



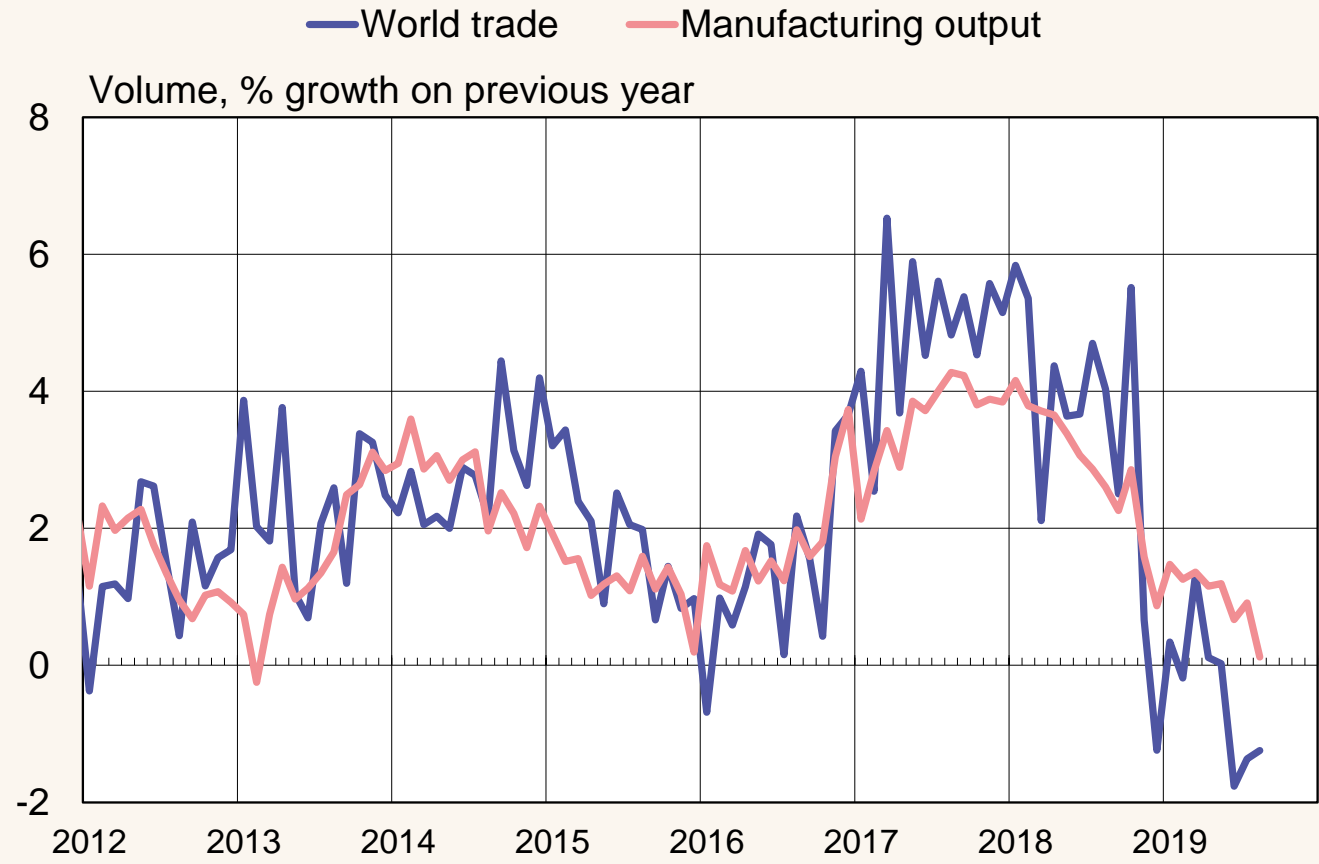
Global and European Economy from the Finnish Perspective

Lunch event hosted by National University of Singapore

7 November 2019

Olli Rehn
Bank of Finland

Pervasive uncertainty is still here – growth of world trade and industrial output have declined sharply



