

Speech by Eurogroup President Jeroen Dijsselbloem on 28 October 2013 at Nueva Economía Forum in Madrid, Spain

Ladies and gentlemen,

It is with great pleasure that I address you here today. I would like to thank Luis for providing this opportunity. The subject that I will discuss today, is recovery and reform. A suitable topic for a Spanish economic forum, since Spain has accomplished much in this respect. Since receiving support for the banking sector, banks' balance sheets have improved markedly. This has led to better financing conditions for both the government and financial institutions. Progress has been made in budgetary consolidation and macro-economic imbalances have diminished.

Consumer and business confidence have been on the rise, unemployment appears to be stabilising and in the third quarter Spain made a return to economic growth.

The measures taken have not been easy and the job is not yet done. But all signs indicate that Spain has turned a corner and is now on the road to recovery. As a result, Spain is now in much better shape than it was a year ago. I therefore don't think that discussions on the exit from the ESM program will be particularly tough. Since many euro area countries are facing similar challenges, it is encouraging to see what Spain has accomplished.

I see these encouraging signs also in the programme countries. In the past year I have visited, amongst others, Greece, Portugal and Ireland. During these visits I was impressed with the efforts that these countries have undertaken, both in fiscal consolidation and in reforms. We can now see the results of these reforms in the economy and financial markets. Two years ago all focus was on short-term survival. Now we are all looking towards the future again. This change in atmosphere is a tribute to all that has been achieved.

From stabilisation to recovery

Ladies and gentlemen,

In recent years European policy has mostly focussed on stabilisation. We have succeeded in avoiding a financial collapse. We have fixed flaws in the design of the Economic and Monetary Union. We have taken many measures that would have been unthinkable in the past. Through this, the European leaders have shown our determination and commitment to the euro as an anchor for financial stability and an engine of growth. The euro is part of the solution, as Luis just quoted and not part of the problem.

However, the work on stabilisation is not yet fully complete. The highest priority is now the move towards a full banking union. In my view this is essential to sever the dangerous link between sovereigns and financial institutions. Keeping in mind how big this task is, I think our progress has been remarkable. I am confident that we will remain on track to complete the banking union on schedule. In this context, I strongly support the principle that risks are borne by the investors that took them, not taxpayers.

The measures we have agreed have succeeded in restoring calm to financial markets and the recession appears to be over. Does this mean the euro area has completely recovered from the crisis? This is still doubtful. In my view, two challenges remain: restoring economic growth and preserving the European social model. Both are strongly interconnected. I will briefly go into both challenges.

Restoring economic growth

Economic growth is essential for a successful recovery from the crisis. However, restoring growth will not be a simple task. We should realize that it will be very hard to return to pre-crisis levels of growth. There are two main reasons for this.

First of all, growth in the years before the crisis was fuelled partly by credit. These debts, both private and public, now have to be repaid. Also, credit will not be as easily accessible as it used to be. If credit is priced too cheaply, it will lead to boom-bust cycles that are ultimately bad for real economic growth.

Secondly, Europe faces a strong demographic challenge that will be felt in the decades to come.

With this in mind, the question is: what can we do? We have already strengthened economic and budgetary policy coordination in Europe to improve incentives for Member States. This was accompanied by a number of growth-enhancing measures at the European level. For instance, we have doubled the capital of the European Investment Bank. We have strengthened the internal market further. And we have undertaken initiatives to improve financing conditions for small and medium enterprises.

I certainly believe we can achieve even more in that respect, for example by negotiating bilateral trade agreements. Recently negotiations with Canada were concluded successfully. I hope that we can achieve similar success in talks with the United States, Japan and the Mercosur countries.

However, most untapped potential lies with the member states. The OECD has estimated that European countries can each gain between 5% and 20% of extra GDP growth over the next ten years by implementing structural reforms. These reforms encompass all measures that improve the functioning of economies and therefore stimulate growth.

There is no one-size-fits all solution. Since countries are diverse, the necessary structural reforms can also vary considerably. However, in broad terms there are challenges that are relevant for all countries in the euro area. For instance, much can be gained by creating a better business environment. World Bank and the OECD indicators show that there is room for improvement in all countries. Of course the actions would differ across nations, so countries should address their own specific bottlenecks.

