



Crisis response in the euro area

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Main elements, guiding principles and results

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How to get out of the crisis?

Different approaches in Japan and the EU towards growth

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* The opinion expressed in this presentation are those of the author and do not necessarily reflect official government positions.

The euro area economy in 2014

The good news first...

- **Confidence has returned...**

- Convergence of risk spreads; stabilising credit flows; gradual normalisation in financial markets; investment is picking up

...thanks to collective action by Member States; ECB; EU/Eurogroup (programmes; differentiated fiscal strategy; accommodative monetary policy; ESM; governance reform of EMU; Banking Union etc.)

- **Economic recovery is broadening**

- GDP forecast to expand in 2014 (1.2%) and 2015 (1.7%), including in vulnerable countries; intra-area adjustment is progressing

- **Supply side reforms show results**

The euro area economy in 2014

...the challenges and risks:

- **Recovery to remain weak**
 - unfinished deleveraging, competitiveness adjustment; lingering financial market fragmentation and uncertainty
 - too weak for strong employment creation and swift recovery of lost output
 - High unemployment could persist and affect long-term growth („hysteresis“)
- **Legacy of high level of public debt**
- **Limited policy space**
- **Bank asset quality review and stress test in 2014**
- **New risks from external environment**

The challenge

„*This time is different*“. It almost never is“. (Reinhardt & Rogoff)

but „*EMU sui generis*“ (Barry Eichengreen)

So, anything special about the euro area crisis ?

The challenge

Euro area idiosyncracies:

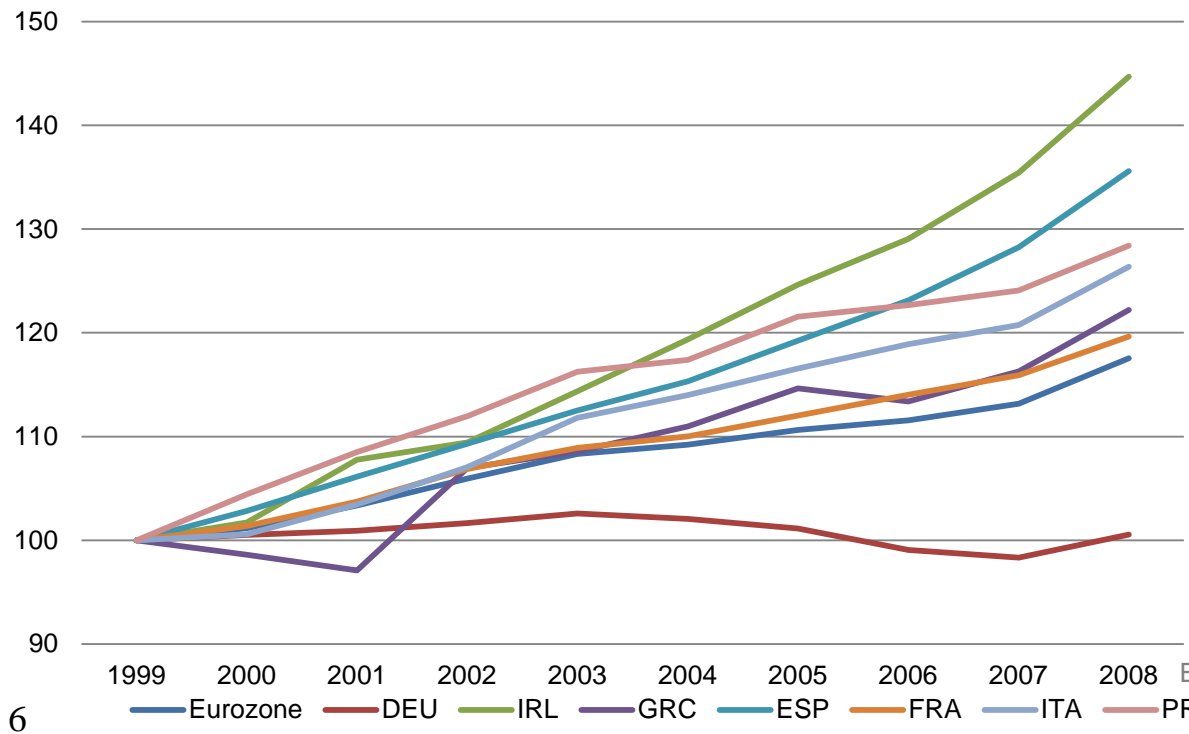
- deep economic and financial integration of 18 Member States (=> spillovers)
- single monetary policy + rules-bound decentralised fiscal and economic policies
- Common rules and institutions (Commission; fiscal surveillance)...
- ...but initial gaps in EMU architecture
 - E.g. No national „*lender of last resort*“ (=> cannot issue own debt); no significant central budget; no financial stability tool; no single supervisor
- Different macro-financial starting positions across euro area Member States, including large external/macro-structural imbalances and deeply exposed banks in some (=> vulnerabilities)



The challenge

- Vulnerable starting conditions when the crisis struck:

Nominal Unit Labour Cost
(Index, 1999=100)

