



**What is the economic outlook
for OECD countries?**

An interim assessment

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Press Briefing
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1. Economic momentum on both sides of the Atlantic somewhat unexpectedly weakened in late 2005, but is now back in line, by and large, with the *Economic Outlook* projections released three months ago. Indeed, against the background of high and volatile energy prices but still intriguingly low long-term interest rates, activity is estimated to have reaccelerated. However, some of the factors that have thus far sustained buoyant overall growth may no longer do so further out. As highlighted on earlier occasions, one source of risk in this regard stems from stretched valuations in some housing markets.

2. The marked economic slowdown in the United States in the fourth quarter of 2005 reflected the adverse one-off effects of the late summer hurricanes rather than fading underlying strength. In Canada, where no such disruption occurred, growth has remained resilient. Recent US data point to a sharp rebound in the first quarter of this year, even after taking into account that unseasonably mild weather in January boosted retail sales and some of the other high-frequency indicators. Job creation has remained robust and business confidence is consistent with above-par growth in the near term.

3. Helped by the vigour of the expansion throughout much of Asia, Japan is now enjoying a broad-based recovery, with a strong year-average performance, at 2.8% in 2005. This recovery was initially driven by exports and business fixed investment, but household spending, including residential investment, has since gathered momentum. Corporations are starting to re-leverage and surveys bode well for continued dynamism over the coming months, albeit with some deceleration from the rapid pace recorded in the last quarter of 2005.

4. The euro area stands out in that “hard” indicators continue to paint a distinctly weaker picture than the “softer” but more forward-looking survey information. This is particularly striking in the three largest economies, and especially in Germany, where activity stalled in late 2005 but where business confidence has reached very high levels, particularly in export-oriented sectors. In the industries that depend more heavily on domestic demand, including in construction and retailing, German firms’ confidence is also improving, although less spectacularly and from a lower base. In the service sector at large, however, confidence remains weak, consistent with still lacklustre labour markets and very subdued wages. All in all, the strong external side should feed through to euro area domestic demand and a rebound can be expected in the first half of 2006. Even so, by mid-year, the euro-area wide output would still be significantly below potential. In the United Kingdom, activity is set to continue to grow at around its potential rate.

5. Against this backdrop, monetary accommodation has now essentially been removed in the United States. However, with limited if any economic slack left and some pressures on costs there may be a case for limited further tightening, subject to the incoming data, including the evolution of house prices. Japan may be at long last exiting deflation, but only very gradually so, despite vigorous growth, which argues for keeping the policy interest rate at zero over the near term. In the euro area, where core inflation remains subdued, headline inflation is reverting to target. Further out, removal of monetary accommodation should be based on unambiguous signs that slack is shrinking and that underlying inflation pressures are mounting.

6. On the fiscal front, consolidation generally remains an overarching imperative, notwithstanding some positive revenue surprises in recent months. Indeed, in cyclically-adjusted terms, the general government deficit in the G7 countries as a group exceeded 3½ per cent of GDP in 2005 for the fourth year in a row. This would call for serious adjustment efforts even in the absence of the fiscal pressures associated with ageing populations, which – despite the pension and health care reforms implemented over the past few years – are continuing to build up.

GDP growth in the G7 economies ¹
in %

	Quarter-on-quarter growth seasonally-adjusted						Year-average growth in 2005	
	05Q1	05Q2	05Q3	05Q4	06Q1	06Q2	Actual	EO78 projection
United States	0.9	0.8	1.0	0.4	1.1 (+/- 0.4)	0.9 (+/- 0.5)	3.5	3.6
Japan	1.5	1.3	0.3	1.4	0.7 (+/- 0.5)	0.5 (+/- 0.6)	2.8	2.4
Euro area	0.3	0.4	0.7	0.3	0.6 (+/- 0.3)	0.6 (+/- 0.3)	1.3	1.4
Germany	0.6	0.3	0.6	0.0	0.6 (+/- 0.5)	0.4 (+/- 0.5)	1.1	1.1
France	0.3	0.0	0.7	0.2	0.5 (+/- 0.4)	0.5 (+/- 0.5)	1.4	1.6
Italy ²	-0.5	0.7	0.3	-0.4	0.4 (+/- 0.4)	0.3 (+/- 0.4)	0.0	0.2
United Kingdom	0.2	0.5	0.5	0.6	0.5 (+/- 0.3)	0.6 (+/- 0.3)	1.8	1.7
Canada	0.5	0.9	0.9	0.6	0.8 (+/- 0.4)	0.8 (+/- 0.5)	2.9	3.0
G7	0.8	0.7	0.7	0.5	0.8 (+/- 0.3)	0.7 (+/- 0.3)	2.6	2.6

1. Based on GDP releases and high-frequency indicators published by 3 March 2006. Seasonally and in some cases also working-day adjusted. Aggregations for the G7 use 2000 purchasing-power-parity weights. Associated ± 1 standard error ranges are in parentheses.

2. The 05Q4 estimate is the outturn implied by the published data for 05Q1-Q3 and the official estimate of zero year-average growth in 2005.

