Speech delivered by H.E. Mr. Jeroen Dijsselbloem
President of the Eurogroup
Minister of Finance of the Netherlands

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[Introduction]

Professor Seike,

Dean Nakamura,

Dean Hosoda,

Excellencies,

Ladies and gentlemen,

It's a great pleasure to visit your fascinating country and a huge honour for me to speak at your university. I'd like to thank your President, Professor Atsushi Seike, for his kind invitation.

Since its founding in 1858, Keio University has always provided a window to the world. For me as a Dutchman, it is an inspirational fact that your famous founder, Yukichi Fukuzawa, started this university as a school for Dutch studies. Fukuzawa was a man of the world, who not only spoke many <u>languages</u>, but also visited many <u>countries</u>, including France, Germany, Portugal, and my country as well. So I couldn't think of a better and more welcoming place to deliver a speech about Europe than this centre of open-mindedness.

Fukuzawa lived and worked at a time of great challenge, like we do now. And as Professor Seike underlines in his mission statement: the greater the change we're dealing with, the more important learning becomes. We are gathered here in the spirit of Yukichi Fukuzawa.

We want to learn from each other, scrutinising both strengths and weaknesses in order to become wiser and stronger. Now, if I had to name one thing I admire in this country, the first that comes to mind is its resilience.

I am impressed by the way Nippon is recovering from the devastating earthquake, the subsequent tsunami and the nuclear disaster that struck your country four years ago. It must still take a lot of energy, courage and willpower to leave the past behind and face the future again.

Some time ago I read an interview with Haruki Murakami, who is possibly, as world renowned authors tend to be, even more famous abroad than at home. For us Europeans Murakami has opened the door to modern life in Japan.

In the interview he talks about the changes caused by the disasters, and I quote: *'the reckoning that comes with losing so much and having to question what matters most'*.

This is an important question. In times of desperation, but also in times of change. So I recognise what he says when I look at the changes needed in Europe. In Europe we are facing a new reality, which is forcing us to re-evaluate our institutions, our welfare state and our expectations. In short: we need to modernise our economies to achieve sustainable growth. For sustainable growth the eurozone needs to regain its competitiveness and its capacity to create jobs. That won't just benefit us, but also this part of the world. Because Europe remains one of the most important consumer markets in the world. In sales terms, Europe consists of 500 million people. They have middle-class incomes and are looking for quality goods. EU member countries account for 19 per cent of world imports and exports. This provides potential.

Your part of the world and mine both have developed economies with great potential, but we also face similar challenges like an ageing population and the need to innovate.So we can benefit from each other through trade and from each other's experience in facing the challenges of our day. To put it simply: we need each other.

[Where do we stand today?]

Let me give you some background information about the euro area, also known as the eurozone. It consists of those European Union countries which have adopted the euro as their currency. The eurozone currently has 19 member states. The 19th member, Lithuania, joined the eurozone on 1 January this year. Sharing a single currency means that euro area countries must coordinate their economic and fiscal policies closely – much more so than other EU countries. Euro area finance ministers meet every month in the Eurogroup. At these meetings we coordinate our policies and take the necessary steps to promote financial stability in the euro area. We also discuss on a monthly basis all issues of common concern for the management of the single currency area. Today, I would like to discuss with you where the eurozone stands and what is needed going forward, while taking account of the experiences of Japan.

[Comparison crisis Japan and euro area]

First, let me briefly touch on Japan's experience during its big banking crisis, and our very recent experience. Both Japan, at the end of the previous century, and the euro area, quite recently, have experienced the impact of a bubble bursting. Both the Japanese and European economies are highly dependent on the banking system. Both experienced a substantial blow. And both are confronted with the drag on economic growth associated with a restoration of balance sheets, a necessary and lengthy process. While some aspects of our experiences are indeed similar, there are important differences as well.

I would argue that the most important difference lies in the underlying structural problems. In Europe, the crisis revealed a number of structural weaknesses in our economies and in the governance of our currency union. Our crisis response has focused on addressing these shortcomings.

