

## A Eurozone recession silver lining needs to come from Berlin

If a future recession leads to a rethink of Eurozone fiscal policy, it could hold a silver lining. On the other hand, if Germany sticks to its current adage of fiscal strictness, euro-risk could re-emerge



Will German Chancellor, Angela Merkel, be able to provide a silver lining?

### Would the next recession be so bad for the eurozone?

The R-word is haunting Europe again. The German economy might already be in it. The rest of the eurozone could follow suit: A recession. With the 2008 global financial and the subsequent euro crises still fresh on everyone's minds, the R-word sounds devastating. Then again, a technical recession (two consecutive quarters of contraction) is by no means a crisis and the question is whether the next recession would be so bad for the eurozone?

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*A technical recession is by no means a crisis*

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In the past decade, despite the euro crisis symptoms, the medicine has worked rather well for Germany. Fundamental was the eurozone not splitting apart and the German economy has, in particular, benefited from low interest rates and a weak exchange rate, the side-effects from those

break-up fears and the ECB's crisis-fighting monetary policy. Right now the tide could turn and a eurozone recession, originating in Germany, could actually benefit the rest of the eurozone.

## Eurozone needs a rethink of its fiscal policies

Why? Because the eurozone desperately needs a rethink of its fiscal policies. A very prudent stance towards fiscal spending has become mainstream in Northern Europe at a time when monetary policy has lost its punch. Fiscal policies were at the heart of the euro crisis and could again be at the centre of the next one, but in a different way. To some extent, the role of fiscal policy in the eurozone has become the famous elephant in the room. The countries which could use more growth-supportive fiscal measures don't use them and the countries which shouldn't use the measures due to high government debt levels are tempted to spend them time and again. This is an unsustainable situation in the longer run.

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*When, if not now, is the perfect time for investing in digital and traditional infrastructure projects?*

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If the current economic slowdown in Germany leads to a rethink of the role of expansionary fiscal policies and reinterpreting the "Black Zero", both the German and the eurozone economy would benefit. When, if not now, is the perfect time for investing in digital and traditional infrastructure projects given negative interest rates and high investment needs? It could lead to stimulus not designed as hastily constructed short-term oriented spending, but as a means to improve the long-term potential of the economy as well as helping to find new engines for growth at a time when the old export and automotive-driven growth model is stuttering, to say the least.

## Eurozone countries have little appetite for more austerity

The eurozone economy could benefit from a German recession if it opened doors to more anti-cyclical fiscal policies; there is also a more worrisome scenario possible. If the German government doesn't budge and it sticks to fiscal strictness and structural reforms, seeing recessions as a kind of religious healing process for structural deficiencies in an economy, the pressure increases on the ECB to step in. It would also cause 'euro risk' to increase significantly. It is hard to see many eurozone countries having a strong appetite to go through yet another round of austerity measures and structural reforms. The centrifugal forces in the eurozone would strengthen.

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*The eurozone economy could benefit from a German recession if it opened doors to more anti-cyclical fiscal policies*

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This would not only cause friction in southern or peripheral eurozone countries. Against the background of the latest aggressive attacks and controversies surrounding the ECB's latest policy measures, even looser monetary policies by the European Central Bank in reaction to fiscal inactivity would worsen the adverse effects on savers, banks, insurance companies and pensioners

in core eurozone countries. Eventually, what is now just negative rhetoric about the ECB could turn into fuel for a eurozone break-up debate in core countries.

The only way to keep the genie of yet another euro crisis in the bottle is to rethink the role of fiscal policy in the eurozone. Not in an irresponsible, unsustainable way but in the context of an economic debate on how to increase potential growth throughout Europe, and hence the level of the neutral interest rates. The current slowdown and a possible recession in Germany will only speed up the debate. The key to whether it is a recession made in heaven or hell lies in Berlin.

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