



# **Some ideas on the Future of the European Union or how to rebuild confidence**

**Thomas Westphal**  
Director General European Policy  
German Federal Ministry of Finance

March 3, 2017  
College of Europe, Bruges

## Four points:

1. Many forms of crisis – one word to describe them all: loss of confidence
2. EMU: from success to crisis
3. Solutions at the aggregate level?
4. A policy proposal

## Four points:

- 1. Many forms of crisis – one word to describe them all: loss of confidence**
2. EMU: from success to crisis
3. Solutions at the aggregate level?
4. A policy proposal

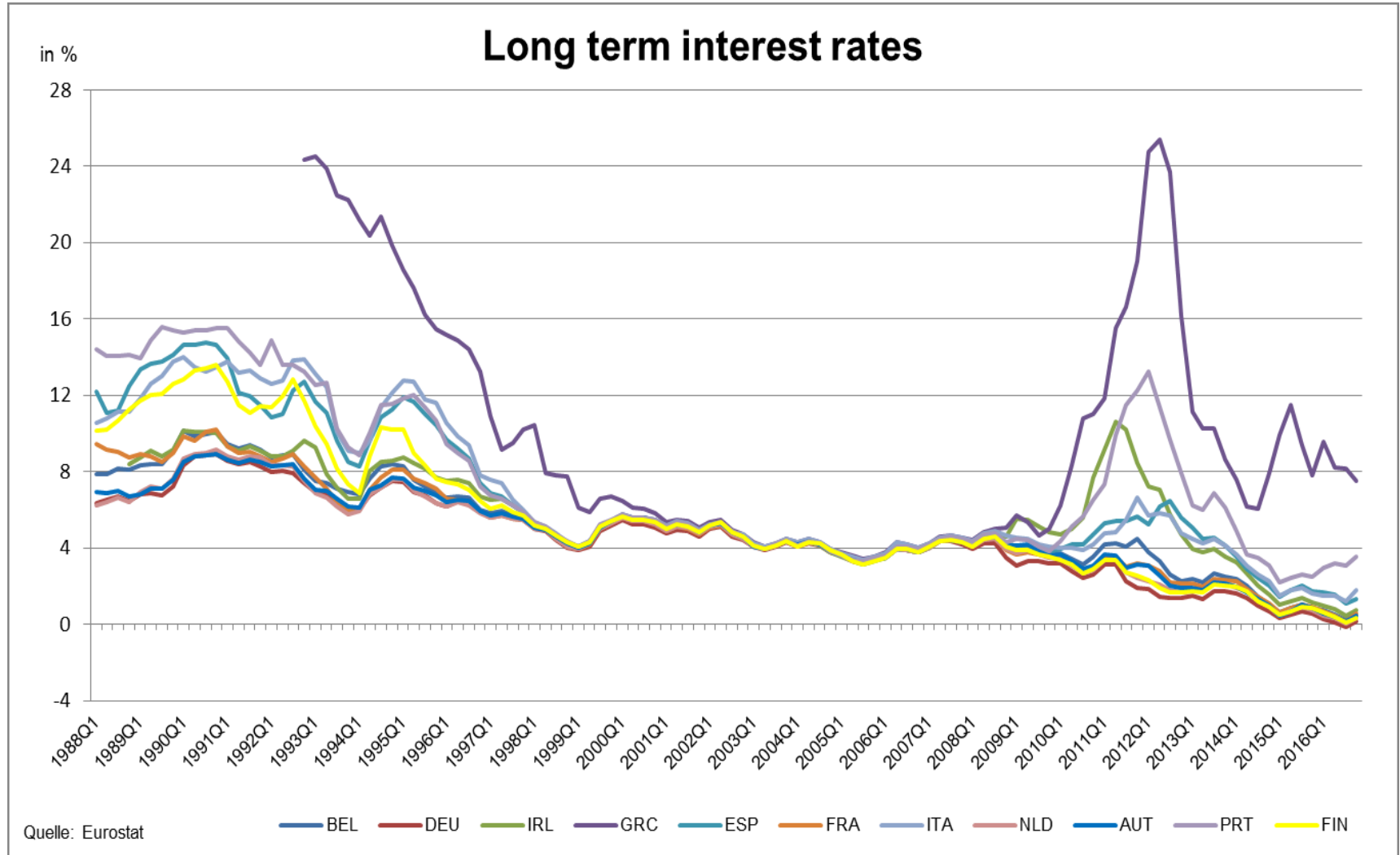
“For years, I’ve been troubled by the problem of understanding the social psychology and economic impact of confidence.”

Robert Shiller, 2013

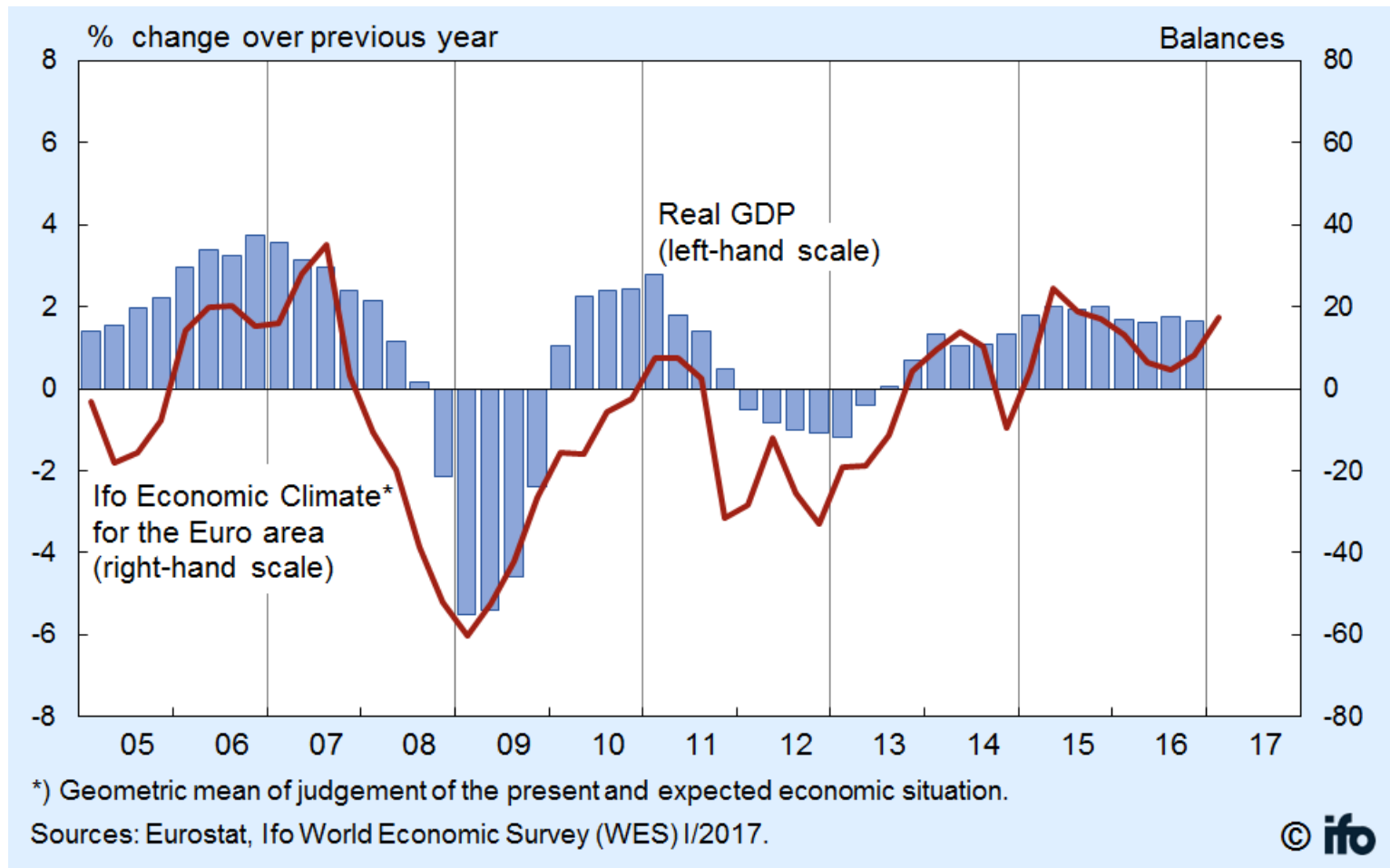
“Confidence... thrives on honesty, on honour, on the sacredness of obligations, on faithful protection and on unselfish performance. Without them it cannot live"

