



OECD INTERIM ECONOMIC OUTLOOK

*Will Soft Foundations and
Financial Vulnerabilities
Derail the Modest Recovery?*

Global Interdependence Center – Central Banking Series
Madrid, 27 March 2017

Catherine L. Mann
OECD Chief Economist



Key messages

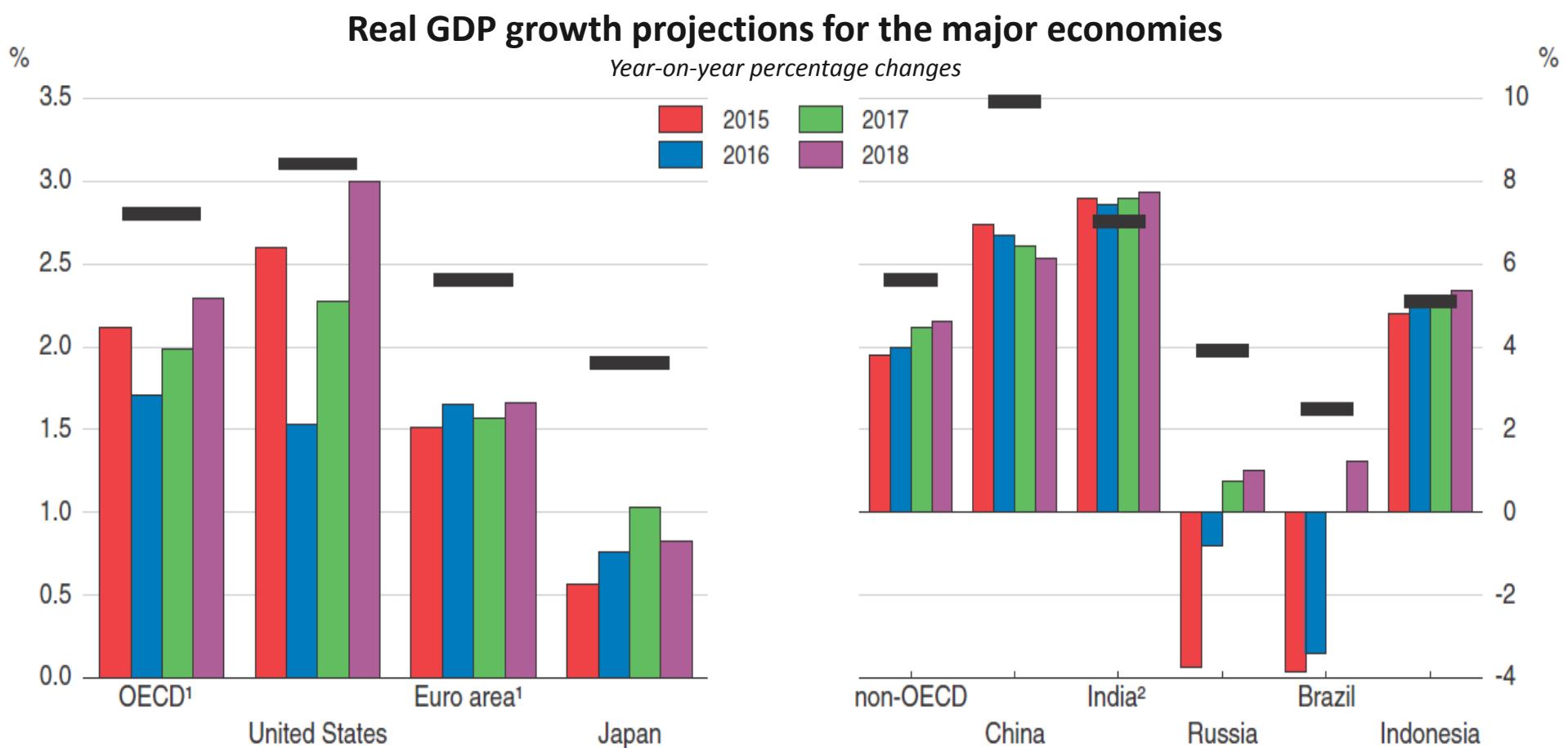
Global growth is set to pick up modestly but remains too slow
... *to meet expectations and entitlement commitments*
... *and productivity foundations are soft.*

Financial vulnerabilities could derail the pick-up
... *including disconnects, volatilities, vulnerabilities.*

Policy needs to strengthen inclusive growth and manage risks
... *avoid trade protectionism, deploy fiscal initiatives*
... *but environment is inauspicious*
... *and policy ambition lags and lacks synergies.*



Improved growth projections, but too slow to make good on commitments



Note: Horizontal lines show the average annual growth rate of GDP in the period 1987-2007. Data for Russia are for the average annual growth rate in the period 1994-2007.

1. With growth in Ireland in 2015 computed using gross value added at constant prices excluding foreign-owned multinational enterprise dominated sectors.

2. Fiscal years.

Source: OECD November 2016 Economic Outlook database.

