

# Don't Write Off Europe

*The case for a comeback.*

BY KENNETH ROGOFF

**A**fter fifteen years of economic upheavals, from the European debt crisis to the Covid-19 pandemic and Russia's invasion of Ukraine, the European economy appears set to underperform in 2024. But are appearances deceiving?

Germany, Europe's largest economy, has been hit particularly hard by the surge in energy prices and China's ongoing slowdown. Moreover, Germany has exacerbated its own economic woes by diluting or abandoning many of former Chancellor Gerhard Schröder's market-oriented reforms, which had previously underpinned its robust GDP growth. Although leading German forecasters project that the country will (barely) avoid a recession in 2024, its economic outlook remains precarious.

France is faring slightly better. But with a fiscal deficit of 5.5 percent of GDP in 2023 and real interest rates rising globally, the French government is under pressure to tighten policy. On the other hand, after years of declining productivity and persistent debt issues, Italy is growing again and appears to be on a positive trajectory. And Greece, which maintains the European Union's largest underground economy, continues to struggle, primarily owing to rampant tax evasion.

Nevertheless, there are several reasons for hope. First, Central and East European economies have been outperforming Western Europe for some time now. According to Eurostat, Poland has overtaken both Greece and Portugal in terms of real GDP per capita, with countries like Romania on track to achieve similar milestones within the next five years. While Hungary has grappled with exchange-rate fluctuations and a 0.8 percent contraction in 2023, reflecting Prime Minister Viktor Orbán's attempts to curb the central bank's independence, the country is expected to return to solid growth in 2024 and 2025.

To be sure, Central and East European countries are also aging rapidly, much like their Western counterparts. Still, for now, the fast-growing East will continue to pull up Europe's overall growth rate. While American observers often take these countries' progress for granted, the European Union's ability to help new member states overcome legacy institutional issues and corruption should not be underestimated.

Second, Southern Europe is also growing faster than Northern Europe, with Spain, Portugal, and even Greece outstripping German growth by a wide margin since 2020. This is partly catch-up from dismal growth in the years following the global financial crisis; but, given these economies' robust tourism industries and lower dependence on manufacturing, it could continue.

Third, it would be unwise to bet against a long-term resurgence of the German economy. When I was a graduate student in

the late 1970s, one of my classmates presented a paper showing how East Germany had outperformed other Soviet bloc economies. "They have yet to invent a system where the German economy is inefficient," he quipped. Although Germany's recent leftward turn may end up proving this argument wrong, it is more likely that the country will manage to correct course and return to building high-quality infrastructure.

Fourth, upcoming elections across Europe could usher in some much-needed effective leadership. French President Emmanuel Macron, once viewed as the successor to former German Chancellor Angela Merkel as Europe's most respected leader, has struggled to address his country's numerous economic challenges and has been criticized for his naivete in dealing with Russian President Vladimir Putin. And Merkel's actual successor as German chancellor, Olaf Scholz, is grappling with dismal approval ratings that make U.S. President Joe Biden seem popular by

comparison. With Germany's 2025 federal elections looming on the horizon, there is a real possibility that Scholz will be replaced.

Despite stabilizing the United Kingdom, Prime Minister Rishi Sunak is hindered by the widespread perception that he is a lame duck. Sunak's Conservative Party is currently trailing far behind in the polls against a revitalized Labour Party, which has successfully positioned itself as economically centrist. By contrast, Italian Prime Minister Giorgia Meloni has unexpectedly emerged as one of Europe's most effective and popular leaders.

Lastly, the looming threat of a Russian victory in Ukraine could catalyze Europe's fiscal integration—an unthinkable prospect not so long ago. Meanwhile, as I recently argued, November's U.S. presidential election is unlikely to mitigate America's ongoing political turmoil, regardless of the outcome.

All of this suggests that Europe could still turn its situation around. European stock markets could easily replicate last year's unexpectedly strong performance, considering that valuations, as measured by price-to-earnings ratios, are significantly lower than those in the United States. Although the U.S. stock market has outperformed Europe's for years, 2024 could be different.

While European economies have underperformed for a long time, no trend lasts forever. As grim as Europe's outlook seems right now, its economic prospects could look a little better later this year. ♦

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