World Economic Situation and Prospects

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Global issues

Global economy grows at a modest pace

The world economy continues to grow at a modest pace. Growth of world gross product is projected to accelerate slightly from 2.6 per cent in 2014 to 2.8 per cent in 2015—a downward revision by 0.3 percentage points from the forecast presented in the World Economic Situation and Prospects 2015 in January. In 2016, global growth is forecast to improve to 3.1 per cent.

The downward revision in global growth for 2015 reflects mainly a deteriorating outlook in the economies in transition and several large developing countries, especially in South America. Gross domestic product (GDP) in the economies in transition is projected to contract by 2 per cent this year, while average growth in developing countries is expected to remain at 4.4 per cent, about 3 percentage points below the pre-crisis pace.

The growth divergence between the various regions is widening in 2015. This can be partly attributed to the differing impacts from the recent drop in the prices of oil and other commodities (see figure). The prospects for developed economies in 2015 have been slightly upgraded from earlier forecasts, with average growth projected to accelerate from 1.6 per cent in 2014 to 2.2 per cent in 2015. Almost all major developed economies are expected to see a pickup in growth momentum. The upward revision reflects a moderately improved outlook for the euro area owing to a number

Summary

- Global economy grows at a modest pace
- Recovery in Western Europe gradually becoming more broadly based, but still fragile
- Economic growth downgraded for commodity exporters, while more diversified economies benefit from lower commodity prices

Table: **Growth of world output 2013–2016 (annual percentage change)**

	Annual percentage change				Change from January 2015 forecast (percentage points)	
	2013	2014	2015	2016	2015	2016
World	**2.5**	**2.6**	**2.8**	**3.1**	**-0.3**	**-0.2**
Developed economies	**1.2**	**1.6**	**2.2**	**2.2**	**0.1**	**-0.1**
United States of America	2.2	2.4	2.8	2.7	0.0	-0.4
Japan	1.6	0.0	1.2	1.0	0.0	-0.1
European Union	0.0	1.3	1.9	2.1	0.2	0.1
Economies in transition	**2.0**	**0.7**	**-2.0**	**0.9**	**-3.1**	**-1.2**
Russian Federation	1.3	0.4	-3.0	0.1	-3.2	-1.1
Developing economies	**4.7**	**4.4**	**4.4**	**4.8**	**-0.4**	**-0.3**
Africa	3.3	3.3	4.0	4.8	-0.6	-0.1
East Asia	6.4	6.1	6.0	6.0	-0.1	0.0
China	7.7	7.4	7.0	6.8	0.0	0.0
South Asia	4.9	6.3	6.7	6.9	1.3	1.2
India	6.4	7.2	7.6	7.7	1.7	1.4
Western Asia	3.1	3.0	3.0	3.6	-0.7	-0.7
Latin America and the Caribbean	2.7	1.0	0.5	1.7	-1.9	-1.4
Brazil	2.5	0.1	-1.1	0.5	-2.6	-1.9
Least developed countries	5.3	5.2	4.9	5.6	-0.8	-0.3

Source: UN/DESA/GEMU.

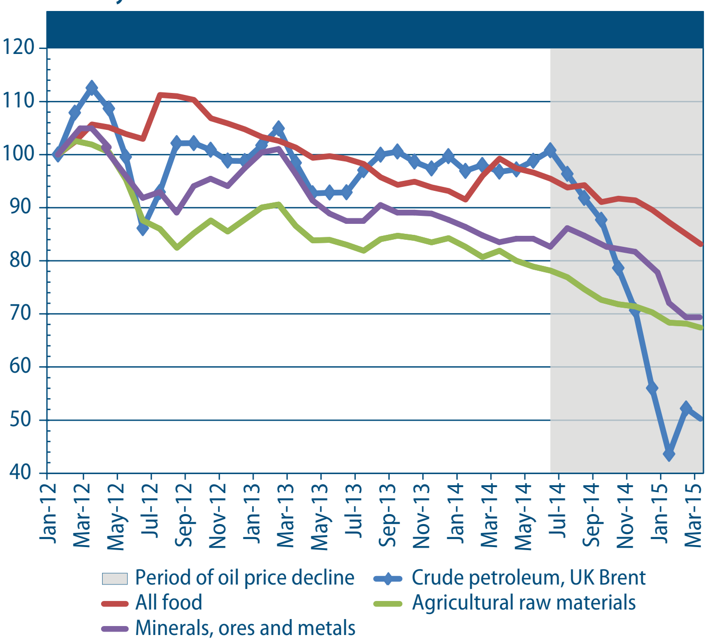
Prepared by the Global Economic Monitoring Unit: Pingfan Hong (Chief), Sergio P. Vieira (Coordinator), Dawn Holland, Hoi Wai Cheng, Grigor Agabekian, Hung-Yi Li, Matthias Kempf, Ingo Pitterle, John Winkel and Sebastian Vergara, supported by Mary Lee Kortes, Nancy Settecasi, Leah C. Kennedy, Cordelia Gow, Ann D'lima, and Gabe Scelta.