Franklin D. Roosevelt, 1933

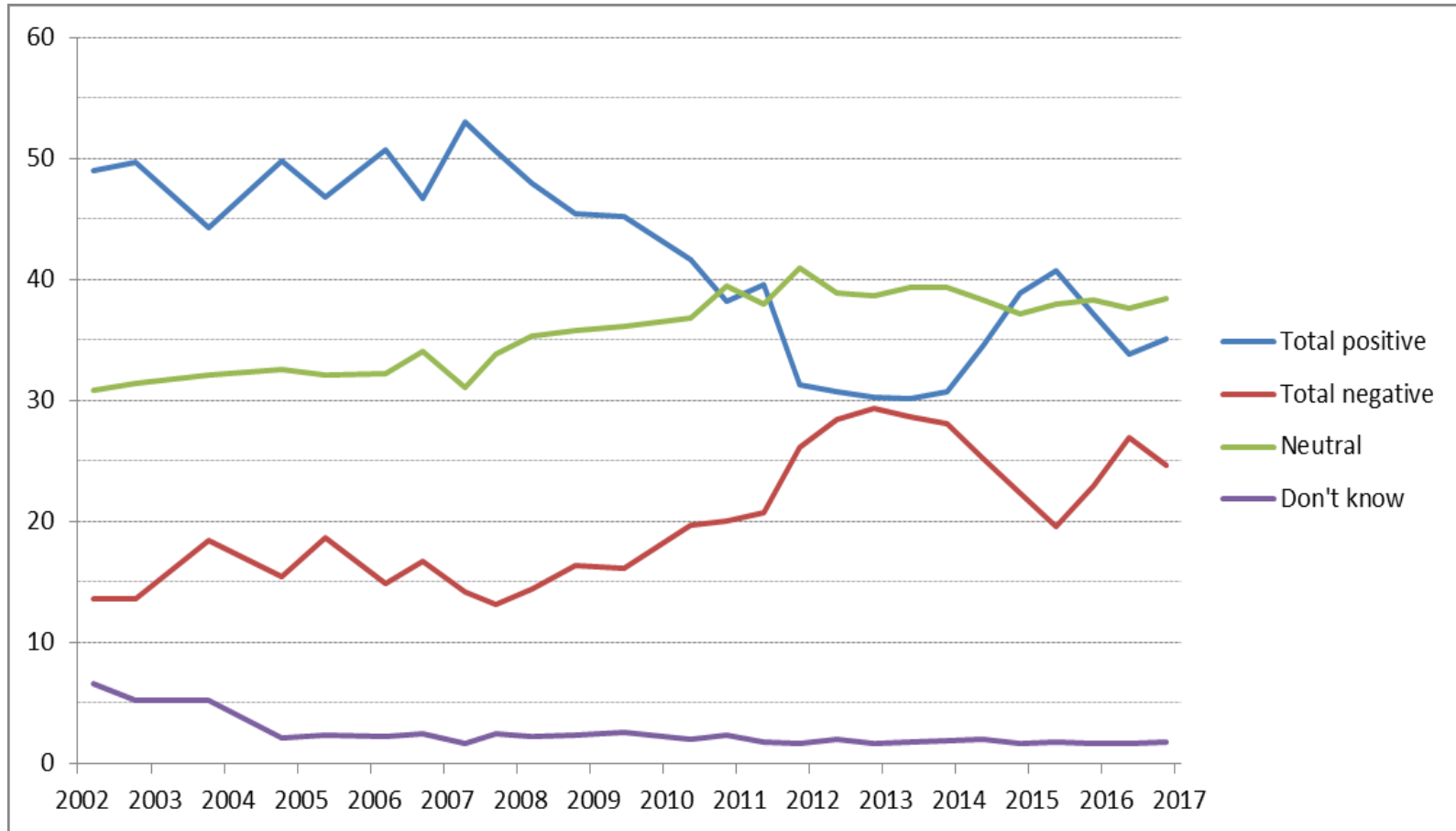
# à la recherche de la confiance perdue...



# Euro zone: Growth, business climat, Ifo



# Image of the EU



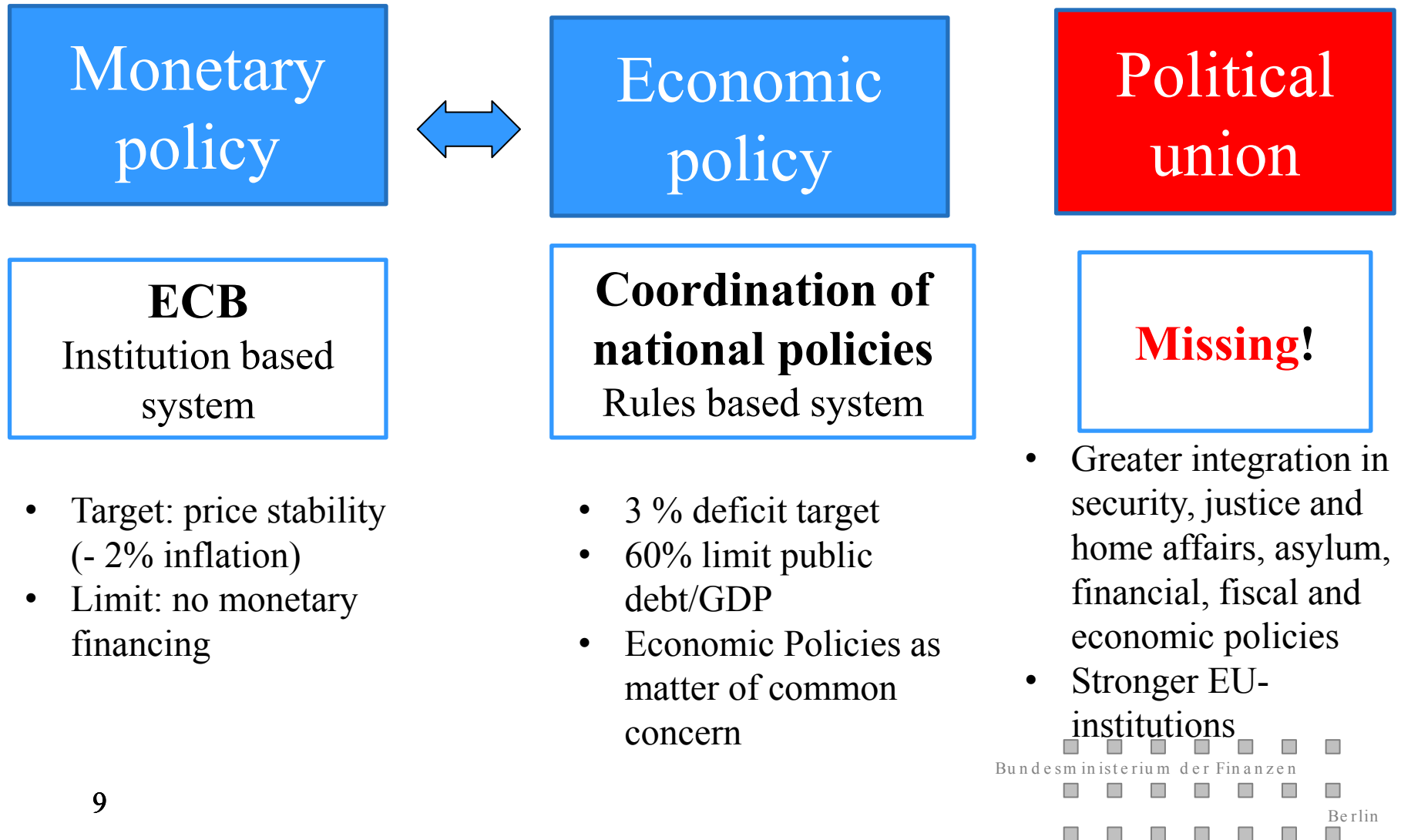
Source: Eurobarometer November 2016, In general, does the European Union conjure up for you a very positive, fairly positive, neutral, fairly negative or very negative image? (in %)

