

# European Stagnation: Private sector 'structural' balance + fiscal policy

Jesper Jespersen, Jesperj@ruc.dk

Roskilde University & Aalborg University

21<sup>st</sup> April 2017

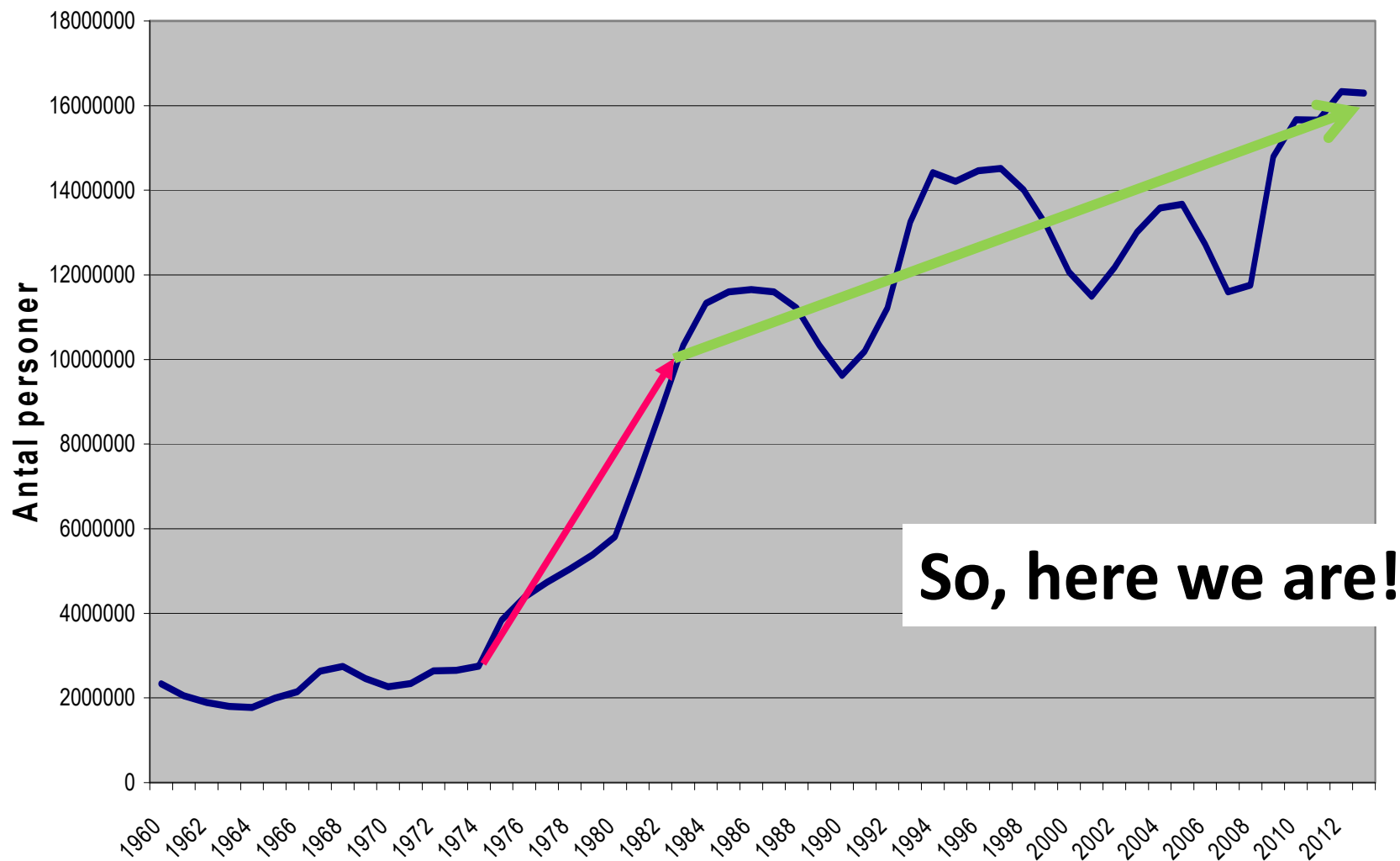
# Secular(?) stagnation in EU

1. Persistently high unemployment
2. Slow growth in 'old' Europe
3. Why?

**Private sector 'structural' imbalances**

# Unemployment in the euro-zone

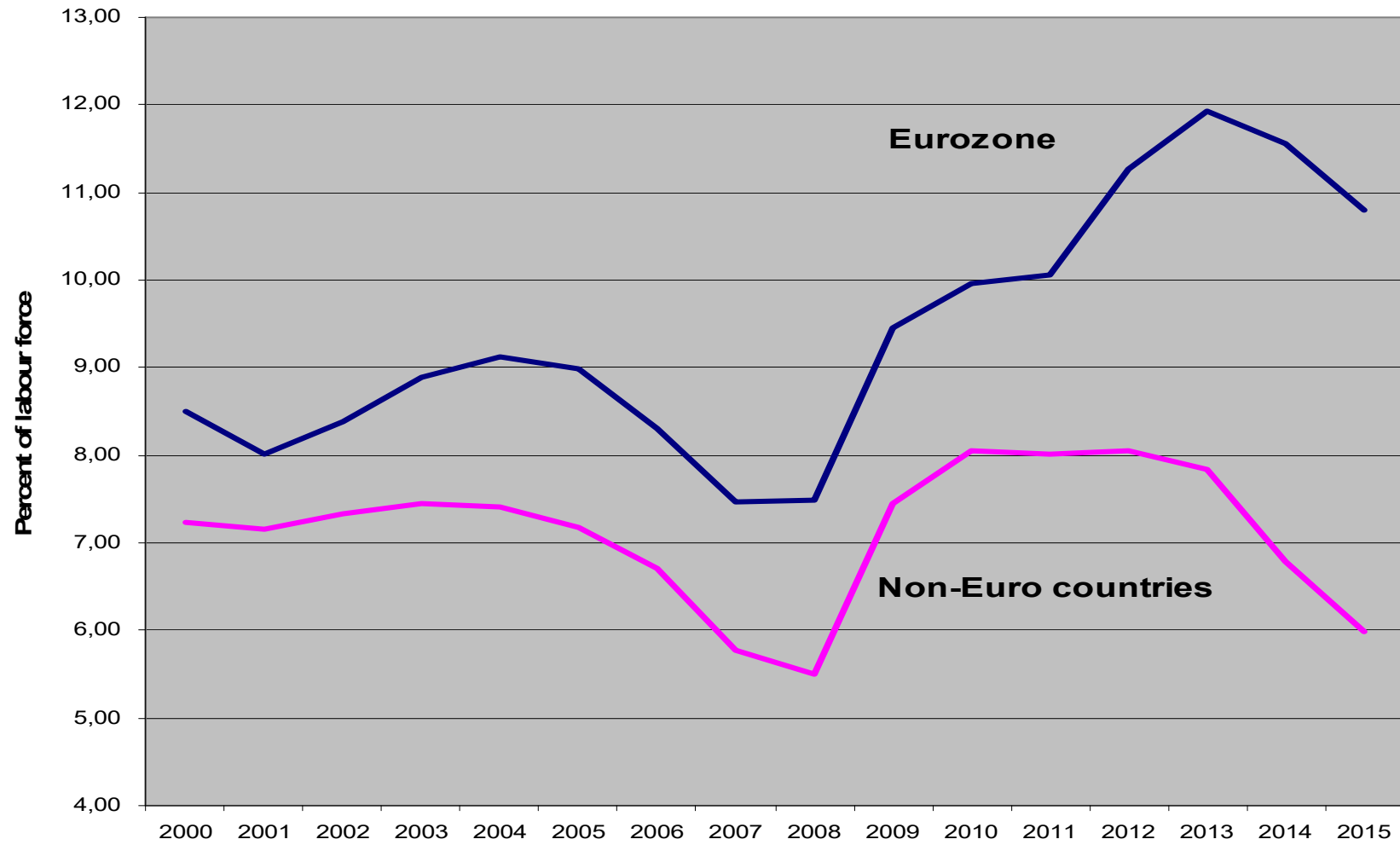
Arbejdsløshed, Euro-zonen (15 lande)



**So, here we are!**

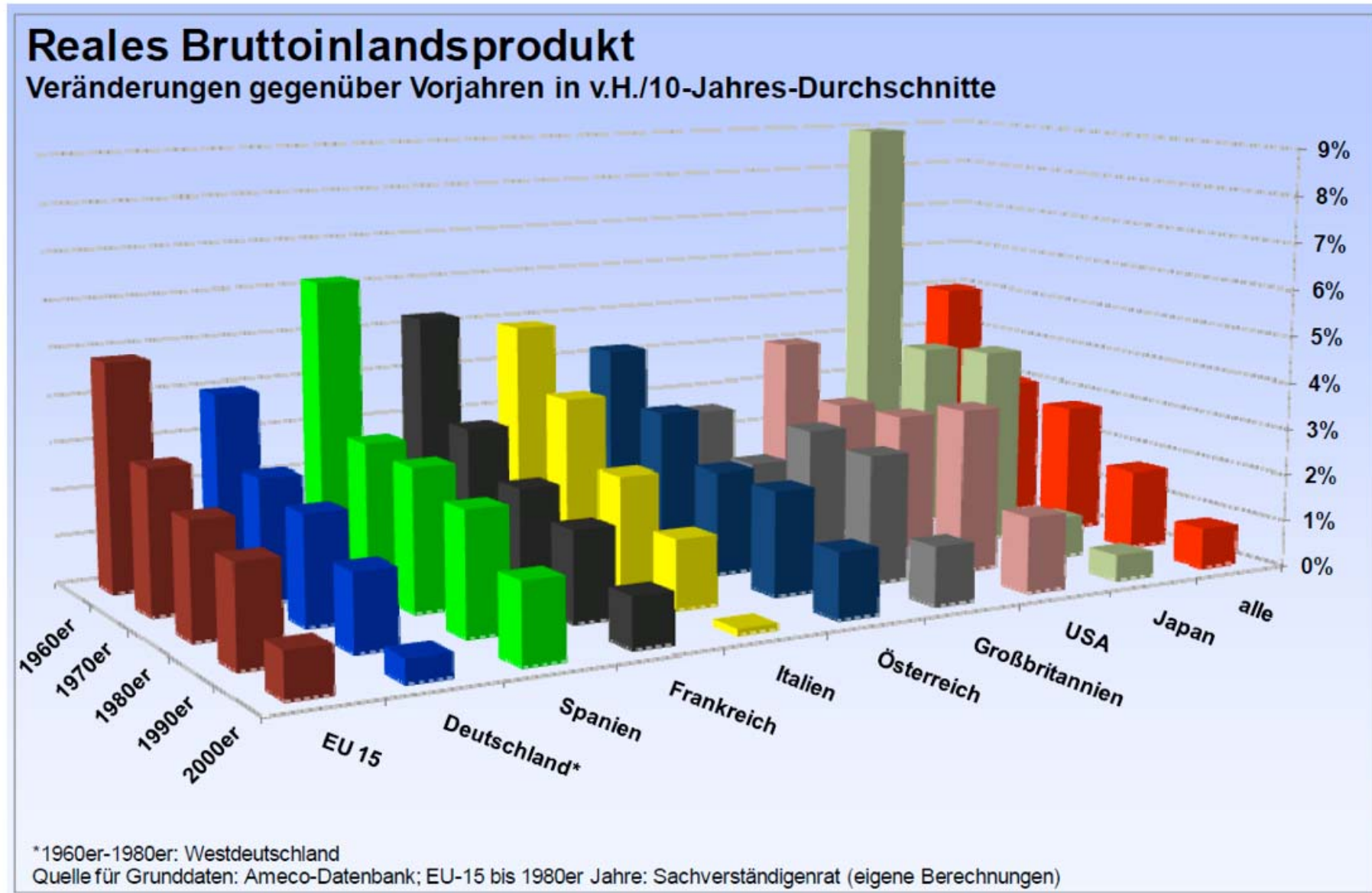
Kilde: OECD, Economic Outlook, dec. 2011

