

Economic governance: prevention and correction of macroeconomic imbalances. 'Six pack'

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In accordance with Regulation (EU) No 1176/2011 on the prevention and correction of macroeconomic imbalances, the Commission presented its alert mechanism report 2020.

The alert mechanism report (AMR) is a screening device for economic imbalances, published at the start of each annual cycle of economic policy coordination. The procedure aims at identifying imbalances that hinder the smooth functioning of Member State economies, the economic and monetary union or the Union as a whole, and spurring appropriate policy responses. This report initiates the ninth annual round of the macroeconomic imbalance procedure (MIP).

The alert mechanism report includes an analysis of the euro area wide implications of Member States imbalances and examines the extent to which a coordinated approach to policy responses is needed in light of interdependencies within the euro area.

Economic background and outlook

The AMR analysis is carried out against the background of a changing economic outlook, where the economic expansion is weakening and inflation expectations have been revised downward. The European Commission autumn 2019 economic forecast estimates real GDP growth to be 1.4% in the EU and 1.1% in the euro area in 2019, implying a deceleration compared with 2% and 1.9% in 2018 respectively. For 2020, GDP is forecast to grow by 1.4% and 1.2% in the EU and the euro area respectively.

The report stated that data since late 2018 have pointed towards a loss of momentum, notably in net exports and in manufacturing output. The slowdown has been particularly visible in large euro area Member States more exposed to trade, on the back of heightened uncertainty surrounding the trade policy environment.

The changing outlook may imply a slower adjustment of existing imbalances or the materialisation of new risks, in a context where the room for policy to deal with shocks is narrowing. Downward risks to the economic outlook relate in particular to trade tensions and the disruption of global value chains, a stronger than expected slowdown in emerging markets, the aggravation of geo-political tensions.

Main challenges for Member States

The report finds that rebalancing within the euro area is still incomplete, while rebalancing of both current account deficits and surpluses is pressing in the current economic context and would be beneficial for all Member States. Whereas most large current account deficits have been corrected, large surpluses persist in a number of euro area countries. The main sources of potential imbalances in Member States are as follows:

- some Member States continue to be mainly affected by multiple and interconnected stock vulnerabilities. This is typically the case for those countries that were hit by boom-bust credit cycles coupled with current account reversals that also had implications for the banking sector and for government debt. This is the case for Cyprus, Greece, Croatia, Ireland, Portugal, Spain and Bulgaria;

- in a few Member States, vulnerabilities are mainly linked to large stocks of general government debt coupled with concerns relating to potential output growth and competitiveness. This is particularly the case for Italy, where vulnerabilities are also linked to the banking sector and the large but rapidly declining stock of NPLs, and in a context of weak labour market performance. Belgium and France mainly face a high general government debt and potential growth issues amidst also compressed competitiveness. In France, a relatively high stock of private debt is on the rise. In Belgium, a relatively high and growing stock of household debt is coupled with possibly overvalued house prices; the external position remains solid but has weakened somewhat recently;

- some Member States are characterised by large and persistent current account surpluses that also reflect, to a varying degree, subdued private consumption and investment, in excess of what economic fundamentals would justify. This is the case notably for Germany and the Netherlands. In the Netherlands, a large surplus is coupled with a high stock of household debt and strong house price growth; house price pressures have been noted recently also in Germany but debt levels therein are comparatively low;

- in some Member States, developments in price or cost variables show potential signs of overheating, particularly as regards the housing market or the labour market. In Sweden, and to a lesser extent in Austria, Denmark, Luxembourg, and the United Kingdom, sustained house price growth has been observed in recent years in a context of possible overvaluation gaps and significant levels of household debt. Stronger but more recent house price growth is coupled with more limited evidence of overvaluation in Czechia, Hungary, Latvia, Slovakia, and Slovenia, which in the cases of Czechia and Slovakia has been observed together with continued mortgage borrowing and rising debts by households.

In-depth reviews (IDRs)

Overall, IDRs are warranted for 13 Member States: Bulgaria, Croatia, Cyprus, France, Germany, Greece, Ireland, Italy, the Netherlands, Portugal, Romania, Spain, and Sweden. All those Member States were subject to an IDR in the previous annual cycle of MIP surveillance, and were considered to be experiencing imbalances or excessive imbalances.

The new IDRs will help going deeper into the analysis of those challenges and assessing policy needs. In particular, forthcoming IDRs will be prepared to assess if those imbalances are aggravating or are under correction, with the view to update existing assessments.

This AMR points also to the possible building up of risks in a number of other Member States that, on the basis of current information, do not seem to warrant an IDR at this stage but nonetheless still justify a close monitoring notably in the upcoming country reports. Those risks concern notably developments related to competitiveness (Czechia, Estonia, Hungary, Latvia, Lithuania, and Slovakia) and to housing prices and housing markets and household debt developments (Austria, Belgium, Czechia, Denmark, Finland, Hungary, Luxembourg, Slovakia, Slovenia, and United Kingdom).