ECONOMIC OUTLOOK
No. 91

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10h (Paris time)

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Secretary-General

&

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For a video link to the press conference and related material:
www.oecd.org/OECDEconomicOutlook

Summary of projections

				2011		2012				2013				2011	2012	2013
	2011	2012	2013	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q4 / Q4		
								Per cent								
Real GDP growth																
United States	1.7	2.4	2.6	1.8	3.0	2.2	2.5	2.5	2.5	2.6	2.7	2.8	2.8	1.6	2.4	2.7
Euro area	1.5	-0.1	0.9	0.7	-1.5	0.0	-0.3	0.3	0.7	0.9	1.2	1.5	1.7	0.7	0.2	1.3
Japan	-0.7	2.0	1.5	7.1	-0.7	4.1	0.8	1.2	1.4	1.5	1.6	1.6	1.8	-0.6	1.9	1.6
Total OECD	1.8	1.6	2.2	2.5	0.9	1.6	1.5	1.9	2.1	2.2	2.4	2.5	2.7	1.4	1.8	2.4
Inflation[1]								year-on-year								
United States	2.5	2.0	1.8	2.9	2.7	2.3	2.0	1.9	2.0	1.9	1.8	1.8	1.8			
Euro area	2.7	2.4	1.9	2.7	2.9	2.7	2.4	2.5	2.2	2.1	2.0	1.9	1.6			
Japan	-0.3	-0.2	-0.2	0.2	-0.3	0.3	-0.3	-0.4	-0.2	-0.8	-0.1	-0.1	-0.1			
Total OECD	2.5	2.2	1.9	2.7	2.7	2.4	2.2	2.2	2.1	2.0	1.9	1.9	1.9			
Unemployment rate[2]																
United States	8.9	8.1	7.6	9.1	8.7	8.2	8.1	8.0	7.9	7.8	7.7	7.5	7.4			
Euro area	10.0	10.8	11.1	10.0	10.4	10.6	10.8	10.9	11.1	11.1	11.1	11.1	11.0			
Japan	4.6	4.5	4.4	4.4	4.5	4.6	4.5	4.5	4.5	4.4	4.4	4.3	4.3			
Total OECD	8.0	8.0	7.9	8.0	7.9	7.9	7.9	8.0	8.0	8.0	7.9	7.8	7.7			
World trade growth	6.0	4.1	7.0	4.9	0.1	4.6	5.5	6.3	6.7	7.1	7.4	7.6	7.8	3.4	5.7	7.5
Current account balance[3]																
United States	-3.1	-3.7	-4.3													
Euro area	0.5	1.0	1.5													
Japan	2.1	1.6	1.9													
Total OECD	-0.6	-0.8	-0.8													
Fiscal balance[3]																
United States	-9.7	-8.3	-6.5													
Euro area	-4.1	-3.0	-2.0													
Japan	-9.5	-9.9	-10.1													
Total OECD	-6.3	-5.3	-4.2													
Short-term interest rate																
United States	0.4	0.4	0.3	0.4	0.5	0.4	0.4	0.4	0.3	0.3	0.2	0.3	0.4			
Euro area	1.4	0.6	0.3	1.6	1.5	1.0	0.6	0.4	0.4	0.3	0.3	0.2	0.2			
Japan	0.1	0.3	0.3	0.1	0.1	0.1	0.3	0.3	0.3	0.3	0.3	0.3	0.3			

Note: Real GDP growth and world trade growth (the arithmetic average of world merchandise import and export volumes) are seasonally and working-day adjusted annualised rates. Inflation is measured by the increase in the consumer price index or private consumption deflator for the United States and total OECD. The "fourth quarter" columns are expressed in year-on-year growth rates where appropriate and in levels otherwise. Interest rates are for the United States: 3-month eurodollar deposit; Japan: 3-month certificate of deposits; euro area: 3-month interbank rate.

The cut-off date for information used in the compilation of the projections is 15 May 2012.

1. USA; price index for personal consumption expenditure, Japan; consumer price index and the euro area; harmonised index of consumer prices.
2. Per cent of the labour force.
3. Per cent of GDP.

Source: OECD Economic Outlook 91 database.

Country projections

Annual real GDP growth, in per cent

	2010	2011	2012	2013
Australia	2.4	2.2	3.1	3.7
Austria	2.5	3.0	0.8	1.6
Belgium	2.2	2.0	0.4	1.3
Canada	3.2	2.5	2.2	2.6
Chile	6.1	5.9	4.4	5.1
Czech Republic	2.6	1.7	-0.5	1.7
Denmark	1.3	1.0	0.8	1.4
Estonia	2.3	7.6	2.2	3.6
Finland	3.7	2.9	0.9	2.0
France	1.6	1.7	0.6	1.2
Germany	3.6	3.1	1.2	2.0
Greece	-3.5	-6.9	-5.3	-1.3
Hungary	1.2	1.7	-1.5	1.1
Ireland	-0.4	0.7	0.6	2.1
Iceland	-4.0	3.1	3.1	2.7
Israel	4.8	4.8	3.2	3.6
Italy	1.8	0.5	-1.7	-0.4
Japan	4.5	-0.7	2.0	1.5
Korea	6.3	3.6	3.3	4.0
Luxembourg	2.7	1.6	0.6	2.2
Mexico	5.5	4.0	3.6	3.8
Netherlands	1.6	1.3	-0.6	0.7
Norway	0.7	1.6	2.3	2.6
New Zealand	2.4	1.3	1.9	2.8
Poland	3.9	4.4	2.9	2.9
Portugal	1.4	-1.6	-3.2	-0.9
Slovak Republic	4.2	3.3	2.6	3.0
Slovenia	1.4	-0.2	-2.0	-0.4
Spain	-0.1	0.7	-1.6	-0.8
Sweden	5.8	4.0	0.6	2.8
Switzerland	2.7	1.9	0.9	1.9
Turkey	9.2	8.5	3.3	4.6
United Kingdom	2.1	0.7	0.5	1.9
United States	3.0	1.7	2.4	2.6
Brazil	7.6	2.7	3.2	4.2
China	10.4	9.2	8.2	9.3
India	10.6	7.3	7.1	7.7
Indonesia	6.2	6.5	5.8	6.0
Russian Federation	4.3	4.3	4.5	4.1
South Africa	2.9	3.1	3.3	4.2

Source: OECD Economic Outlook 91 database.

EDITORIAL

Confidence, recovery, and the euro: Is it different this time?

The global economy is, once again, trying to return to growth, helped by a modest pick-up of trade and an improvement in confidence. It is doing so, however, at different speeds, with the United States and Japan growing at a stronger pace than the euro area and large emerging economies enjoying a moderate cyclical upswing. Different dynamics are also developing in labour markets in the United States, where unemployment is slowly decreasing, and in the euro area, where instead it keeps rising

In the *United States*, growth should continue to strengthen as confidence is picking up in both businesses and households. Financial markets are firming, and household deleveraging is well underway, which should allow saving rates to ease. More generally, growth seems to be increasingly driven by private-sector demand rather than by policy. Fiscal consolidation is dragging growth, but only at a moderate pace. However, the risk of excessive fiscal tightening in 2013 remains to be addressed, failing which, growth would be severely affected. Looking forward, long-term fiscal sustainability remains to be achieved, and a credible fiscal plan is needed to ensure it. Given the still weak recovery and sluggish job creation, monetary policy should remain accommodative, but conditional upon activity developments.

In *Japan*, the very high sovereign debt requires the establishment of a more detailed and credible consolidation programme to put debt firmly on a downward path, and structural reforms are needed to boost growth.

In most *emerging economies*, activity remains strong, but policy challenges are different across countries as inflation acts as a drag on real incomes in some, while it remains subdued in others. Where available, lower inflation provides policy space that could be used to sustain activity. In many emerging countries there are renewed risks of asset price bubbles, also related to capital inflows. Prudential and fiscal policies should deal with such risks.

More generally, while international financial integration enhances efficiency and boosts growth, it may increase financial fragility. OECD research shows that very limited progress has been achieved since 2007 in making the structure of external financial accounts more robust, and this could be a source of adverse risk going forward.

Global imbalances are likely to remain at current levels for some time, but with important changes in geographical composition. Oil producers' surpluses are increasing, while surpluses in Japan and China are slightly declining, reflecting, especially in the latter case, a welcome strengthening of domestic demand.

After some retrenchment at the end of last year, the crisis in the *euro area* has become more serious recently, and it remains the most important source of risk to the global economy. Confidence remains weak or is even declining, financial markets are again volatile, and deleveraging has barely begun. Fiscal drag on growth from consolidation may be significant, especially in some countries.

Such persistent weakness reflects underlying economic, fiscal, and financial imbalances within the euro area, which have been the root cause of the crisis, and have barely begun to unwind. Recovery in healthier countries, while welcome, is not strong enough to offset flat or negative growth elsewhere. Weak competitiveness must be addressed in deficit countries, while structural adjustment and higher wages in surplus countries would contribute to a growth-friendly rebalancing process. Adjustment is underway; however, it is taking place in an environment of slow or negative growth and deleveraging.

Against this background the risk is increasing of a vicious circle, involving high and rising sovereign indebtedness, weak banking systems, excessive fiscal consolidation and lower growth.

Recent events have further increased downside risks. Elections in a number of euro area countries have signalled that reform fatigue is increasing and tolerance for fiscal adjustment may be reaching a limit. With the expectation of euro area with no growth in 2012, but with recession in a number of countries in 2012 and 2013, a combination of enduring financial fragility, rising unemployment and social pain may spark political contagion and adverse market reaction. Dramatic developments in individual countries would accelerate the process. A downside scenario, like the one described in the previous *Economic Outlook*, may materialise and spill over outside the euro area with very serious consequences for the global economy. Avoiding such a scenario requires action to be taken both at country and supranational level.

Fiscal consolidation and structural measures must proceed hand in hand to make the process as growth-friendly as possible. The composition of fiscal consolidation, with a careful balance between spending cuts and revenue increases, is critically important. In addition, much can be gained in efficiency of public spending and through a composition of taxation that is least harmful to growth. Importantly, the reform agenda must be targeted at supporting employment through both labour and product market reforms. Last but not least, resources should be devoted to support the weakest segments of the population and mitigate the pressure of consolidation.

While trying to improve the quality of fiscal consolidation is of the essence, the speed of consolidation should depend on country-specific circumstances. While for some countries there is no alternative but for consolidation to keep its course, for others there is scope for easing the pace. In general, should unforeseen circumstances lead to a further slowdown in activity, the additional structural consolidation needed to attain deficit goals should be implemented only partially.

Credible medium-term consolidation programmes are a key prerequisite for successful adjustment. However, in the current circumstances, when several countries are undergoing fiscal tightening, credibility and confidence would be enhanced by euro area and EU-wide measures.

In this respect much progress has been achieved in recent months. The euro area firewall has been enhanced. IMF resources have been increased, and the LTROs activated by the ECB have injected confidence. However, the effectiveness of the firewall can be further enhanced, for instance by allowing ESM resources to be used directly to meet bank recapitalisation needs. Also, the operational conditions of firewall resources should be improved to provide quick deployment if needed. Were instability and volatility in sovereign markets to increase, the ECB should resume and expand its SMP. Last but not least, given declining inflationary pressures, there is room for further monetary easing.

