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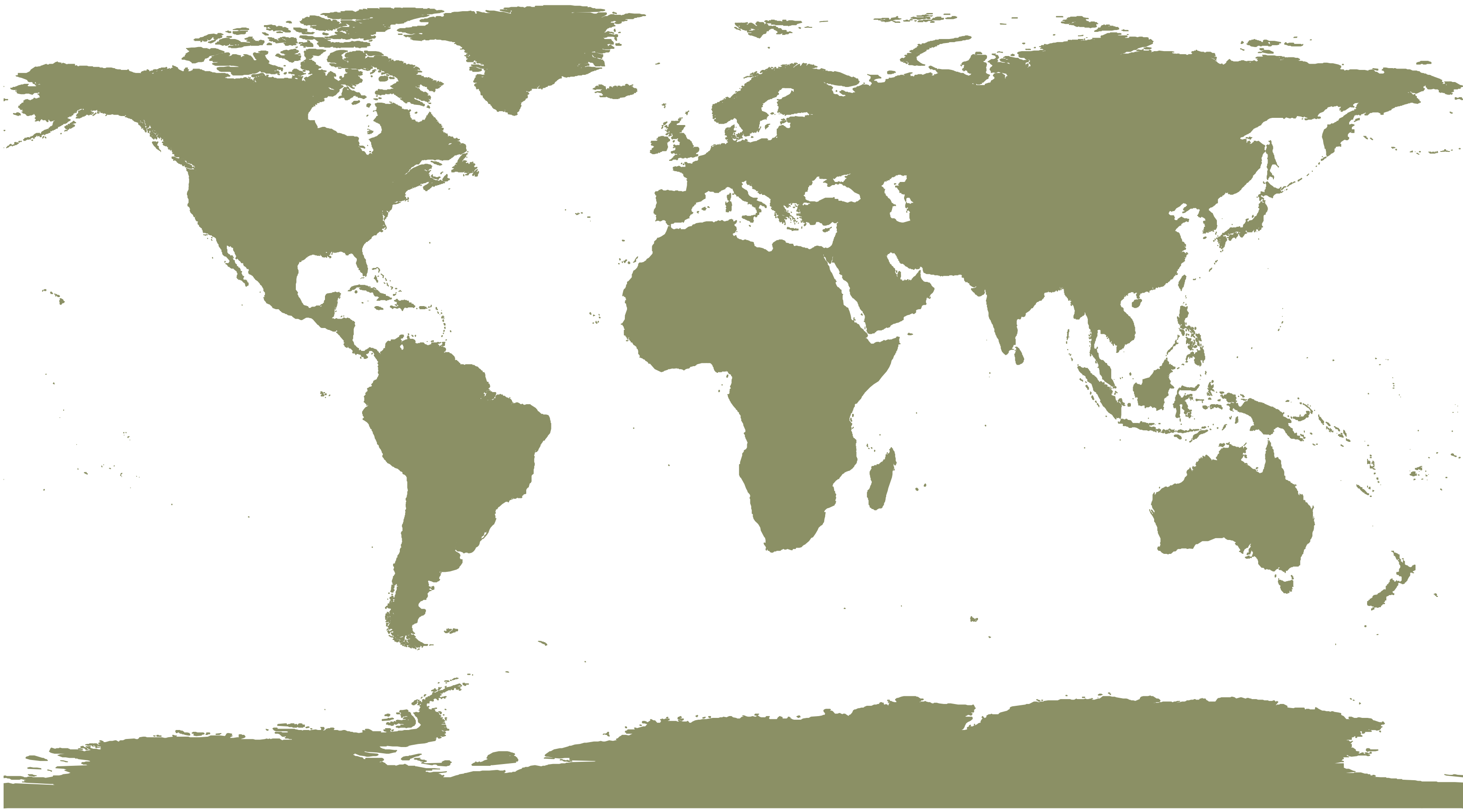
World Economic Situation and Prospects 2015

Update as of mid-2015*



United Nations
New York, 2015

* *The present document updates World Economic Situation and Prospects 2015 (United Nations publication, Sales No. E.15.II.C.2), released in January 2015.*

World Economic Situation and Prospects 2015

Update as of mid-2015*

Summary

The world economy continues to grow at a modest pace. Growth of world gross product is projected at 2.8 per cent in 2015, accelerating to 3.1 per cent in 2016. The growth divergence between various regions is widening in 2015, owing to differing impacts from the recent decline in the prices of oil and other commodities, as well as country-specific factors. The short-term growth prospects of heavily commodity-dependent countries have worsened considerably. By contrast, commodity-importers are benefiting from the lower prices in the form of reduced inflationary, fiscal and balance-of-payment pressures. While the recovery in developed economies is improving, many countries still face considerable headwinds from the legacies of the global financial crisis. The overall subdued performance of the world economy in recent years has raised concerns of a "new normal" of lower growth. The broad-based weakness in investment worldwide not only holds back current growth, but also reduces potential growth in the future.

The major downside risks to the baseline outlook are related to the impact of the upcoming monetary policy normalization in the United States, ongoing uncertainties in the euro area, potential spillovers from geopolitical conflicts, and persistent vulnerabilities in emerging economies. To mitigate these risks and ensure a return to strong, sustainable and balanced growth, a broad set of policy measures at the domestic, regional and global level is needed. The report identifies key challenges in the areas of monetary, fiscal, labour market and trade policies, underlining the need for strengthened international policy coordination. Such coordination becomes ever more critical as the Member States of the United Nations are expected to adopt a new financing framework for sustainable development and an ambitious post-2015 sustainable development agenda.

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I. Global macroeconomic trends

Global growth prospects

The world economy continues to grow at a modest pace. Growth of world gross product is projected to accelerate slightly from 2.6 per cent in 2014 to 2.8 per cent in 2015—a downward revision by 0.3 percentage points from the forecast presented in the World Economic Situation and Prospects 2015 in January. In 2016, global growth is forecast to improve to 3.1 per cent. There are still considerable downside risks to the baseline forecast, related to the upcoming move towards monetary policy normalization in the United States, ongoing uncertainties in the euro area, potential spillovers from geopolitical conflicts and persistent vulnerabilities in emerging economies. The overall subdued performance of the world economy since the global financial crisis has raised concerns of a "new normal" of lower growth, especially in view of a broad-based weakness in investment.

The downward revision in global growth for 2015 reflects mainly a deteriorating outlook in the economies in transition and several large developing countries, especially in South America. Gross domestic product (GDP) in the economies in transition is projected to contract by 2 per cent this year, while average growth in developing countries is expected to remain at 4.4 per cent, about 3 percentage points below the pre-crisis pace. The growth divergence between the various regions is widening in 2015. This can be partly attributed to the differing impacts from the recent drop in the prices of oil and other commodities.