## Four points:

1. Many forms of crisis – one word to describe them all: loss of confidence
- 2. EMU: from success to crisis**
3. Solutions at the aggregate level?
4. A policy proposal

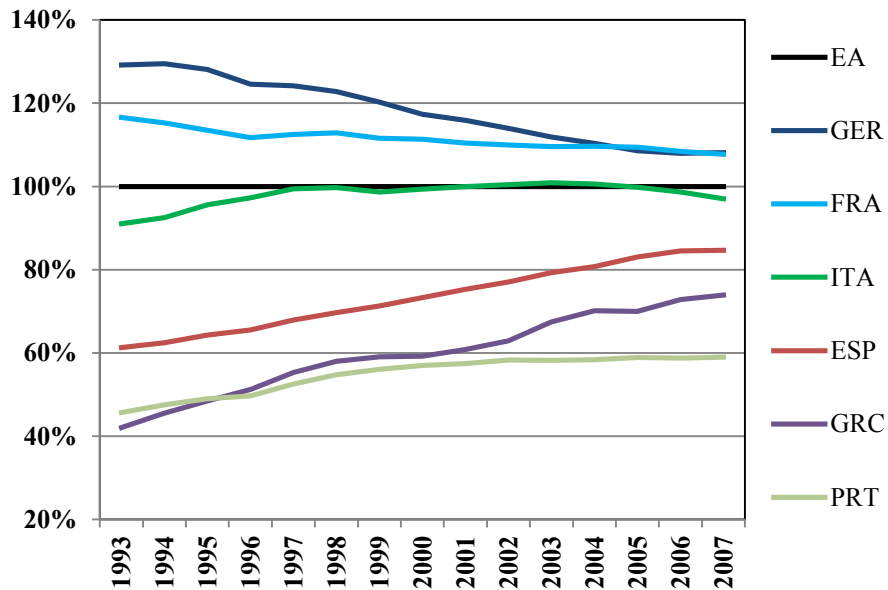


# This is how we started EMU

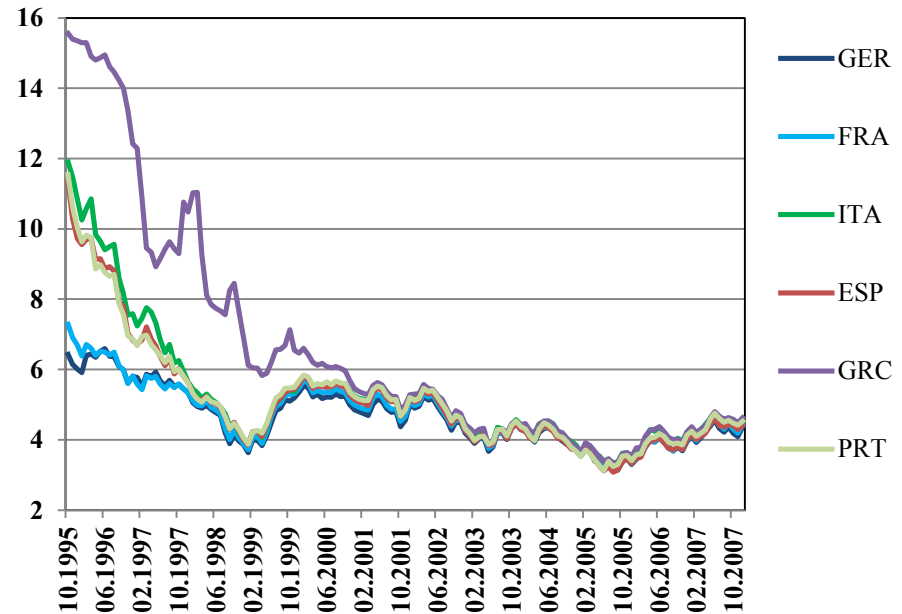


# Years of convergence

**GDP per capita (% of EA)**



**Yields: 10yr government bonds (in %)**



# Optimal Currency Area

Ex-ante criteria:

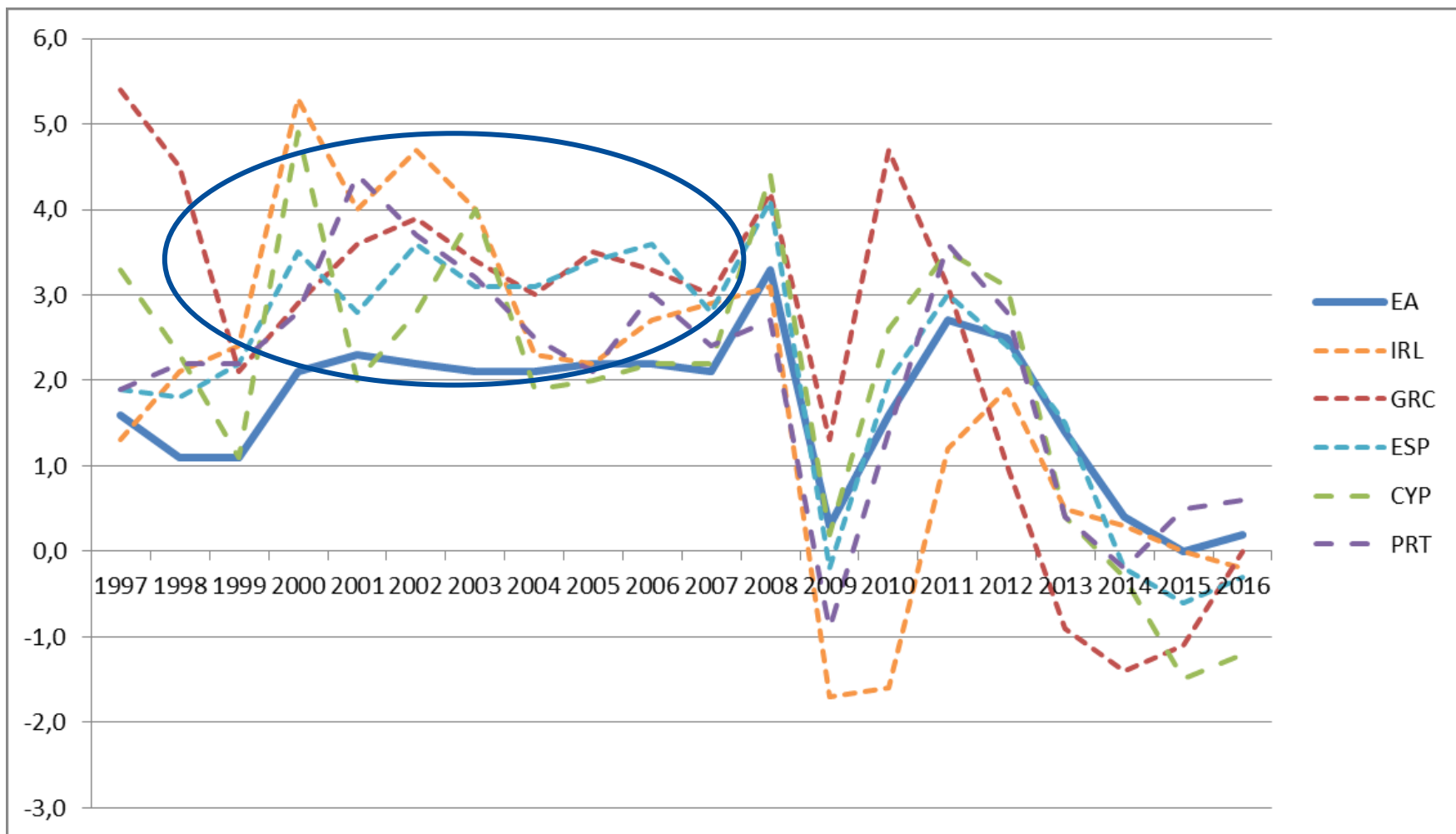
- Flexible prices and wages
- Factor mobility
- Financial market integration
- Open economy

# Optimal Currency Area

Ex-post criteria:

- Trade integration
- Commitment = stability FDI
- Institutional effects

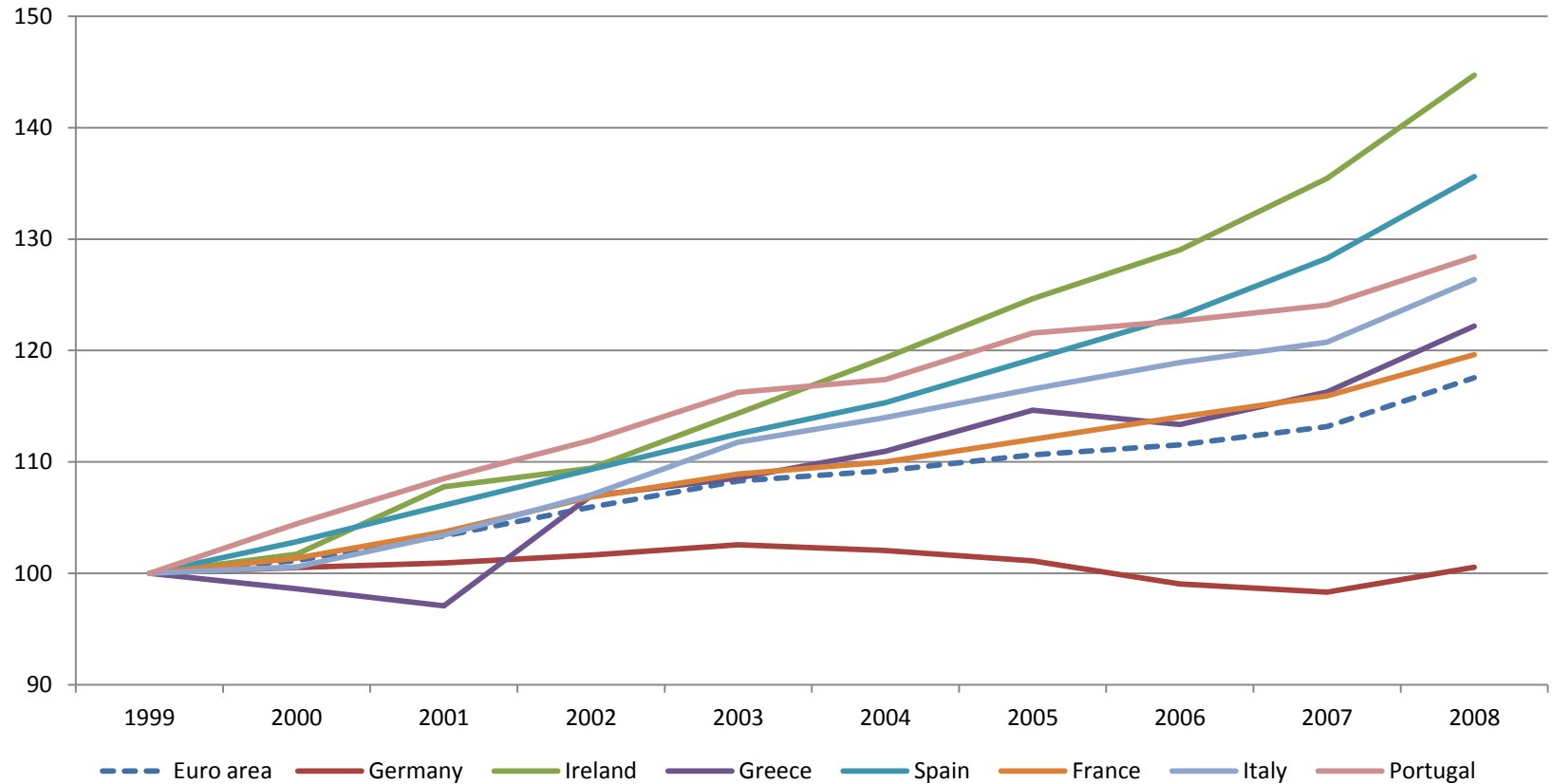
# Inflation divergences



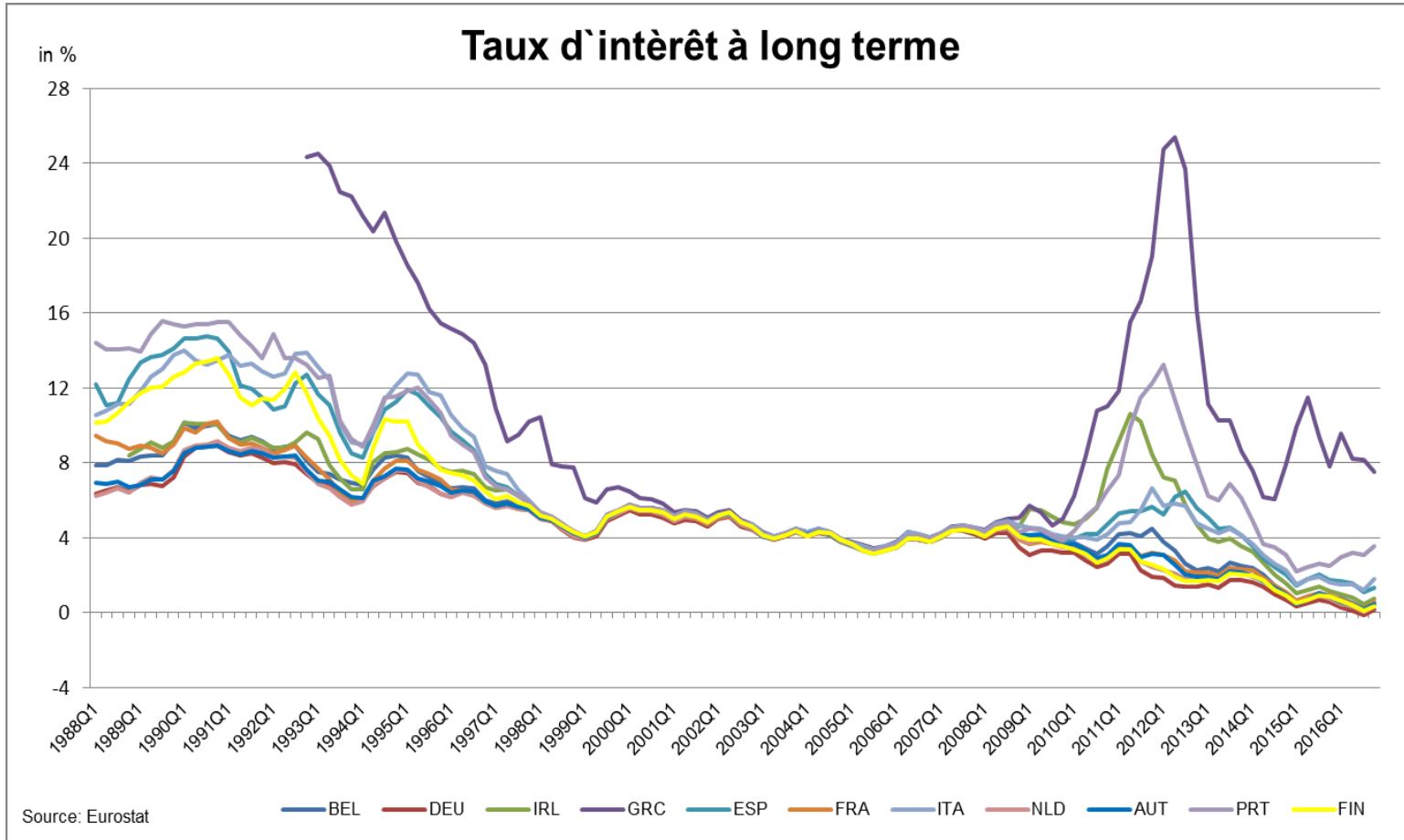
# Building-up of imbalances

## Unit labour costs before the crisis

Index: 1999=100



# EMU countries lost market access!



# Crisis response

**Member  
States**

Reforms to  
improve  
competi-  
tiveness;  
fiscal con-  
solidation

**Financial  
markets**

Banking  
