Samu Kurri

Bank of Finland

Growth overshadowed by hard-to-quantify risks

Monetary policy and the global economy
Bank of Finland Bulletin 4/2016

Themes of the presentation

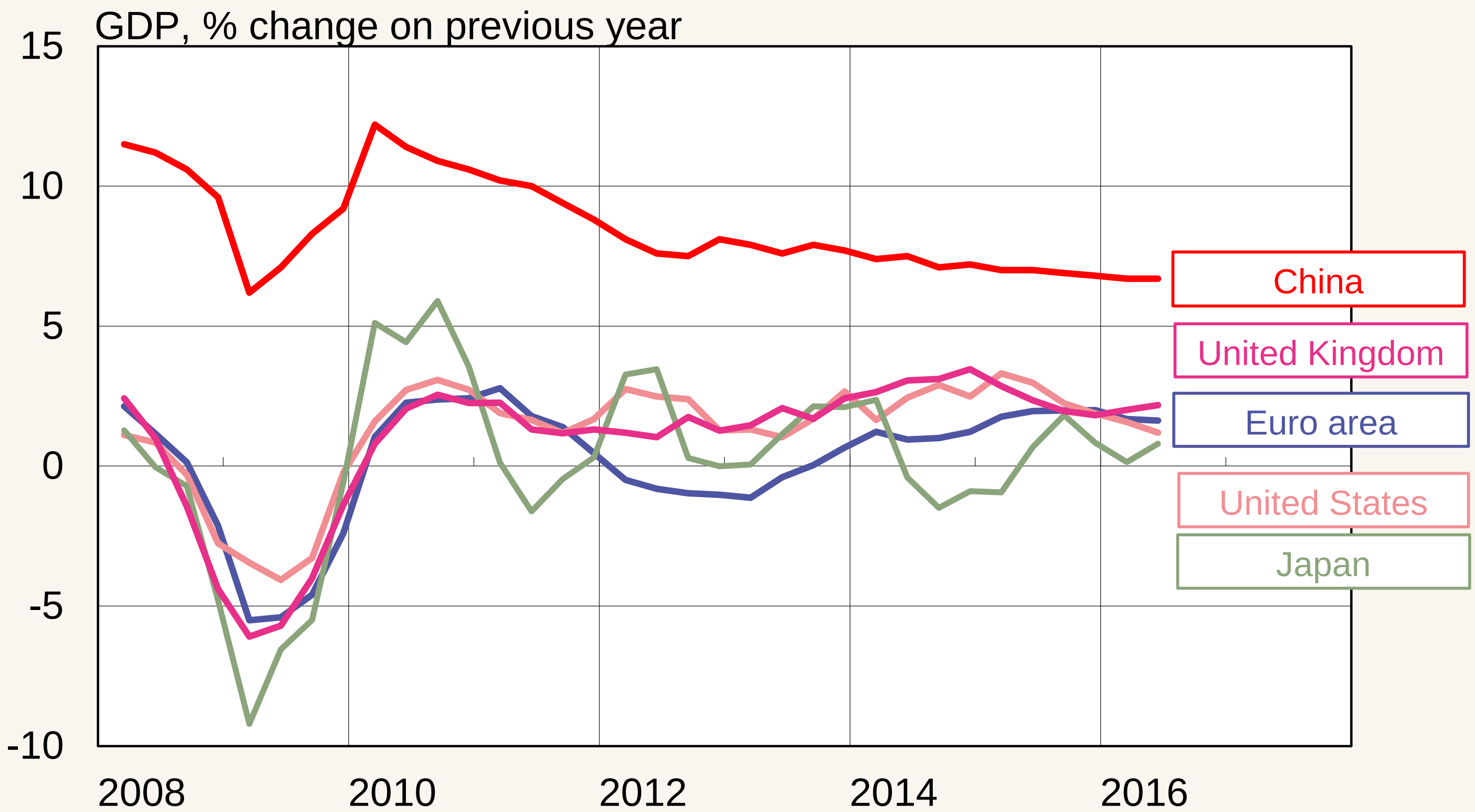
- ***Global growth forecast little changed***
  - *Growth will barely accelerate in the immediate years ahead*
  - *Effects of Brexit hard to assess at this point*

- ***Inflation remains very subdued***
  - *Oil price effect to subside in early 2017*
  - *Difference between markets' and economists' inflation expectations a source of concern*

- ***Risks to growth mainly on the downside***
  - *Some risks relate to economic factors that can be estimated by economics tools*
  - *Some risks are difficult to assess in economic terms*