Energy prices remain high and volatile

West Texas Intermediate (WTI) crude oil prices

Current dollars per barrel, daily observations



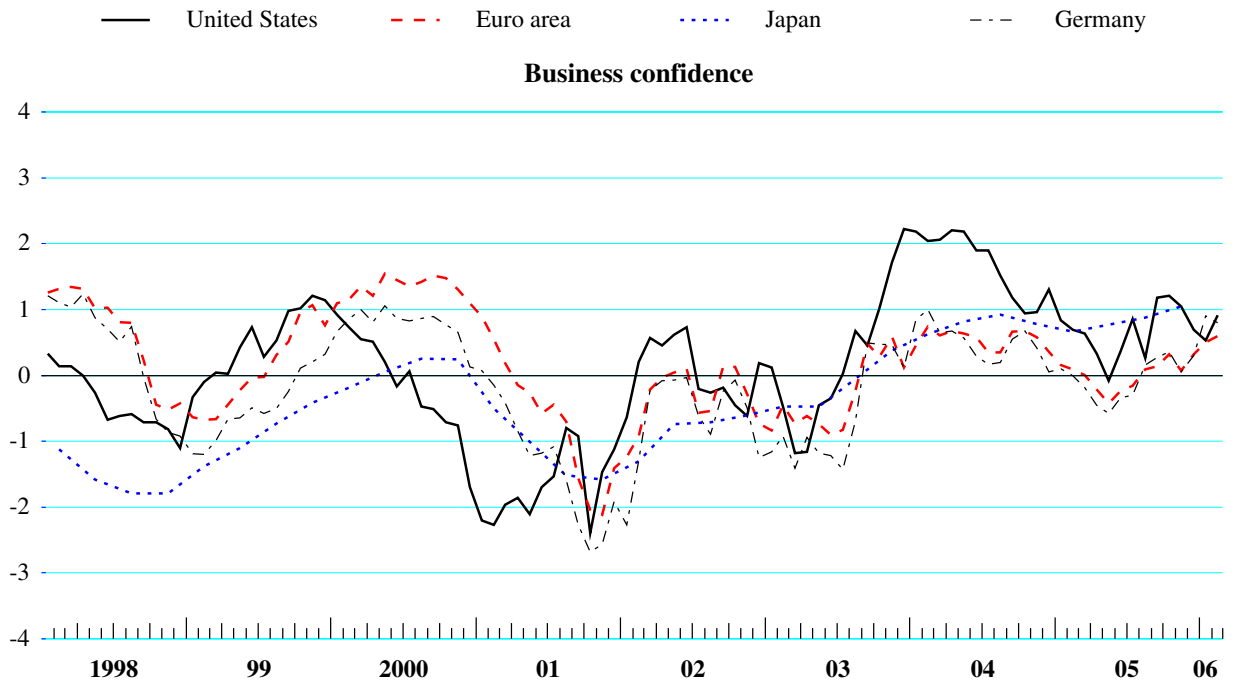
Natural gas spot price in the United States

Henry Hub - Dollars per MMBTU

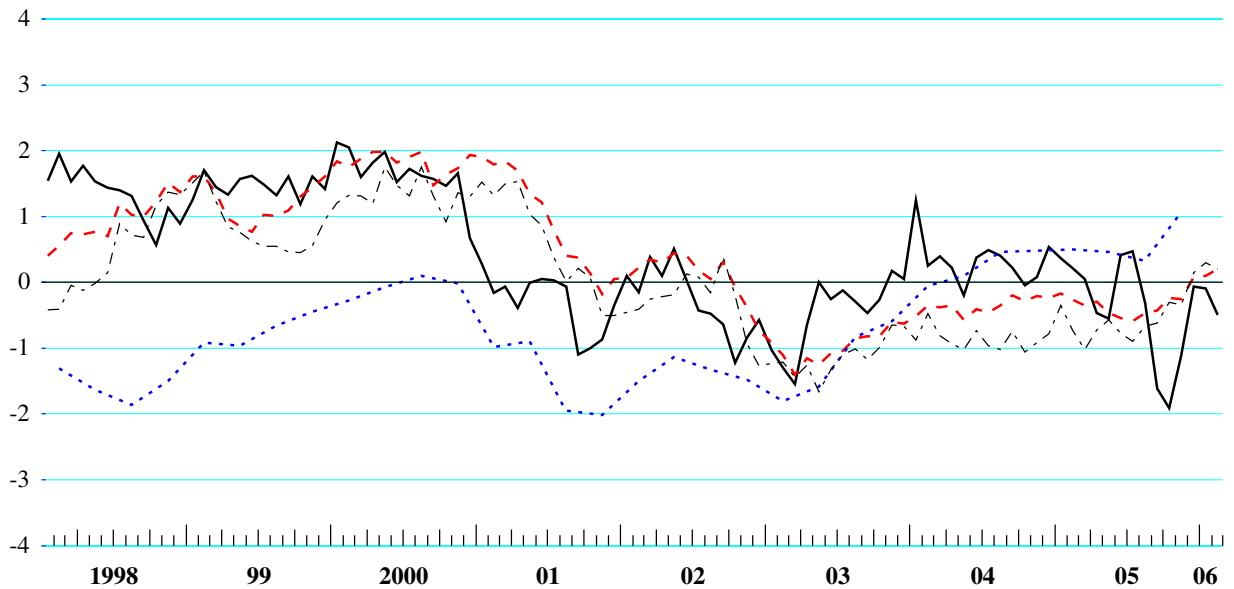


Source: US Energy Information Agency and Datastream.

