



INTERNATIONAL MONETARY FUND

# EUROZONE: STRENGTHENING RESILIENCE IN COMPLEX TIMES

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# **EUROZONE: STRENGTHENING RESILIENCE IN COMPLEX TIMES**

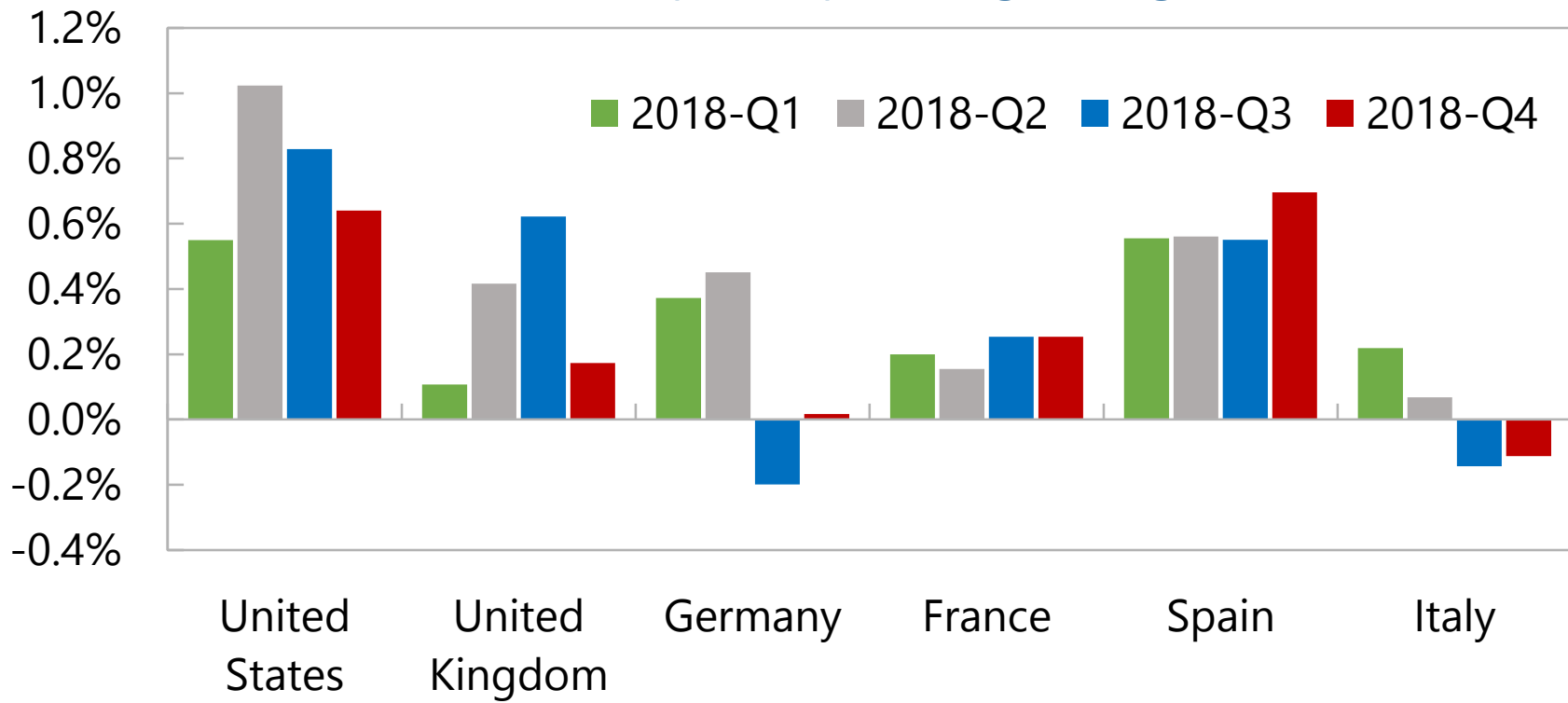
- 1. ECONOMIC OUTLOOK**
- 2. SHORT TERM RISKS**
- 3. MEDIUM TERM CHALLENGES**
- 4. POLICY RECOMMENDATIONS**

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## Disappointing 2018 Q3 and Q4

### GDP growth

Quarter over quarter, percentage change

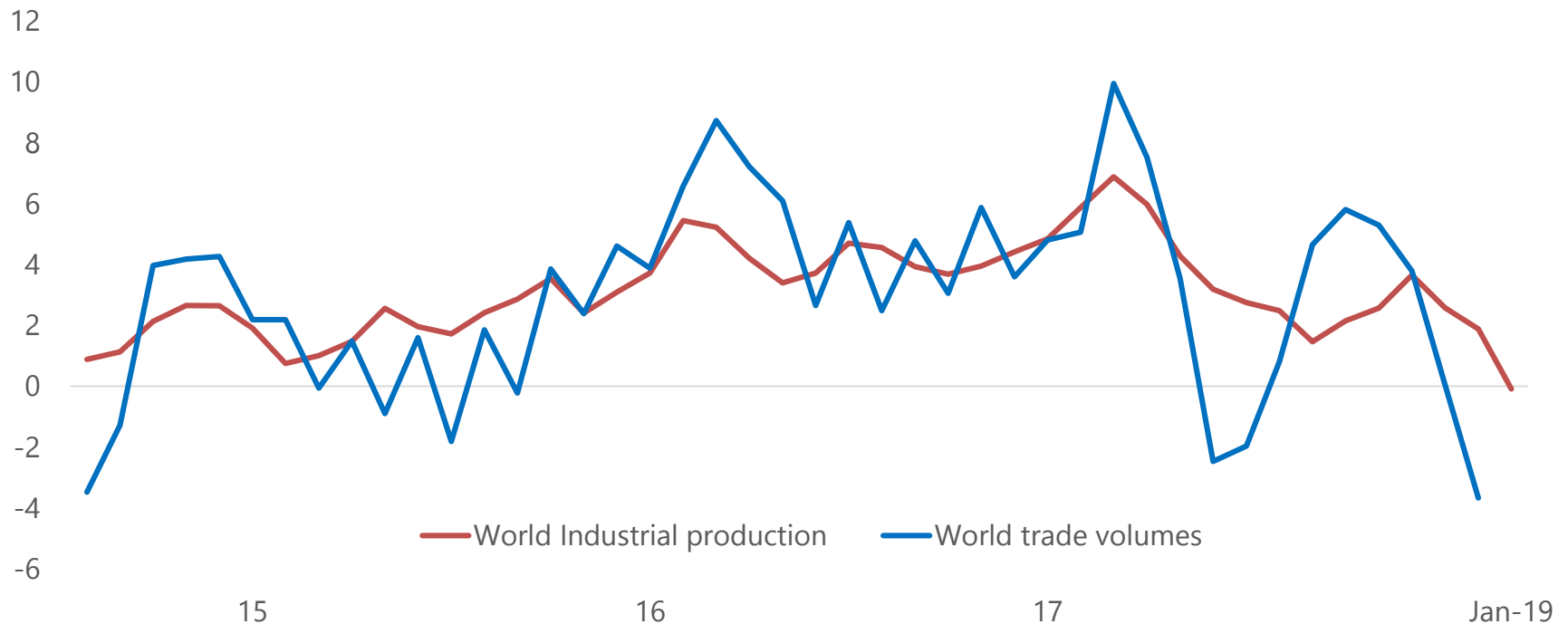


Sources: IMF IFS, Haver analytics, IMF staff calculations.