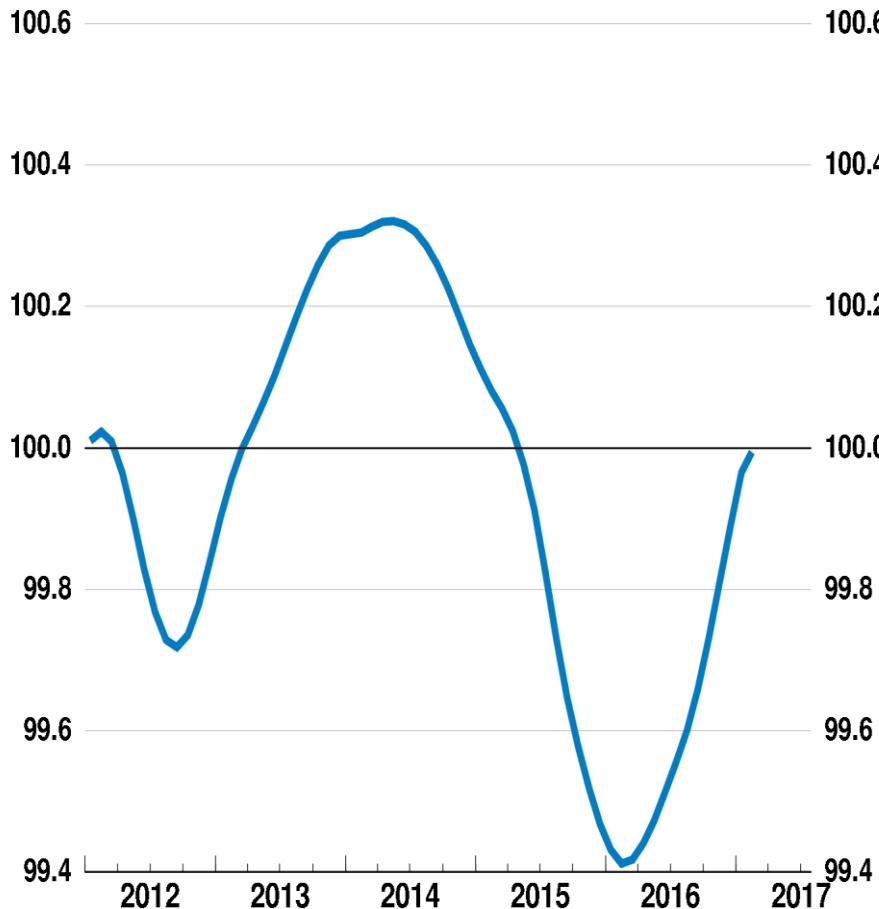


Leading indicators and confidence point to stronger but not stellar growth

OECD Composite Leading Indicator

OECD and BRIICS, ratio to trend, amplitude adjusted

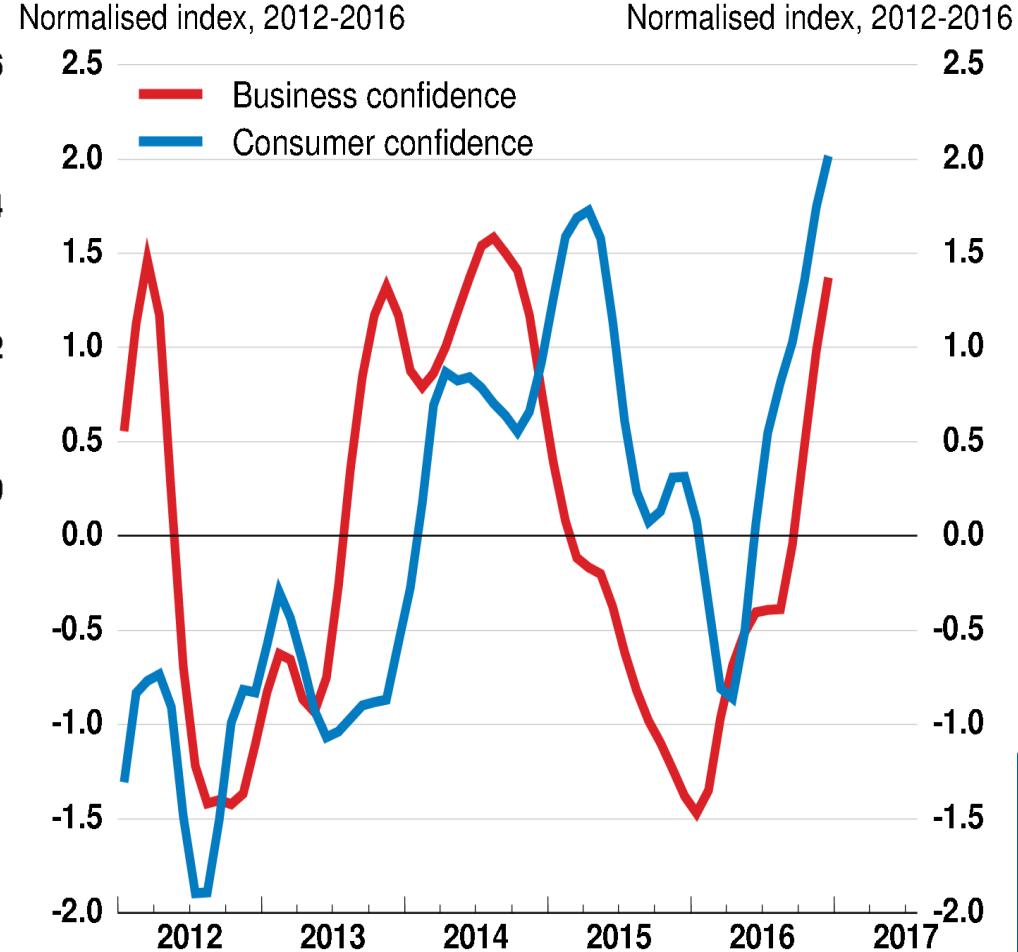
Long-term average = 100



Business and consumer confidence

OECD and BRIICS

Normalised index, 2012-2016

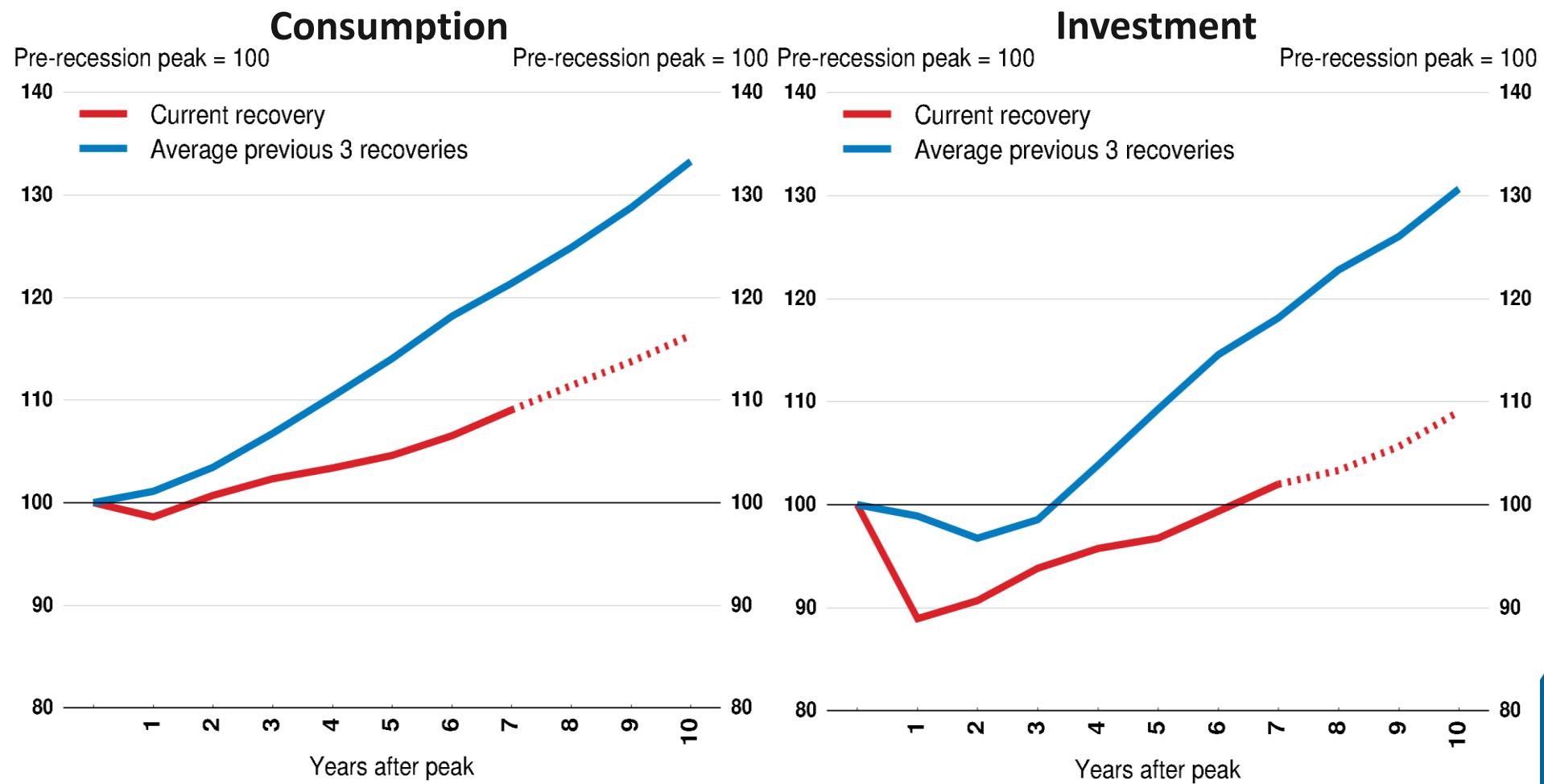


Note: Confidence indices are GDP PPP weighted averages of individual country normalised confidence series.

Source: OECD Composite Leading Indicators; OECD Main Economic Indicators database; Eurostat; and OECD calculations.



Improved market sentiment contrasts with slow growth in consumption and investment



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. Consumption is real total consumers' expenditure and investment is real total gross fixed capital formation.

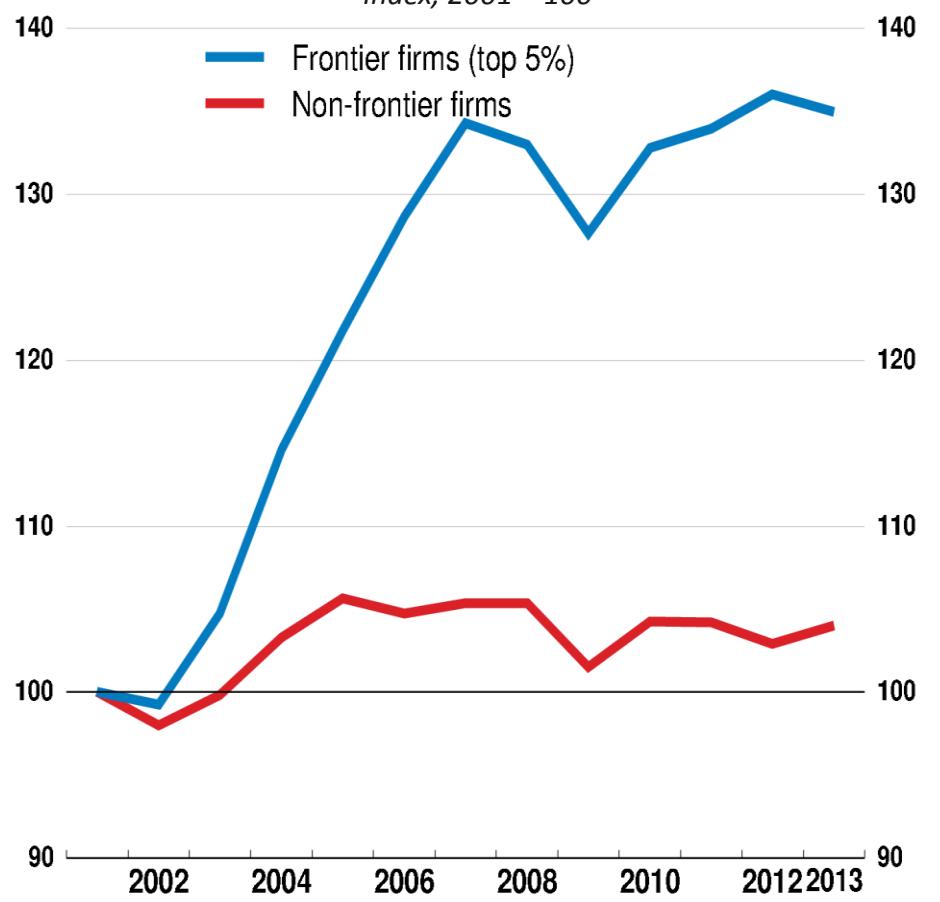
Source: OECD November 2016 Economic Outlook database.



