



# The Economic Forecast for Europe

**Oliver DIECKMANN**

European Commission, DG ECFIN

Economic Situation, Forecasts, Business and Consumer Surveys

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## *The economic forecast for Europe*

# Main messages



### *"Expansion to continue amid new risks"*

- Economic expansion set to continue in all Member States
- Labour market improvements continue
- Inflation expected to move up very gradually
- Public finances are improving further
- External downside risks have risen

Source: Commissioner Moscovici's slides at the SF18 press conference on 3 May 2018



*The economic forecast for Europe*

# The story behind the messages

1. **Central scenario: "*Expansion to continue amid new risks*"**
  - central scenario roughly unchanged from previous forecasts
  - higher growth contributions from net exports and investment
  - downside risks have increased (e.g. financial shocks, protectionism)
2. **Shaking off the crisis experience: a typical expansion?**
  - growth momentum in comparison with previous recoveries
  - putting investment growth into perspective
3. **The output gap, slack, and inflation: above-potential growth ahead?**
4. **Risks: "Trade disputes could blow expansion off course"**

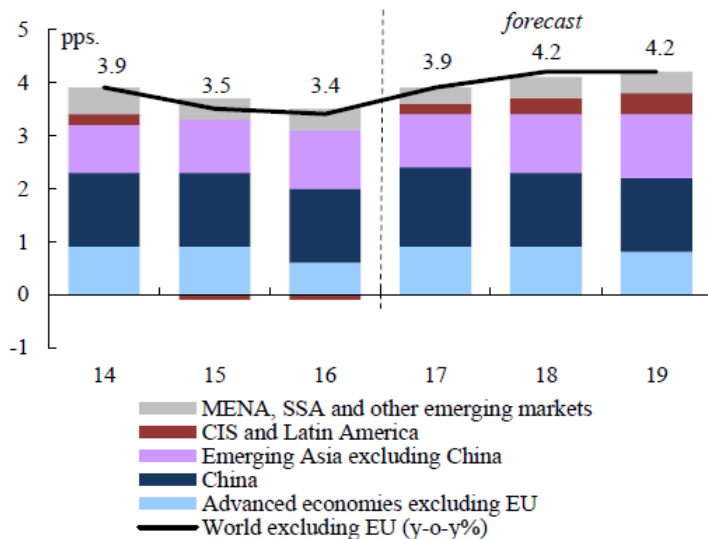


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# 1. The central scenario

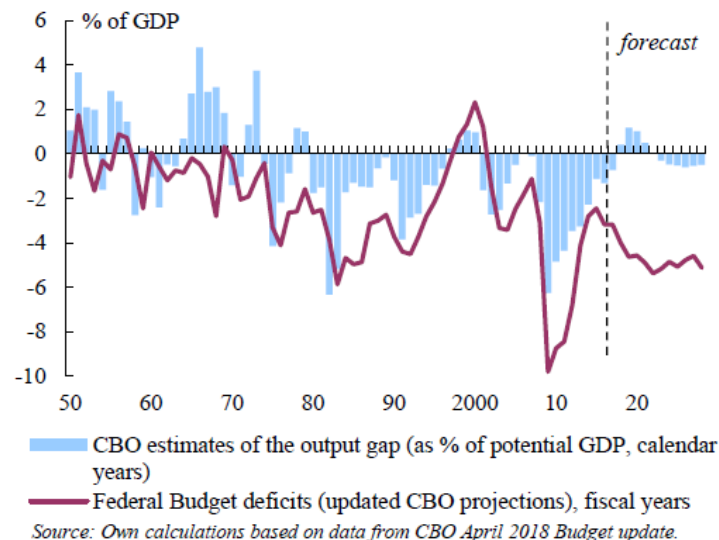
## Global expansion has strengthened...

Graph: Global GDP growth (excl. EU)



## ...with spillovers from pro-cyclical US fiscal policy.

Graph: US Federal Budget deficit and output gap (CBO April 2018 Budget update)

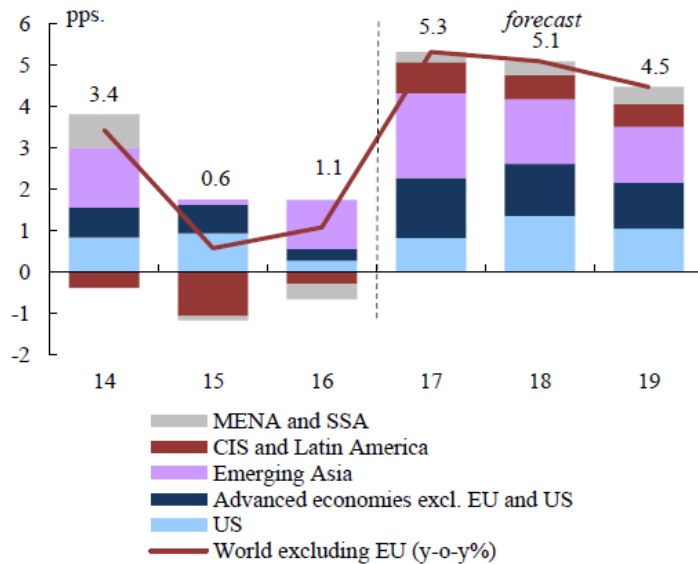


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### 1. Central scenario (world trade, oil prices)

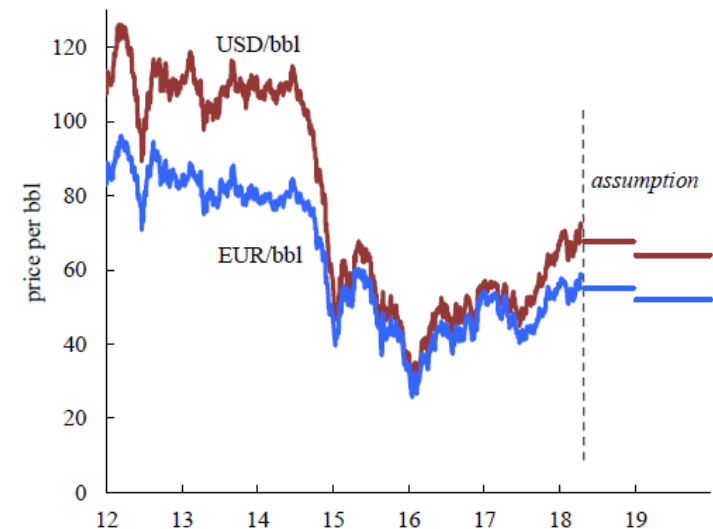
#### Global trade has gained momentum in 2017

Graph: World import growth (excl. EU)



#### Oil prices assumptions had to be revised up

Graph: Oil price assumptions



Source: Macrobond.

