



Economic outlook: Global divergent trends

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Divergent macro trends

1. Global trends

a) Growth divergence appears to be more structural

- a) Growth potential in EM remains sound thanks to demographic trends, rising investment and lower dependence on foreign capital
- b) Advanced economies have to cope with lower growth, higher unemployment and deleveraging (public and/or private)

b) Higher commodity prices lead to inflationary pressures in EM

- a) Poorer developing countries are most fragile

c) Interest rates and fx appreciation trends are focusing flows toward EM

- a) Risk of bubbles: may be at an early stage.

2. Focus on Central and Eastern Europe:

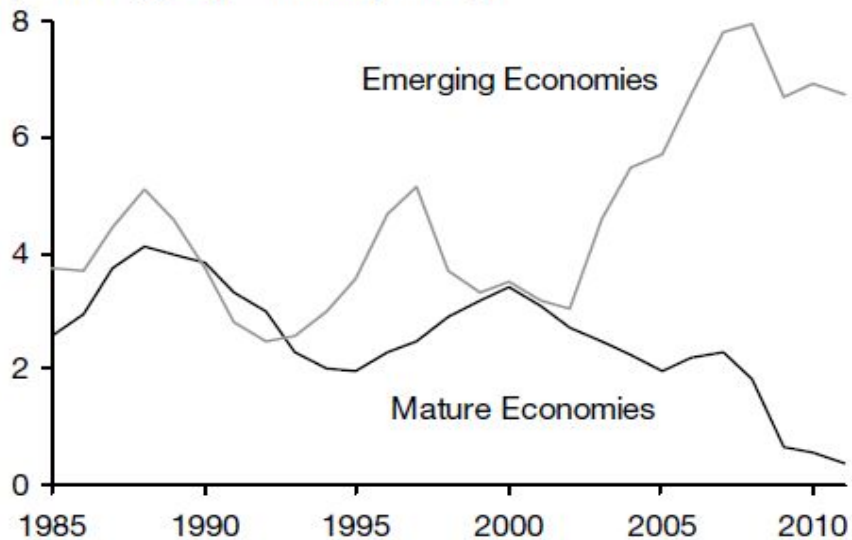
- a) The most painful phase of the adjustment seems behind
- b) An export-led recovery to be gradually replaced by domestic demand
- c) Markets have well discriminated between CEE countries and euro periphery.