First, the crisis revealed weaknesses in the European supervision of banks. These have been vigorously addressed: the creation of the banking union has been a key achievement in restoring the banking sector to health. To start with, common European supervision was established. The European Central Bank exercises direct or indirect supervision over all euro area banks. This enables us to apply the same standards to all banks and reflects the fact that many banks operate across European borders.

We have also created a European resolution mechanism, in case a bank gets into trouble. This provides clarity on what happens if a bank fails and prevents bank problems from infecting sovereigns, and vice versa. This reduces risks for governments and taxpayers.

Finally, only two months ago, the European Central Bank completed a comprehensive assessment of the 130 systemically relevant banks under its direct supervision. These large banks have undergone an asset quality review and a stress test. Over the coming months, banks will have to improve their balance sheets where necessary. This thorough exercise has fostered transparency about the condition that our banks are in. And it has generated confidence that the European banking sector is getting stronger.

Second, euro area countries have been under pressure to get public finances back in order. This differs from Japan’s experience. Since the mid-nineties, Japanese fiscal policy has been highly supportive. As a result of more than two decades of substantial deficits, Japan’s public debt ranks highest among developed economies. Low interest rates and the fact that debt is mostly domestically held, have enabled Japan to sustain this approach. The situation in the euro area is very different. Financial stability has been at risk. With the cost of financing rising quickly, several euro area countries experienced huge pressure to put their public finances once again on a sustainable path. The crisis also revealed shortcomings in the European rules and frameworks governing fiscal policy. So from the moment the crisis started, the sustainability of public finances was tackled with great urgency. We have pursued a strategy of strengthened fiscal discipline and budgetary consolidation. We tightened our budgetary rules. We created a mechanism for monitoring possible macroeconomic imbalances. And we strengthened the European Commission’s role in this surveillance process. For example, last December we discussed the draft budgets of all euro countries in the Eurogroup. This was not an easy discussion. But our candid and robust debate among each other reflects our common interest and commitment to the pact we have.

Finally, the crisis confronted many euro area countries with underlying structural weaknesses in their economies. First, support for countries under pressure from financial markets has been combined with vigorous reform. I want to underline the significance of the efforts made by what are known as the 'programme countries': Greece, Portugal, Ireland, Spain, Cyprus. They have pursued strong reform agendas and continue to do so. Their people have made painful sacrifices and many countries have suffered major losses of income. But also other countries, like the Baltics: Estonia, Latvia, Lithuania, and also my country the Netherlands, have worked hard to strengthen their economies.

Now, the countries that have implemented tough reforms have all achieved positive growth rates again. And this year, all these countries are expected to grow faster than the eurozone average. To sum up: we didn't only tackle our short-term problems. We realised that our architecture and our rules were incomplete and needed improvement. Thanks to all the measures we've taken, the eurozone is stronger than it was before the crisis.

[Weak growth and low inflation]

So where do we stand now? Growth is picking up, but it is weaker and slower than we would like. The peak in unemployment is over, but in many countries, too many people have been left without a job. Inflation remains subdued and in some euro area economies, prices have fallen.

This is another area where Japan and the euro area are often compared. Commentators regularly wonder whether the euro area will experience a 'lost decade', like the years of low growth, rising debt and falling prices in Japan. On this point I would say first that Japan's experience should be put in perspective. Japan's mild deflation hardly played any role in Japan's debt dynamics. Public debt rose, but as a result of government spending, not deflation. So concerns over a negative debt-deflation spiral may be unfounded. Secondly, while growth was moderate, this was mainly caused by Japan's shrinking population. In per capita terms, growth held up relatively well.

The euro area differs from Japan when it comes to the causes of low inflation. Low food and energy prices play a large role. Prices are also affected by both demand and supply side dynamics. It's very difficult to distinguish between the two. But a number of euro area countries have implemented serious reform agendas. Higher productivity and relative price adjustments may cause prices to fall, but at the same time they make these economies stronger and more competitive. Spain is a strong example of this. In itself, the necessary and successful effort made by a number of euro area countries to gain lost ground is a positive development.

[What do we need to do in the years ahead?]

At the same time, we're not done yet. The euro area needs a comprehensive growth strategy.

We need strong and coherent policies in all relevant policy areas. Sound monetary and fiscal policy, high-quality investments and ambitious structural reforms. And we need to connect these different policy strands.

