What is the global economic outlook?

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The outlook

Real GDP growth, in per cent

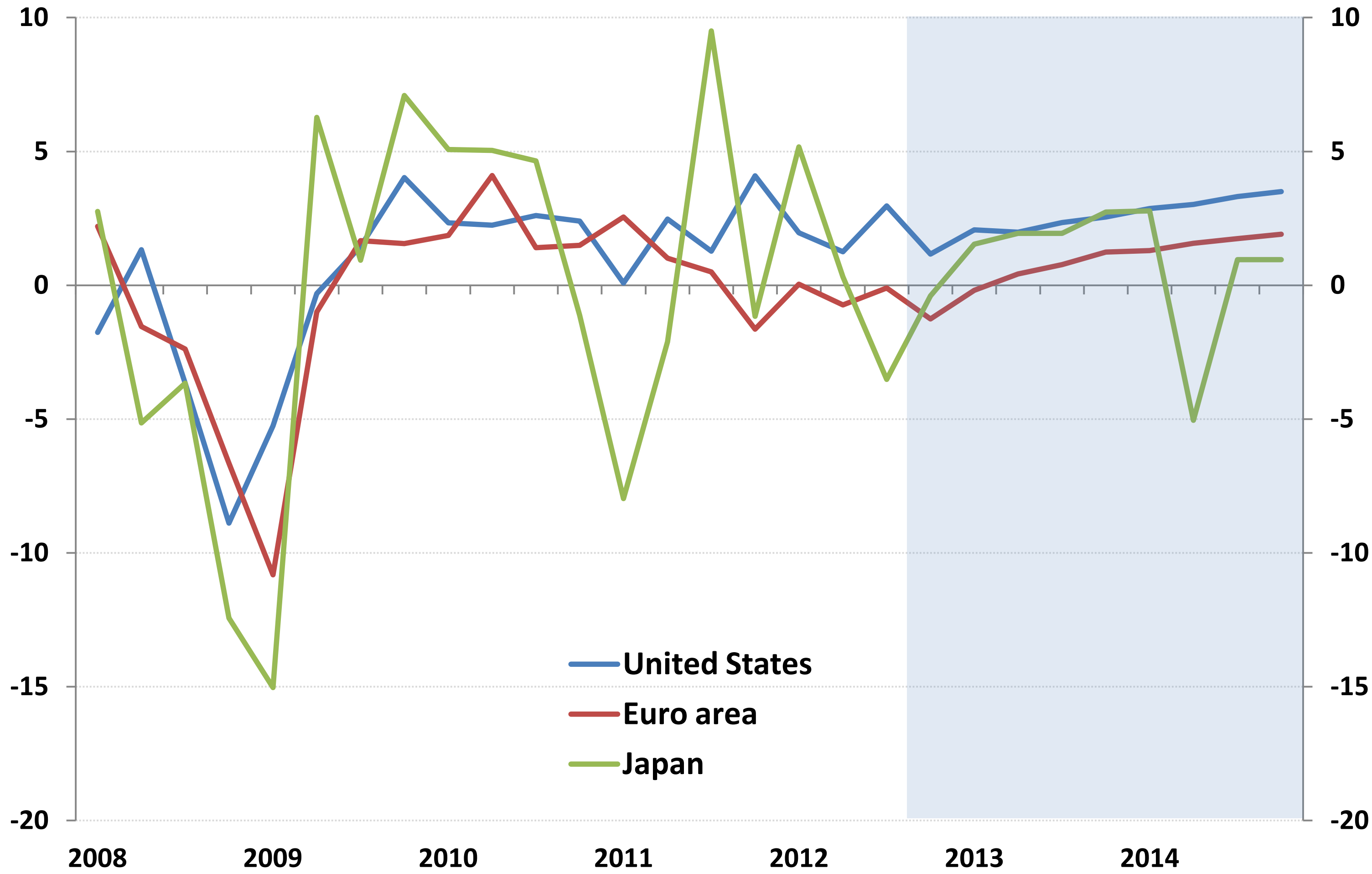
	2011	2012	2013	2014
United States	1.8	2.2	2.0	2.8
Euro area	1.5	-0.4	-0.1	1.3
Japan	-0.7	1.6	0.7	0.8
Total OECD	**1.8**	**1.4**	**1.4**	**2.3**
Brazil	2.7	1.5	4.0	4.1
China	9.3	7.5	8.5	8.9
India	7.8	4.5	5.9	7.0
Indonesia	6.5	6.2	6.3	6.5
Russian Federation	4.3	3.4	3.8	4.1
South Africa	3.1	2.6	3.3	4.0

Source: OECD Economic Outlook 92 database.

Projections - OECD Big 3

Projections

Annualised quarterly real GDP growth, in per cent

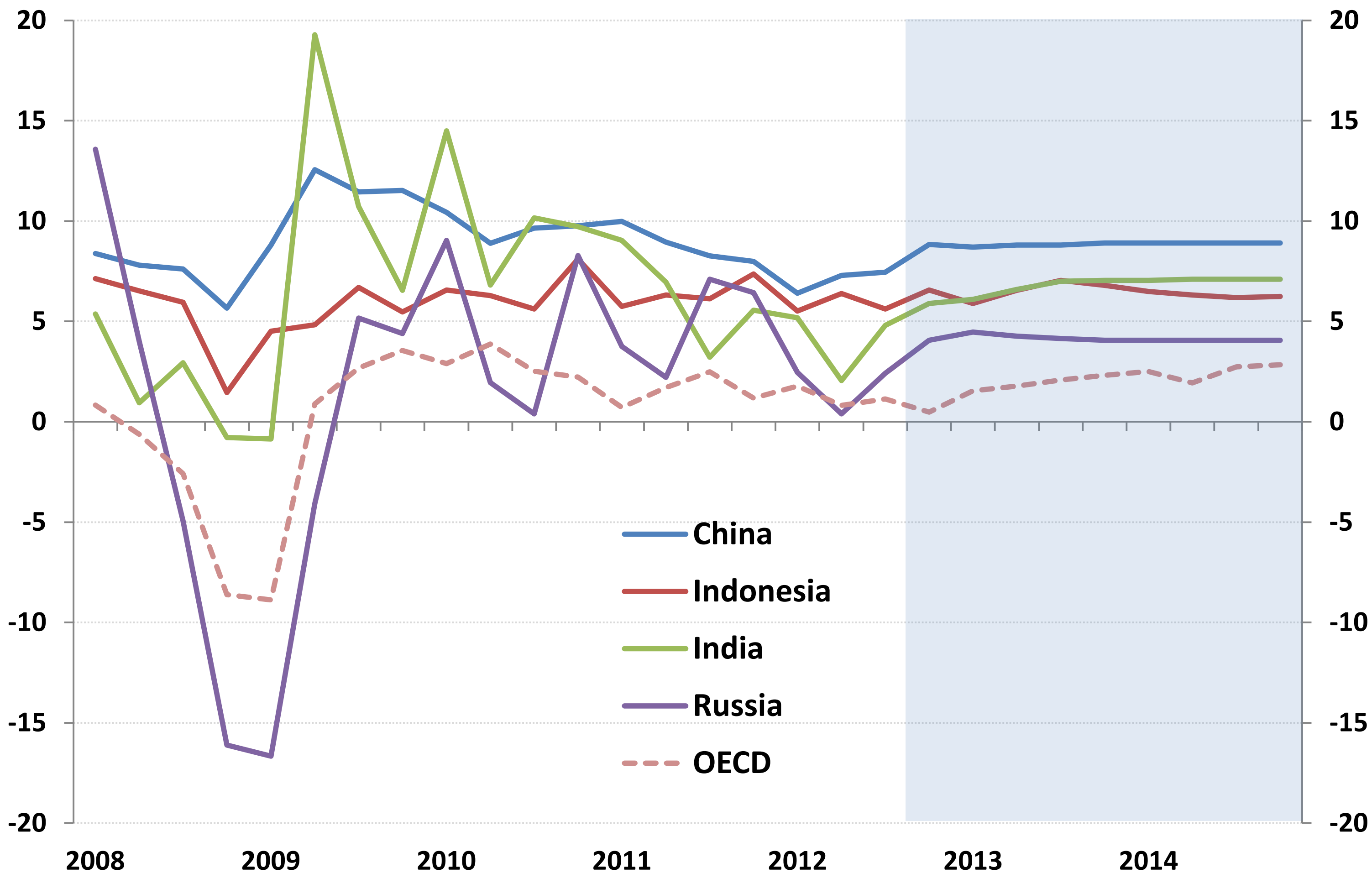


Source: OECD Economic Outlook 92 database.