Stronger sustainable top-line needs stronger foundations of productivity and wage growth

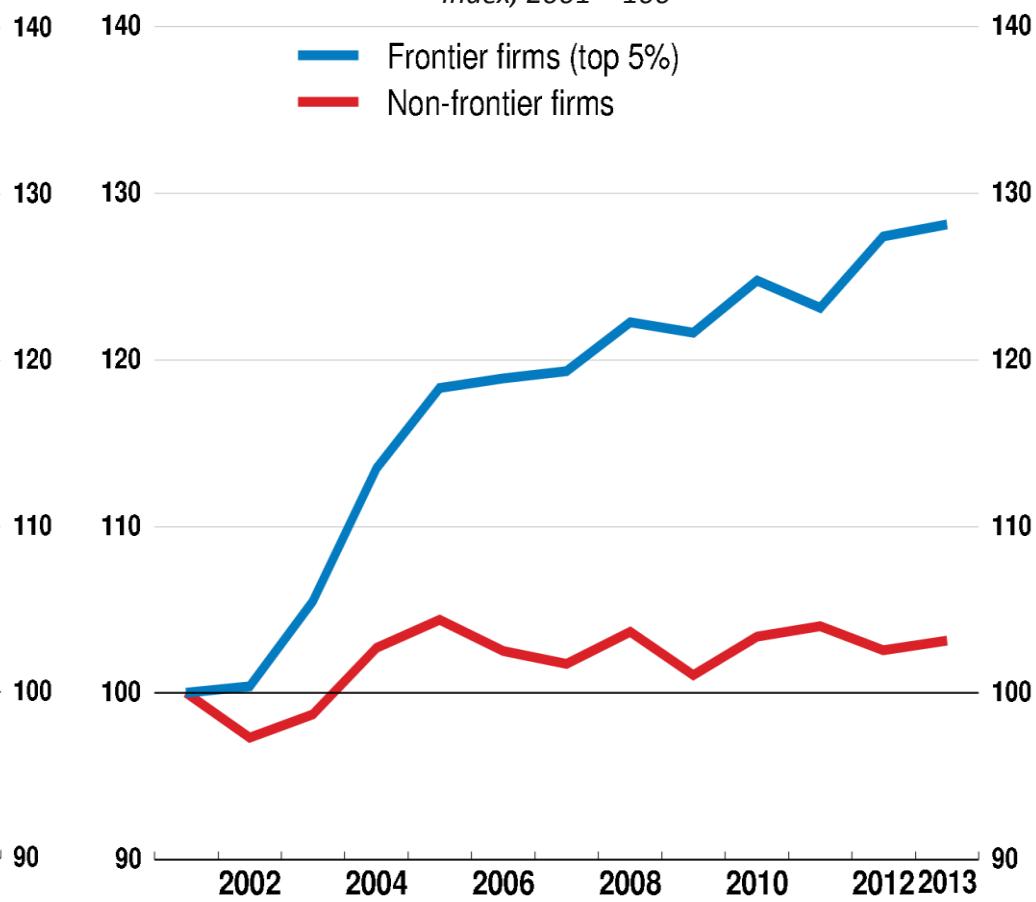
Labour productivity

Index, 2001 = 100



Real compensation per worker

Index, 2001 = 100



Note: Frontier firms are the 5% of firms with the highest labour productivity by year and sector. Included industries are manufacturing and business services, excluding the financial sector, for firms with at least 20 employees.

Source: Andrews, D., C. Criscuolo and P. Gal (2016), "The Best versus the Rest: The Global Productivity Slowdown, Divergence across Firms and the Role of Public Policy", OECD Productivity Working Papers, No. 5; Orbis data of Bureau van Dijk; and OECD calculations.



Risks and financial vulnerabilities could derail the modest recovery

Disconnects

- Sentiment robust, but consumption and investment weak
- Financial markets vs. real economy, inflation and risks

Volatility

- Sharp changes in global interest rates
- Large exchange rate movements
- Diverging interest rates among advanced economies

Vulnerabilities

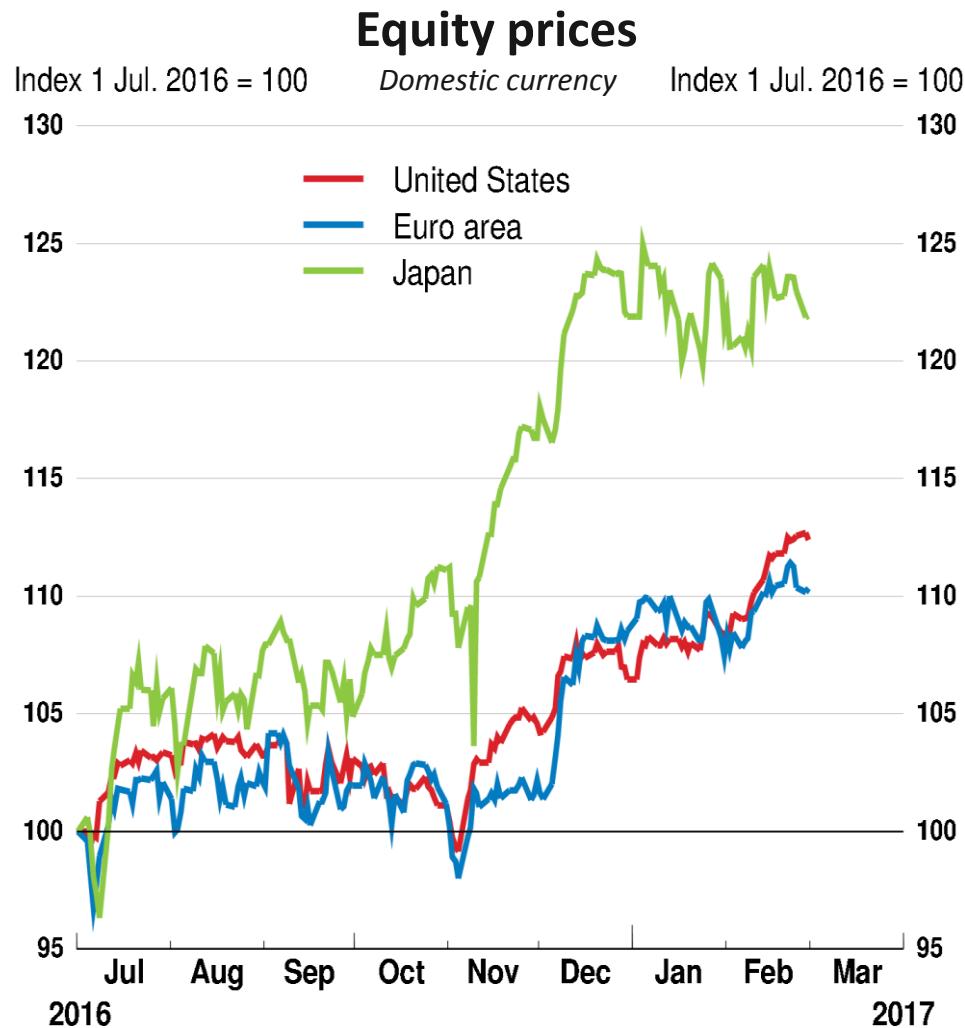
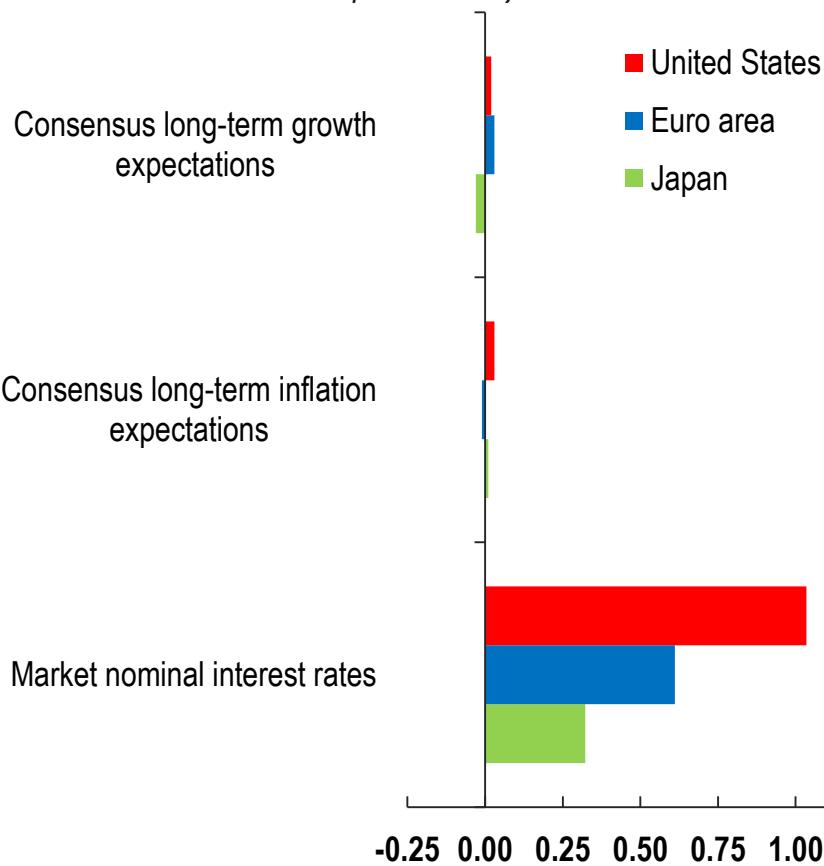
- House prices in some advanced economies
- Private-sector credit growth in many EMEs
- Exposure to overseas borrowing and currency mismatch



