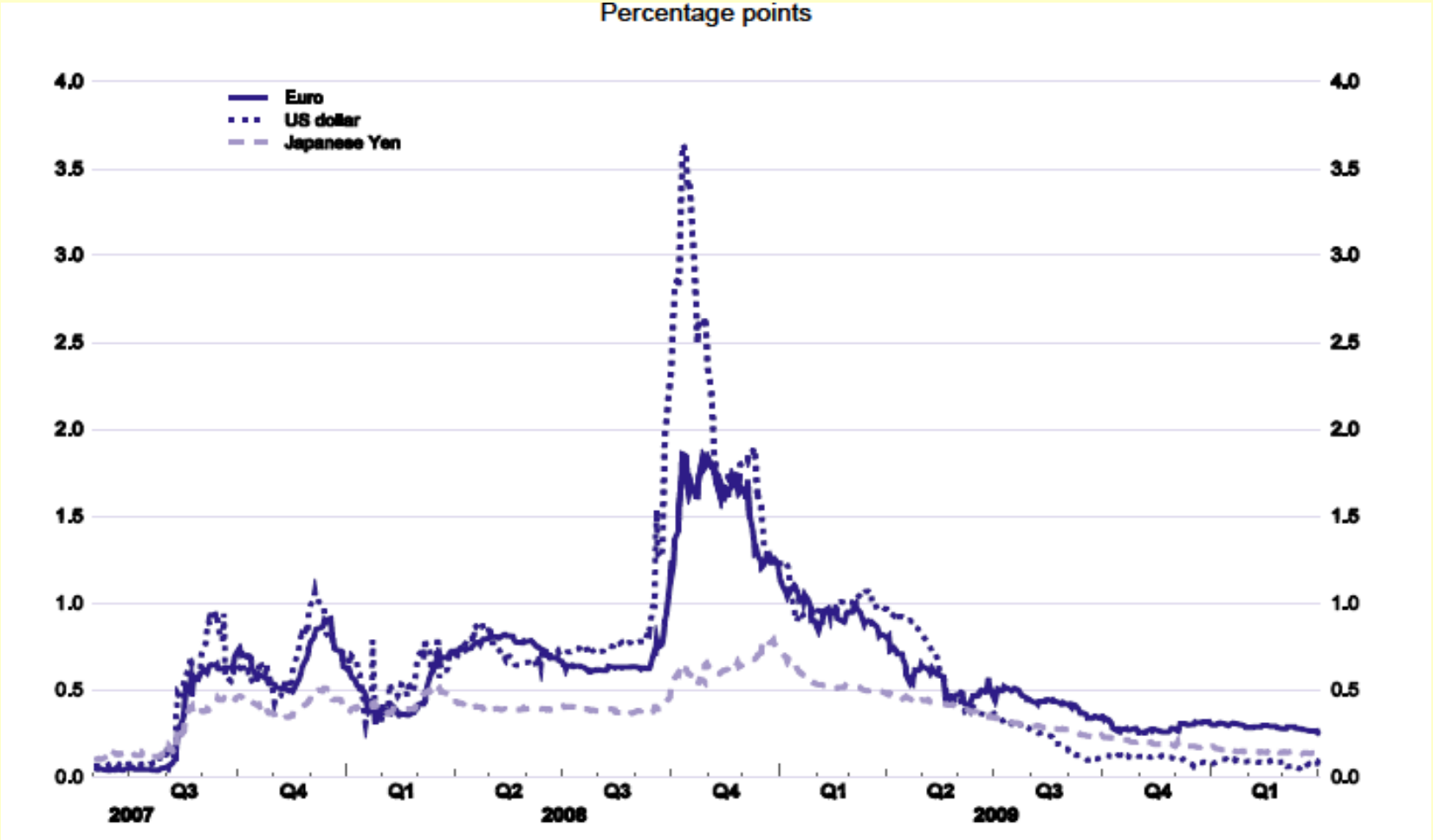
David Smith

After the great recession

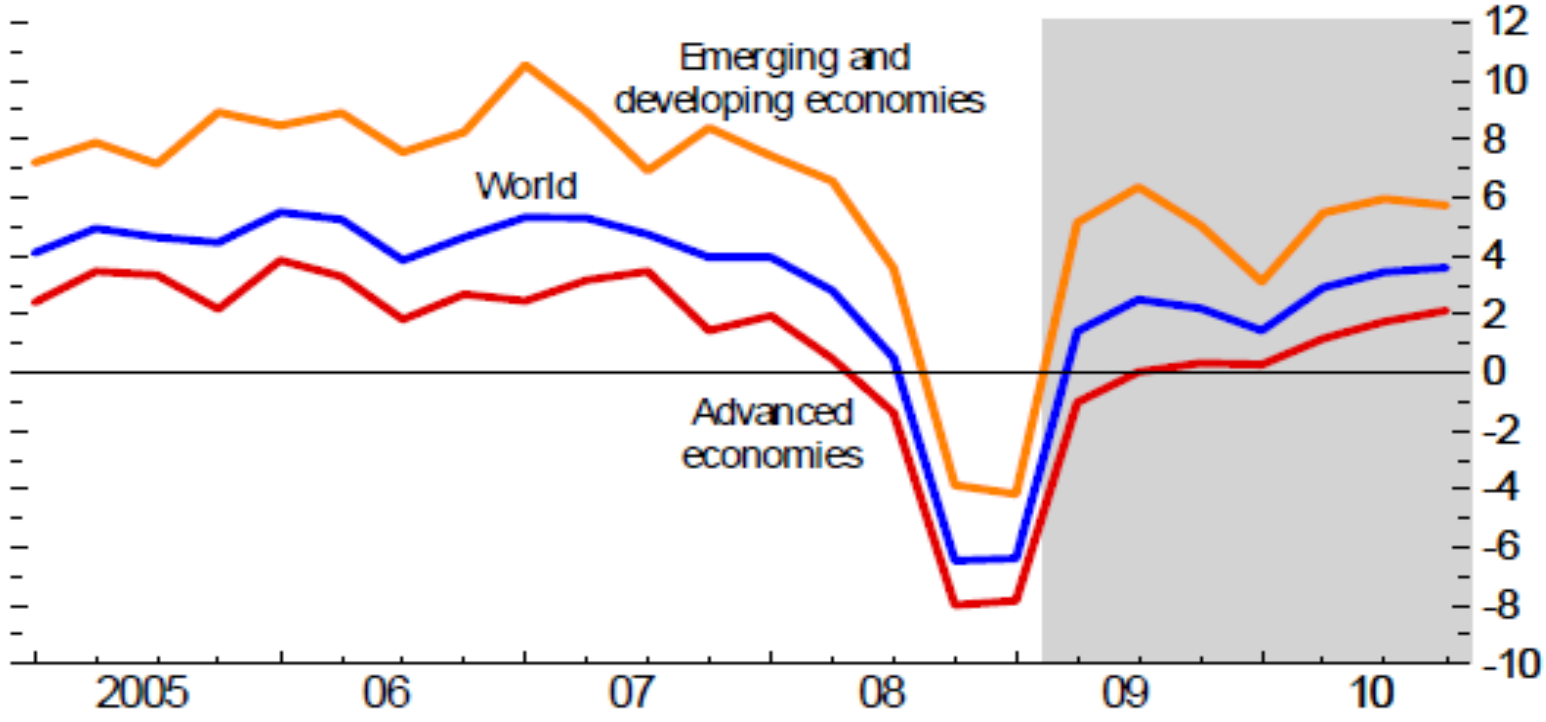
A changing global economy in an age of instability