## Slowing trade and industrial production

### World trade and industrial production

Three-month moving average; annualized percent change

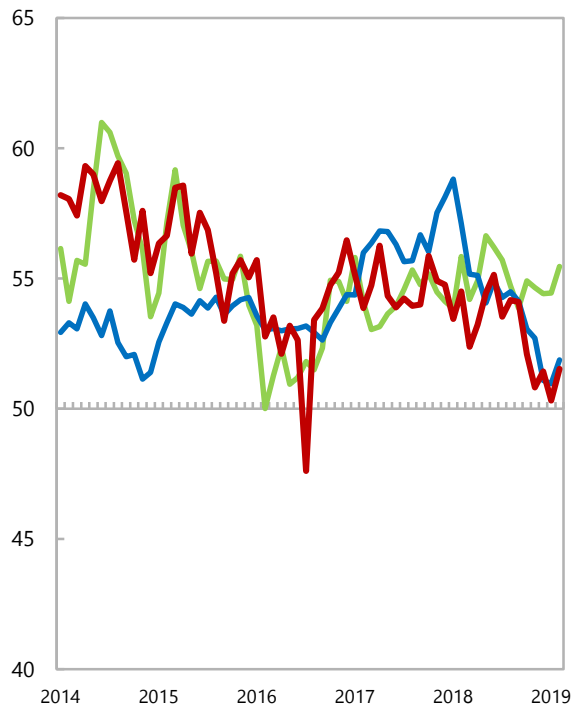


Sources: Haver analytics, CPB, IMF staff calculations.

## Market indicators show a softer momentum

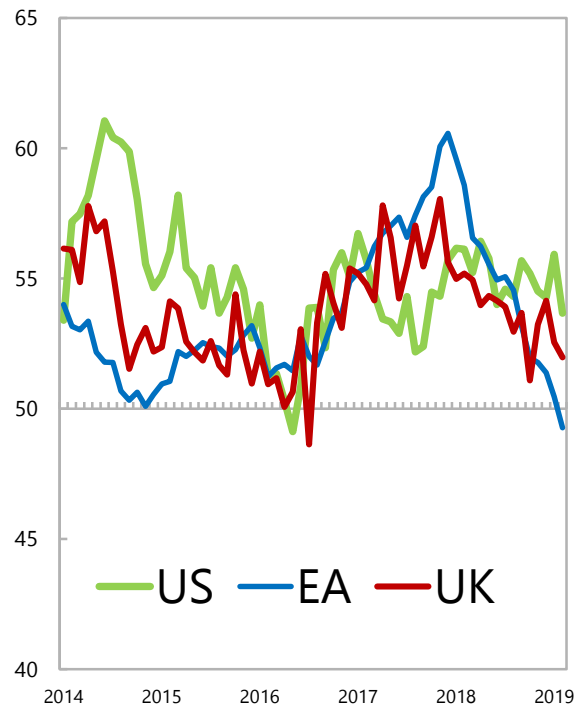
### Composite PMIs

>50 = expansion, sa



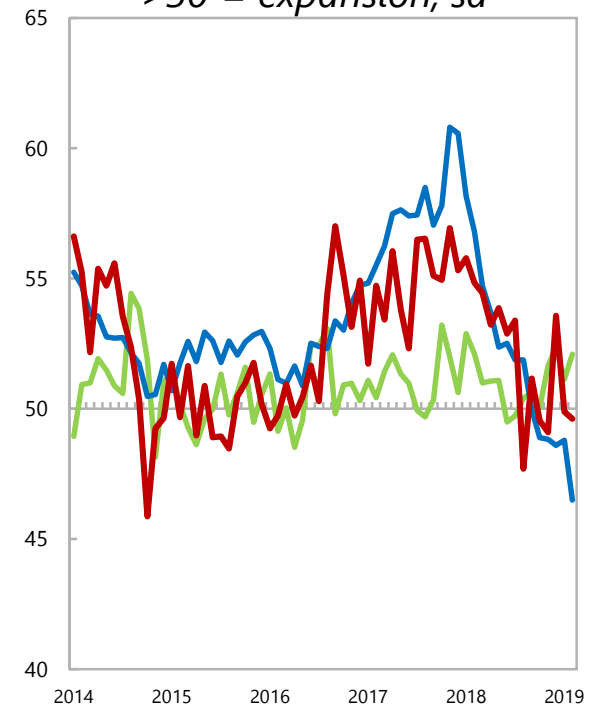
### Manufacturing PMIs

>50 = expansion, sa



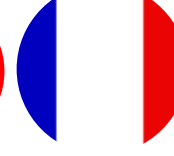
### Manufacturing PMIs export orders

>50 = expansion, sa



Sources: Haver analytics, Markit, IMF staff calculations.

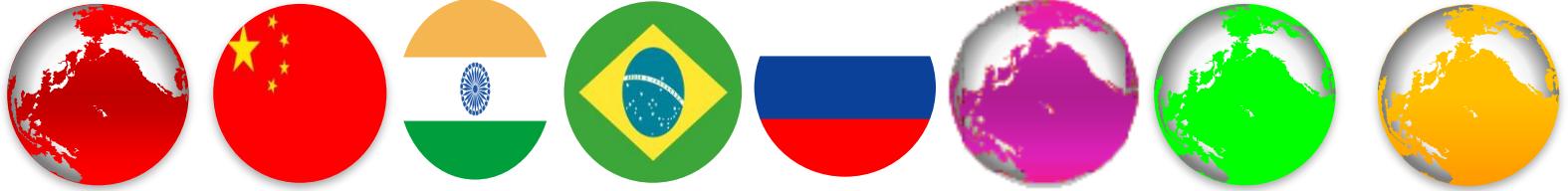
# Advanced economies



	World	Advanced Economies	U.S.	U.K.	Japan	Euro Area	Germany	France	Spain
<b>2018</b>	<b>3.7</b>	<b>2.3</b>	<b>2.9</b>	<b>1.4</b>	<b>0.9</b>	<b>1.8</b>	<b>1.5</b>	<b>1.5</b>	<b>2.5</b>
<b>2019</b>	<b>3.5</b>	<b>2.0</b>	<b>2.5</b>	<b>1.5</b>	<b>1.1</b>	<b>1.6</b>	<b>1.3</b>	<b>1.5</b>	<b>2.2</b>
Revision from Oct. 2018	-0.2	-0.1	0.0	0.0	0.2	-0.3	-0.6	-0.1	0.0
<b>2020</b>	<b>3.6</b>	<b>1.7</b>	<b>1.8</b>	<b>1.6</b>	<b>0.5</b>	<b>1.7</b>	<b>1.6</b>	<b>1.6</b>	<b>1.9</b>
Revision from Oct. 2018	-0.1	0.0	0.0	0.1	0.2	0.0	0.0	0.0	0.0

Sources: IMF, *World Economic Outlook* January 2019 update.

# Emerging economies



	Emerging Market and Developing Economies	China	India	Brazil	Russia	ASEAN-5	Middle East, North Africa, Afghanistan, Pakistan	Low Income Developing Countries
<b>2018</b>	<b>4.6</b>	<b>6.6</b>	<b>7.3</b>	<b>1.3</b>	<b>1.7</b>	<b>5.2</b>	<b>2.4</b>	<b>4.6</b>
<b>2019</b>	<b>4.5</b>	<b>6.2</b>	<b>7.5</b>	<b>2.5</b>	<b>1.6</b>	<b>5.1</b>	<b>2.4</b>	<b>5.1</b>
Revision from Oct. 2018	<b>-0.2</b>	0.0	0.1	0.1	-0.2	-0.1	-0.3	-0.1
<b>2020</b>	<b>4.9</b>	<b>6.2</b>	<b>7.7</b>	<b>2.2</b>	<b>1.7</b>	<b>5.2</b>	<b>3.0</b>	<b>5.1</b>
Revision from Oct. 2018	0.0	0.0	0.0	-0.1	-0.1	0.0	0.0	-0.2

Sources: IMF, *World Economic Outlook* January 2019 update.



