



# **Weak Trade, Financial Distortions....** *how to change global prospects?*

**Global Interdependence Center**  
**Frederick Heldring Award for Global Citizenship**  
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**Catherine L. Mann**  
**OECD Chief Economist**

[www.oecd.org/economy/economicoutlook.htm](http://www.oecd.org/economy/economicoutlook.htm)  
ECOSCOPE blog: [oecdoscope.wordpress.com/](http://oecdoscope.wordpress.com/)



# Outline

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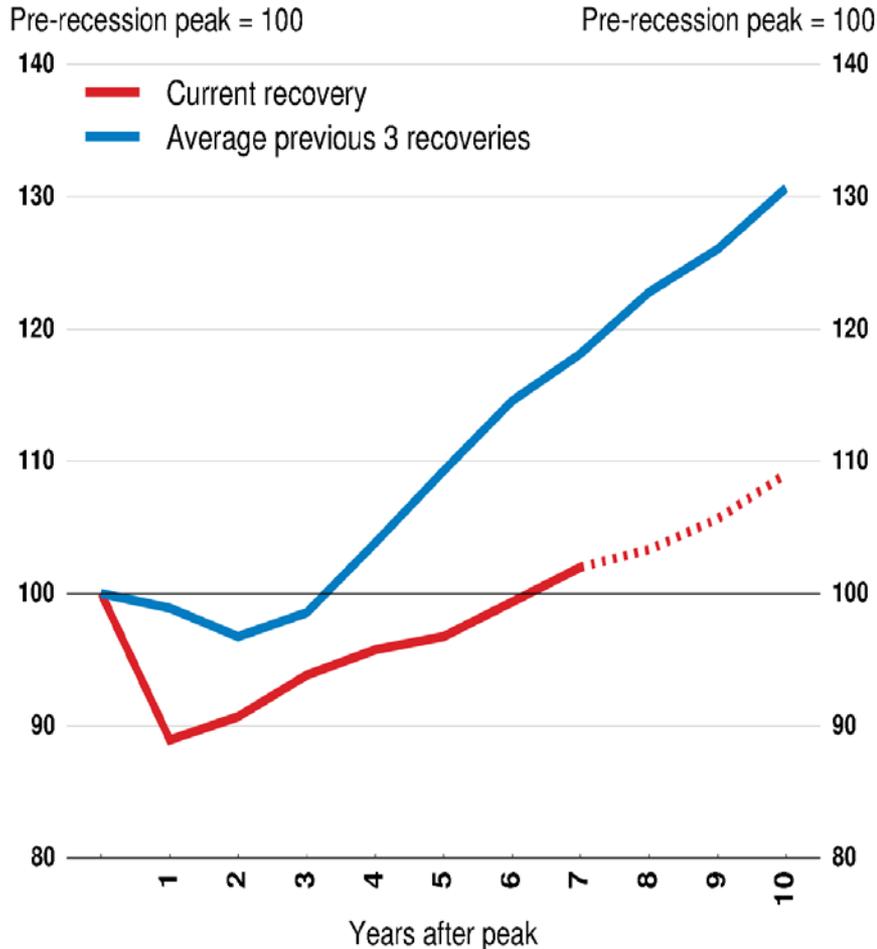
- Current conjuncture:
  - *A low growth trap with financial distortions*
  - *Broken promises*
  - *But there is a window of opportunity*
- Policy ambition to escape the low-growth trap, avoid financial pitfalls, and keep promises
  - *Commit to global openness, supportive local policies*
  - *Deploy fiscal-structural initiatives*



# Real investment remains very sluggish

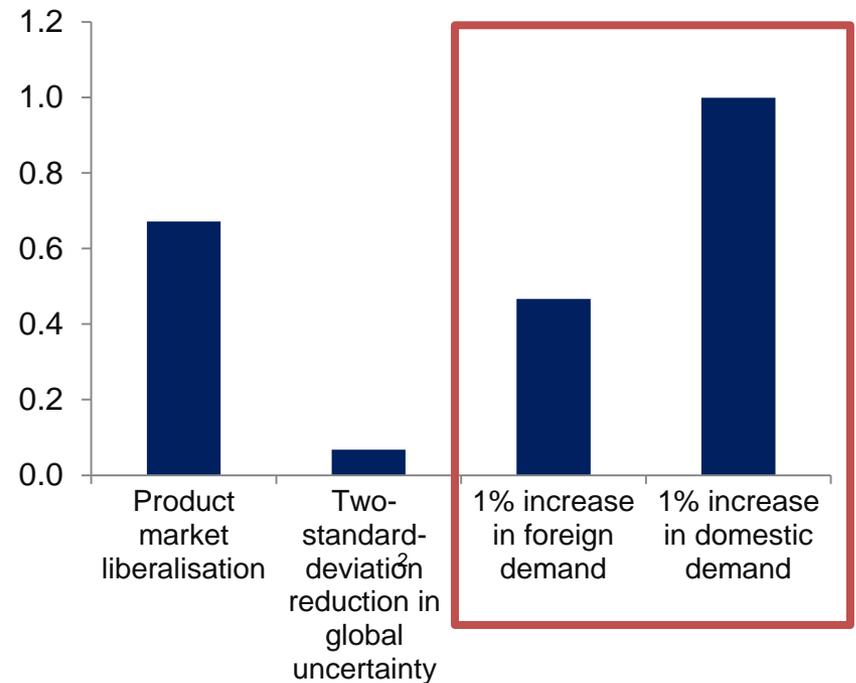
## ... synchronize global demand to signal to invest

### Real investment



### Estimated impact of shocks on investment

Percentage change after 5 years



1. 16% reduction in OECD index of regulation in energy, transport and communications (ETCR) over 5 years, equivalent to the average pace of reduction among 15 OECD countries during the period 1993-2013.
2. Two-standard-deviation reduction in index corresponds to a 26% reduction.

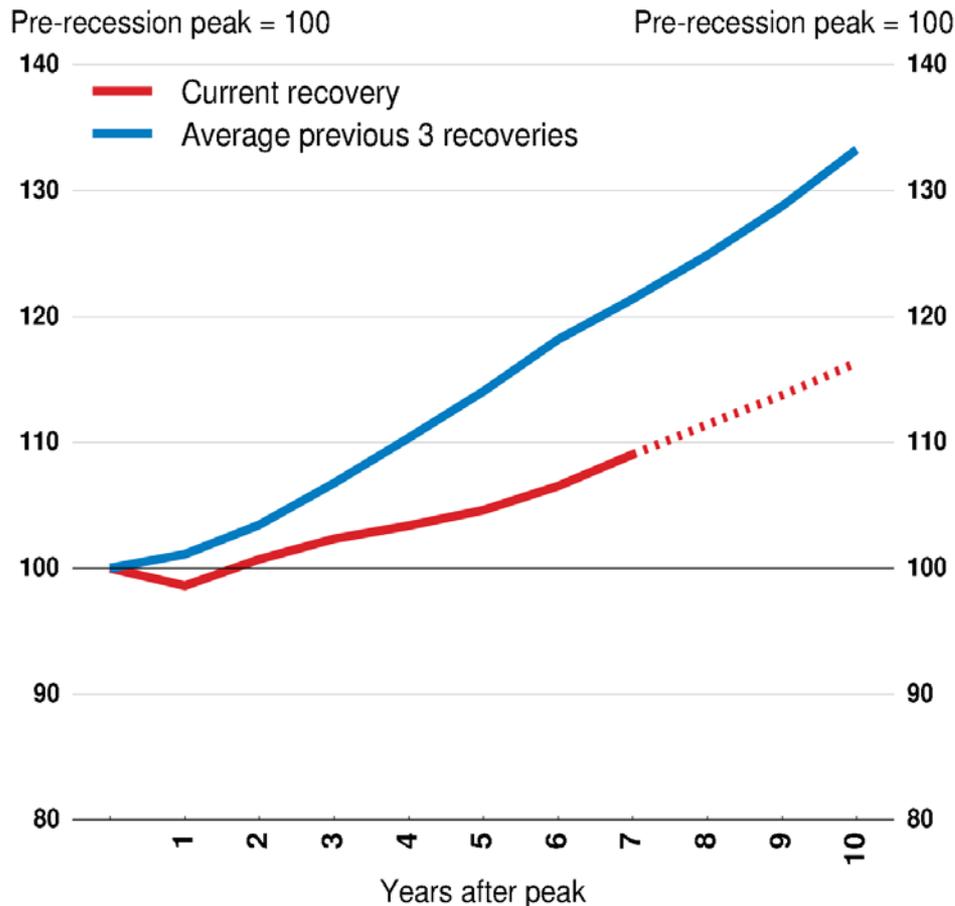
Source: OECD calculations.



