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INTEGRATION AND CONVERGENCE IN THE EMU
A COMPLEX DYNAMICS

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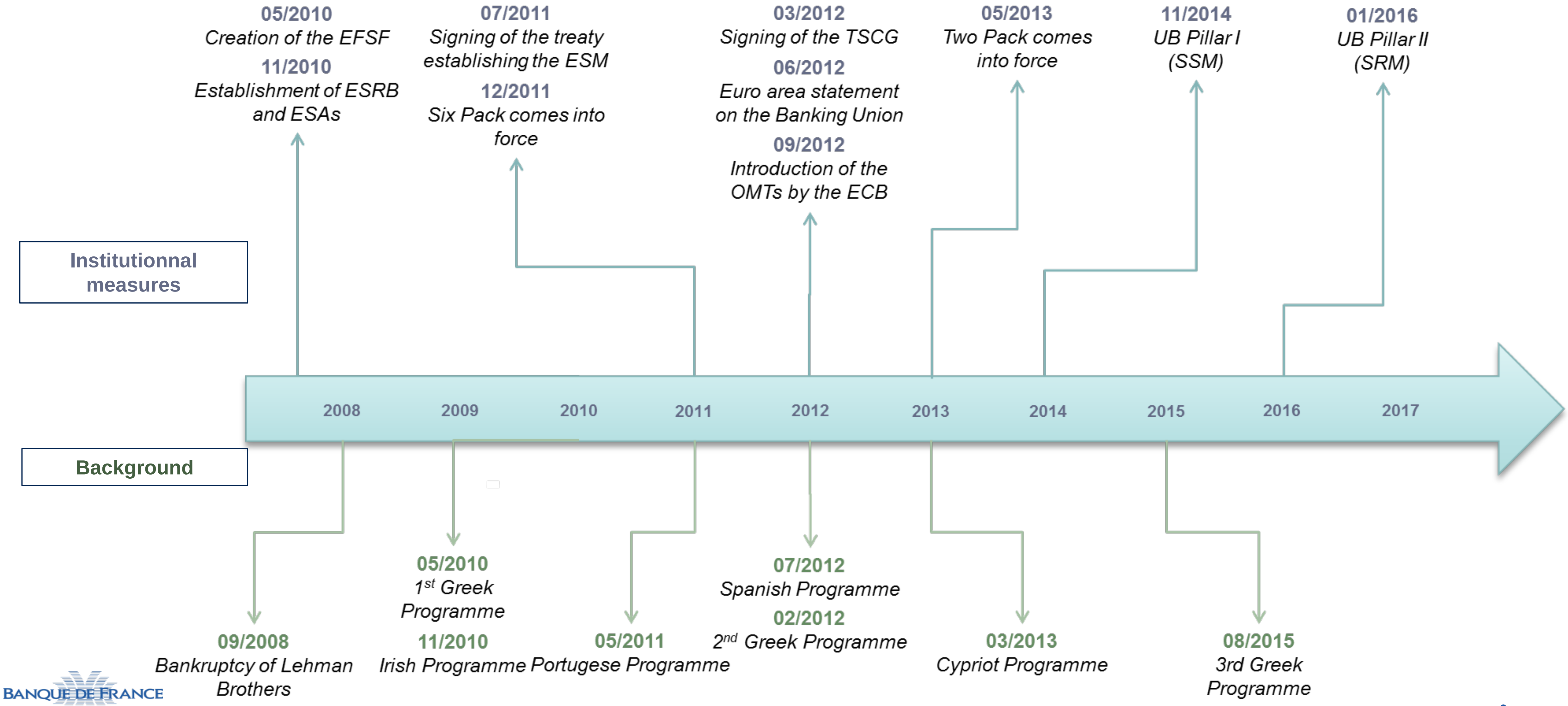
INSTITUTIONAL INTEGRATION : A LOT OF STEPS HAVE BEEN MADE SINCE (AND BECAUSE OF?) THE CRISIS

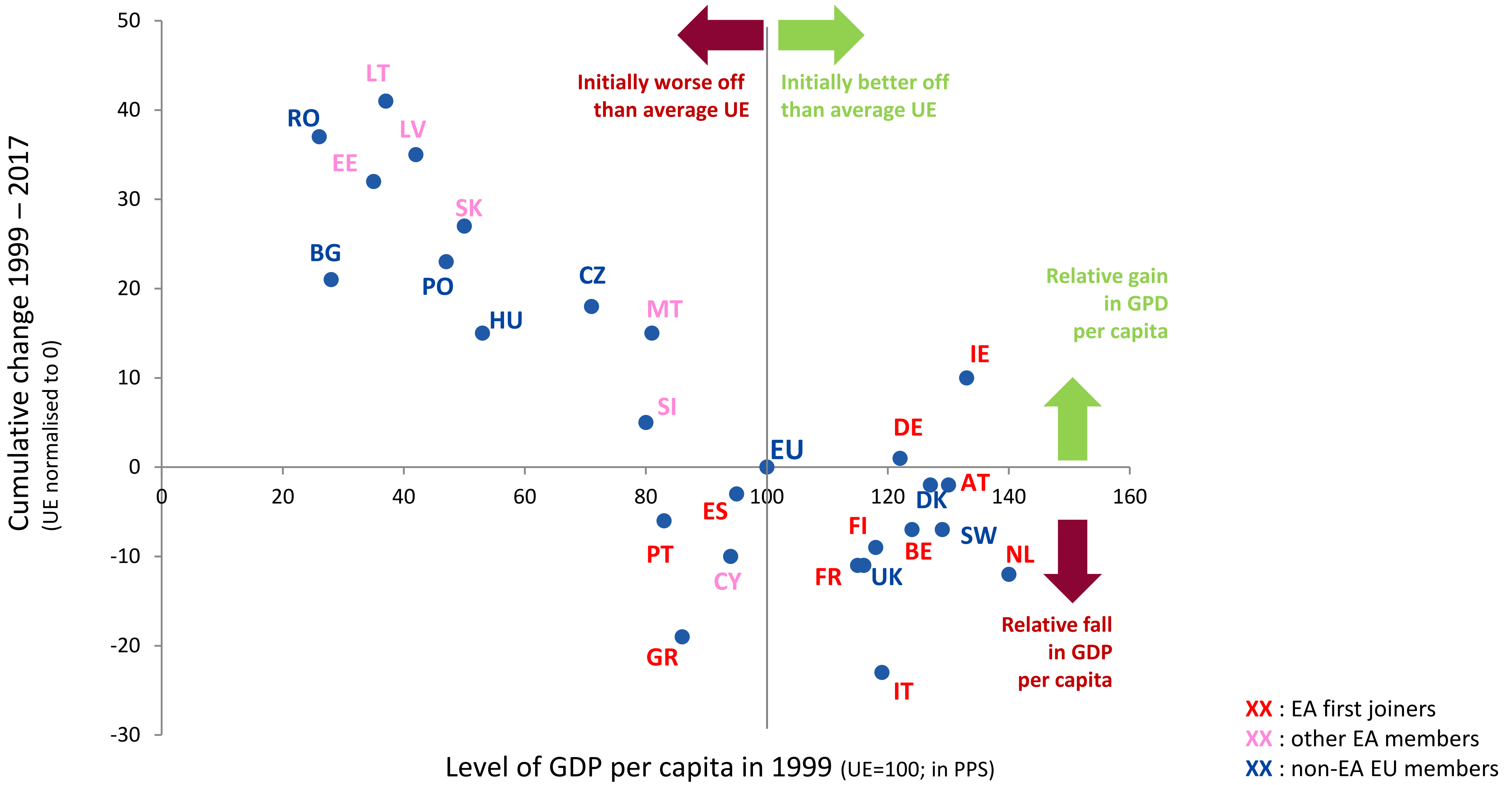


INSTITUTIONAL INTEGRATION: A LOT OF ADDITIONAL STEPS ARE IN THE PIPE BUT TWO STRONG RED LINES REMAIN

- The Meseberg roadmap:
  - Public backstop to the Single Resolution Fund (SRF)
  - European Deposit Insurance Scheme (EDIS)
  - Eurozone budget to promote competitiveness, convergence and stabilization
  - Unemployment insurance stabilization fund (without permanent transfers)
  - Further progress on Capital Markets Union…

- Current (and strong) red lines:
  - Debt mutualization
  - Permanent public transfers

EU REAL CONVERGENCE: WHERE DO WE STAND NOW?



