Q&A

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Europe's economy: building back strength, moving forward for the future

How can we explain the low level of growth of Europe over the last few years - particularly in comparison with the US and China - while savings in EU countries are particularly abundant and investment needs are significant?

The economies of China, the European Union and United States, while broadly similar in terms of size of their economic output, are structurally very different.

China's average real income per person, for example, remains at about a quarter of the living standards in Europe. Its sustained and rapid growth is largely driven by a catching-up process.

The comparison between the US and EU is more appropriate.

If we look at the recent past, it is clear that the initial economic impact of the COVID-19 pandemic was greater in Europe. This largely reflects the degree of the health shock and more stringent containment measures. In addition, the fact that the EU is a more open economy left it more exposed to the collapse in global trade.

Both the US and the EU have taken very sizeable support measures, which contributed to a rapid recovery on both sides of the Atlantic.

In Europe for example, we were quick to activate the general escape clause of our fiscal rules and deploy the SURE job retention scheme.

As a result, the labour market remained more resilient in the EU than in the US. With NextGenerationEU, the EU has also provided a strong incentive to support public and private investment in the post-crisis phase, along with ambitious reforms. The transformative nature of green and digital investment should have a lasting positive impact on economic growth.

While this bodes well for the EU's economic prospects, one has to recognise that the US traditionally has a more dynamic economy, with a stronger capacity to adjust and rebound more quickly than that of the EU.

In the two decades before the COVID-19 crisis, euro area GDP increased by an average 1.4% per year in real terms, while US GDP increased on average by 2.2% per year.
This underscores the need to combine the short-term EU response with longer-term supply side policies. The Recovery and Resilience Facility will play an important role here.

It will be crucial to improve the functioning of product, labour and financial markets.
This will also require continued progress in deepening the single market, completing the Banking Union and deepening the Capital Markets Union.

How will economic recovery be accelerated and supported by the EU Recovery and Resilience Facility? What contribution is expected from private investment and capital markets?

Europe's NextGenerationEU (NGEU) recovery package will significantly boost the EU economy in the post-crisis phase and beyond.
Just in terms of the investment it will generate, we expect NGEU to increase GDP by up to 1.5% and create up to two million jobs during the years of its active operation.

This expected growth will boost consumer demand and create more business opportunities, helping Europe get out of the crisis stronger and more resilient than before.

National recovery plans also contain reforms designed to affect supply side conditions. These are likely to increase the GDP growth and job creation even further.

In addition, our simulations show that positive spillovers account for around one-third of the estimated growth impact for the EU average. This means that even those EU countries that receive a small allocation of funds will indirectly benefit from RRF investments in others.

Private investments and capital markets will play a large role in the recovery and modernisation of our economies, as well as in the green and digital transitions.

For the Recovery and Resilience Facility (RRF) specifically, the European Commission is raising funds on capital markets on behalf of the EU – to date, more than €70 billion raised in long-term funding – with strong demand seen for all our bonds so far.

The first NGEU green bond was issued in October 2021 and raised €12 billion to be used exclusively for green and sustainable investments across the EU.
It is the world's largest green bond issue.

Issuing these high-quality assets also contributes to EU financial stability, as well as providing a new asset for banks and a new opportunity for other investors. This is also important given the scarcity of AAA bonds in financial markets.

On implementation, RRF funds are being released gradually as Member States reach the milestones and targets for the investments and reforms identified in national plans. The plans set out a clear trajectory for the economy, which should encourage more private investment.

The investments and reforms will improve the business environment, reduce regulatory barriers and administrative burdens for businesses.

It shows that we want to make our economies fit for the future and send a clear sign to the markets that the time to invest in Europe is now.

What are the fiscal and economic priorities for achieving sustainable growth in the European Union in the context of over-indebtedness of most Member States and a resurgence of inflation?

The EU economy rebounded strongly in 2021, although the pace of the expansion has moderated towards the end of the year. The current wave of infections, supply bottlenecks, soaring energy prices and rapidly rising inflation rates are creating a drag on economic activity.

In 2022, the overall fiscal stance should remain moderately supportive so that the recovery can build traction. Since debt levels are high in several Member States, it is important that the support is well targeted and does not create a permanent burden for public finances.

We have called for support to come from higher investments, both from those funded by the EU and from national budgets. Higher investment will contribute to raising productivity and thereby potential growth. It will also reduce the risk of sustained inflationary pressures compared with an expansionary fiscal stance fuelled by higher current expenditure.

It will remain important to continue close coordination of fiscal policies in the period ahead.

On one hand, the persistent uncertainty requires fiscal policy to remain agile.

On the other, we need to create clarity and predictability on the general course of our policies beyond the immediate future.

That is why we will very soon provide guidance on fiscal policy for 2023. It will reflect the global economic situation, the specific economic and budgetary situation of each Member State and also the discussion on reviewing the EU's economic governance framework.

A key priority will be to reduce high and divergent public debt ratios in a gradual, continuous and growth-friendly way, considering the importance of investment.

What are the costs and risks of not addressing the ring-fencing practices that explain the complete standstill in which the Banking Union finds itself? How can we move forward?

Banks remain the main funding source for EU economies. We need them to be well capitalised and resilient, but also efficient in managing their costs, operations and cross-border resources.

In this respect, an integrated and completed Banking Union would bring benefits through more efficient management of resources and economies of scale.

It would increase the ability of the private sector to absorb shocks at a time of crisis and allow banks to diversify their exposures to different regions, sectors and sovereigns.

Deepening and diversifying sources of funding remains a key element of our Capital Markets Union project. At the same time, banks play an important role in financing local economies.

They need to be able to provide credit anywhere in the EU to households and businesses, including SMEs – particularly in smaller markets with less availability of other funding sources.

Since banks of different sizes with different business models can respond to a wide range of financing and risk management needs, we have made sure that the our regulatory framework respects the diversity of the EU banking sector.

By completing the Banking Union, we can create the confidence and trust needed to remove ring-fencing practices while protecting financial stability. In turn, this would help us to progress with achieving more cross-border consolidation and reduce the risk of market fragmentation within the Banking Union.

As we emerge from the crisis, risks may come with the phasing out of support measures for the real economy – along with new challenges such as the green and digital transitions and cybersecurity threats.

We cannot properly address these challenges without a complete Banking Union.