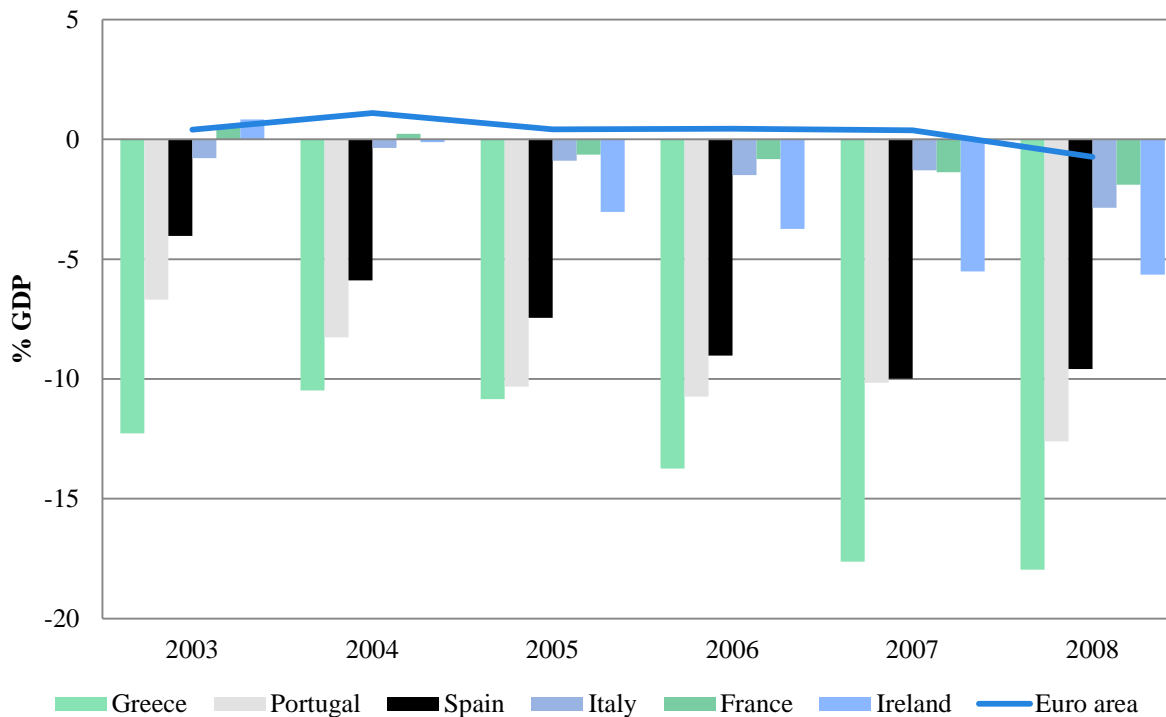


- Accumulated loss of competitiveness

The challenge

- Vulnerable starting conditions when the crisis struck:

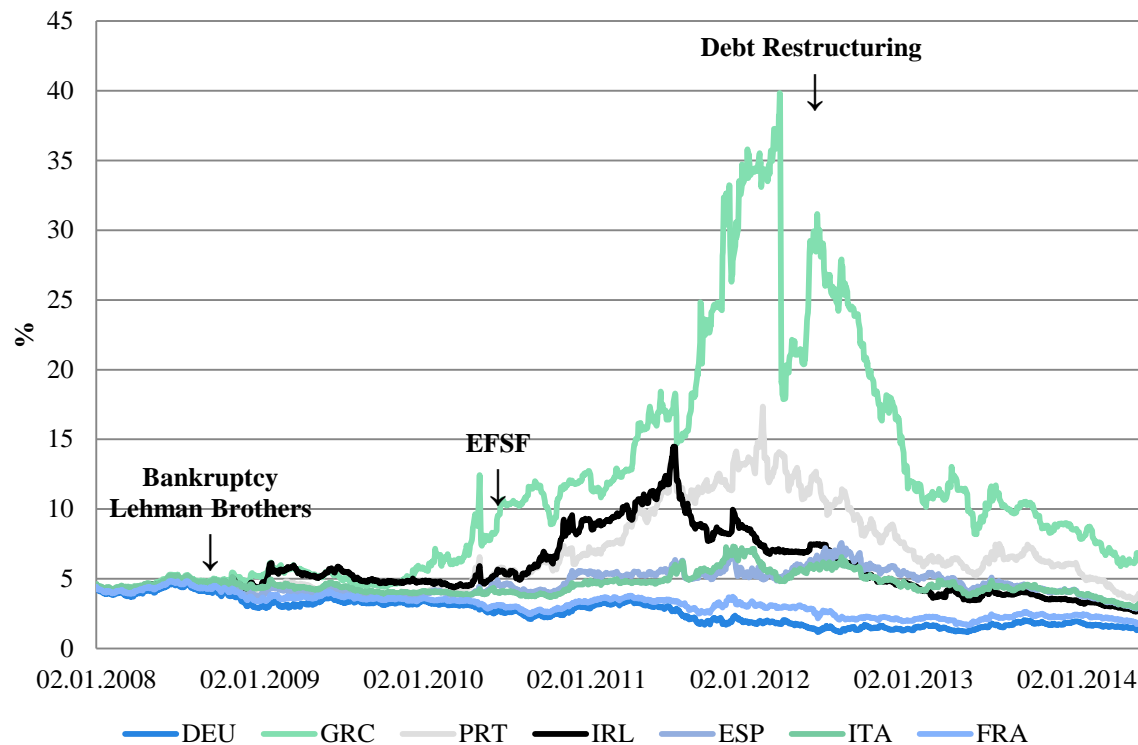
Current Account Balance



- Accumulated external imbalances
- Risk of sudden stop

The crisis impact

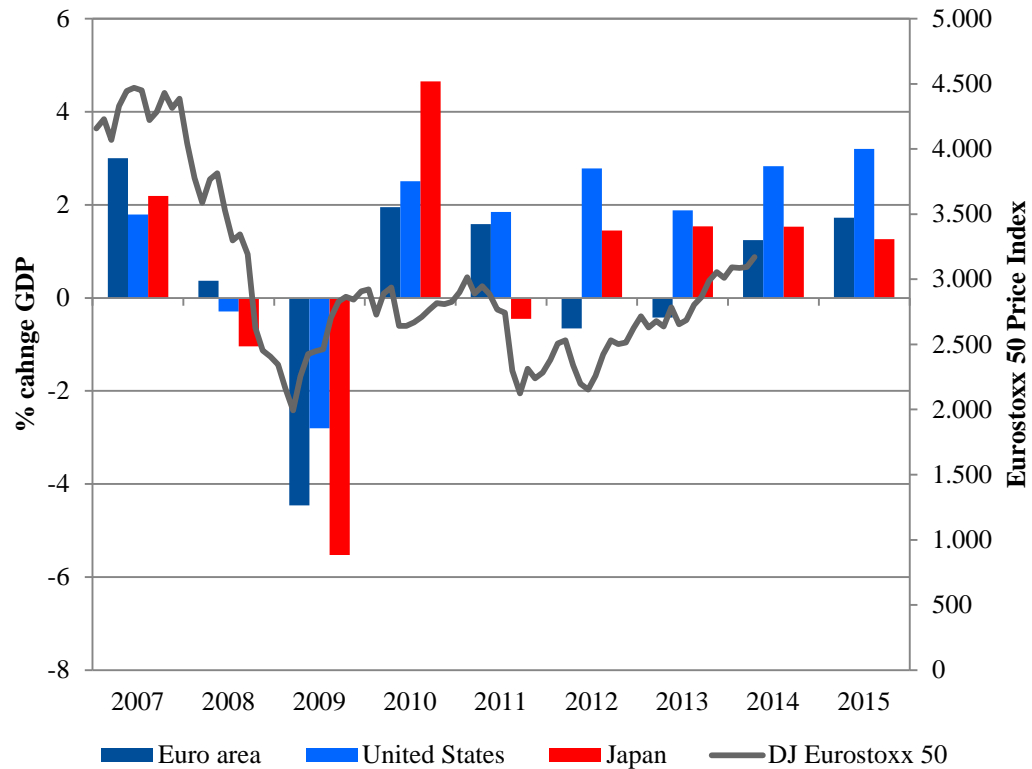
Interest Rates on Government Bonds



- Confidence evaporated
- Default risk rose
- Financing costs soared
- Bank lending reversed

