

COMMENTS ON:
Exchange Rate Regimes & Structural
Realignment of Global Economies

By

Subacchi & Rossi

Chatham House

November 2009

Susan M. Collins

University of Michigan

Outline

- Interesting & Provocative Paper
 - Wide Ranging Essay: Look Back & Ahead
 - Combine country examples with regional data
- Summarize Main Arguments
 - Parts 1-4: Output Performance- Review
 - Parts 5-6: Currency & Exchange Rates
 - Elaborate and/or Alternative View
- Themes
 - Crisis: Importance of Openness
 - Rebalancing: Mature vs. Emerging
 - Prognosis for \$
- Agenda for Future Research

(1) Paper Highlights Regional Variation of Crisis Impact

- Developing economies surprisingly resilient relative to mature economies
 - Note: considerable variation w/in region
- Relative stability in Latin America & Asia
 - Striking - historical high LA volatility
 - Emerging Europe: L.A. déjà vu?

BUT:

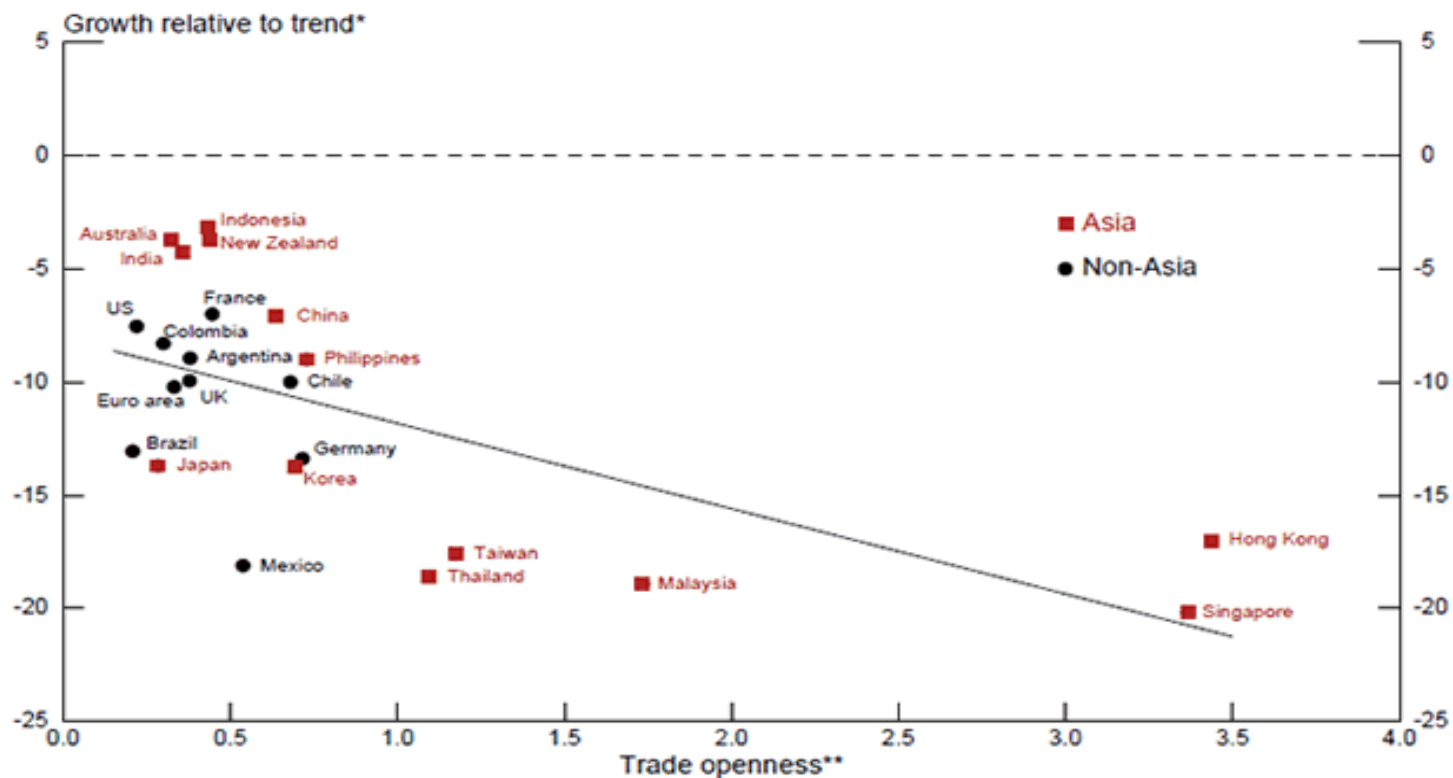
- Chart 1-Regional Averages?
 - Understanding recent divergences in growth
- Outcomes mix implications of impact & (mitigating) response

