

# THE UNITED STATES AND EUROPE: SHORT-TERM DIVERGENCE BUT SHARED CHALLENGES

Discussion of Jason Furman's Talk  
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Bruegel Lunchtime Event – 33 rue de la Charité, Brussels - 11 May 2016

# EU challenges – short term

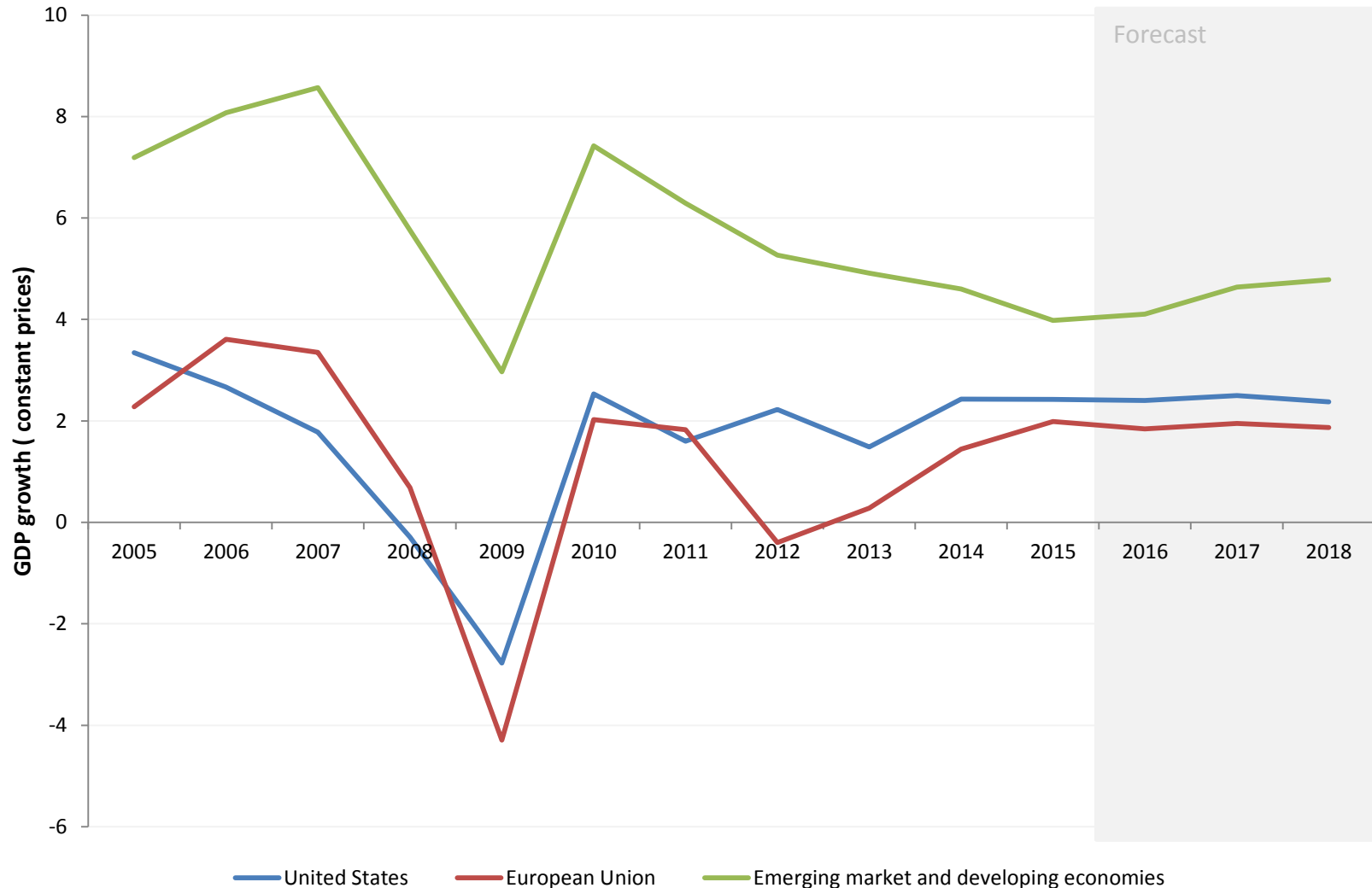
- Recovery, but very moderate
- Heterogeneity across EU countries
- Banking sector restructuring
- Limited room for fiscal stimulus
- Concerns over monetary policy effectiveness
- Political risks – Brexit, Greece, Netherlands, Austria, France...Migrations

# EU challenges – long term

- Competitiveness
  - productivity slowdown
  - demography
- Completing the EU (EA) –make or break?
  - single market
  - Banking Union
  - CMU
  - Euro area “+”

