



# OECD Economic Outlook

November 2023





# OECD ECONOMIC OUTLOOK

114

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NOVEMBER 2023

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**Please cite this publication as:**

OECD (2023), *OECD Economic Outlook, Volume 2023 Issue 2*, No. 114, OECD Publishing, Paris,  
<https://doi.org/10.1787/7a5f73ce-en>.

ISBN 978-92-64-92344-7 (print)  
ISBN 978-92-64-65116-6 (pdf)  
ISBN 978-92-64-66655-9 (HTML)  
ISBN 978-92-64-49806-8 (epub)

OECD Economic Outlook  
ISSN 0474-5574 (print)  
ISSN 1609-7408 (online)

**Photo credits:** Cover © Gorodenkoff/Shutterstock.com.

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## Acknowledgements

This edition of the OECD Economic Outlook was prepared by the Economics Department under the general supervision of Clare Lombardelli, Luiz De Mello, Álvaro Pereira, Isabell Koske and Alain de Serres, and managed by Nigel Pain and Douglas Sutherland.

Chapter 1 was prepared in the Macroeconomic Policy Division and supervised by Nigel Pain, with Geoff Barnard, Catherine MacLeod and Álvaro Pina as principal authors; and Martin Borowiecki, Yvan Guillemette, Patrice Ollivaud, Nobukazu Ono, Lucia Quaglietti and Elena Rusticelli, providing substantive contributions.

Chapter 2 was prepared by the Country Studies Branch, with contributions from Müge Adalet McGowan, Hansjörg Blöchliger, Jesse Bricker, Tim Bulman, Gabriele Ciminelli, Ben Conigrave, Charles Dennerly, Federica De Pace, Abdenbi El Ansary, Falilou Fall, Priscilla Fialho, Erik Frohm, Paula Garda, Federico Giovannelli, Daniela Glocker, Andrea Goldstein, Nicolas Gonne, Antoine Goujard, Robert Grundke, David Haugh, Philip Hemmings, Jens-Christian Høj, Hyunjeong Hwang, Yosuke Jin, Nikki Kergozou, Caroline Klein, Viktoriia Klimchuk, Michael Koelle, Vassiliki Koutsogeorgopoulou, Kyongjun Kwak, Timo Leidecker, Gabriel Machlica, Alessandro Maravalle, Margit Molnar, Ken Nibayashi, Kei Oguro, Alberto González Pandiella, Jon Pareliussen, Pierre-Alain Pionnier, Bertrand Pluyaud, Claudia Ramirez Bulos, Adolfo Rodriguez-Vargas, Oliver Röhn, Cyrille Schwellnus, Patrizio Sicari, Urban Sila, Zuzana Smidova, Donal Smith, Jonathan Smith, Jan Strasky, Enes Sunel, Kosuke Suzuki, Srdan Tatomir, Ania Thiemann, Sébastien Turban, Elena Vidal, Ben Westmore, Yoonyoung Yang, Tetsuya Yoshioka, and Paul Yu. The preparation of the country notes was supervised by Jens Arnold, Sebastian Barnes, Aida Caldera Sanchez, Mame Fatou Diagne, Philip Hemmings, and Vincent Koen.

Overall coordination and key editorial and statistical support provided by Isabelle Fakih and Jérôme Brézillon.

Statistical support was given by Damien Azzopardi, Corinne Chanteloup, Ane Kathrine Christensen, Lutécia Daniel, Véronique Gindrey, Federico Giovannelli, Béatrice Guérard, Mauricio Hitschfeld, Tony Huang, Eun Jung Kim, Seung-Hee Koh, Anne Legendre, Natia Mosiashvili, Axel Purwin and Mafalda Trincão. Editorial support for the country notes was provided by Jean-Rémi Bertrand, Emily Derry, Karimatou Diallo, Laura Fortin, Robin Houngh Lee, Elodie Lormel and Michelle Ortiz.

Background analysis and key database management was provided by the Macroeconomic Analysis Division, with contributions from Yvan Guillemette and Jeroen Meyer, under the supervision of David Turner.

An initial draft of the report was discussed by the OECD Economic Policy Committee. This report is published under the responsibility of the Secretary-General of the OECD.



# Editorial

## Restoring growth

Inflation is easing, but growth is slowing. The tightening of monetary policy needed to tackle inflation is taking effect. Despite stronger-than-expected GDP growth in 2023, tightening financial conditions, weak trade and subdued confidence are taking a toll. Housing markets and bank-dependent economies, particularly in Europe, are feeling the impact.

The pace of growth is uneven. Emerging markets are generally faring better than advanced economies. Europe's growth lags behind North America and major Asian economies. Inflation, while easing, remains a concern.

We are projecting a soft landing for advanced economies, but this is far from guaranteed. The relationship between inflation, activity and labour markets has changed, making the full impact of monetary policy tightening hard to judge. In the United States, the economy is demonstrating more strength than expected, and there is a risk that inflation proves to be persistent. In the euro area, the full impact of tighter monetary policy is still to appear and activity may be hit more strongly than we expect.

Many emerging markets have shown considerable resilience over the past year, but countries characterised by structural debt vulnerabilities have come under market scrutiny.

Global trade is weak. Not only cyclical, but also structural factors are causing a slowdown in the rate at which value chains are integrating across countries. Opportunities for growth, particularly from greater services trade, are being missed. We must revive global trade. Resilience in global value chains is best delivered by diversification, not by protectionism and inward-looking policies.

In many countries, fiscal pressures are mounting. Demographic changes, decarbonisation, and a combination of rising interest payments and slow growth mean countries face a challenging fiscal outlook. Governments need to take bold action to reduce such pressures and give a greater focus to growth in their policy making. That means reforming labour market and pensions policies, increasing competition, and using fiscal levers to increase human capital and productivity enhancing investment, including the investment needed to deliver the green transition.

In summary, the global economy is grappling with inflation, slowing growth, and mounting fiscal pressures. Policymakers must prioritise macroeconomic stability, structural reforms, smart fiscal policies and international cooperation to foster sustainable and inclusive growth.

29 November 2023



Clare Lombardelli  
OECD Chief Economist



# 1 General Assessment of the macroeconomic situation

## Introduction

The global economy continues to confront the challenges of persistent inflation and subdued growth prospects. GDP growth has been stronger than expected so far in 2023, but is now moderating as the impact of tighter financial conditions, weak trade growth and lower business and consumer confidence is increasingly felt. Financial conditions are restrictive, with forward-looking real interest rates having generally risen further in recent months. Activity has slowed in interest-sensitive sectors, particularly housing markets, and in economies reliant on bank-based finance, especially in Europe. Heightened geopolitical tensions are also again adding to uncertainty about the near-term outlook. Headline inflation has fallen in almost all economies, easing pressures on household incomes, but core inflation remains relatively high.

Global GDP growth is projected to ease to 2.7% in 2024, from 2.9% this year, before edging up to 3% in 2025 as real income growth recovers and policy interest rates start to be lowered (Table 1.1). A growing divergence across economies is expected to persist in the near term, with growth in the emerging-market economies generally holding up better than in the advanced economies, and growth in Europe being relatively subdued compared to that in North America and the major Asian economies. Annual consumer price inflation in the G20 economies is projected to continue easing gradually as cost pressures moderate, declining to 5.8% and 3.8% in 2024 and 2025 respectively, from 6.2% in 2023. By 2025, inflation is projected to be back on target in most major economies.

Risks to the near-term global outlook remain tilted to the downside. Heightened geopolitical tensions due to the conflict following the terrorist attacks on Israel by Hamas are a key near-term concern, particularly if the conflict were to broaden. This could result in significant disruptions to energy markets and major trade routes, and additional risk repricing in financial markets, that would slow growth and add to inflation. Headwinds from rising trade restrictions, inward-looking policies and the restructuring of global value chains are also contributing to the uncertain outlook for global trade, which is a key concern given the importance of trade for productivity and development. Continuing cost pressures, renewed rises in energy and food prices, or signs of an upward drift in inflation expectations could compel central banks to keep policy rates higher for longer than expected, potentially generating additional stress in financial markets. Conversely, the impact of higher interest rates and tighter credit standards could prove stronger than anticipated, leading to a more severe slowdown in spending, rising unemployment and higher bankruptcies. Tighter-than-expected global financial conditions would also intensify financial vulnerabilities, including in emerging-market and developing economies, and add to debt-servicing pressures in lower-income countries. On the upside, the global economy and financial markets have so far proved relatively resilient to the tightening of monetary policy, and inflation could return to target without a marked growth slowdown or a sharp rise in unemployment. A continuation of this pattern would imply better-than-expected growth in 2024 while inflation eases. Growth would also be stronger if households were willing to spend excess savings accumulated during the pandemic, but inflation persistence might also be prolonged.

Against this backdrop, the key policy priorities are to ensure that inflation is durably reduced, address mounting fiscal pressures, and improve the prospects for sustainable and inclusive growth in the medium term.


- Monetary policy needs to remain restrictive until there are clear signs that underlying inflationary pressures are durably lowered, with inflation expectations moderating further and a rebalancing of supply and demand in labour and product markets. Policy rates appear to be at or close to their peak in most advanced economies, although some additional rate rises could still be needed if underlying inflationary pressures prove persistent. The need to maintain downward pressure on inflation will limit scope for policy rate reductions until well into 2024, with nominal rates then being lowered in parallel with inflation. In Japan, a gradual increase in policy interest rates would be appropriate in 2024-25 provided inflation settles at 2%, as projected. Policy rate reductions have already begun in some emerging-market economies where policy tightening was initiated at a relatively early stage and inflation has eased significantly. There is scope for further rate reductions over 2024-25, although tight global financial conditions and the need to ensure anchored inflation expectations limit the pace at which these can occur.
- Governments face rising fiscal pressures from high debt burdens and additional spending on ageing populations, the climate transition and defence. Debt-service costs are also increasing as low-yielding debt matures and is replaced by new issuance. Without action, future debt burdens are likely to rise significantly. Past episodes of sustained debt reductions have generally been achieved with countries maintaining a primary budget surplus. On current plans, few countries are likely to achieve this in 2024-25, suggesting it will be more challenging to reduce high debt now than in the past. Stronger near-term efforts are necessary to create space to meet future spending pressures. A key step is to ensure that fiscal support measures, including remaining energy support schemes, are either withdrawn or become better targeted towards those most in need. Credible medium-term fiscal frameworks, with clear spending and tax plans that address future fiscal pressures and preserve the investment needed to support long-term growth and the climate transition, are also essential to ensure sustainability and provide flexibility to respond to future shocks.
- Enhanced multilateral co-operation is required to revive global trade. In an interconnected world, open and well-functioning international markets under a rules-based global trading system are an important source of long-term prosperity for both advanced and emerging-market economies. A key policy challenge is to balance the need for enhanced resilience of global value chains without eroding their benefits for efficiency or losing sight of the income gains that could accrue from lowering trade barriers, especially in service sectors.
- Given the long-term decline in economic growth and the pressing challenges from ageing populations, the climate transition and digitalisation, ambitious structural reforms are needed to reinvigorate growth and improve its quality. As emphasised in the 2023 edition of the OECD *Going for Growth* report, renewed efforts to reduce constraints in product and labour markets, strengthen investment and labour force participation and enhance skills development would improve productivity prospects and maximise the gains from the digital transformation. Faster progress towards decarbonisation is also essential. Increasing green and digital infrastructure investment and support for innovation, strengthening standards to enable a reduction in emissions, and raising the scope and level of carbon pricing are all key areas for policy action.

**Table 1.1. Global growth is projected to remain subdued**

	Average 2013-2019	2022	2023	2024	2025	2023 Q4	2024 Q4	2025 Q4
		Per cent						
<b>Real GDP growth<sup>1</sup></b>								
World <sup>2</sup>	3.4	3.3	2.9	2.7	3.0	3.0	2.9	3.0
G20 <sup>2</sup>	3.5	3.0	3.1	2.8	3.0	3.2	2.9	3.0
OECD <sup>2</sup>	2.3	2.9	1.7	1.4	1.8	1.7	1.5	1.9
United States	2.5	1.9	2.4	1.5	1.7	2.4	1.3	1.9
Euro area	1.9	3.4	0.6	0.9	1.5	0.5	1.1	1.6
Japan	0.8	0.9	1.7	1.0	1.2	1.6	1.4	1.1
Non-OECD <sup>2</sup>	4.4	3.6	4.0	3.8	4.0	4.1	4.0	3.9
China	6.8	3.0	5.2	4.7	4.2	5.5	4.4	4.1
India <sup>3</sup>	6.8	7.2	6.3	6.1	6.5			
Brazil	-0.4	3.0	3.0	1.8	2.0			
<b>OECD unemployment rate<sup>4</sup></b>	6.5	5.0	4.8	5.1	5.1	4.9	5.1	5.1
<b>Inflation<sup>1</sup></b>								
G20 <sup>2,5</sup>	3.0	7.9	6.2	5.8	3.8	5.4	4.5	3.4
OECD <sup>6,7</sup>	1.6	9.3	7.4	5.3	3.9	6.4	4.3	3.6
United States <sup>6</sup>	1.3	6.5	3.9	2.8	2.2	3.2	2.5	2.1
Euro area <sup>8</sup>	0.9	8.4	5.5	2.9	2.3	3.2	2.6	2.1
Japan <sup>9</sup>	0.9	2.5	3.2	2.6	2.0	3.0	2.1	2.1
<b>OECD fiscal balance<sup>10</sup></b>	-3.2	-3.4	-4.8	-4.3	-4.0			
<b>World real trade growth<sup>1</sup></b>	3.4	5.2	1.1	2.7	3.3	2.0	3.0	3.4

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 114 database.

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## Recent developments

### ***Global growth has proved resilient, but there are signs of a slowdown***

In the context of the negative shocks from Russia's war of aggression against Ukraine and the sharp tightening of monetary policy as central banks responded to above-target inflation, global growth has been unexpectedly resilient. The global economy expanded at an annualised rate of 3.1% in the first half of 2023, up from 2.8% in the second half of 2022, similar to the pre-pandemic trend (Figure 1.1). Available data for the third quarter of 2023 suggest that growth was little changed for the OECD economies as a whole, though with some slowdown among emerging-market and developing economies. There are also signs of increasing divergence across countries. Growth has slowed in many advanced economies, especially in Europe, where the importance of bank finance is relatively high and where the drag on incomes from higher energy costs has been particularly strong. The euro area economy grew by only 0.1% in the year to the third quarter of 2023, and several countries experienced output declines over the same period, particularly in Central and Eastern Europe. In contrast, GDP growth has held up better in the United States and many other commodity-producing economies, and the emerging-market and developing

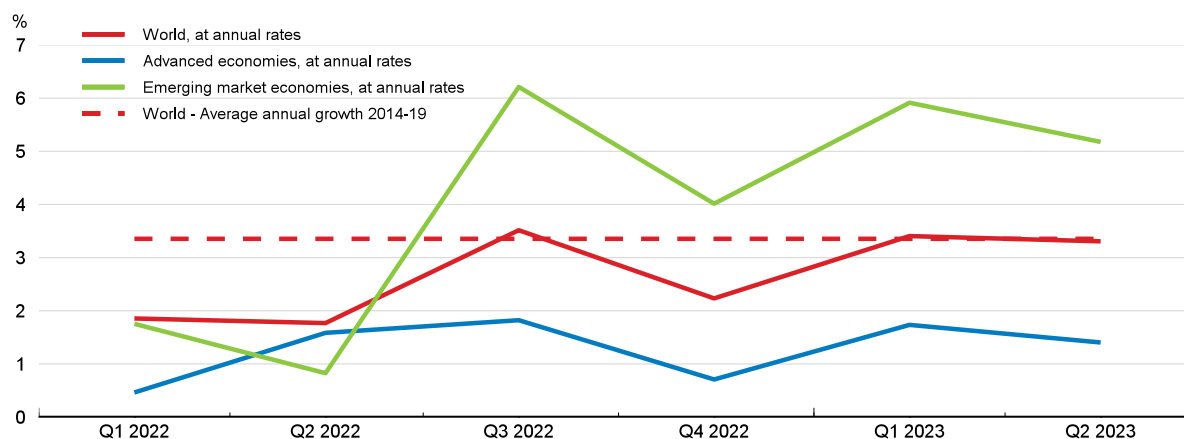
economies have collectively maintained growth rates close to those seen prior to the pandemic. Japan, the only major advanced economy yet to tighten monetary policy, has also experienced above-trend growth over the past year despite facing higher energy prices, though output declined in the third quarter of 2023. Growth in China has been volatile since the reopening of the economy at the start of 2023, amidst ongoing pressures in the property sector, but stabilised in the third quarter, helped by the implementation of a wide range of policy measures to support activity.

Across much of the world, tighter financial conditions are increasingly weighing on interest-sensitive expenditures. However, total household consumption has held up better than expected in the advanced economies, given the fall in real incomes over the past two years, and continued to expand steadily in most major emerging-market economies. Spending has been supported by tight labour markets, with job growth remaining sufficiently strong to keep unemployment rates near historic lows in many countries. In a number of economies, most notably the United States, household spending is also being sustained by the continued low level of household saving rates, with excess savings from the first year of the pandemic being reduced over the past two years. Business investment was also surprisingly positive in some OECD countries in the first half of 2023, despite the rise in the cost of external finance and, in some cases, near-stagnant GDP. In part this may have reflected the greater scope for internal finance of new investment given the rise in profit shares since the start of the pandemic. However, business investment declined in both the United States and Japan in the third quarter of 2023.

A range of recent developments suggest that growth has begun to lose momentum in many economies. These include: the weak PMI readings in many major economies – with India a notable exception (Figure 1.2); slowing credit growth in many economies; and persistently low levels of consumer confidence. These factors all point to a weakening of global growth prospects amidst a widening cross-country divergence.

**Figure 1.1. Global growth proved resilient in the first half of 2023**

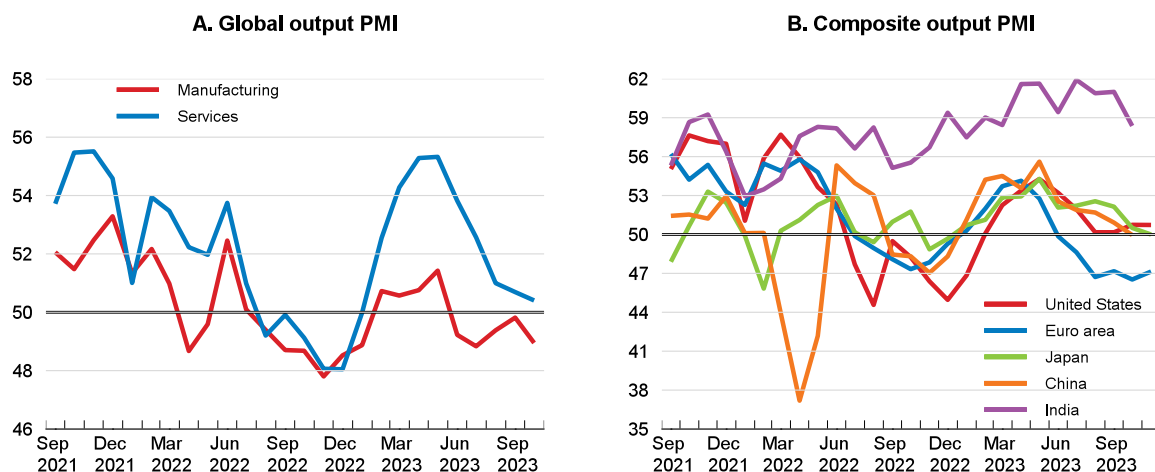
Quarter-on-quarter change in real GDP



Source: OECD Economic Outlook 114 database; and OECD calculations.

StatLink  <https://stat.link/obd8ym>

Figure 1.2. Survey indicators suggest that growth is slowing in many countries



Note: Values below 50 indicate that a balance of firms reports a contraction in output. Panel B includes the November Flash PMIs for the advanced economies.

Source: S&P Global.

Among the signs that tighter financial conditions are curtailing demand is the increase in corporate bankruptcies in many OECD countries (see risk section). Firms are being squeezed by higher debt-service burdens, tighter credit standards and, for many, slowing sales growth. New lending to non-financial corporations in the major advanced economies is either growing more slowly or even contracting, and this should be reflected in a slowdown in OECD non-residential investment. Housing investment is particularly sensitive to interest rates, and was generally weak among OECD economies in the second half of 2022 and the first half of this year as mortgage rates and other long-term lending rates followed policy rates upward (Figure 1.3). Amongst the emerging-market economies, residential investment has slowed this year in Chile, China, Colombia and South Africa, but has stabilised in Mexico after earlier declines. The rise in house prices, strong in many countries in 2021 and much of 2022, has slowed and in some cases reversed. House prices are down almost everywhere in real terms, and the volume of transactions has declined sharply. While there are signs of a bottoming out of housing sector investment in some countries where it has already fallen sharply, including the United States, sales and investment continue to soften in many other countries, especially in Europe.

While unemployment rates remain low, signs of labour market easing have started to appear in many economies, including a slowdown in annual employment growth, falling quit rates, lower vacancies, and in some cases a mild upturn in unemployment rates (Figure 1.4, Panel A). However, labour force growth has remained strong, rising by over 1½ per cent over the year to the third quarter of 2023 in the OECD as a whole, helped by continued high inflows of economic migrants in many countries and, in Europe, the integration of refugees into the labour market (OECD, 2023a). Nominal wage growth has begun to moderate in many economies (Figure 1.4, Panel B), but unit labour cost growth still remains high due to weak productivity growth, with costs rising by more than 4% per annum in many OECD countries over the past year.



**Figure 1.3. Housing market activity is slowing**

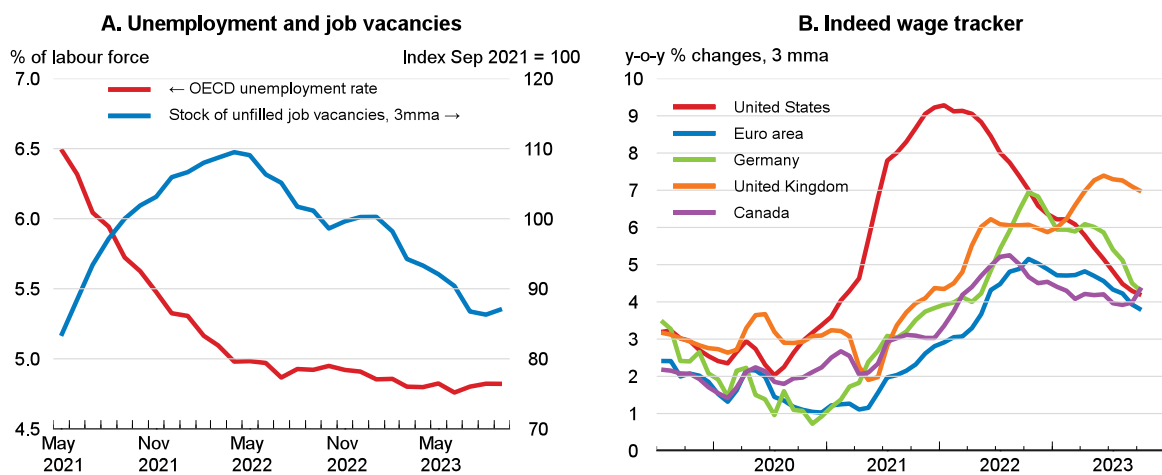
Gross fixed capital formation, housing, volume



Source: OECD Economic Outlook 114 database; and OECD calculations.

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**Figure 1.4. Labour market pressures have begun to ease**



Note: Panel A: Seasonally adjusted stock of unfilled job vacancies, based on data for 12 OECD economies. Panel B: The Indeed Wage Tracker is based on the median of the annual change in wages and salaries advertised in job postings on Indeed, controlling for job titles. Source: Indeed; OECD Short-Term Labour Market Statistics database; and OECD calculations.

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**Headline inflation has declined but core inflation is proving sticky**

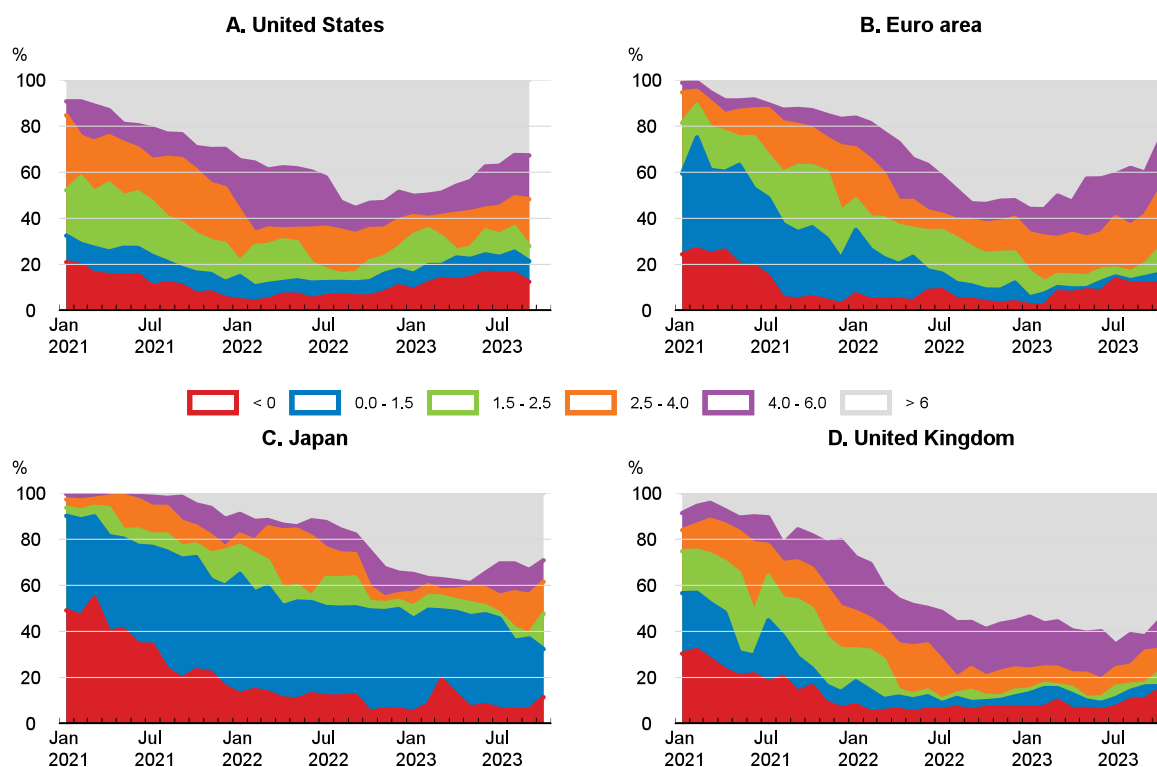
Headline inflation has fallen almost everywhere over the past year, primarily because of the partial reversal of the very large rise in energy prices over the previous two years. However, since June production cuts by key OPEC+ economies have contributed to higher prices. A variety of supply disruptions, alongside rising geopolitical tensions, have also contributed to volatility in European natural gas prices in the latter half of 2023. The upturn in oil prices since June has been reflected in retail prices for petrol, with headline inflation turning back up in some advanced and emerging-market countries.

Most measures of underlying inflation, including core inflation (excluding food and energy), have moderated, but with smaller declines so far. Even so, on a seasonally adjusted quarter-on-quarter basis, core inflation is estimated to have fallen to an annualised rate of below 3% in the G7 economies as a whole in the third quarter of 2023, down from over 4¼ per cent during the first half of the year. Services price inflation remains stickier than goods price inflation as wages are generally the main production cost in services. This is reflected in the distribution of price changes within the inflation basket, with over half of the items still having annual inflation rates above 4% in the United States, the euro area and the United Kingdom (Figure 1.5).

The cost counterpart to the high levels of inflation over the past two years has been higher unit labour costs and higher unit profits. National accounts data for OECD countries indicate that both factors helped to account for the increase in domestically generated inflation in 2022 (OECD, 2023b), a pattern last seen in the 1970s, when energy prices were also rising rapidly. In most advanced economies there was an increase in the profit share of national income in 2022 relative to 2019. In 2023, as inflation has subsided, the contribution of unit profits to inflation has fallen, although it remains higher than prior to the pandemic in most OECD economies. In contrast, the contributions from unit labour costs have increased (Figure 1.6). The experience to date does not point to a large structural shift in the distribution of national income towards firms – rather, it suggests that wages, which initially lagged behind prices, are now catching up, pushing the labour share of income back up. Moreover, firm-level studies do not indicate a generalised increase in mark-ups as inflation rose; mark-ups even fell for some sectors despite a rise in sectoral unit profits, as the latter omits some corporate costs (Piton et al., 2023).

**Figure 1.5. Inflation is easing, but prices are still rising rapidly for many items**

Share of consumer price basket accounted for by items in different inflation ranges

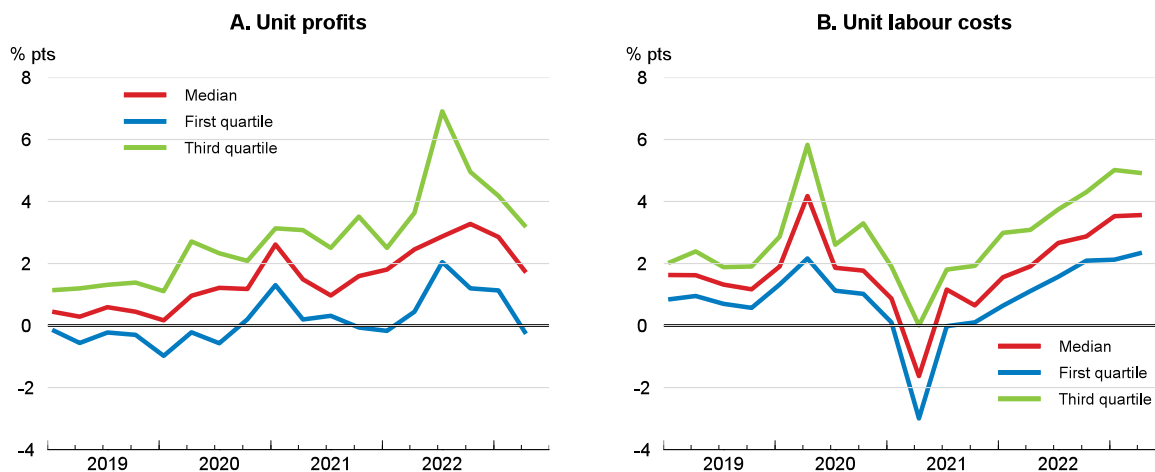


Source: Bank of England; Bank of Japan; Bureau of Economic Analysis; Eurostat; and OECD calculations.

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**Figure 1.6. Unit labour costs are now contributing more to inflation**

Contribution to year-on-year change in the GDP deflator



Note: Based on data for 33 OECD countries. Unit profits are measured as the adjusted gross operating surplus per unit of real GDP, and unit labour costs as the adjusted labour compensation per unit of real GDP. The published gross operating surplus data are adjusted by allocating part of self-employment income to labour compensation, following the methodology in Schwellnus et al., (2018).

Source: OECD Economic Outlook 114 database; and OECD calculations.

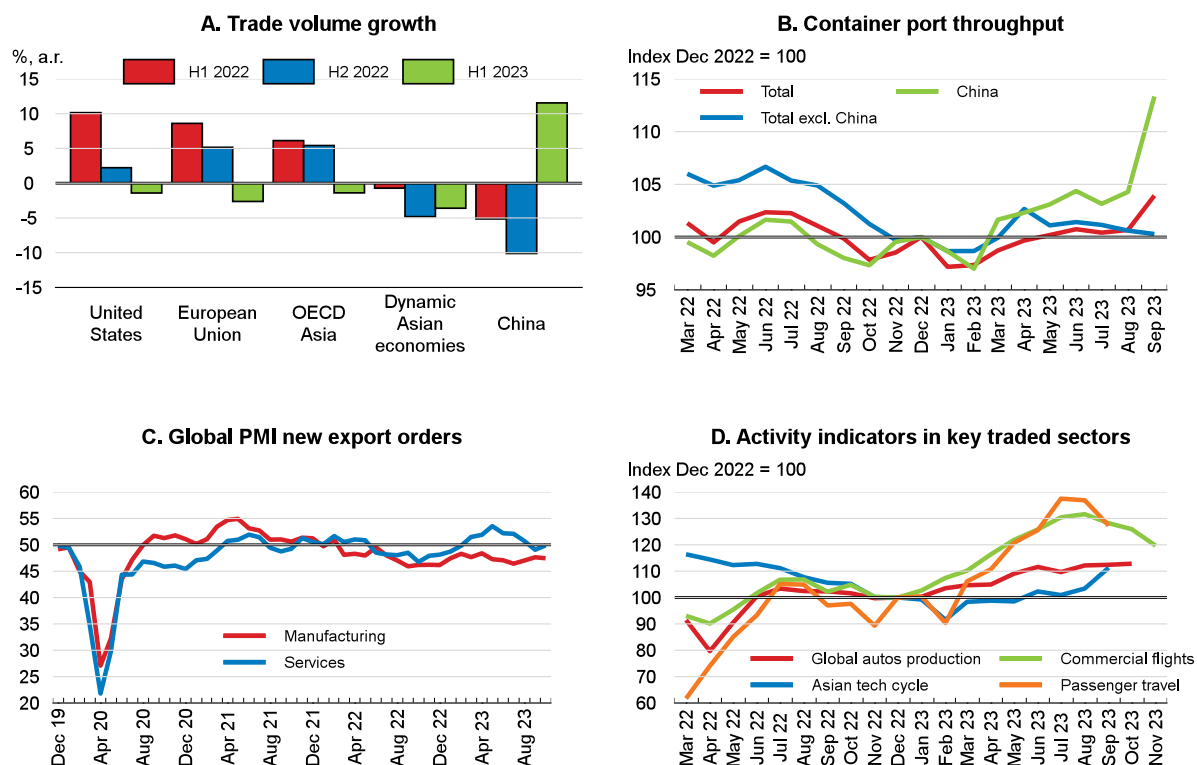
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### **Trade growth is weak and trade openness has declined**

Global trade growth has been surprisingly weak over the past year. Volumes of traded goods and services are estimated to have grown by only 0.1% at an annualised rate in the first half of 2023, following the weak expansion in the latter half of 2022. Merchandise trade volumes fell by 1.9% annualised in the first half of the year, whilst services trade volumes are estimated to have risen by 6.6%, as the ongoing normalisation of travel in Asia helped to boost tourism. Trade volumes rose sharply in China in the first half of 2023 after a very weak second half of 2022, but growth in the OECD economies slowed (Figure 1.7, Panel A). Data for the third quarter show some recovery in trade growth in the United States, Japan and Korea, alongside slower, but still positive Chinese trade growth. By contrast, trade volumes in Germany, France, Spain and the Netherlands contracted.

Near-term indicators suggest that trade will recover only gradually from the current slowdown. Aggregate container port activity indicators point to a mild recovery in total volumes, despite the strong upturn in China (Figure 1.7, Panel B). Freight transport prices are also subdued despite rising energy costs. Shipping rates for most routes remain low, at levels close to their average over the decade prior to the pandemic, although the Baltic Dry index has picked up since mid-2023, supported by strong demand for large vessels carrying coal and iron ore. Survey measures of new export orders remain weak in manufacturing and have slowed sharply in services at a global level (Figure 1.7, Panel C). Notwithstanding these signs of weakening, car production picked up in the third quarter, and there are signs that tech-related production in Asia has begun to improve, albeit from low levels (Figure 1.7, Panel D). International tourism has largely recovered from the pandemic shock, although the number of Chinese tourists remains about 45% lower than pre-pandemic levels. To date, the conflict following the terrorist attacks on Israel by Hamas has not disrupted the flow of goods or oil through the Strait of Hormuz or the Suez Canal, but it represents a significant risk (see below).

**Figure 1.7. Trade growth is weak and near-term indicators are subdued**



Note: Panel A: Trade based on the average of import and export volumes of goods and services, valued in USD at 2015 prices. Dynamic Asian Economies include Hong Kong (China), Malaysia, the Philippines, Singapore, Chinese Taipei, Thailand and Viet Nam. The European Union includes the 22 OECD countries who are members of the European Union, plus Bulgaria, Croatia and Romania. Panel C: A reading above (below) 50 signals that a balance of firms report an expansion (contraction) of orders. Panel D: Global auto production in October is an estimate based on the growth of production in China, France, Germany, Japan, Korea and the United States. The Asian tech cycle is an export-weighted index of tech-related production in Japan, Korea, Singapore and Chinese Taipei. Commercial flights from FlightRadar include both passenger and cargo flights.

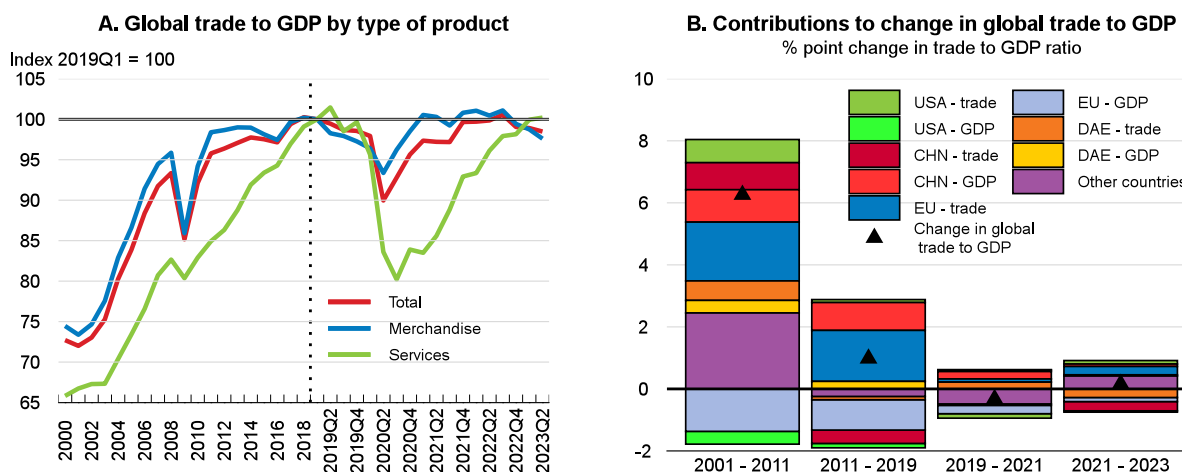
Source: OECD Economic Outlook 114 database; RWI/ISL Container Throughput Index; S&P Global; Bloomberg; FlightRadar; IATA; and OECD calculations.

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Following a rapid recovery from the early months of the pandemic, the ratio of global trade to GDP rose above 2018 levels by the fourth quarter of 2021 and remained there until the third quarter of 2022 (Figure 1.8, Panel A). Nonetheless, the ratio of trade to GDP has remained below the path expected if it had continued to rise at the same pace as in the decade prior to the pandemic. Since mid-2022, lower merchandise trade has pushed down total trade relative to GDP. This recent slowdown, and the broader plateauing of the trade-to-GDP ratio since the global financial crisis, reflect a combination of cyclical and structural factors. Understanding whether cyclical or structural factors dominate provides a sense of the risks to the trade outlook and also the potential avenues through which policy might help trade growth to revive.

Over the last decade, much of the slowdown appears to be structural, with trade intensity either declining in some countries, such as China, or growing more slowly in others (Figure 1.8, Panel B). This reflects in part a slowdown in the pace of global value chain integration, as well as the steady increase in restrictive trade policies being implemented throughout the world and increasingly inward-focused domestic policies (Arriola et al, 2021, Cigna et al, 2022, Antràs, 2021, Baldwin, 2022a). There has also been a steady rise in the share of less trade-intensive emerging economies in world GDP (Haugh et al, 2016; ECB, 2016).

**Figure 1.8. Global trade intensity has recently declined**



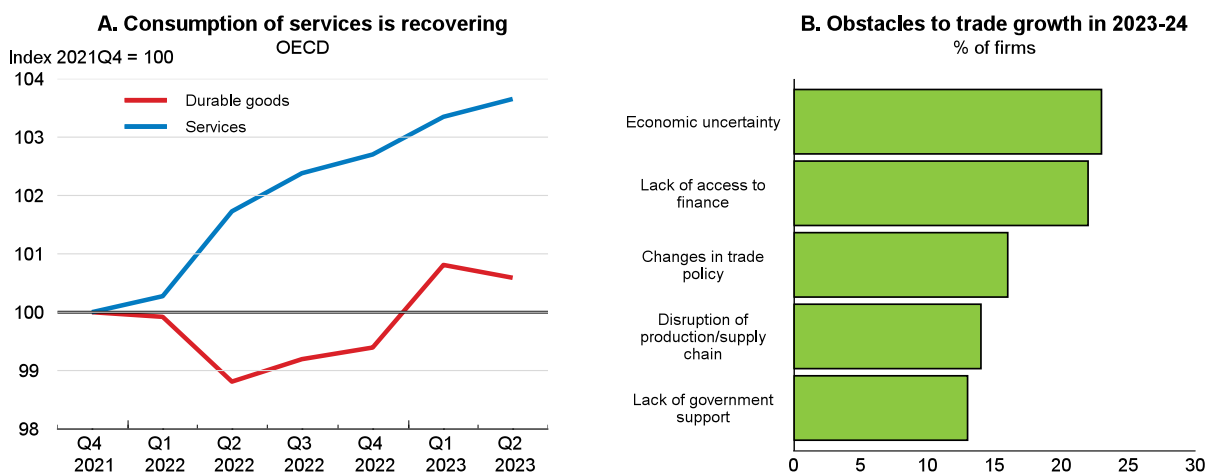
Note: Trade are based on the average of export and import volumes, valued in USD at 2015 prices. Panel B: Shift-share decomposition of changes in the global ratio of trade to GDP into contributions from the change in the trade intensity of each country or region ("trade") and contributions from the change in the share of each country or region in global GDP ("GDP"). Other countries shows the net effect of changes in trade intensity and GDP shares in the rest of the world. Dynamic Asian Economies (DAE) include Hong Kong (China), Malaysia, the Philippines, Singapore, Chinese Taipei, Thailand and Viet Nam. The European Union (EU) includes the 22 OECD countries who are members of the European Union plus Bulgaria, Croatia and Romania, and includes intra-EU trade. 2023 includes projected values where no data are available. Source: OECD Economic Outlook 114 database; and OECD calculations.

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More recently, cyclical differences in growth drivers across countries have clearly contributed to the current trade slowdown.


- Amongst the advanced economies, domestic demand has slowed more sharply in recent quarters in trade-intensive Europe and dynamic Asia than in less trade-intensive economies such as the United States and Japan. This reshuffling of demand has lowered global trade to GDP (Figure 1.8, Panel B).
- Declining trade intensity within economies is being driven by cyclical shifts in the composition of demand. Durable goods spending, which supported the rebound in trade growth in 2021, has softened, whilst households' services consumption has risen in OECD economies – implying, for a given rise in demand, weaker import growth (Figure 1.9, Panel A).
- Manufacturing inventories, which tend to be procyclical and relatively trade intensive, have fallen sharply since the third quarter of 2022 in many economies, as firms seek to respond to softening demand for goods.
- Intermediate goods trade, which reflects in part activity in global value chains, has also slowed following a robust rise in 2021. The WTO estimates that the share of intermediate goods in the value of non-fuel merchandise trade has fallen from a post-pandemic peak of 53.5% in the third quarter of 2021 to 48.3% in the second quarter of 2023 (WTO, 2023a).
- Higher interest rates and tighter credit conditions are also beginning to affect the cost and availability of trade finance. A survey from the Asian Development Bank suggests that the cost of trade finance has risen sharply for firms, and is now the second most important barrier to business for firms (ADB, 2023). Over a third of firms highlight insufficient financing as a significant supply chain issue, while 22% highlight it as the most pressing obstacle to growth (Figure 1.9, Panel B).

**Figure 1.9. Cyclical shifts in demand and credit are now weakening trade intensity**



Note: Panel A: Data calculated in seasonally adjusted volume terms, chain-linked and weighted in PPP. The OECD aggregate excludes countries for which data is not available. Panel B: Share of businesses citing each factor as a barrier.

Source: OECD Quarterly National Accounts database; Asian Development Bank; and OECD calculations.

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### **Financial conditions have become more restrictive**

Financial conditions have tightened in most major economies, reflecting the cumulative effects of past policy rate increases and quantitative tightening, reassessment by market participants of the expected future path of policy rates, and some repricing of risk amidst rising geopolitical tensions. Nonetheless, indicators of systemic financial stress generally remain contained, and there are some signs that risk appetite has begun to revive recently as disinflation continues.

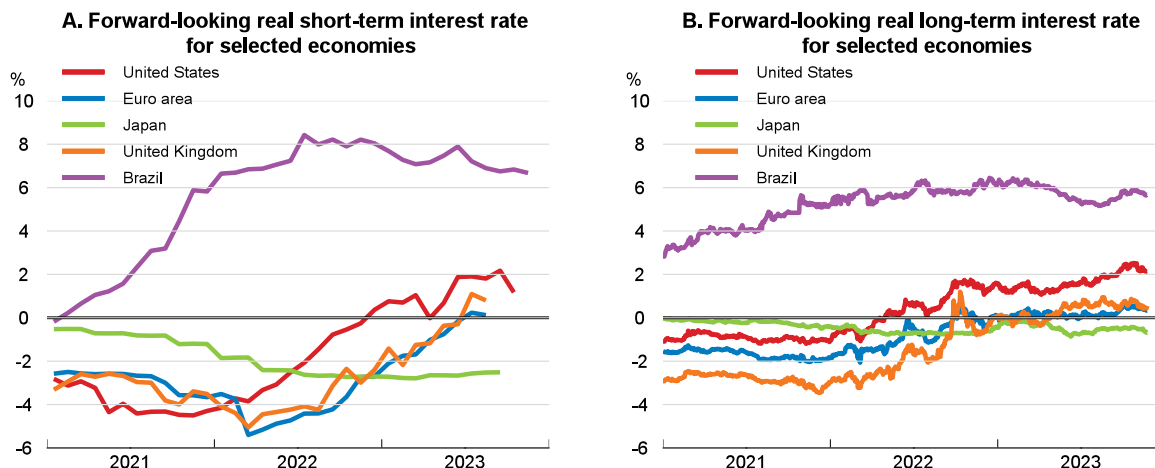
Forward-looking real interest rates are positive in most major economies (Figure 1.10), Japan being an exception, with nominal long-term government bond yields also rising substantially in recent months in most advanced economies. In the United States, both real and nominal long-term rates are now around the levels observed prior to the global financial crisis. An upward shift in market expectations of the future policy interest rate path has contributed to the rise in long-term rates, but term premia have also increased in many advanced economies. Longer-term interest rates and government bond spreads have also risen in most emerging-market economies. However, nominal sovereign bond yields have declined in Brazil, with falling inflation allowing the central bank to begin reducing the policy rate, though real longer-term rates remain high.

The rise in policy interest rates is being transmitted swiftly into bank lending rates to firms and households (Figure 1.11, Panel A). Bank lending standards have tightened in the euro area and the United States (Figure 1.11, Panel B), although not in Japan. The growth of credit to both households and firms has also slowed sharply, reflecting a combination of tighter credit supply and falling credit demand. In the euro area and in the United Kingdom, the slowdown in credit demand has been relatively important, whereas weaker credit supply has mattered more in the United States (Quaglietti, 2023), as reflected in the significant tightening of credit standards for companies (Figure 1.11, Panel B).

Sovereign bond spreads have increased since the summer in Italy, but generally remain contained across the euro area, helped by the availability of the ECB's Transmission Protection Instrument and flexibility across countries in Eurosystem bond reinvestments. Corporate bond spreads have also widened especially in high-yield segments, and issuance has been subdued. Higher long-term interest rates (Figure 1.12, Panel A) are also weighing on equity prices, particularly in many advanced economies (Figure 1.12, Panel B). The US dollar has appreciated against most currencies over the past six months

(Figure 1.12, Panel C), helped by safe-haven effects amidst heightened geopolitical tensions. There have also been sizeable currency depreciations in some emerging-market economies with relatively high or rising inflation and, to a lesser extent, in Japan.

**Figure 1.10. Forward-looking real interest rates continue to rise or remain high**

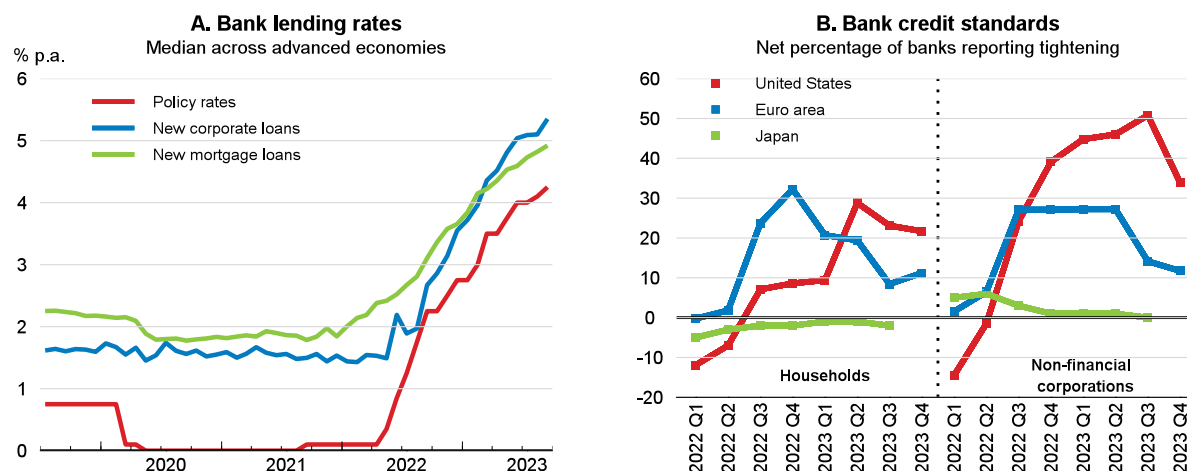


Note: Latest available data up to 23 November 2023. Panel A: Real short-term interest rates are calculated using nominal one-year government bond yields and one year-ahead inflation expectations by consumers in the United States, the euro area and the United Kingdom, by corporates participating the Tankan Survey in Japan, and by market professionals participating the Focus Survey in Brazil. Panel B: Real long-term interest rates show 10-year inflation-linked bond yields.

Source: OECD Economic Outlook 114 database; Banco Central do Brasil; Bank of England; Bank of Japan; Board of Governors of the Federal Reserve System; European Central Bank; University of Michigan; and OECD calculations.

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**Figure 1.11. Bank loan rates have risen sharply and credit standards have tightened**

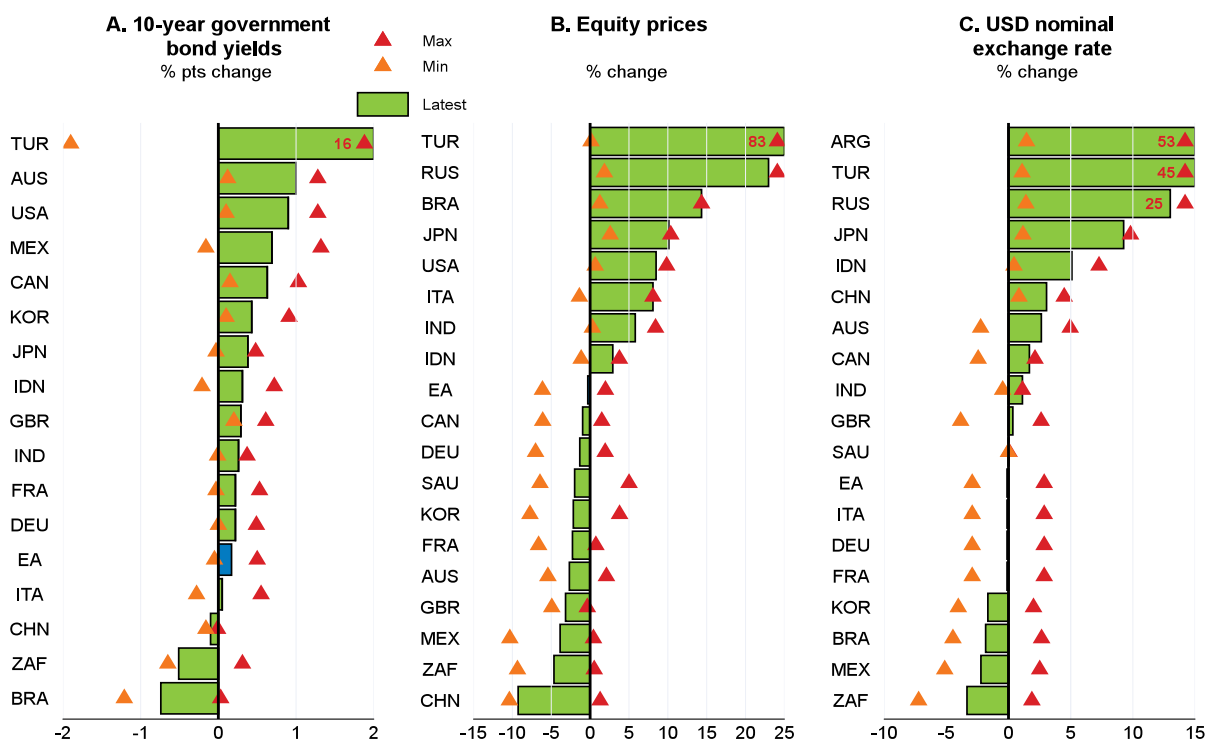


Note: Panel A: The advanced countries included are Australia, Canada, Denmark, France, Germany, Italy, Japan, New Zealand, Norway, Spain, Sweden, Switzerland, the United Kingdom and the United States. Panel B: Net percentages are defined as the difference between the sum of the share of banks reporting a tightening in credit standards and the sum of the share of banks reporting a loosening of credit standards. A positive (negative) balance indicates tighter (easier) credit standards. For the United States and Japan, credit standards to non-financial corporations are for large firms.

Source: Bank of Canada; Bank of England; Bank of Japan; Danmarks Nationalbank; European Central Bank; Japan Housing Finance Agency; Reserve Bank of Australia; Reserve Bank of New Zealand; Statistics Norway; Statistics Sweden; Swiss National Bank; US Federal Reserve; and OECD calculations.

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**Figure 1.12. Bond yields have increased and the US dollar has strengthened**



Note: "Latest" refers to the change between average of May 2023 and the latest available data up to 23 November 2023. Maximum and Minimum refers to the biggest falls and increases from the average of May 2023. Based on a 10-day average of daily observations. Panel C: A positive value indicates a depreciation relative to the USD.

Source: OECD Exchange Rates database; FactSet; and OECD calculations.

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## Projections

### ***A mild slowdown is projected, with a continued moderation of inflation***

The broad picture for the world economy over the next two years is one of a moderate slowdown followed by eventual normalisation, with growth returning to near-trend rates, and inflation converging back to central bank targets by 2025. Global GDP growth is projected to remain subdued through the first half of 2024, with only a modest improvement thereafter. The tightening of monetary policy since early 2022 is increasingly visible, with forward-looking real interest rates still rising in many economies, slowing domestic demand growth. Fiscal policy is also expected to remain mildly restrictive in most countries, particularly in 2024, with remaining energy support measures being phased out. Labour market prospects are a relative bright spot, with OECD-wide unemployment projected to remain at a low level. Real wages are projected to recover as inflation eases, with part of the increase in labour costs being absorbed by a decline in profit shares in many countries.

Global growth in 2023 is projected to be 2.9%, and weaken to 2.7% in 2024, the lowest annual rate since the global financial crisis other than the first year of the pandemic (Figure 1.13, Panel A). As inflation abates further and real incomes strengthen, the world economy is projected to grow by 3.0% in 2025. These outcomes remain highly dependent on the fast-growing Asian economies (Figure 1.13, Panel B).

After a relatively strong start to 2023, quarterly global growth is expected to have slowed gradually to an annualised rate just above 2½ per cent in the latter half of the year. Quarterly growth is projected to pick back up to about 3% from the latter half of 2024 and to remain around that level through 2025, helped by

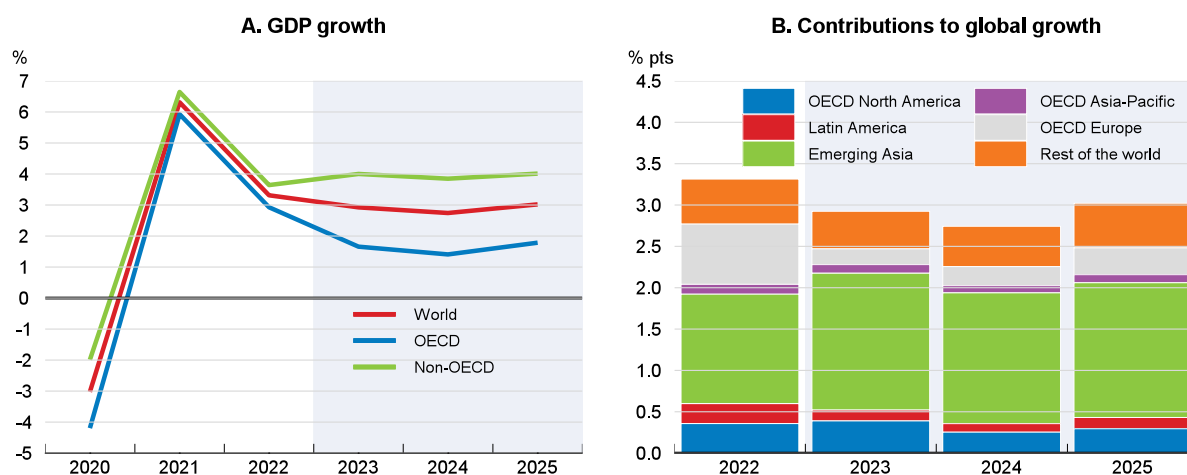


the gradual easing of policy rates. The near-term slowdown is relatively mild. Among the advanced economies, employment growth is projected to slow during 2024-25, but remain positive, alongside a gradual recovery in real wages. With household saving rates expected to remain broadly stable in most countries, the resulting increase in labour compensation is expected to sustain real private OECD-wide consumption growth of about 1.5% per annum on average during 2024-25. Steady but subdued growth is also projected for OECD-wide government consumption, while the annualised increase in total fixed capital investment is expected to pick up from below 1% in the final two quarters of 2023 to about 2¾ per cent by the latter half of 2025. Housing investment, which has already weakened significantly in several countries, is expected to continue declining until mid-2024. Business investment is projected to stagnate in the near term in many countries before picking up gradually through the latter half of 2024 and 2025.

The prospects for individual major economies and regions are as follows:

- In the United States and Canada, domestic demand growth is expected to moderate until mid-2024 due to tighter monetary and financial conditions, with slower job growth and a mild pick-up in unemployment. Monetary policy is expected to ease from the second half of 2024 as inflation continues to decline and is projected to help strengthen domestic demand growth in 2025. Real GDP growth is projected to slow in both countries in 2024, to 1.5% in the United States from 2.4% in 2023, and in Canada to 0.8% from 1.2%, before growth recovers in 2025 to 1.7% in the United States and 1.9% in Canada.
- Growth in the major European economies, which have been relatively hard-hit by the energy price shock in 2022 and the war in Ukraine, is expected to remain weak in the near term but improve gradually as inflation wanes, monetary policy easing gets underway and real incomes recover. Annual GDP growth in the euro area is projected to pick up from 0.6% in 2023 to 0.9% in 2024 and 1.5% in 2025. In the United Kingdom, GDP growth is projected to be subdued, with higher fiscal pressure weighing on household disposable incomes, but to improve from 0.5% in 2023 to 0.7% in 2024 and 1.2% in 2025. Tight labour markets will contribute to inflation persistence in the many countries, but as pressures ease inflation is projected to return to target in the euro area and the United Kingdom by the end of 2025.

**Figure 1.13. Global growth will remain modest and come mainly from the major Asian economies**



Note: In Panel B, Emerging Asia comprises China, India, Indonesia and the Dynamic Asian Economies (Hong Kong (China), Malaysia, Chinese Taipei, the Philippines, Singapore, Thailand and Viet Nam). Latin America comprises Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico and Peru. Contributions calculated moving PPP shares of global GDP.

Source: OECD Economic Outlook 114 database; and OECD calculations.

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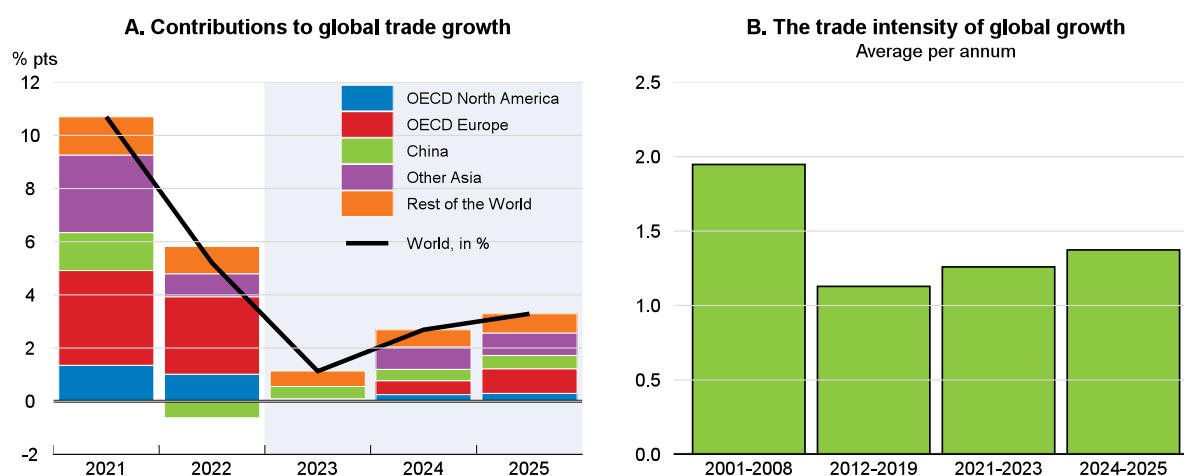
- The war in Ukraine and its initial effects on commodity prices had a pronounced adverse impact on growth and inflation in Central and Eastern Europe, on top of the necessary adoption of more restrictive monetary policies in most economies. As inflation pressures abate, and provided the war in Ukraine does not escalate further, steady growth is projected to resume in 2024-25, with inflation falling back towards central bank targets. Reconstruction efforts following the earthquakes in early 2023 have boosted demand in Türkiye, but with monetary and fiscal policies now being tightened to cool inflation and stabilise the public finances, GDP growth is expected to moderate to around 3% on average over 2024-25, with inflation remaining high but easing gradually.
- The advanced Asian economies are projected to have somewhat divergent growth profiles over 2024-25, reflecting in part different policy stances. In Japan, where monetary policy has remained accommodative, growth is projected to increase to 1.7% in 2023 before moderating to 1% in 2024 and 1.2% in 2025 as the positive contribution from net exports fades and macroeconomic policies begin to be tightened. Wage growth is projected to strengthen gradually, with inflation settling durably at 2% in 2024-25. Real GDP growth in Korea is expected to bottom out at 1.4% in 2023, held back by weak export demand and tighter monetary policy, recovering to 2.3% and 2.1% in 2024 and 2025 respectively as global semiconductor demand picks up and policy interest rates are lowered.
- GDP growth in China is projected to have rebounded to 5.2% in 2023, but is expected to slow to 4.7% in 2024 and 4.2% in 2025. Consumption growth remains subdued and activity in the real estate sector continues to weaken, but monetary policy easing and additional infrastructure investment will help underpin domestic demand. Consumer price inflation is expected to remain very low, at under 2% in 2024 and 2025.
- India has been relatively unaffected by the surge in energy prices in 2022 and the tightening of monetary conditions in the advanced economies over the past two years. Real GDP growth is projected to be 6.3% in FY 2023-24 and 6.1% in FY 2024-25. Surging services exports and public investment will continue to drive the economy. Inflation is also projected to decline progressively, supporting purchasing power. By FY 2025-26, the expected end of the El Niño weather pattern and productivity gains from recent policy reforms are projected to help growth pick up to 6.5%. GDP growth is also projected to remain brisk in Indonesia, at 4.9% this year and 5.2% in 2024 and 2025, with improved labour market conditions and confidence supporting consumer spending. Inflation in Indonesia has already been pushed down by tighter monetary policy and is projected to be 2.4% in 2024 and 2025. Inflation in India is now below the upper band of the central bank's target range, and is projected to be 5.3% in FY 2024-25 and 4.2% in FY 2025-26.
- Current economic conditions in the Latin American economies vary widely, with growth in the first half of 2023 having remained solid in countries such as Brazil, Mexico and Costa Rica, but slowing in Colombia and Chile and weak in Peru and Argentina, with the latter remaining in the grip of an economic crisis. Over 2024-25 some convergence is expected, however, with most of these economies projected to have GDP growth in the range of 2-3% in 2025. A common feature is that inflation is expected to continue to subside, facilitating a recovery of real incomes.

OECD unemployment rates have remained surprisingly low over the past year and a half, even where output has grown slowly or stagnated in the wake of adverse shocks. This would not be expected to persist if growth weakened significantly, but in the projections steady, if lacklustre, growth continues in most countries. The baseline is for OECD-wide unemployment to rise only modestly from the record-low level of 4.8% in September 2023, stabilising at 5.1% in 2024-25. The projected increases are somewhat larger in the United States, the United Kingdom, Canada and Australia, but in Japan and the euro area unemployment is expected to remain low and close to current levels.

Global trade growth is projected to recover gradually alongside global demand, with some support from the end of inventory declines, the ongoing recovery in Asian trade and, in 2025, a pick-up in global investment growth (Figure 1.14). These cyclical forces will provide some offset to the expected continuation of longer-term structural drags on trade growth, such as the projected moderate demand growth in more trade-intensive European economies and the burden of trade restrictions. World trade volumes are projected to rise by 2.7% and 3.3% in 2024 and 2025 respectively, up from 1.1% in 2023.

In the absence of further large shocks to food and energy prices – by assumption, commodity prices are held fixed in the projections (Annex 1.A) – projected headline and core (excluding food and energy) inflation rates return to levels consistent with central bank targets in most major economies by the end of 2025. Headline inflation has fallen earlier and faster than core over the past year given the steep fall in energy prices until mid-2023, but with oil and gas prices having picked up since June, and with commodity prices assumed to be fixed near recent levels through 2024-25, core and headline measures are projected to decline at similar rates from this point onward. In most emerging-market economies, other than economies with very high inflation at present, inflation is projected to reach target ranges by 2025.

**Figure 1.14. Global trade is projected to slowly recover but remain weak by historical standards**



Note: OECD North America includes Canada and the United States; Other Asia includes Japan, Korea, the Dynamic Asian Economies (Hong Kong (China), Malaysia, Chinese Taipei, the Philippines, Singapore, Thailand and Viet Nam), India and Indonesia. Trade growth is based on the average of imports and exports, in volume terms, in USD. Trade intensity calculated as the ratio of the average growth rate of imports and export volumes to GDP growth. Both series are in constant 2015 USD.

Source: OECD Economic Outlook 114 database; and OECD calculations.

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## Risks

There is a range of risks around the baseline projections through 2025. The unusually fast and large-scale tightening of monetary policy in most major economies during 2022-23 creates considerable uncertainty about the full range of effects, and could continue to expose vulnerabilities among households, firms, financial market participants and countries. Rising geopolitical tensions could also slow growth and add to inflation. Continued structural stresses in China create another downside risk to the global growth projections given China's overall importance in the global economy. In addition, ongoing climate change yields an ever-higher risk of extreme weather events, some of which have the potential to result in negative supply shocks with global effects. The El Niño episode that began earlier this year heightens the risks of extreme weather events, as well as potential near-term adverse effects on agricultural output in Australia and New Zealand, Southeast Asia, South Africa and many Latin American economies. Overall, the risks to the projections remain skewed to the downside, even if more favourable outcomes are also possible.

### ***Heightened geopolitical tensions are a key source of uncertainty***

Heightened geopolitical tensions remain a key source of near-term uncertainty and have been raised further following Hamas' terrorist attacks on Israel and the subsequent conflict. The economic effects of this conflict are uncertain and depend on its duration and scope. A temporary but pronounced slowdown is incorporated in the projections for Israel, amid considerable domestic disruptions to supply, but the broader direct effects from this for the world economy are relatively limited. If the conflict were to intensify and broaden within the wider region, there are much stronger risks that could slow growth and push up inflation.

- Oil and gas prices could strengthen significantly. Although less important than in the past, production in the Middle East economies continues to account for an important share of total global oil and liquefied natural gas (LNG) output and could be disrupted in the event of a wider conflict (World Bank, 2023). While the global economy has become less oil-intensive, particularly in the advanced economies, macroeconomic model estimates suggest that a USD 10 per barrel rise in oil prices could raise global inflation by 0.2 percentage points in the first year, and lower growth by 0.1 percentage points, with differential effects across oil producers and oil-importing economies.
- Trade flows could be significantly disrupted, creating supply-chain bottlenecks. Two key shipping routes are the Strait of Hormuz, with significant daily oil and LNG traffic, and the Suez Canal, with daily traffic representing between 12-15 per cent of global merchandise trade.<sup>1</sup>
- A hit to activity could also be accompanied by a sudden pullback from risky assets in financial markets. This could raise bond spreads, lower asset prices and result in losses for firms and investors exposed to these risks (Federal Reserve, 2023).

### ***The anticipated pick-up in global trade could fail to materialise***

There are additional significant downside risks to global trade. The longer-term decline in the trade intensity of growth is driven by structural factors, and the mild projected cyclical upturn in 2024 and 2025 could be weaker than expected. A weaker-than-forecast investment recovery in advanced economies, or tighter monetary conditions that further raise the costs of trade credit could soften trade growth. Structural forces could also intensify, posing risks to trade growth over the longer term. In particular, the increasingly inward-looking orientation of trade and investment policies and heightened geopolitical tensions could add to the downward trend in import intensity in many economies, including the United States and China. Lower trade in relation to GDP could have knock-on effects for potential growth, to the extent it weakens competition, raises prices, hinders productivity growth, and reduces the scope for economies to make use of new technologies to improve their growth prospects. These costs may be particularly heavy for emerging-market economies.

### ***The extent and full impact of monetary policy tightening remains uncertain***

Headline inflation has come down quickly in most economies over the past year, but generally remains some distance from target, and positive base effects from the reduction in energy prices are now fading. Core inflation has proved sticky, and services inflation remains elevated relative to pre-pandemic norms. A risk is that persistent high inflation, or a renewed surge in energy and food prices, might affect the inflation expectations of firms and households, making it more difficult to bring inflation back to target. There is evidence of threshold effects in the attention that people pay to inflation (Figure 1.15). With inflation having

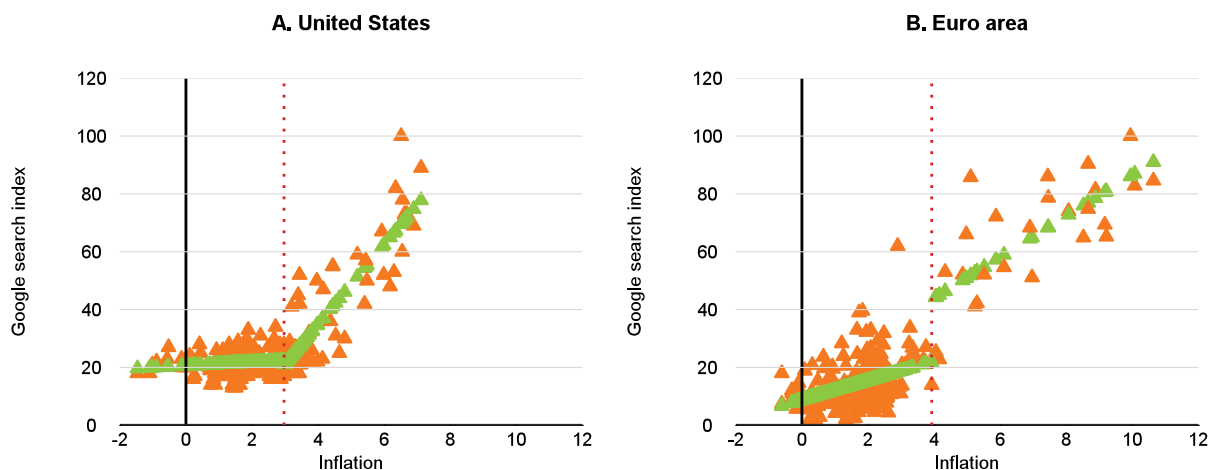
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<sup>1</sup> Disruption to production in Israel could also add to supply difficulties, despite the country's small overall share of global trade. Israel is an important source of several high-tech products, such as integrated circuits and medical instruments, and also provides around 6-8% of global exports of potash and phosphate fertilisers.

been above estimated thresholds (around 3% in many advanced economies) for some time already, it is possible that a degree of “belief scarring” has set in that could keep inflation expectations elevated. Combined with inertia in housing costs, this could make it more difficult than projected to reduce inflation from its current levels and potentially lead to additional monetary policy tightening that could further expose financial vulnerabilities.

It is also possible that the full effects on demand of past monetary policy will be greater than expected, particularly given the simultaneous tightening across many economies. Calibrating policy responses, which is always difficult, has been further complicated by the economic changes resulting from the pandemic and volatile commodity markets. Although the risk of a “hard landing” in the United States and elsewhere appears to be lower now than it was a few months ago, the confluence of weak housing markets, high oil prices and subdued credit growth mean that some empirical models still signal risks of recession in the coming year that are high by historical standards (Chaloux and Turner, 2023).