Current situation and outlook for the real economy

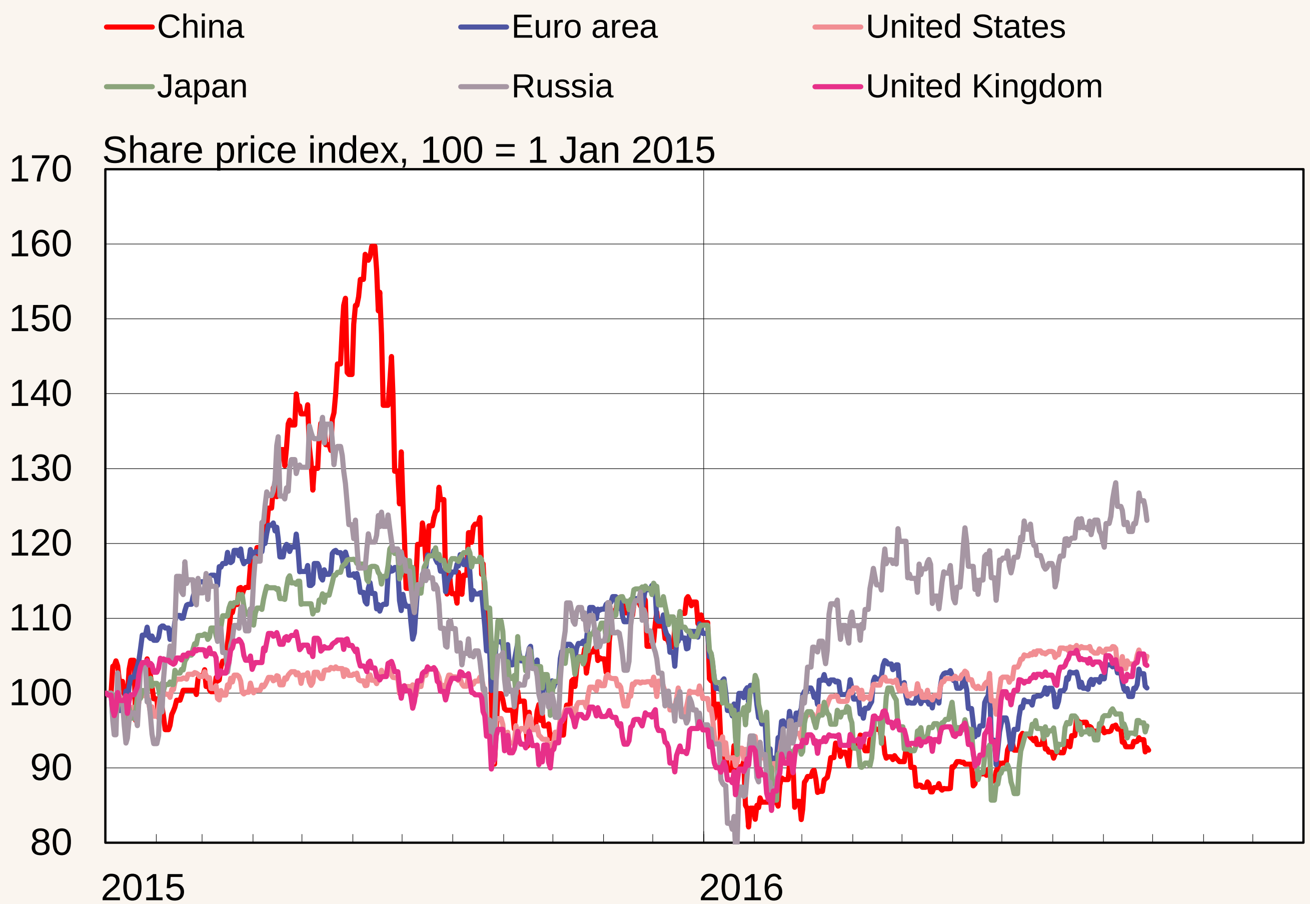
Moderate global growth in early 2016



Sources: National statistical authorities and Macrobond.

32427

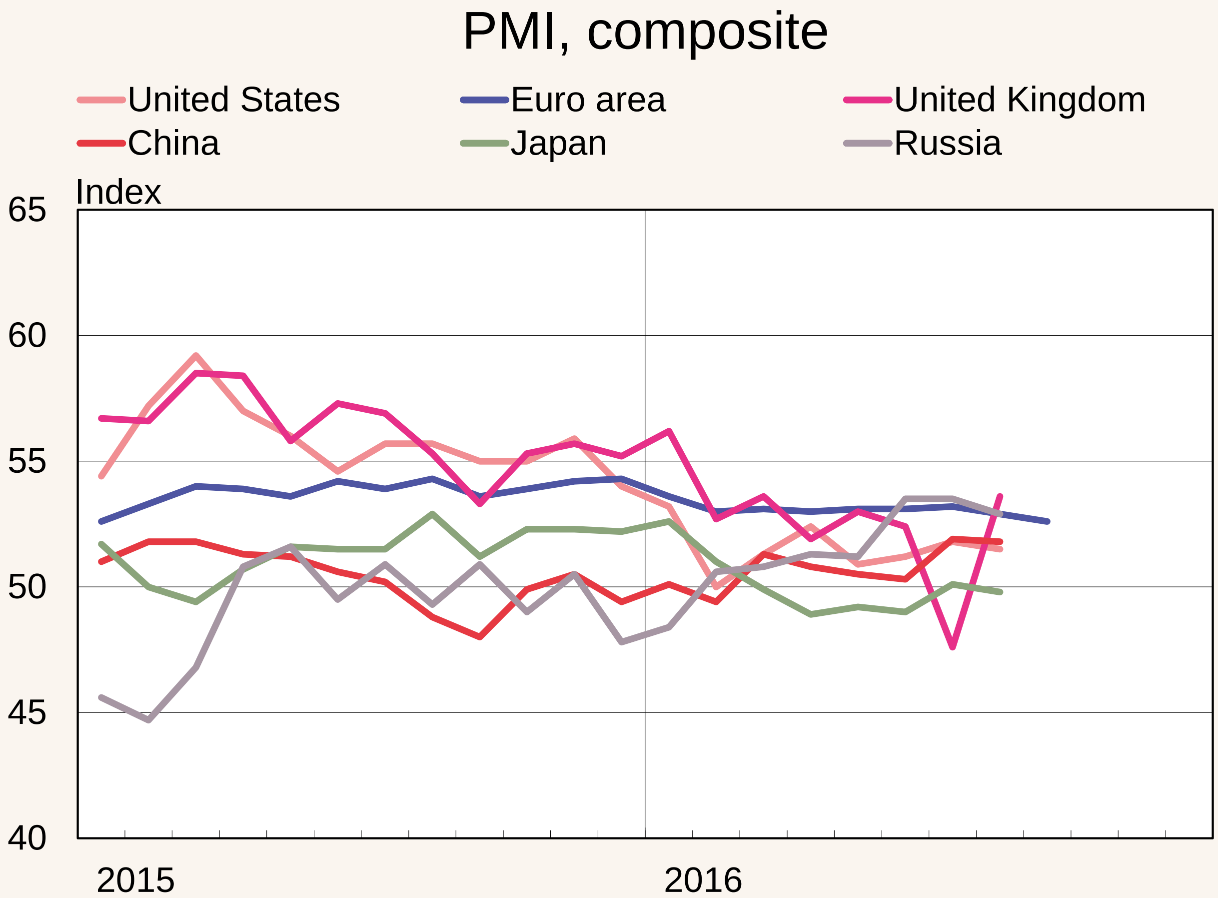
Stock exchanges do not signal any major improvement in growth …



