34. THE UNITED STATES OF AMERICA

Maturing cycle amid high policy uncertainty

US economic growth is forecast to pick up from 1.6% in 2016 to around 2¼% in 2017 and 2018, amid increasing signs of a maturing cycle and rising policy uncertainty. While the assumed fiscal stimulus of the new administration may provide some boost to growth over the forecast horizon, other potential policy shifts, e.g. on trade and immigration, generate substantial risks to the outlook.

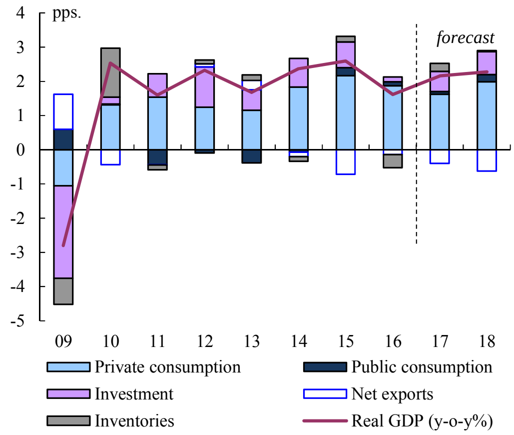
Solid growth amidst a maturing cycle

Early 2017 saw the US recovery entering its 31st quarter with clearer signs of a maturing cycle. The economy rebounded strongly in the second half of 2016 from the temporary soft patch in the first half (due to the correction in energy investment and inventories). The labour market remains buoyant, and the economy seems to be operating at or close to full employment. Inflationary pressures are on the rise, but solid real income growth continues to support private consumption. Against this background, policy plans of the new US administration have greatly increased economic uncertainty. Expectations of a strong pro-business agenda (stimulus, tax reform, deregulation) have helped boost confidence, but this is not yet borne out by hard data. Rising confidence and stimulus could support growth in the near-term, but given the advanced stage of the cycle, may also lead to overheating and faster tightening of monetary policy. Other potential policy shifts (trade, immigration) could turn out disruptive and thus entail downside risks, both in the near and medium term.

Stimulus likely to be smaller than previously expected

Six months after the elections concrete policy plans of the Trump administration are still subject to uncertainty. Compared to initial announcements, expectations of a fiscal stimulus have been scaled down considerably and pushed back in time. The level of ambition of the announced tax reform may also be more limited than initially thought and its implementation delayed until 2018, reflecting the political complexity of the legislative process. Likewise, the administration's Budget Blueprint and a lack of political momentum around the infrastructure investment bill would suggest no major increase in federal spending in the near term. Consequently, this forecast assumes a smaller fiscal package of just around 1% of GDP, implemented only from 2018, and composed exclusively of tax cuts (predominantly to corporate income). The already advanced stage of the US cycle is expected to keep the multipliers low, with the reaction of monetary policy and dollar appreciation likely offsetting some of the benign effects.

Graph II.34.1: **US - Real GDP growth and contributions**



The trend of gradually firming wage and price pressures, visible throughout 2016, is set for a further upgrade. Consumer price inflation is expected to rise from 1.3% in 2016 to 2.2% in 2017 and to 2.3% in 2018.

With consistently strong net job creation in 2016 and early 2017 the US economy appears to be at or very close to full employment. The unemployment rate fell to 4.5% in March, the pre-crisis level, even as participation in the labour force continued to inch up (since mid-2015) outweighing the secular demographic trend. The tightening labour market has already produced higher wage pressures that are expected to accelerate further in 2017 and 2018

These pressures are likely to trigger a faster normalisation of US monetary policy. As widely anticipated, the Fed raised its policy interest rate in March 2017 for the third time in this cycle (to 0.75-1.0%), and broadly upheld its projections for its future path and the outlook for the economy. Fed expectations now suggest two more hikes in 2017 and three in 2018.

Domestic demand to remain growth driver

The solid labour market, rising wages and the assumed cut in personal income taxes (from 2018) are expected to boost private consumption to 2.8% in 2018. Business investment is also set for a recovery, boosted by higher oil prices (2017) and the assumption of lower corporate taxes (2018). At the same time, rising interest rates are expected to partially offset these effects, by moderating the rebound in capital expenditures and demand for housing. Robust domestic demand together with the strong dollar are set to contribute to an increase in the current account deficit (to 3.3% of GDP in 2018) and the widening of the negative contribution from net exports to economic growth (to -0.5 pps).