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**Risks to the outlook are tilted to the downside**

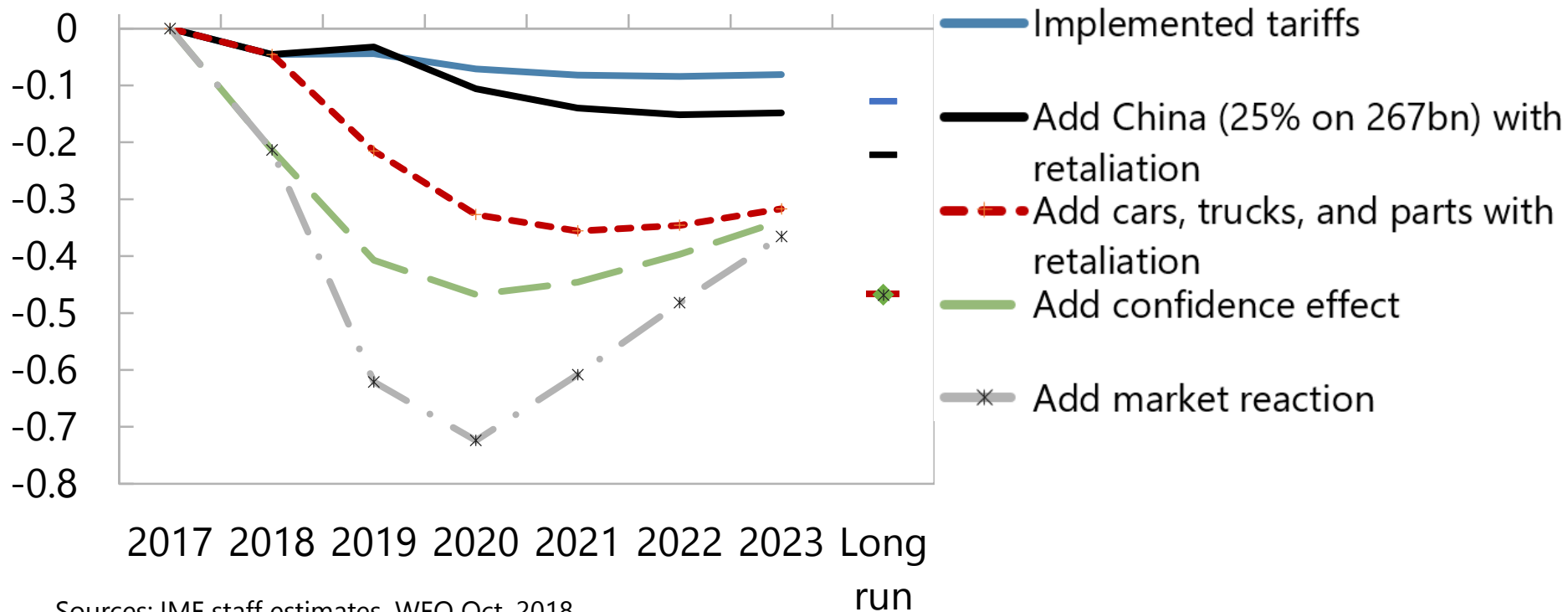
## **Immediate risks include:**

- **An escalation of trade tensions**
- **Sharper slowdown in China**
- **A no deal Brexit**
- **Renew market uncertainties**
- **Political discontents (e.g. Gilets Jaunes)**

## Escalation of trade tensions

### G20 Advanced Economies

Real GDP in trade tensions scenarios

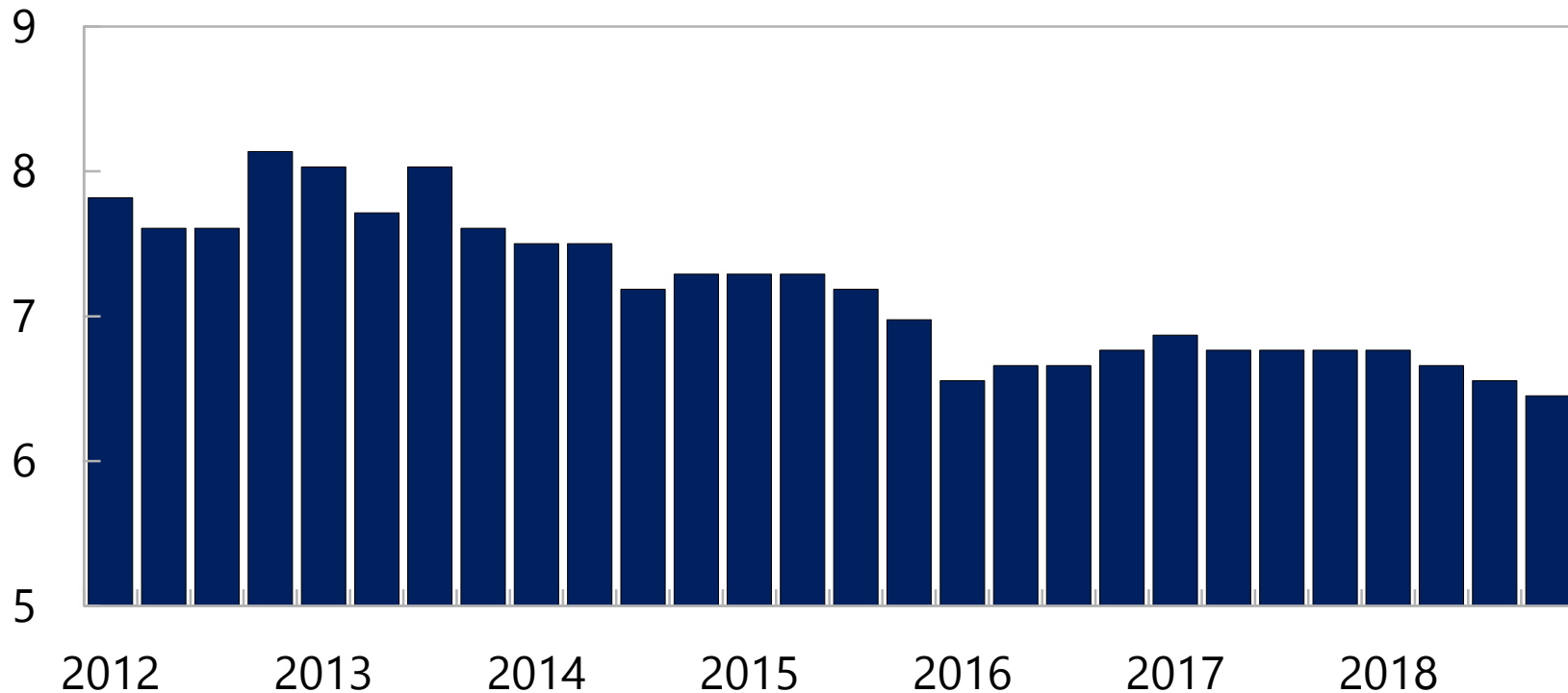


Sources: IMF staff estimates, WEO Oct. 2018.