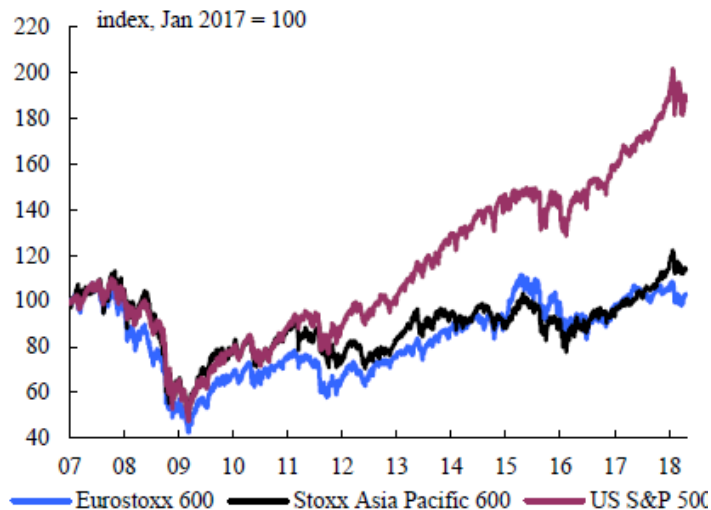


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### 1. Central scenario (financial markets)

#### The **stock market** turmoil in early February 2018 was short-lived

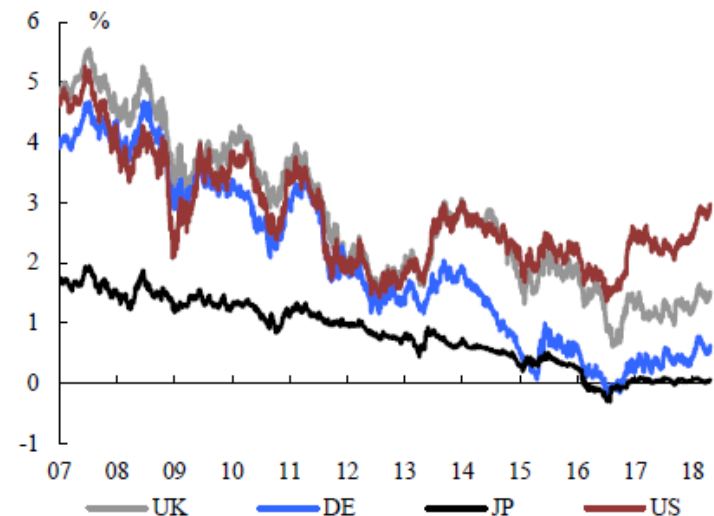
Graph: Stock market performance



Source: Macrobond.

#### **Bond yields** slightly higher, but very low in historical perspective

Graph: Benchmark 10y govt. bond yields



Source: Macrobond.



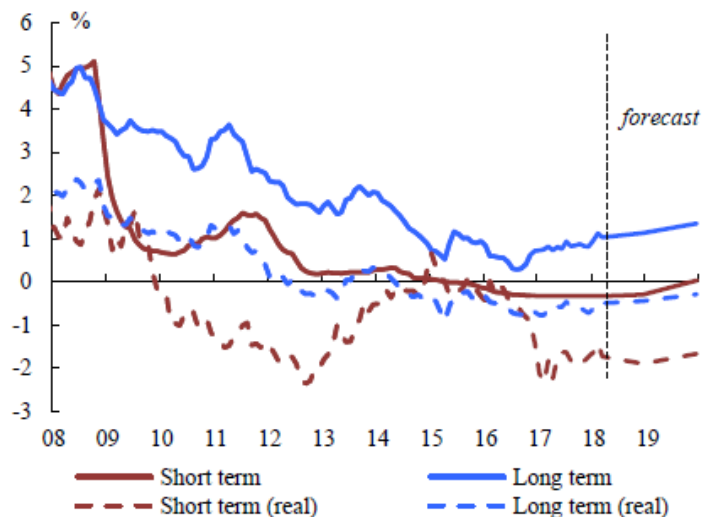


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### 1. Central scenario (monetary policy)

**Monetary policy remains very accommodative...**

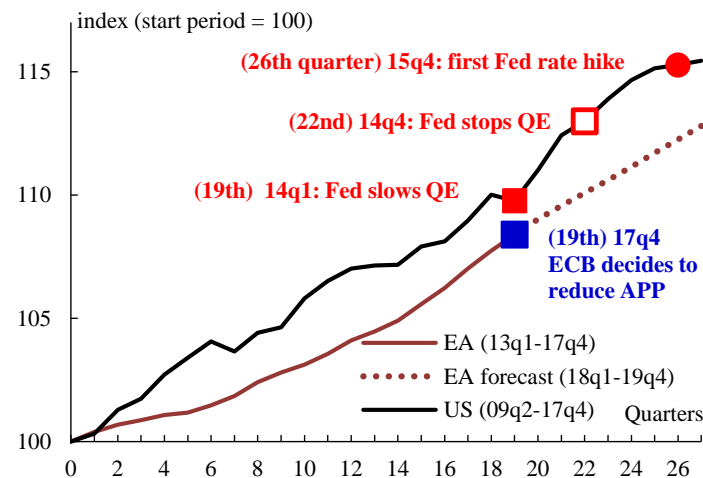
Graph: Interest rates (EA)



Short term rate: 3M Euribor; Long term rate: 10Y interest swap.

**...with the withdrawal of stimulus being discussed.**

Graph: GDP during current expansions in the US and in the EA and monetary policy



Data sources: AWM database, Eurostat and European Commission's Spring 2018 forecast; FRED database for US data.

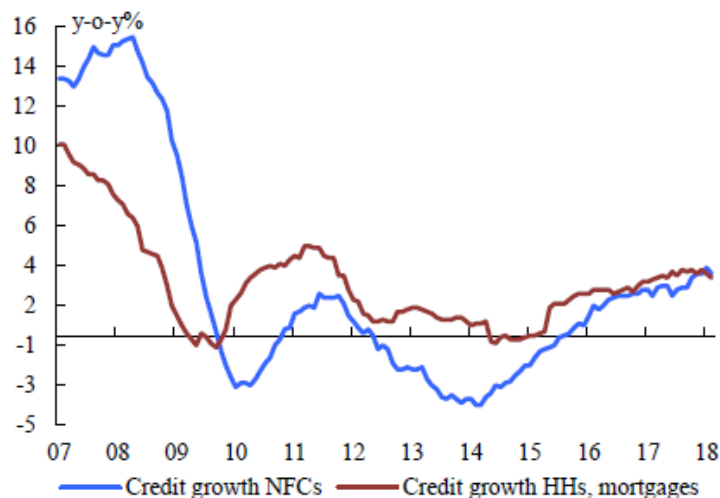


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### 1. Central scenario (financing side)

#### Cyclical upturn of bank lending continues...

Graph: Bank lending to households and non-financial corporations (EA)



Source: ECB.

#### ...and should strengthen, the financial outlook suggests.

**NEW Table:** Financing side – euro area and EU (EU data not shown below)

Table I.2:  
Financing side - euro area and EU

| (Annual percentage change)                 | Euro area |       |       |                      |       |       |
|--|-----------|-------|-------|----------------------|-------|-------|
|  |           |       |       | Spring 2018 forecast |       |       |
|  | 2014      | 2015  | 2016  | 2017                 | 2018  | 2019  |
| Credit to the domestic private sector      | -0.6      | 0.2   | 1.7   | 2.1                  | 3.3   | 3.8   |
| (% of GDP)                                 | 113.0     | 109.2 | 107.8 | 105.4                | 104.8 | 104.9 |
| - Credit to households                     | -0.3      | 1.9   | 2.3   | 3.2                  | 3.8   | 4.2   |
| (% of GDP)                                 | 51.0      | 50.2  | 50.2  | 49.9                 | 49.8  | 50.1  |
| - Credit to other domestic private sectors | -0.9      | -1.3  | 1.1   | 1.2                  | 2.9   | 3.3   |
| (% of GDP)                                 | 62.0      | 59.0  | 57.6  | 55.5                 | 55.0  | 54.8  |
| Short-term interest rate (%)               | 0.2       | 0.0   | -0.3  | -0.3                 | -0.3  | -0.1  |
| Long-term interest rate (%)                | 2.0       | 1.1   | 0.8   | 1.0                  | 0.6   | 0.8   |
| Nominal effective exchange rate            | 2.5       | -6.0  | 4.1   | 2.1                  | 4.9   | 0.2   |



