



Macroeconomic imbalances: a view by the European Commission

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EC Representation, Prague.

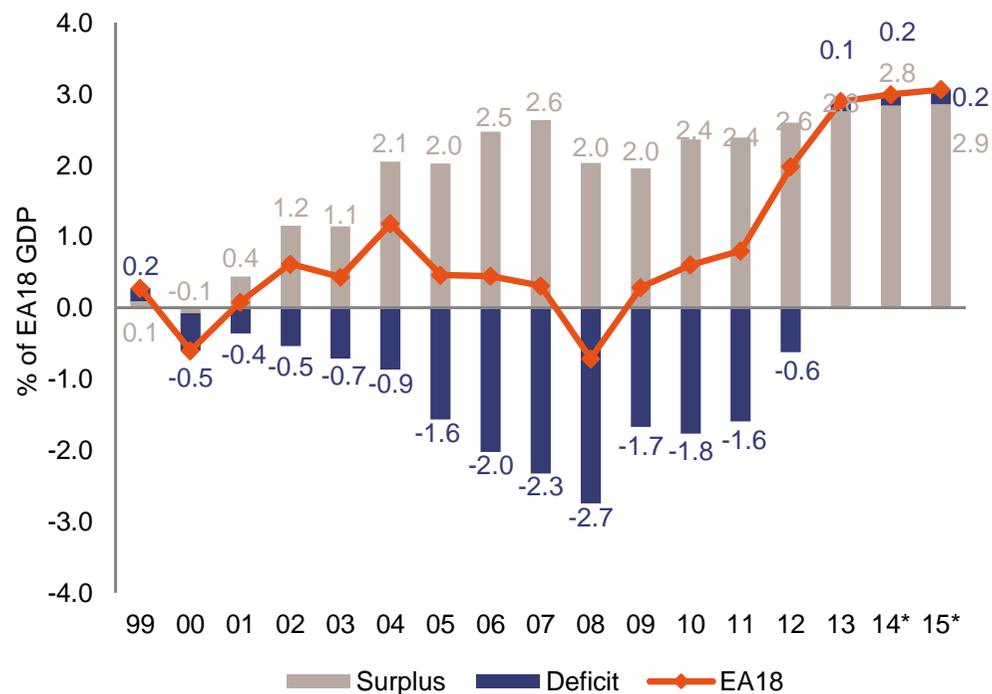
Brno, 21 November 2014



European
Commission

External imbalances

[Di/con]vergence in euro area external positions



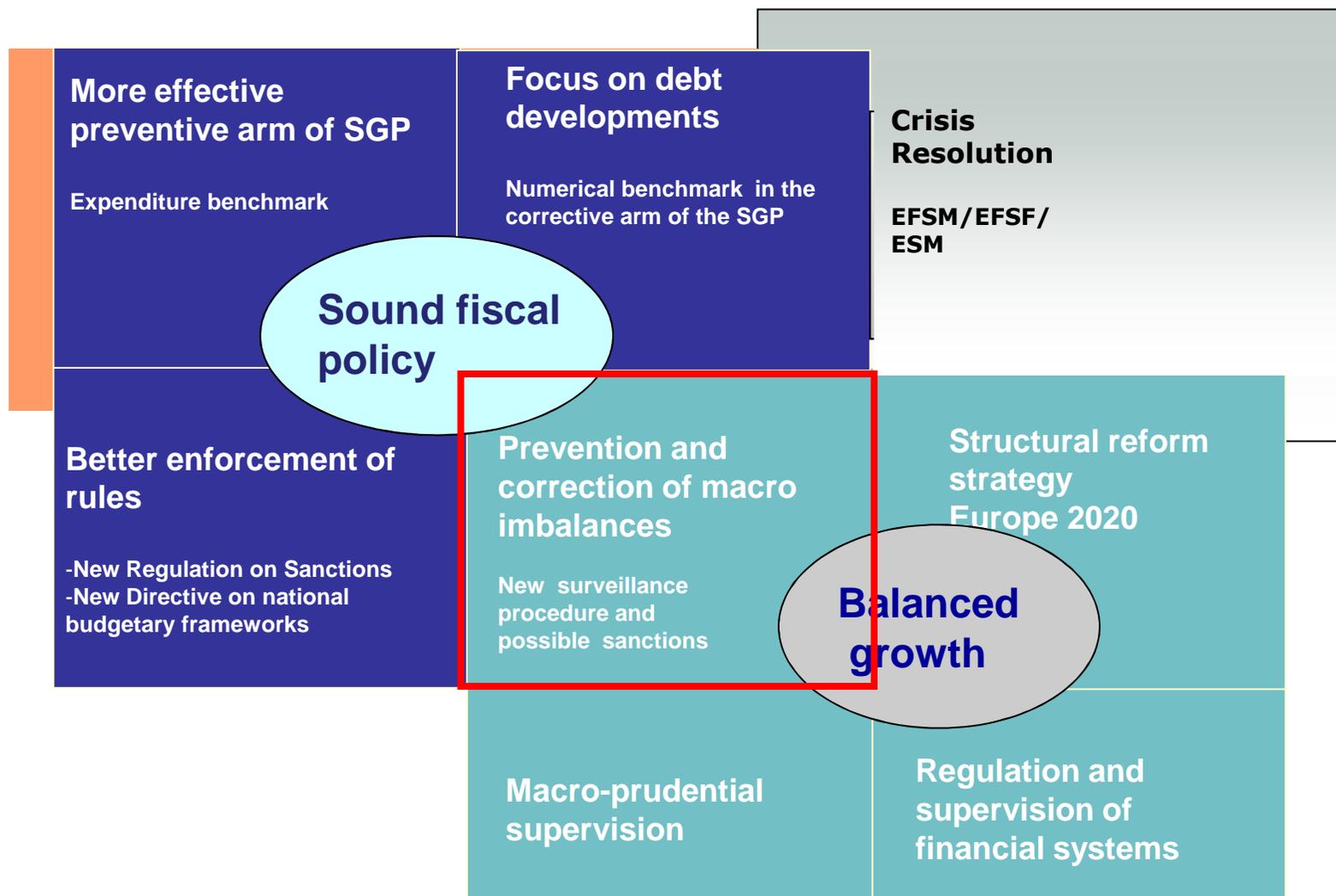
Surplus countries: AT, BE, DE, FI, NL, LU.

Note: EA - from broadly balanced current account in 2005-2009, to a surplus projected at around 2.5% of GDP in 2014-2016 (COM Autumn 2014 Forecast)



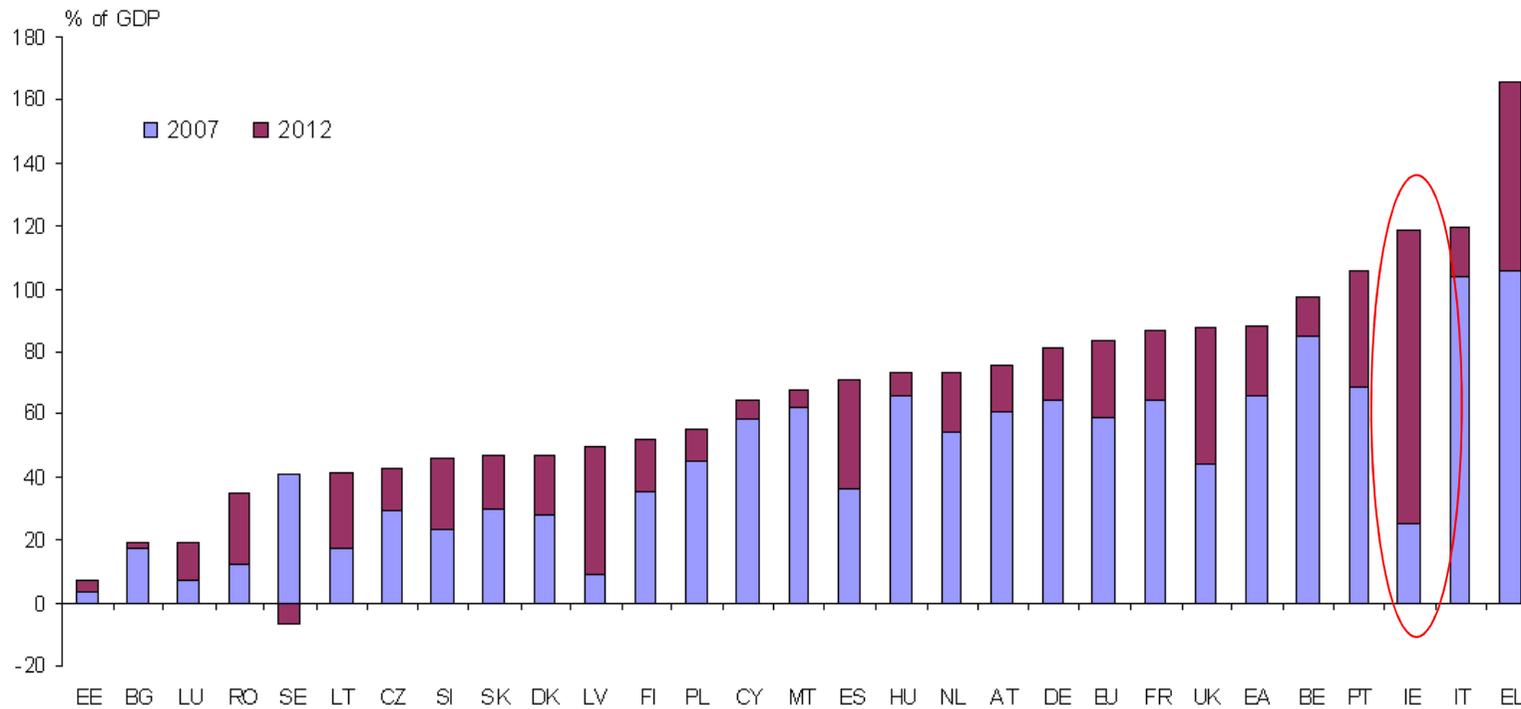
European
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The context: strengthening economic governance in EMU