The « new normal »: divergent macro trends

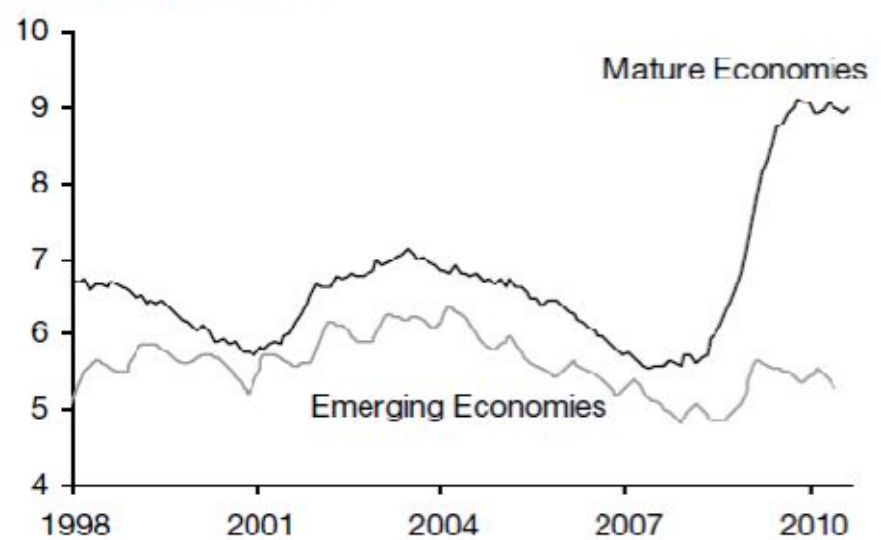
Global Domestic Demand

percent y/y, 5-year moving average



Global Unemployment Rates

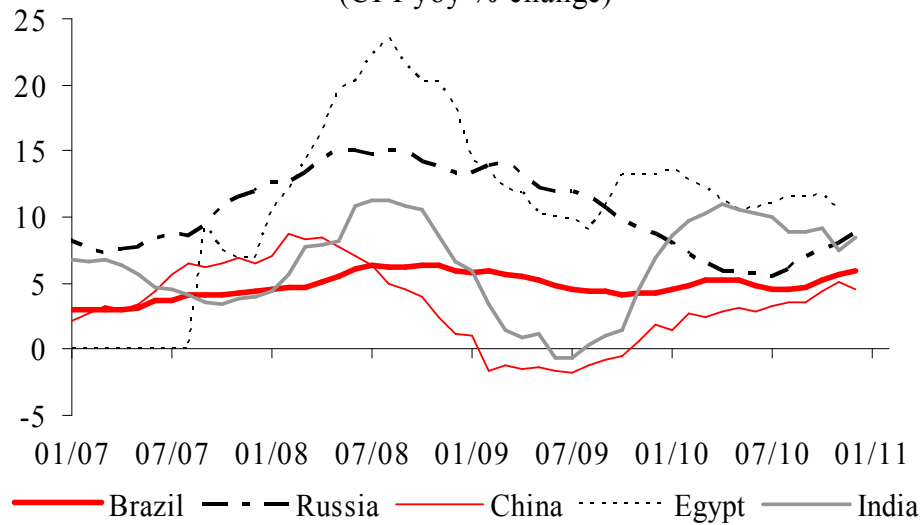
percent of labor force



Rising inflationary pressures

Emerging markets

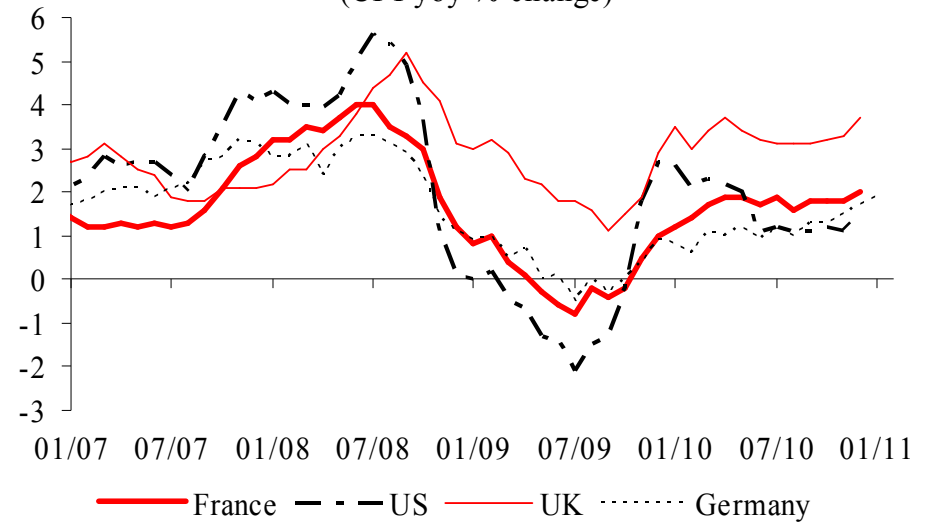
(CPI yoy % change)



source: Bloomberg

Developped markets

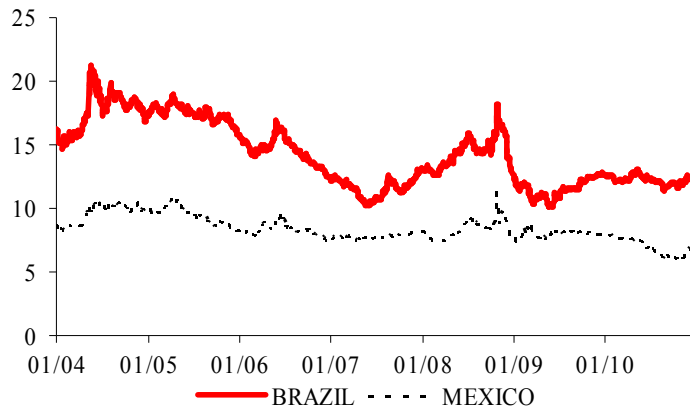
(CPI yoy % change)



