

EURO AREA

GDP growth is projected to remain around 1¼ per cent in 2017 and 2018. Domestic demand will continue to lead the recovery, benefiting from accommodative monetary policy and, more recently, from welcome mildly expansionary fiscal policy. Exports are projected to strengthen, but at a moderate pace, in line with global growth. The unemployment rate will keep declining, but will remain high at around 9%. Inflation will pick up on the back of higher energy prices and narrowing slack, but will remain below the ECB target.

Monetary policy should remain supportive until inflation is clearly and durably rising towards the ECB target. Several countries have fiscal space that should be used to support demand, concentrating on measures that would raise long-term growth, notably public investment. Boosting private investment will require structural reforms to enhance competition and reduce barriers in services and product markets, lower the still high level of non-performing loans in many countries and foster non-bank financing. Confidence in the monetary union would also gain from further progress to complete the banking union.

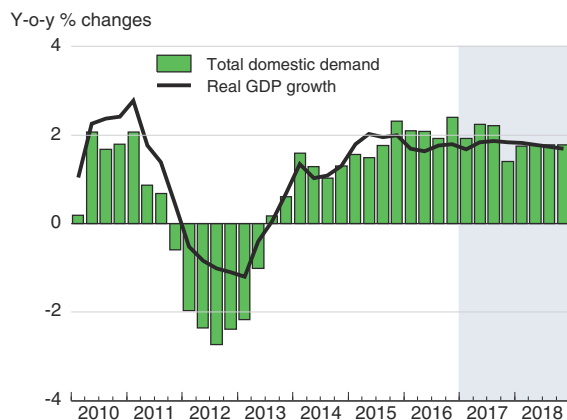
The capacity of the euro area to adjust to trade shocks would be enhanced by strengthening re-training, guidance and job-search support for displaced workers. Increasing the focus of education policies on life-long learning would also help. Promoting R&D, upgrading workers' skills and fostering a greater use of digital technologies would help firms to become more competitive.

The recovery is firming up

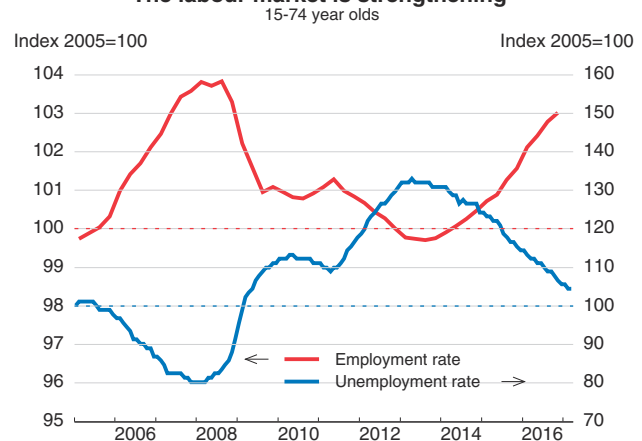
Growth continued in early 2017, with domestic demand remaining the main driver of activity. Exports have also grown robustly, benefiting from stronger global trade and past euro depreciation. The unemployment rate has kept declining but, at 9.5%, is still 2 percentage points above its pre-crisis level. Increases in energy prices and other volatile components have significantly increased headline inflation in the past six months, but core inflation remains subdued.

Euro area

Domestic demand will remain the key driver of growth



The labour market is strengthening



Source: OECD Economic Outlook 101 database; and OECD Short-Term Labour Force Statistics database.

StatLink <http://dx.doi.org/10.1787/888933503054>

Euro area: **Employment, income and inflation**

Percentage changes

	2014	2015	2016	2017	2018
Employment	0.6	1.0	1.8	1.4	1.1
Unemployment rate ¹	11.6	10.9	10.0	9.3	8.9
Compensation per employee ²	1.4	1.4	1.4	1.8	2.1
Labour productivity	0.6	0.8	0.4	0.5	0.7
Unit labour cost	0.7	0.7	1.3	1.2	1.2
Household disposable income	1.2	1.9	2.2	2.8	2.7
GDP deflator	0.9	1.1	0.9	1.2	1.5
Harmonised index of consumer prices	0.4	0.0	0.2	1.7	1.4
Core harmonised index of consumer prices ³	0.8	0.8	0.8	0.9	1.4
Private consumption deflator	0.5	0.1	0.4	1.5	1.4


Note: Covers the euro area countries that are members of the OECD.