## Unemployment: Eurozone & non-eurocountries



Source: OECD, economic Outlook, June 2016

# Increasing stagnation in 'old' Europe, 1960-2015



Source: Norbert Reuter: Presentation on the welfare state in post-growth society

**Angela Merkel:  
It's only resting!  
But, she is wrong:**

**Which a tiny €-  
drop: ECB -  
monetary easing  
cannot help**



### 3. why?

#### 1. Lack of effective demand!

Caused by:

**Private sector (structural) excess financial savings**

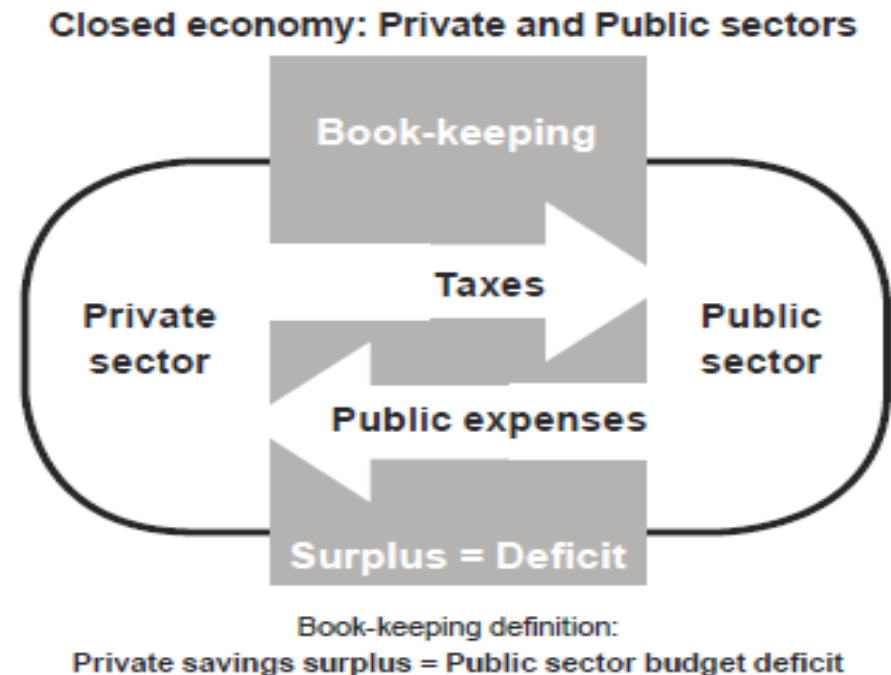
**Structural: full employment (hypothetical calculation – what model is used? )**

**Excess: financial savings > real investment (NB!  $S \equiv I$ )**

**Excess private sector financial savings  $\equiv$   
public deficit + balance of payments surplus**

# Two Sector balance!

A Consolidated two sectors model – closed economy



(1)  $Y \equiv C + I + G$

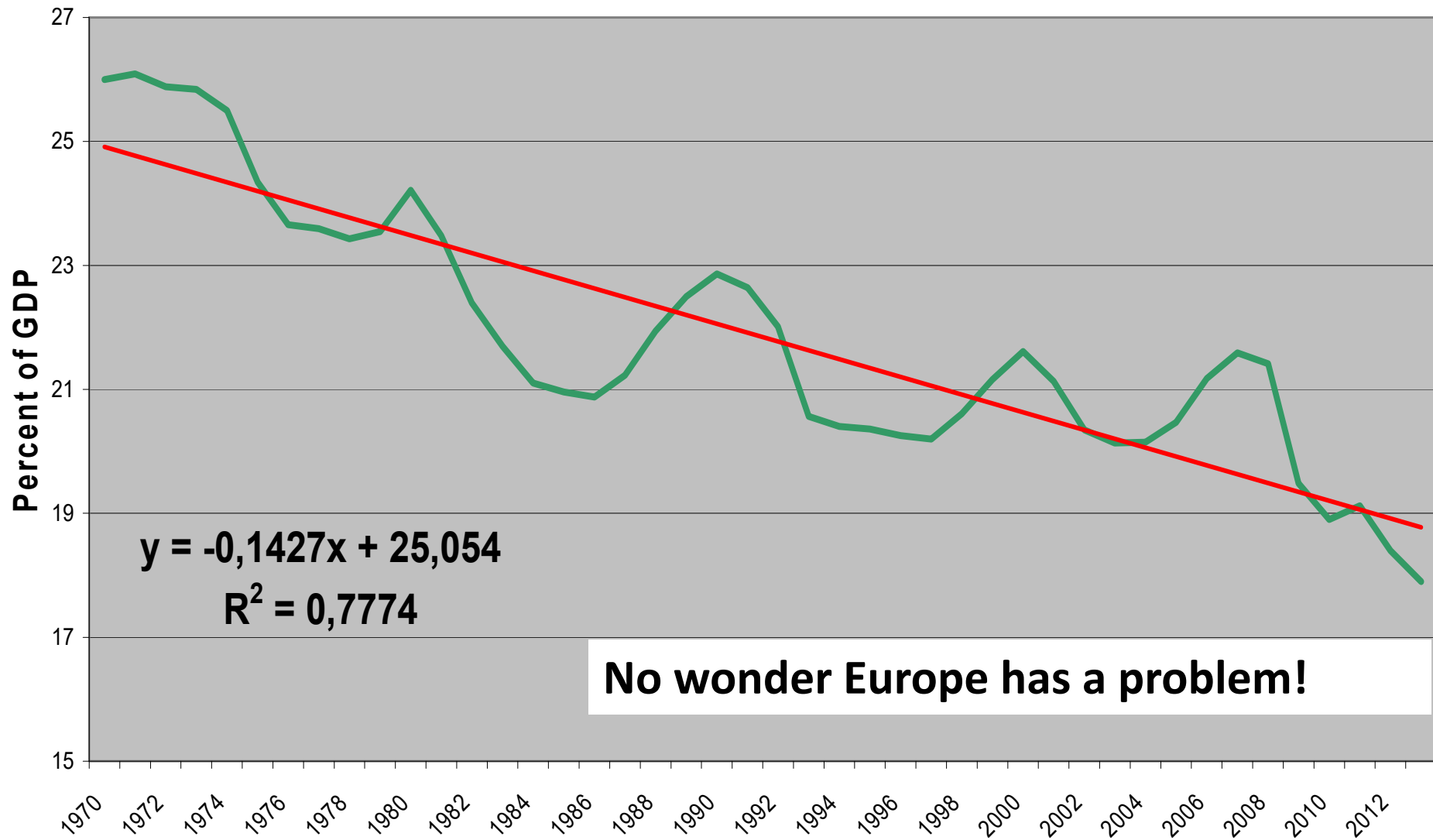
(2)  $Y - \text{Tax} \equiv C + I + [G - \text{Tax}]$

(3) Private **actual excess** savings:  $S_{px} \equiv Y - C - I - \text{Tax} \equiv [G - \text{Tax}]$