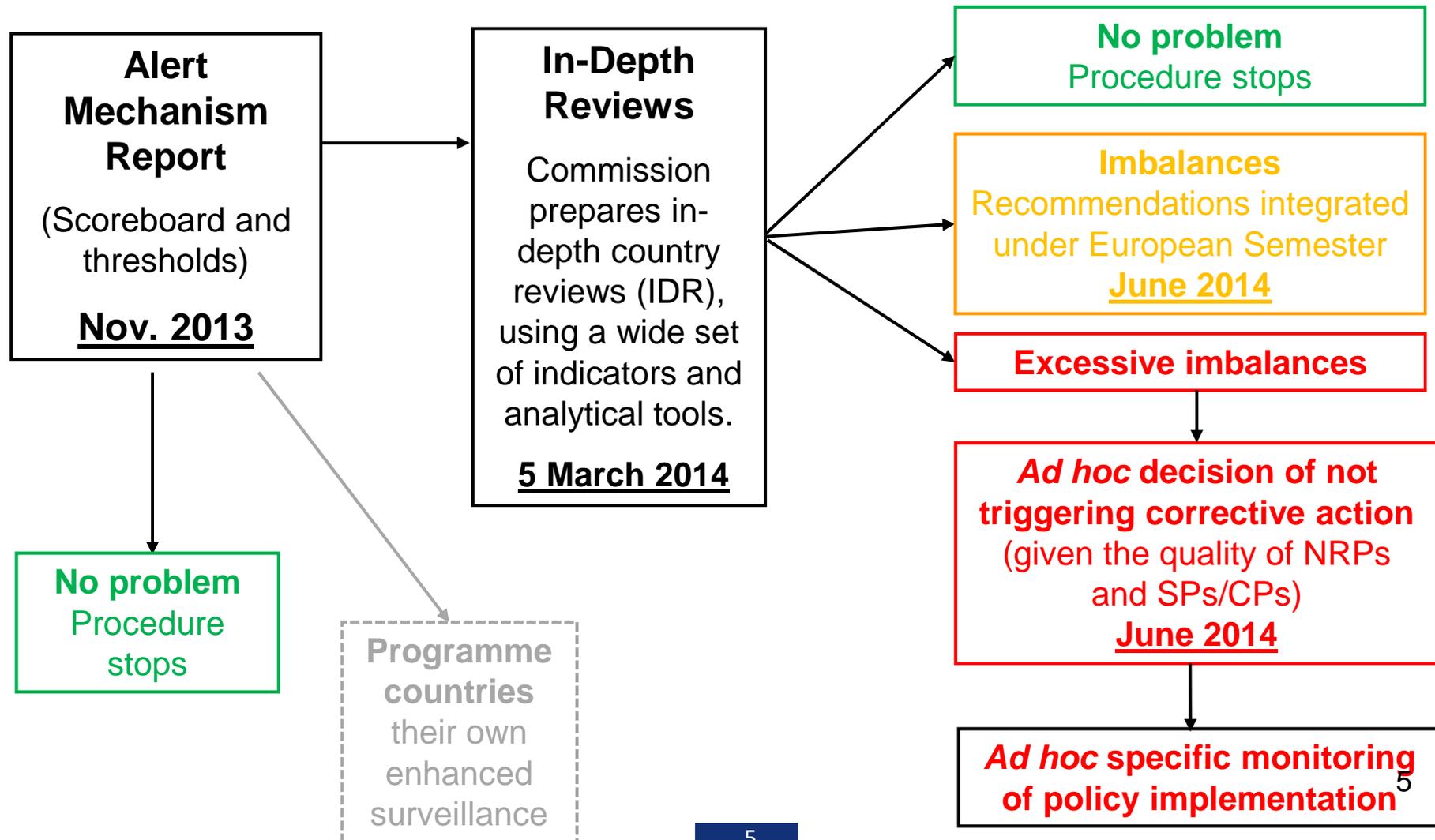


Crisis symptoms - sharp rise in government gross debt! But why...?

Gross debt (in % GDP)

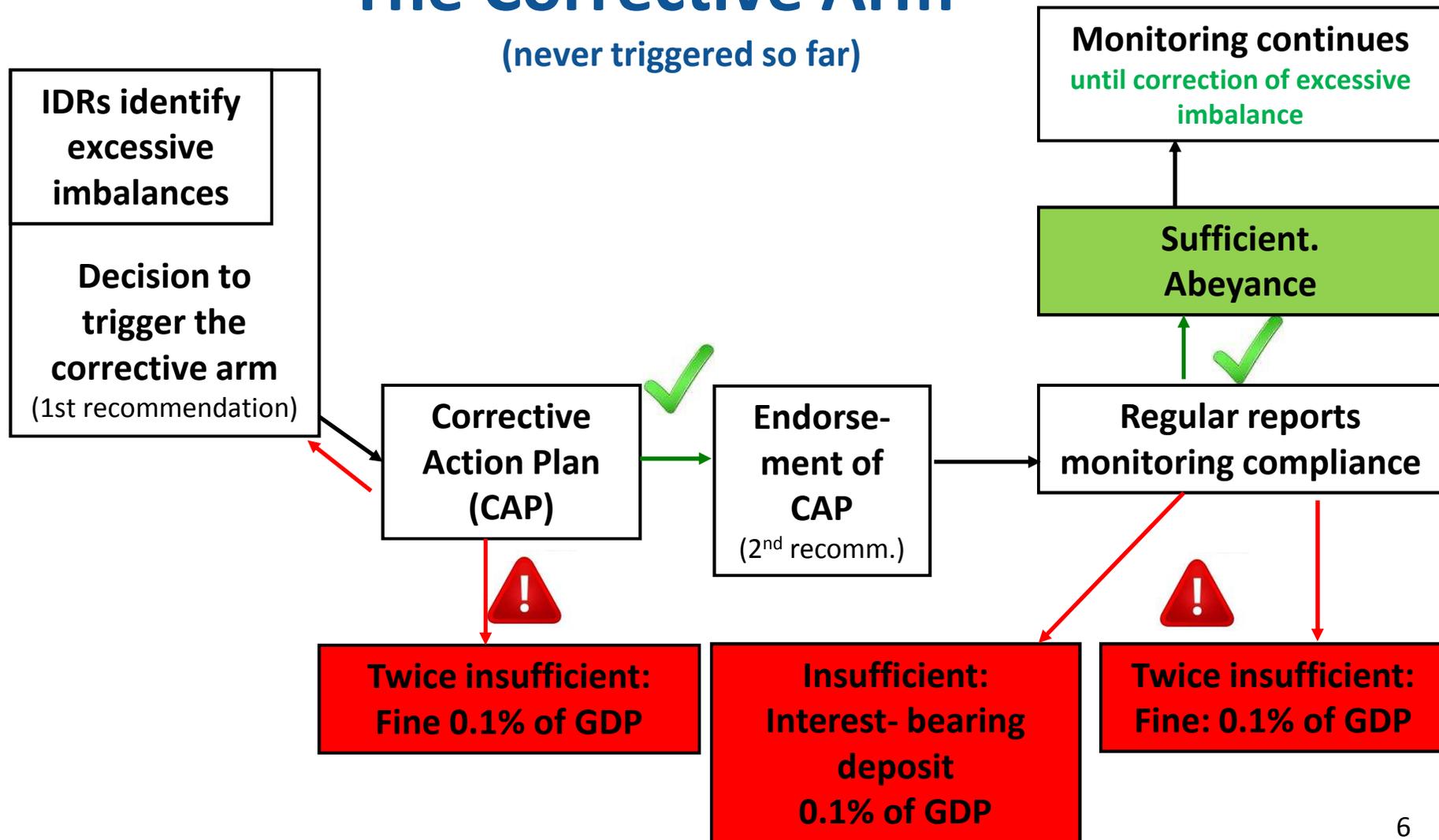


Macroeconomic imbalance procedure (2014)



The Corrective Arm

(never triggered so far)



The scope of the scoreboard



+ auxiliary indicators (no thresholds)

+ auxiliary social indicators (no thresholds)

Table A1. Scoreboard indicators and their indicative thresholds

	External imbalances and competitiveness					Internal imbalances					
Indicator	3-year average of current account balance as a % of GDP	Net international investment position as a % of GDP	% change (3 years) of real effective exchange rate, HICP deflators relative to 41 industrial countries (a)	% change (5 years) in export market shares	% change (3 years) in nominal unit labour cost (b)	y-o-y % change in deflated house prices (c)	Private sector credit flow (consolidated) as % of GDP (d), (e)	Unemployment rate - 3-year average	Private sector debt (consolidated) as % of GDP (d), (e)	General government sector debt as % of GDP	y-o-y % change in total financial sector liabilities, non-consolidated data
Data source	EUROSTAT (Balance of Payments statistics)	EUROSTAT (Balance of Payments Statistics)	DG ECFIN (data base Price and Cost competitiveness).	EUROSTAT (Balance of Payments Statistics),	EUROSTAT (National Accounts)	EUROSTAT	EUROSTAT (National Accounts)	EUROSTAT (Labour Force Survey)	EUROSTAT (National Accounts)	EUROSTAT (EDP – treaty definition).	EUROSTAT (National Accounts)
Indicative thresholds	-4/+6% Lower quartile (also used as a reference for upper threshold)	-35% Lower quartile	+/-5% for EA +/-11% nonEA Lower and Upper Quartiles of EA +/- s.d. of EA	-6% Lower quartile	+9% EA +12% non-EA Upper Quartile EA +3%	+6% Upper quartile	+15% Upper Quartile	+10%	133% Upper Quartile	+60%	16.5%
Some additional indicators to be used in economic reading	Net lending/borrowing vis-à-vis ROW as % of GDP	Net External Debt as % GDP Inward FDI flows and stocks as % of GDP	Real effective exchange rate vis-à-vis rest of the euro area	Relative export market shares relative to advanced economies; Labour productivity; Trend TFP growth	Nominal unit labour costs (changes over 1, 5, 10 years); Effective unit labour cost relative to the rest of euro-area	Real house price changes (cumulated over 3 years); Nominal house price index Value-added in residential construction	Change in private debt	Participation rate, long-term and youth unemployment poverty indicators	Private sector debt based on non-consolidated data		Debt over equity ratio

Notes: (a) For EU trading partners HICP is used while for non-EU trading partners, the deflator is based on a CPI; (b) Index providing ratio of nominal compensation per employee to real GDP per person employed; (c) Changes in house prices relative to the consumption deflator; (d) Private sector is defined as non-financial corporations; households and non-profit institutions serving households; (e) Sum of loans, and securities other than shares.