Disconnect between the real economy and market valuations

Change in GDP growth and inflation expectations and interest rates

% pts since July 2016



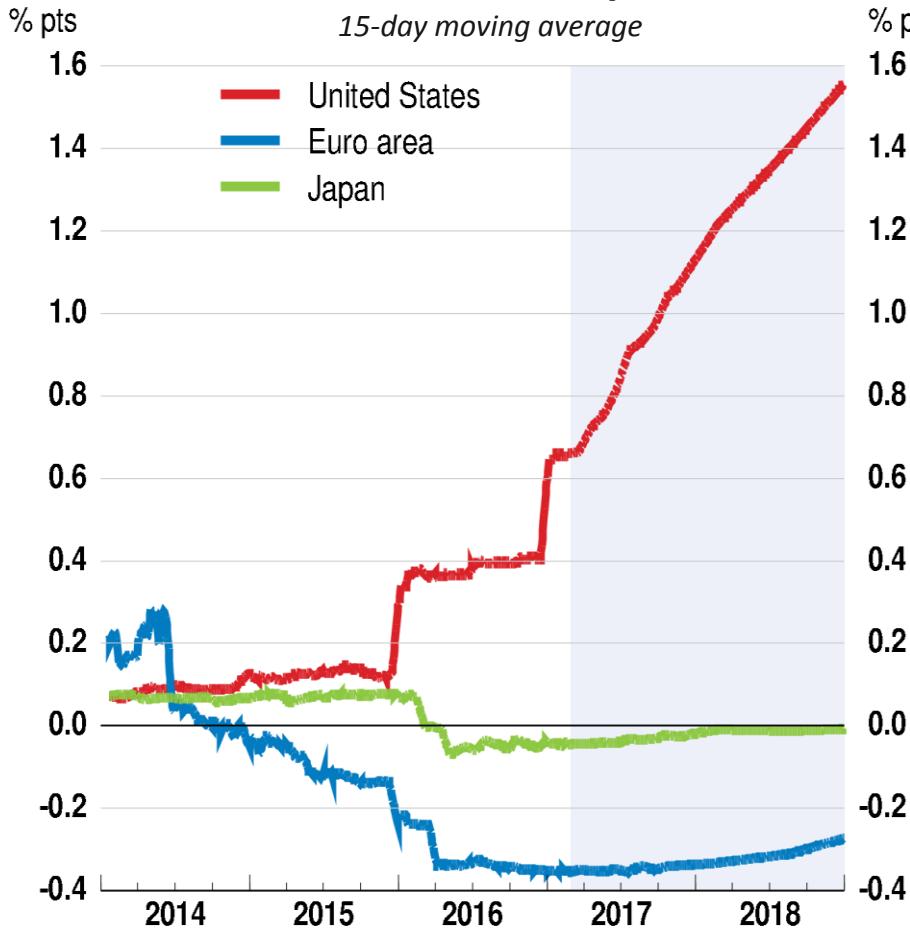
Note: Change in long-term growth and inflation expectations are the change in Consensus Economics forecasts for 2017-26 for average annual real GDP growth and CPI inflation respectively. Nominal interest rates based on 10-year government bond yields.

Source: Consensus Economics; OECD Economic Outlook database; and Thomson Reuters.

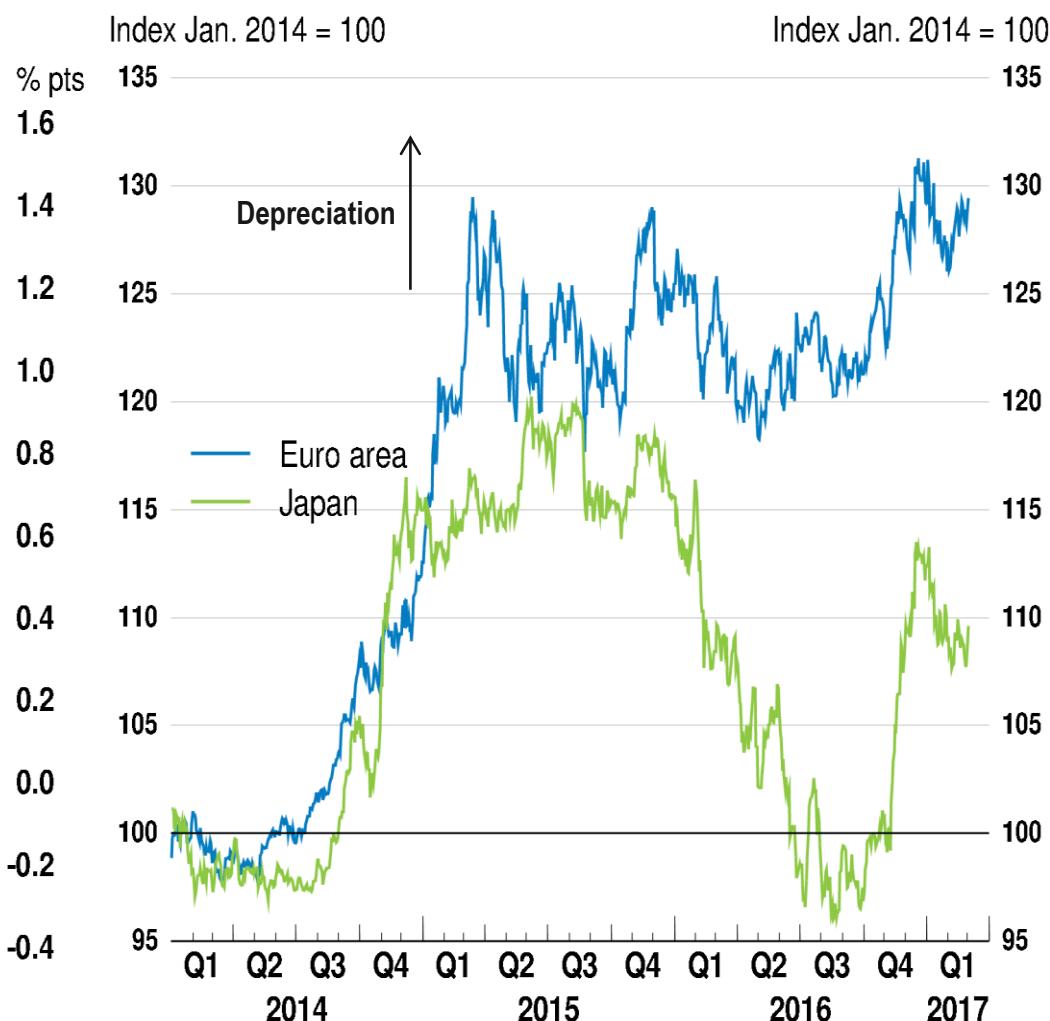


Divergence in interest rates of major economies creates risk of exchange rate volatility