For heavily commodity-dependent economies, the short-term growth prospects have worsened considerably. In some cases, this has been amplified by large capital outflows and by persistent domestic weaknesses, including macroeconomic imbalances, social and political unrest, and inefficient economic management. On the other hand, large commodity-importers have benefited from lower prices in the form of reduced inflationary, fiscal and balance-of-payment pressures, improving the short-term growth outlook for many of these countries. As some of the current headwinds start to recede, growth in developing countries and economies in transition is projected to gain some strength in 2016.

The prospects for developed economies in 2015 have been slightly upgraded from earlier forecasts, with average growth projected to accelerate from 1.6 per cent in 2014 to 2.2 per cent in 2015. Almost all major developed economies are expected to see the growth momentum picking up. The upward revision reflects a moderately improved outlook for the euro area owing to a number of factors, including lower energy prices and significant currency depreciation on the back of the European Central Bank's (ECB's) new large-scale asset-buying program. Despite expectations of a more robust recovery, developed economies continue to face considerable headwinds from the legacies of the global financial crisis, including subdued employment levels, elevated private and public sector debt, and financial sector fragilities.

Employment

The latest available data confirm a modest labour market recovery in 2014, driven by improvements in developed economies, which is expected to continue in 2015. Globally,

Table 1
Growth of world output, 2013–2016, annual percentage change

Annual percentage change					Change from January 2015 forecast	
	2013	2014[a]	2015[b]	2016[b]	2015	2016
World	2.5	2.6	2.8	3.1	-0.3	-0.2
Developed economies	1.2	1.6	2.2	2.2	0.1	-0.1
United States of America	2.2	2.4	2.8	2.7	0.0	-0.4
Japan	1.6	0.0	1.2	1.0	0.0	-0.1
European Union	0.0	1.3	1.9	2.1	0.2	0.1
EU15	-0.1	1.2	1.8	2.0	0.3	0.1
New EU Members	1.3	2.7	2.8	3.2	-0.1	-0.1
Euro area	-0.4	0.9	1.6	1.9	0.3	0.2
Other European	1.4	2.1	0.5	1.3	-1.7	-1.0
Other developed countries	2.0	2.6	2.4	2.8	-0.2	0.2
Economies in transition	2.0	0.7	-2.0	0.9	-3.1	-1.2
South-Eastern Europe	2.4	0.1	1.4	2.5	-1.3	-0.5
Commonwealth of Independent States and Georgia	2.0	0.7	-2.1	0.9	-3.2	-1.2
Russian Federation	1.3	0.4	-3.0	0.1	-3.2	-1.1
Developing economies	4.7	4.4	4.4	4.8	-0.4	-0.3
Africa	3.3	3.3	4.0	4.8	-0.6	-0.1
North Africa	1.0	1.0	2.8	4.0	-1.1	-0.3
East Africa	6.5	6.4	6.6	6.7	-0.2	0.1
Central Africa	2.0	4.1	3.4	4.3	-1.3	-0.7
West Africa	5.6	5.8	5.8	6.2	-0.4	0.1
Southern Africa	3.2	2.5	2.9	3.7	-0.7	-0.4
East and South Asia	6.1	6.2	6.2	6.1	0.2	0.1
East Asia	6.4	6.1	6.0	6.0	-0.1	0.0
China	7.7	7.4	7.0	6.8	0.0	0.0
South Asia	4.9	6.3	6.7	6.9	1.3	1.2
India[c]	6.4	7.2	7.6	7.7	1.7	1.4
Western Asia	3.1	3.0	3.0	3.6	-0.7	-0.7
Latin America and the Caribbean	2.7	1.0	0.5	1.7	-1.9	-1.4
South America	2.9	0.6	-0.4	1.1	-2.3	-1.7
Brazil	2.5	0.1	-1.1	0.5	-2.6	-1.9
Mexico and Central America	1.8	2.3	3.0	3.2	-0.5	-0.6
Caribbean	3.0	1.8	3.1	3.7	-0.7	-0.1
Least developed countries	5.3	5.2	4.9	5.6	-0.8	-0.3
Memorandum items:						
World trade[d]	3.1	3.2	3.8	4.8	-0.7	-0.1
World output growth with PPP-based weights	3.1	3.2	3.4	3.7	-0.1	-0.1
Africa excluding Libya	4.0	3.8	4.2	4.8	-0.3	0.0
North Africa excluding Libya	2.8	2.6	3.5	4.0	-0.1	0.0

Source: UN/DESA.
a Partly estimated
b Forecast, based in part on Project LINK
c Based on newly released data
d Includes goods and services

employment is estimated to have grown by 1.4 per cent in 2014, a similar expansion to that in 2013. While this is a modest improvement compared to average growth between 2007 and 2012, it remains persistently below the pre-crisis pace, when employment growth averaged 1.7 per cent annually. Against the backdrop of modest GDP growth, employment creation remains too weak to recover the jobs lost during the crisis and to absorb new market entrants. Unemployment is thus expected to remain elevated in many developed countries, while part-time jobs and lower labour force participation will remain major challenges. In the euro area, average unemployment is projected to decline only slowly from 11.6 per cent in 2014 to 11.1 per cent in 2015 and 10.5 per cent in 2016. In the United States, the recent positive trend is expected to continue, with unemployment forecast to average 5.1 per cent in 2016, down from 5.5 per cent in March 2015. At the same time, labour market conditions in many developing countries and economies in transition have somewhat worsened. With GDP growth slowing, employment growth is coming down, while gender gaps are often widening. Unemployment rates are estimated to have increased in most developing regions, with the exception of South Asia. During the forecast period, this adverse trend is expected to persist, given that growth will likely remain subdued in many countries.

Inflation

Average global inflation continues to decline amid persistent negative output gaps and the drop in oil and food prices. In 2015, global consumer price inflation is expected to average 2.5 per cent, the lowest level since 2009. With oil prices expected to recover slowly and global activity projected to pick up, average inflation is forecast to accelerate to 3 per cent in 2016. This aggregate picture encompasses a wide range of diverse dynamics. In developed countries, inflation rates—and inflation expectations—have drifted downwards despite unprecedented expansionary monetary policies. Deflation risks remain in place, particularly in the euro area and Japan. In developing countries, lower oil prices have generally reduced inflationary and balance-of-payment pressures, giving central banks more room to tackle slowing growth. The overall impact on inflation differs widely across countries, depending on exchange rate trends, the importance of oil in consumer baskets, monetary policy stances and the extent of fuel subsidies. For instance, exchange rate depreciations have fuelled inflation in the Russian Federation and Ukraine, while keeping inflation above trend in Brazil and Chile. Inflation will still be elevated in several developing countries and economies in transition, including for example Argentina, Belarus, Ukraine and the Bolivarian Republic of Venezuela owing to a variety of factors, such as market distortions, supply shortages, currency depreciations and inflation inertia.

