Ministero dell'Economia e delle Finanze

Dipartimento del Tesoro

Facing the aftermath
Which reforms to rebalance the world growth?

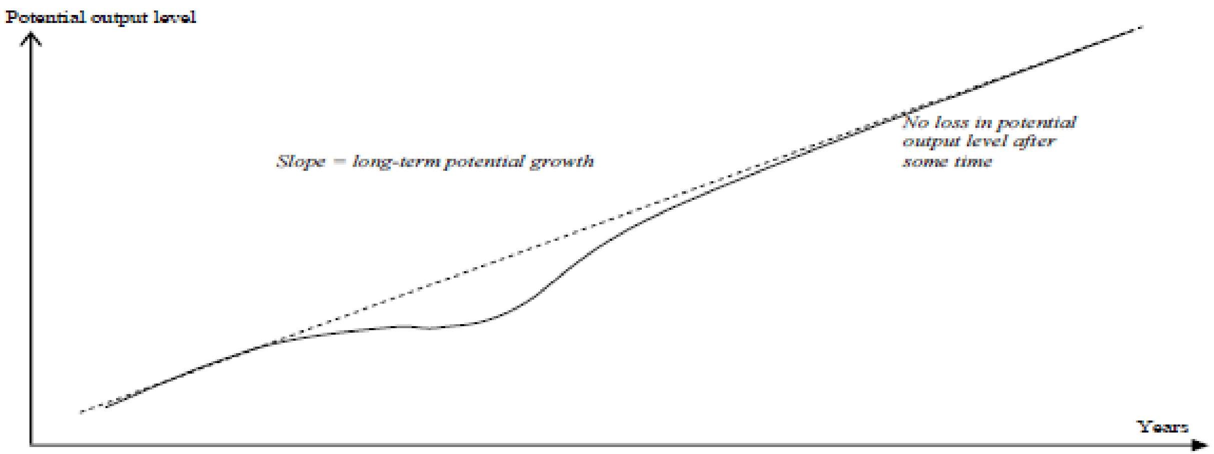
Asia Europe Economic Forum, Tokyo

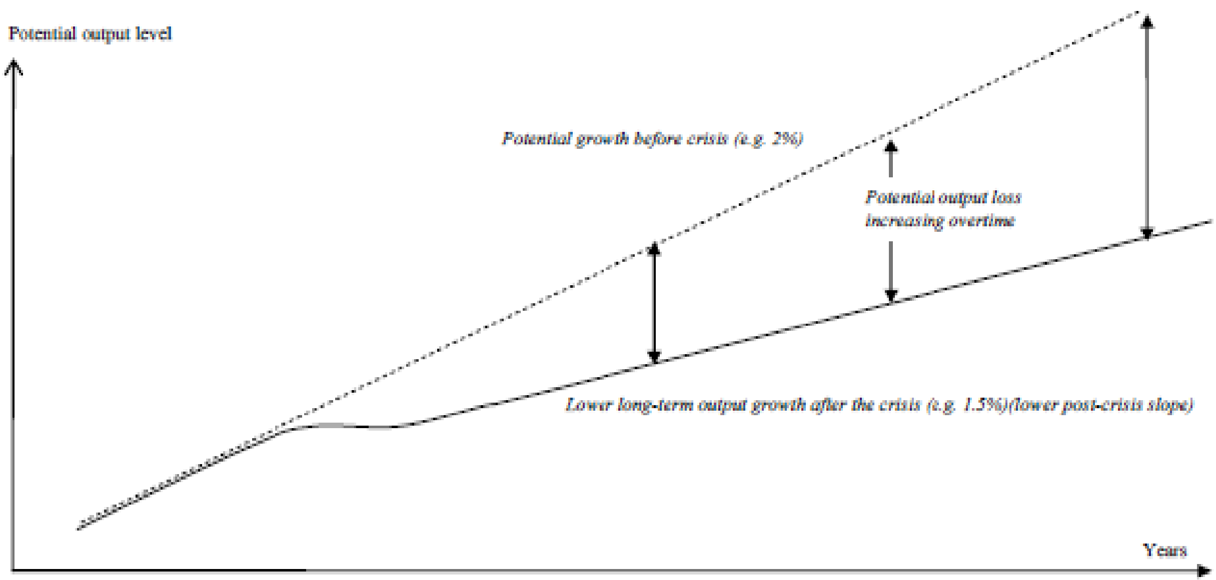
March 24-25, 2010

Lorenzo Codogno

Italy's Ministry of Economy and Finance (MEF)
Department of the Treasury, Economic and Financial Analysis and Planning

