

Constraints for EU 2020 in the aftermath of the Crisis

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Jean Monnet Conference

***The Role of Education and Training in the New
European Economy***

Madrid, 25-26 January 2010

Agenda (1)

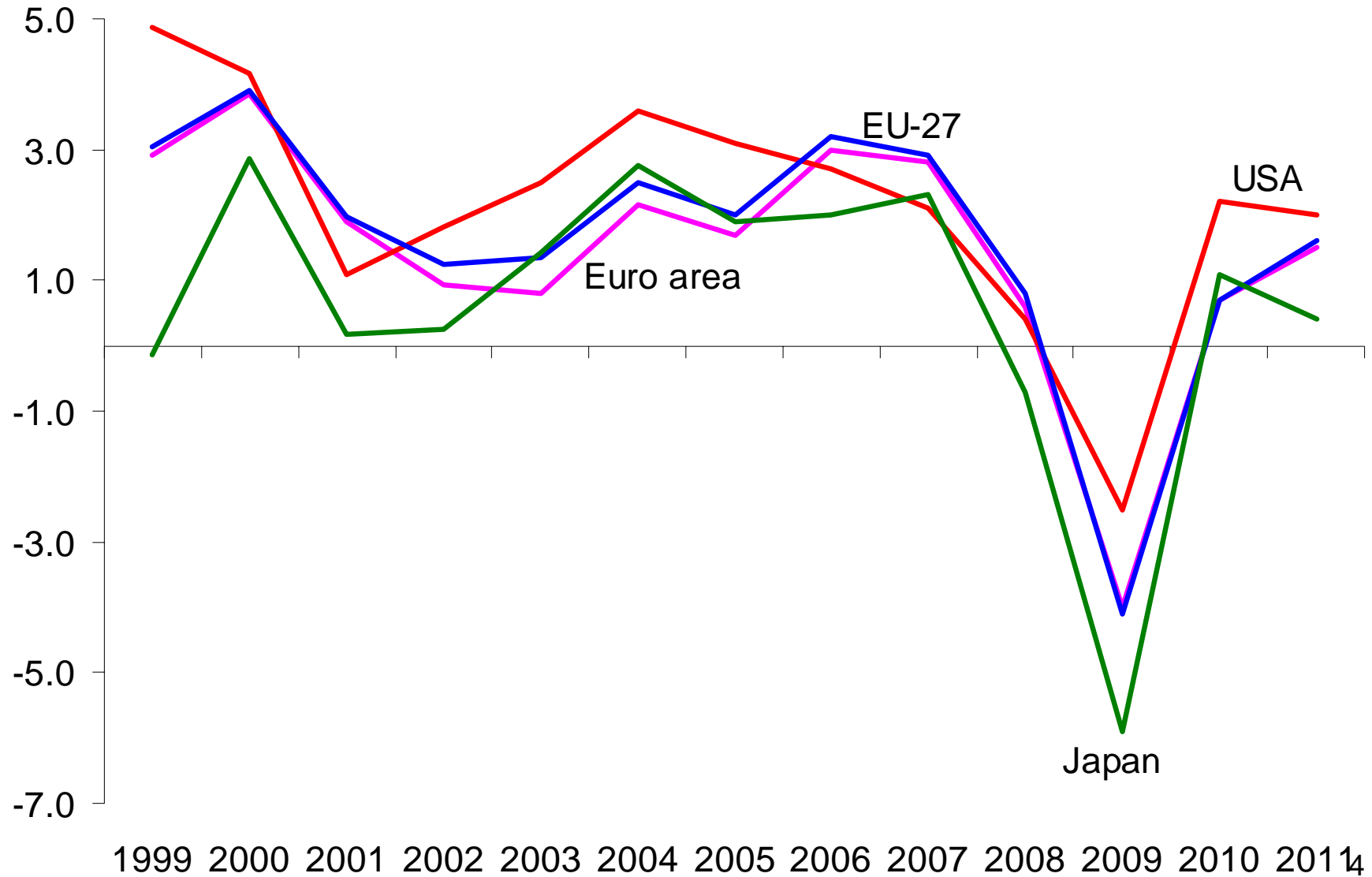
- The **Great Recession** vs The **Great Depression** – lessons learned: monetary + fiscal policy
- **Challenges** ahead – short- and long-term
 - short-term: **exit strategy** – back to recovery (how to overcome the “jobless” recovery?)
 - **Schumpeterian strategy** to overcome the recession: “creative destruction”, i.e. new products, innovation!
 - * legacy of the GFC: **unemployment, debt**
 - long-term: how to bring back potential growth to pre-crisis levels? -----> **“knowledge triangle”** (education-research-innovation)

Agenda (2)

- **EU 2020** strategy – Spring European Council early in 2010
 - **knowledge triangle** (education-research-innovation)
 - comparison “Lisbon” and “EU 2020” – “What’s new?”
- **Alternative** suggestions for an EU strategy for the future post 2010

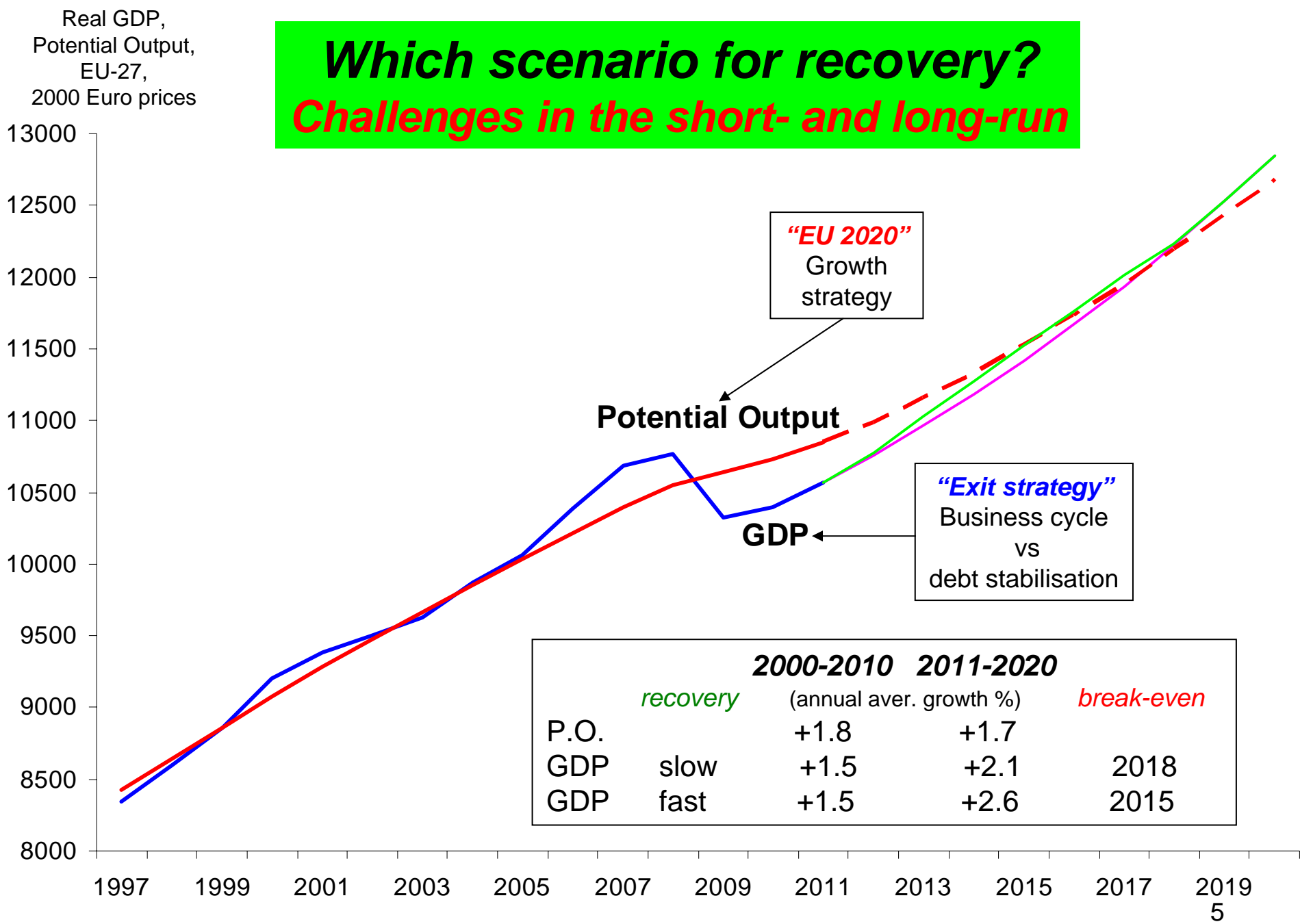
Who grows faster after the Great Recession 2009?

(Real GDP, annual growth rate in %)



