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	2.0	2.5	2.0	2.5	1.7	1.9	2.2	2.3	2.5	2.7	2.8	2.8	1.5	2.0	2.7
Euro area	1.6	0.2	1.4	0.7	-1.0	-0.4	0.5	1.1	1.3	1.5	1.6	1.7	1.8	0.9	0.6	1.7
Japan	-0.3	2.0	1.6	6.0	1.5	1.8	1.8	1.6	1.5	1.5	1.6	1.7	1.8	0.8	1.7	1.6
Total OECD	1.9	1.6	2.3	2.4	1.1	1.2	1.7	2.2	2.1	2.3	2.4	2.7	2.5	1.6	1.8	2.5
Inflation[1]								year-on-year								
United States	2.5	1.9	1.4	2.9	2.9	2.4	2.0	1.8	1.6	1.5	1.4	1.3	1.2			
Euro area	2.6	1.6	1.2	2.7	2.5	2.0	1.6	1.6	1.4	1.3	1.2	1.2	1.2			
Japan	-0.3	-0.6	-0.3	0.2	-0.3	-0.6	-0.5	-0.6	-0.6	-0.5	-0.4	-0.3	-0.2			
Total OECD	2.5	1.9	1.5	2.8	2.6	2.2	1.9	1.8	1.7	1.6	1.6	1.5	1.5			
Unemployment rate[2]																
United States	9.0	8.9	8.6	9.1	9.0	9.0	9.0	8.9	8.8	8.7	8.6	8.5	8.4			
Euro area	9.9	10.3	10.3	10.0	10.1	10.2	10.3	10.3	10.4	10.4	10.3	10.2	10.1			
Japan	4.6	4.5	4.4	4.4	4.5	4.6	4.5	4.5	4.5	4.4	4.4	4.4	4.4			
Total OECD	8.0	8.1	7.9	8.0	8.1	8.1	8.1	8.1	8.1	8.0	8.0	7.9	7.8			
World trade growth	6.7	4.8	7.1	5.8	3.5	4.2	5.5	6.2	6.8	7.3	7.6	7.8	8.1	5.1	5.7	7.7
Current account balance[3]																
United States	-3.0	-2.9	-3.2													
Euro area	0.1	0.6	1.0													
Japan	2.2	2.2	2.4													
Total OECD	-0.6	-0.4	-0.4													
Fiscal balance[3]																
United States	-10.0	-9.3	-8.3													
Euro area	-4.0	-2.9	-1.9													
Japan	-8.9	-8.9	-9.5													
Total OECD	-6.6	-5.9	-5.1													
Short-term interest rate																
United States	0.4	0.4	0.3	0.3	0.4	0.4	0.4	0.4	0.3	0.3	0.2	0.3	0.4			
Euro area	1.4	1.0	0.6	1.6	1.4	1.1	1.0	0.9	0.8	0.7	0.6	0.5	0.4			
Japan	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2			

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 22 November 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 90 database.

StatLink http://dx.doi.org/10.1787/888932541607

EDITORIAL
THE POLICY IMPERATIVE: REBUILD CONFIDENCE

The global economy has deteriorated significantly since our previous *Economic Outlook*. Advanced economies are slowing down and the euro area appears to be in a mild recession. Concerns about sovereign debt sustainability in the European monetary union are becoming increasingly widespread. Recent contagion to countries thought to have relatively solid public finances could massively escalate economic disruption if not addressed. Unemployment remains very high in many OECD economies and, ominously, long-term unemployment is becoming increasingly common. Emerging economies are still growing at a healthy pace, but their growth rates are also moderating. In these countries falls in commodity prices and the slower global growth have started to mitigate inflationary pressures. More recently, international trade growth has weakened significantly. Contrary to what was expected earlier this year, the global economy is not out of the woods.

Many factors underpin this assessment. The headwinds of deleveraging in the financial and government sectors remain with us. Likewise, imbalances within the euro area, which reflect deep-seated fiscal, financial and structural problems, have not been adequately resolved. Above all, confidence has dropped sharply as scepticism has grown that euro area policy makers can deal effectively with the key challenges they face. Serious downside risks remain in the euro area, linked to the possibility of a sovereign default and its cross-border effects on creditors, and loss of confidence in sovereign debt markets and the monetary union itself. Another serious downside risk is that no action will be agreed upon to counter the pre-programmed fiscal tightening in the United States, which could tip the economy into a recession that monetary policy can do little to counter.

