

Emerging from the euro debt crisis – Making the single currency work

Dr. Michael Heise, Allianz SE
Public Policy & Economic Research

American Institute for Contemporary German
Studies
Johns Hopkins University

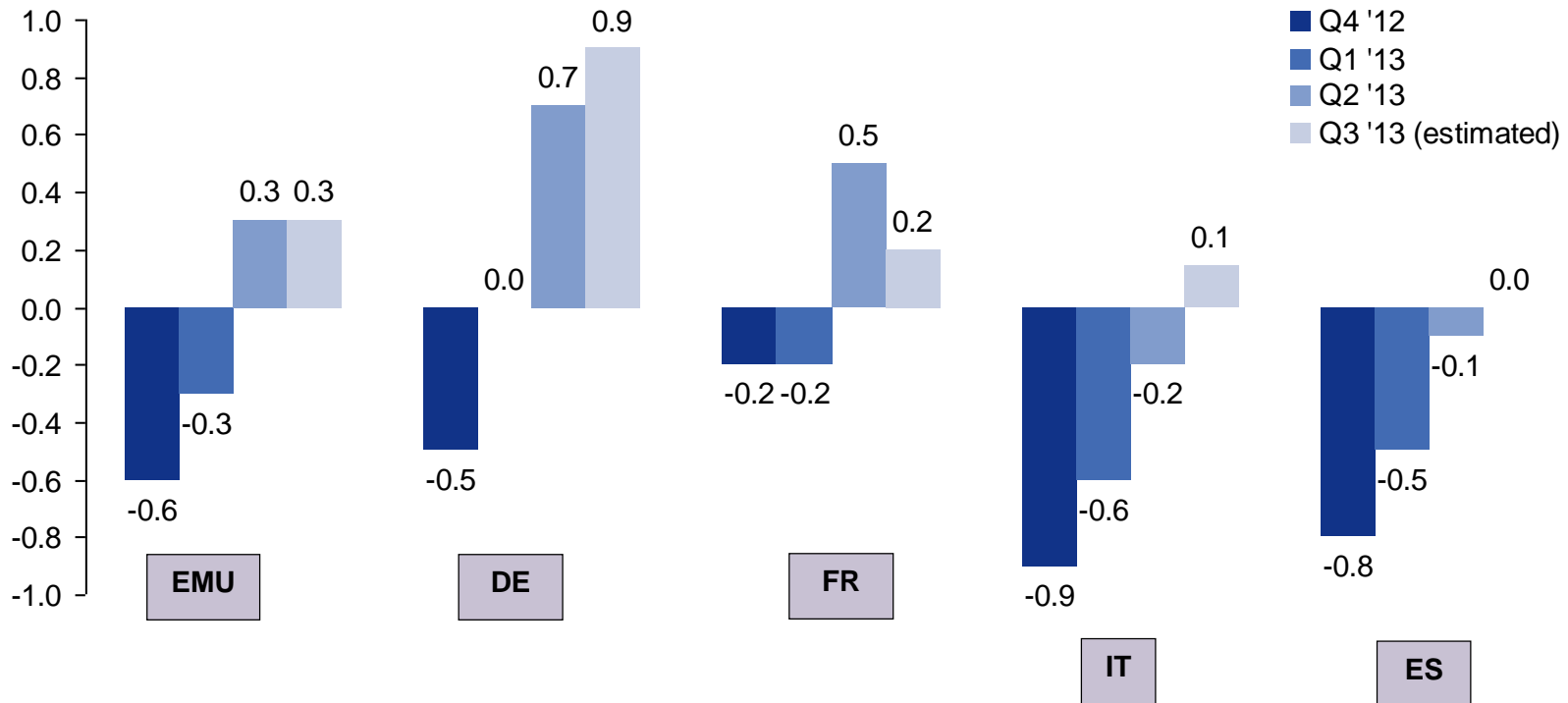
Washington D.C., August 20, 2013

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- 1 Euro debt crisis: Easing but not yet over**
- 2 The way forward: Making the single currency work**

EMU: Recession has come to an end, but growth to remain moderate in the course of the year

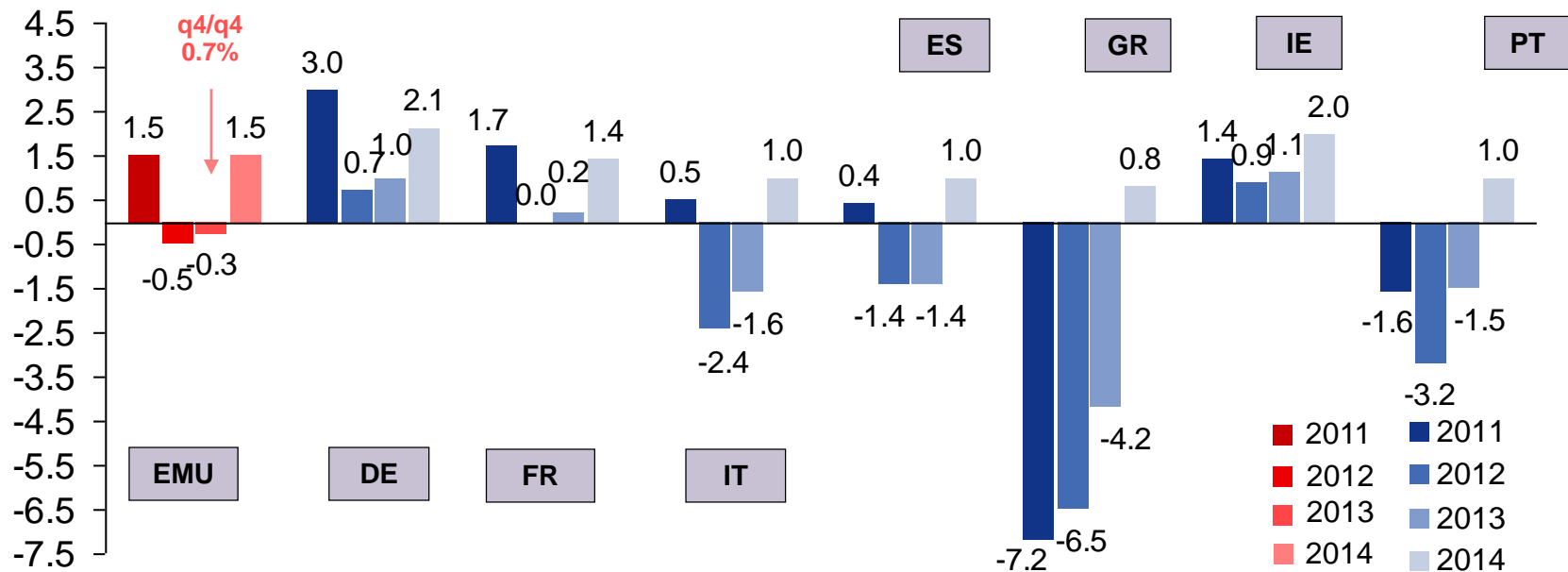
Real GDP growth (%)



Sources: Eurostat, own estimates.