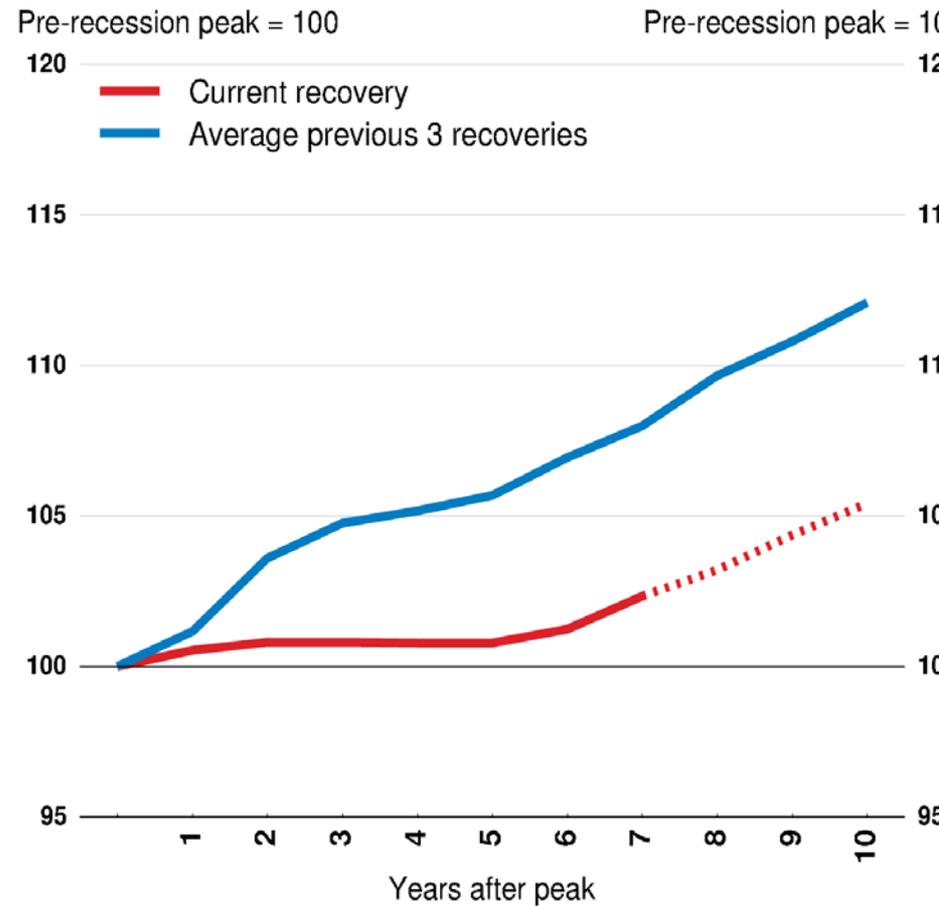
# Consumption growth lags previous recoveries

## *... faster wage growth for sustainable consumption*

### Consumption



### Real wage



NOTE: OECD shown. Current recovery shows since 2008Q1 including the forecasts in the dotted line. Previous 3 recoveries pre-recession peak in 1973Q4, 1980Q1 and 1990Q3.

Source: OECD November 2016 Economic Outlook database.



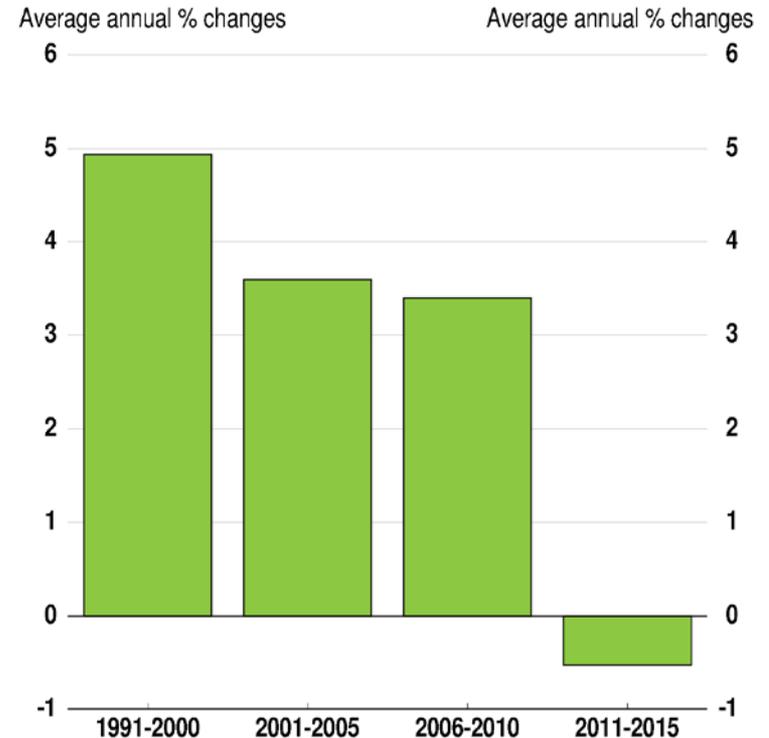
# World trade growth is exceptionally weak ... and global value chains are contracting

## World trade and GDP growth



Note: World GDP volumes measured at PPP exchange rates. World trade volumes measured at market exchange rates in US dollars. For 2014, world trade average growth for four years to remove the rebound following the crisis.  
Source: OECD November 2016 Economic Outlook database; and WTO-OECD-UNCTAD 2016 G20 Trade Policy Monitoring Report.

## Global Value Chain indicator



Note: Structural global value chain indicator shown which adjusts for the economic cycle and changes in commodity prices. For further detail see OECD Economic Policy Paper "Cardiac Arrest or Dizzy Spell: Why is World Trade So Weak and What Can Policy Do About It?".  
Source: OECD June 2016 Economic Outlook database; OECD STAN Bilateral Trade database; and OECD calculations.

