

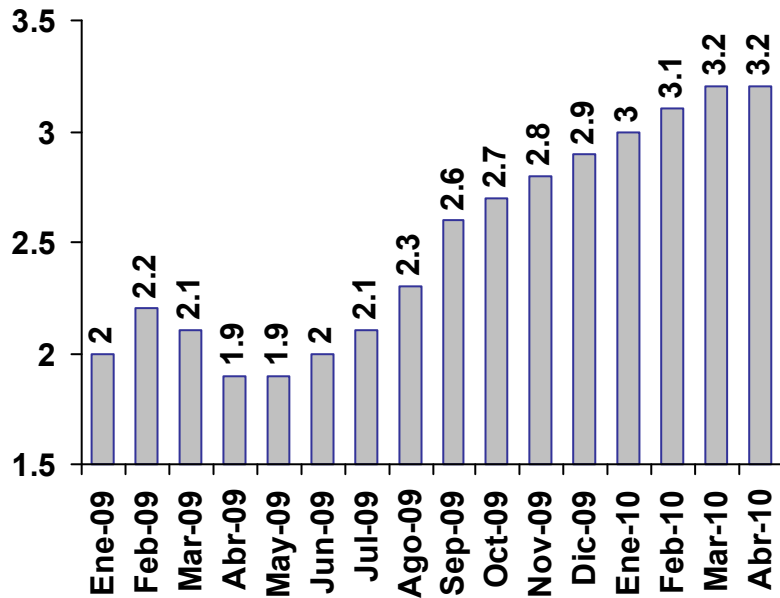
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# **The Global Economy in relation with the precious metal prices**

Claudia Cooper Fort  
Universidad del Pacífico

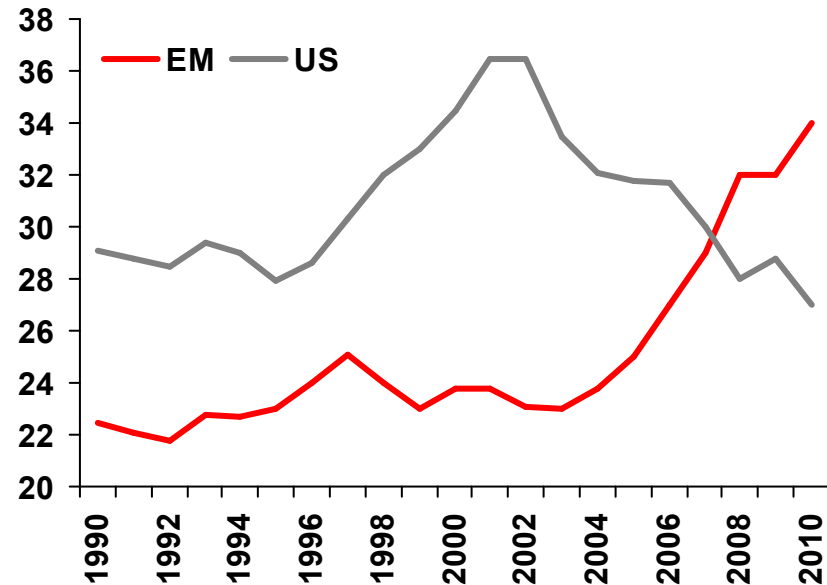
# Recovery was stronger than expected

## GDP Growth 2010 Forecasts (consensus evolution)



Source: Bloomberg

## Evolution of Consumption Structure (% of world total)



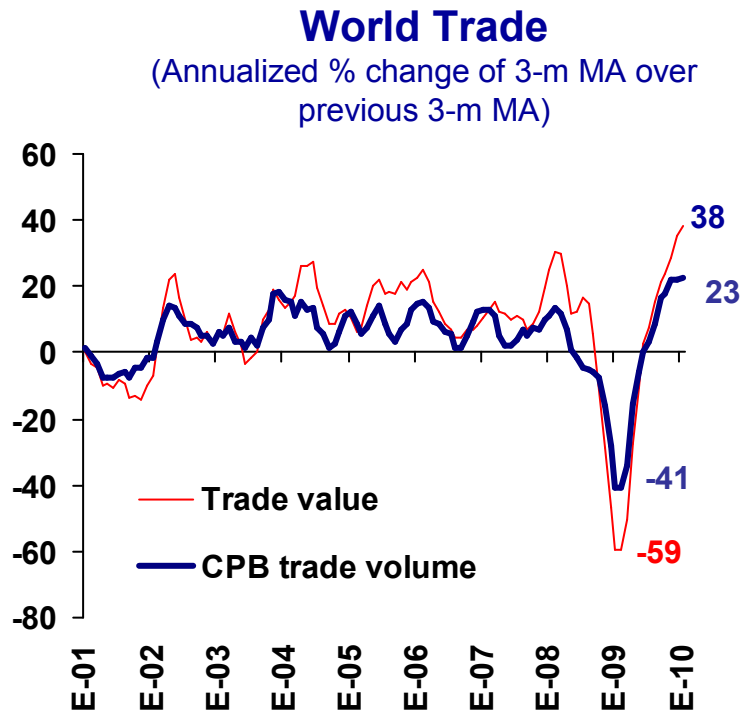
Source: JP Morgan

Emerging Market economies are changing the global landscape

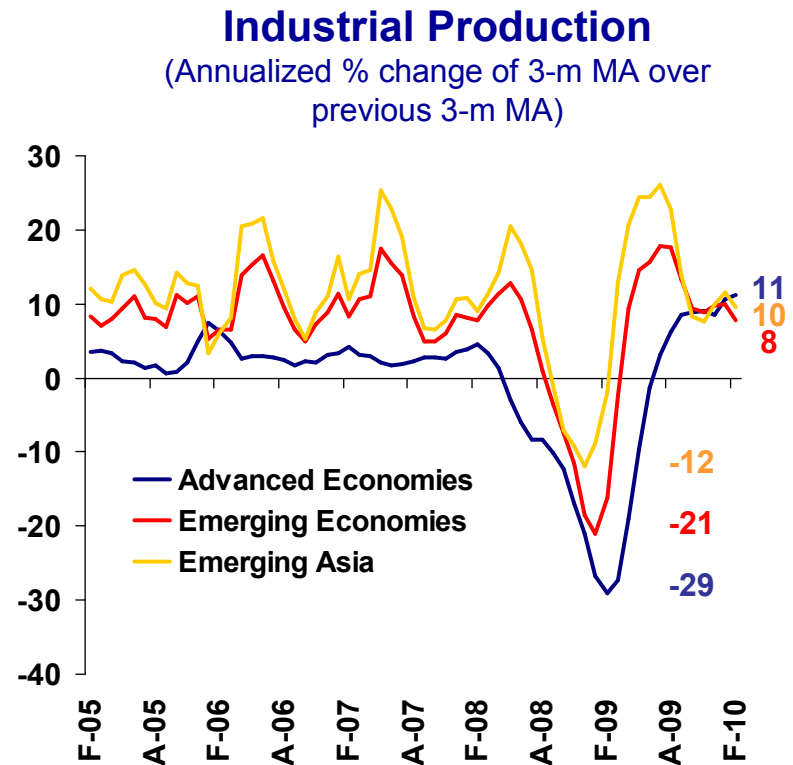
Their share of global consumption is now above one third larger than the US consumer's

their healthier demand trend is having a bigger (positive) impact on global activity

# Recovery was stronger than expected



Source: IMF



Source: IMF

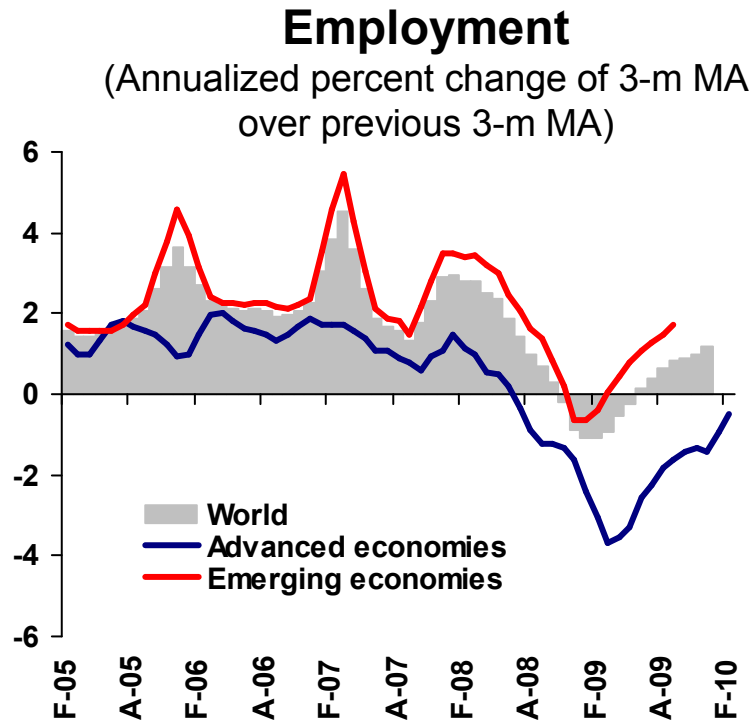
## Advanced economies

- A nascent turn in the **inventory** cycle
- Slowing deterioration (followed recently by improvements) in U.S. **labor markets**
- Strong orders and a recovering **corporate bond market** helped foster investment.