Source: Macrobond.

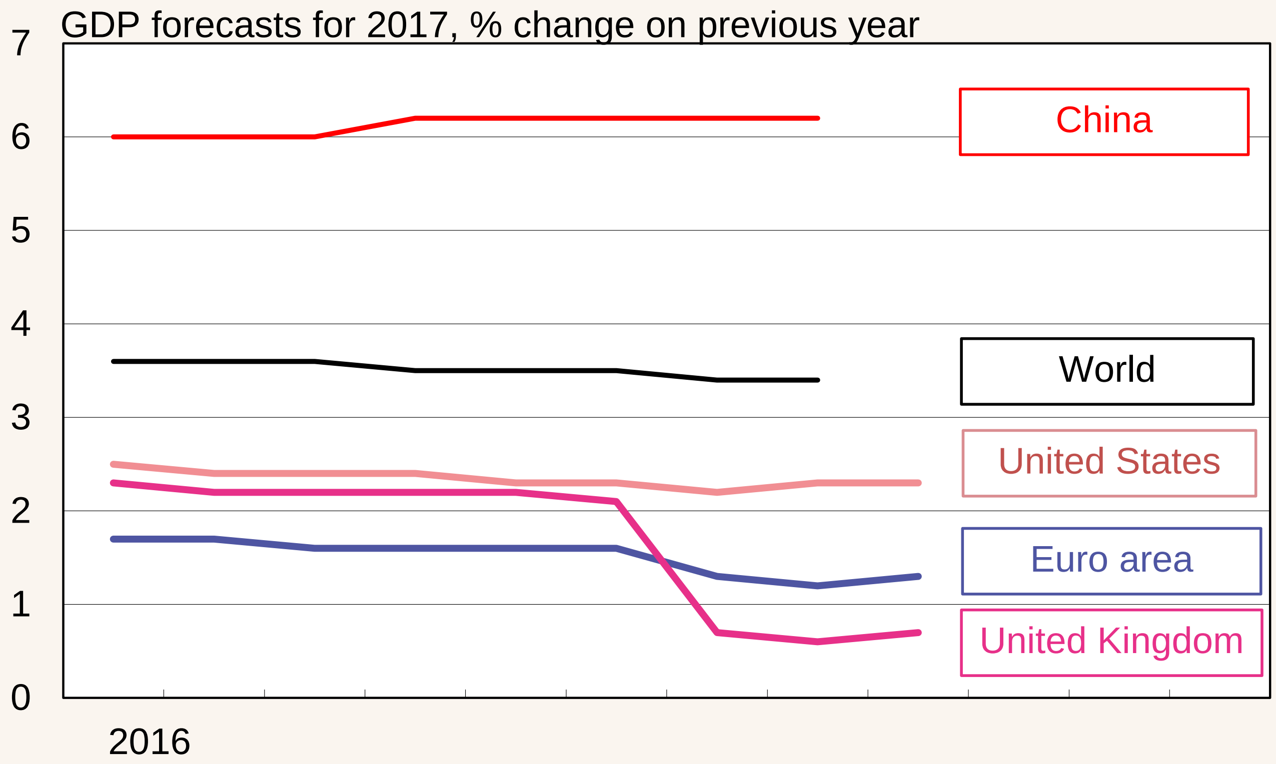
32427

… and neither do the soft statistics



Source: Macrobond.
32427

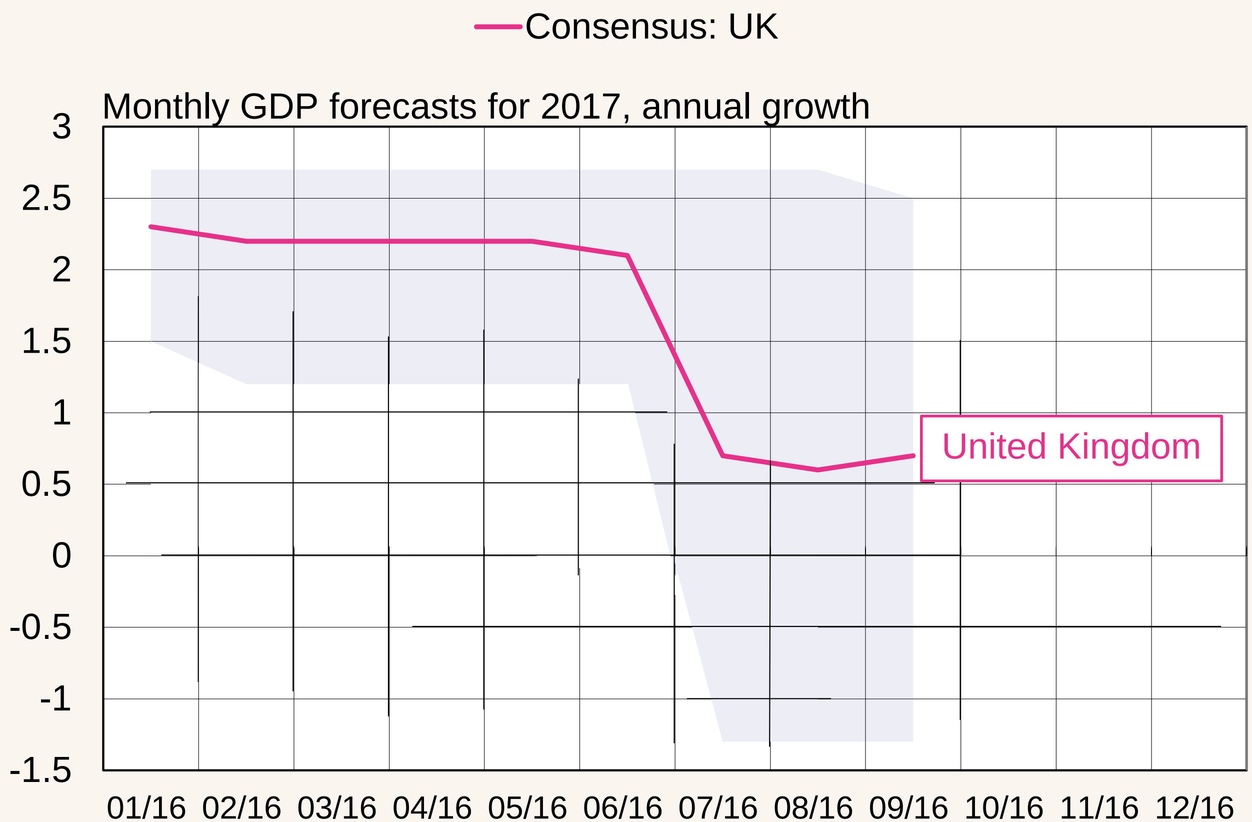
Economists revised down 2017 growth forecasts, notably for the UK