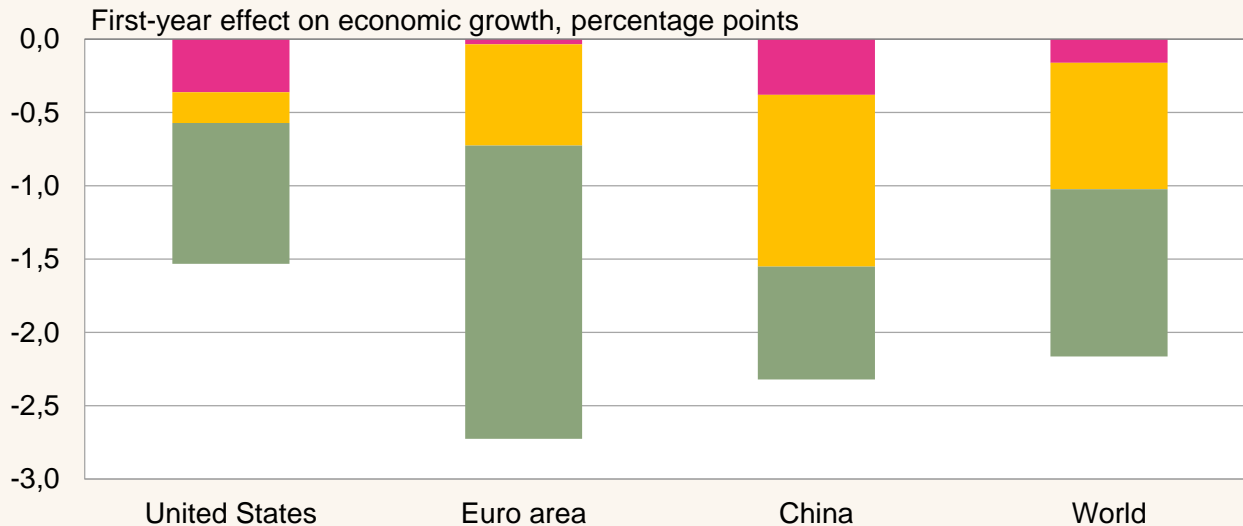
Sources: CPB, Macrobond.

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Bank of Finland risk scenario: Growth to contract significantly if the trade war damages the financial conditions

Risk scenario: trade war escalates, effects spill over to financial markets

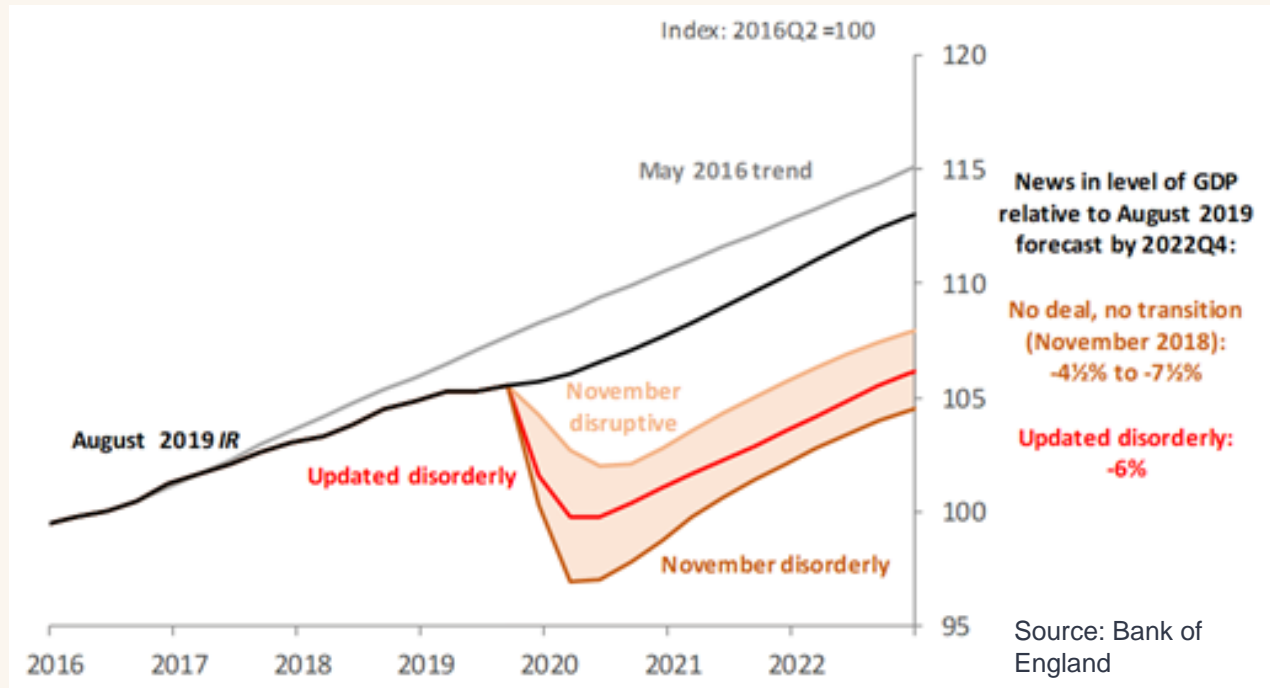
- Global financial market shock
- Increasingly tight financial conditions in emerging economies
- Planned tariff increases