Table A2. MIP scoreboard 2012

Year 2012	External imbalances and Competitiveness									Internal imbalances						
	Current Account Balance as % of GDP		Net International Investment Position as % of GDP	Real Effective Exchange Rate (42 IC - HICP deflators)		Export Market Shares		Nominal ULC		% y-o-y change in Deflated House Prices	Private Sector Credit Flow as % of GDP, consolidated	Private Sector Debt as % of GDP, consolidated	General Government Sector Debt as % of GDP	Unemployment Rate		% y-o-y change in Total Financial Sector Liabilities
	3 year average	p.m.: level year 2012		% change (3 years)	p.m.: % y-o-y change	% change (5 years)	p.m.: % y-o-y change	% change (3 years)	p.m.: % y-o-y change					3 year average	p.m.: level year 2012	
Thresholds	-4/+6%	-	<-35%	±5% & ±11%	-	-6%	-	+9% & ±12%	-	+6%	14%	133%	60%	10%	-	16.5%
BE	-0.4	-2.0	48	-4.3	-2.3	-14.9	-5.2	6.6	4.1	-0.2	-1.5	146	100	7.7	7.6	-3.9
BG	-0.9	-1.3	80	-4.0	-2.0	4.8	-5.5	7.4	-0.5	-5.3 (p)	2.5	132	19	11.3	12.3	10.1
CZ	-3.0	-2.4	-50	0.4	-2.8	-4.2	-4.6	3.9	3.8	-3.9	0.6	72	46	7.0	7.0	5.4
DK	5.9	6.0	38	-7.7	-2.8	-18.6	-4.8	1.0	1.6	-5.1	6.1	239	45	7.5	7.5	5.0
DE	6.5	7.0	42	-8.9	-3.2	-13.1	-4.6	3.0	3.1	1.8	1.5	107	81	6.2	5.5	4.4
EE	0.9	-1.8	-54	-3.4	-0.6	6.5	-4.1	-2.8	4.2	3.5	4.7	129	10	13.2	10.2	12.9
IE	2.3	4.4	-112	-12.2	-4.3	-16.3	-3.3	-10.4	0.0	-11.7	-1.6	306	117	14.4	14.7	-0.7
EL	-7.5	-2.4	-109	-4.5	-3.9	-26.7	-7.3	-8.1	-6.2	-12.4 (1)	-6.8	129	157	18.2	24.3	-3.4
ES	-3.1	-1.1	-93	-5.2	-2.3	-14.6	-4.9	-5.6	-3.0	-16.9	-10.5	194	86	22.3	25.0	3.3
FR	-1.8	-2.2	-21	-7.8	-3.2	-14.0	-6.8	4.1	2.1	-2.3	3.5	141	90	9.9	10.2	-0.1
HR	-0.5	0.0	-89	-8.3	-2.6	-24.7	-7.4	0.8	1.2	-2.4	-2.1	132	56	13.8	15.9	0.9
IT	-2.3	-0.4	-25	-6.2	-1.8	-23.8	-5.0	3.1	2.3	-5.4 (p)	-1.0	126	127	9.2	10.7	7.1
CY	-6.7	-6.9	-82	-5.8	-1.9	-26.5	-9.4	0.8	2.7	-2.2	10.0	299	87	8.7	11.9	-1.9
LV	-0.6	-2.5	-67	-8.5	-1.4	12.3	5.4	-5.8	3.4	-0.6	-1 (p)	91.7 (p)	41	16.9	15.0	4.1 (p)
LT	-1.3	-0.2	-53	-6.7	-2.0	29.3	5.7	-4.6	1.9	-3.2	-0.3	63	41	15.6	13.4	-0.3
LU	7.0	6.6	169	-2.3	-1.4	-18.3	-4.0	9.8	4.7	2.5	-5.0	317	22	4.8	5.1	11.3
HU	0.6	1.0	-103	-1.2	-2.3	-17.8	-7.4	4.4	2.7	-9.2	-6.1	131	80	11.0	10.9	-8.3
MT	-1.6	1.6	25	-7.7	-2.1	4.5	-1.9	4.9	3.7	0.3	-1.6	155	71	6.6	6.4	4.1
NL	8.8	9.4	47	-6.0	-1.8	-12.0	-3.3	3.3	2.8	-8.7	0.2	219	71	4.7	5.3	4.9
AT	2.2	1.6	0	-4.7	-1.7	-21.2	-6.3	4.1	3.0	na (2)	2.7	147	74 (3)	4.3	4.3	-0.9
PL	-4.6	-3.7	-67	1.3	-2.3	1.3	-2.7	4.4	2.0	-5.9 (e)	3.4	75	56	9.8	10.1	9.6
PT	-6.5	-2.0	-115	-4.0	-1.5	-16.0	-5.3	-5.3	-3.1	-8.5 (p)	-5.4	224	124	13.6	15.9	-3.6
RO	-4.4	-4.4	-68	-1.9	-6.0	5.9	-7.1	4.8	6.5	-9.2	0.9	73	38	7.2	7.0	5.3
SI	1.2	3.3	-45	-4.5	-1.2	-19.9	-6.9	0.4	0.8	-8.4	-2.9	114	54	8.1	8.9	-0.8
SK	-1.7	2.2	-64	-3.2	0.0	4.2	1.5	0.9	1.0	-5.9	3.2	73	52	14.0	14.0	2.6
FI	-0.5	-1.7	18	-8.3	-2.7	-30.8	-7.1	4.8	4.4	-0.5 (p)	9.0	158	54	8.0	7.7	-0.2
SE	6.2	6.0	-10	10.1	-0.8	-18.8	-6.0	0.7	2.9	-0.2	1.8	212	38	8.1	8.0	4.4
UK	-2.8	-3.8	-9	5.8	4.3	-19.0	-1.7	6.1	3.0	-0.9	2.6	179	89	7.9	7.9	-4.3

Source: EUROSTAT, DG ECFIN (for the indicators on the REER).

Note: (1) Eurostat estimate based on HPI data from Bank of Greece produced in agreement with ELSTAT. (2) HPI data up until 2011 by Statistics Austria. For 2012, Eurostat estimates a deflated rate of 9.6% based on non-harmonised HPI data by ECB & Central Bank of Austria. (3) Eurostat expressed a reservation on Austrian general government sector debt, see Eurostat press release 152/2013. (4) p= provisional data, e= estimated.

What the scoreboard is and what it is not

A first step (an initial filter) in the procedure

An instrument of communication and accountability

(COM needs to explain its decision taking into account the scoreboard)

A set of indicators that helps identifying macroeconomic risks

(but needs to be complemented by detailed analysis)

It is not:

A tool for a mechanic decision on the existence of imbalances

A tool to identify progress in reforms and developments in macro risks

What is an imbalance? When is it excessive?

General considerations

- It is judgemental
- Constrained discretion illuminated by IDRs
- No numerical benchmarks as in the SGP

Features of imbalances

- Issues of sustainability (which would lead to abrupt adjustments)
- Grave misallocations of resources
- Spillovers (not imbalances per se, but aggravate the assessment of the risks related to imbalances)

Methods of assessment (entry/exit)

- Snapshot (the levels of the main macro indicators, scoreboard and other variables)
- Dynamics (how variables are evolving)
- Policy implementation (to the extent it is expected to impact the dynamics)

IDRs cover a wide range of issues

Main issues	
External sustainability	ES, IE, FR, HR, HU
Presistently large surplus	DE, (NL, SE, LU)
Price/non-price competitiveness	BE, FR, IT, HU, SI, FI, UK, ES, HR, DK, LU
Housing and mortgage markets	ES, NL, SE, UK, IE, HU
Households indebtedness	DK, IE, ES, FR, HR, HU, MT, NL, LU, SE, UK
Firms indebtedness	IE, ES, HR, HU, SI, UK, LU
Labour market	BG, IE, ES
Financial sector stability	IT, ES, IE, SI
Other issues	
Public debt, potential growth, subdued demand/low investment Unemployment, FDIs, etc.	

Findings of the 2014 IDRs

17 countries

Excessive Imbalances

HR, IT, SI

Decision not to open the corrective arm (June 2014) after examination of NRPs and SGPs – decision to put in motion a specific monitoring of policy implementation

Imbalances

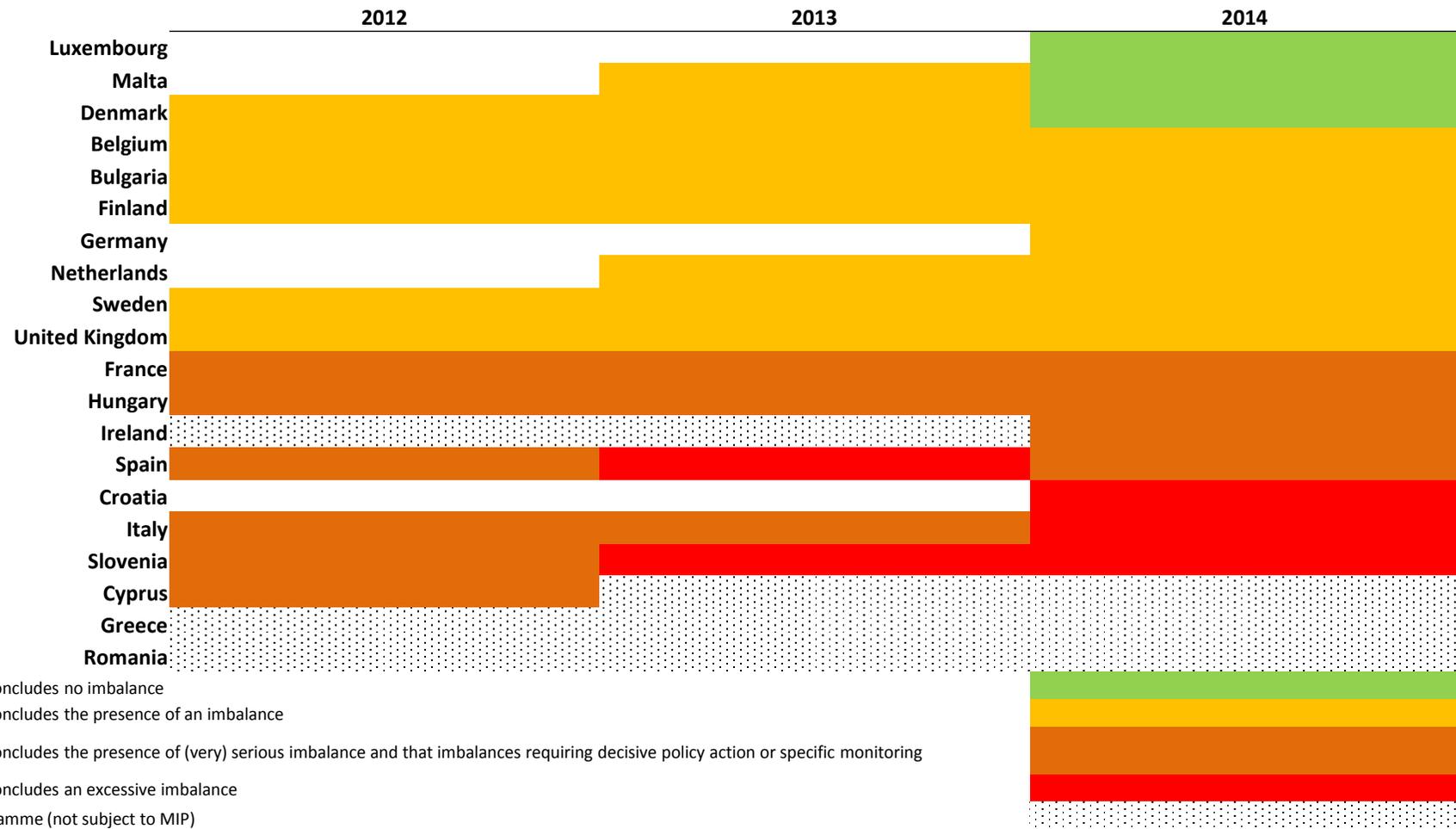
BE, BG, DE, IE, ES*, FR*,
HU*, NL, FI, SE, UK*

