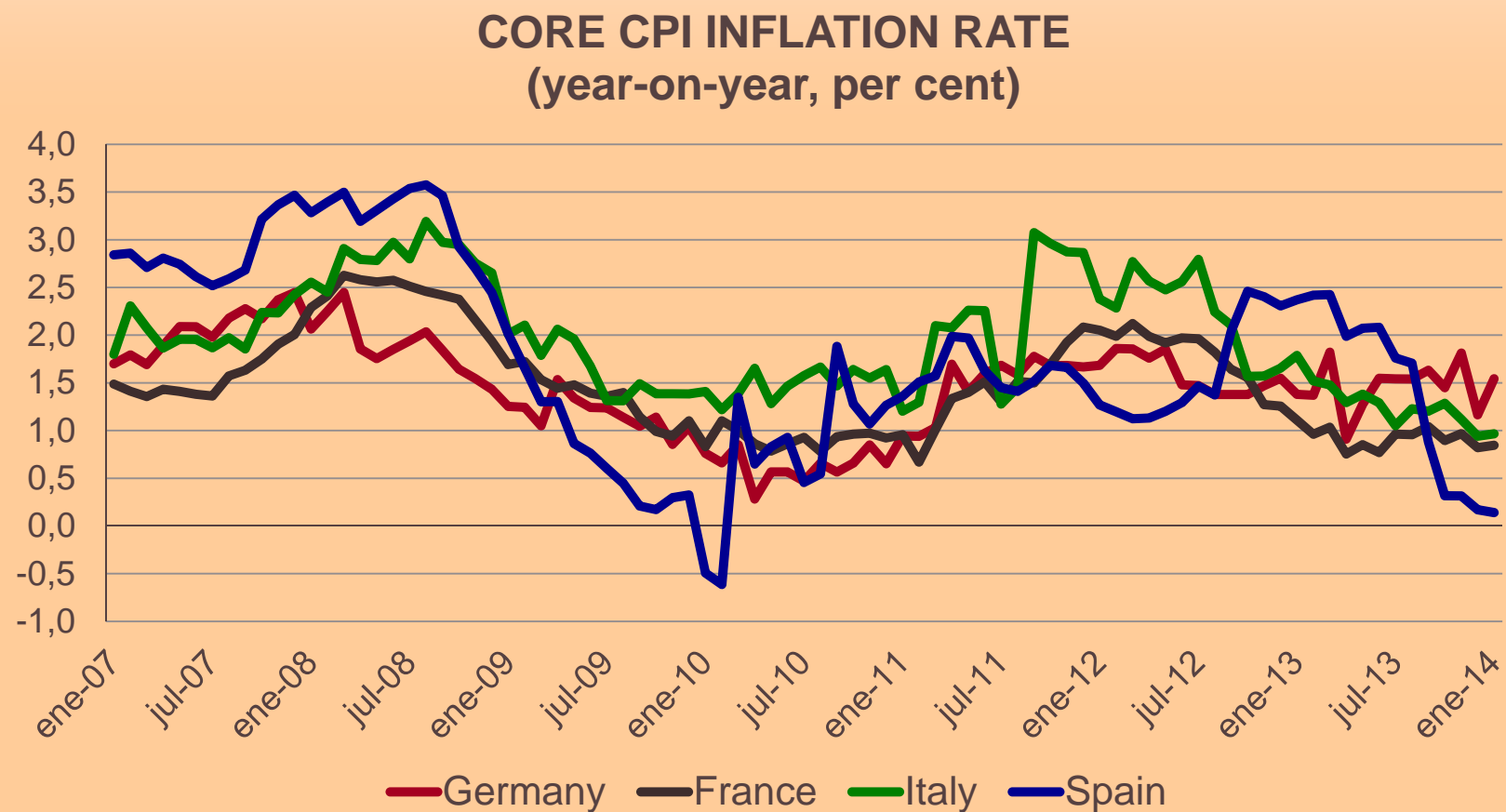
4. What can go wrong: deflation

CORE INFLATION IS LOW AND FALLING



4. What can go wrong: deflation

IN EUROZONE LOW INFLATION IS A HUGE THREAT



