
How to get the EU out of its worst recession ever?

Presentation by Director General Marco Buti
European Commission, Economic and Financial Affairs

Centre for European Reforms breakfast seminar
Brussels, 13 May 2009



EU outlook in a nutshell

- EU economy fell into recession, as financial crisis intensified and world trade contracted sharply
- Financial markets are showing signs of gradual stabilisation, but remain fragile
- Ambitious EU and government action key to achieving stabilisation towards end 2009 and moderate growth in 2010
- Leading indicators provide some positive signals



Global economy in recession

	2007	2008		2009		2010	
(percentage change on preceding year)		Spring	Jan-09	Spring	Jan-09	Spring	Jan-09
World GDP growth	5.1	3.1	3.3	-1.4	½	1.9	2¾
<i>GDP growth in:</i>							
- the US	2.0	1.1	1.2	-2.9	-1.6	0.9	1.7
- Japan	2.4	-0.7	-0.1	-5.3	-2.4	0.1	-0.2
- China	13.0	9.0	9.7	6.1	6¾	7.8	8
- EU	2.9	0.9	1.0	-4.0	-1.8	-0.1	0.5



The EU forecast – an overview

(Real annual % change unless otherwise stated)	euro area			EU27		
	2008	2009	2010	2008	2009	2010
GDP	0.8	-4.0	-0.1	0.9	-4.0	-0.1
Consumption	0.5	-0.9	-0.3	0.9	-1.5	-0.4
Total investment	0.0	-10.4	-2.7	0.1	-10.5	-2.9
Employment	0.7	-2.6	-1.5	0.7	-2.6	-1.4
Unemployment rate *	7.5	9.9	11.5	7.0	9.4	10.9
Inflation	3.3	0.4	1.2	3.7	0.9	1.3
Gov't balance (% GDP)	-1.9	-5.3	-6.5	-2.3	-6.0	-7.3
Gov't debt (% GDP)	69.3	77.7	83.8	61.5	72.6	79.4
Current account bal. (% GDP)	-0.7	-1.2	-1.3	-1.5	-1.9	-2.0

* % of the labour force



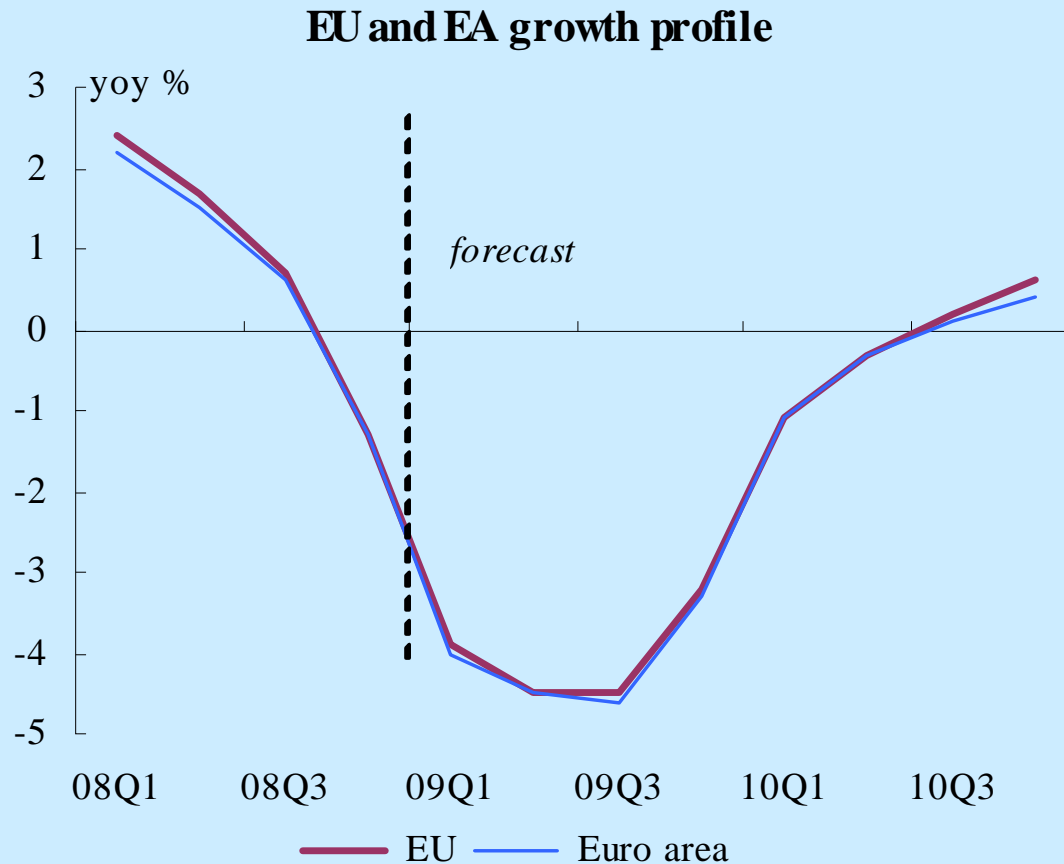
German recession worse than French in 2009

