IMF Sees ‘Alarmingly High’ Risk of Deeper Global Slump

By Sandrine Rastello - Oct 9, 2012

The International Monetary Fund cut its global growth forecasts as the euro area’s debt crisis intensifies and warned of even slower expansion unless officials in the U.S. and Europe address threats to their economies.

The world economy will grow 3.3 percent this year, the slowest since the 2009 recession, and 3.6 percent next year, the IMF said today, compared with July predictions of 3.5 percent in 2012 and 3.9 percent in 2013. The Washington-based lender now sees “alarmingly high” risks of a steeper slowdown, with a one-in-six chance of growth slipping below 2 percent.

“A key issue is whether the global economy is just hitting another bout of turbulence in what was always expected to be a slow and bumpy recovery or whether the current slowdown has a more lasting component,” the IMF said in its World Economic Outlook report. “The answer depends on whether European and U.S. policy makers deal proactively with their major short-term economic challenges.”

The IMF’s 188 member countries convene in Tokyo this week as low growth damped by fiscal consolidation in the richest economies hurts developing counterparts from China to Brazil. As the IMF urged measures to boost confidence, uncertainties out of Europe show no sign of abating, with leaders still divided over a banking union and Spain resisting a bailout.

Confidence Fragile

“Confidence in the global financial system remains exceptionally fragile,” the IMF said. “Bank lending has remained sluggish across advanced economies” and increased risk aversion has damped capital flows to emerging markets, it said.

European stocks were little changed as the region’s finance ministers met in Luxembourg to discuss the sovereign-debt crisis. The Stoxx Europe 600 Index slipped less than 0.1 percent at 11:02 a.m. in London.

In Seoul, World Bank President Jim Yong Kim told a forum today that he saw mildly encouraging signs in Europe. In Tokyo, IMF Chief Economist Olivier Blanchard indicated that yields on Spanish and Italian bonds, which decreased after the European Central Bank’s bond-buying plan announcement, could rise if the countries don’t request bailouts.

The IMF report called for U.S. policy makers to find an alternative to planned automatic tax increases and spending cuts that would trigger a recession. Europeans must follow on their commitments for a more integrated monetary union, and many emerging markets can afford to cut interest rates or pause tightening to fight off risks to their economies, the IMF said.

“It is a call to action,” Blanchard told Bloomberg Television.

Europe’s Contraction

The 17-country euro area economy will contract 0.4 percent this year, 0.1 percentage point worse than forecast in July, and grow 0.2 percent in 2013, less than the 0.7 percent predicted three months ago, the IMF said.

The U.S. is seen expanding 2.2 percent this year, higher than an earlier forecast, and growing 2.1 percent next year, less than previously predicted. Japan’s estimate was cut to 2.2 percent this year and to 1.2 percent in 2013.

Spain’s economy will shrink 1.3 percent next year, 0.7 percentage point worse than predicted in July. German growth is seen at 0.9 percent each year, with the 2013 estimate half a percentage point less than previously forecast.

“Spain and Italy must follow through with adjustment plans that re-establish competitiveness and fiscal balance and maintain growth,” Blanchard wrote in a foreword to the report. “To do so, they must be able to recapitalize their banks without adding to their sovereign debt. And they must be able to borrow at reasonable rates.”

Emerging Economies
Growth forecasts were also lowered for emerging markets, where domestic factors add to external constraints, the IMF said. Brazil had some of the steepest cuts, with growth seen at 1.5 percent this year from 2.5 percent and 4 percent next year.

India’s economy may grow 4.9 percent this year and 6 percent next year, lower than previous forecasts of 6.2 percent and 6.6 percent respectively. China’s estimate was cut by 0.2 percentage point each year to 7.8 percent in 2012 and 8.2 percent in 2013.

Monetary policy should remain accommodative in developed economies, with expectations for slower inflation giving the European Central Bank “ample justification for keeping policy rates very low or cutting them further,” the IMF said. The Bank of Japan may need to ease further, it said.

Other risks to the global economic outlook in the short term include a renewed increase in oil prices and an inability to raise the U.S. debt ceiling, it said.

The IMF forecasts assume oil at $106.18 a barrel this year and $105.10 next year, based on the average prices of U.K. Brent, Dubai and West Texas Intermediate crudes. That compares with estimates of $101.80 and $94.16 in July.

Japan’s Trade

In economic releases in the Asia Pacific region today, Japan reported a larger-than-estimated 454.7 billion yen ($5.8 billion) current-account surplus. In Australia, business confidence recovered in September as the prospect of interest-rate reductions overshadowed weaker sentiment among miners and manufacturers, a private survey showed.

In South Korea, the central bank said today that the nation’s economy faces increased external risks and the finance ministry said it will step up efforts to boost growth.

In Europe, the U.K. may report today that industrial production fell in August, a Bloomberg News survey of economists indicates.

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