**Figure 1.15. Higher inflation raises awareness of inflation and may hinder a fall in inflation expectations**



Note: The charts show an index of Google searches of the word “inflation” plotted against year-on-year headline inflation, monthly, from 2004 onward. The orange triangles refer to the observed values for the Google search index for inflation and the green ones to the fitted values of the threshold regression model. The red vertical lines indicate the estimated threshold for the inflation rate.

Source: OECD Economic Outlook 114 database; Google Trends data; and OECD calculations.

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### ***Tighter financial conditions could expose financial vulnerabilities***

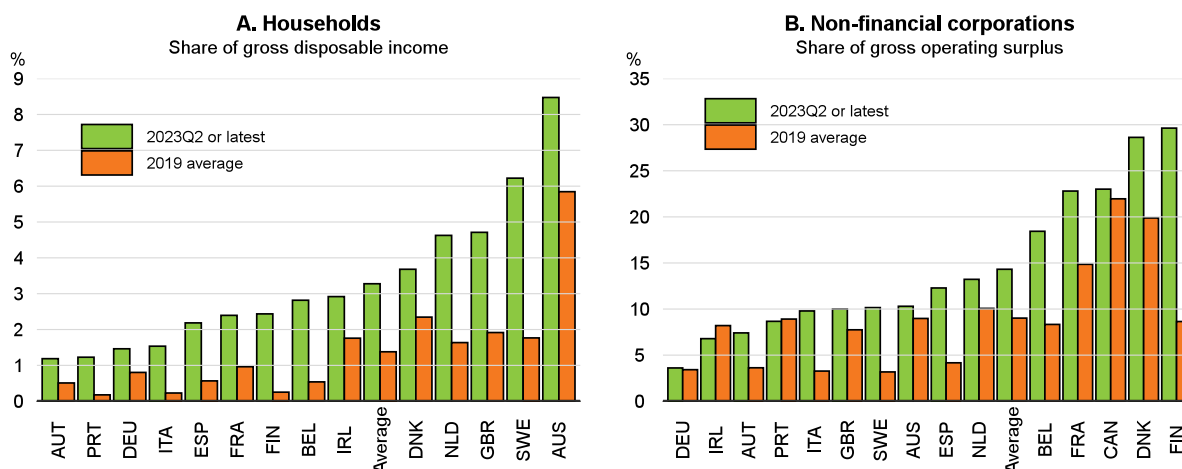
Financial markets have so far been relatively resilient to the tightening of monetary policy, but sizeable risks remain. If interest rates remain elevated for longer than currently expected, or if the impact of past rate rises on activity proves greater than anticipated, the capacity of households and non-financial firms to service debt could deteriorate further, generating credit losses for banks and non-bank financial institutions. Financial institutions also remain vulnerable to liquidity and interest rate risks.

Bank lending rates to households and firms have continued to rise, reaching around 5% on average in the OECD advanced economies, 3 percentage points above end-2019 levels. The rising cost of credit is being reflected in the interest expenses paid by households. In the advanced economies, these rose from an average 1.4% of disposable income in 2019 to 3.3% in the second quarter of 2023 (Figure 1.16, Panel A). Debt-servicing costs have risen particularly in countries where mortgages are predominantly issued at variable rates, including Finland and Sweden, as well as countries where mortgage rates are fixed for a relatively short period, including Italy and the United Kingdom. Interest expenses paid by non-financial corporations have also surged, from an average 9% of the gross operating surplus in 2019 in the major advanced economies to 14.3% in the second quarter of 2023 (Figure 1.16, Panel B).

If interest rates were to increase further, or to stay elevated for a long period of time, households and corporates could experience increasing difficulties in making loan repayments. Borrowers could even fall into distress in the event of a sharp deterioration of economic activity or incomes. The overall number of mortgages in arrears has started to rise across several advanced economies in 2023, but remains low by historical standards (IMF 2023; Bank of England, 2023). In contrast, corporate bankruptcies have risen more noticeably in 2023, and in several countries the number of bankruptcies in 2023 has already exceeded that during 2008-09 (Figure 1.17). Non-financial corporations have emerged from the pandemic with a higher debt stock, at 170% of GDP in the median OECD economy in 2022, and face sizeable repayment and refinancing costs.

Large swings in real estate prices could also jeopardise the ability of households and corporations to service debt. Nominal residential house prices have fallen recently in more than half of the OECD countries, but valuations remain high by historical standards in many countries. Risks of large valuation corrections also remain in commercial real estate markets, where structural changes associated with remote working are adding to the impact of higher financing costs. Commercial real estate prices have declined by 4% in the United States, 10% in the euro area and 20% in the United Kingdom over the past year, with real estate investment trust indices pointing to further falls ahead (Green Street, 2023).

**Figure 1.16. Household and corporate interest payments have risen substantially**

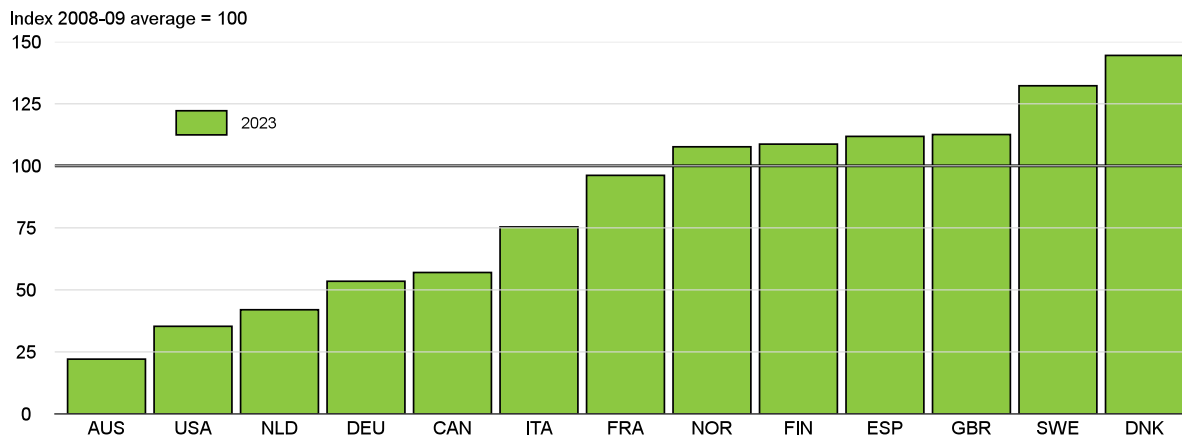


Note: For non-financial corporations interest payments are reported as shares of gross operating surplus and mixed income.

Source: OECD National Accounts database; and OECD calculations.


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**Figure 1.17. Corporate bankruptcies have risen back to 2008-2009 levels in some countries**



Note: Based on data for the total number of corporate bankruptcies. The green bars are computed as averages of Q1 and Q2. To account for seasonality, the 2008-09 index value is also computed as an average of Q1-Q2 in these years.

Source: OECD Timely Indicators of Entrepreneurship; Eurostat; and OECD calculations.

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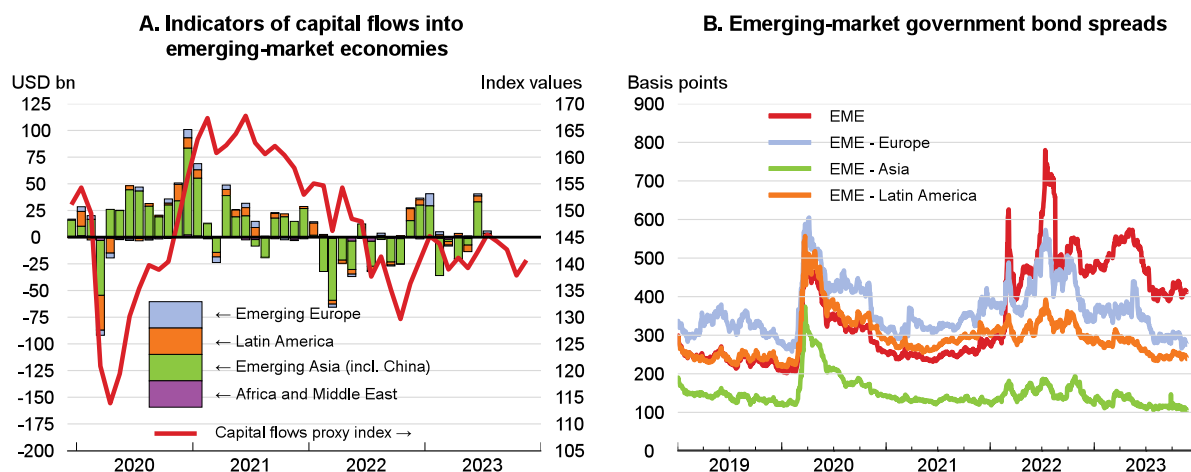
Banks and non-bank financial institutions also face elevated risks. Credit losses could increase if firms and households struggle to repay their debts, potentially weighing on the supply of new credit to the economy, as well as declines in collateral values securing existing loans. Loans to households account for a substantial share of bank assets in some countries, particularly Australia and the United States. The recent further surge in bond yields also intensifies duration risks for financial institutions from declines in the mark-to-market value of fixed-income securities as interest rates rise. In addition, as demonstrated by the failure of some US regional banks earlier in 2023, balance sheet pressures can also materialise rapidly if banks have to sell bonds to meet unexpected deposit outflows (OECD, 2023b).

### ***In emerging-market economies, debt vulnerabilities compound risks from tight global financial conditions***

The recent increases in long-term interest rates are also a potential source of risks for many emerging-market economies. Sovereign bond spreads have been volatile in recent months, and net portfolio capital inflows have declined, driven by net outflows from both equities and debt across most regions (Figure 1.18). Persistently high global interest rates could also exacerbate refinancing risks in countries where sovereign debt is high and debt maturities are short. Some countries also have a large share of foreign currency debt, including Argentina, Colombia and Egypt.

While emerging-market economies have shown considerable resilience over the past year, countries characterised by structural debt vulnerabilities have come under tighter market scrutiny. Sovereign spreads have increased by more in countries with elevated sovereign debt, a larger share of foreign-currency debt and a poorer credit rating (Figure 1.19). In several emerging-market economies, including Colombia, Peru and Romania, foreign-currency-denominated debt also still accounts for more than half of outstanding government debt. This is a potential source of refinancing risk. Moreover, the share of short-term debt over total debt also remains elevated in some economies. Coupled with low foreign exchange reserves, a high share of short-term debt exposes borrowers to rollover risks in the event of a significant further tightening of global financial conditions.

**Figure 1.18. Portfolio capital outflows have resumed and sovereign spreads have been volatile**



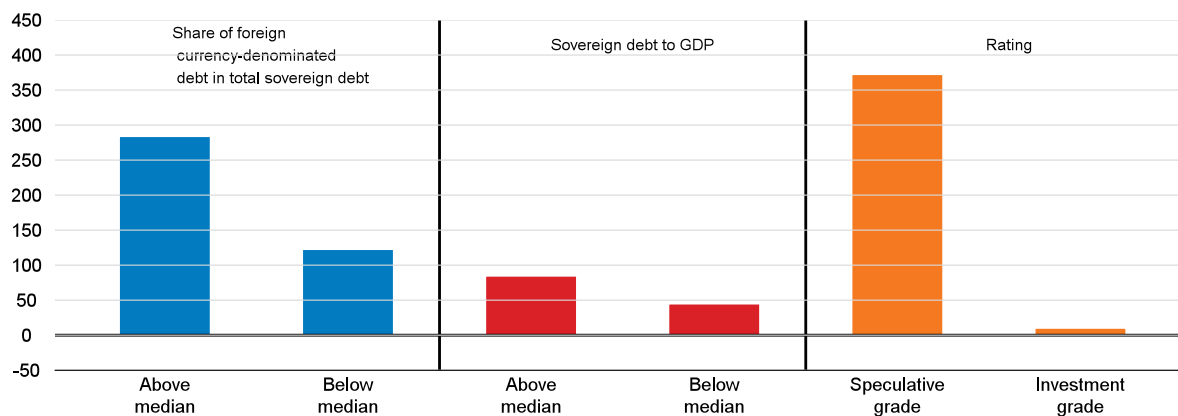
Note: Based on data up to 23 November 2023. Panel A shows the gross portfolio inflows data from the OECD Monthly Capital Flow dataset for 21 emerging-market economies grouped by four geographical areas and the Bloomberg proxy index of capital flows. The latter is a monthly composite index, reflecting the performance of commodity, equity, foreign-currency-denominated government bond and currency asset classes. Increasing (decreasing) values of the index indicate capital flows into (out of) emerging-market economies. Panel B shows unweighted regional averages for 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 Romania and Türkiye. 'EME - Asia' covers China, Indonesia, India, Malaysia, the Philippines and Viet Nam. 'EME - Latin America' covers Brazil, Chile, Colombia, Costa Rica, Mexico and Peru. The 'EME' aggregate covers all mentioned countries plus South Africa and Ukraine.

Source: OECD Monthly Capital Flow dataset; Bloomberg; Factset; and OECD calculations.

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**Figure 1.19. Sovereign bond spreads have risen faster in countries with higher debt vulnerabilities**

Basis point changes in EMBI sovereign spreads between 2021 and November 2023



Note: Based on average changes in EMBI sovereign spreads across a sample of emerging-market and developing economies between the 2021 trough and November 2023. The country composition differs in the three panels, with the left and centre panels based on a smaller sample (34 countries) compared to the right panel (60 countries). Ratings are based on Standard & Poor's classification.

Source: Bloomberg; International Monetary Fund; and OECD calculations.

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In about 20% of a sample of emerging-market and developing economies, USD-denominated sovereign spreads to US bonds were close to or higher than 10% in November 2023, a level at which market access can become restricted. In addition, about 15% of low-income countries are in debt distress, and an additional 45% are estimated to be at high risk of debt distress (IMF, 2023). In an environment of high global interest rates, more countries could lose access to international capital markets if creditors become increasingly concerned that large and growing debt burdens are unsustainable.

### ***A further slowdown in China would hit global growth***

China is the largest national economy in the world (in purchasing power parity terms) and has been a key driver of global growth in recent decades, as well as the largest beneficiary of reductions of the numbers living in absolute poverty. Financial stresses in China's large property sector threaten to diminish its economic growth by more than expected and potentially trigger additional financial distress. The difficulties being experienced by leading property developers have an impact on the public finances in many local authorities, on consumer sentiment, and on the balance sheets of banks and other lenders. There is a clear risk that the property crisis could have a larger and longer-lasting impact on the Chinese economy than projected. This would not only represent a drag on global growth directly, but would also slow growth in other countries. Illustrative scenarios suggest that an unanticipated one-year decline of 3 percentage points in China's domestic demand growth could directly lower global GDP growth by 0.6 percentage points, and potentially by over 1 percentage point in the event of a significant tightening of global financial conditions (OECD, 2023c). Countries with strong trade links with China would be hit hardest by any slowdown in Chinese demand, but the effects would be more widely felt, particularly in advanced economies, if financial conditions were to deteriorate, with risk premia rising and equity prices declining.

### ***Upside risks***

The world economy has been hit by a succession of negative supply shocks in recent years, which have hindered output growth and raised prices, but positive supply shocks are also possible. These would both improve near-term global growth prospects while also helping with disinflation. In particular, a reversal of recent oil output cuts by key OPEC+ countries could see oil prices move back down significantly, particularly given the prospects for stronger supply in 2024 from some non-OPEC producers. This would act as a shock absorber for the current slowdown in demand, provide a renewed downward impetus to consumer price inflation and boost real incomes in oil-importing countries. Continued strong labour force growth would also help to ease tensions in labour markets and limit cost pressures.

Another key area of uncertainty that could provide scope for upside growth surprises is the degree to which excess savings accumulated since the start of the pandemic are reduced. The excess savings phenomenon applies primarily to the advanced economies, where government measures to support household income in the first phase of the pandemic were generally substantial and consumption possibilities were constrained by mobility restrictions and the closing down of parts of the economy, especially in service sectors. Such income support was either absent or less generous in many emerging-market and developing economies, reflecting widespread informality and less-developed social security systems. So far, the extent to which excess savings have been drawn down varies considerably across the advanced economies (Box 1.1). In some large economies, saving rates have remained close to pre-pandemic averages. The baseline projections keep household saving rates in 2024-25 close to recent levels, but lower saving ratios and stronger consumer spending are possible, with excess savings being drawn down. While this would be positive for growth, it would also imply a slower-than-projected reduction in inflation pressures. In a similar vein, if demand-boosting policy measures in China are more successful than expected, this would be positive for global growth but imply more upward pressure on commodity prices and therefore slower-than-projected disinflation.

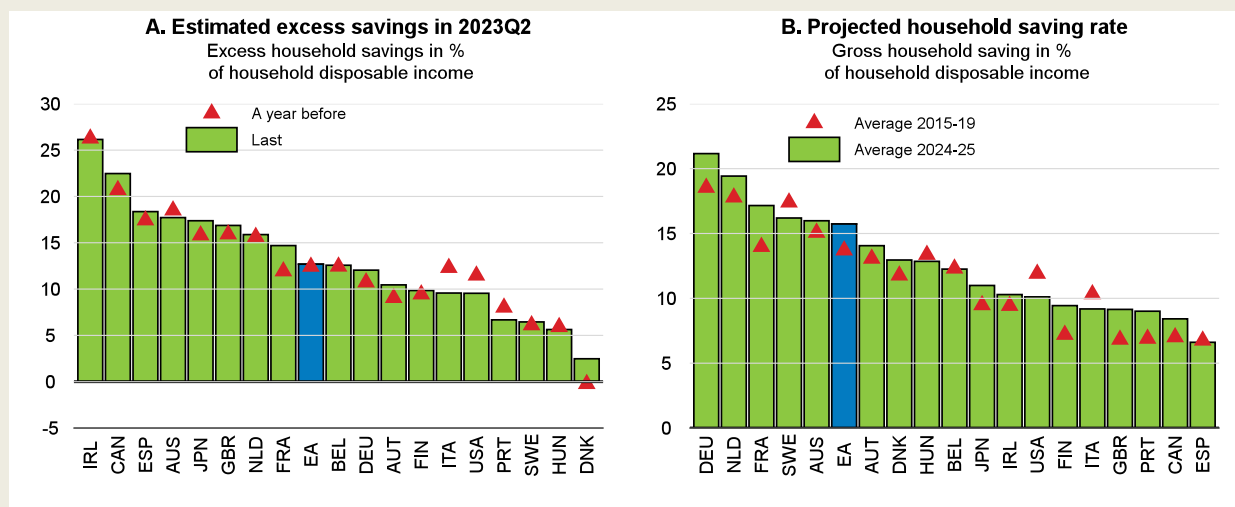
### Box 1.1. The evolution of excess household savings

In most advanced economies, the estimated level of excess household savings accumulated during the pandemic and as yet unspent is high (Figure 1.20, Panel A). Whether and when these accumulated additional savings will be run down remains a key source of uncertainty. An analysis of the composition and distribution of the estimated excess savings suggests that the likelihood that they will be drawn down is limited given the sizeable share held by high-income households and the small proportion held in liquid assets. In addition, recent declines in equity and house prices will have started to reduce the value of the invested savings.

The estimates use the difference between household saving in each quarter since the first quarter of 2020 and the level if the saving rate had been at its average pre-pandemic level (2015-19). A positive value is considered to be “excess” saving in that quarter, and the sum of the quarterly flows from the first quarter of 2020 onward gives the cumulative stock of excess savings.<sup>1</sup> There are large cross-country differences in excess savings levels, with these estimated to be more than 20% of disposable income in Ireland and Canada but less than 5% in Denmark. Over the past year, households in the United States have reduced these savings, whereas they have been stable or increasing in Canada, the euro area as a whole, Japan, and the United Kingdom.


Projected saving rates in 2024-25 are significantly above their 2015-19 average in the euro area as a whole, implying further additions to the stock of excess savings, contrasting with continued low projected saving rates in the United States where excess savings continue to decline through 2024 and 2025 (Figure 1.20, Panel B). This is consistent with more precautionary saving in most European countries than in the United States.

**Figure 1.20. Estimated current stocks of household excess savings and projected saving rates**



Note: Based on gross household savings. Panel A: ‘Last’ corresponds to 2023Q3 for the United States. Excess savings are the cumulated sum of quarterly saving flows since 2020Q1 relative to the levels that would have occurred if the saving rate had been equal to the average 2015-19 saving rate. Saving rates for Japan are estimated from 2021Q1 onwards.

Source: OECD Economic Outlook 114 database; OECD, Quarterly National Accounts database; and OECD calculations.

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The distribution of excess savings is a key factor affecting the extent to which they are likely to be run down. The estimated share of excess savings held by the top 10% of the income distribution rose from under 50% at the end of the first quarter of 2020 in the United States and the euro area to more than 75% and 67%, respectively, by the end of 2022 (Battistini et al., 2023). This shift also likely helps to explain the

fact that excess savings have increasingly been held in less liquid assets. The propensity to spend is higher at the bottom of the income distribution, so the shift in the distribution of excess savings towards better-off households means that the overall propensity to spend excess savings has been declining over time, reducing the potential for higher consumer expenditure out of excess savings. The proportion of savings held in liquid form (currency and deposits) also tends to be higher for lower-income households, so a shift in the distribution of excess savings towards higher-income households lowers the share of such savings held in liquid, ready-to-spend form.

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1. This estimation method, measuring the deviation of saving rates from a baseline, is similar to those used by Alves and Martínez-Carrascal (2023), Colabella et al. (2023), de Soyres et al. (2023) and Klitgaard and Higgins (2023). The choice of period used as the baseline for the household saving rate affects the results, but generally within a limited range. For example, using 2019 as the baseline reduces estimated excess savings by about 4 percentage points for the United States.

## Policies

### ***Monetary policy needs to remain restrictive in most advanced economies until inflation declines durably***

Since September, policy interest rates have been held constant in most advanced economies. Central bank balance sheet reductions, mainly reflecting reductions in bond holdings (quantitative tightening), have continued along well-communicated paths and in some cases gathered pace, adding upward pressure on long-term interest rates. With its long-standing accommodative policy stance, Japan remains an exception, though the conduct of yield curve control has been modified to allow wider fluctuations in the long-term government bond yield from the target rate.

Forward-looking real interest rates are now positive in most advanced economies, but the full effects of the cumulative tightening over the past two years have yet to be felt. Monetary policy needs to remain restrictive until there are clear signs that underlying inflationary pressures are durably lowered, with near-term inflation expectations moderating further and excess resource pressures fading in labour and product markets. As inflation eventually returns towards target, central banks will be able to lower policy interest rates, although they might not return to the very low levels which prevailed prior to the pandemic (see below).

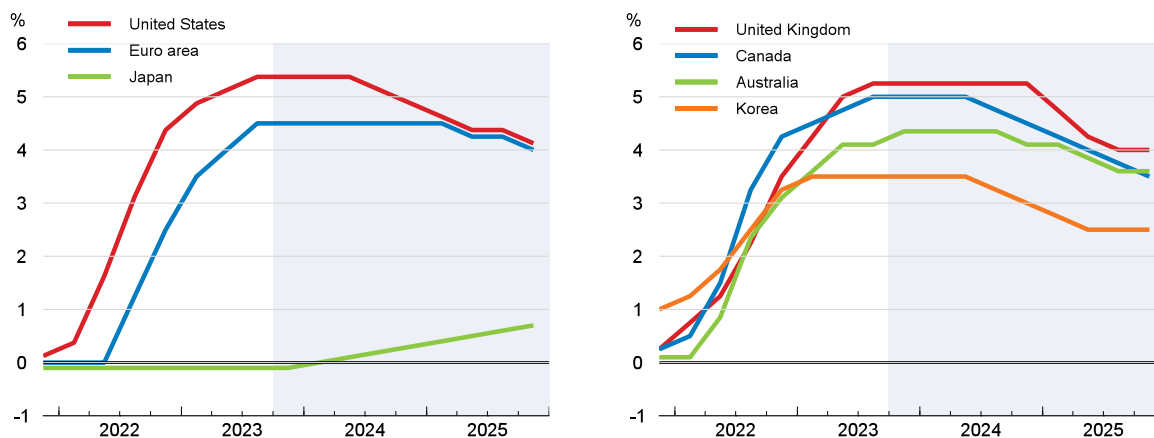
Policy decisions will need to continue to be communicated clearly given the ongoing uncertainty about the strength of the impact on inflation and output from the rapid rise in interest rates. Changes in economic structure – such as the increased prevalence of fixed or semi-fixed-rate debt in some housing markets, or higher levels of debt than in previous tightening episodes – and in financial markets, with the increased role of non-bank financial institutions, are affecting the transmission of monetary policy. The rapid and simultaneous tightening in many jurisdictions has also made the transmission mechanism more complex and uncertain, especially for smaller open economies, and may also affect outcomes as policy rates start to be lowered at a different pace across economies. Should inflation pressures prove more persistent than expected, some additional rate increases could still be needed. Conversely, faster disinflation than projected could pave the way for earlier policy rate cuts. In the event of additional financial market stress, central banks should make full use of the available financial policy instruments to enhance liquidity and minimise contagion risks.

On the basis of the projected outlook for inflation and growth, policy interest rates in all major advanced economies other than Japan are expected to be at, or close to, their peak (Figure 1.21). However, no rate reductions are expected before the second half of 2024, and in some economies not before 2025.

- In the United States, reductions in the federal funds rate are projected to begin in the second half of 2024, as core inflation declines prove sustained, and proceed in 2025, with policy interest rates being lowered to 4-4¼ per cent by the end of 2025. Bond holdings are expected to decline further following a pre-announced path.
- In the euro area, where core inflation pressures are still relatively-elevated, the main refinancing rate and the deposit rate are projected to remain unchanged until the spring of 2025, with subsequent modest rate reductions through the year. Bond holdings are expected to continue to decline with no reinvestment of Asset Purchase Programme redemptions but full reinvestment, at least until end-2024, of maturing Pandemic Emergency Purchase Programme securities.
- In Japan, an exit from the negative short-term policy rate is warranted next year, with the policy rate increasing gradually to 0.7% by the end of 2025, when inflation is projected to have durably settled at 2% and spare capacity is projected to be eliminated. Nevertheless, the monetary policy stance is expected to remain accommodative for some time, with negative real interest rates persisting until the end of 2025.
- No further policy rate increases are projected in Australia, Canada, Korea and the United Kingdom. Reductions in policy rates are projected to start in the second half of 2024 in Australia, Canada and Korea and in early 2025 in the United Kingdom. Central bank bond holdings are assumed to decline further in all these countries other than Korea.

**Figure 1.21. Policy rates are projected to decline only gradually in most advanced economies**

Policy interest rate for selected advanced economies



Source: OECD Economic Outlook 114 database; and OECD calculations.

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In the medium term, central banks will aim to bring policy interest rates back towards levels consistent with neutral real rates. However, the neutral real rate – the real interest rate at which the policy stance is neither accommodative or restrictive – is unobserved, difficult to estimate, and will vary over time due to changes in the underlying factors driving the demand for and supply of savings. Recent estimates of neutral real rates for the United States, the euro area and Canada have typically varied between 0 and 2% (Federal Reserve Bank of New York, 2023; Federal Reserve Bank of Richmond, 2023; Champagne et al., 2023). These are lower than the current yields on some long-term inflation-indexed bonds in financial markets, particularly in the United States, but broadly consistent with longer-term estimates of equilibrium real rates (Grigoli et al., 2023). Estimates of neutral nominal rates have, however, risen recently in some countries (Ferreira and Davin, 2022). Thus, nominal policy rates may remain at higher levels than prior to the pandemic, provided inflation settles at target rather than dropping persistently below target as in the decade after the global financial crisis.

Some factors behind the gradual longer-term decline in estimated neutral real rates persist, including demographic effects from ageing societies and weak potential output growth. However, the supply of public debt to be absorbed is set to be greater than expected prior to the pandemic, which might increase the neutral rate. This reflects the increase in debt since the pandemic began, rising future fiscal pressures, and the move by central banks to sell bonds held on their balance sheets. Stronger investment to achieve the climate transition in some conditions might also add to investment demand, increasing the neutral rate, although investment growth currently remains modest.

### ***Fiscal policy needs to ensure debt sustainability while responding to new priorities***

In 2023, fiscal policy has been mildly restrictive. The underlying primary balance in the median OECD advanced economy is expected to have improved by 0.4% of potential GDP (Figure 1.22) partly due to the full-year expiry of pandemic-related support. Many governments have continued to provide sizeable help to energy users, although energy prices falling from their peaks have helped to moderate the costs and support has already been withdrawn fully or partially in some countries. Defence spending has also been raised in several countries, particularly in Europe (OECD, 2023c), and faster implementation of Next Generation EU plans has boosted expenditure in some European economies. In the United States, higher spending on social security and healthcare and lower-than-expected tax revenues have generated an easing in the fiscal stance.

Fiscal projections for 2024-25 are conditional on announced government measures and OECD assessments of current plans (Annex 1.A.). Fiscal consolidation is expected in the vast majority of countries, but often at a mild pace, with the underlying primary balance in the median OECD economy improving by 0.5% of potential GDP in 2024 and 0.3% of potential GDP in 2025 (Figure 1.22). This largely reflects the further phasing out of support to energy consumers in 2024.

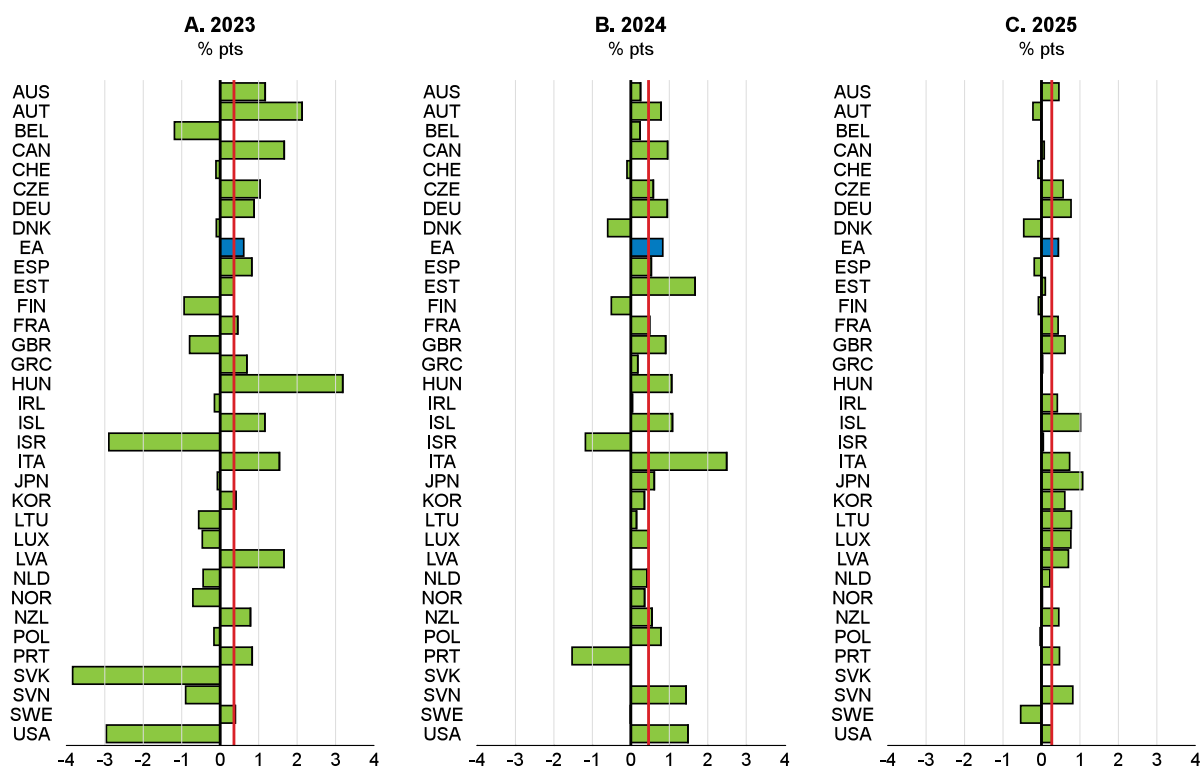
- In the United States, after sizeable fiscal easing in 2023, the fiscal stance is projected to become restrictive in 2024 as the unexpected shocks to receipts and expenditure in the current year fade, with the underlying primary balance rising by 1.5% of GDP. In 2025, a broadly neutral stance is expected.
- In the euro area, moderate fiscal consolidation is projected to continue in 2024-25, with the underlying primary balance improving by 1¼ per cent of GDP in total over this period, largely as a result of the progressive withdrawal of energy support measures. About one-quarter of the change

in the underlying primary balance stems from a change in the accounting treatment of tax credits for home improvements in Italy.<sup>2</sup>

- In Japan, despite an expected increase in defence spending and a new economic package to support households' income and medium-term investment, the underlying primary balance is projected to improve by a cumulative 1¾ per cent of GDP over 2024-25, reflecting the full expiry of pandemic-related measures and a gradual phase-out of sizeable energy support.
- Among other large advanced economies, fiscal policy in 2024-25 is projected to be restrictive in Australia, Canada, Korea and the United Kingdom. Among smaller economies, Iceland and Slovenia envisage cumulative improvements in the underlying primary balance in 2024-25 of more than 2% of GDP to rebuild fiscal space and reduce inflationary pressures, whereas in Israel a conflict-related fiscal expansion of about 1¼ per cent of GDP is projected.

**Figure 1.22. Modest fiscal consolidation is expected to continue in 2024-25**

Change in the ratio of the underlying primary balance to potential GDP



Note: The vertical red line indicates the median of the OECD advanced economies.

Source: OECD Economic Outlook 114 database; and OECD calculations.

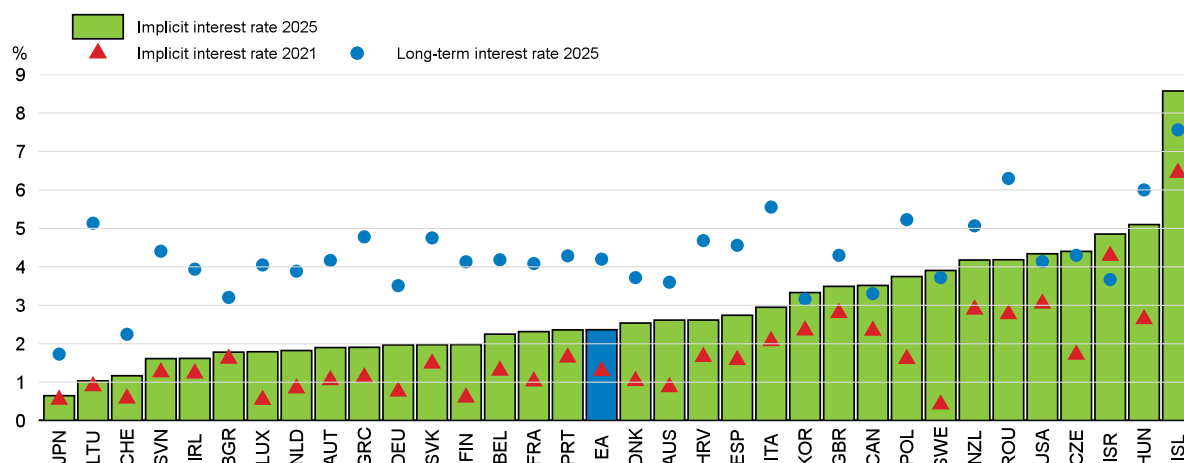
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<sup>2</sup> Tax credits in the Italian Superbonus scheme were initially accounted as non-payable tax credits, giving rise to a loss of revenue over several years after the home renovation took place. They are now treated as payable tax credits, giving rise to increased expenditure in the year the home renovation takes place (Istat, 2023). This improves the fiscal balance in 2024-26 and worsens it in 2021-23 (the three years when most renovations took place) relative to earlier estimates. The scheme is to become less generous as of 2024.

Public debt levels are generally higher than before the pandemic, and in many countries at levels relative to GDP seen before only in wartime. Interest payments on general government debt are set to rise further in 2024-25 as low-yielding debt matures and is replaced by new higher-yielding issuance (Figure 1.23). In the typical OECD economy, the implicit interest rate paid on debt in 2025 is projected to be 1.2 percentage points higher than the rate paid in 2021, with relatively large increases occurring in a number of smaller European economies.

Government debt maturities in many countries have lengthened since the global financial crisis (Figure 1.24), as governments took advantage of low long-term interest rates when issuing new debt. However, in several countries, the impact has been fully offset by the increase in central bank holdings of sovereign bonds. This lowers the effective average maturity of consolidated public debt, by around two years in the typical economy, as the main counterpart of the bond holdings in central bank liabilities is overnight bank reserves. It also magnifies the overall impact of rising interest rates on the wider public finances (when the central bank is included in consolidated accounts), as the central bank is paying interest on commercial bank cash reserves held at the central bank. Recent short-term interest rate increases thus generate larger interest payments to commercial banks as well as a loss of revenue payable from the central bank to national governments (De Grauwe and Ji, 2023).<sup>3</sup>

**Figure 1.23. Interest rates on government debt are set to rise further**



Note: The implicit interest rate is defined as general government gross interest payments in a given year divided by general government gross financial liabilities at the end of the preceding year.

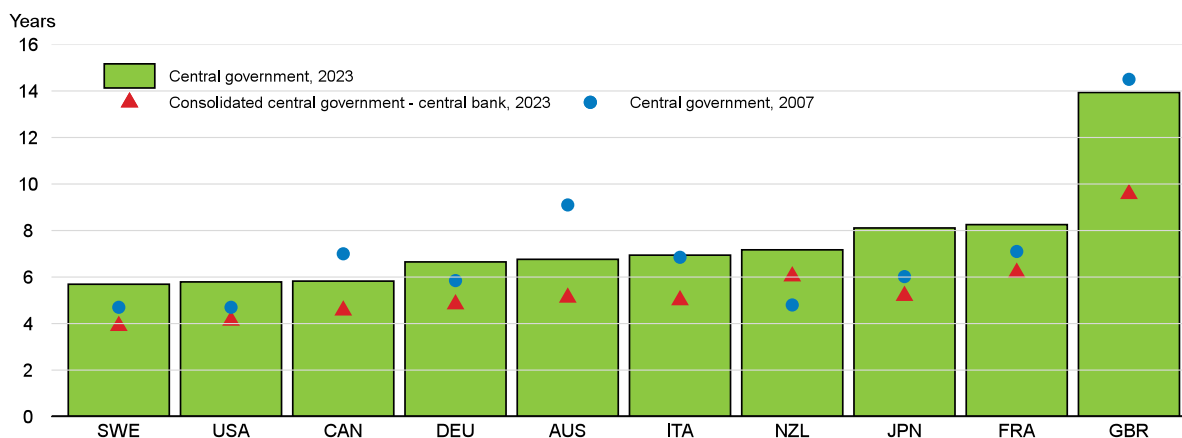
Source: OECD Economic Outlook 114 database; and OECD calculations.

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<sup>3</sup> Moreover, if short rates and long rates move in the same direction there could be capital losses on the debt that central banks have acquired, potentially adding to central bank losses and reducing payments to the government (OECD, 2023b).

**Figure 1.24. Quantitative easing has lowered the average maturity of public sector debt**

Average debt maturity



Note: For each country the red triangle is computed by assigning a zero maturity to central bank holdings of central government debt, since their counterpart in central bank liabilities is typically overnight bank reserves. Debt maturity as of end-August in 2023 and at end-year 2007.

Source: Bloomberg; Bank of England; Bank of Japan; European Central Bank; Ministry of Finance Japan; Reserve Bank of Australia; Reserve Bank of New Zealand; Sveriges Riksbank; US Federal Reserve; OECD Central Government Debt statistics; and OECD calculations.

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Governments face mounting fiscal pressures. Beyond 2025, for most countries, the implicit interest rate on public debt is projected to exceed the nominal GDP growth rate, putting upward pressure on debt-to-GDP ratios, as will the impact of ageing populations on health and long-term care expenditure and pensions expenditure (Guillemette and Château, 2023). In the absence of offsetting spending adjustments or a higher tax burden, such changes will add significantly to current debt levels in many countries (Box 1.2). The climate transition and plans to raise defence expenditure are additional sources of future spending pressures (OECD, 2023a).

### Box 1.2. Long-run fiscal sustainability in G7 countries

All governments face significant challenges from future spending pressures. In the absence of offsetting adjustments to the composition of spending or the level of revenue, government debt will rise. This box uses stylised economic and fiscal projections to trace out the possible evolution of government debt and financing needs in the G7 countries through to 2040. Both of these indicators show that policy changes are needed to prevent sizeable risks to long-run fiscal sustainability in many countries, keeping in mind that there are no specific thresholds for any one fiscal indicator (government debt, fiscal balance, interest rate, etc.) beyond which a country's fiscal position can reliably be characterised as unsustainable (Blanchard et al., 2021).

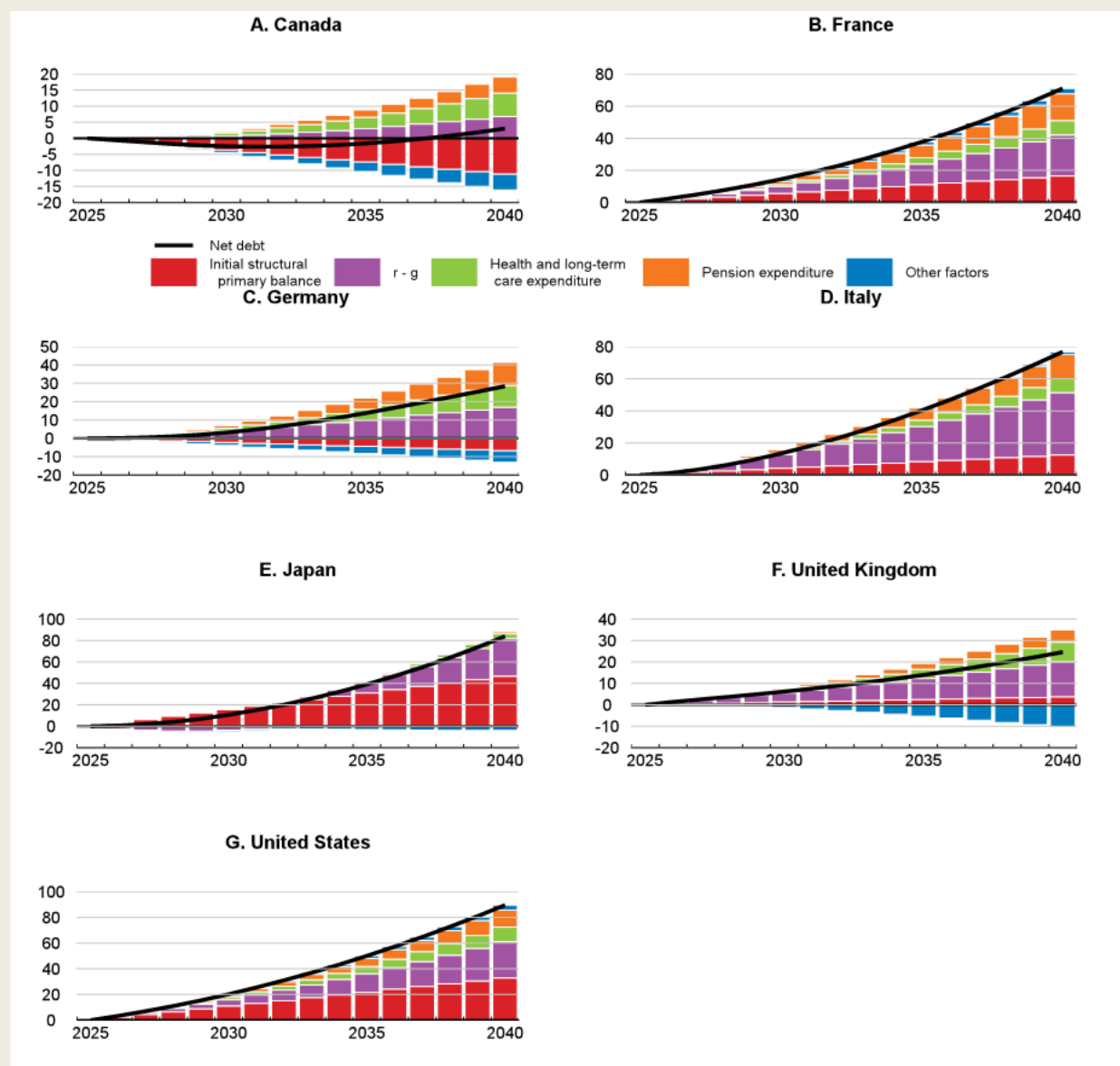
This Outlook's short-run economic and fiscal projections provide the starting point for the debt projections shown in this box, which are mechanical simulations based on a no policy change scenario. The resulting path for government net debt can be broken down into various components (Figure 1.25):

- **Initial structural primary balance.** This component illustrates the contribution that the structural primary government budget balance would make to the evolution of debt if it remained at its projected 2025 value in the future, ignoring the effects of other components discussed below. This is illustrative, not necessarily in line with official medium-term fiscal targets, and does not build in any corrective action in response to rising debt ratios.




**Figure 1.25. Public debt is on a worrisome path in much of the G7**

Net government debt, difference from 2025 in percentage points of GDP



Note: The debt projections shown here are mechanical simulations based on a scenario of no policy change. The underlying economic scenario is described in Guillemette and Château (2023). See Box 1.1 of that study for methodological details regarding the long-term government expenditure projections. See main text for a description of the components in the legend.

Source: OECD Economic Outlook 114 database; and OECD calculations.

StatLink  <https://stat.link/gjno2d>

- $r - g$ . This component is the implicit average interest rate paid on government debt minus the nominal GDP growth rate (but also accounts for interest received on financial assets). The projection of this implicit average rate accounts for the gradual refinancing of outstanding debt at projected market interest rates, assuming that the debt maturity structure remains as it is now. Projected market interest rates include fiscal risk premia that are functions of budget balances and debt-to-GDP ratios. Given

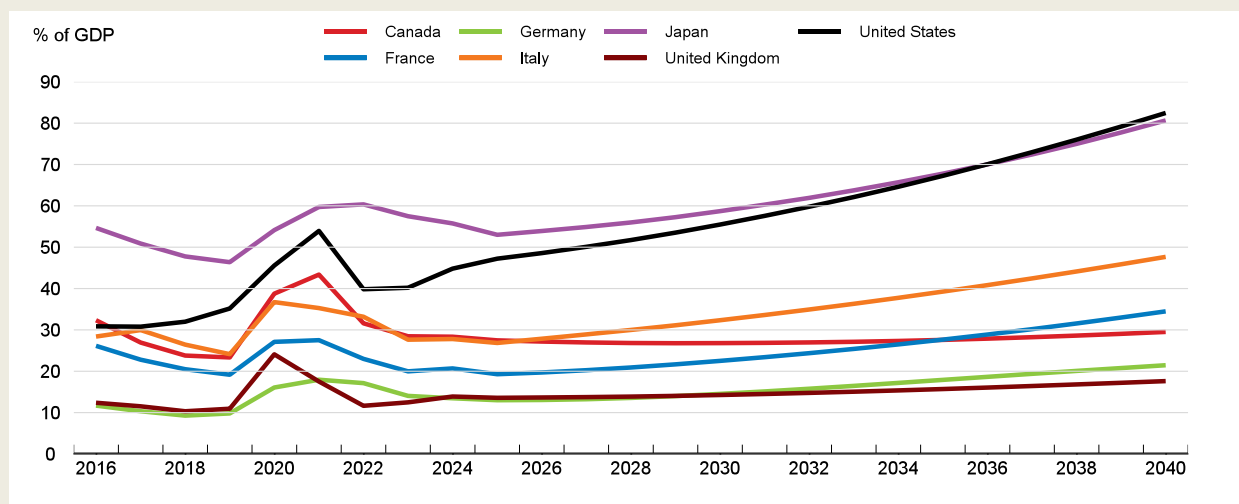
that market interest rates have recently risen and are projected to remain higher through 2040 than they have been in recent history, and that nominal GDP growth generally slows due to declining potential growth and normalising inflation rates, this component worsens debt dynamics. It adds 25 percentage points of GDP in government debt by 2040 in the median G7 country, but much more in countries with relatively high initial debt levels.

- *Health and long-term care expenditure.* Projected increases in public health and long-term care expenditure, due to population ageing and the rising relative price of government services, cause structural fiscal positions to deteriorate in all G7 countries, adding 9 percentage points of GDP of extra debt by 2040 in the median G7 country as spending pressures accumulate.
- *Pension expenditure.* As for health and long-term care, rising public pension expenditure due to population ageing is projected to add 13 percentage points of GDP to government debt by 2040 in the median G7 country, but with sizeable variation across countries. This projection assumes that current country-specific average pension benefit ratios remain constant over time, except in Italy where the ratio is projected to decline over time reflecting the continued implementation of recent pension reforms.
- *Other factors.* This component regroups government current expenditure on items other than health, long-term care and pensions (such as education and cash transfers) as well as net capital expenditure. Net capital expenditure includes capital transfers received, such as Next Generation EU grants, which are projected to taper off over the next few years. It also includes any estimated cyclical effect making the fiscal balance better or worse than the structural one in 2025 and which is projected to gradually disappear. Overall, this component contributes little to debt accumulation in the median country, although no account is taken of potential new sources of expenditure pressure such as climate change adaptation and higher defence spending (see, on the latter, OECD (2023c)).

Altogether, these illustrative projections see net government debt increasing by around 70 percentage points of GDP by 2040 in the median G7 country. Put differently, the median OECD country would need to increase annual revenue over time, by about 3½ percentage points of GDP by 2040, and 6½ percentage points of GDP by 2060, to keep government debt ratios from rising beyond projected 2025 levels given projected expenditure trajectories (Guillemette and Château, 2023).


Another useful indicator of fiscal pressure is the projected evolution of general government gross financing needs, defined as new borrowing requirements plus debt maturing during the year (Figure 1.26). After spiking at more than 35% of GDP during the COVID period, annual financing needs are now around 28% of GDP in the median G7 country. In the no policy change scenario outlined above, where budget balances deteriorate due to spending pressures, annual financing needs increase substantially in the years ahead, particularly in the United States (because of a large initial primary deficit), Japan and Italy (because of high initial debt levels). The United Kingdom is helped by a relatively long debt maturity structure, with an average remaining maturity of approximately fourteen years versus seven for the rest of the G7 as of the third quarter of 2023 (Figure 1.24). The projections (and the average maturity structure statistics) do not account for large holdings of government debt by central banks, which effectively shortens the average maturity of outstanding debt for the consolidated public sector.

**Figure 1.26. Projected annual gross government financing needs**



Note: The underlying economic scenario is described in Guillemette and Château (2023). The fiscal balance and debt projections are the same as in Figure 1.25.

Source: OECD Economic Outlook 114 database, and OECD calculations.

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These illustrative assessments highlight the need for policy changes to help ensure debt sustainability. One of the most effective ways of alleviating future fiscal pressure stemming from population ageing would be to undertake reforms to labour market policies and public pension programmes that seek to raise employment rates and extend working lives (Rouzet et al., 2019). Another would be to index long-term fiscal programmes to their underlying drivers, such as life expectancy in the case of pensions, which can also help reduce fiscal uncertainty (Orszag et al., 2021). Many countries are already making welcome changes in this direction. According to stylised simulations, ambitious labour market reforms, including linking statutory retirement ages to future gains in life expectancy, could halve long-run fiscal pressure in the median OECD country relative to a no-reform scenario (Guillemette and Turner, 2021). Credible medium-term fiscal plans that spell out the strategies governments will use to contain public debt would help the necessary adjustments to take place and reduce the risks of adverse market events.

Stronger near-term efforts to rebuild fiscal space would enable policy to respond effectively to future shocks and improve the near-term alignment of fiscal and monetary policies, thus reducing the burden on monetary policy to lower demand pressures and inflation. However, many OECD economies, including all G7 countries, are expected to record primary deficits this year, a situation often expected to persist, albeit with some improvement, through to 2025. Together with the potentially-higher level of future real interest rates than prior to the pandemic, this suggests that it may prove harder to achieve a significant reduction in debt than in the past (Arslanalp and Eichengreen, 2023). Over the past four decades, episodes of significant reductions in the debt-to-GDP ratio have generally required achieving a primary surplus and sustaining this over several years as well as the favourable impact of very low real interest rates on debt dynamics (Annex 1.B.; Rawdanowicz et al., 2021). Stronger consolidation efforts than those currently envisaged are thus likely to be needed if debt ratios are to be put on a downward trajectory.

Reinforced and credible medium-term fiscal frameworks, with clear guidance about future spending and tax plans, and reassessments of the composition of public spending would help to ensure debt sustainability while reallocating scarce budgetary resources towards unavoidable future spending pressures. This would help ensure that the necessary consolidation does not come at the expense of the investment needed to help foster the green and digital transitions or spending on other high-priority, productivity-enhancing measures such as skills acquisition. During past debt reduction episodes, primary balance improvements have mainly stemmed from declines in the primary expenditure-to-GDP ratio, with some additional, but smaller, revenue increases, especially from direct taxes (Annex 1.B.). Changes to pension expenditure have often accounted for a sizeable share of these declines in the primary expenditure-to-GDP ratio, illustrating the importance of ambitious pension reform to reduce expenditure and debt pressures.

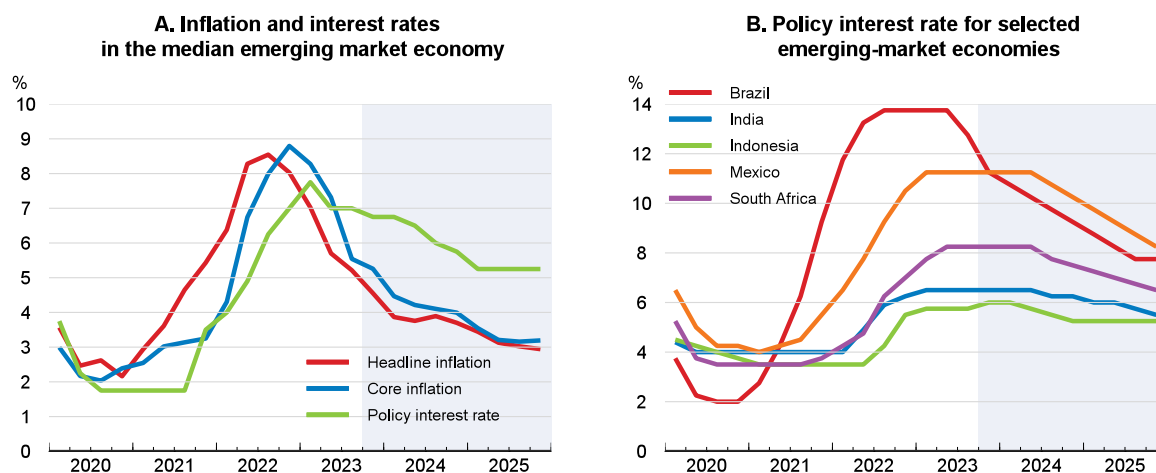
### ***Emerging-market economies need to ensure macroeconomic stability***

Monetary policy remains restrictive in most emerging-market economies, with core inflation often still far above central bank targets. However, the impact of policy tightening on inflation is appearing at a varying pace across countries. In some economies in which significant policy tightening started at a relatively early stage, including Brazil and Chile, central banks have now begun to reduce policy rates as inflation falls. In others, including India, Mexico and South Africa, policy rates remain unchanged with inflation remaining contained but not declining quickly. In contrast, faced with high inflation or currency depreciation pressures, Argentina, Indonesia, Russia and Türkiye have increased policy rates. China is a notable exception, with inflation remaining very low and policy rates being reduced recently to help support growth.

Monetary policy space in most emerging-market economies remains constrained by tight global financial conditions and the need to keep inflation expectations anchored, with positive real interest rates needed to help moderate inflation (Figure 1.27). Hence, in many countries, policy rates are projected to start declining only in 2024. Türkiye is an exception, with further policy rate increases still likely to be needed next year to curb persistently high inflation.


- In Latin America, policy rates in Brazil are projected to continue declining, with tighter credit conditions expected to steadily reduce core inflation. Mexico is projected to start reducing policy rates at a later stage, in the second half of 2024, when both headline and core inflation are expected to fall below 4%, the upper limit of the inflation target band.
- In Asia, continuing food price pressures in India and the need to firmly anchor inflation expectations in Indonesia, coupled with the common goal of avoiding currency depreciation, are expected to delay policy rate declines in these countries until mid-2024.
- The policy rate in South Africa is projected to start declining in the second half of 2024, when inflation is expected to moderate to the central bank target range.

**Figure 1.27. Policy rates are projected to be gradually reduced in many emerging-market economies**



Note: Panel A: The emerging-market economies considered are Brazil, Bulgaria, Chile, China, Colombia, Costa Rica, India, Indonesia, Mexico, Peru, Romania, Saudi Arabia and South Africa for headline inflation and the policy rate, and Brazil, Bulgaria, Chile, Colombia, Costa Rica, Mexico, Peru, Romania and South Africa for core inflation.

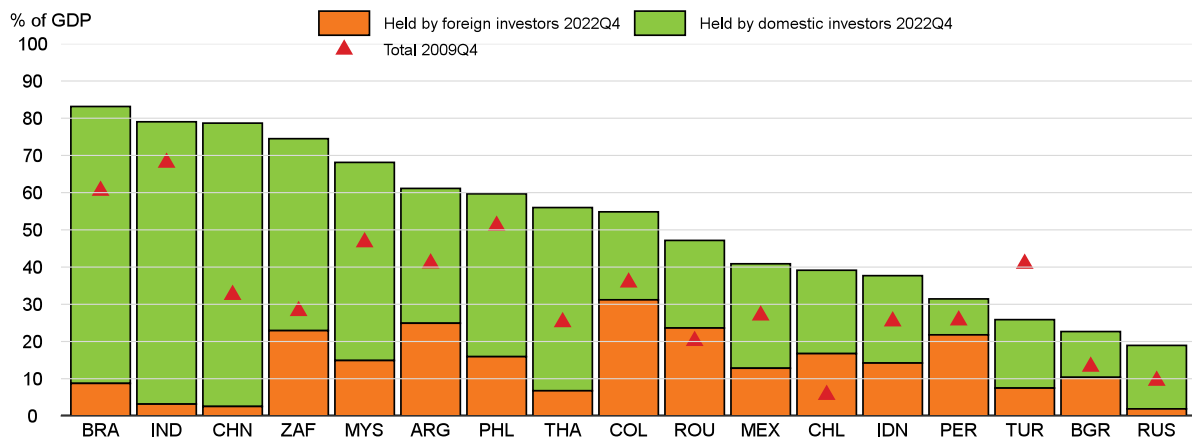
Source: OECD Economic Outlook 114 database; and OECD calculations.

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Fiscal deficits have continued to decline in many emerging-market economies, reflecting the reining in of pandemic-related fiscal support and, in some countries, a gradual withdrawal of energy-related measures. However, revenue windfalls have been deployed to counter the cost-of-living crisis in some countries, including Brazil, leading to a counter-cyclical fiscal expansion. Fiscal developments are expected to vary across countries in 2024. While Mexico is projected to have a sizeable near-term fiscal expansion, with new infrastructure projects and social programmes, fiscal consolidation is projected in Brazil, India and South Africa. In China, fiscal policy has become more supportive with a new package of spending (worth 0.8% of GDP) announced in October.

The stock of debt in the emerging-market economies is high and has risen sharply in some countries since the global financial crisis, eroding fiscal buffers to mitigate new shocks and increasing refinancing risks (Figure 1.28). Governments need to rebuild fiscal space and ensure fiscal sustainability, while supporting those most in need and making the necessary investments to boost growth and achieve the climate transition. Credible fiscal frameworks, based on transparent fiscal rules, would provide greater flexibility to respond to shocks. In commodity-rich countries, fiscal frameworks could also be designed in a way to delink fiscal policy choices from the volatility of commodity prices. Many countries need to strengthen revenue collection and fight tax evasion, including by improved tax administration, modernised property registries and streamlined corporate tax codes (OECD, 2023d), as well as introducing reforms to reduce informality. This would provide greater scope to expand coverage of social protection systems, especially in countries with a large informal sector. The rise in debt distress among lower-income countries also makes it particularly urgent that creditor countries and institutions take joint action to ensure that debt burdens are sustainable and to mitigate the risk that debt overhangs set back development.

**Figure 1.28. Public debt has risen sharply since 2009 in most emerging-market economies**



Note: GDP corresponds to the 4-quarter average.

Source: International Monetary Fund Sovereign Debt Investor Base dataset; and OECD calculations.

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### ***Trade policies should focus on expanding trade as well as enhancing resilience***

Open and well-functioning international markets under a rules-based global trading system are an important source of improvements in living standards. Through trade, higher productivity, lower prices and greater choice have brought greater prosperity for billions of people, especially in emerging-market economies. However, the global economy has now experienced over a decade in which trade growth in volume terms has just kept pace with output growth, after previously rising steadily since the 1990s. This has contributed to the broader structural slowdown in output growth since the global financial crisis. In recent years, the cumulative burden of trade restrictions has also risen, especially since 2018.

A key challenge for trade policy is to balance a rising number of policy objectives within an increasingly complex geopolitical environment. Steps to enhance the resilience of global value chains to supply chain disruptions, and reduce over-reliance on individual suppliers and complexity, should avoid eroding the efficiency benefits that value chains provide. Goods essential for the climate transition (Box 1.3) will require particular attention, given the sharp rise in restrictive trade practices for critical raw materials and the tendency of industrial policy to be increasingly inward-focused.

More concerted policy efforts to support trade in services would boost economic growth. Although services make up more than two-thirds of global GDP, they account for just under a quarter of global trade volumes. The OECD Service Trade Restrictiveness Index highlights the continued challenges of regulatory fragmentation and uneven conditions in access to services markets across countries (Figure 1.30, Panel A). The cost of trading is estimated to be typically twice as high for services than for goods, reflecting regulatory divergence across countries and complex procedures (OECD, 2023e). Reducing these costs by improving market access would generate substantial cost savings (OECD-WTO, 2021), raise trade and potentially strengthen productivity, both in service sectors and manufacturing sectors that purchase services inputs (Beverelli et al., 2017; Fiorini, and Hoekman (2017), Baldwin, 2022b). Acting now is critical, since many of the benefits from lowering services restrictions arise mainly over the medium to long term (Benz et al, 2023).

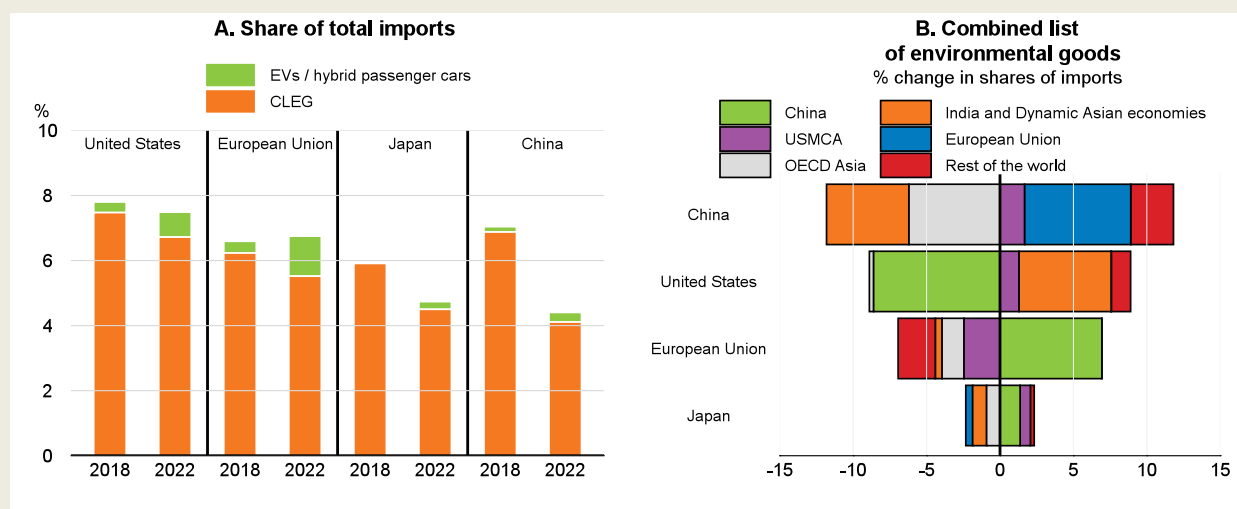
### Box 1.3. The restructuring of green trade

There is ample evidence that geopolitical factors are now contributing to the restructuring of aggregate global trade patterns (Antràs, 2021, Baldwin, 2022a, OECD, 2023b). This box highlights that green trade is also changing in the major global economies. Moreover, green trade has not grown particularly quickly in these economies: over the last 5 years, in value terms, imports of environmentally-related goods grew more slowly than total imports, reflecting in particular weakness in China. By contrast, trade in electric vehicles has risen sharply from low levels.

The analysis uses import data for the United States, Japan, the European Union and China based on the OECD combined list of environmental goods (CLEG) (OECD, 2019)<sup>1</sup> and trade in electric or hybrid passenger vehicles.<sup>2</sup> All data are in nominal US dollars, based on UN Comtrade statistics, as volume data are not available.<sup>3</sup> An unavoidable limitation of this approach is that relative price movements across products as well as exchange rate movements could affect some changes in trade shares over time.


In recent years, trade in environmental goods has collectively outpaced total merchandise trade growth (UNCTAD, 2023; WTO, 2023b). However, the share of environmental goods (CLEG) in the combined total imports of the United States, Europe, China and Japan slipped from 6.8% in 2018 to 5.5% in 2022.<sup>4</sup> In contrast, the much smaller trade in hybrid and electric passenger vehicles rose from 0.3% of total imports in 2018 to 0.7% in 2022 (Figure 1.29, Panel A).

**Figure 1.29. Changes in imports of environmental goods over 2018-22**



Note: All data in value terms, USD. For each of the four major economies, Panel B shows the change in the share of their CLEG imports from selected partner economies. OECD Asia includes Korea and Japan; Dynamic Asian Economies include Hong Kong (China), Malaysia, the Philippines, Singapore, Chinese Taipei, Thailand and Viet Nam; USMCA includes the United States, Mexico and Canada; Rest of the world includes all other countries not mentioned elsewhere in the chart.

Source: UN Comtrade; and OECD calculations.

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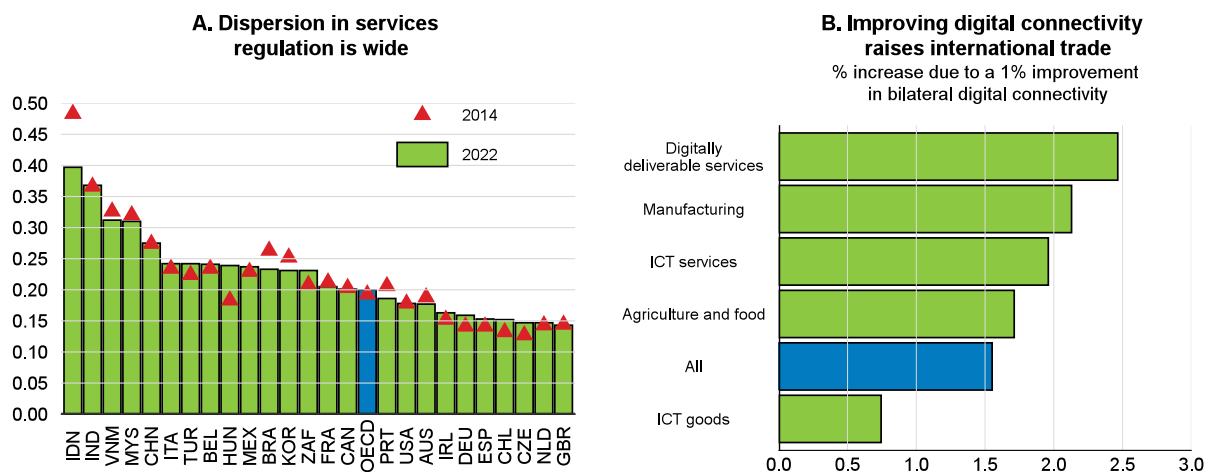
Changes in the bilateral import shares of the combined list of environmental goods have been sizeable (Figure 1.29, Panel B). In the United States, the share of imports from China declined between 2018 and 2022, offset by rising levels of trade with India and the dynamic Asian economies, at both total trade and broad product categories. There were only small changes in the share of imports from Canada and Mexico. In contrast, China's share of imports rose in Europe. In Japan, no strong pattern is evident in overall environmental goods trade. For all three of these economies, the trends are similar to changes in trading partners for manufacturing imports as a whole (Koh et al. 2023).

Trade in environmentally-related goods can help diffuse technology (Garsous and Worack, 2021; Bacchetta et al, 2023). In the first half of 2023, trade in these goods has picked up in Europe, Japan and the United States. As efforts to accelerate the climate transition increase, the potential impact of industrial and trade policies on trade in environmentally related goods should be carefully considered.

1. The CLEG is made up of 11 broad product categories, including renewable energy plants and waste-water treatment. The CLEG contains 248 products at HS 6-digit level.
2. This relatively small category is made up of 6 products, only one of which is in the CLEG.
3. To ensure comparability, United Kingdom data are excluded from the UN Comtrade EU aggregate prior to Brexit.
4. Differences in relative prices could explain some of the decline in shares. Global manufactured goods prices (excluding food and fuel) rose around 11% cumulatively between 2018 and 2022. Whilst there is no index of traded goods in environmental goods, the price of environmental technologies is estimated to have declined by around 10% between 2018 and 2022 (IEA, 2023a).

Concerted efforts to support the digital delivery of services could help to overcome some of the growing risks to services trade – such as the rise in limitations on the business activities of foreign companies, foreign direct investment, and the movement of people. Raising digital connectivity between countries can support trade in services as well as in goods (Figure 1.30, Panel B). However, digital services policy remains fragmented and increasingly restrictive, limiting the benefits of digitalisation. The OECD Digital Services Trade Restrictiveness Index shows that trade restrictions introduced in 2022 particularly affected access to communication infrastructure, the movement of information across networks and the lack of pro-competitive regulations (OECD, 2023f). Governments need to find an appropriate balance between safeguards and ensuring adequate competition in digital services. A set of common, predictable standards for cross-border data flows, privacy and consumer protection, where international agreements are lagging other digitally-related services, would have significant knock-on benefits for trade in services.

**Figure 1.30. Reducing services and digital regulation would boost trade growth**



Note: Panel A: OECD Service Trade Restrictiveness Index. The OECD aggregate is a simple average of all OECD members. Panel B. Values show the estimated impact of a 1% improvement in bilateral digital connectivity on international trade by sector.

Source: OECD (2023e), OECD Services Trade Restrictiveness Index: Policy Trends up to 2023, OECD Publishing, Paris; and López González, J., S. Sorescu and P.Kaynak (2023), "Of bytes and trade: Quantifying the impact of digitalisation on trade", OECD Trade Policy Papers, No. 273, OECD Publishing, Paris.

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### **Reforms are needed to strengthen the climate transition**

Governments face significant medium and longer-term structural challenges from the ongoing decline in potential output growth, ageing populations, the climate transition, digitalisation, and the AI revolution. The 2023 edition of *Going for Growth* (OECD, 2023d) provides country-specific advice to help achieve stronger, more inclusive and resilient growth. Specific reform priorities differ by country, and well-designed policy packages will be needed to address the key challenges. However, securing faster progress towards decarbonisation, strengthening product market competition and contestability, enhancing skills, removing obstacles to the reallocation of labour and capital towards more productive firms, and improving the design and management of social protection programmes are key policy needs in most economies. Finding an appropriate balance between the need for resilient supply chains and the opportunities available to reinvigorate global trade would also strengthen growth and incomes.

Enhanced multilateral co-operation is required to help meet the common challenge of the climate transition. The current policies in place may not lower global greenhouse gas emissions before 2030 (IEA, 2022), making the goal of net-zero emissions by mid-century difficult to attain. Reaching that goal requires structural changes in the economy and will entail substantial reallocation of workers and capital from emission-intensive activities towards greener activities. Accelerating the pace of decarbonisation will require ambitious packages of new policy measures, and action in three major areas: strengthening green investment and innovation; increasing the scope and level of carbon pricing; and enhancing regulations, institutions and standards to enable emission reductions.

- Additional public and private investment in clean energy technologies is needed in all economies. The International Energy Agency (IEA) estimates that investment in clean energy technologies needs to more than double from an estimated USD 1.8 trillion in 2023 to USD 4.5 trillion by 2030 (IEA, 2023b). Governments can foster the needed acceleration by strengthening access to the supply of critical minerals and other products for clean energy investments, and making tax, price and regulatory changes that send clear signals to private investors about the future demand for clean energy technologies. Direct public investment, including support for innovation, also has a clear role to play. Stronger participation by institutional investors in areas such as green infrastructure financing could also support investment given limited fiscal space in many countries.
- A clear and predictable trajectory for the price of carbon would help to incentivise mitigation and provide a clear signal to investors about the long-run returns from investing in low-carbon technologies (OECD, 2021). Strong and stable price signals are necessary but still lacking in most countries. Alongside this, recycling the revenue raised from carbon pricing would offer opportunities for governments to reduce distortionary taxation and counter the adverse distributional effects of a higher carbon price (D’Arcangelo et al., 2022).
- Large mitigation benefits can be reaped through a clear, predictable and carefully-designed regulatory environment and improved emissions standards (Berestycki et al., 2022; D’Arcangelo et al., 2023). These can directly reduce emissions and enhance the effect of pricing measures and the provision of low-carbon options. Regulations such as requirements for energy renovation, emissions tracking and green certification should be strengthened to facilitate mitigation while minimising costs. In some countries, reducing or removing regulatory barriers would facilitate the expansion of renewable energy.

