

13 March 2018

GETTING STRONGER, BUT TENSIONS ARE RISING

Summary

- The world economy will continue to strengthen in 2018 and 2019, with global GDP growth projected to rise to about 4%, from 3.7% in 2017.
- Stronger investment, the rebound in global trade and higher employment are helping to make the recovery increasingly broad-based.
- New tax reductions and spending increases in the United States and additional fiscal stimulus in Germany are key factors behind the upward revision to global growth prospects in 2018 and 2019.
- Inflation remains low, but is likely to rise modestly.
- Still-elevated risk-taking and high debt levels in many countries raise financial vulnerabilities. Monetary policy normalisation could also result in greater volatility of exchange rates and capital flows, particularly in emerging market economies.
- Medium-term growth prospects remain much weaker than prior to the financial crisis, reflecting less favourable demographic trends and a decade of sub-par investment and productivity.
- Economic policies face several challenges:
 - A gradual normalisation of monetary policy is needed, but to a varying degree across the major economies. Continued clear communication about the path to normalisation is essential to minimise the risk of financial market disruptions.
 - Fiscal policy choices should avoid being excessively pro-cyclical and be clearly focused on measures that strengthen the prospects for sustainable and more inclusive medium-term growth.
 - Structural reform efforts should be revived, seizing the opportunity of the stronger economy to help secure a more robust recovery of productivity, investment and living standards.
- Safeguarding the rules-based international trading system will help to support growth and jobs. Governments should avoid escalation and rely on global solutions to resolve excess capacity in the global steel industry.

OECD Interim Economic Outlook Forecasts March 2018

Real GDP growth

Year-on-year % increase

	2017	2018		2019	
		Interim EO projections	Difference from November EO	Interim EO projections	Difference from November EO
World¹	3.7	3.9	0.2	3.9	0.3
G20^{1,2}	3.8	4.1	0.2	4.0	0.2
Australia	2.3	3.0	0.2	3.0	0.3
Canada	3.0	2.2	0.1	2.0	0.1
Euro area	2.5	2.3	0.2	2.1	0.2
Germany	2.5	2.4	0.1	2.2	0.3
France	2.0	2.2	0.4	1.9	0.2
Italy	1.5	1.5	0.0	1.3	0.0
Japan	1.7	1.5	0.3	1.1	0.1
Korea	3.1	3.0	0.0	3.0	0.0
Mexico	2.3	2.5	0.3	2.8	0.5
Turkey	6.9	5.3	0.4	5.1	0.4
United Kingdom	1.7	1.3	0.1	1.1	0.0
United States	2.3	2.9	0.4	2.8	0.7
Argentina	2.9	3.2	0.0	3.2	0.0
Brazil	1.0	2.2	0.3	2.4	0.1
China	6.9	6.7	0.1	6.4	0.0
India³	6.6	7.2	0.2	7.5	0.1
Indonesia	5.1	5.3	0.1	5.4	0.0
Russia	1.5	1.8	-0.1	1.5	0.0
Saudi Arabia	-0.8	1.6	0.0	1.7	0.0
South Africa	1.2	1.9	0.9	2.1	0.6

Note: Difference from November 2017 Economic Outlook in percentage points, based on rounded figures.

1. Aggregate using moving nominal GDP weights at purchasing power parities.

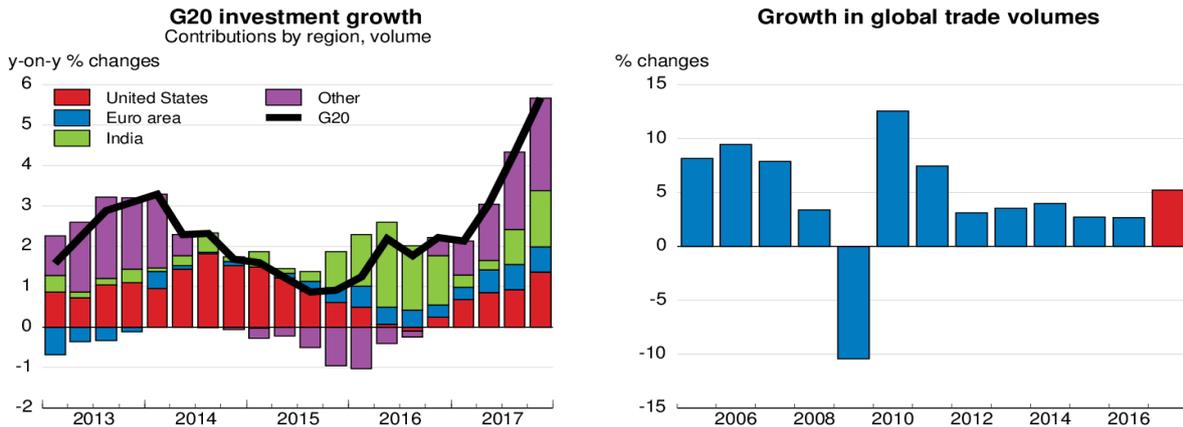
2. G20 aggregate does not include European Union countries who are not members in their own right.