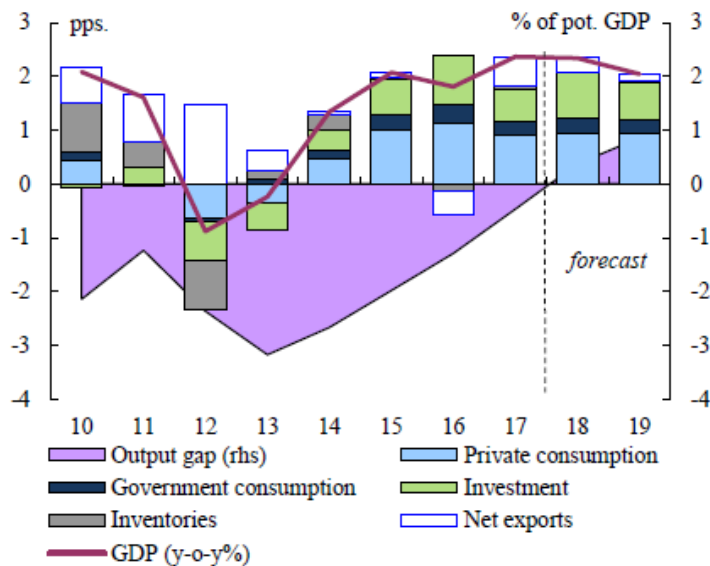


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### 1. Central scenario (GDP; current account)

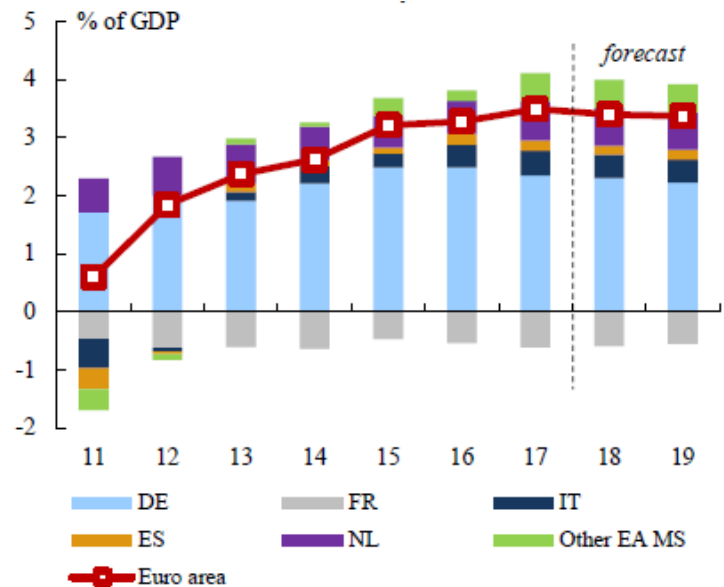
#### Main growth contributions from domestic demand...

Graph: Real GDP and components, euro area



#### ...but the dependence on the external sector makes the economy vulnerable.

Table: Current account balance (EA)



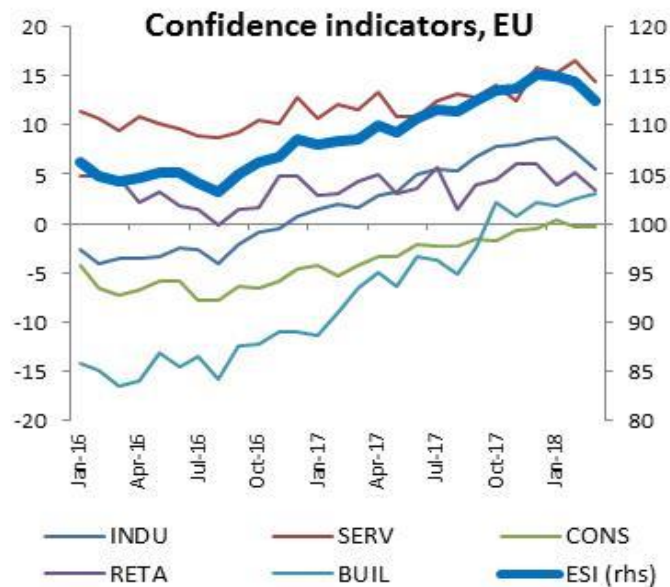


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### 1. Central scenario (short-term outlook)

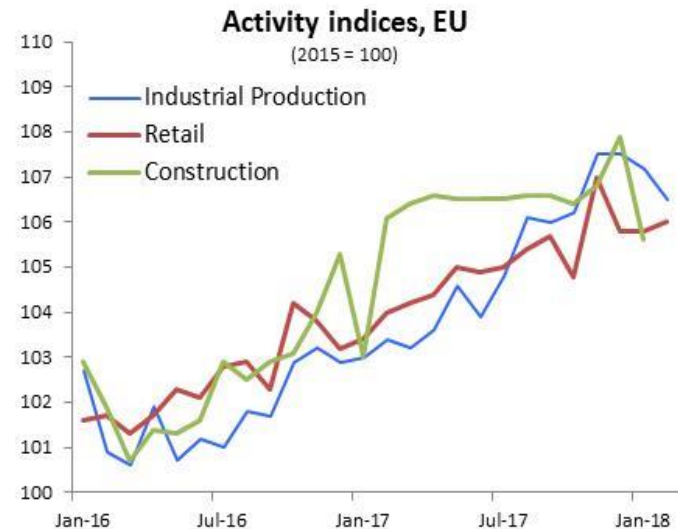
**Surveys** and short-term data surprised on the negative side...

Graph: Confidence indicators, EU



...suggesting a lower **growth momentum** in the near term.

Graph: Selected activity indices



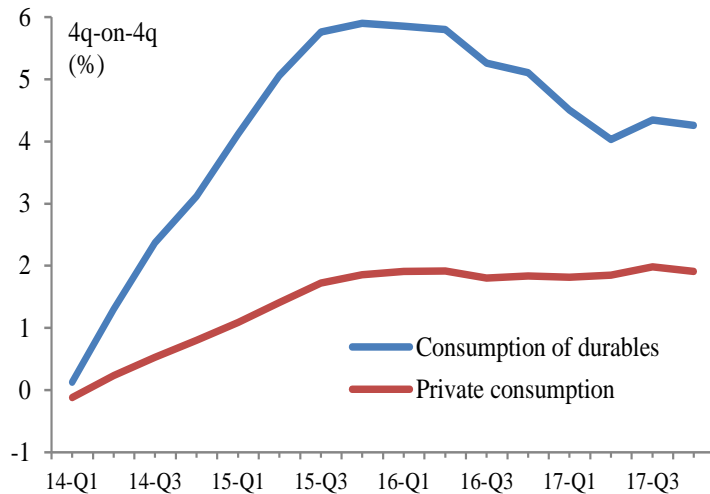


## The economic forecast for Europe

### 1. Central scenario (private consumption 1/2)

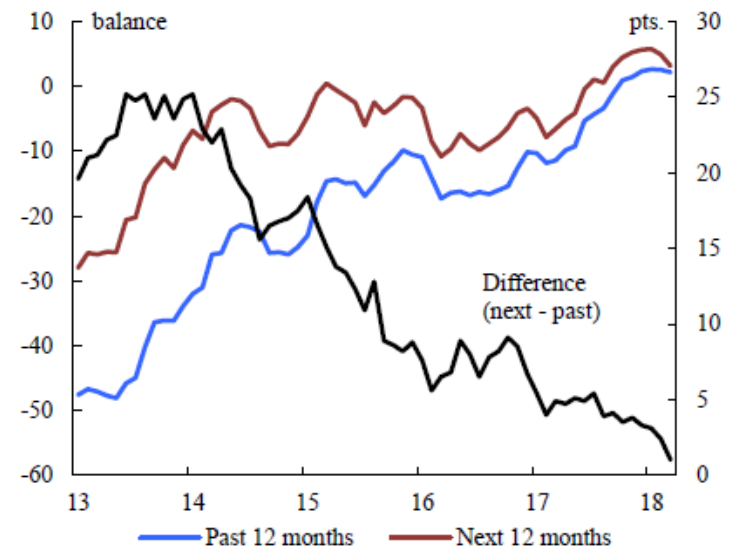
#### Private consumption of durables has lost momentum...