# Bird's eye view on US/EU challenges

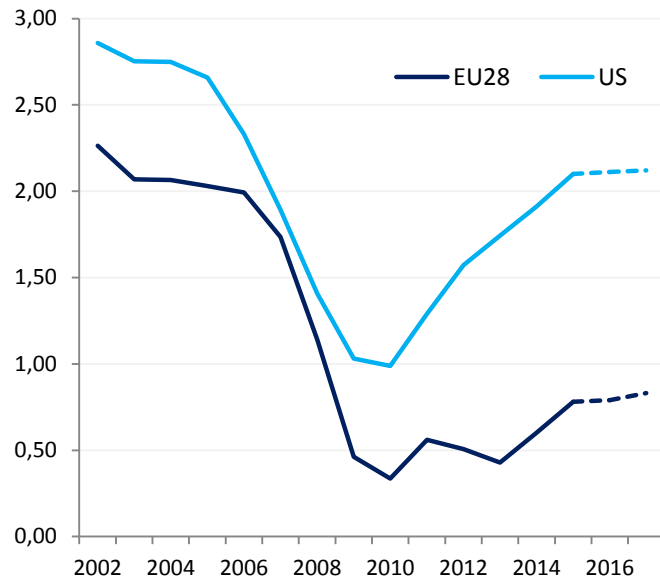
## Real GDP growth, annual %



Source: IMF WEO 2016

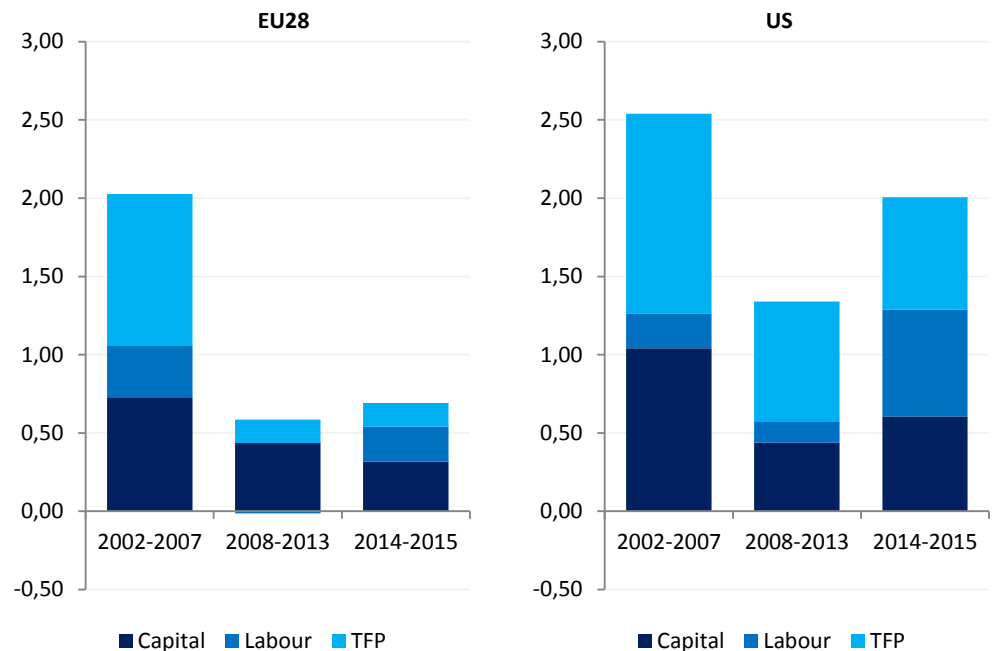
# Potential output: a ST or LT challenge?

**Evolution of potential output growth over time**  
(EU28 vs. US)



Source: EIB/ECON Potential Output Model

**Decomposition of potential output growth**  
Contribution of capital, labour and TFP (EU28 vs. US)



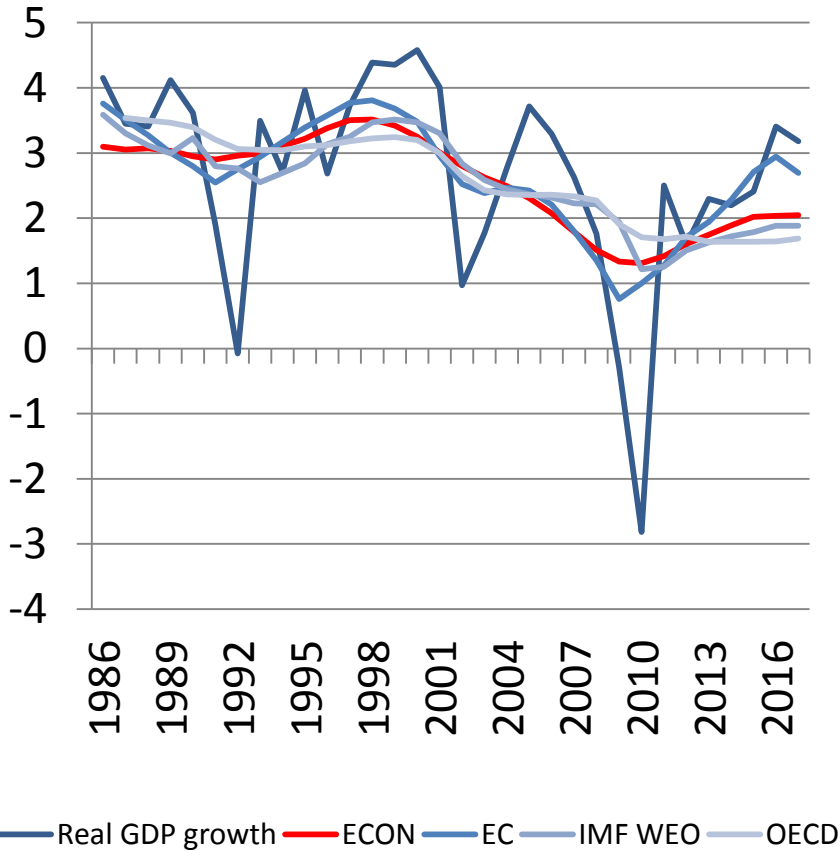
Source: EIB/ECON Potential Output Model

Next: looking at potential with more granularity...  
(all usual caveats apply)