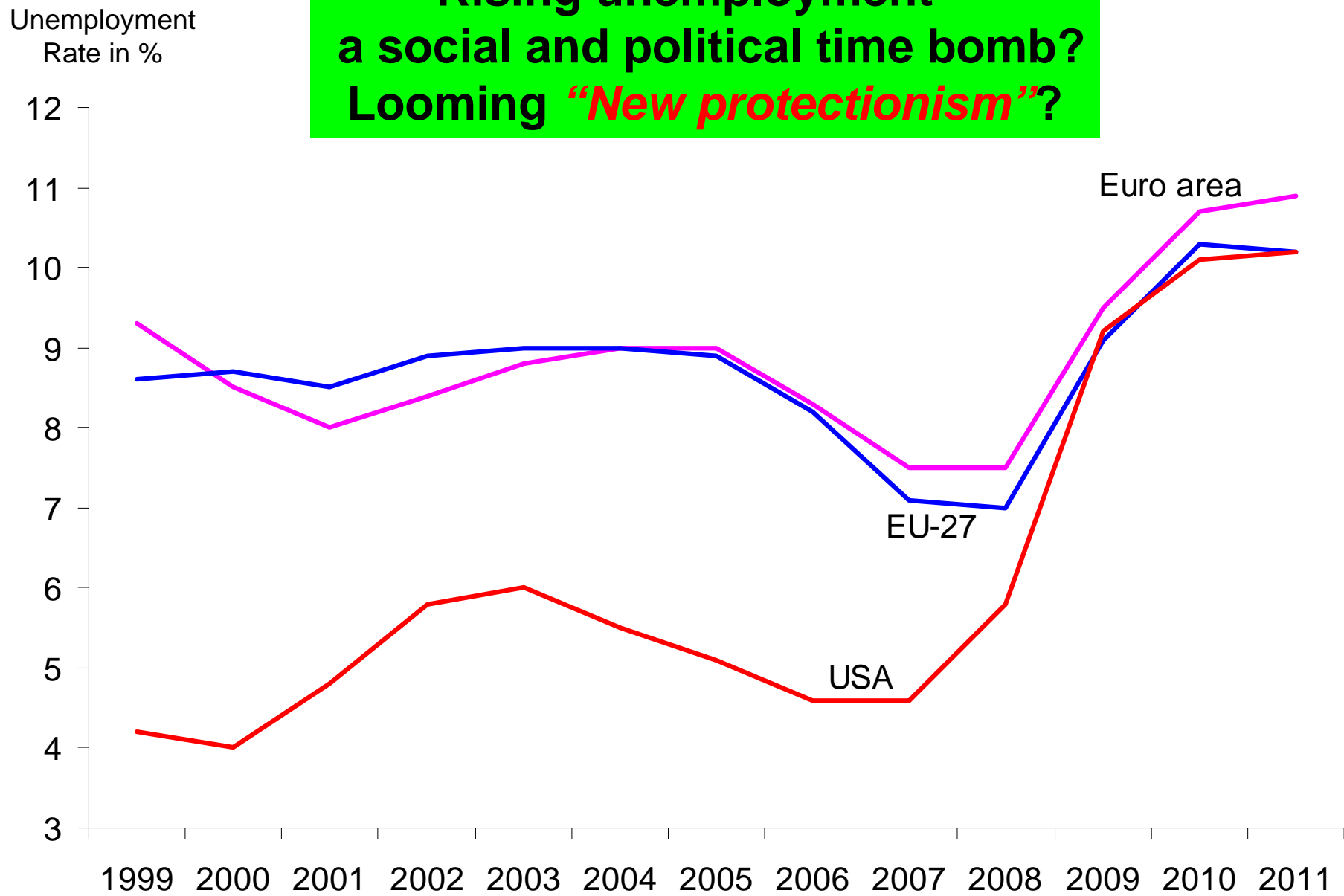
Source: EU Autumn 2009 forecast

Which scenario for recovery? Challenges in the short- and long-run



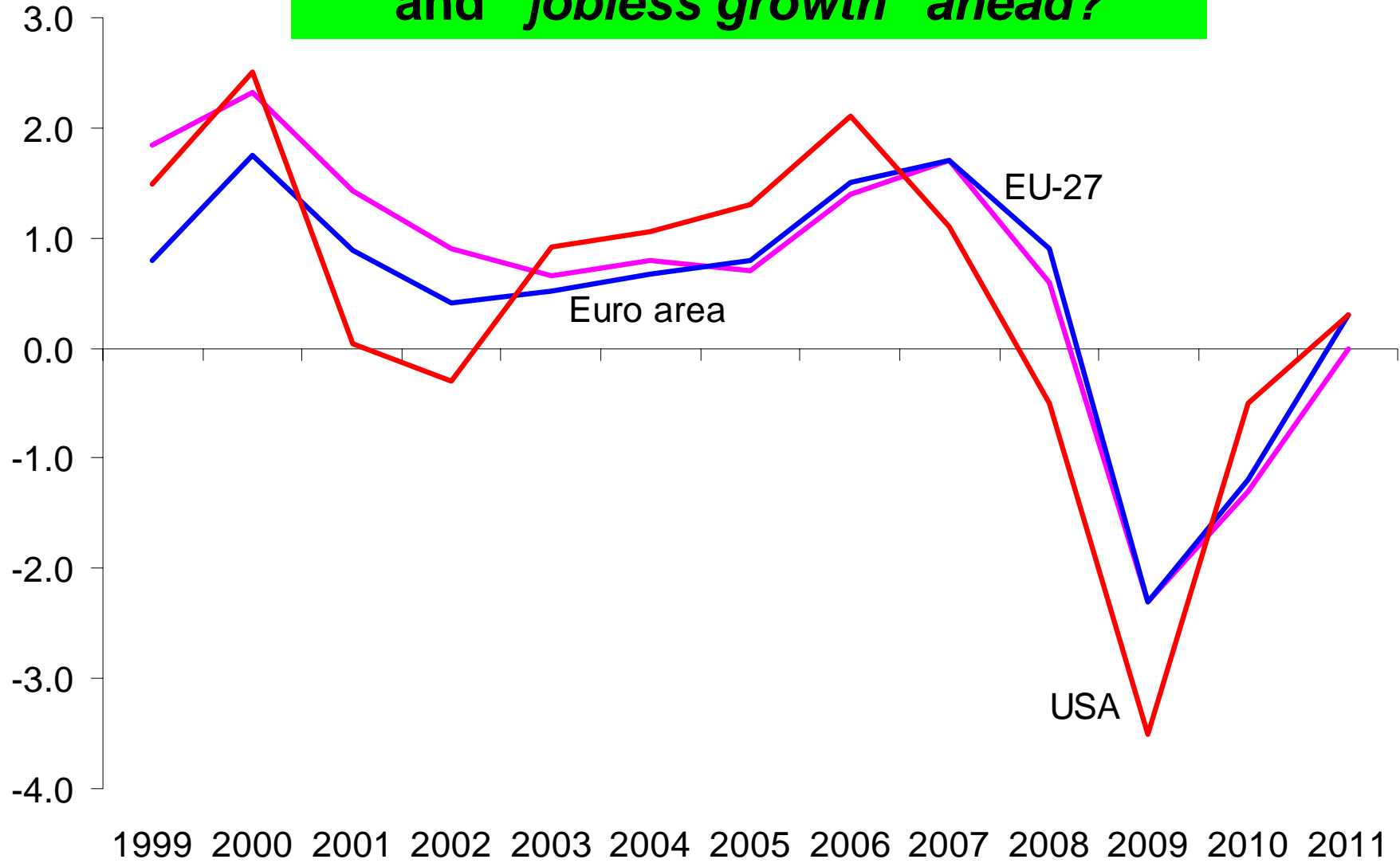
Source: EU Autumn 2009 forecast; own scenarios 2011-2020

**Rising unemployment –
a social and political time bomb?
Looming *“New protectionism”*?**

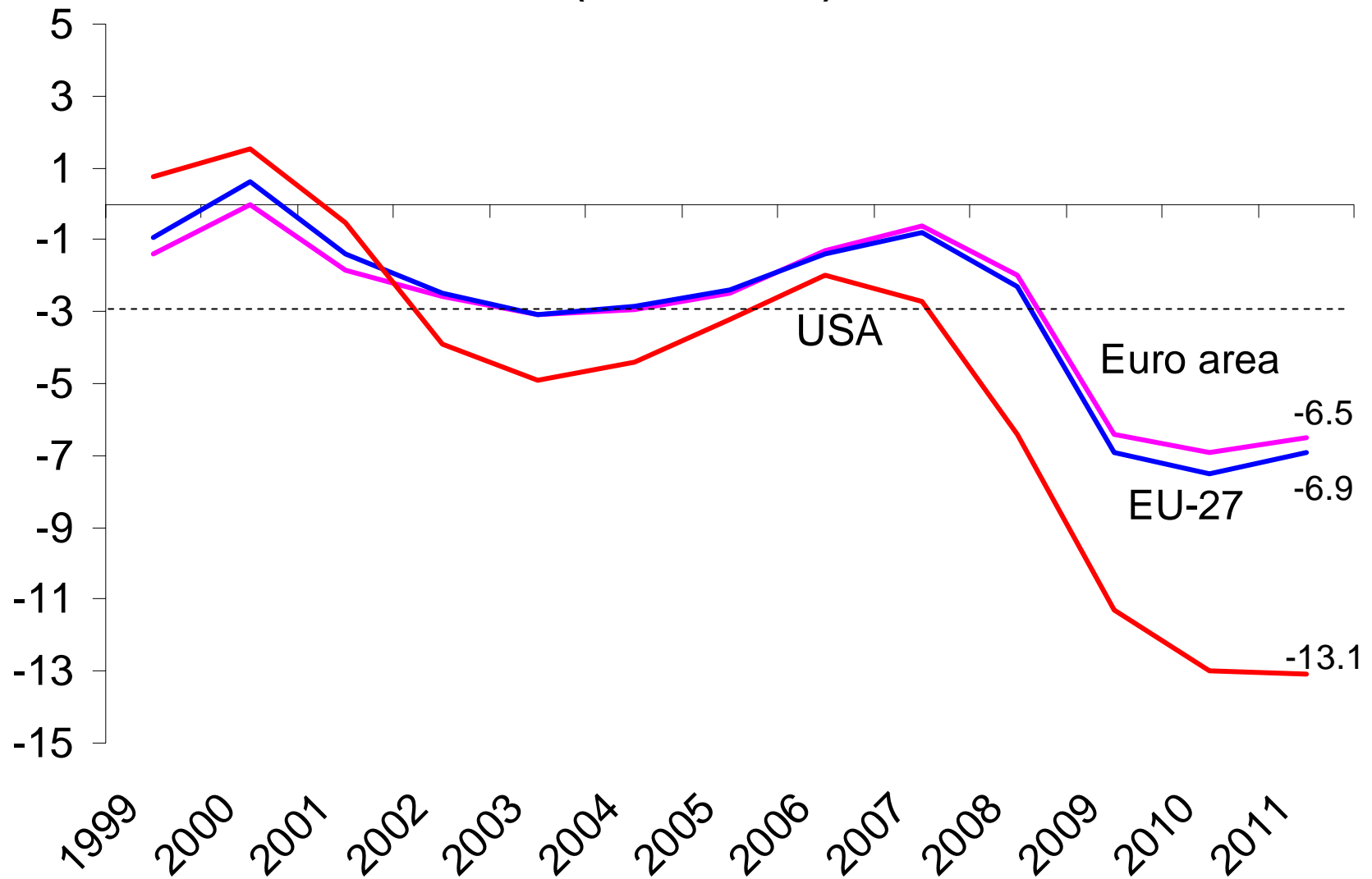


Total
employment,
annual growth
rate in %

Employment growth – a deep recess and “jobless growth” ahead?

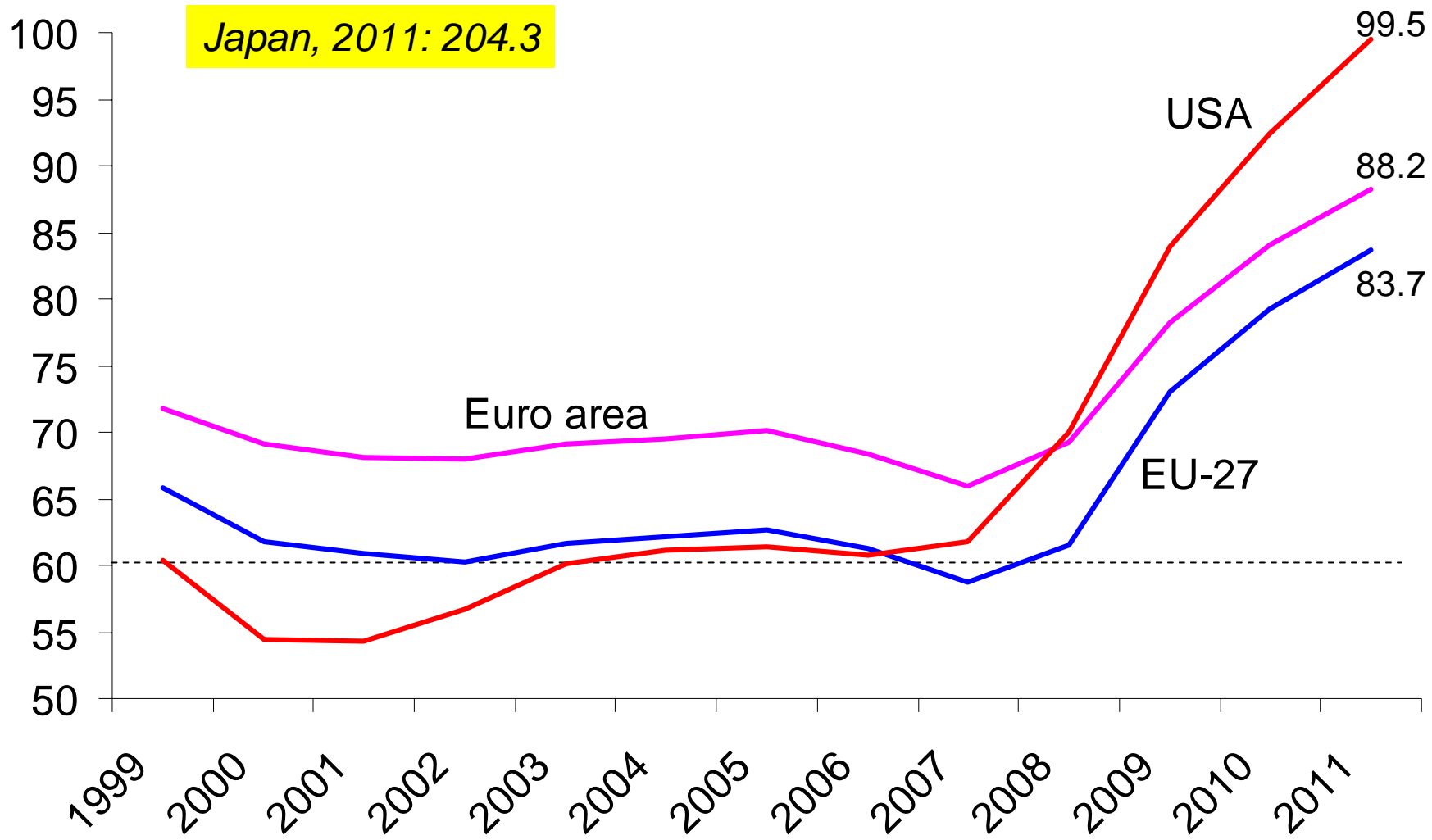


General government balance (as a % of GDP)