Overnight interest rates: actual and market expectations



Exchange rates against USD



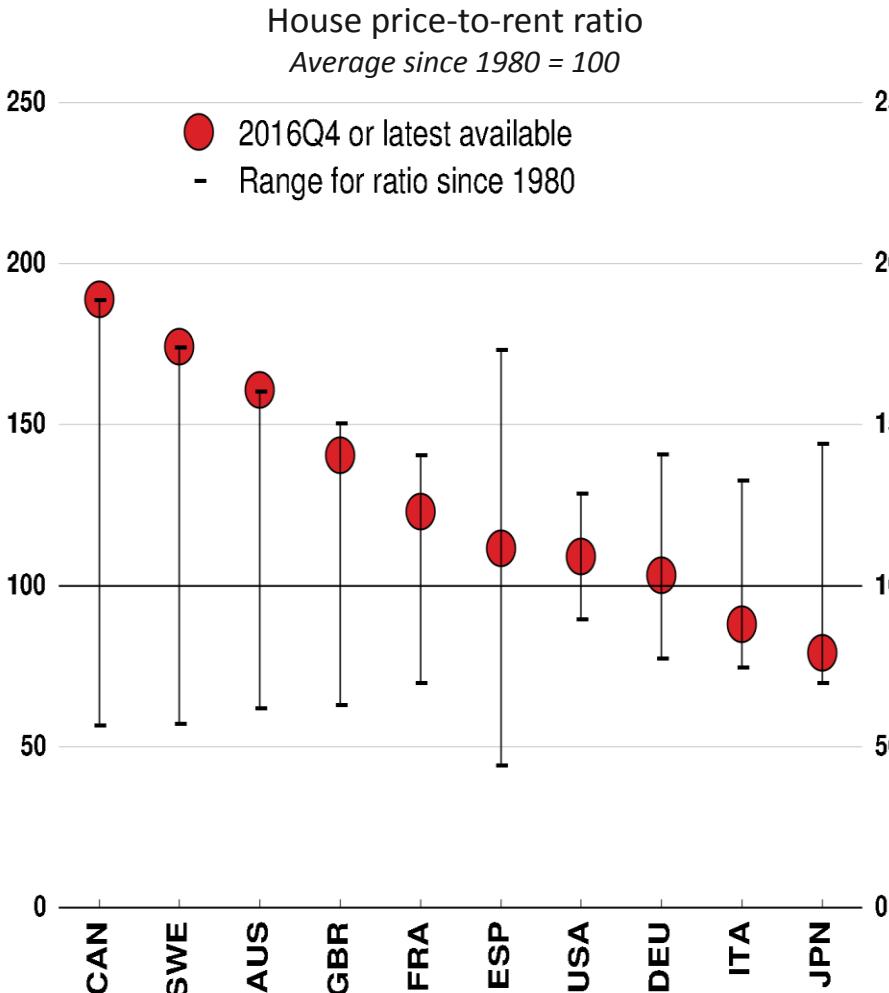
Note: Market expectations at 2 March 2017.

Source: Thomson Reuters; and OECD calculations.



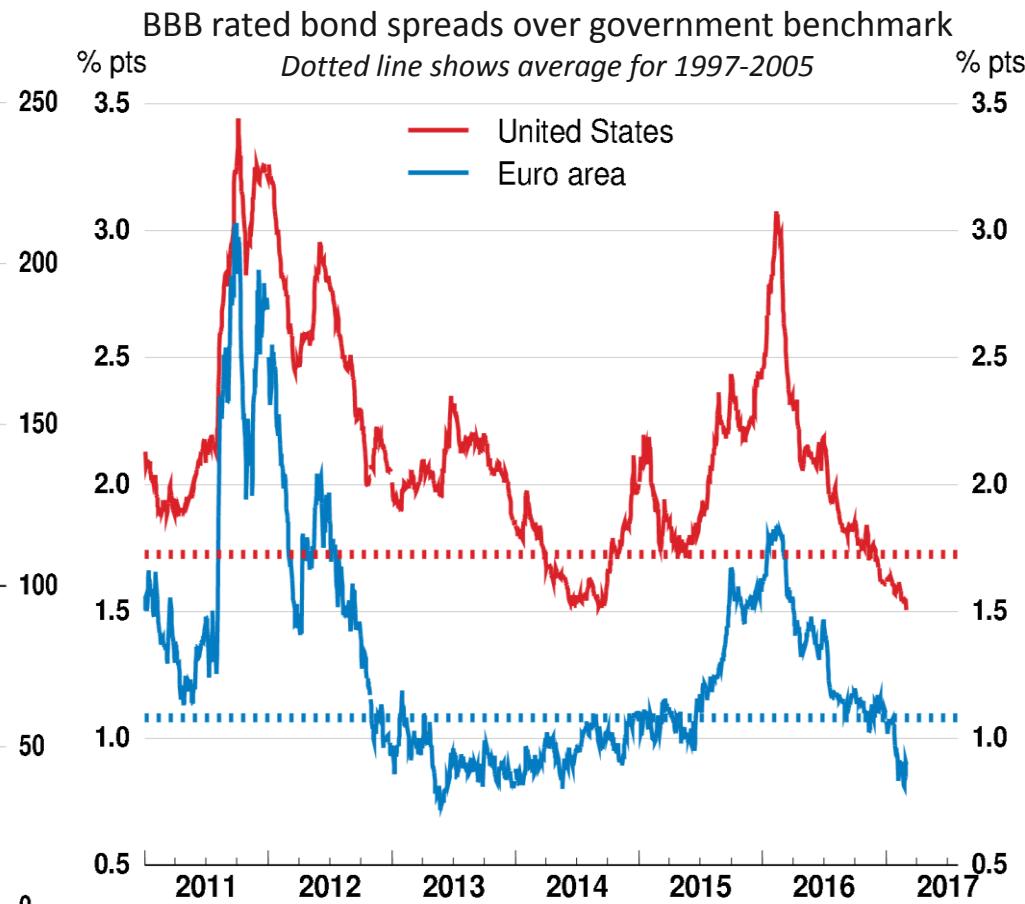
Vulnerabilities from high house prices and under-priced credit risks

House prices are high in some markets



Source: OECD Analytical House Price database.

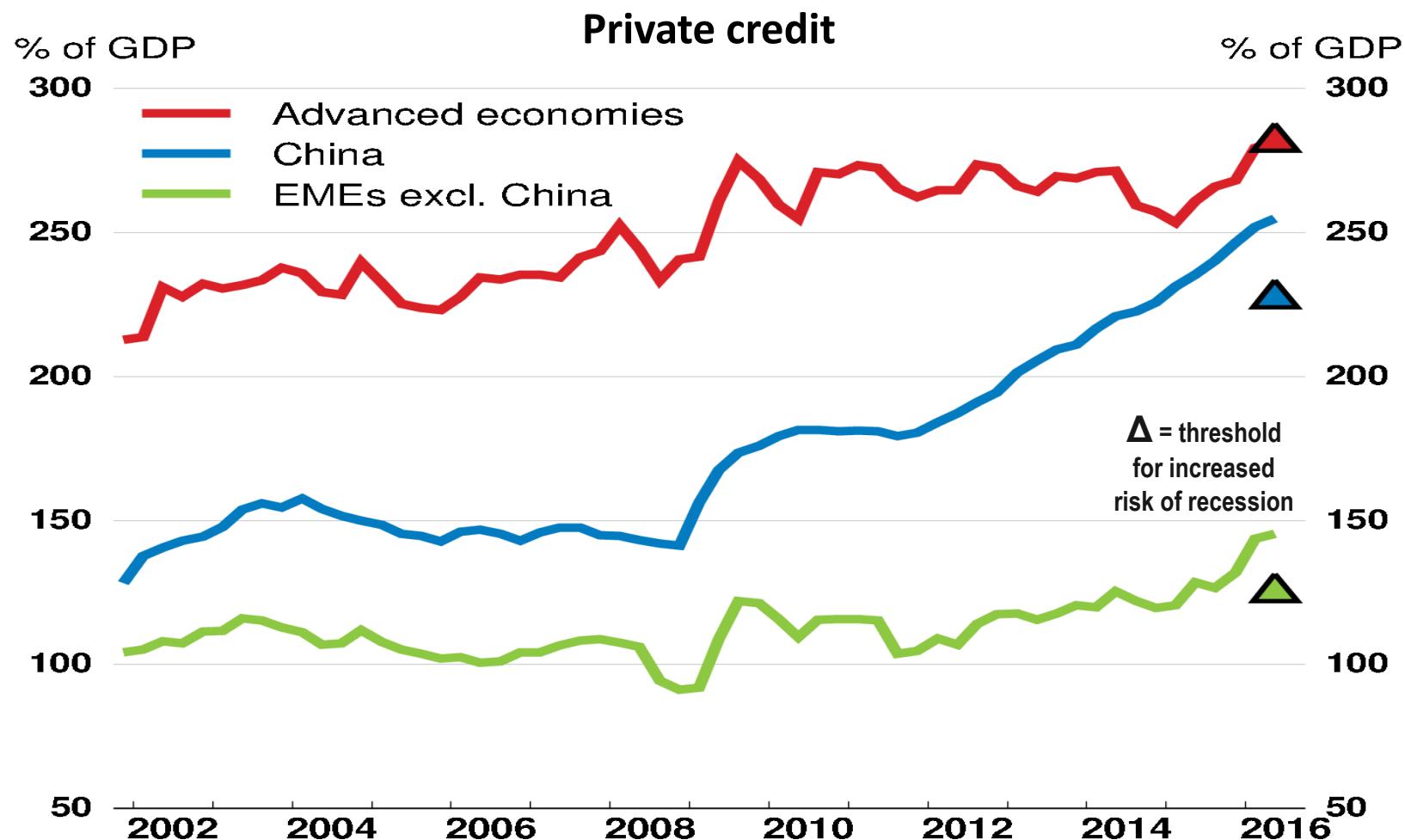
Corporate bond risks spreads are low



Note: Credit spreads between Merrill Lynch corporate BBB rated bonds and government benchmark bonds. Spreads based on average yields for 5-7 years and 7-10 years.
Source: Thomson Reuters.



