



Dipartimento
del Tesoro

Structural Reforms: How to Revive Growth in Asia and in Europe?

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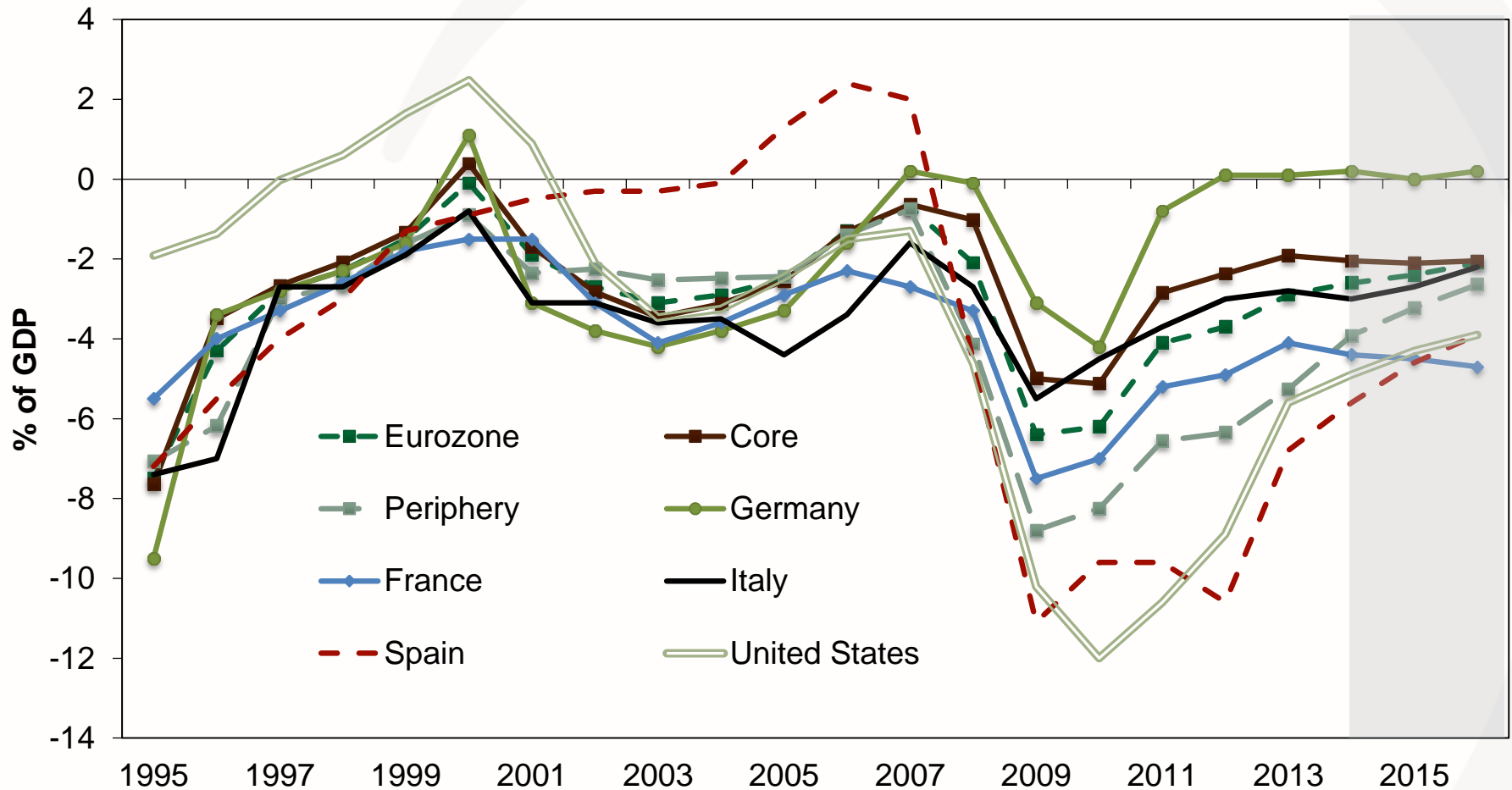
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Have policies worked out six years into the crisis?

- Weakness in **investment activity**.
- Steady decline in **potential growth** almost everywhere.
- High **unemployment**, especially among the youth (but DE).
- Need to absorb **macroeconomic imbalances**.
- Increased **poverty** and reversal of progress towards **social inclusion**, with potential **political risks** (all EA countries).
- Continuing **disinflation** (and risks of de-anchoring expectations and triggering deflation).
- Euro remains too strong for the state of the economy, also due to rising EA **current account surpluses**.