Confidence is picking up in the euro area and Japan

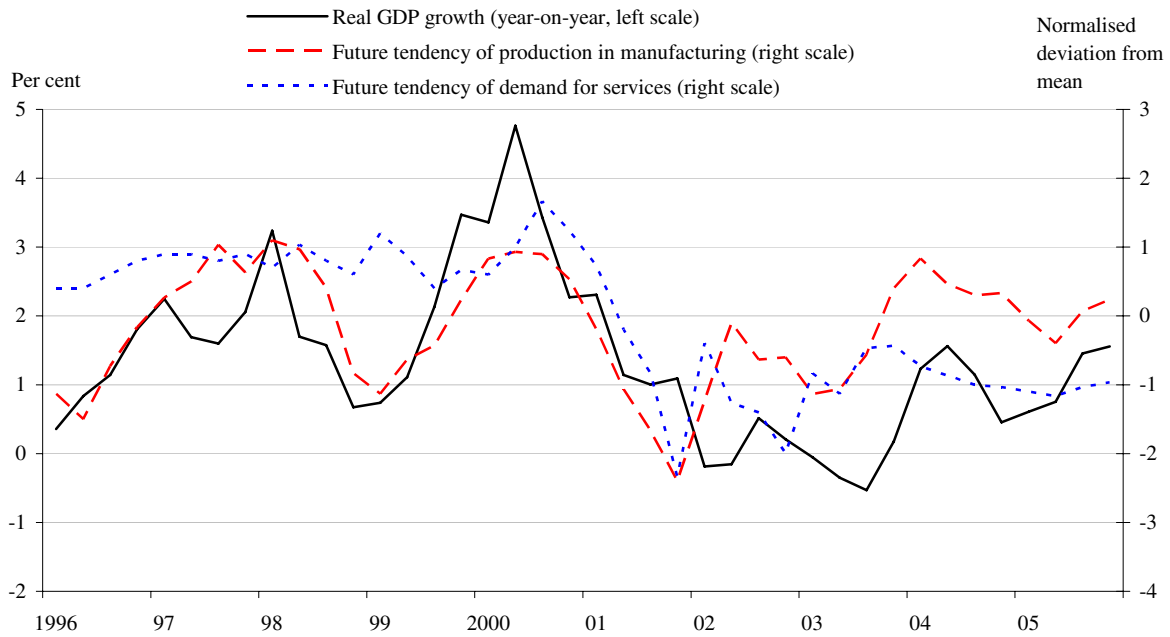


Consumer confidence

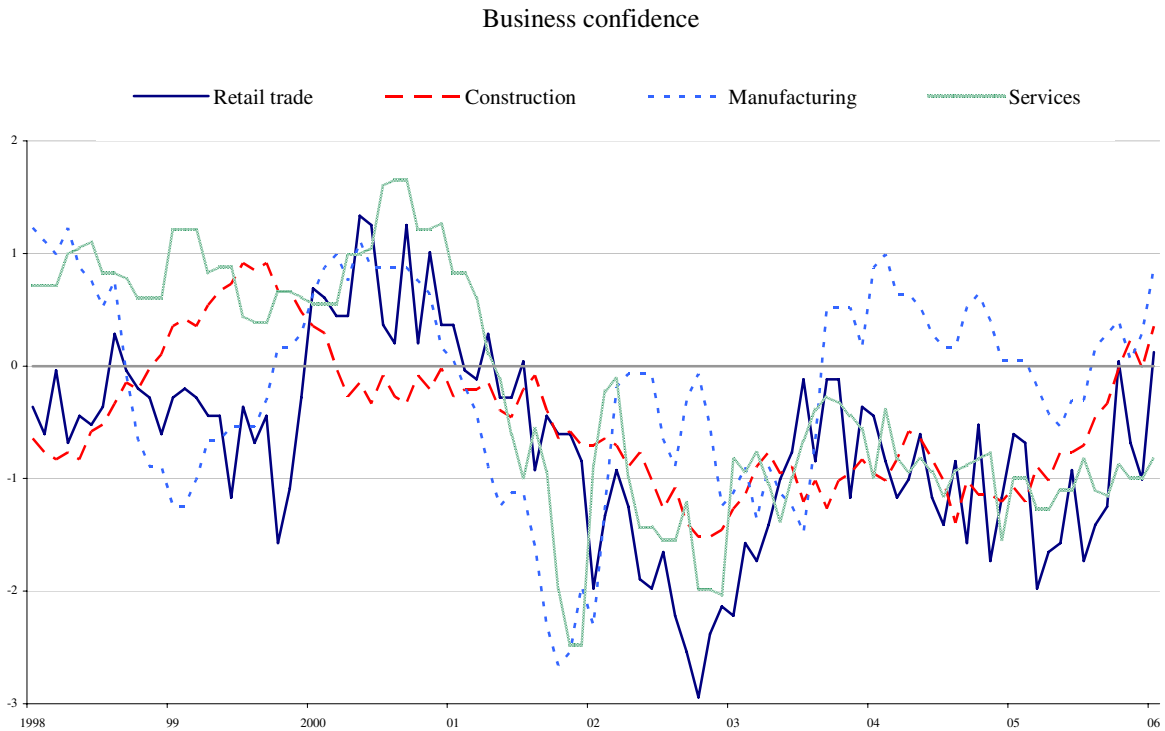


All series have been normalised at the average for the period starting in 1985 and are presented in units of standard deviation.
Source: OECD Main Economic Indicators.