** requiring decisive action; for euro area this puts in motion a specific monitoring of policy implementation*

No Imbalances

DK, LU, MT

Macro imbalances evolve over time



The way forward for the MIP (1)

(six-pack review and beyond)

- **Scoreboard and thresholds**
 - balancing stability with the need of being up to date
- **Social aspects**
 - to be considered, but keeping the procedure focused on causes, not symptoms
- **Definitions of imbalances and excessive imbalances**
 - consolidating views on the use of the MIP in recovery and good times
 - the timely identification of bubbles is analytically demanding
- **Interaction with other surveillance tools**
 - SGP
 - post-programme surveillance

The way forward for the MIP (2)

(six-pack review and beyond)

- **IDRs**
 - so far a great success in contributing to common understanding of problems
 - but frequency and coverage?
- **Unsatisfactory policy implementation**
 - the problem is wider than MIP; how to improve incentives?
- **Triggering the corrective arm and the threat of sanctions**
 - should we trigger the corrective arm?
 - will it be more effective than softer surveillance (specific monitoring)? - how to handle the perspective of sanctions?
- **Communication/complexity** – complete contract?

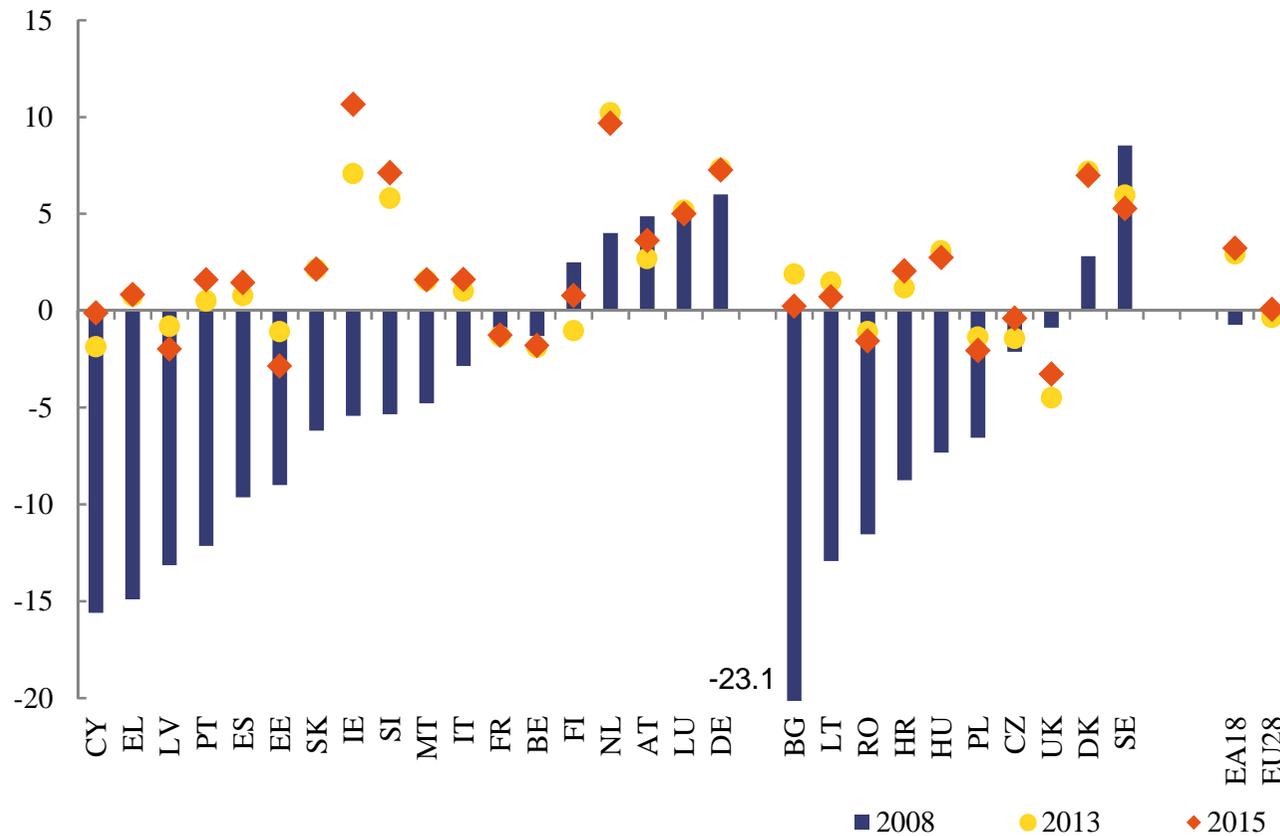
EA -Rebalancing is ongoing but not finished

- **Current account** deficits have largely adjusted while some surpluses remain sizeable
- Negative **net international investment positions** (NIIP) remain large and reflect vulnerabilities
- Despite being reduced, the **debt stock** of non-financial firms and households are still large, implying challenging deleveraging needs in times of low nominal growth
- **House prices** have partly adjusted
- High **unemployment** rates point to the social costs of the crisis



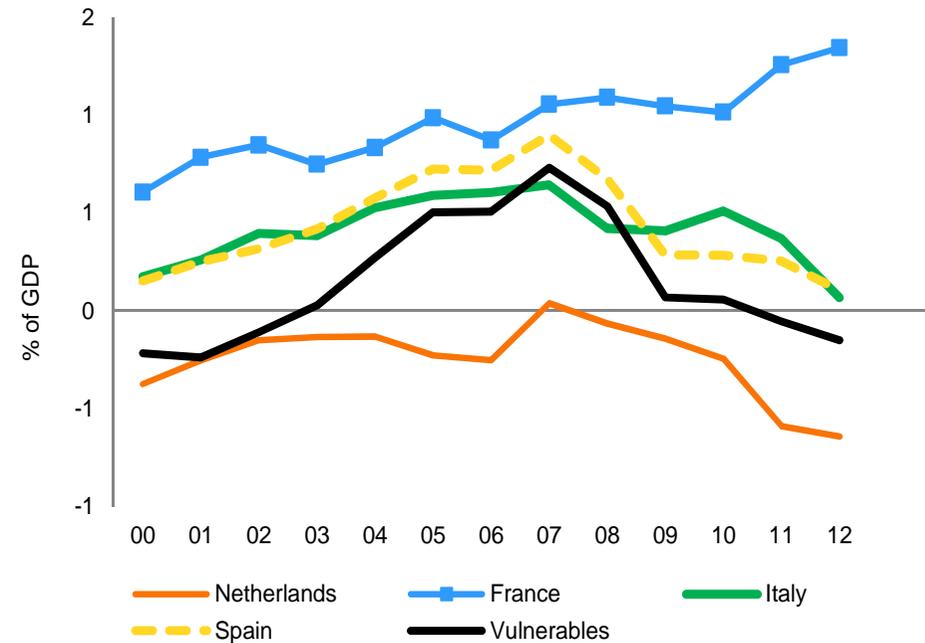
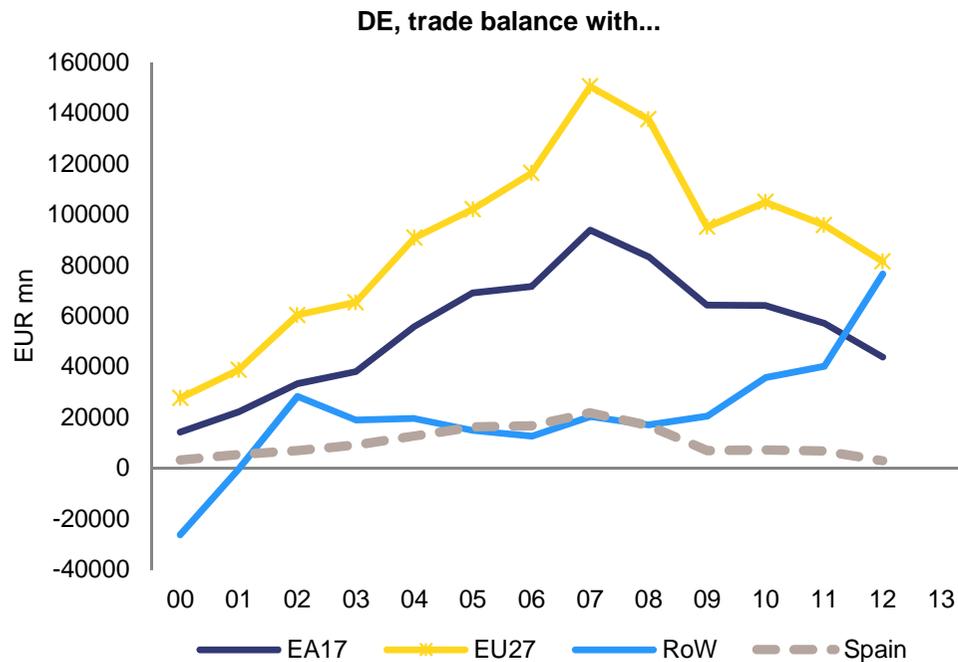
On-going external rebalancing

Current Accounts Deficits (-) and Surpluses (+); 2008, 2013 and 2015 (forecast)
(% of GDP)