Uncertainty on the future path of GDP growth





- Optimistic scenario: no loss in potential output in the medium term.
- Pessimistic scenario: loss in potential output increasing over time.
- Middle-range scenario: loss in potential output only partly recovered

The international policy response to the crisis

- The international response to the crisis: impressive degree of coordination by historical standards both at monetary and fiscal policy level.

- Monetary policy:

  (i) measures to ensure the consistency between market rate and the policy rate;

  (ii) initiatives to alleviate strains in wholesale interbank markets.

The international policy response to the crisis (cont'd)

- The financial sector rescue:

  (i) Measures to facilitate access to more permanent sources of funding.

  (ii) Short-term measures to maintain an adequate functioning of credit market to support the real economy recovery.

- Real economy: fiscal stimulus packages have been mainly based on significant increase of public expenditure and to less extent on tax cuts.

Anti-crisis measures at EU level (EU budget)

- 3T's approach: Temporary, Targeted, Timely.
- The response at Community-level to the crisis has been rapid, relatively flexible and sizeable (0,3 of EU GDP financed by the EU budget).
- Measures aimed at boosting infrastructure development; retraining people and supporting social cohesion (European Social Fund); supporting workers who lost their jobs in 2009 (European Globalisation Adjustment Fund).

Anti-crisis measures at Member States' level

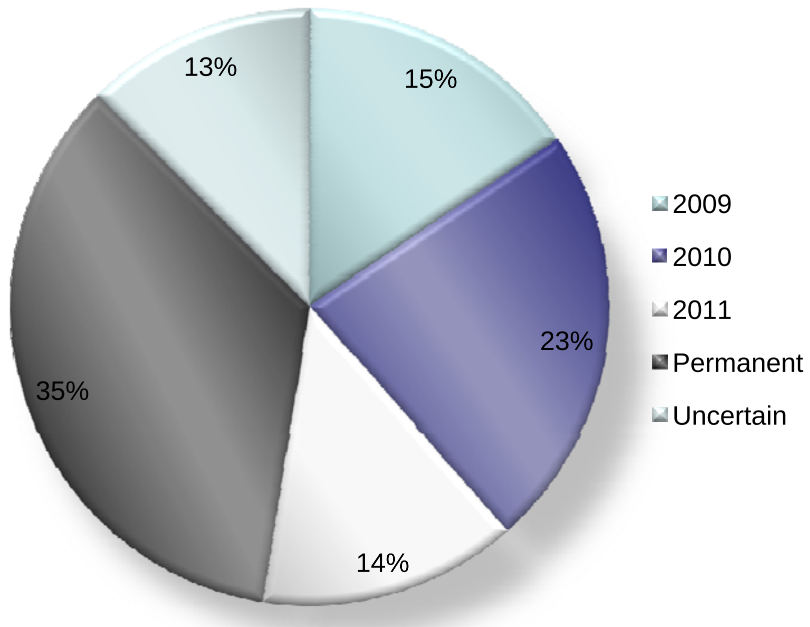
- The size of stimulus packages differs across countries, reflecting their individual initial macroeconomic and fiscal positions, with total recovery measures taken or planned amounting to 2.7% of GDP for 2009-2010 vs. 2008 (1.2% of GDP in the EERP endorsed in December 2008).

- Largely in line with EERP principles (3T's approach), recovery measures have mostly been timely, well targeted and temporary.

