- The Euro area economy has been picking up, although its pace has slowed down. Economic situations in the Euro area vary across countries (Fig. 1). Since the April-June quarter 2014, Germany has lost growth momentum, while Italy continued negative growth. Spain has maintained positive growth as its exports have increased thanks to improved price competitiveness gained through labor market reforms (Figs. 2 and 3).
- In response to the risk of prolonged low inflation, the European Central Bank has implemented monetary easing. A matter of concern is the negative growth of bank lending on a year-on-year basis (Fig. 4). Furthermore, reform to make the labor market more flexible is a challenge for achieving sustained growth.
- The impact of economic sanctions against Russia on exports has been limited (Fig. 5). Rather, the impact of economic sanctions against Russia deteriorated business confidence on investment, which is a larger cause for concern (Fig. 6).

Fig. 1 Real Economic Growth of Major Euro Area Countries

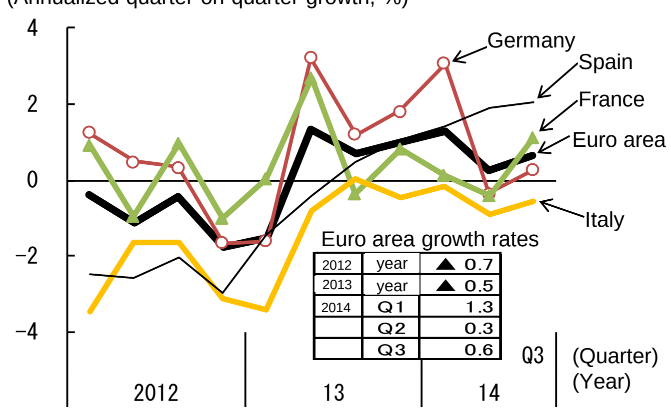


Fig. 2 Real Effective Exchange Rates

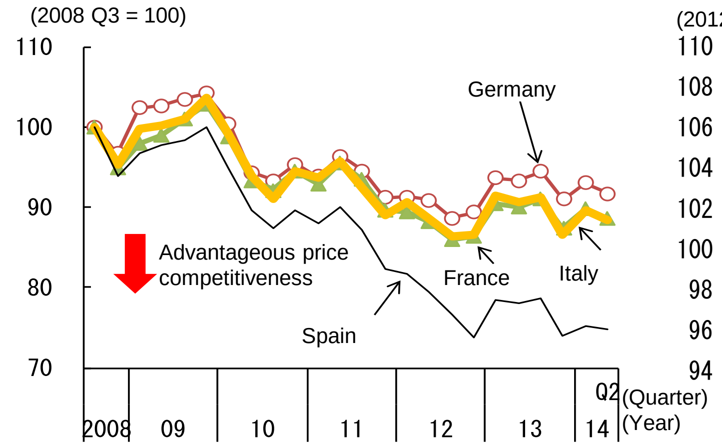


Fig. 3 Major Euro Area Countries' Exports (Goods trade)

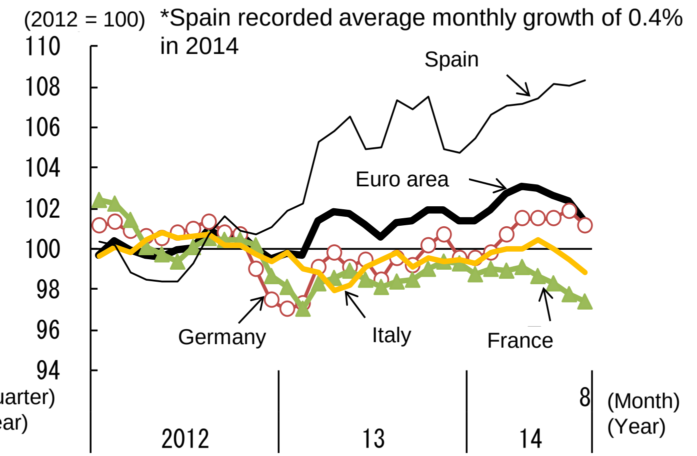


Fig. 4 Euro Area Bank Lending (Outstanding amount, year-on-year change)

