



The EU's investment and growth model going forward

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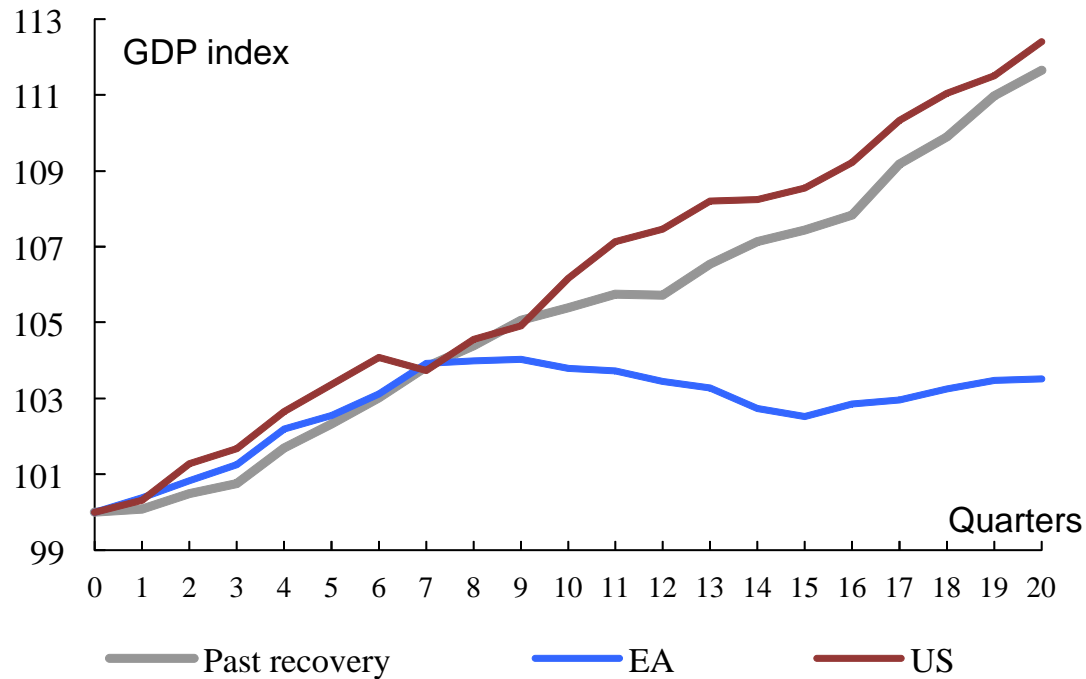
Peterson Institute for International Economics
Washington, October 9, 2014

Outline

- 1. The impact of the crisis on investment**
- 2. What are the factors hampering investment**
- 3. Policy avenues to boost investment**

The recovery: failing to get off the ground?

Comparison of current recoveries against past recovery



* Current recovery: Upturn starting in 2009Q2 in EA and US

** Past recovery: Upturn starting in 1993Q1 in EA

Investment is key for productivity growth and to strengthen demand

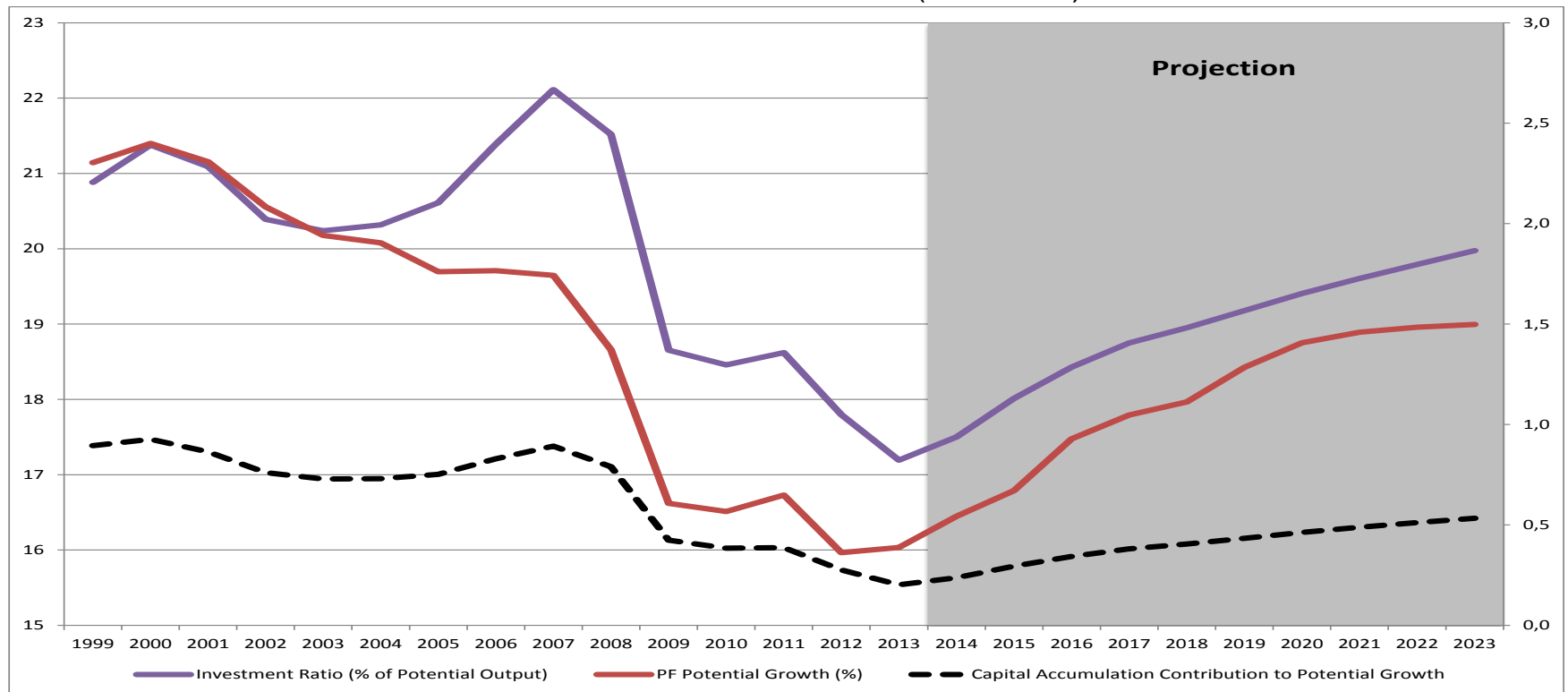
Growth rates in equipment investment in EA-18, selected Member States, and US