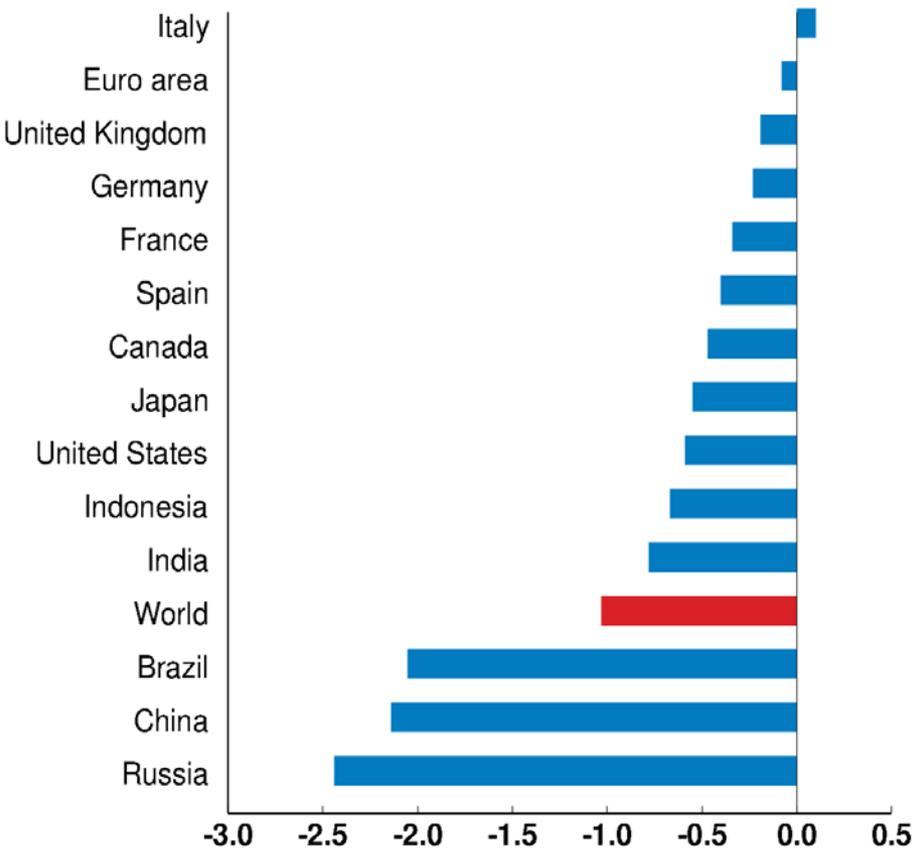


# Real-Financial Disconnect

*...generates financial abnormalities and risks*

## Long-term GDP growth expectations

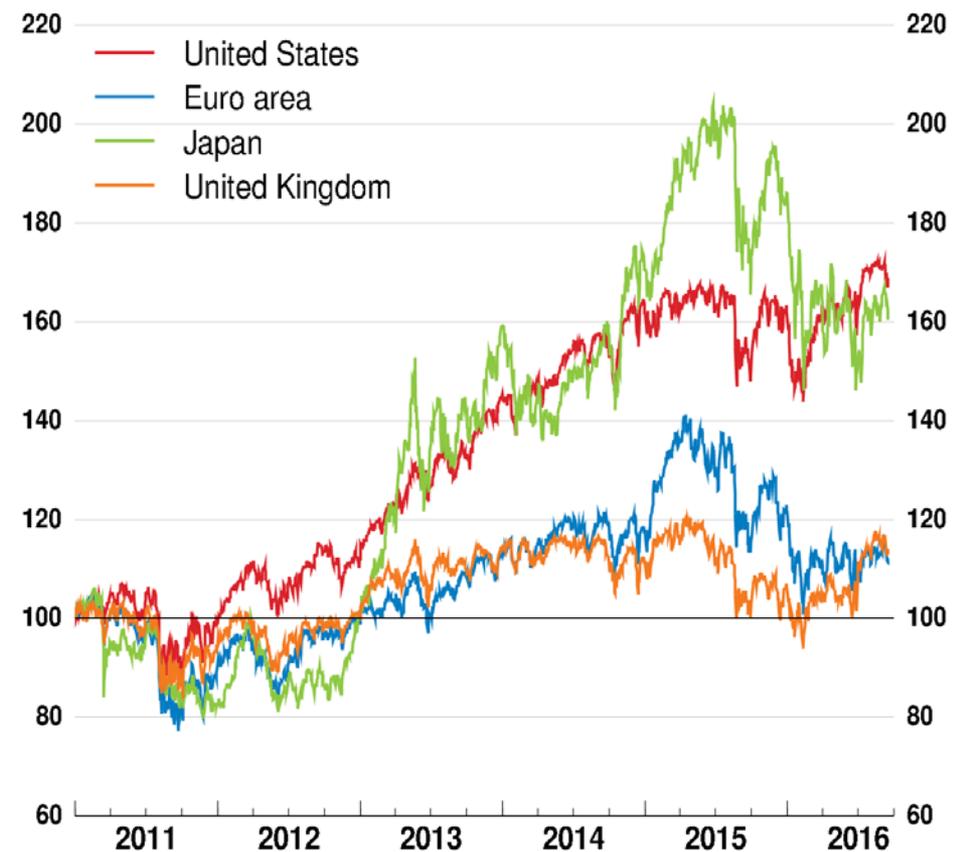
*Change in the past five years*



## Equity prices

Index 3 Jan. 2011 = 100

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Note: Difference between April 2011 projections of average annual GDP growth over 2012-2021 and April 2016 projections of average annual GDP growth over 2017-2026. OECD and World estimates based on weighted average of countries shown, using 2015 PPP shares.

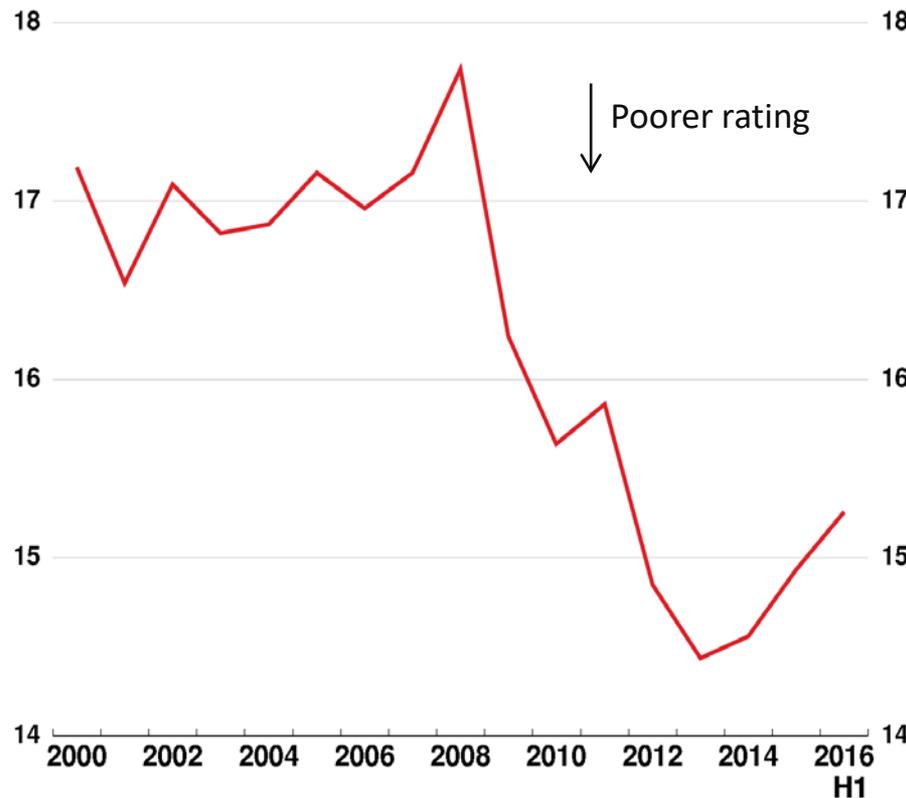
Source: Consensus Forecasts; Thomson Reuters; and OECD calculations.



# Search for yield and price distortions in some markets add to risks

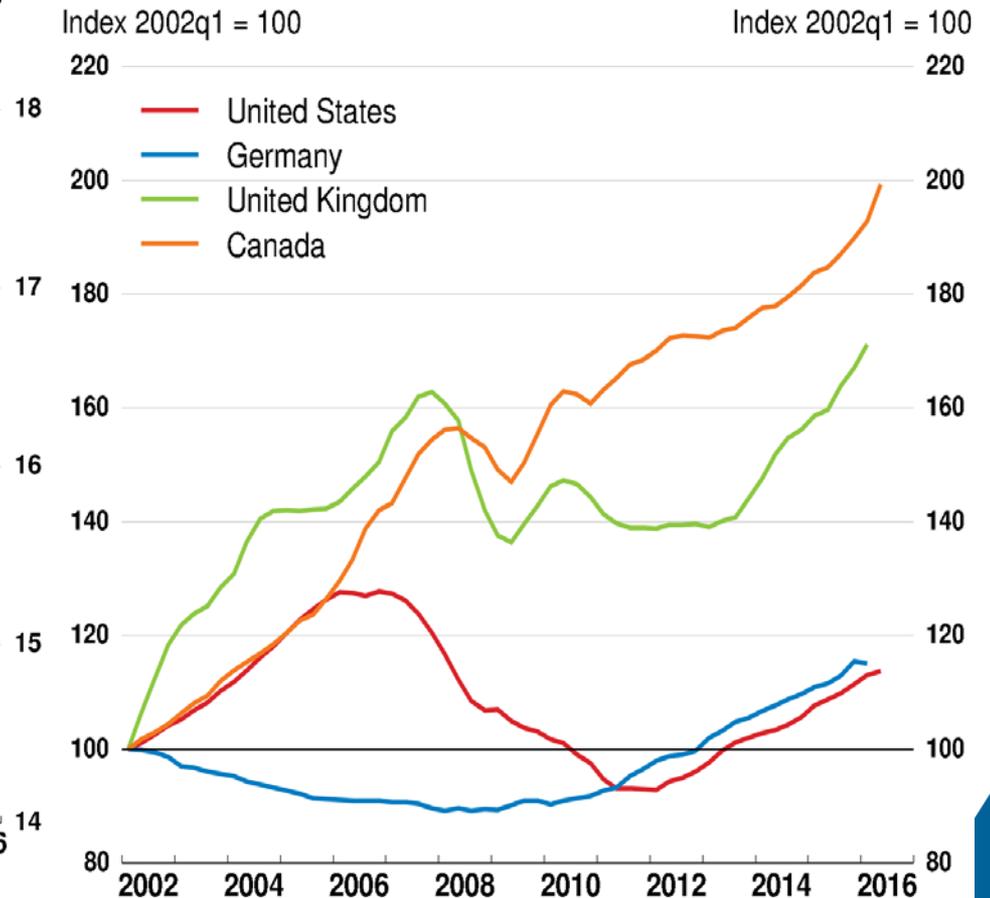
## Quality of corporate bonds has declined

Average value-weighted rating index for newly issued bonds



Source: FactSet; OECD Business and Finance Scoreboard;

## Real house prices



Source: OECD Analytical House Price database.



