Investors are particularly nervous about India: Gita Gopinath, Harvard University

Gita Gopinath, 41, a professor of economics at Harvard University, says she is glad that Ben Bernanke is at the helm of affairs (as Fed Reserve chairman) as the US looks to end an unprecedented and huge monetary easing policy. An alumna of Princeton University and Delhi School of Economics, Gopinath says that Bernanke (whose term ends early next year) and his successor will have to face many "unknowns" while unwinding a measure as unique as quantitative easing (QE). Excerpts from an interview with ET:

Do you have faith in Fed Reserve chairman Ben Bernanke to navigate the US economy through the uncertain period that will follow the end of monetary easing?

To orderly unwind the extraordinary monetary easing that has taken place in recent years is a challenge for any central banker, including Bernanke. There are many unknowns as some of the interventions like QE have no historical precedence. What I will say is that I am glad that Bernanke is at the helm of affairs to see this through since he is a remarkable monetary economist. Most of the impact of the unwinding will, however, take place next year when Bernanke’s term comes to an end, in which case outcomes will depend on the next person on the job.

The likely "step-by-step halt-and-exit" (from QE) is untried and untested in US history. What do you think will be the likely consequences in the US?

There will certainly be an increase in volatility in the bond and stock markets in the short term given all the unknowns. This higher volatility, however, does not have to translate into bad numbers for growth and employment as long as financial institutions continue financing companies and households. As long-term housing mortgage rates rise, it will be interesting to see how housing price growth is impacted. If the recent increase in housing prices was mainly an outcome of QE3, then we could anticipate a slowdown in consumer spending.

How do you view the turmoil in global markets following Bernanke’s hints at easing stimulus? Are there other reasons as well for the fall in global indices?

The easing of stimulus is a big piece of the higher uncertainty in markets in recent days but there are other ongoing problems. For instance, the crisis in the eurozone is far from over and the recent credit crunch in China is adding to the uncertainty. Unwinding monetary stimulus in the US was always going to be complicated and it does not help that large and globally important regions of the world are sources of risk at the same time.

What will be the fallout on the Indian economy, and the rupee?

The recent drop in the value of the rupee is a part of a global phenomenon where investors are moving out of risky emerging market assets. As yields on US assets increase, especially in an environment of uncertainty, there will be a readjustment away from emerging market assets. This was expected and I am not surprised that the rupee has lost value. Some small-scale interventions by the Reserve Bank of India to prevent excessive rupee movements can be called for but I would stop at announcing a target value for the rupee that will be defended at all cost.

The bigger picture though is the lack of good news coming out of the Indian economy. Slowing growth and large current account deficits make investors particularly nervous about India. So while all emerging markets will face currency stress in the short term the markets that are perceived as having weaker fundamentals will take a bigger hit. There is a sense that with elections around the corner in India there is no stomach for tough
reforms that stimulate the economy. This pessimism is costly for the rupee.

Do you see elevated inflation in the US following QE "tapering"?

Since monetary policy works through the economy slowly if there is a pick-up in inflation it will be more because of the earlier QE policies and low interest rates rather than the tapering. The tapering will rein in inflationary pressures. The bigger question is whether there will be sufficient growth in the US and lowering in unemployment that will translate into inflation rising from its near zero level.

When do you expect US unemployment rates to drop to, say, 6.5% (from 7.6% in May)?

This is hard to tell. The recent declines in unemployment rates are partly a result of people choosing to stay out of the labour market, thereby reducing the size of the labour force. That will turn around as people become more optimistic about their job prospects and re-enter the labour pool. Unemployment rates could then rise briefly over the next few months before trending down.

Tapering QE as the labour market strengthens is what Bernanke is planning to do. Is it easier said than done?

Again the argument here is that monetary policy works slowly through the system. So in the best-case scenario, the labour market improves as the positive effects of the prior monetary easing continue to impact the economy and the economy strengthens enough that the withdrawal of QE has a minor impact in the short-term. How exactly this plays out is to be seen.
Readers' opinions (12)

Sort by: Newest | Oldest

suresh (usa)
23 Jun, 2013 09:26 PM

beauty and brains. rare combination. i hope our ruling class listen to her

Kiran Kanchibhotla (Hyderabad, Andhra Pradesh)
23 Jun, 2013 03:40 PM

Investors should not be worried about the Indians, they are worried about the Indian Govt.

bhawana jha
23 Jun, 2013 01:22 PM

GDRs, in combination with QIP and Domestic Institutional Investors (DII), is what Yes Bank aims in order to raise capital of USD 500 million after the approval of AGM held on 8th June in Mumbai. Diversification of capital resources would help investors and shareholders of all class to grow. Besides, this will lead to sustainable development in the economy. For the sustainable economic and growth, support and follow Sh. Narendra Modi on Twitter with #NaMo4PM #NaMoForce.

myalmightygod (India)
23 Jun, 2013 01:19 PM

Thanks, its easy to comment

G20 summit in Russia: Economic worry shifts to emerging markets

» Read more