RIETI BBL Seminar
Handout

“Stronger growth remains elusive: Urgent policy response is needed”

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http://www.rieti.go.jp/jp/index.html
RIETI Seminar, Tokyo

Stronger growth remains elusive: Urgent policy response is needed

29 February 2016

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www.oecd.org/economy/economicoutlook.htm
ECOSCOPE blog: oecdecoscope.wordpress.com/
Key messages

Stronger global growth remains elusive

- Weak trade, investment, and commodity prices
- Disappointing incoming data on demand conditions
- Low inflation and poor wage growth

Financial instability risks are substantial

- Steep declines in global equity markets
- Volatile capital flows and high debt exposures in EMEs

Collective policy action is urgent

- Maintain accommodative monetary policy
- Focus supportive fiscal policies on investment-led spending
- Revive pace of productivity- and growth-enhancing structural reforms
Global growth forecasts: Revised Down

GDP forecasts

Forecast downgrades since November
## Interim Economic Outlook Forecasts

### Real GDP growth (%)

<table>
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<th>2015</th>
<th>2016</th>
<th>difference from November Economic Outlook</th>
<th>2017</th>
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<td>Rest of the World</td>
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Global demand cannot be sustained solely by the US recovery

Contributions to quarterly US GDP growth
Rebalancing in China and financial volatility are dragging on global markets

Composition of growth in China

Currency depreciation and declining reserves

USD trillion

2012
2013
2014
2015

Manufacturing (secondary)
Services (tertiary)
Services (tertiary) excluding finance
Real GDP

Yuan/USD exchange rate
Foreign exchange reserves
Commodity prices have been falling.
Significant slowdown in global trade growth

Global trade volumes and GDP

% changes

15

12

9

6

3

0

-3

-6

-9

-12


% changes

15

12

9

6

3

0

-3

-6

-9

-12

World trade

World GDP
Sluggish demand leads to low inflation and weak wage growth
Financial markets are reassessing prospects, triggering lower and more volatile equity prices.

Share prices in major markets

Volatility Index (VIX)
Risks of financial instability are substantial, particularly from emerging markets.

**Nominal effective exchange rates**

Index Jan. 2014 = 100

- Brazil
- Mexico
- Russia
- South Africa

**EMEs sovereign bond spreads**

EMBI Composite, basis points

Index Jan. 2014 = 100

Graphs showing trends in nominal effective exchange rates and EMEs sovereign bond spreads from 2014 to 2016.
Some EMEs are vulnerable to exchange rate shocks and high domestic debt.

Credit to corporations has increased

Percent of GDP

- Indonesia
- South Africa
- Brazil
- India
- Russia
- Turkey
- China

External liabilities are significant

Percent of GDP, 2014 or latest available

- Indonesia
- South Africa
- Brazil
- India
- Russia
- Turkey
- China

Legend:
- Red: Foreign-currency
- Blue: Other
A stronger collective policy response is needed
Monetary policy working alone is not sufficient to support global demand

Central bank balance sheets

United States (bn USD)
Japan (100 bn YEN)
Euro area (bn EUR)

US federal funds rate expectations

Policy rate
10 February 2016
10 September 2015

14
Fiscal policy is contractionary in many major economies, although not in China.
Interest rates are very low, providing an opportunity to borrow and invest.
Collective fiscal action promotes growth and fiscal sustainability

1st year effects of a ½ per cent of GDP public investment stimulus by all OECD economies

Change from baseline

Effect on GDP

% of GDP

USA  CAN  GBR  World

USA  CAN  GBR  BRIICS

Effect on public debt stock

% of GDP

USA  Euro  CAN  GBR
The pace of structural reforms shows insufficient ambition

Responsiveness to OECD Going for Growth recommendations

Share of recommendations implemented

- 2007-10 average
- 2011-14 average
- 2015 (implemented)
In the EU, much more progress is needed to boost investment and productivity

Juncker investment plan disappoints

- Investment planned for three years
- Estimated investment from approved projects as of January 2016

Deleveraging is needed for financial health

Household and non-financial corporate debt

- % of 2014 GDP
  - 2014 GDP: 2.5
  - Juncker investment plan: 2.0
  - United States: 1.5
  - Euro area: 2.0

- % of GDP
  - GDP: 220
  - United States: 215
  - Euro area: 210
The GDP impact of uncertainties in Europe could be great.

Change in GDP after two years

*Per cent*

- European Union: Investment decline -1.4, Investment decline and financial tensions -1.2
- World: Investment decline -1.0, Investment decline and financial tensions -0.8
- China: Investment decline -0.4, Investment decline and financial tensions -0.2
- United States: Investment decline -0.0, Investment decline and financial tensions -0.0
Global growth flat-lined due to continued subdued global trade, investment and wage growth in advanced economies

Emerging market economies’ growth models have been exposed by the slowdown in trade and falling commodity prices

Despite the boost from low oil prices and interest rates, the most likely scenario is weak global growth in 2016 and 2017

Substantial downside risks centre on financial market volatility and emerging market debt

Collective fiscal action and more ambition on structural policies would raise global growth and reduce financial risks