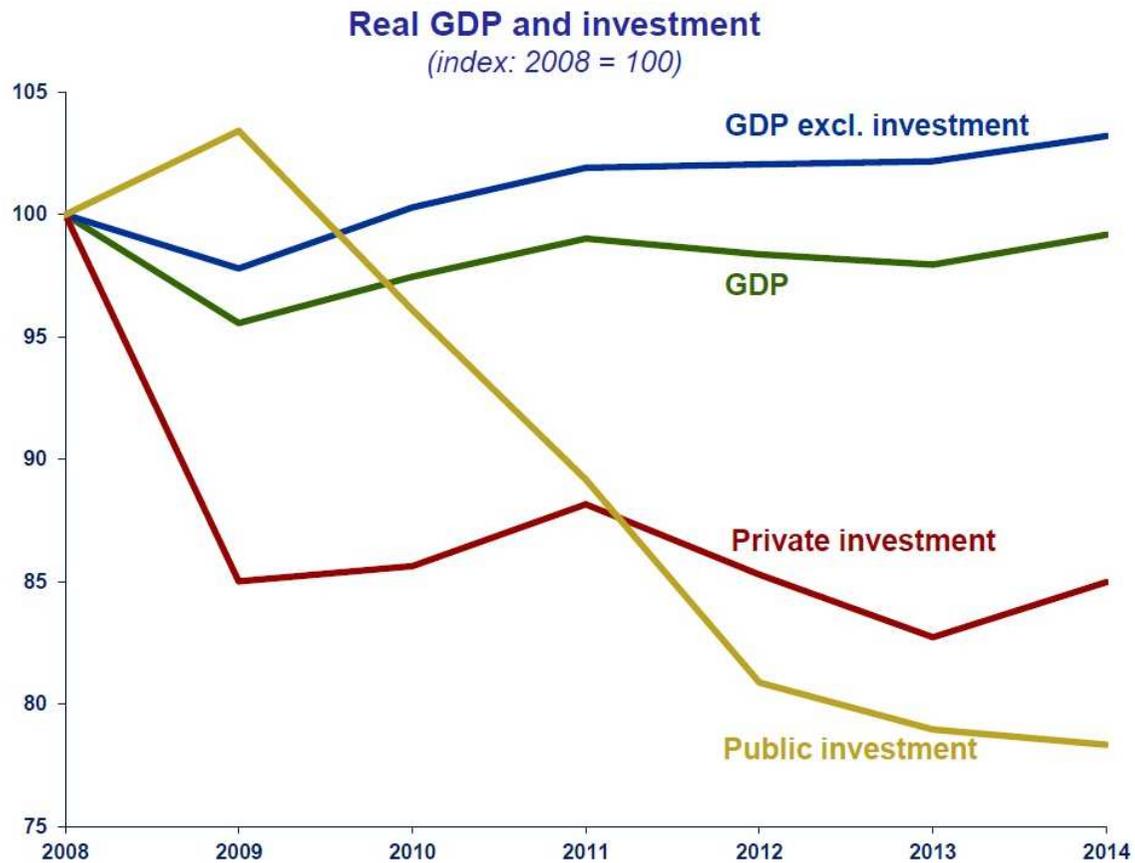
Challenges: Durability of the CA improvement in debtor countries
Lack of demand=large surplus in creditor countries

A corollary: trade rebalancing in the euro area



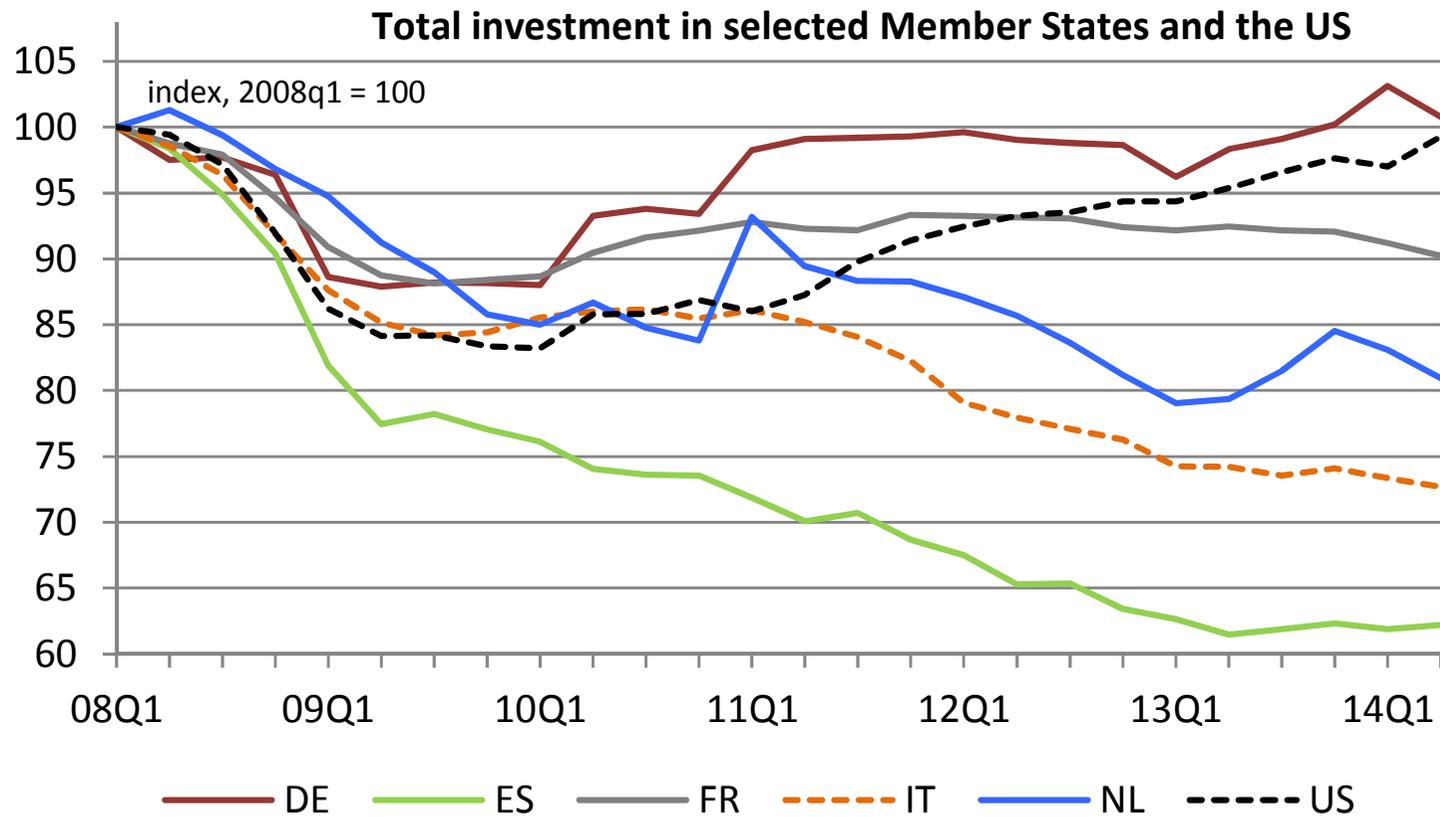
DE trade surplus with the RoEA somewhat declined, but mostly driven by higher deficit with NL and decline of imports from vulnerable countries

But...the investment gap!



Sources: ECB calculations and European
Commission.
Latest data: 2013 (forecast 2014).

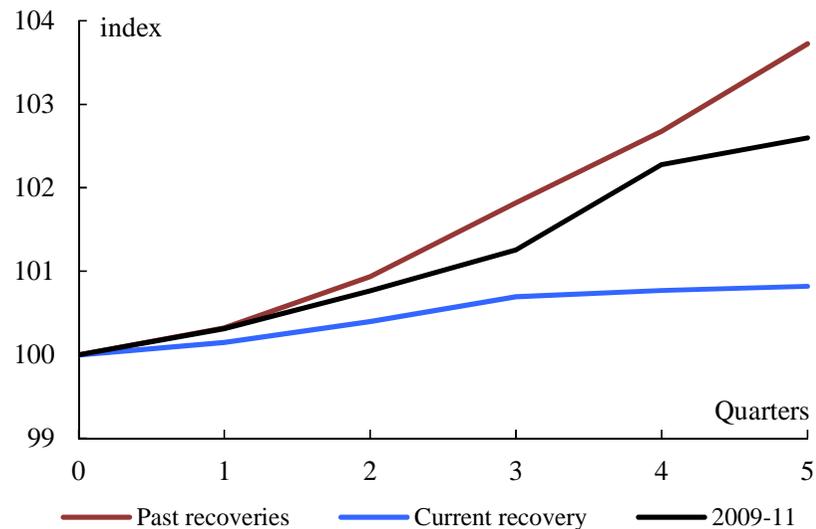
Weak investment in key MS



(Weak) euro area recovery in perspective

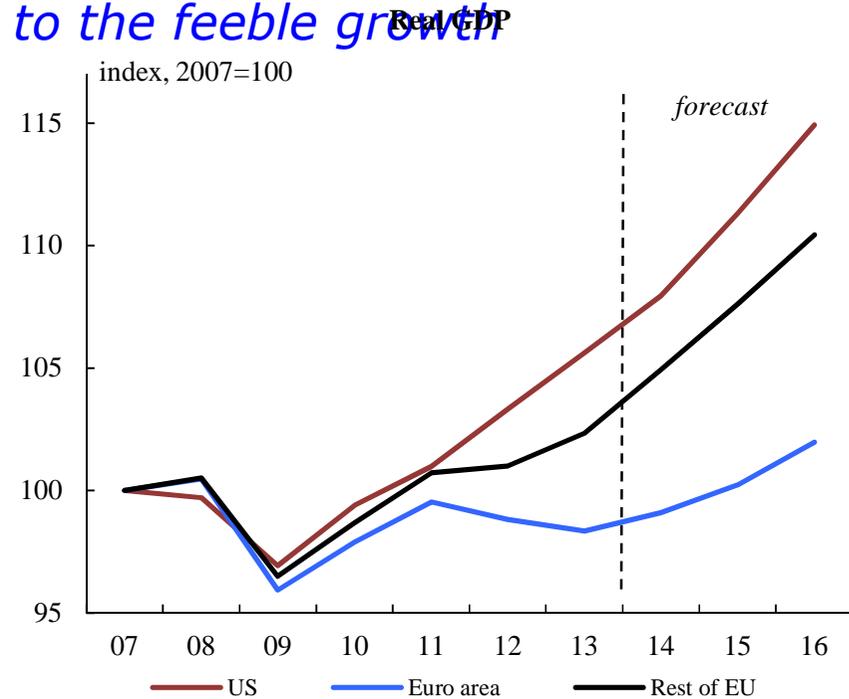
Recoveries after systemic financial crises – slow and bumpy (e.g. Reinhart and Rogoff, 2009)

Comparison of past and current recoveries - GDP, euro area



Note: Past recoveries included are those from the mid-1970s, early-1980s and early-1990s.

