

Economics in Brief



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Efficient investment for higher growth in the euro area

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The financial and economic crisis has led to a pronounced and stubborn lack of investment in the euro area. This is now widely agreed upon. Financial restrictions on the public and private sector, coupled with weak growth and uncertainty, have severely impacted investment activity. A simple comparison with the trend since 1995 shows how far investment has fallen behind. Measured on that basis, gross fixed capital formation in the overall economy fell short by EUR 200–600 billion in the last year (Figure 1). This is not least because of the low level of public investment, which was EUR 50–80 billion below trend (Figure 2).

Now is the right time to increase investment

There is much to be said for increasing investment now. According to EIB estimates, EUR 2 trillion needs to be invested in the EU by 2020 for infrastructure alone. Investment allows expansion and modernisation of capital stock, thus in-

creasing productivity as a driver of higher sustainable growth. Furthermore, according to IMF findings, it is particularly worthwhile to invest more when the economy is in a period of weakness and monetary policy is expansionary. Both are undoubtedly true of the euro area today.

Three approaches to strengthening growth through investment

(1) The public sector in euro area countries remains subject to tight financial constraints. However, there is no fundamental lack of financial resources in the euro area. Far from it: the euro area's current account balance is running a surplus of 2% of GDP. Annual savings thus exceed investment spending to the same degree. The task is therefore to steer existing financial resources into domestic investment projects. This means exploiting fiscal scope within the limits of national and European debt rules. Furthermore, there are sound reasons for allowing loan financing of public

investment. To avoid over-stretching public finances, it is also vital to attract more private investors for the financing and execution of infrastructure projects.

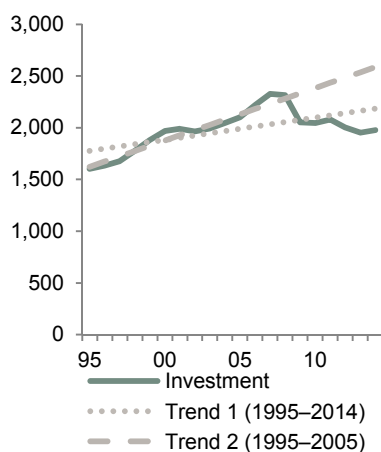
(2) The efficiency of public investment can be increased further. This applies both to the selection of projects, which must be based on their macro-economic viability, and to their execution. The structuring of investment projects as public-private partnerships can make a valuable contribution in this respect, as well as in terms of funding.

(3) Success crucially depends on having a good framework for private investment, since the public sector cannot close the investment gap on its own. A healthy, robust banking system and stability in the financial markets are extremely important in this respect. It is encouraging to note that financing conditions for companies in the euro zone are slowly improving following the implementation of the Single Supervisory Mechanism. The costs of borrowing are falling and lending activity is on the increase. At the same time, structural reforms remain important in order to strengthen the competitiveness of the euro area and reduce barriers to investment.

Policy response: is enough being done?

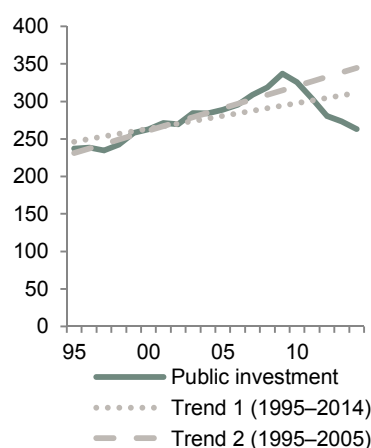
The Investment Plan for Europe, the work being done on the Capital Markets Union and the German Federal government's investment offensive are important elements in the drive to overcome the lack of investment. However, it remains to be seen whether these initiatives are strong enough to revive investment in Europe sufficiently and sustainably. ■

Figure 1: Investment
(EMU, in real terms, 2014 prices)



Source: Eurostat, own calculations.

Figure 2: Public investment
(EMU, in real terms, 2014 prices)



Source: Eurostat, own calculations.