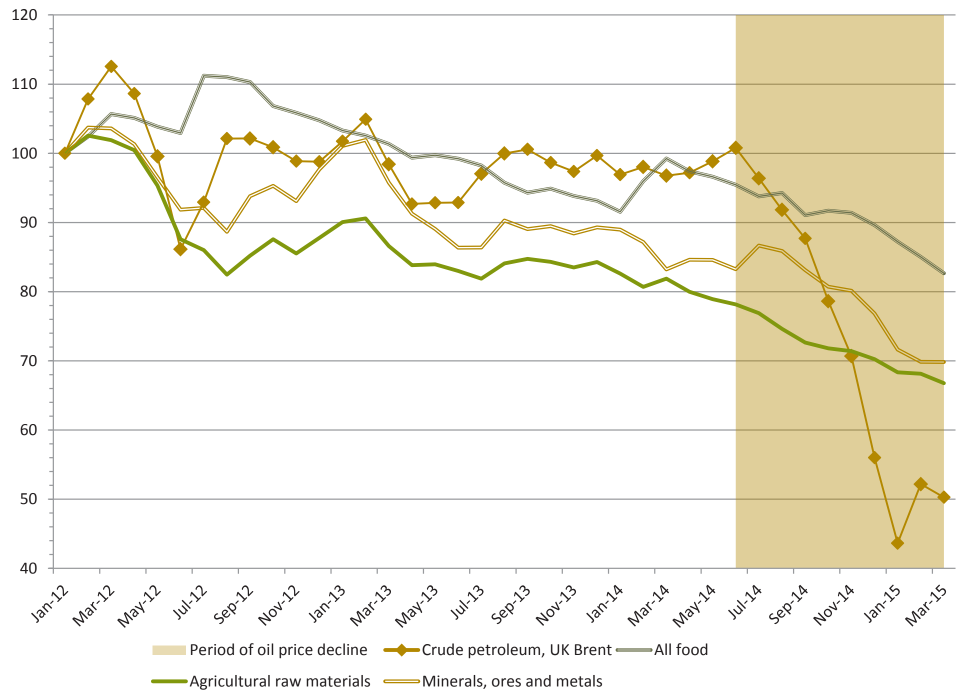
Commodity prices

Global commodity prices continued to decline in early 2015 *(figure 1)* amid sustained oversupply, relatively weak global demand, and a strengthening dollar. The Brent oil price fell by more than 50 per cent between June 2014 and January 2015, dropping to a 5-year low of $45 per barrel (pb). The price has recovered somewhat, fluctuating between $55 and $70 pb in the period February to April. Volatility will likely remain high during 2015, even as the oil market remains oversupplied. The demand-supply gap is expected to narrow considerably in 2016, easing the downward pressure on oil prices. The price is projected to average

Figure 1

Price indices of selected commodity groups, January 2012 - March 2015
(*Index: January 2012=100*)

Source: UNCTADStat



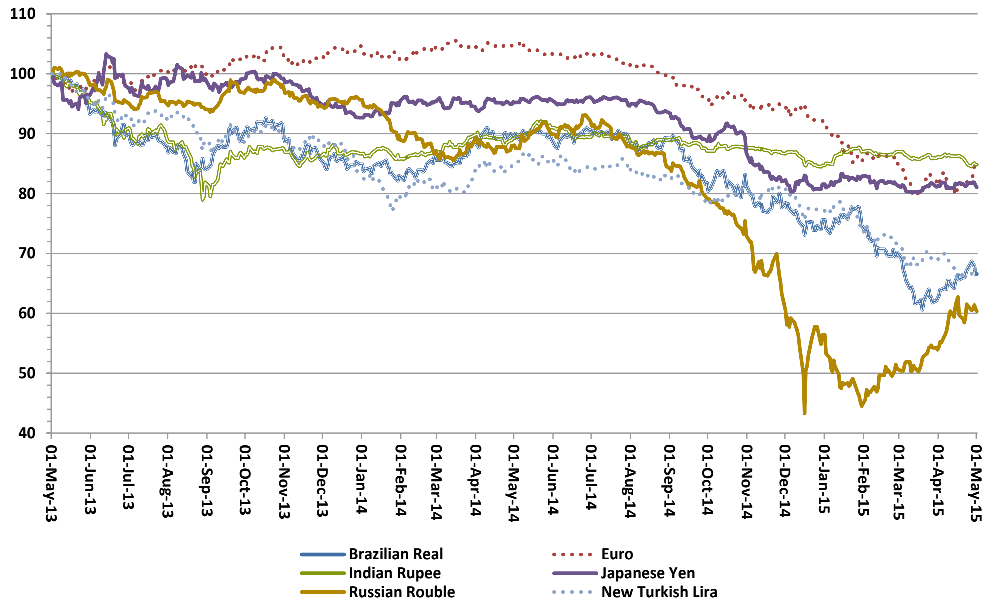
\$60 pb in 2015 and \$70 pb in 2016. Upside risks to this outlook include Organization of the Petroleum Exporting Countries (OPEC) production cuts or conflict escalation in oil exporting countries. Downside risks are related to continued strong growth of North America's shale oil output and a lift of the export ban against the Islamic Republic of Iran. Among non-oil commodities, the group of minerals, ores and metals experienced the sharpest price fall between October 2014 and April 2015, declining on average by 14 per cent. Low oil prices amplified the downward trend of non-oil commodity prices, particularly in the case of food and metals. This partly reflects the fact that energy costs make up a significant portion of production and transportation costs of food and metal. In the forecast period, the downward pressures on non-oil commodity prices will likely persist, although less strongly than in 2014.

Exchange rates

The major trend on global foreign exchange markets has been the strength of the dollar. During the first quarter of 2015, the dollar continued to appreciate, reaching multi-year highs against many currencies *(figure 2)*. Since then, the dollar has pulled back somewhat, but remains relatively strong. The broad-based dollar strength has been driven by the relatively positive outlook for the US economy and expectations of a widening monetary policy divergence between the United States Federal Reserve (Fed) and other central banks. While the Fed is expected to start raising interest rates in the second half of 2015, most

Figure 2

Exchange rates of selected currencies vis-à-vis the US dollar, 1 May 2013 - 1 May 2015
(*Index: 1 May 2013=100*)



Source: J.P. Morgan Markets.

