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**IMFC Statement by Angel Gurría
Secretary-General
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Written Statement to the IMFC

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The Global Economic Outlook

- 1. The global economic outlook has become increasingly fragile and uncertain.** GDP growth is subdued and global trade is contracting. Continued and deepening trade policy tensions are taking an increasing toll on confidence and investment, adding to policy uncertainty, and weighing on risk sentiment in financial markets. Global GDP growth slowed to an annual pace of 3% in the first half of 2019, almost 1 percentage point lower than mid-2017. Improved labour market conditions and accommodative macroeconomic policies continue to hold up household incomes and spending, but investment – a key driver of future prospects – has weakened sharply. Aggregate investment growth in G20 economies has slowed from an annual rate of 5% at the start of 2018 to only 1% in the first half of 2019.
- 2. The September 2019 OECD Interim Economic Outlook predicts global GDP growth will ease to 2.9% in 2019 and 3% in 2020.** These would be the weakest annual growth rates since the global financial crisis. Outcomes could be weaker still if downside risks materialise or interact, including from further use of trade and investment policy instruments that impede business choices, a no-deal Brexit, a failure of policy stimulus to prevent a sharper slowdown in China, and financial vulnerabilities from the tensions between slowing growth, high debt and deteriorating credit quality. A persistent upward spike in oil prices if geopolitical tensions strengthen would also weaken growth prospects.
- 3. The subdued economic outlook and mounting downside risks call for urgent policy actions to reduce policy-related uncertainty, ensure sufficient support for demand, enhance resilience against risks and strengthen prospects for medium-term living standards.** Trade policy unpredictability needs to give way to more orderly approaches to restore a transparent and rules-based system that encourages businesses to invest. Monetary policy has already become more accommodative this year in most major economies, given the growth outlook, but would be more effective if enhanced by stronger fiscal support and greater structural policy ambition. Exceptionally low interest rates provide an opportunity for investing in measures that support near-term demand and incomes and enhance medium-term growth. In the event of an even sharper global growth slowdown than projected, coordinated policy action within and across all the major economies would provide an effective and timely counterweight.
- 4. The widespread moderation in GDP and trade growth prospects appears likely to persist for longer than earlier anticipated.** The bilateral tariff measures introduced by the United States and China since the start of 2018, including those planned for the remainder of 2019, are a major factor behind the weak outlook for global activity and trade over the next two years. OECD estimates suggest that the US-China measures could reduce global GDP growth by between 0.3-0.4 percentage points in 2020 and 0.2-0.3 percentage points in 2021. While China and the United States would be most affected by these shocks, all economies would be adversely affected by policy uncertainty and unpredictability, and the trade slowdown.

5. **Key features of the projections for the major global economies are:**

- GDP growth in the United States is projected to moderate from just under 2½ per cent in 2019 to around 2% in 2020, with support from fiscal easing fading slowly. Solid labour market outcomes and supportive financial conditions still underpin household spending, but higher tariffs have added to business costs and the growth of business investment and exports has moderated.
- In the euro area, GDP growth is projected to remain subdued at around 1% in 2019 and 2020. Wage growth and accommodative macroeconomic policies are supporting household spending, but policy uncertainty, weak external demand and low confidence are weighing on investment and exports. Outcomes in Germany and Italy are set to remain relatively weak, reflecting their greater exposure to the global trade downturn. Growth in France is projected to remain relatively resilient, helped by fiscal measures that are supporting household incomes.
- GDP growth in Japan is set to slow from 1% in 2019 to 0.6% in 2020. Labour shortages and capacity constraints continue to stimulate investment, but confidence has eased and export growth has weakened. Stronger social spending should support demand following the increase in the consumption tax rate in October, but fiscal consolidation efforts will resume in 2020.
- In the United Kingdom, GDP growth is projected to be around 1% in 2019 and 2020, provided the exit from the European Union proceeds smoothly with an agreed deal and a transition period. Growth has weakened, reflecting persistent uncertainty and weak investment, but sizeable fiscal easing should help to support demand next year.
- GDP growth in China is projected to moderate to around 5¾ per cent in 2020. Escalating trade tensions are weighing on investment and adding to uncertainty, but new fiscal and quasi-fiscal stimulus measures and monetary policy easing should help to cushion credit growth and demand.
- In India, GDP growth has proved surprisingly weak in recent quarters, with consumer spending having slowed and tight financial conditions restraining investment. Growth is expected to strengthen from around 6% in FY 2019 to just over 6¾ per cent in FY 2020, with lower interest rates and stronger benefits from reform efforts helping private sector demand to rebound.
- A gradual recovery is set to continue in Brazil, with GDP growth projected to pick up from 0.8% in 2019 to around 1¾ per cent in 2020. Lower real interest rates provide support for private consumption, and progress towards implementing reforms should help to support sentiment and investment.