Euro-area specific factors contribute to the feeble growth



The investment gap – policy perspective

- e.g. Buti (2014): Raising Investment in the Eurozone

- **Low Investment hampers growth**
 - both in short run (demand) and long run (productivity/potential growth)
- **Various causes of lower investment**
 - deleveraging (balance sheet repairs households and corporates)
 - public finance (forced) consolidation, myopic policymaking
 - financial fragmentation
 - high levels of economic uncertainty
- **Possible remedies**
 - structural reforms to boost investment outlook
 - credible fiscal consolidation
 - banking union
 - boost to EIB capital, EU budget, increased investment allocation in 2014-2020
 - (...)



+ to be watched:

***The Commission's Autumn 2014
Package***





Thank you for your attention!

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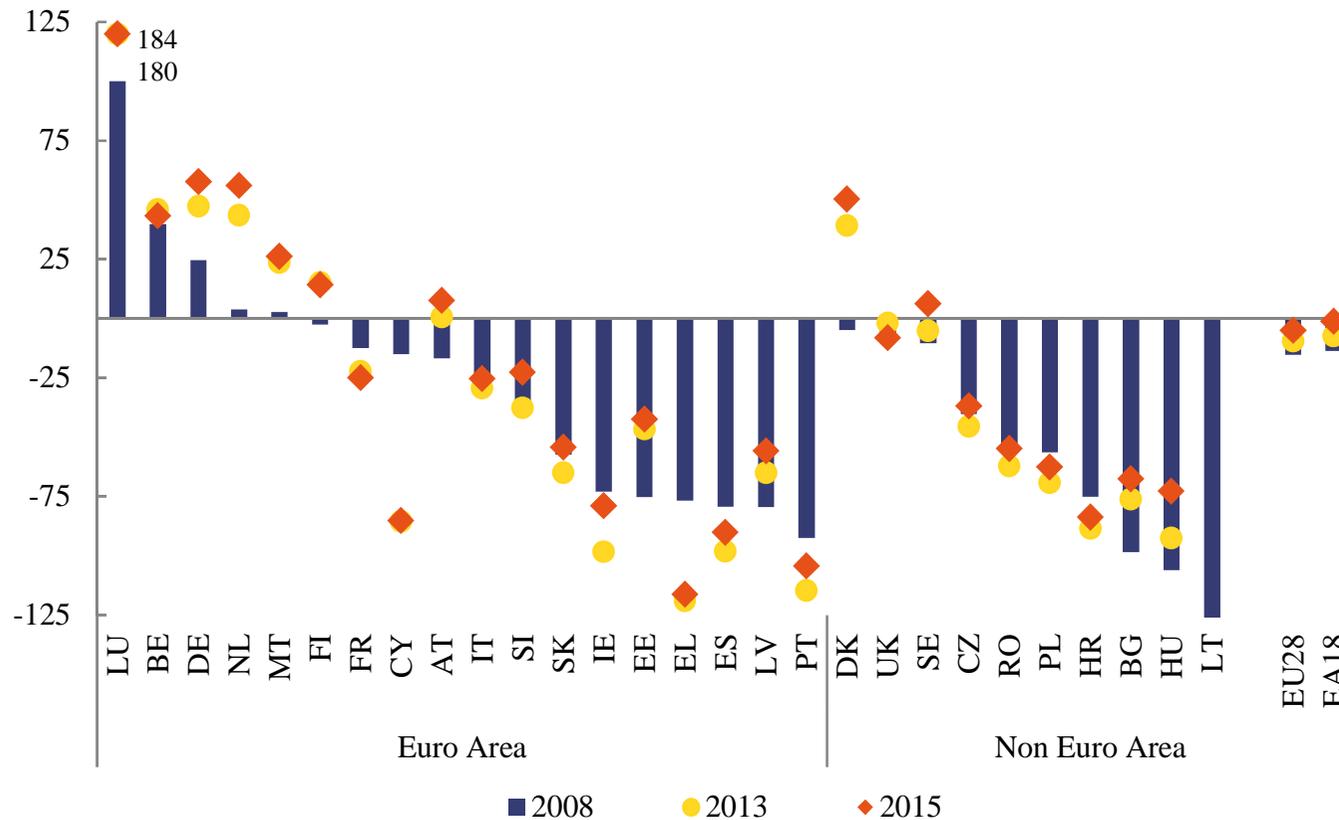


Back-up slides



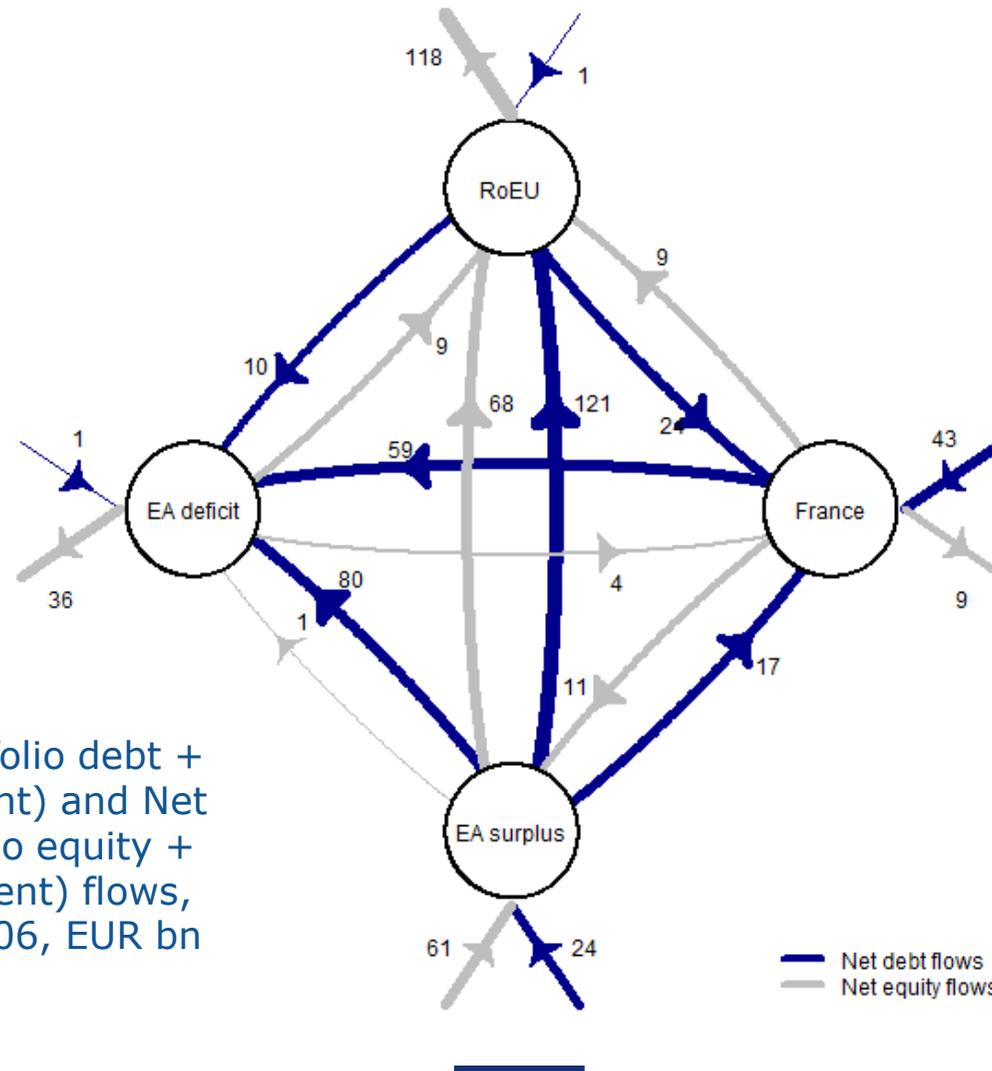
Negative NIIPs illustrate vulnerabilities

Net international investment positions; 2008, 2013 and 2015 (projection)
(% of GDP)



Challenge: The correction of external vulnerabilities will take time

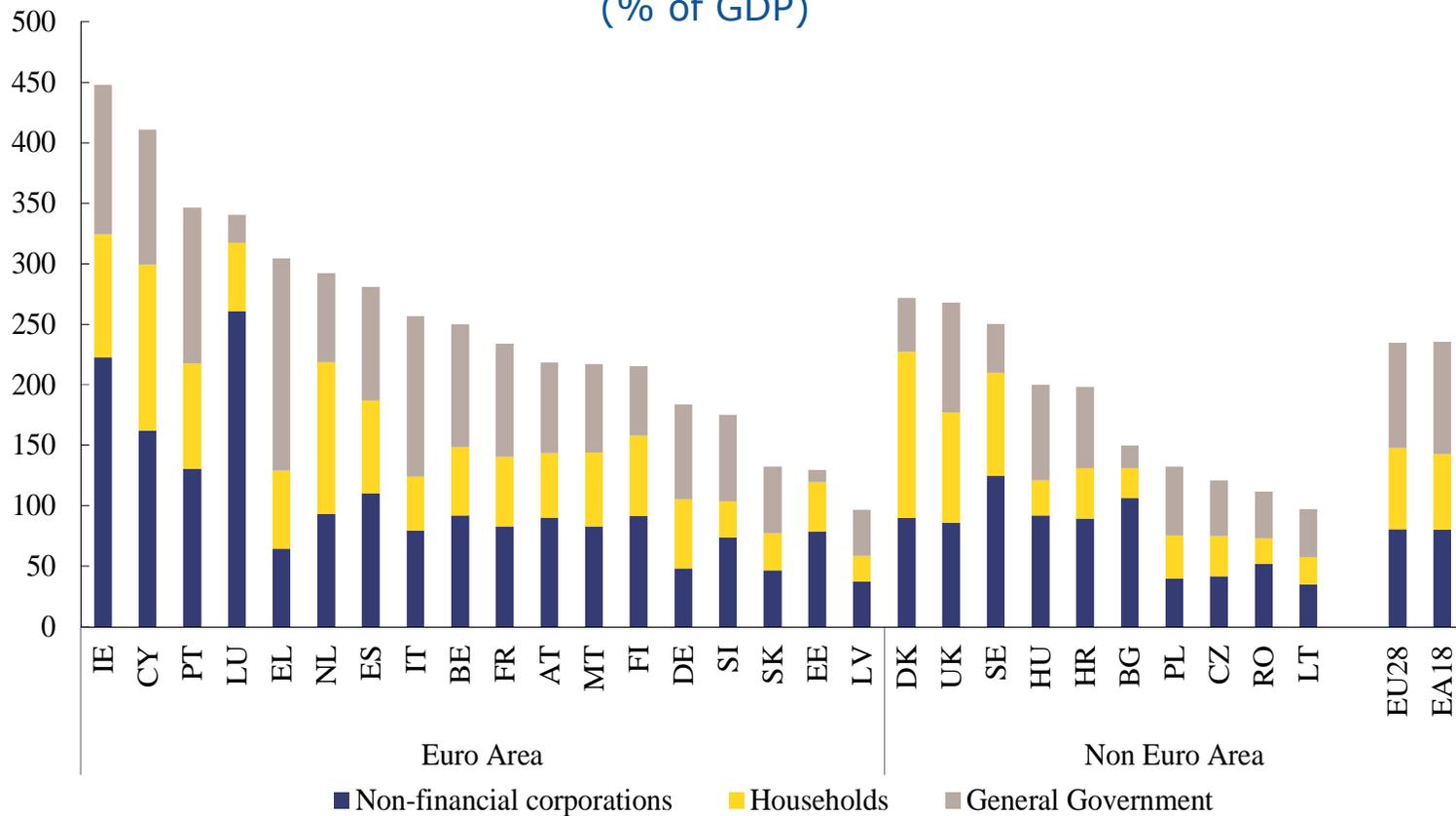
Pre-crisis: deficit countries debt-financed from surplus countries and France