## Slowing demand in China under the impact of trade sanctions

### China GDP growth

Quarterly, y/y percent change, sa

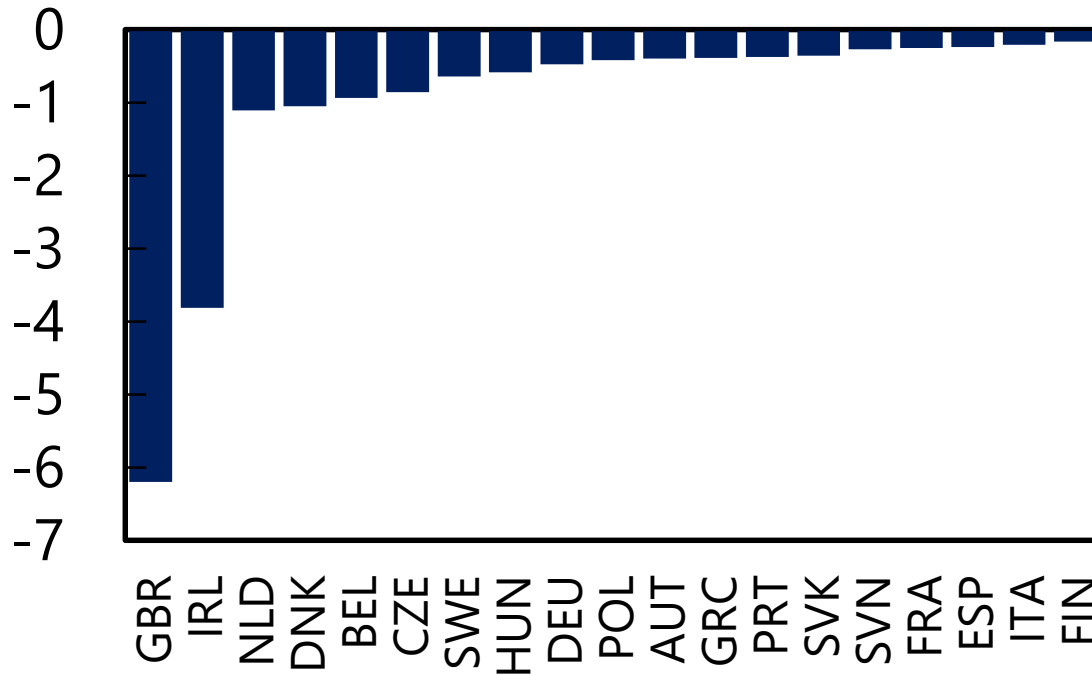


Sources: China NBS, IMF staff estimates.

## A no-deal Brexit would be costly

### Long-Term Impact of Brexit: WTO scenario

(Decline in the level of output compared to a non-Brexit scenario;  
In percent)



### Short term risks

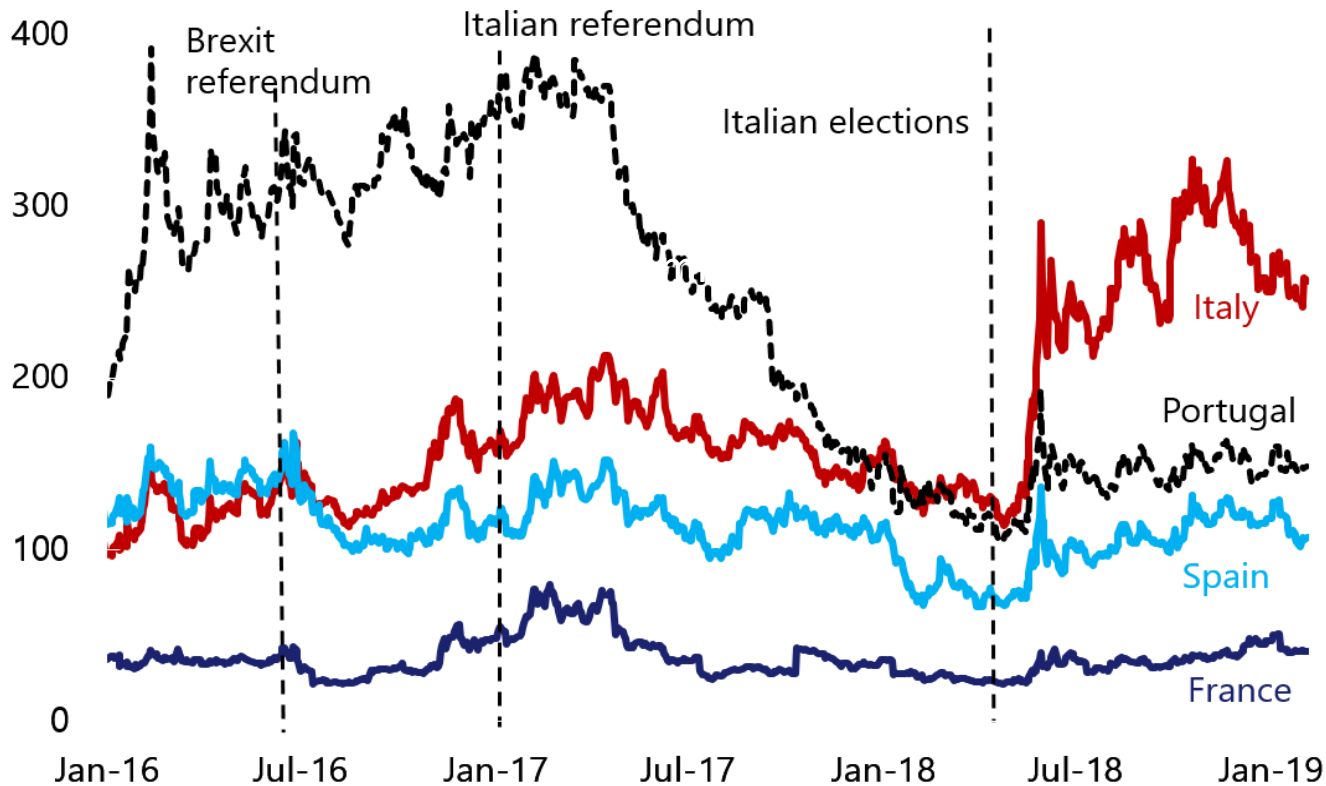
- **Widespread disruptions of production**
- **Decline in confidence**
- **Financial volatility and asset prices decline**

Source: IMF staff estimates.

## Market confidence: Italian spreads remain elevated

### 10-Year Government Bond Yield Spread

(Versus Bunds, basis points)

