

Where Next For The World Economy? Risks And Scenarios For The Recovery

<https://marketpublishers.com/r/W5C4676C164EN.html>

Date: July 2011

Pages: 0

Price: US\$ 975.00 (Single User License)

ID: W5C4676C164EN

Abstracts

Overview

Business Monitor International (BMI) has just published a Special Report examining the risks to the global recovery. The report analyses the following topics:

The risk of a 'hard landing' in China, and fault-lines in its banking sector

The potential for the US economy to surprise us - on both the upside and downside

The possibility of a renewed spike in commodity prices

The risk of social and political upheaval in Iran

The risk of a destabilising power struggle for the presidency in Russia

The risk of a 'hard landing' for the Turkish economy

Executive Summary

The risks to the global economy are mounting, following the earthquake and tsunami in Japan in March and the spike in oil prices on the back of the political crises in the Middle East and North Africa. BMI's core global economic scenario is for steady growth for the remainder of the year and into 2012, with a modest pick-up in the US and key

emerging markets (EMs) on the one hand, and a 'hard soft landing' in China on the other. But several threats loom large over the next 6-12 months that could have a major impact on global businesses and financial markets:

Cracks are beginning to appear in China's growth model, posing grave threats to the global economy. BMI continues to believe that the slowdown in China's economic growth is set to intensify over the coming months and quarters on the back of energy supply problems, Japan-related supply chain issues, and monetary tightening-driven demand moderation. Meanwhile, the Chinese banking sector is on far more treacherous ground than most believe, and in a worst-case scenario, losses could come in at more than US\$100bn.

The US economy is at a critical junction, and could be on the verge of either boom or bust in the coming year. With the recovery still on unsteady legs, a major policy error at this stage could well be enough to tip the world's biggest economy into recession. On the other hand, growth could really begin to accelerate, given the extraordinarily easy monetary policy in place, and the likelihood that key areas of the economy including business investment have nowhere left to go but up. In this scenario, future inflation and interest rates could move higher than currently expected.

A renewed spike in commodity prices from current levels would present a significant headwind to the global economy. The two commodity groups with the greatest potential for a fresh leg higher are energy and grains. A commodity spike would place further upward pressure on inflation, particularly in emerging markets, raising political unrest, encouraging trade restrictions, and choking off the global recovery. The most obvious scenario for a renewed spike in oil prices above already elevated levels would be a significant loss of Saudi oil capacity, which could easily push prices into the US\$150-200/bbl range.

Global political risks abound, and Iran and Russia are seen as potential hotspots in the coming year. Iran is undergoing a period of political, economic, and social tensions, and it is not believed the current situation will be sustainable. Political turmoil there would have a substantial negative impact on the international oil market, driving oil prices up sharply. Meanwhile, in Russia, there remains major uncertainty over who will be president following elections in March 2012—Prime Minister Vladimir Putin or the incumbent, Dmitry Medvedev. BMI assesses the potential outcomes.

One risk that is being very much overlooked comes from Turkey, whose economy may be overheating. BMI is becoming increasingly concerned about the ongoing

deterioration in Turkey's external position and its negative implications for the Turkish lira and investor sentiment and also stresses the growing risks of a worst-case scenario emerging, whereby substantial capital flight leads to a hard landing for the domestic banking sector and wider economy.

Client Benefits

The Special Report draws upon the expertise of BMI's Global Economists and Industry analysts to provide a further strategic dimension to our Country Risk and Industry services. The global recovery is at a delicate phase, and the above threats could send ripples through financial markets.

In particular, the report demonstrates BMI's ability to identify the most pertinent economic risks in a timely and insightful manner.

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