Consensus forecasts collected on the 7th–13th of each month.
Sources: Consensus Economics (US, euro area and UK) and the IMF.

23060

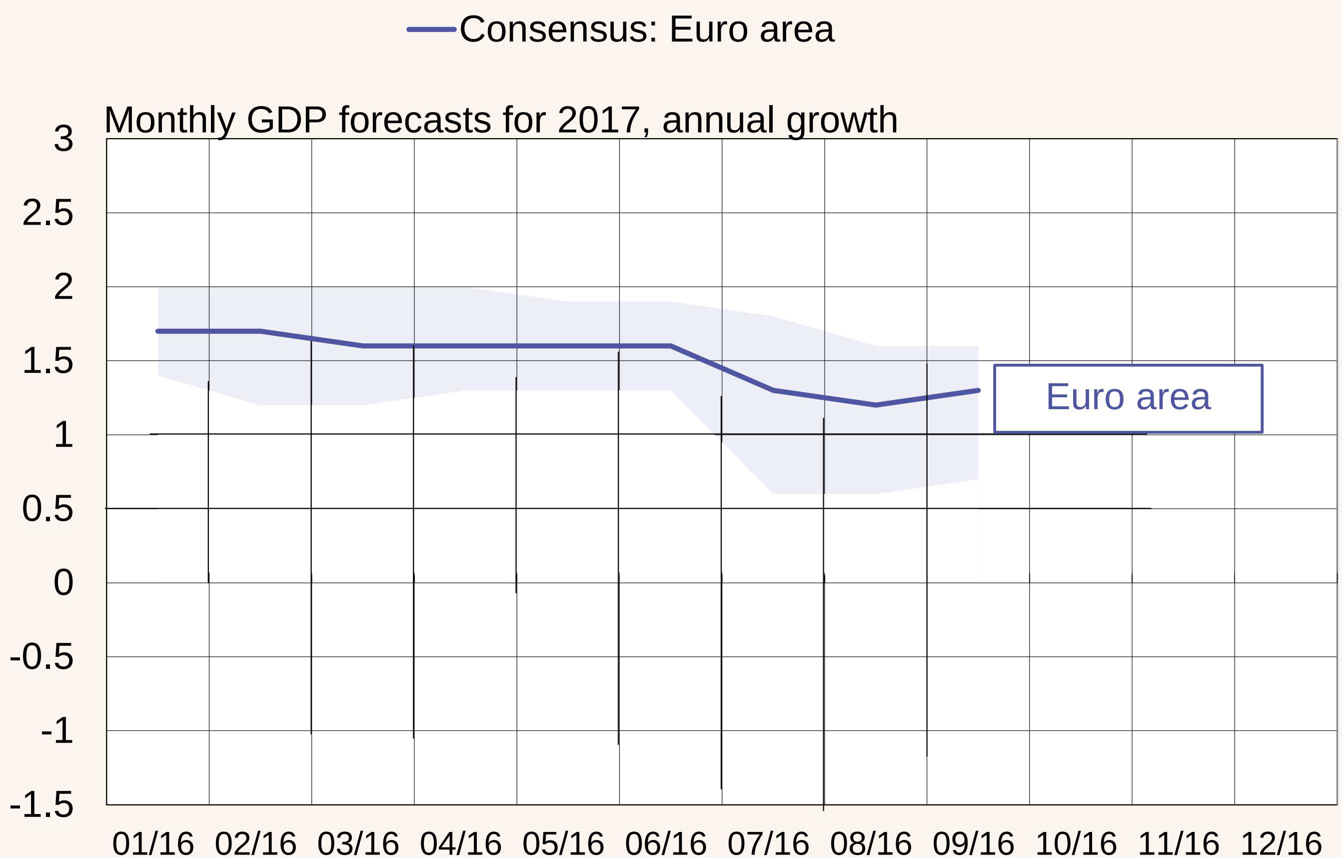
Estimates of the effects of Brexit surrounded by great uncertainty: notably for the UK economy …