3. Fiscal years, starting in April.

The economic outlook is improving

Global GDP growth is estimated to have been 3.7% in 2017, the strongest outcome since 2011, with positive growth surprises in the euro area, China, Turkey and Brazil. Industrial production, investment and trade growth have rebounded, with global trade growth reaching an estimated 5¼ per cent in 2017, and business and consumer confidence remain elevated. Improved cyclical conditions are now being reflected in commodity markets and in labour markets.

Investment and trade growth have rebounded

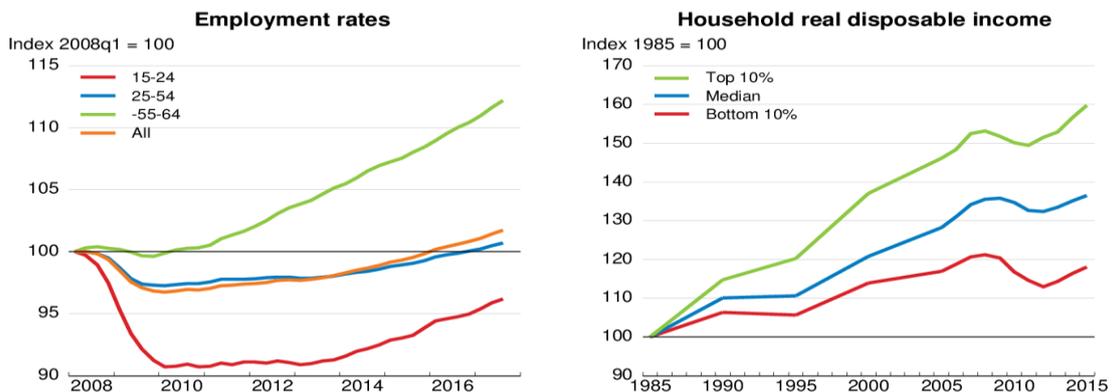


Note: G20 investment aggregate excludes China and Saudi Arabia due to data unavailability. The euro area aggregate includes only Germany, France and Italy. World trade is measured as goods and services trade volumes in constant US dollars.

Source: OECD Economic Outlook Database; and OECD calculations.

Stronger GDP growth is being accompanied by solid job creation, with the OECD-wide unemployment rate having finally fallen below the pre-crisis level. Even so, the recovery in employment remains uneven; the employment rates of older workers (aged 55 and above) have risen sharply in recent years, but prime-age and youth employment rates are only at, or still below, pre-crisis levels in many countries, including the United States.

Income and employment gains remain uneven in the OECD



Note: The OECD employment rate of each age group is the ratio of the number of employed people to the working age population in the age group. The income series are averages of the 17 OECD member countries for which data are available over the full period.

Source: OECD Short-Term Labour Market Statistics; OECD Income Distribution Database; and OECD calculations.

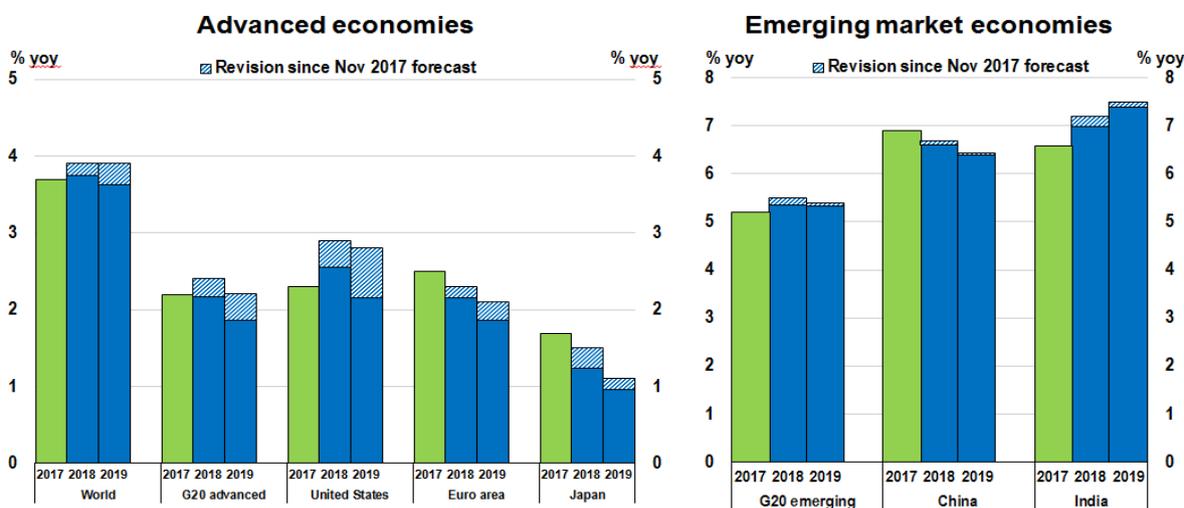
Labour markets have become more polarised, with a decline in the share of middle-skill jobs relative to jobs with higher or lower skill levels. Despite steady declines in unemployment, wage growth generally

remains weak, contributing to popular dissatisfaction with economic performance. Many households have seen little growth in real disposable incomes over the past decade, particularly those with low incomes.