source: Bloomberg

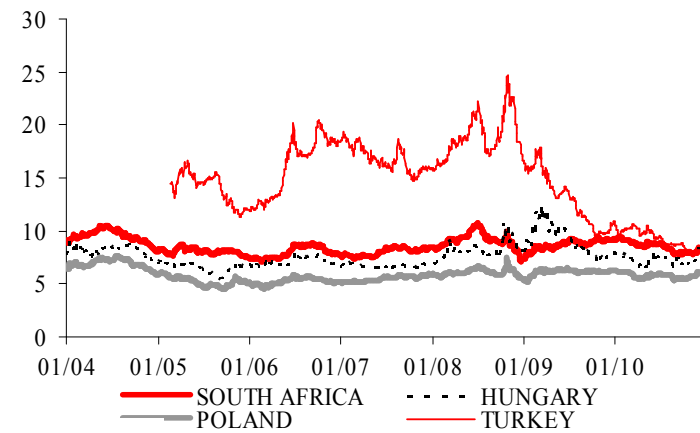
Interest Rate differentials to persist

Long term rates



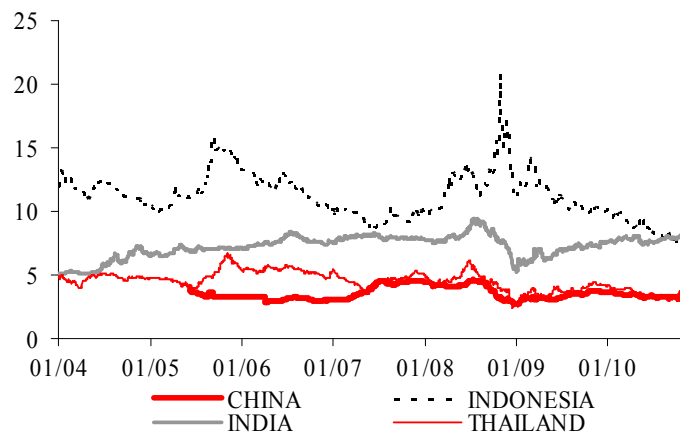
Source: Bloomberg

Long term rates



Source: Bloomberg

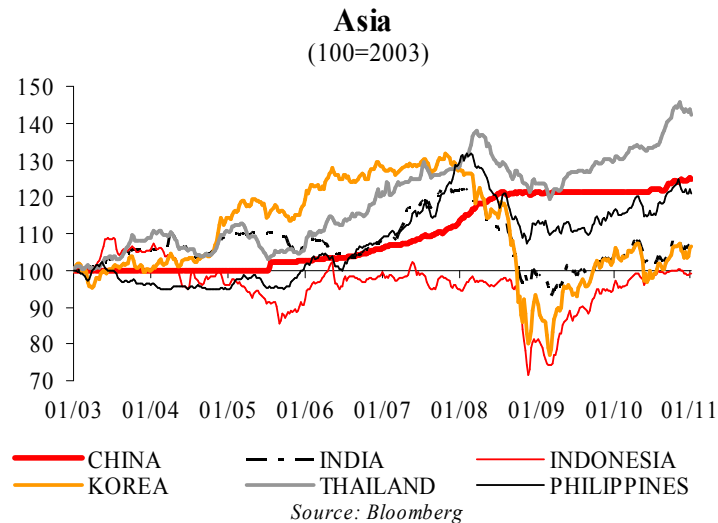
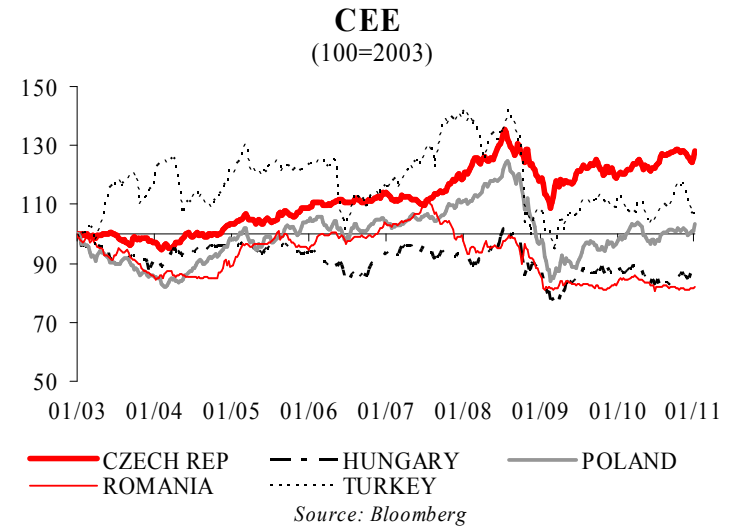
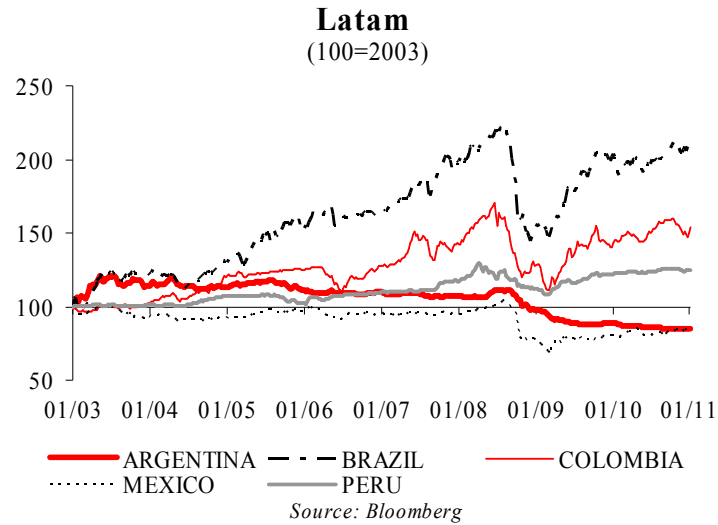
Long term rates