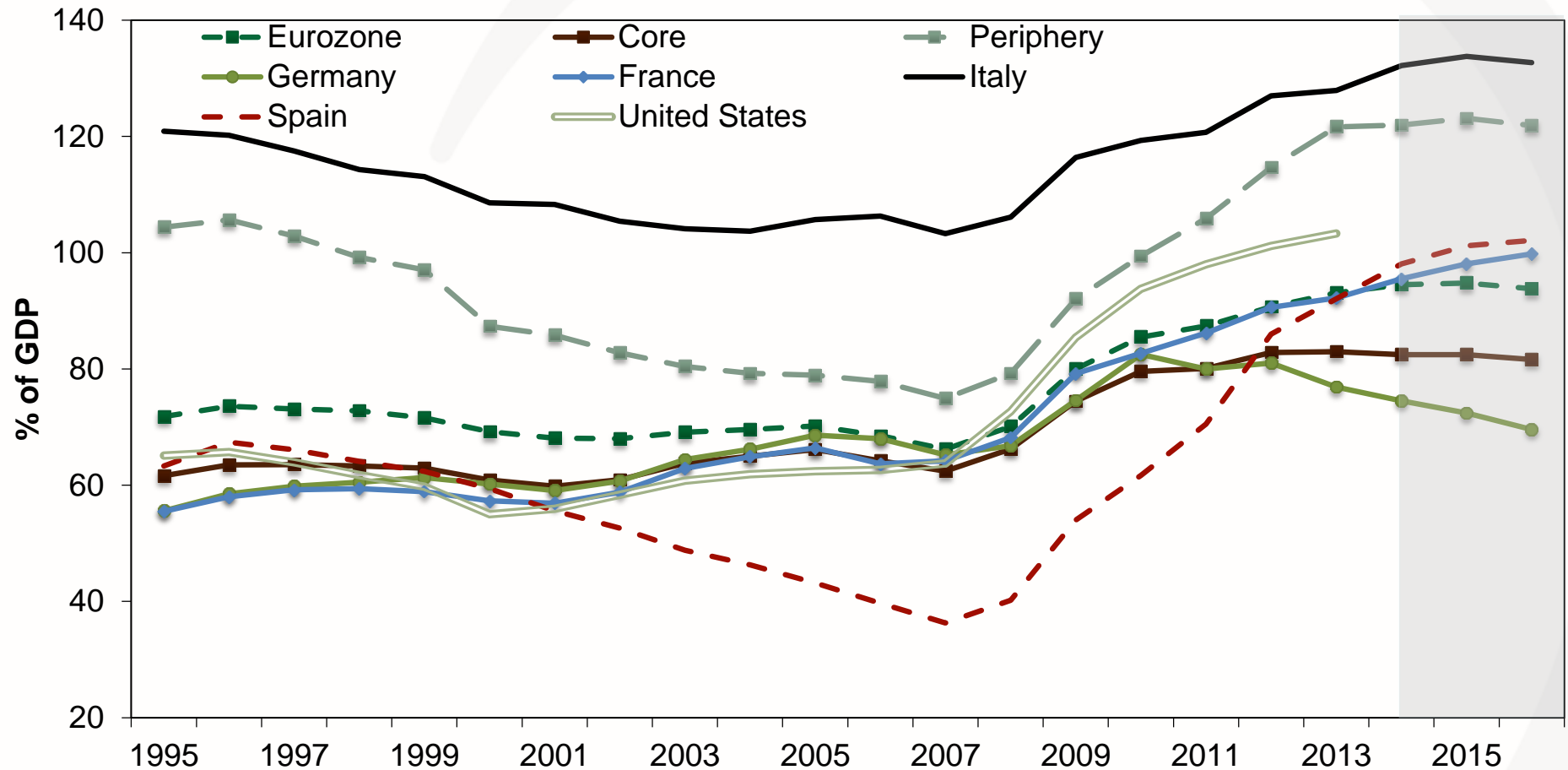
Additional fiscal consolidation is unavoidable



Note: Core Euro area includes Austria, Benelux, Germany, Finland and France. Periphery Euro area includes Greece, Ireland, Italy, Spain and Portugal. Deficit data for Greece are not available for the period 1995-1999.

Source: Eurostat, US Department of the Treasury, Bureau of Economic Analysis, European Commission (forecasts)

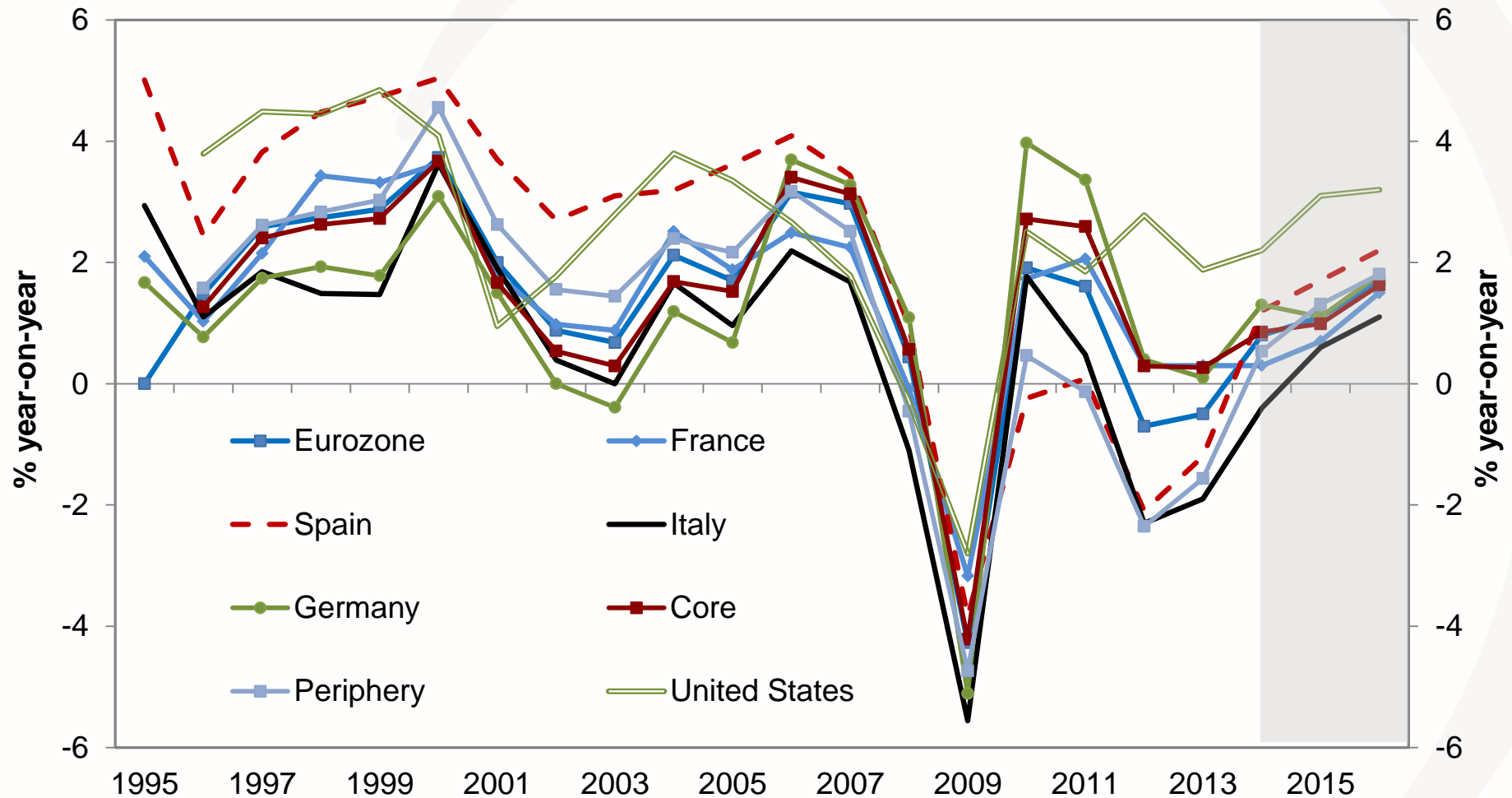
Public debt deleveraging has yet to start



Note: Core Euro area includes Austria, Benelux, Germany, Finland and France. Periphery Euro area includes Greece, Ireland, Italy, Spain and Portugal.