EMU: Pace of growth likely to pick up in 2014

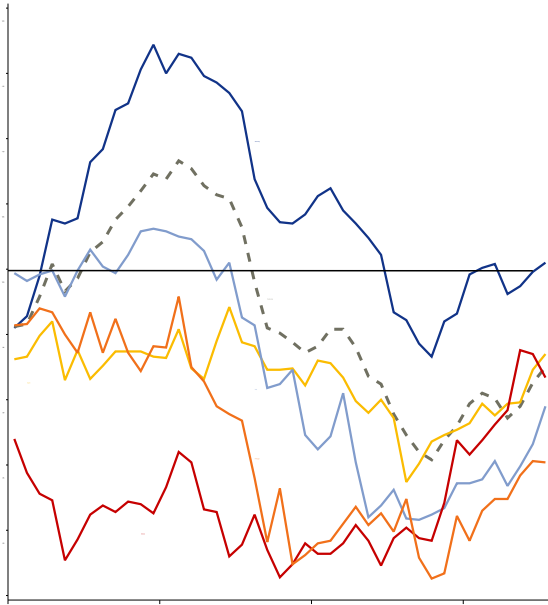
Real GDP growth (%)



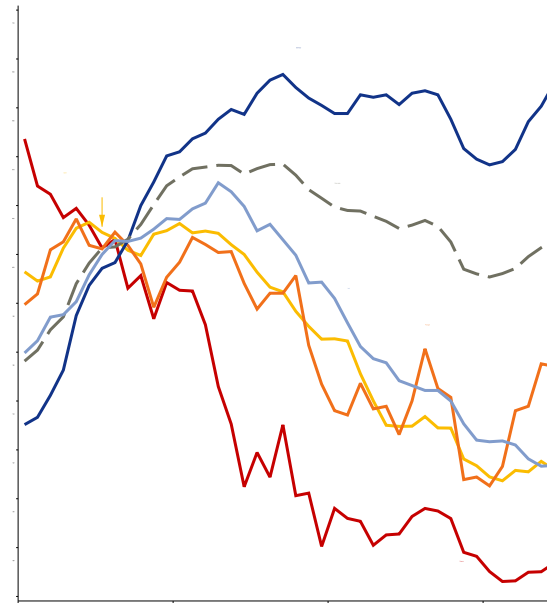
Sources: Eurostat, own forecasts.

EMU: Economic indicators support recovery hopes

Economic Sentiment Indicator
(Business and consumer survey)*



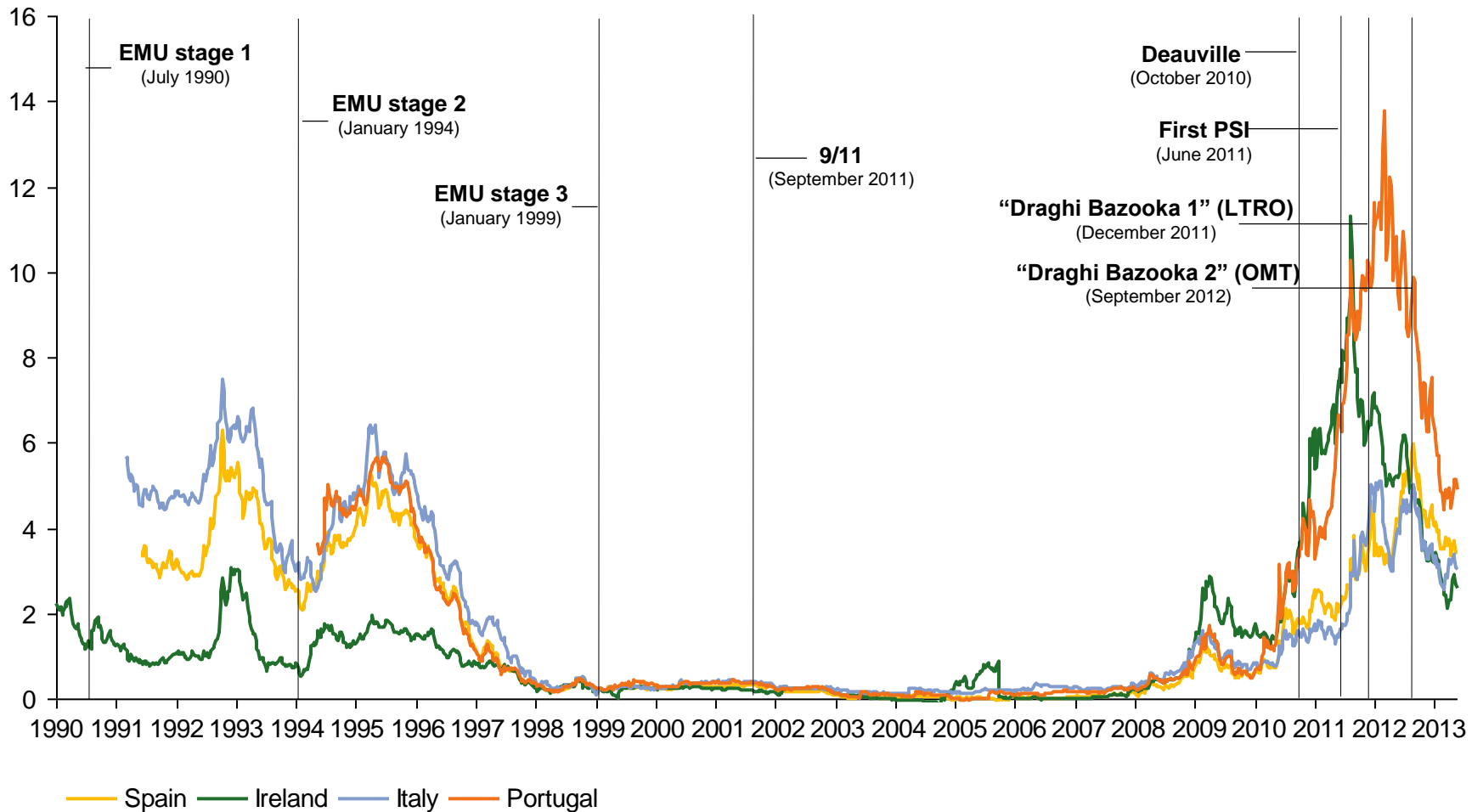
Industrial production (excl. construction)
index 2010 = 100, 3 month moving average



*) The EU Commission's Economic Sentiment Indicator (ESI) is a composite indicator made up of business and consumer sentiment indicators. Results are published as the balance of positive and negative answers.

Source: EcoWin.

Milestones of the euro crisis and sovereign bond spreads



PSI = public sector involvement. LTRO = longer-term refinancing operations. OMT = outright monetary transactions.

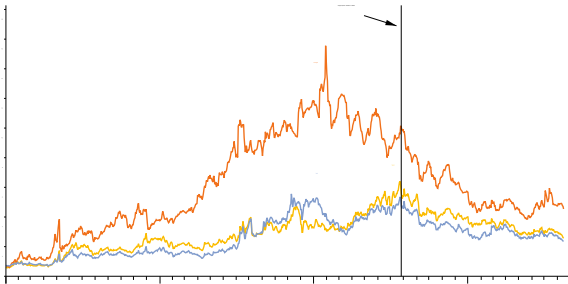
Source: EcoWin.