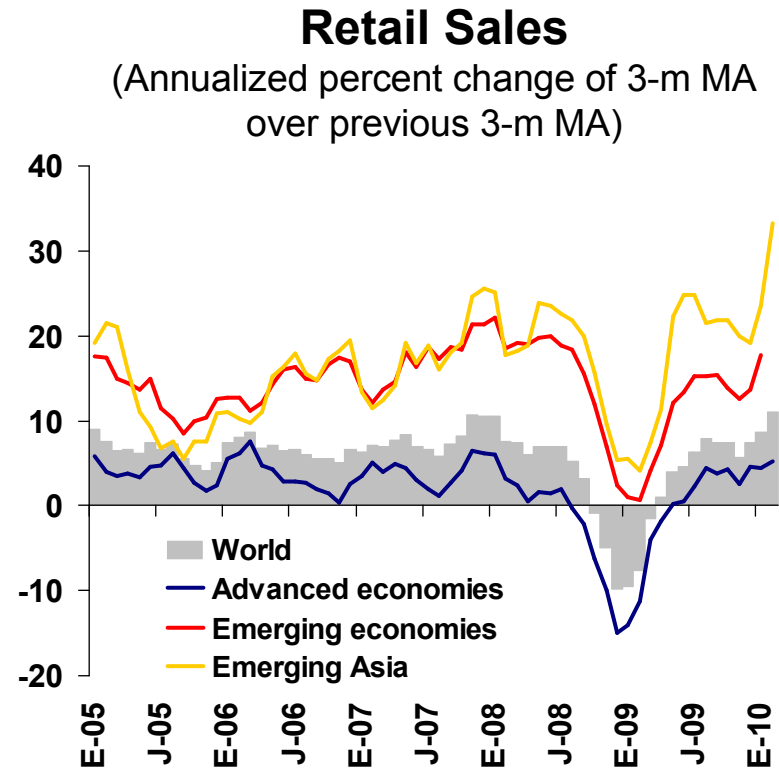
## Emerging and developing economies

- Strong final **domestic demand**, helped by the turn in the inventory cycle
- **External demand** was lifted by the normalization of global trade.

# Economic Indicators – Consumption



Source: IMF



Source: IMF

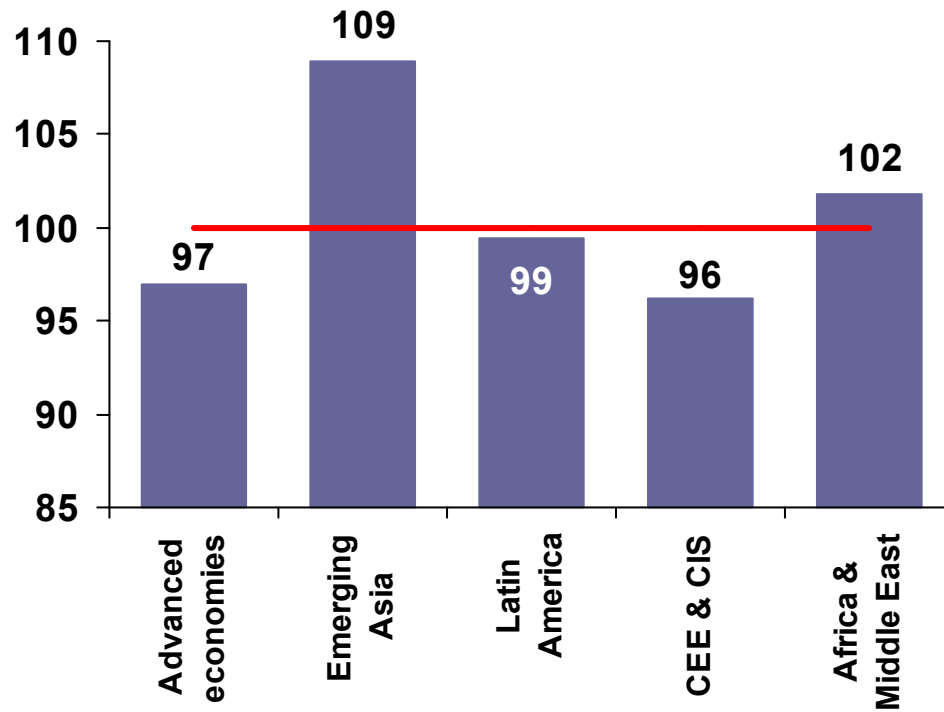
Consumer spending growth has remained solid, partly on the back of a turn in business spending and hiring.

This turn in business behavior is taking place across the globe and appears to be generating a bounce in capital spending

# Looking Forward - GDP

## Change in GDP

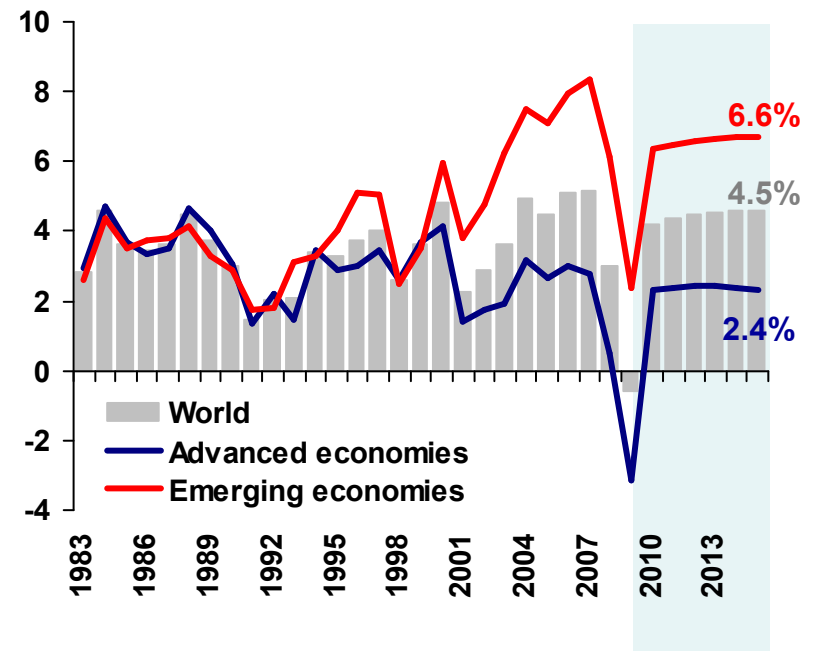
(2009:Q4 GDP in % of 2008:Q2 GDP)