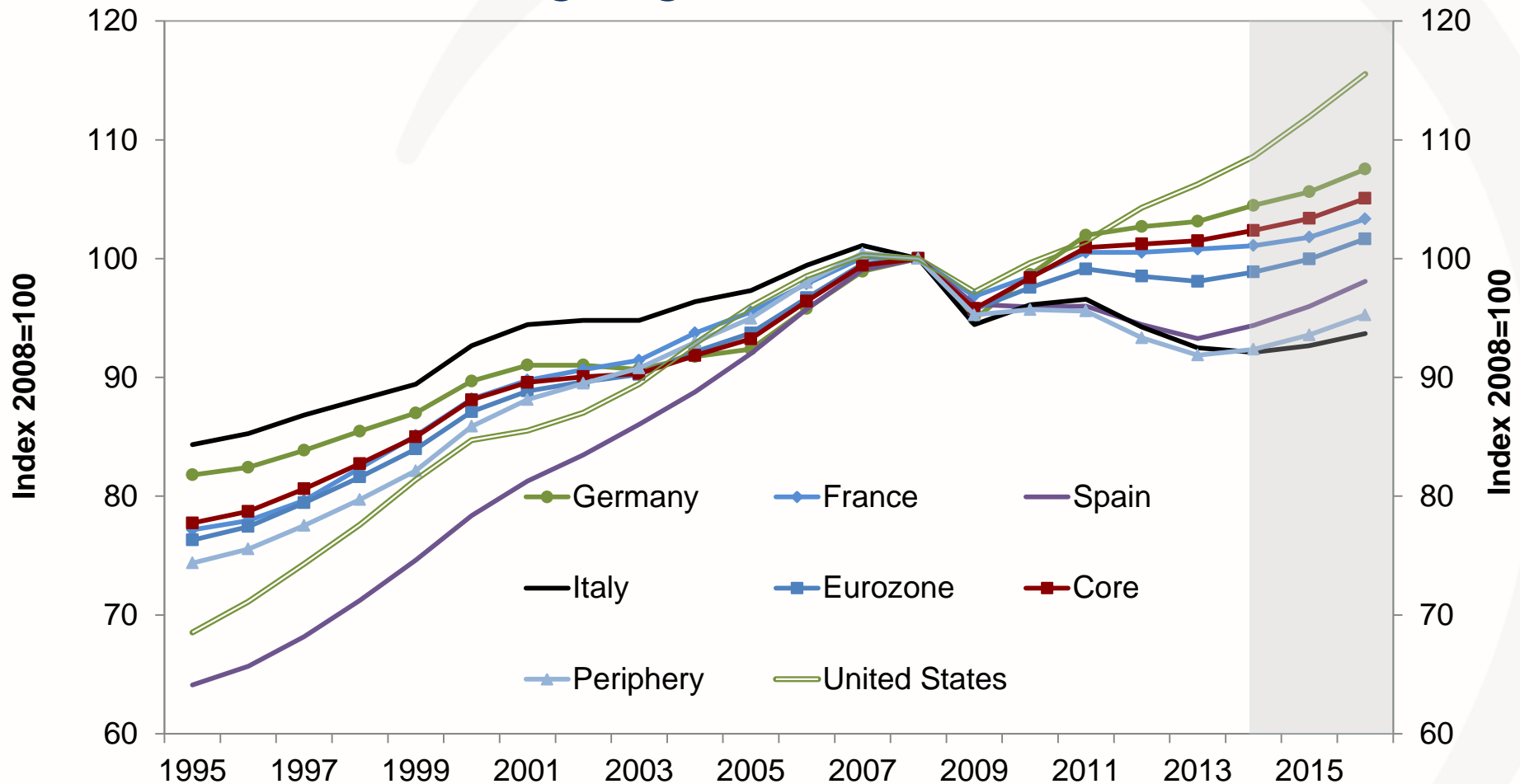
Source: Eurostat, US Department of the Treasury, Bureau of Economic Analysis, European Commission (forecasts)

Is GDP growth going back to its pre-crisis potential?