Four principles for an exit strategy in the EU

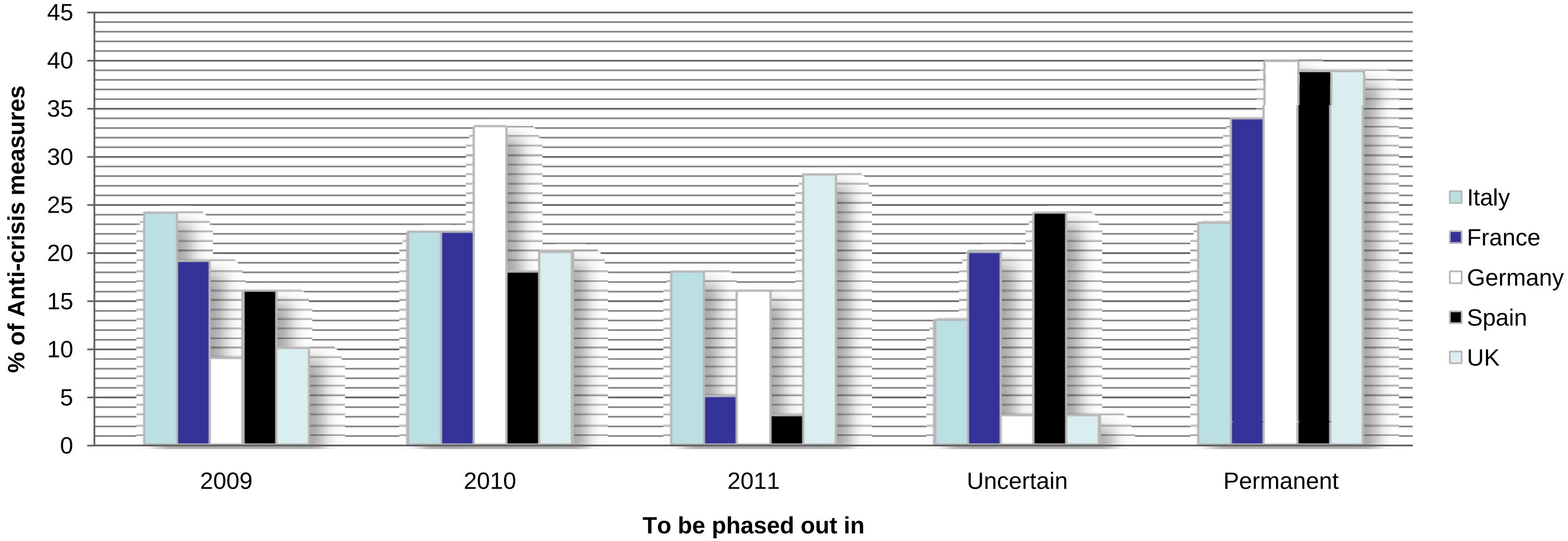
- Sectoral support measures should be phased out as quickly as possible given their distortive effect on the internal market.
- Labour market support measures should be gradually withdrawn when the recovery is secured.
- The withdrawal of schemes to ease financing constraints should depend on the capacity of financial institutions to supply adequate credit.
- The permanent measures adopted during the crisis should be consistent with fiscal consolidation strategies and the Lisbon reform agenda (now called Europe 2020).

