

Macroeconomics in South Europe since the Euro

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Keynote Speech

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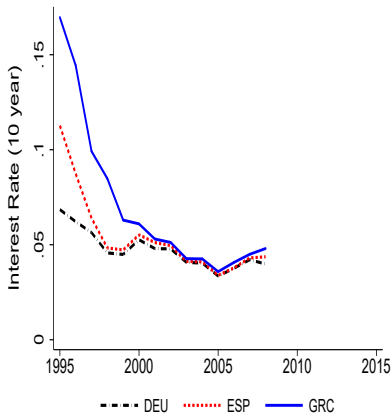
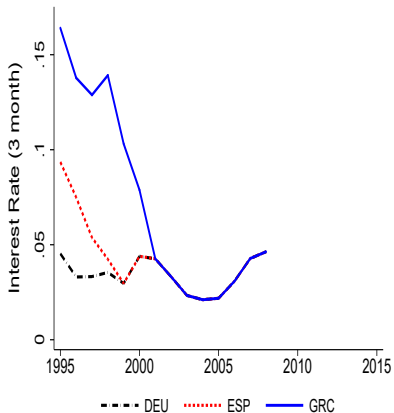
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- boom period (1990s – 2008)
- bust period (2008 – 2010s)

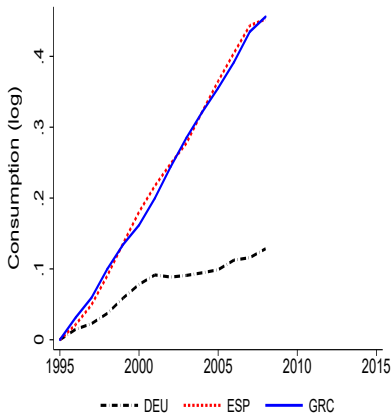
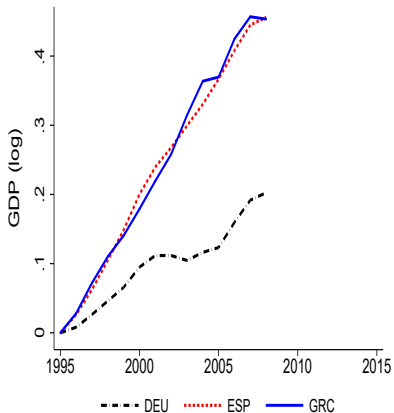
Tale of two countries: Spain and Greece.

The Boom Period (1990s – 2008)

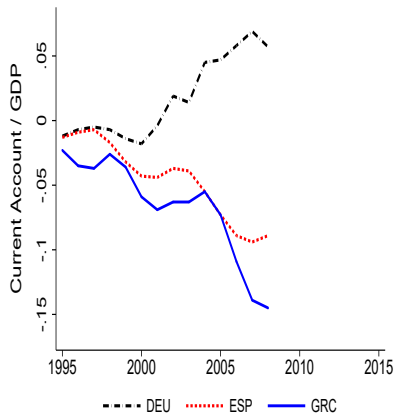
Convergence of Southern interest rates



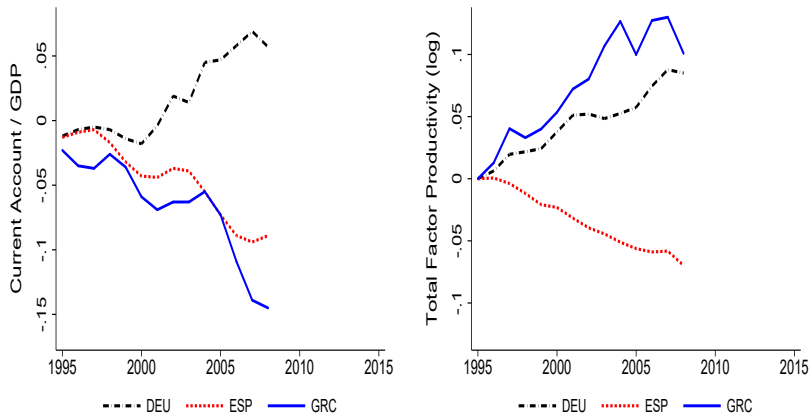
Production and consumption boom in the South



Capital flows from North to South



Capital flows from North to South



- Spain is *puzzling*: capital flowing in but TFP declining.