| | '09 vs '08 | '13 vs '09 | '15 vs '13 |
|-------|------------|------------|------------|
| DE | -22.7 | 8.9 | 11.1 |
| FR | -18.1 | 13.8 | 11.1 |
| IT | -16.8 | -6.8 | 11.9 |
| UK | -20.3 | -1.8 | 16.7 |
| US | -19.0 | 33.8 | 13.7 |
| EA-18 | -19.1 | 3.0 | 11.4 |

Source: European Commission, Spring 2014 forecast

Low investment is hurting future growth prospects

Investment and Potential Growth (Euro area)

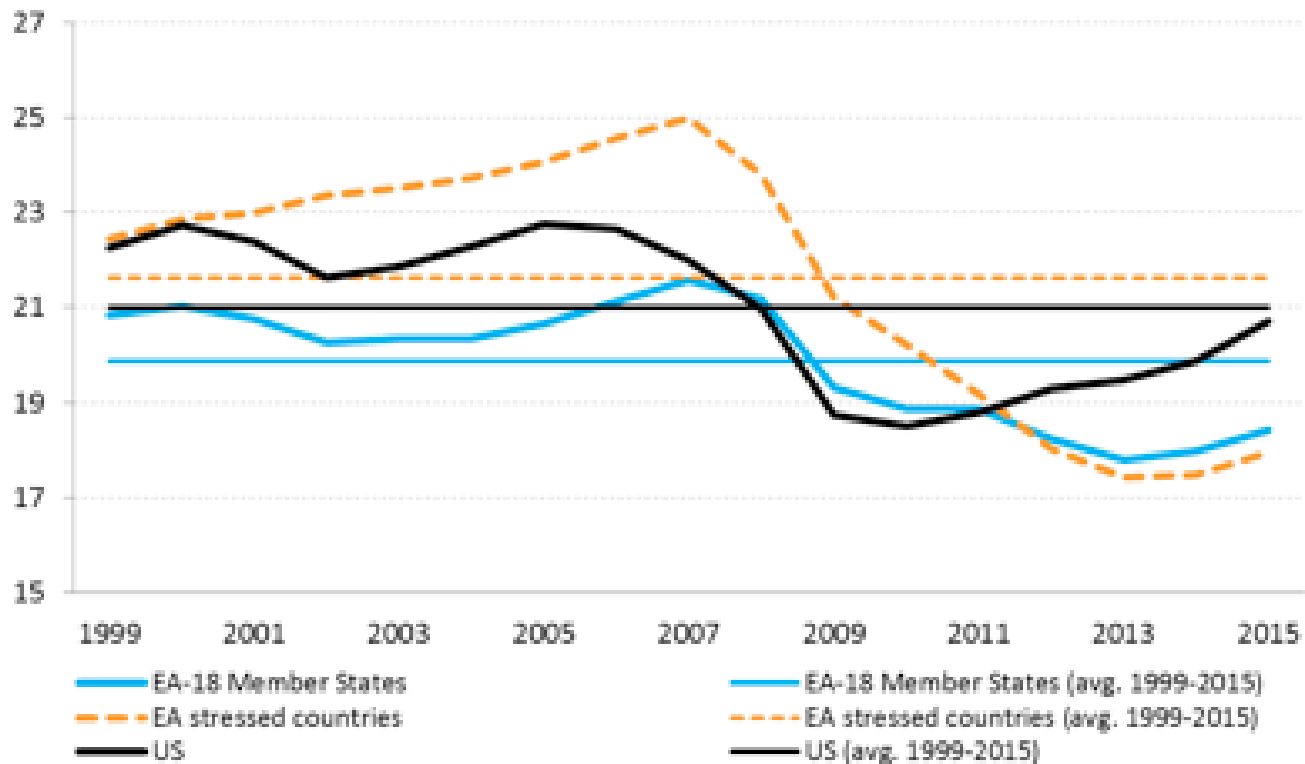


Investment to potential output ratio (lhs)
 Capital Accumulation Contribution to Potential Growth (rhs)
 PF Potential Growth (rhs)