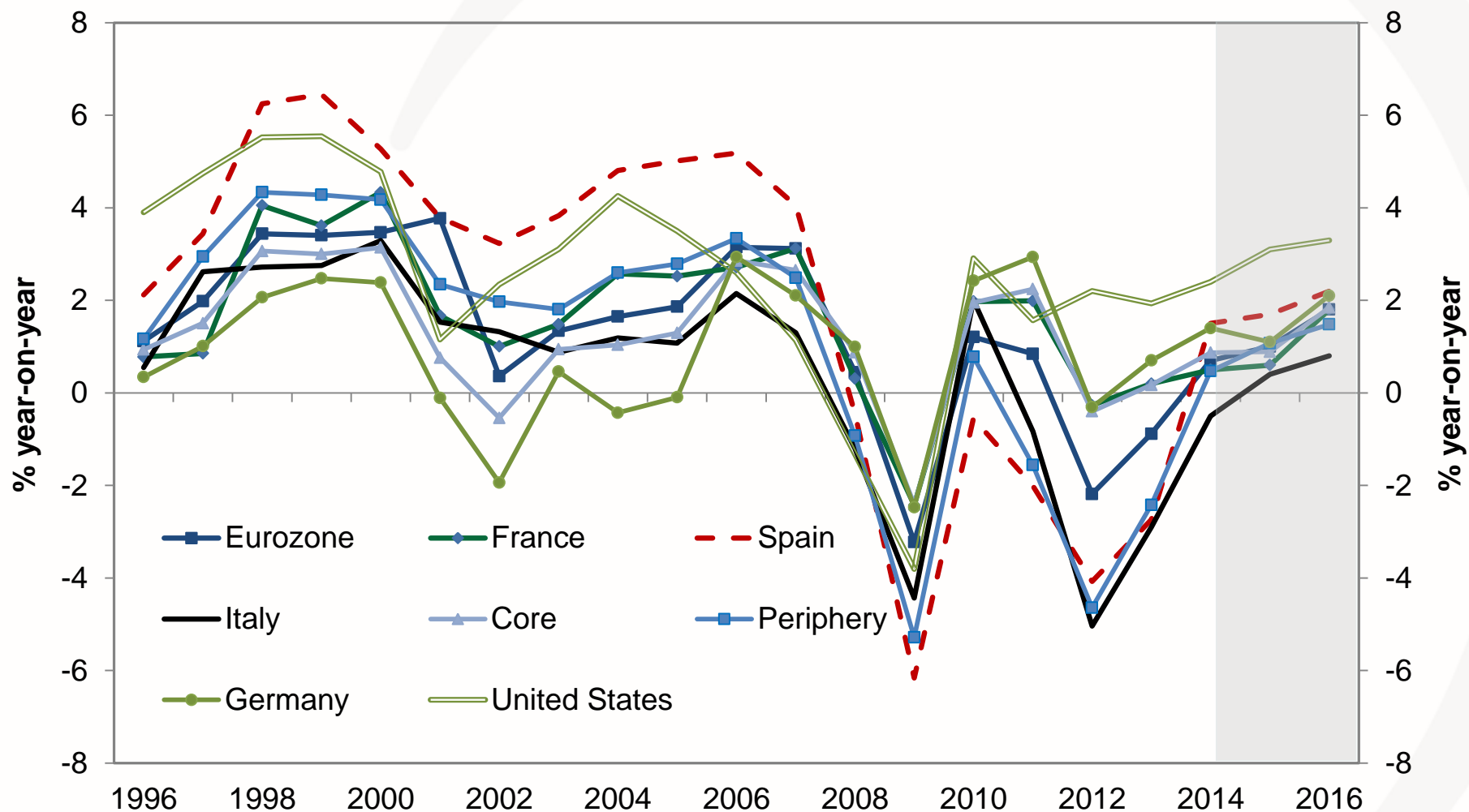
Source: Eurostat, BEA, European Commission (forecasts)

Are GDP level losses going to be recovered?



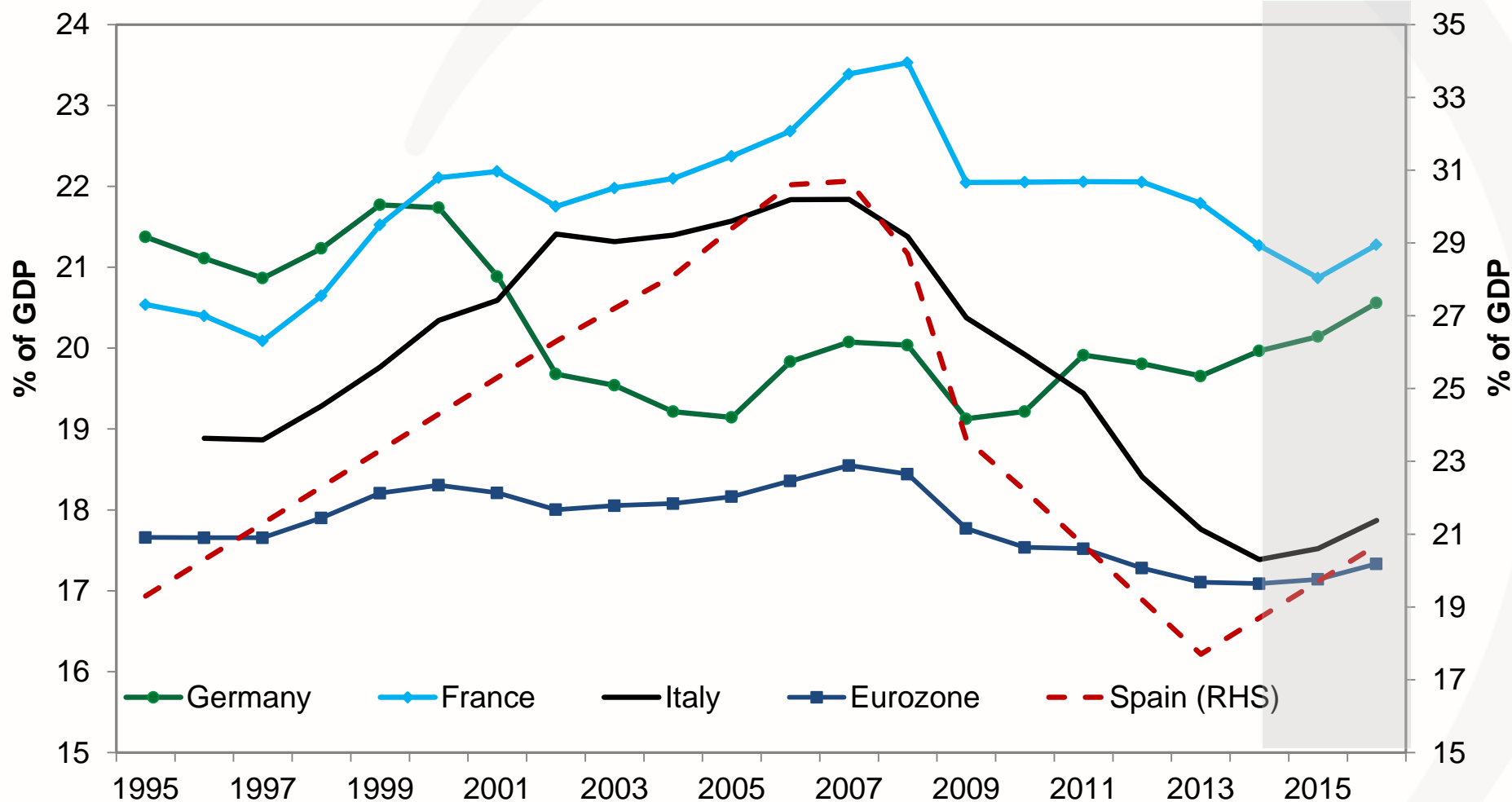
Source: Eurostat, BEA, European Commission (forecasts)