Trade tensions continue to rise and could intensify further

6. **The risk of further escalation in trade and technology policy restrictions around the world is a serious concern.** Such measures disrupt global supply networks, lower productivity, reduce and distort trade, and weigh on confidence, jobs and incomes. The deferral of the tariff increases that were set to take effect in mid-October, as well as the resumption of trade talks on the remaining trade issues between the United States and China, are positive developments. However, risks remain that bilateral tensions could spill into new areas. Services trade, notably tourism, might be restrained; and administrative and regulatory barriers could be enhanced on the affiliates of US companies operating in China, whose sales in China outstrip total US exports to China. Bilateral trade tensions could also spread to other countries, including between the United States and the European Union. Any restrictions in specific trade-sensitive sectors, such as motor vehicles and parts, or aeronautics, would be particularly costly to both economies, given the complexity of the supply chains that would be disrupted.

Growth in China could slow more sharply than expected

7. **The risks of a sharper slowdown in China are intensifying. Exports to China from the major advanced economies have declined significantly over the past year.** Weak import demand in China partly reflects structural changes, such as substitution towards domestically-produced goods, but also raises concerns about the effectiveness of the policy support put in place over the past year, and the underlying strength of the economy. Fiscal policy support this year, of at least 1% of GDP, involves tax reductions and increases in resources to finance infrastructure spending. However, household tax reductions take time to feed through to consumer spending, and investment in infrastructure has picked up only modestly following the sharp moderation in 2018. A sustained decline in domestic demand growth of 2 percentage points per year in China would result in a significant slowdown in global growth, particularly if accompanied by a deterioration in global financial conditions and heightened uncertainty. In such circumstances, global GDP growth could be lowered by 0.7 percentage points per year on average in the first two years of the shock, with the strongest effects being felt in neighbouring economies in Asia.

A no-deal Brexit would be costly

8. **The possibility that the United Kingdom will exit from the European Union without a formal deal is a serious downside risk, and a major source of uncertainty.** Should this occur, the economic outlook would be significantly weaker and more volatile. The effects would be especially costly if preparations to border infrastructure fail to prevent significant delays, or financial market conditions deteriorate considerably, or consumer and business confidence decline sharply.

9. **Even a relatively smooth no-deal exit, with fully operational border infrastructure, would have large costs.** In this event, OECD estimates suggest that UK GDP could be 2-2½ per cent lower than otherwise in 2020-21, potentially pushing the economy into recession. These effects come on top of weaker-than-expected growth in the UK economy since the referendum in 2016. UK exports would be reduced due to higher tariff and non-tariff barriers with the European Union and elsewhere, uncertainty would weigh further on investment, and the longer-term supply-side costs of exit would gradually emerge. In such a scenario, there would also be sizeable negative spillovers in other EU economies, with euro area GDP being over ½ per cent lower than otherwise in 2020-21.

10. **Policy responses could cushion part of these short-term costs.** In the United Kingdom, the Bank of England should react to a much weaker growth outlook and reduce policy interest rates or buy bonds. Fiscal policy could also be eased further, although a no-deal exit would add to pressures on public finances. In European economies, faced with a negative shock, monetary policy could become more accommodative, although there is limited room to do so given negative policy interest rates in some economies. A more effective approach would be to implement targeted and temporary fiscal measures to support investment in some sectors, and to assist with the retraining of displaced workers and new job creation in those countries most affected.

Significant financial vulnerabilities continue to accumulate

11. **Concern remains about the high debt of non-financial corporations and its deteriorating quality.** An increasing share of newly-issued corporate bonds are at the lowest investment grade rating, and leveraged loans to corporates have risen sharply in the main advanced economies, to more than USD 2.1 trillion (2½ per cent of global GDP in 2018). These developments could amplify a recession or a further sharp growth slowdown. A marked reduction in corporate revenue growth could cause corporate stress, triggering a change in investors' risk appetite and a widespread sell-off of corporate bonds. The current composition of corporate bonds may also increase the risk of fire sales, as a high share of these bonds is rated just above non-investment grade. In the event of a downgrade to non-investment grade following a negative economic shock, institutional investors bound by rating-based regulatory requirements would be obliged to sell. With risks having shifted from banking systems towards more lightly regulated non-bank financial institutions since the financial crisis, the resilience of these institutions remains a potential additional source of financial stability risks.

Policy Requirements

12. **The subdued economic outlook and high policy uncertainty call for policy responses that strengthen confidence, stimulate investment and boost the potential for strong growth.** Confidence-building measures that calm trade policy tensions and address other sources of uncertainty are urgently required, and the need for additional macroeconomic policy support has risen in most economies. Monetary policy has already moved in this direction, but the effectiveness of accommodative monetary policy could be enhanced in many advanced economies if accompanied by stronger fiscal and structural policy support.