Growth is set to strengthen further in the next two years

The world economy will continue to strengthen over the next two years, with global GDP growth projected to reach almost 4% in both 2018 and 2019. Growth in the United States, Germany, France, Mexico, Turkey and South Africa is projected to be significantly more robust than previously anticipated, with smaller upward revisions in most other G20 economies. The tax reductions and public spending increases announced over the past three months in the United States, together with a substantially easier fiscal stance in Germany, are key factors behind the upward revision to global growth prospects in 2018 and 2019. Ongoing improvements in business investment in the major economies should be reflected stronger global trade growth. Prospects for investment are also somewhat stronger than previously expected in commodity-producing economies, reflecting the higher level of global commodity prices.

GDP growth prospects have been revised up in advanced and emerging economies



Note: GDP in constant prices. Fiscal year data for India. The G20 aggregate does not include the European Union countries who are not members in their own right. G20 emerging economies include Argentina, Brazil, China, India, Indonesia, Mexico, Russia, Saudi Arabia, Turkey and South Africa.

Source: OECD Economic Outlook database.

Key features of the projections in the G20 economies are:

- In the United States, GDP growth is projected to pick up to between 2¾-3 per cent over 2018-19. Tax reductions and higher government expenditure reinforce the momentum in domestic demand from strong confidence, solid job creation, past gains in household wealth and the rebound in oil production. Taken together, the new US fiscal measures could add between ½-¾ percentage point to US GDP growth both this year and next, with modest positive demand spillovers for other economies (see Box). Gradual monetary policy normalisation is set to continue, bringing higher long-term interest rates, as the labour market tightens further and wage growth and inflationary pressures pick up.
- Growth in the euro area is set to remain robust and broad-based at between 2-2¼ per cent over 2018-19. Accommodative monetary and fiscal policies, improving labour markets and high levels of business and consumer confidence are all helping to boost demand. Investment is also becoming increasingly supportive, on the back of strong global demand and favourable financing

conditions. Growth is set to remain solid in Germany, helped by additional fiscal easing projected in both 2018 and 2019, and France, helped by the impact of recent reforms, but is set to continue at a more moderate pace in Italy.

- Growth surprised on the upside in China in 2017, helped by a strong rebound in exports, but is set to soften to just below 6½ per cent by 2019. Macroeconomic and regulatory policies are gradually becoming more restrictive, the working age population is now declining and credit conditions are less expansionary. Regulatory efforts are continuing to reduce financial risks, deal with overcapacity in some sectors and improve environmental quality. Fiscal policy is now broadly neutral, but additional measures could be implemented if output growth were to slow more sharply.
- GDP growth in Japan is set to remain at around 1½ per cent in 2018 before easing to around 1% in 2019, supported by improved export growth, especially in Asian markets, and the additional spending announced in the recent supplementary budget. Strong corporate profitability should continue to underpin the recovery in business investment, but private consumption is likely to remain subdued if wage and income growth is modest. The global trade rebound, particularly for semi-conductors, is also helping to support demand in Korea. GDP growth is projected to remain around 3% over 2018-19, with the higher minimum wage and stronger social welfare spending supporting household incomes and spending.
- GDP growth in the United Kingdom is projected to ease to a little over 1¼ per cent this year and 1% in 2019. High inflation continues to damp real household income growth and consumer spending, and business investment is slowing, amidst continued uncertainty about the future relationship between the United Kingdom and the European Union.¹
- GDP growth in Canada is projected to soften to around 2¼ per cent in 2018 and 2% in 2019. Macroeconomic policies are gradually becoming less accommodative, but private consumption remains robust, strong employment growth is beginning to be reflected in wages, and firmer commodity prices should boost business investment. Strong commodity demand is also benefitting Australia, with GDP growth projected to pick up to around 3% over 2018-19. Non-mining and infrastructure investment have strengthened, and improved terms of trade and solid job creation provide support for household incomes, despite still modest wage growth.
- In Mexico, fiscal and monetary policies are relatively tight, but strong global demand growth, resilient private consumption and reconstruction spending are all projected to support output growth in 2018-19.
- Robust domestic demand growth is projected to help underpin growth in India, Indonesia and Turkey over 2018-19. Growth in Turkey is projected to moderate from the exceptionally rapid pace seen in 2017 as government stimulus measures fade, but could remain at around 5% over 2018-19 given strong labour force growth and improved external demand. GDP growth is expected to strengthen in India to around 7¼ per cent and 7½ per cent in FY 2018 and FY 2019 respectively, with strong private investment growth driving the rebound from the transitory effects of demonetisation and the introduction of the Goods and Services Tax. GDP growth is also expected to increase gradually in Indonesia over 2018-19, helped by strong infrastructure investment and the improving regulatory environment.

1. The projection continues to be based on the technical assumption that the United Kingdom has a transition agreement with the European Union after formal exit in 2019, minimising possible short-term disruption to trade.

- The resumption of growth in a number of other major emerging commodity-producing economies, including Argentina, Brazil, Russia and South Africa, is now supporting the global upturn. Moderate growth resumed in Brazil and Russia in 2017, and is projected to continue in 2018-19, with activity supported by monetary policy easing, improved sentiment and firmer commodity prices. Improving confidence, and strong reform momentum should help to underpin growth in South Africa and Argentina respectively, despite planned fiscal restraint.