Vulnerabilities from rapid increases in debt,



Note: Thresholds estimates from OECD economic resilience framework.

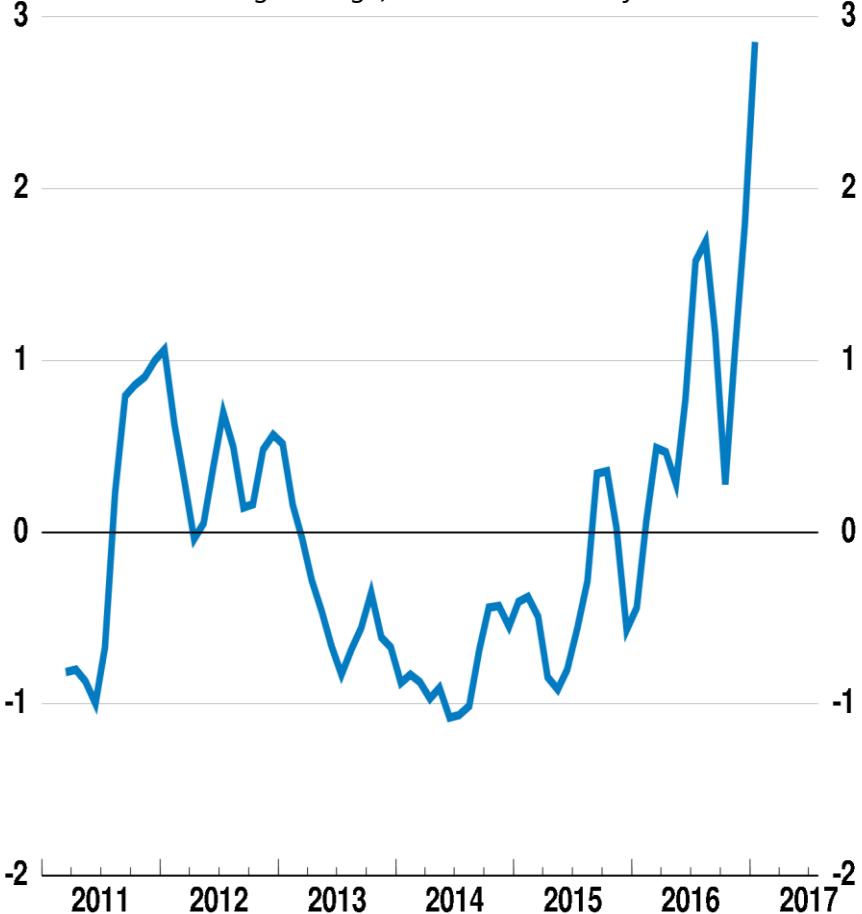
Source: BIS; China Banking Regulatory Commission; Hermansen and Röhn (2017); IMF; OECD Resilience database; and OECD calculations. See: www.oecd.org/economy/growth/economic-resilience.htm.



Inauspicious environment for policy makes reforms more difficult

Global economic policy uncertainty

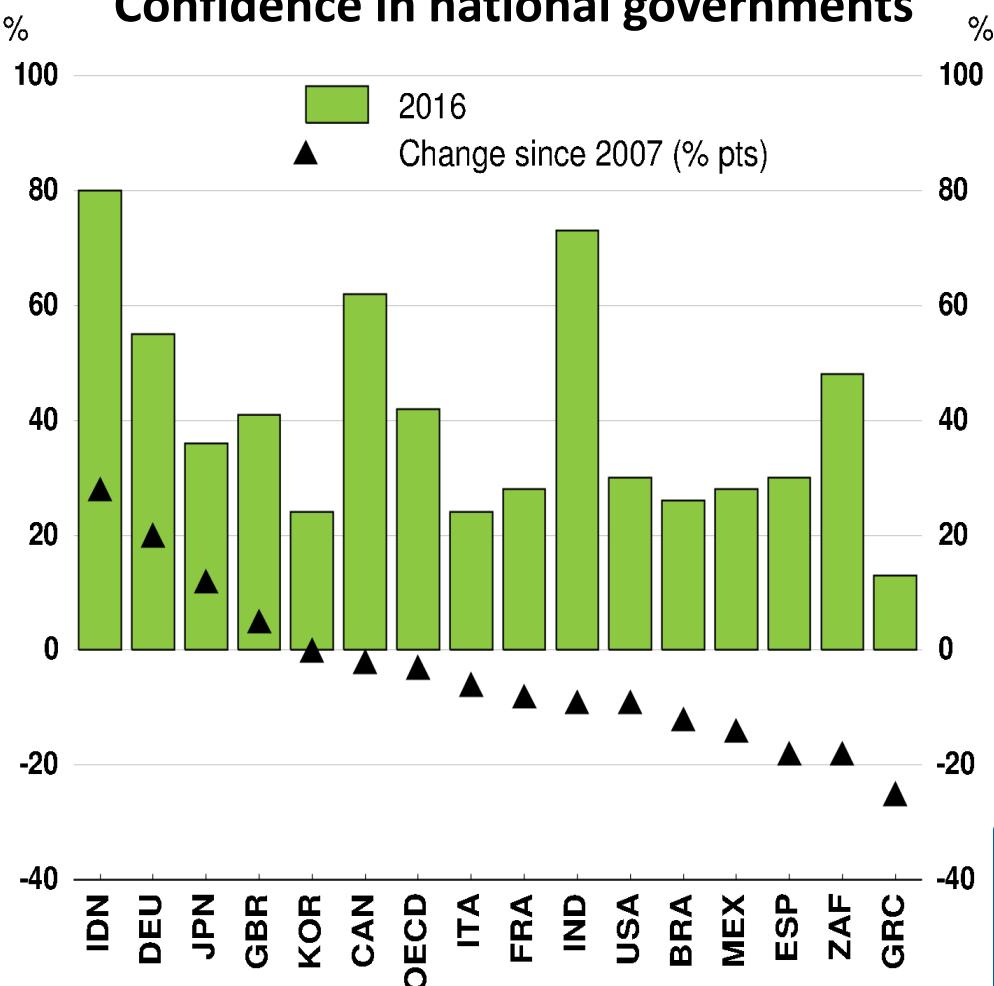
3-month moving average, index normalised for 2011-2017



Note: News-based measure of economic policy uncertainty.

Source: PolicyUncertainty.com; and OECD calculations.

Confidence in national governments



Note: Percentage who answered 'yes' to the question:

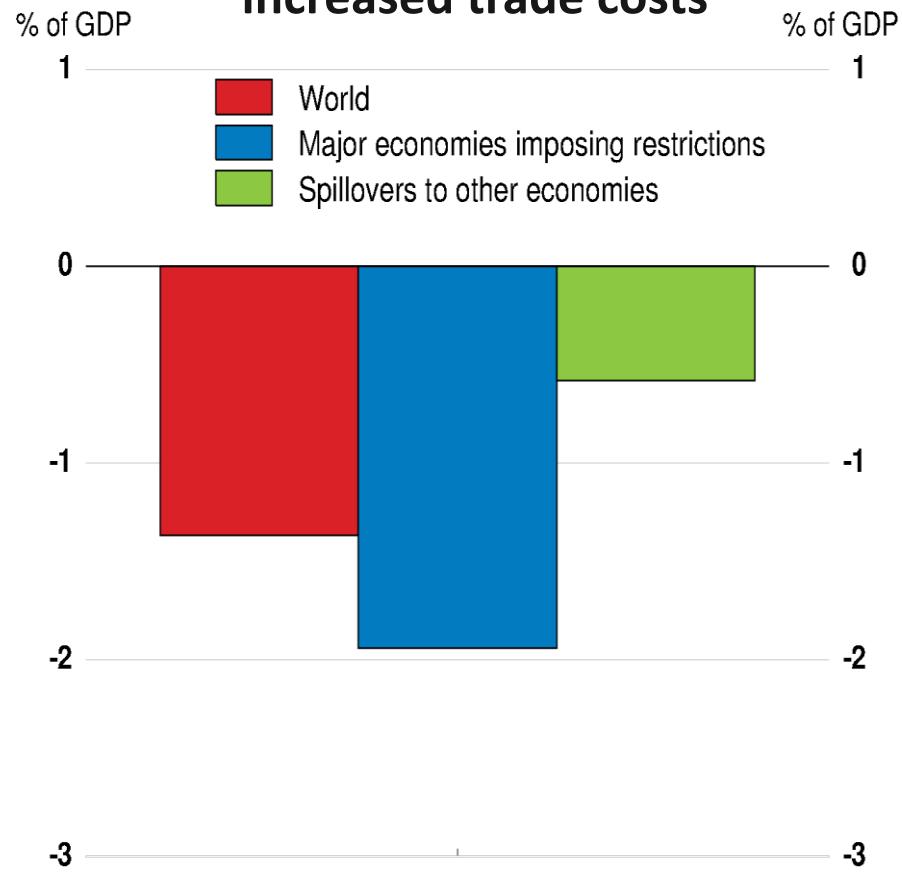
"Do you have confidence in national government?".