Source: IMF

## GDP

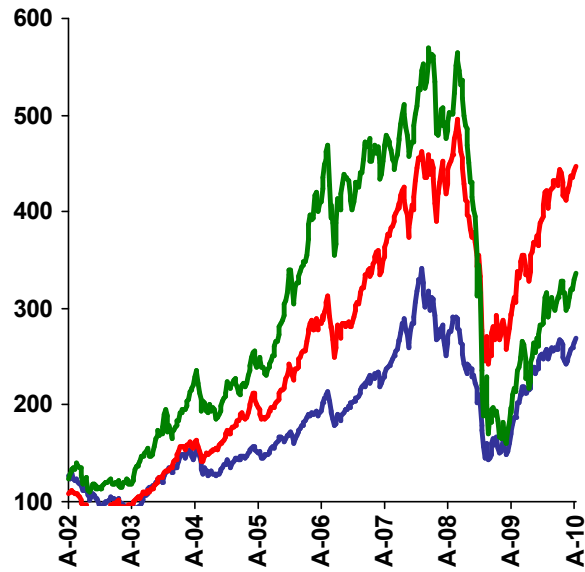
(Annual % change)



Source: IMF

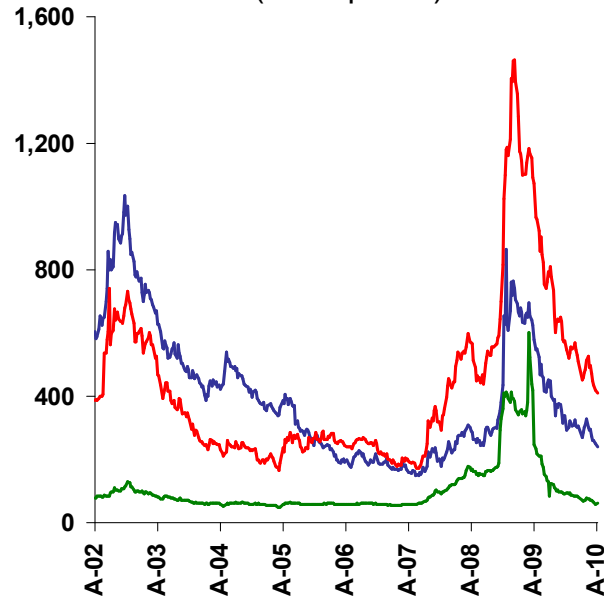
# Market Conditions: recovery to pre-crisis levels?

**Equity Markets**  
(2001 = 100)



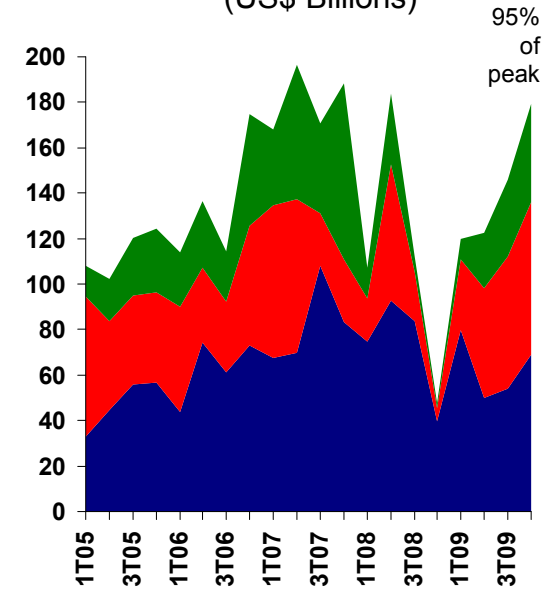
Source: IMF

**Interest Rate Spreads**  
(basis points)



Source: IMF

**EM Issuance**  
(US\$ Billions)



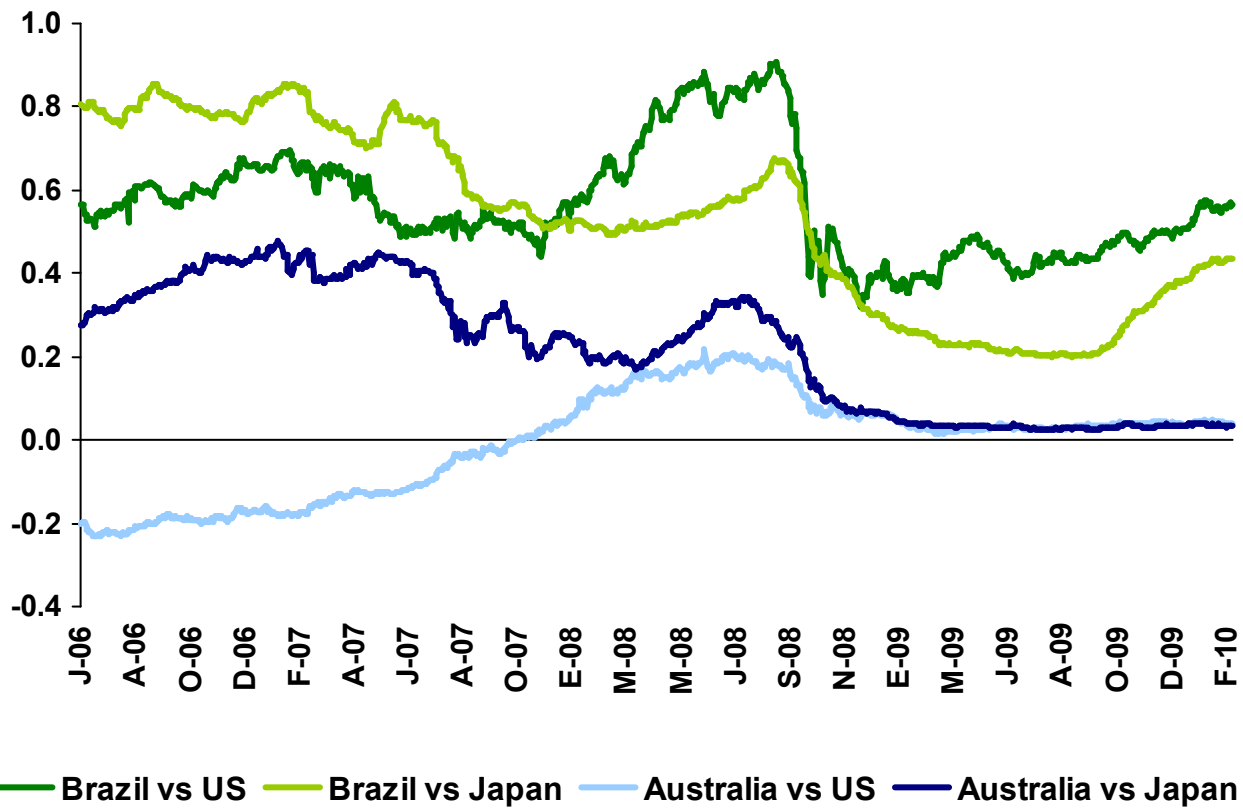
Source: JP Morgan

	Equities (Index)			Bonds (bps)			Issuances (US\$ Bill)*		
	Asia	Latin America	Eastern Europe	EM Bond Index	USB	USAAA	Sindic Loans	Bonds	Equity
<b>% of peak</b>	<b>79%</b>	<b>90%</b>	<b>59%</b>	<b>89%</b>	<b>82%</b>	<b>99%</b>	<b>75%</b>	<b>160%</b>	<b>85%</b>

\* Average of for quarters previous / following to the crisis (4T08)

# Incentives for carry trade are recovering

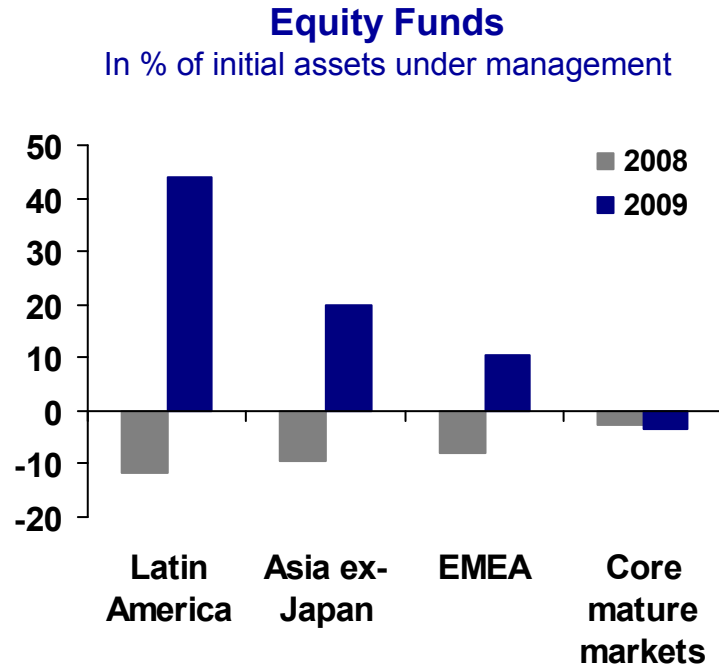
## Incentives for Foreign Currency Carry Trades are Recovering



