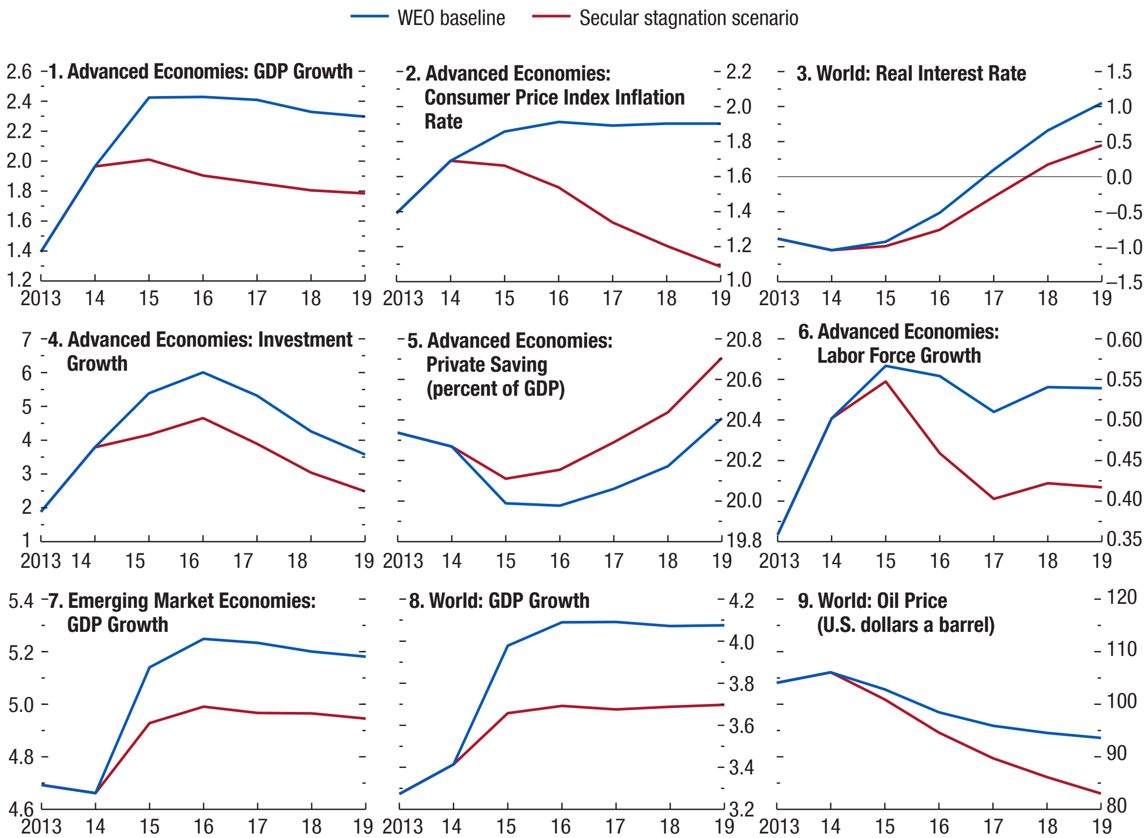
Figure 1.14. Secular Stagnation

(Percent, unless indicated otherwise)

The IMF's G20 Model (G20MOD) is used here to explore a plausible alternative baseline with secular stagnation in advanced economies. The sources of stagnation are lower-than-expected private investment and higher-than-expected private saving, which lead to weaker domestic demand in advanced economies. Investment growth slows by just under 0.5 percentage point a year in the euro area and Japan; it slows by more than 1 percentage point a year in the United States and other advanced economies. Private saving as a share of GDP rises by about 0.2 percentage point a year in advanced economies. Weaker demand conditions in turn have negative spillovers to these economies' potential output. Given capital-embodied technology, lower investment results in slowing productivity growth. In addition, higher unemployment results in skill erosion that raises the natural rate of unemployment, and the labor force decreases as discouraged workers withdraw from the labor force. Overall, the labor supply decreases by roughly 0.1 percent a year in advanced economies.

As a result, growth in advanced economies is roughly 0.5 percentage point below the WEO baseline, while inflation is about 0.8 percentage point lower after five years. Slower advanced economy growth has significant spillovers to emerging market economies, both directly, through lower external demand, and indirectly, because equity markets in emerging market economies are assumed to reflect some of the weakness in advanced economy equity markets. Global growth is roughly 0.4 percentage point below the WEO baseline.



Sources: IMF, G20MOD simulations; and IMF staff estimates.