1. As a percentage of labour force.

2. In the total economy.

3. Harmonised index of consumer prices excluding energy, food, drink and tobacco.

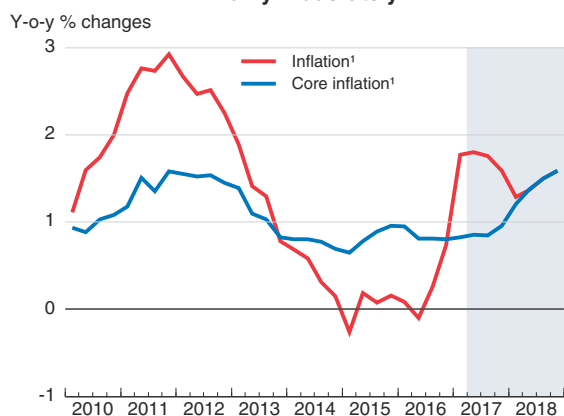
Source: OECD Economic Outlook 101 database.

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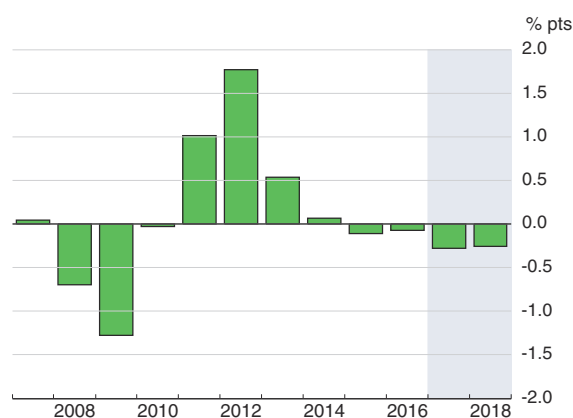
Export orders are strong, business investment is picking up, and job growth should keep its momentum as firms report plans to step up hiring. As a result, business and consumer confidence are now at six-year highs. Economic performance has also started to become more homogenous across countries, with differences in growth rates and employment rates narrowing. Nonetheless, unemployment is still significantly above its 2008 level in many countries. Although investment has started to pick up, as a share of GDP it still remains 10 percentage points below its pre-crisis peak and well below its historical trend. A much stronger recovery in investment is needed to help strengthen productivity growth and ultimately real wages.

Euro area

Inflationary pressures will strengthen only moderately



The fiscal stance has become mildly supportive²



1. Harmonised consumer price index, excluding energy, food, alcohol, and tobacco for core inflation.

2. Change in the underlying primary balance as a percentage of potential GDP.

Source: OECD Economic Outlook 101 database.

StatLink  <http://dx.doi.org/10.1787/888933503035>

Euro area: **Financial indicators**

	2014	2015	2016	2017	2018
Household saving ratio, net ¹	6.2	6.0	5.9	5.8	5.7
General government financial balance ²	-2.6	-2.1	-1.6	-1.2	-0.9
General government gross debt ²	112.3	110.0	109.2	107.9	106.4
General government debt, Maastricht definition ²	94.5	92.8	91.7	90.4	88.9
Current account balance ²	3.1	3.8	3.6	3.3	3.4
Short-term interest rate ³	0.2	0.0	-0.3	-0.3	-0.3
Long-term interest rate ⁴	2.0	1.1	0.8	1.2	1.6

Note: Covers the euro area countries that are members of the OECD.

1. As a percentage of disposable income.

2. As a percentage of GDP.

3. 3-month interbank rate.

4. 10-year government bonds.

Source: OECD Economic Outlook 101 database.

StatLink  <http://dx.doi.org/10.1787/888933505638>

Rebalancing the policy mix towards fiscal policy and structural reform

The European Central Bank (ECB) has extended its net asset purchase programme until at least the end of 2017 but reduced the amount of monthly asset purchases to 60 billion euro from April onwards. The supportive monetary stance remains appropriate, as inflation is still well below the ECB's target of close to but below 2%. However, as the economic outlook improves and inflation approaches the target by end-2018, the degree of monetary stimulus is projected to be somewhat reduced, with the asset purchase programme being tapered off gradually over 2018 and the deposit rate being increased by 15 basis points towards the end of 2018.