Graph: Total and durable consumption (EA w/o SK)



#### ...but surveys hint on optimistic consumers...

Graph: Consumers' assessment of the past and future general economic situation (EA)



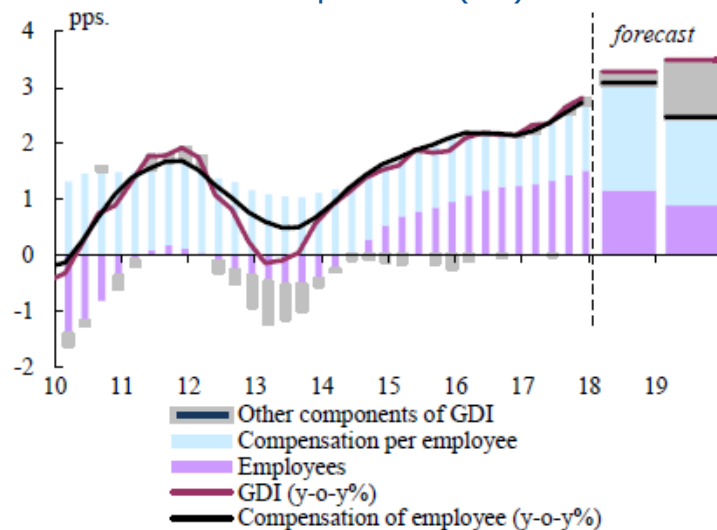


## The economic forecast for Europe

### 1. Central scenario (private consumption 2/2)

...and with **disposable incomes** growing solidly...

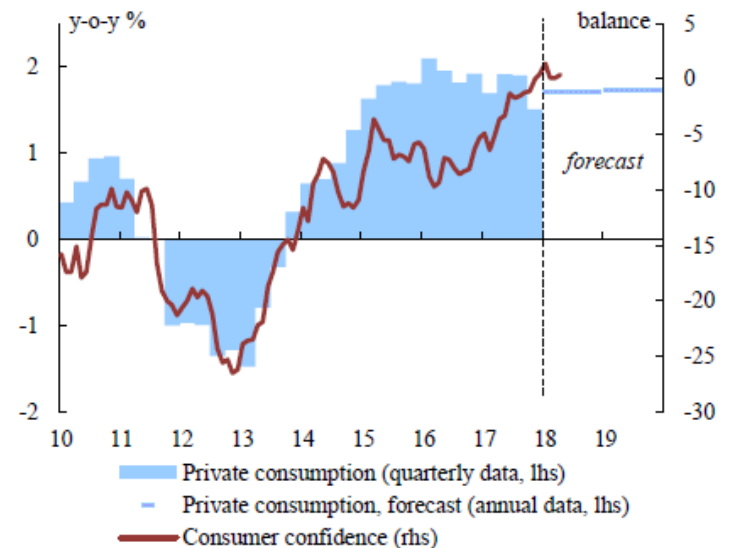
Graph: Gross disposable income (GDI) and its components (EA)



Note: Forecast figures are annual data.

...private consumption is set to grow steadily.

Graph: Private consumption and consumer confidence, euro area

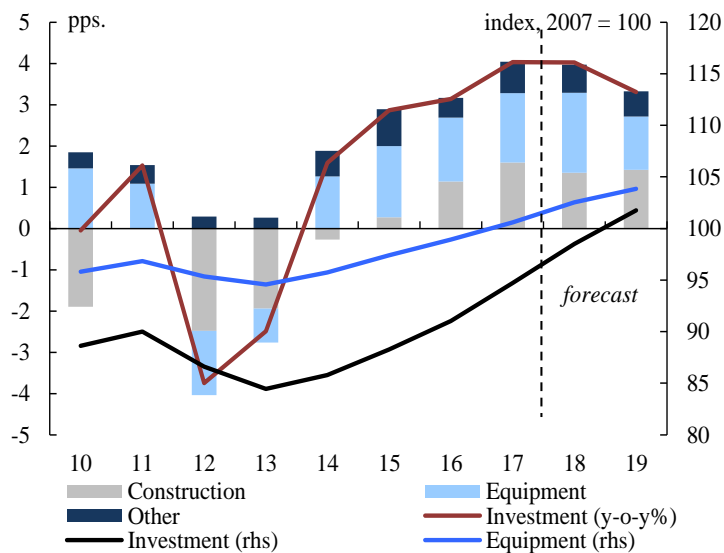




## The economic forecast for Europe 1. Central scenario (investment)

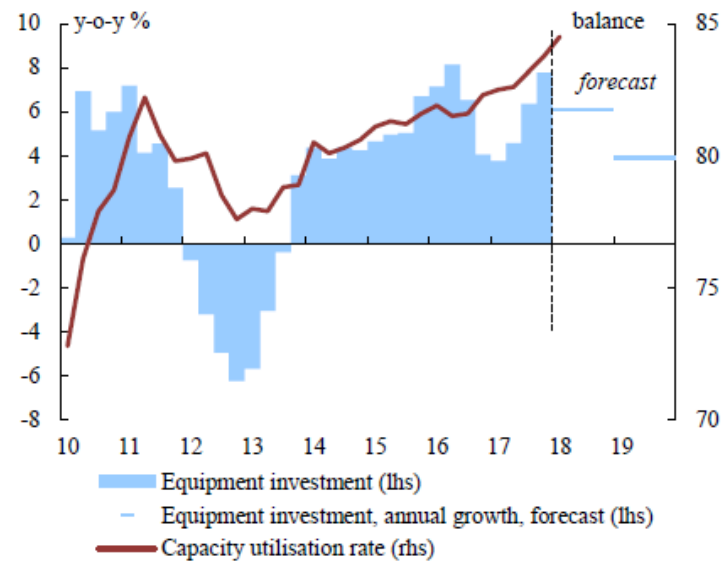
**Investment activity has strengthened...**

Graph: Investment (EA excl. Ireland)



**...with equipment investment expanding strongly.**

Graph: Equipment investment and capacity utilisation (EA)