Two years after the biggest financial storm in a century

Time heals – a long time since 2008

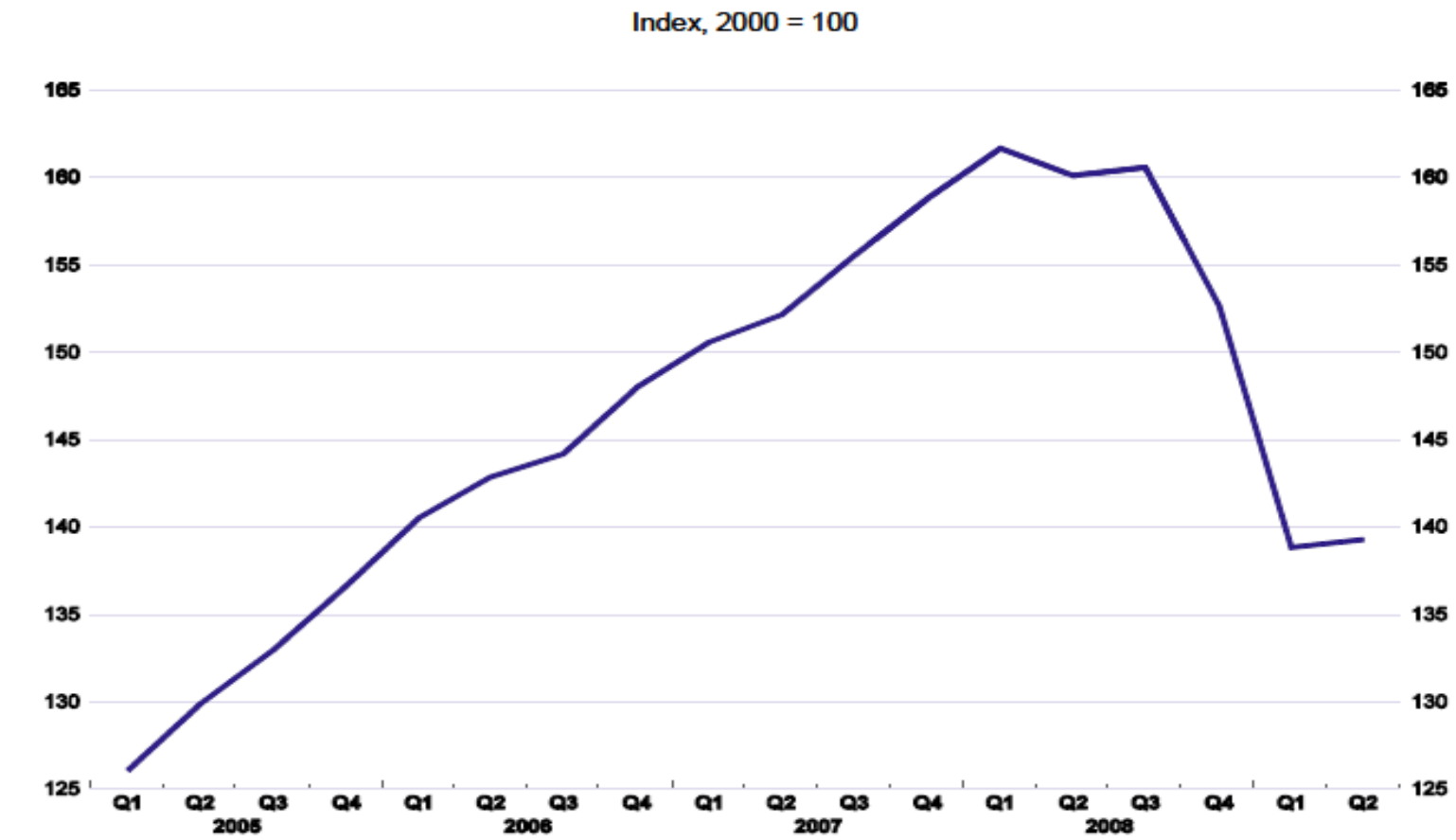


But the worst post-1945 world recession

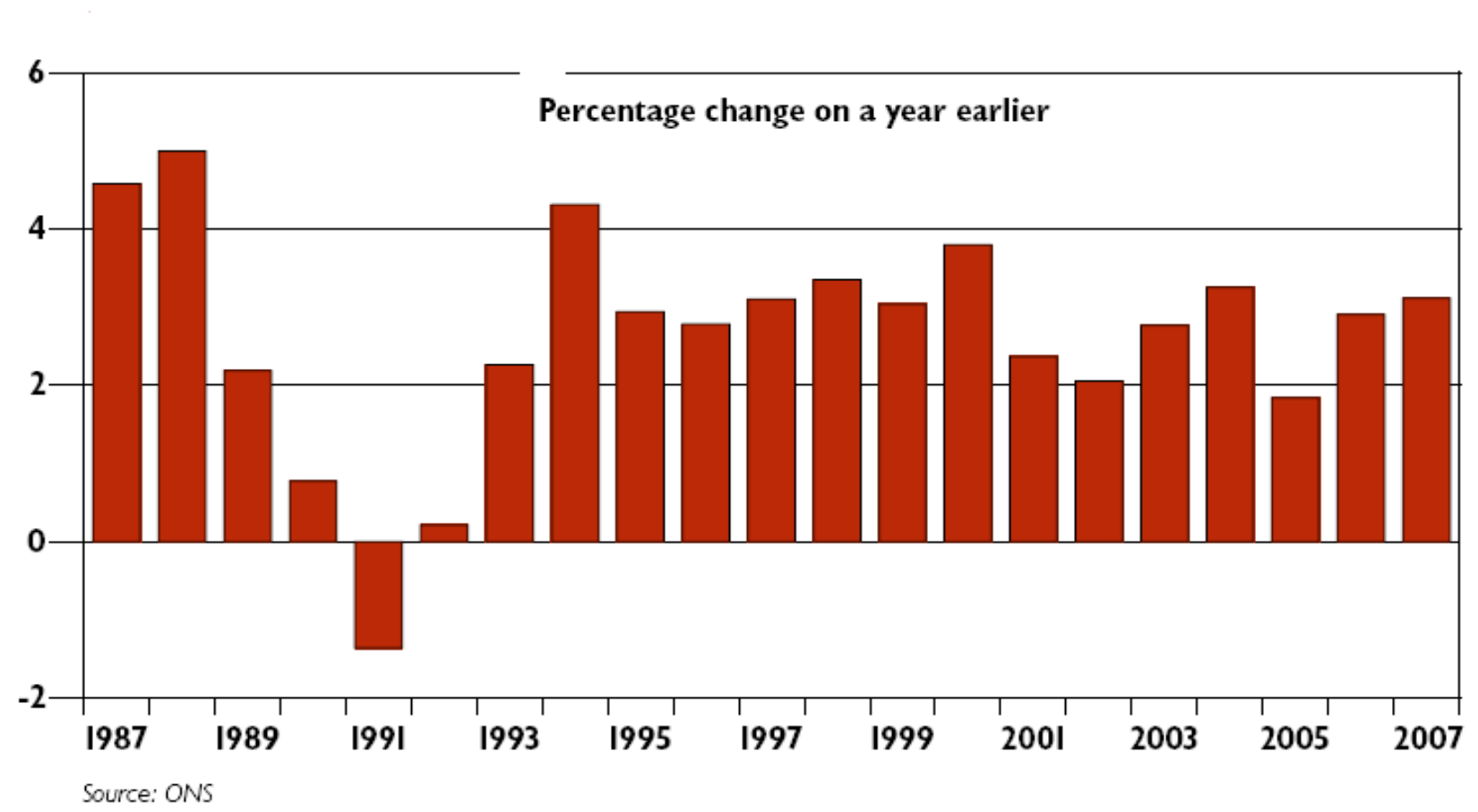


Source: IMF staff estimates.