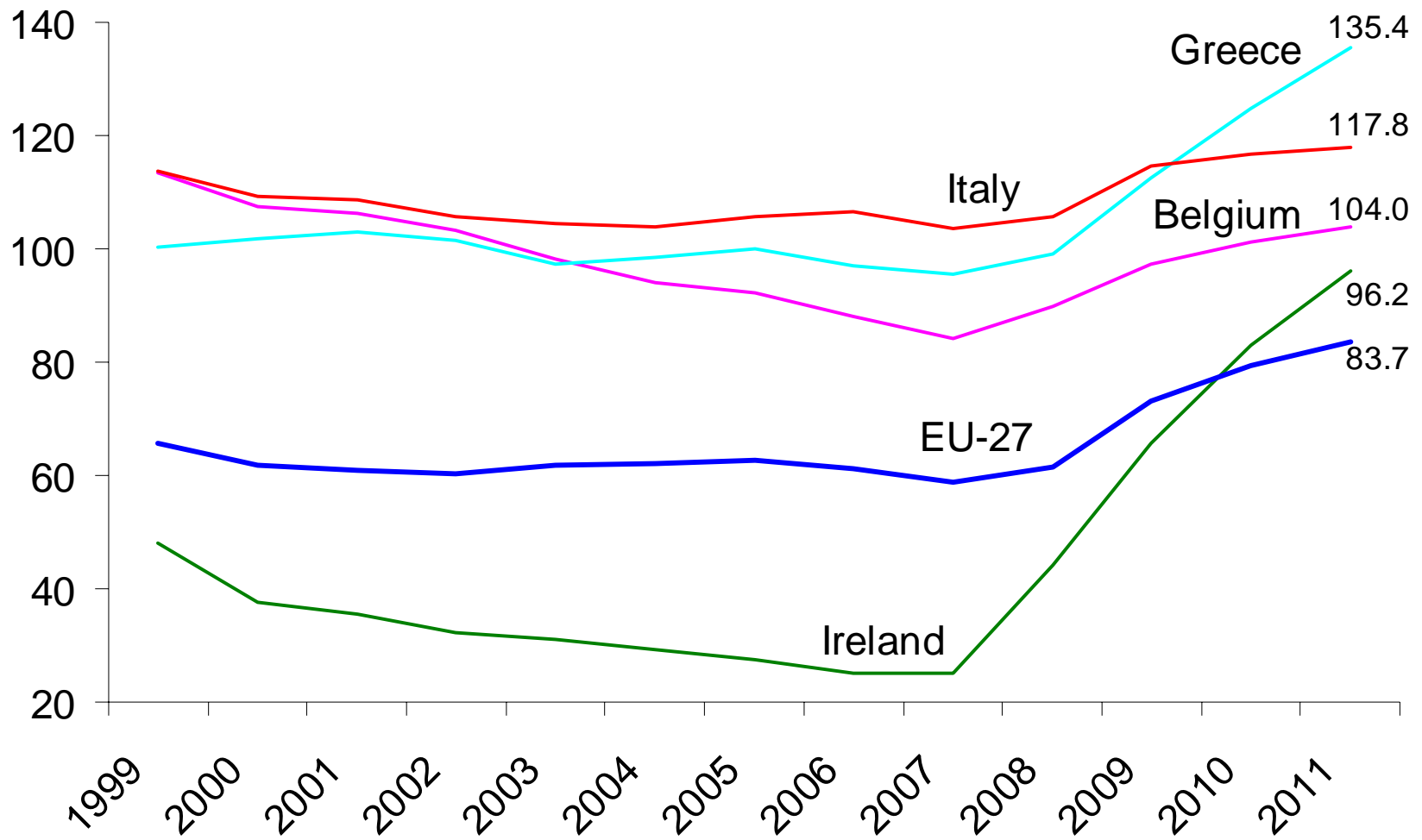
Source: Euro area; EU-27, USA = EU Autumn 2009 forecast

General government gross debt (as a % of GDP)



Sources: Euro area; EU-27 = EU Autumn 2009 forecast; USA = OECD Economic Outlook, Nov 2009

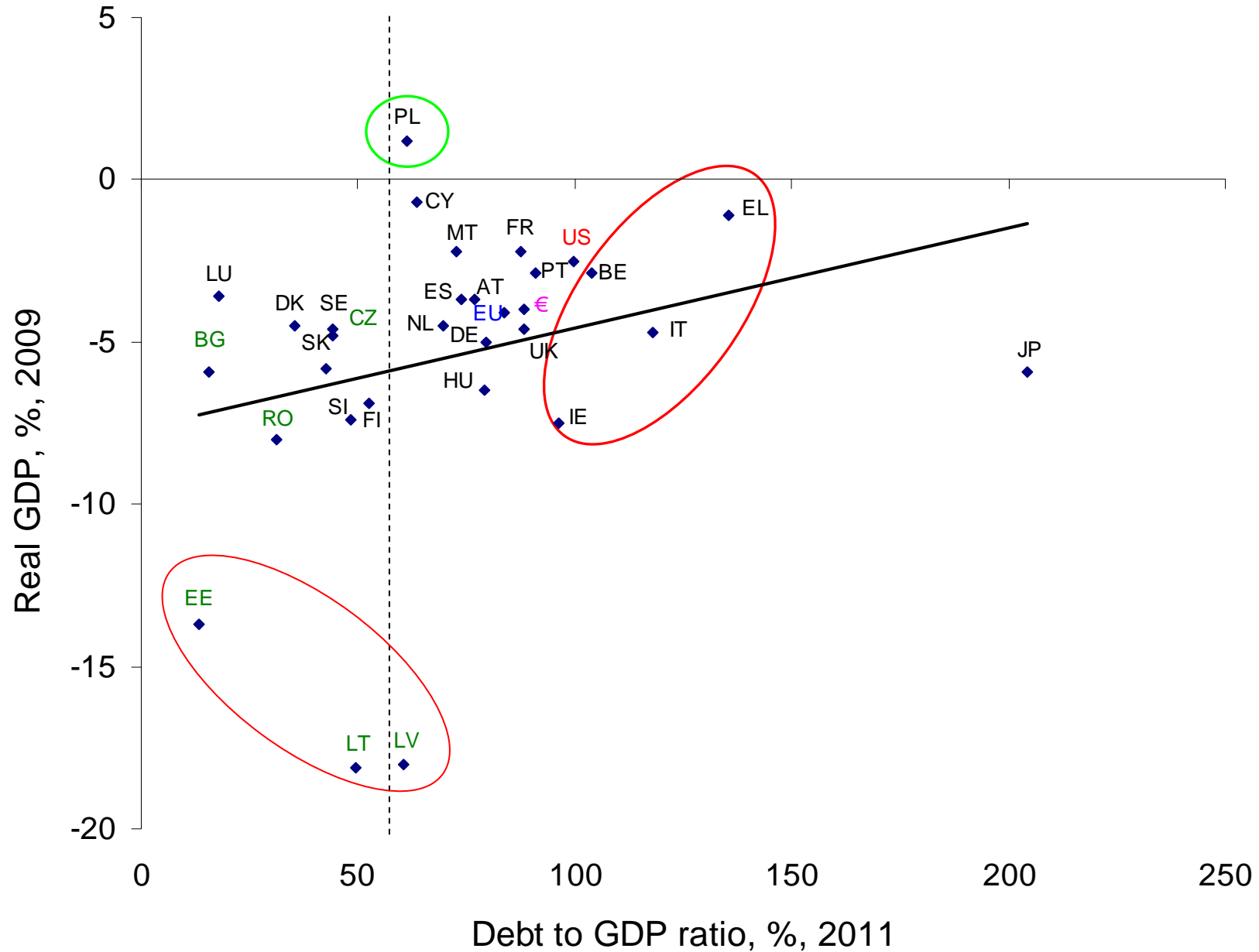
General government gross debt – critical countries (as a % of GDP)