Source: Bloomberg

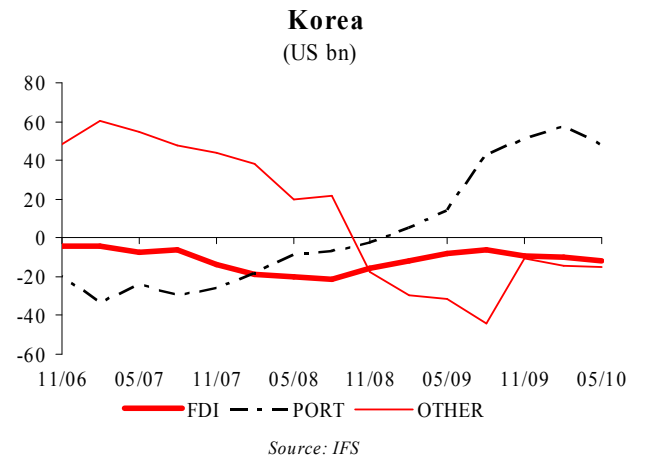
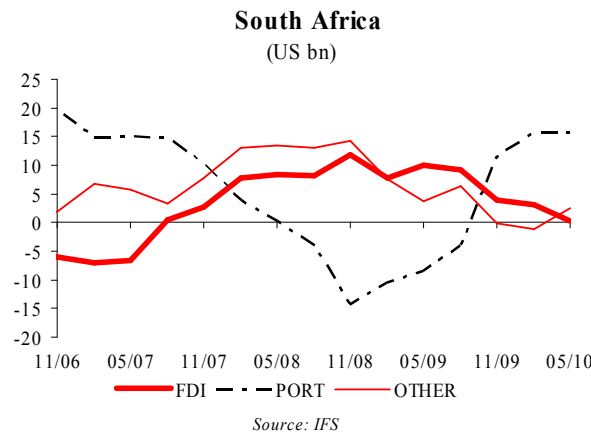
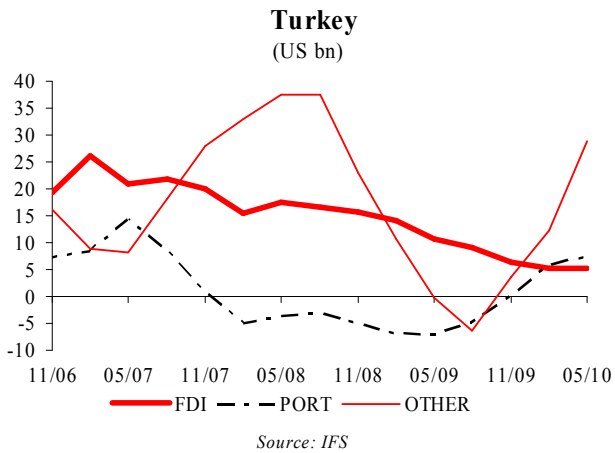
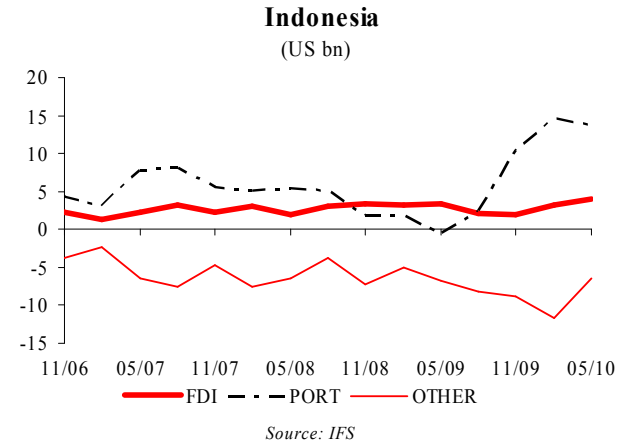
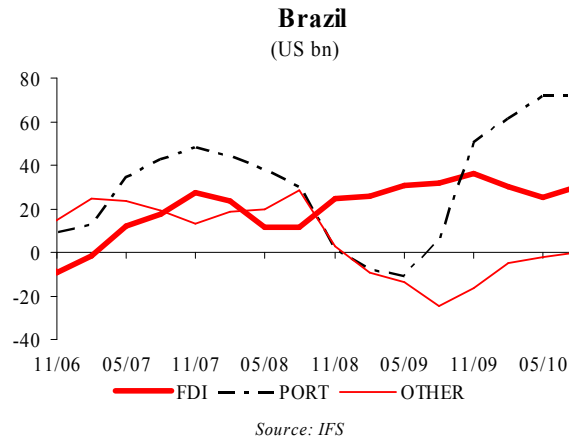
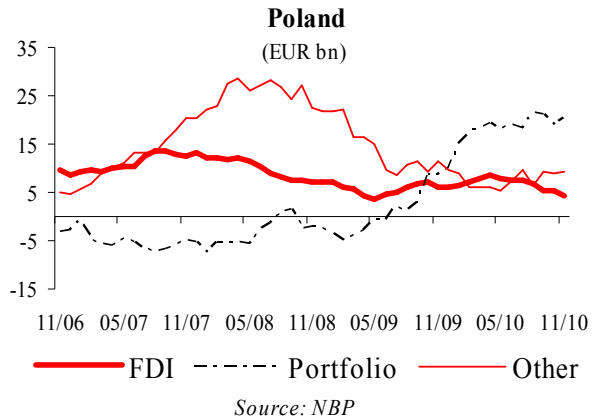