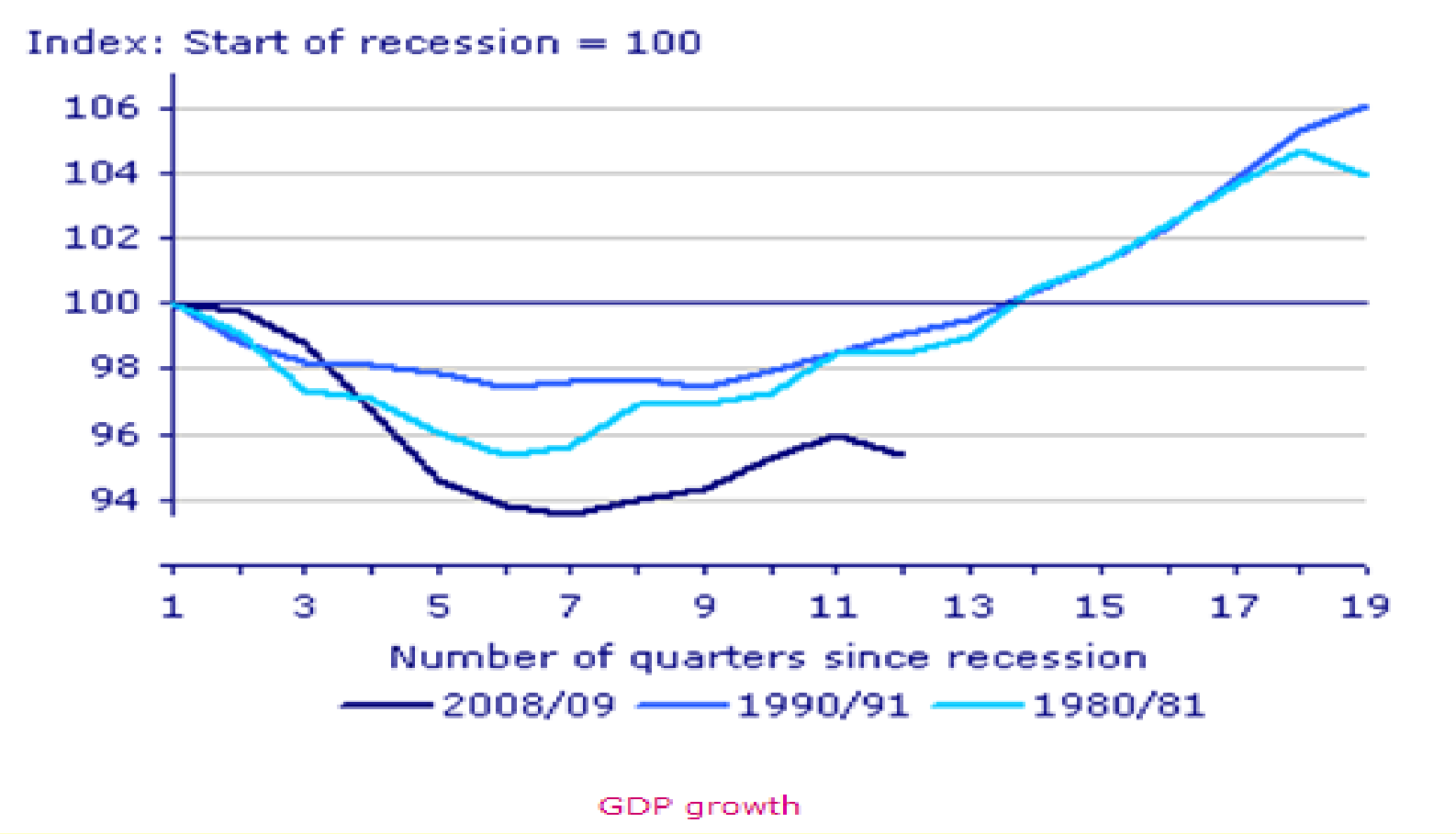
…. And a world trade collapse



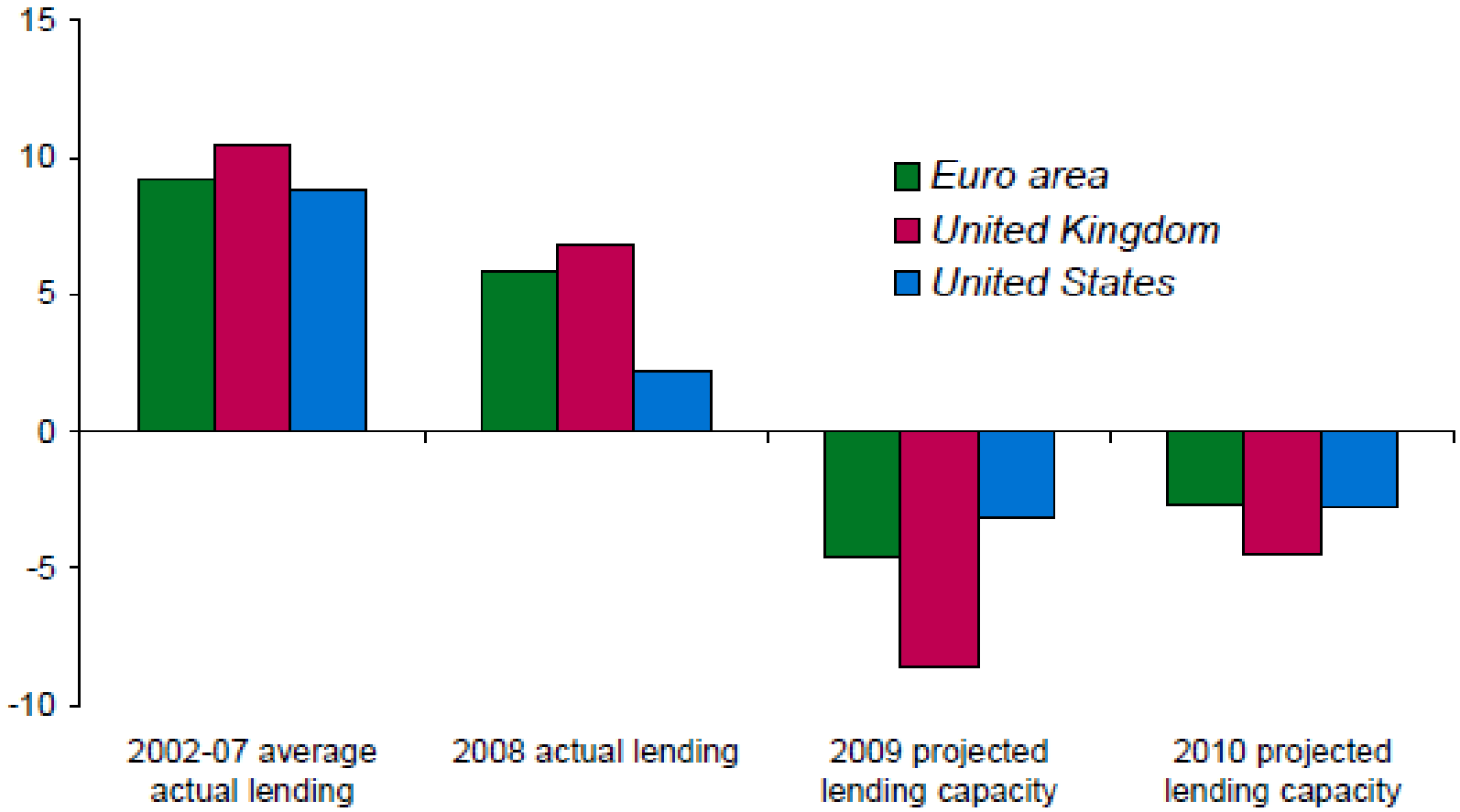
After the long UK upturn



The worst post-war recession

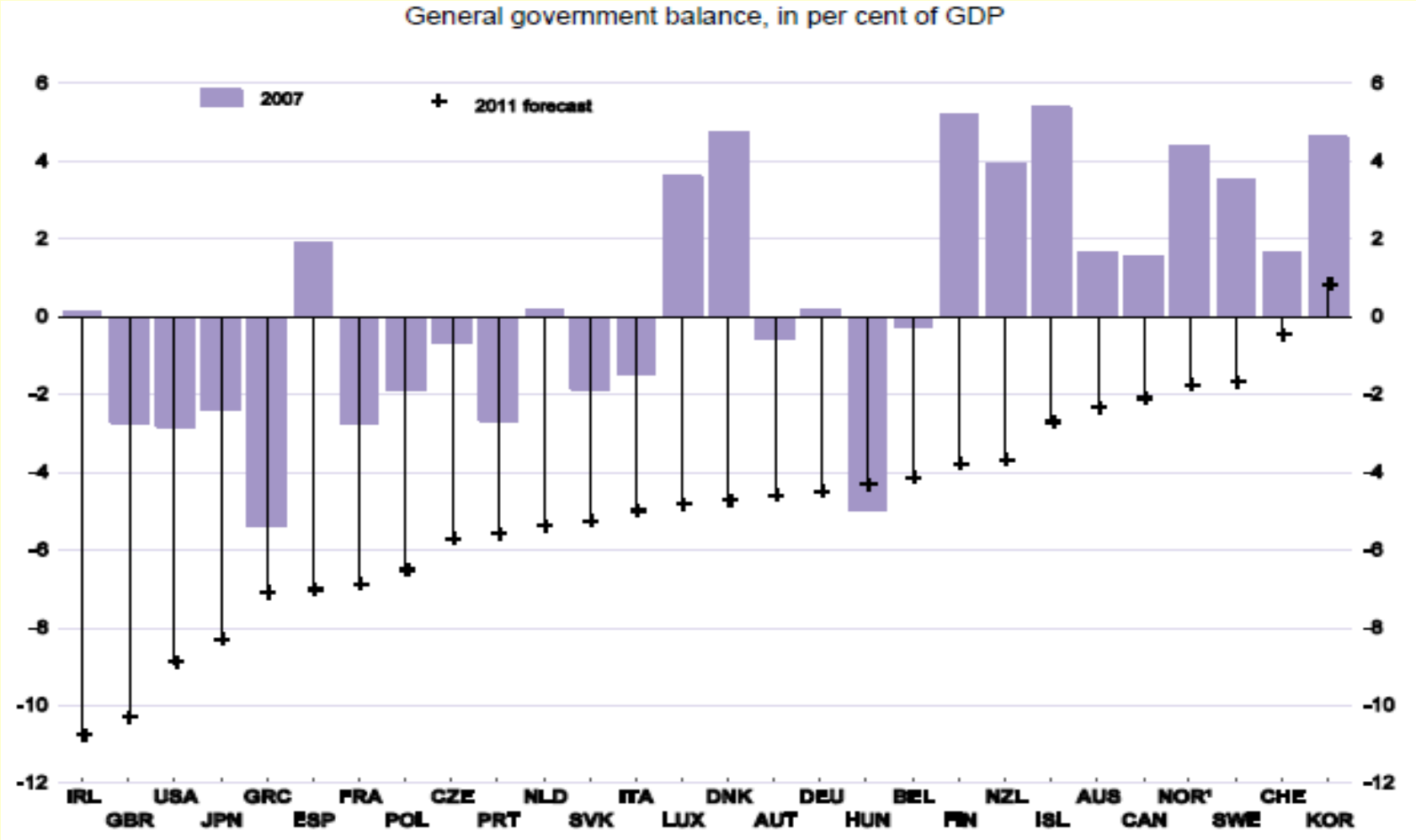


Leaving weakened banking sectors