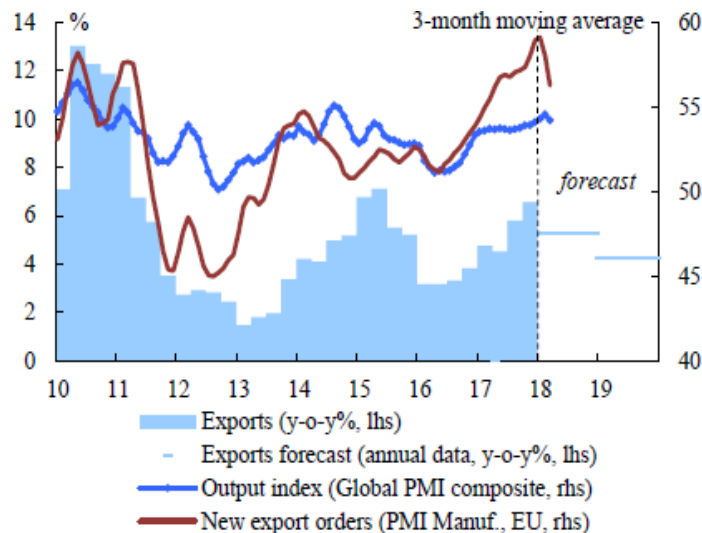


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### 1. Central scenario (exports, GDP)

#### Global demand growth supports European exports

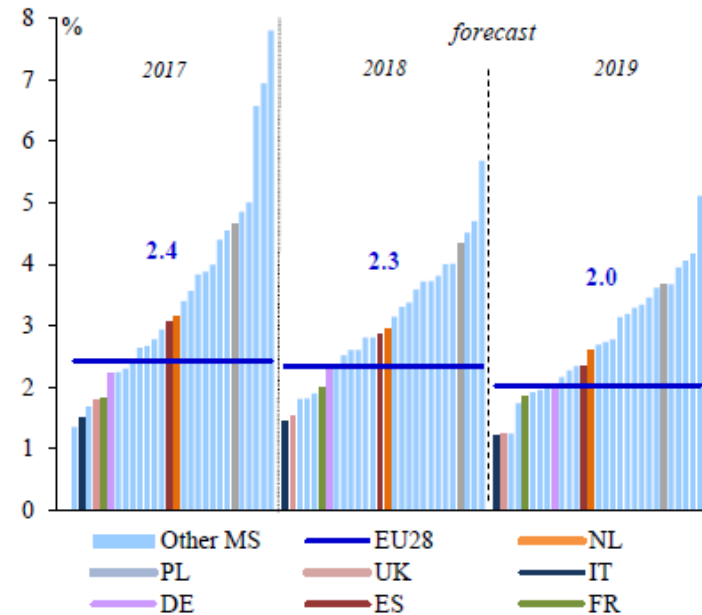
Graph: Global demand, exports and new export orders (EA)



Source: European Commission, Markit.

#### Overall, a slight moderation of growth in Member States

Graph: Real GDP growth, EU and Member States



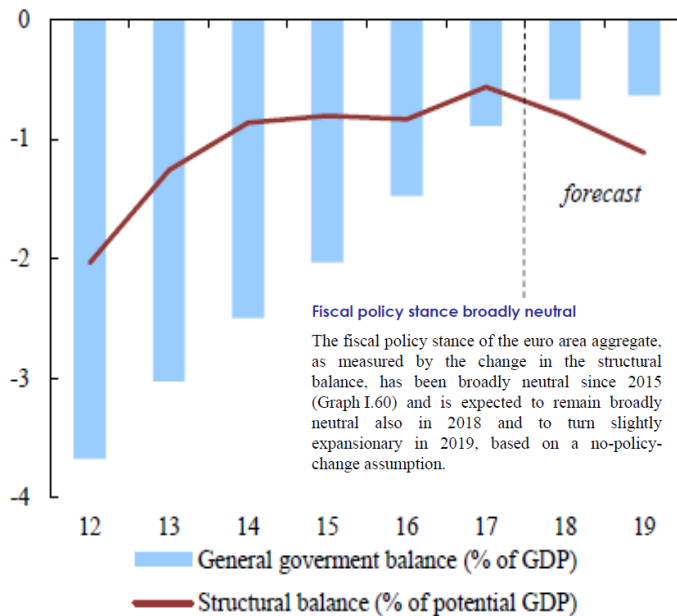
The bars for all 28 current Member States are ranked by size.

## The economic forecast for Europe 1. Central scenario (public finances)

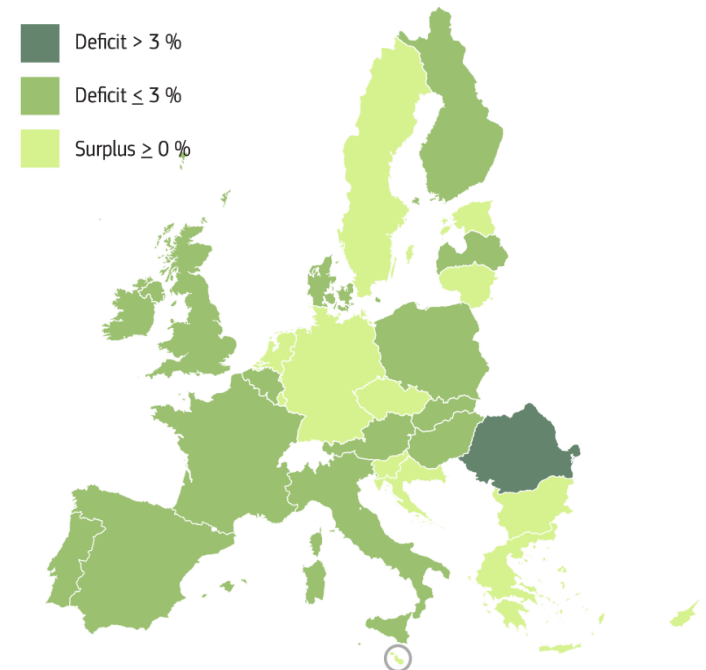
Aggregate headline and structural balances down...

...and deficits below 3% in 27 EU Member States in 2018.

Graph: Budgetary developments (EA)



Graph: Budgetary map, 2018 (SF18)



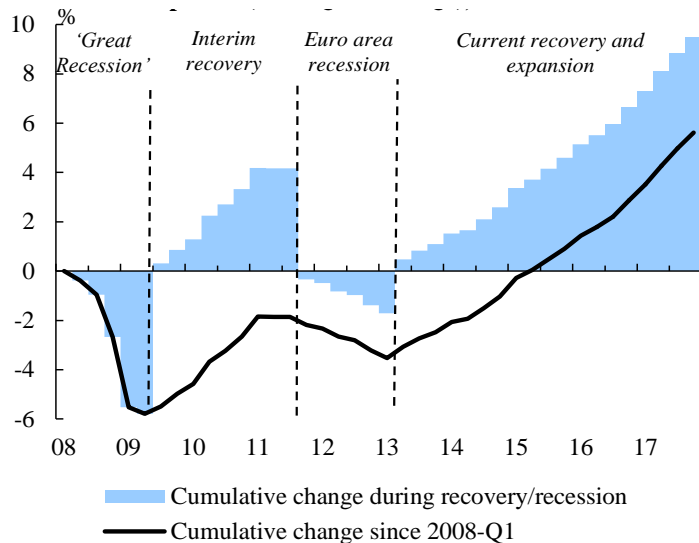


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## 2. A more typical recovery?