Source: Calculations by the Bank of Finland.
eurojatalous.fi / bofbulletin.fi
3.10.2019

- Global economic growth could slow further from around 3% to about 1%.
- Significant ramifications impact on the euro area — calculations are based on limited room for monetary accommodation and no use of fiscal stimulus.

The Bank of England updated its Brexit calculations in September – successful preparations have softened the worst-case scenario



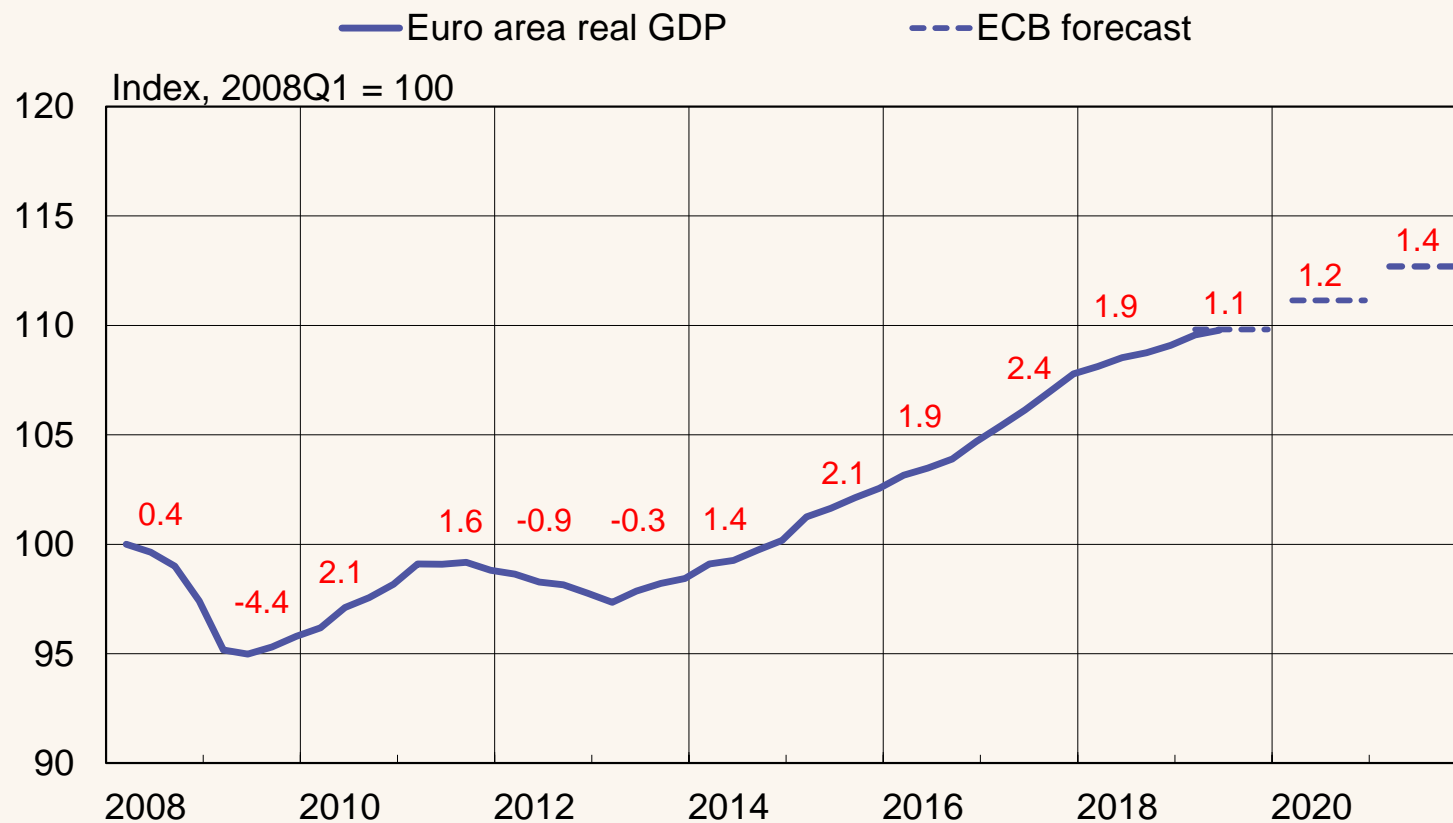
Worst-case scenario: no-deal, disorderly Brexit