Note: A rising index indicates an appreciation of the currency against the US dollar.

other central banks still move in the opposite direction. The ECB's large-scale bond buying programme that was launched in early 2015 sent the euro sharply lower. Several large developing countries, most notably Brazil and Turkey, continued to experience strong downward pressure on their currencies as concerns over weak macroeconomic fundamentals, financial vulnerabilities and political woes led to capital outflows. In the forecast period, the dollar is expected to stay relatively strong against most currencies as the growth and monetary policy divergences remain in place. Given uncertainties over the euro area outlook, the effects of a rise in US interest rates and the weakness in some emerging economies, foreign exchange volatility will likely remain elevated.

International trade flows

Global trade is expected to improve moderately, growing somewhat faster than the rate of global output and expanding by 3.8 per cent in 2015 and 4.8 per cent in 2016. Trade growth in early 2015 has been relatively sluggish, but similar patterns have been observed in recent years with trade rebounding over the rest of the year. Substantial changes in exchange rates are expected to result in some shifts in directions of trade. The broad-based appreciation of the dollar has begun to have some impact on the United States' trade balance and this is likely to increase further in the forecast period as trade patterns adjust to relative prices. Recent exchange rate changes are expected to result in some pick-up for euro area exports and weak import demand in South America. East Asian exports are projected to remain relatively strong. While prospects for global trade are improving, several factors will continue to limit the possibilities for trade to return to higher growth patterns. These include lingering subdued global demand; limited prospects for large increases in trade growth as a result of trade agreements; and perhaps more limited scope for further integration of developing countries into the global trading system. Global services trade will continue to expand at a more rapid rate than merchandise trade, although growth in international tourism is expected to slow slightly in 2015 after expanding by 3.7 per cent in 2014.

International capital flows

Recent trends on global financial markets continue to be driven by highly accommodative monetary policies in a low-inflation or deflationary environment in developed economies. As a result, sovereign and corporate bond yields have plummeted to record lows, while stock markets have reached new highs. Cross-border bank lending has also started to recover, but is still below the levels observed before the financial crisis. Capital flows to developing economies and economies in transition have retreated, with persistent volatility. Given a subdued growth outlook for many of these economies and an upcoming move towards US monetary policy normalization, this downward trend is expected to continue in 2015. Significant declines in equity and debt inflows have been recorded in the Russian Federation and Ukraine—mainly owing to geopolitical tensions and worsening economic conditions—but also in other emerging economies, such as Brazil, Mexico and Turkey. Capital outflows from China have also increased—a trend that could strengthen in the medium run as the country moves to a slower growth path. During the forecast period, the interaction between global monetary conditions and the ongoing fragilities in emerging economies could lead to further capital flow reversals amid rapidly changing investor sentiment. Large commodity-exporting countries with open capital markets appear to be particularly vulnerable.

Global imbalances

Current account imbalances in major economies narrowed slightly in 2014, continuing the trend of the past few years. The decline in the prices of oil and other commodities has contributed to this process, leading to lower deficits in several large commodity-importers and smaller surpluses or even deficits in major commodity-exporters, notably Saudi Arabia and other Gulf Cooperation Council (GCC) countries. The strengthening of the dollar could, however, presage some widening of global imbalances in the outlook period, albeit not to the levels seen in 2006-08. The United States remains by far the world's largest deficit country. In 2014, its current account deficit reached $410 billion, accounting for 2.4 per cent of GDP, the same ratio as in 2013. Among the major surplus countries, China's current account surplus remained steady at about 2 per cent of GDP in 2014, while Germany's surplus continued to rise, equalling 7.4 per cent of GDP. This helped push the euro area's combined surplus to a new record—a trend that could be reinforced by the weakening of the euro. The large and growing surpluses of some euro member countries reflect various factors, including sluggish investment and reluctance to open up service sectors.

II. Economic outlook by region

Developed economies

United States

In the United States, the economic recovery remains on track and the short-term outlook is relatively favorable. Following strong expansions in the second and third quarter of 2014, growth has, however, slowed noticeably. The weak performance in early 2015 can be attributed to less investment in the energy sector, disturbances to international cargo shipping and bad weather. Growth is expected to pick up over the next quarters and reach 2.8 per cent in 2015, before decelerating slightly to 2.7 per cent in 2016. Continuous improvement in the labour market will prompt private consumption to grow at the fastest pace since the Great Recession. Business fixed investment will also expand solidly. However, in addition to subdued demand from trade partners, export growth may also be dampened by the significant appreciation of the US dollar since mid-2014. The Fed is expected to start raising its policy rate during the second half of 2015, but will follow a cautious approach.

Japan

Japan's GDP is projected to grow by 1.2 per cent in 2015 and 1.0 per cent in 2016. In 2014, the Japanese economy suffered from the consumption tax rate hike and fell into recession by mid-year. The tepid recovery that started in the fourth quarter helped lift GDP to the same level as in the previous year. In addition to increasing fiscal spending slightly for the current fiscal year, the Japanese Government has decided to postpone a second tax hike from October 2015 to April 2017. However, weak growth in wages and labour income will fail to make up for the higher price level, and private consumption is expected to further recede slightly in 2015 before resuming growth in 2016. Long after the significant depreciation of the Japanese yen started, export volumes began to increase in late 2014 and are expected to provide support for growth. Since October 2014, the Bank of Japan has increased the scale of its asset purchasing programme to 80 trillion yen per year, further strengthening its efforts to bring the inflation rate back to the 2 per cent target.

Western Europe

The fragile economic recovery in Western Europe is gradually becoming more broadly-based, supported by low oil prices, currency depreciation, expansive monetary stimulus programmes, declining consumer prices and some easing of the pressure for fiscal consolidation. While the EU-15 expanded by just 1.2 per cent last year, growth strengthened in the second half of 2014 and is expected to continue to improve this year. GDP is expected to grow by 1.8 per cent in 2015 and 2.0 per cent in 2016. Stronger consumer spending is underpinned by rising real incomes, given the unexpectedly sharp drop in oil and consumer prices. As prolonged deflation could become entrenched in expectations, the ECB announced a significant loosening of its monetary stance in January 2015. Under the ECB's Expanded Asset Purchase Programme, purchases of public and private sector securities will amount to €60 billion per month, restoring the ECB balance sheet to 2012 levels by September 2016. The looser stance has been reflected in recent exchange rate and asset price movements, and has given a boost to confidence. Weaker currencies will support European external competitiveness, with the notable exception of Switzerland, where the decision to abandon the minimum boundary vis-à-vis the euro allowed a steep appreciation of the Swiss franc in January. The improving euro area outlook relies on a timely agreement between Greece and the Eurogroup of Finance Ministers over financing arrangements. While there has been a significant reduction in external exposure to Greek assets, and a more general improvement in bank capitalisation throughout much of Europe, several countries remain fragile.