Source: ECFIN analysis

Investment is key for productivity growth and to strengthen demand

Investment to GDP ratios 1999-2015

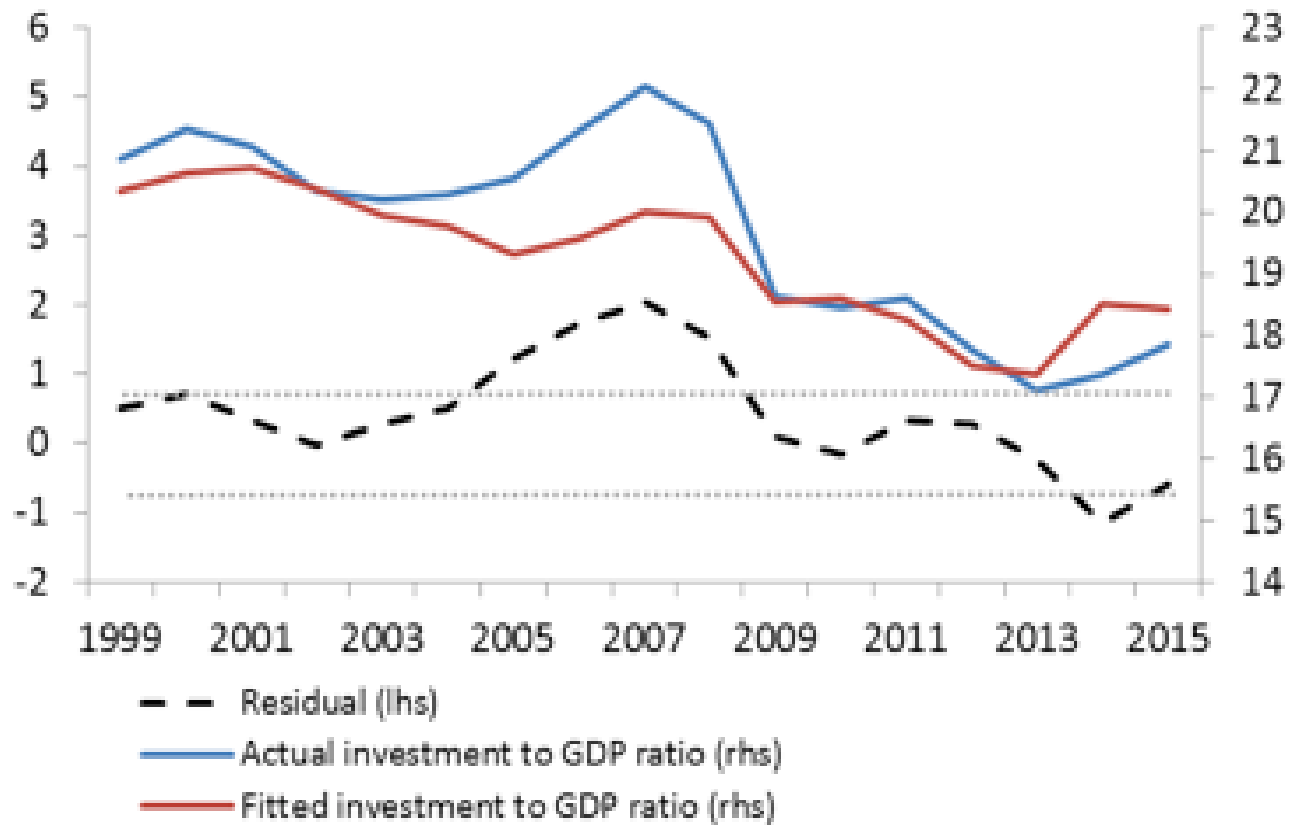


What are the factors hampering investment in EU?

1. The "accelerator" strikes back
2. Need of deleveraging in some countries and reduction of overcapacity in pre-crisis booming sectors
3. Financial fragmentation
4. Cuts in public investment
5. Uncertainty, including policy uncertainty

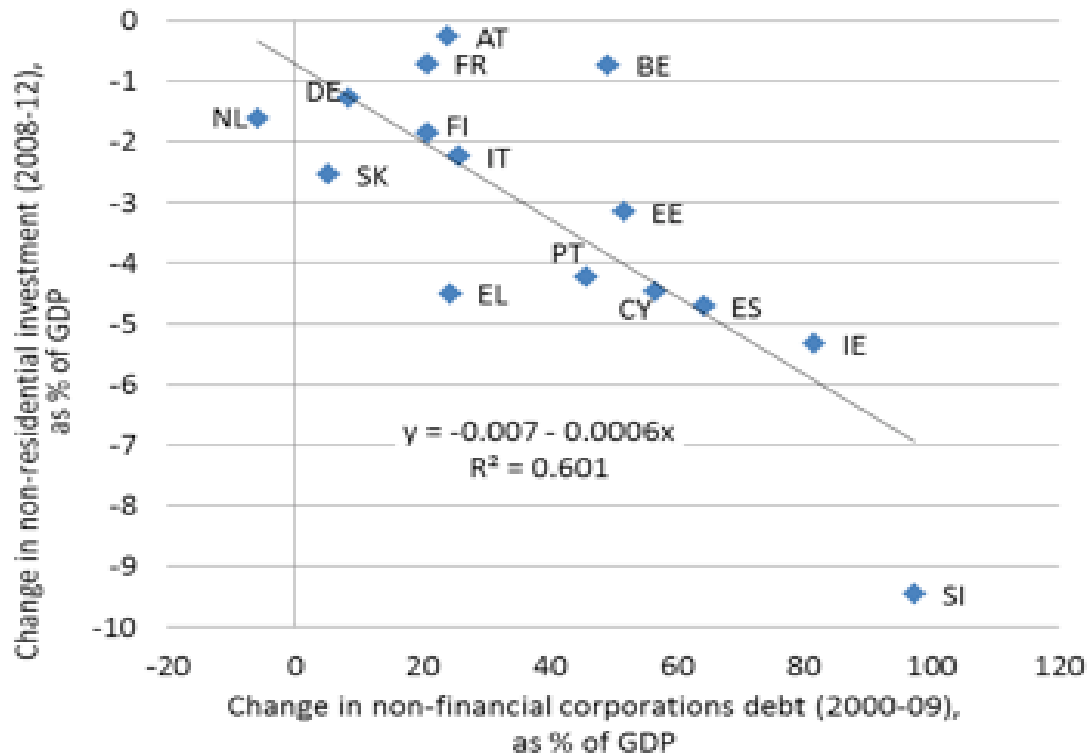
1. Accelerator: no investment without growth

