The European Regional Economic Outlook in the Global Context

NOVEMBER 6, 2019

Poul M. Thomsen
Director of the IMF European Department
Key messages

- As in the rest of the world, Europe’s manufacturing and trade have weakened considerably.

- Europe’s slowdown is mostly externally driven. But signs of softness in investment have started to appear.

- Consumption has been resilient so far, reflecting still very strong labor markets.

- Growth has been weaker in advanced Europe, while it has been robust in emerging Europe excluding Russia and Turkey.

- A modest recovery is expected for 2020. Risks are on the downside.

- Policies:
  - Monetary policy to stay accommodative for longer, but vigilance about adverse side-effects.
  - Fiscal policy to be anchored by medium-term objectives with contingency plans for a severe downturn at hand.
  - Structural reforms remain vital.
As in the rest of the world, manufacturing and export sectors in the EU have weakened driven by vehicles and machinery.

Sources: Eurostat; IMF, GDS; and IMF staff calculations.
Note: EU exports are based on seasonally and working data adjusted data.
Europe’s slowdown is mainly due to industry, but services have started to soften

Sources: Eurostat; Haver Analytics; IHS Markit Purchasing Managers Survey; IMF, *World Economic Outlook*; and IMF staff calculations.

**Europe: Real Gross Value Added by Sector**
(Percentage points; growth in year-over-year percent change)

- Agriculture
- Construction
- Industry ex. Construction
- Services
- Real GVA growth

**European Union: Purchasing Managers; Index (PMI)**
(Index, seasonally adjusted, 50 += expansion)

Sources: Eurostat; Haver Analytics; IHS Markit Purchasing Managers Survey; IMF, *World Economic Outlook*; and IMF staff calculations.
Net exports are driving the slowdown, but investment has also started to weaken

---

Europe ex. Russia & Turkey: Contributions to Real GDP Growth
(Percentage points; growth in percent change)

- Residual
- Net exports
- Investment
- Public consumption
- Private consumption
- Real GDP growth

---

Europe: Trade Uncertainty Index and Business Confidence
(Index, 2014Q1=100)

- Business confidence
  (percent balance, 3-month moving average)
- Trade uncertainty
  (right scale)

---

Sources: Eurostat; Haver Analytics; IMF, World Economic Outlook; World Uncertainty Index (WUI); and IMF staff calculations.

Note: Europe Trade Uncertainty Index: higher values indicate higher uncertainty.
Resilience of consumption depends on labor markets

**European Union: Unemployment Rate**
(Percent, seasonally adjusted)

**European Union: Job Vacancies**
(Quarter-over-quarter percent change)

Sources: Eurostat; and IMF staff calculations.
Slowing growth in Advanced Europe (AE). Generally solid growth in Emerging Europe (EE)

Real GDP Growth
(Quarter-over-quarter percent change, annualized)

Sources: Haver Analytics; and IMF staff calculations.
A modest recovery is projected based on improving external demand. But risks are on the downside

### Real GDP Growth Projections
(Year-over-year percent change)

<table>
<thead>
<tr>
<th></th>
<th>Outturn</th>
<th>IMF Forecast</th>
<th>IMF Forecast</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2018</td>
<td>2019</td>
<td>2020</td>
</tr>
<tr>
<td>World</td>
<td>3.6</td>
<td>3.0</td>
<td>3.4</td>
</tr>
<tr>
<td>Europe</td>
<td>2.3</td>
<td>1.4</td>
<td>1.8</td>
</tr>
<tr>
<td>Advanced Europe</td>
<td>2.0</td>
<td>1.3</td>
<td>1.5</td>
</tr>
<tr>
<td>Euro area</td>
<td>1.9</td>
<td>1.2</td>
<td>1.4</td>
</tr>
<tr>
<td>Emerging Europe ex. Russia &amp; Turkey</td>
<td>4.3</td>
<td>3.7</td>
<td>3.1</td>
</tr>
</tbody>
</table>

**Memo: world trade volume (goods and services)**

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>3.6</td>
<td>1.1</td>
<td>3.2</td>
</tr>
</tbody>
</table>

Sources: IMF, *World Economic Outlook*; and IMF staff calculations.
Most European economies at or above full employment, but …

Output Gap, 2018 (Percent)

Output Gap, 2019 (Percent)

Sources: IMF, World Economic Outlook; and IMF staff calculations.
... almost all economies projected to have slower growth in 2019 versus 2018, creating a policy dilemma
With low inflation and wage pass-through, monetary policy to stay accommodative with heightened vigilance of adverse side effects.

**Projected End-2020 Inflation and Target Range**

(Percent)

- Advanced Europe
- Emerging Europe
- Upper & lower target limits
- Target

**Nominal Wage Growth and Inflation in the Newer EU Member States**

(Year-over-year percent change)

Sources: Eurostat; Haver Analytics; Central banks; BIS; IMF, *World Economic Outlook*; and IMF staff calculations.

Note: Newer EU members (NMS) include Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Lithuania, Latvia, Poland, Romania, the Slovak Republic, and Slovenia.
Fiscal policy guided by MTOs, but ready to act forcefully in case of a severe downturn

Considerations in favor of discretionary relaxation

- Slowing growth and downside risks
- Monetary policy approaching its limit
- Need to address supply-side bottlenecks
- Low/negative interest rates

Considerations against discretionary relaxation

- Still-strong labor markets and positive output gaps
- Projected recovery in 2020
- High sovereign debt levels
- Possibility of sudden reversal in yields
Structural reforms remain vital

**Nominal PPP GDP per Capita**
(Percent; relative to EU15)

**AE: Labor Productivity per Hour Worked**
(2018 US dollars)

**AE: Labor Productivity per Hour Worked**
(Index; relative to US)

Sources: The Conference Board Total Economy Database™ (Original version), April 2019; IMF, World Economic Outlook; and IMF staff calculations.
Imf.org/REOeurope

DOWNLOAD ME

SCAN ME