**However, over the past few years, there is some disconnect
between hard and soft data in Germany...**



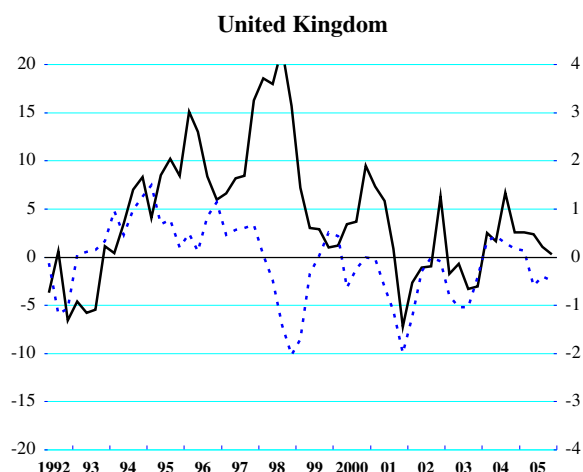
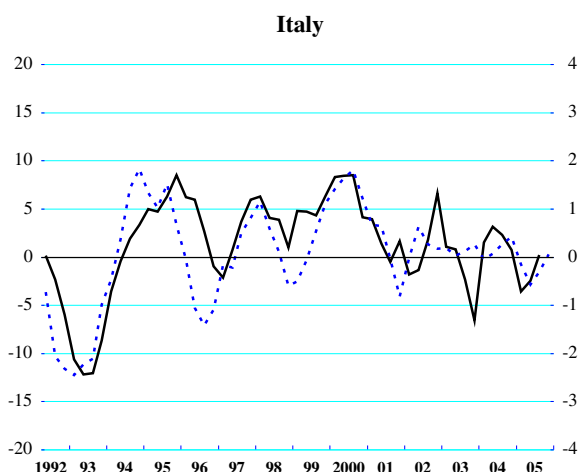
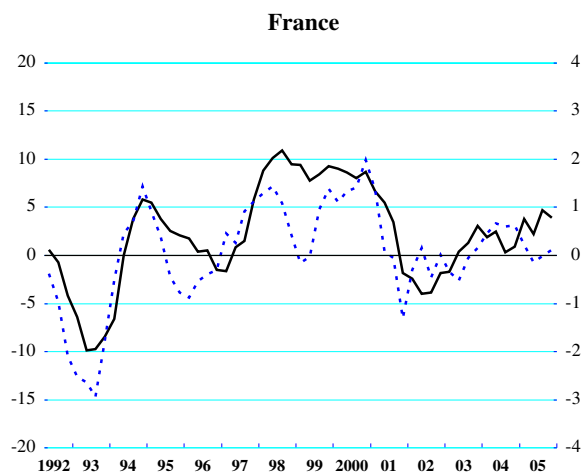
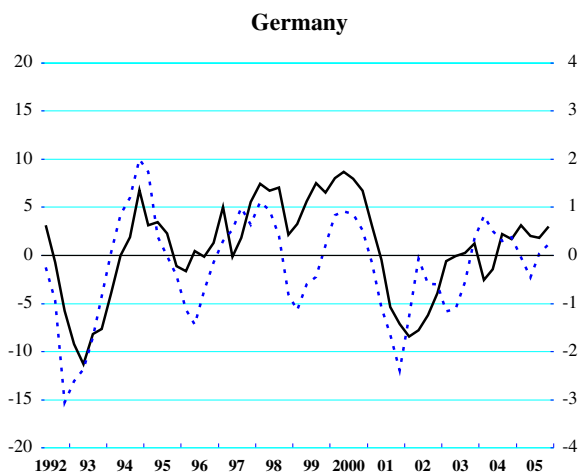
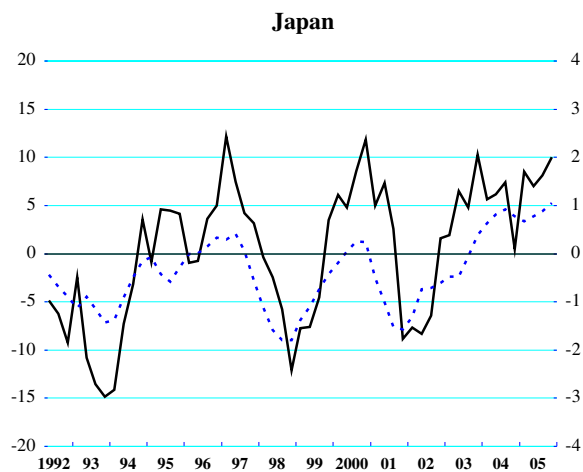
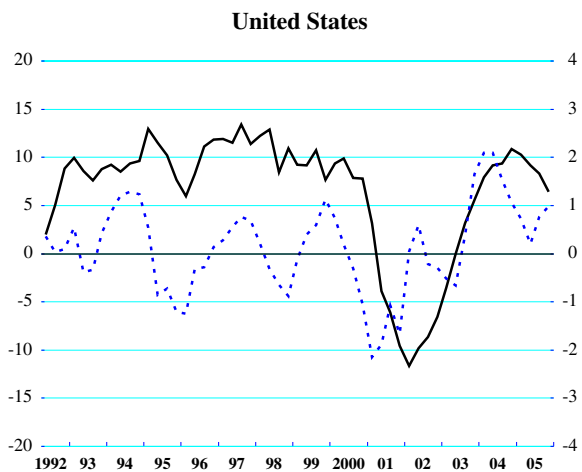
...where confidence is improving in construction and retailing but not yet in services



Source: Eurostat, OECD Main Economic Indicators and OECD Quarterly National Accounts.