Investment regressions using the accelerator model for the EA



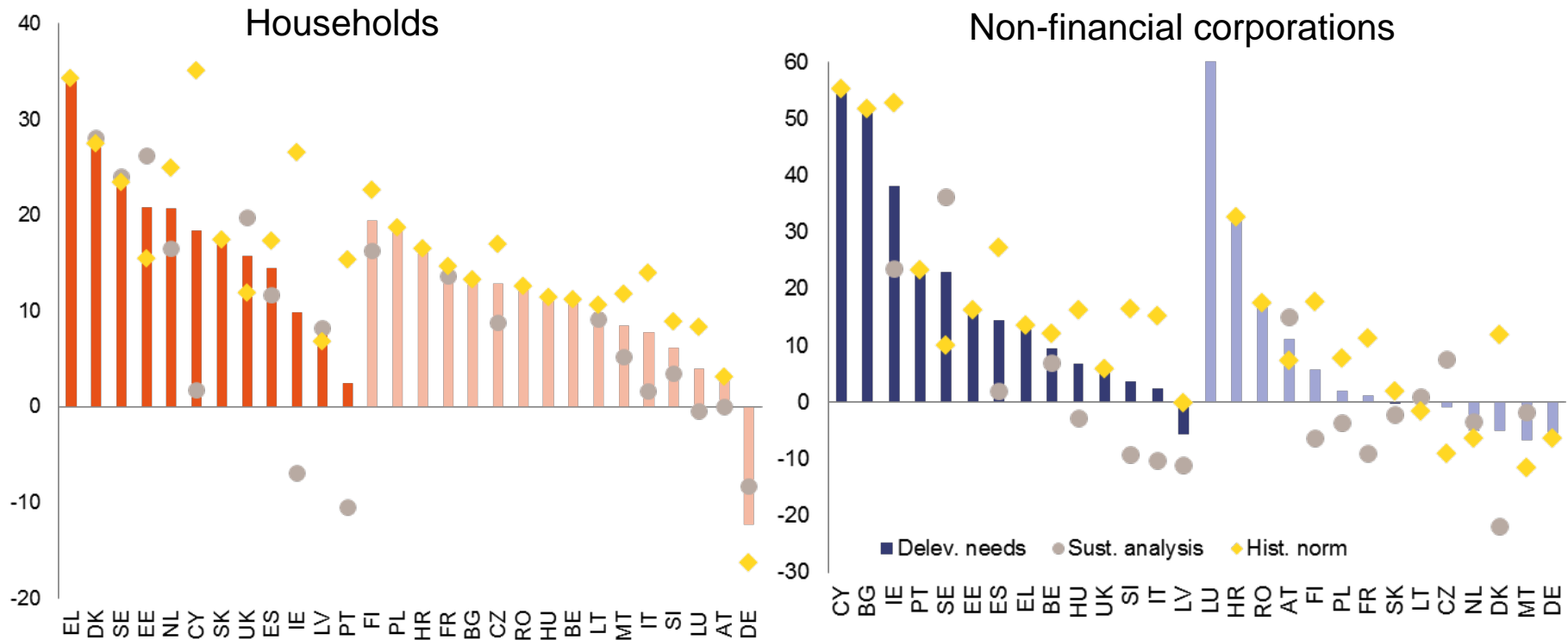
2. Deleveraging: balance sheet repair weighs on investment