The "fiscal compact" has introduced a stronger framework for fiscal discipline. It could be further improved to allow for more selective assessment of spending items in computing debt reduction obligations. In the new regime, a number of fiscal rules will be in force at the same time, so it will be important to ensure transparency in the communication of the fiscal position to avoid unjustified market reactions to inaccurate interpretation of the adjustment efforts. Ultimately, it is important to implement the new framework in a balanced way, ensuring that remaining discretion is used only if appropriate.

Firm fiscal discipline and successful consolidation provide the background conditions for additional measures towards the establishment of a "growth compact". Such measures could include: i) issuance of new jointly guaranteed government bonds to help recapitalise banks and enhance credit availability; ii) increasing jointly guaranteed resources available for the European Investment Bank to fund infrastructure projects; iii) such moves could pave the way to a broader issuance of euro-bonds; iv) redirecting available structural fund resources toward more growth enhancing allocations; and v) a decisive acceleration of single market integration promises to be a major source of growth.

Such set of EU-wide measures would strengthen activity, both directly and indirectly, by boosting confidence and making it easier to achieve the intra euro area rebalancing effort. At national level deficit countries should enhance competitiveness by improving the functioning of their labour and product markets, and surplus countries could enhance investment through liberalisation measures notably in the service sectors. A further boost to confidence could be obtained if euro area countries were to announce and commit to implement such reforms in a coordinated and parallel fashion, signalling enhanced coordination. Higher nominal wages in surplus countries, while boosting domestic demand, could contribute to a less painful readjustment in deficit countries where wage deflation adds to the pressure of increasing unemployment.

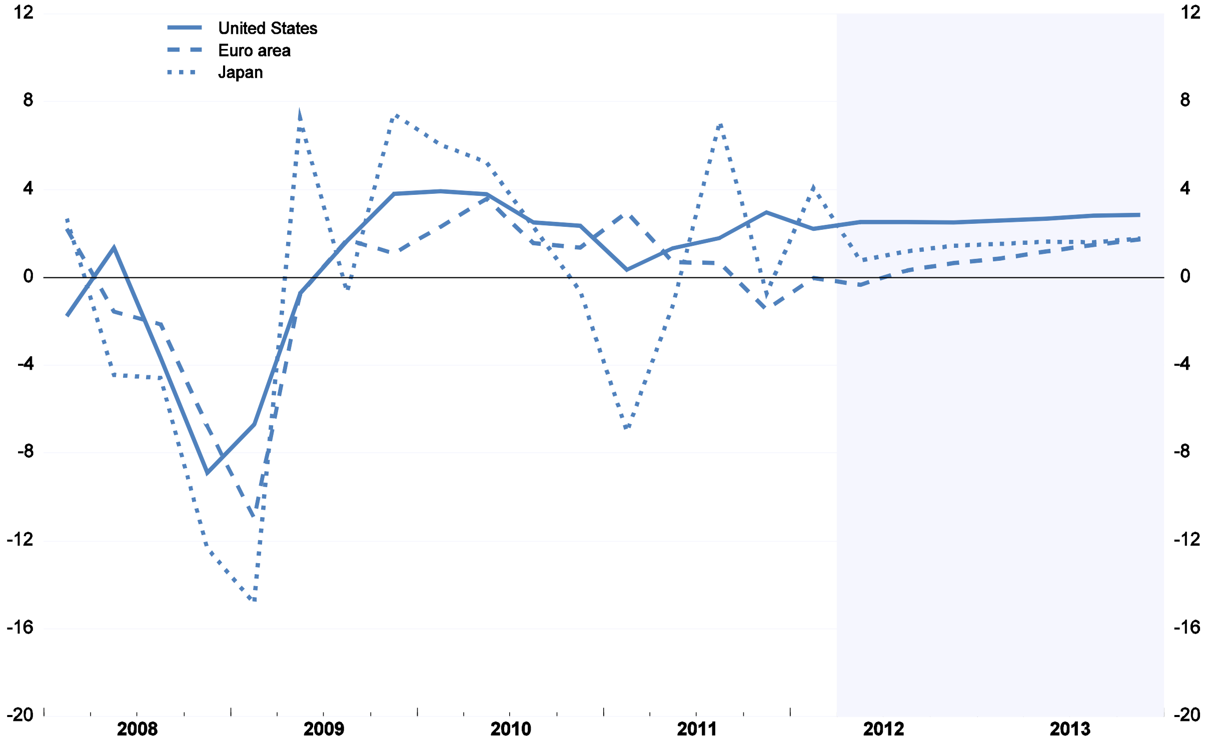
Almost five years ago, in the summer of 2007, turbulence in the US subprime market sparked off the most dramatic financial and economic crisis in several decades. After five years we cannot yet say that the crisis is behind us. More than once signs of recovery have disappointed. Policy mistakes have been made, sometimes reflecting inaccurate reading of events, at other times reflecting policy and political failures. Is it different this time? As long as confidence is not rebuilt on a solid basis with the right policy choices, downside risks will prevail. This is important everywhere but particularly so in the euro area, where crisis management goes hand in hand with the building of the institutions needed for a monetary union to work properly.

22 May 2012

Pier Carlo Padoan
Deputy Secretary-General and Chief Economist

The outlook for growth is different across regions

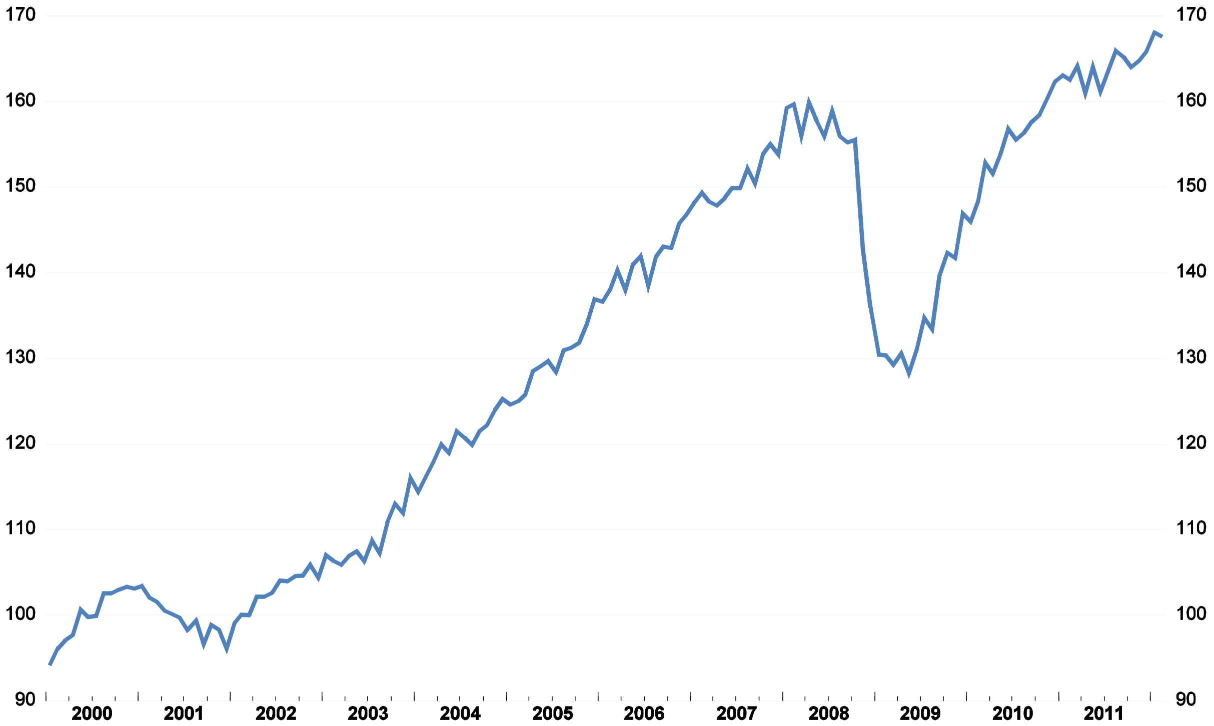
Annualised quarter-on-quarter real GDP growth, in per cent



Source: OECD Economic Outlook 91 database.

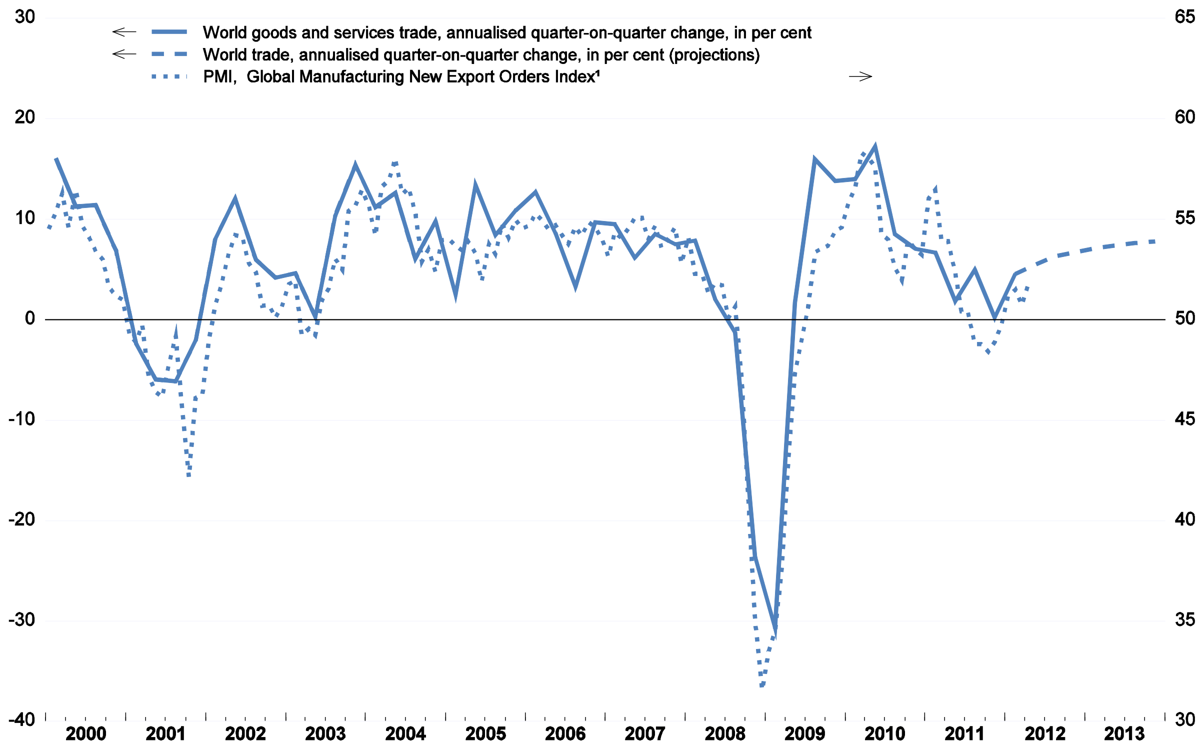
World trade growth is picking up moderately

CPB indicator of world merchandise trade, 2000 = 100



Source: CPB.