# Potential in the United States: mostly a capital stock / investment issue (labour helps)

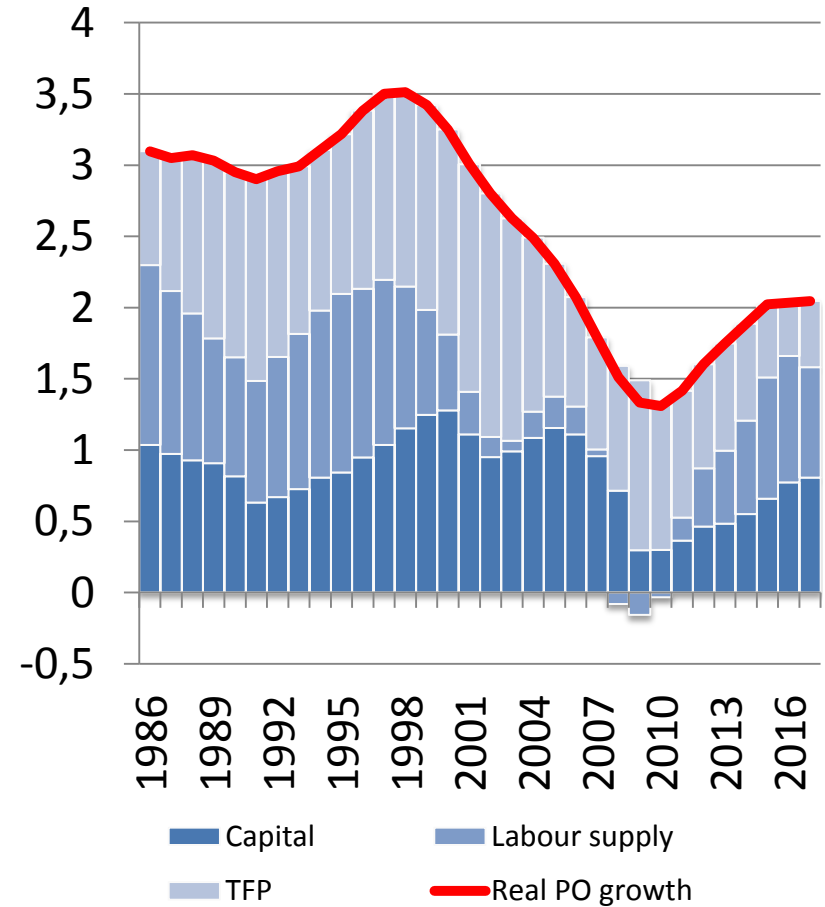
## Potential growth - dynamics

percentage change, yr/yr



## Potential growth - composition

percentage change, yr/yr



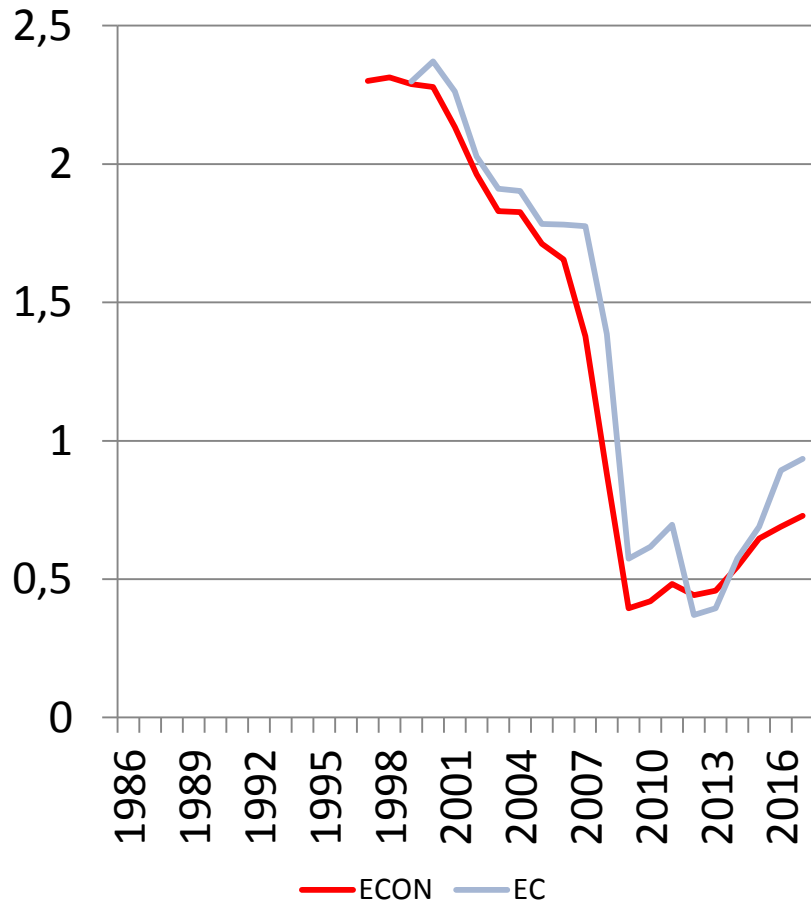
Source: own estimates, EC, OECD, IMF.

Source: own estimates.

# ...While the euro area cumulates handicaps (investment, labour, TFP)...

## Potential growth - dynamics

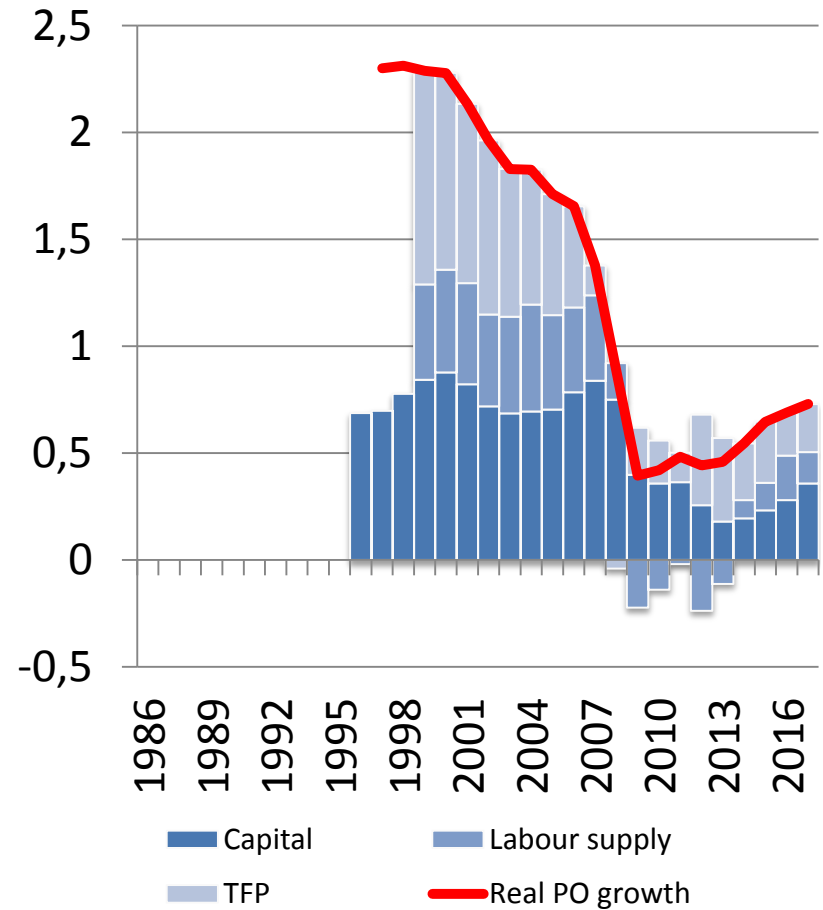
percentage change, yr/yr



Source: own estimates, EC.

## Potential growth - composition

percentage change, yr/yr

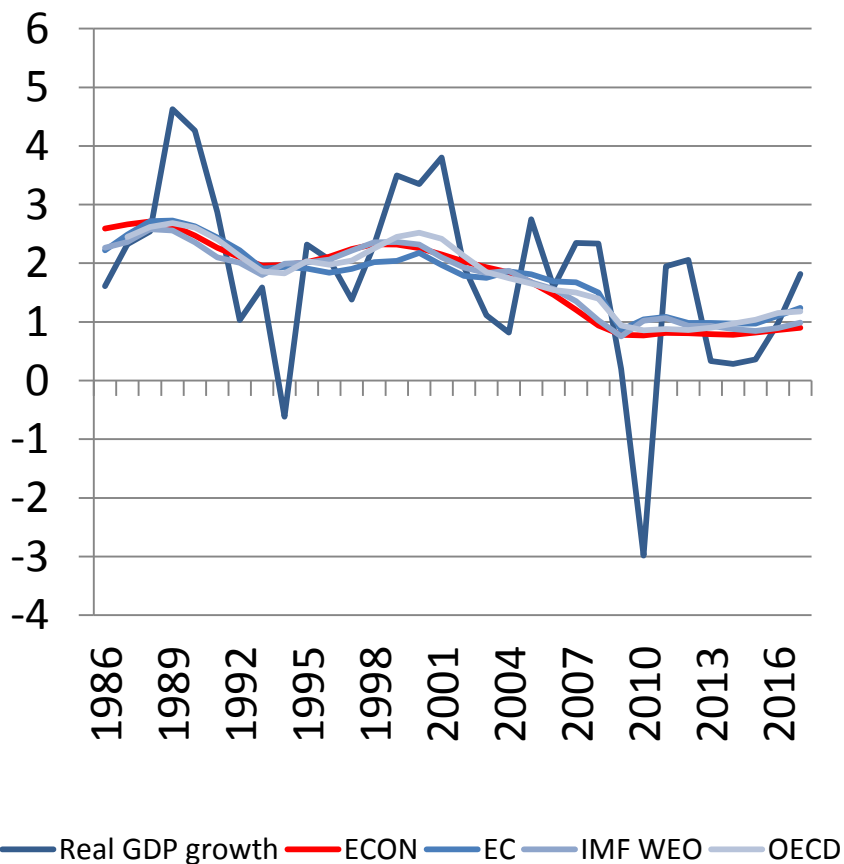


Source: own estimates.