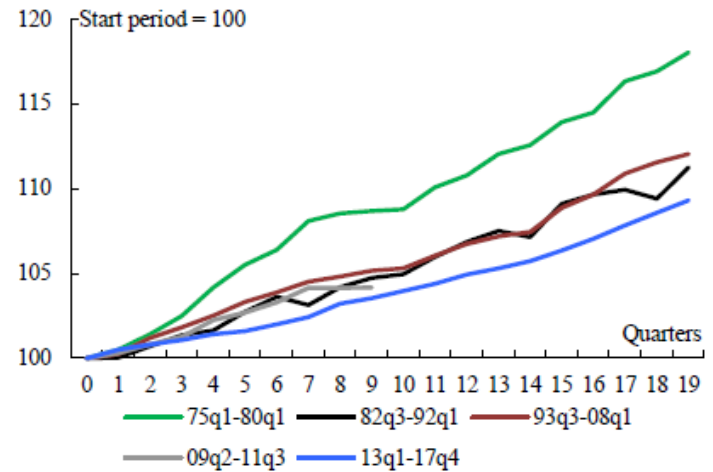
### A view on real GDP in the post-crisis years...

Graph: GDP during cyclical phases (EA)



### ...and an assessment of the recovery years.

Graph: Comparison of GDP recoveries (EA)



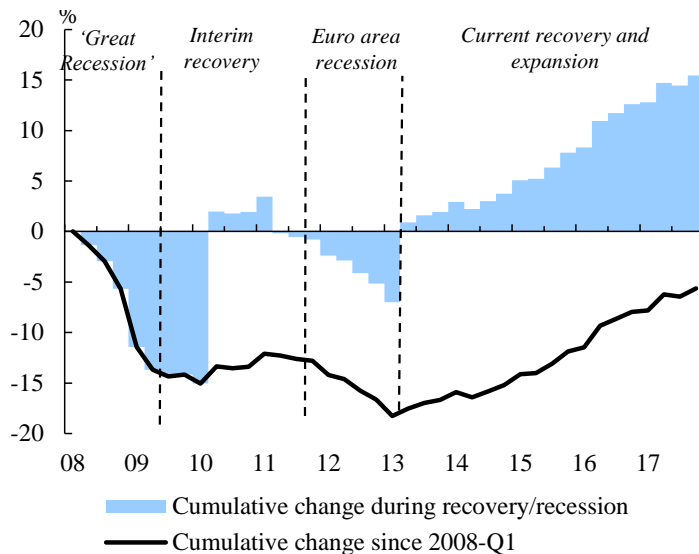
Note: Recoveries according to decisions by the CEPR Business Cycle Dating Committee (data sources: AWM database and Eurostat).

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### 2. A more typical recovery? (investment)

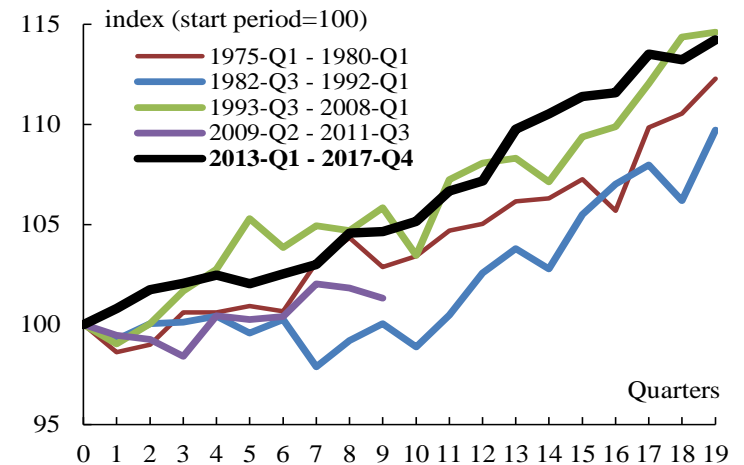
#### A view on investment in the **post-crisis years...**

Graph: Investment during cyclical phases (EA)



#### ...and an assessment of the **recovery years.**

Graph: Comparison of investment recoveries (EA)



Note: Recoveries according to decisions by the CEPR Business Cycle Dating Committee (data sources: AWM database and Eurostat)

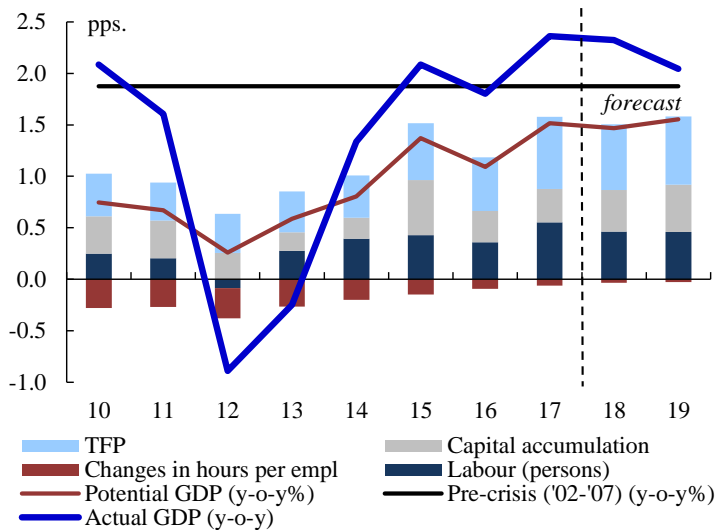


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# 3. Slack and inflation

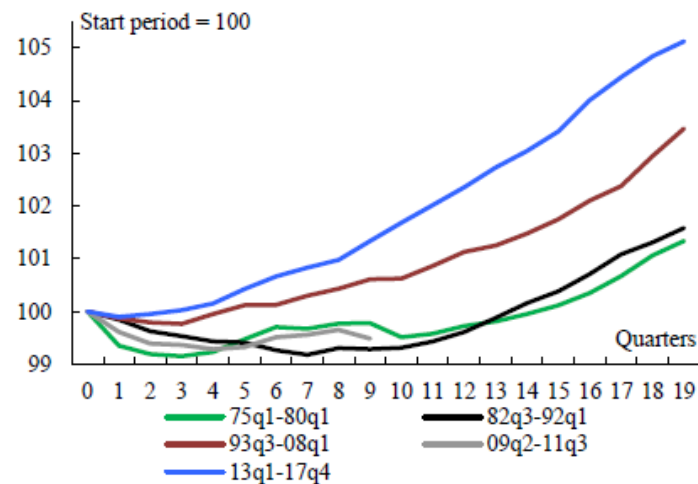
**Above-potential growth is forecast to continue...**

Graph: GDP growth, actual and potential (EA)



**...as the job-rich recovery enters its sixth year...**

Graph: Comparison of recoveries, employed persons (EA)



Note: Recoveries according to decisions by the CEPR Business Cycle Dating Committee (data sources: AWM database and Eurostat).

