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Editorial

Confronting the Crisis

The global economy is reeling from the largest energy crisis since the 1970s. The energy shock has pushed up inflation to levels not seen for many decades and is lowering economic growth all around the world. In the new *OECD Economic Outlook*, we are now forecasting that world growth will decline to 2.2% in 2023 and bounce back to a relatively modest 2.7% in 2024. Asia will be the main engine of growth in 2023 and 2024, whereas Europe, North America and South America will see very low growth.

Higher inflation and lower growth are the hefty price that the global economy is paying for Russia's war of aggression against Ukraine. Although prices were already creeping up due to the rapid rebound from the pandemic and related supply chain constraints, inflation soared and became much more pervasive around the world following Russia's invasion.

As a consequence of the unexpected surge in prices, real wages are falling in many countries, slashing purchasing power. This is hurting people everywhere. If inflation is not contained, these problems will only become worse. Thus, fighting inflation has to be our top policy priority right now.

Central banks around the world are increasing interest rates to curb inflation and anchor inflation expectations in their respective economies. This strategy is starting to pay off. For example, in Brazil, the central bank moved swiftly, and inflation has started to come down in recent months. In the United States, the latest data also seem to suggest some progress in the fight against inflation. Nevertheless, monetary policy should continue to tighten in the countries where inflation remains high and broad-based.

In the fight against rising prices, it is also essential that fiscal policy works hand-in-hand with monetary policy. Fiscal choices that add to inflationary pressures will result in even higher policy rates to control inflation. This means that policy support to shield families and firms from the energy shock should be targeted and temporary, protecting vulnerable households and firms without adding to inflationary pressures and increasing public debt burdens. Governments have already done a lot to ease the economic pain from high energy and food prices, including price caps, price and income subsidies and reduced taxes. However, since energy prices are likely to remain high and volatile for some time, untargeted measures to keep prices down will become increasingly unaffordable, and could discourage the needed energy savings.

Energy markets remain among the significant downside risks around this outlook. Europe has gone a long way to replenish its natural gas reserves and curb demand, but this winter in the Northern Hemisphere will certainly be challenging. The situation might be even more complicated in the winter of 2023-2024, as replenishing gas reserves might prove more difficult next year. Higher gas prices, or outright gas supply disruptions, would entail significantly weaker growth and higher inflation in Europe and the world in 2023 and 2024.

Rising interest rates will also pose many challenges and risks. Debt repayment will be more expensive for firms, governments and households who have variable rate debt obligations or when taking on new debt. We are particularly concerned about low-income countries, over half of which are already in (or at high risk of) debt distress and now face tightening financial conditions. Currency depreciation vis-à-vis the US dollar in many of these countries, and in emerging markets, adds to these risks.

Russia's war against Ukraine is also aggravating global food insecurity by putting pressure on prices, supplies, and food affordability. Some of the most vulnerable people around the globe face the highest risk of food insecurity, and many governments lack the means to address this problem. Keeping markets open and agricultural goods flowing, as well as providing well-targeted aid, should be the utmost priority to avoid further food disruptions and hunger in many of these countries.

Policies for a stronger recovery

Policymakers must take bold policy actions to confront these challenging times. In addition to monetary and fiscal policies, it is time for governments to go back to structural policies to tackle some of the most pressing current issues.

First, investing in energy security and diversifying energy supplies is imperative. To prevent energy disruptions, many countries are reverting temporarily to more polluting and carbon-emitting energy sources. However, high energy prices and concerns about energy security are also encouraging governments and firms to diversify energy sources and boost investment in renewables. Strengthening energy grids and investing in energy efficiency and green technologies will need to be high on political agendas to ensure that we reach our net zero emissions goals. The OECD aims to support this effort through its Inclusive Forum on Carbon Mitigation Approaches (IFCMA), a forum of dialogue between countries at different stages of development that will allow us to better understand and analyse diverse policy approaches to carbon mitigation and their effects.

Second, governments need to keep markets open and international trade flowing. This will strengthen competitive pressures and will help alleviate supply constraints. In contrast, pursuing protectionist policies would be a serious setback for many countries, in particular the world's poorest, and would significantly damage the global economy.

Third, fostering employment is essential to boost potential growth and achieve a stronger and more inclusive recovery. For example, governments should work to decrease the gaps in employment rates between men and women in countries where these gaps remain high. Investing in skills is also essential, to counteract the human capital losses that occurred during the pandemic, especially for the most vulnerable, and address the persistent and emerging skill shortages that many countries are facing.

Summing up

We are currently facing a very difficult economic outlook. Our central scenario is not a global recession, but a significant growth slowdown for the world economy in 2023, as well as still high, albeit declining, inflation in many countries. Risks remain significant. In these difficult and uncertain times, policy has once again a crucial role to play: further tightening of monetary policy is essential to fight inflation, and fiscal policy support should become more targeted and temporary. Accelerating investment in the adoption and development of clean energy sources and technologies will be crucial to diversifying energy supplies and ensuring energy security. A renewed focus on structural policies will allow policymakers to foster employment and productivity, as well as to make growth work for all. In other words, it is in our hands to overcome this crisis. And if we choose to undertake the right set of policies, we will certainly increase our chances of success.

22 November 2022

Álvaro Santos Pereira

OECD Chief Economist ad interim

1 General assessment of the macroeconomic situation

Introduction

The global economy is facing mounting challenges. Growth has lost momentum, high inflation is proving persistent, confidence has weakened, and uncertainty is high. Russia's war of aggression against Ukraine has pushed up prices substantially, especially for energy, adding to inflationary pressures at a time when the cost of living was already rising rapidly around the world. Global financial conditions have tightened significantly, amidst the unusually vigorous and widespread steps to raise policy interest rates by central banks in recent months, weighing on interest-sensitive spending and adding to the pressures faced by many emerging-market economies. Labour market conditions generally remain tight, but wage increases have not kept up with price inflation, weakening real incomes despite the actions taken by governments to cushion the impact of higher food and energy prices on households and businesses. Global GDP growth is projected to be 3.1% in 2022, around half the pace seen in 2021 during the rebound from the pandemic, and to slow further to 2.2% in 2023, well below the rate foreseen prior to the war. In 2024, global growth is projected to be 2.7%, helped by initial steps to ease policy interest rates in several countries. Global prospects are also becoming increasingly imbalanced, with the major Asian emerging-market economies accounting for close to three-quarters of global GDP growth in 2023, reflecting their projected steady expansion and sharp slowdowns in the United States and Europe. Headline consumer price inflation in the major advanced economies is projected to moderate from 6.3% this year to around 4¼ per cent in 2023 and 2½ per cent in 2024 as tighter monetary policy takes effect, demand pressures wane, and transport costs and delivery times normalise, although the pace of decline will vary across countries.

The uncertainty about the outlook is high, and the risks have become more skewed to the downside and more acute. The projections reflect the toll taken by high energy prices over the next two years, but outcomes could be weaker still if there are energy supply shortages in global markets that raise prices further, or if enforced rationing is required to lower gas and electricity demand sufficiently during the next two European winters. Higher policy interest rates could also slow growth by more than projected, with policy decisions difficult to calibrate given high debt levels and strong cross-border trade and investment links that raise the spillovers from weaker demand in other countries. Widespread and rapid monetary tightening also heightens financial vulnerabilities. Financial strategies put in place during the long period of hyper-low interest rates may be exposed by rapidly rising rates and exert stress in unexpected ways. Many emerging-market economies could also face significant difficulties, particularly commodity-importing economies. Higher interest rates, the appreciation of the US dollar and a deterioration in the terms of trade increase the challenges of servicing elevated external debt and deficits, particularly if growth slows sharply and global financial conditions tighten further. Significant risks also remain about the projected steady expansion in China, with the continued weakness in property markets, rising non-performing loans and the disruptions from the continued zero-COVID-19 policy potentially weighing heavily on domestic demand

and global growth. On the upside, reduced uncertainty, easier financial market conditions or lower commodity prices would moderate the slowdown in growth.

Elevated uncertainty, slowing growth, strong inflationary pressure and the ongoing impact of the war in Ukraine on energy markets leave policymakers with difficult choices in order to maintain macroeconomic stability and improve the prospects for sustainable and inclusive growth over the medium term.

- Continued monetary policy tightening is needed in most major advanced economies to anchor inflation expectations and lower inflation durably. Domestic policy measures will need to be carefully calibrated and responsive to new data given uncertainty about the growth outlook, the speed at which higher interest rates take effect and the potential spillovers from restrictive policy in other countries. Tighter global financial conditions and persistent inflation pressures are also likely to prompt further monetary policy tightening in many emerging-market economies, and limit the scope for any easing in countries where growth is slowing and interest rates have already been raised substantially.
- Fiscal support is being provided to help cushion the impact of high energy costs on households and companies. In the absence of such support there would almost certainly be sizeable output declines in many countries, with all of the attendant potential costs these could entail. However, better design is often needed to ensure support is only temporary and concentrated on the most vulnerable households and companies, preserves incentives to reduce energy consumption and can be withdrawn as energy price pressures wane. Short-term fiscal actions to cushion living standards should also take account of the need to avoid a further persistent stimulus to demand at a time of high inflation, thereby ensuring consistency with monetary policy and avoiding adverse effects on fiscal sustainability. Credible fiscal frameworks would help to provide clear guidance about the medium-term trajectory of the public finances and mitigate concerns about debt sustainability at a time of rising spending pressures and higher future payments on public debt.
- The war and the pandemic add to the longstanding challenges for growth, resilience and well-being from the acceleration of digitalisation, population ageing and the need to lower carbon emissions. Effective and well-targeted reform efforts are required to enhance productivity and skills, reduce inequality and improve gender balance, strengthen resilience and boost living standards. Well-chosen policies, such as increased support for childcare and reduced tax wedges for lower paid workers, could help to address the current pressures faced by lower-income households and also offer medium-term benefits for employment and inclusion. Keeping international borders open to trade, removing obstacles to stronger cross-border economic migration, and ensuring faster integration of migrants into the labour market would also help to alleviate near-term supply-side pressures on inflation. Governments also need to ensure that the goals of energy security and climate change mitigation are aligned. Efforts to safeguard near-term energy security and affordability through fiscal support, supply diversification and lower energy consumption should be accompanied by stronger policy measures to enhance investment in clean technologies and energy efficiency.
- The fallout from the war remains a threat to global food security, particularly if combined with further extreme weather events resulting from climate change. Better international cooperation is needed to keep agricultural markets open, address emergency food needs and strengthen domestic supply. Stronger international co-operation on debt relief, including through the G20, is also necessary to minimise the potential adverse economic and social consequences of default, with a rising number of lower-income developing countries already experiencing debt distress and having fragile banking sectors.

Table 1.1 Global growth is projected to slow further

	Average 2013-2019	2021	2022	2023	2024	2022 Q4	2023 Q4	2024 Q4
				Per cent				
Real GDP growth[1]								
World[2]	3.4	5.9	3.1	2.2	2.7	2.0	2.3	3.0
G20[2]	3.5	6.2	3.0	2.2	2.7	2.0	2.2	3.0
OECD[2]	2.2	5.6	2.8	0.8	1.4	1.2	0.9	1.8
United States	2.4	5.9	1.8	0.5	1.0	0.2	0.3	1.6
Euro area	1.9	5.3	3.3	0.5	1.4	1.4	0.7	1.7
Japan	0.8	1.6	1.6	1.8	0.9	2.0	1.2	0.7
Non-OECD[2]	4.4	6.2	3.4	3.3	3.8	2.7	3.6	4.0
China	6.8	8.1	3.3	4.6	4.1	4.4	4.5	4.0
India[3]	6.8	8.7	6.6	5.7	6.9			
Brazil	-0.4	4.9	2.8	1.2	1.4			
OECD unemployment rate[4]	6.5	6.2	5.0	5.3	5.5	5.0	5.5	5.5
Inflation[1]								
G20[2,5]	3.0	3.9	8.1	6.0	5.4	8.0	5.5	5.5
OECD[6,7]	1.6	3.8	9.4	6.5	5.1	9.6	5.5	5.1
United States[6]	1.4	4.0	6.2	3.5	2.6	5.5	3.1	2.3
Euro area[8]	0.9	2.6	8.3	6.8	3.4	9.6	4.9	2.9
Japan[9]	0.9	-0.2	2.3	2.0	1.7	3.2	1.4	1.9
OECD fiscal balance[10]	-3.2	-7.3	-3.7	-3.6	-3.1			
World real trade growth[1]	3.4	10.0	5.4	2.9	3.8	2.4	3.2	4.0

1. Per cent; last three columns show the change over a year earlier.
2. Moving nominal GDP weights, using purchasing power parities.
3. Fiscal year.
4. Per cent of labour force.
5. Headline inflation.
6. Personal consumption expenditures deflator.
7. Moving nominal private consumption weights, using purchasing power parities.
8. Harmonised consumer price index.
9. National consumer price index.
10. Per cent of GDP.

Source: OECD Economic Outlook 112 database.

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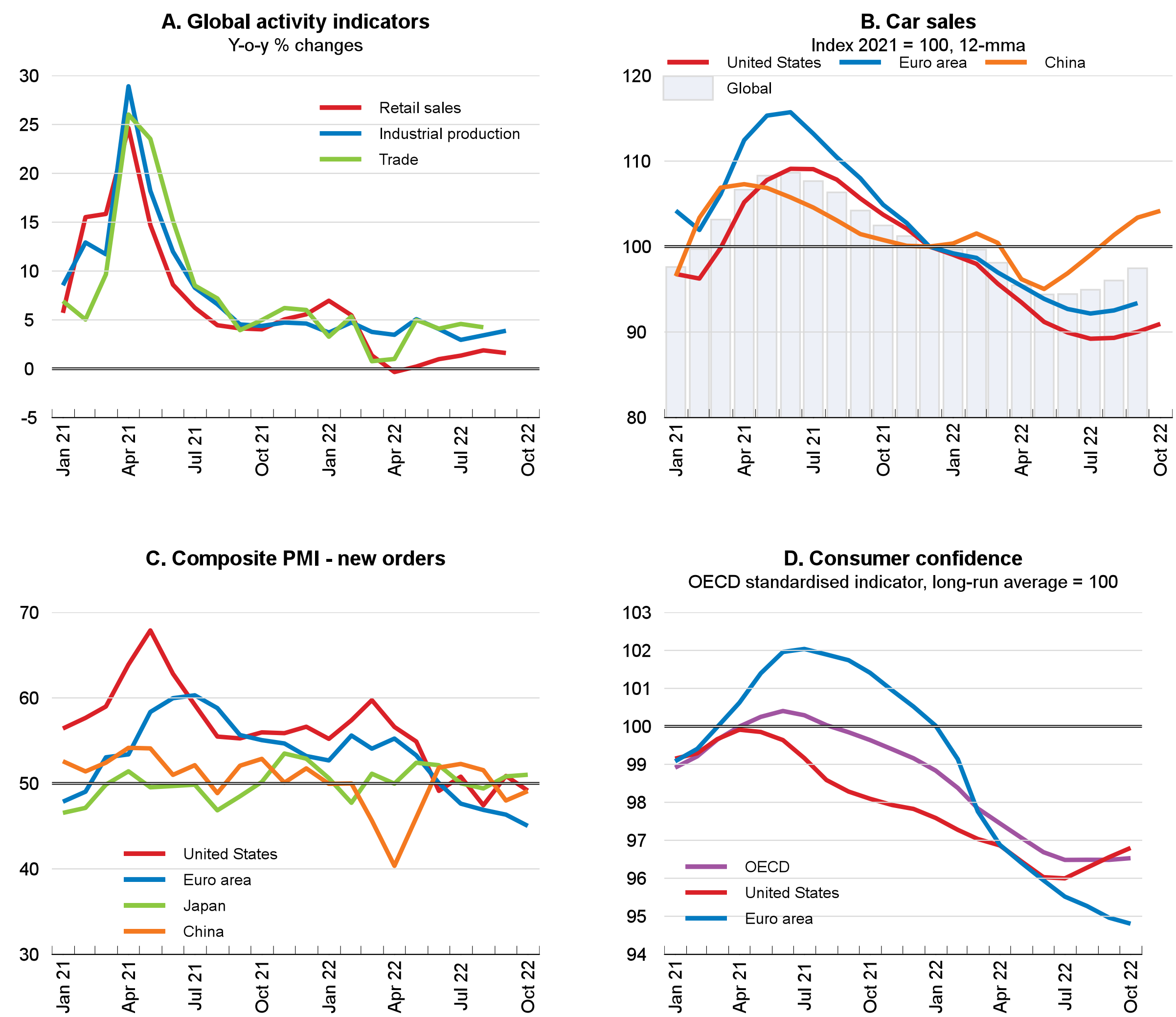
Growth is slowing and financial conditions have tightened

Global growth has lost momentum amidst high inflation

The war in Ukraine is having a persisting adverse effect on economic conditions. Global GDP stagnated in the second quarter of 2022, with sharp falls in output in both Ukraine and Russia, and a contraction of output in both China (reflecting lockdowns due to the zero COVID-19 policy) and the United States. Global growth picked up in the third quarter, helped by a rebound in China and the United States, but remained moderate, with weak real income growth holding back consumers' expenditure and higher energy prices resulting in a sharp slowdown in many economies, particularly in Europe.

In the past few months some indicators of global economic activity, such as retail sales, industrial production and international trade, have stabilised after a particularly weak second quarter (Figure 1.1, Panel A). This has been helped by fewer restrictive anti-COVID-19 measures in China and a consequent rebound in activity, including car sales (Figure 1.1, Panel B). However, survey indicators point to a loss of momentum in many countries, especially in Europe (Figure 1.1, Panels C and D). In the corporate sector, the global all-industry new orders PMI declined steadily for several months through to October, with a broad-based softening across industries. Consumer confidence is notably weak as well, reflecting in part a decline in real household incomes in most OECD economies, with higher inflation not being matched by faster growth in nominal incomes. Low-income households and rural households have been particularly hit, reflecting the large share of food and energy in their expenditures.

Figure 1.1. A variety of high-frequency indicators point to a slowdown



Note: Data in Panel A are PPP-weighted aggregates. The retail sales measure uses monthly household consumption for the United States and the monthly synthetic consumption indicator for Japan.
Source: OECD Main Economic Indicators database; CPB Netherlands Bureau for Economic Policy Analysis; S&P Global; Refinitiv; and OECD calculations.

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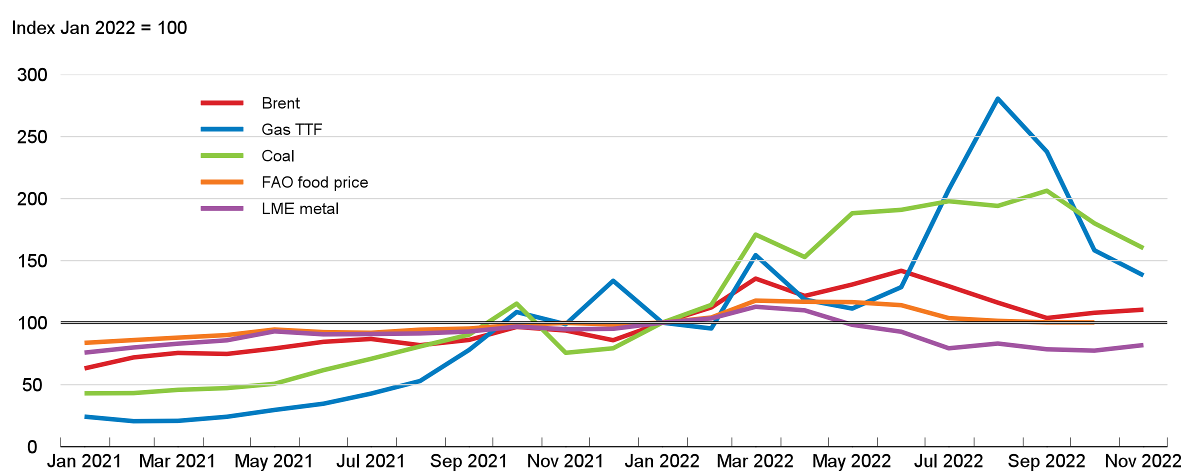
Inflationary pressures have intensified. In the median advanced and emerging-market economy, headline consumer price inflation reached 9.6% and 10.8% respectively in the third quarter of 2022. The unexpected persistence of inflationary pressures this year owes much to the outbreak of the war in Ukraine, which resulted in an immediate spike in a number of key commodity prices – for oil, gas and coal, a range of metals, wheat and corn and some edible oils, as well as fertilisers. While that spike has subsequently been unwound for most commodities, in part due to weak demand from China, the prices of internationally traded gas and coal remain elevated (Figure 1.2).

With spot electricity prices generally being linked to the price of gas, the marginal source of electricity generation, record high gas prices have meant similarly extreme wholesale electricity prices in Europe. Only part of that wholesale price surge has so far been reflected in retail electricity prices (Figure 1.3), with many European governments stepping in to shield consumers from the full impact of the increase in the price of imported gas, adding to the usual factors that limit complete pass-through (Kuik et al., 2022), including the delays in adjusting household and corporate supply contracts. However, some large rises have already occurred, and unless wholesale electricity prices continue to decline (as they have in recent weeks), further retail price rises are likely. If these do not occur, there are risks that distribution companies could become insolvent, and that governments implementing price caps could face costly and potentially long-lasting subsidies.

Even prior to the war in Ukraine, inflation pressures had begun to rise, with both demand- and supply-side factors contributing to price increases in the OECD economies (Box 1.1). Some of these factors have subsided or begun to reverse over the past year. Goods price inflation has eased, with the shift in the composition of demand from services to goods (particularly durable goods) now being reversed (Figure 1.5, Panel A). The normalisation of demand patterns has begun to be reflected in rising inflation rates for services in most countries and, in some, declining inflation rates for goods.[1]

Figure 1.2. Commodity prices have diverged recently



Note: Gas TTF corresponds to the Dutch Transfer Title Facility and coal to the HWWI coal price. November figures are based on the average available data up to November 16.
Source: Refinitiv; and OECD calculations.

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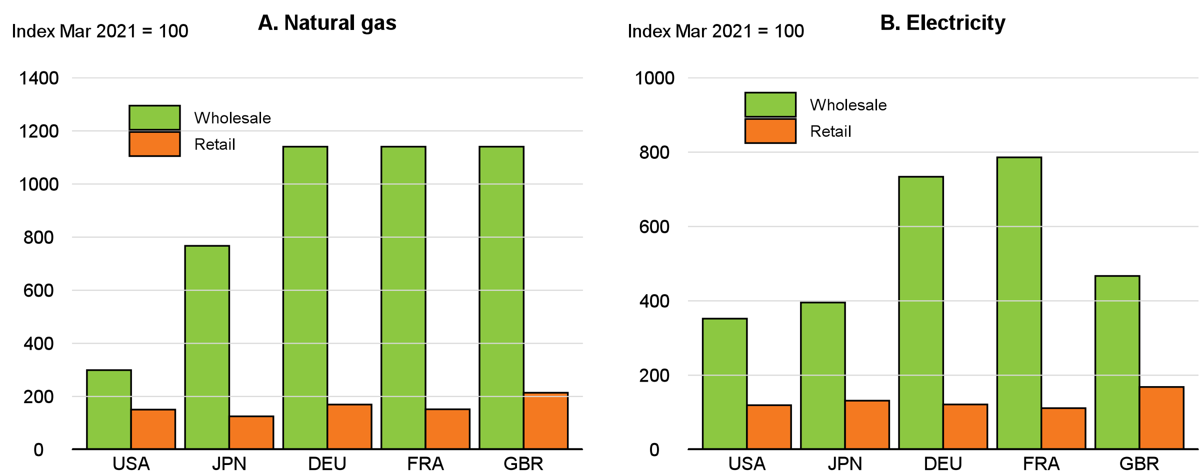
[1] The United States and Canada are two countries where services price inflation is rising and goods price inflation is moderating. For example, in the United States goods price inflation (based on the PCE price index) peaked at 10.6% in March, but has declined to 8.1% in the latest month (September), while services inflation has increased steadily since early 2021, picking up from 2.7% in March 2021 to 5.3% in September 2022.

Figure 1.3. Retail energy prices have increased much less than wholesale prices, especially in Europe



Note: Data for both retail and wholesale prices refer to September 2022. Retail price changes based on the personal consumption expenditures deflator in the United States, harmonised consumer prices in Germany, France and the United Kingdom, and national consumer prices in Japan. Natural gas wholesale prices are proxied by the Henry Hub Natural Gas spot price for the United States, the Liquified Natural Gas price in Asia for Japan and the Dutch Title Transfer Facility (TTF) for Germany, France and the United Kingdom. Wholesale electricity price data come from each domestic electricity market.
Source: Refinitiv; U.S. Bureau of Economic Analysis; Statistics Japan; Eurostat; U.S. Energy Information Administration; Japanese Power; and OECD calculations.

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Another factor that was pushing up inflation until early 2022 but has been ebbing markedly over the past few months is shipping costs. With goods demand in advanced economies easing, and with supply chains being largely restored since the first phase of the pandemic, freight costs have declined sharply of late (Figure 1.5, Panel B). For the G20 countries as a whole, the impact of shipping costs on inflation is estimated to have peaked in the third quarter of 2021, and declined to just 0.18 percentage points by the third quarter of 2022, and zero as of mid-November 2022.[2]

However, inflationary pressures have become more broad-based (Figure 1.6), with higher costs increasingly being passed through into the prices of goods and services, and profit margins rising in some sectors (Brainard, 2022). With many economic agents tending to form their expectations at least partly based on recent experience, it is not surprising in this context that near-term household survey measures of inflation expectations have risen (Figure 1.7), even though market-based indicators of longer-term inflation expectations generally remain well-anchored near central bank objectives.

[2] Based on the framework set out in Guilloux-Nefussi and Rusticelli (2021).

Box 1.1. Supply- and demand-driven inflation in OECD economies

The increase in inflation rates over the past two years in economies around the world has created major challenges for policymakers. One key uncertainty has been whether the surge in inflation has primarily reflected demand factors or negative supply shocks. That question cannot be answered precisely or with certainty, but it is possible to distinguish between demand and supply factors in an approximate way.

One such approach is that of the Federal Reserve Bank of San Francisco, which uses US monthly price and volume personal consumption expenditures (PCE) data to distinguish between items where price and volume shocks move in the same direction and those where they go in opposite directions (Shapiro, 2022a and 2022b). Shocks to prices and volumes in a given month are identified by running vector autoregressions (VARs) for the 10-year period ending in that month for prices and volumes of each item and inspecting the residuals of the respective regressions.[1] The presumption is that price and volume residuals with the same sign reflect demand – greater demand pushes up both prices and volumes and vice versa for lower demand – while residuals with opposite signs correspond to supply shocks – lower supply means a reduction in volume but an increase in price. In addition to items where price changes are identified as clearly demand-driven or supply-driven, an intermediate range, labelled "ambiguous", where price and/or volume residuals are too small to be considered significant, is also identified – a threshold is set that results in approximately 20% of movements on average being classified as ambiguous. The contributions of the three groups sum to total headline PCE inflation, and show the relative importance of supply and demand factors.

Other OECD countries do not have matching disaggregated monthly price and volume data for personal consumption, but quarterly national accounts data for household consumption expenditure by consumption purpose (COICOP) can be used to conduct a similar exercise.[2] Figure 1.4 shows the results of this exercise for eight OECD economies, including the United States. The degree of expenditure disaggregation is generally a good deal lower than in the US case, where the PCE data has 136 categories: the number of categories available in the quarterly national accounts data varies from 11 for Denmark to 110 for the United Kingdom.

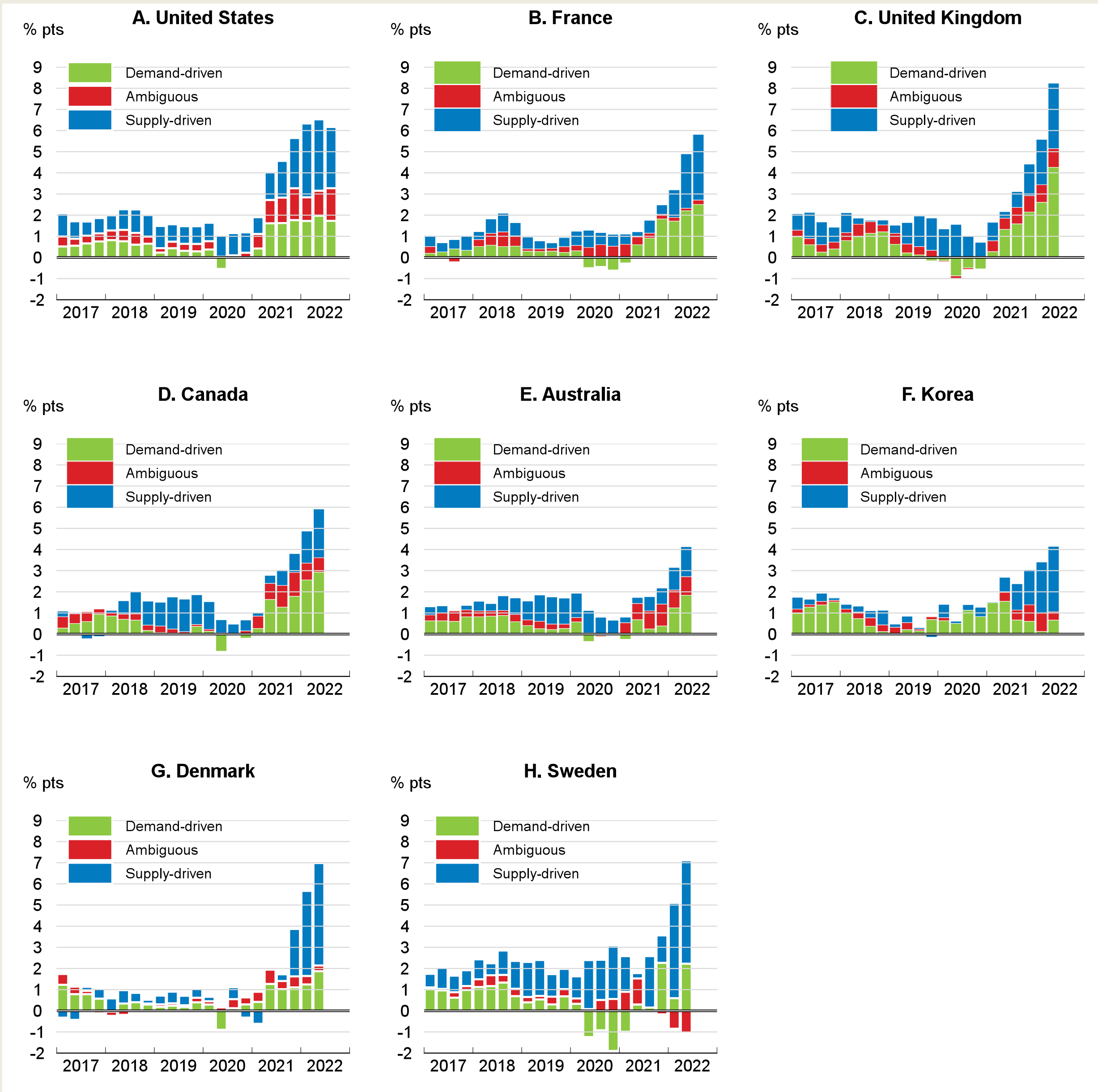
In all countries, the exercise suggests that both supply and demand factors have pushed inflation up since mid-2020. The proportion of inflation accounted for by demand-driven items in the second quarter of 2022 ranges from less than one-quarter in Korea to around half in the United Kingdom and Canada. Supply-driven inflation is estimated to account for roughly half of total inflation on average in the eight countries shown, but well over half in Denmark, Korea and Sweden. The "ambiguous" share is relatively small in all countries in the year to the second quarter of 2022, with the exception of the United States, where it accounts for about one-quarter of total inflation. In general, both supply- and demand-driven contributions have increased in recent quarters, with Korea being an exception: there the demand-driven component peaked in the second quarter of 2021 and has subsequently declined. The United States, for which data are now available through the third quarter of 2022, has had a broadly stable demand-driven contribution for several quarters.

Compared to the immediate pre-pandemic period, when headline inflation was close to, though somewhat below, central bank objectives in all these economies, the estimated contribution of both supply-driven and demand-driven inflation has generally increased. The increase in the contribution of supply-driven inflation has been relatively small in Canada and the United Kingdom. For demand-driven inflation, the increase in the contribution relative to 2019 was largest in the United Kingdom (around 4 percentage points), and also relatively large in Canada and France. The share of inflation classified as ambiguous rose somewhat in Australia, Canada, the United Kingdom and the United States, but not in other countries.

There are several caveats to bear in mind when considering the results of this exercise. First, the method used identifies the price change for each item in a given period as being primarily demand- or supply-driven, but in most cases a mix of supply and demand factors will be operating, even when the exercise allocates the item to the demand-driven or supply-driven category. Also, the pandemic period is clearly atypical, with special factors at play which may make the results less reliable. Finally, the difference in the degree of disaggregation in the available data may limit the extent to which valid conclusions can be drawn from cross-country differences.

Figure 1.4. Contributions of supply- and demand-driven inflation to headline inflation in selected OECD economies

Decomposition of contributions to year-on-year headline inflation



Source: U.S. Bureau of Economic Analysis; Statistics Canada; UK Office of National Statistics; INSEE; Australian Bureau of Statistics; Bank of Korea; Statistics Denmark; Statistics Sweden; and OECD calculations.

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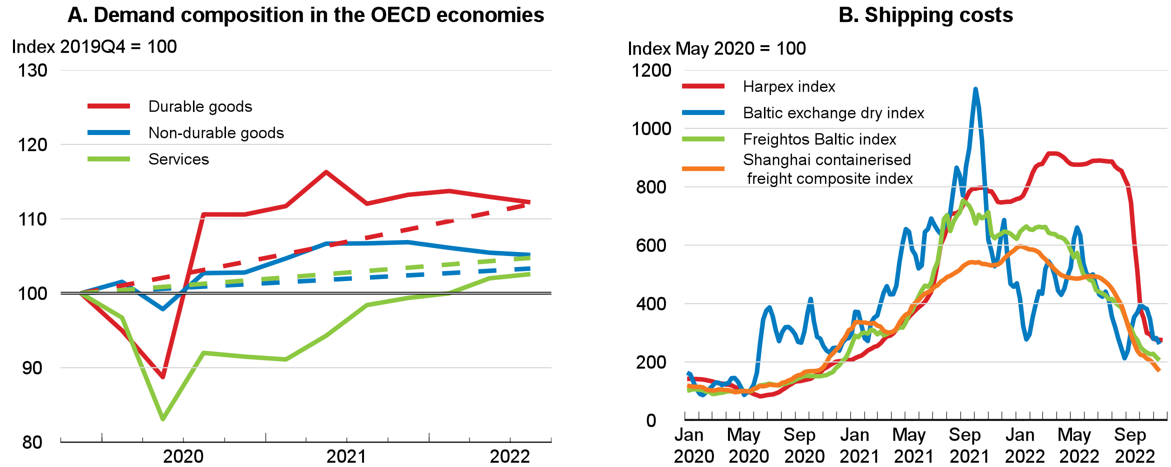
1. A two-equation VAR of prices and quantities: $p_{i,t} = Z_{i,t-1}\gamma + \varepsilon^{p}_{i,t}$ and $q_{i,t} = Z_{i,t-1}\gamma + \varepsilon^{q}_{i,t}$ was estimated where $p_{i,t}$ and $q_{i,t}$ are the logs of the price and quantity indices respectively of category i in quarter t, $Z_{i,t-1}$ is a vector of 4 lags of the log price and quantity indices of category i in quarter t and $\varepsilon^{p}_{i,t}$and $\varepsilon^{q}_{i,t}$ are the price and quantity residuals for category i in quarter t. The equations were estimated over a 10-year rolling window for the period 2005Q4-2022Q2 or 2022Q3. The supply-driven, demand-driven and ambiguous contributions to year-on-year inflation are computed as a weighted sum of the latest four quarterly contributions.
2. In its latest Economic Bulletin (ECB, 2022a), the European Central Bank has replicated the Shapiro exercise using monthly core CPI (excluding energy and food) data and turnover data for services and retail trade from Eurostat's short-term business statistics. The categories are not quite matched, and the turnover data have to be deflated to get volume estimates, but in other respects the exercise follows the US model closely. The ECB finds that the initial surge in core inflation in the euro area was initially mainly supply-driven but that supply and demand factors have played broadly similar roles in recent months.

Figure 1.5. Some factors pushing up inflation prior to the war are now subsiding



Note: In Panel A, the dashed lines correspond to a continuation of the pre-pandemic trend (2010-19). The OECD index is based on a weighted sum of individual country growth rates using GDP weights in PPP terms. Consumption of durable goods, non-durable goods, and services is available for 35, 27 and 27 OECD countries, respectively, except for 2022Q3, where estimates are based on the subset of countries with available data.
Source: OECD Economic Outlook 112 database; Bureau of Economic Analysis; OECD, Quarterly National Accounts; Refinitiv; and OECD calculations.

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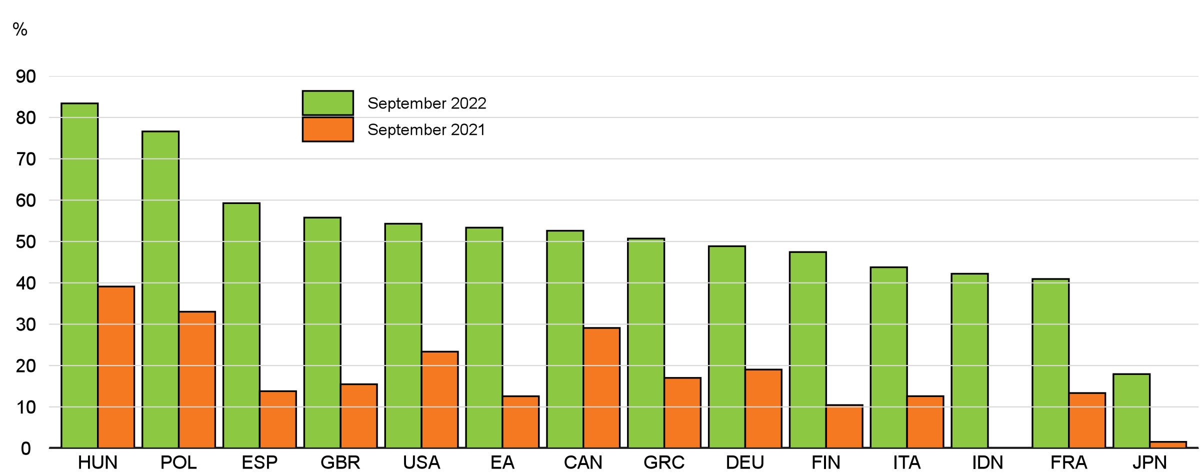
Figure 1.6. Inflation has become increasingly broad-based

Percentage share of products in the inflation basket that have a year-on-year inflation rate above 6%



Note: Inflation based on the personal consumption expenditures deflator in the United States, harmonised consumer prices in the euro area, its member countries and the United Kingdom, and national consumer prices elsewhere. The computation uses about 40 sub-indices for Indonesia, 70 for Japan, 150 for Canada, France, Germany, Greece, Italy and Spain, and more than 200 for the remaining countries.
Source: Bureau of Economic Analysis; Eurostat; Statistics Japan; Office for National Statistics; Statistics Indonesia; and OECD calculations.

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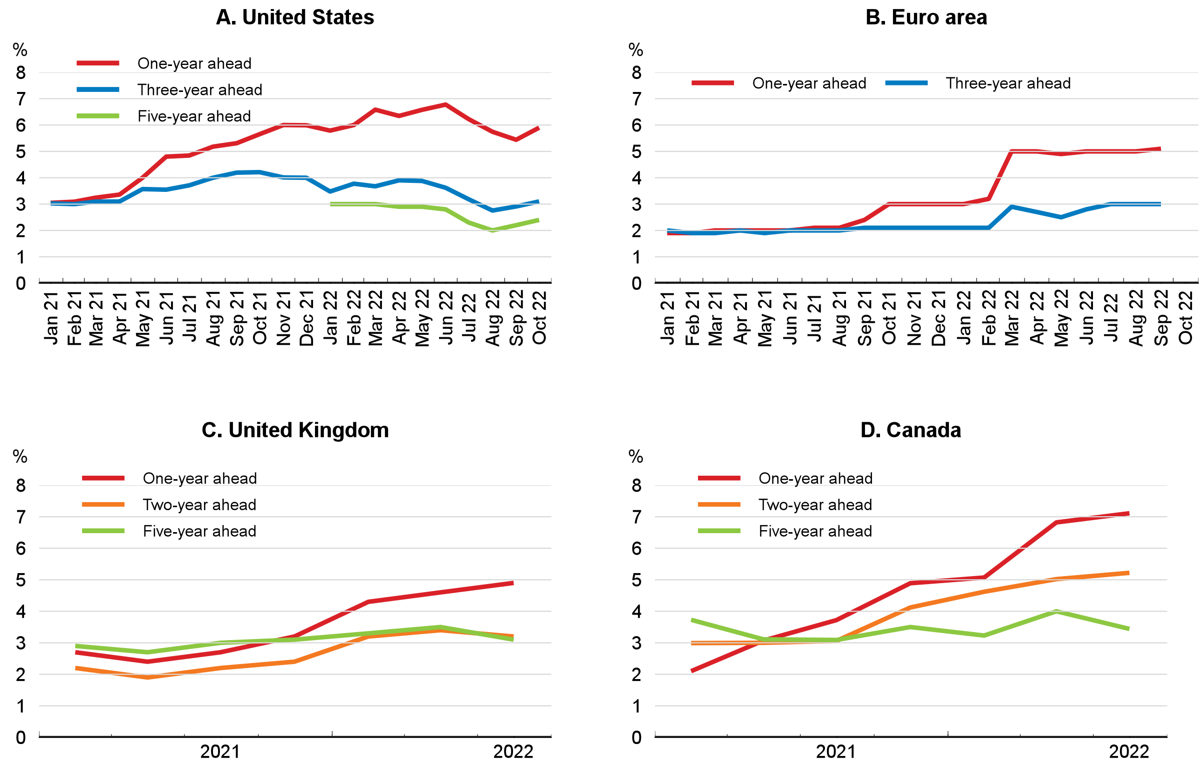
Figure 1.7. Short-term inflation expectations have risen in many economies

Median household inflation expectations



Source: Federal Reserve Bank of New York; European Central Bank; Bank of England; Bank of Canada; and OECD calculations.

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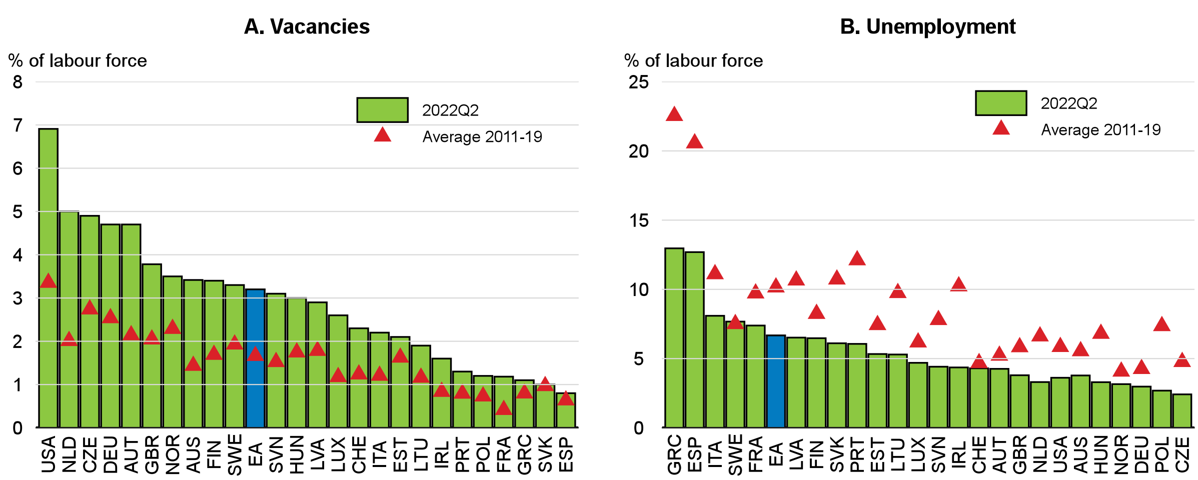
Another key measure of the extent to which above-target inflation is becoming entrenched is the pace of unit labour cost growth. Year-on-year unit labour cost growth is estimated to have been around 4% in the median advanced economy and the aggregate euro area in the third quarter of 2022, over 6% in the United States, and above 10% in some Central and Eastern European economies. In contrast, annual unit labour cost growth remained below 1% in Japan, Spain, and several smaller European economies. Nonetheless, labour cost growth is now rising in most economies, reflecting stronger nominal wage increases and weaker labour productivity growth, with firms retaining workers as output growth slows. Output per employee is estimated to have stagnated in the OECD economies over the year to the third quarter of 2022, and declined in some countries, including the United States. In those countries, unit labour costs have risen more quickly over the past year than wages, putting upward pressure on prices and/or squeezing firms' profit margins.

Labour markets generally remain tight. In many OECD economies, unemployment rates are at their lowest levels in the past two decades and vacancy rates are unusually high (Figure 1.8). The pace of employment growth has, however, slowed recently in some countries, with vacancy rates beginning to ease, and unemployment rates edging up. Nominal wage growth (compensation per employee) has picked up in most economies, but has not kept pace with inflation, resulting in a sharp erosion of wages in real terms in many OECD economies (Figure 1.9). With inflation expected to remain well above target over at least the next year, it is probable that many wage demands in 2023-24 will be considerably higher than previously anticipated.

There are some important differences in labour force developments across OECD member countries since the onset of the pandemic. In most countries, participation rates have continued to rise, with inactivity rates substantially below pre-pandemic levels. Exceptions include the United States, the United Kingdom as well as Colombia, Chile and Latvia, with labour force participation remaining below its pre-pandemic level (Figure 1.10). This may help to explain why some measures of labour market tightness, such as vacancies (Figure 1.8) are more acute in countries such as the United States and the United Kingdom than in countries where inactivity declined substantially relative to the pre-pandemic period, such as Greece and Poland. The reasons for such differences in the evolution of labour force participation are complex, but probably include differential impacts of the pandemic on the health of the working-age population. Countries with high rates of COVID-19 illness and mortality in 2020 and 2021 generally have had less of an increase, or some decline, in labour force participation rates relative to the immediate pre-pandemic level.[3] In addition, the labour market recovery in some emerging-market economies has largely been driven by higher numbers of informal jobs, which will not be reflected in the labour force statistics.

Labour market tightness in some OECD economies has also been accentuated by the relatively low levels of immigration during 2020-21. After a slump during the first year of the pandemic, migration to OECD economies recovered quite strongly in 2021: permanent-type migration into a selection of 24 OECD member countries increased by 25% to 4.2 million (OECD, 2022a). Even so, such migration remained lower than pre-pandemic levels in almost all countries (Canada and Spain being exceptions).[4]

Figure 1.8. Labour markets are tight



Source: OECD Economic Outlook 112 database; Eurostat; OECD, Labour Force Statistics; France Labour Ministry (DARES); and OECD calculations.

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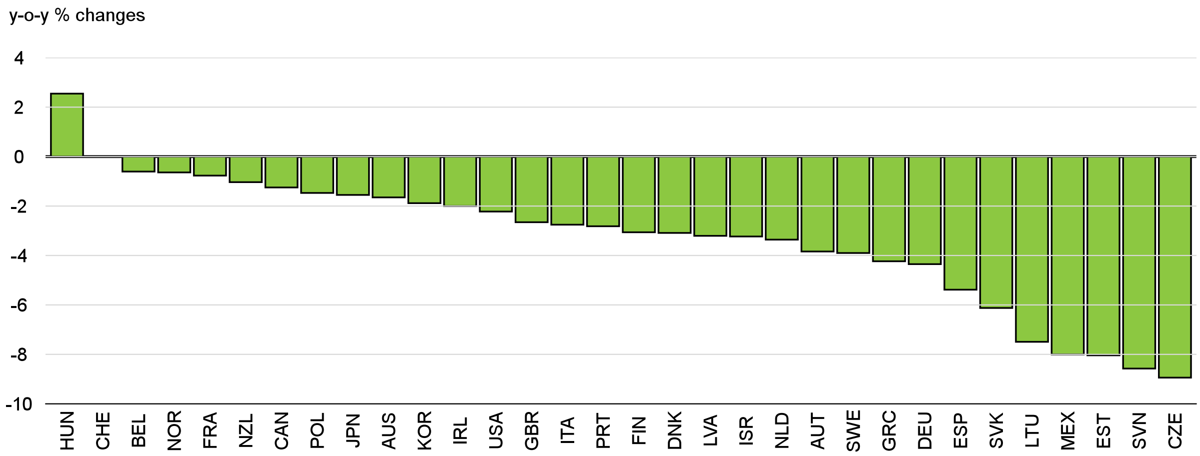
[3] It is less clear whether countries that have experienced a fall in labour force participation for reasons linked to the pandemic have an untapped reserve of workers that could be easily brought into the workforce, or whether these workers' attachment to the labour market has been durably weakened.

[4] Over the two-year period 2020-21, permanent-type immigration to the United States, the largest receiving country, was lower than the pre-pandemic average by nearly 1 million people. The US labour force shrank by 2.3 million in this period, suggesting that the lower level of immigration is likely to have contributed to the tightening of labour market conditions and the emergence of labour shortages in some sectors.

Figure 1.9. Real wages are declining in most economies

Real compensation per employee, total economy, 2022Q3



Note: Compensation per employee deflated using the personal consumption expenditures deflator.
Source: OECD Economic Outlook 112 database; and OECD calculations.

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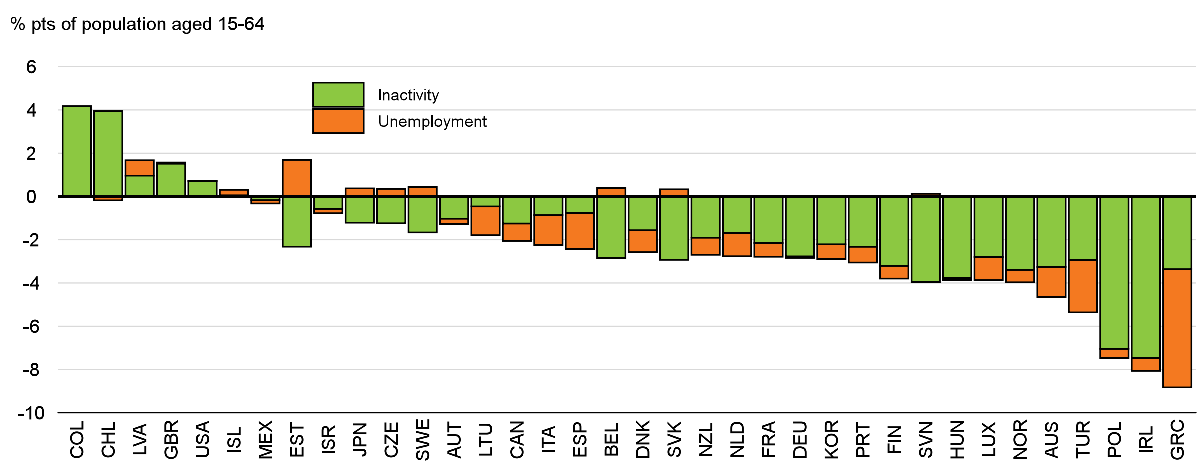
Figure 1.10. Unemployment and inactivity rates have fallen in most OECD economies

Difference between 2022Q2 and 2019Q4



Source: OECD Labour Force Statistics; and OECD calculations.

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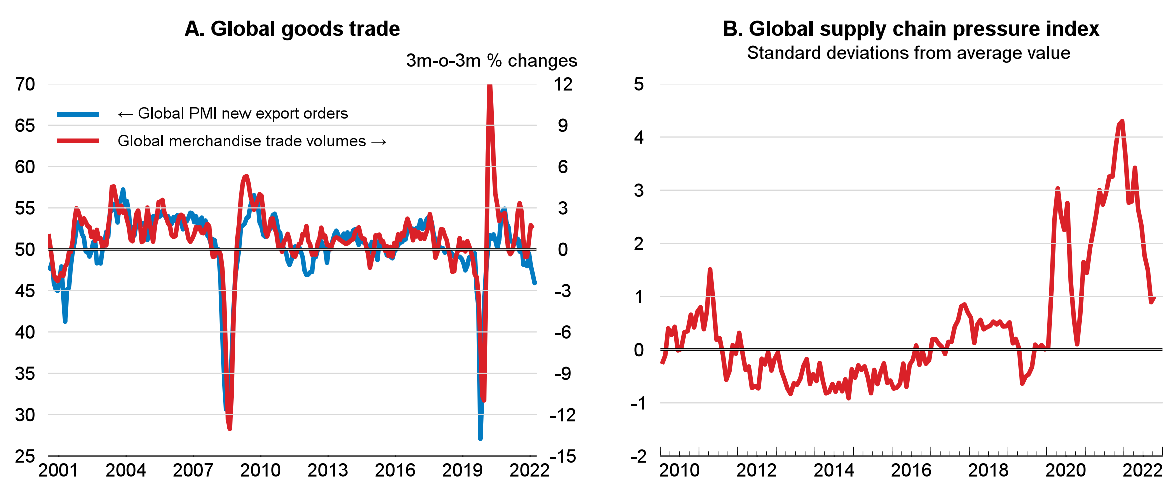
Trade growth held up in the first half of 2022, but recent indicators have weakened

Global trade continued to recover in the first half of 2022, helped by strong demand and some easing in supply chain bottlenecks and port congestion (Figure 1.11, Panel B), alongside the lifting of most COVID-19 restrictions in many countries. This helped to offset a sharp contraction in China's imports in the first half of 2022 as its zero-COVID-19 policy remained in place. Manufacturing surveys suggest backlogs of work have almost normalised and supplier delivery times have improved. The ongoing recovery in cross-border tourism also boosted services exports in most regions in the first half of the year. By the third quarter of 2022, the volume of global trade in goods and services 2022 was over 7% higher than in the fourth quarter of 2019, despite the incomplete recovery in services trade. The war in Ukraine has disrupted the usual pattern of bilateral trade flows, with sharp declines in trade between the advanced economies and Russia, and rising trade between Russia and some Asian economies. The Black Sea grain initiative allowed the resumption of grains trade from the port of Odessa, which has led to 10 million approved tonnes leaving since the first shipment on 1 August 2022.

Recent trade indicators have been mixed, but there are signals that trade growth is set to slow. Survey measures of new export orders in manufacturing have fallen sharply, particularly in Europe (Figure 1.11, Panel A). Container port traffic volumes continued to rise through to September, but early estimates from the Kiel Trade Indicator suggest that global merchandise trade may have contracted in October.

Changes in the terms of trade and net income transfers from the rest of the world impact countries' disposable income and consumption possibilities in addition to the changes in production activity measured by GDP growth. Sizeable swings in the terms of trade have occurred for many countries in 2022, due to changes in exchange rates and commodity prices. As a result, the growth of real gross national disposable incomes (RGNDI) is projected to be very different to real GDP growth in many countries. The growth of gross disposable national income for Norway and Saudi Arabia in 2022 is projected to be over 14 percentage points higher than GDP growth (Figure 1.12), reflecting high oil and gas export prices. In contrast, the trading gain (changes in the terms of trade) is projected to be negative in most other European economies in 2022, with the increase in RGNDI in the median EU economy projected to be over 1 percentage point lower than GDP growth in 2022, and with income declines in some countries, including Germany.

Figure 1.11. Global supply chain pressures have eased but new export orders are declining



Source: S&P Global; CPB Netherlands Bureau for Economic Policy Analysis; and Federal Reserve Bank of New York.

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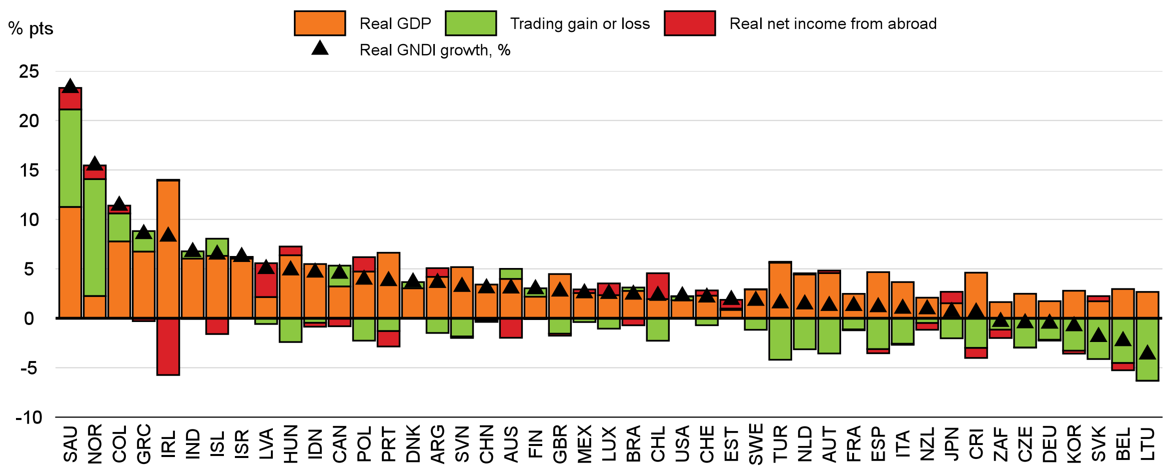
Figure 1.12. Terms-of-trade losses have hit incomes in energy importing economies, especially in Europe

Contribution to real gross national disposable income growth in 2022



Source: OECD calculations.

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Financial market conditions have tightened significantly

The accelerated pace of monetary policy tightening in major economies and rising risk aversion have led to a further tightening of global financial conditions. Volatility has surged, particularly in government bond markets, surpassing the peak observed at the height of the pandemic (Figure 1.13, Panel A). Larger increases in market interest rates in the United States relative to many other economies have pushed the US dollar to its highest level in the last two decades, contributing to greater volatility in the currency markets of advanced and emerging-market economies (Figure 1.13, Panel B). A sharp deterioration of liquidity conditions in sovereign and corporate bond markets has also exacerbated abrupt price developments (OECD, 2022b; IMF, 2022a).[5] Real long-term interest rates have risen in the United States, the United Kingdom and the euro area, reflecting a fast pass-through from surging policy interest rates to the long end of the yield curve, though they remain lower than typically observed prior to the global financial crisis (Figure 1.14).

Slowing growth and rising interest rates have weighed on equity markets in most advanced economies (Figure 1.15, Panel A). Price declines have been relatively large in many Central and Eastern European countries, reflecting weakening growth prospects. Recurring waves of COVID-19 outbreaks in China and moderating growth in Korea have led to capital outflows and also hit equity markets. In contrast, equity prices have risen in a few commodity exporters, as well as in India, where new free trade agreements have attracted foreign capital, and Türkiye, reflecting strong domestic investor demand to hedge against high inflation risk.

Government bond yields have increased in almost all countries since May (Figure 1.15, Panel B). In the euro area, government bond yields have increased broadly in line with those in the United States, despite the earlier start to US monetary policy tightening. The announcement of the Transmission Protection Instrument by the ECB in July and a significant use of flexibility across countries in bond reinvestments have limited the increase in sovereign spreads within the area. Yields have increased significantly less in emerging-market economies and have remained stable in Japan, reflecting the yield curve control policy.

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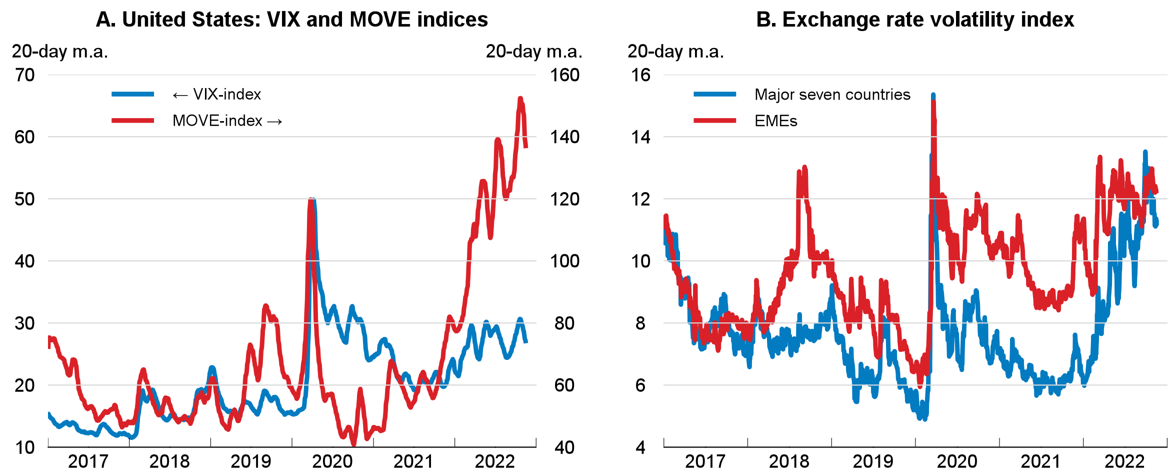
[5] In the United Kingdom, the announcement in September of debt-financed expansionary fiscal plans contributed to an unanticipated surge in long-term gilt yields. Efforts by leveraged UK-based institutional investors, primarily pension funds, to boost liquidity through asset sales then contributed to further rises in bond yields, creating an adverse feedback loop (Breeden, 2022). Intervention by the Bank of England, with a time-limited long-term bond purchase programme in the first half of October, and subsequent changes in fiscal plans, reversed the initial rise in yields by mid-November.

Figure 1.13. Financial market volatility has increased



Note: Implied volatility as measured by the VIX index can be interpreted as the market expectation of risk (future volatility). The MOVE index is a yield curve weighted index of the normalised implied volatility on 1-month Treasury options which are weighted on the 2, 5, 10 and 30 year contracts.
Source: Refinitiv; and OECD calculations.

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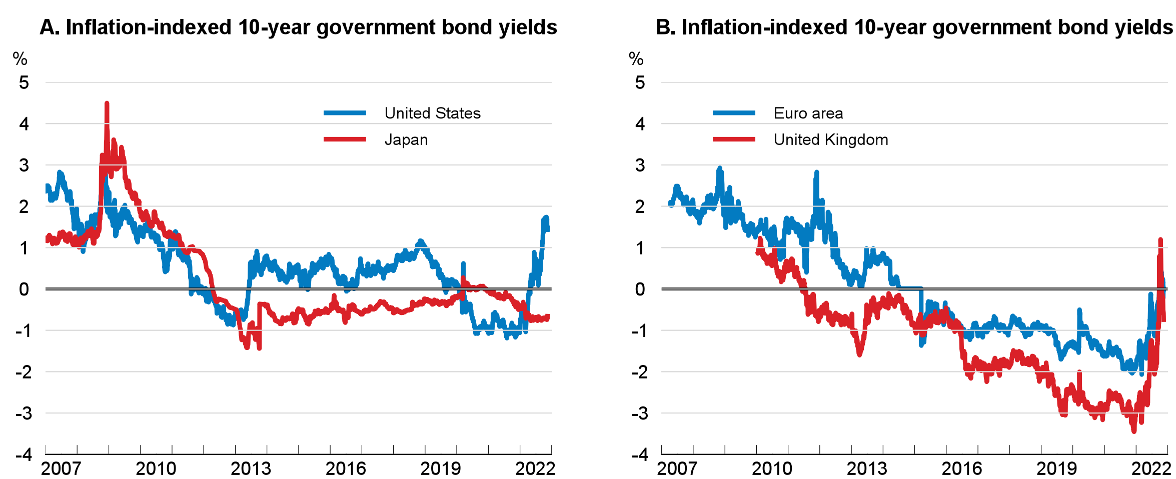
Figure 1.14. Real long-term interest rates have risen sharply in many countries



Source: Refinitiv; and OECD calculations.

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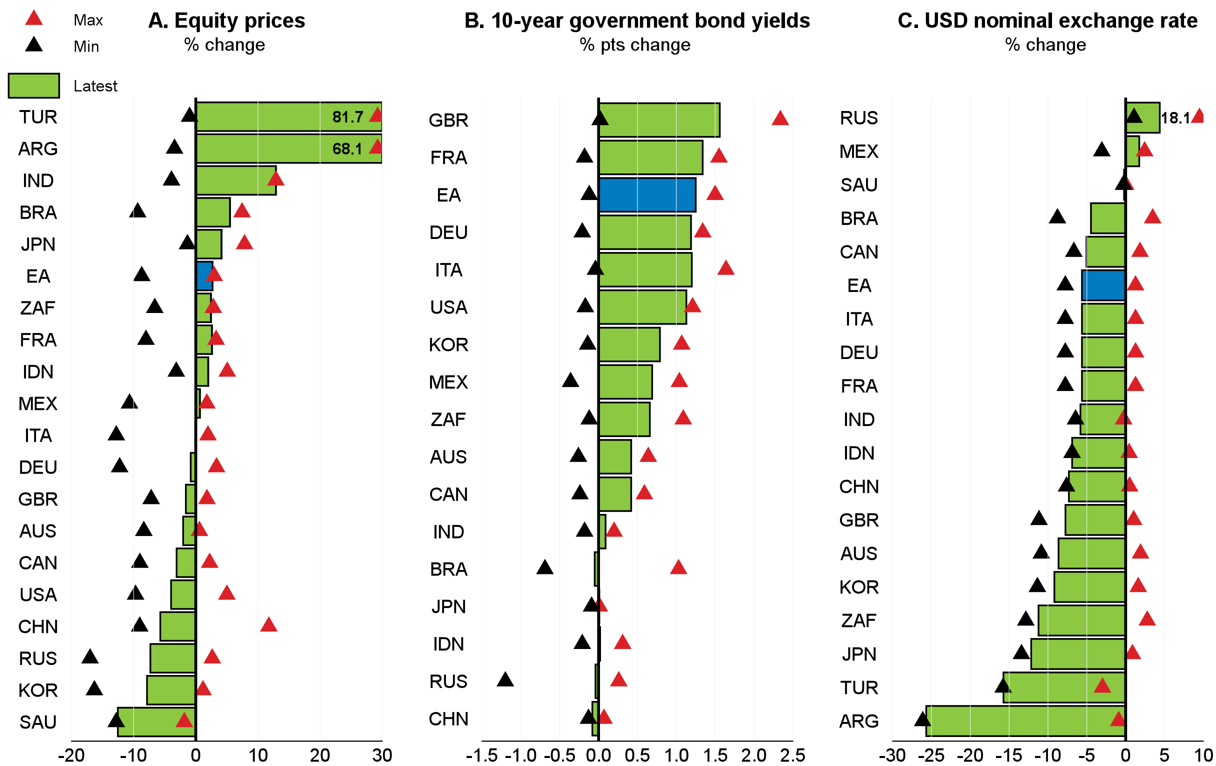
The US dollar has appreciated further against most advanced economy currencies since May (Figure 1.15, Panel C), reflecting a faster pace of monetary policy normalisation in the United States, particularly vis-à-vis Japan, and sharply deteriorating growth prospects in the euro area and the United Kingdom. With the exception of a few commodity exporters, almost all emerging-market economy currencies have depreciated against the US dollar.

Figure 1.15. Financial market conditions have tightened significantly



Note: 'Latest' refers to the change between the average of May 2022 and the latest available data up to November 16. 'Maximum' and 'Minimum' refer to the largest increases or falls relative to the average of May 2022. Based on a 10-day average of daily observations.
Source: Refinitiv; and OECD calculations.

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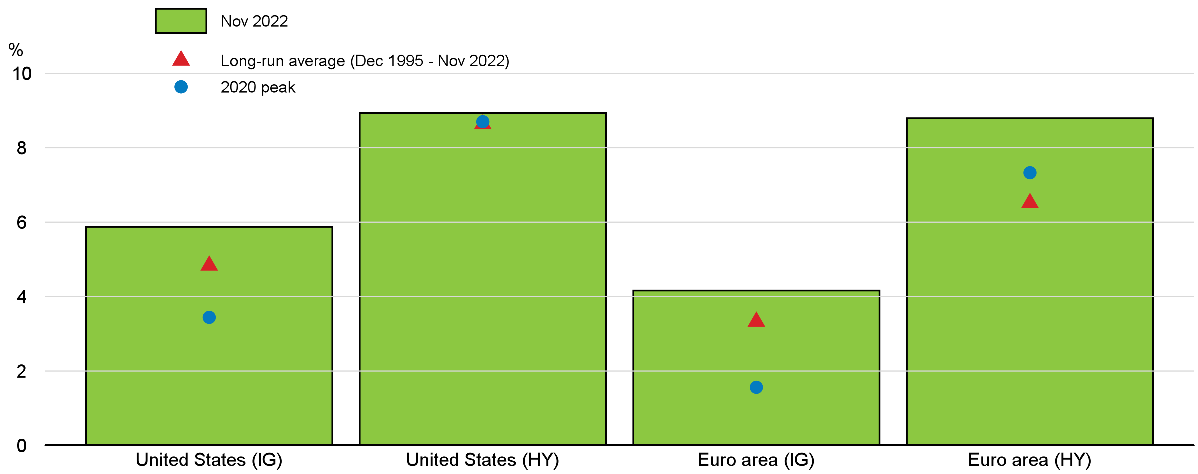
Financing conditions have continued to tighten for firms and households. In the euro area, interest rates on new lending to businesses in September were 120 basis points higher than their 2021 low, and corporate bond yields have also increased. In the United States and the euro area, yields on high-yield bonds and leveraged loans have reached levels close to or above those at the height of the pandemic (Figure 1.16) and recent issuance of high-yield bonds has slowed to its lowest level since the global financial crisis. Corporate bond and credit default spreads have also widened, particularly in Europe in the face of rising concerns about energy shortages and the sustainability of leveraged firms (OECD 2022a). Current and expected increases in policy rates have also passed through swiftly to new fixed-rate mortgage lending rates in many countries, and are also affecting countries with a relatively high share of adjustable-rate mortgages, adding to potential vulnerabilities (see below).

Figure 1.16. Corporate bond yields have risen sharply



Note: IG and HY refer to Investment Grade and High Yield bonds, respectively. The 2020 peak for the United States corresponds to March 2020 and for the euro area to April 2020.
Source: ICE BofA Indices database; and OECD calculations.

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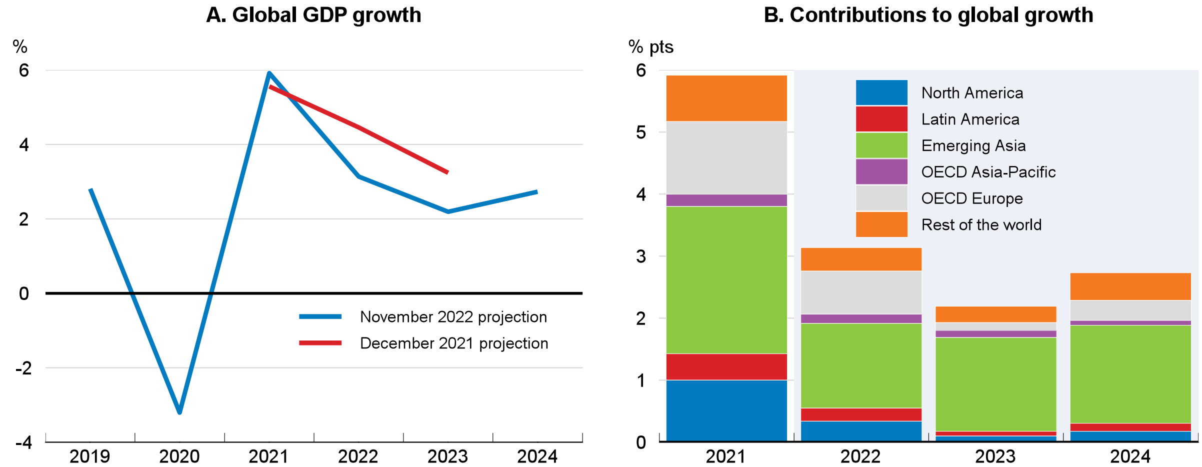
Global growth is projected to weaken further with inflation slowing gradually

The global economy is facing a period of weak growth and persistent inflation, with elevated downside risks. Tighter monetary policy and higher real interest rates, elevated energy prices, weak household income growth and declining confidence are all expected to take a toll on growth, especially in 2023. Fiscal support to cushion the impact of high food and energy costs will help to limit the slowdown, although mild consolidation is still projected in most economies. Job losses may also be more limited than would be expected on the basis of past downturns if firms wish to retain workers that have been hard to recruit after the pandemic. Savings accumulated during the pandemic also provide some buffer for the household and corporate sectors, although these are not evenly distributed. High uncertainty could limit the extent to which savings are drawn down and deter firms from making longer-term investments.

The projected slowdown in global GDP growth in 2023 (Table 1.1; Figure 1.17, Panel A) is cushioned to some extent by an expected further fall in household saving rates in several major advanced economies, though not in the United States, where the saving rate has already dropped below pre-pandemic levels. A mild recovery is projected to get underway in most countries in 2024, with real income growth recovering and fading inflation pressures providing space for initial steps to ease monetary policy in North America, Central and Eastern Europe and many emerging-market economies.

Prospects in the Asia/Pacific region, where many countries have relatively low inflation and policy support is projected to help growth recover in China, appear stronger than in the Americas or Europe. Near-term output declines are projected in many European countries, including Germany, Italy, the United Kingdom and the overall euro area. This results in an unusually imbalanced projection, with outcomes heavily reliant on the absence of any significant downside shocks in the major Asian emerging-market economies, which collectively account for close to three-quarters of global growth in 2023 and around three-fifths in 2024 (Figure 1.17, Panel B). Europe is being affected particularly heavily by the impact of the war in Ukraine and high energy prices, which are expected to persist throughout the projection period.

Figure 1.17. Global growth is projected to slow and be increasingly imbalanced across regions



Note: In Panel B, Emerging Asia comprises China, India, Indonesia and the Dynamic Asian Economies. Latin America comprises Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico and Peru. Contributions calculated moving PPP shares of global GDP.
Source: OECD Economic Outlook 112 database; OECD Economic Outlook 110 database; and OECD calculations.

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The prospects for individual major economies over the next two years differ widely.

- High inflation and rising interest rates are restraining growth in North America. In the United States, real wages have fallen, and the tightening of monetary policy has pushed up interest rates at all maturities, weakening investment, especially in the housing market. Higher interest rates have also resulted in a strengthening of the dollar, exerting a headwind on export activity. GDP growth is projected to slow from 1.8% in 2022 to 0.5% in 2023, before picking up to 1.0% in 2024. Slower growth will lessen the tightness of labour markets, with a rise of about 1 percentage point in the unemployment rate over the projection period. Together with weaker demand pressures and easing of supply chain bottlenecks, this is projected to allow inflationary pressures to gradually recede. Core inflation is expected to get back close to the Federal Reserve's 2% target towards the end of 2024, permitting some easing of monetary policy. Canada's economy is subject to many of the same forces and expected to have a similar profile of growth and inflation through 2023-24, with both headline and core inflation converging towards the 2% target by the end of 2024, permitting some easing of monetary policy in the second half of that year.
- The major advanced economies in Asia are projected to experience less of a slowdown than other regions. Growth in Japan is projected to remain above potential, but moderate gradually. Higher energy prices have hindered real household income growth and dented confidence and business investment, and a loss of economic momentum in key trading partners is checking export growth. Fiscal policy is projected to be more supportive in 2023, but then tighten in 2024. GDP growth is expected to be 1.8% in 2023 and 0.9% in 2024, after 1.6% in 2022. The unemployment rate is projected to continue to edge down in 2023-24, reaching 2.4%, and the further tightening of labour markets is reflected in a projected increase in core inflation from 0.3% in 2022 to 1.6% in 2023 and 1.7% in 2024. Weak external demand is also a factor in the projected slowdown in Korea, along with modest disposable income growth and a soft housing market. GDP growth is expected to slip from 2.7% in 2022 to a little under 2% in 2023 and 2024. Inflation will remain high for some time in 2023 due to service and utility price pressures, but will gradually moderate to under 2% by the end of 2024.

- Growth in Europe is slowing sharply in late 2022 as a result of the war in Ukraine and weak external demand, with output projected to decline in several countries over the winter. Held back by high energy and food prices, weak confidence, continuing supply bottlenecks and the initial impact of tighter monetary policy, annual growth in the euro area in 2023 is projected to be 0.5%, after 3.3% in 2022, before picking up to 1.4% in 2024 as spending starts to recover. The implementation of Next Generation EU plans should underpin investment. Subdued demand growth will help to moderate inflation, but tight labour markets, and the prospect that high wholesale energy prices will continue to feed into retail prices in 2023 and 2024, means that inflation will subside only gradually, remaining above target in 2024. Higher interest rates, elevated energy and food prices and weak confidence are affecting the United Kingdom, where output is projected to contract by 0.4% in 2023 and rise by only 0.2% in 2024, with tighter fiscal policy restraining the rebound. As in the euro area, weaker demand is projected to help bring inflation down steadily, to 6.8% in 2023 and 3.4% in 2024.
- In China, recurring waves of lockdowns have disrupted economic activity in 2022. With weaker housing investment also remaining a significant headwind, growth in 2023 and 2024 will be sustained by infrastructure investment and other measures to moderate the correction in the real estate sector. After 3.3% in 2022, GDP growth is projected to pick up to 4.6% in 2023 before easing to 4.1% in 2024. Consumer price inflation is expected to remain benign, helped by the current policies to manage energy and food prices.
- The other major Asian emerging-market economies are also projected to be relatively resistant to global headwinds next year, and to have only a modest and short-lived overshooting of inflation objectives. In India, growth is projected to dip from 6.6% in the current (2022-23) fiscal year to 5.7% in FY2023-24, before rebounding to 6.9% in FY2024-25, broadly in line with the pre-pandemic trend. Higher food and energy prices have dented households' purchasing power, and the expected weakness of external demand over the coming year will also moderate activity, despite a strong pick up in contact-intensive service sectors, including international tourism. Consumer price inflation will remain above 6% (the upper limit of the central bank's target range) until early 2023 before gradually receding as higher interest rates take effect. Growth in Indonesia is projected to remain buoyant owing to strong demand for Indonesia's main export commodities, as well as pent-up consumption from the pandemic period. GDP growth will remain close to 5% in 2023 and 2024, while inflation should fall back under the 4% ceiling of the central bank's target band by the end of 2023 as the effects of monetary tightening are felt.
- The major Latin American economies have performed better than expected in 2022, especially food and energy exporters which benefitted from improved terms of trade. This rebound is expected to lose steam during 2023 and 2024, amid tighter global and domestic financial conditions, a withdrawal of most remaining fiscal support and less buoyant commodity prices. Inflation in the major Latin American economies is likely to be close to its peak currently, but will recede only gradually, despite early rate increases by many Latin American central banks that have delivered firmly positive real interest rates. In Brazil, slowing export momentum, tight credit conditions and a less expansionary fiscal policy are projected to curb growth in 2023, with only a modest improvement in 2024. Annual GDP growth is projected to be 2.8% in 2022, 1.2% in 2023 and 1.4% in 2024. As supply bottlenecks fade and the effects of higher policy rates continue to materialise, inflation is projected to decline to between 4-4½ per cent in 2023 and 2024.
- Against the backdrop of slowing global trade and tighter monetary conditions, annual GDP growth is expected to weaken in 2023 in most other advanced and emerging-market economies, before recovering somewhat in 2024. Output is projected to contract in a number of economies in 2023, including Chile, the Czech Republic, Latvia and Sweden. Central and Eastern Europe, the region most directly affected by the war in Ukraine, generally has both markedly weak growth and relatively high inflation through 2023, while countries in the Asia/Pacific region typically suffer less of a growth

slowdown next year and have lower peak inflation rates than elsewhere. In almost all the smaller economies, as in the larger ones, inflation is projected to decline in both 2023 and 2024, but often to remain above central bank targets even at the end of that period.