# ...yet, individual countries tell different stories: France (pretty much US like, but at a tiny scale)

## Potential growth - dynamics

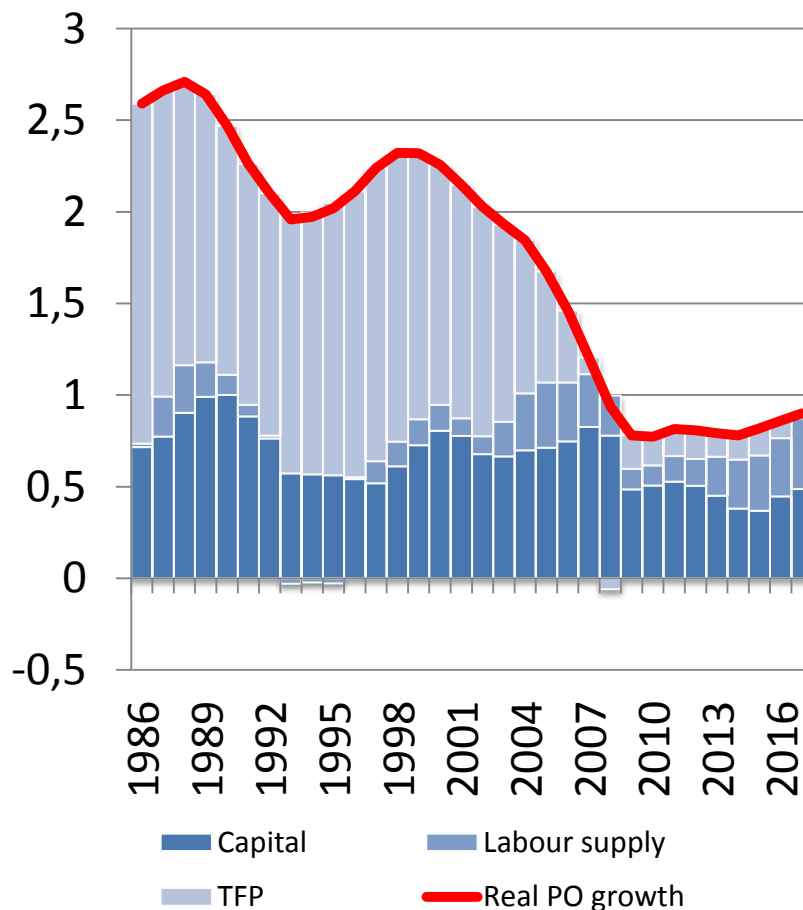
percentage change, yr/yr



Source: own estimates, EC, OECD, IMF.

## Potential growth - composition

percentage change, yr/yr



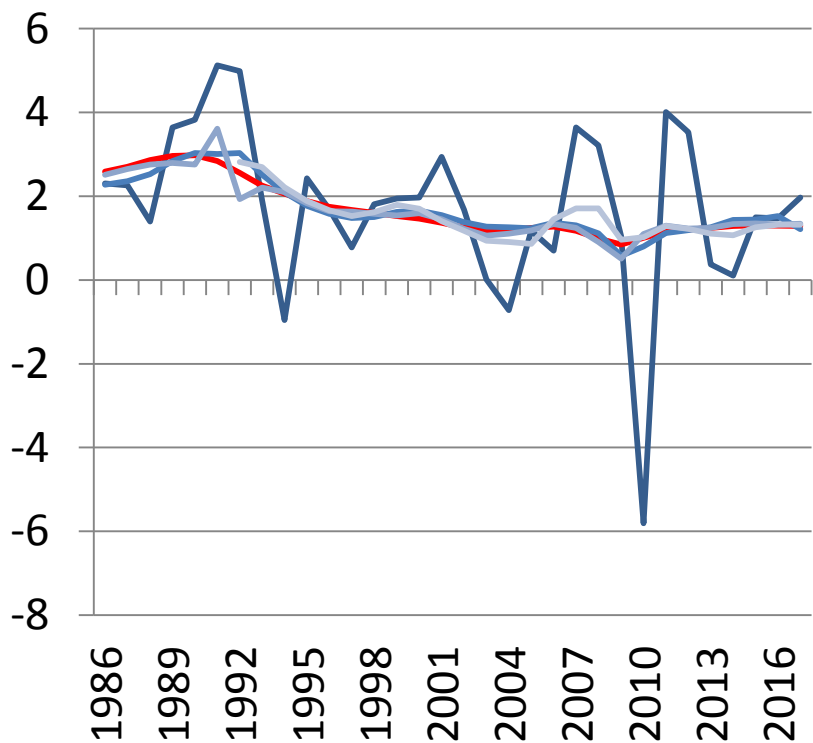
Source: own estimates.



# ...yet, individual countries tell different stories: Germany (where is labour?)

## Potential growth - dynamics

percentage change, yr/yr

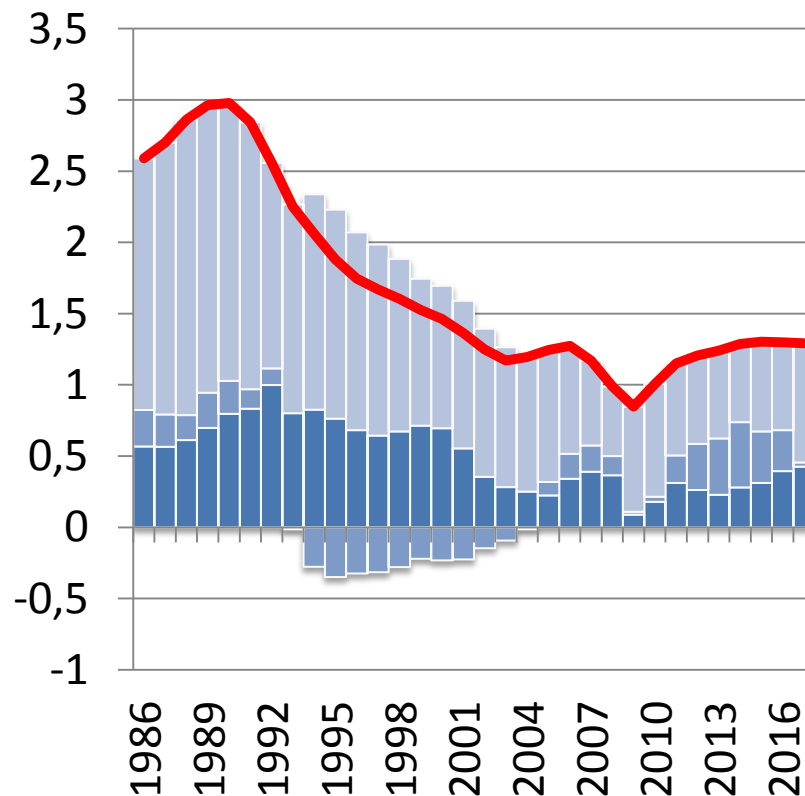


— Real GDP growth — ECON — EC — IMF WEO — OECD

Source: own estimates, EC, OECD, IMF.