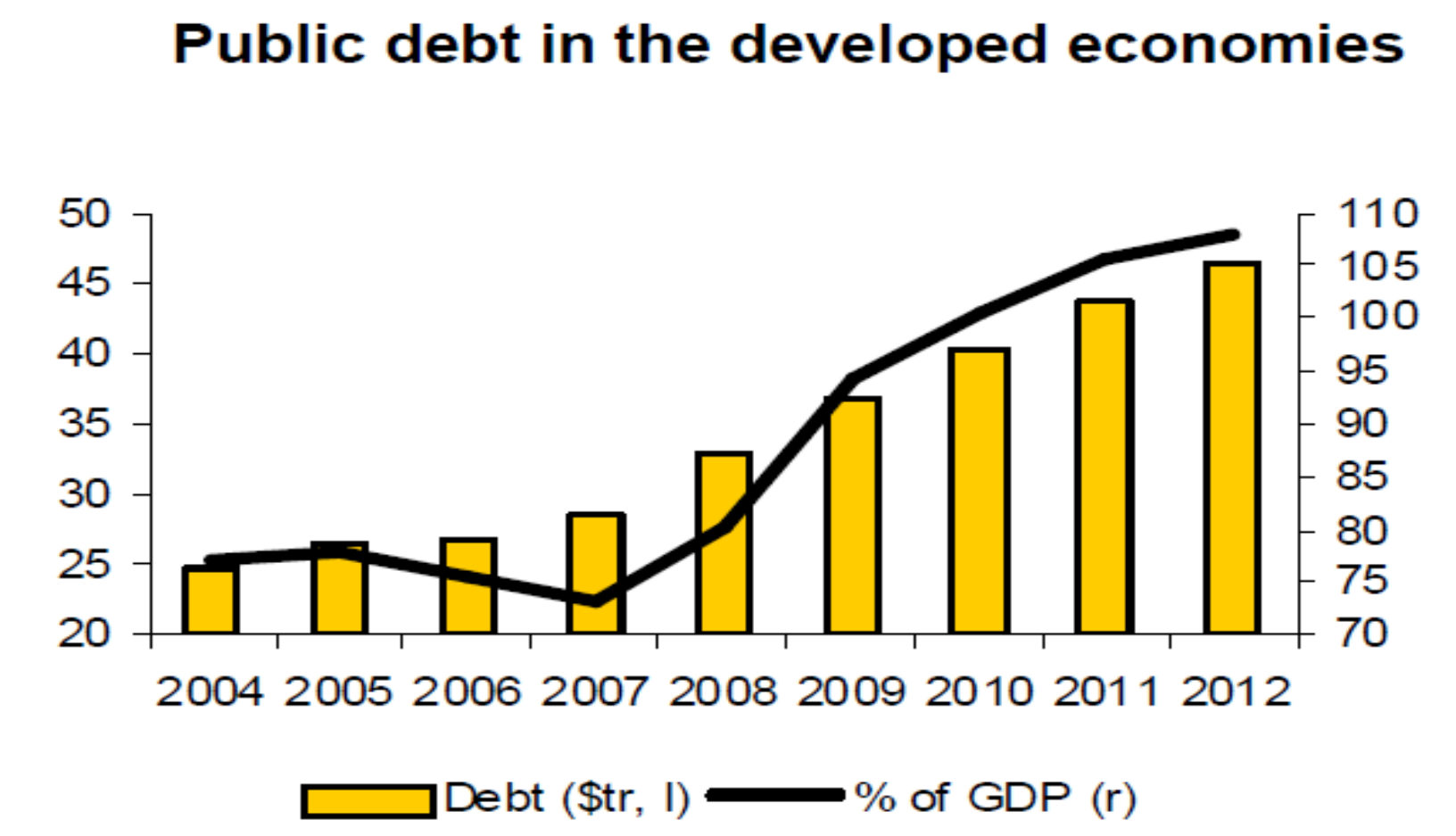


Source: IMF staff estimates.

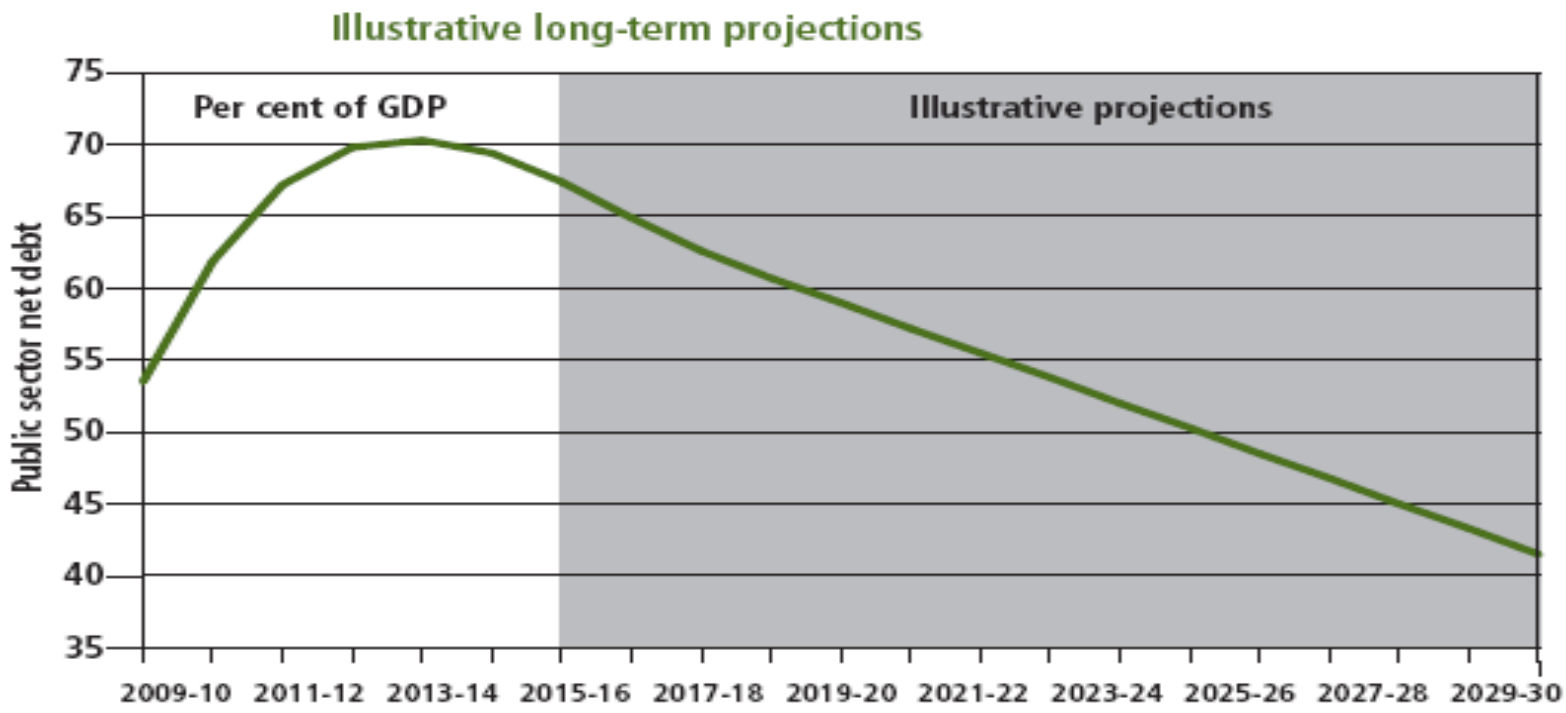
And very painful fiscal hangovers



… which will endure



Debt dynamics require early deficit action



Source: Office for Budget Responsibility and HM Treasury.