New EU Member States

Aggregate GDP growth of the new EU member States, which reached 2.7 per cent in 2014, is expected to further strengthen to 2.8 per cent in 2015 and 3.2 per cent in 2016. The positive impact of reviving private demand and less fiscal drag will be supported by accommodative monetary policies, low energy costs and the pick-up in EU-15 economies. While most economies in the region are expected to expand at about 3 per cent in 2015, Croatia might see near-zero growth. Although in some countries foreign-currency denominated household debt remains a problem—further aggravated by the appreciation of the Swiss franc in January—continuing real-wage growth is expected to bolster household spending. Investment is expected to remain on an upward trend and labour markets are improving. Lower energy and food prices resulted in negative annual inflation in several countries in 2014, with positive, but very low inflation expected for 2015.

Canada and Australia

Growth in Canada is expected to slow from 2.5 per cent in 2014 to 2.1 per cent in 2015, before recovering to 2.6 per cent in 2016. The slowdown mainly reflects reduced investment in the oil sector and falling government revenues amid low oil prices. Higher manufacturing exports, due to stronger growth in the United States and the depreciation of the Canadian dollar, are expected to mitigate the slowdown. In Australia, lower export prices for mineral commodities have reduced fixed investment, but strong private consumption is expected to push the growth rate from 2.7 per cent in 2014 to 2.8 per cent in 2015.

Economies in transition

Commonwealth of Independent States

Growth prospects for the Commonwealth of Independent States (CIS) region in 2015-2016 have been downgraded against the backdrop of low oil prices, military conflict in the East of Ukraine and economic sanctions against the Russian Federation. The aggregate GDP of the CIS and Georgia is expected to contract by 2.1 per cent in 2015 and expand only modestly by 0.9 per cent in 2016. Although the direct impact of sanctions on the Russian economy has been relatively limited, they have contributed to capital outflows, currency depreciation and a weakening in business confidence. The Russian economy is expected to shrink by about 3 per cent in 2015, as weak business sentiment and high interest rates deter investment and high inflation weighs on private consumption. Ukraine's economy is expected to contract sharply owing to the conflict in the industrial part of the country, fiscal tightening and a fall in private consumption. Weaker Russian and Ukrainian markets will also constrain growth in Belarus. Lower oil and gas revenues will lead to a growth moderation in energy-exporting countries, such as Azerbaijan and Kazakhstan. For lower-income energy-importing economies, such as Armenia, Kyrgyzstan, Moldova and Tajikistan, the partial loss of the Russian market and the declining value of remittances outweigh the benefits of lower fuel costs, while fewer opportunities for labor migration have increased labour market pressures. Most of the CIS currencies either were devalued or depreciated significantly in the past year, spurring inflation, in some cases to double-digit levels. Weaker currencies will partly offset fiscal losses in the energy-exporting CIS economies, but many Governments will nonetheless need to draw from their sovereign reserve funds. The weaker currencies will at the same time undermine private consumption and put pressure on the banking systems, constraining credit expansion. The establishment of the Eurasian Economic Union of Armenia, Belarus, Kazakhstan and the Russian Federation in January 2015—Kyrgyzstan is also set to join the union—should bolster intra-regional economic ties, although many aspects of the integration process still have to be agreed.

South-Eastern Europe

The aggregate GDP of South-Eastern Europe is expected to expand by 1.4 per cent in 2015 and 2.5 per cent in 2016, following growth of only 0.1 per cent in 2014. Stronger growth rates will, however, be needed to address the region's structural problems, such as high unemployment. In 2014, the region saw divergent economic performances. The Serbian economy, hit by devastating floods and curbed by fiscal retrenchment, contracted by 1.8 per cent. The former Yugoslav Republic of Macedonia, by contrast, registered growth of 3.6 per cent on the back of strong public investment and increased food exports to the Russian Federation. In 2015, the region is expected to benefit from the pick-up in the EU and see moderate strengthening in foreign direct investment. However, the ongoing fiscal austerity in Serbia, linked to the terms of the International Monetary Fund's (IMF's) stand-by agreement, will weigh on short-term growth. In the outlook period, domestic demand is expected to become the main growth driver. Record-low inflation, negative in some countries, was observed in 2014, and the low-inflation trend is likely to continue in 2015.

Developing economies

Africa

Falling commodity prices and declining exchange rates are painting a mixed picture for Africa, with strong divergence between oil-exporting and oil-importing economies. Average growth is expected to reach 4.0 per cent in 2015 and 4.8 per cent in 2016, which is significantly lower than the previous forecast. Central Africa and North Africa have seen the biggest downward revisions for 2015, with the security situation playing a major role. A large part of the downward revisions for North Africa and for Africa as a whole is due to Libya, which remains trapped in a civil war. Growth remains robust in East Africa owing to continued investment and growth in services. South Africa's growth continues to be lacklustre, hampered in part by energy infrastructure constraints. Average inflation in Africa remains on a downward trend, projected to slow to 7.0 per cent in 2015 and 6.5 per cent in 2016. However, some of the expected decline has been offset by imported inflation due to currency depreciations. Moreover, some dry weather has pushed up food prices in East Africa, though not nearly as much as in 2011. Monetary policies in many countries are expected to remain mostly unchanged, as policymakers balance the need to forestall greater declines in exchange rates with the desire to reduce interest rates in the face of lower inflation. In general, fiscal policies will be expansionary, particularly in the (many) countries that are having elections over the forecast period. Fiscal deficits are projected to narrow slightly in aggregate, driven by lower commodity prices, although deficits in some oil exporters are projected to rise. Export growth is expected to be mixed depending on countries' trading partners and exchange rate trends, with those trading more with developed countries seeing some improvement, while those with a larger share of trade with emerging market economies seeing some deceleration. Lower commodity prices will narrow oil exporters' current account surpluses and push some into deficit. Risks to the forecast are related to a significant change in oil prices and to further geopolitical instability or further slowdowns in major trading partners.