Net Debt (portfolio debt + other investment) and Net equity (portfolio equity + direct investment) flows, Average 2004-06, EUR bn

Deleveraging pressures

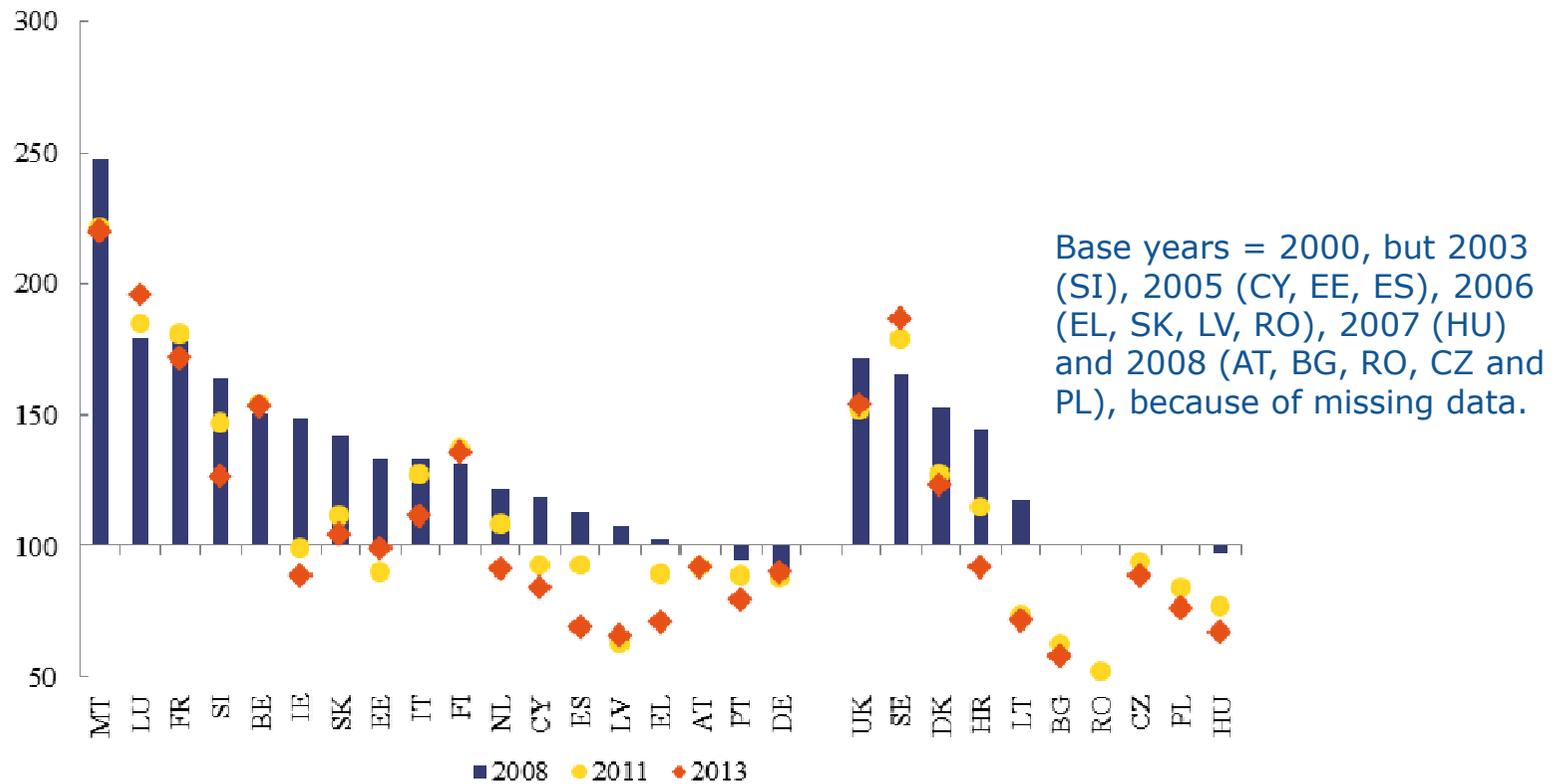
Non-Financial Corporate, Household and General Government Debt,
2013
(% of GDP)



Challenge: Deleveraging in times of low nominal growth

Is the house price cycle complete?

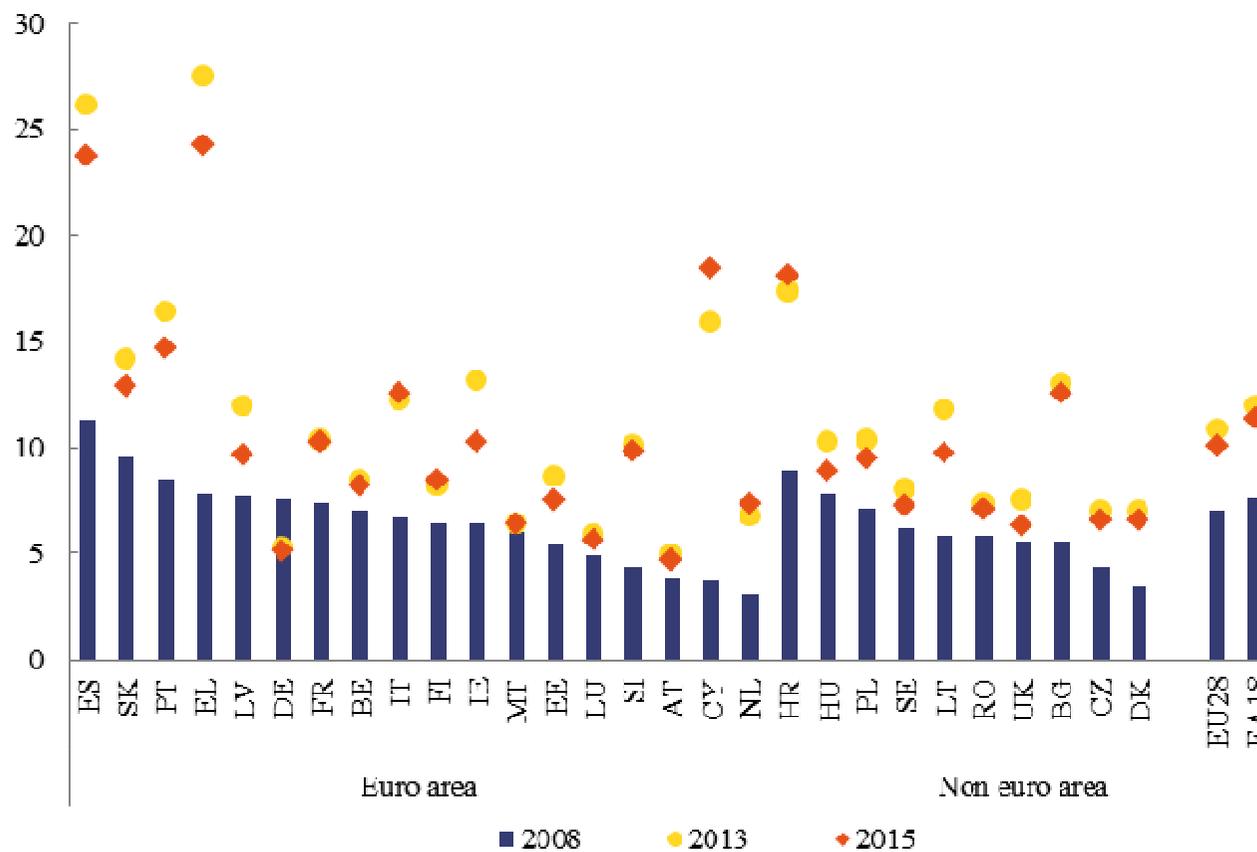
House prices (deflated); 2008, 2011 and 2013
(index 2000=100, u.o.i.)



Challenge: Avoid the emergence of new bubbles

The social cost of the crisis

Unemployment rate
2008, 2013 and 2015 (forecast)



Challenge: Reducing unemployment under a fragile recovery.



