Discussion
IMF ECONOMIC OUTLOOK

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April 2023

Q1. The baseline outlook

Growth Projections
(percent change from a year earlier)

	World	Advanced Economies	U.S.	Euro Area	Italy	U.K.	Emerging Market and Developing Economies	China
2022	**3.4**	**2.7**	**2.1**	**3.5**	**3.7**	**4.0**	**4.0**	**3.0**
Revision from Jan. 2023	0.0	0.0	0.1	0.0	-0.2	-0.1	0.1	0.0
2023	**2.8**	**1.3**	**1.6**	**0.8**	**0.7**	**-0.3**	**3.9**	**5.2**
Revision from Jan. 2023	-0.1	0.1	0.2	0.1	0.1	0.3	−0.1	0.0
2024	**3.0**	**1.4**	**1.1**	**1.4**	**0.8**	**1.0**	**4.2**	**4.5**
Revision from Jan. 2023	-0.1	0.0	0.1	-0.2	-0.1	0.1	0.0	0.0

Source: IMF, April 2023 *World Economic Outlook.*

Why so prudent baseline growth projections?

- Credit contraction?
  - Banks are stronger when interest rates increase. Non-banks mostly contract credit. Banks are major credit providers in the EU
- Fiscal policy?
  - Governments cut back Covid and energy support. However there is support by Next Generation EU for several years. And the military effort

Why so prudent baseline growth projections?

- <u>Lower real wages and consumption?</u>
  - There is, however, an increase in both employment and vacancies
- <u>Energy availability?</u>
- Last year EU countries faced problems in France (nuclear) and Spain and Italy (Hydro), but were helped by low demand from China and good weather conditions. Are strains being considered in the baseline scenario?
- <u>Exports?</u>
  - Is the EU especially affected by further geo-political tensions

Q2. The downside scenario with financial instability

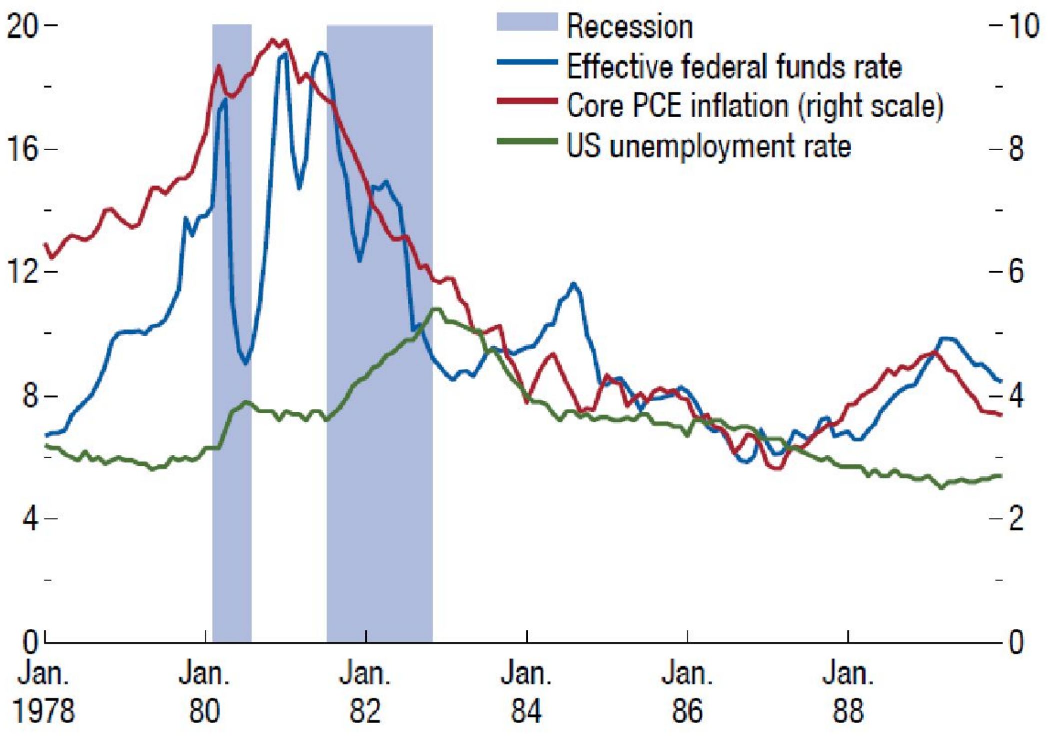
Risks to the Outlook

Downside

- Financial sector tightening from high interest rates
- Sharper monetary policy impact amid high debt
- Stickier inflation
- Systemic sovereign debt distress in EMDEs
- Faltering growth in China
- Escalation of the war in Ukraine
- Geopolitical and economic fragmentation

Ensuring a Durable Fall in Inflation

Risk of Premature Easing: The US Experience in the 1980s
(Percent)



Monetary policy: steady but ready

- Where core inflation persists, raise real rates, hold above neutral, prevent de-anchoring.
- Stand ready to address financial sector risks with available tools.
- If severe downside scenario materializes and financial stability at stake, adjust monetary policy path to minimize contagion.
- Clear communication on inflation goal.

How Likely this Downside Scenario in the EU?

- The ESRB had issued its first warning in 10 years last September. The possible causes:
  - Money tightening, reducing the value of balance sheet assets => materialized in March
  - Geopolitical tensions
- How likely are additional interest rate hikes?
  - Inflationaly supply shocks receding
  - If not enough, there are available tools to fight both instability (purchases) and inflation (interest rates)

How Likely this Downside Scenario in the EU?

- Likelihood of an interest rate increase

- A. expected benefits of reduced inflation
- B. expected costs of reduced economic activity
- C. expected costs of using the tools targeted to financial instability