Investment is accelerating in the euro area and Japan

— Business sector fixed investment (year-on-year percentage change in volume, left scale)¹
 - - - - Business confidence (right scale)²



1. Total fixed investment for Italy.

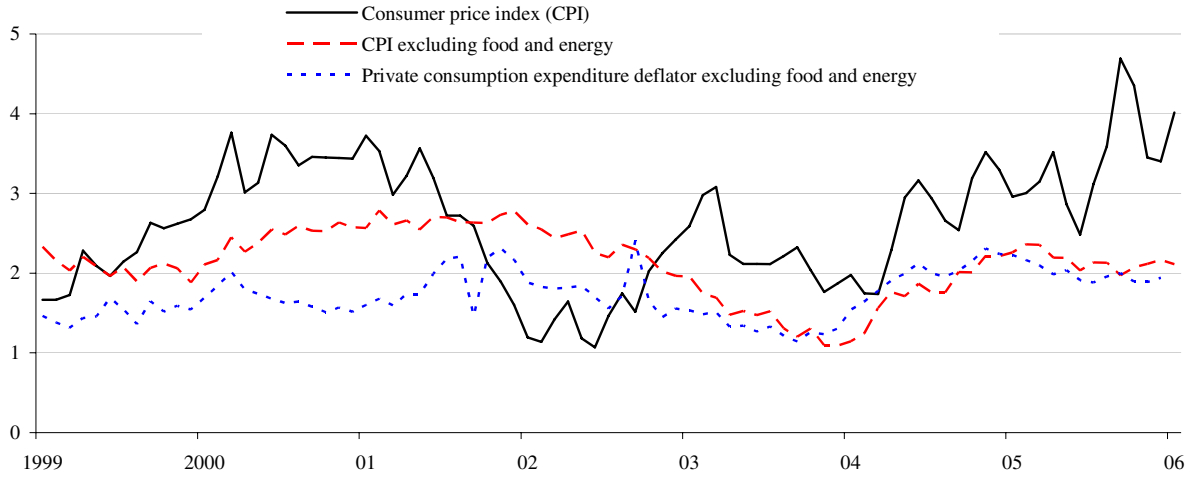
2. Business confidence has been normalised at the average for the period starting in 1985 and are presented in units of standard deviation.

Source : OECD Economic Outlook database.