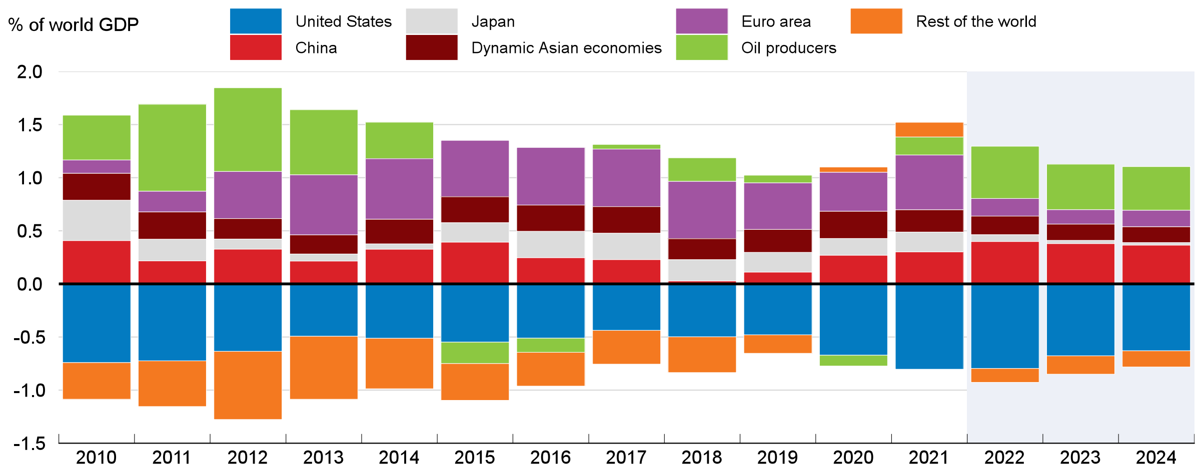
The slowdown in output growth in 2023 is not generally expected to be reflected in large rises in unemployment. The OECD-wide unemployment rate is projected to increase to around 5.5%, some 0.5 percentage points above the low point in mid-2022, with many firms holding on to workers that have been hard to recruit since the pandemic, amidst softer labour force growth and only small increases in participation rates in most OECD economies over the next two years. Job growth is also projected to slow sharply, from around 3% this year in the OECD economies to 0.5% per annum on average in 2023-24, with declines in employment in 2023 in several Central and Eastern European economies, Denmark, Finland, Italy and Sweden. Such labour market outcomes would nonetheless be mild by the standards of past slowdowns, and a risk is that this could prolong elevated cost pressures for longer than expected.

Consumer price inflation in many economies is projected to stay higher for longer than previously foreseen, despite a larger and more rapid tightening of monetary policy in much of the world and the gradual easing of some supply bottlenecks in goods markets. This reflects in part the war in Ukraine, especially in Europe, where the implications of the sharp rise in the price of imported natural gas in 2022 will continue to be felt in 2023 and 2024 as delayed retail price increases for electricity and gas come through and existing price caps become less generous. Nonetheless, with policy interest rates generally rising into 2023 and then being maintained at high levels throughout the projection period, resource pressures diminishing and energy price inflation slowing, inflation is projected to fall and approach central bank objectives in many economies in 2024.

Annual inflation in the OECD economies is projected to decline, from 9.4% in 2022 to 6.5% in 2023 and 5.1% in 2024. Inflationary pressures are projected to ease in all countries, but this is likely to take some time in those with very tight labour markets and broad-based inflation pressures at present. In 2023, headline inflation is projected to be over 10% for a second successive year in Hungary, Poland, the Slovak Republic and the Baltic States, and be 8% in Germany and over 6½ per cent in the euro area as a whole. In contrast, price pressures are expected to ease considerably in 2023 and 2024 in the United States, Canada, Australia and Korea, and remain mild in Japan. Inflation is projected to continue to diverge in the emerging-market economies, with continued low inflation in China, very high inflation in Argentina and Türkiye, and inflationary pressures generally receding in other countries as tighter monetary policy takes effect.

Global trade volume growth is projected to slow to 2.9% in 2023 as demand softens and price pressures mount, with the slowdown particularly noticeable in Europe and the United States. The resumption of growth in China will help to offset some of the softness in OECD activity, but import demand is also expected to be subdued in many commodity-importing countries. A mild upswing is projected in 2024, with global trade growth picking up to 3¾ per cent. Global current account imbalances are expected to remain higher than prior to the pandemic (Figure 1.18). China’s trade surplus will remain elevated as exports grow robustly and international tourism imports remain well below pre-crisis levels over the projection period. This increase is offset by a lower surplus in Japan and in Europe, in part due to the adverse terms of trade shock from higher imported energy prices. The US current account deficit will only decline marginally over the projection period. As commodity prices are assumed to remain unchanged at high levels in the projections, many oil-exporting economies are expected to have persistent and sizeable current account surpluses.

Figure 1.18. Current account imbalances are higher than immediately prior to the pandemic



Note: The Dynamic Asian Economies aggregate includes Hong Kong (China), Malaysia, Chinese Taipei, the Philippines, Singapore, Thailand and Vietnam. The oil producers aggregate includes Algeria, Angola, Azerbaijan, Bahrain, Brunei, Chad, the Republic of Congo, Ecuador, Equatorial Guinea, Gabon, Iran, Iraq, Kazakhstan, Kuwait, Libya, Nigeria, Oman, Qatar, Saudi Arabia, Sudan, Timor-Leste, Trinidad and Tobago, Turkmenistan, United Arab Emirates, Venezuela and Yemen. The rest of the world aggregate includes all countries which are not listed.
Source: OECD Economic Outlook 112 database; and OECD calculations.

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Key risks and vulnerabilities

The impact of lower energy imports to Europe from Russia could prove more severe than expected

European economies continue to face significant challenges from the current and planned embargoes on Russian coal and seaborne oil imports, and from the dwindling supply of gas from Russia into the European market. A key risk around the projections is that the associated increase in energy prices proves much more disruptive and persistent than assumed in the baseline. Past experience suggests that sizeable increases in energy expenditures in OECD economies are often associated with recessions (Box 1.2).

The search for alternative sources of supply has been an important factor pushing up energy costs this year, with European countries bidding to attract supply from other markets amidst tight global supply conditions. There are sizeable differences across European countries and industries in the energy mix and the reliance on different types of energy inputs. The ongoing shift away from Russian imports is thus affecting sectors in different ways according to their initial dependency on energy imports from Russia, the scope to obtain alternative energy supplies, and the extent to which they are impacted by cutbacks elsewhere in their supply chains. Such challenges are particularly acute in Germany, as well as in many Central and Eastern European economies, and in energy-producing sectors, transport (where specialised refined fuels from Russia can be hard to replace), minerals and metals manufacturing and the chemicals industry.

For OECD Europe as a whole, estimates derived by combining input-output and sectoral energy use data suggest that output in manufacturing and market service sectors could decline by between 2¾-3 per cent, if energy inputs from Russia were not offset by drawing down stocks or by substituting other energy inputs (OECD, 2022c). Such estimates are very uncertain, as energy supply disruptions to key production processes or shortages of fuels for transportation could force companies to shut down production completely rather than reduce it proportionally. The near-term impact of a simultaneous sharp contraction in production across many sectors and countries is also likely to be larger than if only one country is affected.

Gas supplies are a particular concern in Europe over the next two winters. Gas and electricity prices are already elevated and could jump further in the event of shortages emerging in Europe. Such shortages could occur if non-Russian gas supplies from outside the EU fail to materialise to the extent expected, or if the demand for gas is exceptionally high due to a cold winter (Haas et al., 2022; IEA, 2022a). EU gas storage levels have been raised considerably through 2022, and in October were over 92% on average in EU member states and full in many. Even at this level, there is still some uncertainty about whether demand in a typical winter can be met without storage levels in the European gas market being pushed below effective operational levels, unless the reductions in energy consumption in the last few months are maintained. In this respect, it is important that fiscal measures to support households and companies continue to allow price signals to operate to help to bring about the necessary adjustment of consumption. A prolonged cold winter would be more likely to result in shortfalls unless additional gas supplies could be obtained in the near term, which would inevitably require substantially higher prices, or demand is reduced strongly. Even if supplies prove adequate for the forthcoming winter, significant challenges are likely to persist through 2023 and keep gas prices elevated, with European economies continuing to face substantial difficulties in securing sufficient supplies to rebuild storage capacity ahead of the 2023-24 winter (Fulwood, 2022; IEA, 2022b). In turn, such efforts will push up gas prices and reduce the quantities of LNG available outside Europe, especially in Asia, with detrimental effects on some developing economies.

Box 1.2. Energy expenditures since the 1970s

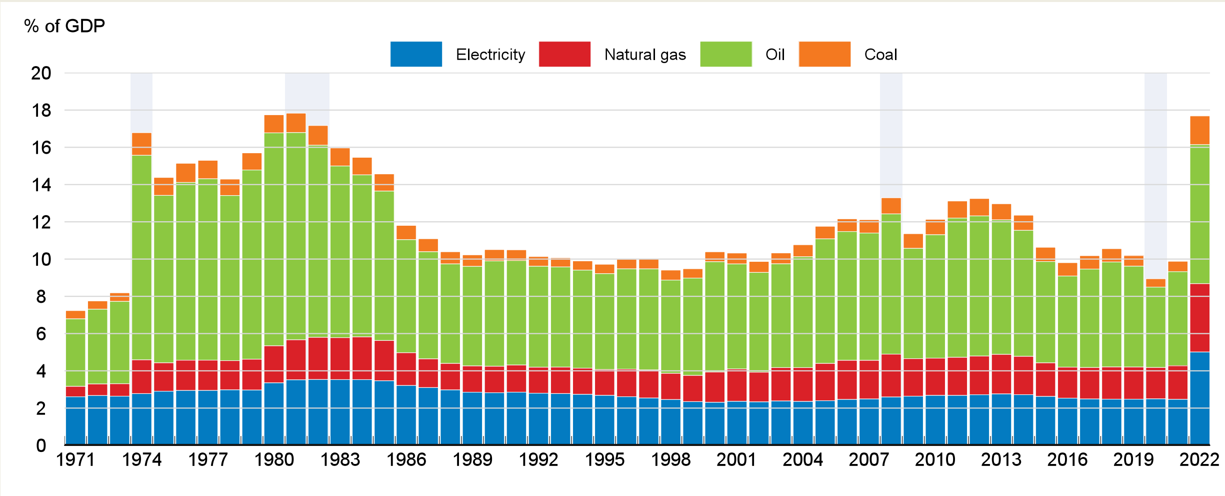
Fluctuations in the share of energy expenditures in total spending are closely associated with cyclical changes in economic activity. With energy an important input for firms, a rise in energy prices typically shifts the aggregate supply curve of the economy upwards, all else equal, lowering output and raising the price level. Higher energy prices also erode the purchasing power of households: when energy prices surge, energy expenditures tend to increase, crowding out other spending. The negative effect on aggregate demand amplifies the effect of the supply shock on output while somewhat offsetting the impact on overall consumer prices. The negative demand effect could be mitigated to the extent that domestic energy producers spend their windfall profits, or distribute the extra income to households who spend it, but most OECD countries are importers of fossil fuels, and recipients of energy price windfalls generally tend to spend their extra income slowly (Cookson et al., 2022).

Estimated expenditures on energy – oil, natural gas, coal and electricity – have risen sharply this year in OECD economies (Figure 1.19), with relatively similar fluctuations over time across most OECD countries. The estimates use consumption volumes and end-use prices – which include taxes – from the International Energy Agency. For 2022, the volumes consumed are assumed to be equal to the average of those in 2019 and 2021, with price levels estimated using the average of observed 2022 data compared to 2021 for reference prices for each category (in local currency terms): Brent for oil products, ICE Newcastle futures for coal, and national wholesale prices for electricity and natural gas.

The expected relationship between energy expenditure shares and economic cycles in the OECD region is clearly visible. During the past five decades, OECD-wide recessions have – with the exception of the COVID-19 recession in 2020 – only occurred when the ratio of energy expenditures to GDP has been at a high level (always at least 13%) and rising. These findings are consistent with the results of studies of even longer periods (Fizaine and Court, 2016) and studies of the link between oil price increases and US recessions (Kilian and Vigfusson, 2017). The rapid rise in estimated OECD-wide energy expenditures this year, to around 17% of GDP, is a warning signal about the near-term risk of widespread recessions among OECD economies.

Figure 1.19. Periods of high energy expenditures are often associated with a recession

Estimated energy end-use expenditures for the OECD economies



Note: Recessions (shaded areas) correspond to years in which there were at least two negative quarterly GDP growth rates for the OECD aggregate. Estimates of the level of energy expenditure, computed as end-use prices in local currency multiplied by volumes consumed, are produced at the country level for 29 OECD countries. GDP shares are then aggregated using moving GDP weights in PPP terms. End-use prices (defined as the average unit price effectively paid by industrial and household consumers as well as for electricity generation) include taxes. Prices start in 1978 in the IEA database; they were backcast to 1971 using the Brent price for oil, and prices for coal products and natural gas, and the rate of increase of the electricity price in the US CPI for electricity. Prices are extended to 2022 using the growth rate of reference prices converted in local currency (average of observed 2022 data compared to 2021): Brent for oil, ICE Newcastle futures for coal, and wholesale prices for electricity and natural gas (available for 25 and 27 OECD countries, respectively). For 2022, the volumes consumed correspond to the average of 2019 and 2021.
Source: International Energy Agency; OECD Economic Outlook 112 database; Refinitiv; US Energy Information Administration; Japanese Power; German Federal Network Agency (SMARD); Korea Electric Power Statistics Information System; Canada Independent Electricity System Operator; and OECD calculations.

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At the same time, the composition of the current surge in energy expenditure is different to that seen in earlier episodes. Past swings in expenditures on energy have been mostly driven by spending for oil products, whereas the upswing in 2022 is more broad-based, with large contributions from gas and electricity. It is possible that this difference is relevant for the relationship between overall energy expenditure and OECD-wide downturns. For one thing, the most extreme increases in the prices of gas and electricity have taken place in Europe: it is likely that the consequences for output will likewise be skewed. Indeed, the United States and a number of other OECD countries are net exporters of gas (and oil) and thus benefit from terms of trade improvements resulting from the surge in energy prices.

The first large increase in OECD-wide end-use expenditures happened in 1974 with the ratio of energy spending to GDP rising by nearly 8½ percentage points in one year, of which over 6½ percentage points came from oil products. This was due to the first oil crisis, following the announcement by Arab members of OPEC of an oil embargo in October 1973, which pushed the oil price sharply higher: the average price in 1974 tripled relative to 1973.

In subsequent decades, spending on oil products has been a key driver of the evolution of energy expenditures, reflecting oil's large share in consumption volumes and its relatively high degree of price volatility. The second oil crisis, in 1979, resulted in an increase in energy expenditure of 3½ percentage points of GDP over two years, while the mid-1980s oil glut caused spending to decline by around

8 percentage points, after which it stabilised at around 10% of GDP. It was only in the second half of the 2000s that energy expenditures started to increase again, peaking in 2008 at around 13% of GDP, with two-thirds of the increase being explained by spending on oil products. The relative stability of energy expenditures from the mid-1980s to the early 2000s hid a decline in energy intensity (energy consumed per unit of real GDP) of about 15% which was offset by a similar increase in the relative (weighted) price of energy. Indeed, energy intensity in OECD economies has declined steadily since the first oil crisis, falling by more than 50% over the period 1971-2021. This was driven by falls in the oil and coal intensity of GDP, with intensity remaining relatively stable for electricity and increasing for gas.

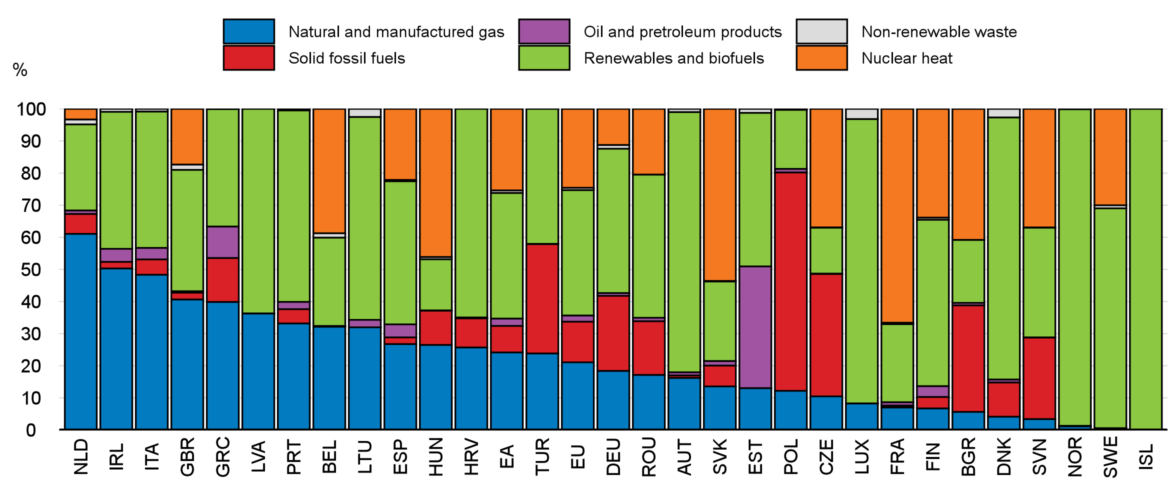
For 2022, the estimated increase of 7¾ percentage points is similar to that observed in 1974, and takes the ratio of energy spending to GDP back to the levels seen from the mid-1970s through to the mid-1980s. Expenditures related to all energy products are increasing significantly, with spending on electricity, oil products, natural gas and coal products increasing by 2½, 2¼, 2 and 1 percentage points, respectively.

One of the key unknowns about the current episode is the speed and extent of the pass-through from global or wholesale prices to end users (Figure 1.3). The increase in global and wholesale prices that has already occurred could be spread into 2023 or beyond, or may never even reach end users, depending on public policies and the future evolution of prices. To the extent that end users are not exposed to the full price impact, the implications for aggregate demand may be more muted than suggested by the underlying swing in energy costs.

EU member countries have already agreed on efforts to lower energy consumption in the near term, and higher prices have also begun to slow demand to some extent. Nonetheless, risks of enforced reductions in usage remain, implying potentially sizeable declines in energy consumption in some countries and industries where there is either a relatively high direct use of gas or a high indirect use via electricity production (Figure 1.20). Some industries that use gas intensively, such as metals manufacturing and chemicals, could see declines of between 4-6% in the median EU economy in the event of a 10% decline in gas usage and a 10% reduction in the use of gas for electricity (OECD, 2022d).

Figure 1.20. Gas is an important energy source for electricity generation in many European countries

Electricity production by energy source in 2020



Source: Eurostat.

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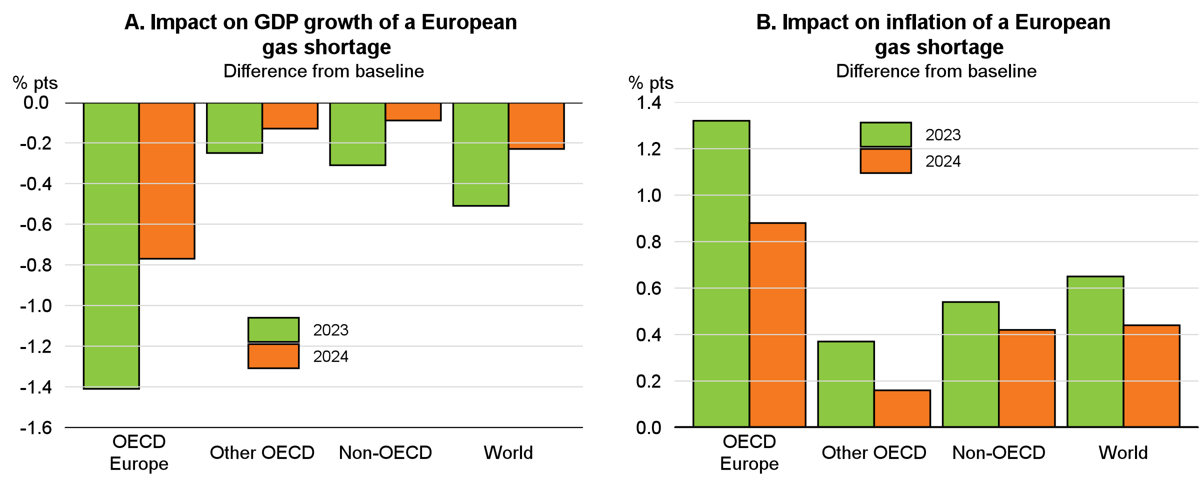
Illustrative simulations, using the NiGEM global macroeconomic model, highlight the potential hit to growth and additional inflation in 2023 and 2024 that could arise from gas shortages in Europe and the associated uncertainty that might arise. Shortages are assumed to push up global gas, fertiliser and oil prices (as European countries bid for additional gas supply in world markets), hit confidence and financial conditions and require a temporary period of enforced reductions in gas use by businesses in early 2023 and again in early 2024 (OECD, 2022d).

Taken together, the shocks could reduce growth in the European economies by close to 1½ percentage points in 2023, relative to baseline, and raise inflation by over 1¼ percentage points (Figure 1.21). This would push many countries into a full-year recession in 2023. Growth would also be weakened in 2024 by around ¾ percentage point in Europe, and inflation raised by 0.9 percentage points. Higher prices and reduced working hours would hit real incomes, with household spending falling by around 2% in the European economies, and private sector investment would be hit by the higher user cost of capital and weak demand, declining by close to 10% by 2024. Within the European Union, the countries in Central and Eastern Europe would collectively be hit harder than others, with output lowered by around 1.6% in 2023, compared to a decline of 1.3% in the rest of the European Union. Outside Europe, the impact of the shocks would be smaller, but there would still be adverse impacts from higher inflation on real incomes (except in gas-producing economies) and weaker demand from Europe. For the world as a whole inflation would be pushed up by 0.6 percentage points in 2023 and 0.4 percentage points in 2024, with growth reduced by ½ percentage point and ¼ percentage point respectively.[6]

Figure 1.21. Prolonged gas shortages and greater uncertainty would hit growth and raise inflation in 2023 and 2024



Note: Illustrative scenario of the impact of gas shortages in Europe. The scenario assumes that global gas, oil and fertiliser prices rise by 50%, 10% and 25% respectively in 2023 and 2024. Greater uncertainty is modelled as an ex-ante 1 percentage point increase in the household saving rate and a 1 percentage point rise in the user cost of capital and investment risk premia in all EU economies and the United Kingdom in 2023 and 2024. A temporary period of enforced rationing in industry use is modelled by a 3% reduction in potential output in all EU economies and the United Kingdom in the first quarter of 2023 and 2024 via a combination of reduced technical efficiency and a fall in average hours worked.
Source: OECD calculations using the NiGEM macroeconomic model.

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[6] A related supply risk is that the impact of EU sanctions against Russian oil exports, which is incorporated in the baseline projections, could also prove more disruptive than anticipated, affecting global supply and pushing up oil prices further. This would add to global inflationary pressures in 2023. Particular uncertainty remains about the extent to which Europe will be able to obtain alternative supplies of some refined oil products currently imported from Russia, particularly diesel, and the possible price.

Monetary policy tightening highlights pre-existing financial vulnerabilities

There are increasing risks that fast-rising interest rates, tighter global financial conditions and significant asset repricing could expose longstanding financial vulnerabilities in advanced and emerging-market economies.

Rising private sector debt-service burdens and lower bond market liquidity are keys risks in the advanced economies

For households and companies, faster-than-expected rises in interest rates increase debt payments and make rollovers more difficult. A sharp increase in interest rates may jeopardise the ability of households and corporates to service their debts, potentially leading to defaults and bankruptcies, and to corrections in house prices. Prices have already started to decline in some OECD countries, albeit from very high levels, with house price-to-income ratios at record highs across most OECD countries in the second quarter of 2022. Population growth and rising disposable income are more important long-term drivers of house prices than real interest rates (Cournède et al., 2020), though the impact of the changes in the latter could be non-linear, with a larger response of house prices to a given increase in rates when these are at a low level (Nocera and Roma, 2017).

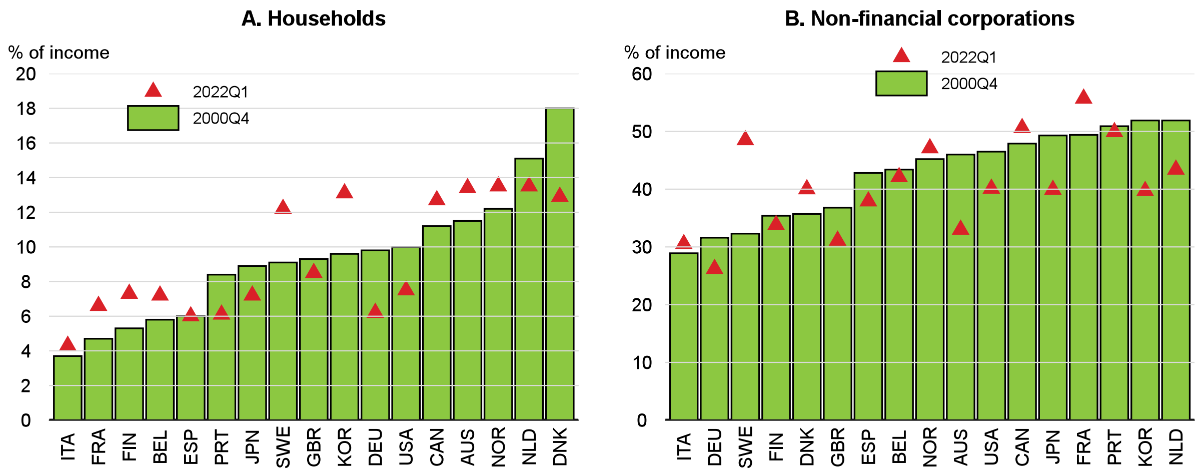
As interest rates continue to rise, households' financial positions can fall under stress given elevated debt levels. Even prior to the large increase in interest rates this year, household debt service ratios in the first quarter of 2022 were already often above those in the early 2000s, when interest rates were significantly higher (Figure 1.22, Panel A), reflecting higher debt levels. At the same time, declines in the share of variable-rate mortgages in some countries over the past two decades should cushion the impact of rising interest rates in the short run, although the share remains high in several countries (Figure 1.23). Moreover, even mortgages classified as fixed-rate are subject to rate renegotiation from time to time in many countries. Nonetheless, many households could still face a significant rise in their debt servicing costs. In many advanced economies, rising policy rates have already been passed through into mortgage rates and bank lending standards have also tightened (European Central Bank 2022b; Bank of England 2022a). Low-income families in countries where households are highly indebted and variable-rate mortgages are widely used, such as some Nordic countries, could be particularly vulnerable (OECD 2022c; Norges Bank 2021). Analysis by the Bank of International Settlements indicates that an increase in interest rates of 425 basis points (akin to the increase in the federal funds rate over the 2004-2006 period) could lead to an increase in debt servicing costs of more than 2 percentage points on average across advanced economies (BIS, 2022).

Rising policy rates can also expose financial vulnerabilities in the corporate sector. In the median OECD economy, the debt of non-financial firms reached 141% of GDP in 2021, 29 percentage points higher than in 2000, and debt-service ratios are already close to those prevailing at that time (Figure 1.22, Panel B). Although debt maturities have lengthened during the pandemic, the share of firms unable to service debt payments could increase sharply in the event of additional tightening by central banks. Default volumes on leveraged loans and high-yield bonds in the United States in June 2022 were already three times higher than in mid-2021 (Fitch Ratings, 2022) and downgrades of speculative-rated corporate bonds have outnumbered upgrades since November 2021 (OECD, 2022b).

Increased stress on households and companies, and the possibility of loan defaults, also raises risks of large potential losses at bank and non-bank financial institutions. This could amplify the impact of a shock to higher borrowing costs if it resulted in further significant tightening of financial conditions and lending standards and additional pressures on debt servicing capacity. Stress tests generally suggest that the tighter regulatory measures put in place since the global financial crisis have helped to improve the resilience of the banking sector to shocks (Ding et al., 2022). Nonetheless, many banks could still face substantial losses if a larger-than-expected downturn occurred, especially in emerging-market economies where banks are particularly sensitive to shocks and typically have lower capital ratios than in advanced economies.

Figure 1.22. Debt service obligations could surge

Debt service ratios



Note: Debt comprises loans and debt securities.
Source: Bank for International Settlements; and OECD calculations.

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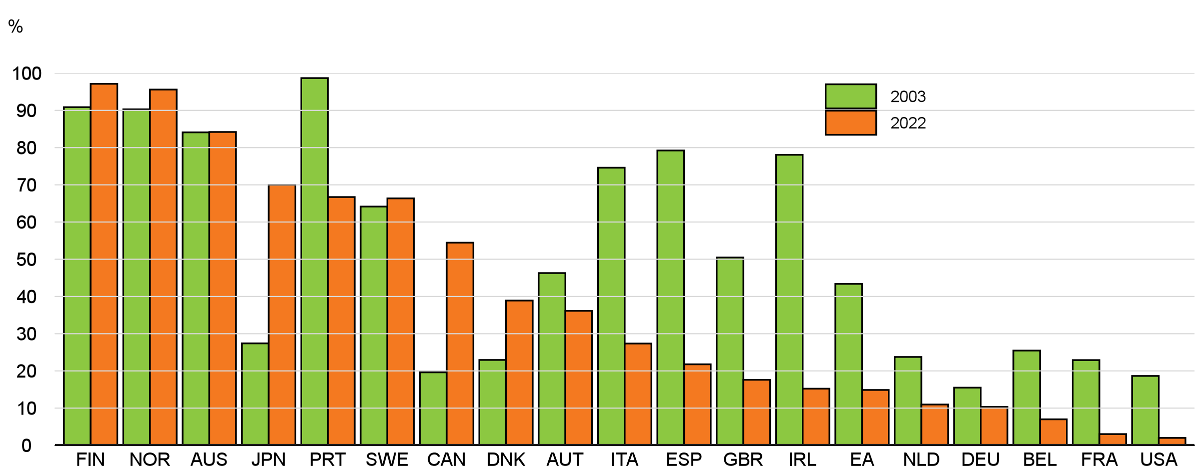
Figure 1.23. Variable-rate mortgages can exacerbate financial risks

Share of adjustable-rate mortgages in new mortgage issuance



Note: Adjustable-rate mortgage loans are new loans issued at variable rate or with an initial rate fixed for a period of up to 1 year. Due to limited data availability, the green bars for Norway and Sweden refer to 2006. For the United Kingdom, Canada and Australia the green bars respectively refer to 2008, 2013 and 2019. Orange bars refer to 2022 or to the latest available data.
Source: ECB; Financial Conduct Authority; Japan Ministry of Land, Infrastructure, Transport and Tourism; Norges Bank; Federal Housing Finance Agency; Bank of Canada; and Australian Bureau of Statistics.

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Rising interest rates can help some non-bank financial institutions, such as pension funds and life insurers, by reducing the net present value of their long-term nominal liabilities. At the same time, rapid increases in interest rates could also expose vulnerabilities in some of these institutions. Repricing of stretched asset valuations could lead to disorderly market corrections and investor outflows. Non-bank financial institutions could also suffer liquidity strains and mark-to-market losses on their assets, including on their portfolios of sovereign bonds, and be confronted with large redemption calls. For institutions that are highly leveraged, or which are subject to severe liquidity mismatches, such as open-ended funds, the impact could be particularly large. Energy utilities could also come under stress, as rising energy prices and high volatility lead to large margin calls on their derivatives positions. Concerns over the liquidity of energy utilities have already prompted several European governments to implement emergency support schemes in the form of short-term liquidity lines and loan guarantees. If defaults of some non-bank financial institutions and utility companies could not be prevented, they could reverberate across the rest of the financial system, leading to a sharp further tightening of financing conditions for households and corporates.

Financial vulnerabilities in emerging-market economies are exacerbated by external spillovers

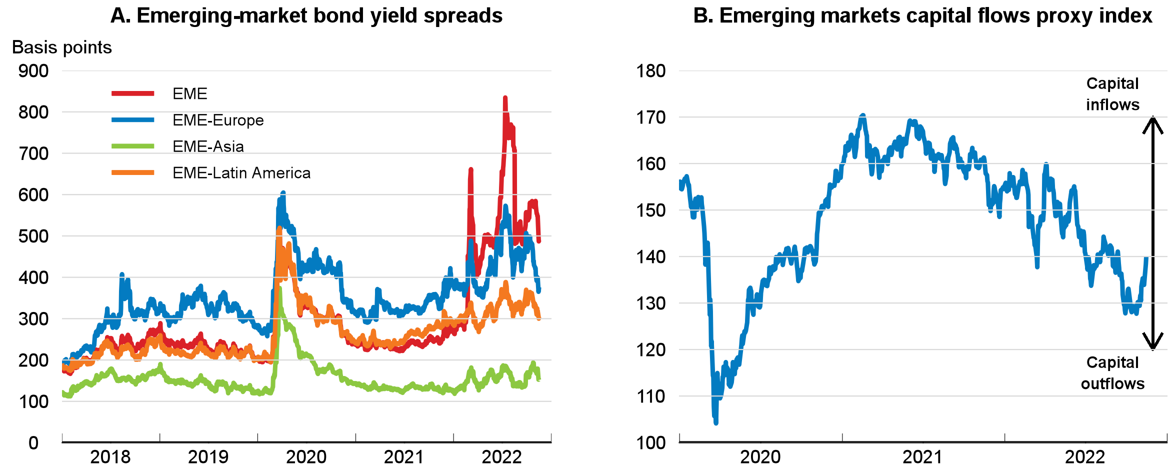
Tighter financing conditions, increased debt, the strong appreciation of the US dollar and the slowdown of export market growth exacerbate vulnerabilities in emerging-market economies. Risk premia have increased, capital outflows have accelerated, and international reserves have declined in many countries. In China, the resurgence of COVID-19 outbreaks or the contagion of financial fragilities in the highly indebted property sector to the rest of the economy could result in a sharper-than-expected slowdown in growth. Several emerging-market and developing economies also face food security risks from high food, energy and fertiliser prices, and supply shortages.

Adverse global economic conditions and elevated uncertainty continue to hamper investor confidence and heighten financial market volatility. Foreign-currency sovereign bond spreads have risen this year, especially in Eastern Europe and Latin America (Figure 1.24, Panel A), and capital outflows have intensified until recently (Figure 1.24, Panel B). Local-currency government bond and equity prices have also declined in Eastern European countries, reflecting geopolitical concerns. Cumulative portfolio outflows since February have been large in China, reflecting large debt outflows and price falls in equity markets. Portfolio outflows have also been sizeable in India, Indonesia and Türkiye, leading to a decline in international reserves in these countries. OECD estimates suggest that a 100 basis points rise in emerging-market economy investment risk premia could reduce output in these economies by around 0.5% in the following year (OECD, 2018).

Total indebtedness has remained higher than its pre-pandemic level in many emerging-market economies (Figure 1.25). Large currency depreciations against the US dollar in commodity-importing countries can add to the increases in debt-servicing burdens from higher global interest rates, especially where there are mismatches between the currency composition of liabilities and external revenues. Currency depreciations are also often associated with rises in foreign- and local-currency government bond spreads, especially in episodes of stress. In addition, depreciations can weigh on domestic demand if they prompt higher domestic interest rates or generate adverse balance sheet effects for foreign currency borrowers. This would offset the benefits of a lower effective exchange rate for trade, and might result in greater stress on the balance sheets of banks.[7]

[7] Recent IMF stress tests suggest that 29% of emerging-market economy banks could see significant capital shortfalls in the event of a severe downturn and a disorderly tightening of global financial conditions (IMF, 2022a).

Figure 1.24. Amidst high and volatile sovereign credit risk, capital outflows from emerging-market economies have risen



Note: Panel A shows the JP Morgan EMBI global bond spread, a measure of the sovereign risk spread of USD-denominated emerging-market economy government bonds over US government bonds. 'EME – Europe' covers Bulgaria, Romania and Türkiye. 'EME Asia' covers China, Indonesia, India, Malaysia, the Philippines, Thailand and Vietnam. 'EME - Latin America' covers Brazil, Chile, Colombia and Mexico. The 'EME' aggregate covers all mentioned countries plus South Africa and Ukraine. Panel B shows a daily composite index reflecting the performance of commodity, equity, foreign-currency-denominated government bond and currency asset classes. Increasing values of the index indicate capital flows into emerging-market economies, whilst decreasing values indicate capital outflows. At its source, the construction of the index sets the weight of the commodity asset class to 10% and those of the remaining asset classes to 30% each.
Source: Factset; Bloomberg; and OECD calculations.

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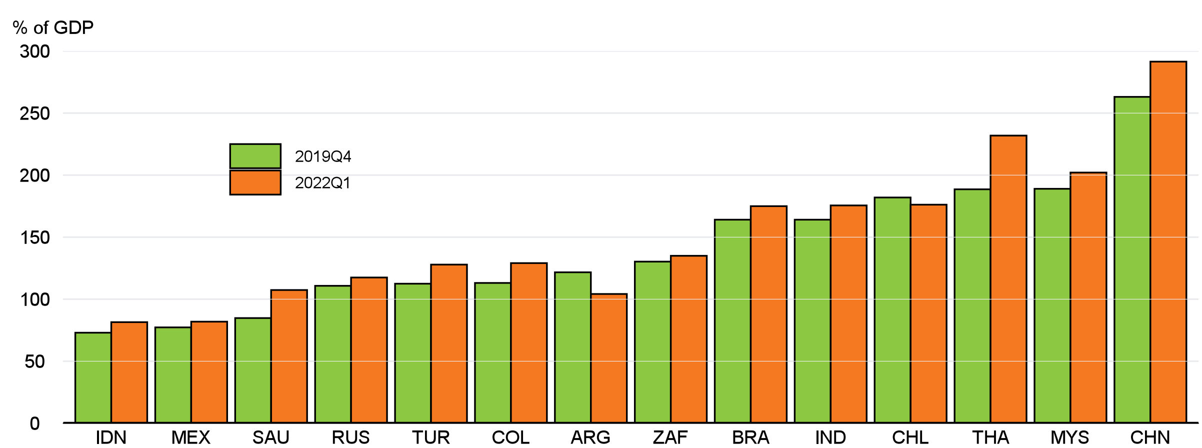
Figure 1.25. Indebtedness is high in many emerging-market economies



Note: Total debt refers to the sum of private non-financial sector debt (based on market values) and general government debt (based on nominal values).
Source: Bank for International Settlements; and OECD calculations.

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The recent appreciation of the US dollar has contributed to downgrades in the sovereign debt ratings of many emerging-market economies. Further dollar strength could add to financial vulnerabilities in these countries.[8] In Chile, Mexico and Türkiye, US dollar-denominated credit extended to non-bank borrowers is relatively high, potentially making domestic demand more vulnerable to currency depreciation (Figure 1.26, Panel A).[9] The import coverage of foreign currency reserves has also declined in many emerging-market economies, potentially reducing the resilience to external shocks (Figure 1.26, Panel B). There are also risks that larger external deficits and lower international reserves could pose challenges to macroeconomic and financial stability in countries like Chile, Colombia and Türkiye (Figure 1.26, Panel C). In contrast, current account balances have improved further or moved from deficit to surplus in some energy-exporting countries such as Saudi Arabia and Indonesia, which continue to benefit from a positive terms of trade shock.

Low-income developing countries also face rising food security and financial risks. High food and fertiliser prices and shortfalls in the supply of cereals from Russia and Ukraine significantly increase risks of hunger in many developing countries. The transmission of these shocks depends on the penetration of food imports in local supply chains, the pattern of fertiliser use in domestic agricultural production and the extent to which alternative food supplies are available (IFPRI, 2022). For instance, Russia and Ukraine account for about three-quarters of total wheat and wheat flour imports of many countries in the Middle East and North Africa (see Box 1.1 in OECD, 2022c; Rauschendorfer and Krivonos, 2022). Illustrative simulations indicate that the rise in the number of the undernourished could double to more than 200 000 in Egypt by 2023, across scenarios of moderate and severe declines in exports from Russia and Ukraine (Rauschendorfer and Krivonos, 2022).

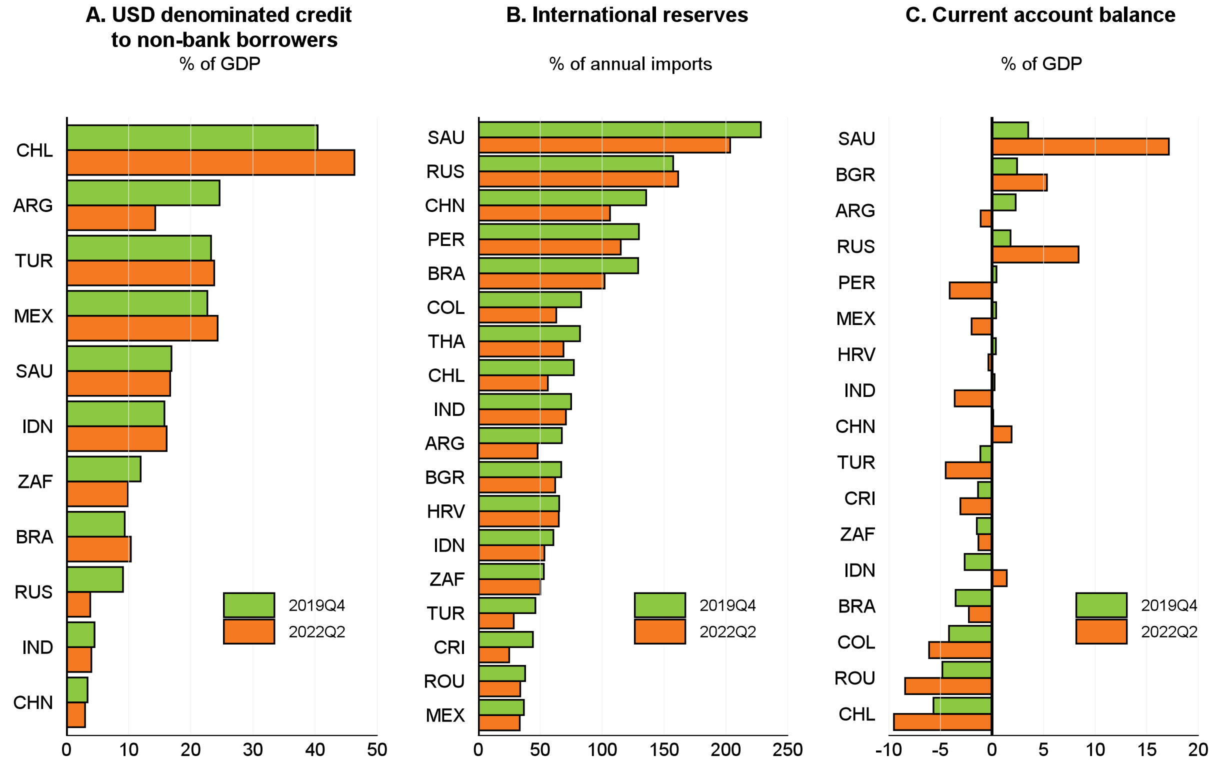
Financial conditions are also deteriorating in many developing economies. IMF debt sustainability analyses for 69 low-income countries suggest that, as of end-September and based on the most recently published data, 9 countries were in debt distress, 28 countries had a high risk of distress and a further 25 countries had a moderate risk of distress.[10] In addition, foreign-currency bond spreads in October exceeded 10 percentage points in 14 frontier developing economies, putting them in the distressed sovereign borrower category with a high risk of default (IMF, 2022a).

[8] Since May 2022, credit rating agencies have downgraded the sovereign debt ratings of Argentina, Chile, Ghana, Mexico, Nigeria, Pakistan and Türkiye. In August 2022, the IMF approved a Flexible Credit Line for Chile (an instrument which adds to precautionary external buffers in recipient countries with strong fundamentals and macroeconomic frameworks), reached an Extended Fund Facility agreement with Pakistan to shore up investor confidence and ease the pressure on the country’s declining international reserves and reached an Extended Credit Facility agreement with Zambia to help reinvigorate domestic inclusive growth plans while maintaining debt sustainability. In October 2022, the IMF deployed a Rapid Financing Instrument for Ukraine to address acute balance of payment difficulties.

[9] In the second quarter of 2022, the average US dollar-denominated non-bank borrower debt-to-GDP ratio in these three countries was 14 percentage points higher than during the “taper tantrum” episode of 2013.

[10] Corresponding to a situation where a country has started, or is about to start, a debt restructuring, or is accumulating arrears.

Figure 1.26. The appreciation of the US dollar could exacerbate financial vulnerabilities in emerging-market economies



Note: Panel A refers to cross-border and local claims denominated in US dollars. In Panels A and B, GDP and annual imports take the sum of the four quarters finishing in the quarter indicated. In Panel C, orange bars refer to data as of 2021Q4 for Russia.
Source: OECD Economic Outlook 112 database; Bank for International Settlements Global Liquidity Indicators database; IMF International Reserves and Foreign Currency Liquidity database; and OECD calculations.

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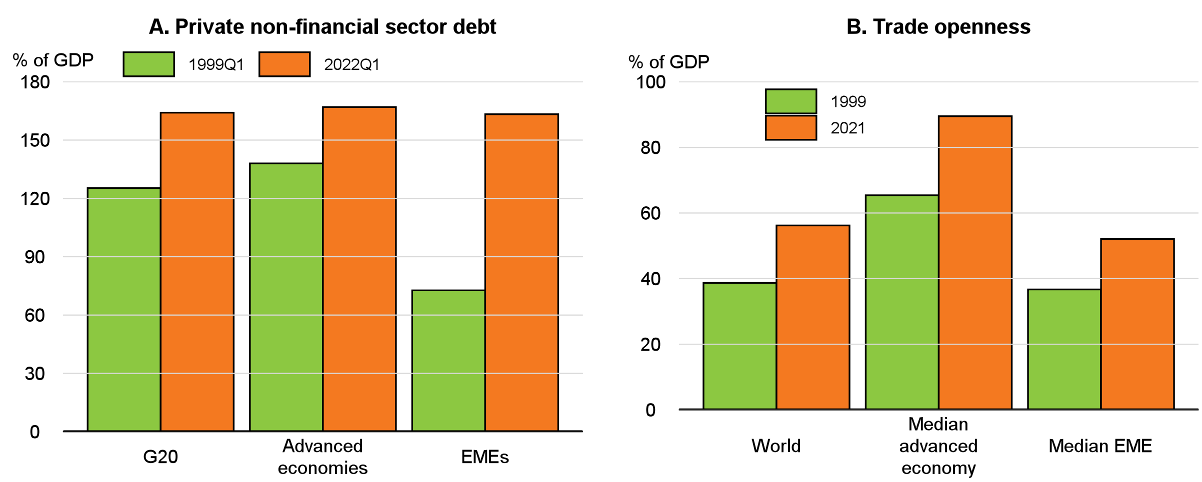
Calibrating monetary policy responses will be challenging

The calibration of monetary policy tightening is particularly challenging at present given uncertainty about the outlook, the balance of the different channels through which higher interest rates impact the economy, and the potential spillovers from tightening in other countries. This raises the risk that policy rates could be tightened more than strictly necessary, or for longer than necessary to bring down inflation, particularly given the exceptional synchronisation of monetary policy changes across economies at present. Concurrent tightening across countries can magnify the effects of domestic policy action, both by reducing foreign demand and by tightening domestic financial conditions, but also potentially change some channels of transmission, such as the exchange rate channel. Some studies for advanced economies suggest that the spillovers of monetary policy actions can be significant, potentially up to about half the size of the own-country effect (Curcuru et al., 2018). A failure to take these spillovers into account could lead to excessively tight monetary policy (Obstfeld, 2022).

Moreover, in many countries, especially advanced economies, it is two decades or more since a sustained tightening of monetary policy last occurred, raising the risk that the effects of higher interest rates could differ from those seen previously. Higher debt levels (Figure 1.27, Panel A), elevated asset prices, changes in the flexibility of product and labour markets, financial innovation and the increased importance of non-bank credit provision (FSB, 2021), and greater trade and financial openness (Figure 1.27, Panel B) may all increase the pace at which policy rate changes feed through. At the same time, higher interest rates also increase interest payments to savers, and some forms of debt, such as mortgages, are now more likely to be at fixed interest rates in some countries.

An illustrative scenario using the NiGEM macroeconomic model highlights some of the differences that might arise for individual countries when domestic monetary policy tightening is accompanied by similar moves to tighten policy in other economies.[11] The scenario considers the impact of a credible monetary policy commitment to lower price inflation sufficiently that the level of nominal GDP is eventually reduced by 5% relative to baseline. The impact from each advanced economy undertaking this policy independently, with policy responses in other countries limited to whatever is necessary given policy objectives and spillovers, is compared to the impact of all advanced economies implementing this policy change simultaneously.

Figure 1.27. The structure of many economies has changed considerably since the late 1990s



Note: Debt is given by total credit to the private non-financial sector from all sectors at market value. Trade openness is given by the ratio of imports plus exports of goods and services to GDP, measured in volumes, in US dollars at market exchange rates.
Source: Bank for International Settlements; OECD Economic Outlook 112 database; and OECD calculations.

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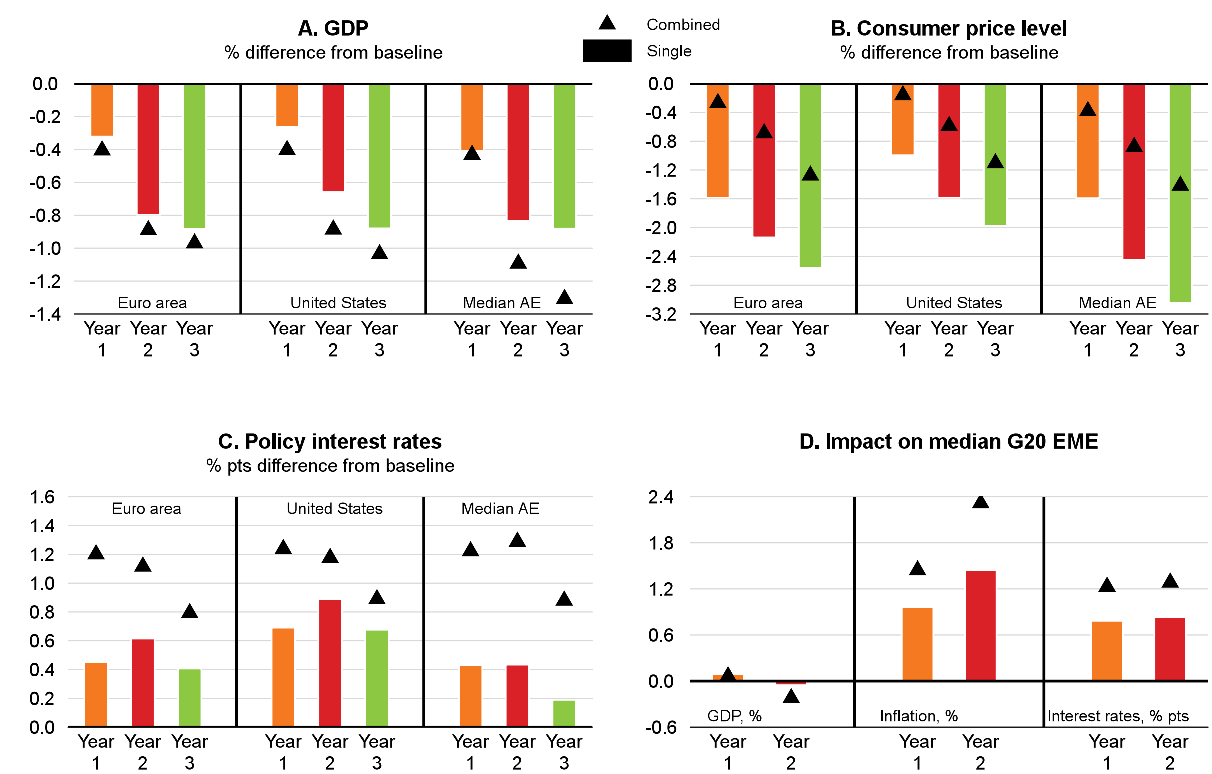
[11] The simulation incorporates monetary and fiscal policy reactions, based on the standard policy rules in NiGEM, unless otherwise stated. The monetary policy rule in NiGEM is a two-pillar rule, with policy interest rates responding to the deviation of inflation and nominal GDP from their target levels. The fiscal rule is that the effective direct tax rate on households adjusts so as to bring the general government budget balance back to its target level.

The results illustrate that the impact on output and inflation in each country from simultaneous moves to tighten policy by many countries may differ from the impact of actions in that country alone.

- Simultaneous action changes the trade-off between the growth and inflation impact of monetary policy tightening. By the second and third year of the shock, the negative impact on output is raised by around one-quarter in the median advanced economy when policy rates are raised in all advanced economies, pointing to the potential adverse impact on growth of widespread tightening in many economies (Figure 1.28, Panel A). In contrast, the impact on prices is reduced by around one-half (Figure 1.28, Panel B). The key reason for this is that the action by one country alone typically results in a sizeable exchange rate appreciation, helping to reduce price pressures. When all the major advanced countries act together, this channel is muted, although there is still some currency appreciation relative to emerging-market economies. As a result, stronger domestic policy interest rate rises in all countries are needed to bring down inflation (Figure 1.28, Panel C), as the main channels for monetary policy are domestic. In either case, the eventual longer-run impact of the policy adjustment is to lower the price level sufficiently to attain the lower nominal GDP target while leaving output close to baseline.[12]

Figure 1.28. The impact of tighter monetary policy varies when all countries act together



Note: Based on forward-looking simulations in which advanced economies set monetary policy so as to durably lower nominal GDP by 5% relative to baseline. "Single" denotes the impact when one central bank acts alone, "Combined" denotes the impact when all advanced economy central banks implement the shock at the same time. Year 1, Year 2 and Year 3 denote the first, second and third year impact of the policy change. Median AE denotes the median advanced economy.
Source: OECD calculations using the NiGEM macroeconomic model.

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[12] There are small negative effects on output from the cumulative impact of several years of weaker investment on the capital stock and potential output.

- In the combined shock, the additional rise in interest rates is greater in smaller, more open economies, where changes in exchange rates typically have the strongest impact on trade volumes and prices. As a result, the interest rate increases in each individual economy are similar to those in the United States, which is the country in which the exchange rate channel has the smallest direct impact.

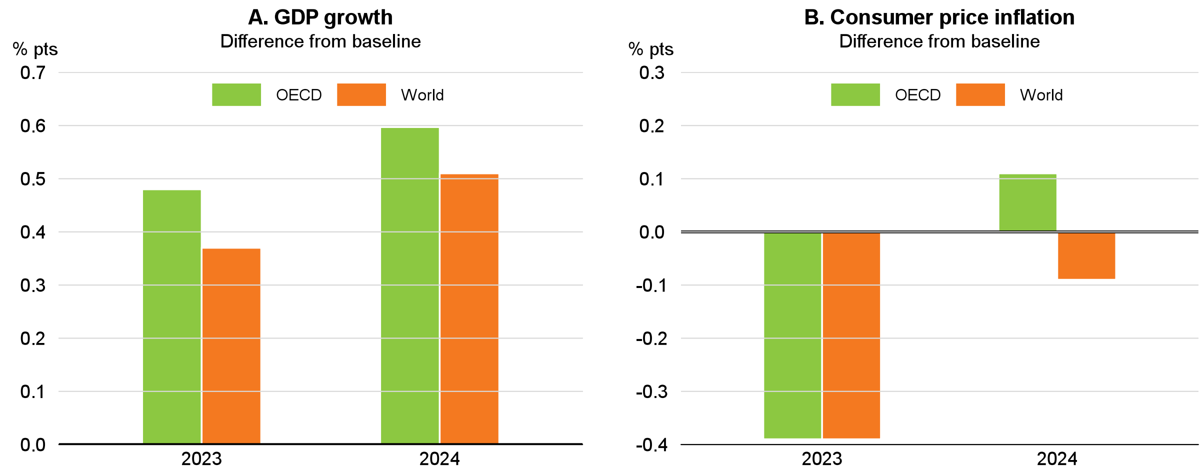
- There are adverse spillovers to emerging-market economies from policy tightening in the advanced economies, with stronger policy interest rate increases required in the typical economy to help ensure inflation returns to target in the combined shock. The emerging-market economies benefit from an initial exchange rate depreciation relative to the currencies of the advanced economies, but this pushes up inflation pressures and necessitates a domestic tightening of monetary policy. These factors are magnified when all the advanced economies tighten monetary policy simultaneously (Figure 1.28, Panel D).

Reduced uncertainty and lower commodity prices are upside risks

The baseline projections reflect the current high level of uncertainty about economic prospects, which is contributing to the tightening of global financial conditions and the weak outlook for business investment. Technical assumptions that commodity prices remain unchanged over the next two years also affect judgements about growth and inflation prospects. An easing of financial conditions due to reduced uncertainty and lower risk premia, or weaker commodity prices due to better-than-expected supply are amongst the possible near-term upside risks around the projections. Upside risks could also arise from an improvement in consumer confidence, with accumulated savings used to finance expenditure to a greater extent than projected, or if inflation responds more quickly to tighter monetary policy than expected. An early resolution of the war in Ukraine would increase the likelihood that these upside risks materialise.

An illustrative scenario, using the NiGEM global macroeconomic model, highlights the potential effects on growth and inflation of some of these factors. The scenario considers the impact of a reduction of 100 basis points in investment risk premia, which lowers the cost of capital, alongside a 10% fall in oil prices, which brings their level closer to that implied by futures markets in 2023-24, and a 5% reduction in global food prices. The latter would be helped by stronger and more stable supply in cereals markets, including the smooth operation of the Black Sea grain initiative. All shocks are assumed to last for two years before fading gradually. Taken together, they could boost global and OECD output growth relative to baseline by around 0.5 percentage points per annum on average in 2023 and 2024 (Figure 1.29, Panel A), helped by stronger investment. Inflation could initially decline by around 0.4 percentage points in 2023 (the first year of the shock) due to lower food and oil prices and remain close to baseline in 2024 (Figure 1.29, Panel B).

Figure 1.29. Reduced uncertainty and lower commodity prices would strengthen growth and ease inflation



Note: Illustrative scenario with a 100 basis points reduction in global investment risk premia, a 10% decline in global oil prices and a 5% decline in global food prices.
Source: OECD calculations using the NiGEM macroeconomic model.

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Policy requirements

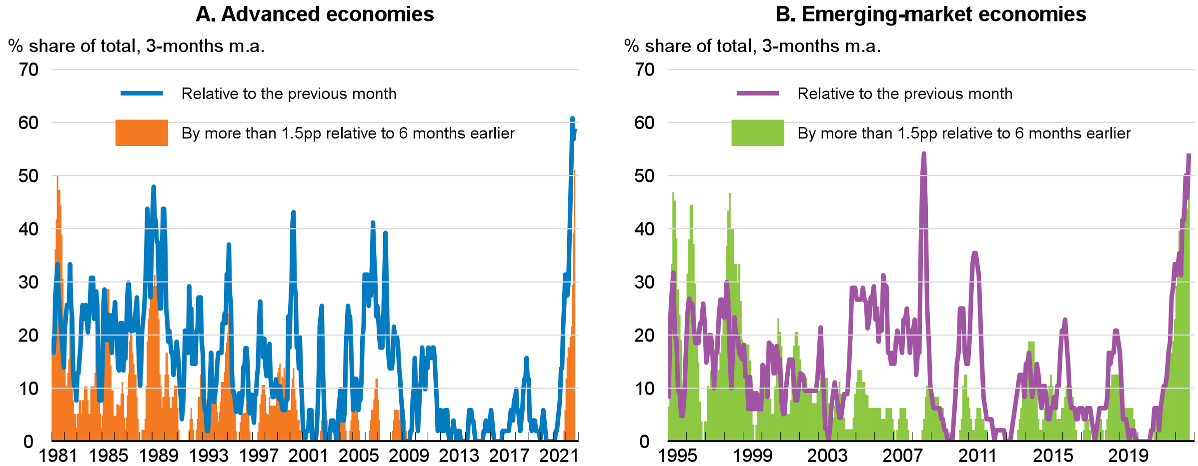
Slowing growth, persisting inflationary pressures and significant downside risks create difficult policy challenges. Continued efforts to lower inflation durably will require additional monetary policy tightening in most countries. Changes in interest rates will need to be carefully calibrated and data dependent, given uncertainty about the outlook and the impact of policy changes, and take account of potential spillovers from concurrent restrictive policy in other countries. Temporary fiscal measures are appropriately being used to cushion the immediate impact of higher food and energy costs for consumers and businesses, but these should be balanced against the need to lower energy consumption, limit further demand stimulus at a time of high inflation and ensure debt sustainability. Policy choices should also ensure that efforts to strengthen energy security do not hamper the need to hasten the green transition.

Further monetary policy tightening is necessary in most countries

In recent months, central banks in many economies have continued to tighten monetary policy in the face of fast rising and broadening price pressures. The pace of policy rate increases has been unusually widespread in both advanced and emerging-market economies (Figure 1.30). Policy rates have been raised by more than 1.5 percentage points in more than half of the advanced economies and more than 40% of emerging-market economies in the past 6 months. Even so, real short-term policy interest rates remain negative, or just above zero, in several jurisdictions. Broadening price pressures throughout the economy have led to more forceful policy rate rises than suggested by earlier forward guidance to minimise the risks of high inflation becoming entrenched in inflation expectations and feeding through into cost pressures in tight labour markets. Delaying action would have heightened the risk of even more forceful measures eventually being required to bring down inflation.

Figure 1.30. Monetary policy tightening has been fast and highly synchronised

Countries raising policy rates



Note: The sample consists of 35 advanced economies and 16 emerging-market economies. All members of the OECD except Costa Rica are included in the sample. The sample composition changes over time according to data availability. Euro area countries are counted separately before 1999 and as one from 1999 onward.
Source: Bank for International Settlements; and OECD calculations.

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Financial conditions are also being tightened in a number of countries due to ongoing reductions in central bank balance sheets, either by not (or not fully) reinvesting the proceeds of maturing bonds (passive quantitative tightening, QT) or by selling securities (active QT). In contrast to policy rate decisions, the pace of balance sheet reduction is varying substantially across countries, but following a pre-announced path (Box 1.3).

- In the United States, four consecutive policy rate increases of 75 basis points since June have pushed the target range for the federal funds rate to its highest level since 2008. The monthly pace of balance sheet reduction has also accelerated since September.[13]
- The ECB ended net asset purchases at the start of July and began increasing policy rates later that month, with the interest rate on main refinancing operations reaching 2% from in November. In July, the ECB also introduced a new tool, the Transmission Protection Instrument (TPI), aimed at preventing financial fragmentation in the euro area unwarranted by fundamentals. Activation of the TPI will enable the ECB to purchase sovereign bonds of countries with fiscal and macroeconomic policies deemed sound and sustainable.
- The Bank of England, the Bank of Canada and the Reserve Bank of Australia have all delivered significant further policy rate increases since June 2022. The latter two central banks have continued to pursue passive QT. After engaging in temporary and targeted bond purchases to calm financial market turbulence in early October, the Bank of England started active QT in November 2022, with the aim of reducing government bond holdings by GBP 80 billion by September 2023.

[13] To up to USD 60 billion for Treasury securities and USD 35 billion for agency debt and mortgage-backed securities.

- All other OECD advanced economies have also increased policy rates since early June 2022. Policy rates remain very high in the Czech Republic, Hungary and Poland, which continue to face very strong inflation pressures. In contrast, Korea and Norway, which also started to tighten policy at an early stage, have raised policy rates in a more gradual way amidst milder inflation. In addition to rate increases, central banks have stepped up passive QT in Sweden and started government bond sales in New Zealand.

Faced with high uncertainty about the path of the economy and the persistence of inflation, central banks have generally shifted to a more data-dependent stance. Calibrating the scale and timing of the monetary policy changes required to steer inflation back to target remains challenging given difficulties in assessing the rate above which monetary policy becomes restrictive, the concurrent policy actions being undertaken in other countries and the speed at which tightening should occur. Clear communication about the policy stance, the key factors behind policy decisions and the expected pace of balance sheet reductions is crucial to minimise financial market disruptions.

To bring inflation back to target in a lasting manner, policy interest rates will need to rise above neutral levels for a period. However, neutral rates – a real interest rate at which the policy stance is neither accommodative or restrictive – are a long-run concept, unobserved, difficult to estimate, and may vary over time due to changes in the underlying factors driving saving and investment decisions. This uncertainty suggests that estimates of neutral rates may offer limited guidance for current policy decisions and would prove difficult to explain in central bank communications. Nonetheless, they remain an important benchmark for the appropriate level of policy rates in the medium term.

In the near term, several quarters of positive real interest rates and below-trend growth will likely be needed to lower resource pressures durably and achieve sustained disinflation, particularly where demand pressures are an important source of inflation (Box 1.1). With 2-3 year ahead household inflation expectations in many major advanced economies currently at 3% or more (Figure 1.7), policy interest rates may need to be raised quickly above this level where this has not already been done.[14] The differential between domestic and US policy rates is also becoming a consideration in some economies in which price pressures are being pushed up in part due to recent sizeable bilateral currency depreciations against the US dollar.

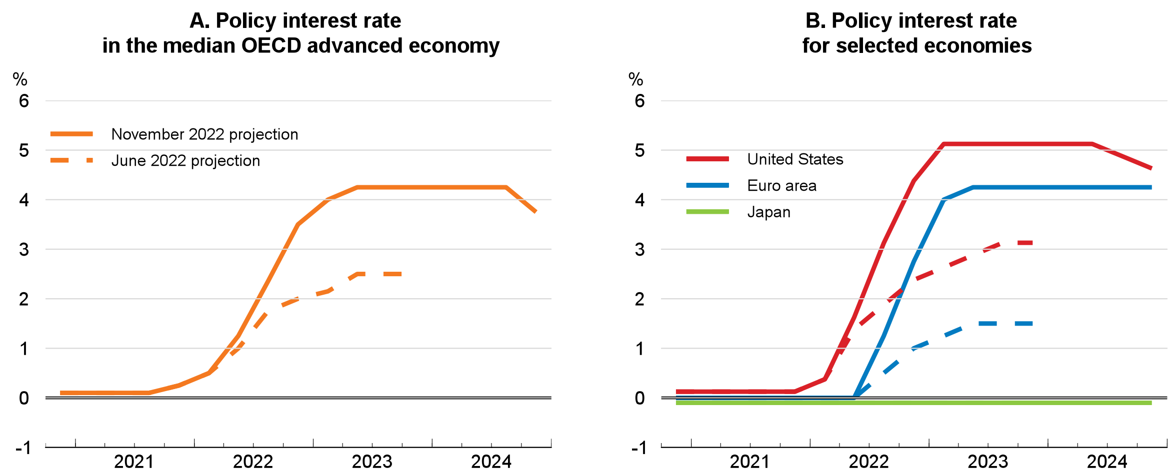
Interest rates are projected to increase further in the near future and then remain unchanged for several quarters in most countries (Figure 1.31). Further tightening is particularly likely in economies where there are signs that medium-term inflation expectations are still higher than before inflation started to rise and market-based real long-term interest rates are still close to zero (Figure 1.14). Once inflation eases and converges towards central bank targets, policy rates may start to decrease in 2024 in some jurisdictions.

- In the United States, where considerable policy tightening has already occurred, the federal funds rate is projected to peak at 5-5¼ per cent from early 2023. Two modest rate reductions are projected in 2024, as core inflation declines towards 2%. Steady quantitative tightening is expected to continue, with long-term interest rates on government bonds projected to average around 5% in 2023-24.

[14] Real long-term government bond yields have risen by 2 percentage points or more in many countries this year, suggesting that recent policy rate increases are already having some impact in financial markets, but they generally remain low and beneath the rates observed prior to the global financial crisis (Figure 1.14).

- In the euro area, significant further tightening is expected, with the main refinancing rate reaching 4¼ per cent by the second quarter of 2023 and remaining at that level until end-2024. Maturing securities are expected to be fully reinvested over the projection horizon, with use being made of all margins of flexibility when reinvesting the proceeds of maturing bonds on the ECB balance sheet to limit financial fragmentation in the euro area.
- The Bank of Japan is projected to maintain an accommodative stance, with no policy rate increases until end-2024. However, with quarterly core inflation expected to reach 2% by the second half of 2024, the projections assume that the yield curve control framework will start to be eased slightly at that stage by allowing a steeper yield curve.
- The Bank of England is projected to increase its policy rate to 4½ per cent by mid-2023 and to keep it at that level throughout the rest of the projection period, with quantitative tightening taking place from November 2022. The Bank of Canada is projected to raise its policy rate to 4¼ per cent by the end of 2022, with some gradual easing expected in 2024 as inflation declines to within the target band.
- Further policy rate increases, sometimes sizeable, are projected in all remaining OECD advanced economies. In central European countries, large subsequent rate decreases are expected once very high inflation subsides. In economies where policy rates are projected to peak at much lower levels, such as Sweden and Switzerland, no rate changes are expected before the end of 2024.

Figure 1.31. Monetary policy tightening is projected to continue in the coming quarters



Note: Solid lines refer to the OECD November 2022 projections and dashed lines refer to the OECD June 2022 projections. In Panel A, advanced economies include Australia, Canada, the Czech Republic, Denmark, the euro area, Hungary, Iceland, Israel, Japan, Korea, New Zealand, Norway, Poland, Sweden, Switzerland, the United Kingdom, and the United States.
Source: OECD Economic Outlook 112 database; OECD Economic Outlook 111 database; and OECD calculations.

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Box 1.3. Projections of the pace of quantitative tightening

Some central banks have reduced the amount of bond holdings on their balance sheets by either not (or not fully) reinvesting the proceeds of maturing bonds (passive quantitative tightening, QT) or by selling securities (active QT). The projected adjustment in balance sheets over the next two years differs across jurisdictions, based on announced policy decisions and the maturity structure of bond holdings, but will generally leave holdings of securities at a higher level than before the pandemic (Figure 1.32).

- In the United States, it is assumed that the monthly caps for balance sheet reduction announced by the Federal Reserve (USD 60 billion for Treasury securities and USD 35 billion for agency debt and mortgage-backed securities), implemented through passive QT with partial reinvestment, are strictly observed.
- In the United Kingdom, the Bank of England is assumed to pursue both passive QT with zero reinvestment and active QT from 1 November, leading to a reduction in government bond holdings of GBP 80 billion over the twelve months from September 2022, as announced. In the remainder of the projection period, passive QT with zero reinvestment is assumed.
- In Canada and in Australia, central banks are assumed to pursue passive QT with zero reinvestment until end-2024. Information on maturing holdings is used in the projections.
- The Reserve Bank of New Zealand is assumed to pursue passive QT with zero reinvestment in tandem, as announced, with sales of government bonds and inflation-indexed government bonds at a rate of NZD 5 billion per fiscal year beginning from July 2022.
- In Sweden, as announced by the Sveriges Riksbank in September 2022, passive QT with partial reinvestment of SEK 18.5 billion is assumed during the second half of 2022, and asset purchases are expected to cease at end-2022, implying passive QT with zero reinvestment in 2023-24.

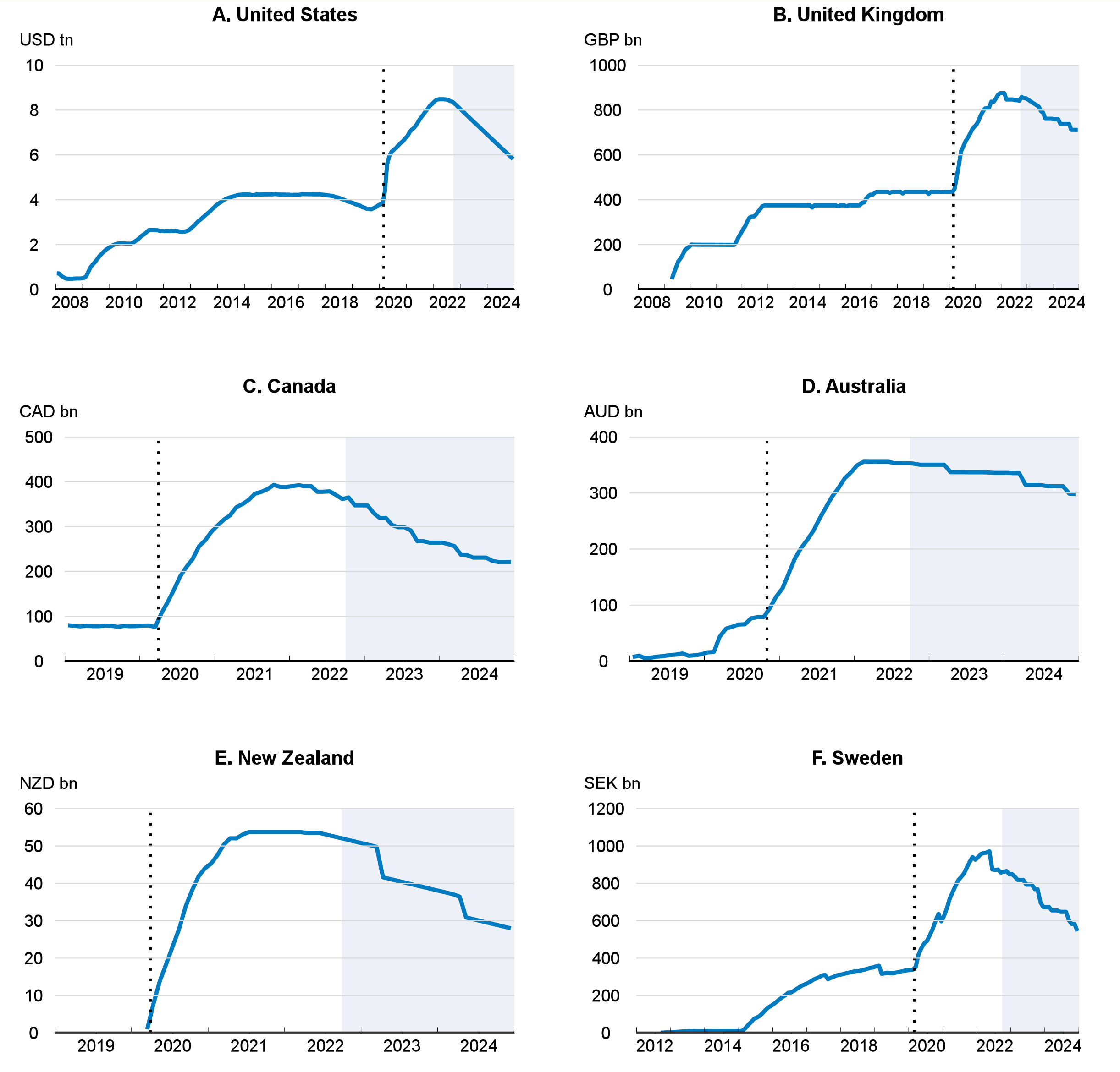
Japan and the euro area have not yet announced plans for balance sheet reduction.

As quantitative easing (QE) has contributed to lower long-term interest rates, QT is likely to increase them. But estimating the possible impact is difficult, given the different circumstances in which the policies are being implemented and the various channels through which the policies operate. Like QE, QT will operate through different channels, whose absolute and relative importance depends on specific circumstances (Bank of England, 2022b). Changes in asset holdings may affect expectations about the path of future policy rates (signalling effects). For instance, QE episodes have likely reduced rate expectations by signalling a commitment to low policy rates for a longer period. Asset purchases or sales may also affect different components of the risk premium on long-term yields, such as by changing the average maturity and the duration risk of private portfolios (portfolio balance effects), impacting liquidity conditions, or mitigating market stress.

The evidence base for QT is even narrower than for QE, and (with the exception of the ongoing QT episodes documented above) essentially limited to the US experience in 2017-19. Over the length of this episode, the average impact of QT on the 10-year Treasury yield has been estimated at about 8 basis points (Smith and Valcarel, 2020).

The estimated effects on long-term yields of QE programmes could also help gauge the likely order of magnitude of QT impacts. As a rule of thumb, bond purchases of 1% of GDP have been found to reduce long-term yields by about 5 to 10 basis points on average (Gagnon, 2016; Finlay et al., 2021; Bank of England, 2022b; Crawley et al., 2022), with impacts tending to be stronger at times of market stress. Applying this simple rule to the amounts of QT projected in Figure 1.32 (from the start of bond holdings reduction in each country to end-2024) would tentatively suggest impacts on long-term interest rates ranging from 15-30 basis points in Australia to a potential range of between ½ and 1 percentage point in the United States.

Figure 1.32. Projections of central bank balance sheet reduction



Note: The charts show: the sum of securities (at face value) held outright in the System Open Market Account (SOMA) of US Treasury debt, federal agency debt, and mortgage-backed securities for the United States; the total gilt purchase proceeds by the Asset Purchase Facility for the United Kingdom; the government of Canada securities holdings (at par value) not on repo for Canada; the sum (at face value) of Australian government securities and semis holdings for Australia; the sum (nominal amount) of New Zealand Government Bond (NZGB) and Local Government Funding Agency (LGFA) holdings under the Large Scale Asset Purchase Programme for New Zealand; the sum (nominal amount) of government securities, covered bonds, municipal bonds, corporate bonds, and commercial paper for Sweden. Other aspects of central bank balance sheets are not included. A vertical dotted line indicates when the central bank started quantitative easing programmes in response to the COVID-19 shock. Sweden, the United Kingdom and the United States had earlier QE episodes. For the United Kingdom, it is assumed that active QT falls on bonds maturing beyond 2024. For Australia, it is assumed that the proceeds of maturing bonds purchased before the start of the QE programme (Bond Purchase Programme) in November 2020 are not reinvested. For New Zealand, it is assumed that the sale of NZD 5 billion of bonds per fiscal year takes place at a constant monthly pace and consists of securities maturing beyond 2024. For Sweden, bonds purchased in the second half of 2022 are assumed to mature beyond 2024.

Source: Board of Governors of the Federal Reserve System; Office for National Statistics; Bank of Canada; Reserve Bank of Australia; Reserve Bank of New Zealand; Sveriges Riksbank; and OECD calculations.

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However, the impacts of QT and QE on longer-term interest rates could turn out to be asymmetric. With policy rates clearly above zero and balance sheet size being reduced gradually and predictably, signalling effects could be (much) smaller in QT than for QE, which was implemented when policy rates were close to their effective lower bound (Bullard, 2019; Lane, 2022). On the other hand, liquidity effects from QT could prove stronger, leading to a substantial increase in liquidity premia. For instance, possible asymmetries between the impact of QE and QT on liquidity claims on banks could make the latter more sensitive to liquidity shocks when QT is underway (Acharya et al., 2022).

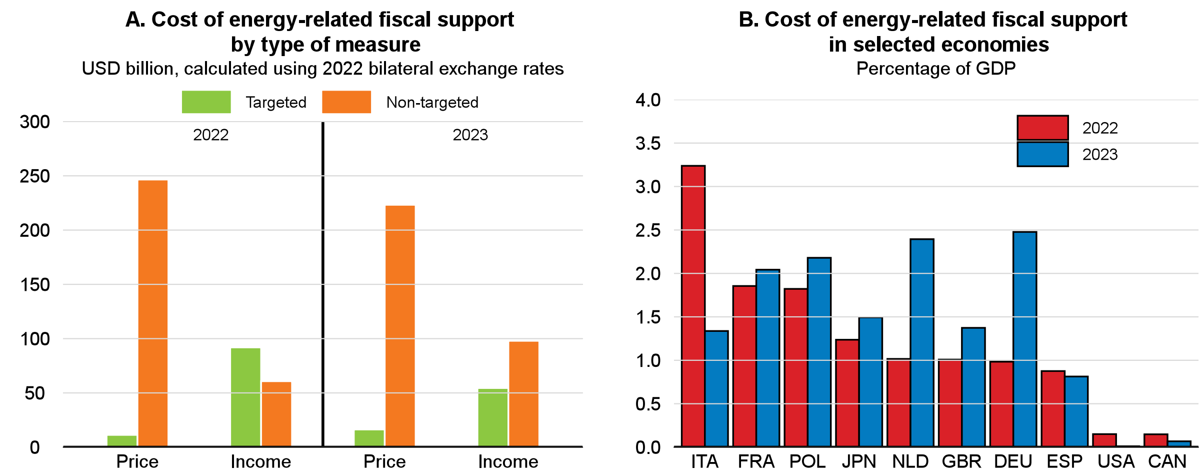
Targeted fiscal policy support is needed

The second half of 2022 has witnessed a further increase in fiscal support measures in many advanced economies to shield households and companies from the impact of elevated energy prices. Especially in Europe, where energy prices have risen the most, many governments have announced new policy packages or extended existing ones, with budget costs approaching or exceeding 2% of GDP in some large economies (Figure 1.33). The overall euro area fiscal stance in 2022 has nonetheless become somewhat less supportive, with the underlying primary balance increasing by an estimated 0.4% of potential GDP (Figure 1.34). This reflects the offsetting impacts of the withdrawal of pandemic-related support and higher-than-expected tax revenues due to higher inflation. In contrast, the United States, Canada and Australia, where energy-related support measures have been much smaller, appear likely to have seen much stronger fiscal consolidation this year.

