

An end to growth?

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This text relies on the 2016-2018 forecast for the global economy and the euro zone, the full version of which [is available here, in French](#).

After avoiding a Grexit in the summer of 2015, Europeans will now have to face a Brexit. In addition to what should be a significant impact on the UK economy lies the question of the effect this shock will have on other countries. Given that all the indicators seemed to be green for finally allowing the euro zone to recover from the double-dip recession following the 2007-2008 financial crisis and then the sovereign debt crisis, will a Brexit risk interrupting the trend towards a recovery? This fear is all the more credible as the delayed recovery was not sufficient to absorb all the imbalances that built up over the years of crisis. The unemployment rate for the euro zone was still over 10% in the second quarter of 2016. A halt to growth would only exacerbate the social crisis and in turn fuel doubt – and therefore mistrust – about Europe's ability to live up to the ambitions set out in the preamble to the [Treaty on the Functioning of the European Union](#) and reiterated in [Lisbon in 2000](#).

Nevertheless, despite fears of a new financial shock, it is clear that it hasn't happened. Brexit will of course be the fruit of a long process that has not yet started, but it seems that the worst has been avoided for now. The British economy will see growth halved in 2017. But the short-term negative effects on other euro zone countries should be fairly limited, except perhaps Ireland which is more interdependent on the United Kingdom. In any case the global recovery should continue, but growth will be down in the euro zone from 1.9% in 2015 to 1.3% in 2018.

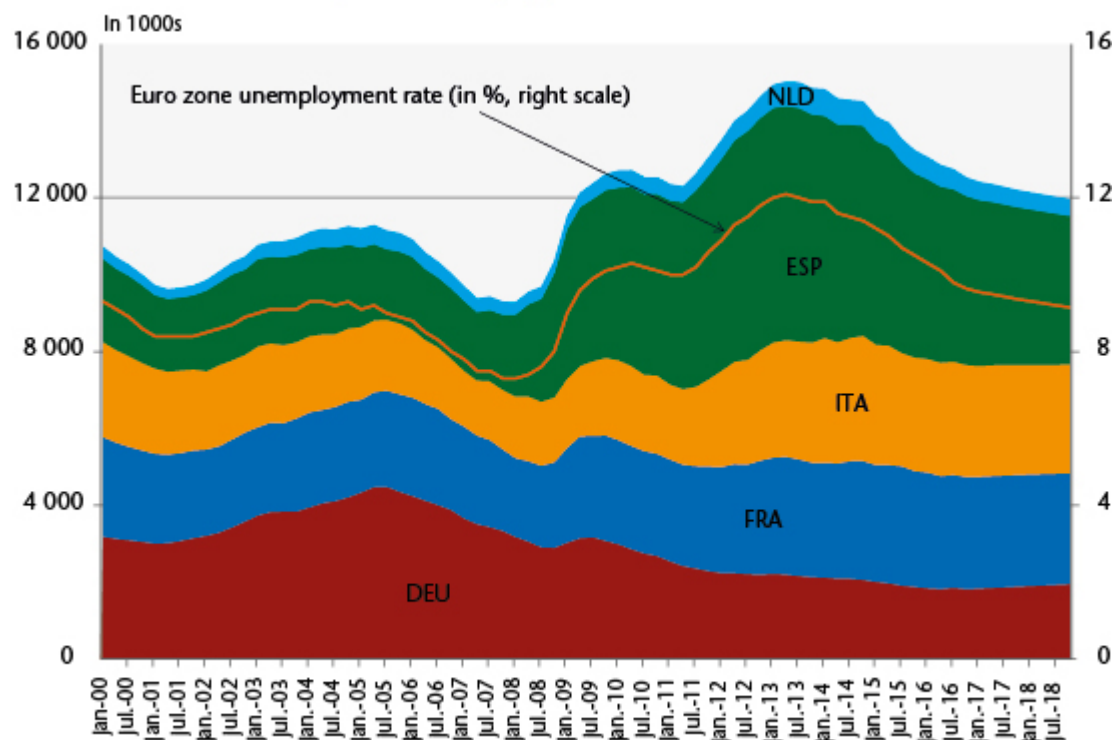
The many factors that helped initiate the recovery^[1] will to some extent lose steam. The price of oil has already begun to rise after hitting a low of under USD 30 in January 2016. It is now once again over 50 dollars a barrel. As for the euro, it has fluctuated since the beginning of the year at around 1.10 dollar, while in 2014 and 2015 it depreciated by 12.5% and 11.3%, respectively. In contrast, the European Central Bank has stuck to its expansionary monetary policy, and fiscal policy is much less restrictive than from 2011 to 2014. In 2015 and 2016, the aggregate fiscal impulse was even slightly positive.

Finally, world trade is slowing significantly, well beyond what would be expected simply from the change in China's economic model, which is resulting in a deceleration of imports. There were hopes that after the recovery kicked off, a virtuous cycle of growth would be triggered in the euro zone. Higher growth partly driven by exogenous factors would lead to job creation, higher incomes and better prospects for households and businesses. These elements would be conducive to a return of confidence and in turn stimulate investment and consumption. The dynamics of productive investment in France and Spain in the last quarter have given credence to this scenario.