Domestic demand improving slowly even in core EA countries



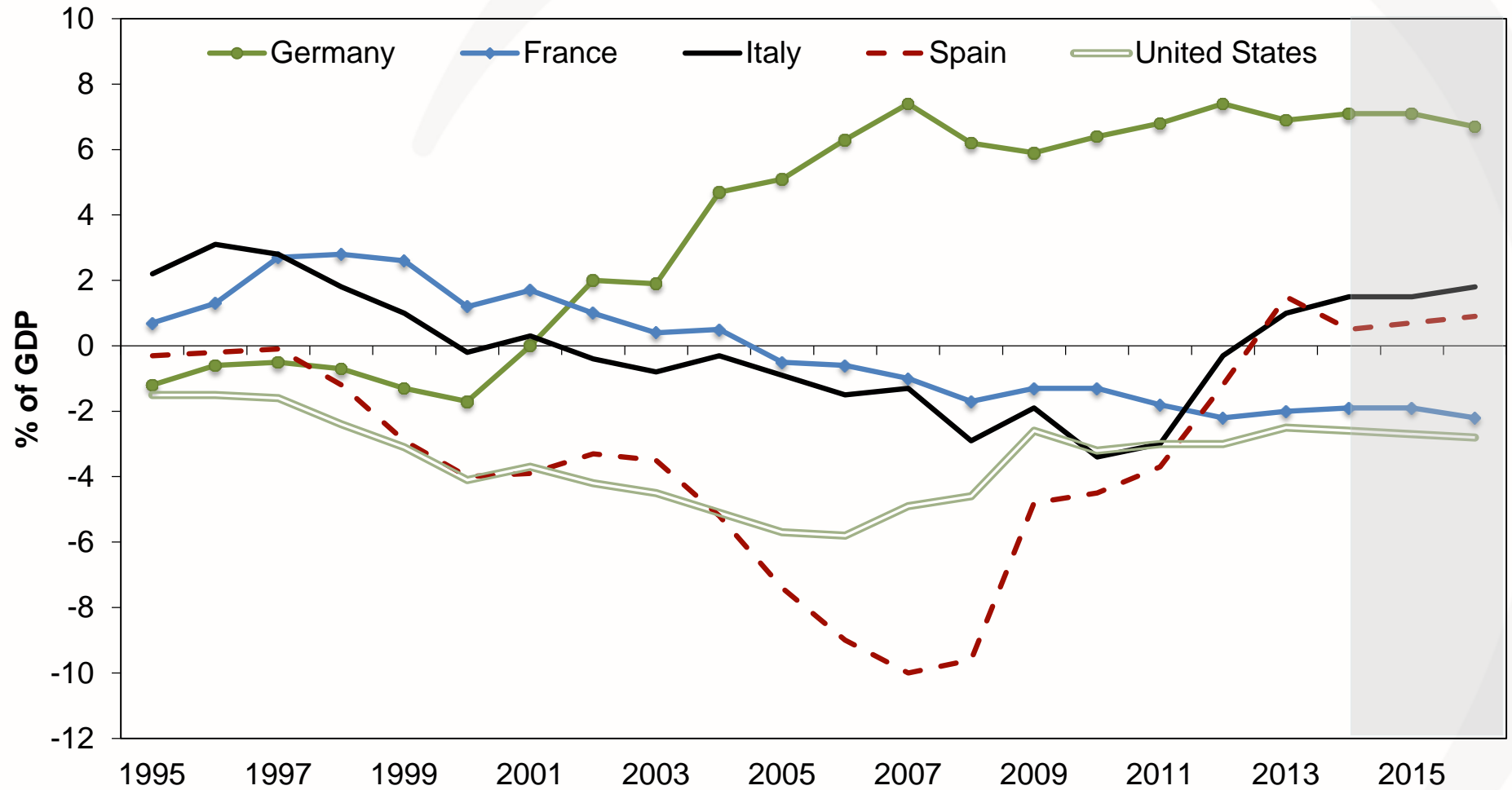
Source: Eurostat, Oxford Economics, European Commission (forecasts)

Investments for growth: the challenge to reverse current trends



Source: Eurostat, European Commission (forecasts)