Euro debt crisis: Easing but not yet over

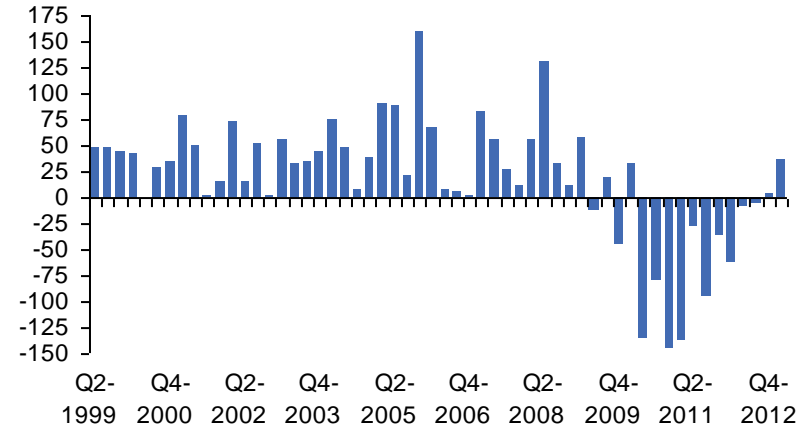
- There are **clear signs that the eurozone economy is bottoming out of a long recession**. But medium term growth will remain moderate due to consolidation and deleveraging needs.
- Despite the errors made in crisis management, the **basic principle** to use ECB measures and rescue fund means **to buy time in exchange for consolidation and structural reforms** has **proven to be right** and is bearing fruit.
- **Austerity does not lead to a downward spiral**, it is a necessity in a situation of over-indebtedness and lack of capital market access. If well-designed (embedded in medium-term concept, focus on spending rather than tax side, combined with pro-growth reforms) consolidation can quickly restore confidence.
- For the future success of the eurozone, it is now essential to establish a **strong and stable architecture in the financial, fiscal, economic and political domains**.

EMU: Financial markets with signs of normalization

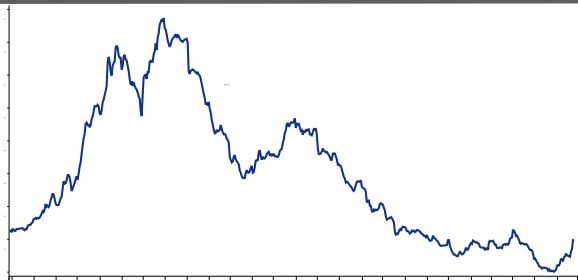
Yield spread over 10y German government bonds, percentage points



Change in net outstanding cross-border financing in the euro area in EUR bn (q-o-q)

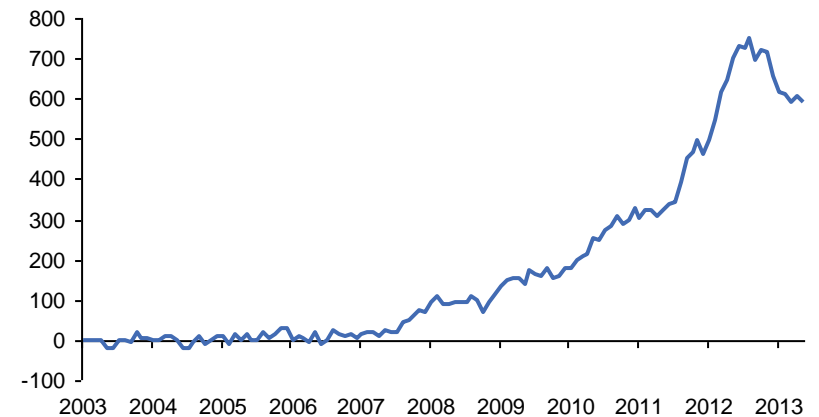


EMU: Corporate spreads*, basis points



* Calculated as: Corporate bond yields (7-10yr.) minus average of govt. benchmark bond yields with maturity of 7 and 10 years.

Net claims of Bundesbank within the Eurosystem (TARGET2), EUR bn

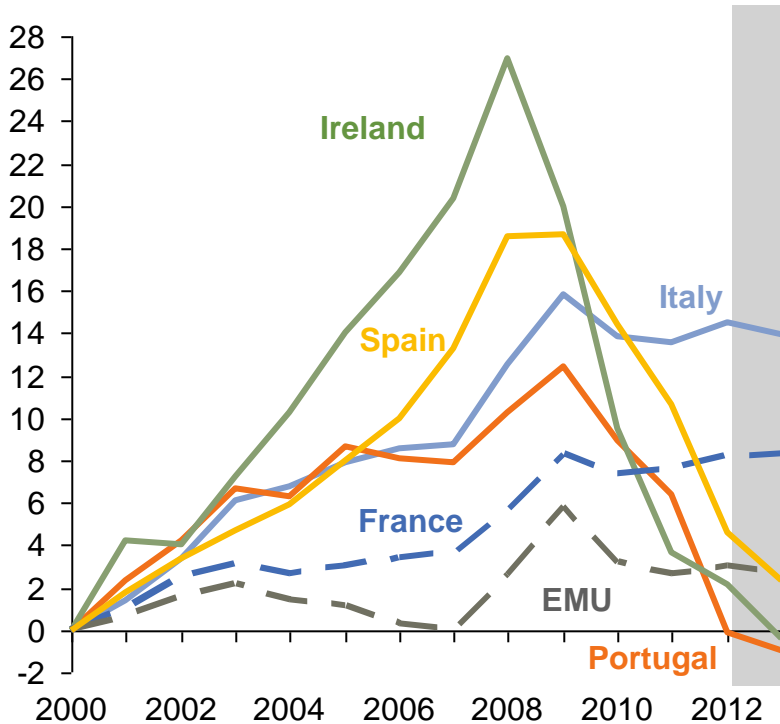


Sources: Deutsche Bundesbank, EcoWin.