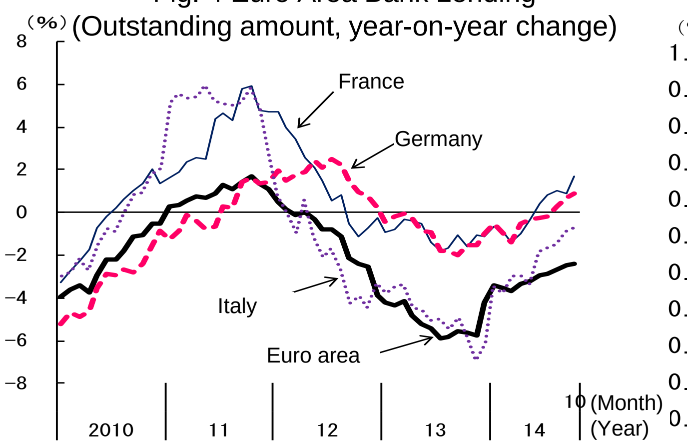


Fig. 5 Shares of Goods Subject to Embargo on Exports to Russia in Total Exports

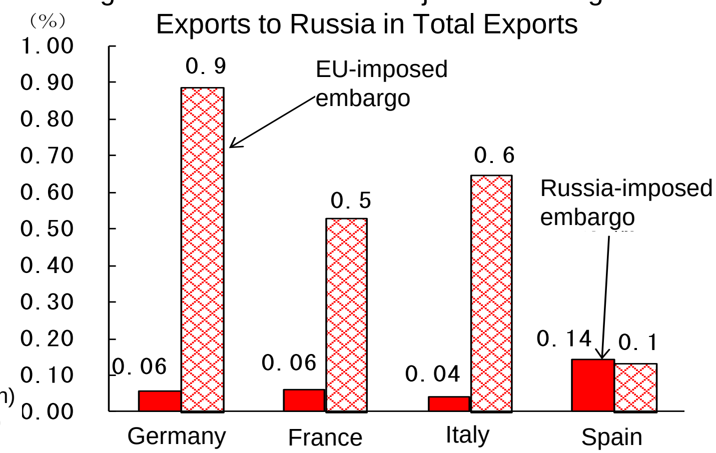
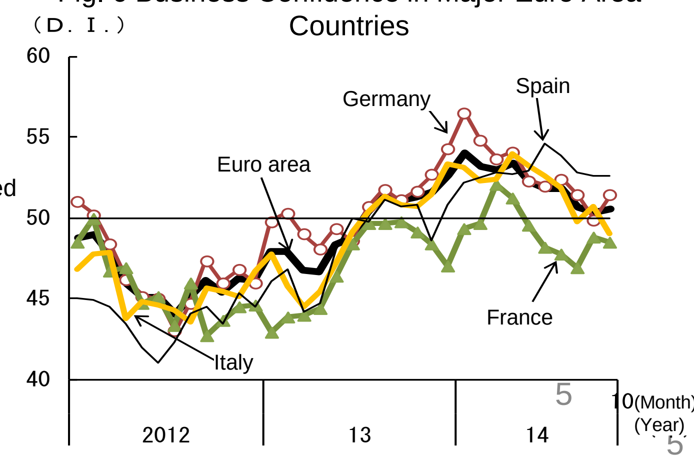
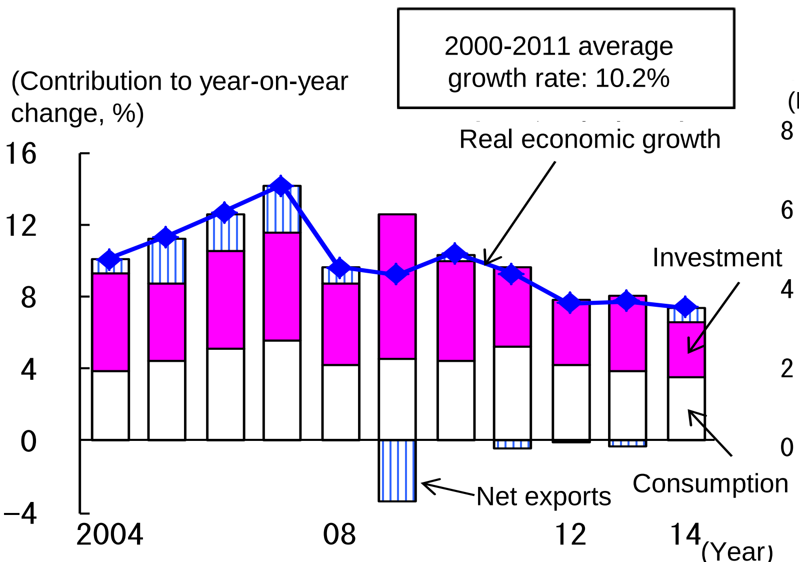