The crisis impact

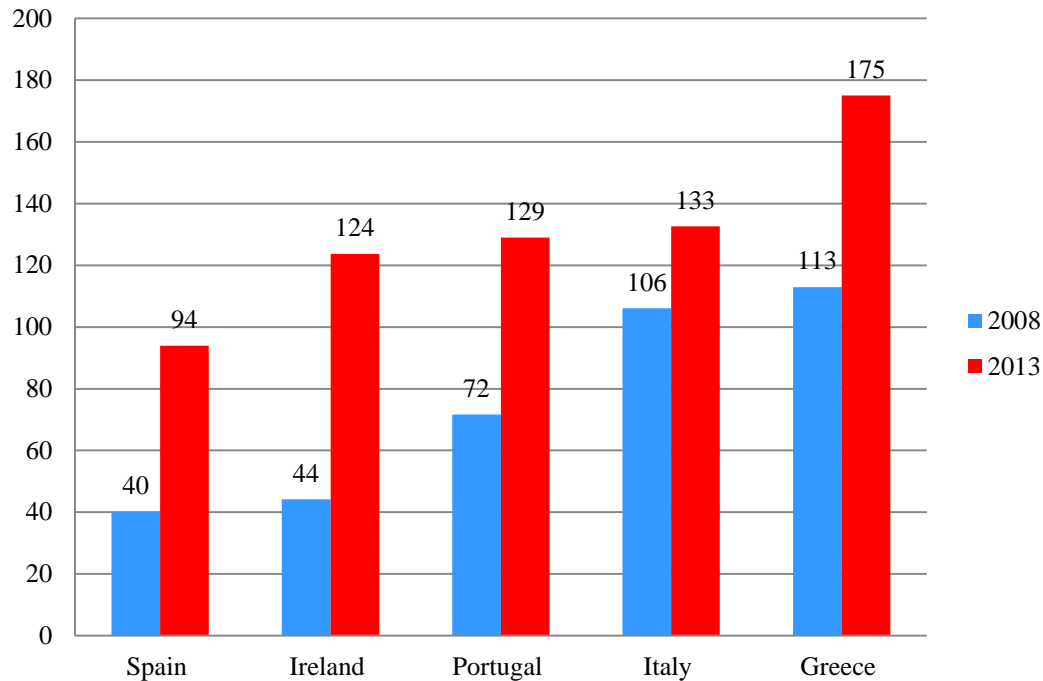
Real GDP Growth and Eurostoxx 50



- Growth slumped
- Unemployment increased
- Consumption fell and investment stopped

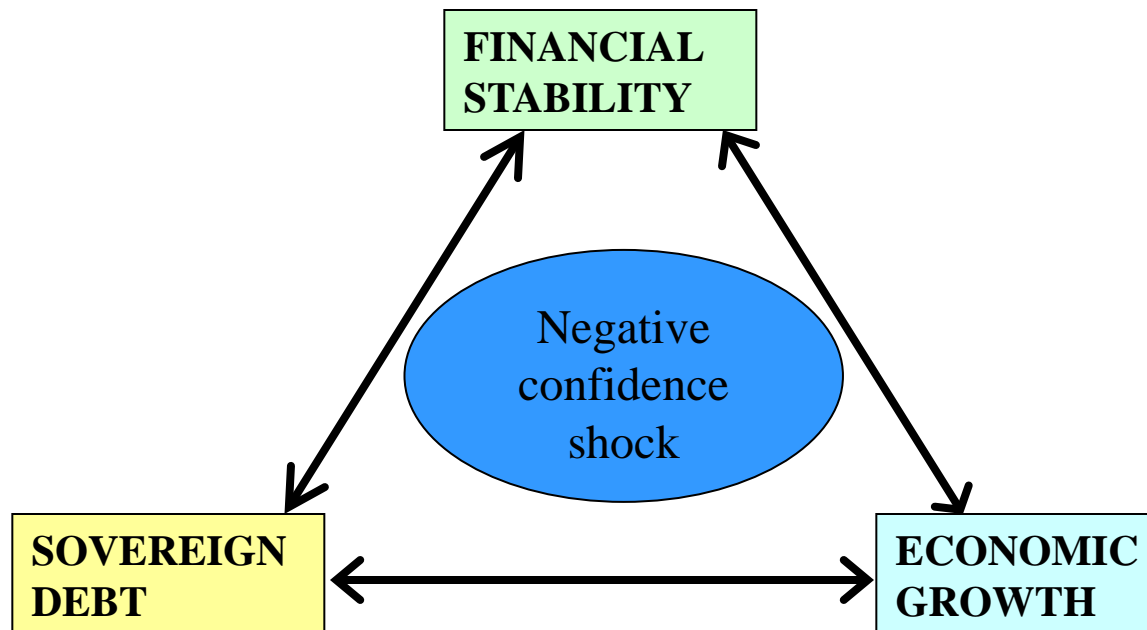
The crisis impact

Public Debt *% GDP*



- Public debt jumped
- Feeding fears of debt sustainability

The crisis impact



The crisis response – guiding principles

- safeguarding the stability of the euro area as a whole
- restoring confidence via credible measures and sustainable solutions
- addressing fundamental weaknesses via deep structural reform
- combining solidarity with conditionality, setting incentives for structural adjustment in Member States concerned
- Country-specific differentiation

