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PRE-RELEASE

# World Economic Situation and Prospects 2010

## Global outlook



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## Pre-Release

This is a pre-release of Chapter I of the World Economic Situation and Prospects 2010, issued on 2 December 2009 in New York. The full report, including regional overviews and a detailed analysis of trends in global trade and finance will be available from the second full week of January 2010

For further information, please see http://www.un.org/esa/policy or contact:

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## Macroeconomic prospects for the world economy

The global economy is recovering with the support of massive fiscal stimuli …

The world economic situation has been improving since the second quarter of 2009. Global equity markets have rebounded and risk premiums on lending have fallen. International trade and global industrial production have also been recovering noticeably, with an increasing number of countries registering positive quarterly growth of gross domestic product (GDP). The economic revival has been driven in no small part by the effects of the massive policy stimuli injected worldwide since late 2008. It also reflects strong cyclical inventory adjustment.

… but the recovery is uneven and conditions for sustained growth remain fragile

This is an important turnaround after the free fall in world trade, industrial production, asset prices and global credit availability which threatened to push the global economy into the abyss of a new great depression in early 2009. Yet, the recovery is uneven and conditions for sustained growth remain fragile. Credit conditions are still tight in major developed economies, where many major financial institutions need to continue the process of deleveraging and cleansing their balance sheets. The rebound in domestic demand remains tentative at best in many economies and is far from self-sustaining. High unemployment rates and the large output gap in most countries, along with a number of other factors, such as the possibility of a further spread of pandemic influenza A (H1N1) that could hurt economic activity, continue to pose challenges for policymakers worldwide. In addition, the global macroeconomic imbalances, which were part of the problem in the first instance, could widen again to form a source of renewed financial instability.

In 2010, global growth will remain below potential and unemployment will stay high

In the outlook, global economic recovery is expected to remain sluggish, unemployment rates will stay high and inflation will remain low. Developing countries, especially those in Asia, are expected to show the strongest recovery in 2010. Nonetheless, growth is expected to remain well below potential and the pre-crisis levels of performance in the developing world. As a consequence, it will take more time and greater efforts to make up for the significant setbacks in the progress towards poverty reduction and the fight against hunger, as well as the other Millennium Development Goals (MDGs). The crisis has impacted severely on low-income countries and the most vulnerable. Even given the signs of economic recovery, many are still facing declines in household incomes, rising unemployment, and the effects of dwindling government revenue on social services. Where these adverse impacts cannot be countered because of weak social safety nets and lack of fiscal space to protect social spending and promote job creation, there is a high risk of long-lasting setbacks in human development.

The most pressing policy challenges include maintaining the momentum towards recovery and rebalancing global growth

While necessary, the fiscal and monetary stimulus policies undertaken to counteract the crisis have at the same time become a source of concern. Some Governments fear that the rapid build-up of public debt could affect economic growth in the longer run and are calling for an exit of the policy stimuli. However, as global demand is still weak, a premature withdrawal of those measures could abort the incipient recovery. Going forward, the most pressing policy challenges over the near term include maintaining the momentum of economic recovery through economic stimulus measures and rebalancing global growth towards a more sustainable path so as to avoid a re-emergence of the global imbalances, while, at the same time, facilitating high growth, especially for developing countries, and addressing the climate change challenge. Achieving all this may require even farther-reaching and unprecedented internationally concerted actions than those that have already been undertaken by the international community since October 2008.

## Growth prospects

Mild growth is forecast for 2010

After a sharp and synchronized global downturn—indeed the only contraction since the Second World War—the world economy is improving. An increasing number of economies showed positive growth in the second quarter of 2009, and momentum towards recovery continued to build in the third quarter. Nonetheless, because of the steep downturn at the beginning of the year, world gross product (WGP) is estimated to fall by 2.2 per cent for 2009. Premised on the assumption of a continued supportive policy stance worldwide (box I.1), a mild growth of 2.4 per cent is forecast in the baseline scenario for 2010 (table I.1 and figure I.1). According to this scenario, the level of world economic activity will be 7 per cent below where it might have been had pre-crisis growth continued.

The rebound was built around three factors

In most countries, the economic rebound has been built around three factors in particular. The first of these consists of the massive, and to some extent concerted, policy actions taken by the major economies, which effectively arrested a further erosion of confidence worldwide (for further discussion, see the section on policy responses below). The second relates to a change in the global inventory cycle. The early stages of the recession were characterized by panic-driven shedding of inventories accompanied by cutbacks in industrial production. Following some stabilization of financial markets and improvement in consumer and business confidence, companies started to resume production and restock inventories. This explains much of the rebound in global trade and industrial production. The third factor relates to the international repercussion effects of the first two.