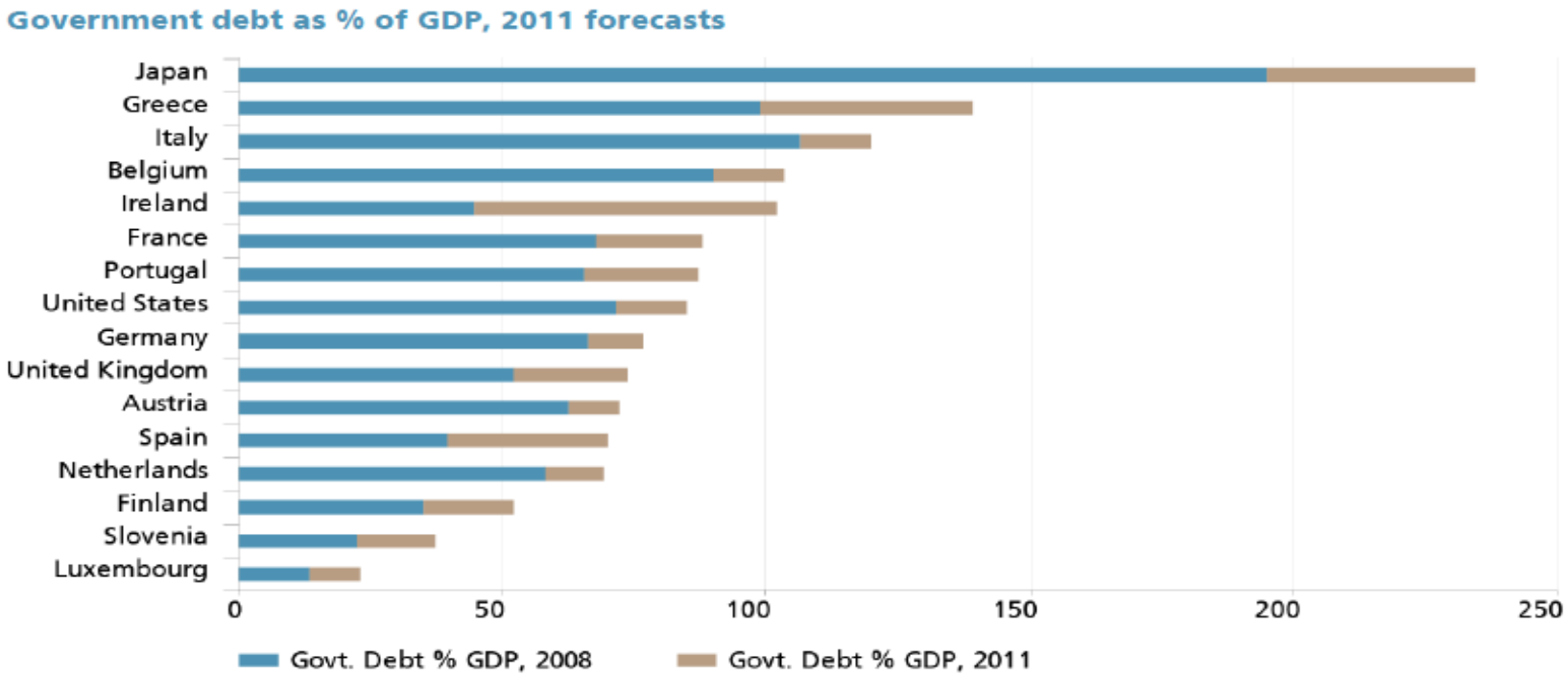
Lessons from the crisis

- Globalisation means financial/banking contagion spreads more rapidly than ever.
- Public finances are highly vulnerable to recessions caused by financial crises.
- Markets are ruthless at exploiting perceived weakness: Thailand, Indonesia, etc., in Asian crisis of 1997-8. Greece, Ireland in 2010.
- Trust, transparency and credible planning are essential.

The world according to PIMCO

- ‘Governments want to convince lenders they've been to rehab and are going straight. But like in Alcoholics Anonymous, just because you've been to a few meetings I'm not going to give you a job.’
- ‘Britain is on a bed of nitro-glycerine’ (January 2010)
- ‘Who will buy Treasuries when the Fed doesn’t? A successful handoff from public to private credit creation has yet to be accomplished, and that will determine the outlook for real growth and the potential reversal in our astronomical deficits and escalating debt levels.’

Japan is trusted – Greece was not



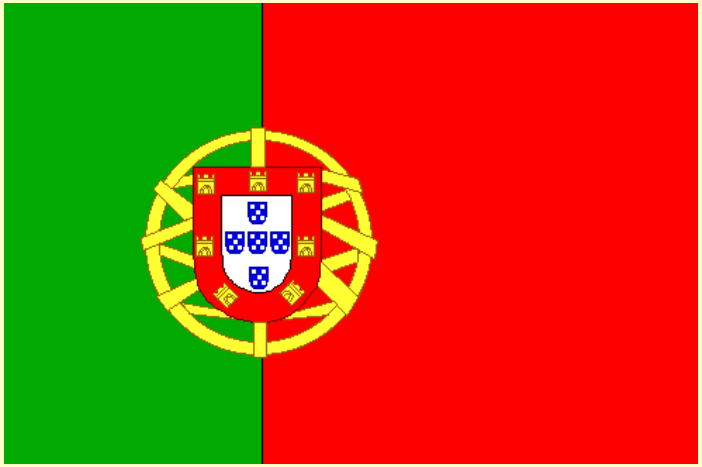
Source: IMF, UBS
Past performance is not an indication of future returns.

UBS

Two rescues down ....

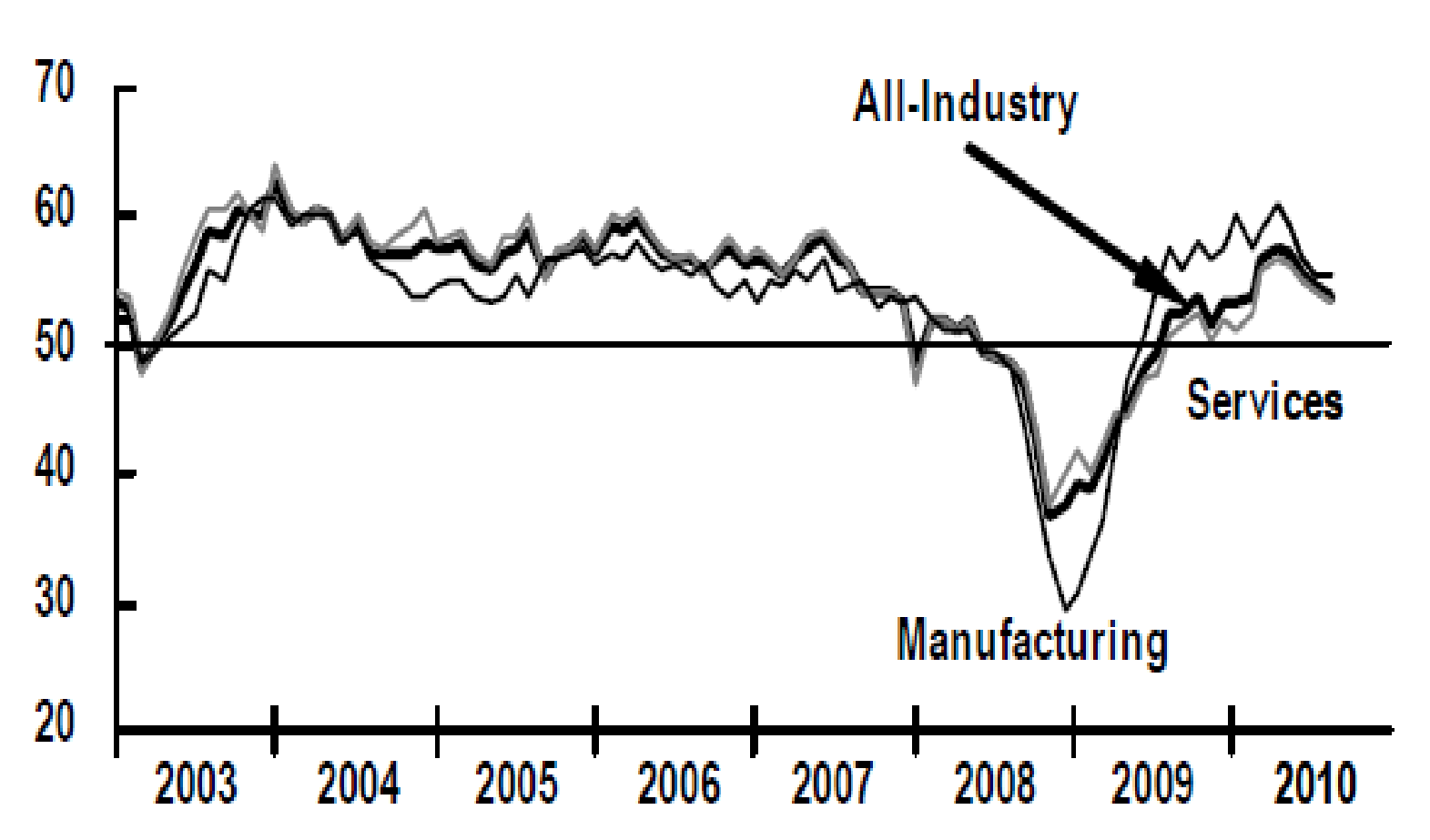
- €110 billion rescue package for Greece, agreed in May 2010.
- EU also agreed €720 billion Europe/IMF fund to provide loan guarantees and credits to other troubled countries.
- €90 billion Irish rescue package agreed in November 2010, focusing on bail-out for Ireland's banks.

…. More to come?