An initial assessment of the impact of US fiscal policy changes

The US Tax Cuts and Jobs Act, and the decision of Congress to raise spending limits over the next two years, imply a significant easing of US fiscal policy of around 1% of GDP in both 2018 and 2019. (In comparison, the November 2017 *Economic Outlook* projections had assumed an easing of 0.5% of GDP in 2018 and unchanged policy in 2019.) This Box provides an initial assessment of the effects on growth prospects of the new fiscal measures.¹

- The main tax measures include a permanent reduction in the marginal corporate income tax rate to 21%, a decrease in personal income tax rates that expires in 2025, and an increase in the rate of bonus depreciation to 100% in 2018-2022 after which it is phased out by 2026. The measures also push the United States towards a more territorial tax system, consistent with most major economies. Overall, the direct costs of the Tax Cuts and Jobs Act raise the federal government deficit by around 0.7% of GDP in 2018 and an additional 0.7% of GDP in 2019 according to estimates from the Congressional Budget Office. Thereafter, the impact on the annual budget deficit is set to fade to around zero by 2026-27, on the basis of current legislation, implying some fiscal tightening in the first half of the 2020s.
- The new two-year budget bill voted in early February provides a higher spending ceiling in both 2018 and 2019 than previously expected.

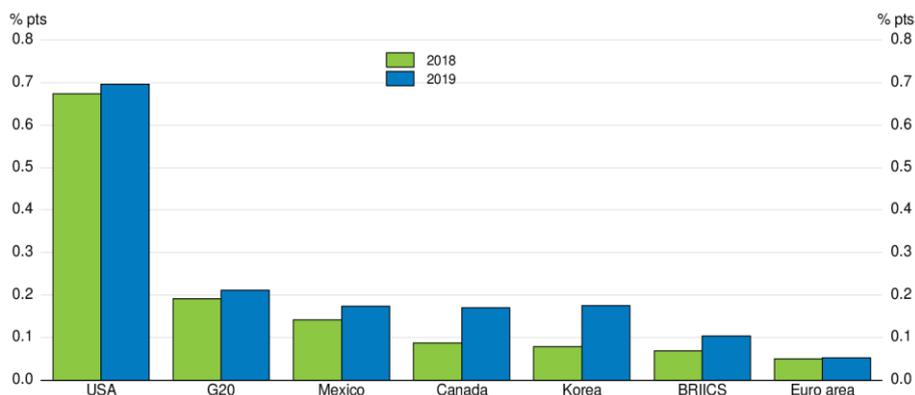
In the model-based scenario these fiscal measures were incorporated as follows:

- A reduction in the effective corporate tax rate of 8 percentage points in 2018 and 7 percentage points in 2019, before slowly easing thereafter. This reduces corporate tax receipts by around 0.5% of GDP in 2018 and 0.8% of GDP in 2019, approximating the impact of the collective changes to the corporate tax system being undertaken. Other tax changes are assumed to occur via reductions in the effective rate of personal income taxes, reducing revenue by around 0.6% of GDP by 2019, before slowly fading thereafter.
- The increase in spending limits was assumed to result in an increase in government consumption of 0.3% of (baseline) GDP in 2018 and 0.6% of GDP in 2019.

The short-term impact of the combined fiscal measures is estimated to raise US GDP growth by between ½-¾ percentage point in both 2018 and 2019. Business investment rises relatively rapidly, helped by a sustained decline in the cost of capital of around 10% and expectations of higher future output. The boost to US final demand also strengthens import growth and adds to labour market pressures, with the unemployment rate declining by ½ percentage point over 2018-19 and real wages above baseline by around 1% by 2019.

The US fiscal stimulus is set to strengthen short-term GDP growth

Difference from baseline, percentage points



Source: OECD calculations.

As stronger short-term activity feeds back into the budget balance, the overall increase in the deficit is closer to 1½ per cent of GDP in 2019. Monetary policy is tightened in the near term, with policy interest rates over ½ percentage point above baseline in 2019, resulting in an appreciation of the US dollar effective exchange rate.

Other countries benefit from stronger external demand in the United States (on an assumption of unchanged trade policies), especially close trading partners such as Canada and Mexico. However, this is offset in part by somewhat tighter domestic monetary policy than otherwise in many countries due to higher import price inflation.

In the medium term, the full impact of the US tax act is difficult to estimate and model, given the changes in underlying incentives and behaviour that may result, including about investment location decisions, and the extent to which tax reductions for high-income households are saved rather than used for additional expenditure. The permanent reduction in the marginal corporate tax rate implies that the real user cost of capital will be lower than otherwise, bringing about a long-lasting increase in the business capital stock. Higher long-term interest rates could however limit the medium-term effects, with the government debt-to-GDP ratio estimated to rise by around 5-6 percentage points by the mid-2020s.

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1. The assessment uses the NiGEM global macroeconomic model, maintained by the UK National Institute of Economic and Social Research. The model was run with forward-looking expectations, so that businesses and households have full knowledge of future fiscal changes. Monetary policy was allowed to be endogenous in all economies, with the exception of the euro area and Japan, where policy interest rates were kept unchanged before 2020. The budget solvency rule was used from 2020 to bring the US deficit-to-GDP ratio back to baseline by the mid-2020s, implying gradual increases in the effective tax rate on household incomes.

Rising trade protectionism would hurt growth and jobs

Trade protectionism remains a key risk that would negatively affect confidence, investment and jobs. Governments of steel-producing economies should avoid escalation and rely on global solutions to resolve excess capacity in the global steel industry, in particular through the Global Forum on Steel Excess Capacity. Safeguarding the rules-based international trading system is essential to prevent the longer-term harm to growth prospects that could arise from a retreat from open markets.