FX appreciation pressures: but most currencies are still below their 2008 peak

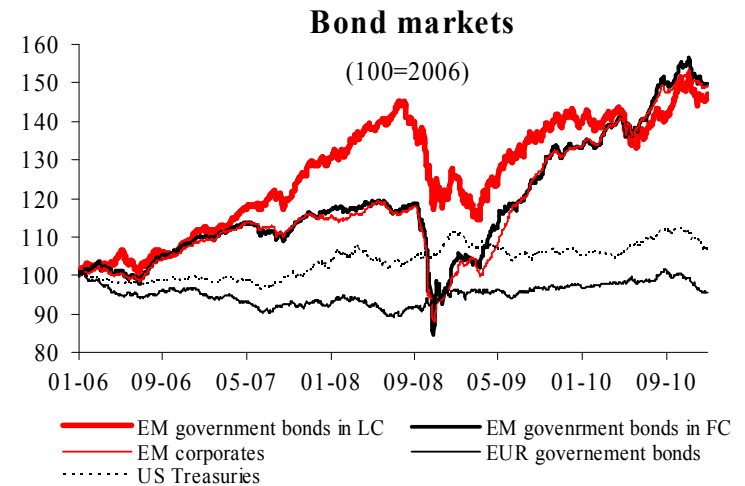
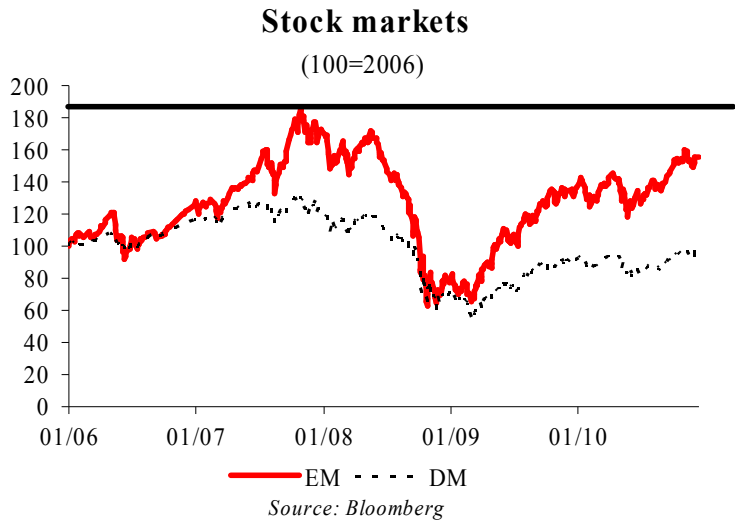




IR differential + FX appreciation driving hot money inflows

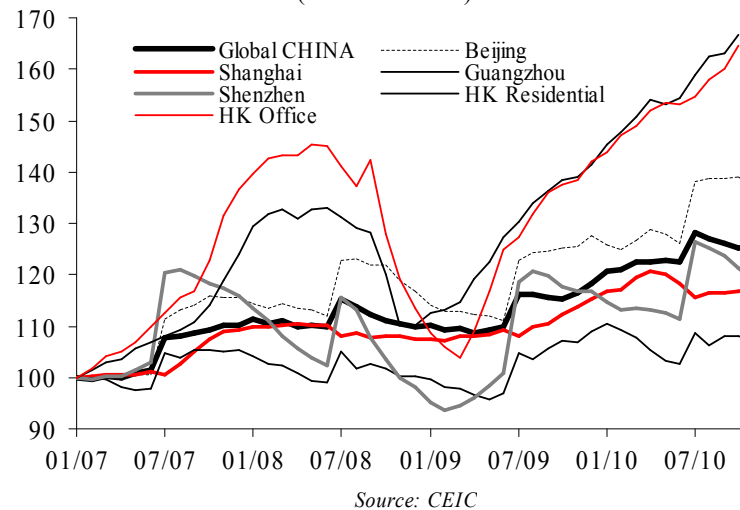


Bubbles in the making ?



Property Prices in China and HK

(Jan 2007=100)