Source: ECB, Banque de France calculations

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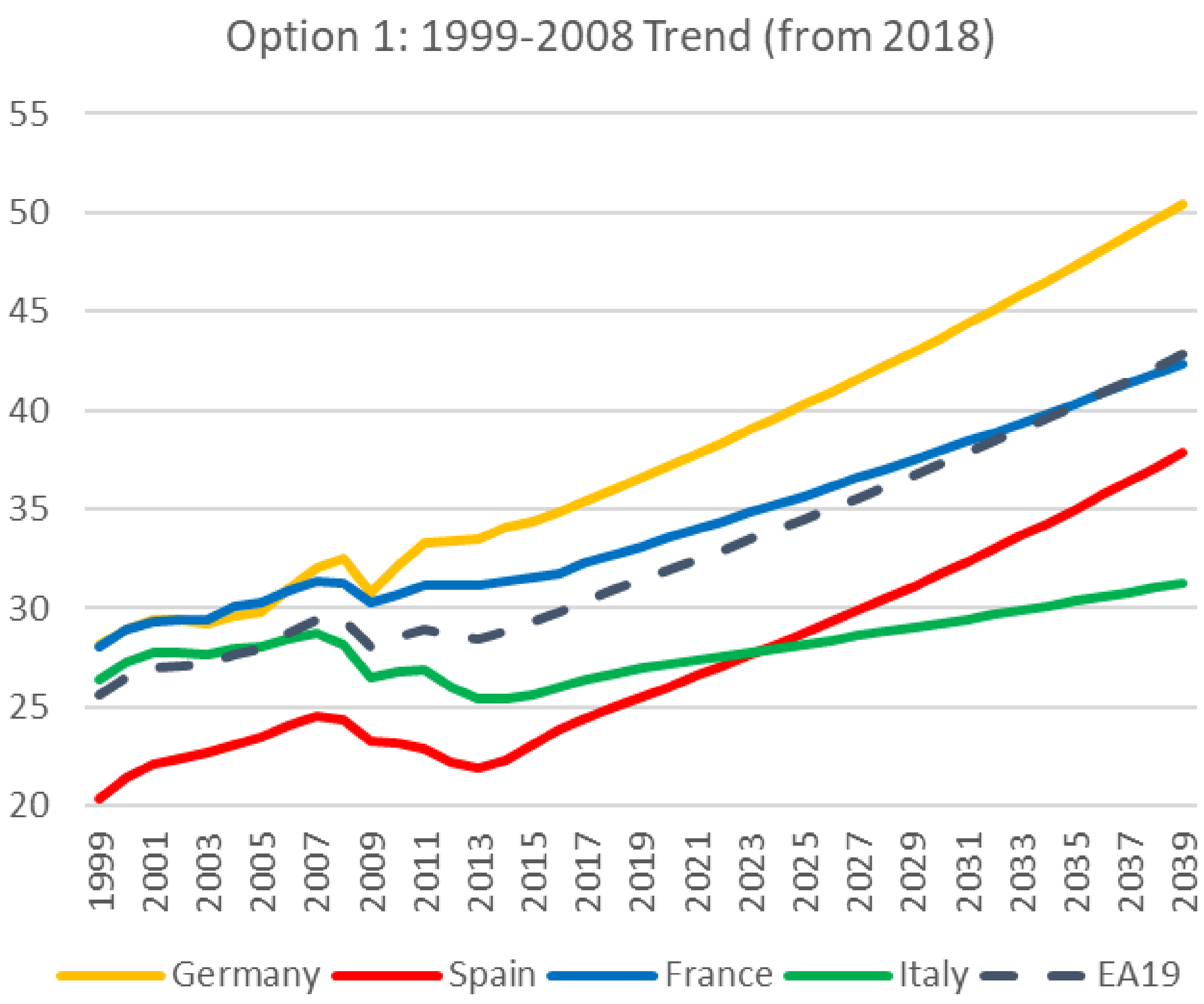
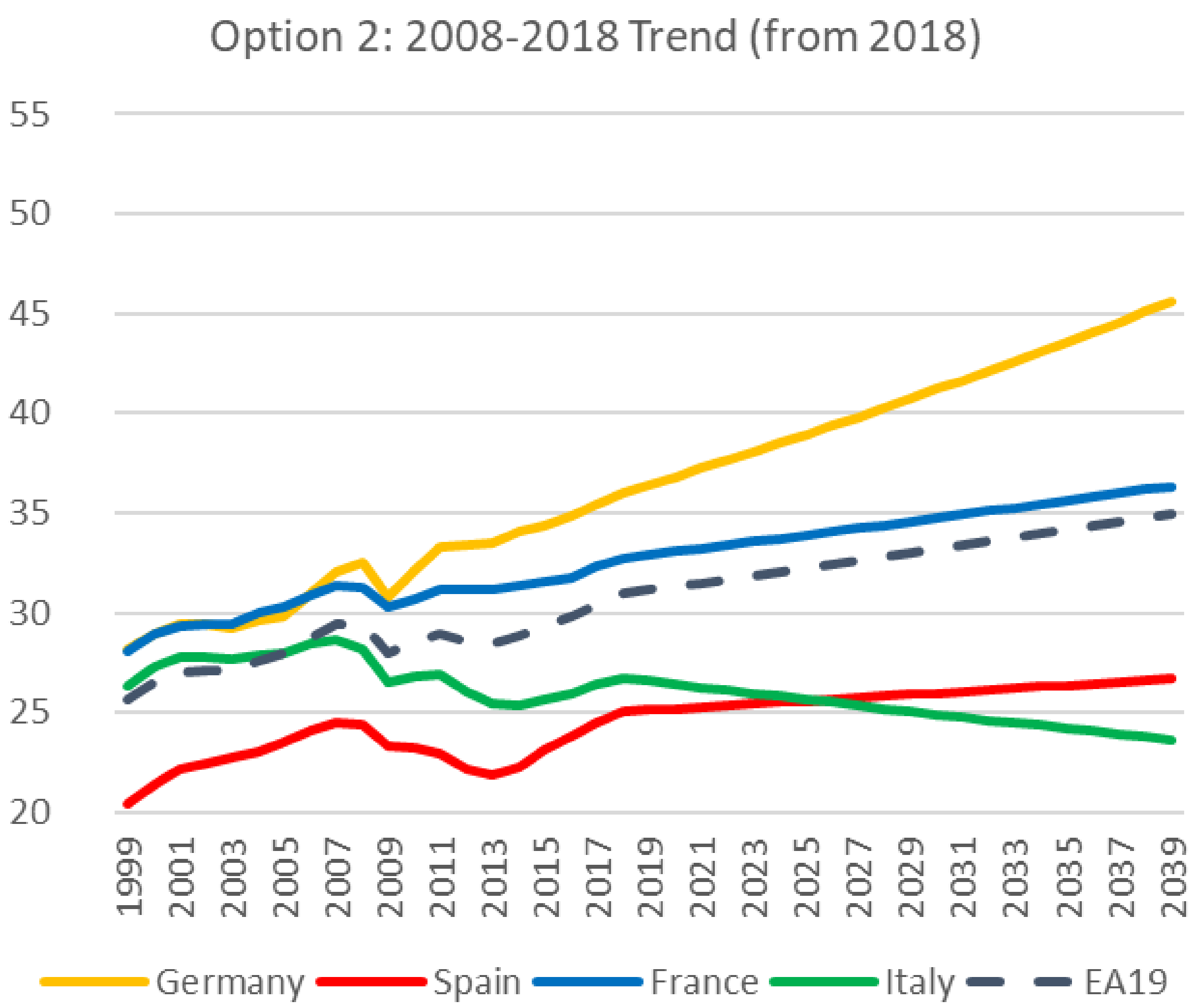
20 YEARS AHEAD : FURTHER REAL DIVERGENCE ?
(GDP PER CAPITA, CONSTANT PRICES – 2010 REFERENCE LEVELS)