Phasing out of anti-crisis measures in Europe



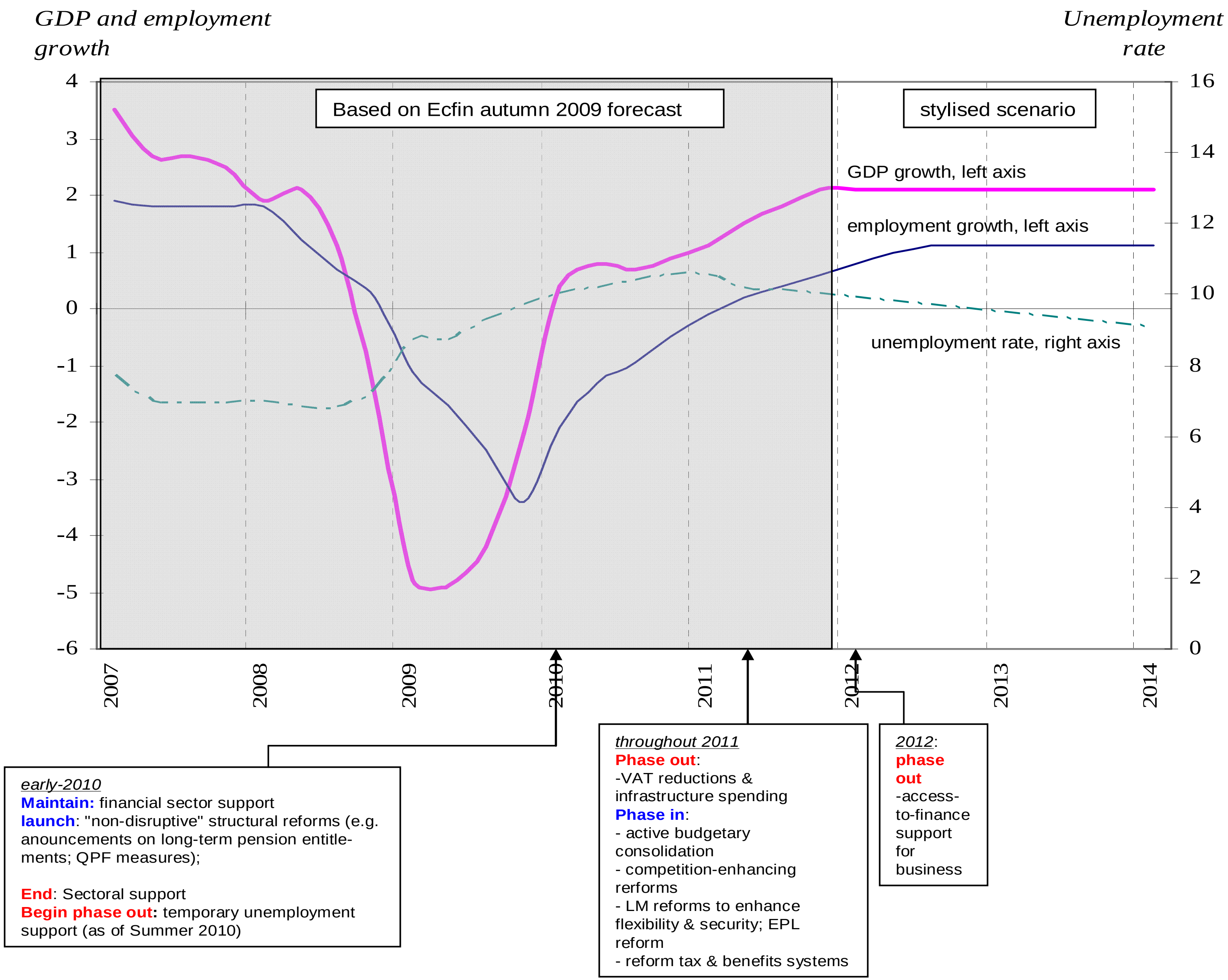
- Most of temporary measures (52%) have explicit sunset clauses. But some measures may be more difficult to reverse, such as measures with no sunset clauses (13%) and permanent ones (35%).

Phasing out differs across European Countries



- DE: 33% in 2010, 16% in 2011, although 40% are permanent.
- IT: 24% of temporary measures expired in 2009, 22% in 2010.
- UK: measures to be withdrawn in 2010 (20%) and 2011 (28%).
- FR: no clear sunset for 20% of measures, 39% are permanent.
- SP: 24% with no clear sunset, 39% permanent.

