

# Handelsblatt

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## Time to seize new opportunities!

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The latest economic data confirms that the eurozone economy is currently expanding at a rapid rate. With economic growth of almost two percent, around 2,000,000 new jobs and a lower - albeit admittedly still high - unemployment rate of 9.2 percent, 2017 looks set to be the eurozone's best year since the crisis. The upward trend has taken all of the EMU countries with it and is being propped up increasingly by domestic demand, making it a more stable development.

It is, however, questionable how long the upswing will last. A great deal depends on how things develop in the United States and China, with both regions facing risks to their economies. Things could also slow down again in Europe itself, for example if the Brexit negotiations fail or familiar debt problems faced by some southern European countries come to a head again. None of these things can be predicted, but they cannot be ruled out either. Economic policy is not well prepared for risks like these.

In many countries, finance ministers have little leeway for expansive measures because sovereign debt has been edging up continually in recent years. And since the ECB's interest rates are still hovering below the zero mark, monetary policy, too, could only react by taking unconventional measures of questionable effectiveness.

As a result, now would be a good time to switch to a slightly more anti-cyclical economic policy and withdraw any existing economic impetus. The EMU member states should make the most of additional tax revenue generated on the back of economic growth - which Germany, too, has been generating for years now - to reduce their budget deficits instead of falling prey to the political temptation to ramp up spending even further.

This sort of preventative policy has been sorely absent to date. Any savings drives were seen primarily in the immediate aftermath of the financial crisis and were launched out of necessity in reaction to the euro debt crisis. This strategy had more of a pro-cyclical effect and led to a further reduction in demand. Over the last three years, efforts to reduce structural deficits have slowed down considerably again. The only savings made by governments have been due to the lower interest burdens driven mainly by monetary policy.

Countries like France, Spain and Italy still have high deficits despite significant improvements in their economic situation. The European Commission should be even more insistent when it comes to getting countries to whittle down their borrowing in order to create a certain degree of room for maneuver for the next economic slump.

The economic environment for the ECB's monetary policy has changed, too. The ECB appears to be stuck in the paradigm of the financial crisis and is procrastinating about when to break ties with its ultra-loose policy. Its continued doubts regarding the strength of the upswing and its belief that inflation is too low mean that it remains wedded to a path of "patience and consistency".

While it is true that the ECB has good reason to point out the risks still hanging over the sustainability of the upswing, which justify a very cautious strategy regarding its exit from the unconventional monetary policy, this cannot mean that it should keep doing everything in its power to stimulate the economy in an environment in which the economy and prices are recovering. This is, however, the only way of interpreting the ECB's ongoing bond purchases and its determination to remain in negative interest rate territory.

This sort of strategy not only creates risks – such as exaggerated valuations on the financial markets – but also considerably restricts the options available to the central bank to stimulate the economy if economic momentum tapers off. While a break with the very expansive monetary policy admittedly comes hand-in-hand with risks, such as soaring capital market yields, it should be possible to limit any increase in yields, especially given the ECB's reputation as a good communicator. What is more, it is important not to over-dramatize the impact of rising yields on the economy. Even if capital market interest rates in the eurozone were to double, they would still be well below the nominal pace of economic growth that acts as the benchmark for a neutral interest rate level in a long-term comparison. This pace of growth has come in at around 3.0 percent in the eurozone over the last two years. Interest rates that are considerably lower than this level provide the economy with expansive impetus.

This means that interest rates could rise without restricting economic growth. The upswing gives the ECB a chance to get its policy back to normal. EMU governments have an opportunity to make real progress with their debt reduction measures – an opportunity that they would now be well-advised to seize.