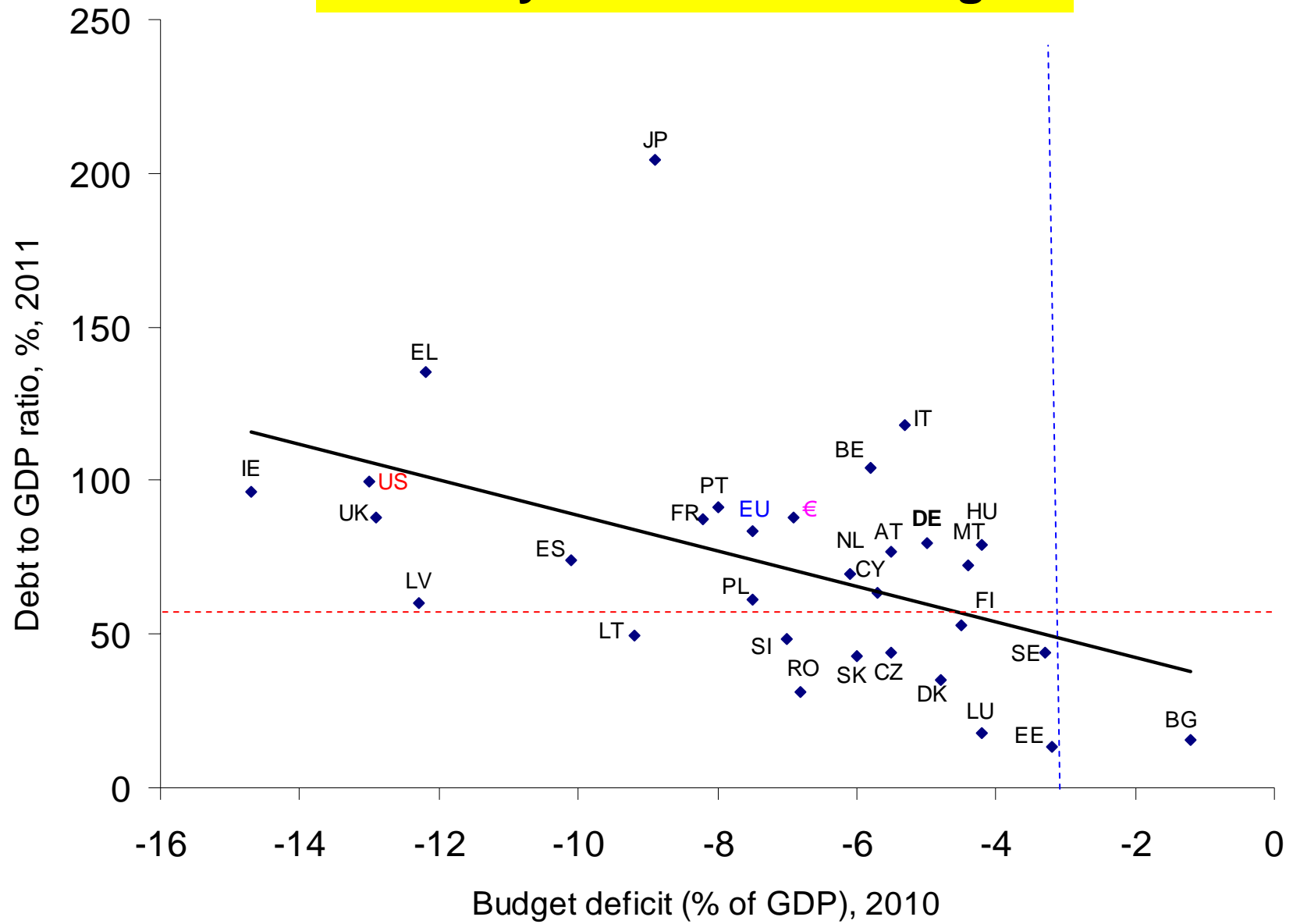
Critical debt dynamic (2007-2011):
 LV + 51%, UK +44%, ES +38%, LT +32%

Source: EU Autumn 2009 forecast

The Great Recession and the Burden of Debt



Far away from the SGP targets



Crisis management 2009 was O.K.

- Quick response of with ***monetary policy*** (Fed, ECB and other national banks)
- Coordinated (within EMU) and national massive ***fiscal policy*** intervention ---->
governments overtook the role of the ***“lender of last resort”*** for the big banks (“too big to fail”!) and for the whole economy ----> rescue packages!
- “Quality” of rescue measures more short-term oriented, less forward-looking

Two World crises Comparison (real GDP)

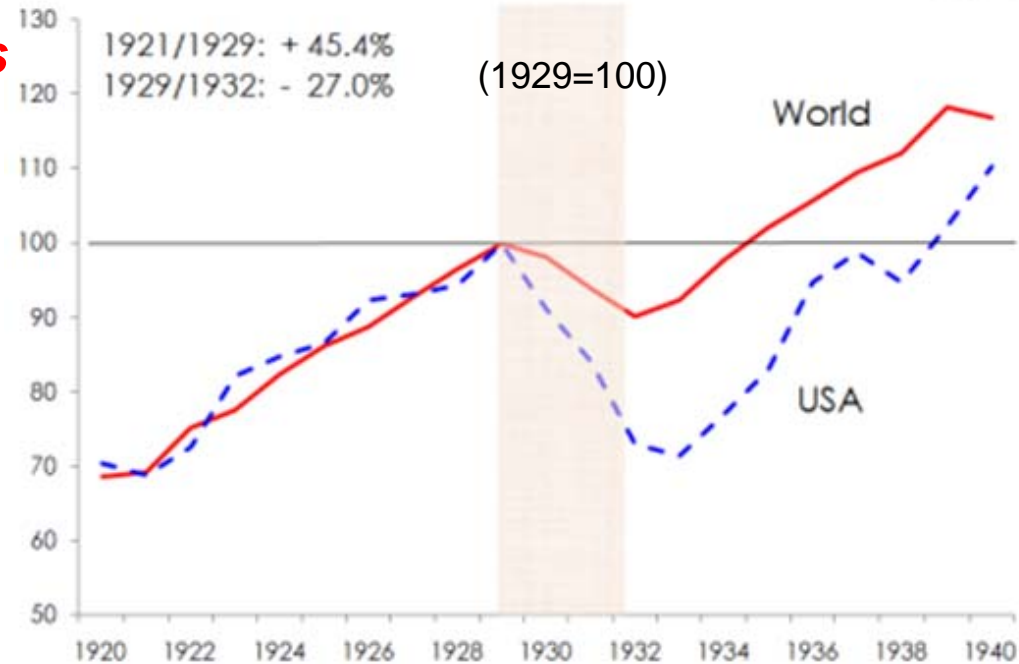
GDP decline

1929/1932

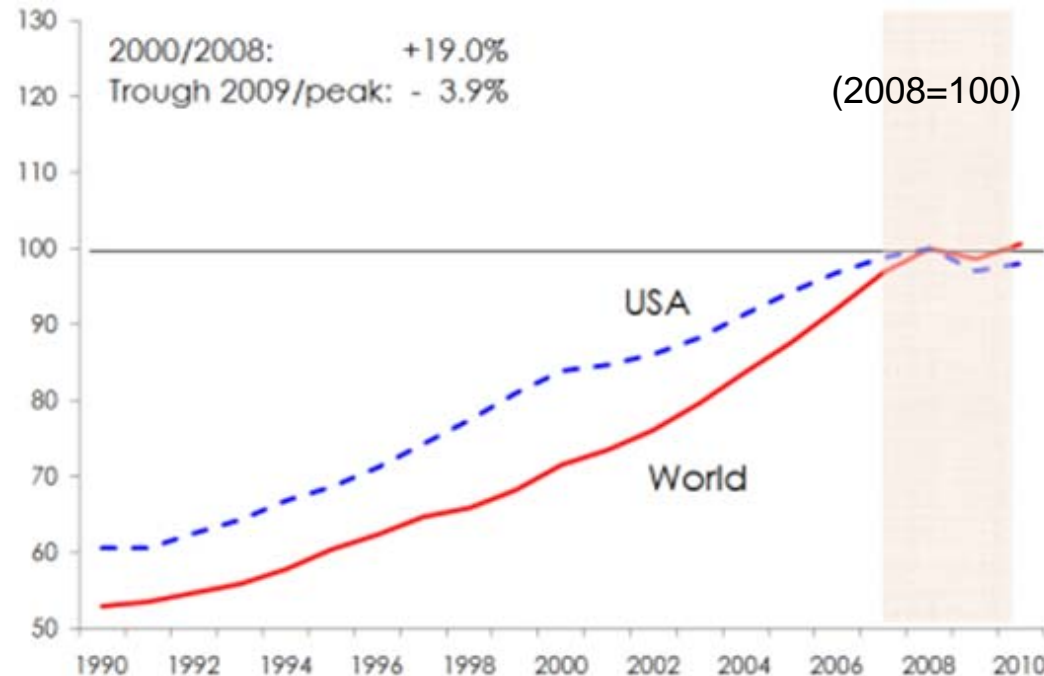
USA -27%
Germany -16%
World -10%

2008/2009

USA -2.5%
Germany -5.0%
EU -4.0%
World -1.0%



The Great
Depression
1929



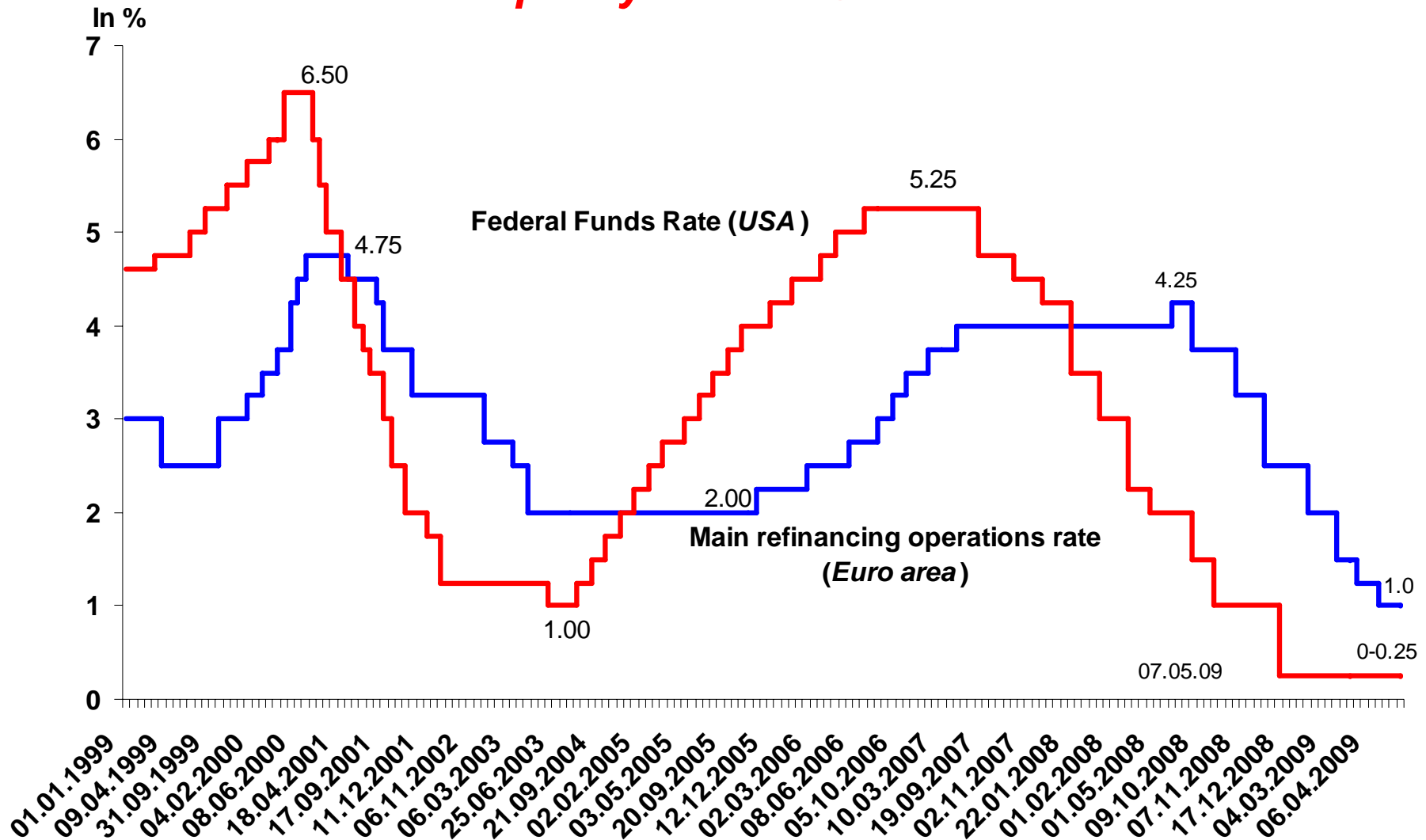
The Great
Recession
2009

Source:

K. Aiginger: The Great Recession
vs. the Great Depression: Siblings
which got different foster parents?
WIFO, Vienna, Nov. 2009