Source: Ameco, BDF calculations

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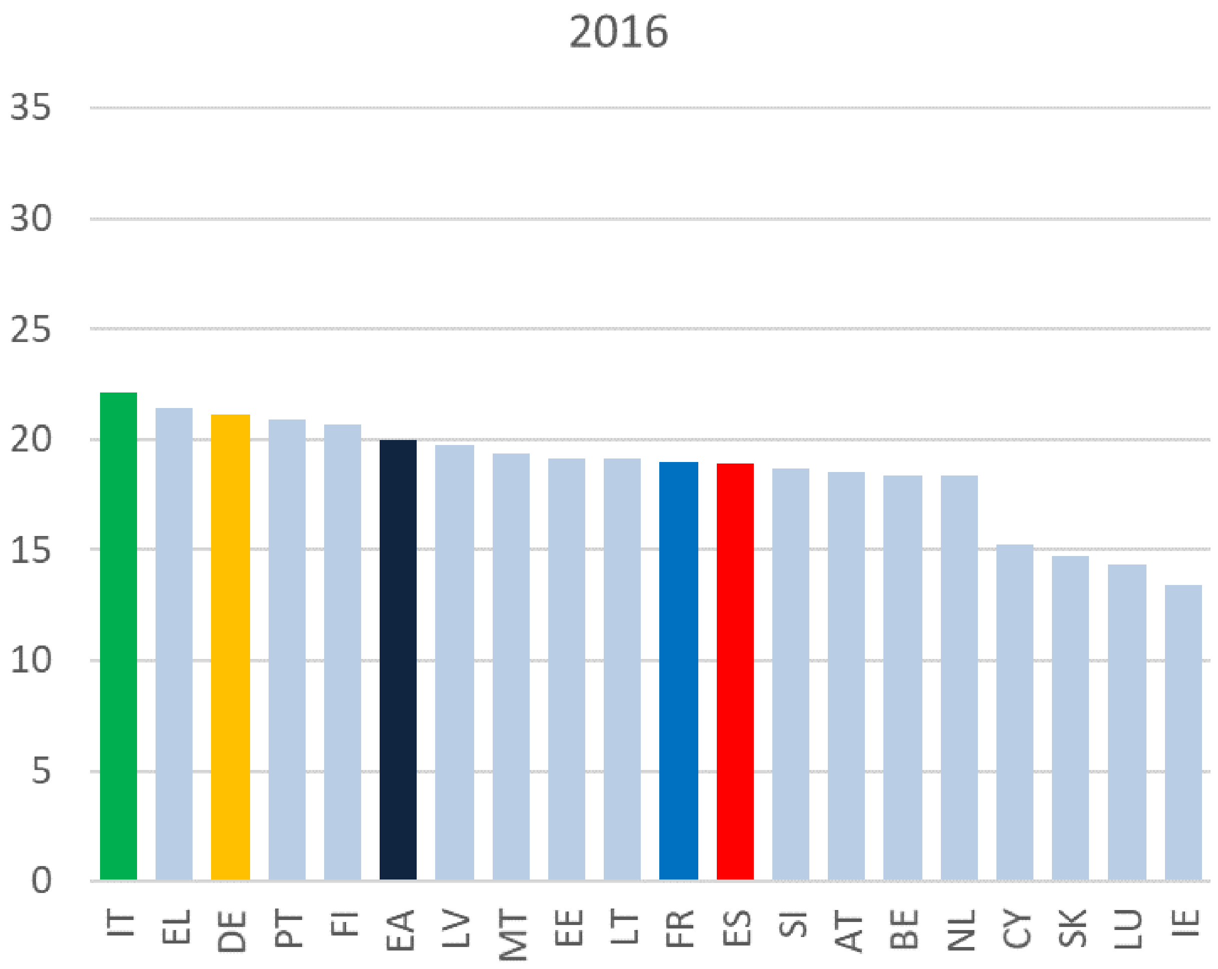
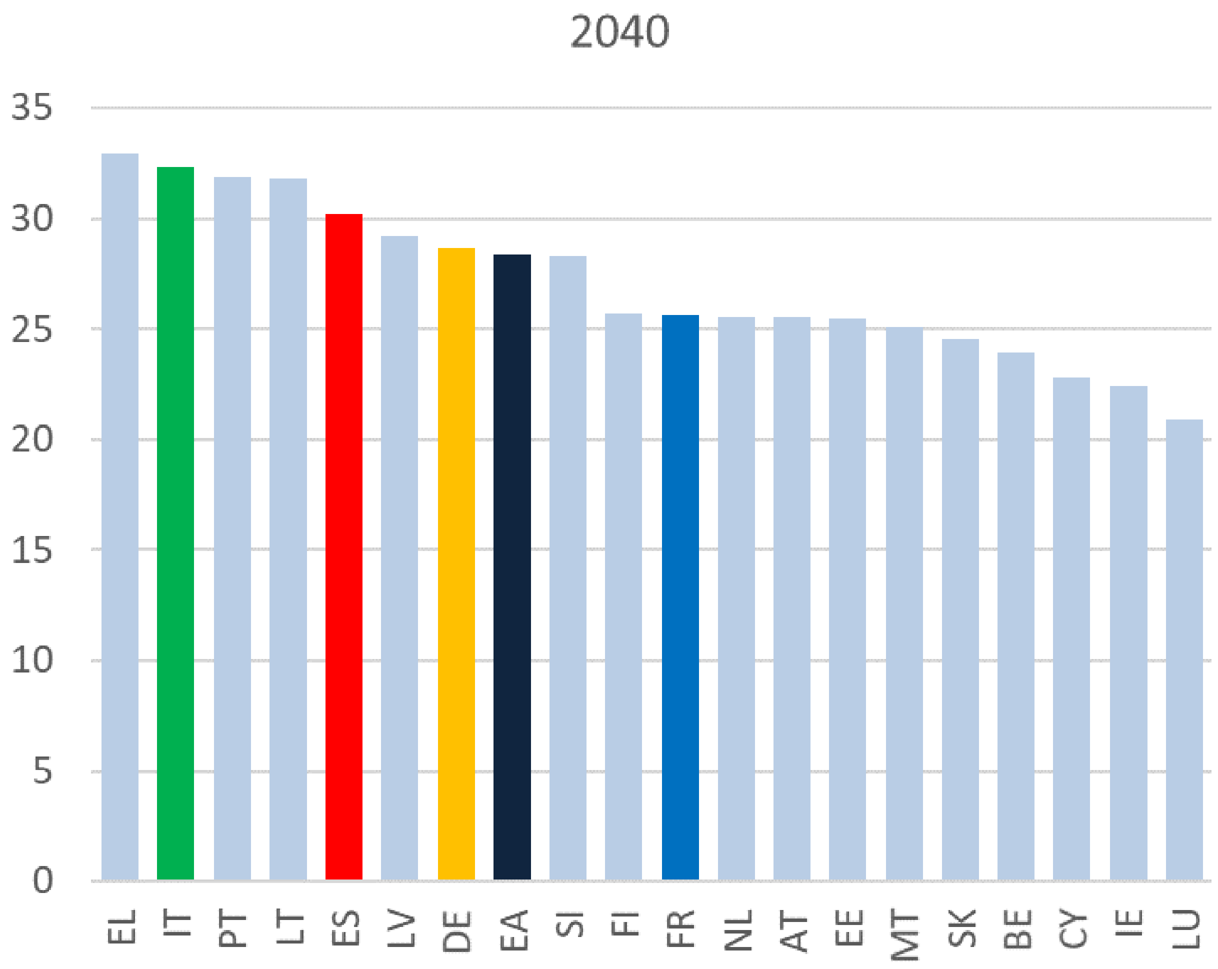
RISE OF OLD-AGE DEPENDENCY RATIO EVERYWHERE, BUT INCREASING DIVERGENCES (65 AND OVER, % OF TOTAL POPULATION)





Source: Ageing report (2018)

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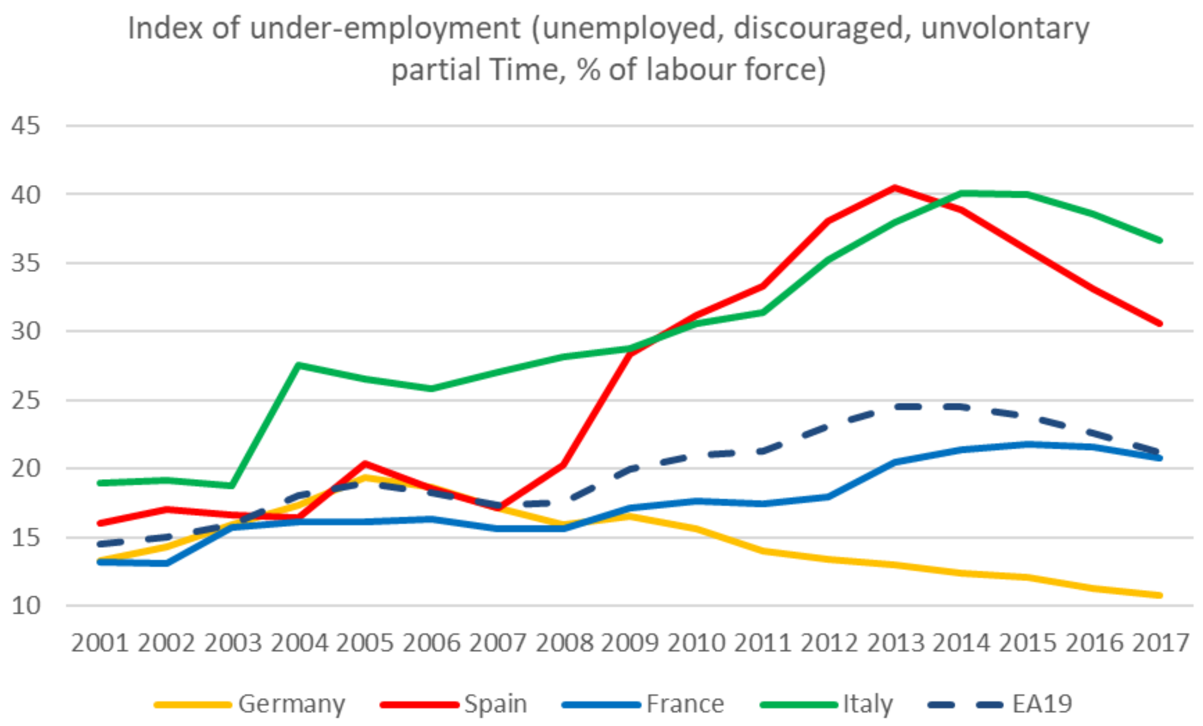
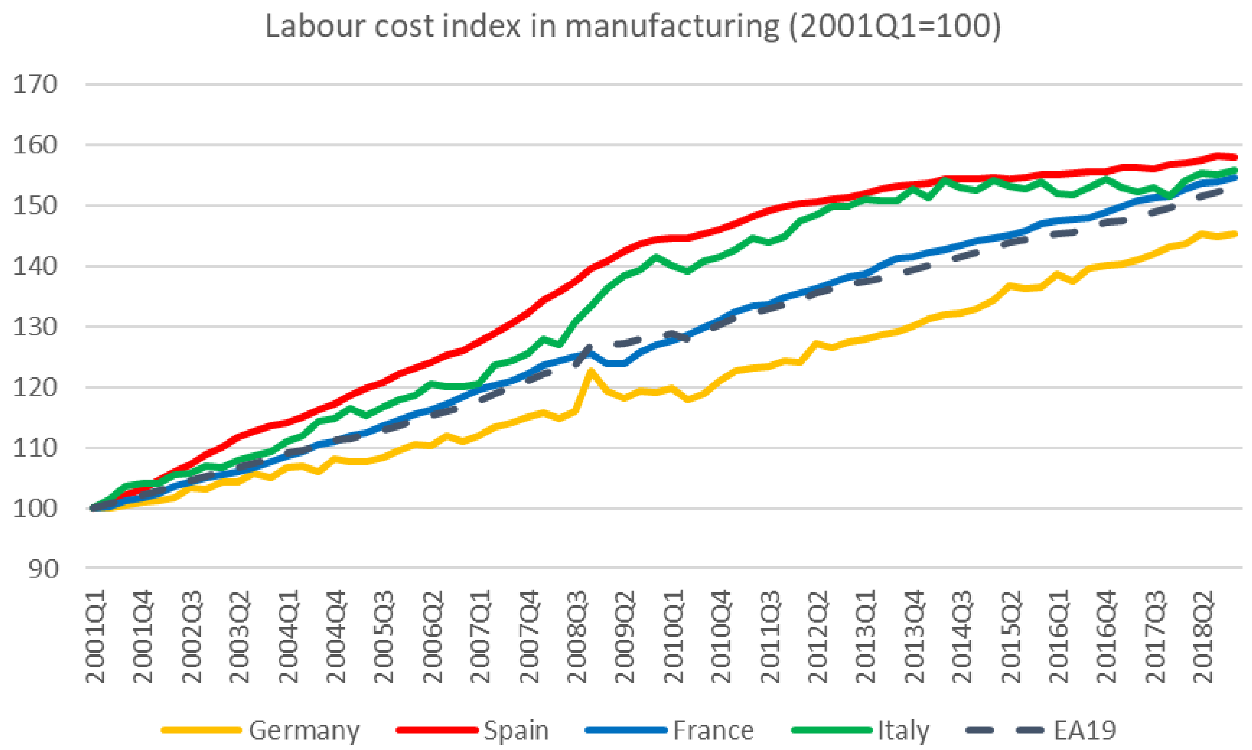
REAL DIVERGENCE, HOW MUCH IT MATTERS?