Non-residential investment and NFC debt

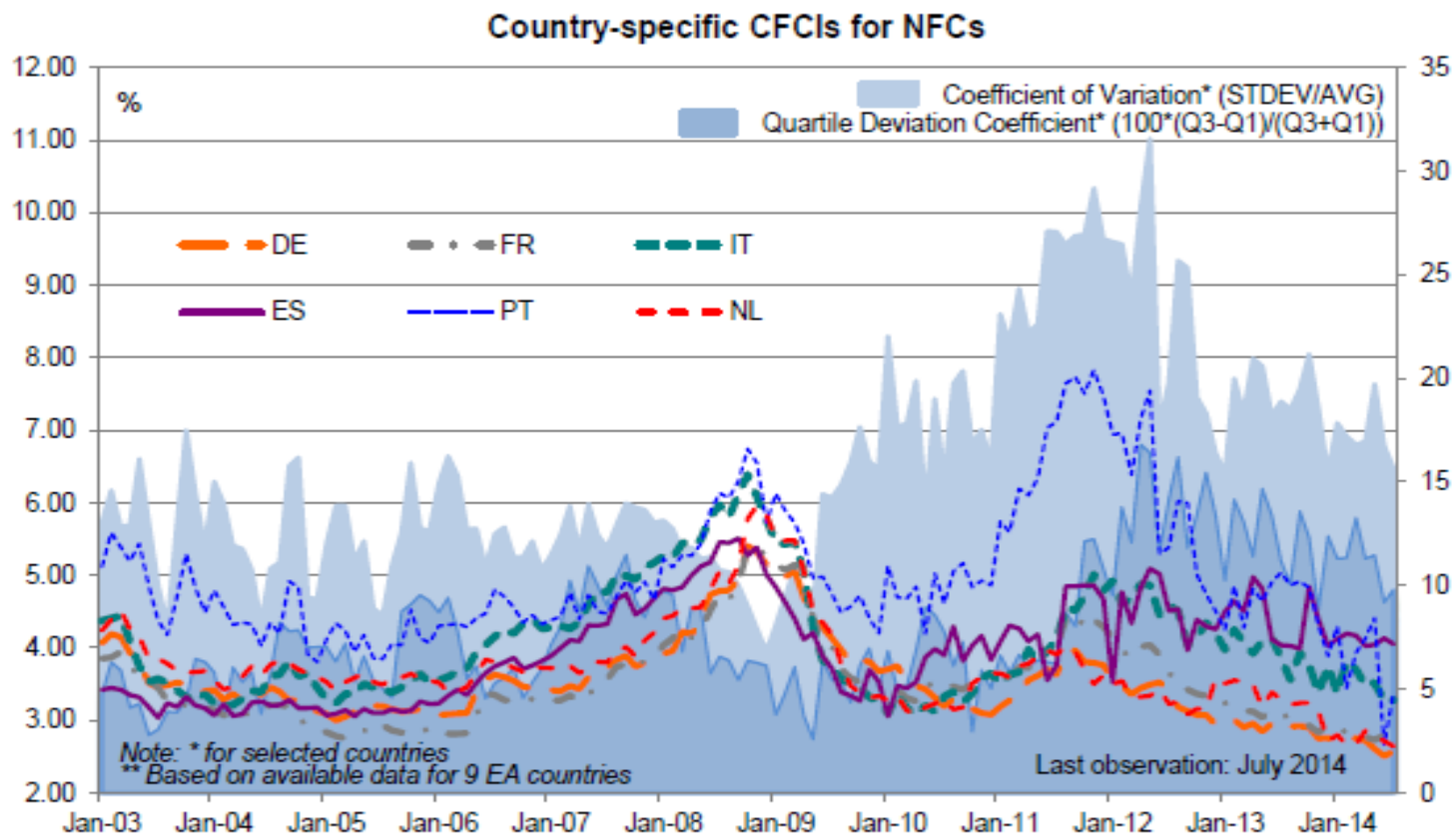


2. Deleveraging: how much still to go?

Estimated deleveraging needs, 2013 data (% of GDP)



3. Financial fragmentation in Europe

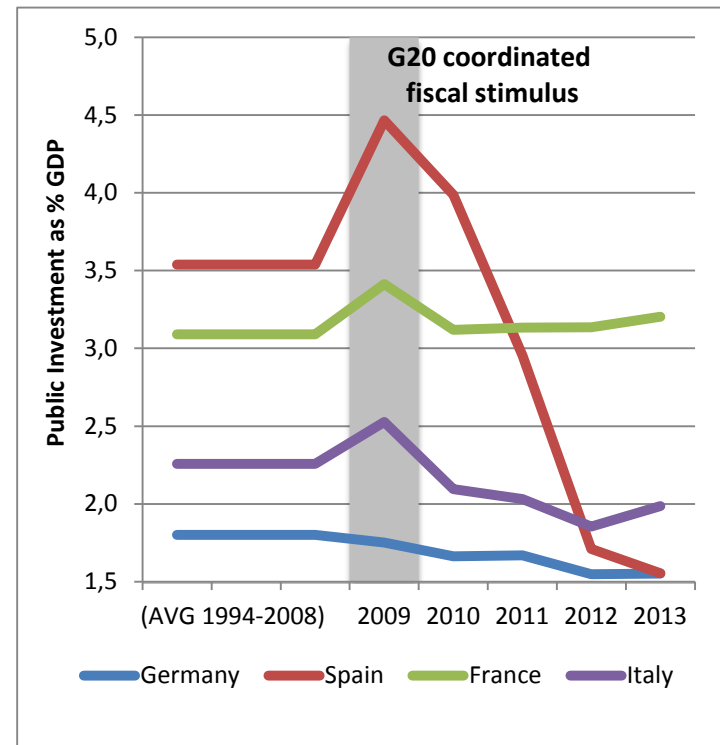
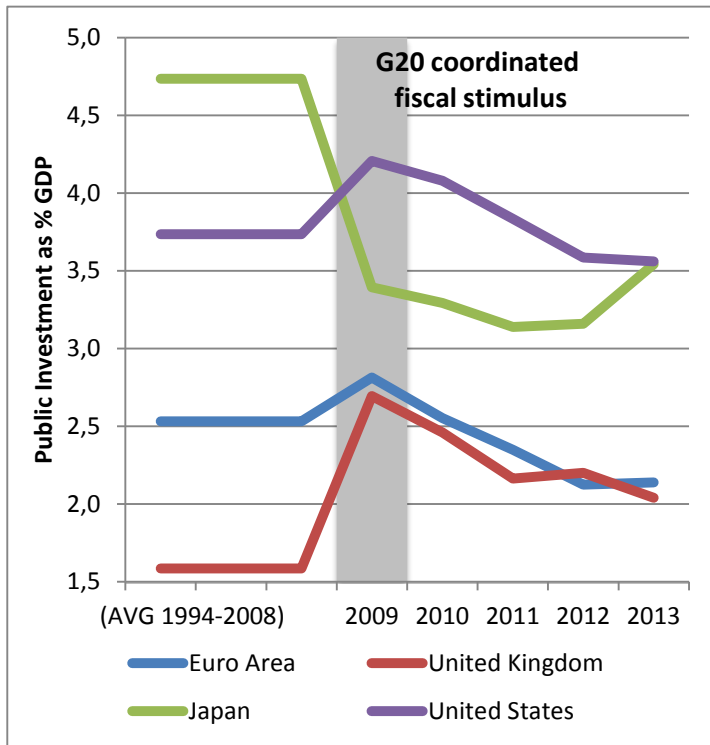