## Potential growth - composition

percentage change, yr/yr



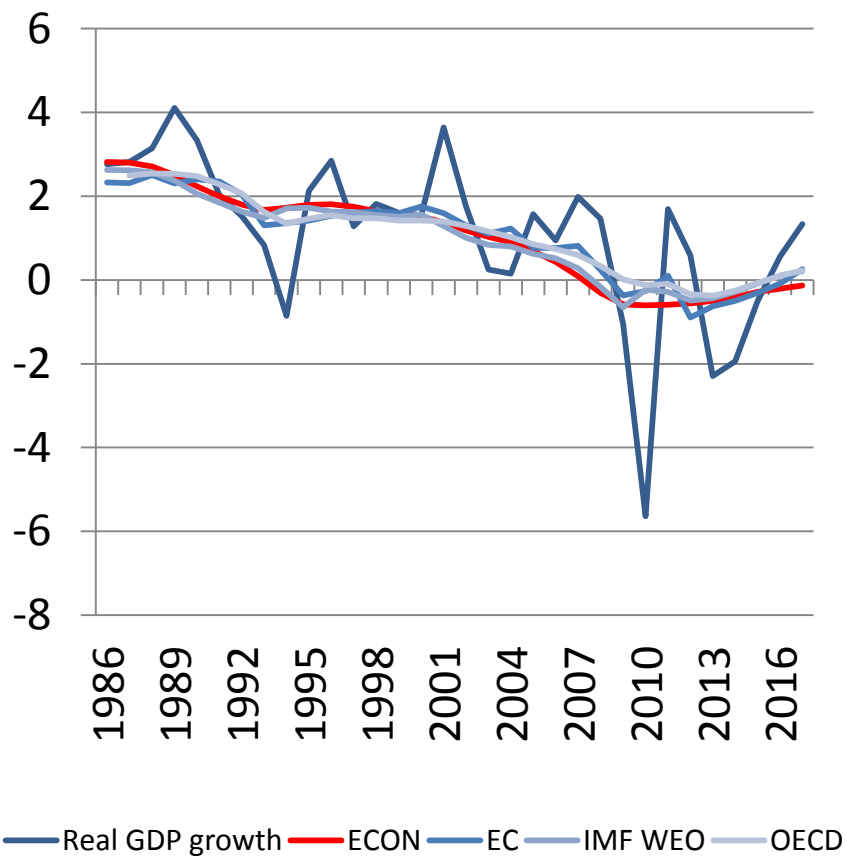
■ Capital ■ Labour supply ■ TFP — Real PO growth

Source: own estimates.

# ...yet, individual countries tell different stories: Italy (pending impact on enacted reforms?)

## Potential growth - dynamics

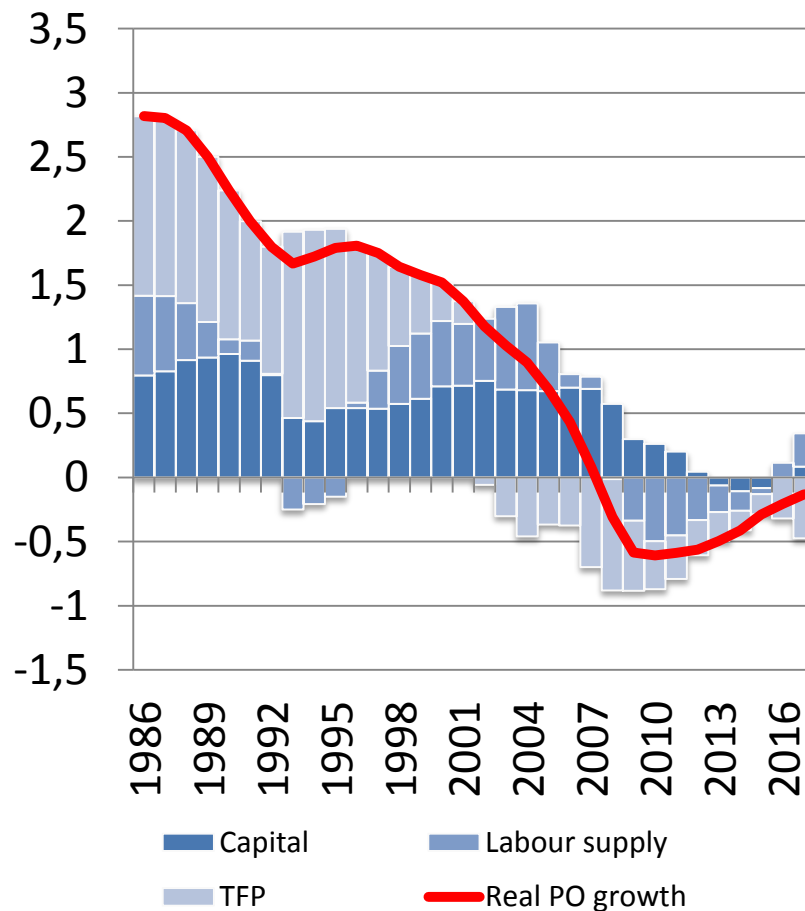
percentage change, yr/yr



Source: own estimates, EC, OECD, IMF.