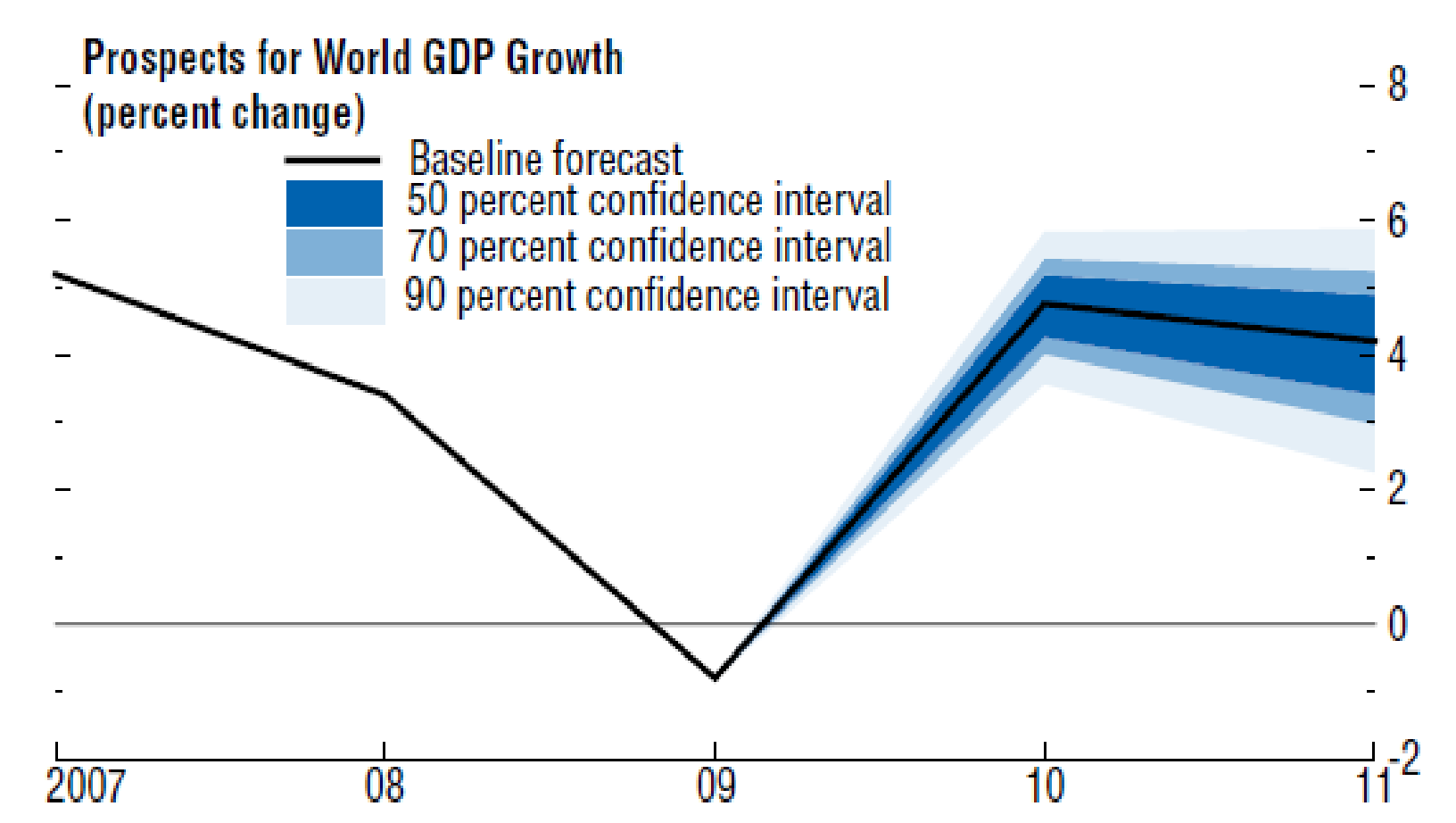


Plenty of global green shoots

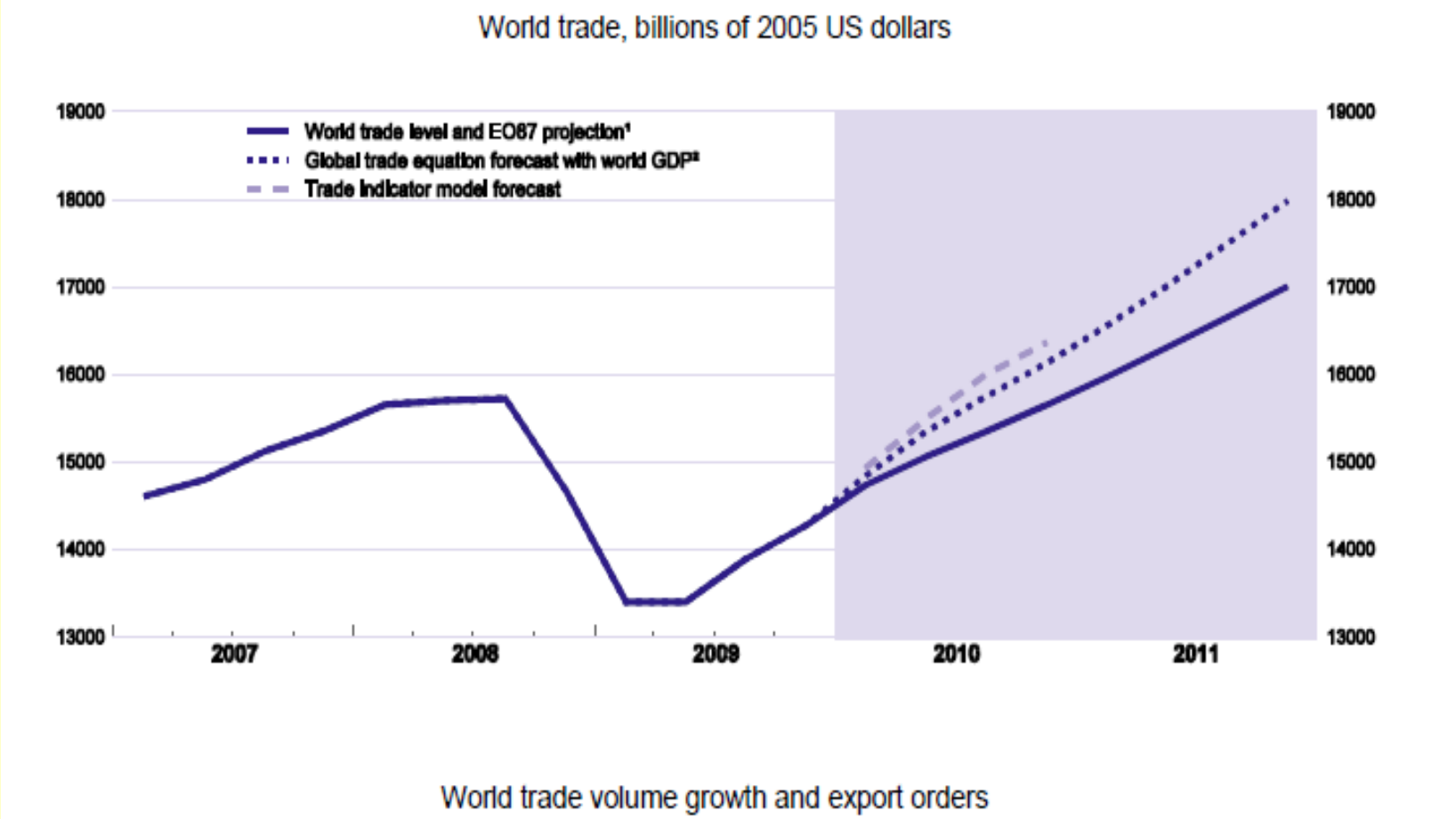
Global PMIs have recovered well



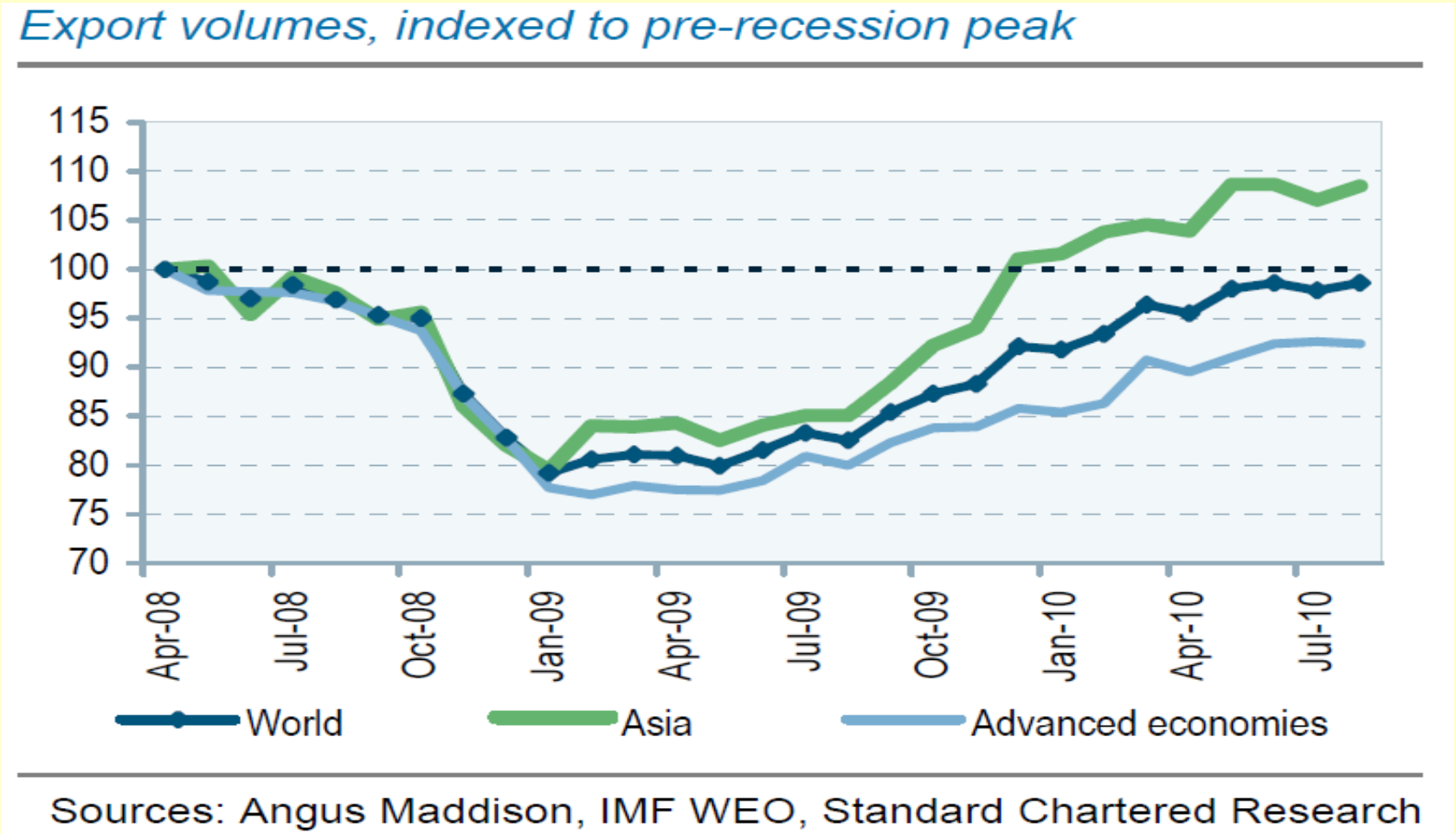
The world's V-shaped recovery



Globalisation threat averted

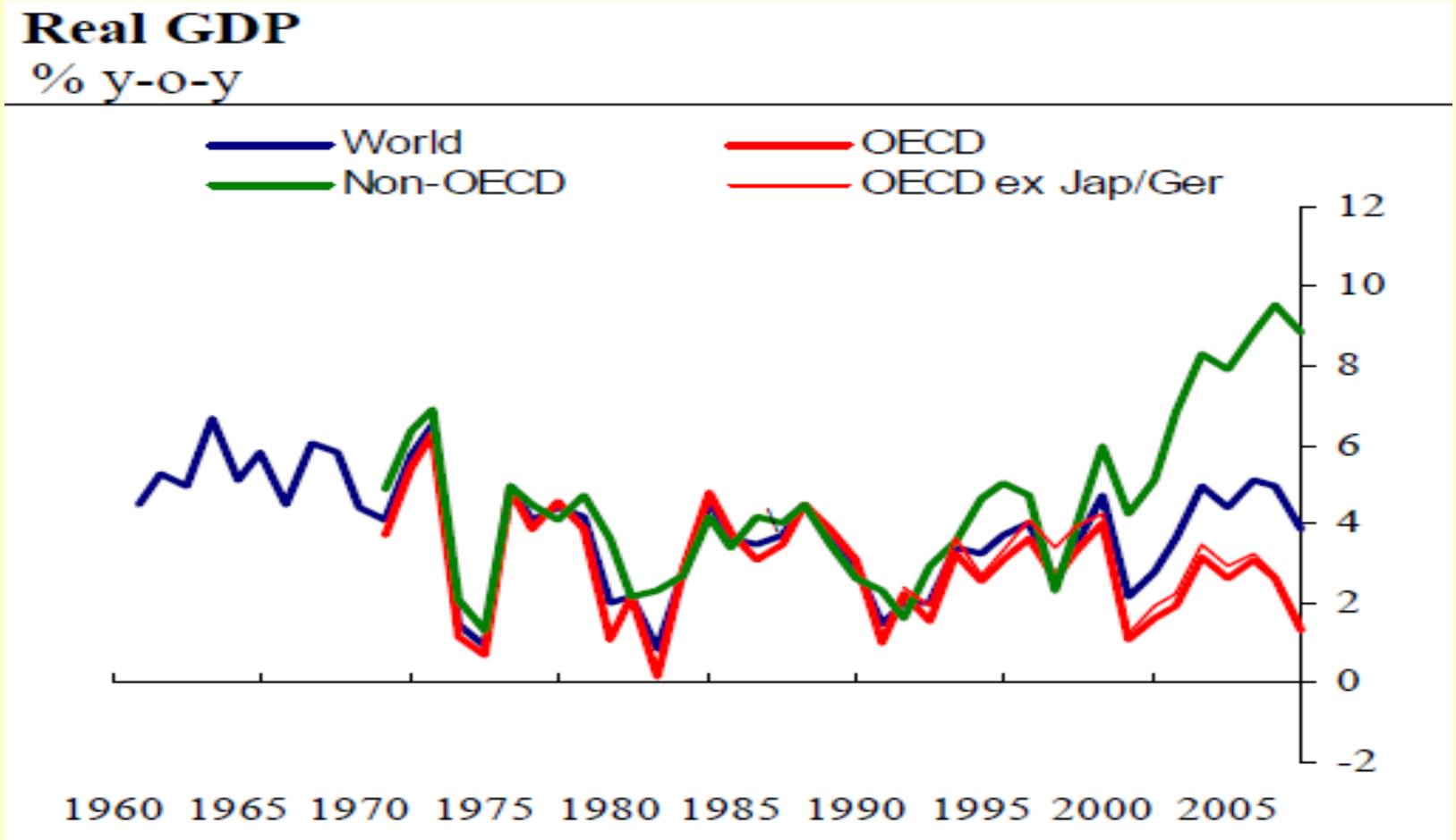


