

MONETARY POLICY ADAPTABILITY IN THE CONTEXT OF GLOBAL IMBALANCES

Hayk Sargsyan

Armenian State University of Economics, Ph.D. in Economics

sargsyan007@gmail.com

ORCID ID: <https://orcid.org/0000-0002-1720-4603>

Abstract: Monetary policy is a fundamental tool for promoting economic stability and growth. In recent years, it has faced a series of global challenges, including trade tensions, geopolitical conflicts such as the Russia-Ukraine war, technological innovation, and the rise of cryptocurrencies. These factors have increased uncertainty and complicated policy decisions for central banks. Additionally, the COVID-19 pandemic and its aftermath have required unprecedented monetary interventions.

The paper explores how monetary authorities - particularly the European Central Bank, the U.S. Federal Reserve, and central banks in emerging markets - have adapted their strategies in response. It examines the effectiveness of recent policy shifts and emphasizes the need for coordinated, adaptive approaches that account for inflation control, financial stability, and long-term economic resilience.

Keywords: monetary policy, European Central Bank (ECB), price stability, World Bank financing, global economic imbalances, interest rates

JEL codes: E51, E52, E61, E63

Research aims: This research aims to analyze the evolution of global and Eurozone monetary policy frameworks, their effectiveness in maintaining price stability, and the role of international financial institutions in supporting economic resilience.

Research novelty: This research offers a novel comparative analysis of post-2020 monetary policy adaptations in the Eurozone and globally, highlighting the interplay between central bank actions and international institutional support mechanisms.

Introduction

Monetary policy plays a critical role in maintaining macroeconomic stability by influencing key economic variables such as inflation, employment, interest rates, and overall growth. In recent years, central banks worldwide have confronted unique challenges, largely driven by the combined effects of the COVID-19 pandemic, geopolitical tensions (including the Russia-Ukraine war), global supply chain disruptions, financial technological advancements, and rising inflationary pressures. In response, monetary authorities, particularly in advanced economies like the Eurozone, have made significant policy shifts, moving away from historically low interest rates and quantitative easing towards monetary tightening beginning in late 2022. This paper examines these transitions, focusing on the European Central Bank (ECB), which operates within a diverse yet unified economic framework, managing policy across various sovereign nations with differing fiscal conditions. This complexity presents both opportunities and challenges for policy effectiveness. In addition, global institutions

such as the World Bank have played a complementary role, particularly in supporting low- and middle-income countries, which face the dual challenges of contractionary policies and limited fiscal space. The study seeks to offer a comprehensive view of the evolution of monetary policy from 2020 to 2025, highlighting the interdependence between global financial assistance and domestic policy responses. It contributes to understanding how central banks and international institutions can jointly foster stability amid uncertainty.

Literature review

Milton Friedman, a key figure in the Monetarist school, modernized the classical Quantity Theory of Money. In *The Quantity Theory of Money: A Restatement* (1956), he argued that there is a direct relationship between the money supply and price levels, asserting that people maintain a stable demand for money. When the money supply exceeds this demand, excess liquidity leads to increased spending and higher prices, causing inflation. Friedman emphasized that changes in the money supply affect nominal, not real, economic variables in the long run. His ideas shaped U.S. monetary policy in the 1970s, influencing Federal Reserve actions under Chairman Paul Volcker to control inflation through strict monetary targets, which led to a recession before policy shifted in 1982. [Friedman, M. 1956].

In *The General Theory of Employment, Interest, and Money* (1936), John Maynard Keynes rejected the direct link between money supply and price levels proposed by the Quantity Theory. He argued that price levels are more influenced by production costs

than money supply fluctuations. Keynes suggested that increasing the money supply lowers interest rates, stimulating investment and aggregate demand, which boosts GDP and employment. This, in turn, raises production costs and price levels. He advocated for monetary policy to manage interest rates to stimulate investment and reduce unemployment, particularly during periods of underemployment, and viewed moderate inflation as beneficial for activating idle resources and creating jobs. (Keynes, J. 1935).

Michael Woodford's work in modern monetary theory, particularly in *Interest and Prices* (2003), advanced the understanding of how expectations shape the transmission of monetary policy. Woodford argued that central banks must not only adjust short-term interest rates but also manage expectations about future policy. He introduced the concept of dynamic stochastic general equilibrium (DSGE) models, showing that forward guidance and central bank credibility are crucial for effective monetary policy. Woodford's framework departs from the simple IS-LM model and underscores the importance of inflation targeting and transparent communication. His work has become foundational in modern monetary policy and is widely used by central banks, including the Federal Reserve and the European Central Bank (Woodford, M. 2003).

