Stability and prosperity in Europe

Speech at the Munich European Conference: Security and Prosperity in Europe, Giesecke+Devrient

15.02.2024 | Munich | Joachim Nagel

Check against delivery.

1 Words of welcome

Ladies and gentlemen,

It is a pleasure and a privilege for me to speak today on the eve of the Munich Security Conference, one of the most important global events that takes place in this country every year, here at the eighth Munich European Conference, which reflects on and debates avenues that can lead to greater security and prosperity in Europe.

I am here as a central banker. That is why I have slightly modified the conference topic of “Security and Prosperity in Europe” with some care to “Stability and Prosperity in Europe” for my keynote speech. Geopolitical security is not a central banker’s key topic. I would therefore ask you to interpret the few comments I make on this subject at the end of my speech as the personal views of a politically minded citizen. Stability, by contrast, is the core competence and mandate of the Eurosystem, and thus also of the Bundesbank: stability of prices, of credit institutions, of the financial system and of payments. That is our contribution to safeguarding prosperity and economic security in Europe.

2 Europe’s prosperity

2.1 EU (European Union) and euro have contributed to prosperity in Europe

Prosperity in Europe gained a notable boost in 1993, when the European single market was established by twelve countries at that time. Fast forward 31 years to the present day, and the single market is home to 31 European countries, 450 million people and around 24 million businesses.

In terms of goods, now everyone can be offered the same product. National regulatory rules do not require country-specific models. And products do not need to undergo approval procedures in every single country. That lessens frictions and allows larger quantities of goods to be manufactured at lower unit costs and lower prices. At the same time, the single market’s common rules and standards have helped create a level playing field and thus spurred competition, economic growth and prosperity.

Our single currency – the euro – has been amplifying the single market’s benefits for 25 years now. In the euro area, exchange rate risk and currency conversion charges are a thing of the past. And prices are easier to compare. Another aspect that is conducive to trade. And which strengthens competition, thereby adding to prosperity. The Bundesbank, under its then-President Karl Otto Pöhl, played an instrumental role in shaping the Maastricht Treaty. Pöhl was convinced that – and I quote – “... the consolidation and ongoing development of the European Monetary System have a key role to play in securing political and economic integration in Europe.”[1]

The single market alone has boosted economic output in the EU (European Union) by around 3 to 5½%, studies have found.[2] This stands in sharp contrast to the impact of Brexit. The United Kingdom’s withdrawal from the single market may have reduced the country’s GDP (Gross Domestic Product) by 6% so far, a recent study suggests.[3] For economic reasons alone, there is everything to be said for strengthening the single market further as a source of prosperity. There is certainly a need for this. Because the single market is still far from perfect.

2.2 Dismantle barriers in the services sector

You see, cross-border trade in services is far smaller than it is for goods.[4] To a degree that is natural, as many services are more difficult to trade across long distances than goods. It is easy to order a book in Paris while sitting in Munich. Visiting a hairdresser in Paris is a trickier undertaking.

That said, a large and growing number of services are being provided at distance thanks to digitalisation. There once was a time when your local agent was the first port of call in insurance or personal finance matters, say. But these days, much can be done over the phone or in fully automated processes through the insurer’s or bank’s own self-service portals. Overall, though, there are home-made barriers restricting the flow of services. Many national regulations inhibit the provision of cross-border services, particularly legal services, but also in the area of architecture and engineering.[5] They’re a drag on efficiency.

Many a national regulation may well exist for a good reason – differences in the legal system or in national preferences, say. But for many barriers, that kind of justification seems fairly questionable. That is why Member States need to dismantle barriers that are uncalled for, particularly in the services sector. They need to further deepen the single market by embracing reform and simplifying public administration as a way of improving competitiveness levels.

2.3 Remove barriers in the financial market: strengthen banking and capital markets union

The banking and capital markets union is another area where we are still a long way off from achieving complete integration. One major barrier is the variety of insolvency regimes across EU (European Union) Member States.[6] I am pleased that the Commission's legislative proposal on the capital markets union is now tackling numerous barriers. What matters is that cross-border investment is promoted as a result.

