



ECONOMIC OUTLOOK

No. 89

Press Conference
Paris, 25 May 2011
10h30 (Paris time)

Angel Gurría
Secretary-General

&

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Deputy Secretary-General and Chief Economist

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

Summary of projections

	2010	2011	2012	2010		2011		2012				2010	2011	2012		
				Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q4 / Q4		
Percent																
Real GDP growth																
United States	2.9	2.6	3.1	2.6	3.1	1.7	3.1	2.9	3.0	3.1	3.3	3.3	3.4	2.8	2.7	3.3
Euro area	1.7	2.0	2.0	1.5	1.0	3.4	1.3	1.7	1.9	2.1	2.2	2.3	2.4	2.0	2.1	2.2
Japan	4.0	-0.9	2.2	3.8	-3.1	-3.7	-3.7	5.3	3.5	2.3	1.6	1.2	1.2	2.4	0.3	1.5
Total OECD	2.9	2.3	2.8	2.5	2.0	2.2	2.0	2.8	2.7	2.9	3.0	3.1	3.2	2.8	2.4	3.0
Inflation¹																
year-on-year																
United States	1.7	1.9	1.3	1.4	1.1	1.6	2.1	2.1	2.0	1.4	1.2	1.3	1.3			
Euro area	1.6	2.6	1.6	1.7	2.0	2.5	2.8	2.9	2.5	1.9	1.5	1.4	1.4			
Japan	-0.7	0.3	-0.2	-0.8	0.1	0.0	0.4	0.8	0.1	0.0	-0.2	-0.2	-0.2			
Total OECD	1.8	2.3	1.7	1.7	1.8	2.0	2.3	2.4	2.3	1.8	1.6	1.7	1.7			
Unemployment rate²																
United States	9.6	8.8	7.9	9.6	9.6	8.9	8.9	8.7	8.5	8.3	8.1	7.8	7.5			
Euro area	9.9	9.7	9.3	9.9	9.9	9.9	9.8	9.7	9.6	9.5	9.4	9.2	9.1			
Japan	5.1	4.8	4.6	5.0	5.0	4.7	4.8	4.8	4.7	4.7	4.7	4.6	4.5			
Total OECD	8.3	7.9	7.4	8.3	8.2	8.0	7.9	7.8	7.7	7.6	7.5	7.3	7.1			
World trade growth	12.5	8.1	8.4	8.7	5.0	9.1	6.0	9.0	8.6	8.4	8.4	8.5	8.5	11.2	8.2	8.5
Current account balance³																
United States	-3.2	-3.7	-4.0													
Euro area	0.2	0.3	0.8													
Japan	3.6	2.6	2.5													
Total OECD	-0.6	-0.7	-0.7													
Fiscal balance³																
United States	-10.6	-10.1	-9.1													
Euro area	-6.0	-4.2	-3.0													
Japan	-8.1	-8.9	-8.2													
Total OECD	-7.7	-6.7	-5.6													
Short-term interest rate																
United States	0.5	0.8	1.9	0.6	0.4	0.4	0.4	1.0	1.3	1.4	1.6	2.1	2.5			
Euro area	0.8	1.3	2.0	0.9	1.0	1.1	1.4	1.4	1.5	1.6	1.8	2.1	2.3			
Japan	0.2	0.3	0.2	0.1	0.1	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2			

Note: Real GDP growth, inflation (measured by the increase in the consumer price index or private consumption deflator for total OECD) and world trade growth (the arithmetic average of world merchandise import and export volumes) are seasonally and working-day (except inflation) adjusted annual rates. 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 19 May 2011.

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 89 database.

Country projections

Annual real GDP growth, in per cent

	2010	2011	2012
Australia	2.6	2.9	4.5
Austria	2.1	2.9	2.1
Belgium	2.1	2.4	2.0
Canada	3.1	3.0	2.8
Chile	5.1	6.5	5.1
Czech Republic	2.2	2.4	3.5
Germany	3.5	3.4	2.5
Denmark	2.1	1.9	2.1
Estonia	3.1	5.9	4.7
Finland	3.1	3.8	2.8
France	1.4	2.2	2.1
Greece	-4.5	-2.9	0.6
Hungary	1.0	2.7	3.1
Ireland	-1.0	0.0	2.3
Iceland	-3.5	2.2	2.9
Israel	4.7	5.4	4.7
Italy	1.2	1.1	1.6
Japan	4.0	-0.9	2.2
Korea	6.2	4.6	4.5
Luxembourg	3.5	3.2	3.9
Mexico	5.5	4.4	3.8
Netherlands	1.8	2.3	1.9
Norway	0.4	2.5	3.0
New Zealand	2.5	0.8	4.1
Poland	3.8	3.9	3.8
Portugal	1.3	-2.1	-1.5
Slovak Republic	4.0	3.6	4.4
Slovenia	1.2	1.8	2.6
Spain	-0.1	0.9	1.6
Sweden	5.3	4.5	3.1
Switzerland	2.6	2.7	2.5
Turkey	8.9	6.5	5.3
United Kingdom	1.3	1.4	1.8
United States	2.9	2.6	3.1
Brazil	7.5	4.1	4.5
China	10.3	9.0	9.2
India	10.4	8.5	8.6
Indonesia	6.1	6.6	6.4
Russian Federation	4.0	4.9	4.5
South Africa	2.8	3.9	4.2

Source: OECD Economic Outlook 89 database.

EDITORIAL

Seeking a durable recovery for all

The global recovery is becoming self-sustained and more broad based. The recovery is taking place at different speeds, between advanced and emerging economies, but also within the first group of countries. Unemployment remains high across most of the OECD countries. In most, headline inflation has risen strongly, and expectations are also drifting up; however, underlying inflation seems likely to edge up only slowly. Vibrant domestic demand growth, negative supply shocks and strong capital inflows in non-OECD economies are generating inflationary pressures prompting policy restraint that could slow the recovery.

Such a scenario calls for differentiated policy responses in advanced and emerging economies. In both groups of countries structural reforms should play a key role while taking into account country-specific needs and institutional features. In advanced economies, structural reforms can boost potential growth, thereby facilitating fiscal consolidation and easing the pace of monetary policy normalization. In emerging economies, monetary policy should tighten more to curb inflation, but this option risks being constrained by inducing stronger capital inflows. In emerging economies structural reforms could make growth more sustainable and inclusive, while contributing to global rebalancing and enhancing long-term capital flows.

The outlook is surrounded by risks. Some of them are endogenous to the pace of expansion; others are associated with the possibility of specific events. Upside risks include unexpected short-term stimulus from additional structural measures and more buoyant private-sector activity as confidence increases. Some of the risks are two-sided. Oil prices may rise or fall back over the projection period. While the earthquake and tsunami in Japan could have additional negative consequences on activity further reconstruction packages could hasten the rebound. Most risks are on the downside, however, including: further increases in oil and other commodity prices which could feed into core inflation, a deeper slowdown in China, an unsettled fiscal situation in the United States and Japan and renewed weakness in housing markets. Financial vulnerabilities are increasing in the euro area in spite of strong adjustment efforts in peripheral countries. A concern is that, if downside risks interact, their cumulative impact could weaken the recovery significantly, possibly triggering stagflationary developments in some advanced economies.

All this suggests that the global crisis may not be over yet. Policy makers must intensify efforts to deal with medium-term challenges. Four such challenges stand out: dealing with high unemployment and preventing it from becoming entrenched; sustaining growth and avoiding stagnation; making progress in fiscal consolidation; and managing global imbalances while supporting orderly saving reallocation. These challenges are interconnected and require a comprehensive and credible policy approach.

While the recovery is bringing some improvements in labour market conditions in advanced economies, total, and especially long-term, unemployment remains high in many countries. Also drawing on lessons from the crisis, labour market policies have a key role to play in preventing cyclical unemployment from turning structural. Such policies could include more effective placement services with training to match workers and jobs; rebalancing employment protection towards temporary workers; and temporary reduction in labour taxation through well targeted marginal job subsidies in countries where labour demand is weak. The employment impact of such measures would be boosted by stronger competition in

sectors such as retail trade and professional services. Moreover, the crisis has demonstrated the utility of well designed work-sharing arrangements in minimizing employment loss during downturns.

Return to work and competition-enhancing measures would also contribute to stronger potential growth, which could otherwise remain weak. Indeed, as experience shows, following financial crises there are risks of stagnation as structural adjustment and financial repair are delayed. Stagnation could also emerge from persistent deterioration of the structural and business environment. Even if such risks do not materialise the impact of the crisis in lowering potential output is becoming clearer. Such permanent output loss could, eventually, lower realised growth rates. The potential for growth-enhancing structural reforms and policies to unleash new sources of growth is substantial. Governments should intensify their efforts in implementing them.

Lower growth would feed back negatively on fiscal consolidation, while evidence shows that, beyond some thresholds, public debt levels have a negative impact on growth. In spite of some improvement in fiscal positions, consolidation requirements to merely stabilise debt are substantial for many countries. The United States and Japan, for which such requirements are among the largest, have yet to produce credible medium-term plans while other countries need to bolster medium-term fiscal targets by specifying the measures that will be implemented to achieve them. For most countries, further action would be needed to bring debt levels back to pre-crisis levels. The overall scenario has changed with respect to the pre-crisis situation when a significant contribution to fiscal sustainability came from the fact that interest rates were well below growth rates. This is unlikely to be the case in the years to come as interest rates will rise and growth could be slower. Structural reforms, while boosting growth, can also help fiscal consolidation by increasing efficiency in the provision of key services such as health and education. Finally, it would be dangerous to believe that higher inflation could address debt sustainability. Higher and persistent inflation could damp real growth by raising price and exchange-rate volatility. It could also risk unhinging inflation expectations, with the result that interest rates would soon increase more than inflation.

Last but not least, imbalances have been widening again as the global economy is recovering. They show, however, a somewhat different configuration as China's current account surplus is well below pre-crisis peaks due to adverse terms-of-trade movements and less buoyant export performance, and high-saving oil-producing economies see mounting surpluses. A desirable rebalancing mechanism should be growth-enhancing and sufficiently symmetric to avoid putting an excessive burden on deficit countries. Such a rebalancing would require more exchange-rate flexibility, which could also help mitigate inflationary pressures in countries where these are strong, while country-specific structural reforms could help to reduce saving and raise investment in surplus countries, and boost saving in deficit countries. In monetary unions, competition-enhancing reforms of labour and product markets could also facilitate adjustments in external positions.

The policy challenge is not to eliminate imbalances but to keep them sustainable, so as to facilitate international reallocation of savings in ways that are supportive of growth. This requires open and long-term-oriented capital markets. Structural policies have an important impact on size and composition of capital movements. At the same time there is a need to reconcile open capital markets with the goal of coping with short-term instability through temporary measures. It is important that, including under the auspices of the G20, advanced and emerging economies agree on a framework that would allow such goals to be reconciled.

The global economy is exiting the recession but is not returning to business as usual. The post-crisis economy will have to deal with old and new challenges, while pursuing new, green and inclusive sources of growth. This requires rethinking the policy paradigm as we draw lessons from the crisis.