Fig. 6 Business Confidence in Major Euro Area Countries



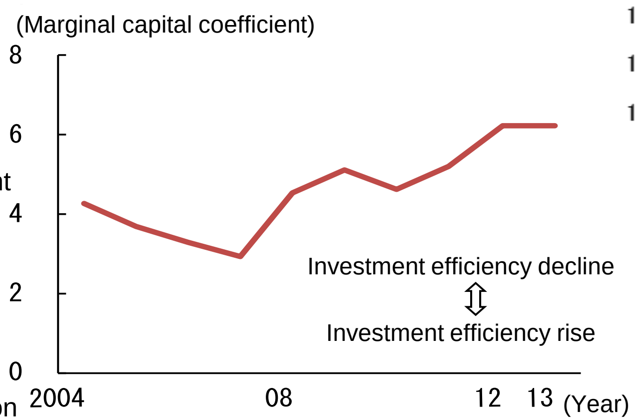
- China achieved double-digit economic growth over decades (Fig. 1). As the high growth depended on exports and investment, overinvestment and excess credit emerged as structural problems. While exports slackened after the global financial crisis, China implemented large-scale economic stimulus measures and monetary easing to achieve economic recovery depending on public and private investment. As a result, overinvestment and excess credit deteriorated further (Figs. 2 and 3).
- The Xi Jinping administration, inaugurated in 2013, has proceeded with structural reforms (to eliminate excess production, capacity and credit), implementing policy management giving priority to the quality of growth. The structural reform policy has been a factor behind slower economic growth. The administration emphasizes that China has entered “the new normal” of slower growth under such policy.
- If structural reform is delayed, however, a hard-landing risk may emerge on an increase in nonperforming loans. Although growth deceleration under structural reform may affect domestic and overseas economic conditions, structural reform will be indispensable for stable growth of not only China but also the world economy.

Fig. 1 Real Economic Growth Rate and Growth Breakdown by Demand



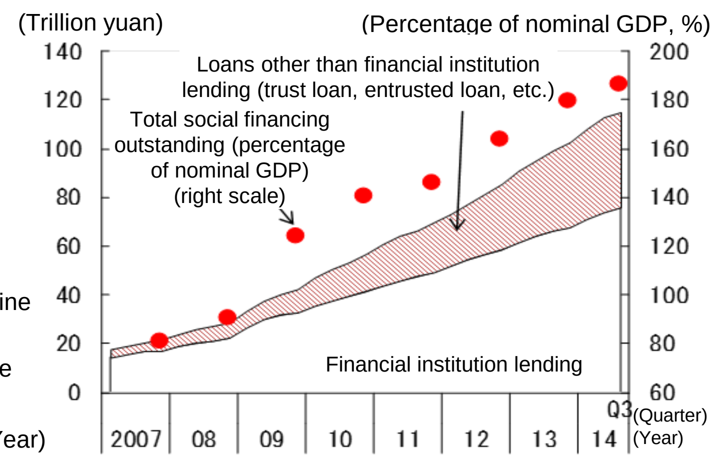
(Notes)
1. Source: National Bureau of Statistics of China
2. January-September period for 2014

Fig. 2 Investment Efficiency Deterioration (Marginal capital coefficient)



(Notes)
1. Source: National Bureau of Statistics of China
2. Dividing investment ratio (gross capital formation/nominal GDP) by real GDP growth

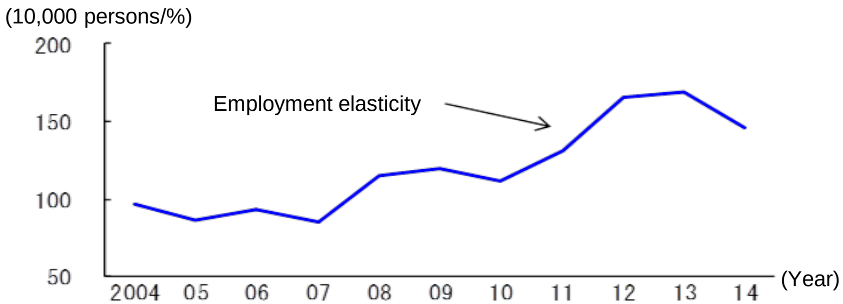
Fig. 3 Excess Credit (Total social financing outstanding)