EMU: Macroeconomic adjustment is substantial

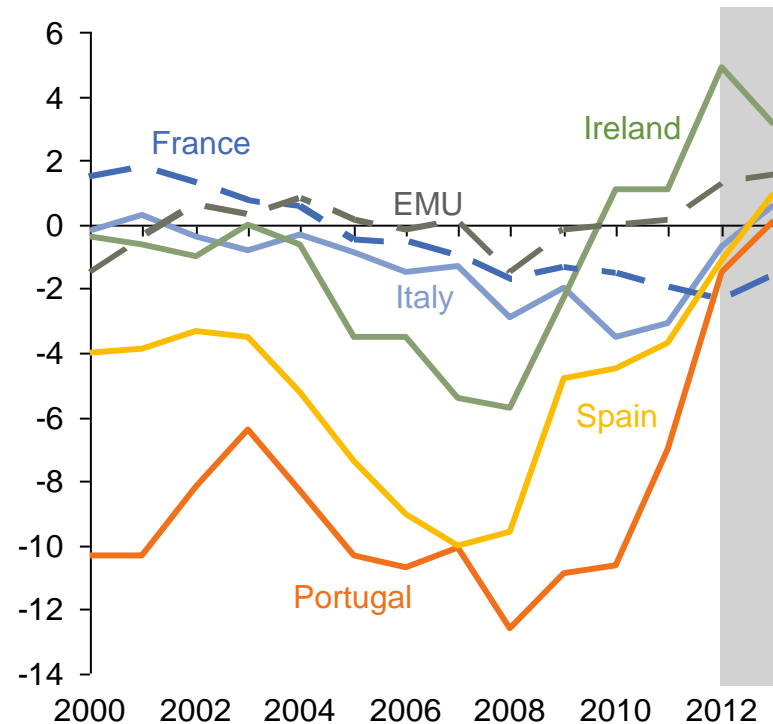
Nominal unit labor costs

Index 2000 = 100, deviation from target path of 1.5% rise per year



Current account balances

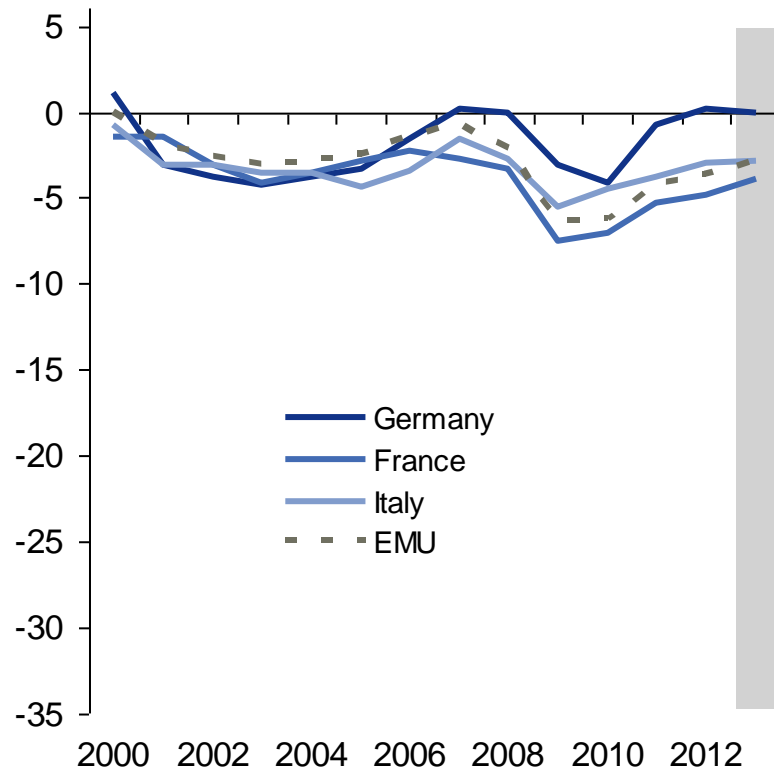
as % of GDP



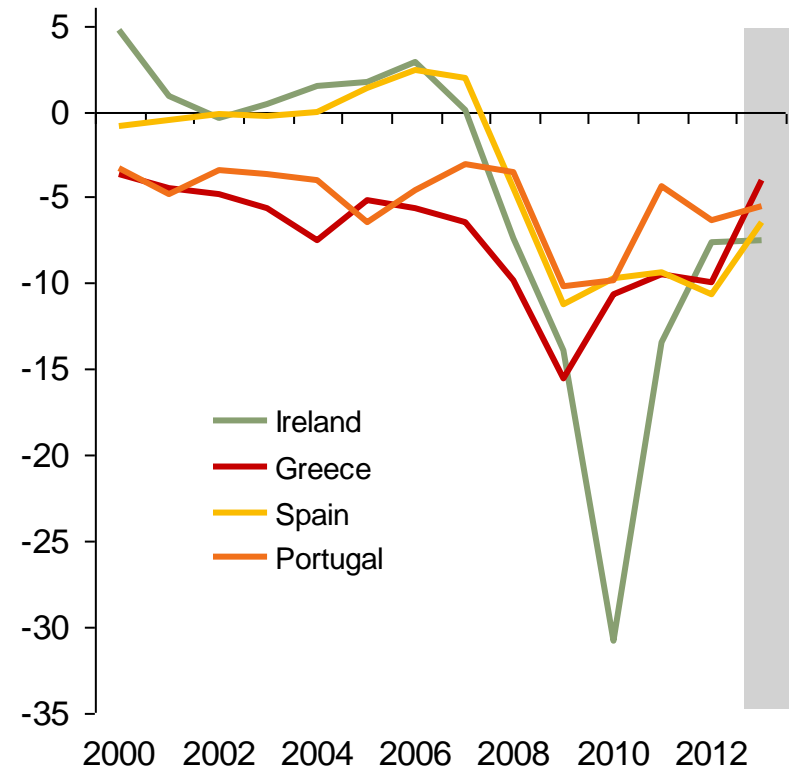
Sources: EcoWin, Eurostat, own calculations and forecasts.

EMU: Consolidation process continues with some delay

Public budget balances, as % of GDP



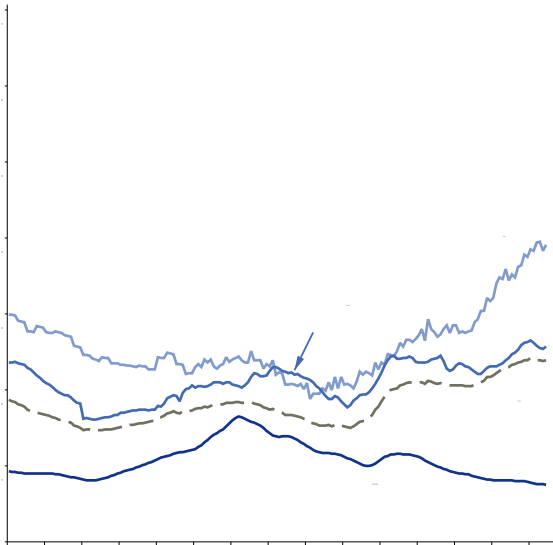
Public budget balances, as % of GDP



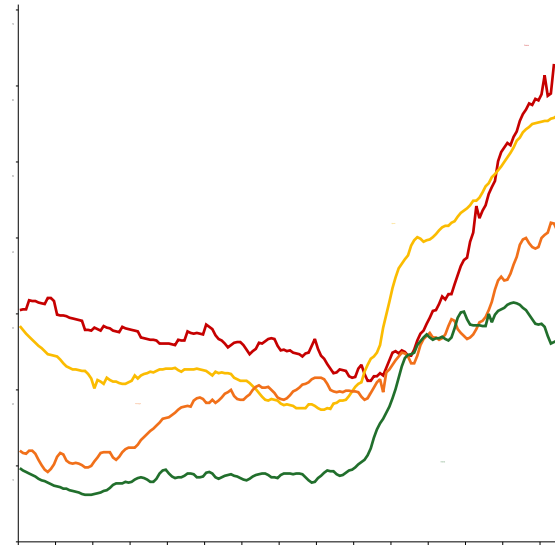
Source: Eurostat, own forecasts.

EMU: Powder keg record-high youth unemployment

Youth unemployment rate*, in %



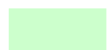
Youth unemployment rate*, in %



*) Harmonized, share of unemployed persons aged less than 25 years in relation to the labor force of the same age group. Source: Eurostat.