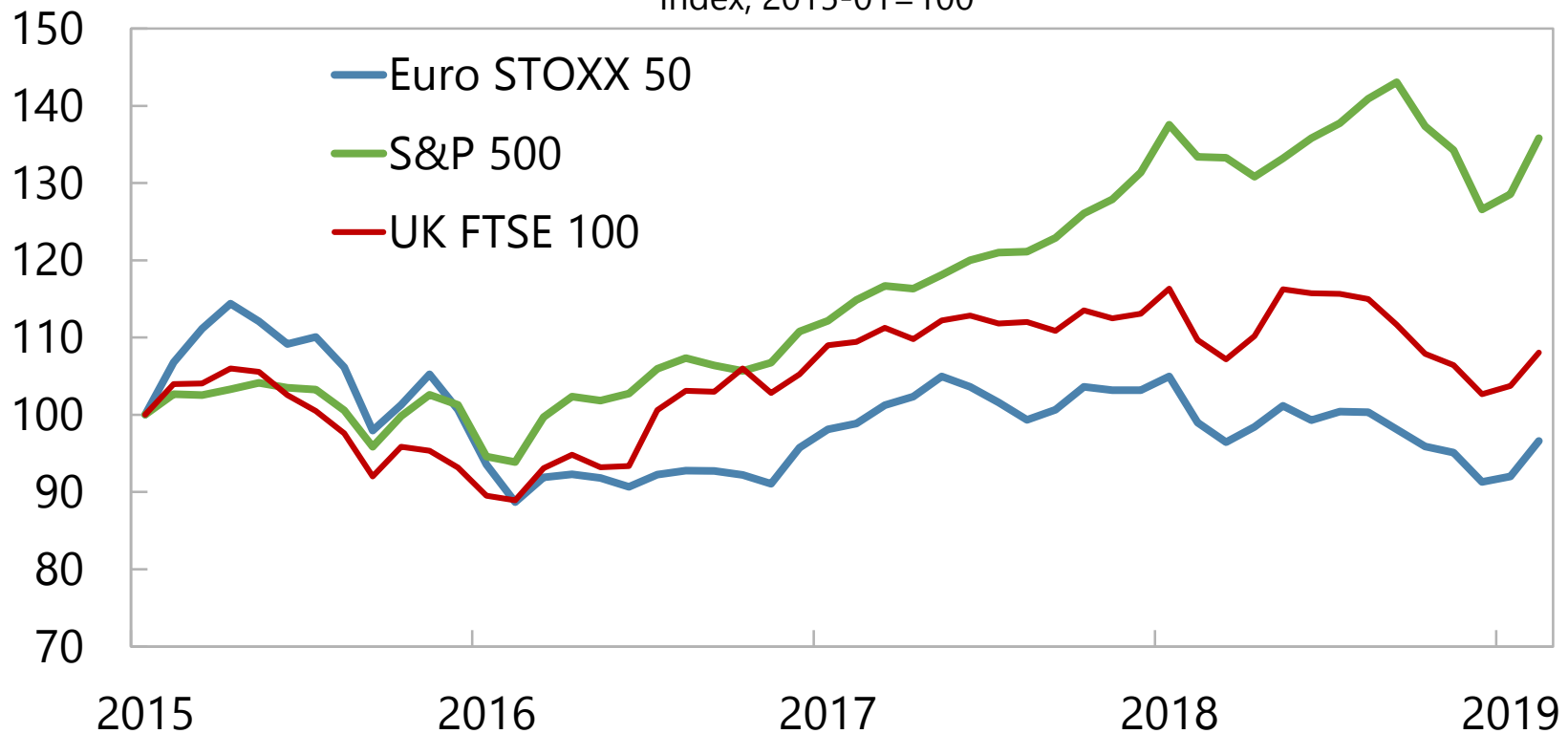


Sources: Bloomberg Finance L.P.

## Financial markets have weakened

### Equity markets

Index, 2015-01=100

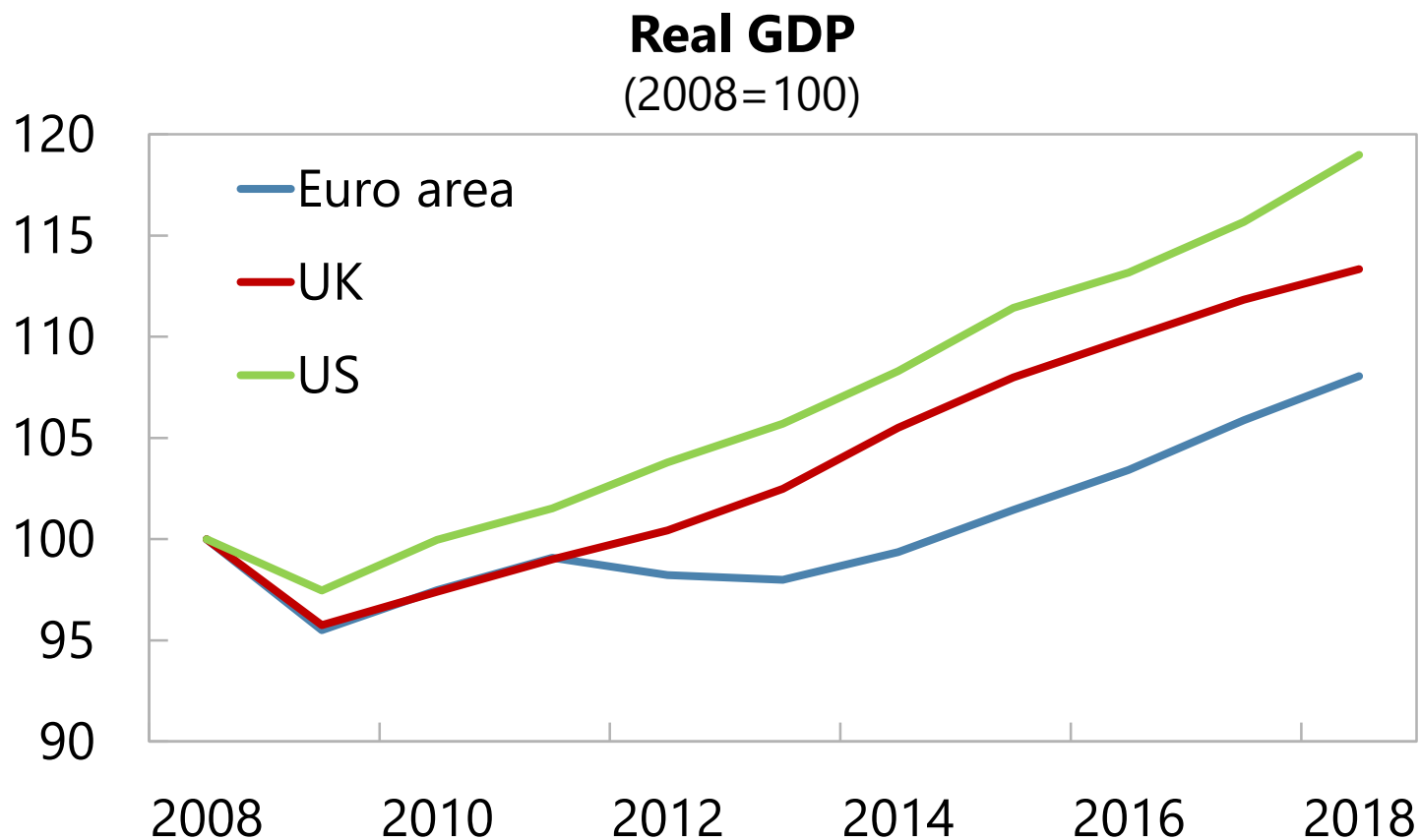


Sources: Haver analytics, Markit, IMF staff calculations.

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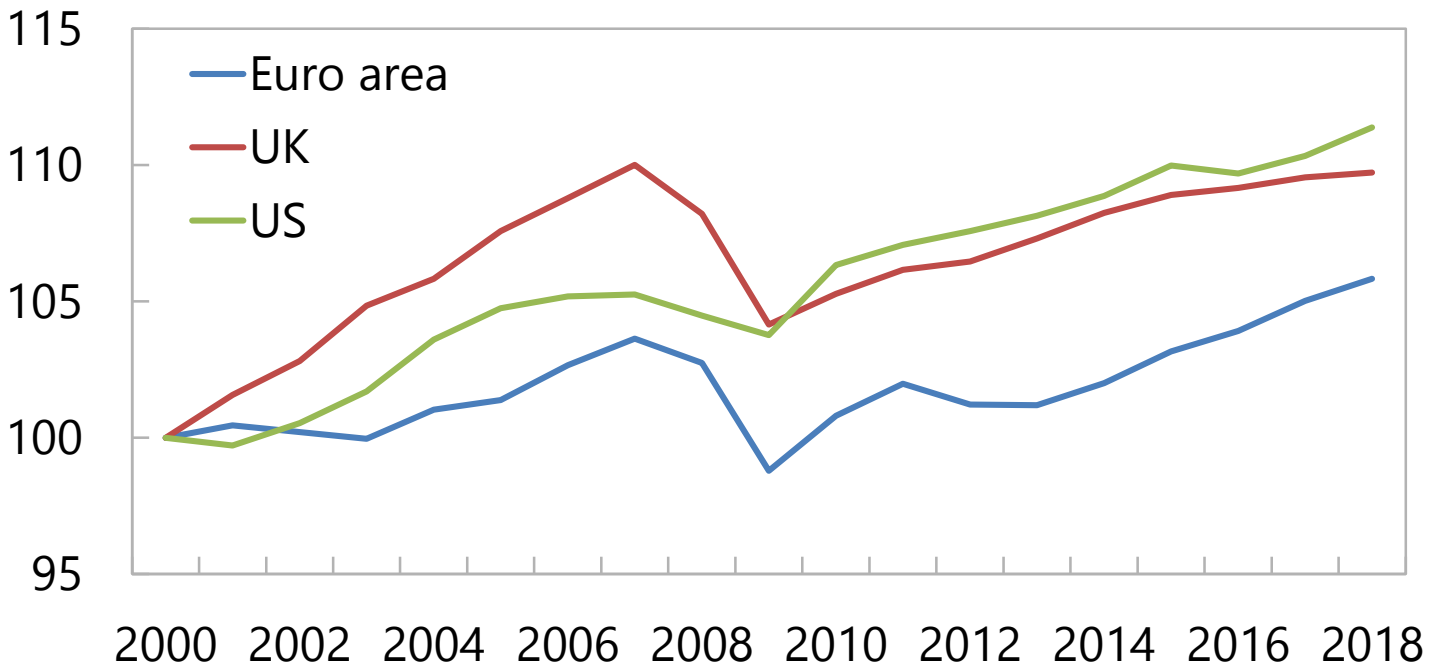
## Euro area recovery has been slower