## Potential growth - composition

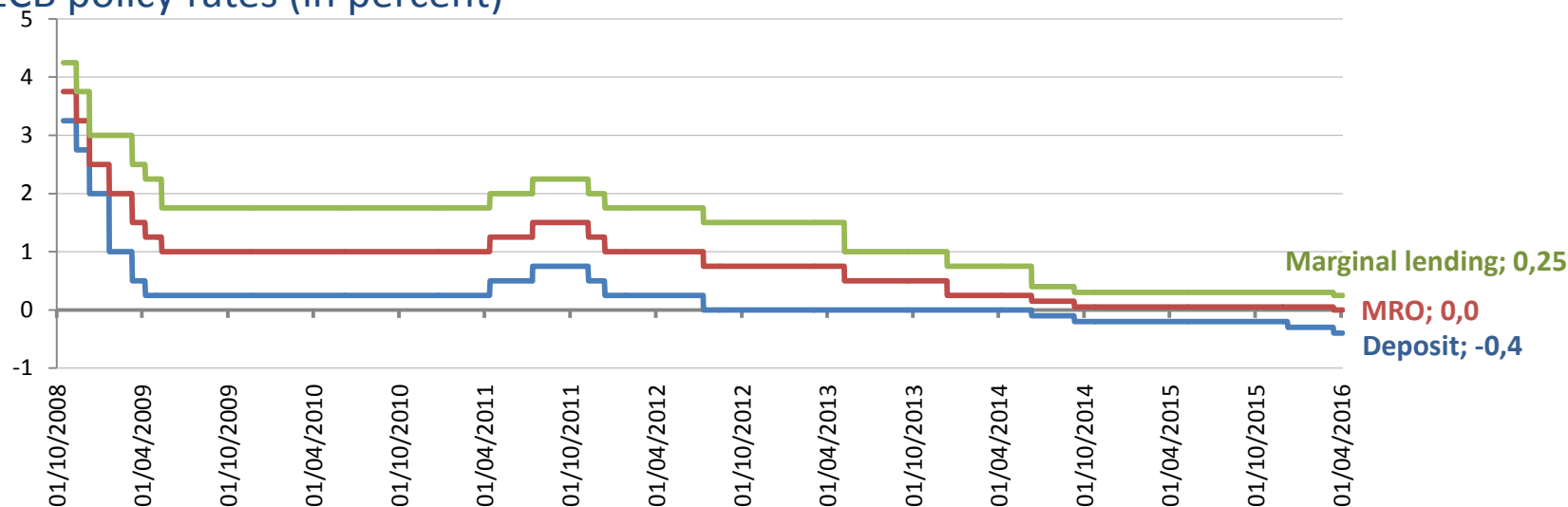
percentage change, yr/yr



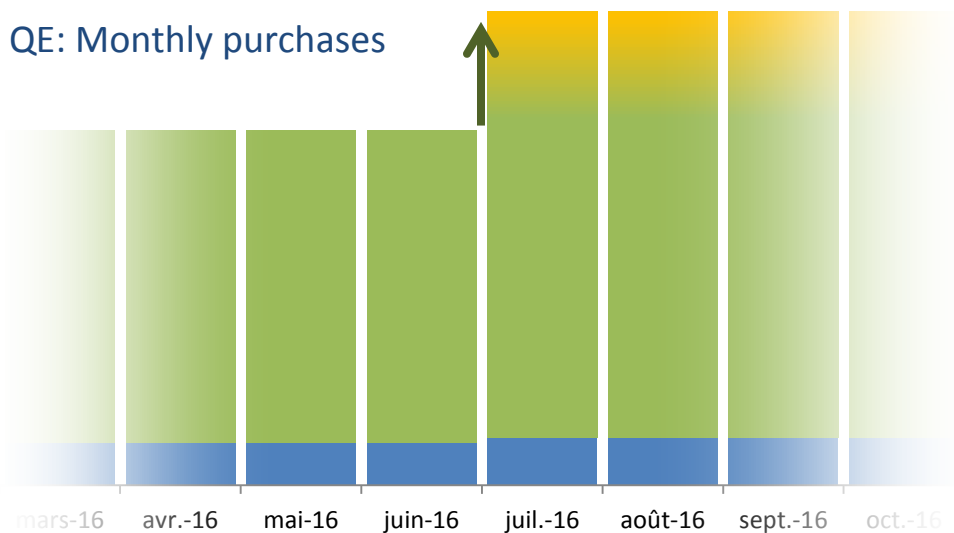
Source: own estimates.

# Monetary policy challenges Fed/ECB: is timing the sole difference?

ECB policy rates (in percent)



ECB's QE: Monthly purchases



Now including investment grade corporate bonds  
Amount estimates: € 5-10 billion

33% overall envelope increase from € 60 billion to € 80 billion

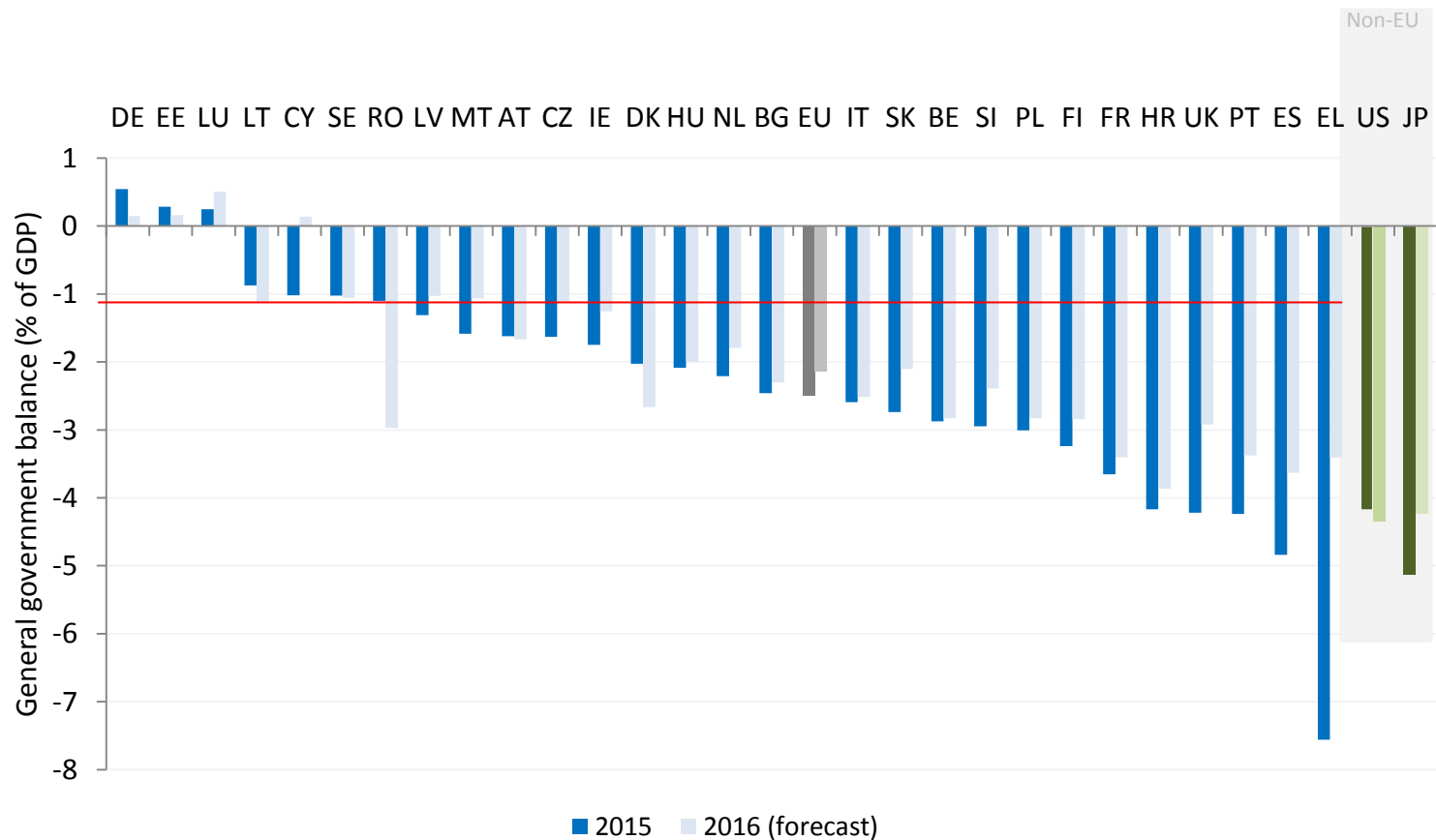
11% increase of EU institutions envelope from € 7.2 billion to € 8.0 billion\*

Source: ECB.