- If there is perfect intra EA labour mobility, real divergence becomes **only a problem of territory planning**

- In this case, limited additional needs of intra EA transfers
  - Transfers for public investment in infrastructures (but no need of change of scale of European Structural and Cohesion Funds)
  - Some mutualisation of public education costs at least during the transition period
  - But legacy problems (public debt)
- And need of structural reforms to facilitate labour mobility
  - Cross-border pensions right portability is key

WEAK INTEGRATION OF LABOUR MARKETS





Source Eurostat, BDF calculations (unemployed, discouraged, unvolontary partial Time, % of labour force)

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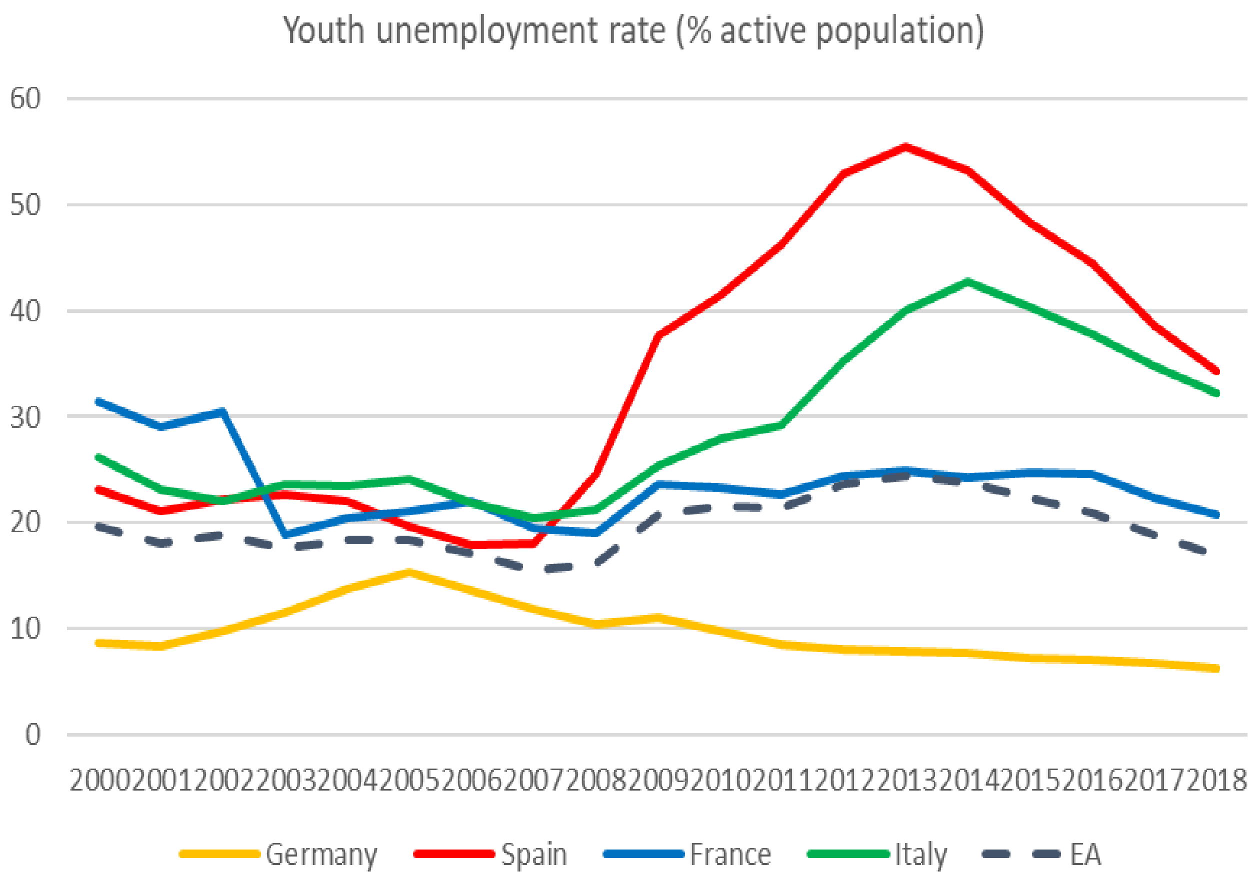
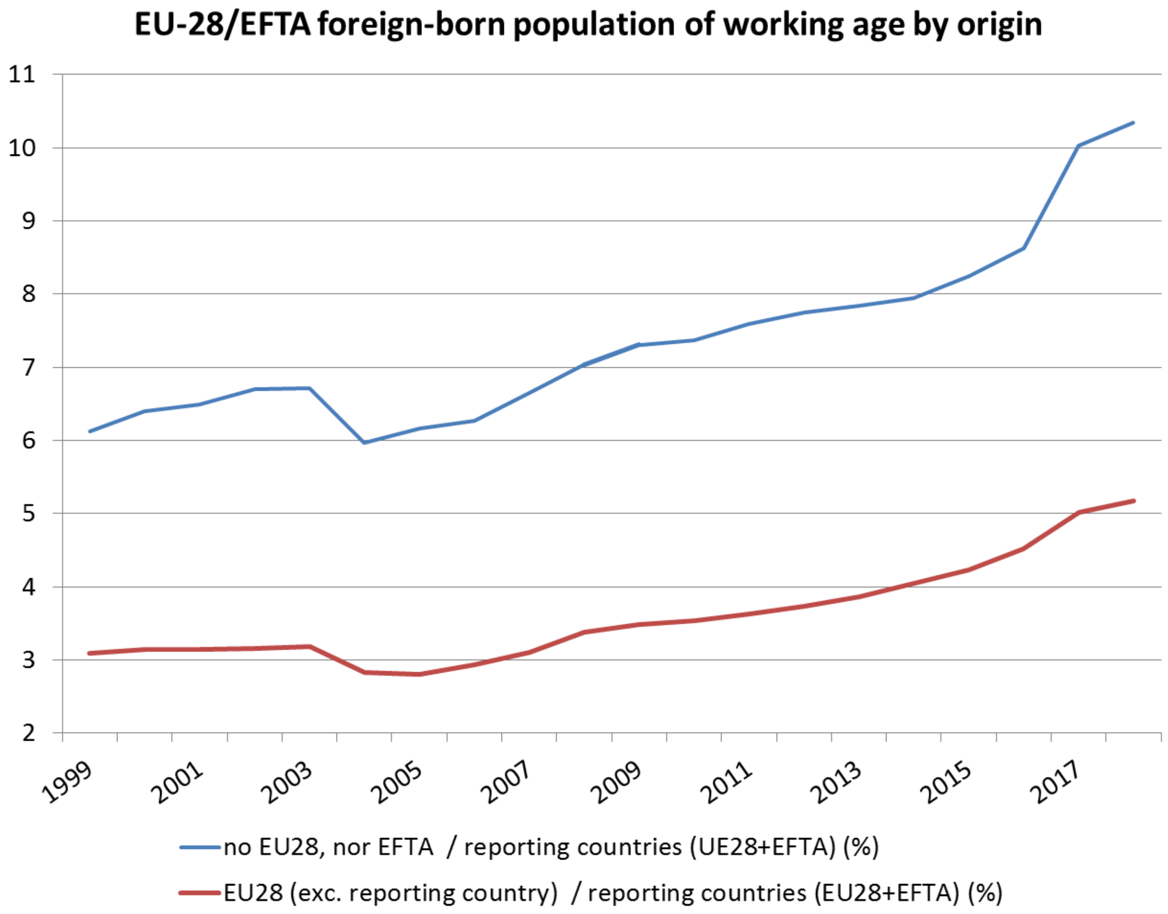
WEAK INTEGRATION OF LABOUR MARKETS