EXIT STRATEGY



OECD recommendations for EU reforms

On product market	On labour market	On financial market
Reducing anti-competitive product market regulations	Reducing Labour taxes	Strengthening regulatory framework
Increasing the use of price instruments in green growth policies	Increasing the use of active labour market policies (flexicurity, training, re-skilling)	Preserving benefits from competition in terms of access to and price of financial services

IMF recommendations for reforms

Reforms of pension and health entitlements	Containment of other spending	Increase tax revenues	Privatisation
Avoiding a rise in entitlements spending as a share of GDP	Improving expenditure priorization	Reducing or eliminating special treatments	Divesting government assets
Increasing the retirement age	Eliminating energy subsidies	Combating fiscal evasion and avoidance	Reducing the size of the government in the economy
Finding other sources of finance	Protecting the poor and the unemployed	Increasing carbon pricing or auctioned emissions rights	

A post-Lisbon growth and jobs strategy

- The Lisbon Strategy, set out by the European Council in Lisbon in March 2000, has been able to only partly achieve its goals.
- The new reform strategy “Europe 2020” has been discussed by EU leaders on 11 February 2010.
- The first priority must be to hasten the exit from the crisis, but the strategy must also provide the building blocks for a future "smart, sustainable, inclusive growth”, through enhanced policy coordination at EU and national level.
- 5 targets for the strategy.

Europe 2020 flagship initiatives

Smart Growth

Innovation

✓ **3%** of EU'GDP reinvested in **R & D**

Education

✓ share of **early school leavers** under **10 %**

✓ at least **40 %** of the younger generation with a **tertiary degree**

Digital Society

✓ **Smart growth**: developing an economy based on knowledge and innovation.

Sustainable Growth

Climate and energy

✓ fulfilment of the **20/20/20 climate/energy targets**

✓ an increase to **30 %** of emission reduction if feasibile

Competitiveness

✓ **Sustainable growth**: promoting a more resource efficient, greener and more competitive economy

Inclusive Growth

Employment and Skills

✓ employment **of 75 % of population aged 20-64**

✓ **Inclusive growth**: fostering a high-employment economy delivering social and territorial cohesion