- UK GDP declines by around 5.5% (previous assessment: -8%)

The impact of Brexit on EU27: 10–30% of the GDP losses experienced by the UK

- Large divergence in country-specific Brexit effects

Euro area GDP, 2008-21

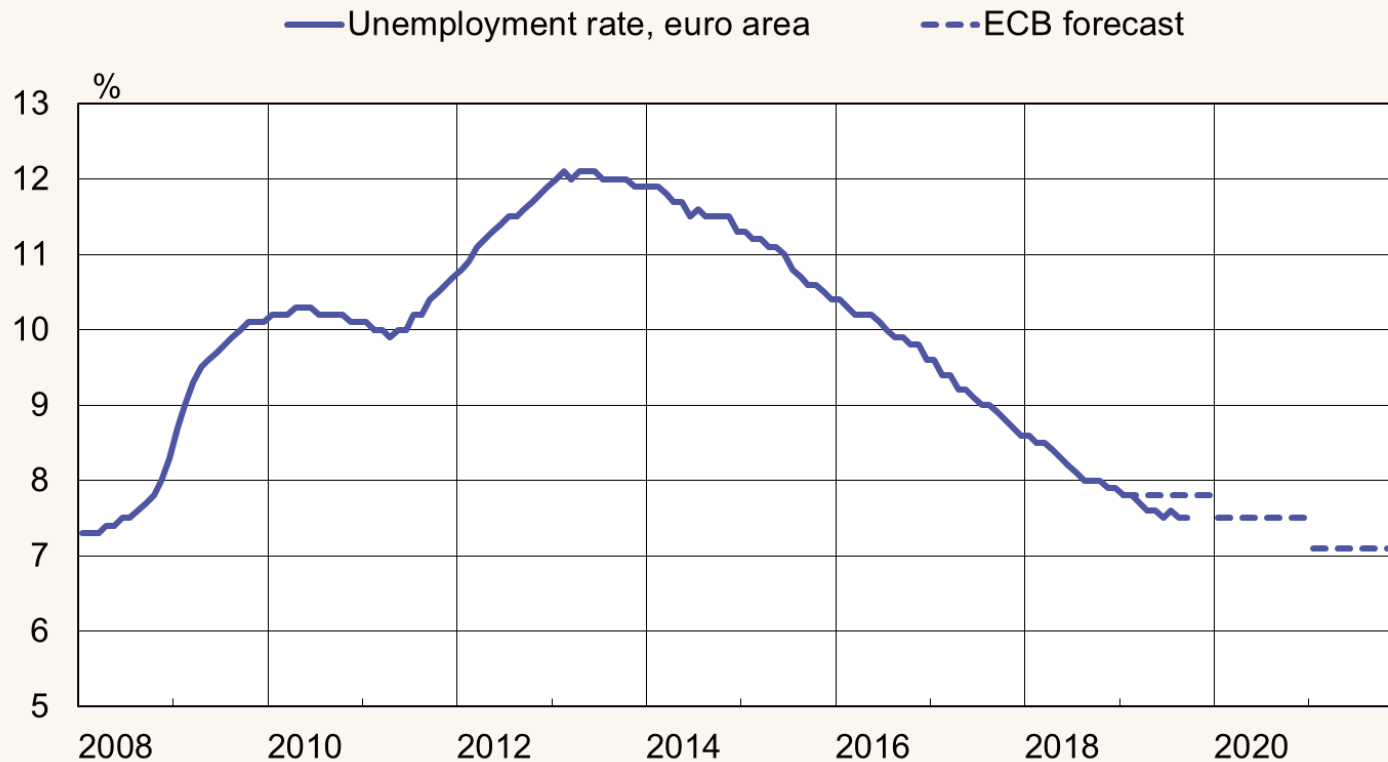


Euro area, changing composition. Figures next to the line are annual growth rates.