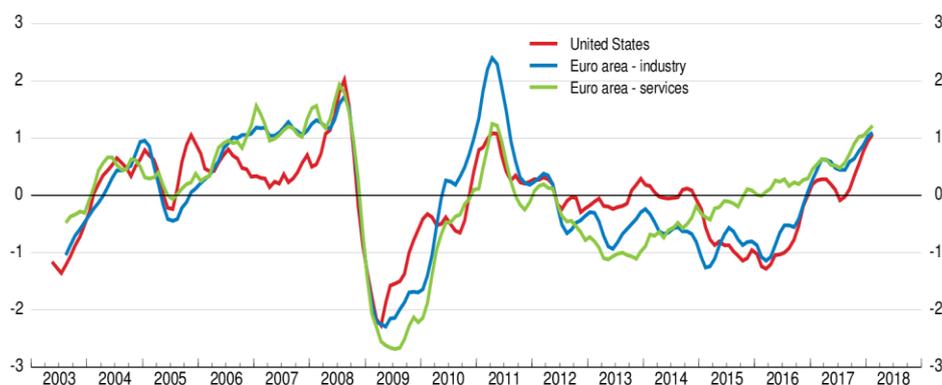
Inflation is set to rise modestly

Price and wage inflation are likely to strengthen gradually in the major economies as labour markets tighten. A modest increase in inflation from subdued levels would be welcome, helping to reduce the need to continue exceptionally supportive monetary policy for an extended period. Recent rises in commodity prices have begun to push up headline inflation in many advanced economies, but underlying inflation remains mild, in part due to the slow pace of the recovery from the crisis. Inflation also generally remains modest in emerging market economies. However, past currency declines and a relatively strong sensitivity to commodity price fluctuations are currently adding to inflation pressures in some countries, including Turkey, Mexico and Argentina.

Forward-looking indicators, such as corporate surveys, now point to emerging constraints, with firms increasingly reporting labour shortages as a constraint on production and raising expectations of future prices. There are also some signs that wage growth has begun to pick up in the United States, Germany and Canada, where broad measures of unemployment are now at, or below, longer-term norms. In Japan, where labour shortages are particularly acute but wage growth is still soft, new corporate tax credits for companies that raise wages by 3% or more may foster stronger compensation growth. Elsewhere, including the aggregate euro area, wage growth remains muted despite strong job growth.

Inflation is set to rise modestly

Corporate selling price expectations have risen Normalised, three-month moving average



Note: The percent balance of the number of firms reporting expectations of higher prices compared with the number of firms reporting expectations of lower prices. Normalised values over the period 2003-2018, expressed in standard deviations.

Source: US Federal Reserve; European Commission; and OECD calculations.

Nonetheless, the rise in inflation appears likely to remain modest. Soft productivity growth, past low inflation, and compositional effects, such as the shift towards part-time work and the rising employment of lower-skilled workers, continue to check wage growth. Declines in unemployment also overstate the pace at which many national labour markets are tightening, given high involuntary part-time work in some and the scope for reforms to encourage more people to participate in the labour force. Inflation developments also appear to have become less sensitive to fluctuations in economic slack over time.

Higher interest rates could expose tensions and financial vulnerabilities

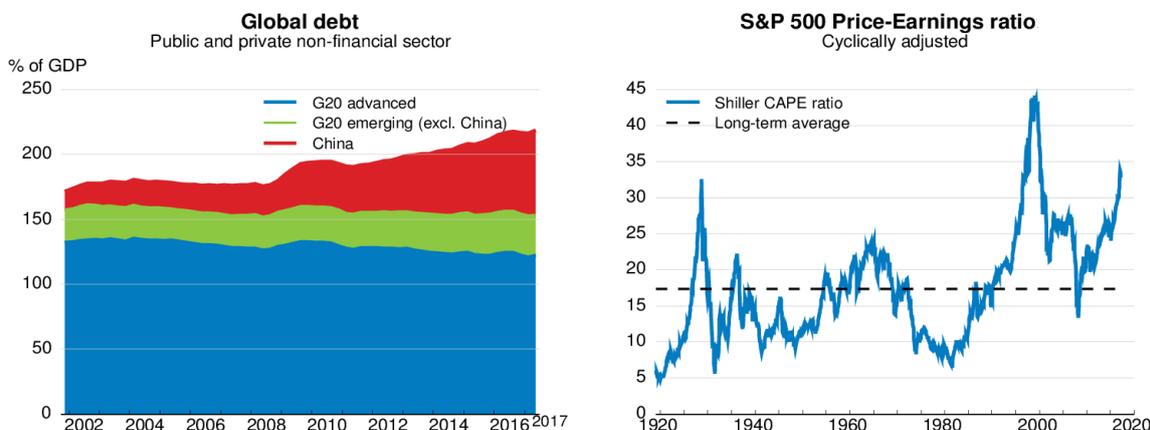
Financial conditions have begun to normalise in many major countries since the start of the year, largely reflecting the stronger recovery and associated expectations of higher inflation and less accommodative monetary policy. Equity prices in the major economies have declined from their recent elevated peaks and stock market volatility has picked up from the unusually low levels seen last year, which should help to reduce excessive risk-taking. Credit markets have, however, largely been calm and corporate and emerging-market bond spreads generally remain low. In the United States, 10-year sovereign bond yields are at the highest level in four years, but remain low by longer-term standards. Further increases, and the extent to which these are accompanied by additional volatility, will depend on the speed of policy normalisation and inflation expectations.