Source: Consensus Economics.

23060@Chart10UK

Estimates of the effects of Brexit surrounded by major uncertainty:
… but also for the euro area

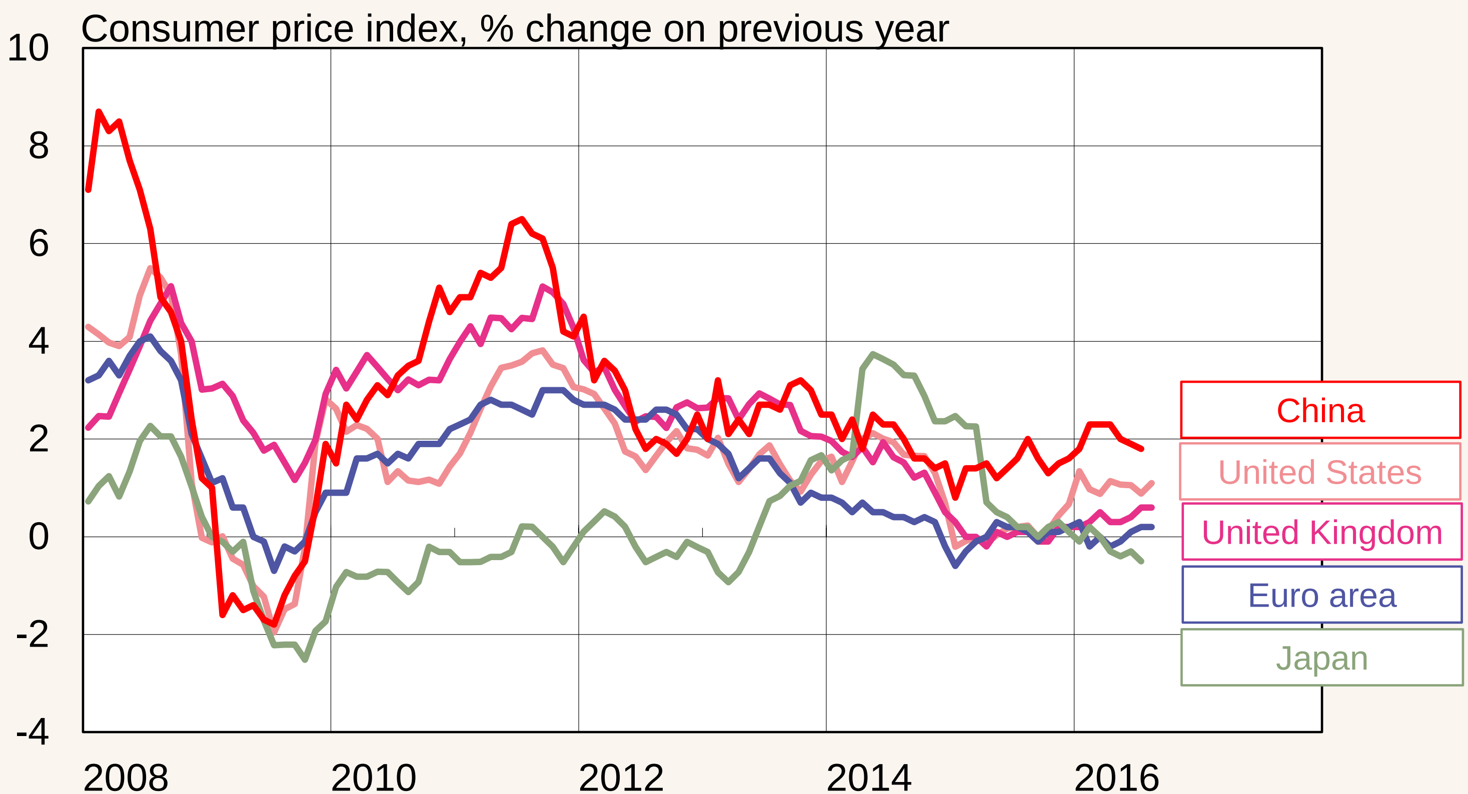


Source: Consensus Economics.

23060@Chart10EA

Inflation picture and underlying factors

Inflation in main economic regions remains subdued



Sources: Eurostat, national statistical authorities, OECD and Macrobond.