Monetary Policy learned the Lessons from the Great Depression

Interest rate policy of the ECB and the FED



Fiscal stimulus programmes in industrial countries

	Net impact on general government balance			Distribution 2008-2010		
	Expenditure	Taxes	Total	2008	2009	2010
	2008-2010			Percentage share of net impact		
	As a percentage of GDP of 2008					
Germany	- 1.4	- 1.6	- 3.0	0	46	54
Italy	- 0.3	0.3	0.0	0	15	85
USA	- 2.4	- 3.2	- 5.6	21	37	42
Switzerland	- 0.3	- 0.2	- 0.5	0	68	32
France	- 0.4	- 0.2	- 0.6	0	75	25
Czech Republic	- 0.5	- 2.5	- 3.0	0	66	34
UK	0.0	- 1.5	- 1.4	15	93	8
Hungary	4.4	0.0	4.4	0	58	42
Spain	- 1.9	- 1.6	- 3.5	31	46	23
Poland	- 0.6	- 0.4	- 1.0	0	77	23
Austria	- 0.3	- 0.8	- 1.1	0	84	16
OECD 11						
Unweighted	- 0.3	- 1.1	- 1.4	6	61	33
Only positive impact						
Unweighted	- 0.9	- 1.3	- 2.2	7	66	29
G 7	- 1.6	- 2.0	- 3.6	17	43	40
OECD total						
Unweighted	- 0.7	- 1.2	- 2.0	10	53	37
Weighted	- 1.5	- 1.9	- 3.4	17	45	39

Source: Breuss, Kaniovski, Schratzenstaller (2009), p. 207

Fiscal stimulus programmes – GDP impact

	Gross domestic product, volume		
	2008	2009	2010
Cumulated deviation from baseline in percent			
Germany	+ 0.1	+ 0.9	+ 1.0
Italy	± 0.0	± 0.0	- 0.3
USA	+ 0.6	+ 2.3	+ 3.6
Switzerland	+ 0.1	+ 0.5	+ 0.1
France	± 0.0	+ 0.2	- 0.2
Czech Republic	± 0.0	+ 0.8	+ 0.6
UK	+ 0.1	+ 0.4	- 0.4
Hungary	± 0.0	- 0.5	- 1.0
Spain	+ 0.8	+ 1.2	+ 0.5
Poland	± 0.0	+ 0.7	+ 0.3
Austria	-	+ 1.9	+ 2.1
Japan	± 0.0	+ 0.8	+ 0.1
Other countries	+ 0.2	+ 1.0	+ 1.2

Forward-looking investment in the fiscal stimulus programmes of selected countries, 2009-2010

	Infra- structure	Science, research and development, innovation	Education	"Green" technologies	Forward- looking investment <i>total</i>	Rest of fiscal stimulus
	Percent of overall size of stimulus programmes					
<i>11 OECD countries</i>	17	4	12	6	38	62
Australia	18	5	30	10	64	36
Canada	31	1	3	4	40	60
Finland	15	0	1	1	17	83
France	34	0	6	0	40	60
Germany	16	3	19	6	45	55
Norway	20	1	1	8	30	70
Sweden	8	9	0	2	19	81
Poland	7	1	–	0	9	91
Portugal	4	16	51	20	91	9
USA	13	2	10	7	32	68
Austria	22	1	1	5	29	71

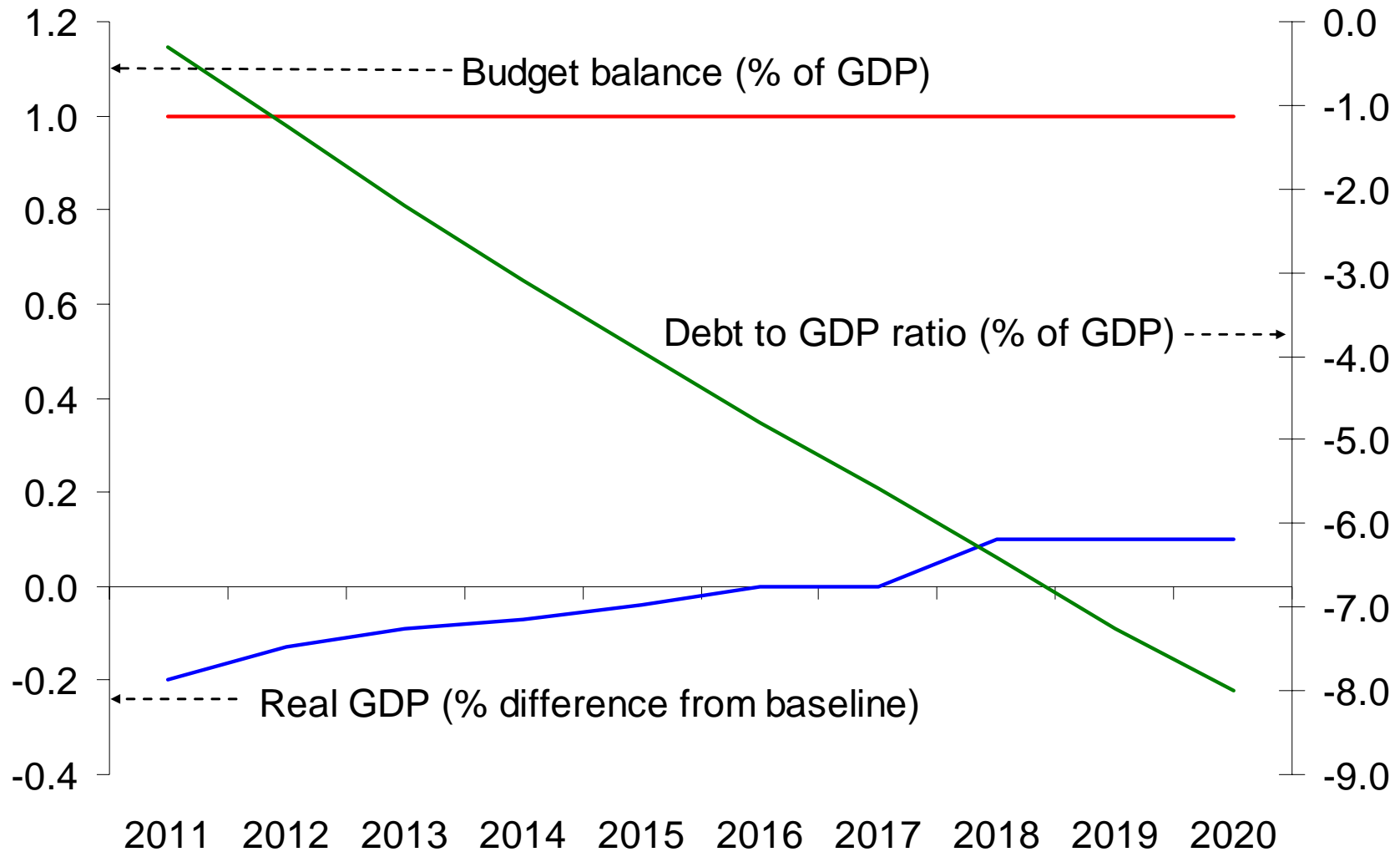
Source: Breuss, Kaniovski, Schratzenstaller (2009), p. 214

Perils of the Exit Strategy

- **Monetary Policy:** as soon as inflation winds up – more restrictionist stance – increase of interest rates; dampening real GDP
- **Fiscal Policy:** “Tightrope walk” between stabilising the upswing and foster recovery (not deteriorate the labour market situation; avoid “jobless growth”) and the necessity to obey the rules of the **SGP**, i.e. consolidate the budgets and reduce public debt
- **Consequences:** Both strategies lead to a short-run slump in GDP.

In the long-run to a **financial constraint** for growth strategy measures aimed at in the “**EU 2020**” – a revival of the failed “Lisbon strategy”

The macroeconomic costs of the Exit Strategy in the Euro area
(Reduction of the budget deficit by 1% of GDP, starting in 2011)

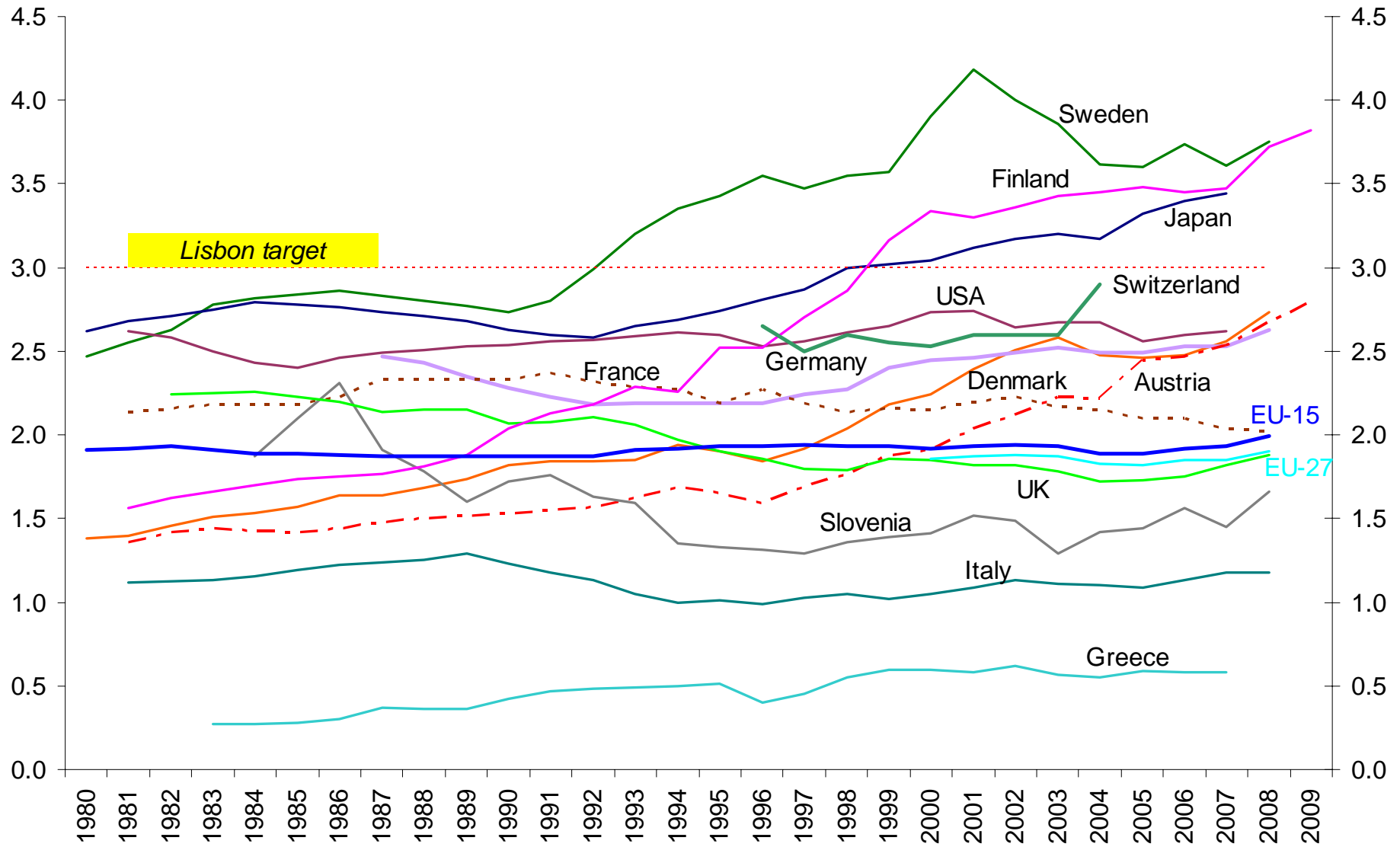


Knowledge triangle – education- research-innovation

- *Facts* on R&D, education, innovation
- *Correlations* “knowledge triangle”
 - which causation?
- Induces *more R&D more GDP growth?*
 - theoretical considerations
 - empirics