More than usual, world economic prospects depend on events, the nature and timing of which are highly uncertain. The projections presented in this *Economic Outlook* portray a scenario that rests on the assumptions that monetary policy remains very supportive (and, in some places, becomes more so), that sovereign debt and banking sector problems in the euro area are contained and that excessive fiscal tightening will be avoided. From the second half of 2012, confidence is assumed to recover gradually as it becomes clearer that worst-case outcomes have been avoided. Near-term output growth is subdued in the OECD economies and at below-trend rates in the major emerging-market economies, developments which are likely to be associated with further short-term weakening of sentiment and confidence. In some economies, especially the euro area, a mild recession is projected in the near term.

Alternative scenarios are possible, and may be even more likely than the baseline. A downside scenario would be characterised by materialisation of negative risks and the absence of adequate policy action to deal with them. An upside scenario could arise if policy action were successful in boosting confidence and no significant negative events occurred.

In the downside scenario, the implications of a major negative event in the euro area will depend on the channels at work and their virulence. The results could range from relatively benign to highly devastating outcomes. A large negative event would, however, most likely send the OECD area as a whole into recession, with marked declines in activity in the United States and Japan, and prolong and deepen the recession in the euro area. Unemployment would rise still further. The emerging market economies would not be immune, with global trade volumes falling strongly, and the value of their international asset holdings being hit by weaker financial asset prices.

What would be required for an upside scenario to materialise? A credible commitment by euro area governments that contagion would be blocked, backed by clearly adequate resources. To eliminate contagion risks, banks will have to be well capitalised. Decisive policies and the appropriate institutional responses will have to be put in place to ensure smooth financing at reasonable interest rates for sovereigns. This calls for rapid, credible and substantial increases in the capacity of the EFSF together with, or including, greater use of the ECB balance sheet. Such forceful policy action, complemented by appropriate governance reform to offset moral hazard, could result in a significant boost to growth in the euro area and the global economy.

An upside scenario also requires substantial and credible commitment at the country level, in both advanced and emerging market economies, to pursue a sustainable structural adjustment to raise long-term growth rates and promote global rebalancing. In Europe, such policies are also needed to make progress in resolving the underlying structural imbalances that lie at the heart of the euro area crisis. Deep structural reforms will be instrumental in strengthening the adjustment mechanisms in labour and product markets that, together with a robust repair of the financial system, are essential for the good functioning of the monetary union. By raising confidence, lowering uncertainty and removing impediments to economic activity, rapid implementation of such reforms could raise consumption, investment and employment.

If combined, stronger macroeconomic and structural policies might raise OECD output growth by as early as 2013. The largest benefits would be felt in the euro area, though these could take some time to emerge. Stronger activity and trade, and the consequent rise in asset values in the OECD economies, should boost activity in the emerging market economies as well.

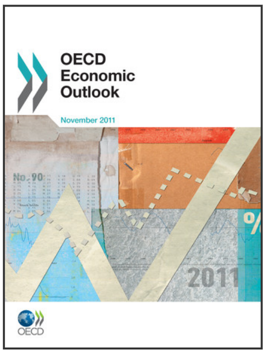
In view of the great uncertainty policy makers now confront, they must be prepared to face the worst. The OECD Strategic Response identifies country-specific policy actions that need to be implemented if the downside scenario materialises: the financial sector must be stabilised and the social safety net protected; further monetary policy easing should be undertaken; and fiscal support should be provided where this is practical. At the same time, stronger fiscal frameworks should be adopted to reassure markets that the public finances can be brought under control.

Beyond this, a wide range of structural measures, which are desirable in their own right, will become urgent. While priorities vary from country to country, such policies include the removal of barriers in product and labour markets that inhibit economic activity and employment. Appropriate labour market policies are needed to deal with the consequences of unemployment which is turning from cyclical to structural, thereby sapping potential growth, hitting confidence and undermining public finances.

The difference between the upside and the downside scenarios reflects the impact of credible, confidence building policy action. Such action, as we have seen, requires measures to be implemented at the euro area level as well as at the country level throughout the OECD, especially in the structural policy domain. In the case of a downside scenario, policy action would clearly be needed to avoid the worst outcomes. But then the question arises of why policy efforts are not taken to deliver the upside scenario even if the worst case does not materialise. Why, in other words, should we settle for less?

28 November 2011

Pier Carlo Padoan
Deputy Secretary-General and Chief Economist



From:
OECD Economic Outlook, Volume 2011 Issue 2

Access the complete publication at:
https://doi.org/10.1787/eco_outlook-v2011-2-en

Please cite this chapter as:

OECD (2011), “Editorial: The Policy Imperative: Rebuild Confidence”, in *OECD Economic Outlook, Volume 2011 Issue 2*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/eco_outlook-v2011-2-1-en