32427

Inflation, GDP and monetary policy

- ***Key factors underlying inflation developments***
  - ***Inflation expectations***
  - ***Actual inflation***
  - ***Output gap, or the difference between actual output and output at full capacity***
  - ***Price of crude oil***

- ***Monetary policy works through***
  - ***Anchoring of inflation expectations***
  - ***Real economic developments.***

Oil price an important one-off factor behind drop in inflation

Oil price and futures prices forecast

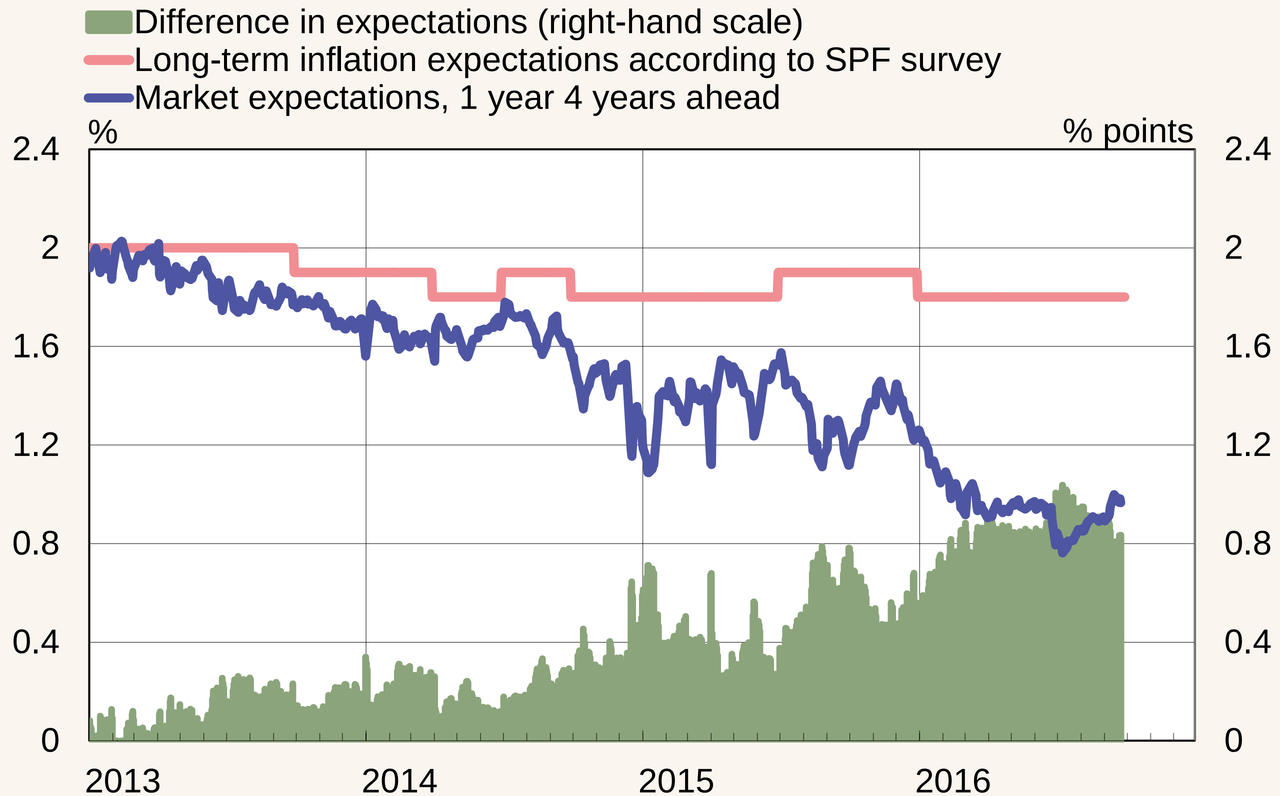
The Bank of Finland forecast assumption is the 10-day average of futures prices on 15 September 2016.

Source: Macrobond.

23060@FutuuritUusin

Sliding oil price not expected to influence longer-term inflation expectations

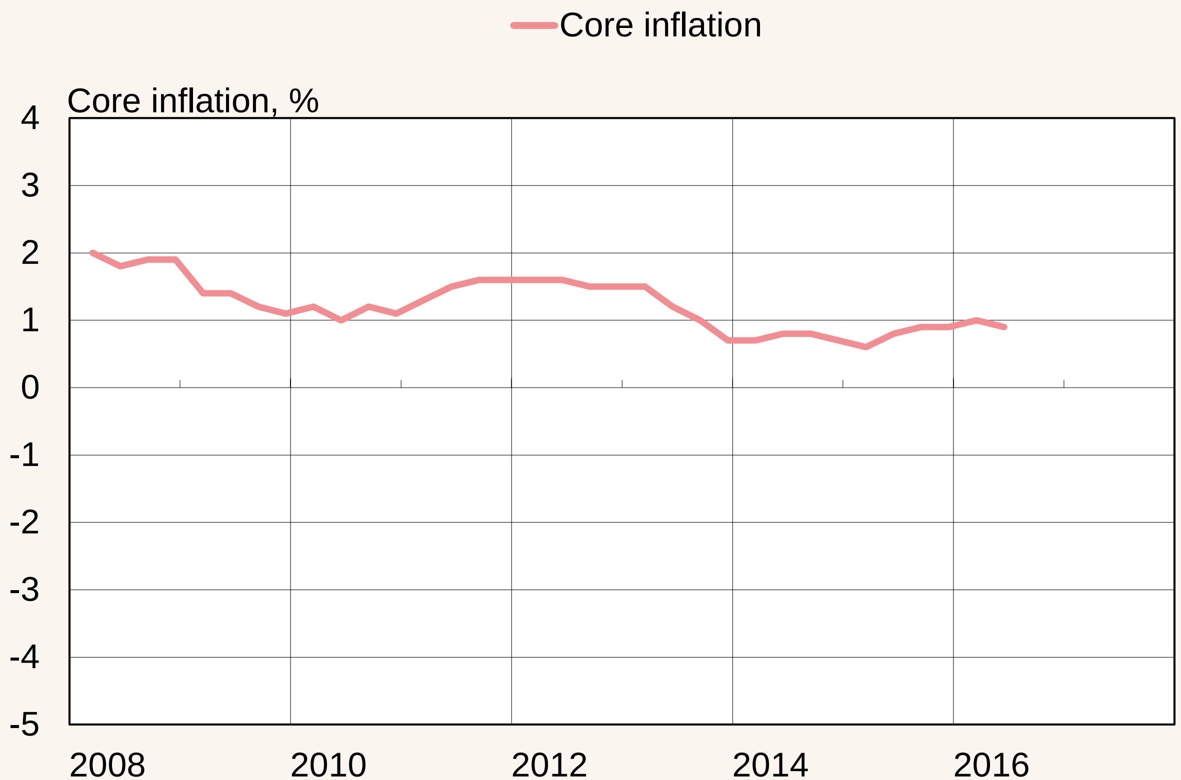
Gulf between inflation expectations of markets and professional forecasters has grown