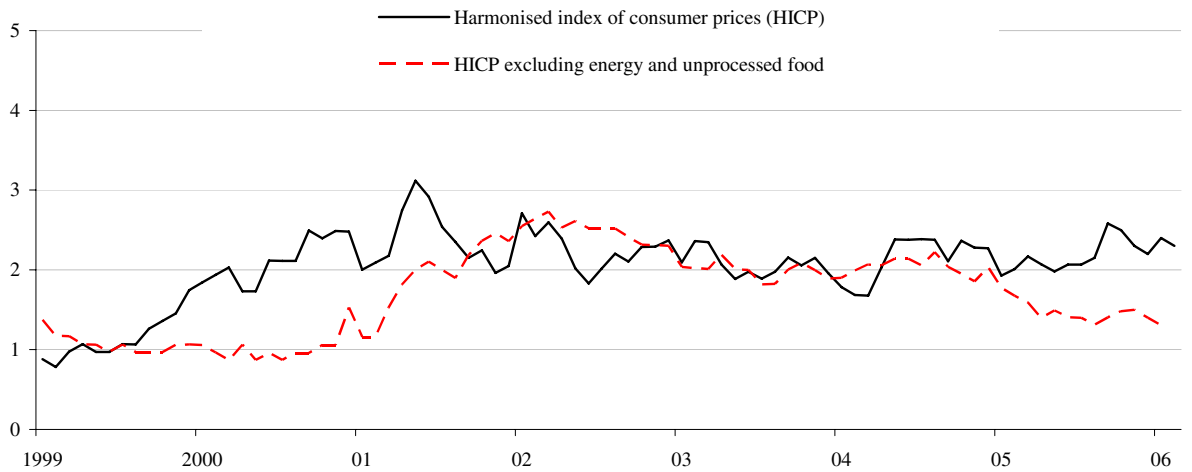
Core inflation remains in check

Year-on-year percentage change

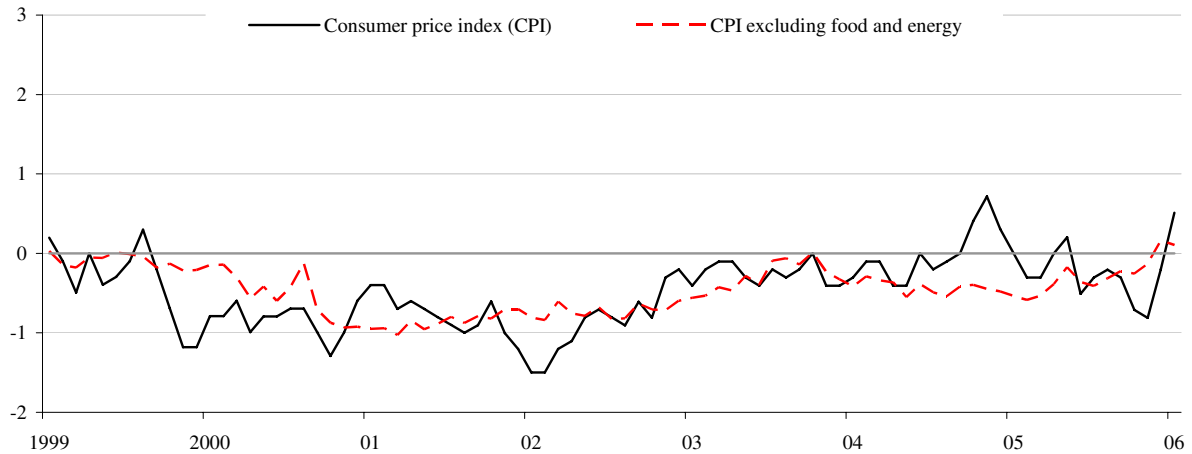
United States



Euro area



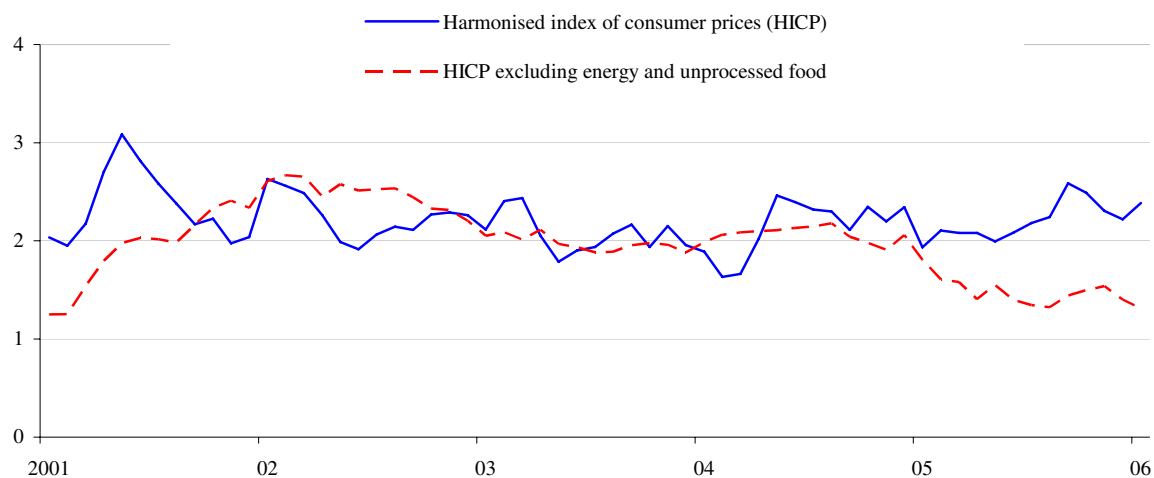
Japan



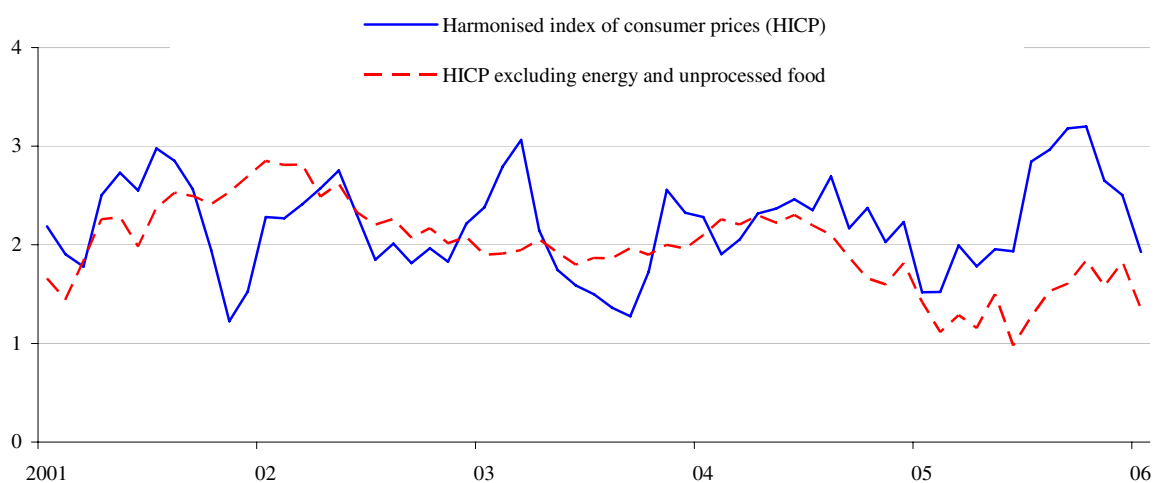
Source: OECD Main Economic Indicators.