Note: * Based on available data for 9 EA countries

Source: ECB, Bloomberg, BofA ML, DG ECFIN calculations

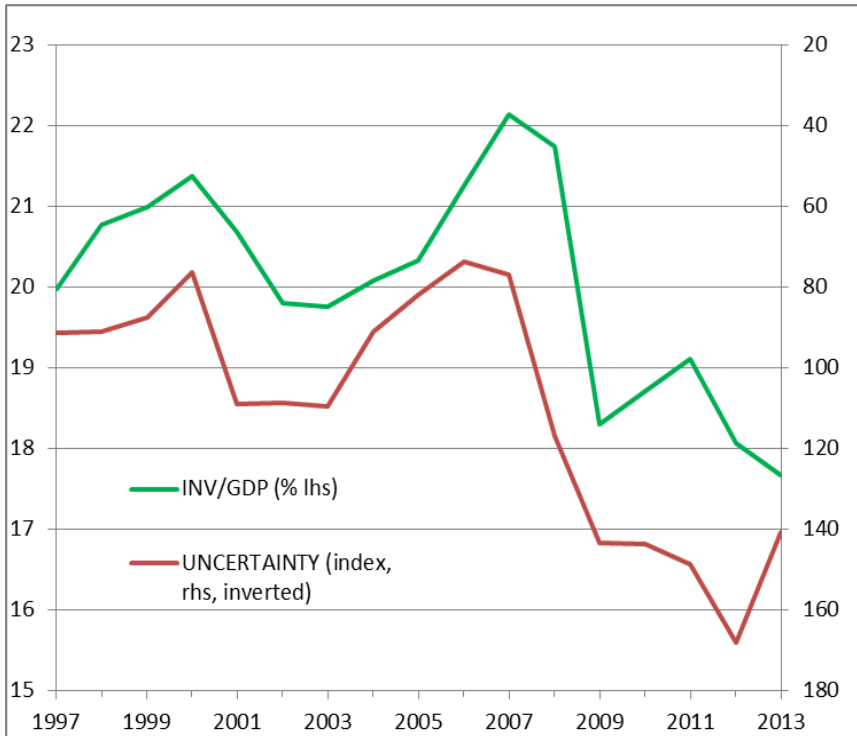
4. Public Investment: is it too low?

Public investment (% GDP)

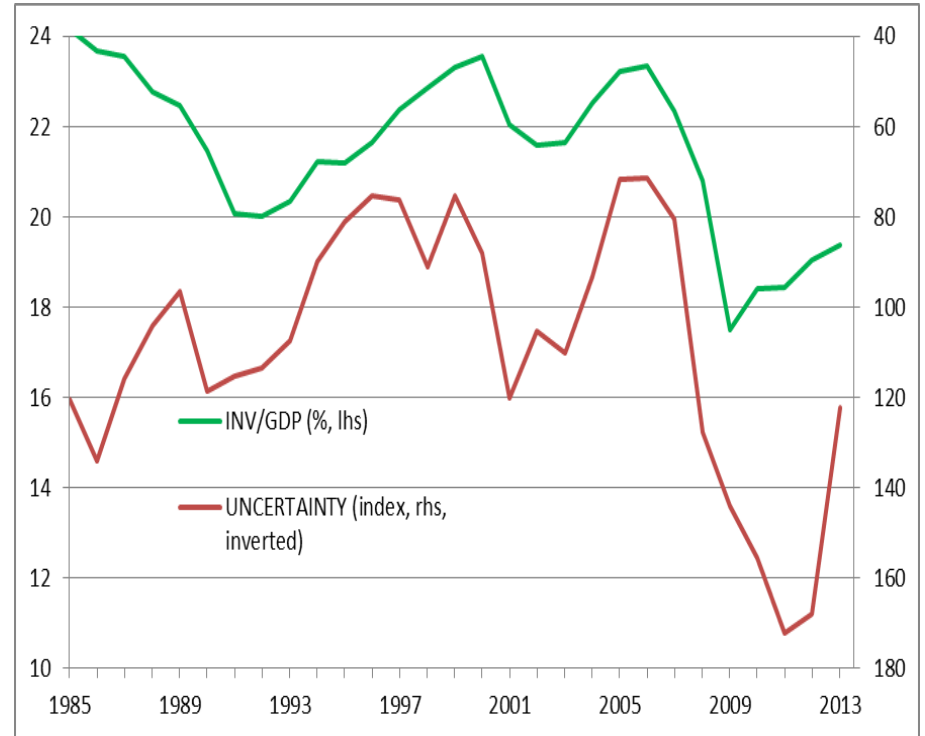


5. Investment and uncertainty

European Union



USA



Source: Calculations based on data from IMF WEO and www.policyuncertainty.com

Policy avenues to restore investment

- Rotation and strengthening of demand to put the accelerator into reverse.
- Product market reforms to unlock investment opportunities.
- Overcome financial fragmentation by completing Banking Union.
- Improving access to long-term finance for investment and reducing "bank-centrism" in the Euro area.
- Safeguarding and improving the quality of public investment, material and immaterial, in consolidation strategies.
- In the G20, adopting a coordinated set of actions aimed at boosting investment both on the demand and the supply side.