Projections - EMEs

Projections

Annualised quarterly real GDP growth, in per cent



Source: OECD Economic Outlook 92 database.

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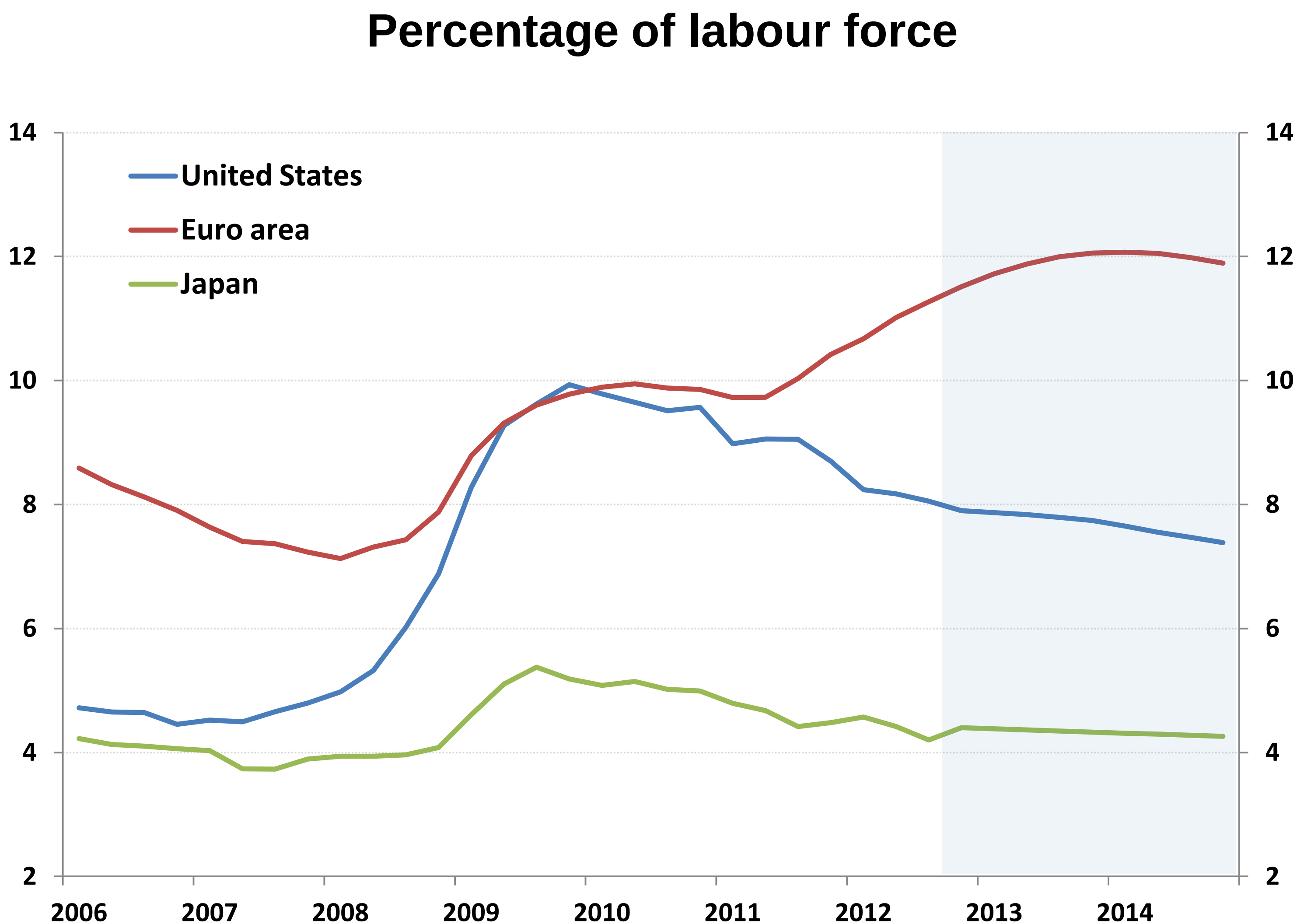
Unemployment

Unemployment rates diverging



Source: OECD Economic Outlook 92 database.

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Downside risks to the outlook

Downside risks

- **Euro area crisis is the largest downside risk :**
  - Policy measures (OMT, ESM) have dampened market pressures but risks of further flare ups remain.
  - Negative financial feed-back loops still operational.
  - Underlying rebalancing still in progress.
- **Excessive budgetary tightening in the United States (the "fiscal cliff")**
- **Geopolitical risk to oil prices**
- **High unemployment undermining confidence**
- **EMEs transition to domestic sources of growth**

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Upside risks to the outlook

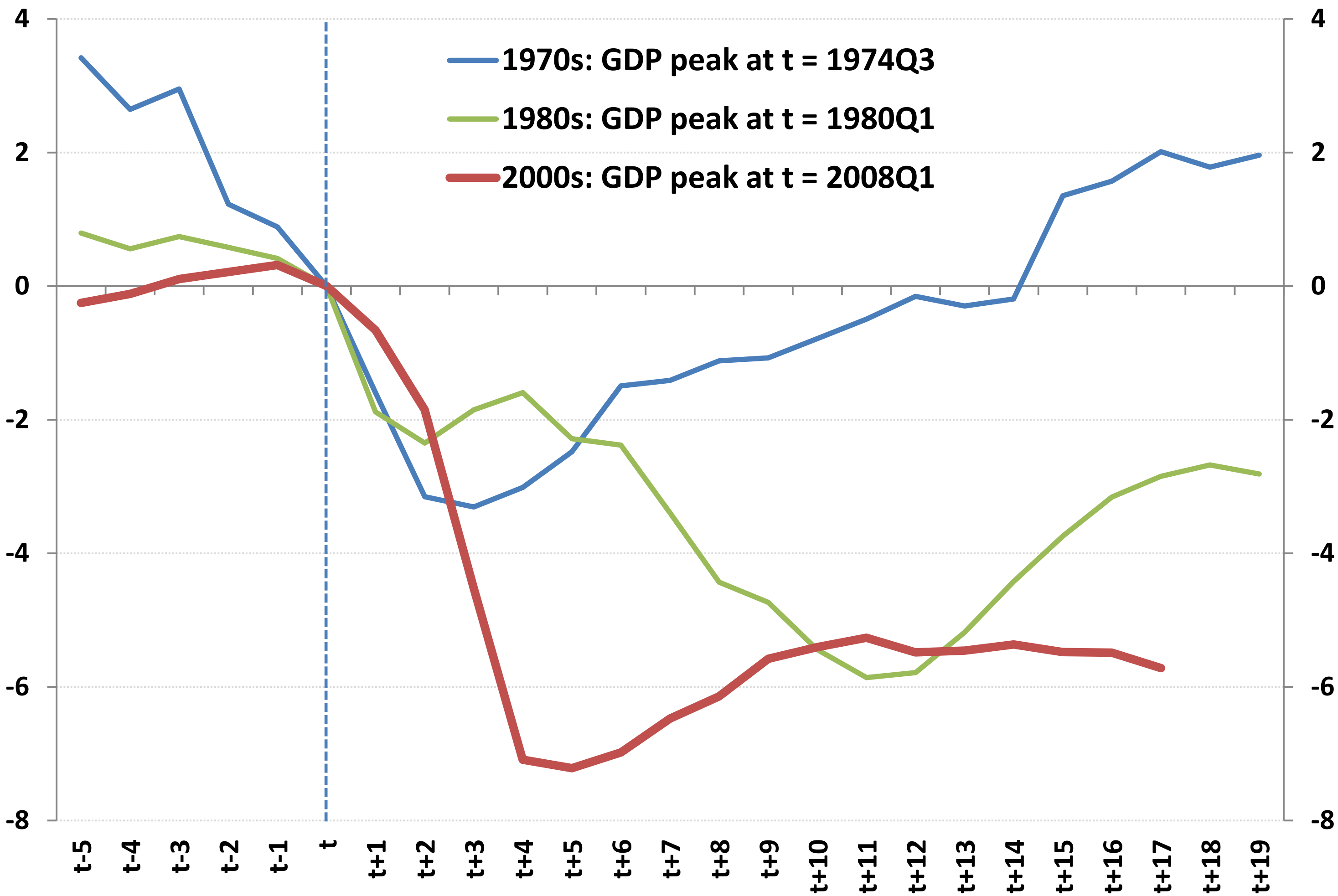
Upside risks

- Comprehensive resolution of euro area crisis
- Medium-term fiscal framework agreed for United States, and releasing pent up demand
- Structural reform benefits flowing through earlier than assumed

Recoveries compared

Recoveries compared

Cumulative change in OECD-wide output gap from quarter *t*



Source: OECD Economic Outlook 92 database.