In the euro area, headline inflation is reverting quickly to target

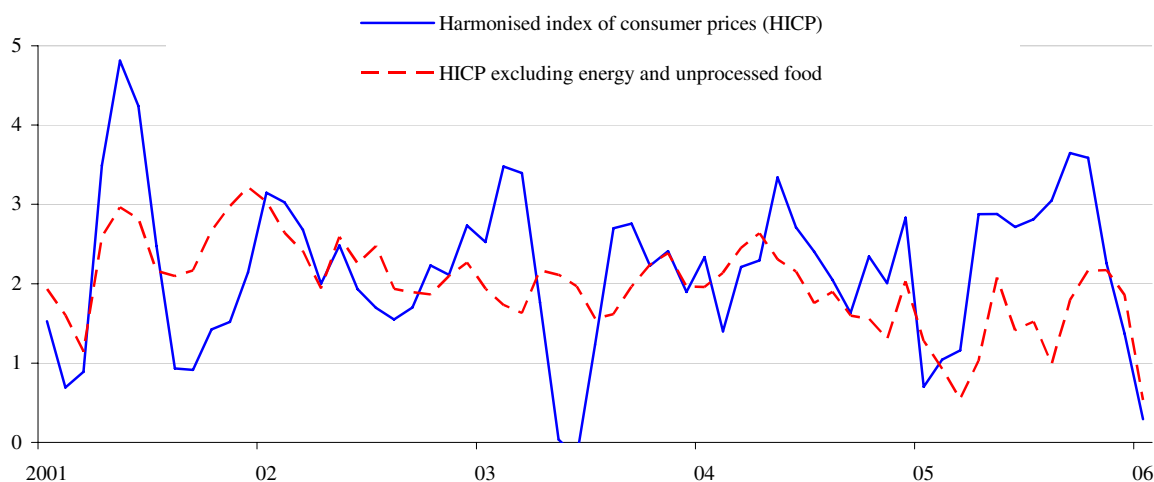
year-on-year percentage change in headline and core price indices



6-month annualised inflation rates



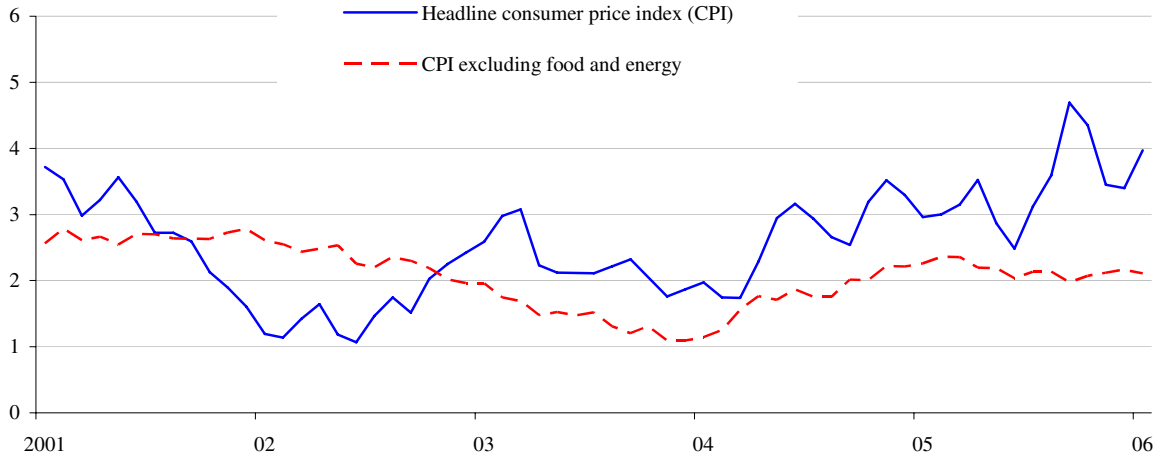
3-month annualised inflation rates



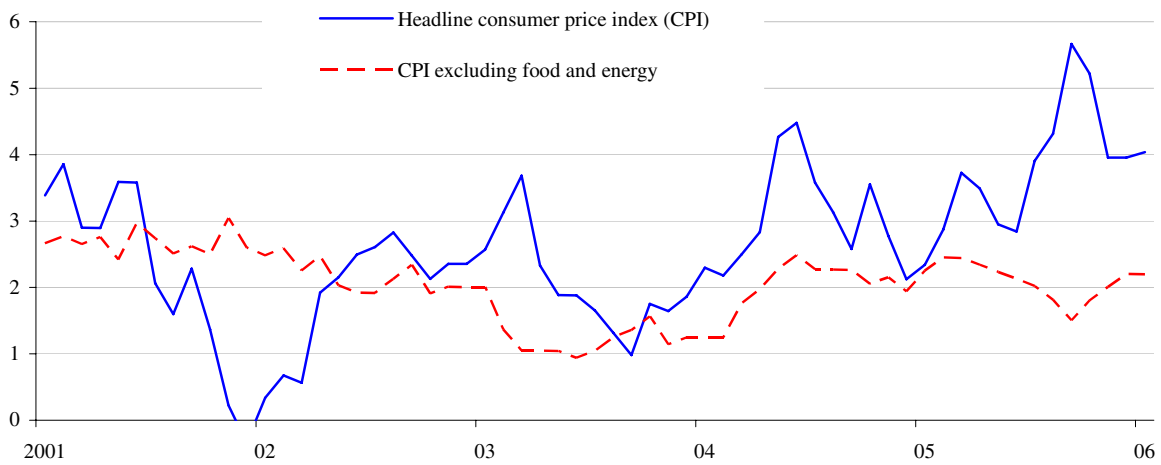
Source: OECD Main Economic Indicators.

