U.S. Monetary Policy and Emerging Markets' Challenges

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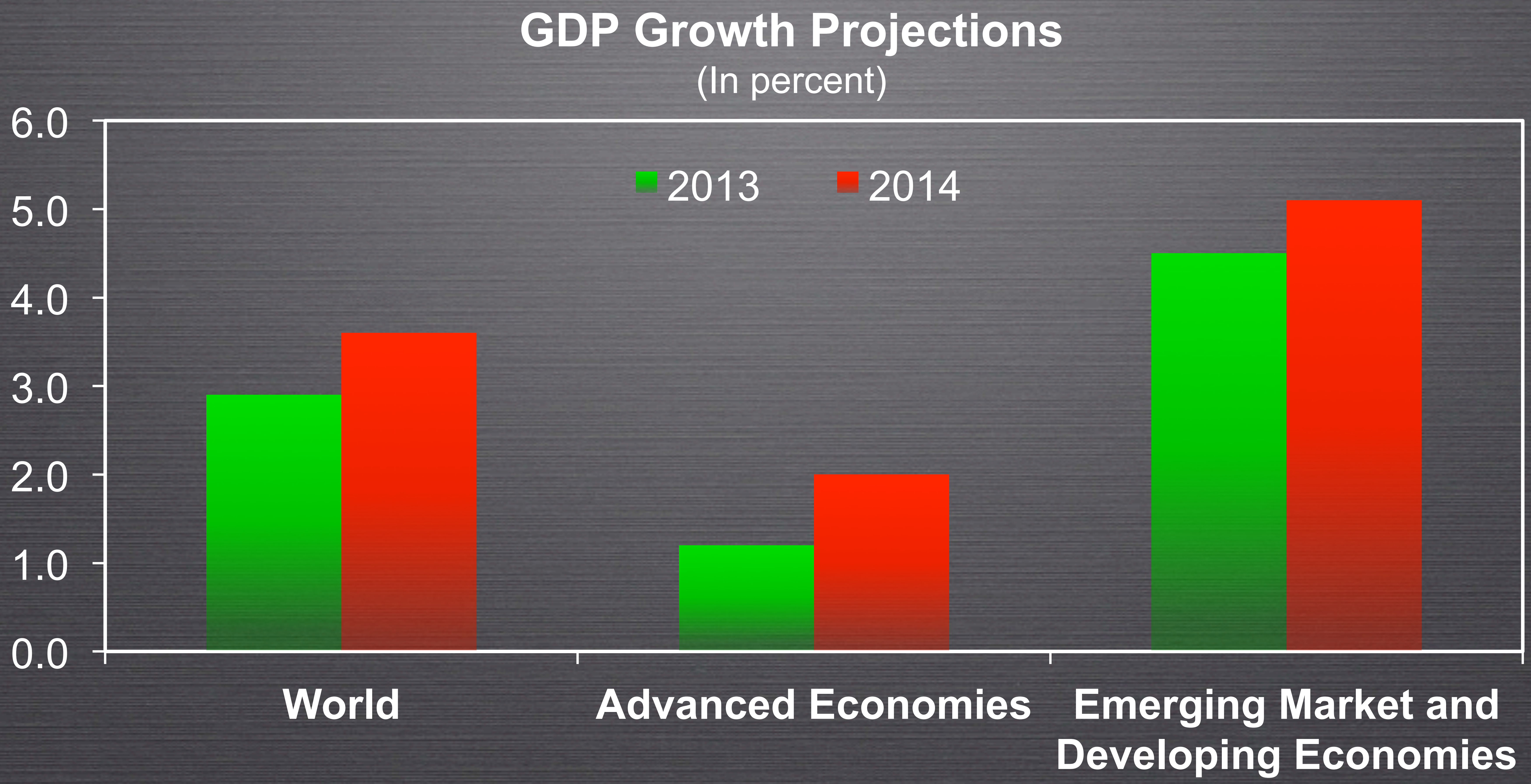
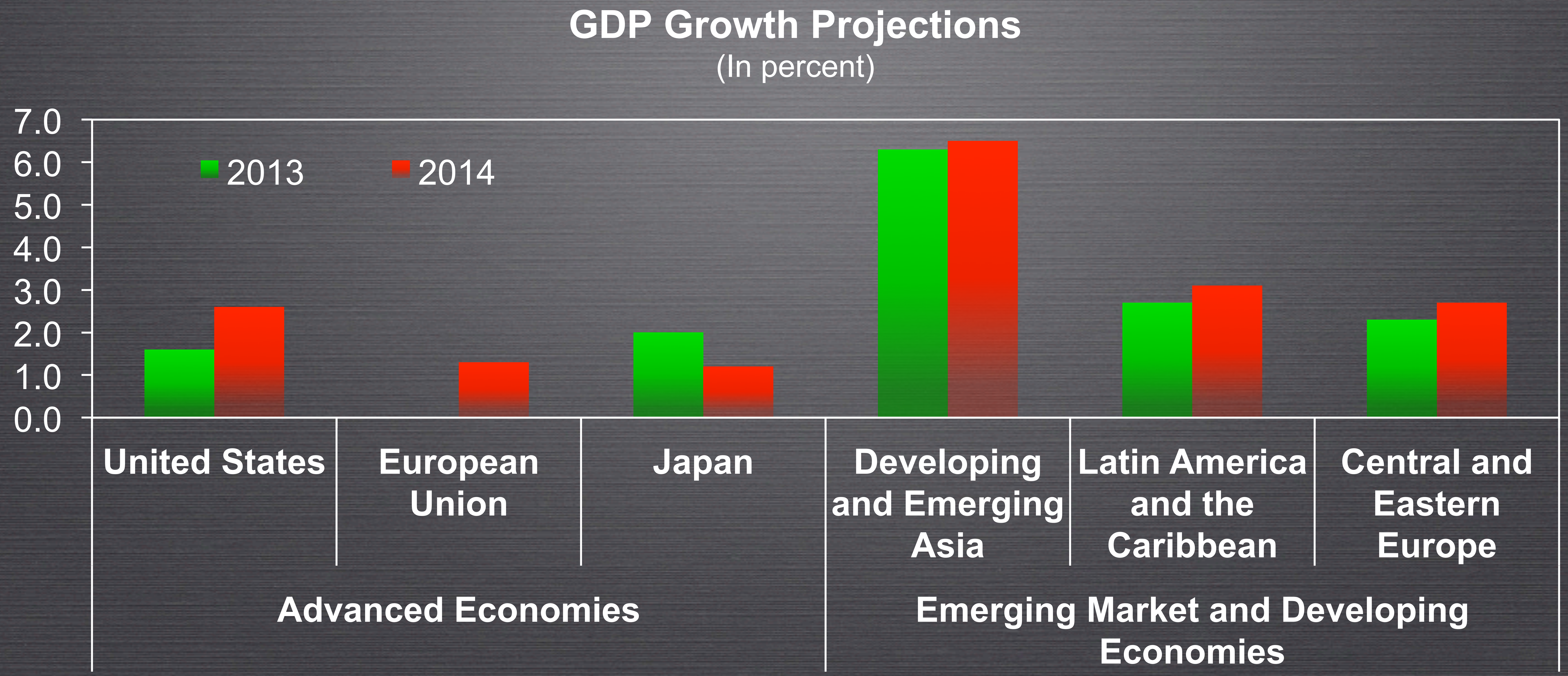
CEMLA, October, 2013