Fiscal policy provided a little support to growth in 2016, and is projected to remain slightly expansionary in 2017 and 2018. Several countries have room for additional fiscal

Euro area: **Demand and output**

	2015	2016	2017	2018	Fourth quarter		
					2016	2017	2018
	Current prices EUR billion	Percentage changes from previous year, volume (2014 prices)					
GDP at market prices	10 391.9	1.7	1.8	1.8	1.8	1.9	1.7
Private consumption	5 703.2	1.9	1.4	1.4	1.9	1.4	1.3
Government consumption	2 153.7	1.8	1.2	1.3	1.5	1.4	1.2
Gross fixed investment	2 052.5	3.4	3.4	3.3	5.0	1.6	3.5
Final domestic demand	9 909.4	2.2	1.8	1.8	2.4	1.4	1.8
Stockbuilding ¹	11.5	-0.1	0.1	0.0			
Total domestic demand	9 920.9	2.1	1.8	1.8	2.4	1.3	1.8
Net exports ¹	471.0	-0.4	0.1	0.1			

Note: Detailed quarterly projections are reported for the major seven countries, the euro area and the total OECD in the Statistical Annex. Covers the euro area countries that are members of the OECD.

1. Contributions to changes in real GDP, actual amount in the first column.

Source: OECD Economic Outlook 101 database.


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Euro area: **External indicators**

	2014	2015	2016	2017	2018
	USD billion				
Foreign balance	474.8	522.6	526.2	499	530
Invisibles, net	- 68.4	- 86.2	- 102.4	- 107	- 114
Current account balance	406.4	436.4	423.8	392	416

Note: Covers the euro area countries that are members of the OECD.

Source: OECD Economic Outlook 101 database.

StatLink  <http://dx.doi.org/10.1787/888933505676>

expansion and they should use it to strengthen aggregate demand and long-term growth. Fiscal expansion could for example be facilitated by excluding net public investment spending from assessment of compliance with the Stability and Growth Pact. To avoid some countries once again facing high interest rates on their public debt, which would constrain their fiscal space, further progress with the banking union and the governance of the euro area is needed. Collective action is needed to complete the banking union by creating a common fiscal backstop to the Single Resolution Fund, further harmonising bank regulation and reinforcing deposit insurance at the national and European levels. It is also crucial to break the negative feedback loop between banks and sovereigns. This requires finding a market solution, if needed with public support, to clean up banks' balance sheets in countries with high levels of non-performing loans.

Higher investment and productivity are crucial for a more dynamic recovery and higher potential growth and to improve the value-added content of exports. Opportunities exist in a number of euro area countries to introduce product market reforms to boost competition, encourage innovation and business dynamism and enhance diffusion of new technologies. The adoption of competition-enhancing reforms could be facilitated by job search support and re-training for displaced workers. Faster implementation of Europe's digital single market and the swift completion of the single market in network sectors and services are also vital to foster investment and productivity growth and to strengthen intra and extra European Union trade. Reforms that stimulate investment, such as reducing barriers to entry in services in countries with current account surpluses, would help to rebalance the large euro area current account surplus.

Growth will remain robust

GDP growth is projected to remain around 1¼ per cent each year in 2017 and 2018. Domestic demand will continue to be the key driver of growth. Business investment should rise as foreign and domestic demand improves and financing conditions remain supportive. Residential investment will keep recovering, supported by growing disposable income. Household spending will remain robust, aided by favourable bank lending conditions and improving labour market conditions, but will lose some steam as higher inflation will limit gains in real disposable income. Unemployment will fall, but significant disparities across euro area countries will persist. Exports are projected to strengthen as global trade demand picks up. A sizeable area-wide current account surplus is likely to decline only marginally, with a projected continuation of large current account surpluses in Germany and the Netherlands.

A growing backlash against globalisation could trigger protectionist policies and undermine international trade, with lower growth as a result. Brexit negotiations remain a significant risk: a break-up of negotiations or the prospect of an unfavourable deal could hurt confidence and trade. As growth and inflation prospects in core euro area economies improve, there is a risk that monetary policy tightens too rapidly, weighing on the recovery in countries with high unemployment, high public and private debt and large negative output gaps. On the upside, more rapid progress with policy reforms could improve financial conditions, confidence and activity. A new cycle of structural funds and a faster implementation of the Investment Plan could lead to higher public and private investment and growth. Faster progress in cleaning up bank balance sheets, together with regained momentum in European integration, would also boost GDP growth.