(4) Private actual **excess** savings  $\equiv$  public sector deficit

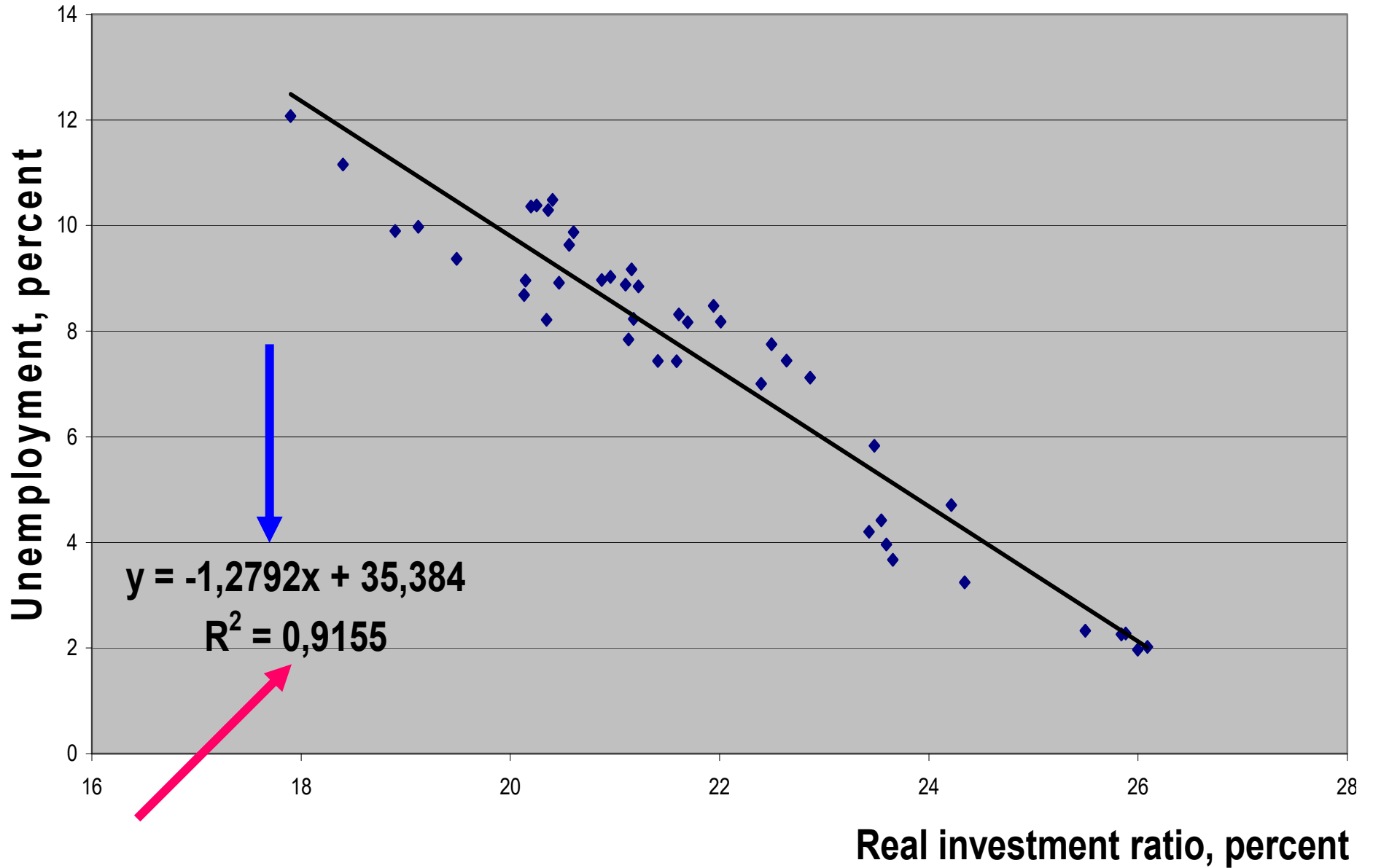


## Euro(15): Real Investment/GDP, 1970-2013

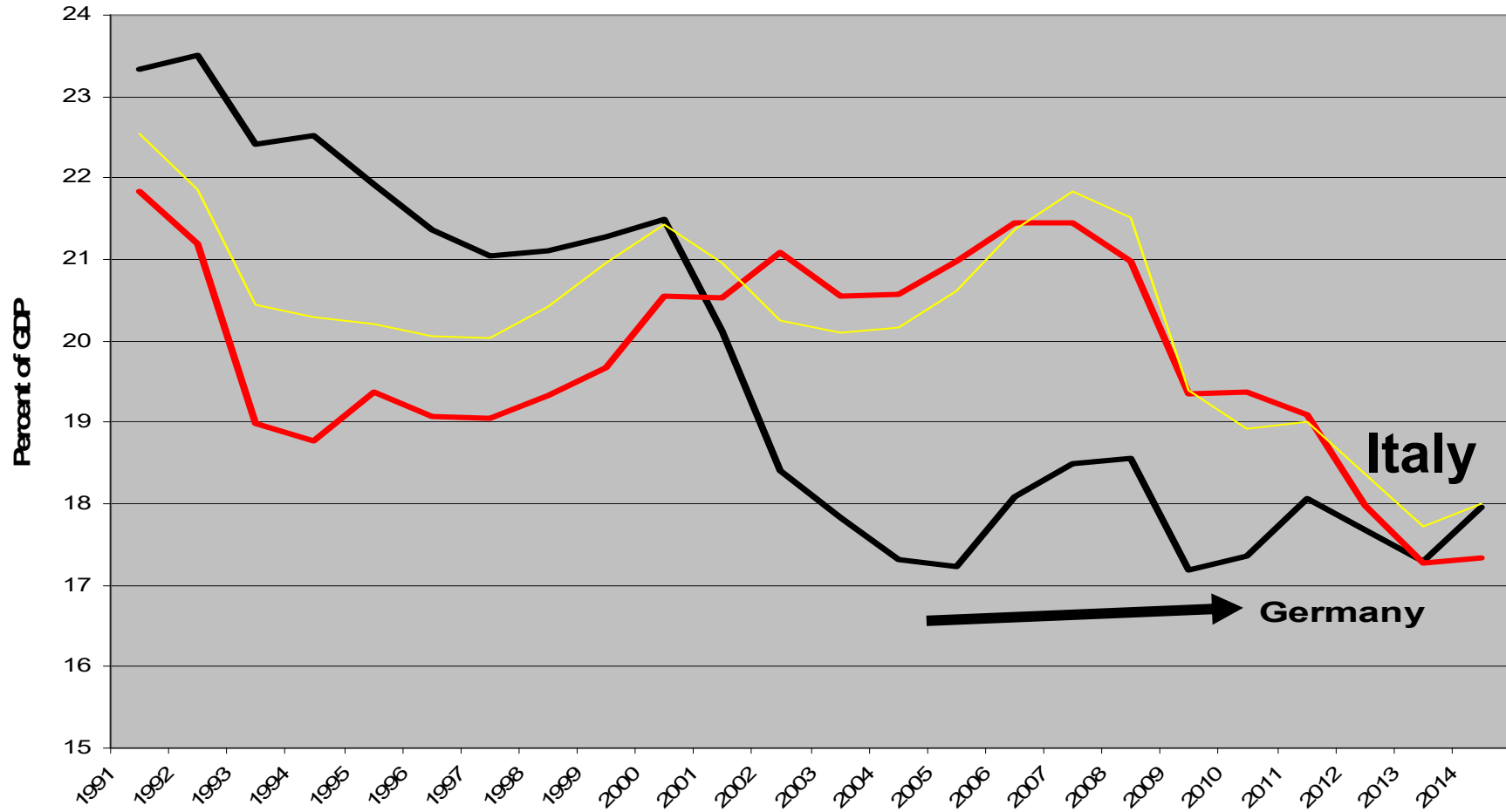


Source: OECD, Economic Outlook, no.90 & 92

# EU15, Real investment ratio & rate of Unemployment, 1970-2013

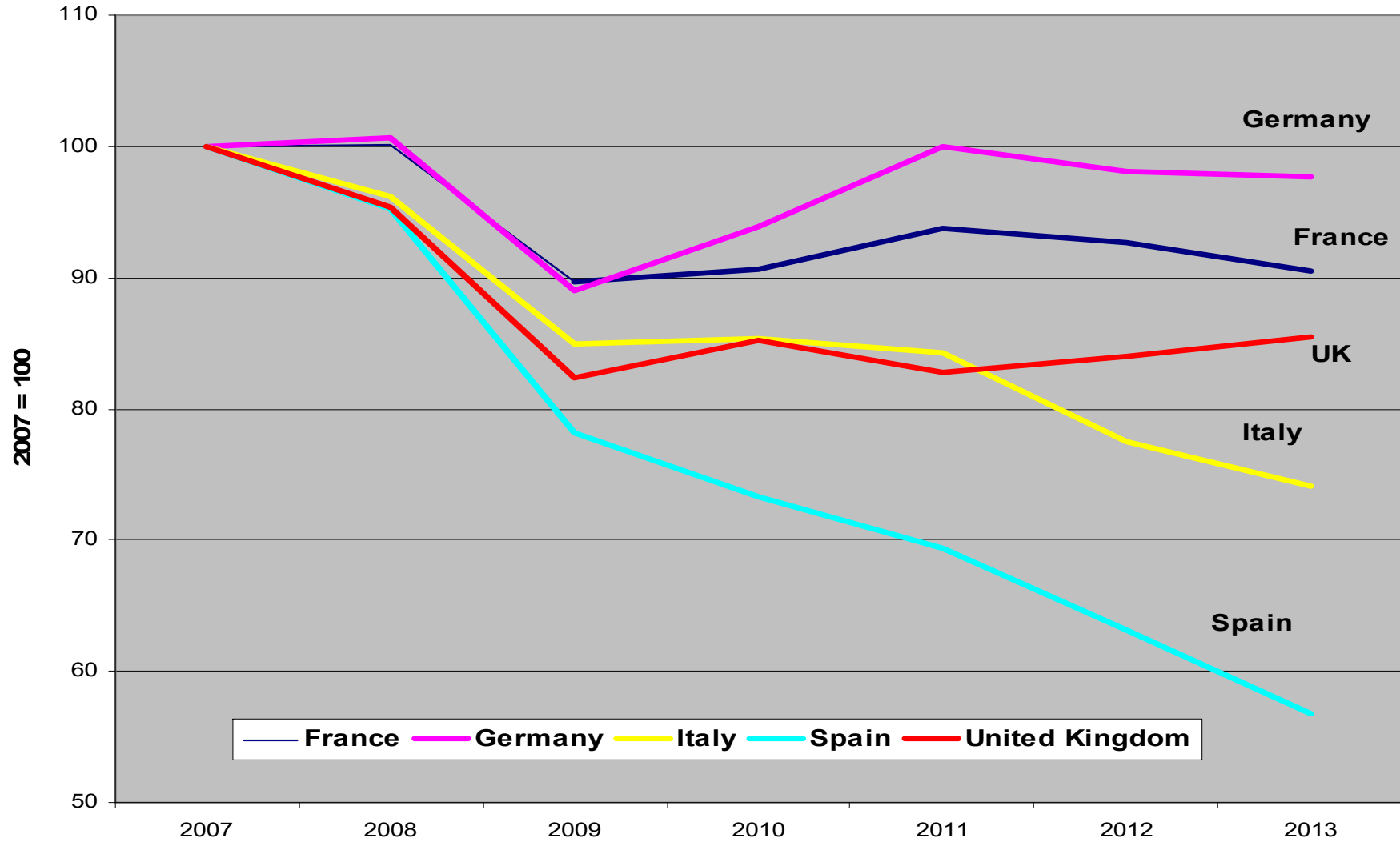


# Real Investment ratio, 1991-2014



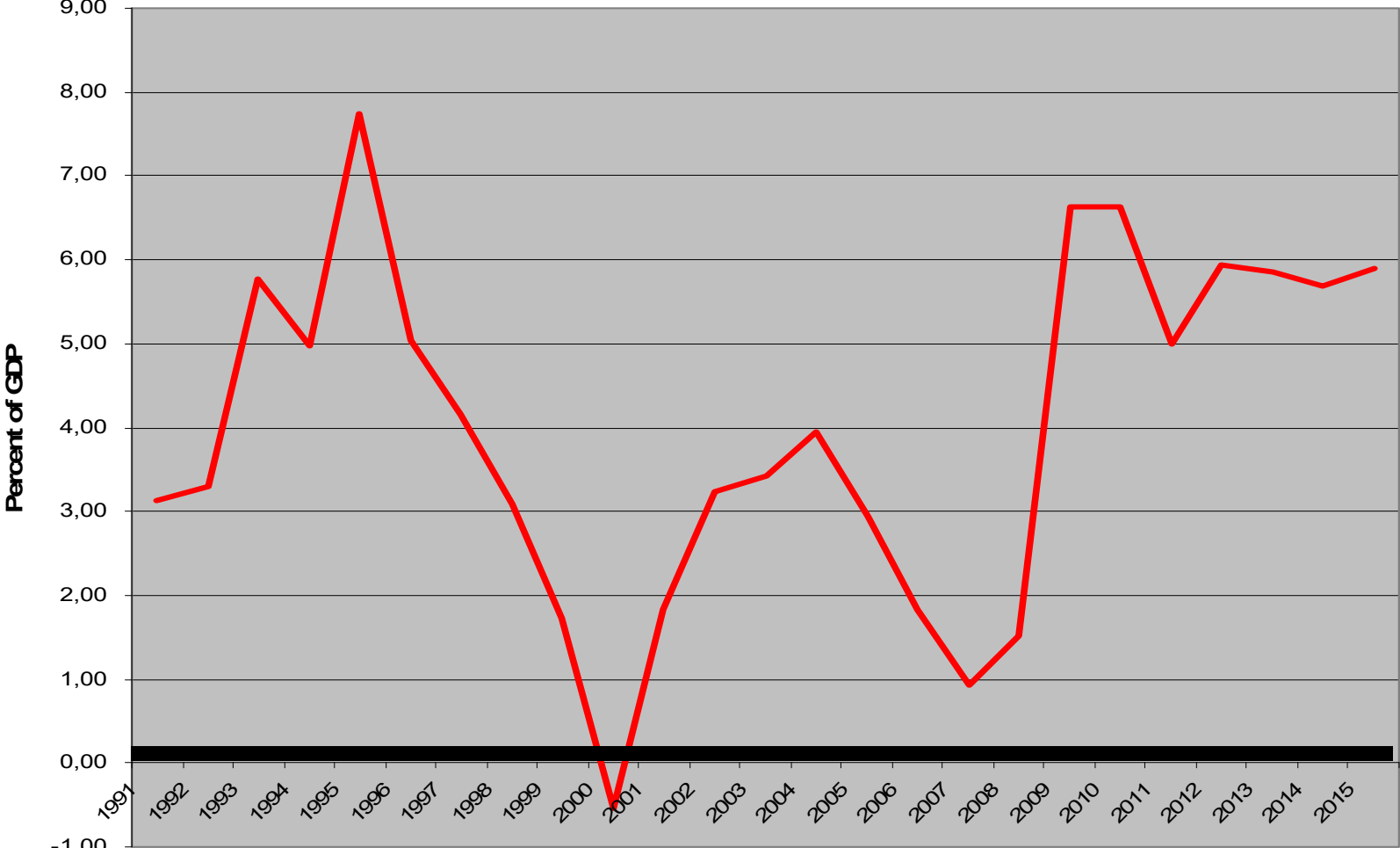
Germany Italy Euro area (15 countries)

# Real Fixed Capital, 2007-2013



Source: OECD, Economic Outlook, June 2013

# Private sector excess savings, Eurozone & Instability!



Source: OECD, Economic Outlook, 2016

**Lack of internal private sector demand of 6 pct. of GDP**

# No wonder Euro-zone has a growth problem!

Lower real investments mean:

1. Short run: lack of effective demand, causing rising unemployment
2. Long run: lower productivity growth, causing growth to slow further down

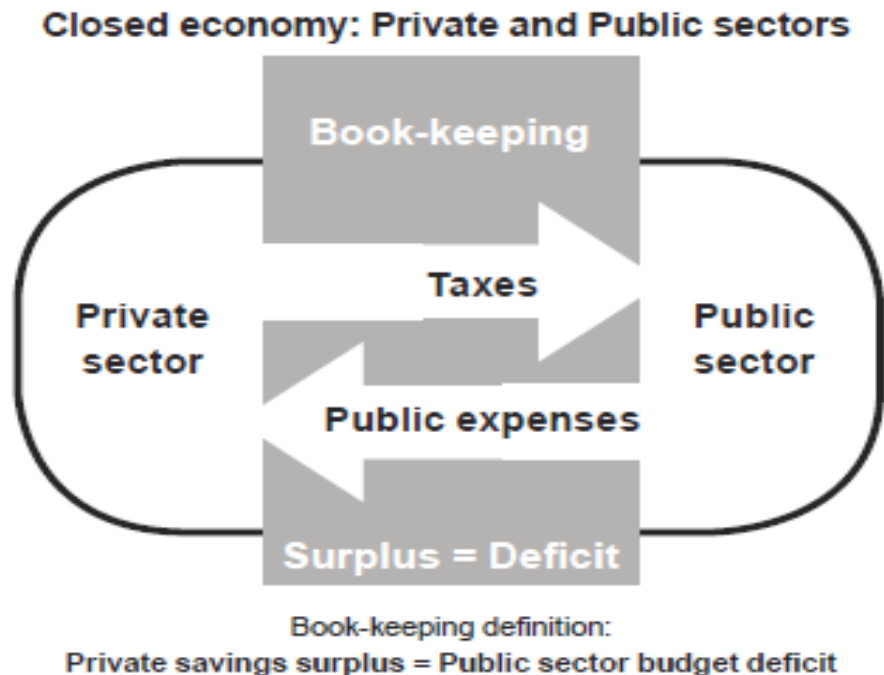
But, even worse it is:

1. Re-enforced by austerity policy due to misunderstood macroeconomics.

Because:

# Two Sector balance!

A Consolidated two sectors model – closed economy



(1)  $Y \equiv C + I + G$

(2)  $Y - \text{Tax} \equiv C + I + [G - \text{Tax}]$

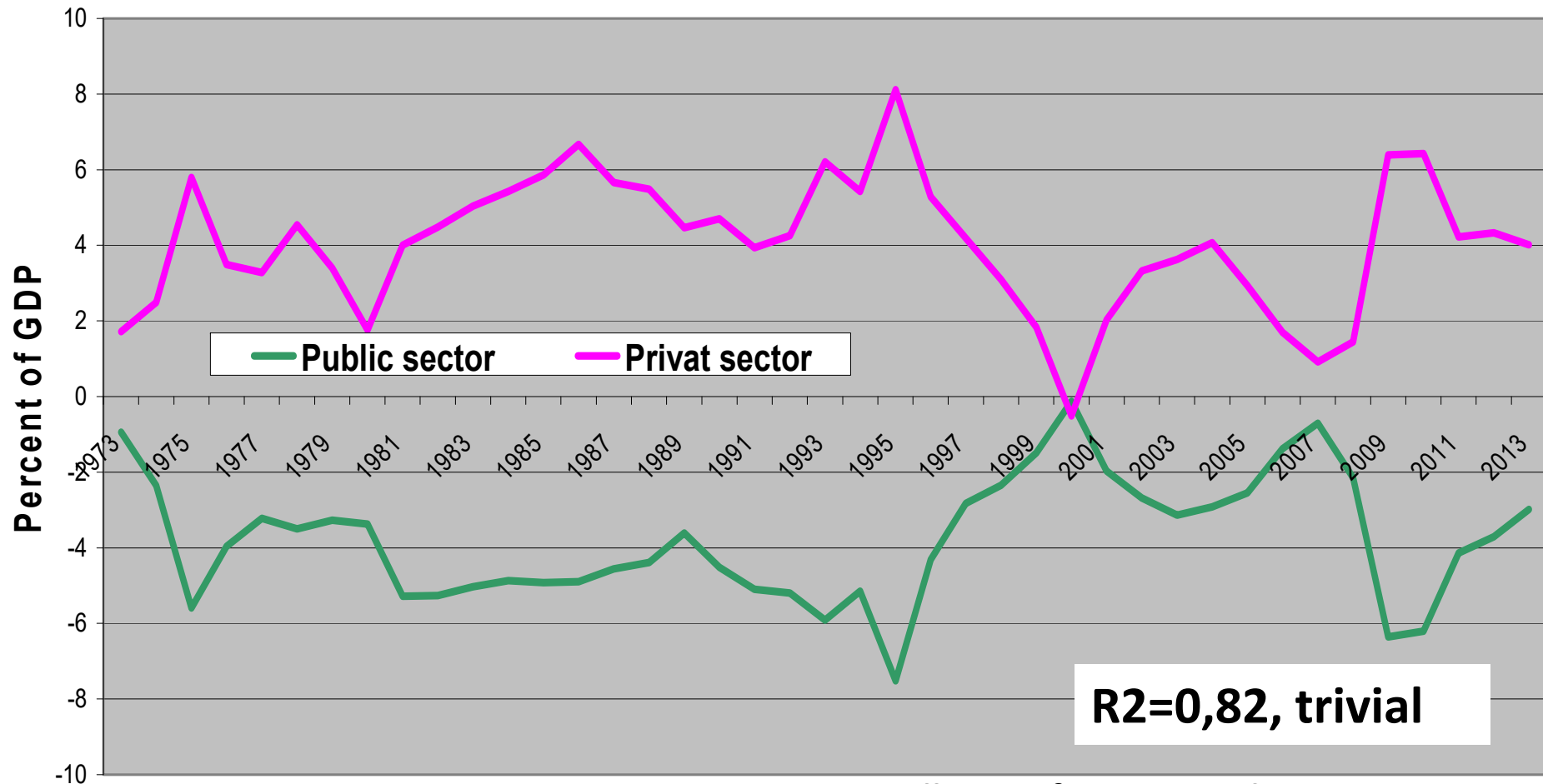
(3) Private **actual excess** savings:  $S_{px} \equiv Y - C - I - \text{Tax} \equiv [G - \text{Tax}]$

(4) Private actual **excess** savings  $\equiv$  public sector deficit

# EU(15): Getting causality right!

Private Sector surplus  $\Leftrightarrow$  Public Sector Deficit?