East Asia

East Asia will remain a key driver of global growth during the forecast period. Economic activity in the region is forecast to grow by 6.0 per cent in both 2015 and 2016, about the same pace as in 2014 and virtually unchanged from the previous forecast. China is projected to grow by 7 per cent in 2015—in line with the government target—and 6.8 per cent in 2016. Weaker-than-expected data on key indicators in early 2015 indicate slowing growth momentum in China, which will likely prompt further accommodative fiscal and monetary policy measures. Growth in many East Asian economies is expected to accelerate in 2015, compared to 2014. Papua New Guinea and Thailand are projected to experience the strongest growth improvements. Papua New Guinea's economy will receive a boost from the first full-year of production at its key liquefied natural gas project. In Thailand, improved political stability is expected to boost tourism and government spending. The region's export growth is projected to pick up as stronger demand in developed economies offsets the impact of China's slowing growth. Government spending will increase in most economies, which will help spur investment growth during the forecast period. Average consumer price inflation in 2015 has been revised downward to 1.7 per cent, with an acceleration to 2.4 per cent expected for 2016. Central banks in China, Indonesia, the Republic of Korea, and Thailand cut their policy rates in the first quarter of 2015. However, concerns over debt levels, asset bubbles, and capital outflows limit the willingness of authorities to further ease monetary policy. East Asian currencies showed resilience against the US dollar in the first quarter of 2015, with several currencies actually gaining ground. This trend also means that most of the region's currencies appreciated in trade-weighted terms, accentuating the trend observed since the global financial crisis and weighing on export growth.

South Asia

South Asia's economic outlook is largely favourable. Most economies are expected to experience a strengthening of growth in 2015-16 on the back of stronger domestic consumption and investment, and a pick-up in exports. The region's GDP is projected to grow by 6.7 per cent in 2015 and 6.9 per cent in 2016, up from an estimated 6.3 per cent in 2014—a significant upward revision from the previous forecast. This revision mostly reflects a higher growth trajectory in India, where recent changes in methodology and data sources have resulted in considerably higher official growth figures for the past two years. India is now projected to grow by 7.6 per cent in 2015 and 7.7 per cent in 2016, surpassing the growth of China. The growth prospects for the Islamic Republic of Iran and Pakistan have also improved moderately, although for both countries significant uncertainties remain. Across

South Asia, the expansion is expected to be driven by buoyant household consumption and a gradual recovery in investment. Private sector demand will be underpinned by a more benign macroeconomic environment, including considerably lower inflation. Average inflation in the region is projected to fall to its lowest level in almost a decade, following the recent decline in oil and food prices. As a result, monetary policy has become more expansionary in several countries, notably in India and Pakistan. Despite the improved outlook, South Asia's economies face, to varying degrees, long-standing development challenges including energy shortages, infrastructure deficits and political and social unrest.

Western Asia

In Western Asia, lower oil prices weigh heavily on oil exporting economies, while the more diversified economies are expected to perform better than anticipated. The region is projected to register 3.0 per cent growth in 2015, the same rate as in 2014. In 2016, growth is expected to improve to 3.6 per cent, helped by rising oil prices and stronger external demand. At the subregional level, the GCC member countries are expected to experience a modest economic expansion in 2015, given sluggish oil output growth. Economic activity will be supported by large fiscal stimulus programmes, targeting mainly infrastructure projects. Fiscal deficits are therefore expected to widen during the forecast period. Conversely, the more diversified economies are expected to perform better in 2015, benefiting from more competitive exchange rates, lower oil prices, and more monetary policy space to stimulate domestic demand. This combination of factors will support growth and help reduce current account deficits in 2015, particularly in Turkey. There are, however, considerable downside risks to this forecast. Geopolitical conflicts, in particular the recent conflict in Yemen (see section on LDCs), could escalate, hampering domestic economic activities and regional trade. If oil prices remain at the current low level for longer than forecast, oil exporting economies will face fiscal pressures, aggravating growth prospects for 2016.

Latin America and the Caribbean

The economic prospects in Latin America and the Caribbean have worsened noticeably, amidst lower commodity prices and persistent domestic fragilities. The region is expected to grow by only 0.5 per cent in 2015 and by 1.7 per cent in 2016, albeit with significant heterogeneity across sub-regions. Economic growth in Mexico and Central America is expected to strengthen moderately in 2015, benefiting from a pick-up in activity in the United States. GDP growth in Mexico is expected to reach 2.8 per cent in 2015. By contrast, South America is slowing down markedly with continuous declines in investment. The Bolivarian Republic of Venezuela is falling into a deeper recession, while Brazil and Argentina are expected to contract by 1.1 per cent and 0.4 per cent in 2015, respectively. Other South American economies, such as Bolivia, Paraguay and Peru, will grow more robustly, above 4.0 per cent. Meanwhile, economic growth in the Caribbean is expected to accelerate to 3.1 per cent in 2015. The decline in commodity prices is having widespread effects across the region. South America's commodity exporters, particularly oil exporters, have experienced significant changes in the terms of trade and thus on their external accounts, in addition to weaker investment prospects. At the same time, most economies have cut interest rates or maintained accommodative monetary policies, as lower oil prices have reduced inflationary pressures; an exception is Brazil, where the tightening cycle continues. Consumer price inflation is projected to remain high in Argentina and the Bolivarian Republic of Venezuela. Fiscal balances have deteriorated slightly owing to the economic slowdown, higher expenditures, and lower commodity prices, limiting the countercyclical policy space. Currency depreciations should gradually boost exports and help regional economies adjust to the change in external conditions.

Least Developed Countries

The least developed countries (LDCs) are expected to see growth of 4.9 per cent in 2015, a deceleration from 5.2 per cent in 2014 and a marked downward revision by 0.8 percentage point compared to the previous forecast. Growth in some LDCs, such as Ethiopia, Rwanda and Tanzania, has been robust and sustained, owing in part to investments in agriculture and infrastructure, expanding services sectors and rising domestic demand. On the other hand, the fall in the prices of commodities, particularly oil, is putting a dent in the revenues of commodity exporters, leading to lower investment and consumption levels. In several LDCs, economic development is hindered by unstable security situations, as is the case in South Sudan or Yemen. Yemen was off track with respect to meeting many of the Millennium Development Goals (MDGs) even before the recent conflict escalation, but living conditions now stand to deteriorate even further, with both unemployment and poverty rates already exceeding 40 per cent. The conflict will harm the economy in various ways, aggravating the fiscal deficit and pushing up inflation.

III. Uncertainties and risks

The economic prospects for the world economy as outlined above entail significant uncertainties and risks. The individual risks are interconnected and could be mutually reinforcing, potentially leading to a much weaker expansion of the global economy than projected in the baseline. In addition to the short-term factors, there are also more medium-term risks. Most importantly, the broad-based weakness of investment in the context of highly accommodative monetary policies and very low real interest rates has raised concerns over further declines in potential growth.

Normalising monetary policy in the United States

The Fed is expected to start normalising policy interest rates in 2015, which have been kept near zero for the past seven years as a drastic measure to fight the financial crisis and the sluggishness of the recovery. Significant risks are associated with the uncertainties over the actual path of the normalization and how financial markets and the real economy respond to interest rate hikes.