4. What can go wrong: normalisation

TAPER TANTRUM

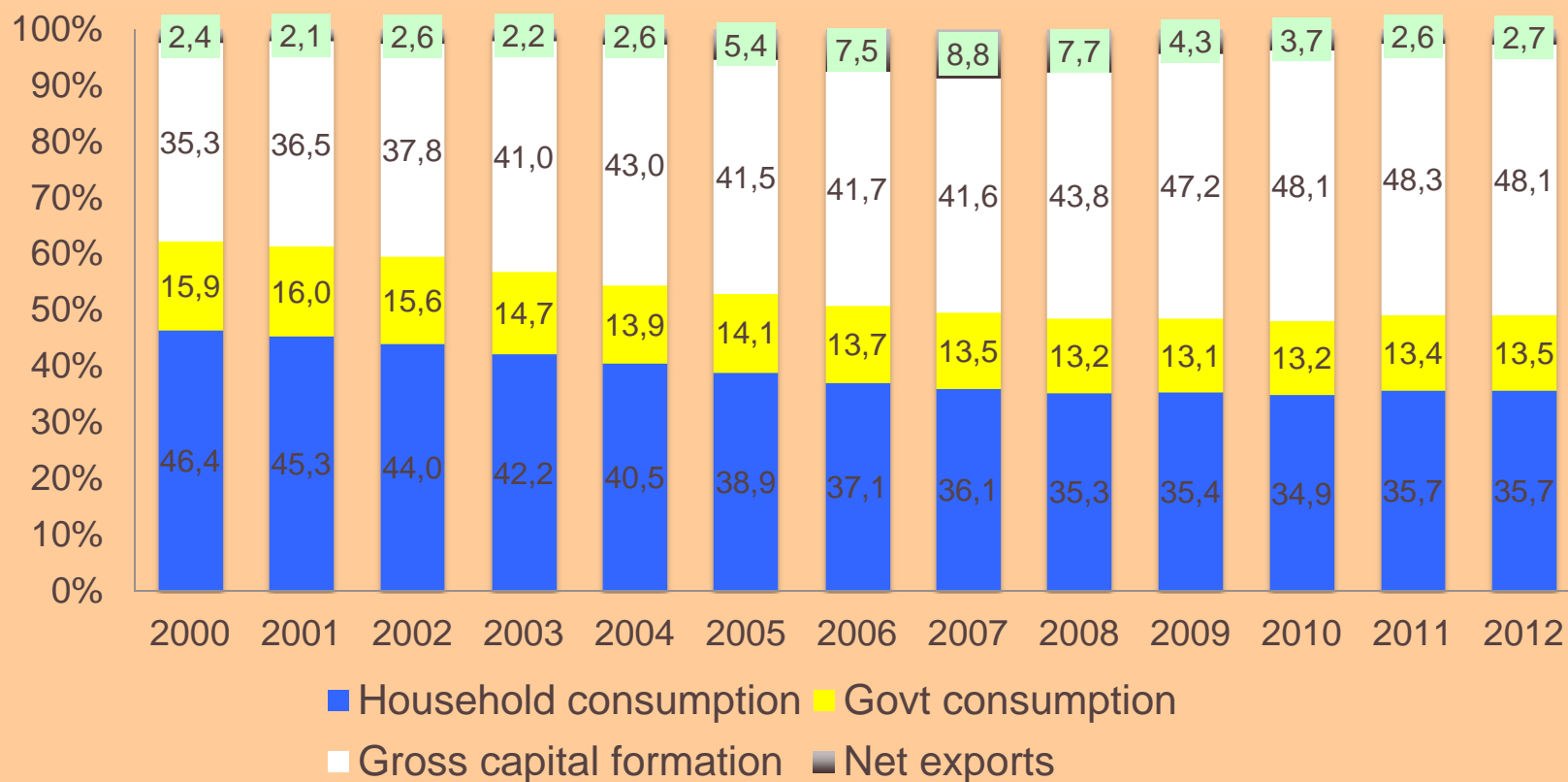
CAPITAL FLOWS TO EMERGING ECONOMIES (\$bn)
(source: IMF World Economic Outlook database)