Excess Private saving  $\rightarrow$  public deficit (and foreign surplus)

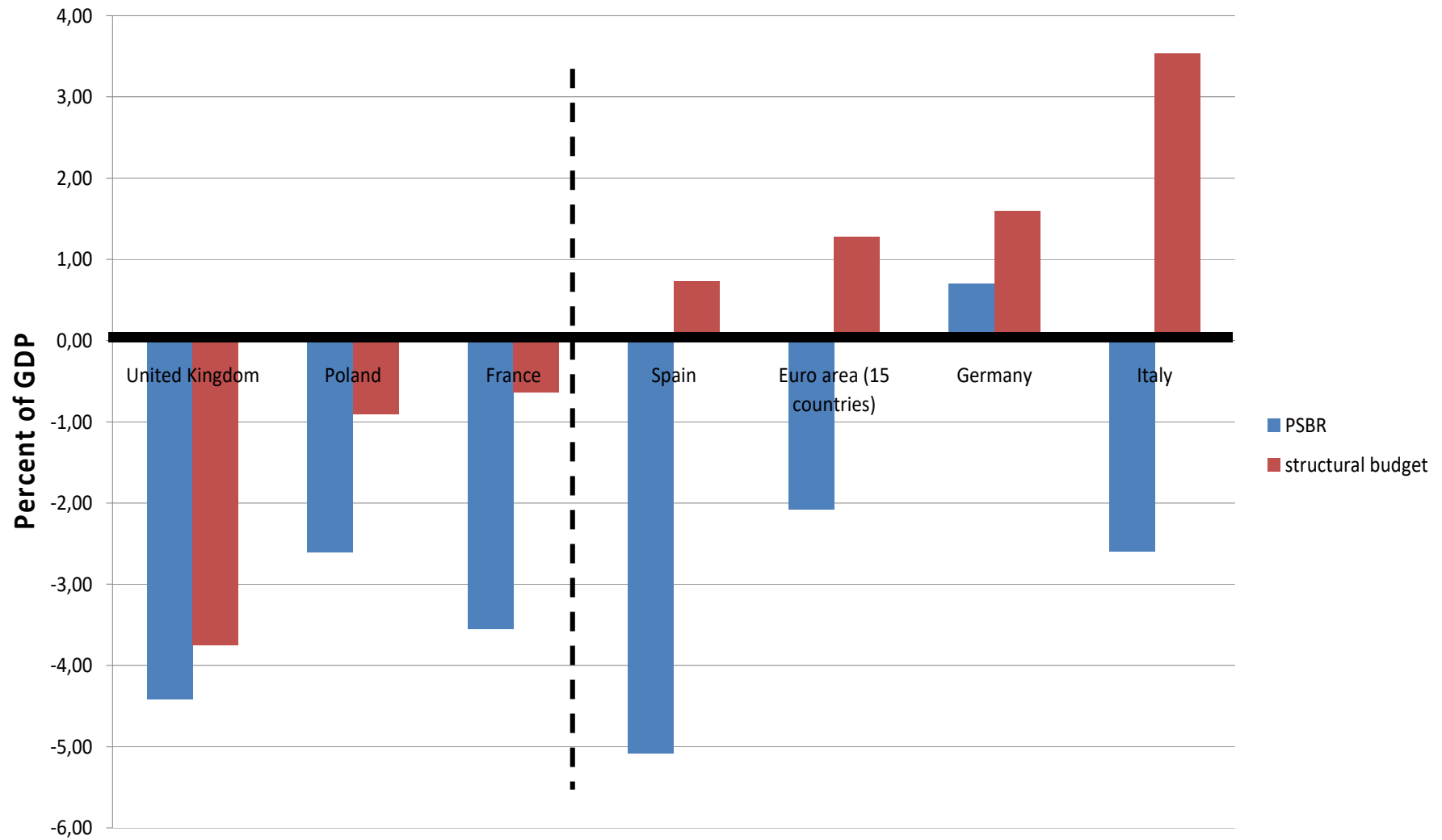


Source: OECD, Economic Outlook, no. 90 & 93

1. Collapse of private real investment
2.  $\rightarrow$  Unemployment
3.  $\rightarrow$  Public sector budget deficit



# Current Budget and Structural Budget, 2015



Source: OECD, Economic Outlook, 2016

Blue column: actual budget

# Limits to the public sector structural and actual budget is destabilizing!

The private sector is not self-adjusting to full employment – and for sure not within the euro-zone (semi-closed area)

So, the conventional calculation of the ‘structural’ public sector budget is only a measure of fiscal policy. (½ pct.)

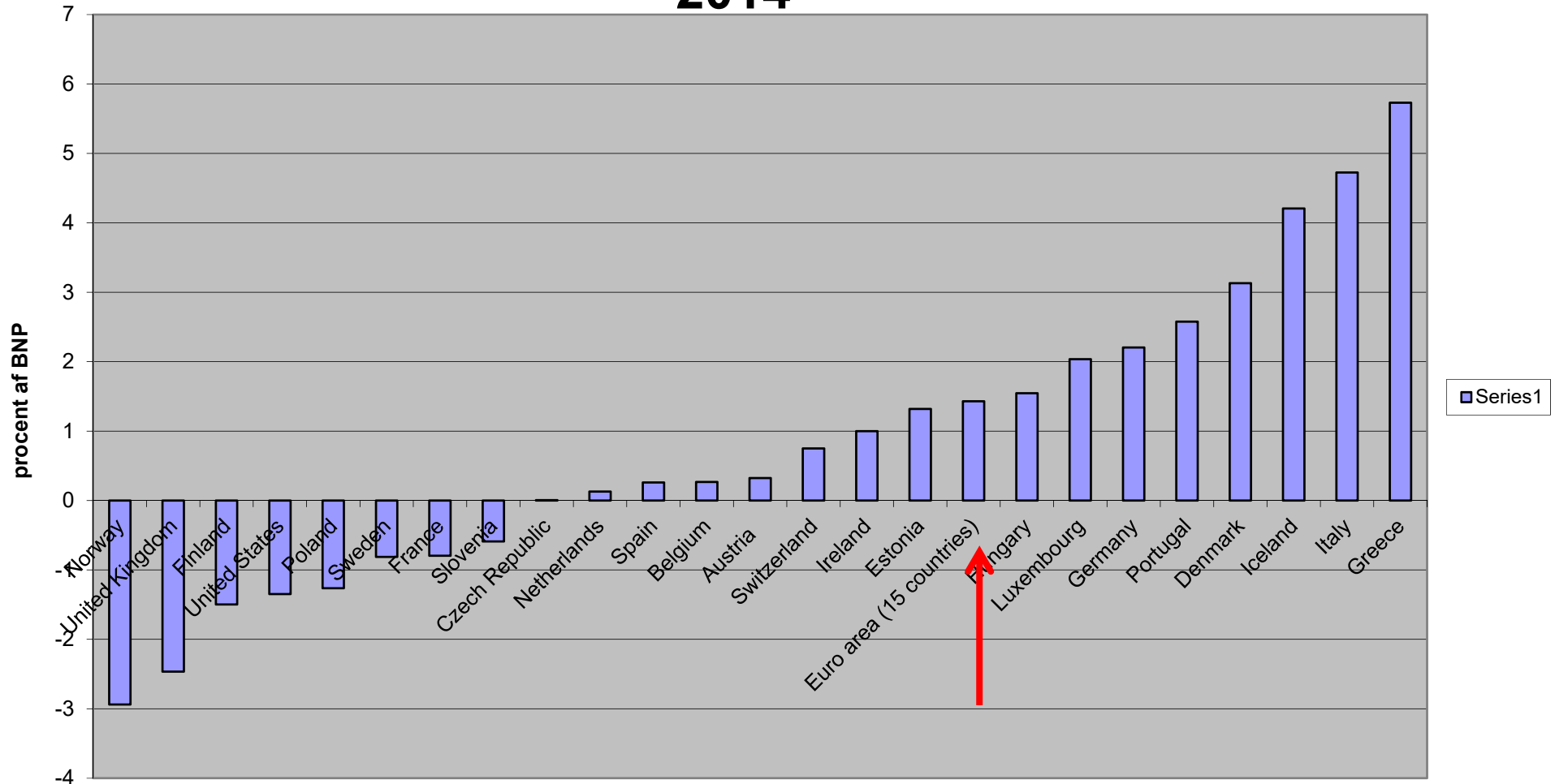
If it is ‘smaller’ than the current deficit – fiscal policy is too restrictive to create full employment.

The current deficit is just a mirror-picture of the lack of effective demand

The relevant calculation is: how much extra effective demand is needed to create full employment!