Structural reform drives – where progress has been achieved

	Greece	Ireland	Portugal	Spain	Italy
Consolidation	far-reaching action	far-reaching action	far-reaching action	far-reaching action	significant action
Public sector efficiency	some action, but still major reform needs and/or insufficient implementation	significant action	significant action	some action, but still major reform needs and/or insufficient implementation	some action, but still major reform needs and/or insufficient implementation
Pensions	far-reaching action	far-reaching action	far-reaching action	far-reaching action	far-reaching action
Labor market	far-reaching action	significant action	far-reaching action	far-reaching action	some action, but still major reform needs and/or insufficient implementation
Deregulation (product markets, professions)	significant action	significant action	significant action	significant action	significant action
Privatization	some action, but still major reform needs and/or insufficient implementation	significant action	far-reaching action		
Financial system	significant action	far-reaching action	far-reaching action	far-reaching action	



far-reaching action



significant action

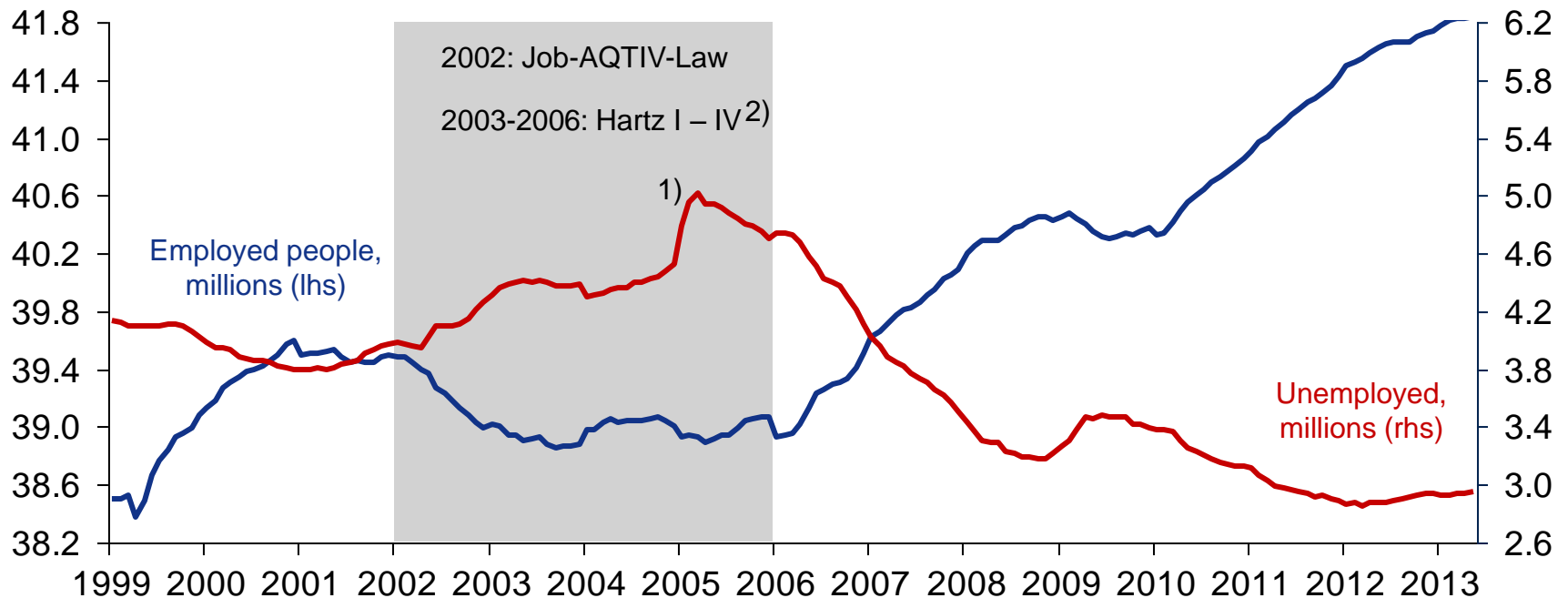


some action, but still major reform needs and/or insufficient implementation

empty = no action / no reform needed

It does not take too long for reforms to start working

Germany: Labor market trends and labor market reforms



1) Welfare benefit recipients capable of work redefined as registered unemployed.

2) Hartz I and II (2003): Liberalization of temporary work; tightening of job suitability rules, Me Incs, job centers, new rules for minijobs and midijobs.

Hartz III (2004): Restructuring of Federal Labor Office, less employment protection in small companies.

Hartz IV (2005-2006): Merging of unemployment and welfare benefit, tightening of entitlement requirements, shorter entitlement period for unemployment benefit.

Source: EcoWin.

Turning to the European level: Key priorities for restoring growth

- Infrastructure improvements (also via project bonds)
- Completion of the single market
- TTIP – exploiting the growth potential of trade
- Joint qualification and education efforts
- Curbing youth unemployment through rechanneling of EU funds

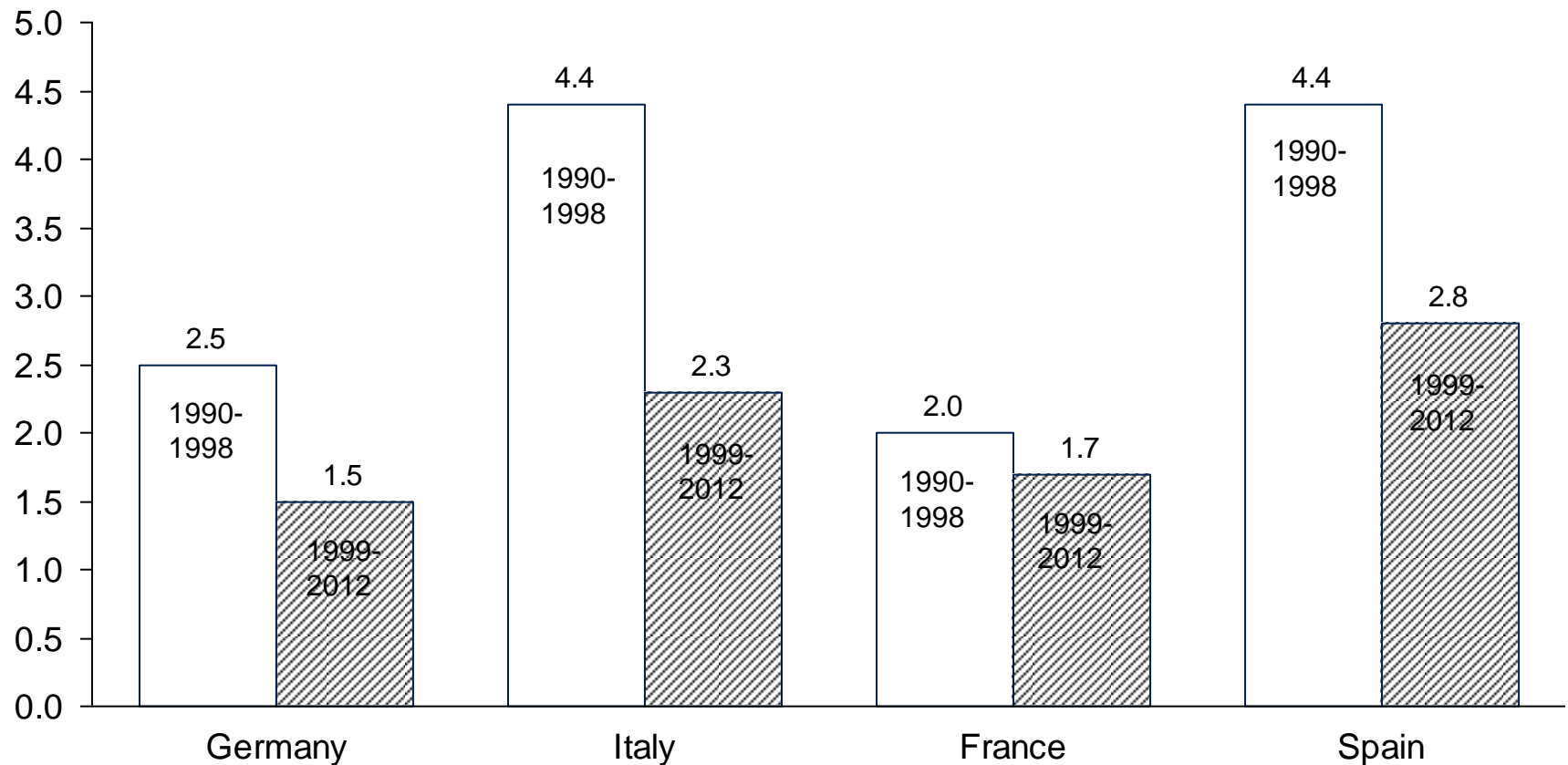
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Success of the euro in stabilizing prices