World goods and services trade and Global Manufacturing New Export Orders Index

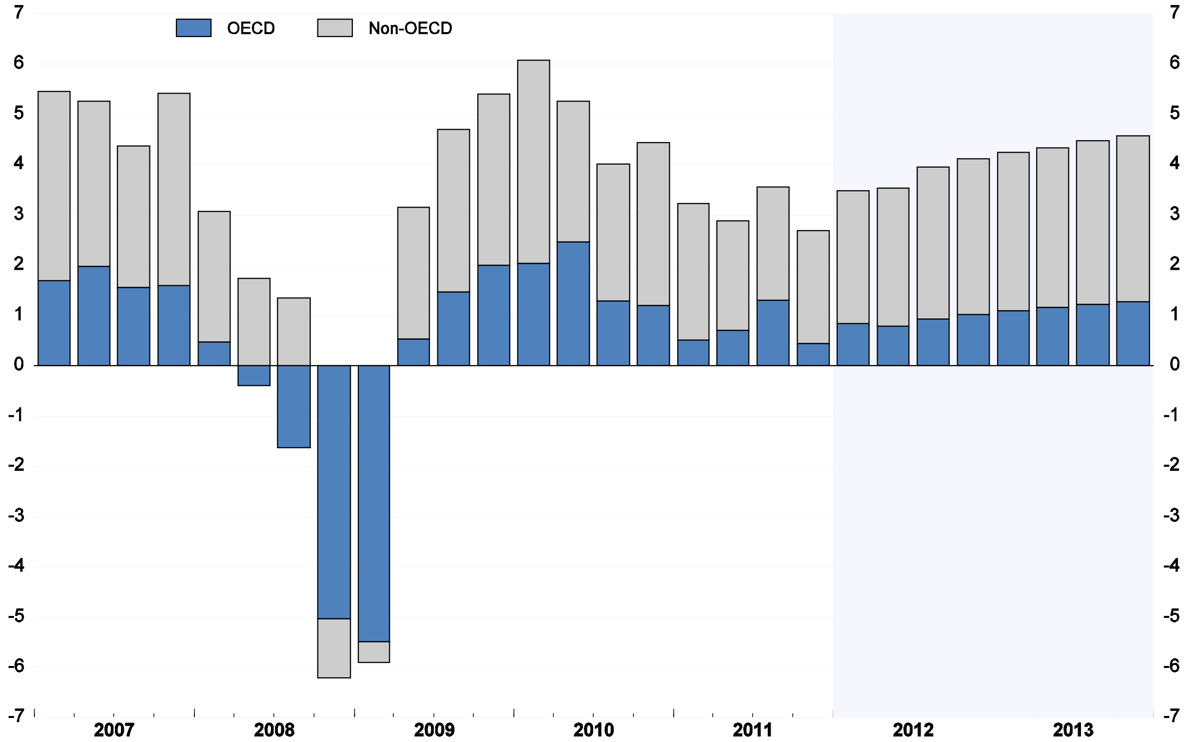


1. Values greater than 50 signify an increase in new export orders.

Source: OECD Economic Outlook 91 database; and Markit Economics Limited.

World growth will continue to be sustained by emerging economies

Contribution to annualised quarterly world real GDP growth, percentage points

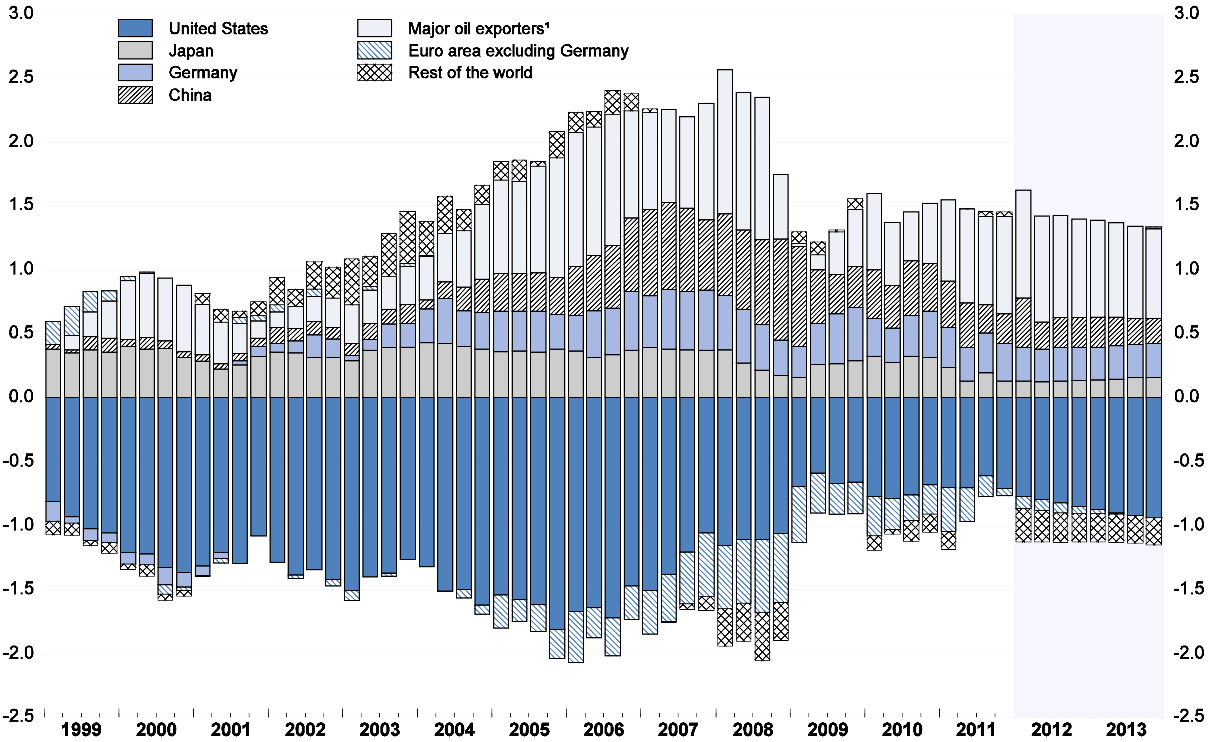


Note: Calculated using moving nominal GDP weights, based on national GDP at purchasing power parities.

Source: OECD Economic Outlook 91 database.

Current account imbalances remain pronounced

Current account balance, in per cent of world GDP

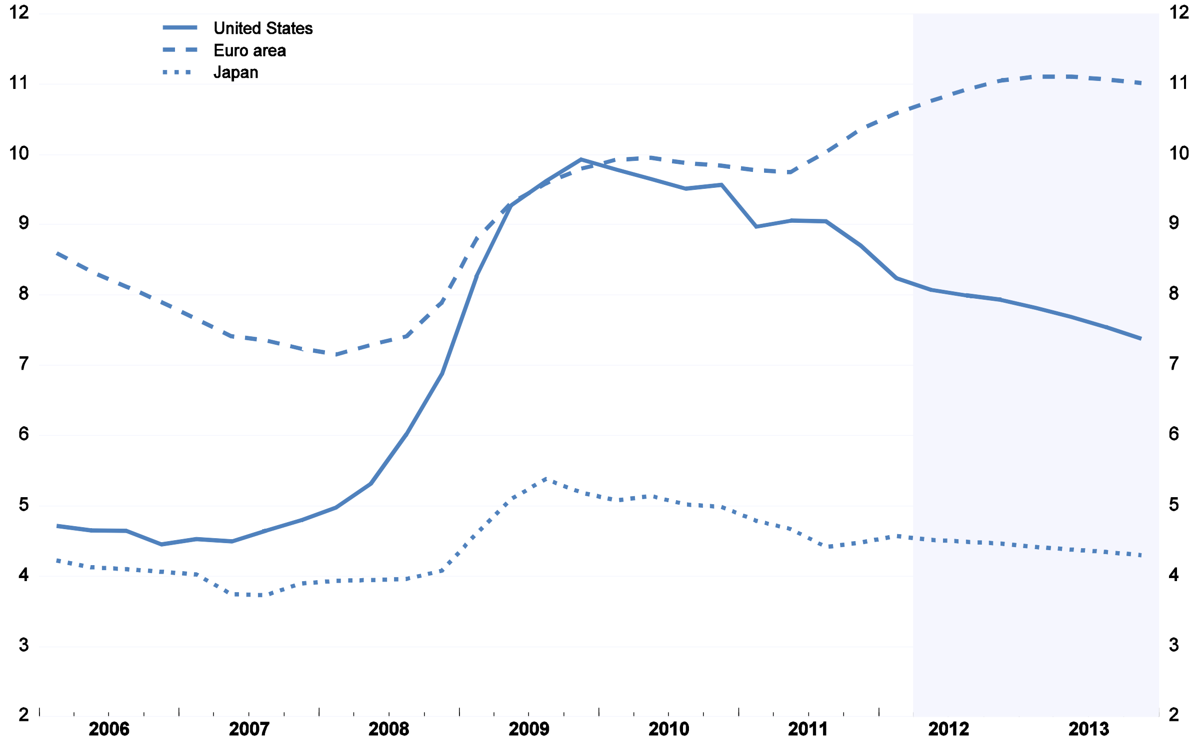


1. Includes Azerbaijan, Kazakhstan, Turkmenistan, Brunei, Timor-Leste, Bahrain, Iran, Iraq, Kuwait, Libya, Oman, Qatar, Russian Federation, Saudi Arabia, United Arab Emirates, Yemen, Ecuador, Trinidad and Tobago, Venezuela, Algeria, Angola, Chad, Republic of Congo, Equatorial Guinea, Gabon, Nigeria and Sudan.

Source: OECD Economic Outlook 91 database.

Unemployment rates are diverging

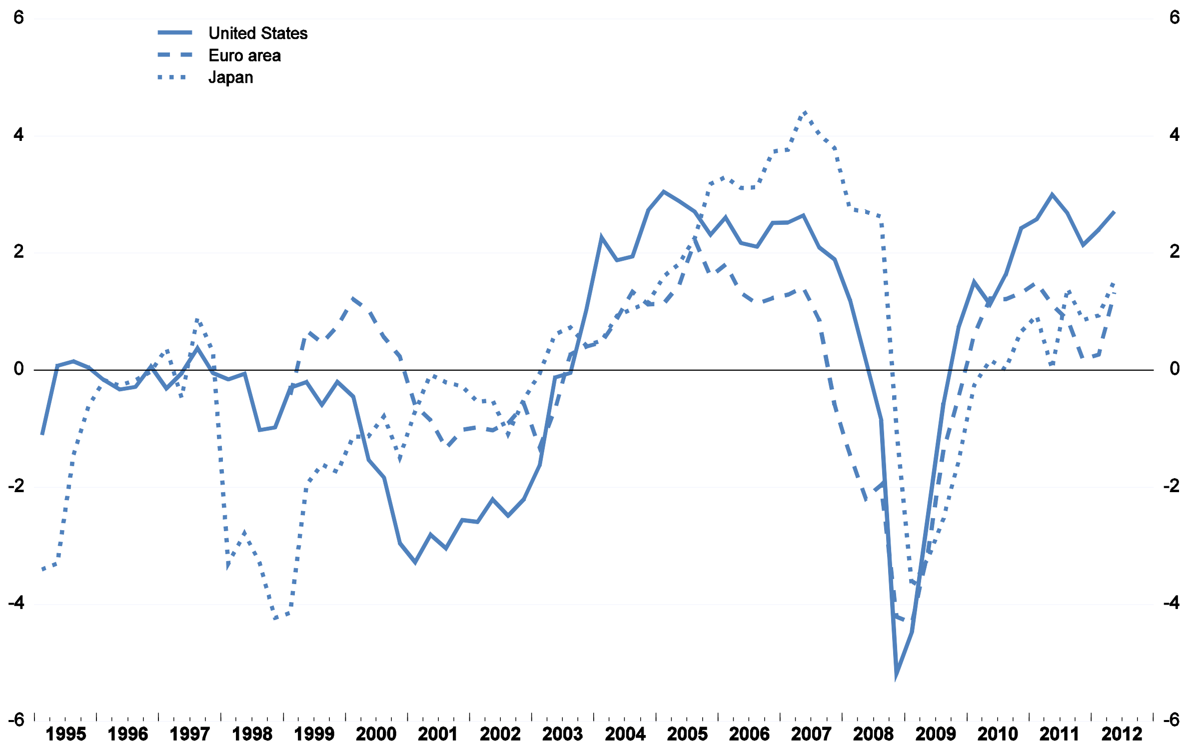
Unemployment rate, percentage of labour force



Source: OECD Economic Outlook 91 database.