(2): Highlights Key Role of Trade

- Countries most open to trade hit hardest (Table 1 in paper, See Chart)
- Deep trade contraction due to
 - Advanced country demand collapse
 - Freeze of trade credits (perhaps unclear?)
- Expand other Factors: Long list
 - Trade Related:
 - where in global supply chain, trade composition (durables; mfg vs services)
 - Financial Openness – difficult to measure?
 - ‘Structural’ Issues, Flexible markets

Exhibit 2

Trade Openness and GDP Growth (2008Q4 - 2009Q1)

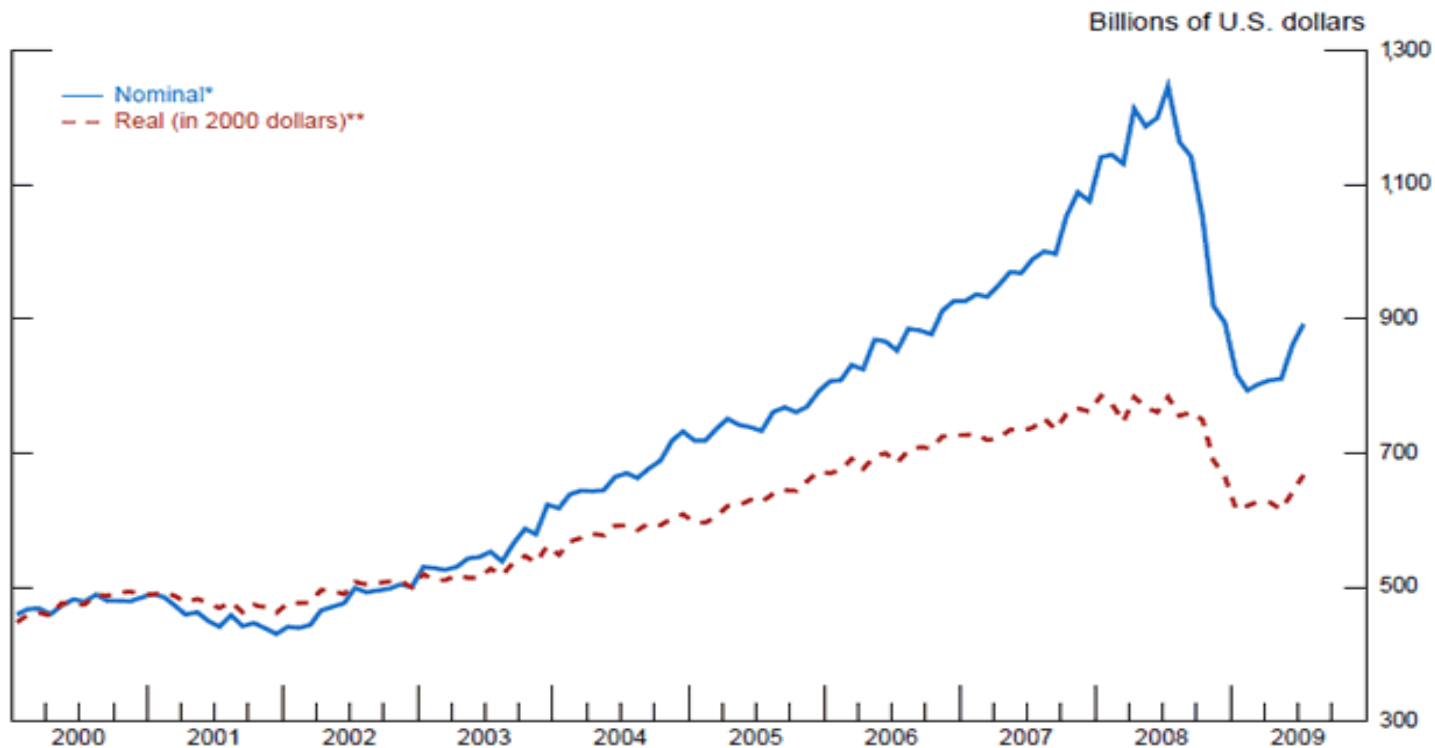


*Growth relative to trend is the percentage point difference between the realized rate of growth during 2008Q4 and 2009Q1, measured at an annual