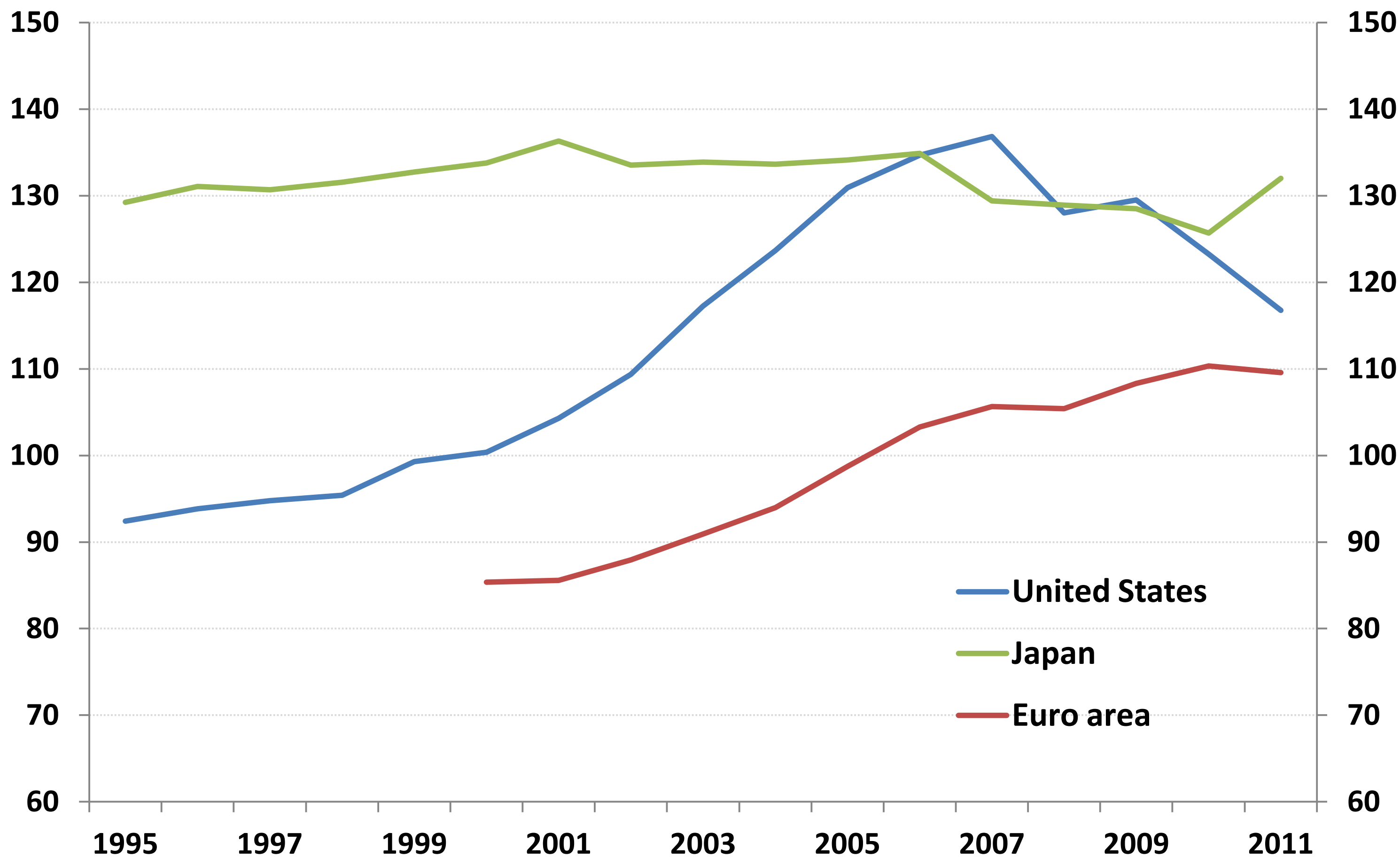
Reasons for the slow recovery

- **Private sector deleveraging :**
  - More advanced in the US, less in the euro area but mixed.
- **Fiscal consolidation :**
  - Fiscal consolidation, while necessary, has affected growth.
- **Euro area crisis :**
  - Crisis has dragged on longer than necessary due to insufficient and delayed policy action.
- **EMEs slowdown :**
  - Domestic factors and only partly induced by euro area crisis.