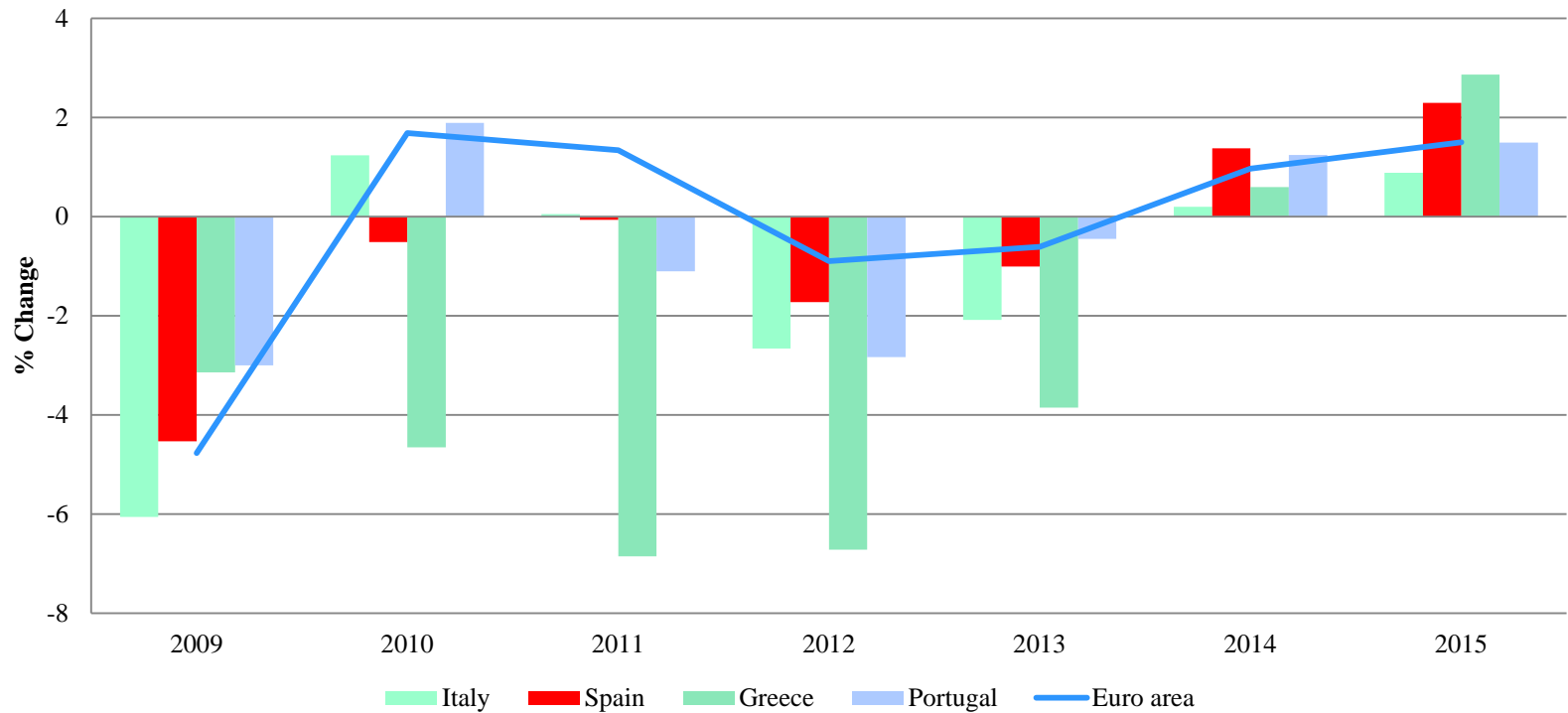
The crisis response – main elements

- **Macro response at euro area level**
 - Accommodative monetary policy + unconventional measures
 - Differentiated and time-consistent fiscal policy strategy
- **Country-specific**
 - Adjustment programmes (guided by Troika = Commission + ECB + IMF)
 - Wage constraints and structural reforms to restore competitiveness and build new foundations for sustainable growth
 - Shoring up troubled banks within EU state-aid regime
- **Institutional**
 - EFSF/ESM
 - Economic governance reform (stronger fiscal rules; new macro-imbalances tool; better economic coordination via enhanced European Semester)
 - Single Supervisory + Resolution Mechanism; Single Rule Book
 - European System of Financial Supervisors; Macro-Systemic Risk Board