Source: Ameco



Source: Eurostat

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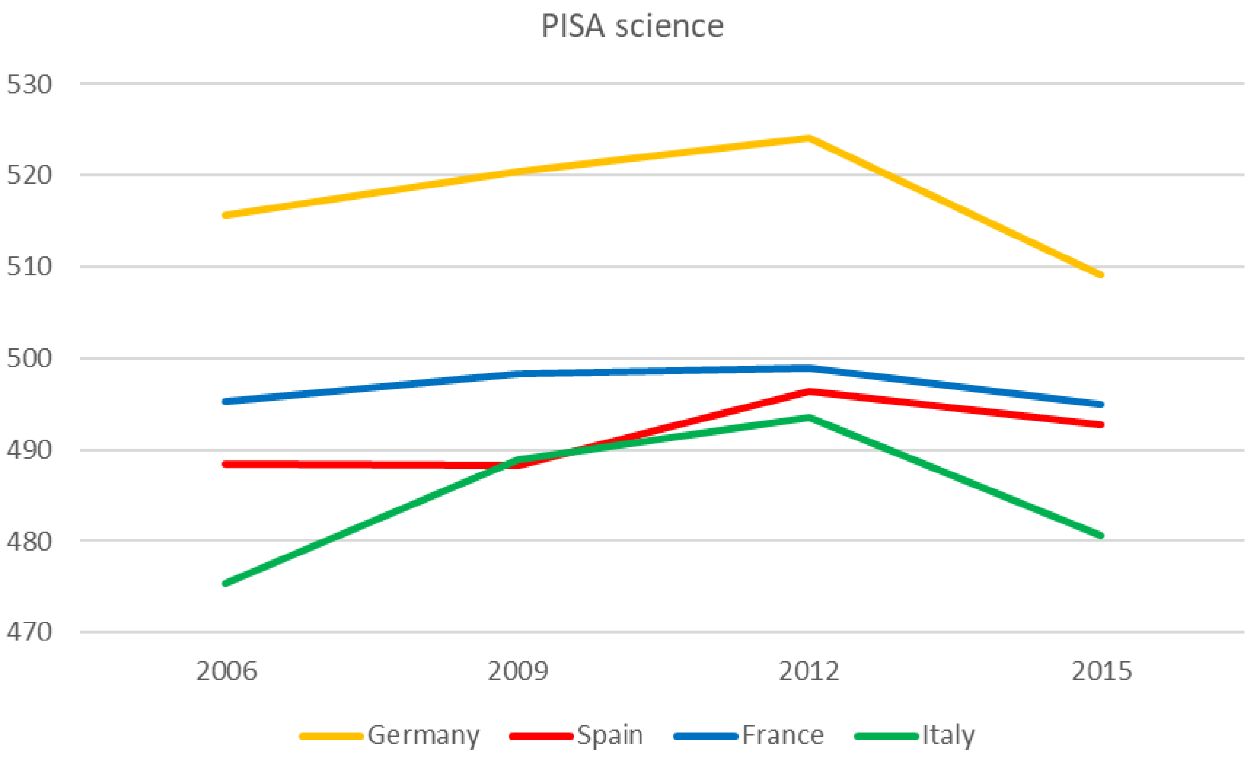
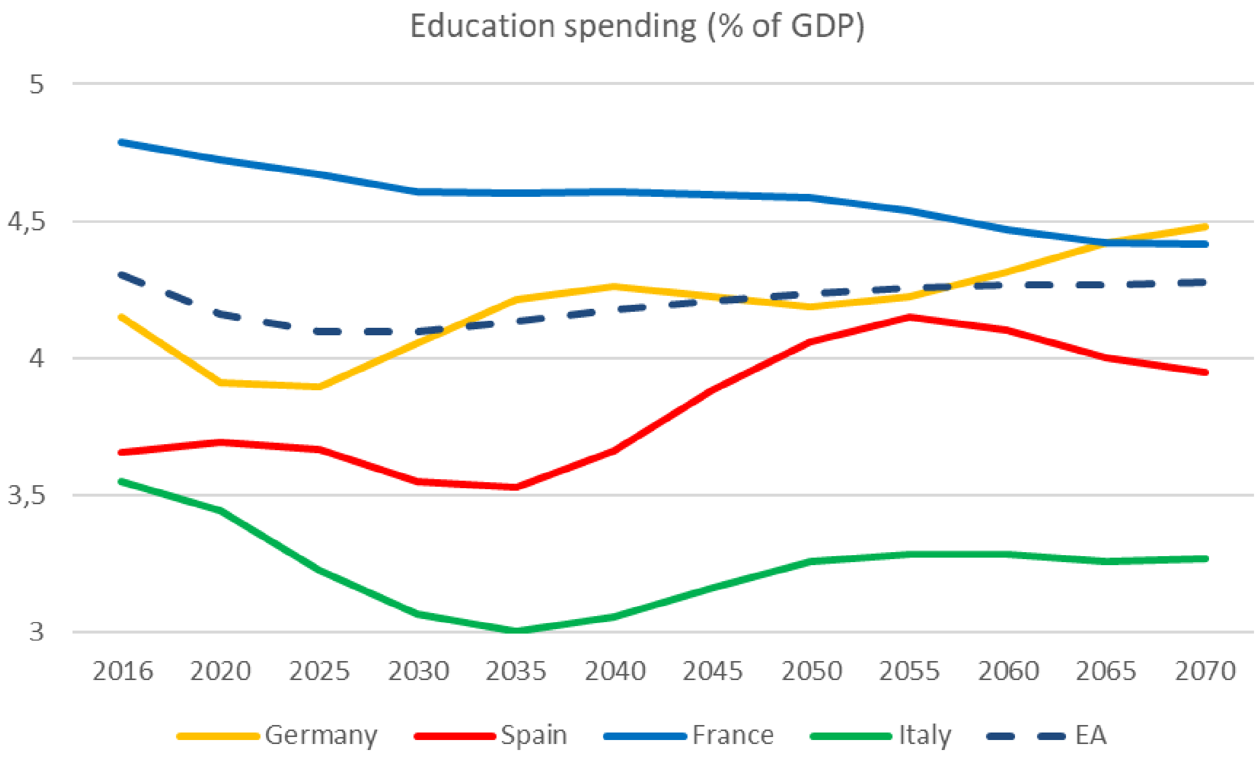
EDUCATION : HETEROGENEITY OF LEVEL AND SPENDINGS



Source: OECD



Source: Ageing report (2018)

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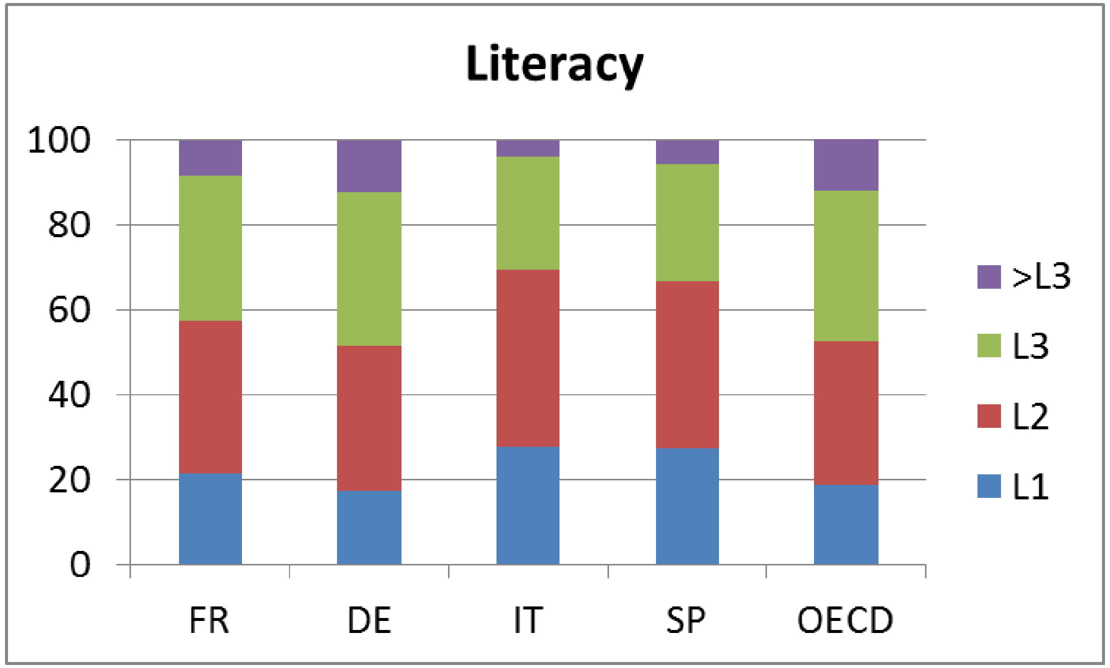
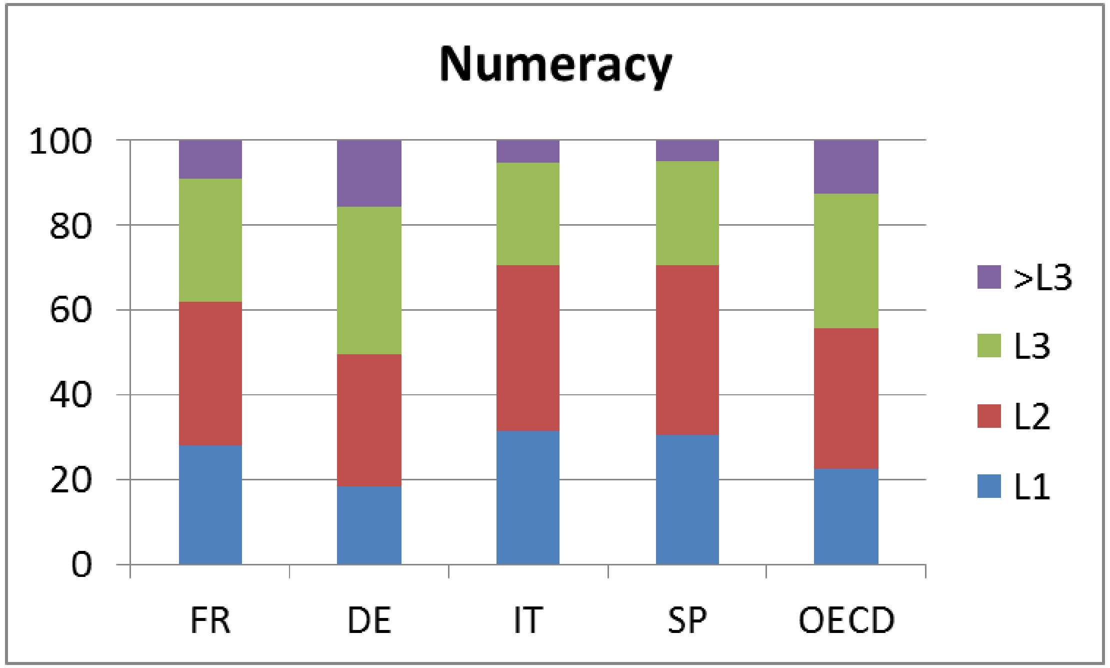
EDUCATION : HETEROGENEITY OF ADULT SKILLS - PIAAC DATA (2016)