First, the upcoming rise in interest rates will increase financial costs for businesses and households. The higher financial costs could stifle growth in the United States, particularly if interest rates moved up faster than anticipated. Secondly, emerging economies have increasingly issued dollar-denominated debt in the past few years and could face higher financial costs and risks of currency mismatch when the Fed increases interest rates. Thirdly, in response to higher interest rates in the United States, the repricing and reallocation of financial assets across financial markets worldwide could happen abruptly. Fourthly, capital flows to and out of emerging markets could become more volatile, leading to heightened volatility in exchange rates and asset prices. A final risk is that higher US interest rates lead to higher rates in many other countries since interest rates in the United States are frequently used as a benchmark for other countries.

Euro area crisis

The debt crisis in Greece continues to cast a shadow over an otherwise improving outlook in much of Europe. An escalation of tensions between the Greek Government and Troika lenders could derail the fragile European recovery, with potentially global repercussions. While the risks of contagion to markets outside of Greece have subsided substantially compared to 2010-12, uncertainty surrounding Greece's continued access to finance, and the future solvency of the Greek Government remain unresolved.

Government finances in Greece have come under severe stress, as negotiations continue between the Greek Government and the euro group of Finance Ministers over the conditions attached to additional financial assistance from the Troika lenders. Until new disbursements of financial assistance are agreed, the Government has few financing options and limited possibilities to roll-over maturing debt, forcing it to rely more heavily on the uncertain and volatile timing of tax receipts in order to remain solvent. Until the solvency issues are resolved, there remains a possibility that a lack of access to finance could compel a withdrawal from the monetary union. The economic implications of such an unprecedented event are highly uncertain, but there is a risk that this could lead to heightened volatility of the euro and European financial markets, which could spill over to markets outside of Europe.

Geopolitical issues

Geopolitical tensions and conflicts constitute a significant downside risk to the economic outlook. In several countries such as Ukraine, the Syrian Arab Republic, Iraq and Yemen, military conflicts have taken a heavy human toll and led to widespread destruction. While the negative economic impact has so far been limited to the subregional level, the risks lie in possible spillover effects of any regional conflict to the global level. Potential transmission channels include trade, commodity prices and financial asset prices.

Geopolitical conflicts, especially in Africa and Western Asia, remain risk factors for the global oil market. In Libya and Yemen, for instance, where military conflicts have escalated, oil production and exports could be easily disrupted, sending prices higher. In the case of Yemen, however, the main source of risk is the possible closure of the route through the Bab el-Mandeb Straits, used by tankers to transport crude oil out of the Gulf region. Oil prices could also rebound if the conflict in Yemen widens into a broader regional conflict, as several countries are currently participating in military actions.

The situation in Ukraine remains a further risk to the economic outlook. While negotiations have produced some agreement on a ceasefire and a stabilisation of the situation, a lasting solution has not yet been reached. Any renewed escalation could further crimp regional economic prospects and might also lead to negative spillover effects, in particular for Western Europe, not least through the energy sector and a fall in business confidence.

Vulnerabilities in emerging economies

Since mid-2011, emerging economies have experienced a significant and broad-based slowdown, reflecting a combination of cyclical and structural factors. Infrastructure deficits, lack of economic reform implementation, strong reliance on commodity exports and political woes have held back growth, while also magnifying the vulnerability to external shocks. While a widespread emerging market crisis, similar to those experienced in the 1990s, seems unlikely, several countries could face painful adjustment processes over the coming years and experience longer-than-expected periods of slow growth.

At present, the most vulnerable emerging economies are those that are exposed to geopolitical risks or political instability or that are heavily dependent on international commodity exports. If the prices of oil and other commodities remain low over the longer term, commodity-dependent emerging economies—particularly in Africa, South America, Western Asia and the CIS—could face increasing pressures on budgets and external balances.

The strong appreciation of the dollar has raised concerns over the rapid build-up of dollar-denominated debt in several economies. The bulk of this debt has been issued by private companies. With the dollar appreciating, the debt service obligations in local currency terms have risen notably. This has created challenges for companies, whose revenues are in local currency, increasing the risk of defaults and bankruptcies. These risks are amplified by the upcoming move towards monetary policy normalization in the United States, which could lead to further dollar appreciation, a significant reduction in capital flows to emerging economies and an increase in debt servicing costs. Countries with persistently large current account deficits and substantial external financing needs could be particularly vulnerable to financial turmoil.

IV. Policy challenges

Monetary policy

Growing divergence in the monetary policy stances of the United States and much of the rest of the world presents considerable macroeconomic policy challenges for many countries.

For the Fed, the key challenge is to manage the pace and sequence of normalising the policy rate so as to maintain macroeconomic stability, and support growth and employment, while at the same time preventing an unwarranted build-up in asset prices. For most other developed economies, risk of stagnation—amid prolonged low inflation, sluggish growth, protracted weak aggregate demand and slow-paced structural reforms—continues to warrant pro-active monetary policy stances, particularly in the euro area and Japan. The ECB continues to face the challenge of removing deflationary pressures, improving financial market conditions and easing access to credit for firms, especially small- and medium-sized enterprises, and households. The Bank of Japan's Quantitative and Qualitative Easing program faces the task of stimulating consumption and achieving the target of 2 per cent inflation while offsetting the impact of the rise in sales taxes last year.

The main monetary policy challenge for many developing economies is to find a balance between easing the policy stance to support growth and stemming currency depreciation, and maintaining capital inflows in the face of the upcoming Fed normalization. Monetary policy stances in many developing economies are expected to remain largely accommodative amid low inflation expectations and subdued growth prospects. However, as US interest rates begin to rise, some countries remain vulnerable to sudden-stops and capital flow reversals. In several countries, significant exchange rate depreciations have led to a build-up of inflationary pressures. As a result, central banks may come under pressure to raise interest rates in tandem with the US, leaving limited room for more accommodative policies to support growth.

Fiscal policy

Thanks to the historically low interest rate environment, most developed economies do not face significant fiscal risks in the near-term. However, public debt levels in many developed economies still remain elevated, averaging 100 per cent of GDP in 2014. Accordingly, reforms of the structure of public expenditure, including the entitlements programs, are kept on the agenda. Nonetheless, the focus of fiscal policy is slowly shifting from stabilisation of public finances to addressing labour market problems and bolstering potential output. As a consequence, most developed economies should face less fiscal drag in 2015-16 than in the past few years. Fiscal policy remains however still fairly restrictive in parts of the euro area, weighing on demand and adding to deflationary pressures.

In developing countries and economies in transition, budget deficits and public debt levels are generally lower than in developed economies. The sharp oil price decline has allowed fiscal authorities in several oil-importing countries to cut fuel subsidies, improving their budget balances. For oil-exporters, however, lower oil prices pose significant challenges.