Sources: Eurostat and ECB.

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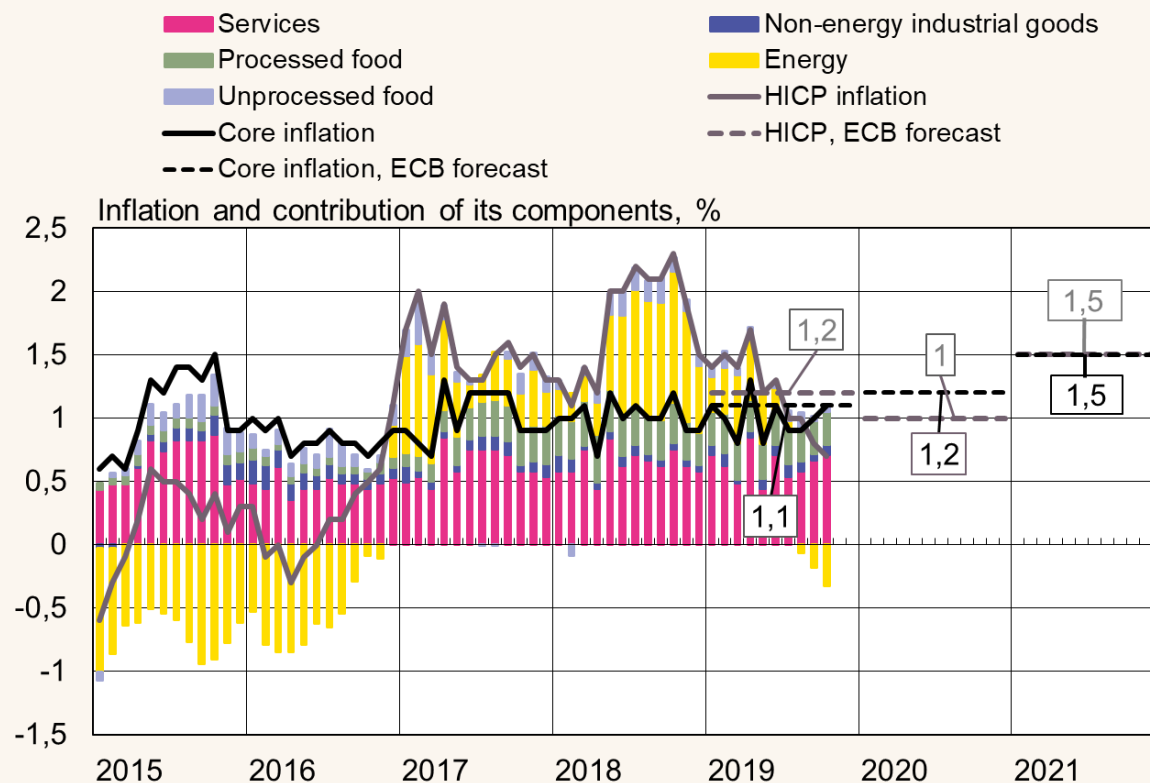
Strong jobs growth in 2013-19 – weaker cyclical conditions have not increased unemployment so far



Sources: Eurostat and ECB.
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Euro area inflation projected to remain well below 2%