An integrated capital market is important, and particularly so in the euro area. It will support the single monetary policy. Because it will play a part in ensuring that monetary policy impulses have equal effect throughout the euro area. And in the event of an economic shock in one Member State, downstream costs would be spread across the currency area. In this respect, greater private risk sharing can be the key to boosting the stability of the financial system.

Another benefit of an integrated capital market is that it would ease the mobilisation of funds for private investment and thus strengthen the forces of growth. Securitisation may also have an important role to play in this context. You see, these financial instruments bridge the gap between bank finance and the capital market. They need to be regulated in a risk-appropriate manner – that goes without saying. What makes the ability to mobilise private capital more easily even more important is the fact that huge amounts of funding will need to be raised in the years ahead. For large and pressing challenges lie ahead of us – first and foremost green structural change towards climate neutrality and digital structural change.

2.4 Press ahead with green structural change

The EU (European Union) has already taken action to address green structural change in the shape of the "European Climate Law", which will see Europe achieve climate neutrality by 2050. Along with a reduction in greenhouse gas emissions by at least 55% by 2030 compared to 1990 levels. "Fit for 55" is the name given to the EU (European Union)'s ambitions on this front. The EU (European Union) emissions trading system (EU (European Union) ETS (emissions trading system)) is the cornerstone of the EU (European Union)'s policy to combat climate change. The EU (European Union) ETS (emissions trading system) offers the decisive benefit of reducing emissions cost-efficiently – that is, at the lowest possible cost to the economy as a whole. Efficient policy measures of this kind are crucial in the face of the Herculean task that green structural change alone represents. At the same time, the EU (European Union) is looking to take the lead in the development and use of sustainable technologies in key areas, such as batteries and solar power systems.

The Green Deal Industrial Plan will use subsidies and financial support to stake out an industrial policy path leading to that goal. In doing so, we need to conduct a realistic stocktake of the potential and constraints of industrial policy. And a subsidy race should be avoided at all costs, including in view of the US (United States) Inflation Reduction Act. Distorting competition would create capacities in the wrong places or might leave taxpayers footing a huge bill.

2.5 Press ahead with digital structural change

Green structural change towards climate neutrality isn't the only challenge that lies ahead: digital structural change is another big ask. Recent advances in artificial intelligence suggest that its impact on labour and financial markets will be momentous, particularly if generative AI is able to create new text, video or audio content. This surge in digitalisation is likely to give productivity an additional boost, of the kind we saw in the past when innovative digital developments emerged. And it is precisely higher productivity that leads to higher economic growth. That point was made recently by Agustín Carstens, General Manager of the Bank for International Settlements.[7]

The public sector can play a role in driving digital structural change – and should do so, too, given the expected boost in productivity. Looking at Germany, it is a matter of pressing ahead with the expansion of high-performance telecommunications networks, digital upskilling – in the education system and with labour market policy – and of the public administration making up the ground it has lost in terms of digital readiness. On that last point I've brought some figures with me: the Online Access Act stated that all key administrative services must have gone digital by 2022. As it turns out, no more than 33 out of 575 public services had gone digital.[8] So there is still a wealth of potential to cut red tape for all and to speed up administrative processes. Things need to move much more quickly here. At the European level, digital structural change is being supported by Digital Decade[9] – a policy programme that sets binding digitalisation targets and establishes legal certainty by mapping out regulatory requirements.

However, the more we go digital, the greater our exposure to cyber risk. A study published last month found that 44% of firms surveyed in Germany saw cyber risk as the greatest risk their business faced.[10] Worldwide, that figure has risen to 36% on average – a long way ahead of the second greatest risk: business disruptions due to supply chain failures and the like. Cybersecurity, then, is a topic that all stakeholders need to regard as an important task. Financial supervisors, for example, are doing just that. That's an area where we at the Bundesbank work hand in hand with BaFin (Bundesanstalt für Finanzdienstleistungsaufsicht). This year, financial supervision has prioritised the risks posed by hackers as well as the outsourcing of IT (Informationstechnologie) services. That more needs to be invested in one's own defences is a view that is becoming increasingly commonplace at the European level, too – and that arguably goes for both IT (Informationstechnologie) security and the security and integrity of borders.