union:  
European  
Supervision;  
serious  
regulation

**EMU-  
Governance**

Re-enforcing  
SGP; Macro  
imbalances  
procedure

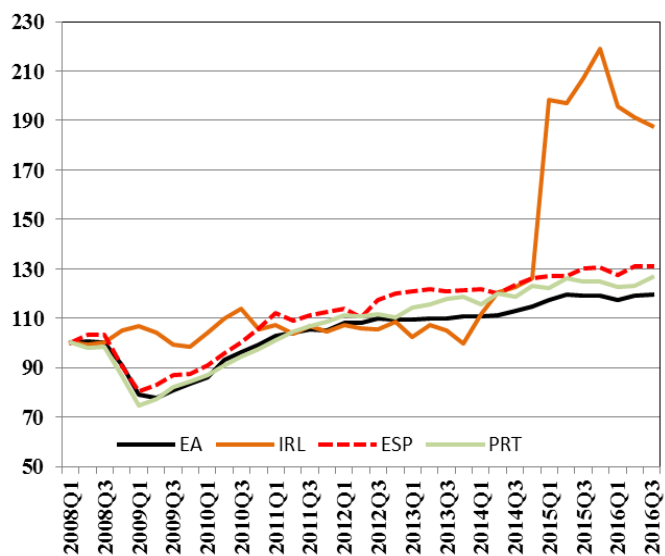
**Crisis  
mechanism:**

EFSM;  
EFSF;  
ESM



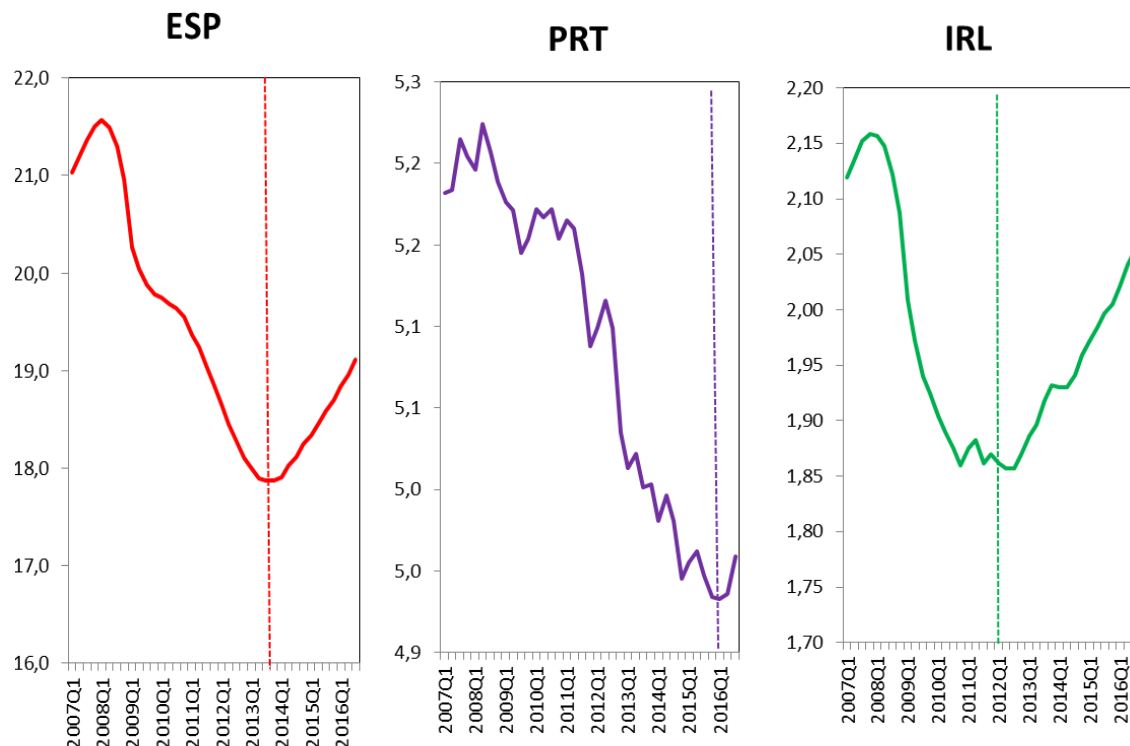
# Successful crisis policies

Export of goods since 2008 (2008Q1=100)



Source: Eurostat

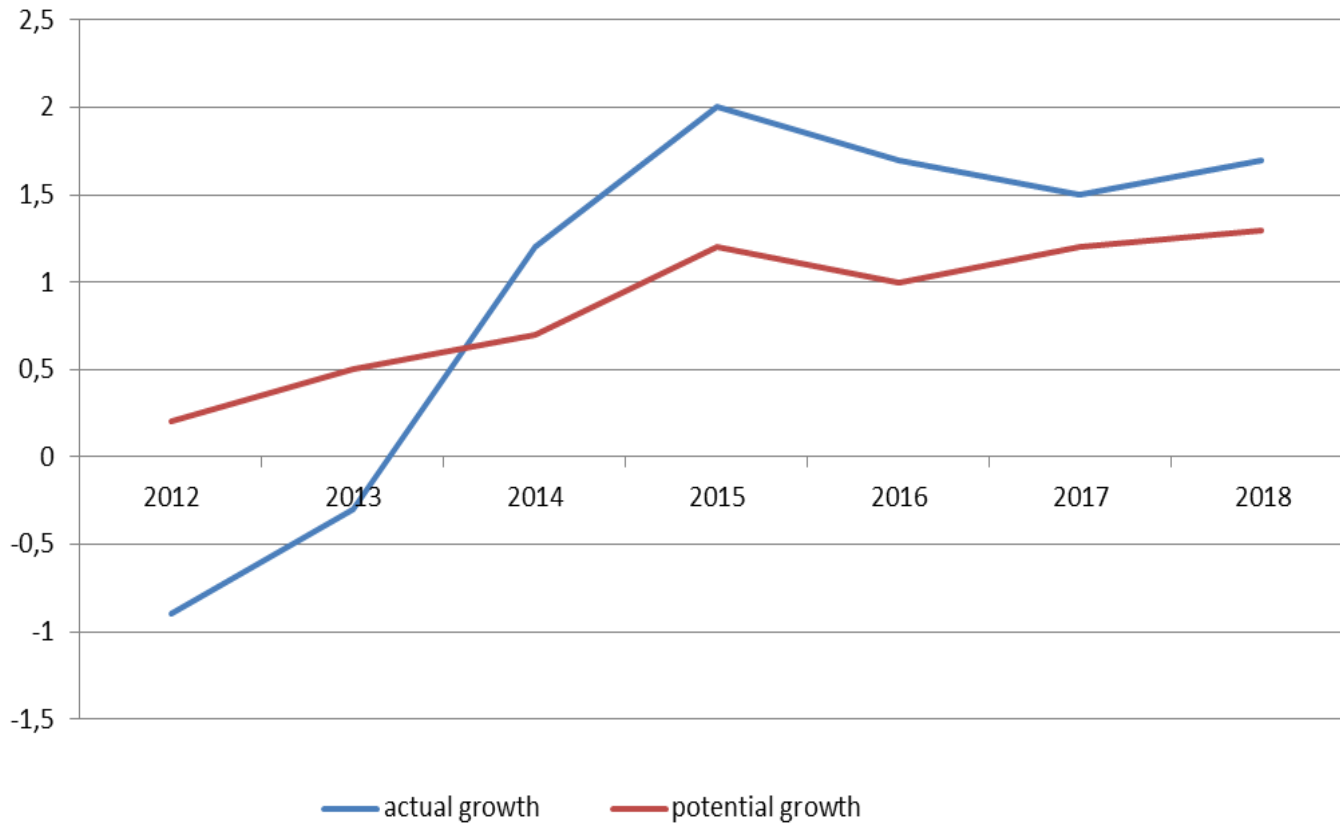
Total employment in million prs. (2007Q1 – 2016Q3)