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

Fiscal policy settings for 2024-25 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. Unless otherwise announced, the phasing-out of any remaining energy-related support measures is assumed to be completed by end-2024 at the latest.

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, and 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 2023.

The projections assume unchanged exchange rates from those prevailing on 10 November 2023: one US dollar equals JPY 151.4, EUR 0.94 (or equivalently one euro equals USD 1.07) and 7.29 renminbi.

The price of a barrel of Brent crude oil is assumed to remain constant at USD 85 until the end of 2025. The TTF natural gas price is assumed to remain constant at EUR 45 MW/h until the end of 2025. Other commodity prices are assumed to be constant over the projection period at their average levels from August 2023.

The cut-off date for information used in the projections is 23 November 2023.

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.

# Annex 1.B. Addressing high public debt: lessons from past debt reduction episodes

## Introduction

Governments face rising fiscal pressures from high debt burdens, increasing debt service costs and additional spending on ageing populations, the climate transition and defence. In dealing with these significant fiscal challenges, governments can potentially draw on the lessons from past episodes in which countries have achieved large and sustained reductions in their debt-to-GDP ratios and changed the composition of public expenditure. The work in this annex builds on earlier studies by the Secretariat (Cournède et al., 2014; Bloch et al., 2016; Rawdanowicz et al., 2021) and examines the drivers of debt reduction episodes in OECD countries since the late 1970s, and the evolution of different revenue and expenditure components during these episodes.

In all, 34 debt reduction episodes since the late 1970s are identified, with 25 OECD member states having experienced at least one episode during this period. On average, these debt-reduction episodes have lasted 9 years, with a total decline of 27 percentage points in the debt-to-GDP ratio.

The key findings are that reductions in the debt-to-GDP ratio have mainly hinged on achieving and sustaining a primary surplus over several years, largely via expenditure restraint, and on favourable cyclical conditions and low interest rates. Declines in the primary expenditure-to-GDP ratio during the episodes have often entailed large cuts in subsidies and certain non-social transfers as a share of GDP, rather than education, healthcare and public investment, as well as containment of spending on pensions. These drivers of debt ratio reductions may be difficult to emulate in the near future (Arslanalp and Eichengreen, 2023), but lessons from past sustained shifts in the composition of expenditure remain highly relevant for present challenges.

## Identifying debt reduction episodes and the key drivers of debt dynamics

Debt reduction episodes are defined as ones that persist for a minimum of five years and bring down the gross general government debt-to-GDP ratio by at least 10 percentage points. Temporary and small debt ratio reversals are allowed from one year to the next during such episodes, but all episodes start in a year after the peak in the debt ratio and end when the debt-to-GDP ratio bottoms out.<sup>1</sup> The analysis covers the periods from the late 1970s to 2019, though data availability is limited for some OECD countries.

Accounting decompositions of changes in the debt-to-GDP ratio ( $d$ ) typically consider three components (Rawdanowicz et al., 2021): the primary balance-to-GDP ratio  $b$  (hereafter the “primary balance”), the interaction of debt and the differential between the implicit interest rate on debt ( $i$ ) and GDP growth  $g$  (the so-called “snowball effect”), and a residual stock-flow adjustment as a share of GDP ( $a$ ). The latter summarises changes in gross debt unaccounted for by the budget balance.<sup>2</sup>

$$\Delta d_t = \frac{i_t - g_t}{1 + g_t} d_{t-1} - b_t + a_t \quad [1]$$

<sup>1</sup> Reversals cannot exceed 2 years or a cumulative 5 percentage points.

<sup>2</sup> Examples are valuation effects and below-the-line operations. The stock-flow adjustment also includes, with a negative sign, the interest receipts of general government. This helps to explain why it makes the debt ratio fall in about two thirds of the episodes.

Equation [1] can also be written in terms of annual averages over the length of each debt reduction episode, denoted as lasting from year 1 to year  $k$ :

$$\frac{d_k - d_0}{k} = \frac{\sum_{t=1}^k \frac{i_t - g_t}{1 + g_t} d_{t-1}}{k} - \frac{\sum_{t=1}^k b_t}{k} + \frac{\sum_{t=1}^k a_t}{k} \quad [2]$$

The average primary balance over each debt reduction episode in [2] can be further decomposed into the initial balance at the time when the debt ratio peaks (year 0) and the average primary balance change over the length of the episode relative to the initial value. Likewise, the aggregate snowball effect can be split to show separate impacts due to the real interest rate ( $r$ , with inflation ( $\pi$ ) measured by the GDP deflator) and real GDP growth ( $g^*$ ).

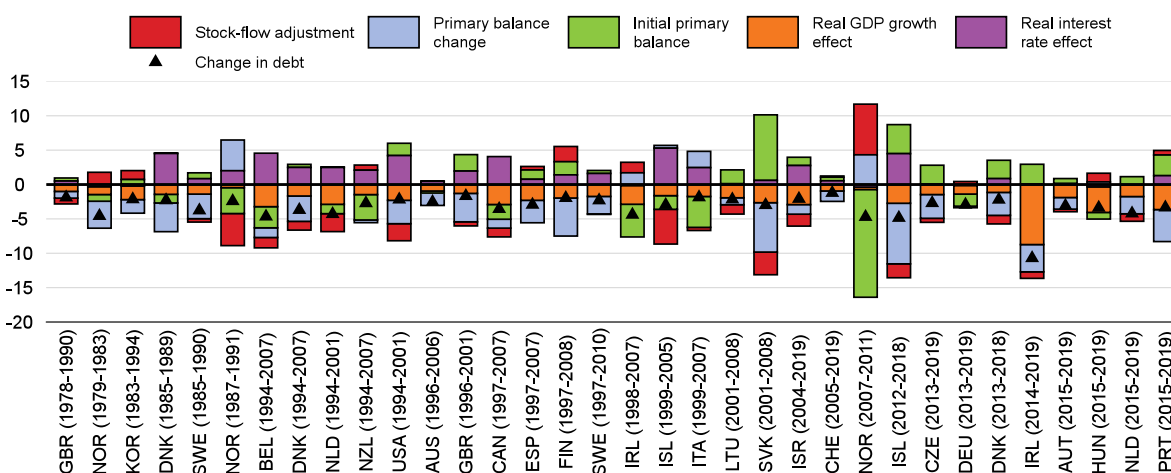
$$\frac{d_k - d_0}{k} = \frac{\sum_{t=1}^k \frac{r_t(1+\pi_t)}{1+g_t} d_{t-1}}{k} - \frac{\sum_{t=1}^k \frac{g_t^*(1+\pi_t)}{1+g_t} d_{t-1}}{k} - b_0 - \left( \frac{\sum_{t=1}^k b_t}{k} - b_0 \right) + \frac{\sum_{t=1}^k a_t}{k} \quad [3]$$

The decomposition of each debt reduction episode is shown in Figure 1.B.1. This highlights two key factors:

- In all but three episodes the primary balance is on average in surplus, thus contributing to a reduction in the debt ratio. This is often (in around 80% of the episodes) due to improvements in the primary balance during the episode itself and, less frequently (in about 40% of the episodes), to a positive starting value of the primary balance.
- In about two thirds of the episodes, and in all but one of the 14 episodes that have begun since the year 2000, the snowball effect contributes positively to debt reductions. GDP growth has on average tended to exceed potential,<sup>3</sup> and the real interest rate has often been only marginally positive or even negative.

### Annex Figure 1.B.1. Decomposition of the average annual change in the debt ratio during debt reduction episodes

Per cent of GDP



Note: The chart shows the average annual change in the debt ratio over the length of each episode and its decomposition according to equation [3] in the text. Episodes are ordered chronologically by starting year. A negative bar indicates that the particular factor has helped to lower debt over the period shown.

Source: OECD Economic Outlook 113 database; and OECD calculations.

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<sup>3</sup> The output gap has almost always improved relative to that prevailing when the debt ratio peaked.

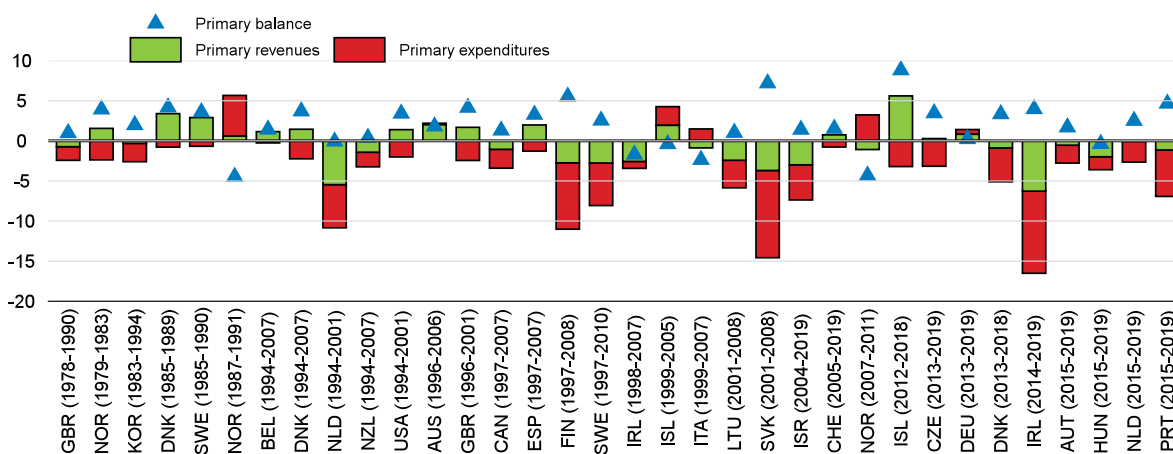
### The evolution of the primary balance during debt reduction episodes

Improvements in the primary balance during debt reduction episodes have clearly been an important source of debt ratio reductions. This raises the question of whether such improvements have occurred mainly through lower primary expenditure to GDP, or from increases in primary revenue to GDP. The separate contributions from expenditure and revenue to the identified change in the primary balance during the 34 debt reduction episodes are shown in Figure 1.B.2.

- The major source of the improvements in the primary balance has been a decline in the share of primary expenditure in GDP. Such declines have occurred in over 80% of the 34 debt reduction episodes.
- Increases in the primary revenue-to-GDP ratio have occurred in fewer than half of the debt reduction episodes, and mostly for episodes that began in the 1980s and 1990s.


### Annex Figure 1.B.2. Primary expenditure restraint has often taken place during debt reduction episodes

Changes in ratios to GDP, percentage points, average over each debt reduction episode



Note: The chart shows the average annual change in the primary balance over the length of each episode relative to its initial value and its decomposition into the changes in primary revenue and primary expenditure. The change in the primary balance (triangles) is the same as in Figure 1.B.1 (blue bars), with inverted sign (hence a positive value now indicates an improvement which helps to lower debt). Episodes are ordered chronologically by starting year.

Source: OECD Economic Outlook 113 database; and OECD calculations.

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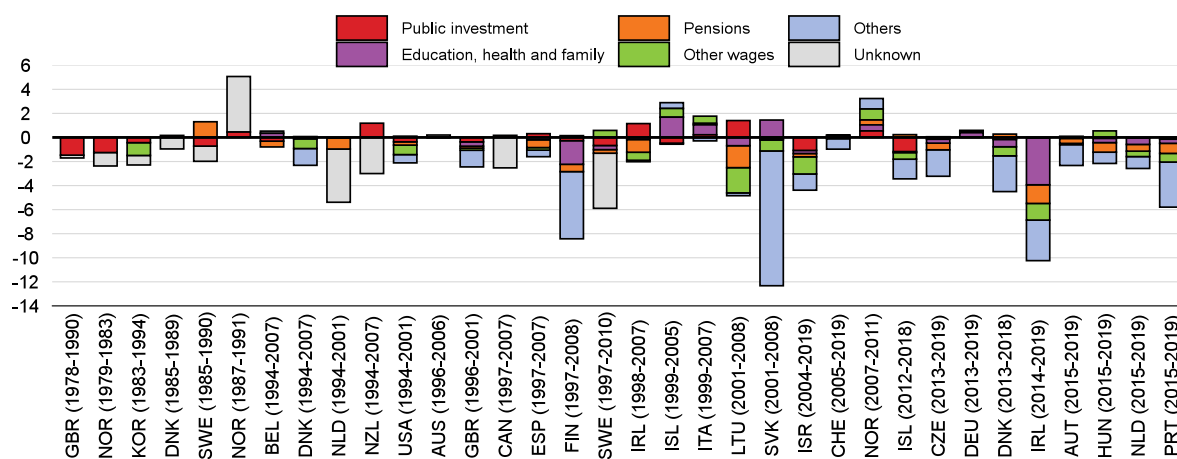
## Compositional changes during debt reduction episodes

The changes in primary expenditure and revenue during debt reduction episodes can be further decomposed to identify shifts in the composition of expenditure and taxation. On the expenditure side (Figure 1.B.3):

- Most categories of primary spending have declined relative to GDP during past debt reduction episodes. There are only a handful of examples in which either public investment or spending on education and health have been raised during debt reduction episodes.
- However, expenditure restraint has often been accompanied, and likely made more sustainable, by growth-friendly shifts in the composition of public spending. Public investment as a share of GDP did decline in about two-thirds of the episodes (23 out of 34), but cuts to investment were often proportionally smaller than other expenditure items. In contrast, large reductions in public investment have often been found in consolidation episodes (Pina, 2016).
- Spending on education, health and family and children, generally regarded as growth- and equity-friendly (Cournède et al., 2014; Fournier and Johansson, 2016), was also preserved to a larger extent than spending on pensions and the bulk of non-education, non-health wages and intermediate consumption. Reductions in the latter types of spending as a share of GDP have often been sizeable.

### Annex Figure 1.B.3. Growth-friendly expenditure has typically been spared during debt reduction episodes

Changes in ratios to GDP, percentage points, average over each debt reduction episode



Note: The chart decomposes the average annual change in primary expenditure as a share of GDP over the length of each episode relative to its initial value (red bars in Figure 1.B.2) into several expenditure components as defined in the OECD Public Finance Dataset. "Education, health and family" denotes most current spending devoted to education, health care and, within social protection, family and children (expenditure items 1, 2 and 7 in Bloch et al., 2016). "Other wages" includes most wages, as well as intermediate consumption, in functions other than education and health (expenditure item 3 in Bloch et al., 2016). "Others" includes unemployment benefits, sickness and disability spending, subsidies, other primary expenditure (expenditure items 5, 6, 8 and 10 in Bloch et al., 2016, item 10 being adjusted to include non-interest property income paid) and, in some cases, a statistical discrepancy term. In some earlier episodes not all components can be identified due to data limitations. Episodes are ordered chronologically by starting year.

Source: OECD Economic Outlook 113 database; OECD Public Finance Dataset; and OECD calculations.

StatLink  <https://stat.link/em4b28>

- Declines in the GDP share of the remainder of public expenditure, including subsidies, unemployment, sickness and disability benefits, non-social current transfers and capital transfers were often the largest factor behind the lower primary expenditure-to-GDP ratio.<sup>4</sup> Many of these items are not growth-enhancing, though some can be very important for incomes, particularly in poorer households.

On the revenue side (Figure 1.B.4):

- Corporate income taxes as a share of GDP increased in almost 90% of all debt reduction episodes, often in tandem with improved cyclical conditions. In 13 of the 15 episodes with an increase in the primary revenue-to-GDP ratio, the contribution of corporate income taxes to that increase was proportionally larger than its initial share in total primary revenue.
- In contrast, an increase in other direct taxes (personal income taxes and social security contributions) as a share of GDP occurred in less than half of all debt reduction episodes. In some cases, debt reductions occurred alongside sizeable reductions in other direct taxes as a share of GDP.
- The contributions of changes in the GDP shares of indirect and property tax revenues to the overall change in primary revenue have typically been relatively small. There have been few debt reduction episodes in which such taxes rose as a share of GDP.

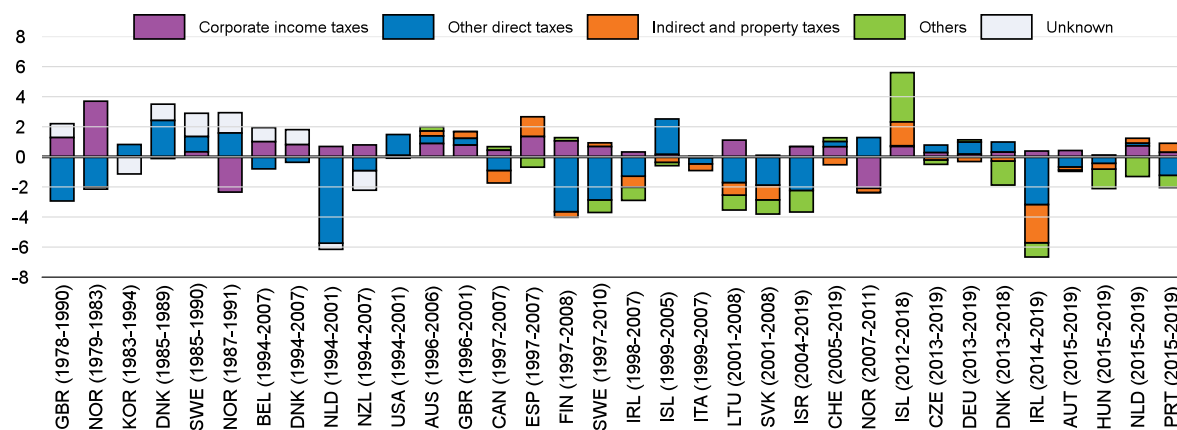
A positive differential between GDP growth and interest rates cannot be relied upon to decrease the debt-to-GDP ratio in the coming years, and primary surpluses via expenditure restraint will not be easy to achieve (Arslanalp and Eichengreen, 2023), particularly when there are demands to raise public investment. This reflects the multiple future spending pressures governments face. Reductions in the debt ratio may thus be harder to achieve in the coming decade than in the past. Nonetheless, past debt reduction episodes illustrate that it is possible to make significant savings in spending items which often harm growth, such as subsidies and certain transfers. In the current context, where the composition of public expenditure needs to change to address new challenges, that lesson remains highly relevant. Any such changes will need to be accompanied by improvements to the overall targeting and design of spending programmes to maintain support for those who need it most.

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<sup>4</sup> Subsidies and non-social current transfers are also the items which account for the bulk of non-targeted expenditure-side energy support (Hemmerlé et al., 2023; Eurostat, 2023).


## Annex Figure 1.B.4. Corporate income taxes have generally increased during debt reduction episodes

Changes in ratios to GDP, percentage points, average over each debt reduction episode



Note: The chart decomposes the average annual change in primary revenue as a share of GDP over the length of each episode relative to its initial value (green bars in Figure 1.B.2) into several revenue components as defined in the OECD Public Finance Dataset. “Other direct taxes” denotes revenues from personal income taxes and social security contributions (revenue items 1 and 2 in Bloch et al., 2016). “Indirect and property taxes” group revenue items 4-7 in Bloch et al., 2016. “Others” includes revenues from sales of goods and services (mainly user charges), other primary revenue (revenue items 8 and 9 in Bloch et al., 2016, item 9 being adjusted to include non-interest property income received) and, in some cases, a statistical discrepancy term. In some earlier episodes not all components can be identified due to data limitations. Episodes are ordered chronologically by starting year.

Source: OECD Economic Outlook 113 database; OECD Public Finance Dataset; and OECD calculations.

StatLink  <https://stat.link/x87bdf>



## **2. Developments in individual OECD and selected non-member economies**

# Argentina

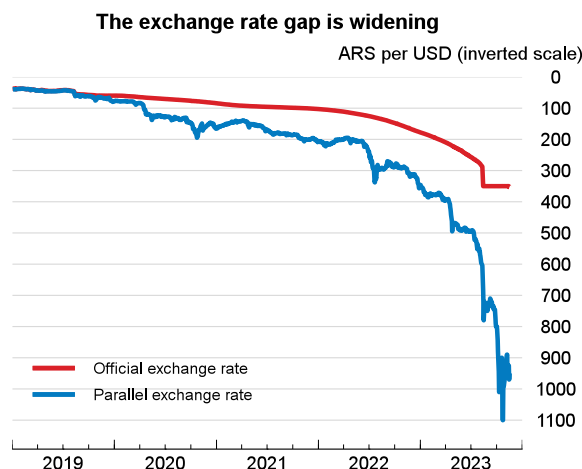
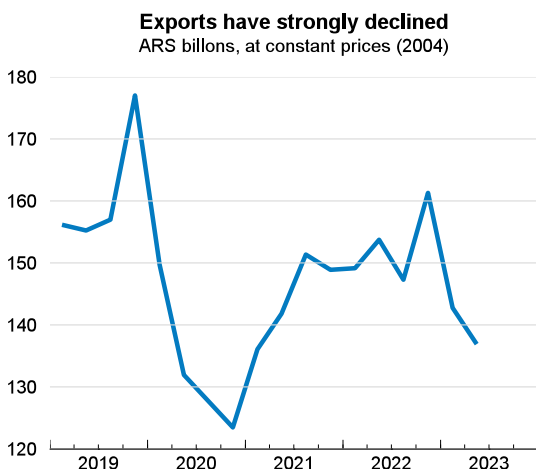
GDP is projected to contract by 1.8% in 2023 and by 1.3% in 2024, before rising by 1.9% in 2025. Tight capital controls, rising inflation and high policy uncertainty will further constrain consumption and investment in the short term. Exports are set to recover in 2024, following a severe drought in 2023. Inflation has surpassed 100% and will continue to rise in the near term due to expectations of a currency devaluation.

Substantial fiscal consolidation will be needed to resolve severe macroeconomic imbalances. A recently-enacted fiscal stimulus package will further worsen fiscal outcomes and make it difficult to attain short-term targets. Stabilising the macroeconomic situation and raising female labour force participation would lay the basis for higher medium-term growth and for reversing the rise in poverty.

## Extremely high inflation is weighing on growth

Output contracted in the second quarter of 2023, mainly driven by a devastating drought that reduced exports. Following a recovery of the agricultural sector in the third quarter, short-term indicators point to a further contraction from the fourth quarter of 2023, mainly due to heightened policy uncertainty and the impact of the high inflation on purchasing power. A still-resilient labour market, with unemployment at 6.2% in the second quarter of 2023, has supported consumer confidence so far. However, informality has increased, approaching 40% of the labour force. Headline inflation rose to 143% in the year to October, the highest inflation rate since the 1991 hyperinflation era.

## Argentina



Note: Exports are seasonally adjusted.

Source: Instituto Nacional de Estadísticas y Censos; OECD Exchange rate database; Central Bank of Argentina; and Ambito.com.

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## Argentina: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices ARS billion	Percentage changes, volume (2004 prices)				
<b>Argentina</b>						
<b>GDP at market prices</b>	27 209.8	10.7	5.0	-1.8	-1.3	1.9
Private consumption	17 878.1	10.4	9.7	0.8	-1.5	1.7
Government consumption	4 591.1	6.3	1.9	3.5	0.0	0.2
Gross fixed capital formation	3 886.2	33.8	11.1	0.7	-0.7	2.2
Final domestic demand	26 355.5	13.0	8.6	1.2	-1.1	1.5
Stockbuilding <sup>1</sup>	36.1	-0.3	-1.0	0.7	-0.2	0.0
Total domestic demand	26 391.6	13.3	7.8	1.8	-1.8	1.6
Exports of goods and services	4 518.3	8.5	5.8	-8.2	4.8	4.1
Imports of goods and services	3 700.1	20.4	17.9	7.1	1.0	2.5
Net exports <sup>1</sup>	818.2	-1.4	-1.6	-2.4	0.4	0.1
<i>Memorandum items</i>						
GDP deflator	—	53.8	69.5	125.4	140.6	52.6
Consumer price index	—	48.0	72.4	124.0	157.1	62.4
Current account balance (% of GDP)	—	1.3	-0.5	-3.2	-1.3	-0.8

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

Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/219elg>

The recent increase in oil and gas production in the Vaca Muerta field could turn Argentina into a net energy exporter in the short term. Commodity sectors will attract foreign direct investment, although capital inflows remain constrained by tight capital controls, multiple exchange rates and policy uncertainty. For the moment, funding provided by the International Monetary Fund (IMF) will be the main source of external financing. Depleted foreign exchange reserves are increasingly putting pressure on the public finances, the external account, and the overall economy.

## Tight macroeconomic policies will be required in the near term

The new government from December 2023 will need to consolidate public finances to rebalance the economy. A recently-launched fiscal support plan contained a combination of subsidies for workers, further income tax exemptions and credit relief, in an effort to protect households against high inflation. This temporary fiscal expansion will further weaken public finances, already strained by weak export tax revenues. The central bank raised the monetary policy rate twice in a row from 97% to 133% in response to the currency devaluation in the wake of the August primary elections. Given the recent acceleration of inflation, the policy rate is assumed to remain high until 2024, when it will start to fall gradually. Continuous and decisive reductions in monetary financing will be key to stabilise the economy, and this will also require further fiscal restraint.

## Growth will contract in 2023 and 2024 in an uncertain environment

The economy will contract by 1.8% in 2023 and by 1.3% in 2024 and then gradually recover to growth of 1.9% in 2025. High inflation, fiscal consolidation and tight financial conditions will all weigh on consumption during 2024, while low confidence levels and heightened political uncertainty will continue to hold back investment. A gradual upturn is projected for 2025 as the macroeconomic situation improves and exports recover. Inflation is projected to remain high in 2023 and 2024, driven by high currency devaluation expectations and the gradual removal of many currency controls, but could subside in 2025. Both short-

and medium-term risks are tilted to the downside. Low foreign reserves, tight currency restrictions and large volumes of outstanding central-bank bonds, in a context of elevated interest rates, could lead to a further currency devaluation, spiralling inflation, and solvency concerns. Moreover, the need to reduce public spending relatively quickly amid mounting social pressures could lead to political instability. On the upside, setting up a solid stabilisation plan could lead to stronger confidence in economic policymaking, reduce pressure on the exchange rate and attract foreign capital.

### **Supporting more sustainable growth**

Given the ageing population, long-term growth will hinge on productivity gains. These could be bolstered by stronger competition and less cumbersome regulations. Female labour force participation is well below developed countries and raising it would allow stronger per-capita income growth. Enhancing social protection through more effective social spending could help to reduce poverty and inequalities, as poverty affects more than 40% of the population. In light of high labour informality, improving incentives for formal job creation through lower non-wage labour costs and labour market reforms would improve equity and also strengthen productivity.



# Australia

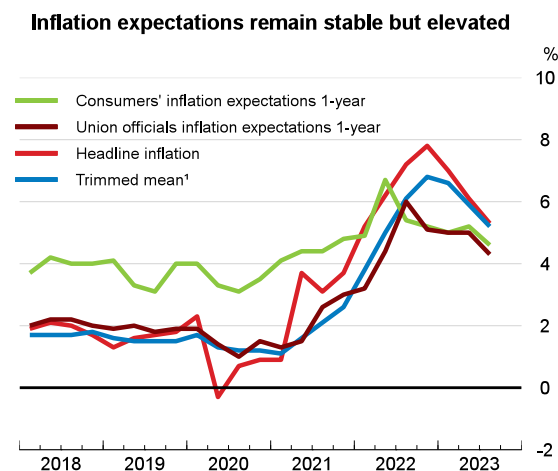
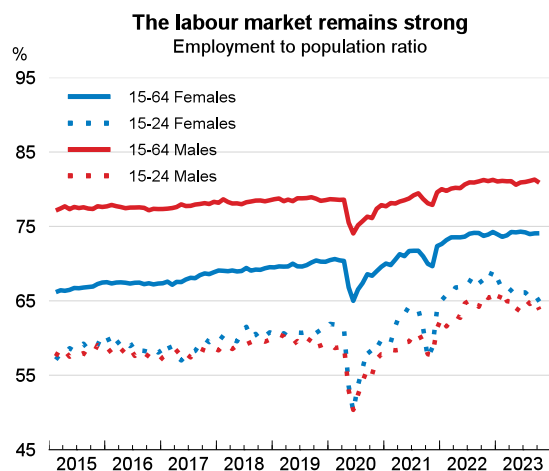
Real GDP growth is projected to slow from 1.9% in 2023 to 1.4% in 2024 before recovering to 2.1% in 2025. The accumulated impact of higher interest rates and cost of living pressures will damp spending by households and businesses over the coming year, though this will be partly offset by continued strong working-age population growth and the ongoing recovery in education and tourism exports. The unemployment rate is projected to rise moderately, reaching 4.4% by mid-2025. Inflation will moderate, aided by abating global inflationary pressures, though inflation of some services components is anticipated to remain elevated throughout 2024.

Fiscal reforms are needed to improve the sustainability of the public finances. Reducing private pension tax breaks and increasing receipts from the goods and services tax would raise revenue as fiscal costs related to the ageing population and climate transition increase. Measures that improve the efficiency of public spending, including encouraging more patient care in primary care settings and preventive health policies, are also a priority.

## Consumption has slowed but labour market conditions remain firm

Economic growth has slowed, with weaker household consumption, high inflation and tightening financial conditions. Nonetheless, labour market conditions remain firm, with the employment to population ratio well above pre-pandemic levels. Public investment has accelerated and there are signs that dwelling approvals have stabilised in recent months after declining over the past year. Inflation, although still high, has peaked, with the CPI rising 5.4% over the year to the third quarter of 2023. The housing component has made a particularly strong contribution to year-ended inflation. One-year-ahead inflation expectations of consumers and union officials have eased, though they remain above the Reserve Bank of Australia's 2-3% target band.

### Australia



1. The trimmed mean is the average rate of inflation after removing the items with the largest price changes (positive or negative). It is the weighted average of the middle 70% of items.

Source: OECD Labour Force Statistics; and Australian Bureau of Statistics.

## Australia: Demand, output and prices

	2020	2021	2022	2023	2024	2025
Australia	Current prices AUD billion	Percentage changes, volume (2020/2021 prices)				
<b>GDP at market prices</b>	1 972.9	5.2	3.7	1.9	1.4	2.1
Private consumption	1 011.5	5.1	6.4	1.7	1.2	1.9
Government consumption	450.2	5.4	5.3	0.9	1.0	0.8
Gross fixed capital formation	442.1	10.6	1.1	0.1	0.8	1.3
Final domestic demand	1 903.8	6.4	4.9	1.1	1.0	1.5
Stockbuilding <sup>1</sup>	- 2.6	0.6	0.4	-0.2	-0.1	0.0
Total domestic demand	1 901.1	7.1	5.2	0.9	0.9	1.5
Exports of goods and services	436.4	-2.1	3.4	9.3	4.5	5.0
Imports of goods and services	364.7	5.6	12.8	4.2	3.0	3.2
Net exports <sup>1</sup>	71.8	-1.5	-1.5	1.6	0.6	0.7
<i>Memorandum items</i>						
GDP deflator	–	5.5	7.9	3.6	3.0	2.7
Consumer price index	–	2.8	6.6	5.6	3.4	2.8
Core inflation index <sup>2</sup>	–	2.4	5.9	5.9	3.5	2.8
Unemployment rate (% of labour force)	–	5.1	3.7	3.7	4.1	4.3
Household saving ratio, net (% of disposable income)	–	14.7	8.0	4.3	5.3	5.6
General government financial balance (% of GDP)	–	-4.8	-1.8	-0.8	-1.2	-1.0
General government gross debt (% of GDP)	–	63.6	56.6	57.3	58.4	59.2
Current account balance (% of GDP)	–	3.0	1.0	1.8	2.3	2.9

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 114 database.

StatLink  <https://stat.link/p8zjo3>

The slowdown in the Chinese economy has had limited impact so far on Australian exports. Despite weaker growth in the property sector, demand for Australian bulk commodity exports has been buoyed by ongoing infrastructure and manufacturing investment in China. Demand for Australian thermal coal has also been supported over the past year by the lifting of Chinese trade restrictions in the first quarter of 2023.

## Monetary policy has tightened further and the fiscal deficit is narrowing in 2023

The Reserve Bank of Australia resumed tightening of monetary policy at the November meeting, raising the official cash rate by 25 basis points to 4.35% after holding the policy rate steady since June 2023. The projections assume that the cash rate will be held at this restrictive level until inflation is clearly declining to the target band, with 75 basis points of interest rate cuts assumed between the third quarter of 2024 and end-2025. The underlying budget deficit is projected to narrow in 2023, largely owing to a spike in tax receipts from businesses and households. Fiscal policy is assumed to have a slightly contractionary influence on economic growth in 2024 and 2025. The Commonwealth Government's Energy Price Relief Plan, which set a cap on wholesale coal and gas prices and provided targeted energy bill relief, is expected to reduce headline inflation by  $\frac{3}{4}$  of a percentage point by the second quarter of 2024.

## Economic growth will continue to slow

Economic growth is projected to slow from 1.9% in 2023 to 1.4% in 2024, before recovering to 2.1% in 2025. Higher interest rates and cost of living pressures will damp spending by households with few accumulated savings and weigh on housing investment. Continued strong working-age population growth and higher exports as foreign student arrivals further recover will partly offset these headwinds. As GDP growth slows, the unemployment rate is projected to start rising, reaching 4.4% in 2025. Inflation will moderate, aided by abating global inflationary pressures particularly for goods, and is expected to fall to the top of the RBA target band by early 2025. More persistent inflationary pressures or a sharper slowdown in China than expected pose downside risks to GDP growth.

## Fiscal reforms can help accommodate ageing costs

Further fiscal reforms are needed to improve the sustainability of the public finances given that costs related to population ageing and the climate transition will intensify. Annual fiscal costs from health and long-term care are estimated to increase by 0.8% of GDP between 2023 and 2040. Raising further revenue, such as through reducing private pension tax breaks and increasing receipts from the goods and services tax, should be considered. There are also potential savings on the spending side, including by encouraging more patient care in primary care settings and preventive health policies. Structural reforms that support medium-term economic growth are also needed. Immigration will continue to play a key role in the labour market, but the composition of the skilled migrant intake needs to be more responsive to changes in the skill needs of industry, including through better use of timely and granular data and the views of employers.

# Austria

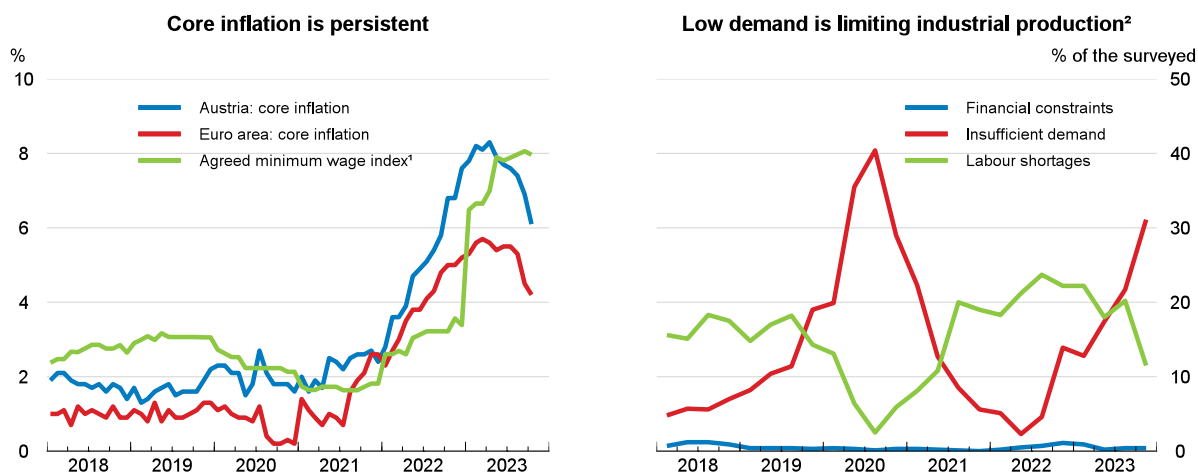
Economic activity has slowed significantly and is expected to contract by 0.4% in 2023. High inflation is weighing on consumption, rising interest rates and labour shortages are damping investment, and external demand has weakened. Growth will slowly pick up to 0.6% in 2024 and 1.5% in 2025. Higher real wages will support consumption in 2024. Investment will remain subdued because of elevated borrowing costs and rising labour costs, and export demand will be held back due to global macroeconomic tightening. Unemployment will increase slightly.

The fiscal stance will be mildly restrictive in 2023 and 2024. The phasing out of crises-related support is largely offset by new discretionary measures in 2024. Higher borrowing costs and relatively high public debt will require a stronger consolidation by reducing expenditures when growth picks up. Activating existing labour reserves, notably by raising the labour force attachment of women and older cohorts, could support medium-term growth.

## The economy will contract in 2023

The economy contracted in the first half of 2023 and high-frequency indicators suggest that output will remain weak in the second half. Lower real wages, with price inflation pushed up by higher prices for energy, and restaurants and hotels, weigh on consumption. Tighter financial conditions and labour shortages are slowing investment and construction. External demand has also been weak in the second quarter. Inflation fell to 4.9% in October but remains higher than elsewhere in Europe because of less direct intervention on energy prices and the importance of catering and accommodation services. Though the unemployment rate is still at a historically low level, the labour market is starting to ease, especially in manufacturing.

## Austria



1. The agreed minimum wage index measures changes in minimum wages and salaries determined by collective agreements or legislation.

2. The surveyed firms respond to the question: "What main factors are currently limiting your production?"

Source: OECD Consumer Prices database; Statistik Austria; and EU harmonised business surveys.

## Austria: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Austria</b>						
<b>GDP at market prices*</b>	380.3	4.4	4.8	-0.4	0.6	1.5
Private consumption	189.7	4.0	5.8	0.1	1.6	1.9
Government consumption	80.3	7.7	0.1	-0.9	-1.0	0.7
Gross fixed capital formation	95.2	6.0	0.3	-2.2	-1.4	0.8
Final domestic demand	365.2	5.3	3.1	-0.7	0.3	1.4
Stockbuilding <sup>1</sup>	3.1	1.2	-0.3	-1.1	0.4	0.0
Total domestic demand	368.3	6.5	2.6	-1.8	0.8	1.4
Exports of goods and services	195.5	9.4	11.8	1.9	2.8	2.8
Imports of goods and services	183.4	14.0	8.1	-0.9	3.5	2.7
Net exports <sup>1</sup>	12.0	-1.9	2.1	1.7	-0.3	0.1
<i>Memorandum items</i>						
GDP deflator	–	2.1	5.3	7.3	3.2	2.2
Harmonised index of consumer prices	–	2.8	8.6	7.7	3.9	2.5
Harmonised index of core inflation <sup>2</sup>	–	2.3	5.1	7.4	4.2	2.3
Unemployment rate (% of labour force)	–	6.2	4.7	5.1	5.5	5.4
Household saving ratio, net (% of disposable income)	–	11.2	9.2	7.7	7.7	7.8
General government financial balance (% of GDP)	–	-5.8	-3.5	-2.6	-2.5	-2.5
General government gross debt (% of GDP)	–	105.5	84.0	83.8	84.7	85.6
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	82.5	78.4	78.2	79.2	80.0
Current account balance (% of GDP)	–	1.6	-0.3	2.8	2.1	2.1

\* 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 114 database.

StatLink  <https://stat.link/mexb60>

Private debt is relatively low in Austria, so that the economy is less sensitive than other European countries to the tightening of financial conditions. However, higher interest rates can pass through quickly to indebted corporations and households due to a prevalence of variable-interest loans. Credit standards have stabilised but demand for business and housing loans has been gradually falling in the last year; and real house prices have fallen faster than elsewhere in the OECD after a steep increase in previous years. As a small open economy, Austria is also exposed to the recent slowdown in global merchandise trade but has benefitted from the post-pandemic pick-up in tourism.

## Fiscal support will slowly decline in 2024

The budget deficit is expected to narrow marginally from 2.6% of GDP in 2023 to 2.5% in 2024 and 2025. On the expenditure side, remaining Covid-related expenses have largely been withdrawn. Price-relief measures will mostly expire by mid-2024. These include an electricity price brake for households (0.5% of GDP) expiring in mid-2024 and an energy cost subsidy for corporations (0.6% of GDP) expiring in 2023. However, those reductions will be offset by an increase in social benefits linked to past inflation, by additional discretionary measures to encourage e-mobility and support vulnerable groups, higher interest payments and the outlays induced by the new agreement on fiscal equalisation (0.3% of GDP in 2024). On the revenue side, rising revenues from carbon pricing and the withdrawal of temporary reductions in energy taxes are being offset by reductions in household and corporate income taxation. Robust consumption is supporting indirect tax revenues, though the economic slowdown weakens revenues from

income taxes and social contributions. The indexation of tax brackets and social benefits on past inflation aggravates the deficit ratio in 2024. Given low growth, the underlying fiscal stance will tighten by 0.8% of GDP in 2024 and will be mildly expansionary in 2025. The stable deficit combined with high nominal growth leads to a slight increase in the public debt ratio from 78.2% in 2023 to 80.0% in 2025.

### **The economy will recover only slowly**

Output will gradually recover and growth will reach 0.6% in 2024 and 1.5% in 2025, as the supply constraints contributing to inflation phase out and interest rates stop increasing. Household consumption will benefit from an improvement in real disposable income due to receding inflation and higher negotiated wages, which use inflation over the previous 12 months as a reference. Excess savings will be exhausted only at the end of 2025. Tighter financial conditions pass through to business investment in 2024, and the global macroeconomic tightening will damp export growth. The labour market will loosen, with unemployment projected to increase from 4.7% in 2022 to 5.5% in 2024. An easing of monetary policy rates and a global recovery will support growth above potential in 2025. Inflation will steadily decrease but remain high over the projection period, driven by sticky inflation in core services. Risks to the projections are skewed to the downside. The persistence of inflation will depend on the outcome of wage negotiations which began in the fall of 2023. With exports representing more than 50% of GDP, Austria is also susceptible to a further slowdown in global trade and external demand.

### **Structural reforms are needed for sustainable growth**

An ageing population will put gradually more pressure on the public finances. Fiscal costs related to ageing are expected to increase by 1% of GDP by 2030 and potentially 7% by 2060. Fiscal sustainability will require structural reforms of the pension system, such as linking retirement age to life expectancy while ensuring good working conditions at older age. Reforms that raise employment rates would have significant fiscal dividends. Better incentives to continue working at an older age would support employment of the elderly. Improving the quality of early child and elderly care services, and encouraging more men to take parental leave, would help raise full-time employment of women. The ongoing reduction in labour tax wedges will raise employment of low-skilled workers.

# Belgium

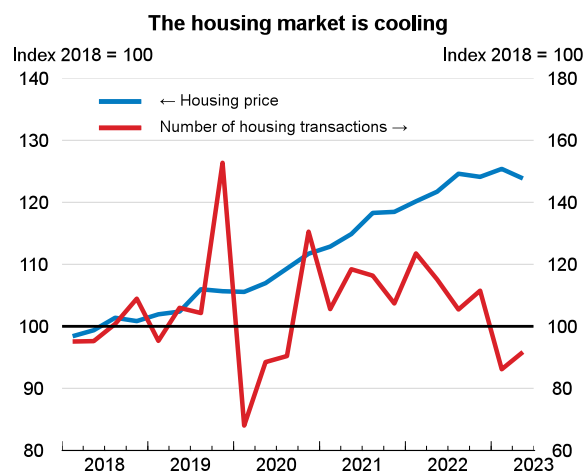
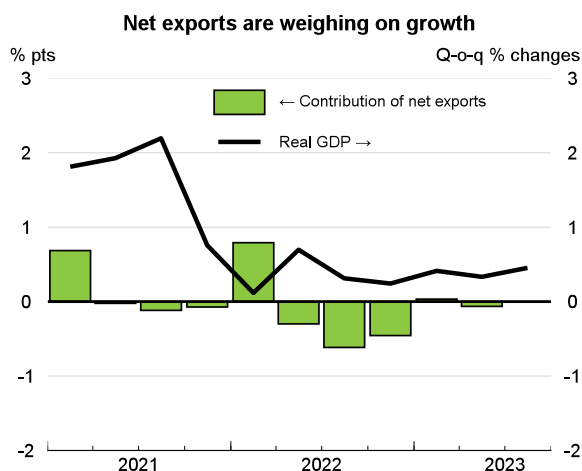
GDP growth is expected to weaken from 1.4% in 2023 to 1.1% in 2024, before increasing to 1.5% in 2025. Household consumption will slow as purchasing power is held back by slowing employment growth, while tight financing conditions restrain investment. Belgium is highly exposed to international economic conditions and a further loss of competitiveness due to wage growth. Headline inflation is projected to increase to 3% in 2024 as energy prices rise and core inflation stays high, before declining to 2.4% in 2025 as economic slack alleviates underlying inflationary pressures.

The fiscal stance is expected to be broadly neutral in 2024 and 2025. Given Belgium's high debt burden, a consolidation plan and expenditure rules are needed to ensure confidence in fiscal sustainability. Strengthening the taxation of personal capital income with a progressive tax rate schedule and a capital gains tax would reduce tax arbitrage opportunities. A credible long-term carbon pricing framework and improved coordination and coherence across federal and regional governments is required to promote green investment and diversification away from fossil fuels.

## Economic growth has slowed

Growth slowed to 0.5% in the third quarter of 2023, amid high inflation and borrowing costs, weakening international trade and high uncertainty. Household consumption has supported growth, partly due to automatic wage indexation and a robust labour market, but weak confidence has weighed on economic activity. Business confidence indicators have fallen during 2023 and higher borrowing costs have held back household residential investment, with mortgage demand at its lowest level since 2007. Annual headline inflation has fallen fast to -1.7% in October, mainly due to lower energy prices. Core inflation remains high at 6.4% in October, but is declining as raw material prices subside, supply chain problems ease, and second-round effects from wage indexation diminish.

## Belgium



Source: OECD Economic Outlook 114 database; and OECD National and Regional House prices and related indicators database.

## Belgium: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Belgium</b>						
<b>GDP at market prices</b>	460.7	6.9	3.0	1.4	1.1	1.5
Private consumption	227.5	6.3	3.2	1.4	1.5	2.1
Government consumption	112.4	5.2	4.2	0.4	1.2	1.6
Gross fixed capital formation	110.9	5.0	-0.2	4.3	1.2	1.5
Final domestic demand	450.9	5.7	2.6	1.9	1.4	1.8
Stockbuilding <sup>1</sup>	0.7	0.4	0.4	0.3	0.0	0.0
Total domestic demand	451.5	6.0	3.0	2.1	1.4	1.8
Exports of goods and services	362.3	13.9	4.9	-0.4	0.3	2.1
Imports of goods and services	353.1	13.0	4.9	0.3	0.7	2.4
Net exports <sup>1</sup>	9.2	0.9	0.1	-0.7	-0.3	-0.3
<i>Memorandum items</i>						
GDP deflator	–	3.2	5.9	4.0	2.7	2.0
Harmonised index of consumer prices	–	3.2	10.3	2.4	3.0	2.4
Harmonised index of core inflation <sup>2</sup>	–	1.3	4.0	6.1	3.5	2.4
Unemployment rate (% of labour force)	–	6.3	5.6	5.6	5.7	5.6
Household saving ratio, net (% of disposable income)	–	10.3	5.7	6.9	6.7	5.8
General government financial balance (% of GDP)	–	-5.4	-3.5	-4.9	-4.8	-5.0
General government gross debt (% of GDP)	–	129.3	104.2	105.3	107.4	109.8
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	108.0	104.3	105.4	107.5	110.0
Current account balance (% of GDP)	–	1.3	-1.0	-1.3	-1.1	-2.0

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 114 database.

StatLink  <https://stat.link/rzcnvh>

The slowdown in world trade has led to a significant decline in exports this year. Belgium has lost price competitiveness due to automatic wage indexation, though this is lessening as wages among neighbouring countries catch-up. Retail energy prices fell substantially; the average annual household bill had fallen 52% by August 2023 from its October 2022 peak. Belgian energy prices are now lower than in all neighbouring countries, with the exception of electricity prices in France. However, an increase in fuel prices is expected this winter as oil and gas prices rise. Natural gas accounts for almost 40% of Belgium's energy supply during peak winter months.

## The fiscal deficit is expected to rise

Financing conditions will remain tight for the government as well as for businesses and households. The fiscal deficit will widen in 2023 and remain large in 2024 and 2025 under current policies. The spring 2024 elections and subsequent coalition negotiations make near-term consolidation unlikely, with major reforms postponed for the next government. Sovereign bond yield spreads are nevertheless stable. Belgian government debt has a relatively long average maturity (just over 11 years) so higher yields transmit slowly to the average cost of debt servicing. Energy policy support measures were all terminated by July 2023, except for the VAT reduction on electricity and gas, which was made permanent. A new excise duty was introduced to partly compensate the revenue loss. Next Generation EU funding will support public investment with around EUR 4 billion to come.



## Economic activity will gradually recover

GDP growth is projected to slow to 1.1% in 2024, before picking up to 1.5% in 2025. Purchasing power will be held back by the ending of energy support measures and slowing employment growth. Lacklustre global trade and reduced cost competitiveness will drag on exports in the near term, while tight financing conditions will also hold back business and residential investment. Improving trade prospects next year alongside moderating labour cost growth suggest some export recovery from 2024, while the stabilisation and anticipated decline in mortgage rates should allow for a recovery in housing investment. Headline inflation is projected to rise to 3% in 2024 as energy prices increase again and core inflation stays high, before easing to 2.4% in 2025 as economic slack reduces underlying inflationary pressures. A slowdown in Belgium's main economic partners, alongside further losses in competitiveness and productivity, are risks to the outlook.

## Ensuring fiscal sustainability is key

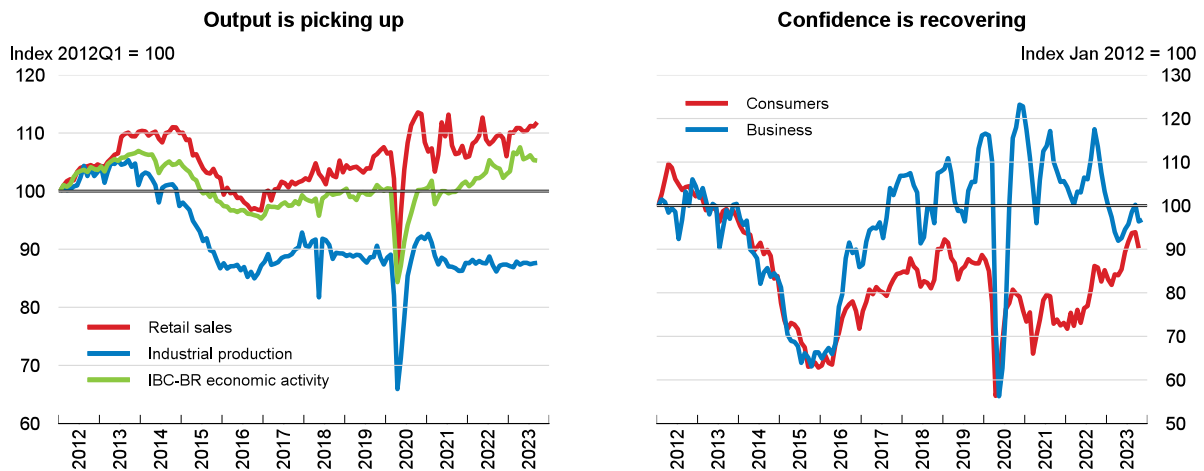
Government debt as a share of GDP (104.3% in 2022) continues to be among the highest in the European Union. Spending pressures from ageing-related costs and the climate transition call for substantial consolidation efforts to stabilise the debt-to-GDP ratio. Ageing-related fiscal pressures are expected to increase health care and pensions costs by 1% and 1.3% of potential GDP by 2040, respectively. The reformulation of EU fiscal rules will help. In addition, a medium-term consolidation strategy, based on spending reviews, is needed to reduce public indebtedness. Adding progressive taxation to all forms of capital income and a capital gains tax would help reduce tax arbitrage opportunities. The postponement of the phase-out of nuclear energy calls for clarity in the strategy to ensure long-term energy security, while a credible long-term carbon pricing framework would promote clean energy investment and diversification away from fossil fuels. Lastly, further removing barriers to competition by reforming complex regulatory, license and permit procedures in services would improve productivity and strengthen growth.

# Brazil

Real GDP is projected to grow by 3.0% in 2023, 1.8% in 2024 and 2.0% in 2025. Economic activity rebounded strongly in the first half of 2023 driven by an exceptional agriculture harvest and resilient household consumption. Despite tight financial conditions, household spending will remain strong due to buoyant employment growth, declining inflation, and higher social transfers. Private investment will recover slightly throughout 2024 as monetary policy eases. Though commodity prices are declining, agricultural products will drive a continued expansion of exports. Inflation has declined markedly over 2023 and will converge toward the target band during 2024.

Monetary policy easing started in August 2023. Real interest rates remain high, leaving room for continued reductions in policy rates over 2024 and 2025. Fiscal policy remains expansionary, but a gradual consolidation is expected in 2024 to achieve the 1% of GDP primary surplus target required by the new fiscal framework. Implementing the new fiscal framework will help to restore confidence and achieve a more consistent macroeconomic policy mix. Stronger infrastructure investment and the planned adoption of a unified value-added tax can boost potential growth. Expanding access to early childhood education would facilitate labour market participation for women and reduce gender disparities.

## Brazil 1



Source: CEIC; Banco Central do Brasil; and OECD calculations.

StatLink  <https://stat.link/Oqjlzu>

## Brazil: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices BRL billion	Percentage changes, volume (2000 prices)				
<b>Brazil</b>						
<b>GDP at market prices</b>	7 609.6	5.3	3.0	3.0	1.8	2.0
Private consumption	4 805.0	4.0	4.3	2.8	2.1	1.9
Government consumption	1 532.2	3.5	1.5	1.8	1.3	1.3
Gross fixed capital formation	1 260.2	16.6	0.8	-2.3	0.8	1.2
Final domestic demand	7 597.4	6.0	3.1	1.7	1.7	1.7
Stockbuilding <sup>1</sup>	- 33.9	0.6	-1.0	0.3	0.1	0.0
Total domestic demand	7 563.6	6.5	2.1	1.9	1.9	1.7
Exports of goods and services	1 252.0	6.5	5.9	7.2	4.0	3.7
Imports of goods and services	1 206.0	12.1	0.6	2.4	4.6	2.1
Net exports <sup>1</sup>	46.0	-0.9	1.0	1.0	0.0	0.4
<i>Memorandum items</i>						
GDP deflator	–	11.0	8.2	4.0	3.7	3.1
Consumer price index	–	8.3	9.3	4.6	3.2	3.0
Private consumption deflator	–	8.6	10.4	5.2	4.0	3.7
General government financial balance (% of GDP)	–	-4.6	-4.6	-7.2	-6.4	-5.8
Current account balance (% of GDP)	–	-2.8	-2.8	-1.7	-1.6	-1.5

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

Source: OECD Economic Outlook 114 database.

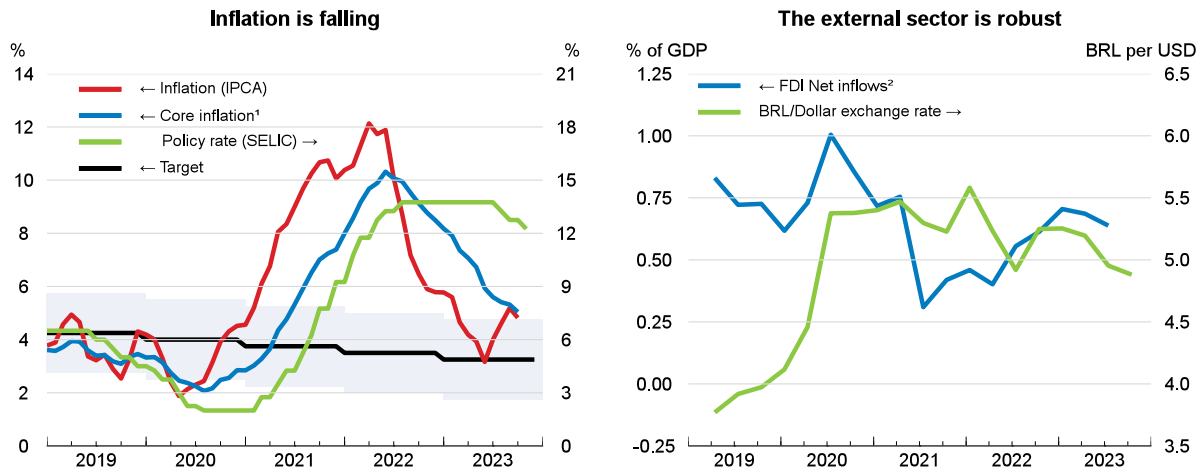
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## Economic activity has picked up

The economy grew robustly in the first two quarters of 2023, with an annualised quarter-on-quarter expansion of 7.5% in the first quarter and 3.7% in the second quarter. The first quarter saw exceptional agricultural production, and early estimates project a new record in agricultural output for the upcoming second harvest. While industrial production improved in August, it remains 1.8% below the pre-pandemic level of February 2020. The services sector contracted consecutively by 0.3% in September 2023 and by 0.9% in August compared to July, following a 2.1% gain in the May-July period. Advanced indicators suggest a progressive slowdown in the second half of the year. The labour market has been strengthening, with the unemployment rate falling to 7.7% in September, the lowest recorded since June 2015. Job creation is predominantly being propelled by the services sector, including domestic services.

Inflation declined to 4.8% in October after a rebound to 5.2% in September, and a significant drop to 3.2% in June. The recent uptick is primarily attributable to higher fuel prices during September. In contrast, food and beverages, which have a strong weight in household consumption, experienced deflation for the fourth consecutive month in October. Furthermore, core inflation is declining, reaching 5.5% in October, down from 6.1% in August.


## Brazil 2



1. Core inflation excludes energy and food products. The shaded area corresponds to the inflation tolerance band.

2. Moving average.

Source: OECD Economic Outlook 114 database; and Banco Central do Brasil.

StatLink  <https://stat.link/t0jxqo>

## Monetary policy easing has started

Despite the recent increase, the declining inflation trend throughout the year has allowed the central bank to ease monetary policy, reducing the policy rate from 13.75% in July to 12.25% by November 2023. With expectations of continued inflation declines and high real interest rates, further policy rate cuts are expected, lowering the rate to 9.2% by the end of 2024 and 7.8% by the latter half of 2025.

In 2023, fiscal policy was expansionary, driven by an increase in social transfers. The primary fiscal deficit is projected to be 1% of GDP. In August 2023, Congress approved a new fiscal framework, enhancing medium-term predictability while adding flexibility, especially for investments. To meet the primary balance target under this framework, the government plans to implement additional tax revenue raising measures equivalent to 1.5% of GDP in 2024, while spending would increase by 1.0% of GDP. Additionally, the lower Chamber of Congress has approved an indirect tax reform, currently under discussion in the Senate, aiming to create a unified value-added tax. This tax reform has strong potential to simplify the tax system and boost economic growth.

## Growth will remain strong

Growth is projected at 3.0% in 2023, slowing to 1.8% in 2024 and 2.0% in 2025. Domestic demand remains the primary driver of economic activity. Job creation continues to bolster household income, stimulating strong household consumption growth. Investment is set to improve due to more favourable financial conditions. Agricultural exports will boost growth in 2023 but this boost is expected to fade in the following years, amid lower commodity prices. Inflation, down from an average of 9.3% in 2022, is expected to decrease to 4.5% in 2023, 3.2% in 2024, and 3.0% in 2025, aligning with the target band as of 2024. The decline in inflation is the result of an early monetary policy response and the normalisation of earlier supply chain disruptions.

Economic risks are balanced. On the upside, another exceptional agricultural harvest could spur growth. Additionally, successful implementation of the tax reform could boost confidence and economic activity, with the effects potentially exceeding expectations. On the downside, slower growth in China, a key trading partner of Brazil, could weigh on external demand. Sustained increases in inflation could delay further policy rate reductions, leading to reduced investment and consumption. Additionally, any further increases in policy rates in advanced economies could exert pressure on the exchange rate.

### **Adopting the tax reform and improving competition will boost growth**

Implementing the new fiscal framework and meeting the primary balance targets will be key to ensure debt sustainability and restore confidence in the public finances. Implementing a unified value-added tax system will simplify the taxation of goods and services and reduce administrative burdens on businesses. Beyond consumption taxes, there is also scope to reform income taxes and improve the progressivity of the tax system. A current personal income tax deductibility of expenditures for private health and education expenses has regressive distributional effects, as 90% of Brazilians have incomes below the threshold where they would pay income taxes and only 25% of Brazilians are subscribed to private health plans, while most of the population relies on the public health system. Recent increases in conditional cash transfers have been well-targeted, reducing poverty and inequality, but further improvements in the effectiveness and targeting of social benefits are needed. Expanding access to early childhood education, especially for low-income households and single parents, can enhance equal opportunities and encourage more women to participate in the labour market. Streamlining regulations and lowering market entry barriers would strengthen long-term growth. Addressing infrastructure gaps in transportation, water, and sanitation can enhance the competitiveness of Brazilian firms in international trade. Deforestation is the leading source of gross greenhouse gas emissions. Stronger enforcement of environmental protection laws including the Forest Code will be crucial to combat deforestation. The agriculture sector is the second-largest direct source of greenhouse gas emissions in Brazil. A better targeting of agricultural credit to low-carbon practices can be effective to combat deforestation and reduce emissions. Introducing carbon pricing mechanisms can complement these efforts and promote fair competition between sectors.

# Bulgaria

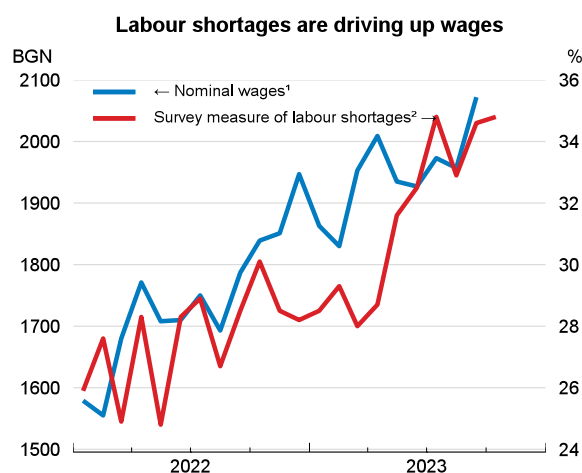
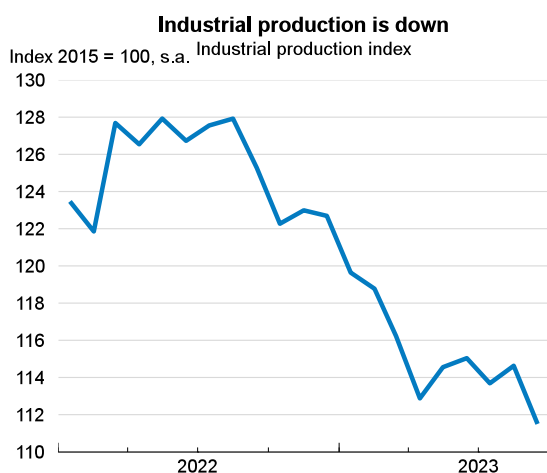
GDP growth is projected to slow to 1.7% in 2023 before recovering to 2.8% in 2024 and 3.0% in 2025. Low interest rates fuelled a household credit boom, boosting private consumption, but this is easing. The catch-up in the disbursement of EU funds is expected to contribute positively to investment in 2024 and beyond. Inflation is high in 2023 but is expected to moderate during 2024. The large, planned minimum wage increases in 2024 create risks of more persistent inflation, while changes in global energy prices could impact exports and inflation.

Interest rates are expected to continue to broadly follow euro area monetary policy given the fixed exchange rate regime of the Bulgarian lev to the euro. The fiscal deficit is likely to widen if spending increases are not fully offset by higher tax collection. Fiscal consolidation would help to manage demand in the economy and prepare for longer-run challenges. Structural reforms are needed given the shrinking labour force and the need to encourage young people to stay in Bulgaria. While some climate policies and targets are in place, the development of a comprehensive green transition roadmap is a priority.

## Domestic demand has been strong

GDP expanded by 1.7% in the year to the third quarter of 2023, with negative real interest rates and robust labour markets supporting strong private consumption and investment. However, government consumption was weak due to the lack of an agreed budget during the first half of the year. The annual inflation rate has fallen rapidly from a peak of 18.7% in September 2022 to 5.8% in October 2023. Core inflation has been more persistent, fuelled by second-round effects from high food and energy prices and rising labour costs. Unemployment is low but rising, although the labour market is set to remain tight given demographic headwinds.

## Bulgaria



1. Nominal average gross monthly wages for all sectors of employees under a labour contract in lev.

2. The shortage of labour measure refers to the share of firm respondents to a business survey conducted by the National Statistics Institute that identified shortage of labour as a factor limiting the activity of their enterprise. It is the arithmetic mean of the same survey conducted in four sectors: industry, construction, retail trade and services.

Source: National Statistics Institute.

StatLink <https://stat.link/8vh6rt>

## Bulgaria: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices BGN billion	Percentage changes, volume (2015 prices)				
<b>Bulgaria</b>						
<b>GDP at market prices</b>	120.5	7.7	3.9	1.7	2.8	3.0
Private consumption	70.3	8.5	3.8	6.6	4.3	3.4
Government consumption	11.7	4.3	4.4	-0.2	5.9	3.1
Gross fixed capital formation	23.0	-8.3	6.5	0.0	7.8	4.4
Final domestic demand	105.0	4.1	4.5	4.5	5.1	3.6
Stockbuilding <sup>1</sup>	13.2	4.8	2.4	-7.0	-1.0	0.0
Total domestic demand	118.2	8.2	6.3	-3.5	3.5	3.3
Exports of goods and services	67.6	11.2	11.6	-3.5	0.3	3.9
Imports of goods and services	65.3	10.7	15.0	-7.1	1.8	4.5
Net exports <sup>1</sup>	2.3	0.4	-1.8	2.5	-0.9	-0.3
<i>Memorandum items</i>						
GDP deflator	–	7.1	16.2	8.6	4.2	2.9
Consumer price index	–	3.3	15.3	9.5	4.5	3.1
Core consumer price index <sup>2</sup>	–	1.4	7.6	9.0	4.6	3.1
Unemployment rate (% of labour force)	–	5.3	4.3	4.4	4.9	4.8
Household saving ratio, net (% of disposable income)	–	5.6	3.0	-0.4	1.2	2.4
General government financial balance (% of GDP)	–	-4.0	-2.9	-3.2	-3.3	-3.6
General government gross debt (% of GDP)	–	35.1	32.2	34.2	36.7	39.7
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	23.9	22.6	24.5	27.1	30.0
Current account balance (% of GDP)	–	-1.7	-1.4	0.6	-0.5	-1.1

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 114 database.

StatLink  <https://stat.link/bixja9>

Weakness in euro area demand will hold back manufacturing exports and tourism in the near term, but this will gradually recover as growth in Europe picks up. With Bulgaria a net electricity exporter, trade prospects depend heavily on developments in European energy markets this winter. A gradual rise in energy prices in the near term could also stoke renewed domestic energy-related inflationary pressures.

### Near-term fiscal policy will be broadly neutral

Interest rate developments will broadly follow monetary policy tightening in the euro area, consistent with the fixed exchange rate to the euro as part of the currency board arrangement and planned euro adoption. Fiscal support to cushion the effects of the energy price shock, such as reduced VAT rates for energy and food products, will be largely phased out by end-2023. The government foresees significantly higher additional spending from increases in public sector salaries and pension payments and plans higher revenues from newly outlined reforms to combat tax evasion and the non-payment of taxes. Overall, the budget deficit will widen if these revenue-raising measures do not fully offset the planned higher spending. The government debt ratio remains low and debt dynamics are supported by low interest rates on government debt. However, there are significant fiscal pressures from a declining labour force and rising pension costs. Meanwhile, long-term ageing-related spending pressures are set to rise given demographic trends, with health care and pension expenditures as a share of GDP expected to increase by 1 percentage point of GDP between 2024 and 2040.

## **GDP growth will slow in the near term before recovering**

Growth has been very rapid but is set to slow to 1.7% in 2023 owing to the weaker-than-expected external environment, but then rebound to 2.8% in 2024 and 3.0% in 2025. The disbursement of EU funds is predicted to spur an increase in private sector investment. Export growth will remain weak in the near term but should gradually recover throughout 2024 in line with developments in the euro area. Inflation is set to slow gradually to 4.5% in 2024, reflecting declining energy prices, but will be kept up by relatively rapid nominal wage growth. With persistent labour shortages, upward pressures on demand and wages could undermine efforts to bring inflation back to target.

## **Fiscal consolidation is needed, while reforms are needed to boost employment**

Monetary policy should remain consistent with the existing currency board arrangement to ensure stability and in anticipation of future euro adoption. Deficit-neutral approaches to financing new government spending in the 2023 budget are helpful, but fiscal consolidation is needed to reduce the deficit, damp domestic demand and offset longer-run spending pressures relating to ageing and demographic challenges. Activation policies and reforms are necessary to tackle inactivity and to raise productivity. While a range of climate policies are in place, an overarching governmental strategy to motivate green transition policies, building on the Strategic Vision for the Sustainable Development of the Electricity Sector, should be developed.



# Canada

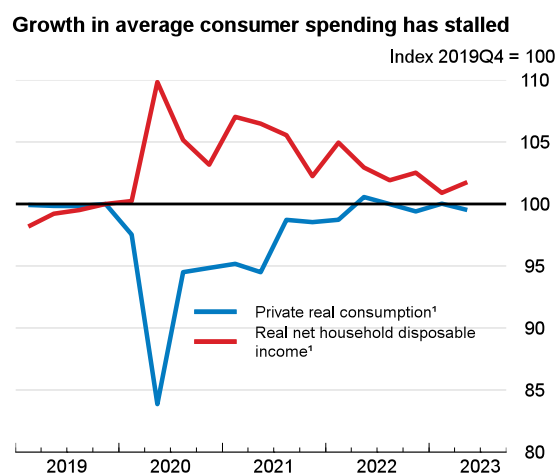
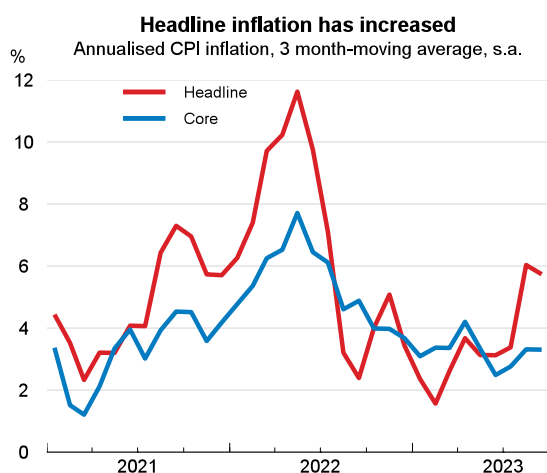
Real GDP growth will drop to 0.8% in 2024, reflecting slowing domestic demand in the wake of higher borrowing costs and weakening exports, before recovering to 1.9% in 2025 as improved global conditions strengthen exports. Immigration will continue to boost private spending and labour supply. Price pressures will ebb in the face of slowing demand and rising unemployment. Were unemployment to rise faster than expected, there could be a substantial fall off in households' consumption demand and a deeper downturn.

The policy interest rate should be kept at its current level until inflation nears its target in 2024. Fiscal consolidation, partly due to the termination of cost-of-living relief, will also help cool the economy. Ensuring long-run fiscal sustainability while accommodating Canada's multi-year spending pressures may require tax reforms and closer attention to spending efficiency. Further efforts to boost business productivity would expand the fiscal revenue base, alongside raising economic capacity and improving standards of living.

## Output growth has stalled

Economic activity has slowed in recent months. Following a strong first quarter (real GDP grew by 0.6%), output growth stalled in the second quarter with effectively zero growth. Data suggest the weakness has continued. In July and August, estimated monthly GDP growth was weak, as were retail sales volumes. Headline inflation spiked up in recent months principally due to increasing fuel prices. Core inflation continues to decline and labour market tensions have eased. The rate of unemployment was 5.7% in October, half a percentage point above rates at the beginning of the year and the job vacancy rate has continued to fall. Nevertheless, by some metrics, the labour market remains tight compared with pre-pandemic norms. Wage growth has remained elevated in recent months.

## Canada 1



1. Per capita.

Source: OECD Economic Outlook 114 database; and Statistics Canada.