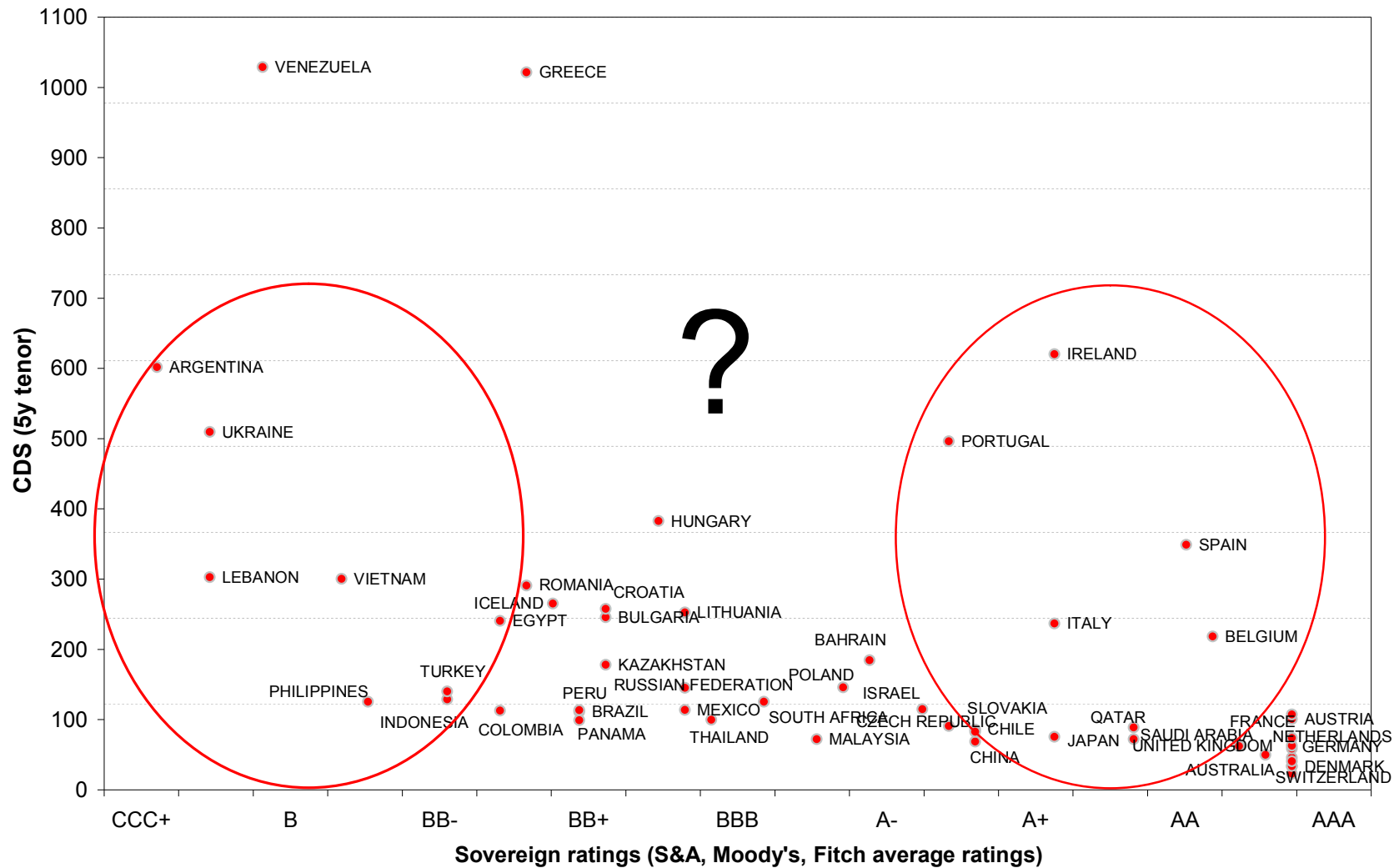




Policy reactions: IR hikes, intervention & capital controls

	IR hikes (ytd)	Reserves accumulation (in USDbn)			Administrative measures
		level	variation	growth	
Brazil	+200 bps to 10,75%	285	+ 45	19%	Oct: tax on non residents bond purchases raised to 6% (Oct 22, from 4% in Oct 5 and 2% in Oct 2009); tax on margin deposits for derivative contracts hiked to 6% from 0.38%.
China	+50 bps to 5,81%	2600	+ 375	17%	Sept :i) tightened limits for banks net open FX position; (ii) strengthened documentation requirements for FX export/import payments.
Indonesia		90	+ 27	43%	July: 1-month minimum holding period for central bank money market certificates. Reserve requirements on FC deposits raised from 1% to 5%
Korea	+50 bps to 2,5%	290	+ 20	7%	July: Caps on banks' FX derivatives as "macroprudentialmeasure"
Thailand	+75 bps to 2%	170	+ 33	24%	Oct: withholding tax (15%) on interest income and capital gains by foreign investors.
Taiwan	+37 bps to 1,625%	380	+ 32	9%	Nov: caps in offshore funds investment allocation to government bonds and money market products Dec: reserve requirements on new LC deposits held by non residents raised to 90%.

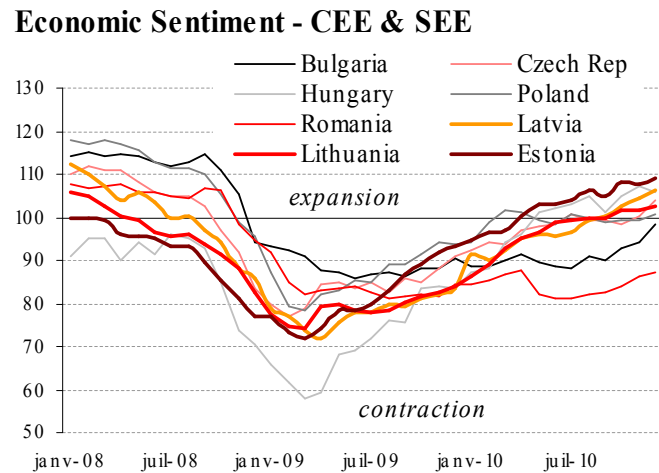
Risks rankings revisited by the markets



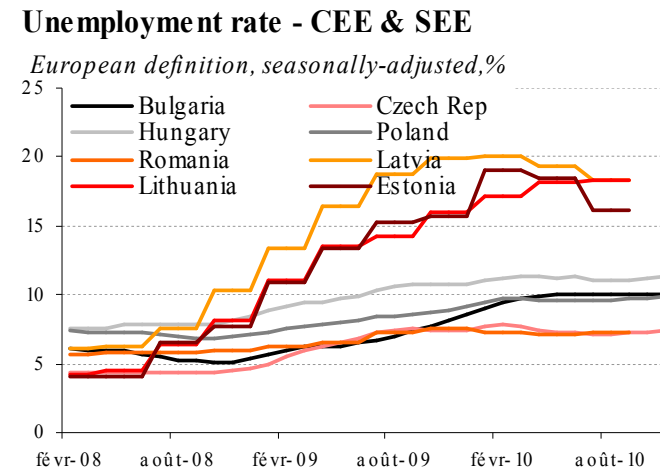
CEE: a gradual, modest, export-led recovery