Inflation rates also lower in stable countries

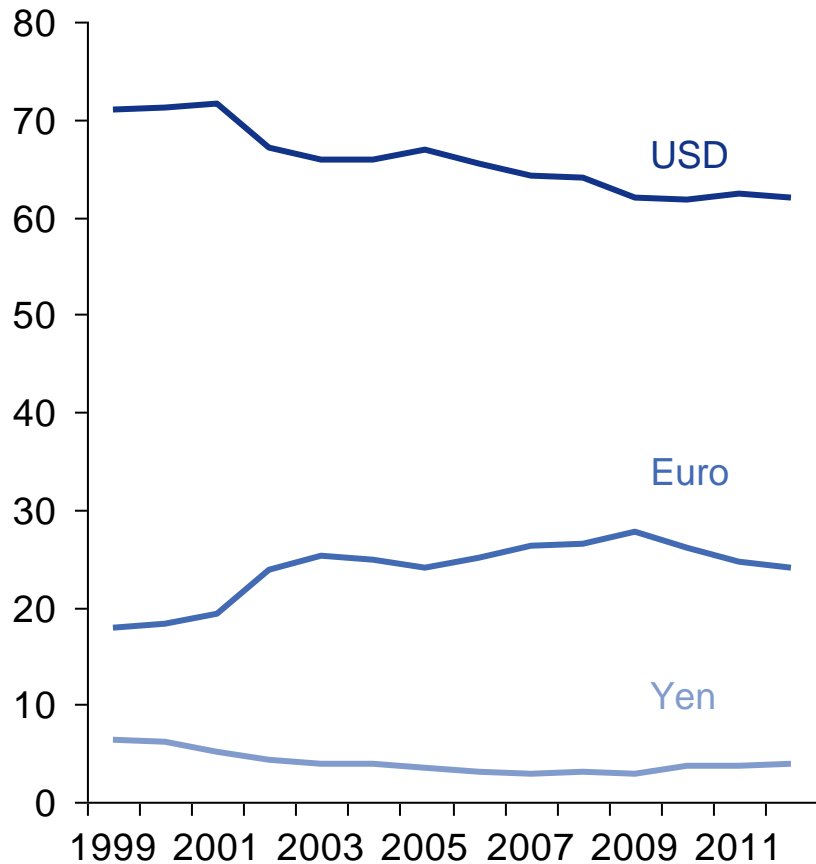
Average yearly rate before (1990-1998) and with the euro (1999-2012)



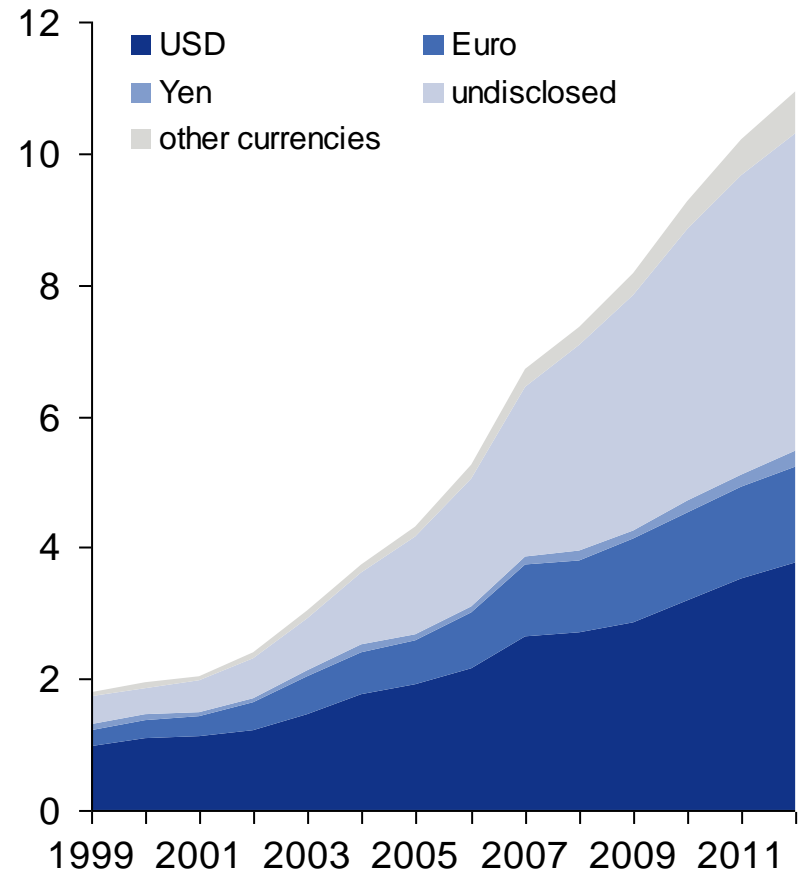
Sources: EcoWin, Allianz calculations.

Currency composition of global foreign exchange rates: Emergence of a global currency