Japan and developing Asia are leading the rebound

Consistent with this pattern, the strongest declines in export volumes and industrial production indices were seen among major manufacturing exporters, especially those in Asia. Following the turn in the inventory cycle, Japan and developing Asia are also leading the rebound in trade and production. The recovery in industrial production, in turn, has allowed for renewed growth in the demand for primary commodities and a rebound in world commodity prices. However, the pace of recovery is still rather uneven across countries. Furthermore, in so far as it is not also based on a resumption of growth in private investment and consumption, recovery may not be lasting.

Consumer and investment demand in developed economies remain subdued

In developed economies, consumer and investment demand remain subdued as a result of the continued rise in unemployment rates, the wealth losses incurred during the crisis and the desire of households and firms to rebuild balance sheets. Domestic demand is further constrained by continued tightness in credit supplies, despite more stable conditions in financial markets. Another important factor is that the impetus from the stimulus measures and the turn in the inventory cycle are expected to diminish over time. The economy of the United States of America is expected to grow by 2.1 per cent in 2010, following an estimated downturn of 2.5 per cent in 2009. Recovery in both the European Union (EU) and Japan is projected to be much weaker, reaching GDP growth of no more than 0.5 and 0.9 per cent, respectively, in 2010. At this pace of recovery, the major developed economies are not expected to provide a strong impetus to global growth in the near term.

Box I.1

## Main assumptions for the baseline forecast

The forecast presented in the text is based on the United Nations Global Forecasting Framework (GFF) in conjunction with Project LINK, a network of institutions and researchers supported by the Department of Economic and Social Affairs of the United Nations. It is informed by provisional individual country forecasts submitted by country experts, which are adjusted based on harmonized global assumptions and the imposition of global consistency rules (especially those of trade flows, by both volume and value) provided by the GFF. The main global assumptions are discussed below. The baseline forecast does not include any specific assumption about the international coordination of macroeconomic policies. It is also assumed that except for these assumptions there are no other exogenous shocks to the global economy. For alternative scenarios to the baseline, see the sections in the main text on risks and uncertainties and on policy challenges.

***Monetary policy***

Given the complex structure of the monetary policy measures adopted by major economies during the global recession, the assumptions regarding policy interest rates are indicative only of the nature of the policy stance in the outlook. The United States Federal Reserve (Fed) is assumed to hold its main policy interest rate, the federal funds rate, at its current range of 0.0-0.25 per cent until the end of the third quarter of 2010, after which it embarks upon a slow process of policy normalization, with an increase of 50 basis points during the last quarter. The European Central Bank (ECB) is also assumed to hold its main policy rate, the interest rate on its main refinancing operations, at the current level of 1.00 per cent through the third quarter of 2010, and then raise it by 50 basis points in the fourth quarter. The Bank of Japan (BOJ) is assumed to hold its policy rate, the target Uncollateralized Overnight Call Rate, at its current 0.10 per cent until the end of 2010.

During the forecast period, the central banks in the major economies will continue to rely on adjusting the unconventional measures that are already in place to manage liquidity in their economies, and it is assumed they will initiate a gradual withdrawal of some of these measures in the second half of 2010 (see chapter IV for details at the country level).

***Fiscal policy***

Fiscal assumptions are made at the country level by the LINK country experts, but they typically reflect currently announced packages and are assumed to be fully implemented. In the current situation, automatic stabilizers are assumed to operate unconstrained, except in those countries experiencing severe financial distress (see chapter IV for details at the country level).

***Exchange-rate movements***

The United States dollar appreciated against the euro to about $1.25 in the first quarter of 2009, but has since depreciated significantly, averaging $1.43 per euro in the third quarter and hovering around $1.48 or higher since late September. The dollar also saw a rebound against the Japanese yen in the first quarter of 2009, but has similarly lost ground since. It averaged ¥94 per dollar in the third quarter and was close to ¥91 in September 2009. In the outlook, it is assumed that the dollar, while experiencing significant volatility, will stay in a trading range centred at $1.44 against the euro and close to ¥90 per dollar through 2010.

***Oil and other commodity prices***

Brent oil prices are expected to average about $61 per barrel in 2009 and to rise on average to $72 for the year 2010, for reasons explained in chapter II. For non-oil commodity prices, detailed assumptions at the individual commodity level are made for a large group of commodities, based on individual market conditions and reflecting other global assumptions. The weighted dollar price index of these non-oil commodities is estimated to have fallen by 18.4 per cent in 2009 and is assumed to increase by a further 4.6 per cent in 2010.