Also, economic efficiency is greatly hampered by protected sectors and professions. For example, the European Commission has identified no less than 4700 regulated professions in countries of the European Union. Some of these make sense, such as medical specialists. Others much less so, like golf instructors or second-hand car salesmen.

Preserving the European social model

The second challenge is preserving the European model. In my view, the European social model is what sets Europe apart from the rest of the world. European governments spend on average 10% of GDP more than other governments. This is entirely due to social expenditure. Of course there are differences between countries, which is a reflection of voters' preferences, tradition and history. But on the whole, European countries have a very even distribution of prosperity compared to the rest of the world.

Remarkably, this extra government expenditure did not prevent strong income growth. In fact, per capita GDP in Europe is among the highest in the world. It is often suggested by economists that every redistribution of wealth goes at the expense of economic growth.

The European experience demonstrates, however, that redistribution can go hand in hand with growth. In my view this is because public support is essential for any economic model in a democratic society. If only the happy few reap the benefits of economic development, this will lead to social unrest. This in turn will ultimately damage growth. Since the European voters' preference is clearly in favour of a certain degree of income distribution, I strongly believe that the European social model supports economic growth instead of harming it.

Preserving the European social model does not mean that we should keep everything as it is today. Our social systems were designed in a time where demographics were favourable and economic growth was self-evident. In order to survive, these systems need to adapt to the new economic reality. For example, life expectancy in Europe has increased by about eight years in the last four decades. During the same period, the effective age of retirement decreased in all countries. Clearly, this is untenable in the long run.

Also, overall unemployment has increased strongly across the euro area. But youth unemployment is even higher, sometimes twice the level. Given the prospect of population ageing, we cannot afford to sideline young people for a prolonged period. We should therefore do our utmost to ensure young people have no barriers in attaining education or employment. This includes a critical look at the role of labour market institutions.

A European agenda

So, how should we address these challenges? Think of the euro zone as an apartment complex. We, the owners' association,

have restructured the foundation, rewired the building and enforced the walls. But to make the renewed building a success, everyone should improve the inside of their own apartment. In short: we have achieved much at the central EU and euro area level, but this cannot solve all problems.

The focus should now be on promoting structural change at the member state level, because the areas where reforms are needed belong mostly to the national domain. Diversity between member states has always been Europe's strength. It reflects the different preferences of voters and encourages innovation through competition. This diversity enables us to learn from each other. The European Commission can play the role of facilitator in this process.

I therefore propose to further strengthen peer review in the area of structural reforms, both in scope and in political commitment within the European Semester. We should enter into this process offensively. We should try to learn from each other in a positive way. Where useful, this can be supported by mutual technical assistance. We should enlist the advice of international institutions. Their insights can be useful to identify bottlenecks and design appropriate policies.

However, this process cannot become too informal. Given the strong interdependencies in the euro area, we should not be afraid to remind each other of our responsibilities. Coordinated action between member states can also be instrumental in overcoming vested interests.

The agenda should be based on more than just peer review and peer pressure. In general we need to focus European economic governance not only on budgetary targets, but also on the completion of meaningful reforms. For instance, the European budgetary rules allow for an extension in bad economic times. This leniency is now granted without any conditions. In future cases, I propose to link deviation of fiscal targets in the Stability and Growth Pact to the concrete achievement of reforms. In other words only if a country pushes forward crucial reforms can the deadline for fiscal targets be extended. Softening of fiscal targets should be tied more concretely to completion of reforms.

Lastly, I would like to see a clearer link between the expenditure from the European budget and loans from the European Investment Bank on the one hand and the implementation of structural reforms by member states on the other. A country growth strategy, modelled after World Bank practice, would be a suitable tool for this.

Conclusion

In conclusion I would like to affirm that the two challenges I mentioned - restoring growth and preserving the European social model - cannot be seen separately. In fact, I see them as mutually reinforcing.

Economic growth is essential for the affordability of social spending. Conversely, social protection is a cornerstone of how we in Europe organise our societies. This creates a stable environment for investing in the future. To achieve these twin goals, each Member State has the responsibility to contribute. Together this builds a stronger Europe.

I thank you all for your attention.

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