Core inflation is higher in the United States

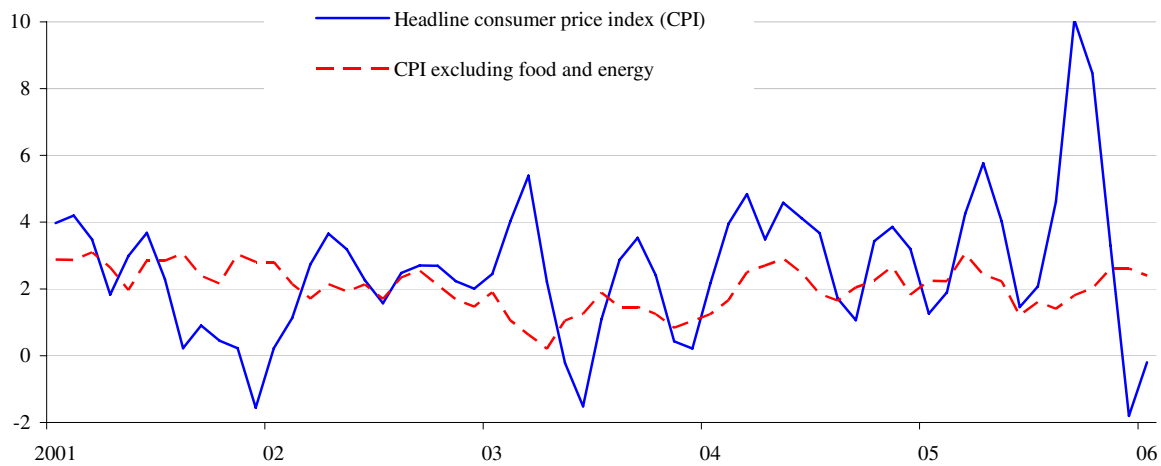
year-on-year percentage change in headline and core price indices



6-month annualised inflation rates

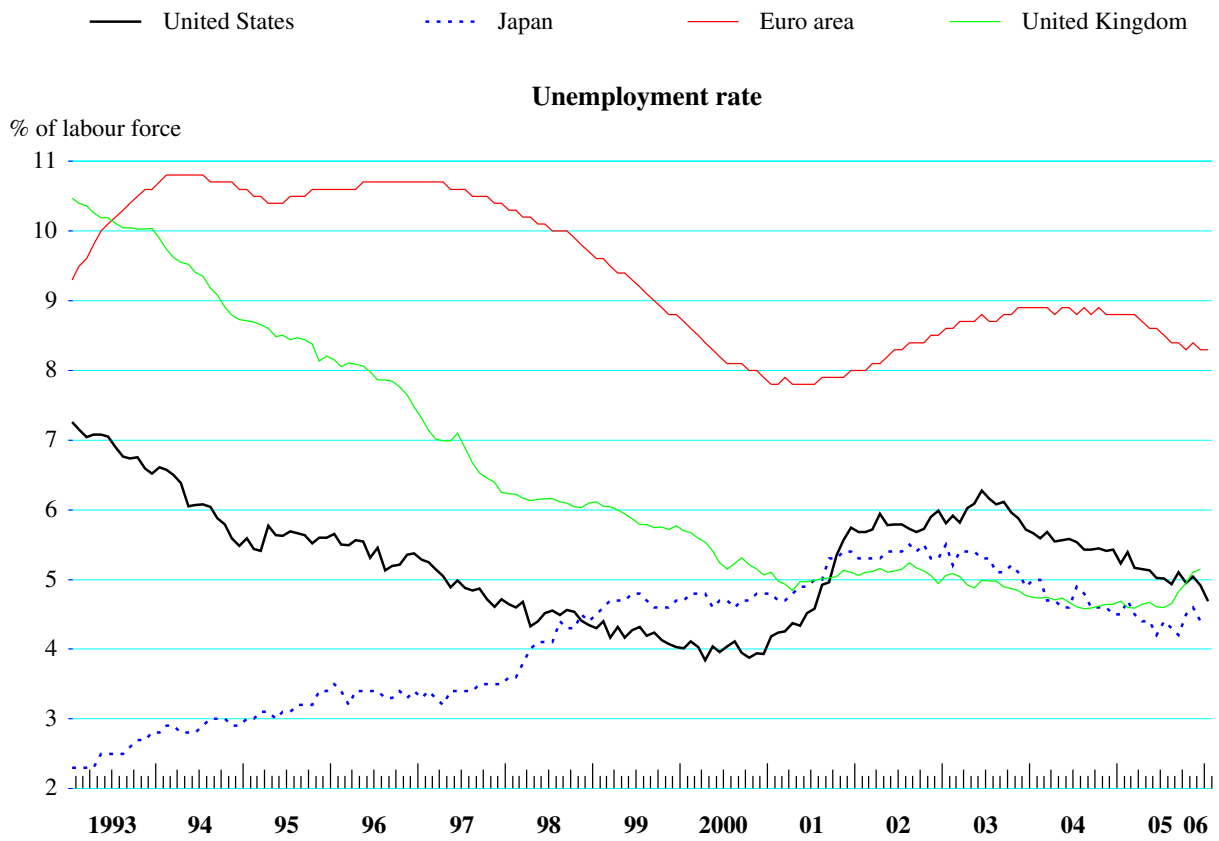


3-month annualised inflation rates



Source: OECD Main Economic Indicators.

The unemployment rate remains high in the euro area



Source: OECD Main Economic Indicators.