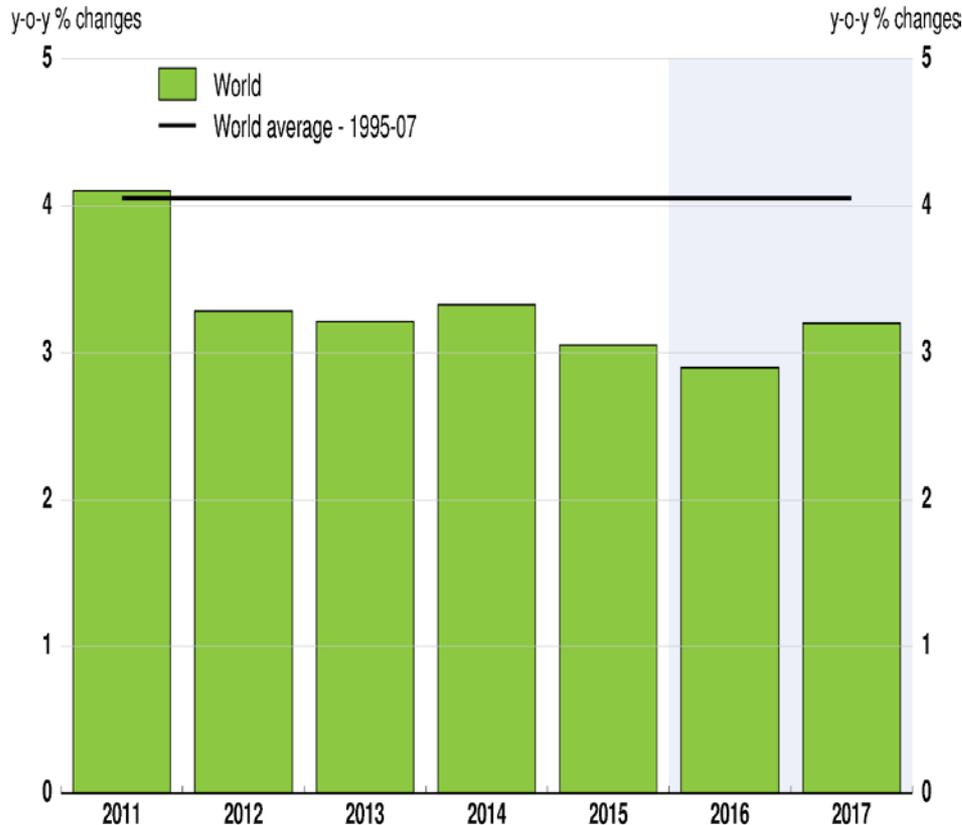
WHAT DOES ALL THIS  
ADD UP TO?



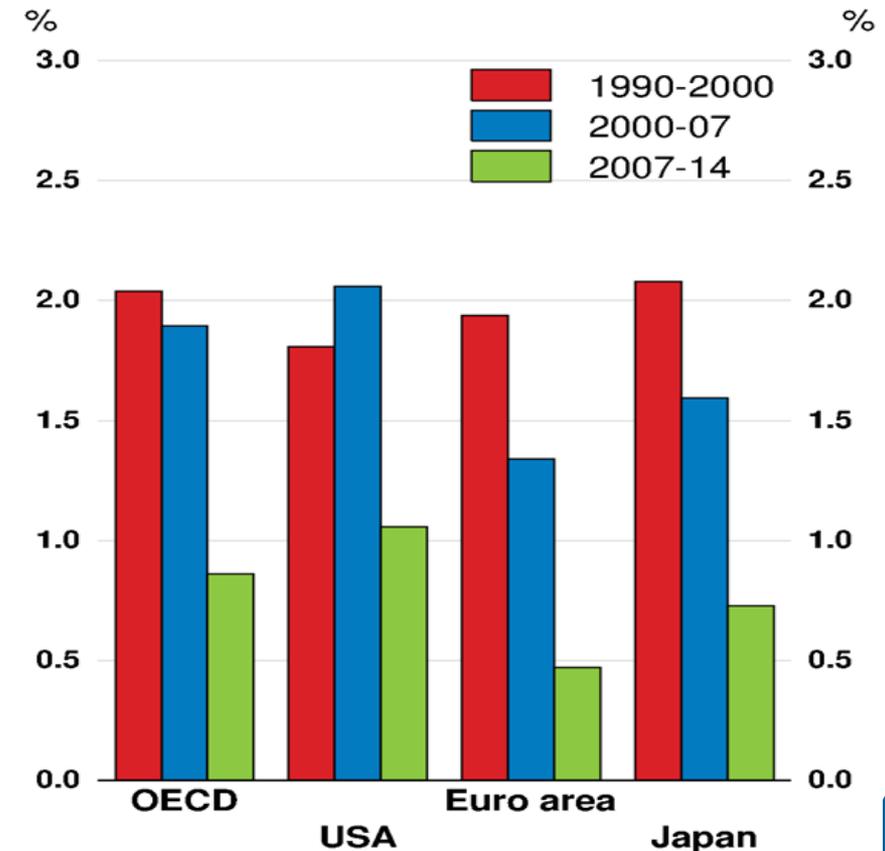
# A Low Growth Trap

... Sluggish global demand, collapsing productivity growth

## World real GDP



## Productivity Growth



Note: World GDP measured at purchasing power parity exchange rates.

Source: OECD Economic Outlook database (September).

Note: Labour productivity growth is output per hour worked at annualised rate. Source: OECD June 2016 Economic Outlook database; OECD National Accounts database; OECD Productivity database; OECD calculations.

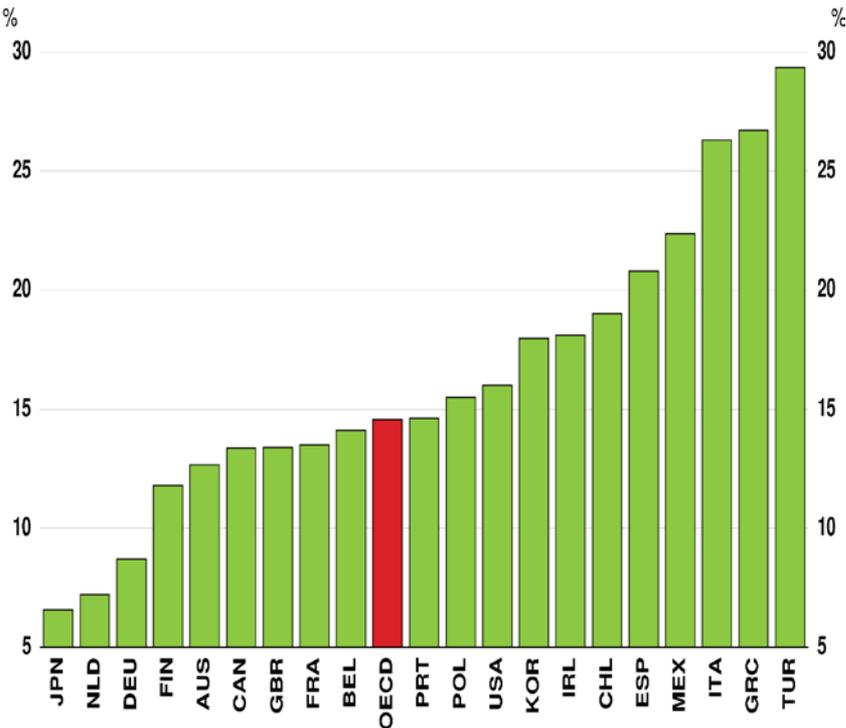


# The Low Growth Trap means broken promises

## ... to the young and to the old

### Inactive and unemployed youth

Share of all youth (15-29 years old)



Note: For LHS, OECD is the unweighted average of 34 OECD countries. 2013 for Chile and the United States. Youth aged 15-24 for Japan. Source: OECD calculations based on national labour force surveys; OECD Short-Term Labour Market Statistics database.