In framing the new, post-crisis policy paradigm, some of the existing principles underlying policy should be confirmed, such as those related to supply-side responses to boost growth, while recognizing that such policies have additional positive effects on rebalancing and fiscal consolidation. The assignment of monetary policy to achieve price stability and a rule-based fiscal policy to achieve sustainable public finances should be confirmed, while the contribution of fiscal institutions to fiscal discipline could be further explored. But additional lessons should be drawn. The endogenous generation of instability and imbalances out of (apparent) tranquillity, a phenomenon common to several if not all crisis episodes, has been dangerously overlooked. This reinforces the need for financial-sector reform and tighter prudential policies, both at the micro and macro levels.

Finally, as a more complex world than what we believed to be the case requires a broader policy tool kit, we also need to take a closer look at how such tools interact and what can be done to enhance synergies. In this vein another lesson from the crisis is that international cooperation is important both in dealing with emergency situations and in shaping the way forward. This requires agreement on common principles, and, if necessary, common rules, while allowing for country-specific needs. As we slowly leave the crisis behind us, we should be wary of the risk of losing impetus in the search for better global economic governance.

25 May 2011

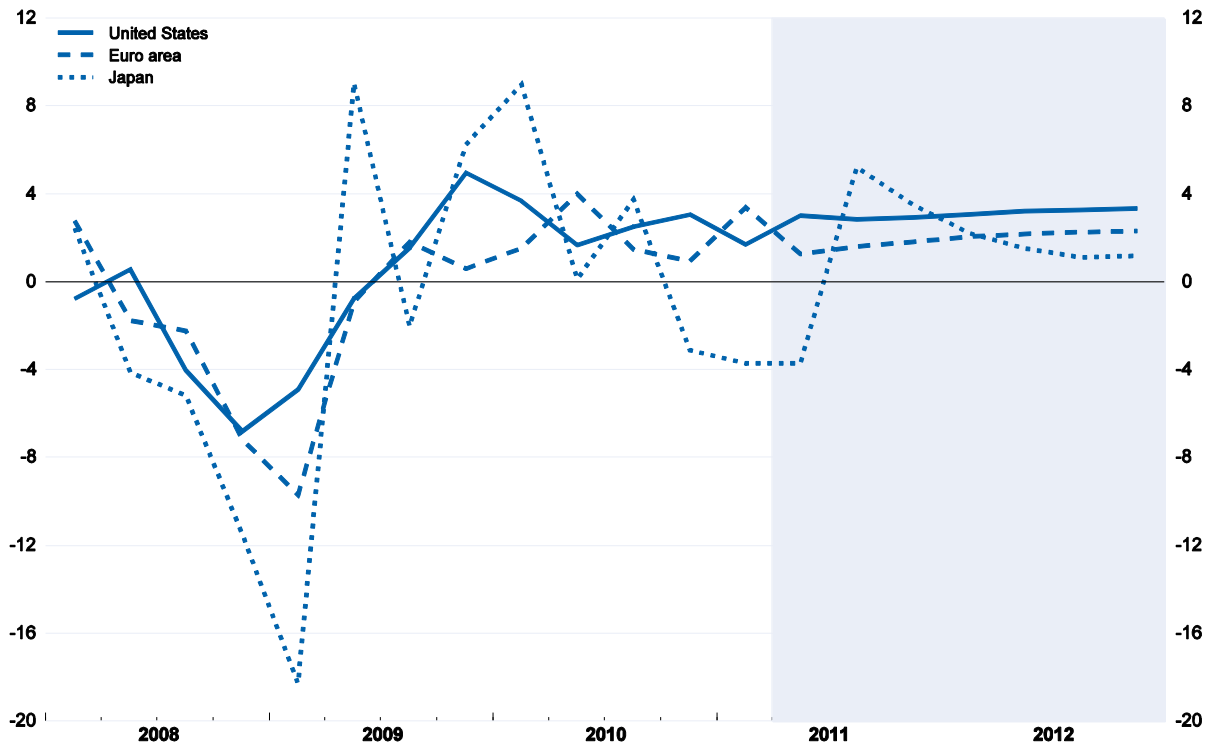
A handwritten signature in black ink, appearing to read 'Pier Carlo Padoan', written in a cursive style.

Pier Carlo Padoan

Deputy Secretary-General and Chief Economist

The recovery is firming

Annualised quarterly real GDP growth, in per cent

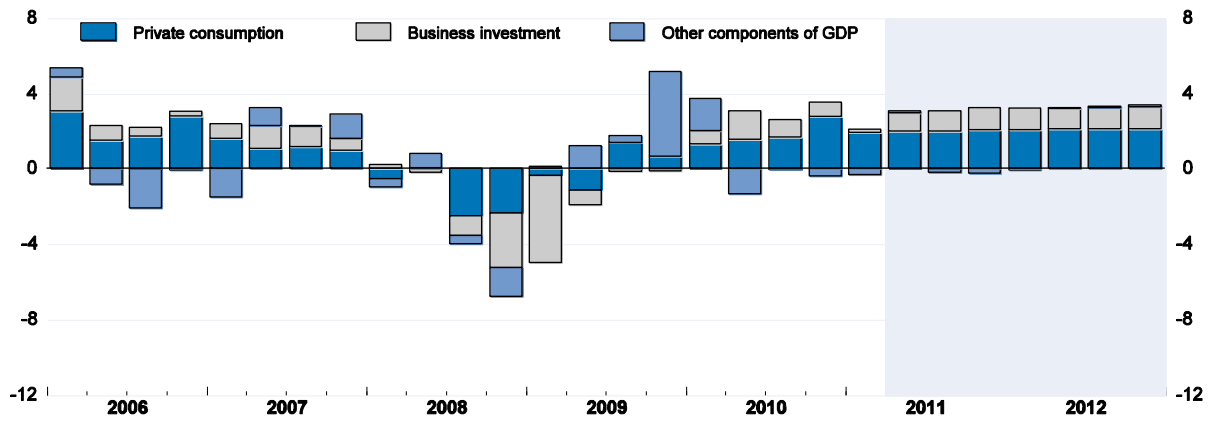


Source: OECD Economic Outlook 89 database.

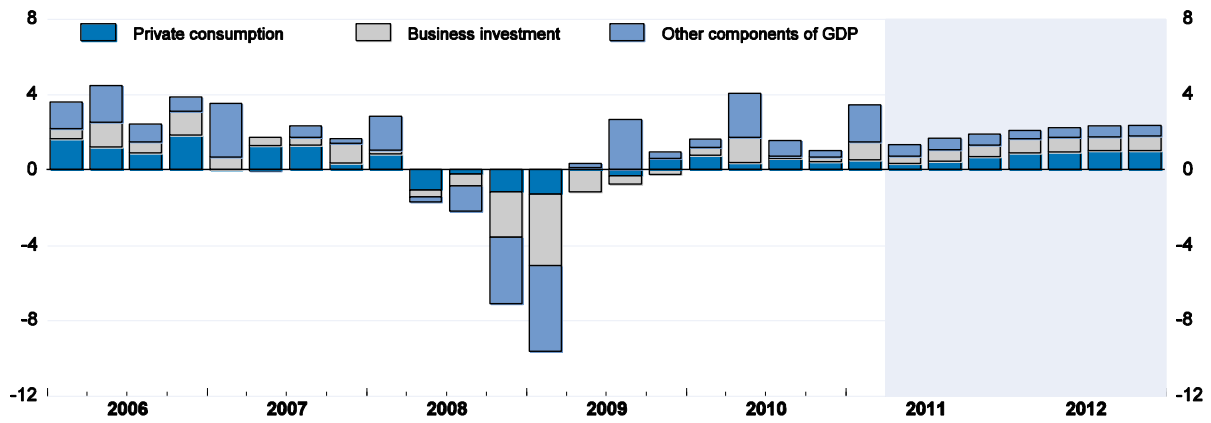
Growth is becoming self-sustained

Contributions to annualised quarterly GDP growth, percentage points

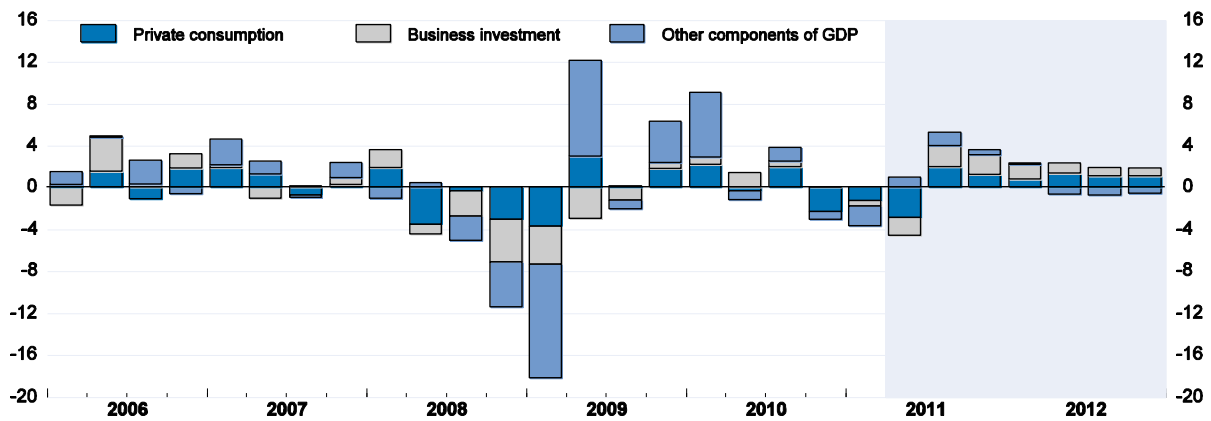
United States



Euro area



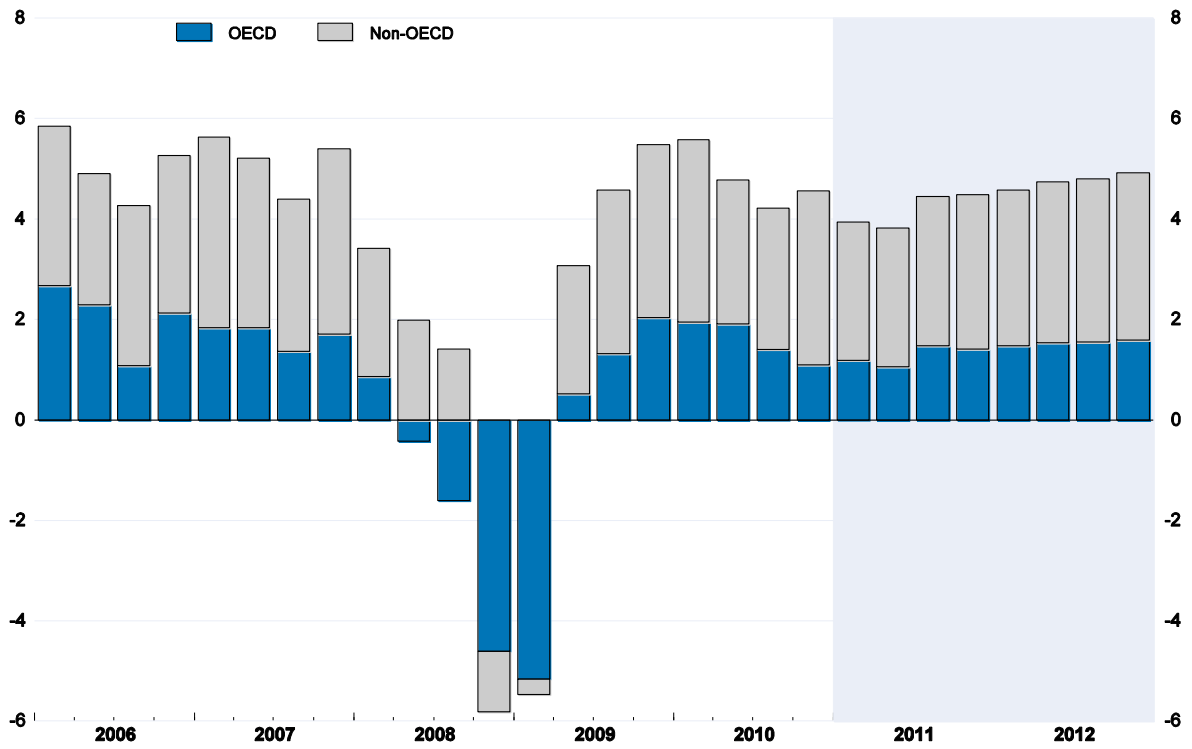
Japan



Source: OECD Economic Outlook 89 database.