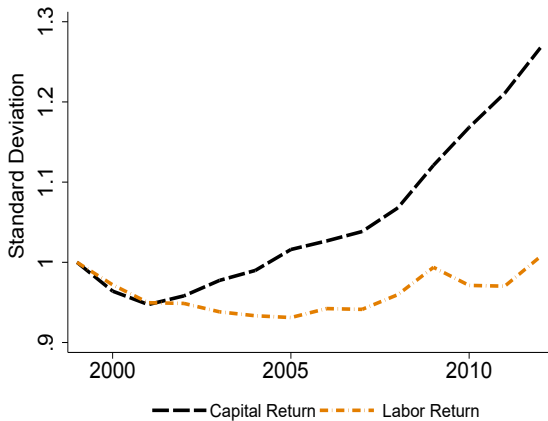
Misallocation hypothesis

- Cross-country differences in productivity (2000s research).
- Dynamics of productivity (2010s research).

Misallocation hypothesis

- Cross-country differences in productivity (2000s research).
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- Spanish version of misallocation hypothesis:
 - Lower interest rates \implies increase in desired capital.
 - Capital flows to unproductive firms because of *financial frictions*.

Increasing dispersion of capital returns in Spain



Capital flows, productivity, and dispersion: South vs North

	1999–2007 (percent)		Increasing Dispersion in 2000s?
	$\frac{\text{Current Account}}{\text{GDP}}$	Δ TFP	Return to Capital
Spain	-6	-4	✓
Italy	-1	-5	✓
Portugal	-4	-1	✓
Germany	2	7	✗
France	1	4	✗
Norway	13	1	✗

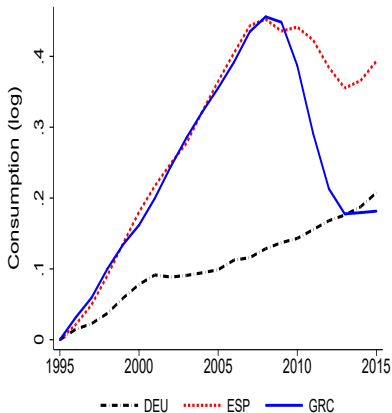
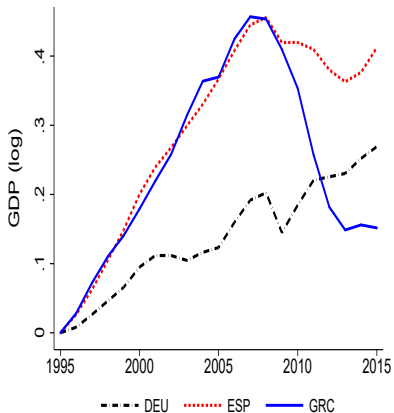
Why was Greek TFP growing?

Increased utilization of capital and labor, in response to:

- Financial liberalization and low interest rates (like Spain).
- Olympic games.
- Expansionary fiscal policy, EU transfers received and anticipated.

The Bust Period (2008 – 2010s)

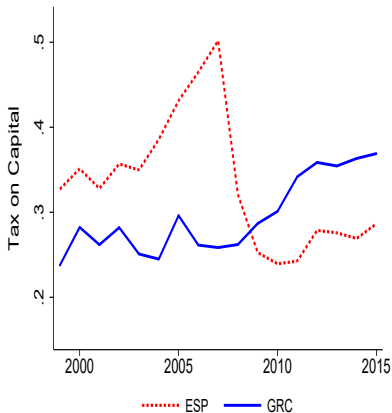
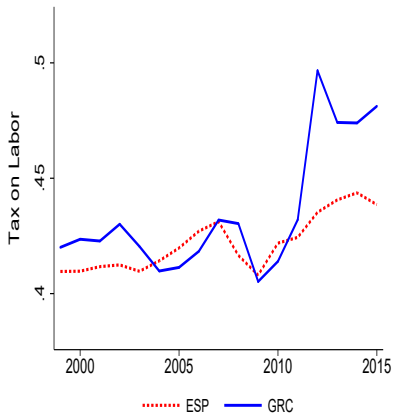
The bust in production and consumption in the South



Why was the bust so deep and persistent in Greece?