=> *Action is needed at all levels: national, European, global*

1. Action at national level

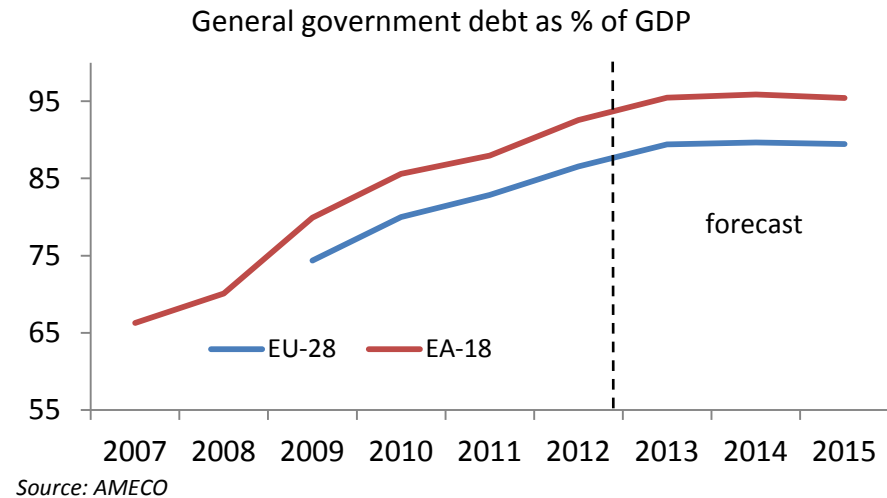
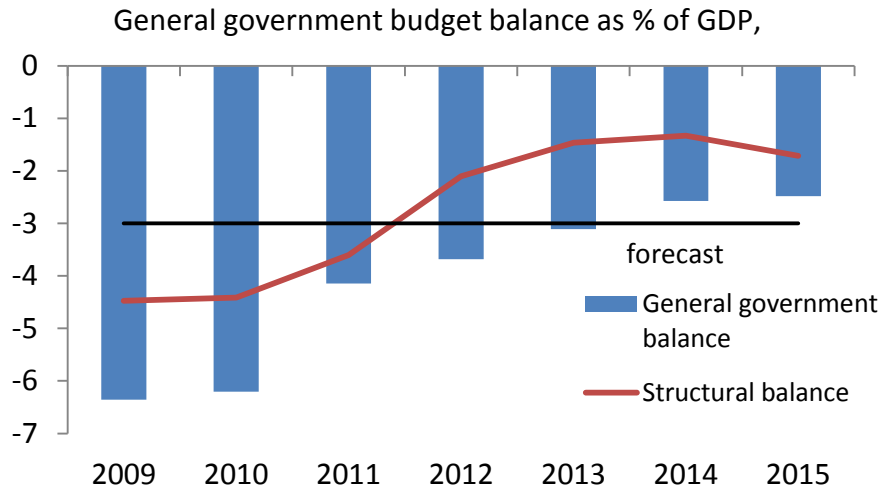
- More balanced adjustment

Growth-friendly differentiated fiscal consolidation to increase public investment

- Structural reforms – country-specific recommendations

Increasing dynamic efficiency and boosting employment, facilitating rebalancing

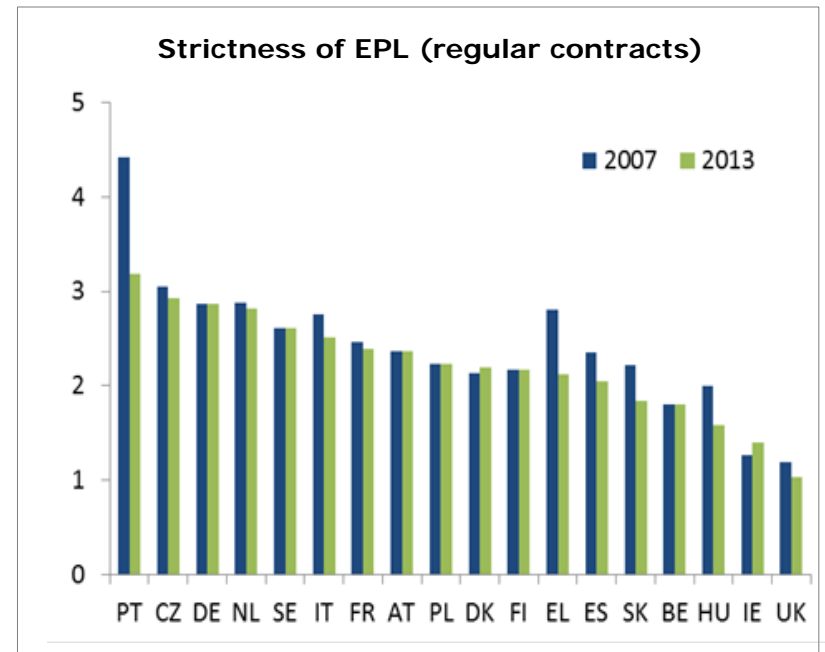
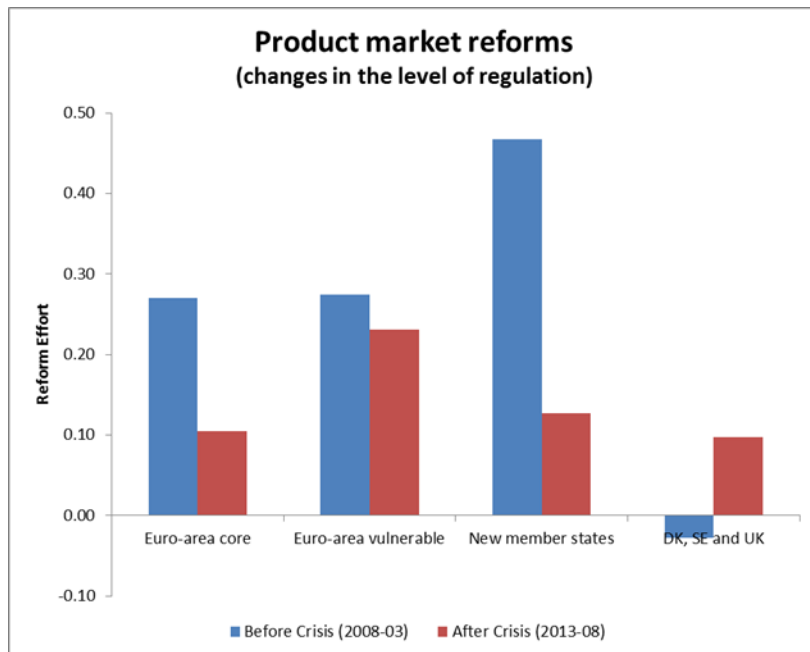
Growth-friendly, differentiated fiscal consolidation: fiscal policy becoming more neutral