Global growth continues be led by the non-OECD economies

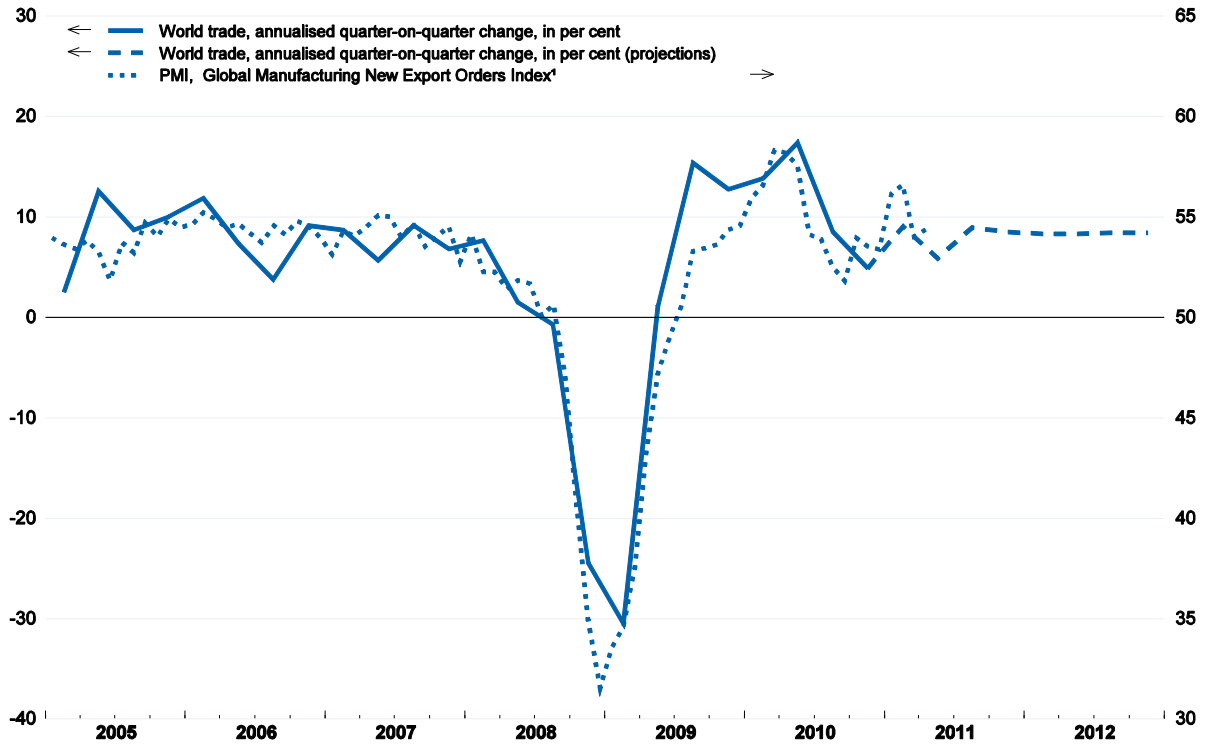
Contribution to annualised quarterly world real GDP growth, percentage points



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

Source: OECD Economic Outlook 89 database.

World trade is normalising

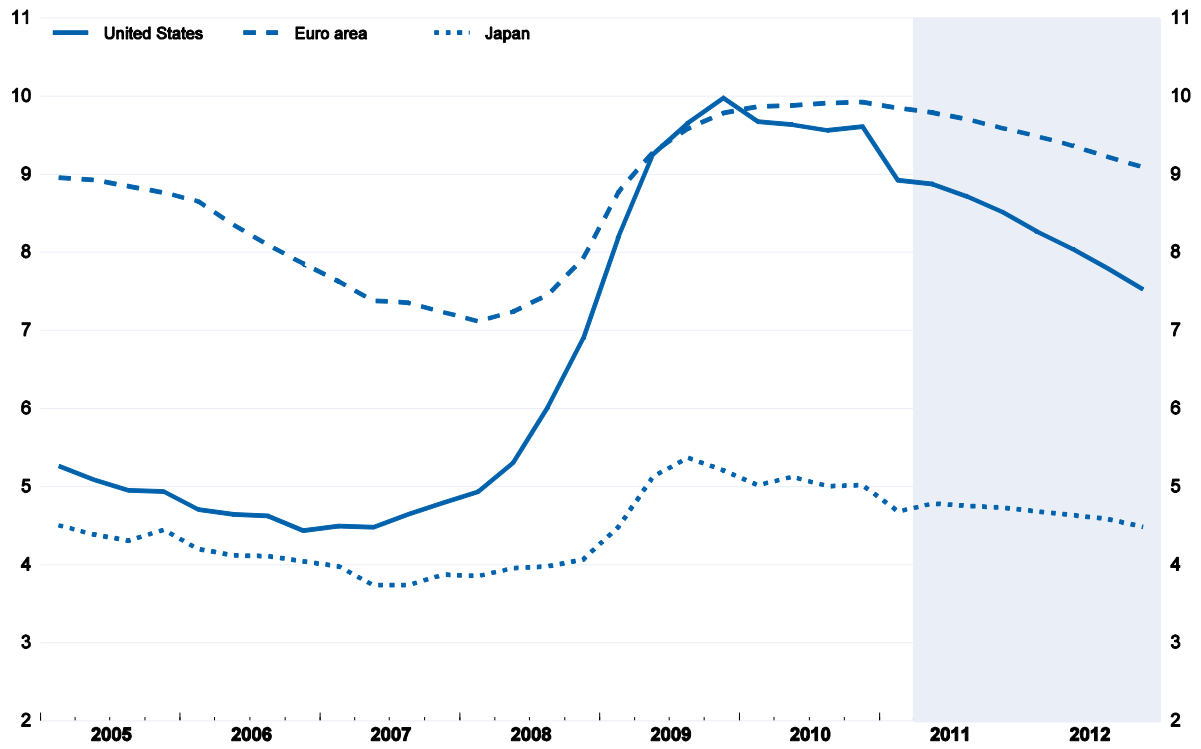


1. Value greater than 50 signifies an increase in new export orders.

Source: OECD Economic Outlook 89 database; and Markit Economics Limited.

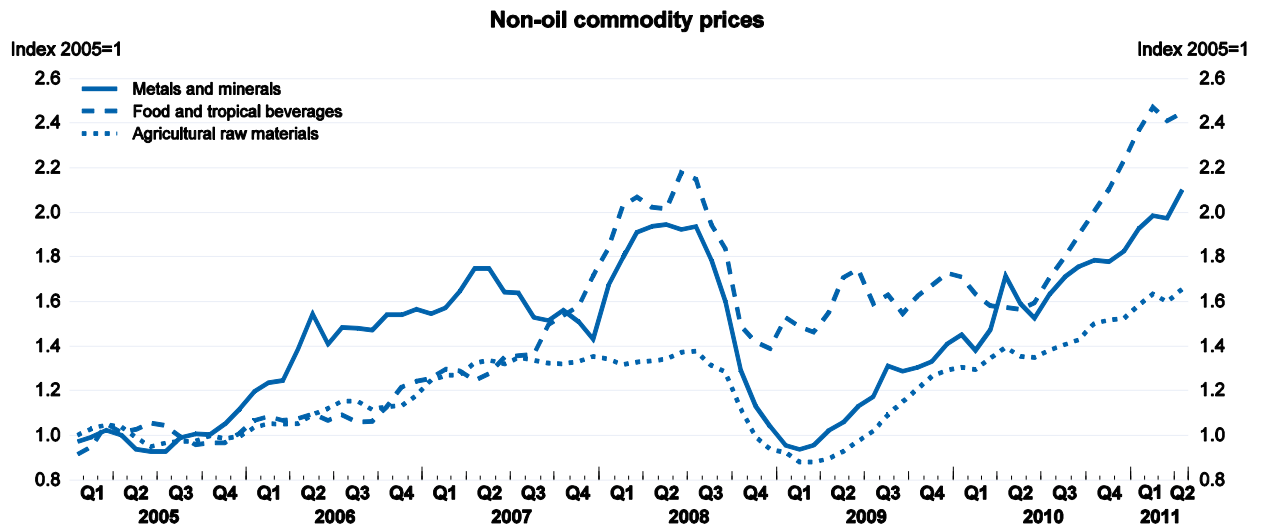
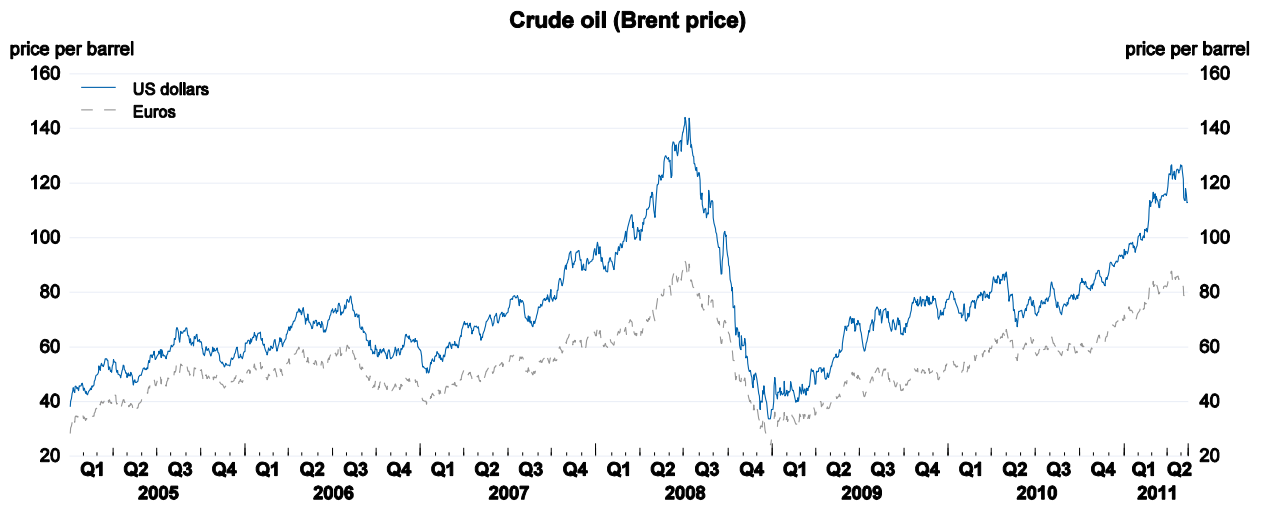
Unemployment rates are now declining but remain high

Percentage of labour force



Source: OECD Economic Outlook 89 database.