All data indicated in this document is year on year, unless otherwise specified.

Contact email: hong@un.org, http://www.un.org/en/development/desa/policy/wesp/wesp_mb.shtml

of factors, including lower energy prices and significant currency depreciation following the European Central Bank's (ECB) new large-scale asset-buying program. Despite expectations of a more robust recovery, developed economies continue to face considerable headwinds from the legacies of the global financial crisis, including subdued employment levels, elevated private and public sector debt, and financial sector fragilities.

Figure
Price indices of selected groups of commodites, January 2012–March 2015



Source: UNCTADstat.

There are still considerable downside risks to the baseline forecast, related to the upcoming move towards monetary policy normalization in the United States of America, ongoing uncertainties in the euro area, potential spillovers from geopolitical conflicts and persistent vulnerabilities in emerging economies. The overall subdued performance of the world economy since the global financial crisis has raised concerns of a "new normal" of lower growth, especially in view of a broad-based weakness in investment.

Monetary, fiscal and labour market policy challenges

Growing divergence in the monetary policy stances of the United States and much of the rest of the world presents considerable macroeconomic policy challenges for many countries. For the Fed, the key challenge is to manage the pace and sequence of normalizing the policy rate so as to maintain macroeconomic stability, and support growth and employment, while at the same time preventing an unwarranted build-up in asset prices. The main monetary policy challenge for many developing economies is to find a balance between easing the policy stance to support growth and stemming currency depreciation, and maintaining capital inflows in the face of the upcoming Fed normalization.

On the fiscal side, public debt levels in many developed economies still remain elevated, averaging 100 per cent of GDP in 2014. Accordingly, reforms in the structure of public expenditure, including the entitlements programmes, are kept on the agenda. Nonetheless, the focus of fiscal policy is slowly shifting from stabilization of public finances to addressing labour market problems and bolstering potential output. As a consequence, most developed economies should face less fiscal drag in 2015-2016 than in the past few years. Fiscal policy, however, remains fairly restrictive in parts of the euro area, weighing on demand and adding to deflationary pressures. In developing countries and economies in transition, budget deficits and public debt levels are generally lower than in developed economies. The sharp oil price decline has allowed fiscal authorities in several oil-importing countries to cut fuel subsidies, improving their budget balances. For oil-exporters, however, lower oil prices pose significant challenges.

In labour markets, despite recent improvements, employment growth remains slow and unemployment rates are still elevated in developed economies as a whole. A significant part of this situation reflects weak aggregate demand. Thus, macroeconomic policies to stimulate aggregate demand, such as targeted infrastructure investments, should be a priority to reduce cyclical unemployment and improve medium-term growth prospects. Weak wage growth is currently another major labour market challenge. In developed economies, wage growth declined rapidly during the crisis and has not recovered since then, contributing to a widening gap between growth in real wages and labour productivity, and to feeble aggregate demand. Several countries have introduced changes to wage policies to improve workers' prospects and stimulate aggregate demand. Setting an adequate minimum wage level is, however, the main challenge, as the level must ensure effectiveness in stimulating demand while avoiding adverse employment effects.