StatLink  <https://stat.link/1qd3lf>

## Canada: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices CAD billion	Percentage changes, volume (2012 prices)				
<b>Canada</b>						
<b>GDP at market prices</b>	2 209.7	5.0	3.4	1.2	0.8	1.9
Private consumption	1 263.8	5.0	4.8	2.1	1.0	2.1
Government consumption	504.0	6.4	2.0	0.6	1.4	1.6
Gross fixed capital formation	519.7	7.4	-1.5	-2.9	0.3	1.0
Final domestic demand	2 287.5	5.8	2.7	0.6	0.9	1.8
Stockbuilding <sup>1</sup>	- 28.3	1.1	2.1	-1.3	-0.1	0.0
Total domestic demand	2 259.2	7.0	4.8	-0.7	0.9	1.8
Exports of goods and services	655.9	1.4	2.8	5.0	1.2	2.1
Imports of goods and services	705.4	7.8	7.5	-0.5	1.3	1.7
Net exports <sup>1</sup>	- 49.5	-2.1	-1.5	1.9	-0.1	0.1
<i>Memorandum items</i>						
GDP deflator	–	8.2	7.2	1.2	3.0	1.9
Consumer price index	–	3.4	6.8	4.0	3.0	1.9
Core consumer price index <sup>2</sup>	–	2.4	5.0	3.8	2.7	1.9
Unemployment rate (% of labour force)	–	7.5	5.3	5.4	6.0	5.8
Household saving ratio, net (% of disposable income)	–	10.7	5.9	4.2	3.5	2.4
General government financial balance (% of GDP)	–	-4.4	-0.8	-0.1	0.2	0.3
General government gross debt (% of GDP)	–	120.9	101.5	100.6	100.3	99.8
Current account balance (% of GDP)	–	-0.3	-0.3	-1.3	-1.4	-1.3

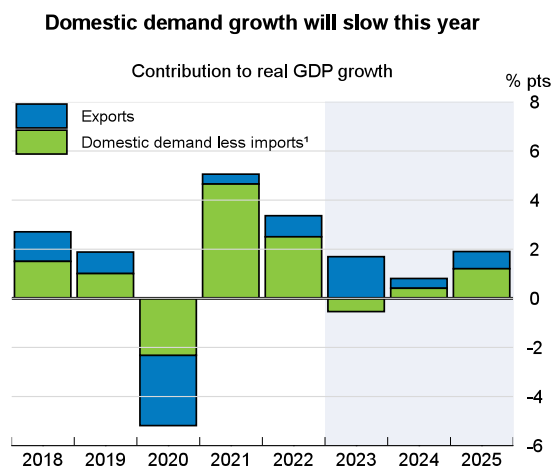
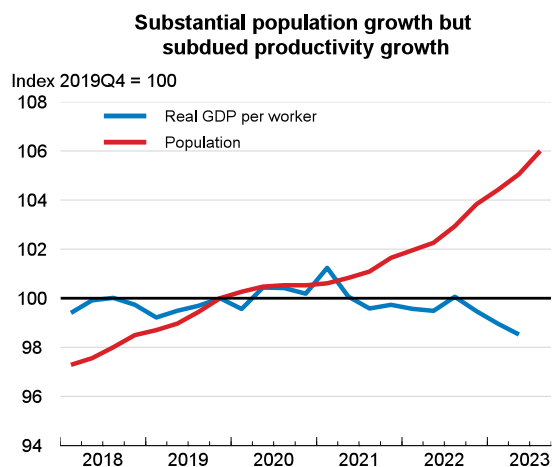
1. Contributions to changes in real GDP, actual amount in the first column.

2. Consumer price index excluding food and energy.

Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/ugmtjp>

## Canada 2



1. Total consumption and investment (including inventory variations) less total imports of goods and services. National accounts data do not disaggregate imports by expenditure component of GDP and intermediate inputs. In practice, imported value added forms part of consumption, investment and also exported goods and services.

Source: OECD Economic Outlook 114 database; and Statistics Canada.

StatLink  <https://stat.link/wf3jxv>

Despite increases in crude oil prices over recent months, Canadian commodity export prices remain below the peaks attained in mid-2022. The terms-of-trade decline has caused a negative income shock which is contributing to moderating demand. Yields of some key farm outputs, notably, wheat, are expected to decrease by 13.1% this year due to dry weather conditions. Extreme weather events, notably wildfires, have devastated a number of communities and caused disruption to some primary industries over the summer.

### **Excess demand is being contained by macroeconomic policies**

Monetary policy remains contractionary, damping demand and helping re-anchor inflation expectations. The policy rate should remain high, at 5%, until mid-2024 to ensure price growth returns within the Bank of Canada's target range of between 1% and 3%. However, macroeconomic conditions may evolve such that further rate rises are needed to quell inflation. As output moves closer to potential, the policy rate should be lowered towards more neutral levels. The projections envisage a 150-basis point decline in the benchmark interest rate by the end of 2025. Gradual quantitative tightening is assumed to continue.

The fiscal stance remains restrictive, eroding the gross general government public debt burden which currently stands at around 100% of GDP. Weaker growth in nominal GDP and business profits will bring further declines in revenue growth. Federal and provincial measures cushioning households from living cost pressures have appropriately diminished. The federal government has not announced major new measures since bringing in a one-off tax credit for low-income households in March. Provinces have also wound down support. Reductions or suspensions of fuel taxation in Alberta and Ontario are scheduled to terminate by the end of this year. The federal government continues to follow through on structural reforms highlighted in its annual budget. These include supporting the green transition, expanding affordable childcare, accommodating the growing costs associated with population ageing and measures to lower the cost of housing.

### **High borrowing costs and subdued foreign demand will weigh on output**

Real GDP growth is projected to drop to 0.8% in 2024. The slowdown in the US economy will damp exports. Capital spending plans will be dented by higher credit costs and a subdued demand outlook. Housing investment will return to growth, but only slowly. Continued rapid rates of population growth will help offset drags on private consumption from higher borrowing costs and weak real income growth. Economic growth will strengthen in 2025 to 1.9%, which is close to potential. Consumer spending will be supported by increased purchasing power. Stronger foreign demand will bolster exports and business investment. A further loosening of the labour market will see additional increases in the rate of unemployment until mid-2024. Wage growth will moderate, remaining roughly in line with consumer-price inflation, which is projected to return to target by the third quarter of next year.

The outlook is surrounded by substantial risks. Labour markets could deteriorate more rapidly, increasing financial pressures on households, prompting cutbacks in consumption and raising difficulties in debt repayment. The high levels of immigration bring upside risks to private consumption along with potential for positive gains from newcomers' skills and increased labour force participation. By expanding productive capacity, high immigration could enable stronger aggregate demand without significantly adding to price inflation.

## Ensuring sustainable fiscal balances is key

Canada's multi-year pressures on public spending represent a challenge for fiscal policy. For instance, over the next 15 years additional health and pension spending is estimated to total 2 percentage points of GDP. Maintaining a workable medium-term plan for lowering federal government debt would help ensure fiscal sustainability. As regards expenditure, ensuring cost-effective delivery on spending priorities will be important, including the expansion of affordable childcare. The effectiveness of measures to help households purchase homes should be kept under close watch, given the risk that such support pushes up the cost of housing. The policy focus should be on reducing excessive limits to supply in urban areas. As regards revenues, a shift towards more indirect taxation, including through higher rates of goods-and-services tax, should remain a policy objective. Canada's long-run fiscal challenges would also be helped by policy to strengthen growth potential, notably through improvements to the business climate. The expected increase in female labour force participation from better access to affordable childcare will be beneficial for business, as well as households. Policy also needs to concentrate on measures that boost growth in business sector productivity, which has been lacklustre in recent years. Lowering barriers to inter-provincial trade in goods and services remains among the practicable steps that Canadian governments could take in this regard.

# Chile

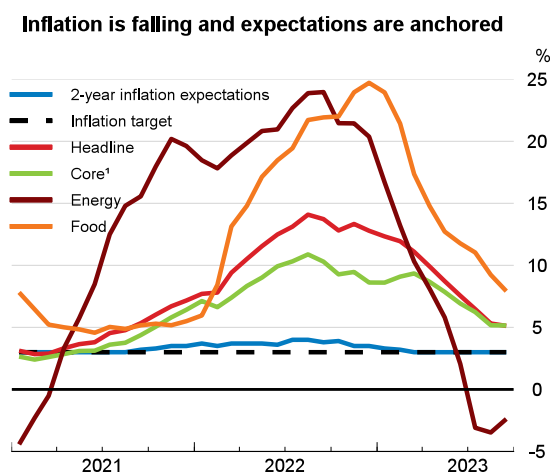
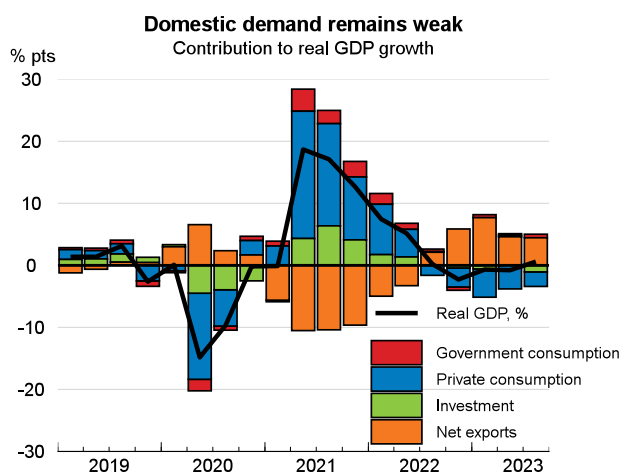
After zero growth in 2023, output will increase by 1.8% in 2024 and by 2.1% in 2025. Rising real wages, due to lower inflation, and falling interest rates will allow consumption to pick up in 2024. Business confidence has improved, but policy uncertainty will weigh on investment growth during early 2024. Strong demand for minerals will continue to sustain exports. Headline inflation will continue abating and will reach the central bank target in the second half of 2024, while core inflation will fall at a slower pace.

The central bank is projected to continue easing monetary policy and reach a neutral stance by late 2024. Fiscal policy will be slightly expansionary, with expenditure in line with the fiscal rule and revenue from mining, including from a new mining royalty, helping to ensure moderate deficits. Government debt will remain at manageable levels. Chile should move towards a more progressive tax system that brings in more revenue for expenditure that enhances growth and reduces inequalities. The global shift toward renewable energies is an opportunity for Chile given its natural resources.

## Domestic demand has been weak

Output grew by 0.3% in the third quarter of 2023 largely due to net exports, as domestic demand is still weak, with a fall in investment offsetting a recovery in consumption. Growth was underpinned by energy and water services, and mining. High-frequency data show retail sales growing in October. Business confidence has improved but is still below historic levels. Headline inflation has fallen steadily and stood at 5% in October, down from 14.1% in August 2022. Core inflation is also falling, and two-year inflation expectations have remained anchored at the 3% target since March.

## Chile



1. Consumer price index excluding energy and food.

Source: Central Bank of Chile; and INE.

StatLink  <https://stat.link/d4xm0k>

## Chile: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>Chile</b>	Current prices CLP billion	Percentage changes, volume (2018 prices)				
<b>GDP at market prices*</b>	200 804.4	11.9	2.5	0.0	1.8	2.1
Private consumption	117 483.4	20.9	2.8	-4.7	2.3	2.0
Government consumption	32 254.3	13.8	4.1	3.1	2.3	2.0
Gross fixed capital formation	45 409.9	15.7	2.8	-2.0	0.7	2.1
Final domestic demand	195 147.6	18.5	3.0	-2.9	1.9	2.0
Stockbuilding <sup>1</sup>	-3 088.1	2.9	-0.7	-1.6	-0.1	0.0
Total domestic demand	192 059.4	21.9	2.3	-4.5	1.8	2.1
Exports of goods and services	62 818.6	-1.3	1.4	0.8	3.0	3.1
Imports of goods and services	54 073.7	31.8	0.9	-11.2	2.8	2.8
Net exports <sup>1</sup>	8 744.9	-9.0	0.1	4.7	0.1	0.0
<i>Memorandum items</i>						
GDP deflator	–	6.9	6.6	6.4	3.2	3.5
Consumer price index	–	4.5	11.6	7.6	3.9	3.4
Private consumption deflator	–	4.3	10.0	7.0	4.2	3.1
Unemployment rate (% of labour force)	–	8.8	7.9	8.5	7.9	7.4
Central government financial balance (% of GDP)	–	-7.7	1.1	-2.0	-2.3	-1.6
Current account balance (% of GDP)	–	-7.3	-9.0	-3.1	-4.0	-3.5

\* 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 114 database.

StatLink  <https://stat.link/iaeryd>

Falling commodity prices earlier this year helped inflation to come down. Copper prices have fallen since July but are still strong. Growth in China has also been weaker than expected. However, a recovery in worldwide tech production since the beginning of 2023, a positive outlook for the use of copper and lithium for electrification, and low global copper inventories signal room for export growth.

## Monetary easing will continue and fiscal policy will return to moderate deficits

Past monetary policy tightening has helped reduce inflation, and expectations have remained anchored at the central bank's target. The Central Bank of Chile began an easing cycle in July, taking the policy rate from 11.25% to 9.0% in November. This is expected to continue over the next two years, with policy rates reaching a more neutral stance from the end of 2024 and being lowered to 4% by the latter half of 2025. In August, the government lifted the freeze on public transport fares, while other support measures to cushion the impact of higher energy prices will end in December 2023. Overall, the fiscal stance will be moderately expansionary, with deficits of 2% of GDP in 2023, 2.3% in 2024, and 1.6% in 2025. This will keep government debt below 45% of GDP, the prudent level set in the decree outlining fiscal policy objectives. Expenditure will follow the fiscal rule based on cyclically-adjusted revenues. Demand for minerals in the medium term will continue to support revenue, although receipts from mining contracts for lithium will moderate in 2024. Revenue from a new copper mining royalty will start coming during 2024-25.

## Growth will rebound in 2024-25

Output will rise by 1.8% in 2024 and 2.1% in 2025. Rising real wages, due to falling inflation, and lower interest rates from monetary easing will help consumption and investment pick up during 2024. The sustained worldwide shift towards electrification, especially of vehicles, will support strong demand for mineral exports. Inflation will continue to abate, with headline inflation reaching the target of the central bank in the second half of 2024. The fall in core inflation will be slower due to indexation of wages and tariffs. Risks to this outlook are tilted to the downside. A deeper slowdown in China can reduce demand for minerals, hurting Chile's exports and growth. Protracted negotiations during 2024 of the tax and pension reforms proposed by the Government could affect policy uncertainty. Climate-change induced events like a worsening of the drought or extreme rains could hit crops, mining and infrastructure, reducing growth and requiring fiscal support.

## Growth-enhancing expenditure requires raising more revenue

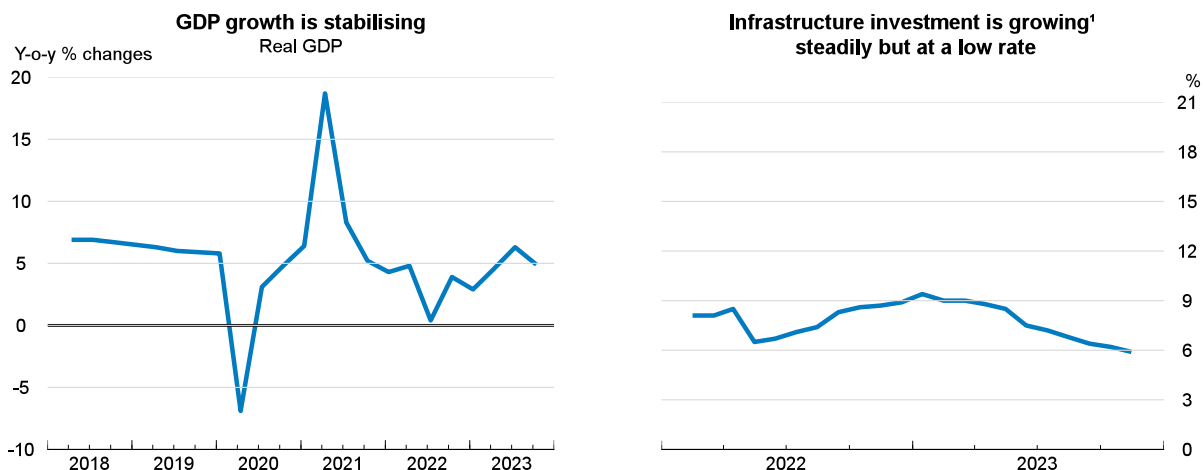
Tax revenue as a share of GDP is low by OECD standards, with few people paying income tax. A more progressive tax system is needed, along with improvements in tax administration, to increase revenue from personal and property taxes. This would allow more expenditure that enhances growth and reduces inequalities, such as boosting public support for SMEs and improving digital infrastructure. Chile is well positioned to profit from the global shift toward renewables. To promote greener energy generation, exemptions from the carbon tax should be accelerated for plants to further incentivise the use of renewables.

# China

Economic growth will rebound only moderately to 5.2% in 2023 and then slow to 4.7% and 4.2% in 2024 and 2025 respectively. Consumption growth will likely remain subdued due to increased precautionary savings, gloomier prospects for employment creation and heightened uncertainty. The ongoing adjustment in the real estate sector continues with falling investment and continued financial stress. Relaxation of some demand-side restrictions is expected to stabilise sales, aided by lower mortgage costs. Excessive indebtedness of local investment vehicles constrains the delivery of urban infrastructure projects. Exports will remain weak amid sluggish global growth. Consumer price inflation will remain very low, though sustained deflation is unlikely. A deeper correction in the real estate market is a key risk. Trade sanctions may disrupt production at some high-tech manufacturers.


Monetary policy should remain supportive, with further interest rate and reserve requirement cuts as needed. The widening of the interest differential with other economies has led to capital outflows and a currency depreciation. Fiscal policy could provide more support for the debt resolution of financing vehicles, in addition to the planned shift in the composition of spending towards infrastructure and urban village reconstruction. Deductions and exemptions of taxes and charges for targeted groups will provide some support. The anticipated stabilisation of the housing sector will bring about a rebound of budgetary revenues at the local level.

## China 1



1. Year-to-date year-on-year growth.

Source: CEIC.

StatLink  <https://stat.link/vf23hq>



## China: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>China</b>						
	Current prices CNY trillion	Percentage changes, volume (2015 prices)				
<b>GDP at market prices</b>	101.4	8.4	3.0	5.2	4.7	4.2
Total domestic demand	98.9	6.8	2.8	6.2	4.6	4.2
Exports of goods and services	18.9	15.7	-3.9	1.9	4.0	4.5
Imports of goods and services	16.4	7.6	-6.7	7.4	3.6	4.4
Net exports <sup>1</sup>	2.5	1.8	0.3	-0.7	0.2	0.2
<i>Memorandum items</i>						
GDP deflator	–	4.6	2.2	0.0	1.7	2.0
Consumer price index	–	0.8	1.9	0.4	1.0	1.5
General government financial balance <sup>2</sup> (% of GDP)	–	-6.4	-6.5	-6.6	-6.7	-6.7
Headline government financial balance <sup>3</sup> (% of GDP)	–	-3.0	-2.8	-3.1	-3.0	-2.9
Current account balance (% of GDP)	–	2.0	2.2	1.6	1.1	1.3

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.

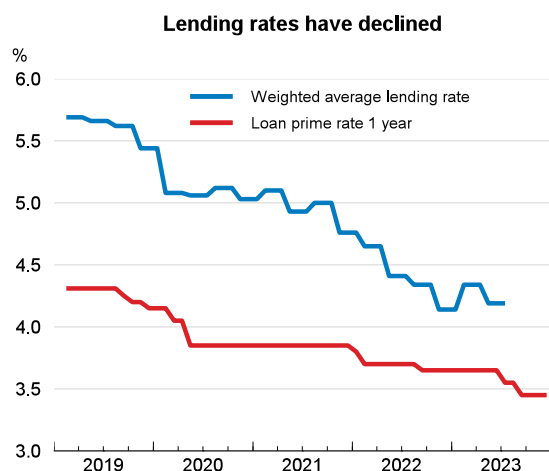
Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/gb4smy>

## Economic activity has rebounded moderately in 2023

Growth bottomed out in the third quarter, following a moderate recovery after the re-opening and weaknesses in the first half of the year. Property investment is still decreasing at a steady rate and weighing on growth. Infrastructure investment has been growing at a steady, but low, rate due to financing constraints, and manufacturing investment is being held back by lower capacity utilisation rates. Consumption growth is stable but is being constrained by relatively high unemployment as a large number of graduate students entered the labour market this year. Weak demand in some key export markets is weighing on export growth, but a very limited recovery of tourism imports is helping to maintain the current account surplus.

### China 2



1. Year-to-date year-on-year growth.

Source: CEIC.



StatLink  <https://stat.link/1m58wh>

The Chinese economy was spared from inflation stemming from soaring global energy and food prices as its food self-sufficiency rate is high and it has substituted some crude oil imports with discounted oil from Russia. More recently, falling energy prices have supported energy imports. Productivity improvements and innovation help to keep overall inflation low, even if food prices have increased. High unemployment, subdued wage growth and low demand are also contributing to low inflation.

## Monetary and fiscal policy will support demand

Monetary policy continues to support the recovery and ensure adequate liquidity. The benchmark lending rate and the ratio of reserves to be kept at the central bank have been cut multiple times. The effective mortgage lending rate is being driven down by the new mortgage rate adjustment mechanism introduced in early 2023, which allows local authorities to remove the mortgage interest floor in cities where new housing prices decrease for three consecutive months. More recent measures, such as facilitating the renegotiation of rates on outstanding loans, also work in that direction. This reduces households' debt service burden. The realised savings on debt payments are expected at least partly to be channelled to consumption. More stringent implementation of credit quotas for presold housing, lower provident fund lending rates for first-time buyers, the broadening of the definition of first-time buyers and other measures will help stabilise the property sector and allow adjustments to continue in an orderly manner.

Fiscal policy will continue to provide support through tax cuts and exemptions for small and micro enterprises and accelerated deductions of research costs. Special treasury bonds of CNY 1 trillion, or around 0.8% of GDP, will support growth in 2024. The issuance of refinancing bonds by several local entities is expected to reduce the pressure on heavily indebted local investment vehicles and help implementation of planned infrastructure projects. While this may provide short-term relief, the problem of implicit debt at the local government level needs to be addressed effectively and in a timely manner. Urban village redevelopment will be a focus of the coming infrastructure drive, with urban infrastructure provision in large swathes of land in the middle of cities and improvements of intra-city connections. This will boost productivity, upgrade the residence status of the inhabitants of those areas and clarify land rights, with potential improvements in living standards.

## Growth is returning to a gradually slowing trend path

Following a moderate rebound after the re-opening, the Chinese economy will return to its gradually slowing path, with 4.7% growth in 2024 and 4.2% in 2025, due to unfavourable demographics and slowing trend productivity growth. The on-going adjustment in the real estate sector will continue to weigh on residential investment and related consumption. Infrastructure investment will pick up, as the debt and financing issues of investment vehicles at the local level are resolved, due to high needs arising from the green transition, urban village redevelopment, and other environmental and social targets. Consumption is expected to remain sluggish given weak confidence and the lack of reforms to strengthen the social safety net. Tourism imports may not recover to pre-COVID levels. By moving up the value chain, China will reduce its reliance on imported parts and components and thus, even amid weak foreign demand, the current account surplus will remain high.

Overall risks are tilted to the downside. Potential further defaults may disrupt orderly adjustment in the real estate sector. Excessive relaxation of demand-side restrictions in the property sector may result in stronger growth but also a further build-up of imbalances and more painful adjustment subsequently. Delays in addressing implicit local government debt may hold back infrastructure investment. Sanctions on frontier technologies might lead to reshuffling of global value chains, disrupting production in high-tech intensive and import-dependent domestic manufacturing sectors in the short run, and reducing productivity growth in the longer term.

## Structural reforms are needed to sustain growth

Monetary and fiscal policy should continue to support growth in the near term, but avoid adding to financial risks. Amid unfavourable demographic prospects and labour shortages, high youth unemployment rates need to be brought down by better matching training options and skills needed in the market as well as better managing expectations with regards to job choices. To rebalance the economy towards consumption and reduce savings, a stronger social safety net is needed. Unemployment insurance coverage should be extended to all, and pensions should provide at least a minimum standard of living to all eligible people. Furthermore, the list of treatments and medicines covered by health insurance should be widened so that health costs do not push people into poverty. Reforms to create a level playing field and enhance competition would help the private sector recovery. Stronger consumer protection could also boost competitive pressures. Administrative monopolies, often with exclusive rights to provide certain goods and services, should be dismantled. Recent measures aimed at creating a single domestic market are a welcome step. Meeting the ambitious climate targets requires a timely phase out of coal-fired power plants.

# Colombia

GDP is expected to grow at moderate rates of 1.2% in 2023 and 1.4% in 2024 before picking up to 3% in 2025. High inflation, interest rates and policy uncertainty will weigh on domestic demand in 2024. The central bank has raised interest rates to a 25-year high to bring inflation under control. Headline inflation has started to come down and is projected to return to the 2-4% target range in the second half of 2025.

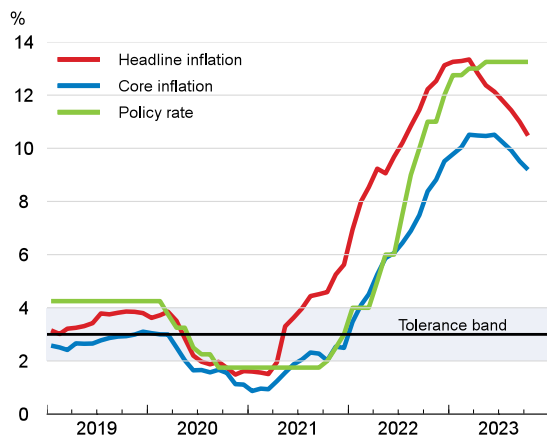
Monetary policy should avoid a premature easing to ensure continued disinflation and safeguard credibility. To ensure debt stabilisation and compliance with fiscal rules while securing fiscal space for an ambitious social reform agenda, it will be necessary to improve spending efficiency and public revenues. Further raising incentives for formal job creation by reducing non-wage labour costs and improving training could foster both productivity and equity.

## Growth has slowed

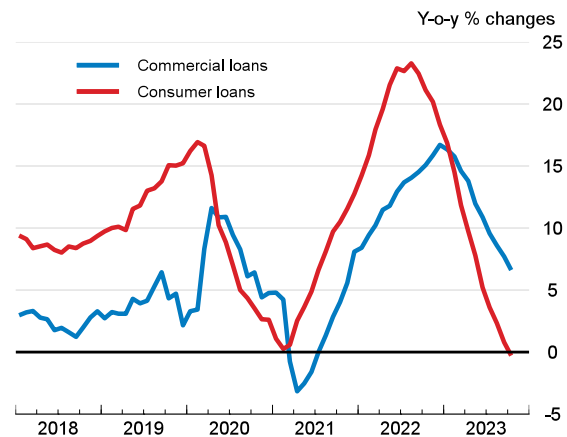
GDP growth has slowed substantially since late 2022 and consumer and business confidence remain relatively weak. Investment has fallen sharply to below 18% of GDP compared to 22% on average during 2014-2019. High interest rates and policy uncertainty are the main factors weighing on investment. Moreover, financial conditions have tightened amidst rising cost of credit and more stringent lending criteria. Private consumption, a key driver of the strong recovery from the pandemic, has also weakened. So far, the slowdown has not yet been passed through to the labour market, where the unemployment rate is 1.5 percentage points below pre-pandemic levels.

## Colombia


**Inflation has started to fall amidst tight monetary policy**



**Credit growth has slowed**



Source: DANE; and BanRep.

StatLink  <https://stat.link/w3jryh>

## Colombia: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices COP trillion	Percentage changes, volume (2015 prices)				
<b>Colombia</b>						
<b>GDP at market prices</b>	997.7	11.0	7.3	1.2	1.4	3.0
Private consumption	706.6	14.5	9.5	1.1	0.3	1.9
Government consumption	171.3	9.8	0.3	2.0	2.0	3.1
Gross fixed capital formation	182.7	17.3	11.4	-7.1	1.2	7.7
Final domestic demand	1 060.6	14.4	8.5	-0.2	0.7	3.0
Stockbuilding <sup>1</sup>	7.6	-0.8	1.0	-3.9	-1.0	0.0
Total domestic demand	1 068.3	13.4	9.4	-4.1	-0.4	3.3
Exports of goods and services	135.0	15.9	14.8	5.1	4.4	3.6
Imports of goods and services	205.5	26.7	22.3	-15.4	-3.1	4.8
Net exports <sup>1</sup>	- 70.5	-3.4	-2.9	5.3	1.5	-0.3
<i>Memorandum items</i>						
GDP deflator	–	7.7	14.3	6.5	6.1	4.4
Consumer price index	–	3.5	10.2	11.7	6.3	4.0
Core inflation index <sup>2</sup>	–	1.8	6.4	9.9	6.1	4.0
Unemployment rate (% of labour force)	–	13.8	11.2	10.0	10.2	10.0
Current account balance (% of GDP)	–	-5.7	-6.2	-3.4	-3.2	-3.2

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 114 database.

StatLink  <https://stat.link/pixyka>

Monetary policy tightening, with interest rates at 13.25% since May, has contributed to the decline in inflation to 10.5% year-on-year in October. Core inflation stood at 9.5%. Disinflation occurred despite significant increases in energy prices, especially fuel, and the pass-through of the 16% minimum wage increase in January into prices especially of services. The alignment of previously subsidised domestic gasoline prices to international prices mitigates the impact of global oil prices on Colombia's public finances. The severity of the ongoing El Niño weather phenomenon, which could cause droughts that might result in food price pressures due to lower harvests, is expected to peak in early 2024.

## The path of fiscal consolidation is uncertain

Fiscal consolidation is taking place but there are risks of non-compliance with fiscal rules. The planned budget deficits of 4.3% of GDP in 2023, 4.5% in 2024, and 3.5% in 2025 would be just within the limits stipulated by the fiscal rule. However, primary expenditure to implement the reform agenda in 2024 is higher than previously anticipated. In addition, oil, customs and tax revenues in 2023 are lower than expected. Moreover, fiscal plans incorporate cyclical and uncertain revenues, notably the collection of tax arrears via litigation, which amount to almost 1% of GDP in 2024 and 0.6% in 2025, according to the fiscal council. Under the current fiscal plans, debt would hover around 55% of GDP in 2033, compared to less than 50% before the pandemic. On the monetary side, a gradual easing of interest rates could start in 2024, assuming inflation will have fallen further and is on a durable path back towards its target, following other central banks in the region. Policy interest rates are projected to fall to 6% by the end of 2025.

## Weak growth will continue well into 2024

GDP growth will remain below potential while monetary policy is restrictive. Growth will gradually pick up with the central bank's easing cycle starting from 2024, although there is a significant lag in the pass through from the benchmark to lending rates. The speed-up in growth from the second half of 2024 will be especially driven by a rebound of investment fuelled by the relaxation of financial conditions. However, this will only make up partly for the earlier decline. Exports, which are currently dominated by oil, will remain subdued given a weak global economy and weak investment into production. Inflation will continue to gradually decrease, to around 10% by end-2023 and around 5% by end-2024, driven by tight monetary policy and weak domestic demand. Domestic risks include a breach of the fiscal rules and challenges to debt sustainability, particularly with high planned public expenses, and a more severe El Niño. On the upside, higher global oil prices could improve the fiscal position.

## A strong macroeconomic framework would support the reform agenda

A continued commitment to the traditionally strong fiscal and monetary framework would support the government's ambitious and fast-paced reform agenda. Improving spending efficiency and raising revenues, for example by reducing tax expenditures and exemptions, will also be needed to ensure compliance with the fiscal rules, debt stabilisation, and financing of the proposed health, pension, labour and education reforms and the energy transition. Reforms to reduce informality, which affects half of Colombian workers, should include lowering non-wage labour costs and improving the quality of training.

# Costa Rica

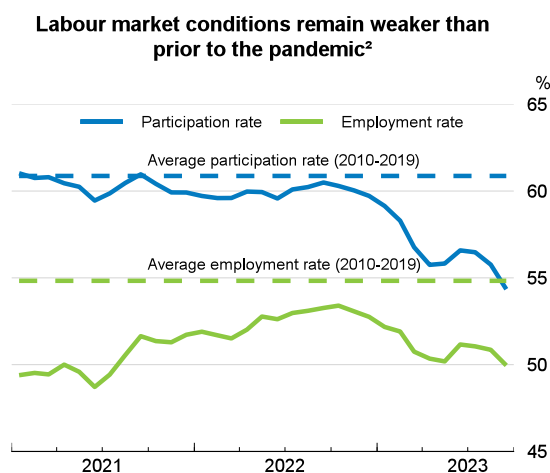
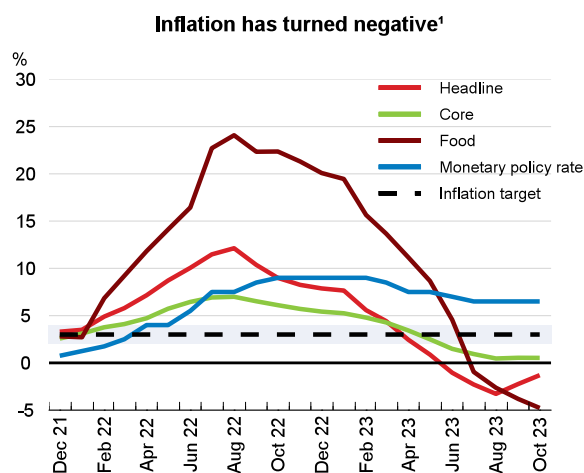
GDP will grow by 3.5% in 2024 and 3.6% in 2025. Domestic demand is projected to gradually strengthen in 2024, as monetary policy continues to ease and labour market conditions gradually improve. External demand is expected to soften in 2024 and pick up again in 2025 as global conditions improve. Inflation is projected to reach 1.9% in 2024 and 3.1% in 2025, just above the 3% target, as improved economic conditions lead to an increase in domestic inflationary pressures.

The fiscal outlook improved in 2023 and the fiscal stance will remain restrictive as the fiscal rule contains public spending. Monetary policy should continue to gradually ease as inflation remains below the target range. Increasing female labour market participation by expanding the coverage of early education and care for children below four years, improving the quality and efficiency of education and increasing the number of science graduates, would support higher growth and equity.

## Economic activity strengthened amid labour market stagnation

Economic activity has strengthened through 2023, with the Monthly Index of Economic Activity increasing by 6.5% (year-on-year) in September 2023, driven by manufacturing, construction and professional services. The rapid decline in inflation (both core and headline), the decrease in interest rates that started in January 2023 and the improvement in the terms of trade strengthened private consumption in the first three quarters of 2023. This is despite employment and labour force participation remaining below pre-crisis norms. Private investment also picked up in the first three quarters of 2023. The Confidence Index for Investment hit a 10-year record high in the third quarter of 2023. Exports accelerated in the first half of 2023, in industries in the free trade regime (medical devices and professional services) and also in the traditional regime.

## Costa Rica



1. The horizontal dashed black line indicates the target inflation rate of monetary policy, and the shaded area the tolerance band around the target (2-4%). Headline and core indicate, respectively, the headline consumer price inflation rate and the core consumer price inflation rate. The core consumer price inflation rate measures consumer price inflation excluding food and energy components.

2. The horizontal blue and green dashed lines indicate the average participation and employment rates computed over the period January 2010 - December 2019.

Source: Banco Central de Costa Rica.

## Costa Rica: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices CRC trillion	Percentage changes, volume (2017 prices)				
<b>Costa Rica</b>						
<b>GDP at market prices</b>	36.5	7.9	4.6	5.1	3.5	3.6
Private consumption	22.8	8.3	3.4	4.4	3.4	3.4
Government consumption	6.5	1.7	2.4	0.1	0.8	0.9
Gross fixed capital formation	5.9	7.8	1.5	10.1	5.0	5.7
Final domestic demand	35.2	7.0	3.0	4.8	3.3	3.4
Stockbuilding <sup>1</sup>	0.0	1.5	-0.9	-1.8	0.6	0.0
Total domestic demand	35.2	8.6	2.0	3.1	3.6	3.3
Exports of goods and services	11.6	15.9	13.2	11.9	6.5	6.9
Imports of goods and services	10.3	19.2	6.0	7.1	7.6	6.8
Net exports <sup>1</sup>	1.3	-0.3	2.6	2.2	0.1	0.5
<i>Memorandum items</i>						
GDP deflator	–	2.4	6.3	-0.2	1.9	3.2
Consumer price index	–	1.7	8.3	0.6	1.9	3.1
Core inflation index <sup>2</sup>	–	0.9	4.2	1.2	2.2	3.1
Unemployment rate (% of labour force)	–	16.4	12.2	9.1	7.8	7.6
Current account balance (% of GDP)	–	-2.4	-3.6	-3.3	-5.0	-5.2

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 114 database.

StatLink  <https://stat.link/51q6i4>

The strong appreciation of the exchange rate to the US dollar (15% year-on-year in October) the reduction in imported commodity prices and modest domestic inflationary pressures contributed to a rapid fall in headline and core inflation that reached -1.3% and 0.5% over a year earlier, respectively, in October 2023. With very low inflation, one- and two-year inflation expectations returned to the 3% target in July 2023. Improvements in the fiscal and economic outlook have led to a reduction in country risk, with the Emerging Market Bond Index spread declining by around 80 basis points between January and September 2023.

### Monetary policy easing will go along with prudent fiscal policy

Monetary policy is projected to continue easing as inflation remains below the 3% target rate. The policy rate is expected to be cut by 150 basis points by the end of 2025. The central government's primary fiscal surplus is projected to remain positive over the projection period (1.6% of GDP in 2023, 1.9% in 2024 and 2025) as the fiscal rule contains expenditures. The corresponding budget deficit is projected to be 3.5% of GDP in 2023 and 3% of GDP in 2024 and 2025, due to large public debt servicing costs. These amount to around 5% of GDP annually in 2024 and 2025. Central government public debt is expected to fall from the record-high of 68% in 2021 to 59.4% by end-2025. Fiscal costs of population ageing (pensions and health) are estimated to increase by around 0.3% of GDP per year until 2030.

### Growth will slow in 2024 and pick up in 2025

Growth will slow to 3.5% in 2024 and inch up to 3.6% in 2025 as global and domestic economic conditions gradually improve. Private consumption will moderate in 2024 as the participation rate remains low and employment growth improves only slowly. High uncertainty due to geopolitical tensions will slow private investment in 2024, with public investment also remaining weak due to a lack of fiscal space. The impact of the strong terms-of-trade improvement recorded in 2023 will moderate export growth in 2024. The high degree of dollarisation of Costa Rica's economy exposes the country to risks associated with sharp



exchange rate movements. Extreme weather events related to El Niño might negatively impact economic activity and inflation. On the upside, the renewed efforts to deepen trade integration might strengthen exports.

### **Continued structural reforms would strengthen growth and reduce inequalities**

Continuing with structural reform implementation would strengthen growth and economic resilience while reducing inequalities. Increasing female labour market participation by expanding the coverage of early education and care for children below four years, and improving the quality and efficiency of education by providing 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 maintain its 100% share of electricity produced from renewable sources, reduce emissions in the transport sector by increasing public transport use and the electrification of transport, continue to increase forest coverage, augment waste recycling and composting, and complete the sewer system coverage.

# Croatia

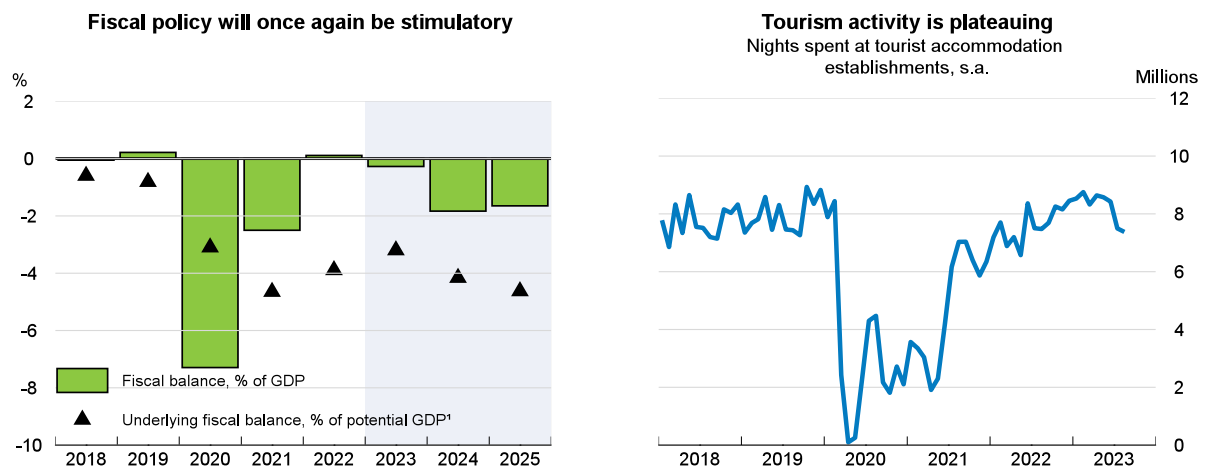
Output growth is expected to remain broadly resilient, picking up slightly from 2.5% in 2023 to 2.6% in 2024 and 2.7% in 2025. Rising public sector investment and resilient private consumption are projected to support demand, offsetting subdued exports. Inflation, which remains high, will decline gradually as labour inputs and excess capacity will remain relatively scarce.

Tighter euro area monetary policy is tempering lending growth and raising interest rates. A small government budget deficit is expected in 2023 but plans for tax cuts and higher spending on investment, wages and pensions are expected to contribute to a wider deficit in 2024. Rising revenues are projected to enable a modest improvement in the budget balance in 2025. Public debt is expected to fall below 60% of GDP by 2025. Ending poorly-targeted price caps and energy and home loan subsidies would help growth to remain sustainable, improve the economy's efficiency and build fiscal buffers for future shocks.

## Robust services exports and rising real incomes are buttressing growth

Output growth has been buoyed this year by recovering consumer spending, as rising wages and employment lifted households' incomes. Robust tourism activity, boosted in part by integration into the euro and Schengen areas, has supported demand in employment-intensive services, helping to reduce the unemployment rate. This has offset weaker industrial production and goods exports, which have been affected by higher energy and other input costs and softer external demand, as well as slowing construction activity. After strong house price rises in 2022 and the first half of 2023, housing demand has moderated with higher borrowing costs and the expiry of a government home-loan subsidy.

## Croatia



1. The fiscal balance corrected for the business cycle measures the government's fiscal stance once cyclical variation in revenues and spending are taken into account.

Source: OECD Economic Outlook 114 database; and Eurostat.

## Croatia: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices HRK billion	Percentage changes, volume (2015 prices)				
<b>Croatia</b>						
<b>GDP at market prices</b>	50.6	13.8	6.3	2.5	2.6	2.7
Private consumption	29.7	10.6	6.7	2.2	2.6	2.6
Government consumption	12.7	3.0	2.7	4.9	3.7	2.5
Gross fixed capital formation	11.2	6.6	0.1	4.0	3.3	4.0
Final domestic demand	53.6	8.1	4.4	3.1	3.0	2.8
Stockbuilding <sup>1</sup>	0.5	0.2	2.4	-2.6	-0.4	0.0
Total domestic demand	54.1	11.4	6.8	1.0	2.6	2.7
Exports of goods and services	20.9	32.7	27.0	1.6	1.4	2.6
Imports of goods and services	24.5	17.3	26.5	-3.3	2.3	2.7
Net exports <sup>1</sup>	-3.5	5.2	-0.5	3.1	-0.5	-0.1
<i>Memorandum items</i>						
GDP deflator	–	1.5	9.5	9.8	4.8	2.9
Harmonised index of consumer prices	–	2.7	10.7	8.6	4.2	2.6
Harmonised index of core inflation <sup>2</sup>	–	1.3	7.6	9.0	4.0	2.6
Unemployment rate (% of labour force)	–	7.6	7.0	6.3	6.0	5.8
Household saving ratio, net (% of disposable income)	–	3.7	2.0	2.7	9.0	6.6
General government financial balance (% of GDP)	–	-2.5	0.1	-0.3	-1.8	-1.6
General government gross debt (% of GDP)	–	98.1	88.7	84.3	83.4	82.9
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	78.1	68.2	61.8	60.3	59.1
Current account balance (% of GDP)	–	1.0	-2.8	2.5	1.6	1.5

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. 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 114 database.

StatLink  <https://stat.link/gue4xp>

The rise in international energy prices has slowed the fall in headline inflation, which reached 6.7% in the year to October. Falls in other international, upstream prices and softening global demand have eased the inflation momentum. International tourism, particularly within Europe, is a key influence on Croatia's economy. Demand plateaued in the third quarter of 2023, albeit still near historic highs, as conditions weakened in key regional markets.

## Fiscal policy will be stimulatory in the near term

Tighter euro area monetary policy is feeding into Croatia's financial sector, with higher borrowing costs and tighter lending conditions contributing to lower growth in lending to businesses. Lending to households is more robust, led by home loans, which had been supported by a temporary government home loan subsidy. The government's budget position has been supported by robust growth in activity and prices lifting revenues, and is expected to record a small deficit in 2023. In 2024, a wider deficit is expected due to higher public-sector pay and pensions, increases in public and defence investment, alongside cuts in household income tax and social contribution rates. The government has extended energy and food price caps and tax reductions to April 2024 and is providing one-off cash transfers. Spending on public investments and transfers for Recovery and Resilience plan projects, largely funded by EU programmes, are projected to rise slightly between 2023 and 2024. In 2025, the fiscal stance is projected to broadly neutral, with higher revenues expected to modestly reduce the budget deficit. Despite the near-term expansion of deficits, public debt is expected to fall below 60% of GDP by 2025.

## **Growth is expected to remain resilient**

Output growth is projected to moderate in the second half of 2023 before firming slightly in 2024 and 2025. Weaker external demand will be the main drag on growth. Robust private consumption, as the tight labour market supports households' real incomes, and rising investment as the government advances with its Recovery and Resilience Plan will support domestic demand. Nonetheless, capacity constraints will ease. Employers' difficulties recruiting workers with relevant skills will be eased by reduced growth and by immigration. Inflation will continue to gradually abate with lower upstream prices and softer external demand, but remain above the euro area target due in part to strong wage growth. If wages continue to rise rapidly into the medium-term, inflation will remain well above other euro-zone countries and Croatia's competitiveness will be weakened. Achieving planned increases in public investment remains a challenge. If investment falls short of plans, domestic activity would be weaker than projected. The capacity for further strong growth in tourism is uncertain. There is also risk of under-performance of industrial production and exports if energy or other input prices rise further or geopolitical uncertainty amplifies.

## **Building fiscal buffers and investing in the green and digital economy will help sustain growth**

Ending poorly-targeted energy price caps and home loan support, fully implementing planned investments, and saving any windfall revenues would improve the sustainability of growth. Ensuring that the budget stance reduces demand pressures while inflation is high, and enables public debt ratios to fall, will help Croatia to face future shocks and looming challenges from the green transition and as the workforce declines and health and other care costs rise with the population ageing. Further expanding adult education and developing a more responsive skilled immigration programme can ease labour market pressures and improve access to higher productivity, higher income jobs.

# Czechia

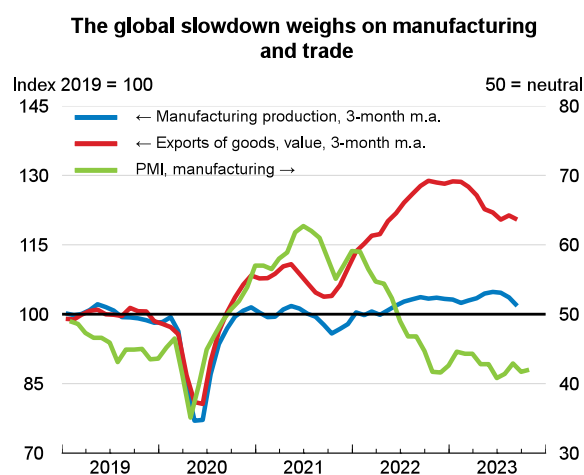
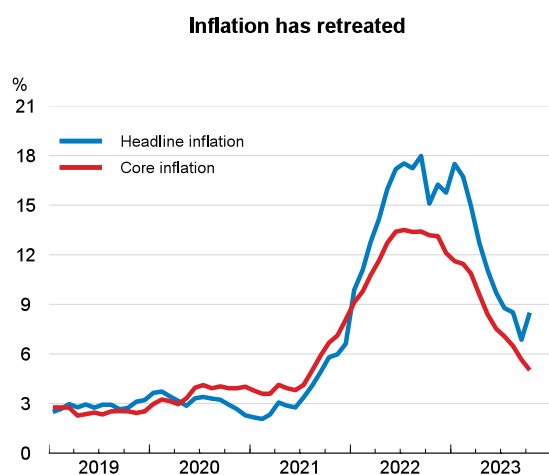
GDP growth is expected to contract by 0.3% in 2023, before picking up to 1.6% and 2.1% in 2024 and 2025, respectively. Elevated inflation and tight monetary policy are weighing on domestic demand. Slower global growth and trade will moderate exports and activity, notably in manufacturing. Private consumption will pick up in 2024, underpinned by growing real wages. Inflation will continue to decline and get close to 3% – the upper boundary of the tolerance band – in early 2024. The labour market will remain tight with an unemployment rate below 3%. Volatility in energy supply and geopolitical tensions remain major risks. Shocks to commodity prices could make inflation more persistent.

Macroeconomic policy needs to maintain a tight stance until inflation is firmly under control, while monitoring risks to financial stability. Fiscal consolidation should also be pursued to rebuild fiscal buffers. An overdue reform of the pension system would help contain steep future rises in public expenditures. Higher labour participation, notably of mothers, would help address chronic labour shortages and support growth. Reducing emissions and reliance on coal would make growth more sustainable.


## The economy has been stagnating

GDP stagnated in the first half of 2023 and declined in the third quarter. Tighter monetary policy and slower global growth are weighing on activity and trade, especially the manufacturing sector. Declining real incomes and low sentiment have hit household consumption. In contrast, public investment is accelerating due to the ending of the EU 2014-2020 programming period as well as the use of funds from the Next Generation EU. Consumer price inflation has declined rapidly since early 2023, to 8.5% in October. The labour market remains tight, with a low unemployment rate of 2.5% in the third quarter of 2023.

## Czechia



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

StatLink  <https://stat.link/bgnvkt>

## Czechia: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices CZK billion	Percentage changes, volume (2015 prices)				
<b>Czechia</b>						
<b>GDP at market prices</b>	5 710.8	3.5	2.4	-0.3	1.6	2.1
Private consumption	2 588.7	4.1	-0.7	-3.0	2.8	2.6
Government consumption	1 242.6	1.4	0.6	2.6	1.2	1.0
Gross fixed capital formation	1 516.4	0.7	3.0	2.0	1.6	2.3
Final domestic demand	5 347.7	2.5	0.6	-0.4	2.1	2.2
Stockbuilding <sup>1</sup>	- 22.1	4.8	0.9	-2.1	-0.6	0.0
Total domestic demand	5 325.5	7.7	1.5	-2.5	1.4	2.1
Exports of goods and services	3 995.1	6.8	7.2	2.8	2.0	3.1
Imports of goods and services	3 609.8	13.2	6.3	0.1	1.8	3.2
Net exports <sup>1</sup>	385.2	-3.6	0.9	2.1	0.2	0.1
<i>Memorandum items</i>						
GDP deflator	–	3.3	8.5	8.7	3.2	2.4
Consumer price index	–	3.8	15.1	10.7	3.1	2.3
Core inflation index <sup>2</sup>	–	5.0	12.2	7.7	3.6	2.3
Unemployment rate (% of labour force)	–	2.7	2.2	2.6	2.7	2.7
Household saving ratio, net (% of disposable income)	–	14.8	11.7	12.8	12.3	12.1
General government financial balance (% of GDP)	–	-5.1	-3.2	-3.6	-2.2	-1.7
General government gross debt (% of GDP)	–	48.3	47.7	48.4	50.0	51.1
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	42.0	44.2	44.9	46.5	47.6
Current account balance (% of GDP)	–	-2.8	-6.1	-1.7	-1.0	-1.0

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 114 database.

StatLink  <https://stat.link/s9l2zm>

Slow growth in trading partners over recent quarters has lowered export growth, offsetting the easing of supply chain bottlenecks and declining costs to producers. Despite this, the contribution of net exports to growth has been positive, as weak domestic demand has reduced imports. Continued monetary policy tightening by major central banks and a narrowing of the interest rate differential has contributed to a depreciation of the koruna since April 2023.

## Macroeconomic policy has tightened

The Czech National Bank (CNB) has kept the policy interest rate at 7% since June 2022. The tight monetary policy stance has slowed the growth of bank loans to households and firms. A gradual easing cycle is projected to start in the first quarter of 2024, with the policy rate being reduced to 4% in 2025. Given the slowing economy, the CNB lowered the countercyclical capital buffer from 2.5% to 2%, effective from October 2023, to ease access to loans. The fiscal situation has deteriorated since the pandemic. The general government deficit is expected to be 3.6% of GDP in 2023. The state budget will likely post a higher deficit than budgeted, owing to measures to cushion the impact of high energy prices and an extraordinary indexation of pensions. For 2024, the government announced faster consolidation, with a 1.4 percentage point improvement in the general government balance as a share of GDP. A further fiscal consolidation of 0.5 percentage points of GDP is assumed in 2025. Expenditure financed by Recovery and Resilience Facility grants will amount to roughly 0.7% of GDP annually in 2023 and 2024, and 0.3% in 2025. General government debt (Maastricht definition) stood at 44.2% of GDP in 2022 and is projected to grow to 47.6% in 2025.

## **GDP will pick up in 2024**

GDP growth is expected to pick up to 1.6% and 2.1% in 2024 and 2025, respectively. Stronger growth in trading partners will support exports. Inflation will drop to about 3% in 2024 and real wage growth will turn positive, sustaining private consumption. The unemployment rate will remain below 3%. However, the outlook is clouded by uncertainty. Renewed energy supply disruptions could restrict economic activity. Unexpected further rises in commodity and energy prices, a steep depreciation of the koruna or rising inflation expectations could make high inflation more persistent and delay monetary easing. A sharp correction in housing prices could threaten financial stability and weigh on growth.

## **Ambitious reforms are needed to unleash labour supply and accelerate the green transition**

Interest rates will have to remain elevated until inflationary pressures are well controlled. The authorities need to continue closely monitoring risks in the housing market. Steady fiscal consolidation is needed to rebuild buffers. An overdue reform of the pension system would help contain steep future rises in public expenditures. Without reform, costs linked to ageing - health, long-term care and pensions – are set to rise by 2.1 percentage points of GDP between 2024 and 2040. Policies to reduce the reliance on coal and greenhouse gas emissions would boost well-being and make growth more sustainable. Boosting the labour supply of mothers, by expanding the supply of childcare and shortening the maximum length of parental leave, as well as extending working lives would help strengthen growth. Improving skills provision and redesigning immigration policy would help attract and retain skilled labour.

# Denmark

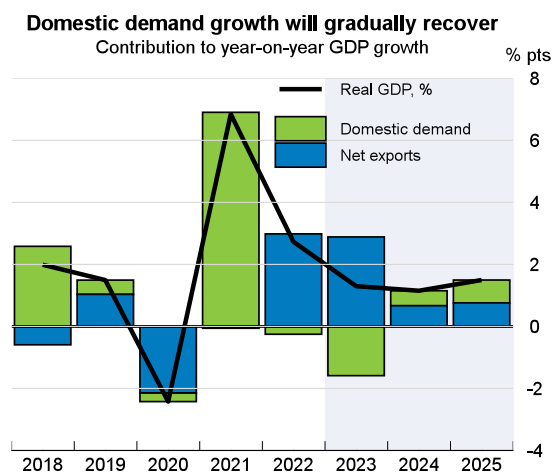
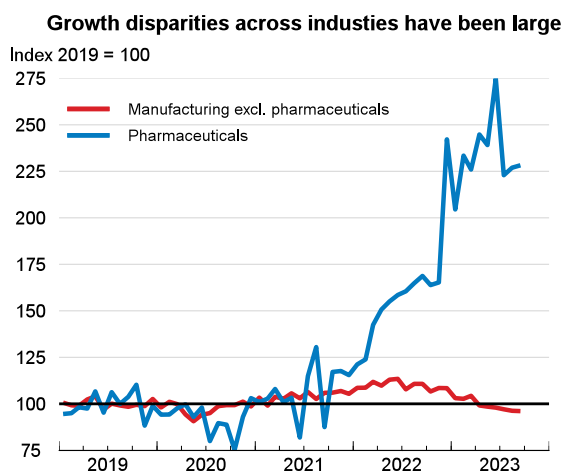
GDP growth is projected to slow to 1.2% in 2024 before recovering to 1.5% in 2025. After a large surge since mid-2022, the growth of the pharmaceutical sector is expected to moderate and exports will lose momentum despite improving foreign demand. Tight financial conditions and weak economic prospects will keep investment low. Nominal wage growth will strengthen, supporting consumption and keeping core inflation above 2% into 2025. Unemployment will increase as firms adjust to higher labour costs and weaker demand. Key risks include a more severe correction in housing and real estate markets and the inflationary impact of labour market developments.

The central bank is expected to keep the interest rate high in line with the euro area to maintain the currency peg. Fiscal policy is projected to be broadly neutral in 2024 and 2025. If inflationary pressures persist relative to the euro area, the government should restrain public spending, for instance on public employment services and business support, while maintaining planned investment in priority areas, notably health, education, and energy infrastructure.

## The economy has been running at two speeds

After a strong first quarter, GDP growth has slowed significantly. Outside the buoyant pharmaceutical sector, the economy is estimated to have contracted by 0.5% in the first half of 2023 as foreign and domestic demand weakened. Private consumption has stabilised thanks to receding inflation and improvements in confidence. However, private investment has declined partly due to lower business confidence and tighter credit conditions. After a sharp fall in prices and sales, since the spring the housing market has started to recover, but developments may be distorted by anticipation of the up-coming property tax reform. While employment has grown, unemployment has increased moderately. Headline inflation fell to 0.1% in October, reflecting strong base effects, while core inflation stood at 3.3%. Underlying price pressures persist as wage growth has strengthened following collective negotiations.

## Denmark



Source: Statistics Denmark; and OECD Economic Outlook 114 database.

StatLink  <https://stat.link/40eth7>



## Denmark: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices DKK billion	Percentage changes, volume (2010 prices)				
<b>Denmark</b>						
<b>GDP at market prices</b>	2 320.9	6.8	2.7	1.3	1.2	1.5
Private consumption	1 073.9	5.5	-1.4	0.6	1.1	1.2
Government consumption	574.2	4.6	-2.8	0.9	2.0	0.9
Gross fixed capital formation	514.3	6.6	3.2	-5.2	-1.3	-0.2
Final domestic demand	2 162.4	5.5	-0.6	-0.8	0.7	0.8
Stockbuilding <sup>1</sup>	8.0	1.8	0.4	-1.0	0.0	0.0
Total domestic demand	2 170.4	7.3	-0.2	-1.7	0.8	0.8
Exports of goods and services	1 279.3	7.7	10.8	7.7	3.3	3.3
Imports of goods and services	1 128.8	8.8	6.5	4.3	2.7	2.5
Net exports <sup>1</sup>	150.5	-0.1	3.0	2.9	0.7	0.8
<i>Memorandum items</i>						
GDP deflator	–	2.9	8.1	-1.5	2.5	2.3
Consumer price index	–	1.9	7.7	3.6	2.8	2.5
Core inflation index <sup>2</sup>	–	1.2	4.0	4.5	3.2	2.5
Unemployment rate (% of labour force)	–	5.2	4.5	5.0	5.8	5.8
Household saving ratio, net (% of disposable income)	–	3.2	9.7	9.2	8.1	6.8
General government financial balance (% of GDP)	–	4.1	3.3	2.8	2.0	1.4
General government gross debt (% of GDP)	–	49.2	34.9	34.5	33.8	35.3
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	36.0	29.8	29.5	28.7	30.3
Current account balance (% of GDP)	–	9.1	13.4	11.5	11.4	11.3

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 114 database.

StatLink  <https://stat.link/asniog>

Economic growth has been mainly driven by a few firms with relatively weak links to the rest of the domestic economy. A surge in demand for medicines patented in Denmark, a significant share of which is produced abroad, has contributed to robust exports, large gains in export market share and a significant current account surplus (11% of GDP in the first half of 2023). By contrast, the weakening of global trade has affected other exporting sectors, including maritime transport. Estimates of productivity growth have declined if firms producing exports abroad (so-called merchanting) are excluded.

## Monetary policy will remain tight and fiscal policy prudent

Financial conditions will remain tight due to high interest rates. Policy rates are expected to decline from 2025 to reach 3.1% at the end of the year. While the fiscal stance is expansionary in 2024 and 2025, the economic impact of fiscal policy is estimated to be broadly neutral over the next two years. Rising public spending on defence and aid to Ukraine, lagged adjustments of social transfers and public sector wages to reflect private sector wage growth, and the normalisation of tax revenues on capital gains will contribute to a decline in budget surpluses, but this will be partly offset by the withdrawal of energy support measures. Aid to Ukraine (around 0.5% of GDP in 2024) will not add to capacity pressures in the economy. In the longer term, population ageing and the green transition will weigh on the budget balance, gradually reducing the significant fiscal space. While spending on pensions is projected to decline thanks to past reforms, healthcare and long-term care will increase by around 0.5% of GDP by 2030.

## **A soft landing is expected, but uncertainty is high**

GDP growth is projected to slow to 1.2% in 2024 before converging to its potential growth rate of 1.5% in 2025. Higher financing and labour costs will take a toll on activity and investment. Wages are projected to increase in line with the euro area and firms will adjust employment to maintain price competitiveness. Even though this and the reopening of the Tyra gas field in 2024 will support exports, they will moderate due to the fading contribution of the pharmaceutical sector and weak external demand. Despite rising debt servicing costs and a fall in employment, the elevated level of savings and wage growth will support the recovery of private consumption and housing investment. As in most other European countries, inflation will decline relatively slowly due to rising unit labour costs. Considerable uncertainty surrounds the outlook. Persistent tensions on the labour market would keep price pressures high, while a sharp adjustment of employment to restore productivity would ease them more than expected. A sharp fall in commercial real estate activity and a deeper correction of house prices would increase loan defaults and reduce credit supply from exposed banks.

## **An agile fiscal policy can support sustainable growth, while keeping inflation low**

Monetary policy should ensure a moderation of inflation and the stability of the peg with the euro. The public finances are in surplus and public debt is low (29.8% of GDP in 2022). However, fiscal policy will need to be tightened if inflationary pressures persist relative to the euro area. Public spending should not be reduced in priority areas. Investment in the green transition should even accelerate to reduce dependence on fossil fuels and achieve decarbonisation targets. Funds allocated to vocational education and to address skills shortages in the public sector should be maintained. Savings could be achieved by improving efficiency in public support to businesses and active labour market policies by phasing out ineffective programmes and developing the digitalisation of services. In the longer run, achieving efficiency gains the public sector will help to maintain the quality of welfare services as costs increase and the fiscal space diminishes.

# Estonia

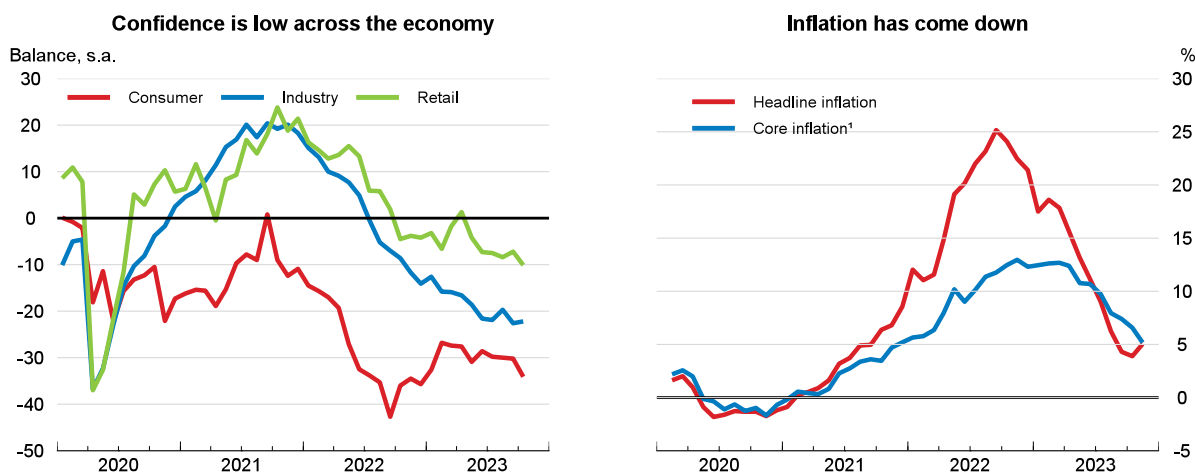
Growth should return in 2024 but will remain subdued at 0.6%, while the labour market is expected to deteriorate. In 2025, growth should reach 2.5% as the recovery in consumption picks up. Inflation has come down substantially, but planned tax increases will bring a temporary spike at the beginning of 2024. Risks to the outlook are tilted to the downside.

Tighter euro area monetary policy has contributed to a tightening of financial conditions and a weakening of the housing market. Fiscal consolidation is underway but needs to be carefully managed. In 2025, changes to the personal income tax parameters should ease the pressure on middle- and high-income households, while a long overdue vehicle tax can provide incentives for the green transition. Any further consolidation in the years ahead should protect low-income households and be guided by effective expenditure reviews.

## The economy remains in recession

Economic growth was weaker than expected this year, with a broad-based contraction of real GDP by 0.19% in the third quarter. Manufacturing was affected by supply problems and close ties to the Nordic markets, where demand for Estonian building products faltered. Higher borrowing costs and inflation have taken a toll on consumption and private investment, as the majority of loans have a variable interest rate. The strong labour market started to weaken. Nevertheless, continued withdrawal of second pillar pension savings and a large inflow of Ukraine migrants have provided a cushion to domestic demand. Business and consumer surveys point to weak confidence.

## Estonia



1. Harmonised index of consumer prices excluding food, energy, alcohol and tobacco.

Source: European Commission, Directorate General for Economic and Financial Affairs (DG ECFIN); and OECD Economic Outlook 114 database.

StatLink  <https://stat.link/fthzg3>

## Estonia: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Estonia</b>						
<b>GDP at market prices</b>	27.4	7.4	-0.5	-2.6	0.6	2.5
Private consumption	13.6	9.3	2.2	-2.3	0.1	1.9
Government consumption	5.7	3.8	0.1	1.4	1.8	2.4
Gross fixed capital formation	7.9	11.3	-4.8	-12.9	1.4	4.1
Final domestic demand	27.3	9.7	-0.3	-4.4	0.8	2.5
Stockbuilding <sup>1</sup>	0.2	1.6	1.2	-1.3	-0.4	0.0
Total domestic demand	27.5	10.2	0.4	-5.5	0.4	2.5
Exports of goods and services	19.0	22.2	3.0	-4.9	0.1	1.2
Imports of goods and services	19.1	23.5	3.3	-5.7	0.0	1.2
Net exports <sup>1</sup>	-0.1	-1.0	-0.2	0.7	0.1	0.0
<i>Memorandum items</i>						
GDP deflator	–	5.7	16.2	8.8	5.2	3.0
Harmonised index of consumer prices	–	4.5	19.4	9.2	3.4	2.4
Harmonised index of core inflation <sup>2</sup>	–	2.8	10.3	8.8	2.9	2.3
Unemployment rate (% of labour force)	–	6.2	5.6	6.6	7.8	7.7
Household saving ratio, net (% of disposable income)	–	3.6	-4.7	-6.4	-1.9	-0.6
General government financial balance (% of GDP)	–	-2.5	-1.0	-3.2	-3.0	-3.1
General government gross debt (% of GDP)	–	24.6	25.5	29.5	33.0	37.5
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	17.8	18.5	20.0	22.2	25.8
Current account balance (% of GDP)	–	-3.1	-3.6	-0.3	0.9	1.7

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 114 database.

StatLink  <https://stat.link/xm1nav>

Exports have been weak for over a year and imports fell in the second quarter as well. The weak demand in the Nordics and the loss of Russian imports are weighing on the economy. Manufacturing is closely linked to housing construction in Finland and Sweden, where tighter financial conditions have slowed activity sharply.

### Tight macroeconomic policies weigh on activity

The tightening of euro area monetary policy has had a strong impact on Estonia, with a weakening of investment and the housing market. Fiscal policy is becoming considerably more restrictive in 2024. As part of the planned fiscal consolidation, the government will increase VAT rates next year and corporate and personal income tax rates in 2025, each by 2 percentage points. Excise taxes and environmental subsidies are also set to rise, and vehicle tax is planned for 2025. In part, the impact of the personal income tax increases will be offset by changes to allowances, which are expected to benefit middle and high-income households disproportionately. The stronger impact of the tax measures on lower-income households will be only partially mitigated by recent increases in the minimum wage. Public investment should remain strong with substantial spending of EU funds expected in the coming years, while defence spending remains a priority at 3% of GDP.

## The economy will slowly recover in 2024

The economy should return to growth next year with real GDP increasing by 0.6% as export markets recover, and business and residential investments begin to pick up. Inflation will continue falling steadily to reach 2.4% in 2025, apart from a policy-induced spike in January 2024 related to the VAT increase. The VAT increase will also induce households to frontload some consumer spending to the end of this year. The unemployment rate is likely to increase to 7.8% in 2024. Real GDP growth should strengthen to 2.5% in 2025 as the recovery progresses both domestically and abroad. Risks to the outlook are tilted to the downside, with weaker than expected developments in exporting markets lowering growth.

## Fiscal consolidation is needed in the years ahead, but needs to be carefully managed

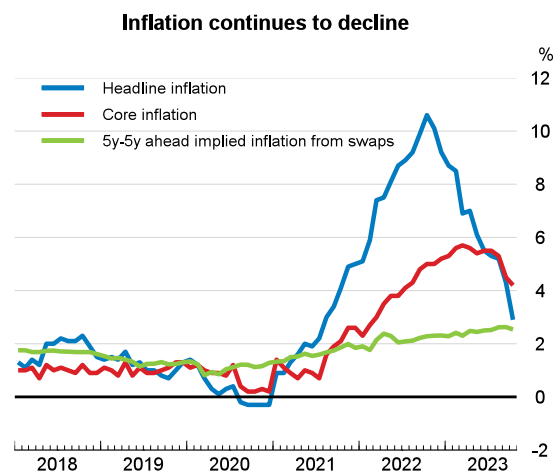
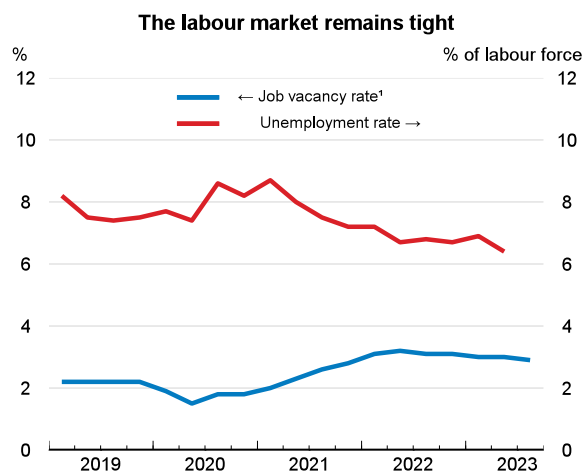
With the budget deficit at over 3% of GDP and spending pressures from higher defence expenditures, healthcare as well as ageing-related costs, some fiscal adjustment is needed in the coming years despite low levels of government debt. The authorities introduced an ambitious fiscal strategy to decrease general government deficit gradually to 1.2% of GDP in 2027. Nevertheless, measures to underpin it are under discussion. Further consolidation should be based on an effective review of expenditures and protect low-income households. The introduction of the vehicle tax is long overdue and needs to provide adequate incentives for the green transition. In the context of increasing wages and to underpin productivity growth, upskilling policies should be broadened.

# Euro area

GDP growth is projected to slow to 0.6% in 2023 before strengthening gradually to 0.9% in 2024 and 1.5% in 2025. Private consumption will be supported by tight labour markets and increasing real incomes as inflation recedes. At the same time, higher costs of financing and uncertainty will weigh on private investment. Wage growth is projected to ease only gradually over the projection period. Employment bottlenecks in services will keep core inflation elevated until mid-2025, despite ongoing reductions in headline inflation.


Persistent core inflation, the rising impact of higher interest rates on the real economy and uncertainty associated with increasing geopolitical risks call for coordinated macroeconomic policies. Prudent fiscal policy is needed to rebuild fiscal space, while the European fiscal rules should be refocused on debt sustainability and multiannual expenditure plans. Monetary conditions need to remain tight to ensure continued disinflation.

## Euro area 1



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.

Source: OECD Labour Statistics database; Eurostat Job vacancy statistics database; Eurostat Harmonised index of consumer prices (HICP) database; and LSEG.

StatLink  <https://stat.link/t2164a>

## Euro area: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>Euro area</b>	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>GDP at market prices</b>	11 421.1	5.9	3.4	0.6	0.9	1.5
Private consumption	5 899.6	4.4	4.2	0.6	1.1	1.6
Government consumption	2 559.2	4.2	1.5	0.1	0.8	0.8
Gross fixed capital formation	2 511.1	3.5	2.7	1.2	0.8	1.5
Final domestic demand	10 969.9	4.1	3.3	0.6	0.9	1.4
Stockbuilding <sup>1</sup>	41.1	0.6	0.4	-0.3	0.1	0.0
Total domestic demand	11 011.0	4.7	3.6	0.3	1.0	1.4
Net exports <sup>1</sup>	410.0	1.3	0.0	0.2	-0.1	0.1
<i>Memorandum items</i>						
GDP deflator	–	2.3	4.6	5.6	2.7	2.2
Harmonised index of consumer prices	–	2.6	8.4	5.5	2.9	2.3
Harmonised index of core inflation <sup>2</sup>	–	1.4	4.0	5.1	3.1	2.3
Unemployment rate (% of labour force)	–	7.7	6.7	6.5	6.6	6.5
Household saving ratio, net (% of disposable income)	–	11.5	7.5	7.5	7.9	7.7
General government financial balance (% of GDP)	–	-5.3	-3.6	-3.3	-2.9	-2.6
General government gross debt (% of GDP)	–	115.5	96.4	96.0	96.8	97.3
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	96.8	92.7	92.2	93.1	93.5
Current account balance (% of GDP)	–	4.1	1.4	3.1	3.0	3.1


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.