Commodity prices have surged

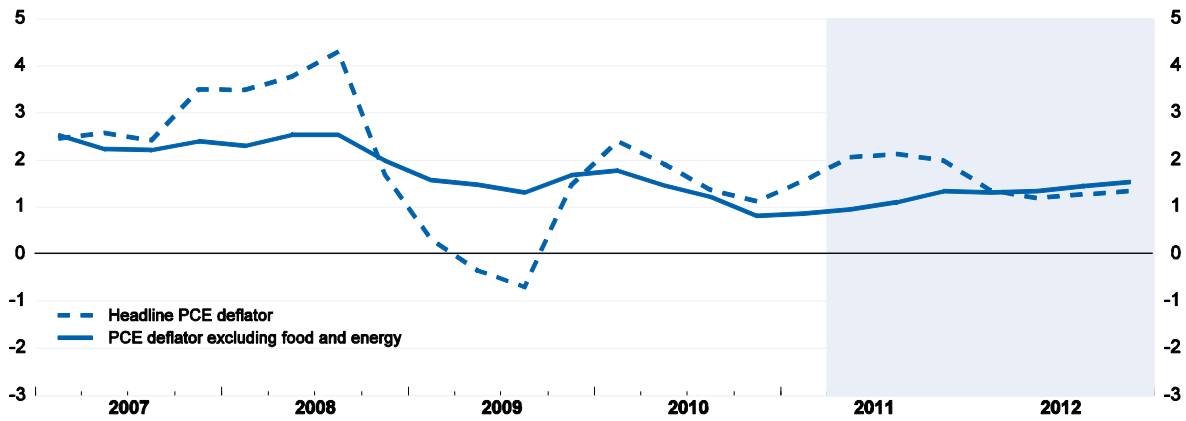


Source: OECD, Main Economic Indicators database; and Datastream.

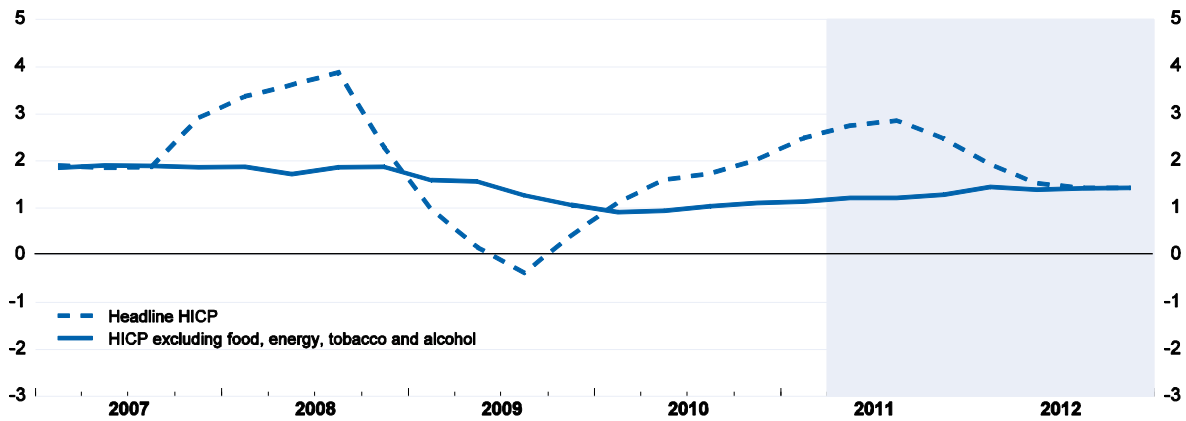
Underlying inflation is edging up from low rates

4-quarter percentage change

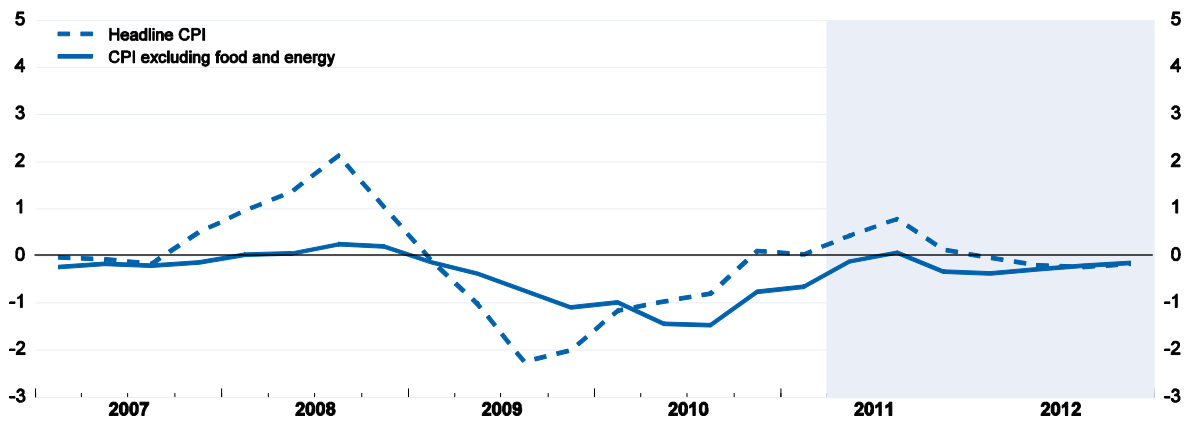
United States



Euro area



Japan

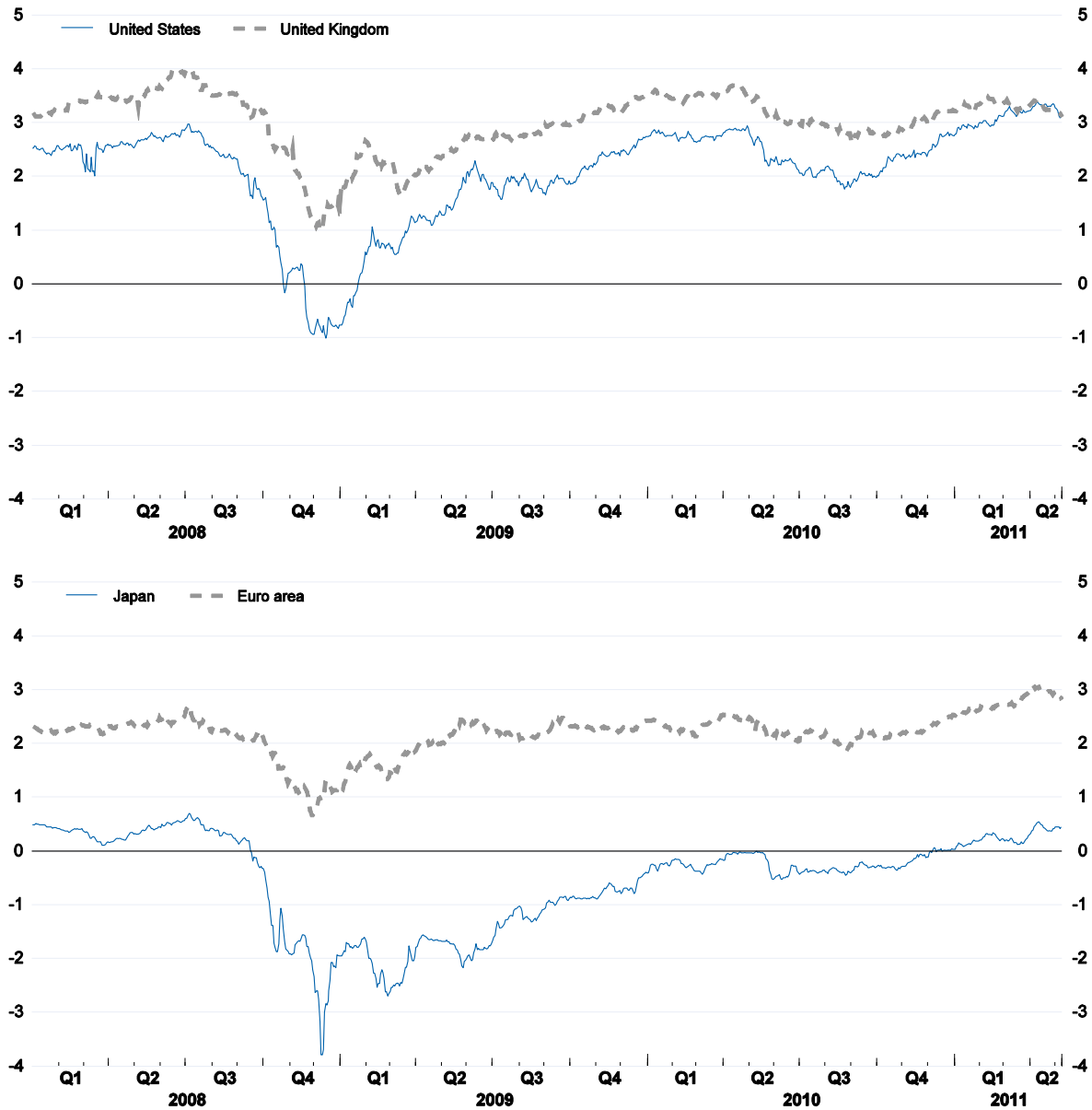


Note: PCE deflator refers to the deflator of personal consumption expenditures, HICP to the harmonised index of consumer prices and CPI to the consumer price index.

Source: OECD Economic Outlook 89 database.