2.6 Safeguard sound public finances

Rising to the challenge of green and digital structural change is a huge ask for everyone, not least for public finances. This is because, on the one hand, there are good reasons to spend more public money on certain forward-looking tasks. On the other hand, government needs to keep its financial affairs in good order. If a crisis strikes, a government will only ever have agency if its finances are sound. This enabled Germany to provide substantial support to households and firms during the COVID (Coronavirus Disease)-19 pandemic. And sound public finances make life easier for monetary policy by allowing it to focus its full attention on maintaining price stability. That's how sound public finances make monetary union more stable.

If we take a look at public finances in the euro area, we see a very mixed picture. Even the average debt ratio of euro area countries is significantly higher than it was at the launch of monetary union. And it is precisely the very highly indebted countries – countries whose general government debt is higher than their annual GDP (Gross Domestic Product) – that nonetheless have persistently high fiscal deficits. In December, an agreement was reached to reform the European fiscal rules. Now it is a matter of leveraging the new rules to actually bring down the high debt ratios. The safeguards introduced by the Federal Government can help make sure that happens. Shrinking debt ratios would boost investor confidence – just like a credible fiscal strategy. Monetary policy has a strong interest in this. And it would promote economic growth and prosperity in Europe.

3 Security in an evolving world

The harsher the world around us gets, the more important it becomes to strengthen Europe economically. Things are getting harsher right now. The world is becoming more muddled. And more conflict-ridden. The Peace Research Institute Oslo reports that more than 50 state-based conflicts have been recorded. That is a particularly high level in postwar history.[11] There was talk in the post-Cold War early 1990s that “the end of history” had been reached.[12] Many were convinced that democracy, liberalism and the market economy would prevail. Things didn’t quite turn out that way, though, and the future world order remains unclear. It does, however, appear to be multipolar.

In that kind of world, stability has to be safeguarded in a variety of ways: by complying with international law, through stable partnerships and with robust international organisations. The World Trade Organization (WTO (Welthandelsorganisation)) is one such organisation I could mention. It stands for a rules-based, open trading system. In a multipolar world, this system could unlock considerable efficiency gains. But to achieve that, the WTO (Welthandelsorganisation)’s system of rules needs to be overhauled at long last.[13] EU (European Union) enlargement is another topic worth mentioning here. The European Council called enlargement a “strategic priority” in light of Russia’s war of aggression against Ukraine. The focus is currently on the Western Balkans. The European Council has committed to gradually integrating these countries into the single market ahead of EU (European Union) accession. In addition, regional free trade agreements are gaining in importance again. These would likewise bolster the resilience of the European economy. And last but not least, given the many elections that will be taking place this year, we can only hope that they elect governments that uphold the values of democracy, comply with the law and international rules, and see themselves as part of a community of nations.

4 Conclusion

Ladies and gentlemen,

Standing up for Europe and bringing out its best are worthy endeavours.

Europe has always been a peace project. And has achieved that mission with great success.

The European single market and the euro were instrumental in boosting prosperity – and still are.

Weakening Europe would destroy prosperity.

We must not let it come to that!

Let us instead help mould a stable Europe.

A Europe that stands for democracy, solidarity and the common good. A Europe that forges peace. A Europe that does not divide, but unites. A modern Europe that inspires people. A Europe that looks ahead, that rises to challenges. A Europe that gives people firm foundations and guidance. A strong European Union.

In all that it does, the Bundesbank will advocate for a stable Europe – as a strong partner in the Eurosystem.