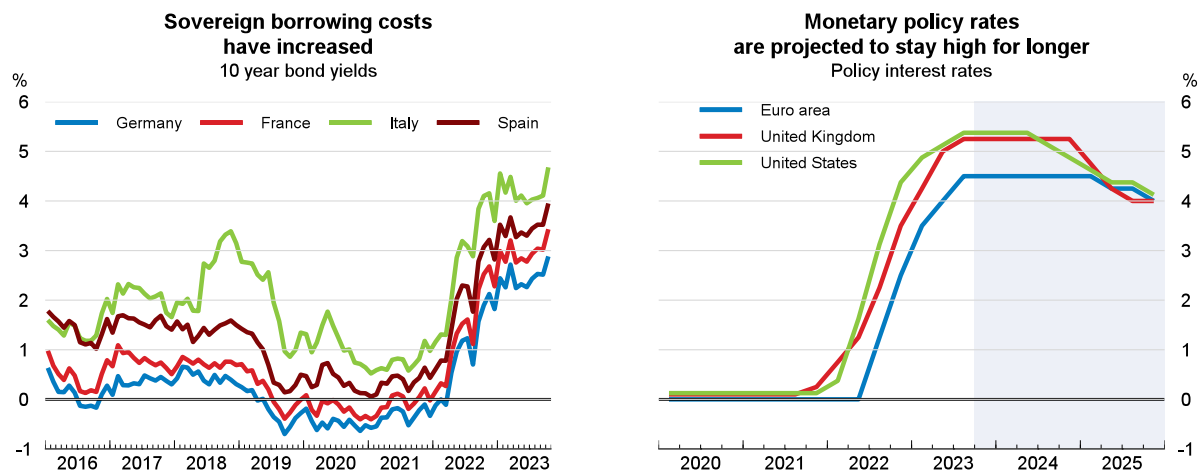
Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/63vmhy>

## Tight financing conditions and geopolitical uncertainty weigh on the outlook

GDP declined by 0.1% quarter on quarter in the third quarter of 2023. Uncertainty has increased further with the worsening geopolitical situation. Forward-looking indicators of sentiment and confidence have deteriorated. Improvements in the composite Purchasing Managers' Indices dissipated in the third quarter of 2023, as manufacturing production continued to decline while confidence as well as output in services weakened. Headline inflation continued to moderate, from 5.2% in August to 2.9% in October. Similarly, core inflation decreased to 4.2% in October. However, underlying inflation remains sticky with services rising by more than 4% in annual terms. Market-based inflation expectations have stabilised above the 2% target even at longer-term horizons. Bank lending to firms and households has continued to weaken amid higher lending rates, lower loan demand and tighter credit standards. At the same time, the labour market has remained tight, with the job vacancy rate just marginally below its recent peak. The euro area seasonally adjusted unemployment rate stood at 6.5% in September 2023, with labour shortages reflected in above-average wage growth in many countries.

## Euro area 2



Source: LSEG; and OECD Economic Outlook 114 database.

StatLink  <https://stat.link/z0np5s>

The increase in US sovereign bond yields in recent months and higher inflation risk premia demanded by investors have increased yields on many euro area sovereign bonds. Against the backdrop of falling equity prices, stock prices of euro area banks increased, outperforming their US counterparts, and lowering the cost of new capital. The economic fallout in the euro area from Russia's war of aggression against Ukraine has been moderate. Direct trade with Russia is low and has been reduced further through multiple rounds of EU-coordinated sanctions. European firms have been resilient during the energy crisis, partly due to strongly reduced demand for energy. Co-ordinated policies have also helped to increase resilience: liquefied natural gas import capacity has been expanded and is well-supplied, with the EU meeting its 90% gas storage target in August, well ahead of the November deadline. Accelerated deployment of renewables has also helped to lower dependence on gas. At the same time, output in the most energy-intensive industries has declined, weighing on growth, and leading to calls for subsidies to national industries that could potentially undermine the EU Single Market. EU countries have recently extended the temporary protection accorded to more than 4 million Ukrainian refugees until March 2025. To help Member States meet the costs of hosting refugees, the EU has made available EUR 21 billion (0.18% of euro area GDP) from the cohesion and pandemic recovery funds.

## Ongoing public investment will help finance the green transition

Comprised of starkly different positions across countries, the euro area fiscal stance is projected to remain restrictive in 2024 and 2025, with cumulative tightening amounting to 1¼% of GDP. Fiscal support to cushion the impact of high energy costs is projected to be withdrawn gradually during 2024. Ensuring that income support is targeted on vulnerable households and avoiding a subsidy race between countries is essential to prevent the deterioration of public finances and provide the needed macroeconomic policy tightening. At the same time, the war in Ukraine has led to an ongoing increase in military spending, and the Next Generation EU (NGEU) programme has triggered investments to secure energy supply and accelerate the green transition of about 1% of euro area GDP per year. This spending needs to be delivered effectively.



The ECB has continued to tighten monetary policy, bringing the deposit rate to 4% and the rate on main refinancing operations to 4.5%, both at historic highs. Policy rates are projected to stay at this level into 2025, to durably reduce the underlying inflationary pressures that are keeping core inflation elevated. A period of below-trend growth will help lower resource pressures, including from buoyant labour markets and the short-term effects of additional public expenditure associated with the NGEU programme. Public investment is estimated to increase by as much as 2.5% of GDP until the end of the NGEU programme in 2026, crowding in private investment amounting to 5% of GDP. The main refinancing rate is projected to remain unchanged until the second quarter of 2025 and then gradually decrease to 4% at the end of the projection period.

### **Growth will strengthen in 2024 as domestic demand picks up**

Quarterly growth is projected to remain weak in the near term, amid tightening financial conditions, rebounding energy and commodity prices, and elevated uncertainty. Despite robust wage growth, consumer price inflation of 5.5% in 2023 will continue to weigh on incomes and private consumption. However, real disposable incomes will recover as disinflation continues over the projection period. Investment will be held back by higher uncertainty and tight financing conditions, although additional spending under the NGEU programme will partly offset this. Headline inflation is projected to moderate further, to 2.9% in 2024 and 2.3% in 2025, with weak domestic demand growth helping to contain price and cost pressures. Core inflation is also projected to decline, albeit at a slower pace, returning to the ECB inflation target by the end of 2025.

The risks to the projections are to the downside. Energy prices may rebound on the back of elevated geopolitical uncertainty, especially during the upcoming winter months. Trade tensions may deteriorate further and could weigh on external demand and rekindle inflationary pressures. Financial stability risks remain elevated, as the effects of higher interest rates could trigger losses from defaulting loans and real estate exposures. Moreover, interest rates may need to stay high for longer than expected, or even rise further, heightening the risk of a recession and the exposure of financial sector vulnerabilities, particularly among non-bank financial intermediaries. On the upside, a stronger decline in elevated household saving rates could support private consumption. In addition, a durable reduction of geopolitical uncertainty could alleviate upward pressure on energy and commodity prices, and a stronger recovery in China could help lift external demand.

### **Macroeconomic policies need to stay the course to reduce inflation**

The investment needs associated with improvements in energy security and decarbonisation policies are substantial. At the same time, prudent fiscal policy is needed to support ongoing monetary policy tightening and to continue rebuilding fiscal space. Effective disbursement of the Next Generation EU funds will help expand productive capacity in the medium term, but requires careful design and monitoring at the EU level. To avoid harmful subsidy races and ensure a level playing field, state-aid rules should not be relaxed further, and existing budgetary resources should be re-directed towards support for green R&D, innovation and early-stage support coordinated at the EU level. The monetary policy stance should remain restrictive, complemented, as needed, by macroprudential policy and the use of targeted instruments to address vulnerabilities in the financial sector.

# Finland

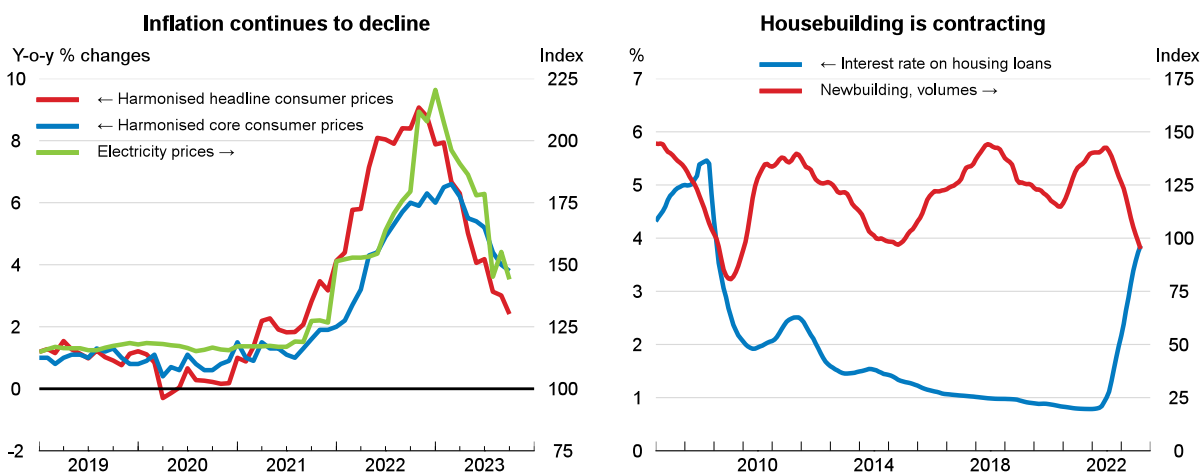
GDP is projected to stall in 2023 and grow by a moderate 0.9% in 2024, before picking up to 1.8% in 2025. As energy prices ease, private consumption is set to recover moderately in 2024 despite the drag from higher interest rates, which together with declining house prices will weigh on residential investment. Unemployment is expected to slowly increase until mid-2024 before starting to decline, as the economy grows and employment growth gains momentum. Lower energy prices and weak demand should help bring headline inflation down from 7.2% in 2022 to 4.5% in 2023 and 2.2% in 2024.

The planned increase in defence and security spending, as well as moderate tax cuts, will outweigh cuts to spending on other items in 2024 and 2025; as a result, fiscal policy is projected to remain expansionary. Given rising public debt, earlier fiscal consolidation would be more appropriate. Improving female and senior labour force participation is necessary to boost labour supply in an ageing society, in addition to the planned reforms of unemployment insurance. Further investing in decarbonisation is also paramount.


## Consumer and business confidence remains depressed

The Finnish economy expanded sluggishly in the first half of 2023 as the drop in investment was milder than expected, but contracted by 0.9% in the third quarter according to flash estimates. High inflation and rising mortgage rates are still a drag, albeit a fading one, on households' purchasing power. After falling by over 7% in the previous two years, real wages rose by 1.4% in the third quarter of 2023. However, consumer confidence declined in August and industrial confidence has kept declining since early 2022. Against the backdrop of weak demand, the unemployment rate edged up to 7.3% in September, while headline and core inflation continued to decline. The drop in measured headline inflation is magnified by the downward correction of the electricity price index by Statistics Finland in August 2023, which will affect year-on-year headline inflation until July 2024.

## Finland



Source: European Central Bank; Statistics Finland; and Bank of Finland.

StatLink  <https://stat.link/j2vclu>

## Finland: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Finland</b>						
<b>GDP at market prices</b>	238.0	3.2	1.6	0.0	0.9	1.8
Private consumption	121.8	3.5	1.7	-0.5	0.2	1.7
Government consumption	57.7	3.9	0.8	8.6	1.2	1.0
Gross fixed capital formation	57.2	1.0	3.2	-3.9	1.7	3.0
Final domestic demand	236.7	3.0	1.8	0.8	0.8	1.8
Stockbuilding <sup>1,2</sup>	1.1	0.0	1.4	-2.2	0.2	0.0
Total domestic demand	237.9	3.1	3.3	-1.3	1.0	1.9
Exports of goods and services	85.2	5.8	3.7	0.1	2.8	3.1
Imports of goods and services	85.0	6.0	8.5	-4.7	2.0	3.3
Net exports <sup>1</sup>	0.2	-0.1	-1.9	2.3	0.3	-0.1
<i>Memorandum items</i>						
GDP deflator	–	2.2	5.4	4.5	2.5	2.3
Harmonised index of consumer prices	–	2.1	7.2	4.5	2.2	2.3
Harmonised index of core inflation <sup>3</sup>	–	1.2	3.6	4.2	2.8	2.3
Unemployment rate (% of labour force)	–	7.6	6.8	7.2	7.4	7.1
Household saving ratio, net (% of disposable income)	–	2.8	-0.9	0.1	2.2	1.7
General government financial balance (% of GDP)	–	-2.8	-0.8	-2.6	-3.4	-3.1
General government gross debt (% of GDP)	–	85.2	80.2	82.2	84.7	87.5
General government debt, Maastricht definition <sup>4</sup> (% of GDP)	–	72.5	72.5	74.5	77.0	79.8
Current account balance (% of GDP)	–	-0.1	-2.4	-0.4	-0.1	-0.1

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 114 database.

StatLink  <https://stat.link/0npiod>

Cost pressures from abroad have been mixed. Lower world food prices are helping moderate inflation in Finland, but oil prices have increased again since July. Russia's war of aggression against Ukraine has closed Russian supplies for some of Finland's imports, pushing up costs, and weighed on tourism exports. The recent damage to the gas pipeline and telecom connector with Estonia is unlikely to have a meaningful impact given alternative infrastructure and low Finnish reliance on natural gas.

## Fiscal policy will remain accommodative in the near term

The continued tightening of monetary policy by the European Central Bank is affecting lending conditions for households and businesses in Finland. House prices declined by 5.6% during the year to mid-2023. Given the high share of variable- or adjustable-rate mortgages, interest rate increases make it harder to service household debt and could put additional pressure on house prices and consumption. Except for emergency loans and credit guarantees for utilities until the end of 2024, all emergency support measures have been wound down in the first half of 2023. The government's current budget proposals include cuts in environmental and social spending, but they will not be enough to offset the proposed increase in security and defence spending, as well as tax breaks. The fiscal stance is projected to ease by about 1% of GDP in 2023 and ½ per cent in 2024, and be broadly neutral in 2025. Consolidation is foreseen in the Government's budget from 2026 onwards. Gross public debt is expected to increase to about 80% of GDP by end-2025. Despite the gradual increase in the retirement age, ageing-related costs are expected to increase by about 2½ per cent of GDP by 2040.

## Growth is expected to pick up gradually in 2024

Underpinned by modest real income growth, private consumption is set to recover in early 2024. Higher interest rates, tighter credit conditions and declining house prices will continue to hold back residential investment. Weak internal demand will slow import growth, leading to a positive contribution of net exports. Unemployment will inch up further to 7.4% by end-2023 but start falling in 2024 as the economy and job creation regain momentum. Headline inflation is expected to decline gradually over 2024 and 2025. Core inflation is expected to decline more slowly than headline, as labour costs are passed through to prices. While Finnish reliance on natural gas is low, the economy is still exposed to the risk of a cold winter in Europe, with spillovers to electricity prices and weak external demand. Finland is also exposed to a risk of higher security tensions with Russia. Higher mortgage rates and energy prices would also further undermine confidence and purchasing power.

## Improving the fiscal balance and boosting employment are key

Productivity growth has been weak. Investing in R&D, digitalisation and tertiary education can sustainably boost productivity growth and innovation. Along with earlier fiscal consolidation – by foregoing some of the planned tax cuts on fuels and for homebuyers – raising growth will help stabilise the debt-to-GDP ratio. Enhancing the labour force participation of women and seniors is also key to address the growing old-age dependency ratio. Finally, accelerating the transition towards decarbonised energy sources (wind, solar, nuclear) is also crucial for increased energy security and meeting Finland's greenhouse gas emissions reduction goals.

# France

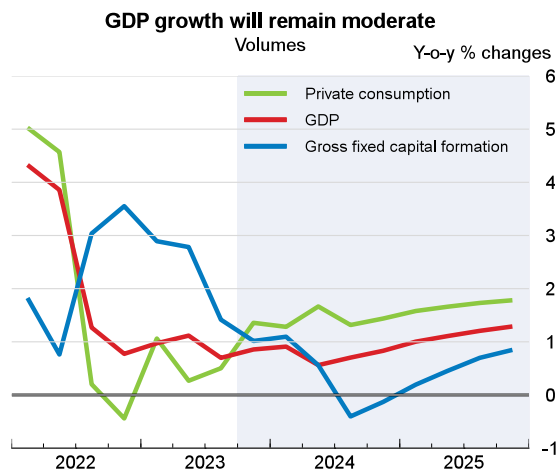
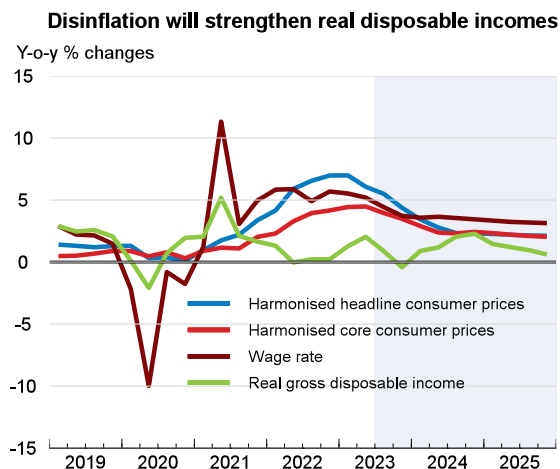
GDP growth is expected to ease from 0.9% in 2023 to 0.8% in 2024 before picking up to 1.2% in 2025. After a slowdown in 2024, exports will recover in 2025 owing to a moderate improvement in external demand. Continued tightness in the labour market will maintain upward pressure on wages, allowing for some gains in purchasing power and a gradual improvement in private consumption, as inflation is expected to ease from 5.7% in 2023 to 2.7% in 2024 and 2.2% in 2025. However, less favourable financing conditions due to tighter monetary policy will continue to weigh on investment and consumption.

Fiscal support measures adopted to shield households and firms from high energy and food prices should be phased out, accelerating the much-needed fiscal consolidation. Despite announced spending cuts, the budget deficit is expected to remain large, at 4.6% of GDP in 2025. Efforts to promote green alternatives to fossil fuels, housing renovation and energy savings should be strengthened. Enhancing access to high-quality education will be key to achieve greater equity and further reduce gender imbalances.


## Activity is slowing in the second half of 2023

GDP growth eased to 0.1% in the third quarter of 2023, and business survey indicators point to persisting weakness in growth in the last quarter of the year. The composite purchasing managers index remained well below the expansion threshold in October, while the Insee business climate indicator fell below its long-term average. Employment continued to increase in the first half of 2023 and the unemployment rate has remained broadly stable since the beginning of the year, standing at 7.3% in September 2023 against 7.2% in December 2022. Inflation remains high at 4.5% in October 2023, according to the harmonised index. Core inflation has fallen to 3.5%, from a peak of 4.7% in April, but energy prices have recently rebounded, and annual food price inflation remains elevated at 8.0%. Amid a tight labour market and persistent inflation, the average nominal wage per employee continues to grow strongly at 5.7% year-on-year.

## France 1



Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/6as58f>

## France: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2014 prices)				
<b>France</b>						
<b>GDP at market prices</b>	2 316.9	6.4	2.5	0.9	0.8	1.2
Private consumption	1 232.7	5.1	2.3	0.8	1.4	1.7
Government consumption	575.7	6.5	2.6	0.6	1.0	0.6
Gross fixed capital formation	539.0	10.2	2.3	2.0	0.3	0.5
Final domestic demand	2 347.4	6.6	2.4	1.1	1.0	1.2
Stockbuilding <sup>1</sup>	18.2	-0.6	0.7	-0.5	0.0	0.0
Total domestic demand	2 365.6	6.0	3.1	0.6	1.0	1.2
Exports of goods and services	633.3	10.7	7.4	1.1	0.9	1.9
Imports of goods and services	682.1	9.1	8.8	0.3	1.5	1.7
Net exports <sup>1</sup>	- 48.7	0.2	-0.6	0.3	-0.2	0.0
<i>Memorandum items</i>						
GDP deflator	–	1.4	2.9	5.3	2.5	2.0
Harmonised index of consumer prices	–	2.1	5.9	5.7	2.7	2.2
Harmonised index of core inflation <sup>2</sup>	–	1.3	3.4	4.1	2.5	2.2
Unemployment rate <sup>3</sup> (% of labour force)	–	7.9	7.3	7.2	7.4	7.5
Household saving ratio, gross (% of disposable income)	–	18.6	17.2	17.3	17.4	16.9
General government financial balance (% of GDP)	–	-6.5	-4.8	-4.9	-4.9	-4.6
General government gross debt (% of GDP)	–	138.7	117.9	118.2	120.9	123.2
General government debt, Maastricht definition <sup>4</sup> (% of GDP)	–	113.0	111.8	112.1	114.8	117.1
Current account balance (% of GDP)	–	0.4	-2.0	-0.7	-0.9	-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.

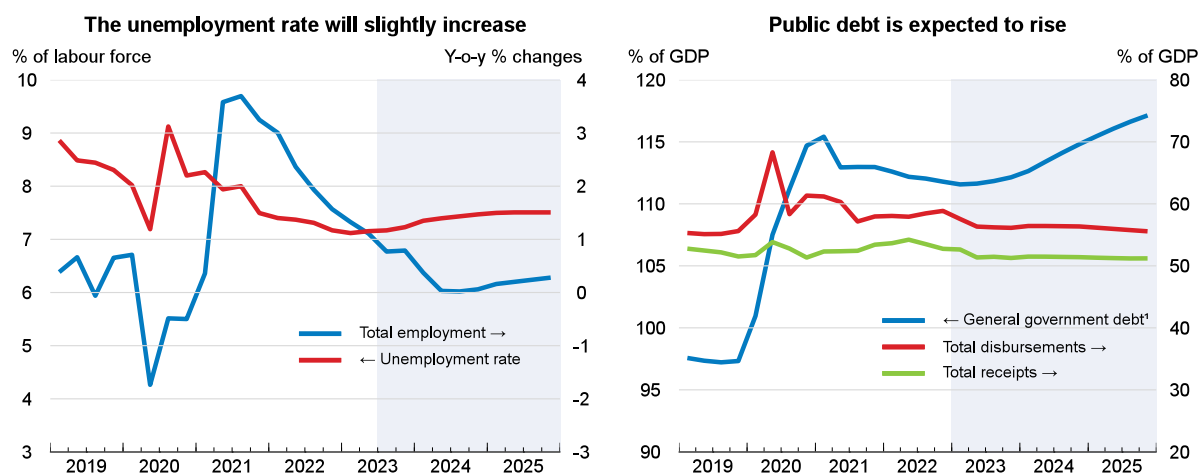
3. National unemployment rate, includes overseas departments.

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 114 database.

StatLink  <https://stat.link/htksz9>

## France 2



1. Maastricht definition.

Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/zihp9s>

Foreign demand growth slowed in 2022 and 2023, amid high inflation and tighter financial conditions in partner countries. As inflationary pressures ease in major trading partners, external demand is expected to gradually gather momentum in 2024 and 2025. In 2022, the trade deficit widened amid rising commodity prices, reaching 3.9% of GDP. With lower energy and raw food prices, it has narrowed this year to 2.5% of GDP in the third quarter.

### **Financial conditions are less accommodative, and fiscal support is fading**

With higher interest rates, credit and private investment have slowed. Growth in housing loans declined from 6.3% year-on-year in September 2022 to 1.8% in September 2023, while loans for consumption and corporate loans have also slowed significantly. At the same time, the implementation of the Next Generation EU plan is supporting public investment, with EUR 40.3 billion of grants planned between 2021 and 2026, equivalent to 1.6% of GDP.

Fiscal support is expected to be gradually reduced, with the budget deficit projected to narrow from 4.9% in 2023 to 4.6% of GDP in 2025. In September, the government presented its draft 2024 budget for discussion in parliament, which was largely in line with the 2023-2027 Stability Programme published in April. Part of the support measures to shield households from high inflation will stay in place next year, notably the cap on regulated electricity prices, which will be phased out by the end of 2024. A similar scheme for natural gas came to an end in June 2023. Low-income households will receive lump-sum payments of 100 euros per car as compensation for the rise in fuel prices in early 2024, at a fiscal cost of EUR 500 million. Overall, with the gradual withdrawal of support measures, the fiscal stance is expected to be tightened by 0.5% of GDP in 2023 and 2024; and 0.4% in 2025. A recent pension reform came into effect in September, including a gradual increase in the retirement age that is expected to raise the labour force and stimulate employment.

### **Improving external demand will support a moderate recovery in 2025**

GDP growth is expected to ease slightly in 2024 and to improve in 2025. In 2024, a lacklustre international environment will limit exports while higher financing costs will weigh on private investment and consumption. In 2025, easing inflation and a moderate improvement in external demand will help GDP growth pick up. Investment will recover only slowly due to persistently tight financial conditions, while the support from NGEU funds is expected to remain constant until the end of 2025. In spite of a slight increase in the unemployment rate, the labour market will remain quite tight, which will continue to fuel wage growth. This will put some upward pressure on prices, even as inflation eases, but also prop up real disposable incomes. The indexation of some social security benefits on past inflation will further support households' purchasing power. Consequently, private consumption growth is expected to strengthen gradually.

The ongoing slowdown in the housing market could become more pronounced than projected, potentially resulting in a stronger fall in housing investment. To date, prices have only fallen by 0.8% from their end-2022 peak. Steeper declines in house prices would further lower household wealth. Labour hoarding, which has been strong since the onset of the pandemic, is projected to lessen but could do so more rapidly than expected. Job losses would then weigh on income and consumption. On the other hand, stronger-than-expected spending of savings accumulated during the pandemic could lead to a stronger boost in private consumption, although this would also add to inflationary pressures.

## Effective fiscal consolidation should be combined with growth-enhancing policies

France should adopt a medium-term fiscal plan to step up the pace of fiscal consolidation. A spending review in 2023 identified a number of priority areas for raising spending efficiency, with potential savings of around EUR 10 billion (0.4% of GDP) per year by 2027. This initiative is welcome, but additional efforts will be necessary to reduce government debt more substantially. Debt stood at 111.8% of GDP at the end of 2022 and is projected to continue rising. Pension, health and long-term care expenditure related to ageing is expected to raise public spending by about 4% of GDP by 2040. The pension reform, effective since September, will help to reduce future spending, but is not expected to balance the accounts of the pension system. Fiscal consolidation could be accelerated through effective measures to boost potential growth. A rapid and complete implementation of the national Recovery and Resilience Plan would help, particularly as the plan entails numerous reforms that would help to green the economy, aid the digital transformation, reduce administrative burdens, improve the coordination of public employment services, and revamp the health strategy at national and local levels. Potential growth could be boosted by implementing policies to make the education system more effective and inclusive from an early age, such as reducing class size in disadvantaged neighbourhoods or promoting innovative practices in teacher training to meet the different needs of pupils.



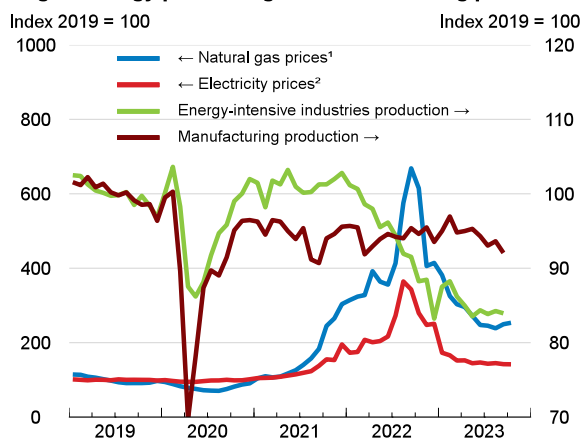
# Germany

The economy is projected to grow by 0.6% in 2024 and 1.2% in 2025, after contracting slightly in 2023. Decreasing inflation and rising wages will support real incomes and private consumption. High interest rates will weigh on residential investment and damp export demand for investment goods. However, non-residential investment will gradually pick up due to support from high corporate savings and investment needs related to the relocation of supply chains, digitalisation and renewable energy expansion. This will be supported by rising public investment and fiscal incentives for green investments. Exports will slowly recover as global demand strengthens.

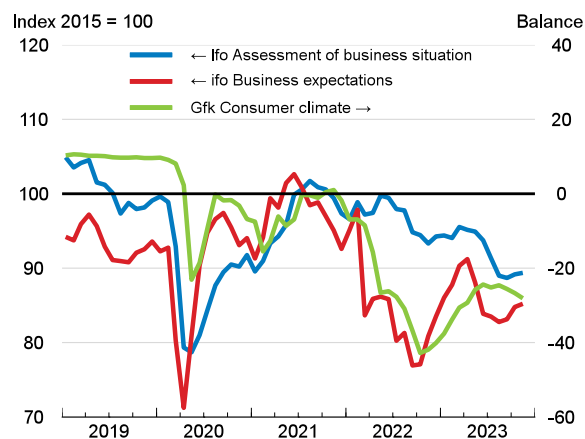
The decreasing fiscal deficit will help contain inflationary pressures. Improving infrastructure planning, approval processes and implementation capacity, particularly at the municipal level, would accelerate the energy transition and digitalisation. Skilled labour force shortages should be addressed by strengthening the work incentives of women, older workers and low-income earners, improving training and adult learning, and facilitating the recognition of the qualifications of migrants and refugees. Raising the quality of basic education and expanding access to early-childhood education is key to increase potential growth and reduce inequality.

## Germany 1

### Higher energy prices weigh on manufacturing production



### Business and consumer confidence are low



1. Prices of natural gas sold to industry.
  2. Electricity prices, when delivered to special contract customers.
- Source: Federal Statistical Office; ifo business surveys; and GfK.

StatLink  <https://stat.link/1eiyyk>

## Germany: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Germany</b>						
<b>GDP at market prices</b>	3 396.7	3.1	1.9	-0.1	0.6	1.2
Private consumption	1 706.6	1.5	3.9	-0.7	0.6	1.4
Government consumption	749.6	3.1	1.6	-2.5	0.5	0.6
Gross fixed capital formation	730.4	-0.3	0.2	1.4	1.2	1.7
Final domestic demand	3 186.6	1.5	2.5	-0.6	0.7	1.3
Stockbuilding <sup>1</sup>	14.5	0.9	0.7	0.0	0.1	0.0
Total domestic demand	3 201.2	2.5	3.4	-0.5	0.8	1.3
Exports of goods and services	1 473.3	9.5	3.4	-0.7	0.5	2.3
Imports of goods and services	1 277.7	8.8	6.8	-1.3	0.9	2.4
Net exports <sup>1</sup>	195.6	0.8	-1.2	0.3	-0.2	0.0
<i>Memorandum items</i>						
GDP without working day adjustments	3403.7	3.2	1.8	-0.3	0.6	1.1
GDP deflator	–	3.0	5.3	6.3	2.4	1.7
Harmonised index of consumer prices	–	3.2	8.7	6.2	2.7	2.1
Harmonised index of core inflation <sup>2</sup>	–	2.2	3.9	5.2	3.1	2.3
Unemployment rate (% of labour force)	–	3.6	3.1	3.0	3.0	2.9
Household saving ratio, net (% of disposable income)	–	14.6	11.5	11.7	12.1	11.9
General government financial balance (% of GDP)	–	-3.7	-2.5	-2.2	-1.6	-0.9
General government gross debt (% of GDP)	–	79.3	65.5	65.4	66.3	66.3
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	69.2	66.2	66.1	66.9	67.0
Current account balance (% of GDP)	–	7.8	4.4	6.7	6.9	6.9

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.

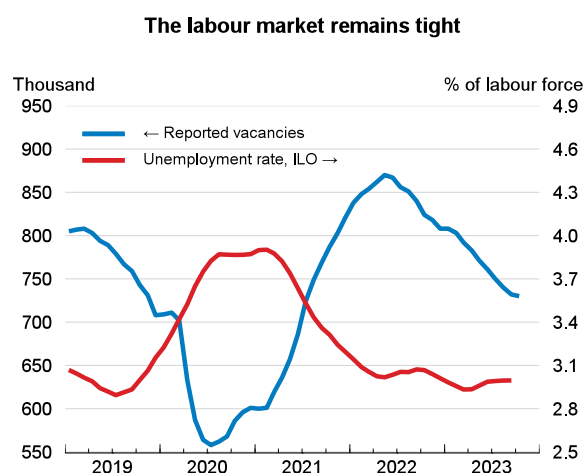
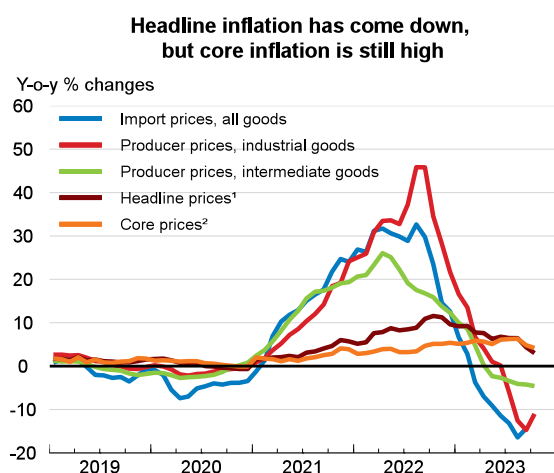
Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/tzn5v3>

## Weak export demand weighs on growth

GDP stagnated in the first three quarters of 2023. Strong nominal wage gains and decreasing inflation stabilised real wages and private consumption. Due to falling energy prices, headline inflation dropped to 3% in October from 4.3% in September, while core inflation remained high at 4.3%. Business investment increased strongly since January despite rising interest rates and weak confidence, but exports declined. Industrial production has fallen since early 2023, with the strong decline in energy-intensive industries partly offset by support for other manufacturing sectors from easing supply chain bottlenecks and a large order backlog. Business expectations have weakened this year, but slightly improved since September, alongside factory sales data. Incoming manufacturing orders rose in August and September, mainly driven by export orders signalling a stabilisation of export demand. The unemployment rate remained at 3% in September.

## 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/phlwig>

High interest rates weigh on global demand for investment goods, which make up a large share of German exports. Export values continued to decline in September and were 7.5% lower than September 2022. Monthly exports to other EU countries declined by 2.1% in September compared to August, while exports to non-EU countries increased by 1.7% in October, mainly driven by rising exports to the United States. Easing supply-chain bottlenecks will continue to help firms meet bulk orders in machinery and equipment industries and support manufacturing activity.

## Public investment and fiscal incentives for private investment will support the recovery

The national debt brake has been reinstated in 2023 after suspension during 2020-2022. Government consumption strongly decreased in 2023 due to the phase-out of pandemic-related health spending. However, the government plans to finance a range of policy priorities until 2026 using special extra-budgetary funds. These funds were endowed with about EUR 400 billion during the suspension of the debt brake, and their net spending is not bound by the national debt brake. The Climate and Transformation Fund (KTF) is supposed to spend about 1%, 1.5% and 1.2% of GDP in 2023, 2024 and 2025 respectively on subsidies and public investment to support the green transition. The net outflow from this fund, which will affect the fiscal deficit according to Maastricht criteria, will be smaller, as the fund also receives about 0.5% of GDP in carbon tax revenues in 2023, increasing to 0.8% in 2025 due to planned increases in the national carbon tax from EUR 30 to 50 per ton of CO<sub>2</sub> during this period. A Supreme Court ruling in November 2023 resulted in a reduction of EUR 60 billion in borrowing allowances available for the KTF, which will particularly affect spending plans for 2025 and 2026. Defence spending will increase to 1.6% of GDP in 2023 and 1.9% of GDP in 2024 and 2025 due to spending from a special defence fund, which has been endowed with EUR 100 billion to improve defence equipment, while core budget spending for defence will likely remain around 1.3% of GDP.

The electricity and gas price subsidies, which are in place until December 2023 with a possible extension until April 2024, are financed by the energy support fund, which has been endowed with EUR 200 billion. Falling retail energy prices will likely result in lower-than-expected fiscal costs from gas and electricity price subsidies, at about 0.9% of GDP in 2023 and 0.1% of GDP in 2024. Phasing out the value added tax reduction for gas as planned would help to strengthen energy saving incentives. The overall fiscal stance is expected to be contractionary in both 2024 and 2025, with cumulative tightening of around 1.7% of GDP, while public debt will slightly increase to 67% of GDP in 2025. The November ruling of the Supreme Court on the KTF might also have consequences on the use of other special funds, requiring additional financing of their spending plans through revenue increases and spending cuts in other areas, which might lead to further fiscal tightening.

### **The economy will slowly recover**

The economy is projected to contract slightly in 2023 and grow by 0.6% in 2024 and 1.2% in 2025. Private consumption will lead the recovery due to declining inflation and rising nominal wages amidst a tight labour market. High interest rates will continue to weigh on housing investment and export demand but easing supply chain bottlenecks and the order backlog will provide some support for manufacturing activity. Business investment will pick up due to high corporate savings and investment needs, supported by rising public investment and fiscal incentives for green investments. Government consumption will start to increase due to ageing-related spending for health and pensions, which is expected to increase by 0.3 percentage points of GDP until 2025, and rising public sector wages. Tighter monetary conditions, fading energy price pressures and fiscal tightening will help to bring down inflation from 6.2% in 2023 to 2.7% in 2024 and 2.1% in 2025.

A major downside risk arises from geopolitical tensions leading to further energy or trade disruptions and the need to relocate supply chains. Continuing political uncertainty related to the financing of support policies for firms and workers during the green transition could weigh on investment and private consumption. If more fiscal tightening is needed to sustain the spending plans of extra-budgetary funds, GDP growth and inflation will be lower. A stronger recovery in China could significantly improve the outlook.

### **Advancing the green and digital transitions requires more investment**

To expand renewable energy supply and raise energy security, it is crucial to continue shortening the time needed to navigate complex planning and approval procedures at the municipal and Länder levels. Speeding up digitalisation will require more investment in digital infrastructure and a more rapid modernisation of the public sector, including by setting mandatory common IT standards and encouraging the harmonization of 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 needed public investment. To address rising labour shortages, which also risk derailing private and public renewable energy investment, the labour market participation of women, low-skilled and elderly workers needs to be raised by setting the right tax incentives, improving training and providing adult learning opportunities. Reforming the current joint income taxation of couples would help raise female labour supply and reduce gender disparities.

# Greece

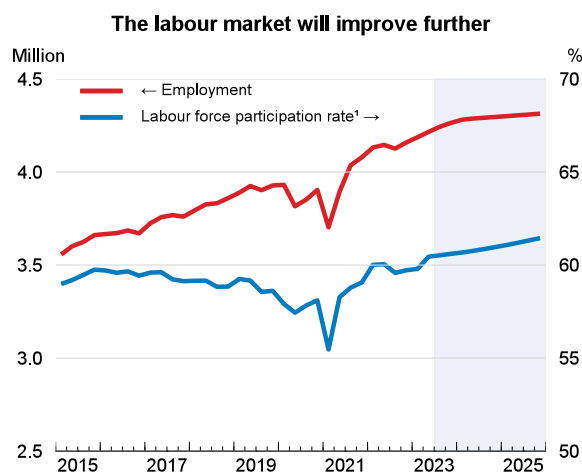
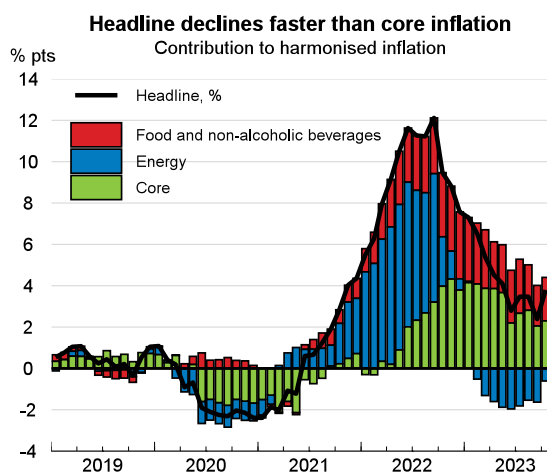
Growth is projected to slow from 2.4% in 2023 to 2.0% in 2024 before picking up to 2.4% in 2025. Real consumption growth has slowed due to high living costs and damage from recent weather events, but will pick up as gradually declining inflation and continued employment growth raise households' purchasing power. Improvements in the business environment, increasing disbursements of European Union funds and strengthening global economic conditions will support investment and exports. The decline in headline inflation will be slowed by wage pressures arising from labour shortages.

Achievements in structural reforms and debt reduction have been reflected in Greece's sovereign debt rating, which returned to investment grade in September 2023. With still low labour productivity, further reforms to remove obstacles to invest – notably in the justice system – and improve skills should be priorities to achieve higher living standards and ensure long-term fiscal sustainability. Recent wildfires and floods emphasise the need to adapt to a hotter climate, notably by broadening property insurance coverage.

## Greece's economy remains robust

GDP rose by 1.3% over the first two quarters of 2023. Private consumption was supported by expanding employment, which is at its highest level since 2010, and by slowing inflation. The rapid fall in the unemployment rate is contributing to rising wages; wage cost indices rose by 4.3% in the year to the second quarter of 2023. Headline inflation dropped to 3.8% in the year to October 2023 as energy prices eased. Real investment grew by 7.9% in the year to the second quarter of 2023, despite rising borrowing costs. Business expectations remained positive in October 2023 and purchasing managers' expectations continued to point towards expanding demand. Forest fires and floods caused large economic damage in mid-2023, especially among manufacturing and agricultural sectors.

## Greece



1. Labour force participation rate, as a percentage of population aged 15-74.

Source: Eurostat; and OECD Economic Outlook 114 database.

## Greece: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Greece</b>						
<b>GDP at market prices</b>	165.3	8.3	6.0	2.4	2.0	2.4
Private consumption	115.5	7.8	8.0	3.1	1.4	1.6
Government consumption	37.6	3.7	-0.9	0.5	0.0	0.8
Gross fixed capital formation	19.3	19.6	11.7	6.4	5.2	6.2
Final domestic demand	172.4	8.3	6.6	3.0	1.6	2.1
Stockbuilding <sup>1,2</sup>	5.5	-0.9	1.9	-1.7	0.9	0.0
Total domestic demand	177.9	7.4	8.2	1.3	2.5	2.0
Exports of goods and services	52.9	21.9	4.5	3.1	0.9	3.3
Imports of goods and services	65.5	16.1	10.0	0.7	2.0	2.4
Net exports <sup>1</sup>	- 12.6	0.7	-3.1	1.1	-0.5	0.3
<i>Memorandum items</i>						
GDP deflator	–	2.1	7.6	5.6	3.8	2.3
Harmonised index of consumer prices	–	0.6	9.3	4.3	2.8	2.4
Harmonised index of core inflation <sup>3</sup>	–	-1.1	4.6	5.7	3.2	2.5
Unemployment rate (% of labour force)	–	14.7	12.4	10.9	10.0	9.9
General government financial balance <sup>4</sup> (% of GDP)	–	-6.9	-2.3	-2.1	-1.4	-1.0
General government gross debt (% of GDP)	–	225.8	191.7	183.6	177.7	173.1
General government debt, Maastricht definition <sup>5</sup> (% of GDP)	–	193.5	171.0	162.8	157.0	152.4
Current account balance <sup>6</sup> (% of GDP)	–	-6.7	-10.2	-6.6	-6.7	-4.7

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 114 database.

StatLink  <https://stat.link/kzr3yl>

Euro area monetary policy tightening has slowed growth in new lending to households and firms, although it remains high. Improvements in Greece's sovereign debt rating partly offset tightening international financial conditions: spreads to German 10-year government bonds have nearly halved since October 2022. Risks of energy supply disruptions have eased. Energy prices in October 2023 were 22% lower than the peak in September 2022. However, food prices, increased by 10.3% over the year to October 2023. Tourism exports have held up, but goods exports declined by 15% in the year to the second quarter of 2023.

### The primary surplus will improve further

Greece is expected to achieve growing primary surpluses, from 1.1% in 2023 to 2.1% in 2025. This will contribute to a rapid decline in the debt-to-GDP ratio from 163% in 2023 to 152% in 2025. That said, the fiscal stance is expected to remain broadly neutral and tighten modestly by around 0.2% of GDP between 2023 and 2025. Growing tax revenues and the phase out of energy and food price subsidies, which amount to EUR 1% of GDP in 2023, create some fiscal space for new fiscal interventions according to the government's budget. Measures worth 0.7% of GDP in 2023 and 1.1% of GDP in 2024 raise incomes of pensioners, civil servants, and low-income groups, though previous pension reforms are expected to contain public expenditures. Government compensation for damages from forest fires and floods is estimated at 0.3% of GDP in 2023. Clearing current delays in implementing investments from the Recovery

and Resilience Fund will boost investment, with spending expected to rise from 1% of GDP in 2023 to 2% of GDP in 2025.

### **Growth is projected to recover slowly**

Output growth is projected to moderate to 2.4% in 2023 and 2.0% in 2024 before picking up to 2.4% in 2025. The previous decline in purchasing power and damages from forest fires and floods are projected to initially slow consumption growth. Rising borrowing costs will temporarily weigh on investment. Both real consumption and investment growth are projected to pick up as inflation declines further and the external environment improves. Continued employment and wage growth will help rebuild households' purchasing power. An improved business environment and continued support through Greece's Recovery and Resilience Plan "Greece 2.0" are projected to spur investment. The decline in inflation is likely to slow as growing capacity constraints contribute to wage pressures. More persistent inflation, or renewed energy and supply disruptions, are key risks and would lower consumption and investment growth.

### **Boosting productivity and tackling climate change are key challenges**

Despite the welcomed reductions in the public debt burden, the level of debt remains high. Achieving primary surpluses of at least 1.5% of GDP into the longer-term and supporting strong growth are important for fiscal sustainability. Growth prospects would be improved by increasing the legal system's effectiveness, for example by promoting alternative dispute resolution mechanisms. Bringing more women and young people into employment, for example by encouraging flexible working arrangements and increasing incentives to hire workers with limited experience, remains also key to bolster further improvements in potential output. Promoting broader property insurance for all buildings could limit the size of fiscal contingent liabilities arising from increasingly severe extreme weather events and help speed up rebuilding after damages.

# Hungary

Economic activity is projected to rise by 2.4% in 2024 and 2.7% in 2025, after a decline of 0.6% in 2023. Lower inflation, mainly driven by energy and food prices, is expected to support a gradual pick-up in investment and private consumption. The main risks around the outlook are related to the pace of the decline in core inflation and the outcome of negotiations with the EU regarding the delivery of EU funds.

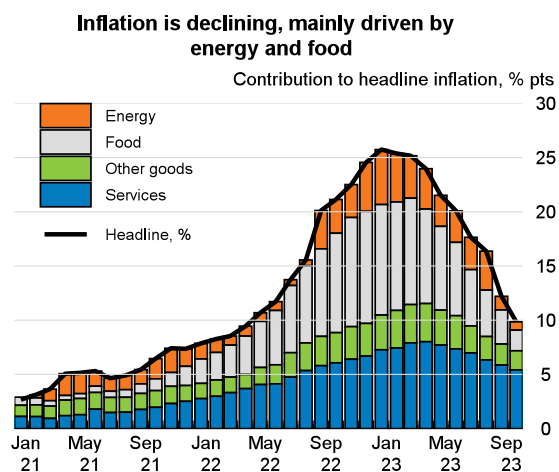
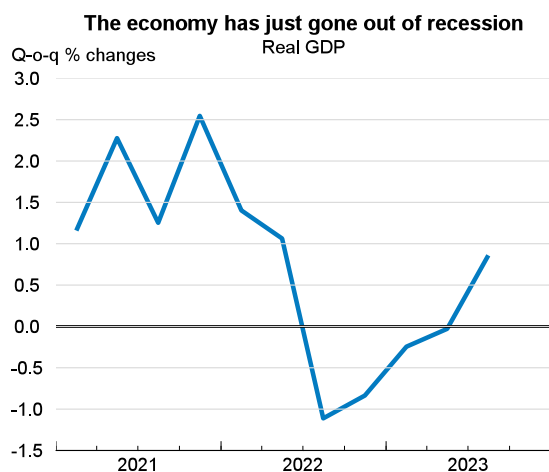
Reducing the budget deficit as planned will be key to rebuilding fiscal space in view of upcoming spending needs related to ageing and the green transition. Restructuring energy support by moving from price caps to targeted cash transfers to support vulnerable households would increase incentives for energy savings, reduce the exposure of public finances to fluctuations in global energy prices, and improve energy security. Productivity growth could be bolstered by strengthening competition in the transport, professional services and telecommunication sectors. This and a wider diffusion of digital skills would accelerate the digitalisation of firms.

## The economy has emerged from recession

After four consecutive quarters of GDP decline, economic growth restarted in the third quarter of 2023. While business confidence remains low, especially in the construction and retail sectors, consumer confidence is slowly improving and the labour market is holding up well, with only a marginal increase in unemployment from 3.5 to 3.9% since the start of the recession. Inflation declined from over 25% in January 2023 to 9.9% in October, mainly driven by declining energy and food prices.

Energy price caps delayed the impact of the 2022 energy price shock on inflation but resulted in a significant fiscal cost. These price caps were either limited or removed later on, thus pushing up energy prices until the second half of 2023. Food inflation has been declining rapidly this year, but services inflation is stickier. Inflation expectations are consistent with a return to the central bank's tolerance band of 2-4% by 2025.

## Hungary



Source: OECD national accounts database; OECD Consumer Prices database; and OECD calculations.

StatLink  <https://stat.link/g7csz4>



## Hungary: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>Hungary</b>	Current prices HUF billion	Percentage changes, volume (2015 prices)				
<b>GDP at market prices</b>	48 425.4	7.1	4.6	-0.6	2.4	2.7
Private consumption	23 968.3	4.6	6.5	-3.3	3.0	2.6
Government consumption	10 327.2	1.8	3.0	1.3	1.1	1.2
Gross fixed capital formation	12 841.3	5.8	0.1	-10.0	0.0	5.4
Final domestic demand	47 136.8	4.2	3.8	-4.2	1.8	3.1
Stockbuilding <sup>1</sup>	354.8	2.0	-0.1	-1.5	0.1	0.0
Total domestic demand	47 491.7	6.4	3.6	-5.0	1.9	3.2
Exports of goods and services	38 113.7	8.3	12.6	0.7	3.1	4.4
Imports of goods and services	37 180.0	7.3	11.6	-4.4	2.3	5.1
Net exports <sup>1</sup>	933.8	0.9	0.8	4.9	0.8	-0.3
<i>Memorandum items</i>						
GDP deflator	–	6.4	14.5	13.1	5.3	3.3
Consumer price index	–	5.1	14.6	17.5	4.6	3.3
Core inflation index <sup>2</sup>	–	4.5	10.2	13.7	4.8	3.3
Unemployment rate (% of labour force)	–	4.0	3.6	4.1	4.2	3.9
Household saving ratio, net (% of disposable income)	–	13.1	8.5	7.5	9.2	9.1
General government financial balance (% of GDP)	–	-7.2	-6.2	-5.2	-4.1	-3.4
General government gross debt (% of GDP)	–	88.7	77.4	73.1	74.1	75.0
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	76.7	73.9	70.0	71.3	72.1
Current account balance (% of GDP)	–	-4.2	-8.3	0.1	0.8	0.5

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 114 database.

StatLink  <https://stat.link/t26ub7>

## Monetary policy is tight and fiscal consolidation is underway

The central bank started to lower its effective policy rate in the spring of 2023, but monetary policy remains tight. Considering the uncertainty related to the evolution of core inflation and the exchange rate, and the need to firmly anchor inflation expectations, further monetary easing is expected to proceed in a gradual manner. Fiscal policy is being tightened substantially, with a projected deficit reduction of around 3 percentage points of GDP between 2022 and 2025 but public debt is expected to remain higher in 2025 than prior to the pandemic. The main consolidation measures in 2023 include the non-repetition of past gas reserve purchases and an increase in temporary windfall taxes. In 2024-25, the main measures include lower government consumption and investment. However, in cyclically-adjusted terms, the bulk of fiscal consolidation has taken place in 2023. The energy price support provided to households is expected to remain in place in 2024 and 2025.

## Economic growth is expected to rebound from 2024 onwards

Economic activity is projected to decline in 2023, mainly due to falling private consumption and investment in the first part of the year. Declining energy prices and economic activity are expected to lower inflationary pressures, which will support a gradual pick-up in household real incomes and private consumption. Public consumption and investment will provide less support to growth in 2024 and 2025, in line with the government's objective of reducing the fiscal deficit. Exports are expected to pick up in 2024-25 as growth in Hungary's main trading partners, including Germany, regains momentum. If core inflation proves more entrenched than expected, the central bank will need to keep rates higher for longer, affecting consumption and investment. A new surge in energy prices would have similar effects, while also straining public finances, given the utility price cap in place. Another risk is related to the delivery of EU funds. Failing to reach an agreement on the complete delivery of those funds may curb investor confidence, increase the cost of capital, and put renewed pressure on the exchange rate.

## Structural reforms are needed for stronger and more sustainable growth

Reducing the budget deficit as planned will be important to rebuild fiscal space in view of the upcoming increase in ageing-related costs (over 5 percentage points of GDP by 2070) and the financing of the green transition. Restructuring energy support by moving from price caps to targeted cash transfers to support vulnerable households would increase incentives for energy savings and improvements in the energy efficiency of dwellings, reduce the exposure of public finances to fluctuations in global energy prices, and lower Hungary's dependence on energy imports. Productivity growth could be bolstered by strengthening competition in the transport, professional services and telecommunication sectors. Lower telecommunication prices and a wider diffusion of digital skills would accelerate the digitalisation of firms and help Hungarian firms, especially SMEs, to bridge the digital gap with peer countries.

# Iceland

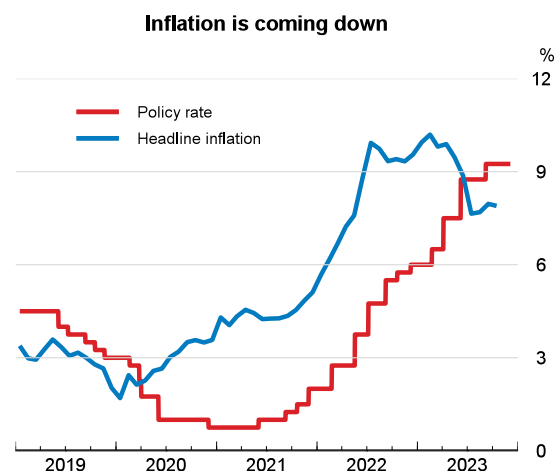
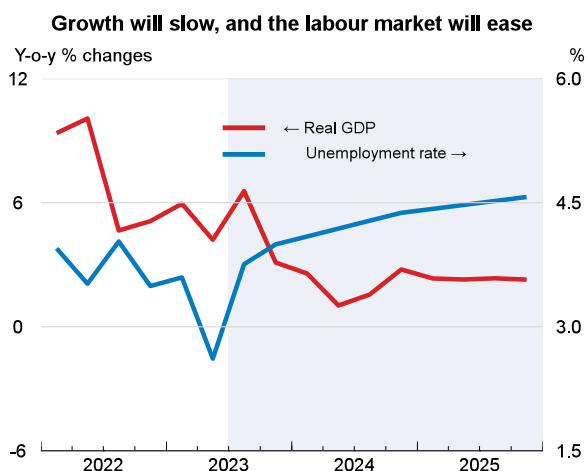
Economic growth will drop to 2.0% in 2024 and edge up to 2.3% in 2025. Private consumption will ease as real wage growth is modest. Business investment will moderate as financial conditions continue to deteriorate and confidence remains lacklustre. Despite tighter financial conditions, housing investment will pick up to satisfy pent-up demand. Public investment will decline in 2024 and remain subdued in 2025. Goods exports and foreign tourism will slow. The unemployment rate will rise gradually to around 4.5%.

In August, the central bank lifted the key policy rate to 9.25%. Consumer price inflation is declining but still at around 8%. It is expected to fall further but remain above target until well into 2025. Fiscal policy is already contractionary and is projected to be tightened further, as planned by the government, to help reduce inflationary pressures and maintain fiscal space. A new tourism strategy should help increase productivity of the tourism sector and reduce pressure on infrastructure and the environment.


## The economy is gradually slowing

The economy is weakening, although growth continues to benefit from strong foreign tourism. Activity in the seafood and aluminium sectors, Iceland's main goods exports, is easing as demand in major export markets has weakened. Household consumption is moderating as real wage growth is sluggish and dissaving has probably come to an end. Business investment is tailing off as financial conditions are worsening, although business sentiment has improved since the early summer. Public investment is declining. The labour market remains tight, with the unemployment rate at around 3.5%, and the labour force is expanding following continued immigration. With seismic movements on the Reykjanes peninsula ongoing, several thousand inhabitants have been evacuated and activity in the area concerned has largely stopped.

## Iceland



Source: OECD Economic Outlook 114 database; Central Bank of Iceland; and OECD Consumer Prices database.

StatLink  <https://stat.link/ohqvie>

## Iceland: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>Iceland</b>	Current prices ISK billion	Percentage changes, volume (2015 prices)				
<b>GDP at market prices</b>	2 920.5	4.5	7.2	4.9	2.0	2.3
Private consumption	1 518.0	7.1	8.5	2.2	2.0	2.0
Government consumption	822.2	2.3	2.2	1.4	1.4	1.5
Gross fixed capital formation	621.5	10.8	7.6	-1.2	4.2	2.8
Final domestic demand	2 961.8	6.5	6.6	1.3	2.3	2.1
Stockbuilding <sup>1</sup>	3.2	-0.1	-0.1	0.0	0.0	0.0
Total domestic demand	2 964.9	6.4	6.5	1.4	2.4	2.1
Exports of goods and services	971.0	14.6	22.3	6.0	2.7	3.0
Imports of goods and services	1 015.4	19.9	19.9	-1.9	3.6	2.4
Net exports <sup>1</sup>	- 44.4	-2.1	0.5	3.7	-0.3	0.3
<i>Memorandum items</i>						
GDP deflator	—	6.5	8.9	6.6	3.5	3.1
Consumer price index	—	4.4	8.3	8.6	4.2	2.9
Core inflation index <sup>2</sup>	—	4.4	7.8	8.3	4.0	2.9
Unemployment rate (% of labour force)	—	6.0	3.7	3.5	4.2	4.5
General government financial balance (% of GDP)	—	-8.5	-4.0	-1.7	-1.2	-0.1
General government gross debt <sup>3</sup> (% of GDP)	—	77.3	78.1	77.4	77.4	76.3
Current account balance (% of GDP)	—	-3.3	-2.3	1.6	1.3	1.6

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 114 database.

StatLink  <https://stat.link/4eifq>

## Monetary and fiscal policies continue to be tightened

In August, the central bank raised the key interest rate by 50 basis points to 9.25%, the 14<sup>th</sup> increase since the tightening cycle started in May 2021, and kept it unchanged in November. Headline consumer price inflation fell from a peak of around 10% in February 2023 to around 8% as import and house prices declined, but it remains above the target of 2.5%. Underlying inflation has become more broad-based. The króna has depreciated since late summer. Fiscal policy was contractionary in 2023 and will be tightened further by around 1.0% of GDP per year following planned tax reforms and cuts in discretionary spending. The overall budget is projected to be close to balance in 2025. This is welcome to help reduce inflationary pressures and to build up fiscal space. The public debt-to-GDP ratio according to the national accounts is projected to decline slightly.

## The economy will slow

Economic growth is expected to drop to 2.0% in 2024 and to rebound to 2.3% in 2025. Consumption will remain muted as real wage growth remains weak. Goods exports will tail off as demand in the destination countries loses momentum. Foreign tourism will slow as domestic capacity limits become more apparent and economic growth remains subdued in major origin countries. Tighter financial conditions will weigh on business investment. Despite higher real interest rates, housing investment will recover in 2024 and 2025 as pent-up demand is worked off. The unemployment rate will edge up towards 4.5%. Inflation will fall in the wake of macroeconomic policy tightening but is projected to remain above target until late in 2025. It could remain higher than expected if wages rise faster than agreed in the past wage agreements or if import prices, notably for oil, start rising again. The impending volcanic eruption on the Reykjanes

peninsula could wreck a geothermal power plant and the “Blue Lagoon” resort. The tourism sector could also suffer from a stronger-than-expected slowdown in foreign tourists’ origin countries. A sharp fall in house prices could expose financial vulnerabilities.

### **A tourist tax could generate revenue and help safeguard natural resources**

Iceland hosts more tourists per inhabitant than any other OECD country. Foreign tourism provides welcome employment and revenue, but it also exerts pressure on infrastructure and the environment, which has become a major structural policy challenge. A balanced tourism strategy could help improve productivity of tourism services; capitalise on the natural assets that form the basis of Iceland’s tourism sector; limit pressures on infrastructure and the environment; and aim for a geographically more even development across the country. Iceland should introduce a tourist tax to generate additional tax revenue, to help safeguard natural resources and to finance and manage public infrastructure.

# India

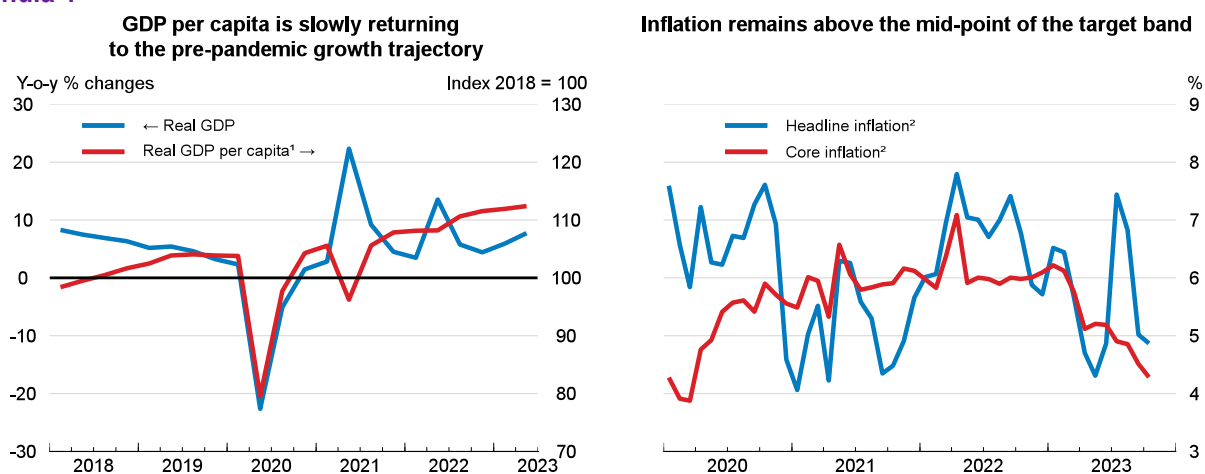
Following a strong outcome in FY 2022-23, real GDP growth is projected to slow to 6.3% in FY 2023-24 and 6.1% in FY 2024-25 on account of adverse weather-related events and the weakening international outlook. Surging services exports and public investment will continue to drive the economy. Inflation will decline progressively, with corresponding improvements of purchasing power. This, along with the end of the El Niño weather pattern, productivity gains from recent policy reforms, and improved global conditions, will help economic activity to strengthen, with projected real GDP growth of 6.5% in FY 2025-26.

Monetary policy easing is assumed to start in the second half of 2024, supporting business investment and discretionary household spending. Government investment will remain at high levels. Nevertheless, further fiscal consolidation is expected, which will increase financial space for the private sector. The challenges that remain to eradicate poverty, mitigate climate change, and accelerate income convergence require substantial fiscal efforts to mobilise additional resources and strengthen regulations, institutions, and standards to steer consumers towards inclusive and sustainable practices.

## Domestic demand is sustaining economic activity

FY 2023-24 started with strong growth driven by public investment and private consumption. However, the global economic slowdown has hit merchandise trade. There are differences along sectoral and territorial lines: services (finance and export-oriented segments in particular) are more buoyant than manufacturing and urban areas are performing better than rural ones. Recent economic statistics are sending mixed signals. According to the income-based national accounts, real GDP grew by 7.8% year-on-year in the April-June quarter, whereas it grew considerably less in the expenditure-based account. Similarly, recent market data for consumption suggest that car sales and air traffic are doing well, but commercial vehicles and tractor sales, as well as passenger rail and cargo aviation traffic are either retrenching or growing slowly. The RBI and PMI industrial surveys indicate that firms see business prospects improving, but other forward-looking surveys are less upbeat concerning demand conditions. Tighter financial market conditions and some softening in commodity prices, which reduces the overall demand for working capital loans, are moderating banking credit growth.

### India 1



1. Real GDP per capita is based on GDP in constant prices (2015 PPP), USD. Quarterly population data are calculated by interpolating annual data. OECD estimates on population data for 2023.

2. OECD seasonal adjustment based on monthly consumer price index and core CPI (index 2012 = 100) from the Ministry of Statistics and Programme Implementation (MOSPI).

Source: OECD Economic Outlook 114 database; OECD Population database; and CEIC.

StatLink  <https://stat.link/4bdoyi>

## India: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>India</b>	Current prices INR trillion	Percentage changes, volume (2011/2012 prices)				
<b>GDP at market prices</b>	198.3	9.1	7.2	6.3	6.1	6.5
Private consumption	121.5	11.2	7.5	4.6	6.9	7.2
Government consumption	23.0	6.6	0.1	3.3	5.2	3.7
Gross fixed capital formation	54.0	14.6	11.4	5.5	5.5	6.3
Final domestic demand	198.6	11.5	7.8	4.7	6.3	6.6
Stockbuilding <sup>1,2</sup>	0.5	0.8	0.0	0.0	0.0	0.0
Total domestic demand	199.1	8.0	8.1	9.7	6.2	6.5
Exports of goods and services	37.1	29.3	13.6	-3.3	7.0	6.4
Imports of goods and services	37.9	21.8	17.1	11.3	7.4	6.6
Net exports <sup>1</sup>	-0.8	0.9	-1.0	-3.7	-0.5	-0.4
<i>Memorandum items</i>						
GDP deflator	–	8.5	8.2	1.6	4.7	5.0
Consumer price index	–	5.5	6.7	6.1	5.3	4.2
Wholesale price index <sup>3</sup>	–	13.0	9.4	0.2	4.3	3.6
General government financial balance <sup>4</sup> (% of GDP)	–	-10.4	-8.9	-8.4	-7.5	-7.0
Current account balance (% of GDP)	–	-1.2	-2.0	-2.2	-2.4	-2.2

Note: Data refer to fiscal years starting in April.

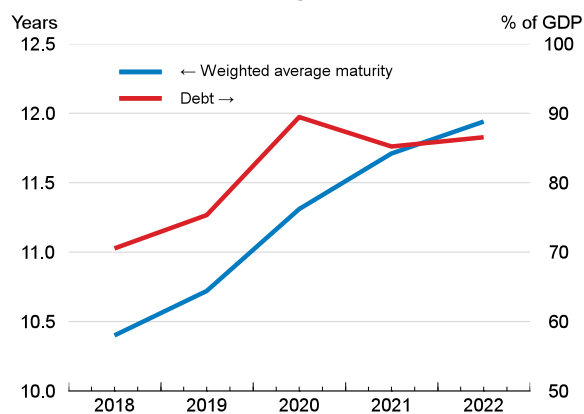
- Contributions to changes in real GDP, actual amount in the first column.
- Actual amount in first column includes statistical discrepancies and valuables.
- WPI, all commodities index.
- Gross fiscal balance for central and state governments.

Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/5oj4zs>

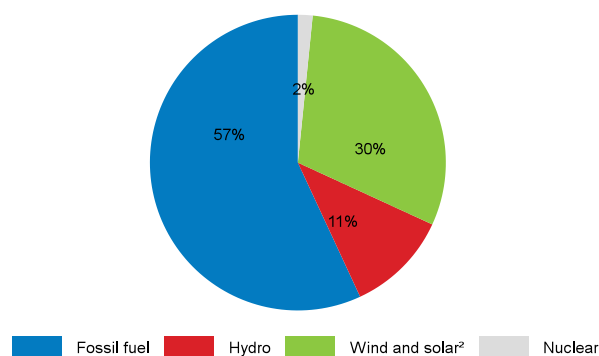
## India 2

### Public debt has risen but the maturity profile has lengthened<sup>1</sup>



### More than 40% of generation capacity is non-fossil fuel

% of installed generation capacity, May 2023



1. Years represent fiscal years. The debt ratio refers to the sum of domestic and external debt of central and state governments in per cent of GDP. The weighted average maturity is based on the issuance of Government of India dated securities.

2. Including other renewables.

Source: Reserve Bank of India; and Ministry of Power.

StatLink  <https://stat.link/rzp51j>

Domestic growth prospects are strongly influenced by global developments, even if India has a relatively low trade-to-GDP ratio. Over a decade, India's global export market share has increased, mostly due to services. The current account deficit narrowed in the first half of the calendar year 2023 and the merchandise trade deficit was 12% smaller in value terms in April-October 2023 than in the corresponding period in 2022. India has seized the opportunity to buy heavily discounted Urals oil. Russia's share in crude oil imports has increased from less than 5% to over one-third.

### Monetary policy is tightening, fiscal consolidation remains a priority

Monetary policy tightening is successfully managing inflationary pressures but is also weighing on household consumption and corporate investment. Headline inflation moderated in the first half of 2023, and dropped below the upper threshold of the central bank's 2-6% target range in September. Food and energy prices remain sensitive to weather conditions and geopolitical tensions. The government has taken additional emergency measures to rein in soaring prices of food staples, including allowing imports of tomatoes from Nepal, selling tomatoes at subsidised prices, and releasing onions from buffer stocks. Banks' financial results and solvency ratios have improved, helped by more effective regulation and supervision, and increasing the room for manoeuvre for monetary policy. Additional efforts may be needed to speed up activation of recent insolvency reforms and facilitate the exit of non-viable firms. Labour force participation, employment and wage estimates suggest improving labour market conditions, including for women and in rural areas, but given the still large reserves of labourers in rural areas, the risk of a wage-price spiral is minimal.

Fiscal consolidation remains a top policy priority given the need to maintain public debt at sustainable levels. As a share of GDP, public debt has grown by 15 percentage points since FY 2018-19 though the average maturity of the debt has lengthened. Given reasonable assumptions about inflation and interest rates, halting the increase in the debt-to-GDP ratio requires either above-potential GDP growth, or a considerably lower deficit than recently attained. Over the next two years the government targets are projected to be achieved, but greater efforts to control expenses are needed at the state level, along with policy interventions to narrow the tax gap. This requires broadening the tax base for corporate and personal income taxes, simplifying the goods and services tax (GST) rate structure, and closing exemptions and loopholes. Efficiency gains can also be achieved by partial or complete divestiture of state-owned enterprises.

### The economy will be resilient despite global tensions

Real GDP growth is expected to slow to 6.3% in FY 2023-24 and 6.1% in FY 2024-25, before rebounding gently in FY 2025-26. With slower growth, inflation expectations, housing prices and wages will all progressively moderate, helping headline inflation converge towards 4.2%. This will allow the RBI to start lowering interest rates from mid-2024 to 5.5% by the end of 2025. The trade restrictions imposed in 2022 to fight inflation (including export bans on various rice varieties) will be withdrawn, helping export growth to recover. The current account deficit will remain within manageable levels.

Risks are tilted to the downside. While indicators suggest that India's growth is stable for now, there are strong headwinds from heightened global uncertainty. In addition, the lagged impact of domestic policy tightening will continue to be felt, coupled with the disappointing dynamics of some socio-economic indicators, such as consumer goods' sales, in rural areas. A below-normal monsoon season could also impact growth negatively. An additional risk is the acceleration of portfolio capital outflows, with consequences for the exchange rate, inflation, and monetary policy.



## Fiscal policy can help accelerate the transition to net-zero emissions

The fight against environmental degradation and climate change requires huge investments and behavioural changes. Stronger revenue mobilisation and further improvement in public expenditure efficiency can free resources for investment in cleaner and energy-efficient infrastructure. In order to encourage renewable energy, targeted subsidies could be increased. Taxes on emissions would discourage dirty energy, with the added benefit of diminishing the reliance on imported fuels. On top of fiscal interventions, public campaigns to encourage the adoption of sustainable lifestyles have proven their effectiveness. The impact on energy consumption, costs and emissions of measures proposed by the government's Lifestyle for Environment (LiFE) initiative is potentially substantial and could build on India's success in achieving its target of producing 40% of electric capacity from non-fossil-fuel sources. Investing in green skills and capabilities, facilitating the international transfer of green technologies, and strengthening regulations, institutions, and standards would mitigate climate change and support growth.