*What we see is an EU imposed Austerity Bias – adding to the stagnation*

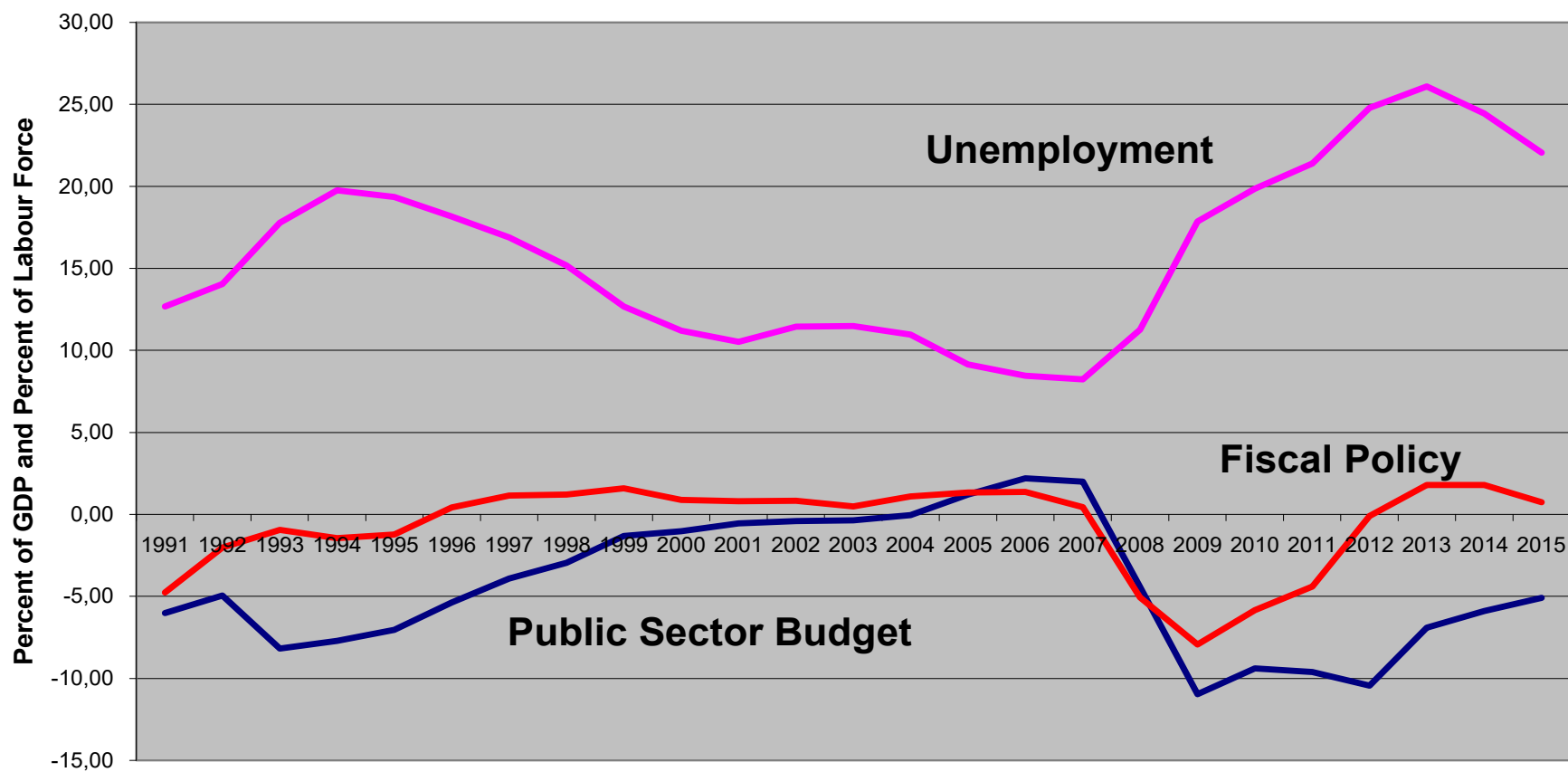
**Fiscal policy: underlying primary public budget, 2014**



Kilde: OECD, Economic Outlook

# A case study: Spain

## SPAIN: Unemployment, Public Sector and Fiscal Policy



Source:OECD, Economic Outlook, 2016

# Country-study

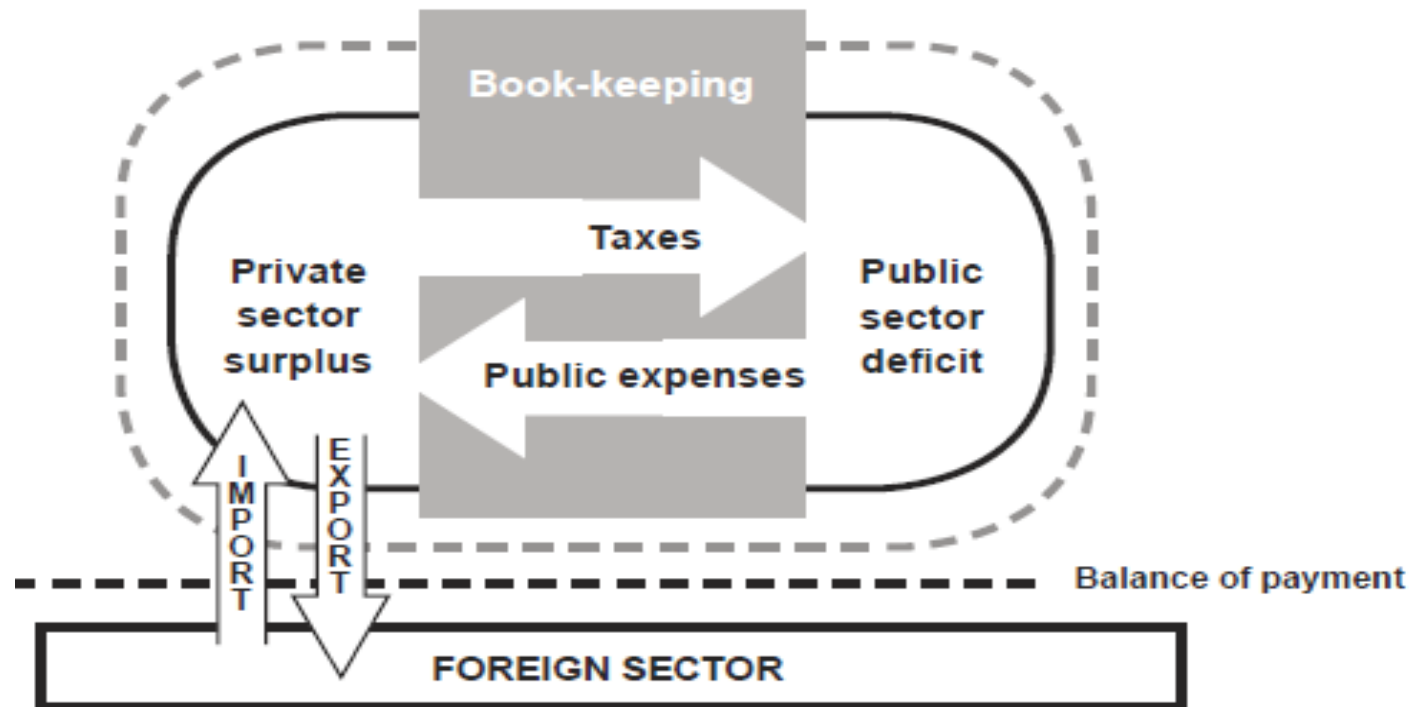
Why has Spain come out so much weaker than Germany during the crisis?

Balance of payments makes a difference!

# Three sector balances!

A consolidated three sectors model – open economy

Open economy: Private, public & foreign sectors



Book-keeping definition:

Private savings surplus = Public deficit + balance of payments surplus



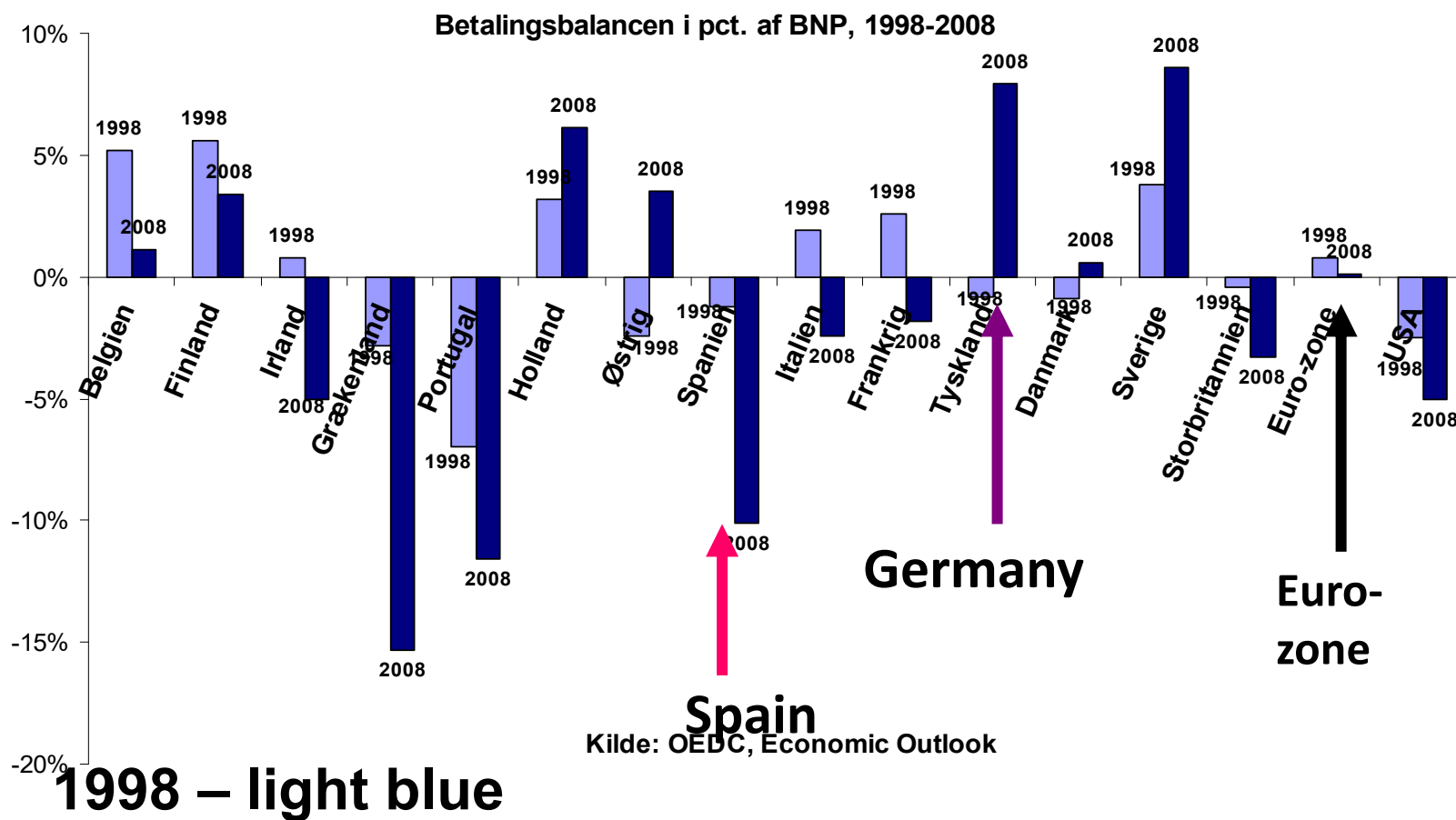
$$(1) \quad Y \equiv C + I + G + [E - M]$$

$$(3) \quad \text{Private excess savings: } S_{px} \equiv Y - C - I - \text{Tax} \equiv [G - \text{Tax}] + [E - M]$$

$$(4) \quad \text{Public sector budget deficit: } [G - \text{Tax}] \equiv S_{px} - [E - M]$$