Sources: IMF WEO, IMF staff estimates.

## Productivity gaps is widening relative to the U.S. ...

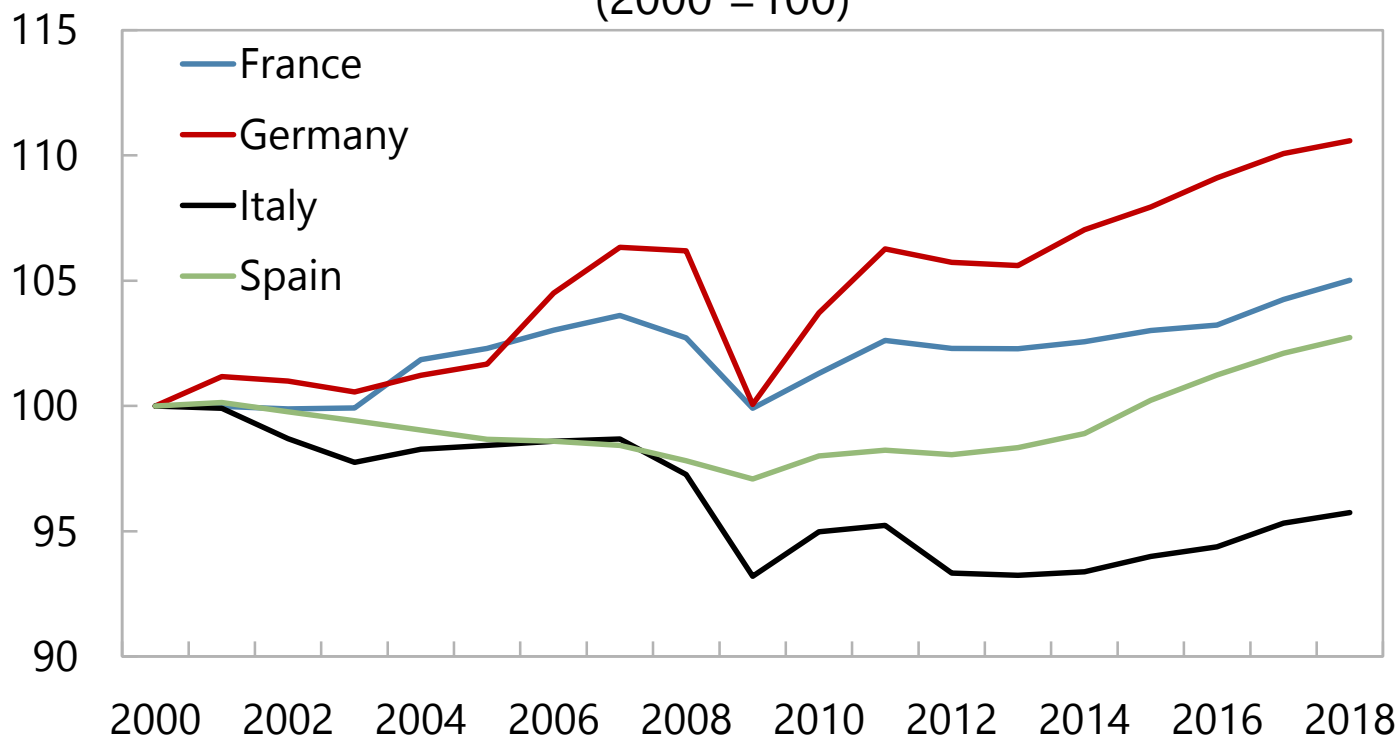
**Total factor productivity**  
(2000 = 100)



Sources: European Commission, AMECO.

## ... and within the euro area

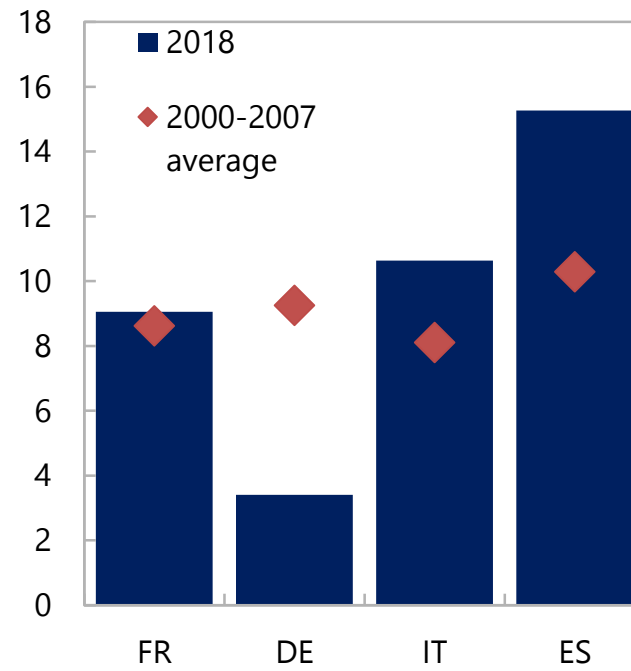
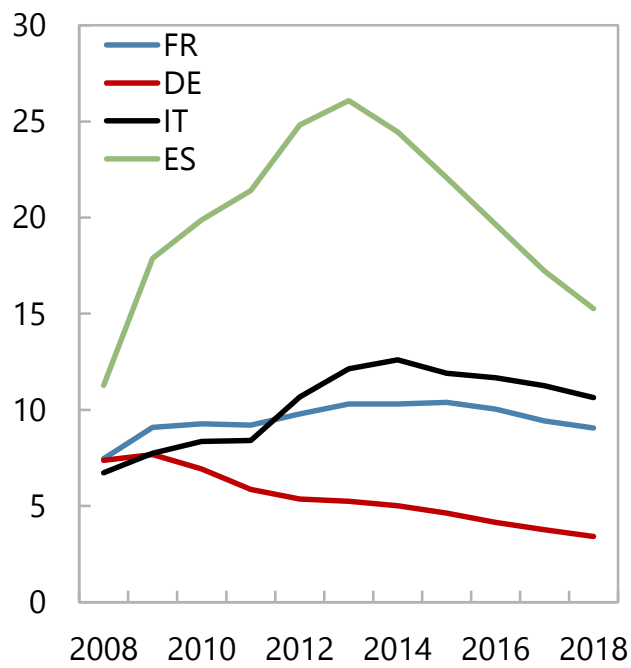
### Total factor productivity (2000 = 100)



Sources: European Commission, AMECO.