Source: Gallup World Poll; OECD Trust and Public Policy (2017).

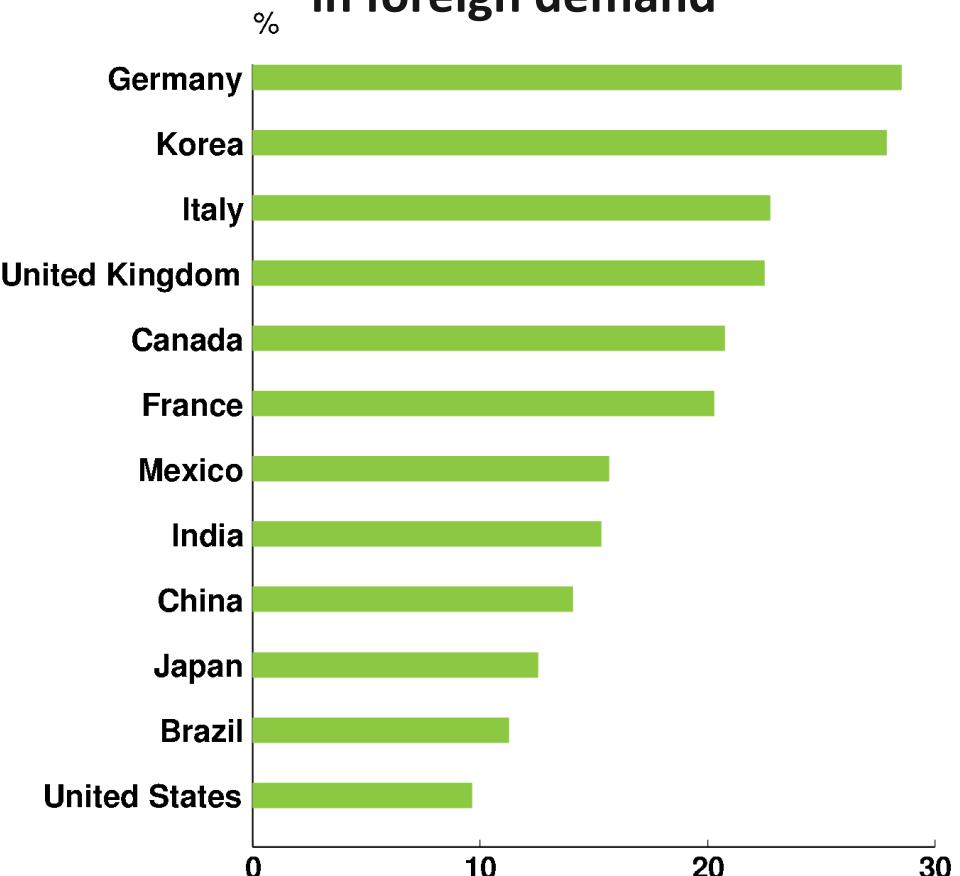


Rolling back trade openness would hurt GDP and put jobs at risk

Medium-term GDP impact of increased trade costs



Share of total employment embodied in foreign demand



Note: LHS 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, when trade negotiations under the Doha Development Round started. RHS for 2011, latest available.

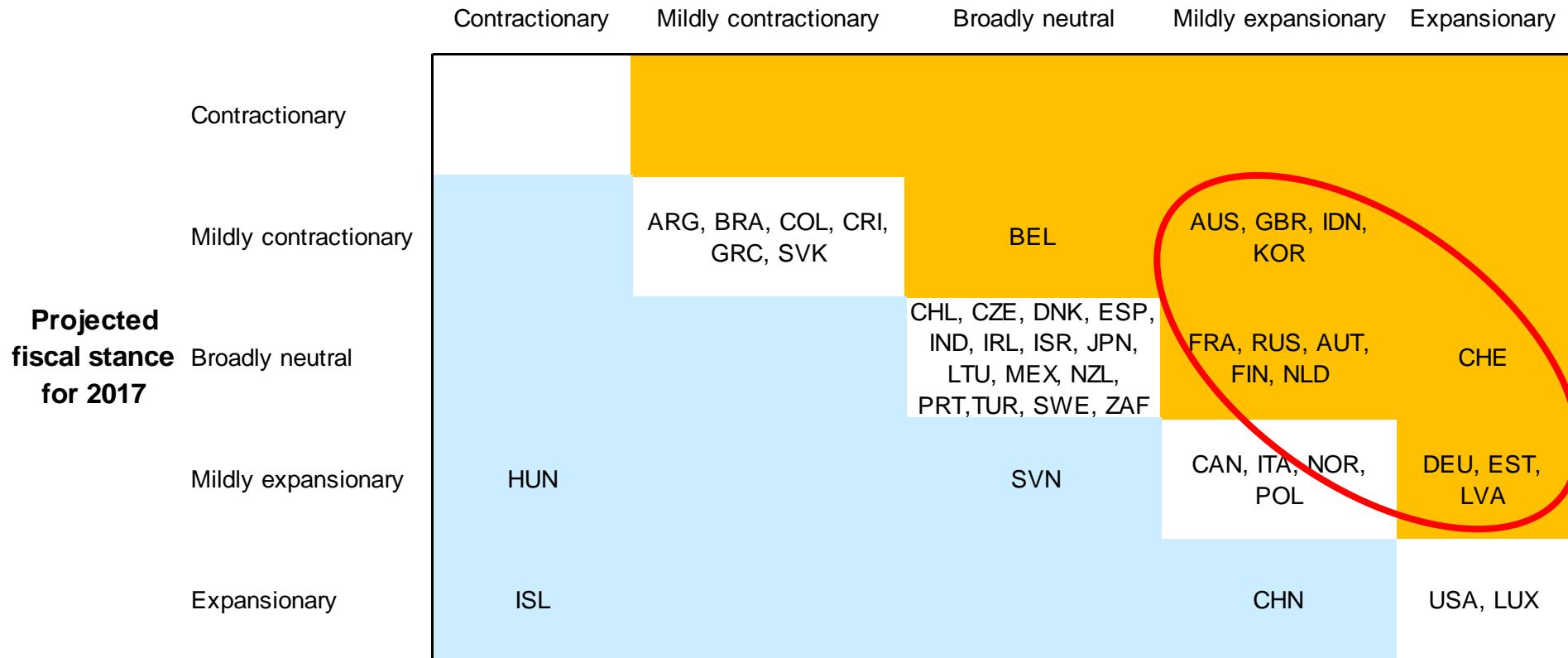
Source: OECD METRO model; OECD TiVA database; and OECD calculations.



Many countries are exploiting fiscal space, but some (esp in Europe) could do more

OECD recommends more expansionary policy than projected

Recommended fiscal stance for 2017



OECD recommends less expansionary policy than projected



Fiscal-structural initiatives to maximise impact on growth and inclusiveness

Type of structural or spending reform and impact on ...	Growth	Income of the poor	Countries with most room for gains
Improving education			CHL, GRC, MEX, PRT, TUR
Increasing public investment and R&D			DEU, GBR, ITA, MEX, TUR, USA
Increasing government effectiveness			FRA, GRC, HUN, ITA, SVN
Increasing family benefits			CHE, ESP, GRC, PRT, USA
Decreasing public subsidies			BEL, CHE