Developed economies

North America: in the United States, economic recovery remains on track

In the United States, the economic recovery remains on track and the short-term outlook is relatively favorable. Following strong expansions in the second and third quarters of 2014, growth has since slowed noticeably. The weak performance in early 2015 can be attributed to less investment in the energy sector, disturbances to international cargo shipping and bad weather. Growth is expected to pick up over the next quarters and reach 2.8 per cent in 2015, before decelerating slightly to 2.7 per cent in 2016. Continuous improvement in the labour market will prompt private consumption. Business fixed investment will also expand solidly. However, in addition to subdued demand from trade partners, export growth may also be dampened by the significant appreciation of the US dollar since mid-2014. The Fed is expected to start raising its policy rate during the second half of 2015, but will follow a cautious approach.

Growth in Canada is expected to slow from 2.5 per cent in 2014 to 2.1 per cent in 2015, before recovering to 2.6 per cent in 2016. The slowdown mainly reflects reduced investment in the oil sector and falling government revenues amid low oil prices. Higher manufacturing exports, due to stronger growth in the United States and the depreciation of the Canadian dollar, are expected to mitigate the slowdown.

Developed Asia: weak economic expansion in Japan

Japan's GDP is projected to grow by 1.2 per cent in 2015 and 1.0 per cent in 2016. In 2014, the Japanese economy suffered from the consumption tax rate hike and fell into recession by mid-year. The tepid recovery that started in the fourth quarter helped lift GDP to the same level as in the previous year. The Japanese Government has decided to postpone a second tax hike from October 2015 to April 2017. However, weak growth in wages and labour income will fail to make up for the higher price level, and private consumption is expected to further recede slightly in 2015 before resuming growth in 2016. Long after the significant depreciation of the Japanese yen started, export volumes began to increase in late 2014 and are expected to provide support for growth. Since October 2014, the Bank of Japan has increased the scale of its asset purchasing programme to 80 trillion yen per year, further strengthening its efforts to bring the inflation rate back to the 2 per cent target.

Western Europe: a broadening recovery

The fragile economic recovery in Western Europe is gradually becoming more broadly based, supported by low oil prices, currency depreciation, expansive monetary stimulus programmes, declining consumer prices and some easing of the pressure for fiscal consolidation. While the EU-15 expanded by just 1.2 per cent last year, growth strengthened in the second half of 2014 and into the first quarter of 2015, and is expected to continue to improve this year. GDP is expected to grow by 1.8 per cent in 2015 and 2.0 per cent in 2016. Stronger consumer spending is underpinned by rising real incomes, given the unexpectedly sharp drop in oil and consumer prices.

In response to deflation risks, the ECB announced a significant loosening of the monetary stance in January 2015. This has been reflected in recent exchange rate and asset price movements, has given a boost to confidence, and, according to the latest Bank Lending Survey by the ECB, has been associated with easing credit conditions and an increase in lending, especially to enterprises. All of these factors should support economic recovery in the euro area this year. However, the improving euro area outlook relies on a timely agreement between Greece and the Eurogroup of Finance Ministers over financing arrangements, which have yet to be clarified.

The new EU members: moderate, but stable growth expected to strengthen further

Aggregate GDP growth in the new European Union (EU) member States, which reached 2.7 per cent in 2014, is expected to further strengthen to 2.8 per cent in 2015 and 3.2 per cent in 2016. The positive impact of reviving private demand and a lessening fiscal drag will be supported by accommodative monetary policies, low energy costs and the pickup in EU-15 economies. While most economies in the region are expected to expand at about 3 per cent in 2015, Croatia might see near-zero growth. Although in some countries foreign-currency denominated household debt remains a problem—further aggravated by the appreciation of the Swiss franc in January—continuing real-wage growth is expected to bolster household spending. Investment is expected to remain on an upward trend and labour markets are improving. Lower energy and food prices resulted in negative annual inflation in several countries in 2014, with positive, but very low inflation expected for 2015.