Table I.1
**Growth of world output, 2004–2010**

Annual percentage change

| | 2004 | 2005 | 2006 | 2007 | 2008 | 2009[a] | 2010[b] | Change from United Nations forecast of June 2009[c]: 2009 | Change from United Nations forecast of June 2009[c]: 2010 |
|---|---|---|---|---|---|---|---|---|---|
| **World output[d]** | **4.0** | **3.5** | **4.0** | **3.9** | **1.9** | **-2.2** | **2.4** | **0.4** | **0.8** |
| ***of which:*** | | | | | | | | | |
| Developed economies | 3.0 | 2.5 | 2.8 | 2.6 | 0.5 | -3.5 | 1.3 | 0.4 | 0.7 |
| Euro zone | 2.2 | 1.7 | 3.0 | 2.7 | 0.7 | -4.1 | 0.4 | -0.4 | 0.5 |
| Japan | 2.7 | 1.9 | 2.0 | 2.3 | -0.7 | -5.6 | 0.9 | 1.5 | -0.6 |
| United Kingdom | 3.0 | 2.2 | 2.9 | 2.6 | 0.6 | -4.5 | 0.6 | -0.8 | 0.8 |
| United States | 3.6 | 3.1 | 2.7 | 2.1 | 0.4 | -2.5 | 2.1 | 1.0 | 1.1 |
| Economies in transition | 7.7 | 6.5 | 8.0 | 8.4 | 5.5 | -6.5 | 1.6 | -0.6 | 0.2 |
| Russian Federation | 7.2 | 6.4 | 7.7 | 8.1 | 5.6 | -7.0 | 1.5 | -0.2 | 0.0 |
| Developing economies | 7.3 | 6.7 | 7.3 | 7.6 | 5.4 | 1.9 | 5.3 | 0.5 | 1.0 |
| Africa | 6.5 | 5.9 | 5.9 | 6.0 | 4.9 | 1.6 | 4.3 | 0.7 | 0.3 |
| Nigeria | 10.6 | 5.4 | 6.2 | 7.0 | 6.0 | 1.9 | 5.0 | 2.4 | 0.3 |
| South Africa | 4.9 | 5.0 | 5.3 | 5.1 | 3.1 | -2.2 | 3.1 | -0.4 | 0.0 |
| East and South Asia | 7.8 | 7.7 | 8.6 | 9.3 | 6.3 | 4.3 | 6.4 | 1.1 | 0.8 |
| China | 10.1 | 10.4 | 11.6 | 13.0 | 9.0 | 8.1 | 8.8 | 0.5 | 0.6 |
| India | 8.3 | 9.3 | 9.7 | 9.1 | 7.3 | 5.9 | 6.5 | 0.9 | 0.2 |
| Western Asia | 8.7 | 6.9 | 6.1 | 5.0 | 4.6 | -1.0 | 3.6 | -0.3 | 0.7 |
| Israel | 5.0 | 5.1 | 5.2 | 5.4 | 4.1 | 0.1 | 2.0 | 1.0 | 1.2 |
| Turkey | 9.4 | 8.4 | 6.9 | 4.5 | 1.1 | -4.9 | 2.2 | -0.4 | 1.0 |
| Latin America and the Caribbean | 5.8 | 4.6 | 5.5 | 5.6 | 4.1 | -2.1 | 3.4 | -0.2 | 1.7 |
| Brazil | 5.7 | 3.2 | 4.0 | 5.7 | 5.2 | 0.0 | 4.5 | 0.6 | 2.0 |
| Mexico | 4.0 | 3.2 | 4.8 | 3.2 | 1.3 | -7.1 | 3.0 | -2.3 | 1.8 |
| ***of which:*** | | | | | | | | | |
| Least developed countries | 8.2 | 7.8 | 7.9 | 8.5 | 7.2 | 3.3 | 5.3 | 0.6 | 0.7 |
| ***Memorandun items:*** | | | | | | | | | |
| World trade | 11.0 | 7.8 | 9.3 | 6.7 | 2.9 | -12.5 | 5.4 | -1.4 | 1.8 |
| World output growth with PPP-based weights | 4.9 | 4.4 | 5.0 | 5.0 | 3.0 | -1.0 | 3.2 | 0.0 | 0.5 |

**Source:** UN/DESA.

a Partly estimated.

b Forecasts, based in part on Project LINK