Percentage of adults scoring at each proficiency level in literacy and numeracy





REAL DIVERGENCE, HOW MUCH IT MATTERS?

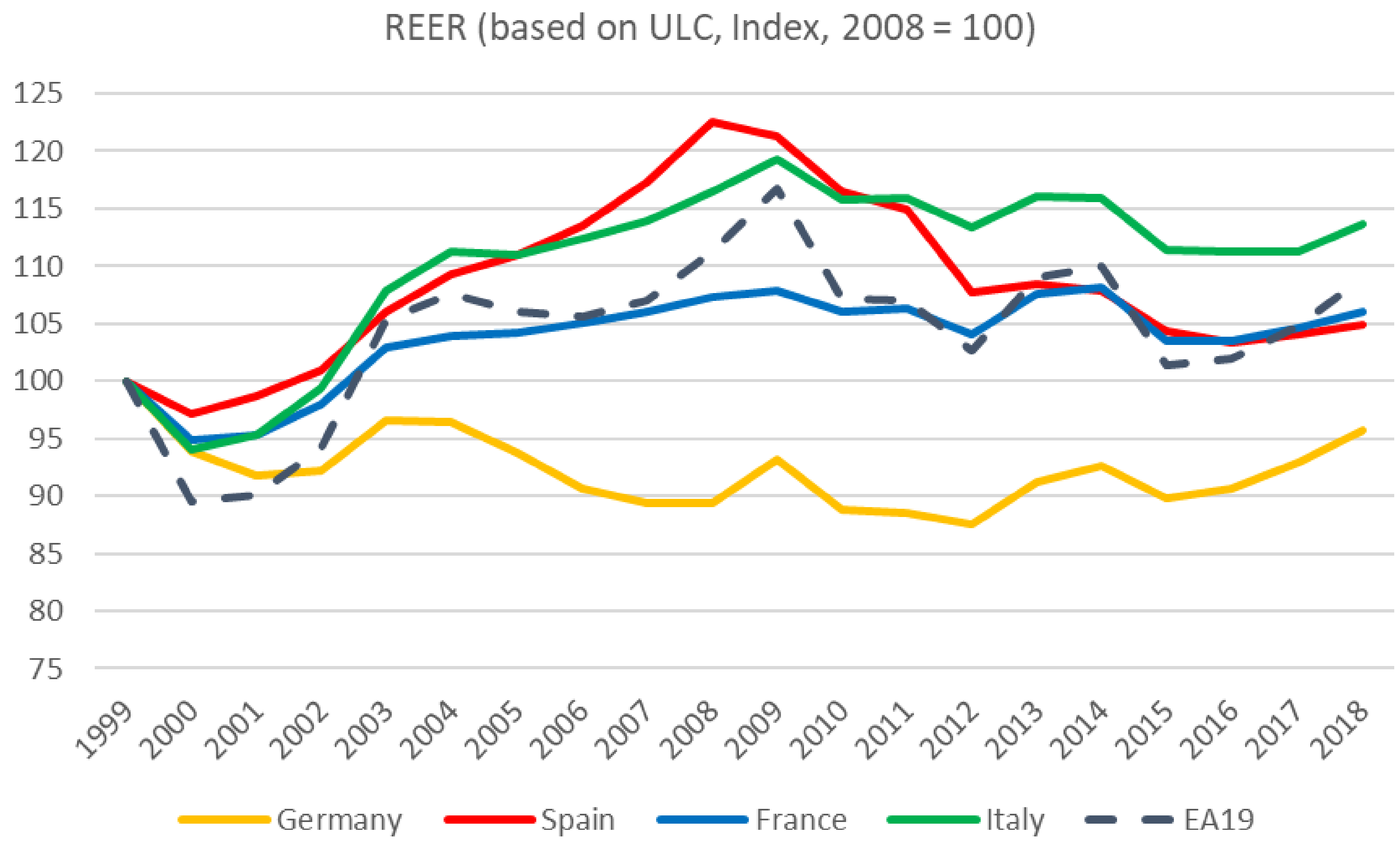
- **If we assume desired imperfect intra EA labour mobility**, **real divergence is inevitable and could be worsened by labour mobility (**« The lessons of Massachusetts for EMU » (P. Krugman, 1993) *: « A more integrated market leads to divergence in both the Economic structure and the growth rate of regions. »*

- **Hence, there is a need for risk sharing**
  - to address idiosyncratic shocks and smooth cyclical divergence
  - but also to mitigate structural divergences

- **Private risk sharing through global financial integration can help**, but would it be enough?

- « The lessons of Massachussetts for EMU » (P. Krugman) *: «In the US the heavily federalized fiscal system offers a partial solution to the problem of regional stabilization. Unless there is a massive change in European institutions, this automatic cushion will be absent."* remain partly true