# Indonesia

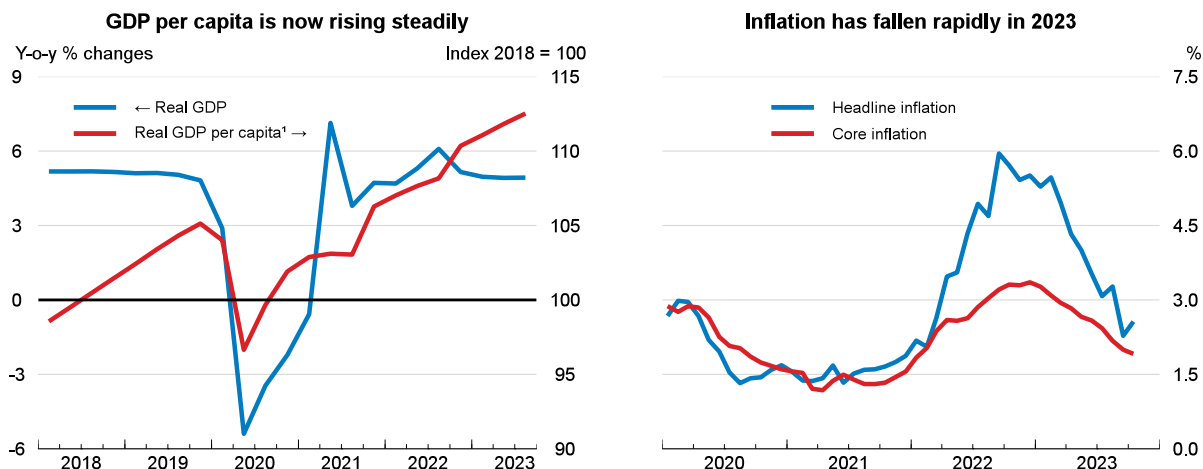
Economic activity continues at a brisk pace, with real GDP growth of 4.9% in 2023 and 5.2% in 2024 and 2025. Household consumption, despite modest real wage gains, will remain the major engine of the economy. Monetary tightening and slowing global trade will weigh on fixed capital formation, but housing construction activity is expected to increase, notably in the new capital city Nusantara. Two years of monetary tightening have pushed down inflation, which is projected to be around 2.5% in 2024 and 2025.

With inflation expectations re-anchored, Bank Indonesia is expected to start easing in mid-2024. The prudent stance of fiscal policy should strengthen Indonesia's credit image and encourage long-term capital inflows, contributing to the stabilisation of the exchange rate. After the February 2024 elections, the incoming administration should focus on promoting pro-growth fiscal policy and institutions, in particular through reducing state-owned enterprises' wide-ranging market privileges, enhancing domestic revenue mobilisation, and making social spending more targeted and effective.

## Economic growth is back to its robust pre-pandemic pace


Real GDP growth in 2023 is close to the approximately 5% average annual rate achieved since 2000. Various indicators suggest improving demand conditions. The manufacturing sector continued to expand at the end of the third quarter at a solid, albeit softer, rate and the hotel occupancy rate in January-July surpassed pre-pandemic levels. However, cement purchases and imports of machinery and equipment, two key indicators of fixed investment, are now lower than a year earlier and demand for new banking finance remains muted. Headline inflation is affected by the strong increase in rice prices, but fell in October to 2.6%. The number of unemployed persons has fallen below 8 million and the jobless rate stands below 6%. There are also positive signs for financial investment over the longer term: the Jakarta Stock Exchange recorded the world's fourth-highest number of new listings in the January-October period, cross-border private equity deals increased as global institutions look for alternatives to China, and Indonesia was the first sovereign borrower to issue samurai blue bonds in Japan (with proceeds earmarked for sustainable activities in the marine sector).

## Indonesia 1



1. Real GDP per capita is based on GDP in constant prices (2015 PPP), USD. Quarterly population data are calculated by interpolating annual data. OECD estimates on population data for 2023.

Source: OECD Economic Outlook 114 database; OECD Population database; and CEIC.

StatLink  <https://stat.link/et5w0z>

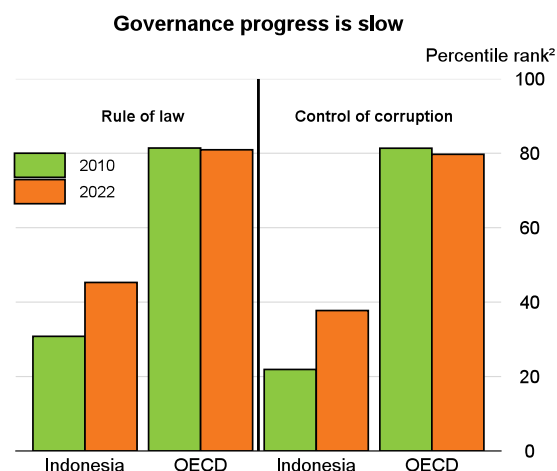
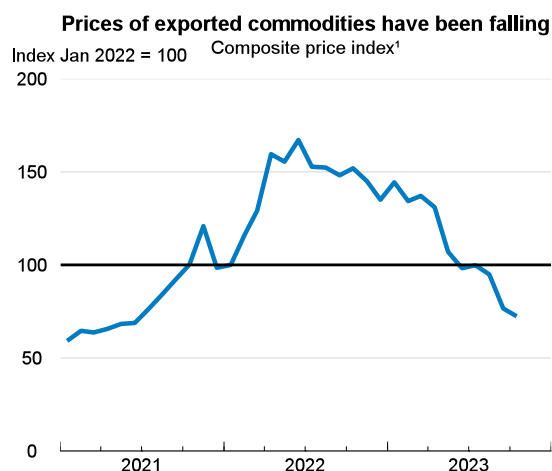
## Indonesia: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>Indonesia</b>	Current prices IDR trillion	Percentage changes, volume (2010 prices)				
<b>GDP at market prices</b>	15 443.4	3.7	5.3	4.9	5.2	5.2
Private consumption	9 101.4	2.0	4.9	4.8	5.1	5.3
Government consumption	1 491.2	4.2	-4.5	3.6	3.4	4.1
Gross fixed capital formation	4 897.0	3.8	3.9	5.0	5.9	5.1
Final domestic demand	15 489.6	2.8	3.8	4.8	5.2	5.1
Stockbuilding <sup>1</sup>	- 307.3	1.5	1.0	-0.1	0.1	0.0
Total domestic demand	15 182.3	4.3	4.6	4.5	5.1	5.0
Exports of goods and services	2 676.5	18.0	16.3	1.0	4.1	5.4
Imports of goods and services	2 415.5	24.9	14.7	-1.6	3.6	4.5
Net exports <sup>1</sup>	261.0	-0.4	0.8	0.6	0.3	0.4
<i>Memorandum items</i>						
GDP deflator	—	6.0	9.6	2.1	1.5	1.9
Consumer price index	—	1.6	4.2	3.6	2.4	2.4
Private consumption deflator	—	1.7	4.8	4.0	1.5	2.7
General government financial balance (% of GDP)	—	-4.8	-3.4	-2.5	-2.4	-2.3
Current account balance (% of GDP)	—	0.3	1.0	0.6	1.0	0.7

1. Contributions to changes in real GDP, actual amount in the first column.  
Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/kvytj4>


## Indonesia 2



1. The price indices for individual commodities (palm oil, coal, iron ore, gold and nickel) are aggregated by using weights based on the share of each commodity in total 2021 exports of these commodities.

2. Percentile rank indicates the country's rank among all countries covered by each indicator, ranging from 0 (worst) to 100 (best).

Source: Ministry of Energy and Mineral Resources of Indonesia; CEIC; World Bank Commodity Markets Outlook; and Worldwide Governance Indicators.

StatLink  <https://stat.link/sgn4bd>

The volatile global landscape, and in particular Russia's war of aggression against Ukraine, has mixed implications for Indonesia. While direct trade with both Russia and Ukraine was limited prior to the war, as were the numbers of visitors from these countries, imports of discounted Urals oil have helped to contain price inflation. Indonesia was negatively affected by high grain and fertiliser prices, but exports have benefited from global price increases for various non-grain crops such as rice, as well as minerals and metals. The terms of trade have improved significantly this year, and net trade has supported growth in 2023, despite export restriction measures on palm oil. Total trade with China in the first semester grew slightly (0.6%) compared with the same period in 2022, whereas it shrunk by 4.7% for ASEAN as a whole.

### The policy mix will aim at stability

Close co-ordination between fiscal and monetary policies has supported economic growth and resilience. The effect of Bank Indonesia's previous six-step increase of the policy rate is increasingly visible, with inflation now within the target range (currently 3.0% consumer price inflation with a  $\pm 1\%$  corridor). However, the weakening of the Rupiah amid increasing global uncertainty prompted the central bank to raise the policy rate again in October. Under current commodities markets assumptions, and provided that global tensions do not escalate, Bank Indonesia is likely to make the first rate cut around mid-2024. Given that the revised inflation target for 2024 is slightly more ambitious (2.5% with a  $\pm 1\%$  corridor), the switch to a more accommodative monetary policy is likely to be cautious and gradual.

Following a widening of the budget deficit during the pandemic, the authorities have intensified fiscal consolidation since 2022. The 2024 budget targets a deficit of 2.3% of GDP and a neutral fiscal stance will be maintained going forward. Tax policy and administration reforms, as well as the completion of some projects, should help to achieve this goal. While extreme poverty has been largely eradicated, the pandemic showed that the emerging middle class remains vulnerable to shocks and in need of safety nets. The prolonged closure of schools aggravated disparities in access to education and training. The expansion of social protection programmes, in terms of both benefits and coverage, should be accompanied by improvements in their automaticity and targeting. If external risks materialise, any sizeable or long economic slowdown should be addressed through additional discretionary spending, given weak automatic stabilisers. A further gradual increase in capital spending is expected over the medium term, including to speed up investments in Nusantara. These are estimated to be around USD 30 billion over the next decade.

### Growth prospects remain favourable

Indonesia is projected to maintain rapid and stable growth over the projection period. Better labour market conditions, lower inflation and improvements in investors' sentiment will support consumption and investment, offsetting the gloomier global trade picture. Tourism arrivals and average expenditures will also continue recovering.

Despite progress in diversifying export products and markets, in particular through preferential trade agreements with other fast-growing partners, and in developing domestic capital markets, Indonesia remains vulnerable to external risks. These include geopolitical tensions in other regions, unexpected global financial market gyrations, and non-tariff barriers on exports arising from partners' regulations on deforestation and carbon border adjustment levies. On the other hand, political risk is limited as the February 2024 elections are unlikely to result in a modification of the overall economic policy stance.

## Despite major advances in the past 25 years, challenges remain

In the past 25 years under democratic rule, public sector governance and infrastructure have experienced significant improvements, while the macroeconomic policy framework has gained credibility. Considerable resources are being provided to improve infrastructure, with some success. Despite cost overrun and delays, the Jakarta-Bandung railway was inaugurated in September. Indonesia has thus become the fourth non-OECD country with a high-speed train service. In the medium run, however, an average annual growth rate of 5% may be insufficient to turn Indonesia into a high-income economy by 2045, which is the overarching goal of the Indonesian authorities. To achieve this vision, a comprehensive new plan of structural reforms should remove distortions in policy areas such as business regulation, finance, state ownership, and competition and reduce the enduring gap in transparency and regulatory clarity relative to OECD economies. The authorities have shown a strong commitment to fiscal discipline and should now adopt a concrete medium-term fiscal strategy, to reap the demographic dividend before ageing starts to become an issue in less than a decade. Revenue mobilisation would benefit from deepening the 2021 tax reform, notably by improving compliance by high-income taxpayers. The energy subsidy reform should include the return of the semi-automatic pricing formula which was applied in 2015-18, based on an international oil price index, exchange rate and other tax and distribution costs. Further work is needed on regulatory implementation, including through greater independence of oversight institutions, such as the Corruption Eradication Commission.

# Ireland

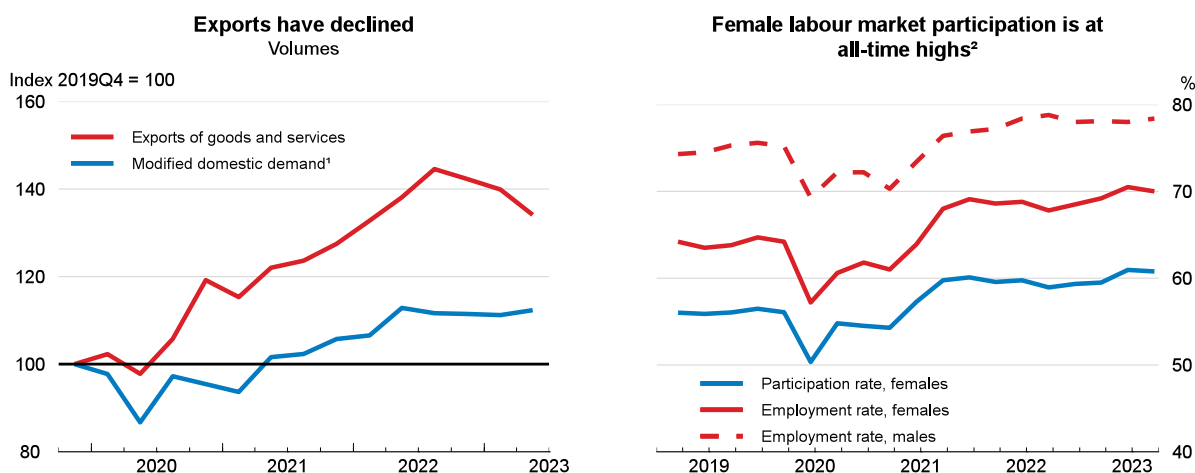
GDP is set to contract by 0.6% in 2023, as heightened global uncertainties, a weaker outlook in main trading partners and high interest rates weigh on exports and investment. With price pressures subsiding, GDP growth is projected to pick up to 2.4% in 2024 and 2.9% in 2025. Modified domestic demand growth, which removes some distortions due to the high share of multinationals, will decline to 2.1% in 2023, before slowing further to 1.7% in 2024 and returning to 2.1% in 2025.

Although tax receipts are set to remain strong, ensuring long-term fiscal sustainability is needed to meet the investment-intensive ageing, housing and climate challenges. The announced move to allocate windfall corporate tax revenues to two new financial vehicles – a long-term savings fund and an investment fund – is thus welcome. Stricter adherence to the 5% spending rule will also be essential. Structural reforms to enhance SMEs' financing would boost innovation and technology diffusion. Planning regulations should be eased to foster investment in housing and renewable electricity generation.

## Falling exports have weakened growth momentum

Household consumption continued to underpin activity in the first half of 2023, on the back of strong employment growth and lower saving rates. However, increased borrowing costs and still relatively high energy and input prices have weighed heavily on business and housing investment. On the external side, the slowdown in global demand triggered marked reductions in export volumes, adding to the post-pandemic contraction in exports of pharmaceutical and medical products. As a result, GDP contracted in the third quarter of 2023.

## Ireland



1. Excludes large transactions of foreign corporations that do not have a big impact on the domestic economy.

2. The participation rate refers to the number of persons in the labour force aged 15 years and over as a percentage of the working-age population. The employment rate refers to the number of persons aged between 15 and 64 in employment as a share of working age population.

Source: OECD, National Accounts database; and Central Statistics Office.

StatLink  <https://stat.link/shv2w1>

## Ireland: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2021 prices)				
<b>Ireland</b>						
<b>GDP at market prices</b>	375.3	14.8	9.5	-0.6	2.4	2.9
Private consumption	94.1	8.3	9.6	3.6	2.3	2.7
Government consumption	48.1	6.5	4.5	1.6	1.3	0.8
Gross fixed capital formation	157.8	-39.8	5.4	-8.8	2.0	2.6
Final domestic demand	300.0	-17.3	7.9	-1.3	2.0	2.3
Stockbuilding <sup>1</sup>	4.2	0.4	1.0	1.9	0.6	0.0
Total domestic demand	304.2	-17.1	8.1	1.2	2.8	2.1
Exports of goods and services	496.8	14.9	14.2	-2.6	1.5	3.7
Imports of goods and services	425.8	-7.2	16.2	-0.2	2.0	3.4
Net exports <sup>1</sup>	71.0	27.9	3.8	-3.3	0.1	1.5
<i>Memorandum items</i>						
Modified final domestic demand <sup>2</sup> , volume	–	6.9	9.7	2.1	1.7	2.1
GDP deflator	–	0.6	6.6	3.6	2.3	2.5
Harmonised index of consumer prices	–	2.4	8.1	5.3	3.1	2.6
Harmonised index of core inflation <sup>3</sup>	–	1.7	4.6	4.6	3.4	2.6
Unemployment rate (% of labour force)	–	6.2	4.5	4.4	4.7	4.6
Household saving ratio, net (% of disposable income)	–	15.7	7.7	5.2	5.4	5.7
General government financial balance <sup>4</sup> (% of GDP)	–	-1.5	1.7	1.3	1.0	1.2
General government gross debt (% of GDP)	–	64.5	46.4	44.4	42.4	40.0
General government debt, Maastricht definition <sup>5</sup> (% of GDP)	–	54.5	44.4	42.4	40.4	38.0
Current account balance (% of GDP)	–	13.7	10.8	9.8	9.4	10.3

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 114 database.

StatLink  <https://stat.link/hf6c4w>

Preliminary estimates suggest harmonised headline inflation slowed to 3.6% in October, driven by weaker energy prices, with electricity providers starting to pass lower generation costs onto consumers. Food price inflation slowed mildly, while high prices of services continued to feed into harmonised core inflation, which went up to 4.3%. To preserve the real income of vulnerable households, the government has announced its fourth cost-of-living package (0.5% of 2022 GDP; 1.0% of GNI\*, i.e., gross national income excluding the distortions from multinationals), which, on top of targeted lump-sum payments to recipients of specific welfare schemes, however, also includes untargeted electricity credits and one-off top-ups to child benefits.

## The 5% spending rule will continue to be breached in 2024

Despite some recent easing in corporate tax receipts, total tax revenues are set to remain resilient and help attain a fiscal surplus of 1.3% of GDP in 2023 (2.3% of GNI\*). The fiscal stance is expected to be broadly neutral in the next two years. The government's 2024 budgetary package (2.8% of 2022 GDP; 5.0% of GNI\*) mainly comprises spending measures, but there are also some tax changes, including personal income tax cuts, the extension of reduced energy VAT rates to end-October 2024, and the establishment of a one-year mortgage interest relief scheme. Higher permanent spending on welfare payments, public services, and infrastructure will reduce inequality and enhance productivity growth but also result in a breach of the 5% spending rule in 2024. Moreover, significant reliance on untargeted –

though temporary – income support measures may accentuate inflationary pressures. The fiscal impact of the new 15% statutory corporate rate, from early 2024, will be limited, with the budget surplus expected to be 1.0% of GDP (1.8% of GNI\*) in 2024 and increase marginally in 2025, as public expenditure growth eases somewhat. Public debt is projected to fall close to 38% of GDP by 2025 (below 70% of GNI\*).

### **Exposure to global risks is substantial**

Private consumption is set to remain supportive over the projection period, as widespread skill shortages will sustain wage growth, despite some easing in labour market conditions. Stronger real income gains, led by easing inflation and supply chain rebalancing, will then pave the way for a pick-up from mid-2024. Higher interest rates will weigh on business investment, especially among SMEs. Further escalation of geopolitical tensions and heightened global uncertainty could lower exports and government revenues. On the upside, faster disinflation would boost business investment, and stronger-than-expected growth in the United States would increase exports.

### **Fiscal caution and structural reforms are key to long-term welfare gains**

Meeting the government's investment-intensive reform agenda, which includes measures to aid the climate and digital transitions, as well as to support the provision of affordable quality housing and health services for a rapidly ageing population, will hinge on ensuring long-term fiscal sustainability and effective structural reforms. Long-term fiscal pressures will be sizeable, as age-related expenditures – on health, long-term care and pensions, for example, are estimated to increase by 8% of GNI\* between 2019 and 2050. Hence, the decision to allocate windfall tax gains into a soon to be established long-term savings fund, as well as into a smaller investment fund aimed at – countercyclically – supporting capital spending on infrastructure and climate-related projects, is welcome. In this perspective, adherence to the 5% spending rule remains essential. Any additional public support to income to mitigate persistent inflationary pressures or renewed energy price shocks should be more effectively targeted to vulnerable low-income households, be temporary, and preserve price signals. Productivity-enhancing policies should prioritise the reform of planning regulations to support housing supply and investment in renewable generation, and measures to expand childcare capacity and flexible work arrangements to further strengthen female employment growth.



# Israel

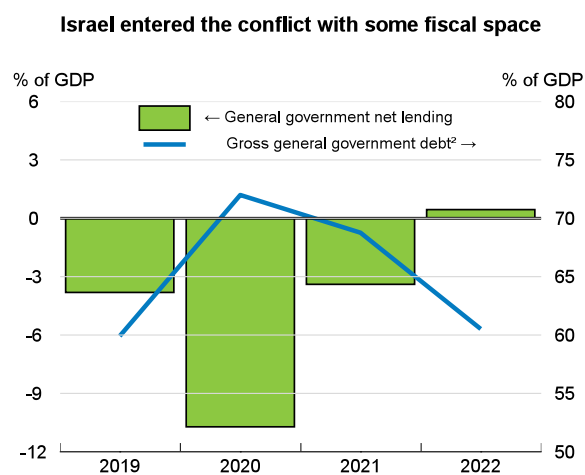
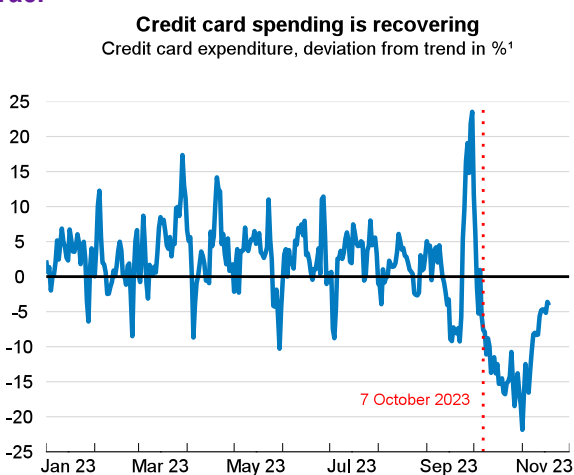
The economic impact of the evolving conflict following Hamas' terrorist attacks on Israel on 7 October is highly uncertain and depends on the duration, scope and intensity of the conflict. The projections assume that the impact will be largely concentrated in the last quarter of 2023, leading to a temporary but pronounced slowdown. GDP growth is projected at 2.3% in 2023 and 1.5% in 2024 before recovering to 4.5% in 2025. Supply side disruptions due to the security situation and the significant decline in the civilian labour force, together with weakening economic sentiment, will mainly affect private consumption and investment. A drop in tourism will weigh on export growth.

Monetary policy accommodation in the near-term will depend on uncertain exchange rate and inflation developments. Fiscal space built up after the pandemic can help provide temporary support to households and firms affected by the war and meet spending needs for defence, security and reconstruction. This should be accompanied by reprioritising permanent expenditure, while safeguarding growth-enhancing spending on infrastructure and skills provision. In the medium term, labour market and educational reforms are needed to address demographic challenges and reduce wide labour market disparities.

## The war is having a significant impact on the economy

The economy was performing robustly before the war. GDP grew by about 3% in the first three quarters of 2023 (average annualised quarterly rate) and the labour market was close to full-employment. Following the terrorist attacks on 7 October, the shekel initially depreciated markedly but recovered to pre-war levels in nominal effective terms by mid-November. The stock market was still around 6% below its pre-war level in mid-November and risk premia are elevated. Consumer and business confidence plummeted in October. Labour shortages in the economy are severe due to the call of reservists into service, evacuation of the population close to the border with Gaza and Lebanon, absences of parents from the workplace due to the closure of the educational system, lack of Palestinian workers and exit of many foreign workers from Israel. Moreover, the number of furloughed workers, for instance due to temporary business closures, increased markedly and vacancies dropped sharply in October. Parts of the educational system and retail shops, bars and restaurants have gradually reopened in November. Credit card data suggests a partial recovery of spending in November. Consumer price inflation, at 3.7% in October, remains above the central bank's 1-3% target range.

## Israel



1. The trend is based on data from January 2016 to September 2023. Underlying data is seasonally adjusted (7-day moving average), index January 2020=1.

2. Data for 2022 is an OECD estimate.

Source: Bank of Israel; OECD Economic Outlook 114 database; and OECD calculations.

StatLink  <https://stat.link/lo3mjc>

## Israel: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices NIS billion	Percentage changes, volume (2015 prices)				
<b>Israel</b>						
<b>GDP at market prices</b>	1 417.3	9.3	6.4	2.3	1.5	4.5
Private consumption	686.7	11.4	7.5	-0.4	1.6	5.1
Government consumption	330.5	5.2	0.0	3.3	6.2	3.0
Gross fixed capital formation	317.8	13.5	10.4	4.6	-2.3	5.4
Final domestic demand	1 334.9	10.4	6.5	1.7	1.6	4.7
Stockbuilding <sup>1</sup>	24.5	0.5	0.9	-0.7	-0.2	0.0
Total domestic demand	1 359.5	10.7	7.3	0.9	1.4	4.6
Exports of goods and services	391.4	14.8	8.5	0.5	3.1	3.3
Imports of goods and services	333.6	21.2	12.1	-4.5	1.9	3.6
Net exports <sup>1</sup>	57.9	-0.9	-0.6	1.4	0.4	0.0
<i>Memorandum items</i>						
GDP deflator	–	2.1	4.8	3.6	2.4	1.8
Consumer price index	–	1.5	4.4	4.3	2.7	1.9
Core inflation index <sup>2</sup>	–	1.3	4.0	4.3	2.7	1.9
Unemployment rate (% of labour force)	–	5.0	3.8	3.6	4.4	4.3
General government financial balance (% of GDP)	–	-3.4	0.4	-3.1	-5.2	-4.6
General government gross debt (% of GDP)	–	68.8	60.5	61.4	64.5	65.4
Current account balance (% of GDP)	–	3.9	3.8	4.2	4.3	4.0

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 114 database.

StatLink  <https://stat.link/5j67qr>

## The authorities are responding to ensure economic stability

On 9 October, the Bank of Israel announced a programme to sell up to USD 30 billion in foreign exchange (about 15% of total foreign exchange reserves or 6% of GDP) and provide swap facilities of up to USD 15 billion in order to moderate exchange rate volatility and to provide the necessary liquidity for the continued proper functioning of financial markets. A credit facility for SMEs via banks was established in early November. By the end of October, the central bank had sold USD 8.2 billion of foreign exchange. On 23 October, the central bank left the policy rate unchanged at 4.75%. In early November, parliament approved a NIS 15 billion (0.8% of GDP) business support package, including grants for firms near the borders with Gaza and Lebanon, and firms in the rest of the country based on their revenue losses. Other support measures include support to households who were evacuated, easier access to unemployment benefits, as well as business liquidity measures including the postponement of VAT payments and loan guarantees. Part of the substantially higher spending on the military and security, reconstruction and support to households and firms affected by the war will be financed by cuts to other spending, extra-budgetary funds and US defence aid. Nevertheless, the projections assume a marked fiscal expansion of around 4% of GDP over 2023-25. Public debt is set to increase to slightly above 65% of GDP in 2025.

## Economic growth is projected to slow markedly in 2024 but uncertainty is large

The uncertainty about the duration, scope and intensity of the conflict, and hence its economic impact, is large. The projections assume no further regional escalation of the conflict, with the main economic impact confined to the last quarter of 2023 and to a lesser extent the first quarter of 2024. Government consumption will rise but falling economic sentiment, high uncertainty, temporary business closures, in particular in the retail, food services and construction sectors, a significant temporary reduction in the civilian labour force and transport disruption will markedly reduce private consumption and investment growth. A drop in tourism (about 5% of total exports) will also weigh on export growth. The projections assume that economic activity will start to recover in 2024 and growth will rise above the potential rate in 2025. Inflation developments will depend on the interplay of supply and demand disruptions. The projections assume that supply disruptions will add some inflationary pressure in the near term. With supply restrictions easing and demand only gradually recovering, inflation will abate in the medium-term. A further escalation into a regional conflict or a more prolonged conflict could lead to more severe supply disruptions, plummeting sentiment and higher risk perceptions, with much more pronounced effects on economic growth and public finances. After the conflict, domestic political tensions (including around the judicial reform) could re-intensify and lead to higher uncertainty.

## Policies should mitigate the economic repercussions of the conflict

In the near-term, the scope for monetary policy accommodation may be constrained by exchange rate developments and above-target inflation. Fiscal space built-up after the pandemic can be used to support the economy. Planned temporary income and liquidity support measures to households and firms can cushion the impact of the war. The authorities could also consider refining the furlough scheme by allowing for a partial adjustment of hours in addition to full furloughs and introducing a small co-financing requirement for employers. With increased spending on defence, security, reconstruction and interest payments in the medium term, some re-prioritisation of permanent expenditure, based on spending reviews, will be needed to mitigate the impact on the public finances. Growth-enhancing spending, including for infrastructure investment and to improve educational outcomes, should be safeguarded. In addition, revenue could be raised, including by reducing inefficient tax expenditures. In the medium-term, structural reforms to strengthen work incentives and improve skills at all stages of the learning cycle are needed to address demographic challenges related to the rising share of population groups with weak labour market attachment. Preserving the rule of law is essential to maintain robust economic performance.

# Italy

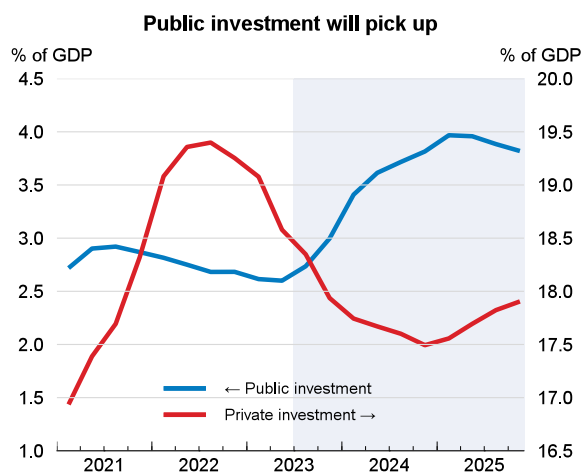
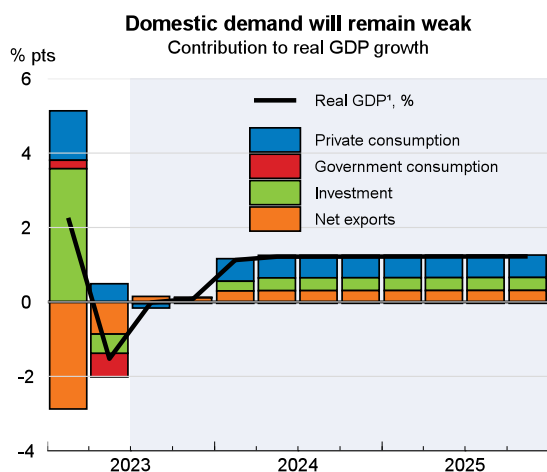
GDP growth is expected to slow to 0.7% in both 2023 and 2024, before picking up modestly to 1.2% in 2025. Low wage growth and high inflation have eroded real incomes, financial conditions have tightened, and most of the exceptional fiscal support related to the energy crisis has been withdrawn, weighing on private consumption and investment. The projected decline of inflation, targeted income tax cuts and the pick-up in public investment related to New Generation EU (NGEU) funds will only partly offset these headwinds. Risks are tilted to the downside. The main downside risk is a larger-than-expected tightening of financial conditions due to tighter euro area monetary policy or an increase in the risk premium on Italian government securities. On the upside, a significant pick-up in public investment related to the National Recovery and Resilience Plan (NRRP) could boost growth in 2024 and 2025.

The effects of monetary policy tightening have started to kick in, while fiscal support to households and businesses to tackle the energy crisis has been scaled back, although the latter is broadly offset by targeted income tax cuts and higher NRRP spending. The broadly neutral stance of fiscal policy will limit the slowdown in growth, but there is room to improve the budget balance more rapidly than currently planned to put the public finances on a more prudent path. Public spending needs to be contained, including by looking for options to reduce pension expenditure and raising the ambition of spending reviews. The speedy implementation of public investment plans and structural reforms in the NRRP will be key to sustain growth and reduce the debt ratio.

## Activity is slowing

GDP was flat in the third quarter, following the contraction of 0.4% in the second quarter that was partly due to exceptionally weak housing investment in the wake of tighter rules for house improvement tax credits. Recent high frequency indicators point to continued weakness in the near term. While industrial production appears to have bottomed out over the past few months, retail sales and confidence indicators remain weak. Despite the slowdown in activity, the unemployment rate remains historically low, employment continues to grow robustly, and nominal wage growth has picked up to around 3%, which should support household incomes and private consumption in the fourth quarter of 2023.

## Italy 1



1. Annualised quarterly rate.

Source: OECD Economic Outlook 114 database.

## Italy: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Italy</b>						
<b>GDP at market prices</b>	1 659.8	8.3	3.9	0.7	0.7	1.2
Private consumption	963.9	5.3	5.0	1.2	0.7	1.0
Government consumption	343.5	1.5	0.7	-0.2	-0.4	-0.2
Gross fixed capital formation	298.0	20.7	10.1	0.8	0.5	1.6
Final domestic demand	1 605.4	7.3	5.2	0.8	0.4	0.9
Stockbuilding <sup>1</sup>	- 4.4	1.0	-0.6	0.1	0.1	0.0
Total domestic demand	1 601.0	8.4	4.5	0.9	0.5	0.9
Exports of goods and services	485.8	14.0	10.7	0.4	1.3	2.0
Imports of goods and services	427.0	15.2	13.1	1.0	0.9	1.2
Net exports <sup>1</sup>	58.9	0.2	-0.5	-0.3	0.2	0.3
<i>Memorandum items</i>						
GDP deflator	–	1.3	3.0	4.2	2.9	2.6
Harmonised index of consumer prices	–	1.9	8.7	6.1	2.6	2.3
Harmonised index of core inflation <sup>2</sup>	–	0.8	3.3	4.6	3.1	2.5
Unemployment rate (% of labour force)	–	9.5	8.1	7.6	7.8	7.6
Household saving ratio, net (% of disposable income)	–	8.1	1.8	0.7	1.9	2.8
General government financial balance (% of GDP)	–	-8.8	-8.0	-5.4	-4.2	-3.6
General government gross debt (% of GDP)	–	172.9	148.5	148.2	148.3	147.4
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	147.2	141.6	141.4	141.4	140.5
Current account balance (% of GDP)	–	2.4	-1.5	-0.2	0.3	0.8

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.

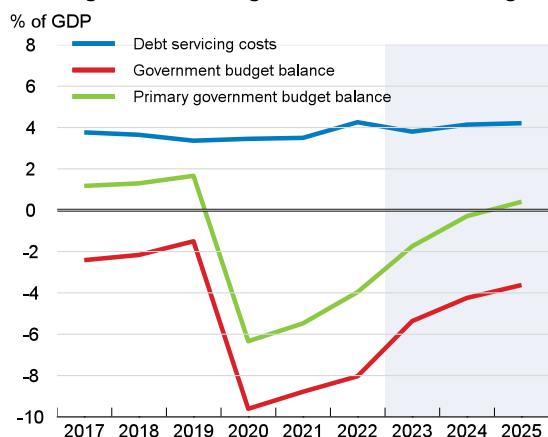
3. The Maastricht definition of general government debt includes only loans, debt securities, and currency and deposits, with debt at face value rather than market value.

Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/fthjeo>

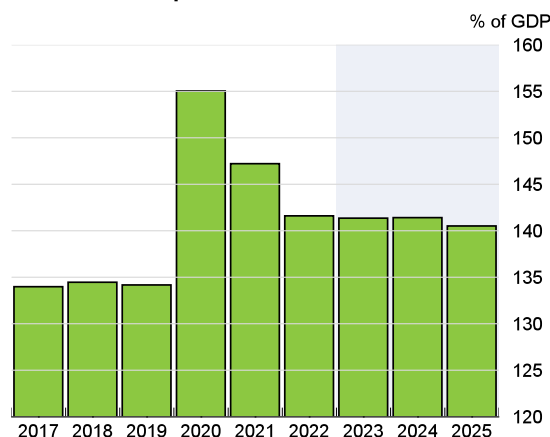
## Italy 2

**The government budget balance will remain negative**



Source: OECD Economic Outlook 114 database.

**The decline in the public debt ratio will come to a halt**



StatLink  <https://stat.link/fmbh3j>

Declines in international energy prices in the first half of 2023 have been transmitted rapidly to consumer price inflation, which declined from more than 12% in November 2022 to 1.8% in October 2023. However, increases in oil prices since the end of June are expected to slow the decline of inflation in the near term. Gas inventories are close to capacity and there has been significant progress in the geographical diversification of gas supply over the past year, limiting the risk of shortages. The tightening of global financial conditions has so far had limited negative spillovers on the banking sector, which has benefited from increased profitability due to higher net interest margins.

### Higher interest rates have had a strong impact

Borrowing costs for households and businesses have increased significantly over the past year following the tightening in euro area monetary policy, with rates reaching 4.2% on mortgages and 5.3% on loans to non-financial corporations in September. Lending standards have also tightened and lending growth has turned negative. Higher interest rates have raised debt servicing costs for the government, which are expected to reach about 4.2% of GDP in 2025.

Abstracting from the impact of a change in the accounting treatment of tax credits for home improvements, the stance of fiscal policy will be broadly neutral in 2024. The recent tightening of the rules for those tax credits will improve the government budget balance in 2024 on an accrual basis, but not on a cash basis, which is largely determined by tax credits granted over 2021-23 that are claimed in later years. Energy crisis support has been scaled back in the course of 2023, but some measures were extended to the fourth quarter, including targeted income support for low-income households, the suspension of fixed charges on gas bills and the reduction in value added taxes on gas. The government plans to phase out these measures over the course of 2024, which should provide fiscal savings of around 1% of GDP. These savings will be broadly offset by targeted income tax cuts for low and middle-income households and the expected ramp-up of spending related to Next Generation EU (NGEU). In 2025, the targeted income tax cuts introduced in 2024 and the targeted social security contribution cuts introduced in 2023 are scheduled to expire under current legislation, implying a mild fiscal tightening and an improvement in the primary fiscal balance of about ½ per cent of GDP. Overall, tight financial conditions and a broadly neutral fiscal policy in 2024 should lead to a gradual easing of inflationary pressures, while growth will remain modest.

### Growth will remain weak in the near term and inflation will recede

Real GDP is projected to grow 0.7% in 2023 and 0.7% in 2024, despite lower energy prices and the expected strengthening of NGEU-related spending, before picking up modestly in 2025. The tightening of financial conditions, the erosion of real incomes due to subdued wage growth and high inflation, and the scaling back of exceptional fiscal support related to the energy crisis will weigh on private consumption and investment. In 2024, these headwinds are only partly offset by spending financed from the remaining household savings accumulated during the pandemic, targeted income tax cuts and the expected pick-up in public investment related to Next Generation EU funds. Private consumption and private investment will remain weak. Inflation is expected to come down gradually over 2024-25 on the back of lower energy prices and moderate nominal wage growth. In 2025, the support to real household incomes from higher real wage growth, continued support from public investment and the strengthening of net exports due to recovering external demand will drive a modest pick-up.

Risks to growth are tilted to the downside. The main downside risk is a larger-than-expected tightening of financial conditions, which could arise from tighter euro area monetary policy or a higher premium on Italian government securities. On the upside, a significant pick-up in public investment related to the National Recovery and Resilience Plan (NRRP) could boost growth in 2024 and 2025.

### **Fiscal adjustment and structural reforms are needed to put the debt ratio on a more prudent path**

The government deficit will narrow but remain above 3% over 2024-25. The public debt ratio is high and there are substantial spending pressures from investment needs and ageing costs, which will increase by about 2½ per cent of GDP over 2023-2040. A sustained fiscal adjustment will be required over a number of years to put the debt ratio on a more prudent path, meet future costs and comply with proposed EU fiscal rules. This should include decisive action to tackle tax evasion, limit the growth of pension spending and ambitious spending reviews. The full implementation of the public investment and structural reform plans in the NRRP could durably lift Italy's GDP, which would have the added benefit of putting further downward pressure on the debt-to-GDP ratio. Progress with structural reforms has been substantial, but spending of NGEU funds is behind the original schedule, which mainly reflects delays in the implementation of public investment projects. The priorities should be to swiftly reallocate implementation to the highest-capacity public administrations, focus on growth-enhancing infrastructure projects, and abandon unviable projects.

# Japan

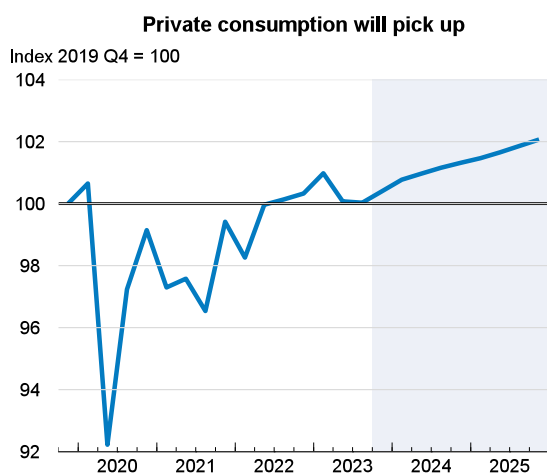
Real GDP growth is projected at 1.0% in 2024 and 1.2% in 2025, mainly driven by domestic demand. Private consumption will be supported by pent-up demand, stronger wage growth and the new economic package. Government subsidies for green and digital investment and high corporate profits will boost business investment, despite higher uncertainty. Headline inflation is projected to moderate but remain around 2% as wage growth gains momentum in 2024-25.

Record high gross government debt, at 246% of GDP in 2022, calls for a detailed and credible medium-term fiscal consolidation strategy, with further gradual increases in the consumption tax rate and measures to control spending. Structural reforms to boost employment and productivity are also key to put the public finances back on a sustainable trajectory and address demographic headwinds. Continued flexibility in the conduct of yield curve control and a gradual modest increase in the short-term policy interest rate are warranted, based on OECD projections of sustained inflation and wage growth.

## Domestic demand has slowed

Following robust growth in the first half of 2023, real GDP contracted by 0.5% in the third quarter. High uncertainty and inflation weighed on private consumption and investment. Headline consumer price inflation stood at 3.3% in October, reflecting decreasing energy prices and the extension of government energy subsidies. Corporate short-term inflation expectations fell slightly to 2.5% for the near term and 2.2% for three years ahead. Nominal wages have been trending up and are expected to gain momentum as the strong result of the *Shunto* wage negotiations (3.6% wage growth) spreads to SMEs.

## 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.

Source: OECD Economic Outlook 114 database; Ministry of Internal Affairs and Communications; and OECD calculations.



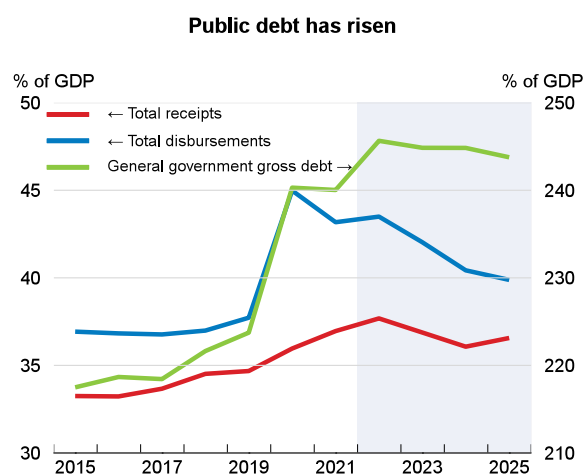
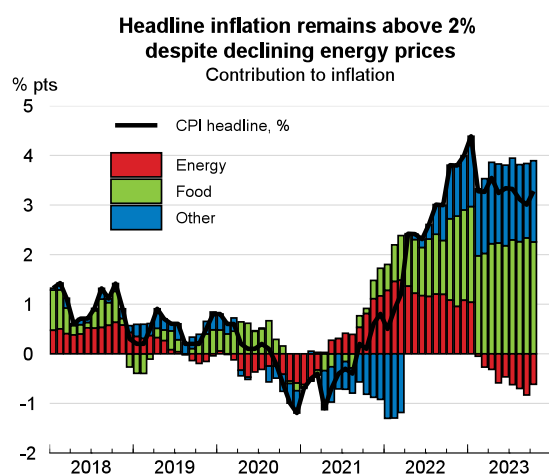
## Japan: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>Japan</b>						
	Current prices YEN trillion	Percentage changes, volume (2015 prices)				
<b>GDP at market prices</b>	539.3	2.2	0.9	1.7	1.0	1.2
Private consumption	291.1	0.4	2.0	0.7	0.7	0.7
Government consumption	113.2	3.5	1.2	0.5	-0.3	0.0
Gross fixed capital formation	137.8	0.2	-1.0	1.7	2.6	2.8
Final domestic demand	542.1	1.0	1.1	0.9	1.0	1.1
Stockbuilding <sup>1</sup>	- 1.4	0.2	0.4	-0.2	-0.2	0.0
Total domestic demand	540.7	1.2	1.5	0.8	0.8	1.1
Exports of goods and services	83.8	11.9	5.1	2.4	3.0	2.4
Imports of goods and services	85.3	5.1	8.0	-1.3	1.8	2.0
Net exports <sup>1</sup>	- 1.5	1.0	-0.6	0.8	0.2	0.1
<i>Memorandum items</i>						
GDP deflator	–	-0.2	0.3	3.5	2.6	2.2
Consumer price index <sup>2</sup>	–	-0.2	2.5	3.2	2.6	2.0
Core consumer price index <sup>3</sup>	–	-0.7	0.3	2.7	2.3	2.0
Unemployment rate (% of labour force)	–	2.8	2.6	2.6	2.5	2.4
Household saving ratio, net (% of disposable income)	–	7.7	5.4	3.3	3.4	1.8
General government financial balance (% of GDP)	–	-6.2	-5.8	-5.2	-4.4	-3.3
General government gross debt (% of GDP)	–	240.0	245.6	244.8	244.8	243.8
Current account balance (% of GDP)	–	3.9	1.8	3.4	3.8	4.0


- Contributions to changes in real GDP, actual amount in the first column.
  - Calculated as the sum of the seasonally adjusted quarterly indices for each year.
  - Consumer price index excluding food and energy.
- Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/j12hy3>

## Japan 2



Source: Ministry of Internal Affairs and Communications; OECD Economic Outlook 114 database; and OECD calculations.

StatLink  <https://stat.link/tc63ng>

In late October, yields on 10-year Japanese government bonds peaked at around 0.9% and the yen depreciated sharply, but pressures subsequently abated somewhat. Despite rising in September, business confidence in manufacturing remains well below that of the non-manufacturing sector. Corporate profits continue to increase and firms' investment plans remained strong in the Bank of Japan's September Tankan Survey, with large firms projecting a 13.6% increase in nominal capital expenditure in FY 2023. Buoyant automobile exports were offset by high service imports in the third quarter. The number of inbound tourists slightly surpassed 2019 levels in October, although the recovery in tourists from China is sluggish at only 35% of pre-pandemic levels.

## Macroeconomic support is projected to gradually decrease

The new economic package announced in November includes measures to moderate the impact of high prices and support medium-term investment in several areas, such as economic security, green and digital transformation, and education. It includes cash handouts to low-income households and temporary cuts to income and residential taxes, which will cost JPY 1.1 trillion (0.2% of GDP) and around JPY 4 trillion, respectively. The current subsidies to cushion the impact of higher fuel oil, electricity and city gas prices are also extended until April 2024, with those for electricity and city gas to continue at reduced rates from May 2024. The related supplementary budget, which also includes expenditures expected to be implemented over multiple years, will be around JPY 13.1 trillion in FY 2023 (2.3% of GDP). The OECD projections assume that the subsidies will remain in place until the end of 2024, albeit gradually declining over time, alongside an annual increase in defence spending of around JPY 1 trillion in 2024-25. Fiscal support is projected to decline with the end of pandemic-related measures and the gradual decline in price subsidies in 2024 and the phase-out of subsidies in 2025. The gross public debt-to-GDP ratio is projected to remain high at 243.8% in 2025.

The short-term policy interest rate remains unchanged at -0.1%, but the conduct of yield curve control has been modified twice in 2023. With the second adjustment in late October, the Bank of Japan shifted to an upper bound of 1% for the yield target of 0% for 10-year Japanese government bonds and stated that the upper bound will serve as a reference, with yields controlled mainly through large-scale Japanese government bond purchases and market operations. Such adjustments to further increase flexibility should be continued. OECD projections of sustained inflation around 2%, increasing wage growth and a closing of the output gap imply a gradual increase in the policy rate is warranted, starting from early 2024. However, if the positive wage-inflation cycle gets underway more slowly than projected, the Bank of Japan is likely to wait for longer before raising interest rates.

## Growth will moderate in 2024-25

GDP growth is projected at 1.0% in 2024 and 1.2% in 2025, as the positive contribution of net exports declines. Private consumption will be supported by rising wages and the new economic package. Business investment will grow, supported by government subsidies and high corporate profits. Public investment in large-scale projects will support growth in 2024. The labour market will remain tight, contributing to higher wage growth in 2024-25. Headline consumer price inflation is projected to increase to over 2% by the end of 2025 as government subsidies end, the output gap closes and wage growth gains momentum.

A key source of uncertainty is the impact of rising import price inflation due to the yen's depreciation and renewed energy price increases. Weaker-than-expected external demand, including a sharper slowdown in China, and further supply chain disruptions due to geopolitical tensions, would lower growth. Persistent cost pressures and further monetary policy tightening in other advanced economies could create pressures on the monetary policy framework, necessitating abrupt changes. On the upside, further depreciation of the yen could strengthen price competitiveness of exports, including inbound tourism.

## Securing fiscal sustainability is key

Rebuilding fiscal buffers and ensuring debt sustainability should be prioritised, in the context of increasing debt service risks associated with a possible rise in long-term interest rates. Prolonged price caps should be phased out. These add to fiscal sustainability challenges and could reduce incentives to shift to renewables and lower energy demand by distorting market signals. Overreliance on supplementary budgets and contingency reserve funds lowers the transparency of fiscal projections and targets. Announcing the concrete revenue and expenditure measures needed for medium-term fiscal consolidation would boost the credibility and sustainability of fiscal policy. Population ageing will raise fiscal pressures, with national projections of an increase of around JPY 17 trillion (2.7% of projected GDP in 2025) in health, long-term care and pension expenditures between FY 2024 and 2040. Raising the pension eligibility age beyond the target of 65, in line with rising life expectancy, would help raise the employment of older persons and reduce fiscal costs. Expanding social security coverage for non-standard workers and enhancing vocational training and education could boost labour productivity and labour supply. Continuing Work Style reforms, including equal pay for equal work and flexible work arrangements, and improving child-care provision, would promote female employment and reduce Japan's large gender wage gap. Lowering barriers to foreign workers and foreign direct investment would also help. Faster progress with the digital and green transformation is also needed. Enhancing energy security and lowering dependence on fossil fuels requires stepping up the promotion of research, development and deployment of clean energy technologies, including renewable energy, and encouraging greater energy efficiency.

# Korea

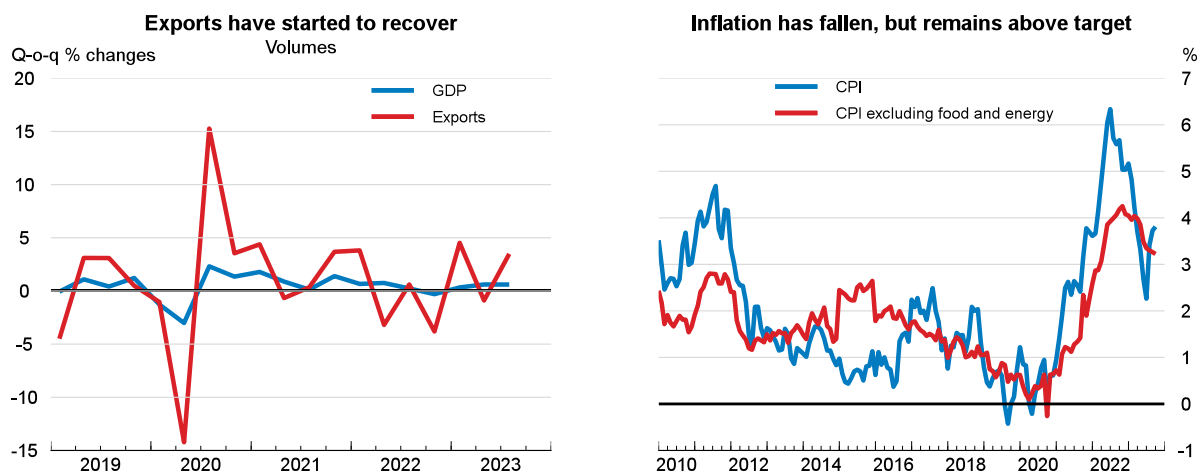
GDP growth is expected to ease to 1.4% in 2023, before rebounding to 2.3% in 2024 and 2.1% in 2025. Elevated interest rates and energy prices are weighing on private consumption and investment in the near term. Exports will strengthen as semiconductor sales recover. Energy and food prices have pushed up consumer prices, but inflation will gradually moderate and reach the target in 2025. Unemployment is set to increase from the current historically low level as weak demand reduces hiring.

The Bank of Korea has maintained the policy rate at 3.5% since January 2023 and signalled that monetary policy will remain tight for some time. Fiscal consolidation should proceed given rapid population ageing, and the proposed fiscal rule should be implemented. Support to households should increasingly address gaps in social protection schemes, including eligibility and enforcement. Structural reforms should facilitate the reallocation of labour and capital to address high productivity gaps.

## Growth is weak, but there are emerging signs of recovery

Domestic demand remains weak, but exports have bottomed out. Real GDP grew by 0.6% in the third quarter of 2023, mainly driven by exports. Private consumption and investment were subdued reflecting high interest rates, weak real wage growth and a sluggish housing market. Exports strengthened further in October, according to customs data, on the back of recovering semiconductor demand. Headline inflation rose to 3.8% in October due to higher energy and food prices, but core inflation has moderated, even though it remains well above the 2% target. The labour market has held up well, with a historically high employment rate and low unemployment.

## Korea



Source: OECD National Accounts database; and Bank of Korea.

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## Korea: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices KRW trillion	Percentage changes, volume (2015 prices)				
<b>Korea</b>						
<b>GDP at market prices</b>	1 940.7	4.3	2.6	1.4	2.3	2.1
Private consumption	900.3	3.6	4.1	1.9	1.4	2.2
Government consumption	350.1	5.5	4.0	1.2	1.1	1.8
Gross fixed capital formation	607.5	3.2	-0.5	1.6	1.6	2.0
Final domestic demand	1 857.9	3.8	2.6	1.6	1.4	2.0
Stockbuilding <sup>1</sup>	11.3	-0.1	0.1	0.0	-0.1	0.0
Total domestic demand	1 869.2	3.7	2.6	1.6	1.3	2.0
Exports of goods and services	705.6	11.1	3.4	2.3	4.0	2.9
Imports of goods and services	634.1	10.1	3.5	2.9	1.9	2.6
Net exports <sup>1</sup>	71.5	0.7	0.1	-0.3	0.9	0.1
<i>Memorandum items</i>						
GDP deflator	–	2.8	1.3	1.9	3.5	2.7
Consumer price index	–	2.5	5.1	3.6	2.7	2.0
Core inflation index <sup>2</sup>	–	1.4	3.6	3.5	2.4	2.0
Unemployment rate (% of labour force)	–	3.6	2.9	2.7	2.9	3.1
Household saving ratio, net (% of disposable income)	–	12.6	10.8	12.4	13.1	13.1
General government financial balance (% of GDP)	–	-0.3	-1.8	-1.9	-1.7	-1.3
General government gross debt (% of GDP)	–	50.9	54.8	58.4	62.8	66.2
Current account balance (% of GDP)	–	4.7	1.7	1.3	1.4	1.8

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 114 database.

StatLink  <https://stat.link/0acmwu>

A slowdown in global demand along with delayed recovery in China, notably for semiconductors, has dampened exports until recently. Rising global bond rates are set to push up domestic bond yields, increasing the interest burden for the government and the private sector.

## Monetary policy remains tight, and fiscal policy is mildly restrictive

The Bank of Korea has kept the policy rate on hold at 3.5% since January 2023. The policy rate is assumed to remain at the current level until the second half of 2024, before being cut gradually to 2.5% by 2025 as inflation approaches the 2% target. The fiscal stance in 2023 is expected to be less contractionary than in the government's original consolidation plan, due to a massive revenue shortfall. The budget for 2024 is mildly restrictive despite contained expenditure growth, as tax revenue is assumed to remain sluggish. The projected contractionary fiscal stance in 2025 is in line with the government's consolidation plan.

## Growth is projected to rebound

Real GDP growth is projected to be 1.4% in 2023, strengthening to 2.3% in 2024 and 2.1% in 2025. Exports are set to pick up with a recovery in semiconductor demand. Elevated debt servicing burdens and inflation will continue to weigh on private consumption and investment in the short term, but demand should strengthen from the second half of 2024. Inflation will gradually moderate and reach the target in 2025. Further turmoil in global financial markets could hold back growth by raising the debt servicing burden for households and firms. Increasing geopolitical tensions may threaten Korean supply chains. Stronger-than-expected global growth and easing geopolitical tensions would improve the economic outlook for the export-dependent Korean economy.

## Structural challenges require policy action

Against the backdrop of rapid population ageing, spending pressures are set to increase by approximately 5% of GDP by 2040 according to the OECD long-term model, driven by pensions and health expenditure. Fiscal consolidation is key to meet this challenge. The proposed fiscal rule, which caps the managed budget deficit at 3% of GDP, should be implemented to limit the build up of fiscal pressure. The pension reform needs to ensure adequate retirement income and fiscal sustainability. The government recently extended a temporary fuel tax cut until the end of 2023 to lower energy bills. It would be better to target vulnerable groups more directly, notably by addressing gaps and weaknesses in the social safety net, including eligibility and enforceability. Reducing the stringency of product market regulation by, for example, shifting to a comprehensive negative-list regulatory system and streamlining public support to SMEs would help to lower productivity gaps between large and small firms and reduce labour market dualism. Policies should also focus on reconciling career and family, including increasing the take-up of parental leave and enabling more flexible working arrangements to boost female employment and fertility. To further reduce greenhouse gas emissions, the emission trading scheme should be aligned with climate targets, and incentives for clean electricity supply and energy savings should be enhanced.

# Latvia

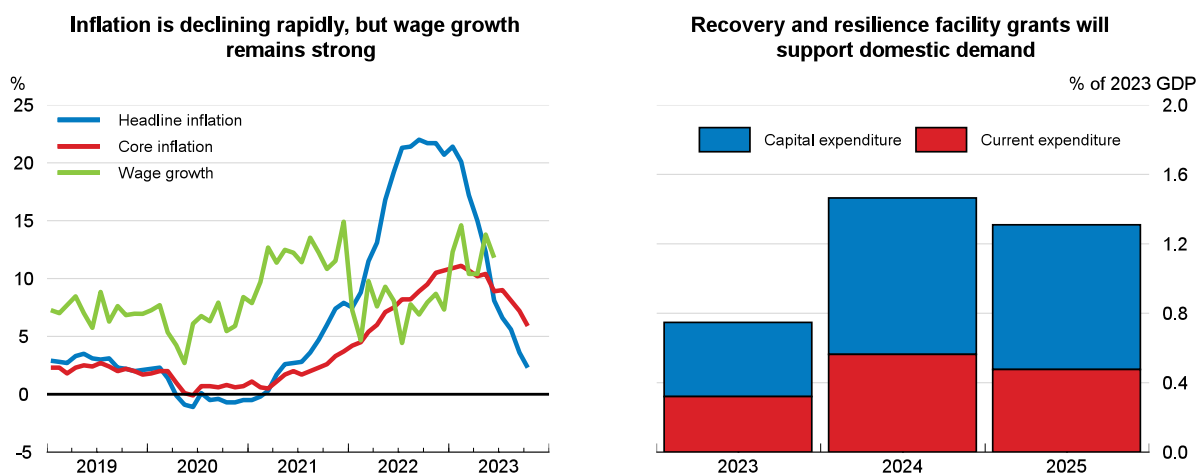
Real GDP is projected to grow by 1.9% in 2024 and 2.7% in 2025 after contracting slightly in 2023. Declining inflation and strong nominal wage growth will bolster private consumption. Tight financing conditions will weigh on housing and business investment, while public investment growth will accelerate as EU funds are absorbed. However, skilled labour shortages and weak capacity in infrastructure planning risk hindering the implementation of investment plans.

To contain inflationary pressures, it is essential to gradually tighten the fiscal stance. Additional spending on health, education and defence should be financed by raising spending efficiency and increasing tax revenue from property, inheritance and capital gains taxes. Skilled labour shortages, including in the public sector, should be addressed by improving access to, and the quality of, training and adult learning, facilitating skilled migration and fostering the adoption of digital technologies. Deepening capital markets by listing large state-owned enterprises would improve access to finance and support investment.

## High inflation and weak exports have weighed on growth


After a technical recession in the first half of 2023, GDP increased by 0.6% in the third quarter of 2023. Strong public investment, helped by the absorption of EU funds, has more than compensated for weak export demand and private consumption. Industrial production increased in recent months, but was still about 3% lower than a year earlier. High interest rates and weak confidence have weighed on private investment and construction. Annual inflation has fallen rapidly to 2.3% in October, due to declining energy and food prices, but core inflation remains high at 5.9%. Average monthly gross wages increased by 12% year-on-year in June, resulting in a slight real wage increase of 0.1%. The labour market remains tight with unemployment at 6.5% in October and a vacancy rate of 2.7%, only 0.3 percentage points lower than its pre-pandemic value, indicating strong skilled labour shortages.

### 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. Wages refer to average monthly wages and salaries of employees. The right-hand panel shows the projected allocation of revenue from the Recovery and Resilience Facility grants.

Source: OECD Prices database; Statistical Central Bureau of Latvia; 2023-26 Stability Programme of Latvia; OECD Economic Outlook 114 database; and OECD calculations.

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## Latvia: Demand, output and prices


	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Latvia</b>						
<b>GDP at market prices</b>	30.1	6.7	3.4	-0.1	1.9	2.7
Private consumption	17.2	7.3	6.0	-1.6	2.1	3.3
Government consumption	6.1	3.5	2.8	4.4	0.8	1.0
Gross fixed capital formation	6.8	7.2	0.6	5.6	2.2	4.0
Final domestic demand	30.0	6.4	4.1	1.0	1.9	3.0
Stockbuilding <sup>1</sup>	-0.3	4.0	0.2	0.5	-0.1	0.0
Total domestic demand	29.7	10.3	4.1	1.4	1.8	3.0
Exports of goods and services	18.3	9.0	10.3	-3.4	1.0	2.9
Imports of goods and services	17.9	15.1	11.1	-1.3	0.8	3.4
Net exports <sup>1</sup>	0.4	-3.5	-0.9	-1.4	0.1	-0.4
<i>Memorandum items</i>						
GDP deflator	–	3.8	12.8	5.3	3.2	3.3
Harmonised index of consumer prices	–	3.2	17.2	9.4	3.1	3.3
Harmonised index of core inflation <sup>2</sup>	–	1.9	7.6	8.7	4.3	3.3
Unemployment rate (% of labour force)	–	7.6	6.8	6.4	6.5	6.4
Household saving ratio, net (% of disposable income)	–	1.9	-7.2	-4.2	-4.1	-4.2
General government financial balance (% of GDP)	–	-7.2	-4.6	-3.3	-2.9	-2.3
General government gross debt (% of GDP)	–	57.8	49.8	50.7	51.1	50.5
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	44.0	41.0	41.9	42.3	41.7
Current account balance (% of GDP)	–	-3.9	-4.7	-3.2	-3.5	-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 114 database.

StatLink  <https://stat.link/4fu6d>

Weaker growth in major export markets and falling export and import prices are weighing on foreign trade. Both export and import values have declined since the spring and in September the volume of foreign trade was around 23% lower than a year earlier. The transport sector and the manufacture of wood and metal products have been hit hard by the sanctions against Russia and Belarus. Tight financial conditions are moderating domestic demand. Rising interest rates on new mortgages remain the highest in the Baltic region, outweighing the impact of falling prices for older dwellings and reducing overall housing affordability.

## Fiscal policy will face multiple expenditure pressures

Fiscal policy will be broadly neutral in 2024, reflecting announcements to increase spending on health and education, improve cybersecurity and external border infrastructure and maintain support for Ukrainian refugees. Defence spending will increase from around 2.2% of GDP in 2023 to 3% of GDP by 2027. Newly introduced energy policy support measures cost 0.1% of GDP in 2023 and any further support is assumed to be phased out by April 2024. Additional expenditure pressures stem from rising general government interest payments, which are estimated to reach around 1% of GDP by 2025. EU Recovery and Resilience Facility grants will finance capital expenditure as well as training measures for small businesses to foster digital and management skills, with average yearly spending of about 1.3% of GDP in 2024-25. Higher indexation of pension benefits in 2022-23 in response to the cost-of-living crisis and the rapid ageing of the population is expected to reverse the surplus of the social security fund from 0.3% of GDP in 2023 to a deficit of 0.1% of GDP in 2026. The fiscal stance will be tightened in 2025 to ensure a slight decline in



the general government gross debt-to-GDP ratio towards the government's objective of 40% in the medium term.

### **Domestic demand will lead the recovery**

Falling inflation and rising nominal wages will support real incomes and raise private consumption over the next two years. Although tight financial conditions will weigh on investment, the significant inflow of EU funds will boost public infrastructure investment and spending on support measures for digitalisation and upskilling in small businesses, which will help to crowd in private investment. Wage growth will remain strong due to skills shortages and planned increases in public sector and minimum wages, leading to sticky core inflation. Delays in the absorption of EU funds and weaker-than-expected growth in key export destinations are the major downside risks. On the upside, a warm winter would contribute to a rapid decline in energy prices and inflation, further boosting household real disposable income and private consumption.

### **Supporting investment and inclusive growth**

The listing of state-owned enterprises would help improve their governance and attract investors. This could deepen capital markets and raise access to finance for other firms. Improving public procurement and infrastructure planning capacity, particularly at the municipal level, is key for the successful implementation of EU funds and raising productivity. Introducing progressively-increasing social security contributions for low-income earners and stepping up enforcement efforts would help to reduce informality. This also requires raising trust in institutions and continuing the fight against corruption, for example by applying the heavy fines for tax evasion and bribery that current legislation allows. To accelerate the green transition, price signals in household energy consumption should be maintained to create incentives for improving energy efficiency, while supporting vulnerable households with loan subsidies or grants. Strengthening competition enforcement would help to raise business dynamism, innovation and productivity.

# Lithuania

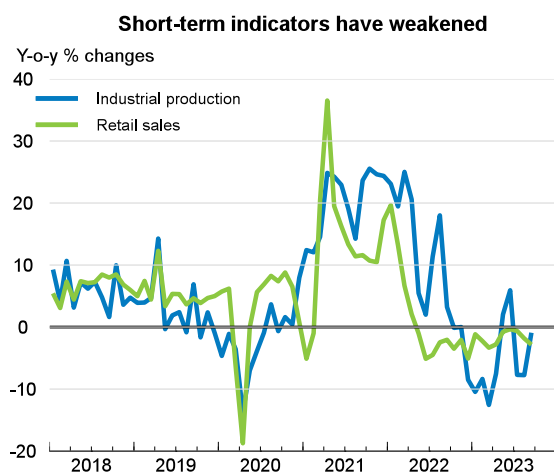
The economy is projected to contract in 2023 by 0.4%, before growing by 1.7% in 2024 and 3.1% in 2025. Although inflationary pressures and supply chain disruptions are receding, higher than expected oil prices have slowed the decline of inflation and will lead to a contraction in private consumption in 2023. Uncertainty and geopolitical tensions will weaken demand in key trading partners and contribute to a slowdown in exports. Public investment, strengthened by EU funds, will support growth. The labour market remains tight with robust wage growth and shortages of high-skilled workers.

Fiscal policy support is helping households and firms with elevated energy costs. Better targeting to vulnerable groups could make this more efficient. Unwinding state support of industry would alleviate some fiscal pressure. Improving participation in lifelong education would help to increase digital skills and help older workers to enter high-growth industries. More targeted support for innovation, particularly for low-carbon technology adoption, would help to tackle hard-to-abate emissions in transport and industry.

## Manufacturing is slowing but consumer confidence is recovering

The economy slowed in the first half of 2023 as the impact of uncertainty from geopolitical tensions, rising interest rates and deteriorating business confidence weighed on activity. GDP also declined marginally in the third quarter of 2023. Industrial confidence has been negative for 17 consecutive months recording its lowest levels since the pandemic. Manufacturing production, retail sales and exports have contracted in recent months. However, consumer confidence is recovering, unemployment remains low, wage growth is robust, and inflation has eased to 3.1% in October. These factors lay the grounds for a rebound in private consumption.

### Lithuania



Source: OECD Main Economic Indicators database; and European Commission business and consumer surveys.

## Lithuania: Demand, output and prices


	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Lithuania</b>						
<b>GDP at market prices</b>	49.9	6.3	2.4	-0.4	1.7	3.1
Private consumption	28.7	8.1	2.0	-0.5	3.2	3.3
Government consumption	9.2	1.2	0.4	0.0	0.7	1.9
Gross fixed capital formation	10.7	9.4	3.6	7.3	3.3	3.2
Final domestic demand	48.6	7.1	2.1	1.3	2.8	3.0
Stockbuilding <sup>1</sup>	-3.4	-0.4	0.0	-3.3	-0.4	0.0
Total domestic demand	45.2	7.7	2.9	-1.2	2.4	3.1
Exports of goods and services	36.5	17.0	12.2	-2.8	1.8	4.4
Imports of goods and services	31.8	19.9	12.4	-4.5	2.8	4.5
Net exports <sup>1</sup>	4.6	-0.3	0.4	1.6	-0.6	0.0
<i>Memorandum items</i>						
GDP deflator	–	6.5	16.5	8.3	3.8	3.0
Harmonised index of consumer prices	–	4.6	18.9	8.8	2.0	2.1
Harmonised index of core inflation <sup>2</sup>	–	3.4	10.5	9.7	4.0	2.2
Unemployment rate (% of labour force)	–	7.1	5.9	6.8	5.9	4.6
Household saving ratio, net (% of disposable income)	–	7.6	1.2	7.3	14.2	15.4
General government financial balance (% of GDP)	–	-1.1	-0.7	-2.6	-3.4	-2.7
General government gross debt (% of GDP)	–	50.4	37.9	39.8	42.6	44.4
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	43.4	38.1	40.0	42.8	44.6
Current account balance (% of GDP)	–	1.4	-5.4	-0.3	-1.5	-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 114 database.

StatLink  <https://stat.link/d2w9rt>

Russia's war of aggression against Ukraine has continued to have a sizeable impact on the economy. Temporary measures related to assistance for displaced people from Ukraine and energy price support for household and firms have added to public expenditure. As of September 2023, over 72,000 Ukrainian refugees had registered for temporary protection. Persistently high inflation and slowing growth in the euro area have curbed external demand and led to a contraction in exports and manufacturing production.

## Fiscal policy is supportive in 2023 but will tighten in 2024-25

Tighter monetary conditions are cooling the housing market and building permits have declined sharply during the first half of 2023. Countercyclical fiscal policy in 2023 implies an increase in the structural deficit, partly owing to temporary spending items worth 1.9% of GDP related to the war in Ukraine. Natural gas price compensation for households has been extended to the end of 2023, but subsidies for electricity have been discontinued. Support will continue for the state railway company which is experiencing losses due to sanctions on Russia and Belarus. Lower-than-expected refugee arrivals and lower costs of acquiring military equipment have allowed some fiscal savings and by 2024-25, large-scale measures supporting households and firms will no longer be needed. The general government budget deficit is expected to fall in 2025, after having risen in 2023 and 2024. Government debt will increase over 2023-2025. The cost of pensions and healthcare are projected to increase by 0.8% and 0.4% of GDP by 2030 due to demographic pressures. Investment will be boosted by implementation of the EU Recovery and Resilience Plan (RRP).

## Growth will pick up progressively, restrained by weak exports

After a projected decline in GDP in 2023, due to persistently weak demand in key export markets and lower consumer spending, GDP growth is expected to resume in 2024 and 2025. Strong real wage growth will support a rebound in private consumption. Public investment will increase with the progressive deployment of EU Recovery and Resilience funds, but private investment will continue to be weighed down by a weak housing market. Export growth is expected to strengthen in 2025 as export markets begin to recover. Lithuania risks losing part of the RRP funding if a real estate bill is not passed or not properly implemented. Stronger than expected wage growth could undermine export competitiveness and push up inflation. On the upside, strong wage growth, coupled with rapidly falling inflation, could support a more forceful rebound in private consumption.

## Securing stronger and more sustainable growth

A general unwinding and stronger targeting of energy price support would reduce fiscal exposure to energy price movements and help rebuild fiscal space. There is a sizeable productivity gap between small and large firms, which could be narrowed with greater use of digital technologies. Promoting higher participation in lifelong education would be one way to achieve this, and could also make growth more inclusive. Reaching emission reduction targets, especially in hard-to-abate sectors like transport and industry, will require a greater role for technology diffusion, helped by more targeted support for innovation and technology adoption.

