FOREWORD

The global economic upswing that began around mid-2016 has become broader and stronger. This new *World Economic Outlook* report projects that advanced economies as a group will continue to expand above their potential growth rates this year and next before decelerating, while growth in emerging market and developing economies will rise before leveling off. For most countries, current favorable growth rates will not last. Policymakers should seize this opportunity to bolster growth, make it more durable, and equip their governments better to counter the next downturn.

Global growth seems on track to reach 3.9 percent this year and next, substantially above our October forecast. Helping to drive this output acceleration is faster growth in the euro area, Japan, China, and the United States, all of which grew above expectations last year, along with some recovery in commodity exporters. Along with China, several other emerging market and developing economies will also do better this year than in our past projections—that group includes Brazil, Mexico, and emerging Europe. The aggregate gains for this country group are, however, weighed down by sharp downward revisions for a few countries in the grip of civil strife, notably Libya, Venezuela, and Yemen. Growing trade and investment continue as notable factors powering the global upswing.

Growth this broad based and strong has not been seen since the world's initial sharp 2010 bounce back from the financial crisis of 2008–09. The synchronized expansion will help to dispel some remaining legacies of the crisis by speeding the exit from unconventional monetary policies in advanced economies, encouraging investment, and healing labor market scars.

Other aftereffects of the crisis seem more durable, however, including higher debt levels worldwide and widespread public skepticism about policymakers' capacity and willingness to generate robust and inclusive growth. That skepticism will only be reinforced—with negative political consequences down the road—if economic policy does not rise to the challenge of enacting reforms and building fiscal buffers. Success in such efforts would strengthen medium-term growth, spread its benefits lower in the income distribution, and build resilience to the hazards that lie ahead.

Future growth prospects look challenging indeed for advanced economies and many commodity exporters. In advanced economies, aging populations and lower projected advances in total factor productivity will make it hard to return to the precrisis pace for the average household's income growth. Substantially raising middle and lower incomes looks even tougher. Moreover, growth rates will inevitably bend toward their weaker longer-term levels. Policy support will fade in the United States and China—despite its necessity in view of those countries' macroeconomic imbalances. And countries that currently can grow more quickly by putting underutilized labor and capital back to work will reach full capacity. The need for a forward-looking policy perspective is therefore urgent—to limit risks as well as enhance growth.

As usual, Chapter 1 of this report sets out the risks to the forecast. These are balanced over the next several quarters, with the possibility of more buoyant growth than forecast balancing out unfavorable contingencies. But as time passes, the likelihood of negative shifts in the forecast rises.

Monetary policy might tighten sooner than expected if excess demand emerges, a notable possibility in the United States, where fiscal policy has turned much more expansive even as the economy has neared full employment. Financial tightening, in turn, would stress highly indebted countries, firms, and households, including in emerging market economies.

An escalating cycle of trade restrictions and retaliation is another risk. The first shots in a potential trade war have now been fired. Conflict could intensify if fiscal policies in the United States drive its trade deficit higher without action in Europe and Asia to reduce surpluses. The multilateral rules-based trade system that evolved after World War II and that nurtured unprecedented growth in the world economy needs strengthening. Instead, it is in danger of being torn apart.

The renewed popularity of nationalistic policies is another aftereffect of the financial crisis and its prolonged aftermath. Diminished prospects for household income growth in advanced economies, coupled with trends of higher polarization in jobs and incomes, have fueled a widespread political backlash hostile to traditional political modalities. If policymakers are complacent and do not tackle the challenge of strengthening long-term growth, political risks could intensify, possibly reversing some of the progress that economic reforms and integration have achieved to date.

The three analytical chapters in this *World Economic Outlook* are unified by their focus on central determinants of long-term economic growth.

Population growth, age distribution, and other structural employment trends are critical for understanding growth, investment, and productivity. Chapter 2 focuses on labor force participation in advanced economies, where population aging and, for many countries, declining overall participation rates are substantial headwinds to growth. Especially worrisome is the widespread decline in participation of young and prime-age men. The chapter shows how a range of policies—for example, educational investments and tax policies—can mitigate these effects. But participation will continue to decline even under best-practice approaches.

Chapter 3 focuses on the declining share of manufacturing employment globally and, most dramatically, in advanced economies. This structural transformation, driven by technology advances as well as globalization, has sparked popular concern about greater earnings inequality as "good jobs" disappear. Another worry is that currently poor countries may be trapped far from the global income frontier if they never pass through a developmental stage of substantial manufacturing employment. The chapter, however, suggests that services can offer considerable scope for productivity gain. Therefore, the best policy response is not to overrule market forces and subsidize manufacturing—possibly a zero-sum game globally—but instead to aim to raise productivity across the economy. The latter effort requires structural reforms, including lower barriers to services trade, along with many of the same investments in people that will enhance labor force attachment, as described in Chapter 2.

Finally, Chapter 4 studies the process through which innovative activity and technological know-how spread across national borders. Cross-border knowledge flows from technological leaders to poorer countries have historically been significant drivers of income convergence. Now, the emergence of China and Korea as leaders in some sectors offers the promise of positive repercussions for others, including the long-established high-income countries. International trade and competition, this chapter suggests, promote global knowledge diffusion and thus provide an important channel through which all countries can benefit from globalization. From this perspective, policies that restrict trade to prop up politically favored sectors of the economy will ultimately harm productivity growth.

Global growth is on an upswing, but favorable conditions will not last forever, and now is the moment to get ready for leaner times. Readiness requires not only cautious and forward-looking management of monetary and fiscal policies, but also careful attention to financial stability. Also necessary are structural and tax policies that raise potential output, including by investing in people and ensuring that the fruits of growth are widely shared. While there is much each country can do on its own, multilateral cooperation on a range of issues—stretching from trade to reducing global imbalances to cybersecurity to climate—remains essential.

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