Fiscal projections for 2023-24 are conditional on announced government measures and OECD assessments of current plans (Annex 1.A.). With energy prices projected to remain high, energy support measures are assumed to continue into 2023 in many countries, and sometimes 2024, in the projections. However, in most cases this involves some changes in design, with some support measures either being phased out completely or becoming less extensive. In the median OECD economy, moderate fiscal consolidation is projected for both years, with the underlying primary balance improving by 0.4% of potential GDP in 2023 and by 0.6% in 2024 (Figure 1.34). Relative to expectations in mid-2022 (OECD, 2022c), the pace of consolidation in OECD economies in 2023 is expected to become both smaller in overall terms and more variable across countries:

- In the United States, the underlying primary balance is projected to improve by more than 2% of potential GDP in 2023-24. This will largely stem from pandemic-related expenditures fully expiring and the withdrawal of energy-related fiscal support at the state level.
- In the euro area, the fiscal stance is projected to remain mildly restrictive. In 2023, the fiscal savings from the full termination of pandemic-related support, which was still in force in several countries in early 2022, more than outweigh in aggregate terms the further expansion of measures to offset energy costs. In some countries, sizeable fiscal stimulus is also projected to stem from increased expenditure on defence and an acceleration, after some initial delays, in the implementation of Next Generation EU plans. In 2024, the main driver of the moderate projected consolidation is the gradual phasing-out of energy support.
- In Japan, the fiscal projections reflect the temporary measures to support vulnerable households and businesses announced in late September and the new economic policy package to support longer-term growth announced in late October. The fiscal stance is expected to be neutral in 2023, when the new support measures and the expiration of the previous COVID-19-related stimulus roughly cancel out. Consolidation of over 1% of potential GDP is projected in 2024, as measures for moderating energy and food prices gradually decline.

Figure 1.33. Planned support to energy consumers is costly and largely non-targeted



Note: Based on data collected up to November 17. Support measures are taken in gross terms, i.e., not accounting for the effect of possible accompanying energy-related revenue-increasing measures, such as windfall profit taxes on energy companies. Where government plans have been announced but not legislated, they are incorporated if it is deemed clear that they will be implemented in a shape close to that announced. Loans, guarantees, and capital transfers that do not immediately change general government net lending have been excluded. When a given measure spans more than one year, its total fiscal costs are assumed to be uniformly spread across months. Measures with no defined end-date are assumed to stay in place until at least December 2023, unless an earlier withdrawal is assumed in the macroeconomic projections of this *Economic Outlook* for the respective country. Panel A covers 40 economies, of which 34 are OECD economies (all members except Iceland, Lithuania, Switzerland and Türkiye) and 6 non-OECD economies (Brazil, Bulgaria, Croatia, India, Romania and South Africa). Measures classified as income support are those that provide lump-sum transfers to energy consumers to help alleviate energy cost increases. Price support includes all measures that reduce the post-tax energy price. Support classified as targeted is provided to specific groups, such as vulnerable households or businesses. Non-targeted support applies to all consumers with no eligibility conditions. For Canada, Germany, Italy, Japan, the Netherlands, Poland and Spain, it has been assumed that some existing measures will be extended into 2023 even though that extension has not been announced yet.
Source: OECD calculations based on the OECD Energy Support Measures Tracker and the OECD Economic Outlook 112 database.

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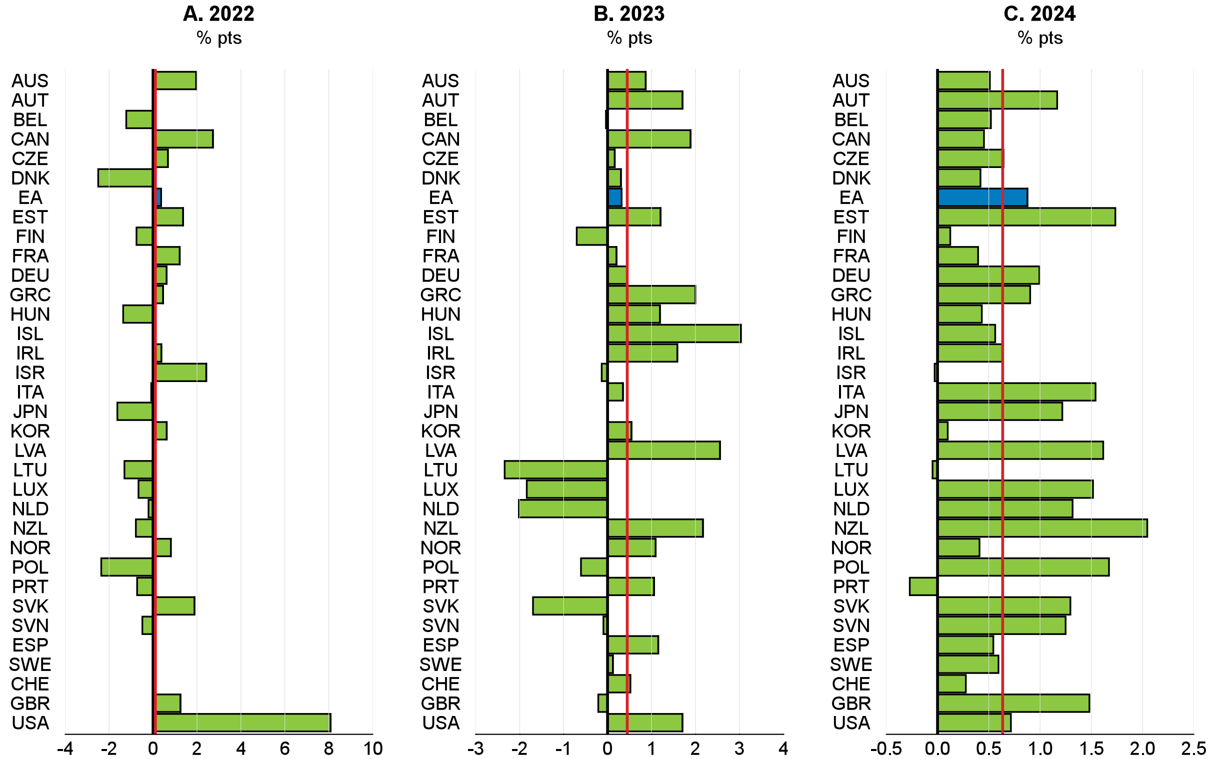
- In most remaining advanced economies, including Australia, Canada, Korea and the United Kingdom, the underlying primary balance is projected to increase over 2023-24. Among smaller countries, Latvia and New Zealand stand out for their strongly-restrictive stance, called for by the need to curb very high inflation in the former and required by the objective to reach a small surplus by 2025 in the latter. In contrast, after strong budget consolidation in 2021-22, no fiscal tightening is projected in Israel over 2023-24.

Energy support measures need to be well-targeted, preserve incentives for energy savings and not outlast the period of exceptional price pressures. Price caps and reduced energy taxes on energy, though simpler and faster to implement and thus often an understandable first line of defence, entail high budget costs and a number of other drawbacks, especially in the likely scenario of energy remaining expensive for an extended period. Careful design is needed to ensure price support does not weaken incentives to reduce energy consumption or hamper reallocation by preserving energy-intensive activities that are not sustainable in the medium term. Setting a consumption threshold beyond which market prices apply could preserve incentives to save energy, provided the threshold is not set at an excessively high level (for instance, it should in general be smaller than average consumption). In addition, whilst reducing inflationary pressures in the short run, price support measures may rekindle those pressures further ahead if the measures are eventually phased out and market prices remain high. Untargeted support to cushion living standards should also not involve a persistent stimulus to demand at a time of high inflation, requiring monetary policy to be tighter for longer than otherwise.

Figure 1.34. Fiscal consolidation is projected to be moderate and uneven across countries

Change in the underlying primary balance, in per cent of potential GDP



Note: Vertical lines indicate the medians for the available OECD economies.
Source: OECD Economic Outlook 112 database; and OECD calculations.

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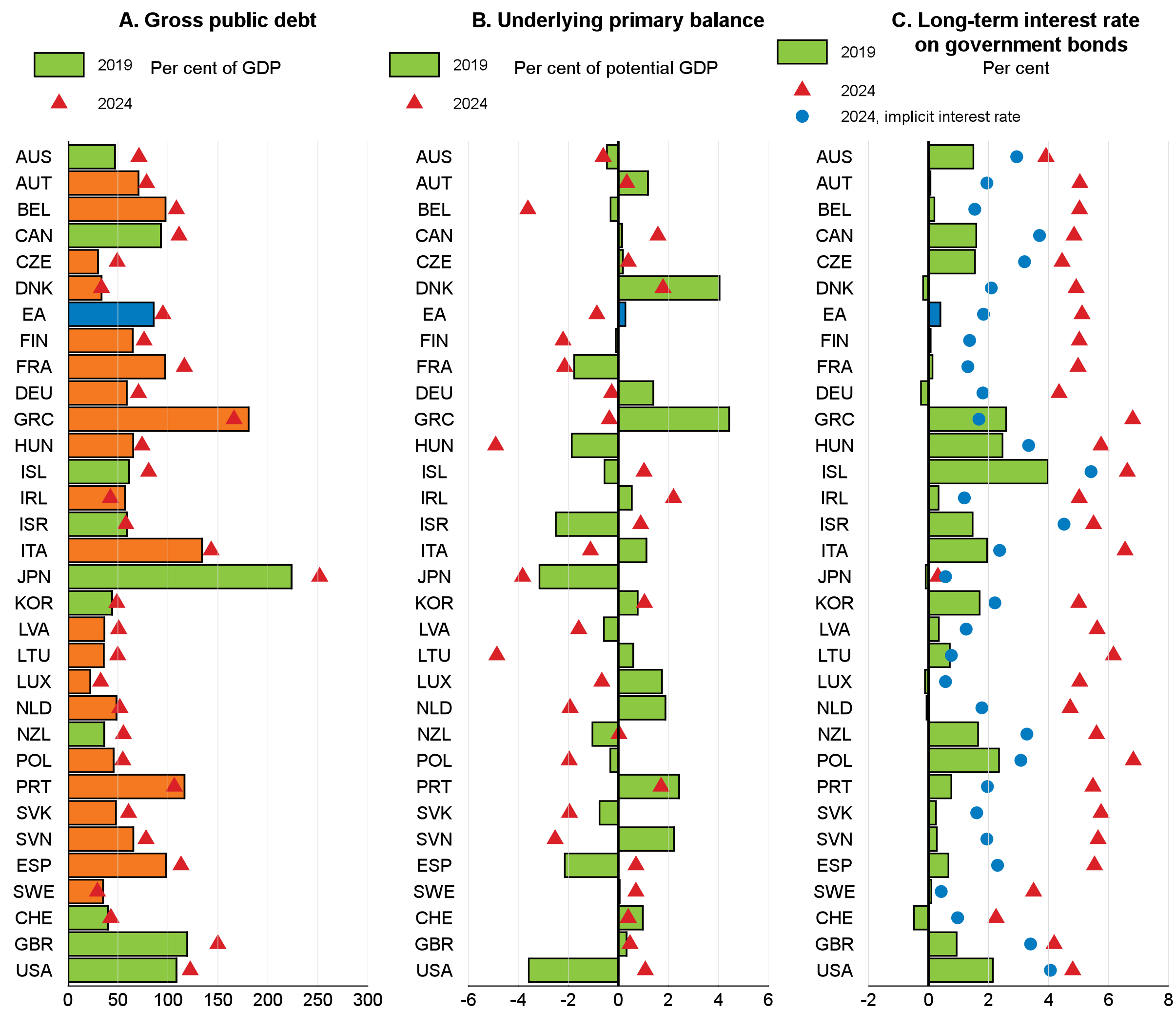
Effective targeting is important both when providing support to households and to firms. Even in countries where social benefit systems are well developed, protecting vulnerable households while high energy prices persist may require moving beyond standard means-testing and resorting, data availability and timeliness permitting, to other targeting criteria such as housing location and quality, household composition and access to public transport (OECD, 2022e). Support to firms should focus on companies that were solvent before the energy price shock and be time-limited, to sharpen firms' incentives to adapt to a possible context of persistently more expensive energy. The usual considerations of transparency, proportionality and non-discrimination in state aid also apply (OECD, 2020).

Ensuring the sustainability of the public finances has become more challenging due to the multiple impacts of the pandemic, the war and energy shocks. Even though inflation will make nominal GDP grow faster, debt-to-GDP ratios in 2023 and 2024 are generally projected to be considerably higher than in 2019, and sometimes still on an upward trend (Figure 1.35). In most OECD economies, and particularly in Europe, underlying primary balances in 2024 are estimated to be more expansionary than before the pandemic, often by a sizeable margin. To a large extent, this is due to the prevalence of costly non-targeted energy price support, such as price caps or lower indirect tax rates. And the outlook for debt service costs has deteriorated substantially, with long-term interest rates generally projected to rise far above the implicit interest rate on public debt – interest paid as a percentage of the nominal debt stock – placing upward pressure on the latter. In the median OECD advanced economy, the implicit interest rate on public debt in 2024 is projected to still remain largely unchanged relative to 2019 levels (at 1.9%), but 10-year yields are estimated to rise seven-fold (from 0.7 to 5.0%), pointing to more costly debt finance in the future.

Figure 1.35. Public debt has increased and the cost of new debt is rising



Note: Orange bars correspond to EU countries for which Maastricht debt is used. The implicit interest rate is defined as general government interest payments divided by general government gross financial liabilities at the end of the preceding year.
Source: OECD Economic Outlook 112 database; and OECD calculations.

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Achieving sustained fiscal consolidation while responding to new budget priorities, such as larger investments in defence or in carbon neutrality, will require either further increases in tax burdens or reprioritising public expenditure and making it more efficient. On both reprioritisation and efficiency grounds, fostering credible medium-term fiscal frameworks, where an expenditure rule targeting a wide spending aggregate is a likely key element, will be of value. Such frameworks would also help to provide clear guidance about the medium-term trajectory of the public finances and mitigate concerns about debt sustainability (Rawdanowicz et al., 2021).

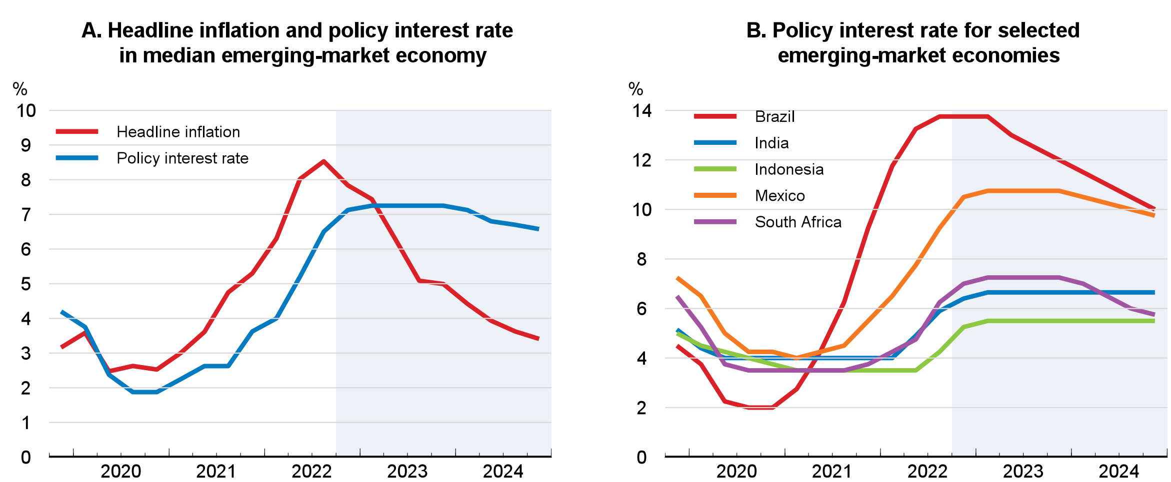
In addition, the operation of fiscal frameworks and their democratic accountability greatly benefit from a transparent and non-fragmented recording of public spending and revenue. Some governments have recently been resorting to off-budget vehicles to fund expenditure increases in areas like defence or energy support. When such spending is carried out by entities statistically classified within general government, it will be reflected in national accounts budget balances (though perhaps not in public accounts ones). When those entities are outside general government, their spending will still weigh on the deficit or debt of the general government if financial support from the latter is eventually needed, such as calls on a debt guarantee granted by the state. In either case, off-budget vehicles detract from transparency, and their use should in general be reduced.

Inflationary pressures and stretched budgets limit the scope for policy support in emerging-market economies

Tighter global financial conditions, persisting inflation pressures and rising debt levels limit the room for policy manoeuvre in the emerging-market economies, especially ones with high levels of foreign currency debt or fiscal deficits considerably above pre-pandemic levels. Central banks in the major emerging-market economies have continued to tighten policy in the second half of 2022 in response to surging headline inflation. Policy interest rates are generally projected to become higher than headline inflation rates in 2023 (Figure 1.36, Panel A), with headline inflation staying above the inflation target range of central banks. In 2024, greater scope is likely to exist to lower policy rates, particularly in economies where the disinflationary effects of monetary policy tightening are projected to become increasingly apparent (Figure 1.36, Panel B). However, the differential between domestic and US policy rates may remain an important policy consideration, limiting the pace of monetary policy easing in the emerging-market economies.

A tight policy stance is needed to prevent a de-anchoring of inflation expectations amidst heightened energy and food prices. Currency depreciation has often made disinflation harder, prompting monetary authorities to raise policy rates further and also, in some cases, intervene in the foreign exchange market to prop up the value of the currency. Monetary policy should remain cautious, especially where sizeable currency depreciation led by capital outflows could harm domestic borrowers that hold unhedged foreign-currency debt (Mimir and Sunel, 2019), and policy rate reductions before inflation durably converges towards the central bank target should be avoided.

Figure 1.36. Policy interest rates are expected to remain high in the near term in emerging-market economies to help reduce inflation



Note: In Panel A, the sample covers Brazil, Chile, China, Colombia, Costa Rica, India, Indonesia, Mexico, Peru, Romania, Saudi Arabia and South Africa.
Source: OECD Economic Outlook 112 database; and OECD calculations.

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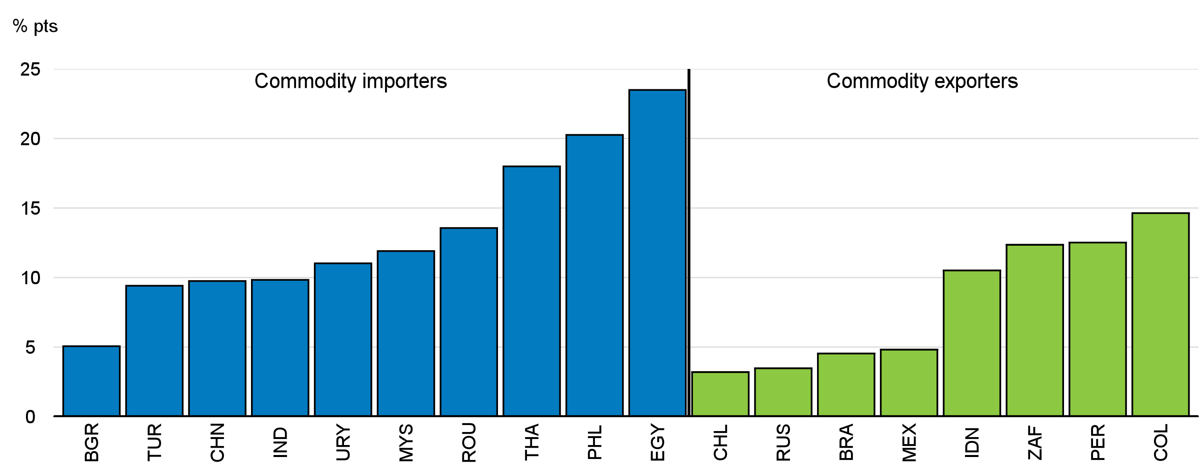
The evolution of policy rates is expected to vary across major emerging-market economies. In Latin America, policy rates are projected to gradually decline over 2023-24 in Brazil, where frontloaded monetary policy tightening is expected to substantially slow down inflation. In contrast, policy rates in Mexico are not projected to start declining before 2024. In China, following a series of interest rate and reserve requirement reductions, no further policy rate adjustment is projected in 2023-24, though further measures to stabilise the currency could be deployed. Inflation pressures also remain relatively subdued in India and Indonesia, allowing policy rates to increase moderately in these economies until early next year and then stabilise. In South Africa, policy rates are projected to increase until early 2023 and start declining in 2024, as inflation converges to the mid-point of the central bank's inflation target range.

The economic recovery from the pandemic and high inflation rates have lifted fiscal revenues in many emerging-market economies. Nonetheless, public debt is typically above pre-pandemic levels, though often with smaller increases in commodity exporters, which have generally benefitted from improved terms of trade, better fiscal outcomes and stronger growth (Figure 1.37). The expiry of pandemic-related support is easing spending pressures in many countries, but additional expenditure to protect vulnerable citizens from high energy prices and address food security risks has limited fiscal consolidation. Sustainable public finances remain essential to maintain investor confidence and limit increases in sovereign spreads.

Figure 1.37. Public debt has risen less in commodity-exporting emerging-market economies

Change in general government gross debt-to-GDP ratio, from 2019Q4 to 2021Q4



Note: General government gross debt, excluding intergovernmental holdings.
Source: IMF Sovereign Debt Investor Base for Emerging Markets database.

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Credible fiscal frameworks are needed to provide clarity about the medium-term path towards public debt sustainability. For example, adhering to government debt targets in Colombia and Chile will help ensure that current measures to shield consumers from high food and energy prices remain temporary and do not endanger sound public finances (OECD 2022f; OECD 2022g). In Indonesia, reducing large energy subsidies and ending monetary financing of deficits would help to reinstate the deficit ceiling as a fiscal anchor. In Brazil, where petrol price caps and increases in social transfers have raised budget deficits, improving the fiscal framework, especially by limiting the growth of mandatory spending, would create space to address budgetary pressures associated with, for instance, population ageing, and help to restore the credibility of public finances. The gradual scaling back of energy subsidies and the expiry of COVID-19-related support will reduce spending pressures in Argentina, but shoring up investor confidence hinges on implementing plans to phase out the monetisation of fiscal deficits. In Türkiye, non-targeted price support measures for energy consumers are expected to continue in the near term, weighing on the public finances. The build-up of foreign-currency-denominated contingent liabilities could also put fiscal sustainability under additional pressure in the medium term. In South Africa, windfall revenues from high commodity prices have financed fuel levy reductions and the continuation of social programmes, but the public sector wage bill needs to be contained to achieve fiscal consolidation.

Structural policy efforts need to be enhanced

The pandemic, the war, the growing fragmentation of the global economy and the proliferation of extreme weather events related to climate change suggest that interacting adverse supply shocks may be more frequent in the future. Other things equal, this would mean weaker potential growth and more upward pressure on prices than otherwise and would pose further threats to the resilience of economies while further straining social cohesion.

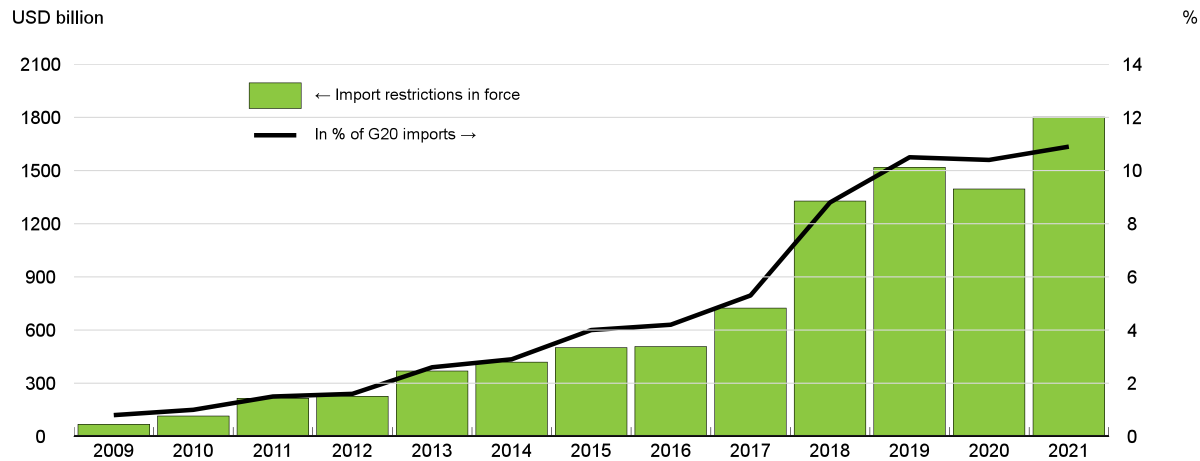
In this context, the need for effective and well-targeted structural policy reforms is greater than ever. Several broad reform priorities suggest themselves, although a major challenge for each country is tailoring and sequencing policy measures to suit its current economic circumstances. Fostering resilient growth requires competitive and transparent markets, sound governance and institutional conditions, and effective risk management strategies able to promote swift and sustained economic recoveries. Enhancing market competition and removing barriers to reallocation helps create the conditions for economies to bounce back from downturns and enables new opportunities revealed by a crisis to be more fully exploited (OECD 2021). This necessitates removing policy barriers that prevent firms from becoming more dynamic, greener and more innovative, and adapting skills policies and competition policies for the digital age. The imperative of investing more in skills has been underlined by the pandemic, which, on average across the OECD, resulted in full (nation-wide) or partial school closures totalling nearly 40 weeks, with the most affected countries seeing nearly twice that level.

The pandemic and the war have highlighted the need for stronger international co-operation as well. Areas requiring both decisive domestic and international policy action include health care (including the manufacturing and distribution of vaccines and health care equipment), climate change, and international trade. Keeping international borders open to trade, removing obstacles to stronger cross-border economic migration, and fostering the integration of migrants (including refugees) into the labour market would help all countries alleviate near-term supply-side pressures on inflation as well as strengthen future growth prospects. OECD countries received 4.8 million new permanent-type immigrants in 2021, a 22% increase relative to 2020 but still more than half a million fewer than in 2019 (OECD 2022a).

There has been some improvement in the balance of policy measures affecting trade taken by G20 economies, with more trade-facilitating than trade-restricting measures in the latest review period (mid-October 2021 to mid-May 2022; OECD/WTO/UNCTAD 2022). Even so, the cumulative total of G20 import restrictions in force has grown steadily since 2009 – both in value terms and as a percentage of world imports. By mid-May 2022, 10.9% of G20 imports were affected by the import restrictions implemented by G20 economies since 2009 that were still in force (Figure 1.38). Greater progress in international trade agreements, including efforts to lower tariffs in agriculture, could support greater access to food at reasonable prices. Ongoing efforts to support port capacity and reduce congestion in logistics are welcome, and should be sustained.

Figure 1.38. The stock of trade-restricting measures has continued to grow

Cumulative trade coverage of G20 import-restrictive measures on goods in force since 2009



Note: Cumulative trade coverage based on information available on import measures recorded since 2009 and considered to have a trade-restrictive effect. The estimates include import measures for which HS codes were available. The figures do not include trade remedy measures. The import values were sourced from the UN Comtrade database.
Source: WTO Secretariat.

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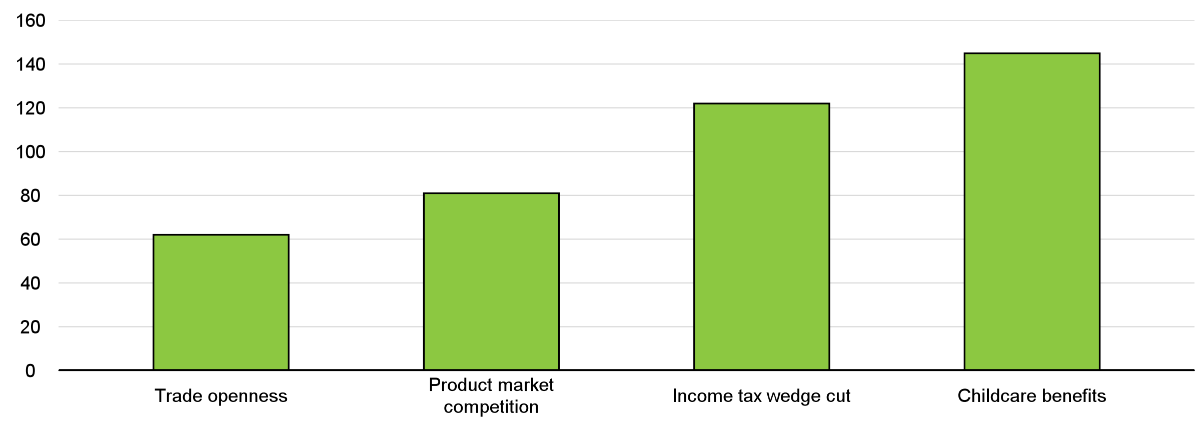
Given the cost-of-living crisis afflicting many countries, with real household incomes falling sharply in some, there is a good case for prioritising structural reforms that have a particularly large and/or direct effect on household disposable income. Recent OECD work (Botev et al., 2022) finds that the relative longer-run effects of structural policy measures on GDP and household disposable income vary substantially across different types of reform. Policies such as in-kind family benefits, family cash benefits and cuts in the income tax wedge have a magnified effect on disposable income (Figure 1.39). This suggests that, alongside the structural reform priorities identified in the regular OECD *Going for Growth* reports (OECD, 2021), increased spending on childcare and early childhood education could be useful parts of policy packages to address the cost-of-living crisis currently being faced by many OECD households.

Such reforms would also help to reduce longstanding gender gaps in labour market participation and employment (OECD, 2022h). In many countries, employment rates for women remain far below those for men (Figure 1.40). This aggravates labour shortages and supply-side bottlenecks, pointing to the need for policies that facilitate female labour force participation, such as measures to improve access to childcare (Thévenon, 2013). Many OECD countries would also benefit from measures to raise employment for other demographic groups, including older people, characterised by low labour force participation rates (OECD, 2021). In many countries, the effects of the pandemic aggravated the tendency for older workers to withdraw from the labour force, contributing to the tightening of labour market conditions. Improving employment incentives for older workers would help ease supply constraints and facilitate disinflation.

Figure 1.39. Some structural policies have larger effects on disposable incomes than GDP

Impact on household disposable income relative to GDP, with the GDP effect normalised to 100



Note: The chart shows the relative effect on household disposable compared to GDP for each policy, computed as the long-run percentage change in household disposable income divided by the long-run percentage change in GDP, with the numbers presented as an index with the long-run change in GDP equal to 100. Thus, if a policy has the same long-run percentage effect on household disposable income as GDP the height of the bar would be 100. Each bar is based on the average of two estimations detailed in Botev et al., (2022).
Source: OECD calculations based on Botev et al., (2022).

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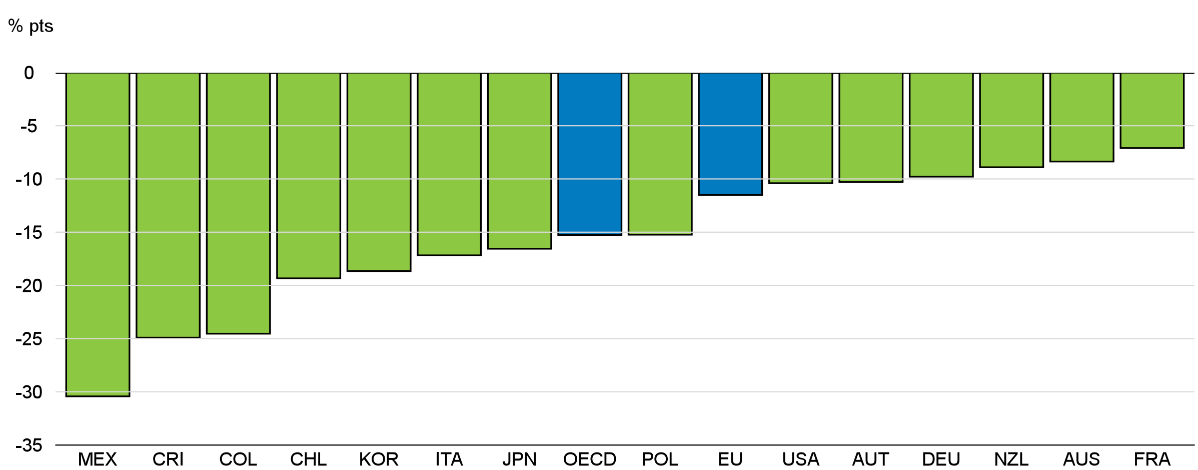
Figure 1.40. Many countries have considerable scope to improve employment rates for women

Difference between female and male employment rates, 2022Q3 or latest available



Note: Figure shows the difference between seasonally adjusted employment rates of females and males aged 15 and over.
Source: OECD Short-term Labour Statistics; and OECD calculations.

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The Russian invasion of Ukraine has highlighted the link between energy policy and security, since, at the outset of the conflict, many OECD countries were still heavily reliant on fossil fuel imports from Russia. This is especially true of Europe, where the gas price is a key determinant of electricity prices. Given that European gas and electricity markets are relatively integrated, such that shifts in consumption and supply in each country can strongly affect prices elsewhere, better outcomes can be achieved if the European economies respond collectively to the challenge of reducing reliance on fossil fuel imports from Russia (Darvas et al., 2022). European Union members have already agreed measures on gas storage and reducing demand, and the European Commission has proposed further demand reduction measures and steps to redistribute excess profits earned by energy companies to final customers (European Commission, 2022). The IEA has called for additional actions, including better coordination among electricity operators across Europe and setting standards to encourage behavioural changes among consumers (IEA, 2022c). An effective collective response also includes maintaining and even increasing cross-border flows of energy within Europe, including by improving gas and electricity interconnections. The European Union could also negotiate contracts for importing liquefied natural gas as a bloc, rather than having individual EU countries competing for shipments.

While short-run tensions between energy independence and the green transition have emerged – for example, some countries in Europe are burning more coal in order to make up for reduced imports of oil and gas from Russia and some countries in Asia are using more coal as a result of LNG supplies being diverted to Europe – the best response to the crisis is to speed up the transition to net zero carbon emissions rather than to durably increase oil and gas imports from elsewhere or to boost domestic production of fossil fuels. Such an acceleration is likely to reduce the long-run costs of the transition (IMF, 2022b) while also improving both energy security and the prospects of meeting climate objectives, as energy represents between half and two-thirds of total greenhouse gas emissions.

Achieving these objectives will require a variety of different policy instruments – price-based, non-price regulation and public investment – the relative importance of which will differ across countries depending on their initial circumstances. Given that global investment in clean power generation and energy infrastructure will need to more than triple by 2030 in order to ensure the world is on a credible path to zero net emissions by 2050 (IEA, 2021), “green” public investment and subsidies are one priority. At the same time, there is a need for a clear commitment to pricing emissions and regulatory standards that can render such investments more viable (OECD, 2020a). A policy framework combining regulatory and fiscal tools, as well as price signals, is therefore necessary, especially given evidence that environmental policy uncertainty has a negative impact on investment (Dechezleprêtre et al., 2022). Currently the framework is incomplete, with most emissions being under-priced and many policy signals remaining unclear (D’Arcangelo et al., 2022).

One specific area where the objectives of energy security and emissions reduction coincide is the waste of natural gas via flaring, venting and leakages. In 2021, 143 billion cubic metres of natural gas was flared globally – close to the volume of gas imported from Russia to the European Union in the same year. This resulted in the release of greenhouse gases equivalent to over 500 Mt of $CO2$ – similar to the combined fossil fuel emissions of France and Spain. Gas flaring, along with the direct venting of gas into the atmosphere and leakages in the transportation and storage of gas, thus not only represents a waste of resources but also exacerbates the tightness in global gas markets and has a sizeable negative impact on climate change. The IEA’s Net Zero Emissions by 2050 Scenario sees a reduction in flared volumes of around 90% by 2030 (IEA, 2022d). Countries should develop national gas flaring reduction roadmaps, and regulators should ensure that existing and new projects capture, compress or otherwise use gas that is currently flared, especially given that gas producers’ financial capacity to invest in flaring reduction is at an all-time high. Assistance from richer countries to poorer ones to reduce gas flaring is one component in the broader need for enhanced efforts on climate financing.

While progress in individual countries to cut greenhouse gas emissions is essential, a cost-efficient approach to climate change requires closer global co-operation in a number of areas, including on instruments used to mitigate greenhouse gas emissions, reporting standards and improving access to climate finance for emerging-market and developing economies. A recent OECD initiative to help countries progress faster towards international and national objectives to mitigate climate change is the Inclusive Forum on Carbon Mitigation Approaches (IFCMA), which was established by the OECD Council in June 2022. The initiative aims to help the signatories of the Paris Agreement meet that agreement's goals by facilitating the emergence of a comprehensive set of well-designed and globally better coordinated climate policies, policies which are complementary while allowing jurisdictions to act independently. To support multilateral exchange, the IFCMA seeks to provide comprehensive analysis on policies to address climate change, their comparative effectiveness and costs.

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Annex 1.A. Policy and other assumptions underlying the projections

Fiscal policy settings for 2023-24 are based as closely as possible on legislated tax and spending provisions and are consistent with the growth, inflation and wage projections. Where government plans have been announced but not legislated, they are incorporated if it is deemed clear that they will be implemented in a shape close to that announced. Existing energy-related support measures have been assumed to be extended into part or the whole of the projection period when that extension is deemed likely, even if it has not yet been announced. When a given energy-related measure spans more than one year, its total fiscal costs are assumed to be uniformly spread across months.

Projections for the EU countries account for spending financed by the Next Generation EU (NGEU) grants and loans, based on expert judgments about the distribution across years and different expenditure categories and informed by officially announced plans where available. NGEU grants are assumed to be budget neutral, i.e. they increase both capital tax and transfers receipts and government expenditure. In addition, positive net one-offs are added in order to reflect the discretionary stimulus associated with those grants, as measured by changes in underlying primary balances.

For monetary policy, the assumed path of policy interest rates and unconventional measures represents the most likely outcome, conditional upon the OECD projections of activity and inflation. This may differ from the stated path of the monetary authorities. In the euro area, 10-year sovereign spreads relative to Germany are assumed to remain constant over the projection period at levels close to those observed in October and November 2022.

The projections assume unchanged exchange rates from those prevailing on 3 November 2022: one US dollar equals JPY 147.30, EUR 1.02 (or equivalently one euro equals USD 0.98) and CNY 7.30.

The price of a barrel of Brent crude oil is assumed to remain constant at USD 95 until the end of 2024. The TTF natural gas price is assumed to average EUR 150 MW/h in 2023 and 2024. Other commodity prices are assumed to be constant over the projection period at their average levels from October 2022.

The cut-off date for information used in the projections is 17 November 2022.

OECD quarterly projections are on a seasonal and working-day-adjusted basis for selected key variables. This implies that differences between adjusted and unadjusted annual data may occur, though these in general are quite small. In some countries, official forecasts of annual figures do not include working-day adjustments. Even when official forecasts do adjust for working days, the size of the adjustment may in some cases differ from that used by the OECD.

2 Developments in individual OECD and selected non-member economies

Argentina

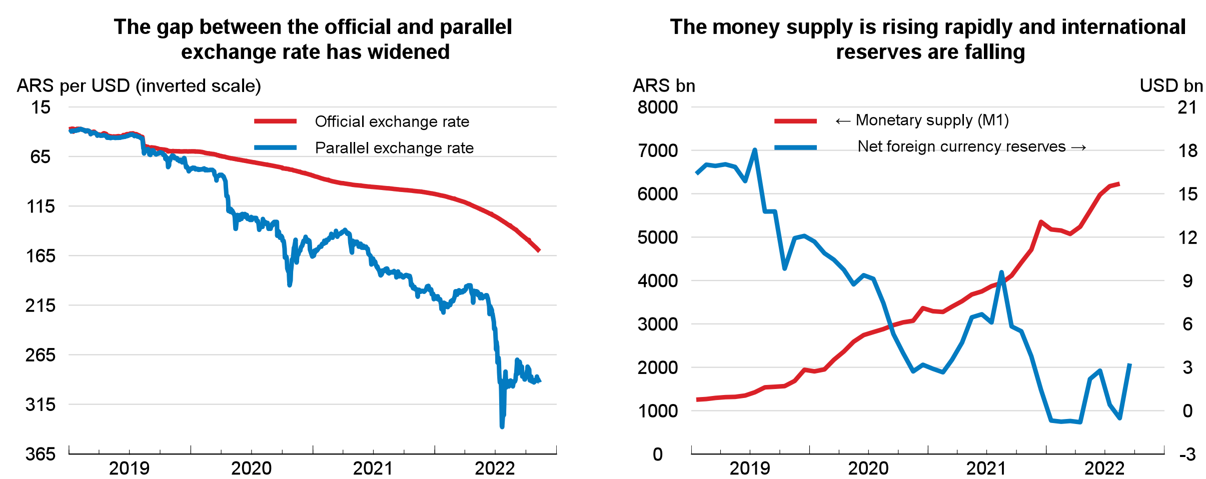
After a strong rebound in 2021 and an expected deterioration in the second half of 2022, GDP is projected to rise by 0.5% in 2023 and 1.8% in 2024. The agreement with the IMF has significantly reduced uncertainty about short-term macroeconomic policies, but the external situation remains fragile. High inflation will weigh on private consumption and will take time to recede. Tight capital controls and policy uncertainty are leading to a sharp fall in investment in the second half of 2022 and their persistence will allow only a modest recovery in 2023 and 2024.

Public spending will fall during 2022 and 2023, as pandemic-related fiscal support is withdrawn and energy subsidies are scaled back. Still, compliance with IMF targets will require further spending restraint. A planned sharp reduction in monetary financing will reduce inflationary pressures in the medium run, reduce the gap between the official and the parallel exchange rates and decrease the risk of devaluation. Stabilising the macroeconomic situation and lowering inflation are crucial to reduce high poverty and mounting social pressures.

Economic activity is stagnating

Economic growth continued to progress in the first half of 2022, but at a slower pace. Short-term indicators point to further slowing during the third quarter of 2022. The unemployment rate has returned to pre-pandemic levels, reaching 6.9% in the second quarter of 2022, although informality has increased sharply, approaching 38% of the labour force. Year-on-year headline inflation rose to 88% in October, amid unanchored one-year ahead inflation expectations of 99% and a widening gap between the official and the parallel exchange rate.

Argentina



Source: Refinitiv; BCRA; and Ambito.com.

StatLink https://stat.link/dgrib6

Argentina: Demand, output and prices

Argentina	2019	2020	2021	2022	2023	2024
	Current prices ARS billion	Percentage changes, volume (2004 prices)				
GDP at market prices	21 558.4	-9.9	10.4	4.4	0.5	1.8
Private consumption	14 256.1	-13.7	10.0	8.8	0.3	1.8
Government consumption	3 544.9	-1.9	7.1	2.4	-0.3	0.9
Gross fixed capital formation	3 061.1	-13.0	33.4	12.3	-0.3	2.4
Final domestic demand	20 862.1	-11.8	12.8	8.3	0.1	1.7
Stockbuilding[1]	2.4	1.6	0.2	-0.8	-0.1	0.0
Total domestic demand	20 864.4	-10.2	13.2	7.3	-0.3	1.3
Exports of goods and services	3 864.3	-17.7	9.2	5.0	2.1	3.6
Imports of goods and services	3 170.3	-18.5	22.0	17.0	-1.2	1.2
Net exports[1]	694.0	-0.5	-1.5	-1.6	0.5	0.2
Memorandum items						
GDP deflator	_	40.1	54.2	70.0	81.2	58.8
Consumer price index	_	40.4	50.9	92.0	83.0	60.0
Current account balance (% of GDP)	_	0.7	1.4	-0.6	-0.3	-0.1

1. Contributions to changes in real GDP, actual amount in the first column.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/t81ojg

Trade links with Russia and Ukraine are minimal, but global price changes are affecting Argentina. While food exports have temporarily benefited from rising global prices, higher costs of energy imports have worsened the trade balance as Argentina is a net energy importer. Higher global energy prices imply higher subsidy expenditures, hampering the ongoing fiscal consolidation plan. This situation has accelerated the need for a gradual removal of energy subsidies, which started in September.

Fiscal and monetary policies are tightening

The IMF formally approved the second review of the Extended Fund Facility programme in October and disbursed USD 3.8 billion (1% of GDP). This reflected the fulfilment of programme targets in the second quarter, which restored market confidence. The Central Bank of Argentina has raised the policy interest rate nine times since early 2022, to 75%. Future increases are expected to be smaller. Large amounts of outstanding central bank bonds, worth 10% of GDP, imply potential risks for the central bank's balance sheet. Primary deficit targets were set at 2.5% of GDP for 2022 and 1.9% of GDP in 2023, implying significant consolidation. IMF targets also include specific limits on transfers from the central bank to the Treasury, which are to decline to 0.8% of GDP in 2022 and 0.6% of GDP in 2023.

Growth is slowing and risks are tilted to the downside

The economy is projected to contract in the third and fourth quarters of 2022, but annual 2022 GDP growth will nonetheless reach 4.4%, before slowing to 0.5% in 2023, and then recovering to 1.8% in 2024. Against the background of high inflation, tightened import restrictions, low international reserves and severely limited fiscal space, risks remain elevated, which will keep investment and private consumption subdued in 2023. A gradual upturn is projected in 2024 as the macroeconomic situation improves. Export growth will slow in 2023, in part due to the overvalued currency, but will gradually pick up in 2024. The combination of temporary measures and strict currency controls will bolster currency reserves in the short term. However, high external financing requirements and a crawling peg exchange rate regime with an overvalued currency imply that reserves will remain low. Inflation is projected to remain high in 2023 driven by further monetary expansion and ongoing wage negotiations but gradual disinflation should start during 2023. Downside risks include a failure to comply with fiscal commitments amid growing social pressures, jeopardising fiscal sustainability. Lower commodity prices could hamper reserve accumulation and raise pressures on the exchange rate. Upside risks to growth include stronger global demand for commodities, which would bolster export revenues.

Structural reforms to boost productivity could reduce imbalances

Improving the business environment for the private sector and strengthening competition could open up new opportunities for raising productivity and exports. Current attempts to improve the targeting of utility subsidies will enhance public spending efficiency, but further progress is needed to ease fiscal imbalances. Better targeting of social transfers, including reviewing tax and pension regimes, would reduce poverty and inequity while improving fiscal accounts. Argentina is implementing a National Decarbonisation Plan aiming at net-zero emissions by 2050 but achieving this goal will likely require more ambitious policies, especially to develop renewable energy sources.

Australia

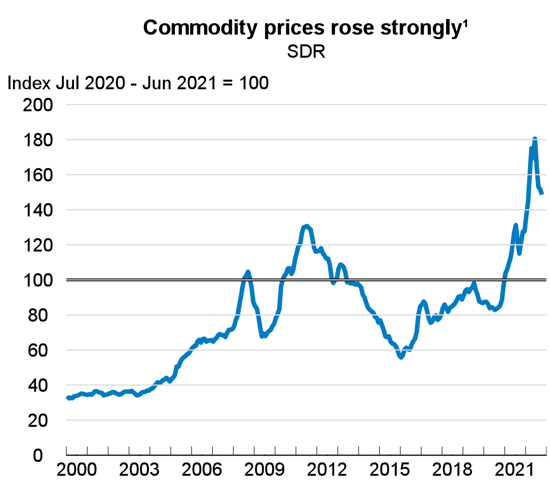
Real GDP is projected to grow by 4% in 2022, 1.9% in 2023 and 1.6% in 2024. Elevated inflation is eroding households' purchasing power and has prompted the Reserve Bank of Australia to raise interest rates at a rapid pace. As growth slows, the tightness in the labour market is expected to subside. Inflationary pressures will diminish as the labour market cools and supply chain bottlenecks ease. A stronger than expected decline in house prices is a key risk to the growth outlook.

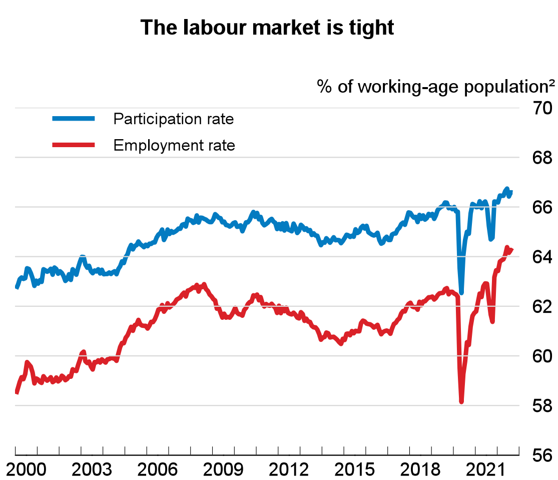
Further monetary policy tightening will be necessary to bring inflation down to the 2-3% target range. Any further fiscal support in response to cost-of-living pressures should be targeted and temporary and maintain incentives for energy savings. Reducing greenhouse gas emissions remains a top priority and will require further action, including investment in renewables and in the transmission network, regulatory changes, structural reforms and higher carbon pricing.

Inflationary pressures are rising due to global factors and a tight labour market

The recovery from the pandemic continued in the second quarter of 2022, with growth driven by strong domestic and export demand. High-frequency indicators suggest that household consumption has slowed somewhat in recent months. The labour market has tightened considerably, with the unemployment rate remaining at 3.5% in September, a historically low level. Labour shortages are rife, with employment and participation rates near all-time highs, in part due to a fall in immigration since the beginning of the pandemic. As a result, wage growth picked up significantly in the third quarter of 2022, with yearly growth in the Wage Price Index rising to 3.1%.

Australia





1. The Index of Commodity Prices measures the prices of 22 major commodities exported by Australia, including rural commodities, base metals, bulk commodities and other resources. The index is shown in terms of Special Drawing Rights (SDR), which is less affected by exchange rate movements.
2. All persons aged 15 years and over.
Source: Reserve Bank of Australia; and Australian Bureau of Statistics.

StatLink https://stat.link/2zbdr3

Australia: Demand, output and prices

Australia	2019	2020	2021	2022	2023	2024
	Current prices AUD billion	Percentage changes, volume (2019/2020 prices)				
GDP at market prices	1 995.0	-2.2	4.9	4.0	1.9	1.6
Private consumption	1 079.0	-5.8	5.0	7.0	2.0	1.6
Government consumption	396.0	7.3	5.4	5.4	1.2	1.3
Gross fixed capital formation	453.5	-2.9	9.8	8.3	2.4	1.3
Final domestic demand	1 928.4	-2.4	6.2	7.0	1.9	1.5
Stockbuilding[1]	- 1.6	-0.2	0.7	-1.2	-0.4	0.0
Total domestic demand	1 926.8	-2.7	6.9	5.6	1.5	1.5
Exports of goods and services	492.3	-9.5	-2.1	2.7	5.0	4.3
Imports of goods and services	424.1	-12.9	6.5	12.2	3.7	4.0
Net exports[1]	68.2	0.4	-1.7	-1.6	0.5	0.3
Memorandum items						
GDP deflator	_	0.9	5.4	6.8	2.8	2.1
Consumer price index	_	0.9	2.8	6.5	4.5	2.5
Core inflation index[2]	_	1.3	2.4	5.8	4.6	2.5
Unemployment rate (% of labour force)	_	6.5	5.1	3.7	3.5	4.0
Household saving ratio, net (% of disposable income)	_	17.3	15.0	9.3	8.0	7.4
General government financial balance (% of GDP)	_	-12.5	-5.3	-3.2	-2.8	-2.7
General government gross debt (% of GDP)	_	66.5	63.7	66.3	68.8	71.0
Current account balance (% of GDP)	_	2.4	3.1	0.9	-0.2	-0.4

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/3rxu4y

Russia's war of aggression against Ukraine has had little direct impact on the Australia economy given the country's limited direct economic links with the most affected countries. However, both the war and the recent stringent lockdowns in China have exacerbated supply-chain issues, particularly in the shipping industry. High global energy prices have also resulted in a rise in inflation and declining consumer sentiment. Consumer price inflation rose to 7.3% year-on-year in the third quarter of 2022, and there is evidence that price pressures are becoming more broad-based. Even so, inflation expectations remain at moderate levels. Higher commodity prices have boosted Australia's terms of trade, and strong global demand for commodities have supported exports, with Australian liquefied natural gas and coal exporters reporting a strong rise in 2022.

Macroeconomic policy is becoming more restrictive

The Reserve Bank of Australia has tightened monetary policy in response to rising inflation, raising its cash rate from 0.1% to 2.85% in the past six months. Accordingly, financial conditions have become more restrictive, with rising corporate bond yields and mortgage interest rates. Further increases in the cash rate will be necessary to bring inflation back to the target range of 2-3%, with the projections assuming that the cash rate will peak at 3.6% in the first quarter of 2023 and remain there until well into 2024. In March, the government provided cost-of-living support to low- and middle-income earners and other vulnerable parts of the population, amounting to more than 0.2% of GDP in tax offsets and direct payments. The fuel excise duty was also halved until September 2022 in response to rising fuel prices. The federal deficit is projected to gradually fall as fiscal support measures introduced during the pandemic and in response to severe flooding earlier in the year are unwound. Public investment, however, is expected to increase due to a large pipeline of public engineering work, including the infrastructure projects announced in the October Budget.

Economic growth will slow after a rapid recovery

Economic growth is projected to slow after the strong recovery from the pandemic, with real GDP growth reaching 1.9% in 2023 and 1.6% in 2024, after 4% in 2022. Tighter financial conditions and elevated inflation will weigh on consumption and investment. Dwelling investment is also projected to slow over the projection period in response to declining house prices. With a very tight labour market, wage growth is expected to pick up further in the near term, but it will ease as unemployment edges up in the second half of 2023. Inflation will moderate, aided by lower commodity prices than in 2022, easing supply disruptions and slowing wage growth later in 2023. Risks to economic growth are tilted to the downside. More persistent price pressures could cause a stronger decline in real incomes and more aggressive policy tightening by the central bank. Falling house prices may also further weaken residential construction and household spending.

Reducing emissions from greenhouse gases remains a priority

Any further support to households and businesses in response to cost-of-living pressures should be targeted, temporary, and delivered in a way that does not distort price signals. The government has committed to net zero emissions by 2050 and recently raised its greenhouse gas emissions reduction target for 2030 to a 43% cut in emissions from 2005 levels. Measures to reduce the country’s reliance on fossil fuels will be important to achieve these targets. These include greater investment in renewables and in the transmission network, regulatory changes, structural reforms and carbon pricing. As proposed by the government, reconsidering the design of the safeguard mechanism, which limits the net emissions of Australia’s largest greenhouse gas emitters, will be an important step towards achieving emissions targets.

Austria

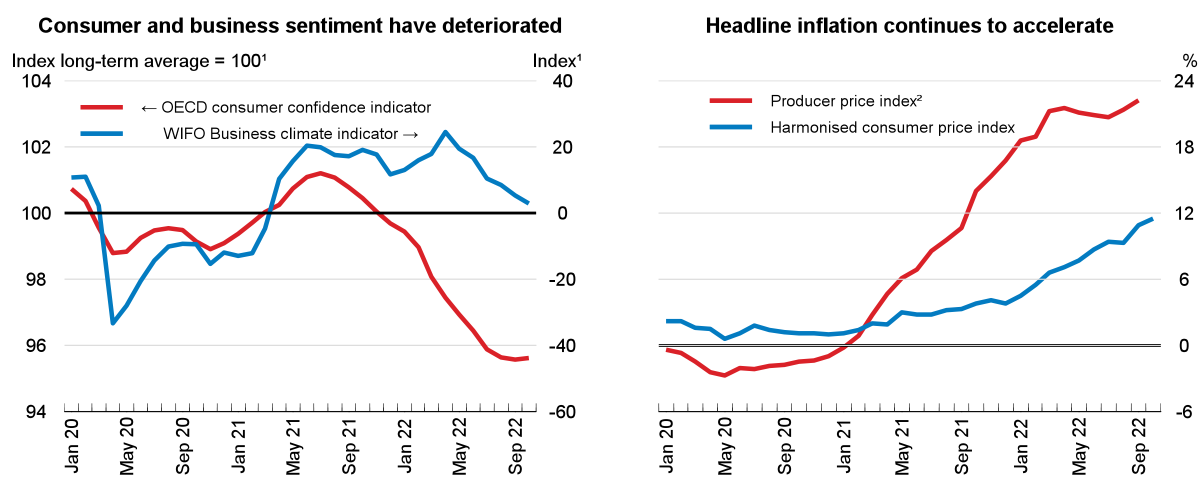
Growth is expected to be 4.5% in 2022, but slow sharply to 0.1% in 2023 and 1.2% in 2024. Headline inflation is broad-based and expected to peak towards the end of 2022, before easing over 2023 and 2024. Real disposable incomes are falling in 2022, depressing private consumption, but should recover as wages catch up with inflation. Low external demand and a deterioration in business confidence will weigh on private investment. Employment growth will weaken, but elevated labour shortages are expected to prevent a significant increase in unemployment.

The fiscal stance will tighten over the projection period. The withdrawal of the pandemic-related support has helped to narrow the primary budget deficit. New support measures to cushion energy price inflation are expected to fade out in 2023-24. Some of these measures aim at lifting growth by reducing labour costs and are welcome. Discretionary measures to compensate for high energy prices need to be better targeted to avoid weakening price signals and to limit fiscal costs. Activating existing labour reserves would help remedy persistent labour shortages.

Growth is slowing amidst rising inflation

Output expanded strongly in the first half of 2022, but will contract in the second half of the year, with GDP declining slightly in the third quarter. Accelerating producer and consumer price inflation has weighed on business and consumer sentiment. Headline inflation reached 11% in October and is broadening, with core inflation accelerating. Producer price inflation also continues to rise and will add pressure on consumer prices. Collective bargaining in the metals industry, usually an important reference point for wage setting in other industries resulted in wage increases of 7.4% for a one-year period starting from November 2022.

Austria



1. Long-term average cover January 2014 to September 2022. The WIFO index ranges from -100 to 100, indicating that a positive (negative) value signals an optimistic (pessimistic) business climate.
2. Producer price index refers to total industrial activities.
Source: OECD Main Economic Indicators database; and WIFO Business cycle survey.

StatLink https://stat.link/4iqd8s

Austria: Demand, output and prices

Austria	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices*	397.0	-6.6	4.7	4.5	0.1	1.2
Private consumption	204.6	-7.9	3.4	3.8	0.7	1.9
Government consumption	77.2	-0.5	7.9	-1.3	-3.5	-0.3
Gross fixed capital formation	98.5	-5.0	8.7	-0.5	1.0	1.4
Final domestic demand	380.4	-5.7	5.7	1.5	-0.1	1.3
Stockbuilding[1]	1.6	0.1	0.7	1.0	0.5	-0.8
Total domestic demand	382.0	-5.5	6.5	2.4	0.0	0.5
Exports of goods and services	222.0	-11.4	10.2	13.6	2.3	4.8
Imports of goods and services	207.0	-9.2	13.7	7.5	1.4	3.8
Net exports[1]	15.1	-1.6	-1.4	3.5	0.5	0.7
Memorandum items						
GDP deflator	_	2.5	1.9	4.3	6.0	3.0
Harmonised index of consumer prices	_	1.4	2.8	8.5	6.7	3.6
Harmonised index of core inflation[2]	_	2.0	2.3	4.9	5.1	2.4
Unemployment rate (% of labour force)	_	5.4	6.2	4.9	5.1	5.2
Household saving ratio, net (% of disposable income)	_	13.3	12.0	6.1	7.0	7.3
General government financial balance (% of GDP)	_	-8.0	-5.9	-3.5	-2.7	-2.0
General government gross debt (% of GDP)	_	112.0	105.6	104.5	103.1	102.0
General government debt, Maastricht definition[3] (% of GDP)	_	83.1	82.3	81.2	79.8	78.7
Current account balance (% of GDP)	_	3.0	0.4	0.7	1.0	1.8

* Based on seasonal and working-day adjusted quarterly data; may differ from official non-working-day adjusted annual data.
1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/ymrxe5

The Austrian economy remains vulnerable to disruptions in gas supply as around 50% of the gas consumed is imported from Russia, down from 80% at the beginning of 2022. As of October 2022, gas reserves cover around 90% of annual gas consumption. This includes the new public strategic gas reserve that could cover two full winter months. Around 60% of the gas can be allocated to Austrian households and businesses. Global energy and commodity price rises have hit households and firms hard, notably in export-oriented manufacturing sectors. As of October 2022, Austria has received 83 000 refugees from Ukraine. The authorities have allocated fiscal support of around 0.13% of GDP (2022) and 0.12% of GDP (2023) for humanitarian help for Ukrainian refugees and their integration in domestic labour markets.

Fiscal spending partly offsets energy price inflation

The primary budget deficit is expected to narrow over the projection period. Fiscal policy shifted from pandemic-related support to measures to compensate for energy price inflation and to lift potential growth, mainly by transforming the economy towards climate neutrality. In the first half of 2022, three support packages, amounting to a budget envelope of 8% of 2021 GDP, have been implemented. They comprise discretionary measures for 2022 and 2023 to mitigate high energy prices on households and firms, including several subsidies, energy vouchers and tax cuts. Furthermore, an electricity cap for every household will be in effect from December 2022 until mid-2024. New structural measures include the establishment of a strategic gas reserve and, from 2023 on, the automatic adjustment of personal income tax brackets to inflation, and a 0.2 percentage point reduction in indirect labour costs. Further, the eco-social tax reform combines an increase in carbon taxes with lower personal and corporate income taxes to be implemented gradually over the projection horizon. Funds from the European Recovery and Resilience Facility, roughly 0.8% of GDP until 2026, will mainly support investment in renewable energy and digitalisation.

Economic growth will be weak

Output will recover gradually and grow by 0.1% in 2023 and 1.2% in 2024. Accelerating producer price inflation, elevated uncertainty over the future course of the war in Ukraine and low external demand will weigh on business investment and exports. Inflation will decline to 3.6% in 2024 with financial conditions tightening and the passing of the energy shock but remain elevated over the projection period. Private consumption will recover in 2024 as real disposable incomes gradually pick up. The labour market may nevertheless remain tight, as shortages of skilled labour constrain activity and keep the unemployment rate low. Downside risks to the projections remain very high. Over the short term, gas imports from Russia cannot be substituted from other sources and a complete halt of imports would have a significant adverse impact on growth. A worsening of the pandemic would interfere with the winter tourism season and weigh on activity in services sectors.

Reforms could make growth stronger and more sustainable

Reducing severe skill shortages is vital to boost growth. Activating existing, but yet untapped, labour reserves would be key. This would require more efforts to promote female employment, for example by improving on the availability and quality of early child education and care services throughout the entire country. Better incentives to continue working at an older age, and ensuring good working conditions for elderly workers, would also help. Programmed public investments to reduce greenhouse gas emissions will make growth more sustainable and enhance energy security. However, more efforts are needed to comply with the ambitious 2040 climate neutrality goal. While the eco-social tax reform is a welcome step, harmonising and raising carbon prices across all economic sectors, along with complementary regulatory and emission savings investment schemes, is necessary. Support measures to counteract high energy prices need to be better targeted at households that are highly exposed to rising living costs, while not undermining incentives to reduce the consumption of fossil fuels.

Belgium

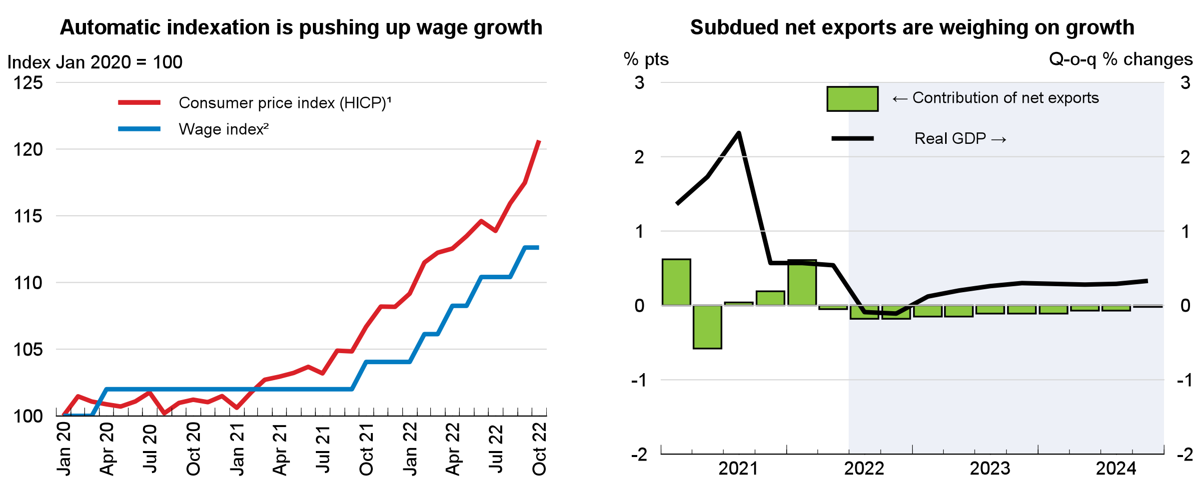
GDP growth is projected to slow considerably from 2.9% in 2022 to 0.5% in 2023 in the face of high inflation and heightened uncertainty, before picking up to 1.1% in 2024. Private consumption will remain weak until mid-2023 despite the automatic indexation of wages, which supports household purchasing power. Subdued net exports will contribute negatively to GDP over the projection period, as international competitiveness deteriorates and the economy is highly exposed to a slowdown in its main trading partners. Headline consumer price inflation is projected to average almost 10% in 2022 and remain high in 2023.

The fiscal stance is expected to be neutral in 2023 and moderately restrictive in 2024. Better targeting of energy support measures while maintaining price signals is crucial for both fiscal sustainability and energy saving, and to limit further inflationary pressures. Clarifying the policy stance on nuclear power is necessary to ensure energy security. Introducing carbon taxation on all emissions is essential to promote green investments and enable the energy transition.

The economy has slowed amid a deteriorating global outlook

High energy prices, declining confidence and weakening international trade have slowed GDP growth, with output declining by 0.1% in the third quarter of 2022. Annual headline inflation surged to 13.1% in October, with persistently high energy inflation at 69.2% and steadily increasing food price inflation approaching 12%. The large 16-point drop in consumer confidence in September was close to that recorded at the onset of the COVID-19 pandemic, despite the automatic indexation that increased most nominal wages and welfare benefits by about 8% since January and prevented a larger decline in real incomes. Business sentiment has declined for several months, including a significant deterioration in construction demand expectations in October. The trade deficit increased by EUR 23 billion (about 4% of GDP) over the first eight months of 2022 compared to the same period in 2021.

Belgium



1. Provisional HICP data for October 2022.
2. For employees whose wages are automatically indexed based on the national consumer price index excluding alcohol, tobacco and motor fuel (about 60% of all employees).
Source: OECD Economic Outlook 112 database; Federal Planning Bureau; National Bank of Belgium; and Statistics Belgium.

StatLink https://stat.link/xuifsd

Belgium: Demand, output and prices

Belgium	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	478.6	-5.4	6.1	2.9	0.5	1.1
Private consumption	245.7	-8.3	5.5	2.5	0.1	2.2
Government consumption	110.2	0.0	4.8	1.0	2.3	0.7
Gross fixed capital formation	116.2	-5.1	4.9	-0.1	1.7	1.1
Final domestic demand	472.1	-5.6	5.2	1.5	1.0	1.6
Stockbuilding[1]	3.5	-0.3	0.4	1.0	0.1	0.0
Total domestic demand	475.6	-5.8	5.5	2.6	1.0	1.5
Exports of goods and services	394.4	-5.0	11.3	3.8	0.3	1.3
Imports of goods and services	391.4	-5.6	10.7	3.4	0.9	1.7
Net exports[1]	3.0	0.4	0.7	0.4	-0.6	-0.4
Memorandum items						
GDP deflator	_	1.5	2.9	6.8	5.5	3.2
Harmonised index of consumer prices	_	0.4	3.2	9.9	6.6	4.1
Harmonised index of core inflation[2]	_	1.4	1.3	3.9	6.1	4.1
Unemployment rate (% of labour force)	_	5.8	6.3	5.8	6.5	6.2
Household saving ratio, net (% of disposable income)	_	13.7	9.9	9.2	9.5	8.2
General government financial balance (% of GDP)	_	-9.0	-5.6	-5.2	-5.8	-5.3
General government gross debt (% of GDP)	_	140.9	129.8	126.8	127.6	129.2
General government debt, Maastricht definition[3] (% of GDP)	_	112.0	109.2	106.2	107.0	108.5
Current account balance (% of GDP)	_	1.1	0.4	-4.6	-4.4	-4.8

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/rbuzqj

Belgium imports all of its fossil fuels, notably through a major LNG terminal in Zeebrugge, but produces about 40% of its electricity consumption from six nuclear reactors. Gas storage is at maximum capacity since late September, but only covers 4% of annual gas consumption. In October, gas, electricity and heating oil were 131%, 85% and 58% more expensive than a year ago, respectively. Energy support for households includes untargeted measures (reduced VAT on electricity and gas, reduced excise duty on gasoline, lump-sum transfers) and measures targeted to lower-income groups (expansion of the social tariff on gas and electricity). Businesses benefit from temporary unemployment schemes, deferred tax and social security payments, and moratoria on debt payments. The fiscal cost of the support package is estimated to about EUR 5 billion (about 1% of GDP) for 2022 and EUR 4 billion (about 0.8% of GDP) for 2023.

Public finances are under pressure

The budget deficit will reach 5.2% of GDP in 2022, down from 5.6% in 2021, helped by the phasing-out of pandemic spending but widened by the expansionary fiscal response to the energy crisis. The OECD projections assume that the energy support package will remain in place until the first quarter of 2024. Other fiscal measures include: a EUR 1 billion (about 0.2% of GDP) reduction in employer social security contributions and an estimated EUR 1 billion increase in defence- and security-related expenses. Fiscal plans are to be funded through both spending cuts, including in healthcare, and new revenue of about EUR 3.1 billion (0.6% of GDP), including an exceptional tax on excess profits in the energy sector. The fiscal stance is expected to be neutral in 2023 and moderately restrictive in 2024, with budget deficits of 5.8% and 5.3% of GDP, respectively.

Growth will be low but improve gradually

GDP is projected to grow by 0.5% in 2023, held back by pressures on household disposable income, weak export market growth and losses in export market share, before picking up to 1.1% in 2024. High energy and commodity prices will weigh on private consumption, while rising long rates depress residential investment and mounting energy and wage costs exert a drag on exports. Business and government investment growth will resume, helped by EU funds, and support GDP, despite tighter monetary conditions. Both headline and core inflation are projected to subside, as financial conditions tighten, but to remain high over the projection period. A continued energy crisis could lead to a wage-price spiral on the back of automatic wage indexation. Supply bottlenecks could also disrupt investment. An acceleration of exports, from higher-than-expected growth in the main trading partners, is an upside risk.

Ensuring fiscal sustainability and energy security is key

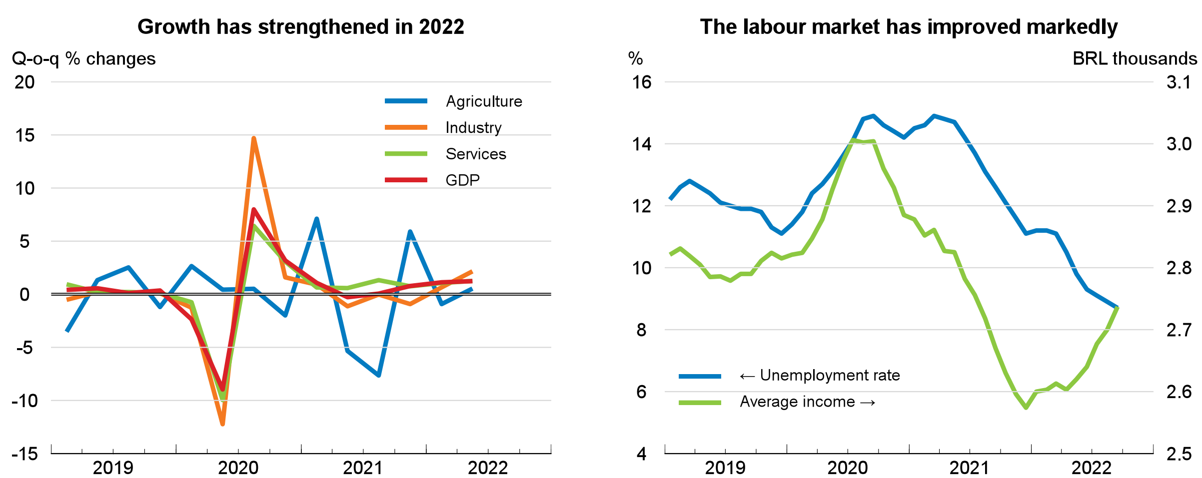
Fiscal support to attenuate the consequences of the energy shock should increasingly target low-income households and viable firms, while maintaining energy saving incentives. A consolidation strategy based on spending reviews is needed to rebuild fiscal buffers and lower the debt-to-GDP ratio gradually. Clarity on the energy policy stance, in particular on nuclear power, is crucial to ensure the security of electricity supply and achieve energy diversification away from fossil fuels. Explicit and predictable carbon taxation on all greenhouse gas emissions is required to promote low-carbon investments. Further removal of barriers to competition would boost productivity and attenuate the impact of increasing wages on international competitiveness.

Brazil

GDP is projected to grow by 2.8% in 2022, 1.2% in 2023, and 1.4% in 2024. Household consumption, private investment and exports will remain the main drivers of growth, although quarterly export growth is projected to slow in 2023. Household spending is buoyed by higher social transfers and vigorous employment growth but will also ease next year. Private investment will continue to rise on the back of improving business confidence. Despite higher global interest rates, the exchange rate has appreciated slightly this year, attenuating inflationary pressures. Inflation is projected to decline over the projection period as the effects of higher energy and food prices fade.

Monetary policy is expected to remain restrictive, with the current policy rate of 13.75% unchanged until mid-2023. Policy interest rates can be lowered once inflationary pressures recede further. Fiscal policy has been expansionary and has contributed to inflationary pressures by raising demand. A comprehensive consolidation strategy is needed to reduce the deficit and restore the credibility of the fiscal framework. Reducing budget rigidities and limiting mandatory government spending would improve spending efficiency. Better managing public infrastructure investment, reforming social transfers, and stronger sustainability incentives for the agricultural sector could boost potential growth while improving public finances. Further developing the energy mix would reinforce resilience to climate shocks.

Brazil 1



Source: IBGE.

StatLink https://stat.link/logw2h

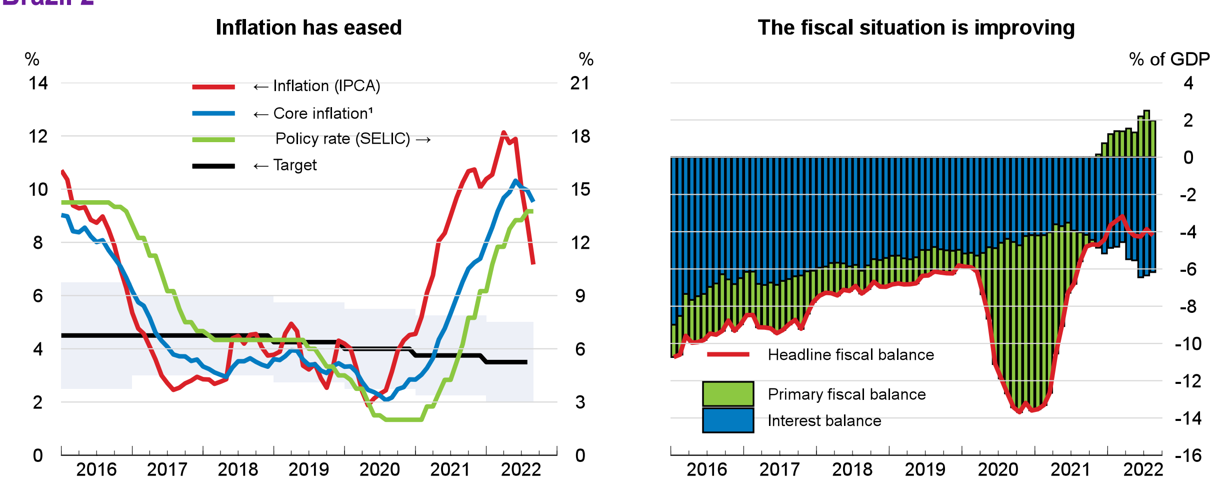
Brazil: Demand, output and prices

Brazil	2019	2020	2021	2022	2023	2024
	Current prices BRL billion	Percentage changes, volume (2000 prices)				
GDP at market prices	7 389.1	-4.2	4.9	2.8	1.2	1.4
Private consumption	4 813.6	-5.5	3.6	4.0	1.8	1.1
Government consumption	1 476.6	-4.5	2.0	0.4	-0.5	0.4
Gross fixed capital formation	1 143.2	-0.5	17.3	-0.3	3.3	3.2
Final domestic demand	7 433.4	-4.5	5.5	2.5	1.7	1.4
Stockbuilding[1]	3.4	-0.7	0.7	-0.2	0.2	0.0
Total domestic demand	7 436.7	-5.4	6.2	2.3	1.9	1.5
Exports of goods and services	1 043.6	-2.3	6.4	2.4	2.6	3.4
Imports of goods and services	1 091.2	-10.3	13.0	-0.6	6.5	3.9
Net exports[1]	- 47.6	1.2	-1.0	0.6	-0.7	-0.1
Memorandum items						
GDP deflator	_	5.5	10.7	7.1	5.2	4.3
Consumer price index	_	3.2	8.3	8.9	4.2	4.5
Private consumption deflator	_	3.2	8.7	9.8	4.7	4.5
General government financial balance (% of GDP)	_	-13.6	-4.7	-6.0	-5.9	-5.7
Current account balance (% of GDP)	_	-1.6	-1.8	-1.5	-1.4	-1.4

1. Contributions to changes in real GDP, actual amount in the first column.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/pgefbc

Brazil 2



1. Core inflation excludes energy and food products. The shaded area corresponds to the inflation tolerance band.
Source: OECD Economic Outlook 112 database; Central Bank of Brazil; and OECD calculations.

StatLink https://stat.link/jadwbg

Activity surprised on the upside in the first half of 2022

Economic activity accelerated in the first and second quarters with higher-than-expected growth of 1.1% and 1.2% (quarter-on-quarter) respectively. However, growth weakened in the third quarter. Monthly indicators point to a slowdown of activity in mining, though indicators are more mixed in manufacturing. The headline figure for manufacturing points to a small aggregate decline driven by intermediate and non-durable goods, but most manufacturing sectors kept growing. Moreover, capacity utilisation in the manufacturing sector has increased to over 80%, confirming a broad-based manufacturing recovery. Services expanded strongly in August for a fourth consecutive month, driven by household services and information and technology, though transport services have been declining. The services sector continues to be the main driver of GDP growth on the supply side, partly still reflecting pent-up demand from the lifting of mobility restrictions. Broad retail sales declined in the third quarter as real wage growth levelled off, household credit decelerated and the savings rate normalised.