13. **In setting national and global reform priorities, countries must also strive to tackle inequality and strengthen sustainability.** Growing inequalities remain one of the biggest social challenges in the world today, perpetuating poverty, and undermining social cohesion and trust. In this context, countries should continue to focus on measures to strengthen inclusiveness, guided by the OECD's flagship Inclusive Growth Initiative and the OECD Framework for Policy Action on Inclusive Growth. At the same time, curbing emissions and pollution is crucial in ensuring that gains in growth and well-being are sustainable in the long-term. The OECD's *2019 Going for Growth* publication has taken steps to integrate environmental sustainability in its reform priority selection framework for countries.

Monetary policy accommodation needs to be supplemented by fiscal support in advanced economies

14. **Against the background of slowing growth and the prospect of inflation remaining below target for a prolonged period, central banks in the main advanced economies have either eased monetary policy in recent months or communicated their readiness to act if the outlook were to deteriorate further.** The actual measures implemented or announced are likely to provide some modest support to aggregate demand and help to stabilise inflation expectations, but will also boost already-high asset prices. In the United States, where growth remains close to trend rates and underlying inflation is close to target, there is limited need for further reductions in policy interest rates unless the risks of a sharper growth slowdown rise. The euro area and Japan have limited scope to ease monetary policy further, but may face a renewed need to do so if sub-par growth weakens further or if inflation remains persistently well below target.

15. **There is room in many advanced economies to allow automatic budgetary stabilisers to operate fully and to implement discretionary fiscal stimulus where needed.** The effective nominal interest rates paid on public debt are expected to remain below nominal GDP growth rates for some time, and projected budget balances are higher than those necessary to stabilise debt. A number of economies have already announced a sizeable fiscal expansion for 2020, including Korea, the United Kingdom and the Netherlands. Low or negative long-term interest rates also offer a low-risk opportunity for many countries to address serious infrastructure shortages. This would both support near-term demand and strengthen longer-term sustainable growth. In the euro area, where growth has dropped below trend rates, a joint programme of fiscal support where space exists and renewed reform efforts to strengthen medium- and long-term growth is needed alongside continued accommodative monetary policy. This would be more effective for growth and create fewer financial distortions than continuing to rely mainly on monetary policy.

Macroeconomic policy requirements in the emerging-market economies

16. **Policy requirements differ across the individual economies depending on their situation.** In China, both fiscal (including quasi-fiscal) and monetary policies have appropriately been eased, given demand weakness. Scope remains for further measures if growth weakens further or if policy instruments are less effective than in the past, but careful choices are needed to avoid adding to high indebtedness and deleveraging challenges. Other emerging-market economies with flexible exchange rate frameworks and manageable exposures to foreign currency denominated debt, such as India and Brazil, have scope to further ease monetary policy as inflation declines, while taking the opportunity to improve their fiscal positions and progress with the implementation of necessary structural reforms. A tight policy stance remains necessary in those emerging-market economies where concerns persist about the sustainability of fiscal or external positions, or the health of the banking sector, in order to retain investors' confidence.

Structural policy ambition needs to be improved in all countries

17. **In the absence of renewed reform dynamism, the prospects for strong and sustained improvement in living standards and incomes in the medium-term remain weak.** Real per capita income growth since the financial crisis has been well below pre-crisis levels in almost all economies. Important reforms continue to be undertaken in some economies but overall, as set out in the latest *OECD Going for Growth* report, structural reform efforts remain below those achieved in the aftermath of the crisis in both advanced and emerging-market economies. Greater reform ambition in both advanced and emerging-market economies would help to enhance living standards, strengthen medium-term prospects for investment and productivity, and allow the benefits of growth to be distributed more widely.

18. **In both advanced and emerging-market economies, the most frequent priorities to be addressed by reforms are in the areas of skills and education and product market regulation.** Amongst the key reforms to take are: helping workers acquire skills by expanding vocational education and training; supporting lifelong learning, particularly in the context of rapid digitalisation; strengthening measures to better target resources on disadvantaged students and schools; and implementing reforms to reduce market segmentation and improve opportunities for women, migrants and older workers. Enhanced efforts to strengthen competition and open up product markets are essential for innovation, the diffusion of digital technologies and ultimately productivity growth and social inclusion. Improved efficiency of tax and transfer policies, including better targeting of transfers, also needs to be an integral part of well-designed policy packages to respond to people's concerns about public services and social benefits, helping to make work pay and strengthening real income growth for poorer households.

19. **At a time of weak global growth, there is also a case for prioritising and packaging reforms that help to support short-term demand, and ensuring that these are implemented with supportive macroeconomic policies.** Part of this package should be a rapid move to reduce restrictions and distortions on cross-border activities and to return to collective action on trade policy issues. This would help to reduce trade policy tensions and the uncertainty that is currently undermining growth prospects in the short- and medium-term.