A broad-based recovery is taking place

Real GDP per capita



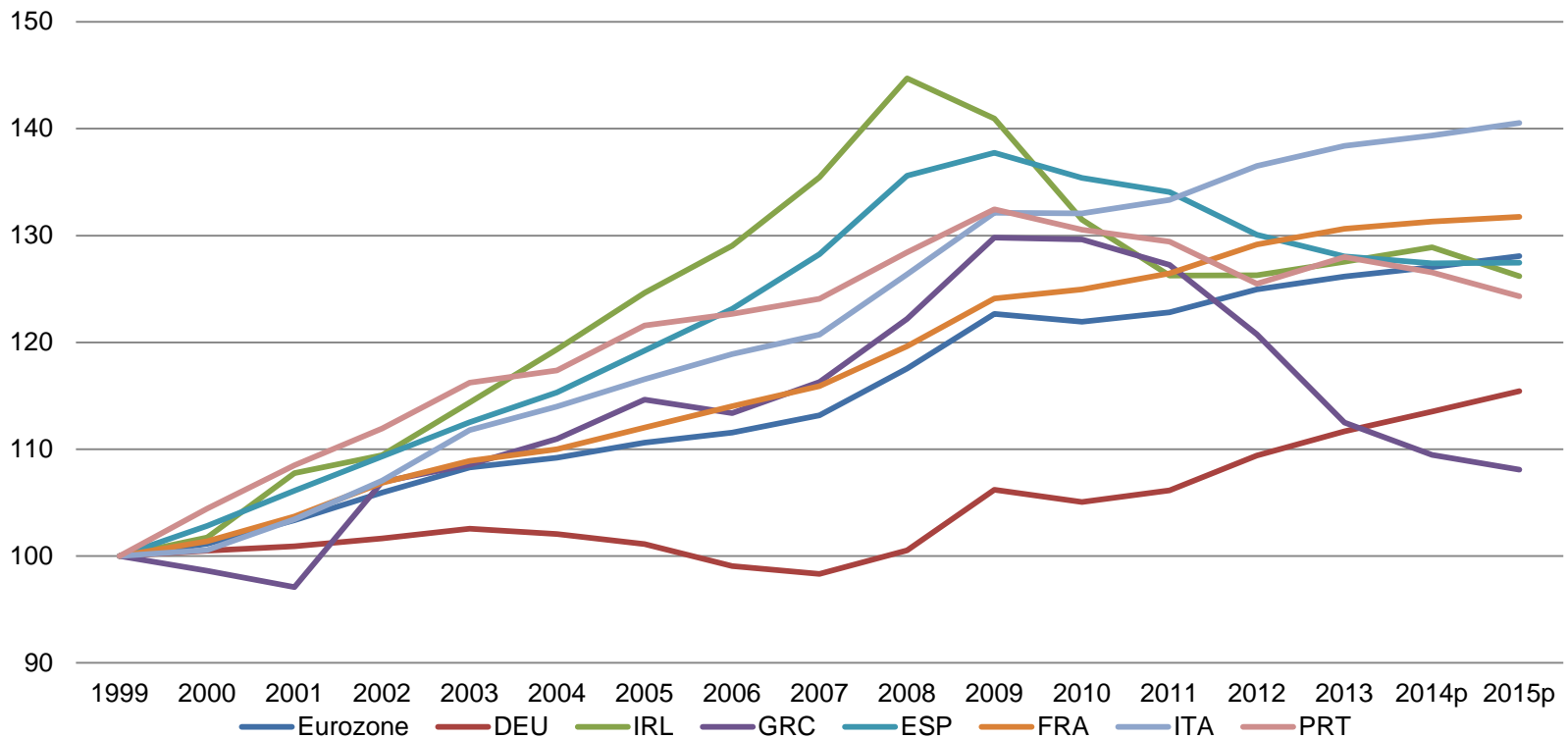
Data: AMECO Spring 2014

Supply side reforms show results

Competitiveness is improving

Nominal Unit Labour Cost

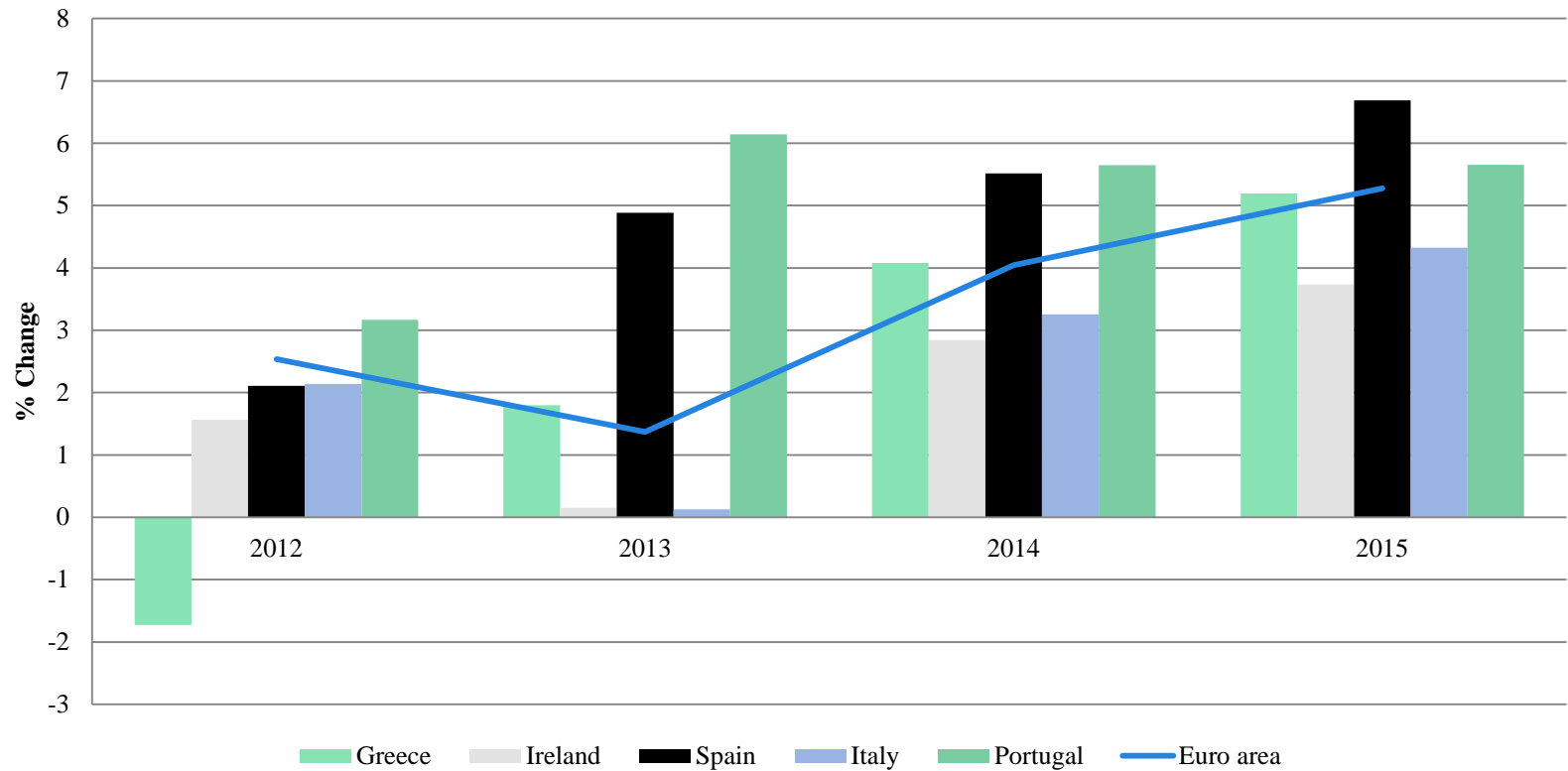
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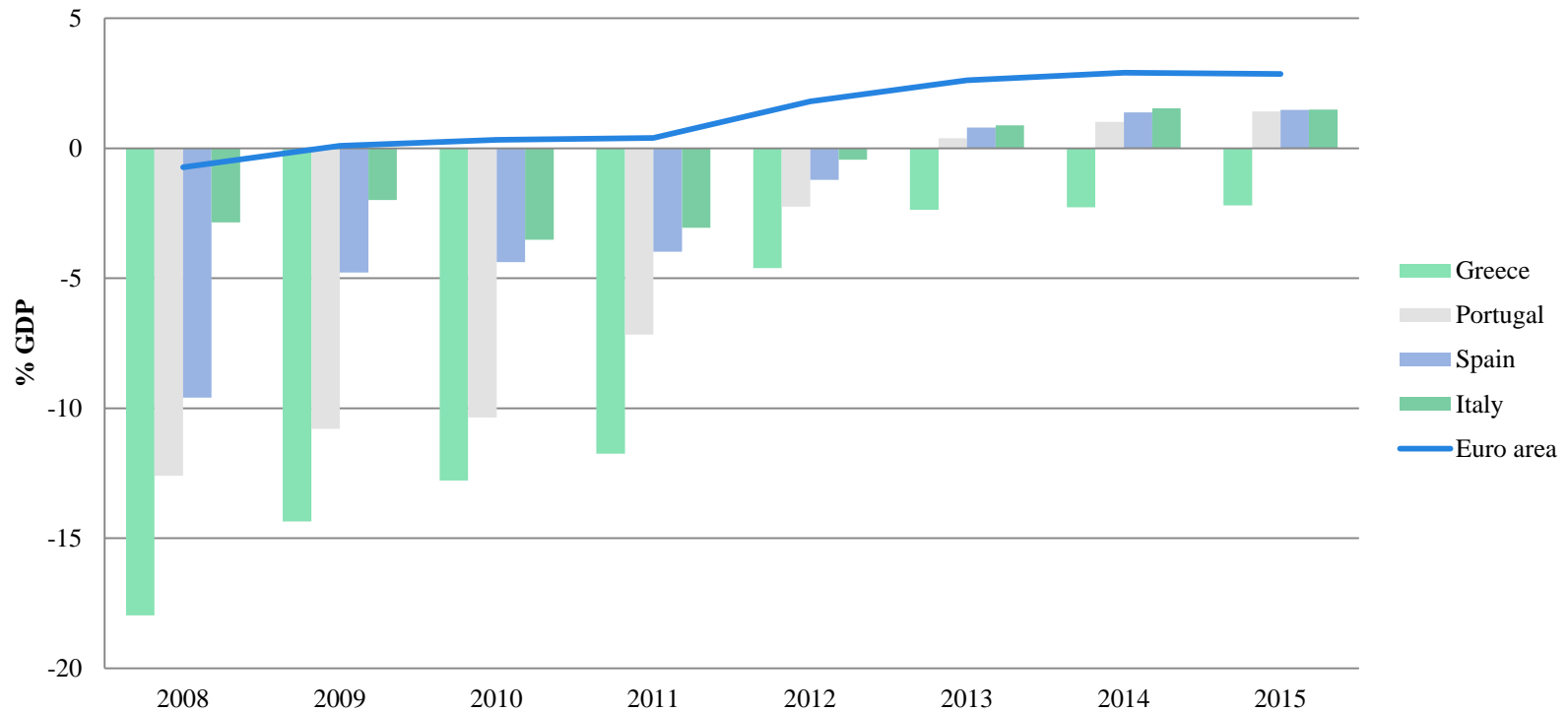
Exports are growing