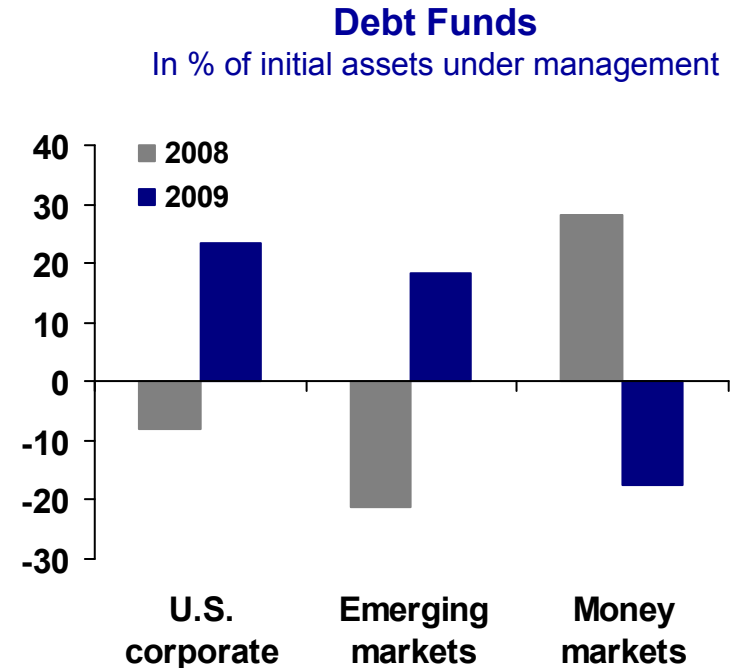
Source: IMF

# Portfolio flows have rebounded strongly

## Cumulative Retail Net Flows to Equity and Debt Funds



Source: IMF



Source: IMF

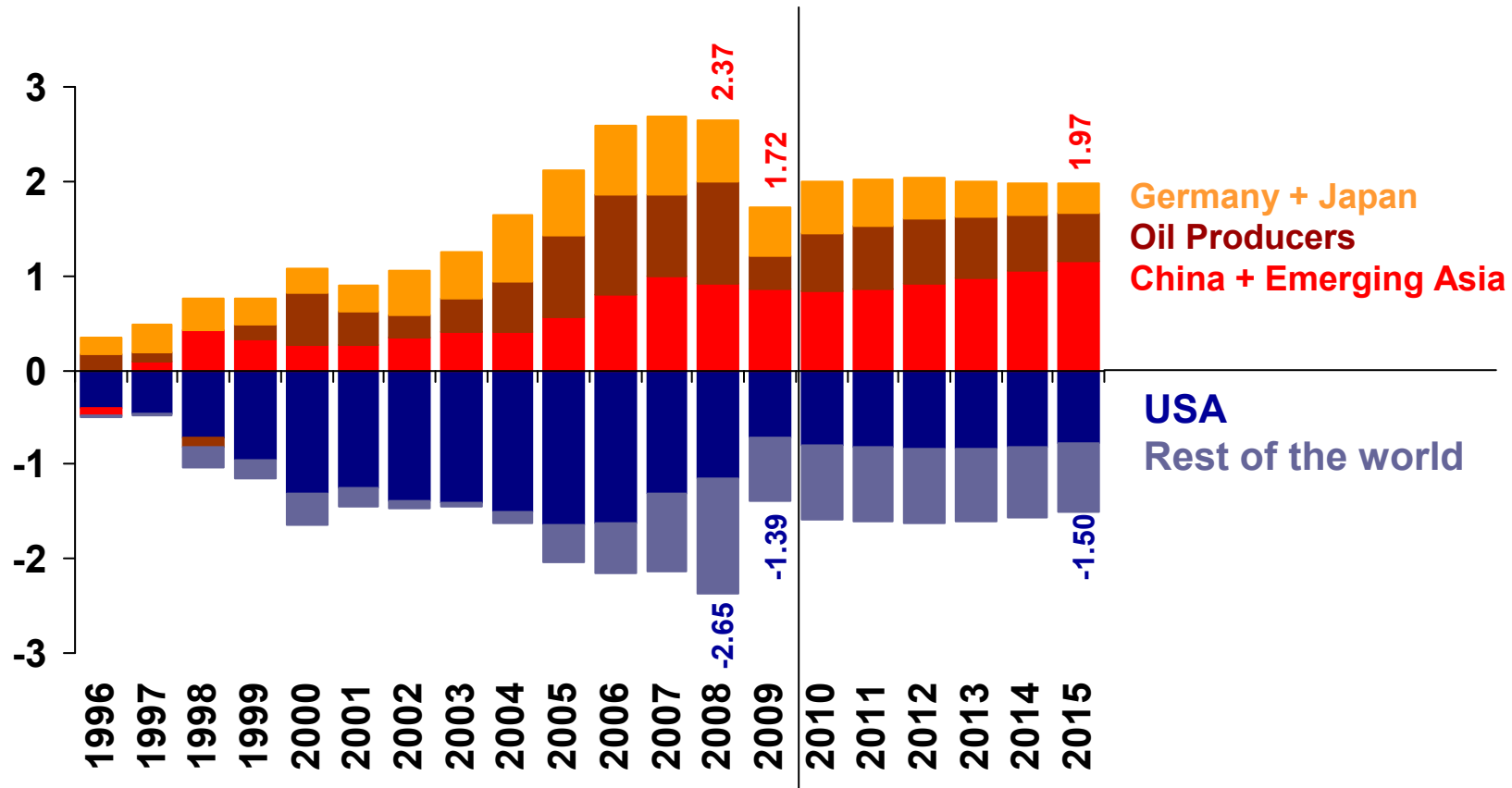
Key drivers behind the renewed capital flows:

- Rapid growth in emerging economies
- Large yield differentials in their favor,
- Returning appetite for risk.

Renewed flows have eased financial conditions in many emerging economies and prompted some authorities to be watchful of increasing property prices,



# Looking Forward - Global Imbalances



Source: IMF

## Global current account imbalances (2008-2009): temporary narrowing

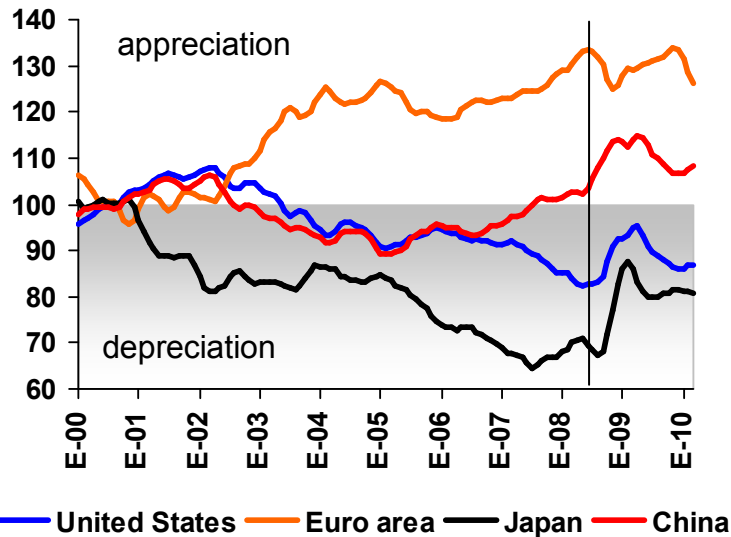
- China: surplus fell from 9.5% to 5.75% of GDP (slump in global trade + steep rise in public spending)
- US: deficit fell from 5% to 3% of GDP (household savings rose and investment slumped)
- Both benefited from lower oil prices, which in turn reduced the surpluses of Middle East
- IMF estimates: current account imbalances will rise as global trade continues to recover, financing improves, and commodity prices stabilize at higher levels