The recovery will certainly not be aborted, but this rate of growth seems insufficient to reduce the imbalances brought about by long years of recession and low growth. At the end of 2018, the unemployment rate in the euro zone will still be nearly 2 percentage points higher than at end 2007 (graphic). For the five largest countries in the euro zone, this represents nearly 2.7 million additional people without jobs. In these conditions, it is undoubtedly the social situation of the euro zone which, even more than Brexit, is putting the European project in jeopardy. Europe certainly cannot be held solely responsible for low growth and high unemployment in the various countries, but the current forecast indicates that we

have undoubtedly not achieved the goals that were set in Lisbon in 2000, i.e. making the European Union “the most competitive and dynamic knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion”.

Figure: Unemployment in the euro zone



Source: Eurostat, OFCE forecasts – October 2016.

[1] View See the OFCE’s earlier [synthesis](#) (in French) of the international outlook (summarized [here](#) in English).

The euro zone quartered

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This text summarizes the [OFCE’s 2013-2014 forecast for the](#)

euro zone economy.

After six quarters of decline, GDP in the euro zone has started to grow again in the second quarter of 2013. This upturn in activity is a positive signal that is also being corroborated by business surveys. It shows that the euro zone is no longer sinking into the depths of depression. It would nevertheless be premature to conclude that a recovery is underway, as the level of quarterly growth (0.3%) is insufficient to cause any significant reduction in unemployment. In October 2013, the unemployment rate stabilized at 12% of the workforce, a record high. Above all, the crisis is leaving scars and creating new imbalances (unemployment, job insecurity and wage deflation) that will act as obstacles to future growth, especially in certain euro zone countries.

Several factors point towards a pick-up in economic activity that can be expected to continue over the coming quarters. Long-term sovereign interest rates have fallen, particularly in Spain and Italy. This reflects that the threat of a breakup of the euro zone is fading, which is due in part to the conditional support announced by the ECB a little over a year ago (see [Friends of acronyms: here comes the OMT](#)). Above all, there should be an easing of fiscal austerity, given that the European Commission has granted additional time to several countries, including France, Spain and the Netherlands, to deal with their budget deficits (see [here](#) for a summary of the recommendations made by the European Commission). Driven by the same mechanisms that we have already described in our previous forecasts, a little higher growth should follow this easing of austerity (-0.4 GDP point of fiscal effort in 2013, down from -0.9 point in 2013 and -1.8 in 2012). After two years of recession in 2012 and 2013, growth is expected to come to 1.1% in 2014.

Nevertheless, this growth will not be sufficient to erase the traces left by the widespread austerity measures implemented

since 2011, which pushed the euro zone into a new recession. In particular, employment prospects are improving only very slowly because growth is too weak. Since 2008, the euro zone has destroyed 5.5 million jobs, and we do not expect a strong recovery in net job creation. Unemployment could fall in some countries, but this would be due mainly to discouraged jobseekers withdrawing from the workforce. At the same time, less austerity does not mean that there will be no austerity. With the exception of Germany, fiscal consolidation efforts will continue in all the euro zone countries. And whether this is achieved through a reduction in public spending or an increase in the tax burden, households will bear the brunt of the adjustment. At the same time, the persistence of mass unemployment will continue to fuel the deflationary pressures already at work in Spain and Greece. The improved competitiveness that results in these countries will boost exports, but at the expense of increasingly undermining domestic demand. The impoverishment of the countries of southern Europe is going to be aggravated. Growth in these countries in 2014 will again be lower than in Germany, Austria, Finland and France (Table).

As a consequence, the euro zone will be marked by increasing heterogeneity, which could wind up solidifying public opinion in different countries against the European project and making the governance of the monetary union more difficult as national interests diverge.

Table. Growth in the euro zone

In %

	2013				2014				2012	2013	2014
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
DEU	0,0	0,7	0,2	0,3	0,3	0,4	0,4	0,4	0,9	0,9	1,5
FRA	-0,2	0,5	0,0	0,2	0,3	0,4	0,4	0,4	0,0	0,1	1,3
ITA	-0,6	-0,3	0,0	0,1	0,1	0,2	0,2	0,2	-2,4	-1,8	0,4
ESP	-0,4	-0,1	0,0	0,0	0,2	0,3	0,3	0,3	-1,6	-1,4	0,7
NLD	-0,4	-0,2	0,3	0,3	0,3	0,3	0,4	0,4	-1,3	-1,1	1,1
BEL	0,0	0,2	0,2	0,4	0,4	0,4	0,6	0,6	0,3	0,1	1,6
IRL	-0,6	0,4	0,2	0,3	0,4	0,4	0,4	0,4	0,1	-0,5	1,4
PRT	-0,4	1,1	0,0	0,2	0,2	0,3	0,3	0,3	-3,2	-1,7	1,0
GRC	1,1	9,6	0,5	-1,1	-3,9	1,2	1,3	1,5	-6,4	-4,1	-0,4
AUT	0,1	0,1	0,3	0,3	0,4	0,4	0,4	0,4	0,6	0,4	1,3
FIN	-0,2	0,2	0,3	0,4	0,4	0,5	0,5	0,5	-0,8	-0,9	1,7
EUZ	-0,2	0,3	0,1	0,2	0,3	0,4	0,4	0,4	-0,6	-0,3	1,1

Sources : Eurostat, OFCE calculations and forecasts, October 2013.