



Oil pain adds to volatile global mix

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Herald Sun

Stephen McMahon
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THE next few months will be crunch time for the global economy as it faces the threats of higher inflation and faltering growth, a leading economist has warned.

Professor Marvin Goodfriend, a 20-year veteran of the US Federal Reserve under former chairman Alan Greenspan's stewardship, said the volatility in oil prices and global stock markets will continue until the uncertainty surrounding the US economy begins to clear.

"We are going to have a very nervous summer (in the northern hemisphere) as we aren't going to get a clear picture until later in the year about whether the US economy can avoid recession," he said.

"The US economy has been whipsawed this year by two opposing forces."

Despite the gloom, Professor Goodfriend is optimistic the US economy can maintain its low-growth trajectory throughout this year - largely thanks to the \$US170 billion (\$A181.46 billion) of rebate cheques given to taxpayers by the government - and avoid an out-and-out recession.

As prices continue to go higher, he is forecasting that Fed chairman Ben Bernanke will be forced to raise rates once this year.

But Professor Goodfriend said the Fed would not engage in a campaign of rate rises required to return interest rates back to the 4-5 per cent level until next year.

"If we get to the Fall (September or October) and it is growing clear we have got past the risk of a recession than Mr Bernanke may raise rates," he said. "But if oil and food prices continue to go up then the Fed may be forced into a series of increases, but that is a long shot."

Professor Goodfriend believes the huge influx of speculators into the oil markets, which has been blamed for prices hitting a peak of \$US139 a barrel last week, are hoping to profit on the US economy avoiding recession and beginning to grow again in late 2008.

"This may possibly fuel a further lift in oil prices allowing them to pocket large profits," he said.

Investors are nervous about oil prices and this has triggered a spate of heavy selling on Wall Street and in financial markets across the world.

The six-year rally of crude oil has accelerated this year, jumping 40 per cent since the start of the year.

Professor Goodfriend, a visitor at the US Studies Centre at the University of Sydney, said if the Fed did not move quickly enough against rising inflation, the dreaded stagflation - slow or no growth combined with rising inflation - could hit for the first time since the 1970s.

Today, he is meeting with senior Reserve Bank of Australia executives to discuss the global scourge of inflation. "Australia is the flip-side to all the problems in the global economy but inflation is its Achilles heel," he said. "Boy, are you benefiting from the upside to commodity prices. Australia is sitting pretty and it needs to recognise that it just needs a stable monetary policy to maintain its positive position."

He stressed the most important thing was that the RBA was given breathing space to make the right decisions about inflation, needed to set Australia up for another generation of growth.

"Educating both politicians and the public about the importance of monetary policy - interest rates - is vital if central banks are going to be allowed to do their job," he said.

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