- German economy is more open: Exports per GDP 49% in Germany vs. 27% in France (2007), Share of manufacturing sector 24% in Germany and 13% in France
- Germany is specialised in investment goods production, and expensive cars in automobile sector
- France has larger public sector, stabilising household income: Compensation of employees paid by the public sector + social transfers 56% of gross disposable income of households in France, compared to 43% in Germany.



Modest recovery starting in 2010 in the EU

(year-on-year real GDP growth, %)



Considerable uncertainties

	Downside risks	Upside risks
External	<p>Negative feedback loop from deteriorating real economy to financial sector</p> <p>Protectionism</p> <p>Disruptive exchange-rate developments</p>	<p>Stronger impact on confidence of recovery packages</p> <p>Faster adjustment in global inventory cycle, US housing sector, recovery in Emerging Markets (incl. China)</p> <p>Commodity prices weakening further</p>
Domestic	<p>Negative feedback loop from deteriorating real economy to financial sector</p> <p>External/domestic vulnerabilities in some MS exacerbated by current crisis</p>	<p>Stronger impact on confidence of recovery packages</p> <p>More favourable consumer response to lower inflation</p>



Implications of the financial crisis

- Key priori in the short term is to get credit flowing again
- Protracted slowdown, a fall in growth potential
 - Potential for innovations weakened by more conservative financial system after the crisis, and by possible pro-incumbent industrial policies
 - Effects on the labour market will linger
- Fall in growth potential hinders intra euro area adjustment
- Reduced capital flows to slow convergence in RAMSs



Europe's first response to the crisis

- Around 5% of EU GDP of overall support over 2009-10: national Recovery plans (1.8%) plus automatic stabilisers (2.7%) plus extra budgetary measures (0.5%)
- ECB key rate cut by 3.25 percentage points since October to 1%
- Bank rescue plans in 19 countries (around €300 bn in recapitalisation operations and €3 tln in bank guarantees)



Way forward: Financial system

- Restoring the flow of credit needed for economic recovery
- Important measures undertaken and announced, must be implemented effectively
- The problem of impaired assets to be dealt with in a coordinated way and taking into account budgetary implications
- Reform needed in regulation and supervision
- Actions at the global level



Way forward: Support real economy

- Need to implement rapidly the planned stimulus measures, which should provide immediate boost while also strengthening the economy in the long run
- Long-term credibility of public finances crucial also with regard to the immediate effects of budgetary support
- Protectionism and retreat to national markets must be avoided
- Structural reforms to remain high on the policy agenda



Way forward: Support people and employment

- Most Member States have introduced employment and social measures
- The employment and social impact of the crisis is likely to be more severe than expected earlier
- Thus, efforts need to be stepped up
- Measures should remain consistent with long-term reform and restructuring needs
- Carefully designed policies support strong recovery



Credible exit strategies

- Financial system: Commitments to restructure and consolidate the banking sector should be adopted now
- ECB determined to unwind expansion when needed
- Fiscal policies: Spell out conditions for stimulus withdrawal and adopt credibility-enhancing moves, such as early reform of entitlements and stronger national fiscal frameworks
- Structural policies: Withdrawal of temporary measures supporting particular sectors; Promote labour supply; Intensify structural reform prioritizing measures with low budgetary costs; Transition to low-carbon economy



Thank you