Recovery of the global economy continues …



Source: World Economic Outlook (WEO, October 2013)

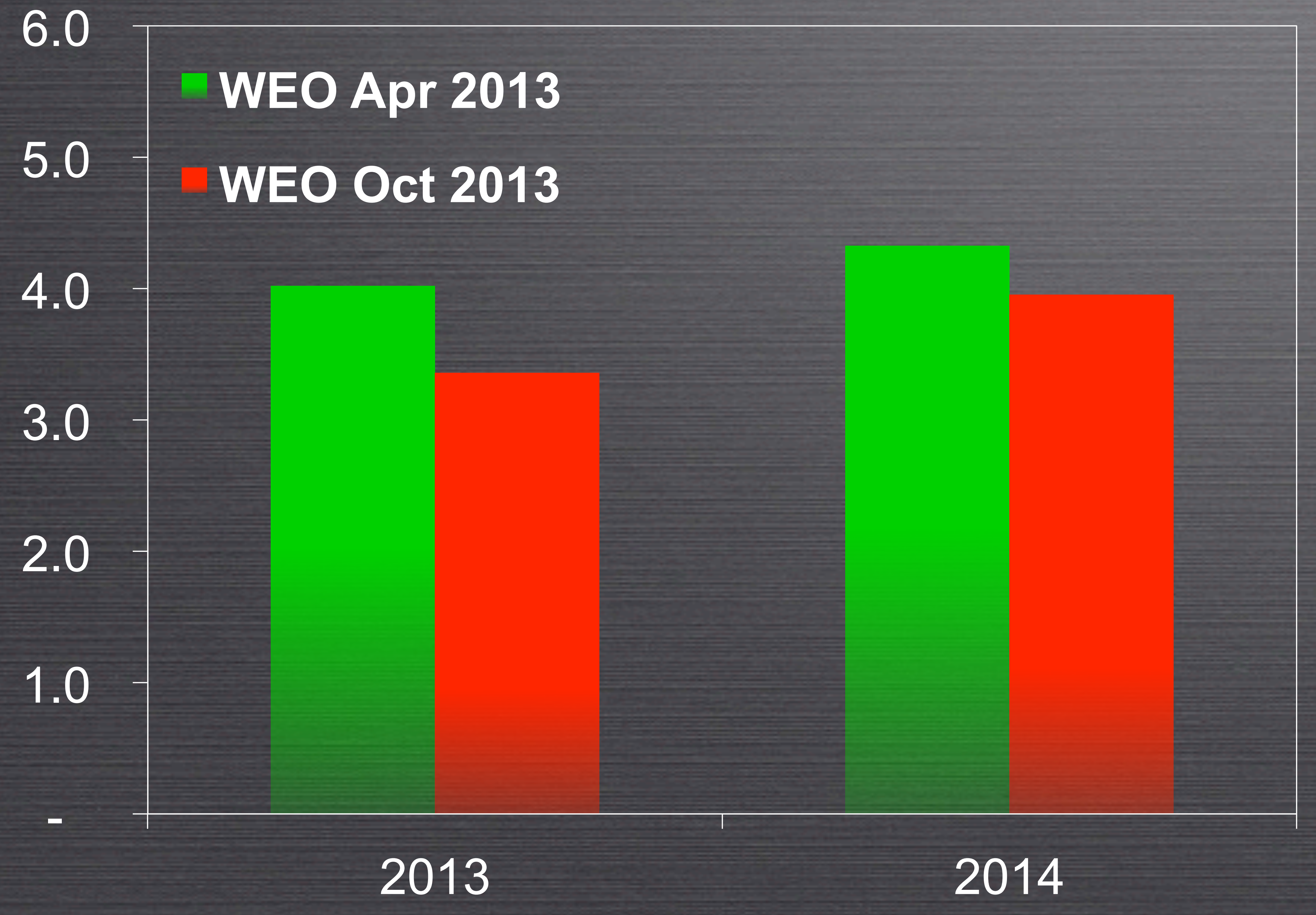
… with regional differences



Source: World Economic Outlook (WEO, October 2013)