### Retirement income for a given contribution

Index 2000 = 100

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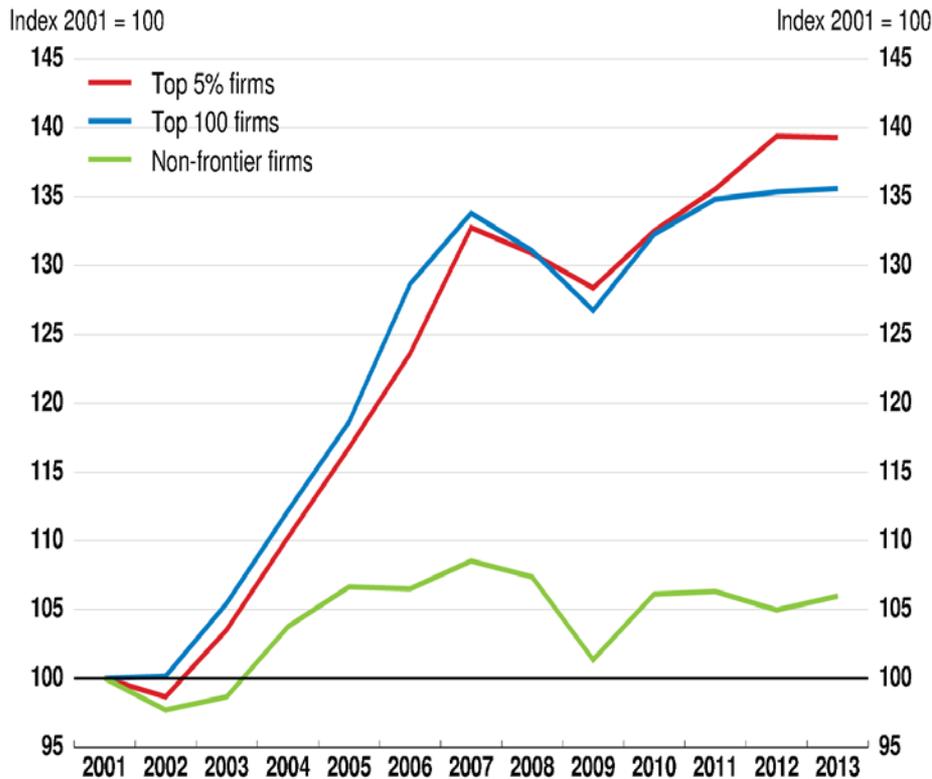


Note: impact of falling interest rates on real incomes in retirement for a defined contribution scheme. Annuity payments calculated for the same hypothetical individual retiring in 2000 vs 2014 | Source: OECD Business and Finance Outlook 2015.



# The Low Growth Trap is characterized by ... widening productivity gap, rising inequality

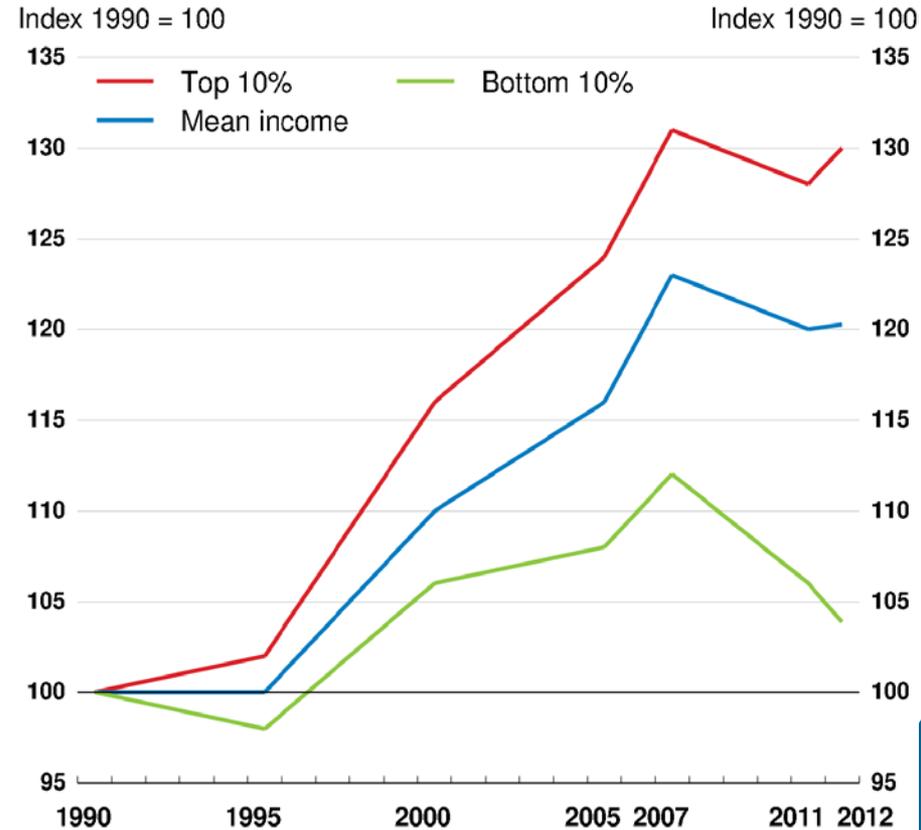
## Productivity diffusion gap



Source: OECD preliminary results based on Andrews, D., C. Criscuolo and P. Gal (2016), "Mind the Gap: Productivity Divergence between the Global Frontier and Laggard Firms", OECD Productivity Working Papers, forthcoming; Orbis data of Bureau van Dijk.

## Inequality in income

Real household disposable income, total population



Note: OECD is the unweighted average of the countries for which data are available.  
Source: OECD estimations based on Kappeler et al. (2016), "Decoupling of Productivity and Median Wage Growth: Macro-Level Evidence", OECD Economics Department Working Papers, forthcoming; OECD National Accounts database; OECD Earnings database; OECD Income Distribution database; OECD calculations.



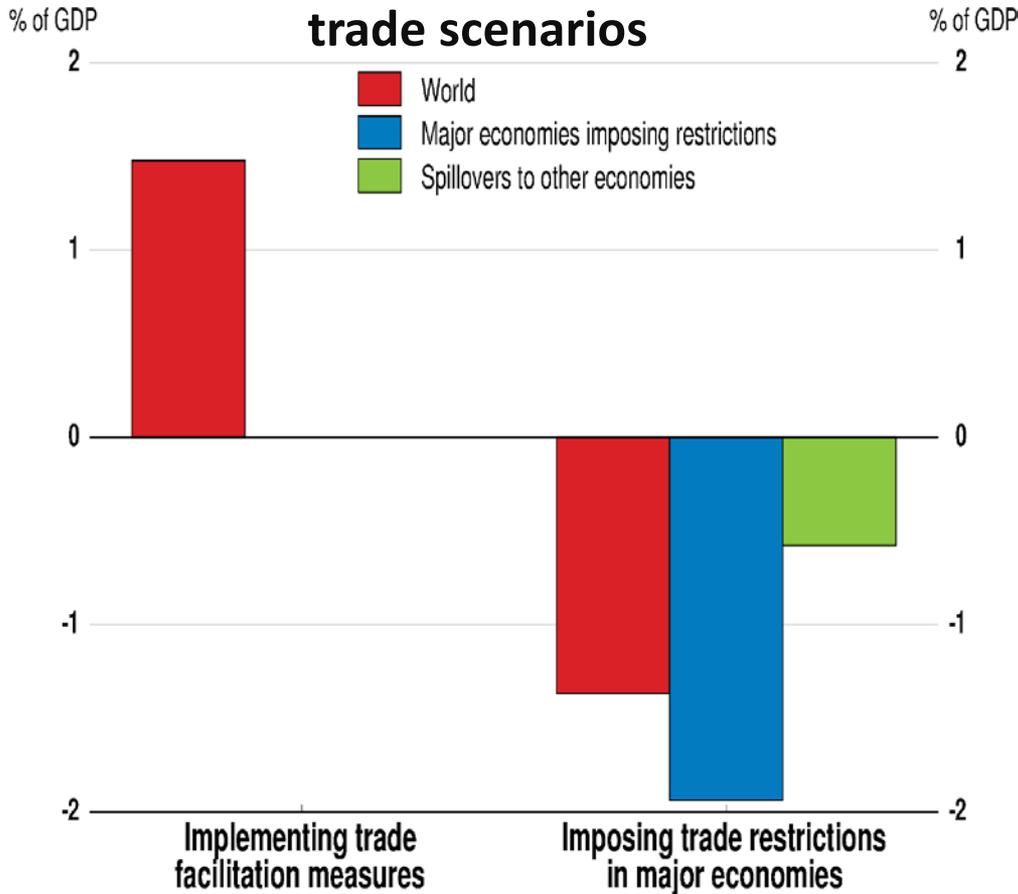
# POLICIES TO ESCAPE THE LOW GROWTH TRAP