# Luxembourg

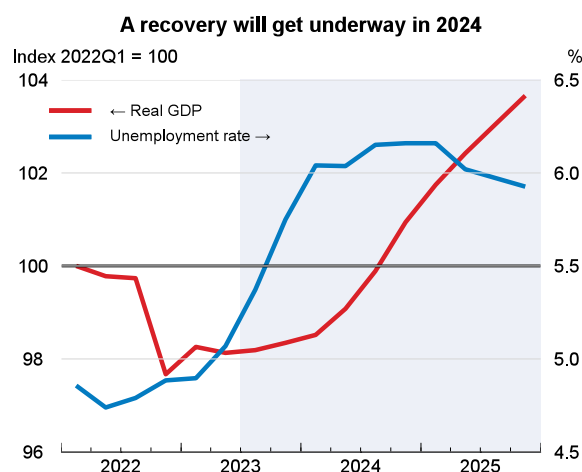
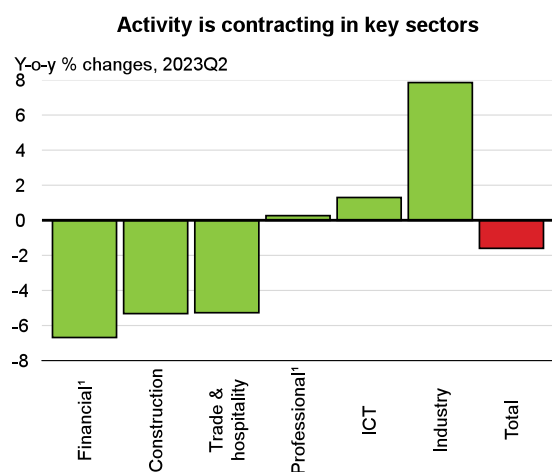
GDP will shrink by about 1.1% in 2023, driven down by a deep contraction of the key financial services sector, before rising by 1.4% in 2024 and 3.1% in 2025, supported by monetary policy easing. The unemployment rate will keep increasing up to the end of next year. Headline inflation will rebound at the beginning of next year, due to base effects and wage indexation, before declining towards 2% in 2025.

Fiscal policy is supporting household incomes through the generous unemployment insurance system and energy support measures, but energy support should be unwound as the economy recovers over 2024-25. The indexation of wages to headline inflation has preserved real wages but risks undermining firm productivity. The government should address long-term fiscal pressures stemming from the pension system and work disincentives due to the joint taxation of couples.

## Activity has contracted

Activity contracted sharply at the end of 2022 and has remained weak this year, primarily reflecting the impact of tighter financial conditions on Luxembourg's large financial services sector. Business surveys and hard economic indicators point to a further deterioration in the second half of 2023. The housing market is undergoing a correction and credit is shrinking due to tighter lending conditions. The ongoing slowdown is weakening the labour market. While headline inflation eased in early 2023, it has recently increased due to the indexation of wages to inflation.

## Luxembourg



1. Services.

Source: Statec; and OECD Economic Outlook 114 database.

StatLink  <https://stat.link/81yu3v>

## Luxembourg: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Luxembourg</b>						
<b>GDP at market prices</b>	64.5	7.2	1.4	-1.1	1.4	3.1
Private consumption	19.5	11.3	2.3	2.4	2.1	4.0
Government consumption	11.9	5.4	2.9	3.3	4.5	1.9
Gross fixed capital formation	10.8	16.0	-7.3	0.7	-0.7	1.6
Final domestic demand	42.2	11.3	-0.1	2.2	2.0	2.8
Stockbuilding <sup>1</sup>	0.4	0.2	-0.5	-0.5	0.4	0.0
Total domestic demand	42.6	12.5	-0.4	1.3	2.6	2.8
Exports of goods and services	131.0	10.3	-0.6	-2.1	0.5	2.7
Imports of goods and services	109.0	12.4	-1.9	-1.4	0.5	2.5
Net exports <sup>1</sup>	21.9	-0.1	2.1	-2.0	0.1	1.3
<i>Memorandum items</i>						
GDP deflator	–	4.5	6.2	8.4	6.8	3.0
Harmonised index of consumer prices	–	3.5	8.2	3.1	3.4	2.3
Harmonised index of core inflation <sup>2</sup>	–	1.5	4.2	4.1	3.7	2.5
Unemployment rate (% of labour force)	–	5.7	4.8	5.3	6.1	6.0
Household saving ratio, net (% of disposable income)	–	12.2	11.6	16.1	14.3	11.3
General government financial balance (% of GDP)	–	0.6	-0.3	-2.6	-2.9	-1.9
General government gross debt (% of GDP)	–	31.4	29.3	30.6	32.4	33.1
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	24.5	24.6	25.9	27.7	28.4
Current account balance (% of GDP)	–	7.9	7.6	4.6	6.7	6.6

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 114 database.

StatLink  <https://stat.link/a7eyvd>

Expectations of tight-for-long monetary policy have prolonged the decline in global bond prices, negatively affecting Luxembourg's key mutual fund industry. Activity in key trading partners has been slowing, while growth in global trade has almost halted. Rising stress in global financial markets, due to geopolitical tensions, may add further pressures. Spillovers from global energy markets to households have been largely contained due to energy price caps.

## Fiscal policy will turn restrictive next year

Euro area monetary policy will remain tight in the short term, before easing gradually over 2025. Fiscal policy support in 2024 will come from measures legislated last year and broadly extended into next year. These include energy price caps for households, the indexation of the personal income tax brackets, subsidies for disadvantaged households and energy-intensive firms, and cuts in employers' social security contributions. These measures support incomes, and aim at keeping inflationary pressures in check to limit the extent of the automatic wage indexations to inflation, but disincentivise energy savings. Most of the measures are due to expire in 2024 and are assumed to not be renewed. The budget deficit will widen to 2.6% of GDP in 2023 and 2.9% in 2024, before improving to 1.9% in 2025 as the fiscal stance is tightened and the economy recovers.

## Activity will recover robustly over 2024-25

The economy will contract further in the second half of this year, dragged down by weak exports on the back of tight financial conditions and slowing global trade, with GDP declining by 1.1% in the year as a whole. Activity will remain subdued in the early part of next year before picking up gradually, driven by the recovery of the key financial services sector, which will benefit from the onset of monetary policy easing in the major economies. GDP growth will be about 1.4% in 2024 and increase to 3.1% in 2025, supported by the continued pick up in exports and the recovery of the construction sector. Yearly headline inflation will rise in the early part of next year due to base effects, as the effect of energy price caps will fade, to then gradually decrease to just above 2% around end-2025. Core inflation will prove stickier, due to past and future rounds of wage indexation. The unemployment rate will rise to 6.2% by the end of 2024, due to the contraction of labour-intensive sectors such as retail trade, hospitality, and construction, and remain around 6% throughout 2025, lagging the economic recovery. An earlier-than-expected recovery in financial asset prices may provide an unexpected boost in activity, while a deeper-than-anticipated housing market correction may dent household wealth and lead to higher precautionary savings.

## The government should focus on embedding resilience

Phasing out discretionary fiscal policy measures as the economy recovers will be important to limit the build-up of the public debt, which is projected to increase from about 24½ per cent of GDP in 2022 to about 28½ per cent in 2025. Reforming the pension system is needed to manage long-term fiscal sustainability pressures, as age-related spending is set to rise by over 4 percentage points of GDP from now until 2050 under current policies. Weakening the link between inflation in imported energy goods and wage re-indexation would promote a more balanced burden sharing of negative supply side shocks between workers and firms, thus preserving firm competitiveness without the need for government interventions. Addressing work disincentives from the joint taxation of couples would help to further reduce gender gaps in the labour market and improve growth prospects.

# Mexico

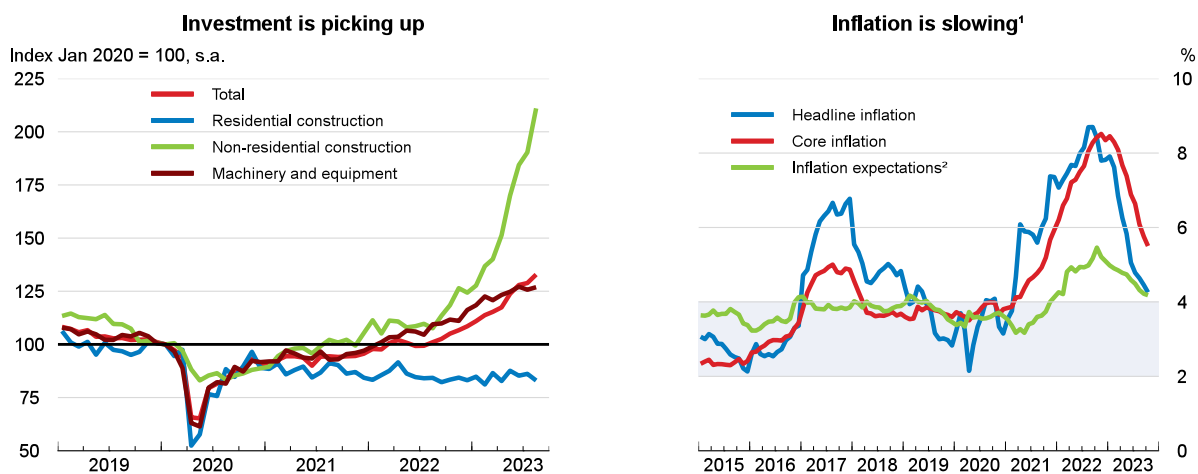
The economy is projected to expand by 2.5% in 2024 and by 2% in 2025, after growing by 3.4% in 2023. Consumption will be supported by a strong labour market. Investment will be backed by public infrastructure projects which are expected to be finalised in 2024 and by the nearshoring of manufacturing activities to Mexico. Export dynamism will be mitigated by milder growth in the United States. Inflation will edge down to 3.9% in 2024 and 3.2% in 2025.

Monetary policy should remain restrictive to ensure that inflation decreases durably towards its target. Targeting social spending increases on low-income households and basing public investment projects on sound cost-benefit analysis would boost public spending efficiency and mitigate inflationary risks. Higher regulatory certainty, including in the energy sector, would help to make the most of the ongoing nearshoring of production processes to Mexico.

## Domestic demand is resilient

Short-term indicators show consumption remaining resilient and investment trending up, particularly in non-residential construction, supported by public infrastructure projects in the south, and investment in machinery and equipment related to nearshoring. Mexican industrial parks across the United States border are at full capacity. Export growth and manufacturing production have remained solid, particularly in the automotive sector. Headline inflation has continued to decline, reaching 4.3% year-on-year in October, while core inflation remains stickier, at 5.5%. Inflationary pressures remain particularly high in services.

## Mexico



1. The shaded area represents the central bank's inflation target range.

2. Private sector inflation expectations for the next 12 months.

Source: INEGI; and Bank of Mexico.

StatLink  <https://stat.link/cs49hr>



## Mexico: Demand, output and prices


	2020	2021	2022	2023	2024	2025
	Current prices MXN billion	Percentage changes, volume (2018 prices)				
<b>Mexico</b>						
<b>GDP at market prices</b>	24 079.8	5.8	3.9	3.4	2.5	2.0
Private consumption	15 920.6	8.1	6.2	4.6	2.7	2.6
Government consumption	2 941.5	-0.5	1.3	1.8	2.1	0.9
Gross fixed capital formation	4 833.2	9.3	8.6	18.0	5.7	3.8
Final domestic demand	23 695.3	7.3	6.1	7.1	3.4	2.7
Stockbuilding <sup>1</sup>	- 4.8	0.2	0.0	0.0	0.0	0.0
Total domestic demand	23 690.5	7.5	6.1	6.8	3.2	2.7
Exports of goods and services	9 450.5	7.2	9.0	-3.5	3.1	4.2
Imports of goods and services	9 061.2	15.0	8.9	7.9	5.5	5.6
Net exports <sup>1</sup>	389.3	-3.0	-0.1	-5.0	-1.3	-1.0
<i>Memorandum items</i>						
GDP deflator	–	4.4	6.7	3.7	3.6	2.7
Consumer price index	–	5.7	7.9	5.5	3.9	3.2
Core inflation index <sup>2</sup>	–	4.7	7.6	6.7	4.1	3.2
Unemployment rate <sup>3</sup> (% of labour force)	–	4.1	3.3	2.8	3.0	3.1
Current account balance (% of GDP)	–	-0.7	-1.3	-0.8	-0.7	-0.9

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 114 database.

StatLink  <https://stat.link/oikw56>

The labour market is strong, with unemployment low (2.9% in September) and broader measures of unemployment confirming the strength. Real wages have increased, supported by increases in minimum wages, beginning-of-the-year salary reviews and the slowdown in inflation. Informality is hovering around 55%, around 3 percentage points below the historical average. Labour market participation is increasing for women, although it remains significantly lower than in regional peers and other OECD countries. With the broader measure of unemployment close to 20%, there seems to be sufficient labour market resources available to respond to increases in labour market demand derived from the ongoing nearshoring of activities to Mexico.

## Monetary policy will need to remain restrictive

To respond to mounting inflationary pressures and anchor inflation expectations, the central bank has gradually increased the policy rate to 11.25%. Headline inflation has continued to soften, but with core inflation proving more persistent and inflation expectations still above target, monetary policy should remain restrictive. The policy rate is assumed to remain at its current level until the second half of 2024, when it would start to be reduced gradually. Fiscal policy continues to prioritise some social programmes, particularly non-contributory pensions, and priority infrastructure projects in the South, which are expected to get a final push towards finalisation in 2024. The budget deficit is expected to increase to 4.9% of GDP in 2024, from 3.3% of GDP in 2023, as budget allocations for social spending, particularly universal non-contributory pensions, and flagship infrastructure projects in the South significantly increase. The deficit will decrease to 2.1% in 2025. The official measure of public debt is expected to remain broadly stable around 50% of GDP.

## Growth will moderate

The economy is projected to expand by 2.5% next year and 2% in 2025. Private consumption will be a key driver, supported by low unemployment and increases in real wages. Private investment will gradually benefit from the relocation of manufacturing activity to Mexico. Exports will suffer from slower growth in major trading partners but will benefit from deep integration in manufacturing value chains and nearshoring. Annual headline and core inflation will continue to slow gradually and are expected to return to the 3% target by the third quarter of 2025. However, the inflation outlook remains very uncertain. Inflation may be more persistent than anticipated, if for example energy or commodity prices rise substantially. Episodes of global financial turmoil may trigger greater risk aversion and increase financing costs and foreign exchange market volatility. On the upside, a swifter reconfiguration of global value chains could boost investment by more than anticipated.

## Boosting productivity is a key priority

Broadening the tax base would help to respond to increasing spending needs in education, health, and infrastructure, safeguard the commitment to debt sustainability, and boost productivity and medium-term growth. Improving access to, and the quality of, early childhood education and care would support female labour force participation, foster growth prospects and reduce inequalities. Reducing the regulatory cost at the state and municipal level of formalising and growing firms, and continuing to improve labour dispute resolution mechanisms, would support stronger formal employment and productivity. Shifting to renewable energy and promoting public urban and inter-urban transport would reduce emissions and the use of fossil fuels.

# Netherlands

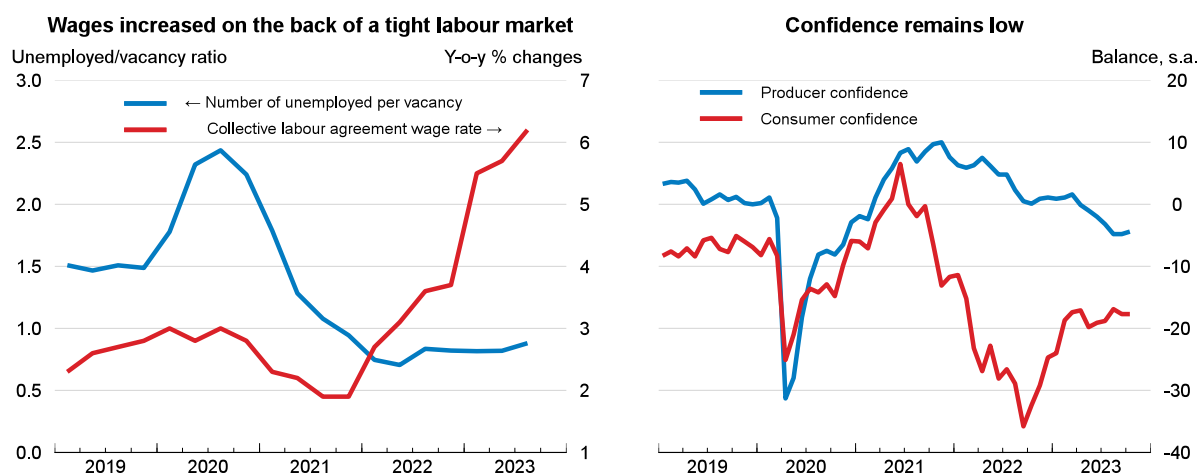
After slowing to 0.2% in 2023, GDP is projected to pick up gradually to 0.5% in 2024 and 1.1% in 2025. Headline inflation is expected to fall to 3.7% in 2024 and to be close to target by the end of 2025. As the labour market remains tight, core inflation will remain elevated at 3.9% in 2024 before gradually falling towards 2% by the end of 2025. Export growth is expected to improve in 2024 and 2025 as external demand recovers.

The fiscal stance is projected to be mildly restrictive despite a purchasing power package for low-income households and increased defence spending. In the medium term, the fiscal deficit is expected to deteriorate with rising expenditure on interest, climate policy and health care. While prudent fiscal policy is still required, the government should continue to tackle structural challenges, focusing on accelerating the green transition and reducing labour market tightness.


## The economy faces severe headwinds in 2023

The economy contracted in the first three quarters of 2023 driven by declines in the trade balance and household consumption. Headline inflation has declined steadily since April 2023, due to falling energy and food prices, with consumer prices in October 1% lower than a year earlier. However, core inflation remains elevated at 4.7% on the back of sharply rising collective labour agreement wage rates and a persistently tight labour market. Private consumption remains subdued, with stable but below long-term average consumer confidence. Business confidence has deteriorated steadily, with production in the industrial sector contracting by 9.3% over the year to September.

## Netherlands



Source: CBS; and OECD Short-Term Indicators database.

StatLink  <https://stat.link/4sohgy>

## Netherlands: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Netherlands</b>						
<b>GDP at market prices</b>	796.0	6.2	4.4	0.2	0.5	1.1
Private consumption	335.6	4.4	6.5	0.2	0.2	0.8
Government consumption	207.4	5.0	1.6	2.7	1.7	1.4
Gross fixed capital formation	173.1	2.9	1.8	2.7	-1.8	0.2
Final domestic demand	716.0	4.2	4.0	1.5	0.2	0.8
Stockbuilding <sup>1</sup>	0.3	0.4	-0.2	-0.5	0.0	0.0
Total domestic demand	716.4	4.6	3.8	0.9	0.1	0.8
Exports of goods and services	622.0	8.0	4.6	-0.9	0.6	2.3
Imports of goods and services	542.4	6.2	4.0	-0.4	0.2	2.1
Net exports <sup>1</sup>	79.6	2.0	1.0	-0.5	0.3	0.4
<i>Memorandum items</i>						
GDP deflator	–	2.9	5.6	7.3	3.3	2.7
Harmonised index of consumer prices	–	2.8	11.6	4.4	3.7	2.4
Harmonised index of core inflation <sup>2</sup>	–	1.8	4.8	6.7	3.9	2.5
Unemployment rate (% of labour force)	–	4.2	3.5	3.6	4.0	4.4
Household saving ratio, net <sup>3</sup> (% of disposable income)	–	17.0	12.7	12.7	12.7	12.6
General government financial balance (% of GDP)	–	-2.2	-0.1	-1.5	-1.9	-2.0
General government gross debt (% of GDP)	–	65.8	54.3	54.0	55.0	56.1
General government debt, Maastricht definition <sup>4</sup> (% of GDP)	–	51.7	50.1	49.8	50.8	51.9
Current account balance (% of GDP)	–	12.1	9.3	10.2	9.8	10.1

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. 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 114 database.

StatLink  <https://stat.link/d2y5mi>

As a small open economy, the Netherlands is exposed to global trade disruptions. Depressed world trade growth amidst heightened geopolitical tensions has weighed on the economy, in addition to high energy prices and increased uncertainty. The Netherlands is well integrated in the global financial system. High interest rates to tame inflation over a prolonged period could pose a risk to the domestic financial system as household debt in the Netherlands is particularly high.

### The fiscal deficit is set to deteriorate

The fiscal deficit is projected to increase gradually over the projection period from 1.5% of GDP in 2023 to 2% of GDP in 2025. The positive effect of removing the energy price cap after December 2023 will be mitigated by planned spending on infrastructure, nitrogen and climate policy and additional defence expenditure. In September, the caretaker government also announced a poverty-reducing package supporting low-income households through increased benefits and selected tax credits. The budgetary cost of these measures amounts to about 0.3% of GDP, which will be largely funded by raising the threshold for the top income tax band by less than inflation, and increased excise duties on alcohol and tobacco. The government debt ratio is likely to marginally increase from around 50% of GDP in 2023 to 52% of GDP in 2025.

## Economic growth will improve slowly

GDP is set to grow by 0.5% in 2024 and 1.1% in 2025. Headline inflation is expected to pick up at the beginning of 2024 due to upward pressure from the removal of the energy price cap, but will then gradually fall from 3.7% in 2024 to 2.4% in 2025. Wages are projected to increase by 6% in 2023, before moderating to 5% in 2024 and to 4% in 2025, as the labour market remains tight. Core inflation is therefore expected to be persistent, declining to 3.9% in 2024 and 2.5% in 2025. Subdued private consumption and investment will weigh on growth as inflation and interest rates remain high. External demand is expected to improve from 2024 as economic growth in key EU trading partners recovers. The outlook is surrounded by significant risks. Heightened geopolitical tensions could hit external demand and weigh on export growth. Increasing pressure on businesses from higher interest rates and labour costs, and greater uncertainty could significantly increase bankruptcies, although these could also support the reallocation of workers and ease labour market tightness in the medium term. Higher income households could also support growth by spending a greater share of their excess savings.

## Increasing labour supply should be a priority

The Netherlands is in a good fiscal position, but an ageing population and advancing the green transition will add budgetary pressure in the medium term. Ageing-related expenditure alone is expected to increase roughly 1.5 percentage points to about 14.5% of GDP over the next five years. The incoming government should address long-standing structural challenges, focussing on increasing labour supply to mitigate some of the pressures. While employment is high, hours worked are low, particularly for women. Government plans to expand free childcare should help to increase the labour supply of mothers. Streamlining existing income-dependent benefits into a system of fewer allowances and tax credits could further help to increase working hours, as the net benefits of an additional hour worked would be more transparent. Shifting the composition of active labour market policies towards training, especially to improve green and digital skills, could help to reduce skill mismatch and accelerate the green transition.

## New Zealand

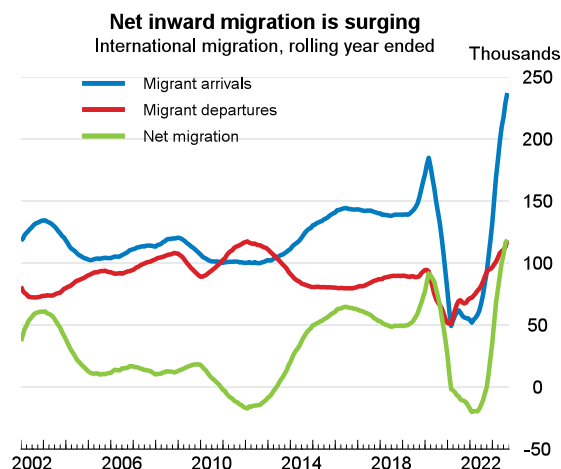
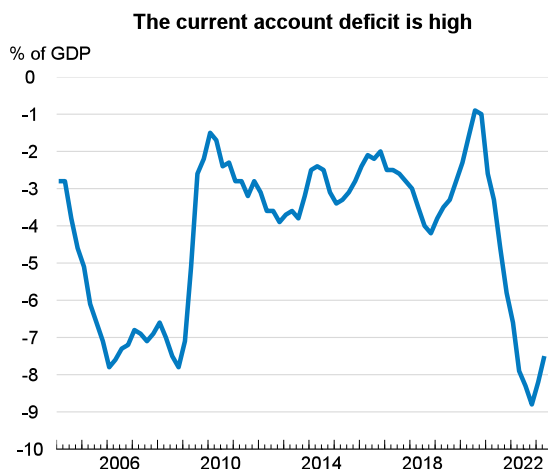
Real GDP growth is projected to ease to 1.3% in 2024 before picking up to 1.9% in 2025. Higher interest rates are weighing on consumption and housing investment, while lower global growth is restraining inbound tourism and reducing the price of commodity exports. Strong net inward migration is set to put a floor under aggregate growth. Many of the migrants are of working age, and labour force growth has been strong, easing labour market tensions. However, employment growth recently turned negative and the unemployment rate is rising.

In line with weaker growth and ebbing labour market tensions, inflation is projected to fall to 3.5% in 2024 and 2.5% in 2025 if monetary policy remains restrictive for an extended period. Sticking to a moderate fiscal consolidation path is important for reducing inflation and maintaining the credibility of fiscal policy. Reforms to boost competition, as well as labour, skills and housing supply, are essential to resolve imbalances in the economy and to sustainably raise productivity and growth.

### Strong net inward migration is moderating the slowdown in activity

The tightening of monetary policy has slowed the housing market and contributed to a decline in housing construction, which contracted from late 2022 to mid-2023. Weak demand from China for commodity exports has also pushed down prices, export values and farmers' incomes. However, the slowdown is being tempered by rapidly rising net inward migration to more than 118 000 (2.3% of the population), which is helping to support consumption. This surge is likely a temporary release of pent-up demand to migrate to New Zealand following the lifting of most COVID-19 border controls by end-July 2022, but also reflects a more permanent liberalisation of work visa schemes in late 2022. A rapid revival of international tourist arrivals, except from China, has also helped to limit the slowdown. Employment expanded through mid-2023, as employers filled a large stock of vacancies partly with migrant arrivals, but fell 0.2% in the third quarter of 2023. With activity slowing, consumer price inflation has fallen from a peak of 7.3% to 5.6% in the third quarter of 2023.

### New Zealand



Source: Statistics New Zealand.

## New Zealand: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices NZD billion	Percentage changes, volume (2009/2010 prices)				
<b>New Zealand</b>						
<b>GDP at market prices</b>	323.0	6.1	2.3	1.6	1.3	1.9
Private consumption	182.5	7.4	3.2	1.9	0.9	1.7
Government consumption	65.3	8.2	4.6	-0.3	1.0	0.0
Gross fixed capital formation	73.7	12.3	4.1	1.6	-2.4	1.8
Final domestic demand	321.5	8.7	3.7	1.4	0.1	1.4
Stockbuilding <sup>1</sup>	- 1.9	1.4	-0.3	-2.1	-0.3	0.0
Total domestic demand	319.6	10.1	3.4	-0.6	-0.2	1.4
Exports of goods and services	77.5	-2.7	-0.2	9.4	4.1	2.8
Imports of goods and services	74.1	14.8	4.7	0.6	-1.2	1.6
Net exports <sup>1</sup>	3.3	-4.0	-1.2	2.1	1.3	0.3
<i>Memorandum items</i>						
GDP deflator	–	3.0	5.5	5.8	3.4	2.2
Consumer price index	–	3.9	7.2	5.8	3.5	2.5
Core inflation index <sup>2</sup>	–	3.7	6.0	5.8	3.6	2.5
Unemployment rate (% of labour force)	–	3.8	3.3	3.8	4.9	4.7
Household saving ratio, net (% of disposable income)	–	8.7	1.1	-2.4	-3.0	-3.4
General government financial balance (% of GDP)	–	-6.0	-2.8	-2.9	-3.2	-2.9
General government gross debt (% of GDP)	–	48.5	53.0	54.9	57.5	59.7
Current account balance (% of GDP)	–	-5.7	-8.5	-6.7	-5.6	-5.4

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 114 database.

StatLink  <https://stat.link/bq6w4p>

## Monetary policy has been tightened before fiscal policy

The Reserve Bank will need to maintain tight monetary policy throughout 2024, especially as core inflation is sticky, fiscal consolidation is very gradual and high population growth due to net inward migration will likely re-ignite pressures in the housing market, slowing the decline in inflation. The official cash rate is projected to remain constant at 5.5% until the end of 2024 and then to be cut gradually to 4.25% by the end of 2025 as inflation approaches the middle of the Reserve Bank's 1-3% target range.

A technical assumption is that fiscal policy follows the expenditure path set out in the September 2023 pre-election update of the previous government. Between 2023 and 2025 the headline deficit is projected to remain constant at around 3% of GDP. However, as economic slack will widen, the implied fiscal stance is mildly contractionary, with the underlying primary balance increasing by around ½ percentage point of GDP per annum between 2023 and 2025.

## Modest economic growth is projected

Economic growth is projected to be 1.3% in 2024 but to pick up to 1.9% in 2025 as disinflation helps to restore modest real household income and consumption growth. A growing shortage of housing and rising house prices is expected to stimulate housing construction, while higher growth in China and other key trading partners will help to boost exports. Inflation is projected to continue easing gradually in line with the end of supply chain tensions, weaker demand, higher unemployment, and more modest nominal wage increases. Risks around this projection are balanced. El Niño conditions have developed in the Pacific Ocean, with a risk of a strong drought in the coming New Zealand summer that would negatively affect agricultural and

horticultural production and exports. On the upside, stronger tourism growth could spark a more vigorous export-led recovery.

### **A more coordinated policy approach is needed to restore macroeconomic stability**

Despite narrowing, New Zealand's current account deficit still reached an unsustainable 7.5% of GDP in the year to June 2023. Together with high inflation, this indicates that strong excess demand has built up. Up until late 2023, too much weight has been put on monetary policy to reduce inflation, requiring higher interest rates and a stronger exchange rate than otherwise, thereby slowing export growth and the rebalancing of the economy. The fiscal deficit is contributing to this imbalance. Fiscal consolidation has suffered from negative surprises, including increased cost pressures, the bill for storm and cyclone damage, and spending slippages. The previous government twice delayed reaching its target of a return to surplus by one year, despite an expected rise of nearly 3% of GDP in ageing-related health and pension expenditure by 2040. In addition, the disinflationary benefits of easing labour market shortages are being reduced by the housing market pressures created by a heavy reliance on migrants to fill vacancies. Fiscal and structural policies need to contribute to lowering inflation and reducing imbalances by encouraging an increase in domestic labour and housing supply, rather than adding to demand via tax cuts or other non-targeted subsidies.



# Norway

Economic growth has slowed amid high inflation and monetary policy tightening. Mainland GDP growth is projected to slow to 1.1% in 2023 and 0.5% in 2024, before picking up to 1.3% in 2025 as domestic demand strengthens. Headline inflation has been declining on the back of lower electricity prices and is set to ease further. Underlying inflation will drift down more slowly, held up by wage pressures and the lagged effects of the weakening of the Norwegian currency. The unemployment rate is expected to rise as economic activity softens, but to remain around its pre-pandemic level.

Monetary policy needs to remain tight for some time to contain inflation and ensure that inflation expectations are anchored. The fiscal stance should not add to inflationary pressures while ensuring well-targeted support to vulnerable groups. Making room for new spending is essential in view of pressures, notably from population ageing. Structural reforms that reduce incentives for early retirement, boost productivity and promote the green transition are key to inclusive and sustainable growth.


## Economic activity has slowed

Mainland GDP growth has slowed during 2023 as high inflation and interest rate increases continued to weigh on domestic demand. Private consumption has weakened due to the rising cost of living, even though subsidies for households' electricity bills and a decline in accumulated savings during the pandemic have provided support. Reduced car purchases, following the surge that preceded the reduction in tax incentives, have also curbed consumption. Housing investment has fallen markedly due to high construction costs and lower house price growth. Business investment growth has also slowed. After falling for four consecutive months, headline inflation increased to 4% in October 2023, as electricity prices edged up. Underlying inflation has also eased but remains elevated. A tight labour market is fuelling wage growth, with ongoing wage negotiations pointing to wage growth of around 5½ per cent in 2023.

## Norway



1. Core inflation is Statistics Norway's CPI-ATE measure which adjusts for tax changes and excludes energy products.
  2. Percentage share of regional network contact businesses responding that labour shortages are curtailing production/sales.
  3. Long-term average of reported labour shortages between Q1 2000 and Q3 2023.
- Source: Statistics Norway; and Norges Bank.

StatLink  <https://stat.link/xz0yqk>

## Norway: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices NOK billion	Percentage changes, volume (2021 prices)				
<b>Norway</b>						
<b>Mainland GDP at market prices<sup>1</sup></b>	3 067.3	4.2	3.8	1.1	0.5	1.3
<b>Total GDP at market prices</b>	3 461.6	3.9	3.3	1.3	0.7	1.5
Private consumption	1 504.0	4.4	6.9	-0.9	0.6	1.2
Government consumption	904.6	5.0	0.1	2.1	1.5	1.5
Gross fixed capital formation	949.7	-0.8	4.3	-0.4	-0.9	1.3
Final domestic demand	3 358.3	3.1	4.3	0.0	0.4	1.3
Stockbuilding <sup>2</sup>	135.5	-0.4	0.1	0.5	-0.1	0.0
Total domestic demand	3 493.9	2.6	4.4	0.7	0.3	1.3
Exports of goods and services	1 115.0	5.8	5.9	5.1	3.2	3.5
Imports of goods and services	1 147.3	1.7	9.2	4.1	3.4	3.9
Net exports <sup>2</sup>	- 32.3	1.3	-0.2	1.7	0.5	0.4
<i>Memorandum items</i>						
GDP deflator	–	17.1	28.1	-9.8	2.4	2.7
Consumer price index	–	3.5	5.8	5.5	3.9	3.2
Core inflation index <sup>3</sup>	–	1.7	3.6	5.9	4.5	3.2
Unemployment rate (% of labour force)	–	4.4	3.2	3.6	3.8	3.8
Household saving ratio, net (% of disposable income)	–	12.7	3.6	1.2	0.3	0.6
General government financial balance (% of GDP)	–	10.6	26.0	14.9	16.6	16.6
General government gross debt (% of GDP)	–	49.2	43.3	..	..	..
Current account balance (% of GDP)	–	13.6	30.4	17.0	18.3	18.2


Note: The numbers do not reflect the 23 November national accounts revisions nor the first estimates for the outcome of 2023Q3.

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 114 database.

StatLink  <https://stat.link/rlui7d>

Lower global energy prices are expected to weaken Norway's terms of trade and related revenues. However, Norwegian exports should continue to benefit from strong energy demand from trading partners to replace mostly Russian gas supply, as well as buoyant energy services exports driven by higher investment in global energy production. Oil and gas investment is expected to increase in view of the number of submitted projects by the end of 2022, halting the decline in the past few years. Thus far Norway has admitted 68 000 Ukrainian refugees and it expects to admit another 37 000 refugees in 2024.

## Containing inflation remains key

The 2024 draft budget increases petroleum revenue spending (transfers from the oil fund to the budget) by 0.4% of mainland trend GDP but its impact on economic activity is broadly neutral according to the government. Support for Ukraine via the Nansen Programme, for instance, accounting for 0.4% of mainland GDP, has a limited effect on domestic demand. The budget extends the electricity support scheme until end-2024 at an expected cost of around 0.2% of mainland GDP. Monetary policy has continued to be tightened, with the policy rate increasing to 4.25% by September 2023. Monetary policy needs to remain tight for some time. While easing, inflation remains well above the target and the Norwegian currency has substantially weakened, pointing to continued inflation pressures. The OECD projections assume that the policy rate will peak at 4.5% in the fourth quarter of 2023 and remain at this level until early 2025, gradually falling to 4% by the end of that year.

## Economic activity will slowly recover

Mainland GDP growth is expected to slow to 1.1% in 2023 and 0.5% in 2024, before edging up to 1.3% in 2025 as domestic activity strengthens gradually due to lower inflation and monetary easing. Headline inflation is projected to decline to around 3% by the end of 2025, helped by lower energy prices and the slowdown in demand. Investment will benefit from an improvement in the external environment and the implementation of climate-related projects. Lower financing costs and potential housing shortages could progressively stimulate housing investment, following a sharp decline in 2023. A still tight labour market, despite some rise in unemployment, will keep wage growth strong. Improved profitability in the manufacturing sector, the front-runner in wage settlements, also points to high wage growth. The outlook is surrounded by uncertainties. Wage growth could be stronger than expected, fuelling inflation. Sluggishness in the housing market could become more pronounced than projected, potentially leading to a sharper fall in housing investment. Higher borrowing costs could intensify risks related to high household indebtedness due to the high share of variable-rate loans. On the upside, households could spend more of the excess savings accumulated during the pandemic, spurring consumption, while faster than foreseen labour market integration of Ukrainian refugees could help ease labour market pressures.

## Ensuring strong and inclusive growth

Making fiscal room is essential to address spending pressures, particularly from population ageing, and to ensure sustainable and inclusive growth. OECD estimates suggest that health and long-term care expenditure will increase by 1.2 percentage points of GDP between 2024 and 2040, with a similar rise in pension expenditure over the same period. More cost-effective implementation of large transport infrastructure projects, which account for a substantial share of public investment, along with a broadening of the ex-post assessment of such projects would create scope for new spending initiatives. Reforms to boost labour force participation by reducing incentives to enter disability pension and sickness benefit schemes, and efforts to enhance innovation and the adoption of new technologies, including by increasing the number of students with ICT skills, are also important. Advancing the green transition is crucial for sustainable growth. Support for green technology initiatives, including carbon-capture and storage projects, needs to continue.

# Peru

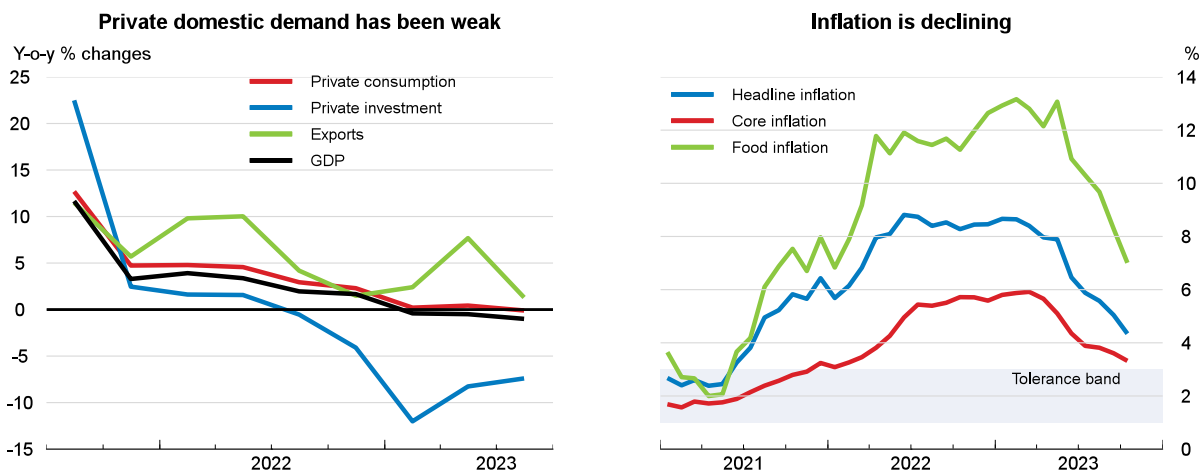
GDP growth is projected to decline to 0% this year, and to gradually pick up to 2.3% in 2024 and 2.7% in 2025. High interest rates and inflation, political uncertainty and severe weather are constraining domestic demand. Government efforts to revamp infrastructure will support investment, despite high interest rates and implementation challenges. Tourism and copper production are set to rebound, enhancing exports. Inflation is expected to continue to slow and reach the 1-3% target range by early 2024, supporting private consumption.

There is room for further gradual monetary easing, as inflation and inflation expectations are falling towards the target. The planned gradual reduction of the fiscal deficit over the next years should be implemented in adherence with fiscal rules to maintain low public debt and rebuild fiscal buffers. A fiscal reform to increase public revenues and spending efficiency is needed to address pressing infrastructure and social needs. A comprehensive strategy to fight widespread informality, including lower non-wage labour costs and better skills, would boost productivity and equity.

## El Niño is weighing on economic activity

After a first quarter disrupted by social unrest, economic activity declined further in the second and third quarters of 2023 due to the El Niño adverse impact on fisheries, agriculture and related industries. GDP declined by 0.6% between January and September, with respect to the same period last year. Mining has sustained growth, bouncing back as social unrest subsided and a new copper mine began its operations, supporting exports and reducing the current account deficit. However, this has not offset weakness in private consumption and investment. Business confidence has improved slightly but is still very weak. A significant increase in central government public investment has helped to mitigate the economic slowdown, despite the decline in subnational government investment.

## Peru



Source: INEI (Instituto Nacional de Estadística e Informática); and Central Reserve Bank of Peru.

StatLink  <https://stat.link/tk6b23>


## Peru: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices PEN billion	Percentage changes, volume (2007 prices)				
<b>Peru</b>						
<b>GDP at market prices</b>	705.7	13.3	2.7	0.0	2.3	2.7
Private consumption	452.3	12.3	3.5	0.6	1.9	2.9
Government consumption	112.4	5.2	-0.9	3.2	2.4	1.0
Gross fixed capital formation	139.2	34.0	0.7	-5.2	1.8	2.4
Final domestic demand	704.0	15.3	2.3	-0.4	1.9	2.5
Stockbuilding <sup>1</sup>	- 9.0	-0.6	0.0	-4.1	-0.5	0.0
Total domestic demand	695.0	15.2	2.3	-4.4	1.5	2.7
Exports of goods and services	159.8	19.1	6.0	13.1	5.4	3.2
Imports of goods and services	149.0	26.2	4.2	-2.8	2.8	2.9
Net exports <sup>1</sup>	10.8	-2.0	0.4	4.4	0.9	0.2
<i>Memorandum items</i>						
GDP deflator	–	8.5	4.5	6.5	3.2	2.4
Consumer price index	–	4.0	7.9	6.4	2.7	2.2
Core inflation index <sup>2</sup>	–	2.2	4.7	4.4	2.5	2.2
Unemployment rate (% of labour force)	–	5.9	4.4	5.0	4.8	4.3
Current account balance (% of GDP)	–	-2.3	-4.1	-0.7	-0.7	-0.5

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 114 database.

StatLink  <https://stat.link/yvqpa5>

Headline inflation has declined but is still above the target range. Core inflation has also dropped, with both goods and services prices edging down. While energy inflation has decreased sharply, food inflation has declined at a more gradual pace, because of still high fertiliser prices and extreme weather conditions. Wage increases have been contained, and real wages are 7% below their 2019 level. The central bank started the normalisation cycle in September cutting the policy rate in three consecutive meetings by a total of 75 basis points in face of declining inflation expectations and a weak economy. Risks associated with volatile global financial conditions are mitigated by large currency reserves and low public debt.

## The planned fiscal restraint should be implemented

The fiscal deficit is on track to hit the limit foreseen in the fiscal rule, implying a moderate fiscal impulse this year. This reflects efforts to stimulate the economy against the backdrop of social unrest and severe weather. Exceptional support to mitigate the climate emergency is limited to 2023 and 2024. However, unexpected revenue shortfalls due to the economic slowdown, coupled with higher-than-expected climate emergency expenditures could challenge adherence to fiscal rules. Following the strategy of implementing a tighter fiscal policy and gradually reducing the fiscal deficit over the next three years is essential to maintain public debt at a sustainable level and rebuild fiscal buffers. These plans should stabilise public debt-to-GDP ratio slightly below the debt rule of 30% of GDP. As inflation expectations return to the target and severe weather dissipates, monetary authorities are expected to continue reducing the policy rate, bringing the monetary policy stance to neutral by 2025 with policy rates declining to 4%. The central bank is expected to remain cautious due to upward inflation risks associated with the El Niño weather phenomenon.

## **GDP growth will rebound once severe weather subsides**

Growth is expected to pick up as climate-related headwinds dissipate from the second quarter of 2024. Inflation is expected to reach the target range by the second quarter of 2024, once the impact on food prices of severe weather subsides, and core inflation will enter the target range in the first quarter of 2024. Lower inflation, the easing of financial conditions and improving business and consumer confidence will support domestic demand. Investment will be upheld by government measures included in the Unidos programme to boost public infrastructure, private investment and public-private partnerships, while exports will benefit from the better performance of mining and tourism. Still, domestic and external risks are unusually high. A slower than anticipated recovery in China, which is Peru's main trading partner, and lower copper prices would have a detrimental effect on exports, fiscal revenues, and prospects for investment. The unpredictable nature of El Niño poses risks, with potential economic setbacks and inflation spikes. Higher global oil prices could also add inflationary pressures. Political uncertainty and renewed flare-ups in social unrest also remain key risks.

## **Greater spending efficiency and tax revenues are needed**

Better spending efficiency and higher tax revenues will be needed to maintain fiscal sustainability and create the necessary fiscal space to address increasing social needs and expand critical infrastructure. Greater spending efficiency will require enhancing the capacities of local governments to implement investment projects and clearly defining the spending responsibilities of national and subnational governments, while gradually granting regions more tax powers and improving the tax collection capacity of local governments. Higher tax revenues can be achieved by strengthening tax administration, reducing tax expenditures, completing and updating the cadastre, and simplifying corporate tax schemes. A comprehensive strategy to foster formalisation, including lower non-wage labour costs, more flexible employment regulation, better skill-upgrading opportunities and stronger tax and labour law enforcement would promote poverty alleviation, narrow inequality, and boost productivity and tax revenues. A pension reform is necessary to improve the extremely low coverage of the system.

# Poland

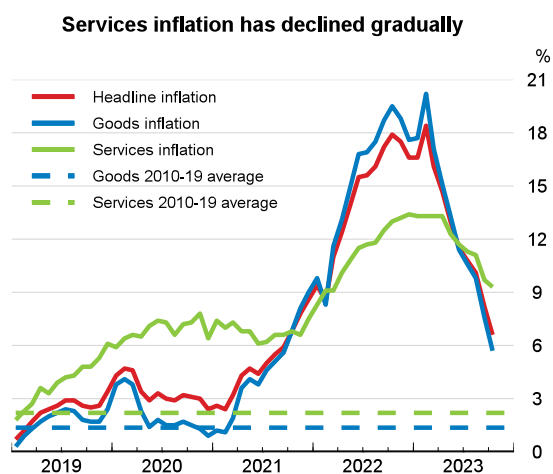
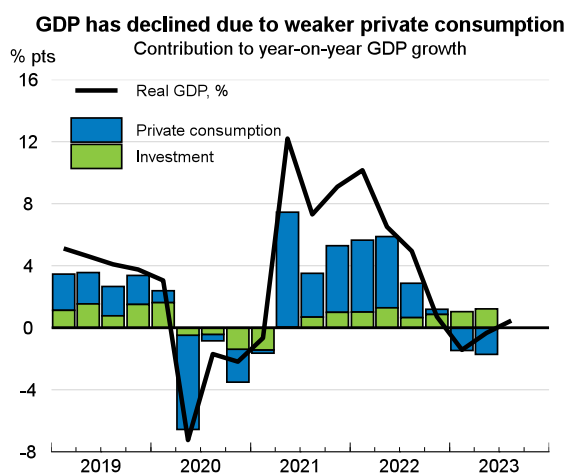
Real GDP is expected to grow by 0.4% in 2023 as high inflation and restrictive monetary policy weaken domestic demand. Growth should recover to 2.6% in 2024 and pick up to 2.9% in 2025 as consumption rebounds and is accompanied by robust investment, supported by EU Recovery and Resilience funds. Headline inflation has halved over 2023 but core inflation is declining more slowly due to a robust labour market. Inflation is projected to reach 3.4% by the end of 2025. Persistent inflation or additional fiscal spending pose upside risks to inflation, while an escalation of the war in Ukraine could lower growth.

Monetary policy should ease only gradually given the risk of inflation persistence and the uncertainty in the outlook. Fiscal consolidation is needed to help reduce inflation and put the public finances on a more prudent path, despite significant spending pressures. In the medium-term, accelerated decarbonisation and digitalisation, supported by policies to improve skills, would raise energy security and lead to greener and stronger economic growth.


## The domestic economy has been subdued in 2023

The economy has remained subdued throughout most of 2023. Private consumption growth has been low as the cost of credit remained high. Despite declines in mortgages and housing construction, total investment growth has remained robust. Since the summer, retail sales have continued to increase. Consumer confidence rose above its long-run average in October. However, the PMI and other business confidence surveys suggest further weakness in manufacturing. The labour market remains resilient, as unemployment held at 2.8% in September, although wage growth has eased. Having peaked in February this year, headline inflation fell to 6.6% in October due to slowing food and energy price growth. Core inflation has declined but remains high at 8.1%.

## Poland



Source: OECD Economic Outlook 114 database; and Statistics Poland.

StatLink  <https://stat.link/mus5jt>

## Poland: Demand, output and prices


	2020	2021	2022	2023	2024	2025
	Current prices PLN billion	Percentage changes, volume (2015 prices)				
<b>Poland</b>						
<b>GDP at market prices</b>	2 335.5	6.8	5.6	0.4	2.6	2.9
Private consumption	1 321.6	6.2	5.2	-1.4	2.6	3.1
Government consumption	442.5	5.0	0.8	4.6	3.3	3.9
Gross fixed capital formation	434.9	0.3	5.6	6.8	1.9	3.3
Final domestic demand	2 199.1	4.8	4.4	1.3	2.6	3.3
Stockbuilding <sup>1</sup>	2.6	3.1	1.6	-4.0	-0.4	0.0
Total domestic demand	2 201.7	8.6	5.9	-2.8	2.2	3.3
Exports of goods and services	1 239.3	12.3	6.8	-2.0	1.1	3.3
Imports of goods and services	1 105.5	16.1	6.9	-5.3	2.2	4.1
Net exports <sup>1</sup>	133.8	-1.1	0.2	2.0	-0.5	-0.2
<i>Memorandum items</i>						
GDP deflator	–	5.4	10.3	10.7	2.4	3.2
Consumer price index	–	5.1	14.4	11.8	4.7	3.7
Core inflation index <sup>2</sup>	–	4.1	9.0	10.1	4.9	3.7
Unemployment rate (% of labour force)	–	3.3	2.9	2.9	3.3	3.5
Household saving ratio, net (% of disposable income)	–	2.0	-2.9	1.7	2.6	1.1
General government financial balance (% of GDP)	–	-1.8	-3.7	-5.2	-4.3	-4.4
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	53.6	49.4	51.4	54.1	56.4
Current account balance (% of GDP)	–	-1.3	-2.4	0.3	-1.3	-1.3

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 114 database.

StatLink  <https://stat.link/ozfaj8>

Exports fell in the first half of 2023 as deteriorating growth in the euro area led to weaker demand. But imports declined by more, as commodity prices decreased and as firms continued to draw down their inventories, leading to an improvement in the current account balance. Reductions in inventories and easing supply chain disruptions contributed to a sharp decline in goods inflation. Services inflation, partly supported by elevated wage growth, has declined more gradually. The significant number of Ukrainian refugees in the labour market, however, will continue to moderate wage growth.

## Monetary policy has eased while fiscal support continued

The National Bank of Poland has started easing monetary policy despite relatively high inflation, reducing interest rates to 5.75% in October, one percentage point below their peak. Fiscal support has continued, with the government's budget deficit over 5% of GDP this year. Energy price caps, subsidies to energy-intensive companies, and the zero VAT rate on food have been maintained in 2023. Healthcare spending has been gradually increasing. Military expenditure is rising to around 4% of GDP this year, up from 2.2% in 2022. The withdrawal of energy and food support measures in 2024 should lead to fiscal tightening, but the eventual fiscal stance will depend on the newly elected government's budget plans.



## The economy will recover gradually, but inflation will decline slowly

The economic recovery will be gradual. Receding inflation and falling uncertainty accompanied by decreasing interest rates should support consumption growth even as the labour market softens. Investment growth should remain robust, underpinned by improving growth prospects and EU Recovery and Resilience funds. After slowing to 0.4% this year, real GDP growth is projected recover to 2.6% in 2024 and 2.9% in 2025. Public debt should rise to 56.4% of GDP over the next two years. Inflation is expected to be 4.7% over 2024 and reach 3.4% by the end of 2025, just under the upper limit of the central bank's target band. Still, the outlook remains uncertain. Persistent inflation or additional fiscal spending could pose upside risks to inflation, warranting tighter monetary policy. An escalation of the war in Ukraine could increase uncertainty and lower growth.

## Fiscal consolidation is needed alongside reforms to boost growth

Given a relatively tight labour market and the risk of persistent inflation, the pace of monetary policy easing should be gradual until inflation durably returns to target. Fiscal consolidation is needed from 2024 onwards to help reduce inflation and put the public finances on a more sustainable path. The new government should develop a credible medium-term fiscal strategy and establish an independent fiscal council. This should address rising healthcare and pension costs due to population ageing, which could amount to 3% of GDP by 2040. Further diversification of energy imports and increased investment in renewables would improve energy security and contribute to greener growth. Skills shortages need to be addressed to reap the full benefits of the digital and green transitions. Managerial skills, key to advancing digitalisation, should be boosted through flexible and modular training. Older adults, the unemployed and the low-skilled require upgrading of weak basic and digital skills and access to lifelong training. Integration of refugees, mostly comprising women with children, should continue through childcare, schooling and language training.

# Portugal

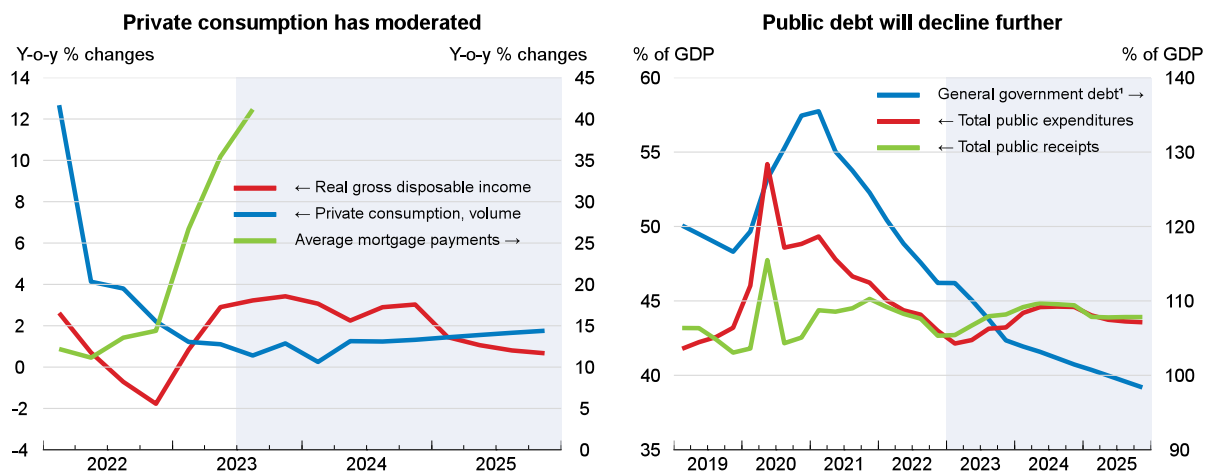
GDP growth is projected to be 2.2% in 2023, 1.2% in 2024 and 2.0% in 2025. Low business and household confidence, modest global growth and high uncertainty are holding back activity, although the tight labour market will support wage growth and private consumption, and the implementation of the Recovery and Resilience Plan (RRP) will boost investment. A progressive strengthening of external demand will support exports in 2024-25. As energy and food prices stabilise and labour demand slows, inflation will fall to 3.3% in 2024 and 2.4% in 2025.

Fiscal policy will ease. The phasing out of support measures to smooth the inflationary shock is projected to be compensated by the implementation of the RRP and household tax cuts in 2024. Timely implementation of the RRP will strengthen green infrastructure, skills acquisition and healthcare capacity. Public debt will decline further and fall below 100% of GDP in 2025. More efficient public spending and a strengthened fiscal framework will help to address mounting spending pressures from an ageing population and strong investment needs.

## Growth has declined

The effects of inflation, tighter financial conditions and weak growth in Portugal's main trading partners have curbed economic activity, although fiscal measures are providing some offset. GDP broadly stagnated over the second and third quarters of 2023. The strong recovery in the tourism sector and increasing RRP spending have supported activity. Yet, industrial production has slowed, and goods exports have declined. Consumer price inflation, which eased to 3.2% in the year to October, and rising debt servicing costs are reducing household consumption and investment. Despite historically high employment rates and wage growth, household and business confidence declined between August and October.

## Portugal



1. Maastricht definition.

Source: OECD Economic Outlook 114 database; and Statistics Portugal (INE).

StatLink  <https://stat.link/fnqs79>

## Portugal: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2016 prices)				
<b>Portugal</b>						
<b>GDP at market prices</b>	200.5	5.7	6.8	2.2	1.2	2.0
Private consumption	128.4	4.7	5.6	1.0	1.0	1.6
Government consumption	38.0	4.5	1.4	1.1	1.8	1.4
Gross fixed capital formation	38.5	8.1	3.0	0.6	2.9	4.5
Final domestic demand	205.0	5.3	4.3	0.9	1.5	2.1
Stockbuilding <sup>1</sup>	- 0.2	0.6	0.1	-0.3	0.1	0.0
Total domestic demand	204.8	5.9	4.4	0.7	1.6	2.1
Exports of goods and services	74.3	12.3	17.4	5.3	2.3	3.6
Imports of goods and services	78.6	12.2	11.1	2.2	3.2	3.8
Net exports <sup>1</sup>	- 4.3	-0.2	2.3	1.5	-0.4	-0.1
<i>Memorandum items</i>						
GDP deflator	–	1.9	5.0	7.0	3.2	2.4
Harmonised index of consumer prices	–	0.9	8.1	5.5	3.3	2.4
Harmonised index of core inflation <sup>2</sup>	–	0.2	5.0	5.7	3.2	2.3
Unemployment rate (% of labour force)	–	6.7	6.1	6.5	6.3	6.3
Household saving ratio, net (% of disposable income)	–	0.4	-4.8	-3.1	-1.3	-1.9
General government financial balance <sup>3</sup> (% of GDP)	–	-2.9	-0.3	0.8	0.2	0.2
General government gross debt (% of GDP)	–	142.9	115.1	107.4	104.2	101.1
General government debt, Maastricht definition <sup>4</sup> (% of GDP)	–	124.5	112.4	104.7	101.5	98.4
Current account balance (% of GDP)	–	-0.8	-1.1	1.6	1.3	1.2

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. 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 114 database.

StatLink  <https://stat.link/a4xfjq>

Merchandise exports declined by 8.2% in the year to September, and expected export orders have deteriorated further in the manufacturing sector. Increasing interest rates are rapidly raising mortgage payments, with around 90% of mortgages subject to variable interest rates. This is holding back consumption and investment. Energy and food prices remain high, although energy prices have declined and the risk of energy supply shortages appears contained, with around 60% of electricity generated from renewable sources in 2022, and elevated gas storage levels.

## Public investment and tax cuts will support economic activity

Fiscal policy is set to ease in 2024-25, with the budget balance projected to decline from 0.8% of GDP in 2023 to 0.2% in 2024 and 2025. Spending from RRP grants is expected to increase from 0.8% of GDP in 2023 to 1.9% in 2024 and 1.1% in 2025, boosting public consumption and investment. By contrast, most measures to help cushion the inflation shock will be phased out in 2024. These include the temporary cuts in energy taxes and VAT, the freeze of the carbon tax, as well as electricity, gas and fuel price subsidies. However, activity will be supported by further increases in public wages and the indexation of pension benefits, new targeted social transfers, the reduction in the personal income tax, prolonged mortgage subsidies, and new business tax incentives to raise investment. The minimum wage will also increase by 7.9% in 2024, with a further 4.3% rise expected in 2025, raising household income. However, the rise in

labour costs could hold back low-wage employment and the foreseen large public investments and permanent personal income tax cuts could add to inflationary pressures in 2024.

### **Growth will progressively strengthen**

GDP growth is projected to be 2.2% in 2023, 1.2% in 2024 and 2.0% in 2025. The spending of European funds is significantly boosting public investment, and the projected recovery in activity across trading partners will support exports. High uncertainty and interest rates will continue to weigh on activity. Despite strong wage developments, consumption growth will remain moderate as employment growth eases and consumer prices and debt-servicing costs remain elevated. Tax cuts and increasing social transfers and public wages will provide some support to household incomes, but also slow the decline in inflation. Headline consumer price inflation will moderate from 5.5% in 2023 to 3.3% in 2024 and 2.4% in 2025 as energy and food prices stabilise and services price pressures diminish. The phasing out of energy and inflation support and high nominal GDP growth will help maintain budgetary surpluses and lower public debt to around 98% of GDP in 2025 (Maastricht definition). Higher-than-expected employment or wage growth would support consumption but also fuel inflation. By contrast, RRP spending could be implemented more slowly than projected, implying both lower growth and lower inflation.

### **Policies to support stronger and more sustainable growth**

Despite a steady decline, public debt relative to GDP remains high. Strong growth, more efficient spending and a strengthened fiscal framework are needed to face mounting fiscal pressures from population ageing and investment needs: the 2021 Ageing Report projects public health, long-term care and pension expenditures to rise by 3% of GDP by 2040. Temporary fiscal support to cushion the inflation shock should be phased out, as planned. Continuing to roll out new accounting standards, develop performance budgeting and reduce tax expenditures would improve the structure and efficiency of public expenditures. Gradually strengthening carbon pricing and aligning prices across sectors and fuels while protecting vulnerable groups will help reach ambitious climate goals. Measures and investments under the RRP have a strong potential to support growth through more effective public sector management, green infrastructure and further skill acquisition. Ensuring the complete implementation of the RRP, strengthening guidance on educational and training programmes for students and workers, and lowering entry barriers in services and retail sectors will maximise the benefits.

# Romania

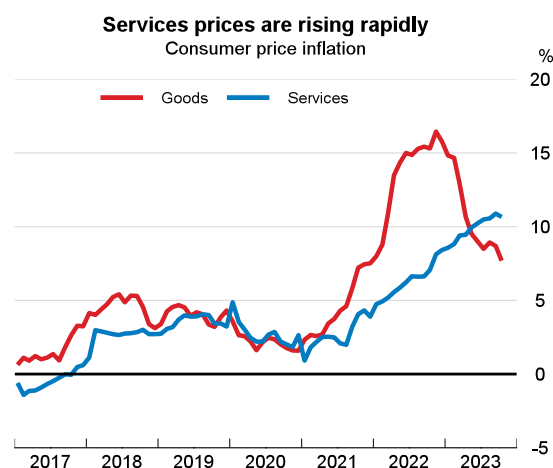
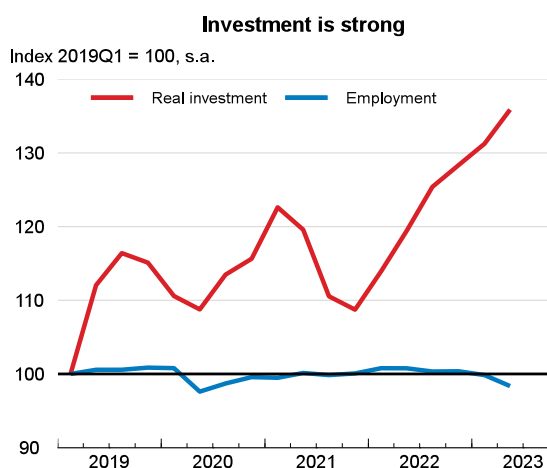
Real GDP growth will decline to 1.9% in 2023, remain below potential at 3% in 2024, and pick up to 3.3% in 2025. High borrowing costs and slower income growth will weigh on private spending. Reduced job creation will see unemployment remain above pre-pandemic rates. Major infrastructure spending will support activity while exports recover due to better international conditions. With spare capacity in the economy, inflation will fall to 3.5% by the end of 2025, the top of the target band. Sustained cost pressure could, however, cause core inflation to stay higher for longer.

Monetary policy must remain tight in 2024 to cool demand and tame high inflation. Higher taxes and spending restraint will reduce the fiscal deficit. However, revenue shortfalls will remain large, requiring comprehensive tax reform to stabilise public debt. To improve the business environment, efforts to strengthen institutions must be matched by policy stability. Carbon pricing can complement building retrofits to reduce emissions while limiting distortions to activity.

## Private demand is cooling, inflation remains high

Economic conditions have weakened. Preliminary estimates suggest growth in real GDP slowed to 0.4% in the third quarter of 2023, down from 1.3% in the second quarter. Manufacturing and farm production are subdued, but infrastructure construction is supporting activity. Consumer spending is flagging. Housing market activity remains soft while retail trade volumes decreased in the year to September. Reduced credit growth is consistent with weakening private investment intentions. Hiring has also slowed. Unemployment is above pre-pandemic levels, at 5.4% in September, but wage pressures are elevated. Lower energy prices helped reduce headline inflation to 8.1% in October, but rising services prices have lifted core inflation.

## Romania



Source: OECD Economic Outlook 114 database; and Eurostat.

StatLink  <https://stat.link/dzftv0>

## Romania: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices RON billion	Percentage changes, volume (2010 prices)				
<b>Romania</b>						
<b>GDP at market prices</b>	1 066.8	5.7	4.6	1.9	3.0	3.3
Private consumption	651.9	7.2	6.9	3.5	2.9	3.0
Government consumption	199.1	1.8	3.1	0.6	0.2	1.7
Gross fixed capital formation	251.0	2.9	5.6	10.8	4.7	4.7
Final domestic demand	1 102.0	5.1	6.0	4.7	2.9	3.2
Stockbuilding <sup>1</sup>	10.7	1.8	-0.8	-4.0	0.3	0.0
Total domestic demand	1 112.7	6.8	5.1	1.1	3.3	3.3
Exports of goods and services	393.4	12.6	9.6	0.1	2.8	3.2
Imports of goods and services	439.3	14.8	9.9	-1.6	3.5	3.2
Net exports <sup>1</sup>	- 45.9	-1.5	-0.7	0.9	-0.4	-0.1
<i>Memorandum items</i>						
GDP deflator	–	5.4	13.4	12.3	5.4	4.2
Consumer price index	–	5.0	13.8	10.4	5.0	3.7
Core consumer price index <sup>2</sup>	–	4.5	10.1	12.5	5.4	3.7
Unemployment rate (% of labour force)	–	5.6	5.6	5.7	5.7	5.6
General government financial balance (% of GDP)	–	-7.2	-6.3	-6.2	-5.4	-5.0
General government gross debt (% of GDP)	–	57.6	51.7	54.4	57.4	60.1
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	48.5	47.2	49.9	53.0	55.6
Current account balance (% of GDP)	–	-7.2	-9.1	-5.8	-5.7	-5.2

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 114 database.

StatLink  <https://stat.link/4z2et1>

Trade has slowed with subdued conditions in European markets. Export values declined in the past year, but imports fell further on lower oil and gas prices. The current account deficit has decreased but remains wide. Banking indicators appear healthy. Lower foreign interest rates and exchange rate stability have encouraged firms to take on more euro-denominated debt in 2023, a development the authorities are monitoring. Romania remains exposed to heightened geopolitical tension in the region.

### Fiscal consolidation is expected to continue

The National Bank of Romania has kept its policy interest rate at 7% since January. With price pressures still strong, monetary policy must remain tight in 2024. Extra capacity in the economy will permit policy easing from mid-2025. The projections assume a 75 basis-point reduction in the policy rate by the end of 2025. Fiscal consolidation has so far undershot government targets, but fiscal policy will tighten in 2024 and 2025. Lower energy prices are expected to reduce outlays on price capping schemes in place until 2025. But increased defence commitments and pension reforms may complicate efforts to contain spending. Higher taxes, and limits on the public payroll, will pull the budget deficit to 5.4% in 2024, helping to cool demand. However, revenue shortfalls will remain wide, increasing the public debt at a time of high borrowing costs.

## Slower growth will ease capacity constraints

GDP growth will strengthen from 1.9% in 2023 to 3% in 2024. Stock drawdowns have weighed on growth this year, but are not expected to be repeated next year. High borrowing costs and increased taxes will keep private demand subdued in 2024. Slow production will reduce hiring. Wage growth will diminish with unemployment at rates above those seen before the pandemic. In 2025, economic growth will pick up to 3.3%. EU-funded infrastructure projects will continue to generate economic activity as trade recovers with stronger foreign demand. Price growth will moderate as domestic capacity constraints ease. By the end of 2025, headline inflation will slow to 3.5%, the top of the target band. Risks to the outlook are elevated. High inflation could prove hard to tame, requiring larger macroeconomic policy corrections. An economic downturn could result in higher unemployment. There are also upside risks. A stronger translation of EU funds to investment could boost GDP growth and lift future productive capacity.

## Tax reform is needed for sustainable, inclusive growth

Commitments to improve health, education and social protection will strain limited government resources. OECD long-term projections suggest ageing-related costs could increase by over 6 percentage points of GDP by 2050. Tax reform is needed to fund future outlays while keeping public debt manageable (52% of GDP in 2022). Removing distortions would limit the growth impact of a larger tax burden. The first priority is to end sectoral income tax exemptions and shift more small firms from distortive turnover-based taxes onto the corporate income tax regime. Romania should also transition to progressive labour income taxation. Reduced tax burdens on those with small salaries would encourage formal employment by low-skilled workers. Tax reform could also complement broader efforts to boost female participation, including planned pension age increases and investment in subsidised childcare. Sustaining rapid productivity growth will depend on stronger institutions and predictable policymaking. Romania's climate strategy aims to reduce energy consumption by upgrading the building stock. Greater use of market-based measures, including carbon pricing, could reduce the economic cost of mitigating greenhouse gas emissions.

# Slovak Republic

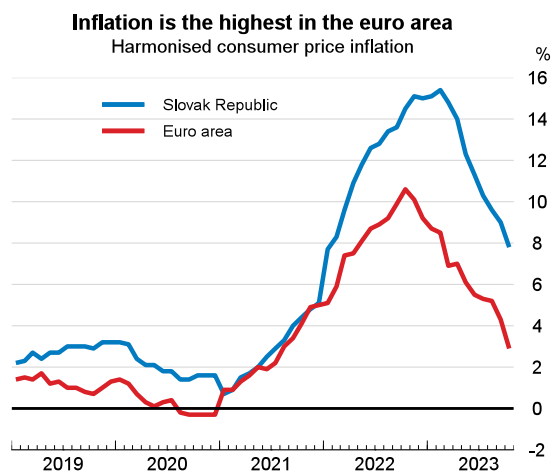
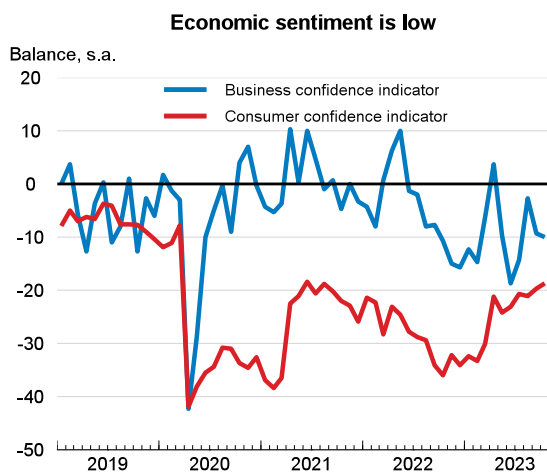
GDP growth is projected to pick-up from 1.1% in 2023 to 1.8% in 2024 and 2.4% in 2025. As inflation abates, real household income growth will bolster consumer demand in 2024 and 2025. Tighter financial conditions will weigh on private investment while EU recovery and resilience funds will sustain public investment throughout the projection period. The recovery of foreign demand will support exports in 2024 and 2025. Risks to the projections are skewed to the downside. They are mainly related to lower absorption of EU funds, which would hamper investment, and higher energy prices, which could lead to persistent inflation.

Fiscal consolidation is needed to rebuild fiscal buffers, reduce inflationary pressures and improve long-term fiscal sustainability in the face of rapid population ageing. The fiscal consolidation strategy should be designed in a way to avoid harming growth and equity. This requires reforming pensions, increasing spending efficiency, and broadening tax bases. Improving the absorption of EU funds can spur growth, reduce socio-economic gaps and accelerate the digital and green transitions.

## Economic growth is subdued and inflation is high

Economic growth slowed in the third quarter of 2023 to 0.2% quarter-on-quarter. High-frequency indicators point to continued modest growth in the last quarter of 2023. Business and consumer sentiment remain subdued. Production and exports in the automotive sector have strengthened alongside an easing of supply chain bottlenecks, with firms working through order backlogs, but remain subdued in other industries. Harmonised consumer price inflation peaked in early 2023 but remains the highest among euro area countries, at 7.8% in October. Core inflation, at 7.7% in October, is also abating but at a slower pace. The labour market continues to be resilient with the unemployment rate close to the pre-pandemic level. Average annual nominal wage growth has risen to around 10%.

## Slovak Republic



Source: Statistical Office of the Slovak Republic; and Eurostat Harmonised index of consumer prices (HICP) database.



## Slovak Republic: Demand, output and prices


	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Slovak Republic</b>						
<b>GDP at market prices</b>	93.4	4.8	1.8	1.1	1.8	2.4
Private consumption	53.7	2.8	5.6	-1.8	1.0	2.3
Government consumption	19.6	4.2	-4.2	-2.5	1.2	0.8
Gross fixed capital formation	18.2	3.5	4.5	6.3	4.1	3.9
Final domestic demand	91.5	3.2	3.2	-0.4	1.7	2.3
Stockbuilding <sup>1</sup>	0.0	2.4	-0.2	-6.4	0.5	0.0
Total domestic demand	91.4	5.9	2.8	-6.1	2.3	2.4
Exports of goods and services	79.3	10.4	3.1	-1.8	3.7	3.1
Imports of goods and services	77.3	11.6	4.5	-9.2	4.2	3.1
Net exports <sup>1</sup>	2.0	-0.8	-1.2	7.9	-0.5	0.0
<i>Memorandum items</i>						
GDP deflator	–	2.4	7.5	8.5	4.2	2.9
Harmonised index of consumer prices	–	2.8	12.1	11.1	5.2	3.4
Harmonised index of core inflation <sup>2</sup>	–	3.3	8.2	9.6	4.9	3.4
Unemployment rate (% of labour force)	–	6.8	6.1	6.0	6.3	6.1
Household saving ratio, net (% of disposable income)	–	4.2	-2.5	0.1	1.0	0.7
General government financial balance (% of GDP)	–	-5.2	-2.0	-5.6	-4.4	-4.3
General government gross debt (% of GDP)	–	79.6	65.4	66.0	66.8	66.9
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	61.1	57.8	58.4	59.2	59.3
Current account balance (% of GDP)	–	-2.5	-8.2	-2.2	-3.6	-3.4

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 114 database.