rate, and trend growth. Trend growth is the average annualized growth rate during 2006 and 2007 of smoothed gross domestic product (GDP) using the Hodrick-Prescott filter.

** $(\text{Exports} + \text{Imports}) / \text{GDP}$ in 2007.

Source: CEIC, Haver, and staff estimates.

Exhibit 1
Global Merchandise Exports



*The nominal data are the sum of the total merchandise exports of 44 economies, including the United States, expressed in U.S. dollars.

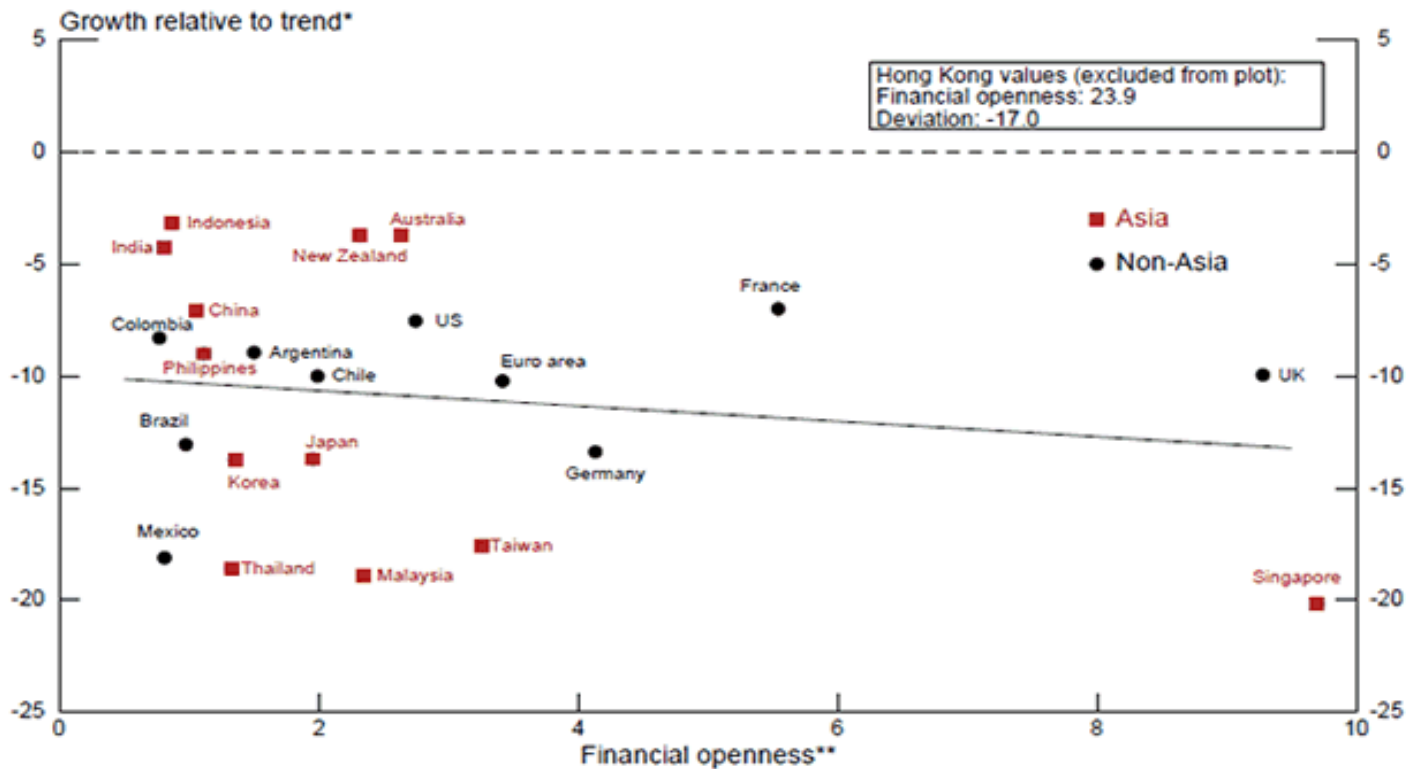
**The real data are calculated by deflating dollar-value nominal exports by export price indexes constructed from local-currency deflators drawn from country sources and dollar exchange rates.

