Banc Ceannais na hÉireann
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Box A: QB 3 – July 2021

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Box A: The International Economic Outlook

By the Monetary Policy Division

The global economic outlook is expected to remain relatively positive as countries continue to recover from the COVID-19 pandemic. However, differences across countries in their ability to combat the virus and rollout vaccines is likely to lead to varying speeds of recovery. In April, the IMF forecast global growth of 6.0 percent in 2021 and a moderation to 4.4 percent in 2022. The latest OECD projections, released in May, expect the global economy to expand by 5.8 percent in 2021 and by 4.4 percent in 2022. The OECD also note that the world economy has now returned to pre-pandemic activity levels but, by end-2022, will still remain short of what was expected prior to the crisis. Fiscal supports are aiding the recovery in the global economy, with stimulus helping to boost demand and reduce the risk of longer-term economic scarring in the wake of the pandemic. However, the slower vaccination deployment in many emerging-market economies, coupled with severe outbreaks of COVID-19 in some countries, could limit growth for some time.

Euro area seasonally-adjusted Gross Domestic Product (GDP) declined by 0.6 percent in the first quarter of 2021, when compared to the previous quarter. The decline follows a negative reading of -0.7 percent in the fourth quarter of 2020, after a strong rebound of 12.5 percent in the third quarter of 2020. Compared with the March 2021 ECB projections, the growth outlook has been revised up for 2021 and 2022. This reflects the assumption that the pandemic will have a smaller economic impact, given the progress on the vaccination campaign, substantial additional fiscal policy measures and an upgrade to the outlook for foreign demand supported by the recent fiscal policy packages in the United States. Euro area GDP is expected to increase by 4.6 percent in 2021 (up from the March forecast of 4.0 percent), 4.7 percent in 2022 (up from 4.1 percent), and 2.1 percent in 2023 (unchanged).

In April 2021, the euro area seasonally-adjusted unemployment rate was 8.0 percent, down from 8.1 percent in March 2021. However, it remains higher than the reading of 7.3 percent in April 2020. Current unemployment estimates should be read with caution, as they are based on the globally used International Labour Organisation standard definition of unemployment, which does not fully capture the unprecedented labour market situation triggered by the pandemic. In May, the euro area Purchasing Managers Index (PMI) Composite Output Index, compiled by Markit, rose to 57.1, from 53.8 in April. The May reading marked a third successive month of expansion and was the best since

February 2018. Similarly, the Services PMI increased to 55.2, from 50.5 in the previous reading. This was the highest reading in just under three years. The final euro area manufacturing PMI posted a new record improvement in May, increasing to 63.1 from 62.9 in April. The reading was the highest since the survey started in June 1997, and marks 11 consecutive months of growth. The PMI readings show the continued progress in business activity as economies in the euro area open from virus-related restrictions.

Euro area headline inflation, as measured by the year-on-year increase in the Harmonised Index of Consumer Prices, stood at 2.0 percent in May, up from 1.6 percent in April, according to a flash estimate. Looking at the main components of euro area inflation, energy had the highest annual rate in May (13.1 percent, compared with 10.4 percent in April), followed by services (1.1 percent, compared with 0.9 percent in April). ECB projections for the euro area inflation have been revised upward for this year and next, and now expect an annual HICP inflation of 1.9 percent in 2021 (up from the March forecast of 1.5 percent), 1.5 percent in 2022 (up from 1.2 percent), and 1.4 percent in 2023 (unchanged).

In June, the Governing Council (GC) of the ECB confirmed that it will continue to conduct net asset purchases under the pandemic emergency purchase programme (PEPP) with a total envelope of €1,850 billion until at least the end of March 2022 and, in any case, until it judges that the coronavirus crisis phase is over. Based on a joint assessment of financing conditions and the inflation outlook, the GC expects purchases under the PEPP to be conducted over the third quarter of 2021 at a significantly higher pace than during the first months of the year. The GC confirmed its commitments with respect to the key ECB interest rates, the asset purchase programme (APP), the expected PEPP reinvestment phase, and the third series of targeted longer-term refinancing operations (TLTRO III).

In the United States, real GDP increased by 1.6 percent quarter-on-quarter in the first quarter of 2021, after a 1.1 percent increase in the fourth quarter of 2020. The increase in first quarter GDP reflected the continued economic recovery, reopening of businesses, and continued government response related to the COVID-19 pandemic. In April, the unemployment rate was little changed from previous months, standing at 6.1 percent. While unemployment levels have declined notably over the past year, they remain well above the pre-pandemic level of 3.5 percent in February 2020. In April, the Federal Reserve's Federal Open Market Committee (FOMC) held interest rates in a range of 0 to 0.25 percent, in a unanimous decision. The FOMC committed to maintaining an accommodative stance, and reiterated that it would continue its asset purchase programme at a rate of $120bn per month until "substantial further progress" was made towards its goals of maximum employment and inflation at a rate of 2 percent over the longer run. The FOMC expects higher inflation in the coming months, but largely due to transitory factors.

In the United Kingdom, GDP is estimated to have contracted by 1.5 percent in the first quarter of 2021. Compared with the same quarter a year ago, when the initial economic impacts of the

coronavirus (COVID-19) pandemic began to show, the UK economy fell by 6.1 percent. At its May meeting, the Bank of England's Monetary Policy Committee (MPC) voted unanimously to maintain the Bank Rate at 0.1 percent. The MPC also voted to maintain the target for the stock of UK government bond purchases at £875 billion and so the total target stock of asset purchases at £895 billion.