BUMPY NOMINAL CONVERGENCE AND PAINFUL ADJUSTMENTS



Source: Ameco

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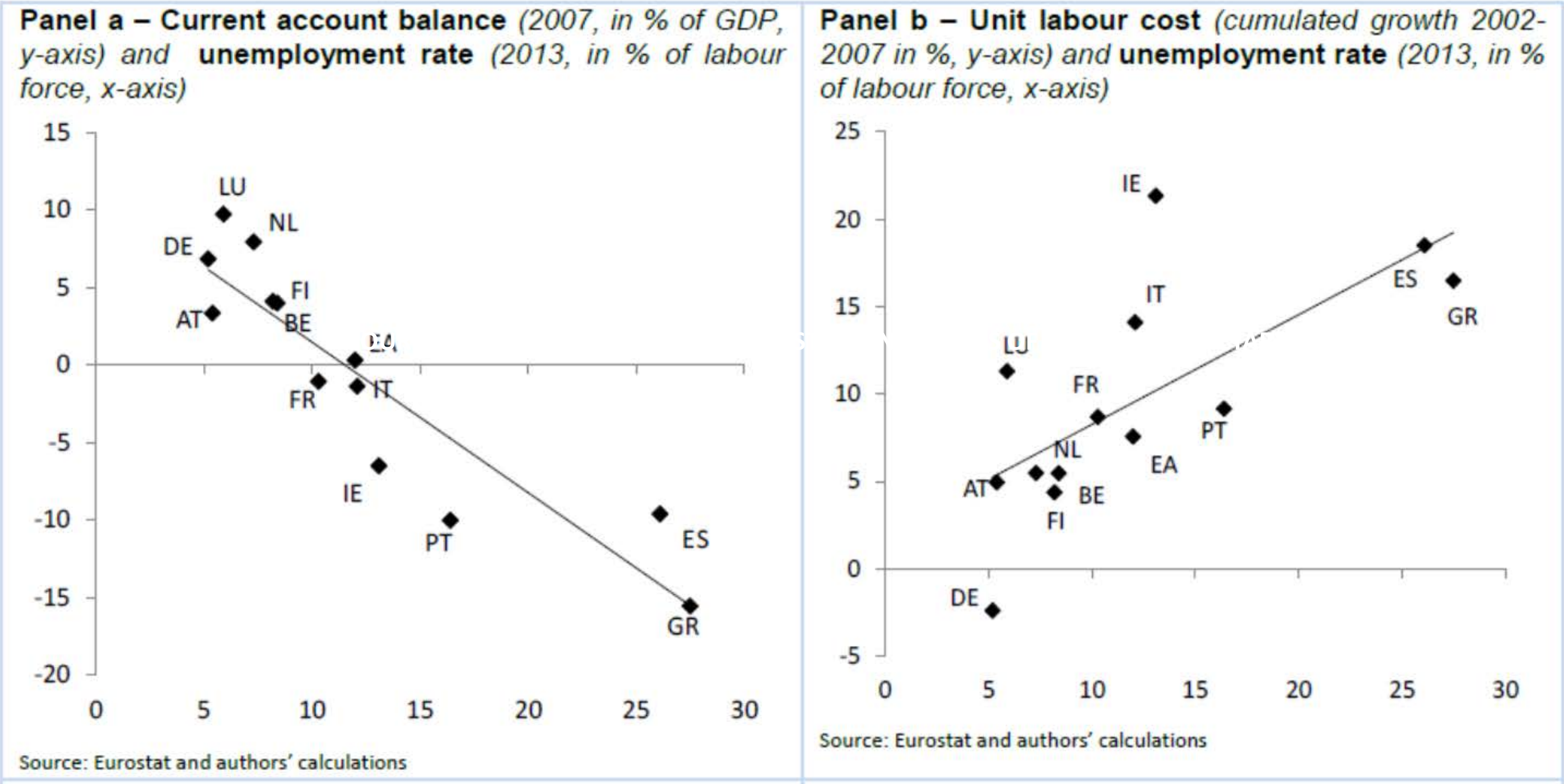
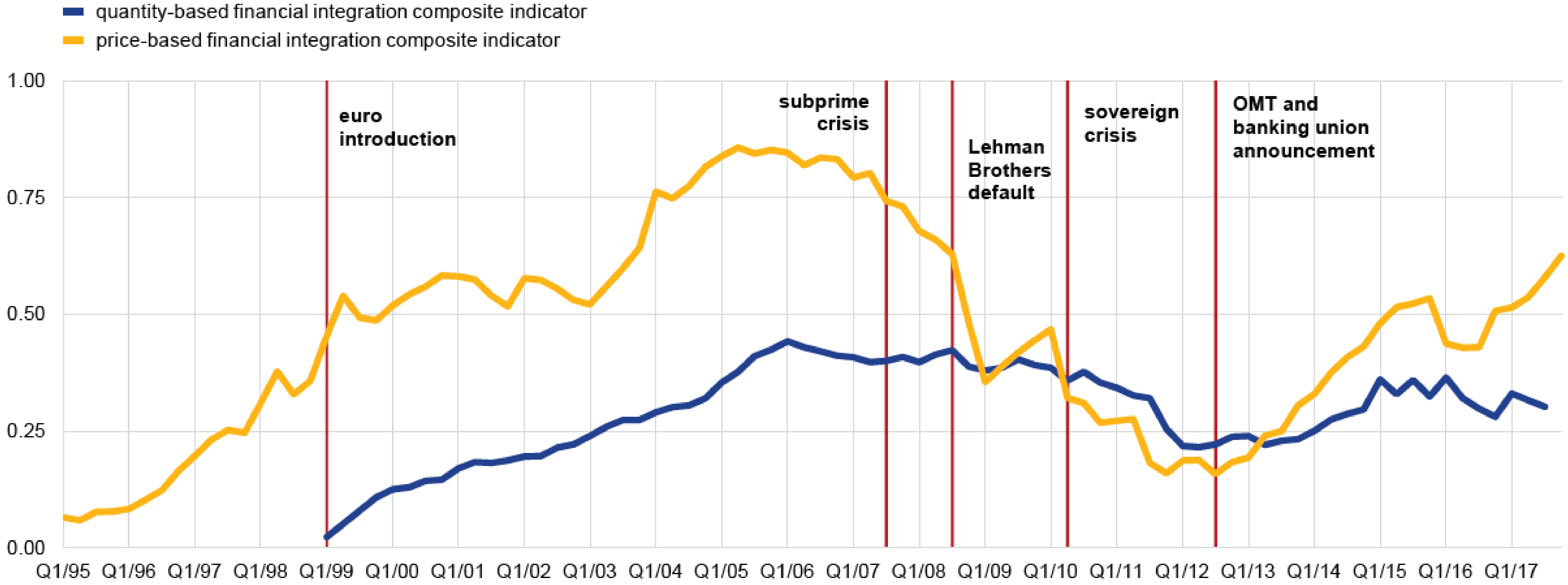
BUMPY NOMINAL CONVERGENCE AND PAINFUL ADJUSTMENTS



SOURCE : HARTMANN, SMETS : THE FIRST TWENTY YEARS OF THE ECB : MONETARY POLICY

BUMPY PATH OF FINANCIAL INTEGRATION IN THE EURO AREA



Sources: ECB and ECB calculations.

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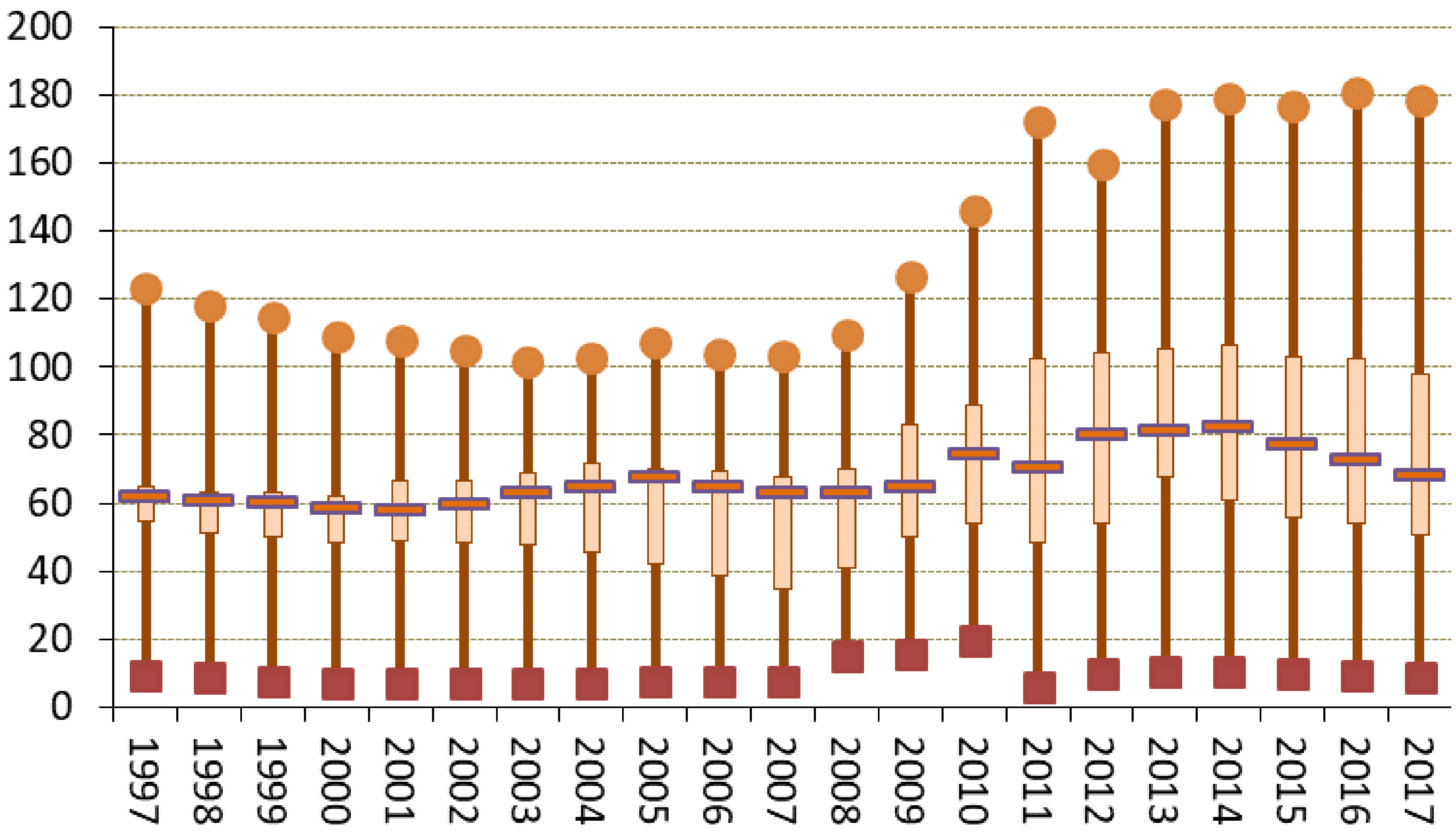
REAL DIVERGENCE, HOW MUCH IT MATTERS?