# Exchange Rates

## Real Effective Exchange Rate

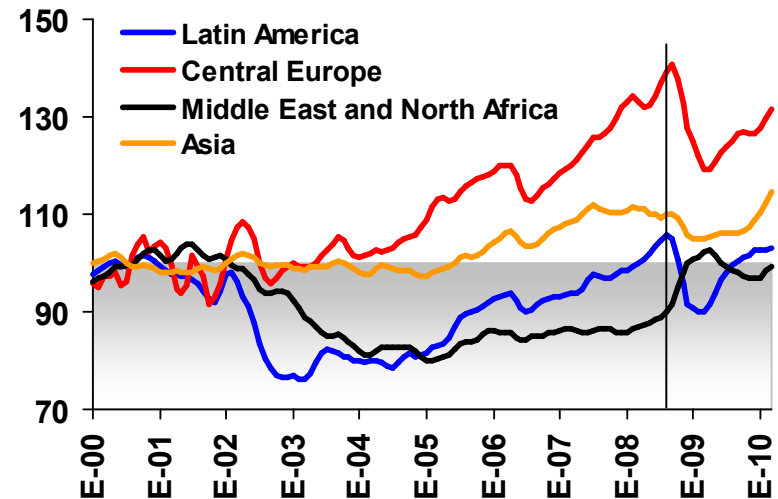
(Index, 2000 = 100; three-month moving average unless noted otherwise)

### Major Currencies



Source: IMF

### Developing Economies

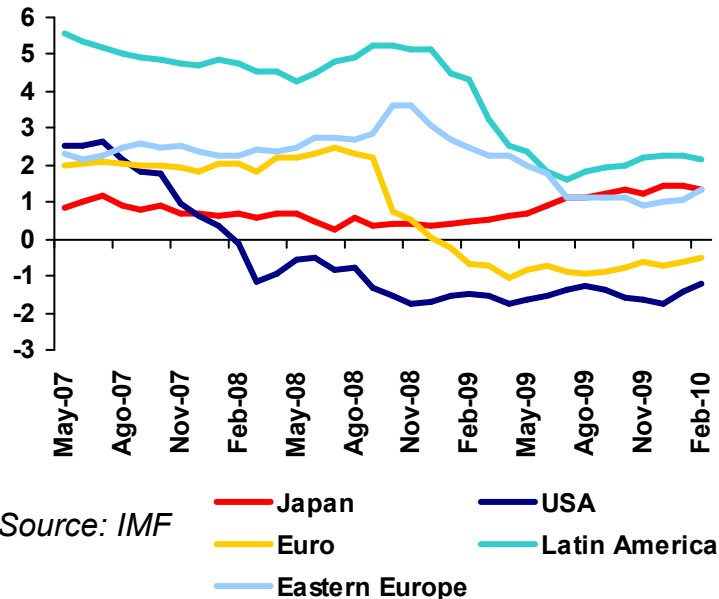


Source: IMF

- Recovery of cross-border flows: depreciation of the U.S. dollar
- Appreciation of other currencies: generally been limited compared with pre-crisis levels
- Countries in line with fundamentals (Middle East, Emerging Europe, Latin America Japan)
- Currencies undervalued (Emerging Asia, especially the renminbi)
- Currencies overvalued relative to medium-term fundamentals (U.S. dollar and euro)

# Monetary adjustment: unconventional liquidity provision

## Real Policy Interest Rates (Annual)

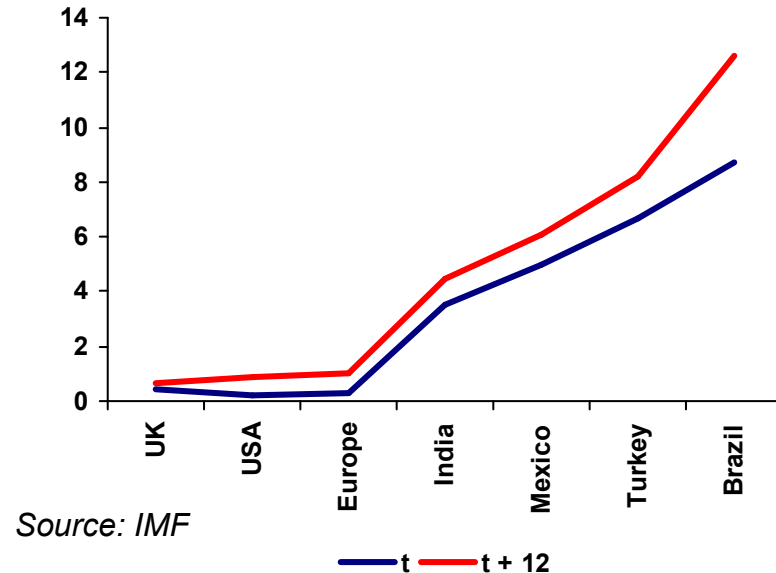


**Policy rates:** record lows, close to zero in many advanced economies.

Exceptional measures

- Public commitments to keep interest rates low for an extended time
- Purchases of long-term government bonds to reduce long-term yields,
- Support for dysfunctional markets (asset-backed securities)

## Real Interest Rates Forecasts (Annual)



**Large economies:**

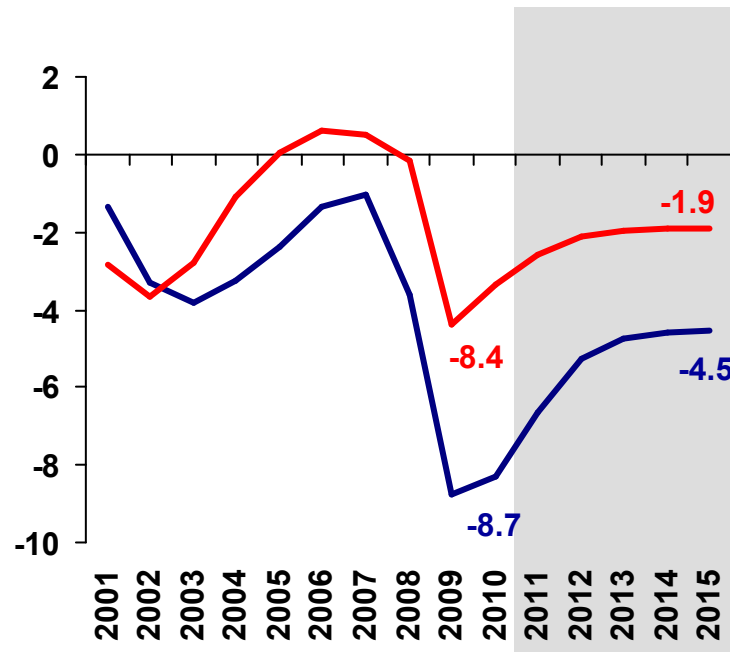
Central bank balance sheets expanded rapidly

**Emerging Economies:**

- Introduction of special liquidity or credit facilities (alleviate shortage of dollar funding)
- Government guarantees and capital injections provided indispensable backing to the system.

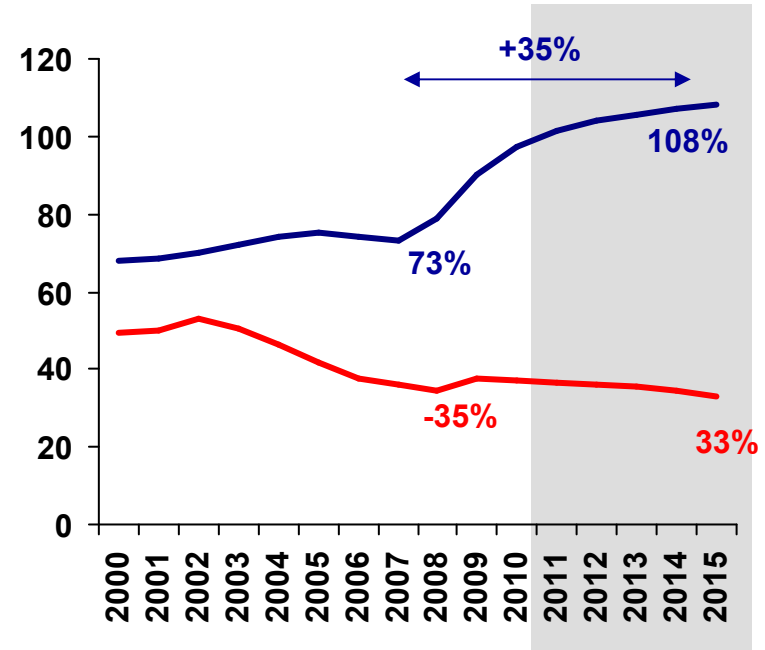
# Policy Support: Essential in Fostering Recovery