Headline inflation has receded from 11.9% year-on-year in June to 6.5% in October, but core inflation remains high at 8.2% in October. Inflation expectations have fallen to 4.7% and 4% for 2023 and 2024 respectively. The decline of headline inflation is mainly due to falling international oil prices and significant tax relief, including a cap on the rate that subnational governments can apply for the largest consumption tax, in addition to reductions and exemptions from federal taxes. These measures effectively reduce the tax burden on fuels, electricity, natural gas, communications and public transport. They have also curtailed states' tax revenues, which cooled off in July, rising by only 1.2% compared to 4.5% until June. The labour market has improved as economic activity gathered momentum. The unemployment rate declined from 11.1% in March to 8.7% in September, as job creation remained vigorous. Average real labour income rose by 2.5% year-on-year in September.

Restrictive monetary and fiscal policies are on the way

The Central Bank of Brazil is expected to maintain the policy rate at 13.75% until mid-2023. Given ongoing monetary policy tightening in advanced countries, which will exercise pressures on the exchange rate, the policy rate should not start declining until trend inflation is on a persistently declining trajectory. Starting from mid-2023, policy rates are expected to be reduced to 10% by the end of 2024.

Fiscal policy has been expansionary in 2022, propelled by tax exemptions to cope with higher energy prices and a 50% increase in the size of the social transfer programme Auxílio Brasil. Both policies are currently set to expire in December 2022, although the increase of the social transfer programme will likely be maintained. This would cost around 0.5% of GDP, similar to the cost of a continuation of the tax exemptions, after adjusting for their likely growth impact. However, maintaining both measures will be hard to reconcile with the fiscal rules and with the need to move towards a more restrictive fiscal policy stance to reduce the deficit and contain public debt from 2023 onwards.

Economic growth is slowing

A deteriorating global outlook, tighter fiscal policy and the effects of higher interest rates will reduce GDP growth from 2.8% in 2022 to 1.2% in 2023, before a slight improvement to 1.4% in 2024. Lower commodity prices and the slowdown in major trading partners will reduce external demand. Tighter credit conditions will limit household consumption along with a slowdown in job creation in 2023. As supply bottlenecks fade and the gradual effects of higher policy rates materialise, inflation is projected to decrease from a year average of 8.9% in 2022 to 4.2% in 2023, but to edge up to 4.5% in 2024 as growth picks up, at the upper end of the 1.5-4.5% tolerance band around the inflation target of the central bank for 2024.

Risks to inflation are tilted to the upside as most of the inflation decline is coming from administered prices such as fuel prices, while market prices, though rising less quickly for industrial goods, remain dynamic in the services sector. Moreover, the tight labour market might keep services inflation and other cyclical prices higher for longer, particularly if real wages start to rise. Uncertainties around future fiscal policy might unsettle financial markets, requiring the central bank to maintain high policy rates for longer, which would weigh on growth.

An overhaul of the fiscal framework is needed

Compliance with the current fiscal framework is becoming increasingly difficult due to the inherent conflict between a fiscal rule that limits the increase of government spending and budget rigidities, as mandatory spending rules affect around 92% of the budget. A reform reducing automatic spending requirements, together with a stronger fiscal framework, could provide some relief for fiscal policy. Brazil already has a relatively clean energy mix, with 86% of electricity sourced from hydropower and biomass and 45% of its energy from renewables. The strong reliance on hydroelectric energy has shown limits in 2021 when droughts lowered reservoir levels, calling for stronger investment in other renewable sources. Wind and solar sources present significant untapped potential. Public investment in infrastructure in Brazil is low compared to the OECD and peers and it has declined over time. Large infrastructure gaps exist in transport, water, and sanitation. Scaling up investment in high-quality and broadly accessible infrastructure would raise productivity and potential growth and contribute to climate mitigation and adaptation.

Bulgaria

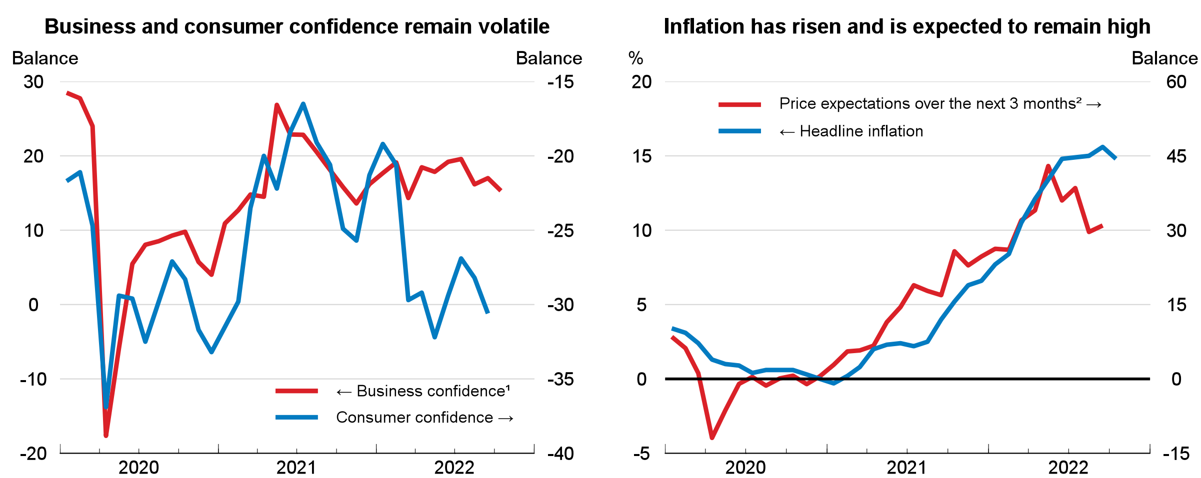
GDP growth is projected to slow to 1.7% in 2023 before rebounding to 3.1% in 2024, supported by investments from EU funds. Exports will be adversely affected by the deteriorating macroeconomic situation in Europe, while high energy prices and rising interest rates will weigh on consumption. Inflation will slowly decline amidst stabilising energy prices and subdued economic activity. Energy supply is secured thanks to low dependence on gas, a new pipeline, and a position as a net exporter of electricity. Bulgaria is assumed to enter the euro area at the start of 2024.

Effective management and roll-out of EU funds is required to support activity and to return to the pre-crisis convergence path towards OECD-average per capita incomes. Support packages, including price caps on electricity along with VAT and excise tax reductions on gas, have shielded consumers and businesses from rising energy prices, but the measures should be better targeted and designed to preserve incentives for energy savings. Investments in renewable energy need to be encouraged as they would help to align efforts to decarbonise the economy and address energy security concerns.

Bulgaria faces weaker growth and high inflation

GDP growth remained robust in the first half of 2022 as exports remained strong and inventories surged. Business confidence has softened slightly, signalling increased uncertainty amid heightened energy prices and expectations of rising interest rates. High inflation is weighing on private consumption, but consumer confidence has improved after an initial drop in 2022. Labour shortages are significant, and unemployment remains low. In contrast with most OECD countries, real wage growth has held up albeit at a slower pace due to high nominal wage increases and regulated energy prices.

Bulgaria



1. Business confidence is expressed by the total business climate indicator, covering industry, retail trade, construction and the service sector.
2. Average balance of opinions about selling price expectations in the business surveys for industry and retail trade.
Source: National Statistical Institute.

StatLink https://stat.link/4ambkr

Bulgaria: Demand, output and prices

Bulgaria	2019	2020	2021	2022	2023	2024
	Current prices BGN billion	Percentage changes, volume (2015 prices)				
GDP at market prices	120.4	-4.0	7.1	2.8	1.7	3.1
Private consumption	71.1	0.0	8.4	2.9	2.1	2.8
Government consumption	20.1	7.9	0.6	4.6	0.8	1.2
Gross fixed capital formation	22.2	0.6	-6.6	-4.6	13.9	5.8
Final domestic demand	113.4	1.6	3.7	1.9	3.9	3.0
Stockbuilding[1]	2.6	-1.3	3.6	3.7	0.1	0.0
Total domestic demand	116.0	0.1	7.3	5.6	3.6	2.8
Exports of goods and services	77.5	-10.3	10.9	5.6	2.8	6.0
Imports of goods and services	73.1	-4.3	10.9	10.3	5.3	5.6
Net exports[1]	4.4	-4.0	0.3	-2.7	-1.6	0.3
Memorandum items						
GDP deflator	_	4.3	7.5	13.7	7.8	5.2
Consumer price index	_	1.7	3.3	14.1	7.5	4.8
Core consumer price index[2]	_	1.2	1.4	7.0	6.4	4.8
Unemployment rate (% of labour force)	_	5.1	5.3	5.0	5.2	4.8
Household saving ratio, net (% of disposable income)	_	8.1	6.4	7.3	7.4	7.0
General government financial balance (% of GDP)	_	-3.8	-3.9	-4.8	-4.3	-3.0
General government gross debt (% of GDP)	_	34.8	35.1	39.2	42.7	44.8
General government debt, Maastricht definition[3] (% of GDP)	_	24.6	24.0	28.1	31.6	33.6
Current account balance (% of GDP)	_	0.0	-0.5	-1.0	-2.5	-2.6

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/wuyj5z

Bulgaria is facing headwinds from weak growth in its main trading partners, with trade with Russia and Ukraine relatively limited but stable. Gas plays only a minor role in Bulgaria's energy mix which is dominated by nuclear and coal-based electricity that is produced at low cost and exported to neighbouring countries. Bulgaria saw a strong inflow of Ukrainian refugees, but many of them have already left the country. Energy support measures, implemented since autumn 2021, need to be more targeted and gradually phased out where possible.

Extensive policy supports have been put in place

Inflation pressures from energy and food prices are cushioned by means of several temporary support schemes including price caps on electricity, subsidies for fuel and tax cuts for gas and bread. Tax exemptions are implemented until mid-2023 and 2025 for some excise duties, while the other short-term measures have recently been extended until the end of 2022 with total costs of around 3.2% of GDP for 2022 as a whole. It is expected that support programmes will be gradually scaled back and become more targeted, although the implementation of additional fiscal policy measures is subject to the formation of a new government. If current commitments implemented until the end of the year are upheld in 2023, the budget deficit would exceed 4.3% of GDP in 2023, breaking with the historically rather prudent fiscal approach. Nevertheless, a more conservative approach involving gradual consolidation is expected. Monetary conditions will be closely aligned with those in the euro area under the currency board. Accordingly, ongoing ECB tightening will contribute to reducing inflation.

A resilient rebound is expected after the near-term slowdown

Bulgaria is facing headwinds from the global macroeconomic situation but will start to recover quickly in 2024 supported by public and private investments driven by EU funds. Deteriorating economic conditions and increasing uncertainty in key trading partners will slow exports and dampen consumption in 2023. The implementation of EU-funded projects has been delayed, but is expected to strengthen in 2023, helping to achieve GDP growth of around 1.7%. Rising interest rates will weigh on activity but headline inflation will moderate from historically high levels of around 14% in 2022 on a year-average basis to around 7.5% in 2023 followed by a further gradual decline in 2024. Core inflation will only marginally decrease in 2023 to around 6.4% and slowly align with headline inflation by 2024 as the pass-through from higher interest rates continues. The labour market will remain resilient with only a marginal increase in unemployment in 2023, but widespread labour shortages will keep unemployment low and real wage growth positive at around 1%. Upward risks to the inflation outlook are created by stronger second-round effects from further wage increases coupled with considerable government spending and investment. Political uncertainty places planned investments at risk. There is also a risk of maintaining support measures longer than necessary and delaying fiscal consolidation.

Structural reform needs are pressing

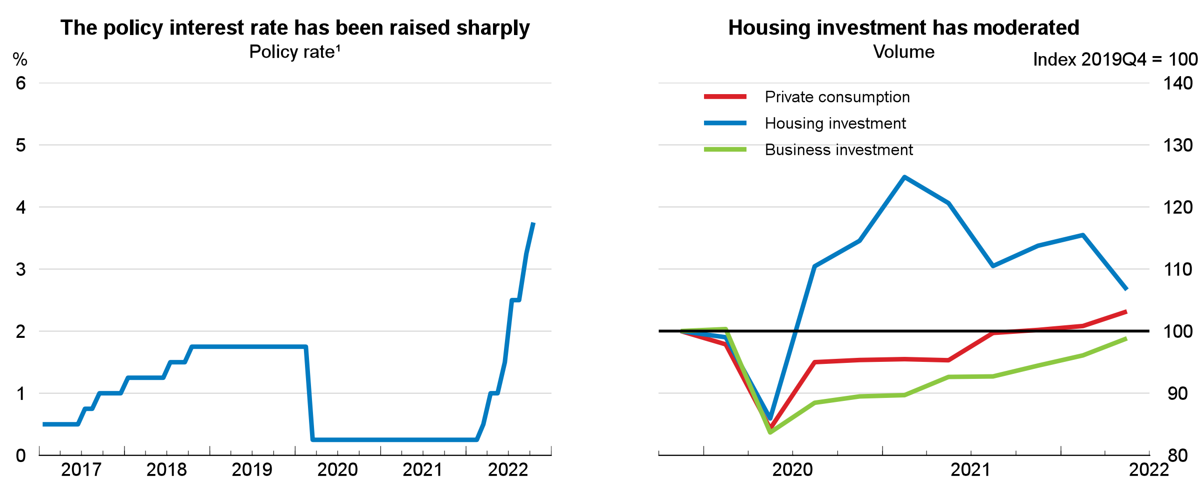
Effective management of EU funds is key for sustaining activity and boosting potential growth. Strengthening the convergence process requires pursuing and deepening reforms to encourage and intensify investments in infrastructure and digitalisation, reduce administrative burdens including improvements to the insolvency framework, strengthen efforts to fight corruption – for example by guaranteeing the accountability of prosecutors – and increase competition. Energy security is currently not a concern, but the decarbonisation of the economy will require considerable further efforts, including an accelerated installation of renewable energy production. Where necessary, the extension of energy support measures in 2023 should be better targeted with a view to gradually reduce fiscal costs.

Canada

Growth in real GDP is projected to slow from 3.2% this year to 1% in 2023 before strengthening to 1.3% in 2024. Higher borrowing costs will weigh on consumer spending while export growth moderates in the near term amid deteriorating conditions abroad. Softer aggregate demand will relieve pressure on capacity, aided by continued recovery in non-housing investment. Labour markets have been tight until recently, but hiring will decline with slower output growth. Wage growth will moderate as the unemployment rate settles slightly above pre-pandemic levels. Inflation will converge on target as underlying cost drivers ease and remaining supply bottlenecks clear.

Large interest rate rises this year will help check excess demand and tame inflationary pressures. The pace of monetary tightening should slow if labour markets show signs of deteriorating. Living-cost relief is weighing on fiscal balances in 2022. Federal and provincial governments should scale back support as price pressures abate. This will reduce fiscal deficits next year and help temper aggregate demand. A raft of measures have been developed to ensure long-term growth in Canada's economy is sustainable. Low-cost emissions mitigation depends on improving policy instruments such as carbon pricing, while supporting green investment.

Canada 1



1. The policy rate is the Bank of Canada's target average rate for overnight money market financing.
Source: OECD Economic Outlook 112 database.

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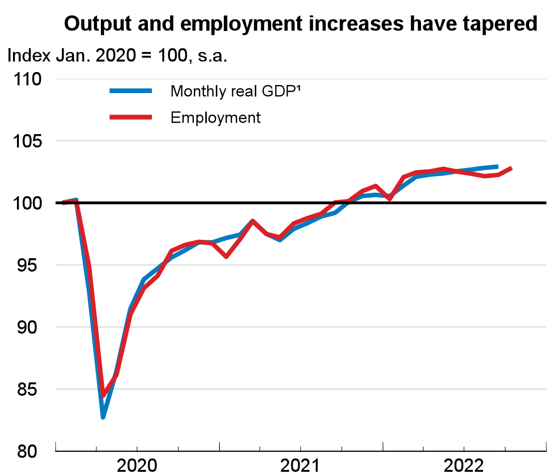
Canada: Demand, output and prices

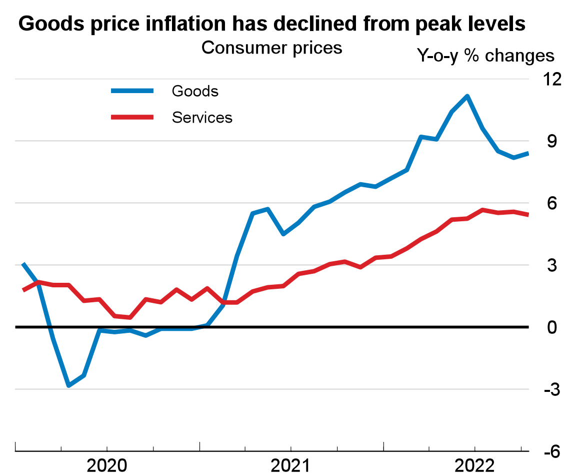
Canada	2019	2020	2021	2022	2023	2024
	Current prices CAD billion	Percentage changes, volume (2012 prices)				
GDP at market prices	2 311.3	-5.2	4.5	3.2	1.0	1.3
Private consumption	1 334.9	-6.1	4.9	5.4	2.0	1.2
Government consumption	479.4	0.0	5.8	1.6	0.7	0.7
Gross fixed capital formation	517.9	-2.8	7.1	0.0	0.3	1.5
Final domestic demand	2 332.2	-4.2	5.6	3.3	1.3	1.2
Stockbuilding[1]	15.5	-1.7	0.9	1.9	0.2	0.0
Total domestic demand	2 347.7	-5.8	6.5	5.2	1.5	1.2
Exports of goods and services	745.2	-9.7	1.4	2.3	2.4	1.9
Imports of goods and services	781.6	-10.8	7.7	8.7	3.8	1.4
Net exports[1]	- 36.4	0.5	-2.0	-1.9	-0.5	0.2
Memorandum items						
GDP deflator	_	0.7	8.1	8.3	2.7	2.2
Consumer price index	_	0.7	3.4	6.8	4.1	2.4
Core consumer price index[2]	_	1.1	2.3	4.9	4.0	2.4
Unemployment rate (% of labour force)	_	9.5	7.4	5.4	5.7	6.0
Household saving ratio, net (% of disposable income)	_	14.4	10.8	5.8	3.2	2.7
General government financial balance (% of GDP)	_	-11.4	-5.0	-1.7	-0.7	-0.5
General government gross debt (% of GDP)	_	126.9	118.7	111.6	111.4	111.1
Current account balance (% of GDP)	_	-1.8	0.0	-0.6	-2.3	-2.3

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/6toupa

Canada 2





1. Flash estimate for September 2022.
Source: Statistics Canada via Refinitiv.

StatLink https://stat.link/1rjvhw

Economic activity is cooling

Strength in Canada's resources sectors has helped offset slower growth in services. Industry GDP data suggest activity has cooled after an earlier post-pandemic rebound in hard-hit sectors including travel and accommodation. Business sentiment dipped in the third quarter on expectations of slower sales. Investment and hiring intentions have moderated and firms are starting to report easing capacity pressures. While job vacancies and employment remain near highs seen earlier in the year, job growth has slowed relative to population increases. Larger-than-usual migration inflows from other countries are helping to fill positions in some sectors. Canada ramped up permanent immigration programmes after international borders re-opened. The country has also welcomed large numbers of Ukrainian refugees; over 375 000 applications have been approved, equivalent to 1% of Canada's population. The latest Bank of Canada Survey of Consumer Expectations showed that tighter credit conditions and a weaker economic outlook are weighing on consumer sentiment. Retail trade has softened recently, consistent with real wage declines. Dwelling investment continues to slip from high levels registered during the COVID-19 crisis. Higher borrowing costs are weighing on housing market activity, and sales are significantly down on year-ago levels. Housing price declines have been particularly large in markets such as Toronto that experienced strong growth in recent years, but many cities have seen falls in property values in recent months.

Canada's remoteness from hard-hit European markets and its domestic oil and gas capacity continue to help shield the country from acute economic pressures arising from Russia's war of aggression against Ukraine. Energy price rises in particular have been lower than in Europe. Lower petroleum prices has helped to reduce consumer price inflation from its peaks earlier in the year. Growth in the headline consumer price index has declined from 8.1% in June to 6.9% in October (year-on-year). Food and services price inflation remains high, although businesses' inflation expectations eased slightly in the third quarter.

Near-term policy goals are to tame inflation and provide living-cost relief

Further near-term monetary policy tightening is needed to bring consumer price inflation to target. But the central bank will need to remain alert to evolving labour market conditions to avoid overcorrecting. The policy rate is projected to increase by a further 50 basis points by the end of the year. Quantitative tightening will continue to put upward pressure on longer-term interest rates. While remaining contractionary over much of the next two years, the monetary stance is assumed to start to ease in 2024 as price pressures diminish. From a peak of 4.25 per cent, the policy interest rate is assumed to decline by 50 basis points by the end of 2024.

Broad-based fuel tax cuts and energy bill rebates introduced in some provinces have been extended. To help offset the effects of high inflation, the federal government has boosted the goods and services tax credit available to low-income households, a measure worth around 0.1 per cent of GDP. The fiscal cost of provincial and federal living-cost support is modest compared with that provided in other OECD countries.

Inflation will moderate as growth slows

Real GDP growth is projected to slow to 1% in 2023. Weaker conditions in the United States and other major economies will pull down export growth. Higher interest rates are expected to weigh on growth in housing investment and private consumption, despite support from population increases. Business investment will continue to recover from low levels during the COVID-19 crisis, aided by expenditure on health and public transport systems as well as large energy sector projects. Labour demand will ease with slower growth in production, causing employment growth to slow. GDP is projected to grow by 1.3% in 2024. Subdued domestic demand will be offset by stronger export growth due to improving conditions in Canada's main trading partners. Higher unemployment will check wage growth in the next two years, helping to alleviate pressure on consumer prices after declines in the cost of energy, food and housing.

Risks to the near-term outlook are tilted to the downside. Wage pressures might not dissipate as soon as expected. Tackling higher inflation could require larger interest rate increases, putting more pressure on sectors sensitive to borrowing costs, particularly those tied to housing market activity. Home prices may prove more sensitive to higher interest rates than assumed in the projections. A significant deterioration in property values might cause broader financial market instability, with negative wealth effects dragging on consumer spending.

Staying focused on sustainable long-term growth

Canada's federal and provincial governments should scale back and re-target living cost relief as price pressures abate. The withdrawal of relief measures will help to improve fiscal balances and ensure fiscal policy does not work against tighter monetary policy. While navigating the current uncertain macroeconomic environment, Canadian governments should keep sight of structural policy priorities for strengthening long-term growth. Successful implementation of the major federal government initiative to improve access to affordable childcare could support labour force participation. Boosting investment and productivity will depend in part on efforts to address barriers to trade between provinces, which limit cross-border flows of goods and services and impede labour reallocation. To ensure it achieves its ambitious climate targets, the federal government is developing a raft of mitigation policies. Alongside the main aim of reducing emissions, policies should be designed to minimise costs. Improving existing market-based measures such as carbon pricing should be a priority. Support for investment in green technology will help ensure that Canada builds on its comparative advantage as a supplier of low-carbon electricity and goods.

Chile

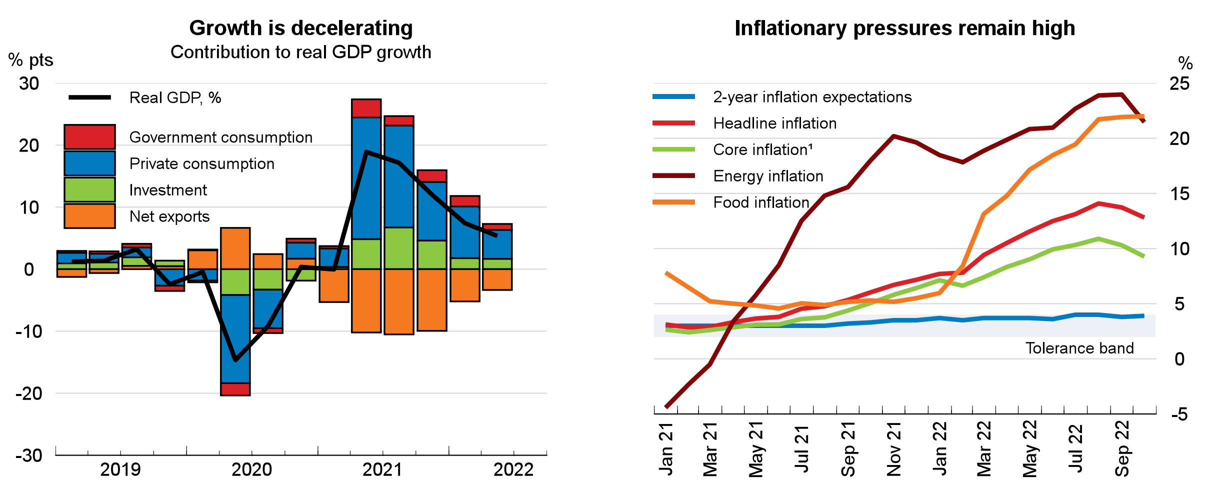
Growth is expected to slow to 1.9% in 2022. A 0.5% contraction of output is projected for 2023, followed by growth of 2.6% in 2024. Tighter financial conditions, the withdrawal of pandemic-related support measures and the eroding effect of inflation on purchasing power will dampen household consumption. Higher interest rates and low business confidence will keep investment subdued. Inflation has recently started to abate and will continue moderating throughout 2023, as the effects of monetary policy tightening on growth and inflation become visible, and will return towards the Central Bank of Chile's 3% target in 2024.

Monetary conditions will need to remain tight to ensure that inflation returns to the target. Adherence to the fiscal rule will allow for moderate deficits in 2023 and 2024, after a surplus in 2022 due to strong revenue collection and the withdrawal of pandemic spending. Reducing barriers to competition and boosting investment in research and development would spur productivity. The envisaged tax reform would make the tax system more progressive and raise additional revenue to strengthen social programmes and public investment.

Activity has cooled down during 2022

Production contracted in the first quarter of 2022 and remained flat in the second. The generous support measures that underpinned a fast recovery from the pandemic have been withdrawn, slowing private and government consumption, and business sentiment has worsened due to inflationary pressures. Monthly activity indicators for retail and manufacturing have remained weak for most of the year, and the unemployment rate has risen steadily, reaching 8% in September. Surging energy and food prices and demand pressures have pushed inflation to historic heights, reaching 12.8% in October, with medium-term inflation expectations close to the upper limit of the central bank's 2-4% tolerance band, suggesting a risk of de-anchoring.

Chile



1. Consumer Price Index excluding energy and food products.
Source: Central Bank of Chile; and INE.

StatLink https://stat.link/u148w9

Chile: Demand, output and prices

Chile	2019	2020	2021	2022	2023	2024
	Current prices CLP billion	Percentage changes, volume (2018 prices)				
GDP at market prices*	195 866.8	-6.2	11.9	1.9	-0.5	2.6
Private consumption	120 661.5	-8.2	20.5	2.1	-4.2	1.8
Government consumption	29 812.2	-4.1	10.4	4.1	2.5	3.2
Gross fixed capital formation	48 074.9	-9.7	18.0	-2.4	-2.0	2.3
Final domestic demand	198 548.5	-8.0	18.3	1.2	-2.8	2.1
Stockbuilding[1]	982.9	-1.6	3.0	1.8	0.1	0.0
Total domestic demand	199 531.4	-9.5	21.7	3.0	-2.6	2.1
Exports of goods and services	54 473.9	-1.2	-1.4	1.6	2.5	3.2
Imports of goods and services	58 138.6	-12.8	31.1	5.2	-3.4	1.8
Net exports[1]	-3 664.6	3.5	-8.9	-1.2	2.2	0.4
Memorandum items						
GDP deflator	_	8.7	7.6	7.5	5.7	3.5
Consumer price index	_	3.0	4.5	11.6	6.9	3.5
Private consumption deflator	_	4.3	5.3	11.5	7.1	3.6
Unemployment rate (% of labour force)	_	10.7	8.8	7.7	7.9	7.6
Central government financial balance (% of GDP)	_	-7.3	-7.7	1.5	-2.8	-2.1
Current account balance (% of GDP)	_	-1.7	-6.5	-8.4	-5.7	-5.3

* Based on seasonal and working-day adjusted quarterly data; may differ from official non-working-day adjusted annual data.
1. Contributions to changes in real GDP, actual amount in the first column.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/2o3h1m

The Russian war of aggression against Ukraine continues to condition inflation and growth developments, both directly, as commodity prices remain high, and indirectly as external demand cools on the back of the energy squeeze and tighter monetary conditions. To soften the impact of higher energy costs, the government provided a one-time cash transfer for winter expenses to vulnerable populations, froze fares on regulated public transportation throughout the country during 2022, and twice increased the subsidy for the existing stabilisation mechanism for fuel prices. Monthly targeted cash transfers to alleviate higher food prices will continue until April 2023.

Commitment to the fiscal rule and restrictive monetary policy in 2023-24

The strong fiscal measures to mitigate the pandemic's adverse effects have been withdrawn, and the government is committed to the fiscal rule. Strong revenue collection and lower expenditure will lead to a budget surplus of 1.5% of GDP in 2022. Revenue will moderate as the economy cools down and inflation abates in 2023, but will pick up as activity gains momentum in 2024. In keeping with the fiscal rule, expenditure will grow moderately in real terms in 2023-24. The deficit is expected to reach 2.8% of GDP in 2023 and 2.1% of GDP in 2024, and public debt will remain below the prudent debt ceiling of 45% of GDP despite the expansionary policy stance in 2023. The Central Bank of Chile has countered inflationary pressures by raising its policy rate, from 0.5% in June 2021 to 11.25% by October 2022. It has stated that the rate will remain at that level as long as necessary to bring inflation back to the target. The projection assumes mild declines in the policy rate in 2024, as inflation wanes.

After a contraction in 2023, growth will resume in 2024

The economy will contract by 0.5% in 2023 and gradually strengthen in 2024. Inflation, tighter financial conditions, and low business confidence will hit consumption and investment during 2023, and weaker growth in trading partners will dampen export growth. As the economy cools, unemployment is projected to increase in 2023, but it will decline in 2024 as growth picks up. Inflation will remain elevated throughout 2023, owing to the lingering effects of high energy prices, but the projected economic downturn and high interest rates will help bring it back to target. Risks appear tilted to the downside. Uncertainty about the path of reform for the Constitution could weaken business and consumer confidence. The war in Ukraine could continue to generate inflationary pressures from energy and commodity prices, which could feed inflation expectations and require further policy tightening, leading to a longer period of below trend growth to bring inflation back to target. Weaker-than-expected growth in Chile's main trading partners, particularly China, would impact exports and investment. On the upside, copper prices could be stronger than assumed, boosting exports. A smooth resolution of the constitutional reform process could strengthen confidence and attract investment.

Policies should aim for higher productivity and a more progressive tax system

Sustainable social and economic progress will require reforms in several areas. Reducing barriers to competition and entrepreneurship, investing more in research and development, fostering female participation in the labour force, and lowering labour costs for formalisation would increase productivity and raise incomes. The tax reform being discussed in Congress, to make the system more progressive, would increase revenues, helping to meet demand for higher social protection and better public services. Achieving Chile's ambitious goal of carbon neutrality by 2050 will require more stringent regulations, and commitments to phase out coal and implement carbon taxes and cap and trade systems to improve price signalling. Taking advantage of the country's remarkable potential for renewable energy, notably solar and wind power, and green hydrogen production would reduce dependence on fossil fuels.

China

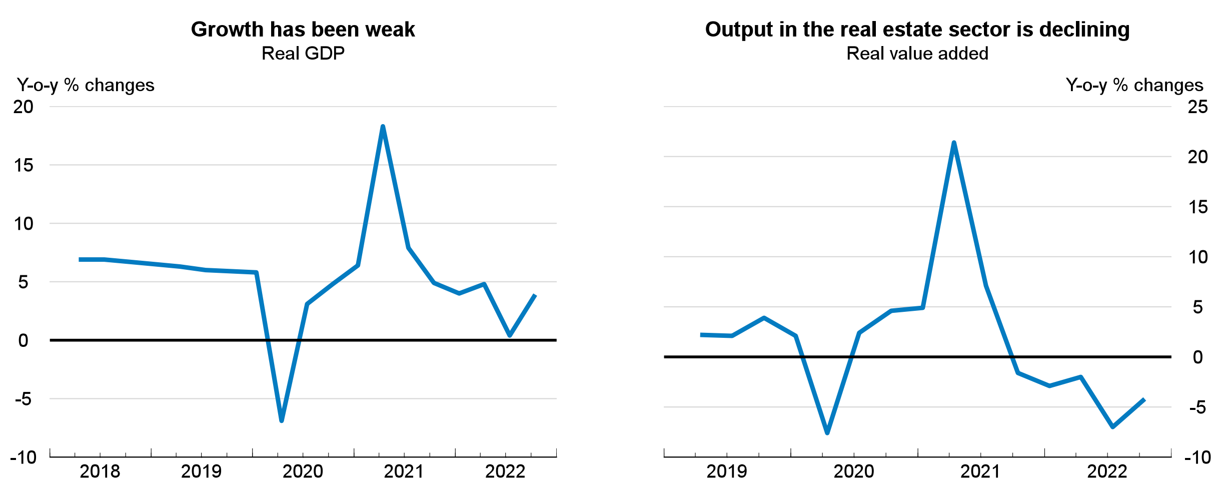
Economic growth will slow to 3.3% in 2022 and rebound to 4.6% in 2023 and 4.1% in 2024. The emergence of the omicron variant has led to recurring waves of lockdowns in 2022, disrupting economic activity. Amid mounting headwinds, growth will be held up by infrastructure investment and supportive measures that moderate the correction in the real estate sector. A pick-up in precautionary savings, spurred by low consumer confidence coupled with inadequate social protection, is holding back a rebalancing of demand towards consumption. Export growth will remain low amid weaker global growth prospects before picking up in 2024. Despite recent fresh food price rises, consumer price inflation will remain benign due to the current measures to manage energy and food prices.

Monetary policy has become more supportive with a series of interest rate and reserve requirement rate cuts. More stringent implementation of credit quotas for presold housing and the lower providence fund lending rate for first homebuyers will mitigate the downturn in the property sector. Fiscal policy will become more supportive with a number of new measures. Tax and various user charge deductions and exemptions for targeted groups will continue to provide some support. A strengthened social safety net would invigorate household consumption.

Disruptions due to pandemic-related lockdowns persist

GDP growth picked up in the third quarter of 2022 to 3.9% year-on-year, following 0.4% year-on-year growth in the second quarter. The rebound partly reflects the easing of COVID-19-related lockdowns as cases fell. Just over 90% of the population is vaccinated by domestically-made vaccines, but these are considered less effective than the ones used in OECD countries. Moreover, a high share of the elderly is unvaccinated. A new COVID-19 management system based on the level of risk has been introduced since July as a transitory measure following hard lockdowns, which allows a faster resumption of activities. Testing requirements for new arrivals are being introduced in a number of cities, erecting internal barriers to economic activities. The restrictions continue to affect the services sector and consumption significantly. Investment growth is firming as infrastructure investment is picking up and new support measures contain the contraction of real estate investment. Stringent regulations governing real estate investment, including the so-called "three red lines" related to financial ratios, caps on real estate lending by bank type and stringent loan-to-value ratios, remain in place.

China 1



Source: CEIC.

StatLink https://stat.link/t9kbpo

China: Demand, output and prices

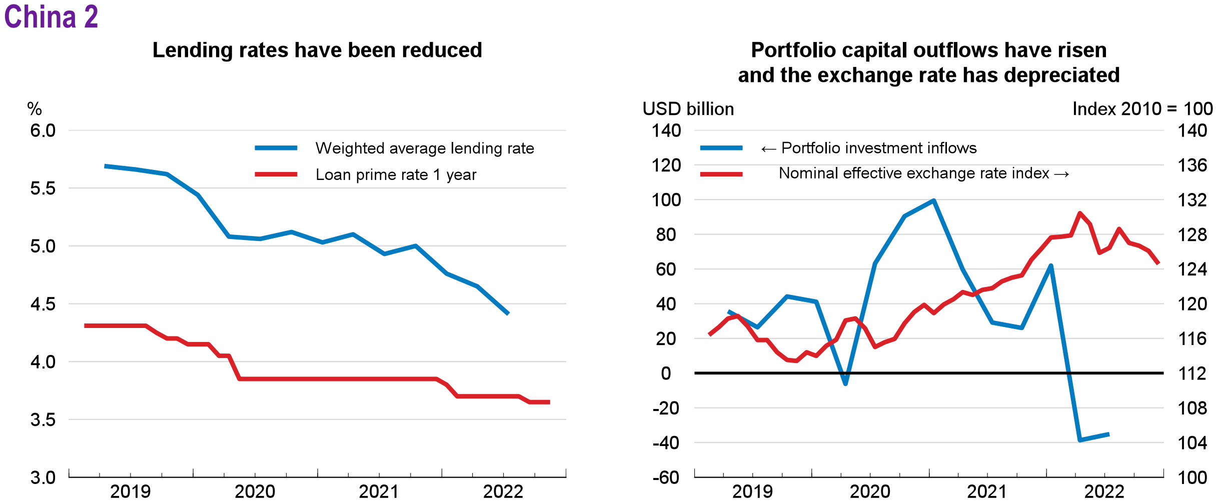
China	2019	2020	2021	2022	2023	2024
	Current prices CNY trillion	Percentage changes, volume (2015 prices)				
GDP at market prices	98.7	2.2	8.1	3.3	4.6	4.1
Total domestic demand	97.7	2.0	6.5	2.5	4.9	4.0
Exports of goods and services	18.2	1.1	15.6	-1.3	2.0	5.3
Imports of goods and services	17.3	-0.3	7.6	-7.2	2.6	5.0
Net exports[1]	0.9	0.3	1.8	0.9	0.0	0.3
Memorandum items						
GDP deflator	_	0.5	4.4	2.7	2.1	1.0
Consumer price index	_	2.5	0.8	2.0	2.2	2.0
General government financial balance[2] (% of GDP)	_	-6.9	-6.6	-6.6	-6.6	-6.8
Headline government financial balance[3] (% of GDP)	_	-3.7	-3.1	-2.9	-3.1	-2.9
Current account balance (% of GDP)	_	1.7	1.8	2.7	2.9	3.1

1. Contributions to changes in real GDP, actual amount in the first column.
2. Encompasses the balances of all four budget accounts (general account, government managed funds, social security funds and the state-owned capital management account).
3. The headline fiscal balance is the official balance defined as the difference between revenues and outlays. Revenues include: general budget revenue, revenue from the central stabilisation fund and sub-national budget adjustment. Outlays include: general budget spending, replenishment of the central stabilisation fund and repayment of principal on sub-national debt.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/574tqi

The impact of Russia's war of aggression against Ukraine has been limited as neither Ukraine nor Russia is an important economic partner for China. Moreover, China is relatively well insulated from global food and energy market shocks due to the structure of consumption, with a large share of food that has limited import content. China's large grain reserves and export restrictions in the form of quotas will continue to mitigate the impact of rising global grain prices on domestic inflation and reduce the risk of shortages. However, lockdown-induced supply-side constraints on fresh food have started to push CPI inflation higher, to 2.8% year-on-year in September. Replacing part of crude oil imports by discounted Urals oil from Russia is also helping to contain inflationary pressure and LNG reserves are being refilled from Russian sources.

China 2



Source: CEIC; and OECD Economic Outlook 112 database.

StatLink https://stat.link/nsegjb

Monetary and fiscal policy have become more supportive

Monetary policy has become more supportive and is assumed to continue providing the necessary liquidity. The required reserves ratio and the benchmark lending rate have been cut twice since late 2021, contributing to a widening interest rate differential with the United States and leading to capital outflows and a depreciation of the currency. To lower lending rates without cutting the benchmark rate and increasing depreciation pressures, major state lenders cut the deposit rate in a coordinated fashion in September for the first time since 2015. Credit supply is ample, but demand is held back by the impacts of the property downturn and zero-COVID-19 policies. The wealth effect of falling property prices is limited, as households tend to hold real estate for longer periods and first-time buyers are benefiting from lower provident fund mortgage lending rates, but heightened uncertainty is boosting precautionary savings and encouraging deleveraging. Enterprise loan demand is constrained by weaker collateral values, weak global economic prospects, tax relief measures, and lockdown-related supply-side disruptions. Corporate debt has stabilised at a very high level of over 150% of GDP. Deleveraging needs to continue and orderly bond defaults would help sharpen risk pricing and gradually remove implicit guarantees.

Fiscal policy will continue to provide support in the form of cuts and deferrals of taxes and charges and spending of reserve funds. Some of the proceeds of special local bonds may be spent only in 2023. A wide range of additional policies are being implemented, including ones outside the public budget. Overall, the measures are worth 1-2% of GDP. Development banks are providing funds financed by bonds to meet own capital requirements in projects, as a lack of funds has appeared to constrain the rolling out of infrastructure projects. Central government-controlled electricity companies will borrow more to fund electricity generation capacity. Sizeable interest subsidies are available to support relending for manufacturing, social services, small and medium-sized companies and individual businesses. The recent requirement for local government investment vehicles to secure the budget prior to carrying out infrastructure projects helps contain contingent liabilities and has constrained their activities.

Activity will recover only slowly

GDP growth will gradually move back up to its underlying pace, which is slowing. Infrastructure investment will pick up, partly offsetting weaker real estate investment. A further rise in corporate defaults will improve risk pricing, but may adversely affect banks, trust companies, as well as other private and institutional investors. Further virus outbreaks and restrictions are likely, constraining consumption, though to a lesser extent than in early 2022 assuming case numbers decline. A stable supply of energy and grains will play a key role in containing price increases, helping headline inflation remain benign.

The sanitary situation remains a key downside risk as outbreaks continue and there are no signs of a full abandonment of zero-COVID-19 policies. Continued defaults and disorderly deleveraging in the overstretched property sector may trigger failures of smaller banks and shadow banking institutions. By contrast, relaxing prudential measures and encouraging investment in real estate may fuel the bubble and cause greater disruptions further down the road.

Structural reforms are needed to reinvigorate the economy

Fundamental reforms to strengthen the social safety net would help to reduce precautionary savings and rebalance demand from investment to consumption. Pension and unemployment insurance coverage should be extended to all. The list of treatments and medicines covered by health insurance should be widened. Levelling the playing field would support private sector investment, which has weakened with the property downturn and has less been able to benefit from infrastructure projects. Reforms to enhance competition would sustain the economic recovery from the pandemic. Administrative monopolies, often with exclusive rights to provide certain goods and services, should be dismantled. Recent measures aiming at creating a single domestic market are a welcome step. Stronger consumer protection could boost competitive pressures. Raising vaccination rates and increasing their effectiveness would reduce disruptions to economic activity. As renewables production has become sustainable and subsidies are being phased out, more funds should be channeled to support the transition to zero net emissions. Small-scale renewables production could be encouraged by allowing producers to sell any excess electricity through the grid. The relocation of energy-intensive industries to regions with ample renewable energy should accelerate. Investment in coal, even if clean, will likely lead to stranded assets, suggesting that investment in new coal-fired power plants should be halted.

Colombia

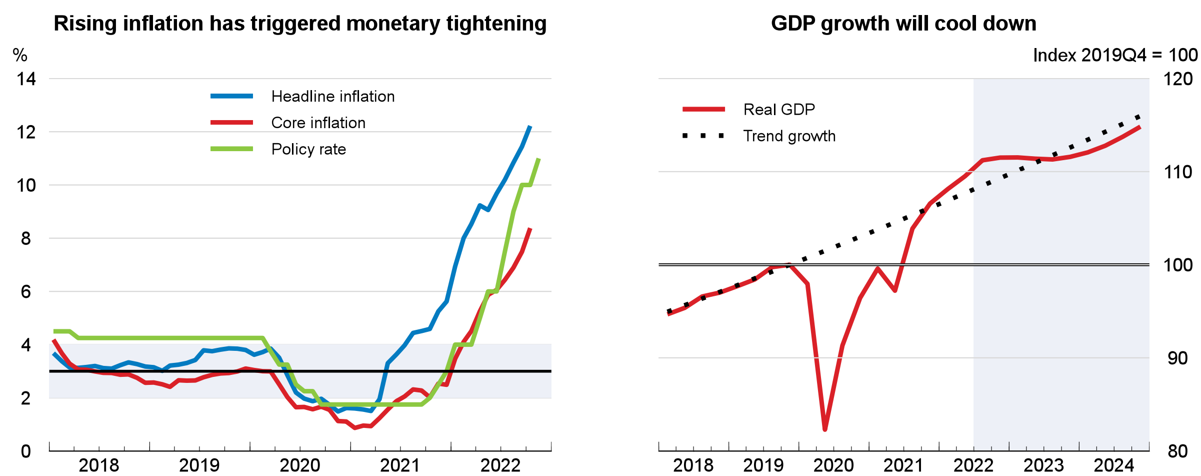
GDP growth is projected to slow sharply from 8.1% in 2022 to 1.2% in 2023, and then edge up to 1.7% in 2024. Consumption and investment will remain subdued as households and firms cope with high inflation and interest rates and uncertainty about the economic outlook and economic policy. Inflation is set to exceed 10% this year but is projected to gradually return to the 2-4% target range by 2024.

Monetary policy is expected to remain tight, with policy rate increases stopping once inflation stabilises, and some policy easing starting in 2024. Boosting public revenues will lower the budget deficit under current spending plans, which include a necessary increase in social expenditure. Widening social protection coverage and simplifying the corporate tax regime are needed for stronger and more inclusive growth.

The economy is cooling down

The economy expanded by more than 10% year-on-year during the first half of 2022, mainly driven by vigorous private consumption on the back of a strong employment recovery and consumer credit growth. The recovery of investment also picked up its pace. In September, the unemployment rate stood at 10.7%, only marginally above pre-pandemic levels. Wages in manufacturing and retail trade were up 10-11% year-on-year in August, slightly above the 10% minimum wage increase in 2022. Consumption fell in the third quarter, and consumer confidence deteriorated further in October. Annual consumer price inflation reached 12.2% in October and is becoming increasingly entrenched, with the core measure at 8.4%. Prices have risen particularly steeply for food and energy, as well as for manufactured goods. One-year ahead inflation expectations are around 7%, and two-year expectations are 4.8%. The depreciation of the peso, which declined almost 10% against the US dollar in October alone, has increased the cost of imports and inflation. Sovereign risk premia have risen significantly since 2021.

Colombia



Source: DANE; BRC; CEIC; and OECD Economic Outlook 112 database.

StatLink https://stat.link/ojez4y

Colombia: Demand, output and prices

Colombia	2019	2020	2021	2022	2023	2024
	Current prices COP trillion	Percentage changes, volume (2015 prices)				
GDP at market prices	1 060.1	-7.0	10.7	8.1	1.2	1.7
Private consumption	727.9	-5.0	14.8	9.5	-1.9	0.7
Government consumption	167.2	-0.6	10.3	4.7	2.6	2.7
Gross fixed capital formation	225.5	-23.3	11.2	11.8	0.8	1.0
Final domestic demand	1 120.6	-8.0	13.5	9.2	-0.8	1.0
Stockbuilding[1]	1.2	0.6	0.3	1.3	0.0	0.0
Total domestic demand	1 121.8	-7.5	13.6	11.0	0.3	1.0
Exports of goods and services	168.2	-22.7	14.8	16.4	4.3	3.6
Imports of goods and services	229.9	-20.5	28.7	25.6	-0.9	-0.2
Net exports[1]	- 61.7	0.8	-3.9	-3.6	1.1	0.8
Memorandum items						
GDP deflator	_	1.4	6.5	13.8	8.9	5.9
Consumer price index	_	2.5	3.5	10.2	9.5	4.8
Core inflation index[2]	_	2.0	1.8	6.4	7.7	4.7
Unemployment rate (% of labour force)	_	16.5	13.8	11.1	11.7	12.6
Current account balance (% of GDP)	_	-3.5	-5.6	-5.4	-3.9	-3.5

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding primary food, utilities and fuels.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/dspotg

Colombia's gas and electricity markets are decoupled from Europe. Regulated prices of electricity, most of which is produced from hydropower, will be cut by 4-8% in 2023. The energy crisis is impacting Colombia mainly through the price of oil (which makes up a third of its exports), boosting exports and fiscal revenue. This revenue will help replenish the accumulated deficit of the fuel price stabilisation fund (2% of GDP in 2022 and 1.5% in 2023), a pre-existing scheme which is now used to limit the pass-through to domestic fuel prices. In addition, small gradual increases in the regulated petrol price have taken effect from September.

Fiscal and monetary policy will remain tight

Monetary policy has been significantly tightened during 2022, with seven consecutive increases of at least 100 basis points each. The Central Bank of Colombia is expected to continue raising policy rates by an additional 150 basis points until early next year and then maintain them unchanged until mid-2024. Improving fiscal outcomes will shore up confidence, after several years of large fiscal deficits. Public debt reached 61% of GDP in 2021, above the medium-term debt anchor of 55% stipulated in the fiscal rule. Central government expenditure will increase by 15% in value terms in 2023, due to welcome increases in social spending. Boosting revenues would enable gradual fiscal consolidation while keeping space to support the most vulnerable. Two tax reforms, one approved in 2021 and one passed by Congress in October, are expected to bring close to 3% of GDP of additional revenue once fully implemented by 2024.

Growth is projected to weaken

The economy will slow significantly in 2023 and 2024. Domestic demand will weaken in 2023, as high inflation, interest rates and uncertainty weigh on consumers and investors. Exports will keep growing albeit more slowly, benefitting from improved competitiveness and the demand in advanced economies for non-Russian oil. Import penetration will decline towards its pre-pandemic level. Consumption and investment will pick up during 2024 when inflation declines more markedly and monetary policy starts to ease. Inflation will fall to the upper limit of the target band (4%) by the end of the projection horizon. Slower disinflation, or a stronger-than-expected rise in interest rates in advanced economies, would prompt the central bank to push interest rates higher and for longer. On the upside, higher oil prices would bring additional fiscal and export revenues.

Streamlining the tax and benefit system and supporting the green transition

Increasing the coverage and amount of cash benefit and pension programmes would reduce poverty and inequalities. There is further scope to improve the design of the tax and social protection system by replacing social security charges on formal sector wages with general tax revenues to reduce informality. Reducing tariff and non-tariff barriers to trade, starting with those items where the current barriers are highest, would boost productivity. Gradually reducing dependence on oil and gas is needed for the green transition. It would need to be accompanied by more investment in renewables and the phasing out of fossil fuel subsidies to lower domestic consumption. This would help lower emissions and diversify the economy. Defining a timeline for raising and expanding the carbon tax, while channelling part of the revenues towards low-income households, would also support the green transition.

Costa Rica

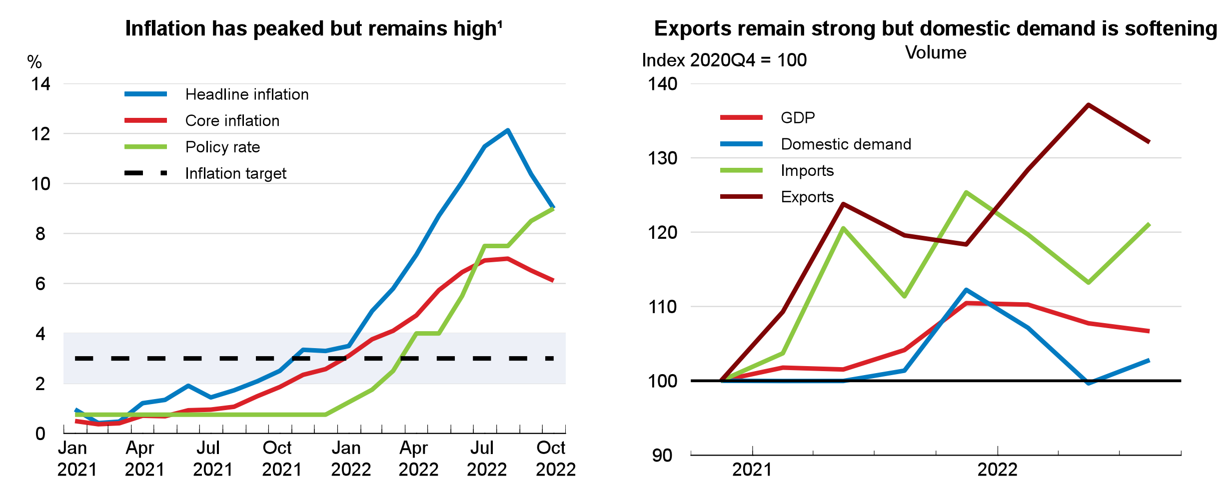
GDP will grow by 2.3% in 2023 and 3.7% in 2024. High inflation and a tight monetary policy stance will hold back private consumption in 2023, and fiscal restraint will contain public spending. Exports will be hampered by weaker global growth in 2023 but gain strength in 2024. Annual inflation peaked at 12% recently but is set to decline to 4.2% in year-average terms by 2024, still above the 3% target.

The fiscal outlook has improved due to the full implementation of the fiscal rule and better-than-expected revenues. However, with public debt at 70% of GDP and large interest payments, the fiscal stance will need to remain prudent. The monetary policy tightening that started in December 2021 to contain inflationary pressures and prevent the de-anchoring of inflation expectations is expected to continue until the end of 2022. Improving the quality and efficiency of education, by providing more targeted support to students with learning gaps and increasing the number of science graduates, would support higher growth and equity.

Exports have been driving growth amid high inflation

Domestic demand softened in the first three quarters of 2022, despite buoyant ICT activity, as high inflation and monetary policy tightening weighed on private consumption and public investment remained low. Exports continue to support GDP growth, demand for manufacturing output remains solid and tourism activity is approaching pre-pandemic levels.

Costa Rica



1. The horizontal dashed black line indicates the target inflation rate of monetary policy. The shaded area reports the tolerance band around the inflation target (+2% to +4%). Headline and core inflation indicate, respectively, the headline consumer price inflation rate and the core consumer price inflation rate, which excludes food and energy.
Source: Banco Central de Costa Rica.

StatLink https://stat.link/fb5a8q

Costa Rica: Demand, output and prices

Costa Rica	2019	2020	2021	2022	2023	2024
	Current prices CRC trillion	Percentage changes, volume (2017 prices)				
GDP at market prices	37.8	-4.3	7.8	4.3	2.3	3.7
Private consumption	24.3	-6.9	7.0	3.6	2.3	2.7
Government consumption	6.3	0.8	1.7	2.1	0.1	0.8
Gross fixed capital formation	6.1	-3.4	11.0	1.6	-0.5	5.5
Final domestic demand	36.8	-5.0	6.6	3.0	1.4	2.9
Stockbuilding[1]	- 0.1	0.2	1.1	-0.8	0.6	0.0
Total domestic demand	36.7	-4.8	7.8	1.8	1.7	2.8
Exports of goods and services	13.0	-10.6	15.9	12.2	8.8	9.1
Imports of goods and services	11.9	-12.9	16.9	5.5	8.5	7.5
Net exports[1]	1.1	0.4	0.3	2.5	0.6	1.1
Memorandum items						
GDP deflator	_	0.8	2.0	7.8	6.4	4.2
Consumer price index	_	0.7	1.7	8.8	6.9	4.2
Core inflation index[2]	_	1.3	0.9	4.5	5.8	4.2
Unemployment rate (% of labour force)	_	19.5	16.4	12.2	11.4	11.1
Current account balance (% of GDP)	_	-1.1	-3.3	-4.4	-3.8	-2.7

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/4kszil

Headline and core inflation stood at 9% (year-on-year) and 6.1%, respectively, in October, above the 3% inflation target but below the peak recorded in August. Domestic cost pressures remain contained and real wages decreased by 3.8% in August with respect to December 2021. Median two-year ahead household inflation expectations rose to 5.4% in October, from 5% a month earlier, and remain above the upper end of the inflation tolerance band of 2-4%. To mitigate the impact of the increase in energy and food prices the fuel tax was frozen for six months in July (with an estimated cost of 0.05% of 2021 GDP) and a monthly subsidy of around USD 90 for poor households, renewable for up to three months, was established in November (with an estimated cost of 0.05% of 2021 GDP).

Fiscal prudence and tight monetary policy will continue

Adherence to the fiscal rule is assumed to keep public spending in check, making it possible to meet the government's fiscal targets over the projection horizon. Central government net lending is projected to fall to 4% in 2022, 2.6% in 2023 and 2.2% in 2024. Under these assumptions, public debt will peak at around 70% in 2022 before starting to decline. Monetary policy tightening is assumed to continue until the end of 2022 with the policy rate reaching 9%. Monetary policy is assumed to start easing in late 2023 with the inflation rate nearing the upper bound of the 2-4% inflation tolerance band. The policy rate is expected to be cut by 50 basis points in 2023Q4 and 2024Q1, and by 25 basis points in each of the following three quarters, reaching 7.25% by 2024Q4.

Growth will gradually strengthen after slowing in 2023

Growth will slow to 2.3% in 2023 before strengthening to 3.7% in 2024 as the global economy recovers. High and persistent inflation and a tight monetary policy stance will hit household real disposable incomes, softening private consumption in the second half of 2022 and in 2023, and limiting the positive impact of the assumed full recovery of tourism on economic activity and employment. Export growth will slow in 2023, but gain traction in 2024 as global demand strengthens. Foreign direct investment inflows are assumed to continue over the projection period, while public investment will remain weak. Inflation is projected to fall to 6.9% in 2023 and to 4.2% in 2024, as external inflationary pressures wear off and domestic cost pressures are contained by a tight monetary policy stance. The high degree of dollarisation of Costa Rica’s economy exposes the country to external funding and exchange rate risks. On the upside, the renewed efforts to deepen trade integration could bring stronger exports.

Pushing ahead with structural reform would increase growth and equity

Continuing to implement structural reforms initiated during the OECD accession process would increase growth and economic resilience and reduce income inequalities. Establishing virtual one-stop shops could reduce the high administrative burden to start a company. Improving the quality and efficiency of education, by providing more targeted support to students with learning gaps and increasing the number of science graduates, would support higher growth and equity. To achieve net carbon neutrality by 2050, Costa Rica should reduce emissions in the transport sector by strengthening the public transport network and expanding the fleet of zero-emission vehicles, as well as maintaining the 100% share of electricity produced from renewable sources.

Croatia

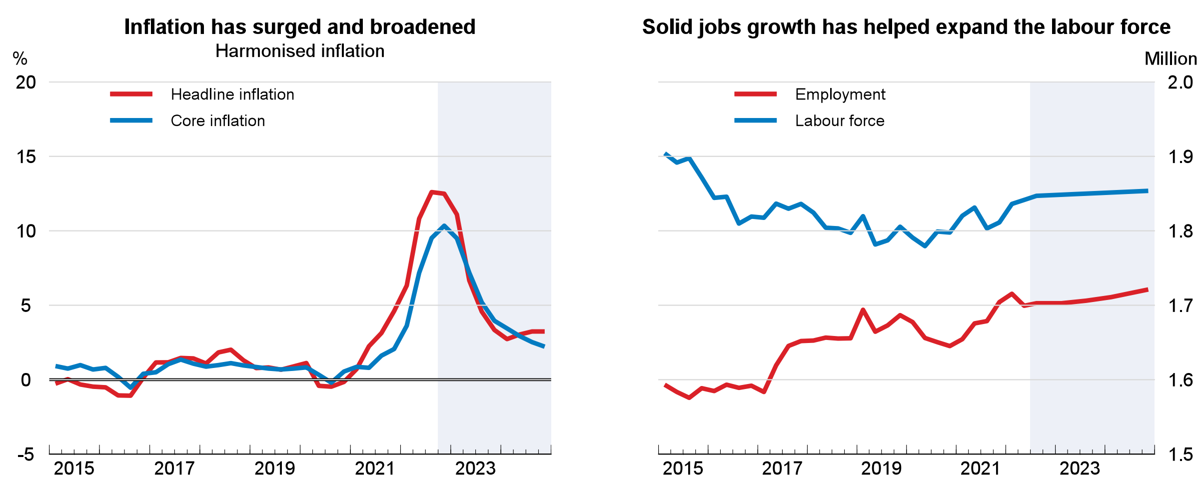
The energy and price shocks are projected to sharply slow Croatia's growth from 6.4% in 2022 to 0.8% in 2023. Rising exports, employment and wages are projected to support incomes as energy prices and supplies stabilise, lifting output growth to 1.5% in 2024. Faster implementation of EU-funded projects and Croatia's integration into the euro and Schengen visa areas will encourage investment. Labour market tightness, especially for specialised skills, and scarce spare capacity risk amplifying wage and cost pressures.

Substantial fiscal measures offset the drag of scarce and more expensive energy on household well-being, production and exports, mostly by limiting price rises, but could add to demand pressures. Making support measures more targeted towards vulnerable consumers and designing them so as to maintain incentives for energy savings would improve fiscal sustainability and raise Croatia's lagging energy efficiency. Continuing fiscal consolidation would reduce demand pressures and free resources to address other challenges to sustained growth, such as skills shortages.

Surging energy prices and uncertainty are stalling the strong rebound

GDP grew strongly in the first half of 2022, supported by the rebound in tourism and other exports, and strong household consumption. Tourist receipts in the year to August 2022 exceeded the previous record in 2019. High-frequency indicators suggest that this momentum stalled in the third quarter of 2022, as heightened international uncertainty amplified the drag from surging energy and other prices and supply disruptions. By August 2022, industrial production had retreated from the historic highs achieved earlier in the year. Retail spending also fell, as slowing employment growth and strong consumer price inflation, reaching 12.6% in September 2022, compressed households' real incomes. Inflation, initially led by energy and food prices, has broadened into other goods and services, lifting core inflation above the headline rate.

Croatia



Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/ayblm1

Croatia: Demand, output and prices

Croatia	2019	2020	2021	2022	2023	2024
	Current prices HRK billion	Percentage changes, volume (2015 prices)				
GDP at market prices	412.2	-7.8	9.8	6.4	0.8	1.5
Private consumption	234.7	-5.3	9.9	3.5	0.6	1.4
Government consumption	85.0	4.2	3.2	2.3	3.7	0.6
Gross fixed capital formation	88.7	-5.9	7.5	5.6	1.1	2.8
Final domestic demand	408.4	-3.4	8.1	4.0	1.4	1.5
Stockbuilding[1]	7.3	0.7	-4.7	0.8	-0.4	0.0
Total domestic demand	415.7	-0.7	7.1	3.7	1.0	1.4
Exports of goods and services	207.0	-19.1	27.8	27.3	3.0	2.3
Imports of goods and services	210.5	-12.1	14.4	24.2	2.7	2.1
Net exports[1]	- 3.5	-3.4	5.0	1.3	0.0	0.0
Memorandum items						
GDP deflator	_	0.0	3.1	12.0	10.3	4.0
Harmonised index of consumer prices	_	0.0	2.7	10.6	6.3	3.1
Harmonised index of core inflation[2]	_	0.4	1.3	7.7	6.4	2.8
Unemployment rate (% of labour force)	_	7.5	7.6	7.5	7.8	7.4
Household saving ratio, net (% of disposable income)	_	9.2	7.6	5.4	5.7	5.6
General government financial balance (% of GDP)	_	-7.3	-2.6	-2.1	-2.3	-1.6
General government gross debt (% of GDP)	_	106.9	100.2	95.3	93.7	93.4
General government debt, Maastricht definition[3] (% of GDP)	_	87.0	79.9	75.0	73.4	73.1
Current account balance (% of GDP)	_	-0.1	0.4	-1.4	-1.5	-0.9

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/vid2mz

Croatia sourced a modest share of its energy from Russia prior to 2022, thanks to extensive renewable energy capacity and its expanding energy import infrastructure. Nonetheless Croatia is exposed to surging European wholesale energy prices. To offset these, it has introduced measures worth at least 3.7% of annual GDP, including: tax relief and excise rate cuts (2.6% of GDP); income support for vulnerable groups (0.8% of GDP); and support for energy renovations (0.3% of GDP). In addition, support for loans and grants to businesses is valued at 1.7% of GDP. It has increased social benefits for pensioners and other vulnerable groups, and is raising civil servants' wages. Most of these measures are scheduled to expire in March 2023, but are expected to be extended for an additional 12 months as the energy crisis persists.

Fiscal and monetary conditions will remain supportive

Strong growth in activity and prices in 2022 buoyed revenues, enabling the government to increase transfers and other spending. The government expects the budget deficit to be near 2.4% of GDP in 2023, as it expects revenue growth to slow while it maintains increased spending on energy support measures and public investment. However, the carry-over in revenues from stronger growth in 2022, and rising construction costs which add to the challenges of implementing planned investment projects, may lead to a smaller deficit. Croatia's integration into the euro area on 1 January 2023 will support access to finance and reduce its cost, eliminating the exchange rate risk of euro-denominated loans. Rating agencies are upgrading Croatia's sovereign debt rating and spreads on public debt may fall further. For private borrowers, this could partly offset rising euro area interest rates.

Rising investment will rekindle growth

Weaker external conditions, the loss of real incomes, shortages and uncertainty are projected to slow consumption, investment and exports in the near-term. With reduced pressures on capacity and recruitment, inflation should ease. From 2023, supplies and prices of energy are expected to stabilise, while increased public spending and substantial wage rises help to rebuild households' real incomes. Investment is projected to lead the pick-up, supported by European funds disbursements, and as Croatia attracts greater financing and foreign direct investment following its integration into the euro and Schengen visa areas. The expiry of energy support measures, expected in 2024, will lift headline inflation temporarily. Inadequate energy supplies, especially over the coming winters, would risk deeper contractions in activity and spending. Improving competitiveness, fiscal credibility, and the full implementation of Croatia's recovery and resilience plan are central to raising investment. This would be imperilled if wage or price growth outpace peers, fiscal consolidation falls short of medium-term objectives, or the planned improvements to the business environment are not achieved.

Addressing skills shortages and improving the economy's resilience will help sustain growth

As Croatia integrates into the euro area, further reductions of the fiscal deficit would improve the sustainability of growth and reduce the risks from capacity constraints and declining competitiveness. Shifting from fiscal measures that cap energy prices to targeted help for households and firms to reduce their energy needs – such as renovating buildings or improving the efficiency of transport and other equipment – would reduce exposure to energy price fluctuations, reduce the fiscal costs of support measures and improve environmental quality. Raising participation in quality active labour market programmes, and reforming pension and retirement arrangements to encourage older workers to continue contributing to the workforce, would help address labour market pressures. In the longer term, raising participation in high-quality vocational education programmes would help to ensure that adults have the skills to benefit from emerging, higher productivity opportunities.

Czech Republic

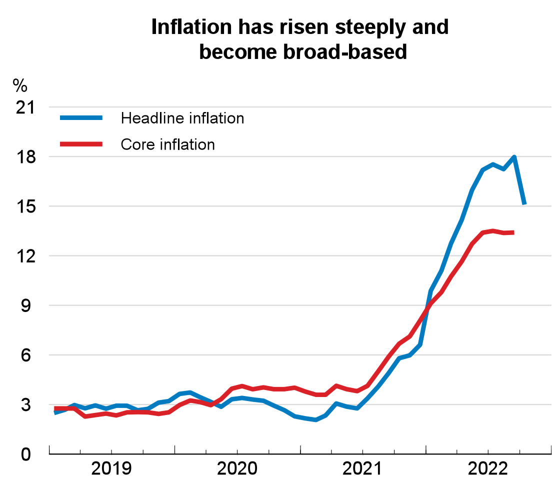
GDP growth will slow from 2.4% in 2022 to -0.1% in 2023, before picking up to 2.4% in 2024. Higher energy and commodity prices and supply disruptions to gas and oil imports from Russia have triggered steep rises in the cost of living and a risk of energy shortages. Lower global growth, persistent constraints in global supply chains and tight financing conditions will hold back activity in 2023. Inflation will start subsiding in 2023 but will remain well above the 2% target. The unemployment rate will remain low, at under 3%.

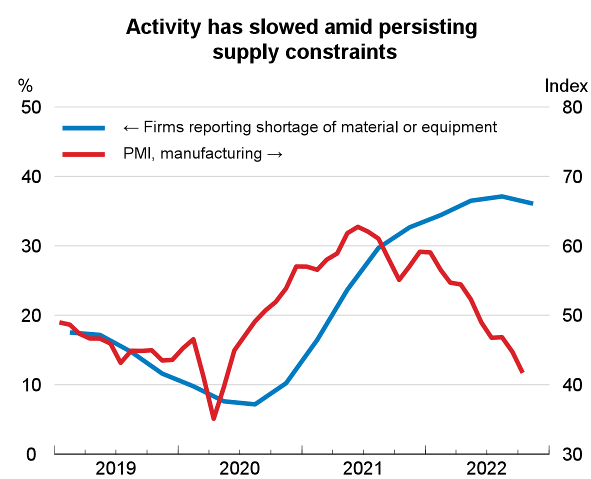
Macroeconomic policy needs to maintain a tight and well-coordinated stance until inflation expectations are firmly under control. Steady consolidation of the structural fiscal balance should be started, which will also serve to rebuild fiscal buffers. Measures to counter high energy prices should be well-targeted and temporary while preserving incentives for energy savings. Strengthening labour supply and accelerating the green transition would support growth and make it more sustainable.

The economy has slowed markedly

According to the preliminary estimate, GDP fell by 0.4% in the third quarter of 2022. Russia's war of aggression against Ukraine has exacerbated problems in global supply chains and increased pressures on energy and commodity prices. Exports and activity, notably in manufacturing and construction, are constrained by disruptions in the supply of important raw materials and components. Growth in trading partners is slowing significantly. Inflation has risen to very high levels – 15.1% in October 2022 – and become broad-based, squeezing real household incomes. High uncertainty and the looming energy crisis have resulted in large falls in consumer and business sentiment, lowering domestic demand. The labour market remains tight and the unemployment rate low, at 2.2% in the third quarter of 2022. However real wages have fallen sharply.

Czech Republic





Source: Czech Statistical Office; Czech National Bank; and S&P Global.

StatLink https://stat.link/cdu5lp

Czech Republic: Demand, output and prices

Czech Republic	2019	2020	2021	2022	2023	2024
	Current prices CZK billion	Percentage changes, volume (2015 prices)				
GDP at market prices	5 793.9	-5.5	3.5	2.4	-0.1	2.4
Private consumption	2 712.0	-7.2	4.0	0.5	-0.5	2.4
Government consumption	1 134.5	4.2	1.5	0.2	1.0	1.4
Gross fixed capital formation	1 568.2	-6.0	0.6	4.9	-0.9	2.8
Final domestic demand	5 414.7	-4.5	2.5	1.7	-0.3	2.3
Stockbuilding[1]	29.8	-0.9	4.8	1.5	0.0	0.0
Total domestic demand	5 444.5	-5.4	7.6	3.1	-0.2	2.2
Exports of goods and services	4 284.6	-8.1	6.8	3.1	1.6	3.9
Imports of goods and services	3 935.2	-8.2	13.2	4.1	1.4	3.6
Net exports[1]	349.4	-0.4	-3.6	-0.6	0.1	0.2
Memorandum items						
GDP deflator	_	4.3	3.3	8.7	8.8	4.2
Consumer price index	_	3.2	3.8	15.2	9.9	4.1
Core inflation index[2]	_	3.6	5.0	12.4	10.0	4.1
Unemployment rate (% of labour force)	_	2.5	2.8	2.3	2.6	2.8
Household saving ratio, net (% of disposable income)	_	16.8	15.6	8.6	7.6	8.5
General government financial balance (% of GDP)	_	-5.8	-5.1	-4.5	-4.1	-2.4
General government gross debt (% of GDP)	_	47.0	48.5	51.7	54.5	55.7
General government debt, Maastricht definition[3] (% of GDP)	_	37.6	42.0	45.2	48.0	49.3
Current account balance (% of GDP)	_	2.0	-0.8	-4.0	-2.9	-3.1

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/9wrfgn

The Czech economy relied heavily on energy imports from Russia prior to the war, with virtually all gas originating from Russia. Efforts have continued to fill gas storage capacity sufficiently and find alternative sources. With usual winter temperatures the current supply should suffice for the 2022-23 winter, and the projections assume no major supply issues over the 2023-24 winter. The government has introduced measures to cushion the impact of high energy prices, including income support to households and SMEs, price caps on energy, and temporary cuts in excise taxes on fuels, partly financed by a newly introduced tax on excess profits of energy producers, traders and banks. The Czech Republic has witnessed a large inflow of Ukrainian refugees. According to the United Nations High Commission for Refugees, at end-October, around 455 000 refugees were recorded in the country, which is the highest ratio of all receiving countries and equivalent to 4.3% of the total population. Provision of basic services and cash transfers add to fiscal costs. At the same time, about a third of refugees of working age were employed as of late August 2022, easing slightly the tightness of the labour market and reducing reliance on government aid.

A tight macroeconomic policy stance is warranted

The central bank has tightened monetary policy significantly to counter rapid increases in core inflation and rising inflation expectations. Between June 2021 and June 2022, it raised the policy interest rate from 0.25% to 7%, after which it paused its tightening cycle. It also intervened more actively on the foreign exchange market to reduce exchange rate volatility and stave off depreciation pressures on the koruna.

The projections assume that the policy interest rate rises further to 7.75% in the fourth quarter of 2022. A gradual easing cycle is projected to start in the fourth quarter of 2023. Fiscal policy has been providing stimulus over recent years to support the economy during the pandemic, but too many measures have been untargeted and with a permanent impact on the government structural balance. The fiscal situation has deteriorated, fiscal rules have been loosened and a credible fiscal consolidation plan has yet to be presented. Recently introduced measures to cushion the impact of high energy prices are assumed to stay in place over the projection horizon, contingent on the evolution of market prices. The general government deficit will be at 4.1% of GDP in 2023 and fall to 2.4% in 2024, while public debt will continue rising.

High uncertainty will continue to weigh on growth

Activity will be held back in 2023 by high energy prices and continued high uncertainty. Private consumption will remain subdued due to rising prices and depleted household savings. Uncertainty and tighter financing conditions will hold down private investment, but public investment will be boosted by EU financing. With eased global supply disruptions, growth will pick up in 2024 as international trade growth strengthens. Inflation will start falling from currently very high levels, as tightened financing conditions dampen domestic demand. Unemployment will rise slightly, but the labour market will remain tight over the projection horizon. Risks include rises in commodity and energy prices, a strong depreciation of the koruna and de-anchored inflation expectations, each of which would further fuel inflation and make it more persistent. A breakdown of trust among social partners would likely result in a destabilising wage-price spiral. On the other hand, a deeper recession and lower confidence would lower inflation more quickly.

Strengthening labour supply and accelerating the green transition would support growth

The central bank has appropriately tightened monetary policy, and interest rates will have to remain elevated until inflationary pressures are well controlled. Fiscal policy should avoid stimulating aggregate demand in order not to undermine monetary policy. Fiscal support measures to cushion rising energy prices should be better targeted and maintain incentives for energy savings. Boosting domestic labour supply (through increased employment of mothers and older workers), better matching skills provision with skills needs and using immigration policy more effectively would help attract and retain skilled labour. Investment into renewable energy and electric vehicle mobility would reduce reliance on the gas and oil markets and help the recovery. Incentives to boost energy efficiency, including for heating and insulation in the residential sector, should be strengthened to reduce reliance on coal.

Denmark

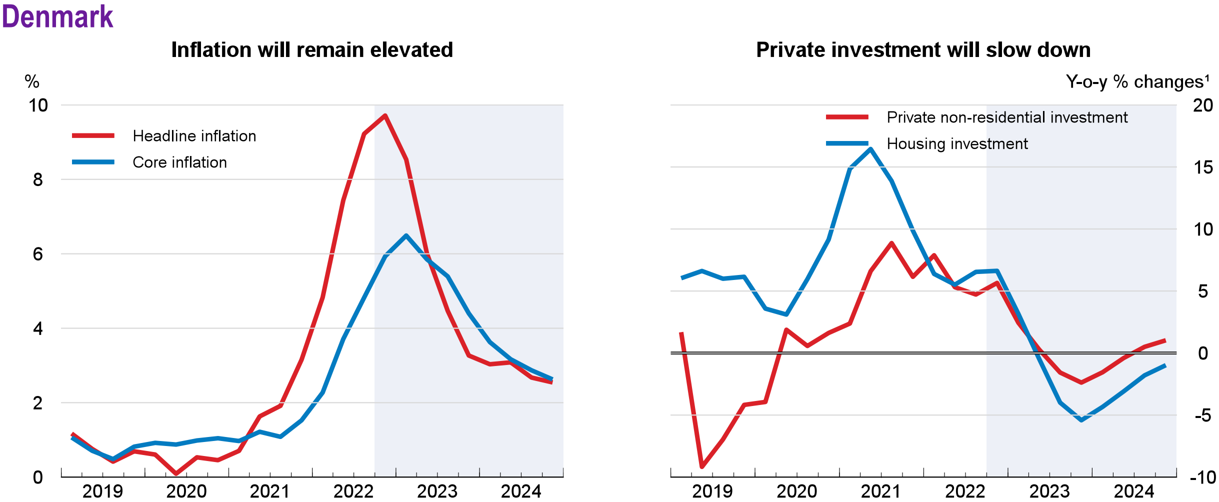
GDP growth is projected to slow to 0.1% in 2023, before recovering to 1.1% in 2024. High inflation and falling housing prices will erode household purchasing power. Weak activity in the main trading partners and rising costs will weigh on business investment and exports. Inflation is expected to recede from a year average of around 8% in 2022 to below 3% in 2024. Main risks to the outlook include stronger supply disruptions and persistent shortages on the labour market that would further increase prices and reduce activity.

Compared to other European countries, support measures in response to rising energy prices have been limited so far. They should remain targeted on vulnerable households as the economy is close to full employment and additional stimulus could add to inflationary pressures. Fiscal policy is expected to be slightly restrictive in 2023 and 2024, but further tightening should be considered if stronger price pressures emerge. Clear price signals and support for energy efficiency investments should accelerate the green transition and further reduce dependence on fossil fuels.

The economy has cooled

The economy is showing signs of a slowdown in the second half of the year on the back of rising costs, weaker international trade and high uncertainty. Industrial production has been strong, contrasting with neighbouring countries, but capacity utilisation has declined. Business expectations have deteriorated significantly, especially in construction and retail trade. While still well below its pre-crisis level, the unemployment rate has started to rise, and job postings have decelerated. Consumer confidence dropped to a record low, following the rapid surge in prices. Consumer price inflation has broadened and reached 10% in October, its highest level since the 1980s. The pass-through to wages and the increase in inflation expectations have remained contained so far. After two years of high sales and price growth, the housing market has weakened, reflecting tightening financing conditions.

Denmark



1. 12-months moving average.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/6ac9if

Denmark: Demand, output and prices

Denmark	2019 Current prices DKK billion	2020	2021	2022	2023	2024
		Percentage changes, volume (2010 prices)				
GDP at market prices	2 311.0	-2.0	4.9	3.1	0.1	1.1
Private consumption	1 084.9	-1.3	4.1	-1.4	0.0	1.2
Government consumption	557.6	-1.4	4.2	0.7	-0.7	0.7
Gross fixed capital formation	490.9	5.1	6.2	4.9	-2.1	0.6
Final domestic demand	2 133.4	0.1	4.6	0.7	-0.7	0.9
Stockbuilding[1]	14.2	-0.2	0.0	1.7	0.4	0.0
Total domestic demand	2 147.6	-0.2	4.5	2.6	-0.3	0.9
Exports of goods and services	1 355.3	-6.3	8.0	5.5	2.3	2.9
Imports of goods and services	1 191.9	-3.5	8.0	3.7	1.3	2.8
Net exports[1]	163.4	-1.9	0.5	1.4	0.8	0.3
Memorandum items						
GDP deflator	_	2.6	2.8	8.4	3.9	2.2
Consumer price index	_	0.4	1.9	7.8	5.5	2.8
Core inflation index[2]	_	1.0	1.2	4.2	5.5	3.1
Unemployment rate (% of labour force)	_	5.8	5.2	4.5	5.7	5.6
Household saving ratio, net (% of disposable income)	_	6.1	5.5	5.3	5.1	5.7
General government financial balance (% of GDP)	_	0.2	3.6	2.3	1.5	1.5
General government gross debt (% of GDP)	_	58.9	50.6	49.6	48.6	47.6
General government debt, Maastricht definition[3] (% of GDP)	_	42.2	36.6	35.7	34.6	33.6
Current account balance (% of GDP)	_	7.9	9.0	11.4	10.5	10.0

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/gum3dt

Domestic production of oil and gas and relatively low fossil fuel consumption limit the risk of energy supply disruptions. Further development of domestic energy production, including the reopening of the Tyra gas field in 2024, will help to reduce energy imports further. Nevertheless, energy prices have increased dramatically over the past year, by around 130% for gas and 85% for electricity as of October. Those detached from the labour market have been more severely affected by price increases, not least because social benefits that are indexed to past wages adjust to inflation with delays.