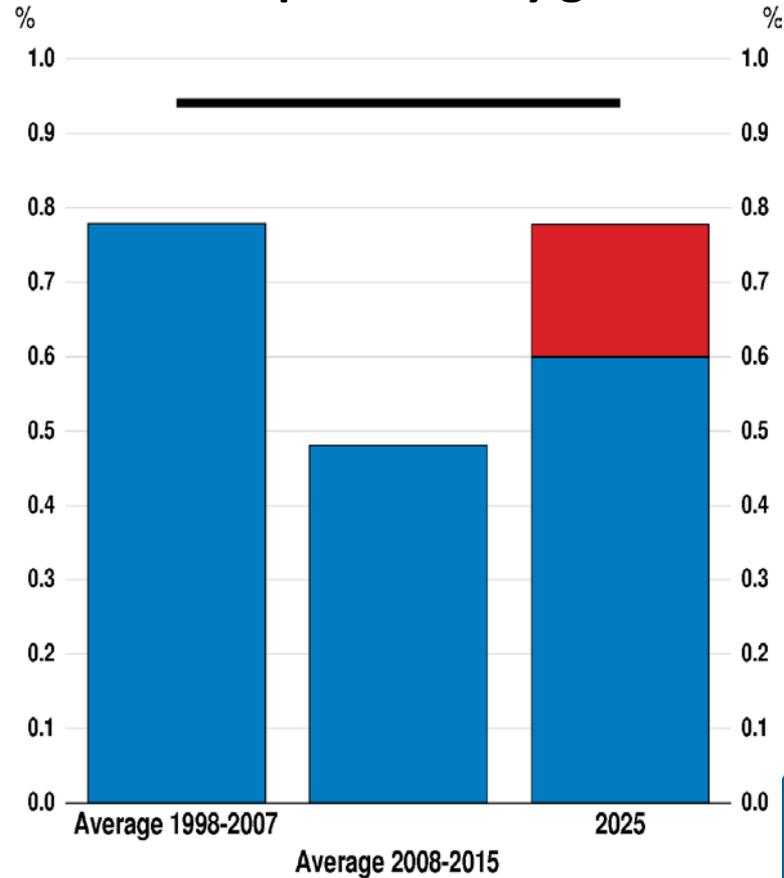
# Trade policy choices

*... Restrictions hurt; opening boosts productivity*

## Medium-term GDP impact of different trade scenarios



## OECD annual productivity growth



Note: The implementing trade facilitation measures scenario shows the impact of a trade cost reduction by 1.3% across all sectors in all countries, an estimate of the global average derived from the OECD's Trade Facilitation Indicators. The imposing trade restrictions in major economies scenario shows the impact of a goods trade cost increase of 10 percentage points for China, Europe and the United States against all trading partners, equivalent to an average increase in tariffs to 2001 levels, the year when trade negotiations under the Doha Development Round started. Source: OECD METRO model; and OECD calculations.



# Policy packages are needed

*... sharing globalization gains also raises productivity*

## People in advanced economies are more negative about globalisation

*Views on trade and foreign investment, 2014*



Source: Pew Research Center.

## Trade policies must be accompanied by:

Social protection and support for workers in transition

Investing in human capital and infrastructure

Active labour market policies to promote skills upgrading and matching

Product market reforms to promote competition and firm entry

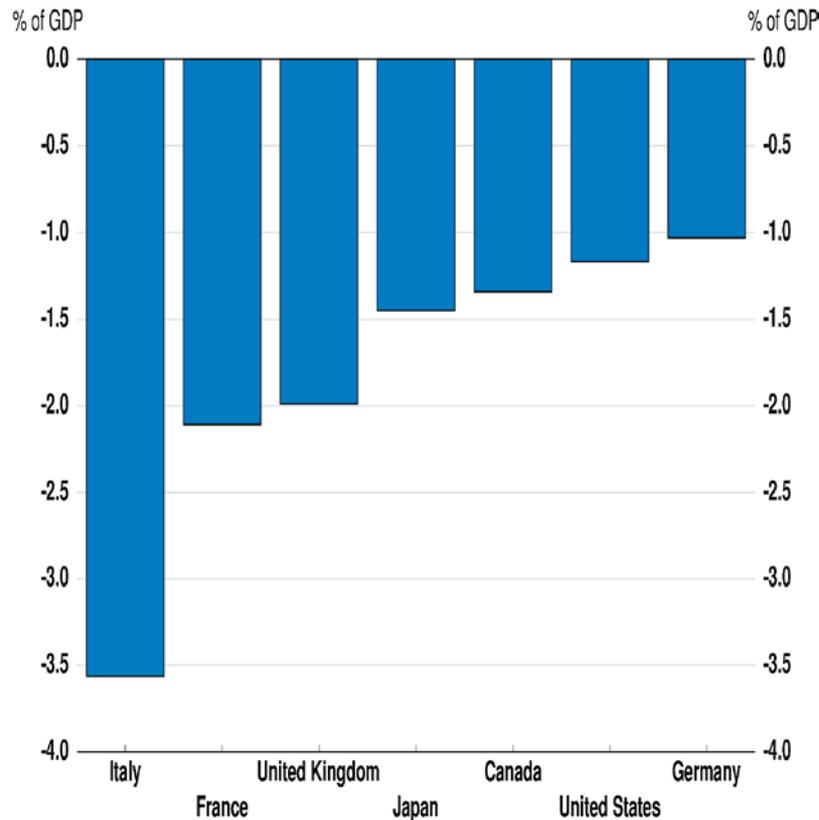


# Multi-year fiscal initiative is possible

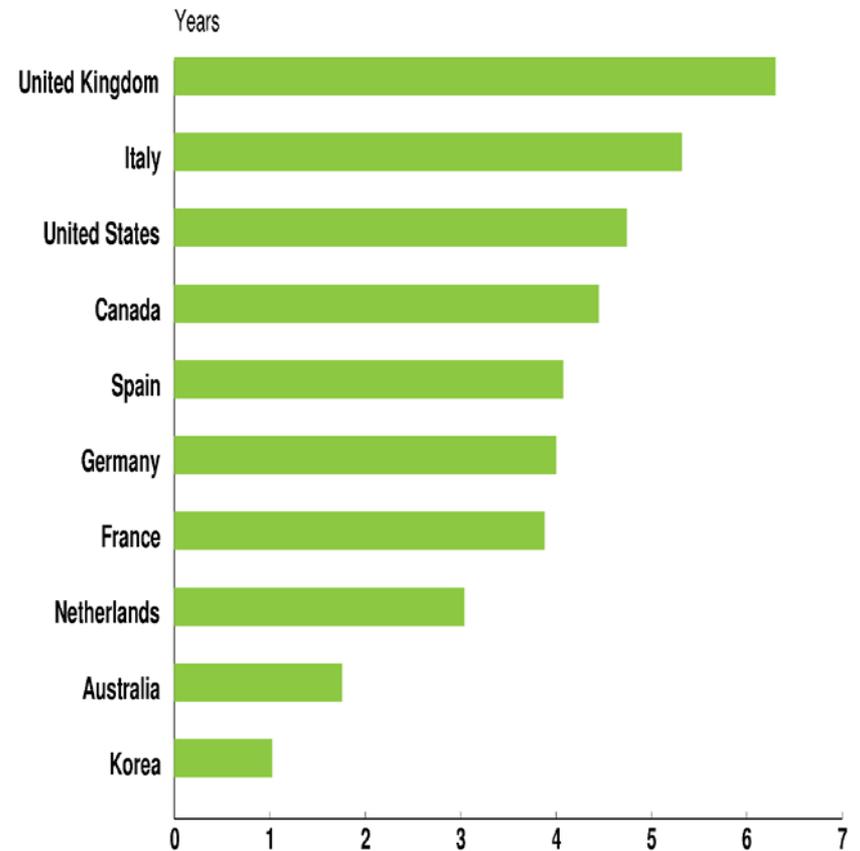
*... use window of opportunity of low interest rates*