Fiscal Balance  
(% of GDP)



Source: IMF  
— Advanced economies  
— Emerging economies

Public Debt  
(% of GDP)



Source: IMF  
— Advanced economies  
— Emerging economies

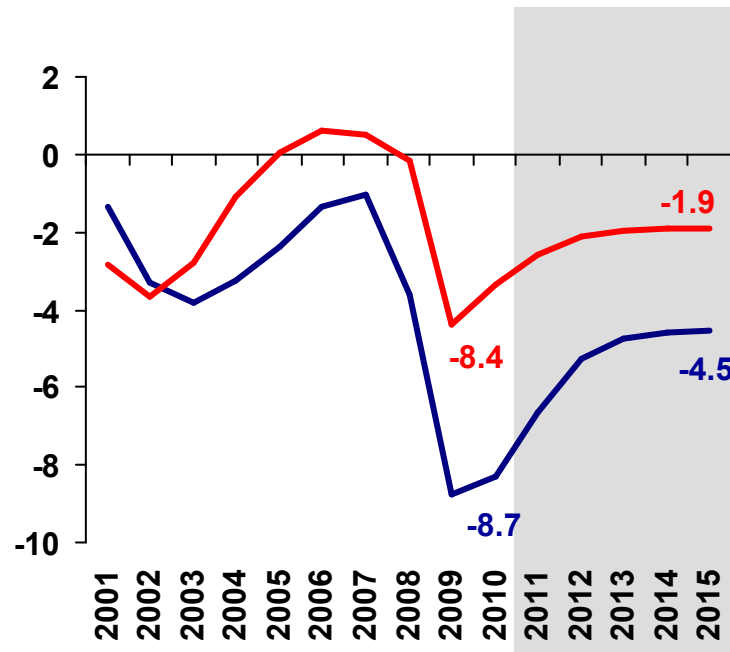
**Fiscal Policy:** major support especially in advanced economies.

- Slump in activity and stimulus measures pushed deficits in these economies up 9% of GDP
- Debt/GDP ratios, expected to exceed 100% of GDP in 2014 (35% higher than before the crisis)
- Fiscal deterioration: result of declines in output and tax payments from lower asset prices and diminished financial sector activity.
- Correction in primary balance needed to stabilize debt profile: 8% of GDP

Withdrawal of the stimulus measures will reduce government spending at most 1.5% of GDP

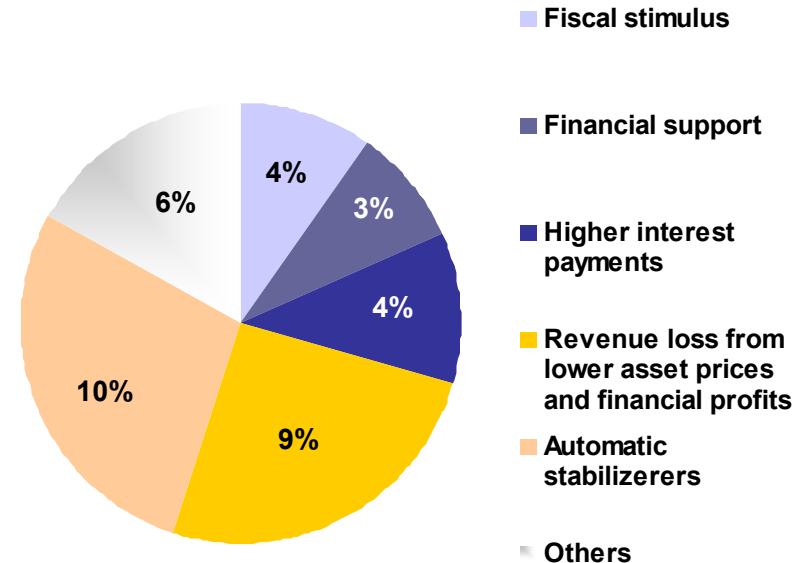
# Policy Support: Essential in Fostering Recovery

Fiscal Balance  
(% of GDP)



Source: IMF  
— Advanced economies  
— Emerging economies

Decomposition of Government Debt Increase, 2007–14  
(debt Increase: 35% of GDP)



Source: IMF

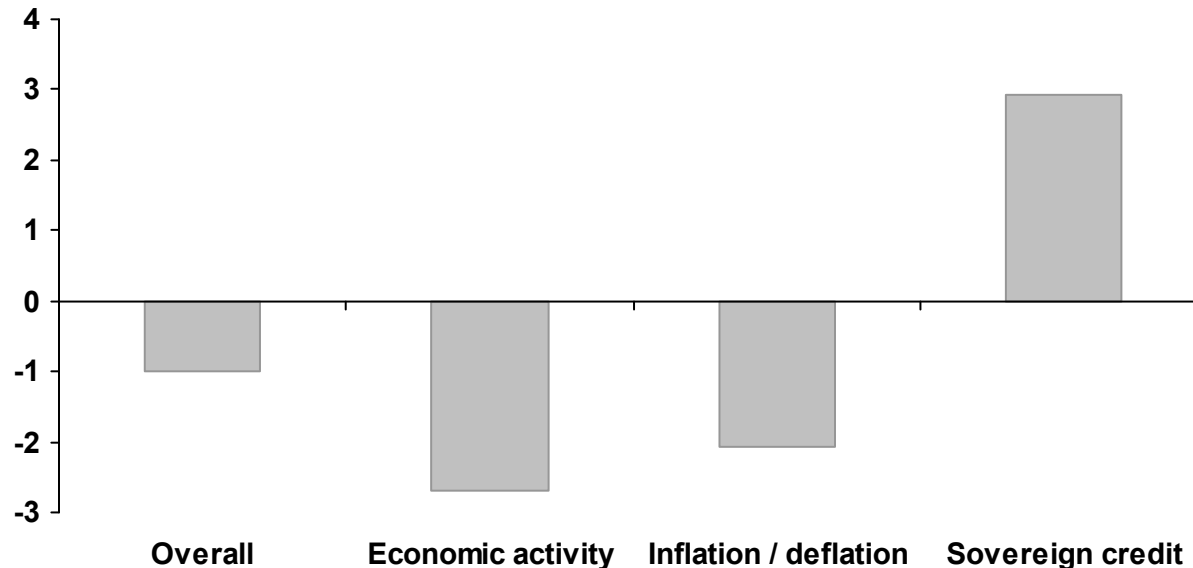
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# Important Risks Remain

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Macroeconomic Risks in the Global Financial Stability Map  
(Changes in notches in the past 6 months)



- Room for policy maneuvers in advanced economies are largely exhausted or very limited
- Potential for positive financial surprises is lower. Systemic risks originating in the financial sector have fallen further
- Growth of public debt in advanced economies, have become sharply more evident:
- Outlook for activity remains unusually uncertain.
- Risks related to sovereign debt could depress output:
  - Premature withdrawal of fiscal stimulus
  - Households and investors could lose confidence in governments' ability to implement sound consolidation plans and in response could sharply reduce their spending
  - Abrupt changes in exchange rates that distort production