Financial conditions are supportive

OECD Financial Conditions Index

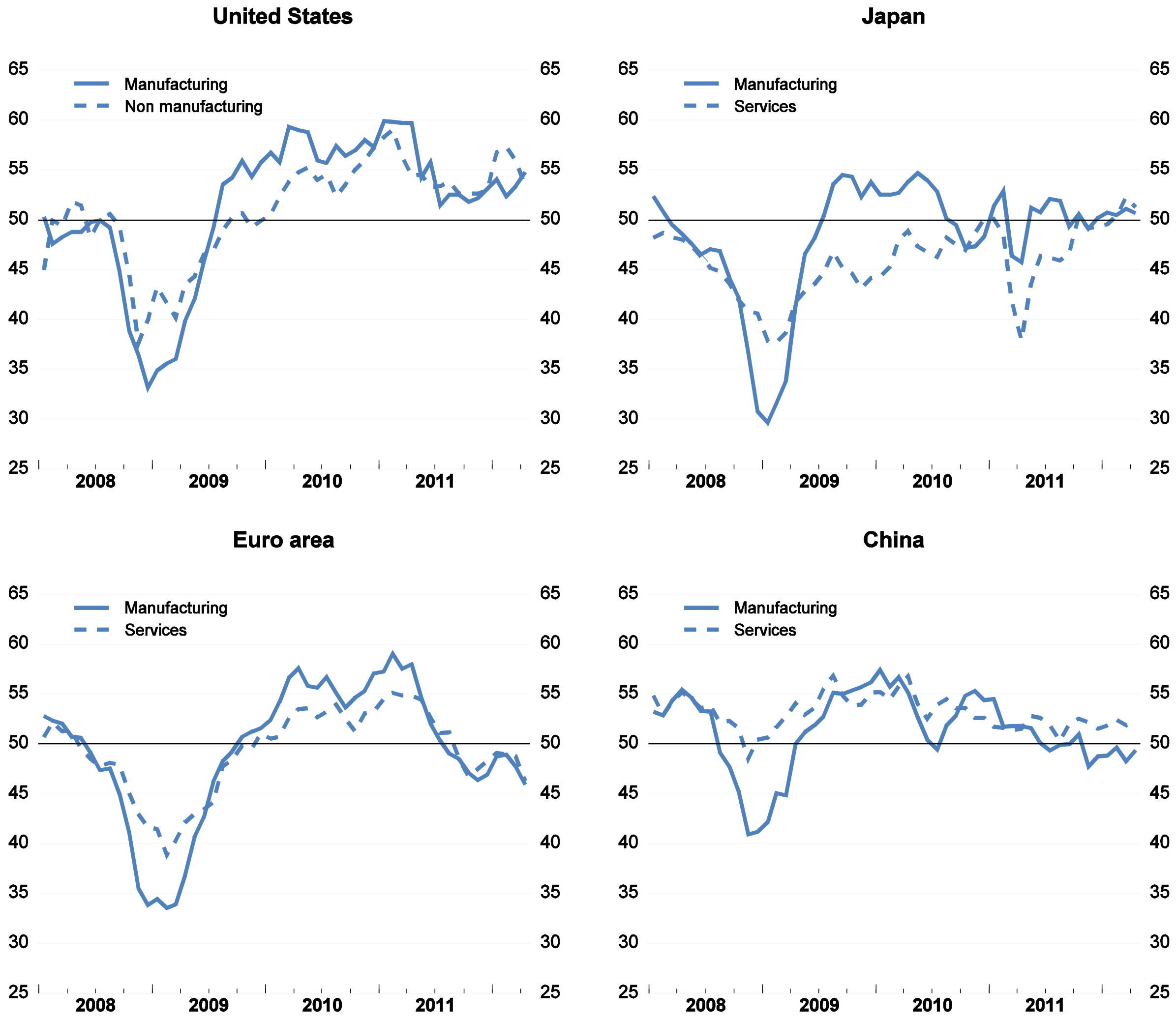


Note: A unit increase (decline) in the index implies an easing (tightening) in financial conditions sufficient to produce an average increase (reduction) in the level of GDP of ½ to 1% after four to six quarters. See details in Guichard et al. (2009). The estimation is done with available information up to 15 May 2012.

Source: Datastream; OECD Economic Outlook 91 database; and OECD calculations.

Business confidence is deteriorating further in the euro area

Purchasing Managers Index (PMI) for manufacturing and services

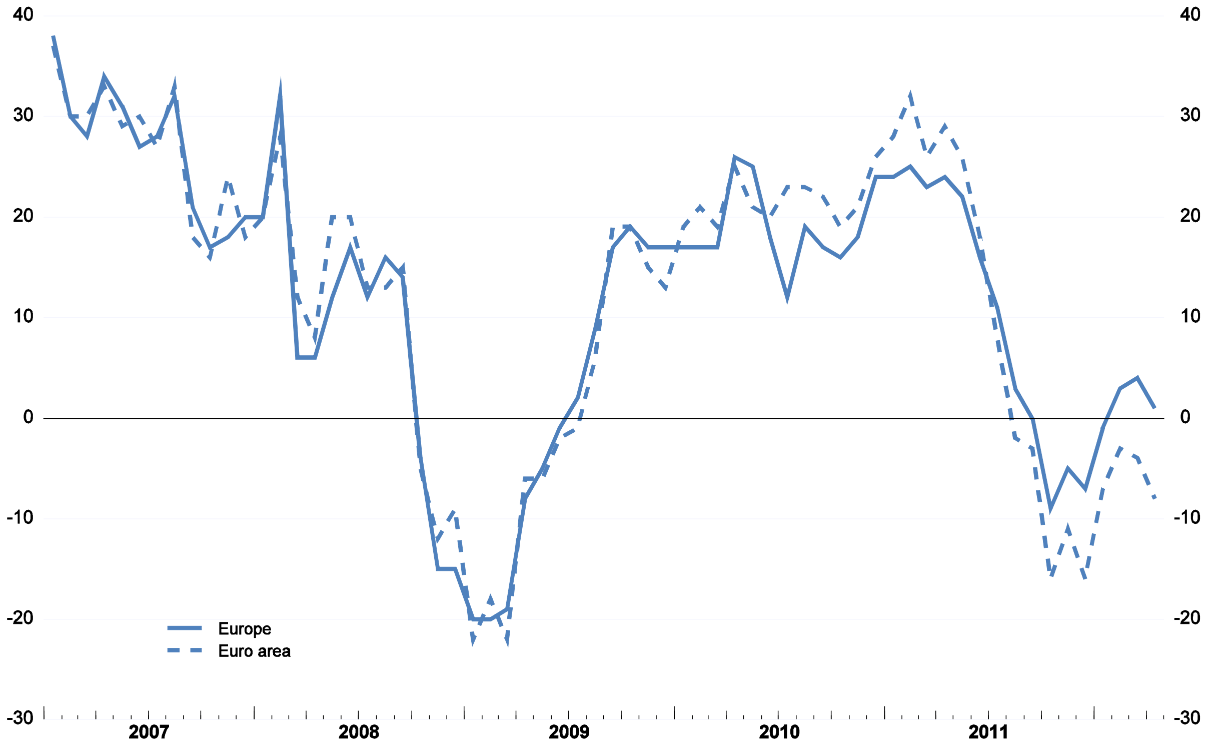


Note: Values greater than 50 signify an improvement in economic activity.

Source: Markit Economics Limited.

Euro area financial sector confidence is weakening again

Financial services confidence indicator, balances, in percentage points

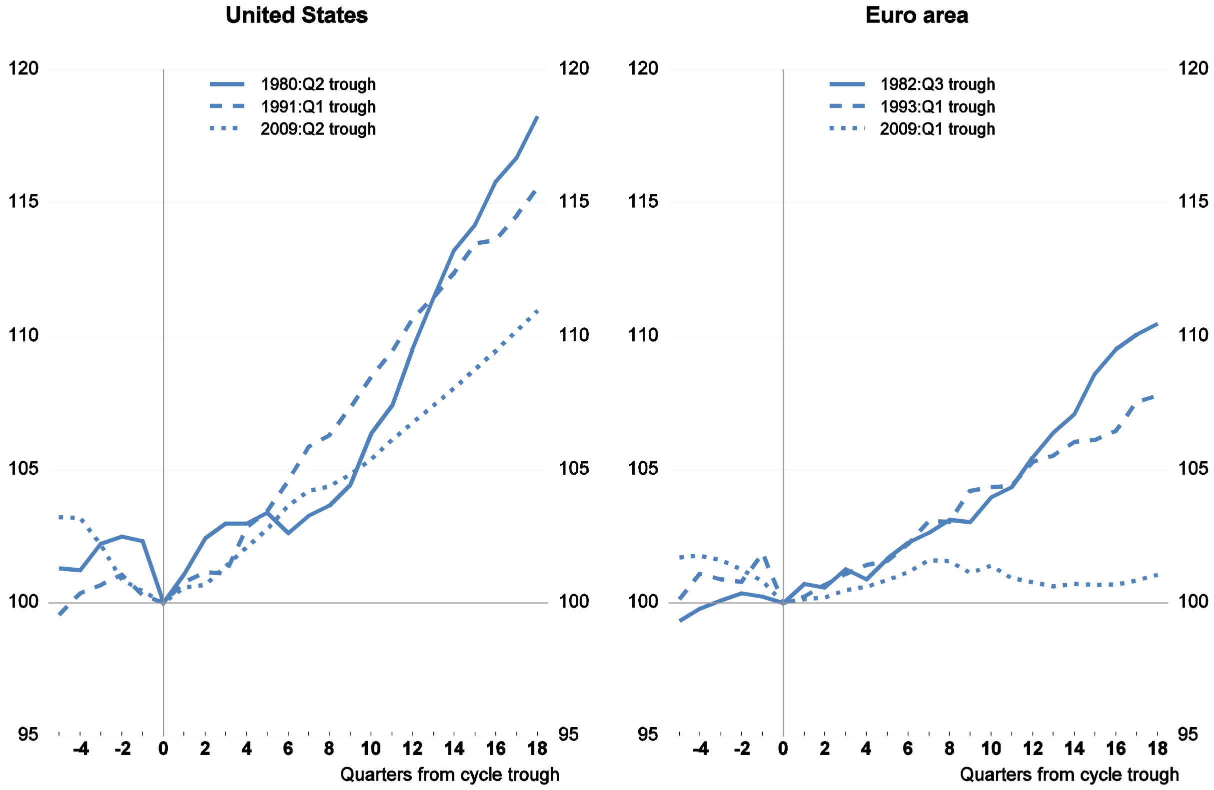


Note: The confidence indicator is the arithmetic average of the balances (in percentage points) for the questions on business conditions, and past and expected evolution of demand. Balances are differences between the percentages of respondents giving positive and negative replies. Data are not seasonally adjusted. Europe includes Czech Republic, Germany, Spain, France, Italy, Luxembourg, Hungary, the Netherlands, Poland and the UK. Euro area includes Germany, Spain, France, Italy, Luxembourg, and the Netherlands.