Deleveraging is progressing

Deleveraging

Household gross debt, in percent of net disposable income

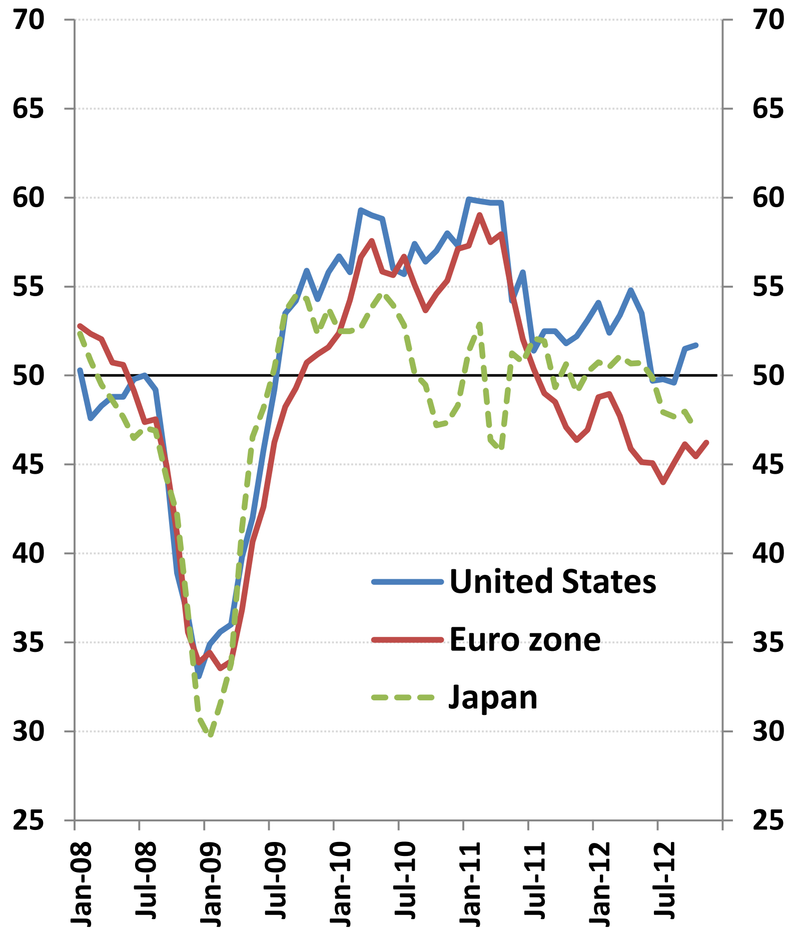


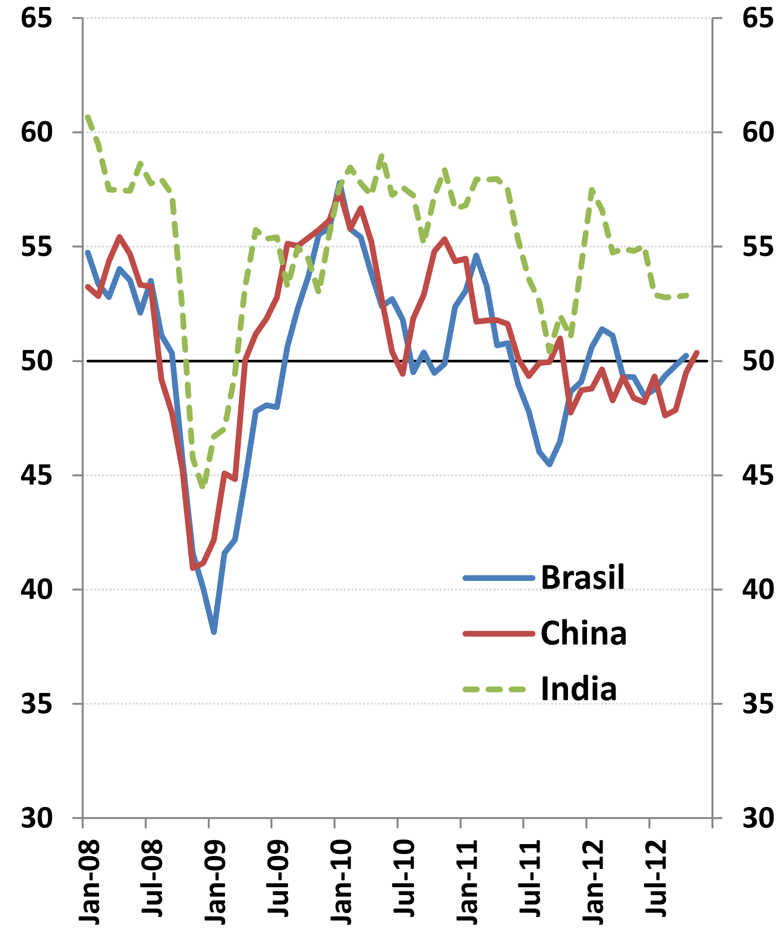
Note: Data for USA and Japan are not consolidated. For Japan, net disposable income for the year 2011 is an estimate from the OECD Economic Outlook 92 database.
Source: OECD Annual National Accounts, and OECD Economic Outlook 92 database.

Business sentiment is mixed

Business sentiment

Purchasing Managers Index (PMI) for manufacturing



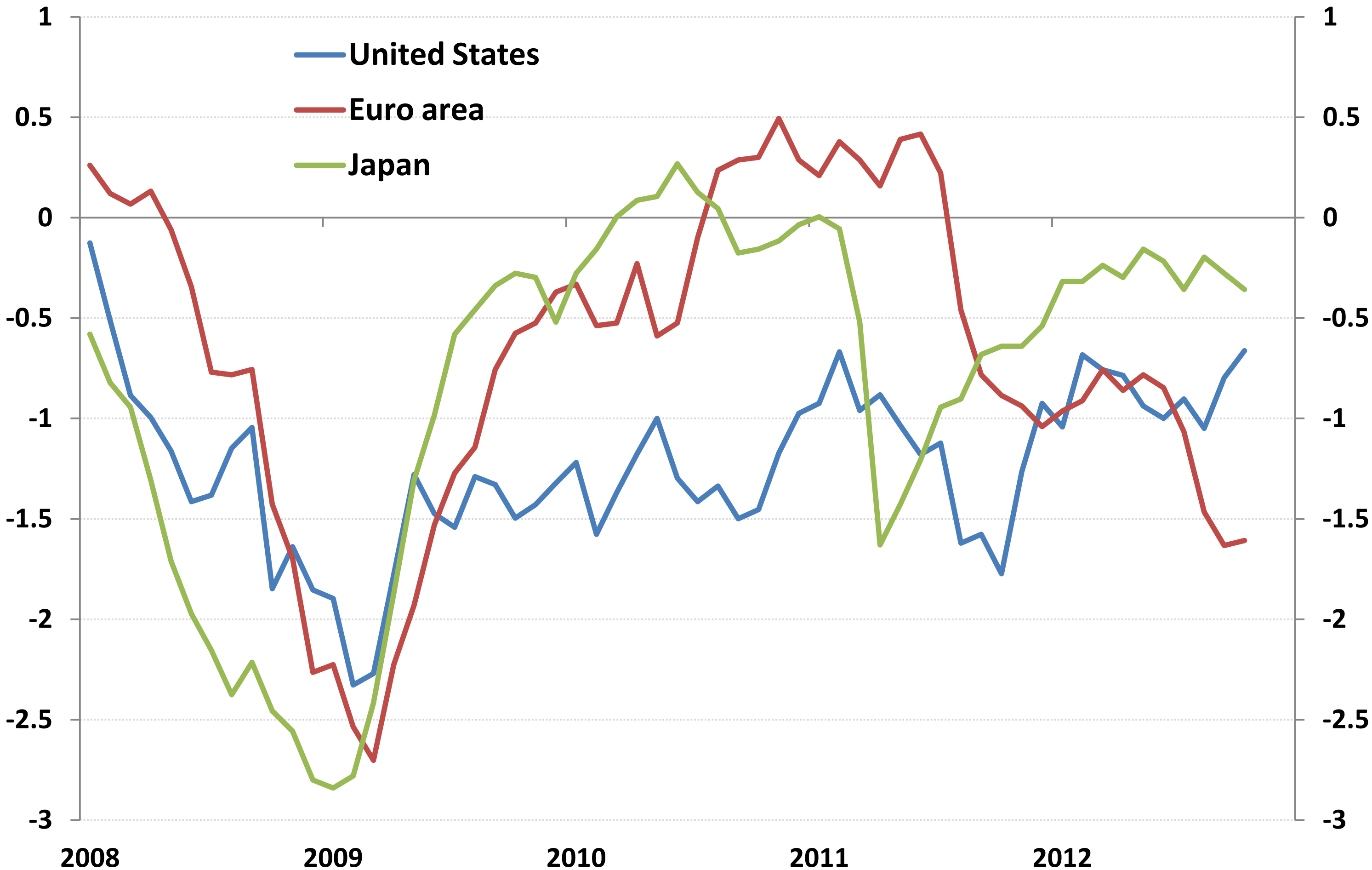


Source: Markit.

Consumer confidence is weak

Consumer confidence

Consumer confidence survey indicators, standard deviations



Note: Normalised at 1999M1 to 2012M10 period average and presented in units of standard deviation. Values above zero signify levels of consumer confidence above the period average.
Source: Datastream, and European Commission.

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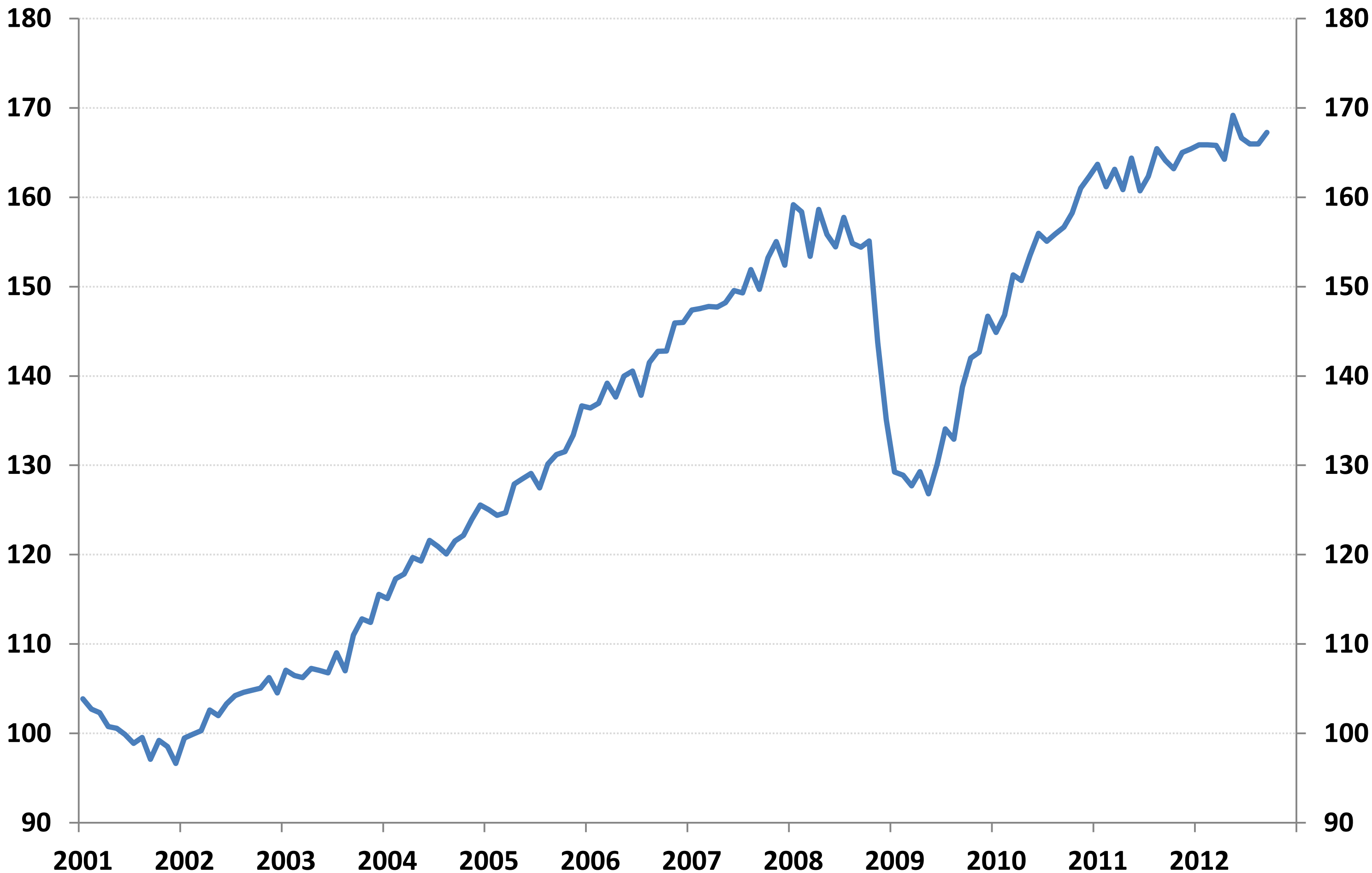
World trade has stopped growing