Shares of disclosed reserves

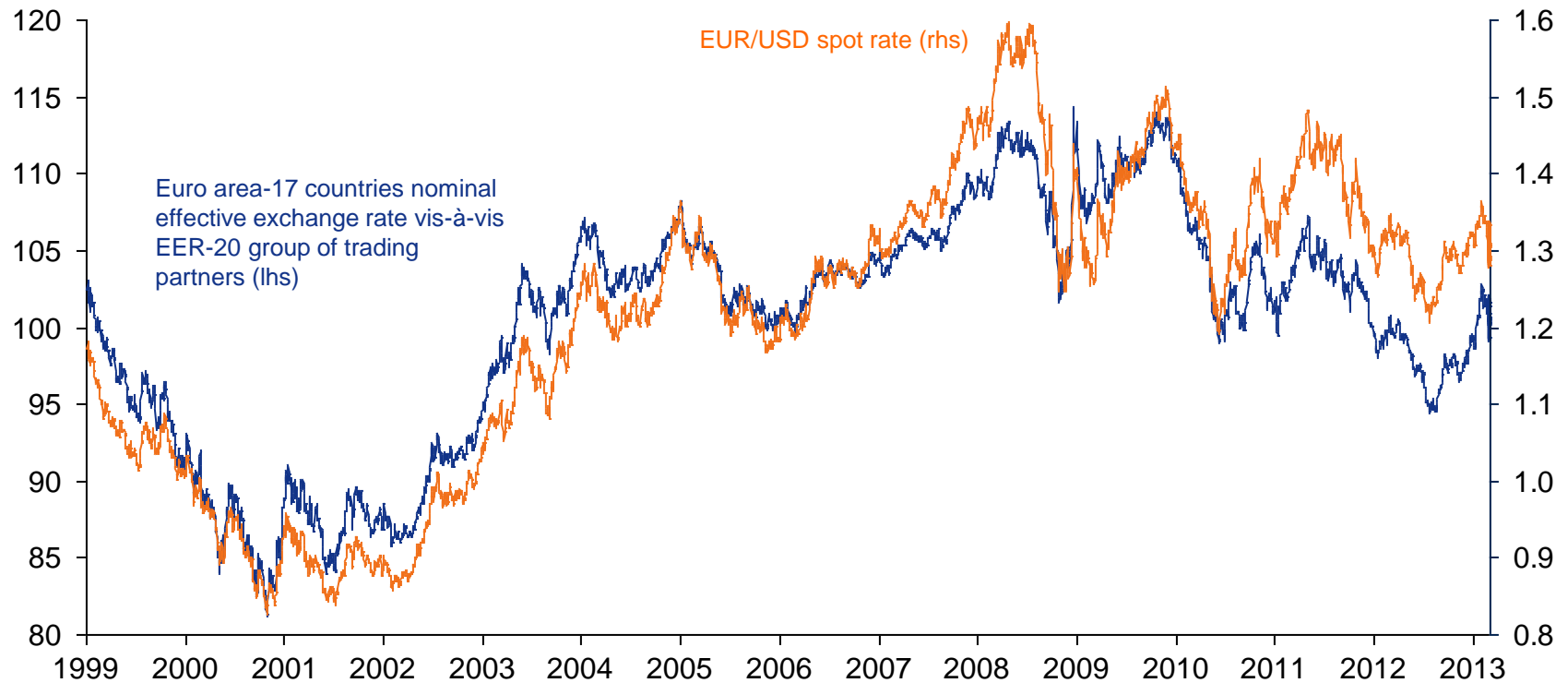


Amounts in trillion USD



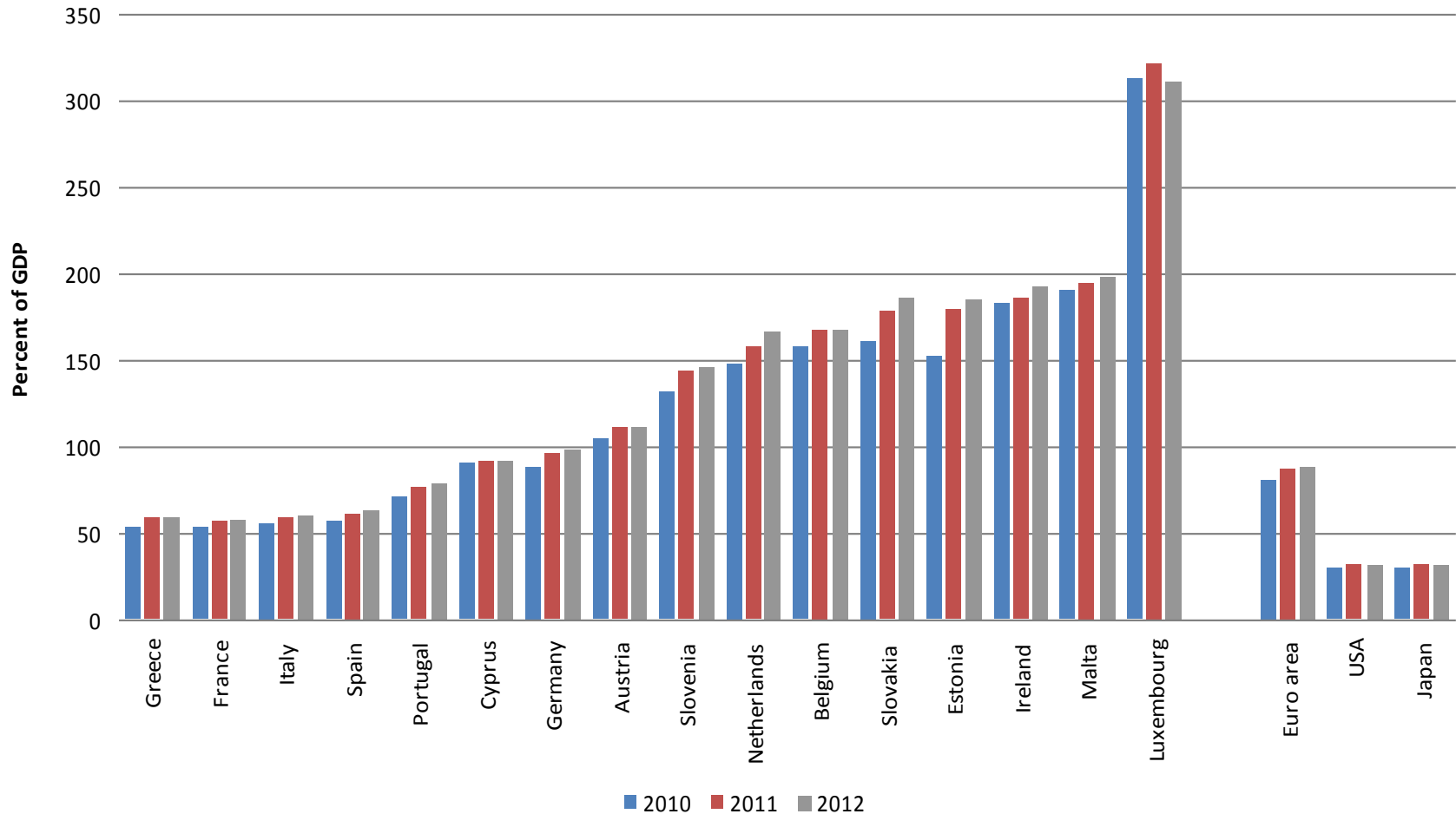
Source: IMF Statistics Department COFER database and International Financial Statistics.