Fiscal and monetary policies will remain prudent

Further monetary policy tightening will contribute to moderating inflation. In September 2022, the central bank ended more than ten years of negative interest rates. It is expected to mirror ECB decisions to maintain the peg to the euro and thus to progressively increase its policy rate to around 3.5% in 2023. Fiscal policy is projected to be slightly restrictive over the next two years, despite rising defence spending. Support to energy consumers is set to remain limited compared to other EU countries, at around 0.3% of GDP for 2022 and 2023, and mainly targeted at the most vulnerable. Measures include heating checks for disadvantaged households, checks for low-income pensioners, and a temporary reduction of the electricity tax. A voluntary loan scheme allows consumers to postpone the payment of part of their energy bills and repay their debt to energy providers over a period of four years. Support measures to energy consumers are fully funded, notably by cuts in public investment. The government surplus is projected to reach around 1.5% of GDP in both 2023 and 2024 with debt remaining low.

Strong inflation will dent economic growth

GDP growth is projected to fall to 0.1% in 2023 before recovering to 1.1% in 2024. Inflation will dent household disposable income and the saving ratio will fall moderately due to pressures on spending power and uncertainty. Rising interest rates and debt servicing costs will dampen private investment. Despite easing pressures on supply chains and robust demand for major exported goods and services (such as freight transport, pharmaceuticals, environmental goods), weaker growth in trading partners will weigh on foreign demand. Inflation is expected to gradually decelerate to 5.5% in 2023 and 2.8% in 2024, on the back of mounting spare capacity and reduced supply bottlenecks. Wages will grow only moderately amidst rising unemployment. The main risks to the outlook include a worsening of the energy crisis that would induce stronger disruptions and production stoppages in neighbouring countries and a steeper economic downturn. De-anchoring of inflation expectations and lingering tensions on the labour market could trigger larger-than-projected increases in wages and higher second-round inflation. Sharper falls in housing prices and equity to well below pre-crisis levels could dampen domestic demand.

Containing inflationary pressures is a priority

While continuing to protect the most vulnerable, Denmark should maintain prudent fiscal policy to contain inflationary pressures. It should also keep pursuing its ambitious environmental objectives to reduce dependency on fossil fuels. Strong price signals are key for the decarbonisation of the economy and energy efficiency gains. Support measures should continue to target those most severely affected by inflation and broad prices and tax cuts should be avoided. The recent agreement on the green tax reform and the establishment of a green fund in June 2022 are steps in the right direction, but more can be done by further clarifying the climate strategy, reducing policy uncertainty, and making emission pricing more uniform.

Estonia

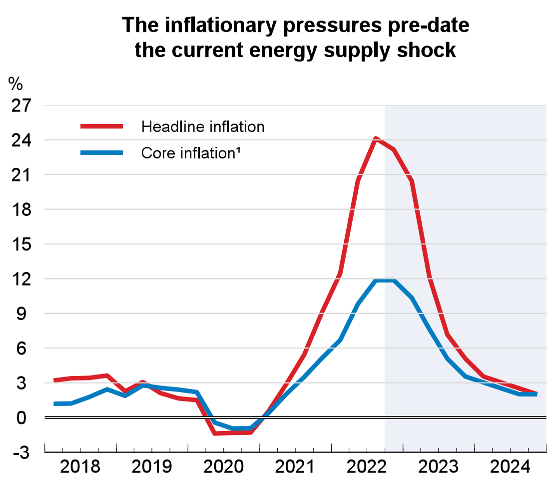
The economy will weaken considerably as the impact of Russia's war of aggression against Ukraine becomes more broad-based. Real GDP growth is projected to slow to 0.5% in 2023 due to weaker domestic demand and a deteriorating external environment, despite support from fiscal policy. Growth will rebound in 2024 to 3.2%. Inflation should peak by the end of this year but remain elevated in 2023 and decrease only as spare capacity in the economy increases.

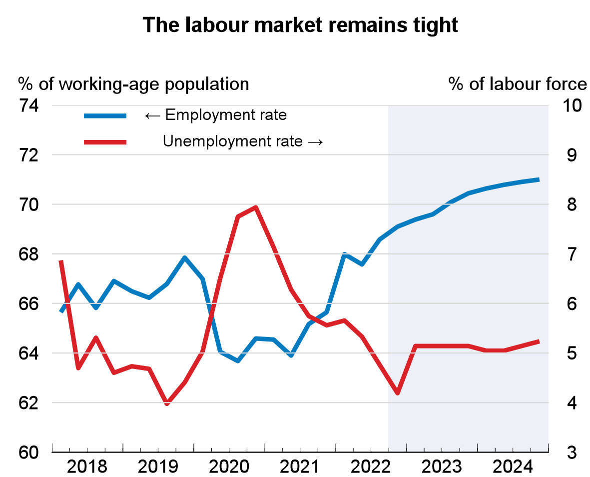
To avoid boosting inflationary pressures further, fiscal policy support should be temporary and targeted towards the vulnerable and support for refugees. In the medium term, effective integration of refugees and reskilling policies could help to alleviate tensions in the labour market. Additional investment in energy infrastructure and security will strengthen resilience.

The economy is slowing

Following a strong recovery in 2021, when GDP grew by 8.1%, the Estonian economy started to slow in the first half of 2022 with growth hindered by high energy prices, supply chain disruptions and labour market pressures. Headline consumer price inflation is among the highest EU-wide and stood at 22.5% in October. Sustained by lower saving, private consumption increased in the first half of the year. Ukrainian refugees have eased some of the labour market pressures, and unemployment reached 5.7% in September, but companies nevertheless continued to cite labour shortages as the biggest obstacle to increasing production, notably in services and construction. Business and consumer confidence have declined since the beginning of the year and export orders are down.

Estonia





1. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/g4d7zp

Estonia: Demand, output and prices

Estonia	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	27.7	-0.4	8.1	0.8	0.5	3.2
Private consumption	13.9	-1.1	6.7	2.2	-0.4	4.1
Government consumption	5.4	2.9	3.9	0.1	0.6	1.6
Gross fixed capital formation	6.9	20.6	7.0	-14.6	5.2	4.1
Final domestic demand	26.3	5.8	6.9	-3.3	1.2	3.6
Stockbuilding[1]	0.3	0.3	0.9	3.9	0.0	0.0
Total domestic demand	26.6	5.1	6.6	0.5	1.0	3.2
Exports of goods and services	20.5	-5.3	20.0	-1.1	3.3	5.0
Imports of goods and services	19.4	0.2	21.4	-0.8	3.6	5.0
Net exports[1]	1.1	-4.0	-0.9	-0.2	-0.2	0.0
Memorandum items						
GDP deflator	_	-0.6	5.8	15.2	7.2	2.9
Harmonised index of consumer prices	_	-0.6	4.5	20.2	10.8	2.8
Harmonised index of core inflation[2]	_	0.0	2.8	10.1	6.6	2.4
Unemployment rate (% of labour force)	_	6.8	6.2	5.0	5.3	6.0
Household saving ratio, net (% of disposable income)	_	10.5	8.3	2.7	0.6	-6.2
General government financial balance (% of GDP)	_	-5.5	-2.4	-2.7	-3.5	-2.3
General government gross debt (% of GDP)	_	24.8	24.4	29.0	33.2	35.8
General government debt, Maastricht definition[3] (% of GDP)	_	18.6	17.6	17.8	19.1	19.7
Current account balance (% of GDP)	_	-1.0	-2.3	-1.4	-1.4	-0.3

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/yurhjf

Spillovers from the war in Ukraine have been relatively contained, helped by a resilient domestic financial sector, and the full impact of sanctions on Russia is expected to be reflected in trade only in the second half of the year. Russia's share in Estonian exports was below 2% before 2022. Some 56 000 Ukrainians have settled in Estonia to date, corresponding to around 4% of the population, with children being just over a half of the migrants. High energy prices explain around half of headline inflation and have passed through quickly to the rest of the economy. Gas demand has been covered by LNG procured from Lithuania and a new central storage unit purchased at a Latvian terminal. Further investments to increase storage capacity are under way. Fiscal policy has cushioned some of the impact of high energy prices with a supplementary budget adopted in mid-year that increased social benefits and support for refugees and added extra resources for defence.

Balancing adequate support to the vulnerable with the need to tame inflation

Fiscal policy will continue to support households and firms facing the impact of the cost-of-living surge in 2023. The minimum wage will rise by 11% and certain public sector salaries by 15% (including teachers and the police). The government is increasing spending on social welfare support and lowering the income tax burden in 2023. These measures come on top of agreed temporary energy price caps for households and small enterprises. Moreover, Estonia is receiving EU cohesion funds. Higher euro area interest rates will dampen growth but remain low relative to the underlying growth of the Estonian economy, making the case for the tighter fiscal stance.

The economy is projected to slow amid high inflation and uncertainty

Real GDP growth is projected to slow to 0.5% next year before picking up to 3.2% in 2024. High uncertainty and lower consumer and business confidence will slow domestic demand growth considerably in 2023. The deteriorating economic outlook in Estonia's main trading partners will lead to lower external demand growth. Nevertheless, fiscal policy will help to cushion the downturn during 2023. Inflation will fall as spare capacity increases, reaching 2.8% in 2024. Considerable uncertainty and risks to the outlook remain, tilted to the downside. Further escalation of the war would increase uncertainty and exacerbate inflation. Disruptions to energy supply in Europe could hit activity both in Estonia and its trading partners. Inflation could be more persistent than projected if wage pressures gather momentum. On the upside, a quick resolution of the war would reduce uncertainty and inflationary pressures.

Policies need to maintain incentives for energy savings, strengthen the energy network and facilitate the green transition

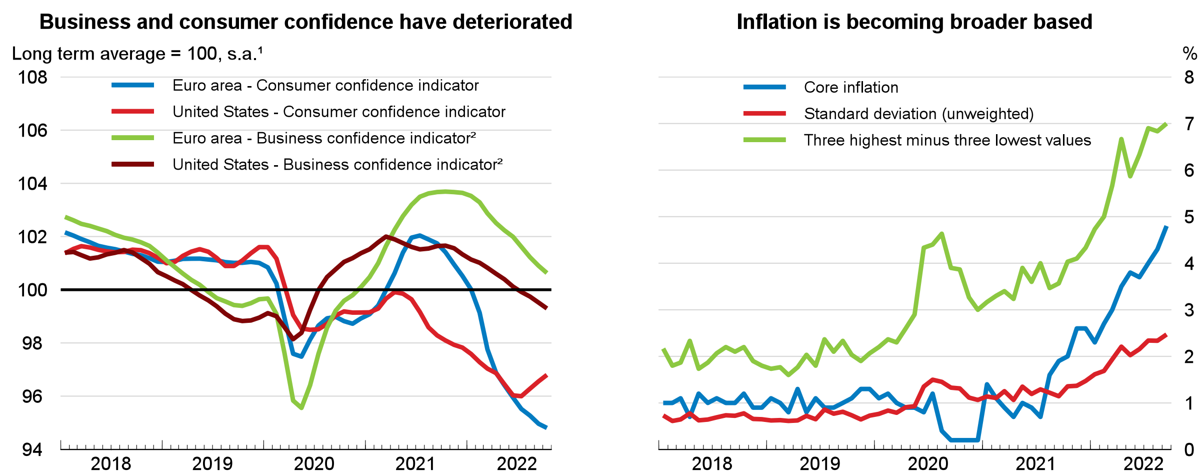
Fiscal policy should continue to shield the most vulnerable from inflation, but better targeting is needed to avoid adding to considerable inflationary pressures. It should also maintain incentives for energy savings. Diversifying energy imports and upgrading the energy network and security, as planned, would improve the resilience of the economy and increase the capacity for greener growth. Effective integration of refugees could help to ease persistent skills shortages.

Euro area

After a strong first half of the year, real GDP growth is projected at 3.3% in 2022 and only 0.5% in 2023 owing to Russia's war of aggression against Ukraine, monetary policy tightening and the global slowdown. Growth is projected to rebound to 1.4% in 2024 as consumption and investment pick up. Inflation is set to decline only gradually, remaining above target in 2024, fuelled by elevated energy prices and tight labour markets. Risks remain tilted to the downside as cold winters and further disruptions in energy supply would hit growth while pushing inflation higher.

High uncertainty, declining real incomes and increasingly widespread inflationary pressures require careful and coordinated policy actions. Fiscal measures to shield households and companies from surging energy and food prices need to avoid providing fiscal stimulus at a time of high inflation. They should be well targeted on the most vulnerable and avoid distorting price signals. Monetary policy should act decisively to bring inflation down, while using all margins of flexibility when reinvesting the proceeds of maturing bonds on the ECB balance sheet to limit financial fragmentation.

Euro area 1



1. OECD standardised, amplitude adjusted.
2. Business confidence refers to the manufacturing sector.
Source: OECD Main Economic Indicators database; Eurostat Harmonised index of consumer prices (HICP) database; and OECD calculations.

StatLink https://stat.link/pe609y

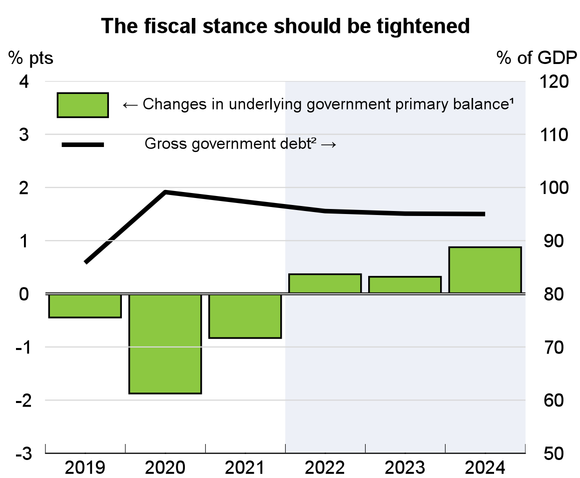
Euro area: Demand, output and prices

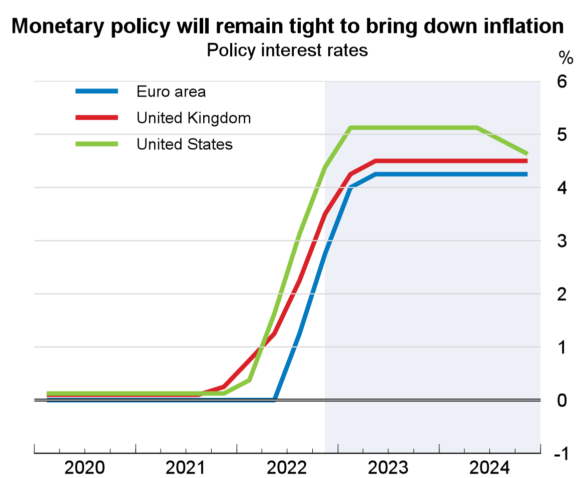
Euro area	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	11 955.9	-6.3	5.3	3.3	0.5	1.4
Private consumption	6 363.3	-7.8	3.8	3.7	0.3	1.0
Government consumption	2 450.1	1.0	4.3	1.7	0.3	0.6
Gross fixed capital formation	2 653.1	-6.5	3.5	2.6	1.1	2.0
Final domestic demand	11 466.4	-5.7	3.8	3.0	0.5	1.2
Stockbuilding[1]	83.7	-0.3	0.3	0.4	0.0	0.0
Total domestic demand	11 550.1	-5.9	4.2	3.4	0.5	1.1
Net exports[1]	405.8	-0.5	1.3	0.1	0.0	0.3
Memorandum items						
GDP deflator	_	1.8	2.1	4.5	5.5	3.1
Harmonised index of consumer prices	_	0.3	2.6	8.3	6.8	3.4
Harmonised index of core inflation[2]	_	0.7	1.4	3.9	4.7	3.1
Unemployment rate (% of labour force)	_	7.9	7.7	6.8	7.1	7.1
Household saving ratio, net (% of disposable income)	_	13.6	11.5	7.4	7.2	7.2
General government financial balance (% of GDP)	_	-7.1	-5.2	-3.7	-3.8	-3.1
General government gross debt (% of GDP)	_	121.0	115.4	113.5	113.0	112.9
General government debt, Maastricht definition[3] (% of GDP)	_	99.1	97.3	95.6	95.1	95.0
Current account balance (% of GDP)	_	2.6	3.7	1.4	1.4	1.7

Note: Aggregation based on euro area countries that are members of the OECD, and on seasonally-adjusted and calendar-days-adjusted basis.
1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/klutxq

Euro area 2





1. Underlying government primary balance as percentage of potential GDP defined as cyclically-adjusted government net lending excluding net interest paid and net one-off operations.
2. Maastricht definition.
Source: OECD Economic Outlook 112 database; and OECD calculations.

StatLink https://stat.link/rcg2s8

Disruption of energy supplies and high inflation are weighing on the outlook

Growth slowed in the third quarter of 2022, after the strong consumption growth during summer. Moreover, forward-looking indicators of sentiment suggest that growth may decline further and even turn negative in the fourth quarter. The output PMIs have been pointing to declining output for several months. Euro area consumer and, to a lesser extent, business confidence have deteriorated sharply. Meanwhile, inflation has continued to strengthen, to 10.6% in October, becoming more broad-based geographically and across categories of goods and services. Inflation expectations have increased and for many market participants and households are now well above the ECB inflation target. Declining real incomes have been partly cushioned by fiscal measures compensating households for the effect of higher energy prices. Although negotiated wage growth has remained contained so far, wage demands are picking up in some countries, including Belgium and Germany. Unemployment has continued to decline; in September 2022, the euro area seasonally-adjusted unemployment rate was at its historical low of 6.6%, down from 8.6% at its recent peak in September 2020, and well below the average rate of about 9% observed in the last decade.

Direct trade with Russia is low and will likely shrink further as the ban on Russian crude and oil imports and other sanctions come into effect. Although 40% of gas and a fifth of oil and petroleum imports came from Russia before the war, the dependency on Russian energy imports has been reduced by about a half in the second quarter of 2022, mainly through supply diversification. Nonetheless, the war in Ukraine continues to have substantial effects on the euro area economy through higher energy prices, persistent supply chain disruptions and rising input costs. Spending to protect vulnerable households and businesses is adding to pressures on public finances already strained by the debt accumulated during the pandemic and long-term spending needs. The war is also affecting trade in agricultural and other commodities as well as increasing their global prices. In addition, EU countries are sheltering about 4.3 million Ukrainian refugees. To help Member States meet related costs, the EU has made available EUR 27 billion from its cohesion funds and pandemic recovery funds.

Fiscal policy needs to avoid providing stimulus in a time of high inflation

While starkly different across the euro area, the fiscal stance is projected to be restrictive for the euro area as a whole in 2023 and even more so in 2024. Many countries have introduced additional support to shield households and companies from surging energy and food prices in 2022. However, in the absence of common European guidelines and co-ordination, the measures are not equally well designed and targeted across the euro area, which may reduce their effectiveness, distort competition, and possibly work against needed macroeconomic policy tightening. In addition, the war in Ukraine has triggered a rise in military spending in many countries as well as investments to secure energy supply.

The ECB has started monetary policy tightening, but further policy rate increases are needed to ensure that forward-looking measures of real interest rates become positive, the de-anchoring of inflation expectations is reversed, and inflation pressures are durably reduced. This will likely involve a period of below-trend growth to help lower resource pressures. The main refinancing rate is projected to rise to 4.25% in the second quarter of 2023 and to remain unchanged through the rest of the projection period.

Growth will slow sharply in 2023, gradually resuming afterwards

Quarterly growth is projected to turn negative in the final quarter of 2022, although strong carryover effects from 2021 and strong performance in the first half of the year mean that annual GDP growth of 3.3% is projected. High energy and food prices, weak confidence, continuing supply bottlenecks, and the initial impact of tighter monetary policy will lead to a sharp slowdown in 2023. Despite robust wage growth, consumer price inflation of 8.3% in 2022 and 6.8% in 2023 will lead to a contraction of real disposable income in 2022 and 2023, and a slowdown of private consumption growth. Investment will be held back by slowing demand, although additional funding of about 0.5% of GDP a year under the pandemic recovery funds will moderate the slowdown. Inflation is projected to moderate perceptibly only in 2024, with subdued domestic growth helping to contain price and cost pressures. Even so, core inflation is projected to still be above the ECB inflation target at the end of the projection horizon.

The risks to the projections are to the downside. The ongoing energy price shock and disruptions to supply chains could worsen, for example through difficulties in replacing diesel products previously imported from Russia, an enforced reduction in gas usage in industry due to further disruptions to energy supplies or a colder-than-usual winter during the projection period. In addition, the risk of a sustained downturn in China would be associated with slower global growth and lower external demand in the euro area. Inflation may well remain high for longer, especially in case of further disruptions in gas supply and the uncertain evolution of food prices due to extreme weather events and fertiliser shortages. A much tighter monetary policy could also heighten the risk of a recession. On the other hand, deceleration of hostilities during the winter months or a durable ceasefire represent upside risks.

Supporting long-term resilience and the green transition

The Russian invasion of Ukraine has heightened awareness of the link between the goals of energy security and climate change mitigation. Continuing a rapid and effective disbursement of the Next Generation EU funds will help accelerate both the diversification of energy supplies and the green transition. Coordination at the EU level and careful design would help to maximise the effectiveness of such policies and ensure a level playing field. Fiscal policy action to help cushion the impact of higher energy prices should be temporary and well targeted on the most vulnerable, while preserving incentives to reduce energy consumption, for example by using targeted income support rather than price freezes and tax cuts.

In addition to national fiscal policies, the need to kick-start energy resilience and the green transition may also warrant some common spending and borrowing, for example to invest in critical common energy infrastructure. As investment in clean energy and energy infrastructure will need to increase substantially by 2030, a clear policy framework for combining price signals with regulatory and fiscal tools is needed at the European level. Finally, continued monetary policy tightening needs to be complemented by using all margins of flexibility when reinvesting the proceeds of maturing bonds, and if needed other policy tools, such as the Transmission Protection Instrument, to limit financial fragmentation in the euro area.

Finland

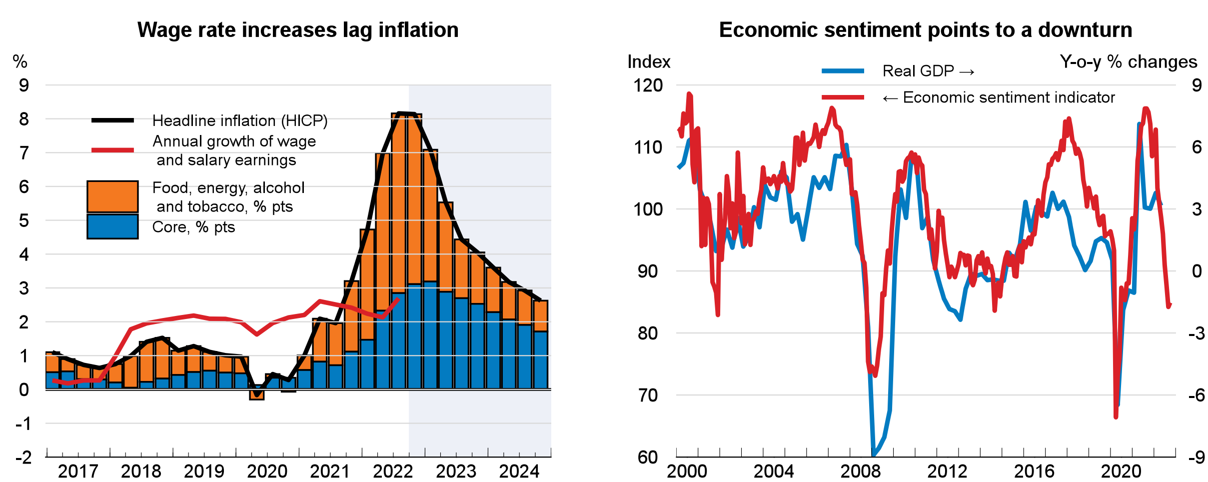
Economic growth is projected to slow sharply because of Russia's war of aggression against Ukraine, with a 0.3% contraction in 2023, before recovering to 1.1% in 2024. Consumption will weaken in response to falling real wages but subsequently recover as inflation moderates and wages rise. Export growth will decline markedly with weaker demand in export markets but then pick up as they strengthen. The unemployment rate will increase to 7.9% in 2023 and remain elevated in 2024. Inflation will fall to 3.1% in 2024, when the energy shock will have passed.

Fiscal consolidation is needed both to support monetary policy tightening and to put medium- and long-term public finances on a sustainable path. A comprehensive public spending review should be undertaken to identify consolidation measures. State aid to companies that does not enhance productivity should be reduced. Labour market regulations should be made less restrictive to facilitate greater employment and innovation.

An economic downturn has begun

Growth surged during the first half of 2022 following the removal of COVID-19 restrictions but has slowed sharply since because of Russia's war of aggression against Ukraine. Energy prices have soared, boosting annual headline HICP inflation to 8.2% in the third quarter of 2022. Core inflation rose to 4.5% as higher energy and food prices fed into other HICP components. Increases in the wage and salary index also strengthened but, at 2.6%, lagged far behind price increases. Retail sales volumes are falling and consumer confidence has dropped to a record low. The residential construction cycle turned down during the second quarter of 2022 and the number of issued building permits is falling. Business investment has also started to weaken as has business confidence. Strong employment growth abruptly ceased in the third quarter of 2022, when employment was flat and the unemployment rate jumped to 7.3%.

Finland



Source: Statistics Finland; OECD Economic Outlook 112 database; and European Commission.

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Finland: Demand, output and prices

Finland	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	239.9	-2.2	3.0	2.2	-0.3	1.1
Private consumption	126.1	-4.0	3.7	2.3	-0.6	1.4
Government consumption	55.6	0.3	2.9	2.8	-0.3	0.1
Gross fixed capital formation	57.1	-0.9	1.5	3.0	-0.7	0.2
Final domestic demand	238.8	-2.3	2.9	2.6	-0.6	0.8
Stockbuilding[1,2]	0.6	0.2	-0.1	3.7	0.0	0.0
Total domestic demand	239.5	-1.9	3.0	6.3	-0.6	0.7
Exports of goods and services	95.7	-6.8	5.4	-0.5	1.9	3.1
Imports of goods and services	95.3	-6.0	6.0	9.0	1.2	2.3
Net exports[1]	0.4	-0.3	-0.2	-3.7	0.3	0.3
Memorandum items						
GDP deflator	_	1.5	2.5	6.0	4.7	3.1
Harmonised index of consumer prices	_	0.4	2.1	7.0	5.3	3.1
Harmonised index of core inflation[3]	_	0.5	1.2	3.6	4.3	3.1
Unemployment rate (% of labour force)	_	7.8	7.6	7.0	7.9	7.8
Household saving ratio, net (% of disposable income)	_	4.7	2.0	-1.4	-1.2	-1.3
General government financial balance (% of GDP)	_	-5.5	-2.7	-2.5	-3.9	-3.6
General government gross debt (% of GDP)	_	90.8	85.0	84.9	87.2	88.8
General government debt, Maastricht definition[4] (% of GDP)	_	74.8	72.4	72.2	74.5	76.2
Current account balance (% of GDP)	_	0.7	0.6	-2.6	-2.2	-1.9

1. Contributions to changes in real GDP, actual amount in the first column.
2. Including statistical discrepancy.
3. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
4. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/miozxw

Following Finland's application to join NATO in May, Russia terminated gas and electricity exports to Finland. While most gas was imported from Russia, gas only represents 5% of total energy consumption and plans are advanced for sourcing most of it elsewhere, in LNG form. This transition will be challenging for some industries but not for households as their gas consumption is minor. Additional electricity from local and neighbouring sources has replaced imports from Russia (10% of consumption). A new nuclear power plant will supply 14% of Finland's electricity when it reaches normal operating capacity this winter. Finland no longer imports oil from Russia. To contain energy price increases, the VAT rate on electricity will be reduced from 24% to 10% over December 2022-April 2023 (EUR 209 million) and targeted assistance to households will be provided over this period (EUR 600 million). The government has also implemented other targeted measures focused on transport that expire at the end of 2023 (EUR 900 million).

Fiscal policy is mildly expansionary but will become neutral in 2024

Fiscal policy was mildly expansionary in 2022, despite a large reduction in COVID-19 expenditures, and will be again in 2023 (the underlying primary deficit is estimated to increase by 0.7% of GDP in both 2022 and 2023) and neutral in 2024. Additional expenditures related to the war in Ukraine have added 0.8% of GDP to the structural budget deficit in 2022 and 2023, but will add somewhat less in 2024. Compared with 2022, most of the increase in the structural budget deficit in 2023 is attributable to the setting-up costs of the health and social services reform and the measures to contain energy price increases.

The economy is heading into a short-lived recession

The economy is set to stall in 2023, weighed down by high inflation and tightening monetary conditions, but to recover in 2024 as these headwinds diminish. Consumption will weaken in response to falling real wages but subsequently strengthen as wages rise. Business investment will be depressed by low demand growth and tighter monetary conditions but begin to recover in late 2024 as domestic and international economic conditions improve. Export growth will decline markedly with demand in export markets, which are being hit by the large reduction in gas supplies from Russia, but pick up as these energy sources are replaced and external demand recovers. The unemployment rate should peak at around 8% and only fall slightly by the end of 2024. Inflation will fall to 3.1% in 2024, when the energy shock will have passed. Key domestic risks are that industry fails to fully replace Russian gas imports by other energy sources, that the new nuclear power plant does not reach normal operating capacity by the end of 2022 and that electricity imports are limited in coming months by a drought-induced decline in hydroelectricity production in Norway, all of which would reduce economic growth.

Further measures are needed to enhance fiscal and environmental sustainability

Fiscal consolidation should resume in 2024 to rebuild buffers and put public finances on a more sustainable path. It should aim to reduce the structural budget deficit to the medium-term objective of 0.5% of GDP. Further labour market reforms to increase work incentives and labour market flexibility would not only contribute to higher employment and productivity, but also to fiscal consolidation. The biofuels mandate, which results in very costly abatement, should be reduced to the minimum level required by EU regulations and compensated for by aligning the carbon price used to calculate carbon tax rates on heating fuels with that used for transport fuels and, if necessary, increasing this carbon price. Instruments should be created to guide the cultivation of peatlands (16% of emissions) towards paludiculture (i.e., the cultivation of wetted peatlands). Policies to reduce car dependency in cities should be strengthened while support for low-carbon cars should be focused on areas with limited public transport options.

France

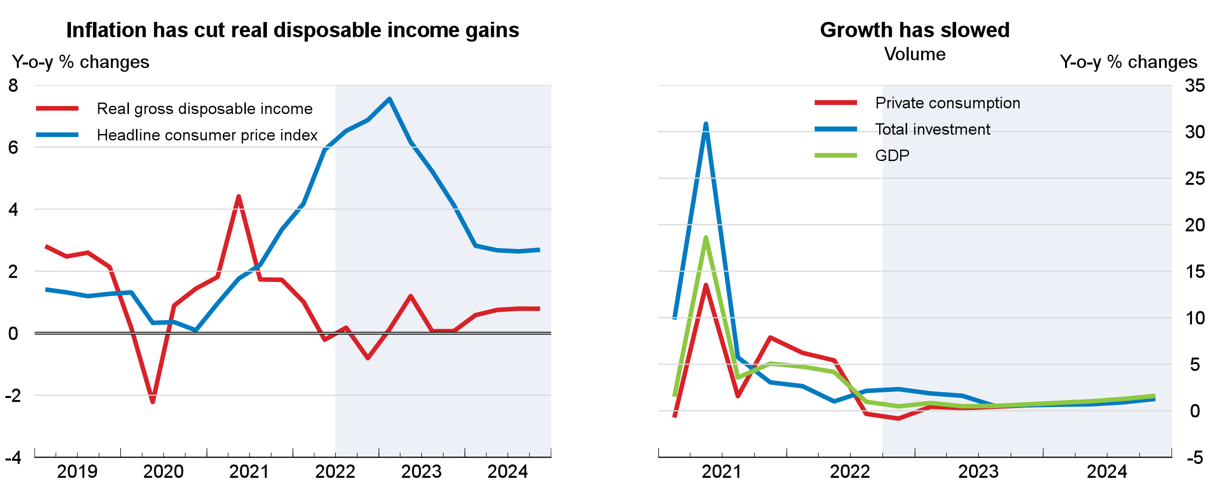
Real GDP is projected to grow by 2.6% in 2022, 0.6% in 2023 and 1.2% in 2024. Russia's invasion of Ukraine, supply chain disruptions and elevated energy prices have dented economic prospects. Inflation is expected to reach 5.9% in 2022, 5.7% in 2023 and 2.7% in 2024, lowering household purchasing power and consumption growth. The decline in business and household confidence, weaker global economic conditions and high uncertainty will hold back investment and exports. Wages are accelerating, owing to recent labour market improvements and the indexation of the minimum wage. Yet, with slowing growth and declining employment, the unemployment rate will rise to 8.1% in 2024.

Fiscal policy will gradually become less supportive. The temporary caps on regulated energy prices and temporary subsidies and cash transfers have smoothed energy price shocks, but these measures are expected to be progressively phased out in 2023-24. Though energy supply remains uncertain, it is crucial to improve the targeting of support measures to reduce fiscal cost, avoid impeding structural change and limit additional inflationary pressures. An ageing population and higher interest rates will weigh on the public finances, raising the need for improved spending efficiency and a reform of the pension system.

Growth has slowed

Rising energy prices, Russia's war of aggression against Ukraine and supply-chain disruptions slowed the rapid rebound in GDP in 2022. GDP rose by just 0.2% quarter-on-quarter in 2022Q3. Despite historically high employment rates, large accumulated savings and the lifting of COVID-19 sanitary restrictions, surging energy prices, high uncertainty and declining real wages have held back consumption and household investment. A rebound of activity in services, particularly tourism, and robust business investment supported growth over the summer of 2022, but business and consumer confidence have declined, and goods consumption was down by 3% in the year to September. Consumer prices were up by 7.1% in the year to October, with retail energy price growth at 20% and price pressures broadening. The pass-through of inflation to wages remains limited so far.

France 1



Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/1bcjgu

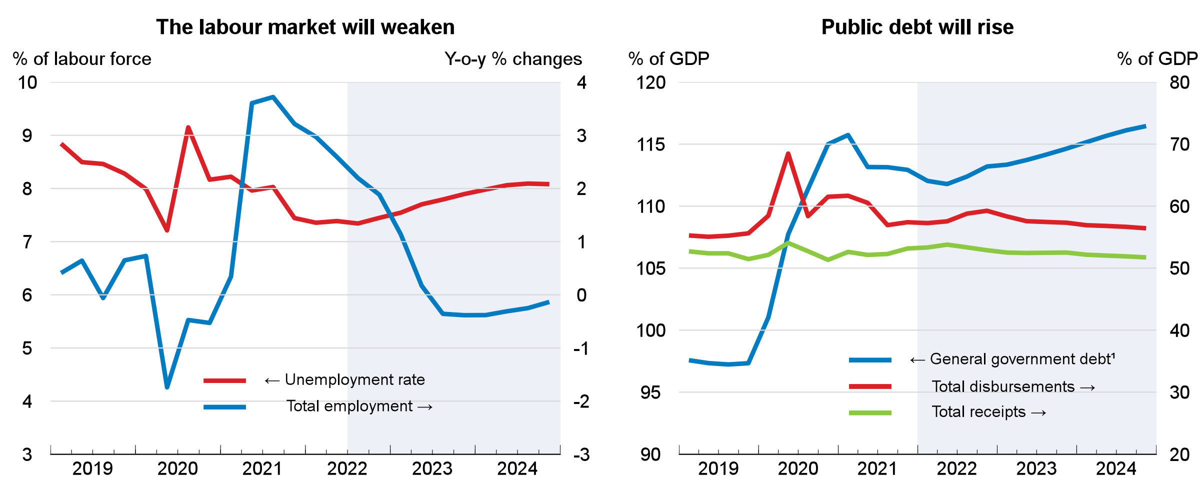
France: Demand, output and prices

France	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2014 prices)				
GDP at market prices	2 440.1	-7.9	6.8	2.6	0.6	1.2
Private consumption	1 307.5	-6.8	5.3	2.5	0.4	1.0
Government consumption	560.6	-4.0	6.4	2.4	0.5	0.5
Gross fixed capital formation	573.3	-8.4	11.4	2.0	1.1	0.9
Final domestic demand	2 441.4	-6.6	6.9	2.4	0.6	0.9
Stockbuilding[1]	22.3	-0.2	-0.3	0.6	0.2	0.0
Total domestic demand	2 463.7	-6.7	6.6	3.0	0.8	0.9
Exports of goods and services	771.4	-17.0	8.6	7.5	2.8	3.4
Imports of goods and services	795.0	-13.0	7.8	8.5	3.0	2.3
Net exports[1]	- 23.6	-1.1	0.1	-0.4	-0.2	0.3
Memorandum items						
GDP deflator	_	2.8	1.3	2.3	3.3	2.2
Harmonised index of consumer prices	_	0.5	2.1	5.9	5.7	2.7
Harmonised index of core inflation[2]	_	0.6	1.3	3.5	3.8	2.2
Unemployment rate[3] (% of labour force)	_	8.1	7.9	7.4	7.7	8.1
Household saving ratio, gross (% of disposable income)	_	20.5	18.3	16.3	16.2	16.0
General government financial balance (% of GDP)	_	-9.0	-6.5	-4.9	-5.2	-4.7
General government gross debt (% of GDP)	_	146.2	138.4	138.6	140.1	141.9
General government debt, Maastricht definition[4] (% of GDP)	_	115.0	112.9	113.2	114.6	116.5
Current account balance (% of GDP)	_	-1.8	0.4	-1.8	-2.4	-2.1

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. National unemployment rate, includes overseas departments.
4. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/9soqlc

France 2



1. Maastricht definition.
Source: OECD Economic Outlook 112 database.

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Despite strong services activity, the trade deficit has worsened further due to rising energy import costs, persistent difficulties in the aeronautical and automotive sectors, as well as constrained nuclear production capacity. As wholesale gas and electricity prices remain at historical highs, they will continue feeding through into retail prices, keeping inflation pressures high. The fiscal costs of energy price caps and support measures will amount to 1.9% of GDP in 2022 and 2% in 2023, with a 15% increase of regulated electricity and gas prices in 2023, an assumed similar increase in 2024, and the end of road fuel tax cuts in January 2023. At the same time, euro area monetary policy tightening is progressively curbing internal demand, including via a slowdown in new mortgage loans.

Fiscal measures are partly cushioning external shocks

Fiscal policy is assumed to remain broadly neutral in 2023 and to shift to moderate consolidation in 2024. Despite new energy support measures, the budget deficit will narrow to 4.9% of GDP in 2022 thanks to strong revenue growth and the phasing-out of COVID-19-related spending. To respond to persistently high commodity and energy prices, the government has capped gas and electricity charges, increased a voucher scheme to subsidise low-income households' energy consumption and announced additional one-off means-tested transfers in 2022-23. The government also cut road fuel taxes until end-2022, increased targeted conditional subsidies for businesses, raised social benefits and public wages, and capped rent increases in 2023. In addition, one-off taxes on electricity producers and oil refineries (worth EUR 7 billion) will help finance additional temporary energy support measures for firms in 2023. The direct energy support measures amount to EUR 49 billion (1.9% of GDP) in 2022 and EUR 56 billion (2.0% of GDP) in 2023. Energy-support measures are assumed to be partly phased out in 2024, with a 15% increase in regulated prices. Further measures to support economic activity in the projection period include spending from the recovery plan worth EUR 10 billion in 2023-24 and further housing and business tax cuts in 2023-24.

Monetary and financial conditions are becoming less supportive in the euro area. Yet, the implementation of the Next Generation EU plan is supporting growth in France with EUR 38 billion of grants, and in its main trading partners. The 2022 resilience plan has pushed forward funding for housing renovation and insulation, while the energy saving plan foresees a decline of 10% in energy consumption by 2024. Government-guaranteed loans and subsidies for highly affected firms will support corporate liquidity. Car and energy investment subsidies for households are targeted on green alternatives, and will raise durable goods consumption and housing investment. Greater public investment in infrastructure and digitalisation, as well as additional financing for training programmes, are expected to improve productivity and long-term growth.

Domestic demand growth is slowing

GDP growth is projected to slow to 0.6% in 2023 and increase to 1.2% in 2024. Inflation is weighing on household purchasing power and pent-up demand is vanishing. The pass-through of high wholesale energy prices and the indexation of the minimum wage will raise core inflation and wages in 2023, despite caps on regulated energy prices and rent increases. Yet, wholesale energy and food price pressures will progressively ease. Tighter financing conditions and a weakening labour market will curb core inflation, wage growth and housing investment. As demand from trading partners softens and supply bottlenecks persist, exports will rise only slowly from their current low levels. Business investment is set to remain resilient, as the support from the recovery and resilience plans will partly compensate reduced profit margins, high uncertainty, softer global demand and increasing financing costs. The budget deficit and public debt are projected to remain high relative to GDP, with debt rising above 116% of GDP in 2024 (Maastricht definition).

Worsening geopolitical tensions, a stronger upheaval in energy markets and further supply-chain disruptions could lead to higher-than-expected inflation and lower domestic demand and growth in France, and weaken external demand. Some sectors, such as transport equipment, travel and tourism services, would be particularly affected. With sizeable debt, in part due to government loan guarantees, some companies will face liquidity and solvency concerns, which could lead to bankruptcies and dent economic prospects. The extent to which large, accumulated household savings are spent is particularly uncertain and a higher or lower-than-projected saving rate would affect domestic demand and growth.

Supporting more sustainable growth

Unconditional energy price support measures, notably price caps, should be phased out progressively, as they have high fiscal costs and create economic distortions. To dampen the effects of persistent energy price pressures and geopolitical tensions, additional support to the most vulnerable households and firms should remain temporary and become more targeted. As geopolitical and price tensions dissipate and growth becomes more firmly based, a medium-term fiscal strategy to gradually lower public expenditures and increase their efficiency should be firmly implemented to raise growth and improve medium-term fiscal sustainability. This strategy should build on more efficient and transparent public spending allocation through spending reviews. Policy steps to broaden progress towards green alternatives and energy savings, and ensure a fair transition, should also continue. Speeding up housing renovation and energy savings would help the longer-term energy transition and should build on regular evaluations of related support schemes. Ensuring broad access to lifelong learning for low-skilled and long-term unemployed people, as well as an efficient implementation of quality standards for these programmes, is also needed to support growth and help bring about longer working lives, as foreseen in the planned pension reform. In particular, continuing to strengthen education from an early age will be key to ensure greater equity.

Germany

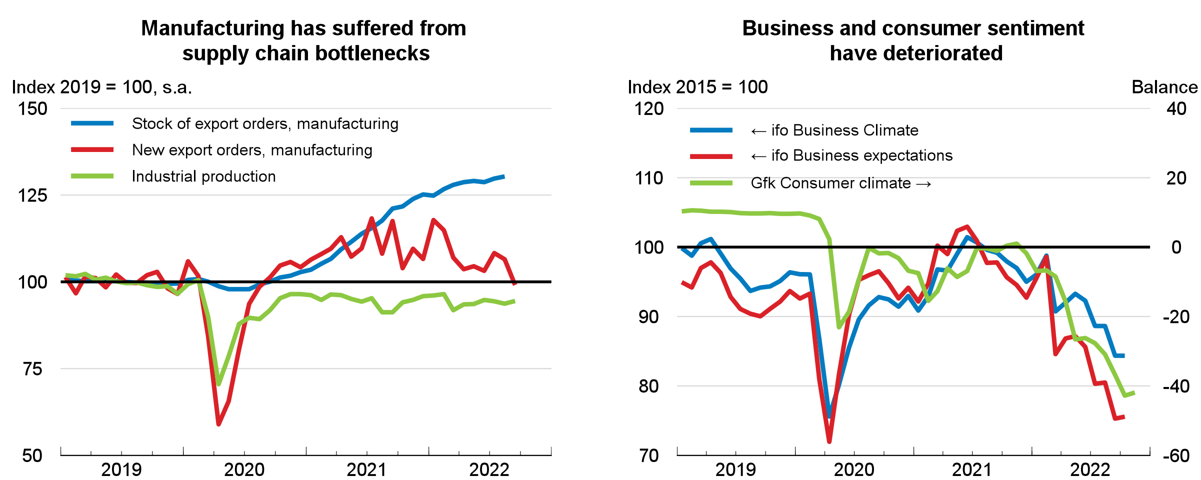
The economy is projected to grow by 1.8% in 2022, contract by 0.3% in 2023 and recover by 1.5% in 2024. Uncertainty is high amidst strong energy price volatility. High inflation is reducing real incomes and savings, damping private consumption. Despite weakening external demand, export growth will recover through 2023 due to easing supply chain bottlenecks and a record-high order backlog. If energy saving requirements are not met during the winter, gas rationing would imply severe production disruptions.

The fiscal deficit will widen in 2023, before contracting in 2024. It is crucial that energy support measures establish strong incentives for gas savings and target vulnerable households. Corporate support measures should address liquidity concerns and not impede necessary structural change. Improving planning and approval processes and capacity, particularly at the municipal level, would accelerate the energy transition and digitalisation. Skilled labour shortages should be addressed by raising the labour supply of women, elderly and low-skilled workers, improving training and adult learning, and facilitating the recognition of the qualifications of migrants and refugees.

Uncertainty and high inflation exert a drag on growth

Following Russia's invasion of Ukraine, GDP growth slowed to 0.1% (seasonally adjusted quarterly rate) in the second quarter of 2022 and 0.3% in the third quarter. High inflation and plummeting consumer confidence have limited the rebound of private consumption that had been imparted by the lifting of pandemic containment measures and high excess savings. Heightened uncertainty, high energy prices and material shortages have hurt manufacturing and construction as well as investment. Business confidence plunged in September, but stabilised in October. High order backlogs and easing supply chain bottlenecks are supporting exports. Annual consumer price inflation rose to 10.9% in September with the phase-out of fuel and public transport subsidies and continued to rise to 11.6% in October. Producer prices rose by 45.8% over the year to September. Household inflation expectations for one, five and ten years ahead averaged 8.2%, 6% and 5.5%, respectively, in September. The labour market remains robust amid intensifying labour shortages, but annual negotiated pay rose only by 2.9% in the second quarter of 2022, resulting in a real wage decrease of 4.4%.

Germany 1



Source: Federal Statistical Office; ifo business surveys; and GfK.

StatLink https://stat.link/vl5bjr

Germany: Demand, output and prices

Germany	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	3 479.4	-4.1	2.6	1.8	-0.3	1.5
Private consumption	1 807.4	-5.9	0.4	4.5	-0.2	0.7
Government consumption	703.2	4.0	3.8	3.8	-0.7	0.8
Gross fixed capital formation	745.4	-3.0	1.0	0.3	0.4	2.0
Final domestic demand	3 256.0	-3.1	1.3	3.4	-0.2	1.0
Stockbuilding[1]	24.9	-0.2	0.5	0.2	0.0	0.0
Total domestic demand	3 280.9	-3.3	2.0	3.6	-0.2	1.0
Exports of goods and services	1 627.6	-10.1	9.5	1.8	1.7	2.6
Imports of goods and services	1 429.1	-9.1	8.9	5.8	2.1	1.7
Net exports[1]	198.5	-1.0	0.8	-1.6	-0.1	0.5
Memorandum items						
GDP without working day adjustments	3473.3	-3.7	2.6	1.7	-0.5	1.5
GDP deflator	_	1.8	3.1	5.7	7.1	3.5
Harmonised index of consumer prices	_	0.4	3.2	8.5	8.0	3.3
Harmonised index of core inflation[2]	_	0.7	2.2	3.6	4.4	3.0
Unemployment rate (% of labour force)	_	3.7	3.6	3.1	3.5	3.5
Household saving ratio, net (% of disposable income)	_	16.0	15.3	9.3	9.0	10.6
General government financial balance (% of GDP)	_	-4.3	-3.9	-2.7	-3.2	-2.2
General government gross debt (% of GDP)	_	78.5	77.6	78.3	78.8	79.4
General government debt, Maastricht definition[3] (% of GDP)	_	68.1	68.8	69.5	69.9	70.6
Current account balance (% of GDP)	_	6.8	7.5	3.8	3.6	4.4

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

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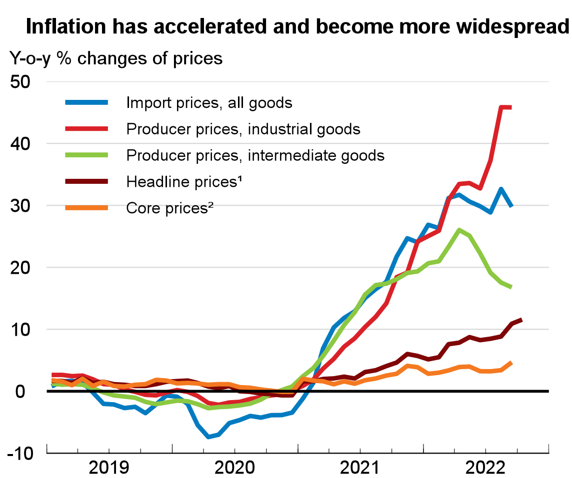
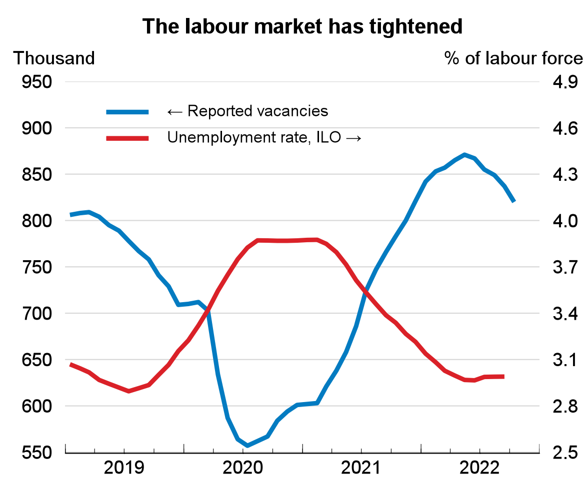
Germany 2





1. Harmonised index of consumer prices.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
Source: Federal Statistical Office; and Eurostat.

StatLink https://stat.link/eu8b3d

Prior to Russia's war of aggression against Ukraine, Germany was highly dependent on Russian gas, oil and coal, with around one-third of primary energy supply coming from Russia. A rapid diversification of energy suppliers, the EU coal embargo and the shutdown of Russian gas pipelines have strongly reduced Russian energy imports. Despite gas storage levels already reaching 100% and the planned opening of two LNG terminals by the end of the year, gas consumption needs to be reduced by around 20% to prevent gas shortages during the winter. Industry has already reduced gas consumption by around 25% (compared to the average over 2018-21), including through output reductions in some energy-intensive industries. Energy savings will be further incentivised by a gas auction mechanism for firms to supply their excess gas capacity. Households and small firms reduced gas consumption by 31% due to high prices and relatively warm weather in October. Electricity production using gas has been reduced and replaced by phased-out or reserve coal power plants which have been reactivated. The three remaining nuclear power plants, which were scheduled to close on 1 January 2023, will continue operating until mid-April 2023. So far, Germany has received 1 million refugees from Ukraine (equivalent to 1.2% of Germany's population).

Fiscal policy is supporting households and firms

The fiscal deficit will widen in 2023 due to broad energy price support. Pandemic-related support programmes were phased out in June, but three energy support packages estimated at EUR 95 billion (2.6% of GDP) in direct expenditures and an energy support fund of EUR 200 billion (5.5% of GDP) financed by credit allowances have been announced. The support packages include various measures to support real incomes, comprising both targeted transfers through social assistance and housing allowances, and non-targeted ones such as one-off payments to all employees, pensioneers and students, and adjustments of the income tax schedule. The VAT rate on gas was lowered from 19% to 7% in October. These measures can be realised within the current budget, as high inflation and repayments of COVID-19 support grants led to higher-than-expected tax revenues. For 2023, electricity price support will amount to EUR 43 billion and will be partly financed by a windfall tax on electricity producers. The energy support fund will finance gas price support for households and firms up to a total of EUR 40 billion in 2023 as well as liquidity support, equity injections and grants for firms. The electricity and gas price support will subsidise around 80% of past average consumption through transfers, limiting consumer price increases in 2023 to about a doubling from 2022 prices, and maintaining market prices for any consumption exceeding 80% of past average consumption. Energy price support measures are planned to be phased out in April 2024.

To reach its ambitious climate targets, the government plans to invest around EUR 200 billion until 2026, with fiscal incentives to crowd in private investments playing a major role. It also envisions a significant increase in military spending of EUR 100 billion over the next few years to upgrade military equipment. Most of these debt-financed investments as well as the energy support fund will be funded through shadow budgets, the spending of which is excluded from the national debt brake that is planned to be reinstated from 2023. Exact spending plans for the shadow budgets are currently missing, but capacity constraints in the construction sector and long and complex planning and approval procedures will likely slow the disbursement of funds.

The recovery is hampered by the war in Ukraine and high energy prices

High inflation and plummeting consumer sentiment will weigh on private consumption. Investment remains subdued due to high uncertainty and rising interest rates, but will eventually pick up due to high corporate savings and investment needs related to the relocation of supply chains and renewable energy expansion, as well as rising public investment. High energy prices will weigh on energy-intensive industries, but exports should continue to recover due to a substantial order backlog and easing supply chain bottlenecks. Inflation will stay high due to the pass-through of energy and producer prices to consumers, the depreciation of the euro and rising wage pressures, but gradually moderate over the projection period. Wage growth will rise, helped by the minimum wage increase from 48% to 60% of the median wage in October 2022, continued labour shortages and pressure from unions to preserve the purchasing power of workers. Fiscal tightening is projected for 2024.

A severe downside risk to the projection arises from potential gas rationing in the next two winters if planned fiscal support measures do not sufficiently preserve price incentives for gas savings. New waves of the pandemic could further depress private consumption or exacerbate supply chain bottlenecks. Rising interest rates could cause strong corrections in housing markets, affecting financial markets. On the upside, a quicker end of the war could restore investor and consumer confidence and lower energy prices.

Expanding renewables to raise energy security

Energy support measures should be better targeted on vulnerable households and firms and establish strong incentives for gas savings. To expand renewable energy supply, it is crucial to continue accelerating complex planning and approval procedures at the municipal and Länder level. Speeding up the digitalisation of the economy requires more investments in digital infrastructure, a more rapid modernisation of the state and better coordination of policies and administrative procedures across levels of government. Increasing the efficiency of public spending by effective use of spending reviews, reducing regressive and environmentally harmful subsidies and tax exemptions, and improving tax enforcement could free up additional resources for necessary public investment. To address rising labour shortages, which also risk derailing private and public renewable energy investment, labour market participation of women, low-skilled and elderly workers needs to be raised by setting the right tax incentives and improving training and adult learning policies. Boosting skilled migration and facilitating the labour market participation of Ukrainian refugees, including through better access to childcare, is also key.

Greece

Growth is expected to moderate from 6.7% in 2022 to 1.6% in 2023 and 2024. Despite the rebound in tourism and continued fiscal support, consumption is projected to slow in 2023 as real incomes shrink and uncertainty remains elevated. Receding energy prices are projected to reduce inflation and support consumption in 2024. Disbursements of Greece's Recovery and Resilience Plan are projected to sustain modest investment growth in the face of higher costs. Inflation is becoming more broad-based as growing labour shortages contribute to wage pressures.

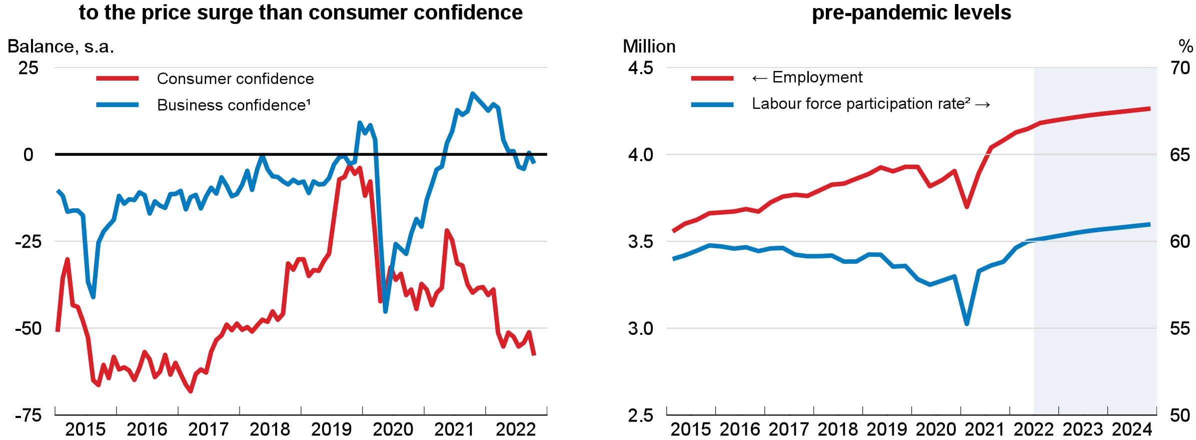
Planned support measures sustain demand while capacity constraints are growing. Shifting fiscal measures towards income transfers to vulnerable groups and greater support to improve energy efficiency would encourage energy savings, support public finances and ease ongoing inflationary pressures. This would help Greece to achieve an investment grade sovereign debt rating. It would also address longer-term goals, notably cutting emissions and reducing high levels of energy poverty.

Rebounding tourism and fiscal support have driven strong economic growth

Greece's economy grew strongly during the first half of 2022 owing to rebounding exports, led by services, rising investment, and substantial fiscal support. Tourism receipts from June to August 2022 returned to their 2019 historical peak, while receipts from shipping in the second quarter of 2022 exceeded the same period in 2019 by 57%. Business confidence has retreated slightly since the start of Russia's war of aggression against Ukraine but remains close to pre-pandemic peaks. Employment in September 2022 reached its highest level since 2010. Greece now reports one of the largest increases in labour shortages of EU countries, especially in sectors recovering strongly, such as construction. Year-on-year consumer price inflation reached 12.1% in September 2022, before slowing in October 2022 as energy prices eased. Inflationary expectations remain at historical highs especially in construction, services and retail trade.

Greece

Business confidence remains more robust to the price surge than consumer confidence | **Employment continues to grow above pre-pandemic levels**



1. Business confidence is an unweighted average of confidence indicators in industry, construction, retail trade and services.
2. Labour force participation rate, as a percentage of population aged 15-74.
Source: Eurostat; and OECD Economic Outlook 112 database.

StatLink https://stat.link/ehlfvk

Greece: Demand, output and prices

Greece	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	183.3	-9.0	8.3	6.7	1.6	1.6
Private consumption	126.6	-7.9	7.8	8.6	0.8	1.0
Government consumption	36.7	2.6	3.7	1.9	1.6	0.1
Gross fixed capital formation	19.4	-0.3	19.6	7.3	2.7	5.6
Final domestic demand	182.7	-5.0	8.2	7.1	1.2	1.4
Stockbuilding[1,2]	3.7	1.4	-0.9	0.5	-0.3	0.0
Total domestic demand	186.4	-3.3	7.3	7.5	0.9	1.3
Exports of goods and services	73.5	-21.5	21.9	9.7	2.8	3.3
Imports of goods and services	76.7	-7.6	16.1	9.3	2.4	2.5
Net exports[1]	- 3.2	-5.5	0.7	-0.6	0.0	0.2
Memorandum items						
GDP deflator	_	-0.8	2.1	7.9	3.4	2.6
Harmonised index of consumer prices	_	-1.3	0.6	9.7	4.3	2.3
Harmonised index of core inflation[3]	_	-1.2	-1.1	4.6	4.8	2.6
Unemployment rate (% of labour force)	_	16.3	14.7	12.6	11.8	11.3
General government financial balance[4] (% of GDP)	_	-9.9	-7.4	-4.3	-2.5	-1.5
General government gross debt (% of GDP)	_	242.3	225.7	207.8	203.0	198.5
General government debt, Maastricht definition[5] (% of GDP)	_	206.4	193.3	175.4	170.7	166.2
Current account balance[6] (% of GDP)	_	-6.6	-6.7	-5.5	-5.8	-5.6

1. Contributions to changes in real GDP, actual amount in the first column.
2. Including statistical discrepancy.
3. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
4. National Accounts basis. Data also include Eurosystem profits on Greek government bonds remitted back to Greece, and the estimated government support to financial institutions and privatisation proceeds.
5. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
6. On settlement basis.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/t2ocx0

Food and energy supply disruptions and higher prices, amplified by the war in Ukraine, are reducing real incomes, with consumer energy prices increasing by 53% in the year to September 2022. Greece has adopted measures totalling 5.5% of GDP in 2022 to support households and firms against high energy costs, of which 3.6% of GDP are financed by the Green Transition Fund, mainly stemming from Greece's mechanism of collecting windfall revenues in the wholesale electricity market. Greece is increasing imports of liquified natural gas, but has little storage capacity and is seeking storage agreements with neighbouring countries. It has already agreed with Italy to stock gas equivalent to 5% of its consumption during the first half of 2022. The government does not expect shortages in energy supply and has not announced a plan to ration energy supplies in the event of gas shortages. Monetary tightening and growing international uncertainty have led to increasing government bond yields. Spreads between Greek and German sovereign bond yields rose by more than in other euro area countries in the year to November. Average borrowing costs for businesses rose more slowly, however, partly reflecting banks' improving access to loanable funds.

Fiscal measures are expected to provide continued support to the economy

The government plans to return to a modest primary surplus of 0.7% of GDP in 2023, implying a tightening fiscal stance and one of the largest fiscal consolidations among EU countries. Energy support measures in 2022 mostly reduce energy costs for households and firms via price subsidies with generous eligibility criteria. These add to support measures initiated during the pandemic, including cuts to social insurance contributions and tax rates, valued at 2% of GDP in 2022. The draft 2023 budget does not extend existing measures but provides a reserve of 0.5% of 2023 GDP for energy measures. Prolonged energy disruptions, leading to current energy support measures being extended to mid-2023, are projected to lead to fiscal costs of about 1% of GDP in 2023. Other substantial fiscal measures include making permanent social insurance and tax rate cuts adopted during the pandemic, and subsidies of home loan interest costs for young people. Fiscal costs for these amount to 1.6% of GDP in 2023.

High uncertainty and rising prices are projected to moderate growth

Rising prices and investment costs and unwinding fiscal support are projected to moderate economic growth. Consumption growth is projected to weaken as high inflation weakens households' real incomes. Fiscal support to shield households from the rising cost of living is expected to expire from 2023. Strong growth in the costs of investment projects plus high uncertainty are expected to weigh on investment, even as the Greece 2.0 plan implements projects valued near 2.4% of GDP annually. Demand, while moderating, is rising faster than firms' capacity, reinforcing capacity constraints and underlying price pressures. Headline inflation is projected to moderate as energy prices stabilise over the projection period and euro area monetary tightening takes effect, though the removal of energy price subsidies, expected in the second half of 2023, will lead inflation to rise temporarily. If energy supply disruptions or high prices continue beyond mid-2023 or are more severe than foreseen, consumption and production would weaken, and the public finances would come under greater pressure. Slower fiscal consolidation could risk delaying the upgrading of Greece's sovereign debt to investment grade, leading to more expensive and scarcer access to finance. Stricter sanctions on Russian oil exports would curtail shipping receipts from Russia, which amounted to 1.6% of total shipping receipts in 2021. If wage growth becomes poorly coordinated as labour markets tighten, inflation could become more entrenched.

Well-designed fiscal measures can address both short- and long-term energy challenges

Limiting fiscal responses to high energy prices to well-targeted temporary support for vulnerable households would allow the government to rebuild some fiscal space and ease inflationary pressures as activity reaches capacity constraints. Shifting the main mechanism for wage adjustments from administrative increases in the minimum wage to broad and timely collective bargaining that reflect sectoral conditions and workers' productivity would support real incomes and competitiveness, allow wage rates to better reward productivity, and mitigate inflationary pressures. Cross-country experience suggests that the new fiscal subsidy for home loan interest costs may raise house prices when new supply is constrained, with the effect of reducing access to home ownership. Allocating these resources to expand programmes that support access to higher-quality housing, such as for energy efficiency-improving renovations, would reduce households' energy costs, address high levels of energy poverty and help Greece achieve net zero greenhouse gas emissions.

Hungary

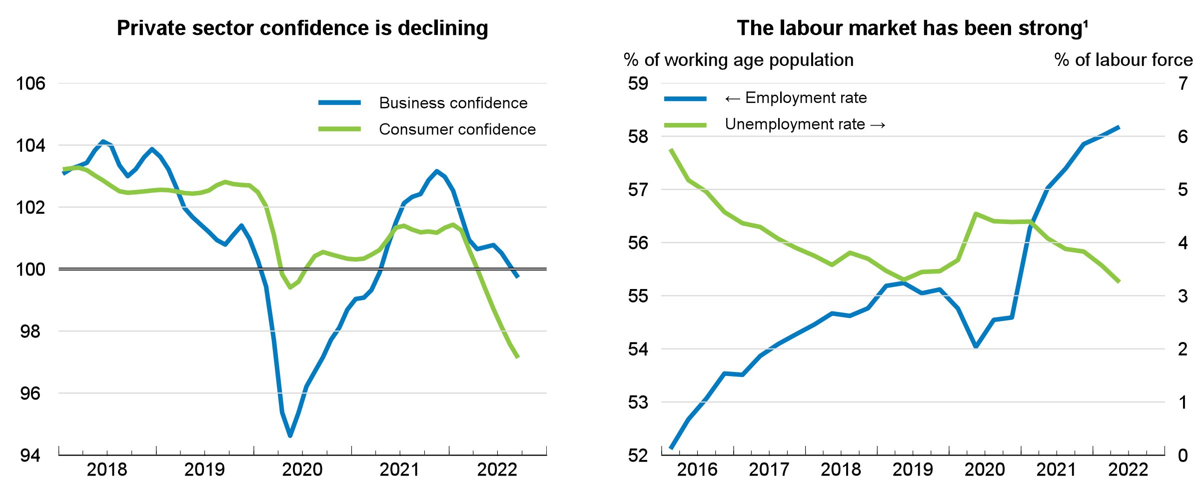
Growth is projected to decline from 6% in 2022 to 1.5% in 2023, before recovering to 2.1% in 2024. The slowing reflects persistently high inflation, the economic fall-out of Russia's war of aggression against Ukraine, weaker external demand and negative confidence effects. Private consumption is likely to be dampened by increasing unemployment and a deceleration of real wages. Business investment is projected to slow in the face of high interest rates and falling demand, although this is to be partly offset by higher public investment amidst an inflow of EU funds.

Further monetary tightening may be warranted to contain inflation. Fiscal policy will turn restrictive in 2023, but more restraint is needed to reduce inflationary pressures. Support to groups that are vulnerable to high energy prices and to improve the often-poor thermal efficiency of the housing stock should be financed through savings elsewhere. Productivity growth should be raised by accelerating the digitalisation of the economy, fostering competition in product markets, and strengthening labour mobility.

The economy is slowing in face of headwinds

Economic activity has been slowing in the second half of 2022 before turning negative under the impact of increasing inflation, high energy prices, higher interest rates and deteriorating consumer and business confidence. Retail sales have declined. Nonetheless, the labour market has remained strong with a stable unemployment rate of 3½ per cent over the summer – half a percentage point lower than a year earlier – underpinning strong wage growth. By mid-2022, private sector wages had increased 14% year-on-year. This contributed to pushing core inflation to 12.4% and, together with higher food and energy price, headline inflation to 21.1% in October.

Hungary



1. All persons aged 15 years and over.
Source: OECD Composite Leading Indicators database; and OECD Main Economic Indicators database.

StatLink https://stat.link/dy1oqu

Hungary: Demand, output and prices

Hungary	2019	2020	2021	2022	2023	2024
	Current prices HUF billion	Percentage changes, volume (2015 prices)				
GDP at market prices	47 664.9	-4.5	7.1	6.0	1.5	2.1
Private consumption	23 462.0	-1.2	4.9	7.3	1.1	2.0
Government consumption	9 564.8	-0.5	2.0	2.6	1.5	2.0
Gross fixed capital formation	12 873.3	-7.1	5.2	6.3	3.4	3.8
Final domestic demand	45 900.1	-2.7	4.3	6.0	1.8	2.5
Stockbuilding[1]	664.4	0.0	1.8	0.6	-0.2	0.0
Total domestic demand	46 564.5	-2.7	6.3	6.4	1.6	2.3
Exports of goods and services	38 868.6	-6.1	10.3	7.5	1.4	3.8
Imports of goods and services	37 768.3	-3.9	9.1	8.1	1.5	4.0
Net exports[1]	1 100.4	-2.0	1.1	-0.4	-0.2	-0.3
Memorandum items						
GDP deflator	_	6.4	6.3	13.7	11.9	5.4
Consumer price index	_	3.3	5.1	13.5	12.7	5.2
Core inflation index[2]	_	3.3	4.5	10.1	10.1	5.2
Unemployment rate (% of labour force)	_	4.1	4.0	3.5	4.7	5.2
Household saving ratio, net (% of disposable income)	_	10.5	9.5	6.2	4.6	6.5
General government financial balance (% of GDP)	_	-7.5	-7.1	-6.2	-5.6	-5.3
General government gross debt (% of GDP)	_	97.2	88.9	85.3	84.6	86.2
General government debt, Maastricht definition[3] (% of GDP)	_	79.3	76.8	73.3	72.6	74.2
Current account balance (% of GDP)	_	-1.1	-4.2	-5.6	-4.6	-4.6

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/1jecq8

Hungary imports about 95% of its gas and 45% of its oil and petroleum products from Russia. These shares are expected to remain unchanged with exemptions from EU sanctions. Starting in late 2021, the government has been introducing price ceilings for petrol, diesel and seven fundamental foodstuffs to combat fuel and food inflation. These measures are expected to reduce inflation by approximately 4 percentage points. In addition, the re-introduction of a 13th month of pension payment was completed. Almost 1.5 million refugees from Ukraine, equivalent to nearly 16% of the population, had arrived in Hungary by the end of August, which has led to temporary spending pressures on education, health care, and social assistance. Nearly 60,000 of these have obtained work permits, while many have moved on to other European countries.

Monetary policy continues to combat inflation

After raising the base rate from 11.75% to 13%, the central bank announced the end of its base rate increases in September 2022. Subsequently, monetary conditions were tightened by absorbing liquidity through higher reserve requirements and the introduction of longer instruments. In October, the effective monetary policy rate – the rate on overnight deposits – was increased to 18%, while the overnight lending rate (the upper bound of the interest rate corridor) was raised to 25% to contain market turbulence, leaving the base rate unchanged. As part of the broader unwinding of monetary support, the bank discontinued government bond purchase programmes and other crisis management programmes in late 2021. To anchor inflation expectations, the continued acceleration of inflation may necessitate higher policy rates for a limited period of time; these are assumed to reach up to one and a half percentage points. In 2022, fiscal policy was expansionary. Fiscal measures to tackle cost-of-living issues have been introduced. These include higher public sector wages, an income tax exemption for those under 25, a pension bonus and new tax reductions for households and businesses, financed to a large extent by higher taxes and spending restraint in other areas. In 2023 and 2024, fiscal policy will be restrictive as the temporary measures are phased out. Nonetheless, the public deficit will decline only gradually as the economy slows.

Growth will be restrained by inflation before picking up in 2024

The slowing of the economy in 2023 reflects the impact of high inflation and weaker external demand. Private consumption will hardly expand due to falling real disposable incomes. Exports are decelerating as export markets slow under the impact of high food and energy prices. Job creation will lose speed, contributing to higher unemployment and slower wage growth. Consumer price inflation will come down, although only slowly as the labour market remains relatively tight and as the depreciation of the forint adds to domestic inflationary pressures. Downside risks to growth include lower-than-projected wage moderation that would boost inflation, and the emergence of energy shortages. On the upside, a faster-than-expected recovery in export markets would stimulate domestic production.

Securing stronger growth

Additional fiscal tightening would alleviate inflation pressures and prepare public finances for future ageing-related spending pressures. Additional fiscal measures to combat the energy crisis should be focussed on groups most vulnerable to higher energy prices and on improving the often-poor thermal efficiency of the housing stock. Long-term productivity growth is weak. A more competition-friendly regulatory framework would strengthen competitive pressures, foster new market entry and help spur the adoption of new technologies. Labour reallocation and geographical mobility are important given the tight labour market but are held back by a rigid housing market and an underdeveloped rental market, in addition to remaining weaknesses in local transport and rural commuting infrastructure.

Iceland

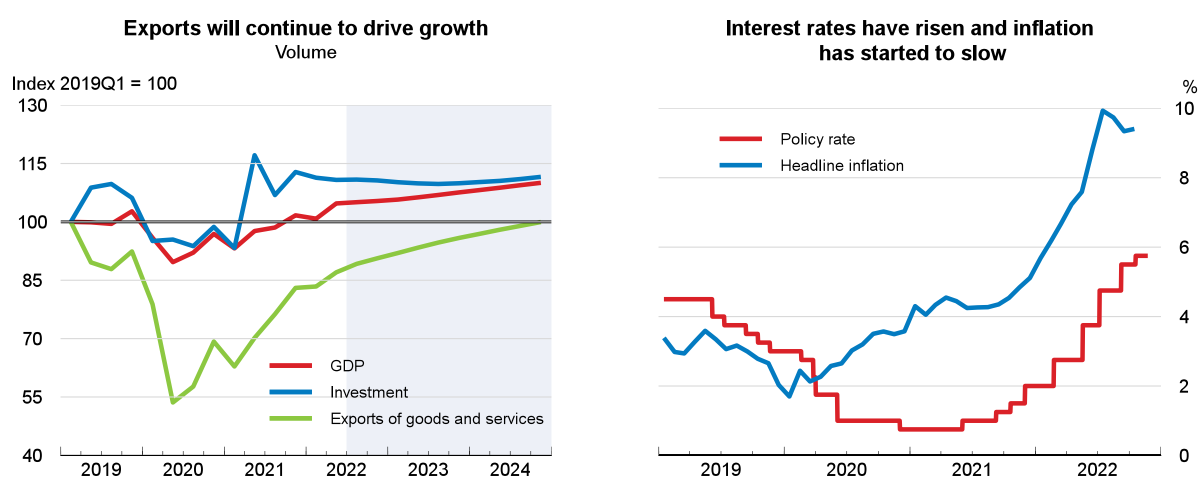
Economic growth will slow to 2.5% in 2023 and 2.3% in 2024. Private consumption will weaken as wage growth moderates and dissaving comes to an end. Business and housing investment are likely to decrease as financial conditions continue to tighten, and public investment will also decline in 2023-24. Export growth will remain strong thanks to robust growth of foreign tourism. The unemployment rate will rise gradually to around 4.5%. Headline inflation peaked at around 10% in late summer and is expected to subside over the projection period.

In early October, the central bank lifted the policy rate to 5.75%, the ninth increase since tightening started in May 2021. The bank is projected to tighten further to bring inflation back to target in due course. The fiscal consolidation planned for 2023-24 is appropriate to reduce inflationary pressures and maintain fiscal space. Investing in energy diversification and research and development could help improve energy security and achieve the government's climate targets.

Strong exports are driving the economy

Iceland's economy is growing rapidly, benefitting from rising exports of energy-intensive products, such as aluminium, which have been expanding steeply over the past few months. Foreign tourism is also recovering rapidly from its pandemic-induced collapse. Household consumption remains strong on the back of continued wage growth and dissaving, although real wages have started to decline in the wake of high inflation. Business investment is stalling as confidence declines and financial conditions tighten. The labour market remains tight, and labour shortages have become more apparent. Around 2 500 Ukrainian refugees (0.7% of the population) have found shelter in Iceland, with immediate access to the labour market.

Iceland



Source: OECD Economic Outlook 112 database; Central Bank of Iceland; and OECD database on Consumer Price Indices.

StatLink https://stat.link/k8nhwo

Iceland: Demand, output and prices

Iceland	2019	2020	2021	2022	2023	2024
	Current prices ISK billion	Percentage changes, volume (2015 prices)				
GDP at market prices	3 043.8	-6.8	4.4	6.4	2.5	2.3
Private consumption	1 519.5	-2.9	7.7	9.3	1.3	1.6
Government consumption	744.0	4.7	2.2	1.5	1.0	1.0
Gross fixed capital formation	648.3	-9.8	12.3	3.1	-0.9	0.8
Final domestic demand	2 911.8	-2.5	7.2	5.8	0.8	1.3
Stockbuilding[1]	- 5.4	0.9	-0.1	-0.3	-0.1	0.0
Total domestic demand	2 906.5	-1.7	7.0	5.5	0.7	1.3
Exports of goods and services	1 350.2	-29.9	12.7	19.8	7.3	4.8
Imports of goods and services	1 212.9	-21.5	20.3	17.7	3.7	2.8
Net exports[1]	137.4	-4.7	-2.7	0.5	1.8	1.1
Memorandum items						
GDP deflator	_	3.6	6.0	6.2	3.0	2.5
Consumer price index	_	2.8	4.4	8.3	5.5	2.9
Core inflation index[2]	_	2.9	4.4	7.9	5.4	2.9
Unemployment rate (% of labour force)	_	6.4	6.0	4.0	4.4	4.5
General government financial balance (% of GDP)	_	-8.8	-7.8	-4.1	-2.7	-2.2
General government gross debt[3]	_	70.3	76.6	78.3	79.7	80.8
Current account balance (% of GDP)	_	1.9	-1.6	-1.1	1.3	2.2

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. Includes unfunded liabilities of government employee pension plans.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/b3kizr

Fiscal and monetary policies are tightening

Monetary policy continues to tighten. In early October, the central bank raised the interest rate by 25 basis points to 5.75%, the ninth increase since the cycle started in May 2021. Consumer price inflation peaked at around 10% in late summer and is ebbing, as housing, food and commodity prices moderate. Inflation expectations are also subsiding. Since the spring of 2022, the krona has depreciated by almost 10% against the US dollar but has hardly moved against the euro. The central bank is projected to raise interest rates further to around 6¼ per cent in 2023 to bring inflation back to target.

Fiscal policy has already tightened and is projected to tighten further by around 3% of GDP in 2023 and 0.6% of GDP in 2024. This is appropriate to counter inflationary pressures and to build up post-pandemic fiscal space, although growth is projected to slow significantly. Gross public debt is projected to climb from around 78% of GDP in 2022 to around 81% in 2024, reflecting persisting fiscal deficits.

The economy will slow considerably

Economic growth is expected to moderate from 6.4% in 2022 to 2.5% in 2023 and 2.3% in 2024. Household consumption will slow as real wages continue to weaken. Tighter financial conditions and rising uncertainty will weigh on business investment. Energy-intensive sectors and services will drive export growth. Housing investment will recover in 2023 as pent-up demand from 2022 is realised, but it will abate in 2024 as higher interest rates bite, given the expanding share of variable-interest mortgages. Public investment will be cut as planned by the government. The unemployment rate will rise to around 4.5%. Inflation will decelerate in the wake of tighter policy, although it is projected to stay above target at the end of the projection period. The small size of the economy makes it volatile and vulnerable. Goods and service exports could suffer from a stronger-than-expected slowdown in major trading partners. Domestic shocks, such as a bad fishing season or a decline in viable fishing stocks, could reduce exports of marine products. Investment could take an additional hit if financial conditions worsen further and uncertainty about the impact of the war in Ukraine persists.