Sources: ECB, Macrobond and Bank of Finland.

27227@Chart27(3)

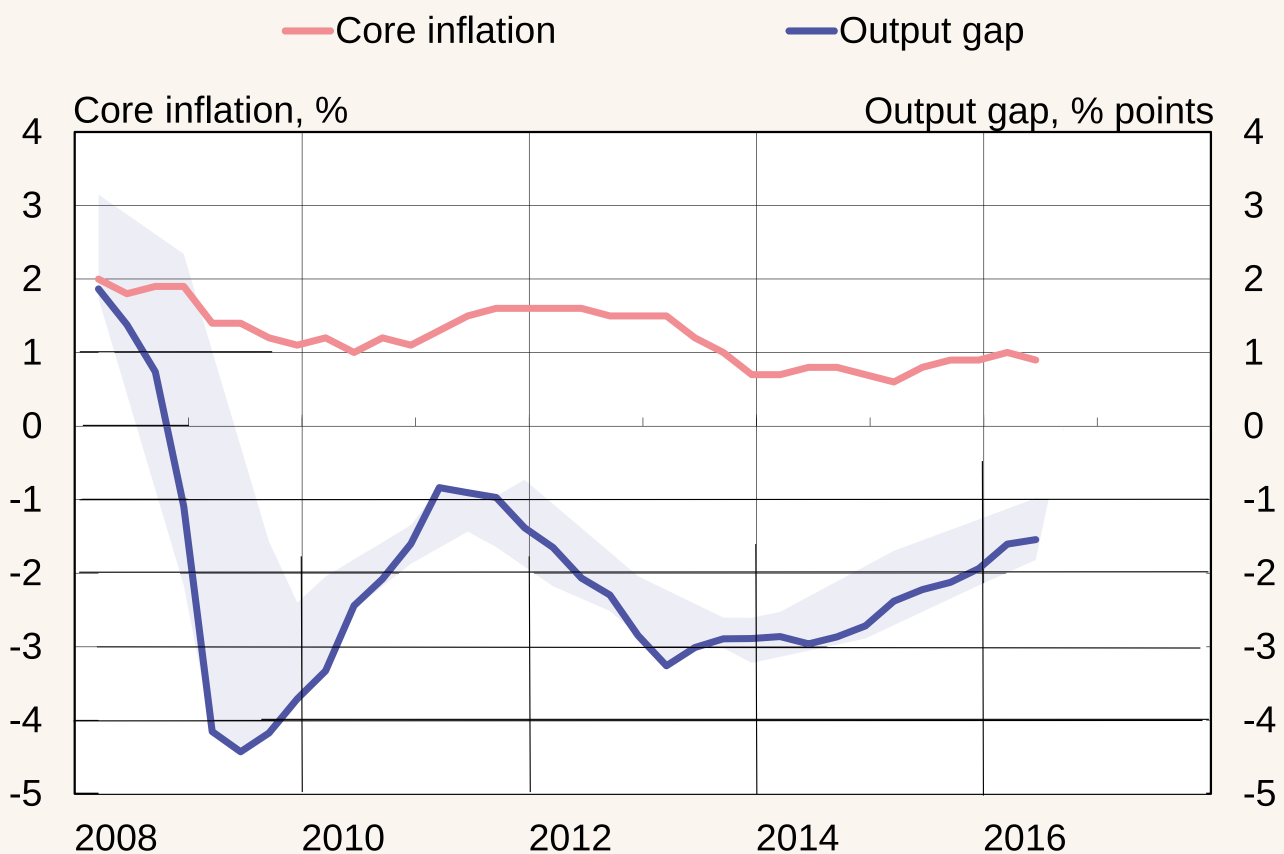
Euro area core inflation subdued …



Sources: Eurostat, European Commission, OECD, IMF and calculations by the Bank of Finland.

23060

… as the output gap remains significant



The shaded area delineates the range between the minimum and maximum output gap assessment.

Sources: Eurostat, European Commission, OECD, IMF and calculations by the Bank of Finland.

