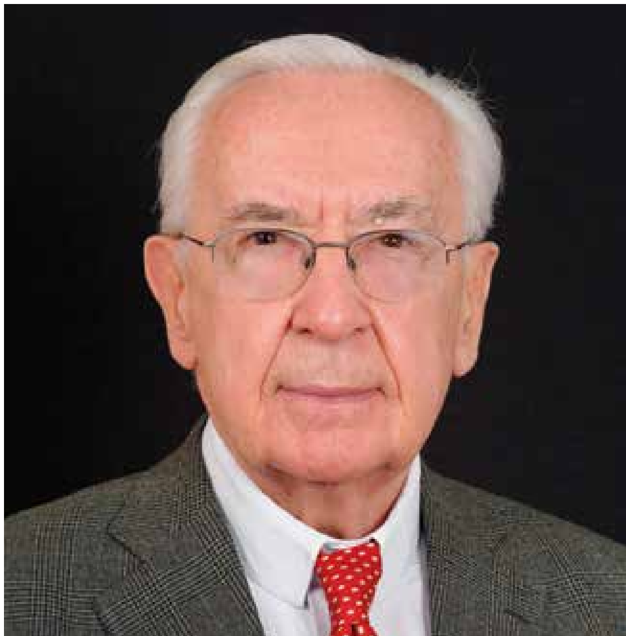

Q&A

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The EMU: what priority for the next five years?

What is hindering economic growth in Europe and how can productive investment be revitalized?

The central issue behind the modest economic growth in Europe over the past 20 years revolves around productive investment. Investment is the lifeblood of competitiveness and productivity. After the global financial crisis, net investment in the United States (US) and Europe fell significantly, but the decline was particularly pronounced in Europe. This has resulted in a sluggish economy in Europe, characterized by a decrease in medium- and long-term projects. These risky long-term investments are less likely to occur when real interest rates are zero or close to zero, as fund holders (savers, investors) prefer to hold liquid assets that they can mobilize at any time.

The environment in the US is very different. The bulk of future financing (long-term investments) is conducted through markets and equity. Although household savings are low in the US, the American financial market is highly developed and global. Significant portions of national savings from EU countries tend to flow to the US, either because interest rates and return on assets are higher or because the prospects for stock market valuation are more attractive to investors.

Acceptance of the risk of loss is at the heart of American financing: 80% of investment in stocks for a typical institutional portfolio. In Europe, the figures are more around 40 to 50%, which already constitutes an improvement compared to a few years ago. Moreover, European regulation tends to favor the holding of bonds over stocks because debt servicing is tax-deductible, whereas dividend distribution is not.

In summary, while the design of regulation in favor of a single financial market is important, addressing the core of the problem requires prioritizing other aspects as well.

What role has monetary policy played here? What can be done to encourage more productive investment in Europe and thus stimulate economic growth?

It is an illusion to think that a highly accommodative monetary policy with real interest rates close to zero or at zero can promote productive investment. As we have seen over the last fifteen years, such a policy results in a shortening of savers' investment horizons, as they prefer to keep liquid and easily mobilizable assets, like demand deposits, due to the lack of returns. A zero-interest rate monetary policy favors speculative bubbles, particularly in real estate. As recently noted by I. Schnabel, real estate investment is predominantly in existing properties to gain from increased valuations rather than creating new spaces, with 95% of real estate investment focused on existing assets.

The disparity between American and European banking systems significantly impacts the effectiveness of monetary policy on productive investments. American banks finance only a quarter of the economy, while in Europe, banks finance three-quarters of the economy. This difference influences how monetary policy affects the market and market intermediaries' willingness to finance productive investments. Additionally, American households are much less risk-averse compared to European households, and investment funds in the US do not hesitate to allocate a significant portion of their investments in stocks (80%). In contrast, European investment funds are more reluctant with stock investments ranging from 40-50%.

In addition to these inherent weaknesses of Europe compared to the US, there is a fundamental flaw in the way monetary policy has been conducted over the past 25 years that is exacerbating Europe's economic problems.

Indeed, this policy has inevitably contributed to a widening of the economic gap between North and South. The ECB's key interest rates are, by construction, an average for the eurozone economy as a whole, which makes it easier for countries with

higher inflation, higher public deficit and current account deficit. Since the creation of the euro, this factory of growing economic disparities between the countries of the monetary union has been able to flourish, even if the inflation differentials between countries have narrowed since the Covid crisis. This situation could have been remedied. To do so, macroeconomic policies would have had to be personalised and tightened in those countries that were prone to higher inflation. But this was not done.

Should we shift the monetary paradigm?

A change of monetary paradigm is critical. it is necessary to refrain from fixing administratively ("or directing" the market) long-term interest rates and to accept to let the market remunerate medium – and long-term savings – according to supply and demand – the only way to remunerate long-term savings, without which there can be no productive investment or productivity gains.

Should we also shift the economic paradigm?

Europe also needs to systematically promote productive supply by investing in research, innovation, and new technologies, rather than relying on grants or allowances to stimulate household consumption and internal demand. In highly indebted countries, this shift requires a reorganization of their public finances to achieve primary surpluses, thereby prioritizing public investments over expenditures that meet the current needs of households.

Reorienting national economic policies towards supply involves channeling long-term savings into productive investment. This approach is essential to enhance the economic attractiveness of economies and improve the returns on the assets developed there. Unlike Europe, the US can afford budget deficits because it issues the world's currency and benefits from the largest, most liquid, and deepest markets.

How can Europe boost private risk sharing to stimulate productive investment?

Everything must be done to ensure that venture capital, private equity, and equity financing develop in EU countries, allowing companies of all sizes and locations within the Union to find the financing they need in Europe. All regulatory actions in Europe should focus on this objective. The European legal and regulatory system must not discourage private equity players; rather, it should encourage them through favorable investment fund regulations. Ensuring that savings are invested where they can be most productive requires allowing market forces to set interest rates rather than relying on administrative controls.

By addressing these core areas, Europe can create a more dynamic and resilient economic environment, capable of sustaining long-term growth and innovation.

Should the European Union modify its competition policy and develop an industrial policy?

EU competition policy should be revamped to help companies scale up and better compete in global markets. It would also be valuable for Europe to design and implement a genuine industrial industry to boost its industry and to accelerate the single market while re-establishing a community preference.

European projects financed by European companies should also be encouraged. The development of Important Projects of Common European Interest (IPCEIs) and collaborative projects between Member States is undeniably a way forward, given that they align their objectives, they identify qualifying and profitable projects and that they find adequate funding. This would facilitate and foster the emergence of competitive European companies, champions and SMEs, as they would benefit from economies of scale in the single market.

You have just published a book on the economic decline of France. Why is it necessary to turn the tables?

If we do not turn the tables, France will remain in a state of permanent decline, culminating in catastrophe in a few years' time. The truth is that we have been investing far too little in France for the past 20 years. Continuing this policy of monetary and budgetary ease would lead to further disinvestment in this country. If this is what we seek, we should say so. The surreptitious return to a monetary policy of zero real interest rates, particularly to finance excessive deficits in heavily indebted countries like France, is a way of lying to the nation. The purpose of this book is to show that there is an alternative.