Investing in energy diversification and security is important

Iceland depends overwhelmingly on domestic, reliable and renewable energy sources, with geothermal and hydro power covering around 90% of energy demand, much more than in any other OECD country. The country is largely sheltered from the fallout of energy market imbalances, except for oil powered cars and the fishing fleet. To maintain energy security, the government should continue to support energy diversification, notably by supporting investment in wind energy and by reforming the regulatory framework for energy generation, transmission and distribution. Investing in low-carbon infrastructure would yield a double dividend by helping improve energy security and achieve climate targets.

India

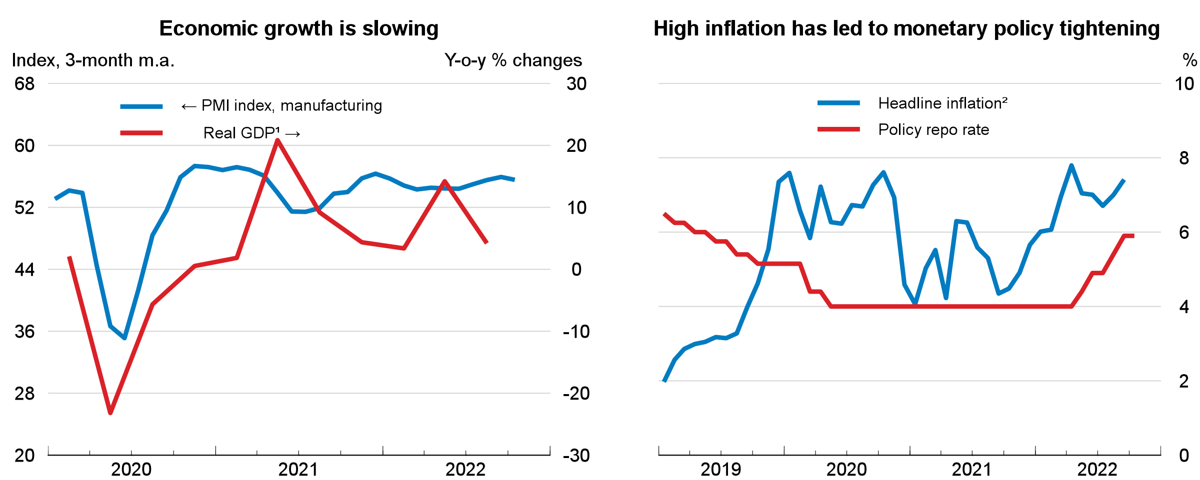
India is set to be the second-fastest growing economy in the G20 in FY 2022-23, despite decelerating global demand and the tightening of monetary policy to manage inflationary pressures. GDP growth will slow to 5.7% in FY 2023-24, as exports and domestic demand growth moderate. Inflation will crimp private consumption but moderate at the end of the projection period, helping, along with improved global conditions, to boost growth to 6.9% in FY 2024-25, in line with the 20-year average (excluding the COVID-19 recession). After a spike in 2022, the current account deficit will narrow as import price pressures abate.

High medium-term global uncertainty reinforces the importance of continued efforts to raise potential output growth and resilience. Macroeconomic stability should be pursued through monetary policy geared towards anchoring inflation expectations and fiscal policy oriented towards debt control and targeting of current and capital spending. Improvements in the business climate, when combined with financial deepening and skills development, can boost investment and infrastructure and create more and better jobs.

The strong recovery has slowed

Economic growth has lost momentum over the summer, due to a combination of erratic rainfall, which impacted sowing activities, and falling purchasing power. Concerns over demand conditions are considerable in services and infrastructure sectors, while consumers have become cautious regarding non-essential spending due to higher prices for food and energy. Tighter financial market conditions are weighing on the demand for capital goods, a leading indicator for aggregate investment. Export growth remains well-oriented, especially for services, and the progressive entry into force of comprehensive trade agreements with major partners is helping to improve prospects. Nonetheless, the monthly energy and food import bill keeps rising and the current account deficit widened in the July-September quarter to 2.9% of GDP. Headline inflation remains above 6% (the central bank's upper bound of the tolerance band), mostly due to the trend increase in the price of food (which in India accounts for a larger share of the consumer basket than in any other G20 country). Unemployment estimates suggest improving labour market conditions in both urban and rural areas, but there are few signs of a wage-inflation spiral.

India 1



1. Projected value for 2022Q3.
2. Headline inflation refers to the change in price of all goods in the basket. OECD seasonal adjustment based on monthly consumer price index (index 2012 = 100) from the Ministry of Statistics and Programme Implementation (MOSPI).
Source: OECD Economic Outlook 112 database; S&P Global; CEIC; and RBI.

StatLink https://stat.link/3bw71v

India: Demand, output and prices

India	2019	2020	2021	2022	2023	2024
	Current prices INR trillion	Percentage changes, volume (2011/2012 prices)				
GDP at market prices	200.7	-6.6	8.7	6.6	5.7	6.9
Private consumption	122.4	-6.0	7.9	17.7	6.5	7.2
Government consumption	22.0	3.6	2.6	5.3	8.2	8.1
Gross fixed capital formation	57.4	-10.4	15.8	6.9	4.6	6.3
Final domestic demand	201.8	-6.3	9.4	13.2	6.1	7.0
Stockbuilding[1,2]	4.2	-0.8	1.5	-0.3	0.0	0.0
Total domestic demand	205.9	-7.7	11.3	9.8	6.0	7.0
Exports of goods and services	37.5	-9.2	24.3	10.4	5.2	6.0
Imports of goods and services	42.7	-13.8	35.5	22.6	6.5	6.5
Net exports[1]	- 5.2	1.4	-2.9	-3.7	-0.8	-0.7
Memorandum items						
GDP deflator	_	5.6	10.0	10.8	9.7	9.4
Consumer price index	_	6.2	5.5	6.8	5.0	4.3
Wholesale price index[3]	_	1.3	13.0	12.5	11.7	11.5
General government financial balance[4] (% of GDP)	_	-13.3	-9.6	-7.5	-7.5	-6.1
Current account balance (% of GDP)	_	0.9	-1.2	-3.4	-3.0	-2.8

Note: Data refer to fiscal years starting in April.
1. Contributions to changes in real GDP, actual amount in the first column.
2. Actual amount in first column includes statistical discrepancies and valuables.
3. WPI, all commodities index.
4. Gross fiscal balance for central and state governments.
Source: OECD Economic Outlook 112 database.

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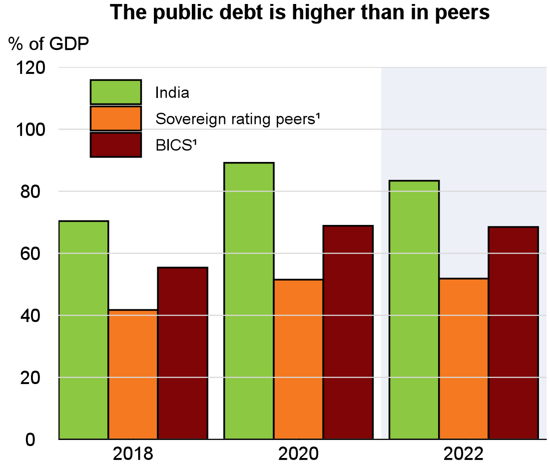
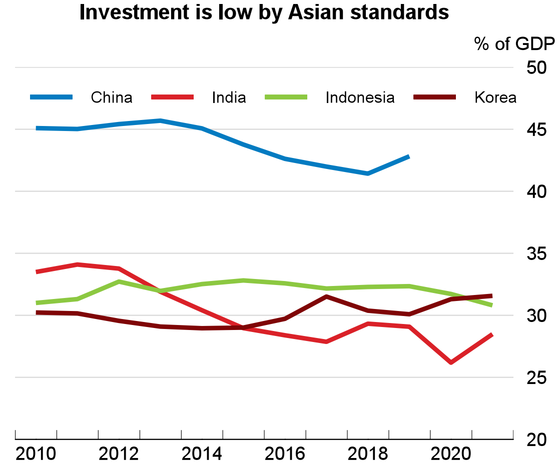
India 2





1. The unweighted average of general government debt ratio for similarly-rated countries (Bulgaria, Costa Rica, Hungary, Indonesia, Kazakhstan, Mexico, Malaysia, Peru, the Philippines, Romania, Thailand and Uruguay) and BICS countries (Brazil, Indonesia, China and South Africa).
Source: IMF (2022), World Economic Outlook, October; and World Bank, World Development Indicators.

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Global developments greatly influence the business climate. The share of India’s oil imports from Russia rose to 16% in April-August 2022 from 2% in FY 2021-22 and is expected to grow further. The reversal of capital flows has contributed to the rupee’s depreciation against the US dollar. On the fiscal front, the free food programme for the poor, the world’s biggest, has been extended several times (most recently, until end-2022), bringing the cost to almost USD 50 billion since April 2020 (2.6% of FY 2021-22 GDP). It is necessary to ensure that any increase in minimum dietary intakes is sustained once the intervention is phased out.

Macroeconomic policies are turning restrictive

In line with the central bank’s commitment to take calibrated action to bring headline inflation back within the 2-6% tolerance band and keep inflation expectations anchored, policy rates are expected to rise by 75bps, to reach 6.65% in February 2023 before the tightening cycle is paused. In fighting inflation, monetary policy is complemented by cuts in excise taxes and a series of measures taken by the government, such as the export bans on wheat, wheat flour, sugar and broken rice and a 20% export duty on some varieties of non-basmati rice. Such trade restrictions must be temporary, use transparent methodologies to determine their duration, and give due consideration to the effects on trading partners’ food security.

Expanding infrastructure spending, such as on highways and railways, occupies a central position in the government strategy. These programmes are being successfully implemented, surmounting some technical obstacles at the state level. At the same time, prolonged targeted and non-targeted fiscal measures and rising interest rates weigh on the public debt. On current trends, tax collection will surpass the budgeted projections by the end of FY 2022-23, due to higher inflation and better compliance, thus reducing borrowing requirements. The projections assume fiscal tightening in the next biennium. There still remain considerable margins to improve efficiency, accountability, and transparency of public spending, devoting more resources to health and education and building fiscal space to enhance resilience.

The economy will not escape the global slowdown

After hitting 6.6% in FY 2022-23, GDP growth is expected to slow in coming quarters, to 5.7% in FY 2023-24, before reverting to around 7% in FY 2024-25. CPI inflation will remain above the central bank’s upper limit target of 6% at least until early 2023 and then gradually recede as higher interest rates take effect. High inflation will slow household consumption and delay investment, as financing becomes more expensive, and exports will be affected by the economic slowdown in advanced countries and geopolitical tensions. Offsetting these forces, at least partially, some improvements can be expected as more contact-intensive services sectors normalise, including international tourism once borders are fully open and restrictions lifted.

Most risks to the projections are tilted to the downside and include a deterioration of banks’ assets quality, despite enhanced provisioning and the establishment of a ‘bad bank’, as well as possible delays in fiscal consolidation and in concluding bilateral trade negotiations. Declining geopolitical uncertainty, on the other hand, would boost confidence and benefit all sectors, as would faster-than-expected conclusion of free-trade agreements with key partners and the incorporation therein of services.

Progress in financial inclusion and energy security can be further extended

India has recorded impressive progress in recent years in extending access to financial services to a larger portion of the population, including disadvantaged socio-economic groups. Leveraging the country's competitive strength in ICT, the Unified Payments Interface (UPI) and other tools are easing the transition towards a cashless economy. Nonetheless, gaps and challenges in the usage of financial services are still considerable: in particular, roughly a third of bank accounts are inactive. In order to enhance energy security, the use of LED bulbs in private and public spaces can have sizeable effects (savings of more than 4% of electricity final consumption per year); important results have been achieved and further actions are needed to develop appropriate financial instruments (for example, the Treasury is expected to debut on the green bonds market with a forthcoming INR 160 billion issue), test new business models and strengthen institutional capacity.

Indonesia

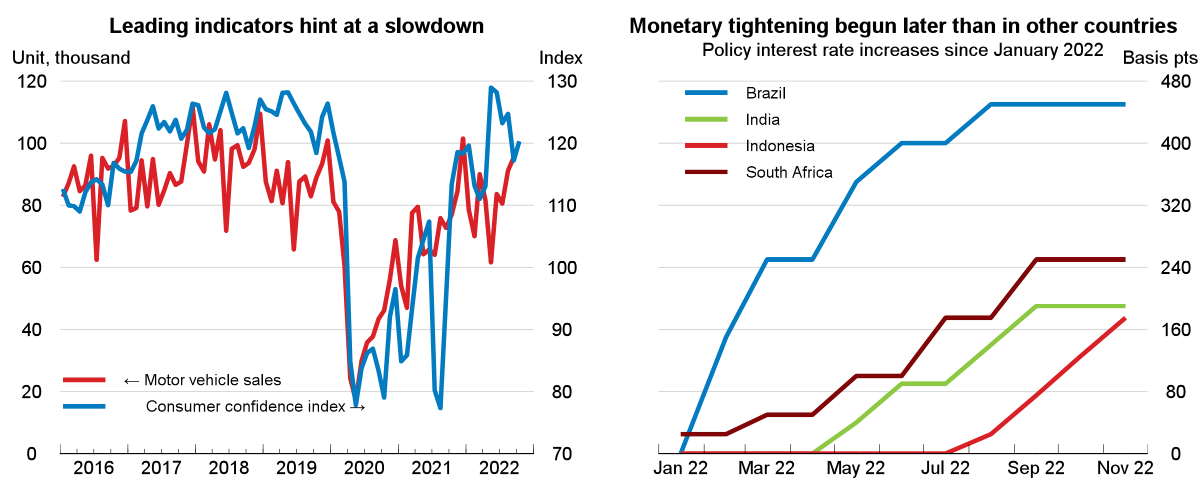
Favourable commodity prices and still buoyant capital inflows are helping Indonesia to resist strong global headwinds. However, domestic demand and private consumption growth is being held back by high headline inflation. With foreign investors recognizing the progress made towards macroeconomic stability and enhanced structural reforms, and expanding their reach in Indonesia, GDP growth is projected to average around 5% in 2022 and 2023 and strengthen slightly in 2024. Persistent tensions on energy, fertiliser and food markets and social unrest ahead of the February 2024 presidential elections are the main downside risks.

Fiscal and monetary policies should remain tight, while support for vulnerable households should be maintained. In the medium run, the overarching imperative remains to spur productivity growth through appropriate human capital policies, the removal of obstacles to business activity and the restructuring of state-owned enterprises (SOEs). It is also important to reinforce the independence and professionalism of the Indonesia Investment Authority, the recently-established sovereign wealth fund. On the upside, the impact on potential output of reforms enacted in recent years to liberalise labour markets may turn out to be larger than expected.

Recent developments provide mixed signals

Growth accelerated in the first three quarters of the year: domestic demand was buoyant as mobility restrictions to curb COVID-19 cases were withdrawn and external trade was supported by the rise in global prices for commodities such as coal, palm oil, and nickel (a critical component in electric vehicle batteries). In US dollars, exports over the year to September 2022 were 36% higher than in the previous year. A recovery in tourism is underway (boosted by the broadening of visa-on-arrival procedures), although the number of visitors remains below pre-pandemic levels.

Indonesia 1



Source: CEIC; and OECD Economic Outlook 112 database.

StatLink https://stat.link/1xwtqz

Indonesia: Demand, output and prices

Indonesia	2019	2020	2021	2022	2023	2024
	Current prices IDR trillion	Percentage changes, volume (2010 prices)				
GDP at market prices	15 832.7	-2.1	3.7	5.3	4.7	5.1
Private consumption	9 171.9	-2.7	2.0	5.0	4.4	5.3
Government consumption	1 394.6	2.0	4.2	-3.4	4.6	1.1
Gross fixed capital formation	5 121.4	-5.0	3.8	4.0	3.9	5.7
Final domestic demand	15 687.9	-3.1	2.8	3.9	4.3	5.1
Stockbuilding[1]	215.2	-0.5	0.1	0.1	0.3	0.0
Total domestic demand	15 903.1	-3.6	2.8	4.0	4.6	5.0
Exports of goods and services	2 943.5	-8.1	24.0	20.0	10.2	10.6
Imports of goods and services	3 013.9	-16.7	23.3	17.1	10.8	11.4
Net exports[1]	- 70.4	1.4	1.0	1.5	0.4	0.4
Memorandum items						
GDP deflator	_	-0.4	6.0	10.9	11.2	9.5
Consumer price index	_	1.9	1.6	4.2	4.1	2.5
Private consumption deflator	_	1.9	1.7	4.9	5.2	3.4
General government financial balance (% of GDP)	_	-5.4	-5.8	-4.2	-2.9	-2.4
Current account balance (% of GDP)	_	-0.4	0.3	1.0	0.9	1.1

1. Contributions to changes in real GDP, actual amount in the first column.
Source: OECD Economic Outlook 112 database.

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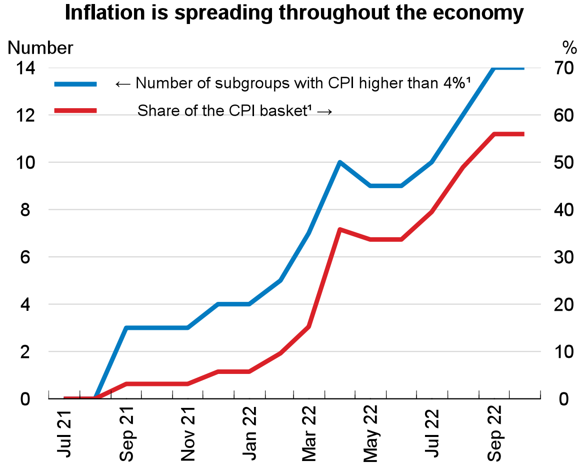
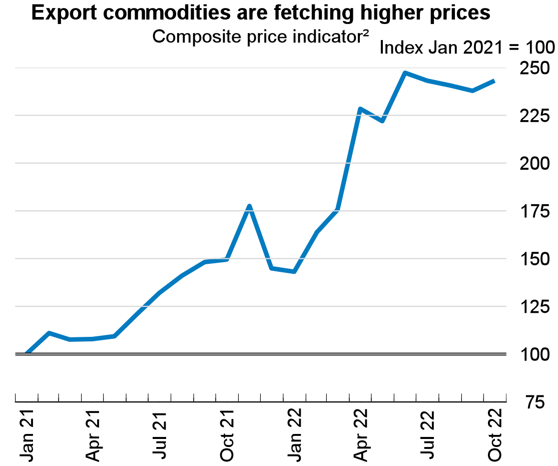
Indonesia 2

Inflation is spreading throughout the economy



Export commodities are fetching higher prices



1. In total there are 43 subgroups. The cumulated share of the subgroups with inflation exceeding 4% in the total inflation basket is calculated with the constant weights (Index 2018 = 100).
2. The price indices for individual commodities (palm oil, coal, iron ore and gold) are aggregated by using weights based on the share of each commodity in the total 2020 exports of these commodities.
Source: Statistics Indonesia; Ministry of Energy and Mineral Resources; and World Bank Commodity Markets Outlook.

StatLink https://stat.link/ftrh1s

Price pressures continue to build, with annual CPI inflation reaching 6% in September and core inflation settling at 3.2%. The number of product categories in the consumer basket experiencing high inflation has also grown. Bank Indonesia started increasing its policy rate (seven-day repo reverse rate) in August 2022. Since the summer, most high-frequency indicators and sentiment surveys have stalled, but there have not been any major capital outflows: foreign multinationals have maintained their expansion plans, the stock market is the best performing in the Asia-Pacific region this year, and currency depreciation against the US dollar has been less pronounced than in other emerging Asian economies.

Indonesia, the world's largest thermal coal exporter, has gained considerable market share in new overseas markets following the introduction of EU sanctions on Russian energy exports. At the same time, oil and gas imports have almost doubled in value since the Russian invasion of Ukraine. The government is considering purchasing oil from Russia at a discount. The principal tool used to cushion the impact of the crisis has been the universal fuel subsidy, with additional resources equal to IDR 502 trillion (4.5% of 2021 GDP). In addition, direct cash assistance (BLT) and wage subsidies (BSU) targeted programmes now reach 21 and 16 million citizens, respectively.

Fiscal and monetary policies should remain tight

The 2023 Budget aims to bring down the deficit to the 3% of GDP ceiling set in the Constitution. The main forces acting are increasing tax revenue (+30% from pre-pandemic levels) and declining spending (-4% from the 2022 Budget, with most cuts in healthcare). Nonetheless, various socio-economic groups, such as youth, women, remote villagers, and people with disabilities, remain vulnerable to post-pandemic scarring effects and the rise in inflation. It is therefore opportune to provide them with sufficient welfare support, to make it well-targeted, and to improve the social assistance delivery system.

Over the years, thanks to its legal independence, Bank Indonesia has acquired the necessary credibility to pursue front-loaded, pre-emptive, and forward-looking monetary policy normalisation at a more gradual pace than in other emerging market economies. From 5.25% at end-2022, the policy rate is expected to rise by 25 basis points in early 2023 and to remain unchanged throughout the projection period. So far, most financial indicators point to greater resilience than during previous episodes of global turmoil and banks have built an adequate level of provision against non-performing loans, which are likely to see an increase once most regulatory forbearance is phased out early next year. However, interest payments on public debt absorb a relatively high share of Indonesia’s budget, reflecting Indonesia’s low tax effort, and the Treasury is exposed to foreign-exchange fluctuations.

Steady growth is projected to persist

External demand for commodities and pent-up consumption will support growth. In 2023, despite heightened global uncertainty, demand for export commodities is projected to remain brisk. Although macroeconomic policy support is set to wither as real interest rates turn positive and fuel subsidies are trimmed, domestic demand will benefit from pent-up consumption and a gradual increase in capital spending. The 30% increase in fuel prices due to reduced subsidies is contributing to the initial acceleration of core inflation as higher energy costs spread through the economy. With monetary tightening and the base-year effect of higher inflation in the first half of 2022 wearing off, inflation expectations will eventually decrease. This will allow consumer price inflation to fall to the upper value of the target band of 3±1% in the second half of 2023.

Risks remain tilted to the downside and include a slower-than-projected taming of inflation, with the ensuing purchasing power losses weighing on household consumption and political turbulence and social unrest in the run-up to 2024 Presidential elections which might distort international investors' perception of the strengths of the Indonesian economy.

Sound macroeconomic policies and structural reforms can boost productivity

The fiscal-monetary synergy approach that authorities have adopted since 2020, consisting of large private placements of government bonds with Bank Indonesia and the central bank's purchases of Treasury paper in the primary market, should be progressively wound down to avoid fiscal dominance and crowding out private investment. Indonesia's productivity level remains stuck at a fraction of the OECD average and state-owned enterprises – given their sheer size and reach – could make a greater contribution in this regard. The consolidation of 108 companies into 41 in 12 business clusters, where they may develop sufficient size and efficiency to compete in global markets, and the planned partial privatisation of operating subsidiaries of the national oil company are encouraging. The Indonesia Investment Authority can also play a positive role in attracting foreign capital and therefore accessing high-productivity technologies, provided it remains immune from political interference. For Indonesia to reach the 2060 net zero goal, clean energy investment needs to nearly triple by 2030. Greenhouse gas emissions can be lowered through a consistent strategy to reduce reliance on cooking with inefficient heat sources.

Ireland

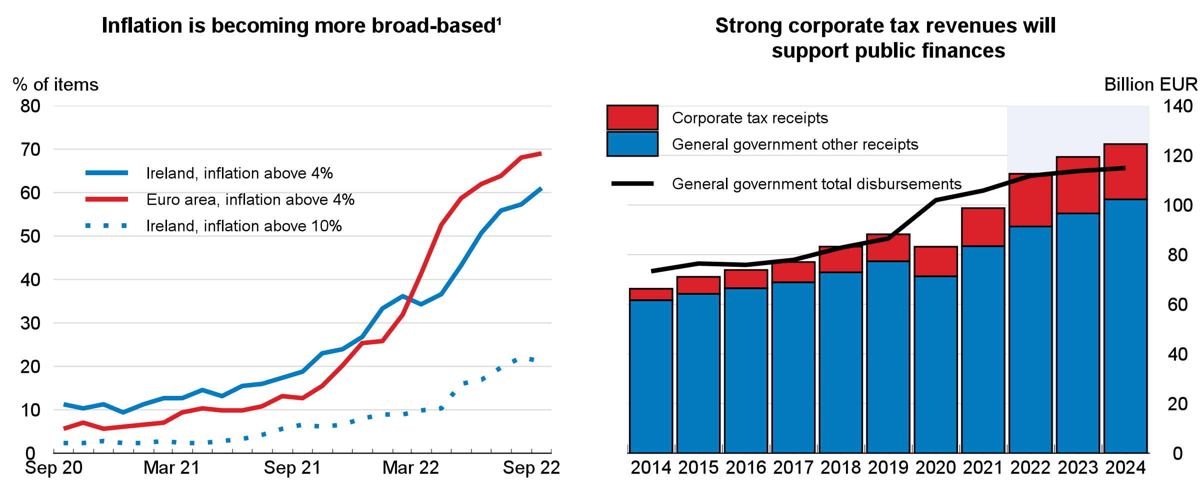
GDP growth is projected to exceed 10% in 2022, following the full relaxation of pandemic-related restrictions early in the year. Falling real incomes due to high inflation will hold back consumer spending up to mid-2023, despite significant wage growth. High costs and low confidence will reduce firms' incentives to invest. Modified domestic demand will thus only grow by 0.9% next year, before rebounding by 3.1% in 2024. As exports in multinational-dominated sectors, though moderating, will remain supportive, GDP is projected to grow by 3.8% in 2023 and 3.3% in 2024.

On the back of record-high tax receipts, boosted by multinationals' large profits and labour market resilience, the government announced a wide set of measures to support households and SMEs against high inflation in 2022-23. If needed, further measures should be targeted and temporary. The welcome decision to allocate part of the windfall corporate tax revenues to the National Reserve Fund should be continued in the event of further windfall gains. Reverting to the new spending rule, after temporarily deviating from it in 2022 and 2023, would move fiscal policy onto a more stable spending path.

Rising prices are lowering real household incomes

The full relaxation of pandemic-related restrictions in early 2022 led to a rebound in consumer and domestic firms' capital spending in the second quarter. On the back of higher energy prices and supply chain constraints, pent-up demand lifted inflation to a record high of 9.6% in June. Recent retail sales and credit card payments data suggest weaker consumer spending in the third quarter, as rising prices hit households' real incomes, despite sizeable wage growth amidst tight labour market conditions.

Ireland



1. Calculations based on a common set of 213 sub-indices.
Source: Eurostat; and OECD Economic Outlook 112 database.

StatLink https://stat.link/c1h205

Ireland: Demand, output and prices

Ireland	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2020 prices)				
GDP at market prices	355.7	5.6	13.4	10.1	3.8	3.3
Private consumption	104.2	-11.9	4.5	5.7	1.3	3.1
Government consumption	42.8	10.3	6.1	2.5	-0.3	-0.8
Gross fixed capital formation	193.5	-17.0	-39.1	2.7	4.1	3.1
Final domestic demand	340.5	-12.4	-18.0	4.9	2.1	2.3
Stockbuilding[1]	4.3	0.5	0.4	0.3	-0.6	0.0
Total domestic demand	344.8	-12.1	-18.0	4.1	1.0	2.4
Exports of goods and services	455.7	11.1	14.0	12.5	5.4	4.0
Imports of goods and services	444.8	-2.2	-8.3	9.4	4.7	3.8
Net exports[1]	10.9	16.9	27.9	7.9	3.0	1.9
Memorandum items						
Modified total domestic demand[2], volume	_	-4.8	5.9	8.0	0.9	3.1
GDP deflator	_	-0.5	0.4	6.1	4.1	1.9
Harmonised index of consumer prices	_	-0.5	2.4	8.4	7.2	2.9
Harmonised index of core inflation[3]	_	-0.1	1.7	4.8	4.6	3.0
Unemployment rate (% of labour force)	_	5.8	6.2	4.7	5.3	5.1
Household saving ratio, net (% of disposable income)	_	21.8	20.2	16.8	14.6	12.4
General government financial balance[4] (% of GDP)	_	-5.0	-1.7	0.2	1.1	1.7
General government gross debt (% of GDP)	_	72.1	65.9	59.8	56.2	52.9
General government debt, Maastricht definition[5] (% of GDP)	_	58.2	55.4	49.4	45.7	42.5
Current account balance (% of GDP)	_	-6.8	14.2	16.4	18.9	18.7

1. Contributions to changes in real GDP, actual amount in the first column.
2. Excludes airplanes purchased by leasing companies in Ireland but then operated in other countries and investment in imported intellectual property by multinationals.
3. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
4. Includes the one-off impact of recapitalisations in the banking sector.
5. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/1g7uar

Consumer and energy price inflation were high in October, at respectively 9.6% and 48% year-on-year, according to preliminary estimates. Furthermore, inflationary pressures have become more broad-based with 5.1% core inflation in September. Soaring prices of energy and other essentials disproportionately affect poorer households – particularly elderly, youths and lone parents. Likewise, elevated input costs coupled with reduced demand pose a threat to SMEs relying on household discretionary spending. Hence, in September, the government introduced a wide package of partly one-off budgetary measures (2.6% of GDP) – about 40% of which is targeted, aimed at supporting households and SMEs against high inflation in 2022-23.

Windfall tax revenues will boost public finances

High corporate tax receipts, which accounted for one fifth of government revenues in 2021, are supporting public finances. Whilst the recently introduced spending rule, which caps annual primary spending growth at 5%, is set to be temporarily breached in 2022 and 2023, due to the cost of the adopted fiscal packages, the budget position is expected to reach a balance this year and a surplus in 2023. Given the potentially transient nature of corporate tax revenues, the decision to put EUR 6 billion of windfall tax gains in the National Reserve Fund by 2023 is welcome. The wide set of cost-of-living measures announced in September, ranging from targeted welfare payments, tax measures, and an SME energy support scheme to universal energy credits and temporarily reduced indirect taxes, will help the most exposed households and businesses in 2022-23. Public investment support through the National Development Plan will partly offset weaker private business and residential investment. Budget 2023 also allocates EUR 2 billion to support Ukrainian refugees, whose numbers topped 62 000 by early November (1.2% of Ireland's population). Public support is set to be scaled back in 2024, as economic conditions improve.

Risks to domestic activity are considerable

Higher inflation and uncertainty, exacerbated by Russia's invasion of Ukraine, will weigh on domestic activity. Real income losses will hold back household consumption from end-2022 to mid-2023, despite government support and strong wage growth. Consumer spending is projected to strengthen somewhat thereafter, as inflationary pressures gradually recede thanks to reduced energy prices and the rebalancing of supply chains, which will also support business investment. With core inflation still relatively high in 2024, risk-averse households are likely to keep savings well above pre-pandemic levels. On the external side, exports of multinational-dominated high-growth sectors will continue to support GDP growth, albeit less, as exports of medical products ease in 2024. More elevated input and funding costs than assumed might further delay domestic firms' investment and the government's plans to boost housing supply and residential retrofitting. Lingering uncertainties around the full implementation of Brexit agreements could further weigh on firms' competitiveness. Moreover, renewed instances of non-delivery of contracted electricity generation, on the back of surging demand from datacentres, might increase the risk of supply disruptions and weigh on growth.

Sustainable public finances are needed to deliver on long-term reforms

Long-term fiscal sustainability is key to the effective delivery of the government's investment-intensive reform agenda to ensure a just climate transition, as well as affordable quality housing and health services. In this context, allocating any future windfall tax gains to the National Reserve Fund is warranted. In addition, structural reforms will be required for sustainable and resilient growth. Overhauling planning, permit and judicial review regulations could help speed up needed investment in network and renewable generation capacity and housing. The design of policy schemes to shield businesses and consumers from high energy prices should avoid undermining incentives for energy savings.

Israel

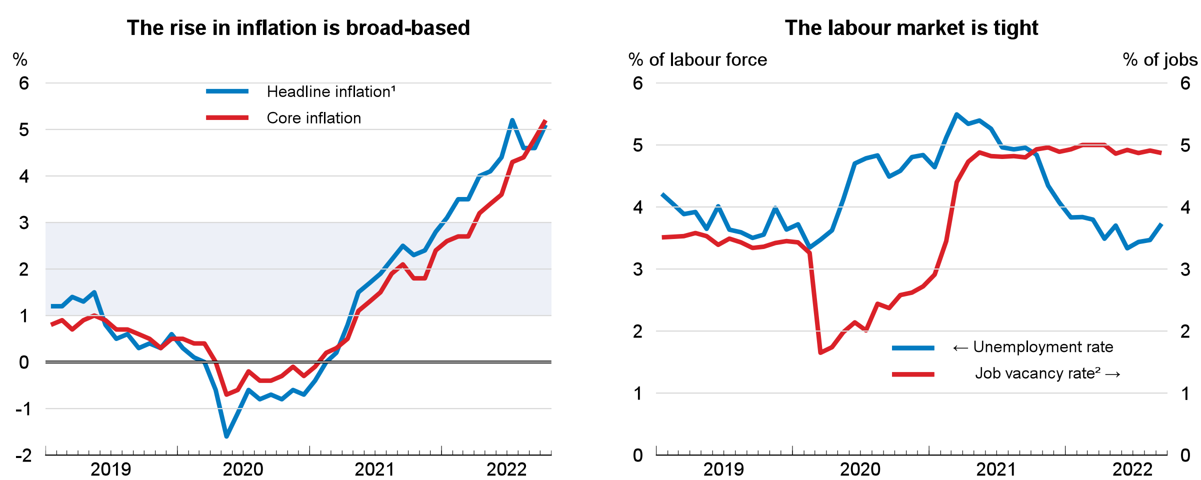
GDP growth is projected to moderate from a strong 6.3% in 2022 to 2.8% in 2023 and 3.4% in 2024. The global slowdown is set to weaken demand from Israel's trading partners. Elevated inflation will slow disposable income and private consumption. Increasing interest rates and lower stock market valuations will weigh on investment. Growth is projected to pick up towards its potential rate in 2024 as inflation abates. Risks are skewed to the downside, and particularly related to a continuation of Russia's war of aggression against Ukraine.

The gradual tightening of monetary policy should continue in order to bring inflation back into the target range. Fiscal policy should avoid adding to inflationary pressures while allowing for temporary and targeted support to households and firms most affected by rising costs. Recent reforms to reduce tariff and non-tariff import barriers are welcome and should continue. The expansion of renewable energy should be promoted by removing administrative barriers and investing in storage and transmission capacity.

Economic activity is robust

GDP growth moderated to 2.1% (annualised quarterly rate) in the third quarter of 2022. Private consumption contracted slightly, but investment expanded robustly. Confidence in the business sector remains positive. The labour market is tight, with employment above pre-crisis levels. The vacancy rate has stabilised at a historically high level in recent months. Consumer price inflation, at 5.1% in October, is lower than in most OECD countries, but is above the central bank's 1-3% target range. Inflation has become increasingly broad-based, with about three-quarters of the components of the consumer price index growing faster than the central bank's target. One year-ahead inflation expectations are around 3%. Real wages have declined somewhat in recent months, despite robust nominal wage growth.

Israel



1. Shaded area is the Bank of Israel's inflation target range (i.e. 1-3%).
2. The job vacancy rate measures the proportion of total posts that are vacant, expressed as the ratio of the number of job vacancies to the number of occupied posts plus the number of job vacancies.
Source: OECD Consumer Price Statistics database; and Israel Central Bureau of Statistics.

StatLink https://stat.link/a6r0jw

Israel: Demand, output and prices

Israel	2019	2020	2021	2022	2023	2024
	Current prices NIS billion	Percentage changes, volume (2015 prices)				
GDP at market prices	1 434.6	-1.8	8.5	6.3	2.8	3.4
Private consumption	751.1	-7.9	11.1	6.9	2.8	4.0
Government consumption	316.5	2.8	4.3	0.8	1.7	1.2
Gross fixed capital formation	325.0	-3.8	11.5	8.9	4.1	5.1
Final domestic demand	1 392.7	-4.5	9.5	6.0	2.9	3.7
Stockbuilding[1]	9.7	1.2	0.5	1.0	-0.1	0.0
Total domestic demand	1 402.3	-3.3	9.9	6.8	2.7	3.6
Exports of goods and services	420.3	-2.7	14.5	8.6	3.5	2.7
Imports of goods and services	388.0	-8.1	20.7	13.0	3.1	3.0
Net exports[1]	32.3	1.4	-0.8	-0.8	0.2	0.0
Memorandum items						
GDP deflator	_	1.0	2.2	4.4	2.4	1.8
Consumer price index	_	-0.6	1.5	4.3	3.3	2.2
Core inflation index[2]	_	-0.1	1.2	3.8	3.5	2.2
Unemployment rate (% of labour force)	_	4.3	4.9	3.6	3.8	4.0
General government financial balance (% of GDP)	_	-10.7	-3.8	-0.2	-0.7	-1.0
General government gross debt (% of GDP)	_	70.6	67.8	61.8	59.7	57.9
Current account balance (% of GDP)	_	5.4	4.3	3.4	3.3	3.1

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/twv5ax

Russia's war of aggression against Ukraine continues to put pressure on global energy and food prices, although energy price effects in Israel are more limited given the country's self-sufficiency in natural gas. The war weighs on demand from trading partners in the short term. In the medium term, Israel may benefit from increased defence exports and natural gas exports to Europe. Immigration from Ukraine and Russia has increased significantly, accounting for around 0.3% of the population in July. The pronounced decline in technology stock markets since the beginning of the year is weighing on financing conditions for the high-tech sector.

Macroeconomic policy is tightening

The central bank has raised the policy rate five times in 2022, from 0.1% to 2.75%. Quantitative easing measures, including the purchase of government bonds, ended in late 2021. The central bank has signalled that the pace of further interest rate increases will be determined by inflation and activity developments. The OECD projections assume that the policy rate will reach 4.25% in the second quarter of 2023 and remain at that level until the end of the projection horizon. The budget deficit continued to narrow considerably in 2022 thanks to the phasing out of pandemic support and strong revenue growth. Revenue growth is expected to slow as the recovery moderates and some transitory factors, related to high real estate valuations and surging corporate profits, dissipate. Measures taken to mitigate the increase in the cost of living, such as an expansion of the earned income tax credit and child tax allowances, as well as temporary reductions of coal and transport fuel excise taxes, are estimated to cost around 0.7% of GDP in 2022. A budget for 2023 has not yet been submitted due to the political situation. The projections assume that some support measures will be extended in 2023 before being largely phased out in 2024, with the fiscal stance being broadly neutral in both years.

Growth is set to moderate

The global slowdown will lower demand from Israel's trading partners. Elevated inflation is weighing on disposable income and private consumption growth. The increase in real interest rates and high uncertainty are set to slow investment. The labour market will slightly cool as growth moderates. Inflation should gradually slow towards the mid-point of the central bank target, supporting a pick-up in domestic demand in 2024. A prolonged conflict in Ukraine could adversely affect the economy through more persistent inflation and lower external demand. An increase in security incidents could heighten uncertainty, weighing on consumption and investment.

Policy support should be temporary and targeted

Consumer price inflation above the central bank's target range and robust domestic demand call for a continuation of the gradual tightening of monetary policy. Fiscal policy should remain tight so as not to add to inflationary pressures and not to require even tighter monetary policy. Additional fiscal policy support to mitigate the increase in energy prices and broader costs of living, if needed, should be temporary and well targeted on the most vulnerable households and firms, be aligned with environmental goals and preserve energy savings incentives. Boosting renewable energy is needed to accelerate the green transition but requires investment in transmission and storage infrastructure as well as removing administrative barriers. Recent reforms to reduce tariff and non-tariff import barriers, including for foods, are welcome as they can both reduce the cost of living and spur competition and productivity.

Italy

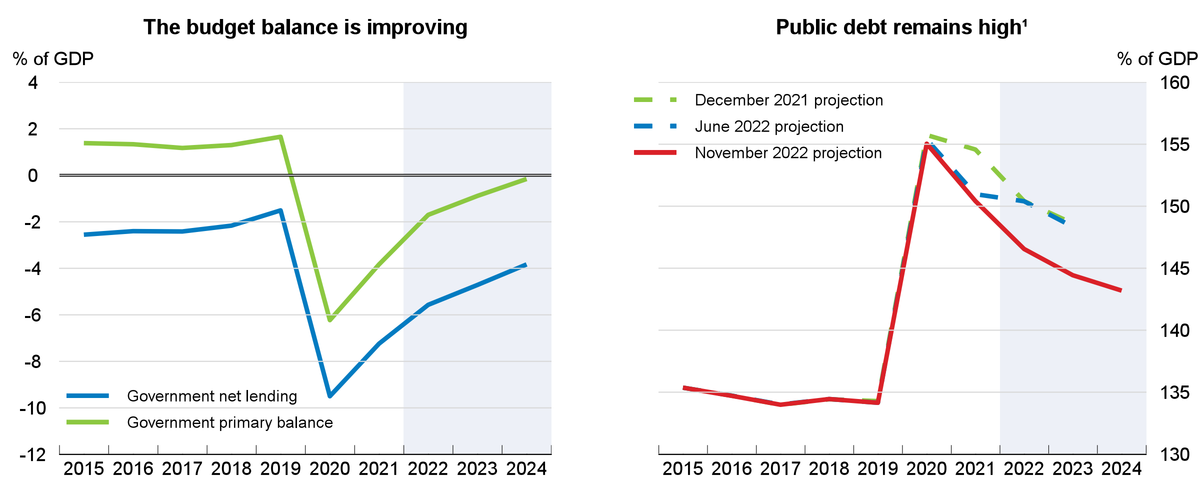
Real GDP growth is projected at 3.7% in 2022, slowing to 0.2% in 2023, before picking up moderately to 1% in 2024. High energy prices will act as a brake on production in energy-intensive industries, while falling real incomes due to high inflation, increasing interest rates and subdued export market growth will moderate demand growth. Unemployment will rise and labour market participation decline, with employment shrinking in 2023. Consumer price inflation is expected to come down only gradually from about 10% at the end of 2022, as energy price caps are phased out in 2023 and recent increases in energy and food prices are triggering wider price pressures.

Monetary policy tightening will partly be offset by higher public investment related to the National Recovery and Resilience Programme. Timely implementation of new investments, reform of the competition law and the effective targeting of energy crisis support measures will be paramount to sustain activity in the short term and to lay the ground for sustainable growth in the medium term.

Activity is slowing

Following strong growth over the first three quarters of 2022, recent high-frequency indicators point to a decline in activity. Industrial production has been resilient, but retail sales and confidence indicators have been weakening. Employment has been trending down recently, although unemployment has continued to recede. Overall, the recent weakness of activity indicators, rising borrowing costs and the erosion of real household incomes related to high inflation are driving a turning point in activity.

Italy 1



1. Gross public debt, Maastricht definition.
Source: OECD Economic Outlook 112 database; OECD Economic Outlook 110 database; OECD Economic Outlook 111 database; and OECD calculations.

StatLink https://stat.link/0zmcfk

Italy: Demand, output and prices

Italy	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	1 796.5	-9.1	6.7	3.7	0.2	1.0
Private consumption	1 074.8	-10.4	5.1	3.4	0.2	0.5
Government consumption	334.5	0.0	1.5	0.0	-0.7	-0.4
Gross fixed capital formation	323.2	-8.2	16.5	8.7	0.9	3.3
Final domestic demand	1 732.6	-8.0	6.5	3.8	0.2	0.9
Stockbuilding[1]	3.5	-0.5	0.3	0.6	0.0	0.0
Total domestic demand	1 736.1	-8.5	6.8	4.4	0.2	0.9
Exports of goods and services	569.3	-14.2	13.5	10.4	1.8	3.2
Imports of goods and services	508.8	-12.7	14.8	12.9	1.7	2.9
Net exports[1]	60.5	-0.9	0.1	-0.5	0.0	0.1
Memorandum items						
GDP deflator	_	1.6	0.5	3.2	4.9	2.7
Harmonised index of consumer prices	_	-0.1	1.9	8.1	6.5	3.0
Harmonised index of core inflation[2]	_	0.5	0.8	3.2	4.3	3.1
Unemployment rate (% of labour force)	_	9.3	9.5	8.1	8.3	8.5
Household saving ratio, net (% of disposable income)	_	10.3	7.6	4.0	3.0	2.4
General government financial balance (% of GDP)	_	-9.5	-7.2	-5.6	-4.7	-3.8
General government gross debt (% of GDP)	_	185.1	174.3	170.5	168.3	167.2
General government debt, Maastricht definition[3] (% of GDP)	_	155.0	150.4	146.5	144.4	143.3
Current account balance (% of GDP)	_	3.9	3.1	-0.3	-0.8	-0.7

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

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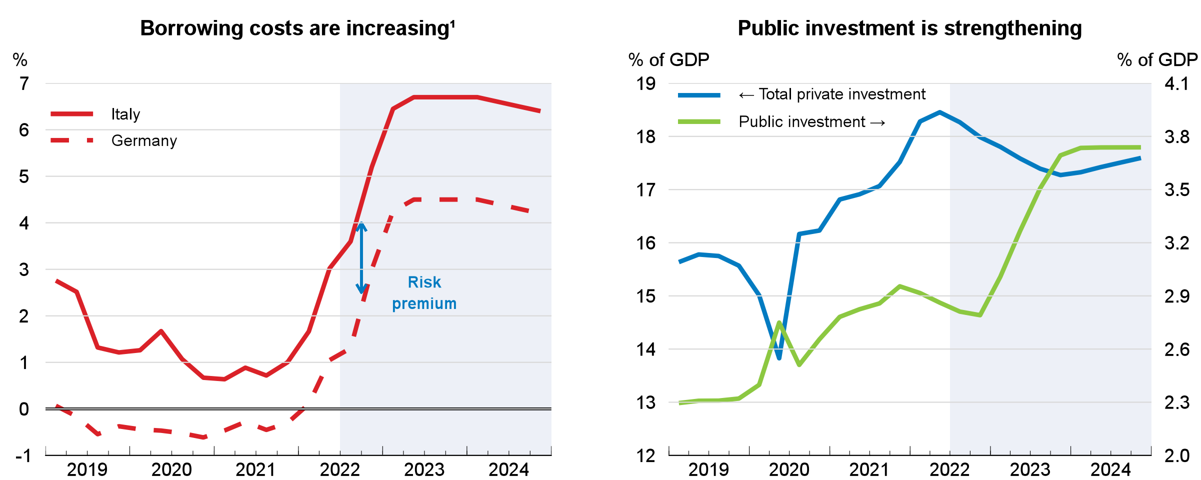
Italy 2



1. 10-year interest rates.
Source: OECD Economic Outlook 112 database; and OECD calculations.

StatLink https://stat.link/u68le2

Large price increases for energy and agricultural commodities on international markets are being passed on to domestic inflation, which approached 13% in October. The substitution of Russian natural gas has been rapid but increases in energy and food prices have triggered wider price pressures, with core inflation around 5½ per cent in October.

Monetary policy is tightening, but fiscal policy remains supportive

The tightening of euro area monetary policy is having significant effects on financial conditions in Italy. This implies higher borrowing costs for the government, households and businesses even though the risk premium on long-term Italian government bonds over German bonds is projected to remain constant.

In order to cushion the impact of inflation on households and businesses, the government has taken fiscal measures amounting to around 3½ per cent of GDP in 2022. This includes tax credits for firms with large increases in gas and electricity bills, reductions of fixed charges on gas and electricity, as well as targeted income support for low-income households. These measures are likely to continue, although the Budget for 2023 has been delayed by the elections. It is assumed that fiscal measures in 2023 will strike a balance between supporting the economy and fiscal prudence, with current measures being extended over the winter months and then gradually withdrawn by mid-2023, resulting in fiscal savings of about 2% of GDP over the full year relative to 2022. At the same time, the expected ramp-up of spending related to Next Generation EU by 1½ per cent of GDP relative to 2022 will boost public investment. Overall, the combination of tighter financial conditions and mildly supportive fiscal policy in early 2023 is expected to limit the risks of second-round effects on inflation from higher wage growth and help prevent a persistent contraction of activity over 2023. Public sector wage growth, which will be a key determinant of inflation and the fiscal position, is expected to remain contained over 2023 and 2024.

Growth will pick up only slowly, with risks tilted to the downside

Real GDP is anticipated to contract in late 2022, before picking up moderately over 2023 and 2024. On the supply side, increases in input prices are expected to curtail production, especially in energy-intensive sectors. On the demand side, high inflation and declining employment are eroding real incomes despite significant energy crisis support, while the sharp slowdown in export market growth and increasing interest rates are weighing on private investment. As public investment increases strongly in 2023 and inflation gradually recedes on the back of stabilising commodity prices, real income growth and activity should gradually pick up over 2023 and 2024. However, the upturn may remain modest, with energy crisis support measures gradually phased out despite energy prices remaining exceptionally high, and the full effects of higher real interest rates on activity starting to kick in.

Risks and uncertainties are larger than usual and tilted to the downside. While energy rationing is unlikely even in the event of a complete cut-off of Russian natural gas, delays in implementing the National Recovery and Resilience Programme could weigh on public investment and larger-than-expected monetary policy tightening in the euro area could further push up the risk premium on Italian long-term government securities. This would not only lead to a further tightening of financial conditions in the private sector but also raise debt-servicing costs on high public debt. Even though short-term public debt dynamics have been favourable over the past year – largely reflecting higher-than-anticipated nominal GDP growth – and the average maturity of public debt is long, this could lead to a deterioration in debt dynamics in the long term. On the upside, the effective implementation of structural reforms related to the National Recovery and Resilience Programme could have a larger-than-anticipated positive effect on productivity in the short term.

Efficient spending of Next Generation EU funds will be key to support growth

Improving the effectiveness of public administration will be a key priority to support demand in the short term and boost productivity in the long term. This is particularly the case for the Next Generation EU funds, where efficient implementation, management and prioritisation of public investment will be paramount for a timely delivery of quality projects. To reap the full benefits of the National Recovery and Resilience Programme, public investment should be coupled with effective implementation of structural reforms, especially the recent competition law reform. While the diversification of natural gas supplies away from Russia over the past year is welcome, accelerating the transition to renewable energies would have the added benefit of making Italy less dependent on fossil fuel supply from abroad and making growth more sustainable. Effectively targeting energy crisis support measures and reducing the recourse to broad-based price caps would encourage energy savings while preserving the incomes of the most vulnerable households.

Japan

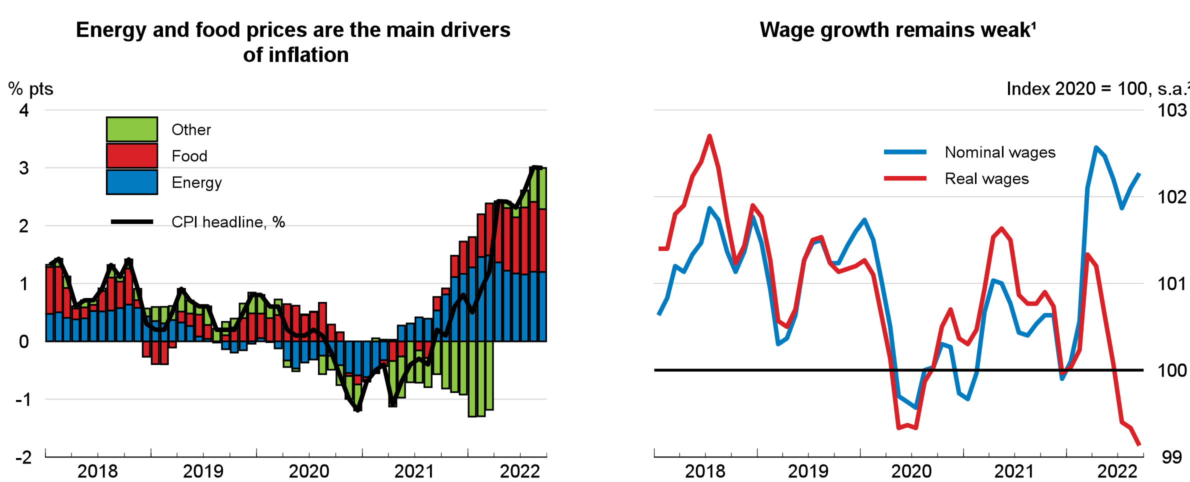
Real GDP growth is projected at 1.8% in 2023 and 0.9% in 2024. The new economic policy package will support domestic demand, partly offsetting subdued household confidence and real income. Loss of momentum in trading partner economies will moderate exports. After peaking in the course of 2022, headline consumer price inflation will fall back in late 2023 as energy prices stabilise, but then gradually increase again towards 2% in 2024 as wage growth gains momentum. The labour market will continue to tighten gradually, with the unemployment rate falling to 2.4% in 2024.

The measures to protect the most vulnerable households and firms in the face of higher prices should be temporary and more targeted. Monetary policy will remain accommodative but yield curve control is projected to be eased near the end of the projection period, when inflation reaches its target sustainably, accompanied by stronger wage growth. The latest economic package will also support longer-term growth, with investment in skills, digitalisation and the green transition. Diversifying energy sources, increasing the share of renewables and enhancing the electricity grid would improve energy security.

External pressures are weighing on the domestic demand-driven recovery

The 7th wave of COVID-19, starting from late June 2022, recorded the highest number of infections and deaths, but no confinement measures were introduced, limiting the impact on economic activity. In addition, border controls for foreign travellers have been gradually eased and were fully lifted in October. However, increasing prices have affected consumer sentiment. Energy and food prices remain the biggest driver of headline consumer price inflation, which reached 3% in August and September. However, cost increases have been only partly passed through into prices, and government measures, such as price caps on oil, have helped keep inflation relatively muted. The labour market has been tightening, but wage growth remains sluggish.

Japan 1



1. Nominal wages are total cash earnings per employee. Real wages are nominal wages deflated by the consumer price index excluding imputed rent.
2. Three-month moving average.
Source: Ministry of Internal Affairs and Communications; Ministry of Health, Labour and Welfare; and OECD calculations.

StatLink https://stat.link/xwf783

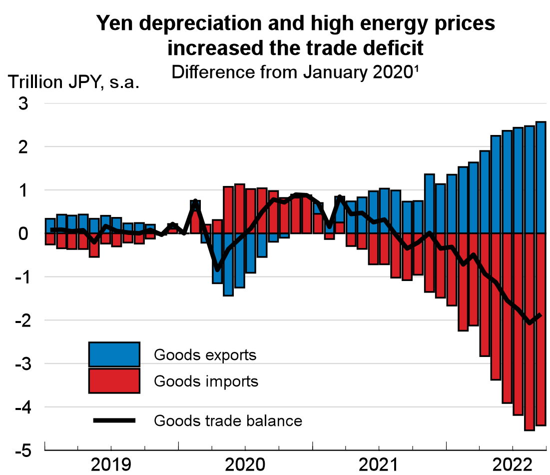
Japan: Demand, output and prices

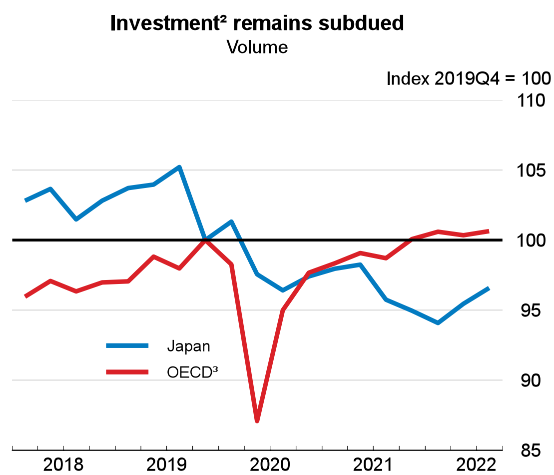
Japan	2019	2020	2021	2022	2023	2024
	Current prices YEN trillion	Percentage changes, volume (2015 prices)				
GDP at market prices	558.2	-4.6	1.6	1.6	1.8	0.9
Private consumption	304.6	-5.2	1.3	2.9	1.4	1.1
Government consumption	111.3	2.3	2.1	1.8	0.1	-0.9
Gross fixed capital formation	142.5	-4.9	-1.5	-1.0	3.7	1.6
Final domestic demand	558.4	-3.7	0.8	1.7	1.7	0.8
Stockbuilding[1]	1.4	-0.1	-0.2	0.4	-0.1	0.0
Total domestic demand	559.8	-3.8	0.6	2.1	1.6	0.8
Exports of goods and services	97.4	-11.6	11.8	4.6	2.9	2.2
Imports of goods and services	99.0	-6.7	5.1	7.4	2.4	1.8
Net exports[1]	- 1.6	-0.8	1.0	-0.6	0.0	0.0
Memorandum items						
GDP deflator	_	0.9	-0.9	-0.3	1.2	1.6
Consumer price index[2]	_	0.0	-0.2	2.3	2.0	1.7
Core consumer price index[3]	_	0.1	-0.7	0.3	1.6	1.7
Unemployment rate (% of labour force)	_	2.8	2.8	2.6	2.5	2.4
Household saving ratio, net (% of disposable income)	_	12.1	8.7	6.1	3.8	2.3
General government financial balance (% of GDP)	_	-9.0	-5.5	-6.7	-5.9	-4.3
General government gross debt (% of GDP)	_	241.3	241.6	248.0	250.6	251.8
Current account balance (% of GDP)	_	2.9	4.0	1.8	1.1	0.9

1. Contributions to changes in real GDP, actual amount in the first column.
2. Calculated as the sum of the seasonally adjusted quarterly indices for each year.
3. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/hbtan1

Japan 2





1. The trade deficit in January 2020 was JPY 0.06 trillion.
2. Gross fixed capital formation.
3. Moving nominal gross fixed capital formation weights, using purchasing power parities.
Source: Ministry of Finance; OECD Economic Outlook 112 database; and OECD calculations.

StatLink https://stat.link/9ch853

While domestic demand is recovering slowly but steadily, external demand has been volatile. Supply chain disruptions arising from Russia's war of aggression against Ukraine and China's zero-COVID-19 measures have held back production, investment and exports. Furthermore, widening policy interest rate differentials with other advanced economies have led to additional yen depreciation, adding upward pressures on the prices of imported energy, food and raw materials. The impact of currency depreciation on imports has been larger than that on exports, increasing the trade deficit and decreasing corporate profits and incomes for firms dependent on imports while boosting those of exporting firms. The government has reacted strongly to the shock, with a set of measures worth JPY 3.5 trillion (0.6% of GDP) in September to moderate the price surge and support vulnerable households and businesses. This includes the extension of the subsidy for the oil price cap until the end of December, the freezing of the government selling price of imported wheat at the April level, a one-off special cash benefit to low-income households, and a special grant to local governments to help them support vulnerable households and businesses. Energy security concerns have also given an impetus to the ongoing discussions on putting nuclear power reactors back into service, most of which were suspended after the accident in Fukushima.

Fiscal measures are moderating the impact of external shocks

Some of the measures in the new economic policy package announced at the end of October, such as a further extension of the oil price cap subsidy until September 2023 and the introduction of new schemes to reduce electricity and utility gas bills from January to September 2023 (JPY 6.3 trillion, 1.2% of GDP), aim to moderate prices. The package also includes medium-term expenditures to strengthen local economies, to boost investment in human capital, digitalisation and the green transition, and to bolster economic security. The related supplementary budget will be around JPY 30 trillion (5.5% of GDP), but includes contingency reserve funds and expenditures expected to be implemented over multiple years. Hence, the near-term impact of the subsidies, especially for R&D and investment, is expected to be limited. The OECD projections assume that pandemic-related measures will be phased out, and that the one-off cash benefit will not be renewed, while the main measures for moderating energy and food prices, notably the price subsidies, will remain in place but gradually decline over time. Without additional revenues, the substantial additional expenditures will worsen the fiscal balance, and the debt-to-GDP ratio will continue to increase to unprecedented levels.

Consumer price inflation has exceeded the 2% target for several months and forex interventions have been carried out since September with a view to reduce exchange rate volatility. At the same time, the Bank of Japan announced the continuation of its current accommodative stance, mentioning that recent inflation is driven by external factors and that wage pressures remain weak. So far, yield curve control, maintaining 10-year Japanese government bond yields at around zero within a range of plus or minus 0.25 percentage point, has been kept unchanged. The projections assume that the yield curve control framework will start to be eased slightly, by allowing a steeper slope without changing the short-term rate, at the end of the projection period when the Bank's criteria on inflation and wage growth will be met.

The economic recovery will continue, but downside risks have risen

GDP growth is projected at 1.8% in 2023, supported by the new economic policy package. Nevertheless, low confidence and real disposable incomes will hold back private consumption. Weak external demand and high import prices will weigh on trade. Despite a fall in confidence and external demand, private investment will substantially increase due to government subsidies, especially those supporting green and digital investment. GDP growth will decline to 0.9% in 2024, which is still above potential. This reflects lower domestic demand, as pandemic-related support is fully phased out, government spending declines and business investment normalises, following the post-pandemic rebound. Headline consumer price inflation will continue to remain elevated until early 2023 due to increasing food prices and higher energy costs, but government support measures will dampen the impact on consumers. As the output gap closes, inflation is projected to increase to the 2% target at the end of 2024. The unemployment rate will continue to decline. Wage growth, while set to remain subdued in the near term, will gain momentum as the labour market tightens.

A key source of uncertainty is the impact on domestic demand of rising inflation from yen depreciation and energy price increases. Weaker-than-expected external demand and further supply chain disruptions due to new COVID-19 shocks or geopolitical uncertainty could threaten energy security and depress trade, production and investment. On the upside, further yen depreciation could strengthen the price competitiveness of exports, including inbound tourism.

Accelerating structural reforms will be critical to boost productivity and wages

If downside risks materialise, further fiscal measures to support vulnerable households and businesses should be temporary and more targeted. Prolonged price caps add to fiscal sustainability challenges and could reduce incentives to shift to renewables and lower energy demand by distorting market signals. Securing and reallocating employment, global supply chains and energy sources are high priorities both in the short and longer term. Continuing “work-style” reforms, expanding social security coverage for non-standard workers, and enhancing vocational training and education could boost labour productivity and labour supply and offset the effects of an ageing population. Lowering barriers to foreign workers and foreign direct investment would also help. Faster progress with the digital and green transformation is needed, which will be supported by the new economic policy package. However, higher permanent government expenditures without additional revenues will worsen fiscal sustainability and threaten sustainable growth. It is important to either set out a clearer roadmap to achieve the fiscal consolidation target by FY 2025 or to reconsider the earlier plan on account of the ongoing crisis and define a new credible target underpinned by a specific set of measures. Fiscal consolidation efforts should resume on both the expenditure and the revenue side, including social security and tax system reforms, as the recovery strengthens. As further rapid changes in economic conditions might trigger a revision to the monetary policy framework, the Bank of Japan should continue to communicate its current and future monetary stance clearly and in a timely manner.

Korea

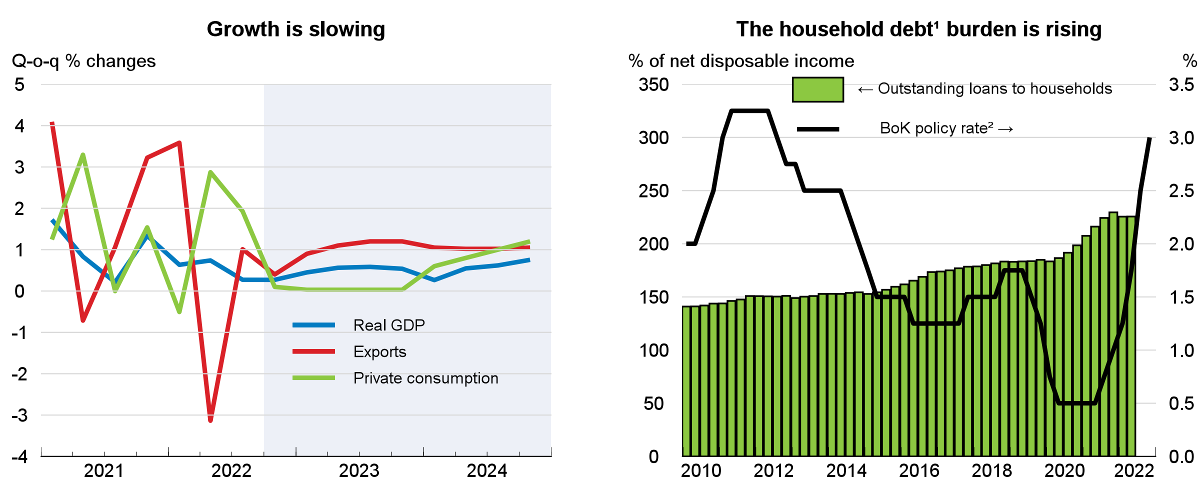
GDP growth is projected to reach 2.7% in 2022 and to slow to just under 2% in 2023 and 2024. In response to weak disposable income growth and a sluggish housing market, private consumption and investment are set to lose momentum. Declining semiconductors sales will weigh on exports in the short term. Unemployment is set to increase from the current low rate, and inflation will remain elevated for some time.

Monetary policy tightening should continue to re-anchor inflation expectations. Fiscal consolidation should proceed gradually with support moving from broad-based measures towards targeting people vulnerable to rising living costs and enhancing incentives for energy savings. Reducing gaps in social protection and reforming pensions to secure adequate retirement income in a fiscally sustainable framework are key priorities in this respect. Structural reforms should facilitate a reallocation of labour and capital to expanding sectors and strengthen competition to address productivity gaps between large and small companies.

The economy faces headwinds

Growth has lost momentum. Real annualised GDP growth fell to 1.1% in the third quarter of 2022 mainly driven by subdued exports growth. Private consumption had grown robustly, but has slowed amid high inflation. Customs exports declined by 6% (year on year, in USD) in October 2022 due to lower global demand for semiconductors, and headwinds from China's zero-COVID-19 policy. Headline consumer price inflation moderated to 5.7% in October 2022 from its 6.3% peak in July. Inflation expectations have peaked, but remain well above the 2% inflation target. Core inflation stood at 4.2% in October as service prices continued to rise. Employment has recovered to pre-crisis levels. Unemployment has started rising but remains historically low.

Korea



1. Household debt has been calculated using the Bank of Korea's Flow of Funds statistics.
2. Bank of Korea policy rate for the last month of each quarter, except for 2022Q4, where it refers to thepolicy rate in October.
Source: OECD Economic Outlook 112 database; and Bank of Korea.

StatLink https://stat.link/krm9q8

Korea: Demand, output and prices

Korea	2019	2020	2021	2022	2023	2024
	Current prices KRW trillion	Percentage changes, volume (2015 prices)				
GDP at market prices	1 924.5	-0.7	4.1	2.7	1.8	1.9
Private consumption	935.9	-4.8	3.7	4.7	1.8	2.2
Government consumption	328.7	5.1	5.6	3.4	0.5	0.8
Gross fixed capital formation	579.0	3.5	2.8	-1.3	1.1	2.2
Final domestic demand	1 843.6	-0.4	3.8	2.5	1.3	1.9
Stockbuilding[1]	27.1	-0.8	-0.1	0.2	0.2	0.0
Total domestic demand	1 870.7	-1.2	3.6	2.7	1.6	1.9
Exports of goods and services	755.9	-1.7	10.8	4.5	2.3	4.5
Imports of goods and services	702.1	-3.1	10.1	4.6	2.5	4.4
Net exports[1]	53.8	0.5	0.7	0.1	0.0	0.0
Memorandum items						
GDP deflator	_	1.6	2.5	2.1	2.3	1.9
Consumer price index	_	0.5	2.5	5.2	3.9	2.3
Core inflation index[2]	_	0.4	1.4	3.6	3.5	2.0
Unemployment rate (% of labour force)	_	3.9	3.6	2.8	3.3	3.2
Household saving ratio, net (% of disposable income)	_	14.7	5.9	0.4	1.0	1.4
General government financial balance (% of GDP)	_	-2.7	-0.8	0.2	0.7	0.9
General government gross debt (% of GDP)	_	50.0	50.5	50.3	49.3	48.9
Current account balance (% of GDP)	_	4.5	4.9	1.6	1.2	1.0

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/nhkvsi

Although the direct impact of Russia's war of aggression against Ukraine has been relatively modest, given limited direct trade and financial links, global energy prices have driven up inflation. Electricity and gas prices were raised by 5% and 16% respectively in October and are set to increase further. Currency depreciation has pushed up import prices.

Macroeconomic policies are tightening

The Bank of Korea has raised the key policy rate in eight steps from 0.5% to 3.0% since August 2021 to try and keep inflation expectations in check. Further policy rate increases are expected in the near term, with the OECD projection assuming increases until the first quarter of 2023. Meanwhile, policymakers should keep an eye on the rising debt of households and small businesses. To relieve the burden of soaring energy prices, the government extended a temporary fuel tax cut until the end of 2022 and plans to expand energy voucher support for vulnerable households. Fiscal policy is expected to be tightened from 2023 in line with the government's fiscal consolidation plan. The 2023 budget proposal built in a cut in the managed budget deficit (excluding social security), to 2.6% of GDP from 5.1% of GDP in 2022, mainly by reducing pandemic supports. The recently-proposed fiscal rule limits the managed budget deficit to 3% of GDP. The fiscal stance is assumed to be broadly neutral in 2024.

Growth is projected to weaken

Real GDP growth is on course to reach 2.7% in 2022 and is expected to slow to just under 2% in 2023 and 2024. Inflation and higher interest rates will dampen private consumption. Weak global demand is set to weigh on exports. Inflation will remain high for some time in 2023 due to service and utility price pressures but will gradually moderate. The rising debt servicing burden increases the risk of accelerating the housing price correction and may trigger corporate failures, posing downside risks to consumption and investment. Increasing protectionism, such as rising tensions between the United States and China, Russia's war against Ukraine and potential further geopolitical tensions may trigger realignments of Korean supply chains. Easing geopolitical tensions, relaxation of China's zero-COVID-19 policy or faster-than-foreseen expansion of contact-intensive services could improve the economic outlook.

Structural challenges call for policy action

Fiscal consolidation should proceed, and the proposed fiscal rule should be adopted by the National Assembly to help reduce inflationary pressures and prepare for rapid population ageing. Policy should move from broad-based crisis support and energy price support toward targeting households and businesses vulnerable to rising living costs, and ensure that incentives for energy savings are enhanced. Stepping up training and activation policies for those who lose their job and strengthening the social safety net would facilitate workforce reallocation. Reducing the stringency of product market regulation would help to lower productivity gaps between large and small firms and reduce labour market dualism. The government initiative to reform pensions is welcome and should help to secure adequate retirement income and fiscal sustainability. In addition to the government's renewed promotion of nuclear energy, steps should be taken to align Korea's emission trading scheme (ETS) with climate targets. Improving the institutional framework for electricity supply would allow the marginal carbon cost to pass through, enhancing the effectiveness of the ETS for electricity generation.

Latvia

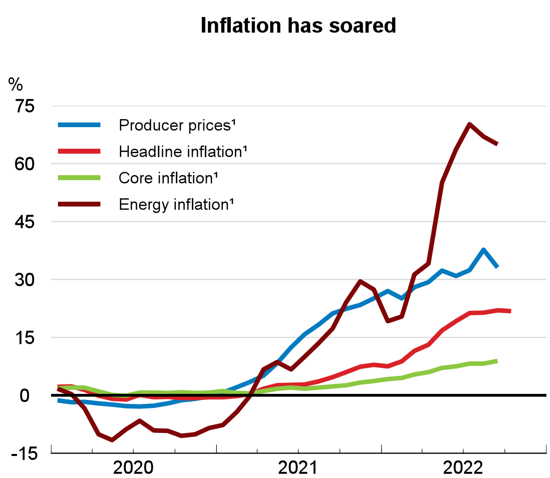
Economic growth will slow to 2.3% in 2022 and -0.2% in 2023, before rebounding to 2.3% in 2024. The negative confidence shock that followed Russia's invasion of Ukraine as well as very high and broad-based inflation are weighing on private consumption. Business investment will continue to slow due to high uncertainty and worsening financial conditions, while high energy prices and lower external demand weigh on industrial production. Inflation will reach 17% in 2022 in year average terms and decline only gradually, to 10.7% in 2023 and 5% in 2024.

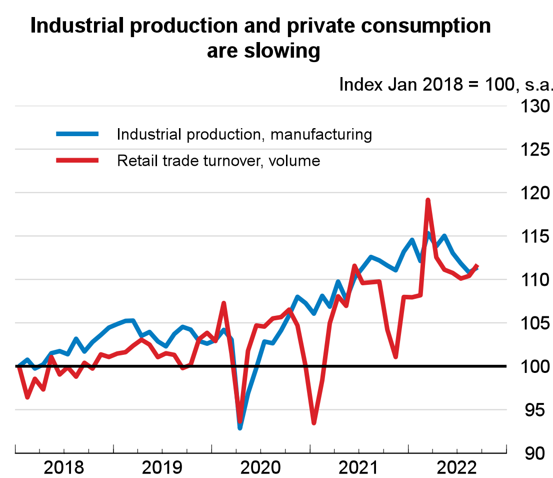
Fiscal policy will become less supportive as most pandemic-related spending is phased out. Support measures to mitigate the impact of higher energy prices should be better targeted to limit additional inflationary pressure on non-energy components and incentivise energy savings. Creating fiscal space to increase public investment in energy security and support structural change is key. Active labour market policies should be expanded to reduce skill mismatches and facilitate job reallocation.

The economy is slowing due to high inflation and uncertainty

GDP declined by 1.7% (seasonally adjusted quarterly rate) in the third quarter of 2022. Business confidence has fallen since Russia's war of aggression against Ukraine began. Consumer price inflation reached 21.8% in October, mainly driven by energy and food prices, whose share in the consumption basket is considerably higher than in the euro area. Nonetheless, electricity tariffs fell in October as a price cap was introduced. Inflation has become broad-based: prices of about 70% of the CPI basket rose by more than 4% in September. The unemployment rate declined in the first half of 2022 but remained unchanged in the third quarter while the vacancy rate remained elevated, reflecting skills mismatches.

Latvia





1. Headline inflation refers to the harmonised index of consumer prices, core inflation refers to the harmonised index of consumer prices excluding food, energy, alcohol and tobacco, energy inflation refers to the harmonised index of consumer prices of energy goods, producer prices refer to the producer prices index for all industry.
Source: OECD Prices database; and Statistical Central Bureau of Latvia.

StatLink https://stat.link/az5o83

Latvia: Demand, output and prices

Latvia	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	30.7	-2.2	4.1	2.3	-0.2	2.3
Private consumption	17.9	-4.6	8.2	5.5	-2.0	1.9
Government consumption	6.0	2.4	4.4	2.4	2.0	1.8
Gross fixed capital formation	7.1	-2.6	2.9	0.8	1.7	4.5
Final domestic demand	30.9	-2.9	6.1	3.7	-0.5	2.4
Stockbuilding[1]	0.0	1.0	4.0	0.3	0.7	0.0
Total domestic demand	30.9	-2.2	9.6	4.2	0.2	2.2
Exports of goods and services	18.4	-0.3	5.9	6.6	-1.0	2.5
Imports of goods and services	18.6	-0.3	15.3	9.3	-0.3	2.3
Net exports[1]	- 0.2	0.0	-5.4	-2.0	-0.5	-0.1
Memorandum items						
GDP deflator	_	1.0	6.9	13.1	6.9	4.2
Harmonised index of consumer prices	_	0.1	3.2	17.0	10.7	5.0
Harmonised index of core inflation[2]	_	0.9	1.9	7.2	6.9	4.5
Unemployment rate (% of labour force)	_	8.1	7.5	6.7	7.0	6.8
Household saving ratio, net (% of disposable income)	_	6.3	5.9	1.5	2.2	2.6
General government financial balance (% of GDP)	_	-4.3	-7.0	-6.5	-4.1	-2.4
General government gross debt (% of GDP)	_	54.4	57.5	61.3	63.9	64.6
General government debt, Maastricht definition[3] (% of GDP)	_	42.0	43.6	47.4	50.0	50.8
Current account balance (% of GDP)	_	2.6	-4.2	-4.0	-4.3	-4.4

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/y7ms8j

Latvia has been particularly vulnerable to the war in Ukraine because of its high dependence on imported Russian oil and gas. Russia provided almost 100% of Latvia's gas needs, although the reliance on Russia in total energy supply was much smaller (about 26%). As Latvia has secured enough gas reserves to satisfy demand over the 2022/2023 winter by switching to other energy sources and relying on imported liquefied gas, economic activity should not be hindered by gas rationing. Exports of goods to Russia, Belarus and Ukraine accounted for 9.8% of Latvia's exports in 2021. This share has declined to about 7.6% on average since March 2022. At the same time, the total value of exports increased by 30%, reflecting a successful reorientation of trade to other countries.

Fiscal policy is tightening

Fiscal policy will be contractionary due to the phasing-out of substantial COVID-19 support measures, declining from 6.9% of GDP in 2021 to 3.7% in 2022 and 0.8% in 2023. The government has introduced new measures to shield households and firms from rising electricity and heating prices, including non-targeted price-caps, transfers to pensioners and low-income families and grants to energy-intensive firms. These are expected to amount to about 2% of GDP and to be partially phased out in 2024. The government has also provided crucial support to the more than 30 000 Ukrainian refugees (1.7% of Latvia's population) who entered Latvia since the beginning of the crisis. Defence spending will rise from 2.2% of GDP in 2022 to 2.5% by 2025. Latvia will receive about 6.7% of its 2020 GDP in grants from the Next Generation EU fund by 2026, one-third of which is expected to be spent in 2023 and 2024.

Economic growth will slow while inflation remains high

High inflation and uncertainty will reduce private consumption, especially during the forthcoming winter due to higher utility bills. Exports will decline in 2023 due to weak external demand. EU-funded investments will expand and support medium-term growth, but high uncertainty, increasing interest rates and rising construction costs due to labour and material shortages will weigh on private investment. Inflation will remain elevated as high producer prices are passed on to consumers. Nonetheless, price pressures are expected to ease in 2023 as oil, gas, and food prices stabilise and ECB monetary policy tightening takes effect. The minimum wage (earned by 17% of Latvian employees) is set to increase by 24% in 2023 and 13% in 2024. Overall, nominal wages are expected to grow more moderately than inflation over 2022 and 2023, as automatic indexation is not widespread, but will exceed inflation in 2024. This and phasing out the energy price caps will keep inflation above target in 2024. Despite the slowdown in growth, the fiscal balance is projected to strengthen by about 2.4 percentage points of GDP in 2023. There is a risk that high inflation could become entrenched due to further energy market disruptions and increasing labour shortages. Upside risks include a swifter-than-expected use of EU recovery funds and fast integration of Ukrainian refugees into the labour market.

Investing in energy security and addressing labour shortages

Fiscal policy measures should target vulnerable households and maintain price incentives to shift towards low-carbon energy sources. Accelerating investment in renewables and completing the integration of regional power and gas markets are key to raise energy security. This will also require tackling rising labour shortages. Facilitating the recognition of qualifications would promote the labour market integration of refugees. Supplying more affordable housing and improving public transport services would help to improve labour mobility. Providing tertiary students with greater financial support and improving access to, and the quality of, training (including through establishing training funds) would boost productivity and ease labour shortages.

Lithuania

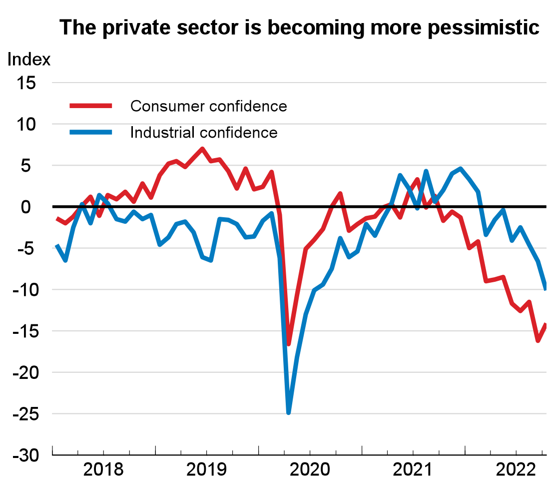
Growth is projected to slow to 2.5% in 2022 and 1.6% in 2023, before recovering to 2.0% in 2024. Lower growth in 2023 reflects higher inflation, negative confidence effects of Russia's war of aggression against Ukraine and weaker external demand. Private consumption is negatively affected by higher unemployment and a contraction of real wages. Investment is underpinned by EU funds and the government's multi-annual investment programme.