StatLink  <https://stat.link/tg751e>

Financial conditions have tightened. Banks have quickly transmitted higher euro area policy rates to lending rates for new credit to households and firms. Bank lending to households and firms has slowed markedly and house prices and residential investment have declined. Bank deposit rates have also increased albeit more moderately. Given high current inflation, near-term real interest rates remain negative, in contrast to many OECD countries.

## EU funds will support public investment

The fiscal stance has been highly expansionary in 2023. The budget deficit expanded significantly on account of energy crisis measures (3.3% of GDP) and permanent measures, such as higher family benefits (1.1% of GDP) and VAT reductions in the hospitality and sports sectors (0.2% of GDP). Energy support measures are expected to be largely phased out by the end of this year. The indexation of various social benefits to past inflation will add to spending pressures in the coming years. Slovakia is expected to use significant funds from the EU Recovery and Resilience Facility in 2024-25 (about 2.7% of GDP per year on average), which will boost public investment. A new government coalition was formed in October, waiving the requirement to present a balanced budget for two years under current debt rules. The projections assume a neutral fiscal stance, which is somewhat tighter than implied by the national expenditure rule.

## Economic growth will pick up moderately in 2024 and 2025

As inflation abates in 2024 and 2025, the recovery in real household incomes will support a pick-up in consumer demand. The negative impact of tighter financial conditions on investment will be partly offset by higher usage of EU recovery and resilience funds. After regaining some export market share due to fewer supply chain disruptions in the near-term, exports will grow largely in line with foreign demand over the next two years. Headline inflation will decline, with core inflation declining more slowly due to the lagged pass-through of energy prices to other goods and the effects of nominal wage increases. Risks to the projections are skewed to the downside. Lower absorption of EU funds would negatively affect investment. Higher wage growth or energy prices than assumed in the projections could lead to persistent inflation.

## Stronger efforts to ensure fiscal sustainability are needed

Steady fiscal consolidation is needed to reduce inflationary pressures and ensure fiscal sustainability. Defence spending is expected to increase towards to the NATO target of 2% of GDP. Ageing-related spending could increase by more than 7 percentage points of GDP by 2070. Ageing-related challenges must be addressed, including by improving the sustainability of the pay-as-you-go public pension system, for example through tightening early retirement options. Measures to broaden the tax base, including by reversing VAT exemptions and reductions granted in recent years and improving tax compliance, would bolster fiscal sustainability. Parental leave should be reduced to avoid disincentives for mothers to take up work. Other family benefits have increased substantially and should be carefully evaluated. Support should be primarily targeted to households not sufficiently covered by the social safety net if needed. Large inflows of EU funds offer opportunities for ambitious consolidation without undermining key investments in education, health, and the digital and green transitions.

# Slovenia

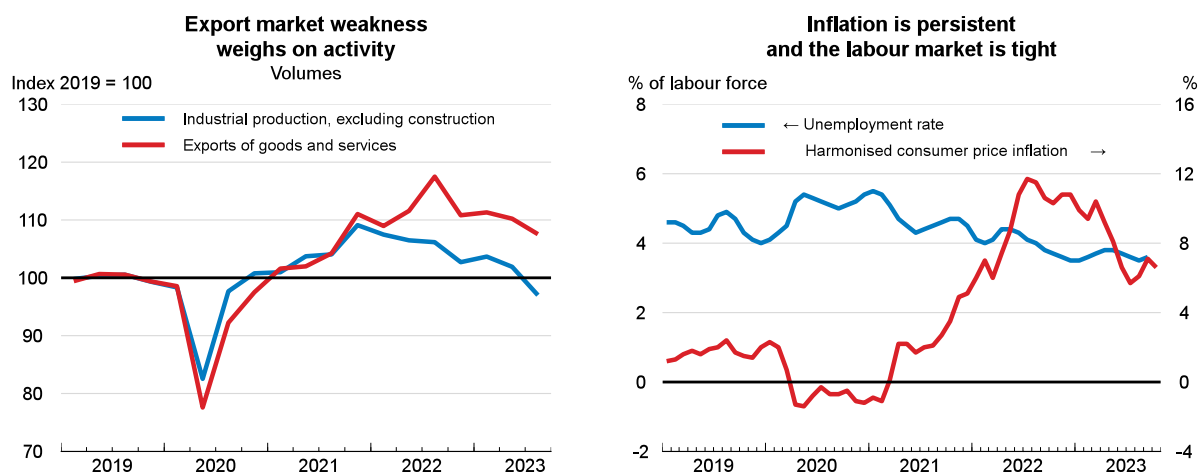
GDP growth is projected to slow to 1.4% in 2023, reflecting weaker domestic and external demand, but will pick up to 1.8% in 2024 and 2.7% in 2025, as disinflation continues to support real incomes and global economic conditions improve. EU funds and the government's flood recovery measures will sustain investment. The tight labour market will fuel stronger wage growth, limiting the pace of disinflation.

Fiscal policy will remain expansionary in 2023, reflecting government measures to mitigate high energy prices and recover from the devastating floods of the summer, before tightening in 2024 and 2025. Fiscal consolidation should be undertaken through more efficient prioritisation of spending, as the current expansionary fiscal stance risks exacerbating inflationary pressures. Structural reforms are needed to preserve fiscal sustainability and raise potential growth, including measures to improve the labour force participation of older workers and reduce labour shortages, and to lower the labour tax burden.


## Economic activity is moderating as foreign demand weakens

Economic activity slowed in the third quarter of 2023, with GDP declining by 0.2% quarter-on-quarter due to subdued private consumption and lower exports. The labour market remains tight with the unemployment rate at 3.6% in September. Minimum wages increased (in January 2023) as well as public sector wages (as a result of negotiated wage agreements in October 2022). Overall, this is reflected in strong wage growth, with labour costs and earnings per hour worked both increasing by 14.6% year-on-year in the second quarter. Wage pressures have contributed to high core inflation of 7.0% in the third quarter of 2023 (year-on-year), with headline inflation at 6.3%.

## Slovenia



Source: OECD Main Economic Indicators database; Statistics Slovenia; OECD Economic Outlook 114 database; and OECD calculations.

StatLink  <https://stat.link/7ju24x>

## Slovenia: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2010 prices)				
<b>Slovenia</b>						
<b>GDP at market prices</b>	47.0	8.2	2.5	1.4	1.8	2.7
Private consumption	23.7	10.3	3.6	0.3	1.3	2.6
Government consumption	9.7	6.1	-0.5	1.9	2.1	1.4
Gross fixed capital formation	8.9	12.6	3.5	8.6	3.7	3.8
Final domestic demand	42.3	9.8	2.7	2.5	2.0	2.6
Stockbuilding <sup>1</sup>	0.5	0.4	1.0	-4.7	-0.3	0.0
Total domestic demand	42.8	10.1	3.7	-2.7	1.7	2.7
Exports of goods and services	36.6	14.5	7.2	-2.5	1.6	3.3
Imports of goods and services	32.4	17.8	9.0	-6.6	1.1	3.4
Net exports <sup>1</sup>	4.2	-1.0	-1.0	3.7	0.5	0.2
<i>Memorandum items</i>						
GDP deflator	–	2.7	6.5	9.1	4.9	3.4
Harmonised index of consumer prices	–	2.0	9.3	7.5	4.8	3.2
Harmonised index of core inflation <sup>2</sup>	–	0.9	5.9	7.0	5.3	3.3
Unemployment rate (% of labour force)	–	4.8	4.0	3.7	3.6	3.6
Household saving ratio, net (% of disposable income)	–	10.2	6.4	7.5	8.0	7.5
General government financial balance (% of GDP)	–	-4.6	-3.0	-4.5	-3.8	-2.9
General government gross debt (% of GDP)	–	95.1	74.4	76.8	79.1	80.5
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	74.4	72.3	71.4	70.1	68.6
Current account balance (% of GDP)	–	3.3	-1.0	4.5	3.1	3.8

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 114 database.

StatLink  <https://stat.link/eothk2>

Slower global growth and deteriorating cost competitiveness (owing to increased energy prices and labour costs) have weakened exports: in the third quarter of 2023, real exports declined by 9.2% year-on-year. Gas import dependency on Russia has declined and gas consumption has been lowered this year. Euro area monetary policy tightening has resulted in tighter financial conditions. Loans to the non-banking sector decreased by 0.6% in August year-on-year, from around 5% average growth before the pandemic.

## Supportive fiscal policy adds to demand and inflationary pressures

The government extended the cap on electricity and gas prices for households and small business until the end of 2023 and will maintain it for all households in 2024, albeit at a lower level, reflecting lower market prices. The cap for electricity will cover up to 90% of 2023 consumption throughout next year, but the gas cap will end in April 2024 with the heating season. The government announced flood recovery support of 1.1% of GDP in 2023 and further measures of 1.9% in 2024 and 0.9% in 2025. Structural measures include an increase in spending on long-term care by less than 0.1% of GDP in 2024 and 0.5% in 2025. These measures are expected to contribute to a budget deficit of 4.5% of GDP in 2023, before the fiscal stance is tightened in both 2024 and 2025, as flood recovery and energy support measures are gradually withdrawn. The expansionary fiscal stance in 2023 has added to demand and inflationary pressures, already heightened by strong wage growth.

## Economic growth is set to moderate

Growth is projected to slow to 1.4% in 2023, reflecting weaker domestic and external demand, before picking up to 1.8% in 2024 and 2.7% in 2025. Elevated inflation is holding back private consumption, but investment is being supported by the inflow of EU funds and the flood recovery measures. The labour market will remain tight, contributing to stronger nominal wage growth but real income growth will be subdued by elevated headline inflation. Growth will improve as foreign demand recovers and headline inflation gradually abates. Public debt is projected to decline to 71.4% of GDP in 2023 and further in the next two years, mainly reflecting strong nominal GDP growth and a gradual reduction in state budget liquidity reserves. A key downside risk is that disruption in energy markets from Russia's war of aggression against Ukraine and the conflict in Israel would restrict economic activity. Also, persistent wage growth and higher energy prices could fuel inflationary pressures. On the upside, recent measures to facilitate the recruitment of foreign labour could help alleviate labour market shortages and wage pressures, while stronger growth among trading partners may revive exports.

## Fiscal consolidation and structural reforms are needed for more sustainable growth

Faster fiscal consolidation is needed to reduce demand and contain inflationary pressures. Fiscal space should be rebuilt by better targeting support for high energy prices, if needed, at the most vulnerable households and through more efficient public spending. Ageing-related public expenditure is projected to increase by 3.7 percentage points of potential GDP between 2024 and 2040. Continued efforts to diversify gas supply will help to improve energy security. Such efforts should be implemented alongside structural reforms to raise potential growth. A growth-friendly tax reform to lower the labour tax burden could be financed by higher environmental and property taxation. This should be complemented by measures to further improve the labour force participation of older workers, extend working lives and reduce labour shortages, such as raising the minimum years of contributions required to retire and stronger incentives to remain in the work force after the statutory retirement age. This, together with the establishment of a rule-based system of public wage increases with enough flexibility to address sector-specific recruitment problems would strengthen fiscal sustainability.

# South Africa

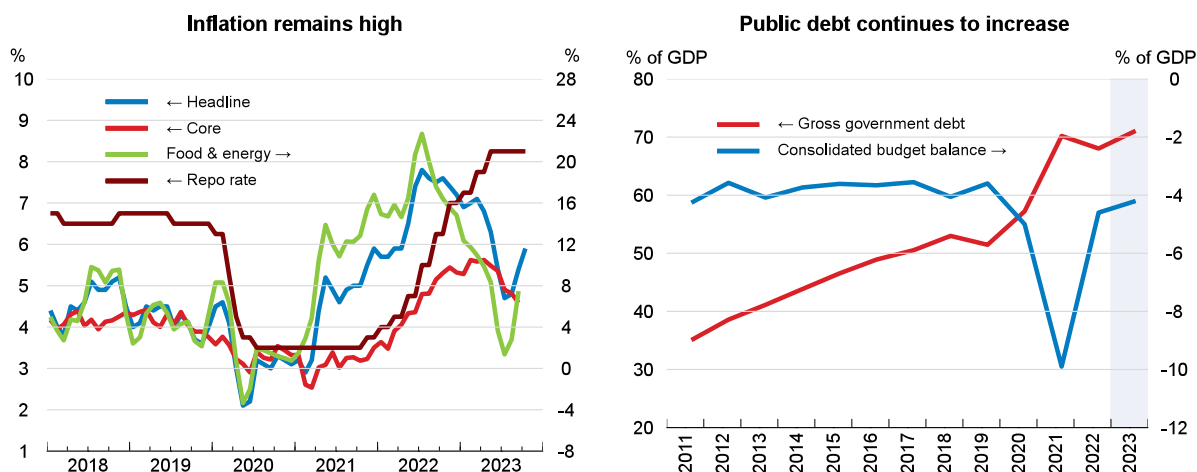
GDP growth is projected to slow to 0.7% in 2023 before increasing by 1% in 2024 and 1.2% in 2025. Investment in machinery and equipment for energy production will remain strong, despite tighter financing conditions. Net exports will weigh on growth as most machinery and equipment are imported and external demand has weakened. Private consumption growth will ease amid still high inflation and lower household purchasing power but will remain positive, helped by employment returning to its pre-COVID-19 level. Inflation will gradually return to the target range, although risks remain to the upside.

The fiscal balance is expected to deteriorate this year, setting back the pace of fiscal consolidation. Higher external financing needs imply greater risk of exposing the government to increasing borrowing costs. Strengthening the medium-term fiscal framework would help to put public debt on a declining path and rebuild fiscal buffers. The central bank should be vigilant and not ease monetary policy until inflation approaches the mid-point of the target range. Improving access to childcare facilities would increase female labour force participation and durably raise employment levels.

## Economic activity surprised positively in the first half of the year

GDP expanded by 0.4% and 0.6% in the first two quarters of 2023, driven by investment in infrastructure, machinery and equipment, including renewable energy products to address longstanding electricity shortages. Despite this expansion, the recovery from the downturn at the end of 2022 is not yet complete. In the second quarter of 2023, household consumption contracted for the first time since 2021. Consumer confidence continues to deteriorate, and annual credit growth slowed from a 15 year high of 10.5% last year to 6.4% in July 2023. At the same time, employment increased 5% in the year to June 2023, marginally surpassing its pre-COVID-19 level. Annual consumer inflation increased again in October, rising to 5.9%.

## South Africa



Note: Data refer to fiscal years.

Source: Statistics South Africa; CEIC; OECD Consumer Price Indices database; National Treasury; and OECD calculations.

StatLink  <https://stat.link/fobcp4>

## South Africa: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices ZAR billion	Percentage changes, volume (2015 prices)				
<b>South Africa</b>						
<b>GDP at market prices</b>	5 568.0	4.7	1.9	0.7	1.0	1.2
Private consumption	3 481.1	5.8	2.5	0.6	0.7	1.5
Government consumption	1 145.6	0.5	1.0	2.3	1.5	1.0
Gross fixed capital formation	768.8	0.6	4.8	7.1	5.5	3.9
Final domestic demand	5 395.5	4.0	2.5	1.9	1.6	1.8
Stockbuilding <sup>1</sup>	- 70.8	0.7	1.2	0.3	0.1	0.0
Total domestic demand	5 324.8	4.8	3.9	2.2	1.7	1.8
Exports of goods and services	1 532.7	9.1	7.4	4.2	2.9	2.1
Imports of goods and services	1 289.5	9.6	14.9	9.1	4.9	3.7
Net exports <sup>1</sup>	243.2	-0.1	-2.0	-1.5	-0.7	-0.6
<i>Memorandum items</i>						
GDP deflator	–	6.5	4.8	4.6	4.8	4.5
Consumer price index	–	4.6	6.9	5.9	5.0	4.6
Core inflation index <sup>2</sup>	–	3.1	4.6	5.4	5.0	4.6
General government financial balance (% of GDP)	–	-6.4	-4.8	-6.4	-6.3	-6.0
Current account balance (% of GDP)	–	3.7	-0.5	-1.9	-1.8	-2.1

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 114 database.

StatLink  <https://stat.link/e7zlf6>

The external balance continues to deteriorate amid declines in the terms of trade, lower export volumes, higher import volumes, and a weak domestic currency. The current account deficit rose to 2.3% of GDP in the second quarter of 2023. Severe electricity rationing, due to poorly maintained and ageing power stations that are not able to meet demand, continues to weigh on domestic activity and on the currency. The availability of electricity has been deteriorating since 2018. The level of power cuts experienced in 2023 already exceeds that in 2022.

## The fiscal outlook has deteriorated, keeping borrowing costs elevated

Tax revenue collection declined substantially in the first half of the year and the public sector wage settlement was higher than budgeted in March 2023. The fiscal deficit is therefore expected to deteriorate significantly this year, after 2 years of fiscal consolidation. The debt-to-GDP ratio continues to increase, together with debt servicing costs. In August, interest payments had already reached 4.9% of GDP and 20% of fiscal revenues. The sovereign bond spread also remains above its pre-pandemic average. The fiscal balance is projected to improve slightly in 2024 and 2025 as the fiscal stance becomes contractionary again. The government is expected to implement cost-cutting measures to lower spending, including a hiring freeze. Although inflation returned to the target range of 3-6% in June, the central bank has kept the policy rate at 8.25% since May, its highest level in fourteen years. Monetary policy is expected to start easing slowly in mid-2024, once inflation converges to the mid-point of the target range, with the policy rate reaching 6.5% by the end of 2024.

## Investment in power generation is driving the recovery

Investment will be the main driver of growth in the near term. Power cuts are expected to ease gradually in 2024 and 2025 as investment in energy generation progressively expands capacity. Weaker global economic activity is expected to reduce demand for South Africa's exports, while investment in energy infrastructure, machinery and equipment will keep import growth elevated. Private consumption will remain subdued amid still high inflation and will only pick up gradually as employment continues its recovery and monetary policy eases. Inflation will gradually fall closer to the mid-point of the target range as supply disruptions alleviate. Political uncertainty around the upcoming presidential elections could reduce investor confidence and slow progress in addressing the energy crisis. In contrast, a stronger expansion of energy supply from private sources would strengthen the recovery. Disinflation is subject to significant risks. Dry weather conditions in the context of El Niño could severely impact crop yields and push up domestic food inflation. Prolonged energy and logistical constraints could increase the cost of doing business and consumer prices even further.

## Accelerating fiscal consolidation efforts would boost investor confidence

Elevated public debt leaves limited fiscal space to mitigate potential adverse shocks, exposes the government to increasing borrowing costs, and contributes to a higher country risk premium and long-term interest rates. Accelerating fiscal consolidation, through a combination of expenditure and revenue-based measures, is essential to put public debt on a declining path, rebuild fiscal buffers, and mitigate financial risks. Fiscal space should be used to reduce poverty, step up carbon mitigation efforts, adapt to climate change, and respond to an ageing population. Strengthening the medium-term fiscal framework, by anchoring the expenditure ceiling with a debt ceiling, would help restore its credibility, boost investor confidence, and strengthen the recovery. Reforms that continue to facilitate access to the power grid for private providers using renewable sources would reduce power outages and strengthen growth, while at the same time making it more sustainable. Further combining competition policy and economic regulation would help foster productivity growth in key network sectors.



# Spain

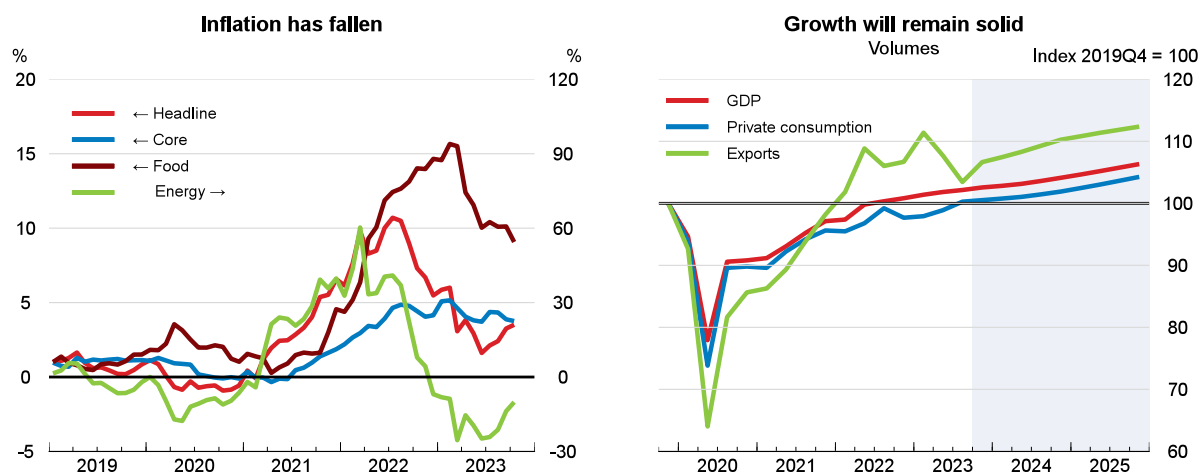
GDP is projected to grow by 1.4% in 2024 and 2.0% in 2025. Domestic demand will be the key driver of growth. Private consumption and investment growth will moderate due to tight financial conditions and persistent inflation in 2024, before picking up in 2025. External demand will be less supportive of growth than in previous years. Inflation is projected to slightly increase to 3.7% in 2024, before decreasing to 2.3% in 2025.

The fiscal deficit is falling over the projection period, but stronger and sustained fiscal consolidation is needed to keep debt on a downward path and create space for ageing-related and growth-enhancing spending. To increase productivity and innovation, efforts should be targeted at fostering R&D projects through partnerships between firms and research institutes, and reducing regulatory differences across regions.

## The economy is slowing

GDP increased by 0.3% in the third quarter of 2023. Business confidence indicators have been sluggish since the spring and business activity surveys show weaker developments across sectors since July. Consumer confidence remains low. The labour market is robust, with employment growing at an annual rate of 2.6% in October, reflecting a higher employment rate and the incorporation of immigrants in the labour force. The unemployment rate increased to 11.8% in September 2023. Nominal wages increased by 4.3% over the year to the third quarter of 2023. Inflation has moderated significantly but increased from 2.1% in July 2023 to 3.5% in October, driven by higher energy prices and base effects. Core inflation has gradually moderated, reaching 3.8% in October 2023.

## Spain



Source: Instituto Nacional de Estadística; Eurostat; and OECD Economic Outlook 114 database.

StatLink  <https://stat.link/fwldin>

## Spain: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices EUR billion	Percentage changes, volume (2015 prices)				
<b>Spain</b>						
<b>GDP at market prices</b>	1 119.0	6.4	5.8	2.4	1.4	2.0
Private consumption	627.5	7.1	4.7	2.2	1.9	2.0
Government consumption	246.3	3.4	-0.2	2.6	1.6	1.3
Gross fixed capital formation	228.5	2.8	2.4	1.7	1.4	2.3
Final domestic demand	1 102.4	5.3	3.2	2.2	1.7	1.9
Stockbuilding <sup>1</sup>	0.5	1.4	-0.2	-0.3	-0.1	0.0
Total domestic demand	1 102.9	6.7	3.0	1.9	1.6	1.9
Exports of goods and services	344.4	13.5	15.2	1.4	1.4	2.6
Imports of goods and services	328.3	14.9	7.0	0.0	2.0	2.4
Net exports <sup>1</sup>	16.1	-0.2	2.9	0.6	-0.2	0.1
<i>Memorandum items</i>						
GDP deflator	–	2.7	4.1	5.5	2.1	2.4
Harmonised index of consumer prices	–	3.0	8.3	3.5	3.7	2.3
Harmonised index of core inflation <sup>2</sup>	–	0.6	3.8	4.3	3.1	2.2
Unemployment rate (% of labour force)	–	14.8	12.9	12.0	12.0	11.8
Household saving ratio, net (% of disposable income)	–	9.6	2.9	2.9	1.6	1.3
General government financial balance (% of GDP)	–	-6.7	-4.7	-3.6	-3.2	-3.1
General government gross debt (% of GDP)	–	140.9	116.3	114.1	114.7	114.6
General government debt, Maastricht definition <sup>3</sup> (% of GDP)	–	116.8	111.6	109.5	110.1	110.0
Current account balance (% of GDP)	–	0.8	0.6	2.5	1.4	1.2

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 114 database.

StatLink  <https://stat.link/ufntjh>

Export and import growth have decreased in recent quarters as activity in Spain's main trading partners has eased. Monetary policy tightening is influencing activity. Credit standards for loans to enterprises and consumers have tightened and loan costs have increased for all sectors. Housing credit to households and credit to firms decreased by 3.4% and 4.7% respectively over the year to September 2023. Households are highly exposed to rising interest rates, with 70% of mortgages on variable rates.

## Mild fiscal consolidation is underway

The government deficit is projected to decline to 3.2% in 2024 and 3.1% in 2025. Measures to curtail inflation have been prolonged until end-2023, including a EUR 200 cheque for low-income households, a VAT cut for essential food products and targeted support to specific sectors. In addition, previous tax cuts on gas and electricity and some subsidies on transport fees have been extended. Most of these measures are expected to end in December 2023, with tax cuts on energy and food expected to be phased out in the first half of 2024.

## Growth is moderating, but will remain solid

GDP is projected to moderate to 1.4% in 2024, before picking up to 2.0% in 2025. Restrictive monetary policy along with less supportive fiscal policy will slow private and public consumption in 2024. Investment will also slow due to tight credit and financial conditions. Net exports are expected to improve from 2025, helped by stronger growth in the main EU trading partners. The gradual decrease in inflationary pressures,

along with the resilience of the labour market and the deployment of projects under the Recovery, Transformation and Resilience Plan (RTRP) will support growth in 2025. Inflation is expected to pick up in the first half of 2024 as the measures to curtail energy price inflation will be gradually phased out from December 2023, but will decrease again towards the end of 2024 and in 2025. Core inflation is expected to remain high in 2024 due to the lagged effect from the pass through of higher energy prices, but fall in 2025. The outlook is surrounded by significant risks. A further escalation of geopolitical conflicts could push up energy prices and inflation and worsen the economic outlook in Spain's main trading partners. Slow implementation of the RTRP could restrain growth more than expected. On the upside, a faster-than-expected improvement in the international environment and a greater impact from the RTRP funds would support activity.

### **Public debt needs to be reduced further**

Stronger and sustained fiscal consolidation is needed to maintain debt on a downward path and create space for growth-enhancing spending. Ageing-related spending is estimated to increase by 2.7% points of potential GDP from 2024 to 2040. Sizeable fiscal support helped to mitigate the effects of the inflationary shock on business and households, but the support should end as planned. Efforts to foster R&D projects through partnerships between firms and research institutes and reduce regulatory differences across regions would improve productivity and innovation. Improving skills and enhancing education outcomes can enhance job prospects, especially for the youth, and should be prioritised together with more efficient active labour market policies. Fulfilling the country's objectives to fight climate change will require a more environment-friendly tax regime, with a broader taxation base and fewer exemptions, and gradually increasing tax rates on non-ETS emissions.

# Sweden

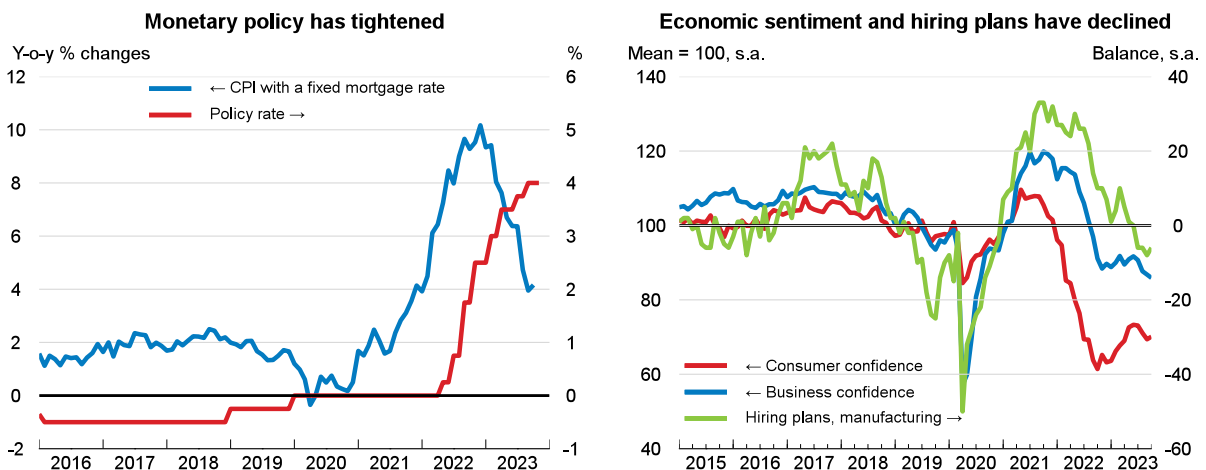
After a projected 0.5% contraction in 2023, GDP is projected to rise by 0.9% in 2024 and 2.6% in 2025. In the near term, elevated inflation will continue to weigh on households' real disposable income and private investment, which is also held back by higher construction costs and declining demand for manufactured goods. Private consumption growth is expected to start regaining momentum in early 2024 as real disposable incomes start recovering.

Monetary policy should remain restrictive until inflation is clearly moving towards target. Continued fiscal restraint would help to combat inflation and maintain fiscal space. Tax reform, including aligning property taxes more closely with market values and phasing out mortgage interest deductions would improve tax efficiency and fairness. Loosening rent controls and other reforms facilitating mixed-background neighbourhoods, equal opportunities in schools, and the integration of disadvantaged groups into the labour market remain priorities.

## Economic activity has declined

After declining by 0.8% in the second quarter, mainly due to falling exports and investments, preliminary estimates suggest output remained unchanged in the third quarter. Recent indicators show a deterioration in economic activity, with the monthly GDP indicator and household consumption declining. High production costs and falling housing prices continue to weigh on housing investment. Confidence remains low among households and businesses. The labour market is deteriorating with declining employment, increased layoff notices and rising new unemployment registrations. Long-term unemployment is below pre-pandemic levels, but many jobseekers lack necessary skills. In October, consumer price inflation with a fixed mortgage rate (CPIF) was down to 4.2%, but CPIF inflation excluding energy remained at 6.1%. The Swedish krona has depreciated significantly, recently hitting all-time lows against the euro.

## Sweden



Source: Sveriges Riksbank; Statistics Sweden; and National Institute of Economic Research.

## Sweden: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices SEK billion	Percentage changes, volume (2022 prices)				
<b>Sweden</b>						
<b>GDP at market prices</b>	5 034.8	5.9	2.9	-0.5	0.9	2.6
Private consumption	2 215.5	6.2	1.9	-1.9	0.6	2.5
Government consumption	1 331.4	2.9	0.1	2.1	1.6	2.0
Gross fixed capital formation	1 266.2	6.8	6.2	-1.6	0.5	3.4
Final domestic demand	4 813.1	5.4	2.6	-0.8	0.8	2.6
Stockbuilding <sup>1</sup>	- 1.6	0.4	1.1	-0.4	-0.1	0.0
Total domestic demand	4 811.5	5.9	3.7	-1.2	0.7	2.6
Exports of goods and services	2 205.4	10.8	7.1	2.0	2.6	3.5
Imports of goods and services	1 982.0	11.3	9.4	0.7	2.4	3.5
Net exports <sup>1</sup>	223.4	0.3	-0.6	0.7	0.2	0.1
<i>Memorandum items</i>						
GDP deflator	–	2.6	5.9	5.5	3.5	2.3
Consumer price index <sup>2</sup>	–	2.2	8.4	8.6	3.8	2.2
Core inflation index <sup>3</sup>	–	2.4	7.7	6.0	2.6	2.2
Unemployment rate (% of labour force)	–	8.9	7.5	7.7	8.3	8.4
Household saving ratio, net (% of disposable income)	–	15.5	13.3	13.4	13.8	14.0
General government financial balance (% of GDP)	–	0.0	1.1	-0.3	-0.8	-1.4
General government debt, Maastricht definition <sup>4</sup> (% of GDP)	–	36.6	32.9	33.0	33.3	33.5
Current account balance (% of GDP)	–	6.8	4.8	5.0	5.2	5.1


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 114 database.

StatLink  <https://stat.link/rkl0ix>

The Swedish economy remains affected by Russia's war of aggression against Ukraine and the ongoing global economic slowdown. Despite a recent fall, persistently elevated commodity prices are still exerting pressure on economic activity. Tightening global financial conditions, together with the depreciation of the Swedish krona, have heightened the risk of financial stress and are adding to debt servicing costs. Swedish exporters benefit from the weak krona, but sluggish demand in key trading partners is constraining export growth.

### Macroeconomic policies are restrictive

The Riksbank held its policy rate unchanged at 4% in November, likely signalling that the Swedish policy rate has reached its peak. Monetary easing is expected from early 2025, with policy rates declining by 50 basis points through the year. The fiscal stance over 2023 and 2024 remains broadly neutral with discretionary spending being scaled back. Ageing-related public expenditure is projected to increase by 1.8 percentage points of GDP by 2040. The 2024 budget bill features new measures of around SEK 38 billion (0.7% of GDP), primarily targeting households, welfare and defence. This includes an earned income tax credit (0.2% of GDP), tax cuts for pensioners (0.1% of GDP), cuts in petrol and diesel taxes (0.1% of GDP) and targeted grants to local governments for healthcare and education services (0.1% of GDP). The budget also aims to increase defence spending from 1.3% in 2023 to 2% of GDP in 2024, aligning with the NATO target. These measures are to be largely funded through cost-saving measures, such as a temporary pause of the state income tax threshold indexation and the more efficient use of central government and labour policy resources.

## A rebound is expected from 2024

The economy is projected to contract by 0.5% in 2023 before rebounding by 0.9% in 2024 and 2.6% in 2025. In the near term, economic activity will be held back by elevated inflation and tighter macroeconomic policies. Employment is set to shrink further as companies adjust staffing plans in response to reduced demand. Inflation is projected to revert to target by late 2025, amid fading commodity price pressures and monetary policy restraint. A gradual increase in household consumption is expected from early 2024, driven by real wage growth. Significant risks surround the outlook. Escalations of the conflict in the Middle East and Russia's ongoing aggression against Ukraine could lead to renewed supply chain disruptions, affecting the export-oriented Swedish economy. Tighter than foreseen ECB policy may prompt the Riksbank to follow suit to keep disinflation on track and prevent an excessive weakening of the krona. Tighter interest rates and financial conditions in turn may be challenging for highly leveraged commercial real estate developers and households. Lower-than-expected inflation could lead to a faster-than-assumed downward adjustment of policy rates and a quicker economic recovery.

## Making economic growth more inclusive and sustainable

Continued fiscal policy restraint is warranted to help combat inflation and preserve fiscal space. Aligning property taxes with market values and gradually phasing out mortgage interest deductions should also be considered. Policies to enhance inclusion, equal opportunity and make use of underutilised labour resources include loosening rent controls and ensuring that schools effectively counterweigh social disadvantage. A recent overhaul of the employment service can help reduce persistently high long-term unemployment if implemented effectively. Temporary gasoline and diesel tax cuts should be phased out to align with climate goals. Streamlining permitting procedures is also essential to sustain the ongoing green transition.

# Switzerland

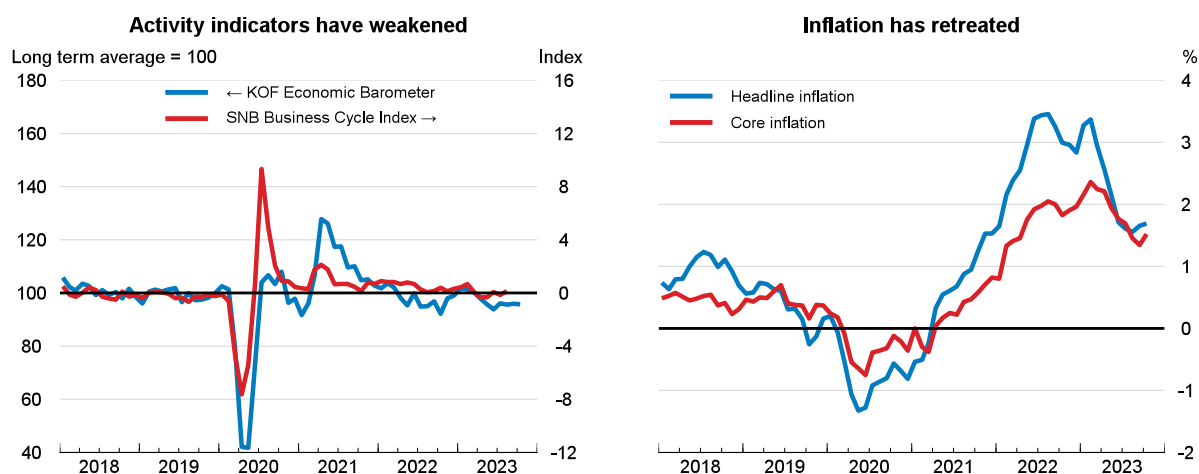
Real GDP is projected to grow by 0.9% in 2024 and 1.4% in 2025. Tighter financial conditions, heightened uncertainty and weaker global trade growth will weigh on private investment and exports. Rises in rents and electricity prices will push inflation above 2% in 2024, before it returns to the Swiss National Bank's target range of 0-2% in 2025. These higher prices will moderate household consumption. Further weakness in foreign demand, energy supply disruptions and a sharp house price correction are key downside risks to activity.

Monetary policy should remain tight to ensure that inflationary pressures subside. Continued low fiscal surpluses are appropriate. Structural reform is needed to tackle population ageing and challenges due to the green and digital transitions. Increasing labour market participation, notably of mothers and older workers, would help alleviate labour shortages. Faster emission reductions and further electrification would improve environmental sustainability and increase energy security.


## The economy has stagnated amid slower global growth

Economic growth has weakened in 2023. Past monetary tightening to fight inflation is cooling the economy, particularly investment spending. Manufacturing activity has stalled, with slow demand in trading partners weighing on exports. The KOF Economic Barometer, the Purchasing Manager Index (PMI) and the SNB's business cycle indicator point to a loss of momentum in the economy. Household consumption has remained relatively strong despite very low consumer confidence, buttressed by a strong labour market. Headline inflation has retreated to the 0-2% target range since June 2023, after peaking at 3.5% in August 2022. This decline largely reflected lower import prices, with consumer price inflation of domestic goods and services remaining above 2%. Longer-term inflation expectations of companies and financial analysts have stayed within the 0-2% range.

## Switzerland



Source: Swiss National Bank; KOF Swiss Economic Institute; and Federal Statistical Office.

StatLink  <https://stat.link/zj64bm>

## Switzerland: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices CHF billion	Percentage changes, volume (2015 prices)				
<b>Switzerland</b>						
<b>GDP at market prices</b>	695.8	5.4	2.7	0.8	0.9	1.4
Private consumption	361.3	1.8	4.2	2.2	0.8	1.0
Government consumption	84.5	3.3	-0.8	0.6	0.5	1.0
Gross fixed capital formation	187.9	2.8	1.2	-1.2	-1.6	1.0
Final domestic demand	633.7	2.3	2.6	1.0	0.1	1.0
Stockbuilding <sup>1</sup>	18.4	-2.2	-0.6	-1.2	-0.5	0.0
Total domestic demand	652.1	0.0	1.8	-0.5	-0.6	1.0
Exports of goods and services	445.8	13.6	6.3	3.7	1.9	3.2
Imports of goods and services	402.1	5.6	6.0	2.6	0.2	3.2
Net exports <sup>1</sup>	43.7	5.4	0.9	1.2	1.4	0.5
<i>Memorandum items</i>						
GDP deflator	–	1.2	2.5	1.1	1.9	1.6
Consumer price index	–	0.6	2.8	2.2	2.1	1.5
Core inflation index <sup>2</sup>	–	0.3	1.7	1.9	1.8	1.4
Unemployment rate (% of labour force)	–	5.1	4.3	4.1	4.4	4.4
Household saving ratio, net (% of disposable income)	–	20.5	19.3	19.1	19.0	18.8
General government financial balance (% of GDP)	–	-0.3	1.2	0.8	0.5	0.4
General government gross debt (% of GDP)	–	41.5	37.7	37.0	36.6	36.4
Current account balance (% of GDP)	–	8.9	9.9	9.8	10.4	10.8

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 114 database.

StatLink  <https://stat.link/zp3bry>

Goods exports have slowed since the beginning of the year, as export market growth has moderated. The strength of the Swiss franc, supported also by foreign exchange interventions by the Swiss National Bank (SNB), has reduced export competitiveness, mitigated import price pressures and helped temper domestic inflation. Despite the strength of the currency, tourism inflows have continued and are now close to pre-pandemic levels, supporting activity in accommodation and hospitality sectors.

## Macroeconomic policy has been tight

The SNB's key policy rate has been raised to 1.75% - a cumulative 250 basis points since June 2022. Interest rates are assumed to increase to 2% by the fourth quarter of 2023 and remain at that level until the beginning of 2025 to ensure that inflation returns durably within the 0-2% band. The general government is expected to register another surplus of 0.8% of GDP in 2023, despite weakening GDP growth. Fiscal prospects improved substantially during 2023, underpinned by extraordinary items. For example, the rescue mechanism for the electricity industry (0.5% of GDP) was not needed. In 2024, further spending is anticipated on Ukrainian refugees, as well as on infrastructure and renewable energy sources. General government debt is projected to decline to 36.4% of GDP by 2025.

## GDP growth will remain modest

Real GDP growth is projected to remain below potential until the middle of 2024, reflecting the impact of tighter monetary policy on external and domestic demand. The economy is projected to grow by 0.9% in 2024 and 1.4% in 2025 as the economy recovers. Consumption growth is expected to be weaker in 2024 because of subdued household purchasing power. Rent increases, linked to the rising mortgage reference



rate, and increases in electricity prices in the domestic retail market in the beginning of 2024, will push consumer prices higher. Headline inflation is projected to rise again above 2% during 2024, before moderating into 2025. Risks related to energy supply and prices remain for the upcoming winter. Uncertainty also remains around the persistence of core inflation and the impact of monetary policy tightening on growth. Tighter financial conditions could heighten the risks surrounding high indebtedness and the repricing of real estate, with potential repercussions on the financial sector.

### **Reforms are needed to accelerate the green transition and boost inclusiveness**

Despite low public debt and a return to fiscal surpluses, pressures are growing in the medium term related to population ageing, the green transition and defence spending. Given the weakening of the economy, a slight fiscal easing is appropriate in the short term while medium-run challenges call for structural reform to counter rising costs and strengthened tax revenues. Switzerland must either cut spending, notably on pensions, or significantly raise public revenues over the coming years. Economic growth would benefit from higher labour market participation. Longer working lives and lower barriers for mothers to work full time would help in this regard. Stronger incentives and speedier approval processes can help accelerate emission reductions, notably in the transportation and building sectors, and facilitate further electrification of the economy, making growth more sustainable.

# Türkiye

After a strong first half of the year, economic growth is projected to reach 4.5% in 2023, before slowing to 2.9% in 2024 and 3.2% in 2025. Tighter financial conditions, subdued economic sentiment and stubbornly high inflation will moderate household consumption. However, investment growth will remain elevated due to ongoing reconstruction activity following the earthquakes at the beginning of this year. Exports will gain traction in 2025, reflecting stronger global growth. Inflation is projected to decline over the projection period, but will remain considerably high.

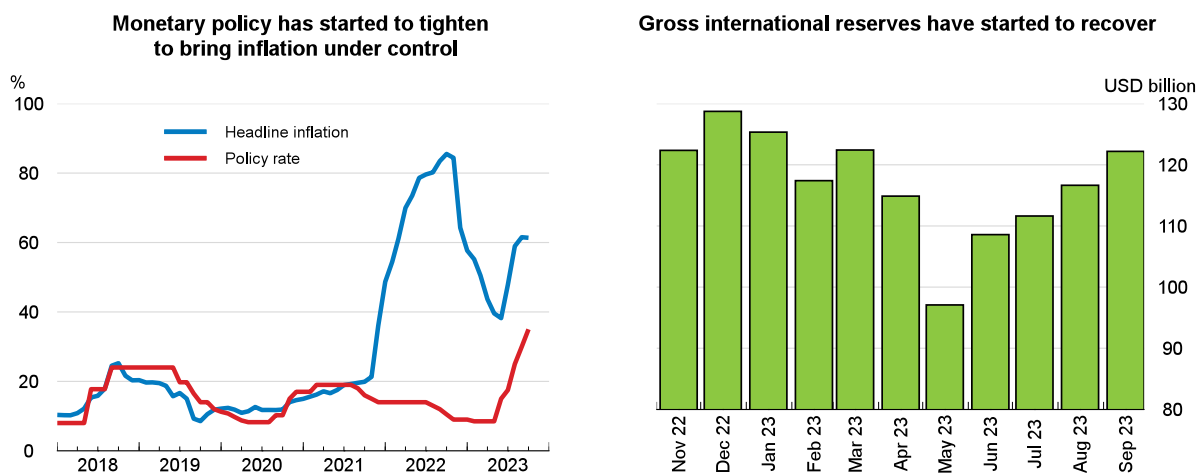
Further rate rises are expected as the central bank is now determined to tighten monetary policy as needed until there is a significant improvement in the inflation outlook. Meanwhile, the government is moving ahead with fiscal consolidation measures to stabilise public finances. Accelerating labour supply reforms would help to support the current efforts to stabilise the macroeconomic framework.

## Robust growth was supported by domestic demand

Despite earthquake-induced effects, economic activity remained strong in the first half of the year. High growth was driven by strong domestic demand supported by overly accommodative monetary and fiscal policy. Real household consumption growth was one of the highest rates in the last 40 years. The unemployment rate has dropped below 10%. However, forward-looking indicators such as consumer confidence and capacity utilisation suggest a moderation of growth for the second half of the year. Furthermore, inflation remains persistently high and reached almost 60% in October, driven by higher input costs, strong demand, and the depreciation of the lira, which has lost almost one-third of its value since the beginning of the year.

Tourism revenues have helped to reduce the high current account deficit. The number of foreign visitors rose by 12.6% to almost 40 million people in the first 9 months of the year compared to the same period last year. The depleted foreign currency reserves have also started to increase. However, higher energy prices and the slowdown in the global economy could generate pressures on the current account balance, though the start of natural gas production from the Sakarya field will ease these risks somewhat.

## Türkiye



Source: OECD Main Economic Indicators database; CBRT; and BIS, Central bank policy rates.

StatLink  <https://stat.link/d8uhg2>

## Türkiye: Demand, output and prices


	2020	2021	2022	2023	2024	2025
<b>Türkiye</b>	Current prices TRY billion	Percentage changes, volume (2009 prices)				
<b>GDP at market prices</b>	5 048.6	11.4	5.5	4.5	2.9	3.2
Private consumption	2 866.0	16.0	18.5	14.9	1.5	2.7
Government consumption	757.0	3.2	4.3	6.6	3.5	1.6
Gross fixed capital formation	1 389.5	7.2	1.3	7.1	6.0	3.7
Final domestic demand	5 012.4	11.5	11.3	11.5	2.9	2.9
Stockbuilding <sup>1</sup>	192.8	-6.3	-5.4	-0.8	-0.6	0.0
Total domestic demand	5 205.2	4.0	5.0	10.4	2.5	3.1
Exports of goods and services	1 470.2	25.1	9.9	-2.6	3.4	3.8
Imports of goods and services	1 626.8	1.7	8.6	13.3	2.0	3.3
Net exports <sup>1</sup>	- 156.6	6.8	0.5	-6.7	0.4	0.1
<i>Memorandum items</i>						
GDP deflator	—	29.0	96.0	63.0	48.8	30.8
Potential GDP, volume	—	4.4	4.4	4.3	4.3	4.2
Consumer price index <sup>2</sup>	—	19.6	72.3	52.8	47.4	31.6
Core inflation index <sup>3</sup>	—	18.3	57.3	57.4	47.7	31.6
Unemployment rate (% of labour force)	—	12.0	10.5	9.6	10.0	10.2
Current account balance (% of GDP)	—	-1.0	-5.4	-4.1	-3.0	-2.4

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

2. Based on yearly averages.

3. The consumer price index excluding food, energy, alcoholic beverages and gold.

Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/ck504x>

## Fiscal and monetary policy have become tight

Since June, the central bank has been tightening monetary policy to restore price stability. The policy interest rate has been lifted from 8.5% in June to 40% in November accompanied by strong signalling of further increases until inflation is under control. The projections assume that the policy rate is raised to 45% in 2024. In addition, credit and quantitative tightening measures have been put in place, including lowering the growth limit for commercial, car and all-purpose loans. These steps are welcome. At the same time, the government has started to tighten fiscal policy to restore fiscal sustainability. The budget deficit is expected to be reduced mainly through taxation. Tax on petrol has been tripled, the standard VAT rate raised from 18% to 20%, the reduced VAT rate for essential items such as basic food and textiles increased by 2 percentage points, and the VAT on some cleaning products increased from 8% to 20%. Without these measures, the deficit would have increased substantially. It is important that fiscal discipline is restored as prudent fiscal policy has been an important policy anchor over the past two decades in Türkiye.

## Growth is set to moderate

Restrictive monetary and fiscal policy coupled with elevated inflation will moderate private consumption. The labour market will cool slightly as growth eases. In contrast, total investment will remain strong as reconstruction efforts after the earthquake continue in 2024. Export growth will gradually improve in line with the global economic environment. The measures to contain inflation will have an impact, but nevertheless inflation will decrease only gradually and will remain above 20% until the end of the projection period. There is a risk that inflation could become entrenched at high levels if monetary policy were to be relaxed. In contrast, further credible policy improvements in fiscal, financial and monetary policy might improve investors' sentiment and strengthen growth.

## Securing stronger growth

Structural reforms can support the current efforts to stabilise the macroeconomic framework and raise long-term growth potential. Notably, labour-market reform would help increase high-quality formal job creation. Making permanent contracts more flexible and ensuring that statutory minimum wages are affordable for firms will help create more formal jobs, raising welfare as well as fiscal revenues. In addition to the current consolidation effort, the government should systematically monitor risks stemming from contingent liabilities, as they have expanded in recent years, including from public-private partnerships. This raises Türkiye's vulnerability to shocks. Expenditure reviews should also be undertaken to improve public spending effectiveness.

# United Kingdom

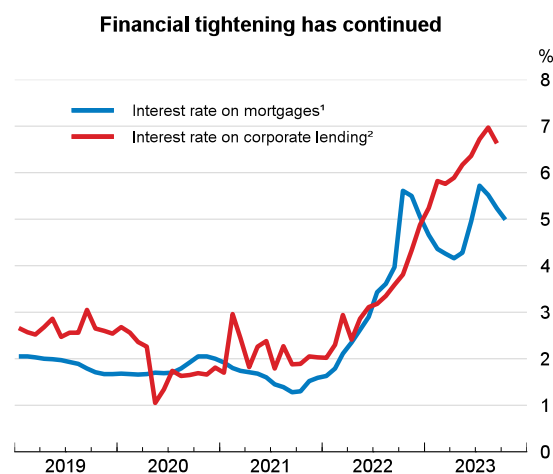
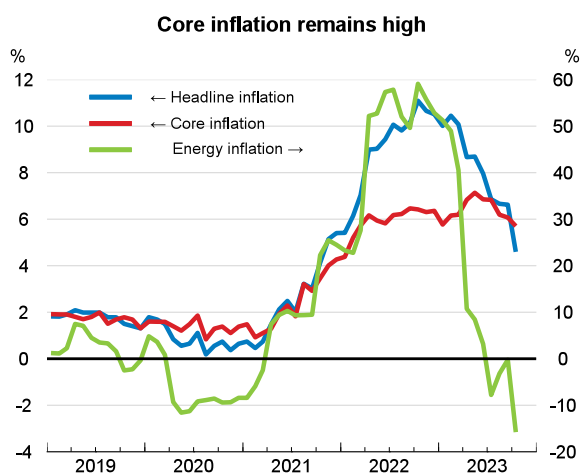
GDP growth is projected to pick up from 0.5% in 2023 to 0.7% in 2024 and 1.2% in 2025. Private expenditure will replace government consumption and investment as the main driver of growth, helped by easing price pressures. Headline inflation will subside from historically high levels but remain above target over most of the projection period. Core inflation will linger at 3.8% in 2024 and 2.6% in 2025 on the back of the tight, albeit easing, labour market. Unemployment will edge up to 4.9% in 2025.

The fiscal stance is becoming restrictive and adequately supports monetary policy, which is expected to remain tight until price pressures ease sustainably. Continuing to address fiscal challenges is a priority, including by swiftly implementing planned supply-side reforms to boost potential growth. Better land-use planning regulations are necessary for the timely rollout of decarbonisation investments.

## Monetary tightening is working its way through the economy

GDP is estimated to have stagnated in the third quarter, after growing by 0.2% in the second quarter. Retail sales volumes are falling and were 2.7% lower in October than in the same month a year earlier. Consumer confidence remains depressed, although it is markedly higher than a year ago. New mortgage lending has continued to decline, with fewer than 45 000 new approvals for house purchase in September, down from almost 100 000 in January 2021 when the monetary tightening cycle started. After a short-lived pick up, business sentiment in services has deteriorated again. Lending to businesses contracted by 1.5% over the year to September.

## United Kingdom 1



1. Average quote for 5-year fixed rate (75% LTV).


2. Sterling weighted average rate on loans and new advances to private non-financial corporations.

Source: Bank of England; and Office of National Statistics.

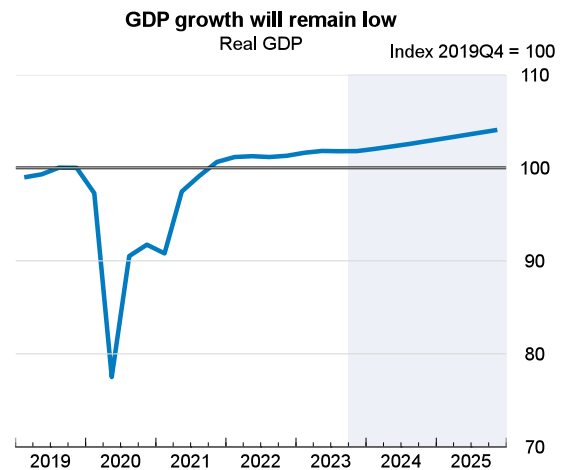
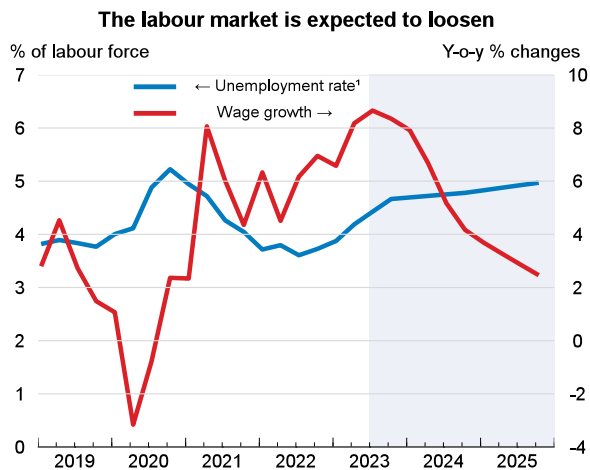
## United Kingdom: Demand, output and prices

	2020	2021	2022	2023	2024	2025
	Current prices GBP billion	Percentage changes, volume (2019 prices)				
<b>United Kingdom</b>						
<b>GDP at market prices</b>	2 104.3	8.7	4.3	0.5	0.7	1.2
Private consumption	1 246.1	7.5	5.2	0.5	1.4	1.6
Government consumption	475.6	14.9	2.5	-0.4	0.0	0.4
Gross fixed capital formation	367.5	7.4	7.9	2.7	-1.8	-0.1
Final domestic demand	2 089.2	9.1	5.1	0.7	0.5	1.0
Stockbuilding <sup>1</sup>	2.3	0.1	-0.5	-0.5	0.2	0.0
Total domestic demand	2 091.5	9.1	4.6	0.2	0.7	1.0
Exports of goods and services	624.8	4.9	8.6	-0.4	1.5	1.6
Imports of goods and services	612.0	6.1	14.1	-1.3	1.5	1.1
Net exports <sup>1</sup>	12.8	-0.3	-1.7	0.3	0.0	0.1
<i>Memorandum items</i>						
GDP deflator	—	-0.1	5.2	7.3	2.9	1.9
Harmonised index of consumer prices	—	2.6	9.1	7.3	2.9	2.5
Harmonised index of core inflation <sup>2</sup>	—	2.4	5.9	6.3	3.8	2.6
Unemployment rate (% of labour force)	—	4.5	3.7	4.3	4.7	4.9
Household saving ratio, gross (% of disposable income)	—	12.5	8.1	8.8	9.4	8.8
General government financial balance (% of GDP)	—	-7.9	-4.6	-5.5	-4.5	-3.7
General government gross debt (% of GDP)	—	105.3	100.4	101.1	103.3	104.9
Current account balance (% of GDP)	—	-0.5	-3.1	-3.5	-2.7	-1.9

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.  
 Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/ubf2ls>

## United Kingdom 2



1. Share of active population aged 15 and over.  
 Source: OECD Economic Outlook 114 database.

StatLink  <https://stat.link/yqwj9d>

Lower wholesale energy and imported food materials inflation, and the appreciation of the sterling on a year earlier, are helping to tame price pressures. Annual inflation fell to 6.7% in September, and dropped further to 4.6% in October as the large base effect from the October 2022 increase in the regulated energy price disappeared. The labour market shows signs of easing, with unemployment picking up steadily since the spring and vacancies continuing to fall. However, wage growth remains high, with annual nominal regular pay growth in the private sector at 7.8% in the three months to September, down from 8.1% in the three months to August. This has contributed to enduring services price pressures and a major upward surprise in core inflation over the summer.

## The policy mix is strongly restrictive

The Bank of England is assumed to maintain its base rate at the current value of 5.25% throughout 2024. In line with the Bank's statement, the pace of quantitative tightening is assumed to increase, from GBP 80 billion in the twelve months to September 2023 to GBP 100 billion by September 2024, bringing the balance sheet to a total of GBP 658 billion. Monetary policy is expected to ease in 2025 as core inflation starts subsiding sustainably, with the base rate declining to 4% by the end of the projection period.

The fiscal stance will be restrictive in 2024-25, with assumed consolidation of almost 2% of GDP, as the government complies with its national fiscal rule of decreasing public debt within a five-year horizon. Energy support measures have been phased out and the energy price cap no longer binds. Fiscal pressure on households and businesses has increased significantly since the spring Budget, due to the freeze of income tax brackets and the corporate income tax rate increase. The government is also committed to increase defence spending from about 2% to 2.5% of GDP. In the longer run, the supply-side measures in the Autumn Statement and spring Budget, including the cuts in national insurance contributions and the "full-expensing" investment allowance, could enable the government to reduce fiscal pressure by gradually increasing labour market participation and business investment. However, ageing and high inflation coupled with the triple lock will push up pension spending by about 0.8% of GDP by fiscal year 2027/28; the necessary public investments to decarbonise power, the built environment and industry amount to about 0.5% of GDP per year; and the rising take-up of electric vehicles will cost about 0.4% of GDP a year in forgone fuel duty by 2030.

## Growth will remain stable but low

GDP will grow by 0.7% in 2024 and 1.2% in 2025, despite the restrictive policy stance. Private consumption will pick up as real wages finally grow due to fast nominal pay growth and lower consumer price inflation. However, monetary tightening is weighing on housing and business investment, higher fiscal pressure will reduce household disposable income, and uncertainty will continue to be a drag on trade. The labour market is set to loosen, thereby moderating real wage growth beyond a period of catch up to inflation, and unemployment will increase steadily to about 4.9%. The government deficit will improve from 5.5% of GDP in 2023 to 4.5% of GDP in 2024 and 3.7% of GDP in 2025, owing mostly to fiscal consolidation. However, public debt will remain above 100% of GDP and continue to increase over the projection period.

Significant risks surround the outlook. The relatively large proportion of inflation-linked public debt and the recent decrease in average debt maturity, combined with rising borrowing costs, leave little fiscal space to confront possible shocks, including potential further surges in wholesale gas prices due to Russia's war of aggression against Ukraine and rising tensions in the Middle East. Renewed political uncertainty would affect households, firms and markets' confidence negatively. A rundown of excess household savings and faster-than-expected negotiations of new trade relationships constitute upside risks.

## Continuing to address fiscal challenges is urgent

Maintaining and strengthening current fiscal efforts is essential against the challenging backdrop of high borrowing and debt, and as higher debt interest payments have eroded fiscal headroom. Reforming the costly triple lock uprating of state pensions would help, by indexing pensions to an average of CPI and wage inflation, and by providing direct transfers to poor pensioners to mitigate poverty risks. Delivering on planned supply side reforms to reduce labour market inactivity and further reducing policy uncertainty for business investment would also improve fiscal sustainability by raising GDP. Enhancing framework conditions, especially land-use planning, is necessary to enable the investments required to reach net zero.

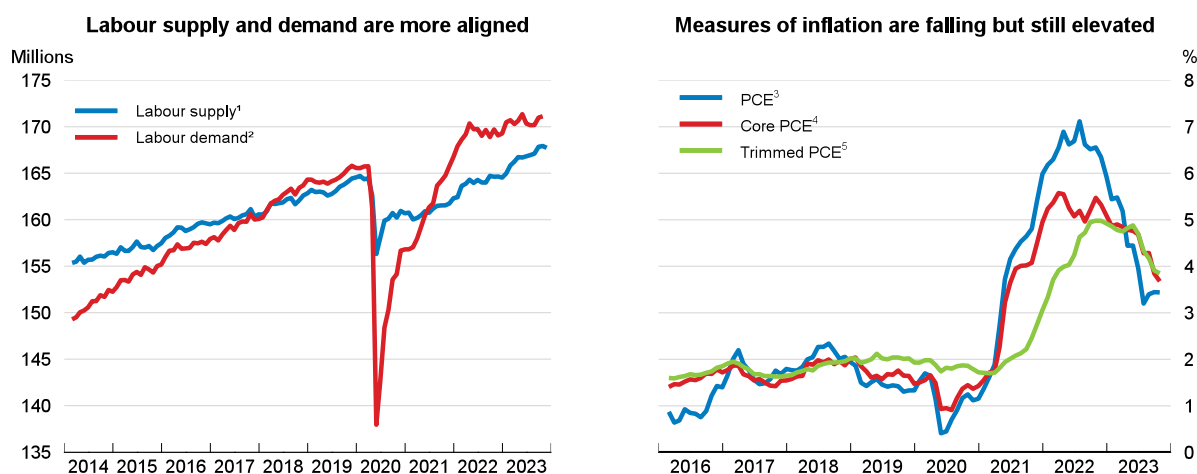


# United States


Real GDP is projected to grow by 2.4% in 2023, 1.5% in 2024, and 1.7% in 2025. Growth in private consumption and investment are expected to moderate in response to the effects of tighter monetary and financial conditions. Employment growth will slow further in response to weaker demand and the unemployment rate will continue to edge up through the first half of 2024. Inflation will decline, allowing for monetary policy easing in the second half of 2024 and a recovery of domestic demand growth in 2025. The outlook could worsen if the effects of tighter policy rates are stronger than assumed or lead to financial stress. A stronger decline in inflation combined with resilient employment could lead to a greater easing of financial conditions and an improved growth outlook.

Monetary policy will remain restrictive in the near term, exerting downward pressure on inflation while still allowing for economic growth, but will ease gradually from late 2024. The budget deficit will narrow somewhat in 2024 but remain large, while long-term fiscal pressures are mounting. Adopting a framework to improve the sustainability of public finances will help produce a more sustainable and inclusive economic future, while enhancing macroeconomic stability.

## United States 1



1. Labour supply is total number of employed and unemployed people.
  2. Labour demand is total number of employed persons plus total number of job openings.
  3. Personal Consumption Expenditures price index.
  4. Personal Consumption Expenditures price index excluding food and energy.
  5. The Trimmed Mean PCE inflation rate is published by the Federal Reserve Bank of Dallas and is an alternative measure of core inflation in the price index for personal consumption expenditures (PCE).
- Source: U.S. Bureau of Economic Analysis (BEA); Federal Reserve Bank of Dallas; and US. Bureau of Labor Statistics (Current Population Survey and Job Openings and Labor Turnover Survey).

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## United States: Demand, output and prices

	2020	2021	2022	2023	2024	2025
<b>United States</b>	Current prices USD billion	Percentage changes, volume (2017 prices)				
<b>GDP at market prices</b>	21 322.9	5.8	1.9	2.4	1.5	1.7
Private consumption	14 206.2	8.4	2.5	2.2	1.5	1.6
Government consumption	3 178.3	0.3	-0.9	2.6	0.8	0.5
Gross fixed capital formation	4 602.4	5.3	0.9	1.4	1.7	3.4
Final domestic demand	21 986.9	6.6	1.7	2.1	1.5	1.8
Stockbuilding <sup>1</sup>	- 37.6	0.3	0.6	-0.3	0.1	0.0
Total domestic demand	21 949.3	6.9	2.3	1.8	1.6	1.8
Exports of goods and services	2 150.1	6.3	7.0	2.5	1.9	1.8
Imports of goods and services	2 776.5	14.5	8.6	-1.5	1.9	2.5
Net exports <sup>1</sup>	- 626.4	-1.2	-0.5	0.5	-0.1	-0.1
<i>Memorandum items</i>						
GDP deflator	—	4.6	7.0	3.8	2.7	2.1
Personal consumption expenditures deflator	—	4.2	6.5	3.9	2.8	2.2
Core personal consumption expenditures deflator <sup>2</sup>	—	3.6	5.2	4.2	2.7	2.2
Unemployment rate (% of labour force)	—	5.4	3.6	3.6	4.1	4.2
Household saving ratio, net (% of disposable income)	—	11.7	3.4	4.4	3.5	4.0
General government financial balance (% of GDP)	—	-11.5	-4.0	-7.8	-7.0	-7.0
General government gross debt (% of GDP)	—	124.8	119.8	120.9	123.8	127.1
Current account balance (% of GDP)	—	-3.5	-3.8	-3.1	-3.0	-3.1

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 114 database.

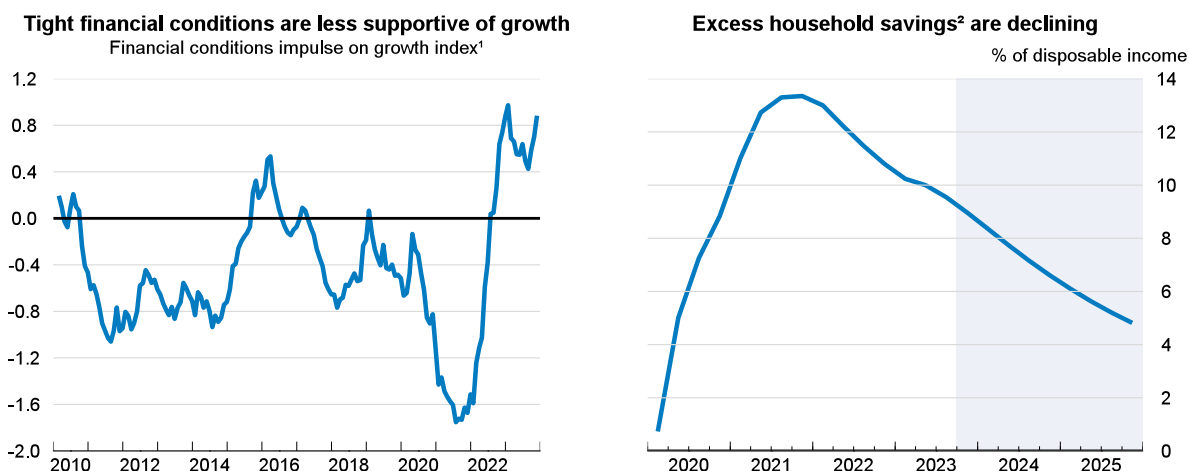
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## Growth has remained resilient and the labour market has eased

Real GDP growth remained robust in the first half of 2023 and strengthened in the third quarter to an annualised rate of 4.9%. After a period where labour demand growth outpaced labour supply, supply and demand are now more aligned, and job growth has continued at a moderate but slowing pace in 2023. The unemployment rate has edged up in recent months but remains low by historical standards. Measures of inflation have decreased since the beginning of 2023, though headline inflation has recently risen again due to higher energy prices. Still, core and headline inflation are elevated, with housing and services inflation putting upward pressure on core inflation.

International developments were supportive of growth in the first half of 2023 and net exports contributed positively to GDP growth, even as the dollar effective exchange rate remained elevated. Petroleum exports have risen to record levels in 2023. However, bilateral trade with China fell in the first half of the year. Exports to China are roughly flat but imports from China fell by 25% from a year earlier.


## United States 2



1. The figure shows the Financial Conditions Impulse on Growth computed with 3-year lookback window. Positive (negative) values of the index denote headwinds (tailwinds) to GDP growth over the next year.

2. Excess savings in 2020-2025 are estimated and projected using the 2015-2019 average household saving rate as a benchmark.

Source: Ajello, A., M. Cavallo, G. Favara, W. Peterman, J. Schindler, and N. Sinha (2023). "A New Index to Measure U.S. Financial Conditions," *FEDS Notes*. Washington: Board of Governors of the Federal Reserve System and OECD calculations.

StatLink  <https://stat.link/z9tka5>

## Monetary and fiscal policy will exert a contractionary influence in 2024

The federal funds rate is currently in the 5¼-5½ per cent range, which is near the expected peak of the tightening cycle that began in 2022, and is likely to remain elevated until the second half of 2024 given the anticipated persistence of core inflation. Recent increases in the 10-year bond yield—and the pass-through to private rates—have further tightened financial conditions. The OECD projections assume that cuts in the federal funds rate will begin in the third quarter of 2024, after inflation has fallen closer to the 2% target. The federal funds rate is projected to fall to around 4 to 4¼ per cent by the end of 2025 with the 10-year interest rate at a similar level.

Fiscal policy is expected to tighten in 2024 after an unexpected fiscal expansion in 2023, and be broadly neutral in 2025. Though extraordinary supports for households and businesses have mostly been unwound, the fiscal deficit increased in 2023 due to a combination of lower-than-expected tax receipts and higher-than-expected spending on mandatory social programs. Government net lending as a share of GDP is projected to be 7% in 2024 and gross debt will increase to 124 per cent of GDP in 2024, and rise further in 2025.

## Growth will be sluggish before recovering

Real GDP growth will slow to 1.5% in 2024 before increasing to 1.7% in 2025. More restrictive financial conditions due to tighter monetary policy will act as a headwind. The supportive effects of earlier rising asset prices and accumulated excess household savings are fading. Housing and business investment will slow through the first half of 2024. As demand slows, employment growth will ease further, and the unemployment rate will edge up. Inflation will continue to decline as core inflation eases due to a slowing economy, and as supply conditions ease further. As inflation subsides and monetary policy eases, consumption and investment growth are projected to pick up in the second half of 2024 and into 2025.

The outlook could surprise on the downside if the effects of tight financial conditions prove to be stronger than anticipated or if core inflation remains elevated, delaying any potential monetary policy easing. Banking sector stress in early 2023 has subsided, but volatility in bond markets may prove to be a stronger impediment to growth. In the near-term, a potential government shutdown would be a drag on growth until its resolution. However, the outlook could surprise on the upside if the labour market loosening continues without a rise in unemployment and declines in inflation continue unabated.

### **Policy should focus on durably reducing inflation and narrowing the deficit**

Monetary policy should remain tight until the Federal Reserve's inflation objectives are durably achieved, while continuing to assess the impact on real activity. Financial stability risks arising from the financial sector should continue to be closely monitored. Stronger efforts should be made to narrow the large budget deficit and put the government debt ratio on a downwards path to more sustainable levels. Population ageing will push future outlays higher, with increases in pension and health expenditures projected to rise by more than 3 percentage points of potential GDP by 2040. Adopting a solid medium-term focused framework to improve the sustainability of public finances would ease these pressures and create space for the funding of future productivity-enhancing projects, such as improvements to public digital infrastructure, and policies to achieve the climate transition.

# OECD Economic Outlook

The global economy continues to confront the challenges of persistent inflation and subdued growth prospects. GDP growth has been stronger than expected so far in 2023, but is now moderating as the impact of tighter financial conditions, weak trade growth and lower business and consumer confidence is increasingly felt. The slowdown is projected to be mild, with continued disinflation, but a growing divergence across economies is expected to persist in the near term. The Outlook underlines a range of risks, including the potential for disruptions to commodity markets and trade from heightened geopolitical tensions, uncertainty about the persistence of inflation, and the extent to which excess household savings will be run down. Key policy priorities are to ensure that inflation returns durably to target, address mounting fiscal pressures, revive global trade and improve the prospects for sustainable and inclusive growth in the medium term.

This issue includes an assessment of the global economic 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.

**Volume 2023/2**  
**No. 114, November**



**PRINT ISBN 978-92-64-92344-7**  
**PDF ISBN 978-92-64-65116-6**



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