4. What can go wrong: China

THE UNBALANCED ECONOMY

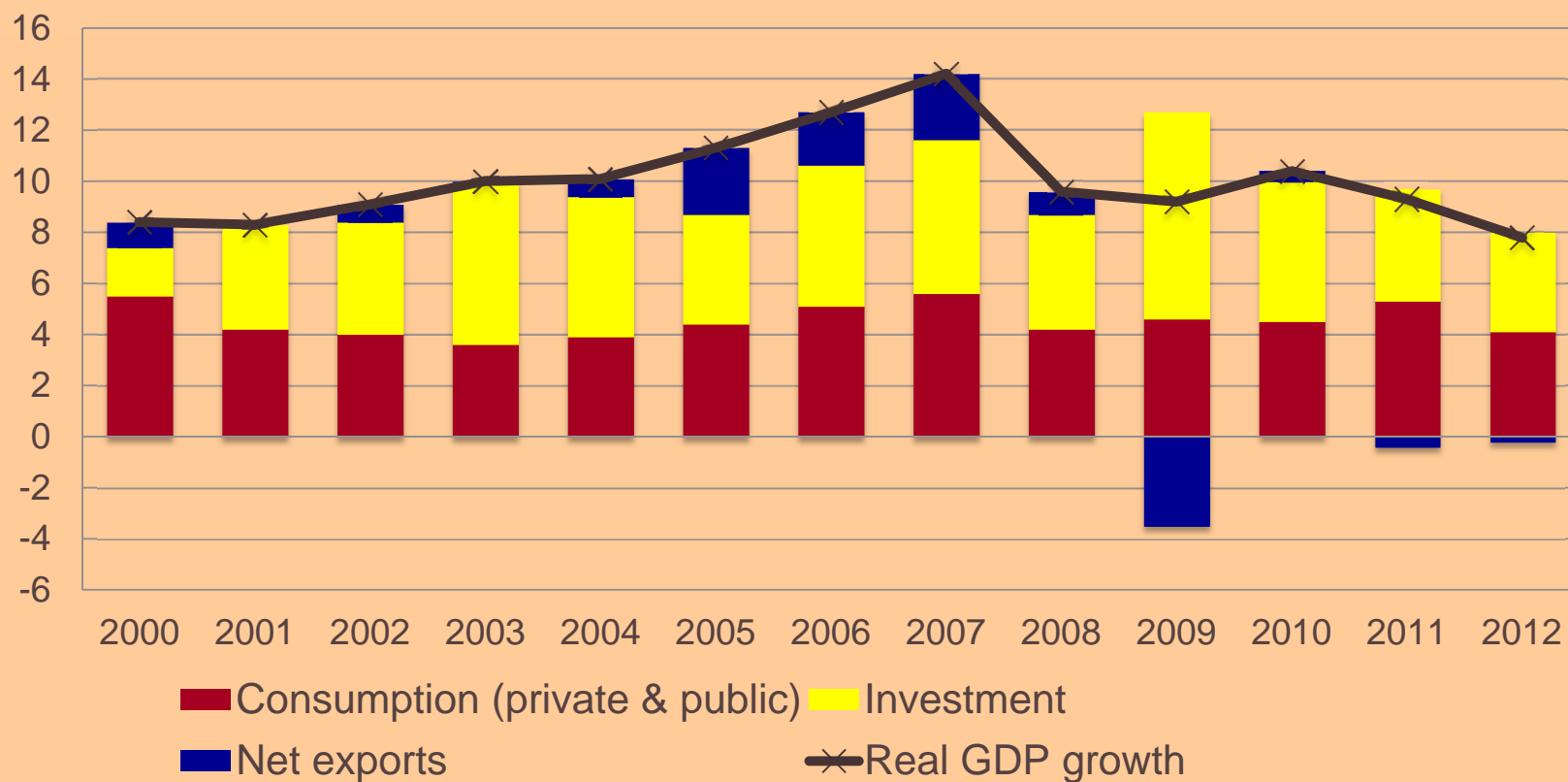
STRUCTURE OF CHINA'S DEMAND



4. What can go wrong: China

THE UNBALANCED ECONOMY

DEMAND CONTRIBUTIONS TO CHINESE GDP GROWTH



4 What can go wrong: geopolitics

- Here is a disturbing list:
 - Japan-China;
 - Iran;
 - Ukraine;
 - Middle East;
 - Terrorism.
 - Anything else

5. Conclusion

- There is room for hope:
 - The US might do quite well;
 - The eurozone might heal;
 - China might continue to grow fast;
 - And normalisation might work smoothly.
- Yet big uncertainties and risks exist:
 - Uncertainty over growth potential;
 - Risks over economics and politics.