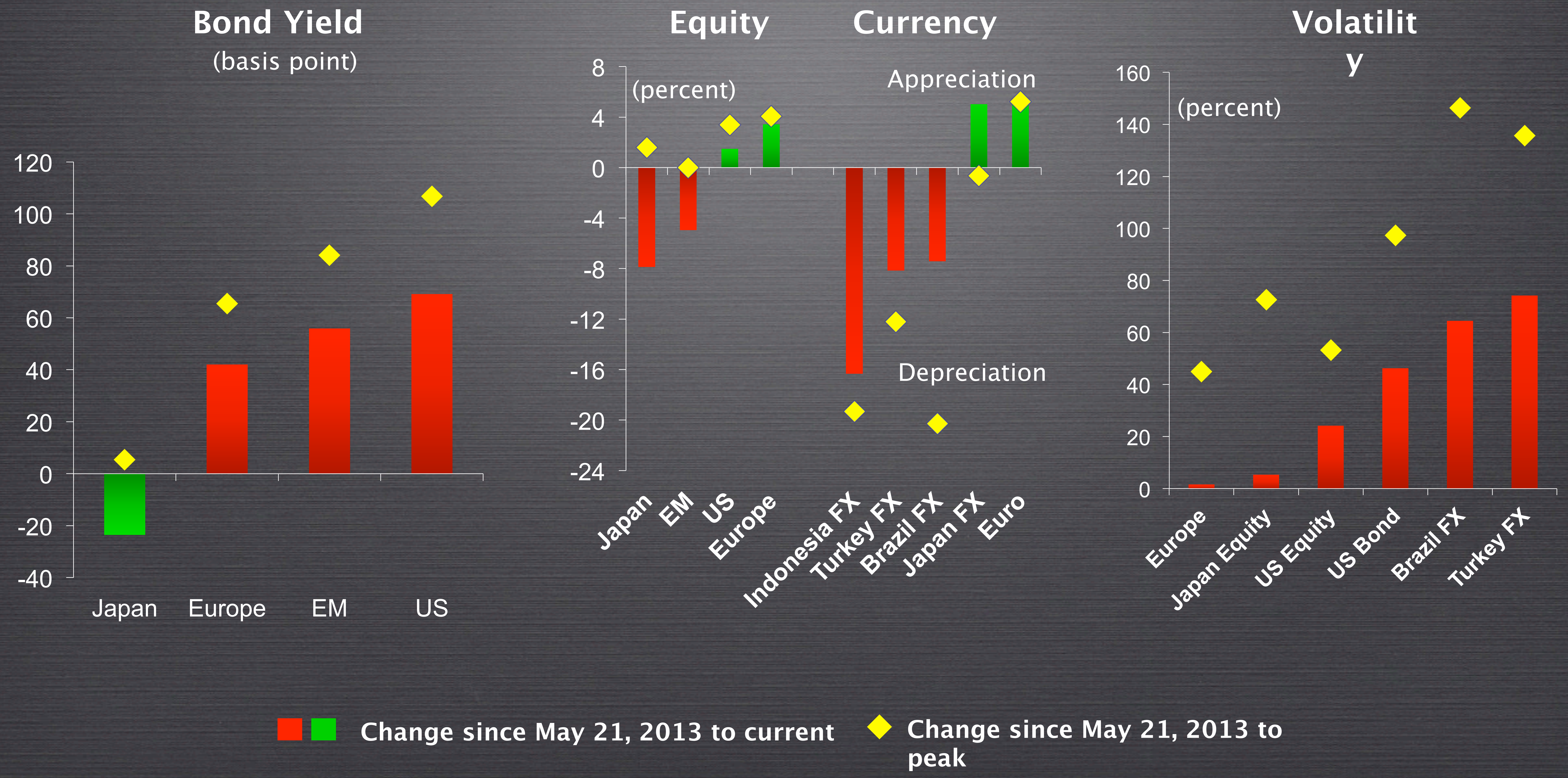
Key challenges for emerging markets: internal and external

Emerging Markets - GDP Growth Projections
(In percent)



10 Year U.S. Government Bond Yield

Recent market turbulence: temporary or more to come?