## Fall in government interest payments

*Estimated budget gains over 2015-17 due to lower interest rates*



## Number of years a permanent investment increase of 0.5% of GDP can be funded with temporary deficits



Note: Budget gains calculated based on general government debt at tl stock matures each year, comparing the interest rate on 10-year gover the 2016 average to August for 2016 and 2017.

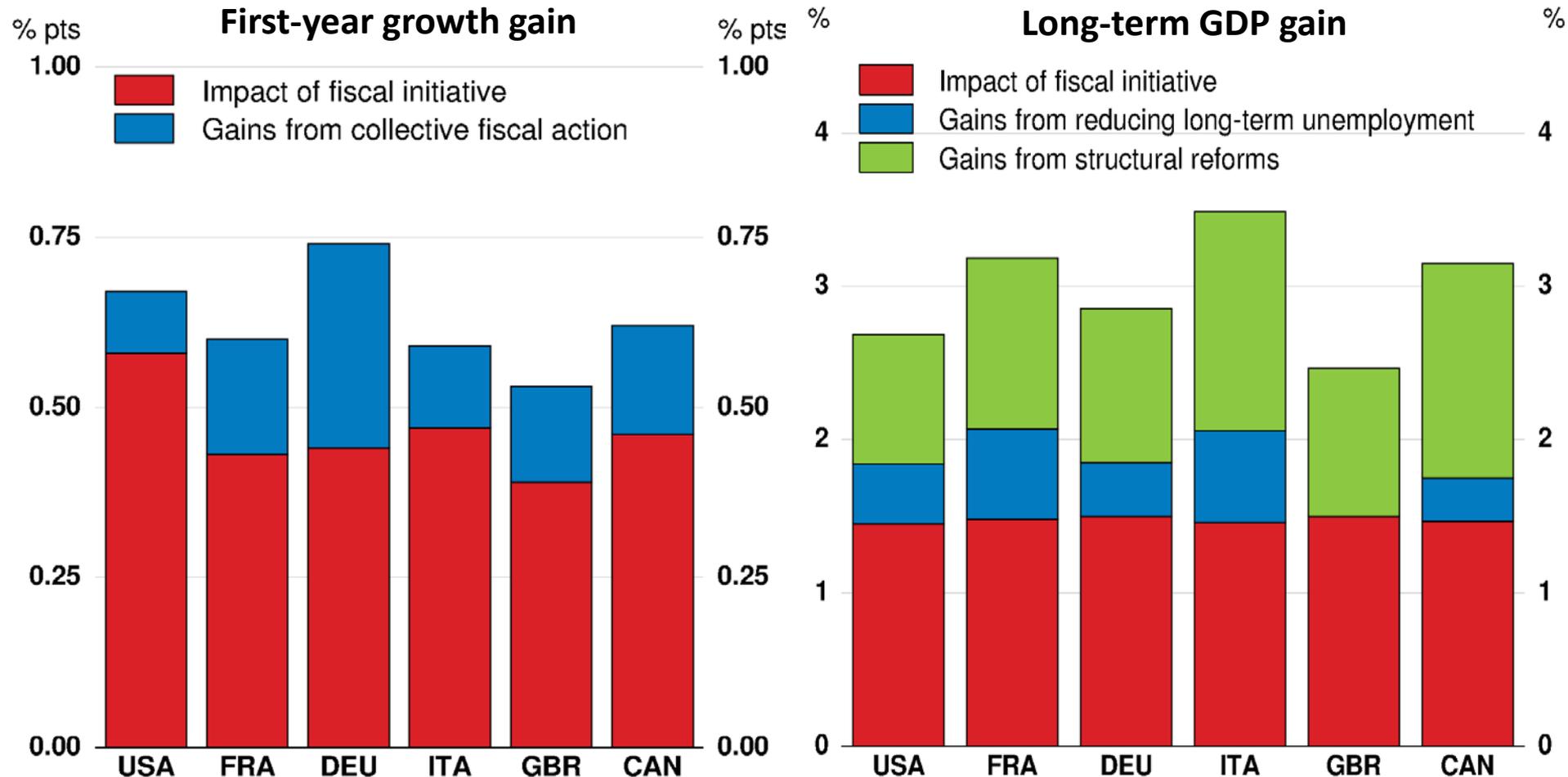
Source: OECD June 2016 Economic Outlook database; and OECD calculations.



# Deploy collective fiscal-structural initiatives

*... synchronizes demand upturn, boosts productivity*

From a 0.5% of GDP increase in public investment



Note: Structural reforms shows the impact of a 10% reduction of product market regulations.

Source: Mourougane A. et al. (2016), "Can an increase in public investment sustainability lift economic growth?" OECD Economics Department Working Papers, No. 1351, OECD Publishing, Paris; and OECD calculations.