Led by Asia

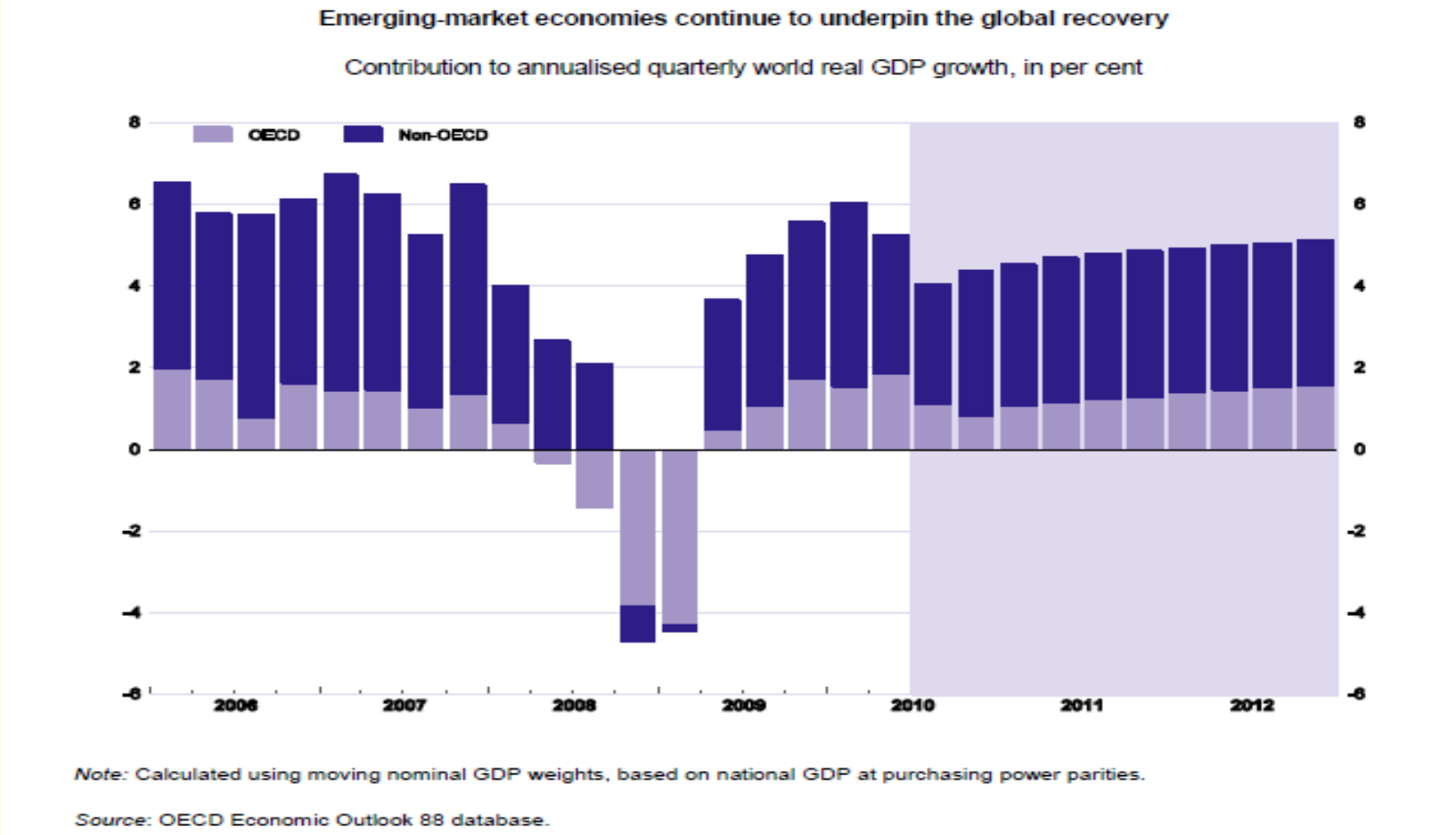

Export volumes, indexed to pre-recession peak
115
110
105
100
95
90
85
80
75
70
Apr-08
Jul-08
Oct-08
Jan-09
Apr-09
Jul-09
Oct-09
Jan-10
Apr-10
Jul-10
World
Asia
Advanced economies
Sources: Angus Maddison, IMF WEO, Standard Chartered Research

