

## AT A GLANCE . . .

### The world economy

- Despite the credit crisis, global growth will slow from 4.7 per cent in 2007 only to 4.2 per cent in 2008 largely thanks to the resilience of Asian economies.
- A pick-up in inflation will be difficult to shake off: prices in the OECD will rise by 3.1 per cent this year and 2.7 per cent in 2009.
- The stagflationary mix will be especially acute in the United States, whose GDP will grow by only 1.3 per cent this year while prices will rise by 4.3 per cent.
- The Euro Area will slow markedly, growing by 1.5 per cent this year and 1.9 per cent in 2009.
- Helped by continuing rapid expansion in China, Japan will perform better than most big developed economies, growing by 1.8 per cent this year and 2.0 per cent in 2009.

As the most serious credit crisis since the early 1930s unfolds, an extreme outcome in braking the global economy, including a recession in the OECD, cannot be excluded. However, progressively more ambitious attempts by the world's main central banks to forestall the potential fall-out have lessened the danger. Our central forecast is that global growth will decelerate fairly modestly – from 4.7 per cent last year to a still robust 4.2 per cent in 2008.

A reassuring overall outlook masks a sharp divergence between the developed and emerging economies. Growth in the mainly advanced OECD group of economies will slow from 2.7 per cent in 2007 to 2.0 per cent this year. By contrast, the relentless pace of Chinese growth will barely skip a heartbeat, as GDP expands by 10.4 per cent in 2008. The Asian upswing is being buoyed by lax monetary policy, which is keeping short-term interest rates well below the rate of nominal GDP growth in several countries, including China and India. The downside is an upsurge in inflation, which now poses the most serious risk to the economic stability of the region.

The prospects for the US economy are poor, as GDP growth slows from 2.2 per cent in 2007 to 1.3 per cent in 2008 and 1.7 per cent in 2009. Output is expected to have fallen in the first quarter of this year and the outcome for 2008 as a whole would be far worse but for the big loosening of monetary and fiscal policy, which together are boosting this year's growth by around 1.5 percentage points. The risk is that a surge in inflation will linger; measured by the private-consumption deflator, prices will rise by 4.3 per cent this year, falling back only to 2.9 per cent in 2009.

Unlike the Fed, the European Central Bank has made no

change in interest rates since the credit crisis began last August. Furthermore, exporting firms in the Euro Area are being squeezed by the rapid rise in the euro against the dollar. As a result, Euro Area growth will also slow markedly, from 2.6 per cent in 2007 to 1.5 per cent in 2008, before picking up a bit to 1.9 per cent in 2009. The ECB's stern monetary stance should limit the inflationary shock; although consumer prices rose by 3.6 per cent in the year to March, they are forecast to rise by 2.5 per cent in 2008 compared with 2007.

While the US and the Euro Area feel the pain of the credit crisis, Japan will ride out the storm. Japanese banks, still scarred by the banking crisis of the 1990s, did not participate in the risky behaviour of European and American banks that has backfired so spectacularly. The economy will expand by 1.8 per cent this year and 2.0 per cent in 2009, supported despite a stronger yen by the continuing boom in China, which now purchases around a fifth of Japanese exports.

Summary of the forecast – World economy  
percentage change, year-on-year

	Real GDP	Consumer prices <sup>(a)</sup>	World trade <sup>(b)</sup>
2007	4.7	2.0	5.9
2008	4.2	3.1	6.6
2009	4.3	2.7	6.7

(a) OECD countries. (b) Volume of total world trade.