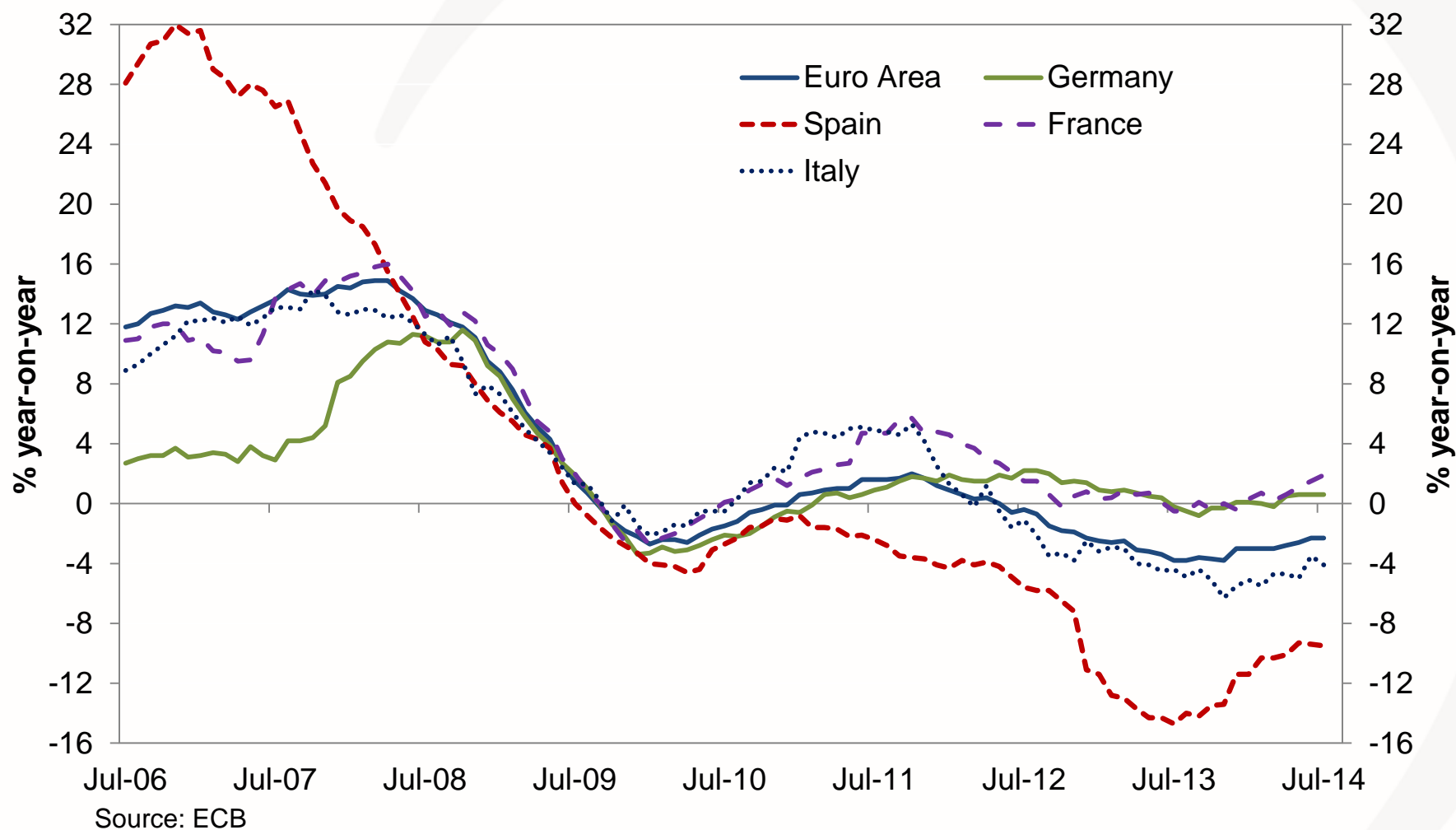
Policy mix leading to current account surpluses



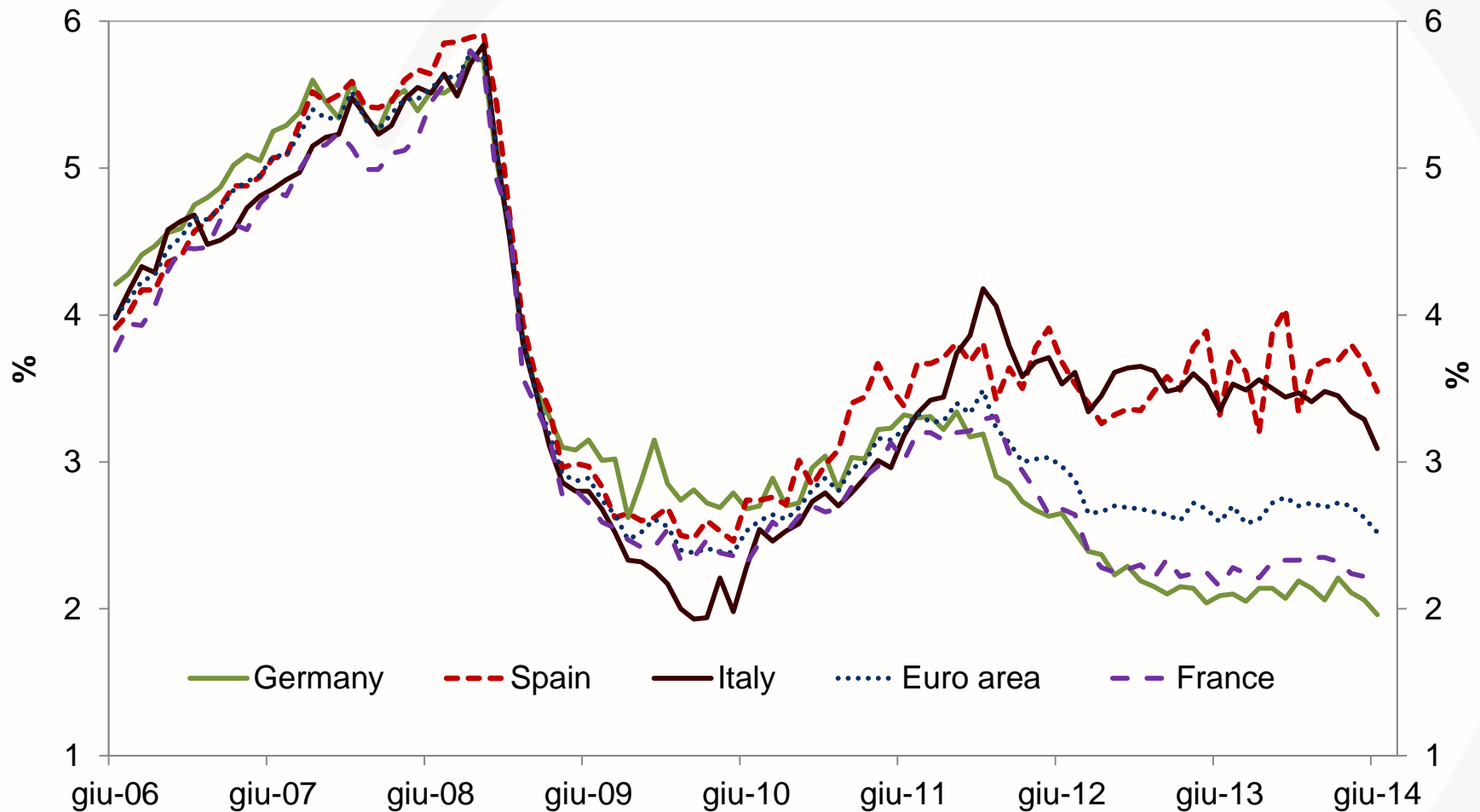
Note: Euro area data are not available in the period 1995-1998.