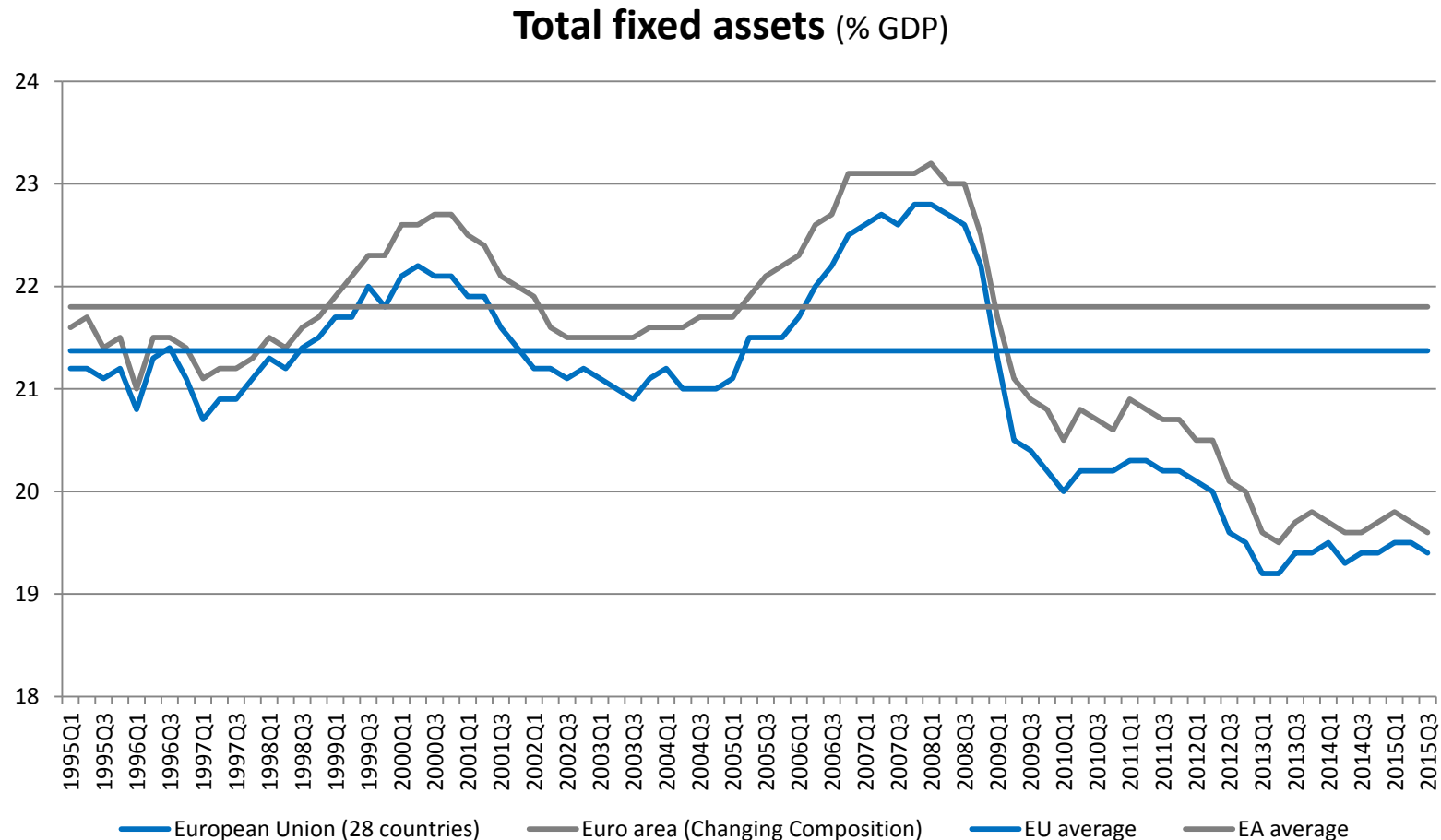
\* Limit per EU issuer increased from 33% to 50% of outstanding.

# Fiscal balances: will the “exorbitant privilege” do the trick for the US?

## General government balance (% of GDP)



# Investment: an EU-specific challenge?



→ about 2pp below pre-crisis average

# Digging into EU investment “gaps” ...

## Annual investment needs

Investment need/objective	Annual investment (EUR billions)		
	Required	Current	Gap
Education	960	860	100
Energy	230	130	100
ICT	160	95	65
Industry	320	230	90
R&D	170	85	130
Transport and Logistics	160	80	80
Water and Waste	138	48	90
<b>Total</b>	<b>2,138</b>	<b>1,528</b>	<b>EUR 655bn</b>

Source: EIB (2016) Restoring EU Competitiveness

Note: For details on calculations, please see report Restoring EU Competitiveness