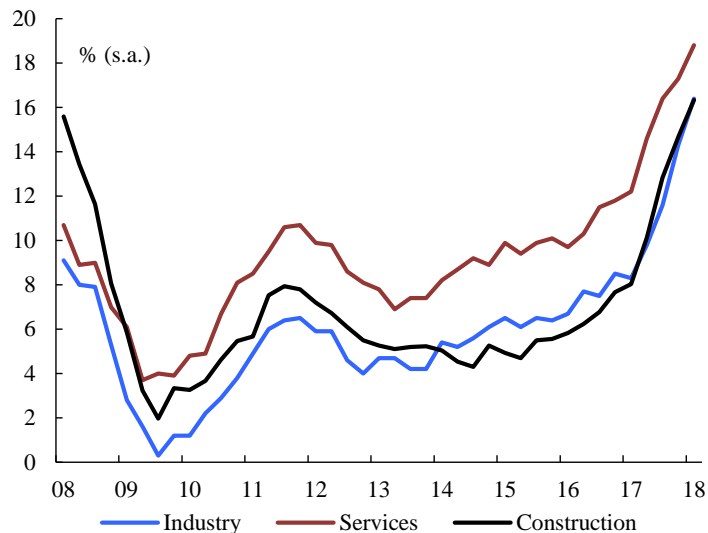


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3. Slack and inflation (shortages vs. slack)

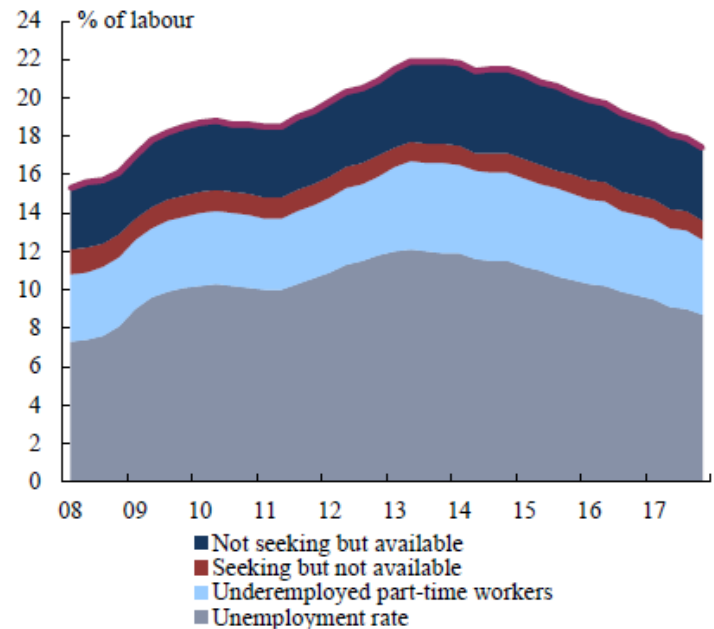
...with increasing concerns about labour shortages...

Graph: Labour seen as limiting factor of activity (EA)



...as slack is receding slowly in the euro area...

Graph: Underemployment (EA)



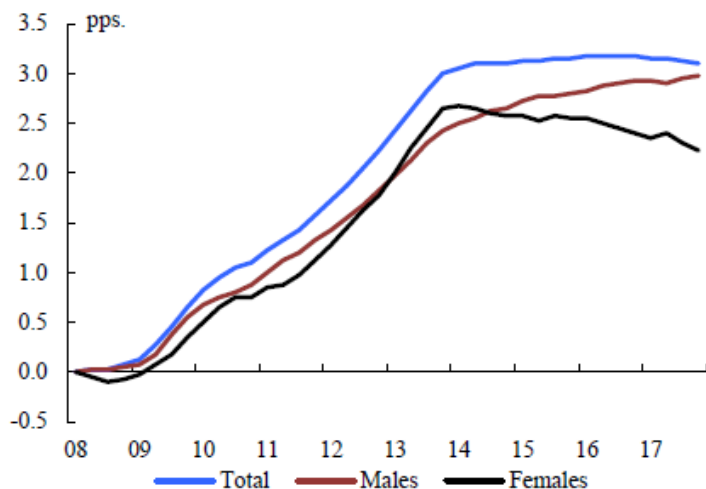


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3. Slack and inflation (part-time, unemployment outlook)

...and the share of **part-time work** is roughly stabilising.

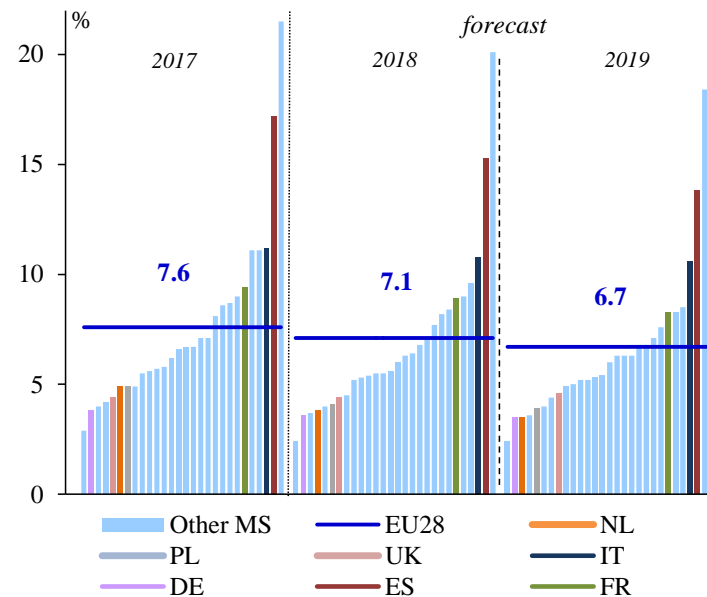
Graph: Part-time employment as a share of total employment since 2008-Q1 (EA)



Note: four-quarter moving averages as compared to the base period 2008-Q1.

Ahead, lower employment growth and smaller declines in the **unemployment rate**

Graph: Unemployment rates (EU and MS)



The bars for all 28 current Member States are ranked by size.

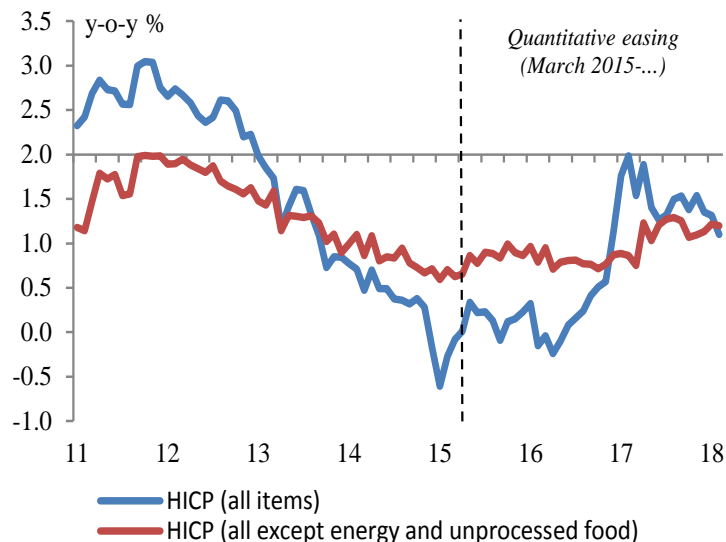


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### 3. Slack and inflation (HICP, seasonal factors)

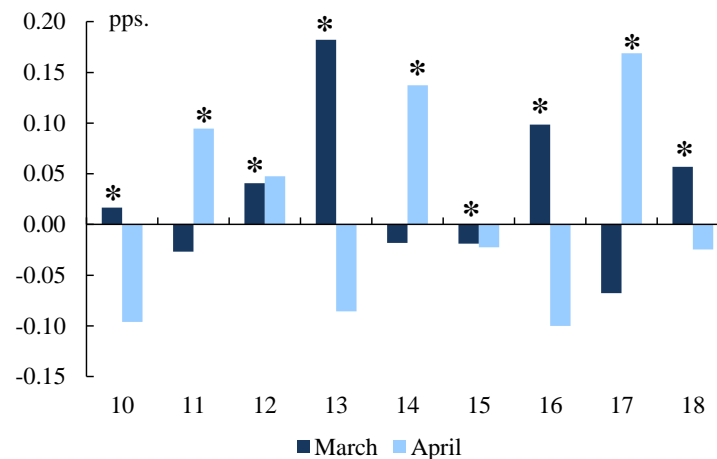
**HICP inflation** has remained subdued...