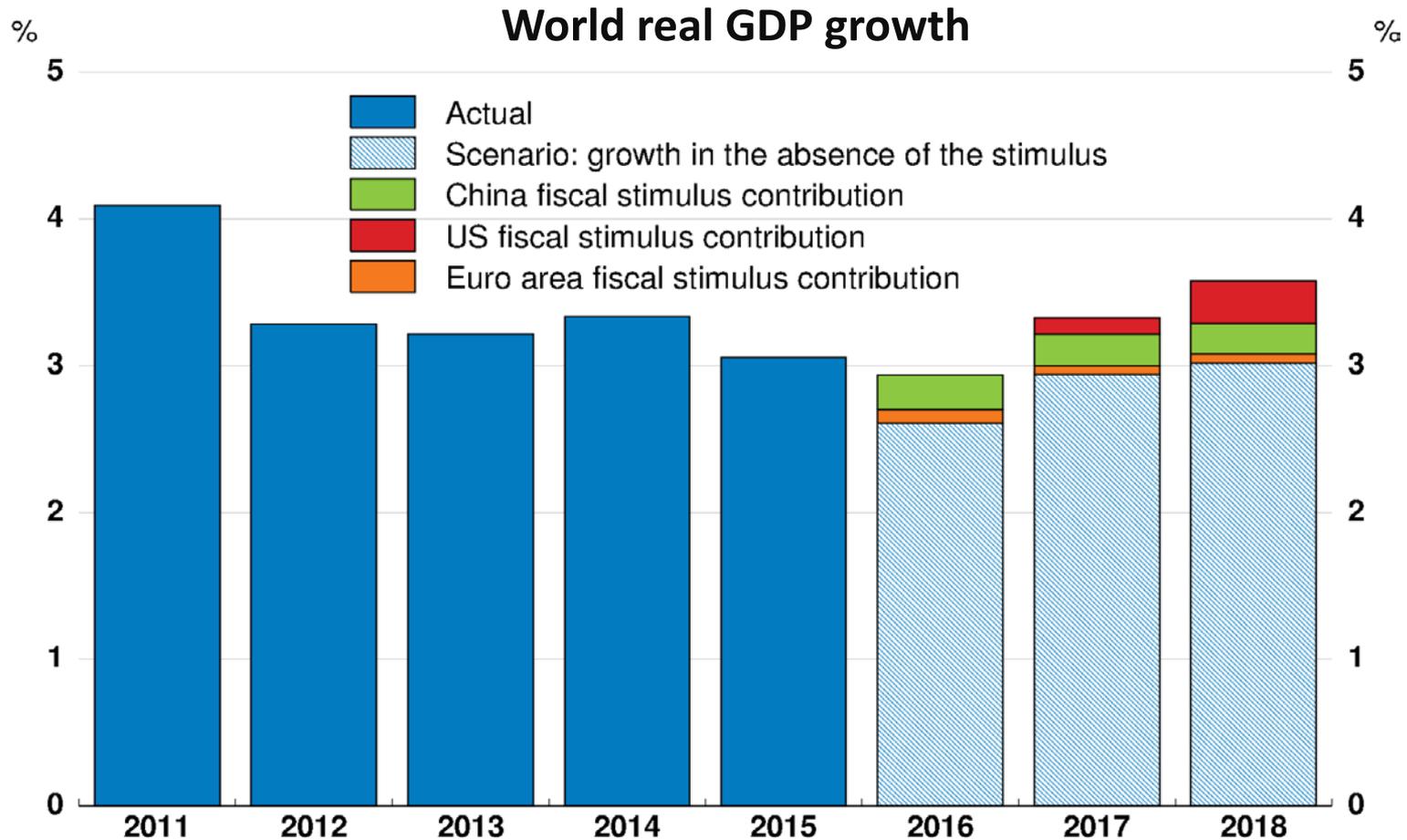
## Key Messages

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- **Weak demand undermines productivity and potential output**
  - *Leading to a low growth trap and broken promises*
- **Real-financial disconnect and exceptionally low interest rates generate financial distortions and risks**
  - *But low interest rates create a window of opportunity*
- **Policy ambition to escape the low-growth trap and keep promises**
  - *Commit to global and local policy packages*
  - *Deploy fiscal-structural initiatives*



# Would policies make a difference?

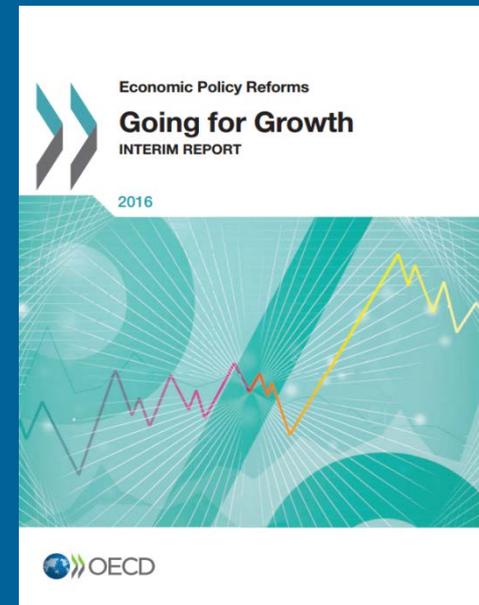
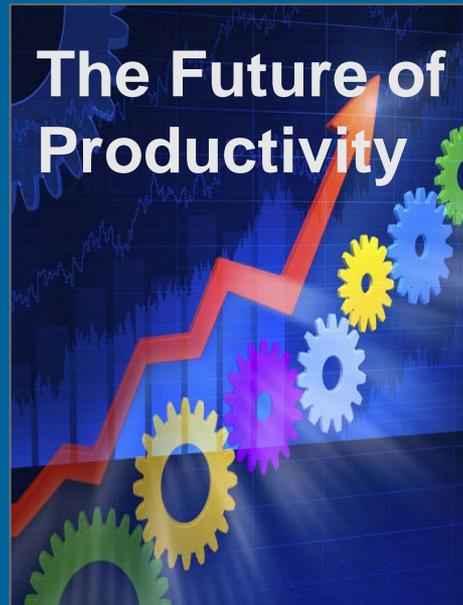


Note: Based on macro-model simulations of an assumed fiscal stimulus in the US worth  $\frac{3}{4}$  per cent of GDP in 2017 and  $\frac{1}{4}$  per cent of GDP in 2018; estimated fiscal stimulus in China of  $\frac{1}{2}$  per cent of GDP in 2016 and 1 per cent of GDP in both 2017 and 2018; and estimated fiscal stimulus in the euro area of 0.4 per cent of GDP in 2016, 0.2 per cent of GDP in 2017 and 0.3 per cent of GDP in 2018. The stimulus in China and the euro area is assumed to be implemented through government final expenditure on consumption.

Source: OECD November 2016 Economic Outlook database; and OECD calculations.



# THANK YOU!



[www.oecd.org/economy/economicoutlook.htm](http://www.oecd.org/economy/economicoutlook.htm)  
[www.oecd.org/global-forum-productivity](http://www.oecd.org/global-forum-productivity)  
[www.oecd.org/eco/growth/goingforgrowth.htm](http://www.oecd.org/eco/growth/goingforgrowth.htm)  
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# Most countries are moving toward the right fiscal stance, but Europe could do more

OECD recommends more expansionary policy than projected

## Recommended fiscal stance for 2017

Contractionary    Mildly contractionary    Broadly neutral    Mildly expansionary    Expansionary

Contractionary

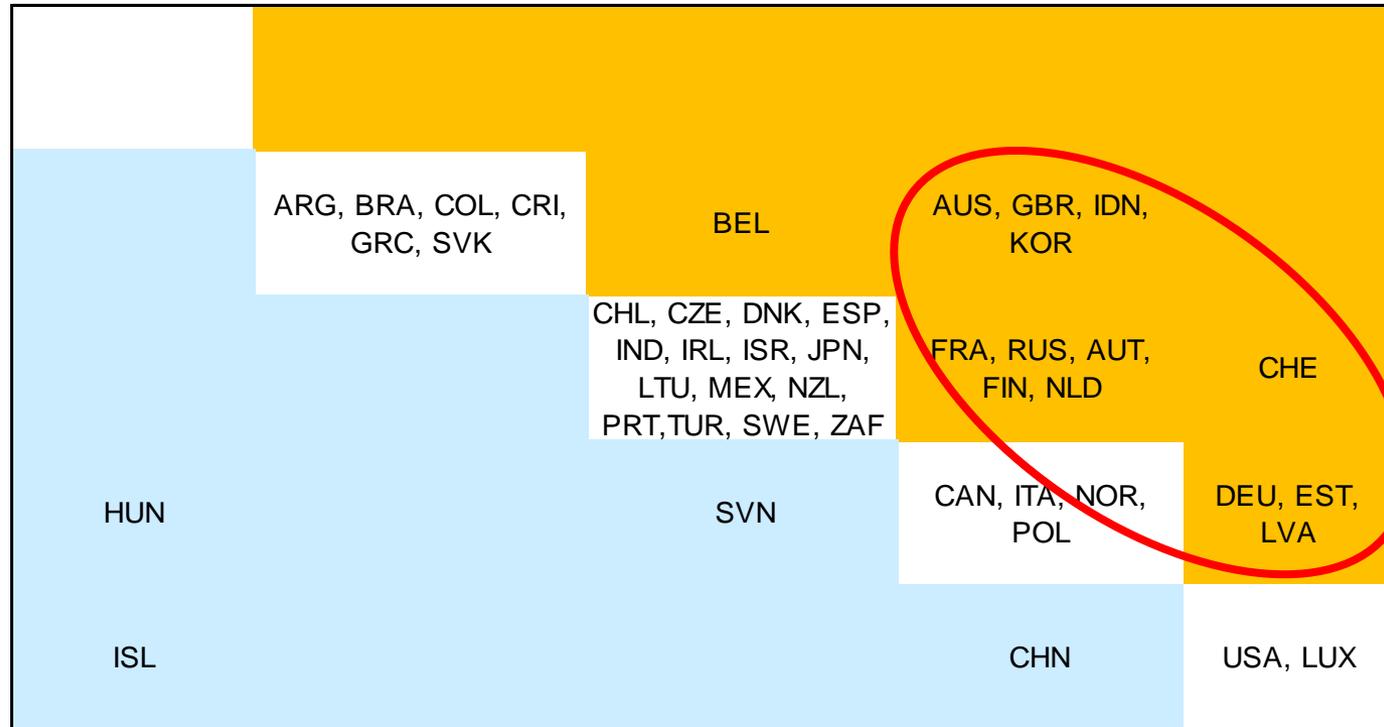
Mildly contractionary

Broadly neutral

Mildly expansionary

Expansionary

**Projected  
fiscal stance  
for 2017**



OECD recommends less expansionary policy than projected