Exports of Goods and Services



External imbalances are receding

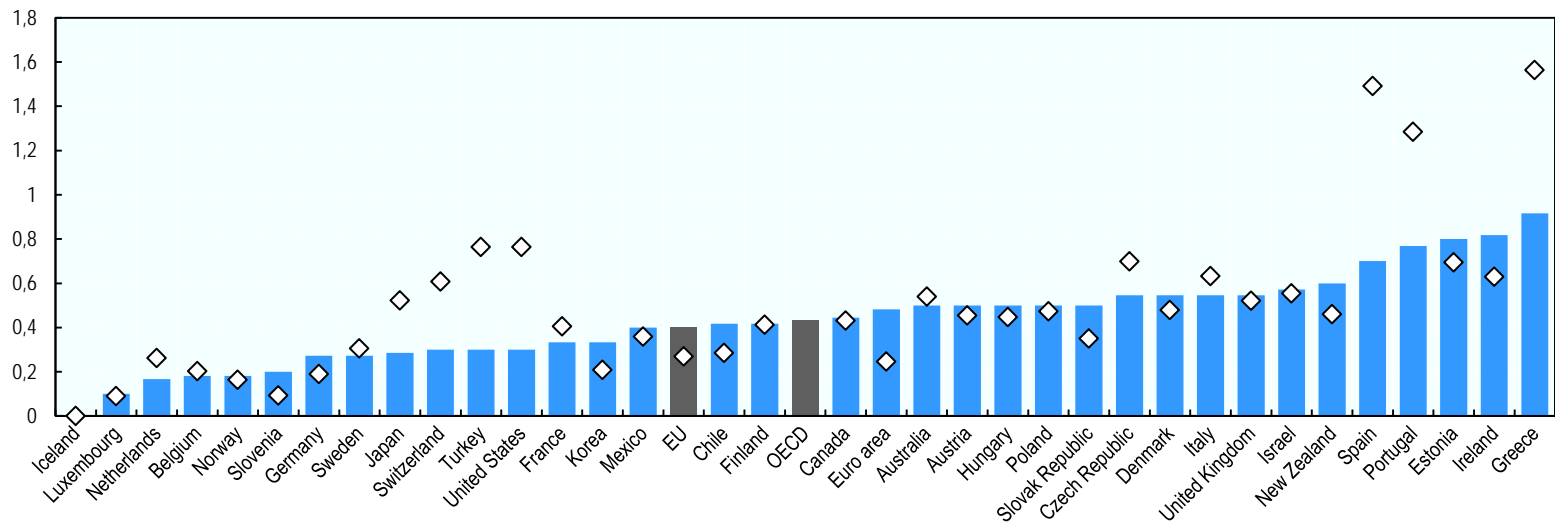
Current Account Balance



Data: AMECO Spring 2014

Reforms are progressing

Responsiveness to Going for Growth recommendations across OECD countries, 2011-12