Lars Svensson's inflation forecast targeting model further builds on these ideas by making inflation expectations central to monetary policy formulation. Unlike traditional models that rely on past data, Svensson's approach is forward-looking and emphasizes central banks' ability to guide expectations regarding future inflation. This framework enhances transparency and accountability

while allowing for more flexible policy responses to economic fluctuations. Svensson's model has influenced monetary policy in countries such as Sweden, New Zealand, and the UK, offering an alternative to the strict targeting of money aggregates (Svensson, L. 1997).

In *Inflation Targeting: Lessons from the International Experience* (1999), Ben Bernanke and his co-authors analyze inflation targeting as an effective monetary policy tool, drawing on case studies from various economies. They highlight how inflation targeting anchors expectations, reduces volatility, and stabilizes output. Bernanke also discusses the importance of central bank independence and clear communication in enhancing the effectiveness of inflation targeting, particularly in emerging markets (Bernanke, B. et al. 1999).

Together, these frameworks provide a comprehensive view of contemporary monetary policy, highlighting the evolving role of central banks in managing inflation and economic growth.

The methodology

The methodology incorporates a comparative analysis of key economic theories, including Monetarist and Keynesian perspectives, based on foundational works by Friedman, Keynes, Woodford, Svensson, and Bernanke. The study combines theoretical frameworks with empirical case studies from various countries to assess the impact and effectiveness of different monetary policy approaches.

Research results

The global economy in 2024 is experiencing a mix of stability and varying growth across regions. Global GDP growth for the third quarter was 0.1 percentage point below expectations, largely due to weaker economic performance in Asia and Europe. China's growth slowed to 4.7 percent, below forecasts, with a decline in domestic consumption, partly due to a sluggish property market. India also saw slower growth, driven by a deceleration in industrial activity. In Europe, especially Germany, recovery remains weak, though consumption has improved with rising real incomes. Japan's economy contracted slightly due to supply disruptions. Conversely, the U.S. economy showed robust growth, expanding by 2.7 percent year-over-year, driven by strong consumer spending. Despite global disinflation, inflation reduction has stalled in some regions, with core inflation staying above 2 percent globally. Services price inflation continues to rise, particularly in the U.S. and the euro area, complicating efforts to balance inflation control with economic growth (IMF, 2025).

Global growth is expected to remain stable but lackluster, with forecasts at 3.3 percent for both 2025 and 2026, below the historical average of 3.7 percent from 2000 - 2019. These projections have remained largely unchanged since October, indicating modest growth over the next few years. In the United States, underlying demand is 0.5 percentage point higher than previously forecast, reflecting carryover from 2024, strong labor markets, and accelerating investment. While U.S. growth is robust for the time being, it is expected to taper off towards potential in 2026 as the economy stabilizes.

The CFR Global Imbalances Tracker can be used to gauge, through time, the vulnerability of individual countries and the global economy to the buildup of imbalances in the current account (of which trade deficits or surpluses are the largest component). Below, the Global Imbalances Index shows the total size of global current account deficits and surpluses as a percentage of world output (Steil B., 2025).