To the extent that current developments reflect a necessary adjustment in bond yields due to expectations of less accommodative monetary policy, the direct impact on growth may be modest. However, significant vulnerabilities remain, with implications for growth prospects. The prolonged period of low interest rates and volatility has encouraged greater risk-taking, making the financial system more exposed to shifts in market sentiment as monetary policy normalises. New tensions are particularly likely if policy rates were to be changed abruptly in event of an upside inflation surprise. Further corrections in asset prices remain possible as monetary policy normalises, given the still-high valuations in some markets, including equity markets in the United States, housing markets in Canada and Australia, and corporate bonds.

Financial stability concerns also arise from still-low credit risk spreads and high private and public debt levels in many countries. Stronger nominal GDP growth and more moderate credit provision in China have helped to slow the rise in global debt-to-GDP ratios, but debt levels in many countries and sectors remain above pre-crisis levels. High indebtedness could amplify the impact of any further correction in

asset prices and bond yields, with a risk of rising defaults, higher debt-service burdens and a retrenchment in private sector spending.

Debt levels remain high, and stock market valuations are elevated



Note: Debt of general government and the non-financial private sector expressed as per cent of GDP weighted by nominal GDP at PPP exchange rates. G20 Advanced comprises Australia, Canada, France, Germany, Italy, Japan, Korea, the United Kingdom and the United States. G20 Emerging comprises Argentina, Brazil, India, Indonesia, Mexico, Russia, Saudi Arabia, South Africa and Turkey. The Cyclically Adjusted Price-to-Earnings ratio (CAPE) is obtained by dividing the S&P 500 index by a 10-year moving average of earnings, adjusted for inflation. The long-term average is calculated over the 1920-2018 period.

Source: BIS; OECD; Robert J. Shiller; and OECD calculations.

Policy needs to be focused on achieving a durable and inclusive improvement in living standards

Against the backdrop of the stronger global economy, the priorities for policy are to foster productivity, make growth more inclusive, and enhance resilience against possible risks, especially financial vulnerabilities. The need for monetary policy support can be eased gradually as economies approach full employment. Fiscal and structural measures should be focused on the medium term, and be used to strengthen investment and productivity growth and ensure that the benefits from growth are distributed more widely. Active and timely deployment of prudential and supervisory policies would help to reduce the risks from financial vulnerabilities in both advanced and emerging market economies, including high debt levels in some countries and sectors.

Monetary policies are set to diverge

A gradual normalisation of monetary policy is needed in the major economies, but to a varying degree, reflecting the different outlook for growth, inflation and financial market developments. Improved growth prospects could result in a faster and larger withdrawal of monetary policy support than previously anticipated. At the same time, a moderate upturn of inflation, or even a mild overshooting of medium-term objectives, would not merit an abrupt increase in policy rates. Continued clear communication about the path towards monetary policy normalisation is essential to minimise financial market disruptions.

In the United States, the Federal Reserve should continue to increase policy rates gradually and progress with balance sheet reduction. The additional fiscal stimulus being implemented in 2018-19 is likely to raise the path for policy interest rates over the next two years, which could push the upper bound of the target federal funds rate to 3¼ per cent by the end of 2019. Some tightening of monetary policy is also likely in Canada and the United Kingdom, given limited economic slack and inflation at or above medium-term objectives. In the euro area, an upturn in actual and expected inflation would allow the ECB to reduce asset purchases gradually this year and subsequently phase out the negative interest rate policy. In Japan, where underlying inflation and inflation expectations remain low, current stimulus measures

need to be continued to help achieve the inflation target. Amongst the major emerging market economies, there may be scope for future policy easing in Brazil, Mexico, South Africa and Russia, provided inflationary pressures subside, but less so in India or Indonesia. In China, policy should contribute to the need to reduce the high level of corporate debt.