■ Responsiveness rate

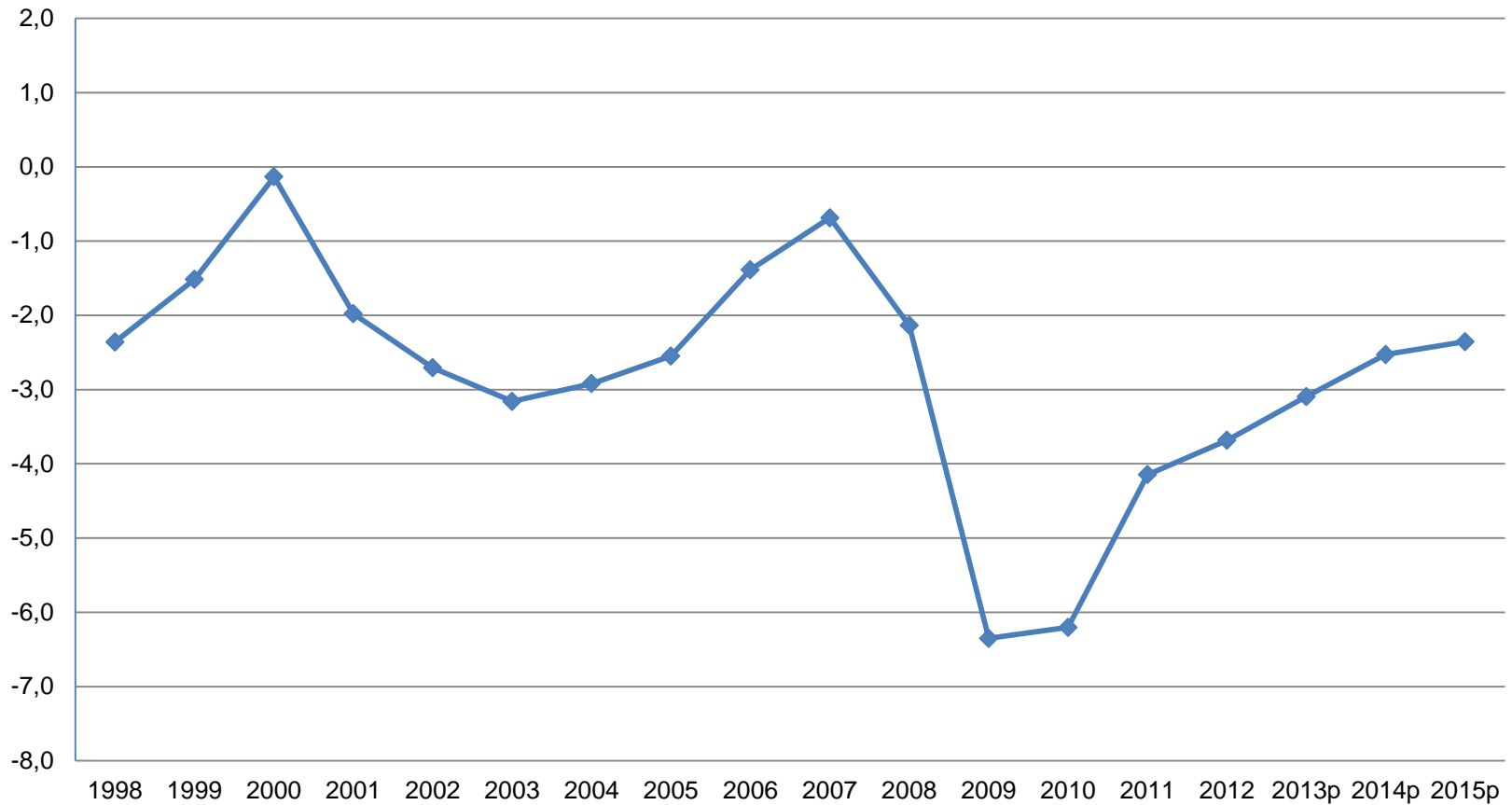
◇ Responsiveness rate adjusted for the difficulty to undertake reform

Bundesministerium der Finanzen
Berlin



Deficits decline...

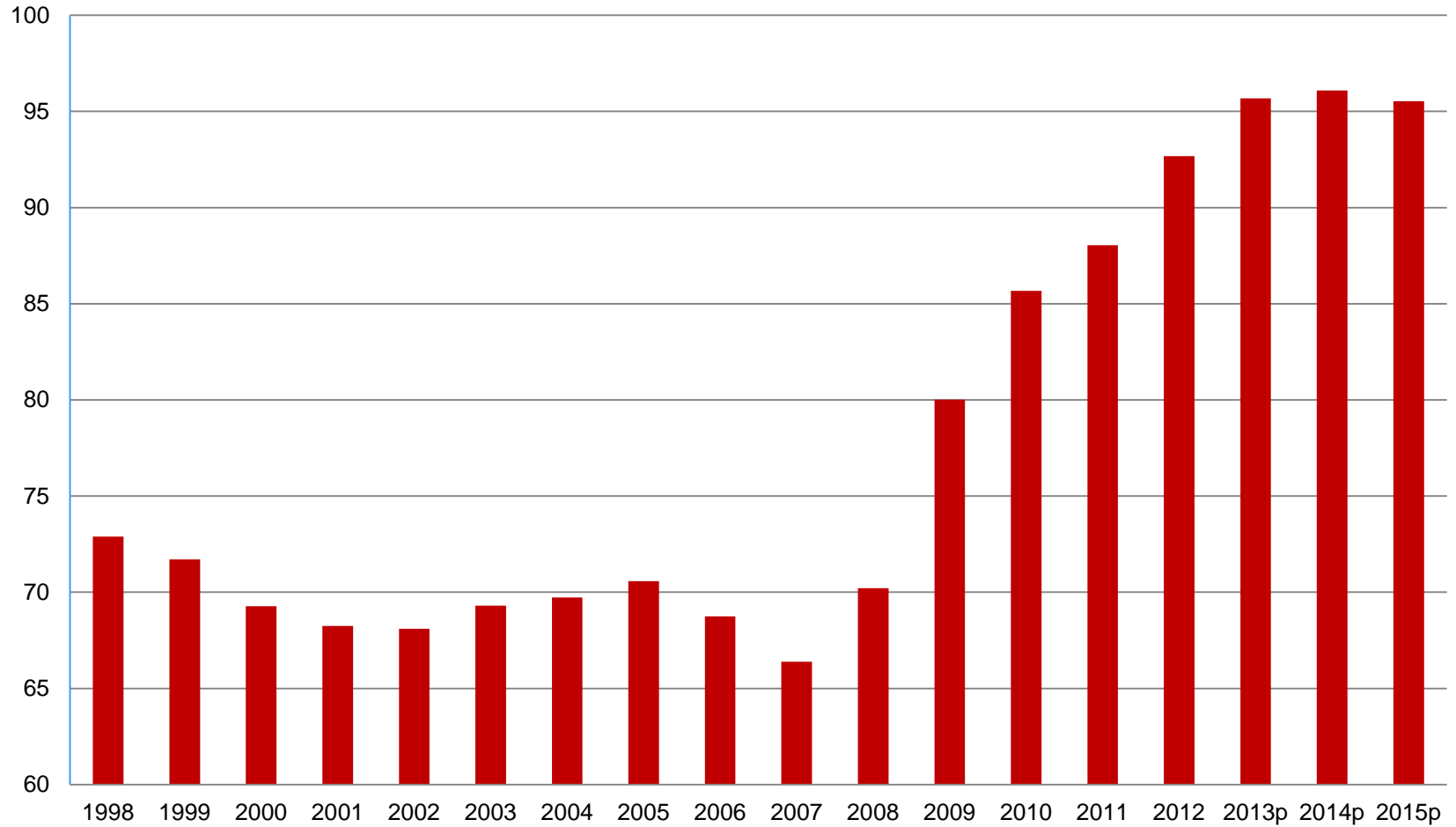
Eurozone public sector deficit in % of GDP



