34. THE UNITED STATES OF AMERICA

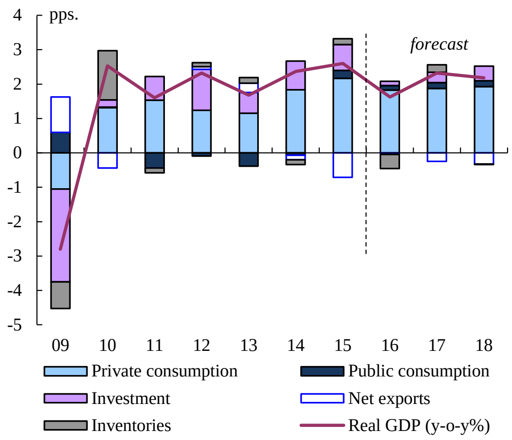
Fiscal stimulus boosts near-term outlook amid rising uncertainties

US economic growth is forecast to pick up from 1.6% in 2016 to 2.3% and 2.2% in 2017 and 2018, respectively. The near-term outlook has been revised up in line with assumptions concerning fiscal stimulus measures. Nonetheless, the economic cycle is maturing and risks to the outlook have increased, particularly given the uncertain future policy directions of the new Administration among key areas.

Strong rebound from weak first half of 2016

Following a weak first half of the year, activity in the US rebounded strongly in the third quarter. Real GDP growth accelerated to 0.9% (q-o-q) to moderate to 0.5% (q-o-q) in the fourth quarter (in the advance estimate), as private consumption continued at a robust pace and drags from energy investment and inventories began to dissipate. Key drivers of the US economy, including private consumption, the labour market and business investment, appear to be in place to sustain this relatively strong momentum into 2017.

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



Election result has increased policy uncertainty

The Presidential election has greatly increased uncertainty regarding the future course of US domestic and foreign policies. Throughout the election campaign, the new president proposed numerous tax cuts, increased infrastructure investment, deregulation, a tougher stance on immigration, repeal of the Affordable Care Act and greater protection of US manufacturing from foreign competition. How these announcements translate into concrete policy actions still remains to be seen and will impact the US outlook over the forecast horizon and beyond. Overall, however, while the fiscal stimulus would likely boost growth in the short term, a shift towards more protectionist policies has the potential to dampen medium-term growth prospects.

Initial reactions from financial markets to the new Administration's stimulus and deregulatory proposals have been positive, with consumer and businesses confidence also rising to multi-year highs. While there is a risk that this investor optimism may reverse (e.g. if actual policies fall short of expectations), improved confidence, if sustained, has the potential to materially impact on both consumption and investment levels.

Near-term outlook boosted by fiscal stimulus...

Although there is growing anticipation of a stimulus package in the near term, details of its size, timing and composition remain unclear. This forecast is therefore based on a technical assumption that stimulus of around ⅓% of GDP is implemented in 2017, followed by an additional 1% of GDP in 2018. Although providing a boost to growth, its benign impact would be constrained by the already advanced stage of the US cycle, with the labour market entering 2017 at close to full employment. The re-emergence of upward wage pressures over recent months further points to limited remaining slack.

...offset in part by tightening monetary policy.

The trend of gradually firming wage and price pressures, visible throughout 2016, is thus set for a marked upgrade. Assisted in part by rising energy prices, consumer price inflation is expected to rise from 1.3% in 2016 to around 2.5% in 2017 and 2018. In turn, nominal wage growth is set to double from 2016 to about 5% in 2018.

The release of these pressures is likely to trigger an accelerated monetary policy tightening cycle. As widely anticipated, the Fed raised its policy interest rate in December 2016 (to 0.5-0.75%), as well as raising its projections for its future path. Fed expectations now suggest three hikes in both 2017 and 2018, prompting dollar appreciation and US Treasury bill yields reaching 2½-year highs.

A stronger dollar and higher interest rates are expected to partially offset the growth impulse provided by fiscal stimulus. In the near term, business investment is forecast to recover in 2017 as higher oil prices support energy-related activity, while surging business sentiment has improved the outlook for capital expenditures in other sectors. However, rising financing costs are expected to begin weighing on business and residential investment from 2018 onwards.