[Monetary policy]
Let me start with the support provided by the ECB's monetary policy. Like many other central banks, including the Bank of Japan, the ECB is confronted with the zero lower bound. In response, and in the context of a weak euro area economy, it has resorted to unconventional measures. These days, monetary policy – and quantitative easing in particular – is a topic of lively debate.

One point to make is that monetary measures will only be effective in combination with sound policies in other areas. It doesn't take politicians off the hook. We want the liquidity provided by the ECB to finance productive investments in the real economy instead of creating bubbles. This means that we have to take the right structural measures as well. Restoring our banks to health, as I mentioned earlier, has been a key element of this. And going forward, we need further measures to boost attractive investment opportunities.

[Fiscal policy]
Also, besides monetary policy, we need sound fiscal policies. From the moment the crisis started, the sustainability of public finances was tackled with great urgency. We have pursued a strategy of stronger fiscal discipline and budgetary consolidation. And with an eye to our aging continent and keeping our social security system future-proof, healthy public finances remain a top priority.

In this context, our set of common budgetary rules, the so-called Stability and Growth Pact, is key. The Stability and Growth Pact is a rule-based framework for the coordination of national fiscal policies. It imposes fiscal discipline, with limits on budget deficits and debt. It functions as an anchor of confidence. Confidence among euro countries and confidence for the financial markets. And all countries – large and small – should abide by these rules.

[Investment]
The third element of our coherent policy mix is investment. Investment levels across Europe are too low and must be raised. In November, the new European Commission presented a 315 billion euro private and public investment programme, equivalent to about 45 trillion yen. This plan has three pillars. It mobilizes capital for investment through a European Fund for Strategic Investments. It brings together viable investment projects and private and public financing. And it contains measures to strengthen our investment climate. This includes better regulation, the development of a capital markets union and completion of the internal market in Europe. In particular, the digital agenda and energy grids offer opportunities for new investments.

So we need to increase investment in Europe, and most of the increase has to come from private sources. To achieve this we need to attract private investors. Companies' confidence in our growth potential will increase if we vigorously implement ambitious structural reforms, at both the European and national level.

[Structural reforms]
This brings me to the final policy strand. Structural reform is our key challenge. No stimulus can replace the need to make our economies more competitive and fit for the 21st century.
Years of strong credit-fuelled growth have masked some of our structural weaknesses.
And a number of serious challenges lie ahead of us. Such as ageing and globalisation.

Japan is facing very similar challenges. Your government's three arrow strategy reflects the fact that monetary, fiscal and structural policies should go hand in hand. The government is committed to structural reform, but is finding that this is no easy task. It's very much the same in Europe.

To address weaknesses in our European economies, we need structural reforms. Well designed, well timed. We need to improve our labour markets, lower the tax wedge on labour and further improve the skills of our workforce. We need to make our product markets more flexible, modernise our welfare system and improve the quality of our research and innovation.

That's why we need to focus on what we've already achieved and on the potential benefits that still lie ahead.

In its 'Going for Growth' report, the OECD presents the achievements of reforms in Europe over the last two years. It shows that Greece, Italy and Spain have reduced regulatory barriers to competition. Ireland and Slovakia have strengthened Research & Development and innovation incentives. Countries like France, Italy, the Netherlands and Portugal have reduced problems in their labour markets. And so I could continue. But we're not there yet. Take, for instance, the problem of protected sectors and professions. The European Commission has identified no fewer than 4,700 regulated professions in EU countries. Some of these make sense, such as medical specialists. You don't want everyone to say that he is a medical specialist. Others much less so, like golf instructors or second-hand car salesmen. So this is an issue we must continue to address. Other issues include the age of retirement and dealing with the costs of health care. In many European countries an issue of concern.

Implementing the right reforms can boost growth. The OECD has calculated that adopting best practices in labour and product markets could increase the eurozone's output by more than 6% over 10 years. In the Eurogroup we say: let's use this potential!