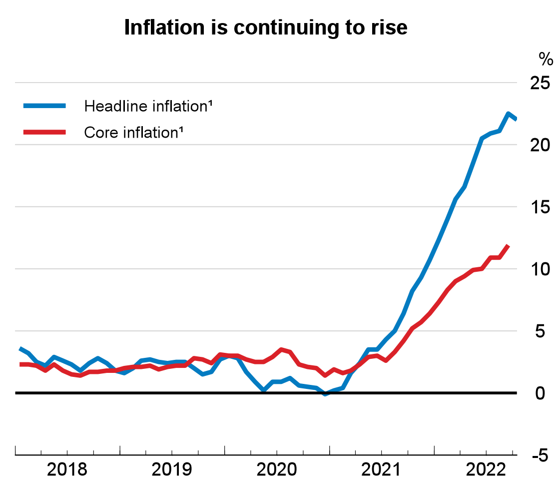
Fiscal policy support is helping households and firms to cope with rising energy prices. This support could be made more effective by moving from broad measures to more targeted support of vulnerable groups. In addition, this would enhance incentives for energy savings. Demand should also be restrained more to counter inflationary pressures. Structural reforms to bolster growth should focus on skills acquisition and better management of the many state and municipal-owned enterprises.

The economy is slowing in face of continued headwinds

During 2022, domestic economic activity has declined, as private consumption and investment began to contract under the impact of increasing inflation and deteriorating consumer and business confidence. Exports have also been curbed by the war in Ukraine and slowing export market growth, but imports contracted more than exports, leading to continued expansion of real GDP. Job creation has continued unabated, contributing to a two percentage point fall in the unemployment rate over the past year, leaving it at 5% after the summer. During the same period, skills shortages remained prevalent and even doubled in the construction sector. These labour market dynamics have led to a near-doubling of wage growth to 14%. Since January, the latter has contributed to a 4.6 percentage points rise in core inflation to nearly 12% in September. Together with higher energy and food prices, this nearly doubled headline inflation to 22.5%, before it came down by ½ percentage point in October.

Lithuania





1. Harmonised indices.
Source: OECD Main Economic Indicators database; and Eurostat, Harmonised Indices of Consumer Prices (HICPs).

StatLink https://stat.link/npgcyb

Lithuania: Demand, output and prices

Lithuania	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	48.9	0.0	6.0	2.5	1.6	2.0
Private consumption	29.4	-2.4	8.0	2.2	2.1	2.2
Government consumption	8.3	-1.4	0.9	0.7	0.3	0.0
Gross fixed capital formation	10.5	-0.2	7.8	3.9	4.5	3.9
Final domestic demand	48.1	-1.8	6.6	2.3	2.3	2.1
Stockbuilding[1]	- 1.8	-1.8	-0.3	-0.3	0.0	0.0
Total domestic demand	46.3	-3.8	7.3	2.3	2.2	2.0
Exports of goods and services	37.8	0.4	17.0	4.7	0.3	4.0
Imports of goods and services	35.2	-4.5	19.9	4.5	1.1	4.0
Net exports[1]	2.6	3.5	-0.3	0.4	-0.7	0.0
Memorandum items						
GDP deflator	_	1.8	6.5	15.8	8.3	3.9
Harmonised index of consumer prices	_	1.1	4.6	18.8	11.9	4.0
Harmonised index of core inflation[2]	_	2.6	3.4	10.1	8.1	3.9
Unemployment rate (% of labour force)	_	8.5	7.1	5.8	6.5	6.7
Household saving ratio, net (% of disposable income)	_	9.0	3.9	2.3	3.0	5.8
General government financial balance (% of GDP)	_	-7.0	-1.0	-2.0	-4.8	-4.6
General government gross debt (% of GDP)	_	55.5	50.8	50.2	53.4	56.9
General government debt, Maastricht definition[3] (% of GDP)	_	46.3	43.7	43.0	46.3	49.8
Current account balance (% of GDP)	_	7.6	1.2	-3.9	-4.1	-3.9

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/qzbd4a

Trade will continue to suffer from the war in Ukraine. Prior to the war, Russia accounted for 12% and 11% of imports and exports, respectively. Energy supplies have largely been secured as Lithuania stopped importing gas and oil from Russia in spring 2022, replacing them with imported liquefied natural gas and a diversification of oil import sources. However, the trade balance is negatively affected by higher international energy and food prices, which will also continue to fuel inflationary pressures. Ukrainian refugees now amount to more than 2% of the population, temporarily adding to fiscal spending pressures, but are also helping relax labour shortages.

Fiscal stimulus is being gradually withdrawn

In 2022, the fiscal stance became expansionary as a revised draft budget allocated an additional 2% of GDP to support Ukrainian refugees (accounting for 0.6% of GDP) and to help households and firms weather the energy crisis. The latter includes compensation for energy price increases above 40%, support for vulnerable households via an increase in non-taxable income, an extension of means-tested heating compensation and higher pensions. The package supplements earlier measures, such as energy price caps, subsidies for energy efficiency and a strengthening of energy independence. In 2023, the fiscal stance will become less expensionary only once temporary measures expire, including price energy caps. Tighter fiscal policy is needed to reduce overall demand pressures and thus lower risks of prolonged inflationary pressures. Moreover, support could become more targeted and effective by replacing current measures with ones that provide support to groups that are most vulnerable to energy price shocks. This would also enhance general energy saving incentives. A broadly neutral fiscal stance is assumed in 2024.

Growth will remain restrained

Growth is projected to slow under the impact of high inflation, the negative confidence effects of the war in Ukraine, and continued slow export market growth. High inflation and a weaker labour market will erode real incomes. Slower demand will dampen business sector investment, although total investment will benefit from EU funds and the implementation of the government’s multi-year investment programme. Headline inflation will come down slowly as the effects of higher energy and food prices peter out and under the impact of higher euro area monetary policy rates. In addition, unemployment will increase throughout the projection period, leading to slower wage growth and thus service inflation. Downside risks to the projections hinge mainly on the evolution of the war in Ukraine and its impact on the external environment and energy supply. On the upside, a faster-than-expected labour market integration of Ukrainian refugees could alleviate labour market shortages and wage pressures sooner than projected.

Securing stronger growth

Population ageing will weigh on growth and public finances, necessitating structural reform to secure a better use of available resources. A priority in this respect is better management of the many state- and municipality-owned enterprises, subjecting such enterprises to the same legal, financial, and regulatory framework as private firms. Similarly, better skills acquisition is needed through the timely implementation of the newly introduced curricula for schools, including attainment targets for digital skills, and a strengthening of firm-based learning in vocational training in all sectors. This should be complemented by measures to facilitate faster labour market integration of Ukrainian refugees.

Luxembourg

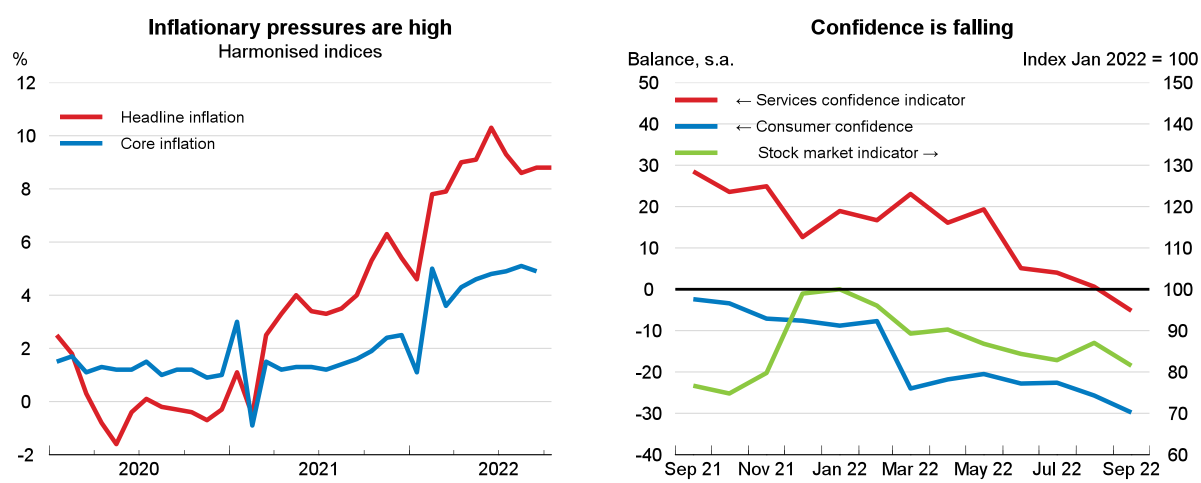
Luxembourg's economic growth is set to slow to 1.5% in 2023, before picking up again in 2024. Activity has slowed due to broadening inflationary pressures, falling manufacturing activity, and the uncertain outlook on the back of the Russian war of aggression against Ukraine. Financial services growth will slow in 2023 and high interest rates will delay business investment and housing purchases. Government support to households will underpin incomes and spending. Annual public investment of 4% of GDP will continue into 2024. The labour market will remain tight despite the growth slowdown. Rising prices of services will lift core inflation.

Income support to households should be targeted on the most vulnerable, be limited in time to avoid raising domestic demand pressures, and designed to preserve incentives to save energy. Reforms to the wage indexation system should be undertaken in consultation with the social partners to take account of the productivity, employment and investment effects. To enhance resilience, economic diversification requires stepping up investments in R&D and ICT, and in the transition to a low-carbon economy.

The economy is slowing

After a buoyant start to the year supported by the end of lock-down restrictions, the economy has slowed amidst rising uncertainty and inflation, exacerbated by the war in Ukraine. Retail trade volumes rose by 2.1% year on year in the first eight months of 2022, and employment remains robust. The unemployment rate stood at 4.8% in September 2022. Nonetheless, consumer confidence has fallen to its lowest point since 2002, as high inflation and interest rates weigh on sentiment. Business confidence has fallen from a high in early 2022 and manufacturing and residential construction activity have slowed. Consumer price inflation eased to 8.8% in October from a peak of 10.6% in June. Inflation was initially driven by energy prices, but price pressures are broadening, with core inflation rising to 5.2%. House price inflation has remained high. Salaries in the second quarter were 7.8% higher than a year earlier, after automatic indexation increased all wages and social benefits by 2.5% on 1 April.

Luxembourg



Source: Eurostat, Consumer Prices database; Statec, Business opinion survey in services; European Commission, Consumer confidence indicator; and Refinitiv.

StatLink https://stat.link/eiaym4

Luxembourg: Demand, output and prices

Luxembourg	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	62.3	-0.8	5.1	1.7	1.5	2.1
Private consumption	21.0	-7.2	9.4	2.8	2.0	3.6
Government consumption	10.7	7.3	5.5	2.9	3.4	3.1
Gross fixed capital formation	10.8	-3.2	6.1	-2.8	-2.5	4.1
Final domestic demand	42.5	-2.5	7.5	1.4	1.3	3.6
Stockbuilding[1]	0.6	-0.3	0.5	-0.2	0.0	0.0
Total domestic demand	43.1	-2.9	8.4	1.0	1.3	3.6
Exports of goods and services	127.4	0.2	9.7	0.8	1.1	1.6
Imports of goods and services	108.2	-0.5	11.9	0.3	0.9	2.1
Net exports[1]	19.2	1.1	-0.2	1.2	0.8	-0.2
Memorandum items						
GDP deflator	_	4.6	6.1	6.0	1.1	1.6
Harmonised index of consumer prices	_	0.0	3.5	8.2	4.0	3.2
Harmonised index of core inflation[2]	_	1.2	1.5	4.5	4.1	2.9
Unemployment rate (% of labour force)	_	6.4	5.7	4.8	5.0	5.2
Household saving ratio, net (% of disposable income)	_	19.0	12.4	12.9	14.9	13.0
General government financial balance (% of GDP)	_	-3.4	0.8	-0.2	-2.2	-0.7
General government gross debt (% of GDP)	_	32.1	31.0	33.5	36.9	39.2
General government debt, Maastricht definition[3] (% of GDP)	_	24.5	24.6	27.0	30.5	32.7
Current account balance (% of GDP)	_	4.6	4.7	6.4	5.6	5.2

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/fbacmt

Total trade exposure to Russia is minimal. Luxembourg imports almost all of its energy, with oil accounting for 60% of all energy consumption and natural gas for about 15%. Natural gas meets about 46% of heating needs. Most natural gas comes through LNG facilities in Belgium, primarily sourced from Norway and the United Kingdom, and gas shortages are not expected in the near term. Luxembourg has access to a gas storage facility in Germany and more storage through a multilateral agreement with neighbouring countries. The impact of the war is tangible through high gas prices, which are affecting energy-intensive firms, such as steel, glass and cement, and consumers. Luxembourg has taken in some 4 500 Ukrainian refugees, mostly women and minors, with temporary hosting facilities at full occupancy.

Fiscal policy will remain supportive

In response to the energy price shock, the government is implementing a total support package of around EUR 2.5 billion over 2022-23 (3.3% of GDP), including EUR 500 million in business loan guarantees. Measures include capping household gas prices at September 2022 levels and electricity prices at 2022 prices from January 2023; reducing most VAT rates by 1 percentage point; subsidising domestic heating fuel as well as energy-intensive firms; and giving cash allowances to disadvantaged households. The energy price cap and reduced VAT rates aim to limit the pace of future wage indexation tranches as agreed with social partners, and the potential associated loss of competitiveness. Public investment of over 4% of GDP annually between 2022 and 2024 will continue to support infrastructure, the green transition and innovation. The magnitude of public support means that there will be small fiscal budget deficits in 2022-24. Although the government will embark on fiscal consolidation in 2024, energy prices are likely to remain high into 2024, which is assumed to result in the government continuing the support measures.

Economic growth will slow significantly before gradually recovering

GDP will slow to 1.7% in 2022 and 1.5% in 2023, before picking up to 2.1% in 2024. High inflation is eroding confidence as well as disposable incomes, but government measures will support consumption in 2022-23. Public sector investment will support growth. Private investment will be held back by labour shortages and rising interest rates and only recover slowly. Export growth will moderate in 2023, as global financial market conditions remain difficult, and some supply-chain restrictions remain. The measures to contain inflation will have some impact, but a tight labour market will maintain wage pressures and keep core inflation high in 2023. Risks to the outlook are mainly on the downside. Higher-than-anticipated inflation could trigger further wage increases, sustaining upward pressures on prices and undermining competitiveness. The overheating of the housing market poses risks for some borrowers on variable rates as interest rates rise, particularly those with lower incomes. A sharp weakening of financial markets could negatively affect activity and exports.

To embed resilience, policy should focus on productivity and investment

Policies to mitigate inflation impacts on households should be better targeted, time-bound, and maintain incentives for energy savings. The wage indexation system risks exacerbating high inflation when large shocks occur, potentially harming longer-term competitiveness. In the longer run the system should be reformed in consultation with social partners to account better for productivity, employment and investment effects. Efforts to reform pensions and implement spending reviews would help maintain fiscal space over the longer term. Encouraging greater investment by the business sector in R&D and innovation would boost productive capacity and lift productivity growth, thereby also helping to reduce inflationary pressures. The bankruptcy bill currently before parliament should help restructure failing firms, and allow exit for non-viable ones.

Mexico

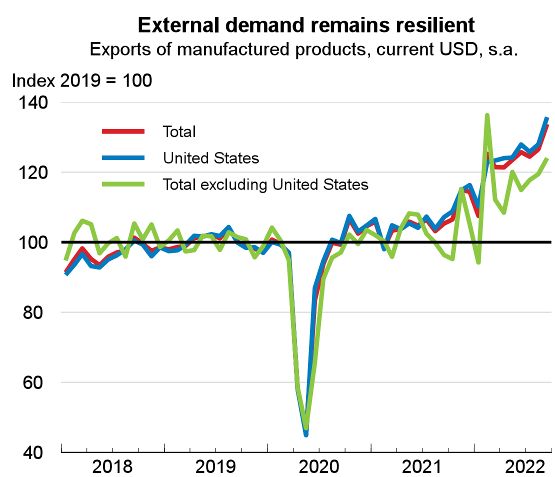
Real GDP growth is projected to slow from 2.5% this year to 1.6% in 2023, but to edge up to 2.1% in 2024. Consumption will be supported by the gradual improvement in the labour market but dampened by high inflation. Exports will continue to benefit from high integration in global value chains, but their dynamism will be mitigated by the slowdown in the United States. Inflation will edge down to 5.7% in 2023 and 3.3% in 2024.

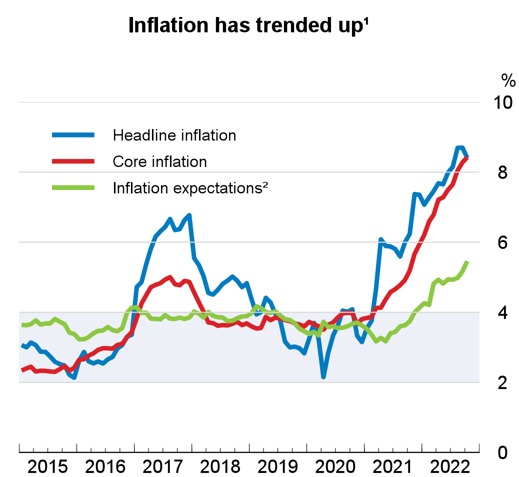
Measures to respond to increases in energy prices should target the most affected households and SMEs and provide incentives for energy savings. Monetary policy should remain tight to anchor inflation expectations. Independent and adequately funded competition authorities and regulators would contribute to boosting competition and productivity. Improving access to and the quality of childcare would support female labour force participation and reduce educational inequalities.

The outlook for activity is worsening and inflationary pressures remain high

After robust growth during the first three quarters of 2022, high-frequency indicators show activity declining in some sectors. Mining and construction output recently contracted although auto production remains resilient, on the back of easing supply constraints. External demand has held up, but is expected to soften as growth in the United States weakens. Inflationary pressures remain high and broad-based. Annual headline and core inflation stood at 8.4% in October. Medium-term inflation expectations have risen.

Mexico





1. The shaded area represents the central bank's inflation target range.
2. Private sector inflation expectations for the next 12 months.
Source: Bank of Mexico.

StatLink https://stat.link/8jg2yz

Mexico: Demand, output and prices

Mexico	2019	2020	2021	2022	2023	2024
	Current prices MXN billion	Percentage changes, volume (2013 prices)				
GDP at market prices	24 445.7	-8.1	4.8	2.5	1.6	2.1
Private consumption	15 866.4	-10.3	7.5	6.9	2.7	3.5
Government consumption	2 785.2	-0.2	1.0	1.3	1.6	0.9
Gross fixed capital formation	5 037.8	-17.7	9.5	6.5	3.1	2.8
Final domestic demand	23 689.4	-10.6	7.1	6.1	2.7	3.0
Stockbuilding[1]	818.6	-0.4	0.2	-0.1	0.0	0.0
Total domestic demand	24 508.0	-11.1	7.5	6.0	2.7	3.0
Exports of goods and services	9 490.1	-7.3	6.9	7.6	3.8	5.0
Imports of goods and services	9 552.4	-13.8	13.6	10.1	6.9	6.7
Net exports[1]	- 62.3	2.4	-2.2	-0.9	-1.3	-0.8
Memorandum items						
GDP deflator	_	4.2	7.1	8.7	5.7	3.6
Consumer price index	_	3.4	5.7	8.0	5.7	3.3
Core inflation index[2]	_	3.8	4.7	7.5	5.5	3.3
Unemployment rate[3] (% of labour force)	_	4.4	4.1	3.3	3.4	3.3
Current account balance (% of GDP)	_	2.4	-0.4	-1.5	-1.6	-1.2

1. Contributions to changes in real GDP, actual amount in the first column.

2. Consumer price index excluding volatile items: agricultural, energy and tariffs approved by various levels of government.

3. Based on National Employment Survey.

Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/l90mqu

Fiscal policy remains prudent and monetary policy will need to remain restrictive

A retail fuel price stabilisation mechanism was put in place to reduce cost pressures and support household purchasing power. Estimates suggest that this is lowering inflation by between 2 and 4 percentage points. The associated budgetary cost is estimated at 1.4% of GDP in 2022. It is assumed that this mechanism remains in place during the projection period. Higher oil revenues cover the cost of the stabilisation mechanism but greater pass-through of global fuel price changes to domestic retail prices would lower the future budgetary cost of the mechanism and provide better incentives for energy savings. This would create some fiscal space to strengthen social programmes and provide more targeted support to vulnerable households. The government has also taken steps to mitigate price pressures for basic goods, including the temporary elimination of import tariffs for basic goods, cooperation with the private sector to freeze the prices of 24 key products (mainly food) for six months and measures to increase production of basic grains.

Fiscal policy remains prudent and continues to prioritise some social programmes, particularly non-contributory pensions, and priority infrastructure projects in the South. The budget deficit is expected to increase to 3.6% of GDP in 2023, from 3% of GDP in 2022, with the official measure of public debt expected to stabilise around 50% of GDP. Mexico has also started to rebuild fiscal buffers, by gradually replenishing the stabilisation fund, which now has 0.1% of GDP in resources available. This is a welcome step to increase the ability to react in the event of a negative shock.

To respond to mounting inflationary pressures and anchor inflation expectations, the central bank has gradually increased the policy rate, to 10%. With widespread price pressures expected to persist, further interest rate increases are warranted. The policy rate is assumed to increase to 10.75% by the first quarter of 2023 and to remain at that level until the beginning of 2024, when it would start to be gradually reduced.

Growth will be moderate in the near term

The economy is projected to expand by 1.6% in 2023 and 2.1% in 2024, slightly above potential. Domestic consumption will be a key driver of growth and services related to tourism will continue to recover gradually. Exports will continue to benefit from deep integration in manufacturing value chains, particularly in electronics and automotive sectors, but will suffer from slower growth in the main trading partners. Inflation will moderate in 2023 and 2024, as the impact of higher interest rates takes effect and ample spare capacity limits wage pressures. However, the inflation outlook remains very uncertain. Inflation may be higher for longer, eroding purchasing power, particularly of vulnerable households, calling for greater tightening of monetary policy. Episodes of financial volatility may trigger greater risk aversion, reduce net financial inflows and increase financing costs. On the upside, swifter near shoring of production processes to Mexico, to facilitate access to the United States market, could imply stronger exports.

Boosting productivity is a key priority

Broadening tax bases would help to respond to increasing spending needs in education, health and infrastructure, to safeguard the commitment to debt sustainability, and to boost productivity and growth. Reducing the regulatory cost of formalising a business, particularly at subnational level, and continuing to improve labour dispute resolution mechanisms would support stronger formal employment. Allocating more resources towards primary education would mitigate the pandemic’s adverse effects on educational outcomes. Promoting public urban and interurban transport as well as renewables energy would reduce emissions and the use of fossil fuels.

Netherlands

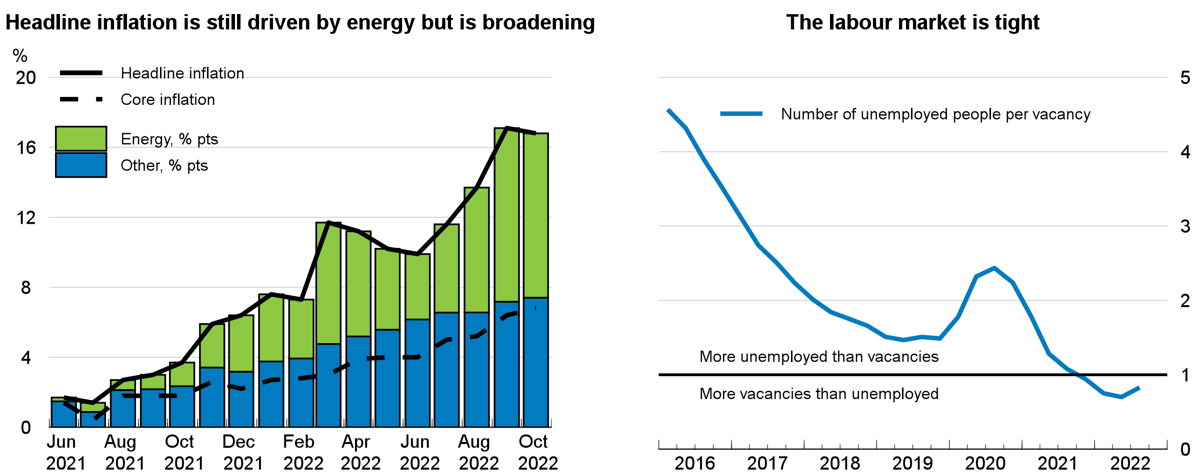
Following a 4.3% expansion in 2022, economic growth is projected to slow to 0.8% in 2023 and 1.1% in 2024. Inflation is expected to moderate to 3.9% by the end of 2024, after peaking at 15.4% in the fourth quarter of 2022. Private consumption is projected to weaken in the short term, but will gradually strengthen, aided by government support measures and welfare adjustments. Despite a small increase over the projection period, unemployment will remain low at 4.3% in 2024 as the labour market remains tight.

The fiscal stance set out in the 2023 budget is expansionary. The energy price cap to cushion the impact of high energy prices on households is needed but should be targeted more towards lower income households and better incentivise energy savings. The government should continue to tackle structural challenges, prioritising an acceleration of the green transition to ensure energy security and reduce fossil fuel dependence.

The outlook has darkened

GDP declined in the third quarter of 2022 by 0.2%, and high frequency indicators indicate a further deterioration in the outlook. Inflation reached 16.8% in October mostly due to rising energy prices. Unemployment is low, at 3.8% in September. The number of vacancies remains high, with less than one unemployed person per vacancy, indicating a tight labour market. Collective labour agreement wage rates are starting to accelerate and were up 3.5% in October over a year earlier. Business confidence dropped for the third successive month in October, and consumer confidence has fallen to an all-time low amid rapidly rising living costs.

Netherlands



Source: Eurostat; and CBS.

StatLink https://stat.link/3ca6gh

Netherlands: Demand, output and prices

Netherlands	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	813.0	-3.9	4.9	4.3	0.8	1.1
Private consumption	353.6	-6.4	3.6	5.8	0.4	1.0
Government consumption	200.1	1.6	5.2	0.7	3.8	2.5
Gross fixed capital formation	172.9	-2.6	3.2	2.6	0.0	1.0
Final domestic demand	726.6	-3.3	4.0	3.6	1.3	1.5
Stockbuilding[1]	6.8	-0.8	-0.1	0.0	0.1	0.0
Total domestic demand	733.4	-4.2	3.9	3.6	1.4	1.4
Exports of goods and services	670.7	-4.3	5.3	4.5	1.8	2.0
Imports of goods and services	591.2	-4.8	4.0	3.7	2.5	2.4
Net exports[1]	79.6	-0.1	1.4	1.1	-0.4	-0.2
Memorandum items						
GDP deflator	_	1.9	2.5	5.8	7.8	4.1
Harmonised index of consumer prices	_	1.1	2.8	12.2	8.5	4.2
Harmonised index of core inflation[2]	_	1.9	1.8	4.9	8.7	4.4
Unemployment rate (% of labour force)	_	4.9	4.2	3.6	4.1	4.3
Household saving ratio, net[3] (% of disposable income)	_	18.8	17.6	11.6	10.7	9.9
General government financial balance (% of GDP)	_	-3.7	-2.6	-1.1	-3.4	-2.4
General government gross debt (% of GDP)	_	70.4	66.5	64.3	65.2	66.0
General government debt, Maastricht definition[4] (% of GDP)	_	54.7	52.5	50.3	51.2	51.9
Current account balance (% of GDP)	_	5.1	7.2	6.4	6.4	6.5

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. Including savings in life insurance and pension schemes.
4. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/nfe93b

The Dutch direct dependence on Russian gas is limited, only 3-4% of energy consumption was imported from Russia in recent years. Gas storage levels over 90% and a 25% reduction of gas consumption in the first half of 2022 significantly mitigate the risk of gas shortages. Nevertheless, the Netherlands is a net-importer of gas and therefore vulnerable to spill-over effects from rising global energy prices. The government will introduce an energy price cap in 2023 to protect households and other small energy consumers as well as a separate measure that provides an allowance to energy-intensive SMEs. The cap covers the difference to market prices and could have a significant budgetary impact if energy prices are persistently high, as assumed in the projections, or if demand is high, due to weather conditions. Russia's war of aggression against Ukraine has led to an inflow of 82 000 refugees to the Netherlands by the beginning- of November. Around 40% of the earlier arrivals were employed by end-August.

Support measures and higher public spending will increase the fiscal deficit

After a deficit of 1.1% of GDP in 2022, due to lower COVID-19 related expenses and high economic growth, the fiscal deficit is projected to increase to 3.4% of GDP in 2023 due to increased spending on energy support measures and raised welfare benefits. The budget announced in September includes a purchasing power package to protect households from cost-of-living increases. The package amounts to about EUR 11 billion in 2023 (1.1% of GDP), with around EUR 6 billion in temporary measures, such as an energy discount for lower-income households and a continuation of the 21% reduction in excise duty fuel.

Almost EUR 5 billion are allocated to structural measures, such as a decrease in the tax on labour, increased child and rental allowances and a 10% increase in pension and welfare benefits that is to follow the 10% increase in the minimum wage in January 2023. The total cost of the energy price cap and the allowance for SMEs, will depend on energy price developments, but is estimated at approximately EUR 25 billion (2.4% of GDP). As temporary energy support measures are scheduled to be phased out by end 2023, the fiscal deficit will decrease to 2.4% of GDP in 2024.

Economic growth will slow

GDP growth is projected to be 4.3% in 2022 before slowing to 0.8% in 2023 and picking up to 1.1% in 2024. Headline inflation is projected to reach 15.4% in the fourth quarter of 2022 before moderating over 2023 to an annual average of 8.5%, aided by the energy price cap, and to 4.2% on average in 2024 as tighter monetary policy takes effect, although the removal of the price cap could add to upward pressure on inflation. Wages are projected to increase by around 5% in both 2023 and 2024 and to stop declining in real terms at the end of 2023. Private consumption is projected to be subdued as disposable income will be eroded by high inflation. However, the recent government support measures will cushion the impact of high energy prices. After strong export growth in 2022, the deterioration in growth in main EU trading partners (notably Germany) will weigh on exports in 2023, before some improvement in 2024. The outlook is surrounded by significant downside risks as a further escalation of the war could increase energy prices even more and worsen the economic outlook in main trading partners and, if combined with a cold winter and reduced availability of LNG gas, the government could be obliged to strongly incentivise the reduction of gas consumption. Bankruptcies, which are still below the pre-pandemic level, could rise significantly due to the increasing pressure on business from higher interest rates, labour cost and uncertainty. An upside risk to the projection is that higher income households could spend a greater share of their excess savings.

Carefully monitoring support measures and ensuring energy security is key

Well-targeted fiscal policy support to aid vulnerable households with high living costs is needed as long as high energy prices persist and significantly erode households' disposable income. The government should carefully monitor the energy price cap, and revise it as needed, to ensure that it is targeted at households in need and that incentives to save energy are in place. An acceleration of the green transition, to ensure energy security and reduce fossil fuel dependence should be a priority. Implementing re-skilling and up-skilling programs to address the tight labor market, particularly for jobs supporting the green transition, could help towards this goal. Boosting productivity, by stepping up the adoption of digital technologies, improving digital skills, and reducing regulations, would support debt sustainability as the population ages.

New Zealand

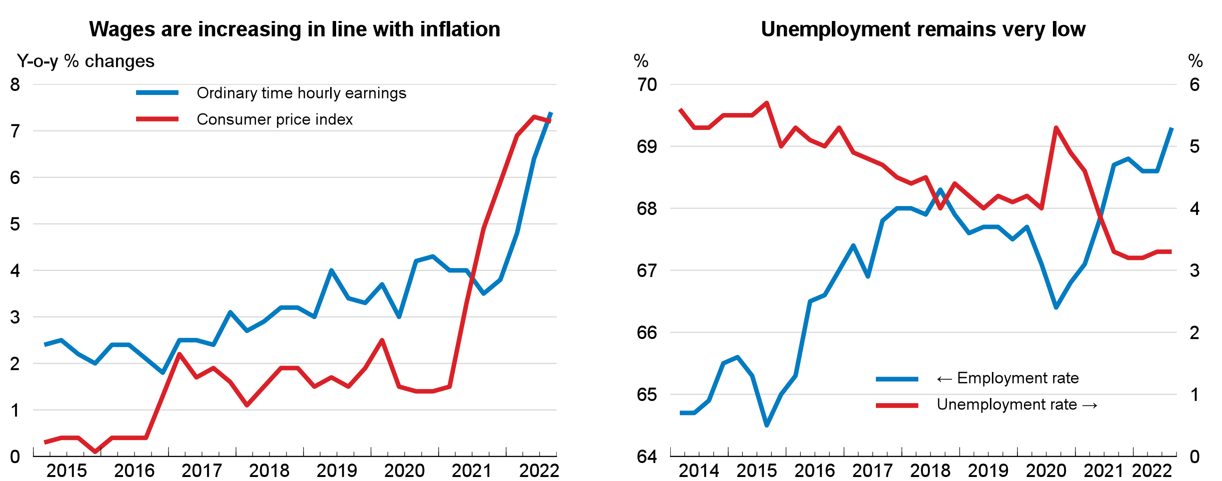
Real GDP growth is projected to slow to 1.0% in 2023 and 1.2% in 2024. Private consumption will weaken with lower employment growth and rising mortgage-servicing costs. Tighter credit conditions and weakening demand will weigh on business investment. Unemployment will increase and headline inflation will fall throughout the projection period. There is a risk that house prices fall more than assumed, accentuating the downturn.

Monetary policy should continue to be tightened to bring inflation to the mid-point of the 1-3% target band. Fiscal consolidation should proceed to reduce inflationary pressures and ensure that New Zealand is on track to meet its 2025 operating surplus target. In the longer term, fiscal policy should aim to reduce the debt-to-GDP ratio to rebuild buffers to respond to adverse economic shocks and to cope with the fiscal costs of population ageing. Education reforms, including to teaching methods, are needed to improve learning outcomes.

Growth remains strong and the labour market is stretched

Following the gradual easing of COVID-19-related restrictions, growth has picked up. Border re-opening has contributed to a surge in tourist arrivals, albeit to levels that remain much lower than before the pandemic. Private consumption has slowed after the rebound following the easing of pandemic restrictions but remains robust. Business and consumer sentiment have improved after plummeting earlier this year, but remain very depressed. The labour force participation rate has increased to a record high, and the unemployment rate remains close to historical lows. To address labour shortages, the government has increased caps on seasonal and working holiday visas. Wages have increased sharply in line with consumer price inflation, which reached a 30-year high in the second quarter, at 7.3%. After surging during the pandemic, house prices are now down by 13% since the peak in November last year. Although the direct impact of Russia's war of aggression against Ukraine has been limited, rising energy and commodity prices have fed through to non-tradable inflation.

New Zealand



Source: Statistics New Zealand.

StatLink https://stat.link/jx2h7c

New Zealand: Demand, output and prices

New Zealand	2019	2020	2021	2022	2023	2024
	Current prices NZD billion	Percentage changes, volume (2009/2010 prices)				
GDP at market prices	320.2	-1.1	4.8	2.1	1.0	1.2
Private consumption	183.2	-1.2	6.2	2.4	-0.7	1.0
Government consumption	59.8	6.9	9.9	7.0	-2.0	-2.0
Gross fixed capital formation	75.9	-7.0	9.0	2.7	-0.5	1.4
Final domestic demand	318.9	-1.1	7.6	3.4	-0.9	0.4
Stockbuilding[1]	1.2	-0.9	1.5	-0.4	0.1	0.0
Total domestic demand	320.1	-1.9	9.1	2.9	-0.9	0.4
Exports of goods and services	87.7	-12.7	-3.6	1.3	8.5	3.8
Imports of goods and services	87.6	-16.0	14.9	3.3	0.1	0.8
Net exports[1]	0.1	0.9	-4.3	-0.6	2.0	0.8
Memorandum items						
GDP deflator	_	2.2	2.9	5.7	4.4	3.1
Consumer price index	_	1.7	3.9	7.3	5.2	3.2
Core inflation index[2]	_	2.2	3.7	6.0	5.3	3.2
Unemployment rate (% of labour force)	_	4.6	3.8	3.3	4.0	4.6
Household saving ratio, net (% of disposable income)	_	5.8	4.7	0.6	0.2	0.2
General government financial balance (% of GDP)	_	-7.4	-3.9	-4.9	-3.4	-1.8
General government gross debt (% of GDP)	_	42.5	45.7	52.0	54.5	55.5
Current account balance (% of GDP)	_	-1.1	-5.9	-7.9	-6.4	-5.5

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/zx1cle

Macroeconomic policies are tightening

The Reserve Bank of New Zealand (RBNZ) embarked on monetary policy normalisation earlier than most other central banks and has raised the Official Cash Rate (OCR) by a cumulative 3.25 percentage points, to 3.5%, over the past year. The OCR is assumed to rise further to a peak of 4.75% before starting to decline from the second half of 2024. The RBNZ's "Funding for lending" programme, which allowed eligible banks to borrow directly from the RBNZ at the OCR, will end in December, putting further upward pressure on interest rates. Over the coming five years, the RBNZ will also sell back government bonds acquired during the pandemic. Yields on 10-year government bonds are projected to average 5½ per cent in 2023-24.

In May 2022, the government adopted a new fiscal strategy stipulating that New Zealand should reach a small budget surplus by 2025. The fiscal stance will tighten over the projection period, as temporary COVID-19-related support is withdrawn, and tax revenues increase in line with GDP. The government introduced a one-off NZD 350 cost-of-living payment to support some 2.1 million low- and-middle-income earners grappling with mounting costs. The temporary cuts in petrol excise duty, road user charges and public transport fares introduced in March have been extended, but are assumed to end in February 2023.

Growth will decline due to policy tightening and global uncertainty

Real GDP growth is set to slow in 2023, owing to weakening private demand. Rising debt servicing costs and falling real incomes and house prices will constrain household consumption. Private investment will moderate, reflecting easing capacity constraints, slower domestic and global demand growth, and increases in the cost of capital. Unemployment will increase gradually throughout the projection period, due to moderating economic activity but remain low by historical standards. Inflationary pressures will abate as aggregate demand slows, global energy prices stabilise and global supply chain disruptions ease. Risks to the projection are tilted to the downside. If monetary conditions need to be tightened more than assumed to bring down inflation, this will reduce growth, including by increasing mortgage servicing costs, which would accentuate declines in housing prices and consumption. On the upside, China relaxing its zero-COVID-19 policy earlier than expected would boost tourism to New Zealand.

Reforms are needed to improve productivity and public finances in the long run

Monetary policy tightening should continue to seek to anchor inflation expectations and prevent inflation from becoming entrenched. Fiscal consolidation is appropriate to reduce demand pressures and to make sure that New Zealand is on track to meet its budget surplus target. Measures to cushion the impact of higher energy prices on households, if prolonged, should be more targeted on the most vulnerable. In view of population ageing and the accompanying rise in healthcare expenditures, structural measures, such as linking pension eligibility to life expectancy, will be needed to safeguard public finances in the long run. Strengthening mathematics and science teaching in primary schools and promoting digital apprenticeships and internships would make New Zealand better positioned to take advantage of the digital transition and enhance long-term productivity growth. To meet its greenhouse gas emissions reduction targets, increases in the price of carbon emissions will need to be complemented by other measures, such as supporting the roll-out of a charging network for electric vehicles.

Norway

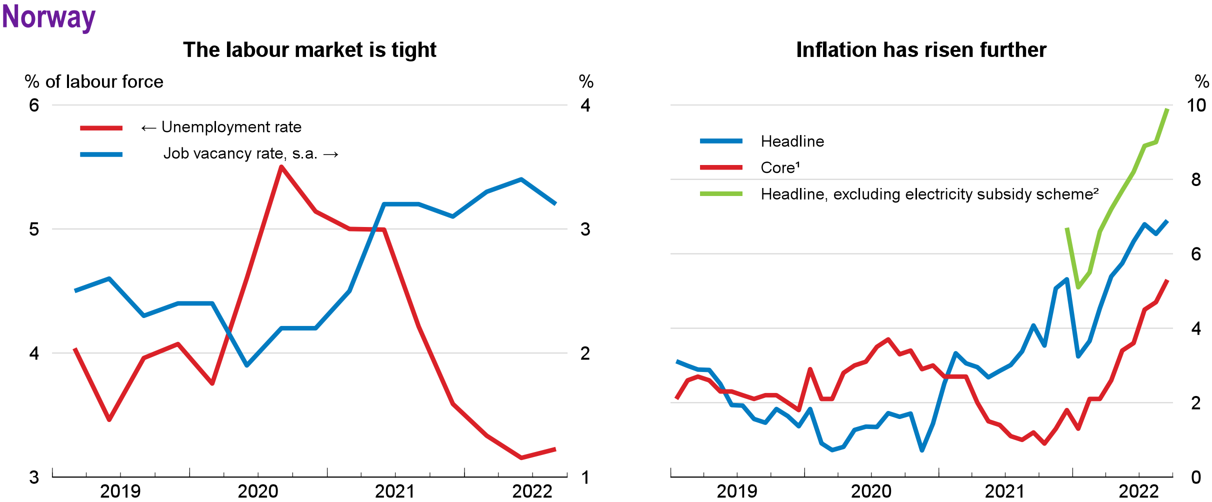
Mainland GDP growth is projected to slow to 0.7% in 2023 but rebound to 1.3% in 2024. Broad-based increases in prices will weigh on private consumption and investment. Even though headline inflation will ease as energy prices stabilise, helping domestic demand to recover, underlying price pressures will persist. The unemployment rate will increase on the back of a softening economy, but the labour market will remain tight, putting pressure on wages.

Monetary policy tightening should continue, given that inflation is well above target and inflation expectations have risen. Fiscal policy should provide well-targeted and temporary support to cushion the impact of high energy costs on vulnerable groups, while not distorting incentives to enhance energy efficiency. Progress in the green transition needs to continue. Structural policies should focus on improving the business environment and promoting higher labour force participation.

High inflation affects growth momentum

Mainland GDP growth bounced back following the lifting of pandemic-related restrictions earlier in the year. However, rapidly rising prices have reduced household purchasing power, consumer confidence and private consumption, despite support from electricity price subsidies and the use of accumulated savings. High prices, supply constraints and weaker global growth are weighing on business investment. Interest rate increases have put additional pressure on domestic demand. Headline consumer price inflation reached 7.5% in October, owing largely to higher food and energy prices, with the rise in the latter partly contained by the government electricity subsidy scheme. Underlying price pressures have also intensified, reflecting a broadening of inflation to non-energy items. Tight labour market conditions are likely to push wage growth in 2022 above the 3.7% increase agreed in this year's wage negotiations.

Norway



1. Core inflation is Statistics Norway's CPI-ATE measure which adjusts for tax changes and excludes energy products.
2. Hypothetical CPI calculated by Statistics Norway showing the overall price growth if the government had not introduced the electricity subsidy scheme for households.
Source: OECD Economic Outlook 112 database; and Statistics Norway.

StatLink https://stat.link/5hd01e

Norway: Demand, output and prices

Norway	2019	2020	2021	2022	2023	2024
	Current prices NOK billion	Percentage changes, volume (2019 prices)				
Mainland GDP at market prices[1]	3 063.0	-2.3	4.1	2.9	0.7	1.3
Total GDP at market prices	3 563.5	-0.7	3.9	2.5	1.8	1.6
Private consumption	1 579.1	-6.6	4.9	6.4	0.7	1.3
Government consumption	867.7	1.8	3.8	0.1	1.3	1.2
Gross fixed capital formation	957.8	-5.6	-0.9	1.4	0.2	3.1
Final domestic demand	3 404.5	-4.2	2.9	3.3	0.7	1.7
Stockbuilding[2]	106.1	-0.4	0.2	2.3	0.1	0.0
Total domestic demand	3 510.7	-4.5	3.0	5.9	0.8	1.6
Exports of goods and services	1 292.2	-1.2	4.7	1.2	5.8	3.9
Imports of goods and services	1 239.4	-11.9	2.3	11.4	5.5	5.4
Net exports[2]	52.8	3.7	0.8	-2.9	1.2	0.3
Memorandum items						
GDP deflator	_	-3.6	16.9	20.7	3.1	3.0
Consumer price index	_	1.3	3.5	5.7	4.5	3.2
Core inflation index[3]	_	2.7	1.7	3.6	4.4	3.3
Unemployment rate (% of labour force)	_	4.7	4.4	3.3	3.6	3.7
Household saving ratio, net (% of disposable income)	_	14.2	12.5	8.3	7.6	7.3
General government financial balance (% of GDP)	_	-2.6	9.9	16.2	16.3	16.4
General government gross debt (% of GDP)	_	54.1	49.9	..	..	..
Current account balance (% of GDP)	_	0.7	14.9	23.5	23.6	23.3

1. GDP excluding oil and shipping.
2. Contributions to changes in real GDP, actual amount in the first column.
3. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/49a5ic

High global energy prices have fuelled inflation. The government has introduced a scheme to reduce households' electricity bills in response to rising energy costs. However, high energy prices have also improved Norway's terms of trade considerably, with record-high government petroleum-related revenues. Gas sales are estimated to have increased by around 8% in real terms in 2022 over the previous year. Norway plans on taking in around 40 000 Ukrainian refugees (equivalent to around 0.5% of Norway's population) in 2022 and another 30 000 in 2023. The 2023 draft Budget allocates approximately 0.3% of mainland GDP to the provision of assistance for them.

Fiscal and monetary policies are tightening

The draft 2023 Budget envisages a tightening of fiscal policy, mainly due to the phasing-out of COVID-19 support, resulting in lower petroleum revenue spending of 0.6 percentage points of mainland trend GDP. This is appropriate to contain inflationary pressures and ensure adherence to the fiscal rule which stipulates that over time the structural non-oil deficit should equal to 3% of the value of the oil fund (the Government Pension Fund Global). The Budget extends the household electricity support scheme until end-2023, at a cost of around 1.2% of mainland GDP. The subsidy scheme should be better targeted on lower-income households, while ensuring that it encourages greater energy savings. Monetary policy continues to tighten. The Norges Bank increased the policy rate further in November by 0.25 percentage points to 2.5%. This is appropriate, given that inflation is well above the 2% target and inflation expectations have risen. The OECD projections assume that the policy rate will peak at 3.25% in the first quarter of 2023 and remain at this level until end-2024.

Growth will recover in 2024 but remain moderate

Mainland GDP growth will slow to 0.7% in 2023, as high inflation and policy tightening weigh on domestic demand, but will recover to 1.3% in 2024. The stabilisation of energy prices and easing demand will help reduce consumer price inflation, although the decline may be more limited if the electricity subsidy scheme is withdrawn in 2024. Following a slowdown, business investment is expected to pick up gradually over the projection period, with the implementation of projects related to the reduction of emissions and the strengthening of power supply, and helped by the pick-up in external demand. While declining, core inflation will remain well above the 2% target at the end of the projection period. The unemployment rate will rise as a consequence of the slowdown, but labour market conditions will remain tight in view of labour shortages. Higher-than-projected price and wage increases, or lower-than-expected trading partner growth could lower growth prospects further. On the upside, energy security risks are comparatively low, given that Norway is an exporter of oil and gas, and to some extent also electricity. Fast integration of Ukrainian refugees into the labour market could help alleviate skills shortages and wage pressures.

Ensuring sustainable and inclusive growth is key

Advancing the green transition is essential for sustainable and inclusive growth. The focus of the draft 2023 Budget on emissions reduction, including through an increase in the tax on non-Emission Trading System emissions by 21%, and promotion of green-technology initiatives, notably the carbon-capture and storage (Longship) programme, go in the right direction. The electricity subsidy scheme to households should remain temporary, so that planned longer-term solutions, including facilitating more fixed-price contracts in energy supply chains to reduce price volatility, are not delayed. Improving conditions for innovation and technology adoption is essential to boost productivity. More effective insolvency procedures would help the reallocation of workers to sectors with greater potential. Further efforts should be made to strengthen labour force participation, including through disability benefit reforms to reduce incentives for early retirement.

Peru

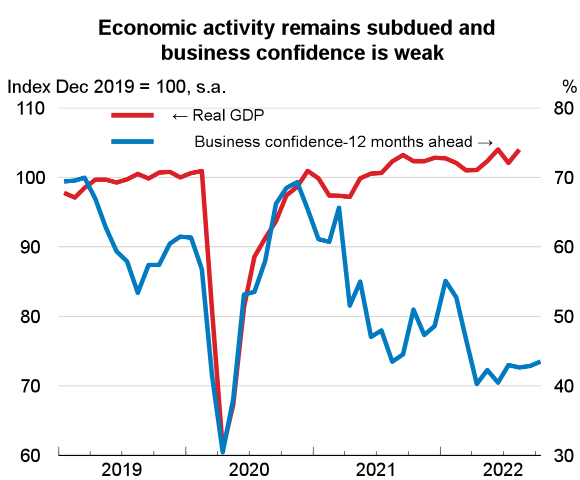
GDP is projected to grow by 2.6% in 2023 and 2.9% in 2024, driven mainly by higher mining production and exports and the recovery of tourism. Still elevated inflation and tighter financial conditions will weigh on household consumption. High political uncertainty, low business confidence and structurally slow budget execution at regional and local levels will constrain investment. Inflation, which has started to decline, will converge to the 2% target in the course of 2024. Informality, above pre-pandemic levels, will widen inequalities.

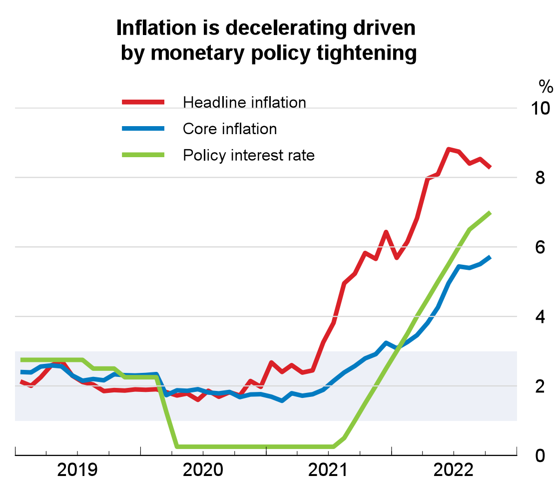
The central bank should maintain a restrictive stance to ensure inflation expectations get re-anchored. Safeguarding fiscal sustainability will hinge on maintaining the envisaged fiscal consolidation path. With formal job creation lagging, and high poverty and food and energy prices, targeted fiscal support to the most vulnerable is needed. A tax reform to increase structurally low public revenues would help to address pressing infrastructure and social needs, enhance tax progressivity and make growth more inclusive. Expanding electricity generation from renewable resources would help reduce fossil fuel dependence and costs.

Social unrest in mining and high inflation are weighing on growth

After surpassing pre-pandemic levels in 2021, economic activity has lost momentum. Economic activity grew by 3.5% in the first half of 2022, driven by a fast job recovery, pension fund withdrawals and rapid credit growth, leading to buoyant household consumption. Between July and September, economic activity was up only by 1.7% year-on-year. The recovery in sectors most positively affected by the easing of COVID-19 restrictions started to dissipate and was offset by weakness in mining and agriculture. Much of the drag in mining production stems from protest-related disruption in copper mines. Political uncertainty has undermined business confidence and manufacturing output has contracted in the last three months. Softer exports together with higher oil prices and the resulting larger import bill are widening the current account deficit. Employment has recovered and is above pre-pandemic levels, but informality has increased, reaching 70% of the workforce.

Peru





Source: BCRP; and INEI.

StatLink https://stat.link/2vcpyf

Peru: Demand, output and prices

Peru	2019	2020	2021	2022	2023	2024
	Current prices PEN billion	Percentage changes, volume (2007 prices)				
GDP at market prices	761.6	-10.9	13.2	2.7	2.6	2.9
Private consumption	493.6	-9.6	11.4	4.4	3.1	2.8
Government consumption	100.7	8.4	6.4	-0.9	0.4	1.1
Gross fixed capital formation	159.8	-16.7	35.3	2.1	1.3	1.7
Final domestic demand	754.1	-8.8	15.2	3.2	2.3	2.3
Stockbuilding[1]	- 1.2	-1.3	-0.3	-0.8	0.5	0.0
Total domestic demand	752.9	-10.1	15.4	2.4	2.8	2.3
Exports of goods and services	183.1	-18.2	17.0	5.3	3.4	4.6
Imports of goods and services	174.4	-15.4	25.0	4.2	3.9	2.2
Net exports[1]	8.7	-0.7	-2.3	0.2	-0.2	0.5
Memorandum items						
GDP deflator	_	3.8	8.4	5.0	3.7	2.2
Consumer price index	_	1.8	4.0	7.9	7.0	3.2
Core inflation index[2]	_	1.9	2.2	4.7	5.6	3.1
Unemployment rate (% of labour force)	_	7.7	5.9	4.8	4.8	4.5
Current account balance (% of GDP)	_	1.2	-2.4	-4.1	-3.5	-2.2

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/cwr7ib

Annual headline consumer price inflation peaked at 8.8% in June and is now on a downward trajectory, but remains high. Core inflation reached 5.7% in October. The main drivers of high inflation have been rising food and energy prices. In addition, the currency has depreciated amid domestic political and global uncertainties, pushing one-year ahead inflation expectations to 4.8% in October, above the central bank inflation tolerance range of 1-3%. Wage increases have been contained, and real wages were down by 1.3% from a year earlier in August.

Monetary and fiscal policy will remain restrictive

To protect households from high inflation, the government has taken emergency measures, including waiving most taxes on petrol, giving vouchers to the poor to buy cooking gas and food, and increasing cash transfers for vulnerable households and the elderly. The government has also raised the minimum wage by 10% and allowed for a sixth extraordinary withdrawal from pension funds since the pandemic began. The government has appropriately committed to an ambitious fiscal consolidation path to ensure fiscal sustainability and maintain the credibility of the fiscal framework. In 2022, the fiscal deficit will be 2% of GDP, well below the limit of 3.7% foreseen by the fiscal rule. A welcome return to pre-pandemic fiscal rules should help to bring public debt under 30% of GDP by 2032, from 36% of GDP in 2021, and the fiscal deficit within 1% of GDP by 2026. Lagging formal job creation and high levels of poverty signal a need to provide targeted fiscal support. With inflationary pressures receding, the central bank will soon end the monetary policy tightening cycle, keeping policy rates unchanged until mid-2024 to ensure inflation expectations are re-anchored.

Economic growth will remain weak in an uncertain environment

Household consumption growth will be supported by the liquidity remaining from pension fund withdrawals and job creation but will be dampened by still high inflation, low household confidence, and significant monetary tightening. Recent SMEs financing support measures, new and extended tax exemptions and measures to foster public-private partnerships will support private investment, but only partly offset the impact of political uncertainty and high interest rates on business confidence and investment. Public investment will be subdued due to local and regional structurally low budget execution. GDP growth will pick up in 2024 as monetary conditions ease and global growth turns up. Inflation should slowly converge to the 2% target by the second half of 2024. The main downside risks to the outlook include increased domestic political uncertainty, higher-than-expected monetary policy tightening in advanced economies, social unrest related to fertiliser shortages and food and energy prices. Higher or lower growth in China, the main trading partner, could affect commodity prices and demand for exports.

Reforms to reignite growth and decrease inequalities are needed

Raising productivity and investment will hinge on stronger competition, higher quality public infrastructure and improved state capacity. A recent stimulus programme aims to boost investment, but implementation will remain challenging. More investment in renewables can help to diversify the economy and boost productivity, while reducing dependence on fossil fuels and costs. In the medium term, introducing a carbon tax and phasing out fossil fuel subsidies could support these efforts and create fiscal space to support the most vulnerable. Ensuring adequate funding for social and infrastructure spending will require improved spending efficiency and higher tax revenues. Reducing tax evasion and expenditures while enhancing the progressivity of the system will be key for inclusive growth. Expanding social protection coverage and benefits of social assistance programmes and reducing labour charges for low-income workers would curb informality. Improving the quality of public education and professional training would boost productivity and reduce informality and inequalities.

Poland

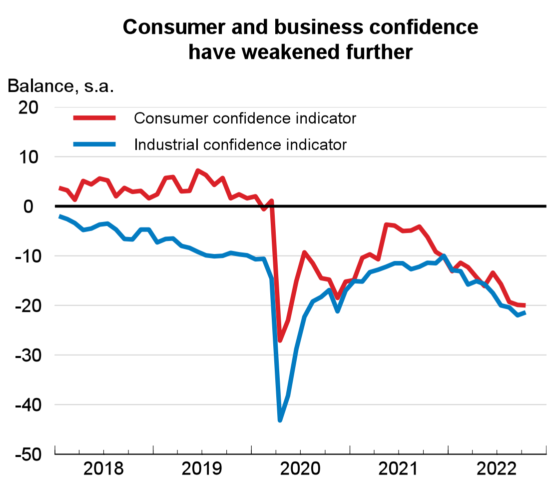
Real GDP growth is forecast to slow to 0.9% in 2023 due to higher energy prices as a result of Russia's war of aggression against Ukraine, weaker domestic demand and a deteriorating external environment, before recovering to 2.4% in 2024. Inflation should peak in early 2023 but is likely to remain above target by the end of 2024.

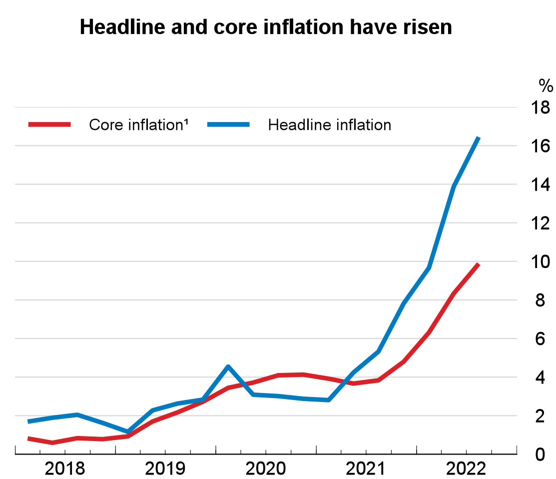
Monetary policy should continue to tighten to prevent persistently high inflation. Fiscal policy support should be better targeted towards vulnerable households and supporting refugees and needs to avoid adding to inflationary pressure. In the medium term, greater decarbonisation and digitalisation, underpinned by policies to improve skills, would enhance energy security and lead to greener and stronger economic growth.

The economy is slowing as a result of higher energy prices

Output in the second quarter of 2022 was only 0.3% higher than in the final quarter of 2021, amid high volatility. Private consumption grew, partly boosted by Ukrainian refugee spending and by the recovery from the pandemic, but investment slowed sharply. Nonetheless labour markets remain robust and wage growth has increased. Annual headline consumer price inflation rose to 15.7% in September, pushed up by higher energy and food prices, and core inflation reached 11.5%. Consumer and business confidence have continued to weaken and industrial production growth has slowed.

Poland





1. Consumer price index excluding food and energy.
Source: Eurostat, European Commission Business and Consumer Surveys; and OECD Economic Outlook 112 database.

StatLink https://stat.link/5jl27s

Poland: Demand, output and prices

Poland	2019	2020	2021	2022	2023	2024
	Current prices PLN billion	Percentage changes, volume (2015 prices)				
GDP at market prices	2 288.5	-2.0	6.8	4.5	0.9	2.4
Private consumption	1 322.3	-3.4	6.3	4.5	2.0	2.5
Government consumption	412.4	4.9	5.0	1.9	3.0	2.1
Gross fixed capital formation	432.9	-2.3	2.1	6.1	1.2	3.5
Final domestic demand	2 167.6	-1.6	5.2	4.2	2.0	2.6
Stockbuilding[1]	36.1	-1.1	3.0	3.9	-1.9	0.0
Total domestic demand	2 203.8	-2.8	8.3	9.3	0.3	2.4
Exports of goods and services	1 217.4	-1.1	12.5	3.6	1.2	1.5
Imports of goods and services	1 132.7	-2.4	16.1	6.8	1.8	1.5
Net exports[1]	84.7	0.6	-1.0	-1.6	-0.3	0.0
Memorandum items						
GDP deflator	_	4.3	5.1	11.5	8.9	5.4
Consumer price index	_	3.4	5.1	14.2	10.8	6.6
Core inflation index[2]	_	3.8	4.1	8.7	7.8	4.4
Unemployment rate (% of labour force)	_	3.2	3.4	2.9	3.5	3.8
Household saving ratio, net (% of disposable income)	_	7.3	0.4	-1.3	1.5	-0.4
General government financial balance (% of GDP)	_	-6.9	-1.8	-3.5	-4.9	-4.0
General government debt, Maastricht definition[3] (% of GDP)	_	57.2	53.8	51.9	53.6	54.9
Current account balance (% of GDP)	_	2.5	-1.5	-3.7	-3.5	-2.9

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/x9vky4

Poland imports around 60% of its energy but it has diversified its sources of energy supply away from Russia. The exchange rate has depreciated since February and energy and food prices have surged, accounting for most of the increase in headline inflation. Around 1.3 million Ukrainian refugees (equivalent to 3.5% of the Polish population) are currently hosted in Poland. Most have been able to find work, but many are working in elementary jobs. This has temporarily alleviated labour shortages in parts of the economy. Direct trade with Russia, Belarus and Ukraine, representing 3-5% of GDP before 2022, has decreased sharply as a result of sanctions.

Fiscal policy is supporting the economy but monetary policy is tightening

Fiscal policy will expand further to support households and firms against the impact of the war in 2023, before tightening in 2024. Existing support measures such as the Anti-Inflation Shield, which includes reductions in VAT and excise duties on energy and food, have been extended to the end of the year and support is assumed to continue in 2023. Heating subsidies have been introduced and electricity prices will remain capped. National defence spending is set to increase from 2.2% of GDP in 2022 to 3% by 2023 while healthcare spending is set to grow by 0.25% of GDP, adding to demand pressures. The government is also raising public sector salaries by 7.8% and increasing spending on social welfare programmes. Given persistently rising inflation, the key policy interest rate has been raised from 1.25% in November 2021 to 6.75% in September 2022 and has remained unchanged since then. Interest rates are anticipated to continue to rise until mid-2023 and reach 8%.

The economy is projected to slow amid high inflation and uncertainty

Real GDP growth is projected to slow to 0.9% next year before picking up to 2.4% over 2024. High uncertainty and lower consumer and business confidence will hold back domestic demand over 2023. Weaker growth in Poland’s major trading partners is projected to moderate export growth. Inflation will fall as retail energy price growth slows and tighter monetary policy takes effect, but will remain at 6.6% in 2024, above the central bank’s target range. Rising spare capacity will exert downward pressure on inflation while the economy recovers, partly driven by EU funds. There is considerable uncertainty and risks to the outlook remain tilted to the downside. Further escalation of the war would increase uncertainty, exacerbate inflation and strain public finances. Additional disruptions to energy supply could hit output and trade. Continued disagreements on strengthening the judiciary could further delay the disbursement of EU Recovery and Resilience Facility funds. On the upside, expansionary fiscal policy may prolong high inflation and require additional monetary tightening. A quick resolution of the war would boost growth and reduce inflation.

Policies should be coordinated and facilitate the green and digital transitions

Fiscal policy should continue to shield the most vulnerable households from inflation but should be better targeted, designed to incentivise energy savings, and should avoid adding inflationary pressure in the economy. Further diversifying energy imports and increasing investment in renewables would improve energy security and ensure greener growth. To facilitate the digital and green transitions and address skills shortages, labour market policies should upgrade weak basic skills and improve access to lifelong training for older adults, the unemployed and the low-skilled. Integration of refugees in the labour market should continue to be supported through childcare provision and language training.

Portugal

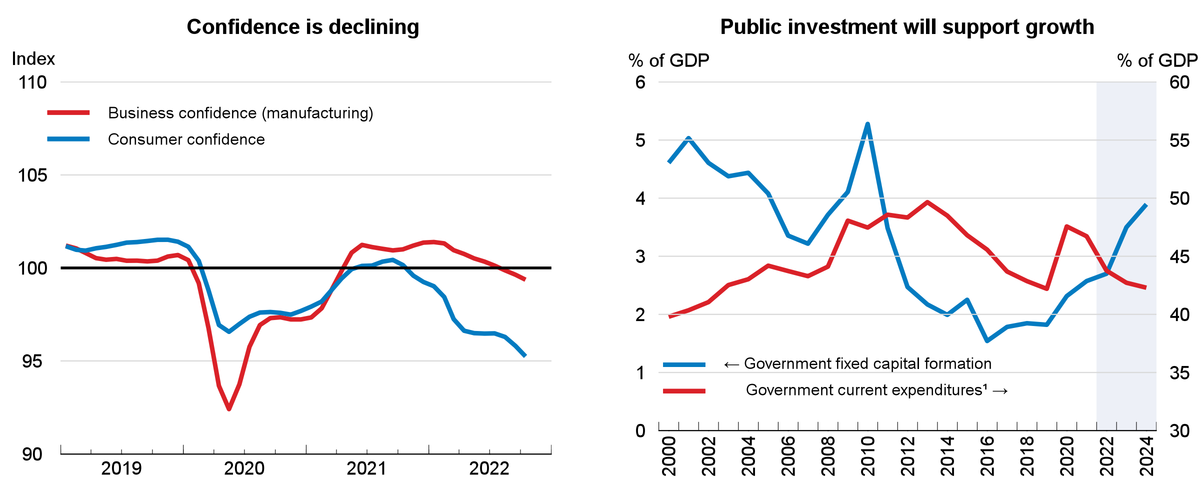
Real GDP growth is projected to decline from 6.7% in 2022 to 1% in 2023 and 1.2% in 2024, as Russia's war of aggression against Ukraine, supply-chain disruptions, elevated energy prices and rising interest rates weigh on activity. The Recovery and Resilience Plan (RRP) will boost public investment, but there are risks that implementation delays continue. Elevated energy and food prices will push headline consumer price inflation to 8.3% in 2022, before it moderates to 6.6% in 2023 and 2.4% in 2024. Wage growth will strengthen as the unemployment rate remains low, but not enough to protect households' purchasing power.

Fiscal policy will become more restrictive. Support measures, notably cash transfers, helped to smooth energy price shocks in 2022 but will be increasingly phased out in 2023. While the increase in public debt since 2019 has been moderate compared to other OECD countries, its high level and an ageing population make fiscal consolidation a priority. Ensuring an efficient and timely implementation of the RRP would boost green infrastructure, energy efficiency and the capacity to generate renewable energy, and help to offset the slowdown in 2023.

The recovery has lost steam

As the rebound in consumption and tourism fade, the slowing global economy, elevated energy prices, uncertainty and rising interest rates have started to weigh on activity. GDP grew by 0.4% on a quarterly basis in the third quarter of 2022. While historically-high employment rates, excess savings and government cash transfers are providing some support to households, consumer confidence has slowed, and the Bank of Portugal's coincident private consumption indicator continued to ease in September. Strong rises in production costs and materials shortages have negatively affected business confidence, and particularly sentiment in construction and industry. Wage growth has lagged behind annual consumer price inflation, which reached 10.6% in October, reducing household purchasing power.

Portugal



1. Current expenditures includes government final consumption, social security benefits, property income and other outlays.
Source: OECD Main Economic Indicators database; and OECD Economic Outlook 112 database.

StatLink https://stat.link/q04eox

Portugal: Demand, output and prices

Portugal	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2016 prices)				
GDP at market prices	214.4	-8.3	5.5	6.7	1.0	1.2
Private consumption	137.3	-7.0	4.7	5.4	0.3	1.0
Government consumption	36.4	0.3	4.6	1.9	2.3	1.8
Gross fixed capital formation	38.8	-2.2	8.7	1.7	2.6	3.5
Final domestic demand	212.6	-4.9	5.4	4.0	1.1	1.6
Stockbuilding[1]	0.8	-0.5	0.3	-0.1	-0.1	0.0
Total domestic demand	213.4	-5.3	5.6	3.9	1.0	1.6
Exports of goods and services	93.3	-18.6	13.5	17.4	3.5	3.0
Imports of goods and services	92.3	-11.8	13.3	10.4	3.4	3.9
Net exports[1]	1.0	-3.0	-0.2	2.6	0.0	-0.5
Memorandum items						
GDP deflator	_	2.0	1.4	5.3	6.4	2.9
Harmonised index of consumer prices	_	-0.1	0.9	8.3	6.6	2.4
Harmonised index of core inflation[2]	_	-0.2	0.2	5.1	4.9	2.4
Unemployment rate (% of labour force)	_	7.0	6.6	6.1	6.4	6.2
Household saving ratio, net (% of disposable income)	_	3.3	1.3	-3.3	-6.5	-5.5
General government financial balance[3] (% of GDP)	_	-5.8	-2.9	-1.8	-0.6	0.0
General government gross debt (% of GDP)	_	157.5	143.7	134.1	128.1	124.6
General government debt, Maastricht definition[4] (% of GDP)	_	134.9	125.5	115.9	109.9	106.4
Current account balance (% of GDP)	_	-1.0	-1.2	-1.6	-1.0	-1.0

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. Based on national accounts definition.
4. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/upvmt1

Elevated energy and commodity prices are raising costs for households and firms, despite energy support measures worth close to 1.6% of GDP in 2022. Monetary and financial conditions are also becoming less supportive. With almost 70% of housing loan rates fixed for only up to one year, higher interest rates will rapidly raise mortgage payments, holding back household consumption and investment. The risk of a reduction in energy supply appears contained. Portugal imports gas via ship and has the capacity to generate a notable share of electricity from renewables, reaching almost 55% of electricity generated between January and September 2022. There are limited energy connections between the Iberian Peninsula and the rest of Europe.

Policy support will ease

Fiscal policy is expected to become less supportive over 2023 and 2024. The budget deficit will narrow to 1.8% of GDP in 2022, as COVID-19-related spending is phased out and additional tax revenues due to greater-than-expected inflation help to offset the cost of energy support measures. In 2022, support totalling 1.6% of GDP includes one-off cash transfers to households (EUR 1.9 billion) and lower energy prices through reduced taxes and tariffs and public transport prices (EUR 1.7 billion). Some energy measures have been extended into 2023 (EUR 648 million), such as reduced taxes on fuels and electricity and public transport prices. The Energy Bill Support Package for Companies will lower electricity and gas costs for firms. Energy measures are assumed to have been phased out by 2024. Measures under the 2022 Medium-Term Agreement on improving incomes, wages and competitiveness will also support household income, including through the increase in the minimum wage by 8% in 2023 and fiscal incentives for firms to raise wages. The implementation of the RRP will boost investment. Spending from grants is projected to start at 0.5% of GDP in 2022, increasing to 1.5% of GDP in 2023 and 1.9% of GDP in 2024.

Growth is slowing

GDP growth is projected to moderate to 1% in 2023 and 1.2% in 2024. Consumption growth will weaken as monetary and financial conditions become less supportive, pent-up demand eases, employment growth slows and elevated inflation lowers purchasing power. However, energy support measures and rising wages will provide some offset. Export growth will ease as the rebound in tourism ends and global growth slows. Investment will be boosted by European funds. Headline consumer price inflation will moderate to 6.6% in 2023 and 2.4% in 2024 as energy prices stabilise and spare capacity rises. High nominal GDP growth will help to lower public debt (Maastricht definition) to just over 106% of GDP in 2024. If wages increase by more than projected, this would boost consumption and inflation. However, a larger-than-expected decline in the housing market would further weigh on consumer sentiment and residential investment. Additional delays in RRP spending would also constrain activity and the green transition.

Policy can support sustainable growth

Additional support measures against rising energy prices should remain temporary, become increasingly targeted on the most vulnerable households and firms and maintain incentives for energy reductions. Investments under the RRP will increase energy efficiency, green infrastructure and the capacity to generate renewable energy. Ensuring the complete implementation of the RRP in a timely manner is key to maximise the benefits. Maintaining the government’s focus on fiscal consolidation should help limit increases in borrowing costs as euro area monetary policy normalises. A clear and credible medium-term fiscal strategy would further support external credibility. While levels of education have improved drastically over the past two decades, they remain below the OECD average and participation in adult education is low. Continuing to support lifelong learning will be crucial to boost incomes and productivity.

Romania

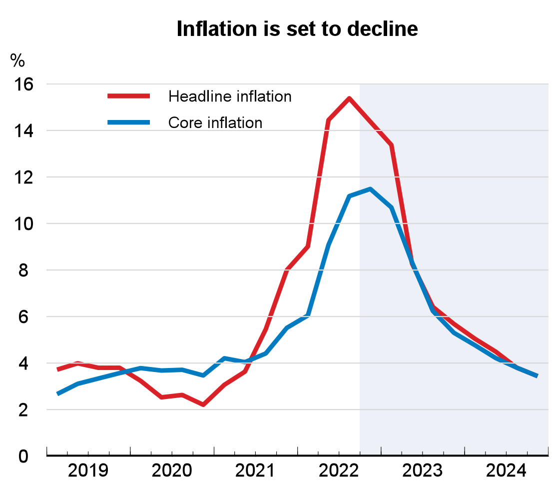
Output growth of 6.5% is projected for 2022, largely reflecting a strong recovery from the economic impact of COVID-19 early in the year. Quarterly growth in the second half of 2022 is being damped by the effects of high inflation on consumption and reduced foreign demand on exports. Output growth will gradually strengthen as these effects diminish. Increased inflows of EU funds will provide additional impetus to investment. Real GDP growth is projected at 1.4% in 2023 and 2.8% in 2024. Uncertainty about commodity prices and energy supply relating to Russia's war of aggression against Ukraine is a key risk.

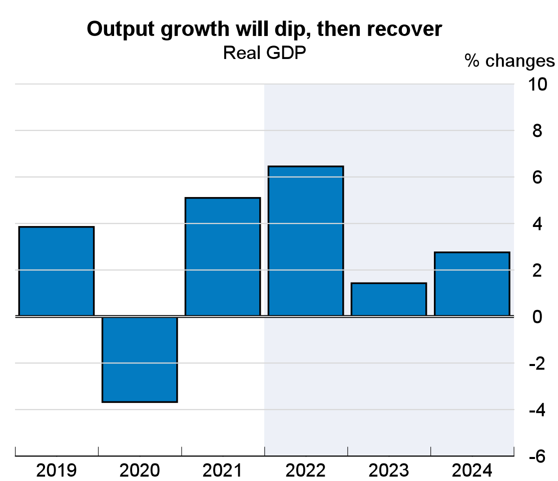
With headline consumer price inflation expected to be 13.3% in 2022, tighter monetary policy should continue to re-anchor inflation expectations and bring inflation back towards target. Fiscal consolidation should continue in 2023 and 2024. The government should target cost-of-living support to low-income households. An expansion of the tax base is needed in the medium term. Greening the energy mix and achieving more efficient energy use, notably in housing, needs to be a priority.

Rising interest rates and a bad harvest are weighing on economic activity

Solid GDP growth in the first half of 2022, driven by household consumption and exports, was reflected in falling unemployment. The unemployment rate declined further over summer, to 5.2% in September. Output growth is showing signs of slowing. Industrial production decreased by 1% in August (year-on-year) and the grain harvest is estimated to be 25% lower than in 2021 due to drought. Headline inflation reached 15.3% in October (year-on-year). In recent months, food price inflation has continued to rise while increases in other components of the consumer price index have decelerated.

Romania





Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/jzxkg9

Romania: Demand, output and prices

Romania	2019	2020	2021	2022	2023	2024
	Current prices RON billion	Percentage changes, volume (2010 prices)				
GDP at market prices	1 063.8	-3.7	5.1	6.5	1.4	2.8
Private consumption	662.5	-3.9	7.1	5.9	1.5	2.0
Government consumption	186.6	1.1	0.4	0.4	2.3	2.5
Gross fixed capital formation	244.5	1.1	2.9	4.4	3.7	4.0
Final domestic demand	1 093.5	-1.8	4.9	4.6	2.1	2.6
Stockbuilding[1]	13.9	-0.6	1.1	2.1	-1.0	0.0
Total domestic demand	1 107.4	-2.3	6.0	6.5	1.1	2.5
Exports of goods and services	427.6	-9.5	12.5	6.5	1.7	3.1
Imports of goods and services	471.3	-5.2	14.6	6.6	1.0	2.4
Net exports[1]	- 43.6	-1.5	-1.4	-0.4	0.2	0.1
Memorandum items						
GDP deflator	_	4.1	5.4	15.8	8.0	4.6
Consumer price index	_	2.6	5.0	13.3	8.3	4.2
Core consumer price index[2]	_	3.7	4.5	9.5	7.6	4.0
Unemployment rate (% of labour force)	_	6.1	5.6	5.5	6.1	6.1
General government financial balance (% of GDP)	_	-9.2	-7.1	-6.3	-6.0	-5.5
General government gross debt (% of GDP)	_	58.9	57.6	57.9	61.1	64.1
General government debt, Maastricht definition[3] (% of GDP)	_	46.9	48.9	49.2	52.3	55.4
Current account balance (% of GDP)	_	-4.9	-7.3	-8.4	-7.8	-7.2

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/le5rz0

Romania's direct trade and financial links to Russia and Ukraine are small. In 2020, Ukraine was the destination of 1% of goods exports and for Russia the share was 1.6%. Around 70% of Romania's energy comes from domestic production and around one quarter of energy consumed is from renewable sources. Also, Romanian natural gas production in the Black Sea is coming on stream. However, the country's integration into European oil and gas markets means it shares with other European countries the high level of uncertainty about the future supply and price of energy. Around 1.3 million border crossings directly from Ukraine into Romania had been recorded as of September 2022 with additional inflows via Moldova. Most incoming refugees transit to other countries; around 80 000 (equivalent to 0.4% of Romania's population) have remained in Romania according to United Nations estimates.

The monetary stance has tightened

In response to inflationary pressures the central bank has increased its policy rate since late last year from 1.5% to 6.75% in November. It is expected the rate will now remain unchanged until late in 2024. Fiscal spending is being pushed up by measures to shield consumers' spending power, including a cap on electricity and gas prices that is in place until August 2023. Outlays on the measures amount to around 1.5% of GDP. Nevertheless, the fiscal deficit is projected to narrow. For 2022, strong growth in economic activity in the first half of the year and termination of COVID-19 support outweigh energy-bill support. Further deficit reduction is expected in 2023 and 2024, reflecting reduced spending on support and recovery in economic activity. Implementation of the Next Generation EU Plan is expected to see around one-third of available funds accessed by the end of 2024.

Growth will slow and then pick up gradually

Growth will weaken from 6.5% in 2022 to 1.4% in 2023, reflecting weaker household consumption and external demand. Inflation is projected to decline due to easing oil and food prices along with rising unemployment. Inflation is projected to reach the upper bound of the central bank's target (2.5% within a target band of +/-1 percentage point) in 2024. Policy rate cuts are expected to commence in late 2024. Uncertainty around future commodity prices and energy supply are key risks. The continued wide trade deficit, though largely funded by foreign direct investment and EU funds, remains a concern. A faster uptake of EU funds would bolster activity.

Tax reform could improve public finances and reduce inequality

Macroeconomic policy needs to remain responsive to changing conditions in steering a course towards lower inflation while avoiding a substantial economic downturn. For the medium term, expanding the tax base, notably by removing special tax regimes and exemptions, would improve public-finance sustainability and make the tax system more equitable. Improving living standards and reducing disparities, including those across regions, requires improvements in coverage and adequacy of social assistance, further efforts to tackle corruption and more infrastructure investment. The latter would be helped by increasing the capacity to absorb EU funds. Better take up of EU funds would also help the green transition, including through accelerating building refurbishment and investment in renewable energy.