23060@EA_CoreCPI_GAP

Bank of Finland forecast for the global economy

Forecast for the global economy little changed

% change on previous year (previous forecast)				
GDP	**2015**	**2016f**	**2017f**	**2018f**
EU22	2.0 (1.7)	1.7 (1.6)	1.3 (1.8)	1.6 (1.8)
United States	2.6 (2.4)	1.6 (2.2)	2.3 (2.3)	2.2 (2.2)
Japan	0.6 (0.5)	0.4 (0.4)	0.9 (0.7)	1.0 (1.2)
China	6.9 (6.9)	6.5 (6)	6 (6)	5 (5)
Russia	-3.7(-3.7)	-1 (-3)	1 (0)	1.5 (1)
World	**2.9** (2.8)	**2.8** (2.8)	**3.1** (3.2)	**3.1** (3.2)
World trade	2.3 (1.4)	1.5 (2.7)	3.2 (3.8)	3.5 (4.0)

f = forecast
E22 = euro area, the UK, Sweden and Denmark.

Oil price change broadly reflected in the inflation outlook

% change on previous year (previous forecast)				
Inflation	**2015**	**2016f**	**2017f**	**2018f**
EU22	0.0 (0)	0.4 (0.2)	1.4 (1.4)	1.5 (1.6)
United States	0.1 (0.1)	1.1 (1.0)	2.1 (2.3)	2.2 (2.2)
Japan	0.8 (0.8)	-0.1(0.2)	0.6 (1.5)	1.0 (1.4)

f = forecast
E22 = euro area, the UK, Sweden and Denmark

Forecast risks

- ***Risks external to the euro area***
  - ***Step-up in US productivity growth*** ***(+)***
  - ***Protectionism, introversion*** ***(-)***
  - ***Financial market disruption in China*** ***(-)***

- ***Risks internal to the euro area***
  - ***Effects of Brexit*** ***(-)***
  - ***Political uncertainty (in Italy), banking system in Italy*** ***(+/-)***

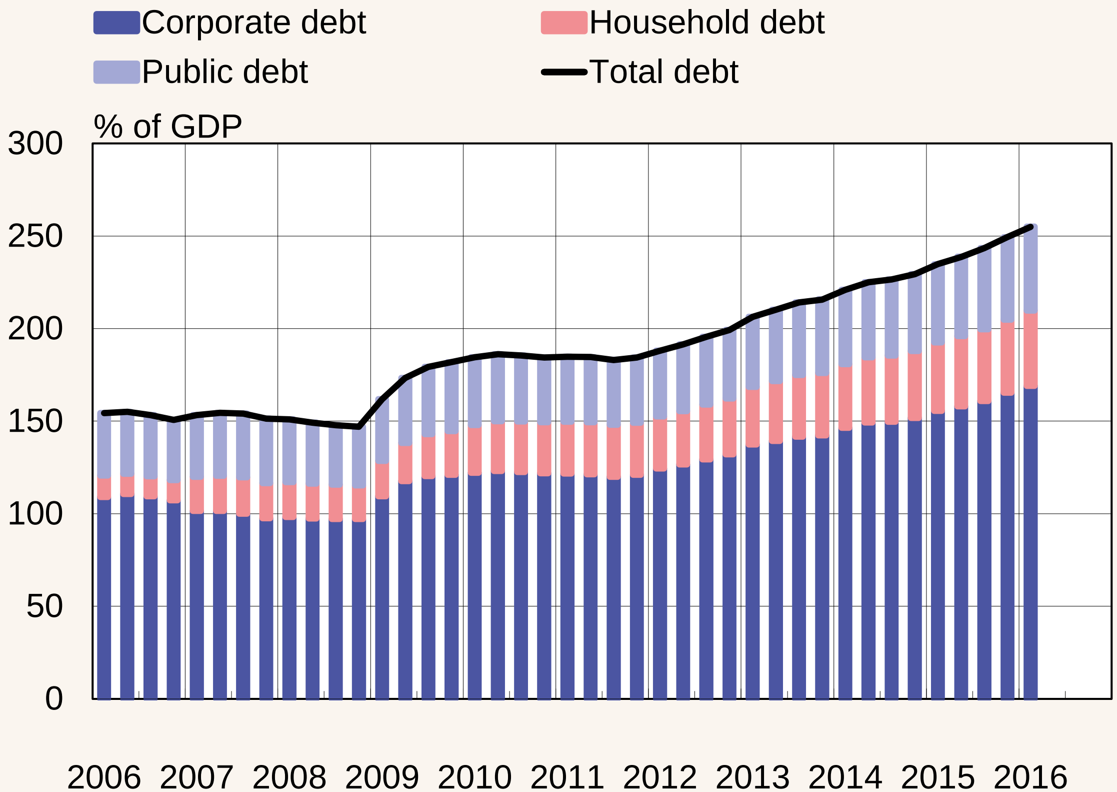
Many unresolved issues remain in assessment of Brexit effects

- *What does Brexit mean?*
  - *Resignation likely to be triggered in early 2017*
  - *No information on negotiation objectives, negotiations likely to go on beyond the end of 2018*

- *Bank of Finland's forecast mainly takes account of the trade effects of Brexit*
  - *UK growth forecasts surrounded by uncertainty*
  - *Assumptions of contagion effects marked by uncertainty*

- *Bank of Finland forecast does not take account of the*
  - *Effects on the mobility of labour, on investment and productivity*
  - *Effects on the EU's future internal dynamics*

Chinese debt surging in all sectors



Source: BIS.

Protectionism and turning inwards

- ***World trade already sluggish for many years***
  - *Partly due to the prolonged recession*
- ***Protectionism back in the headlines***
  - *International trade boosts size of cake*
  - *Cake nevertheless unevenly divided*
- ***Political processes hard to assess***
  - *Brexit, free-trade negotiations, …*
  - *Uncertainty surrounding both probabilities and impacts*

Globalisation and ICT boosted US productivity growth in 1995–2005

Source: BLS.

32428

Thank you!