Economies in transition

CIS: growth prospects downgraded

Growth prospects for the Commonwealth of Independent States (CIS) region in 2015-2016 have been downgraded against the backdrop of low oil prices, military conflict in the East of Ukraine and economic sanctions against the Russian Federation. The aggregate GDP of the CIS and Georgia is expected to contract by 2.1 per cent in 2015 and expand only modestly by 0.9 per cent in 2016. Although the direct impact of sanctions on the Russian economy has been relatively limited, they have contributed to capital outflows, currency depreciation and a weakening in business confidence. The Russian economy is expected to shrink by about 3 per cent in 2015, as weak business sentiment and high interest rates deter investment and high inflation weighs on private consumption. Ukraine's economy is expected to contract sharply owing to the conflict in the industrial part of the country, fiscal tightening and a fall in private consumption.

Lower oil and gas revenues will lead to a growth moderation in energy-exporting countries, such as Azerbaijan and Kazakhstan. For lower-income energy-importing economies, such as Armenia, Kyrgyzstan, Moldova and Tajikistan, the partial loss of the Russian market and the declining value of remittances outweigh the benefits of lower fuel costs, while fewer opportunities for labor migration have increased labour market pressures. Most of the CIS currencies either were devalued or depreciated significantly in the past year, spurring inflation, in some cases to double-digit levels. Weaker currencies will partly offset fiscal losses in the energy-exporting CIS economies, but many Governments will nonetheless need to draw from their sovereign reserve funds. The weaker currencies will at the same time undermine private consumption and put pressure on the banking systems, constraining credit expansion. The establishment of the Eurasian Economic Union of Armenia, Belarus, Kazakhstan and the Russian Federation in January 2015—Kyrgyzstan is also set to join the union—should bolster intra-regional economic ties, although many aspects of the integration process still have to be agreed.

South-Eastern Europe: the region should benefit from pickup in the EU

The aggregate GDP of South-Eastern Europe is expected to expand by 1.4 per cent in 2015 and 2.5 per cent in 2016. Stronger growth rates will be needed to address the region's structural problems. In 2014, the Serbian economy, hit by devastating floods and curbed by fiscal retrenchment, contracted by 1.8 per cent. The former Yugoslav Republic of Macedonia, by contrast, registered growth of 3.6 per cent on the back of strong public investment and increased food exports. In 2015, the region is expected to benefit from the pickup in the EU and see moderate strengthening in foreign direct investment. However, fiscal austerity in Serbia will weigh on short-term growth. Record-low inflation was observed in 2014, and the low-inflation trend is likely to continue in 2015.

Developing economies

Africa: GDP accelerating at the aggregate level, amid a more diverse growth picture

Falling commodity prices and declining exchange rates are painting a mixed picture for Africa, with strong divergence between oil-exporting and oil-importing economies. Average growth is expected to reach 4.0 per cent in 2015 and 4.8 per cent in 2016, which is significantly lower than the previous forecast. Central Africa and North Africa have seen the biggest downward revisions for 2015, with the security situation playing a major role. Average inflation in Africa remains on a downward trend, projected to slow to 7.0 per cent in 2015 and 6.5 per cent in 2016. Some of the expected decline has been offset by imported inflation due to currency depreciations. Monetary policies in many countries are expected to remain mostly unchanged, as policymakers balance between forestalling exchange-rate depreciations and supporting growth. Overall, fiscal policies will be expansionary, particularly in the (many) countries that are having elections over the forecast period. Fiscal deficits are projected to narrow slightly in aggregate, driven by lower commodity prices, although deficits in some oil exporters are projected to rise. Lower commodity prices will narrow oil exporters' current-account surpluses and push some into deficit. Risks to the forecast are related to a significant change in oil prices and to further geopolitical instability or further slowdowns in major trading partners.

East Asia: the region remains a key driver of global growth

The aggregate East Asian economy is forecast to grow by 6.0 per cent in both 2015 and 2016. Growth in many East Asian economies is expected to accelerate in 2015. Papua New Guinea and Thailand are projected to experience the strongest growth improvements. The former will receive a boost from the first full-year of production at its key liquefied natural gas project, while improved political stability in the latter is expected to boost tourism and government spending. China is projected to grow by 7 per cent in 2015 and 6.8 per cent in 2016. Weaker-than-expected data in early 2015 will likely prompt further accommodative fiscal and monetary policy measures.