**So, Public sector deficit  $\equiv$  Private excess savings + balance of payments deficit**

# Balance of payments imbalances



Kilde: OEDC, Economic Outlook

2008 – dark blue – **German surplus, €200 bill.**

Forthcoming, November 2016





# Accumulated wealth, 1998-2014

Bill. Euro	Priv. finans Wealth	Foreign Wealth	Public Debt
France	1673	25	1648
<u>Germany</u>	3260	1940	1320
Italy	2030	-147	2177
Spain	244	-647	891

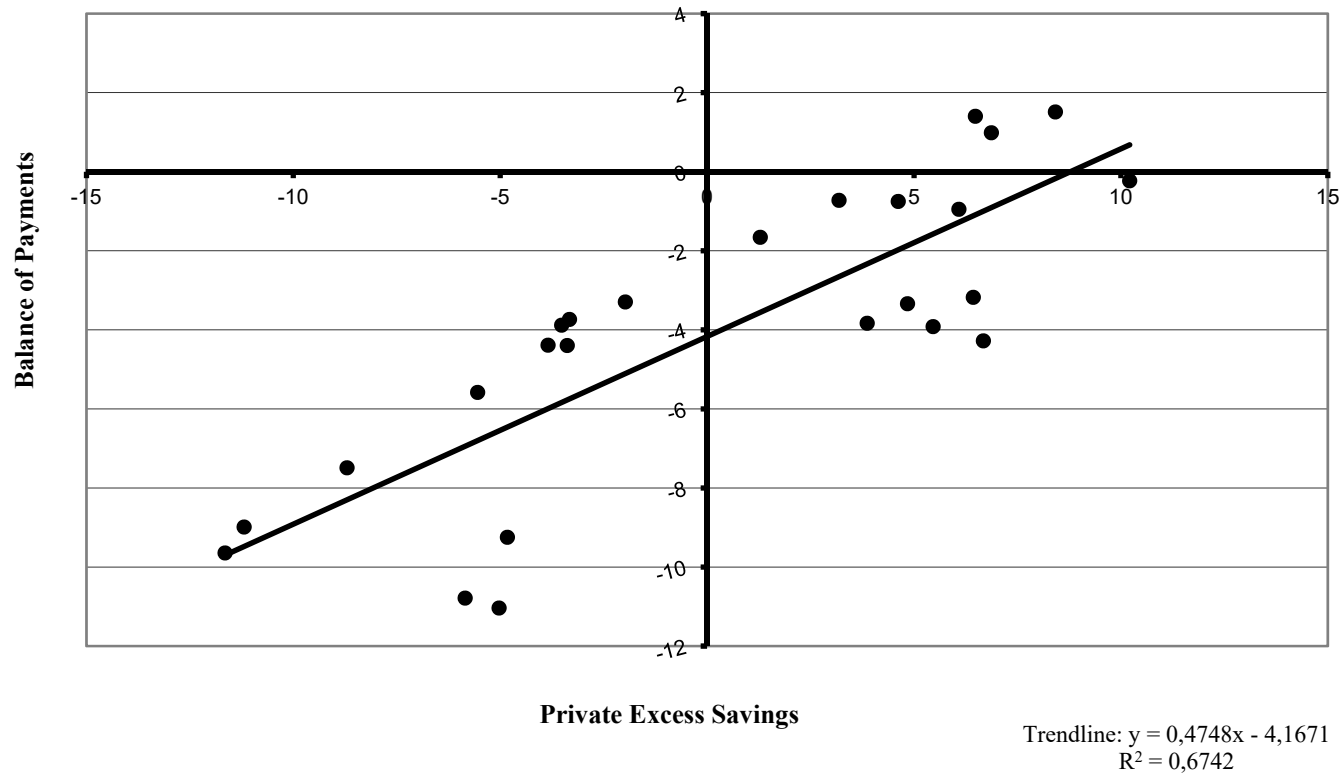
**Figure 5.A.1 Spain: private Savings=>Unemployment,  
1991<sup>30</sup>-2015**



Source: OECD Economic Outlook No. 99

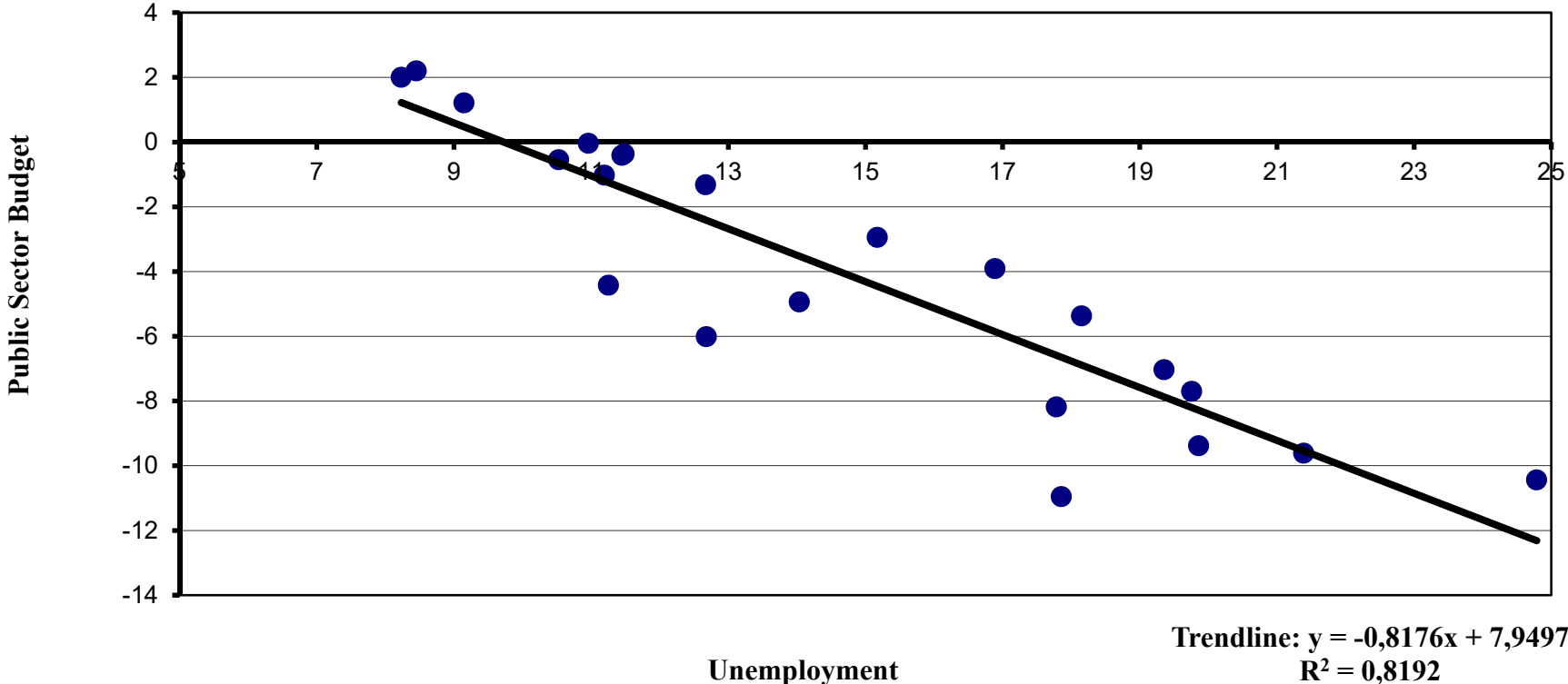
# Spain: Excess savings and B-o-P

Appendix 5.A.2. Spain: Private Excess Savings & Balance of Payment  
1991-2015



Source: OECD Economic Outlook No. 99

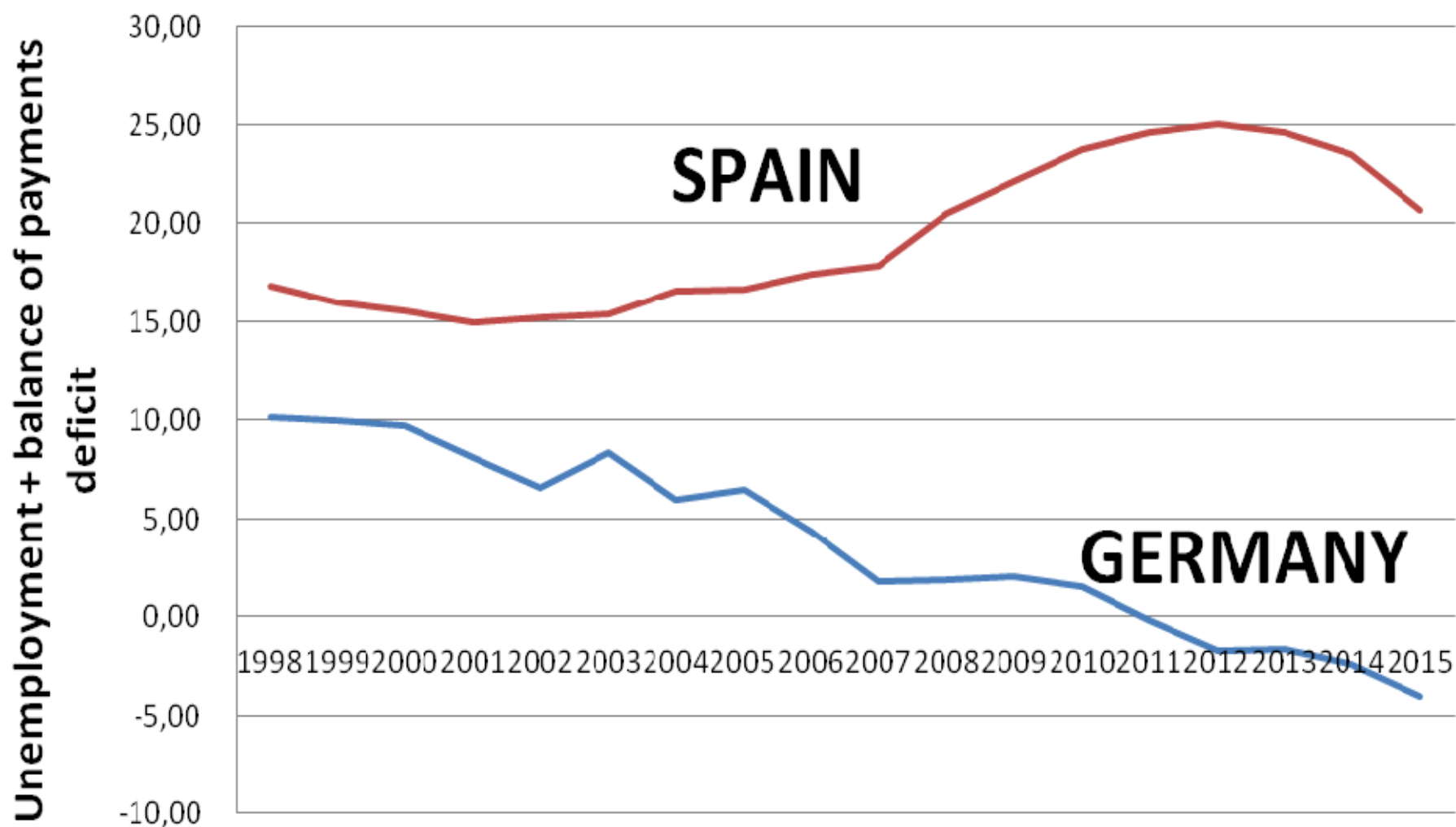
**Figure 5.A.3. Spain: Unemployment & Public Sector Budget, 1991-2012**