Source: European Commission, Business and consumer survey results.

Private consumption has stagnated in the euro area

Private consumption volumes, index = 100 at cycle troughs

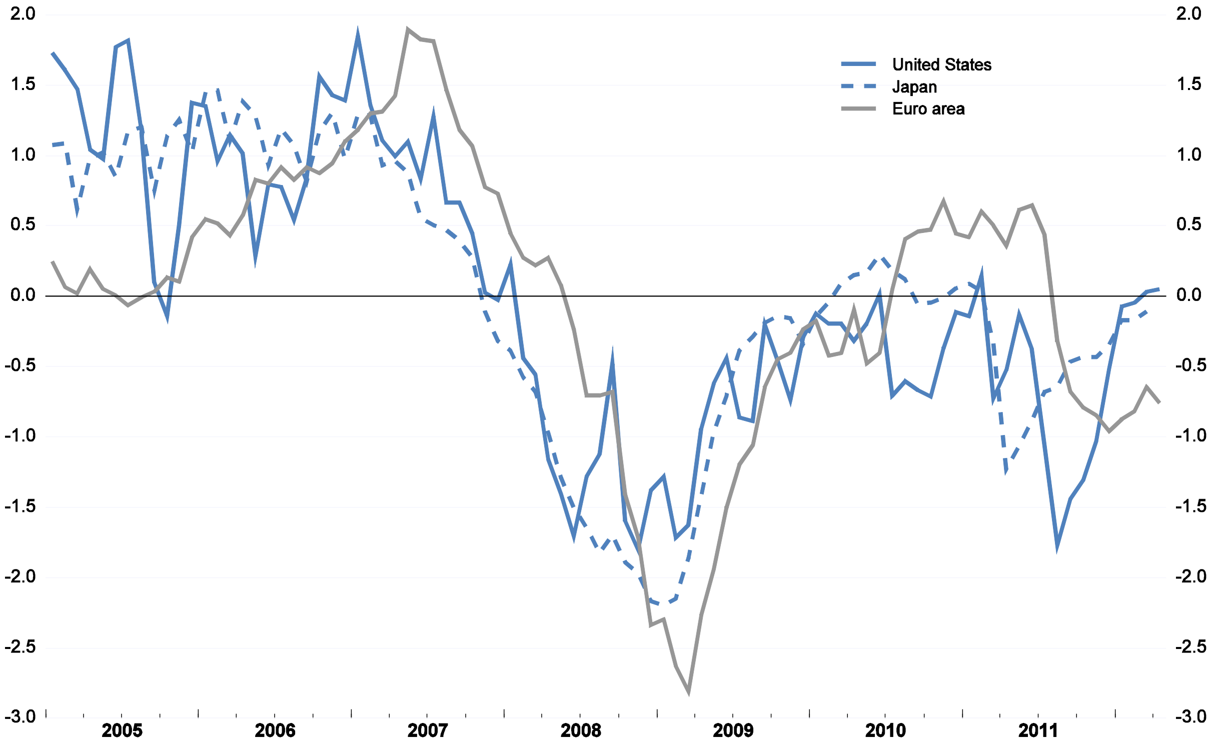


Note: Private consumption volumes are indexed to 100 in the quarter in which they reached the lowest level during the last three recessions. Zero on the horizontal axis corresponds to the quarter of these troughs.

Source: OECD Economic Outlook 91 database.

Consumer confidence is firming in the United States

Consumer confidence survey indicators, standard deviations

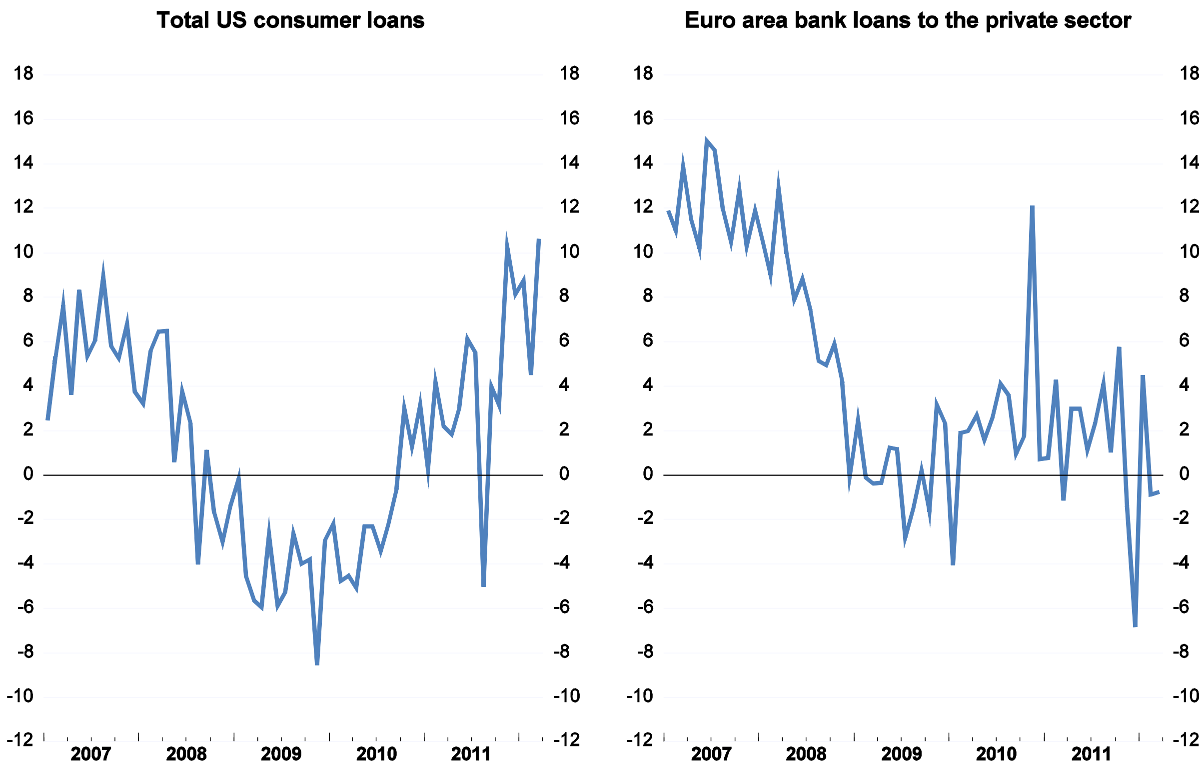


Note: Normalised at period average and presented in units of standard deviation. Values above zero signify levels of consumer confidence above the period average.

Source: OECD Main Economic Indicators.

Consumer lending is growing robustly in the United States but contracting in the euro area

High-frequency lending indicators, annualised monthly percentage change

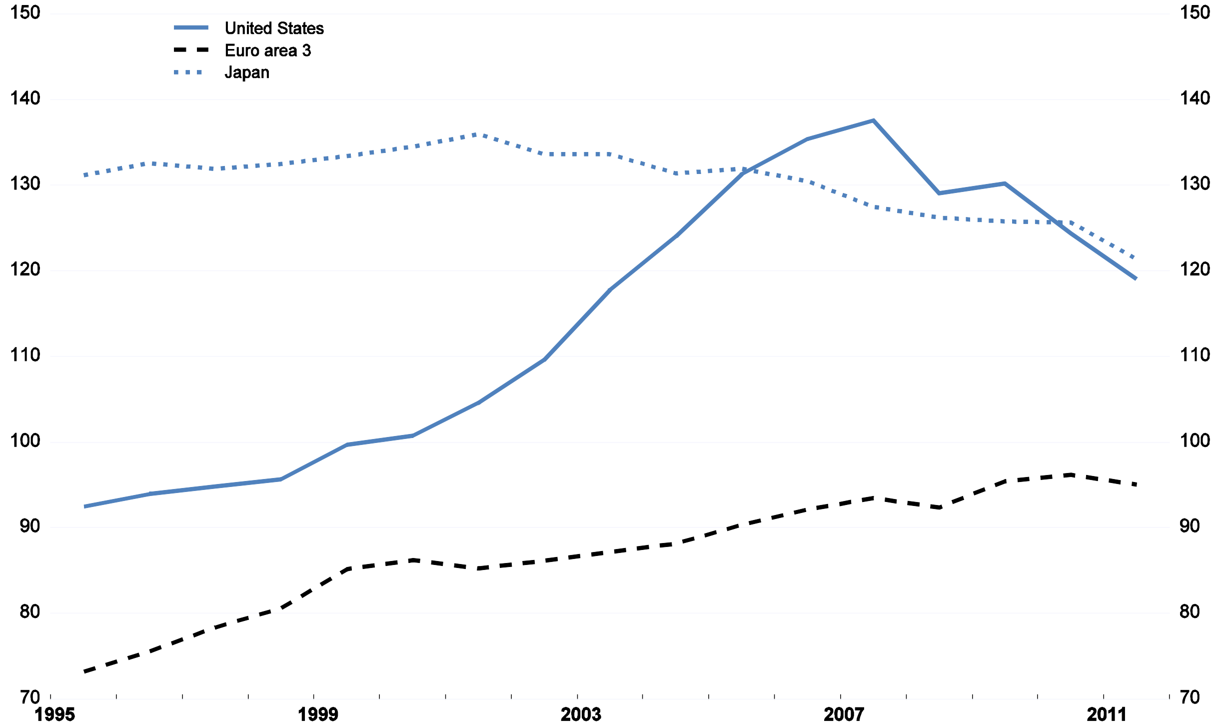


Note: Annualised monthly rate of change of seasonally adjusted stocks, in per cent. Euro area data are adjusted for the impact of securitisation. Last observation: March 2012

Source: Datastream; and ECB.