- 1 Fiscal adjustment program, especially increased *taxes*.
- 2 Other factors:
 - weak financial conditions: default, global crisis,
 - weak external demand: shipping,
 - weak domestic demand: idiosyncratic risk.

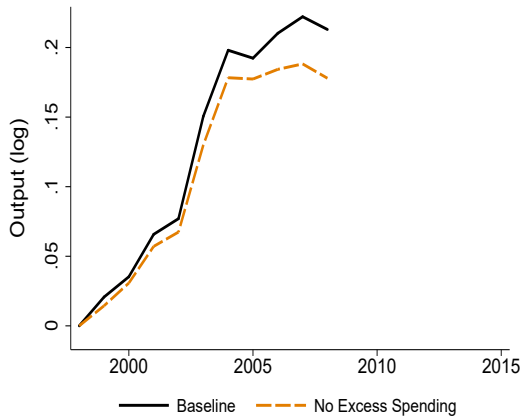
Tax rates increased more in Greece than in Spain



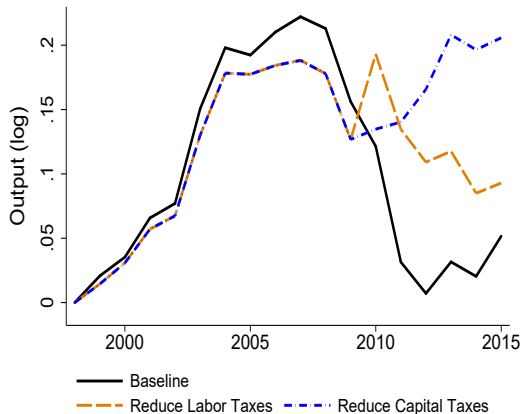
Greek fiscal adjustment

- 1 Why was there a fiscal adjustment during the bust?
 - trigger: misreporting of deficit and debt
 - cause: excessive spending in the boom
- 2 Could Greece have done better in the bust?
 - yes, by tilting adjustment towards spending instead of taxes
 - yes, by not having spent so much in the boom

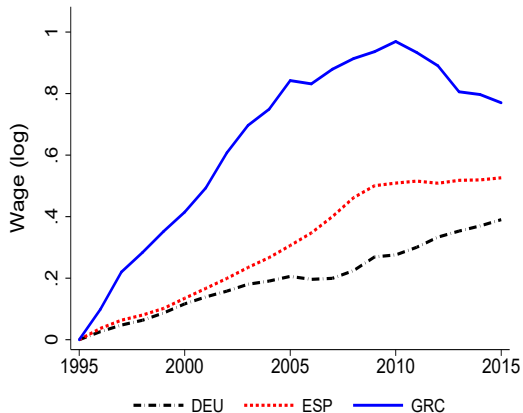
Eliminating excess Greek spending in the boom ...



... avoids painful Greek adjustment in the bust



What about a devaluation/exit of Greece?



- Greece became *more* competitive in the bust.

Policy implications for South Europe

- Financial underdevelopment linked to productivity losses.
- Excessive spending in boom brought painful adjustment in bust.
- Not obvious devaluation/exit would have helped much.

References

Gabriel Chodorow-Reich, Loukas Karabarbounis, and Rohan Kekre, “The Macroeconomics of the Greek Depression.” NBER Working Paper No. 25900, May 2019.

Gita Gopinath, Sebnem Kalemli-Ozcan, Loukas Karabarbounis, and Carolina Villegas-Sanchez, “Capital Allocation and Productivity in South Europe.” *Quarterly Journal of Economics*, 132(4), 1915-1967, November 2017.

Additional Data Sources: OECD, EU KLEMS, IMF WEO, PWT, Cara McDaniel's Tax Database.