The global economy’s shifting sands

The great divergence is recent



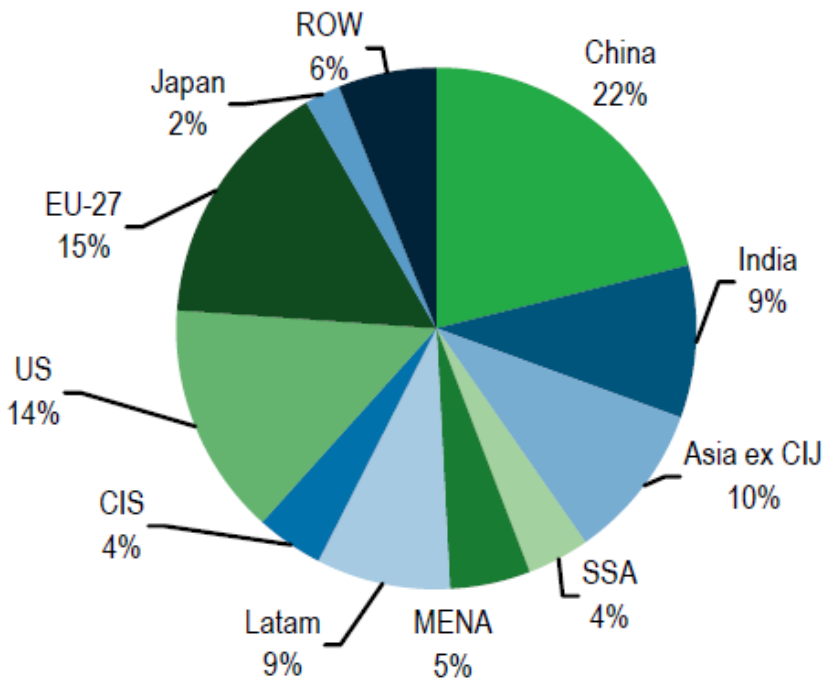
But is likely to be a feature of the upturn



Where the growth will come from

Two-thirds of global growth to 2030 will come from EMs

% of total (based on real 2009 prices and dollars)



Sources: IMF, Standard Chartered Research

Accelerating the global shift

- 2007: China was expected to overtake Japan's GDP in 2015, America in the mid-2030s.
- 2010: China has already overtaken Japan; will overtake America in the 2020s.
- Global crisis and its aftermath has accelerated the shift by 5-10 years.
- China, India and America should be the world's big three: only one is flagging.

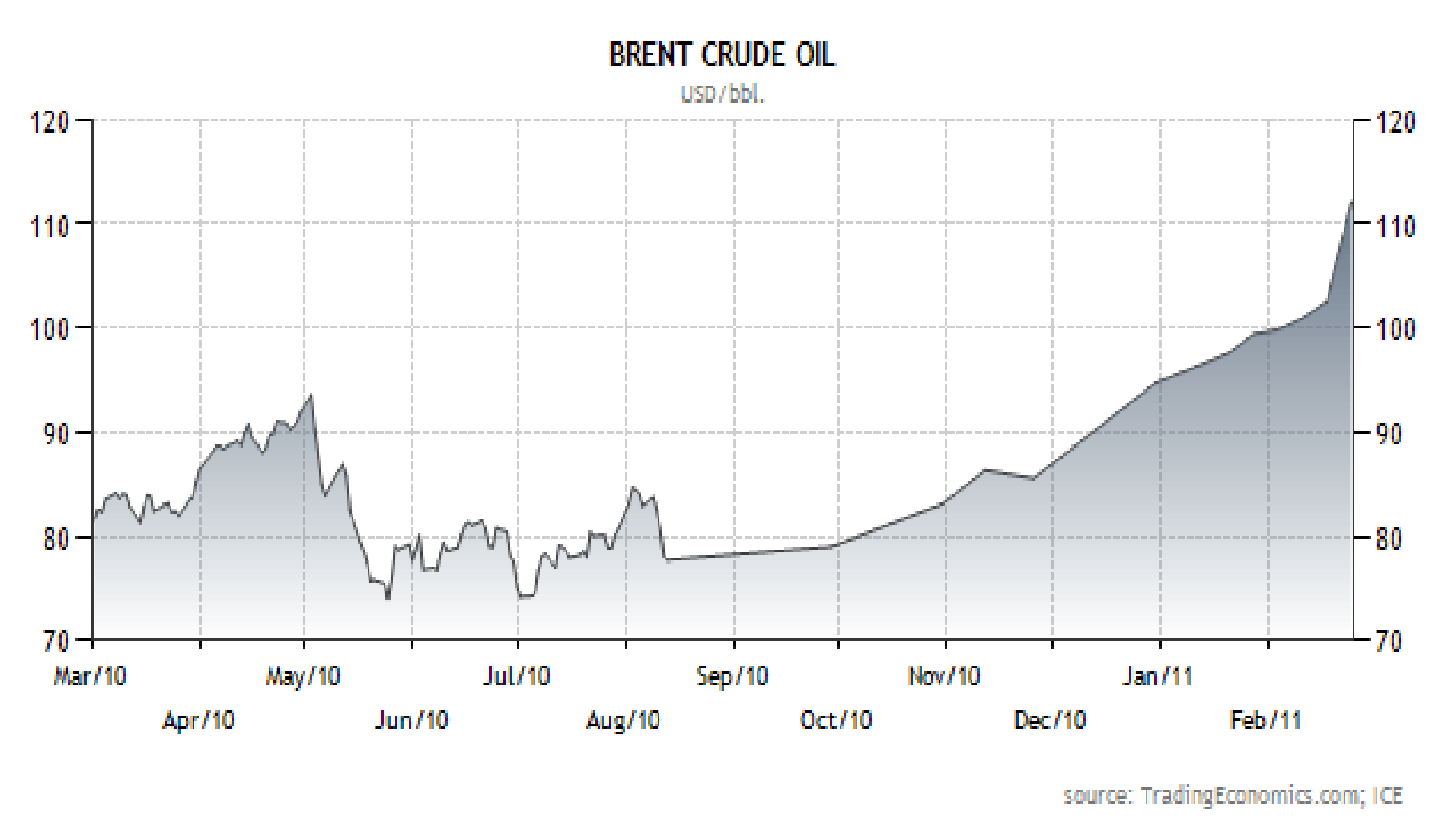
But nothing is guaranteed

- Many potential pitfalls.
- Crime, corruption, bureaucracy, absence of the rule of law.
- Absence of trust, failure to respect international standards. Lack of belief in statistics, public & private accounts.
- Inflexible labour markets.

What could go wrong (short-term)?

- Credit Crunch II – refinancing and deleveraging by the banks.
- Sovereign debt – the euro zone and beyond.
- Currency wars – China versus America as the new heavyweight bout but also others.
- Protectionism – either provoked by or in addition to currency manipulation.
- Fiscal consolidation and the economic and political reaction to it.
- Unknown unknowns (Japan’s earthquake)

Political change pushes up oil prices



And terrible natural disasters

What could go wrong (long-term?)

- Politics – a backlash against capitalism; pressures for democracy; inequality.
- Growth momentum fades dramatically as the easy emerging market catch-up phase comes to an end.
- Globalisation goes into reverse, led by the actions of the advanced economies.
- Resource constraints.

Conclusions

- Global economy recovering strongly from the biggest shock in decades – depression averted. Markets believe in the world upturn.
- Two big, mainly advanced-country hangovers: banking & fiscal indigestion, which is more of a constraint than in emerging economies.
- The balance of global growth has shifted fundamentally in favour of emerging economies.
- In a globalised world, trust and transparency are hard-won advantages, which should not be relinquished.