Deleveraging is barely starting in the euro area

Household gross debt, in per cent of net disposable income

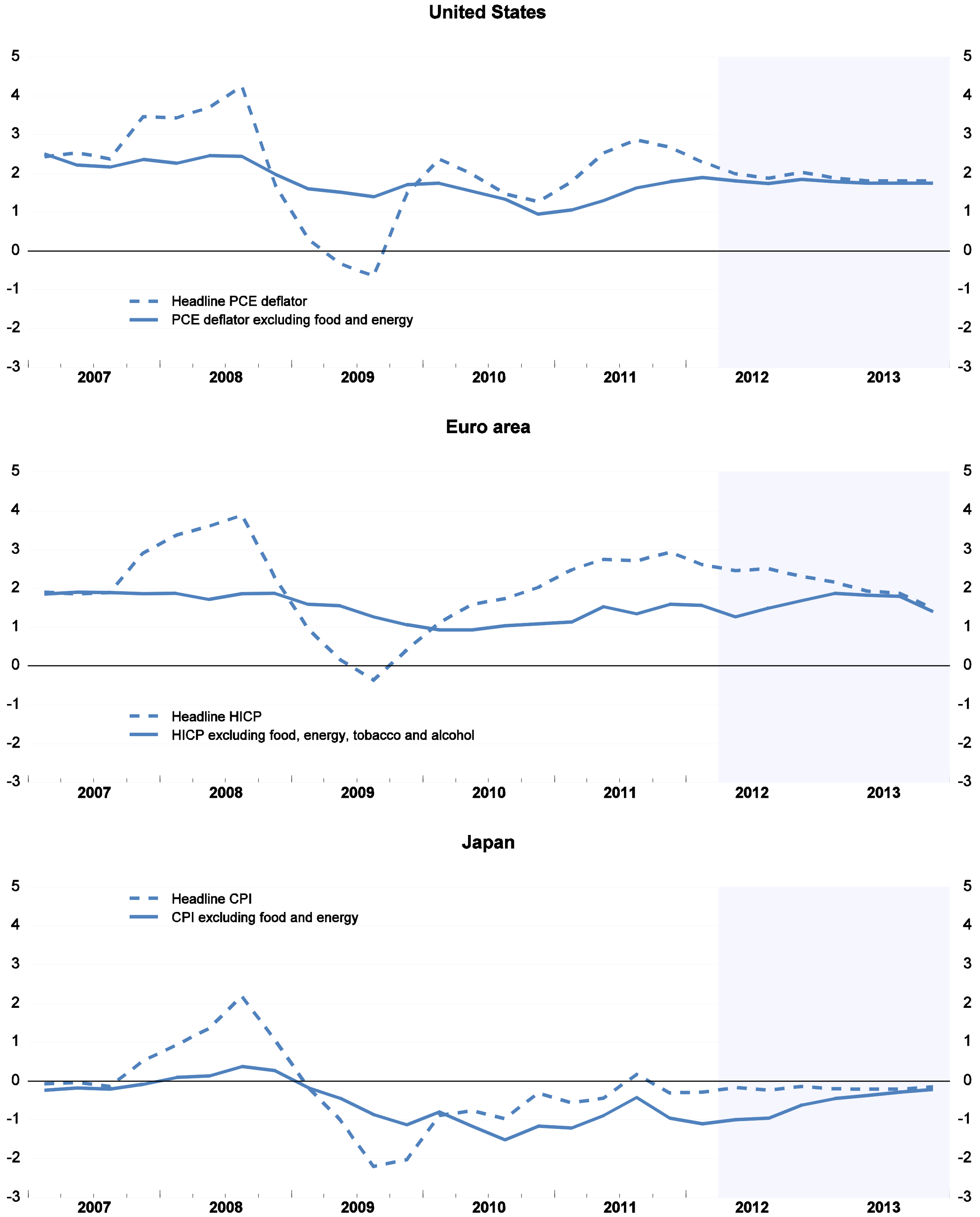


Note: Data for USA and Japan are not consolidated. For 2011 Q3 data are growth rates (2010 end of year to 2011 Q3) of balance sheets published by US Federal Reserve, Bank of Japan, and ECB. Euro area 3 is Germany, France and Italy.

Source: OECD Annual National Accounts.

Underlying inflation is likely to remain moderate

Headline and core inflation, 4-quarter percentage change

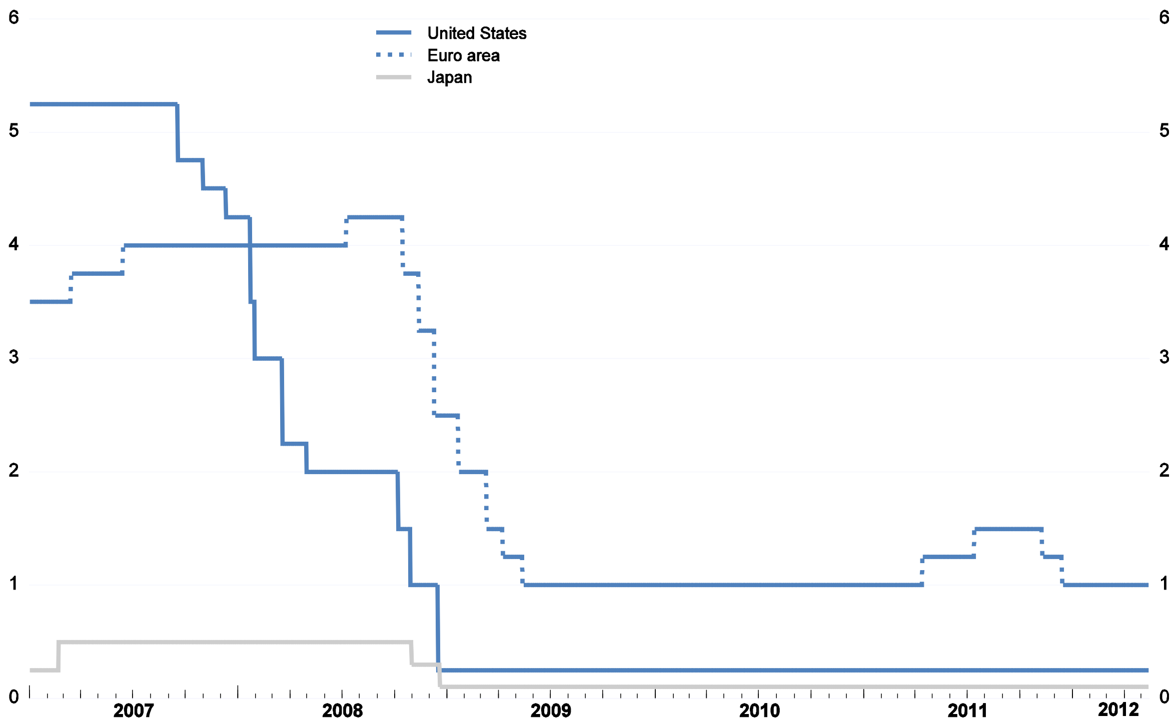


Note: PCE deflator refers to the deflator of personal consumption expenditures, HICP to the harmonised index of consumer prices and CPI to the consumer price index.

Source: OECD Economic Outlook 91 database.

Monetary policy rates remain extremely accommodative

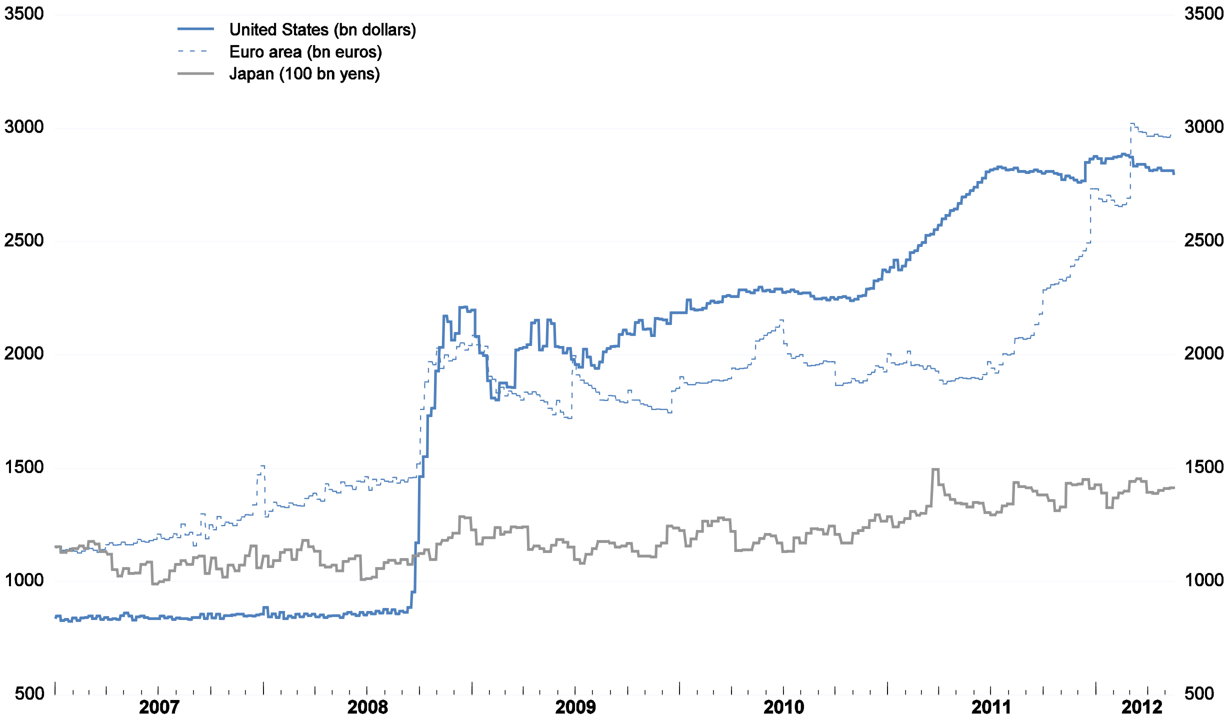
Policy interest rates, in per cent



Source: Datastream.

Central bank balance sheets reflect vigorous asset purchase programmes

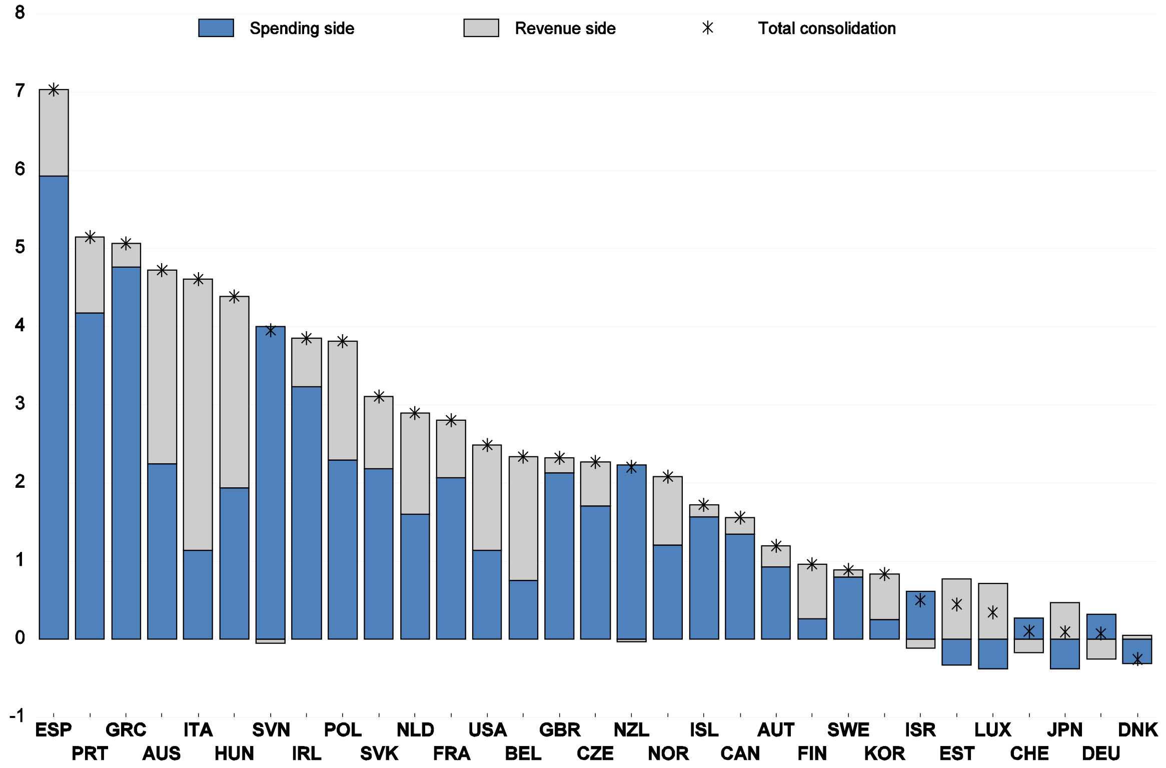
Central bank liabilities, local currency



Source: Federal Reserve; Bank of Japan; and European Central Bank.