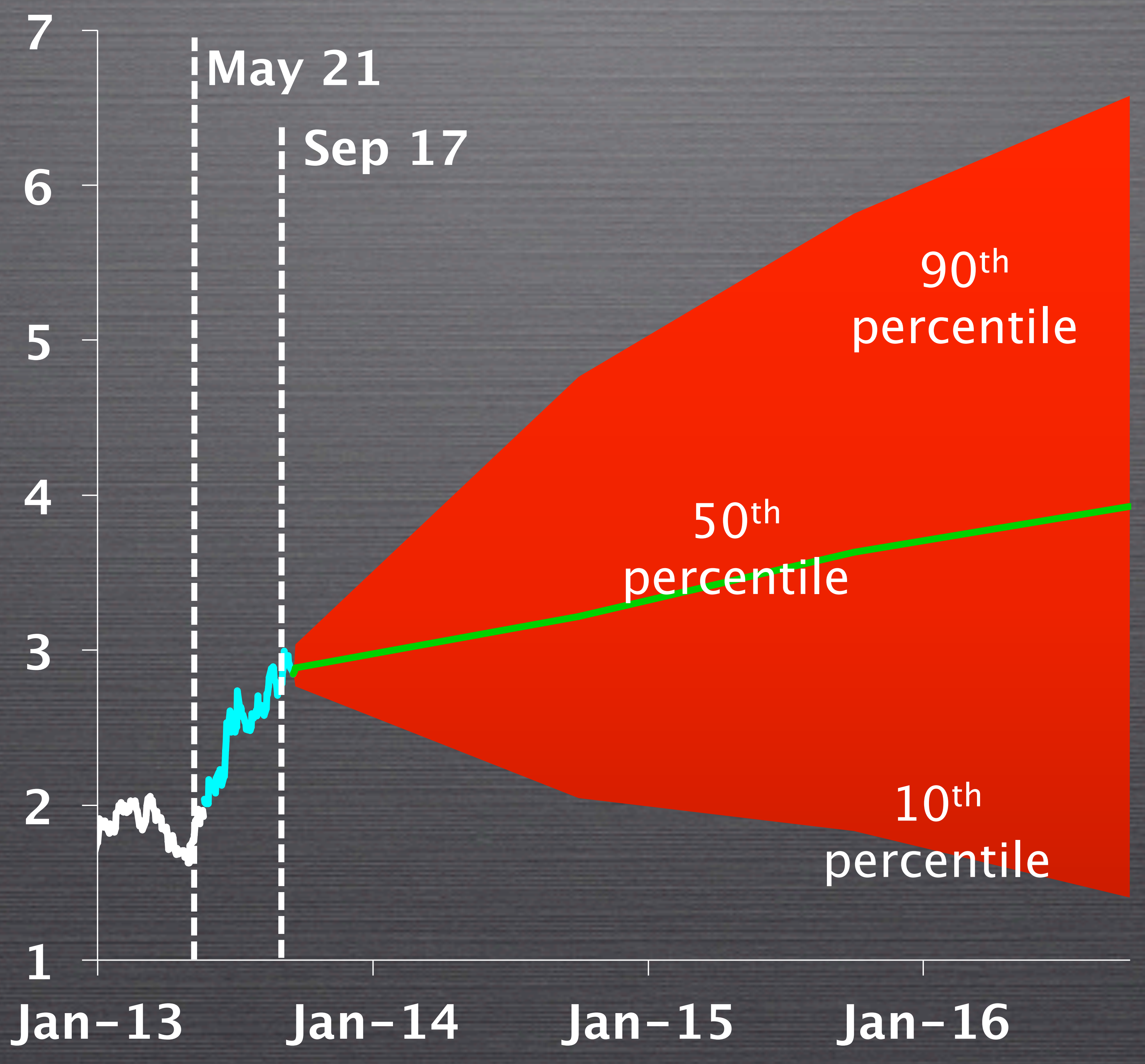


How will the U.S. monetary exit be?

Smooth

- Gradual recovery expected
- Tapering smooth and tightening gradual
- Much already "priced in"
- Volatile adjustment largely behind us

US 10-year Treasury Yield
(percent)