Research & Development – R&D

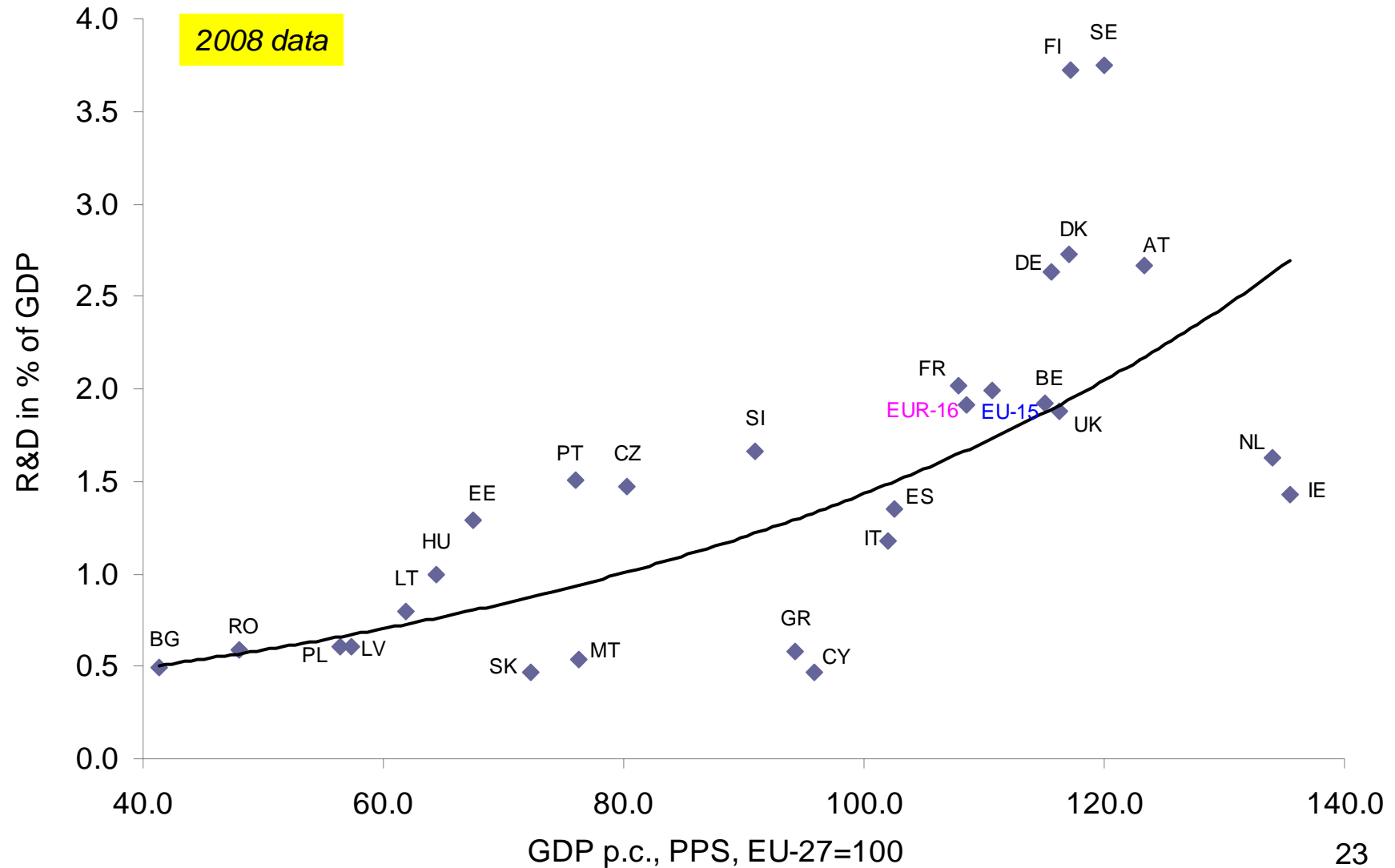
(Gross domestic expenditure on R&D in % of GDP)



Source: Eurostat

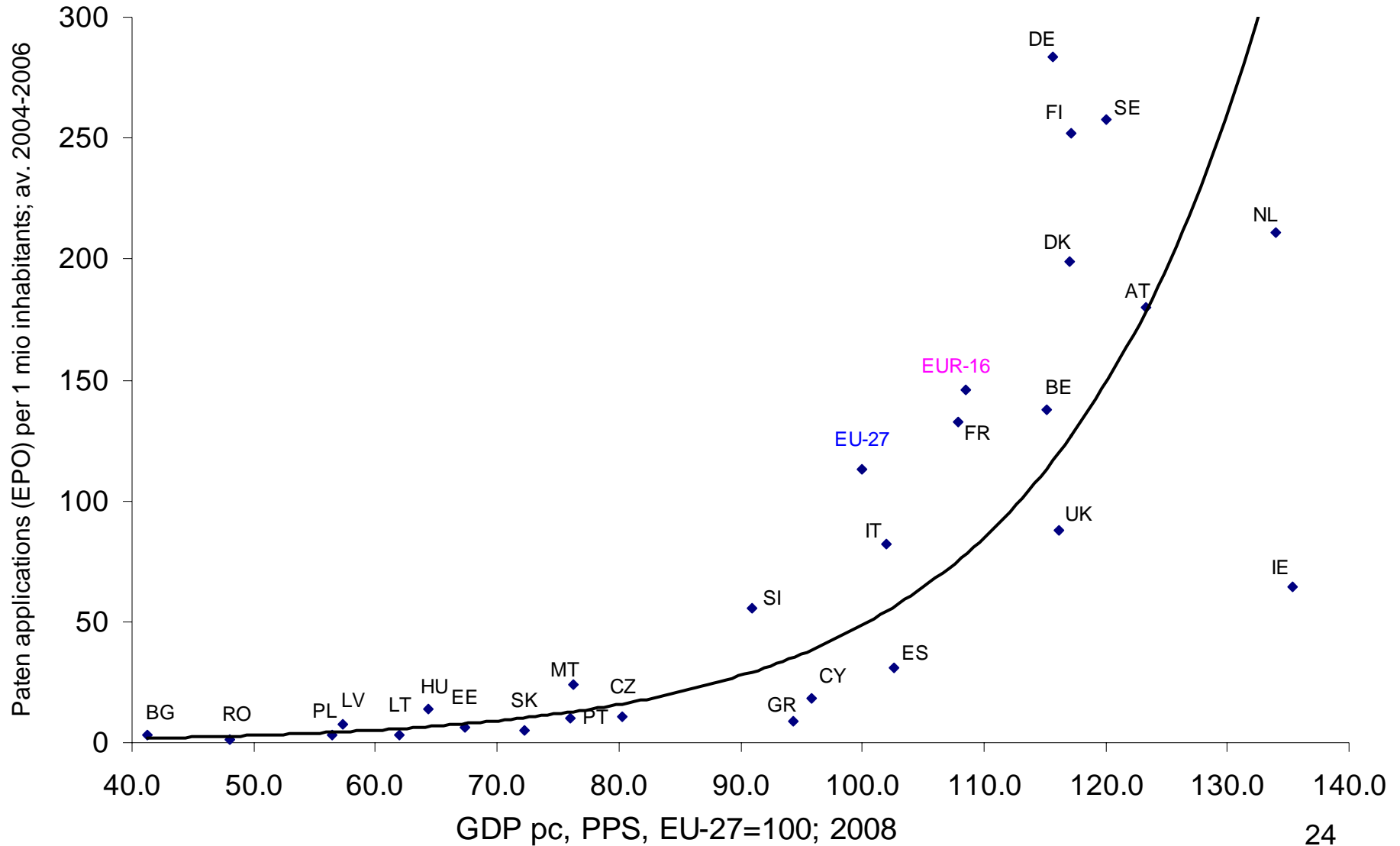
Richer countries can afford more R&D ...

(Or are they rich because of more R&D investment?)



Source: Eurostat

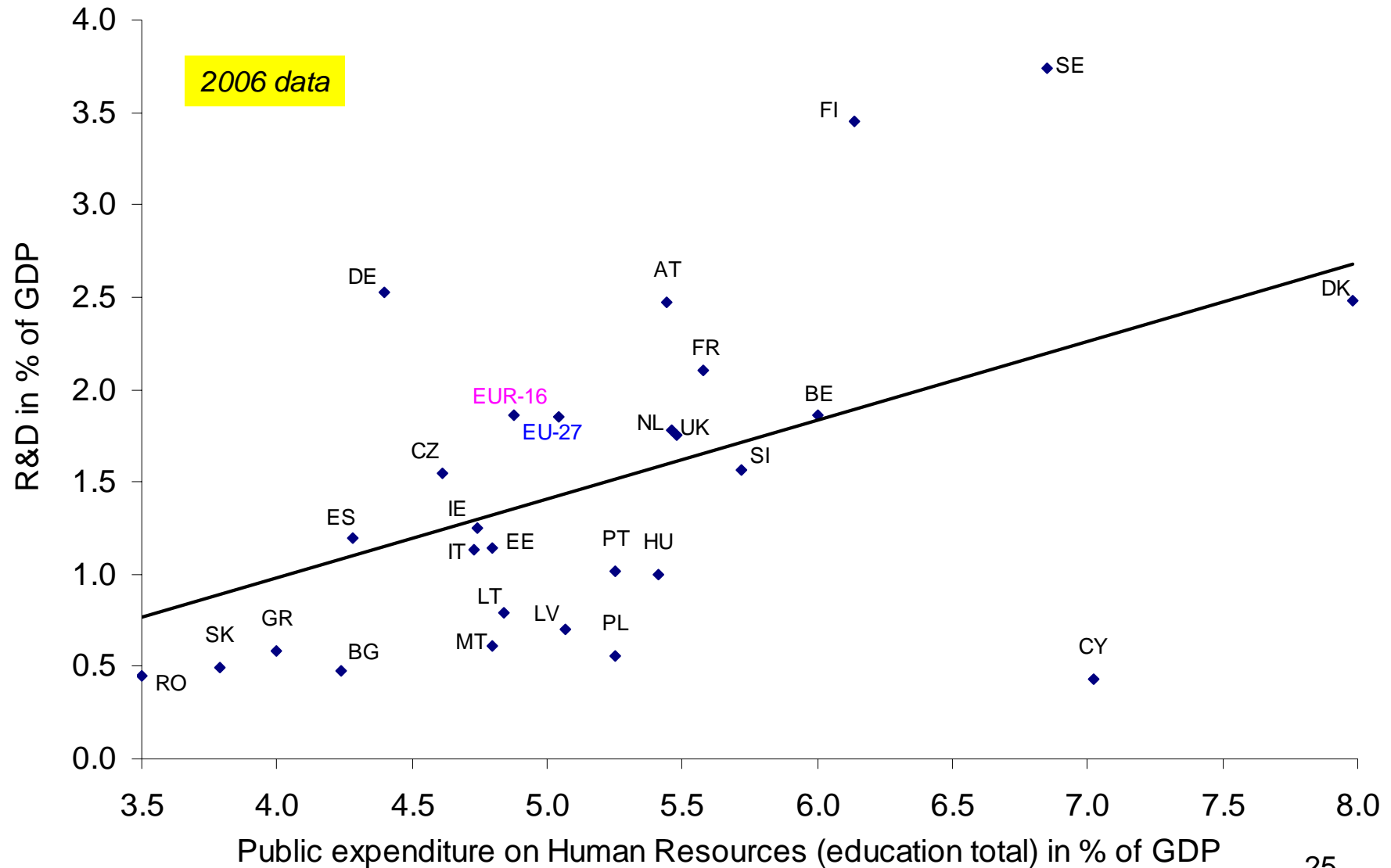
... and are more innovative!
(more research – more patents)



