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Group Communications and Corporate Responsibility

Media Release

Euro Monitor: Economic tailwind but reluctance to reform

- Overall indicator reaches its highest level since 2001
- Decreasing reform momentum gives cause for concern
- Germany remains in pole position within the euro area
- Progress indicator for Germany declined

Munich, March 21, 2018

From an economic point of view, the eurozone could hardly be in better shape than it is today. The upswing seems likely to continue , the peak has just begun. This development is reflected in the results of this year's Euro Monitor, with which we measure the state of the euro economies on the basis of 20 indicators every year. The average rating for the euro area now stands at 6.8 points in the good midfield of the scale of one to ten. Furthermore, no EMU country is located in the critically defined depreciation area (1-4 points).

The strong improvement in the overall indicator since 2012 is not only due to the recent economic upswing, but also in particular to the crisis-related structural reforms of the labor and product markets in the former programme countries. Macroeconomic imbalances have been reduced and, above all, the internal adjustment mechanisms of the monetary union have been strengthened in the long term by higher wage and price flexibility. This should also increase the convergence of key macroeconomic variables, which is the most important prerequisite for a stable currency area. The Euro Monitor data supports this thesis. After the harsh setbacks in the crisis years, the economic rapprochement of the EMU members has intensified again. Although the development of the individual indicators was not uniform, according to our calculations the economic divergence between the national economies is even lower today than it was before the crisis.

“The thesis of many critics that the necessary adjustment processes in the euro area cannot take place due to political or social constraints can be refuted. The crisis of the years around 2012 was not caused by the monetary union itself, but triggered by the misguided policy mix in some countries, which in turn resulted in excessive debt, foreign trade deficits and a loss of competitiveness. The problem was not the currency, but economic and fiscal policy”, said Michael Heise, chief economist at Allianz.

However, in view of the remaining imbalances, such as the high public debt burden and high unemployment rates in many EMU member states, the clean-up process has not yet been completed. In the subdivision of indicators into longer-term levels and progress parameters, measuring progress in reducing weaknesses, it is clear that the level indicator 2017 alone contributed to the improvement of the overall indicator, while the progress indicator

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stagnated. The reasons for this are not only the economic upswing, but also the declining crisis mood and the ECB's expansionary monetary policy.

Heise: “There is some evidence that the eurozone is now more crisis-resistant and more stable than in 2007. Reform progress however has stalled since 2015. It is definitely too early for that. The economic tailwind should be used for reforms to arm the monetary union for worse times. The next downturn is bound to come.”

For the former crisis countries, this means further reducing the legacy burden of the crisis. The core EMU countries, on the other hand, should make up for the lack of reforms in recent years. This concerns mainly France, Italy and Belgium, which are at the rear end in our ranking, but also Germany and Luxembourg, which recently showed very little ambition for reform. In addition, measures at EMU level are needed to support national reform efforts. National reform efforts should be supported by measures at EMU level that promote convergence in the monetary area, such as better coordination of economic policies and (financial) incentives to implement structural reforms

Germany: Positive overall picture, but more progress should be possible

Germany managed to defend its top position in the overall eurozone ranking with an unchanged score of 8.1 points compared to 2016. At 8.9 points, Germany fares exceptionally well in the longer-term level indicator if we consider the country's low debt ratios, low labor market imbalances and a stable international competitive position.

Nevertheless, the momentum of reform in Germany is not that impressive. This is shown by the progress indicator: its score for Germany declined slightly to 7.3 (2016: 7.4). This places Germany only at a mid-field in ninth position within the eurozone. Germany has not been in such a modest position in the progress indicator since 2003 – a time when Germany was labeled the sick man of Europe

The most important results of the Euro Monitor 2017 in detail:

- Although the overall indicator has peaked since 2001, performance has not been consistently positive: Fifteen countries were able to improve on their rating in 2017 compared with 2016, with only four losing ground.
- In most countries, public-sector deficits and government debt ratio improved, as well as unemployment rates, employment growth and labor productivity. There were backward steps, however, in reducing structural budget deficits, export growth in relation to global trade dynamics and in reducing corporate debt.
- Germany remains in pole position within the euro area in terms of economic stability, with an overall score of 8.1 in 2017 - unchanged from the previous year. This is due, in particular, to the country's solid performance in the fiscal sustainability and private and foreign debt categories. The Netherlands is just behind Germany in second place with 8.0 points.
- France takes bottom position in our overall rankings this year with 5.4 points, just below Italy with 5.6 points, economic imbalances have widened.
- Shooting stars of the year: Looking at ranking improvements alone, the countries that moved up the most in the rankings were Austria and Ireland. Cyprus, on the other hand, made the biggest leap in terms of its overall score, which rose by 0.8 points to 6.2.

- As far as the level indicator is concerned, Germany leads the field with 8.9 points. Slovenia (8.4 points) and Malta (8.3 points), on the other hand, top the progress indicator table.
- The individual indicator that gave the most cause for concern in 2017 was again the unemployment rate (2017: 9.1%). The average EMU rating remains in the critical zone with four points, despite clear improvements in recent years.
- The best results were achieved in the current account indicator (average EMU rating: 10 points). Long-term development in unit labor costs, the budget deficit and the employment structure have also been positive on the whole.

Euro Monitor Rating 2017

Rank 2017	Country Code	EMU Member State	Rating 2017	Rank 2016	Rating 2016	Rank 2012	Rating 2012
1	DE	Germany	8.1	1	8.1	2	7.5
2	NL	Netherlands	8.0	2	7.6	8	6.4
3	SL	Slovenia	7.7	3	7.2	9	5.9
4	MT	Malta	7.5	4	7.1	10	5.6
5	AT	Austria	7.2	9	6.5	6	6.5
6	IE	Ireland	7.2	10	6.5	16	4.4
7	EE	Estonia	7.1	8	6.7	2	7.5
8	LT	Lithuania	7.0	7	7.0	1	7.8
9	LV	Latvia	6.9	6	7.0	4	6.9
10	SK	Slovakia	6.9	4	7.1	5	6.7
11	ES	Spain	6.6	12	6.4	14	4.7
12	LU	Luxembourg	6.5	10	6.5	7	6.4
13	FI	Finland	6.4	14	6.1	11	5.4
13	PT	Portugal	6.4	15	6.0	17	4.0
15	BE	Belgium	6.2	13	6.2	12	5.2
15	CY	Cyprus	6.2	17	5.4	19	3.7
15	GR	Greece	6.2	16	5.9	18	3.9
18	IT	Italy	5.6	19	5.3	15	4.5
19	FR	France	5.4	17	5.4	13	5.0
	EZ19	Eurozone	6.8		6.6		5.6

You can find the study on our homepage:
https://www.allianz.com/en/economic_research/publications/working_papers

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