Fiscal consolidation plans combine spending reductions and tax increases

Change in the underlying primary balance 2011-13, in per cent of potential GDP

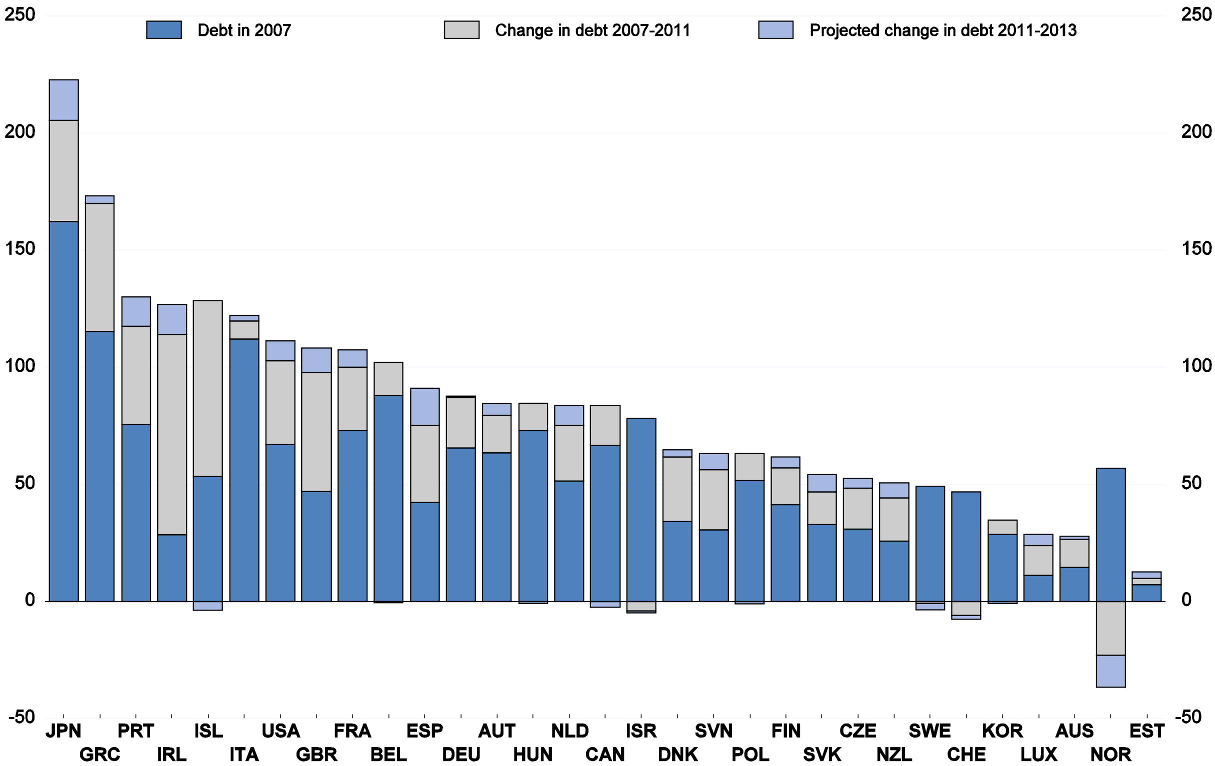


Note: Total consolidation is the projected difference in the underlying primary balance; revenue side is the projected increase in the underlying receipts excluding interest earned on financial assets; and spending side is the projected decline in the underlying primary spending excluding interest payments on debt.

Source: OECD Economic Outlook 91 database; and OECD calculations.

Government debt accumulation is slowing on the back of consolidation efforts

Government gross financial liabilities, per cent of GDP

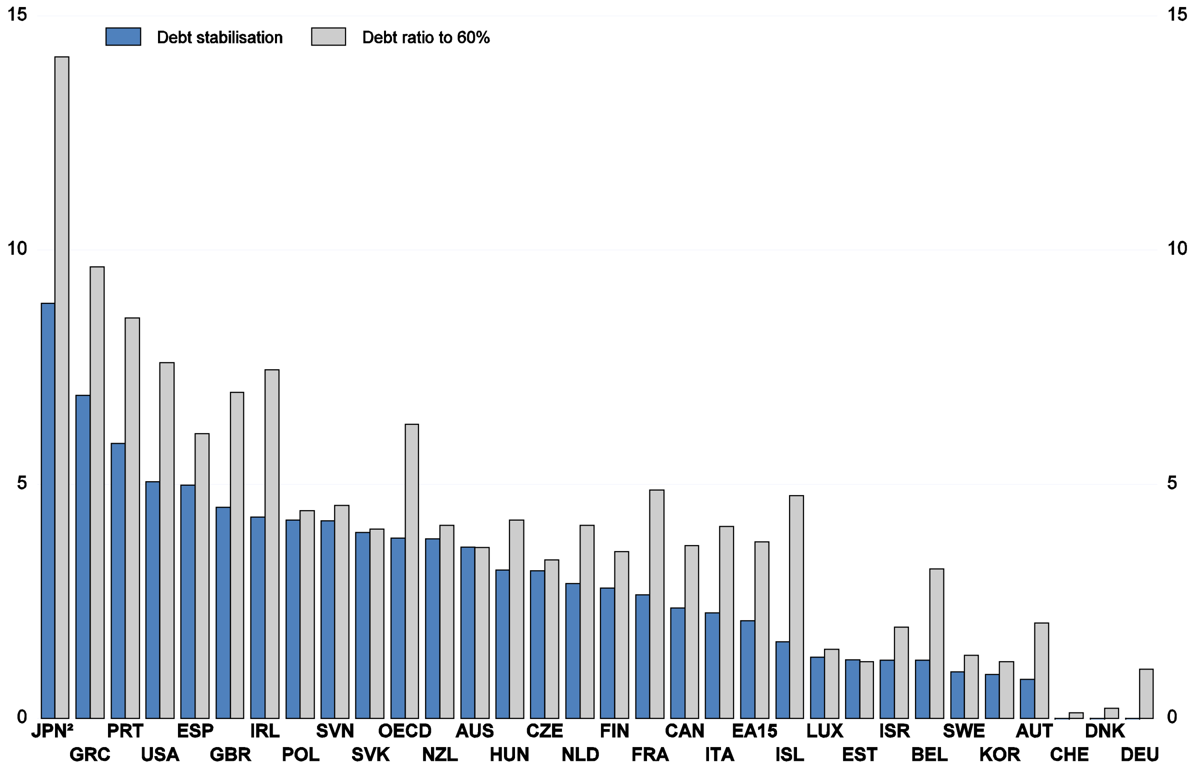


Note: Change in debt includes cumulated deficit for 2007-11 and 2011-13, debt-increasing equity participations in companies and the impact of GDP growth. For Norway cumulated deficits correspond to mainland only.

Source: OECD Economic Outlook 91 database.

Government debt sustainability remains a long-term challenge in many countries

Average increase in the underlying primary balance from 2011 to 2030, in percentage points of GDP[1]

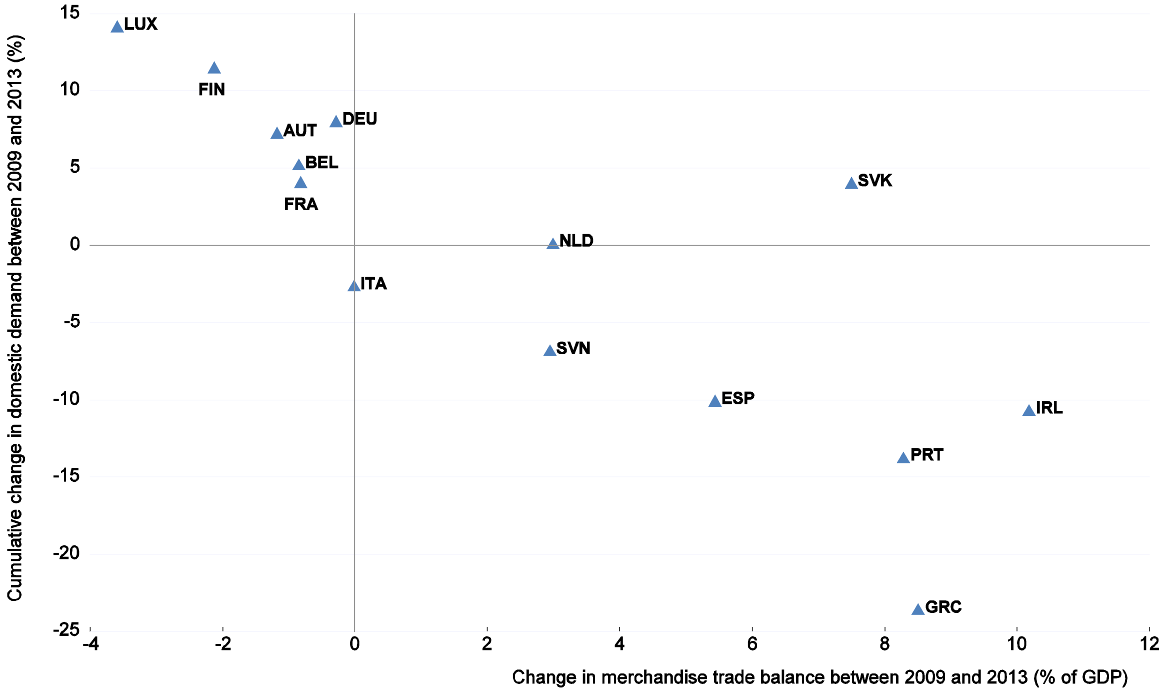


1. The bars show the average improvement in the underlying primary balance between 2011 and 2030 necessary to either stabilise government debt ratios or bring them down to 60% of GDP. When simply stabilising debt ratios, the average increase in the underlying primary balance over this period corresponds closely to the peak increase over the same period. When targeting 60%, however, the peak increase will be substantially higher than the average increase, but past the peak fiscal policy can be loosened and the underlying primary balance decrease before the debt ratio stabilises at 60% of GDP. In some cases the debt target is reached only after 2030.
2. In Japan's case, the average consolidation shown would be sufficient to stabilise the debt ratio but only after 2030.