Long-term inflation expectations are trending upwards in some countries

Based on bond yield differentials, percentage points

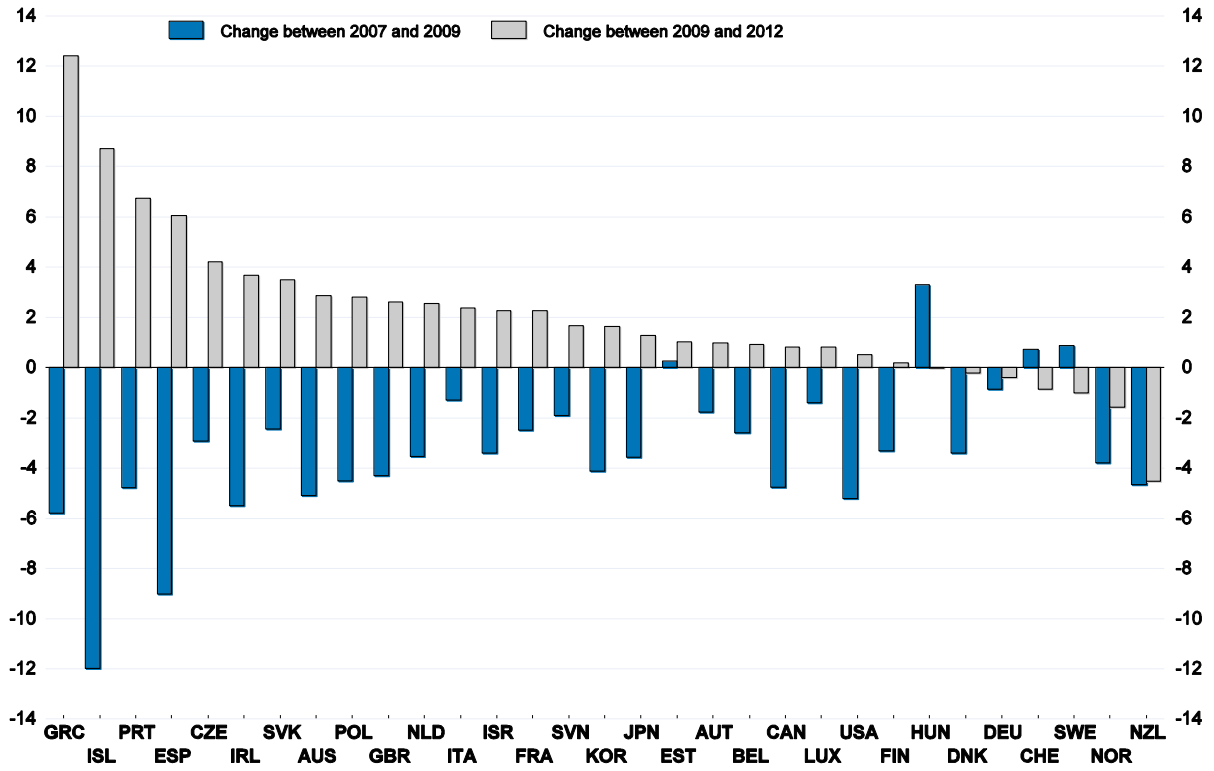


Note: Yield differential between 10-year government benchmark and inflation-indexed bonds (Merrill Lynch series).

Source: Datastream.

Fiscal policy is shifting from stimulus to tightening

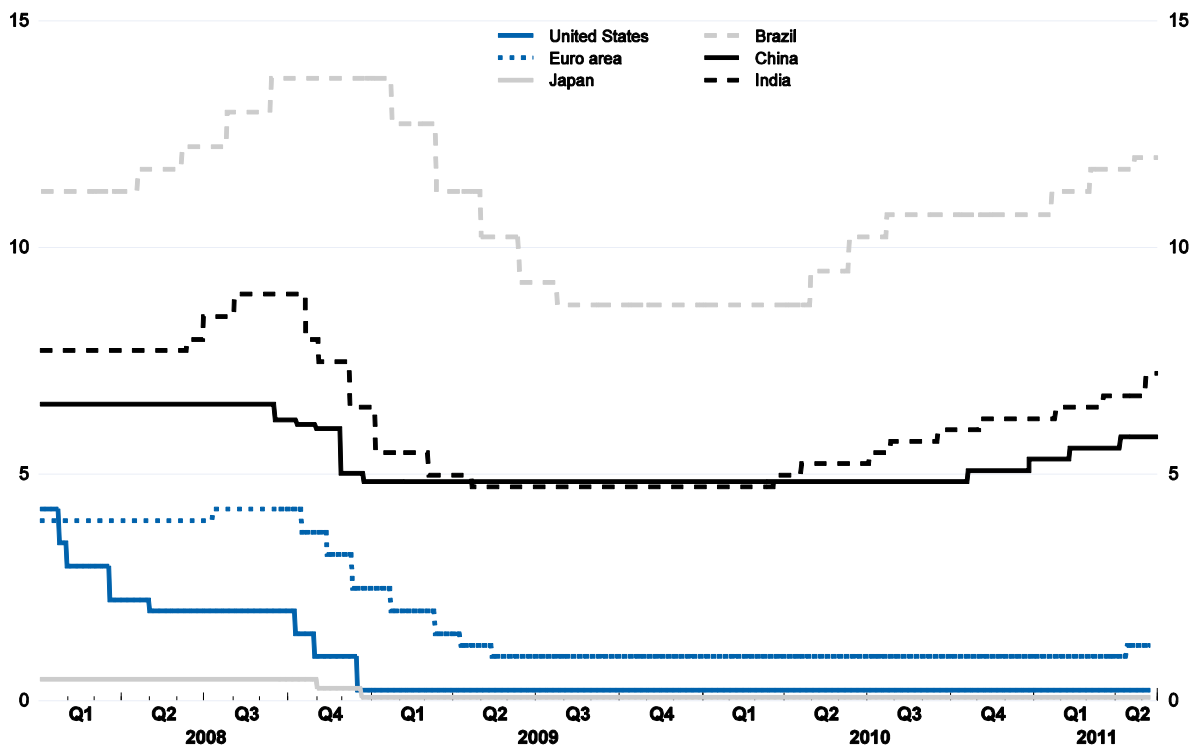
Change in underlying budget balance, in per cent of potential GDP



Source: OECD Economic Outlook 89 database.

Monetary policy is tightening in emerging-market economies

Policy interest rates, percentage points

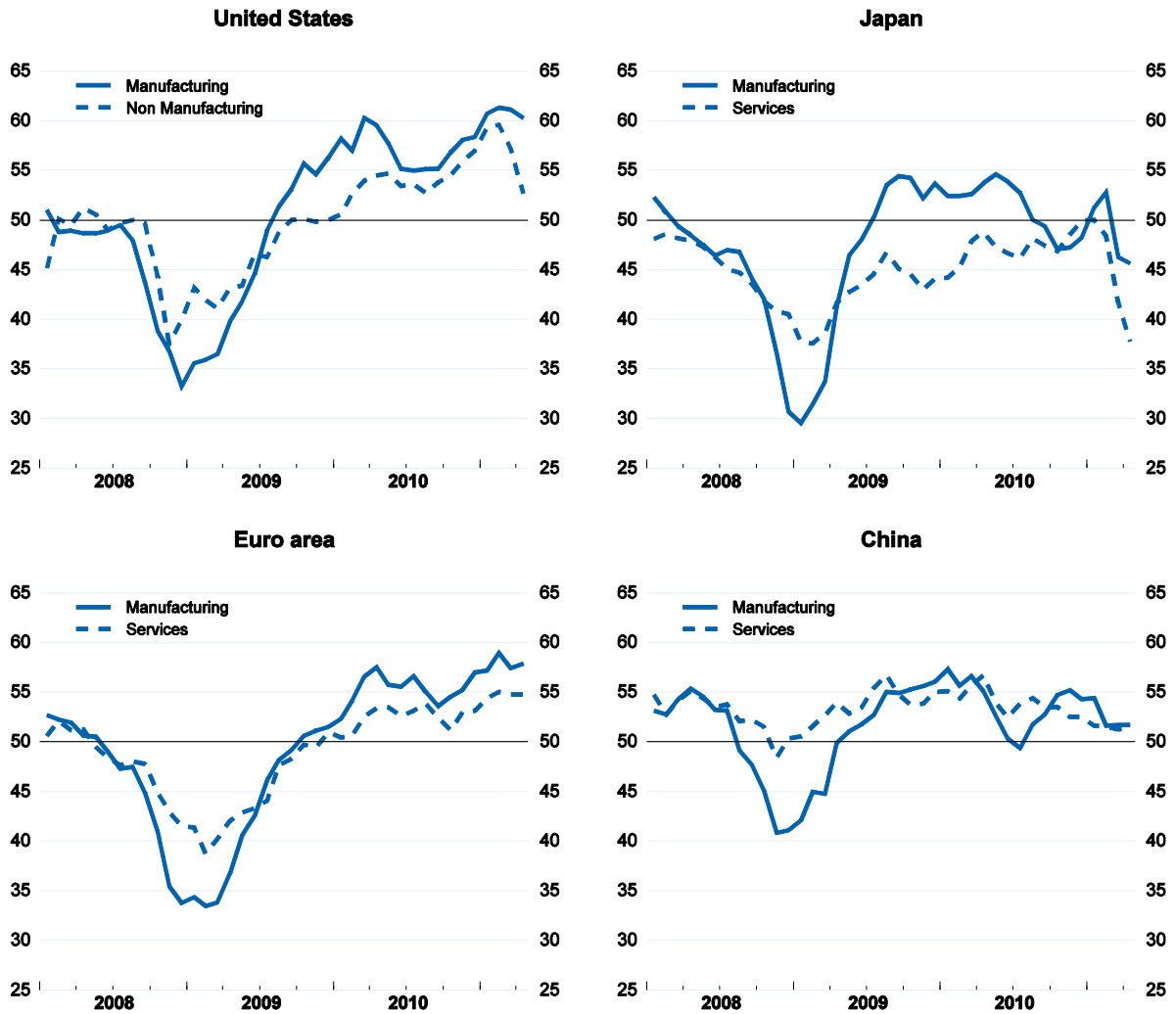


Note: Last observation 23 May 2011.

Source: Datastream; Central Bank of Brazil; Reserve Bank of India; and CEIC.

Business confidence is strong outside Asia

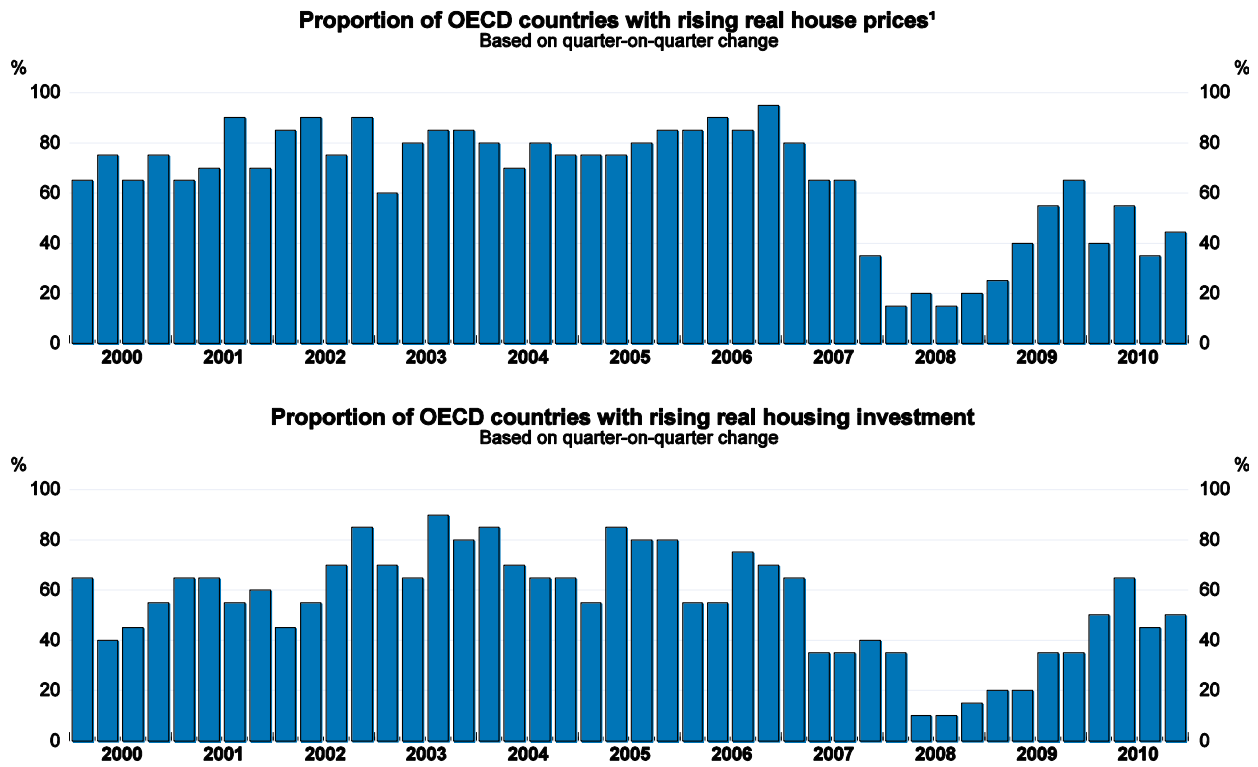
Purchasing Managers' Indices for manufacturing and services



Note: Value greater than 50 signifies an improvement in economic activity.

