World Economic Outlook

THE WORLD ECONOMY IS WAITING TO REBOUND

U.S.: Effects Of Budget Deficit Stalemate May Not Last Long

The U.S. Government shut down operations for lack of funds after President Bill Clinton vetoed two emergency funding bills. Despite the first U.S. government default, financial markets did not seem overly worried. There was no notable turmoil in the bond and foreign exchange markets.

One explanation for this attitude can probably be found in the inflation front. The prior budget crises took place during periods of high inflation, but presently, inflation is remarkably moderate and is expected to remain under control. Another explanation would be a positive perspective on the U.S. economy. A larger than expected jump in the growth rate of real GDP from 1.2% to 4.2% was recorded between the second and third quarters,.

Nobody can predict how long the crisis will last. However, it is expected that there will soon be some sort of reconciliation between the Republicans and the Administration, and that the effects of the current budget crisis will not last long.

It is recognized that the jump in the growth rate was more a temporary rebound from the sluggish second quarter than a strong economic re-acceleration. The latest statistics showed a continuing decline in the growth of nominal domestic spending over the past six to nine months. In fourth quarter of last year, spending rose 6.1%, but by the third quarter of this year, it had only increased 4.2%. As long as the Fed's target rate is not lowered, the growth of spending will continue to slow. However, the funds rate will not be cut in the near future, although the Fed will eventually lower its target rate sometime during the first half of next year. The U.S. economic growth rate is projected to be 2°≠2.5% for 1996.

Rest Of The World: Still Struggling, But Ready To Rebound

The Japanese Finance Ministry released its second interim report on resolving the Japanese banking crisis; however, it had no significant impact on the market. Most of the recommendations were vague and reflective of a gradual repairing of the problems. The current account surplus in September was US$10.6 billion, down from US$11.83 billion in the same month a year earlier. In the meantime, the "Japan premium" remained high at the 42 basis point, though significantly off its peak of 1 percentage point set last month.

None of these suggest any strong sign of economic rebound for next year. However, indications in investment were one of the few positive signs. Real business investment in plants and equipment jumped 10.3% in the second quarter, which marks the fourth consecutive quarter of increase. Furthermore, the NIKKEI stock index has been climbing gradually, thanks to significant buying by foreign investors. It is our perspective that there will be a stronger economic recovery in Japan next year. The weaker Yen, low interest rates, an easing of monetary policy, and some progress in handling bad-debt issues will be the key factors for a rebound. VIP

(Joon-Ho Lee)