



# **International Monetary and Financial Committee**

Thirty-Fourth Meeting  
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**IMFC Statement by Angel Gurría  
Secretary-General  
OECD**



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# **2016 IMF and World Bank Fall Meetings:**

## **IMFC Written Statement**

**Angel Gurría**

**OECD Secretary-General**

**8 October 2016**  
**Washington, DC**

## **The Global Economic Outlook**

1. **The world economy remains in a self-fulfilling low-growth trap.** Persistent growth disappointments are weighing on current expectations of future growth and feeding into weak trade, investment, productivity, and wages. Breaking out of this trap is essential if strong, sustainable, balanced and inclusive growth is to be achieved.

2. **The OECD's September *Interim Economic Outlook* suggests global GDP growth has slipped further to 2.9% in 2016, with only a marginal improvement projected for 2017.** The advanced economies have failed to gain momentum and improvements in emerging market economies have been modest. The UK's vote to leave the European Union has created considerable uncertainty that is likely to persist for an extended period.

3. **Labour markets are showing some signs of recovery from the global financial crisis, but progress remains slow.** The OECD's *2016 Employment Outlook* suggests that three-quarters of OECD countries still face either a sizeable unemployment gap – an unemployment rate that is 2 percentage points or more above the pre-crisis level – or a sizeable wage gap – average wages at least 5% below the level they would be at if they had continued the trend increase during 2000-07 – or both.

4. **Global trade remains exceptionally weak.** The volume of world trade declined in the first quarter of 2016. Despite some recovery in the second quarter, global trade growth is likely to equal or fall below GDP growth for the year as a whole. This is well below past trends and suggests that globalisation, as measured by trade intensity, may have stalled. Structural factors, such as the slowdown and reversal of trade liberalisation and the weakening of global value chains (particularly in China and East Asia) account for a significant proportion of the moderation in trade growth between 2011 and 2015. Cyclical factors, including the deep recessions in some commodity-producing economies, and the widespread weakness of fixed investment, have compounded structural problems. If sustained, the trade slowdown will undermine OECD productivity growth further and, in turn, may affect living standards.

5. **Supportive macroeconomic policies and low commodity prices continue to underpin activity in the advanced economies.** However, there are few signs of the pick-up in wage growth and business investment needed for stronger growth.

- **In the United States, GDP growth has remained unexpectedly subdued at around 1.5% in 2016, with solid consumption and job growth offset by weak investment and a prolonged inventory correction.** Demand growth is likely to improve in 2017, but is expected to remain below historical trends.
- **Weak domestic demand, including the stalling of the short-lived recovery in investment, has slowed GDP growth in the euro area.** While employment continues to increase slowly, there remains significant slack in the labour market and there are few signs of inflation and wage pressures. GDP growth is set to remain moderate, easing below 1.5% in 2017 as the negative effects of weaker demand growth in the UK are realised.
- **In Japan, growth remains weak and uneven, with the appreciation of the yen and sluggish Asian trade weighing on exports.** The postponement of the consumption tax

increase and higher government spending in the 2016 Supplementary Budgets will support demand and growth in 2017.

- **While markets have stabilised following the UK's decision to leave the European Union, available indicators anticipate a growth slowdown in 2016 and prolonged uncertainty, despite the prompt support provided by the Bank of England.** GDP is projected to rise by 1% in 2017, well below the pace in recent years and the outlook prior to the referendum.

6. **Emerging market economies are likely to experience mixed outcomes, reflecting differences in available policy support, the impact of low commodity prices, progress in enacting structural reforms, and the extent of financial vulnerabilities.** Overall, growth is set to pick up slowly in 2017, driven by a gradual easing of the recessions in Brazil, Russia and other commodity-producing countries. In China, fiscal and monetary stimulus is supporting demand as efforts to rebalance the economy from investment and manufacturing-led growth towards consumption and services continue. Managing this rebalancing alongside financial system risks remains a key challenge. Strong domestic demand growth, supported by credit expansion, continues to support activity in many other Asian economies, offsetting the drag from weak trade developments in China. In India, a large increase in public sector wages and the recent passage of key structural reforms, particularly the goods and services tax, will support growth.

7. **Prolonged weaknesses in demand are reflected increasingly in adverse supply-side developments that are contributing to the low-growth trap in advanced and emerging economies.** For the OECD as a whole, potential GDP per capita growth is estimated at 1% in 2016, around 1 percentage point below the average in the two decades preceding the crisis. This decline reflects both weak investment and slower total factor productivity growth, itself the result of a slowing of diffusion of innovations across firms and – more recently – slowing innovation at the technological frontier. Potential output growth in the BRIICS on a per capita basis has also been revised down in recent years, by over 1½ percentage points in China since 2011 and 1 percentage point in the remaining economies. Survey measures of expected long-term GDP growth have also declined over the past five years, especially in countries with past growth disappointments.