Source: Eurostat

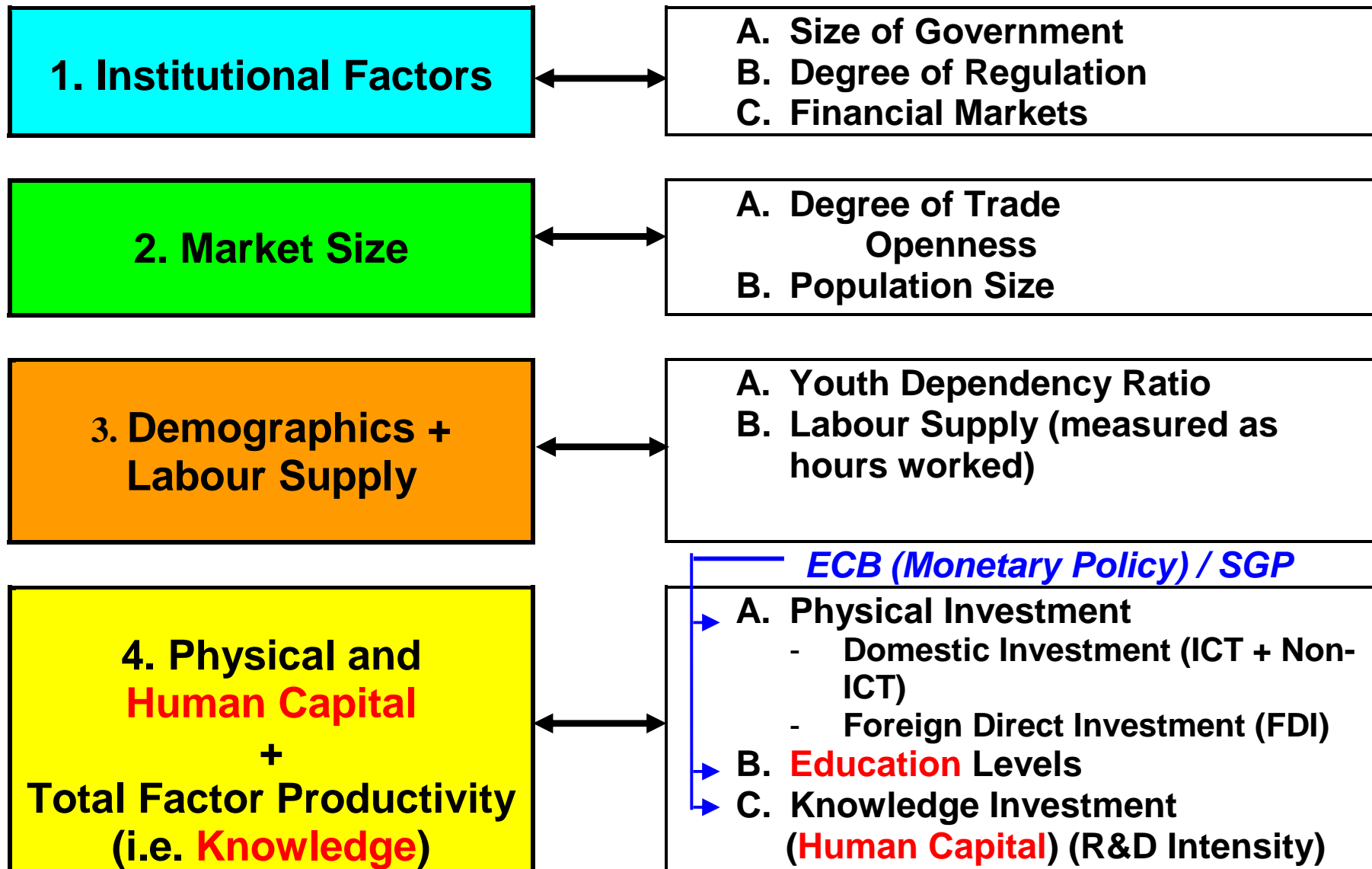
More education – more Research!

(One facet of the Knowledge Triangle)



Source: Eurostat

Basic Growth Determinants



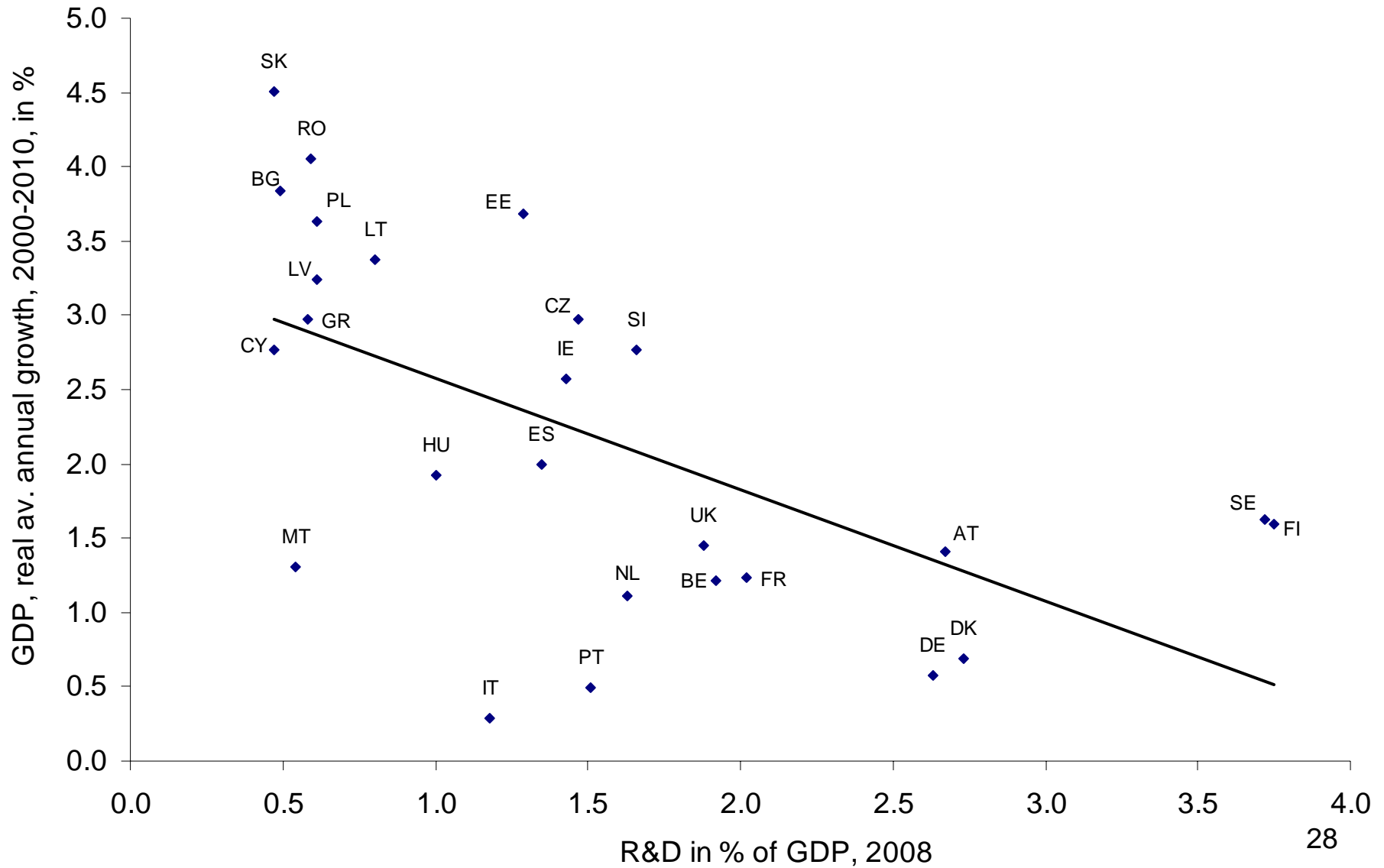
Long-run effects of Labour Productivity Determinants

MAJOR DETERMINANTS	EFFECT ON ANNUAL LABOUR PRODUCTIVITY GROWTH RATE (PERCENTAGE POINTS)
PHYSICAL INVESTMENTS + REGULATION (CAPITAL DEEPENING)	
1. Physical Investment (Permanent 1 % point increase in Investment Share)	0.05
2. Regulation (EU moving to US levels of regulation)	0.15
KNOWLEDGE INVESTMENTS (TFP)	
3. R&D (Permanent 1% point increase in R&D spending)	0.60
4. Education (Permanent 1 year increase in average education levels of labour force)	0.45
5. Ageing (Permanent 10% points decline in youth dependency ratio)	-0.25
6. Openness & Market Size (Permanent 10% points increase in intra-Euro area trade)	0.10
HOURS WORKED (CAPITAL DEEPENING)	
7. Permanent 1 % increase in Hours Worked	-0.25