Slovak Republic

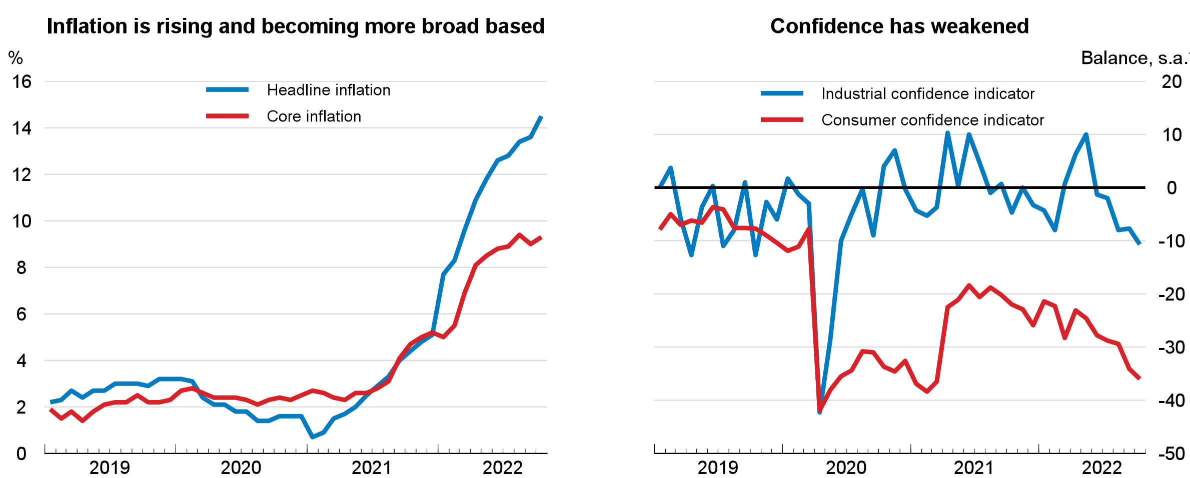
The economy is projected to grow by 1.6% in 2022, 0.5% in 2023 and 2.1% in 2024. High inflation will weigh on household disposable income and private consumption. Continuing supply chain disruptions and weaker global demand will hold back export growth in 2023. Investment growth will remain robust, sustained by the absorption of EU funds. Growth will strengthen in 2024 as supply disruptions and inflation abate. A prolongation of Russia's war of aggression against Ukraine would increase the risk of energy supply shortages and higher inflation, with severe negative consequences for growth.

While large increases in food and energy prices may call for fiscal support, measures should be temporary and targeted on the most vulnerable. Greater fiscal restraint is needed to avoid fuelling inflationary pressures but also to ensure public finance sustainability over the longer run, especially in view of demographic challenges. Investment in the green transition should be accelerated to enhance energy security and reduce dependence on imported oil and gas.

Economic growth has weakened

The economy continued to grow robustly in the third quarter of 2022 (0.3% quarter-on-quarter). High-frequency indicators suggest that the economy has been slowing in the last quarter of the year. Business and consumer confidence have weakened since Russia's invasion of Ukraine. Harmonised consumer price inflation accelerated to 14.5% in October as food and, to a lesser extent, energy prices continued to rise, adding to pre-existing pressures from supply chain bottlenecks. Inflation has become broad-based, with core inflation reaching 9.3% in October. While the labour market has continued to recover, the registered unemployment rate remains above pre-pandemic levels, at 6.1% in September 2022.

Slovak Republic



1. Values of the confidence indicators range from -100 (responses of all respondents are totally pessimistic) to 100 (responses of all respondents are totally optimistic).
Source: Eurostat; and Statistical Office of the Slovak Republic.

StatLink https://stat.link/67lyer

Slovak Republic: Demand, output and prices

Slovak Republic	2019 Current prices EUR billion	2020	2021	2022	2023	2024
		Percentage changes, volume (2015 prices)				
GDP at market prices	94.4	-3.4	3.0	1.6	0.5	2.1
Private consumption	53.2	-1.4	1.8	4.1	-2.9	2.0
Government consumption	18.5	-0.6	4.2	-1.6	0.6	0.2
Gross fixed capital formation	20.3	-10.8	0.2	4.1	10.3	2.2
Final domestic demand	92.0	-3.3	2.0	2.8	0.3	1.7
Stockbuilding[1]	2.2	-1.9	2.0	-0.4	0.0	0.0
Total domestic demand	94.2	-4.8	4.2	2.3	0.2	1.6
Exports of goods and services	86.7	-6.5	10.6	-2.0	2.1	5.6
Imports of goods and services	86.5	-8.3	12.0	-1.2	1.6	4.9
Net exports[1]	0.2	1.7	-0.9	-0.8	0.3	0.4
Memorandum items						
GDP deflator	_	2.4	2.4	7.3	12.1	4.4
Harmonised index of consumer prices	_	2.0	2.8	12.0	15.5	5.1
Harmonised index of core inflation[2]	_	2.4	3.3	8.1	7.9	5.0
Unemployment rate (% of labour force)	_	6.7	6.8	6.3	6.7	6.5
Household saving ratio, net (% of disposable income)	_	5.1	4.9	-2.6	-3.3	-0.8
General government financial balance (% of GDP)	_	-5.4	-5.5	-3.4	-5.0	-3.1
General government gross debt (% of GDP)	_	79.2	81.5	80.6	79.9	79.9
General government debt, Maastricht definition[3] (% of GDP)	_	58.9	62.2	61.4	60.7	60.6
Current account balance (% of GDP)	_	0.6	-2.5	-7.3	-7.0	-6.3

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/y2swrt

Prior to Russia's invasion of Ukraine, Slovakia was strongly dependent on oil and gas imports from Russia. Pre-existing supply bottlenecks intensified over the course of 2022. Together with the surge in energy prices, this led some energy-intensive industries to suspend production in August. In line with the EU plan to enhance energy security, Slovakia increased gas inventories to 94% of capacity in October. Additionally, gas consumption in August and September was 24% lower than in previous years. Diversification of gas import providers will be facilitated by the newly inaugurated pipeline with Poland, which will open access to terminals in the Baltic Sea and to Norwegian gas. Around 100,000 Ukrainian refugees have applied for temporary residence in Slovakia. This is expected to boost the labour force by around 1% in 2022.

The government plans a significant expansion of support to mitigate the energy crisis

In August 2022, Parliament approved permanent increases of family benefits (higher child allowances and tax breaks) to mitigate the increasing cost of living, costing 1% of GDP per year. Moreover, a one-time payment for pensioners was approved in 2022 (0.2% of GDP) and firms can receive a subsidy to partially cover their energy costs above a specific threshold of the wholesale electricity and gas prices for September-October 2022 and January-March 2023 (0.5% of GDP). Overall, the draft budget for 2023 includes a reserve of EUR 3.5 billion (3.4% of GDP) for measures to support households and firms. The projections posit that a large part of these measures will be implemented, leading to a marked fiscal expansion in 2023. Structural consolidation is assumed to start in 2024. Funds from the EU Recovery and Resilience Plan of around 1.3% of GDP on average per year over the period 2022-24 will boost investment. In addition, Slovakia can still draw about 5% of GDP of unused 2014-20 EU Cohesion funds by 2023.

Economic growth is set to slow sharply in 2023

High inflation will lead to declines in real wages, disposable incomes and private consumption in 2023. Continuing supply chain disruptions and faltering foreign demand will weigh on exports. Some regaining of export market shares is projected for 2024 as supply disruptions abate. High uncertainty will weigh on private investment, but substantial inflows of EU funds will boost government investment in 2023. Headline inflation will increase in 2023 due to delayed pass-through of market energy prices to regulated electricity, gas and heating prices and to a lesser extent the assumed fiscal expansion. Inflation is projected to slow in 2024 due to reductions in energy and food prices and the tighter monetary stance in the euro area. Unemployment will increase only moderately as the short-time work scheme was recently made permanent. Risks are skewed to the downside and largely related to the war in Ukraine. An intensification of the energy crisis could lead to energy rationing with severe impacts on investment and exports. Higher and more prolonged inflation would further erode disposable income and depress private consumption. The budget deficit could be lower in 2023 if unspent EU funds are allowed to be used to finance the crisis measures.

Fiscal support should be temporary and targeted

The planned fiscal support for households and business should be temporary and targeted on the most vulnerable and preserve energy savings incentives. Fiscal policy should be prudent to reduce inflationary pressures and build up fiscal space to prepare for long term fiscal challenges, such as population ageing. Consolidation measures should be specified in line with the recently adopted expenditure ceilings. Accelerating investment for the green transition should be a priority to enhance energy security. Strengthening active labour market policies, such as training, can help the integration of Ukrainian refugees and support workers during the green and digital transitions.

Slovenia

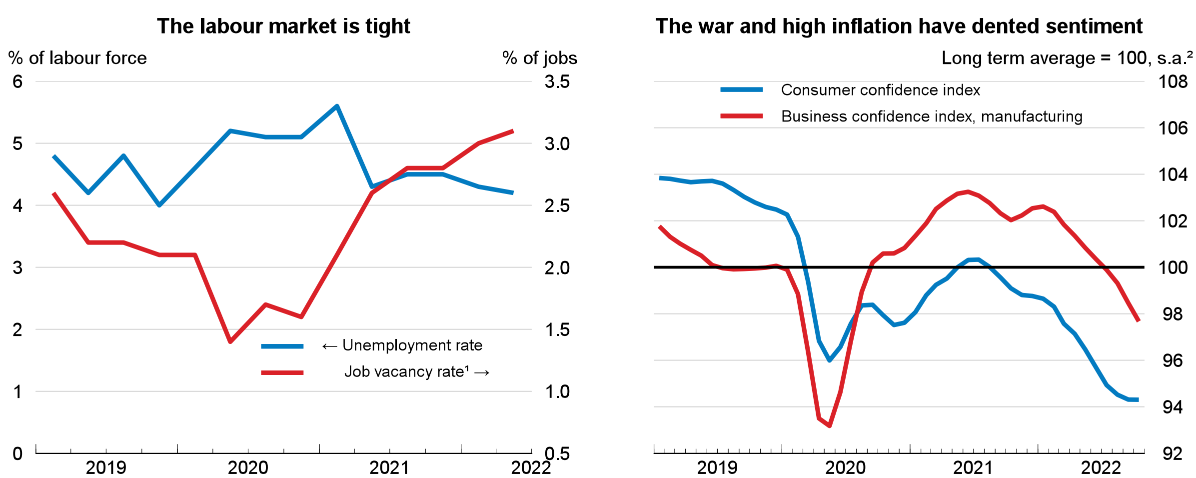
GDP growth is projected to slow from 5% in 2022 to 0.5% in 2023, reflecting higher inflation, weaker external demand and the negative impact on confidence from Russia’s war of aggression against Ukraine. Despite slowing activity, the labour market is expected to remain tight, fuelling stronger wage growth and contributing to inflationary pressures. Nonetheless, real wages will fall, damping private consumption. Growth will pick up to 2% in 2024 as inflation slowly recedes.

Fiscal policy will remain supportive in 2023, before tightening in 2024. Government measures aim to mitigate the effects of increasing energy prices on households. Fiscal support should be targeted on low-income households, preserve energy saving incentives and be financed by spending cuts, as the current expansionary fiscal stance risks intensifying inflationary pressures. Structural reforms to address labour shortages and raise potential growth should focus on reducing labour taxes, financed by higher environmental and property taxes.

Economic activity has proven resilient so far

Economic activity continued to grow in the first half of 2022 driven by strong private consumption. This came despite higher inflation, a worsening external environment and a deterioration of consumer and business sentiment due to the war in Ukraine. Growth continued into the summer, supported by the expansion of service activities. However, retail trade turnover (without volatile automotive fuel sales) registered weaker growth of 0.4% month-on-month in September, while industrial production growth turned negative. The labour market remains tight with an unemployment rate of 4.1% in September, and the job vacancy rate at a historic high. The tight labour market is also reflected in stronger wage growth, with nominal gross wages rising by 5.7% year-on-year in August. Such domestic price pressures have contributed to a rise in core inflation to 6.6% in September. Headline inflation reached 11.7% in July but has declined to 10.3% in October, helped by a cap on electricity and gas prices.

Slovenia



1. The job vacancy rate measures the proportion of total posts that are vacant, expressed as the ratio of the number of job vacancies to the number of occupied posts plus the number of job vacancies.
2. OECD standardised, amplitude adjusted.
Source: Statistical Office of Slovenia; and OECD Main Economic Indicators database.

StatLink https://stat.link/jyfozm

Slovenia: Demand, output and prices

Slovenia	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2010 prices)				
GDP at market prices	48.5	-4.3	8.2	5.0	0.5	2.0
Private consumption	25.5	-6.9	9.5	7.6	0.2	2.1
Government consumption	8.9	4.1	5.8	0.7	1.0	0.8
Gross fixed capital formation	9.5	-7.9	13.7	4.2	0.9	3.1
Final domestic demand	43.8	-4.9	9.6	5.3	0.5	2.1
Stockbuilding[1]	0.5	0.1	0.4	3.0	0.3	0.0
Total domestic demand	44.4	-4.7	9.9	7.3	1.1	2.0
Exports of goods and services	40.6	-8.6	14.5	6.7	2.2	3.0
Imports of goods and services	36.4	-9.6	17.6	10.3	2.5	3.0
Net exports[1]	4.2	0.0	-0.8	-2.3	-0.2	0.0
Memorandum items						
GDP deflator	_	1.3	2.6	6.6	7.5	4.4
Harmonised index of consumer prices	_	-0.3	2.0	9.2	7.5	4.4
Harmonised index of core inflation[2]	_	0.8	0.9	5.7	5.7	4.3
Unemployment rate (% of labour force)	_	5.0	4.8	4.3	4.5	4.9
Household saving ratio, net (% of disposable income)	_	16.3	12.1	2.5	4.0	3.8
General government financial balance (% of GDP)	_	-7.7	-4.7	-3.8	-5.0	-4.0
General government gross debt (% of GDP)	_	109.8	95.2	95.4	98.0	99.9
General government debt, Maastricht definition[3] (% of GDP)	_	79.6	74.5	74.7	76.7	78.1
Current account balance (% of GDP)	_	7.6	3.8	-0.2	-0.8	0.0

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/zl8fxo

Direct trade with Russia and Ukraine was low at the onset of the war, although nearly all gas and 17% of oil and petroleum imports came from Russia. Since then, dependence on Russian gas and oil imports has been reduced through the diversification of suppliers. Also, gas storage targets were met earlier than expected. Nonetheless, higher international energy prices have a negative impact on the trade balance and contribute to inflationary pressures. Higher gas prices are also weighing on gas-intensive manufacturing (such as basic metals, chemicals, paper and paper products), which accounts for 4.5% of employment, more than almost anywhere else in Europe.

Fiscal policy remains supportive

The government responded to the energy crisis with a fiscal package of 0.6% of GDP in 2022 and announced further spending of 2% of GDP for 2023. This includes direct subsidies to households and businesses and temporary tax cuts. The government also capped the price of electricity and gas in September for one year for households and small businesses. Temporary measures are assumed to be phased out in 2023. In addition, structural measures include higher pension benefits due to higher pension indexation and higher replacement rates. These measures are expected to increase the budget deficit to 5% of GDP in 2023, before the fiscal stance is tightened in 2024. The supportive fiscal stance adds to demand pressures. This comes at a time when euro area policy interest rates may be lower than needed to contain inflation and inflation expectations in Slovenia, as in other peer economies with strong growth and inflation.

Economic activity is set to slow

Growth is projected to slow in 2023, reflecting high inflation and weaker foreign demand. Private consumption will be hit by the impact of high inflation on households' disposable income. Weaker demand and higher interest rates will slow investment, although the inflow of EU funds should moderate the fall to some extent. The labour market will remain tight, contributing to stronger wage growth. This, together with high energy and food prices, will keep headline inflation elevated. Only in 2024 will growth pick up as foreign demand recovers and headline inflation slowly recedes, reflecting declining domestic demand pressures on the back of fiscal tightening. Downside risks depend on the continuation and intensity of the war in Ukraine and its impact on international energy markets and trade. Colder-than-usual winters could still force the government to ration supplies for heavy industrial users. On the upside, stronger labour force participation of older workers and migration could help reduce labour market shortages and wage pressures.

Fiscal policy needs to tighten and reduce demand pressures

Faster fiscal consolidation is needed to reduce demand pressures. Support should be financed by cuts to other recurrent spending and be better targeted. This entails replacing energy price caps with temporary direct subsidies for low-income households that preserve energy saving incentives. Efforts to diversify gas supply, including the expansion of LNG capacity held in other countries and in coordination with the European Union, will help improve energy security. Such efforts should be implemented alongside structural reforms to raise potential growth and address labour shortages. This includes a growth-friendly tax reform with lower labour taxes, financed by higher environmental and property taxation.

South Africa

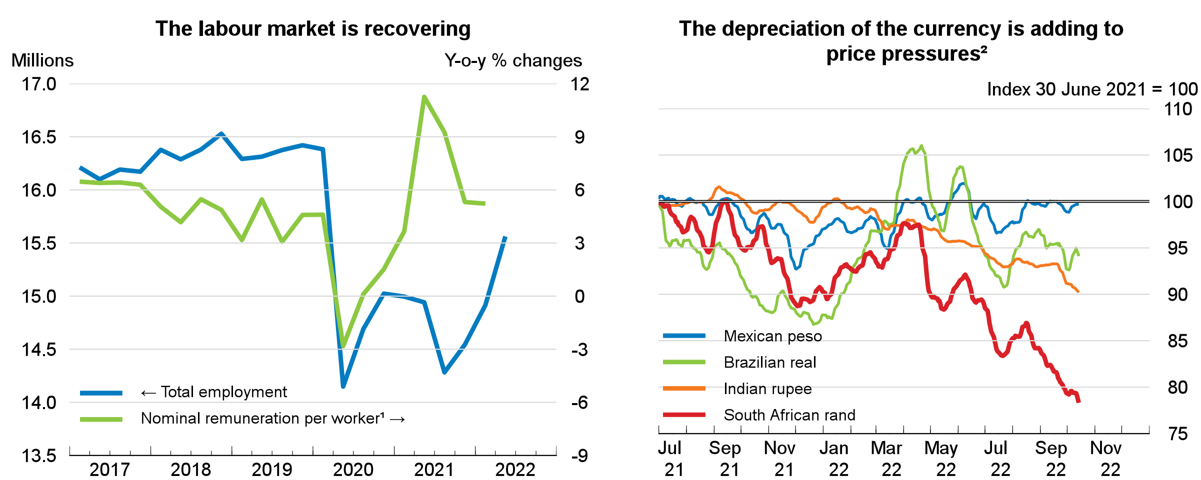
GDP is projected to grow by 1.7% in 2022, 1.1% in 2023, and 1.6% in 2024. Private consumption and investment will remain the main drivers of growth. Household spending remains supported by social transfers and an improving labour market. Private investment will rise as companies replace an increasingly obsolete capital stock. Inflation is projected to slowly fall in response to tighter monetary policy. Risks to growth include prolonged electricity shortages and more persistent inflationary pressures than expected, potentially delaying the reduction of policy rates.

Fiscal risk has eased thanks to a favourable commodity cycle, but debt-servicing costs are rising. Efforts to rein in the public sector wage bill and to address weaknesses in the management of public procurement and state-owned enterprises should continue. Redesigning tax exemptions would lower distortions, increase revenues, and improve equity. Monetary policy should continue to tighten until inflation comes close to the South African Reserve Bank mid-point target. The planned split of the national power company should proceed to allow other producers to compete and complement capacity, while also bringing prices down.

Power outages weigh on the economic recovery

After two quarters of positive real GDP growth, flooding in KwaZulu Natal and extensive electricity outages contributed to a contraction of 0.7% (quarter-on-quarter) in the second quarter of 2022. The flooding damaged factories and disrupted supply chains. Power outages affected trading hours in services, mining, manufacturing and agriculture. Lower fuel prices contributed to an easing of consumer price inflation to 7.5% in September, down from a peak of 7.8% in July. The unemployment rate fell close to 34% and job creation increased to its highest level since 2020. However, nominal wage growth is still lower than the inflation rate.

South Africa



1. Non-agricultural public and private sectors.
2. Nominal US dollar exchange rate, 7-day moving averages.
Source: Statistics South Africa; South African Reserve Bank; Refinitiv; and OECD calculations.

StatLink https://stat.link/pts40b

South Africa: Demand, output and prices

South Africa	2019 Current prices ZAR billion	2020	2021	2022	2023	2024
		Percentage changes, volume (2015 prices)				
GDP at market prices	5 613.7	-6.3	4.9	1.7	1.1	1.6
Private consumption	3 588.9	-5.9	5.6	3.1	1.7	1.8
Government consumption	1 104.5	0.8	0.6	1.2	0.9	1.4
Gross fixed capital formation	865.5	-14.6	0.2	4.5	4.2	7.0
Final domestic demand	5 558.9	-5.9	3.8	2.9	1.9	2.4
Stockbuilding[1]	24.5	-1.8	0.9	0.7	0.1	0.0
Total domestic demand	5 583.3	-8.0	4.8	3.7	2.0	2.4
Exports of goods and services	1 532.4	-11.9	10.0	7.3	1.9	3.3
Imports of goods and services	1 502.1	-17.4	9.5	15.0	4.9	5.9
Net exports[1]	30.3	1.8	0.1	-2.0	-0.9	-0.9
Memorandum items						
GDP deflator	_	5.7	6.2	4.7	4.5	3.6
Consumer price index	_	3.3	4.6	6.6	5.9	4.9
Core inflation index[2]	_	3.4	3.1	4.5	5.8	5.0
General government financial balance (% of GDP)	_	-11.3	-6.6	-6.3	-6.1	-5.7
Current account balance (% of GDP)	_	2.0	3.7	0.1	-0.6	-0.8

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/itlmwq

As the fleet of coal-fired generators ages, falling energy generation capacity has prompted further electricity cuts, and weak governance in the state power company has pushed up the cost of electricity. Movements in the international price of crude oil have contributed to rising domestic fuel prices, exacerbated by currency depreciation. To cushion the impact of higher fuel prices, the government reduced the fuel levy from April to July 2022, at a fiscal cost of around 0.1% of GDP.

Fiscal and monetary policy are turning contractionary

The commodity cycle boom has boosted tax revenues. These windfall revenues have allowed the government to prolong the Social Relief Distress grant until March 2024 and to introduce temporary measures to cushion the impact of inflation, without adding pressure on public finances. The fiscal balance this year should outperform budget forecasts. However, debt remains above 70% of GDP and rising debt-service costs already represent 15% of government spending. The fiscal stance is expected to be contractionary in 2023 and 2024 to consolidate public finances, achieved mostly by containing the public sector wage bill. The central bank increased the policy rate by 75 basis points to 6.25% in September 2022. Monetary policy is expected to continue tightening, with the policy rate reaching 7.25% in early 2023 and staying at that level until core inflation falls close to 5%, anchoring inflation expectations and limiting pressures on the exchange rate.

The challenging global outlook worsens domestic growth prospects

Growth will continue to be driven by the recovery of private consumption and investment. Social transfers, better employment prospects and falling saving rates should sustain private consumption, although attenuated by high inflation and tighter financial conditions in 2023-24. Private investment will continue its recovery to pre-pandemic levels despite less favourable financial conditions, as capital stocks need replacement. Nonetheless, the price of South Africa's commodity exports is expected to fall in 2023-24, leading to a deterioration in the terms of trade and the current account balance. Lower global growth will also weigh on exports in the near term. Core inflation is likely to continue increasing until early 2023, when rents and medical insurance premiums are set to increase. Tighter monetary policy will slowly bring inflation down in 2023-24. Downside risks to growth include electricity supply which will remain tight with a high risk of prolonged outages. Pushback against public-sector wage restraint and financially distressed state-owned enterprises are major fiscal risks. Additional tightening of global financial conditions and the potential volatility of capital flows are risks to the exchange rate. On the upside, if the recovery of international tourism outpaced expectations, this would provide additional support to growth.

Boosting productivity and strengthening the tax system are key priorities

Allowing private providers of renewable energy to feed power into the grid would help reduce electricity shortages, while creating incentives for private investors to develop clean and cost-effective electricity generation capacity. Broadening the base of corporate and personal income taxes, by redesigning tax exemptions, and raising property and environmental taxes, would create fiscal space to finance growth-enhancing reforms, while also improving the efficiency and equity of the tax system. The fiscal space should be used to improve the quality of energy, transport and telecommunications infrastructure, which would give a boost to productivity growth and living standards.

Spain

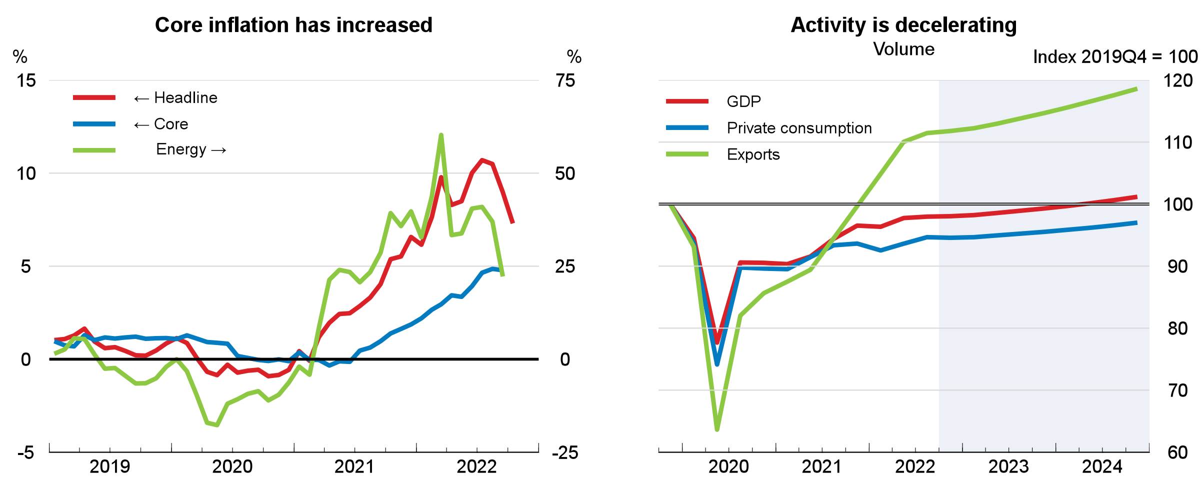
Activity is projected to grow by 1.3% in 2023 and 1.7% in 2024, after increasing by 4.7% in 2022. High inflation will curb household purchasing power, but savings accumulated during the pandemic will support consumption. With deteriorating demand prospects and rising financing costs, private investment is expected to remain subdued. The slowdown in key trading partners will dent exports. Inflation will peak at 8.6% in 2022 and then decline to 4.8% in 2023 and 2024.

Fiscal measures aimed at sheltering households and firms from the rise in energy prices will need to be reviewed periodically to ensure they are warranted, targeted towards the most exposed and compatible with fiscal and environmental policy targets. A timely and effective use of Next Generation EU funds will be key to support investment, boost long-term productivity and achieve the green transition.

Signs of a slowdown are accumulating

Economic growth slowed in the third quarter of 2022, with GDP rising by 0.2% after 1.5% in the second quarter. Consumer confidence fell to very low levels, close to those reached in the beginning of the pandemic. The unemployment rate rose to 12.7% in the third quarter after 12.5% in the second. Although it receded from a peak at 10.7% in July 2022, inflation remains high, standing at 7.3% in October, and core inflation reached 4.8% in September. The wage rate increased by 3.3% between the third quarter of 2021 and the same quarter of 2022. The government has agreed to raise the salary of public workers by a total of at least 8% and up to 9.5% (depending on the evolution of inflation and GDP) cumulated over 2022, 2023 and 2024.

Spain



Source: Instituto Nacional de Estadistíca; Eurostat; and OECD Economic Outlook 112 database.

StatLink https://stat.link/z2drj9

Spain: Demand, output and prices

Spain	2019	2020	2021	2022	2023	2024
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
GDP at market prices	1 245.5	-11.3	5.5	4.7	1.3	1.7
Private consumption	714.5	-12.2	6.0	2.0	1.3	1.4
Government consumption	234.9	3.5	2.9	-1.8	0.9	0.7
Gross fixed capital formation	249.5	-9.7	0.9	5.4	2.3	3.7
Final domestic demand	1 199.0	-8.7	4.2	1.9	1.4	1.7
Stockbuilding[1]	9.9	-0.8	1.0	-0.2	0.0	0.0
Total domestic demand	1 208.9	-9.4	5.3	1.6	1.4	1.7
Exports of goods and services	434.8	-19.9	14.4	18.1	3.5	3.2
Imports of goods and services	398.2	-14.9	13.9	9.7	4.2	3.4
Net exports[1]	36.6	-2.2	0.3	3.1	-0.2	0.0
Memorandum items						
GDP deflator	_	1.2	2.3	3.0	3.8	4.5
Harmonised index of consumer prices	_	-0.3	3.0	8.6	4.8	4.8
Harmonised index of core inflation[2]	_	0.5	0.6	4.0	4.8	3.7
Unemployment rate (% of labour force)	_	15.5	14.8	12.9	12.9	12.7
Household saving ratio, net (% of disposable income)	_	10.8	7.0	4.2	4.2	2.3
General government financial balance (% of GDP)	_	-10.1	-6.9	-4.9	-4.2	-3.7
General government gross debt (% of GDP)	_	148.2	142.7	140.3	139.7	137.6
General government debt, Maastricht definition[3] (% of GDP)	_	120.4	118.3	115.9	115.2	113.1
Current account balance (% of GDP)	_	0.6	1.0	0.7	0.6	0.4

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/7c543l

The government has implemented two successive sets of fiscal measures to attenuate the impact of the rise in prices. The first one, effective from April to June 2022, and estimated to cost EUR 6 billion (0.5% of annual GDP), included tax rebates and direct aid to firms and households, notably a rebate on motor fuels. The second one, covering the second half of 2022, amounts to around EUR 9 billion (0.7% of GDP), of which EUR 5.5 billion are spending measures and EUR 3.6 billion are tax cuts (extending those in the first package and a new cut in the VAT rate on electricity from 10% to 5%). Furthermore, in June, the European Commission approved public aid worth EUR 6.3 billion, effective until May 2023, in direct grants to electricity producers (the so-called “Iberian exception”). Finally, the VAT rate on gas was reduced from 21% to 5% from October until December 2022 and the government announced in October new measures worth EUR 3 billion, including regulated gas prices for collective residential heating systems until the end of 2023, and new subsidies on low-income households’ heating and electricity bills.

Fiscal support will be adjusted

The general government deficit is expected to decline to 4.2% of GDP in 2023 and 3.7% in 2024, after 4.9% in 2022. The draft budget for 2023 features a 10.5% rise in social spending and a 25% rise in defence spending. Pensions will be raised by around 8.5%. New tax measures, targeting firms and higher-income households, are expected to increase tax collection by EUR 3.1 billion cumulated over 2023 and 2024. No new measure to cushion the impact of Russia’s war of aggression against Ukraine was included in the draft budget but the current support measures will be assessed at the end of the year. In the projections, it is assumed that direct aid will not be renewed in 2023 and that tax rebates will be maintained in 2023 and gradually removed in January and July 2024. Under these assumptions, the fiscal stance would be tightened by 1.2% of GDP in 2023 and 0.5% in 2024.

Growth will slow

Growth is expected to slow in 2023 and remain moderate in 2024, mainly due to the depressing effect of inflation on household purchasing power and weaker in foreign demand prospects. The rise in euro area interest rates will weigh on business investment, while public investment is expected to remain dynamic thanks to the support from Next Generation EU funds. Increasing interest rates will also hamper consumption and housing investment, although the impact is expected to be more moderate than in previous periods of rising rates, as the share of floating-rate housing loans has fallen considerably over the last decade, to less than 75%. Under the assumption of a stabilisation in energy import prices, inflation would recede in the course of 2023, but remain high. The main risks surrounding the projection are related to the impact on activity from the EU plans to lower energy consumption and to the evolution of the war in Ukraine, although Spain is likely to be less affected than a majority of the EU countries by gas shortages, as it is less dependent on Russian gas imports. A swifter use of European funds would hasten the recovery.

Measures to cushion inflation should not jeopardise the green transition

An agreement with social partners to share the burden of the rise in import prices will mitigate the risk of a wage-price spiral. Fiscal measures to alleviate this burden must be temporary, targeted towards those most in need, be balanced with the necessary medium-term fiscal consolidation, and maintain incentives for energy savings. The latter will require the introduction of an efficient regulatory framework and adequate incentives to foster private investment in green technologies.

Sweden

Output is projected to decline in the near term, resulting in annual growth of 2.9% this year, -0.6% in 2023 and 1.9% in 2024. High inflation, rising mortgage interest rates and falling asset prices will erode household purchasing power, holding back private consumption. Unemployment will increase and inflation is expected to recede gradually and close in on the 2% inflation target in the latter half of 2024.

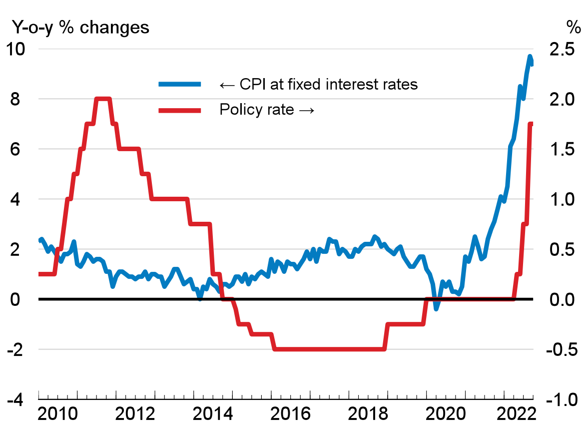
Monetary policy should continue to ensure that inflation expectations are anchored. Fiscal support measures should become more targeted to people vulnerable to rising living costs, while preserving incentives for energy savings. The pandemic has increased long-term unemployment, which has been a persistent policy challenge. Reskilling and upskilling the workforce are key to facilitate a reallocation of labour to expanding sectors. In addition, increasing labour mobility through more affordable housing could also help reallocation. Strengthening electricity transmission capacity is also needed to enhance energy security.

Growth is weakening

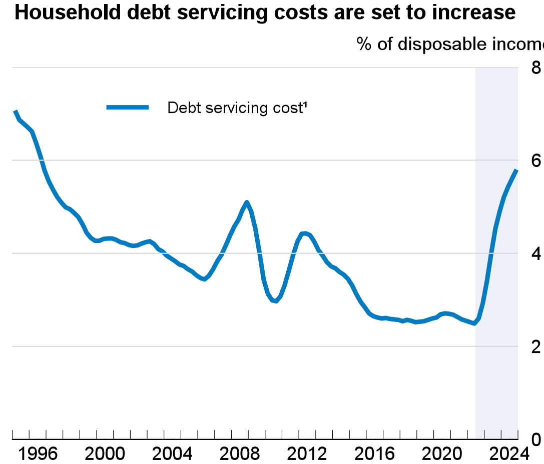
After strong quarterly growth of 0.7% in Q3 2022, the economy is slowing sharply. New export orders have plateaued, and manufacturing confidence has fallen for five successive months. Household confidence fell to a record low in October, partly reflecting negative real wage growth and rising mortgage rates. House prices have fallen sharply, but remain above pre-pandemic levels. The labour market is tight, with the unemployment rate dropping to 6.5% in September. Inflation ticked down to 9.3% in October from a three-decade high in September.

Sweden

The policy rate has been lifted rapidly to tackle inflation



Household debt servicing costs are set to increase



1. The shaded area represents the Riksbank's forecast on household debt servicing costs.
Source: OECD Economic Outlook 112 database; and the Riksbank's Monetary Policy Report, September 2022.

StatLink https://stat.link/f2vi8g

Sweden: Demand, output and prices

Sweden	2019	2020	2021	2022	2023	2024
	Current prices SEK billion	Percentage changes, volume (2021 prices)				
GDP at market prices	5 051.9	-2.3	4.8	2.9	-0.6	1.9
Private consumption	2 267.7	-3.2	5.9	3.7	-1.6	2.4
Government consumption	1 300.5	-2.0	2.5	-0.3	1.9	1.0
Gross fixed capital formation	1 235.4	1.5	6.0	6.1	-1.2	1.7
Final domestic demand	4 803.6	-1.7	5.0	3.3	-0.6	1.9
Stockbuilding[1]	35.4	-0.7	0.4	1.0	-0.2	0.0
Total domestic demand	4 839.1	-2.4	5.4	4.3	-0.8	1.8
Exports of goods and services	2 419.9	-5.8	7.6	4.9	2.1	3.2
Imports of goods and services	2 207.1	-6.3	9.3	8.3	1.9	3.2
Net exports[1]	212.9	0.0	-0.3	-1.2	0.1	0.1
Memorandum items						
GDP deflator	_	2.0	3.0	6.3	6.0	2.3
Consumer price index[2]	_	0.5	2.2	8.3	7.0	2.3
Core inflation index[3]	_	0.5	2.4	7.7	5.1	2.2
Unemployment rate (% of labour force)	_	8.5	8.8	7.5	8.3	8.5
Household saving ratio, net (% of disposable income)	_	17.0	15.5	12.0	12.7	11.3
General government financial balance (% of GDP)	_	-2.8	-0.1	0.9	-0.4	0.4
General government debt, Maastricht definition[4] (% of GDP)	_	39.6	36.4	31.5	29.1	29.5
Current account balance (% of GDP)	_	5.9	5.4	3.2	3.4	3.4

1. Contributions to changes in real GDP, actual amount in the first column.
2. The consumer price index includes mortgage interest costs.
3. Consumer price index with fixed interest rates.
4. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/v63pqe

Even with limited direct trade and financial exposures, Russia's war of aggression against Ukraine is affecting the Swedish economy, mainly through higher energy prices and low growth in important trading partner economies. Electricity prices have soared, particularly in southern areas where they generally depend on trade with other European countries. As of early November, nearly 49 000 Ukrainian refugees (0.5% of the population) had arrived in Sweden, some of them having returned to Ukraine.

Fiscal policy remains supportive

To mitigate soaring energy bills, the tax on diesel and petrol was temporarily reduced from June until October, and the housing allowance targeting economically vulnerable families with children was temporarily increased from July until December. The fiscal stance in 2023 is expected to be broadly neutral. The new government proposes to cut fuel taxes, support electricity bills, increase unemployment benefits, and boost defence spending, costing around 0.6% of GDP. This is to be largely financed by structural savings. High inflation has forced the Riksbank to accelerate interest rate rises. After a 50 basis points rate increase in June, it raised the repo rate by a further 100 basis points in September, the biggest increase since the inflation target came into effect in 1995. The policy rate is expected to reach 3% in the first quarter of next year and to remain at that level through the rest of 2023-24.

The economy will contract in the near term

The economy is projected to contract in the fourth quarter of 2022 and the first half of 2023. After a 2.9% expansion in 2022, output will shrink by 0.6% in 2023 before growing by around 2% in 2024. Investment is expected to decline in the near term, against the backdrop of rising input and financing costs. Inflation will remain high in 2023 as price pressures broaden. Nominal wage growth is set to increase after upcoming wage negotiations. Real wages will nonetheless decline over the projection period and will, together with falling housing prices and higher debt-service burdens, weigh on consumption. Uncertainty remains high. A long period of very low interest rates has boosted household debt, which now amounts to 200% of disposable income. This debt burden could reduce consumption further if mortgage rates rise faster, given the high prevalence of variable-rate mortgages. Highly leveraged commercial real estate developers may also face financial difficulties as interest rates rise, with potential repercussions on the financial system. On the upside, inflation could be brought under control more quickly, aided by restraint in collective bargaining, limiting the need for monetary policy tightening.

Long-term unemployment remains a major challenge

The duration of unemployment spells has increased during the pandemic. This is especially the case among vulnerable groups who face difficulties in getting a job amid Sweden’s compressed wage structure. There have been continuous efforts to address this issue, notably by reinforcing activation policies. In addition, measures to increase labour mobility should be considered, notably for low-income households, including the provision of affordable homes near job opportunities. Easing rent controls for new dwellings would encourage investments in rental housing and contribute to affordable housing in the longer run. The fiscal support measures should shift from generalised energy tax cuts that can lead to overconsumption and disproportionally benefit higher-income households to targeting those most vulnerable to rising living costs. Limited electricity transmission capacity between the North and the South has resulted in large price differentials, showing that investments in the grid are needed to make the most of Sweden’s potential in the renewable energy sector.

Switzerland

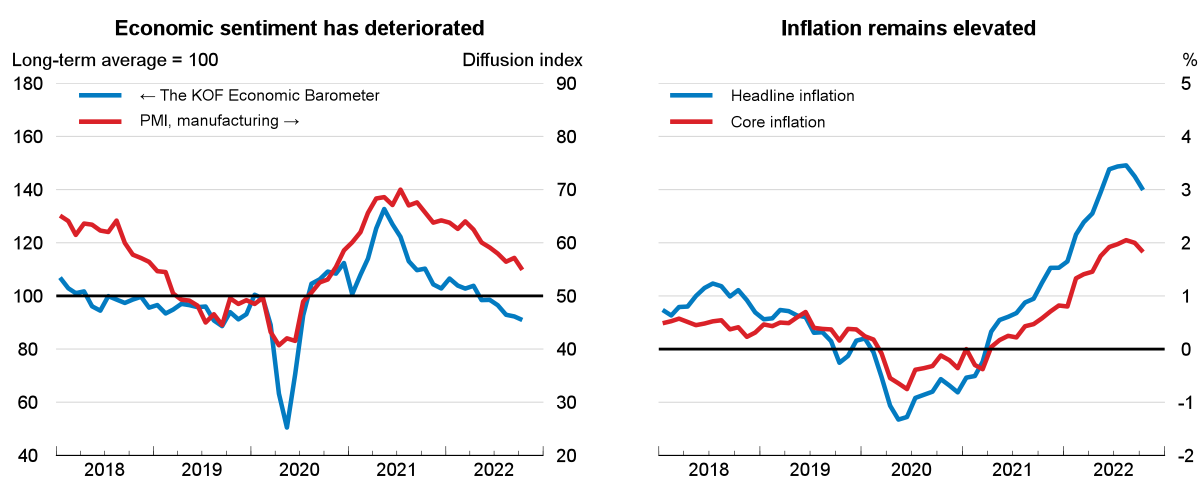
GDP is projected to grow by 0.6% in 2023 and 1.4% in 2024. Repercussions from Russia's war of aggression against Ukraine will further weaken foreign demand and thus slow trade and investment. Low consumer confidence will moderate consumption. Rising electricity prices and wages will keep headline inflation above the Swiss National Bank's target range in 2023, before moderating in 2024. Disruptions to industrial production due to natural gas or electricity shortages and a stronger weakening of global demand are key downside risks to activity.

Monetary policy will need to be tightened further to contain core inflation and to ensure that long-term inflation expectations remain anchored. Fiscal consolidation should proceed as planned, but targeted measures to assist vulnerable refugees are warranted. Structural reforms are needed to boost labour market integration, remove barriers to competition, and raise energy efficiency to help ensure energy security and improve environmental sustainability.

Growth momentum has weakened

Economic growth has slowed. Real GDP rose by 0.3% in the second quarter of 2022, primarily driven by the recovery in services as remaining COVID-19 restrictions were lifted. Consumer confidence is at a record low amid heightened uncertainty surrounding the war, rising energy prices and elevated inflation. The KOF Economic Barometer remains subdued and the manufacturing PMI has declined. The labour market remains very tight, with low unemployment and a high number of vacancies. Headline inflation was 3.0% in October 2022, the highest rate since 2008, driven primarily by prices of energy and imported goods, while core inflation moderated to 1.8%. Medium-term inflation expectations remain below 2%, within the target-range of the Swiss National Bank.

Switzerland



Source: KOF Swiss Economic Institute; Swiss Association for Material Management and Purchasing; and Federal Statistical Office.

StatLink https://stat.link/qo0crb

Switzerland: Demand, output and prices

Switzerland	2019	2020	2021	2022	2023	2024
	Current prices CHF billion	Percentage changes, volume (2015 prices)				
GDP at market prices	717.3	-2.5	4.2	2.1	0.6	1.4
Private consumption	375.6	-4.2	1.7	3.7	0.7	0.8
Government consumption	81.4	3.5	3.5	0.9	-0.2	0.8
Gross fixed capital formation	190.8	-3.1	4.1	0.1	0.6	1.5
Final domestic demand	647.8	-2.9	2.7	2.3	0.5	1.0
Stockbuilding[1]	- 2.2	2.1	-3.2	1.0	0.9	0.0
Total domestic demand	645.6	-0.6	-0.8	3.4	1.5	1.0
Exports of goods and services	481.0	-5.5	12.2	0.4	0.7	3.2
Imports of goods and services	409.3	-3.0	4.9	2.1	2.0	2.9
Net exports[1]	71.7	-2.0	5.0	-0.9	-0.7	0.5
Memorandum items						
GDP deflator	_	-0.8	1.1	3.0	2.2	1.5
Consumer price index	_	-0.7	0.6	2.9	2.5	1.5
Core inflation index[2]	_	-0.3	0.3	1.7	1.6	1.5
Unemployment rate (% of labour force)	_	4.8	5.1	4.4	4.6	4.5
Household saving ratio, net (% of disposable income)	_	23.1	24.1	21.9	21.2	20.8
General government financial balance (% of GDP)	_	-3.1	-0.5	-0.1	0.1	0.3
General government gross debt (% of GDP)	_	43.8	41.2	42.3	42.7	43.0
Current account balance (% of GDP)	_	1.6	7.4	6.5	5.8	6.3

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/kig9om

Natural gas makes up 15% of Swiss energy consumption and about half was imported from Russia prior to the war. Although energy prices have risen sharply because of Russia's invasion of Ukraine, Swiss households are less affected than other Europeans insofar as energy accounts for a smaller share of their consumption expenditures. The government has not yet announced any support packages for households or firms to offset high energy prices, but steps have been taken to reduce natural gas use during the upcoming winter. In the event of shortages, companies equipped with dual-fuel installations may be ordered to switch away from natural gas to oil. The use of gas for specific purposes would be restricted (room temperatures could for example be capped) or prohibited. All installations that are not considered "protected consumers" (households, essential social services, district and heating facilities serving households) would be subject to a quota in case of severe shortages. Plans are also being prepared to reduce electricity use in the event of shortages.

Tighter monetary policy is needed to lower inflation

The Swiss National Bank has raised interest rates by a cumulative 125 basis points since June 2022, to 0.5% in September 2022, after seven years of negative interest rates. The authorities remain willing to intervene in the foreign exchange rate market to ensure that the value of the Swiss franc is consistent with appropriate monetary conditions. As inflationary pressures are building up and global interest rates are rising, policy interest rates are assumed to increase to 2.0% by the second quarter of 2023 and to remain at that level throughout the projection period. The federal government has continued to scale back COVID-19-related fiscal support as the economic situation has improved. A fiscal surplus is expected in 2023, with further budgetary consolidation in 2024.

Growth will remain low and inflation will gradually recede

Real GDP growth is projected to moderate to 0.6% in 2023 and 1.4% in 2024. This mainly reflects the negative impact on global growth from Russia's war in Ukraine, hampering exports and slowing domestic demand. A progressive reduction of the high saving rate is projected to support private consumption over the next two years. Pressures from the tight labour market and high energy prices will keep headline inflation above the central bank's target range in 2023, before it gradually falls to 1.5% in 2024. However, the rationing of natural gas in the event of severe supply disruptions would adversely affect industrial production. Additional disruptions in global supply chains could also further weaken economic activity and raise inflation. Moreover, close monitoring of financial risks related to the real estate market and rising interest rates is warranted.

Ensuring inclusive growth and accelerating the green transition

Fiscal policy should continue to provide support to the roughly 68 000 Ukrainian refugees (0.8% of the population) that have arrived in Switzerland since the onset of the war. The planned fiscal consolidation should progress. Simplifying and speeding-up the process for recognition of foreign qualifications and increased access to training programmes will raise participation in the labour market. Boosting labour market integration of under-represented groups and removing barriers to entry would help sustain the recovery and improve inclusiveness. Further investment in renewable energy and infrastructure for electric vehicle mobility would reduce reliance on the gas and oil markets and enhance energy security.

Türkiye

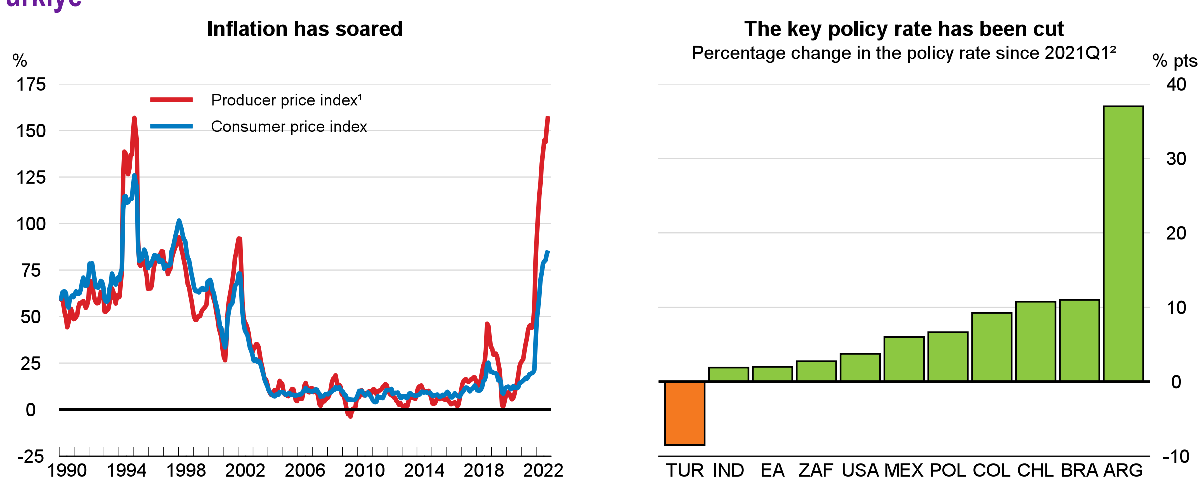
GDP growth will moderate from 5.3% in 2022 to around 3% over the projection period. Inflation will decline but remain above 40%. This will dent household purchasing power while heightened uncertainty will hold back investment. Export growth will slow as external demand weakens. The unemployment rate is projected to stay above 10% in 2023. Large external financing needs and low reserve buffers leave the economy highly vulnerable to shocks.

The central bank should raise its policy rate and provide credible forward guidance for a realistic convergence path to the official inflation target to shore up confidence and re-anchor inflation expectations. Measures to shield households from rising energy prices are welcome but should be temporary and targeted to keep fiscal costs manageable. Reducing employment costs and promoting more flexible work contracts would boost job creation in the formal sector.

Growth has been strong, but vulnerabilities are rising

Real GDP grew by 7.5% in the first half of 2022 (year-on-year), one of the fastest growth rates in the OECD. Buoyant private consumption has been driven by favourable labour market developments as labour force participation returned to pre-pandemic levels. Exporters have been able to exploit opportunities from disruptions of Asian supply chains, and tourism has fully recovered in 2022. However, investment activity has been subdued and macroeconomic imbalances have risen. The current account deficit has widened due to increased energy imports, and consumer price inflation reached 85.5% and producer price inflation 158% by October 2022. The minimum wage was raised by 30% in July, six months after a 50% increase. Lira depreciation has raised import price pressures. Monthly domestic indicators such as electricity production suggest that economic activity is decelerating.

Türkiye



1. Producer price index refers to domestic industrial activities.
2. The last data point refers to 14 November 2022.
Source: OECD Main Economic Indicators database; BIS; and CBRT.

StatLink https://stat.link/3kdjyh

Türkiye: Demand, output and prices

Türkiye	2019	2020	2021	2022	2023	2024
	Current prices TRY billion	Percentage changes, volume (2009 prices)				
GDP at market prices	4 311.7	1.8	11.4	5.3	3.0	3.4
Private consumption	2 456.3	3.0	15.7	15.2	4.1	3.4
Government consumption	665.5	2.2	2.7	0.2	3.0	2.3
Gross fixed capital formation	1 117.1	7.3	7.4	2.8	2.8	3.8
Final domestic demand	4 238.8	4.0	11.3	9.5	3.6	3.4
Stockbuilding[1]	- 29.1	4.0	-6.2	-6.4	-0.3	0.0
Total domestic demand	4 209.7	8.6	4.1	2.2	3.1	3.3
Exports of goods and services	1 402.5	-14.6	24.9	12.2	4.4	4.2
Imports of goods and services	1 300.5	7.1	2.4	4.2	4.8	3.6
Net exports[1]	102.0	-6.9	6.4	2.8	-0.3	0.1
Memorandum items						
GDP deflator	_	15.0	29.0	91.7	51.1	46.1
Potential GDP, volume	_	3.8	4.0	3.8	3.7	3.6
Consumer price index[2]	_	12.3	19.6	73.2	44.6	42.1
Core inflation index[3]	_	11.2	18.3	58.6	45.6	42.1
Unemployment rate (% of labour force)	_	13.1	12.0	10.7	10.3	10.0
Current account balance (% of GDP)	_	-5.0	-1.7	-5.6	-3.8	-2.5

1. Contributions to changes in real GDP, actual amount in the first column.
2. Based on yearly averages.
3. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/yeign2

The government has introduced measures to shield vulnerable groups from rising energy and food prices. Households in the lowest decile of the income distribution spend nearly 70% of their budget on food and housing. The number of households receiving energy assistance has doubled to 4 million and electricity tariffs for low-consumption households have been cut. Non-targeted price support measures, such as tax cuts on energy and the abolition of some electricity fees, have also been introduced and will continue throughout the projection period. Türkiye imports 99% of its gas and 93% of its oil, leaving the economy exposed to energy supply disruptions and price volatility.

Financial conditions and fiscal policy remain supportive

Despite high inflation, the central bank has reduced its base rate by 8.5 percentage points since September 2021 to the current level of 10.5%, with Türkiye the only OECD country to have lower policy interest rates during this period. The policy rate is expected to remain at the current level over the projection period. At the same time, the authorities have tightened macroprudential and collateral requirements. Since April, the reserve requirement ratio has increased from 10% to 30%. Consequently, lending rates have increased, although they vary considerably as collateral requirements differ according to the type of loans. For example, commercial loan rates are around 18% and even lower for exporting companies, while consumption loan rates are above 30%. Despite these measures, lending rates for all types of loans remain negative in real terms. Fiscal policy will remain supportive over the projection period with support measures for energy consumers and ambitious state-subsidised social housing projects.

Economic growth will moderate

Economic growth is projected to slow to around 3% per annum on average in 2023-24. Weak external demand and persistent geopolitical uncertainties will weigh on investment and limit export growth. At the same time, household consumption will slow considerably as persistently high inflation will dent household purchasing power. Inflation is projected to decline, in part due to base effects, but remain above 40% over the projection period, reflecting a gradual pass-through of the recent lira depreciation and wage increases to consumer prices.

Risks are high and tilted to the downside. The adverse effects of Russia's war of aggression against Ukraine on prices and economic activity could rise. A complete cessation of energy exports from Russia to Europe could significantly affect Türkiye's main trading partners and thus weigh on exports. Commodity prices could be higher than projected, adding pressures on inflation as Türkiye is heavily dependent on imported oil and gas. Further significant minimum wage increases could also trigger additional wage and price pressures. A negative confidence shock due to widening macroeconomic imbalances could trigger a disorderly adjustment process involving stronger currency depreciation and spiralling inflation.

Strengthening the macroeconomic policy framework and introducing structural reforms would increase economic resilience

The central bank should raise its policy rate and provide forward guidance stressing its intent to achieve the official inflation target of 5% to shore up confidence and re-anchor inflation expectations. The government should continue to protect households from rising living costs, but this support should be temporary and targeted on the most vulnerable to contain fiscal costs, and be designed to maintain price signals. To create more and better jobs and improve productivity, rigid labour regulations should be eased, and the role of active labour market policies should increase. Given its heavy dependence on oil and gas imports, Türkiye should continue to improve energy efficiency and diversify its supply sources.

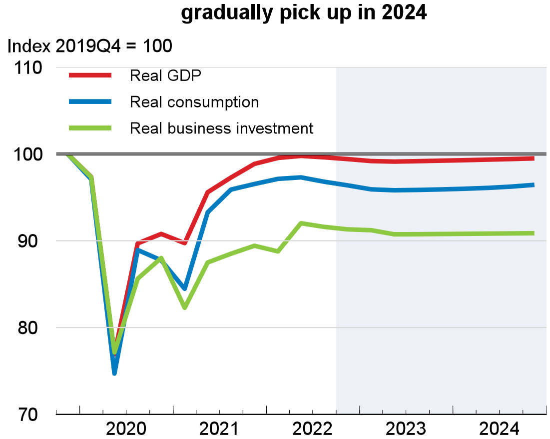
United Kingdom

Following a contraction of 0.4% in 2023, GDP is projected to increase by 0.2% in 2024. Consumer price inflation will peak at around 10% in late 2022 due to high energy prices and continuing labour and goods supply shortages, before gradually declining to 2.7% by the end of 2024. Private consumption is expected to slow owing to rising living costs, but will be aided by a 9.7% increase in the minimum wage and the usual uprating of welfare benefits and pensions in April 2023. Public investment is set to rebound in 2023 and 2024 as supply bottlenecks ease, in line with government plans. The unemployment rate is expected to rise to 5% by the end of 2024.

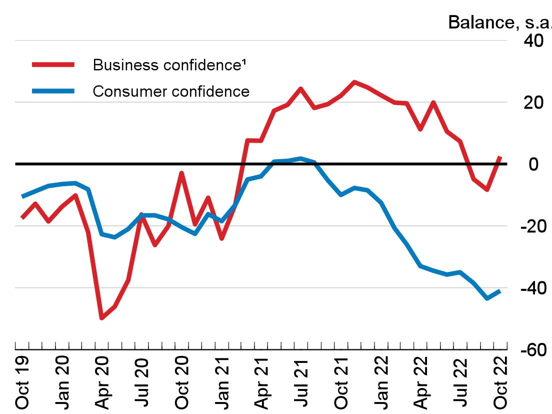
Complying with the fiscal plan and ensuring that future changes to fiscal targets follow a transparent and clearly defined process would maintain fiscal policy credibility and mitigate concerns about debt sustainability. The untargeted Energy Price Guarantee announced in September 2022 by the government will increase pressure on already high inflation in the short term, requiring monetary policy to tighten more and raising debt service costs. Better targeting of measures to cushion the impact of high energy prices would lower the budgetary cost, better-preserve incentives to save energy, and reduce the pressure on demand at a time of high inflation.

United Kingdom 1

After contracting, GDP growth will gradually pick up in 2024



Consumer confidence remains subdued



1. Business confidence in the manufacturing sector.
Source: OECD Economic Outlook 112 database; and OECD Main Indicators database.

StatLink https://stat.link/cnz35u

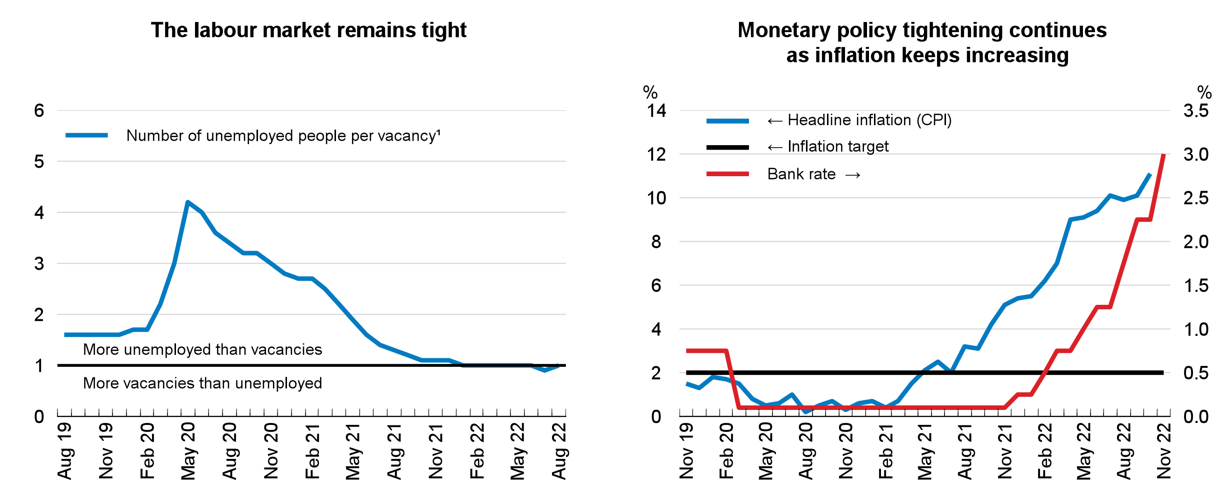
United Kingdom: Demand, output and prices

United Kingdom	2019	2020	2021	2022	2023	2024
	Current prices GBP billion	Percentage changes, volume (2019 prices)				
GDP at market prices	2 238.3	-11.0	7.5	4.4	-0.4	0.2
Private consumption	1 440.0	-13.2	6.2	4.7	-1.1	0.3
Government consumption	425.6	-7.3	12.6	1.6	2.3	0.6
Gross fixed capital formation	403.4	-10.5	5.6	5.6	1.0	1.3
Final domestic demand	2 269.0	-11.6	7.5	4.2	0.0	0.6
Stockbuilding[1]	5.5	-0.7	1.2	1.0	-2.2	0.0
Total domestic demand	2 274.5	-12.3	8.6	5.2	-2.1	0.6
Exports of goods and services	699.7	-12.1	-0.3	9.7	5.5	1.6
Imports of goods and services	735.8	-16.0	2.8	12.4	-0.5	2.5
Net exports[1]	- 36.1	1.5	-0.9	-0.9	1.9	-0.4
Memorandum items						
GDP deflator	_	5.9	0.4	4.8	4.7	2.5
Harmonised index of consumer prices	_	0.9	2.6	8.9	6.6	3.3
Harmonised index of core inflation[2]	_	1.4	2.4	6.2	6.4	3.4
Unemployment rate (% of labour force)	_	4.6	4.5	3.7	4.3	4.8
Household saving ratio, gross (% of disposable income)	_	15.8	12.5	7.9	7.6	7.5
General government financial balance (% of GDP)	_	-13.1	-8.2	-6.2	-7.6	-6.8
General government gross debt (% of GDP)	_	152.0	145.6	142.6	145.9	149.9
Current account balance (% of GDP)	_	-3.2	-2.0	-4.8	-3.5	-3.5

1. Contributions to changes in real GDP, actual amount in the first column.
2. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/vzhcex

United Kingdom 2



1. UK vacancies excluding agriculture, forestry and fishing.
Source: ONS; OECD Economic Outlook 112 database; and Bank of England.

StatLink https://stat.link/yeopb9

Rising living costs weigh on economic growth

GDP growth has slowed and high-frequency indicators point towards a further deterioration in the outlook. Following growth of 0.7% in the first quarter of 2022 and 0.2% in the second, real GDP fell by 0.2% in the third quarter, as price growth outpaced wage growth, resulting in deteriorating household incomes. Annual CPI inflation reached 11.1% in October on the back of high energy prices and rising food prices and rising underlying inflation. Growth in average total pay picked up to 6% in the three months to September 2022, amidst labour market tightness, but real wages were down by 2.6%. In the third quarter, the unemployment rate of 3.6% fell below pre-pandemic levels, partially due to higher economic inactivity among 50 to 64 year-olds than before the pandemic. The number of vacancies remains high. Business sentiment picked up in October, following a period of deterioration driven by policy uncertainty and a worsening global outlook. Consumer confidence remained subdued after having fallen for several consecutive months amidst rapidly rising living costs.

The UK economy has limited direct trade linkages with Russia and Ukraine but is vulnerable to developments in the global energy market. Although Britain is not reliant on Russian exports, it imports gas and electricity from the continent during the coldest months. A particularly cold winter could risk supply disruptions, exposing the economy to rolling power cuts.

Monetary policy is set to tighten further but fiscal support is sizeable

The Bank of England has responded to rising inflation with monetary tightening, raising the policy rate from 0.1% in December 2021 to 3% by November 2022. It has also continued with quantitative tightening by no longer reinvesting the proceeds of gilt redemptions in new gilt purchases and gradually reducing its holdings of sterling corporate bonds until the end of 2023. From November 2022, the Bank of England started to sell government bonds to gradually reduce the GBP 838 billion stock that was built up since the global financial crisis. Monetary policy tightening is expected to continue, with the bank rate reaching 4.5% by Q2 2023 and remaining at that level throughout the projection period.

The government has introduced several support measures to help households and businesses to cope with rising energy prices. To protect households and businesses from high energy prices, the government introduced the Energy Price Guarantee and the Energy Bill Relief Scheme, which both are effective from October 2022 until end-March 2023. Households will benefit from the Energy Price Guarantee, which caps the cost per unit, with the government covering the difference to the market price. This new scheme, expected to cost about GBP 25 billion, will reduce the annual cost of electricity and gas for an average household with typical energy expenditure to around GBP 2 500 a year. On average usage, a household will save GBP 1 000 a year. Over the same period, gas and electricity prices will also be capped for businesses, charities and the public sector under the Energy Bill Relief Scheme, estimated to cost GBP 18 billion. This six-month long support for households and businesses together is estimated to cost about GBP 43 billion (1.9% of 2022 GDP). The government announced that for the fiscal year 2023/24, the cap of the Energy Price Guarantee will be raised to GBP 3 000 per year for the energy consumption of a typical household (worth about GBP 13 billion) and that the most vulnerable households will be aided with additional support to mitigate the rising cost of living. These measures for households and businesses come on top of support packages announced earlier in the year (worth GBP 37 billion) to help households, including a GBP 11.7 billion Energy Bills Support Scheme worth up to GBP 400 each for around 28 million households, as well as a GBP 150 disability cost-of-living payment and a GBP 650 cost-of-living payment for households on means-tested benefits. Moreover, the government reversed the 1.25 percentage points increase in national insurance contributions previously planned to take effect from November 2022. While most of the support package is debt financed, from April 2023, an increase in the corporate income tax rate from 19% to 25% and a decrease of the income threshold for taxation at the additional rate of 45% for higher earners from GBP 150 000 to GBP 125 140 will support the public finances. In 2023, the fiscal stance is expected to be slightly expansionary before tightening by 1.5 percentage points of potential GDP in 2024.

Economic activity will slow

Following a 4.4% expansion in 2022, GDP is projected to contract by 0.4% in 2023, and rise by just 0.2% in 2024. Inflation will remain above 9% into early 2023 before slowly falling to 4.5% by the end of 2023 and to 2.7% by the end of 2024. Reduced purchasing power and tighter monetary policy are expected to take a toll on consumer spending and rising long-term interest rates will lead to a slowdown in the housing market. Business investment will remain subdued over the projection period due to a higher cost of capital and lingering uncertainty. Continued tightness of the labour market is expected to push up wages, but wage growth is expected to remain below inflation over the projection period. Unemployment is set to gradually increase to 5% by the end of 2024 due to weaker demand. Public investment is expected to pick up from 2023 with planned spending increases on infrastructure and climate-related investment. The general government deficit is projected to decline from 7.6% of GDP in 2023 to 6.8% of GDP in 2024.

Risks to the outlook are considerable and tilted towards the downside. Higher-than-expected goods and energy prices could weigh on consumption and further depress growth. A prolonged period of acute labour shortages could force firms into a more permanent reduction in their operating capacity or push up wage inflation further. While households may seek to boost their real income by striking for stronger wage increases, they may also increase their labour supply either by returning from inactivity or by increasing working hours, which would be an upside risk. Further progress in trade deals could also support growth.

Raising productivity will be key to sustained growth

Fiscal support measures to help with high energy prices are warranted, but should ensure that incentives for energy reduction remain intact. Accelerating progress towards net zero is fundamental to enhance energy security and reduce dependence on fossil fuels. The policies in place are not yet sufficient to deliver the net zero target. The government can stimulate investment by being clearer about its approach to the transition to a net zero economy and developing an economy-wide plan with specific deadlines, policies and priorities, in line with a target-consistent emission pricing trajectory. To ensure sustainable growth, the government should also continue to implement its productivity enhancing “Plan for Growth” to support a shift towards greener and more inclusive growth through large-scale public investment in infrastructure, skills and innovation.

United States

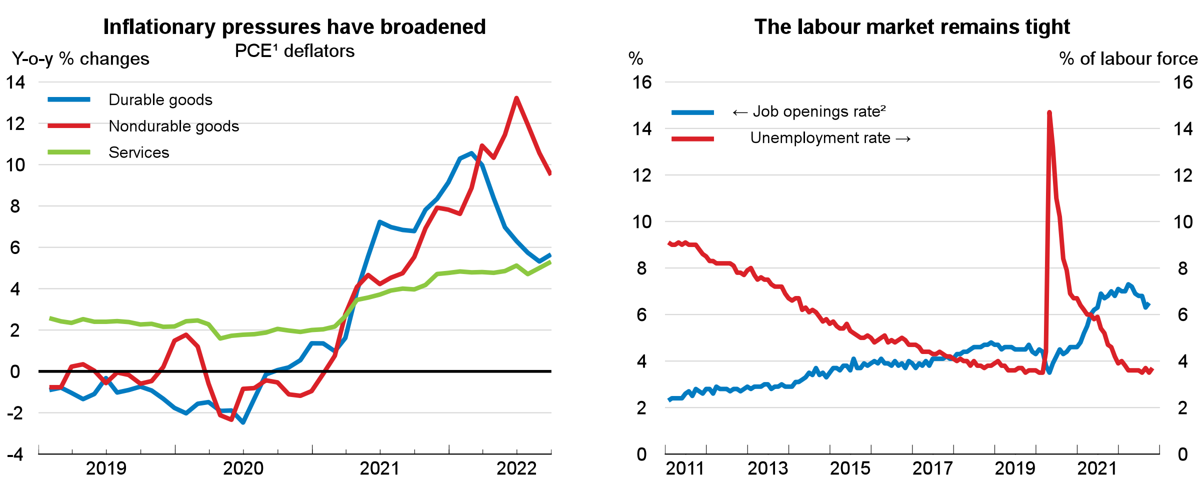
Real GDP is projected to grow by 1.8% in 2022, 0.5% in 2023 and 1.0% in 2024. High inflation and tighter financial conditions will further crimp spending plans across the economy. With the notable slowing in domestic production, labour demand and wage growth will weaken. Price pressures will recede as energy prices stabilise and demand slows, but core inflation is not projected to return to the vicinity of the Federal Reserve target until late 2024.

The continued tightening of monetary policy will provide a headwind to near-term growth. Government spending has now returned to more normal levels with the unwinding of pandemic support, though some states have introduced new measures in response to rising energy prices. Further reducing dependence on fossil fuels continues to be a priority given global energy shortages and the aim to reach net zero emissions by 2050. Nonetheless, climate change policies will have different effects across regions, industries and households that should be reflected explicitly in the national climate strategy.

Economic activity is slowing but inflationary pressures persist

Economic growth is slowing. Personal consumption expenditures have continued to increase, but at a more modest pace since the start of 2022. Investment has weakened, especially in the housing market. Accordingly, labour demand growth has moderated, although some sectors continue to experience labour shortages. Nominal wages have risen, leading to stronger growth in unit labour costs. This has contributed to broadening inflationary pressures. While goods price inflation remains high, services inflation has also gradually picked up. Real wages have declined.

United States 1



1. Personal Consumption Expenditures price index.
2. The job openings rate is the number of job openings on the last business day of the month as a per cent of total employment plus job openings.
Source: U.S. Bureau of Economic Analysis; and U.S. Bureau of Labor Statistics.

StatLink https://stat.link/uzxko5

United States: Demand, output and prices

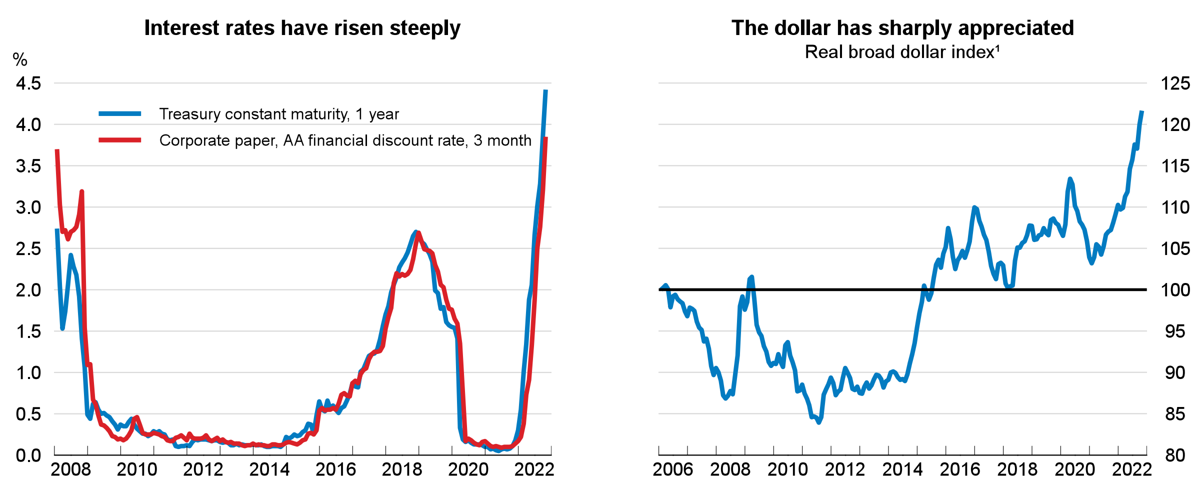
United States	2019	2020	2021	2022	2023	2024
	Current prices USD billion	Percentage changes, volume (2012 prices)				
GDP at market prices	21 381.0	-2.8	5.9	1.8	0.5	1.0
Private consumption	14 392.7	-3.0	8.3	2.6	0.6	1.0
Government consumption	3 008.8	2.2	1.3	-0.4	0.6	0.5
Gross fixed capital formation	4 485.5	-1.2	5.7	-0.5	0.0	1.7
Final domestic demand	21 887.0	-1.9	6.7	1.5	0.5	1.1
Stockbuilding[1]	72.8	-0.6	0.2	0.7	-0.2	0.0
Total domestic demand	21 959.8	-2.4	7.0	2.2	0.3	1.1
Exports of goods and services	2 538.5	-13.2	6.1	7.4	4.2	3.3
Imports of goods and services	3 117.2	-9.0	14.1	8.7	1.1	2.7
Net exports[1]	- 578.8	-0.3	-1.2	-0.5	0.3	0.0
Memorandum items						
GDP deflator	_	1.3	4.5	6.9	3.5	2.5
Personal consumption expenditures deflator	_	1.1	4.0	6.2	3.5	2.6
Core personal consumption expenditures deflator[2]	_	1.3	3.5	5.0	3.6	2.6
Unemployment rate (% of labour force)	_	8.1	5.4	3.7	4.2	4.7
Household saving ratio, net (% of disposable income)	_	17.5	12.4	4.1	4.2	4.4
General government financial balance (% of GDP)	_	-14.9	-12.1	-4.1	-3.7	-3.7
General government gross debt (% of GDP)	_	133.3	126.2	121.9	121.9	122.3
Current account balance (% of GDP)	_	-2.9	-3.6	-3.8	-3.5	-3.6

1. Contributions to changes in real GDP, actual amount in the first column.
2. Deflator for private consumption excluding food and energy.
Source: OECD Economic Outlook 112 database.

StatLink https://stat.link/c8ae3l

The direct economic impact from Russia's war of aggression against Ukraine has been more limited than in many other OECD countries. The United States is a net exporter of energy and some other commodities that have experienced trade disruptions due to the war. US exports of natural gas and wheat have risen in response to shortages on global markets. Nonetheless, largely as a result of the war, domestic food and gasoline prices remain elevated compared with the pre-pandemic period.

United States 2



1. Higher levels indicate U.S. dollar appreciation.
Source: U.S. Federal Reserve System.

StatLink https://stat.link/jtonbi

Macroeconomic policy is becoming more restrictive

The Federal Open Market Committee is now rapidly tightening monetary policy in response to the surge in inflation. The Federal Funds Rate has been lifted by 3¾ percentage points since March 2022 and central bank holdings of Treasury securities, agency debt and agency mortgage-backed securities are being reduced. Market interest rates have risen sharply at all maturities, reflecting both actual policy decisions and the expectation of further monetary policy tightening ahead. The rapid tightening of monetary policy has contributed to a sharp appreciation in the exchange rate, providing a headwind to export activity. The disinflationary impact of the appreciation is more limited, however, as the bulk of US imports is invoiced in US dollars.

Government support introduced during the pandemic has now been largely unwound, but some transfers from Federal to state and local governments are yet to be fully spent and some households still hold accumulated savings from the fiscal programmes. Some state governments have also suspended state gas taxes in response to rising gas prices. The ongoing implementation of the Infrastructure Investment and Jobs Act will push public investment slightly higher in the coming years. The overall impact on aggregate demand of the various Inflation Reduction Act provisions will be limited in the period to 2024, with expenditure on a range of climate and energy initiatives and extensions to health care subsidies estimated to be largely offset by the introduction of a minimum corporate tax. Overall, fiscal policy is assumed to tighten in 2023 and 2024 as both pandemic-related and energy-related fiscal supports fully expire.

Economic growth will ease further

Real GDP is projected to grow by 1.8% in 2022, 0.5% in 2023 and 1.0% in 2024. Rising inflation has eroded household purchasing power and the OECD projections assume that the Federal Funds Rate will be further increased to a peak of 5-5¼ per cent in early 2023. Private investment, especially in housing, is expected to moderate further in response to weaker demand and higher interest rates. With the slowing in domestic production, pressure in the labour market will begin to abate; vacancies are expected to decline further and the unemployment rate is projected to rise to 4.7% in 2024. Wage growth will moderate in response. The further reorientation of domestic demand back toward the services sector should help attenuate supply shortages. Price pressures are expected to recede, but core inflation is not projected to return to around the Federal Reserve 2% target until late 2024.

Risks to the growth projections are tilted to the downside. Inflationary pressures may prove more persistent than anticipated, prompting stronger tightening of monetary policy. This could particularly impact heavily indebted firms. Further disturbances to global markets in response to Russia's war against Ukraine could also have substantial negative impacts. On the upside, recent easing in supply chain bottlenecks and commodity prices could contribute to a faster moderation in inflationary pressures than is currently projected.

The climate transition remains a top priority

Reforms that further reduce dependence on fossil fuels will be key against the backdrop of global energy shortages and the administration's commitment to reach net zero greenhouse gas emissions by 2050. Recent measures announced as part of the Inflation Reduction Act are an important step. Nonetheless, further regulatory changes, green investment, structural reforms and carbon pricing will be required over the years ahead. Climate policies will have different effects across regions, industries and households. The national climate strategy should explicitly take the distributional effects of different climate change policies into account. Those regions most heavily reliant on fossil fuel production for employment and output will require a combination of place-based policies and reduced barriers to geographical and labour mobility of those affected by employment losses. Any displaced workers would also benefit from further modernisation of state-based unemployment insurance systems. Many states continue to experience significant delays in processing unemployment claims and have outdated software systems that limit the design of support measures. As part of the modernisation process, such systems should be well integrated with job search assistance and training programmes.

OECD Economic Outlook

The global economy is facing mounting challenges amidst the largest energy market shock since the 1970s and the cost-of-living crisis for many households from rising inflation pressures. The *OECD Economic Outlook, Volume 2022 Issue 2* highlights the unusually imbalanced and fragile outlook, the significant downside risks associated with energy market developments and rising financial vulnerabilities as interest rates are raised, and the associated policy challenges. Well-designed and timely policy actions are required to maintain economic stability, enhance energy security and strengthen the prospects for future growth.

This issue includes a general assessment of the macroeconomic situation, and a chapter summarising developments and providing projections for each individual country. Coverage is provided for all OECD members as well as for selected partner economies.

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