World trade

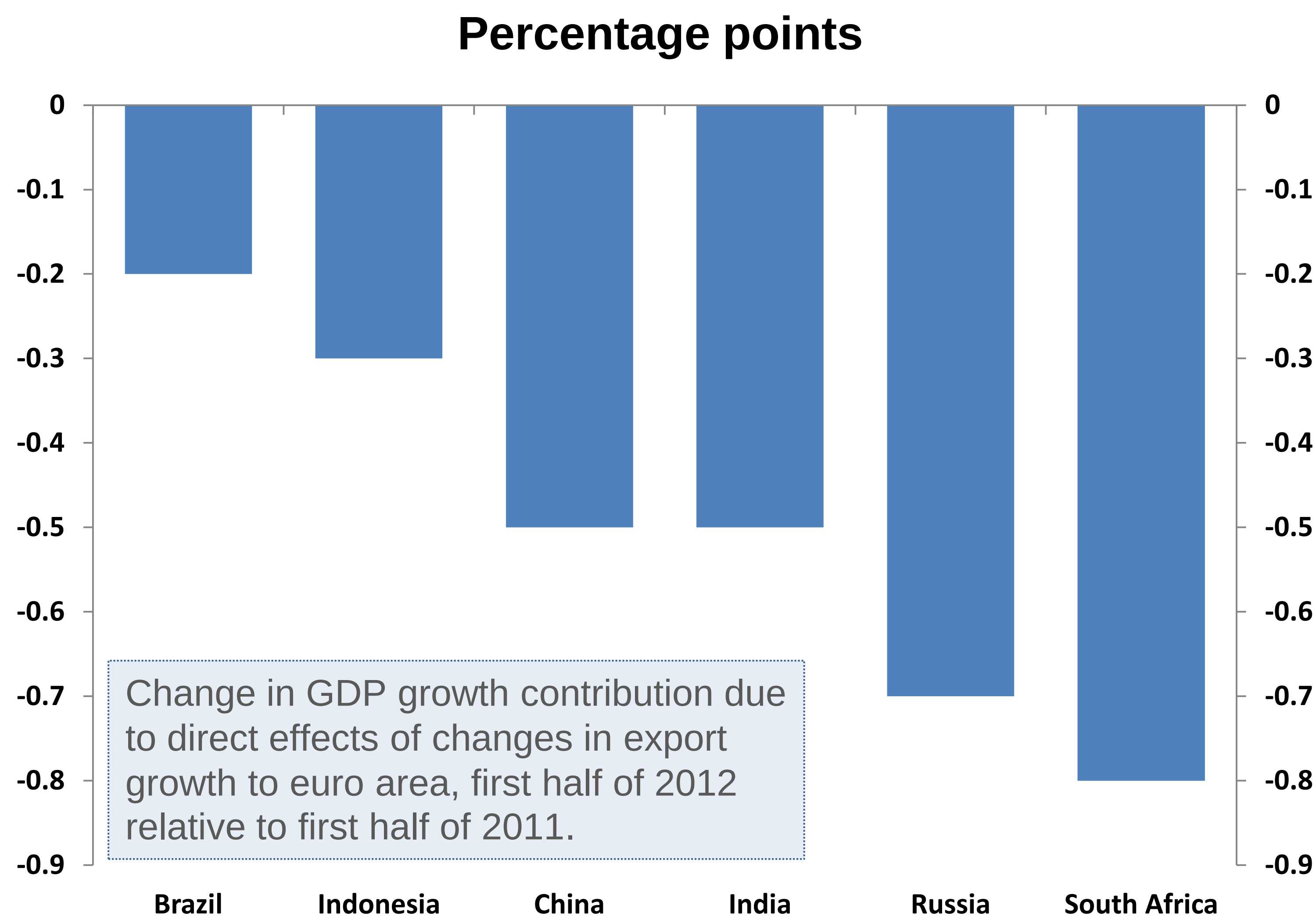
CPB indicator of world merchandise trade, 2001 = 100



Source: CPB.

Euro area trade spillovers on emerging economies

Euro area impact on trade

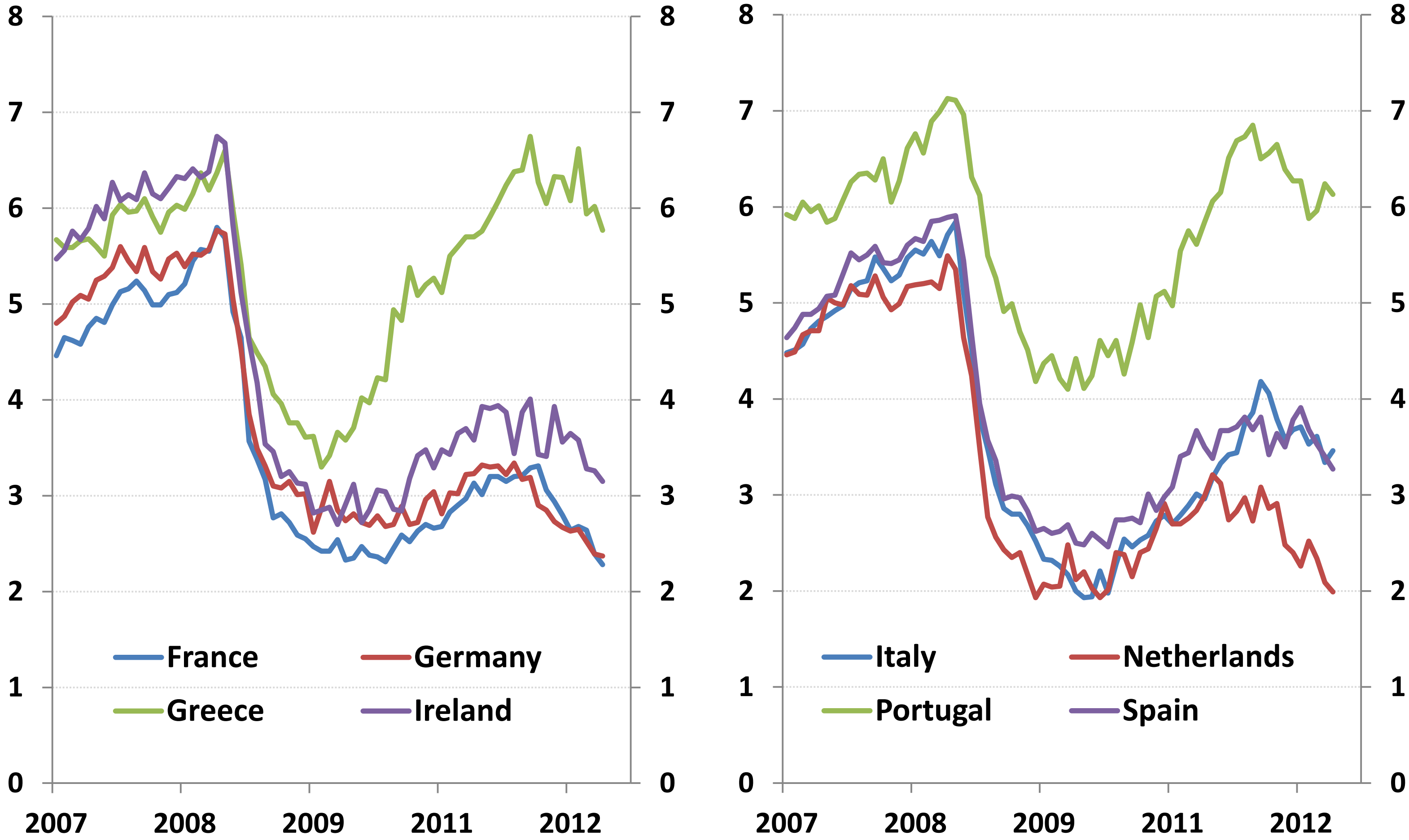


Source: OECD Economic Outlook 92, and OECD calculations.