Source: IMF, SG estimates

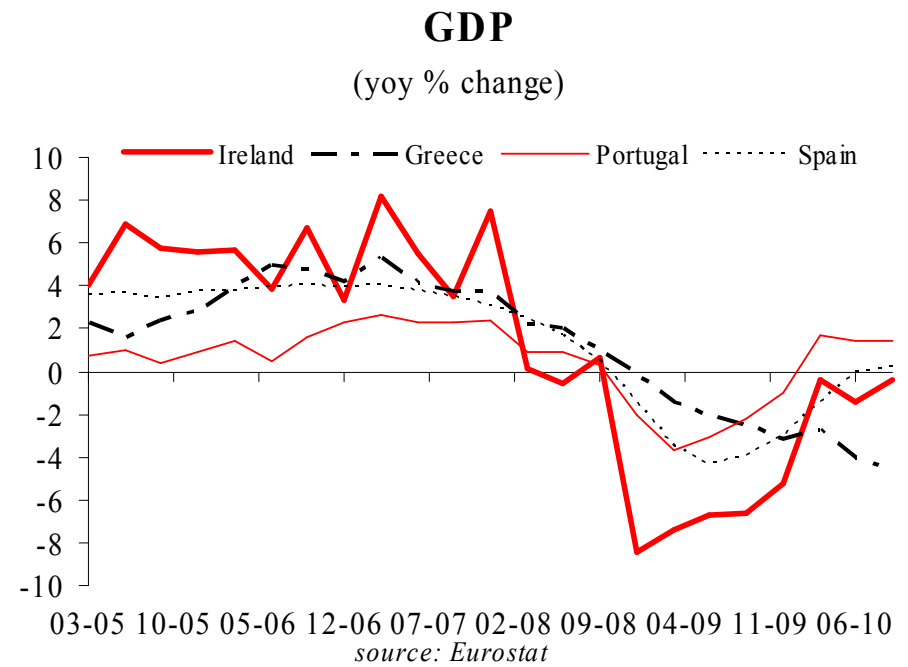
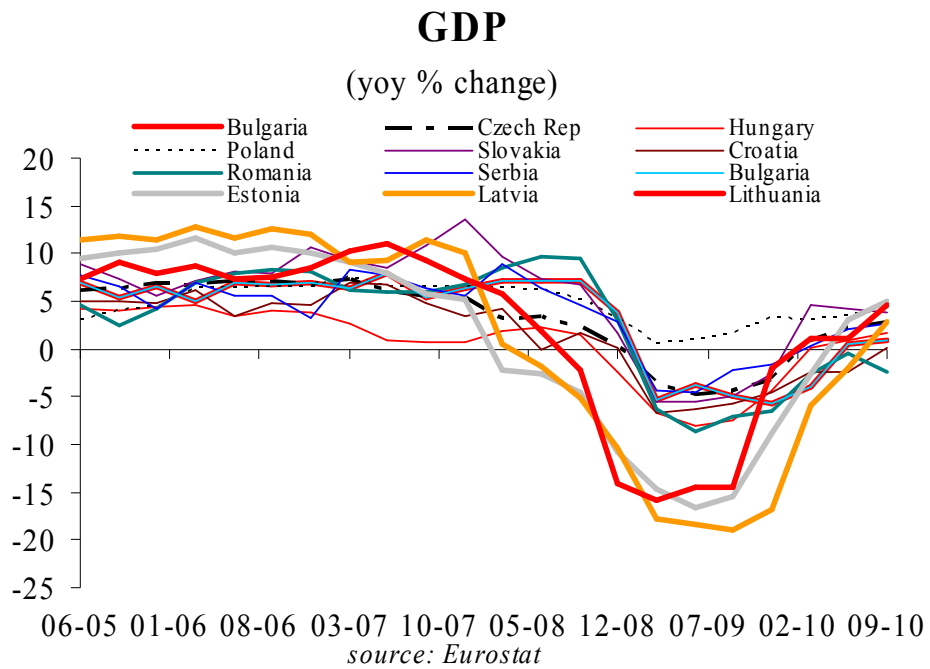