8. **Persistently low growth has contributed to exceptionally low, and even negative, market interest rates, largely reflecting both actual and expected monetary policy stimulus.** Almost USD 15 trillion of government bonds – more than 35% of OECD sovereign debt – is trading at negative yields. This situation creates a number of distortions and risks in financial markets and poses challenges to the business models of financial institutions, including banks, asset managers and pension funds.

9. **Low interest rates are leading to widespread and substantial increases in asset prices, both internationally and across asset classes, which is distorting financial investment and encouraging leveraged risk-taking.** Share prices have risen significantly in advanced economies, despite declines in long-term growth expectations. House prices are also growing at a similar or higher pace than prior to the crisis in a number of countries, with price-to-rent ratios reaching record highs in some. These developments increase the likelihood and adverse economic impact of a sharp correction in asset prices. A reassessment in financial markets of expected future interest rates could thus result in substantial re-pricing of assets and heighten financial volatility even if interest rates remain below long-term

averages. This effect is reinforced by the rising average duration of outstanding government and corporate bonds.

### **Macroeconomic Policy Requirements**

10. **A stronger collective fiscal and structural policy response is needed to break out of the low-growth trap.** This policy mix should reflect country and region-specific conditions, and account for international spillovers. If policy remains on the current path, with monetary policy showing clear signs of becoming overburdened, low growth will continue with negative consequences for productivity, trade, jobs and inclusiveness.

11. **The fiscal space provided by low interest rates should be used to boost growth and equity.** Well-targeted, growth-friendly fiscal measures need not increase debt ratios in the longer term if they raise potential output. Collective action to direct fiscal resources to projects with a high-growth impact would deliver additional output gains from cross-country spillovers. Increasing hard and soft infrastructure spending, and using fiscal measures to support structural reforms – such as greater spending on well-targeted active labour market programmes and basic research – would benefit both short-term demand and longer-term supply. These measures could also mitigate the negative short-term effects of structural reforms, particularly when demand is weak.

12. **More ambitious structural reforms and faster implementation of announced measures are needed to strengthen output growth and ensure that the benefits of higher growth are shared broadly.** Renewed steps are needed to ease competition-restraining product market regulations and barriers to foreign trade and FDI; strengthen skills acquisition and use; adjust the structure and efficiency of tax systems; and improve R&D and innovation policies. More could be done to improve labour utilisation, notably through adjusting unemployment and social benefits and active labour market policies to promote skill upgrading and matching. While reform priorities vary by country, there is significant room for raising performance in all major advanced and emerging economies. An enhanced collective focus on trade policies is also essential, to avoid new protectionist measures, roll back protectionist measures introduced since the crisis, and reduce unnecessary trade costs.

### **Implications of 'Brexit'**

13. **The UK's vote to leave the European Union on 23 June has exacerbated downside risks to the global economic outlook.** The 'Brexit' process is expected to be disruptive and costly, generating uncertainty and weakening demand. Collective policy efforts to increase aggregate demand in the short-term will position countries to manage these challenges.

14. **UK output growth has slowed in line with the more moderate scenarios produced prior to the referendum, in part reflecting the swift actions taken to ease macroeconomic policies following the vote.** In 2016, growth is expected to reach 1.8% and slow to 1% in 2017. Spillovers to the global economy, particularly close trading partners, are likely to become apparent in 2017. Since the referendum, the UK effective exchange rate has depreciated by around 10 per cent.

15. **Uncertainty about the future direction of policy, the relationship between the UK and the European Union, and the reaction of the economy remains very high, and is likely to persist.** News-based measures of policy uncertainty have risen sharply both domestically and internationally,

and survey evidence suggests that the vote will negatively impact UK corporate capital spending, hiring and turnover in the coming year.

16. **The UK's future trading arrangement with the European Union and other partners will be critical to its economic prospects.** Outcomes – and the longer-term supply-side costs to the UK economy and other economies in Europe – will hinge crucially on whether the UK remains in the Single Market (and accepts the free movement of people and goods, services and capital, and continues to make a budgetary contribution to the European Union), or settles for a less close association. An additional risk is a prolonged period of no or slow progress in market opening involving the European Union. This would hamper efforts by G20 economies to trigger productivity improvements and growth through trade and investment opening as part of a package of comprehensive structural reforms.

17. **The longer-term supply side costs for the UK arise through several channels.** Lower trade openness would disrupt complex value chains and adversely impact economic dynamism, productivity and incomes. Reduced access to the European market would also lower inward foreign direct investment, with associated negative effects on innovation, managerial quality and productivity. Reductions in net migration inflows would add to these challenges by reducing the size of the labour force. While reductions in UK regulatory burdens are often cited as offsets to these effects, the scope for such reductions is limited, as UK regulations were already among the most flexible, even before Brexit. The overall impact on UK living standards from these effects will be negative. By 2030, OECD estimates suggest that UK GDP could be over 5% lower than if the UK had remained in the European Union, with possible declines ranging from 2.5% to 7.5% depending on the severity of the resulting shocks.