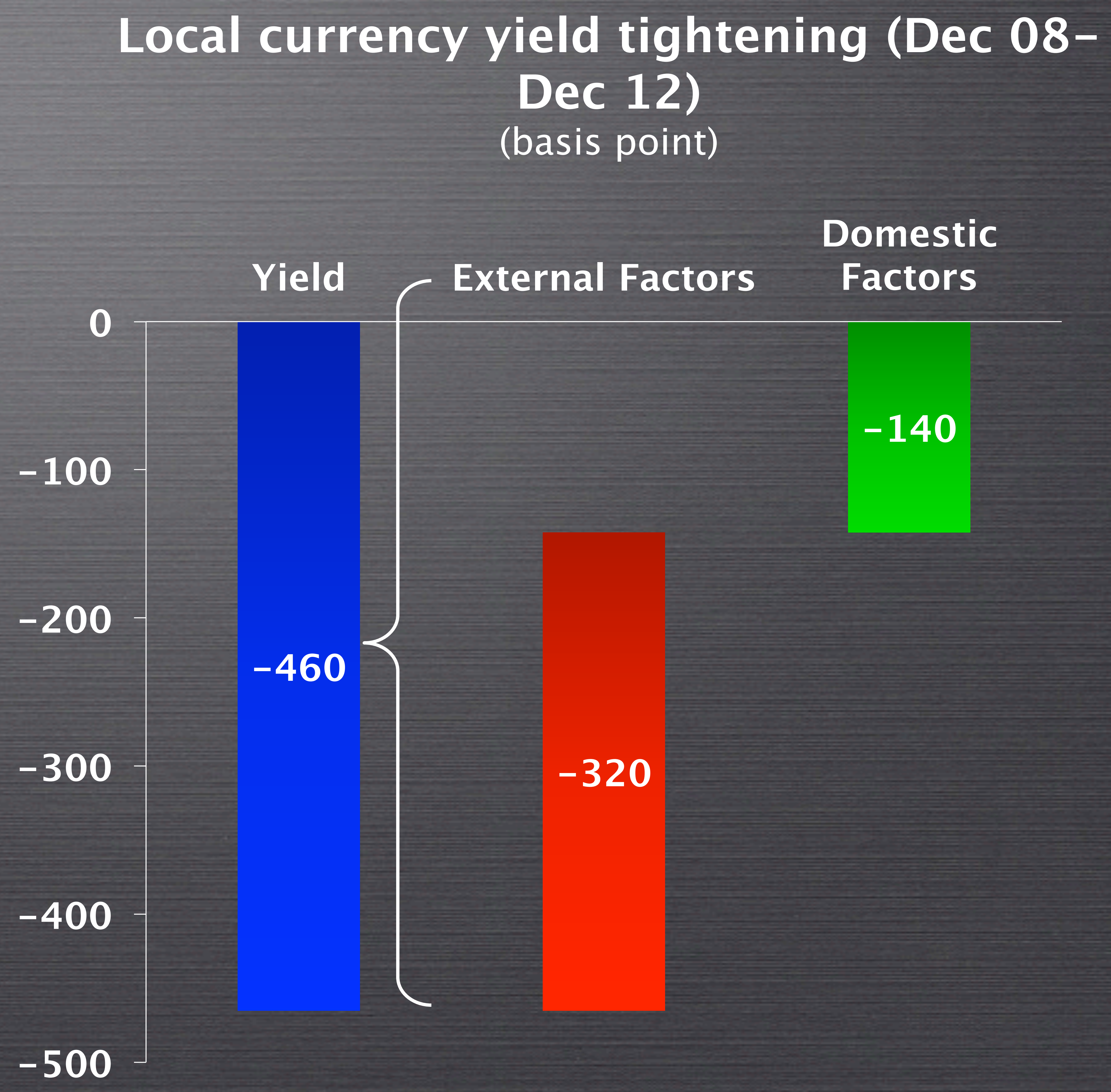


Bumpy

- Timing of recovery uncertain
- Tapering has not even started, let alone tightening
- Unchartered territory
- Fed doesn't control long-term rates
- Potentially destabilizing market dynamics