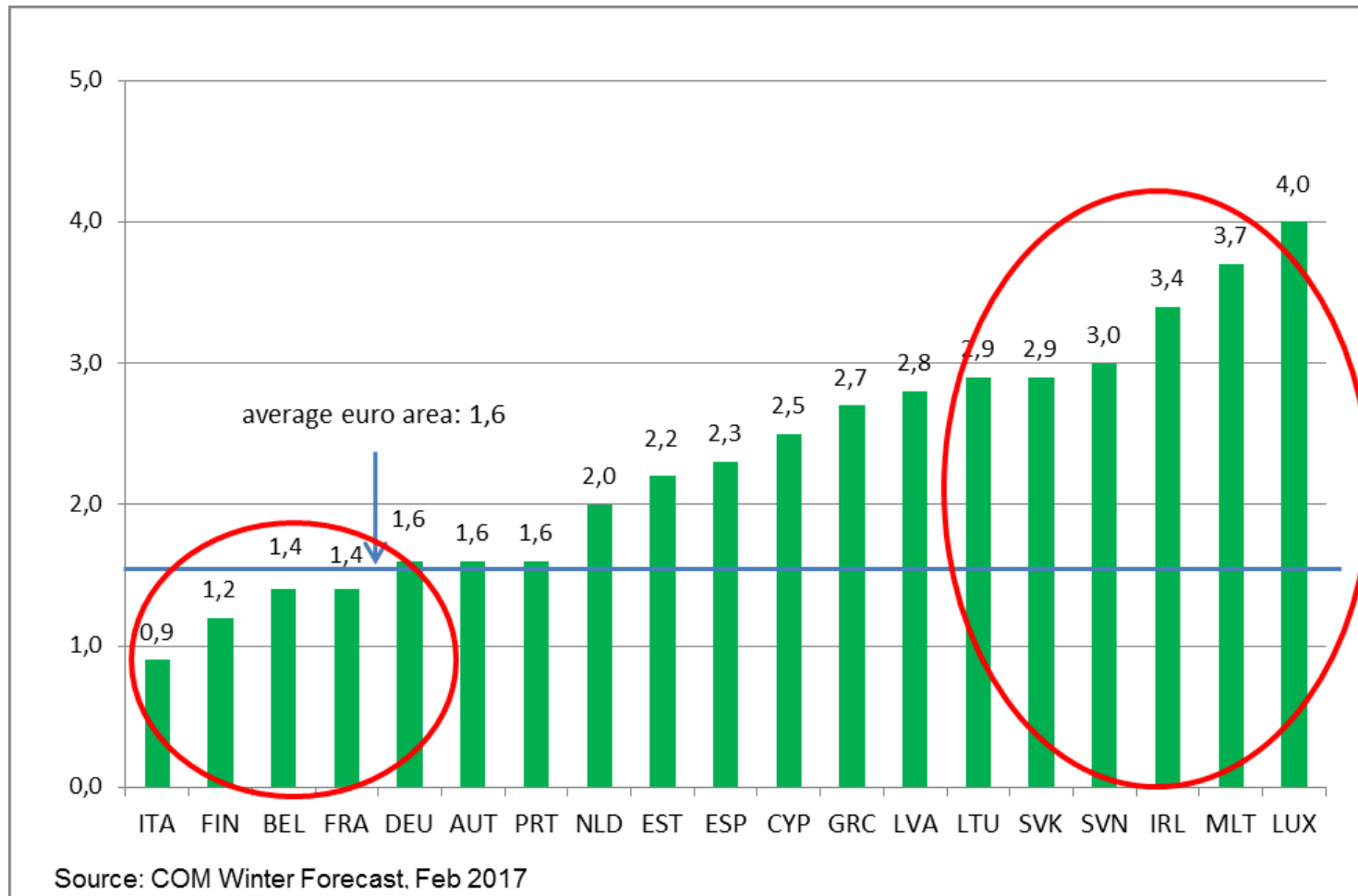
## Four points:

1. Many forms of crisis – one word to describe them all: loss of confidence
2. EMU: from success to crisis
- 3. Solutions at the aggregate level?**
  - **agregate fiscal stance**
  - **one size fits all/European solution for national problems**
4. A policy proposal