Source: Commission Autumn Forecast, November 2013



Eurozone public debt – high but stabilising - in % GDP-

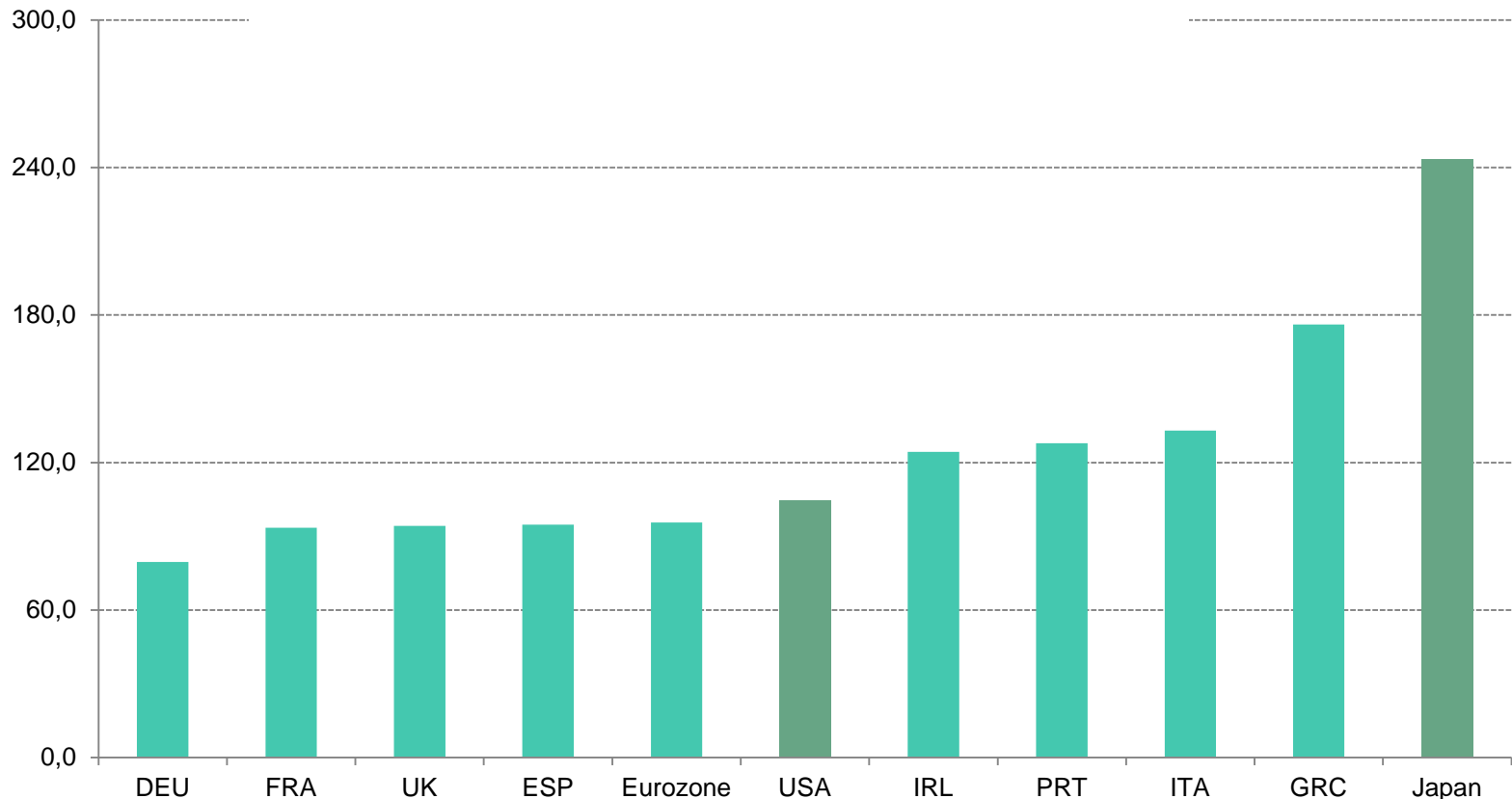


Source: Commission Autumn Forecast, November 2013



Public debt in international comparison

- 2013 in % of GDP -



Source: Commission Autumn Forecast, November 2013

The challenge ahead

- Move from recovery to sustained growth
- Maintain twin-strategy of differentiated fiscal consolidation combined with structural reforms to enhance growth and competitiveness and to bring debt levels to safe territory
- Improve the quality of public finances
 - Improve quality of consolidation
 - Raise efficiency of social security systems; public administrations etc.
- Implement Banking Union (SSM/SRM); consolidate banks
- Foster the functioning of the EU internal market

Thank you...

... for your attention!

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