Source: Eurostat, ECB, IMF, European Commission (forecasts)

Contraction in credit: still no turning point

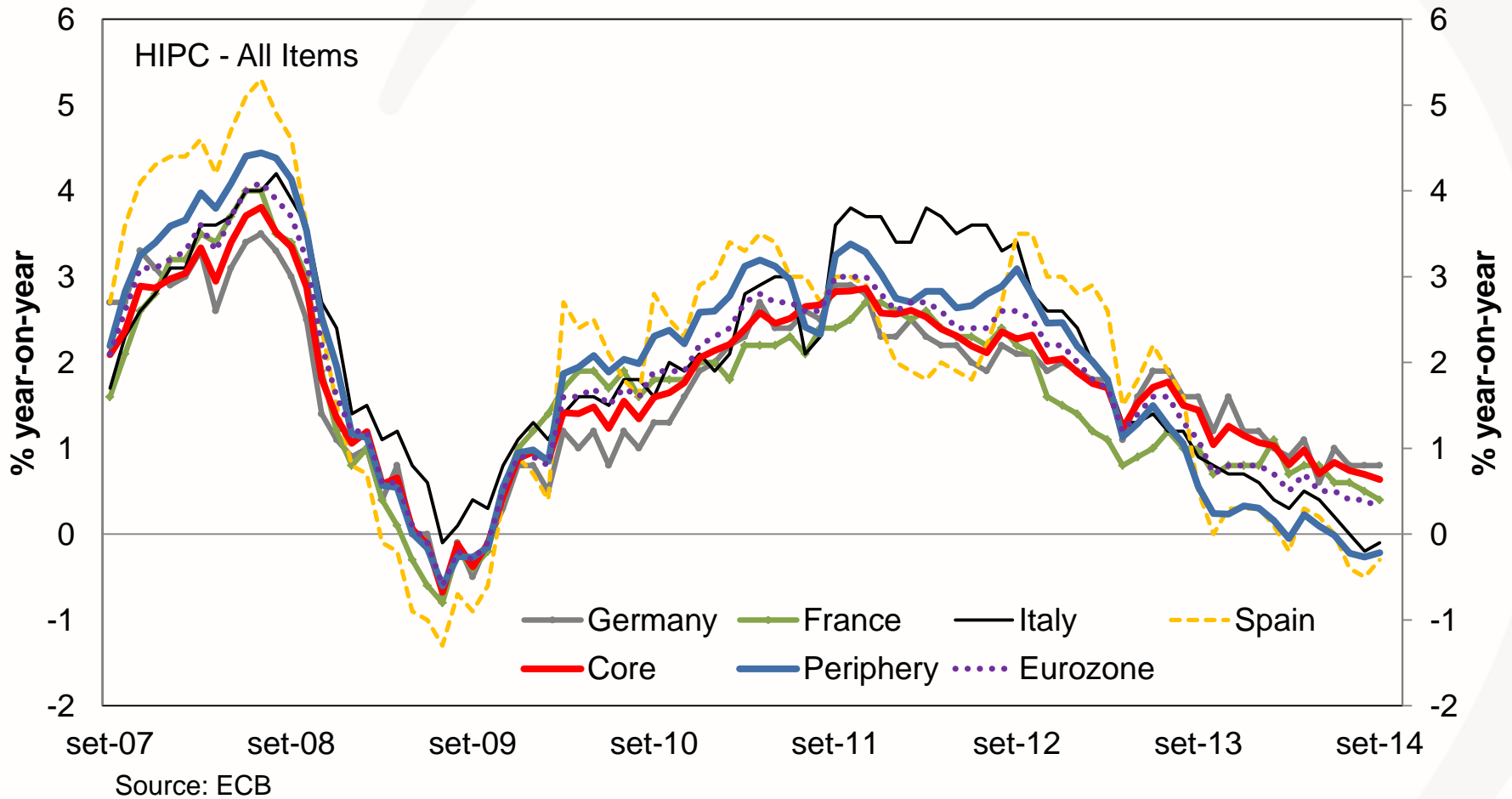


Cost of credit: the gap among EA countries remains wide



Source: ECB

Disinflation continues (with non-negligible risk of deflation)

