The headquarters of the US Federal Reserve, the European Central Bank and the Bank of Japan. The impact of central bank actions is mainly felt in currency markets; the dollar has once again emerged stronger as the yen and euro weakened. — *AP, Bloomberg and AFP*

Central banks of advanced economies face dilemma

Recovery not stable, hence their actions follow similar trends

DOHA DATELINE

Dr R. Seetharaman

THIS MONTH IN JACKSON HOLE, US Federal Reserve Chairperson Janet Yellen stated that there is still "remaining slack in the labour market". It was understated by the unemployment rate at six per cent. She highlighted the challenges faced by the Fed in assessing how far the economy now stands from the attainment of its maximum employment goal. The Federal Reserve's monetary policy objective is to foster maximum employment and price stability.

In July 2014 the consumer inflation is up two per cent, which is line with the target set by Federal Reserve. The estimates of slack necessitate difficult judgments about the magnitudes of the cyclical and structural influences affecting labor market variables, including labour force participation, the extent of part-time employment for economic reasons and labour market flows, such as the pace of hires and quits. The Fed has kept interest rate hike options open and will monitor incoming information on labour markets and inflation to determine appropriate stance of monetary policy.

European Central Bank President, Mario Draghi said at Jackson Hole that the bank is ready to do more to boost the shaky recovery in euro region but has warned governments must join in efforts to reduce stubbornly-high unemployment. Inflation is a weak 0.4 per cent, well below the bank's goal of just under two per cent, and unemployment is quite high at 11.5 per cent. The euro-area economy stagnated in the first half of this year and Draghi restated the ECB's readiness to introduce further measures of monetary stimulation, but he also invited the governments to support their domestic demand through growth-oriented fiscal policies while remaining within the agreed budgetary limits. Structural reforms required to create more efficient public services and more flexible labour and product markets. The ECB's response has highlighted the fact that coordinated monetary and growth-oriented fiscal policies were needed to support a sustainable euro area economic recovery.

The recent minutes of Bank of England's Monetary Policy Committee, or MPC, has indicated dissent among policy makers as two policy makers wanted an interest rate increase. The two MPC members argued that a rise in bank rate was needed to keep inflation in check against a strengthening economy and tumbling unemployment. Both officials saw signs that quickening growth would soon start to drive faster growth in wages, fuelling inflation. The majority of officials had concluded the economy wasn't yet strong enough to justify higher borrowing costs. However, their dissent has fuelled speculation that a rate rise could come sooner, maybe before the end of 2014.

The Bank of Japan intends to keep pursuing its aggressive monetary easing policy for "some time" to completely eliminate deflation. The BoJ stood by its assessments of an improving domestic economy based on an expected pickup in global exports, corporate spending and local consumer confidence in Japan. As part of Abenomics, the BoJ deployed an intense burst of monetary stimulus in April 2013, when it pledged to double its money base with a quantitative easing programme of asset purchases. The programme was initially successful, with consumer inflation having recently hit 1.3 per cent, excluding the impact of an April sales tax hike. Inflation is expected to slow in the coming months as the boost from a weak yen on import costs begins to fade. Japan's inflation is slightly above one per cent recently and is aiming for a two per cent target set as part of Abenomics. If the inflation rate drops below one per cent that would raise the chances of additional easing by the BoJ.

> The impact of central bank actions is mainly felt in currency markets

The economic recovery in advanced economies is not stable and hence the monetary action also follows similar trends. The BoE and US Fed face a dilemma in relation to timing of raising interest rates taking into consideration the economic recovery. Japan and the ECB face similar situation in relation to continuation of easing measures as growth and deflation pose major challenges to their respective economies. The impact of central bank actions mainly felt in currency markets. The dollar has once again emerged stronger as the yen and euro weakened on expectation of continued easing by the BoJ and the ECB. The pound has also weakened against the dollar as expectations of interest rate hikes by the Fed in 2015 still prevail.

The writer is the group chief executive officer of Doha Bank. Views expressed are his own and do not reflect the newspaper's policy.