Their fiscal balances will deteriorate in 2015-16. In some countries, lower revenues will, in the short run, be offset by spending from sovereign wealth funds or other domestic sources rather than borrowing. Persistently low oil prices would, however, eventually compel Governments to enact public expenditure reforms. The vulnerability of commodity-dependent countries once again highlights the need for targeted fiscal spending to support economic diversification.

The upcoming rise in US interest rates may lead to higher costs of debt refinancing against the background of changing investor sentiment or further currency depreciations, especially affecting countries with large short-term external debt. This may pose fiscal challenges for some developing economies, particularly those with weakening growth prospects. Nevertheless, countries that have favourable terms of access to financial markets could use the current low interest rate environment for long-term borrowing to invest in infrastructure and human capital.

Labour market policy

Despite recent improvements, employment growth remains slow and unemployment rates are still elevated in developed economies as a whole. A significant part of this situation reflects weak aggregate demand. Thus, macroeconomic policies to stimulate aggregate demand, such as targeted infrastructure investments, should be a priority to reduce cyclical unemployment and improve medium-term growth prospects. This would also have positive effects on reducing long-term unemployment and on avoiding additional structural unemployment, which remain important features of current labour market conditions. These measures need, however, to be complemented by active labour market policies, such as job search assistance and training programmes, which would increase labour force participation and reduce risks of aggravating structural unemployment. At the same time, reforms to reduce labour market segmentation should continue, in order to boost formal employment more permanently, including for young people.

Weak wage growth is currently a major labour market challenge. In developed economies, wage growth declined rapidly during the crisis and has not recovered since then, contributing to a widening gap between growth in real wages and labour productivity, and to feeble aggregate demand. Several countries have introduced changes to wage policies to improve workers' prospects and stimulate aggregate demand. In Germany, the recently enacted minimum wage law is expected to raise incomes at the bottom of the pay ladder. In the US, several States have lifted minimum wages in an attempt to improve the living standards of low income workers, but also to increase labour force participation and stimulate private consumption. In developing economies, particularly in Latin America, raising minimum wages and expanding social transfers has been a useful tool to boost demand during the global financial crisis. Setting an adequate minimum wage level is however the main challenge, in order to ensure its effectiveness in stimulating demand, while avoiding adverse employment effects.

Youth unemployment is a major concern across regions. The global youth unemployment rate is estimated at 13 per cent, three times higher than the overall rate, as young people were disproportionately affected by the financial crisis. Unemployment early in life can lead to discouragement and alienation, preventing human capital formation, especially when the absence from labour markets is prolonged. Hence, special attention has to be given to youth unemployment, by addressing skills mismatches and improving the transition from education to labour markets, as well as by raising education levels and reducing school dropouts.

Trade policy

Trade agreements remain an important policy challenge in many regions as various issues surrounding the negotiations continue to be politically charged and have raised publicly debated concerns. As tariff rates have come down considerably for a large majority of countries, the current negotiations increasingly centre on non-tariff measures such as domestic subsidies and intellectual property rules. Some progress has been made in the negotiations for the Bali Package of the WTO's Doha round. The members adopted decisions on public stockholding for food security purposes and the Trade Facilitation Agreement (TFA) in November 2014. Countries are now in the process of accepting the TFA provisions at the national level, which is expected to conclude before the next World Trade Organization (WTO) Ministerial Conference in Nairobi in December 2015. Two-thirds of the members will need to ratify the TFA for it to come into force.

At the same time, difficulties in concluding a multilateral agreement have driven countries to pursue bilateral and regional trade agreements (RTAs). Negotiations over large-scale RTAs such as the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Pact (TTIP) continue. Progress has been made, but questions remain surrounding the prospects of trade promotion authority (TPA) in the United States, an important step to more rapid approval of the deals. There are still political concerns about some provisions of the agreements, such as the investor-state dispute settlement (ISDS) provisions that opponents argue will interfere with national policy setting as has been the case with some bilateral investment treaties. Furthermore, there are widespread fears that regulatory harmonization could result in lower environmental, health and product regulation standards. Other large-scale agreements, which cover significant portions of world trade, are in the process of being negotiated or finalized. These include: the Regional Comprehensive Economic Partnership (RCEP), covering the majority of trade in Asia and Oceania; Economic Partnership Agreements (EPAs) between the EU and the five regions of Africa; and the China-Japan-Korea Free Trade Agreement, among others. There are risks for overlap between the many agreements, pointing to further need for countries to participate in WTO processes in order to harmonize the multilateral, regional and bilateral trading frameworks.

International policy coordination

At the finance ministers' meeting in April 2015, the G-20 reaffirmed its commitment to strengthen international policy coordination to manage the spillover effects of domestic policies against the backdrop of diverging monetary policy stances and rising financial market volatility. With a view to completing the financial reform agenda, countries agreed to finalize the proposed common international standard on total-loss-absorbing-capacity for global systemically important banks (G-SIBs) by November this year, taking fully into account the impact on banks in emerging markets. They further agreed to finalize the methodology for identifying systemically important financial institutions outside the banking and insurance sectors by the end of 2015. The G-20 also agreed to implement the updated shadow banking roadmap to further improve the oversight and regulation of shadow banking and strengthen cross-border cooperation for enhanced regulation of over-the-counter derivatives markets.

In conjunction with the G-20 commitment to push forward the financial reform agenda, the Financial Stability Board (FSB) recently adopted a work plan to assess financial stability risks associated with market liquidity in fixed income markets and asset management, identify longer-term structural financial stability issues in these activities and recommend appropriate policy measures in its next meeting in September 2015. The FSB also decided on a work plan to promote clearing through central counterparties to enhance resilience of financial systems and facilitate resolution of defaults.

Outstanding reforms of the IMF's quota and governance system remain a stumbling block in international policy coordination. The IMF has set June 2015 as the new deadline for completing the quota reforms, which were agreed during the 14th General Review of Quotas in 2010. The deadline for the 15th general review of quotas has been pushed to December 2015. Pending implementation of the reforms, the G-20 has urged the IMF to propose options for meaningful interim steps towards the full implementation of the 2010 reforms.

International policy coordination in the areas of monetary policy and financial regulation will become ever more critical as the Member States of the United Nations are expected to adopt a new financing framework for sustainable development in July and an ambitious post-2015 sustainable development agenda in September. Realization of the post-2015 development agenda will require strengthened international cooperation to build resilience against economic shocks and contagion and ensure adequacy and predictability of long-term development finance.

For further information,
see http://www.un.org/en/development/desa/policy/wesp/

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