Source: OECD Economic Outlook No. 99  
Note: time period shortened due to changed fiscal policy

# Diverging Economies

## Macroeconomic Imbalances, Germany and Spain



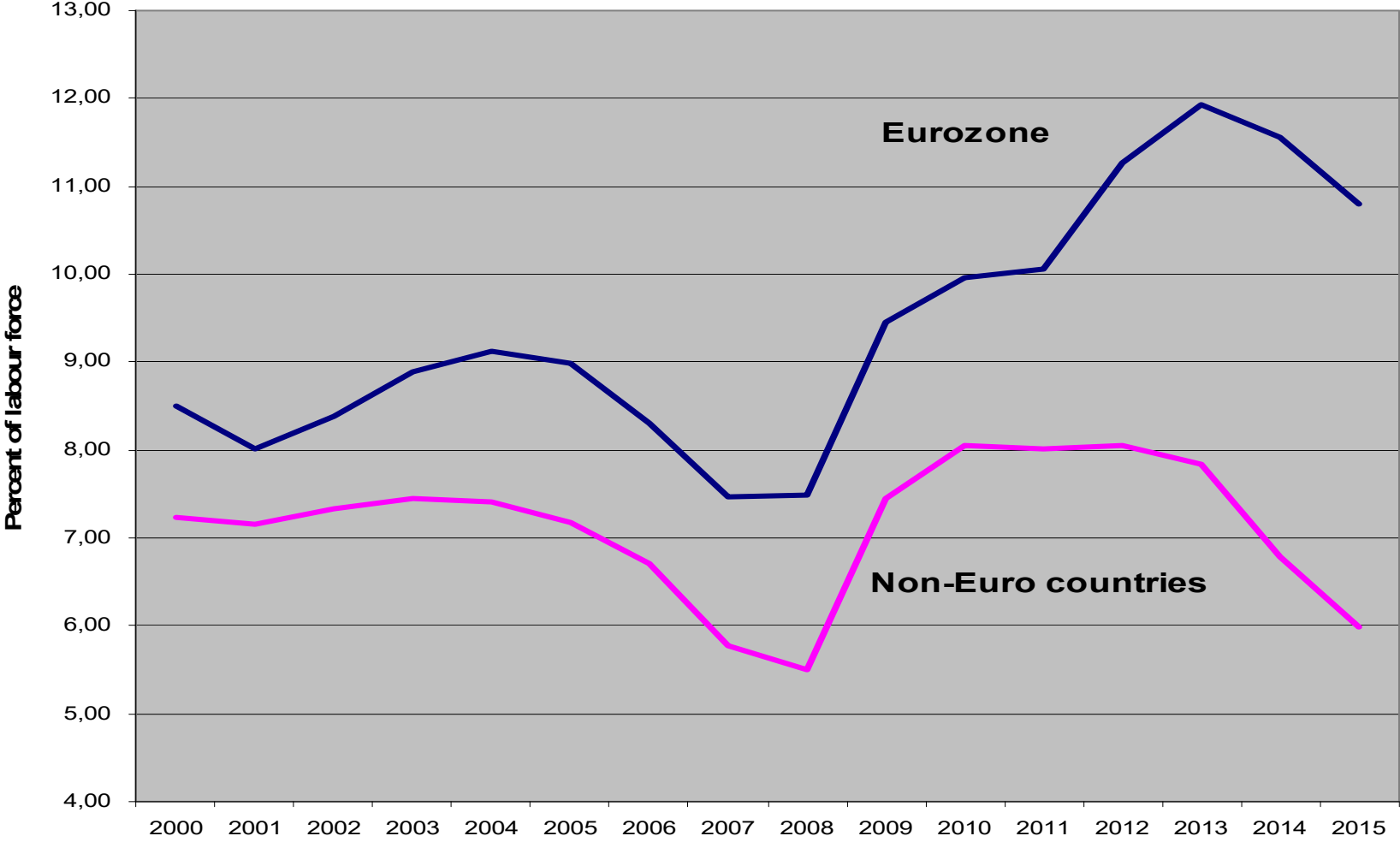
# Old Euro-stagnation

1. Falling rate of real investment
2. Private excess savings
3. Not counterbalanced by fiscal policy due to misunderstood macroeconomics
4. Balance of payments imbalances due to fixed exchange rates

**Thank you for your attention**

# Uneven development

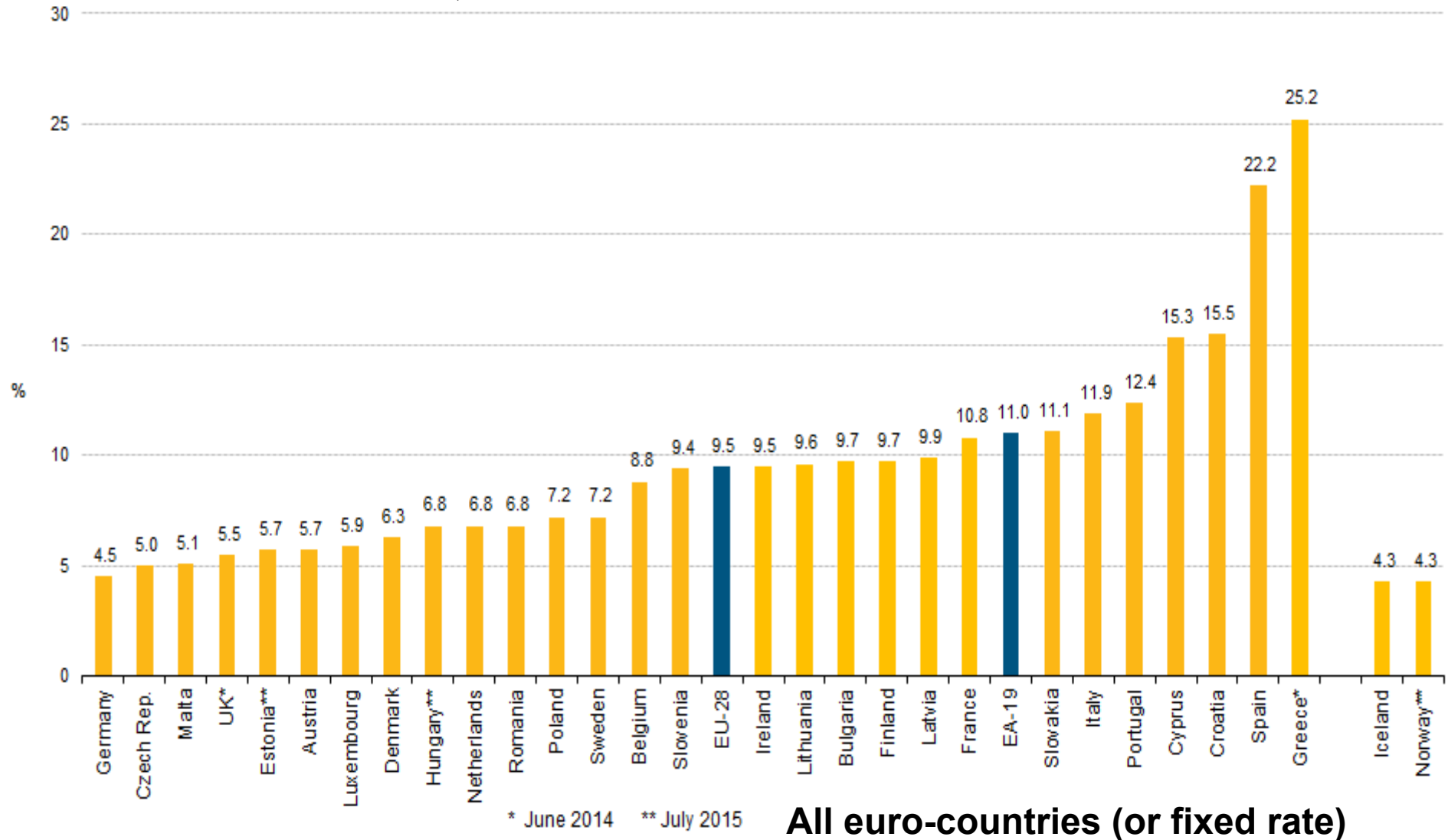
## Unemployment: Eurozone & non-eurocountries



Source: OECD, economic Outlook, June 2016



# Unemployment: high and unfairly distributed, 2015





## Inspiration from Keynes:

### How to analyse 'uncertainty'

← Keynes reading Mathematics and Philosophy in Cambridge 1902-05

His fellowship dissertation (1909) submitted to King's college was later (1921) published:

### **Treatise on Probability**

It demonstrates that Keynes was a highly sophisticated mathematician, but it also underscored his views about **uncertainty, knowledge and risk**.

Keynes understood that some risks could not be calculated or compared because they relied on assumptions about the future which had no basis in probability [or reality], which made these calculations simply wrong.

Source: <http://www.howtothinkaboutthefuture.com/?p=99>

**→ Jobs do not come by themselves!**