(Notes)
1. Source: The People’s Bank of China
2. Total social financing outstanding is estimated by the accumulation since 2002.
3. Nominal GDP for September 2014 is annualized (estimated)

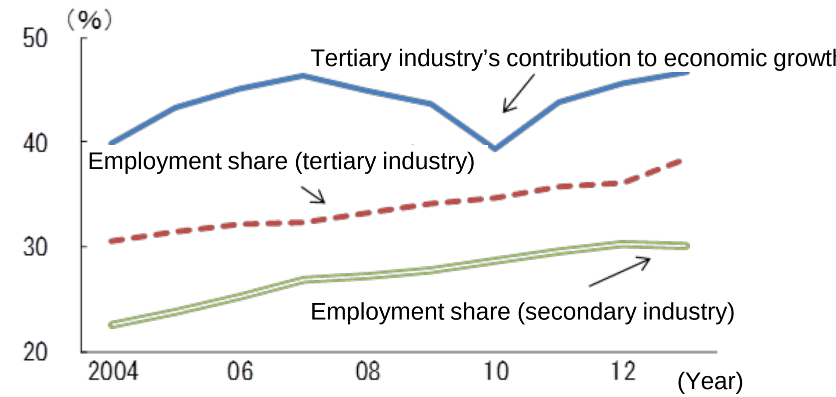
- Economic policy emphasizes stable employment and prices. Employment has increased on progress toward a service-oriented economy (Figs. 4 and 5). Prices have been stable as food prices have restored their stability (Fig. 6).
- The government plans to maintain economic growth (growth target of mid-7% in 2014) between the minimum growth for maintaining and securing employment and the maximum growth for refraining from accelerating price hikes. The government plans to implement targeted economic measures to maintain and support stable growth only if downside pressure arises on the economy (Table 7).

Fig. 4 Employment Elasticity* Rising on Progress toward a Service-oriented Economy
(*Employment growth resulting from 1% GDP growth)



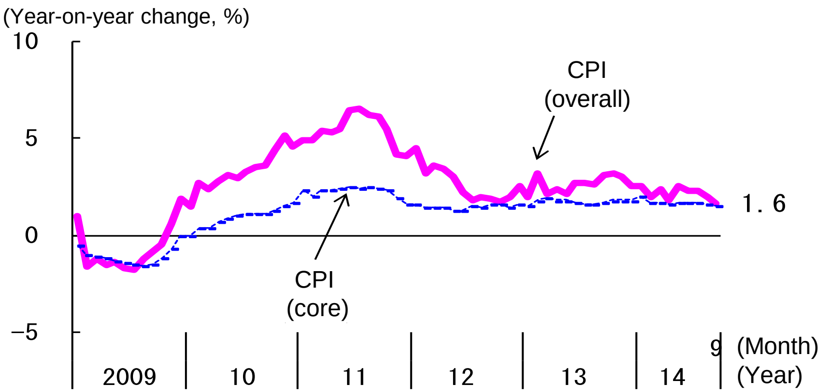
(Notes)
1. Sources: National Bureau of Statistics of China, Ministry of Human Resources and Social Security
2. Employment elasticity = Number of newly employed people / real GDP growth
3. A figure for 2014 covers the January-September total.

Fig. 5 Tertiary Industry's Contribution to Growth and Employment



(Note) Source: National Bureau of Statistics of China

Fig. 6 CPI Inflation Stabilized in Recent Years



(Note) Source: National Bureau of Statistics of China

Table 7 Targeted Economic Measures (2014)

(1) Front-loading infrastructure investment
Railway construction, etc.
(2) Supporting housing purchases
Easing housing loan regulations (easing loan regulations for second houses)
(3) Tax exemption/reduction and other support measures for enterprises
Expanded support for small and micro enterprises, corporate tax cuts
(4) Targeted monetary easing
Monetary easing for rural agriculture and small/micro enterprises