Source: OECD Economic Outlook 91 long-term database.

Rebalancing in the euro area is underway

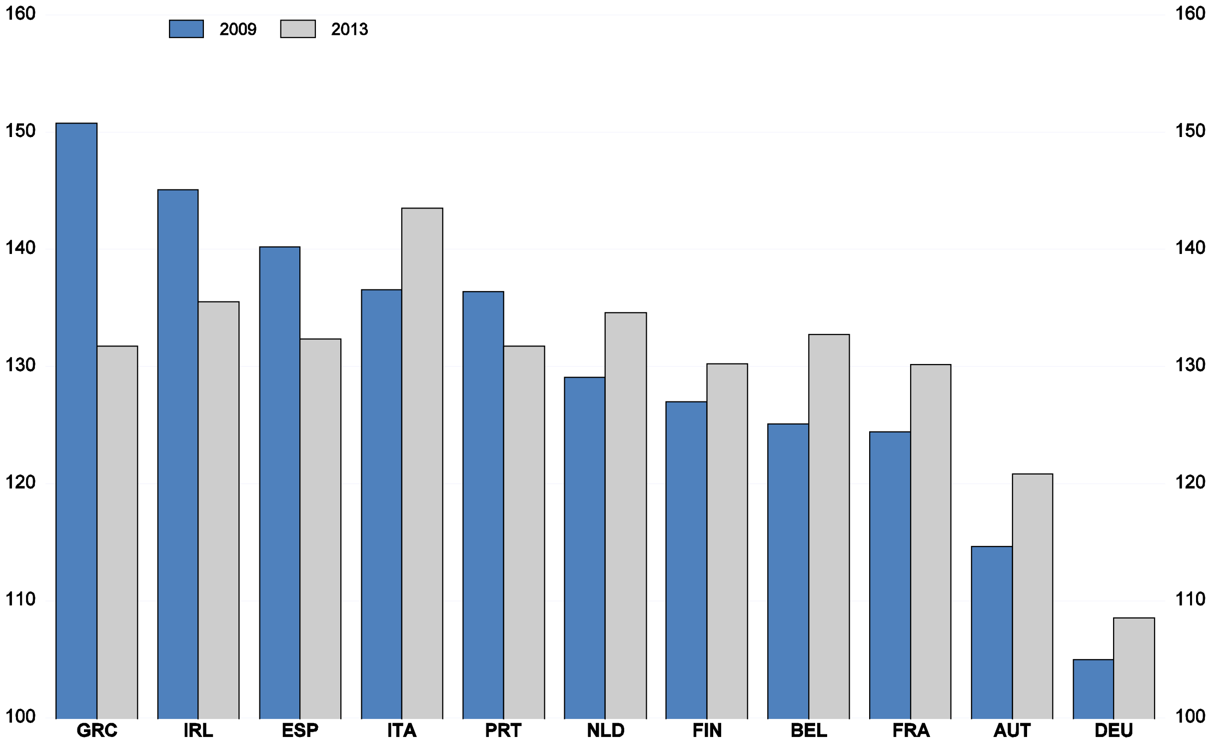
Changes in domestic demand and trade balances, 2009-13



Source: OECD Economic Outlook 91 database.

Unit labour costs have begun to adjust in the euro area

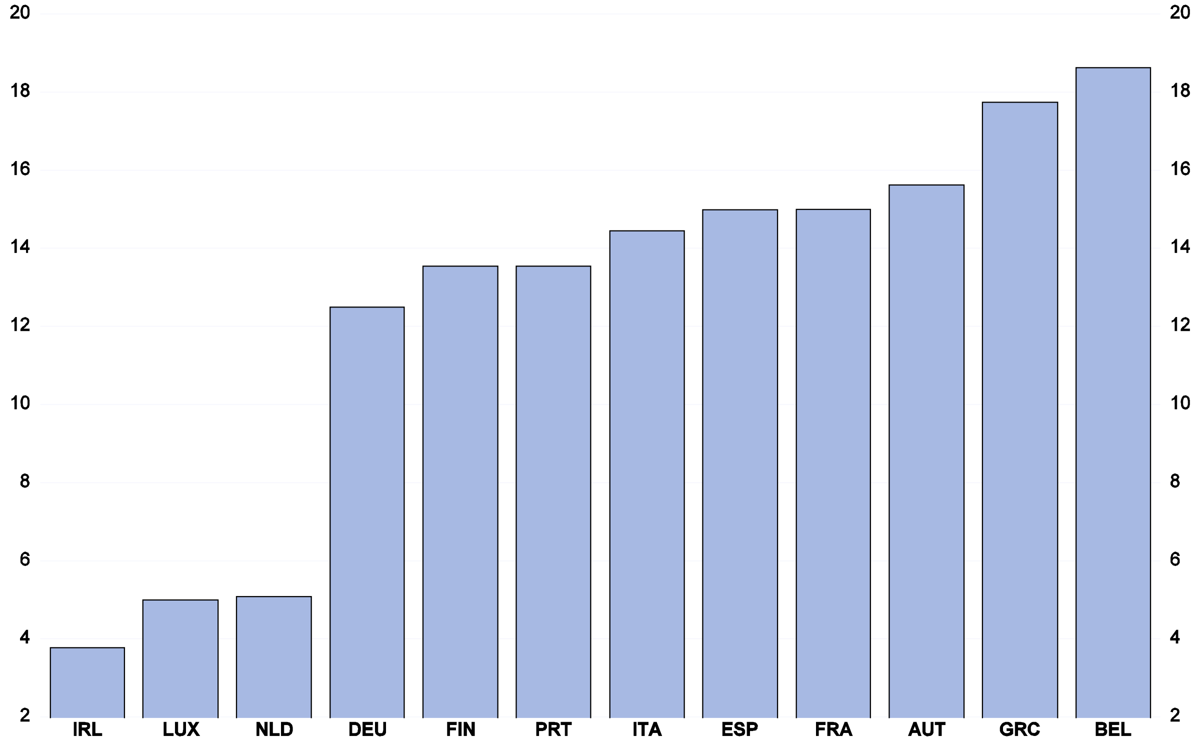
Unit labour cost, 1999 = 100



Source: OECD Economic Outlook 91 database.

Large potential gains from a broad package of reforms

Overall GDP per capita gains over 10-year horizon, in per cent

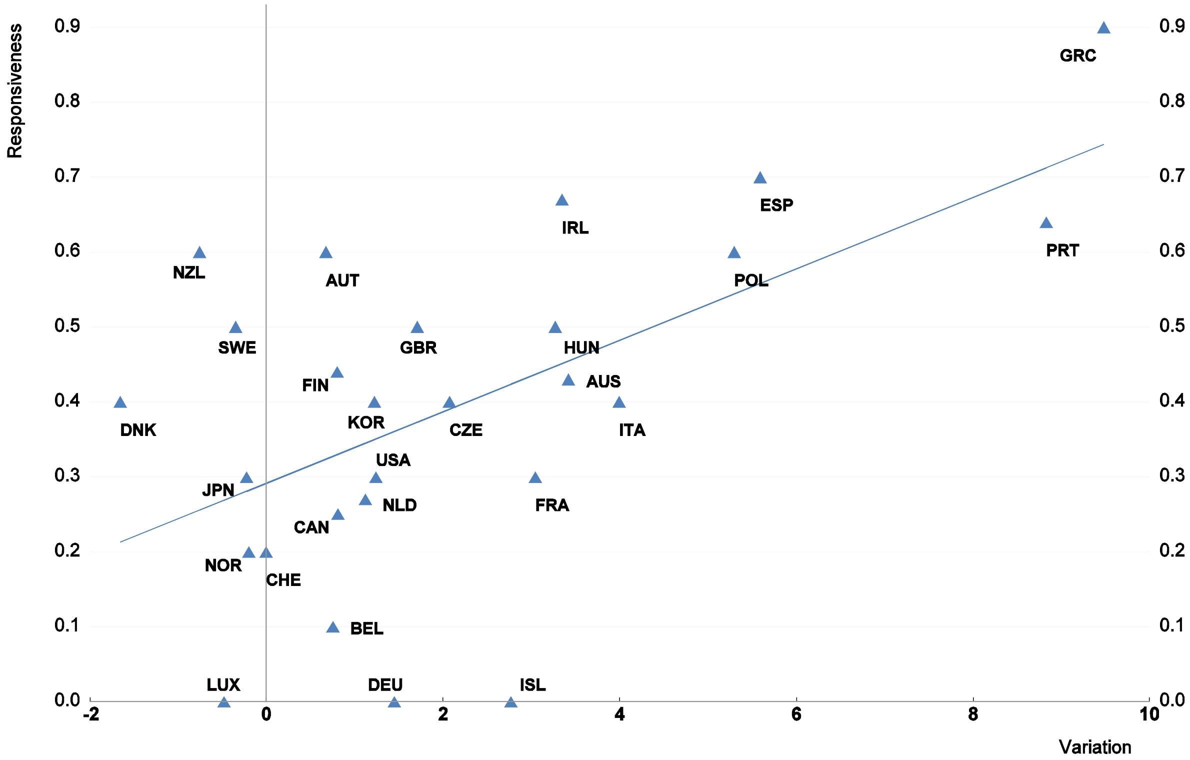


Note: Estimated cumulative GDP impact from reforms specified in Bouis and Duval (2011). The coverage of reforms varies across countries, partly because of data coverage issues. This figure therefore does not show a ranking across countries but possible effects from structural reforms.

Source: R. Bouis and R. Duval (2011), "Raising the Potential Growth After the Crisis: A Quantitative Assessment of the Potential Gains from Various Structural Reforms in the OECD Area and Beyond", OECD Economics Department Working Papers, No. 835, Figure 15.

Fiscal sustainability concerns have given impetus to reform

Overall responsiveness to Going for Growth priorities and fiscal consolidation effort



Note: horizontal axis: variation in the underlying primary balance as a percentage of potential GDP from 2010 to 2012; vertical axis: responsiveness rate, 2010-2011. Correlation coefficient: 0.57; statistically significant at the 1% confidence level.

Source: OECD Quarterly National Accounts; OECD Main Economic Indicators and OECD Economic Outlook 90 Database.

Euro area policy compact

National policies

Pro-growth structural reforms

- Boost growth through productivity and employment
- Strengthen competitiveness
- Protect weak segments of population
- Contribute to current account rebalancing
- Wage adjustment in deficit and surplus countries

Growth friendly fiscal consolidation

- Medium term plans
- Composition of spending cuts and revenues

Financial system repair

- Transparency in balance sheet assessment
- Recapitalize viable banks

Reforms have already started in many countries. Benefits could materialise earlier than expected.

European Union policies

Firewall

- Has been strengthened
- Could be enhanced

Fiscal compact

- Implementation, transparency, communication

Growth

- Single Market can deliver (much) more
- Innovation can be boosted (EU patent)
- EIB lending, infrastructure investment
- Jointly guaranteed bonds
- Redirect structural funds

European Central Bank

- Balance sheet could be used more broadly
- Interest rate can be lowered