Private consumption to remain growth driver

Strong labour market dynamics ensure that private consumption will continue to grow at robust rates over the coming period (2.5% and 2.8% in 2017 and 2018, respectively), with high wage growth providing considerable impetus. US dollar strength over the forecast horizon is also expected to contribute to a surge in import growth; while export growth, although recovering moderately in line with rising demand among trading partners, is set to be constrained. As a result of these dynamics, the current-account deficit is forecast to deteriorate by 1 pp. (to -3.5% of GDP) by 2018.

On the whole, GDP growth is forecast to increase from 1.6% in 2016 to around 2¼% in the 2017-18 period. This represents a 0.2 pps. (2017) and 0.4 pps. (2018) upward revision relative to the Autumn Forecast 2016, and largely reflects the assumed short-term impacts of fiscal stimulus. Even with this upward revision, however, the economy's signs of gradual maturation persist.

Fiscal deficit and debt set to deteriorate...

Public deficit and debt dynamics will also be materially impacted by any stimulus measures, with the deficit forecast to reach around 5½% of GDP by 2018 and debt levels resuming their upward trend to reach 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 towards a more protectionist stance, implying significant losses for the US and global economy. On the upside, the size or growth impulse arising from fiscal stimulus measures and deregulation may 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**	**2.3**	**2.2**
Private Consumption	12283.7	68.1	2.7	1.5	2.9	3.2	**2.7**	**2.5**	**2.8**
Public Consumption	2604.9	14.4	1.5	-2.4	-0.7	1.6	**0.8**	**1.1**	**1.6**
Gross fixed capital formation	3576.6	19.8	2.2	3.0	4.2	3.7	**0.8**	**3.3**	**3.0**
of which: equipment	1217.5	6.8	4.5	3.2	4.6	3.0	**-2.2**	**1.4**	**2.6**
Exports (goods and services)	2264.3	12.6	4.4	3.5	4.3	0.1	**0.4**	**2.1**	**3.4**
Imports (goods and services)	2786.3	15.4	5.0	1.1	4.4	4.6	**1.1**	**4.8**	**6.3**
GNI (GDP deflator)	18242.3	101.1	2.6	1.7	2.3	2.3	**1.5**	**2.3**	**2.2**
Contribution to GDP growth: Domestic demand			2.6	1.2	2.7	3.1	**2.1**	**2.5**	**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**	**-0.4**	**-0.5**
Employment			-	1.0	1.6	1.7	**1.7**	**1.0**	**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**	**3.6**	**4.9**
Unit labour costs whole economy			1.7	0.8	2.0	2.0	**2.5**	**2.3**	**3.3**
Real unit labour cost			-0.2	-0.8	0.2	1.0	**1.1**	**0.2**	**0.9**
Saving rate of households (b)			10.4	10.6	11.2	11.4	**11.9**	**11.6**	**11.6**
GDP deflator			2.0	1.6	1.8	1.1	**1.3**	**2.0**	**2.4**
Consumer-price index			2.4	1.5	1.6	0.1	**1.3**	**2.4**	**2.5**
Terms of trade goods			-0.4	0.7	-0.2	2.3	**0.1**	**-0.7**	**-0.9**
Trade balance (goods) (c)			-4.6	-4.4	-4.5	-4.4	**-4.1**	**-4.5**	**-4.9**
Current-account balance (c)			-3.5	-2.2	-2.3	-2.6	**-2.5**	**-3.0**	**-3.5**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-3.5	-2.2	-2.3	-2.6	**-2.5**	**-3.0**	**-3.5**
General government balance (c)			-5.0	-5.4	-4.8	-4.2	**-4.8**	**-5.1**	**-5.7**
Cyclically-adjusted budget balance (d)			-	-	-	-	**-**	**-**	**-**
Structural budget balance (d)			-	-	-	-	**-**	**-**	**-**
General government gross debt (c)			70.0	104.6	104.6	105.2	**107.3**	**108.5**	**109.6**

(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.