EURO AREA AT A CROSSROADS\textsuperscript{1}

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\textsuperscript{1} Based on IMF’s 2016 Euro Area Article IV Staff Report

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EURO AREA RECOVERY CONTINUES, LED BY DOMESTIC DEMAND...

Contribution to Growth

\begin{center}
\begin{tabular}{l|c|c|c}
& Net exports & Domestic demand & GDP \\
\hline
2013Q2 & -0.5 & 0.5 & 0.0 \\
2013Q3 & 0.0 & 0.5 & 0.0 \\
2014Q1 & 0.0 & 0.5 & 0.0 \\
2014Q2 & 0.0 & 0.5 & 0.0 \\
2015Q1 & 0.5 & 1.0 & 1.0 \\
2015Q2 & 0.5 & 1.0 & 1.0 \\
2015Q3 & 0.5 & 1.0 & 1.0 \\
2015Q4 & 0.5 & 1.0 & 1.0 \\
2016Q1 & 0.5 & 1.0 & 1.0 \\
\end{tabular}
\end{center}

Source: Eurostat.
AND SUPPORTIVE FISCAL AND MONETARY POLICIES

Euro Area: Structural Balance Fiscal Impulse (Percent of potential GDP)


Euro Area: Corporate Lending Conditions (Percent)

Source: Haver Analytics.

BUT MEDIUM-TERM OUTLOOK FOR GROWTH AND INFLATION REMAINS WEAK...

Euro Area: Real GDP Over Various Cycles (Index: business cycle peak Q = 100)

Sources: ECB; WEO and IMF staff calculations.

Various Inflation Measures (Percent, y-o-y)

Sources: Bloomberg, L.P.; and Haver Analytics.
**DUE TO CRISIS LEGACIES OF STILL HIGH UNEMPLOYMENT...**

Unemployment Rate since the Financial Crisis (Percent) *

Sources: Haver and IMF staff calculations. Note: */ after adjusting for changes in labor force participation.

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**...AND SLOW PROGRESS IN DELEVERAGING...**

Total Debt-to-GDP (Percent of GDP)

Source: Haver Analytics. Note: NPISHs = non-profit institutions serving households. EA financial corporate debt is non-consolidated.

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Nonperforming Loans and Write-offs

...WEIGHING ON INVESTMENT, ESPECIALLY FOR SMEs\textsuperscript{2}

\textbf{Euro Area: NFC Leverage (Debt to Assets; in percent)}

\textbf{Euro area: Contribution to Investment Growth (Percent)}

Source: Banque de France, BACH database.


\textsuperscript{2} "Investment, Firm Size, and the Corporate Debt Burden: A Firm-Level Analysis of the Euro Area," IMF 2016 Euro Area Selected Issues Paper

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LAGGING PRODUCTIVITY AND COMPETITIVENESS...

\textbf{Service Sector Productivity: US and Euro Area (Index 2007 = 100)}

\textbf{ULC-based REER vis-a-vis Germany (Index, 1999Q1=100)}

Source: Haver Analytics.

Source: Haver Analytics.

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RISKS TO THE OUTLOOK HAVE INCREASED…

Favorable View of the EU (Percent)

Source: Pew Research Center.
Note: */ Data for Italy begins in 2012.

Bank Equity Prices (Index, Dec 31, 2015 = 100)

Source: Bloomberg, LP.

POTENTIAL SPILLOVERS FROM BREXIT TO EURO AREA

European Country Export to UK, 2014

Source: Office of National Statistics; Haver Analytics; WEO; IMF staff calculations.

Euro Area: Main Economic Indicators, 2016-18

Staff report
Real GDP (percent) 1.7 1.7 1.7
Inflation (percent) 0.3 1.2 1.4

Preliminary forecast update
Real GDP (percent) 1.6 1.4 1.6
Inflation (percent) 0.2 1.1 1.2

Source: IMF staff estimates.