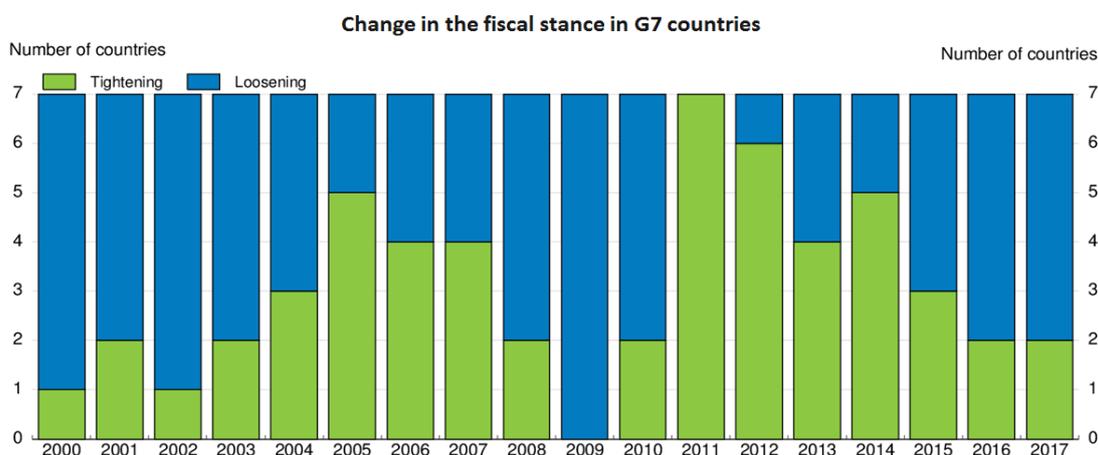
Risks of spillovers via exchange and interest rates arise from the likely further divergence in policy rates across the major economies over the next two years. Given the importance of US financial developments for global financial markets, there is a risk of repricing in other asset markets and more volatile capital flows if US monetary policy is tightened more abruptly than expected. An appreciation of the US dollar would also raise servicing costs on dollar-denominated foreign debt in many emerging market economies. Domestic currency weakness could also necessitate an earlier monetary policy tightening in some than would otherwise be warranted.

Fiscal policies need to be focused on medium term challenges

The supportive fiscal measures put in place by many countries over the past two years have helped to achieve stronger rates of growth after years of sub-par global growth. Given the broad-based recovery, it is important that policy should now avoid being excessively pro-cyclical and be focused on addressing structural challenges. Thus the focus of fiscal policy should shift towards the medium term and measures that strengthen the prospects for solid and more inclusive growth. Improved growth potential can in turn do much to underpin fiscal sustainability by helping reduce public debt-to-GDP ratios.

The fiscal stance is being eased in many advanced economies, by around ¼ per cent of GDP in the typical economy and in the euro area in 2018, and by substantially more in the United States. Additional easing is assumed to occur in 2019 in a handful of countries, including the United States and Germany. In some countries, such as Japan and the United Kingdom, fiscal policy has also been eased implicitly by the decision to push longstanding budgetary objectives further into the medium term. To avoid excessive pro-cyclicality, choices about spending and tax policies need to be well-targeted, enhance incentives to invest and participate in the labour market, and ensure that increases in incomes and living standards are shared more widely. Amongst emerging market economies, fiscal policy is becoming broadly neutral in China, but is being tightened modestly in many other countries. Some countries, such as Brazil, also need to implement additional fiscal and pension reforms to help ensure longer-term fiscal sustainability.

Fiscal policy has eased in the major economies



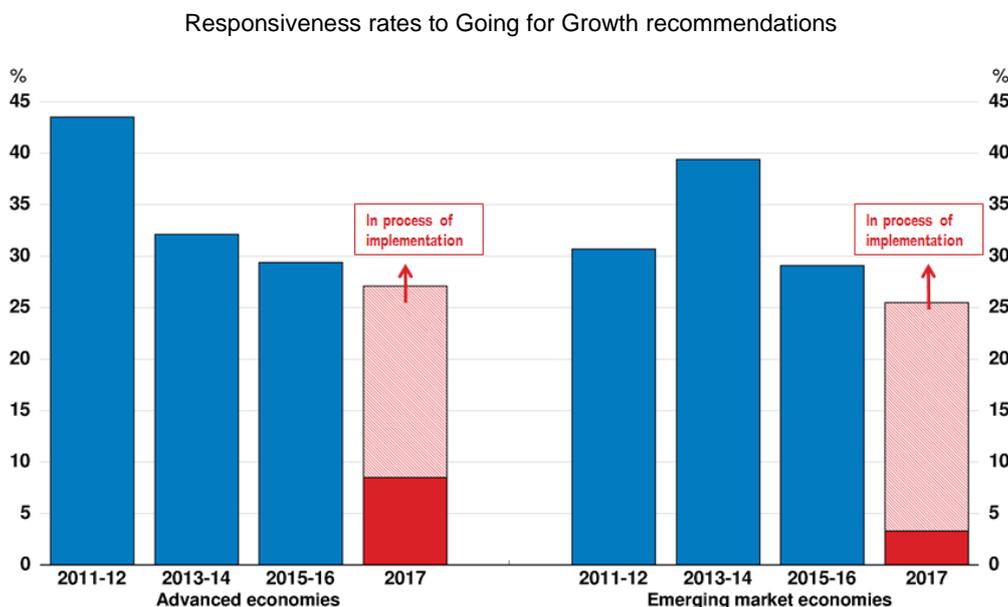
Note: Loosening and tightening respectively indicate a negative and a positive change in the underlying government primary balance to potential GDP ratio.

Source: OECD Economic Outlook database; OECD calculations.

Structural policy ambition needs to be stepped up to achieve stronger medium-term inclusive growth

Intensified structural policy efforts are needed in both advanced and emerging market economies to improve the medium-term prospects for investment, trade and productivity, and to ensure that the recovery yields benefits for all. However, as highlighted in the forthcoming OECD *Going for Growth 2018*, structural reform efforts have slowed in both advanced and emerging market economies, including in 2017, despite major actions in some G20 countries including Italy, France, Japan, India and Argentina. A continuation on this path, with weak productivity and wage outcomes, raises the risk of larger shortfalls from past performance in the growth of living standards, further diminishing trust in the capabilities of policymakers. Any retreat from open markets and common multilateral frameworks and standards would also harm prosperity.