The euro has a fairly high valuation



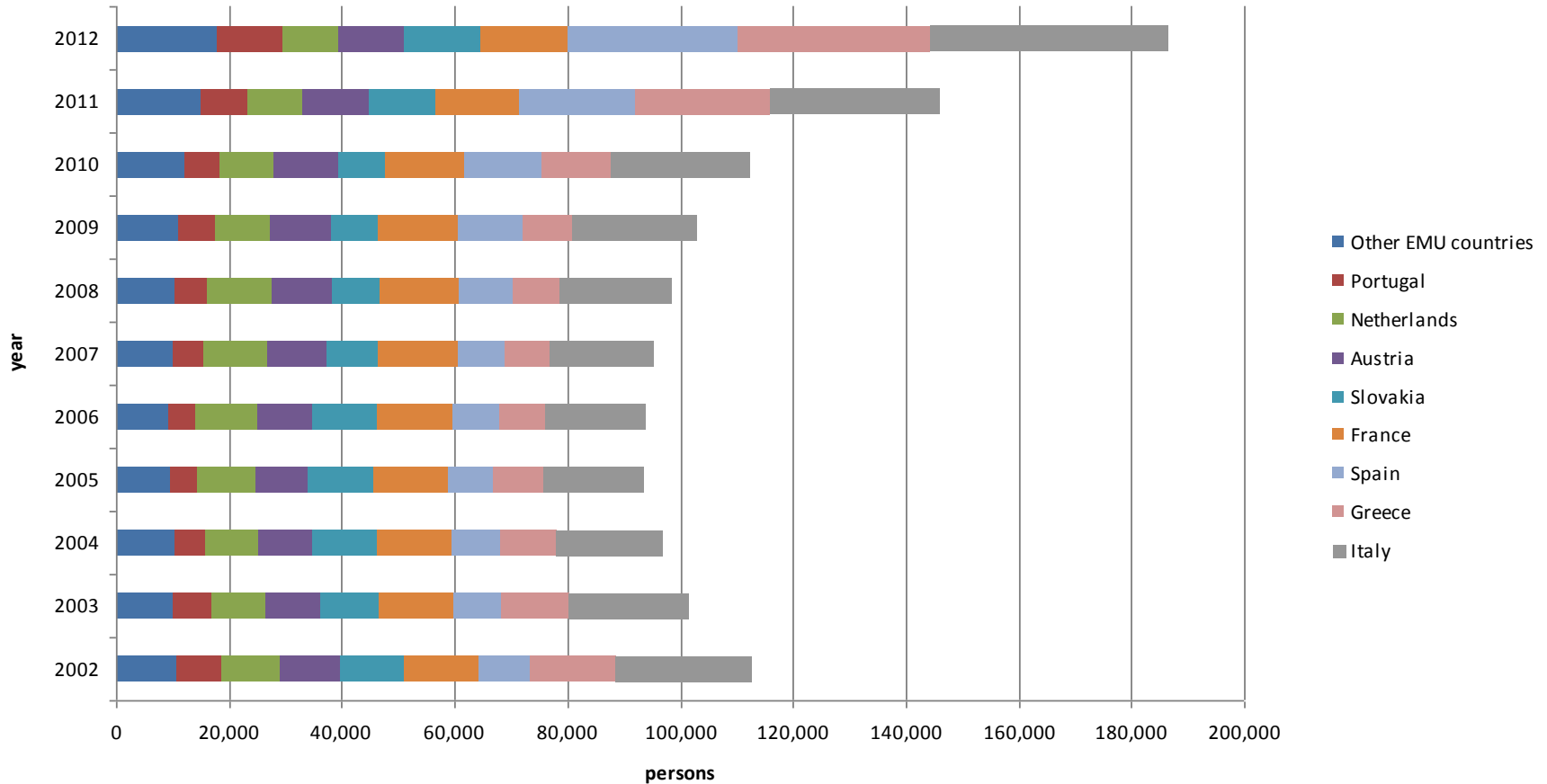
Source: EcoWin.

An optimum currency area? Openness indicator



The Openness Indicator is defined as the sum of imports and exports of goods and services in percent of national GDP. The graph is based on national account data (current prices) from Eurostat Database. Data for Greece is provisional. Euro area includes all member states of the respective year.

Migration from other EMU countries to Germany (non-nationals)



2012: preliminary data.
Source: Statistisches Bundesamt, Wiesbaden 2012.

A toothless stability pact: Heatmap on the deficit criterion

Country	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Austria	yellow	yellow	blue	yellow	yellow	red	yellow	yellow	yellow	yellow	red	red	yellow
Belgium	yellow	blue	light green	yellow	yellow	yellow	yellow	light green	yellow	yellow	red	red	red
Cyprus	red	yellow	yellow	red	red	red	yellow	yellow	green	light green	red	red	red
Estonia	red	yellow	yellow	light green	light green	light green	light green	light green	light green	yellow	yellow	light green	light green
Finland	light green	green	green	green	light green	light green	light green	green	green	green	yellow	yellow	yellow
France	yellow	yellow	yellow	red	red	red	yellow	yellow	yellow	red	red	red	red
Germany	yellow	light green	red	red	red	red	red	yellow	light green	yellow	red	red	yellow
Greece	red	red	red	red	red	red	red	red	red	red	red	red	red
Ireland	light green	green	light green	yellow	light green	light green	light green	light green	light green	red	red	red	red
Italy	yellow	yellow	red	red	red	red	red	red	yellow	yellow	red	red	red
Luxemburg	green	green	green	light green	light green	yellow	blue	light green	green	green	yellow	yellow	yellow
Malta	red	red	red	red	red	red	yellow	yellow	yellow	red	red	red	yellow
Netherlands	light green	light green	yellow	yellow	red	yellow	yellow	light green	light green	light green	red	red	red
Portugal	red	red	red	red	red	red	red	red	red	red	red	red	red
Slovakia	red	red	red	red	yellow	yellow	yellow	red	yellow	yellow	red	red	red
Slovenia	yellow	red	red	yellow	yellow	yellow	yellow	yellow	blue	yellow	red	red	red
Spain	yellow	yellow	yellow	yellow	yellow	yellow	light green	light green	light green	red	red	red	red



Source: EcoWin.

Seven steps towards Euro 2023

1. Reform of EU governance enhancing EU decision-making and democratic legitimacy of EU institutions.
2. Explicit exit rules for countries that do not live up to their commitments within the Monetary Union.
3. A precise fiscal rulebook empowering an EU finance commissioner to intervene when necessary.
4. An effective mechanism at EU level to detect and correct the development of imbalances that could derail economies.
5. Enhanced competencies for European institutions, particularly with regard to the European banking system.
6. More common policies that lead investments in Europe's physical and intellectual infrastructure boosting growth and competitiveness.
7. A sovereign debt restructuring mechanism guaranteeing an orderly process in the case of default.



Appendix

Euro area: Economic indicators and forecasts*

	2012				2013				2014				2012	2013f	2014f	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
GDP real	-0.1	-0.2	-0.1	-0.6	-0.3	0.3	0.3	0.3	0.5	0.4	0.4	0.4	-0.5	-0.3	1.5	
Private consumption	-0.2	-0.5	-0.1	-0.6	0.0	0.2	0.2	0.2	0.2	0.2	0.3	0.3	-1.3	-0.3	0.9	
Government spending	-0.1	-0.3	-0.1	0.0	-0.2	0.0	0.0	0.1	0.0	0.0	0.0	0.0	-0.4	-0.2	0.0	
Investment	-1.3	-1.8	-0.8	-1.5	-1.9	0.3	0.7	0.5	0.8	0.5	0.6	0.6	-4.2	-3.2	2.5	
Exports	0.8	1.5	0.8	-0.9	-0.9	1.3	1.4	1.0	1.2	1.2	1.3	1.0	2.9	1.1	4.8	
Imports	0.0	0.3	0.2	-1.2	-1.2	1.0	1.4	0.8	0.7	1.0	1.2	1.0	-0.7	-0.3	4.0	
Industrial production (excl. construction)	-0.5	-0.6	0.1	-2.0	0.2	0.9	0.4	0.5	0.7	0.6	0.6	0.6	-2.3	-0.5	2.5	
Unemployment rate	%	10.9	11.3	11.5	11.8	12.0	12.1	12.3	12.3	12.1	12.0	11.9	11.7	11.4	12.2	11.9
Consumer prices	y-o-y	2.7	2.5	2.5	2.3	1.9	1.4	1.4	1.3	1.3	1.4	1.5	1.6	2.5	1.5	1.5
Producer prices	y-o-y	4.0	2.7	2.6	2.4	1.2	0.0	0.1	0.9	1.2	2.6	2.4	2.0	2.9	0.6	2.0
Current account balance	EUR bn, nsa	20.4	27.2	35.3	43.5	57.2	55.0	40.0	40.0	45.0	45.0	40.0	35.0	126.4	192.2	165.0
	% of GDP													1.3	2.0	1.7
Budget balance	% of GDP													-3.7	-2.9	-2.5

* quarterly values: percentage change over previous period, seasonally adjusted, except where noted; annual GDP not adjusted; foreign trade incl.intra trade

f = forecast.