Source: European Commission

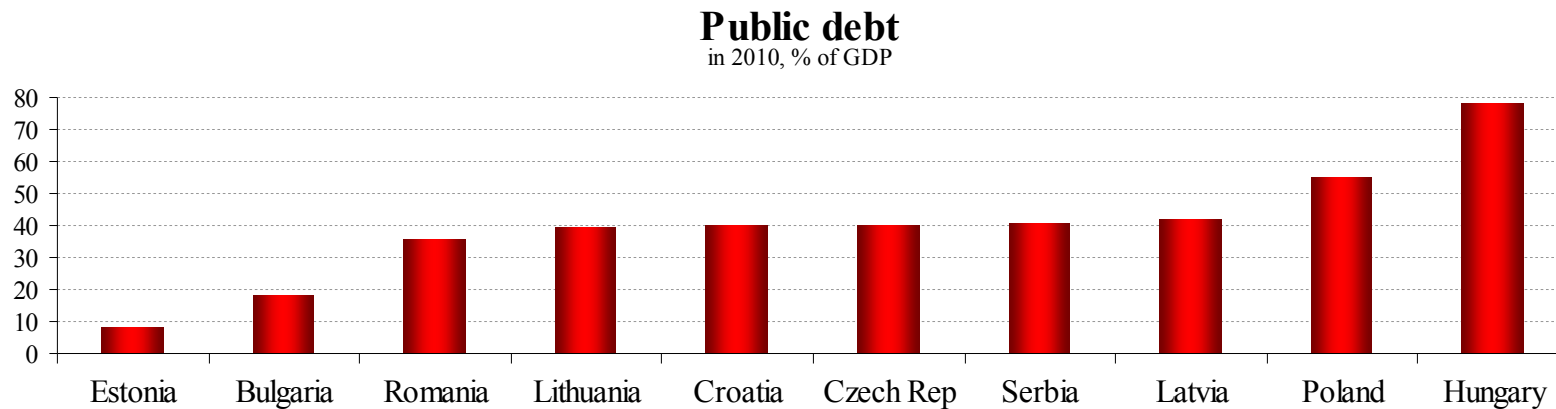
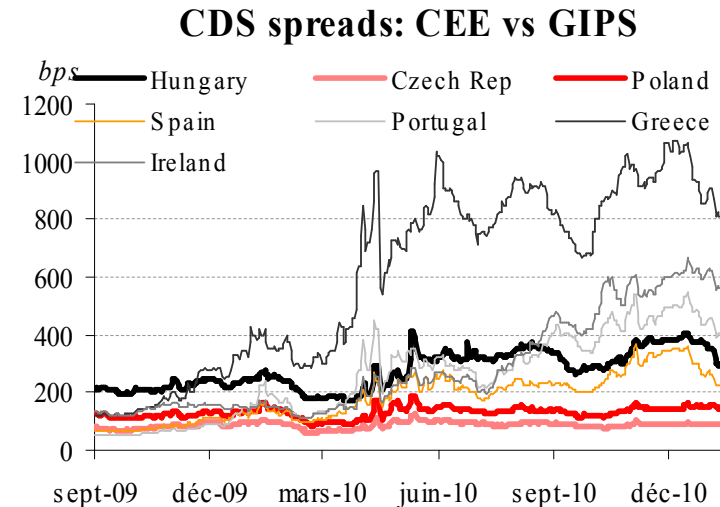
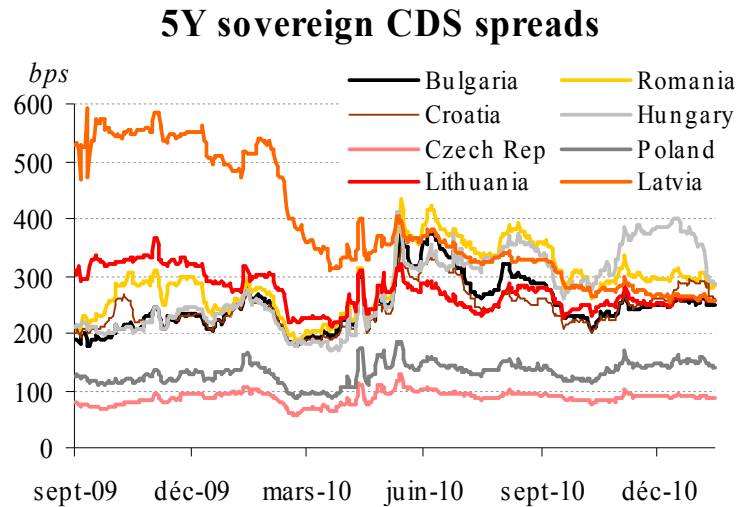


Source: Eurostat

Comparing the sizes of the adjustments



Risk aversion has shifted towards EMU periphery





Meanings of the “new normal”

- **Growth divergence to last**
 - ▶ EM: strong domestic demand and sound financial profile
 - ▶ DM: fiscal austerity plans and financial stability issues
- **Fundamentals are conducive to capital inflows and currency appreciation**
 - ▶ Policy dilemmas: inflation versus currency appreciation
 - ▶ Capital controls target the composition of flows rather than volumes.
- **To watch:**
 - ▶ Widening current account deficits in **Brazil, Turkey, India**
 - ▶ Municipalities finances and segments of real estate markets in **China**
 - ▶ Overheating/bubbles risks: still at an early stage
 - ▶ Further capital controls to come
- **Central and Eastern Europe medium term challenges :**
 - ▶ To ensure productivity gains specially in a fixed exchange rate regimes
 - ▶ To grow with moderate external imbalances
 - ▶ Euro adoption