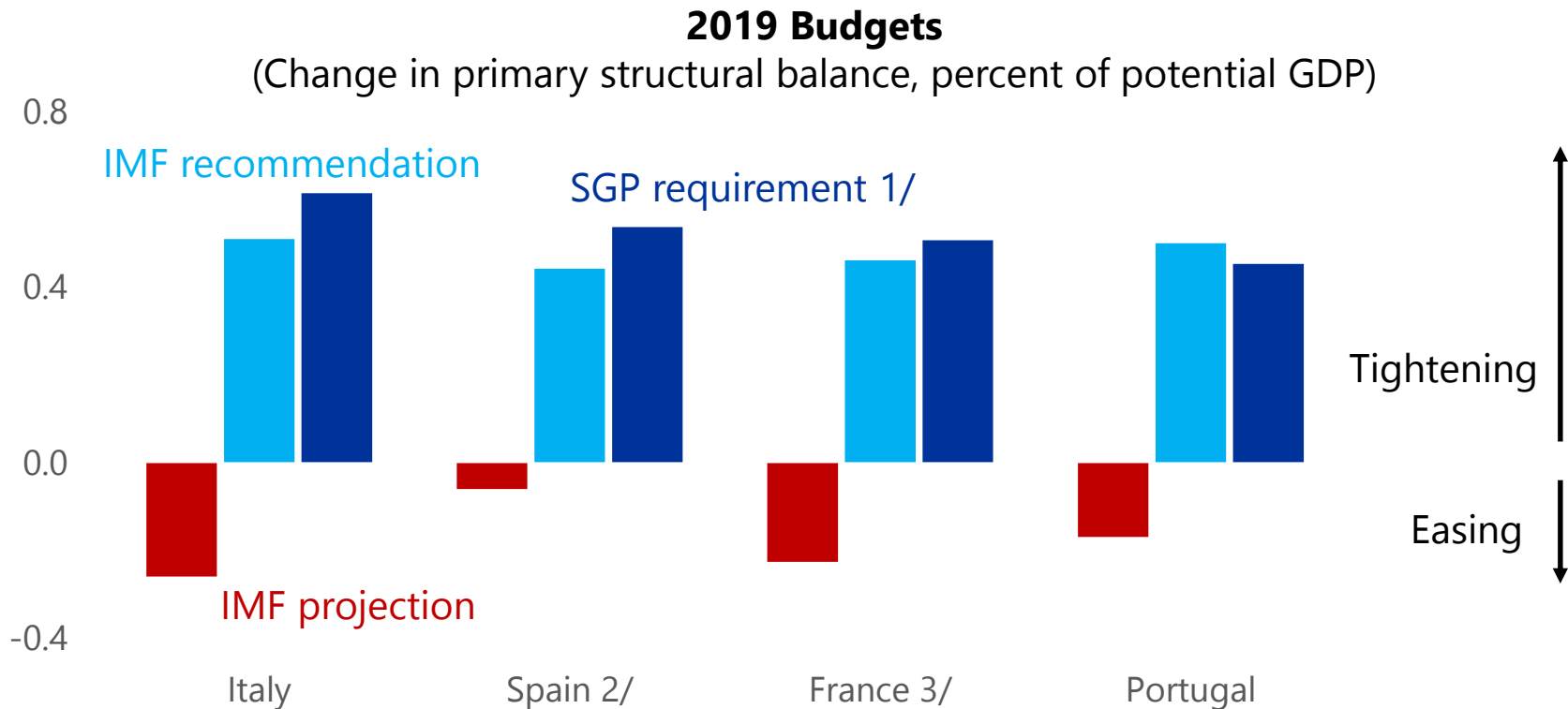
## Unemployment rates are now closer to their pre-crisis level but remain elevated

### Unemployment rate (Percent)



Sources: Eurostat.

## Little consolidation is planned in 2019...



Sources: WEO and country authorities.

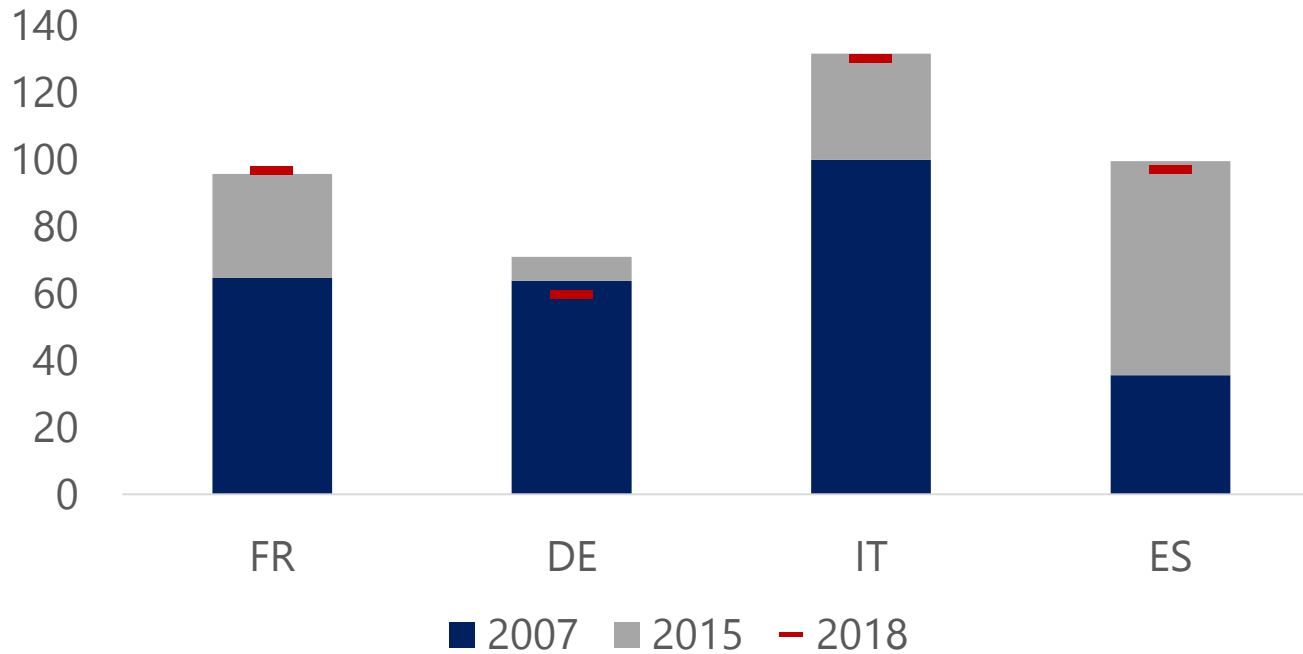
1/ SGP requirement on the structural balance is adjusted for the change of interest expenses to translate it into the primary structural balance.

2/ The IMF projection assumes the extension of the 2018 budget and already legislated measures.

3/ This corresponds to the average for 2019-20. The IMF projection is based on legislated and identified measures only.