Fighting poverty

✓ **20 million less** people should be at risk of poverty

Single Market for globalisation era

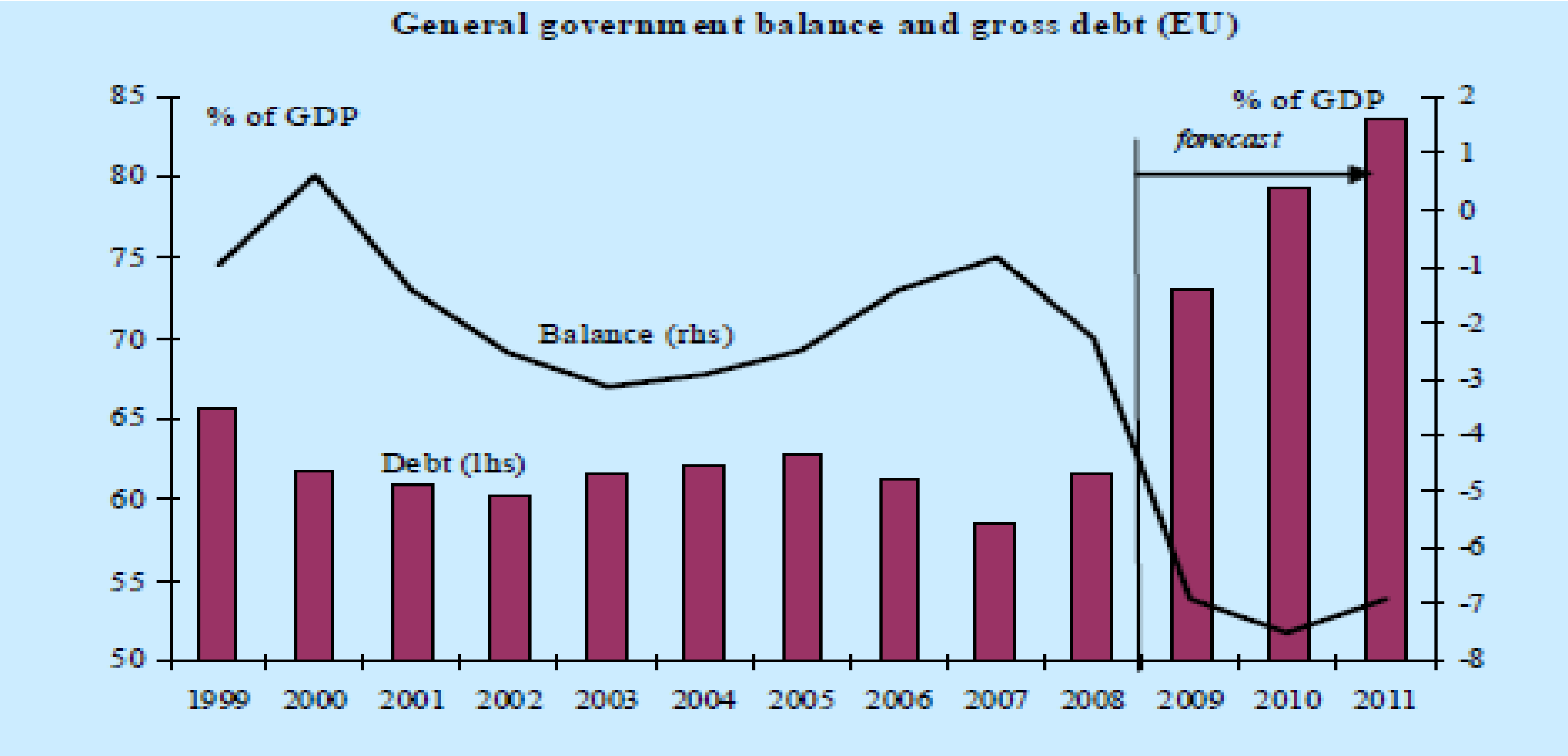
Financing Europe 2020

External Economic Policy

Europe 2020 governance

Overall Institutional structure	**Integrated Guidelines** establishing scope and policy priorities, including **headline targets** for the EU27 to reach by 2020 and to be translated into national targets.	
Delivery	**Country reporting *(Treaty-based surveillance)*** **Aim:** help Member States ✓ to define and implement exit strategies ✓ to restore macroeconomic stability, ✓ to return their economies to sustainable growth and public finances. **Approach:** enhanced assessment by the *ECOFIN* of main macro-economic challenges facing Member States taking account of spillovers across Member States and policy areas. **Instruments:** ✓ reporting by the Member States through their stability and convergence programmes, ✓ followed by separate but synchronised recommendations on fiscal policy in SCP Opinions and on macro imbalances and growth bottlenecks in the BEPGs (art. 121.2 of the TFUE).	**Thematic approach *(flagship initiatives)*** **Aim:** deliver headline targets agreed at EU level combining concrete actions at EU and national levels. **Approach:** strategic role of the sectoral Council formations for *implementing flagship initiatives* and monitoring and reviewing progress towards the agreed targets. **Instruments:** ✓ reporting by the Member States through streamlines national reform programmes ✓ including information on growth bottlenecks and progress towards the targets, followed by policy advice at EU level based on transparent evaluation frameworks issued in the form of recommendations under BEPGs (art. 121.2 of the TFUE) and the Employment Guidelines (art. 148 of the TFUE).

The Stability and Growth Pact and Europe 2020



- Fiscal consolidation is a key element for a credible structural reform agenda: Europe 2020 to strengthen fiscal sustainability, in line with the SGP.

An evidence-based approach for structural reforms

Evaluating policy responses

	Performance	Priority	Adequacy of policy response	Recommendations
ANALYSIS	Performance of a Member State in different policy areas relative to other EU countries and/to agreed targets.	Relative priority of a policy area in terms of its potential contribution to growth and jobs in the country concerned	The adequacy of the annual policy response, in terms of its relevance, ambition and credibility	***CSR(s) (or none)***
TOOLS	**Quantitative and qualitative analysis (e.g. LAF, EMCO indicators)**	**Economic and political economy considerations (NRPs, LAF, MACMIC)**	**Criteria of successful reforms** **Application of these criteria**	