Source: Markit Economics Limited.

The housing market recovery is hesitant

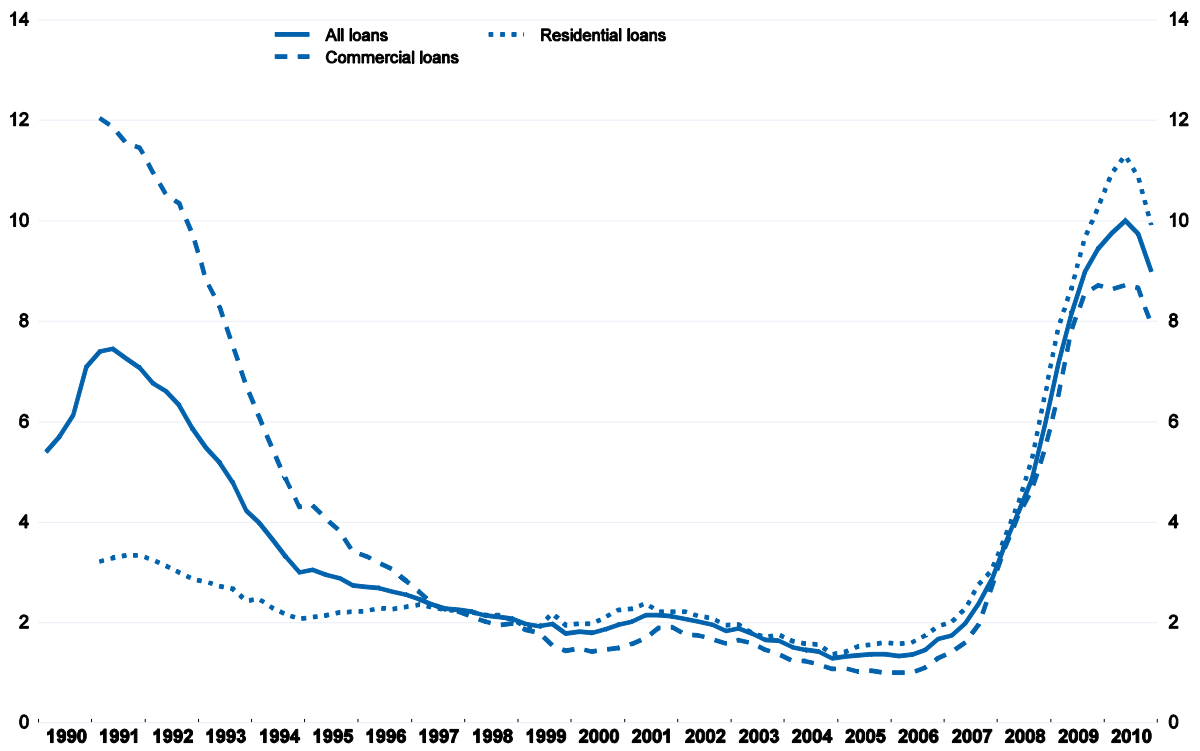


1. House prices deflated by the private consumption deflator. Calculation based on 20 countries (18 available in Q4 2010).

Source: OECD Economic Outlook 89 database; and various national sources, see table A.1 in Girouard, N., M. Kennedy, P. van den Noord and C. André (2006), "Recent house price developments: the role of fundamentals", *OECD Economics Department Working Papers*, No. 475.

Is the US housing sector turning the corner?

Delinquency rates on real estate loans,¹ in per cent

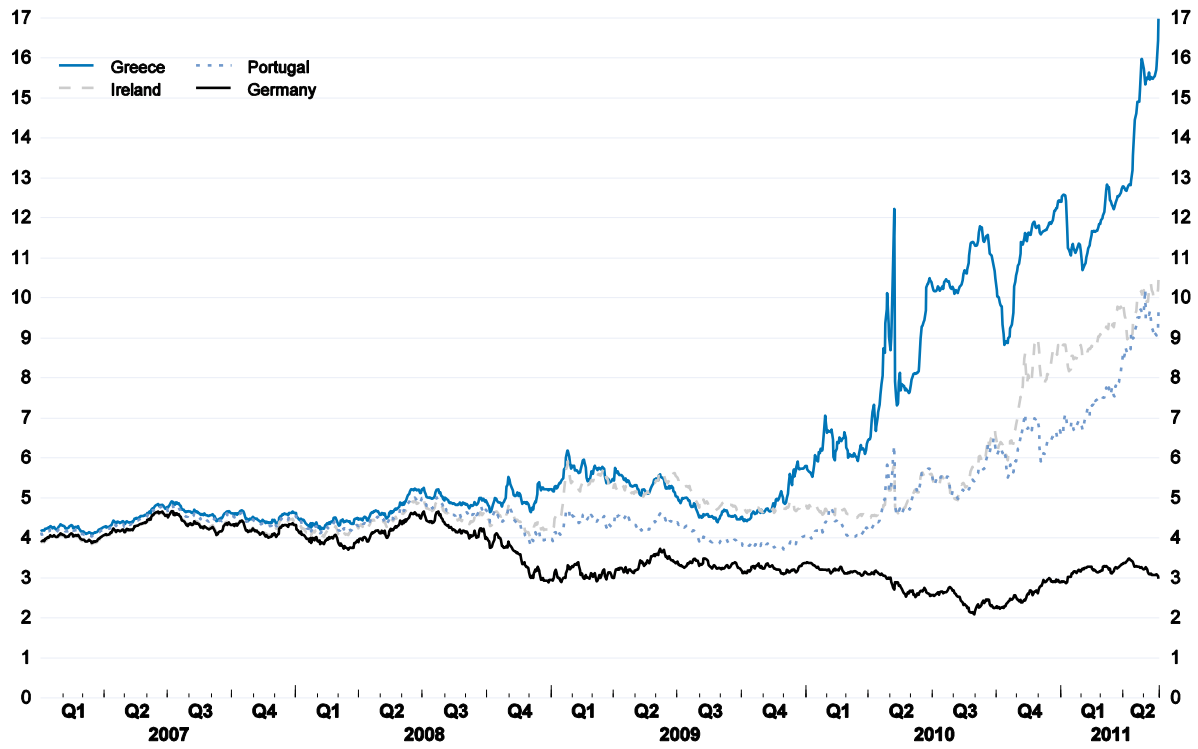


1. Delinquent loans are those past due thirty days or more.

Source: Datastream.

Sovereign spreads remain very high for peripheral euro-area countries

10-year government bond yields, percentage points

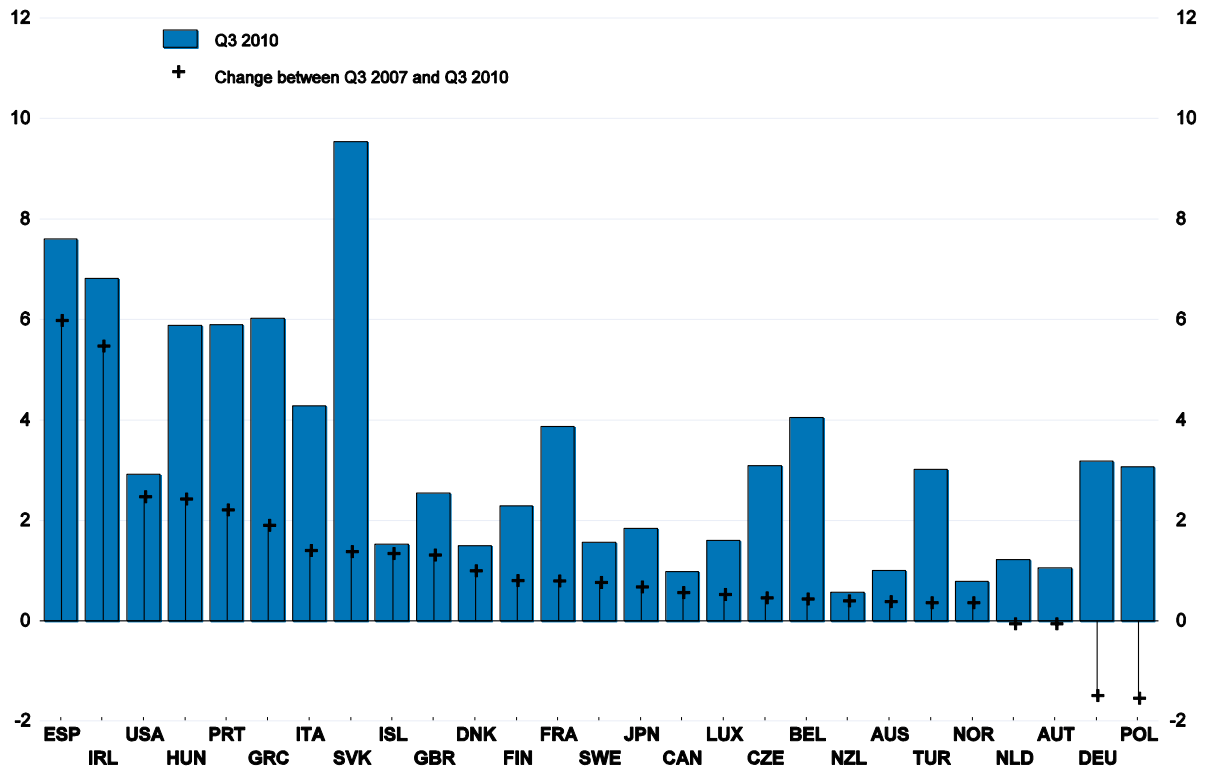


Note: Last observation 23 May 2011.

Source: Datastream.