Euro area cost of credit

The cost of credit among euro area countries has diverged

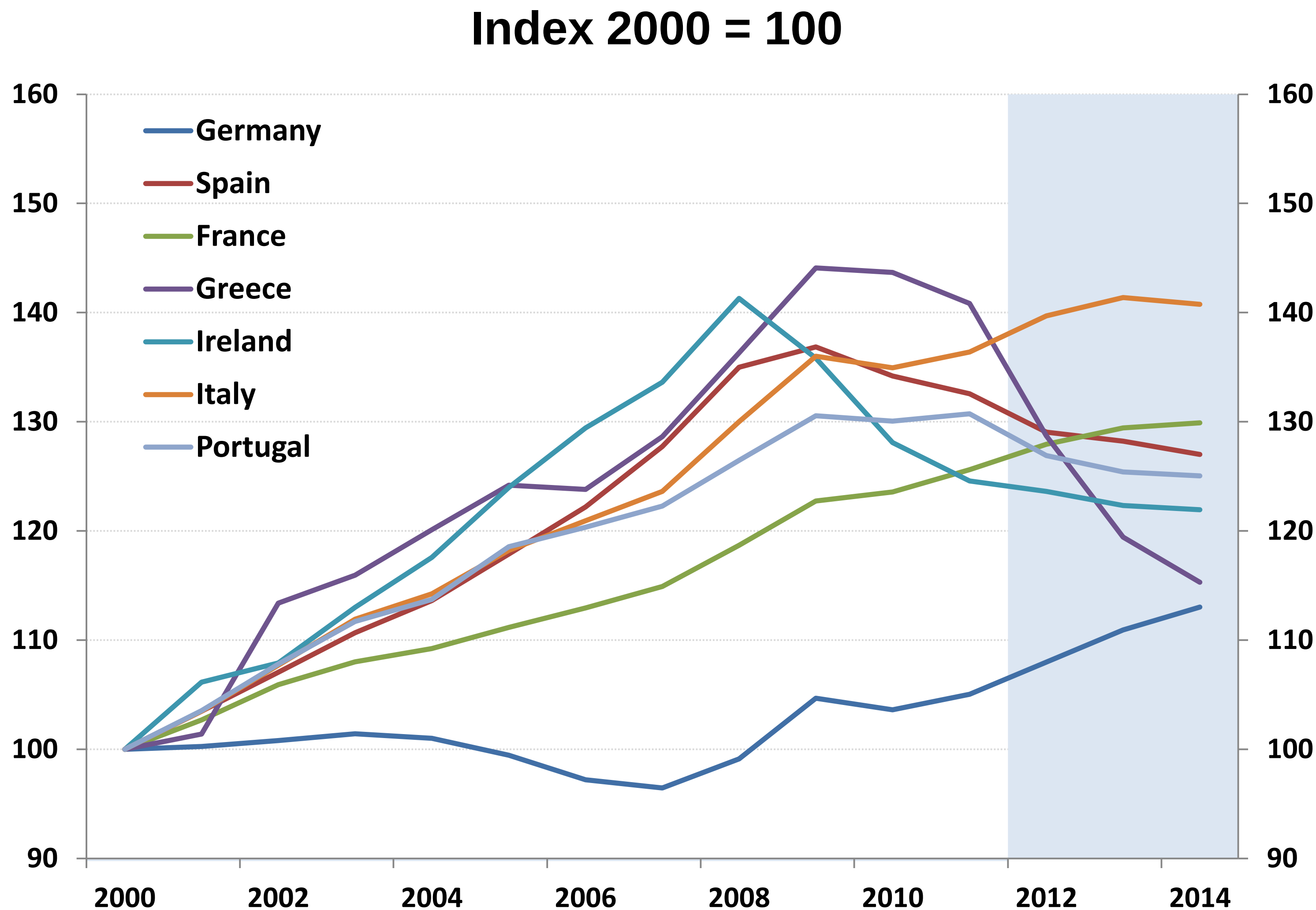
Bank interest rates for lending to business, percent



Note: Cost of credit is defined as interest rates on new loans to non-financial corporations (all maturities) with the exception of Greece where it refers to new loans with maturity of up to one year. Last observation is September 2012.
Source: European Central Bank.