Potential impact on emerging markets

- External conditions
- Quality of domestic fundamentals

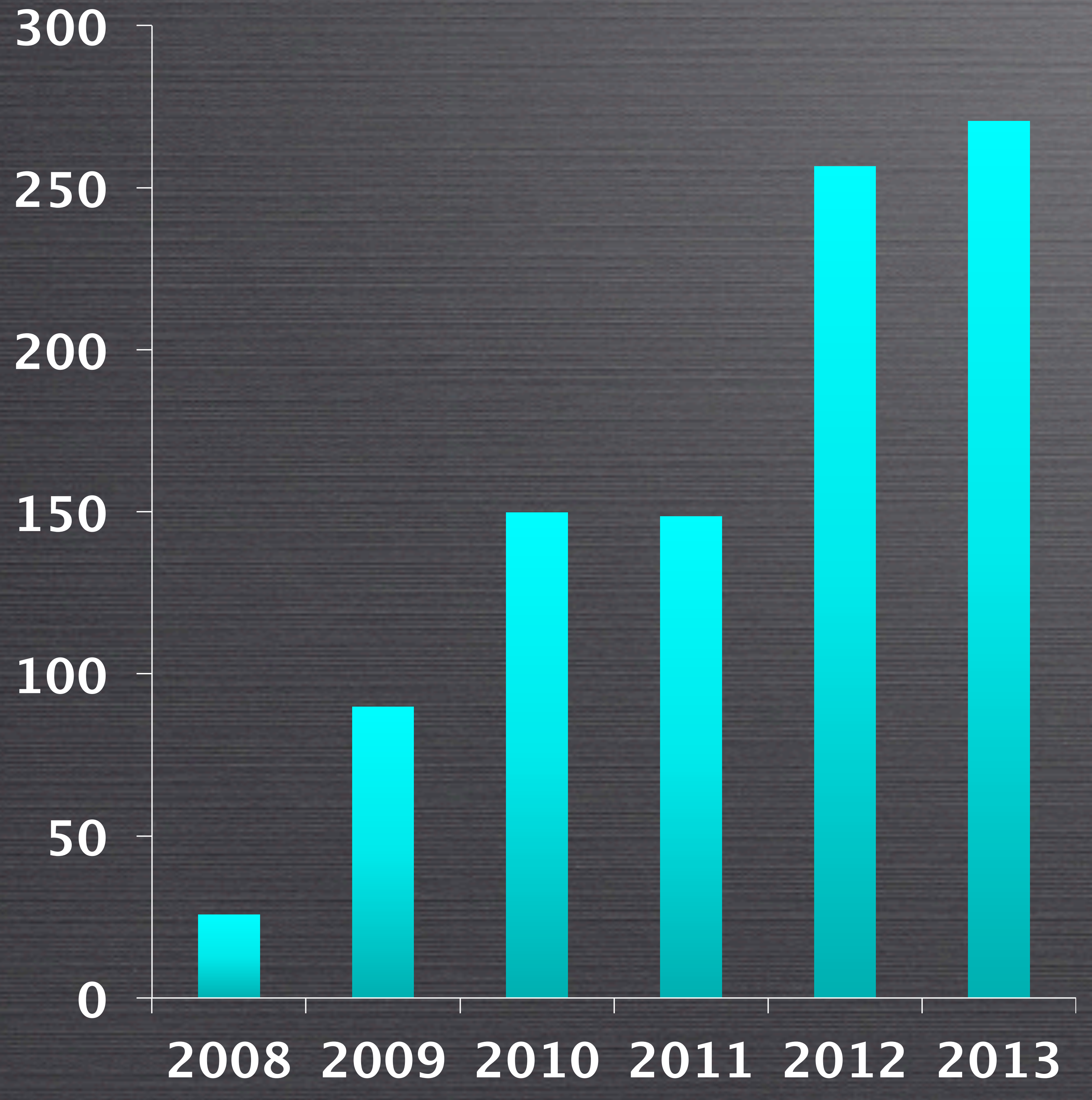


Volatility amplifiers in the U.S. monetary exit process

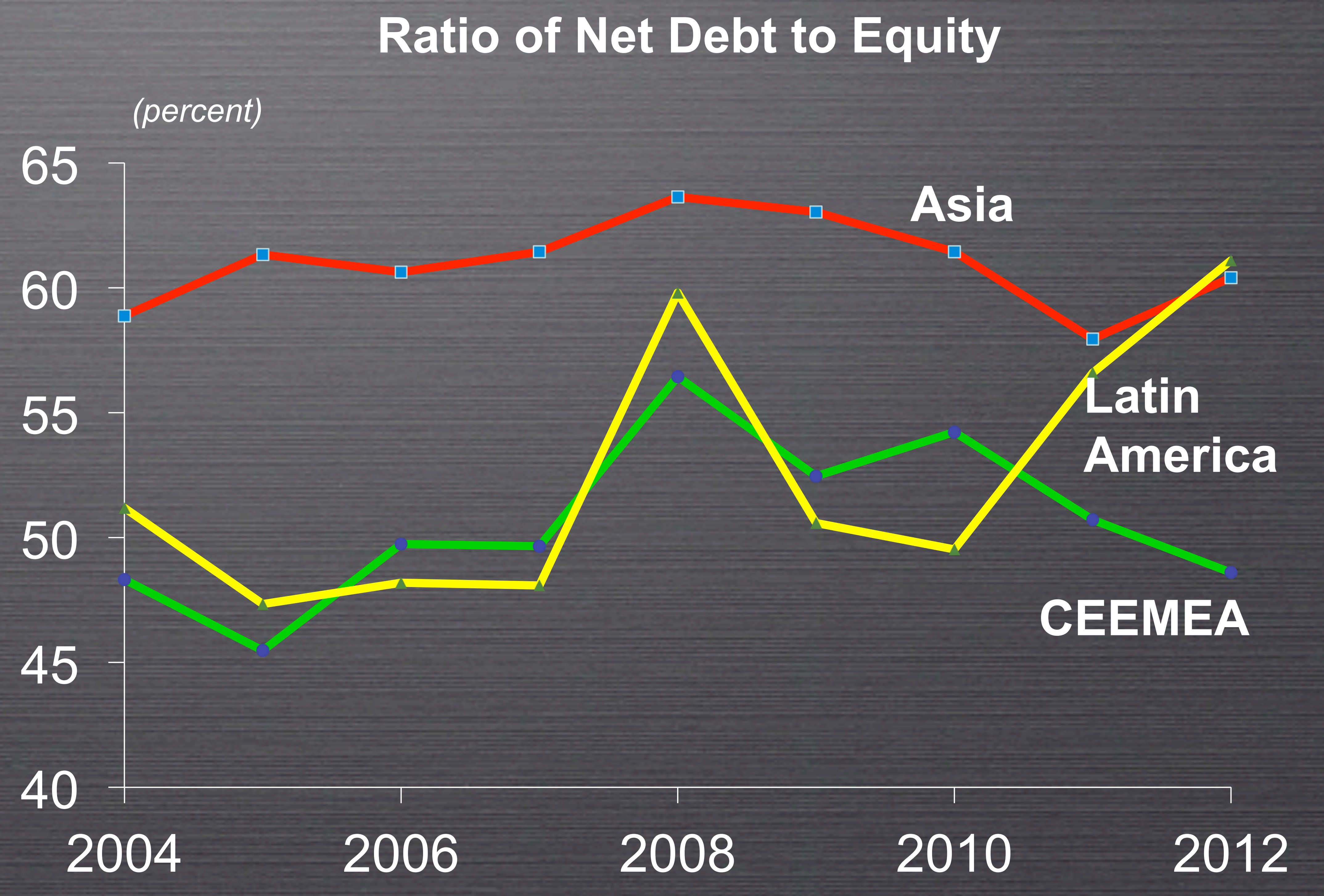
- Massive shift to fixed income (U.S., EM)
- Increased duration (U.S., EM)
- Structurally lower market liquidity (U.S., EM)
  - Foreign investors have crowded in local markets (EM)
  - Higher role of cross –over investors (EM)

Rising corporate leverage in emerging markets

New issuance of corporate debt
(billions of US dollar)