Euro area inflation and decomposition by commodity group



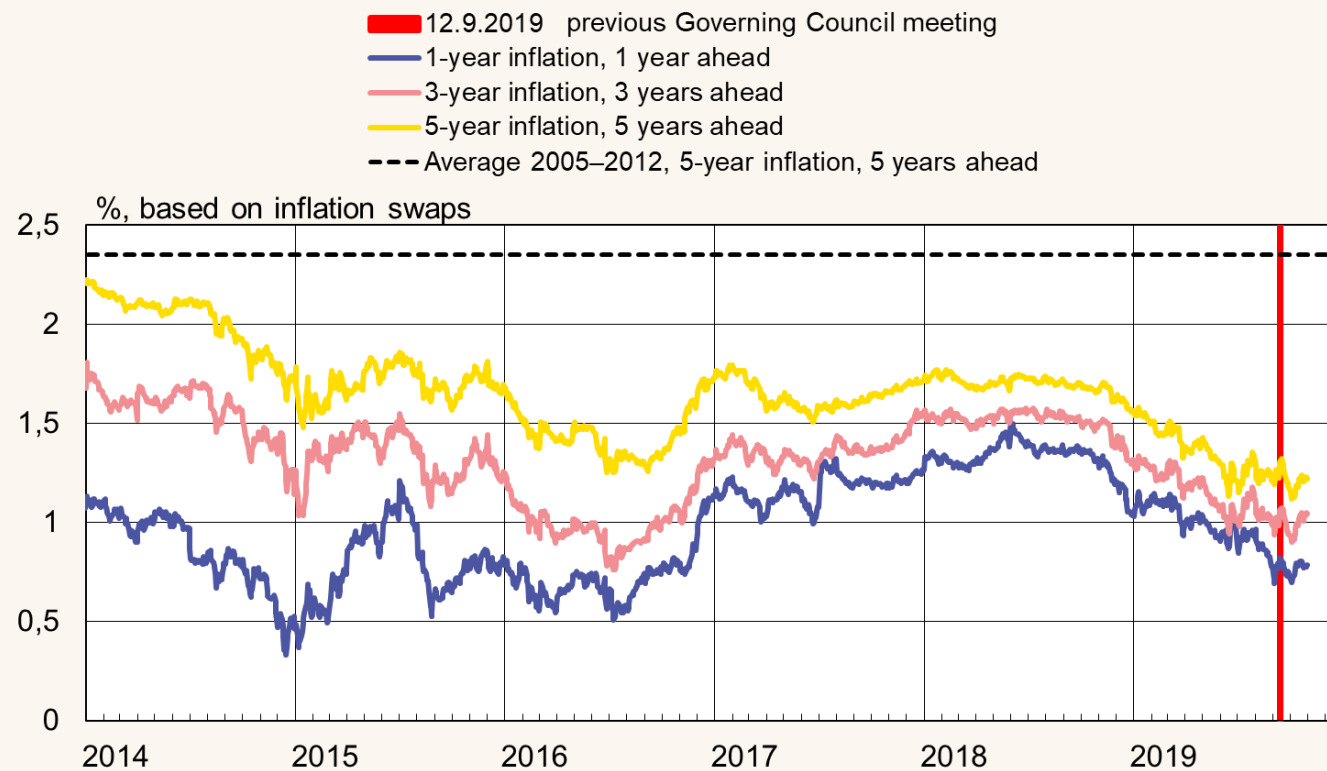
NB: Annual inflation rate of 2015 is distorted due to the change in methodology.

Sources: Eurostat and ECB.

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Inflation expectations in the euro area still at low levels

Market-based euro area inflation expectations



Sources: Bloomberg and Bank of Finland calculations.