European Economic Forecast – Autumn 2014

Key messages

- **The economic recovery is not happening as fast and as strongly as expected last spring**
- **GDP growth is expected to rise slowly in 2015 and accelerate in 2016**
- **Diversity across Member States is large**
- **Inflation is projected to pick up very gradually as economic slack is reduced and import prices increase**

EU specific factors also hold back growth

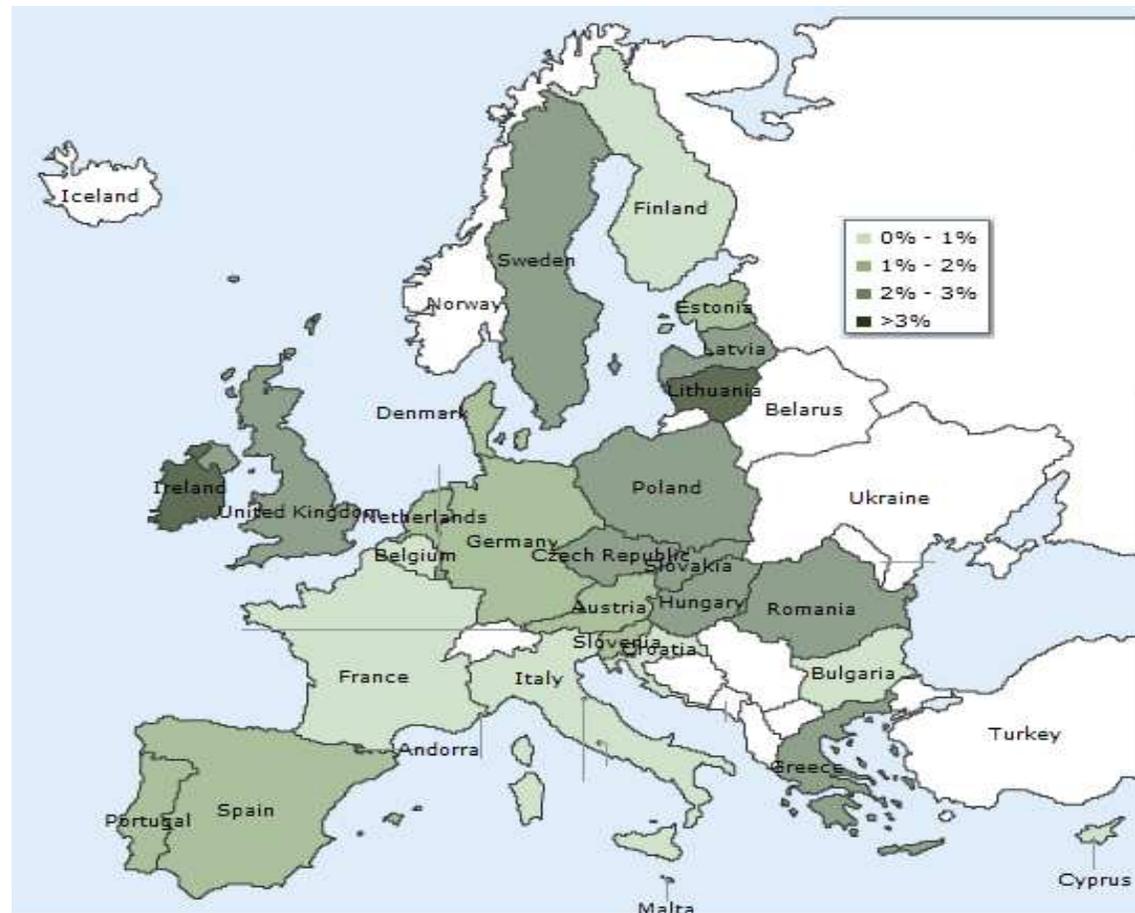
- **Already existing deep-seated structural problems**
- **Public and private debt overhang**
- **Ongoing financial fragmentation related to the sovereign debt crisis**

Autumn forecast

European Economic Forecast Autumn 2014				
Forecasts for EU	2013	2014	2015	2016
GDP growth (% , yoy)	0.0	1.3	1.5	2.0
Inflation (% , yoy)	1.5	0.6	1.0	1.6
Unemployment (%)	10.8	10.3	10.0	9.5
Public budget balance (% of GDP)	-3.2	-3.0	-2.7	-2.3
Gross public debt (% of GDP)	87.1	88.1	88.3	87.6
Current account balance (% of GDP)	1.4	1.4	1.5	1.5

European Economic Forecast Autumn 2014				
Forecasts for EA	2013	2014	2015	2016
GDP growth (% , yoy)	-0.5	0.8	1.1	1.7
Inflation (% , yoy)	1.4	0.5	0.8	1.5
Unemployment (%)	11.9	11.6	11.3	10.8
Public budget balance (% of GDP)	-2.9	-2.6	-2.4	-2.1
Gross public debt (% of GDP)	93.1	94.5	94.8	93.8
Current account balance (% of GDP)	2.4	2.5	2.6	2.5

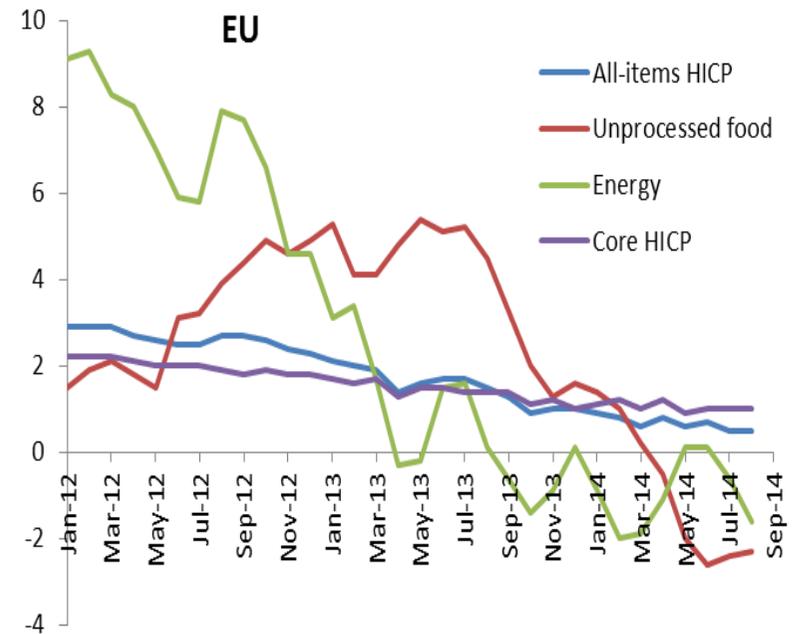
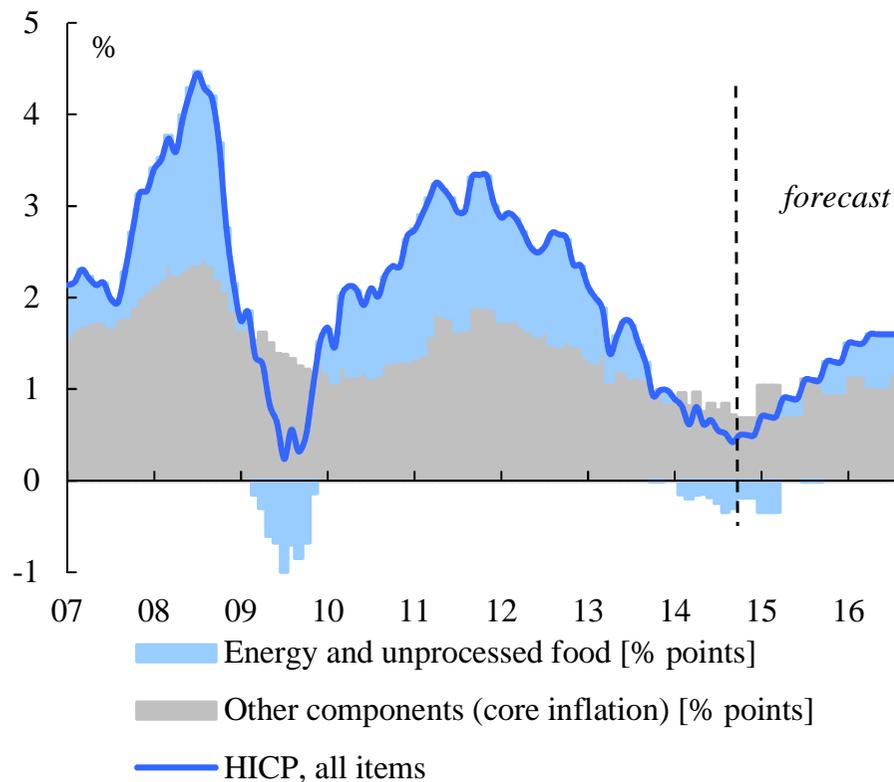
In 2015, most EU economies will grow at more than 1%



Source: European Commission

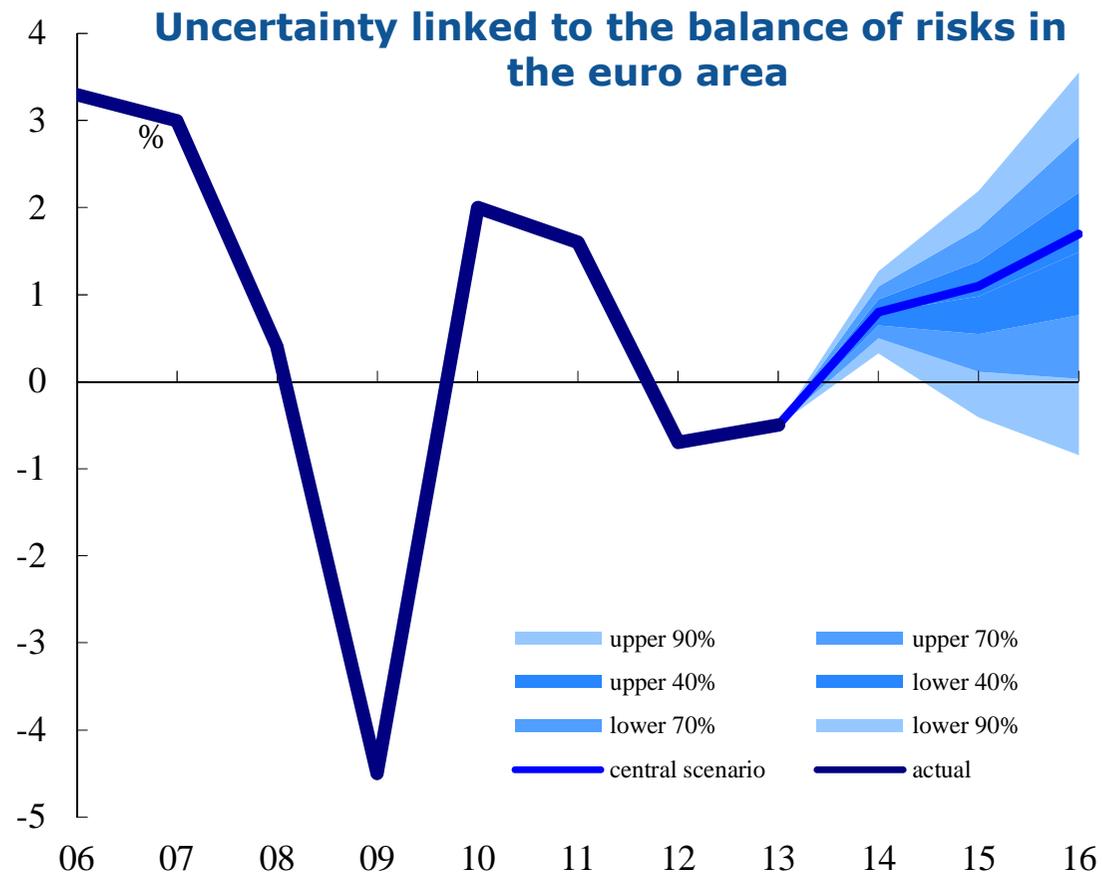


Low inflation is persisting



Source: European Commission

Risks to the growth outlook remain tilted to the downside



Source: European Commission