# ...suggests that investment is needed in both “traditional” and “innovative” sectors

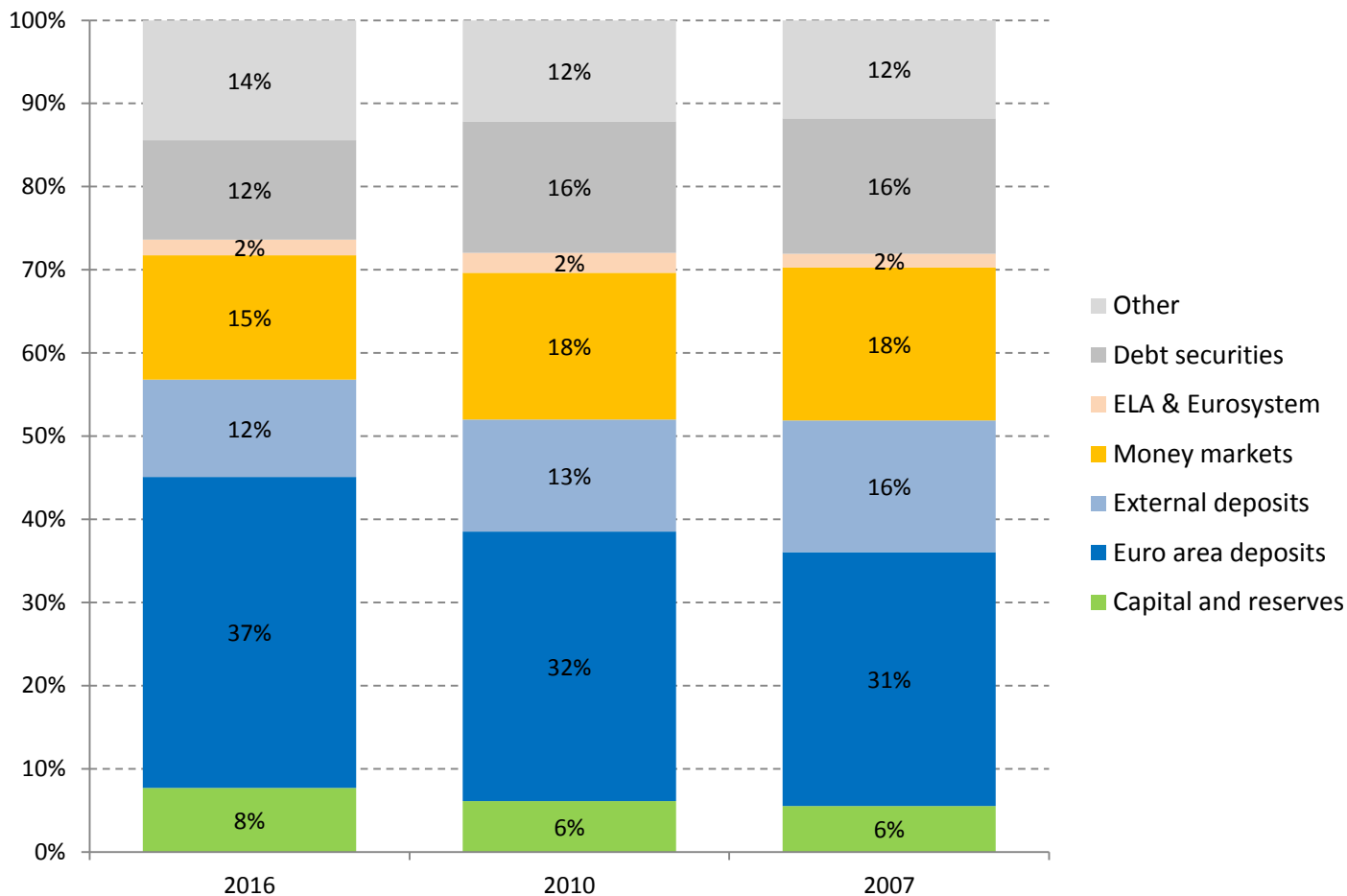
Investment need/objective	Annual investment (EUR billions)		
	Required	Current	Gap
<b>Education</b>	<b>960</b>	<b>860</b>	<b>100</b>
Capital expenditure on education infrastructure, including IT equipment	80	70	10
Operating expenditure (mostly teaching staff)	880	790	90
<b>Energy</b>	<b>230</b>	<b>130</b>	<b>100</b>
Energy efficiency savings in buildings and industry	112	42	70
Power generation, including renewables	53	41	12
Upgrading energy networks (gas and electricity)	65	47	18
<b>ICT</b>	<b>160</b>	<b>95</b>	<b>65</b>
Matching US data centre capacity	50	25	25
Matching US investments in cyber-security	35	25	10
Reaching global benchmark for broadband services	75	45	30
<b>Industry</b>	<b>320</b>	<b>230</b>	<b>90</b>
Adoption of latest generation technology in advanced manufacturing sector	320	230	90
<b>R&amp;D</b>	<b>170</b>	<b>85</b>	<b>130</b>
Life sciences/pharmaceuticals	40	15	25
Machinery and equipment, including ICT and electronics	75	40	35
Other sectors			25
Renewable energy and eco-innovation			20
Transport equipment	55	30	25
<b>Transport and Logistics</b>	<b>160</b>	<b>80</b>	<b>80</b>
Ensuring sufficient capacity in interurban traffic	80	40	40
Modernising urban transport to meet global benchmarks	80	40	40
<b>Water and Waste</b>	<b>138</b>	<b>48</b>	<b>90</b>
Additional needs for resilient and efficient urban infrastructure	40	13	27
Compliance and rehabilitation of Europe’s water infrastructure	75	30	45
Enhancing waste management/materials recovery	8	3	5
Water security, including flood risk management	15	2	13
<b>Total</b>	<b>2,138</b>	<b>1,528</b>	<b>EUR 655bn</b>

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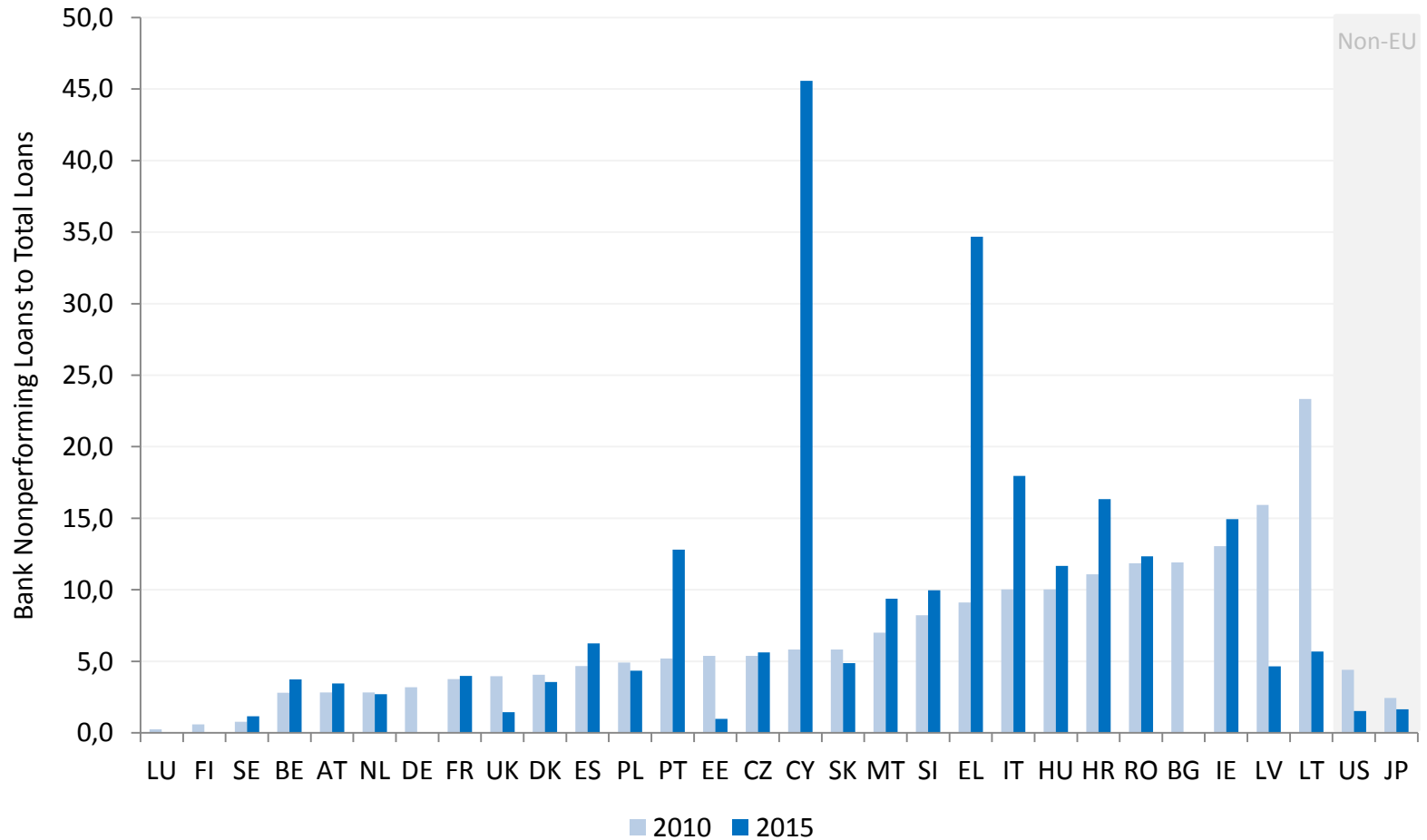
# A reminiscent challenge in Europe: bank balance sheets – assets...

## Balance sheets MFI euro area





# ...and liabilities



# Bottom line

- Currency (will) make(s) the difference
  - International role
  - Fiscal space
- Monetary policy ahead: complex everywhere
- Potential growth: labour markets and mobility
- Will politics dominate anyway?