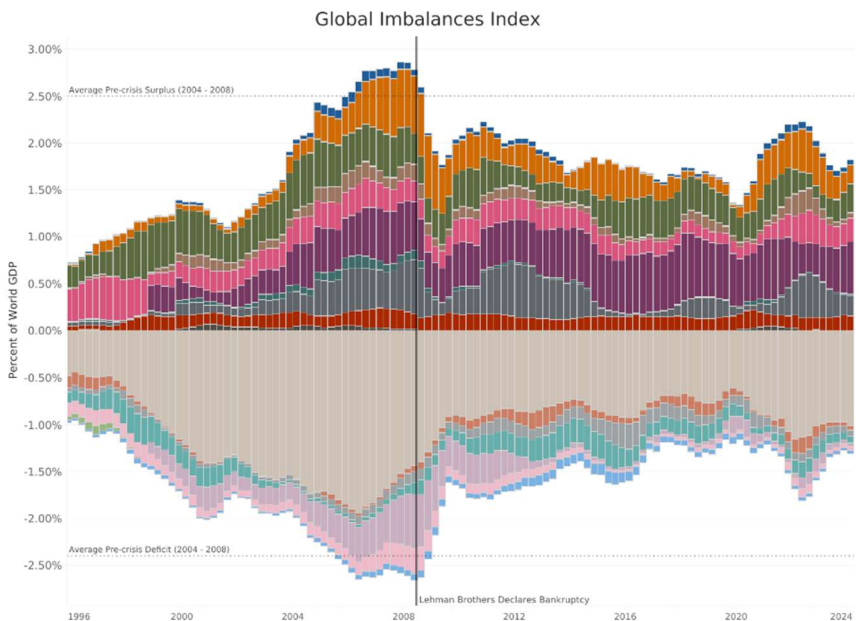


Figure 1. Global Imbalances Index, 1996-2024

Source: Steil B. January 2025. Global Imbalances Tracker.

<https://www.cfr.org/tracker/global-imbances-tracker#2>

The colored segments of each column represent the contributions to total deficits and surpluses from different regions, defined in the legend above.

In the euro area, growth is expected to rise at a slower pace, with a downward revision to 1.0% for 2025 due to geopolitical tensions and manufacturing weakness. However, growth is projected to reach 1.4% in 2026, driven by stronger domestic demand and improved confidence. The ECB's survey also revised inflation forecasts, predicting 2.2% for 2025 and 2.0% for 2026, reflecting persistent economic challenges and inflationary pressures (Reuters, 2025).

For other advanced economies, growth forecasts remain stable, influenced by two opposing factors. On one hand, recovering real incomes are expected to drive consumption, supporting cyclical recovery. On the other hand, heightened trade policy uncertainty is expected to suppress investment, limiting growth potential.

In emerging markets and developing economies, growth projections for 2025 and 2026 are expected to broadly align with 2024 performance. For China, growth is slightly revised upward by 0.1 percentage point to 4.6 percent for 2025, reflecting carryover effects and a fiscal stimulus package announced in November. The outlook for China's growth in 2026 remains stable at 4.5 percent as trade policy uncertainty subsides and the effects of an aging population slow the decline in labor supply. India's growth is projected at a solid 6.5 percent in both 2025 and 2026, aligning with the October forecast.

In the Middle East and Central Asia, growth is expected to improve, but Saudi Arabia's 2025 growth forecast has been revised

down to 3%, primarily due to extended OPEC+ production cuts. The IMF's World Economic Outlook lowered Saudi Arabia's 2025 GDP growth from an earlier estimate of 3.3%, also reducing its 2026 projection by 0.4 percentage points to 3.7%. For the broader region, growth was revised down to 3% from 3.6% (Saini M., 2025). Latin America and the Caribbean are projected to see slight growth acceleration to 2.5% in 2025, despite slowdowns in major economies. In sub-Saharan Africa, growth is expected to rise, while emerging and developing Europe faces slower growth due to regional challenges.

Recent forecasts indicate a slight downward revision in world trade volume estimates for 2025 and 2026, largely driven by heightened trade policy uncertainty, which is expected to disproportionately affect investment decisions among trade-intensive firms. However, this impact is considered transitory, with some short-term offset provided by the front-loading of trade flows in anticipation of tighter trade restrictions. On the inflation front, global disinflation is expected to continue in line with prior forecasts. Labor market cooling and declining energy prices are expected to support a gradual return of inflation toward central bank targets. In the United States, inflation is likely to remain slightly above the 2 percent target in 2025, while inflationary pressures in the euro area and China are expected to be more subdued. Amid these macroeconomic challenges, the World Bank Group has played a crucial countercyclical role, providing approximately \$100 billion annually between 2019 and 2023 to low- and middle-income countries, helping offset the contractionary effects of tight monetary policies and supporting fiscal stability.

The World Bank Group consists of five institutions dedicated to reducing poverty and promoting sustainable development globally. Between fiscal years 2019 and 2023, these institutions collectively disbursed nearly 100 billion dollars in various forms of financing to low- and middle-income countries. Since FY2019, funding has increased across all institutions, with the Multilateral Investment Guarantee Agency (MIGA) seeing a rise in gross issuance. The International Development Association (IDA) reached its peak funding in FY2022 before decreasing slightly in FY2023, though overall funding has grown since FY2019. Additionally, disbursements from the International Finance Corporation (IFC) nearly doubled during this period, while funding through recipient-executed disbursing accounts surged from 2.5 billion to over 19 billion U.S. dollars by FY2023 (Einar H. Dyvik. 2024).