The region's export growth is projected to pick up as stronger demand in developed economies offsets the impact of China's slowing growth. Government spending will increase in most economies, which will help spur investment growth. Central banks in China, Indonesia, the Republic of Korea and Thailand cut their policy rates in the first quarter of 2015. However, concerns over debt levels, asset bubbles, and capital outflows limit the willingness of authorities to further ease monetary policy. East Asian currencies showed resilience against the US dollar in the first quarter of 2015. Most of them appreciated in trade-weighted terms, accentuating the trend observed since the global financial crisis and weighing on export growth.

South Asia: growth in South Asia expected to strengthen, led by India

South Asia's economic outlook is largely favourable. Most economies are expected to see a strengthening of growth in 2015-16 following stronger domestic consumption and investment, and a pickup in exports. The region's GDP is projected to grow by 6.7 per cent in 2015 and 6.9 per cent in 2016, up from an estimated 6.3 per cent in 2014. India's economy is forecast to expand by 7.6 per cent in 2015 and 7.7 per cent in 2016, making it the world's fastest-growing large economy. The prospects for the Islamic Republic of Iran and Pakistan have also improved moderately, although in both countries significant uncertainties remain. Following the devastating earthquake, growth in Nepal has been lowered for 2015, but reconstruction activities should support growth in 2016. Across South Asia, the expansion is expected to be driven by strong household consumption and a recovery in investment, underpinned by a more benign macroeconomic environment. With oil and food prices declining, average inflation is projected to fall to its lowest level in almost a decade. As a result, several central banks, for example in India, Pakistan and Sri Lanka, have loosened monetary policy. Despite the improved outlook, South Asia's economies face, to varying degrees, long-standing development challenges including energy shortages, infrastructure deficits and political and social unrest.

Western Asia: more diversified economies expected to perform better than anticipated

In Western Asia, economic conditions continue to be hampered by several conflicts in the region. Lower oil prices weigh heavily on oil-exporting economies, while the more diversified economies are expected to perform better than anticipated. The region is projected to register 3.0 per cent growth in 2015, the same rate as in 2014. In 2016, growth is expected to improve to 3.6 per cent, boosted by rising oil prices and stronger external demand. At the subregional level, the GCC member countries are expected to experience a modest economic expansion in 2015, given sluggish oil output growth. Economic activity will be supported by large fiscal stimulus programmes, targeting mainly infrastructure projects. Fiscal deficits are therefore expected to widen during the forecast period. Conversely, the more diversified economies are expected to perform better in 2015, benefiting from more competitive exchange rates, lower oil prices, and more monetary policy space to stimulate domestic demand. This combination of factors will support growth and help reduce current-account deficits in 2015, particularly in Turkey. There are, however, considerable downside risks to this forecast. Geopolitical conflicts, in particular the recent conflict in Yemen, could escalate, hampering domestic economic activities and regional trade. If oil prices remain at the current low level for longer than forecast, oil-exporting economies will face fiscal pressures, aggravating growth prospects for 2016.

Latin America and the Caribbean: economic conditions deteriorate further

The economic prospects in Latin America and the Caribbean have worsened noticeably, amidst lower commodity prices and persistent domestic fragilities. The region is expected to grow by only 0.5 per cent in 2015 and by 1.7 per cent in 2016, albeit with significant heterogeneity across subregions. Economic growth in Mexico and Central America is expected to strengthen moderately in 2015, benefiting from a pickup in activity in the United States. GDP growth in Mexico is expected to reach 2.8 per cent in 2015. By contrast, South America is slowing down markedly with continuous declines in investment. The Bolivarian Republic of Venezuela is falling into a deeper recession, while Brazil and Argentina are expected to contract by 1.1 per cent and 0.4 per cent in 2015, respectively. Other South American economies, such as Bolivia, Paraguay and Peru, will grow more robustly, above 4.0 per cent. Meanwhile, economic growth in the Caribbean is expected to accelerate to 3.1 per cent in 2015. The decline in commodity prices is having widespread effects across the region. For instance, South America's commodity exporters, particularly oil exporters, have experienced significant changes in the terms of trade and thus on their fiscal and external accounts, in addition to weaker investment prospects.