## Euro area: real GDP growth

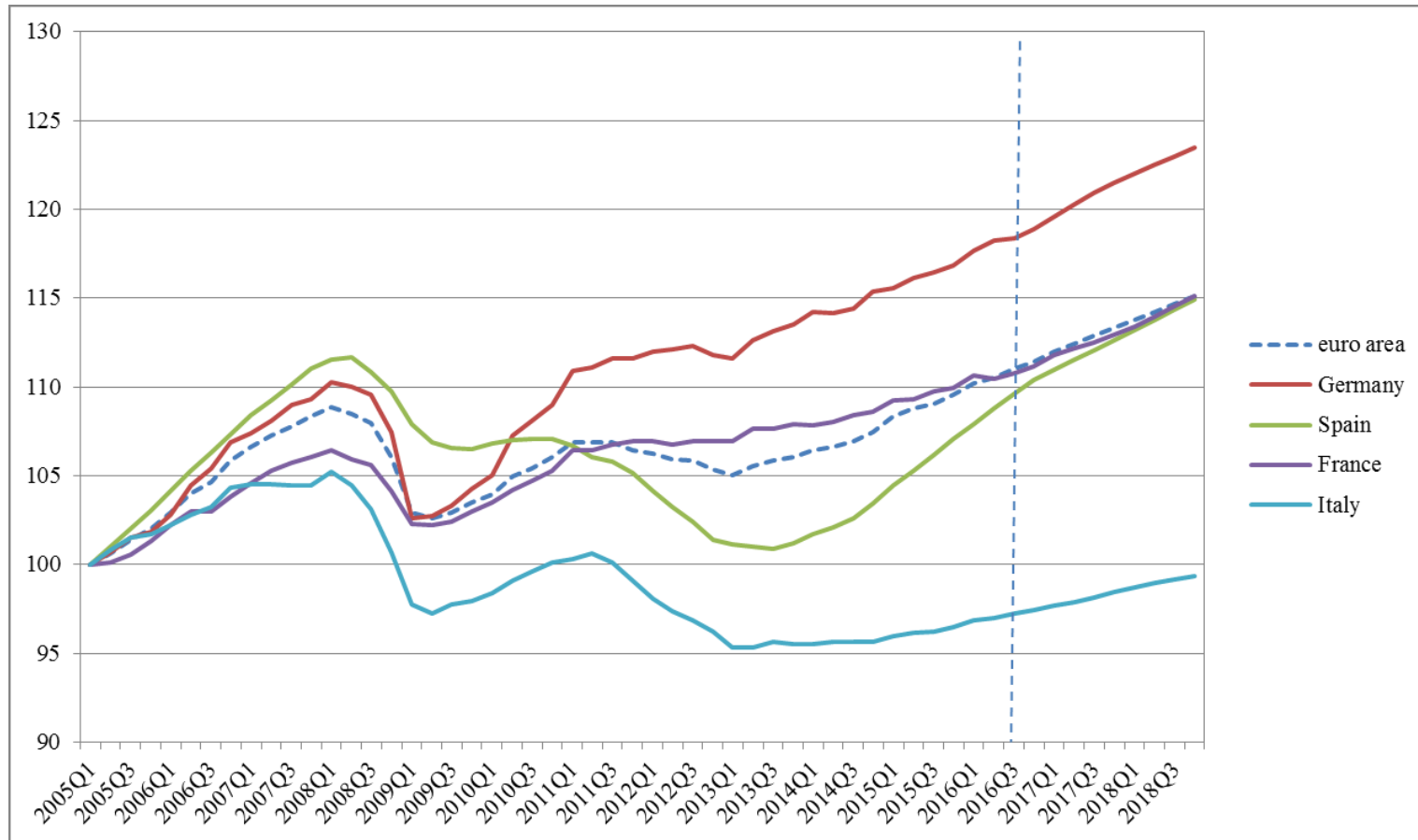


# GDP growth in 2017

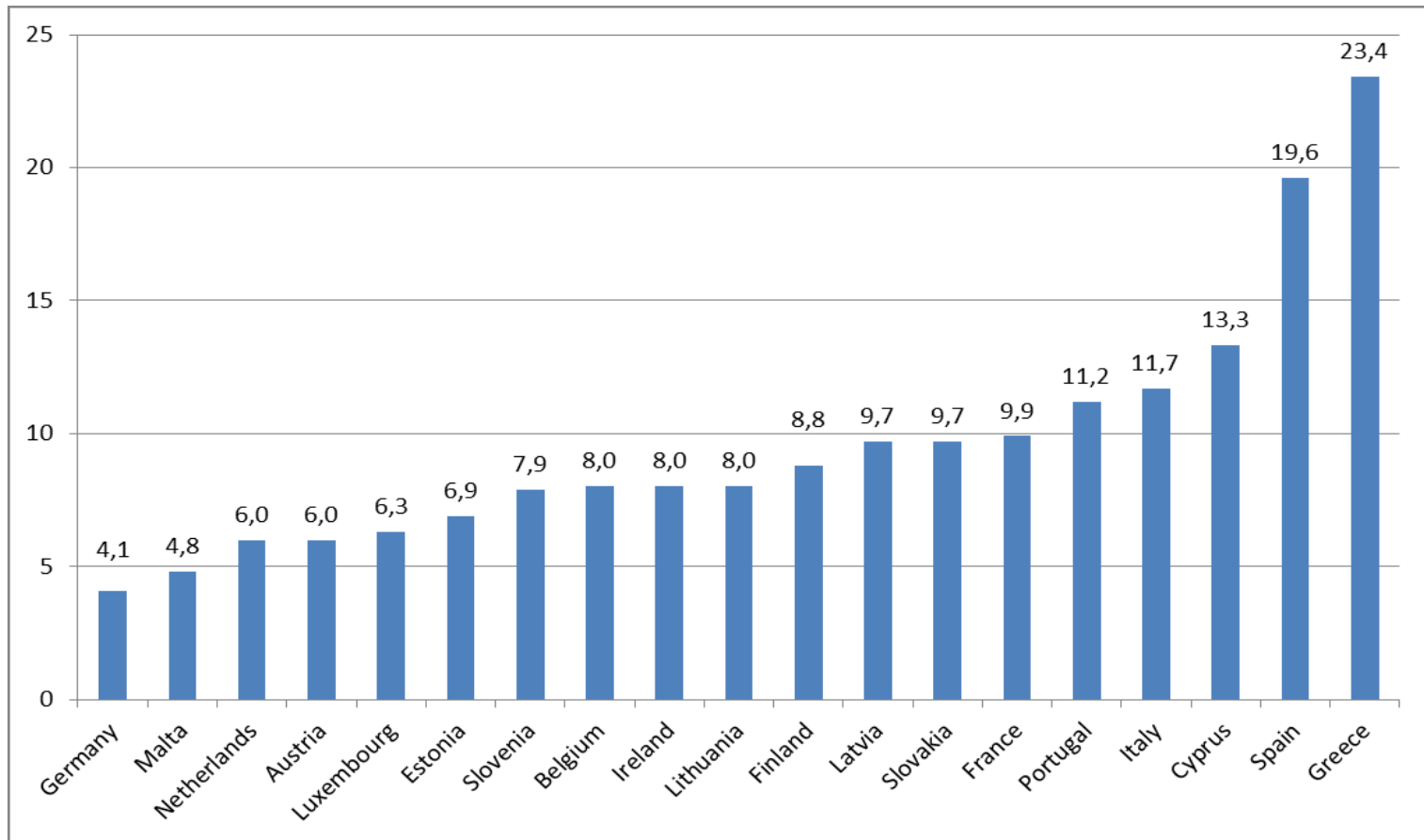


# Real GDP in the euro area

index: 2005Q1=100

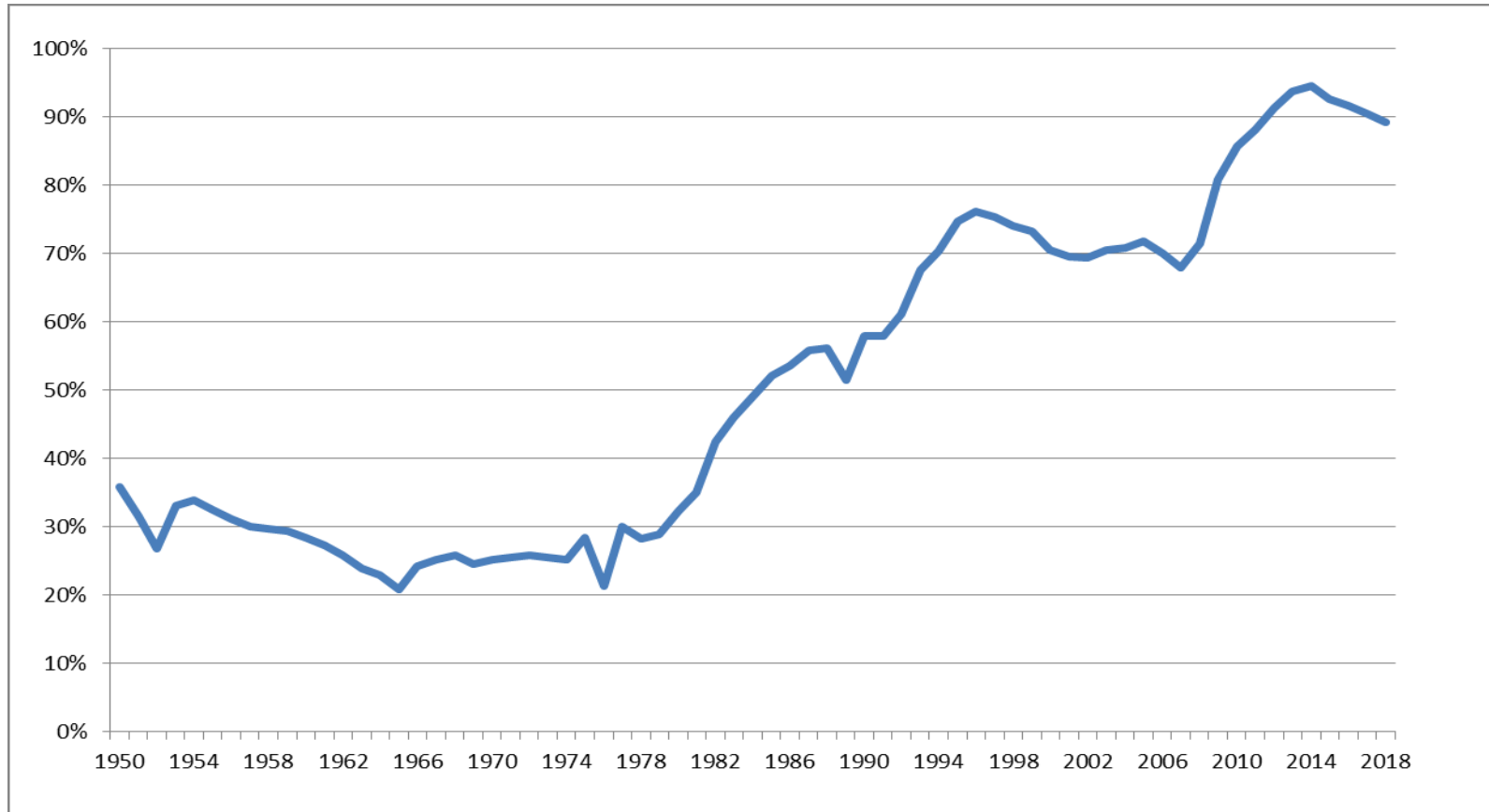


# Unemployment rates in 2016 (in %)



# EMU has a debt problem

Public debt euro area in % of GDP

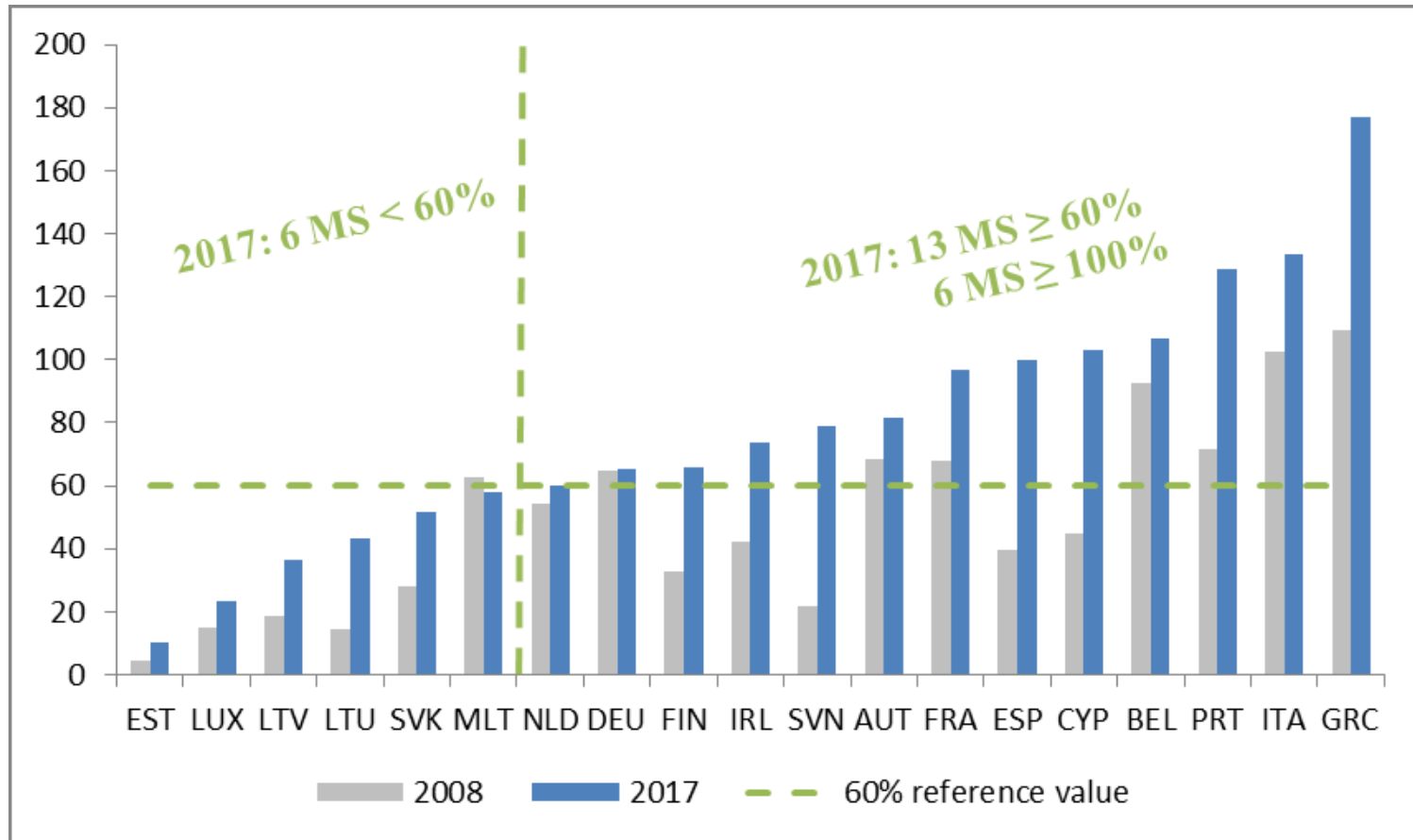


Sources: IMF historical public debt database, Angus Maddison Project, BMF staff calculations, COM Winter Forecast 2017. Note: Euro area covers a subset of 8 MS until 2011 (Austria, Belgium, France, Germany, Italy, Netherlands, Portugal, Spain).

■ ■ ■ ■ ■ ■ ■  
Bundesministerium der Finanzen  
■ ■ ■ ■ ■ ■ ■  
Berlin

# EMU has a debt problem

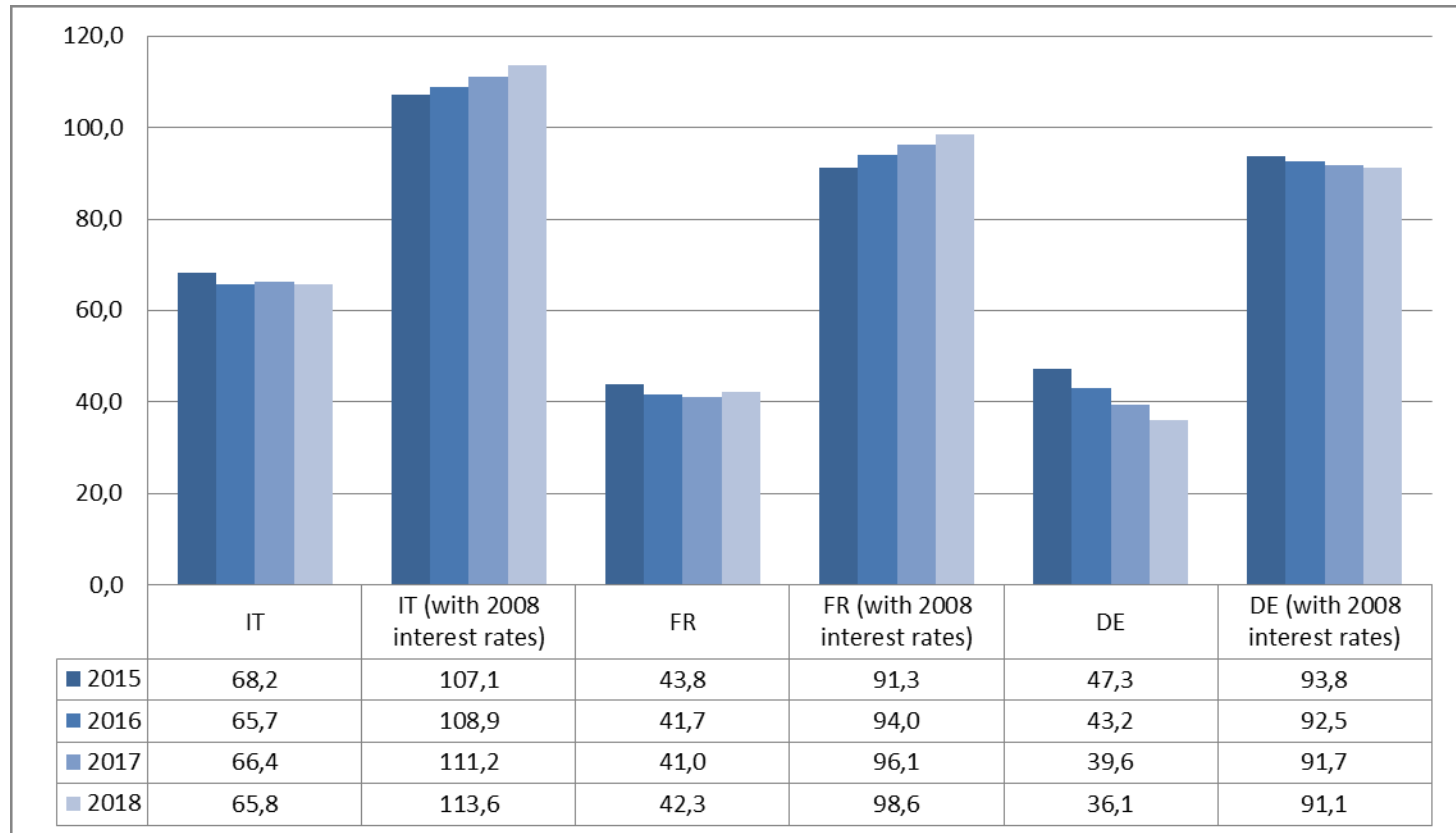
Government debt 2008 vs. 2017 in % of GDP





# Significant windfall profits

## General government interest payments in bn. Euro



Source: COM Winter Forecast 2017, BMF staff calculations. IT, FR, DE: MS with highest nominal debt in 2016, 2008 reference period with highest implicit interest rates in the last 10 years.

## Four points:

1. Many forms of crisis – one word to describe them all: loss of confidence
2. EMU: from success to crisis
3. Solutions at the aggregate level?
- 4. A policy proposal**
  - Sound analysis allows successful policies**