McKinsey & Company has analyzed the impact of monetary policy on global banking profitability. In 2022, banks worldwide experienced a \$280 billion profit boost due to rising interest rates, marking the sector's best performance since the 2008 financial crisis. However, McKinsey cautioned that this profit rebound may be short-lived, as declining interest rates and reduced loan demand could compress net interest margins by approximately 16% by 2030. To maintain returns, banks would need to implement cost-cutting measures at five times the current pace (McKinsey & Co. 2023).

Conclusion

The global economic landscape has undergone significant upheaval in recent years, driven by challenges such as the COVID-

19 pandemic, geopolitical tensions, technological advancements, and rising trade uncertainties. These factors have deeply impacted the effectiveness of monetary policy, especially for central banks like the European Central Bank (ECB) and the U.S. Federal Reserve. In this environment, central banks have faced the complex task of balancing inflation control with the need to support economic growth and stability.

This paper highlights the evolving nature of monetary policy in the post-pandemic era, focusing on the adaptation of policy frameworks to address global economic imbalances. A notable shift has been the transition from historically low interest rates and quantitative easing to monetary tightening in response to inflationary pressures. While the immediate effects of these changes have been varied, the necessity for coordinated and flexible strategies has become clear.

International financial institutions, particularly the World Bank, have played a crucial role in supporting low- and middle-income economies, helping them navigate the adverse effects of contractionary policies and ensuring fiscal stability. These institutions offer essential countercyclical support where domestic policy tools are limited.

Looking ahead, monetary policy will require a more integrated approach, addressing both domestic and global challenges. Given the persistent risks of trade uncertainty and geopolitical tensions, central banks must remain adaptable, balancing inflation control, financial stability, and long-term economic resilience. The global imbalances will require enhanced coordination among

policymakers, economists, and international institutions to foster sustained growth and stability.

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**ԴՐԱՄԱՎԱՐԿԱՅԻՆ ՔԱՂԱՔԱԿԱՆՈՒԹՅԱՆ
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Հայկ Սարգսյան

Հայաստանի պետական տնտեսագիտական համալսարան,
տ.գ.թ.

Բանալի բառեր - դրամավարկային քաղաքականություն, Եվրոպական Կենտրոնական Բանկ (ԵԿԲ), գնաճի կայունություն, Համաշխարհային Բանկի ֆինանսավորում, գլոբալ տնտեսական անհավասարակշռություններ

Ժամանակակից գլոբալ տնտեսական միջավայրը ընդգրկում է անորոշությամբ, որը պայմանավորված է համավարակով, աշխարհաքաղաքական հակամարտություններով, մասնավորապես՝ ռուս-ուկրաինական պատերազմով, սանկցիոն սահմանաչափերի սահմանմամբ և մատակարար-

ման շղթաների խախտումներով, ֆինանսական տեխնոլոգիաների զարգացմամբ և գնաճային ճնշումների աճով:

Այս պայմաններում դրամավարկային քաղաքականությունը դարձել է առանցքային գործիք՝ մակրոտնտեսական կայունության պահպանման, գնաճի վերահսկման և տնտեսական աճի խթանման համար: Հողվածում ուսումնասիրվում են Եվրոպական կենտրոնական բանկի, ԱՄՆ Դաշնային պահուստային համակարգի և զարգացող երկրների կենտրոնական բանկերի կողմից ձեռնարկված ռազմավարական քայլերը՝ տոկոսադրույքների կարգավորման, սպասումների կառավարման և շուկայի վստահության ամրապնդման ուղղությամբ:

Ուշադրություն է դարձվում նաև ԱՀԲ-ի և այլ միջազգային կառույցների դերը՝ որպես աջակցող գործիք՝ ցածր և միջին եկամուտ ունեցող երկրների դիմադրողականության ամրապնդման հարցում: Ուսումնասիրության արդյունքները փաստում են, որ արդյունավետ դրամավարկային քաղաքականությունը պահանջում է միջազգային համագործակցություն և կառուցվածքային ճկունություն՝ համաշխարհային անհավասարակշռություններին դիմակայելու համար:

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