Source: CEIC, Haver, and staff estimates.

Why did trade fall so sharply?

- Severe Recession –
 - Caroline Freund (WB) elasticities have risen and are higher in recession
- Credit Squeeze Cut Trade Finance– How Big?
 - Anecdotal evidence mixed
 - Role of MNCs?
- Global Supply Chain – source domestically
- Uncertainty: Consumer Durables, Investment

Exhibit 3
Financial Openness and GDP Growth
 (2008Q4 - 2009Q1)



*Growth relative to trend is the percentage point difference between the realized rate of growth during 2008Q4 and 2009Q1, measured at an annual rate, and trend growth. Trend growth is the average annualized growth rate during 2006 and 2007 of smoothed gross domestic product (GDP) using the Hodrick-Prescott filter.

** $(\text{International Assets} + \text{Liabilities}) / \text{GDP}$ in 2007.

Source: CEIC, Haver, and staff estimates. International investment position data are from Haver and the U.S. Bureau of Economic Analysis.

(3): Key Mitigating Factors?

- Paper Highlights both
 - Structural Factors
 - incl. service share of output
 - Policy Responses
 - Fiscal & monetary stimulus
 - Prior macro balances – stimulus feasibility
- Need to clarify distinction between explaining impact and mitigation

(4): Future Growth Prospects for Emerging vs. Mature Economies

- Mature – sluggish growth prospects?
 - Chart 8: highlight weak 2010
 - Chart 2: 2011-14 similar to 2000-07
 - 2.5% growth, some LDCs catching-up
 - Significant uncertainty to forecasts esp. in transition ‘out of stimulus’
- Emerging markets ‘rosy picture’
 - Continued potential in Emerging Asia
 - (Emerging Europe notable exception)
 - Where are the markets for their output?

(5): Crisis Impact on Currencies

- Most Asian & LA economies avoided currency collapse
 - ER Flexibility
 - Usage of accumulated reserves (temporary)
 - ‘Corners Hypothesis’ Debunked!
- Eastern Europe – more traditional BOP crisis reactions
 - Lessons from Asia & LA
 - Revisit BOP Crisis literature

(6) Currency Trends: What is Plausible?

- Argues that falling \$ is implausible due to implications for other currencies
 - Collapse vs MR to LR \$ decline?
 - Parts (1)-(4) on Emerging Economy Strength?
- Failure to reduce US CA deficit implausible? vulnerable for future crises...
- Uncertainties in near term – longer focus
- Alternative scenarios
 - Shift global demand to emerging markets
 - Revitalize Investment: produce for LDC mrkts
 - Newly vibrant economies – currency strengthen

Research Topics:

- Giving up Option to Realign: Euro Zone
- Exchange Rate Regime Performance
- Benefit/Cost of Reserve Accumulation
- BOP Crises: The 'Next' Generation

Research Topics: BOP Crises Once Again

- Multiple episodes; single shock
- Relative importance of
 - ‘weak fundamentals’
 - Exchange rate regime
 - ‘currency mis-matches’
 - Debt levels vs. ‘original sin’
 - Policy response: Internally; role of IMF

Summary

- Interesting, informative, provocative paper
 - Covers lots of ground!
- Highlights maturing of emerging markets in Latin America as well as Asia
 - Calls into question some dimensions of old ‘conventional wisdom’
- Future scenarios (\$) – speculative
- Points to series of potentially important research projects