Footnotes:

1. Pöhl, Karl Otto (1985), speech in Paris, Quotes by Karl Otto Pöhl *[https://www.bundesbank.de/resource/blob/608060/06cde29bffa5ad90ac478d3ed584d903/mL/zitate-von-karl-otto-poehl-data.pdf]* .
2. Felbermayr, G., J. Gröschl and I. Heiland (2022), Complex Europe: Quantifying the cost of disintegration, Journal of International Economics, Vol. 138, September 2022 *[https://www.sciencedirect.com/journal/journal-of-international-economics/vol/138/suppl/C]* and Mayer, T., V. Vicard and S. Zignago (2019), The cost of non-Europe, revisited *[https://academic.oup.com/economicpolicy/article/34/98/145/5486061]*, Economic Policy, Vol. 34, April 2019. A study conducted on behalf of the European Commission estimates that EU (European Union) GDP (Gross Domestic Product) is as much as 8 to 9% higher thanks to the single market; see in 't Veld, J. (2019), Quantifying the Economic Effects of the Single Market in a Structural Macromodel *[https://economy-finance.ec.europa.eu/system/files/2019-02/dp094_en.pdf]*, European Commission, Discussion Paper 094, February 2019.
3. Cambridge Econometrics (2024), London's economy after Brexit: Impact and implications *[https://www.camecon.com/what/our-work/londons-economy-after-brexit-impact-and-implications/]* .
4. Vandermeeren, F. (2022), 30 years of single market – taking stock and looking ahead *[https://favis.inet.bundesbank.de/csdav/nodes/555999871/30-years-single-market-taking-stock-and-looking-ahead_en_]* , Single Market Economy Papers.
5. European Commission (2021), Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs (Small and medium-sized enterprises), Mapping and assessment of legal and administrative barriers in the services sector – Summary report *[https://op.europa.eu/en/publication-detail/-/publication/6d8d8858-a756-11eb-9585-01aa75ed71a1/language-en]* , Publications Office, 2021, p. 4.
6. Bhatia, A. V. et al., A Capital Market Union for Europe *[https://favis.inet.bundesbank.de/csdav/nodes/555999871/A-Capital-Market-Union-For-Europe-46856_]* , IMF (International Monetary Fund) Staff Discussion Note, September 2019.
7. Carstens, Agustín, Where are we on the journey toward price stability?, Speech at the Statistisch-Volkswirtschaftliche Gesellschaft (SVG (Statistisch-Volkswirtschaftlichen Gesellschaft)) Basel, 22 January 2024. "Achieving higher and sustainable growth can only be accomplished by boosting productive potential through measures enhancing the supply side and boosting innovation. This requires renewed efforts to design and implement structural reforms in product and labour markets, which have slowed considerably over the past two decades.

8. ”National Regulatory Control Council (2023), Positionspapier des Nationalen Normenkontrollrates zum Entwurf eines Gesetzes zur Änderung des Onlinezugangsgesetzes sowie weiterer Vorschriften
[file:///C:/Users/o3504bq/AppData/Roaming/OpenText/OTEdit/EC_favis/c555999871/ozg-positionspapier.pdf]
, p. 1.
9. European Commission (2024), Europe’s Digital Decade: digital targets for 2030
[https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/europe-fit-digital-age/europes-digital-decade-digital-targets-2030_en]
10. Allianz Risk Barometer
[https://www.allianz-trade.de/wissen/wirtschafts-news/allianz-risk-barometer-2024-geschaeftsrisiken.html]
(2024)
11. Peace Research Institute Oslo (2023), Conflict Trends: A Global Overview, 1946-2022
[https://cdn.cloud.prio.org/files/dc754702-b1ec-4787-97bb-7a41f187036a/Obermeier%20Rustad%20-%20conflict%20trends%20a%20Global%20Overview%201946-2022%20PRIO%20Paper%202023.pdf?inline=true]
, p. 10.
12. Fukuyama, F. (1989), The End of History?, p. 4.
13. Deutsche Bundesbank (2020), Consequences of increasing protectionism
[https://www.bundesbank.de/resource/blob/822438/306c76bad7214946ac90075a442691ad/mL/2020-01-protektionismus-data.pdf]
, Monthly Report, January 2020, pp. 45-66.