Unit labour costs

Euro area unit labour costs

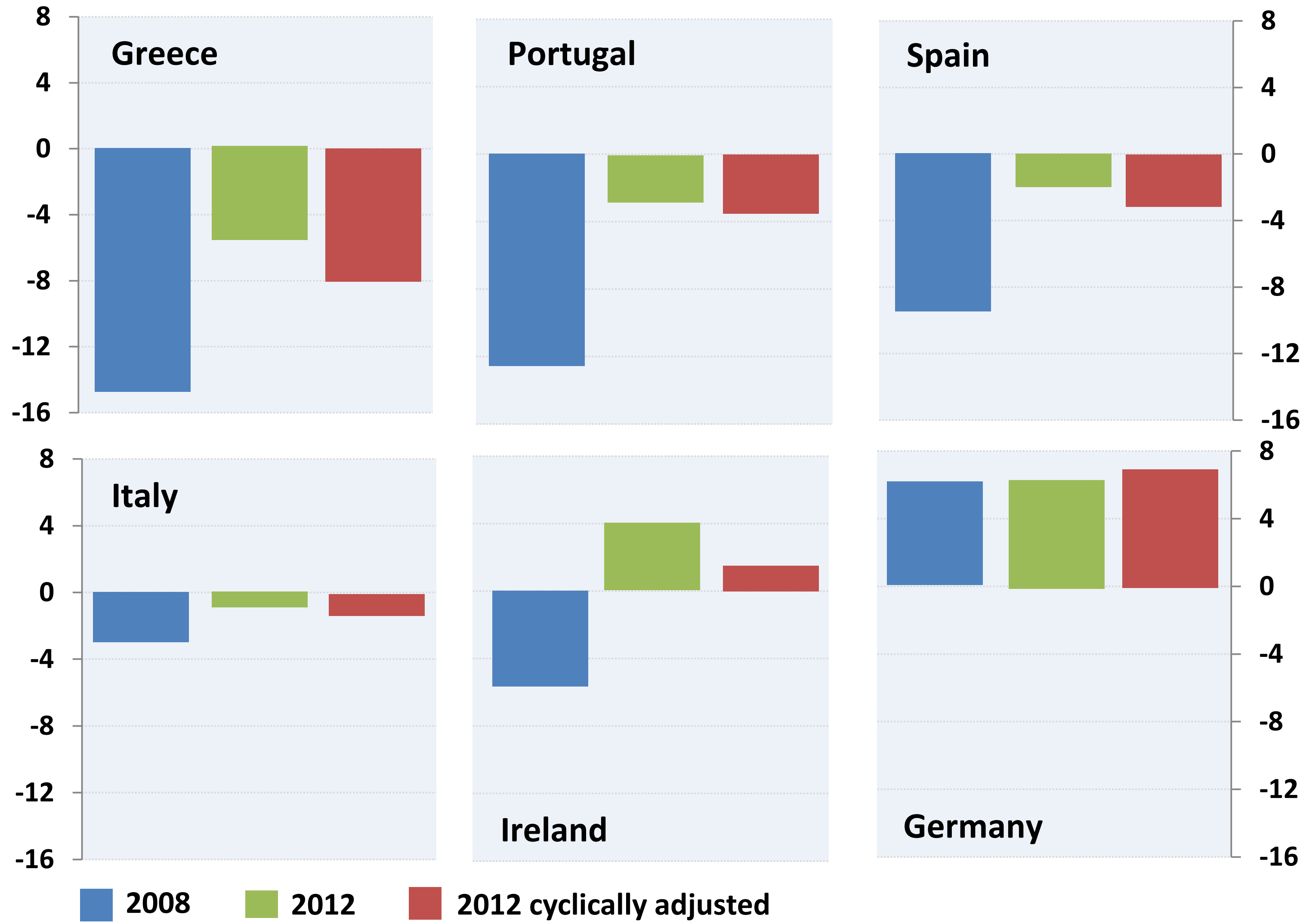


Note: The figures shown are for whole economy unit labour costs. If wage developments in the public sector diverge from those in the rest of the economy, changes in private sector costs may differ from those shown. This may mean that economy-wide labour costs are falling more sharply than private sector costs in the EU/IMF programme countries. *Source:* OECD Economic Outlook 92 database.

Rebalancing in the euro area countries

Rebalancing in the euro area

Current account balances, in per cent of GDP

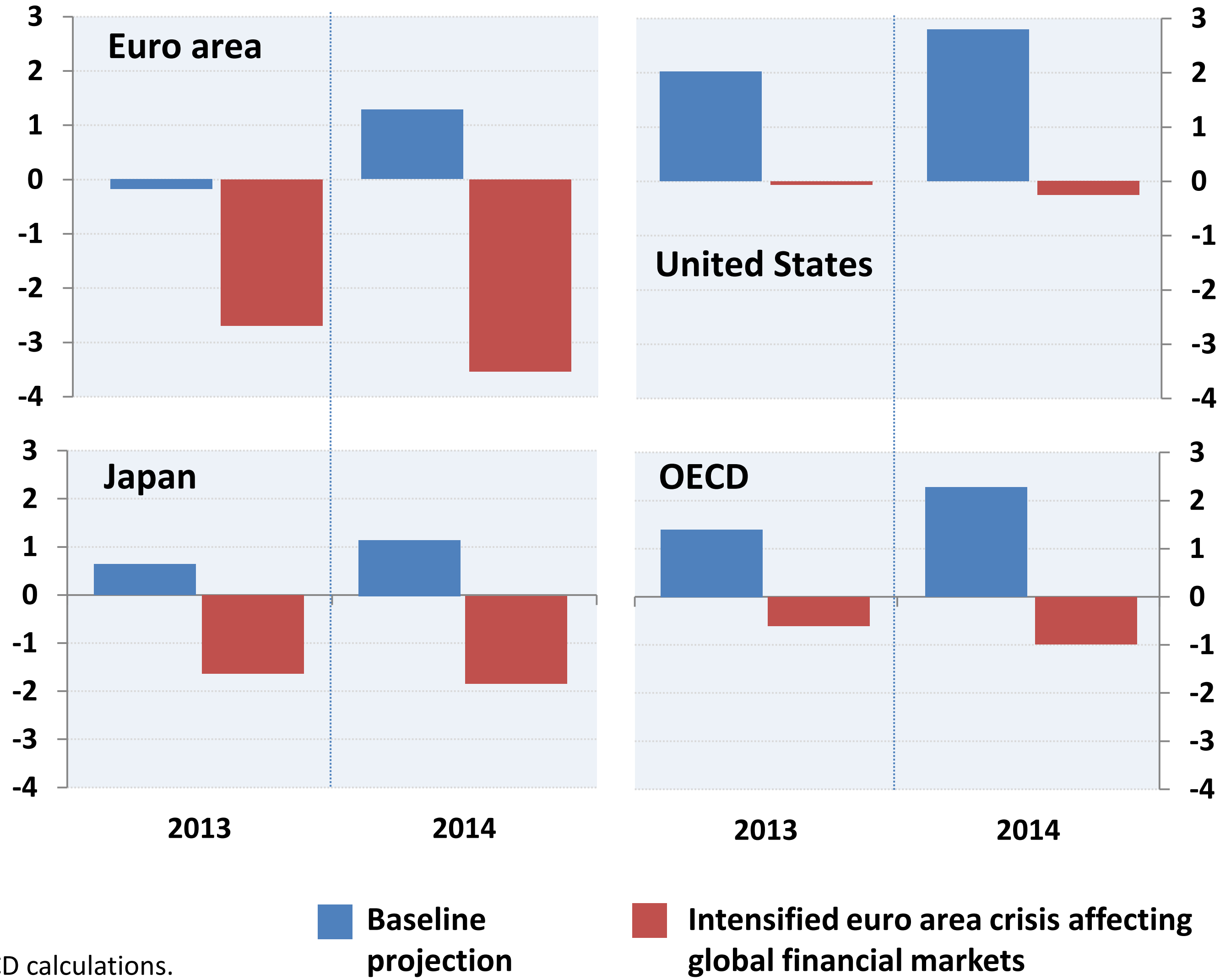


Note: Assuming the economy's cyclical position is the same as that of its (trade weighted) trading partners.
Source: OECD Economic Outlook 92 database, and OECD calculations.

Downside risks from intensification of euro area crisis

Downside scenario

GDP growth, per cent



Source: OECD calculations.

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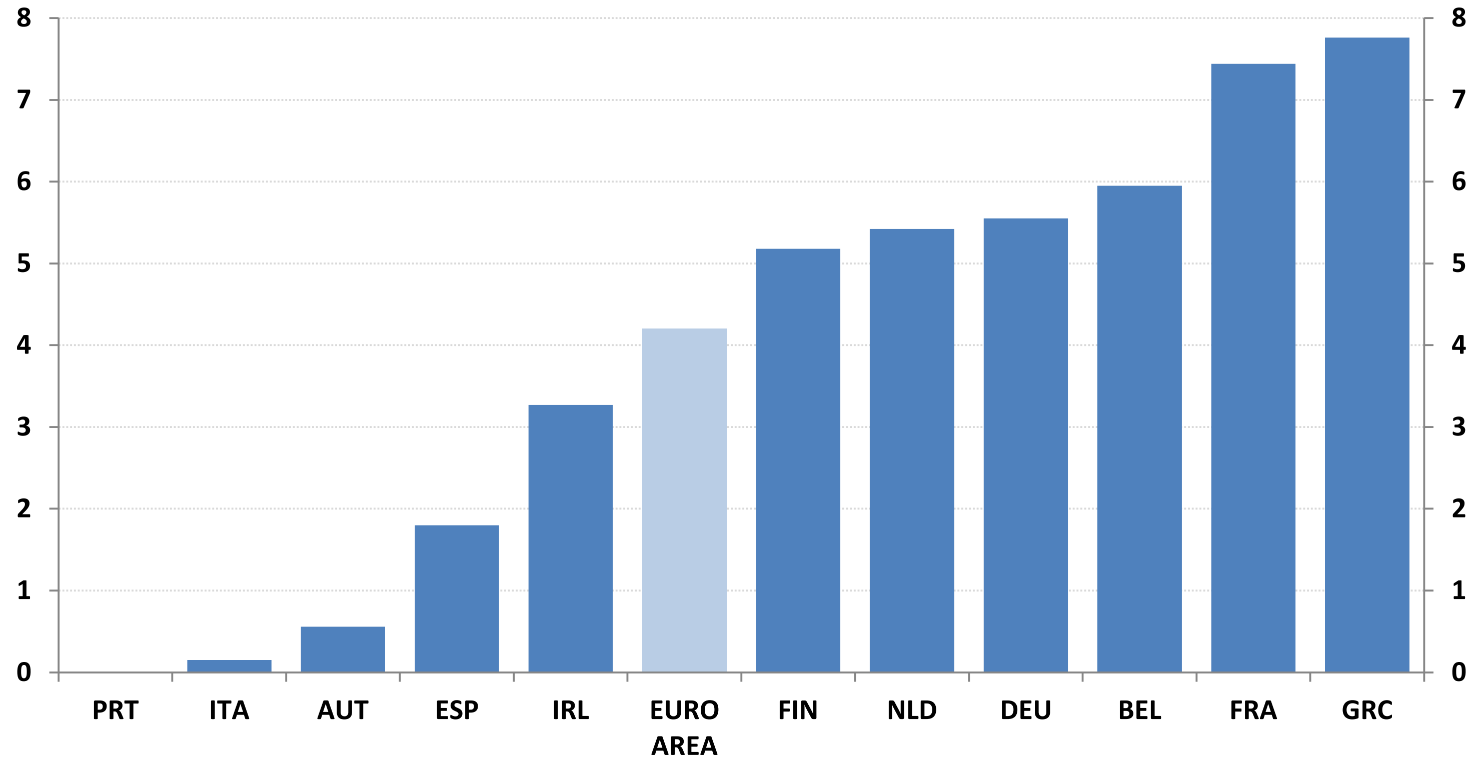
Policies for the euro area