# Policymakers are faced with major challenges

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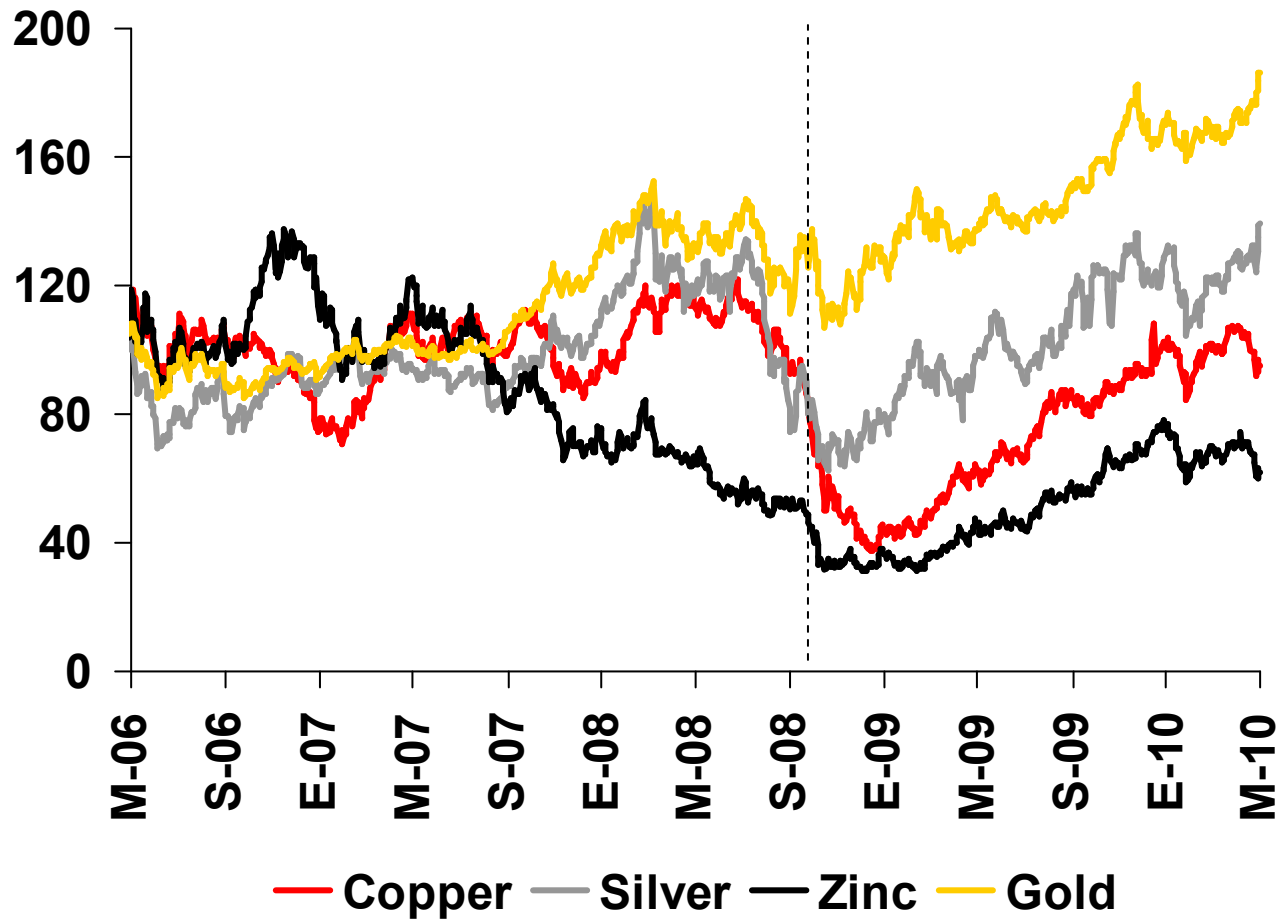
## Advanced Economies

- Consolidate public finances
  - Entitlement spending: can be changed only gradually  
(Health care reform would not impede the current recovery and would deal with the longer-term problems)
  - Broadening tax bases, especially by eliminating distortionary exemptions  
(Debt-financed consumption, or use of particular fuels)
  - Strengthening fiscal rules with explicit fiscal targets
  
- Repairing the financial sector: essential for sustained growth of private demand
  - Prudential policies and frameworks, authorities with broad powers
  - Higher capital requirements
  - Fees to cover bailout costs (ex ante and ex post);
  - Incentives to keep financial institutions smaller and more manageable
  - Direct restrictions on the size and scope of financial activities
  
- Rebalance demand away from the public and toward the private sector
  
- Combat pressures for trade and financial protectionism.

## Emerging economies

- Tap domestic sources for growth: demand from advanced economies will remain weaker than before the crisis
  
- Deal with exchange rate appreciation from surging capital inflows  
Concerns of short run destabilization of their external and financial markets may affect long run stabilization goals such as a stronger domestic demand and excessive current account surpluses

# Metals: behavior in the financial crisis

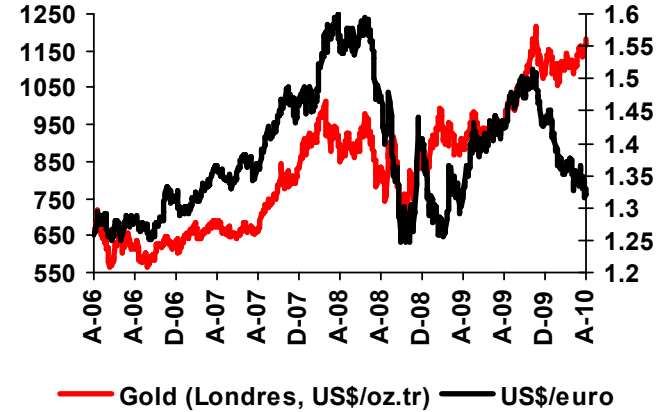
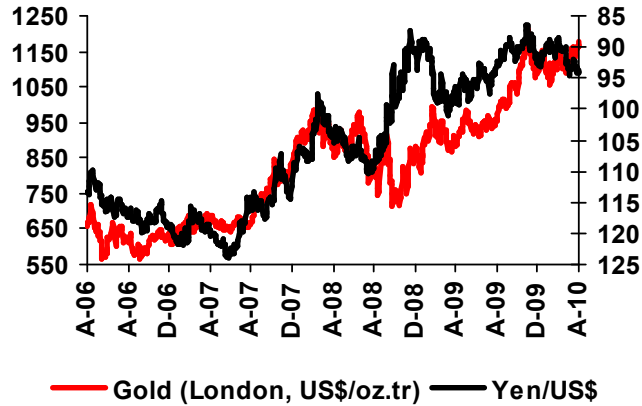


