Economic hit softer than expected: OECD

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Australia's recession will be less severe than expected but its recovery will depend on continuing fiscal support and no return to severe lockdowns, the Organisation for Economic Co-operation and Development says.

The Paris-based OECD also pointed to the need for industrial relations and tax reforms to ensure employment growth.

In fresh forecasts issued last night, the OECD said Australia's first recession in 29 years would see economic output contract 4.1 per cent this year, better than its June forecast of a 5 per cent contraction.

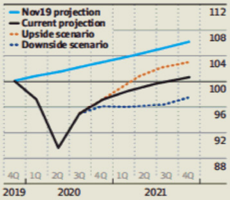
However, the local economy is tipped to rebound only 2.6 per cent in 2021, down from an earlier projection of a 4.1 per cent bounce.

The forecasts assume sporadic local outbreaks of COVID-19 will continue, but there will not be further, severe lockdowns.

The report pointed to renewed lockdowns such as Victoria's dragging on the recovery and said forecasts could be downgraded if further severe lockdown measures were imposed.

Plan B

World GDP (index, 4Q19=100)



Real GDP growth, 2020 (% YoY)

	Interim EO projections	Difference from Jun^ (ppts)
China	1.8	4.4
US	-3.8	3.5
Canada	-5.8	2.2
World	-4.5	1.5
UK	-10.1	1.4
Euro area	-7.9	1.2
Australia	-4.1	0.9
Japan	-5.8	0.2
India	-10.2	-6.5

^Single-hit scenario

SOURCE: OECD

"Localised lockdowns, border closures and new restrictions being imposed in some countries to tackle renewed virus outbreaks are likely to have contributed to the recent moderation of the recovery in some countries, such as Australia," it said.

The OECD modelled two scenarios of the global economy outside of its base case.

"On the downside, confidence could remain weak for an extended period, and uncertainty deepen, if COVID-19 outbreaks were to intensify, or more stringent containment measures were required to control their spread.

"Illustrative simulations of this downside risk scenario suggest that it could reduce global growth by between 2-3 percentage points in 2021, halving the global growth rate projected for 2021 in the baseline."

However, the OECD's "upside" scenario sees consumer and business confidence improve more quickly than assumed if "only mild containment measures were required to control new virus outbreaks". It estimates that if this were to be the case, stronger household spending and higher business investment would help lower unemployment by around 1 percentage point in the major advanced economies.

Less than three weeks before the Morrison government's budget, the report warned fiscal supports had to be maintained and not tightened too early.

"Premature withdrawal of fiscal support in 2021 would stifle growth, as occurred in the aftermath of the global financial crisis in many countries.

"At the same time, governments need to reassess and adapt the design and balance of support measures, ensuring that they are well targeted, closely monitored, and reduced gradually as the recovery progresses to facilitate the necessary reallocation of labour and capital towards sectors with better long-term prospects."

A "delicate balance" had to be struck between facilitating the immediate recovery by supporting viable jobs and companies, and ensuring that policy allowed for sufficient flexibility when reallocating resources across sectors.

"Reforms to reduce barriers to labour mobility, such as occupational licensing restrictions and housing market rigidities, would also help to facilitate job reallocation and reduce the chances of persistent scarring effects."

Worldwide GDP is also now expected to fall 4.5 per cent this year, less severe than the 6 per cent contraction the OECD forecast in June, but still the largest projected in 60 years. Upgrades to China and the United States were the biggest contributors to the new world GDP forecast.