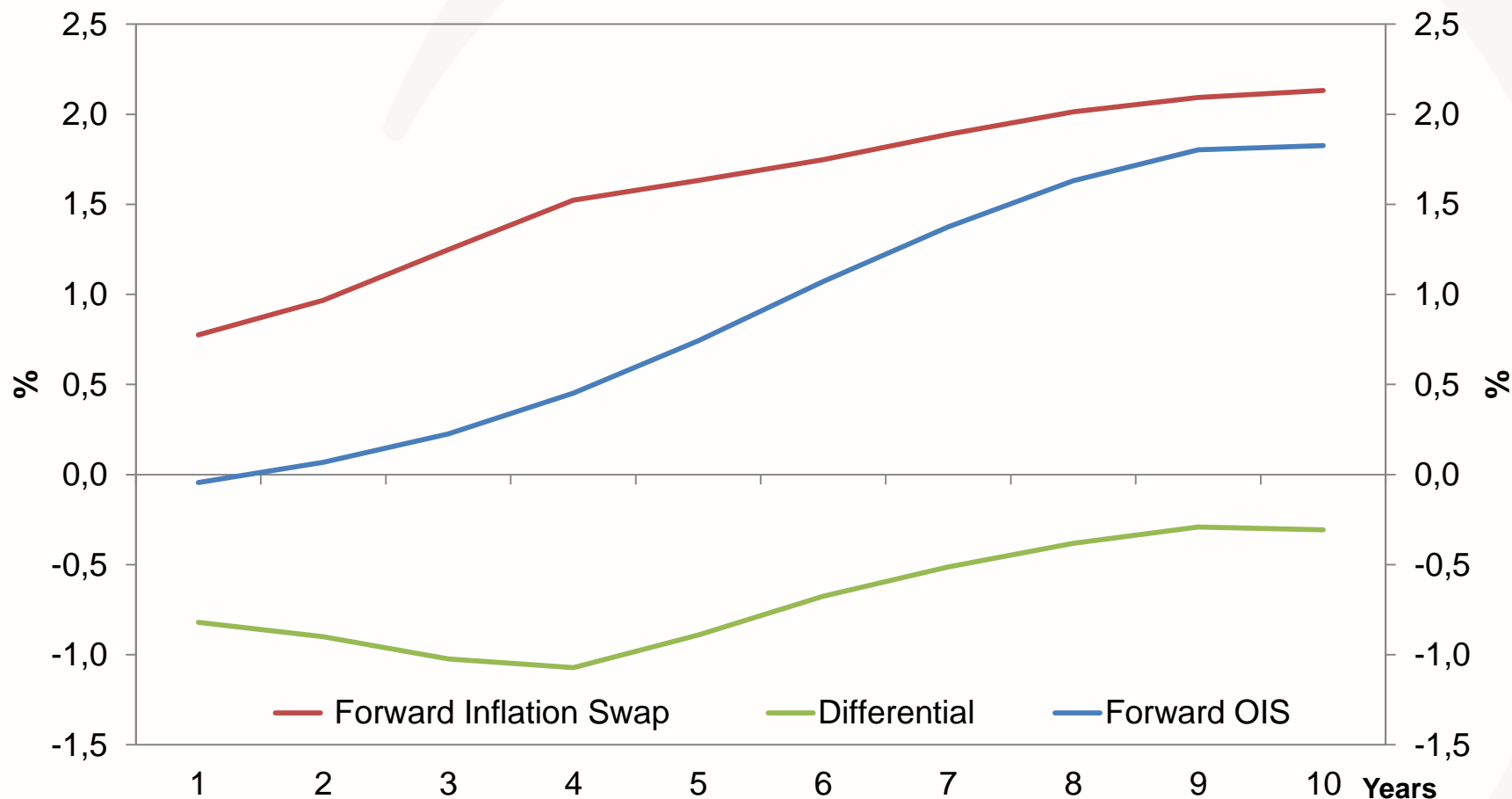


Inflation expectations has declined steadily



Source: Thomson Reuters Datastream

Secular stagnation already priced in



Source: Bloomberg

Where do we get growth from?

- **Lack of aggregate demand:** Is the current policy mix a correct stance for the Euro Area?
- **Supply-side reforms:** what can be done to strengthen them? How can we provide incentives for reforms within the existing fiscal framework?
- Are European **fiscal rules** appropriate for the current economic environment? Can we overcome the moral hazard issue?

IMF Art.IV EA: The SGP may reduce incentives for growth

- **“The SGP may reduce incentives to foster long-term growth:** Two issues features prominently in current discussions. The first is that the SGP may limit the space to finance structural reforms that entail sizeable short-term budgetary costs. Although the 2005 reform explicitly recognized that these costs should be accompanied, the present framework has so far only been applied to some types of pension reforms. Going beyond pension reforms is proving contentious. A second question is whether the MTO and, to a lesser extent, the 3 percent deficit cap, discourages public investment by limiting the capacity to borrow to fund projects that increase long-term growth potential.”

Does it make sense to allow flexibility for structural reforms?

- Structural reforms increase **potential growth** over the medium-long run and thus lower the **structural part of the deficit**.
- Structural reforms often imply either near-term recessionary effects or need to compensate losers with a **negative impact on public accounts**.
- What really matters is **long-term sustainability of debt**: supporting reforms makes sense also from a fiscal point of view.
- Risk of providing the **wrong incentives**: if you do fiscal consolidation you are fine, if you do structural reforms you are punished.

How to measure structural reforms?

- Already a large body of **economic literature**. Methods to assess how much reforms add to economic growth over time.
- Work of the LIME WG attached top EPC and plenty of papers by the Commission. Uncertainty is admittedly high, but it is feasible to come up with reasonable ranges.
- **Surveillance of structural reforms is already sufficiently developed and deep enough** to allow an evidence-based decision on flexibility for reforms.

Juncker's Plan: investment for growth?

- Very important for the **long-term prospects** of the EU economy.
- What can be done by the **private sector** and what instead can only be done by governments (or a supranational institution)?
- Unlikely to provide strong **support to the economy over the near term**, but could give a boost to **confidence** and thus support the recovery.
- Focus on the **quality of public investment**.

What's the way out?

- Need for more integrated **common and country-specific structural policies** to support long-term growth, employment and social cohesion.
- EU Member States are engaged in **fiscal consolidation** and efforts to reduce **macroeconomic imbalances**, which inevitably have near-term negative effects on demand: **need for fine-tuning and flexibility linked to structural reforms.**
- The **transmission mechanism of monetary policy** is still not working properly. Need for **inflation moving back to target soon.**

Best policy for an indebted country in a severe recession?

- Many targets: balancing public finance objectives, supporting the economy, respecting fiscal rules and maintaining credibility in financial markets.
- But one priority: **structural reforms** to boost confidence and change expectations of economic agents and investors.
- Unfortunately, structural reforms take time to bear fruits.
- The **ultimate goal must be sustainable economic growth and prosperity** .

Italy's key reforms, completed or under way

- **Institutional reforms:** new electoral law, end to bicameralism, simplification of the multilayer governance.
- **Labour market reform:** further flexibility in hiring, labour law reshuffling and simplification, 'Youth Guarantee'.
- **Tax system:** reduction in the tax wedge, a more equitable, transparent, simplified and growth-oriented tax system.
- **Speeding up of payments of the public administration:** new regulatory and monitoring framework, electronic invoicing.

Italy's key reforms, completed or under way

- **Privatisation programme:** State-owned/local gov't companies and real estate assets to improve efficiency and reduce debt.
- **Spending review:** reducing procurement costs, increasing efficiency and cutting unproductive public spending.
- **Investment framework:** alternative financing especially for SMEs, incentives for large-scale infrastructure investment; extra budget leeway for public investment at local level.
- **Public administration:** digitalisation and modernisation, open data, transparency, red tape reduction, fight against corruption.

Thank You

Living document on Italy's reforms can be found on website:

http://www.dt.mef.gov.it/en/analisi_programmazione_economico_finanziaria/strategia_crescita/index.html