- **Break feedback loop between banks and governments :**
  - Strengthen capital position of banks.
  - Banking union (single supervisor, bank resolution, common deposit insurance, common fiscal backstop).
- **Break feedback loop between exit risk, bond yields and debt sustainability :**
  - Commitment to reforms and ESM/OMT.
  - Fiscal Compact.
  - Deal with legacy debt.
- **Boost growth :**
  - Structural reforms and Single Market.

Capital positions of euro area banks need strengthening

Euro area bank capitalisation

Required increases in capital of large banks to reach a 5% leverage ratio, in percent of GDP



Note: Based on around 200 euro area banks. The number of banks in the sample for each country displayed and the corresponding number of banks with less than 5% leverage ratio (in brackets) are as follows: Austria 19 (8), Belgium 9 (4), Finland 5 (3), France 8 (8), Germany 60 (30), Greece 9 (4), Ireland 10 (2), Italy 33 (8), Netherlands 9 (5), Portugal 8 (0) and Spain 27 (8).
Source: Company Reports, and OECD.

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Upside for the euro area

- **Fiscal consolidation is progressing :**
  - Immediately beyond the forecast period, debt-to-GDP ratios falling in most euro area countries, boosting confidence.
- **Structural reforms may have larger than expected positive short-run effects**
- **Progress with institution building may proceed more rapidly than expected and have strong confidence effects**

Monetary policy

- **Further easing required in Japan, euro area and some EMEs. United States should keep current stance**

- **If downside risks materialise, a stronger response would be warranted :**
  - Including further quantitative easing, and forward guidance.

- **Caveats :**
  - Creating conditions for high leverage and bubbles.
  - Misallocation of credit as costs of forbearance and ever-greening fall.

Fiscal policy (1)

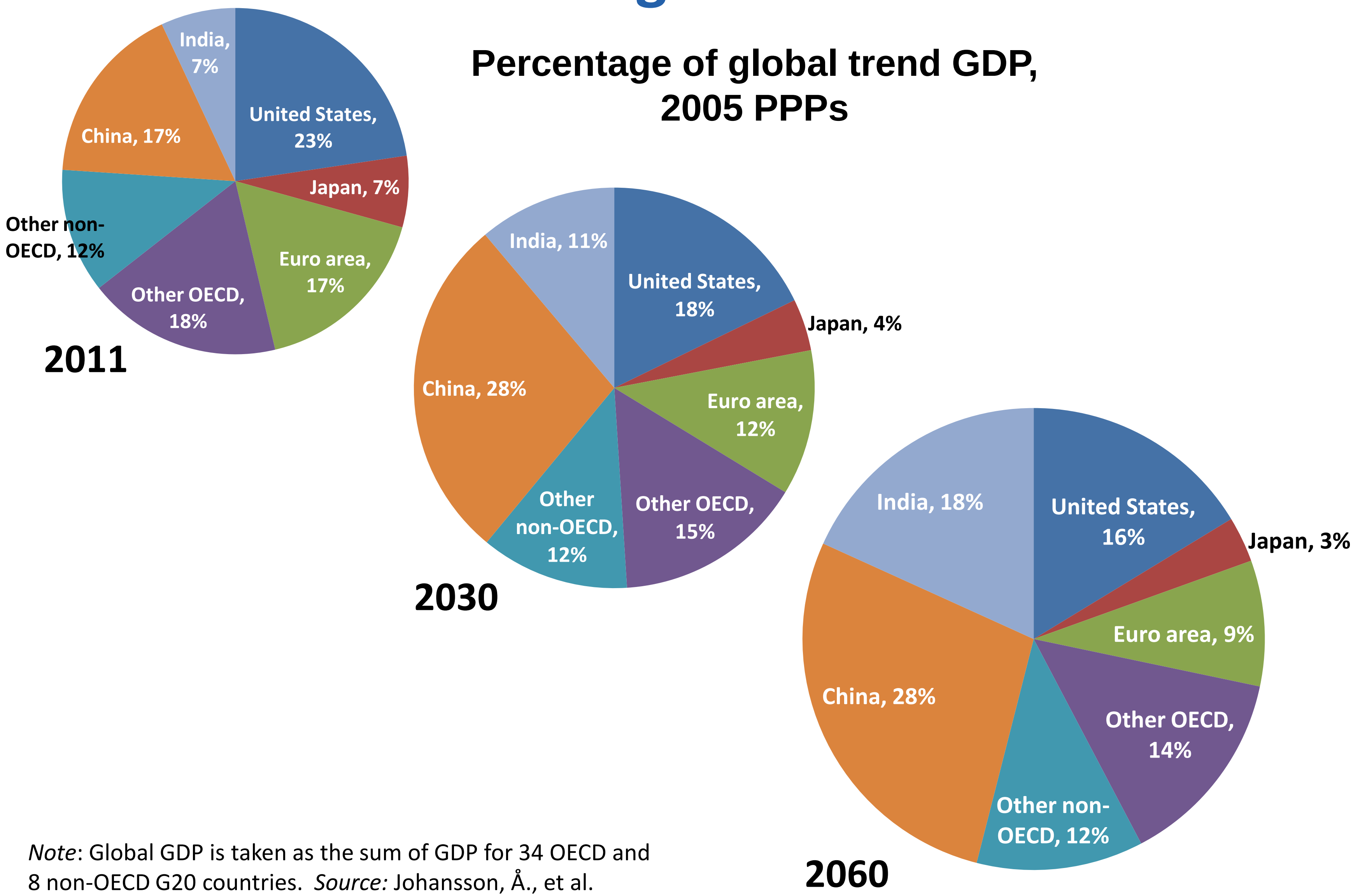
- **Multipliers are likely to be high at the current juncture :**
  - Significant weight on expenditure cuts.
  - Limited room for monetary easing and impaired financial system.
  - Simultaneous consolidations across countries.
- **General recommendations :**
  - Choose an appropriate pace of consolidation.
  - Let automatic stabilizers play around structural consolidation path.
  - Countries with space should ease if downside materialises.
- **United States : link fiscal cliff resolution to medium term consolidation**
- **Euro area : more effectiveness by coordinated action**

Fiscal policy (2)

- **Consolidation needs to balance :**
  - Short-term demand impact.
  - Social impact.
  - Long-term growth impact.
- **Mix of consolidation instruments can improve tradeoffs**
- **Preferred instruments :**
  - Reduce tax breaks to wealthy and cut un-warranted tax expenditures.
  - Increase taxes on real estate and energy in some countries.
  - Shift taxes from labour to consumption.
  - Tackle public spending inefficiencies.
- **Consolidation and inequality**
  - Transfers versus taxes.

Long-term shift in the composition of global GDP

Long-term scenario



Note: Global GDP is taken as the sum of GDP for 34 OECD and 8 non-OECD G20 countries. *Source:* Johansson, Å., et al. (2012), OECD Economic Policy Papers, No. 3.

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Long-term developments and policy implications

Long-term scenario and policy

- **Long-term global developments :**
  - Growth will be sustained by emerging economies but at a declining rate.
  - Relative sizes of economies will shift dramatically.
  - GDP per capita gaps will narrow, but differences will persist.
  - Saving will decline in line with demographics.
  - Current account imbalances may build up.
- **Role of policy :**
  - Product market reforms will speed income convergence.
  - Labour market and retirement reforms and rising education levels will lift long-run GDP.
  - Ambitious fiscal consolidation and structural reforms would reduce imbalances and boost growth.

Thank you