positive impact



uncertain or no impact

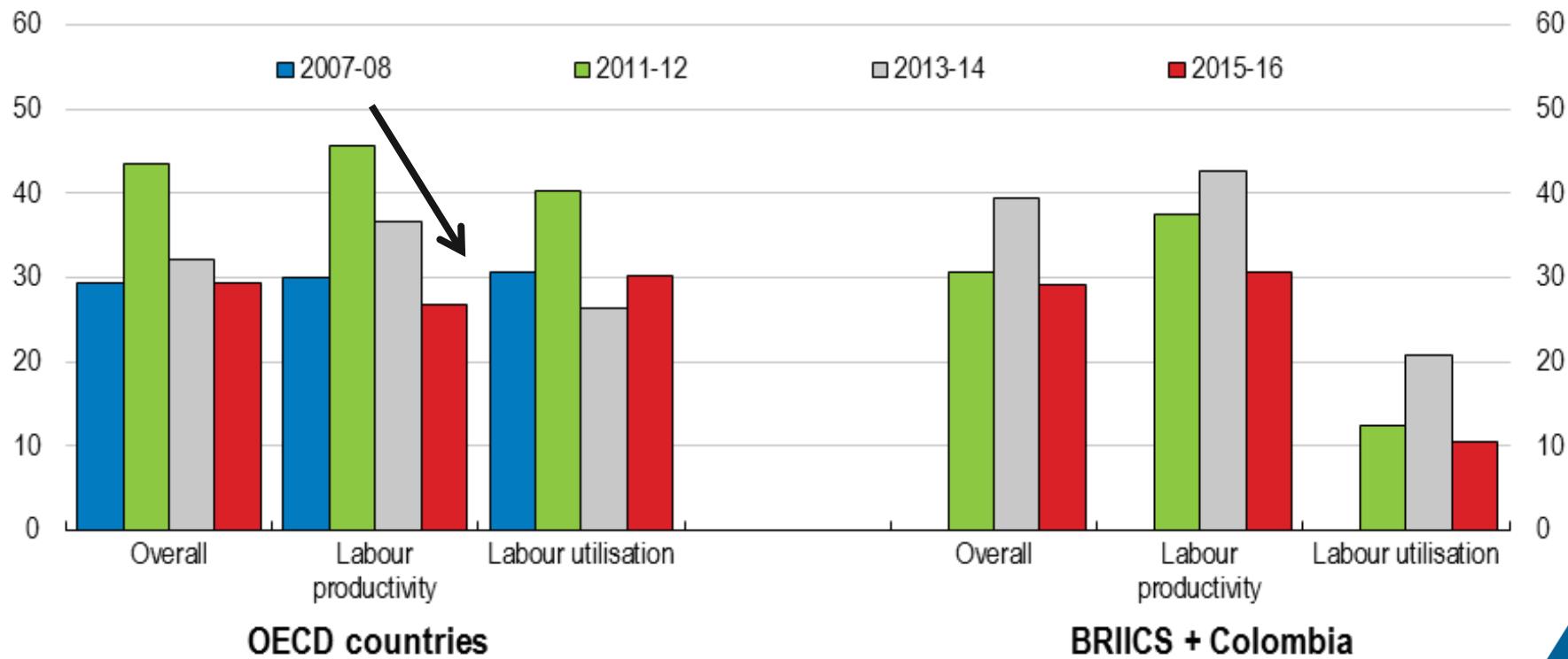
Source: Based on Fournier and Johansson (2016), "The Effect of the Size and the Mix of Public Spending on Growth and Inequality", OECD Economics Department Working Papers, No. 1344, OECD Publishing, Paris.



Lagging ambition on structural reform Particularly productivity-enhancing reforms

Indicator of number of actions taken in response to
OECD Going for Growth recommendations

Responsiveness rate

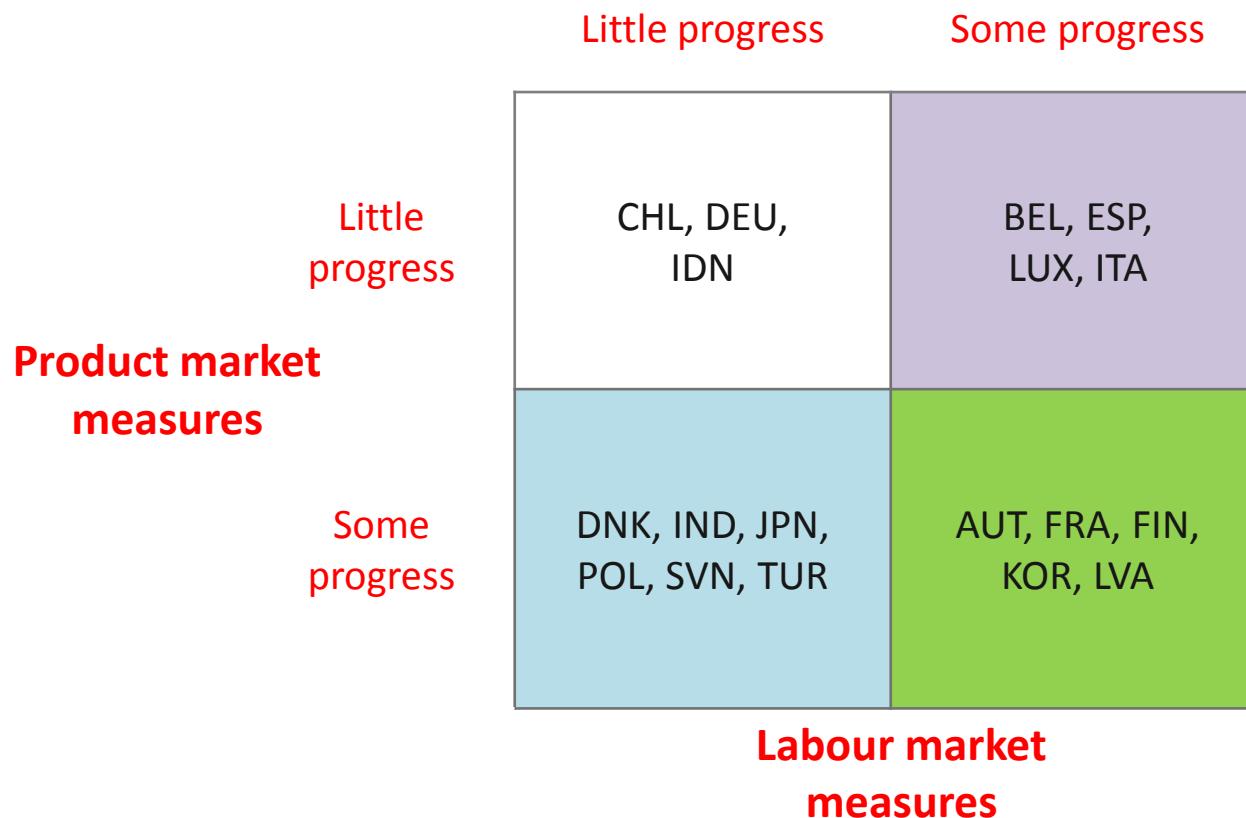




And many countries are not exploiting policy packages to deliver inclusive growth

Where are countries making complementary reforms for inclusive growth?

2015-16



Note: Reform progress based on responsiveness to *Going for Growth* recommendations by policy area. Little progress corresponds to a reform responsiveness rate of 0 to 20% and some progress for a responsiveness rate of more than 20%. Source: OECD *Going for Growth* 2017, forthcoming on March 17: www.oecd.org/eco/growth/goingforgrowth.htm.



Policy synergies can strengthen demand, supply, and inclusiveness, as well as manage risks

Address financial vulnerabilities and promote resilience

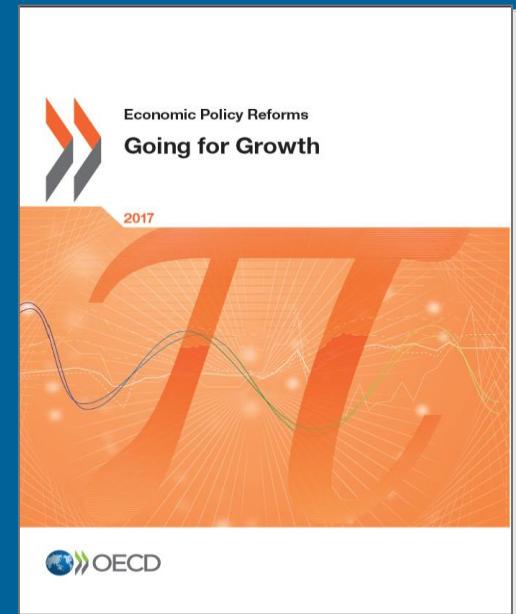
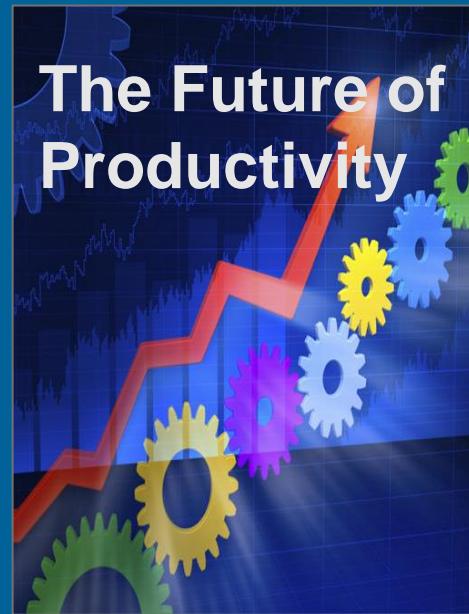
- Ensure robust early warning and recognition of risks
- Use macro-prudential, but consider growth and risk together

Implement fiscal-structural packages to boost inclusive growth

- Political commitment needed to accelerate reforms
- Fiscal initiatives of tax-transfer-structural support demand, increase supply, and promote inclusiveness
- Country-specific packages can improve labour market outcomes, business environment, and trade policies together



THANK YOU!



www.oecd.org/economy/economicoutlook.htm
www.oecd.org/global-forum-productivity
www.oecd.org/eco/growth/goingforgrowth.htm
ECOSCOPE blog: oecdecoscope.wordpress.com/