Long-term unemployment has risen sharply in some countries

Ratio of long-term unemployed to labour force¹, per cent

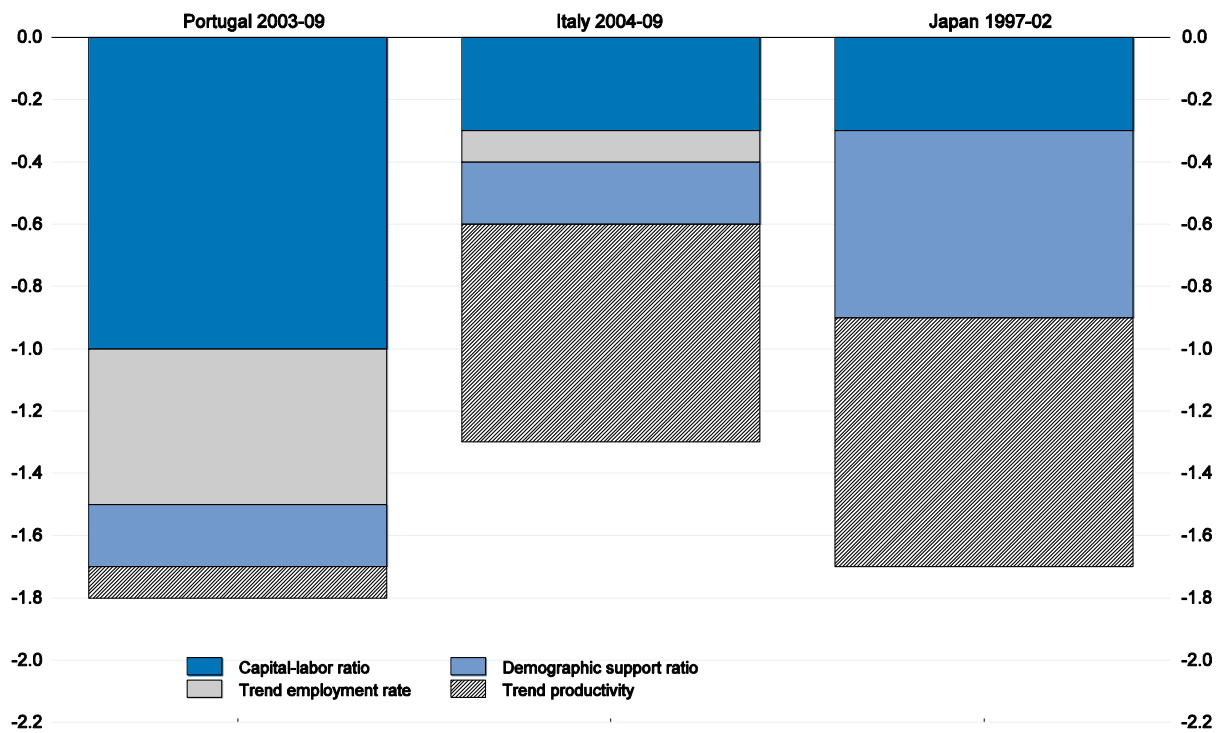


1. Long-term unemployed are those out of work for longer than 12 months; series smoothed using three-quarter centred moving averages.

Source: OECD Economic Outlook 89 database.

Productivity and capital allocation suffer during stagnation periods

Change in contributions to growth in potential output per capita relative to previous decade, period average percentage points

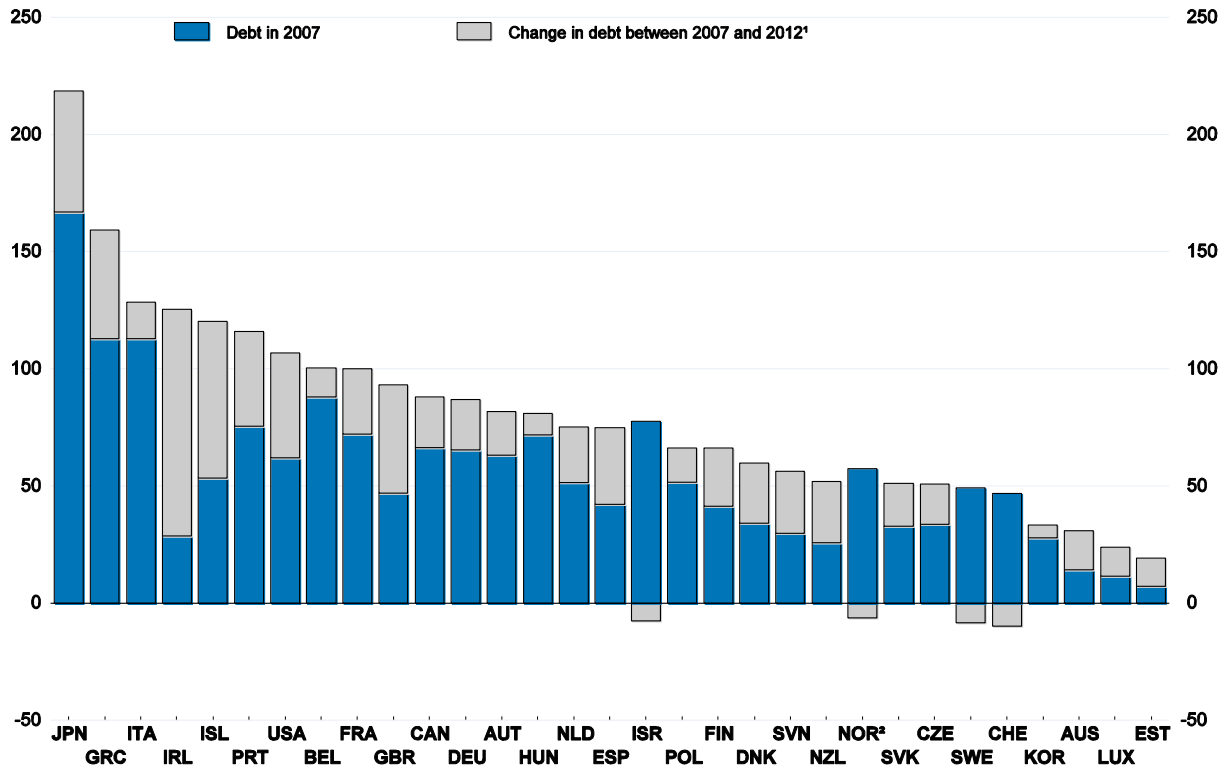


Note: For details see Table 4.6, Chapter 4 of OECD Economic Outlook, No. 89, May 2011.

Source: OECD Economic Outlook 89 database.

Government debt continues to accumulate apace

In per cent of GDP



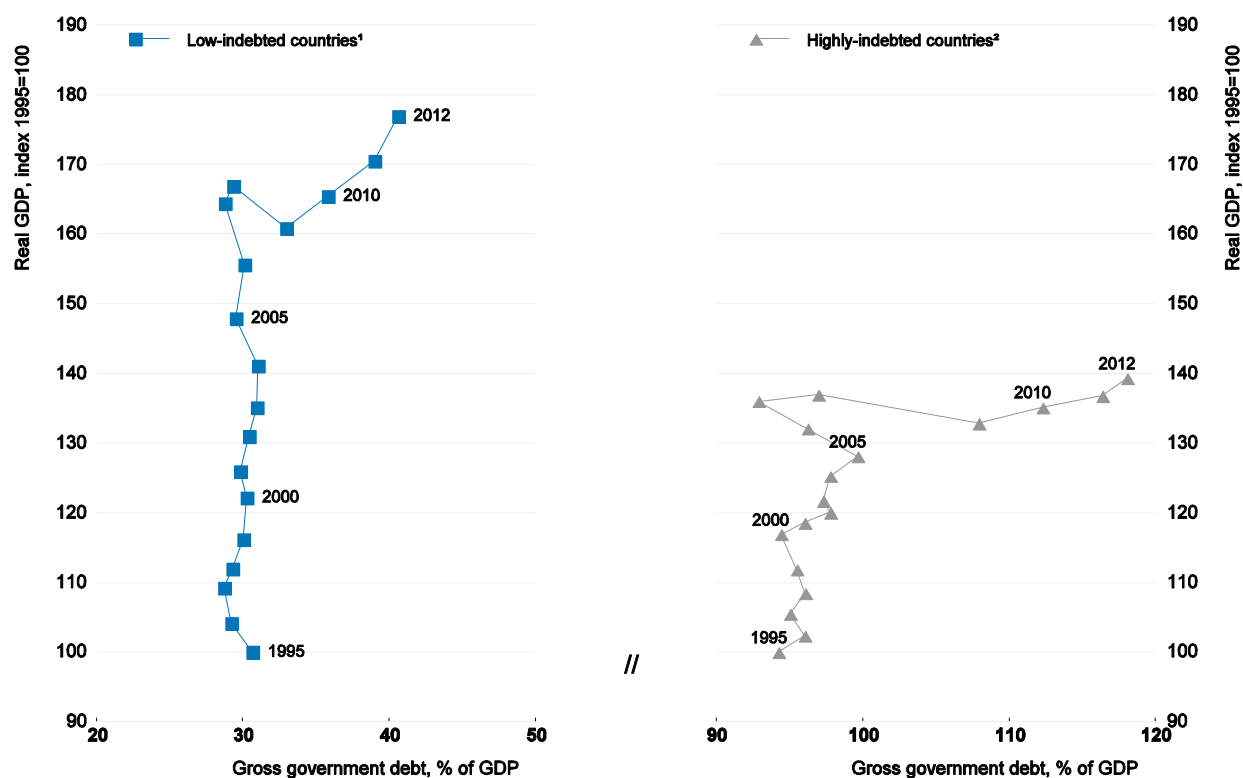
1. Includes cumulated deficit for 2008-12, debt-increasing equity participations in companies and the impact of GDP growth.

2. Cumulated deficits correspond to mainland only.

Source: OECD Economic Outlook 89 database.

Highly indebted countries have tended to grow more slowly

Government debt (per cent of GDP) versus level of real GDP (index 1995=100)



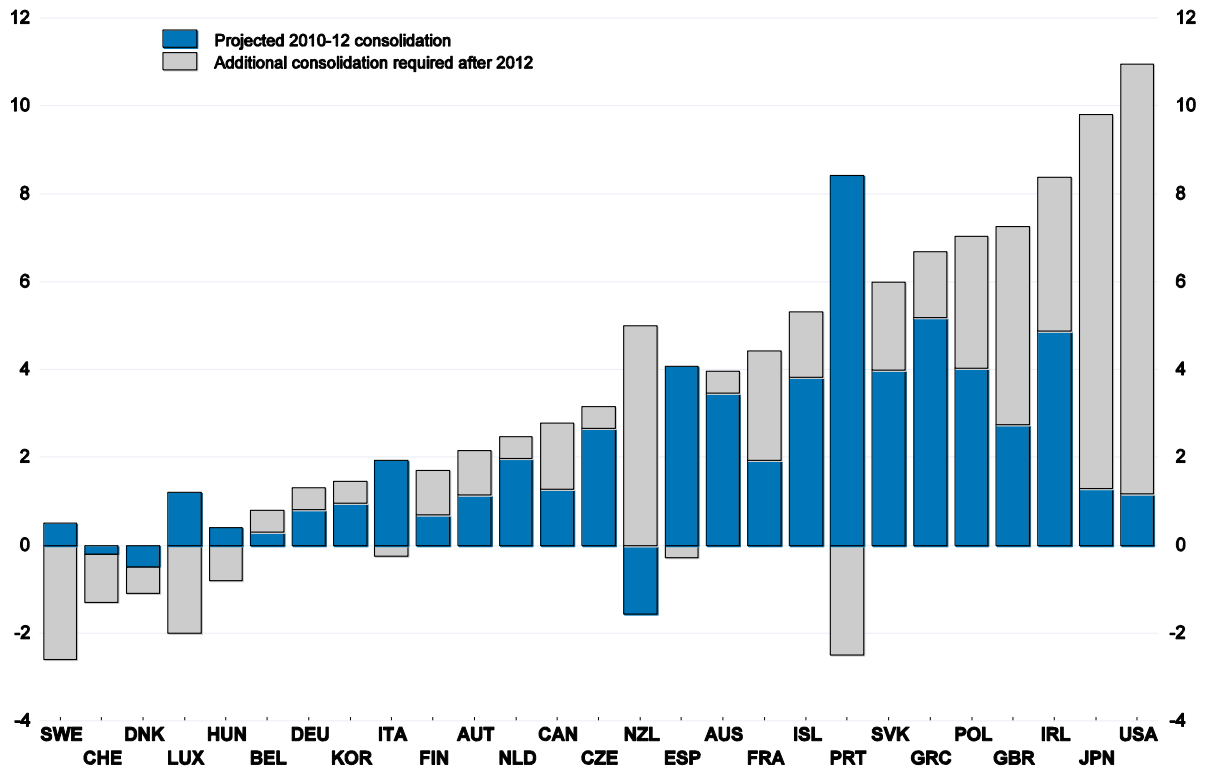
1. Low-indebted countries are those with gross government debt of less than 60 per cent of GDP for the duration of the period 1995-2012: Australia, Switzerland, Czech Republic, Estonia, Korea, Luxembourg, Norway, New Zealand, Slovak Republic and Slovenia.
2. Highly-indebted countries are those with gross government debt remaining above 60 per cent of GDP for the duration of the period 1995-2012: Austria, Belgium, Canada, France, Greece, Israel, Italy, Japan and Portugal.