Source: Bloomberg

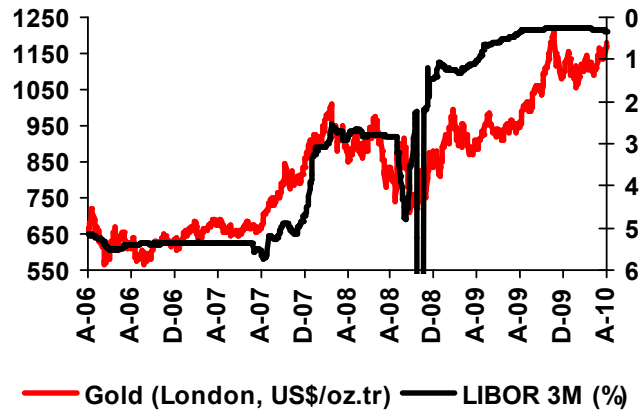


# Precious Metals: Correlation with Financials

## Gold price an US Exchange Rate

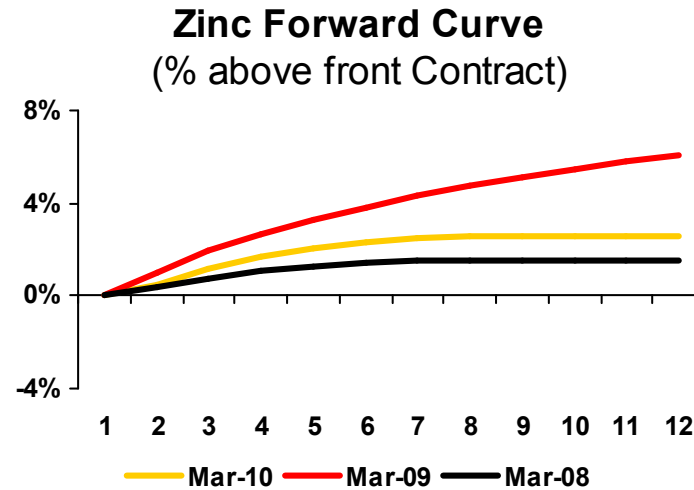
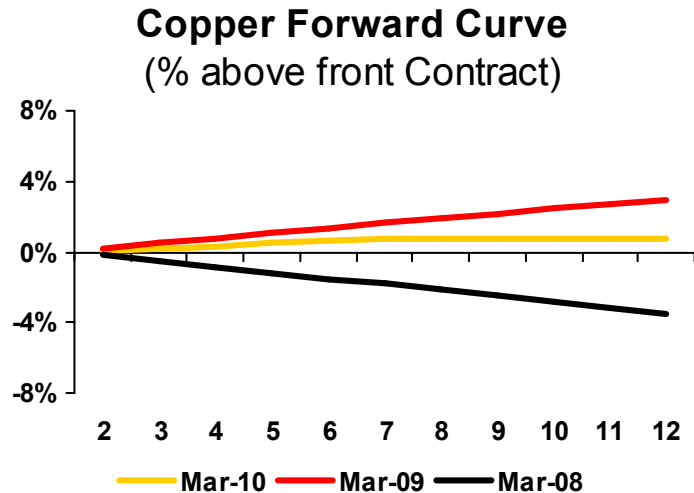
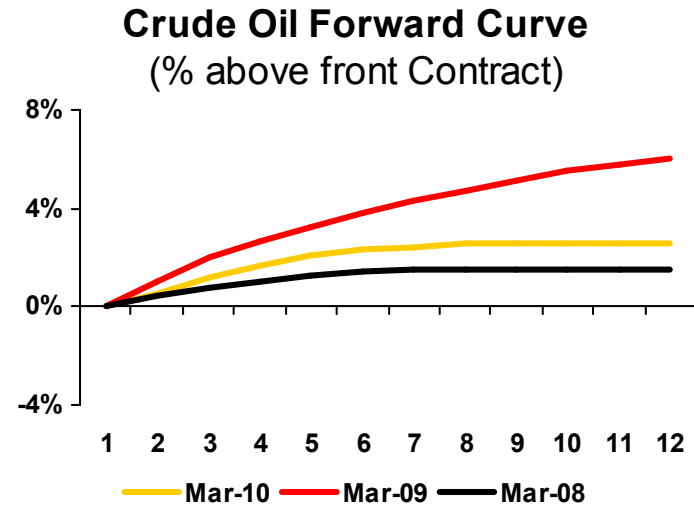
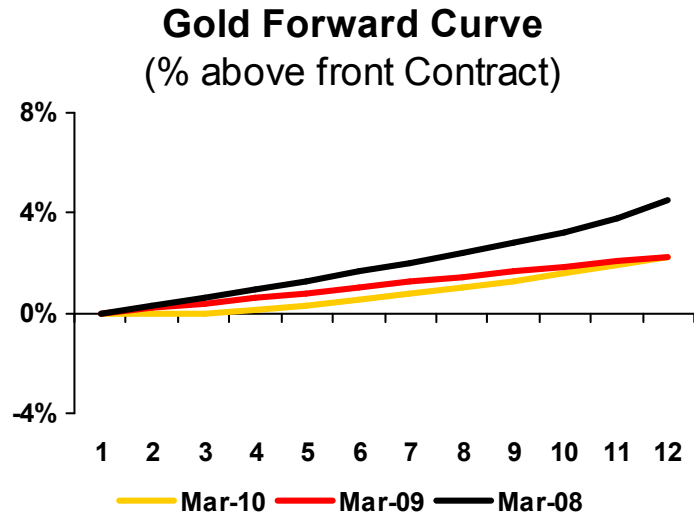


## Gold price an Market Interest Rate



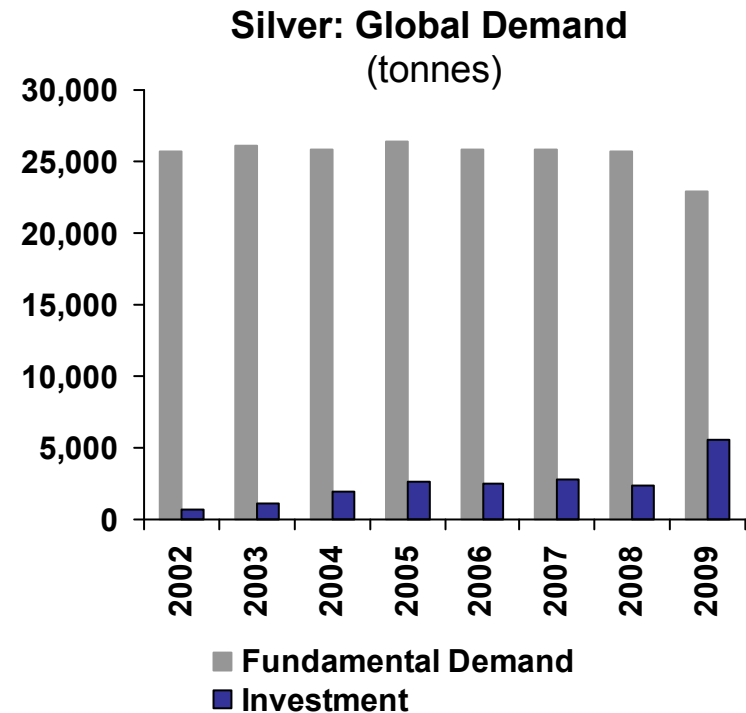
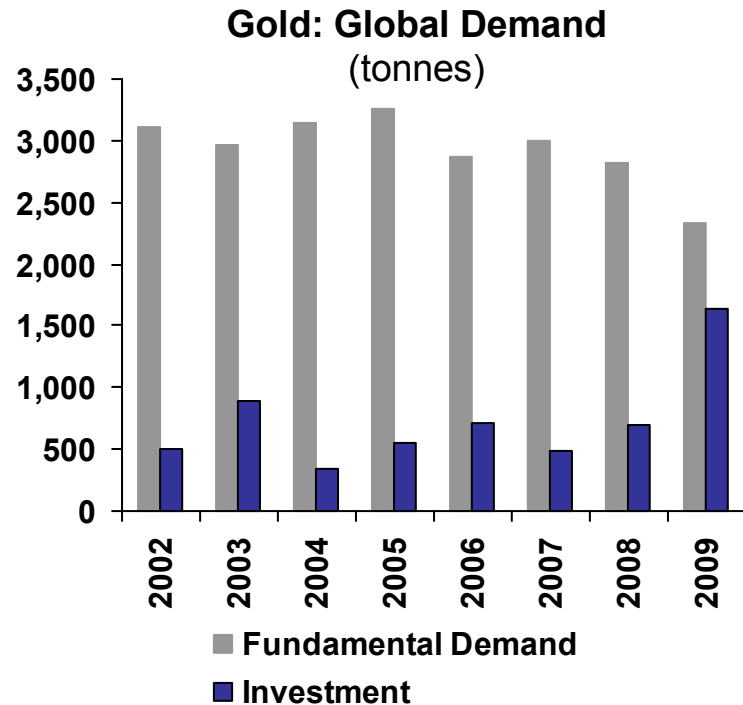
	Gold	Silver	Zinc	Copper
Yen/US\$	-87%	-37%	79%	46%
Euro/US\$	-56%	-74%	32%	-37%
Libor 3M	-84%	-51%	63%	26%
Gold		73%	-64%	-10%
Silver			-11%	45%
Zinc				58%
Copper				

# Precious Metals: Short Run Prospects



Source: JP Morgan

# Speculative Investment: loosing strength?



Source: Morgan Stanley

## Demand risks

- A rising US dollar and stabilizing financial markets pose a risk to sustained investment demand, especially ETF inflows
- In the absence of renewed financial crisis in the US, this pattern can continue, with negative implications for ETF inflows and the gold price.

# Conclusions

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Stronger than expected recovery

- Emerging Asia: growth already surpassed pre-crisis levels
- Global growth led by emerging economies (especially Asia)
- Unprecedented policy support was essential in fostering recovery
- Portfolio flows show solid rebound: risks of bubble formation in the financial markets (housing prices, currencies, equities, credit)

Major challenges

- Financial sector reform
- Public finances consolidation
- Rebalance of world demand from public to private sector and from US to emerging economies

Precious metals

- Downside risks: due to gold's strong correlation with financials, the stabilization of the world financial markets imposes limits to gold demand
- Upside risks: strong prospects of fundamental demand due to the emerging world incidence in global growth prospects

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