On the whole, GDP growth is forecast to increase from 1.6% in 2016 to around 2¼% in the 2017-18 period. Compared to the winter forecast, a 0.1 pps. downward revision in 2017 was offset by a commensurate upward revision in 2018, reflecting the assumed delay in implementation of the fiscal stimulus.

Fiscal deficit and debt set to deteriorate...

Assumed tax cuts of around 1% of GDP will impact materially the fiscal outlook from 2018 onward. The general government deficit is thus forecast to widen to around 5% of GDP by 2018 and debt levels are expected to reach almost 110% of GDP by 2018.

...while other risks have increased.

The principal downside risk facing the US economy is a potential shift of economic policy, including on trade and immigration, towards a more protectionist stance, implying significant losses for the US and global economy. There is also a growing risk of a backlash in sentiment should fiscal stimulus or other pro-growth policies fail to materialise or be significantly delayed. Increasing risks are also related to upcoming fiscal negotiations (current and next year's federal budget, debt ceiling) which could turn disruptive and weigh heavily on sentiment. On the upside, the size and composition of the fiscal package and other growth-enhancing measures could still be greater than currently assumed.

Table II.34.1:

Main features of country forecast - USA

	2015			Annual percentage change						
bn USD		Curr. prices	% GDP	97-12	2013	2014	2015	2016	2017	2018
GDP		18036.6	100.0	2.4	1.7	2.4	2.6	**1.6**	**2.2**	**2.3**
Private Consumption		12283.7	68.1	2.7	1.5	2.9	3.2	**2.7**	**2.4**	**2.8**
Public Consumption		2604.9	14.4	1.5	-2.4	-0.7	1.6	**0.8**	**0.6**	**1.5**
Gross fixed capital formation		3576.6	19.8	2.2	3.0	4.2	3.7	**0.7**	**3.1**	**3.3**
of which: equipment		1217.5	6.8	4.5	3.2	4.6	3.0	**-2.3**	**1.7**	**3.1**
Exports (goods and services)		2264.3	12.6	4.4	3.5	4.3	0.1	**0.4**	**3.0**	**3.5**
Imports (goods and services)		2786.3	15.4	5.0	1.1	4.4	4.6	**1.2**	**4.8**	**6.1**
GNI (GDP deflator)		18242.3	101.1	2.6	1.7	2.3	2.3	**1.5**	**2.2**	**2.3**
Contribution to GDP growth:	Domestic demand			2.6	1.2	2.7	3.1	**2.1**	**2.4**	**2.8**
	Inventories			0.0	0.2	-0.1	0.2	**-0.4**	**0.2**	**0.0**
	Net exports			-0.2	0.3	-0.1	-0.7	**-0.1**	**-0.3**	**-0.5**
Employment				-	1.0	1.6	1.7	**1.7**	**1.1**	**0.7**
Unemployment rate (a)				6.0	7.4	6.2	5.3	**4.9**	**4.6**	**4.5**
Compensation of employees / f.t.e.				3.4	1.5	2.8	3.0	**2.3**	**3.5**	**4.0**
Unit labour costs whole economy				1.7	0.8	2.0	2.0	**2.4**	**2.3**	**2.3**
Real unit labour cost				-0.2	-0.8	0.2	1.0	**1.1**	**0.4**	**0.1**
Saving rate of households (b)				10.4	10.6	11.2	11.4	**11.9**	**11.8**	**12.0**
GDP deflator				2.0	1.6	1.8	1.1	**1.3**	**1.9**	**2.2**
Consumer-price index				2.4	1.5	1.6	0.1	**1.3**	**2.2**	**2.3**
Terms of trade goods				-0.4	0.7	-0.2	2.3	**0.1**	**-0.6**	**-0.4**
Trade balance (goods) (c)				-4.6	-4.4	-4.5	-4.4	**-4.1**	**-4.5**	**-4.8**
Current-account balance (c)				-3.5	-2.2	-2.3	-2.6	**-2.5**	**-2.8**	**-3.3**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-3.4	-2.2	-2.3	-2.6	**-2.5**	**-2.8**	**-3.3**
General government balance (c)				-5.0	-5.4	-4.8	-4.2	**-4.8**	**-4.7**	**-5.2**
Cyclically-adjusted budget balance (d)				-	-	-	-	**-**	**-**	**-**
Structural budget balance (d)				-	-	-	-	**-**	**-**	**-**
General government gross debt (c)				70.0	104.6	104.6	105.2	**107.4**	**107.8**	**108.7**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.

(*) Employment data from the BLS household survey.