In Europe, but also in Japan, concerns about the fragile state of the economy are having a big impact on the discussion about structural reform. For the euro area, a number of reform measures will not only strengthen our growth potential in the longer run, but may also increase demand in the short run. It's a myth that the impact of reform is only felt in the distant future. Take, for example, measures to improve the tax system, reduce red tape and lower regulatory barriers have an immediate impact. These can spur investment

in both the short and long term. Reducing the tax wedge would also bring benefits to many euro countries. Many countries have been working on this reform, which impacts both supply and demand side.
Finally, increasing the pension age and extending the working week can immediately improve public finances, even in the short term.

[Connecting the policy strands]
My previous points underline the links between policies in different areas. A growth strategy for the eurozone requires us to connect all of these policy strands. This approach has been endorsed by the European Council, which will discuss ways of strengthening the Economic and Monetary Union in the coming months. Together with Presidents Juncker, Draghi and Tusk, we will work on improving the coordination of our economic policies.

We should put growth and jobs at the top of our priority list. We have to seize opportunities. We have to act promptly and rigorously. So our work should focus on the delivery of key reforms.

To this end, we can do more to integrate reforms and budgetary efforts. This makes sense, because the implementation of structural reforms can increase economic activity and potential growth, and have a positive impact on public finances as well. It is also a way to incentivise reform efforts.

So I advocate a more integrated assessment of compliance with our budgetary rules and the European Commission's reform recommendations. In making this assessment, we should distinguish between countries.

Some countries fall under the preventive arm of the Pact. Under the rules, these countries must stick to medium-term goals. Countries that implement key structural reforms could be given some flexibility in reaching these medium-term budgetary targets. Reform measures should be well-specified, time-bound and have a positive impact on public finances.

The story is different for countries whose deficit is higher than 3 per cent. This is what is called the corrective arm. Under the corrective arm, the rules of the Pact are more strict. While extension of the deadline for correcting an excessive deficit for those countries is already possible, this should require a reform effort as well. Countries that ask for an extension for their budgetary targets should step up their reform efforts in addition to meeting the current requirements.

[Shared goals]
Ladies and gentlemen,

Making changes in the face of new circumstances is difficult for anyone, anywhere.
It’s not easy to switch to a new approach, especially when you’ve known success in the past.

Yet it can be done. By countries, by partnerships and by companies. Let me give you one striking example: Fujifilm. This company has always illustrated Japan’s innovative and resilient spirit. And over time the company has proven its value more than ever. Because after the introduction of the digital camera – and perhaps more importantly the camera on our phones – the market for camera film collapsed. Where a company like Kodak didn't transform and went belly up, Fujifilm reinvented itself. Nowadays, Fujifilm is a giant in life sciences, even working on a vaccine against the devastating disease Ebola. Switching from making camera film to curing viral diseases: that kind of mentality should make this country proud.

Just like Fujifilm, the economies of both the eurozone and Japan have to adapt to new circumstances. We both have to implement structural reforms. We both know what needs to be done. But implementation is hard. You can plan all you want, but the moment never seems right. And it’s encouraging that monetary policy and fiscal policy can ease some of the pressure. But as soon as the pressure lets up, there is a risk of delay. This should ring alarm bells. It is crucial to push ahead. We can do so by connecting sound monetary and fiscal policy, high quality investments and ambitious structural reforms. I will work relentlessly to achieve this goal. But I think it’s always smart to learn from others. I trust Europe and Japan will continue to learn from each other. And support each other. To modernise our economies. To achieve sustainable growth. And to prepare for the future.

[Conclusion]

Ladies and gentlemen,

In Europe, the oak is considered the strongest of all the trees. Oaks are usually the last trees standing after a storm. But if the storm becomes a typhoon, even the mighty oak may fall. Japan and Europe have both withstood seemingly unstoppable storms. We did not fall. So perhaps we are not oaks. If necessary, we change our form. We move with the wind. We bend with it, leaning in a different direction, but we don’t fall. We are not the oak. We are the bamboo.

I strongly believe the best is yet to come for both parts of our world. Haruki Murakami we have to ask ourselves what really matters. You and I agree with your founder Fukuzawa that learning is one of those things. It matters a lot. But I would also like to mention another priority: the friendship between the countries of the eurozone and Japan. May that friendship support us in our common effort to renew economic growth. Thank you.