## ... in an environment of high debt

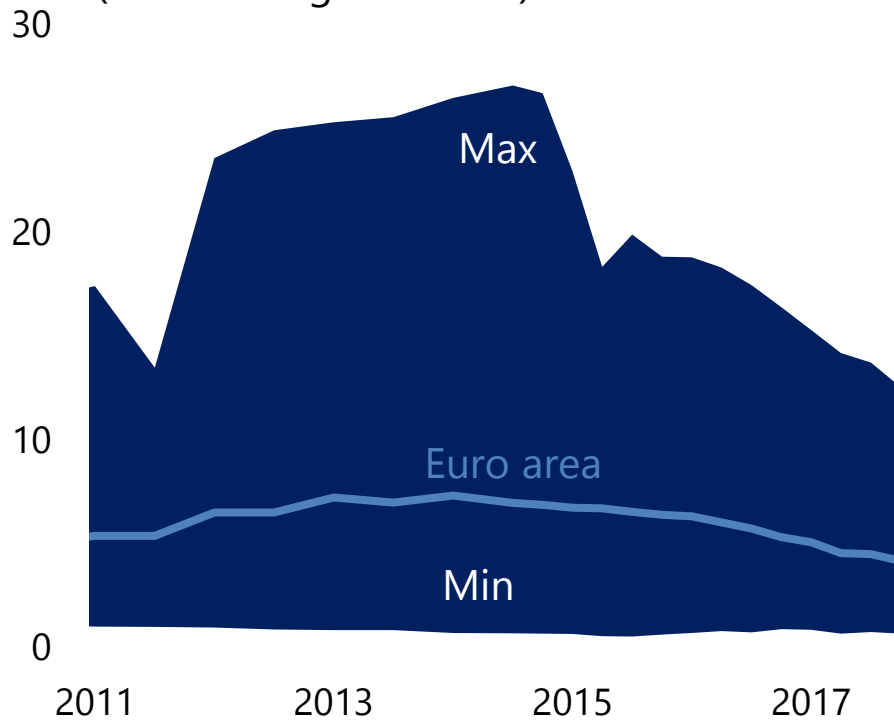
### Gross public debt Percent of GDP



Sources: IMF WEO, IMF staff estimates.

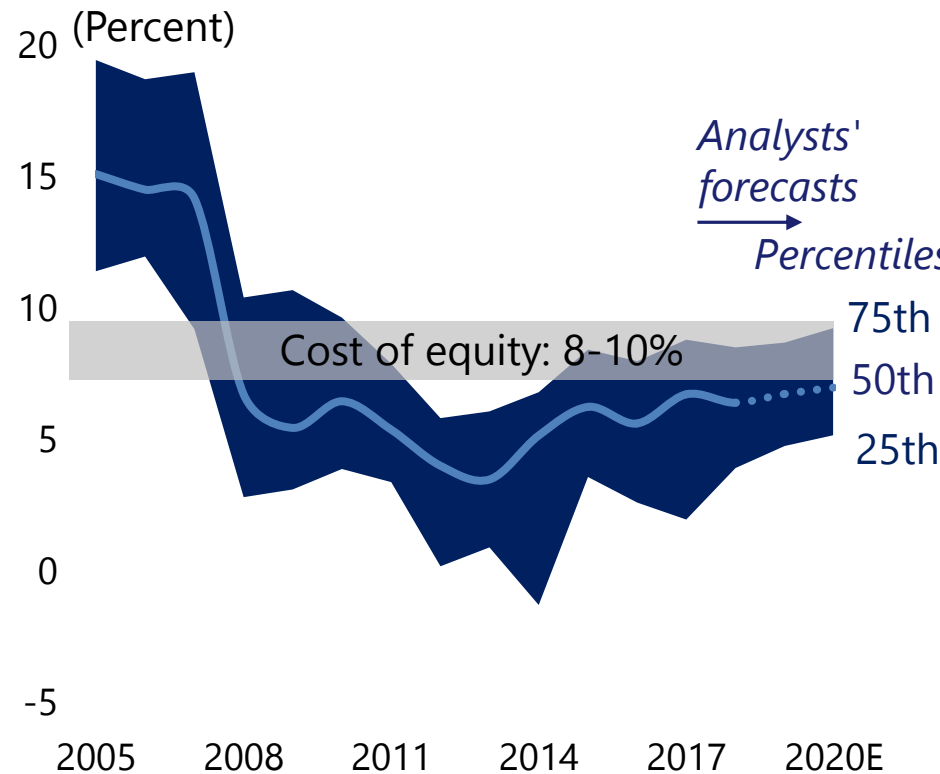
## The health of banks is improving but risks remain

**Non-Performing Loans**  
(Percent of gross loans)



Note: Cyprus and Greece excluded.  
Source: ECB.

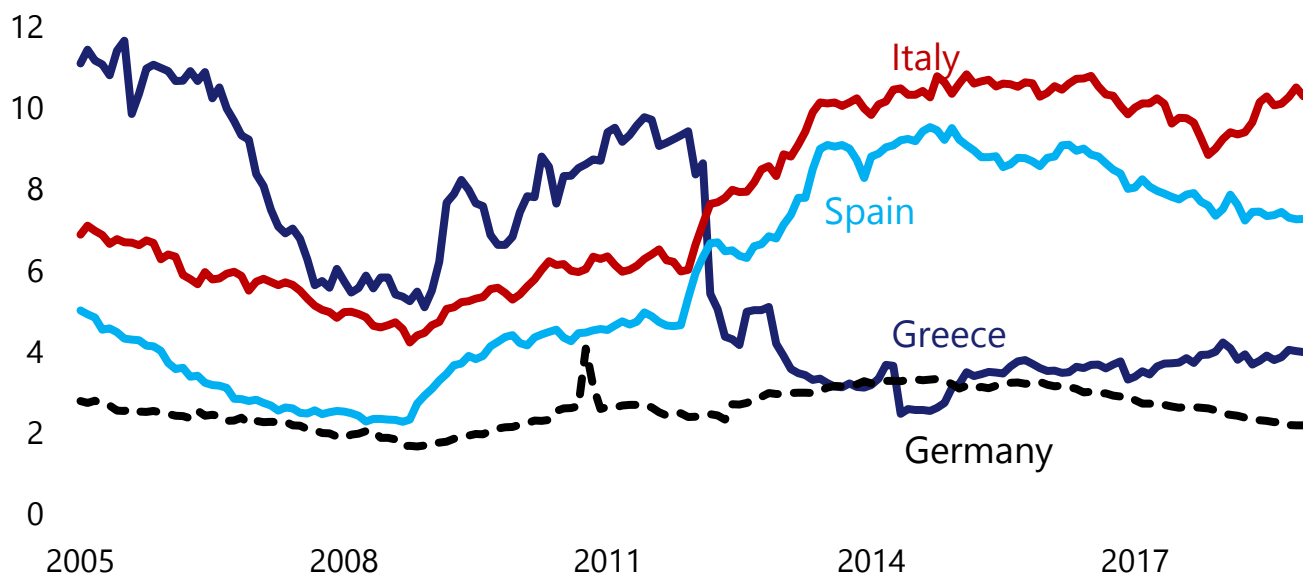
**Return on Equity**



Note: The ROEs are average of 100 largest banks.  
Sources: Bloomberg Finance L.P., Fitch; and IMF staff calculations.

## Strong bank-sovereign links leave no room for complacency

### Bank Holdings of Domestic Sovereign Bonds (Percent of bank assets)



Source: ECB.



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## Multilateral cooperation is needed!

### Trade

- Deescalate tensions
- Address sources of dissatisfaction with the rules based trading system
- Limit disruptions related to Brexit

### More cooperation

- Financial regulatory reform
- International taxation to avoid tax evasion
- Building a financial safety net
- Mitigating and adapting to climate change

# Policy priorities

## Structural reforms to boost productivity

→ **Country-specific structural reforms to enhance resilience and boost productivity growth** (product and labor markets; business environment)

→ **Strengthen EU reform governance** (benchmarking; fiscal incentives; coordination)

# Policy priorities

## Sound fiscal policies and shock insurance

→ **National fiscal policies towards reduction of imbalances**

→ **Simplified, enforceable EU fiscal rules**

→ Support macroeconomic stabilization through a **Central Fiscal Capacity**

## More robust and integrated financial sector

→ **Complete the Banking Union** (operationalize the SRF backstop; EDIS)

→ **Continue to repair balance sheets** (reduce NPLs)

→ **Build a European Capital Markets Union**



# Thank You!

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