Note: The real GDP indices for each group are calculated on the basis of the unweighted growth rates of individual countries within each group. Likewise, gross government debt as a percentage of GDP is calculated using the unweighted average for the individual countries within each group.

Source: OECD Economic Outlook 89 database.

Many countries require substantial fiscal consolidation merely to stabilise the debt-to-GDP ratio

Improvement in underlying primary balances from 2010, percentage points of GDP¹

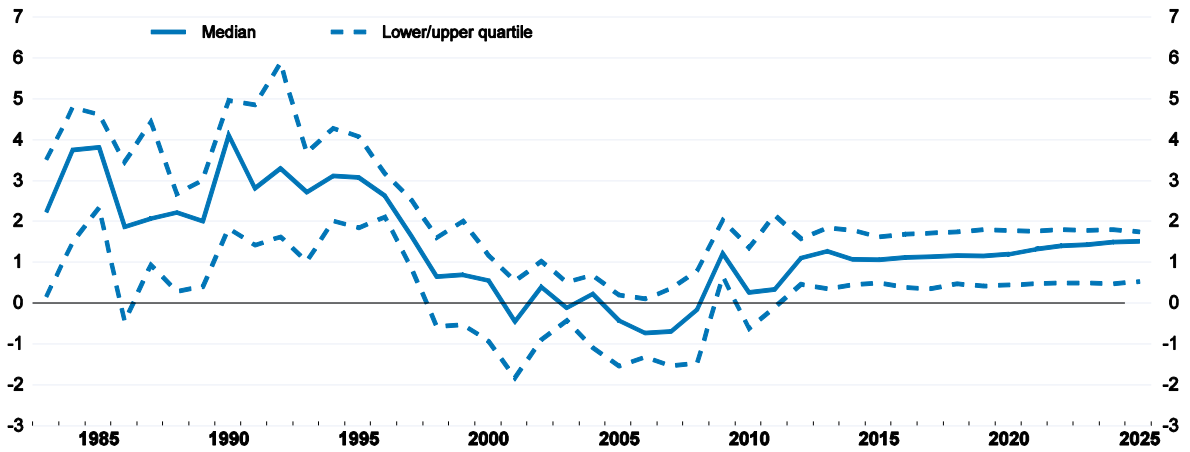


1. Consolidation through 2011 and 2012 as projected in Economic Outlook 89; consolidation after 2012 assumed to be an additional ½ percentage points of GDP each year until the debt-to-GDP ratio stabilises.

Source: OECD Economic Outlook 89 database; and OECD calculations (see OECD Economic Outlook, No. 89, May 2011, Chapter 4 for details).

Interest rates have begun to normalise from extreme pre-crisis lows

The differential between long-term interest rates and nominal potential growth for 20 OECD countries

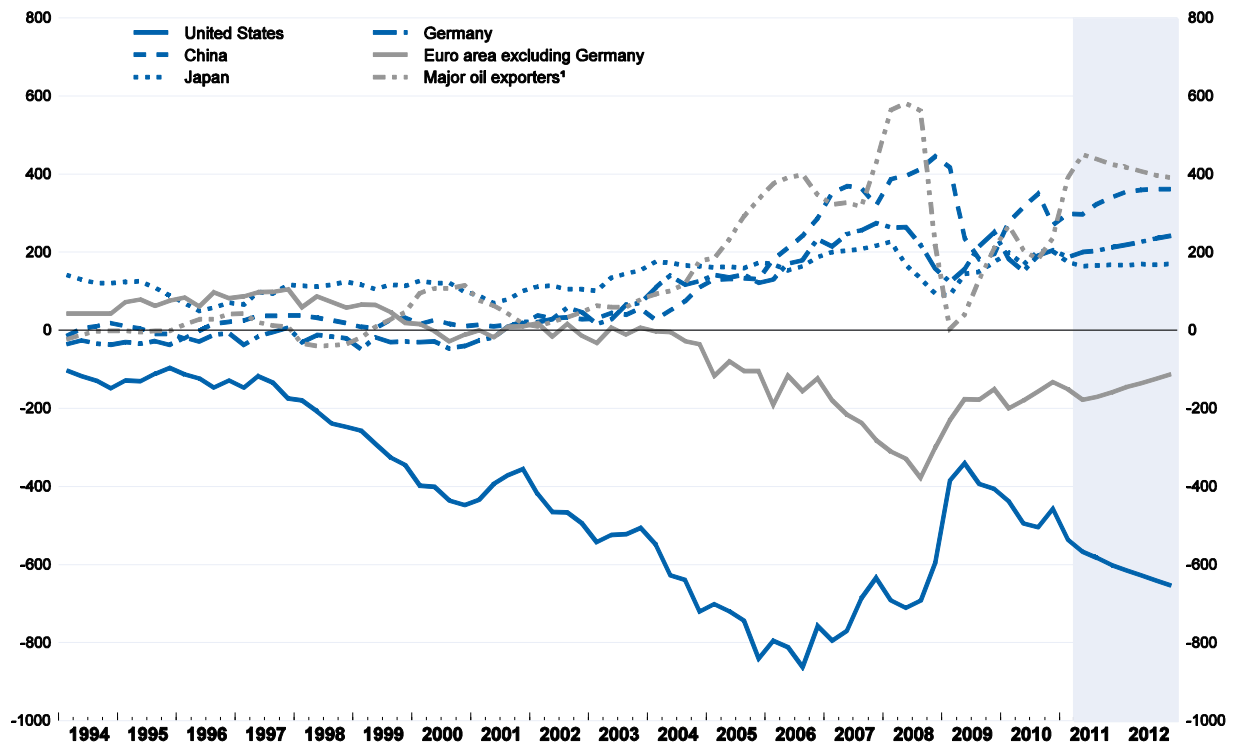


Note: The 20 OECD countries have been chosen on the basis of having consistent time series estimates for potential output and long-term interest rates on 10-year government bonds from 1983. Using nominal potential growth instead of actual GDP growth abstracts from the cycle and so gives a better impression of trend movements in the differential.

Source: OECD Economic Outlook 89 database; and OECD calculations.

Global imbalances remain wide

Current account balance, in US\$ billions

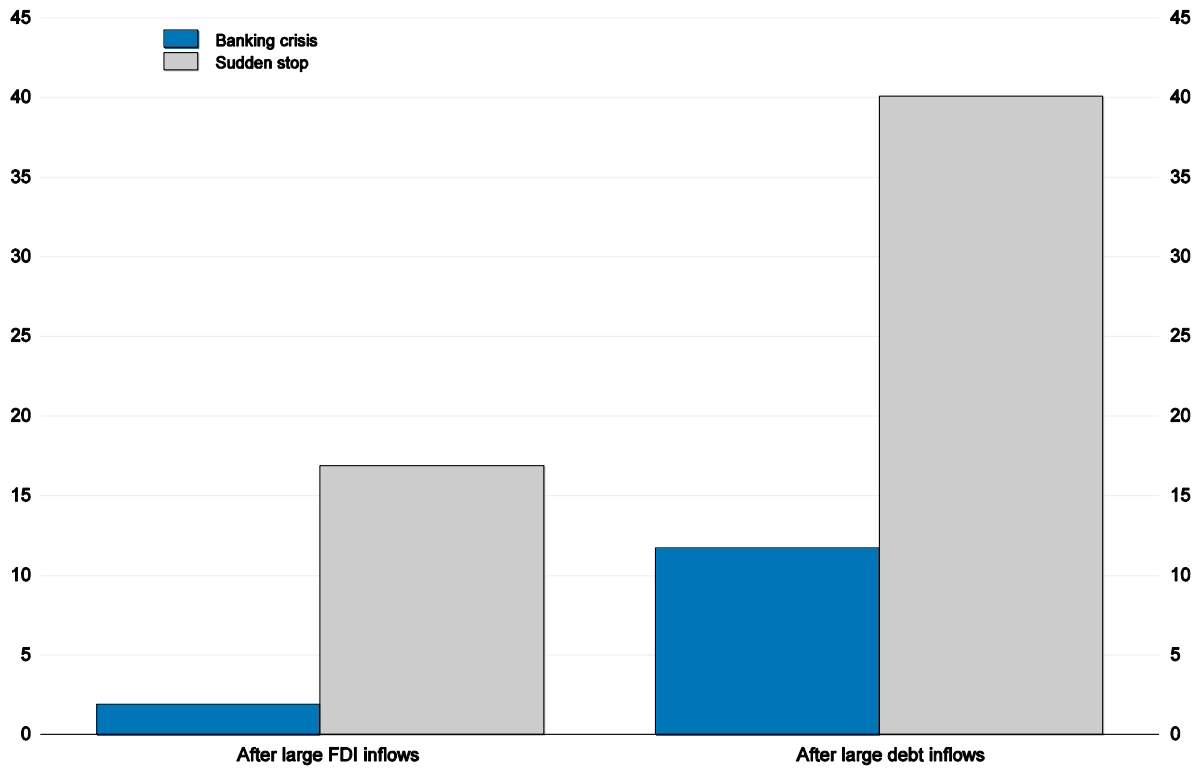


1. Includes Azerbaijan, Kazakhstan, Turkmenistan, Brunei, Timor-Leste, Bahrain, Iran, Iraq, Kuwait, Libya, Oman, Qatar, Saudi Arabia, United Arab Emirates, Yemen, Ecuador, Trinidad and Tobago, Venezuela, Algeria, Angola, Chad, Rep. of Congo, Equatorial Guinea, Gabon, Nigeria and Sudan.

Source: OECD Economic Outlook 89 database; and OECD calculations.

The likelihood of a crisis depends on the nature of capital flows

Annual probability of banking crisis and sudden stops, in per cent



Note: Based on regression results in Table 10 and 14 in Furceri, D., S. Guichard and E. Rusticelli (2011), "Episodes of Large Capital Inflows and the Likelihood of Banking and Currency Crises and Sudden Stops", *OECD Economics Department Working Papers*, No. 865. Probabilities are evaluated at sample means for all other variables entering the equation.

Source: OECD calculations.