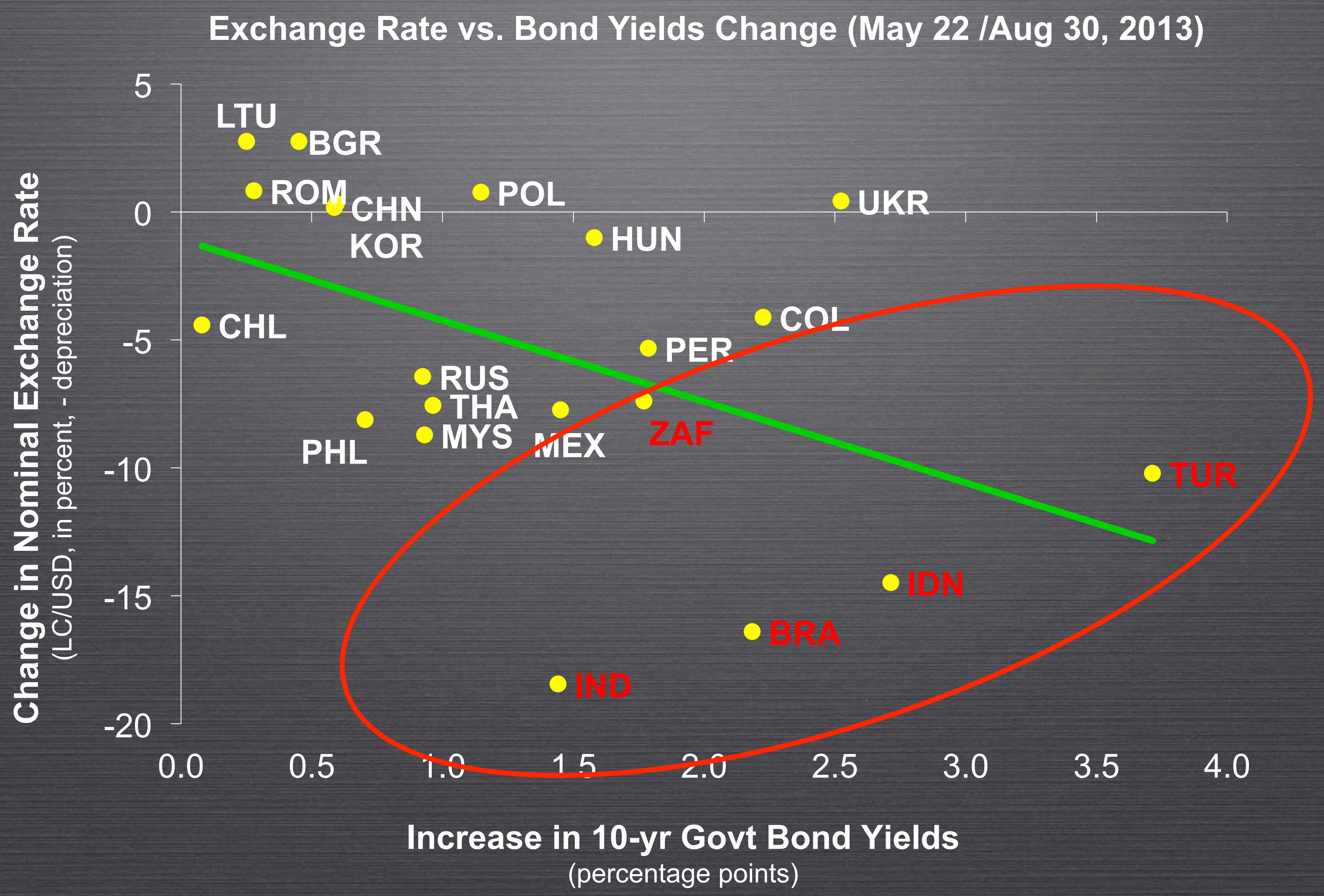


Nonfinancial Corporate Balance Sheet Metrics

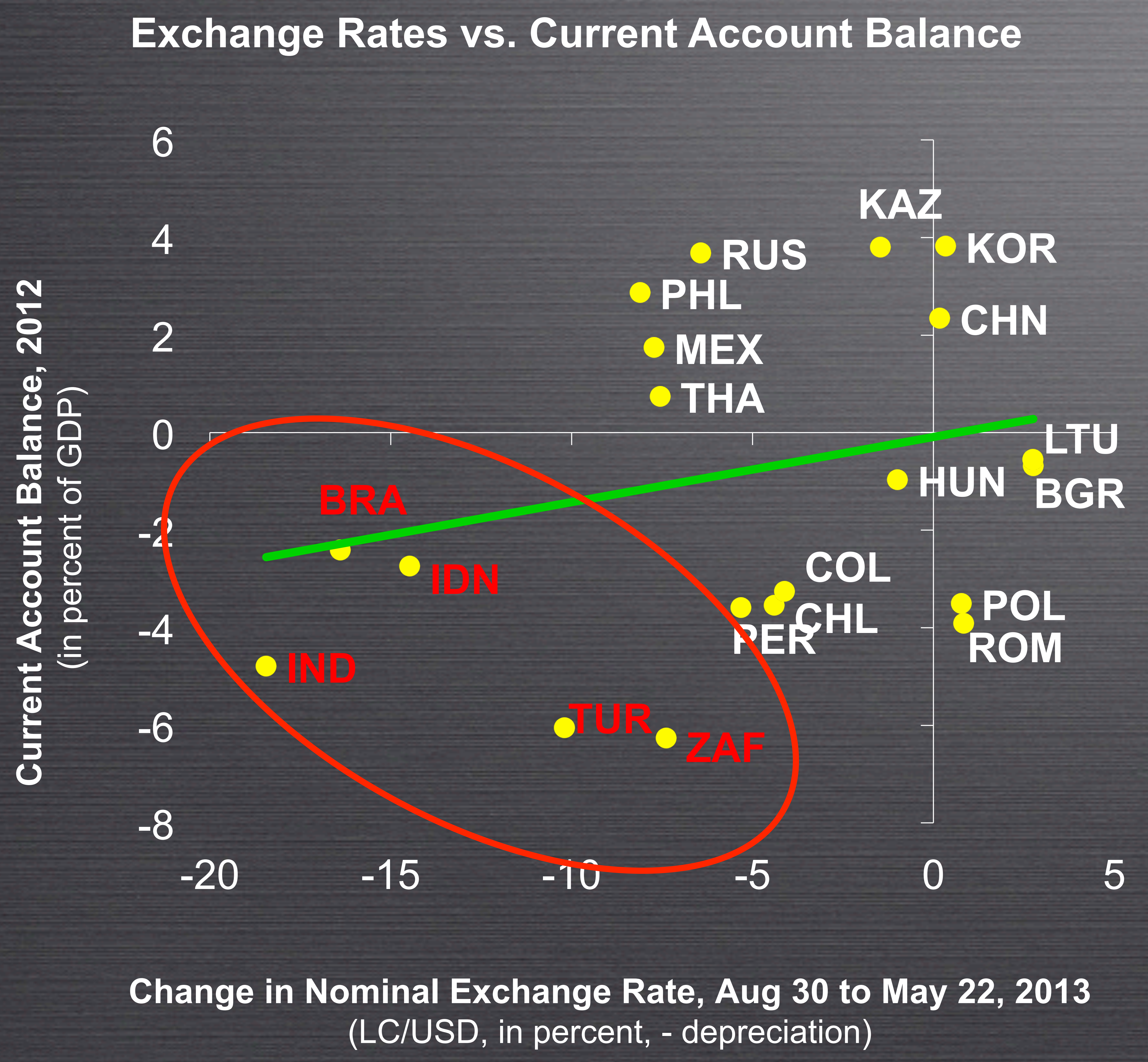


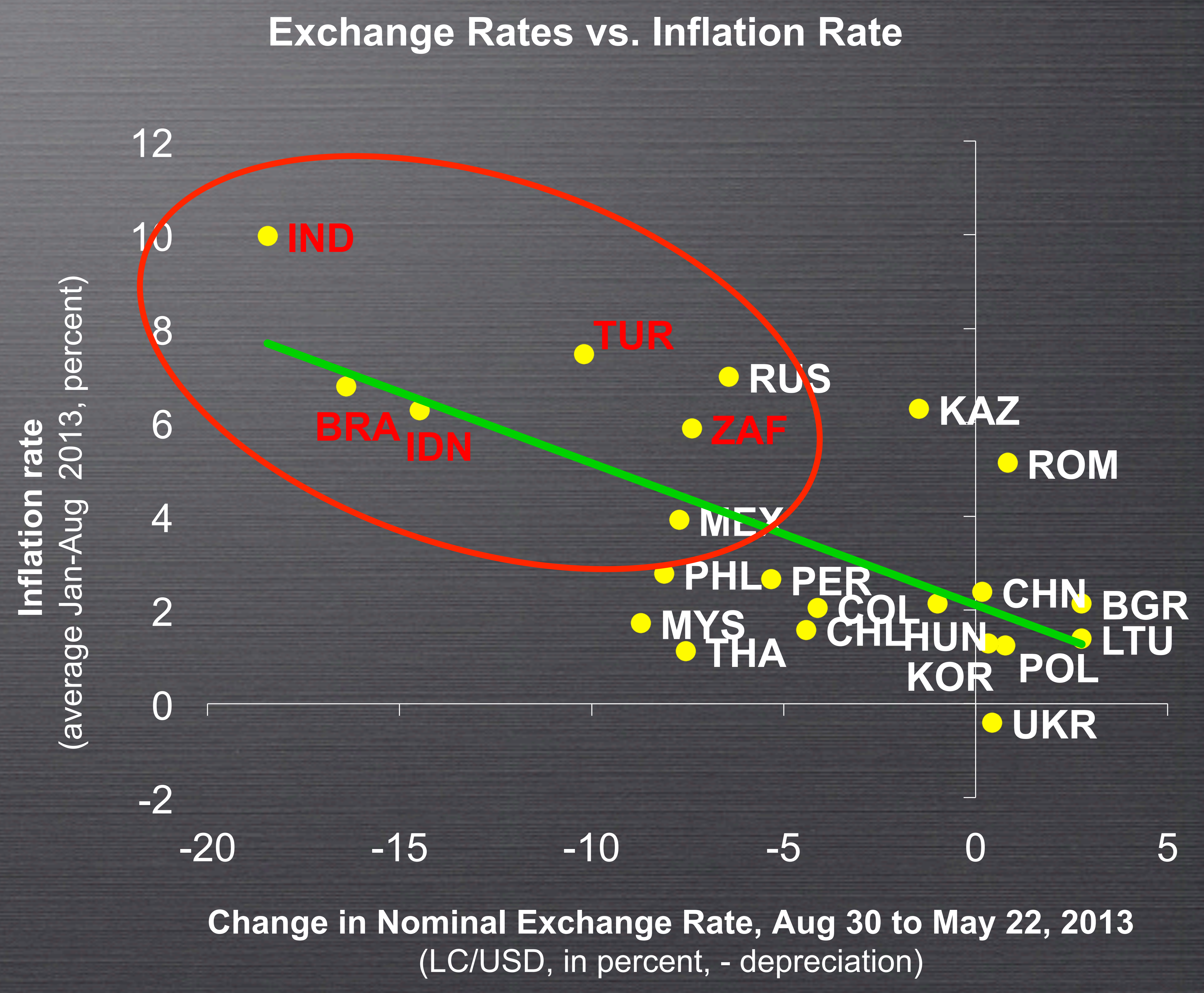
Sources: Bloomberg L.P.; and IMF staff calculations.
Note: Computed as the median of all available firm data. CEEMEA - central and eastern Europe, the Middle East, and Africa. Firms with negative net debt were excluded.

Recent "mini-stress" tests: currencies and bonds hit the most



Recent "mini-stress" tests: fundamentals matter





It takes two to tango

US

- Manage tapering and tightening (execute + communicate)
- Prudential policies key for stability

Emerging Markets

- Strengthen macro-financial policy frameworks and buffers
- Facilitate orderly market adjustment

Specifically for emerging markets

- In preparation ➔ strengthen fundamentals/keep them in check

- If serious tensions arise:

  - Allow exchange rates to adjust in line with fundamentals
  - Provide liquidity
  - Adjust macroeconomic policies
  - Prudential policies
  - Swap lines, IMF facilities