# The wrong way!

underperform

oversell



# Silo policy



# Economic policy

restart convergence!  
growth, jobs

## Integrated reform policy

Economic  
policy  
coordination

CSR to identify  
main challenges

**Action:**  
EU-semester  
as central  
instrument for  
coordination



Cohesion  
policy

CSRs define  
funded  
projects

**Action:**  
MS present  
projects to  
implement  
CSRs



EU-  
budget

EU-  
budget  
supports  
national  
reforms

EU-  
budget  
finances  
EU-  
policies

EU-  
budget  
finances  
European  
public  
goods

# Fiscal policy

Objective: Room  
for manoeuvre;  
Stability

**Action:**  
respect MTOs

Debt rule respected;  
Debt ratios decline  
towards 60%

Lower interest payments

- Independence from market volatility
- Allows lower taxes/improved public services

Structural balanced  
budget creates room  
to react in crises.  
Automatic  
stabilisers can  
work.

Bundesministerium der Finanzen



Berlin

Financial  
market  
policy

Objective:  
stable financing  
of the economy

Reduce risk in the sector

**Action:**  
Harmonise  
legal  
framework

**Action:**  
Reduce  
sovereign  
exposure

# Thank you for your attention

**Thomas Westphal**  
**Director General European Policy**  
**German Federal Ministry of Finance**