Figure 1. The slow pace of structural reform is a risk to medium-term inclusive growth

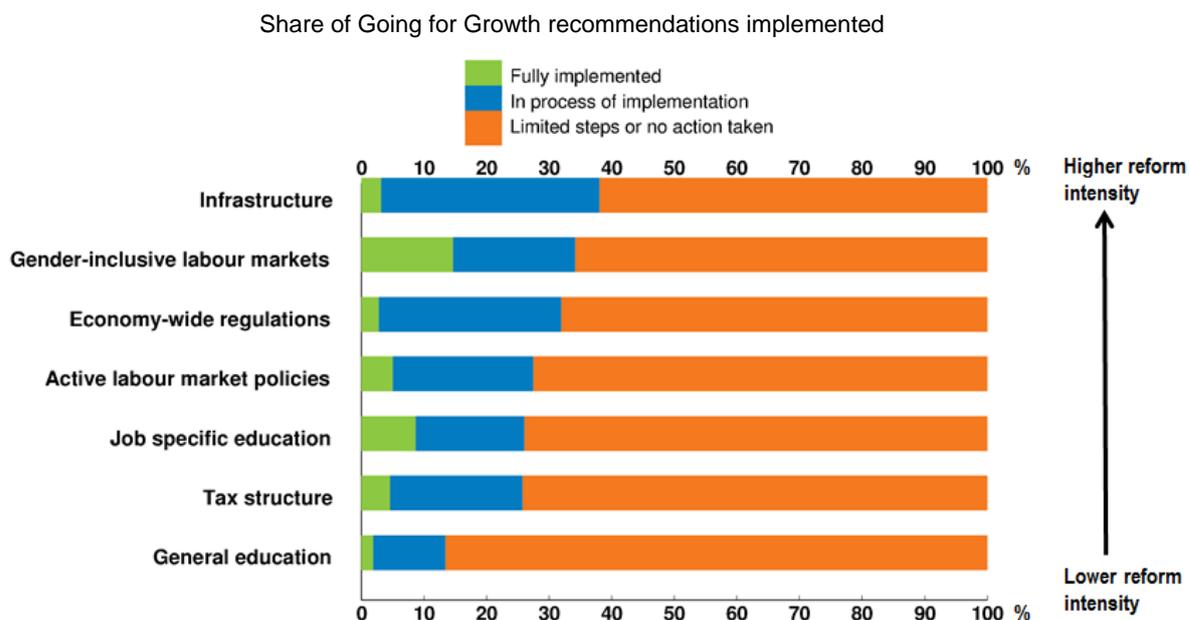


Note: Fully coloured bars refer to the share of fully implemented reforms. The estimated take-up of reforms is captured by the Going for Growth indicator of reform responsiveness. For 2017, reforms in the process of implementation are shown to ensure comparability with previous two-year periods. Emerging market economies include Argentina, Brazil, Chile, China, Colombia, Costa Rica, Indonesia, India, Mexico, Russia, South Africa and Turkey. Advanced economies include all non-emerging OECD member countries and Lithuania.

Source: OECD *Going for Growth 2018* (forthcoming).

A much improved economic outlook provides an opportune moment to implement more ambitious reforms. Any short-term costs from reforms may be lower and shorter-lived when demand and job creation are stronger, especially if accompanied by complementary labour market reforms and income support that help displaced workers transition to new jobs and acquire new skills. Other actions needed to enhance inclusiveness, such as improving the participation of under-represented groups in the labour market, are also more likely to have durable benefits if implemented at a time of job-rich growth. Recent progress has, however, been modest in enacting reforms to reduce gender gaps, strengthen job creation and help workers find new jobs.

Figure 2. Progress with tax and skills reforms is particularly slow



Note: Selection of reform areas with the largest number of recommendations. Infrastructure includes physical and legal infrastructure. Job specific education includes higher education, vocational education and training. General education includes primary and secondary education.

Source: OECD *Going for Growth* 2018 (forthcoming).

In advanced economies, modest medium-term growth prospects also point to a widespread need for renewed efforts to implement competition-friendly regulations, including via trade policy. These would strengthen competitive pressures in product markets, enhance incentives to invest and help revive the diffusion of innovations between frontier firms and the rest of the economy. Moving towards more reallocation-friendly insolvency regimes would also free resources trapped in high-debt “zombie” firms, improving the ability of more productive firms to attract additional capital. Progress in enacting other reforms to enhance growth, such as improving the efficiency of the tax structure and skill acquisition, has been particularly slow.

Renewing economic dynamism in emerging market economies is also essential to strengthen the prospect for further convergence in living standards across economies. Better performance could be achieved by lowering barriers to foreign trade, investment and firm entry, and reducing the scope and improving the governance of state-owned enterprises. Tackling structural bottlenecks, expanding public investment in infrastructure and human capital, and strengthening resilience by addressing potential financial vulnerabilities would also help to foster long-term investments. Improving education and tackling labour market informality would also help make growth more inclusive.

Advanced and emerging market economies both need to seize the window of opportunity provided by a stronger global economy to undertake the structural reforms necessary to boost skills, jobs and incomes. Implementing structural reforms provides the best guarantee for stronger and more inclusive growth.