Graph: HICP headline and core inflation (EA)



...driven by energy prices and **seasonal factors**...

Graph: Package holidays inflation in March and April, contributions to HICP inflation (EA)



\* Months in which the Good Friday week started.

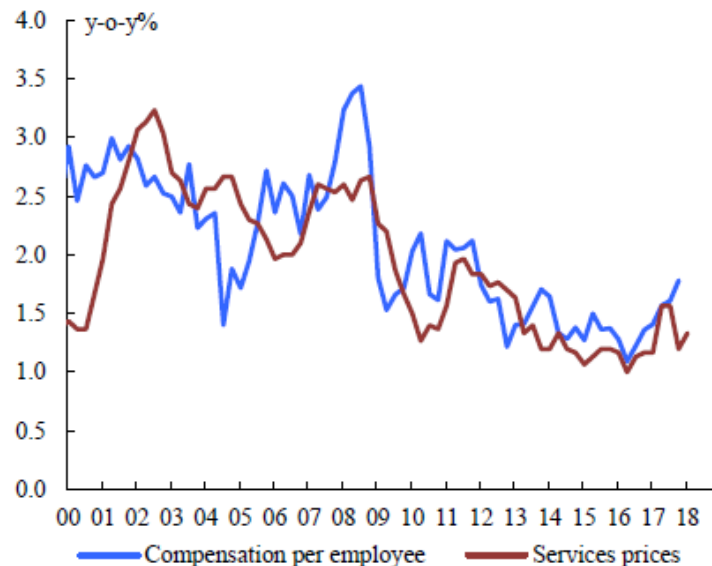


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### 3. Slack and inflation (wages and inflation outlook)

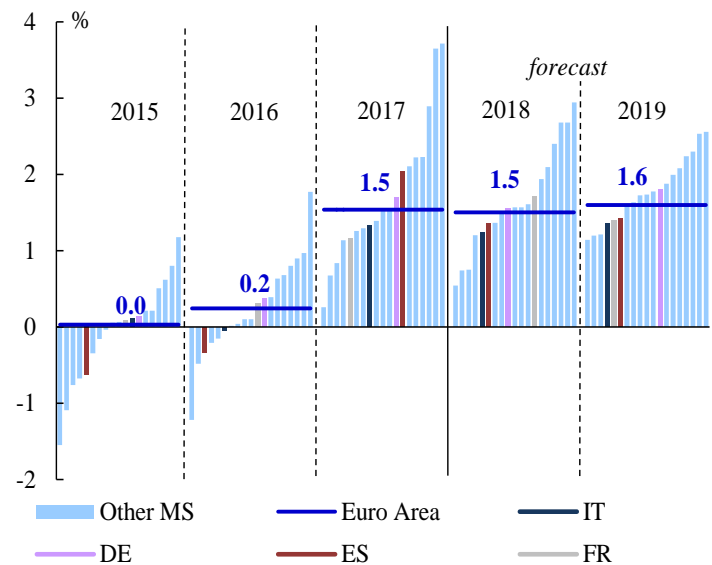
...and **wages rising gradually** as the output gap closes.

Graph: Wage growth and services inflation (EA)



**HICP inflation should rise slightly by 2019**

Graph: Inflation rates (EA and MS)



Note: in each period, the bars for all 19 euro area economies are ranked by size.





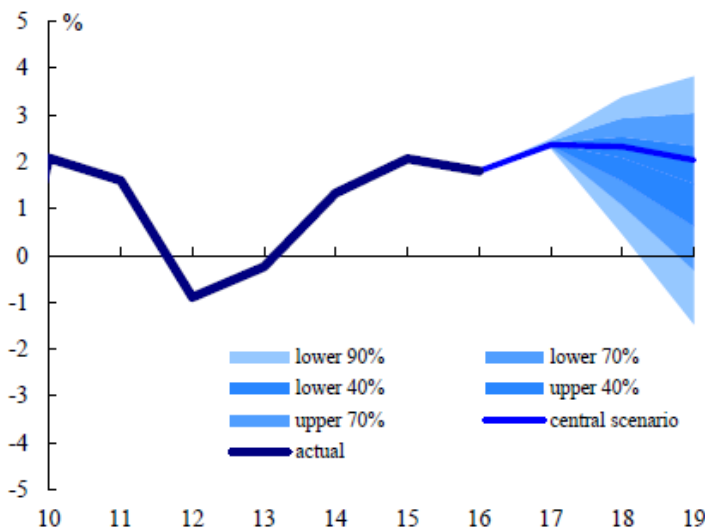
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# 4. Risks

(“Trade disputes could blow expansion off course”)

## Risks to growth higher and tilted to the downside...

Graph: Fan chart, euro area GDP (SF18)



## ...as (interrelated) external downside risks intensified.

### External risks

- (-) Unwarranted effects of the US fiscal stimulus (e.g. faster Fed tightening)
- (-) Global financial market stress / pick-up in yields
- (-) Trade disputes and protectionism
- (-) Geopolitical tensions

### Domestic risks

- (-) Outcome of the Brexit negotiations
- (+) Stronger-than-expected investment expansion

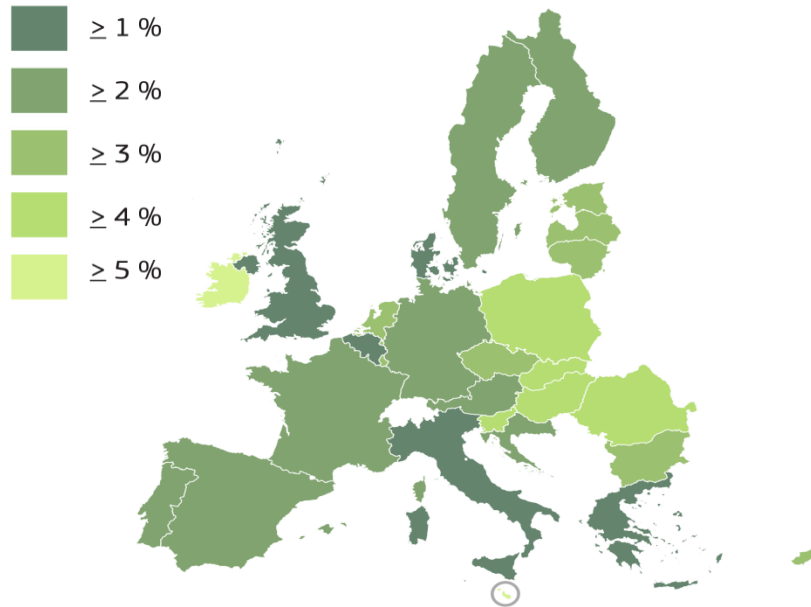


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# Final remarks

"Expansion to continue amid new risks" in **all MS...**

Graph: EU growth map, 2018 (SF18)



...with a **special factor** to be watched in June/July 2018.



FIFA WORLD CUP  
**RUSSIA 2018**

Table:

**Real GDP, 2008-2017**

(Total percentage change)

**Football World Cup 2018**

|                                   | Qualified   | Not qualified |
|-----------------------------------|-------------|---------------|
| Euro area Member States           | 7.6         | 1.2           |
| <b>Other EU Member States (a)</b> | <b>14.5</b> | <b>13.8</b>   |
| EU Member States                  | 9.8         | 3.1           |

(a) UK GDP used for team England.

**Thank you for your attention**