- Expenditure side: raise quality of public expenditure, prioritising productive investment
- Revenue side: make the tax system more fair and efficient
- Countries with more fiscal space should take measures to encourage domestic demand and make adjustment more symmetric

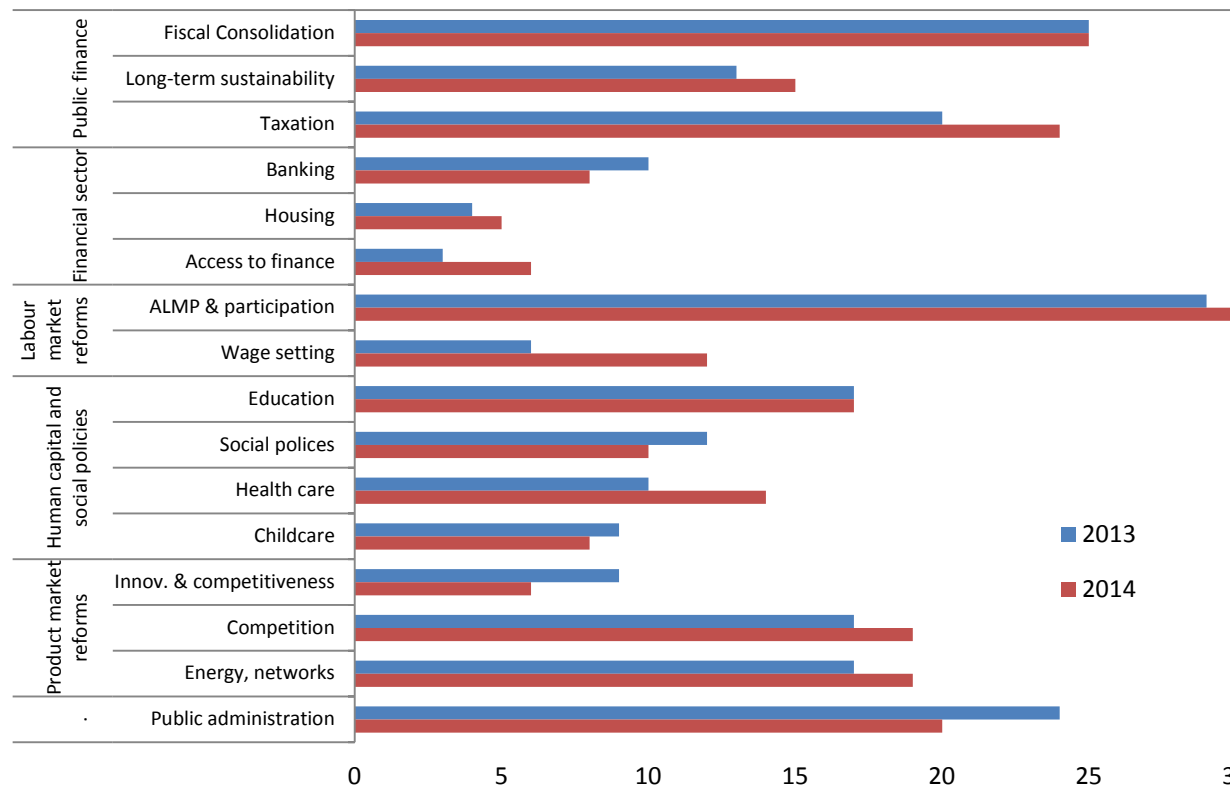
Structural reforms to boost growth and facilitate rebalancing

- Important measures taken by vulnerable countries in labour markets, but employment will take time to recover. More is needed in product markets
- Less progress has been made in core countries; product market reforms needed to improve competition and strengthen domestic demand



The EU-level policy advice addresses major reform priorities

Number of Country-specific recommendations in 2013 and 2014, by policy area



2. Action at EU level

- Remove regulatory bottlenecks to investment
- Better use of available resources: EIB, EU budget
- Increase access to long-term financing
- Overcome financial fragmentation, complete Banking Union
- ECB latest decisions will help inflation return to target
- Design "Juncker's investment package"

3. Action at global level

Restoring investment is also a main concern:

- Brisbane Summit: G20 members' growth strategies
- Objective to lift collective GDP by 2% above the trajectory implied by current policies over 5 years
- G20 meetings run-up to Brisbane: work in progress
 - Brisbane Action Plan
 - Global Infrastructure Center



European
Commission

**Thank you very much for your
attention!**