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Consequently, the ECB maintains a very accommodative monetary policy stance

Governing Council's decisions of September 2019 concerning key ECB interest rates

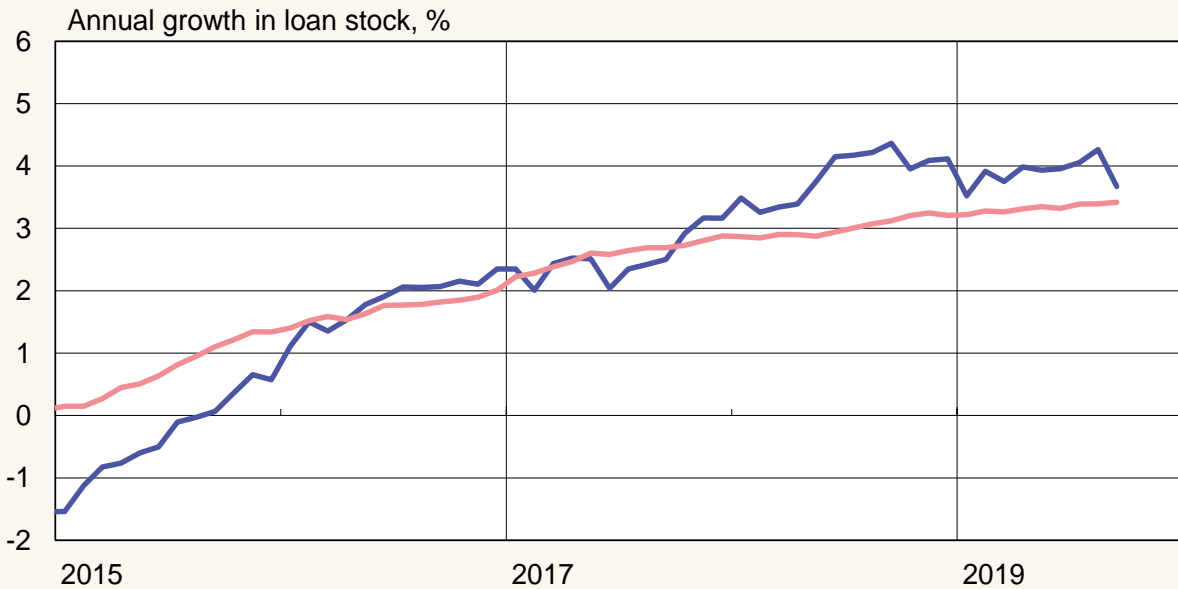
- The deposit facility rate was lowered from -0.40% to -0.50%.
- The Governing Council now expects the key ECB interest rates to remain at their present or lower levels until the inflation outlook has robustly converged to a level sufficiently close to, but below, 2% within the projection horizon and such convergence has been consistently reflected in underlying inflation dynamics.

Governing Council's September decisions concerning the asset purchase programme (APP)

- The Governing Council will restart net purchases under the APP at a monthly pace of EUR 20 billion as from 1 November 2019.
- The purchases are expected to run for as long as necessary to reinforce the accommodative impact of policy rates, and to ease shortly before the Governing Council starts raising the policy rates.
- As previously announced, the Governing Council intends to continue reinvesting, in full, the principal payments from maturing securities purchased under the APP for an extended period of time.

Financial conditions continue to ease in the euro area

— Non-financial corporations — Households



Adjusted for loan sales securitisation.
Source: ECB.

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— Non-financial corporations — Households



Source: ECB.

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Monetary and fiscal policies in the current context

- Fiscal policy has a bigger role to play when monetary policy is constrained by the effective lower bound.
 - If faced with recession, use fiscal policy space, where and when available.
 - Policy coordination is important to have optimal effect.
- New economic landscape and new monetary policy tools call for a strategy review of ECB monetary policy framework.

Intensify the reform of Economic and Monetary Union

- Complete the Banking Union
- From ‘Capital Markets Union’ to ‘Growth and Investment Union’?
 - Activate retail investors, both SMEs and households
 - Facilitate the European market for green bonds
 - Continue working on a European safe asset
- Make the EMU fiscal rules more counter-cyclical
 - Debt anchor linked to medium-term growth trajectory
 - Expenditure rule to ensure solid implementation

Summary: the Euro area outlook in the end of 2019

- Prolonged uncertainty is damaging growth, but no recession (yet).
- Monetary policy remains very accommodative for an extended period of time.
- Need a better policy mix of fiscal and monetary policy.
- A strategy review of monetary policy under consideration.
- Intensify the reform of Eurozone architecture.



Thank you!

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