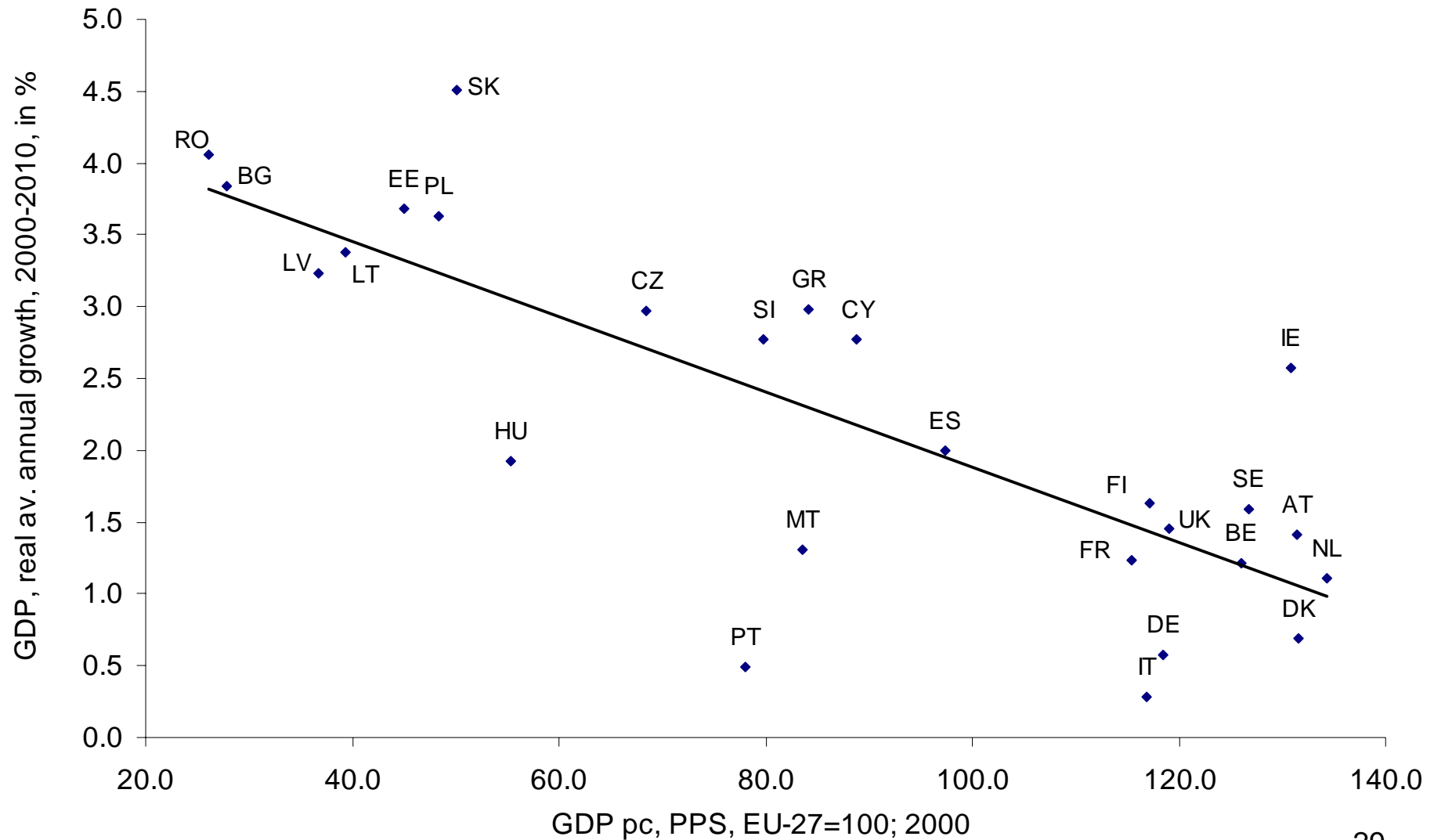
Source: Denis, McMorro, Röger (2004), p. 46 (ECFIN model)

More R&D – more Growth?

(Life is not that simple!)



Still a strong catching-up in enlarged EU-27



Lisbon Strategy ----->
EU 2020

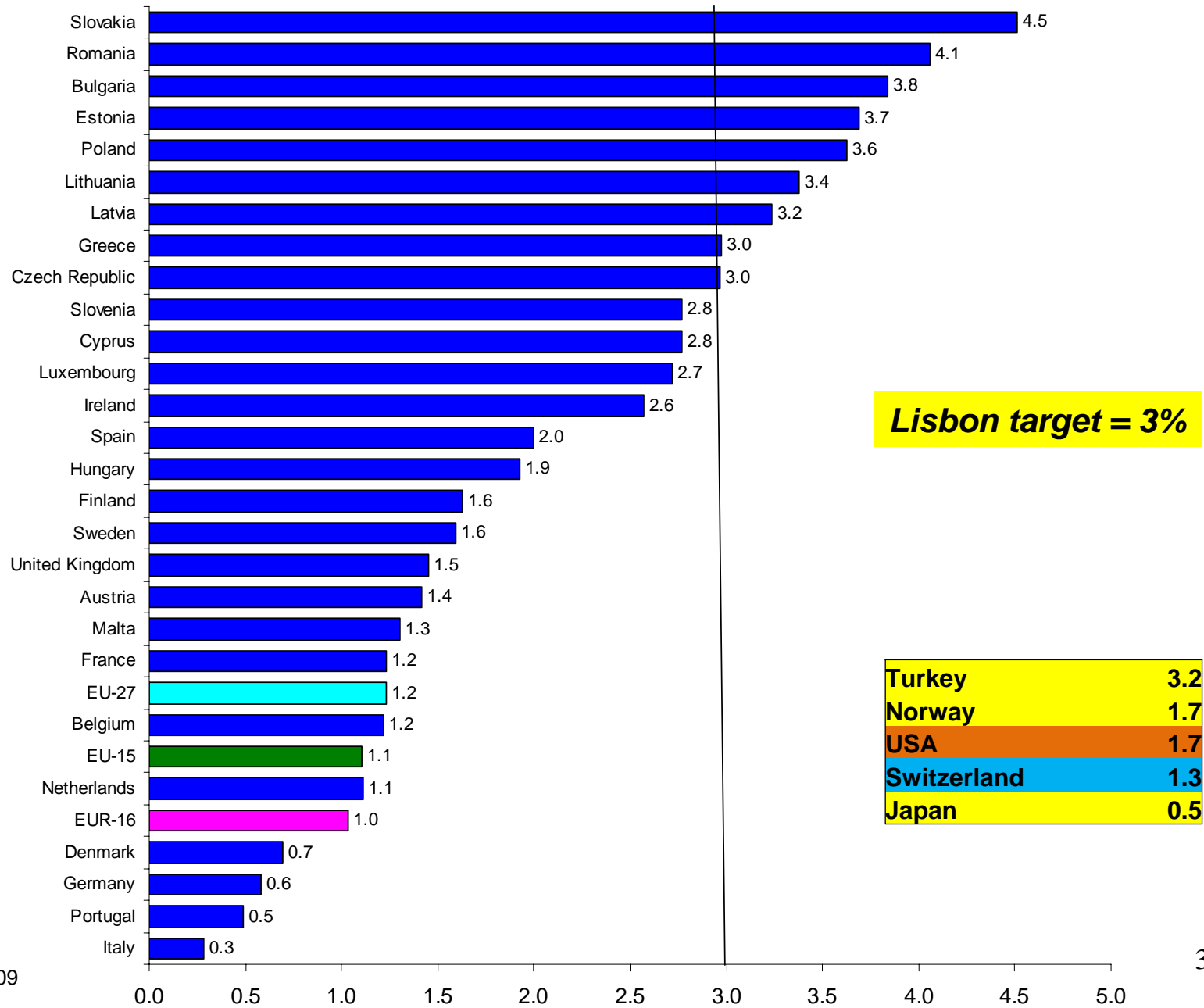
What's new?

Long-run strategies	Objectives	Additional priorities
LS-2000 2000-2010	Growth, jobs, international competitiveness, knowledge, social	Environment
LS-2005	Growth and jobs	Environment, good governance <u>3 dimensions:</u> <i>Economy, social welfare and environment</i>
LS-2006 (new program cycle 2008-2010)	Growth and jobs	“Global Europe”
EU-2020 2010-2020	Sustainable “social market economy”^{*)} , an inclusive, smarter, greener economy	“European Knowledge Area” Successful exit from the crisis

^{*)} Art. 3(3) Treaty on European Union (*Lisbon Treaty*)

Lisbon growth target and realisation, 2000-2010

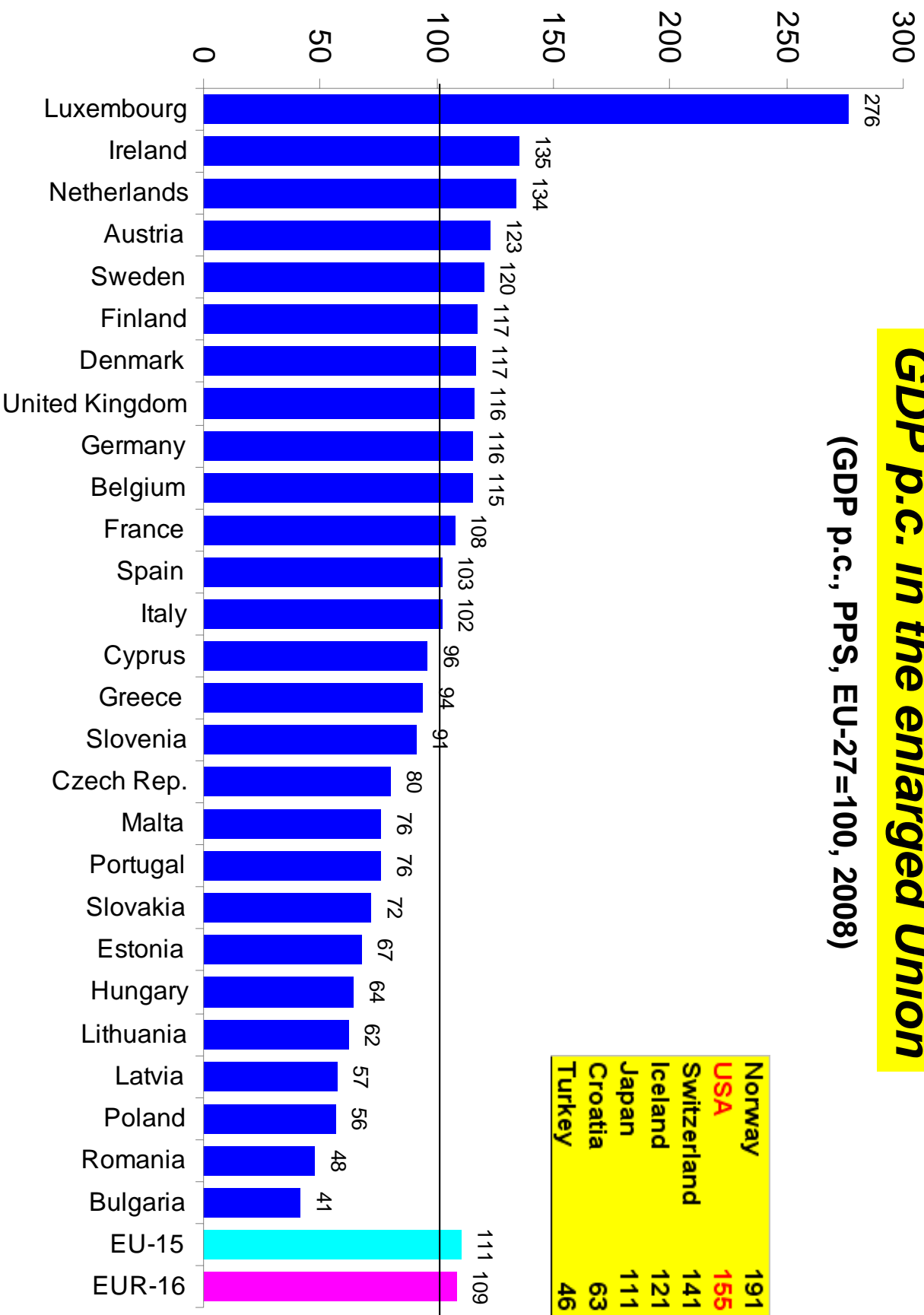
(Real GDP, annual average growth rates, %)



Source:
EU Autumn 2009
forecast

GDP p.c. in the enlarged Union

(GDP p.c., PPS, EU-27=100, 2008)



Source: Eurostat

Challenges for Europe Post 2010?

- **Globalisation** – GFC – *immigration* (asylum seekers)
- **Demography** – aging society
- **Social cohesion** – „Workfare“ instead of „Welfare“
- **Environment** – climate change – energy
- **Acceptance** of the EU – “Europe feeling” of the population of the EU member states

----- **instead of EU 2020** -----

- **Less „planification“** à la Lisbon Strategy and „EU 2020“ – “10 years plan”! – “Nice weather strategy”
- What is missing is a **“CRISIS” strategy** to prevent a new “GFC” ----> new **“EU stability or crisis fund”**
- **Ultimate goal of the EU:** „Social Europe in a Global World“

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