- **The trade off between risk sharing and risk reduction** : the unpleasant arithmetic due to :
  - divergent public debt level and path
  - GDP growth divergence
  - resilient banks/sovereign nexus and doom loop
  - worsening effect of potential increased labour mobility

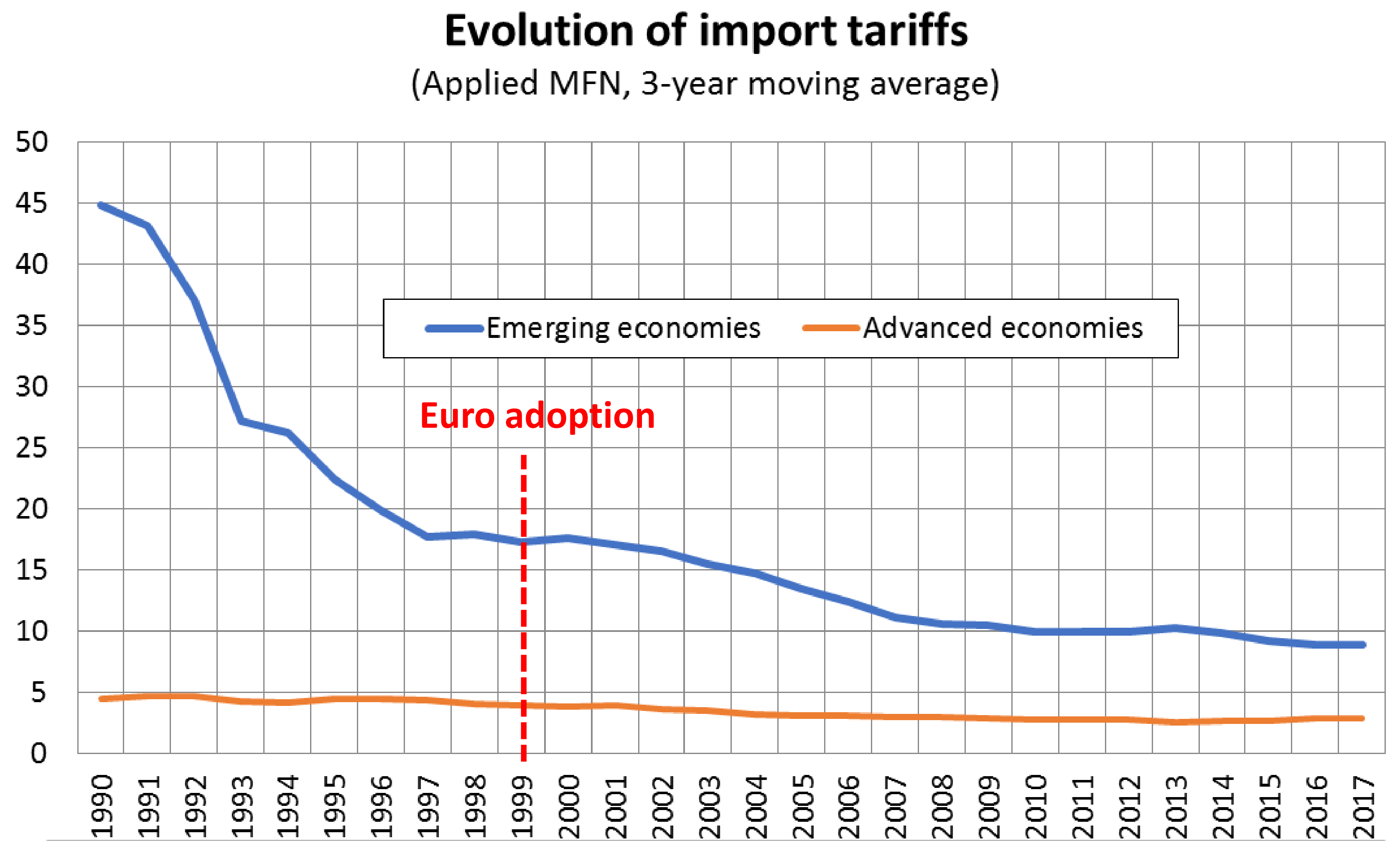
Banking Union, Capital Markets Union are decisive (but unachieved) steps forward but we could need more?

EVOLUTION OF PUBLIC DEBT IN THE EURO AREA
(GROSS PUBLIC DEBT, % OF GDP)



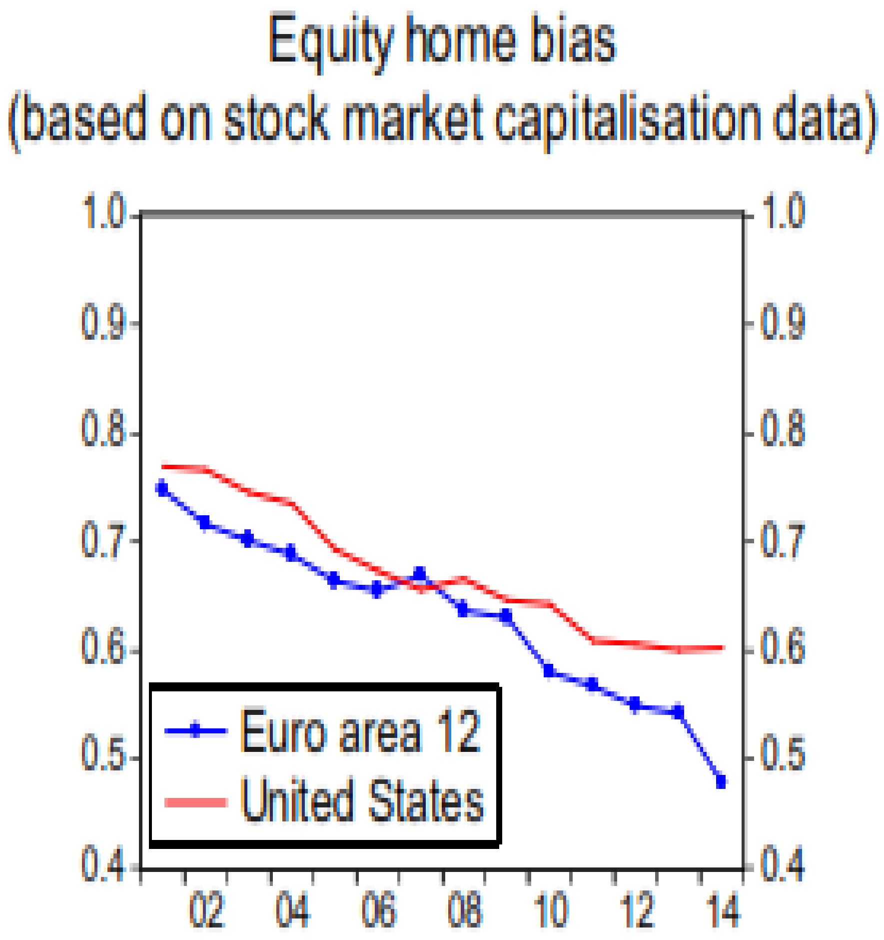
Source: Eurostat

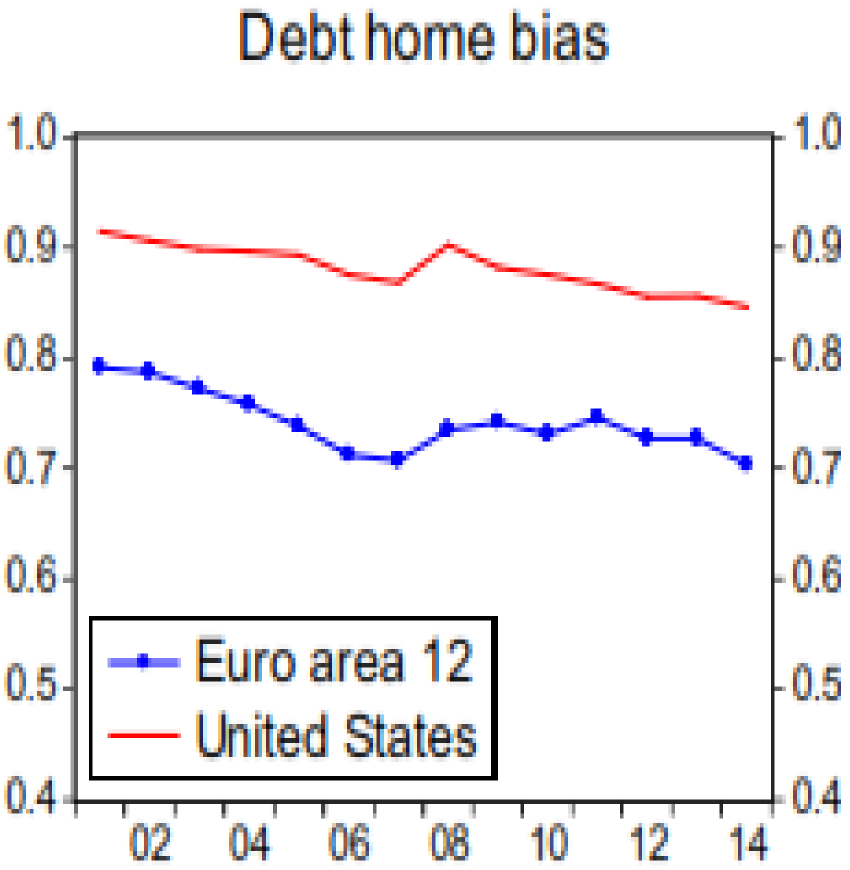
EMU IN A GLOBALISED WORLD : A DECREASING COMPARATIVE ADVANTAGE OF A CUSTOMARY UNION



Emerging = average Brazil, China, India, Russia, Korea; Advanced = average France, United Kingdom, United States, Japan
Source : World Bank

EMU IN A GLOBALISED WORLD : A DECREASING COMPARATIVE ADVANTAGE OF FINANCIAL INTEGRATION





SOURCE : INSTITUTIONAL INVESTORS HOME BIAS IN EUROPE'S CAPITAL MARKET UNION, DARVAS, SCHOENMAKER, WP BRUEGHEL, 2017

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EMU IN A GLOBALISED WORLD : 2038 AGENDA

- Achieve the Single Market, including for financial services
- Strengthen the institutional integration
- More labour market integration,
- Upward education level harmonisation