3”Macroeconomic Implications of the United Kingdom Leaving the European Union,” 2016 IMF United Kingdom Selected Issues Paper
COLLECTIVE, COMPREHENSIVE ACTION NEEDED TO BOLSTER GROWTH AND STRENGTHEN THE UNION

Create better incentives for growth-friendly structural reforms

Strengthen fiscal framework while expanding centralized fiscal support

Comprehensive, more balance mix

Accelerate balance sheet repair and complete the banking union

Continue monetary policy accommodation

1. INCENTIVIZE GROWTH-FRIENDLY STRUCTURAL REFORMS

**Euro Area: Labor Market Reform and Outcomes**
(Bubble’s size indicates the level of labor market rigidity in 2013)

**Euro Area: Product Market Reform and Outcomes**
(Bubble’s size indicates the level of product market rigidity in 2013)

Sources: OECD and IMF staff calculations.

2. STRENGTHEN FISCAL FRAMEWORK AND EXPAND CENTRALIZED SUPPORT

Euro Area: Debt-stabilizing Primary Gap in 2016 (Percentage points of GDP)

General Government Debt (Percent of GDP)

3. MAINTAIN MONETARY ACCOMMODATION TO BOOST INFLATION...

Annual Loan Growth Required to Maintain Net Interest Margin, end-2015 (Y/y percent change) *

Scope of Available Assets after Completion of Current Asset Purchase Program (APP) as of end-March, 2016 (EUR billion)

Sources: Bloomberg L.P., EBA Transparency Exercise (2015), ECB, SNL, and IMF staff calculations.

Note: */ The values are reported in nominal terms and take into account existing and planned purchases until March 2017 as well as issuer/issue limits (incl. SMP), and exclude government debt securities outside the eligible maturity range of between 2 and 30 years and securities trading below the deposit rate (as cap on the eligible market for each asset class); the amount is also reduced by further by the allocation of purchases based on the pro-rated ECB capital key (without Greece and Cyprus). **/ includes sub-national and agency debt securities. For all securities, only the non-encumbered market was considered.

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4. ... AND REPAIR BANK BALANCE SHEETS AND COMPLETE BANKING UNION

Euro Area: Time to Reduce Stock of Nonperforming Loans to Pre-Crisis Levels (Percent of total loans/years) *

Sources: EBA, ECB, national authorities, and IMF staff calculations. Note: */ As of end-Q2 2015 (for IRL and ITA, end-2014); assumes future loan growth in line with nominal GDP and non-performance of new loans at pre-crisis default rates.

7 "A Strategy for Resolving Europe’s Problem Loans" and “Tackling Small and Medium-Size Enterprise Loans in Europe,” IMF Staff Discussion Notes 15/19 and 15/04, 2015

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“THE WHOLE IS GREATER THAN THE SUM OF ITS PARTS...”

Euro Area: GDP Growth Simulations (Percent)

Sources: IMF, World Economic Outlook (April 2016); and IMF staff calculations.


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References

1 Based on IMF’s 2016 Euro Area Article IV Staff Report

2 “Investment, Firm Size, and the Corporate Debt Burden: A Firm-Level Analysis of the Euro Area,”

3 “Macroeconomic Implications of the United Kingdom Leaving the European Union,” 2016 IMF
   United Kingdom Selected Issues Paper

   Selected Issues Paper

5 “Options for A Central Fiscal Capacity in the Euro Area,” 2016 IMF Euro Area Selected Issues

6 “Negative Interest Rate Policy (NIRP): Implications for Monetary Transmission and Bank
   Profitability” 2016 IMF Euro Area Selected Issues Paper

7 “A Strategy for Resolving Europe’s Problem Loans”
   Size Enterprise Loans in Europe,” IMF Staff Discussion Notes 15/19 and 15/04, 2015

8 “Comprehensive, Integrated Policies to Boost Euro Area Growth,” 2016 IMF Euro Area Selected

July 10, 2016